

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

---

August 10, 2010

Volume 3 Issue 152

---

## **Market Overview**



## **Tonight's Research Points**

- SPX making its highest close in 20 days on the lowest NYSE volume in 20 days has ordinarily been followed by a pullback over the next few days.
- The SPX and VIX closing higher on the same day has historically suggested short-term bearish implications.
- Fed Days have historically had a bullish tilt, though it has been less bullish over the last 17 years when SPY has had a strong close the day before.
- The Aggregator System turned flat.
- The NDX Aggressive Trend Timer remained flat.

## ***Short-term Outlook***

### ***The Bottom Line***

The rising VIX and the extremely low volume on Monday combined with the strong close appear to be trumping the fact that tomorrow is a Fed Day. The long Aggregator signal only lasted a day and the outlook over the next few days is now hazy. I'll be looking to reduce exposure ahead of tomorrow's meeting.

*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>				
August 10, 2010	VIX Up SPX Up on Monday	1 day	Bearish	
August 10, 2010	SPX 20-day high, NYSE vol 20-day low	1-2 days	Bearish	-1.20%
August 10, 2010	Close in top 25% of range before Fed Day	1 day	Bullish	
August 9, 2010	2 Unfilled Down Gaps	1-5 days	Bullish	2.46%
August 5, 2010	SPX 10-high on NYSE 10 low vol	1-5 days	Bearish	-2.10%
<b>Active - Long Term</b>				
August 3, 2010	50 high 90% volume	1-25 days	Bullish	
July 20, 2010	Down 1 week after FTD	int term	Bearish	
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	
<b>Dropped Tonight</b>				
August 9, 2010	VIX:VXV < 0.85		Bearish	
August 3, 2010	50-day breakout on lower vol	1-5 days	Bullish	1.80%

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

**The Evidence**

The bullish tendencies played out today as the market rose on quiet trading. The SPX gained 0.55% while the Nasdaq closed up 0.75% and the Russell 2000 rose 1.4%. Breadth was squarely positive as both the NYSE Up Issues % and the Up Volume % came in at 71%. Volume was extremely light as the NYSE volume came in at what appears to be the lowest level of the year according to my data provider.

Several studies appeared tonight that examined the low volume / high price combination we saw today. Below is one was that was last updated in the August 14, 2009 blog.

SPX makes highest close in 20 days on lowest NYSE volume in 20 days. Buy on close. Sell X days later. \$100k/trade. 1978 - 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	-24,983.24	50	21	29	42.00	994.74	-1,581.82	0.63	0.46	-499.66
4	-25,013.20	51	19	32	37.25	902.09	-1,317.28	0.68	0.41	-490.45
3	-20,116.10	51	19	32	37.25	720.77	-1,056.58	0.68	0.41	-394.43
2	-21,594.47	53	25	28	47.17	523.65	-1,238.78	0.42	0.38	-407.44
1	-14,744.66	56	23	33	41.07	316.69	-667.53	0.47	0.33	-263.30

**89% of instances closed below the entry price at some point in the next week.**

This suggests the market is likely to pull back in the next few days. The size of the pullback hasn't been tremendous but the consistency has been impressive.

I did find that the edge has strengthened a bit in the last several years, especially over the 1<sup>st</sup> 1-4 days. Below is the same test run back to 1997.

SPX makes highest close in 20 days on lowest NYSE volume in 20 days. Buy on close. Sell X days later. \$100k/trade. 1997 - 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	-10,216.00	24	8	16	33.33	1,298.16	-1,287.58	1.01	0.50	-425.67
4	-12,758.02	25	7	18	28.00	1,032.57	-1,110.33	0.93	0.36	-510.32
3	-12,376.55	25	9	16	36.00	819.51	-1,234.51	0.66	0.37	-495.06
2	-15,511.27	27	11	16	40.74	512.18	-1,321.58	0.39	0.27	-574.49
1	-9,650.54	29	11	18	37.93	239.39	-682.44	0.35	0.21	-332.78

**88% of instances closed below the entry price at some point in the next 4 days.**

Also notable on Monday was that the VIX ended higher along with the SPX. It's a bit unusual for the SPX and the VIX to close in the same direction. Historically, when they both close higher there has been some giveback from the S&P over the next few days. One quirk with the VIX though is that it has a tendency to fall on Fridays and rise on Mondays. Therefore this setup is more common on Mondays than any other day of the week. I discussed this and broke out the results based on Mondays, Fridays, and mid-week occurrences in the 8/3/09 Letter. I updated the Monday results in the 10/20/09 Subscriber Letter. Below I have updated them again.

