

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 25, 2008

Issue 196

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 25, 2008	Up 3% with Poor Spyx or Vol	1-2 days	Bearish	-3.30%	-6.70%
November 25, 2008	2 Up Days In Chop	1-4 days	Bearish	-1.40%	-2.80%
November 24, 2008	Op-ex Friday Up > 1%	1-4 days	Bearish	-1.80%	-3.34%
November 24, 2008	50 Low High Vol then Up Hi Vol	1-3 days	Bullish	2.65%	5.10%
November 20, 2008	5% Drops	1-4 days	Bullish	5.28%	8.43%
November 20, 2008	Up Issues % 10ema < 30	1-5 days	Bullish	4.50%	7.78%
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) –somewhat bearish – updated 11/25

The market followed through on Friday's gains in a big way today. The major indices were all up strongly – generally between 5%-8%. Those numbers were despite a late-day swoon that saw the S&P lose about 2% in the last 20 minutes. Breadth was very strong. Over 90% of the volume on the NYSE was up volume. The Up Issues % came in at a very strong 87%. The fly in the ointment was the volume, which came in lighter than both the last 2 days. Also, the Quantifiable Edges Volume Spyx indicators came in weak on both the S&P 500 and the Nasdaq.

Massive rally days like today rarely occur on declining volume. When it's happened it hasn't been good. I looked for any other time the S&P rallied at least 5% and the volume came in lower than the day before. There were only 4 occurrences prior to today. They're listed below along with the 5-day returns (results based on \$100k/trade):

TradeStation Trades List									
#	Type	Date/Time	Signal	Price	Roll Over USD/Lot	Shares/Ctrts	Net Profit Profit Cum Net Profit	% Profit	Run-up DrawDown
1	Buy	10/21/07	Buy	\$258.37	\$0.00	387	(\$9,713.70)	(9.71%)	\$0.00
	Sell	10/28/07	Sell	\$233.27			(\$9,713.70)		(\$12,418.83)
2	Buy	07/29/02	Buy	\$898.96	\$0.00	111	(\$7,143.96)	(7.16%)	\$1,407.48
	Sell	08/05/02	Sell	\$834.60			(\$7,143.96)		(\$7,272.72)
3	Buy	09/30/08	Buy	\$1,166.36	\$0.00	85	(\$14,461.05)	(14.59%)	\$56.95
	Sell	10/07/08	Sell	\$996.23			(\$14,461.05)		(\$14,461.05)
4	Buy	10/13/08	Buy	\$1,003.35	\$0.00	99	(\$1,777.05)	(1.79%)	\$4,055.04
	Sell	10/20/08	Sell	\$985.40			(\$1,777.05)		(\$13,614.48)

Abysmal returns. Even the 10/13/08 instance which only lost 1.79% had a drawdown of over 13.5% in the first three days.

Low levels of Volume Spyx have typically led to market underperformance. This is especially true when they occur on an up day. There have only been 2 instances where the S&P 500 Volume Spyx has come in under 40 and the market has gained 5%. Therefore I loosened the parameters to a 3% gain.

SPX closes > 3% higher. SPYX < 40.										
Buy SPX on close. Sell X days later. \$100k/trade. 1998-present.										
X days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
10	(\$26,621.71)	7	2	5	28.57	\$3,189.54	(\$6,600.16)	0.48	0.19	(\$3,803.10)
9	(\$27,344.51)	7	2	5	28.57	\$2,073.14	(\$6,298.16)	0.33	0.13	(\$3,906.36)
8	(\$26,492.14)	7	2	5	28.57	\$2,153.73	(\$6,159.92)	0.35	0.14	(\$3,784.59)
7	(\$18,594.05)	7	2	5	28.57	\$2,753.29	(\$4,820.13)	0.57	0.23	(\$2,656.29)
6	(\$23,775.64)	7	2	5	28.57	\$2,841.23	(\$5,891.62)	0.48	0.19	(\$3,396.52)
5	(\$25,464.21)	7	2	5	28.57	\$2,087.20	(\$5,927.72)	0.35	0.14	(\$3,637.74)
4	(\$16,404.63)	7	4	3	57.14	\$1,181.19	(\$7,043.13)	0.17	0.22	(\$2,343.52)
3	(\$12,881.97)	7	3	4	42.86	\$1,483.07	(\$4,332.79)	0.34	0.26	(\$1,840.28)
2	(\$20,448.38)	7	2	5	28.57	\$1,455.56	(\$4,671.90)	0.31	0.12	(\$2,921.20)
1	(\$10,883.37)	7	2	5	28.57	\$796.28	(\$2,495.19)	0.32	0.13	(\$1,554.77)

