

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

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November 9, 2010

Volume 3 Issue 216

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## **Market Overview**



## **Tonight's Research Points**

- Persistent up moves rarely come to an abrupt end. There is a good chance the SPX closes higher within the next week.
- Unfilled gaps from 50-day highs will often see further selling over the next 1-2 days.
- Pullbacks from high areas that are initiated on very light volume offer solid risk/reward for the short-term bear case.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

## **Short-term Outlook**

### **The Bottom Line**

Studies are greatly mixed. And while the net expectation is for a continued rise, tomorrow's expectation is slightly negative. This is reflected in the 1-day outlook above. Should the 1-day move lower occur, it could set up a nice swing long opportunity. I'm still flat and looking towards tomorrow afternoon or Wednesday morning to possibly begin scaling long.

*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>				
November 9, 2010	Low volume drop from 50-day high	1-6 days	Bearish	-1.80%
November 9, 2010	Unfilled gap down from 50-day high	1-2 days	Bearish	-1.10%
November 9, 2010	SPX 5+ up days then 1 down	1-6 days	Bullish	2.10%
November 8, 2010	SPY volume decline twice at 50-high	1-2 days	Bearish	-0.90%
November 8, 2010	%b > 1.15 2 days in row. 20-day high	1-6 days	Bullish	2.20%
November 5, 2010	Gap-n-Go to a 50-day high	1-3 days	Bearish	-1.00%
November 5, 2010	Strong breadth and vol at a 10-day high	1-5 days	Bullish	1.30%
November 5, 2010	Very strong breadth & 50-day high	1-5 days	Bullish	2.00%
<b>Active - Long Term</b>				
November 5, 2010	Very strong breadth & 50-day high	1-30 days	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	
October 18, 2010	SPX up. Issue% and Vol% very low	1-25 days	Bearish	
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
<b>Dropped Tonight</b>				
November 4, 2010	Outside day 50-high, strong volume.	1-3 days	Bearish	-0.90%

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

***The Evidence***

Generally quiet trading led to a mixed day on Wall St. The SPX finished down 0.2% while the Nasdaq and Russell 2000 each gained less than 0.1%. Breadth was a little negative as the NYSE Up Issues % came in at 45% and the Up Volume % was 46%. Total NYSE volume was the lightest in a couple of weeks.

In the note on the intraday Quantifinder this afternoon I mentioned that the day was likely to trigger some studies from the 10/28 letter and that traders may want to take a look at it. When it was over they did both trigger.

This first one looked at pullbacks from persistent moves higher. When the market is lodged in a persistent move higher it is less likely to see an abrupt end to that move. One way to measure persistency is to simply require a streak of up days. The first study below from the 10/28 Letter did just this.

After closing higher for at least 5 days in a row SPX closes lower but above the 200ma.  
Buy on close. Sell X days later. \$100k/trade. 1995 - 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
10	55,101.74	51	41	10	80.39	1,676.77	-1,364.60	1.23	5.04	1,080.43
9	56,287.79	56	46	10	82.14	1,602.62	-1,743.29	0.92	4.23	1,005.14
8	49,677.69	56	39	17	69.64	1,826.52	-1,268.04	1.44	3.30	887.10
7	43,248.65	58	40	18	68.97	1,619.03	-1,195.14	1.35	3.01	745.67
6	41,696.90	60	41	19	68.33	1,537.67	-1,123.56	1.37	2.95	694.95
5	32,010.06	60	40	20	66.67	1,269.62	-938.74	1.35	2.70	533.50
4	29,728.05	60	38	22	63.33	1,245.43	-799.93	1.56	2.69	495.47
3	13,609.76	60	36	24	60.00	1,014.18	-954.20	1.06	1.59	226.83
2	7,630.80	60	36	24	60.00	847.05	-952.62	0.89	1.33	127.18
1	4,412.07	60	36	23	60.00	530.38	-638.33	0.83	1.30	73.53

53 of 60 instances (88%) closed above the entry price at some point in the next week.

