

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 24, 2009

Volume 2 Issue 36

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
Active					
February 24, 2009	5 Days Below Lower Bollinger	1 day	Bullish	1.50%	3.50%
February 23, 2009	CBI = 7	1-5 days	Bullish	1.80%	4.20%
February 23, 2009	Gap dn 1% Close 0.5%>open but dn	1-2 days	Bullish	3.10%	6.50%
February 23, 2009	5 Lower Closes at 50 Low	1-4 days	Bullish	2.10%	3.90%
February 20, 2009	McClellan < -200	1-6 days	Bullish	3.85%	6.92%
February 18, 2009	2.5% drop after 5-day low	1-5 days	Bullish	4.20%	7.90%
Active - Long Term					
March 17, 2008	Consumer Sentiment Stretch	1-12 months	Bullish		
Dropped Tonight					
February 20, 2009	2-day RSI<2 & SPX 50-day low	1-2 days	Bullish	2.70%	6.35%

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 2/23 – bullish

The carnage continued Monday as stocks dropped for the 6th day in a row. The major indices mostly closed about 3.5% lower today. Over the last 9 days the S&P 500 has fallen 14.5%. Today was the lowest close since 1997 and the S&P came within a whisker of taking out the November intraday lows. Breadth was solidly negative but not to a great extreme. The NYSE Up Issue % was 14% and the Up Volume % was 21%. Total volume declined quite a bit from Friday's levels.

In today's intraday update I noted that the S&P was set to close below its lower Bollinger Band for the 5th day in a row and cited some results. Below are details of that test:

S&P 500 closes below its lower Bollinger Band 5 days in a row.												
Buy on close. Sell X days later. \$100k/trade. 1960-present												
X days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade		
10	\$7,326.88	23	13	10	56.52	\$3,224.34	(\$3,458.96)	0.93	1.21	\$318.56		
9	\$17,776.14	23	13	10	56.52	\$3,212.07	(\$2,398.08)	1.34	1.74	\$772.88		
8	\$23,613.42	23	14	9	60.87	\$2,739.92	(\$1,638.38)	1.67	2.60	\$1,026.67		
7	\$15,404.13	23	13	10	56.52	\$2,527.11	(\$1,744.83)	1.45	1.88	\$669.74		
6	\$6,872.35	23	12	11	52.17	\$2,268.05	(\$1,849.47)	1.23	1.34	\$298.80		
5	(\$1,747.90)	23	13	10	56.52	\$1,663.31	(\$2,337.09)	0.71	0.93	-\$76.00		
4	\$3,402.18	23	13	10	56.52	\$1,407.71	(\$1,489.80)	0.94	1.23	\$147.92		
3	\$18,235.92	23	18	5	78.26	\$1,270.41	(\$926.27)	1.37	4.94	\$792.87		
2	\$17,185.09	23	18	5	78.26	\$1,552.33	(\$2,151.37)	0.72	2.60	\$747.18		
1	\$20,250.00	23	19	4	82.61	\$1,589.21	(\$2,486.24)	0.64	3.04	\$880.43		

