

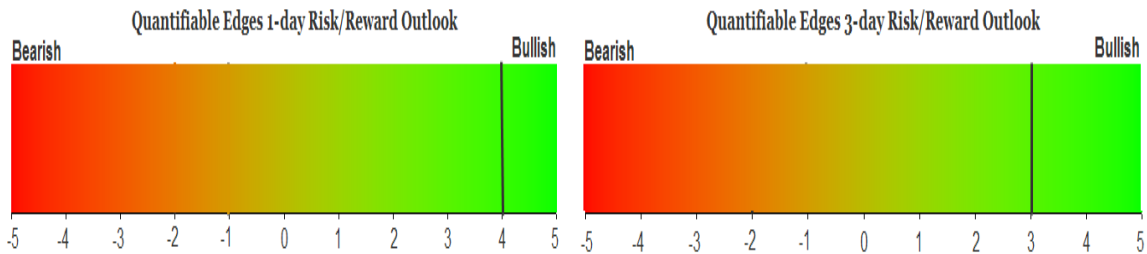
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 24, 2010

Volume 3 Issue 227

Market Overview



Tonight's Research Points

- 2 consecutive unfilled gaps down have typically been followed by a rebound over the next week since 1998.
- Wednesday and Friday surrounding Thanksgiving have been seasonally bullish. Perhaps even more so when Monday and Tuesday close lower.
- Drops > 1% on poor breadth are often followed by gains over the next 1-9 days.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook

The Bottom Line

Tuesday's selloff has setup another long entry for the Aggregator. Tonight's studies are all suggesting bullish implications. The market is oversold and there is an ample amount of bullish evidence. I'm long and looking to possibly get longer.

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 24, 2010	2 Unfilled Gaps Down in SPY	1-5 days	Bullish	2.10%
November 24, 2010	Wed-Fri Thanksgiving Seasonality	2 days	Bullish	
November 24, 2010	SPX down 1% Decliners 2x Advancers	1-9 days	Bullish	3.00%
November 17, 2010	Down 4 on Wednesday	1-8 days	Bullish	
Active - Long Term				
November 22, 2010	High number of POMO Days recently	int term	Bullish	
November 15, 2010	QQQQ 5 lower lows and large drop	1-20 days	Bullish	
November 15, 2010	SPX down 1% SOX Up	1-20 days	Bullish	
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	
Dropped Tonight				
November 22, 2010	SPY low vol. VIX low. Op-ex.	1-4 days	Bearish	-1.90%
November 22, 2010	Op-ex up on mediocre volume	1-2 days	Bullish	0.90%
November 17, 2010	Down 4 and worst day of downmove	1-5 days	Bullish	

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

The Evidence

Overnight news put the market off to a bad start on Tuesday and it never recovered. The major indices all had rough days. The SPX dropped 1.4%, the Nasdaq lost 1.5% and the Russell 2000 fell 1.0%. Breadth was extremely negative as the NYSE Up Issues % came in at 23% and the Up Volume % was just 9%. Total volume rose from Monday's level.

While Monday's muted action didn't give us much to talk about last night, Tuesday's session more than made up for it. There's a lot to discuss so I'll get right to it.

Tuesday was the 2nd day in a row that the SPY gapped down and failed to fill. In the 8/9/10 Subscriber Letter I looked at other times the SPY gapped down and failed to fill 2 days in a row. This setup appeared to provide a long side edge which was most prominent since 1998. Below I have updated that study.

SPY posts an unfilled gap down today and yesterday.
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	29,559.76	32	24	8	75.00	1,786.41	-1,664.26	1.07	3.22	923.74
4	16,459.64	33	18	15	54.55	2,143.80	-1,475.25	1.45	1.74	498.78
3	10,604.71	33	17	16	51.52	1,767.47	-1,215.14	1.45	1.55	321.35
2	7,418.64	34	14	20	41.18	1,925.52	-976.93	1.97	1.38	218.20
1	9,044.85	37	21	16	56.76	919.65	-641.74	1.43	1.88	244.46

These results appear to favor upside. Tonight I also decided to filter the study based on the 200ma. Those results are below.

