

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 26, 2012

Volume 5 Issue 122

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Long	100% Long XIV	Flat	Long

## Tonight's Research Points

- 2 strong down days of 1.5% in a week's time are typically enough to warrant a short-term bounce.
- SPY's unfilled gap down following an unfilled gap up is not encouraging – especially since the down day was bigger.

## Short-term Outlook

### The Bottom Line

The Aggregator is still bullish. Friday's bounce registered a quick fail on Monday, but I am viewing it as an opportunity to get some long exposure that I missed out on Friday.

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

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
June 26, 2012	1.5% loss 2x in week > 200ma	1-3 days	Bullish	2.25%
June 26, 2012	Gap down < 2ago. Gap up yest. > 200	1-3 days	<b>Bearish</b>	<b>-1.80%</b>
June 25, 2012	Sweet spot bounce from 1.75% drop	1-5 days	Bullish	3.00%
June 22, 2012	SPY closes at 5-day low 1st time > 2 wks	1-4 days	Bullish	1.60%
<b>Active - Long Term</b>				
June 25, 2012	Nasdaq leading SPX	int term	Bullish	
June 18, 2012	POMO modestly bullish	int term	slight bull	
June 13, 2012	FTD with modest breadth & vol	int term	<b>Bearish</b>	
June 7, 2012	90% up day on 3rd day of rally	1-14 days	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
<b>Dropped Tonight</b>				
<b>June 25, 2012</b>	<b>SPY unfill gap up. Lower high. &gt; 200</b>	<b>1-3 days</b>	<b>Bearish</b>	<b>-1.50%</b>

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

***The Evidence***

Monday was bad from the start. And though the selloff hit bottom around noon, it never rose much off the lows. The SPX finished down 1.6%, the Nasdaq lost 2.0%, and the Russell 2000 fell 1.7%. Breadth was very strongly negative as the NYSE Up Issues % came in at 14% and the Up Volume % was 11%. Total NYSE volume finished at the lightest level in over a week.

So I am on vacation and mentioned in my note to subscribers that I would prefer the market do nothing interesting and chop sideways while I am away. As often happens with the market, “hoping” does no good. Monday easily qualified as “interesting” action, and there was a decent amount to sort through in the Quantifinder. The studies below highlight the most important observations.

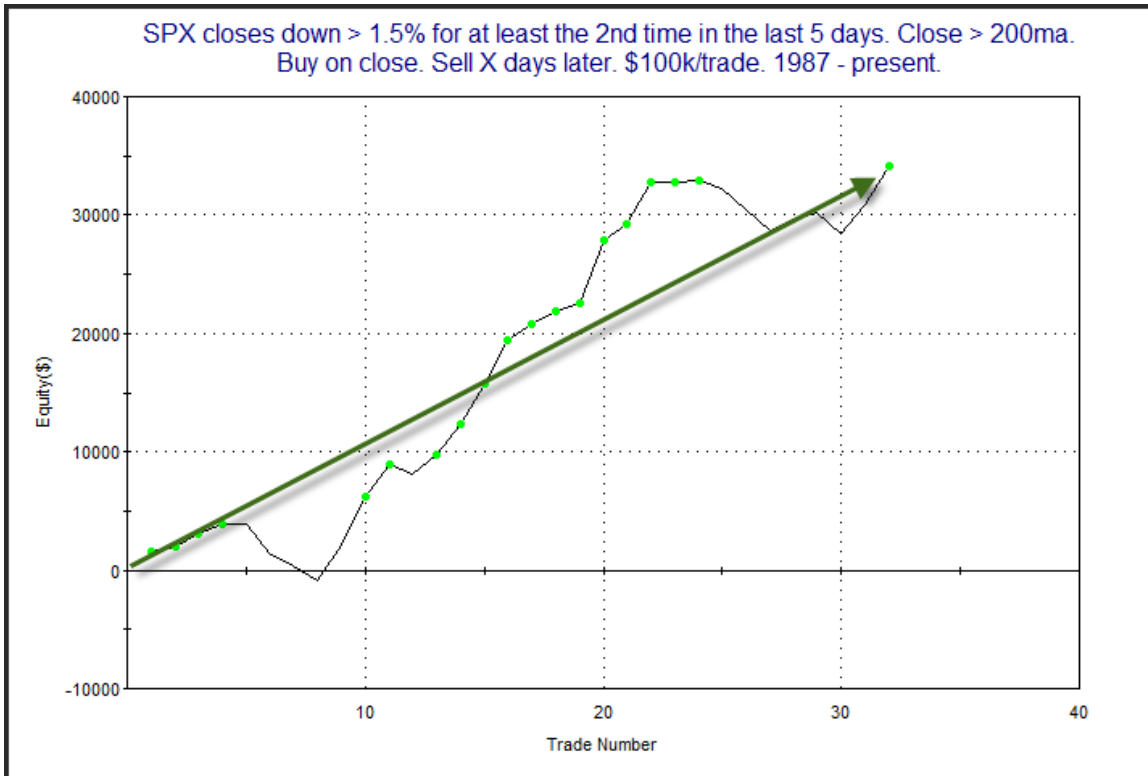
This first one was last reviewed in the 5/5/10 subscriber letter. It examines performance following 2 strong down days within a week. Results are updated.

