

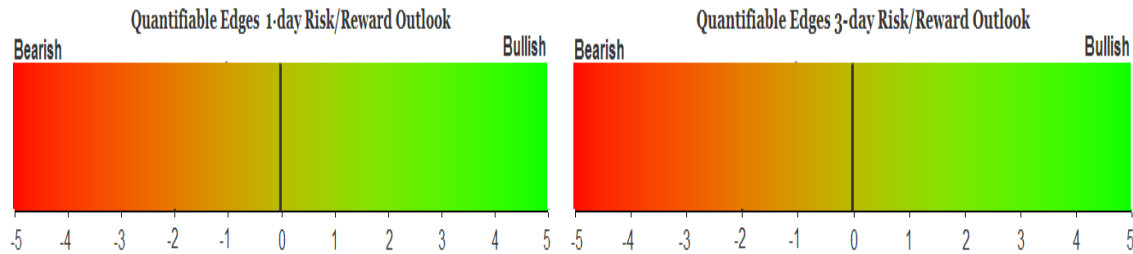
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 12, 2010

Volume 3 Issue 29

Market Overview



Tonight's Research Points

- Today was a Follow Through Day for the market. Over the short-term that has provided a bit of an upside edge.
- Strong breadth for the 2nd time in 3 days suggests negative implications when the market fails to make a new 10-day high.
- The Friday before Presidents Day is seasonally bearish.
- The Aggregator System changed to flat at Thursday's close.

Short-term Outlook – updated 2/12

The Bottom Line

If the market can keep its momentum Thursday's Follow Through Day could lead to a move back near or above the January highs. The news was mixed, though with bearish studies also appearing tonight. I'm happily back on the sidelines and awaiting the market to tip it's hand a bit before looking to re-enter.

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				
February 12, 2010	Friday before Presidents Day	1 day	Bearish	
February 12, 2010	2 of 3 75% Up Issues % No 10-day high	1-9 days	Bearish	-4.40%
February 12, 2010	IBD Follow Through Day	1-6 days	Bullish	2.70%
February 9, 2010	Put/Call Ratio 3-day spike	1-4 days	Bullish	2.50%
February 5, 2010	2% Drop 10 low bottom 10% range	1-7 days	Bullish	4.50%
Active - Long Term				
February 8, 2010	Worden %>200ma - %>40ma > 40	3 - 7 weeks	Bullish	
February 1, 2010	McClellan -60 for 6 days in a row	1-20 days	Bearish	
January 13, 2010	No bearish divergence at high	int. term	Bullish	
Dropped Tonight				
February 10, 2010	Unfilled large gap from 50-low	1-2 days	Bearish	

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

The Evidence

After starting a little weak the market put in a nice turnaround on Thursday. The major indices all closed strongly higher and near the top of their daily ranges. The S&P 500 rose 1%, the Nasdaq 1.4%, and the Russell 2000 was up 1.6%. Breadth was strong as the NYSE Up Issue % came in at 76% and the Up Volume % was 79%. Total NYSE volume rose but still came in below average.

With the markets rising more than 1% on higher volume exactly 4 days after a potential bottom, today can be labeled a Follow Through Day (FTD). As I mentioned last night I did an extensive study of FTD's on the blog back in 2008. A summary page with links may be found here:

<http://quantifiableedges.blogspot.com/2008/07/follow-through-days-quantified.html>

Among the links found on that page, traders might be especially interested in the study of short-term implications [from Feb 1, 2008](#). In that post I point out that while intermediate-term traders often view the FTD with bullish optimism, swing traders may see it as a short setup since the market is now "overbought in a downtrend". We've seen many, many times before that overbought doesn't necessarily mean a downside edge and oversold doesn't necessarily mean an upside edge. This is why two lines are incorporated in the Aggregator and why confirmation is needed with both lines before a position is taken. So below I've updated the stats showing SPX performance in the days following a FTD.

