

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 2, 2011

Volume 4 Issue 22

Market Overview



Tonight's Research Points

- The weak volume on the strong breadth move to a new high is a bit of a short-term concern.
- 2 unfilled up gaps and a new 50-day high suggest there should be more upside over the next 3-4 days.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

The strong move higher the last 2 days now has the SPX overbought and the Aggregator neutral. I'll wait until there is a more pronounced edge before looking to take on new positions.

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				
February 2, 2011	Strong breadth, new high but weak vol	1-3 days	Bearish	-1.00%
February 2, 2011	2 Unfilled Up Gaps & 50-day high	1-3 days	Bullish	0.90%
February 1, 2011	Unfilled gap up inside day	1-2 days	Bearish	
February 1, 2011	< 10ma in uptrend entering 1st of month	1-5 days	Bullish	
February 1, 2011	Sweet spot bounce	1-6 days	Bullish	3.20%
January 31, 2011	10-high to 10-low in 1 day	1-3 days	Bearish	
January 27, 2011	100-day high on a Fed Day	1-6 days	Bullish	1.70%
January 27, 2011	Unfilled gap up & close > open Fed Day	1-5 days	Bearish	-2.60%
January 21, 2011	1st close < 10ma in over 25 days	1-11 days	Bullish	3.60%
January 21, 2011	SPY gap down & partial revers fr 5-low	1-10 days	Bullish	3.20%
Active - Long Term				
January 21, 2011	SPY 1st close < 10ma in over 25 days	1-20 days	Bullish	
January 19, 2011	SPX 20-day high. Vol 20-day high.	int term	Bullish	
December 16, 2010	2 Hindenburg Signals	1-50 days	Bearish	
December 9, 2010	SPX & TNX 50-day highs	1-50 days	Bearish	
November 22, 2010	High number of POMO Days recently	int term	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	

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

The Evidence

The market followed up Monday's solid bounce with a very strong start to February. The major indices all finished substantially higher. The SPX rose 1.7%, then Nasdaq was up 1.9% and the Russell 2000 gained 2.3%. Breadth was very strongly positive as the NYSE Up Issues % came in at 81% and the Up Volume % was 88%. Volume dropped slightly from Monday's levels.

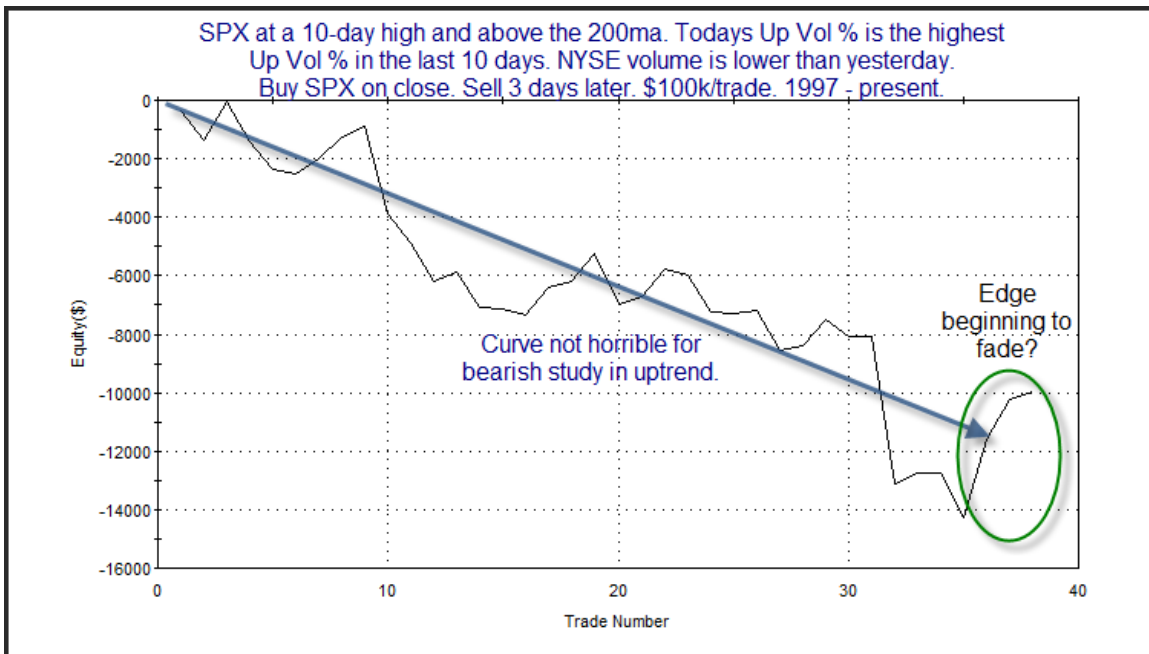
With the market hitting new highs, Quantifinder studies were a bit mixed tonight.