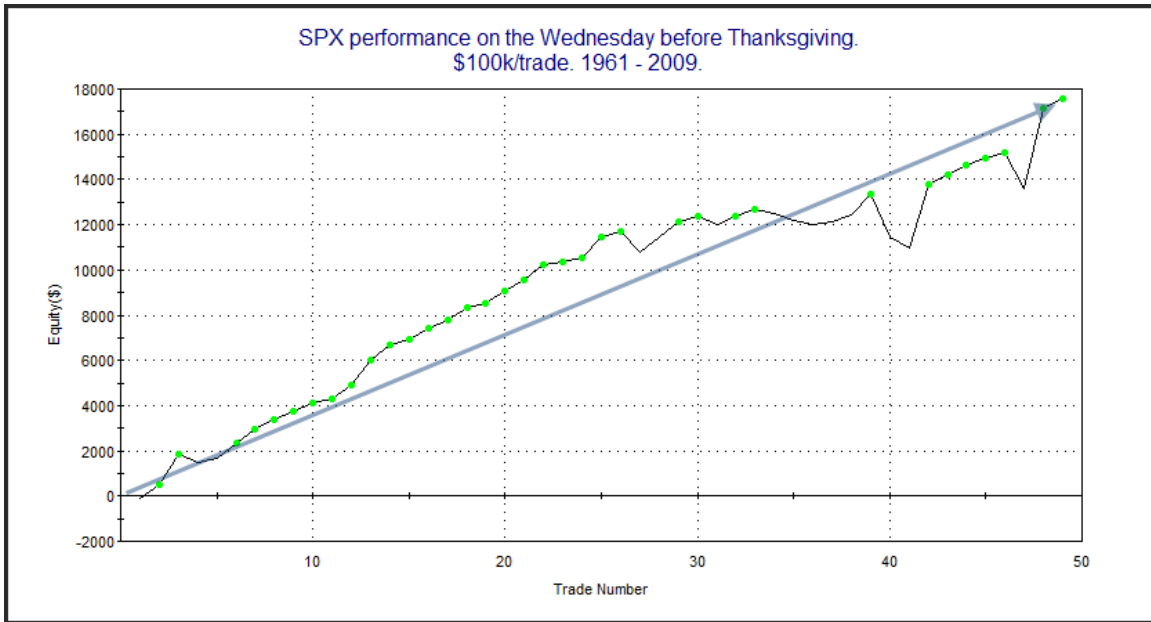
SPY posts an unfilled gap down today and yesterday. Close > 200ma.
Buy on close. Sell X days later. \$100k/trade. 1998 - present.

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	13,319.00	15	13	2	86.67	1,493.24	-3,046.54	0.49	3.19	887.93
4	10,906.02	15	11	4	73.33	1,478.33	-1,338.90	1.10	3.04	727.07
3	7,011.21	15	10	5	66.67	1,238.00	-1,073.75	1.15	2.31	467.41
2	3,389.96	15	8	7	53.33	1,213.90	-903.03	1.34	1.54	226.00
1	2,426.71	15	9	6	60.00	783.52	-770.83	1.02	1.52	161.78

14 of 15 instances (93%) closed above the entry price at some point in the next week.

