

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 31, 2012

Volume 5 Issue 146

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Flat	50% Long XIV	Flat	Flat

Tonight's Research Points

- Monday's low-volume pullback from the high was somewhat concerning.
- A big drop on Tuesday could set up a bullish scenario.

Short-term Outlook

The Bottom Line

I'm still neutral, but a strong selloff ahead of the Fed on Tuesday would inspire me to get long.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
July 30, 2012	SPY 2 unfilled up gaps & 50 high	1-3 days	Bullish	1.00%
July 30, 2012	SPX 50-day high on 90% up vol	1-5 days	Bullish	2.60%
Active - Long Term				
July 30, 2012	SPX 50-day high on 90% up vol	1-50 days	Bullish	
July 16, 2012	POMO modestly bullish	int term	Bullish	
June 13, 2012	FTD with modest breadth & vol	int term	Bearish	
February 1, 2012	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.

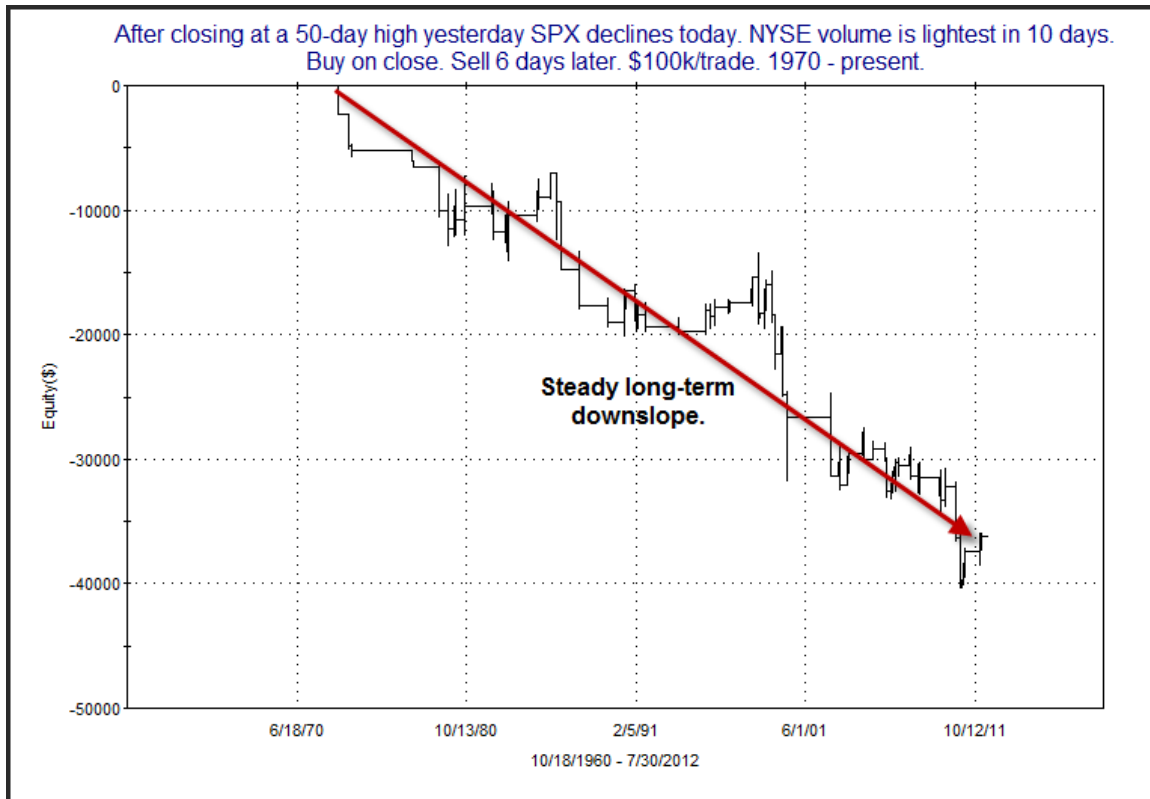
The Evidence

After 2 strong up days to end last week, Monday saw a quiet pullback. The SPX fell less than 0.1%, the Nasdaq dropped 0.4% and the Russell 2000 declined 0.6%. Breadth was mixed as the NYSE Up Issues % came in at 47.6% and the Up Volume % was 50.3%. Total NYSE volume came in very light.

While the pullback in the SPX was mild, very low volume is a bit of a concern. It caused the study below to trigger. I last showed this study in the 1/25/12 subscriber letter. Results shown here are all updated.

