

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 21, 2010

Volume 3 Issue 138

## Market Overview



## Tonight's Research Points

- Mega-outside days with the open & close beyond the previous day's low & high have often led to a short-term pullback on the past.
- The Aggregator System remained flat.
- The NDX Aggressive Trend Timer remained flat.

## Short-term Outlook

### The Bottom Line

Tuesday's big reversal bar appears to have negative inclinations – but only for a day or two. The Aggregator is on a crash course with a short set up tomorrow barring strongly bullish evidence or a large down day.

*Summary of Recent Active Studies (see <http://QuantifiableEdges.blogspot.com> or Letters from listed dates for details)*

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
July 21, 2010	Open/close beyond yest hi/low	1-2 days	Bearish	
July 20, 2010	1.75% drop then bounce less than 25%	1-3 days	Bearish	-2.20%
July 20, 2010	2% drop. Then Up Issue%>60, dn vol	1-6 days	Bearish	-5.50%
July 19, 2010	7 day high close to a 7 day low close	1-4 days	Bearish	-2.50%
July 19, 2010	Unfilled gap -n- crap	1-3 days	Bearish	-3.20%
July 16, 2010	SPX Up VIX Up	1-4 days	Bearish	-3.10%
July 14, 2010	Follow Through Day	1-6 days	Bullish	
July 14, 2010	75% Up Issue twice in 3 days	1-9 days	Bullish	3.30%
<b>Active - Long Term</b>				
July 14, 2010	75% Up Issue twice in 3 days	1-20 days	Bullish	
July 13, 2010	5 higher close from a 50-day low	int term	Bullish	
July 7, 2010	McClellan Oscillator Bottom Divergence	int term	Bullish	
July 5, 2010	5 down under 200 and 50 low	1-20 days	Bullish	

If the avg max move is achieved the study will appear in ***bold italic blue*** and no longer be active

### ***The Evidence***

Tuesday saw a very difficult start lead to a very strong finish. After gapping down over 1.25%, the SPX closed up over 1.1%. The Nasdaq also gained 1.1% while the Russell 2000 added on a very strong 1.8% for the day. Breadth was strongly positive as the NYSE Up Issues % came in at 80% and the Up Volume % was 83%. Total volume rose from Monday's level and was just above average.

A couple of days ago in the intermediate-term outlook I suggested that a bullish sign for the intermediate-term would be to see the short-term negatives ignored for a few days. That is what has happened as the bulls have managed to overcome difficult starts and finish the day strong the last 2 days. We are now 5 day from the 7/13 follow through day and the market is still lower. That typically suggests about a 2/3 chance of the rally failing. Still, I'm encouraged by the last two days from an intermediate-term standpoint, and there remain substantial intermediate-term bullish studies still active.

From a short-term perspective the Quantifinder was loaded tonight with studies that looked at big gaps down that reversed and finished positive. Below is one from the 8/20/2009 Subscriber Letter that is representative of what the studies are suggesting.

SPY opens below yesterday's low and closes above yesterday's high. Buy on close. Sell X days later. \$100k/trade. 1993 - present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	661.31	26	13	13	50.00	2,060.96	-2,010.09	1.03	1.03	25.44
4	-13,400.90	26	11	15	42.31	2,090.02	-2,426.08	0.86	0.63	-515.42
3	-14,630.72	26	11	15	42.31	1,598.35	-2,147.51	0.74	0.55	-562.72
2	-14,209.25	26	10	16	38.46	872.42	-1,433.34	0.61	0.38	-546.51
1	-8,660.79	26	9	16	34.62	510.70	-828.57	0.62	0.35	-333.11

**23 of 26 instances (88.5%) posted a close below the entry price at some point in the next 3 days.**

There seems to be a bit of a downside edge over the next few days.

In the 9/15/09 Subscriber Letter I showed another study that looked at gaps down and strong finishes. One of the filters in that study that proved compelling was to require the

