

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 28, 2009

Volume 2 Issue 80

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 | | | | | |
| April 28, 2009 | QQQQ up Nasdaq down over 0.5% | 1 day | Bearish | | |
| April 27, 2009 | Friday Follow-through | 1-2 days | Bullish | 1.80% | 3.50% |
| April 27, 2009 | Gap-n-go | 1-9 days | Bearish | -3.40% | -6.50% |
| April 24, 2009 | Russell lags S&P badly | 1-3 days | Bearish | -3.30% | -6.60% |
| April 24, 2009 | Poor Nasdaq Breadth on Up Day | 1-9 days | Bearish | -4.10% | -8.20% |
| Active - Long Term | | | | | |
| April 20, 2009 | Low Nasdaq Weekly Vol Spyx | 1-10 weeks | Bearish | | |
| April 6, 2009 | Appel Daily Breadth | 1-20 days | Bullish | | |
| March 26, 2009 | Rise after follow through day | | Bullish | 920 before 666 | |
| Dropped Tonight | | | | | |
| April 27, 2009 | 2 Days Up In Chop | 1-4 days | Bearish | | |

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 4/28 – somewhat bearish

Monday was a generally weak day for the market as most indices closed lower. It started with a substantial gap down of more than 1% for the S&P. It did manage to rally intraday before faltering early afternoon and closing back down near its open. Statistics were a bit odd. Breadth was strongly negative with the NYSE Up Issues % at 32% and the Up Volume % at 22%. Despite the large gap and lopsided breadth, volume came in at its lowest level in 10 days. The range on the S&P 500 was also the lowest in 10 days.

Low volume and low range when the market is under the 200ma is typically a bearish indication looking out over the next several days. An example of this can be seen in the below study, which was taken from the 2/10/09 Subscriber Letter.

(Stats through 2/9/09)

| SPX has NR10 day on lightest volume in 10 days and closes under 200ma. | | | | | | | | | | |
|------------------------------------------------------------------------|---------------|--------|------|--------|--------|------------|--------------|-----------|---------------|------------|
| Buy on close. Sell X days later. \$100k/trade. 1978-present. | | | | | | | | | | |
| X Days | Net Profit | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 5 | (\$53,276.24) | 82 | 37 | 45 | 45.12 | \$1,898.95 | (\$2,745.27) | 0.69 | 0.57 | (\$649.71) |
| 4 | (\$62,181.70) | 83 | 35 | 48 | 42.17 | \$1,546.80 | (\$2,423.32) | 0.64 | 0.47 | (\$749.18) |
| 3 | (\$58,491.48) | 83 | 31 | 51 | 37.35 | \$1,526.44 | (\$2,074.73) | 0.74 | 0.45 | (\$704.72) |
| 2 | (\$44,229.75) | 83 | 34 | 49 | 40.96 | \$1,266.25 | (\$1,781.27) | 0.71 | 0.49 | (\$532.89) |
| 1 | (\$28,357.47) | 89 | 38 | 51 | 42.70 | \$991.30 | (\$1,294.64) | 0.77 | 0.57 | (\$318.62) |

The issue with Monday's action is that the large gap and strongly negative breadth seem to contrast the low range and small volume. I filtered the above test further to look for other times where the NR10 and low volume occurred following a 1% gap down. Those results are below.