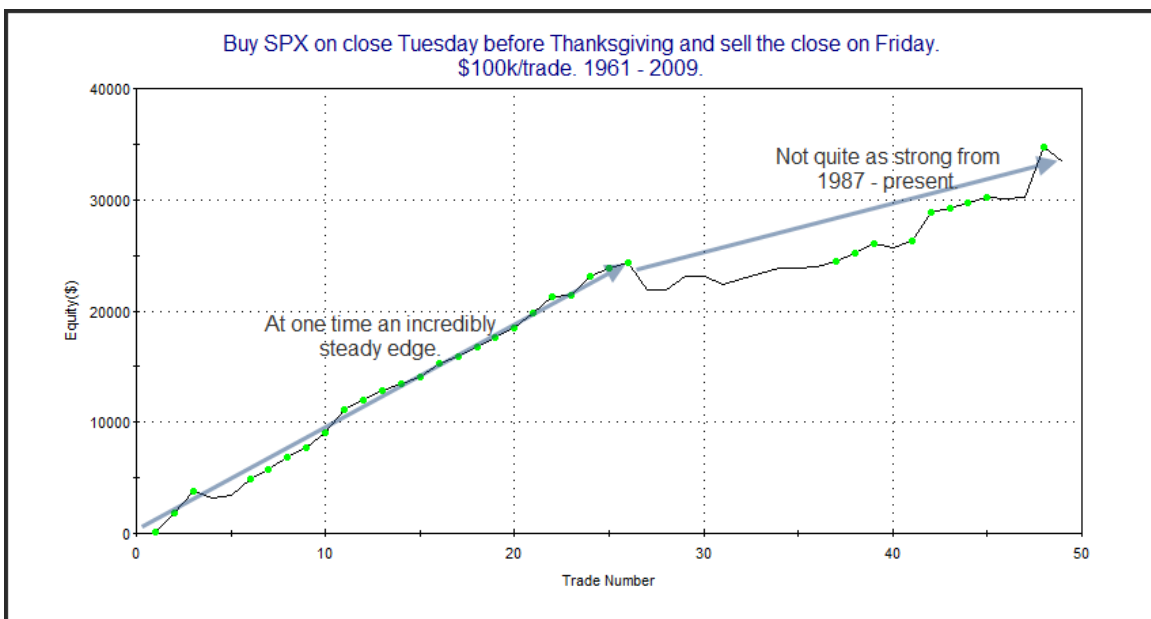
As often happens with bullish reversal studies, this one appears to be more consistent yet not quite as powerful when the market is trading above its 200ma. Fourteen of fifteen instances closing above the entry price at some point in the next week is a compelling statistic, especially for a study with so few parameters.

In the Sunday night letter I discussed the positive tendencies this week – primarily Wednesday and Friday surrounding Thanksgiving. Below is the equity curve I showed in that letter that looked at the Wednesday before Thanksgiving over the last 49 years.



As I mentioned then the edge generally looks fairly steady over a long period. Still, there have been a couple of sharp dips in the last 10 years. 2000 saw the SPX drop 1.85% and in 2007 it fell 1.59%.

I also looked at what would've happened if you bought Tuesday's close and sold Friday's close each year. This would have you long the 2 seasonally bullish days. That chart is again below.



Interesting about this week is that the lead-up to the Wed-Fri trade has seen Monday and Tuesday both close down. I checked to find all the other instances where Monday and Tuesday both saw the SPX decline. Those results are below.

If SPX closes down Monday and Tuesday before Thanksgiving then buy Tuesday's close.
Sell Friday's close. \$100k/trade. 1961 - 2009.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$7,330.81	Profit Factor	12.03
Gross Profit	\$7,995.43	Gross Loss	(\$664.62)
Total Number of Trades	8	Percent Profitable	87.50%
Winning Trades	7	Losing Trades	1
Even Trades	0		
Avg. Trade Net Profit	\$916.35	Ratio Avg. Win:Avg. Loss	1.72
Avg. Winning Trade	\$1,142.20	Avg. Losing Trade	(\$664.62)
Largest Winning Trade	\$1,974.02	Largest Losing Trade	(\$664.62)

Instances are low but the stats are heavily lopsided to the short-term bullish case. All the dates are listed below.

If SPX closes down Monday and Tuesday before Thanksgiving then buy
Tuesday's close. Sell Friday's close. \$100k/trade. 1961 - 2009.

