

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 3, 2009

Volume 2 Issue 22

## 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
<b>Active</b>					
February 2, 2009	2 Down In Chop	1-3 days	Bullish	1.60%	3.40%
<b>January 30, 2009</b>	<b>Gap &amp; Crap</b>	<b>1-3 days</b>	<b>Bearish</b>	<b>-3.40%</b>	<b>-6.40%</b>
January 30, 2009	2.5% - 5% Drop During Bear	1-3 days	Bearish	-4.90%	-9.40%
<b>January 29, 2009</b>	<b>Gap Up N Go</b>	<b>1-4 days</b>	<b>Bearish</b>	<b>-3.70%</b>	<b>-7.70%</b>
<b>January 28, 2009</b>	<b>3 Up Days &lt; 200 Declining Vol</b>	<b>1-10 days</b>	<b>Bearish</b>	<b>-3.15%</b>	<b>-5.70%</b>
<b>Jan 22 and Jan 28</b>	<b>Tight range Inside Days</b>	<b>1-6 days</b>	<b>Bearish</b>	<b>-2.60%</b>	<b>-4.90%</b>
<b>Active - Long Term</b>					
December 18, 2008	Break above 50-day		Neutral - Trading Range		
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		
<b>Dropped Tonight</b>					
January 5, 2009	Appel Breadth Thrust	1-20 days	Bullish	3.70%	5.70%
<b>January 27, 2009</b>	<b>SPX Rally On Lightest Vol in 10</b>	<b>1-5 days</b>	<b>Bearish</b>	<b>-2.15%</b>	<b>-4.20%</b>
<b>February 2, 2009</b>	<b>Last Friday of Month Drops 1%</b>	<b>1 day</b>	<b>Bearish</b>	<b>-1.50%</b>	<b>-3.80%</b>

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*.

### **Short-term Outlook (1-5 days) – updated 2/2 – neutral**

A big gap down Monday morning found support and the market was able to rally for much of the day. When it was over the results were mixed as the Nasdaq and small caps were positive while the S&P and Dow were negative. NYSE breadth was slightly negative while Nasdaq breadth was somewhat positive. Volume came in lower on both exchanges.

It's fairly rare to have the Nasdaq gain more than 1% on a day the S&P finishes lower. In fact it has only happened 38 times since the inception of the Nasdaq in 1971. About 2/3 of those occurrences took place between 1998 and 2002. Unfortunately looking at results following such instances I was unable to extract an edge either way. I did find it interesting that even as volatile as the market has been during the recent bear, this is the 1<sup>st</sup> time this has happened since 2002.

This morning I sent out a special notice to subscribers that the market was near a 2% gap down. I linked to a blog study which showed every 2% gap down and how long until the SPY closed above the gap open price. After sending the note, the SPY recovered some of its losses prior to the open. The 2% drop criteria therefore was not quite met. Still, the big gap lower led to a move higher during the day.

In the past when I've looked at large gaps lower that reversed they've exhibited bearish tendencies. Examples of this could be found in the 1/9/9, 12/4/8 and 11/28/8 Subscriber Letters. What's common among all those examples is that the intraday move back higher creates a positive close on the day. Today the SPY failed to close higher. My first test suggested today's action was strongly bullish:

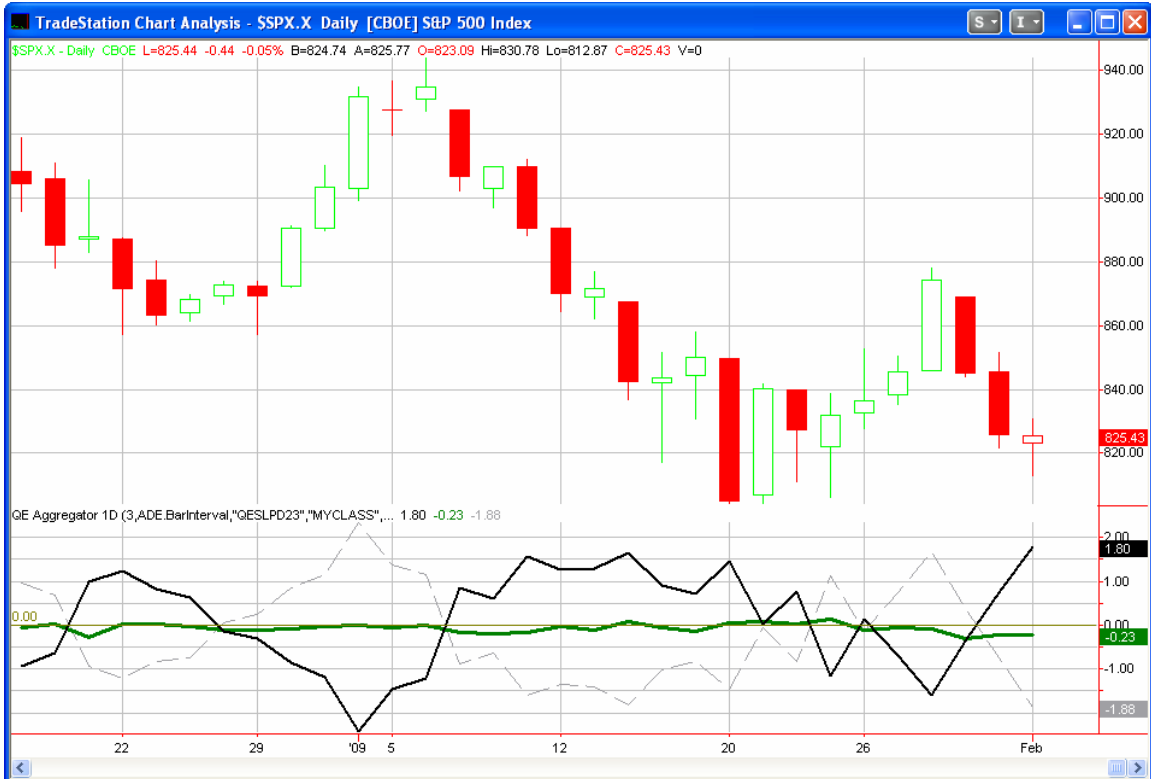
<i>SPY gaps lower by at least 1%. It then gains over 1% from open to close but fails to close positive on the day.</i>										
<i>Buy on close. Sell X days later. 100k/trade. 1993-present.</i>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
2	\$50,051.59	20	17	3	85.00	\$3,264.33	(\$1,814.03)	1.80	10.20	\$2,502.58
1	\$37,836.93	20	14	6	70.00	\$3,271.13	(\$1,326.48)	2.47	5.75	\$1,891.85

The S&P 500 today only closed lower by 0.05%. So what if it had ended up closing just slightly higher? Below is a study that addresses this:

<i>SPY gaps lower by at least 1%. It then gains over 1% from open to close and closes positive on the day.</i>										
<i>Buy on close. Sell X days later. 100k/trade. 1993-present.</i>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
2	(\$14,814.00)	33	16	17	48.48	\$1,452.63	(\$2,238.59)	0.65	0.61	(\$448.91)
1	(\$12,203.37)	33	14	19	42.42	\$1,373.41	(\$1,654.27)	0.83	0.61	(\$369.80)

Since the SPY closed marginally lower it falls into the 1<sup>st</sup> camp and not the 2<sup>nd</sup>. While the tests are black and white, reality may be a bit more grey. With the close so near breakeven I've decided not to include the above among the active studies.

With all that in mind tonight's [Aggregator](#) chart is below:



The green Aggregator and black differential lines remain strongly opposed to each other. The differential line is showing that the market has underperformed expectations over the last 3 days as much as it has in months. The Aggregator is still suggesting more downside is possible. It should be noted when looking at the studies list that most of the bearish studies have hit their lower target price and may not wield as much influence anymore. Most of them are expiring in the next few days anyway. The Aggregator chart is strongly split. Meanwhile the S&P is in a trading range. Neither one of these conditions is appealing. Combined they make me want to sit out one more day and see what sets up. There is one individual stock trade idea below.

