

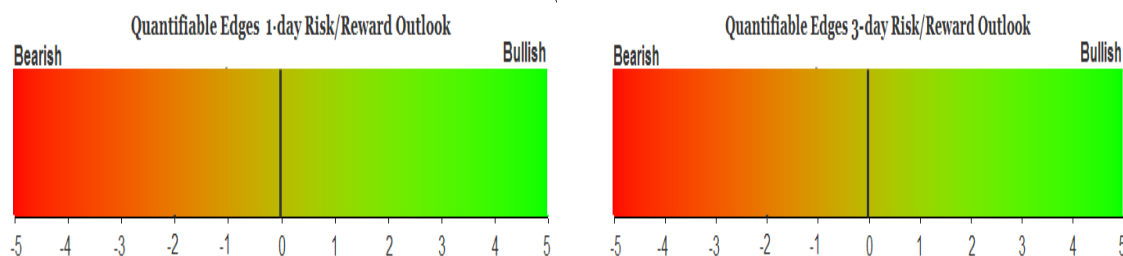
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 8, 2009

Volume 2 Issue 171

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 8, 2009	Strong Breadth No 10-high	1-8 days	Bearish	-4.20%
September 8, 2009	Rise into Labor Day	1-4 days	Bearish	-1.35%
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				

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

Short-term Outlook – updated 9/8

The Bottom Line

The bullish edge of the last two days has pretty much worn off. The market is no longer oversold and risk/reward now appears about breakeven. A little more time and northward price movement could set up a downside edge but we aren't there quite yet.

The Proof

Price and breadth put in strong days on Friday. The market found its low in the first 25 minutes of trading and then put in a steady move higher for most of the rest of the day. It also managed to close near its highs. The NYSE Up Issues % came in at 80% and the Up Volume % was 86.5%. Total volume was the lowest in over 2 weeks, which isn't terribly surprising heading into a long weekend.

Several studies came up in the Quantifinder tonight and most of them were related to breadth. What's interesting is that there was some conflict between the studies with regards to the effect of the strong breadth over the last 2 days. Let's dig into them and see if we can determine where the edge really lies.

The bullish results came from the breadth study originally published to the blog on 4/21/08. I've re-run that study and updated the results below:

NYSE Up Issues % > 75% in 2 of the last 3 days. Buy SPX on close. Sell X days later. \$100k/trade. 1970-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: WinLoss Ratio	All: ProfitFactor	All: Avg Trade
20	87,977.22	38	27	11	71.05	4,693.29	-3,521.96	1.33	3.27	2,315.19
19	87,325.04	40	28	12	70.00	4,400.07	-2,989.74	1.47	3.43	2,183.13
18	82,340.51	40	30	10	75.00	3,841.51	-3,290.49	1.17	3.50	2,058.51
17	81,010.18	41	29	12	70.73	4,213.78	-3,432.44	1.23	2.97	1,975.86
16	70,698.54	41	30	11	73.17	3,909.60	-4,235.41	0.92	2.52	1,724.35
15	58,822.23	42	26	16	61.90	4,182.97	-3,120.94	1.34	2.18	1,400.53
14	55,995.56	42	31	11	73.81	3,363.61	-4,388.75	0.77	2.16	1,333.23
13	48,005.39	43	31	12	72.09	3,072.73	-3,937.43	0.78	2.02	1,116.40
12	29,221.02	44	28	16	63.64	3,094.48	-3,589.02	0.86	1.51	664.11
11	35,282.95	44	26	18	59.09	3,363.87	-2,898.76	1.16	1.68	801.89
10	44,588.69	44	28	16	63.64	3,344.91	-3,066.80	1.09	1.91	1,013.38
9	43,871.93	44	29	15	65.91	3,258.34	-3,374.66	0.97	1.87	997.09
8	38,900.32	44	29	15	65.91	2,790.48	-2,801.58	1.00	1.93	884.10
7	34,889.27	44	28	16	63.64	2,852.17	-2,810.72	1.01	1.78	792.94
6	32,174.88	45	29	16	64.44	2,363.05	-2,272.11	1.04	1.89	715.00
5	29,160.57	46	29	17	63.04	2,171.65	-1,989.25	1.09	1.86	633.93
4	35,704.30	48	29	19	60.42	1,966.77	-1,122.75	1.75	2.67	743.84
3	27,187.51	50	31	19	62.00	1,939.01	-1,732.73	1.12	1.83	543.75
2	12,702.61	56	33	23	58.93	1,349.32	-1,383.69	0.98	1.40	226.83
1	21,178.46	62	38	23	61.29	955.08	-657.15	1.45	2.40	341.59

This suggests that when you get a series of strong breadth days in close succession it often leads to further follow through. The % profitable and avg trade columns are both quite positive. If this is all we looked at then the interpretation of the move over the last 2 days would have to be bullish.