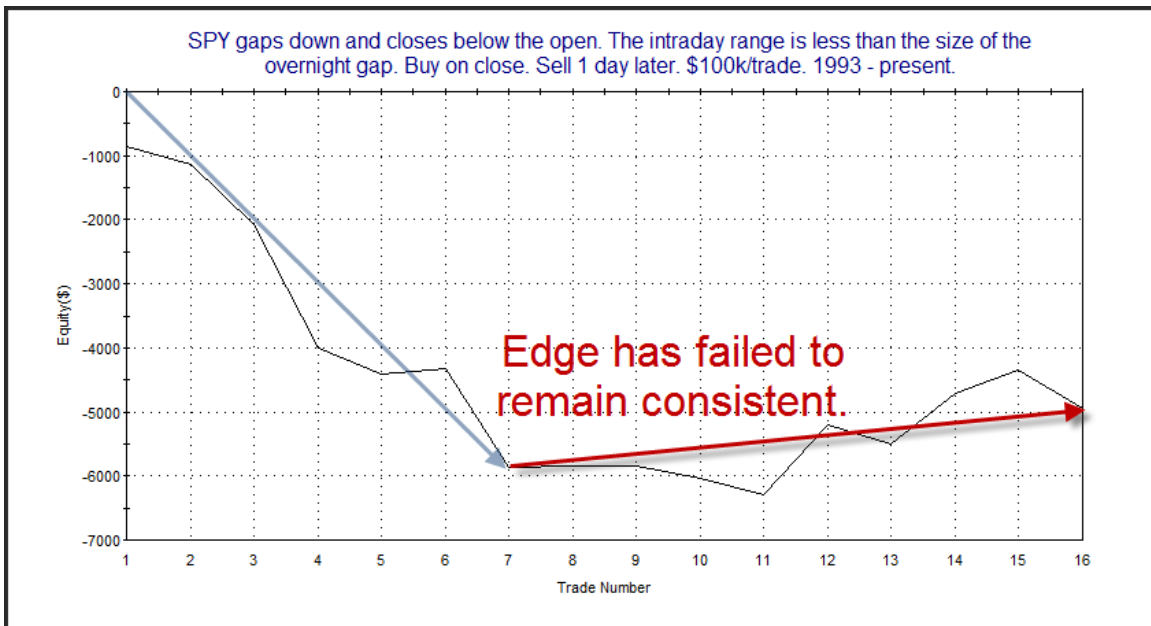
Date/Time	Signal	Price	% Profit	Run-up DrawDown
11/24/64	Buy	\$85.73	(0.66%)	\$0.00
11/27/64	Sell	\$85.16		(\$664.62)
11/22/66	Buy	\$79.67	1.48%	\$1,480.90
11/25/66	Sell	\$80.85		\$0.00
11/25/69	Buy	\$92.94	0.94%	\$935.25
11/28/69	Sell	\$93.81		\$0.00
11/23/71	Buy	\$90.16	1.97%	\$1,974.02
11/26/71	Sell	\$91.94		\$0.00
11/20/73	Buy	\$98.66	0.79%	\$1,114.30
11/23/73	Sell	\$99.44		\$0.00
11/23/82	Buy	\$132.92	1.47%	\$2,037.92
11/26/82	Sell	\$134.88		(\$586.56)
11/22/94	Buy	\$450.08	0.49%	\$619.38
11/25/94	Sell	\$452.29		(\$1,309.80)
11/23/99	Buy	\$1,404.64	0.85%	\$1,462.60
11/26/99	Sell	\$1,416.62		(\$388.37)

We haven't seen both Monday and Tuesday close lower since 1999 and we haven't seen Wed-Fri fail to rally following this setup since 1964.

There was one bearish study that appeared in the Quantifinder tonight. It looked at times the SPY gapped down an amount that turned out to be larger than the full intraday range. When I first looked it appeared to have bearish tendencies. I've updated the study below.

SPY gaps down and closes below the open. The intraday range is less than the size of the overnight gap. Buy on close. Sell X days later. 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
3	505.50	16	7	9	43.75	1,781.28	-1,329.28	1.34	1.04	31.59
2	-1,372.15	16	6	8	37.50	1,584.18	-1,359.65	1.17	0.87	-85.76
1	-4,947.78	16	5	11	31.25	471.52	-664.13	0.71	0.32	-309.24

The numbers here are not as compelling as they once were. Since the edge basically only lasts 1 day I ran an equity curve using the 1-day exit strategy below.



