

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 20, 2009

Volume 2 Issue 96

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 + 1/2 Std Dev
Active					
May 19, 2009	2.5% rise low volume	1-5 days	Bearish	-5.30%	-7.70%
May 18, 2009	5 Lower lows from 50-day high	1-10 days	Bearish	-2.40%	-3.30%
May 15, 2009	Strong breadth weak volume	1-3 days	Bearish	-3.40%	-4.80%
May 14, 2009	3 Dn & 2 Drop 1.75%	1-10 days	Bullish	5.70%	7.60%
Active - Long Term					
April 20, 2009	Low Nasdaq Weekly Vol Spyx	1-10 weeks	Bearish		
Dropped Tonight					

If the avg max move is achieved it will appear in **bold and brown**. If the avg + 1/2 std deviation is achieved, the study will in *bold italic blue*.

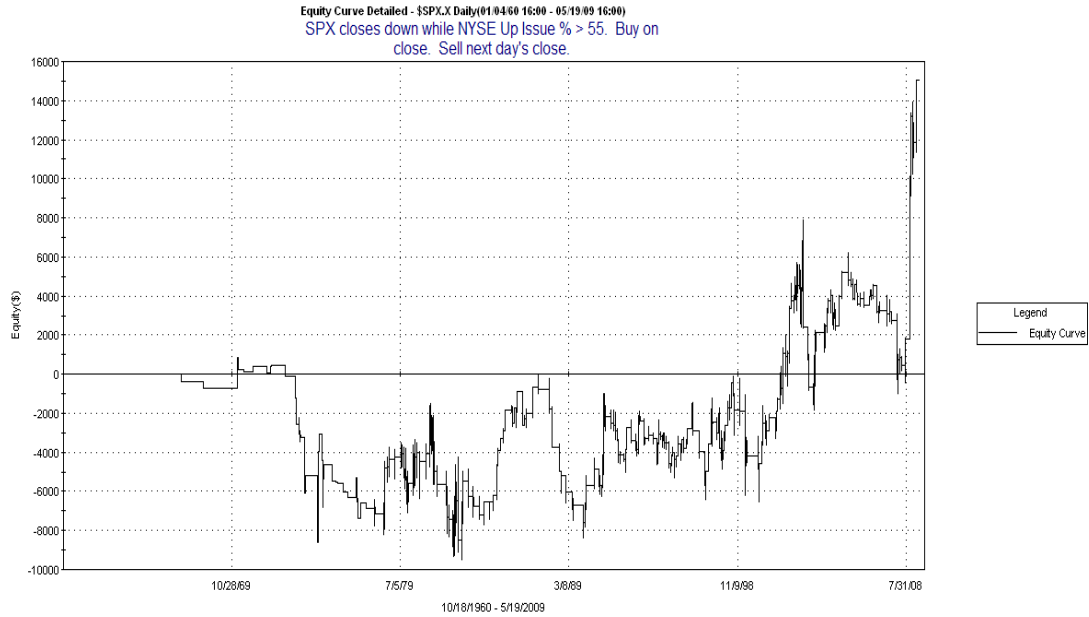
Short-term Outlook (1-5 days) – updated 5/20 – bearish

Not much action today in the market. Low range, low volume, and the indices mostly finished near unchanged. Breadth was a slight bright spot for the bulls. The NYSE Up Issues % came in at 60% and the Up Volume % was 55%. Total volume was again the lowest in 10 days.

Positive breadth when the market closes lower is often cited bullish. In fact I'd say the edge it provides is marginal at best. Below is a study that looks at purchasing the S&P following a down day in which the Up Issues % closed above 55%.

SPX closes lower while the NYSE Up Issues % closes above 55%.										
Buy on close. Sell X days later. \$100k/trade. 1970-present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
5	\$74,021.11	242	142	100	58.68	\$1,618.69	(\$1,558.33)	1.04	1.48	\$305.87
4	\$86,337.70	256	150	106	58.59	\$1,566.85	(\$1,402.74)	1.12	1.58	\$337.26
3	\$47,691.13	266	150	116	56.39	\$1,385.27	(\$1,380.17)	1.00	1.30	\$179.29
2	\$9,425.51	273	137	136	50.18	\$1,137.30	(\$1,076.35)	1.06	1.06	\$34.53
1	\$15,767.55	285	140	144	49.12	\$834.22	(\$701.55)	1.19	1.16	\$55.32

What we see here is a mild bullish tendency over the next week. Really the tendency doesn't even kick in until later in the week. Below is a chart of the 1-day returns to illustrate this point.

