

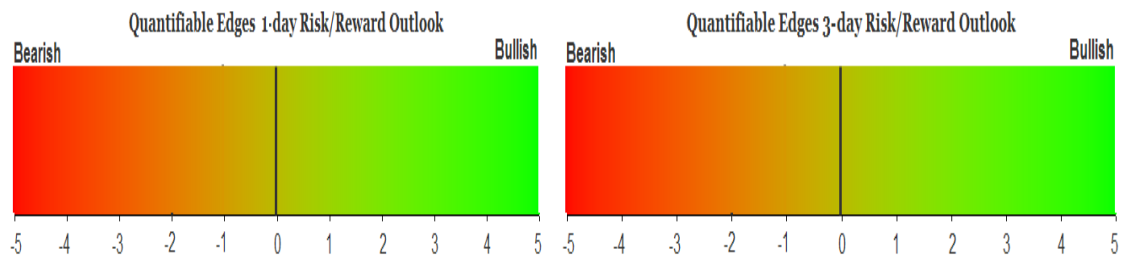
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 26, 2010

Volume 3 Issue 78

Market Overview



Tonight's Research Points

- SPX breaking out to a new 50-day high on lower volume suggests a bullish short-term edge.
- A late surge in the VIX brought up 2 SPX/VIX studies that suggest a short-term pullback.
- The streak of days the NDX has spent above the 10ma is now at an all-time high of 50. The Dow is at 48. They are providing more evidence that the intermediate-term rally has a ways to go.
- The Aggregator System remained flat at the close.
- The NDX Aggressive Trend Timer remained flat at the close.

Short-term Outlook – updated 4/26

The Bottom Line

Evidence is mixed but it currently seems to favor the long-side over the next few days. With the market severely overbought by many short-term measures both the Aggregator and the NDX Trend Timer are sidelined and awaiting a better entry point. Risk seems a bit high at these levels to initiate new longs.

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					
April 26, 2010	Low vol breakout to 50-day high	1-3 days	Bullish	1.30%	1.00%
April 26, 2010	SPX & VIX up 2 days in row / on Fri	1-2 days	Bearish	-1.00%	-0.80%
April 22, 2010	SPX down while NYSE Up Issues > 55%	1-3 days	Bullish	1.20%	0.90%
Active - Long Term					
April 26, 2010	No breadth divergence at new high	int. term	Bullish		
April 19, 2010	1st drop below 10ma in long time	int. term	Bullish		
April 13, 2010	Ttl Put/Call 40-low. SPX no 0.5% up.	1-5 weeks	Bearish	-4.90%	-3.30%
April 6, 2010	SPX and TNX hit 50-day closing highs	int. term	Bearish		
February 16, 2010	Nasdaq/S&P RS Indicator Positive	int. term	Bullish		
Dropped Tonight					
April 19, 2010	Down day after 5 up closes > 200m	1-10 days	Bullish	2.20%	1.65%
April 23, 2010	SPX close up less than 0.25% in top 10%	1 day	Bearish		

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 some mild weakness in the morning the market spent the afternoon again marching higher. The major indices all again finished the day positive. They also all closed at new 52-week highs. The SPX gained 0.7%, the Nasdaq 0.4% and the Russell 2000 tacked on 1.1%. Breadth was solidly positive as the NYSE Up Issues % came in at 71% and the Up Volume % at 66%. In other breadth news the NYSE Advance/Decline line hit a new high and the number of new 52-week NYSE highs just barely missed. Total NYSE volume declined from the last couple of days.

This was the 1st new high the SPX has made in over a week after pulling back strongly last Friday. The lower NYSE volume may sound concerning to some technicians, but when you're talking about the major index breakouts low volume is actually favorable. I've discussed this some in the past but I thought I'd show it again tonight in the context of the current market environment.

Below are 2 studies. They look at SPX breakouts to new highs. The only difference between the two is that the 1st one requires a rise in volume and the 2nd one requires a decline in volume.

