

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 24, 2009

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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
Active					
March 24, 2009	2% Gaps Up	1-2 days	Bearish	-3.70%	-7.70%
March 24, 2009	High Volume 1% Drop	1-6 days	Bearish	-5.30%	-9.50%
March 23, 2009	Op-ex Friday 1% Drop	1-4 days	Bearish	-2.90%	-5.20%
March 23, 2009	High Volume 1% Drop	1-5 days	Bearish	-1.50%	-3.60%
March 20, 2009	Nas Spyx < 0 whil Nas > 10ma	1-7 days	Bearish	-5.10%	-10.90%
March 20, 2009	Gap Up 1% then close negative	1-3 days	Bearish	-5.80%	-10.70%
March 19, 2009	Fed Day Spike	1-8 days	Bearish		
March 19, 2009	Appel Daily Breadth	1-20 days	Bullish		
March 16, 2009	4 Up From 200 Low	1-10 days	Bearish	-4.10%	-8.40%
Active - Long Term					
March 13, 2009	2 90% Up Days	1-25 days	Bullish	8.00%	11.40%
Dropped Tonight					
March 18, 2009	Lowest vol and highest close in 15	1-4 days	Bearish	-1.40%	-3.70%
<i>March 21, 2009</i>	<i>2 Down In Chop</i>	<i>1-3 days</i>	<i>Bullish</i>		

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 3/24 – bearish

The market put in a massive rally on Monday. The major indices all vaulted higher with the S&P 500 and Nasdaq both up close to 7% while the Russell 2000 gained 8.5%. Breadth was once again extremely strong. Volume was conspicuously light. It was the lowest reading in 4 days and also below the 10-day moving average.

The rally began with a gap up of about 2.5% this morning. As I discussed last night, extra large gaps up have a tendency to create short squeezes and often lead to further upside intraday. This was certainly the case on Monday. I've looked at large gaps a number of different ways in the past. One thing I found a while back was that 2% gaps had a tendency to pull back over the course of the next few days. Below is a table that first appeared on the blog last fall. It shows how long it took for the SPY to close below the open of an extra large (2%) gap higher.

SPY Gaps up 2% +		
Instance	Date	Closed <= Gap Open (up to 5 days)
1	9/8/1998	1 day later
2	10/6/1998	same day
3	9/3/1999	2 days later
4	6/2/2000	same day
5	12/8/2000	same day
6	12/11/2000	2 days later
7	4/5/2001	1 day later
8	9/24/2001	NO
9	7/17/2002	same day
10	7/29/2002	4 days later
11	10/15/2002	1 day later
12	10/17/2002	same day
13	4/7/2003	same day
14	8/17/2007	same day
15	12/12/2007	same day
16	3/11/2008	3 days later
17	9/8/2008	same day
18	9/19/2008	same day
19	10/7/2008	same day
20	10/9/2008	same day
21	10/13/2008	2 days later
22	10/14/2008	same day
23	10/20/2008	2 days later
24	10/28/2008	NO
25	10/30/2008	5 days later
26	11/4/2008	1 day later
27	11/21/2008	NO
28	11/24/2008	NO
29	11/25/2008	same day
30	12/8/2008	same day
31	1/28/2009	1 day later
32	3/10/2009	NO

What was once a very strong tendency now appears to have lost much of its edge as 4 of the last 9 2% Up Gaps have failed to post a close below the gap open within the next week. What's interesting about the failures is that they all occurred either 1 or 2 days after the market had closed at a 200-day low. In fact, the only one that was 2 days after was Monday 11/24/08, which was the day after the 11/21/08 occurrence that also didn't fill. Monday the market was far removed from its 200 day low. Of course SPY would need quite a pullback if it were to close below Monday's open anytime in the next few days.

I've also looked at 5% up days in the past. The 12/17/2008 Subscriber Letter contains a few studies related to such large gains. Below is an updated version of one of them:

S&P 500 rises at least 5%.										
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
8	(\$28,192.43)	12	4	8	33.33	\$4,627.33	(\$5,837.72)	0.79	0.40	(\$2,349.37)
7	(\$29,254.16)	13	5	8	38.46	\$4,223.39	(\$6,296.39)	0.67	0.42	(\$2,250.32)
6	(\$7,041.98)	13	7	6	53.85	\$4,747.38	(\$6,712.27)	0.71	0.83	(\$541.69)
5	(\$6,707.62)	13	7	6	53.85	\$5,195.41	(\$7,179.25)	0.72	0.84	(\$515.97)
4	(\$2,972.16)	13	7	6	53.85	\$5,117.37	(\$6,465.62)	0.79	0.92	(\$228.63)
3	\$9,914.44	14	6	8	42.86	\$6,214.41	(\$3,421.50)	1.82	1.36	\$708.17
2	(\$7,932.26)	14	7	7	50.00	\$3,625.43	(\$4,758.61)	0.76	0.76	(\$566.59)
1	\$4,682.45	16	6	10	37.50	\$3,226.42	(\$1,467.61)	2.20	1.32	\$292.65

Monday was the 17th day ever where the S&P 500 has put in a gain of 5% or more. Of the previous 16 instances, the only three that didn't close lower than the close of the 5% day at some point in the next 4 days were 5/27/70, 11/21/08, and 3/10/09. Here again you'll notice that each of the "failures" to pull back occurred when the 5% day came on the heels of a 200-day closing low. The low volume on Monday also stands out here. The three 5% days that failed to pull back all posted 5-day highs in volume. Monday wasn't even close and was the lowest of the last 4.