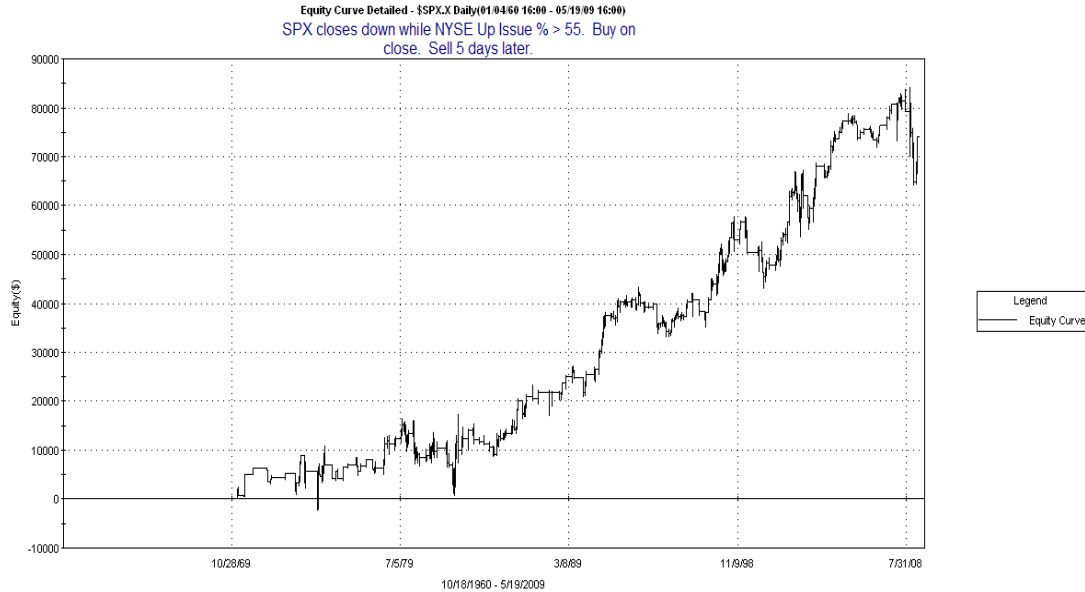


Note that nearly all of the gains came in the last six months on only 4 trades. With all the gains due to some recent outliers, this isn't a trigger I'd put much faith in.

Looking out 5 days returns are more evenly dispersed and there is a mild edge. The table below shows the 5-day returns based on different breadth numbers.

SPX closes lower while the NYSE Up Issues % closes above X%.										
Buy on close. Sell 5 days later. \$100k/trade. 1970-present.										
X%	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
60%	\$10,041.11	60	30	30	50.00	\$2,116.45	(\$1,781.75)	1.19	1.19	\$167.35
55%	\$74,021.11	242	142	100	58.68	\$1,618.69	(\$1,558.33)	1.04	1.48	\$305.87
50%	\$149,760.73	558	317	241	56.81	\$1,651.56	(\$1,550.96)	1.06	1.40	\$268.39
45%	\$166,609.64	926	516	410	55.72	\$1,585.17	(\$1,588.63)	1.00	1.26	\$179.92
40%	\$211,019.31	1223	661	562	54.05	\$1,702.43	(\$1,626.85)	1.05	1.23	\$172.54
35%	\$178,734.26	1389	747	642	53.78	\$1,663.50	(\$1,657.17)	1.00	1.17	\$128.68
30%	\$210,267.10	1495	808	687	54.05	\$1,653.28	(\$1,638.40)	1.01	1.19	\$140.65
25%	\$184,112.96	1558	843	715	54.11	\$1,659.34	(\$1,698.89)	0.98	1.15	\$118.17
20%	\$191,802.29	1589	860	729	54.12	\$1,656.47	(\$1,691.04)	0.98	1.16	\$120.71
15%	\$153,517.84	1610	867	743	53.85	\$1,667.98	(\$1,739.73)	0.96	1.12	\$95.35
10%	\$175,120.27	1622	872	750	53.76	\$1,695.55	(\$1,737.87)	0.98	1.13	\$107.97
5%	\$187,912.56	1626	875	750	53.81	\$1,700.40	(\$1,733.26)	0.98	1.14	\$115.57
0%	\$187,912.56	1626	875	750	53.81	\$1,700.40	(\$1,733.26)	0.98	1.14	\$115.57

As you can see, there does appear to be a bit of an edge. A 5-day equity chart shows the winnings are more evenly dispersed as well:



I'd say there is a slight bullish tilt over the next week suggested by this study.

The volume and range are producing studies with bearish tilts. Below is one example from the 4/14/09 blog. (Table not updated.)