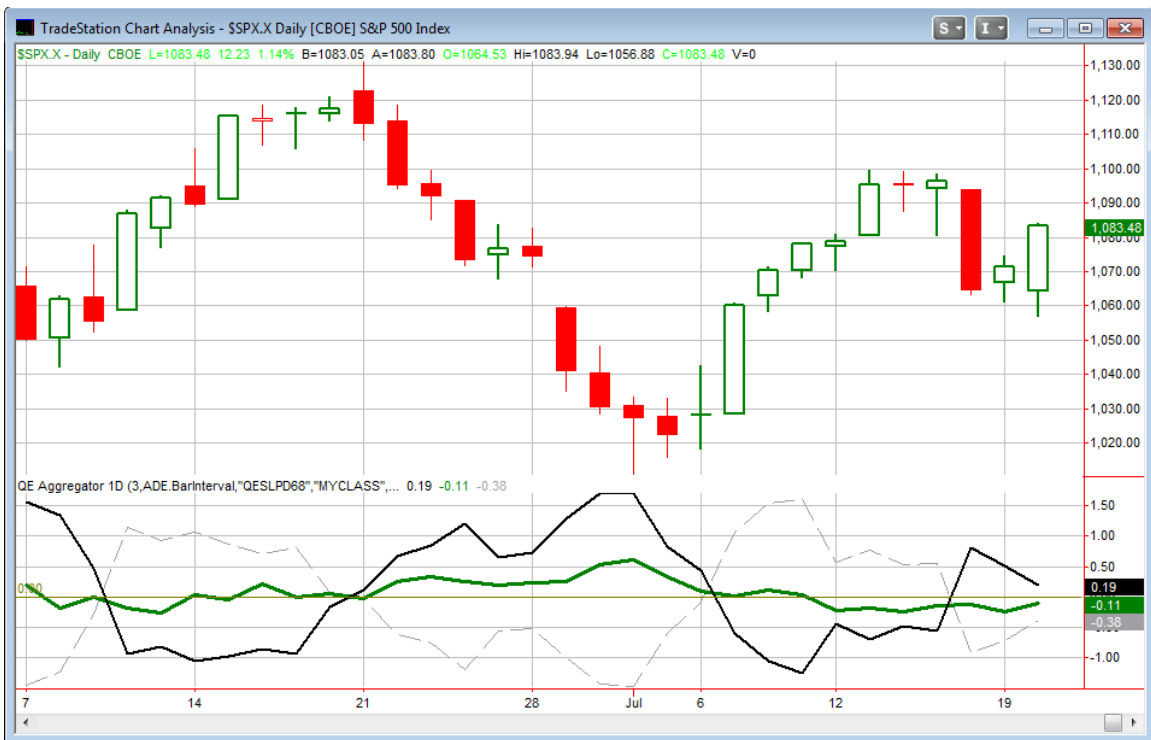
SPY to close in the top 10% of its daily range. Rather than re-running that study I thought it would be interesting to see how adding the “Top 10%” stipulation might affect the outside day study posted above.

**SPY opens below yesterday's low and closes above yesterday's high. Close in top 10% of daily range. Buy on close. Sell X days later. \$100k/trade. 1993 - present.**

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	4,572.07	19	11	8	57.89	2,026.66	-2,215.15	0.91	1.26	240.64
4	-3,363.40	19	10	9	52.63	1,979.03	-2,572.63	0.77	0.85	-177.02
3	-6,600.08	19	10	9	52.63	1,458.19	-2,353.55	0.62	0.69	-347.37
2	-11,876.21	19	8	11	42.11	649.48	-1,552.00	0.42	0.30	-625.06
1	-9,454.14	19	5	13	26.32	260.71	-827.52	0.32	0.12	-497.59

Stats here are even more compelling over the 1<sup>st</sup> couple of days.

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



Once again the green Aggregator line remains below zero. The negative Aggregator line value indicates the net expectation from the Active Studies over the next few days is for downside. Meanwhile the black Differential line shows the SPX has still mildly underperformed expectations over the last few days. So we have negative expectations but a market that is oversold versus recent expectations. This is considered a neutral configuration. Based on this the Aggregator System remained flat at the close.

Based on the current studies the green Aggregator line is set up to remain negative tomorrow. Of course strong bullish evidence could change this. Meanwhile, with Fridays drop exiting the back end of the equation, the Differential pivot will drop to 1058.86 tomorrow. This means it would take an SPX close at or below this level in order for the black Differential line to remain positive. That would be almost a 2.5% drop.

So it appears the chance of the Aggregator triggering a short signal at the close on Wednesday is pretty good. Unless there is a strong drop or extremely bullish evidence it should happen. I'm not terribly gung-ho about this signal potential signal just yet. My intermediate-term bias is to the bullish side and we really only had one day of selling in the last 11. And 9 of the last 10 have closed in the upper portion of their range. Bulls have been in control so I feel as though I am dealing with a possible counter-trend trade on the short-side here even though the market is below the 200ma and has yet to break its series of lower highs. Therefore, I will look to take it slow in the trade ideas section and may even stop adding at 2 or 3 lots rather than the full 4.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 7/12 – skittishly and mildly bullish. I will switch to neutral or bearish if the market fails to bounce substantially by Tuesday.***

From an intermediate-term standpoint, quite a bit of bullish evidence has emerged over the last couple of weeks. I thought I'd go through it chronologically and then point out one study I'll have my eye on this upcoming week.

