

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

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December 3, 2008

Issue 201

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## 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
December 2, 2008	5% Drop	1-4 days	Bullish	5.30%	8.50%
November 28, 2008	RSI Thrust	1-4 days	Bullish	1.70%	3.60%
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) –neutral – updated 12/3*

The market moved strongly higher Tuesday, aided by a gap opening and a sharp run up into the close. Breadth was strong as NYSE advancers led decliners by 3:1 and up volume made up nearly 89% of total volume. Total volume rose but only slightly and to a level that was close to the 50-day average.

Even with the strong move Tuesday I struggled tonight trying to find a clear edge. One thing I looked at was performance following days that gapped higher by at least 1% and then tacked on at least another 1% by the close. Over the next several days it was a 50/50 proposition. Among other things I also looked at performance after a drop of at least 5% was followed by a rally of at least 3%. There have been 8 occurrences. Over the next 2-5 days 4 closed up and 4 closed down. Basically everything I looked at came up with empty.

It doesn't help matters that we're in the middle of a range. Risk/reward is best at the outer edges of ranges – not in the middle.

The [Aggregator](#) chart is updated below:



Both the green Aggregator line and the black differential line remained above zero today suggest that the market has underperformed expectations over the last few days and expectations are positive over the next few days. Last night's cautious limit on close order in SPY was obviously not triggered today. While the Aggregator positioning is bullish I'm not keen on buying in after a day where the market has just risen% and remains squarely range-bound. We were able to book some nice profits yesterday afternoon. Rather than force the issue I prefer to wait for a clearer edge to appear.

Individual names and etf's also haven't been setting up much the last few days. Automation (AN) was the only stock to make the triggers list tonight as a potential short setup. At the current time there's just not a lot of strong edges identified by our systems.

As a side note, I hope to have a few more systems pages set up by the end of the week. There are more that I haven't gotten to yet.

***Intermediate-term Outlook (2 weeks – 2 months)–slightly bullish -updated 12/1***

The market has managed to bounce strongly from levels that were **extremely oversold based on historical measures**. Most of the time in the past this has led to continued follow through over the next few weeks or months. This is the third try for such a rally since early October. The first two attempts quickly died out.

The S&P has already rallied over 19% off its lows. It rallied about 12% just last week. In the November 2nd Letter I showed a study that compared the 1<sup>st</sup> week gains of the S&P off the lows with the 1<sup>st</sup> week gains of the IBD 100. The IBD 100 is an active index whose components change from week to week. It is compiled and tracked by Investors Business Daily and it is supposed to represent leading stocks.

The premise of the study was that outperformance of the S&P 500 over the IBD 100 could suggest a rally driven by short-covering as laggards were outperforming leaders. What was found out was that this kind of short-covering is desirable at the beginning of a new rally. Those attempts that saw the IBD 100 lag in week one actually performed quite a bit better than those that didn't. While the October attempts struggled I'd still consider it a good sign that the S&P has performed so strongly as compared to the IBD 100 over the last week.

Another notable occurrence from last week is the possible direction change in the trend vs. chop chart, which can be found on the website [by clicking here](#). While it's too early to know for sure, it appears the trend vs. chop chart is also attempting to put in a bottom. This would signal a character change for the market as the environment could move from one where directional moves are more often reversed strongly on a daily basis to one that favors follow-through day to day. The last such attempt to move from a choppy to a trendy environment was in early October and that reverted to choppy very quickly. I'll continue to keep an eye on this attempt.

Basically I'm seeing evidence that would suggest the market got so overdone and has bounced so violently that it is likely to put in a rally that could last from a few weeks to a few months. Unfortunately many of the same indications were given at the October rally attempts. Should the pullback manage to put in a higher low, which seems likely at this point, I will likely begin to trade with a bit of a bullish bias.

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

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

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

MDT is still officially open although we exited a while ago.

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

None new

#### ***Broad Market Large Cap CBI – 1 (MDT)***

#### ***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	2.33
DJ US Insurance Index	IAK	0.00	DJ US Financial	IYF	0.34
DJ US Regional Banks	IAT	0.00	DJ US Financial Services	IYG	0.00
DJ US Utilities	IDU	0.00	DJ US Healthcare	IYH	2.82
DJ US Oil&Gas Expl & Prod	IEO	3.45	DJ US Industrial Sector	IYJ	0.00
DJ US Oil Equip & Svcs	IEZ	1.92	DJ US Consumer Goods	IYK	0.68
DJ US Pharmaceuticals	IHE	0.00	DJ US Basic Materials	IYM	1.35
DJ US Healthcare Providers	IHF	4.08	DJ US Real Estate	IYR	1.22
DJ US Medical Devices	IHI	4.88	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	2.19	Nasdaq 100	QQQQ	2.00

### **Additional New Trade Ideas**

*None tonight*

### **Active Trades Table**

None.

