

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 3, 2010

Volume 3 Issue 212

Market Overview



Tonight's Research Points

- When the SPX has closed at a 20-day high just before a Fed Day, performance has been lacking.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

No clear edge at the moment. Certainly we could see one emerge in the next few days should the market react strongly to the news.

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
Active				
November 2, 2010	SPY up but 1% below high of day	1-2 days	Bullish	
October 28, 2010	1st Day Down After 5 up. Close > 200ma	1-9 days	Bullish	2.10%
Active - Long Term				
October 25, 2010	SPX Golden Cross	int term	Bullish	
October 20, 2010	20-high to 5 -low after persistent rise	1-12 days	Bullish	
October 18, 2010	SPX up. Issue% and Vol% very low	int term	Bearish	
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
Dropped Tonight				
November 2, 2010	SPX up. VIX up on Monday.	1 day	Bearish	
November 1, 2010	SPX down. Up Issue % > 55%.	1-3 days	Bullish	1.20%

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

The Evidence

The market put in a strong day ahead of the election and the Fed announcement. Perhaps traders were looking to get in ahead of a positive reaction. The SPX rose 0.8%, the Nasdaq was up 1.1% and the Russell 2000 led the way with a 2.1% gain. Breadth was strongly positive as the NYSE Up Issues % came in at 74% and the Up Volume % was 73%. Total volume declined for the 4th day in a row.

Tomorrow is a Fed Day, and I've mentioned that a few times in the past couple of days. Fed Days have generally exhibited an upside bias for nearly 30 years. One reason I believe Fed Days have performed well is that the Fed is often looked upon as the savior of the economy (and the market). Fed actions are often met with optimism and this optimism is often good for a short-term boost.

This optimism is also often a reaction desired by the Fed itself. They try and manage expectations not only through their monetary policy but also through the statements they release. Never wanting things to overheat too much or for a panic to ensue. During good times they will focus more on risks in their statements and will keep a bit of a lid on the excitement. During tough times they will focus more on positives. A panicky public is not good for either the market or the economy so they will act as the voice of reason when it appears panic may set in. And during those times when it seems neither overheating nor panicking is much of a danger, they simply look to instill confidence. Confidence in the economy, the market, the government, and their own abilities.

So when is the market least in need of a confidence boost? I'd say when it is already trading at an intermediate-term high. I ran a new study tonight that looked at other times the SPX closed at a 20-day high on the day before a Fed Day. Results below.

SPX closes at a 20-day high. Tomorrow is a Fed Day.
Buy on close. Sell next day's close. \$100k/trade. 1982 - present.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	(\$1,413.21)	Profit Factor	0.86
Gross Profit	\$8,920.90	Gross Loss	(\$10,334.11)
Total Number of Trades	33	Percent Profitable	42.42%
Winning Trades	14	Losing Trades	19
Even Trades	0		
Avg. Trade Net Profit	(\$42.82)	Ratio Avg. Win:Avg. Loss	1.17
Avg. Winning Trade	\$637.21	Avg. Losing Trade	(\$543.90)
Largest Winning Trade	\$1,934.04	Largest Losing Trade	(\$2,492.10)

What I see here is that there has been no tendency for the market to advance under these circumstances. There could even be a slight downside edge, but the numbers aren't compelling enough for me to bank on that. I'd simply view it as neutral. Compare these results to those times where the SPX did NOT close at a 20-day high just before a Fed Day.

SPX closes below a 20-day high. Tomorrow is a Fed Day.
Buy on close. Sell next day's close. \$100k/trade. 1982 - present.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$67,933.28	Profit Factor	2.35
Gross Profit	\$118,147.42	Gross Loss	(\$50,214.14)
Total Number of Trades	197	Percent Profitable	61.93%
Winning Trades	122	Losing Trades	75
Even Trades	0		
Avg. Trade Net Profit	\$344.84	Ratio Avg. Win:Avg. Loss	1.45
Avg. Winning Trade	\$968.42	Avg. Losing Trade	(\$669.52)
Largest Winning Trade	\$5,130.15	Largest Losing Trade	(\$2,442.96)

Here the results strongly suggest an upside edge.

Market watchers seem to be very focused on tomorrow's announcement as it relates to QE2. So will the Fed see the current market as one it needs to save? Does it at least need to instill greater confidence? The fact that the market is already at a 20-day high suggests perhaps not. Of course there are many that would argue a little more confidence is

exactly what this economy needs. So it will be interesting to see just how the Fed decides to handle it all. Bottom line in my eyes is that this Fed Day appears to be more of a crapshoot than most.

I'll be watching tomorrow's reaction carefully to see how it might translate to further edges over the next few days.

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



The green Aggregator line tonight remains above zero. The positive value indicates the net expectation from the Active Studies over the next few days is for a move up. Meanwhile the black Differential line fell further below 0. This means the SPX has outperformed expectations over the last few days. So we have positive expectations but a market that is relatively overbought. This is considered a neutral configuration. This can be seen on the Aggregator chart whenever both lines are on opposite sides 0. Due to this the Aggregator System remained flat at the close.

The green Aggregator line is set up to remain positive tomorrow. Of course that could change if bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,186.77. Any close at or below this level would move the black Differential line back into positive

territory. So for the SPX to move to oversold versus recent expectations and possibly trigger a long it will need to close about 0.6% lower tomorrow.

Between the Fed and the election news I'm happy to be sidelined. The market reaction could very well be strong as the news gets absorbed. And strong reactions tend to lead to strong edges. I'd expect some tradable opportunities to appear soon.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/1 – bullish

Not much to discuss from an intermediate-term standpoint. The market again made new rally highs this week. With the very tight action in the market over the past week, no studies of intermediate-term consequence emerged. I'm still not seeing strong evidence that the uptrend is about to end.

The Nasdaq/SPX relative strength indicator continues to favor the Nasdaq. A leading Nasdaq has historically been a good sign. The Advance/Decline line hit another new high this past week suggesting breadth remains positive. Momentum is certainly favoring the upside and the market is trading above important moving averages. Until the market begins to falter and more bearish evidence emerges, I'll continue to trade with a bullish bias. For my own trading a bullish bias means I tend to trade the long side with a little more aggressiveness and I will be extra selective with short trades.

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. If the market sells off tomorrow and closes under the Differential Pivot then it could trigger a long signal. Aggressive traders could check the Intraday Quantifinder and the Systems page before the bell tomorrow to see if a bullish outlook appears likely.

Current Open Trade Ideas

None.

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