

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 25, 2009

Volume 2 Issue 121

## 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
<b>Active</b>					
June 25, 2009	Strong breadth weak vol	1-2 days	Bearish		
June 25, 2009	2 Days Up in Chop	1-4 days	Bearish		
June 24, 2009	Weak breadth on bounce	1-5 days	Bearish	-4.20%	-5.10%
June 23, 2009	1% drop with decliners dbl advancers	1-9 days	Bullish	2.90%	3.90%
June 18, 2009	Down 3 with slowing rate of decline	1-6 days	Bullish	2.50%	3.20%
<b>Active - Long Term</b>					
June 22, 2009	VIX:VXV hits 100-day low	1-20 days	Bearish	-3.80%	-5.50%
June 11, 2009	4-day tight range above 10ma	1-20 days	Bullish	4.00%	4.80%
June 10, 2009	Nasdaq/NYSE Volume High	1-20 days	Bearish		
June 1, 2009	Nasdaq Relative Strength Leading		Bullish		
April 20, 2009	Low Nasdaq Weekly Vol Spyx	1-10 weeks	Bearish		
<b>Dropped Tonight</b>					
May 28, 2009	SOX up 1% while SPX down 1%	1-20 days	Bullish	13.10%	16.10%

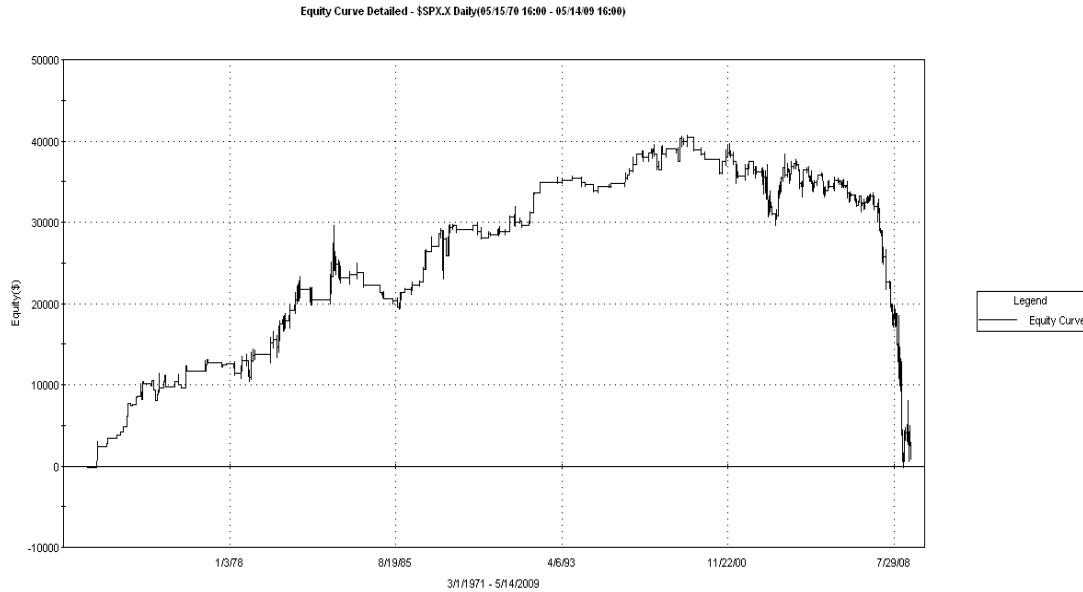
If the avg max move is achieved it will appear in **bold and brown**. If the avg + 1/2 std deviation is achieved, the study will in *bold italic blue*.

### **Short-term Outlook (1-5 days) – updated 6/25 – slightly and increasingly bearish**

Excitement pre-Fed saw no follow through as much of the gains were given back following the 2:15 announcement. The Nasdaq still finished up over 1% but the S&P was only up about 0.5% and the Dow was down. Breadth was strongly positive. NYSE Up Issues % closed at 72% and the Up Volume % closed at 73%. Total volume declined for the 3<sup>rd</sup> day in a row.