But on 4/2/2009 in the nightly Subscriber Letter I looked at similar studies and showed that not only was the breadth an important determinant, but also where the thrust took place within the context of the recent price range. I found at that time that multi-day breadth thrusts similar to this were typically bullish if they also caused the market to be hitting new short-term price highs. Failure to reach new highs suggested a bounce that was more likely to falter. I've updated two of those studies below that demonstrate this principal.

First let's look at time where the breadth thrust led to a new 10-day high.

NYSE Up Issues % closes above 70% for 2 days in a row. SPX makes a 10-day intraday high today. Buy SPX on close. Sell X days later. \$100k/trade. 1970 -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
15	70,103.77	75	44	31	58.67	3,448.69	-2,633.50	1.31	1.86	934.72
14	76,693.30	75	44	31	58.67	3,252.63	-2,142.66	1.52	2.15	1,022.58
13	75,718.79	76	48	28	63.16	3,058.84	-2,539.48	1.20	2.06	996.30
12	52,548.75	76	47	29	61.84	2,748.22	-2,641.99	1.04	1.69	691.43
11	47,422.65	76	49	27	64.47	2,600.60	-2,963.22	0.88	1.59	623.98
10	58,201.91	77	50	27	64.94	2,605.22	-2,668.86	0.98	1.81	755.87
9	42,285.84	78	45	33	57.69	2,561.13	-2,211.06	1.16	1.58	542.13
8	33,534.77	79	47	32	59.49	2,296.30	-2,324.72	0.99	1.45	424.49
7	28,468.03	80	46	34	57.50	2,344.73	-2,334.99	1.00	1.36	355.85
6	29,759.81	84	49	35	58.33	2,053.79	-2,025.02	1.01	1.42	354.28
5	28,644.45	85	50	35	58.82	1,775.01	-1,717.32	1.03	1.48	336.99
4	15,949.59	86	49	37	56.98	1,548.48	-1,619.62	0.96	1.27	185.46
3	10,371.96	88	47	41	53.41	1,411.06	-1,364.59	1.03	1.19	117.86
2	11,439.73	92	53	39	57.61	987.72	-1,048.96	0.94	1.28	124.34
1	10,286.85	101	54	46	53.47	658.32	-549.18	1.20	1.41	101.85

This test varied slightly from the one above in that it only required a 70% Up Issue % rather than 75% and it also required the 2 days be consecutive. The results were pretty much in line, though, suggesting bullish tendencies if we achieve a new 10-day high.

Now for those times where the breadth thrust failed to achieve a 10-day high as was the case on Friday.

NYSE Up Issues % closes above 70% for 2 days in a row. SPX fails to make a 10-day intraday high today. Buy SPX on close. Sell X days later. \$100k/trade. 1970 -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
12	-77,761.09	25	7	18	28.00	1,926.16	-5,069.12	0.38	0.15	-3,110.44
11	-64,165.29	25	5	20	20.00	3,082.94	-3,979.00	0.77	0.19	-2,566.61
10	-62,346.57	25	7	18	28.00	1,831.49	-4,175.94	0.44	0.17	-2,493.86
9	-58,336.87	25	7	18	28.00	1,917.53	-3,986.64	0.48	0.19	-2,333.47
8	-63,574.16	25	7	18	28.00	1,660.26	-4,177.56	0.40	0.15	-2,542.97
7	-53,040.00	25	8	17	32.00	2,026.68	-4,073.73	0.50	0.23	-2,121.60
6	-32,257.05	25	8	17	32.00	2,090.88	-2,881.42	0.73	0.34	-1,290.28
5	-22,926.01	25	10	15	40.00	1,461.57	-2,502.78	0.58	0.39	-917.04
4	-11,998.95	25	14	11	56.00	1,430.06	-2,910.89	0.49	0.63	-479.96
3	-714.58	25	13	12	52.00	1,619.62	-1,814.14	0.89	0.97	-28.58
2	1,549.75	25	12	13	48.00	1,660.47	-1,413.53	1.17	1.08	61.99
1	1,491.14	26	13	13	50.00	1,102.83	-988.12	1.12	1.12	57.35

