

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 5, 2009

Volume 2 Issue 85

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					
May 5, 2009	2 Up In Chop	1-4 days	Bearish		
May 5, 2009	Banks Up 10%	1-2 days	Bearish		
May 5, 2009	3% up on strong volume	1-7 days	Bullish	3.20%	6.60%
May 4, 2009	10-high low volume low bar pattern	1-5 days	Bearish	-2.00%	-3.50%
April 27, 2009	Gap-n-go	1-9 days	Bearish	-3.40%	-6.50%
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		
March 26, 2009	Rise after follow through day		Bullish	920 before 666	
Dropped Tonight					
April 30, 2009	1% Gap-n-Go	1-3 days	Bearish	-3.20%	-5.80%

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 5/5 – bearish

The market exploded higher on Monday. A morning gap went unfilled and it led to a strong trend day higher that closed near its high. The S&P 500 was up over 3% while the banks led the way with a rise of over 14%. Breadth was extremely strong as the NYSE Up Issues % came in at 85% and the Up Volume % at 95%. Overall volume was also strong as it came in at the highest level in about a week and a half.

The studies today came in mixed. First I'll look at some potentially bullish action. Strong moves on strong volume have a much better chance of continuing higher than strong moves on weak volume. In the January 22, 2009 Subscriber Letter I showed a study that broke out 3% up days by those that were accompanied by the highest volume in 5 days vs. those that were not. Today's action did occur on the highest volume in at least 5 days. Below I've updated the study from that January Letter.

S&P 500 rises 3% on the highest volume in 5 days.										
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 Fact	Avg Trade
10	\$69,489.19	38	26	12	68.42	\$4,101.79	(\$3,096.44)	1.32	2.87	\$1,828.66
9	\$75,037.00	38	24	14	63.16	\$4,517.41	(\$2,384.34)	1.89	3.25	\$1,974.66
8	\$53,979.90	38	25	13	65.79	\$3,718.92	(\$2,999.47)	1.24	2.38	\$1,420.52
7	\$55,826.22	38	26	12	68.42	\$3,644.14	(\$3,243.46)	1.12	2.43	\$1,469.11
6	\$51,154.28	40	26	14	65.00	\$3,688.76	(\$3,196.68)	1.15	2.14	\$1,278.86
5	\$47,708.50	40	29	11	72.50	\$3,146.93	(\$3,959.31)	0.79	2.10	\$1,192.71
4	\$38,560.82	40	28	12	70.00	\$2,854.42	(\$3,446.92)	0.83	1.93	\$964.02
3	\$39,275.07	40	23	17	57.50	\$3,197.14	(\$2,015.24)	1.59	2.15	\$981.88
2	\$20,389.12	40	22	18	55.00	\$2,200.89	(\$1,557.25)	1.41	1.73	\$509.73
1	\$24,772.11	40	24	16	60.00	\$1,791.07	(\$1,138.34)	1.57	2.36	\$619.30

Here we see a solid edge to the upside. Strong price movement on high volume has often led to additional follow-through. Interesting about today was that the strong move was coming at a high rather than near a volatile bottom. I decided to check and see whether filtering out non new-highs would matter. I looked at instances like the above but that were closing at 10-day highs.

S&P 500 rises 3% on the highest volume in 5 days. It closes at the highest level in 10 days.										
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 Fact	Avg Trade
10	\$30,255.50	20	14	6	70.00	\$3,693.91	(\$3,576.55)	1.03	2.41	\$1,512.78
9	\$28,059.43	20	13	7	65.00	\$3,817.57	(\$3,081.28)	1.24	2.30	\$1,402.97
8	\$23,161.08	20	13	7	65.00	\$3,598.61	(\$3,374.40)	1.07	1.98	\$1,158.05
7	\$30,408.55	20	13	7	65.00	\$3,597.46	(\$2,336.91)	1.54	2.86	\$1,520.43
6	\$21,033.20	21	13	8	61.90	\$3,384.18	(\$2,870.14)	1.18	1.92	\$1,001.58
5	\$18,138.86	21	13	8	61.90	\$3,134.31	(\$2,825.90)	1.11	1.80	\$863.76
4	\$12,404.67	21	14	7	66.67	\$2,348.44	(\$2,924.79)	0.80	1.61	\$590.70
3	\$12,468.26	21	13	8	61.90	\$2,194.46	(\$2,007.46)	1.09	1.78	\$593.73
2	\$7,537.03	21	12	9	57.14	\$1,659.50	(\$1,375.21)	1.21	1.61	\$358.91
1	\$7,845.48	21	13	8	61.90	\$1,210.19	(\$985.88)	1.23	1.99	\$373.59

Breaking it out this way didn't reveal much of a difference from the 1st test. Even considering the market was at new short-term highs, the powerful up days were still followed by more buying.

