

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 16, 2012

Volume 5 Issue 158

Market Overview



Signals Overview

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

Tonight's Research Points

- Low SPY volume at a SPY price high has often been followed by weakness.
- The small move up after 2 down days provides mild evidence that Monday could struggle.

Short-term Outlook

The Bottom Line

Story hasn't changed. This non-action just isn't creating a compelling edge. I'll remain sidelined.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
August 16, 2012	SPX down 2 then up < 0.2%	1 day	Bearish	
August 16, 2012	SPY 50-high on 20-low vol	1-2 days	Bearish	-1.10%
August 15, 2012	SPY up. VIX up > 6%.	1-3 days	Bullish	1.60%
August 15, 2012	SPY 50-high then 5-day inside range	1-3 days	Bullish	1.10%
August 14, 2012	3/10 Offset HV < 0.3 4th day in row	1-4 days	Bullish	
Active - Long Term				
August 16, 2012	SPY 50-high on 20-low vol	1-10 days	Bearish	
August 15, 2012	SPY 50-high then 5-day inside range	1-10 days	Bullish	
August 10, 2012	SPX & TNX 50-day highs.	1-20 days	Bearish	
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	
Dropped Tonight				
August 14, 2012	Up 5 in row to 50-high, then down	1-2 days	Bullish	
August 14, 2012	Multiple days of very low vol near high	1-2 days	Bearish	

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

The Evidence

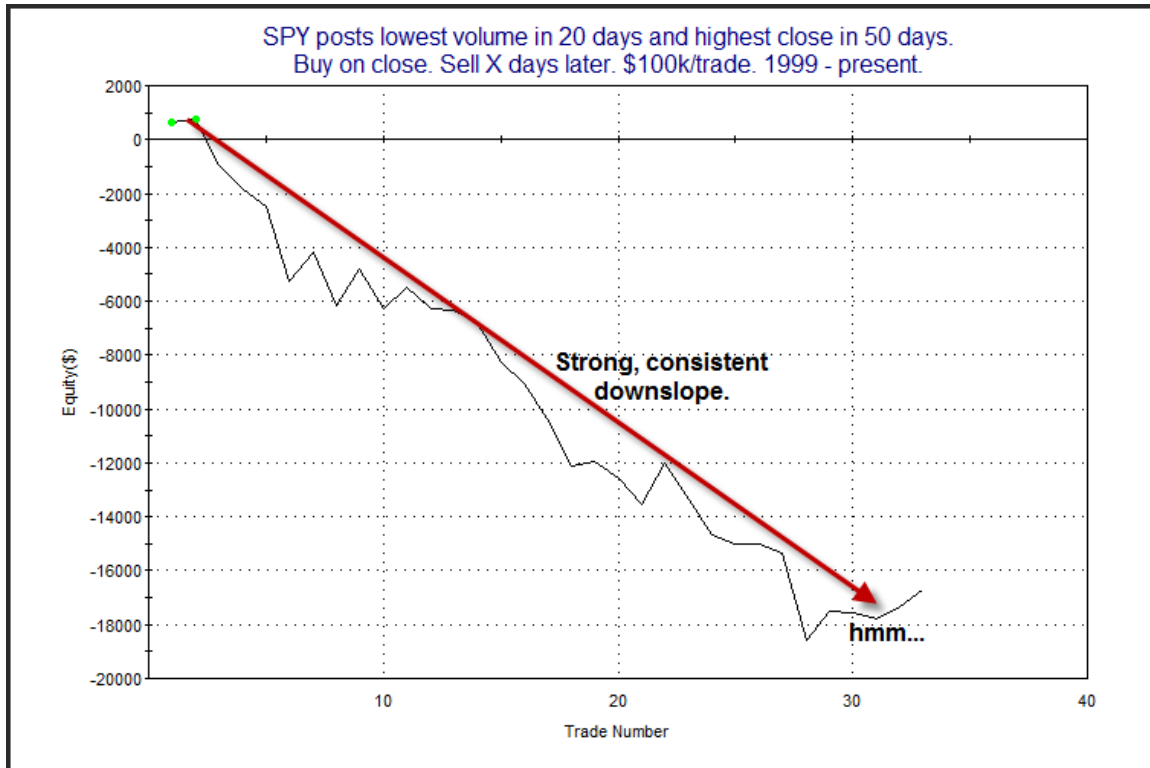
The market is officially asleep. Today the SPX gained 0.1%, the Nasdaq rose 0.5%, and the Russell 2000 actually moved some with a 0.9% gain. Breadth was moderately positive as the NYSE Up Issues % and Up Volume % both came in at 62%. Volume was once again very small.

