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May 13, 2024

# Market Structure EDGE

## Going Short the Market Using Broad Sentiment

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**Tim Quast**

Founder & CEO  
Market Structure EDGE

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Cont. 

As with all investments, your capital is at risk

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# **Going Short the Market**

## ***Using EDGE Broad Sentiment***

**Tim Quast, founder and CEO of  
Market Structure EDGE  
May 13, 2024**

- **Tim Quast – founder of two market structure analytics firms**
- **Market Structure EDGE – Only quantitative Supply and Demand data for traders**
- **IBKR content partner**
- ***My market education will necessarily emphasize what I know.***



**Objective: A high-probability approach to making money in markets that are declining.**

***BEWARE: Shorting stocks is risky!  
Don't do it unless you know what you're doing.***

***FIRST: Understand how the market works.***



Illustration [25072962](#) © [Skypixel](#) | [Dreamstime.com](#)

How about shorting stocks with high short interest?

Nope. Terrible correlation!

Performance								
Watchlist		Change Today	1 Month Return	1 Year Return	Total Return			
Stocks with Highest Short Interest		+4.91%	-	-	-			
^GSPC		+0.40%	-3.32%	+23.16%	+5317.61%			
30 Symbols								
Symbol	Company Name	Last Price	Change	% Change	Market Time	Volume	Avg Vol (3 month)	Market Cap
CVNA	Carvana Co.	114.6999	+27.61	+31.70%	12:51 PM EDT	17.96M	6.30M	20.37B
MPW	Medical Properties Trust, Inc.	4.815	+0.18	+4.00%	12:51 PM EDT	5.93M	18.47M	2.90B
AI	C3.ai, Inc.	23.06	+0.37	+1.63%	12:51 PM EDT	1.65M	7.38M	2.81B
KSS	Kohl's Corporation	24.4713	+0.92	+3.91%	12:51 PM EDT	1.29M	5.44M	2.71B
ABR	Arbor Realty Trust, Inc.	13.115	+0.14	+1.12%	12:51 PM EDT	1.02M	4.32M	2.48B
CNK	Cinemark Holdings, Inc.	17.515	+0.08	+0.49%	12:51 PM EDT	1.80M	3.21M	2.14B
UPST	Upstart Holdings, Inc.	23.3	+0.43	+1.88%	12:50 PM EDT	1.34M	5.60M	2.05B
PLUG	Plug Power Inc.	2.4407	+0.14	+6.12%	12:51 PM EDT	17.79M	33.02M	1.70B
ENVX	Enovix Corporation	9.04	+2.53	+38.86%	12:51 PM EDT	13.33M	4.59M	1.54B
ZIM	ZIM Integrated Shipping Services Ltd.	12.4801	-0.88	-6.59%	12:51 PM EDT	3.46M	4.47M	1.50B

Source Data from May 2, 2024: <https://finance.yahoo.com/u/yahoo-finance/watchlists/stocks-with-the-highest-short-interest/>

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# The Problem with Short Interest

## § 220.1 Authority, purpose, and scope.

(a) *Authority and purpose.* Regulation T (this part) is issued by the Board of Governors of the Federal Reserve System (the Board) pursuant to the Securities Exchange Act of 1934 (the Act) (15 U.S.C.78a et seq.). Its principal purpose is to regulate extensions of credit by brokers and dealers; it also covers related transactions within the Board's authority under the Act. It imposes, among other obligations, initial margin requirements and payment rules on certain securities transactions.

- 1. Short Interest is a 1974 measure, and largely unchanged since then.**
- 2. Created by the Federal Reserve to regulate brokers, not by the SEC to meter shorting.**
- 3. Established in response to currency, interest-rate, volatility arising from leaving gold standard in 1971.**
- 4. Almost zero correlation to how stocks behave.**

Source: [ecfr.gov](https://www.ecfr.gov), Federal Reserve System

**Short Interest is the WRONG BASIS for shorting.**

**Short Volume. Not Short Interest.  
(We call Short Volume “Supply.”)**

# Here's what the SEC says about SHORT VOLUME

**From:** <https://www.sec.gov/investor/pubs/regsho.htm>

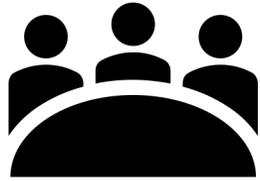
## Naked Short Sales

“Naked” short selling is **not necessarily a violation of the federal securities laws or the Commission’s rules...[BECAUSE]...**broker-dealers that make a market in a security generally stand ready to buy and sell the security on a regular and continuous basis at a publicly quoted price, even when there are no other buyers or sellers.

