

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 4, 2009

Volume 2 Issue 170

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				
September 3, 2009	Big down then little down	1-6 days	Bullish	2.40%
September 3, 2009	2 down in chop	1-4 days	Bullish	2.70%
September 2, 2009	1% drop heavy vol no 10-low	1-5 days	Bearish	-2.90%
Active - Long Term				
July 14, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
Dropped Tonight				
August 28, 2009	2 down in chop	1-3 days	Bullish	
August 28, 2009	False breakdown & close at new high	1-5 days	Bullish	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 9/3

The Bottom Line

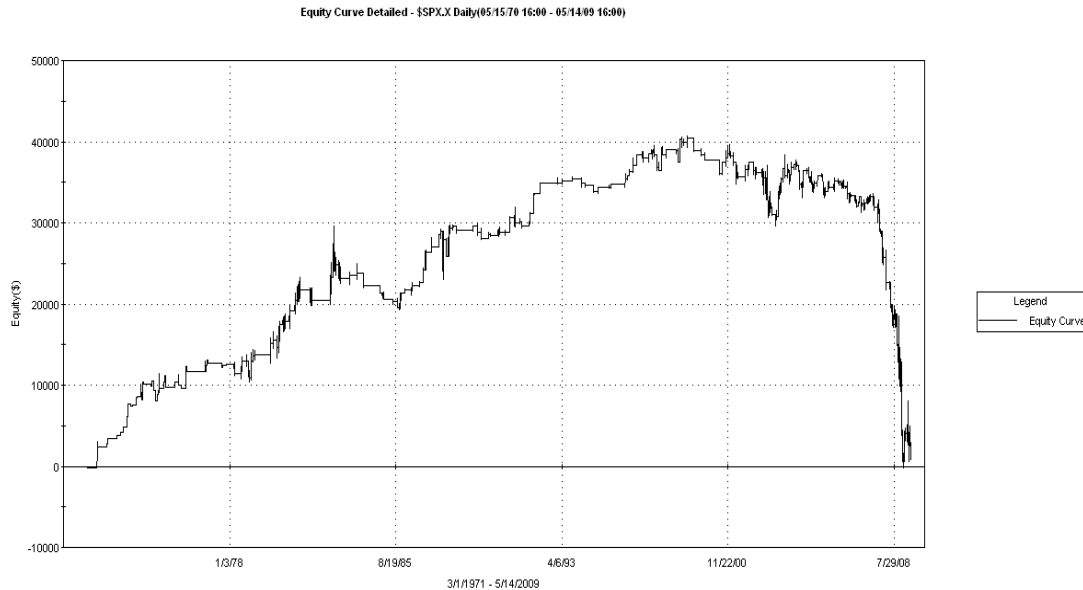
The move up today failed generate any truly bearish signals. The current active studies still remain slanted bullish. History suggests we may see some more upside tomorrow. If the market does rise then much of the bullish edge should wear off. So while I'm expecting strength I'll also be looking to sell into it.

The Proof

After gapping up and pulling back in early trading the market bounced and then consolidated for most of the day. A surge in the last hour led to a strong finish. Both the Nasdaq and S&P closed up about 0.8%. NYSE breadth was strong. The NYSE Up Issues % closed at 77.5% and the Up Volume % was 85%. Volume came below the levels of the last few days.

The one study that showed up on the Quantifinder tonight was one that examined strong breadth / weak volume days like today. Below is an excerpt from the 5/15/09 Subscriber Letter:

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:

Advancers outnumber down issues by at least 2 to 1. Volume declines from yesterday.										
Buy S&P 500 on close. Sell X days later. \$100k/trade. 08/01/2007 - present.										
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.