So while the breadth on the rebound was strong, the volume was very weak. This brought up a study from 5/15. Below is a excerpt from the Letter. (Study not updated)

*Below is a chart that shows the equity curve of buying any day that advancers outnumber decliners 2 to 1 while volume declines. The holding period for each trade is 1 day.*



*From 1970 until August of 2007 this setup had no bearish implications. In fact, for most of the period, the strong breadth had bullish implications on the next day's trade. This bear market has seen sharp, consistent selling following such days. Below is a table breaking down the 1-5 day performance over the recent period:*

<b>Advancers outnumber down issues by at least 2 to 1. Volume declines from yesterday.</b>										
<b>Buy S&amp;P 500 on close. Sell X days later. \$100k/trade. 08/01/2007 - present.</b>										
X Days	Net Profit	Trades	Wins	Losses	% Wins	Avg Win	Avg Loss	W/L Ratio	Profit Fact	Avg Trade
5	(\$71,244.40)	34	12	22	35.29412	\$1,690.66	(\$4,160.56)	0.406355	0.221648	(\$2,095.42)
4	(\$56,060.01)	36	12	24	33.33333	\$1,880.45	(\$3,276.06)	0.573997	0.286999	(\$1,557.22)
3	(\$59,506.71)	45	15	30	33.33333	\$2,075.83	(\$3,021.47)	0.687026	0.343513	(\$1,322.37)
2	(\$70,400.52)	46	15	31	32.6087	\$839.52	(\$2,677.20)	0.313581	0.151733	(\$1,530.45)
1	(\$32,523.85)	47	18	29	38.29787	\$935.06	(\$1,701.89)	0.549423	0.341021	(\$692.00)

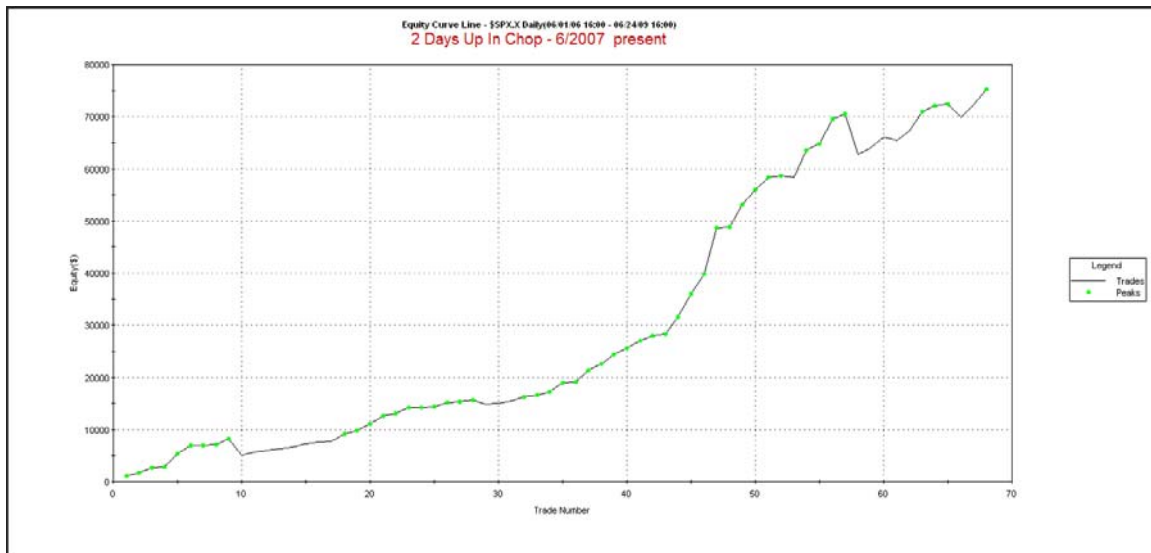
*Looking at the recent past there seems to be a pretty strong indication of a downside edge.*

In addition to the strong breadth/weak volume pattern, Wednesday also triggered our "2 Days Up In Chop" system. Below are updated performance statistics:

If SPX closes higher 2 days in a row, sell short on close. Exit on first profitable close. Cover 4 days later if still not profitable. \$100k/trade. 6/2007 - present

TradeStation Performance Summary <span style="float: right;">Collapse ▲</span>			
All Trades			
Total Net Profit	\$75,301.23	Profit Factor	5.91
Gross Profit	\$90,628.47	Gross Loss	(\$15,327.24)
Total Number of Trades	68	Percent Profitable	91.18%
Winning Trades	62	Losing Trades	6
Even Trades	0		
Avg. Trade Net Profit	\$1,107.37	Ratio Avg. Win:Avg. Loss	0.57
Avg. Winning Trade	\$1,461.75	Avg. Losing Trade	(\$2,554.54)
Largest Winning Trade	\$8,783.02	Largest Losing Trade	(\$7,832.88)
Max. Consecutive Winning Trades	23	Max. Consecutive Losing Trades	1
Avg. Bars in Winning Trades	2.68	Avg. Bars in Losing Trades	5.00

Also below is an equity graph.



As you can see, the most recent trade again put the system as new equity highs.