The massive 14% gain in the banking index is something that has become more commonplace over the last year. I found 17 other instances dating back to 1992. All of them have happened since July of 2008. Most often it's been following by additional market selling.

BKX closes up 10%.										
Buy S&P 500 on close. Sell X days later. \$100k/trade. 1992-present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
10	(\$20,548.43)	11	4	7	36.36	\$5,129.52	(\$5,866.64)	0.87	0.50	(\$1,868.04)
9	(\$23,062.14)	12	4	8	33.33	\$6,207.12	(\$5,986.33)	1.04	0.52	(\$1,921.85)
8	(\$58,961.65)	13	3	10	23.08	\$3,659.60	(\$6,994.05)	0.52	0.16	(\$4,535.51)
7	(\$62,856.86)	13	2	11	15.38	\$4,943.56	(\$6,613.09)	0.75	0.14	(\$4,835.14)
6	(\$29,784.21)	13	7	6	53.85	\$2,911.54	(\$8,360.83)	0.35	0.41	(\$2,291.09)
5	(\$17,902.80)	14	7	7	50.00	\$3,734.34	(\$6,291.88)	0.59	0.59	(\$1,278.77)
4	(\$25,004.95)	14	6	8	42.86	\$2,193.81	(\$4,770.98)	0.46	0.34	(\$1,786.07)
3	(\$11,896.85)	15	6	9	40.00	\$3,206.27	(\$3,459.39)	0.93	0.62	(\$793.12)
2	(\$20,935.29)	16	6	10	37.50	\$1,937.62	(\$3,256.10)	0.60	0.36	(\$1,308.46)
1	(\$17,248.24)	17	7	10	41.18	\$1,034.87	(\$2,449.23)	0.42	0.30	(\$1,014.60)

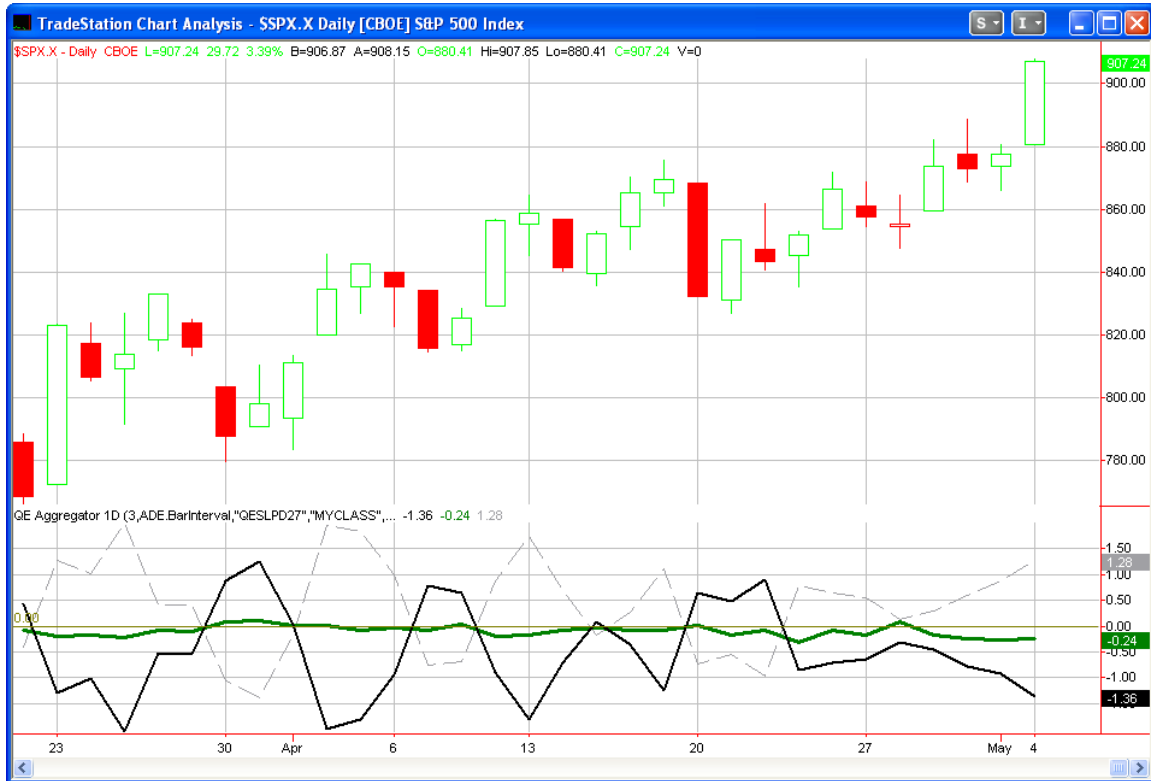
These strong upside reactions have often been overreactions.

