

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

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April 15, 2008

Issue 40

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## Market Overview

*Summary of Recent Active Studies (see <http://QuantifiableEdges.blogspot.com> for details)*

Study Date	Description	Time span	Bias
April 15, 2008	WR7 Down NR7	1-15 Days	Bullish
April 14, 2008	Sharp Selloff in Consolidation	20 days	Bearish
April 10, 2008	Relatively High Put/Call	20 days	Bullish
April 8, 2008	Negative Reversal Bars	3-5 days	Bearish
April 4, 2008	Trend Over Volatility (TOV)	20 days	Bullish
April 1, 2008	3 Surge Days	2-6 weeks	Bullish
February 1, 2008	FTD's Short-Term Implications	long-term	Bearish
March 24, 2008	Nasdaq Leadership Bullish	1-10 weeks	Bullish
March 19, 2008	Bottom Explosion 2	1-20 days	Bullish
March 19, 2008	3.5% Up Cluster	10-20 days	Bullish

### *Intermediate-term Outlook (2 weeks – 2 months) – neutral – updated 4/14/2008*

On Friday April 11<sup>th</sup> the market took a bit of a dive. The catalyst for the selloff was GE's poor earnings announcement. In a healthier market environment the large gap down at the open would have been viewed by market participants as a buying opportunity and the market would have spent the day clawing back from its losses rather than extending them. By the end of the day Friday, the S&P 500 had lost over 2% and the Nasdaq 100 had lost nearly 3%. This action is concerning.

In [tonight's blog](#), I looked at large selloff's in the past that occurred in non-trending markets and were not breakdowns. For this test I used ADX to define trend and a violation of a 10-day closing low to determine a possible break of support. The results were quite negative over every exit point from 1-day to 4-weeks out. This is the first study with bearish intermediate-term implications I've produced for several weeks.

As I mentioned in my last intermediate-term outlook a few days ago we are also seeing some of the more bullish studies from a few weeks back begin to age and expire. The first one occurred last Thursday. This Thursday the 17<sup>th</sup> both of the bullish studies from March 19<sup>th</sup> will fall off the list as their influence wanes.

Another concern is the action in the Nasdaq this week, and especially Friday. As I mentioned above, GE was the catalyst, and the prime culprit for their earnings miss was the disruption in the financial markets. You would expect financials to take this news

poorly and sell off in sympathy. The Nasdaq, which had taken a leadership role over the NYSE Composite a few weeks ago, should have held up a bit better. GE is largely unrelated to technology. Yet it fell even harder than the broad market – nearly 3% versus the S&P 500's 2%. This has moved the weekly relative strength of the Nasdaq below the NYSE's. As I've discussed in the past, the general market has typically struggled to advance when the Nasdaq has failed to take leadership from the NYSE.

It will be important to monitor the market's ability to hold above recent support levels. As noted, it has failed to break down in any way so far. Friday did move the S&P 500 and Nasdaq below their 50-day moving averages. While these are lines that many analysts looked at to possibly provide support, I find it neither surprising nor concerning that they were broken. Moving averages many times will provide support or resistance based on their slope. A moving average which has a nice up-slope serves a decent chance of providing at least temporary support. When a moving average is flat, many times it will act more as a pendulum than a support/resistance level. The recent move up in the market served to flatten out the 50-day moving averages. It may cross back and forth above and below it several times before the direction is fully determined and the moving average will begin to act as a support/resistance level again.

The late March lows are more significant in my eyes. These were around 1313 for the S&P 500. If the market can remain above these then the series of higher lows remains in tact and the baby rally has a chance of growing up. If these are broken then the last line of defense is the mid-March lows around 1257. If they're broken then it's a bit late to begin to notice the failure.

For now there still are many positives to look at. Even outside of the March 19<sup>th</sup> explosion studies that will be falling off the board, there are several more that make the bullish case. These include Trend Over Volatility, the High Put/Call, the 3 Surge Days and sharp drop in Consumer Sentiment. There is no need to overreact to the negative inferences of the April 11<sup>th</sup> market action. It is simply the first intermediate-term caution flag we've seen in the last month. It should be respected and we'll need to keep a close watch on further action. For now, I am moving the overall bias to neutral. I will therefore be willing to take both longs and shorts equally.