SPX and VIX both close up on a Monday. Buy on close. Sell X days later. \$100k/trade. 1998 - 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	-46,323.66	112	52	60	46.43	1,757.98	-2,295.64	0.77	0.66	-413.60
4	-39,527.21	115	51	64	44.35	1,577.33	-1,874.55	0.84	0.67	-343.71
3	-42,301.85	115	51	64	44.35	1,223.81	-1,636.19	0.75	0.60	-367.84
2	-35,553.48	115	49	66	42.61	963.18	-1,253.78	0.77	0.57	-309.16
1	-30,965.89	115	45	70	39.13	702.75	-894.14	0.79	0.51	-269.27

As you can see there has been a bit of a downside edge. I thought tonight it might be worthwhile to break down this data by uptrends vs. downtrends as I often do. First let's look at times like now when the SPX is trading above its 200ma.

SPX and VIX both close up on a Monday. SPX > 200ma. Buy on close. Sell X days later. \$100k/trade. 1998 - 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	-990.36	84	43	41	51.19	1,467.03	-1,562.75	0.94	0.98	-11.79
4	-8,592.46	86	41	45	47.67	1,263.13	-1,341.79	0.94	0.86	-99.91
3	-13,369.24	86	40	46	46.51	1,023.53	-1,180.66	0.87	0.75	-155.46
2	-16,395.46	86	37	49	43.02	749.91	-900.86	0.83	0.63	-190.64
1	-19,875.11	86	33	53	38.37	483.62	-676.12	0.72	0.45	-231.11

The uptrend does not eliminate the upside edge. It does appear to shorten it though as the edge primarily exerts itself on day 1.

Now let's examine instances that occurred during a downtrend.

SPX and VIX both close up on a Monday. SPX < 200ma. Buy on close. Sell X days later. \$100k/trade. 1998 - 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	-45,333.30	28	9	19	32.14	3,148.08	-3,877.16	0.81	0.38	-1,619.05
4	-30,934.75	29	10	19	34.48	2,865.57	-3,136.34	0.91	0.48	-1,066.72
3	-28,932.61	29	11	18	37.93	1,952.12	-2,800.33	0.70	0.43	-997.68
2	-19,158.02	29	12	17	41.38	1,620.77	-2,271.02	0.71	0.50	-660.62
1	-11,090.78	29	12	17	41.38	1,305.36	-1,573.83	0.83	0.59	-382.44

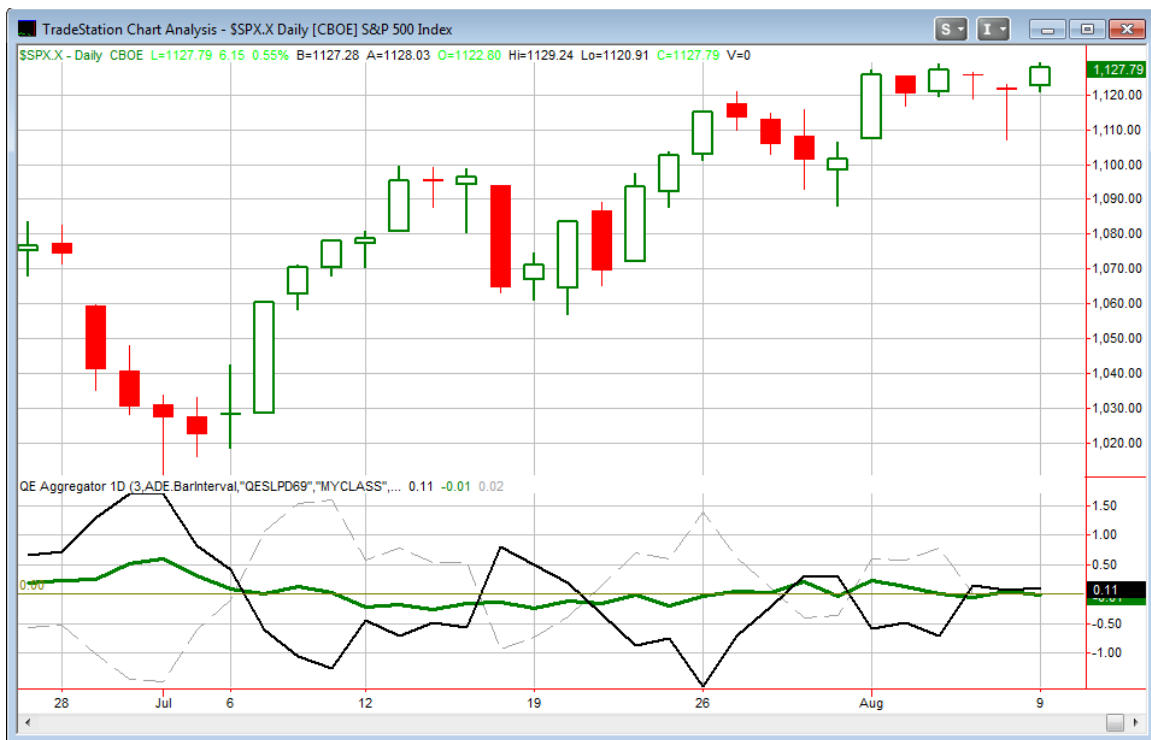
Day 1 isn't a whole lot different, but the instances that pull back do so much harder and for a longer period of time. If the market was trading below the 200ma then we could view this as a 5-day bearish edge rather than a 1-day bearish edge.

