

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 19, 2010

Volume 3 Issue 53

## Market Overview



## Tonight's Research Points

- A weak pullback from a strongly overbought condition as measured by RSI(2) is often followed by a quick move back higher.
- The Aggregator System remained flat at the close.
- The NDX Aggressive Trend Timer remained flat at the close.

## Short-term Outlook – updated 3/19

### The Bottom Line

We're continuing to see evidence of more upside in the short-term. Unfortunately the market still remains too overbought to consider entry. With a low number of active studies things could change rapidly in the next few days here. For now I don't see a substantial edge so I will wait until I do.

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
<b>Active</b>					
March 19, 2010	SPX down. RSI(2) > 90. Close > 200ma	1-2 days	Bullish	1.10%	0.80%
March 17, 2010	100-day closing high on a Fed Day	1-8 days	Bullish	2.00%	1.70%
March 16, 2010	SPY 10 high Vol 5 low, Lower hi & low	1-4 days	Bearish	-1.80%	-1.30%
<b>Active - Long Term</b>					
March 10, 2010	Ttl Put/Call 40-low. SPX no 0.5% up.	1-5 weeks	Bearish	-4.90%	-3.30%
February 22, 2010	VIX:VXV Ratio falls below 0.9	int. term	Bearish		
February 16, 2010	Nasdaq/S&P RS Indicator Positive	int. term	Bullish		
<b>Dropped Tonight</b>					
March 16, 2010	Up Vol & Up Issue % < 45% SPX Up > 200	1-3 days	Bearish	-1.70%	-1.40%

If the avg max move – 1/3 Std Dev is achieved the study will appear in **bold italic blue** and no longer be active.

### The Evidence

After 14 days higher in a row, SPY finally “suffered” a down day – sort of. It lost 6 cents while trading in a tight 70 cent range for the day. With very little action the indices finished mixed. The SPX was down 0.03% while the Nasdaq rose 0.09% and the Russell 2000 was up 0.04%. Though the indices were mixed, breadth was fairly negative. The NYSE Up Issues % came in at 42% and the Up Volume % was 35%. Total volume dropped to the lowest level in a little over a week.

I’ve shown many times before how strong selloffs rarely end when the 1<sup>st</sup> day of the bounce is meek. Most of the time to get a strong multi-day move off a low, you need a convincing day-1 bounce. Tonight I decided to flip this concept on its head a little bit and examine what happens after a small pullback day during a strong upmove. For this study I used the 2-day RSI. The 2-day RSI is a very sensitive indicator so it would take a very small decline from a very overbought position in order for it to remain above 90 on a down day. This is what happened on Thursday and what I examined below.

SPX closes down but RSI(2) > 90. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - 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	
3	9,911.68	14	9	5	64.29	1,250.69	-268.91	4.65	8.37	707.98	
2	9,120.13	14	11	3	78.57	916.60	-320.83	2.86	10.48	651.44	
1	5,381.82	14	12	2	85.71	510.07	-369.48	1.38	8.28	384.42	

There appears to be a fairly strong upside tendency over the last 13 years based on these results. The edge pretty much plays itself out within the first two days though. Looking further out in time did not showing significant results. What I find most appealing about this study is not the high winning % or the strong average trade results, but rather the risk/reward. To get a better feel for potential upside versus potential downside I have listed all the instances in the table below. Be sure to read the note at the bottom of the graphic.

