

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 14, 2008

Issue 189

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
November 14, 2008	5% Spike	1-2 days	Bearish	-2.00%	-3.20%
November 14, 2008	S&P Rises 2% and Spyx > 80	1-6 days	Bullish	3.40%	5.80%
November 13, 2008	5% Drop	1-4 days	Bullish	4.00%	7.00%
November 13, 2008	95% Down Volume	1 day	Bullish	2.50%	3.25%
November 12, 2008	2 Days Lower In Chop	1-2 days	Bullish	1.50%	3.20%
November 9, 2008	2.5% Rally On Poor Volume	1-7 days	Bearish	-5.15%	-10.10%
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		

If the avg max move is achieved it will appear in **bold and brown**. 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 11/14

The bounce we were expecting arrived today in a pronounced fashion. After dropping hard in the morning and making new bear market lows, the major indices all rallied strongly in the afternoon. The S&P 500 gained over 10% between 1 and 4pm. Breadth was strong and so was volume. By the close the major indices were all up between 6%-7%.

Upside volume today on the NYSE accounted for over 90% of total volume. I look for other times since 1970 where a 90% downside volume day like yesterday was followed immediately by a 90% upside volume day. There were only 2 to be found: 3/6/07 and 8/29/07.

Not only was volume strong, but our **S&P 500 Spyx indicator** posted a reading over 98. High readings over 80 tend to lead to a bounce when the market has moved lower on the day. They also show a bit of an edge when the market moves sharply higher:

S&P 500 rises over 2% and Volume Spyx closes over 80.										
Buy on close. Sell X days later. \$100k/trade. 1996 - present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
10	\$8,168.11	23	14	9	60.87	\$2,606.64	(\$3,147.21)	0.83	1.29	\$355.14
9	\$18,985.86	24	14	10	58.33	\$3,096.53	(\$2,436.56)	1.27	1.78	\$791.08
8	\$17,502.58	25	14	11	56.00	\$2,828.98	(\$2,009.37)	1.41	1.79	\$700.10
7	\$5,936.91	25	16	9	64.00	\$2,900.80	(\$4,497.32)	0.65	1.15	\$237.48
6	\$29,691.50	26	19	7	73.08	\$2,741.83	(\$3,200.48)	0.86	2.33	\$1,141.98
5	\$28,160.48	26	17	9	65.38	\$2,862.54	(\$2,278.08)	1.26	2.37	\$1,083.10
4	\$21,226.05	27	18	9	66.67	\$2,493.19	(\$2,627.94)	0.95	1.90	\$786.15
3	\$20,147.65	27	18	9	66.67	\$2,273.53	(\$2,308.44)	0.98	1.97	\$746.21
2	\$16,166.41	28	19	9	67.86	\$1,707.81	(\$1,809.11)	0.94	1.99	\$577.37
1	\$6,578.70	28	16	12	57.14	\$1,060.91	(\$866.32)	1.22	1.63	\$234.95

A decent, though not overwhelming, upside bias is apparent over the next 1-6 days.

I recently looked at one-day selloff of over 5% and found them to have a nice upside edge. Tonight I looked at rallies of 5% or greater. For the S&P there the sample size is small but there has been a bit of a downside bias since 1960:

S&P 500 rises over 5%.										
Buy on close. Sell X days later. \$100k/trade. 1996 - present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
8	(\$24,301.21)	9	3	6	33.33	\$3,918.53	(\$6,009.47)	0.65	0.33	(\$2,700.13)
7	(\$26,491.11)	9	4	5	44.44	\$3,056.06	(\$7,743.07)	0.39	0.32	(\$2,943.46)
6	(\$6,370.59)	9	5	4	55.56	\$3,373.48	(\$5,809.50)	0.58	0.73	(\$707.84)
5	\$5,977.13	9	5	4	55.56	\$5,257.16	(\$5,077.17)	1.04	1.29	\$664.13
4	(\$3,691.88)	9	5	4	55.56	\$3,831.90	(\$5,712.85)	0.67	0.84	(\$410.21)
3	\$2,390.97	10	4	6	40.00	\$5,329.69	(\$3,154.63)	1.69	1.13	\$239.10
2	(\$9,702.26)	10	5	5	50.00	\$2,793.62	(\$4,734.07)	0.59	0.59	(\$970.23)
1	\$2,462.83	11	3	8	27.27	\$4,014.02	(\$1,197.40)	3.35	1.26	\$223.89

Of the 11 instances, the only one that didn't close below the close of the 5% day within the next 4 days was the 5/27/70 occurrence.