While breadth was strong, the decline in volume was not encouraging. Below is a study from the 12/2/10 Subscriber Letter that examined other instances of new highs being made on strong breadth but weak volume. I have updated the results.

SPX at a 10-day high and above the 200ma. Today's Up Vol % is the highest Up Vol % in the last 10 days. NYSE volume is lower than yesterday. Buy SPX 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
10	-4,460.81	35	18	17	51.43	1,704.94	-2,067.63	0.82	0.87	-127.45
9	-7,437.12	35	21	14	60.00	1,396.49	-2,625.96	0.53	0.80	-212.49
8	-11,364.86	35	19	16	54.29	1,253.63	-2,198.99	0.57	0.68	-324.71
7	-18,649.54	35	19	16	54.29	969.48	-2,316.86	0.42	0.50	-532.84
6	-14,858.35	36	19	17	52.78	768.04	-1,732.42	0.44	0.50	-412.73
5	-9,511.92	37	20	17	54.05	717.86	-1,404.06	0.51	0.60	-257.08
4	-8,480.74	37	18	19	48.65	762.92	-1,169.12	0.65	0.62	-229.21
3	-9,980.45	38	17	21	44.74	726.78	-1,063.60	0.68	0.55	-262.64
2	-5,270.38	38	20	18	52.63	527.40	-878.80	0.60	0.67	-138.69
1	-2,229.41	38	19	19	50.00	393.66	-510.99	0.77	0.77	-58.67

The stats table seems to suggest a bit of a downside edge. The edge appears to be weakening though. I also updated the 3-day equity curve below.



I have some concern about the recent string of moves higher. This definitely merits keeping an eye on. Still, the curve doesn't yet seem so out of whack that I would eliminate the study from consideration.

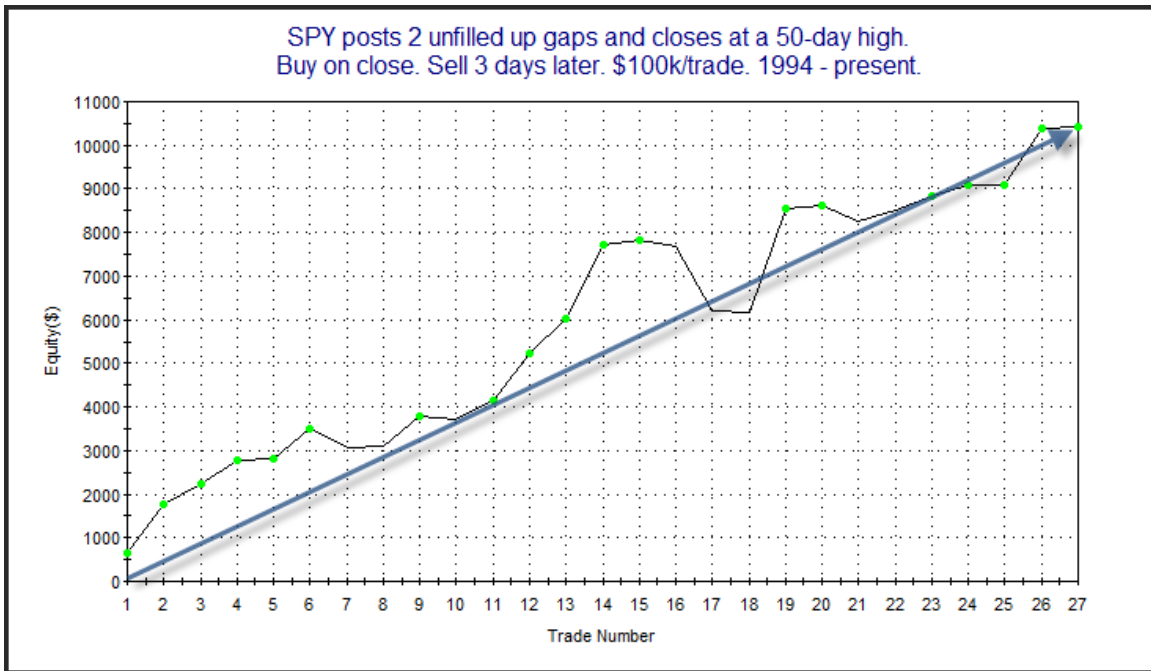
And though volume created a bit of a concern, the price action over the last 2 days triggered a bullish study last reviewed in the 12/23/10 letter. It looked at performance following 2 consecutive unfilled up gaps and a close at a new 50-day high. I have updated the results below.