Speaking of weak volume, on November 10th I posted a study which looked at days with strong moves on light volume. Below is an updated version:

S&P 500 rises at least 2.5%. NYSE volume is under its 10ma.										
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	(\$63,218.19)	26	10	16	38.46	\$2,388.27	(\$5,443.81)	0.44	0.27	(\$2,431.47)
9	(\$73,096.53)	26	11	15	42.31	\$1,788.72	(\$6,184.83)	0.29	0.21	(\$2,811.41)
8	(\$74,768.06)	28	12	16	42.86	\$1,967.32	(\$6,148.49)	0.32	0.24	(\$2,670.29)
7	(\$69,375.00)	29	9	20	31.03	\$3,113.59	(\$4,869.87)	0.64	0.29	(\$2,392.24)
6	(\$66,110.04)	31	12	19	38.71	\$2,539.20	(\$5,083.18)	0.50	0.32	(\$2,132.58)
5	(\$70,881.03)	33	14	19	42.42	\$1,957.23	(\$5,172.75)	0.38	0.28	(\$2,147.91)
4	(\$44,141.96)	34	12	22	35.29	\$2,449.23	(\$3,342.40)	0.73	0.40	(\$1,298.29)
3	(\$42,892.41)	38	12	26	31.58	\$3,086.89	(\$3,074.43)	1.00	0.46	(\$1,128.75)
2	(\$46,204.56)	39	15	24	38.46	\$1,724.15	(\$3,002.78)	0.57	0.36	(\$1,184.73)
1	(\$2,566.75)	41	20	21	48.78	\$1,218.78	(\$1,282.97)	0.95	0.90	(\$62.60)

Such light volume moves have been punished going forward over the next couple of weeks. I also updated the statistics for the 1-week returns based on the magnitude of the low-volume move:

S&P 500 Up X%. NYSE Volume under 10-day moving average.										
Buy on close. Sell 5 days later. \$100k/trade. 1960-present.										
X% Rise	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
4	(\$37,189.49)	9	4	5	44.44	\$2,637.56	(\$9,547.95)	0.28	0.22	(\$4,132.17)
3.5	(\$47,604.91)	13	6	7	46.15	\$1,953.67	(\$8,475.27)	0.23	0.20	(\$3,661.92)
3	(\$54,081.48)	19	9	10	47.37	\$1,960.53	(\$7,172.62)	0.27	0.25	(\$2,846.39)
2.5	(\$70,881.03)	33	14	19	42.42	\$1,957.23	(\$5,172.75)	0.38	0.28	(\$2,147.91)
2	(\$54,499.83)	60	30	30	50.00	\$2,126.29	(\$3,942.95)	0.54	0.54	(\$908.33)
1.5	(\$30,180.56)	130	70	60	53.85	\$2,024.08	(\$2,864.43)	0.71	0.82	(\$232.16)

As you can see, the stronger the move higher, the stronger the ensuing pullback over the next week.

Back in November I also noted that the bearish influence of the sharp light volume rallies has been more pronounced since 2001. Below are updated tables of the same tests as shown above, but from 2001-present:

S&P 500 rises at least 2.5%. NYSE volume is under its 10ma.										
Buy on close. Sell X days later. \$100k/trade. 2001-present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
10	(\$80,073.63)	13	2	11	15.38	\$1,036.62	(\$7,467.90)	0.14	0.03	(\$6,159.51)
9	(\$79,117.01)	13	3	10	23.08	\$1,597.98	(\$8,391.10)	0.19	0.06	(\$6,085.92)
8	(\$77,044.55)	14	4	10	28.57	\$1,635.33	(\$8,358.59)	0.20	0.08	(\$5,503.18)
7	(\$61,533.13)	15	4	11	26.67	\$4,426.77	(\$7,203.66)	0.61	0.22	(\$4,102.21)
6	(\$72,467.31)	17	2	15	11.76	\$4,666.60	(\$5,453.37)	0.86	0.11	(\$4,262.78)
5	(\$76,773.02)	19	5	14	26.32	\$1,848.08	(\$6,143.81)	0.30	0.11	(\$4,040.69)
4	(\$48,603.11)	19	4	15	21.05	\$3,661.27	(\$4,216.55)	0.87	0.23	(\$2,558.06)
3	(\$44,338.48)	22	6	16	27.27	\$3,662.48	(\$4,144.58)	0.88	0.33	(\$2,015.39)
2	(\$49,720.98)	23	7	16	30.43	\$1,560.25	(\$3,790.17)	0.41	0.18	(\$2,161.78)
1	(\$7,175.43)	24	11	13	45.83	\$1,340.33	(\$1,686.08)	0.79	0.67	(\$298.98)

