

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 14, 2012

Volume 5 Issue 30

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Short	100% Short SPY	Short	Flat

## Tonight's Research Points

- A 20-day high followed by an unfilled gap down followed by an unfilled gap up has historically suggested a downside inclination over the next few days.

## *Short-term Outlook*

### *The Bottom Line*

There is still a large amount of short-term bearish evidence and now the SPX is modestly overbought. This means the Aggregator is suggesting a short-side edge. I will look to take advantage of it with a short position. I will keep the size small though since there are intermediate-term forces working against the short.

*Summary of Recent Active Studies (see Letters from listed dates for details)*

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
February 14, 2012	8-day Avg Closing Range > 75%	1-6 days	Bearish	-1.90%
February 13, 2012	8-day Avg Closing Range > 75%	1-2 days	Bearish	-1.40%
February 13, 2012	< 1% drop from 50-high. Bad breadth.	1-2 days	Bearish	-1.90%
February 13, 2012	60-day low SPY range > 200ma	1-6 days	Bearish	-2.15%
February 10, 2012	SPX up VIX up 2 days. SPX 50-high.	1-3 days	Bearish	-1.40%
February 9, 2012	QE Buying Power Index System Short	1-5 days	Bearish	
February 7, 2012	Low vol drop from 50-high	1-6 days	Bearish	
February 7, 2012	Unfill Gap Up 20-high then unfill gap dn	1-6 days	Bearish	
<b>Active - Long Term</b>				
February 6, 2012	Up Issues % > 75% 2 of 3. 10 high.	1-16 days	Bullish	4.70%
February 2, 2012	50-high then 5-day consolidation	1-10 days	Bullish	2.30%
February 1, 2012	Golden Cross	int term	Bullish	
January 31, 2012	SPY 1st close < 10ma in over 25 days	1-20 days	Bullish	4.70%
January 17, 2012	Nasdaq leading SPX	int term	Bullish	
December 5, 2011	POMO activity flat to negative	int term	Bearish	
October 19, 2011	FTD on strong breadth/20day high	int term	Bullish	
<b>Dropped Tonight</b>				
February 6, 2012	Up Issues % > 75% 2 of 3. 10 high.	1-6 days	Bullish	2.60%
February 9, 2012	SPX 50-high. VIX up > 2.5%.	1-3 days	Bearish	