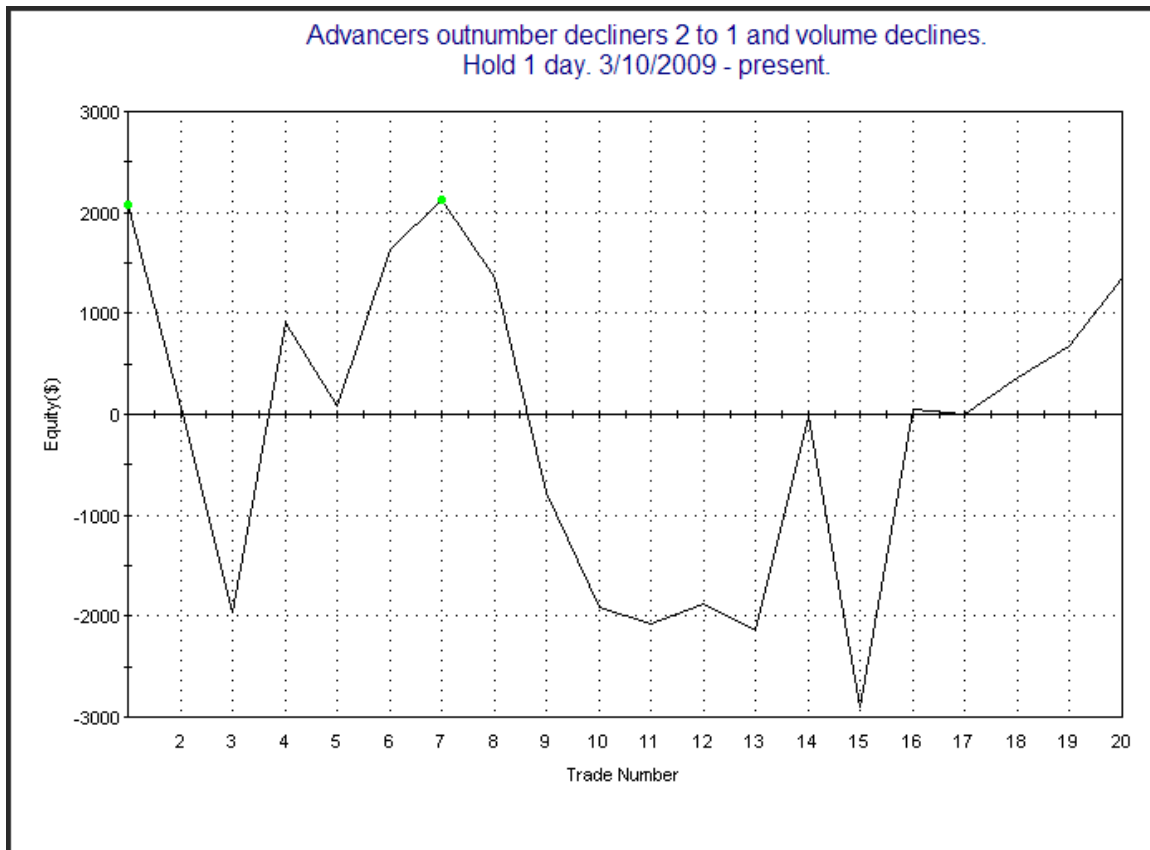
Of course the concern with the time period I looked at here is that the market already had an extreme negative bias – especially after up days. So were the results due primarily to the strongly bearish market conditions, or did a sustainable downside edge exist with the

good breadth / bad volume combo? To examine this I looked at this same setup since the March bottom. The results are below:

**Advancing outnumber declining issues by at least 2 to 1. Volume declines from yesterday.
Buy SPX on close. Sell X days later. \$100k/trade. 3/10/2009 - 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	7,174.74	12	8	4	66.67	2,239.43	-2,685.18	0.83	1.67	597.90
4	12,701.12	14	9	5	64.29	2,518.70	-1,993.44	1.26	2.27	907.22
3	3,041.62	16	8	8	50.00	2,597.59	-2,217.39	1.17	1.17	190.10
2	942.85	19	11	8	57.89	1,614.38	-2,101.92	0.77	1.06	49.62
1	1,353.71	20	10	10	50.00	1,360.98	-1,225.61	1.11	1.11	67.69

There have been a decent number of instances and no downside edge is apparent. Below is the equity graph for the 1-day holding period.



If there's an edge here I'm not clever enough to find it. I'll likely drop this study from the Quantifinder for the time being.

But this doesn't really fully address whether Thursday's low volume should be a concern. I decided to run a few additional tests to see how the market had performed after other times there was a bounce from severely oversold short-term conditions. I looked back to

the beginning of 1999 for these tests. First let's look at what happened when volume came in higher.