Of course tomorrow is a Fed Day. I've discussed many times before that Fed Days tend to be bullish. As I mentioned last night though, a big determinant in the size of the edge is where the market closes in relation to its daily range. Strong closes in the top 25% of

the daily range have greatly reduce the upside edge in the past. This was shown in The Quantifiable Edges Guide to Fed Days and it was also discussed in the 1/27/10 Subscriber Letter. A link to that letter is below.

[2010-01-27 QE Subscriber Letter.pdf](#)

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



The low volume and rising VIX on Monday helped to sink the green Aggregator line back below 0, though just barely. The negative value indicates the net expectation from the Active Studies over the next few days is for some downside. Meanwhile the black Differential line is above zero, indicating the SPX has slightly underperformed expectations over the last few days. So we have mildly negative expectations but a market that is already a little oversold versus recent expectations. Both lines on opposite sides of 0 is considered a neutral configuration. Due to this the Aggregator System turned flat at the close.

Currently the green Aggregator line is set up to flip back to positive tomorrow. Of course new bearish studies could change this. Meanwhile the Differential pivot will be 1,126.88

tomorrow. This means it would take an SPX close at or below this number to keep the black Differential line positive.

So even with a Fed Day on tap the Aggregator couldn't manage to remain positive. Sometimes when it appears the Aggregator signal is likely to turn off I will send out an email alerting subscribers that I will be exiting the trade idea at the close. In this case I had no interest in exiting the long SPY position at the close. This is due to 2 studies from the Quantifiable Edges Guide to Fed Days. These studies show 1) that since 2003 there has been a strong upside tendency in the overnight from the day before the Fed Day until the morning of, and 2) of the 20 instances that saw the SPY gap down since 2003, 18 filled the gap by 2pm and all 20 by the 4pm close. Based on these bits of information it seemed worthwhile to hold overnight and try to exit in the morning. I'll detail my plan in the Trade Ideas section below.

**Intermediate-term Outlook (2 weeks – 2 months)– updated 8/9 – bullish**

Monday's SPX breakout on strong breadth led to a few studies with intermediate-term implications that appear in the August 3<sup>rd</sup> Letter Monday night. They both looked at times the market hit new 50-day highs on extremely strong breadth. The first one simply looked at any 50-day high on a 90% or greater NYSE Up Volume %.

SPX closes at a 50-day high while the NYSE Up Volume % close > 90%. Buy 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
21	66,250.56	16	13	3	81.25	5,314.80	-947.29	5.61	24.31	4,140.66
20	59,416.79	17	13	4	76.47	5,105.66	-1,739.19	2.94	9.54	3,495.11
19	56,188.99	17	14	3	82.35	4,568.72	-2,591.04	1.76	8.23	3,305.23
18	52,597.01	17	13	4	76.47	4,768.23	-2,347.49	2.03	6.60	3,093.94
17	45,628.34	17	13	4	76.47	4,442.24	-3,030.20	1.47	4.76	2,684.02
16	43,642.00	17	12	5	70.59	4,744.13	-2,657.51	1.79	4.28	2,567.18
15	45,653.48	17	13	4	76.47	4,391.20	-2,858.02	1.54	4.99	2,685.50
14	35,151.48	18	13	5	72.22	4,142.55	-3,740.34	1.11	2.88	1,952.86
13	30,920.05	18	13	5	72.22	3,773.18	-3,626.26	1.04	2.71	1,717.78
12	33,165.24	18	11	7	61.11	4,500.07	-2,333.65	1.93	3.03	1,842.51
11	37,504.81	18	11	7	61.11	4,264.55	-1,343.60	3.17	4.99	2,083.60
10	35,501.76	18	12	6	66.67	3,824.66	-1,732.36	2.21	4.42	1,972.32
9	25,265.04	18	11	6	61.11	3,476.45	-2,162.66	1.61	2.95	1,403.61
8	24,873.22	18	12	6	66.67	3,305.37	-2,465.20	1.34	2.68	1,381.85
7	24,220.47	18	12	6	66.67	3,197.44	-2,358.14	1.36	2.71	1,345.58
6	25,043.14	18	12	6	66.67	2,797.62	-1,421.39	1.97	3.94	1,391.29
5	29,139.19	19	15	4	78.95	2,331.05	-1,456.62	1.60	6.00	1,533.64
4	23,823.24	19	16	3	84.21	1,935.10	-2,379.47	0.81	4.34	1,253.85
3	20,616.55	19	14	5	73.68	1,778.35	-856.06	2.08	5.82	1,085.08
2	20,893.52	19	17	2	89.47	1,261.72	-277.87	4.54	38.60	1,099.66
1	13,553.71	20	14	6	70.00	1,119.17	-352.45	3.18	7.41	677.69