As you see the edge has failed to remain consistently bearish. I'll continue to keep an eye on this one to see if it decides to reassert itself, but am not including it among the active studies tonight.

The Quantifinder also noted a study last seen earlier this month in the 11/15/10 Letter. Below I have clipped an excerpt from that letter. (Study NOT updated.)

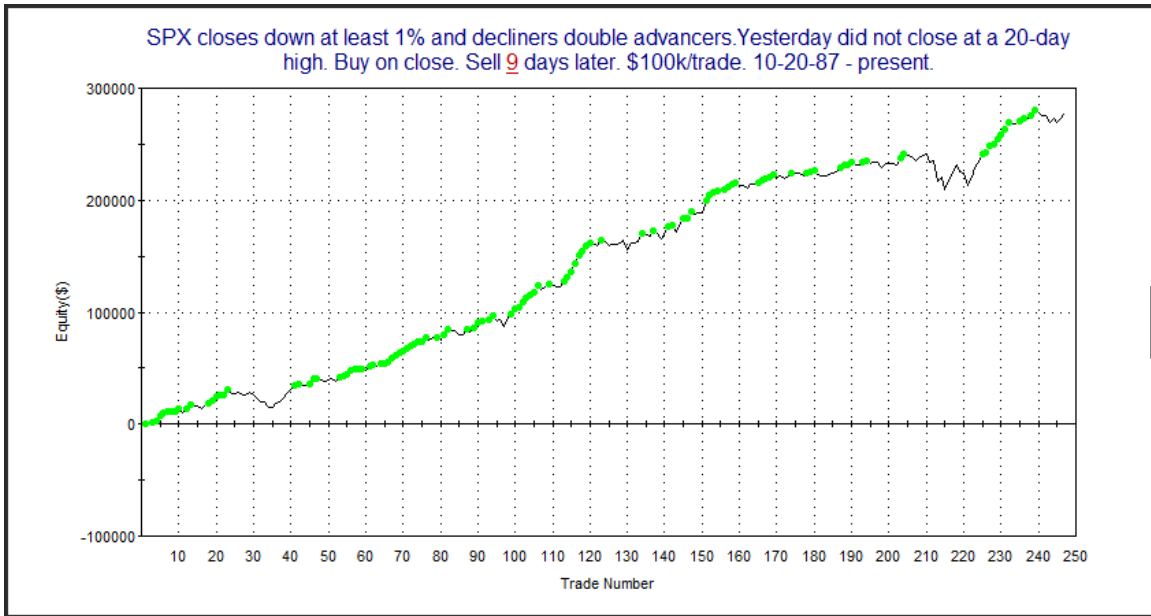
Another SPX study looked at strong selloffs on very weak breadth as we saw on Friday. This study was last seen in the 8/20/10 Subscriber Letter. I have updated the results below.

SPX closes down at least 1% and decliners double advancers. Yesterday did not close at a 20-day high. Buy on close. Sell X days later. \$100k/trade. 10-20-87 - 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	237,477.28	237	155	82	65.40	2,981.90	-2,740.45	1.09	2.06	1,002.01
9	277,601.27	247	173	74	70.04	2,813.18	-2,825.39	1.00	2.33	1,123.89
8	237,497.89	260	172	87	66.15	2,777.11	-2,760.52	1.01	1.99	913.45
7	230,961.73	278	174	104	62.59	2,648.14	-2,209.75	1.20	2.00	830.80
6	208,695.50	293	183	110	62.46	2,528.96	-2,310.04	1.09	1.82	712.27
5	198,998.45	319	193	126	60.50	2,343.44	-2,010.20	1.17	1.79	623.82
4	159,481.16	340	200	140	58.82	2,132.98	-1,907.97	1.12	1.60	469.06
3	162,260.65	374	232	142	62.03	1,830.09	-1,847.32	0.99	1.62	433.85
2	157,149.10	425	241	184	56.71	1,725.71	-1,406.23	1.23	1.61	369.76
1	108,828.25	478	282	196	59.00	1,147.32	-1,095.49	1.05	1.51	227.67

84.5% of instances closed above the entry price at some point in the next week.