**Intermediate-term Outlook (2 weeks – 2 months)–neutral -updated 2/2**

I looked at a few things from a little bit longer-term perspective this weekend. The S&P 500 has now closed down 4 weeks in a row. I checked to see if 4 lower weekly closes suggested an edge. Results below:

<b>SPX down 4 weeks in a row.</b>										
<b>Buy on close. Sell X weeks later. \$100k/trade. 1987-present.</b>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
10	\$48,015.62	54	33	21	61.11	\$5,563.60	(\$6,456.34)	0.86	1.35	\$889.18
9	\$40,592.46	56	32	24	57.14	\$5,369.25	(\$5,467.65)	0.98	1.31	\$724.87
8	\$50,995.86	57	32	25	56.14	\$5,231.00	(\$4,655.84)	1.12	1.44	\$894.66
7	\$46,230.73	58	34	24	58.62	\$4,759.93	(\$4,816.95)	0.99	1.40	\$797.08
6	\$52,869.27	59	33	26	55.93	\$4,693.49	(\$3,923.69)	1.20	1.52	\$896.09
5	\$54,791.42	59	34	25	57.63	\$4,210.57	(\$3,534.72)	1.19	1.62	\$928.67
4	\$19,033.43	59	31	28	52.54	\$3,793.51	(\$3,520.19)	1.08	1.19	\$322.60
3	\$26,545.00	59	34	25	57.63	\$2,836.35	(\$2,795.64)	1.01	1.38	\$449.92
2	\$12,459.35	59	32	27	54.24	\$2,657.04	(\$2,687.63)	0.99	1.17	\$211.18
1	\$17,256.79	59	36	23	61.02	\$1,777.65	(\$2,032.11)	0.87	1.37	\$292.49

While there is a very slight upside bias it is nothing I would consider basing a trade on.

The January effect is a well known study from the Stock Traders Almanac. It states that “as goes January, so goes the year”. In other words, if January closes down, there is a good chance the entire year will close down. Of course the bear case has a head start. I decided to eliminate that head start and look at performance from the end of January forward. Below performance is shown from the end of January to the end of the year.

<b>SPX closes lower in January.</b>										
<b>Buy at close. Sell X months later. \$100k/trade. 1960-present.</b>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
11	(\$47,567.58)	18	9	9	50.00	\$10,000.30	(\$15,285.59)	0.65	0.65	(\$2,642.64)
10	(\$56,286.10)	18	8	10	44.44	\$9,503.63	(\$13,231.51)	0.72	0.57	(\$3,127.01)
9	(\$70,879.26)	18	8	10	44.44	\$7,353.36	(\$12,970.61)	0.57	0.45	(\$3,937.74)
8	(\$81,899.17)	18	8	10	44.44	\$6,661.22	(\$13,518.89)	0.49	0.39	(\$4,549.95)
7	(\$43,885.48)	18	7	11	38.89	\$7,979.11	(\$9,067.20)	0.88	0.56	(\$2,438.08)
6	(\$53,810.18)	18	8	10	44.44	\$6,800.71	(\$10,821.58)	0.63	0.50	(\$2,989.45)
5	(\$53,532.70)	18	7	11	38.89	\$6,274.77	(\$8,859.65)	0.71	0.45	(\$2,974.04)
4	(\$21,887.49)	18	10	8	55.56	\$4,686.30	(\$8,593.81)	0.55	0.68	(\$1,215.97)
3	(\$7,998.32)	18	9	9	50.00	\$3,468.34	(\$4,357.04)	0.80	0.80	(\$444.35)
2	(\$5,965.88)	18	6	12	33.33	\$3,936.34	(\$2,465.33)	1.60	0.80	(\$331.44)
1	(\$24,782.03)	18	5	13	27.78	\$2,210.29	(\$2,756.42)	0.80	0.31	(\$1,376.78)

What strikes me here is that other than the first two months, wins and losses are almost dead even. Any bearish case is very slight and based upon the Win/Loss Ratio. I also looked at it using the Dow going back to 1920:

<b>Dow closes lower in January.</b>										
<b>Buy at close. Sell X months later. \$100k/trade. 1920-present.</b>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
11	\$93,414.67	30	15	15	50.00	\$15,810.85	(\$9,583.21)	1.65	1.65	\$3,113.82
10	\$49,283.15	30	13	17	43.33	\$15,653.97	(\$9,071.67)	1.73	1.32	\$1,642.77
9	\$8,519.35	30	14	16	46.67	\$11,317.60	(\$9,370.44)	1.21	1.06	\$283.98
8	(\$7,747.59)	30	13	17	43.33	\$9,790.42	(\$7,942.53)	1.23	0.94	(\$258.25)
7	\$22,837.72	30	16	14	53.33	\$7,949.61	(\$7,454.01)	1.07	1.22	\$761.26
6	(\$5,962.86)	30	14	16	46.67	\$9,087.40	(\$8,324.15)	1.09	0.96	(\$198.76)
5	(\$72,220.54)	30	13	17	43.33	\$7,591.34	(\$10,053.41)	0.76	0.58	(\$2,407.35)
4	(\$39,658.16)	30	15	15	50.00	\$6,603.48	(\$9,247.35)	0.71	0.71	(\$1,321.94)
3	(\$11,533.00)	30	16	14	53.33	\$5,136.93	(\$6,694.56)	0.77	0.88	(\$384.43)
2	\$5,689.22	30	13	17	43.33	\$4,624.38	(\$3,201.63)	1.44	1.10	\$189.64
1	(\$3,683.40)	30	15	15	50.00	\$3,084.60	(\$3,330.16)	0.93	0.93	(\$122.78)

Here again the winners and losers are about even for the rest of the year. I see no significant edge here.

I also broke January's performance down by percent lost to see if that made a difference looking forward.

<b>SPX closes January down X%.</b>										
<b>Buy on close. Sell 11 months later. 1960-present.</b>										
X%	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
0	(\$47,567.58)	18	9	9	50.00	\$10,000.30	(\$15,285.59)	0.65	0.65	(\$2,642.64)
0.01	(\$39,286.21)	16	8	8	50.00	\$10,957.82	(\$15,868.60)	0.69	0.69	(\$2,455.39)
0.02	\$4,312.23	11	6	5	54.55	\$10,715.82	(\$11,996.54)	0.89	1.07	\$392.02
0.03	(\$31,041.17)	9	4	5	44.44	\$7,235.38	(\$11,996.54)	0.60	0.48	(\$3,449.02)
0.04	(\$22,706.69)	8	4	4	50.00	\$7,235.38	(\$12,912.05)	0.56	0.56	(\$2,838.34)
0.05	(\$29,840.73)	6	3	3	50.00	\$5,470.16	(\$15,417.07)	0.35	0.35	(\$4,973.46)

Doesn't seem to matter much here. Each level shows about a 50% chance of success. Let's again look at the Dow under such circumstances:

<b>Dow closes January down X%.</b>										
<b>Buy on close. Sell 11 months later. 1920-present.</b>										
X%	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fac	Avg Trade
0	\$93,414.67	30	15	15	50.00	\$15,810.85	(\$9,583.21)	1.65	1.65	\$3,113.82
0.01	\$34,832.11	25	12	13	48.00	\$14,463.36	(\$10,671.40)	1.36	1.25	\$1,393.28
0.02	\$19,334.61	20	10	10	50.00	\$11,341.61	(\$9,408.15)	1.21	1.21	\$966.73
0.03	(\$9,582.63)	17	8	9	47.06	\$8,711.11	(\$8,807.95)	0.99	0.88	(\$563.68)
0.04	(\$35,429.05)	12	5	7	41.67	\$6,670.39	(\$9,825.86)	0.68	0.48	(\$2,952.42)
0.05	\$8,921.66	8	5	3	62.50	\$6,670.39	(\$8,143.43)	0.82	1.37	\$1,115.21

More of the same here. Appears to be a 50-50 shot to me.

With the market still range bound, I'm still not seeing much that would lead me to strongly favor either the bullish or bearish case. My focus will remain short-term and I will look to trade both sides of the market.

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

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

#### ***Open Catapult Triggers***

None

#### ***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	0.00	DJ US Financial	IYF	0.68
DJ US Regional Banks	IAT	1.25	DJ US Financial Services	IYG	1.40
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	0.38
DJ US Oil Equip & Svcs	IEZ	0.00	DJ US Consumer Goods	IYK	0.00
DJ US Pharmaceuticals	IHE	2.70	DJ US Basic Materials	IYM	1.35
DJ US Healthcare Providers	IHF	0.00	DJ US Real Estate	IYR	0.00
DJ US Medical Devices	IHI	0.00	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	2.63
DJ US Consumer Svcs	IYC	0.44	Nasdaq 100	QQQQ	0.00

### **Additional New Trade Ideas**

*DOW – buy @ \$11.00 limit on close. Having already triggered system 80418 from the triggers list, DOW could be a Catapult candidate tomorrow should it close much lower. I'll look to take it even with a slight drop.*

### **Active Trades Table**

none

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