Also suggesting downside is our “2 Days Up In Chop” system. This incredibly simple system has fared exceptionally well since June of 2007 when the market became substantially more choppy. It looks to **short** the S&P after it closes higher for 2 days in a row. The exit signal comes on the first profitable close up to 4 days later. After 4 days the trade is exited regardless of profitability. Below are updated results from June 1, 2007 – May 4, 2009. Results are based on \$100k/trade and are frictionless.

TradeStation Performance Summary				Collapse ^
All Trades				
Total Net Profit	\$72,035.42	Profit Factor	6.62	
Gross Profit	\$84,844.10	Gross Loss	(\$12,808.68)	
Roll Over Credit	\$0.00			
Open Position Profit/Loss	\$0.00			
Select Total Net Profit	\$63,252.40	Select Profit Factor	5.94	
Select Gross Profit	\$76,061.08	Select Gross Loss	(\$12,808.68)	
Adjusted Total Net Profit	\$55,261.44	Adjusted Profit Factor	3.98	
Adjusted Gross Profit	\$73,798.34	Adjusted Gross Loss	(\$18,536.90)	
Total Number of Trades	64	Percent Profitable	92.19%	
Winning Trades	59	Losing Trades	5	
Even Trades	0			
Avg. Trade Net Profit	\$1,125.55	Ratio Avg. Win:Avg. Loss	0.56	
Avg. Winning Trade	\$1,438.04	Avg. Losing Trade	(\$2,561.74)	
Largest Winning Trade	\$8,783.02	Largest Losing Trade	(\$7,832.88)	

Another note that I'll expand upon in the blog tomorrow morning is that I'm see some breadth measures again are near or hit all-time extremes. Worden Bros. measures the % of stocks trading at least 1 and 2 standard deviations above their 40-day moving average. I mentioned the 1-standard deviation indicator (T2110) in the blog a couple of weeks ago. At the time it was hitting an all-time high of nearly 81%. Tonight it broke that record registering over 83%. The 2 standard deviation indicator (T2112) all hit a new extreme Monday. Before Monday this indicator had never reached 40%. Monday it spiked up to 52.14%. This suggests the market is incredibly overbought.

