

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 9, 2009

Volume 2 Issue 172

## 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
<b>Active</b>				
September 9, 2009	Low range & vol 20 close > 10ma	1-5 days	Bearish	
September 9, 2009	SPY rising on falling volume	1-3 days	Bearish	
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 2, 2009	1% drop heavy vol no 10-low	1-5 days	Bearish	-2.90%
<b>Active - Long Term</b>				
July 14, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
<b>Dropped Tonight</b>				
<b>September 3, 2009</b>	<b>Big down then little down</b>	<b>1-6 days</b>	<b>Bullish</b>	<b>2.40%</b>
<b>September 3, 2009</b>	<b>2 down in chop</b>	<b>1-4 days</b>	<b>Bullish</b>	<b>2.70%</b>

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

### **Short-term Outlook – updated 9/9**

#### **The Bottom Line**

The bullish studies came off the board tonight. New bearish ones were added. Also, the market is becoming stretched and overbought. Based on the Aggregator chart below it appears the bearish tendencies are now stronger than they've been in weeks. Edge goes to the bears tonight.

#### **The Proof**

The market gapped up almost 1% today, and then...nothing. As one astute reader pointed out, today's SPY range was the lowest in 550 days. That's over 2 years. Breadth was tilted positive as the NYSE Up Issues % registered 75% and the Up Volume % 65%.

Total volume was about average on the NYSE. Curiously low was the volume in the major ETF's – SPY and QQQQ.

A lot popped up on the Quantifinder tonight. There were 9 studies listed and not a single one of them was bullish. Some studies had to do with breadth, which I covered fairly in depth yesterday. There were also several related to low volume and low range days for SPY and QQQQ.

The most relevant of the low range / low volume studies was last updated in the 6/29 Letter and I've updated it again tonight.

SPY intraday range is the smallest in 20 days on the lightest volume in 20 days and close > 10ma.  
Buy on close. Sell X days later. \$100k/trade. 1993 - 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	-64,116.86	44	21	23	47.73	1,878.10	-4,502.47	0.42	0.38	-1,457.20
14	-53,473.70	46	27	19	58.70	1,918.72	-5,541.00	0.35	0.49	-1,162.47
13	-44,317.30	46	29	17	63.04	1,966.52	-5,961.55	0.33	0.56	-963.42
12	-38,668.64	47	28	19	59.57	1,839.66	-4,746.27	0.39	0.57	-822.74
11	-35,670.47	47	26	21	55.32	1,801.34	-3,928.83	0.46	0.57	-758.95
10	-42,192.15	47	24	23	51.06	1,867.15	-3,782.77	0.49	0.52	-897.71
9	-39,319.05	47	25	22	53.19	1,765.74	-3,793.75	0.47	0.53	-836.58
8	-27,507.38	49	27	22	55.10	1,754.57	-3,403.67	0.52	0.63	-561.38
7	-34,366.86	49	25	24	51.02	1,567.11	-3,064.36	0.51	0.53	-701.36
6	-26,487.94	49	26	23	53.06	1,488.62	-2,834.43	0.53	0.59	-540.57
5	-38,495.33	51	21	30	41.18	1,495.12	-2,329.76	0.64	0.45	-754.81
4	-35,917.75	51	22	29	43.14	1,231.69	-2,172.93	0.57	0.43	-704.27
3	-23,615.97	54	23	31	42.59	1,245.96	-1,686.23	0.74	0.55	-437.33
2	-18,535.37	55	23	32	41.82	945.43	-1,258.76	0.75	0.54	-337.01
1	-18,776.92	56	22	34	39.29	803.79	-1,072.36	0.75	0.49	-335.30

The 1<sup>st</sup> 5 days are fairly suggestive of a downside edge. While the chances of trading higher or lower are about even after that, the win/loss ratio is heavily skewed to the bearish side. This suggests bearish implications may last even longer than a week.