Still the number of instances is low, but a low Volume Spyx combined with a price spike higher has been a bad combination. Below are the 7 instances and their 2-day returns:

TradeStation Trades List										
#	Type	Date/Time	Signal	Price	Roll Over USD/Lot	Shares/Ctrts	Net Profit	% Profit	Run-up	DrawDown
1	Buy	09/23/98	SPYX B	\$1,066.10	\$0.00	93	(\$1,985.55)	(2.00%)	\$0.00	
	Sell	09/25/98	Sell	\$1,044.75			(\$1,985.55)			(\$3,073.65)
2	Buy	10/28/99	SPYX B	\$1,342.44	\$0.00	74	\$864.32	0.87%	\$2,277.72	
	Sell	11/01/99	Sell	\$1,354.12			\$864.32			\$0.00
3	Buy	05/30/00	SPYX B	\$1,419.56	\$0.00	70	\$2,046.80	2.06%	\$2,046.80	
	Sell	06/01/00	Sell	\$1,448.80			\$2,046.80			(\$284.20)
4	Buy	12/05/00	SPYX B	\$1,376.56	\$0.00	72	(\$2,376.72)	(2.40%)	\$0.00	
	Sell	12/07/00	Sell	\$1,343.55			(\$2,376.72)			(\$2,685.60)
5	Buy	04/01/08	SPYX B	\$1,370.15	\$0.00	72	(\$60.48)	(0.06%)	\$561.60	
	Sell	04/03/08	Sell	\$1,369.31			(\$60.48)			(\$825.84)
6	Buy	10/20/08	SPYX B	\$985.40	\$0.00	101	(\$8,950.62)	(8.99%)	\$4.04	
	Sell	10/22/08	Sell	\$896.78			(\$8,950.62)			(\$11,068.59)
7	Buy	11/04/08	SPYX B	\$1,005.75	\$0.00	99	(\$9,986.13)	(10.03%)	\$0.00	
	Sell	11/06/08	Sell	\$904.88			(\$9,986.13)			(\$10,494.99)

Instances are low, but whether we are looking at overall market volume or the volume Spyx it would seem apparent that the low volume and the construction of it today is suggestive of a short-term pullback. To get a somewhat workable number of instances I checked to see what happened when *either* of them came in weak.

SPX closes > 3% higher. Volume Spyx < 40 or total NYSE volume lower than yesterday.										
Buy SPX on close. Sell X days later. \$100k/trade. 1998-present.										
X days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
5	(\$44,093.52)	20	9	11	45.00	\$2,757.37	(\$6,264.53)	0.44	0.36	(\$2,204.68)
4	(\$43,012.75)	21	10	11	47.62	\$1,969.02	(\$5,700.27)	0.35	0.31	(\$2,048.23)
3	(\$38,120.89)	21	9	12	42.86	\$1,644.16	(\$4,409.86)	0.37	0.28	(\$1,815.28)
2	(\$40,493.04)	21	7	14	33.33	\$1,783.65	(\$3,784.19)	0.47	0.24	(\$1,928.24)
1	(\$19,010.71)	21	8	13	38.10	\$885.01	(\$2,006.98)	0.44	0.27	(\$905.27)

The downside edge here is most pronounced in the first two days.

I've discussed incessantly over the past couple of months that the dominant characteristic of the market over the last 18 months has been the choppy action. Amazingly, today marks only the 2nd time since September that the S&P has closed higher 2 days in a row. On August 28th I showed a simple short-biased system for handling the chop. Basically, it would short the S&P any time it rose 2 days in a row. It would exit and take profits at the first close lower than the entry point. It would be allowed 4 days to work. After 4 days the trade would be covered regardless of profitability. Below are updated results for this system from June 1, 2007 – present.

TradeStation Performance Summary				Expand
All Trades				
Total Net Profit	\$48,901.82	Profit Factor	13.07	
Gross Profit	\$52,953.81	Gross Loss	(\$4,051.99)	
Total Number of Trades	48	Percent Profitable	95.83%	
Winning Trades	46	Losing Trades	2	
Even Trades	0			
Avg. Trade Net Profit	\$1,018.79	Ratio Avg. Win:Avg. Loss	0.57	
Avg. Winning Trade	\$1,151.17	Avg. Losing Trade	(\$2,026.00)	
Largest Winning Trade	\$8,783.02	Largest Losing Trade	(\$3,230.74)	
Max. Consecutive Winning Trades	19	Max. Consecutive Losing Trades	1	
Avg. Bars in Winning Trades	2.72	Avg. Bars in Losing Trades	5.00	
Avg. Bars in Total Trades	2.81			

Here we have another bit of evidence strongly suggesting downside over the next few days.

