

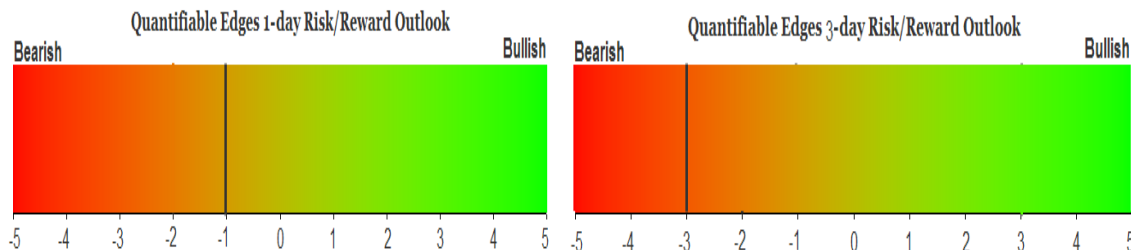
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 20, 2010

Volume 3 Issue 12

Market Overview



Tonight's Research Points

- Moves from a 5-day low to a 10-day high are often followed by a pullback.
- The Aggregator System remains short.

Short-term Outlook – updated 1/20

The Bottom Line

Tuesday's strong rally occurred in the face of a couple of bearish studies from the weekend. Another bearish study appeared tonight and the short-term edge appears to be to the downside at this point.

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	Avg MM - 1/3 Std Dev
Active					
January 20, 2010	5 low to 10 high	1-5 days	Bearish	-1.80%	-1.20%
January 19, 2010	10 high drop on highest vol and %	1-3 days	Bearish	-1.40%	-1.00%
January 19, 2010	7 day high to 7 day low above 200ma	1-2 days	Bearish	-1.10%	-0.70%
Active - Long Term					
January 13, 2010	No bearish divergence at high	int. term	Bullish		
December 23, 2009	SPX and TNX hit 50-day high	1-10 weeks	Bearish		
December 23, 2009	Low p/c without strong SPX rise	1-5 weeks	Bearish		
December 7, 2009	Nasdaq Leading S&P	int. term	Bullish		
December 2, 2009	VIX:VXV crosses below 0.9	2-5 months	Bearish		

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

Subscribers will note that I have added (back) another column to the Active Studies list. This time it displays the Average Max Move – 1/3 Standard Deviation. As volatility has waned fewer and fewer studies have seen their targets achieved. With the VIX now below 20 I decided it was time again to lower the targets. Long-time subscribers will recall that back in late 2008 and early 2009 the target was the Average Max Move + 1 Standard Deviation. As the VIX fell under 40 it was lowered to Avg MM + ½ Standard Deviation, and for the last several months we’ve just been targeting the Avg Max Move. With volatility continuing to shrink and so few studies achieving their targets I’ve decided to now ratchet the target down again. As volatility levels change over time I’ll continue to adjust the targets.

The Evidence

A very small down open was immediately filled and the market put in a steady trend day higher from there. The major indices all saw nice gains with the S&P gaining 1.3%, the Nasdaq up 1.4% and the Russell 2000 gaining 1.8%. Breadth was strongly positive. The NYSE Up Issues % was 76% and the Up Volume % came in at 84%. Total volume declined from Friday’s levels and was below normal.

Only one study appeared in the Quantifinder this evening, and it seemed to be the most substantial piece of evidence that I found tonight. The last time I wrote about this was in the Jan 5th 2010 Letter. I’ve updated the stats again tonight.

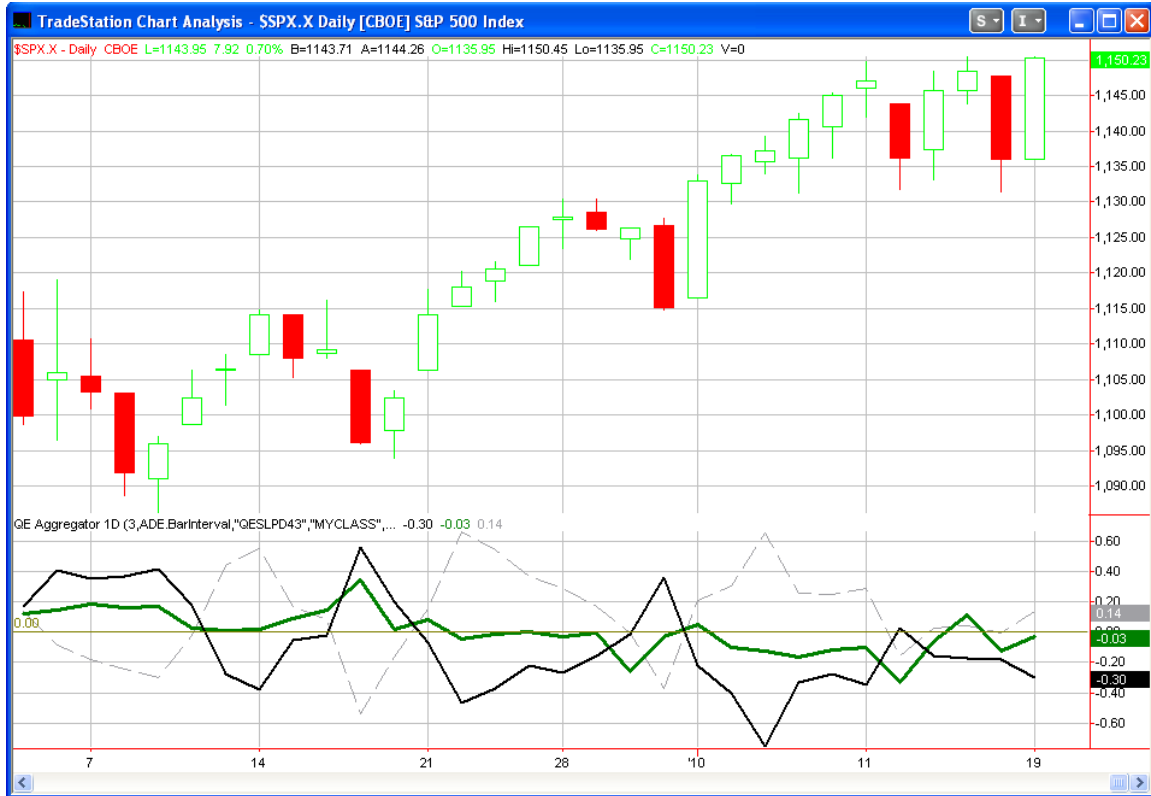
Yesterday the SPX closed at a 5-day low. Tonight is closed at a 10-day high.
Buy on close. Sell X days later. \$100k/trade. 1994 - present.