SPX closes at a 50 day high after not doing so for at least 5 days. NYSE volume is higher than yesterday. Buy SPX on close. Sell X days later. \$100k/trade. 1996 - 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	-7,058.69	48	21	27	43.75	2,021.48	-1,833.70	1.10	0.86	-147.06
9	-8,318.15	48	21	27	43.75	2,016.80	-1,876.70	1.07	0.84	-173.29
8	-8,877.22	50	25	25	50.00	1,763.11	-2,118.20	0.83	0.83	-177.54
7	2,228.32	50	24	26	48.00	1,987.12	-1,748.56	1.14	1.05	44.57
6	2,257.98	50	28	22	56.00	1,441.97	-1,732.60	0.83	1.06	45.16
5	5,091.55	50	26	24	52.00	1,467.67	-1,377.83	1.07	1.15	101.83
4	-199.82	50	29	21	58.00	1,107.48	-1,538.89	0.72	0.99	-4.00
3	-700.37	50	28	22	56.00	1,018.02	-1,327.49	0.77	0.98	-14.01
2	-6,652.29	50	23	27	46.00	737.23	-874.39	0.84	0.72	-133.05
1	473.70	50	25	25	50.00	452.47	-433.52	1.04	1.04	9.47

What we see here is that there is no edge apparent when the breakout is accompanied by an increase in volume. Now let's look at the study with decreasing volume.

SPX closes at a 50 day high after not doing so for at least 5 days. NYSE volume is lower than yesterday. Buy SPX on close. Sell X days later. \$100k/trade. 1996 - 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	28,199.08	42	27	15	64.29	1,916.53	-1,569.81	1.22	2.20	671.41
9	34,084.94	42	31	11	73.81	1,748.24	-1,828.24	0.96	2.69	811.55
8	30,957.59	42	29	13	69.05	1,735.38	-1,489.88	1.16	2.60	737.09
7	22,937.07	42	26	16	61.90	1,528.42	-1,050.12	1.46	2.37	546.12
6	27,563.70	43	27	16	62.79	1,530.58	-860.13	1.78	3.00	641.02
5	33,816.86	43	28	15	65.12	1,645.95	-817.98	2.01	3.76	786.44
4	26,258.98	43	31	12	72.09	1,201.59	-915.87	1.31	3.39	610.67
3	29,800.15	43	32	11	74.42	1,183.93	-735.04	1.61	4.69	693.03
2	15,183.73	43	31	12	72.09	794.56	-787.31	1.01	2.61	353.11
1	7,869.62	43	31	12	72.09	435.09	-468.17	0.93	2.40	183.01

39 of 43 instances (91%) closed above the entry price at some point in the next 3 days.

These stats are substantially better and suggest a decent upside edge over the next few days.

The requirement that the market has not closed at a new high for 5 days was included to show that this is a fresh breakout and not a market that is already extended upwards and has been making new highs for multiple days. To see the effect of this filter I ran a few tests that demanded different periods without new highs. This first one looks at a 1-day holding period.

SPX closes at a 50 day high after not doing so for at least X days. NYSE volume is lower than yesterday. Buy SPX on close. Sell 1 day later. \$100k/trade. 1996 - 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	4,462.22	25	17	8	68.00	408.31	-309.88	1.32	2.80	178.49
9	4,462.22	25	17	8	68.00	408.31	-309.88	1.32	2.80	178.49
8	4,542.32	26	18	8	69.23	390.08	-309.88	1.26	2.83	174.70
7	8,739.10	32	24	8	75.00	467.42	-309.88	1.51	4.53	273.10
6	10,042.36	35	27	8	77.14	463.76	-309.88	1.50	5.05	286.92
5	7,869.62	43	31	12	72.09	435.09	-468.17	0.93	2.40	183.01
4	8,031.08	49	34	15	69.39	411.37	-397.03	1.04	2.35	163.90
3	9,130.23	55	37	18	67.27	470.77	-460.46	1.02	2.10	166.00
2	4,647.93	64	41	23	64.06	460.58	-618.95	0.74	1.33	72.62
1	2,272.09	91	53	38	58.24	488.97	-622.20	0.79	1.10	24.97
0	-892.09	211	94	85	44.55	449.30	-507.37	0.89	0.98	-4.23

Here you see that fresh breakouts tend to do better than extended conditions. The “0 days” row shows a slight negative expectation. Stats once you get out about 5 days look pretty strong and remain so as you go farther out.

I also ran this same test with a 3-day holding period.

SPX closes at a 50 day high after not doing so for at least X days. NYSE volume is lower than yesterday. Buy SPX on close. Sell 3 days later. \$100k/trade. 1996 - 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	21,765.77	25	20	5	80.00	1,316.36	-912.28	1.44	5.77	870.63
9	21,765.77	25	20	5	80.00	1,316.36	-912.28	1.44	5.77	870.63
8	22,458.19	26	21	5	80.77	1,286.65	-912.28	1.41	5.92	863.78
7	29,882.00	32	26	6	81.25	1,356.74	-898.88	1.51	6.54	933.81
6	29,408.80	35	27	8	77.14	1,320.02	-778.98	1.69	5.72	840.25
5	29,800.15	43	32	11	74.42	1,183.93	-735.04	1.61	4.69	693.03
4	32,231.06	49	37	12	75.51	1,113.18	-746.39	1.49	4.60	657.78
3	28,574.85	55	40	15	72.73	1,110.07	-1,055.19	1.05	2.81	519.54
2	26,126.14	64	42	22	65.63	1,155.50	-1,018.40	1.13	2.17	408.22
1	23,427.05	88	53	35	60.23	1,166.42	-1,096.95	1.06	1.61	266.22
0	17,065.60	150	82	68	54.67	1,057.00	-1,023.66	1.03	1.25	113.77