In the 5/30/08 Subscriber Letter I showed how 3 up days for the SPX had different meanings depending on the volume pattern. Rising volume suggested more upside while volume that wasn't consistently rising suggested a pullback. Notable today was that SPY has closed higher for 3 days in a row and SPY volume declined every one of those days. Below is a study that looks at this situation:

SPY closes higher 3 days in a row while volume declines 3 days in a row.  
Buy on close. Sell X Days later. \$100k/trade. 1993 - present.

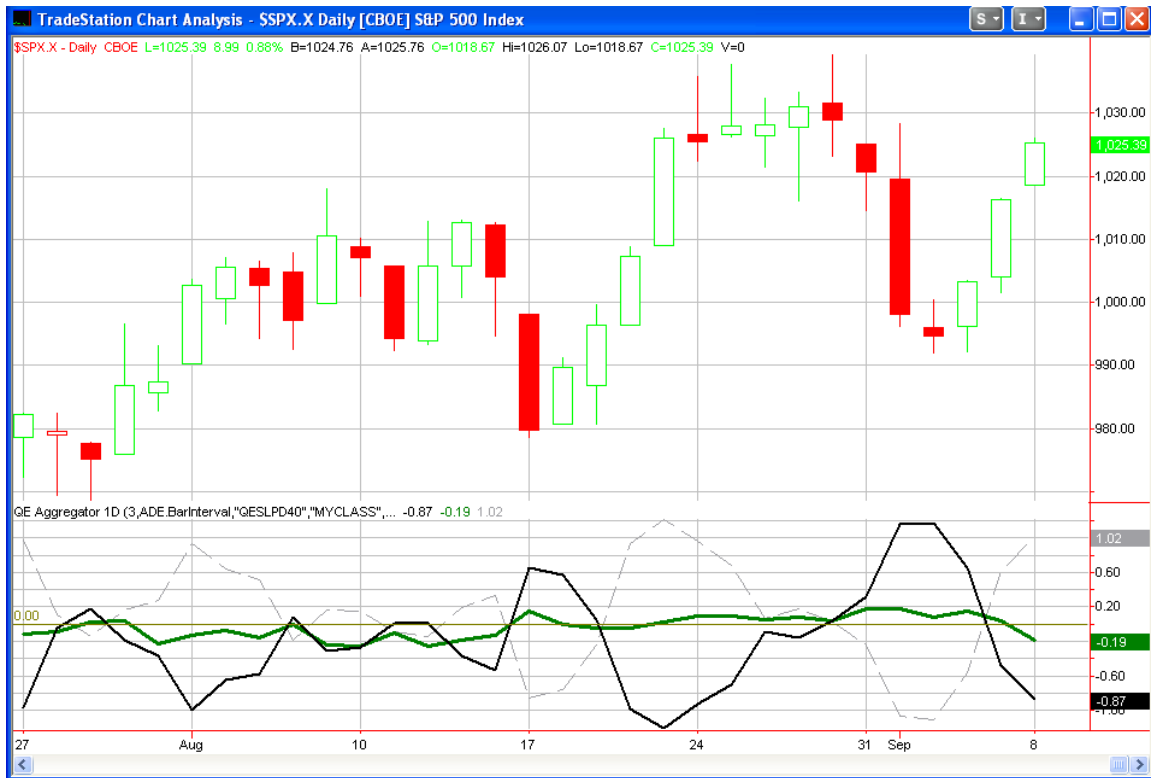
QE Finder Tester: daysin	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	-66,032.07	30	9	21	30.00	3,725.23	-4,740.91	0.79	0.34	-2,201.07
19	-70,295.92	30	9	21	30.00	3,442.05	-4,822.59	0.71	0.31	-2,343.20
18	-60,734.47	32	11	21	34.38	3,019.04	-4,473.52	0.67	0.35	-1,897.95
17	-58,654.12	32	10	22	31.25	2,861.10	-3,966.59	0.72	0.33	-1,832.94
16	-53,084.32	32	11	21	34.38	2,827.21	-4,008.75	0.71	0.37	-1,658.89
15	-60,264.39	32	11	21	34.38	2,774.92	-4,323.26	0.64	0.34	-1,883.26
14	-56,551.71	33	11	22	33.33	2,950.64	-4,045.85	0.73	0.36	-1,713.69
13	-55,598.80	33	11	22	33.33	2,535.20	-3,794.82	0.67	0.33	-1,684.81
12	-42,077.64	33	14	19	42.42	1,813.48	-3,550.86	0.51	0.38	-1,275.08
11	-31,307.25	33	14	19	42.42	1,958.68	-3,090.99	0.63	0.47	-948.70
10	-35,211.99	33	15	18	45.45	2,135.82	-3,736.08	0.57	0.48	-1,067.03
9	-31,426.61	33	16	17	48.48	1,930.90	-3,665.94	0.53	0.50	-952.32
8	-25,532.32	33	14	19	42.42	2,092.73	-2,885.82	0.73	0.53	-773.71
7	-29,878.63	33	16	17	48.48	1,404.00	-3,078.98	0.46	0.43	-905.41
6	-31,241.33	33	14	19	42.42	1,341.44	-2,632.71	0.51	0.38	-946.71
5	-34,420.85	33	15	16	45.45	940.84	-3,033.34	0.31	0.29	-1,043.06
4	-29,602.40	34	12	21	35.29	1,030.20	-1,998.32	0.52	0.29	-870.66
3	-31,789.18	34	11	23	32.35	793.93	-1,761.84	0.45	0.22	-934.98
2	-13,708.01	35	13	22	37.14	1,036.96	-1,235.84	0.84	0.50	-391.66
1	-2,527.86	37	16	21	43.24	1,265.06	-1,084.23	1.17	0.89	-68.32