SPX closes down > 1.5% for at least the 2nd time in the last 5 days. Close > 200ma.  
Buy on close. Sell X days later. \$100k/trade. 1987 - 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
5	34,580.49	30	20	10	66.67	2,734.69	7,070.28	-2,011.34	-6,368.04	1.36	2.72	1,152.68
4	38,710.33	31	22	9	70.97	2,489.58	5,187.49	-1,784.49	-4,917.36	1.40	3.41	1,248.72
3	34,131.53	32	23	9	71.88	1,990.95	5,339.18	-1,295.59	-2,662.66	1.54	3.93	1,066.61
2	29,156.17	35	22	13	62.86	1,966.41	4,809.66	-1,085.00	-3,863.25	1.81	3.07	833.03
1	24,535.64	38	29	9	76.32	1,309.54	5,117.46	-1,493.45	-5,829.81	0.88	2.83	645.67

88% of instances have closed above the entry price at some point in the next week.

The suggestion by the stats table is that this kind of extreme action while the market is above the 200ma is often short-term exhaustive and that a bounce typically ensues. Below is the equity curve using a 3-day holding period.



It is a little choppier than I would prefer, but we are again at new profit highs and the general slope seems good enough to warrant consideration. In the 5/3/10 letter I filtered this study further. Those results seems to provide extra confirmation of the upside edge.

In that letter I looked for the SPX to have made a 20-day intraday high in the last 5 days. I have updated that table below as well.