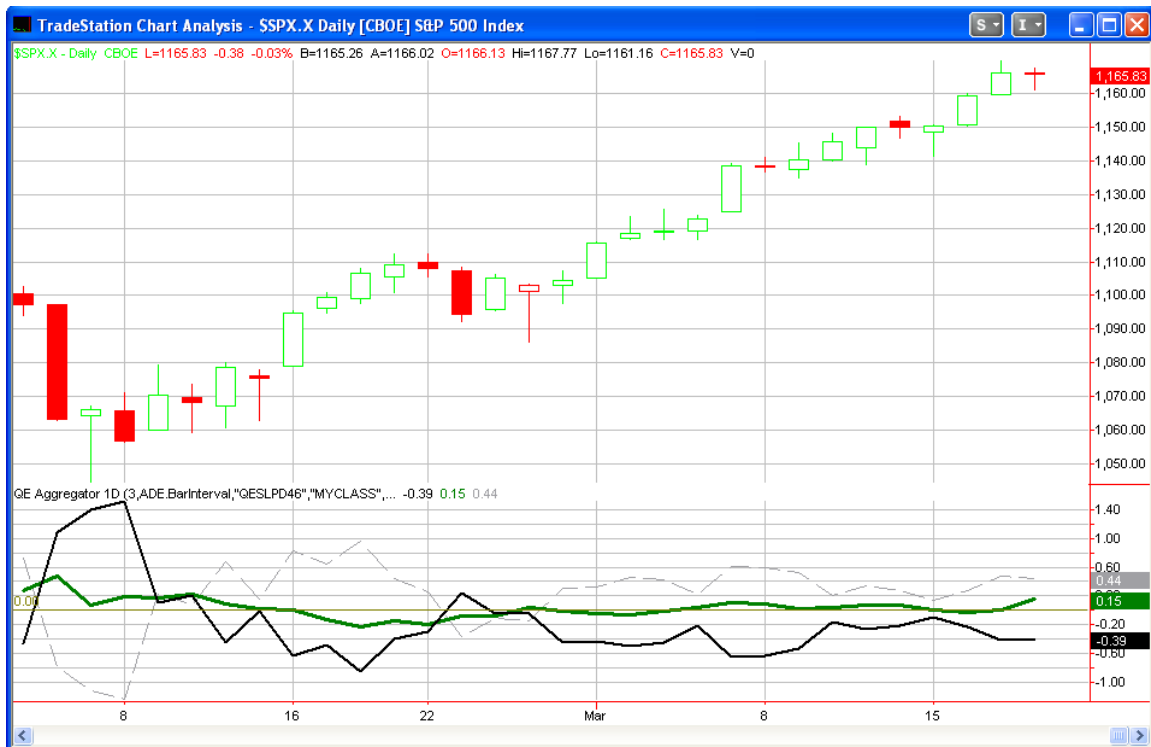
SPX closes down but RSI(2) close > 90. Close > 200ma.  
Buy on close. Sell 2 days later. \$100k/trade. 1997 - present.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
12/31/97	Buy	\$970.43	0.69%	\$1,256.60
01/05/98	Sell	\$977.08		(\$484.10)
11/03/98	Buy	\$1,110.85	2.06%	\$2,072.70
11/05/98	Sell	\$1,133.68		(\$117.90)
12/27/99	Buy	\$1,457.09	0.44%	\$705.84
12/29/99	Sell	\$1,463.46		(\$293.08)
05/28/04	Buy	\$1,120.63	0.39%	\$664.83
06/02/04	Sell	\$1,124.99		(\$650.59)
11/15/04	Buy	\$1,183.82	(0.16%)	\$389.76
11/17/04	Sell	\$1,181.94		(\$714.00)
01/10/06	Buy	\$1,289.69	(0.28%)	\$401.17
01/12/06	Sell	\$1,286.06		(\$358.05)
08/30/06	Buy	\$1,304.27	0.52%	\$589.76
09/01/06	Sell	\$1,311.01		(\$138.32)
03/22/07	Buy	\$1,434.54	0.21%	\$300.15
03/26/07	Sell	\$1,437.50		(\$776.94)
07/17/09	Buy	\$940.38	1.51%	\$1,711.90
07/21/09	Sell	\$954.58		\$0.00
07/22/09	Buy	\$954.07	2.64%	\$2,674.88
07/24/09	Sell	\$979.26		(\$83.20)
08/24/09	Buy	\$1,025.57	0.25%	\$1,181.46
08/26/09	Sell	\$1,028.12		(\$388.00)
11/10/09	Buy	\$1,093.01	(0.53%)	\$1,124.76
11/12/09	Sell	\$1,087.24		(\$738.01)
03/08/10	Buy	\$1,138.50	0.62%	\$849.12
03/10/10	Sell	\$1,145.61		(\$313.20)
03/12/10	Buy	\$1,149.99	0.82%	\$884.94
03/16/10	Sell	\$1,159.46		(\$734.44)
03/18/10	Buy	\$1,165.83	n/a	\$0.00
open	n/a	\$1,165.83		\$0.00

Deepest pullback →

Average max upside was 1.05%. Zero instances dropped that much. The *max* downside over the following 2 days was less than 0.8%.

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



Tonight's bullish study has helped to push the green Aggregator line further above 0. This illustrates the net positive expectation from the active studies for the next few days. Meanwhile the black Differential line remains squarely below zero. This shows the SPX has strongly beaten expectations over the last few days. As has been the case an awful lot lately the Aggregator chart is showing the market is overbought with expectations for more upside. As I'm sure most of you are aware this is considered a neutral configuration. Once again tonight the Aggregator System is flat.

Looking ahead the Aggregator value is set to remain positive tomorrow. Meanwhile the Differential pivot level will be 1,160.04. So a close at or below this level would move the Differential value back above the zero line. It would likely also lead to a long trigger for the Aggregator System.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 3/15 – somewhat bullish***

From an intermediate-term standpoint this past week was marked more by intermediate-term bullish studies achieving their objectives than by a large number of new intermediate-term studies emerging. The Fed-day studies were taken off the Active list earlier this week as the market approached new highs. And now with a new intraday high being achieved on Friday, I've removed a few other intermediate-term studies that have suggested we should get this far.

There was one bearish intermediate-term study added this week that looked at Tuesday's very low CBOE Equity Put/Call reading. If you missed it you can [see it here](#).

My conviction isn't as strong as it was a few weeks ago when I felt we were destined to reach these new highs. Still, I'm not seeing a compelling amount of evidence suggesting

the market is about to roll over and begin a significant down leg at this point in time either. Until a substantial amount of bearish evidence emerges, I'll side with the trend for my intermediate-term outlook.

### **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.*

*Buy 1/4 index position in SPY on SPX close of 1,160 or lower unless systems page indicates Aggregator long trigger is unlikely. Chances are a close below the Differential pivot Friday would cause an Aggregator long signal to trigger. I'll look to take advantage of it with a small position at the close.*

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