

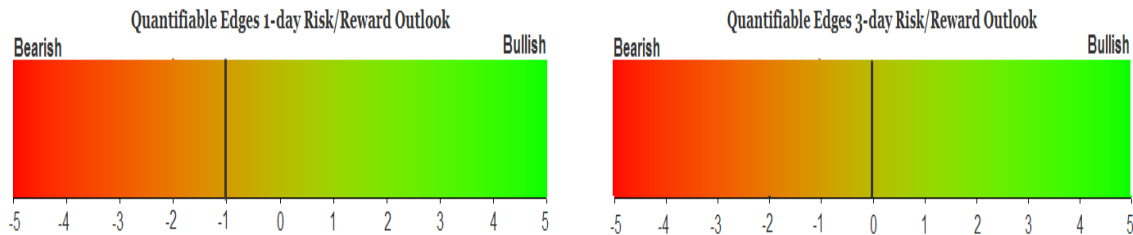
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 25, 2009

Volume 2 Issue 162

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
Active				
August 24, 2009	Strong breadth & vol breakout	1-5 days	Bullish	1.50%
August 24, 2009	Op-ex week positive return	1-5 days	Bearish	-0.90%
August 20, 2009	2 Days Up In Chop	1-4 days	Bearish	
Active - Long Term				
August 4, 2009	75% Up Issues 2 of 3 Days	1-20 days	Bullish	4.80%
July 14, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
Dropped Tonight				
August 21, 2009	Nasdaq 3:2 breadth for 3 days	1-2 days	Bearish	-1.70%
August 24, 2009	Ttl Put/Call 33% < 200ma	1-4 days	Bearish	-2.00%

If the avg max move is achieved the study will appear in **bold italic blue** and no longer be active.

Short-term Outlook – updated 8/25

The Bottom Line

Monday's action was uninspiring and provided little in the way of meaningful new studies. A few bearish studies are dropping off the active list tonight and the Aggregator is beginning to turn positive. The market is still overbought, though. The 1-day edge is based on slightly negative expectations for tomorrow and the overbought nature of the market. I'd prefer to see more decisive action tomorrow before taking any aggressive positions. Right now we're in a bit of a no-man's land.

The Proof

A gap up Monday led to new highs but the rally began to roll over mid-day. After some late wiggling the major indices all ended up fairly close to breakeven. Breadth also came in neutral. The NYSE Up Issue % was 51% and the Up Volume % was 55%. Total volume was lower than Friday but still above average.

Reversals from highs as was seen today are often interpreted as bearish. I've found them to have little predictive value. Below is an example of a study I ran tonight looking at such reversal bars:

SPY gaps up, makes a 20-day high and closes down on the day. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1994 - 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
5	6,143.43	75	37	38	49.33	1,430.91	-1,231.59	1.16	1.13	81.91
4	8,413.21	76	39	36	51.32	1,229.03	-1,097.75	1.12	1.21	110.70
3	1,016.01	80	49	31	61.25	878.62	-1,356.00	0.65	1.02	12.70
2	-696.52	87	49	37	56.32	739.96	-998.77	0.74	0.98	-8.01
1	9,578.12	89	55	33	61.80	591.25	-695.16	0.85	1.42	107.62

There's no discernible edge that I can find when looking at reversals from highs. Reversals from lows, on the other hand, will often suggest an upside edge because the winners tend to be substantially larger.

Only one study appeared on the Quantifnder at the end of the day. It was an interesting one because it had to do with the recent Equity put/call ratios we've been seeing. It last appeared in the 4/14/09 blog. Most interesting was the fact that it had bullish results:

The 3-day average CBOE Equity Put/Call Ratio falls 20% below the 100-day average. Buy SPX on close. Sell X days later. \$100k/trade. 6/2004 - 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
10	18,855.35	16	11	5	68.75	2,444.44	-1,606.69	1.52	3.35	1,178.46
9	16,213.49	16	12	4	75.00	2,019.51	-2,005.16	1.01	3.02	1,013.34
8	20,133.41	17	10	7	58.82	3,093.10	-1,542.51	2.01	2.86	1,184.32
7	14,408.97	17	10	7	58.82	2,379.25	-1,340.50	1.77	2.54	847.59
6	9,197.07	17	8	9	47.06	2,989.01	-1,635.00	1.83	1.63	541.00
5	11,684.67	18	10	8	55.56	2,616.93	-1,810.58	1.45	1.81	649.15
4	12,815.26	20	10	10	50.00	2,529.33	-1,247.80	2.03	2.03	640.76
3	5,930.29	20	13	7	65.00	1,445.32	-1,836.98	0.79	1.46	296.51
2	5,648.85	21	11	10	52.38	1,664.75	-1,266.34	1.31	1.45	268.99
1	6,079.21	22	12	10	54.55	1,059.66	-663.67	1.60	1.92	276.33

This would seem to fly in the face of some of the studies we've seen the last few night suggesting low equity put/call ratios are bearish. My interpretation is that the other studies looked simply at 1-day ratios. In those cases and extremely low day may often have been over exuberance, which was quickly followed by a pullback. When you get a series of days with very low put/call ratios then that is likely due to a series of strong market moves. A lone day is more likely to reverse but real strength that may be seen in over multiple days, is more likely to continue.