**Thus, market makers must sell a security to a buyer even when there are temporary shortages of that security available in the market.** This may occur, for example, if there is a sudden surge in buying interest in that security, or if few investors are selling the security at that time...particularly in a fast-moving market, [when they] may need to sell the security short without having arranged to borrow shares.

**SOURCE:** <https://www.sec.gov/investor/pubs/regsho.htm>

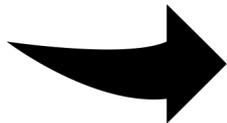
# GameStop (GME): Let's Suppose...



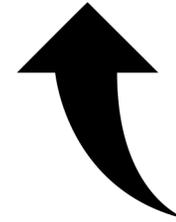
GME Stockholders  
Neither buy or sell



100% of the outstanding stock



...Retail traders jam the pipeline  
with limit orders to buy...



...and Market Makers  
manufacture stock...



Stock Soars!



# Why Can Market Makers Manufacture Stocks?

**Regulation National Market System (Reg NMS): *Regulators wanted a “continuous auction market” where there are always 100 shares of everything to buy or sell (the minimum bid/offer).***

- Market-makers said: Impossible to make bids/offers on everything without exemption from “short locate” rules (T+3 to verify stock can be borrowed)
- SEC agreed
- *Market Makers are exempt from **Reg SHO Rule 203(b)(2)** requiring everyone to locate shares to borrow*

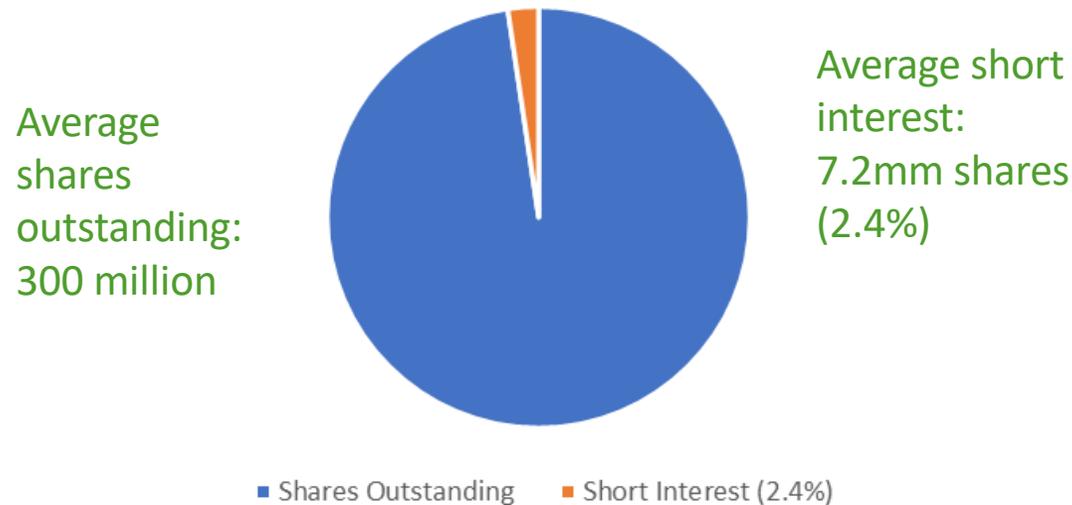
## Short Volume:

1. **Modified uptick rule: Reg SHO Rule 201.**
2. **Finra requires brokers to furnish data.**
3. **SEC exempts brokers engaged in bona fide market-making (bids/offers) from Reg SHO Rule 203(b)(2).**

# Short Volume vs. Short Interest

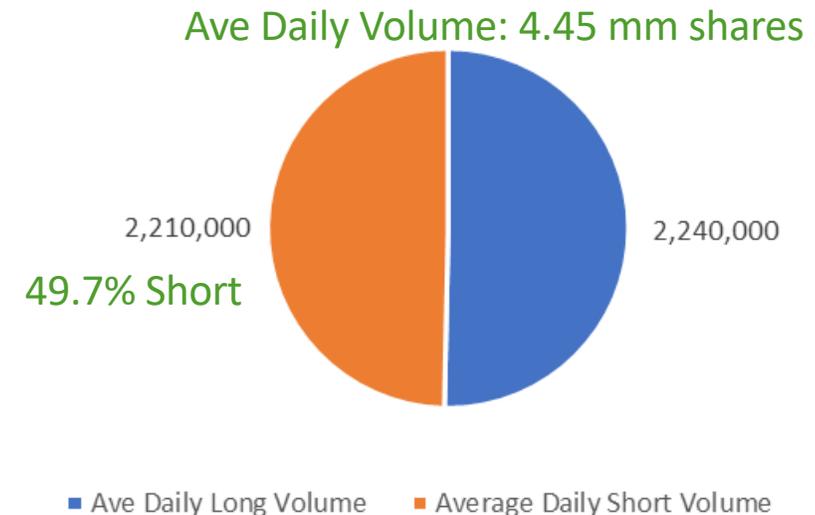
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Average S&P 500 Shares Out, Short Interest (June 2023 - Data S&P Global, Yardeni Research)



This does not set price, because these shares aren't trading.