Below are listed the one-day performance following all 5% up days for the S&P 500.

Performance the day after a 5% up day for the S&P 500.				
#	Date	Signal	Price	% Profit
1	5/27/1970	Buy	\$72.77	
	5/28/1970	Sell	\$74.61	2.53%
2	10/20/1987	Buy	\$236.83	
	10/21/1987	Sell	\$258.37	9.10%
3	10/21/1987	Buy	\$258.37	
	10/22/1987	Sell	\$248.25	-3.92%
4	10/28/1997	Buy	\$921.86	
	10/29/1997	Sell	\$919.16	-0.29%
5	9/8/1998	Buy	\$1,023.45	
	9/9/1998	Sell	\$1,006.20	-1.69%
6	1/3/2001	Buy	\$1,347.53	
	1/4/2001	Sell	\$1,333.29	-1.06%
7	7/24/2002	Buy	\$843.43	
	7/25/2002	Sell	\$838.68	-0.56%
8	7/29/2002	Buy	\$898.96	
	7/30/2002	Sell	\$902.78	0.42%
9	9/30/2008	Buy	\$1,166.36	
	10/1/2008	Sell	\$1,161.06	-0.45%
10	10/13/2008	Buy	\$1,003.35	
	10/14/2008	Sell	\$998.01	-0.53%
11	10/28/2008	Buy	\$940.51	
	10/29/2008	Sell	\$930.09	-1.11%

A couple of things to note: First, 8 of the last 9 have closed lower. Second, the lower closes have generally been tame – both in relation to the 5% up day and compared to the instances that continued to rise the next day.

I also looked at the Dow since my data there went back to 1920. There have been 58 days where the Dow gained 5% or more over that time. During the Great Depression there was a multitude of 5% up days. Of the 58 instances, only 19 of them (33%) closed higher the next day. Again though the winners averaged a significantly greater move the next day than the losers and the net amount would have been a small gain. Notable about those that did manage to close higher is that 11 of the 19 maintained their strength and didn't close below the trigger day's close for at least the next 4 days.

Today's wild action meant basically all of the targets for the studies listed in the table were met today – both bearish and bullish. Tonight's [Aggregator chart](#) with our new studies included is below:



The green Aggregator line is basically neutral with a reading of +0.02. The black differential line is still showing the S&P has underperformed the last few days. This suggests there could be more room to the upside. Even so I am not looking to push my luck. One of the most reliable triggers over the last year and a half has been to sell any two days higher in a row. Should we close higher tomorrow I will certainly exit the remaining portion of my S&P position. We're going to need to wait for the market to set up again before looking for additional entries. For now it is a matter of managing the open positions. Much more on that in the active trade ideas section below.

Intermediate-term Outlook (1 week – 2 months)– bullish -updated 11/10

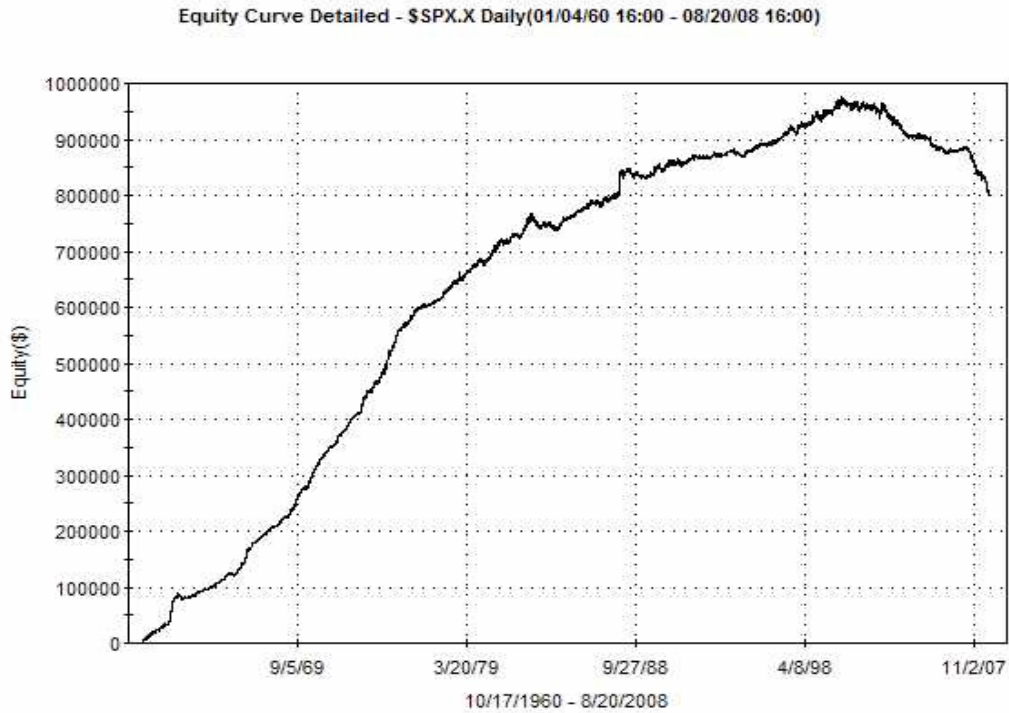
While the market did suffer a steep drop mid-week, it did manage to hold substantially above its October lows. Extremes anywhere close to those we saw at the October lows that I've previously outlined have almost always led to rallies lasting a few weeks to a few months. Much of this was discussed in the 10/26 intermediate-term outlook.

