

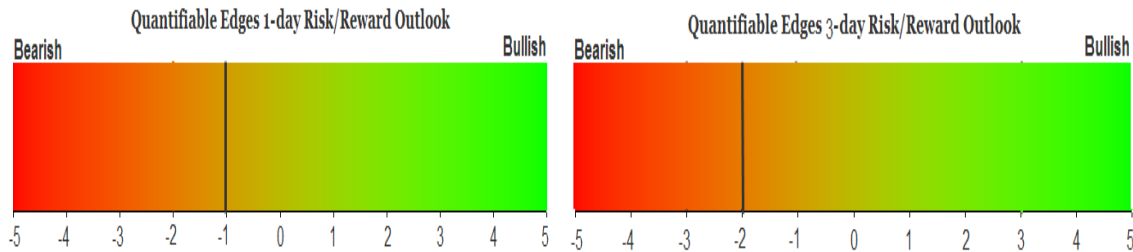
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 20, 2009

Volume 2 Issue 201

Market Overview



Tonight's Research Points

- The profit target for the October 15 bullish study was reached which removes it from the Active Studies list a bit early.
- Last night's short-term bearish study based on strong drops from a 10-day high got off to a rough start. I find no evidence that suggests the study should not remain in place at this point, though.
- The SPX and VIX both closed up. This is more common on Mondays than any other day, but still suggests a short-term downside edge for the SPX.
- The Aggregator system fired off a short signal today as the Aggregator line joined the Differential line in negative territory.

Short-term Outlook – updated 10/20

The Bottom Line

Another strong day wiped out Friday's losses and put the market at new highs. The market remains overbought and some short-term bearish studies are now beginning to emerge. There appears to be a mild downside edge at the moment. AAPL's afterhours trading may help to get a gap up tomorrow. From an already high level this could provide a favorable short entry.

Should the gap expand tomorrow morning, traders may want to revisit this old blog post.

<http://quantifiableedges.blogspot.com/2009/08/large-gaps-up-from-1-month-high.html>

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				
October 20, 2009	SPX & VIX both close higher on Monday	1-3 days	Bearish	-1.70%
October 19, 2009	Big drop from 10-high above 200	1-3 days	Bearish	-1.40%
October 15, 2009	Breakout above 50-day high	1-5 days	Bullish	1.80%
Active - Long Term				
October 19, 2009	VIX:VXV drops below 0.9	2-5 months	Bearish	
Dropped Tonight				
October 14, 2009	SPX 5 up then down while > 200ma	1-9 days	Bullish	2.10%

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

The Evidence

The market put in a strong performance Monday. After a small gap up, it pulled back briefly and filled the opening gap. From there it rallied strongly for most of the rest of the day. The major indices all tacked on about 1% today. Breadth was positive as the NYSE Up Issues % came in at 73% and the Up Volume % was 69%. Total volume declined to the lowest level in a week. A bit of a boost was provided after the bell by AAPL's earnings.

Today's action didn't leave a whole lot to go on, but there were a few things worth looking at. Last night's study suggested a big drop on big volume from a 10-day high provided a short-term downside edge. That study got off to a rough start today as the SPX rallied back to a new 10-day high. I wondered whether this might invalidate the bearish edge suggested last night. Therefore I looked at other times that last night's setup was followed by a new 10-day high the next day. Of the 36 instances that qualified last night, only 4 managed a 10-day high close the next day. Stats of those 4 instances are below.

Two days ago SPX closed at a 10-day high. Yesterday it suffered its largest drop in 10 days on the highest NYSE volume in 10 days. Today it rallied back to close at a new 10-day high. Buy on close. 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	
5	-3,174.11	4	2	2	50.00	1,920.79	-3,507.84	0.55	0.55	-793.53	
4	-3,716.69	4	2	2	50.00	1,565.63	-3,423.97	0.46	0.46	-929.17	
3	-3,201.34	4	2	2	50.00	1,956.39	-3,557.06	0.55	0.55	-800.34	
2	-1,118.52	4	1	3	25.00	1,709.70	-942.74	1.81	0.60	-279.63	
1	-759.31	4	1	3	25.00	2,565.94	-1,108.42	2.31	0.77	-189.83	

You never want to read much into 4 instances, but I certainly don't see any evidence that the bearish edge is invalidated by today's move.

With a late surge the VIX managed to close in positive territory today. It's a bit unusual for the SPX and the VIX to close in the same direction. Historically, when they both close higher there has been some giveback from the S&P over the next few days. One quirk with the VIX though is that it has a tendency to fall on Fridays and rise on Mondays. Therefore this setup is more common on Mondays than any other day of the week. I discussed this and broke out the results based on Mondays, Fridays, and mid-week occurrences in the 8/3/09 Letter. Below I've updated the Monday results.

