

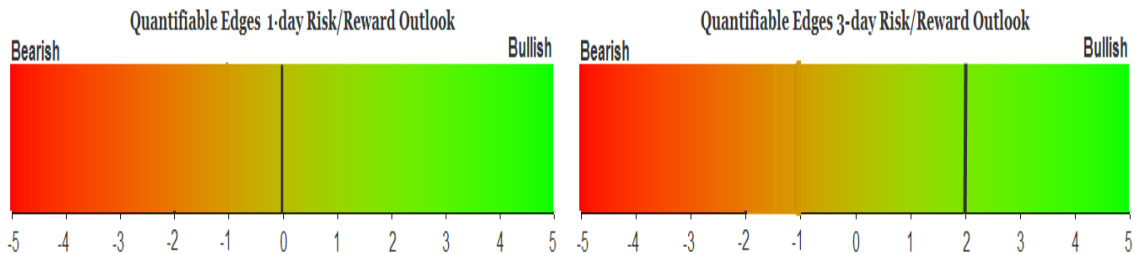
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 29, 2010

Volume 3 Issue 229

Market Overview



Tonight's Research Points

- Friday's unfilled down gap immediately following an unfilled up gap appears to be a short-term negative.
- The Monday after Thanksgiving has historically been a difficult day for the market.
- POMO activity should reach record levels over the next 2 weeks and could provide a boost to the market.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook

The Bottom Line

The market bounce got smacked back a bit on Friday. The studies suggest we still should go higher, but Monday is iffy thanks to seasonality and the SPY pattern over the last 2 days.

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 29, 2010	Unfilled Gap Up then unfilled gap down	1-3 days	Bearish	-1.80%
November 29, 2010	Monday after Thanksgiving Seasonality	1 day	Bearish	
November 26, 2010	Lowest vol 20. SPX up 1% in uptrend	1-2 days	Bearish	-1.60%
November 26, 2010	Up Vol % Rank increases > 85%	1-3 days	Bullish	1.30%
November 24, 2010	2 Unfilled Gaps Down in SPY	1-5 days	Bullish	2.10%
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	
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
Dropped Tonight				
October 18, 2010	SPX up. Issue% and Vol% very low	1-25 days	Bearish	
November 24, 2010	Wed-Fri Thanksgiving Seasonality	2 days	Bullish	

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

The Evidence

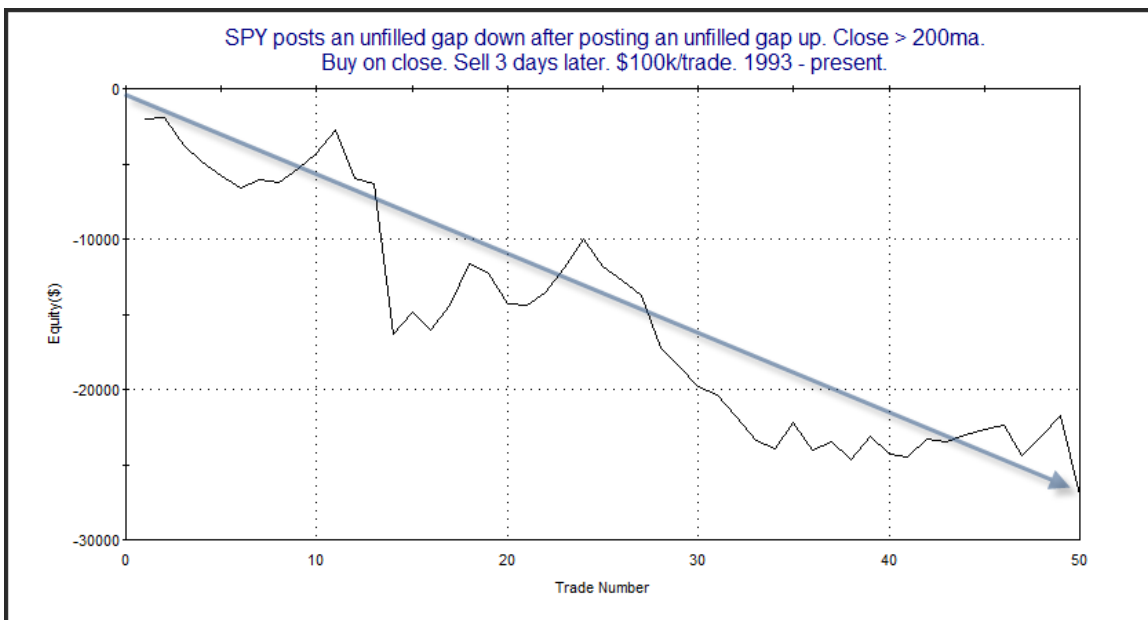
We saw a mix of studies in Thursday night's Letter and the bearish ones won out on Friday. A big gap down only partially filled and the major indices all suffered losses. The SPX lost 0.75%, the Nasdaq fell 0.3% and the Russell 2000 dropped 0.5%. Breadth was strongly negative as the NYSE Up Issues % came in at 33% and the Up Volume % was 17%. Volume fell with many traders on vacation and Friday being a shortened session.