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
10	2,648.42	25	16	9	64.00	1,599.08	-2,548.54	0.63	1.12	105.94
9	-4,494.78	25	14	11	56.00	1,484.62	-2,298.14	0.65	0.82	-179.79
8	-9,637.20	25	14	11	56.00	1,507.21	-2,794.38	0.54	0.69	-385.49
7	-13,925.35	25	12	13	48.00	1,533.01	-2,486.26	0.62	0.57	-557.01
6	-16,219.72	25	12	13	48.00	1,133.63	-2,294.10	0.49	0.46	-648.79
5	-15,079.10	25	11	14	44.00	1,116.94	-1,954.67	0.57	0.45	-603.16
4	-8,312.99	25	12	13	48.00	1,255.94	-1,798.79	0.70	0.64	-332.52
3	-2,544.62	25	16	9	64.00	883.76	-1,853.87	0.48	0.85	-101.78
2	-6,760.49	25	10	15	40.00	788.97	-976.68	0.81	0.54	-270.42
1	-1,955.48	25	16	9	64.00	463.33	-1,040.97	0.45	0.79	-78.22

80% of instances closed lower than the trigger price at some point in the next week.

The last couple of instances have not acted according to the norm as the recent rally has run this study over. Still, there appears to be a bearish edge and I’m not prepared to back off it yet. I’ve decided to include this study in the Active Studies list above.

I have updated the [Aggregator](#) chart below.



Tuesday's runup didn't change the basic configuration of the Aggregator chart. The green Aggregator line remains below 0, illustrating the net negative expectations from the active studies over the next few days. Meanwhile the black Differential line shows that the SPX has outperformed expectations over the last few days. Both lines below 0 is a bearish configuration and has historically provided a downside edge. The Aggregator System remains short, and I will be looking to add short exposure in the trade ideas section below.

Without additional bullish studies the Aggregator line will remain negative tomorrow. The pivot level for the Differential number will be 1145.15 tomorrow. A close below this level would move the black Differential line into positive territory and signal an end to the Aggregator System short signal.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/19 –somewhat bullish

When the SPX hit a new high on Monday the 11th, it was also accompanied by a new high in the advance/decline line and a new high in the % of new 52-highs on the NYSE. I discussed last week that every major top since 1970 has seen a divergence lasting a minimum of 2 months in at least one of these breadth measures before the ultimate top was hit in the SPX. I provided a link to that study last week and have included it again below. It can be found in the intermediate-term section of the letter.

[2009-10-12 QE Weekly Research Letter.pdf](#)

The one major difference between all the tops I examine in the study and the current situation is that the others all took place at all-time highs. While the SPX has run up close to 70% from the March bottom, it is still nowhere near an all-time high. A top here could exhibit different characteristics than those previous tops. Still, the evidence would seem to suggest to me that the market is not yet ripe to undergo any type of major correction and we will probably be hitting new highs again before any major correction occurs.

While these broad breadth measures are arguing for a continuation of the rally, there has been what could be perceived as a lack of buying conviction lately. Enthusiasm seems to be waning. The last time there was a 90% up volume day was early November. And it's not just breadth, but total volume has also been failing to spike on up days. It was this strong buying conviction that kept the Aggregator positive for most of the fall, and it's the lack of this type of action that has allowed for negative Aggregator readings over the last few weeks. Positive Aggregator readings will also typically arise when the market gets overdone to the downside. And in uptrends like we are in now, even mild pullbacks often suggest a bullish edge. But there haven't been any. Since Thanksgiving there has only been once instance where the S&P pulled back two days in a row. That was December 7th and 8th. Other than that, every down day has been followed by an up day. Generally, it would seem that that lack of enthusiastic breadth and volume on up days leaves the market more susceptible to a minor pullback. I wouldn't expect we'll see a whole lot more than that, though – even with the bearish intermediate-term studies that may be found on the studies list near the top of this letter.

Also contributing to the bullish outlook is the fact that the Nasdaq continues to lead the S&P in terms of relative strength.

I won't be betting against this uptrend on an intermediate-term basis until I see real evidence of weakness.

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 ¼ index position @ \$115.06 limit.

SPY – short ¼ index position @ \$115.06 limit on close.

I'm looking to take on a ½ short position. I'll look to take the 1st piece at a level equal to Tuesday's close. The 2nd piece will be added at the close if the market doesn't sell off.

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.