**82% of instances posted a close below the entry price at some point in the next 4 days.**

This setup appears especially bearish over the 1<sup>st</sup> week. Like the 1<sup>st</sup> study, possible bearish implications extend far out beyond the 1<sup>st</sup> week, though.

As I noted in my intraday email this morning both of the bullish studies from the Active List achieved their targets and have therefore been removed from the Aggregator. They are being replaced with the 2 bearish studies shown tonight.

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



Both the green Aggregator line and the black Differential line continued to fall on Tuesday and are now both squarely below 0. This indicates that the net expectations from the studies is bearish over the next few days and the performance over the last 3 days has exceeded expectations. Overbought with negative expectations is a bearish configuration and is what I look for when considering short trades.

To take advantage of this I'm going to look to take on some short exposure. In fact, I personally took some near the close Tuesday. Often I'll look to take on at least part of my allocation near the close rather than waiting for the next day's open. Subscribers who wish to anticipate how the Aggregator and market outlook may change from day to day could do so by incorporating the intraday quantifinder. The intraday quantifinder will often give a flavor of some of the studies to be discussed that night and included in the Aggregator. Between knowing the bullish studies are about to come off the board as I mentioned Tuesday morning and the Intraday Quantifinder showing up all red, subscribers should have been fairly confident that the Aggregator would be suggesting a bearish edge.

In the near future I will release results of a system that automates Aggregator signals to take positions long and short. I believe subscribers will find the results interesting and encouraging.

***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***

*none*

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

*none*

***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.*

*SPY – Short 1/4 index position @ \$102.90 limit. Based on the short-term market outlook above. I'm looking to keep it small for now since the market remains in a strong intermediate-term uptrend and shorting has been extremely difficult for the last few months. I'll likely look to take some pretty quick profits on at least part of the position since this is a counter-trend trade.*

### **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>
IWN	9/3/2009	\$52.12	\$54.17	3.93%		<b>sold on close</b>
AVP(1/3)	9/4/2009	\$29.96	\$31.37	4.71%		<b>sold on close</b>

Both AVP and IWN met their targets as discussed in the intraday update and were sold at the close for nice profits.

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