This isn't the kind of setup that will necessarily lead to explosive results. What we do see here are very consistent results on an ample sample size. Over 80% of the trades are profitable once you get out almost 2 weeks.

Though the SPY didn't fall too far today, it did gap down and fail to fill that gap. The 2<sup>nd</sup> study I noted from that October 28<sup>th</sup> letter looked at unfilled gaps down from 50-day highs. I have updated it below.

SPY posts an unfilled down gap from a 50-day high. Close > 200ma.  
Buy on close. Sell X days later. \$100k/trade. 1999 - 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	-15,833.50	44	19	25	43.18	1,035.71	-1,420.48	0.73	0.55	-359.85
4	-7,975.78	44	22	22	50.00	822.24	-1,184.78	0.69	0.69	-181.27
3	-11,414.66	45	20	25	44.44	458.72	-823.56	0.56	0.45	-253.66
2	-16,780.98	50	21	29	42.00	565.76	-988.34	0.57	0.41	-335.62
1	-7,832.34	50	23	27	46.00	590.25	-792.89	0.74	0.63	-156.65

These unfilled gaps from high levels often tend to lead to more selling over the next few days. The edge isn't huge, but it certainly appears worthy of consideration.

I also noted that volume was very light today. Light volume pullbacks are generally regarded as bullish. Yet in my research I have found that when pullbacks begin on very light volume the pullback serves a good chance of deepening. Today's mild pullback in the SPX occurred on the lightest NYSE volume in over 2 weeks. Below I have devised a study to look at similar scenarios.

After closing at a 50-day high yesterday, the SPX declines today. NYSE volume is the lightest in 10 days. Buy on close. Sell X days later. \$100k/trade. 1970 - present.

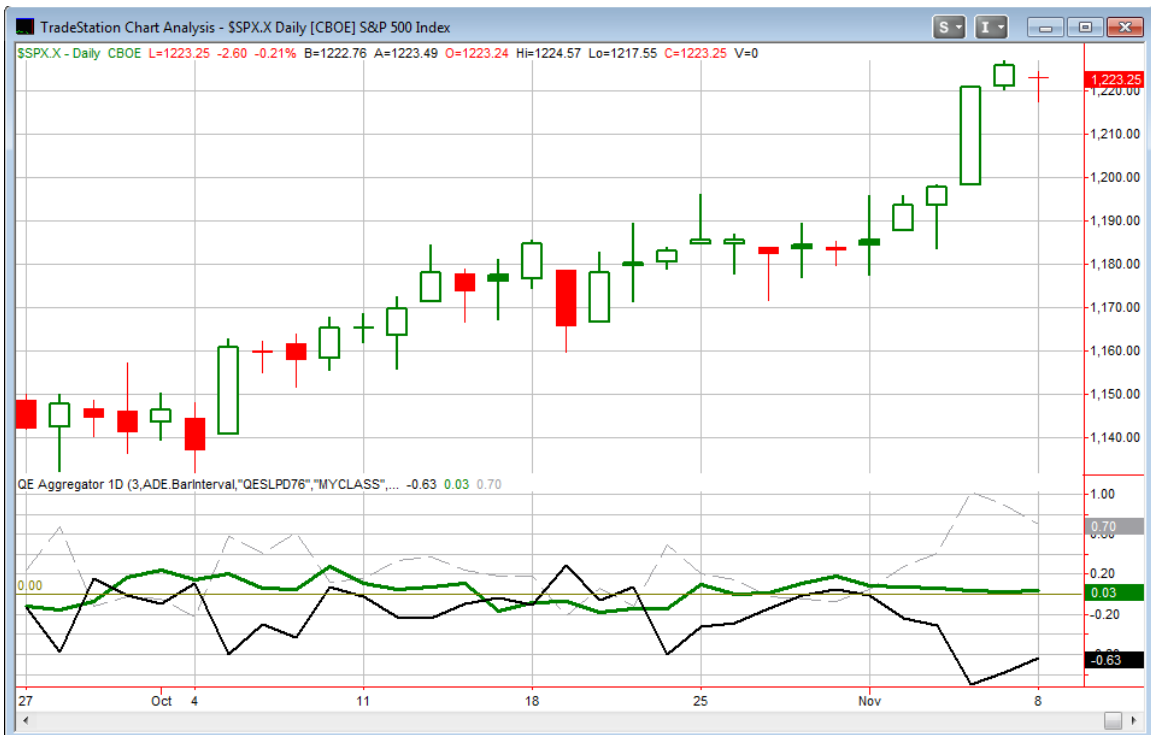
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-22,648.01	55	29	26	52.73	1,757.62	-2,831.50	0.62	0.69	-411.78
9	-19,839.87	55	28	27	50.91	1,785.42	-2,586.35	0.69	0.72	-360.72
8	-30,403.11	55	26	29	47.27	1,487.96	-2,382.42	0.62	0.56	-552.78
7	-35,890.07	55	25	30	45.45	1,353.41	-2,324.18	0.58	0.49	-652.55
6	-36,280.43	56	24	32	42.86	1,164.09	-2,006.83	0.58	0.44	-647.86
5	-24,892.32	57	26	31	45.61	1,002.17	-1,643.50	0.61	0.51	-436.71
4	-19,799.34	59	29	30	49.15	907.14	-1,536.88	0.59	0.57	-335.58
3	-4,611.63	60	32	28	53.33	923.11	-1,219.68	0.76	0.86	-76.86
2	-1,834.06	60	30	30	50.00	823.51	-884.65	0.93	0.93	-30.57
1	-4,127.00	60	30	30	50.00	561.66	-699.22	0.80	0.80	-68.78

