

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 29, 2008

Issue 177

## Market Overview

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

Study Date	Description	Time span	Bias	Avg Max Move	Avg MM + 1 Std Dev
October 29, 2008	Strong Bounce Without Volume	1-2 Days	Bearish	-3.50%	-6.20%
<b>October 27, 2008</b>	<b>Up Iss 10 MA &lt; .375 SP 100 low</b>	<b>1-10 Days</b>	<b>Bullish</b>	<b>4.57%</b>	<b>9.12%</b>
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		

If the avg max move is achieved it will appear in **bold and green**. If the avg + 1 std deviation is achieved, the study will in *bold italic blue* and will be removed tomorrow.

### *Short-term Outlook (1-5 days) – slightly bullish – updated 10/29*

The market rally we were expecting arrived in a big way today. The Nasdaq rose about 10% while the Dow and S&P rose almost 11%. Breadth was solid. Up/down volume statistics were especially good as up volume accounted for 95% of all volume on the NYSE. Total volume was disappointing, though as it failed to even post a 5-day high.

Tonight I looked at other instances where the S&P 500 closed at a 100-day low and then gained at least 3% the next day. I broke the results down to those times when the 3% rise came on the highest volume in 5 days and those times when it didn't.

First let's look at times unlike today when volume came in strong:

Yesterday the SPX closes at a 100-day low. Today it rises over 3% on the highest volume in 5 days.												
Buy on close. Sell X days later. \$100k/trade. 1960-present.												
X Days	Net Profit	Trades	Wins	Losses	% Wins	Max Win	Max Loss	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
5	\$25,837.68	8	7	1	87.50	\$9,334.72	(\$1,536.08)	\$3,910.54	(\$1,536.08)	2.55	17.82	\$3,229.71
4	\$19,820.35	8	6	2	75.00	\$7,003.30	(\$3,869.74)	\$4,228.38	(\$2,774.96)	1.52	4.57	\$2,477.54
3	\$23,740.99	8	5	3	62.50	\$9,591.40	(\$2,035.00)	\$5,715.56	(\$1,612.27)	3.55	5.91	\$2,967.62
2	\$11,133.44	8	5	3	62.50	\$5,193.72	(\$3,081.26)	\$3,164.68	(\$1,563.31)	2.02	3.37	\$1,391.68
1	\$17,874.70	8	5	3	62.50	\$9,089.88	(\$1,441.44)	\$4,050.33	(\$792.31)	5.11	8.52	\$2,234.34

Low instances but bullish results. An average gain of another 3% 5 days out is twice the size of the Max Loss after 5 days. Seven of eight instances showed positive returns for that time frame as well. All time frames 1-5 days out showed positive expectations along with strong W/L ratios and Profit Factors.

Now let's look at those times when the NYSE total volume failed to make a 5-day high:

Yesterday the SPX closes at a 100-day low. Today it rises over 3% but fails to register the highest volume in 5 days.												
Buy on close. Sell X days later. \$100k/trade. 1960-present.												
X Days	Net Profit	Trades	Wins	Losses	% Wins	Max Win	Max Loss	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
5	(\$13,468.78)	8	4	4	50.00	\$3,474.90	(\$14,461.05)	\$2,156.11	(\$5,523.30)	0.39	0.39	(\$1,683.60)
4	(\$16,875.21)	8	3	5	37.50	\$3,711.51	(\$9,304.95)	\$2,019.49	(\$4,586.74)	0.44	0.26	(\$2,109.40)
3	(\$18,914.80)	9	2	7	22.22	\$1,500.84	(\$5,706.05)	\$1,477.12	(\$3,124.15)	0.47	0.14	(\$2,101.64)
2	(\$23,965.64)	9	1	8	11.11	\$355.41	(\$9,455.49)	\$355.41	(\$3,040.13)	0.12	0.01	(\$2,662.85)
1	(\$5,703.79)	9	3	6	33.33	\$873.18	(\$2,259.18)	\$562.22	(\$1,231.74)	0.46	0.23	(\$633.75)

There's a very stark contrast to the first test. Here results are negative in all time frames. There is a decided downside tilt in the 1<sup>st</sup> two days as 8 of 9 instances declined over that time period. The lone winner followed the 9/24/2001 instance. The average loss was 3.0% while the lone gain was only 0.35%. Even though instances are low I am listing this among the active studies.