When the recent selloff was hitting its low point on July 2<sup>nd</sup> this study appeared:

SPX closes lower for at least the 5th day in a row. It also closes under the 200ma and at a 50-day low. At least one of these conditions was not present yesterday.  
Buy on close. Sell X days later. \$100k/trade. 1973 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	91,528.80	37	27	10	72.97	5,049.51	-4,480.79	1.13	3.04	2,473.75
15	63,238.82	39	26	13	66.67	4,323.45	-3,782.38	1.14	2.29	1,621.51
10	60,591.83	44	27	17	61.36	3,972.62	-2,745.23	1.45	2.30	1,377.09
9	64,150.62	44	29	15	65.91	3,478.94	-2,449.25	1.42	2.75	1,457.97
8	60,167.73	44	31	13	70.45	3,051.09	-2,647.39	1.15	2.75	1,367.45
7	44,164.57	45	29	16	64.44	3,004.24	-2,684.90	1.12	2.03	981.43
6	42,243.37	45	29	16	64.44	2,942.74	-2,693.50	1.09	1.98	938.74
5	49,443.79	45	30	15	66.67	2,614.11	-1,931.98	1.35	2.71	1,098.75
4	47,213.33	45	30	15	66.67	2,357.50	-1,567.45	1.50	3.01	1,049.19
3	25,860.93	45	24	20	53.33	2,434.03	-1,627.79	1.50	1.79	574.69
2	20,387.96	45	28	17	62.22	1,658.49	-1,532.33	1.08	1.78	453.07
1	21,089.93	45	28	17	62.22	1,306.29	-910.95	1.43	2.36	468.67

89% of instances closed higher than the entry price at some point in the next week.

It didn't disappoint and a bounce followed starting the very next day (7/5). When that bounce occurred it triggered this study which examined the large divergence we were seeing in the McClellan Oscillator:

Yesterday the market closed at a 100-day low. Today it closes higher. The lowest Ratio Adjusted McClellan Oscillator reading of the last 10 days is above the lowest McClellan Oscillator reading of the last 100 days by at least 65 points.  
Buy on Close. Sell X days later. \$100k/trade. 1950 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	52,869.75	13	10	3	76.92	7,525.55	-7,461.91	1.01	3.36	4,066.90
15	32,111.38	13	9	4	69.23	5,926.91	-5,307.71	1.12	2.51	2,470.11
10	33,039.92	13	10	3	76.92	4,920.18	-5,387.31	0.91	3.04	2,541.53
9	31,321.94	13	9	4	69.23	4,997.56	-3,414.03	1.46	3.29	2,409.38
8	32,694.56	13	9	4	69.23	4,528.81	-2,016.17	2.25	5.05	2,514.97
7	39,314.58	13	10	3	76.92	4,908.61	-3,257.18	1.51	5.02	3,024.20
6	41,973.34	13	11	2	84.62	4,121.01	-1,678.90	2.45	13.50	3,228.72
5	45,547.00	13	11	2	84.62	4,269.94	-711.17	6.00	33.02	3,503.62
4	33,448.07	14	11	3	78.57	3,159.71	-436.25	7.24	26.56	2,389.15
3	29,916.22	16	12	4	75.00	3,004.27	-1,533.76	1.96	5.88	1,869.76
2	23,808.79	16	13	3	81.25	2,307.51	-2,062.94	1.12	4.85	1,488.05
1	14,960.73	16	12	4	75.00	1,585.47	-1,016.23	1.56	4.68	935.05

On schedule we saw a strong move higher follow this study triggering as well. While much of the positive influence from this study appears in the 1<sup>st</sup> week, even 4 weeks out the implications are strongly bullish, and some more details shown in the 7/5 Letter indicated that a decent chance of a new high was suggested by this setup as well.

The July 13<sup>th</sup> Subscriber Letter carried this intermediate-term bullish study.

After closing at a 50-day low, SPX then makes 5 consecutive higher closes. Close < 200ma.  
Buy on close. Sell X days later. \$100k/trade. 1960 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
25	40,237.44	15	13	2	86.67	3,182.67	-568.65	5.60	36.38	2,682.50
24	40,003.67	15	14	1	93.33	2,906.91	-693.00	4.19	58.73	2,666.91
23	40,708.96	15	14	1	93.33	2,994.76	-1,217.70	2.46	34.43	2,713.93
20	25,307.77	15	11	4	73.33	2,838.72	-1,479.53	1.92	5.28	1,687.18
15	13,182.85	15	9	6	60.00	1,861.74	-595.47	3.13	4.69	878.86
10	-8,214.63	16	8	8	50.00	1,586.21	-2,613.04	0.61	0.61	-513.41
9	-12,770.97	16	8	8	50.00	1,419.53	-3,015.90	0.47	0.47	-798.19
8	-9,938.99	16	8	8	50.00	1,491.82	-2,734.19	0.55	0.55	-621.19
7	-10,049.38	16	8	8	50.00	1,544.51	-2,800.68	0.55	0.55	-628.09
6	-5,040.99	16	10	6	62.50	1,362.69	-3,111.31	0.44	0.73	-315.06
5	-5,504.10	16	9	7	56.25	1,407.27	-2,595.64	0.54	0.70	-344.01
4	-3,483.45	16	9	7	56.25	1,381.05	-2,273.27	0.61	0.78	-217.72
3	2,543.29	16	12	4	75.00	1,024.13	-2,436.56	0.42	1.26	158.96
2	-5,275.58	16	9	7	56.25	967.67	-1,997.80	0.48	0.62	-329.72
1	-5,604.17	16	11	5	68.75	573.68	-2,382.94	0.24	0.53	-350.26

Here we see a questionable short-term has consistently been followed by substantial upside over the next 4-5 weeks.