**SPY posts 2 unfilled up gaps and closes at a 50-day high.
Buy on close. Sell X days later. \$100k/trade. 1994 - 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	7,722.82	27	19	8	70.37	931.81	-1,247.69	0.75	1.77	286.03
4	11,451.39	27	22	5	81.48	826.86	-1,347.89	0.61	2.70	424.13
3	10,430.86	27	21	6	77.78	616.08	-417.82	1.47	5.16	386.33
2	7,573.03	27	20	6	74.07	536.88	-527.44	1.02	3.39	280.48
1	440.69	31	17	14	54.84	304.40	-338.16	0.90	1.09	14.22

29 of 31 instances (94%) posted a close above the entry price at some point in the next 4 days.

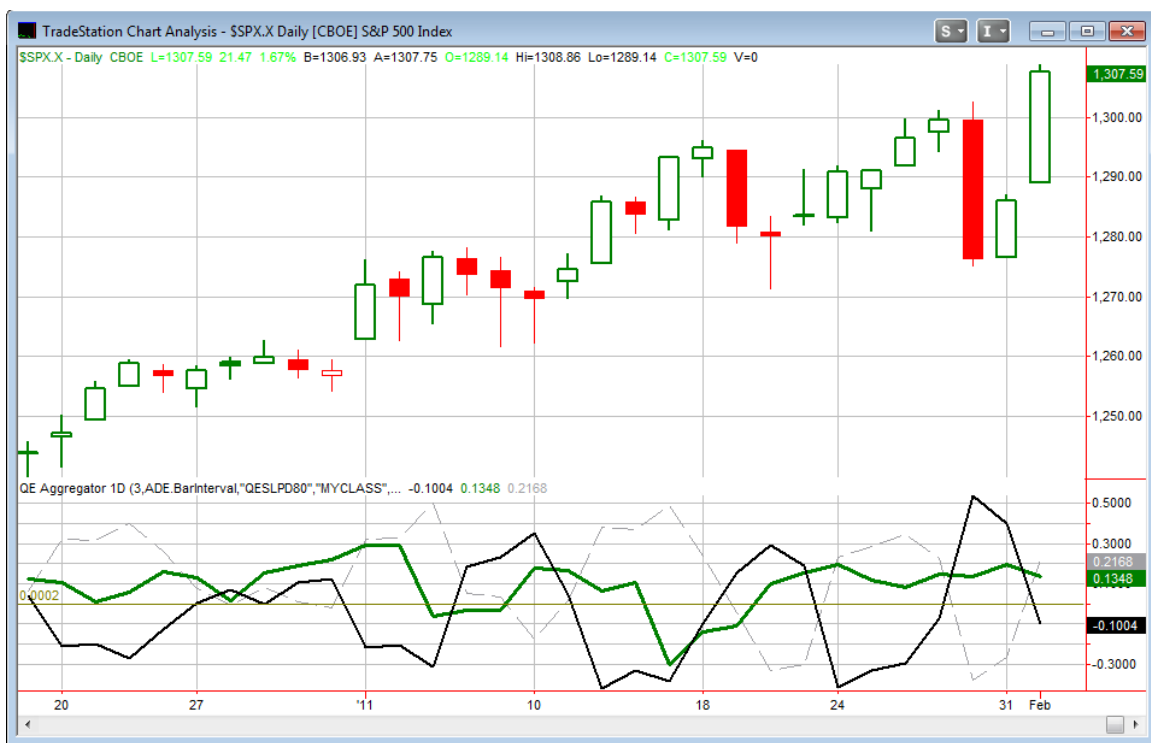
The size of the move isn't huge, but the consistency is very strong over the next 3-4 days. Below is a look at the equity curve using a 3-day exit strategy.