| SPY gaps down 1%. It then trades in the narrowest range in 10 days while NYSE volume posts a 10-day low. Close < 200ma. | | | | | | | | | | |
|-----------------------------------------------------------------------------------------------------------------------------------|-------------|--------|------|--------|--------|------------|--------------|-----------|---------------|------------|
| Buy SPY on close. Sell X days later. \$100k/trade. 1994-present. | | | | | | | | | | |
| X Days | Net Profit | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 5 | \$21,800.13 | 5 | 5 | 0 | 100.00 | \$4,360.03 | \$0.00 | 100.00 | 100.00 | \$4,360.03 |
| 4 | \$18,037.91 | 5 | 5 | 0 | 100.00 | \$3,607.58 | \$0.00 | 100.00 | 100.00 | \$3,607.58 |
| 3 | \$12,780.45 | 5 | 4 | 1 | 80.00 | \$3,363.55 | (\$673.75) | 4.99 | 19.97 | \$2,556.09 |
| 2 | \$6,593.31 | 5 | 4 | 1 | 80.00 | \$2,288.39 | (\$2,560.25) | 0.89 | 3.58 | \$1,318.66 |
| 1 | \$697.54 | 5 | 3 | 2 | 60.00 | \$1,990.66 | (\$2,637.23) | 0.75 | 1.13 | \$139.51 |

Only 5 instances, but interestingly all five of them are strongly positive. I've listed all 5 below along with their 1-week returns.

| Date/Time | Signal | Price | Roll Over USD/Lot | Shares/Ctrts | Net Profit | % Profit | Run-up DrawDown |
|-----------|--------|----------|-------------------|--------------|----------------|----------|-----------------|
| | | | | Profit | Cum Net Profit | | |
| 09/17/98 | Buy | \$102.00 | \$0.00 | 980 | \$2,332.40 | 2.33% | \$4,900.00 |
| 09/24/98 | Sell | \$104.38 | | \$2,332.40 | \$2,332.40 | | (\$2,998.80) |
| 08/12/02 | Buy | \$90.62 | \$0.00 | 1103 | \$5,272.34 | 5.27% | \$5,658.39 |
| 08/19/02 | Sell | \$95.40 | | \$5,272.34 | \$7,604.74 | | (\$2,867.80) |
| 10/14/02 | Buy | \$84.63 | \$0.00 | 1181 | \$6,542.74 | 6.55% | \$6,932.47 |
| 10/21/02 | Sell | \$90.17 | | \$6,542.74 | \$14,147.48 | | \$0.00 |
| 03/27/09 | Buy | \$81.61 | \$0.00 | 1225 | \$3,246.25 | 3.25% | \$3,675.00 |
| 04/03/09 | Sell | \$84.26 | | \$3,246.25 | \$17,393.73 | | (\$4,471.25) |
| 04/07/09 | Buy | \$81.65 | \$0.00 | 1224 | \$4,406.40 | 4.41% | \$5,985.36 |
| 04/15/09 | Sell | \$85.25 | | \$4,406.40 | \$21,800.13 | | (\$134.64) |

With just 5 instances I'm not comfortable extrapolating out the results or considering them predictive. They are strong enough, though, that I would not consider the negative effects of the original broader test influential in this case.

To my dismay I managed to take a short position in basically the only thing that went up on Monday. The fact that the QQQQ diverged so greatly from the broader Nasdaq Composite Index was especially interesting. I ran some studies to evaluate performance following other times of similar divergences.

I first started with a positive QQQQ and a Nasdaq Comp drop of at least 0.75%.

| QQQQ closes up but under the 200ma. The Nasdaq Composite drops at least 0.75% on the day. | | | | | | | | | | |
|--------------------------------------------------------------------------------------------------|---------------|--------|------|--------|--------|------------|--------------|-----------|---------------|--------------|
| Buy QQQQ on close. Sell X days later. \$100k/trade. 1999-present. | | | | | | | | | | |
| X Days | Net Profit | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 5 | (\$4,875.65) | 8 | 5 | 3 | 62.50 | \$3,845.06 | (\$8,033.65) | 0.48 | 0.80 | (\$609.46) |
| 4 | (\$27,322.63) | 8 | 3 | 5 | 37.50 | \$5,000.59 | (\$8,464.88) | 0.59 | 0.35 | (\$3,415.33) |
| 3 | (\$20,928.82) | 8 | 3 | 5 | 37.50 | \$5,462.83 | (\$7,463.46) | 0.73 | 0.44 | (\$2,616.10) |
| 2 | (\$32,805.10) | 8 | 2 | 6 | 25.00 | \$1,031.44 | (\$5,811.33) | 0.18 | 0.06 | (\$4,100.64) |
| 1 | (\$30,330.64) | 8 | 2 | 6 | 25.00 | \$1,376.10 | (\$5,513.81) | 0.25 | 0.08 | (\$3,791.33) |

Low instances, but some very large risks. The average losing trade over the next 2 days was nearly 6%. Also notable is that 7 of 8 instances closed below the trigger day close at some point in the next 3 days.