Results here suggest a similar conclusion. You are better off buying breakouts that haven't made a new high for at least a week or so than you are buying any new high. Anything beyond a week shows fairly consistent results.

So the good news is that we had a new, low-volume breakout to SPX highs which we hadn't seen for at least a week. Not all the news was good, though.

One indicator that flashed a warning was the VIX which rallied hard in the last few minutes of the day to finish positive. Below is a excerpt from the 3/11/10 Subscriber Letter which is fitting for the current action as well. **Note: the study contains updated stats.**

Most often the VIX and SPX move in opposite directions, but today marked the 2nd day in a row where they both closed higher. Since 1998 such setups have carried a bearish edge. And although there were just a small number of instances that occurred with the SPX below its 200ma, I felt it important to separate them since results have been so extreme below the 200ma. First let's look at other times like the present where the SPX is trading above its 200ma.

SPX and VIX both close up today and yesterday. SPX > 200ma. Buy SPX 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	1,015.33	15	10	5	66.67	1,155.38	-2,107.68	0.55	1.10	67.69
4	-4,301.80	15	8	7	53.33	954.83	-1,705.78	0.56	0.64	-286.79
3	-4,770.52	15	7	8	46.67	735.07	-1,239.50	0.59	0.52	-318.03
2	-3,887.37	15	5	10	33.33	626.71	-702.09	0.89	0.45	-259.16
1	-3,141.40	18	7	11	38.89	246.65	-442.54	0.56	0.35	-174.52

The only instance that didn't post a close lower than the entry price at some point in the next 3 days was 3/10/10.

While the average trade stats aren't huge, the tendency to sell off soon after is 100% accurate. Now let's peek at those times in which the setup occurred with the SPX below its 200ma.

SPX and VIX both close higher 2 days in a row. SPX closes < 200ma. Buy SPX 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	-16,342.21	4	0	4	0.00	0.00	-4,085.55	0.00	0.00	-4,085.55
4	-19,238.00	4	0	4	0.00	0.00	-4,809.50	0.00	0.00	-4,809.50
3	-17,313.63	4	0	4	0.00	0.00	-4,328.41	0.00	0.00	-4,328.41
2	-15,014.48	4	0	4	0.00	0.00	-3,753.62	0.00	0.00	-3,753.62
1	-5,986.26	4	1	3	25.00	912.33	-2,299.53	0.40	0.13	-1,496.57

While it's too few instances for statistical significance, inclusion of the above results into the original test dramatically alters the results. By segregating the results I believe you are seeing a more realistic expectation.

Also unusual about the VIX rising along with the SPX is that it occurred on a Friday. Fridays often see the VIX decline in the afternoon. It then pops a bit on Monday to get back on track. The study below therefore looks at occurrences of the SPX and VIX both closing up on Fridays.

SPX up VIX up on Friday. 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	-15,777.21	38	17	21	44.74	1,646.30	-2,084.02	0.79	0.64	-415.19
4	-23,031.29	38	15	23	39.47	1,621.09	-2,058.59	0.79	0.51	-606.09
3	-19,197.62	38	14	24	36.84	1,419.11	-1,627.71	0.87	0.51	-505.20
2	-21,078.53	38	11	27	28.95	1,254.38	-1,291.73	0.97	0.40	-554.70
1	-30,094.52	38	10	28	26.32	579.14	-1,281.64	0.45	0.16	-791.96

Like the previous study I also found this one was worth segregating into uptrend and downtrend to help get a better estimate for expectations. First let's look at instances below the 200ma.

SPX up VIX up on Friday. SPX close < 200ma. 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	-13,781.90	10	5	5	50.00	1,331.04	-4,087.42	0.33	0.33	-1,378.19
4	-16,772.90	10	3	7	30.00	2,709.58	-3,557.38	0.76	0.33	-1,677.29
3	-12,493.02	10	4	6	40.00	2,035.88	-3,439.43	0.59	0.39	-1,249.30
2	-11,520.91	10	3	7	30.00	1,660.25	-2,357.38	0.70	0.30	-1,152.09
1	-21,670.80	10	4	6	40.00	609.89	-4,018.39	0.15	0.10	-2,167.08

You can see here that some very big losses are skewing the results of the 1st study quite a bit. So lastly let's look at times like now where the SPX is above its 200ma.