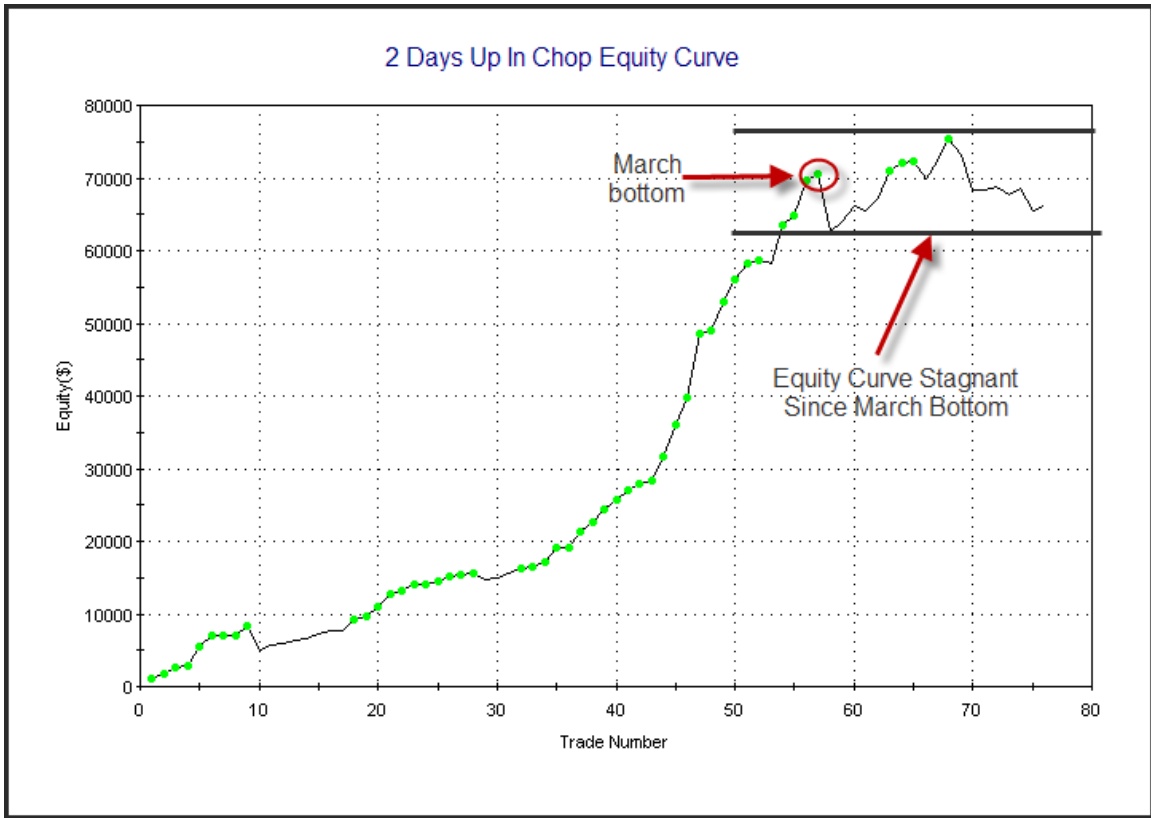
There is a drastic difference here in the results. Implications went from solidly bullish to very strongly bearish. The failure to make a new 10-day high after 2 strong up days suggests there must have been a sizable move down just prior to the bounce. In most cases the selloff managed to reassert itself.

But now let's recall that the 1st test with the most bullish results required a 75% Up Issues % rather than just the 70% used above. What if we increased the above requirements to 75%? How would the results look then?