Prior to the Crash of '87, very weak breadth days were often followed by more weakness. This changed after the crash. This is the reason that I only run this test back until just after the crash. As you can see there have been a large number of instances over the last 23 years. The edge appears to be very solid as well. Below is the equity curve using a 9-day exit.



While there have been some brief dips the equity curve has been incredibly steady for such a common setup over such a long period.

Everything came up roses tonight as far as the studies. Only bullish additions to the Active Studies List.

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



Tuesday's action had a strong impact on the Aggregator chart. The green Aggregator line moved farther above 0 as more bullish evidence emerged. 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 popped sharply back above 0. The positive value means the SPX has underperformed expectations over the last few days. So we have positive expectations and a market that is currently oversold. Historically this combination has provided a short-term bullish edge. A bullish configuration can be seen on the Aggregator chart whenever both lines are above 0. Due to this the Aggregator System turned long at the close.

The green Aggregator line is set up to remain positive tomorrow. This could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be at 1,205.63. This means the SPX will need to gain over 2.1% in order to be considered overbought and place the Differential line below 0. So for the long bias to change tomorrow we'll either need to see very bearish studies or a very strong upward move in the SPX.

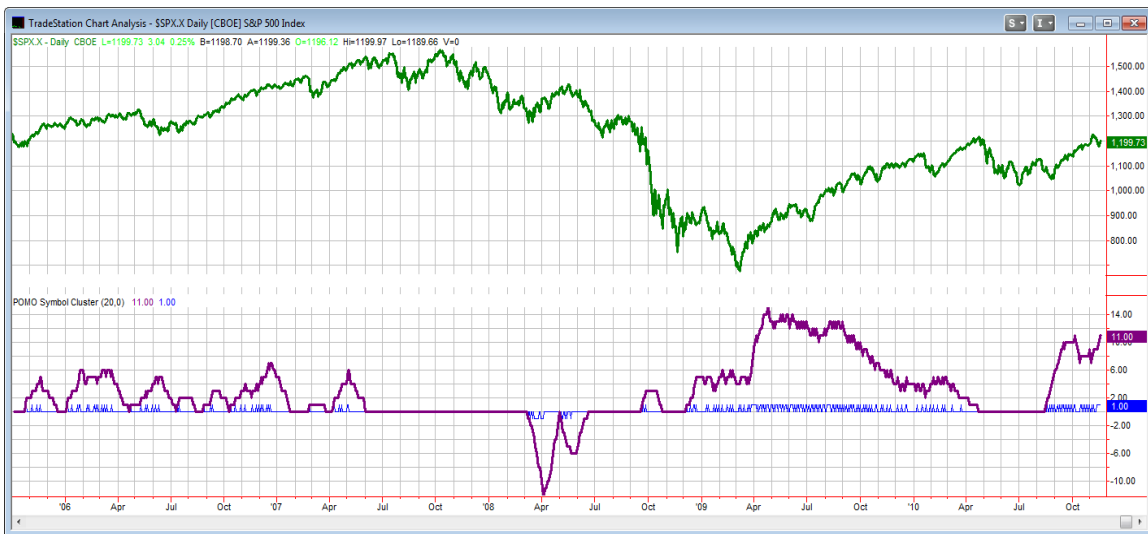
Too many bullish indications for me not to be interested in the long side. We're seeing price patterns, oversold breadth, seasonality and POMO action all suggesting a bounce. Additionally, the one short-term bearish study that was on the board reached its target today and was removed. I am already fairly long, but will look to scale in a bit more tomorrow.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/22 – bullish