The Fed is set to make a rate announcement Wednesday at 2:15. I looked at other times the market rose 2% or more the day before a Fed announcement. There were 8 other instances. They are listed below.

TradeStation Trades List										
#	Type	Date/Time	Signal	Price	Roll Over USD/Lot	Shares/Ctrts Profit	Net Profit Cum Net Profit	% Profit	Run-up DrawDown	
1	Buy	08/23/82	Buy	\$116.11	\$0.00	861	(\$671.58)	(0.67%)	\$1,214.01	
	Sell	08/24/82	Sell	\$115.33			(\$671.58)		(\$1,747.83)	
2	Buy	01/04/88	Buy	\$255.94	\$0.00	390	\$1,045.20	1.05%	\$2,277.60	
	Sell	01/05/88	Sell	\$258.62		\$1,045.20	\$373.62		\$0.00	
3	Buy	10/01/90	Buy	\$314.93	\$0.00	317	\$85.59	0.09%	\$1,505.75	
	Sell	10/02/90	Sell	\$315.20		\$85.59	\$459.21		\$0.00	
4	Buy	03/29/99	Buy	\$1,310.17	\$0.00	76	(\$715.92)	(0.72%)	\$0.00	
	Sell	03/30/99	Sell	\$1,300.75		(\$715.92)	(\$256.71)		(\$1,101.24)	
5	Buy	05/15/00	Buy	\$1,452.36	\$0.00	68	\$930.24	0.94%	\$1,226.72	
	Sell	05/16/00	Sell	\$1,466.04		\$930.24	\$673.53		(\$108.80)	
6	Buy	11/14/00	Buy	\$1,382.95	\$0.00	72	\$493.92	0.50%	\$936.72	
	Sell	11/15/00	Sell	\$1,389.81		\$493.92	\$1,167.45		(\$590.40)	
7	Buy	03/17/03	Buy	\$862.79	\$0.00	115	\$420.90	0.42%	\$477.25	
	Sell	03/18/03	Sell	\$866.45		\$420.90	\$1,588.35		(\$624.45)	
8	Buy	08/06/07	Buy	\$1,467.67	\$0.00	68	\$614.72	0.62%	\$1,402.84	
	Sell	08/07/07	Sell	\$1,476.71		\$614.72	\$2,203.07		(\$807.16)	

What stands out to me is the fact that the Fed day appears to be quite a bit less volatile than the day that preceded it. We could be in for a relatively quiet day tomorrow. Of course relatively quiet these days could still be a 4-5% range. I'd be surprised to see upside follow-through of that sort, though.

My mind-set right now is profit-taking mode. The SPY position was sold out of on Tuesday in two parts via intraday updates to subscribers. The first part was at the open and the 2<sup>nd</sup> part at the close. Should the market rally tomorrow following the Fed announcement, I will look to take a SPY short position. [Fed rallies have a tendency to pull back over the following days.](#) Combined with tonight's volume study, that would provide me cause to short.

I may also look to take partial profits in the Catapult trades, and will likely send out an update on those during the morning tomorrow.

***Intermediate-term Outlook (1 week – 2 months)–slightly bullish -updated 10//20***

I generally list the time frame of the Intermediate-term Outlook to be 2 weeks – 3 months. In this market environment 3 months appears to be farther out than I'd be comfortable anticipating. By several measures I've discussed lately the action over the past 4 weeks has been worse than anything ever witnessed. Historical comparisons are few outside of the Crash of '29 and to a lesser degree the Crash of '87. More than anything this suggests to me that we are at a period in time that is unique in many ways.