I'm shocked that I have anything to talk about, but I do.

In the 8/7/12 Subscriber Letter just over a week ago, I showed a study that demonstrated the bearish inclinations suggested by very low SPY volume. That study triggered again tonight, and I have updated it once again below.

SPY posts lowest volume in 20 days and highest close in 50 days. Buy on close. Sell X days later. \$100k/trade. 1999 - 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	-26,571.04	26	10	16	38.46	973.42	1,756.85	-2,269.07	-5,617.30	0.43	0.27	-1,021.96
9	-21,444.61	26	12	14	46.15	850.79	2,134.16	-2,261.01	-4,893.46	0.38	0.32	-824.79
8	-14,067.83	28	12	16	42.86	1,358.56	3,010.86	-1,898.16	-4,522.35	0.72	0.54	-502.42
7	-19,135.42	29	13	16	44.83	883.53	2,046.06	-1,913.83	-4,833.14	0.46	0.38	-659.84
6	-14,561.33	30	13	17	43.33	857.93	1,820.52	-1,512.62	-4,350.58	0.57	0.43	-485.38
5	-9,811.28	32	15	17	46.88	971.76	2,209.52	-1,434.57	-4,272.30	0.68	0.60	-306.60
4	-12,999.90	32	16	16	50.00	801.10	1,725.46	-1,613.59	-4,141.80	0.50	0.50	-406.25
3	-16,780.94	32	12	20	37.50	797.33	1,883.84	-1,317.45	-4,581.36	0.61	0.36	-524.40
2	-16,692.96	33	10	22	30.30	789.68	1,512.64	-1,117.71	-3,265.65	0.71	0.32	-505.85
1	-5,043.18	34	13	21	38.24	527.67	1,470.70	-566.81	-1,935.36	0.93	0.58	-148.33

The numbers here suggest a solid downside edge over the next few days. A good part of the edge plays out in the 1st 2 days. So below is a curve for a 2-day holding period.



The curve has basically been a consistent downslope for a long time. But the last few trades haven't panned out as well. At this point, you are only looking at 3 instances that didn't comply (out of the last five), so I'm not going to get too worked up about this little upturn yet. But I'm taking notice, and will suspend this study if this type of action continues.

Another interesting study that triggered was from the 4/23/12 subscriber letter. In it I looked to see whether there was a substantial difference in performance following a small move *down* after two down days versus a small move *up* after two down days. I decided to revisit the whole study below.

First let's consider what happens after two down days are followed by a third lower close, but that third close is a drop of less than 0.2%.

SPX declines for exactly the 3rd day in a row. Today's drop is < 0.2%.
Buy on close. Sell next day's close. \$100k/trade. 1999 - present.