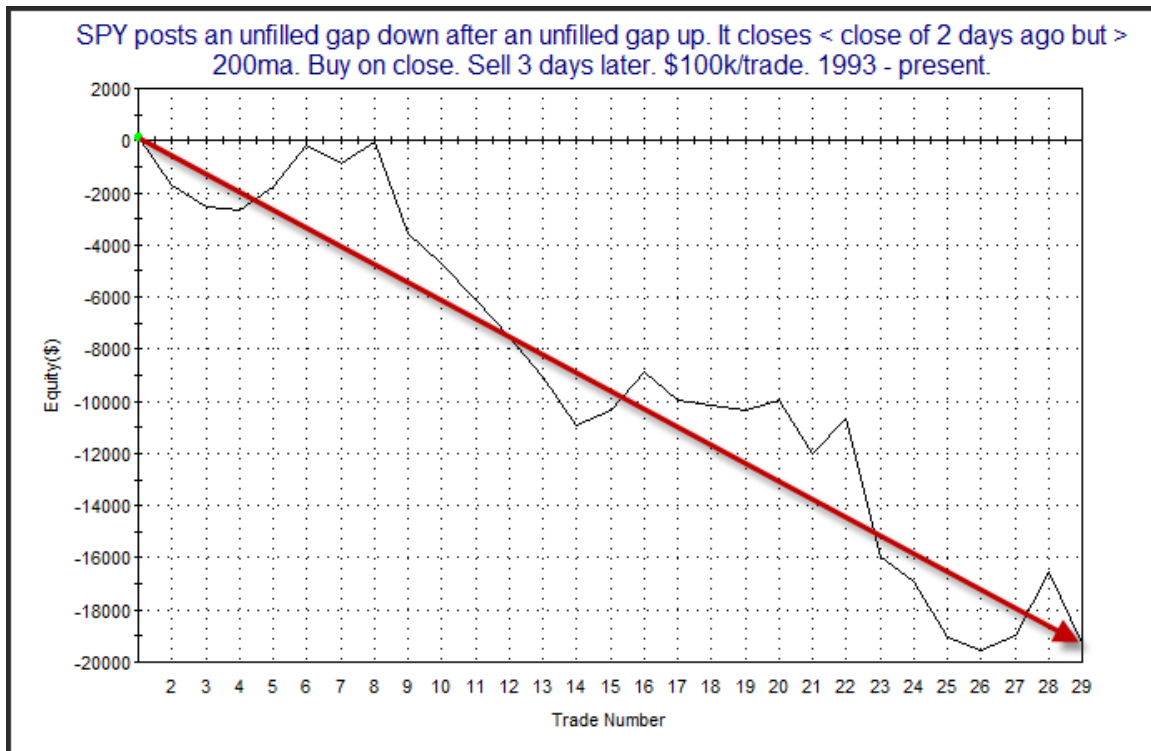
SPX closes down > 1.5% for at least the 2nd time in the last 5 days. Close > 200ma. SPX made a 20-day intraday high within the last 5 days. Buy on close. Sell X days later. \$100k/trade. 1987 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % 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
5	14,858.50	10	8	2	80.00	2,856.82	5,460.84	-3,998.01	-6,368.04	0.71	2.86	1,485.85
4	13,377.25	10	7	3	70.00	2,888.22	5,187.49	-2,280.09	-4,917.36	1.27	2.96	1,337.72
3	17,667.37	10	8	2	80.00	2,530.34	5,339.18	-1,287.69	-1,748.88	1.97	7.86	1,766.74
2	14,848.96	10	8	2	80.00	2,045.63	3,591.28	-758.03	-1,099.56	2.70	10.79	1,484.90
1	9,428.77	10	9	1	90.00	1,299.25	2,547.74	-2,264.50	-2,264.50	0.57	5.16	942.88
<b>All 10 instances have closed above the entry price at some point in the next 3 days.</b>												

Instances are a little low, but it does act as nice confirmation of the 1<sup>st</sup> study. I have decided to include the first study above on the short-term active list.

Not all the Quantifinder observations were bullish though. The study below was last seen in the 5/12/11 letter. It looks at other times while above the 200ma that an unfilled gap up was followed by an unfilled gap down and the gap down day was more powerful.

SPY posts an unfilled gap down after an unfilled gap up. It closes < close of 2 days ago but > 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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-5,502.98	27	11	16	40.74	1,356.01	3,445.05	-1,276.20	-3,791.20	1.06	0.73	-203.81
4	-5,338.14	27	11	16	40.74	1,377.38	3,174.85	-1,280.59	-4,926.08	1.08	0.74	-197.71
3	-19,298.02	29	10	19	34.48	1,018.98	2,463.47	-1,551.99	-5,321.00	0.66	0.35	-665.45
2	-16,494.09	29	10	18	34.48	822.35	1,754.40	-1,373.20	-3,893.00	0.60	0.33	-568.76
1	-206.06	29	14	14	48.28	479.02	1,325.15	-493.74	-1,564.50	0.97	0.97	-7.11