SPX up VIX up on Friday. SPX close > 200ma. 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	-1,995.31	28	12	16	42.86	1,777.67	-1,457.96	1.22	0.91	-71.26
4	-6,258.39	28	12	16	42.86	1,348.97	-1,402.87	0.96	0.72	-223.51
3	-6,704.60	28	10	18	35.71	1,172.40	-1,023.81	1.15	0.64	-239.45
2	-9,557.62	28	8	20	28.57	1,102.18	-918.75	1.20	0.48	-341.34
1	-8,423.72	28	6	22	21.43	558.65	-535.25	1.04	0.28	-300.85

25 of 28 instances (89%) close below the entry price at some point in the next 2 days.

The average trade isn't as strong but you can see that the downside consistency is actually quite good. A decline has typically been seen right off the bat on day 1 or day 2.

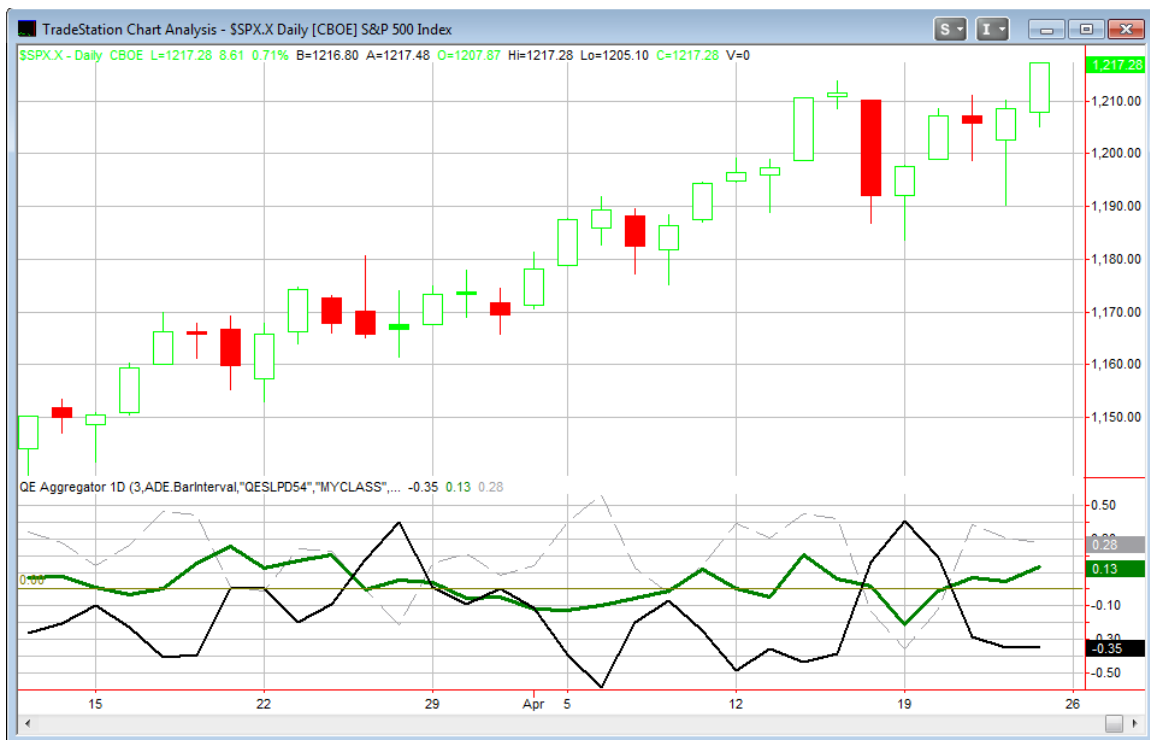
So we're seeing some fairly strong conflicting short-term evidence tonight. The positive studies are bit stronger at this point and you'll see that reflected in the Aggregator.

You'll also note that the "1st Down Day After At Least 5 Up Closes" study from a week ago reached its target level and has been removed from the Active Studies List tonight.

Traders should also note that there is a Fed meeting this week. An announcement is due on Wednesday afternoon. I'll discuss Fed Days a bit more in Tuesday's letter but you may find lots of information on Fed Days in the blog using the link below:

<http://quantifiableedges.blogspot.com/search/label/Fed%20Study>

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



Again the Aggregator is in a position where I don't see a strong trading edge. The green Aggregator line is squarely above zero as the net expectation from the active studies is for upside over the next few days. The "problem" though is the black Differential line. It is well below 0, which illustrates the SPX has easily beaten expectations over the last few days. We have positive expectations but are already overbought. This is considered a neutral configuration. The Aggregator System remains flat tonight as it has the last several days.