After closing at a 50-day high yesterday SPX declines today. NYSE volume is 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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-18,624.60	59	32	27	54.24	1,782.89	5,104.00	-2,802.86	-6,121.74	0.64	0.75	-315.67
9	-15,065.39	60	32	28	53.33	1,770.98	3,955.23	-2,562.02	-6,236.87	0.69	0.79	-251.09
8	-25,525.97	60	30	30	50.00	1,523.85	3,521.07	-2,374.72	-6,661.66	0.64	0.64	-425.43
7	-35,789.68	60	28	32	46.67	1,344.09	3,732.48	-2,294.50	-7,193.64	0.59	0.51	-596.49
6	-36,194.63	61	28	33	45.90	1,130.77	2,563.47	-2,056.25	-5,426.99	0.55	0.47	-593.35
5	-25,227.42	62	29	33	46.77	964.01	2,273.04	-1,611.62	-4,288.68	0.60	0.53	-406.89
4	-20,345.26	64	31	33	48.44	901.80	2,457.84	-1,463.67	-4,263.60	0.62	0.58	-317.89
3	-3,326.51	65	36	29	55.38	878.09	2,169.48	-1,204.75	-3,726.24	0.73	0.90	-51.18
2	-837.56	65	34	31	52.31	766.75	2,328.05	-867.97	-4,049.40	0.88	0.97	-12.89
1	-3,560.74	65	34	31	52.31	535.70	2,235.13	-702.40	-3,068.81	0.76	0.84	-54.78

The first few days don't show much of an edge, but once you get out 6-7 days there appears to be a possible downside inclination. To confirm this I took a look at the equity curve. In this case I decided to show time on the x-axis rather than instances to demonstrate how consistent the edge has been over the years.



For a study without strongly lopsided statistics, the steadiness is impressive. With no real edge appearing for the first several days, I decided not to include this study on the active list. Still, I believe it is worth keeping in mind.

As I mentioned last night, Wednesday is a Fed Day. Fed Days have historically performed very well. This has been especially true if the day before the Fed Day the market struggles. One simple and effective stat I consider on the day before a fed day is the closing range value. Times when SPY has closed in the bottom 25% of its daily range the Fed Day has done substantially better. As a general rule, the worse the finish, the larger the upside edge on the Fed Day. Of course Wednesday is also the first trading day of August. I've documented numerous times that since the late 80s the first trading day of the month has had a bullish tendency. So I wondered how the market has performed on days that a Fed Day has coincided with the first trading day of month. There have only been six instances over the time frame I examined. I've listed them all below.

SPX performance when 1st trading day of the month is also a Fed Day.
\$100k/trade. 1988 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
10/31/88	Buy	\$278.96	0.04%	\$146.78
11/01/88	Sell	\$279.06		(\$340.10)
09/30/91	Buy	\$387.86	0.34%	\$436.90
10/01/91	Sell	\$389.19		\$0.00
06/30/92	Buy	\$408.13	1.16%	\$1,161.30
07/01/92	Sell	\$412.87		\$0.00
01/31/95	Buy	\$470.42	(0.00%)	\$493.96
02/01/95	Sell	\$470.40		(\$239.56)
06/30/98	Buy	\$1,133.86	1.30%	\$1,293.60
07/01/98	Sell	\$1,148.56		(\$1.76)
10/31/05	Buy	\$1,206.98	(0.35%)	\$29.52
11/01/05	Sell	\$1,202.76		(\$436.24)

Early indications suggest a possible upside edge, but really we have too few instances to draw any conclusions without overwhelmingly lopsided results. Still, I thought this was interesting enough to share.

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



Very little change tonight. The green Aggregator Line remained squarely above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is still extremely far below 0. This means the SPX is very short-term overbought versus expectations. So net expectations are bullish but the SPX is extremely overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. This meant the Aggregator System remained flat at the close.

Based on the current studies, expectations are slated to remain bullish on Tuesday. Of course that could change if bearish evidence emerges. The Differential Pivot will be 1,367.67 on Tuesday. This is about 1.3% below Monday's close. So it will take a fairly large drop on Tuesday, ahead of Wednesday's August 1 Fed Day, to relieve the overbought condition.

While it is unlikely to happen, strong down closes preceding Fed Days have been bullish, and the same goes for strong down closes on the last trading day of the month. So if the SPX does happen to drop that much, I'll be a buyer. Otherwise, I don't see a big edge right now, so I'll continue to exercise patience and sit on the sidelines.

Intermediate-term Outlook (2 weeks – 2 months)– updated 7/30 – bullish

The intermediate-term outlook was last updated in the 7/30 letter. Link below:

[2012-07-30 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 ½ size index position (2 normal sized lots) on SPX close of 1,367.67 or lower.** Based on the short-term outlook above. I will definitely be out of at least 1 of these lots before Wednesday’s Fed announcement, and may get out as early as Wednesday’s open.*

Current Open Trade Ideas

None

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