***Short-term Outlook (1-5 days) –bullish – updated 4/15/08***

As typically happens, the sharp selloff on Friday continued Monday. Volume was light and price moved in a narrow band all day, which is a positive. [Tonight in the blog](#) I looked at wide range down days that are followed by narrow range days. Historically this pattern has provided a quantifiable edge in the NDX and SPX. This therefore scores a point for the bullish case.

Over the last few days the market has continued to provide mixed signals, making it difficult to trade aggressively. On a positive note, the market inched closer to but held above its late March lows. In last night's short-term outlook I indicated I felt these would be important levels for the market to hold. Failure could indicate we are in the midst of another leg down for the market. With support levels close by we are now approaching an area where risk/reward is once again skewed in the favor of the longside. Traders could begin to scale in to an index position soon with the late-March lows as a possible stop.

As I sometimes like to do when I find a market setup with an edge, I tested the setup across numerous individual stocks. Rather than just sell "X" days out I instituted stop and target levels. With crude stop setting techniques the results were slightly favorable. By managing risk/reward I believe the setup could work quite nicely. Rather than enter a market position tonight, I instead found an individual stock with a reasonable stop level close by and room to run on the upside.

### **Catapult and Capitulative Breadth Statistics**

*(Catapult Presentation Part 1) (Catapult Presentation Part 2)*

#### ***Open Catapult Trades***

none

#### ***Open Big 50 Trades***

None

#### ***Open Catapult for ETF's Trades***

None

#### ***Broad Market Large Cap CBI – 0***

#### ***Sector CBI Breakdown (% of stocks with active catapult triggers within each sector.)***

<b>Index</b>	<b>ETF</b>	<b>CBI %</b>	<b>Index</b>	<b>ETF</b>	<b>CBI %</b>
DJ US Broker Dealers	IAI	0.00	DJ US Energy	IYE	0.00
DJ US Insurance Index	IAK	1.35	DJ US Financial	IYF	0.68
DJ US Regional Banks	IAT	1.25	DJ US Financial Services	IYG	0.00
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	0.00
DJ US Oil&Gas Expl & Prod	IEO	0.00	DJ US Industrial Sector	IYJ	0.00
DJ US Oil Equip & Svcs	IEZ	0.00	DJ US Consumer Goods	IYK	0.00
DJ US Pharmaceuticals	IHE	0.00	DJ US Basic Materials	IYM	1.35
DJ US Healthcare Providers	IHF	0.00	DJ US Real Estate	IYR	2.44
DJ US Medical Devices	IHI	2.44	DJ US Transportation	IYT	0.00
DJ US Aerospace & Defense	ITA	0.00	DJ US Technology Sector	IYW	0.50
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	0.44	Nasdaq 100	QQQQ	0.00

No signs of capitulative selling at the present time.

## **Additional New Trade Ideas**

*MSFT – buy @ \$28.06 – set stop @ \$27.74 if filled. Sell @ \$29.00 limit if filled.* With support nearby, MSFT is providing a potential reward which is 3x the risk. I ran some tests earlier with entry at the close and a target price at the close of the day before the WR7. Using varying stop techniques, the profit factor was coming out very similar – about 1.2. Setting the stop at the NR7's low resulted in about 28% winners, while setting it at a distance equal to the distance from the close two days ago changed the % winners to about 52%. In either case, the net profits were similar. My takeaway is that by having a reasonable technical support level nearby and some room to run on the upside, we should be able to skew the odds more heavily in our favor. Having the market set up in a similar pattern also helps. I don't anticipate this trade will last more than a few days.

## **Additional Trades Active Table**

<b>Symbol</b>	<b>Entry Date</b>	<b>Entry Price</b>	<b>Current Price</b>	<b>% Gain/Loss</b>	<b>Stop</b>	<b>Notes</b>
SLB	4/8/2008	\$90.58	\$91.19	-0.7%		cover on close < 10ma
GRMN	4/11/2008	\$45.25	\$44.26	-2.2%		

## **Stocks and ETF's on my Radar**

### ***Strong Selloffs In Congestion -***

***AXP, WFR, WM, RIMM, INTC, HES, AMZN, TYC, ATI, UTX.***

### ***WR7NR7 –***

***ALL, CI, IWB, OEF, PPH, QQQQ, XLI***

## **Notable S&P 500 stocks outside my “tradable” radar**

### ***Oversold***

None

### ***Overbought***

None

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