Looking ahead the expectations are scheduled to remain positive over the next couple of days. Of course additional bearish studies could quickly change this. Meanwhile the pivot value for the black Differential line is 1,203.87 for Monday. This means it would take a close of 1,203.87 or lower in order to flip the Differential value into positive territory. Without closing this low, the Aggregator System will not trigger a long on Monday.

This move upwards over the last couple of months has been highly unusual with regards to its persistence and somewhat frustrating from a trading standpoint. The Aggregator System only looks to go long if 1) expectations are positive and 2) the market has underperformed expectations over the last few days. We have had positive expectations based on the studies for much of the period. Unfortunately the market has hardly pulled back at all in order to allow for long entries. The pullback criteria really doesn't even require a pullback. The SPX doesn't need to drop a certain amount. It just needs to underperform expectations. The market has consistently outperformed expectations. I'll discuss just how historically abnormal the current rally is in the intermediate-term section below.

While the Aggregator has been a bit frustrating recently, the NDX Aggressive Trend Timer System has been able to participate in some of the upside and post decent gains. My original inspiration for the system came last July when the Aggregator also struggled during a runaway upmarket. The system is flat now as it "turns off" when the market gets extremely short-term overheated. Really the "best" system lately has been "Buy & Hold". Of course the chances of that remaining the best system in my eyes are about 0%.

Intermediate-term Outlook (2 weeks – 2 months)– updated 4/26 somewhat bullish

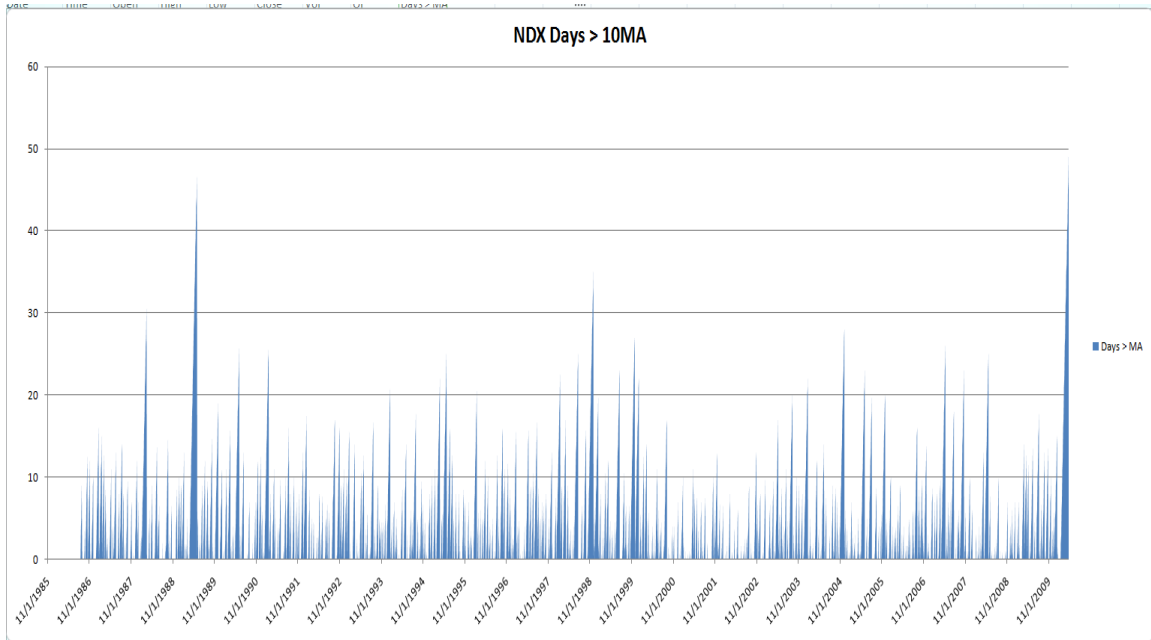
A few times recently I discussed the incredible string of days the SPX went without closing below its 200ma. Today I will show the NDX and the Dow streaks. First I'll review my comments from last week.