After leaving an unfilled gap up on Wednesday the SPY left and unfilled gap down Friday. Below is a study that looks at similar scenarios during long-term uptrends.

SPY posts an unfilled gap down after posting an unfilled gap up. Close > 200ma.
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
10	-5,931.69	45	20	25	44.44	2,137.34	-1,947.14	1.10	0.88	-131.82
9	-15,338.78	45	19	26	42.22	2,111.54	-2,133.00	0.99	0.72	-340.86
8	-14,889.17	45	19	26	42.22	1,925.43	-1,979.70	0.97	0.71	-330.87
7	-15,771.18	45	18	27	40.00	1,994.33	-1,913.67	1.04	0.69	-350.47
6	-18,498.66	46	20	26	43.48	1,575.28	-1,923.24	0.82	0.63	-402.14
5	-17,710.07	48	20	28	41.67	1,460.53	-1,675.74	0.87	0.62	-368.96
4	-11,617.36	49	21	28	42.86	1,314.46	-1,400.75	0.94	0.70	-237.09
3	-27,037.67	50	20	30	40.00	1,160.22	-1,674.74	0.69	0.46	-540.75
2	-19,546.31	51	22	28	43.14	863.05	-1,376.20	0.63	0.49	-383.26
1	-870.64	51	24	26	47.06	697.46	-677.30	1.03	0.95	-17.07

These results would suggest a short-term bearish edge. Using the 3-day exit strategy I ran an equity curve to see how consistent the edge has been.



Certainly returns have been choppy, but it's again making new lows and the trend down has been in place a very long time. In looking at the Wednesday-Friday unfilled gaps, you'll notice that Wednesday's move up was more powerful as the low on Friday still didn't manage to close Wednesday's opening gap. I added this as a filter to see any possible implications.

SPY posts an unfilled gap down after posting an upfilled gap up. Today's low is above the close of 2 days ago. Close > 200ma. 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
10	-14,749.04	14	3	11	21.43	3,379.67	-2,262.55	1.49	0.41	-1,053.50
9	-18,163.61	14	3	11	21.43	2,997.19	-2,468.65	1.21	0.33	-1,297.40
8	-17,284.40	14	3	11	21.43	2,583.41	-2,275.88	1.14	0.31	-1,234.60
7	-18,635.41	14	2	12	14.29	2,268.60	-1,931.05	1.17	0.20	-1,331.10
6	-19,152.96	14	3	11	21.43	1,286.55	-2,092.06	0.61	0.17	-1,368.07
5	-13,736.62	14	5	9	35.71	1,331.58	-2,266.06	0.59	0.33	-981.19
4	-13,438.98	14	6	8	42.86	1,043.41	-2,462.43	0.42	0.32	-959.93
3	-15,156.47	14	5	9	35.71	1,219.61	-2,361.62	0.52	0.29	-1,082.61
2	-4,569.83	15	8	7	53.33	823.00	-1,593.40	0.52	0.59	-304.66
1	450.16	15	8	7	53.33	836.67	-891.88	0.94	1.07	30.01

Instances are a little low but if anything the fact that Wednesday's gap went unfilled appears to be bearish over the next 2-10 days. At the very least it confirms the results of the previous test.