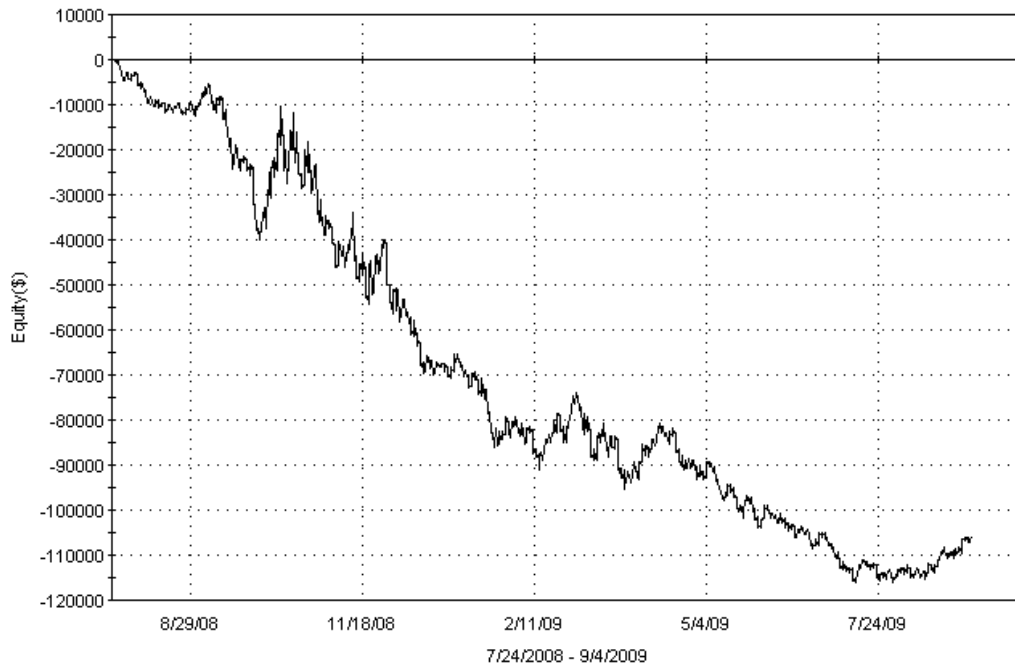
NYSE Up Issues % closes above 75% for 2 days in a row. SPX fails to make a 10-day intraday high today. Buy SPX on close. Sell X days later. \$100k/trade. 1970 -present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	-21,390.40	5	0	5	0.00	0.00	-4,278.08	0.00	0.00	-4,278.08
15	-15,689.60	5	1	4	20.00	2,546.00	-4,558.90	0.56	0.14	-3,137.92
10	-14,343.78	5	0	5	0.00	0.00	-2,868.76	0.00	0.00	-2,868.76
9	-15,440.84	5	1	4	20.00	1,165.80	-4,151.66	0.28	0.07	-3,088.17
8	-11,827.14	5	1	4	20.00	2,197.60	-3,506.19	0.63	0.16	-2,365.43
7	-10,209.42	5	1	4	20.00	2,251.20	-3,115.16	0.72	0.18	-2,041.88
6	-4,911.21	5	1	4	20.00	2,090.40	-1,750.40	1.19	0.30	-982.24
5	1,837.45	5	2	3	40.00	2,198.90	-853.45	2.58	1.72	367.49
4	7,330.18	5	5	0	100.00	1,466.04	0.00	100.00	100.00	1,466.04
3	5,351.84	5	3	2	60.00	2,720.99	-1,405.56	1.94	2.90	1,070.37
2	6,553.27	5	3	2	60.00	2,474.56	-435.21	5.69	8.53	1,310.65
1	7,848.51	6	4	2	66.67	2,250.23	-576.21	3.91	7.81	1,308.09

There are too few instances here to draw solid conclusions from but the consistency is compelling nonetheless. First we see that all 5 instances followed through to the upside over the short-term. Four days out they were all trading higher with an average gain of close to 1.5%. In fact, while they failed to make a 10-day high on the initial 2-day thrust, 4 of the 5 instances did manage to make 10-day highs within the next 4 days. Fascinating though is that the bounce was a bit of a last hurrah for all of them. Once we get out 10 and 20 days you can see that every occurrence led to lower prices. And the average loss was quite substantial – 2.9% over 10 days and 4.3% over 20 days. Again, this last test is too limiting to draw any solid conclusions from but I do find it confirming of the previous study that showed failure to make a 10-day high on the move suggest a downside edge.

Subscribers will also note that Friday would have triggered a short entry for the “2 Days Up In Chop” system that I have tracked here for over a year. I am not including “2 Days Up In Chop” in the Aggregator tonight for a couple of reasons. First of all the studies above are already suggestive that the market has risen strongly for two days. Adding the system to these results would effectively be double counting. Secondly, as I’ve noted several times recently, “2 Days Up In Chop” has struggled since the March bottom. Below is an updated equity curve.