Another notable about Friday's selloff that demonstrates how persistent the uptrend has been is the fact that it caused the SPX to close below the 10ma for the 1st time since February 12th. That streak consisted of 42 trading days above the 10ma before Friday. In the 3/22/10 Letter I discussed the fact that the SPY had gone more than 25 days above its 10ma. (The SPY streak was broken on 3/26 after going 30 days.) In that Letter I showed the 5 other times since 1993 that SPY had gone at least 25 days above the 10ma. My conclusion after viewing the charts was the following... "Strong and persistent upside movement like we have seen lately hasn't just ended and lead to an immediate correction. The 1st dip has always been just that – a dip. New highs were always made in short order." With this Letter already quite long I decided not to reproduce those charts again. Instead, if you would like to view them you may find them in the intermediate-term section of the 3/22 Letter which I have provided a download link to below:

[*2010-03-22 QE Weekly Research Letter.pdf*](#)

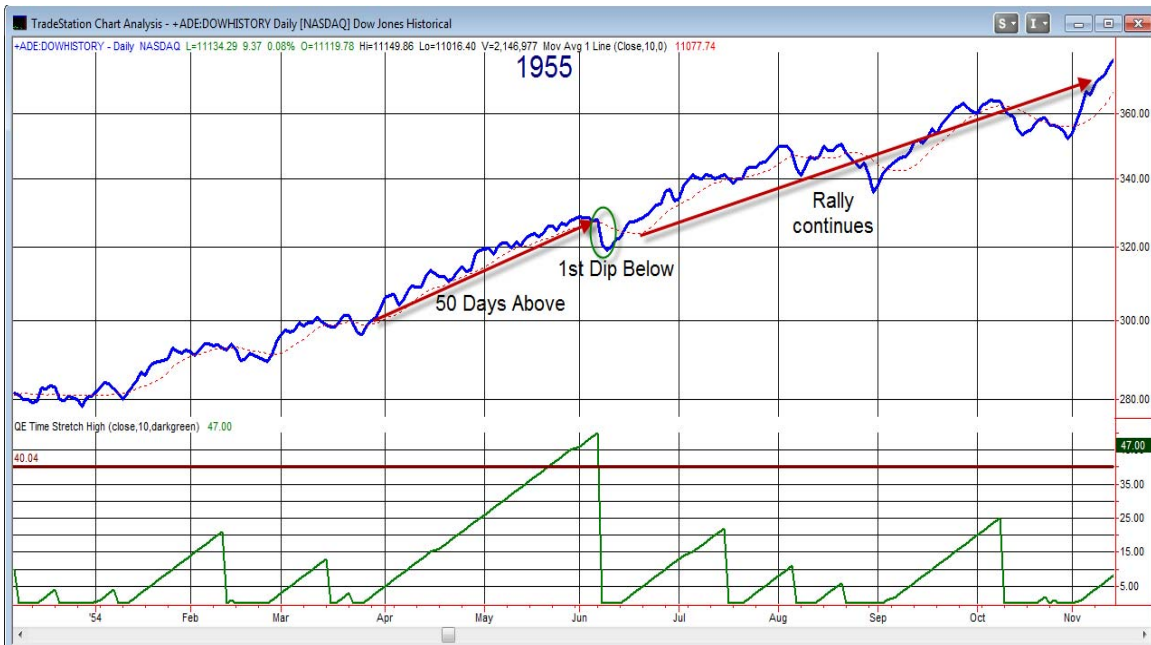
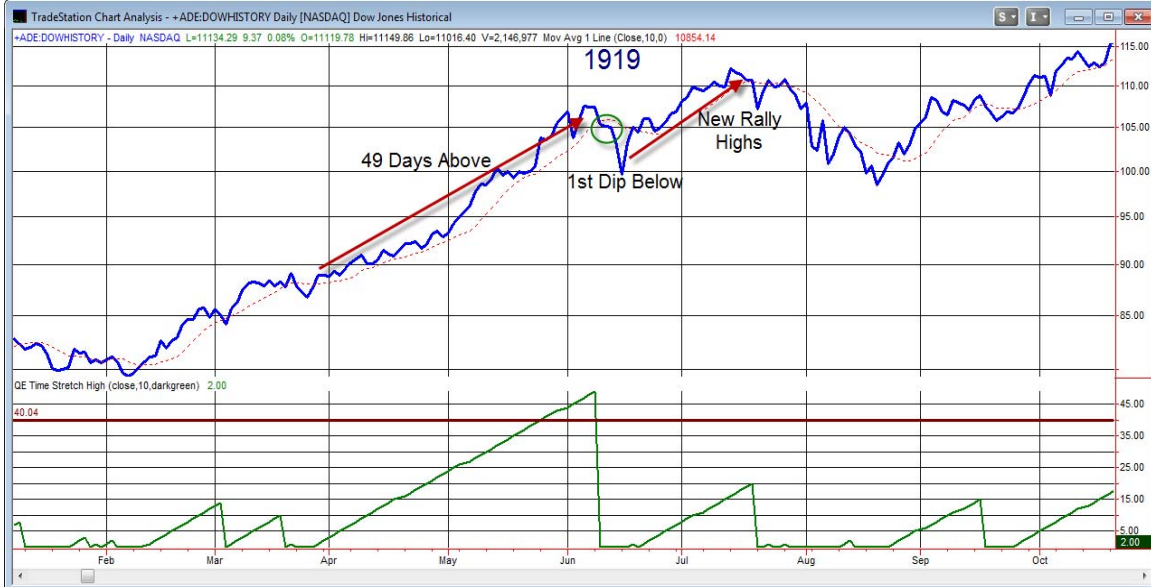
Along these lines this weekend I looked for other times the SPX closed above the 10ma for at least 40 days in a row. Looking back to 1960 there were only 4 other instances – the most recent occurring in 1972. The dates when the other 4 instances finally dipped below the 10ma were Feb 1961, Oct 1968, Feb 1971, and Jan 1972. In looking at those instances I am drawn to the same conclusion as the 3/22 study referenced above. Persistent strength never just ended on that 1st pullback. The market went on to make new highs each time and the rally continued.