To get a few more instances I loosened the requirement to a Nasdaq drop of only 0.5%:

| <i>QQQQ closes up but under the 200ma. The Nasdaq Composite drops at least 0.5% on the day.</i> | | | | | | | | | | |
|-------------------------------------------------------------------------------------------------|---------------|--------|------|--------|--------|------------|--------------|-----------|---------------|--------------|
| <i>Buy QQQQ on close. Sell X days later. \$100k/trade. 1999-present.</i> | | | | | | | | | | |
| X Days | Net Profit | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 5 | (\$14,705.74) | 13 | 7 | 6 | 53.85 | \$4,057.16 | (\$7,184.31) | 0.56 | 0.66 | (\$1,131.21) |
| 4 | (\$25,082.76) | 14 | 5 | 9 | 35.71 | \$6,054.97 | (\$6,150.85) | 0.98 | 0.55 | (\$1,791.63) |
| 3 | (\$26,793.31) | 14 | 5 | 9 | 35.71 | \$6,139.64 | (\$6,387.94) | 0.96 | 0.53 | (\$1,913.81) |
| 2 | (\$40,769.49) | 14 | 5 | 9 | 35.71 | \$2,034.93 | (\$5,660.46) | 0.36 | 0.20 | (\$2,912.11) |
| 1 | (\$39,790.07) | 14 | 3 | 10 | 21.43 | \$1,605.14 | (\$4,460.55) | 0.36 | 0.11 | (\$2,842.15) |

A few more instances here and results are quite similar. You're still looking at a rough 1-2 days for the QQQQ. In this case 12 of 14 closed below the trigger day close at some point in the next 3 days.

I've also discussed several times lately that short-term highs in a long-term downtrend tend to lead to pullbacks over the next few days. Below is a test that combines Monday's short-term QQQQ high with its low volume:

| <i>QQQQ makes a 10-day high. It closes under the 200ma. Today's volume is the lightest in 10 days.</i> | | | | | | | | | | |
|--------------------------------------------------------------------------------------------------------|---------------|--------|------|--------|--------|------------|--------------|-----------|---------------|--------------|
| <i>Buy QQQQ on close. Sell X days later. \$100k/trade. 1999-present.</i> | | | | | | | | | | |
| X Days | Net Profit | Trades | Wins | Losses | % Wins | Avg Win | Avg Loss | W/L Ratio | Profit Factor | Avg Trade |
| 5 | (\$19,497.18) | 14 | 5 | 9 | 35.71 | \$1,739.12 | (\$3,132.53) | 0.56 | 0.31 | (\$1,392.66) |
| 4 | (\$15,309.27) | 14 | 6 | 8 | 42.86 | \$1,581.25 | (\$3,099.60) | 0.51 | 0.38 | (\$1,093.52) |
| 3 | (\$5,051.10) | 14 | 6 | 8 | 42.86 | \$1,465.33 | (\$1,730.39) | 0.85 | 0.64 | (\$360.79) |
| 2 | (\$641.51) | 16 | 7 | 9 | 43.75 | \$2,094.51 | (\$1,700.34) | 1.23 | 0.96 | (\$40.09) |
| 1 | (\$3,827.92) | 19 | 6 | 13 | 31.58 | \$1,786.28 | (\$1,118.89) | 1.60 | 0.74 | (\$201.47) |

This is also suggestive of a short-term pullback.

The [Aggregator](#) has been updated below.