S&P 500 Up X%. NYSE Volume under 10-day moving average.										
Buy on close. Sell 5 days later. \$100k/trade. 2001-present.										
X% Rise	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
4	(\$42,529.34)	7	2	5	28.57	\$2,605.20	(\$9,547.95)	0.27	0.11	(\$6,075.62)
3.5	(\$52,944.76)	11	4	7	36.36	\$1,595.54	(\$8,475.27)	0.19	0.11	(\$4,813.16)
3	(\$54,653.01)	13	5	8	38.46	\$1,821.81	(\$7,970.26)	0.23	0.14	(\$4,204.08)
2.5	(\$76,773.02)	19	5	14	26.32	\$1,848.08	(\$6,143.81)	0.30	0.11	(\$4,040.69)
2	(\$69,083.12)	27	10	17	37.04	\$1,741.37	(\$5,088.05)	0.34	0.20	(\$2,558.63)
1.5	(\$48,292.27)	46	20	26	43.48	\$1,785.60	(\$3,230.94)	0.55	0.43	(\$1,049.83)

These studies seem to strongly favor a pullback in the next few days.

Also notable is that this is the third light volume rise of 2.5% or more in the last 8 days. It also occurred on 3/12 and 3/17. This would seem to further strengthen the case for a pullback.

With these studies in mind, below is tonight's [Aggregator](#) chart:



With the studies already bearish entering tonight, the new studies have pushed the green Aggregator line even farther south. Meanwhile, today's huge move has quickly moved the differential line well below 0. With both lines south of 0, this is the desired configuration when looking for a short entry.

With so many studies suggesting so strongly that the market should pull back here I'm going to be looking for a short entry. Should the S&P close higher tomorrow as well then a "2 days up in chop" entry will also trigger. I noted in last night's letter that pullback in the "2 days DOWN in chop" system like we were encountering had previously been met with large wins. That certainly happened and my concerns about playing the chop are quickly becoming alleviated.

As I usually do, I'll be looking to scale in to my index position. The move up is extremely strong and I don't want to take on too much short exposure too quickly here. I will use a limit order above the current price as detailed in the trade ideas section below. Should the market continue to rise I anticipate continuing to scale in over the next few days.

Intermediate-term Outlook (2 weeks – 2 months)–neutral -updated 3/23

Just two quick points to discuss tonight for the intermediate-term. First, while I've been expecting a substantial rally at least lasting several weeks to emerge at some point, the fact is that the current rally already ran up over 20% from low to high. On Thursday I discussed the fact that this is the third such 20% rally since the fall. The only other period of time with such a close cluster of 20% rallies occurred in 1931-33. Results were mixed following those rallies, but the ones in the fall both petered out almost

immediately. There's a possibility that the market has already come so far so fast that it may not have a lot left in this rally.

I've also been asked about the propensity of the market to test lows before forming a lasting bottom. In looking back at major bottoms in the S&P 500 from 1960 – present I did find a large percentage of them had some kind of retest. I haven't yet quantified the results, but it raises the possibility that the S&P may drop down to a few percentage points of the 666 bottom before continuing its rally.

Overall I've been quite impressed with the magnitude of the rally of the recent lows – especially from a breadth standpoint. While there's a bit of a lack of short-term bullish studies at the moment, I'm still optimistic that the breadth thrusts we've seen will help to lead this market on a rally lasting several weeks or months and taking us up 30% or more. The evidence isn't yet overwhelming so from a trading standpoint I'll forego a strong intermediate-term bias and defer to my short-term bias.

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.)

Index	ETF	CBI %	Index	ETF	CBI %
DJ US Broker Dealers	IAI	0.00	DJ US Energy	IYE	0.00
DJ US Insurance Index	IAK	0.00	DJ US Financial	IYF	0.00
DJ US Regional Banks	IAT	0.00	DJ US Financial Services	IYG	0.00
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	0.00
DJ US Oil Equip & Svcs	IEZ	0.00	DJ US Consumer Goods	IYK	0.00
DJ US Pharmaceuticals	IHE	0.00	DJ US Basic Materials	IYM	0.00
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	0.00
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	0.00	Nasdaq 100	QQQQ	0.00

Absolutely nothing.

Additional New Trade Ideas

SPY – short 1/4 index position @ \$82.89 limit. If not filled intraday short 1/4 index position @ \$82.22 limit ON CLOSE. Based on short term market outlook above, I am looking to get short on further strength.

I'll just track the SPY officially, but KO and SO from the triggers page could also provide some interesting short opportunities.

Active Trades Table

None

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