Then with the strong IBD Follow Through Day occurring on July 13<sup>th</sup>, these two additional intermediate-term studies appeared in the July 14<sup>th</sup> Letter:

NYSE Up Issues % > 75% in 2 of the last 3 days and makes a 10-day intraday high.  
Buy SPx on close. Sell X days later. \$100k/trade. 1970 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	107,484.86	36	27	9	75.00	5,166.10	-3,555.54	1.45	4.36	2,985.69
15	92,949.90	37	27	10	72.97	4,246.02	-2,169.27	1.96	5.28	2,512.16
10	71,424.42	39	30	9	76.92	3,341.47	-3,202.19	1.04	3.48	1,831.40
9	71,150.64	39	28	11	71.79	3,481.40	-2,393.52	1.45	3.70	1,824.38
8	59,700.36	39	29	10	74.36	2,916.50	-2,487.81	1.17	3.40	1,530.78
7	54,559.48	39	28	11	71.79	2,891.16	-2,399.37	1.20	3.07	1,398.96
6	47,615.27	40	30	10	75.00	2,408.70	-2,464.58	0.98	2.93	1,190.38
5	41,881.89	41	29	12	70.73	2,156.61	-1,721.65	1.25	3.03	1,021.51
4	33,006.29	43	26	17	60.47	2,019.98	-1,147.83	1.76	2.69	767.59
3	27,801.06	44	28	16	63.64	1,729.99	-1,289.92	1.34	2.35	631.84
2	15,797.54	50	31	19	62.00	1,219.09	-1,157.60	1.05	1.72	315.95
1	11,269.24	54	32	20	59.26	773.69	-674.45	1.15	1.84	208.69

**93% of instances closed above the entry price at some point in the next week. In two weeks it was 98%.**

Buy on the close of a Follow Through Day. Sell X days later. \$100k/trade. 1970 - present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
8	35,567.30	73	38	35	52.05	3,406.58	-2,682.36	1.27	1.38	487.22
7	34,283.01	73	41	32	56.16	3,056.14	-2,844.33	1.07	1.38	469.63
6	46,811.91	73	47	26	64.38	2,666.59	-3,019.91	0.88	1.60	641.26
5	40,182.62	73	45	28	61.64	2,506.49	-2,593.19	0.97	1.55	550.45
4	36,401.40	73	41	32	56.16	2,513.19	-2,082.49	1.21	1.55	498.65
3	33,353.47	73	41	32	56.16	2,270.76	-1,867.12	1.22	1.56	456.90
2	23,883.71	73	41	32	56.16	1,905.90	-1,695.57	1.12	1.44	327.17
1	23,336.56	73	39	34	53.42	1,166.68	-651.89	1.79	2.05	319.68

One study I'll be keeping an eye on over the next couple of days is [this one that looks at short-term implications of action just after a FTD](#). It suggests that if the market does not continue higher in the week after a FTD, then there is about a 2/3 chance of failure. On the other hand, a market that closes higher 5 days after a FTD stands about a 2/3 chance of a successful rally. So far it is not looking too promising.

So the short-term is suggesting more selling and the intermediate-term is providing a good amount of bullish evidence. But we also see a study that says the intermediate-term may be dependent on the short-term. It appears if a bounce fails to materialize shortly then the intermediate-term outlook could be in danger. The short-term outlook is for downside, but if the market ignores the current short-term tendencies and powers higher then that should bode well for the intermediate-term as well. In any case, it should be an interesting week with action that will be well worth watching and considering.

### **Catapult and Capitulative Breadth Statistics**

[Catapult & CBI Presentation Link](#)

#### ***Open Catapult Triggers***

*none*

#### ***Catapult for ETF's Trades***

*none*

#### ***Broad Market Large Cap CBI – 0***

### **Additional New Trade Ideas**

*A full listing of system triggers can be found at the [system triggers 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.*

*SPY – short ¼ index position @ \$108.50 LIMIT ON CLOSE. I'll be looking to short a higher close in the SPY tomorrow. If SPY closes down I'll evaluate overnight and likely look for an entry the next morning.*

### **Current Open Trade Ideas**

None.

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