

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 26, 2023

Volume 16 Issue 205

Market Overview



Signals Overview

Aggregator	CBI Reading
Long	5

Tonight's Research Points

- A discussion on what it would take to see a VIX spike.

Short-term Outlook

The Bottom Line

The Aggregator is bullish. But evidence is light and the market is getting volatile. Reward/risk is favorable for the bulls, but not greatly.

Summary of Current Active Studies (see Letters from listed dates for details)

Study Date	Description	Time span	Bias	Avg Run-up	Avg DrawDn	Avg DrawDn - 1 Std Dev
Active - Short Term						
October 24, 2023	5 down days & close < 200ma	1-8 days	Bullish	4.30%	-2.05%	-4.85%
Active - Long Term						
October 23, 2023	NASDAQ Lagging	int term	Neutral			
October 2, 2023	SPX down 4 weeks but above 40-week ma	1-10 weeks	Bullish			
May 22, 2023	SPX 50-day high < 1/2 SPX stocks > 50ma	1-12 months	Neutral			
February 2, 2023	SPX Golden Cross	int term	Bullish			
January 13, 2023	Whaley ADT5 > 73.66	1-12 months	Bullish			
March 14, 2022	Fed Hawkish / QE done	int term	Bearish			
Dropped Tonight (expired, tgt hit, or avg ddn + 1 std dev exceeded)						
October 24, 2023	5 down days. Turn Tues tomorrow	1-2 days	Bullish			

The Evidence

So Wednesday was a rough one. The SPX dropped 1.4%, the NASDAQ fell 2.4%, and the Russell 2000 lost 1.7%. Breadth was weak with the NYSE Up Issues % coming in at 24% and the Up Volume % at 28%. NYSE total volume rose some from Tuesday's level.

We have a new low once again for SPX. QQQ, which up until Wednesday had managed to avoid closing below its September lows, broke down to the lowest level since early June. Meanwhile, the Russell 2000 is less than 1% from breaking below its 2022 lows. It is already below its peak from August of 2018. So if you bought the Russell in August 2018 and are still holding it 5+ years later, you're underwater.

Meanwhile, the VIX is still just a hair over 20. This has many people wondering what it will take to get the VIX to really spike – like into the 30s. I'll tell you what it will take. It will take some days that are substantially worse than we have seen so far. Today's 1.4% decline was the worst drop for SPX since September.

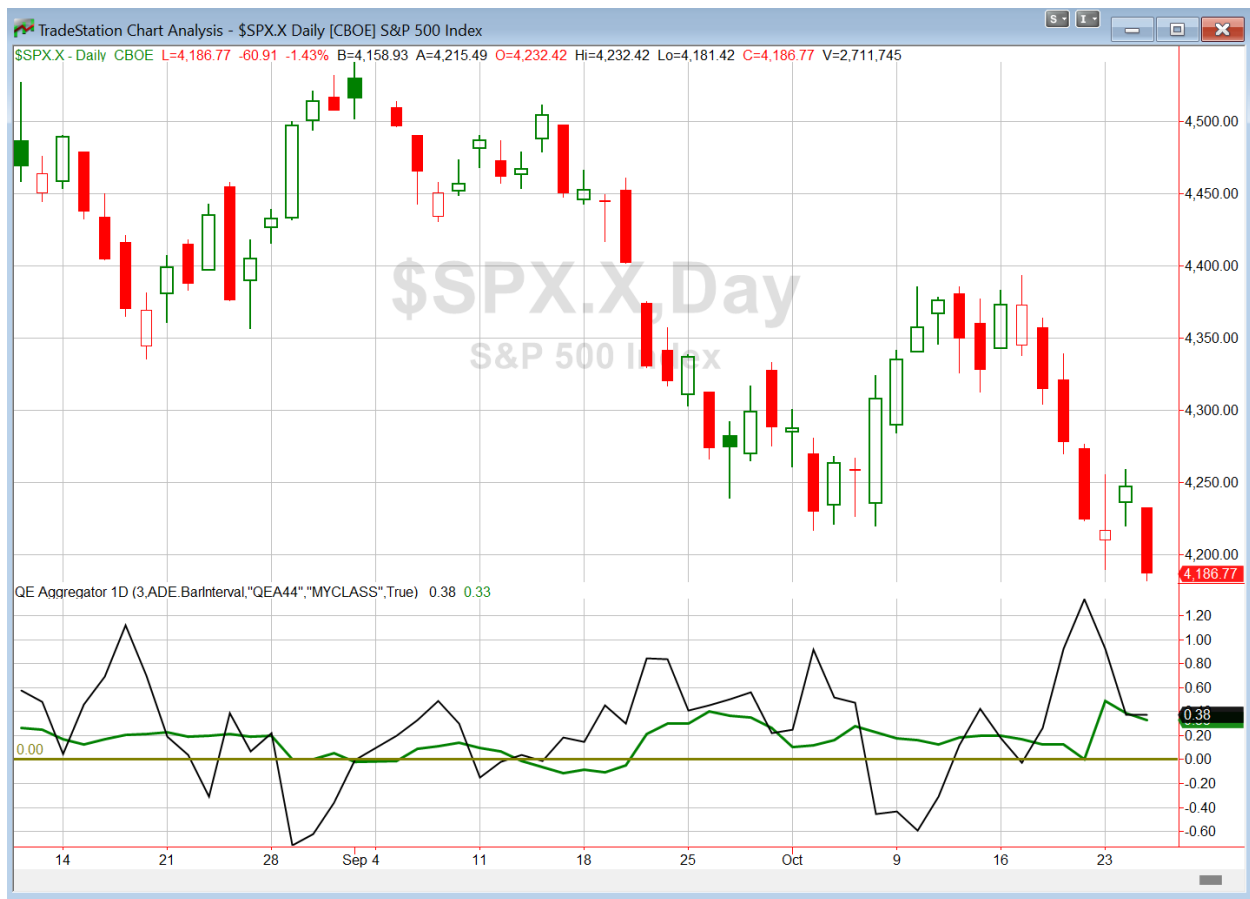
Let's recall what the VIX measures. It estimates implied volatility in SPX options over the next 30 days. A VIX of 16 implies options traders are baking in an average daily volatility of about 1%. A VIX of 32 would imply 2% daily moves over the next 30 days. We have not seen the market close down (or up) by 2% since February. So it would be very difficult to charge option buyers nearly 2% implied volatility when there has not been a 2% daily move in a very long time. The VIX spike will come if realized volatility expands. And such an expansion would be quite uncomfortable.