Rather than having two put/call studies basically offsetting each other I decided to simply remove the existing one from the active list.

The [Aggregator](#) chart is updated below.

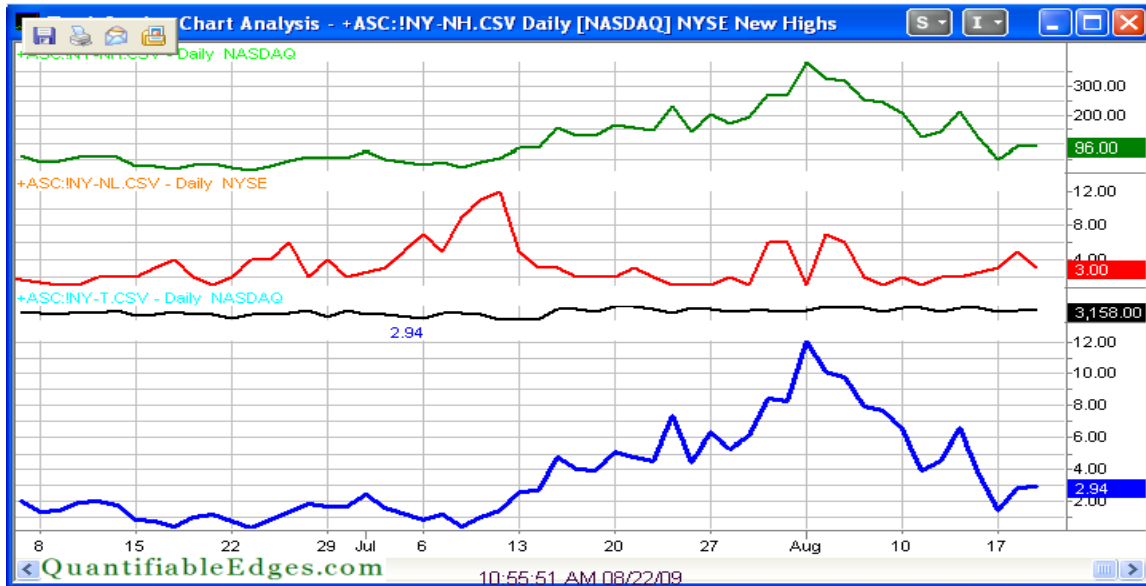


With 2 bearish studies being removed from the active list tonight the green Aggregator line curled up a bit and is now suggesting a slight upside edge over the next 3 days. Tomorrow is slightly negative and then the next two days have positive projections. At the same time the black Differential line is showing that the market has strongly outperformed expectations over the last few days. SPX remains nearly as overbought versus expectations as it has been in over a month. Overbought with upside expectations is basically a neutral configuration.

Intermediate-term Outlook (2 weeks – 2 months)– updated 8/24 – very slightly bullish

Whether this rally can continue or whether it flounders may depend greatly on the breadth of the rally. Breadth is giving somewhat mixed signals lately. One oddity that traders may notice from the charts page is that while the market is now trading at new

highs there has been a noticeable dropoff in the number of individual issues hitting new highs. Below is the chart from the website to demonstrate.



The blue line at the bottom is the net % of stocks hitting new 52-week highs. On August 1st this number was about 12%. Friday it was only 3% - a 9% dropoff. It's fairly rare to see a dropoff this large, but when I tested it I found that it wasn't necessarily bearish. For purposes of testing I lowered the dropoff required to 5% in order to get enough instances. Regardless of the cutoff I used I found the results to be inconsistent and neither bullish nor bearish. Below is one example of a test I ran.

SPX makes a 20-day intraday high and close above its 200ma. The net % of stocks hitting new highs on the NYSE is at least 5 points lower than its 20-day high. Buy on close. Sell X days later. 1970 - present

QE NHs lag on rally: daysin	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
20	16,885.06	26	16	10	61.54	2,088.30	-1,652.78	1.26	2.02	649.43
19	10,845.83	26	14	12	53.85	2,186.88	-1,647.54	1.33	1.55	417.15
18	2,558.27	26	14	12	53.85	1,831.28	-1,923.30	0.95	1.11	98.40
17	-356.37	27	14	13	51.85	1,681.95	-1,838.75	0.91	0.99	-13.20
16	-6,924.34	27	14	13	51.85	1,539.03	-2,190.06	0.70	0.76	-256.46
15	2,688.11	27	15	12	55.56	1,630.76	-1,814.45	0.90	1.12	99.56
14	-2,709.75	27	13	14	48.15	1,733.16	-1,802.92	0.96	0.89	-100.36
13	-1,942.53	29	14	15	48.28	1,922.41	-1,923.75	1.00	0.93	-66.98
12	3,525.81	29	16	13	55.17	1,503.91	-1,579.75	0.95	1.17	121.58
11	2,925.81	29	14	15	48.28	1,467.47	-1,174.59	1.25	1.17	100.89
10	2,778.74	30	15	15	50.00	1,426.81	-1,241.56	1.15	1.15	92.62
9	1,293.47	33	19	14	57.58	951.41	-1,198.80	0.79	1.08	39.20
8	2,294.14	35	20	15	57.14	1,165.27	-1,400.75	0.83	1.11	65.55
7	-2,728.57	38	21	17	55.26	1,212.78	-1,658.64	0.73	0.90	-71.80
6	-627.21	40	24	16	60.00	1,106.06	-1,698.29	0.65	0.98	-15.68
5	-13,004.25	40	17	23	42.50	1,053.25	-1,343.90	0.78	0.58	-325.11
4	-9,092.87	42	17	25	40.48	955.78	-1,013.64	0.94	0.64	-216.50
3	-7,474.66	46	23	23	50.00	664.15	-989.14	0.67	0.67	-162.49
2	-12,506.03	52	22	30	42.31	583.81	-845.00	0.69	0.51	-240.50
1	-8,443.40	67	30	37	44.78	441.60	-586.25	0.75	0.61	-126.02