Last week I looked at the short-covering component of the rally, and what that suggested. That research indicated rallies that begin with short covering tend to serve a *better* chance of continuing than those that are led by previously strong stocks. The outperformance of the S&P 500 over the IBD 100 off the recent lows suggested there was a good chance the rally would continue through November.

As of yet the market has shown nothing to dissuade me from the idea that it could continue upwards through at least November and perhaps longer.

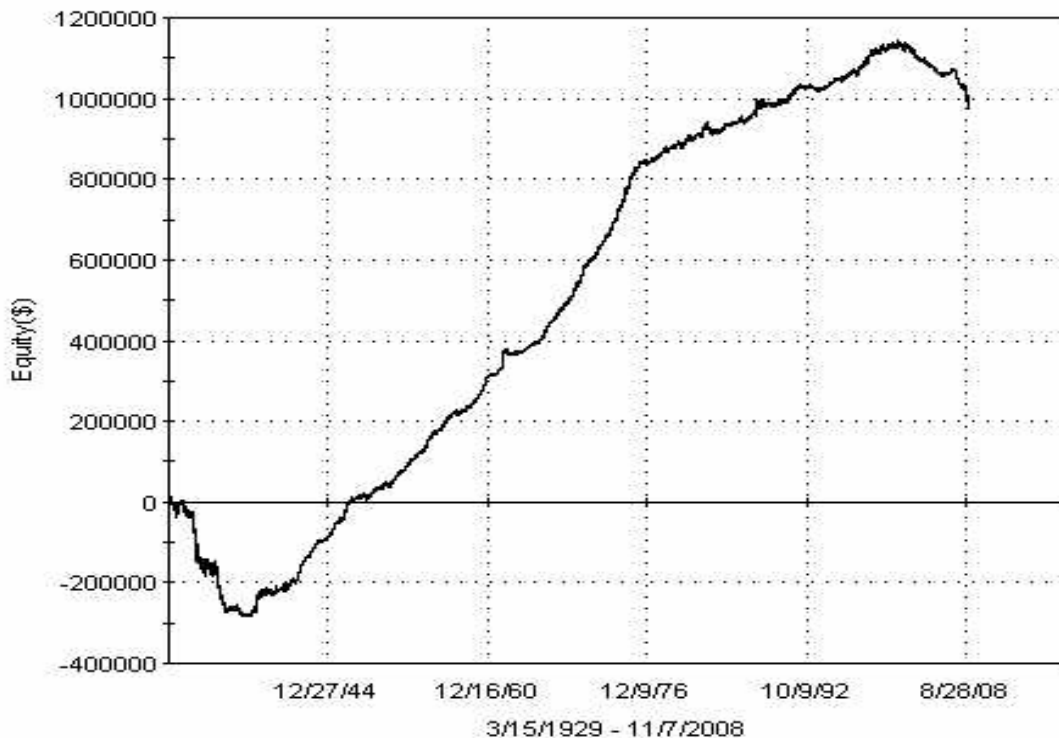
Some of the more interesting research I've done in the last few months had to do with the recent [tendency of the market to chop rather than trend](#). One of the findings of that research was that prior to 2000 the S&P 500 has most often followed up days with more positive days and down days with more negative days. The market had a strong tendency to trend in this way. In 2000 this reversed and starting in 2007 the tendency to chop has accelerated. The test went back to 1960, which is as far back as my S&P data went.