These results suggested bullish tendencies both in the short-term and the intermediate-term.

I also examined the implications of fresh breakouts to new highs versus a repeated new high. Fresh breakouts typically provide a better edge and I found that was true in this case as well. This 2<sup>nd</sup> study from the August 3rd letter demonstrated this.

SPX closes at a 50-day high after not having done so for at least 10 days. NYSE Up Volume % > 90%. 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
25	50,143.03	10	9	1	90.00	5,867.85	-2,667.60	2.20	19.80	5,014.30
20	45,876.72	10	7	3	70.00	7,144.22	-1,377.60	5.19	12.10	4,587.67
15	38,685.53	10	7	3	70.00	6,262.94	-1,718.35	3.64	8.50	3,868.55
10	35,095.45	10	8	2	80.00	4,657.74	-1,083.25	4.30	17.20	3,509.55
9	29,807.00	10	7	2	70.00	4,616.82	-1,255.38	3.68	12.87	2,980.70
8	26,436.14	10	8	2	80.00	3,968.24	-2,654.88	1.49	5.98	2,643.61
7	26,064.35	10	8	2	80.00	3,950.95	-2,771.63	1.43	5.70	2,606.44
6	21,595.12	10	8	2	80.00	3,382.30	-2,731.65	1.24	4.95	2,159.51
5	24,817.77	10	8	2	80.00	3,549.12	-1,787.58	1.99	7.94	2,481.78
4	17,452.07	10	8	2	80.00	2,867.70	-2,744.75	1.04	4.18	1,745.21
3	21,710.82	10	9	1	90.00	2,432.15	-178.50	13.63	122.63	2,171.08
2	17,810.14	10	10	0	100.00	1,781.01	0.00	100.00	100.00	1,781.01
1	12,193.10	10	9	1	90.00	1,362.43	-68.80	19.80	178.23	1,219.31

Follow through so far has been weak. Wednesday (day 2) is the only day that the market closed above Monday at this point. But down days have been muted and with the short-term outlook now appearing positive we could get another leg up here soon.

Overall there are still a good number of intermediate-term studies in effect suggesting upside. Meanwhile, very little is appearing that would favor the bears. I'm still feeling more comfortable buying the dips than I am shorting the rallies.

### **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.*

*None tonight. I'll see if we get a more substantial edge to play in the next couple of days. Note due to Monday's strong finish neither Fed Day based SPY trade ideas triggered.*

### **Current Open Trade Ideas**

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	8/9/2010	\$112.39	\$112.99	0.53%		sell @ \$112.99 limit
IJR	8/9/2010	\$57.50	\$58.04	0.94%		System 90609

I will look to exit SPY at Monday's closing price. So if it gaps up as is often the case on Fed Day, then I would get a better fill. If it gaps down, then I will give it until 2pm to fill (90% of gaps down have filled by 2pm on Fed Days). If still not filled by 2pm, I will exit the trade. Should it gap down and consolidate in the first half hour, there is a chance I would place a stop below the consolidation. If so, I will send out an intraday update to subscribers.

This report has been prepared by Hanna Capital Management, LLC and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy securities. While information contained herein is believed to be accurate at the time of publication, we make no representation as to the accuracy or completeness of any data, studies, or opinions expressed and it should not be relied upon as such. Robert Hanna, Hanna Capital Management, LLC or clients of Hanna Capital Management, LLC may have positions or other interests in securities (including derivatives) directly or indirectly which are the subject of this report. This report is provided solely for the information of Hanna Capital Management, LLC clients and prospects who are expected to make their own investment decisions without reliance upon this report. Neither Hanna Capital Management, LLC nor any officer or employee of Hanna Capital Management, LLC accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. This report may not be reproduced, distributed or published by any recipient for any purpose without the prior express consent of Hanna Capital Management, LLC.

Copyright © 2010 Hanna Capital Management, LLC.