The Aggregator chart remains little changed from yesterday. Expectations are still net negative over the next few days and the S&P has outperformed over the last few days. This all suggests the downside edge remains in place.

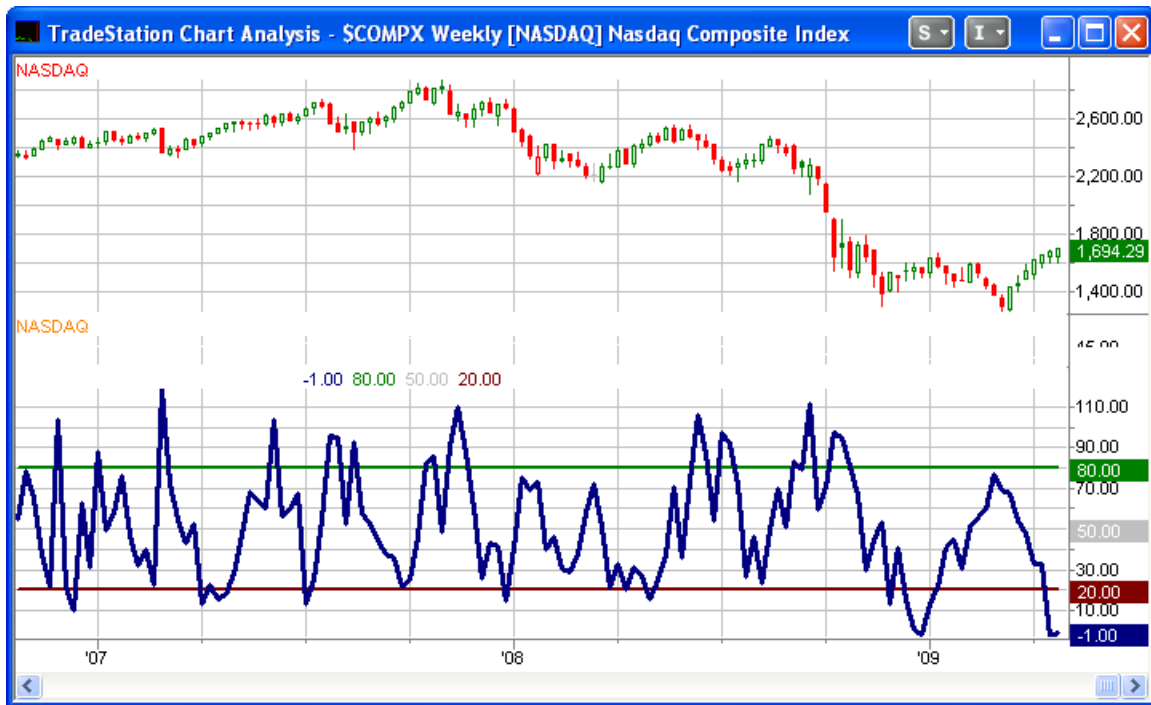
Most notable about the current Aggregator calculations is that should the S&P close lower tomorrow, there is a chance that both the green Aggregator line and black Differential line could flip up to positive. I will be watching this closely tomorrow as such action would almost certainly lead me to cover the entire QQQQ short position. The green Aggregator line may only be a 1-day flip depending on tomorrow night's studies, so I wouldn't be looking to go long without first completing my research tomorrow night.

While things can change dramatically between now and the open it appears there's a decent chance the market could again gap down on Tuesday. With the fact that most major indices closed lower on Monday, I'd look to take advantage of a strong gap lower and take partial profits on the outstanding QQQQ trade idea. Details in the trade ideas section below.

For now I'm not looking to add any more exposure. The only S&P 100/ETF trigger on the systems page tonight was UNG. (There were a few S&P 500 triggers, although I rarely track them in the Letter for liquidity reasons.) UNG is not a great vehicle for playing overbought/oversold systems. It has a tendency to trend stronger and become more overbought/oversold than a more diverse ETF would. I'll stand aside for that reason.

