

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

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February 3, 2011

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## **Market Overview**



## **Tonight's Research Points**

- Very light volume pullbacks from 50-day highs suggest a downside edge over the next 1-6 days or so.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

## ***Short-term Outlook***

### ***The Bottom Line***

The net expectations are still bullish but the market remains overbought. This leaves the Aggregator configuration neutral and me awaiting a better risk/reward setup.

*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>				
February 3, 2011	Pullback from 50-high on 10-low vol	1-6 days	Bearish	-1.80%
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	< 10ma in uptrend entering 1st of month	1-5 days	Bullish	
February 1, 2011	Sweet spot bounce	1-6 days	Bullish	3.20%
January 27, 2011	100-day high on a Fed Day	1-6 days	Bullish	1.70%
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%
<b>Active - Long Term</b>				
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	
<b>Dropped Tonight</b>				
January 31, 2011	10-high to 10-low in 1 day	1-3 days	Bearish	
February 1, 2011	Unfilled gap up inside day	1-2 days	Bearish	
January 27, 2011	Unfilled gap up & close > open Fed Day	1-5 days	Bearish	-2.60%

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

### ***The Evidence***

I barely traded today as I spent the day battling another winter storm. This one complete with snow, then ice, then rain, then back to ice. Perhaps there were a lot of other traders doing the same thing, or perhaps they were just content to hand-sit after yesterday's buying spree. Whatever the reason, market action seemed to come to a bit of a halt on Wednesday. After gapping down it chopped sideways for most of the day. The major indices finished modestly lower. The SPX and Russell 2000 lost 0.3% and the Nasdaq dropped 0.1%. Breadth was negative as the NYSE Up Issues % came in at 48% and the Up Volume % was just 35%. Total NYSE volume dried up to the lowest level in weeks.

More than anything it was the light volume that appeared most notable. 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 has a good chance of deepening. Today's mild pullback in the SPX occurred on the lightest NYSE volume in over 2 weeks. This triggered a study from the 11/9/10 Subscriber Letter. I have updated the study below.

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.

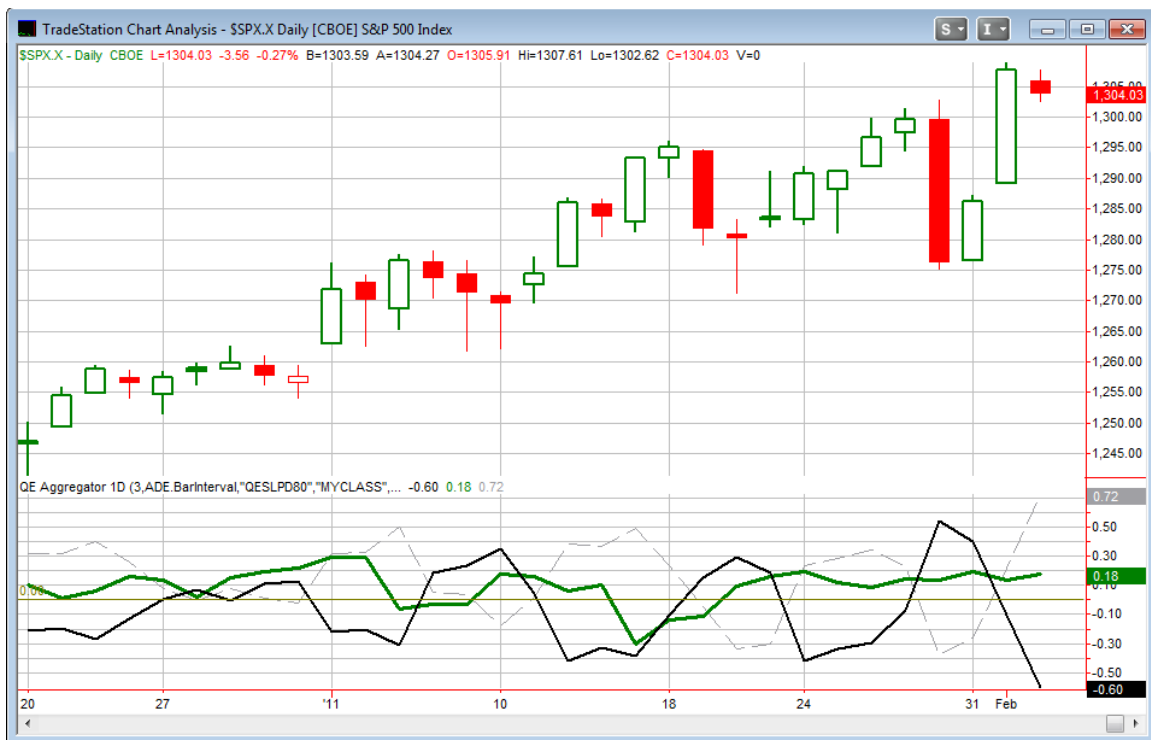
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-23,542.55	57	30	27	52.63	1,737.82	-2,802.86	0.62	0.69	-413.03
9	-20,395.67	57	29	28	50.88	1,770.38	-2,562.02	0.69	0.72	-357.82
8	-30,991.06	57	27	30	47.37	1,490.76	-2,374.72	0.63	0.56	-543.70
7	-38,446.56	57	26	31	45.61	1,342.16	-2,365.90	0.57	0.48	-674.50
6	-38,725.24	58	25	33	43.10	1,165.24	-2,056.25	0.57	0.43	-667.68
5	-26,889.09	59	27	32	45.76	967.59	-1,656.69	0.58	0.49	-455.75
4	-21,658.89	61	30	31	49.18	879.83	-1,550.12	0.57	0.55	-355.06
3	-5,160.35	62	33	29	53.23	902.34	-1,204.75	0.75	0.85	-83.23
2	-2,064.34	62	31	31	50.00	801.38	-867.97	0.92	0.92	-33.30
1	-4,864.02	62	31	31	50.00	545.50	-702.40	0.78	0.78	-78.45

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.



While readings became more extreme the Aggregator chart configuration remained the same. A bearish study was added to the active but 3 bearish studies expired. This left the green Aggregator line 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 continued to drop and is now well 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 remained flat at the close.

The green Aggregator line is set up to remain above 0 on Thursday. Of course this could change if strong bearish evidence emerges. Meanwhile the Differential Pivot will be 1,291.97. This is almost 1% below Wednesday's close. For the Differential line to move back above 0, it will take a drop of at least this much in the SPX. So as it stands, without strong movement or very compelling studies the Aggregator configuration is likely to remain neutral on Thursday.

The mild 1-day bearish edge I noted last night did play out today. It would have been difficult to capture but traders can also look to apply knowledge of probabilities to keep

them out of bad trades. Even if a short opportunity doesn't avail itself, extra caution from the long side could mean not taking possible long breakout trades that would have failed. There are many ways to use information. And avoiding bad trades is just as important as capturing good ones.

I'm still in "wait and see" mode. I don't believe in putting money at risk without an edge and I don't feel there is much of one right now. That won't last long so I'll exercise a little patience and see what tomorrow brings.

***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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