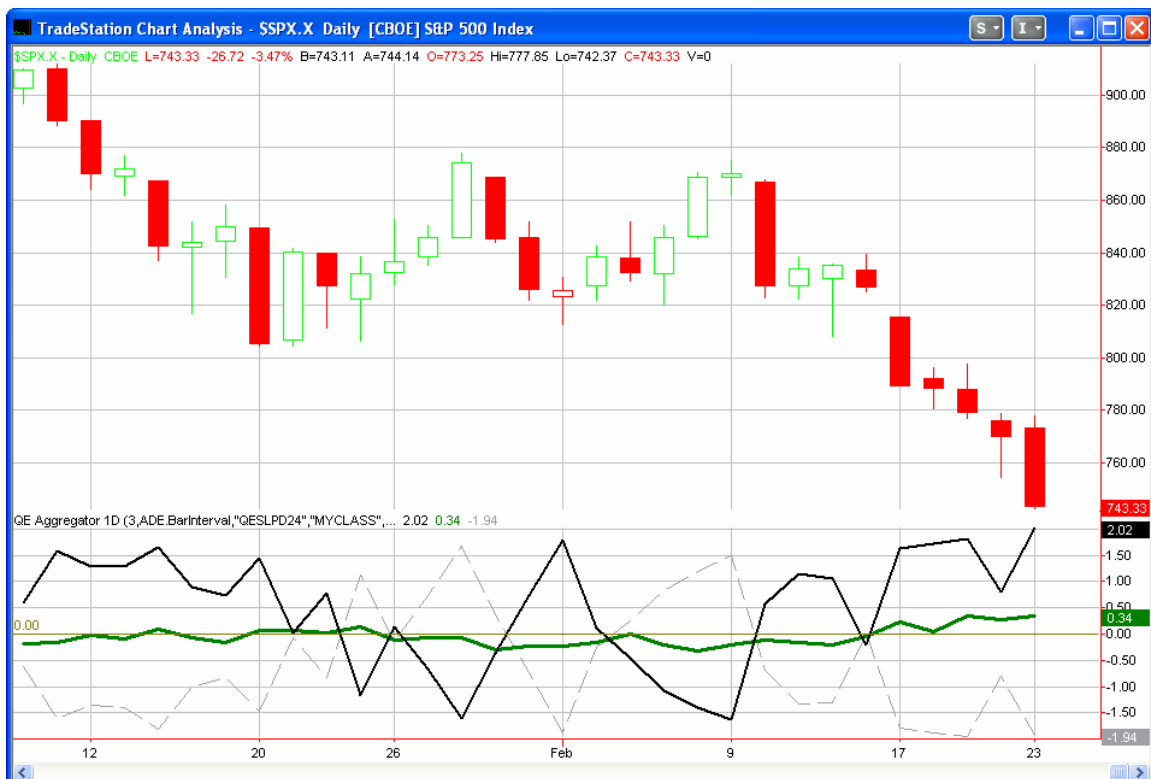
As you can see, while the edge is strong in the very short-term it doesn't last. This would suggest that if we get a bounce as expected that it may be wise to be careful not to stay in the trade too long. Monitoring the strength of the bounce will be important. Also, as I mentioned this afternoon, 22 of 23 instances closed above their trigger day close at some point in the next 3 days.

There were a few oddities about today's action that didn't seem to have much impact on results going forward. One oddity was the decline in volume while the S&P was selling off hard and closing at new lows, volume declined. I ran some tests and found the declining volume neither to be encouraging nor discomfoting. The place where we want to see volume come in is on a rebound. That's when volume will matter.

It's also unusual that new lows contracted on a day that the S&P low was over 1% lower than the day before. Again here, though, testing came up without a significant edge. Some technicians may note that the total number of new lows is quite a bit lower than when we were trading at these levels in November. While some may consider that to be a positive divergence, my past research was unable to uncover anything very positive about it. In fact, the most recent divergence of this sort happened in November when the October new lows levels failed to be breached.

The VIX did spike a bit today but the VIX:VXV ratio still stands at a fairly neutral 1.04. The McClellan Oscillator as measured by Worden Bros closed at -340, just slightly above the 10/9/08 record low of -363.

Tonight's [Aggregator](#) chart is below:



The high reading on the black differential line shows the market has underperformed expectations by a very large degree over the last 3 days. The green Aggregator line is about as positive as it has been since it is filled with nothing but bullish studies. The odds of a strong bounce in the next few days appear quite good. I'm going to look to put the last ¼ of the index allocation into SPY. Details in trade idea section below.

Intermediate-term Outlook (2 weeks – 2 months)–neutral -updated 2/23

The S&P 500 lost nearly 7% this past week and is down just shy of 15% so far for 2009. The Dow has fallen through its November lows and they aren't far behind for the S&P. The Nasdaq – with hardly any exposure to the financial sector is still above its January lows and far above the November bottom.

With the November S&P bottom fast approaching one thing we haven't seen yet is a sharp spike in the VIX. Some may find this concerning. I've looked at this a few times in the past and failed to find evidence that a VIX spike is a necessary component for making a bottom. One such study was posted to the blog on [July 1, 2008](#). Tonight I decided to compare a 50-day low that is accompanied by a VIX spike to a 50-day low that isn't.