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



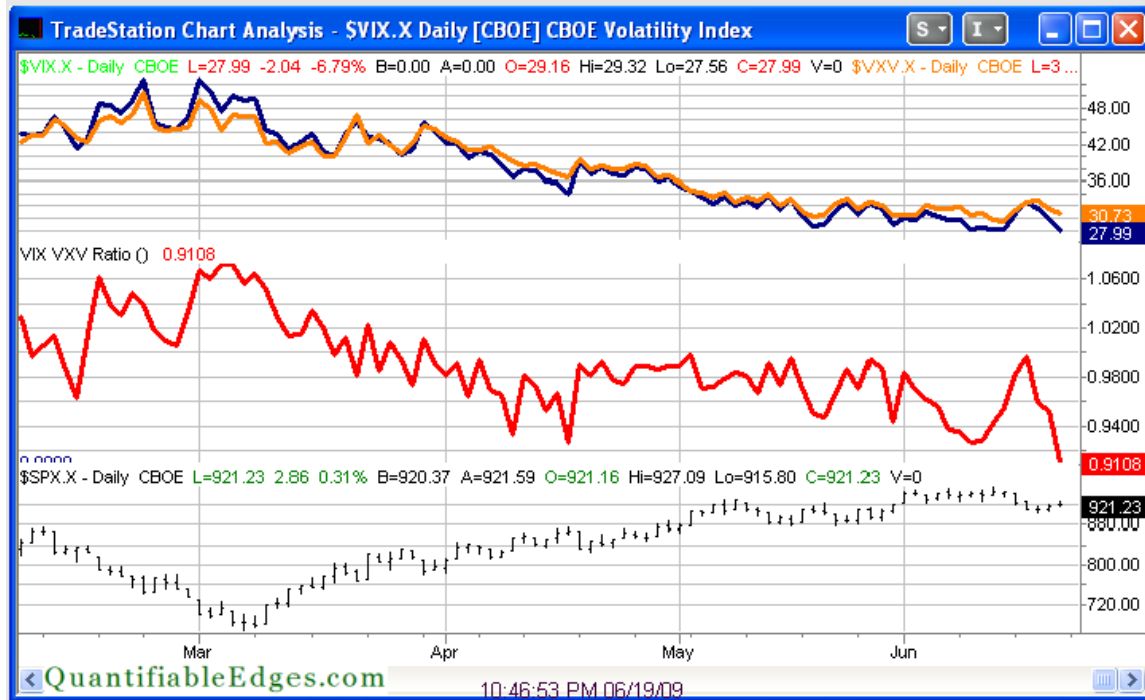
The green Aggregator line has now moved even farther below the zero line. This shows that the net expectations of the studies for the next few days are strongly negative. Meanwhile the black Differential line remains above 0. This illustrates that the market has strongly underperformed expectations over the last 3 days. With both lines on opposite sides of 0 this typically suggests a neutral bias.

Noteable about tomorrow is the fact that Monday's 3% market drop is going be eliminated from the Differential calculation. Unless the S&P suffers a sharp drop, the black Differential line will fall below zero. The green Aggregator line is also scheduled to remain strongly negative. I'll be looking to take advantage of this emerging negative outlook as described in the trade ideas section below.