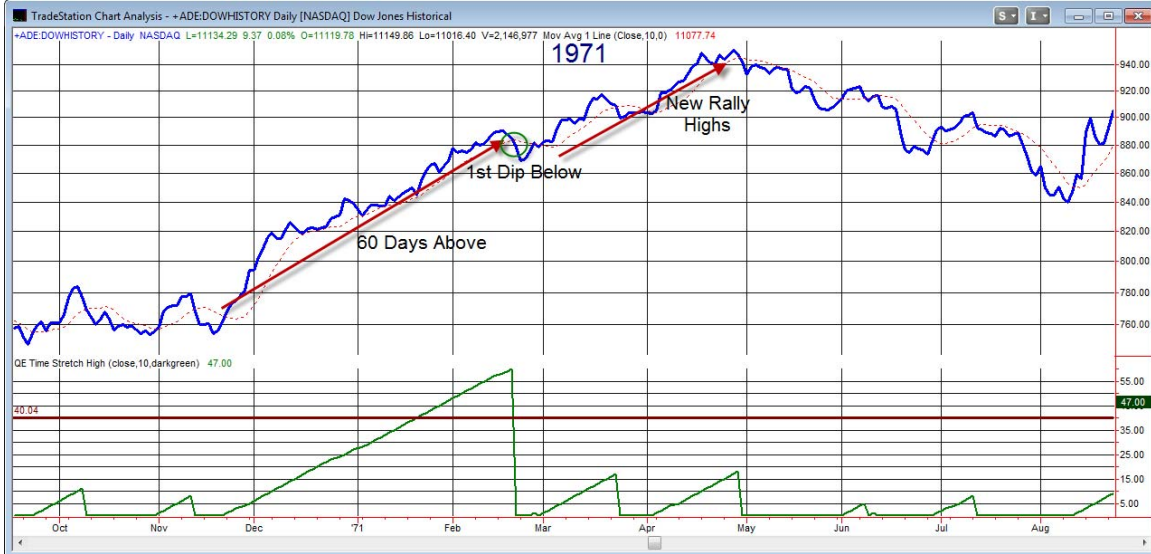
The NDX and the Dow STILL haven't dropped below their 10-day ma's. For the NDX the streak is now 50 days. The DIA is also 50, but the cash Dow is "just" 48 days. For the NDX this is the longest streak since its inception in 1986. Below is a chart that shows the number of days the NDX has spent above it 10ma at any point in time.