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

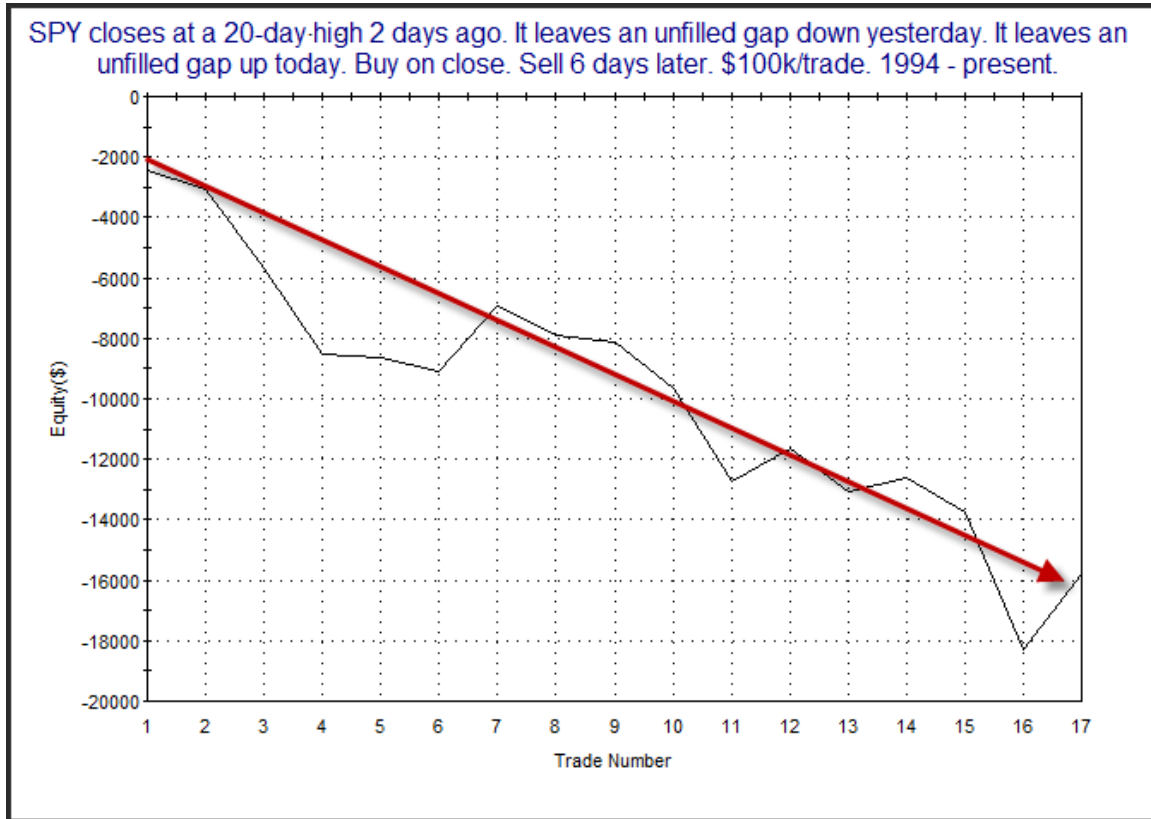
**The Evidence**

Upside momentum is trumping the bearish inclinations suggested by so many studies over the past few days. The major indices all rebounded from Friday and posted nice gains. The SPX was up 0.7%, the Nasdaq rose 1.0% and the Russell 2000 gained 1.4%. Breadth was strongly positive as the NYSE Up Issues % came in at 73% and the Up Volume % was 76%. Total NYSE volume dipped from Friday's level.

Action in SPY the last couple of days has been interesting as it has left large unfilled gaps in both directions. The study below is from the 12/12/11 subscriber letter. It looks at other instances where you had a 20-day closing high, then an unfilled gap down, and then an unfilled gap up. All results are updated.

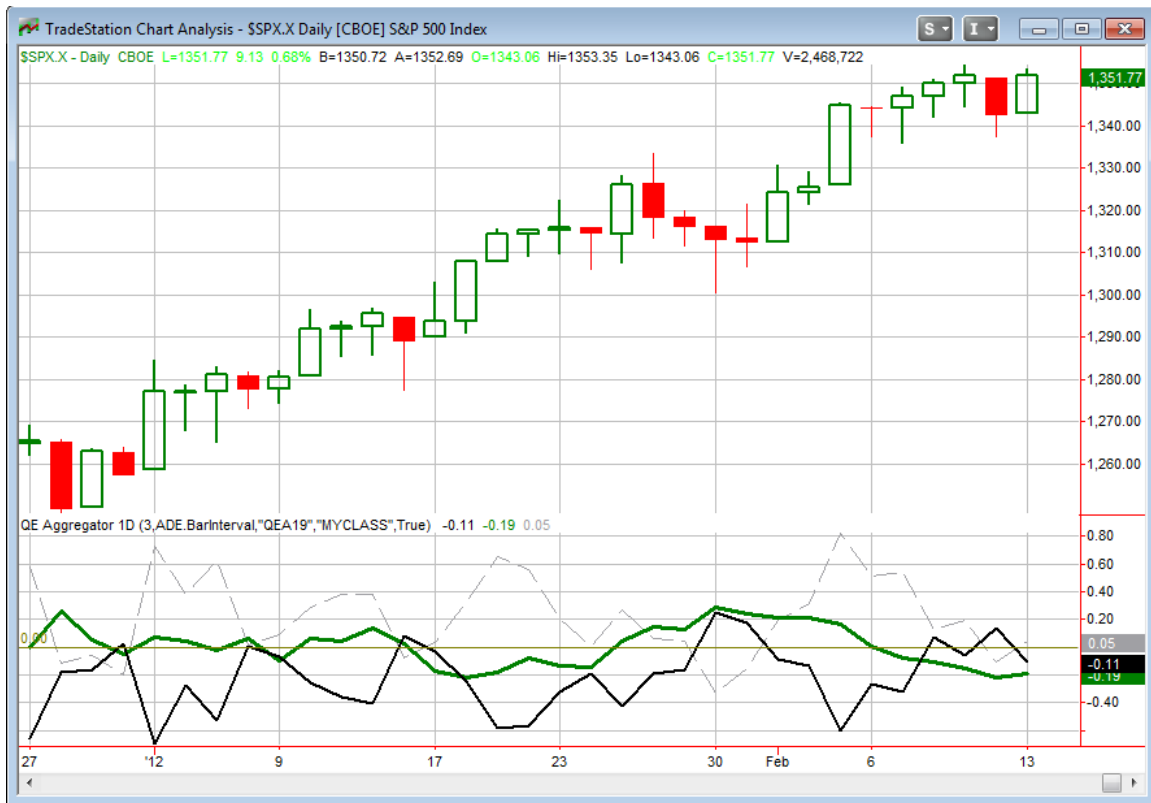
SPY closes at a 20-day high 2 days ago. It leaves an unfilled gap down yesterday. It leaves an unfilled gap up today. Buy on close. Sell X days later. \$100k/trade. 1994 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
6	-15,817.46	17	4	13	23.53	1,558.85	2,489.06	-1,696.38	-4,567.68	0.92	0.28	-930.44
5	-13,437.80	17	6	10	35.29	743.77	1,638.76	-1,790.04	-3,536.78	0.42	0.25	-790.46
4	-5,002.11	17	8	9	47.06	1,096.80	2,184.76	-1,530.72	-3,068.91	0.72	0.64	-294.24
3	-4,803.31	17	7	10	41.18	1,070.90	1,700.60	-1,229.96	-3,417.83	0.87	0.61	-282.55
2	-3,045.42	17	6	11	35.29	1,109.47	2,150.80	-882.02	-2,510.75	1.26	0.69	-179.14
1	-1,710.00	17	6	11	35.29	583.52	1,361.70	-473.74	-1,459.12	1.23	0.67	-100.59

These results seem to suggest a mild downside edge over the next 6 days. Below is a profit curve that assumes a 6-day holding period.