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

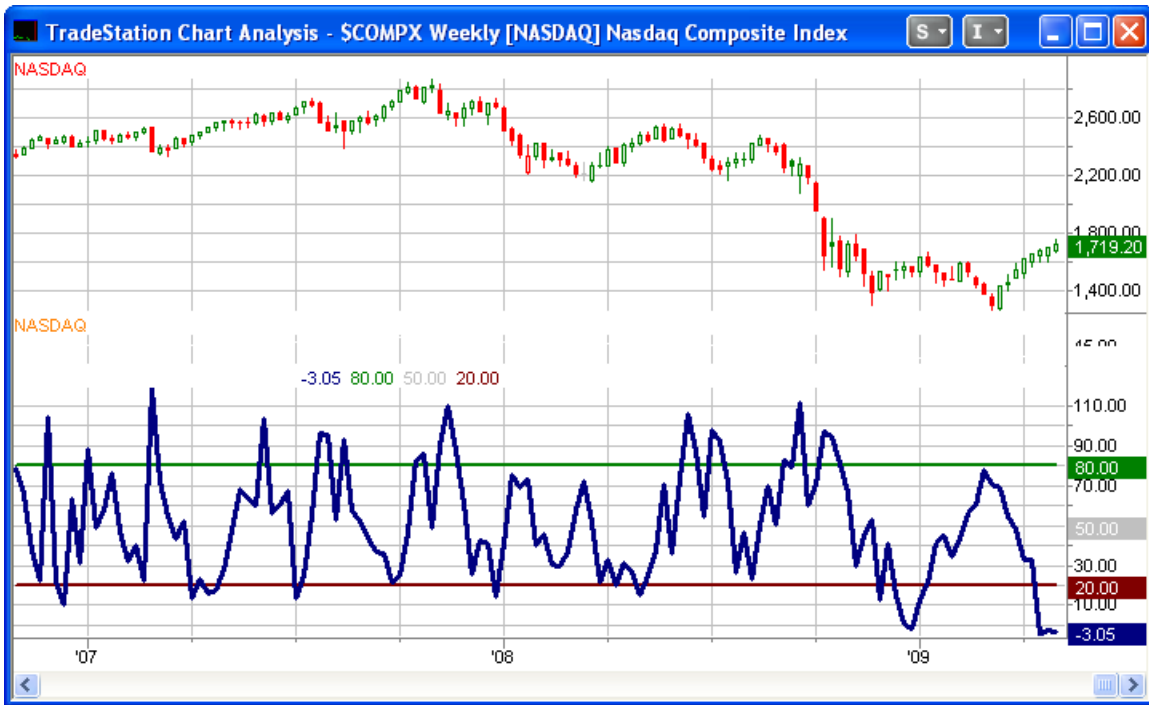


Even with a bullish study added to the mix, both the green Aggregator and black Differential lines remain strongly below 0. The studies are suggesting more downside and the market is overbought. This implies a strong downside edge.

I'll be looking to add to the short position tomorrow as described in the trade ideas section.

Intermediate-term Outlook (2 weeks – 2 months)–starting to lean bearish -updated 5/4

One indicator that I've discussed the last couple of weeks that has been suggesting an intermediate-term pullback may in order is the Nasdaq Weekly Volume Spyx. While the Nasdaq rose again this week, the Spyx remained quite low. Below is this week's chart form the chart page on the website:



No sense in beating a dead horse here. This indicator is still suggesting a selloff. Subscribers may reference research from either of the last 2 weeks for details.

One concern about the move higher last week was the leadership of the move. It appears the 2 strongest major sector ETF's last week were IYZ(telecom) and XLU (Utilities). Both of these rose over 4.5% on the week while the S&P closed less than 1.5% higher. Neither Utilities nor Telecom are among the sectors that you would prefer to see exerting leadership. Below are some studies that explain why this is.

First let's look at utilities. For this test I used the XLU and SPY ETF's. I looked for other times the SPY moved higher but lagged XLU by a substantial amount:

SPY closes up on the week. XLU (utilities) outperforms SPY by at least 1 percent.										
Buy on close. Sell X weeks later. \$100k/trade. 11/2002-present.										
X Weeks	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
10	(\$22,678.48)	16	9	7	56.25	\$4,802.86	(\$9,414.89)	0.51	0.66	(\$1,417.41)
9	(\$26,900.35)	17	7	9	41.18	\$4,646.20	(\$6,602.64)	0.70	0.55	(\$1,582.37)
8	(\$7,421.94)	18	8	10	44.44	\$5,207.29	(\$4,908.02)	1.06	0.85	(\$412.33)
7	(\$6,506.53)	18	10	8	55.56	\$3,806.87	(\$5,571.90)	0.68	0.85	(\$361.47)
6	(\$11,361.32)	21	10	11	47.62	\$5,310.61	(\$5,860.67)	0.91	0.82	(\$541.02)
5	(\$22,555.94)	23	12	11	52.17	\$3,665.47	(\$6,049.24)	0.61	0.66	(\$980.69)
4	(\$28,800.92)	27	14	13	51.85	\$3,300.32	(\$5,769.65)	0.57	0.62	(\$1,066.70)
3	(\$9,685.25)	29	14	15	48.28	\$2,829.20	(\$3,286.27)	0.86	0.80	(\$333.97)
2	\$331.81	31	16	15	51.61	\$2,531.31	(\$2,677.94)	0.95	1.01	\$10.70
1	(\$1,217.69)	32	17	14	53.13	\$1,528.59	(\$1,943.12)	0.79	0.96	(\$38.05)

This study was actually run back to 1/1/2000, but no instances occurred prior to 2002. I also looked to see how typical weeks over the time period had performed. The average

week from 11/2002 to present gained about 0.03%. The negative results of the study above are therefore quite a bit worse than a typical week.