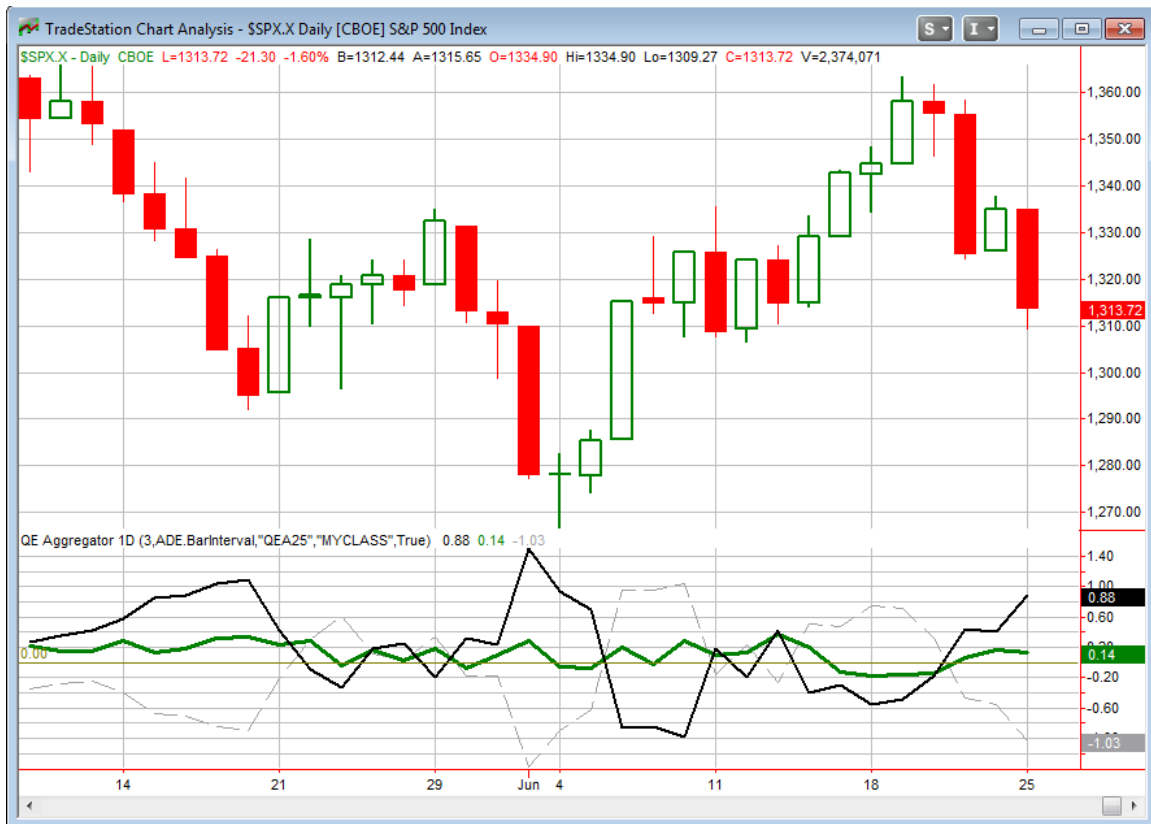
These results suggest a short-term bearish edge. Below is the equity curve using a 3-day exit strategy.



Certainly returns have been choppy but it is again near new lows and the downtrend has been in place for a long time.

Monday giving back Friday's gains was also concerning to me in another way. In last night's letter I showed a very compelling study that looked at "sweet spot" bounces which made up 25% - 75% of the losses of a drop of 1.75% or more (while > 200ma). There were 33 other instances since 1961 and results showed a strong inclination to bounce over the next few days. I revisited that study tonight to examine other times the Day 1 reaction was so poor. Monday was easily the worst Day 1 of the entire lot. No other instances suffered a Day 1 loss of > 1%, and no other instances reversed down and closed below the close of 2 days ago. Monday's action puts it on an island, which isn't just lonely, but also suggests elevated risk.

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



With tonight's studies factored in the green Aggregator line remained positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is now strongly above zero. This means the SPX is short-term oversold versus expectations. So net expectations are bullish and the SPX is oversold versus recent expectations. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This meant the Aggregator System remained long at the close. This was indicated as likely on the systems page before the bell.

Based on the current active studies expectations are set to remain positive Tuesday. Of course this could change if more bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,322.23 on Tuesday. A close at or above this level would cause the Differential Line to flip back below 0, indicating the SPX has moved from oversold to overbought. It would require a gain of about 0.65% to get there.

The Aggregator is bullish, but there are clearly some short-term risks. My biggest concern is the uniqueness of the action over the last 3 days. On Friday I was looking for a small long entry and the gap up left me unfilled. A small lot is about all I would want here so I'll look to put that same size back on Tuesday. Details are in the Trade Ideas section near the bottom of the letter.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 6/25 – slightly bullish***

Intermediate-term outlook was last updated in the 6/25 letter. A link is below:

[2012-06-25 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 – buy ¼ index position @ \$131.50 limit.*** This is \$0.18 above the closing price. It is a bit more aggressive entry than I often do for the first lot, but I would like to get some exposure and am viewing this as a “gift” entry after missing my entry on Friday. So if we gap up again Tuesday, I won’t require a complete fill.

### **Current Open Trade Ideas**

*None.*

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