Yesterday the SPX RSI(2) closes < 5. Today the SPX closes up on **higher** volume.
Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1999 - 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	-1,415.88	13	6	7	46.15	1,439.39	-1,436.03	1.00	0.86	-108.91
4	-2,691.05	13	7	6	53.85	965.99	-1,575.50	0.61	0.72	-207.00
3	-6,497.85	13	3	10	23.08	2,058.11	-1,267.22	1.62	0.49	-499.83
2	-5,247.04	13	4	9	30.77	1,059.24	-1,053.78	1.01	0.45	-403.62
1	-6,793.21	13	4	9	30.77	315.66	-895.09	0.35	0.16	-522.55

11 of 13 (85%) instances closed below the entry price at some point in the next 3 days.

Interesting that the high volume bounces failed to follow through. The number of instances is a bit low but the numbers are fairly compelling anyway. Let's see how this compares to low volume bounces:

Yesterday the SPX RSI(2) closes < 5. Today the SPX closes up on **lower** volume.
Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1999 - 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	16,958.31	21	11	10	52.38	2,678.62	-1,250.66	2.14	2.36	807.54
4	12,921.05	23	13	10	56.52	2,025.54	-1,341.10	1.51	1.96	561.78
3	8,292.65	23	14	9	60.87	1,532.04	-1,461.76	1.05	1.63	360.55
2	8,895.06	23	14	9	60.87	1,360.26	-1,127.62	1.21	1.88	386.74
1	7,027.74	23	13	10	56.52	960.09	-545.34	1.76	2.29	305.55

19 of 23 (83%) instances closed above the entry price at some point in the next 3 days.

Here the results have a solid bullish tilt.

From my perspective, I can find no reason to believe Thursday's light volume should be of any concern. In fact, it may be a market positive.

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



Even with the move up today the Aggregator chart remains bullish. The green Aggregator line is solidly above 0, signifying net bullish expectations over the next few days. The black Differential line is also well above zero. This illustrates the market has strongly underperformed expectations over the last 3 days. Tomorrow night we will see Tuesday's selloff drop out of the calculation. Therefore any rise or breakeven day tomorrow should see the Differential line drop below zero. A move of either line through the zero line is often a good exit signal, so I will be looking to sell my index position into strength tomorrow.

Intermediate-term Outlook (2 weeks – 2 months)– updated 8/31 – very slightly bullish

A week of going nowhere has done nothing to clarify the intermediate-term picture. Breadth was the big discussion in last week's outlook nothing was resolved there. The 90% up day on Friday the 21st has not been closely followed by another breadth surge. If it had that would have hinted at real strength.

I also discussed in detail how the number of stocks hitting new 52-week highs had shrunk since late July / early August. While the market was hitting new highs the stocks participating in those highs was declining. As I showed, this is not a death sentence for the rally. Results going forward were mixed. The market outlook does improve substantially, though, when the number of new highs is expanding and confirming the index highs.

The other indicators that have provided some interesting studies over the last several weeks haven't changed at all in the past week, either. Negative indications such as

the low VIX:VXV ratio, the excessive Nasdaq vs. NYSE volume and the generally downsloping total volume over the last few months are still in play. Of course the negative effects of these indicators 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 2-3 months. I don't see compelling evidence of it just yet.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

CAT – buy 1/3 position at \$43.84 (bought @ \$43.84)

CAT – buy 1/3 position @ \$43.51 (no fill – cancel entry order)

AVP – buy 1/3 position @ \$30.01

Catapult for ETF's Trades

IWN – bought @ \$52.12

Broad Market Large Cap CBI –3(CAT-2,AVP)

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.

AVP – buy 1/3 position @ \$30.01 limit. Based on the Catapult signal listed above.

Note: there are also quite a few triggers on the triggers page tonight for traders looking for more action.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/L	Stop	Notes
CAT(1/3)	9/2/2009	\$43.84	\$45.04	2.74%		
SPY(1/4)	9/3/2009	\$99.90	\$100.65	0.75%		

CAT is getting quite close to its exit trigger. After I calculate them in the morning I will alert subscribers as to the target prices.

SPY has some nice support around the \$99.50 - \$99.60 area having bottomed there 2 days in a row. I may look to place a stop there depending on early action tomorrow. If SPY opens at \$101.25 or higher I will sell half of the position on the open. If not filled on the open, that order will be cancelled. In any case I will look to sell the whole lot on a close of \$101.66 or higher tomorrow.

The employment report should set the tone tomorrow. Traders could consider taking some profits before the announcement (premarket) if they're concerned about the reaction to the report.

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