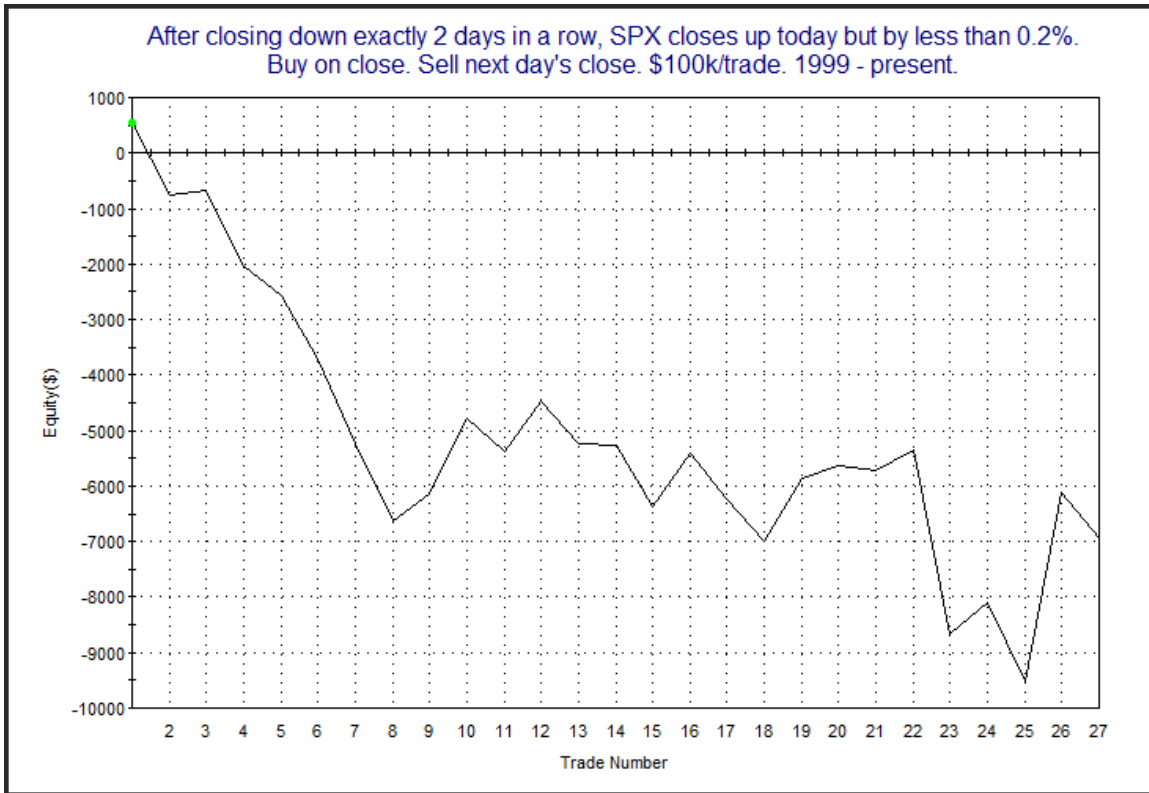
TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$9,851.02	Profit Factor	1.91
Gross Profit	\$20,659.07	Gross Loss	(\$10,808.05)
Total Number of Trades	33	Percent Profitable	69.70%
Winning Trades	23	Losing Trades	10
Even Trades	0		
Avg. Trade Net Profit	\$298.52	Ratio Avg. Win:Avg. Loss	0.83
Avg. Winning Trade	\$898.22	Avg. Losing Trade	(\$1,080.81)
Largest Winning Trade	\$2,286.08	Largest Losing Trade	(\$2,452.26)

Results here appear to suggest a decent upside edge.

Now let's look at times like the present where two down days were followed by an up day, but that up day rose less than 0.2%.