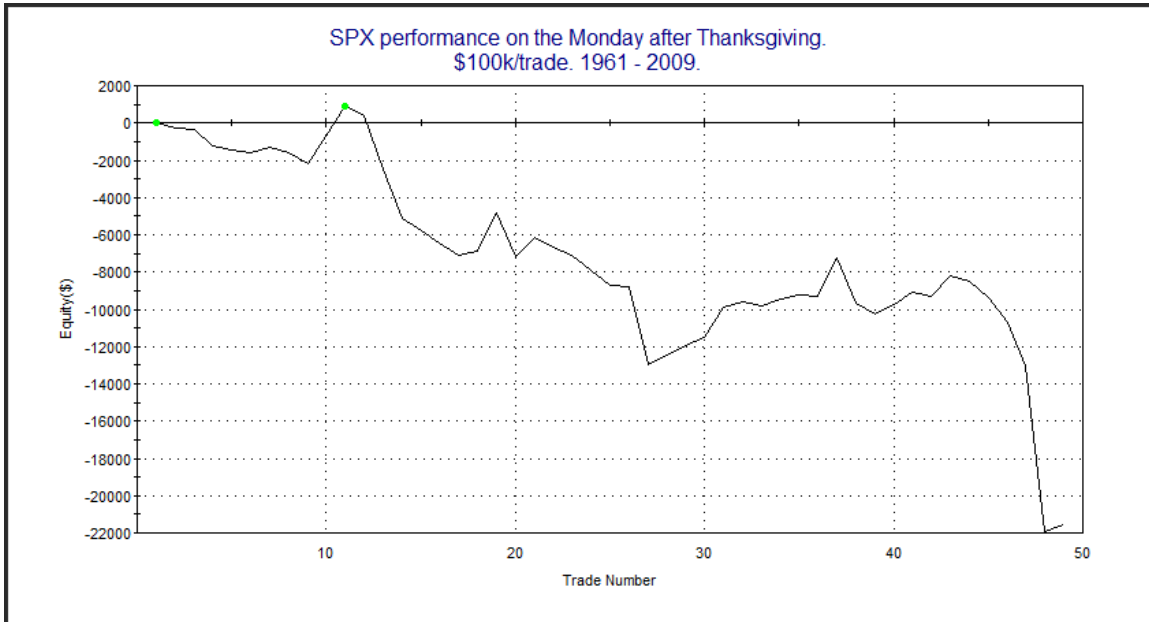
The Quantifinder also identified a study last highlighted in the 11/1/10 subscriber letter. It showed an environmental edge where since the 2009 market bottom down Fridays had been followed by strong Mondays. This edge appears to have weakened significantly in the last several months. Below I've listed all the occurrences back to the end of May.

SPX Mondays after a down Friday. \$100k/trade.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
05/28/10	Buy	\$1,089.41	(1.72%)	\$487.76
06/01/10	Sell	\$1,070.71		(\$1,776.32)
06/04/10	Buy	\$1,064.88	(1.35%)	\$602.64
06/07/10	Sell	\$1,050.47		(\$1,396.86)
07/02/10	Buy	\$1,022.58	0.54%	\$1,932.24
07/06/10	Sell	\$1,028.06		(\$410.31)
07/16/10	Buy	\$1,064.88	0.60%	\$913.26
07/19/10	Sell	\$1,071.25		(\$350.61)
08/06/10	Buy	\$1,121.64	0.55%	\$676.40
08/09/10	Sell	\$1,127.79		(\$64.97)
08/13/10	Buy	\$1,079.25	0.01%	\$310.04
08/16/10	Sell	\$1,079.38		(\$897.92)
08/20/10	Buy	\$1,071.69	(0.40%)	\$919.77
08/23/10	Sell	\$1,067.36		(\$428.73)
10/29/10	Buy	\$1,183.26	0.09%	\$1,054.20
11/01/10	Sell	\$1,184.38		(\$471.24)
11/12/10	Buy	\$1,199.21	(0.12%)	\$682.26
11/15/10	Sell	\$1,197.75		(\$170.98)

I'll see if this reasserts itself in the near future but at this point I'm not inclined to include it among the active studies.