Average Daily Volume S&P 500 Components: 4.45mm shares, 49.7% of it is Short, Borrowed



This sets price, because this is VOLUME.

Sources: ModernIR.com, Finra, Yardeni Research, S&P Global, Inc. Data: 200D Ave Oct 2023.

### NVDA Market Structure Sentiment™ (Demand) vs. Closing Price

October 24, 2023 - December 5, 2023

Market Structure Sentiment™: 1.8 Closing Price: 465.66 Trade Date: 12/5/2023



### Short Volume

#### NVDA Short Volume % (Supply)

Short Vol %: 44.7 Trade Date: 12/5/2023

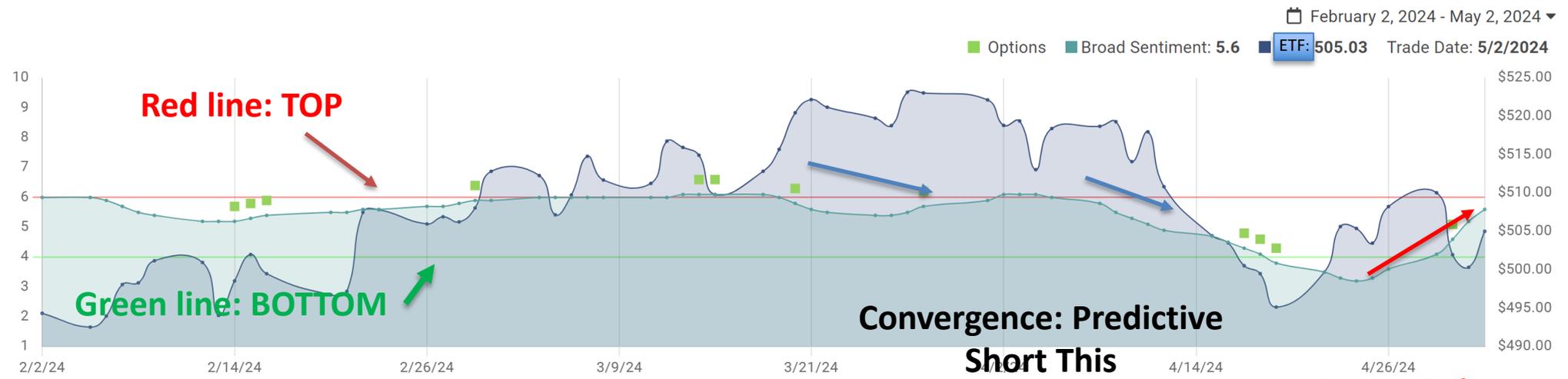


Data from Market Structure EDGE

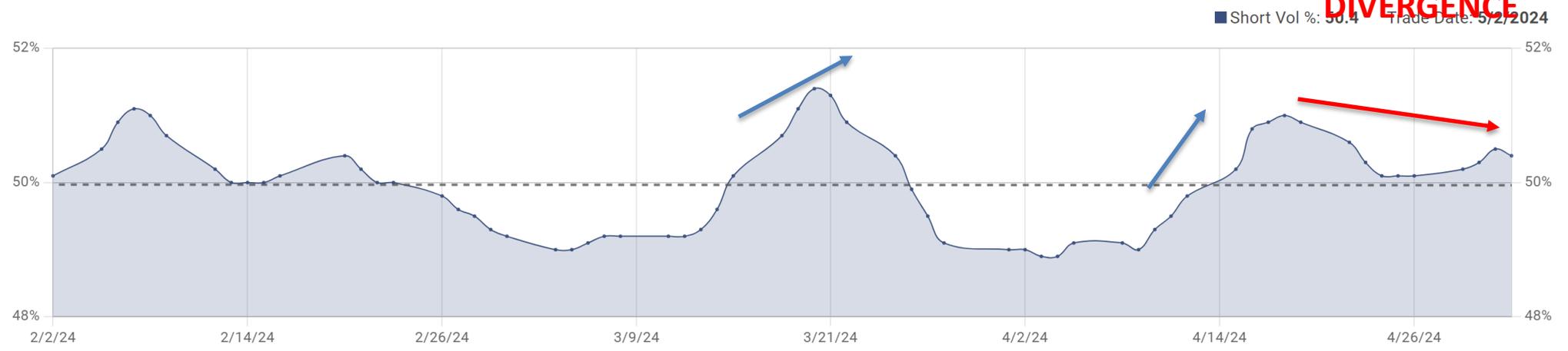
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Broad Sentiment, the EDGE risk-management tool, reflects average Market Structure Sentiment™ (Demand) for composite S&P 500 stocks versus the price of [redacted] ETF. Green squares show monthly options and futures expirations.