The peak in the curve actually occurred in late June but we've basically been in a range for 5 ½ months now. Much of this is due to the fact that the market has in fact acted less choppy lately. Below is an updated "Trend vs. Chop" chart from the website.



An upward slope suggests the market is following through on a day to day basis while a downward slope suggests the market is chopping back and forth. More information may be found out about this indicator by using the [Trend vs. Chop label on the blog](#).

Until I see some reassertion of choppy market conditions I will give careful consideration before including the “2 Days Up In Chop” strategy in the Aggregator.

From a seasonality standpoint, Labor Day week has historically been a bit weak.

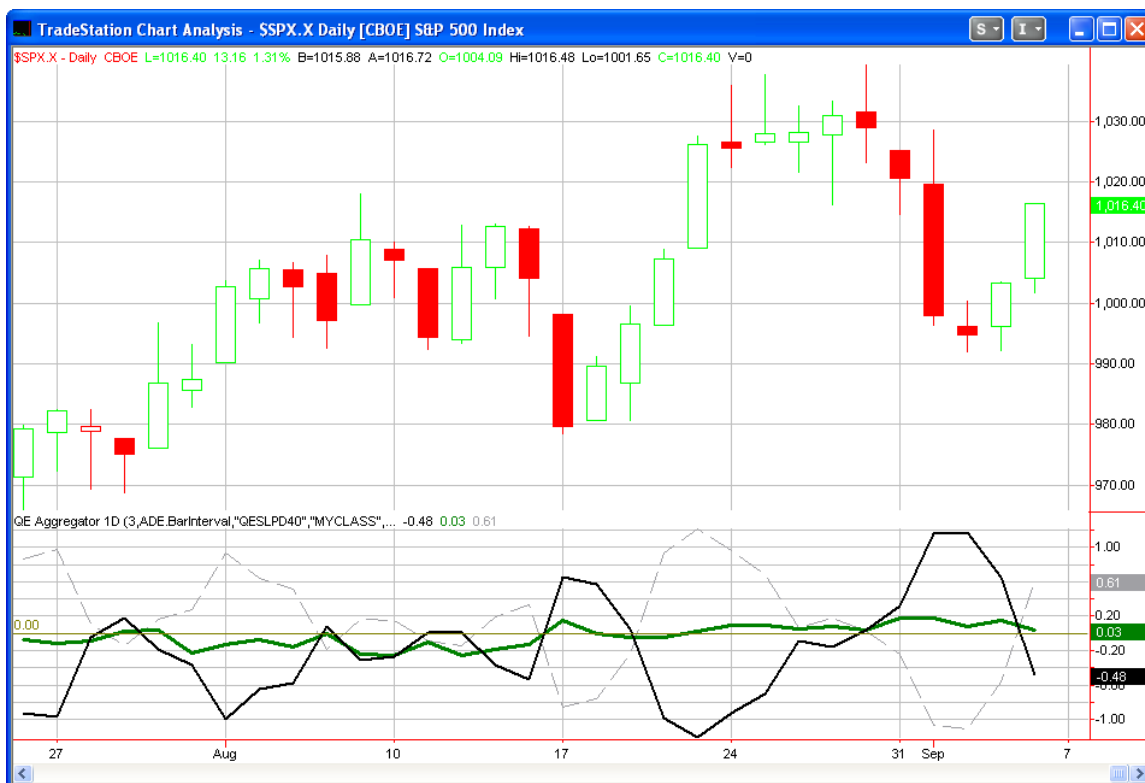
Labor Day week performance of SPX. \$100k/trade. 1960 - present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
4	-3,171.76	48	23	25	47.92	1,328.59	-1,349.18	0.98	0.91	-66.08
3	-8,079.30	48	25	23	52.08	923.12	-1,354.67	0.68	0.74	-168.32
2	-4,681.96	48	22	25	45.83	1,136.65	-1,187.53	0.96	0.84	-97.54
1	-927.22	48	26	22	54.17	852.60	-1,049.76	0.81	0.96	-19.32

Tuesday – Thursday have shown risk/reward to favor the bears, though whether the market is up or down has basically been a coin toss. If we look at times like the present where the market has made gains in the weeks leading up to Labor Day, you’ll find the implication is a bit more bearish.