### ***Intermediate-term Outlook (2 weeks – 2 months)– updated 6/22 - neutral***

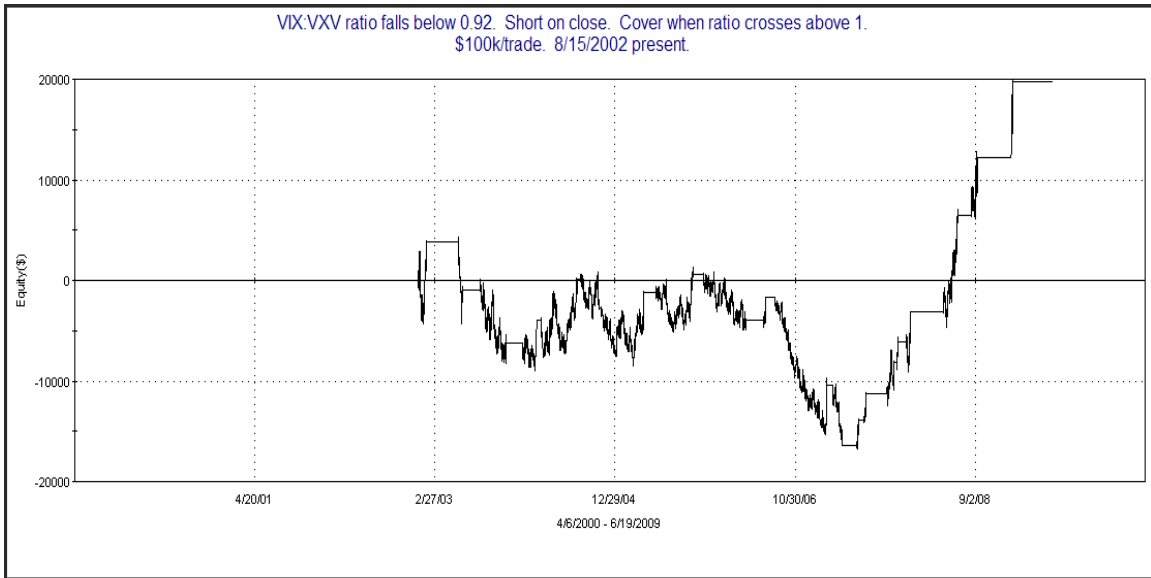
One notable intermediate-term indicator that is beginning to provide some interesting readings is the VIX:VXV ratio. The ratio compares short-term volatility expectations (VIX 30-day) to long-term volatility expectations (VXV 90-day). A low reading suggests that volatility is likely to rise over the next 1-3 months. Rising volatility is often associated with a falling market and therefore a low VIX:VXV ratio can be interpreted as possibly bearish. The VIX:VXV chart is updated on the members' chart page. Below is a copy of the most recent chart.

## VIX:VXV Ratio



Friday's 0.9108 reading is the lowest since last August. At that time I showed some studies which suggested that moves below 0.90 carried a bearish bias. (Note: The VXV has only been listed since late 2007. The CBOE back-calculated the data to 2002 and I was fortunate enough to get my hands on this data. Therefore, rather than just using 18 months worth of data I'm able to look back nearly 7 years.) If you'd like to review the studies from last August [you may do so here](#).

This weekend I tweaked the system discussed in that Letter and used 0.92 for the trigger instead of 0.90. The loosened criteria still gave negative results, but they were not as consistent and depended entirely on the most recent run of trades. Below is an equity curve to illustrate.



My inclination after seeing this was that you'd be quite a bit better off waiting for a 0.90 stretch rather than jumping the gun at 0.92.

Another way I looked at the indicator did seem to suggest a downside edge, though. Below is a performance table showing how the SPX has performed following other occurrences where the VIX:VXV ratio posted a 100-day low.

VIX:VXV ratio hits 100-day low.  
Buy on close. Sell X days later. \$100k/trade. 8/15/2002-present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
25	-27,771.25	12	3	9	25.00	2,174.80	-3,810.63	0.57	0.19	-2,314.27
24	-25,975.57	12	3	9	25.00	2,373.62	-3,677.38	0.65	0.22	-2,164.63
23	-25,819.41	12	4	8	33.33	1,599.44	-4,027.15	0.40	0.20	-2,151.62
22	-24,091.90	12	4	8	33.33	1,633.94	-3,828.46	0.43	0.21	-2,007.66
21	-21,887.34	12	5	7	41.67	1,400.79	-4,127.33	0.34	0.24	-1,823.95
20	-24,940.85	12	6	6	50.00	987.18	-5,143.99	0.19	0.19	-2,078.40
19	-23,508.06	13	6	7	46.15	1,607.21	-4,735.91	0.34	0.29	-1,808.31
18	-19,171.07	13	5	8	38.46	2,006.65	-3,650.54	0.55	0.34	-1,474.70
17	-11,843.27	13	5	8	38.46	1,614.09	-2,464.21	0.66	0.41	-895.64
16	-11,060.60	13	4	9	30.77	2,052.08	-2,140.99	0.96	0.43	-850.82
15	-7,456.54	13	5	8	38.46	1,391.62	-1,801.83	0.77	0.48	-573.58
14	-8,085.31	13	7	6	53.85	872.36	-2,365.31	0.37	0.43	-621.95
13	-7,384.93	13	6	7	46.15	1,112.78	-2,008.80	0.55	0.47	-568.07
12	-7,102.97	13	5	8	38.46	1,311.49	-1,707.55	0.77	0.48	-546.38
11	-8,100.96	13	6	7	46.15	828.92	-1,867.79	0.44	0.38	-623.15
10	-6,412.05	13	6	7	46.15	752.04	-1,560.61	0.48	0.41	-493.23

Market losses greatly outweighed then gains over the next 2-5 weeks. The bearish tilt can be observed in several of the above columns.