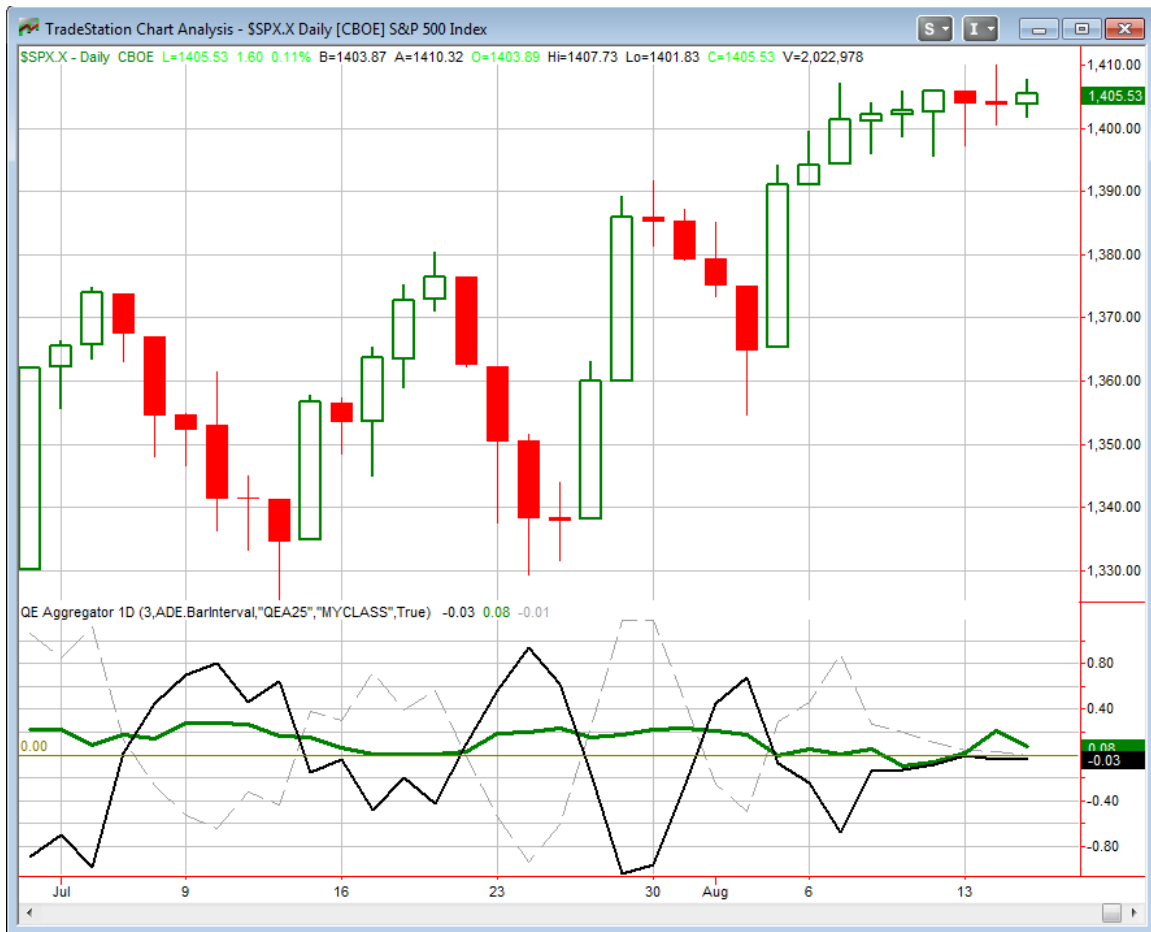
TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	(\$6,947.82)	Profit Factor	0.59
Gross Profit	\$10,026.37	Gross Loss	(\$16,974.19)
Total Number of Trades	27	Percent Profitable	40.74%
Winning Trades	11	Losing Trades	16
Even Trades	0		
Avg. Trade Net Profit	(\$257.33)	Ratio Avg. Win:Avg. Loss	0.86
Avg. Winning Trade	\$911.49	Avg. Losing Trade	(\$1,060.89)
Largest Winning Trade	\$3,390.64	Largest Losing Trade	(\$3,325.38)

As you can see, results here suggest a small down day is substantially different than a small up day. While not overwhelming, the odds here appear to favor a down day Thursday. Lastly, here is the profit curve.



I don't love this curve, but I suppose it is good enough to merit some small consideration, and have therefore listed the study on the Short-Term Active List above.

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



Despite the bearish studies tonight the green Aggregator Line held 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 a very small amount below 0. This means the SPX is mildly overbought versus recent expectations. So net expectations are bullish but the SPX is a little overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. This left the Aggregator System signal neutral.

Based on the current studies expectations will remain positive on Thursday. This could change if additional bearish evidence emerges. The Differential Pivot will be 1,402.23 on Thursday. This is about 0.2% below Wednesday's close. So a close below this level would move the SPX from overbought to oversold and flip the Differential Line.

As long as the market does nothing, I probably won't do anything either. I just don't see a sizable edge, and intend to wait until I do.

The video below drive the patience point home. Charles Kirk, who is one trader and educator I hold in very high regard, tweeted this link out this evening. It is a clip from

Boardwalk Empire (which I have yet to ever watch). It sums up greatly what I have been talking about lately with regards to exercising patience until you have a sizable edge. (Some foul language.)

<http://www.michaelcovel.com/2012/08/06/the-definition-of-an-asymmetric-bet/>

Intermediate-term Outlook (2 weeks – 2 months)– updated 8/13– slightly bullish

The intermediate-term outlook was last updated in the 8/13 letter. A link is below:

[2012-08-13 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.

[None tonight.](#)

Current Open Trade Ideas

None.

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