Short Volume (Supply) is the average percentage of daily volume in S&P 500 stocks that's short (borrowed, created by market-makers).



Source: Daily Trading Ideas at Market Structure EDGE, IBKR

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## Using Leveraged ETFs:

1. **Shorting is RISKY!**
2. **Short Demand/Supply imbalances, not fundamentals.**
3. **Never take your eyes off a fleeting short.**
4. **Leveraged shorts are one-day trades.**

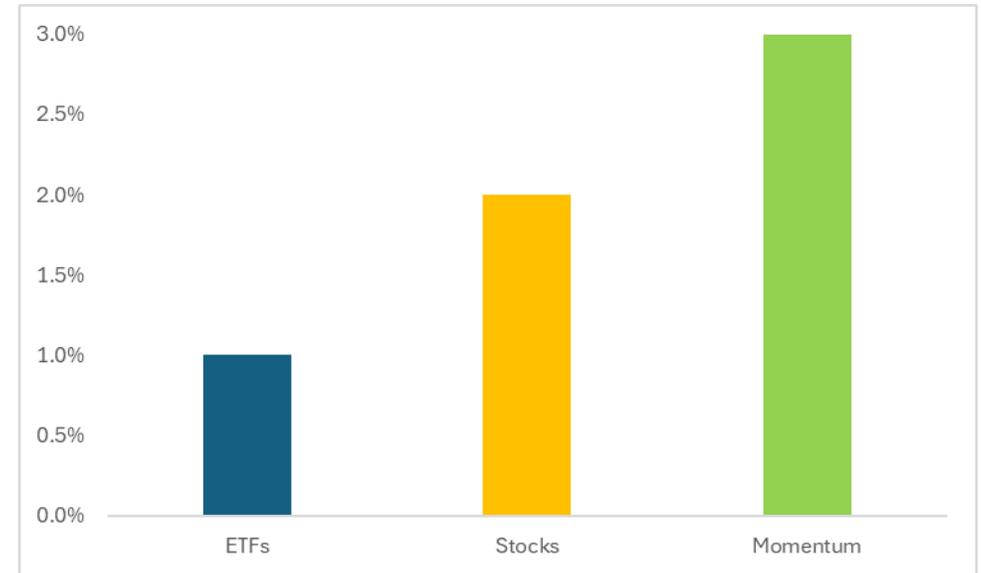


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# Short Entries/Exits

1. Market trackers like SPY average 1% daily VOLATILITY.
2. Underlying stocks average 2% VOLATILITY.
3. Momentum stocks have 3% (or more!) VOLATILITY.
4. Shorting: Entry - Use VOLATILITY



Data: ModernIR.com models, marketstructureedge.com.  
VOLATILITY: Average intraday high/low spread.

## Illustration:

1. If shorting a 1x vehicle, and it's DOWN 1% like here, because the market is UP, that's ALL the market's volatility. A great entry. You only need HALF of it for entry.
2. See the liquidity. This instrument has 1.6mm shares at the bid and offer. Used heavily by machines.
3. Don't take risks! You can leave quickly if the price moves against you.

ORDER TICKET OPEN ORDERS (7) ?

PROSHARES SHORT S&P500 ARCA

**12.25** Bid/Ask **12.25** **12.26**  
Size 453,600 1,123,200

-0.13 -1.05%

Realtime Price: Consolidated | Last Size: 4,000 | Exchanges for Last: Y Bid: AKPTXZU Ask: ABNJKPTYZU

Your Account

Buying Power	49,283
Available to Trade	49,283
Settled Cash	49,283
Equity w/Loan	49,283
Initial Margin	0
Maintenance Margin	0
Position / Avg. Price	0 / 0
Open Orders	0

Buy Order Sell Order

QUANTITY

100 - + Shares

~1,225.00 USD

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COMMISSION COST FREE

Buy Order Preview

**Source:** Interactive Brokers platform. Data are illustrative only do not endorse a strategy or instrument.

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