It is very difficult to time the market when many indicators have posted and continue to post readings that have rarely or never been seen before. A couple of weeks ago I showed a table with some incredible historical extremes I was seeing. The suggestion was that the market was more overdue for a bounce than it had ever been by many measures. That bounce arrived on 10/13. It was one of the strongest one-day rallies in the history of the market. It lasted until just after the opening bell the next day.

Rallies from conditions as extreme as we saw 2 weeks ago should last longer than 1-2 days – especially when they begin so strong. We are now hitting new extremes for several of the same indicators along with some new ones:

<b>Current Condition</b>	<b>Severity</b>
<b><i>Breadth Extremes</i></b>	
% Stocks 2 Std Dev Below 200 MA = 86%	Highest since data available back to 1986
%Stocks 1 Std Dev Below 200 MA = 95%	Highest since data available back to 1986
<b><i>Price Extremes</i></b>	
SPX over 32% below 200ma	Since 1960 (as far back as data goes) this is the lowest
Dow Industrials 29% below 200ma	10/10/2008 was slightly lower - other than that this is the lowest since 1938.
<b><i>Volatility Extremes</i></b>	
VIX close @ 79.13 and high @ 89.53	Both all time high (back to 1990)
SPY 20-period Avg True Range = 7.6%	Highest since SPY inception
SPY 10-period Absolute Avg Gap = 3.07%	Highest since SPY inception
S&P 500 20-per. Avg True Range = 6.70%	Highest since at least 1960

Some truly incredible numbers here. Most astonishing to me is the fact that the SPY has gapped an AVERAGE of 3% during the last 2 weeks. Again, this is suggesting a bounce should be in the cards here fairly soon. I believe the next strong bounce is likely to result in at least a multi-week rally similar to those we saw coming off the January, March and July “bottoms”.

My visibility beyond that is poor and will depend largely upon how the world economies react to the global stimulus plans currently in place.

**Catapult and Capitulative Breadth Statistics**

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

***Open Catapult Trades***

Listed below under “Broad Market Large Cap CBI”

## Catapult for ETF's Trades

None

## Broad Market Large Cap CBI –8/4 (AIG-3, MA-3, COV, HPQ)

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

Index	ETF	CBI %	Index	ETF	CBI %
DJ US Broker Dealers	IAI	0.00	DJ US Energy	IYE	5.81
DJ US Insurance Index	IAK	5.41	DJ US Financial	IYF	10.27
DJ US Regional Banks	IAT	0.00	DJ US Financial Services	IYG	2.10
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	24.65
DJ US Oil&Gas Expl & Prod	IEO	0.00	DJ US Industrial Sector	IYJ	13.79
DJ US Oil Equip & Svcs	IEZ	9.62	DJ US Consumer Goods	IYK	18.37
DJ US Pharmaceuticals	IHE	10.81	DJ US Basic Materials	IYM	8.11
DJ US Healthcare Providers	IHF	30.61	DJ US Real Estate	IYR	30.49
DJ US Medical Devices	IHI	29.27	DJ US Transportation	IYT	0.00
DJ US Aerospace & Defense	ITA	13.89	DJ US Technology Sector	IYW	10.05
DJ US Home Construction	ITB	14.29	DJ US Telecommunications	IYZ	13.16
DJ US Consumer Svcs	IYC	14.04	Nasdaq 100	QQQQ	9.00

### Additional New Trade Ideas

SPY – Short on CLOSE ABOVE \$94.50. This is based on the short-term market outlook above.

### Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
MA	10/27/2008	\$127.63	\$136.01	6.57%		Catapult
SPY	10/27/2008	\$83.95	\$90.55	7.86%		closed
MA	10/28/2008	\$126.35	\$136.01	7.65%		Catapult
HPQ	10/28/2008	\$31.18	\$35.09	12.54%		Catapult

Half of the SPY position was exited at the open and the other half at the close.

COV came within 4 cents of the limit price but did not officially fill before launching higher.

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