I noted in the 11/22 Subscriber Letter last week when going over Thanksgiving seasonal edges I showed that the Monday after Thanksgiving has struggled historically. Below is a copy of the equity curve shown last week along with comments from that letter.



As you can see while the Monday after has carried a bit of a downside edge for many years, the raw numbers are skewed quite a bit by the almost 9% drop in 2008. Without that the downside edge would appear much more modest. Still, there does appear to be one.

I also looked at how the Monday edge may be affected based on the Wed-Fri action and by Friday's action alone. Results were not so different that I thought they warranted using.

I should also note that the CBI as laid out in the Catapult and CBI section below has remained at either 5 or 6 for 6 days in a row now. Typically readings of this size have a mild upside influence on the market. It's unusual to see them remain at a mildly bullish level like this for an extended period as they now have. Normally the condition will

resolve itself with a quick market bounce or the selling will intensify and the CBI will begin to hit critical levels of 10 or higher. I looked at other instances of this happening in the past. Between 1995 and now there were only 13 other instances where the CBI lingered between 5 and 9 for 6 days in a row. Results following these instances were inconclusive.

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



More bearish studies tonight have reduced the short-term bullish expectations and the green Aggregator line reading. It did still remain above 0 though. 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 also remained 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 remained long at the close.

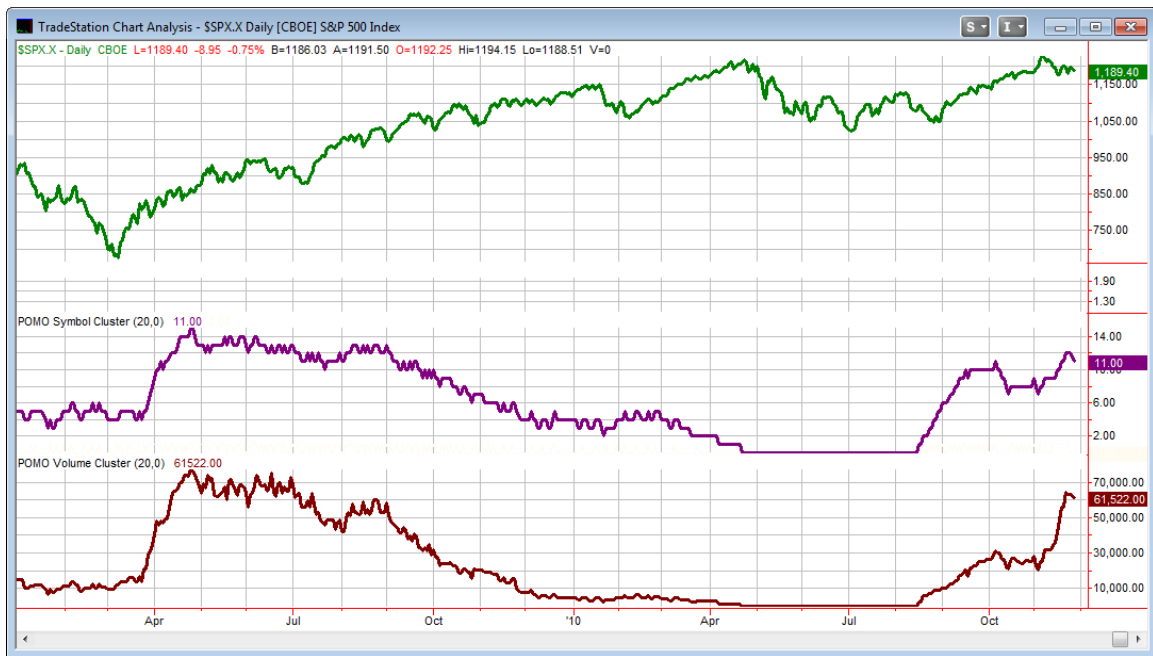
The green Aggregator line is set up to remain positive tomorrow. This could change if strong bearish evidence emerges. With the Tuesday's big drop exiting the Differential

