

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 6, 2012

Volume 5 Issue 213

Market Overview



Signals Overview

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

Tonight's Research Points

- The SPX price pattern the last 2 days suggests a failure by the bears. Bulls have a chance to take charge over the next few days.
- The election presents a large event risk for Wednesday.

Short-term Outlook

The Bottom Line

Estimates remain strong and the market is still oversold. If not for the election I would be holding firm until at least Wednesday. As is I will take partial profits if the market closes up again on Tuesday.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
November 6, 2012	Double big reversal days > 200 < 10	1-4 days	Bullish	1.60%
November 1, 2012	End of month < 10ma and > 200ma	1-5 days	Bullish	2.20%
October 25, 2012	20-low reversal	1-6 days	Bullish	
October 24, 2012	4 lower lows. 20-day low.	1-8 days	Bullish	
Active - Long Term				
October 25, 2012	20-low > 200ma on a Fed Day	1-9 days	Bullish	
October 24, 2012	SPY dn 1% and SOX up	1-20 days	Bullish	
October 15, 2012	Breadth not diverging at top	int term	Bullish	
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
October 25, 2012	2x outside days	1-5 days	Bullish	
November 5, 2012	Down on Employment Day > 200	1 day	Bullish	

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

The Evidence

It looked like the market was headed to new multi-month lows this morning but it turned around and finished positive. The SPX gained 0.2%, and the Nasdaq and the Russell 200 each rose 0.6%. Breadth finished just above breakeven as the NYSE Up Issues % was 50.1% and the Up Volume % came in at 54%. Total NYSE volume fell for the 3rd day in a row.

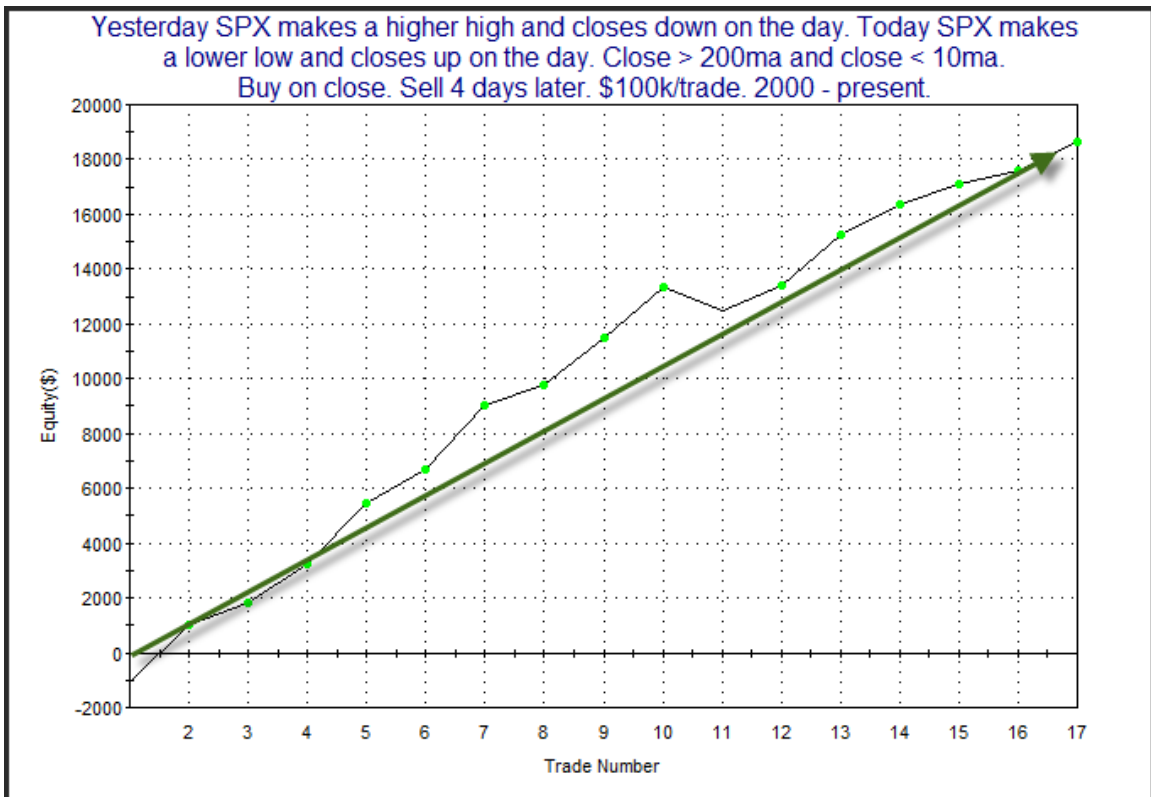
On Friday the bulls tried to make a move higher and failed, making for a higher high and a lower close. On Monday the opposite happened. The bears failed in their attempt at a move lower. In the 3/3/11 Subscriber Letter I looked at two-day moves like this. I found results to be substantially different based on whether the market is near the top or the bottom of its short-term range. When the pattern occurs in the lower end of the short-term range it has been consistently bullish over the next 4-5 days. This can be seen in the below test, which I have updated.