The strong steady upslope is encouraging. This study has also been added to the active list.

I should note quickly that there were a few studies that appeared in the Quantifinder related to the Up Volume % Bounded. They should not have triggered and I am looking into why they did.

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



The green Aggregator line didn't move much, dropping just slightly. It is still well above 0. The positive value means the net expectation from the Active Studies List is for upside over the next few days. Meanwhile the black Differential line dropped sharply and is now below 0. The negative value means the SPX has outperformed expectations over the last few days. So net expectations are for upside but the SPX has outperformed recent expectations. This is considered a neutral configuration. A neutral configuration is evident on the chart whenever both lines are on opposite sides of zero. Due to this the Aggregator System changed to flat at the close.

The green Aggregator line is set up to remain above 0 on Tuesday. Of course this could change if strong bearish evidence emerges. Meanwhile the Differential Pivot will be 1,280.50. This is over 2% below Tuesday's close. For the Differential line to move back above 0, it will take a drop of at least this much in the SPX. It appears the most likely scenario on Wednesday would be for another neutral configuration. Of course a big move or some strong studies could change that.

One other thing I should note is that while expectations over the next few days are for a move higher, net expectations for just Wednesday are for very slight downside. This is why the 1-day risk/reward outlook at the top of the letter is at minus-one instead of zero. The time frame is too short for me to be interested in a swing trade. About the only way I would consider using that information is perhaps selling into a gap higher for a day trade (or shorter). Incidentally I did check the Master the Gap site, and it appears a gap higher may provide favorable shorting odds based on Scott Andrews criteria. He also showed some research at the beginning of his video tonight suggesting gaps could have a high probability of filling tomorrow since we have had 2 unfilled up gaps in a row. Below is a link to that video.

http://www.masterthegap.com/public/Probability_Trading_Video_Large_gap_up_in_the_UH_zone_on_the_first_day_of_the_month_plus_research_on_fading_gaps_that_follow_2_successive_unfilled_up_gaps.cfm

From a swing standpoint I am back to neutral and awaiting the next opportunity. While the Aggregator nailed this move the last 2 days, the trade ideas tracked in the subscriber letter barely missed being filled, which was a bit disappointing. Of course subscribers can always check out the Quantifinder and Systems pages as we approach the close if they want to get an idea of how the short-term outlook is likely to shake out. And even though the letter missed this bounce, the trade ideas did have a solid month in January. None were huge winners but all 6 that were tracked did close positive.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/31 - mildly bullish

The intermediate-term outlook is basically unchanged from last week. No new studies with long-term implications appeared and with the short-term outlook quite lengthy tonight, I decided not to make a big fuss of the intermediate-term.

Bulls still have POMO, trend, and momentum on their side, while the bears hopes continue to hinge on breadth and perhaps bond action. At this point the selloff is just one day. It was strong and violent though, and the action this upcoming week could provide some strong hints.

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.

Current Open Trade Ideas

None

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