First let's look at instances where the 50-day low is accompanied by a VIX spike:

SPX closes at a 50-day low. VIX stretched more than 10% above its 10-day ma.											
Buy on close. Sell X days later. \$100k/trade. 1990-2/20/2009.											
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade	
12	\$39,220.05	50	29	21	58.00	\$3,476.42	(\$2,933.14)	1.19	1.64	\$784.40	
11	\$42,178.74	50	29	21	58.00	\$3,166.90	(\$2,364.83)	1.34	1.85	\$843.57	
10	\$22,479.00	50	26	24	52.00	\$3,380.46	(\$2,725.54)	1.24	1.34	\$449.58	
9	\$25,834.31	55	32	23	58.18	\$3,370.74	(\$3,566.50)	0.95	1.31	\$469.71	
8	\$36,021.98	58	35	23	60.34	\$3,167.85	(\$3,254.47)	0.97	1.48	\$621.07	
7	\$34,637.59	60	34	26	56.67	\$3,151.44	(\$2,788.90)	1.13	1.48	\$577.29	
6	\$40,678.40	62	37	25	59.68	\$2,821.36	(\$2,548.47)	1.11	1.64	\$656.10	
5	\$49,714.63	66	38	28	57.58	\$2,569.25	(\$1,711.31)	1.50	2.04	\$753.25	
4	\$17,536.97	71	44	27	61.97	\$1,965.76	(\$2,553.94)	0.77	1.25	\$247.00	
3	\$30,767.71	80	52	28	65.00	\$1,823.81	(\$2,288.22)	0.80	1.48	\$384.60	
2	\$41,125.51	94	56	38	59.57	\$2,091.91	(\$2,000.56)	1.05	1.54	\$437.51	
1	\$40,629.20	135	74	61	54.81	\$1,760.50	(\$1,469.63)	1.20	1.45	\$300.96	

Now let's look at a 50-day low with a VIX spike:

SPX closes at a 50-day low. VIX not stretched more than 10% above its 10-day ma.										
Buy on close. Sell X days later. \$100k/trade. 1990-2/20/2009.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
12	\$18,727.57	36	23	13	63.89	\$3,140.27	(\$4,115.28)	0.76	1.35	\$520.21
11	\$41,069.19	37	24	13	64.86	\$3,389.58	(\$3,098.52)	1.09	2.02	\$1,109.98
10	\$38,325.09	39	27	12	69.23	\$2,925.21	(\$3,387.98)	0.86	1.94	\$982.69
9	\$56,900.65	40	27	13	67.50	\$3,392.41	(\$2,668.80)	1.27	2.64	\$1,422.52
8	\$41,206.16	40	26	14	65.00	\$3,110.93	(\$2,834.15)	1.10	2.04	\$1,030.15
7	\$43,021.13	42	28	14	66.67	\$2,791.73	(\$2,510.52)	1.11	2.22	\$1,024.31
6	\$26,299.24	42	26	16	61.90	\$2,619.28	(\$2,612.63)	1.00	1.63	\$626.17
5	\$23,026.84	47	24	23	51.06	\$2,942.60	(\$2,069.38)	1.42	1.48	\$489.93
4	\$16,421.58	49	30	19	61.22	\$2,087.02	(\$2,431.00)	0.86	1.36	\$335.13
3	\$28,712.59	51	35	16	68.63	\$1,986.15	(\$2,550.18)	0.78	1.70	\$562.99
2	\$17,981.18	62	31	31	50.00	\$1,982.54	(\$1,402.50)	1.41	1.41	\$290.02
1	\$17,533.60	76	49	27	64.47	\$1,007.94	(\$1,179.82)	0.85	1.55	\$230.71

It's more common to see a spike in the VIX than not. Comparison between the two sets of results, though, shows very little difference. This suggests the VIX is not an effective filter when considering whether a drop in the market is likely to mark a low. While I'm sure a very sharp spike would produce some bullish studies and help provide some possible juice for a rebound, it's not something I'm going to worry over a great deal.

From an intermediate-term standpoint it appears too late to get strongly bearish but without some real signs of strength too early to get strongly bullish. My summary from last week still works for me so I'll repeat it below.