Intermediate-term Outlook (2 weeks – 2 months)–starting to lean bearish -updated 4/27

One indicator I looked at last week that was showing bearish readings was the Quantifiable Edges Nasdaq Weekly Volume Spyx chart. The Nasdaq Spyx weekly chart is calculated in a similar manner as the [S&P 500 and Nasdaq Volume Spyx daily charts](#) that are updated each night on the website. The primary difference is that it uses weekly data rather than daily. After posting a reading below 0 last week, it again did it this week. Below is an updated weekly chart of the Nasdaq Spyx.



Going back to 2000 (as far as Nasdaq Spyx data has been calculated) there has only been one other time the market had back to back readings below 0. That was the week ending 11/29/02, which came 7 weeks after the October 2002 bottom. It marked the top of that rally. From there it pulled back for over 3 months before the March 2003 rally and new bull market began. Similarly, we are now 7 weeks off of the March bottom.

Another instance that came close to a back to back sub-zero reading was December of 2008. What followed that was obviously quite bearish over the next few months.

There have only been 4 instances where the Nasdaq Spyx has posted a sub-zero weekly reading and then the Nasdaq has risen the next week. Those four instances along with their 8-week returns are listed below.

| Date/Time | Signal | Price | Roll Over USD/Lot | Shares/Ctrts Profit | Net Profit Cum Net Profit | % Profit |
|-----------|--------|------------|-------------------|---------------------|---------------------------|----------|
| 01/04/02 | 1 | \$2,059.38 | \$0.00 | 485 | (\$124,470.40) | (12.46%) |
| 03/01/02 | Sell | \$1,802.74 | | | (\$124,470.40) | |
| 11/29/02 | 1 | \$1,478.78 | \$0.00 | 676 | (\$92,368.64) | (9.24%) |
| 01/24/03 | Sell | \$1,342.14 | | | (\$216,839.04) | |
| 12/03/04 | 1 | \$2,147.96 | \$0.00 | 465 | (\$52,140.45) | (5.22%) |
| 01/28/05 | Sell | \$2,035.83 | | | (\$268,979.49) | |
| 01/02/09 | 1 | \$1,632.21 | \$0.00 | 612 | (\$155,674.44) | (15.58%) |
| 02/27/09 | Sell | \$1,377.84 | | | (\$424,653.93) | |

The “best” result above was the 12/04 – 1/05 period where the Nasdaq “only” lost 5%.

The rally is getting long in the tooth. Stocks have now moved higher for 7 weeks. Some measures hit the [most overbought readings in over 23 years](#) last week and remain nearly as high right now.

Breadth is strong and price has been moving higher, but both may be getting a bit overdone. Lower volume and extremely low Nasdaq Volume Spyx readings appear to be signaling warnings. I believe risk/reward will soon favor the downside if it hasn't already shifted that way.

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 | 0.70 |
| 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 |

No signs of capitulative selling at the present time.

Additional New Trade Ideas

None tonight.

Active Trades Table

| Symbol | Entry Date | Entry Price | Current Pr | % Gain/L | Stop | Notes |
|--------------|------------|-------------|------------|----------|------|------------------|
| QQQQ(1/4)(s) | 4/24/2009 | \$33.69 | \$33.73 | -0.12% | | |
| QQQQ(1/4)(s) | 4/27/2009 | \$33.73 | \$33.73 | 0.00% | | shorted on close |

As I mentioned in the short-term market outlook above, I'll be looking to cover part of the position should we get a gap lower tomorrow. I'll also be looking to exit the entire position should it closer much lower. I may also look to trail stops intraday should the market start the day in our direction. If so, I'll send out intraday updates.

So here are the levels I'm looking at:

Cover 1 lot ON OPEN of \$33.50 or lower. This is only a cover on open trade. Should it open above this level, then the order will be cancelled.

Cover entire position ON CLOSE of \$33.50 or lower. This again is a limit on close order.

As per usual I will send out any adjustments during the day, but that is my game plan going in.

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