The [Aggregator](#) chart has been dramatically altered by today's action:



Both the green Aggregator line and the black differential line have gone from strongly above to now below the 0 line on the chart. The Aggregator is still only slightly negative but is set to decrease further tomorrow as the bullish studies begin to drop off. It would seem with the combination of the bearish studies above, the negatively configured Aggregator, the short-term overbought nature of the market and the fact that we're in the worst bear market in perhaps 70 years that an aggressive short position would be obvious here. Not necessarily.

While I'm interested in establishing a small short, I'm not interested in getting aggressive with it. The caveat to all this is the position of the market. Remember, we are coming off historically oversold conditions and the market is sorely overdue for an intermediate-term rally as well. The most dangerous time to short is often when the market is bouncing strongly from a possible bottom. During such thrusts the market is capable of becoming extremely overbought before pulling back. For examples you may examine the August 2007, October 2002, and September 2001 bottoms.

In summary – bearish, but cautious today. I'll look to dip my toe short, but risks are a bit higher here than if the market was in the middle of a consolidation. See trade idea section below for details.

Intermediate-term Outlook (1 week – 2 months)–neutral -updated 11/24

I have very little to say from an intermediate-term standpoint this week. The market has several times in the last 2 months reached levels that have nearly always led to a sizable rally over at least a period of a few weeks to a few months. This market's failure to do so is just another example of the historical extremes we are hitting.

Of course as I mentioned last week, we have had two rallies in the last month and a half that were near or above 20%. The problem was that the first one lasted a day and a half and the second one lasted six days. It's possible that the intermediate-term rally that I've been expecting has come in condensed versions, but it seems unlikely. At some point soon I expect this market to rally for long enough to convince a great number of people that the worst is behind us.

Against the current backdrop, though, I'll need to see some strong evidence that a bounce is likely to turn into something more substantial. Often evidence of this sort takes the form of a change in the market's character. I'll be watching closely to try and observe such changes but with the current rally less than 1 day old it's a bit too early for me to make any such observations.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Trades

All Catapult positions were exited today either via stops or at the close. Several of them failed to hit their exit triggers and they will continue to be tracked in the "Broad Market Large Cap CBI" below. I may consider re-entering some positions should they pull back favorably.

Catapult for ETF's Trades

None new

Broad Market Large Cap CBI – 7/4 (GD-3, AA, DD, C, MDT)

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	12.79
DJ US Insurance Index	IAK	8.11	DJ US Financial	IYF	5.82
DJ US Regional Banks	IAT	1.25	DJ US Financial Services	IYG	2.80
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	13.38
DJ US Oil&Gas Expl & Prod	IEO	6.90	DJ US Industrial Sector	IYJ	8.05
DJ US Oil Equip & Svcs	IEZ	15.38	DJ US Consumer Goods	IYK	9.52
DJ US Pharmaceuticals	IHE	5.41	DJ US Basic Materials	IYM	21.62
DJ US Healthcare Providers	IHF	18.37	DJ US Real Estate	IYR	9.76
DJ US Medical Devices	IHI	17.07	DJ US Transportation	IYT	9.52
DJ US Aerospace & Defense	ITA	8.33	DJ US Technology Sector	IYW	4.52
DJ US Home Construction	ITB	9.52	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	14.47	Nasdaq 100	QQQQ	7.00

CBI levels remain high across the board. More of a bounce is needed to work them off.

Additional New Trade Ideas

SPY – short ¼ index position @ \$86.75. If not filled during the day, short on close @ \$85.50 limit. I'm hoping to get in near Monday's high. If I don't get a fill there, then I'll look to short basically any close higher. Leaving plenty of size for scaling in should it continue to rally.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
GD	11/18/2008	\$53.51	\$50.49	-5.64%		<i>sold on close</i>
GD	11/19/2008	\$53.24	\$50.49	-5.17%		<i>sold on close</i>
GD	11/20/2008	\$48.67	\$50.49	3.74%		<i>sold on close</i>
SPY	11/20/2008	\$75.45	\$82.48	9.32%		<i>Avg sale price shown</i>
BAC	11/21/2008	\$11.25	\$13.04	15.91%		<i>Avg sale price shown</i>
CBS	11/21/2008	\$4.51	\$5.60	24.17%		<i>Avg sale price shown</i>
DD	11/21/2008	\$21.95	\$24.29	10.66%		<i>sold on close</i>
GS	11/21/2008	\$52.00	\$58.17	11.87%		<i>Avg sale price shown</i>
TYC	11/21/2008	\$15.65	\$18.69	19.42%		<i>Avg sale price shown</i>

I was a bit too quick with the intraday exits – especially with regards to BAC and GS. Still, some impressive gains over the last few days are helping to make November a very good month.

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