SPY posts lowest volume in 20 days and closes above its 10-day moving average.										
Buy on close. Sell X days later. \$100k/trade. 1993-present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
10	(\$47,076.40)	125	64	61	51.20	\$2,228.79	(\$3,110.15)	0.72	0.75	(\$376.61)
9	(\$46,613.56)	128	73	55	57.03	\$1,925.76	(\$3,403.53)	0.57	0.75	(\$364.17)
8	(\$31,788.98)	136	77	59	56.62	\$1,901.74	(\$3,020.73)	0.63	0.82	(\$233.74)
7	(\$43,850.51)	139	70	68	50.36	\$1,854.19	(\$2,553.58)	0.73	0.75	(\$315.47)
6	(\$53,291.81)	142	68	73	47.89	\$1,688.89	(\$2,303.24)	0.73	0.68	(\$375.29)
5	(\$69,244.92)	152	68	83	44.74	\$1,522.37	(\$2,081.52)	0.73	0.60	(\$455.56)
4	(\$52,672.55)	161	76	85	47.20	\$1,244.03	(\$1,731.99)	0.72	0.64	(\$327.16)
3	(\$53,244.06)	166	64	101	38.55	\$1,330.06	(\$1,369.98)	0.97	0.62	(\$320.75)
2	(\$41,102.84)	177	74	103	41.81	\$1,072.32	(\$1,169.46)	0.92	0.66	(\$232.22)
1	(\$39,672.01)	202	82	119	40.59	\$773.80	(\$866.58)	0.89	0.62	(\$196.40)

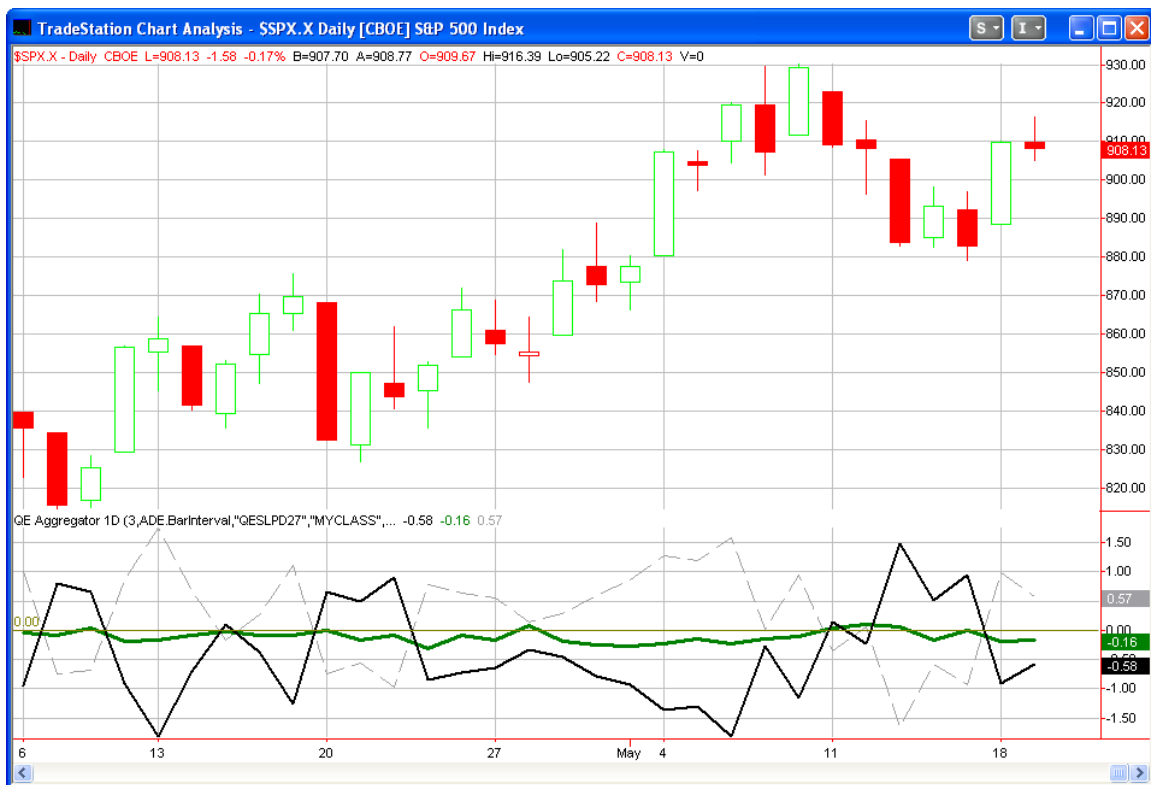
While not the strongest downside edge I've ever seen this study does do a little more than just offset the bullish breadth study above.

Another study that popped up again tonight looked at the narrow range and low volume for the SPX on Tuesday. This one was last shown on 2/10/09. The table below has been updated.