As I've been saying, I expect we're likely to see a decent rally of 30% or more lasting at least 2-3 months emerge here at some point. I have serious doubts that next rally will lead to a multi-year bull market run, though. Until I see signs otherwise, I'm treating this market as one that is more similar to the 1930's than any other period in time. Past evidence of this includes volatility studies, Dow Trend vs. Chop studies, and studies of severe selloffs such as we saw in the fall. I'll be sure to revisit these studies when appropriate. For now my focus remains short-term.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

DOW (Dow Chemical) –@ \$9.29 (1/3)

DOW (Dow Chemical) –@ \$8.62 (1/3)

DOW (Dow Chemical) – bought last 1/3 position @ \$8.60

CAT – bought 1/3 position @ \$28.44

CAT – bought 1/3 position @ \$26.14

CAT – bought final 1/3 position @ \$26.66

C – (not recommended) @ \$1.95

New

PFE – buy 1/3 position @ \$13.27 limit

Catapult for ETF's Trades

DIA – bought @ \$73.73 limit

Broad Market Large Cap CBI – 8/4 (DOW-3, CAT-3, C, PFE)

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

Index	ETF	CBI %	Index	ETF	CBI %
DJ US Broker Dealers	IAI	3.45	DJ US Energy	IYE	2.33
DJ US Insurance Index	IAK	9.46	DJ US Financial	IYF	9.25
DJ US Regional Banks	IAT	21.25	DJ US Financial Services	IYG	13.99
DJ US Utilities	IDU	1.35	DJ US Healthcare	IYH	7.04
DJ US Oil&Gas Expl & Prod	IEO	5.17	DJ US Industrial Sector	IYJ	6.13
DJ US Oil Equip & Svcs	IEZ	5.77	DJ US Consumer Goods	IYK	4.76
DJ US Pharmaceuticals	IHE	10.81	DJ US Basic Materials	IYM	8.11
DJ US Healthcare Providers	IHF	2.04	DJ US Real Estate	IYR	2.44
DJ US Medical Devices	IHI	2.44	DJ US Transportation	IYT	0.00
DJ US Aerospace & Defense	ITA	2.78	DJ US Technology Sector	IYW	3.02
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	3.51	Nasdaq 100	QQQQ	2.00

Regional banks and financial services CBI% 's spiking.

Additional New Trade Ideas

See PFE from Catapult section.

SPY – buy last 1/4 allocation at \$74.75 limit. Looking to play the bounce over the next few days as discussed in the short-term outlook above.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
DOW(1/3)	2/17/2009	\$9.29	\$7.41	-20.24%		Catapult
DOW(1/3)	2/18/2009	\$8.62	\$7.41	-14.04%		Catapult
SPY(1/4)	2/18/2009	\$79.22	\$74.65	-5.77%		
DOW(1/3)	2/19/2009	\$8.60	\$7.41	-13.84%		Catapult
CAT(1/3)	2/19/2009	\$28.44	\$25.12	-11.67%		Catapult
SPY(1/4)	2/19/2009	\$78.18	\$74.65	-4.52%		
SPY(1/4)	2/20/2009	\$77.42	\$74.65	-3.58%		
CAT(1/3)	2/20/2009	\$26.14	\$25.12	-3.90%		Catapult
KBE	2/20/2009	\$10.86	\$10.88	0.18%		Catapult
CAT(1/3)	2/23/2009	\$26.66	\$25.12	-5.78%		Catapult
DIA	2/23/2009	\$73.73	\$71.15	-3.50%		Catapult

The numbers for this round of Catapult trades are looking ugly. While they'll likely bounce strongly when the market finally does, the chances of the Catapults being net winners at this point seems remote. During most selloffs you'd be seeing the number of triggers ramp up now. In this case there was only the PFE trigger this afternoon.

Getting the archives online this past weekend seems like pretty good timing. Although the current trades look pretty awful now, they normally do near a bottom. I'd encourage subscribers to go back to previous lows over the last year and see how the trades looked before and after the rebound.

While I don't believe the upcoming rebound will be nearly as strong as we saw in October and November, it could have some pretty good juice to it. A bounce anywhere near where the market is now could excite traders about the possibility of a double bottom formation. This would in turn create additional buying enthusiasm and make the bounce all that more powerful.

As I've stated before the action of the rebound may provide important clues. What we don't want to see at this point is a weak bounce on quiet volume and neutral or bearish breadth.

Sitting through a selloff like the current one can be harrowing and it can certainly test a trader's nerves. While it's conceivable the market could continue to crumble for several more days, I prefer to get my money in when I believe there is an edge and keep it there until the edge is gone. In cases like this that means selling into a bounce that will most likely be very strong.

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 © 2009 Hanna Capital Management, LLC