Buy on the close of a Follow Through Day. 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
10	30,152.12	71	40	31	56.34	3,282.24	-3,262.49	1.01	1.30	424.68
9	28,745.79	71	38	33	53.52	3,378.94	-3,019.82	1.12	1.29	404.87
8	33,900.71	71	37	34	52.11	3,432.08	-2,737.84	1.25	1.36	477.47
7	33,416.03	71	40	31	56.34	3,095.44	-2,916.18	1.06	1.37	470.65
6	45,144.37	71	46	25	64.79	2,665.48	-3,098.71	0.86	1.58	635.84
5	41,243.01	71	44	27	61.97	2,499.27	-2,545.36	0.98	1.60	580.89
4	37,110.22	71	40	31	56.34	2,510.98	-2,042.87	1.23	1.59	522.68
3	35,777.60	71	40	31	56.34	2,279.14	-1,786.71	1.28	1.65	503.91
2	25,423.41	71	40	31	56.34	1,915.83	-1,651.93	1.16	1.50	358.08
1	23,203.93	71	38	33	53.52	1,186.73	-663.39	1.79	2.06	326.82

79% of instances posted a close above the entryprice at some point in the next week.

Results are solidly, though not overwhelmingly, bullish. In any case the edge appears to be to the upside and it is certainly an environment that you want to be cautious of trying to short. Another point made in that Feb 1, 2008 post was that the direction the market takes in the week after the FTD is often indicative of the chances of success. I'll be sure to keep this in mind as the next week's action unfolds.

The one study that appeared in the Quantifinder tonight was from the 9/8/2009 Letter and looked at strong breadth days that occurred within close proximity of each other. I've updated the results below:

NYSE Up Issues % > 75% in 2 of 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: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	99,285.85	44	31	13	70.45	4,484.08	-3,055.42	1.47	3.50	2,256.50
15	73,685.73	48	32	16	66.67	3,863.15	-3,120.94	1.24	2.48	1,535.12
10	60,865.56	50	34	16	68.00	3,233.37	-3,066.80	1.05	2.24	1,217.31
9	58,997.70	50	33	17	66.00	3,330.64	-2,994.92	1.11	2.16	1,179.95
8	52,311.42	50	34	16	68.00	2,798.77	-2,677.93	1.05	2.22	1,046.23
7	47,774.87	51	33	18	64.71	2,905.48	-2,672.56	1.09	1.99	936.76
6	42,672.50	52	34	18	65.38	2,420.91	-2,202.13	1.10	2.08	820.63
5	36,527.82	53	35	18	66.04	2,094.20	-2,042.74	1.03	1.99	689.20
4	39,572.38	55	35	20	63.64	1,859.91	-1,276.22	1.46	2.55	719.50
3	30,002.66	57	36	21	63.16	1,855.49	-1,752.14	1.06	1.82	526.36
2	13,684.30	63	38	25	60.32	1,294.53	-1,420.31	0.91	1.39	217.21
1	21,286.11	69	41	26	59.42	913.75	-622.21	1.47	2.32	308.49

On the surface results appear to be strong. In that 9/8/09 Letter I used a slightly different setup and filtered by times the market achieved an intraday high versus times it didn't. I applied that same filter to the above test this evening. First let's look at times the breadth was accompanied by a new short-term high:

NYSE Up Issues % > 75% in 2 of last 3 days and makes a 10-day intraday high. 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	107,484.86	36	27	9	75.00	5,166.10	-3,555.54	1.45	4.36	2,985.69
15	92,949.90	37	27	10	72.97	4,246.02	-2,169.27	1.96	5.28	2,512.16
10	71,424.42	39	30	9	76.92	3,341.47	-3,202.19	1.04	3.48	1,831.40
9	71,150.64	39	28	11	71.79	3,481.40	-2,393.52	1.45	3.70	1,824.38
8	59,700.36	39	29	10	74.36	2,916.50	-2,487.81	1.17	3.40	1,530.78
7	54,559.48	39	28	11	71.79	2,891.16	-2,399.37	1.20	3.07	1,398.96
6	47,615.27	40	30	10	75.00	2,408.70	-2,464.58	0.98	2.93	1,190.38
5	41,881.89	41	29	12	70.73	2,156.61	-1,721.65	1.25	3.03	1,021.51
4	33,006.29	43	26	17	60.47	2,019.98	-1,147.83	1.76	2.69	767.59
3	27,801.06	44	28	16	63.64	1,729.99	-1,289.92	1.34	2.35	631.84
2	15,797.54	50	31	19	62.00	1,219.09	-1,157.60	1.05	1.72	315.95
1	11,269.24	54	32	20	59.26	773.69	-674.45	1.15	1.84	208.69

93% of instances close above their entry price at some point in the next week.