I also ran a similar study looking at telecom:

SPY closes up on the week. IYZ (telecom) outperforms SPY by at least 1 percent.											
Buy on close. Sell X weeks later. \$100k/trade. 06/2004-present.											
X Weeks	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade	
10	(\$31,889.45)	17	9	8	52.94	\$4,213.25	(\$8,726.08)	0.48	0.54	(\$1,875.85)	
9	(\$47,317.82)	18	9	9	50.00	\$2,676.56	(\$7,934.10)	0.34	0.34	(\$2,628.77)	
8	(\$59,963.94)	18	6	12	33.33	\$2,666.42	(\$6,330.20)	0.42	0.21	(\$3,331.33)	
7	(\$36,768.88)	20	8	12	40.00	\$3,029.84	(\$5,083.96)	0.60	0.40	(\$1,838.44)	
6	(\$13,044.45)	20	11	9	55.00	\$2,617.74	(\$4,648.84)	0.56	0.69	(\$652.22)	
5	(\$29,047.58)	23	12	11	52.17	\$2,185.12	(\$5,024.46)	0.43	0.47	(\$1,262.94)	
4	(\$27,583.29)	25	11	14	44.00	\$2,380.07	(\$3,840.29)	0.62	0.49	(\$1,103.33)	
3	(\$21,176.42)	27	14	13	51.85	\$1,882.17	(\$3,655.91)	0.51	0.55	(\$784.31)	
2	(\$15,856.63)	30	13	17	43.33	\$1,716.56	(\$2,245.40)	0.76	0.58	(\$528.55)	
1	(\$25,379.81)	33	12	21	36.36	\$984.66	(\$1,771.22)	0.56	0.32	(\$769.09)	

Here again I'm only showing results from the first instance forward. Over the time period above the average week experienced a loss of 0.06%, or -\$56.20. So while negative results would be expected over the test period, results are still substantially more bearish than typical.

Of course both of these studies understate the percentage outperformance by the sectors over the broad S&P. Below is a breakdown of IYZ for a 4-week holding period based on the size of the outperformance.

SPY closes up on the week. IYZ (telecom) outperforms SPY by at least X percent.											
Buy on close. Sell 4 weeks later. \$100k/trade. 06/2004-present.											
X Weeks	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade	
2.5	(\$10,168.22)	4	1	3	25.00	\$1,429.23	(\$3,865.82)	0.37	0.12	(\$2,542.06)	
2	(\$21,468.53)	8	3	5	37.50	\$1,128.00	(\$4,970.51)	0.23	0.14	(\$2,683.57)	
1.5	(\$26,821.52)	14	6	8	42.86	\$1,968.71	(\$4,829.23)	0.41	0.31	(\$1,915.82)	
1	(\$27,583.29)	25	11	14	44.00	\$2,380.07	(\$3,840.29)	0.62	0.49	(\$1,103.33)	
0.5	(\$15,213.51)	34	17	17	50.00	\$2,783.61	(\$3,678.52)	0.76	0.76	(\$447.46)	

The larger the outperformance the worse the market performed over the next month. When looking at XLU the results weren't as cut and dry since there were a few strong moves higher when the differential was greater than 2%. Still, the overall edge remained lower.

Lastly you'll note that the breadth thrust was removed from the active studies list tonight. It's been a month since it triggered and our previous tests found the bulk of the move often came within the 1st month. Therefore, with its bullish influence potentially waning, I've removed it from the list.

More and more evidence is suggesting the market is ripe for a pullback. I expect we may begin to see one fairly soon. Still, from a price standpoint the uptrend is obviously still in place. Before getting too aggressive on the short side I'll need to see these negative indications confirmed by price. I'm not excited about chasing intermediate-term long positions at this point.

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	0.38
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

Still no signs of capitulative selling.

Additional New Trade Ideas

SPY short 1/4 index position at \$90.75 LIMIT. – Based on the short-term market outlook. I'm placing this order a little below Monday's close in case of a gap down that doesn't quite fill.

IYT – short a “system trade” size position at \$60.15 limit. – From the triggers page IYT is set up with a -81217 trigger. I'll look to take some at Monday's closing price. The exit for this system is a close below the 5-day moving average.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/Loss	Stop	Notes
SPY(1/4)(s)	4/30/2009	\$88.55	\$90.88	-2.63%		
SPY(1/4)(s)	5/4/2009	\$88.55	\$90.88	-2.63%		

The gap up this morning gave us the worst possible entry from last night. My \$88.55 limit on open order was hit right on the penny. One cent less and the entry would have been at the close rather than the open – a 2.5% difference. Bad fills and bad luck are just part of trading. The market still appears likely to sell off short-term. I'll be looking to take advantage of it when it does. Whether this particular trade ends up positive is not of paramount importance. What's important is taking a consistent approach when I believe the odds are in my favor. That's what should pay off over time.

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