I've seen a lot written lately about POMO days. POMO stands for Permanent Open Market Operations and it's the Fed's current method for trying to inject life (by injecting money) into the economy. They used to lower interest rates when they wanted to stimulate the economy but with interest rates already at zero that is no longer an option. It has been noted by a number of analysts that these liquidity injections appear to be stimulative for the stock market as well. Tom McClellan of McClellan Financial Publications wrote an excellent piece on POMO days a few weeks ago. Tom suggested that the liquidity injection may not take effect immediately and he looked at the how the market acted if there was a POMO within the last week rather than just being in the market on the day of the actual POMO. You can read his piece using the link below:

http://www.mcoscillator.com/learning_center/weekly_chart/pomo_the_hot_new_timing_tool

I decided to take my own look at POMO days. In doing so I decided to see how the market performed when a series of POMO days were clustered together. The assumption here is that if the Fed is regularly pumping money into the system it is more likely to have a bullish effect on the stock market than if there is just an occasional solitary injection. I examined different lookback periods. Below is a 20-day (approx 1-month) lookback period. It shows how many POMO days there have been in the last 20 days at any given point in time since August 0f 2005. This is as far back as data is available. (Data can be found on [the Fed's website here](#).) The top line on the chart is the S&P 500.



It's a little tough to read on the chart, but there have now been 11 POMO days in the last 20 day period. This is as large a cluster as we have seen at any time other than the mid-

April through mid-September pumping in 2009. That pumping coincided with a very strong stock market rally.

You'll note that in 2008 the POMO days cluster went negative. This is because the Fed went on a bit of a selling spree at that time. Those were days where they were selling securities rather than buying them. Since they were selling I represented them on my indicator as a negative day. As you can see the market did not perform too well after that period of Fed selling.

The tentative POMO day schedule is currently showing 11 more POMO buying days between now and December 9th, so we aren't likely to see a dip in the current cluster any time soon. To see possible implications I ran several studies examining performance after clusters had reached certain sizes. Below is a sample optimization report on some tests I ran.

Hold SPX if there are "POMO Days" number of POMO Days over the last "Days Back", offset "Offset" number of days. Go flat if the cluster of POMO Days is not large enough.

Days Back	Offset	POMO 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
18	0	5	56,271.24	299	170	129	56.86	982.02	-857.92	1.14	1.51	188.20
19	0	5	53,538.94	322	183	139	56.83	968.18	-889.49	1.09	1.43	166.27
20	0	5	39,932.49	348	192	156	55.17	951.73	-915.38	1.04	1.28	114.75
18	1	5	61,362.54	298	174	124	58.39	969.74	-865.91	1.12	1.57	205.91
19	1	5	46,969.64	321	180	141	56.07	964.00	-897.52	1.07	1.37	146.32
20	1	5	44,105.37	347	194	153	55.91	955.02	-922.67	1.04	1.31	127.10
18	0	6	40,800.84	224	130	94	58.04	934.71	-858.64	1.09	1.51	182.15
19	0	6	45,271.28	237	137	100	57.81	946.35	-843.79	1.12	1.54	191.02
20	0	6	42,200.09	252	143	109	56.75	919.70	-819.42	1.12	1.47	167.46
18	1	6	37,979.78	223	126	97	56.50	941.70	-831.69	1.13	1.47	170.31
19	1	6	39,857.89	236	134	102	56.78	917.66	-814.79	1.13	1.48	168.89
20	1	6	32,748.43	251	141	110	56.18	918.96	-880.22	1.04	1.34	130.47
18	0	7	40,380.97	199	114	85	57.29	990.66	-853.58	1.16	1.56	202.92
19	0	7	38,323.24	204	116	88	56.86	977.40	-852.90	1.15	1.51	187.86
20	0	7	40,972.87	209	120	89	57.42	969.64	-847.01	1.14	1.54	196.04
18	1	7	37,873.50	198	112	86	56.57	980.18	-836.13	1.17	1.53	191.28
19	1	7	39,732.76	203	116	87	57.14	965.25	-830.30	1.16	1.55	195.73
20	1	7	37,463.63	208	118	90	56.73	970.99	-856.82	1.13	1.49	180.11
18	0	8	38,068.85	170	95	75	55.88	1,064.24	-840.45	1.27	1.60	223.93
19	0	8	38,204.86	181	102	79	56.35	1,024.88	-839.65	1.22	1.58	211.08
20	0	8	39,237.94	191	109	82	57.07	990.37	-837.96	1.18	1.57	205.43
18	1	8	33,724.19	169	94	75	55.62	1,043.02	-857.60	1.22	1.52	199.55
19	1	8	35,504.11	180	101	79	56.11	1,013.12	-845.83	1.20	1.53	197.25
20	1	8	35,264.73	190	106	84	55.79	997.78	-839.28	1.19	1.50	185.60