SPX moves higher over the 20 days leading up to Labor Day. Buy SPX on close the Friday before Labor Day. Sell X days later. \$100k/trade. 1960-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
4	-11,993.69	30	11	19	36.67	1,117.61	-1,278.28	0.87	0.51	-399.79
3	-9,308.92	30	15	15	50.00	879.86	-1,500.45	0.59	0.59	-310.30
2	-7,183.71	30	12	17	40.00	1,004.65	-1,131.74	0.89	0.63	-239.46
1	-4,971.69	30	16	14	53.33	615.88	-1,058.99	0.58	0.66	-165.72

This isn’t the most compelling edge I’ve ever published, but for a study based primarily on seasonality, it’s not bad.

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



As I discussed was possible Thursday night, the strong move up on Friday caused some significant changes to the Aggregator chart. The green Aggregator line dropped quite a bit and is now just slightly above zero. This suggests a net positive expectation from the studies over the next 3 days, but one that is barely in line with the long-term drift of the market. The black Differential line dropped sharply and is now well below zero. This illustrates that the market has overshot positive expectations over the last 3 days.

This basically leaves the SPX overbought with mildly positive expectations. This suggests a situation where risk/reward is close to even. Notable is that both bullish studies are very close to their target levels. In other words, if the market can just manage a small rally at some point tomorrow, then the 2 bullish studies will likely achieve their profit targets and be removed from the Active List. Should this happen we would see a substantially negative effect on the Aggregator line. So if the market manages to actually close up above 1020 then there stands a good chance, dependent on the studies tomorrow, that I'd begin taking on short exposure.

Intermediate-term Outlook (2 weeks – 2 months)– updated 9/8 – neutral

There's little to say from an intermediate-term standpoint that I haven't said in the last couple of weeks. There are a fair amount of indicators suggesting downside but over the last month and a half or so those suggestions haven't been worth anything.

The VIX:VXV ratio again dropped below 0.9 on Friday as noted by the Quantifinder. From 2002 – mid 2009 this was a very reliable precursor to a market selloff. The selloffs didn't always occur immediately. In fact the average amount of time the signal took to completely wear off was close to 4 months. So the fact that it has been nearly 2 months and this indicator hasn't "worked" isn't entirely abnormal.

I believe breadth will be important to monitor as we move forward here. There have been some strong breadth numbers over the last couple of days. In the short-term outlook above I concluded that the combination of market structure and breadth suggested downside rather than upside. This could change should we continue to see strong advance/decline readings. Another breadth measure that may be worth watching is the NYSE Net New Highs %. I showed a couple of weeks ago that while a lagging number of new 52-week highs is not a death sentence, the market prospects can be substantially improved when new 52-week highs confirm new index price highs. So far we've got a ways to go before either is reached.

I've seen nothing that would cement the idea that the current rally is over. There's a decent amount of evidence that the market has come too far too fast and we'll likely see a pullback at some point here in the not-to-distant future.

The basic premise I'm working under remains that we are in a [1930's – style environment](#) in which both rallies and selloffs will be much more exaggerated than most market participants are used to. Just as the bear market up to March 2009 was incredibly extreme, so has been the rally since then. I believe there is going to be a lot of back and forth over the next few years and the swings will continue to feel extreme. It may be important to keep this in mind when considering market action.

Catapult and Capitulative Breadth Statistics

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

Open Catapult Triggers

AVP – buy 1/3 position @ \$30.01

Catapult for ETF's Trades

IWN – bought @ \$52.12

Broad Market Large Cap CBI –1(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.

None – With the market outlook neutral and some positions already on, I’m content to simply manage the current trades and wait for a more substantial edge before allocating additional capital.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Pr	% Gain/Lo	Stop	Notes
CAT(1/3)	9/2/2009	\$43.84	\$46.11	5.18%		sold on close
SPY(1/4)	9/3/2009	\$99.90	\$102.06	2.16%		sold on close
IWN	9/3/2009	\$52.12	\$53.45	2.55%	\$52.20	
AVP(1/3)	9/4/2009	\$29.96	\$30.88	3.07%	\$29.99	

CAT and SPY were both closed out for nice gains. Both also just missed 2nd entries on 9/3/09 – with CAT missing by only a few cents. It can be disappointing when you don’t get a large fill on very successful trades, but it’s all part of trading. It’s nice to have the solid gains even if the sizes were a little small.

Should the market come through with a bit more upside before dropping lower as the studies are suggesting then there is a good chance IWN and AVP will hit their exit triggers. In case things fall apart sooner than anticipated, I’ve put stops in on both. No sense letting trades that are this profitable turn into losers.

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.