### **November Final Trade Idea Results**

Below are the results for all trade ideas closed in November. Of course I've written a fair share of explanation and caveats before you get to them. It was an especially good month in large part to the Catapult trades. Months like November are exceptional and I'd be surprised to see another month with numbers this gaudy any time soon.

*I don't suggest position sizes. The primary reason for this is I'm not acting as a financial advisor. I don't feel it is appropriate to suggest allocation sizes without understanding someone's financial situation and risk tolerance. Even for my own trading I run different portfolios with different levels of aggressiveness. For instance, my most aggressive portfolio is my IRA. Here I may use options to sometimes get 400-500% leveraged. The partnership I manage on the other hand takes much more conservative stances and rarely reaches or exceeds 100% exposure.*

*Since I don't suggest position sizes this is not truly a performance report, but rather a trade idea scorecard. Therefore, no matter how objective I try to be the reporting of the results is always going to be skewed depending on how you approach the trades. For instance, I always recommend scaling into the Catapult positions in 3 parts, whereas the "System" trades (whatever system I unveil other than Catapult) are normally one entry. The "QE Index" trades I normally recommend scaling into as well. For my own trading I normally trade larger size with a Catapult than most "system" trades since Catapult is my favorite system. I trade much much larger size with the index trades than any of the individuals.*

*I also control my exposure by limiting the total amount invested per day. As I mentioned, this will very depending on the account I'm trading. My most aggressive account I may put in up to 100%/day and get heavily leveraged using options. A conservative account may max out at 15%-20% per day.*

*I've also mentioned in the past that days with large numbers of triggers tend to produce better results than those with less triggers. Also, the later trades in a cluster often provide profits large enough to overshadow the early losing trades in a cluster. Therefore, one way to play the Catapult trades is to only begin taking them once there are several active. However they are taken, they typically provide 1-2 excellent opportunities to profit greatly each year. November was one of those times. October, January and March also provided nice opportunity. June/July was a difficult group of trades.*

*It's unlikely anyone would have taken all of the trades with equal amounts, so results could vary greatly depending on your approach.*

With all that out of the way, below is a complete list of November's trade ideas:

**Trades Ideas for November:**

Security	Type	Strategy	Position	Entry Dt	Entry Prc	Exit Date	Exit Prc	Pct G/L
QQQQ	Index	QE Index	Short	10/31/2008	\$32.84	11/5/2008	\$32.30	1.7%
SPY	Index	QE Index	Long	11/12/2008	\$88.23	11/14/2008	\$89.70	1.7%
GOOG	Stock	QE System	Long	11/12/2008	\$302.05	11/17/2008	\$310.02	2.6%
IP	Stock	Catapult	Long	11/13/2008	\$11.77	11/17/2008	\$12.77	8.5%
CBS	Stock	Catapult	Long	11/13/2008	\$6.07	11/18/2008	\$6.24	2.8%
SPY	Index	QE Index	Long	11/18/2008	\$85.15	11/19/2008	\$85.39	0.3%
GD	Stock	Catapult	Long	11/18/2008	\$53.51	11/24/2008	\$50.49	-5.6%
GD	Stock	Catapult	Long	11/19/2008	\$53.24	11/24/2008	\$50.49	-5.2%
GD	Stock	Catapult	Long	11/20/2008	\$48.67	11/24/2008	\$50.49	3.7%
SPY	Index	QE Index	Long	11/20/2008	\$75.45	11/24/2008	\$82.48	9.3%
BAC	Stock	Catapult	Long	11/21/2008	\$11.25	11/24/2008	\$13.04	15.9%
CBS	Stock	Catapult	Long	11/21/2008	\$4.51	11/24/2008	\$5.60	24.2%
DD	Stock	Catapult	Long	11/21/2008	\$21.95	11/24/2008	\$24.29	10.7%
GS	Stock	Catapult	Long	11/21/2008	\$52.00	11/24/2008	\$58.17	11.9%
TYC	Stock	Catapult	Long	11/21/2008	\$15.65	11/24/2008	\$18.69	19.4%
SPY	Index	QE Index	Short	11/25/2008	\$87.30	11/25/2008	\$86.51	0.9%
November Totals								102.7%

<b>November Summary Breakdown</b>									
	Trades	Wins	Losses	Win %	Avg Win	Avg Loss	Avg Trade	Profit Factor	Total Gains
Total	16	14	2	87.50%	8.11%	-5.40%	6.42%	10.50	102.7%
Index	5	5	0	100.00%	2.76%	na	2.76%	na	13.8%
Catapult	10	8	2	80.00%	12.13%	-5.40%	8.63%	-8.98	86.3%
System	1	1	0	100.00%	2.60%	na	2.60%	na	2.6%

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