Here we see results appear even stronger. Now let's examine times like the present where the strong breadth days did not come with a new short-term intraday high

NYSE Up Issues % > 75% in 2 of last 3 days. High < highest high of last 10 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: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
20	-18,545.54	12	5	7	41.67	1,947.28	-4,040.28	0.48	0.34	-1,545.46
15	-27,313.84	13	5	8	38.46	2,531.77	-4,996.59	0.51	0.32	-2,101.06
10	-23,741.26	13	4	9	30.77	2,422.57	-3,714.61	0.65	0.29	-1,826.25
9	-26,236.28	13	5	8	38.46	2,486.39	-4,833.53	0.51	0.32	-2,018.18
8	-21,283.96	13	5	8	38.46	2,115.94	-3,982.96	0.53	0.33	-1,637.23
7	-16,235.92	14	5	9	35.71	2,985.66	-3,462.69	0.86	0.48	-1,159.71
6	-13,569.11	14	4	10	28.57	2,512.47	-2,361.90	1.06	0.43	-969.22
5	-11,779.42	14	6	8	42.86	1,792.57	-2,816.86	0.64	0.48	-841.39
4	2,060.32	14	9	5	64.29	1,397.49	-2,103.42	0.66	1.20	147.17
3	3,595.33	14	8	6	57.14	2,294.75	-2,460.44	0.93	1.24	256.81
2	-1,802.94	14	8	6	57.14	1,463.82	-2,252.25	0.65	0.87	-128.78
1	10,016.87	15	9	6	60.00	1,411.72	-448.10	3.15	4.73	667.79

The first few days are basically a tossup but after you get out 1-2 weeks the stats appear quite bearish.

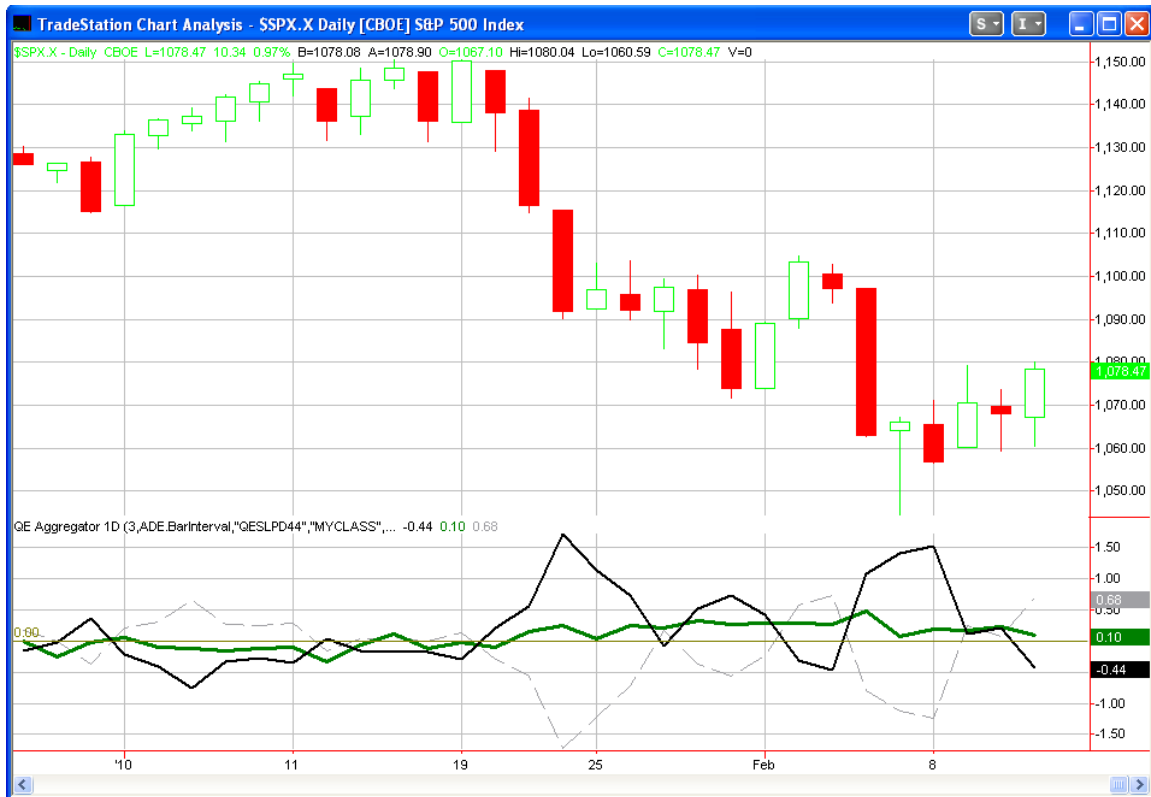
Lastly tonight I should note that the Friday before President's has appeared to be seasonally weak in the past. Below is a list of all Fridays prior to Presidents Day since 1992:

Performance from Thursday's close to Friday's close just before President's Day. \$100k/trade. 1992 - present.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
02/13/92	Buy	\$413.68	(0.29%)	\$38.56
02/14/92	Sell	\$412.47		(\$600.09)
02/11/93	Buy	\$447.65	(0.69%)	\$8.92
02/12/93	Sell	\$444.58		(\$684.61)
02/17/94	Buy	\$470.34	(0.56%)	\$159.00
02/18/94	Sell	\$467.69		(\$905.24)
02/16/95	Buy	\$485.22	(0.67%)	\$0.00
02/17/95	Sell	\$481.97		(\$669.50)
02/15/96	Buy	\$651.34	(0.52%)	\$12.24
02/16/96	Sell	\$647.98		(\$665.55)
02/13/97	Buy	\$811.83	(0.42%)	\$45.51
02/14/97	Sell	\$808.45		(\$452.64)
02/12/98	Buy	\$1,024.14	(0.40%)	\$0.00
02/13/98	Sell	\$1,020.08		(\$623.71)
02/11/99	Buy	\$1,254.03	(1.91%)	\$0.79
02/12/99	Sell	\$1,230.13		(\$2,251.50)
02/17/00	Buy	\$1,388.25	(3.04%)	\$0.00
02/18/00	Sell	\$1,346.09		(\$3,090.96)
02/15/01	Buy	\$1,326.61	(1.90%)	\$0.00
02/16/01	Sell	\$1,301.47		(\$2,507.25)
02/14/02	Buy	\$1,116.48	(1.10%)	\$54.29
02/15/02	Sell	\$1,104.18		(\$1,179.25)
02/13/03	Buy	\$817.37	2.14%	\$2,137.44
02/14/03	Sell	\$834.89		(\$285.48)
02/12/04	Buy	\$1,152.11	(0.55%)	\$410.22
02/13/04	Sell	\$1,145.81		(\$763.68)
02/17/05	Buy	\$1,200.75	0.07%	\$180.11
02/18/05	Sell	\$1,201.58		(\$282.20)
02/16/06	Buy	\$1,289.38	(0.17%)	\$6.93
02/17/06	Sell	\$1,287.24		(\$408.87)
02/15/07	Buy	\$1,456.81	(0.09%)	\$0.00
02/16/07	Sell	\$1,455.54		(\$356.32)
02/14/08	Buy	\$1,348.86	0.08%	\$84.36
02/15/08	Sell	\$1,349.98		(\$794.02)
02/12/09	Buy	\$835.19	(1.00%)	\$504.56
02/13/09	Sell	\$826.84		(\$1,187.62)

The average trade lost 0.6%.

With all this in mind I have updated the [Aggregator](#) chart below.