The offset may be a little confusing so I'll explain that a little more. The assumption there is that even if the Fed buys treasuries today and pumps money into the banking system, that money will take at least a day to make its way into the stock market. So the offset of "1" is really looking at how big the cluster would have been as of yesterday.

Results here are strong across the board. The best performing parameters would be to look for a cluster of at least 5 POMO (buying) days in an 18-day period, offset 1 day.

This is a bit of an exercise in data mining and so picking the best results and assuming they will work as well in the future is dangerous.

Still, with positive results across the board during a period when the market was essentially flat it appears POMO activity by the Fed may have a bullish influence on the stock market. There is an old adage that says “Don’t fight the Fed.” It was written back in the days when interest rates would move up and down. But even with interest rates at 0, fighting the Fed appears to be a bad idea.

In the next week or so I’ll hold a webinar discussion on POMO days to discuss these studies in a little more detail. Also, if there is sufficient interest I may add a chart to the website like the one shown above. For those who would like to read more on POMO days, both the Zerohedge and ETF Prophet sites have published research and information on them as well.

Other than POMO there was little in the way of studies with intermediate-term influence this past week. The pullback was a bit more extreme in terms of consecutive down days than is usually seen in an uptrend. There were some signs of panic early in the week as well. Still there doesn’t appear to be bearish consequences as of yet. The only possible issue as I noted last week is that the number of new highs was lower at the recent peak than at the April peak. As of now that is a small complaint compared to the large amount of bullish evidence.

The market is still in an uptrend. We are in a seasonally strong period for the market. The Nasdaq continues to lead. And the Fed wants to help. I’ll continue to favor the long side and trade extra selectively from the short side.

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

GOOG – @ \$603.29

GOOG – @ \$595.47

GOOG – @ \$583.72

MSFT – @ \$25.81

ABT – @ \$47.66

*ABT – buy 1/3 @ \$46.95 **NEW***

Catapult for ETF’s Trades

None

Broad Market Large Cap CBI – 6 (GOOG-3, MSFT, ABT-2)

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 – buy ¼ index position at \$117.65 LIMIT ON OPEN. If not filled on open, then cancel order and look to buy @ \$117.50 LIMIT ON CLOSE instead. Based on Aggregator signal and short-term outlook above. If I am filled on this one I probably won't look to put on the last ¼ of the index position until at least after the close Monday.

ABT – buy 1/3 position @ \$46.95 limit. New Catapult trade listed above. Those unfamiliar or who would like a review may watch the Catapult & CBI presentation using the link below.

<http://www.quantifiableedges.com/videos/QE20100621.html>

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GOOG(1/3)	11/15/2010	\$603.00	\$583.01	-3.32%		Catapult
SPY(1/4)	11/16/2010	\$118.16	\$118.45	0.25%		Aggregator
GOOG(1/3)	11/16/2010	\$593.39	\$583.01	-1.75%		Catapult
GOOG(1/3)	11/17/2010	\$583.72	\$583.01	-0.12%		Catapult
MSFT	11/17/2010	\$25.81	\$25.12	-2.67%		Catapult
ABT	11/17/2010	\$47.66	\$46.95	-1.49%		Catapult
SPY(1/4)	11/23/2010	\$118.45	\$118.45	0.00%		Aggregator

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.