The chart below is taken from that study. It shows the results of buying the S&P on any up day and then selling and reversing the position short on any down day. An uptrending graph suggests follow-through prevails, while a downtrending graph suggests choppy conditions prevail:



As you can see, trendiness dominated until 2000 – even during bear market periods. This weekend I decided to run the same test on my Dow data going back to the beginning of 1929. Once again I found the results very interesting:

Equity Curve Detailed - +ASC:DJ30W.CSV Daily(01/02/29 16:00 - 11/07/08 16:00)



Here we see that by extending the study beyond the original 1960 date there is one more period in history where chop was as prevalent as it is today – the Great Depression. There are many differences in what is happening now versus what happened then. The world is certainly not the same as it was 70-80 years ago. But as I noted on the blog recently, study after study of historical extremes and market action are continuing to point back to this period in time as the only resemblance of today.

Difficult to see in the chart above is that the market changed from a choppy to a trending behavior about a year prior to the 1937 bottom – which was the ultimate low for the period. I believe there are several reasons it would be well worth monitoring the trend vs. chop market behavior going forward. One reason is that a shift back to a trending environment may either confirm or anticipate a bottom of some importance as it did in the 1930's. I shall be adding trend vs. chop charts to the charts section of the website this week.

In summary I believe the market has set up for a tradable rally here. I am not terribly optimistic that it will be the start of the next great bull market and that we will see steadily rising prices for the next 10 years. I am also not ready to suggest we will continue to see lower lows for the next several years. I do think we are in a very tricky period where constant evaluation and study will be important. I intend to handle it in just that way.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Trades

IP - bought @ \$11.77 limit
CBS – bought @ \$6.07 limit

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 2 (IP,CBS)

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	1.35	DJ US Financial	IYF	2.05
DJ US Regional Banks	IAT	0.00	DJ US Financial Services	IYG	1.40
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	11.27
DJ US Oil&Gas Expl & Prod	IEO	5.17	DJ US Industrial Sector	IYJ	8.43
DJ US Oil Equip & Svcs	IEZ	9.62	DJ US Consumer Goods	IYK	14.29
DJ US Pharmaceuticals	IHE	2.70	DJ US Basic Materials	IYM	2.70
DJ US Healthcare Providers	IHF	14.29	DJ US Real Estate	IYR	3.66
DJ US Medical Devices	IHI	9.76	DJ US Transportation	IYT	4.76
DJ US Aerospace & Defense	ITA	5.56	DJ US Technology Sector	IYW	8.04
DJ US Home Construction	ITB	9.52	DJ US Telecommunications	IYZ	5.26
DJ US Consumer Svcs	IYC	10.53	Nasdaq 100	QQQQ	2.00

Additional New Trade Ideas

None tonight.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY (1/4)	11/12/2008	\$88.23	\$91.17	3.33%	\$88.23	sold 1/2 on close
GOOG	11/12/2008	\$302.05	\$312.08	3.32%	\$299.99	sold 1/2 on close
IP	11/13/2008	\$11.77	\$13.77	16.99%	\$11.77	sold 1/2 on close
CBS	11/13/2008	\$6.07	\$6.43	5.93%		

Position management

- 1) Should SPY gap up tomorrow to \$91.50 or higher I will close out the rest of the trade idea at the open. Otherwise I will monitor the action in the morning and likely place a stop under the low of the 1st ½ hour to 1 hour. If it closes higher in the afternoon and the position is still open I will then look to sell at the close.
- 2) CBS finished strong. I'll look to take ½ profits at a limit of \$6.37. If it is filled I will place a stop on the rest of the idea under today's low at \$5.80.
- 3) Stops are now in place in IP and GOOG. I will also look to sell them on a large gap open. \$17.50 for IP and \$325.00 for GOOG. If not filled on open, those exit orders will be cancelled.
- 4) The GOOG trade idea is closed if the %b closes above 25.
- 5) Depending on the action in all these tomorrow I will likely send out an intraday update again as I did today.

This report has been prepared by Hanna Capital Management, LLC and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy securities. While information contained herein is believed to be accurate at the time of publication, we make no representation as to the accuracy or completeness of any data, studies, or opinions expressed and it should not be relied upon as such. Robert Hanna, Hanna Capital Management, LLC or clients of Hanna Capital Management, LLC may have positions or other interests in securities (including derivatives) directly or indirectly which are the subject of this report. This report is provided solely for the information of Hanna Capital Management, LLC clients and prospects who are expected to make their own investment decisions without reliance upon this report. Neither Hanna Capital Management, LLC nor any officer or employee of Hanna Capital Management, LLC accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. This report may not be reproduced, distributed or published by any recipient for any purpose without the prior express consent of Hanna Capital Management, LLC.

Copyright © 2008 Hanna Capital Management, LLC