Tonight's studies have left the green Aggregator line above zero for now as the net expectation from the Active Studies calls for more upside over the next few days. Thursday's strong move higher caused a fairly steep drop in the black Differential line, which is now below 0. In other words, while the studies suggest we may get more upside, the SPX is already overbought versus expectations over the last few days. When this happens and the lines are on opposite sides of 0, it is considered a neutral configuration. This caused the Aggregator System to turn flat tonight.

Looking ahead to tomorrow the green Aggregator line is currently set up to remain positive. A very mild positive reading is anticipated at this point, so any new bearish studies may be able to shift the expectations negative. The pivot level for the Differential is 1,074.96. In other words, a close below this number in the SPX would cause the black Differential line to rise back above 0.

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

Two useful breadth statistics that are tracked by Worden Bros. are the % of Stocks Trading Above the 200ma (T2107) and the % of Stocks Trading Above the 40ma (T2108). At the current time the difference between these two readings is very large. 72% of stocks remain above their 200ma, but only 24% stocks are above their 40ma. The only other time since 1986 when Worden Bros. began tracking these statistics that the difference has been this large was late October / early November of 2009. To get such a large difference between the readings you would need to have a strong pullback occur in a strong uptrend. I was curious to see whether such a strong pullback was likely to derail

the long-term uptrend and lead to further selling. To get a better sense I lowered the required difference between the 2 to 40. Below are those results.

Worden Bros T2107 (% stocks > 200ma) minus T2108 (% stocks > 40ma) crosses over 40. Buy SPX on close. Sell X days later. \$100k/trade. 1986 - 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	
35	21,475.58	4	4	0	100.00	5,368.90	0.00	100.00	100.00	
30	23,219.60	4	4	0	100.00	5,804.90	0.00	100.00	100.00	
25	21,741.08	4	4	0	100.00	5,435.27	0.00	100.00	100.00	
20	20,572.12	5	5	0	100.00	4,114.42	0.00	100.00	100.00	
15	19,107.91	5	5	0	100.00	3,821.58	0.00	100.00	100.00	

The 5 dates shown for the 20-days out test are:
10/27/97, 3/11/04, 3/2/07, 10/27/09, and 11/27/09.

In general returns were positive from day 1. From a long-term perspective, such sharp pullbacks have been followed by additional buying. Any uptrend strong enough that such a large number of stocks were trading above their 200ma that the difference could be as large as 40 simply didn't fall apart when a strong selloff occurred. The 2004 instance saw a retest of the highs before the market underwent a lengthy but shallow selloff. The other instances all rallied through their old highs and kept rising. Instances are definitely low but results couldn't be any more bullish.

While we are now way above a difference of 35, I also ran that to get a few more instances.

Worden Bros T2107 (% stocks > 200ma) minus T2108 (% stocks > 40ma) crosses over 35. Buy SPX on close. Sell X days later. \$100k/trade. 1986 - 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
35	23,068.19	10	9	1	90.00	5,402.87	-25,557.66	0.21	1.90	2,306.82
30	22,283.78	10	9	1	90.00	5,187.10	-24,400.14	0.21	1.91	2,228.38
25	33,480.55	10	8	2	80.00	4,272.10	-348.13	12.27	49.09	3,348.06
20	24,726.47	10	9	1	90.00	2,876.02	-1,157.70	2.48	22.36	2,472.65
15	35,452.69	12	11	1	91.67	3,320.18	-1,069.30	3.11	34.16	2,954.39

This seems to confirm the previous findings and suggests the current breadth differential is indicative of not a market about to fall apart, but rather a market that is likely to resume its uptrend.

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.

None tonight.

Active Trades Table

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	2/5/2010	\$106.56	\$108.13	1.47%		sold on close
SPY(1/4)	2/5/2010	\$106.44	\$108.13	1.59%		sold on close
VXX(s)	2/8/2010	\$33.31	\$31.40	5.73%		cover 1/2 on close < \$31.40

It took some time but the SPY trade finally closed out nicely positive.

I'll look to take partial profits on the VXX position if it can close lower tomorrow. I may let the 2nd half run a bit depending on how action unfolds over the next few days.

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