Is it BETTER to have the number of new highs expanding? Yes. Below I show a similar test where net new highs are also hitting a new high:

<p style="text-align: center;">SPX makes a 20-day intraday high and closes above its 200ma. The net % of stocks hitting new highs on the NYSE the highest in 20 days. Buy on close. Sell X days later. 1970 - present</p>											
QE NHs lag on rally: daysin	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	
20	59,666.34	87	55	32	63.22	2,926.27	-3,164.95	0.92	1.59	685.82	
19	82,536.66	91	59	32	64.84	2,956.05	-2,874.64	1.03	1.90	907.00	
18	86,537.02	91	60	31	65.93	2,844.26	-2,713.51	1.05	2.03	950.96	
17	65,533.97	93	57	36	61.29	2,718.05	-2,483.18	1.09	1.73	704.67	
16	71,709.96	96	61	35	63.54	2,550.55	-2,396.39	1.06	1.85	746.98	
15	72,810.49	99	63	36	63.64	2,537.90	-2,418.82	1.05	1.84	735.46	
14	58,225.04	102	65	37	63.73	2,360.60	-2,573.34	0.92	1.61	570.83	
13	64,551.10	105	72	33	68.57	2,039.31	-2,493.30	0.82	1.78	614.77	
12	51,733.67	108	67	41	62.04	2,073.75	-2,127.01	0.97	1.59	479.02	
11	51,450.24	112	70	42	62.50	1,997.82	-2,104.69	0.95	1.58	459.38	
10	46,021.40	114	66	48	57.89	2,001.49	-1,793.27	1.12	1.53	403.70	
9	52,224.07	115	72	43	62.61	1,816.61	-1,827.25	0.99	1.66	454.12	
8	46,836.80	123	73	50	59.35	1,736.29	-1,598.25	1.09	1.59	380.79	
7	43,034.75	124	73	51	58.87	1,640.14	-1,503.84	1.09	1.56	347.05	
6	28,952.82	131	76	55	58.02	1,450.06	-1,477.31	0.98	1.36	221.01	
5	19,908.03	138	79	59	57.25	1,285.57	-1,383.93	0.93	1.24	144.26	
4	29,381.48	145	76	69	52.41	1,228.56	-927.38	1.32	1.46	202.63	
3	23,529.89	153	84	69	54.90	988.79	-862.73	1.15	1.40	153.79	
2	22,182.02	167	87	80	52.10	803.28	-596.29	1.35	1.46	132.83	
1	17,266.09	217	118	99	54.38	558.37	-491.13	1.14	1.36	79.57	

So if we see this number expand then that would help the rally's chances to continue. On the positive side the advance/decline line is hitting new highs. We also had a 90% day on Friday. As we saw in July, if we get a couple of 90% up days within close proximity then that can often be a decent intermediate-term buy signal. Therefore I'll be very interested to see if we get some additional days of extremely strong breadth this week.

Many of the negatives that had been present are still present, such as the low VIX:VXX ratio, the excessive Nasdaq vs. NYSE volume and the generally downsloping total volume over the last few months. Still, the negative effects of these influences has been slow to kick in.

Right now the market is still in rally mode, and betting against it for any extended period of time has not worked. Short trades need to be small and profits taken when available. I expect we're going to see a substantial selloff begin at some point in the next several months. I don't see evidence of it happening just yet.

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

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.

None tonight – Neutral market bias and almost nothing showing up on the triggers page. Wait and see mode.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/L	Stop	Notes
SPY(1/4)(s)	8/20/2009	\$100.75	\$102.96	-2.19%	\$104.01	

I've placed a stop above Monday's high on the SPY position. A move that strong would likely be accompanied by strong breadth and combined with Friday's strong breadth day could trigger another intermediate-term breadth signal. Rather than attempt a graceful exit, I'll just take the loss on my ¼ position, step aside, and wait for a better edge. A move down tomorrow could ignite some bullish studies and would also likely convince me to exit. I may lower stops or suggest closing the trade idea on a close lower via an intraday update tomorrow.

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