Despite the last instance the decline appears fairly steady. This serves as confirmation of the downside edge.

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



Tonight's studies didn't do much to change the value of the green Aggregator line. It remained negative. Readings below 0 mean net expectations from the Active List are for downside over the next few days. Meanwhile, the black Differential Line continues to gyrate around 0 and is now back to negative. A negative Differential reading means the SPX has outperformed expectations over the last few days. So net expectations are bearish and the SPX is overbought versus recent expectations. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below 0. This caused the Aggregator System to change from flat back to short at the close.

Based on the current active studies, expectations are again scheduled to remain negative on Tuesday. This is unlikely to change but could if strong bullish evidence emerges. Meanwhile, the Differential Pivot will be 1,347.27 on Tuesday. This is only about 0.3% below Monday's close. So it won't take much of a decline to turn the Differential Line back to positive and trigger a quick end to the Aggregator short signal.

Short-term evidence continues to pile up in favor of the bears – and to a degree that is quite unusual when the market is making new intermediate-term highs. Pullbacks have been brief and shallow lately and the market is only moderately overbought, so the opportunity here does not appear huge. Additionally, the QE Buying Power Index moved out of negative territory on Friday and is set to hit 3 at Tuesday's close. In general, trying

to short when the QE Buying Power Index is strong has been a difficult thing to do. All this suggests to me that a conservative approach to the short side is prudent. I will look to take advantage of a possible dip tomorrow, but I will keep the position size small and if profits materialize, I will be quick to take them.

### A brief note on QE Buying Power Index Swing System exits

In the QE Buying Power Index webinar for subscribers a few weeks ago I laid out an exit strategy in which I would exit a trade before a mean reversion took place if 1) the QE Buying Power Index had turned against the position, and 2) the trade was over 5 days old. The reason I used the time-based requirement is that in studies it was found that the QE Buying Power Index readings generally appear to have a strong impact over the next 4-6 days. In the webinars I did last week for non-subscribers I did not get into detail with regards to the time-based criteria. I did note that a move in the QE Buying Power Index could be reason to exit a trade.

In reality, whether you gave the trade a certain amount of time or not seems to have made very little difference since 2008. This can be seen in the table below, which requires the trade be at least “X” days old before considering exiting based on a change in the QE Buying Power Index.

QE Buying Power System Exit Optimization. Exit triggered on QE Buying Power Index move (to >0 for shorts or <= 0 for longs) and trade at least X days old.												
QE POMO trade: daysin	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	71,982.34	49	40	9	81.63	2,278.40	8,004.64	-2,128.21	-4,354.77	1.07	4.76	1,469.03
9	72,371.69	49	40	9	81.63	2,278.40	8,004.64	-2,084.94	-4,838.16	1.09	4.86	1,476.97
8	75,605.96	50	41	9	82.00	2,228.87	8,004.64	-1,753.07	-3,849.08	1.27	5.79	1,512.12
7	75,937.04	50	40	10	80.00	2,278.40	8,004.64	-1,519.92	-2,776.80	1.50	6.00	1,518.74
6	78,607.65	50	40	10	80.00	2,278.40	8,004.64	-1,252.85	-2,799.05	1.82	7.27	1,572.15
5	76,547.44	50	40	10	80.00	2,278.40	8,004.64	-1,458.88	-3,249.00	1.56	6.25	1,530.95
4	76,940.66	50	40	10	80.00	2,278.40	8,004.64	-1,419.55	-2,750.44	1.61	6.42	1,538.81
3	73,991.44	51	40	11	78.43	2,244.67	8,004.64	-1,435.95	-4,441.44	1.56	5.68	1,450.81
2	74,732.12	51	40	11	78.43	2,189.49	8,004.64	-1,167.96	-2,750.44	1.87	6.82	1,465.34
1	77,682.96	51	42	9	82.35	2,117.99	8,004.64	-1,252.50	-2,750.44	1.69	7.89	1,523.20

With such little difference in the results over the first few days it is really a matter of preference whether you elect to give the trade some time to work or not. My personal inclination is to give it a few days, which is why I did decide to use time as a factor. There is no “right” answer here, and traders could consider other factors (such as the Aggregator) into their exit decisions if they elect to trade signals based on the QE Buying Power Index. More details on the system and the QE Buying Power Index may be found by clicking on the presentation link on the videos page.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 2/13 – bullish***

The intermediate-term outlook was last updated in the 2/13/12 letter. Below is a link to that letter.

[2012-02-13 QE Subscriber Letter.pdf](#)

**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.*

***SPY – short 1/4 index position @ \$135.36 limit.*** Based on the short-term outlook above.  
***If this order is filled, then I will look to cover on a close of \$134.85 or lower. (This is approximately where the SPX would reach its Differential Pivot.)***

**Current Open Trade Ideas**

*None.*

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