Yesterday SPX makes a higher high and closes down on the day. Today SPX makes a lower low and closes up on the day. Close > 200ma and close < 10ma.
Buy on close. Sell X days later. \$100k/trade. 2000 - 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	23,191.94	17	13	4	76.47	1,802.08	3,344.64	-58.78	-150.48	30.66	99.64	1,364.23
4	18,642.29	17	15	2	88.24	1,373.43	2,345.07	-979.61	-1,089.90	1.40	10.52	1,096.61
3	7,662.65	17	12	5	70.59	1,120.85	2,224.32	-1,157.51	-3,490.90	0.97	2.32	450.74
2	5,652.42	17	11	6	64.71	1,173.62	2,967.00	-1,209.57	-2,226.32	0.97	1.78	332.50
1	3,342.29	17	9	8	52.94	868.14	1,712.28	-558.87	-1,180.27	1.55	1.75	196.61

The only instance that did NOT post a close above the entry price at some point in the next week was the 1st one on 1/25/00.

Odds strongly favor a move higher and the win/loss ratio and profit factors are very impressive. Instances are a little lower than I would prefer but the evidence is so lopsided it appears worthy of consideration. Below is an equity curve using a 4-day exit strategy to see how the edge has played out over time.



The strong, steady rise is impressive.

While not applicable to the current situation, I also updated the results when the pattern occurred and the SPX closed above the 10ma. This table is also from the 3/3/11 letter and has also been updated.

Yesterday SPX makes a higher high and closes down on the day. Today SPX makes a lower low and closes up on the day. Close > 200ma and close > 10ma. Buy on close. Sell X days later. \$100k/trade. 2000 - 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	-7,514.79	34	19	15	55.88	876.44	1,657.22	-1,611.14	-3,770.60	0.54	0.69	-221.02
4	-12,374.20	36	18	18	50.00	835.11	1,984.54	-1,522.56	-4,575.48	0.55	0.55	-343.73
3	-8,765.32	36	17	19	47.22	905.06	1,918.21	-1,271.12	-2,726.23	0.71	0.64	-243.48
2	-2,694.25	37	20	17	54.05	522.64	1,844.90	-773.36	-2,362.36	0.68	0.80	-72.82
1	-1,751.45	37	18	19	48.65	464.69	1,063.14	-532.42	-1,275.95	0.87	0.83	-47.34

We see here that the winning % is a tossup and the downside risk has outsized the upside reward. In this case implications are not bullish. With the 50% winning % and the fairly mild average decline I'm not sure I'd call it bearish either.

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



The green Aggregator line remains well 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 also moderately positive. This means the SPX is oversold versus recent expectations. So net expectations are bullish and the SPX is oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This caused the Aggregator system to remain long at the close.

Based on the current studies, expectations are set to remain bullish again on Tuesday. This is unlikely to change unless very bearish evidence emerges. The Differential Pivot will be 1,420.44 on Monday. This is 1.3% above Monday's close. So it would take a close higher of at least this much to move the Differential Line into negative territory, signifying that SPX has moved from oversold to overbought. That is a tall order for 1 day. And it is even taller on an election day where prices may be frozen waiting for results. So the signal will likely persist for another day or so.

I like the long side but we certainly have some additional risk here. I don't know of a consistent election reaction. I do know that it could be sharp. On Wednesday after the election 4 years ago the SPX lost over 5%. Of course volatility was much higher in November of 2008. An equivalent drop on Wednesday would be much more muted. I'll probably hold part of my position through the election, but if we get an up day tomorrow, I'll take some of the position off just to reduce risk into a big news event.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/5– bullish

The intermediate-term outlook was last updated in the 11/5 letter. Link below:

[2012-11-05 QE Subscriber Letter.pdf](#)

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

ALL – 1/3 @ \$38.56 (bought @ limit)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 1(ALL)

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

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	10/22/2012	\$143.15	\$141.85	-0.91%		Aggregator
SPY(1/4)	10/22/2012	\$141.35	\$141.85	0.35%		sell on close >= \$141.86
ALL(1/3)	11/5/2012	\$38.21	\$38.68	1.23%		sell on close >= \$39.45

I am estimating ALL's exit trigger for the sell price. Normally I would hold a Catapult until the next morning but with the big event risk, I'd rather just take profits if it hits its target.

I will look to exit 1 lot of SPY on a close higher.

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