calculation the Differential Pivot is going to drop to 1,183.08. This means unless the SPX loses over 0.5% and closes below this level the Differential line will flip to negative.

Notable is that while the net expectations over the next 3 days are positive, Monday's expectations are actually breakeven. The Aggregator always looks out 3 days. I don't normally trade off the 1-day number but I do show it in the heat map at the top of the Letter. Also worth considering is that the Differential line is set up to zigzag over the next 2 days. If the SPX traded flat on Monday and Tuesday the Differential would show an overbought reading (below 0) on Monday evening and move back to an oversold reading (above 0) Tuesday evening. So I don't want to over react to the potential move in the Differential Monday. I will only look to take profits on part of the position. Since my intermediate-term outlook is so positive I've been looking to hold the other piece a bit longer, and that remains my intention.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/29 – bullish

Last week I discussed the possible effect of POMO Days in some detail. POMO stands for Permanent Open Market Operations and it is how the Fed goes into the open market to buy securities. The net effect of this buying is an influx of cash into the system. It appears a portion of that cash makes its way to the stock market and works as a bullish influence. A “POMO Day” is simply a day where these operations take place. Looking at [the tentative schedule posted on the Fed’s website](#) it appears the next 9 trading days are ALL scheduled POMO days. It also appears the amount of buying will be quite large on most of these days. The chart below is updated from Tuesday night’s letter. The top pane is the S&P 500. The middle pane is the rolling number of days in the last 20 that have been POMO days. The bottom pane is the total amount of money infused into the system over the previous 20 days.



As you can see both measures are already approaching levels as high as were reached during the summer of 2009, which contained the most amount of stimulus ever. Over the next 2 weeks the stimulus provided by both measures (days and \$\$) should exceed those 2009 levels. This should provide a substantially bullish influence over the next several weeks and possibly longer.

From a studies standpoint, there are now 6 intermediate-term studies on the active list. They cover POMO Days, breadth, price patterns, leadership (relative strength), and momentum. All of them are bullish. In fact the only potential issue I’ve noted over the past few weeks 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. European debt and Korean military action could provide additional shocks. These are difficult to quantify though and not something that factors into my decision making. 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 – @ \$46.95

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.

No new entries tonight for me. There are a few long systems triggers on the spreadsheet for those traders looking for more trade ideas.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GOOG(1/3)	11/15/2010	\$603.00	\$590.00	-2.16%		Catapult
SPY(1/4)	11/16/2010	\$118.16	\$118.80	0.54%		Aggregator
GOOG(1/3)	11/16/2010	\$593.39	\$590.00	-0.57%		Catapult
GOOG(1/3)	11/17/2010	\$583.72	\$590.00	1.08%		Catapult
MSFT(1/3)	11/17/2010	\$25.81	\$25.25	-2.17%		Catapult
ABT(1/3)	11/17/2010	\$47.66	\$46.80	-1.80%		Catapult
SPY(1/4)	11/23/2010	\$118.45	\$118.80	0.30%		exit SPX close>1,183.07
ABT(1/3)	11/24/2010	\$46.95	\$46.80	-0.32%		Catapult

Personally I would consider trailing an intraday stop on the 1 lot of SPY and then exiting if broke down below intraday support. Should it happen to continue down and close below the pivot I would then buy some or all of it back. This is a little tricky to try and execute via a nightly letter. For now I'll just use the exit on close as described above. I may look to trail a stop tomorrow via an intraday update. I won't be looking for another entry at least until tomorrow night's letter is published.

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