Below is a list of all the trades with a 25-day exit:

**VIXVXV ratio hits 100-day low.**  
**Buy on close. Sell X days later. \$100k/trade. 8/15/2002-present.**

<b>Date/Time</b>	<b>Signal</b>	<b>Price</b>	<b>% Profit</b>	<b>Run-up DrawDown</b>
08/12/03	Buy	\$990.35	3.60%	\$4,206.00
09/17/03	Sell	\$1,025.97		(\$999.00)
02/12/04	Buy	\$1,152.11	(3.68%)	\$956.32
03/19/04	Sell	\$1,109.74		(\$4,257.00)
04/12/04	Buy	\$1,145.22	(5.34%)	\$225.33
05/17/04	Sell	\$1,084.08		(\$5,994.30)
07/12/04	Buy	\$1,114.35	(3.14%)	\$467.25
08/16/04	Sell	\$1,079.34		(\$4,773.07)
12/17/04	Buy	\$1,194.22	(2.16%)	\$1,965.44
01/25/05	Sell	\$1,168.41		(\$2,529.01)
07/15/05	Buy	\$1,227.92	(0.67%)	\$1,453.14
08/19/05	Sell	\$1,219.71		(\$971.19)
09/16/05	Buy	\$1,237.87	(4.71%)	\$0.00
10/21/05	Sell	\$1,179.59		(\$5,573.60)
12/14/05	Buy	\$1,272.74	(0.70%)	\$1,728.48
01/23/06	Sell	\$1,263.83		(\$2,106.00)
08/16/06	Buy	\$1,295.43	1.74%	\$2,548.70
09/21/06	Sell	\$1,318.03		(\$457.38)
12/11/06	Buy	\$1,413.04	1.24%	\$1,556.10
01/19/07	Sell	\$1,430.50		(\$634.90)
12/20/07	Buy	\$1,460.12	(6.70%)	\$2,633.64
01/29/08	Sell	\$1,362.29		(\$12,924.76)
05/15/08	Buy	\$1,423.57	(7.43%)	\$1,166.90
06/20/08	Sell	\$1,317.86		(\$7,637.70)
06/19/09	Buy	\$921.23	n/a	\$0.00
open	n/a	\$921.23		\$0.00

The maximum intratrade drawdown above is the 4,206 (4%) from the 1<sup>st</sup> trade in August of 2003.

The recent success of moves below 0.92 combined with the fact that the ratio has made a 100-day low suggests the VIX:VXV ratio is indicating a bearish edge over the next several weeks.

Unfortunately, this bearish indication is doing little but keeping our intermediate-term indicators mixed. For now I continue to look for opportunities on both sides of the market and further evidence that a clearer bias is emerging.

## **Catapult and Capitulative Breadth Statistics**

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

### ***Open Catapult Triggers***

DIS –@ 23.49 (*stopped out but still tracking for CBI purposes*)

BA – bought 1/3 @ \$43.14

*New*

BA – buy 1/3 @ \$41.32 limit

### ***Catapult for ETF's Trades***

*none*

***Broad Market Large Cap CBI – 3(DIS,BA-2)***

## **Additional New Trade Ideas**

*A full listing of system triggers can be found at the [system triggers page](#) each night. I will cherry pick some of my favorite setups from the S&P 100 and ETF lists along with occasional other trade ideas to track below.*

*BA – buy 1/3 @ \$41.32 limit – from the Catapult section above. A reminder to subscribers that Catapults are the most volatile strategy we typically have. Size accordingly.*

*SPY –short 1/4 index position @ \$90.90 limit on open. If not filled then move limit to \$91.15 during the day. If still not filled then look to short @ \$90.15 limit on close. I'm looking for a favorable spot to begin scaling in on the short side. I am only looking to enter 1 lot. Should I be filled then subsequent orders will be cancelled.*

## **Active Trades Table**

<b>Symbol</b>	<b>Entry Date</b>	<b>Entry Price</b>	<b>Current Pr</b>	<b>% Gain/Lo</b>	<b>Stop</b>	<b>Notes</b>
GDX	6/9/2009	\$41.30	\$38.30	-7.26%		<b>sold on close &gt; 10ma</b>
AAPL	6/11/2009	\$139.55	\$136.22	-2.39%	\$132.75	<b>sold 1/2 @ \$139.48</b>
GOOG (1/2)	6/12/2009	\$426.86	\$409.29	-4.12%	\$401.00	
GOOG (1/2)	6/15/2009	\$416.77	\$420.09	0.80%		<b>sold @ \$420.09</b>
BA (1/3)	6/24/2009	\$43.14	\$41.32	-4.22%		Catapult

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