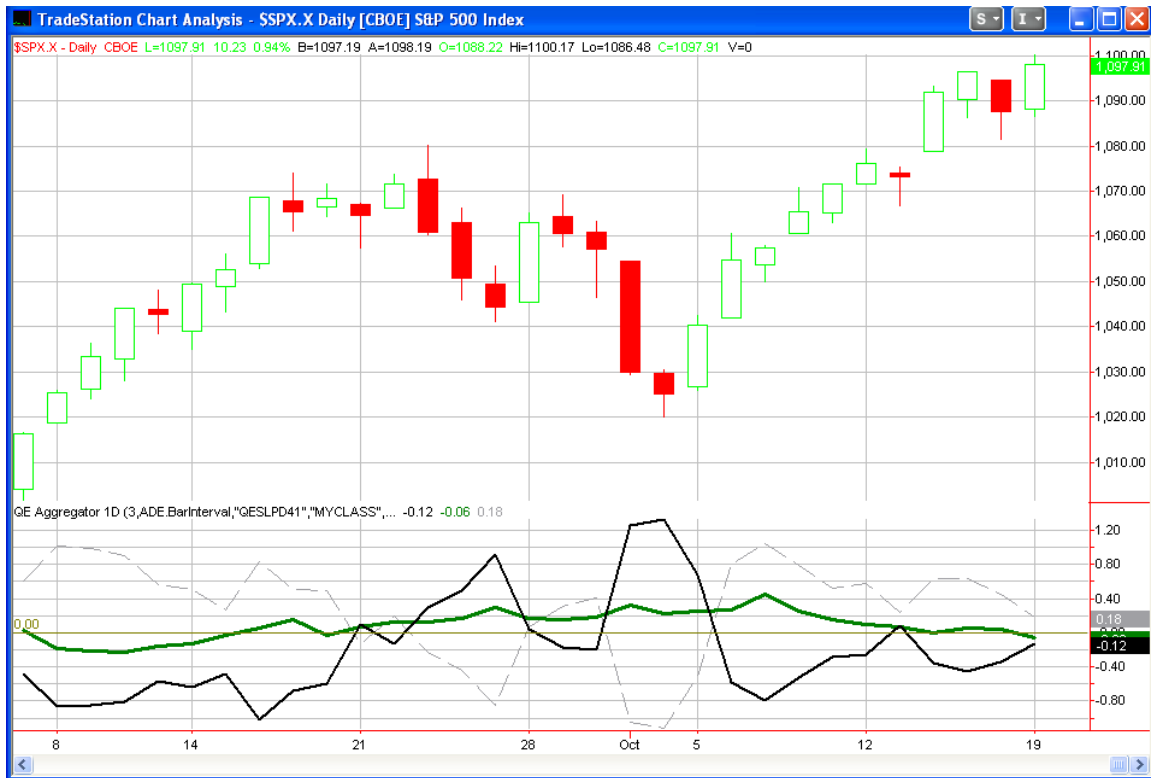
SPX and VIX both close up. Buy on close. Sell X days later. \$100k/trade. 1998 - present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-45,591.22	109	50	59	45.87	1,786.60	-2,286.80	0.78	0.66	-418.27
4	-39,127.02	112	49	63	43.75	1,615.88	-1,877.86	0.86	0.67	-349.35
3	-42,048.53	112	50	62	44.64	1,221.94	-1,663.64	0.73	0.59	-375.43
2	-35,281.59	112	48	64	42.86	955.12	-1,267.62	0.75	0.57	-315.01
1	-30,973.20	112	44	68	39.29	701.23	-909.22	0.77	0.50	-276.55

78% of instances closed lower than the entry price at some point in the next 3 days.

Even with the tendency for the VIX to rise on Mondays built in to the study, there still appears to be a bit of a downside edge.

Notable from the Active Studies list is the fact that the "Breakout to a 50-day high" study from the October 15th Letter reached its profit target as has been removed. This along with the SPX/VIX study above has helped to swing net expectations negative.

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



The green Aggregator line dipped below 0 tonight to finish at -0.06. This illustrates the negative expectations from the active studies. The black Differential line crept higher but still closed in negative territory as well. This shows that the SPX has outperformed expectations over the last few days. Both lines below 0 is typically considered a bearish configuration. It basically means the market is overbought with negative expectations. Historically this has provided a downside edge.

The configuration, though bearish, is relatively weak from both the Aggregator and Differential values. Personally, rather than go full boar, I'll start by tiptoeing on the short side. Shorts have also been especially tricky for months now, which lends a bit more reason to be cautious.

The systems page was updated with the probable short outlook from the Aggregator system about 15 minutes before the close today. Notification was sent out via Twitter. Be sure to follow "qerob" on Twitter if you want notification when the systems page is updated each afternoon.

Intermediate-term Outlook (2 weeks – 2 months)– updated 10/19 – slightly bullish

The intermediate-term outlook is unchanged since the 10/19 Letter. That Letter may be accessed using the link below:

[2009-10-19 QE Subscriber Letter.pdf](#)

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.

SPY – short 1/4 index position @ \$109.79 limit. Based on the short-term market outlook. Just dipping my toe at this point. I'll likely increase the size should the edge appear to grow.

SPY – short 1/4 index position @ \$110.65 limit ON OPEN. If not filled on open – cancel order. As noted in the “Bottom Line” on page 1 of the Letter, a large gap up tomorrow would also suggest an intraday downside edge. With a downside edge already in place based on the Aggregator, I would look to get a bit more aggressive if I could sell into a large gap up. Depending on market action, I may look to exit this portion of the trade at tomorrow's close. Below is another link to the study mentioned above on page 1.

<http://quantifiableedges.blogspot.com/2009/08/large-gaps-up-from-1-month-high.html>

Active Trades Table

none.

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