Another way to look at it is to compare current realized volatility to implied. For realized, I often use the 21-day historical volatility number. Twenty-one trading days is about 30 calendar days, so in this case you are measuring backwards about the same amount of time you are implying forwards. You could use a shorter-term historical volatility number, like a 10-day, since VIX spikes can happen quite quickly. But it does not matter greatly.

As of Wednesday's close, the 21-day HV for SPX closed at 12.76. The VIX closed at 20.19. That is a spread of 7.43. Now the VIX will typically trade above the 21-day HV number. So to give you some idea, I looked back over the last year. And the 7.43 spread put Wednesday in the 93rd percentile. In other words, the spread is larger than has been seen 93% of the time over the last year. So by this measure, the VIX is already quite high. Unless historical volatility rises, we are likely to see the ratio revert and the VIX come down a bit.

What would make volatility rise at this point? Panic selling is the most likely answer. Not seeing that yet. We don't have a lot of short-term evidence to go on – really just one bullish study on the short-term active list at this point. So a panic selloff is possible, but I would not say it is probable. I wish I had some very compelling short-term evidence to discuss tonight that would give us a better clue. But based on what we have seen, and the one study that is active, the market appears overdue for a decent bounce. Things are bad. They could get worse. But betting on things to get worse at this point would seem dangerous.

I have updated [the Aggregator chart](#) below.



Without any new evidence making the cut tonight, the green Aggregator Line held above zero. Positive readings mean net expectations are for upside for the next few days. Meanwhile the black Differential Line remained above zero. The positive Differential Line reading means that SPX is oversold versus recent expectations. So expectations are positive and SPX is oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above zero. Therefore, the Aggregator formation stayed long at the close.

Based on the current active studies, expectations are set to remain positive on Thursday. This could change if compelling new bearish evidence emerges. Meanwhile, the Differential Pivot will be 4241.97 on Thursday. That is 1.3% above Wednesday's close. So SPX will need to close up over 1.3% on Thursday if it is to flip from oversold to overbought versus recent expectations.

So the Aggregator is bullish. Risks appear somewhat elevated with volatility increasing. But there has been a lot of selling recently and this market is about due for a bounce. We could certainly see a strong one if traders decide they want to front-run the Fed announcement next Wednesday. In any case, while risks are above normal, reward/risk still appears favorable for the bulls. I have a small long index position. I will maintain that for now. I won't look to add to it unless I see some compelling new bullish evidence emerge in the coming days.

Intermediate-term Outlook (2 weeks – 2 months) – updated 10/23– neutral

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

TXN – 1/3 @ \$146.32 (bought @ limit)

LOW – 1/3 @ \$186.24 (bought @ limit)

New

LOW – 1/3 @ \$186.09 (buy @ limit)

HD – 1/3 @ \$280.93 (buy @ limit)

TMO – 1/3 @ \$433.18 (buy @ limit)

Broad Market Large Cap CBI – 5(TXN, LOW-2, HD, TMO)

Additional New Trade Ideas

A full listing of system triggers can be found at the [numbered systems page](#) each night. I will cherry pick some of my favorite setups from the S&P 100 and ETF lists along with occasional other trade ideas to track below.

LOW – Buy 1/3 Catapult position @ \$186.09 LIMIT. From the Catapult section above, this is the 2nd of up to 3 possible lots of LOW.

HD – Buy 1/3 Catapult position @ \$280.93 LIMIT. From the Catapult section above, this is the 1st of up to 3 possible lots of HD.

TMO – Buy 1/3 Catapult position @ \$433.18 LIMIT. From the Catapult section above, this is the 1st of up to 3 possible lots of TMO.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Notes
SPY(1/4)	10/20/2023	\$421.19	\$417.55	-0.86%	Aggregator
TXN(1/3)	10/24/2023	\$146.32	\$141.79	-3.10%	Catapult
LOW(1/3)	10/25/2023	\$185.55	\$186.09	0.29%	Catapult

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