These results suggest a mild bearish edge over the 1<sup>st</sup> 6-7 days. The edge is not the most reliable as the “% Profitable” is close to a coin toss. The edge lies in the fact that downside risk has strongly outsized reward. Since it doesn't appear to be terribly reliable, I also ran a chart using a 6-day exit to see how the edge has played out over time.



Even without the real high percentage, the edge has been nicely consistent over the last 40 years. It certainly seems worthy of inclusion among the active studies.

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



The green Aggregator line tonight remains mildly 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 is still far below 0. The negative value means the SPX has strongly outperformed expectations over the last few days. So we have positive expectations but a market that is strongly overbought. This is considered a neutral configuration. This can be seen on the Aggregator chart whenever both lines are on opposite sides of 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 enough bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,223.05. Any close at or below this level would move the black Differential line back into positive territory. So just about any lower close tomorrow would leave the SPX relatively oversold versus expectations.

I've been patient over the last week as the market has remained overbought and kept me from suggesting new trade ideas. We may be getting the pullback I've been waiting for here. There is a very strong chance that a move lower would trigger a long Aggregator System signal on Tuesday. Traders who would like to get in ahead of time rather than wait for confirmation from tomorrow night's letter should check the systems page tomorrow as we approach the close. I normally update it with about 10 minutes left to go in the day. I also typically send out a tweet as soon as it is updated as a reminder. <http://twitter.com/qerob>

***Intermediate-term Outlook (2 weeks – 2 months)– updated 11/8 – bullish***

The acceleration to new highs on strong breadth produced some strong intermediate-term studies in Thursday night's letter. I won't repeat that whole discussion here, but it seems to provide another bit of evidence that the move up may have further to go. We also went another week without any bearish studies of intermediate-term significance emerging.

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 and the number of NYSE new 52-week highs is approaching its spring peak. Momentum is certainly favoring the upside and the market is trading above important moving averages. As I've been saying, 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 again tonight. Aggressive traders could look to start taking on long exposure if we close down tomorrow. Should this happen I expect to have 1 or 2 trade ideas tomorrow night.

## **Current Open Trade Ideas**

*None.*

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