SPX has NR10 day on the lowest volume in 10 days and closes under the 200ma.										
Buy on close. Sell X days later. \$100k/trade. 1970-present.										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Factor	Avg Trade
5	(\$85,586.58)	141	60	81	42.55	\$1,956.30	(\$2,505.74)	0.78	0.58	(\$607.00)
4	(\$93,180.15)	146	61	85	41.78	\$1,603.30	(\$2,246.84)	0.71	0.51	(\$638.22)
3	(\$77,626.01)	153	63	89	41.18	\$1,445.14	(\$1,895.16)	0.76	0.54	(\$507.36)
2	(\$59,214.55)	158	68	90	43.04	\$1,238.37	(\$1,593.60)	0.78	0.59	(\$374.78)
1	(\$39,708.64)	177	77	99	43.50	\$819.97	(\$1,038.85)	0.79	0.61	(\$224.34)

Not shown in the above table is that 74% of instances closed below their trigger day low at some point in the next 3 days. Of the studies looked at tonight this one appears to have the biggest edge. It is the only one I chose for inclusion in the Aggregator.

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



The configuration of the Aggregator remains bearish. The green Aggregator line is squarely below zero, which indicates the net expectations of the active studies is for downside over the next few days.

Meanwhile the black Differential line is also solidly negative. This illustrates the S&P outperformance over the last few days as compared to expectations.

The SPY trade idea entry just missed on Tuesday, but with the outlook still bearish I'll again look for a favorable entry on Wednesday. Details in the trade ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)– bearish -updated 5/18

Over the last few weeks we've seen some intermediate-term bearish evidence building up. The [Nasdaq Weekly Volume Spyx readings](#) were the 1st sign of impending weakness. While the market seemingly ignored those readings to begin with, they do remain in effect for the next several weeks. Next, in the May 4th subscriber Letter I showed two studies that questioned the leadership at that point.

The strong outperformance by transports and telecom suggested a bearish edge for at least 4 weeks from that point. There's still two weeks to go for those studies.

Worden Bros. T2112 indicator, which measures the number of stocks trading at least 2 standard deviations above their 40-day moving average, hit a historical peak on May 8th at 55.93%. (I looked at this indicator in the [May 5th blog](#).) The reaction this past week was strongly negative. So much so that the 10-day ema of the Up Issues % is now registering multiple sub-50 readings for the 1st time since the March bottom. Continued weakness would be worrisome.

Lastly, we saw in tonight's short-term outlook the implications of 5 lower lows coming off of a 50-day high. While the downside edge was most prevalent over the 1st two weeks, even as far out as 4 weeks there were negative expectations. What's quite unusual about the current setup is that it is occurring under the 200-day moving average. To have a 50-day high occur under a 200-day moving average it needs to first be preceded by a strong downtrend. Below are charts of the last 4 times the S&P has posted 5 lower lows following a 50-day high while under the 200ma. The blue arrow indicates where the setup took place.

May 2008



December 2002



May 2001



April/May 1982



Interesting that 3 of the 4 were “sell in May and go away” setups. Only one occurred that wasn’t in May.

From an intermediate-term perspective I am now seeing indications of volume, leadership, breadth, and price that suggest we should see some additional downside in the next few weeks. I am therefore changing the bias to bearish. For my trading this means that I will be more demanding of long entries and quicker to take profits on the long side. On the short side I will be more aggressive with my setups and perhaps hope to catch longer moves.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

RTN – bought 1/3 position @ \$44.87

RTN - buy 1/3 position @ \$44.44 limit.

Catapult for ETF’s Trades

none

Broad Market Large Cap CBI – 2/1(RTN-2)

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	1.35	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	2.84
DJ US Pharmaceuticals	IHE	2.86	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	2.94	DJ US Technology Sector	IYW	1.62
DJ US Home Construction	ITB	0.00	DJ US Telecommunications	IYZ	0.00
DJ US Consumer Svcs	IYC	0.48	Nasdaq 100	QQQQ	2.00

Additional New Trade Ideas

RTN – buy 1/3 position @ \$44.44 from the Catapult section above. This is the 2nd of possibly 3 entries into RTN. As I mentioned last night, this is not the greatest set as far as Catapults go. It’s a 1-off trade rather than part of a cluster. Also it is going against my general short bias. Combined these things are leaving me with little excitement about this one. I rarely ignore a Catapult setup, though and am playing this one. I’d suggest you’re conservative with position sizing, especially if you haven’t previously tracked any Catapult trades. The volatility can be quite large.

SPY – short 1/4 position under 1 of the following circumstances: 1) a gap up to \$91.75 or higher or 2) if it doesn’t gap up to at least \$91.75, set a limit order at \$92.15 or 3) if that is not hit intraday, I’ll look to short limit on close at \$91.50. If any one is filled the others will be cancelled. Basically I’m looking to short into any strength tomorrow.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
RTN(1/3)	5/19/2009	\$44.87	\$44.44	-0.96%		Catapult

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