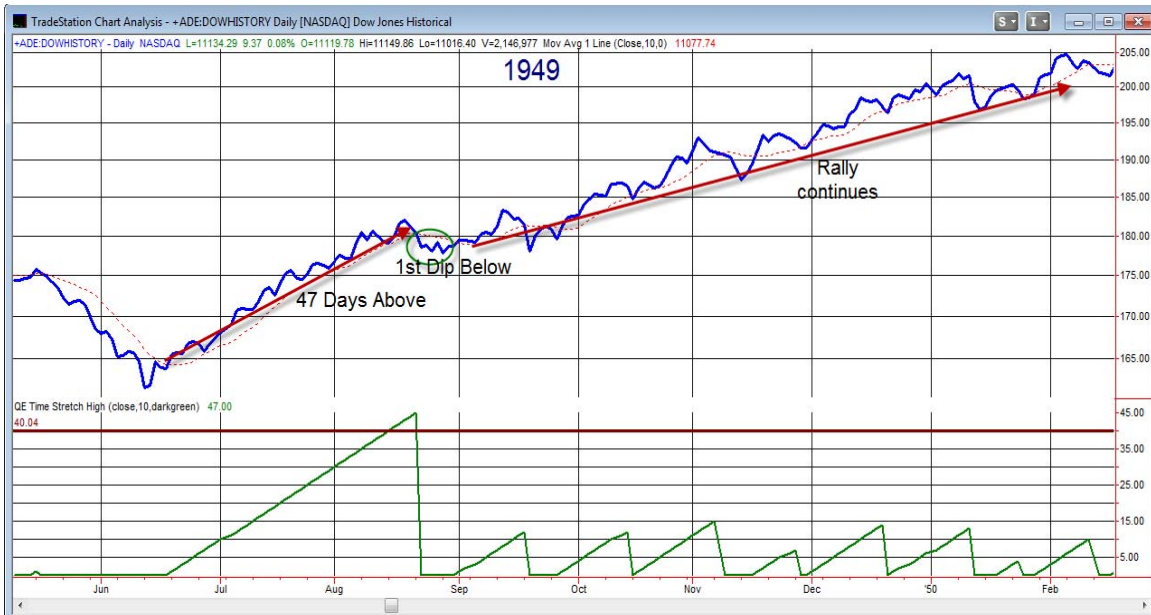
It's a little difficult to read when try to jam so much history into a small area, but the spike on the right is the current count and it is up to 50. The previous high lasted 47 days in 1989.

The Dow streak of 48 days is also remarkable. For the Dow Index I was able to look back to 1915 in search of similar streaks. I produced a graphic like the NDX one above, but as you can imagine with history going back that far it was imperceptible. I therefore produced some charts to show the action around similar streaks. There have only been 3 that have lasted as long as the current one. They were in 1919, 1955, and 1971. Their charts are below. The indicator on the bottom is simply a count of the number of days the Dow spent above the 10ma.



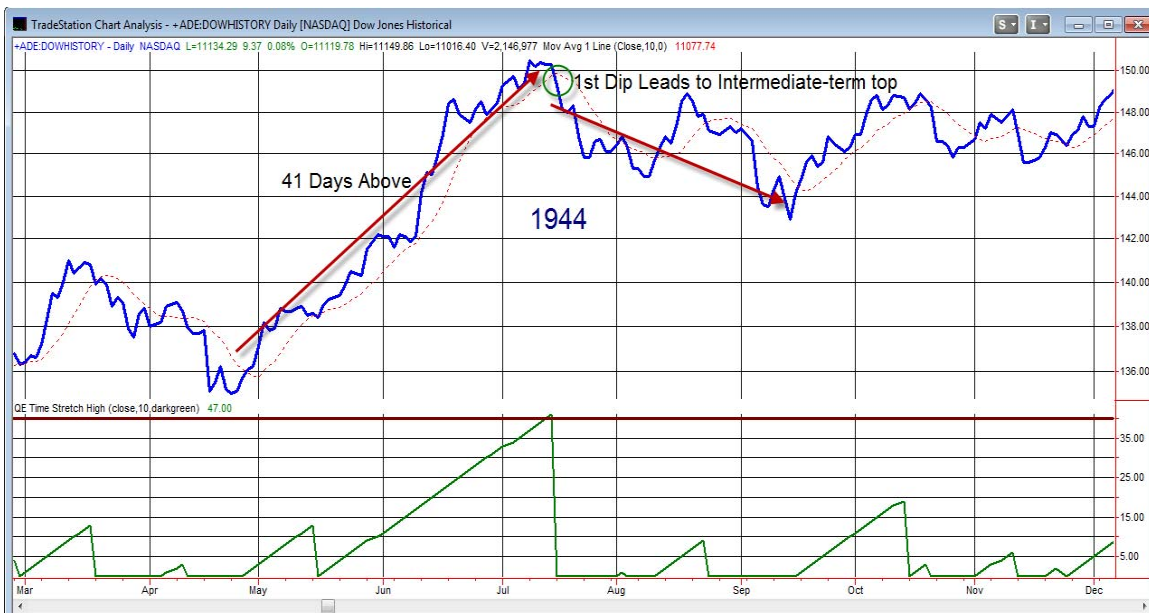


As with the SPX observations we see here that the rally continued in each case after that 1st dip. Rallies this strong and persistent seem unlikely to end on the 1st pullback. In 1949 and 1968 there were rallies that almost reached the current length. I've posted those below.





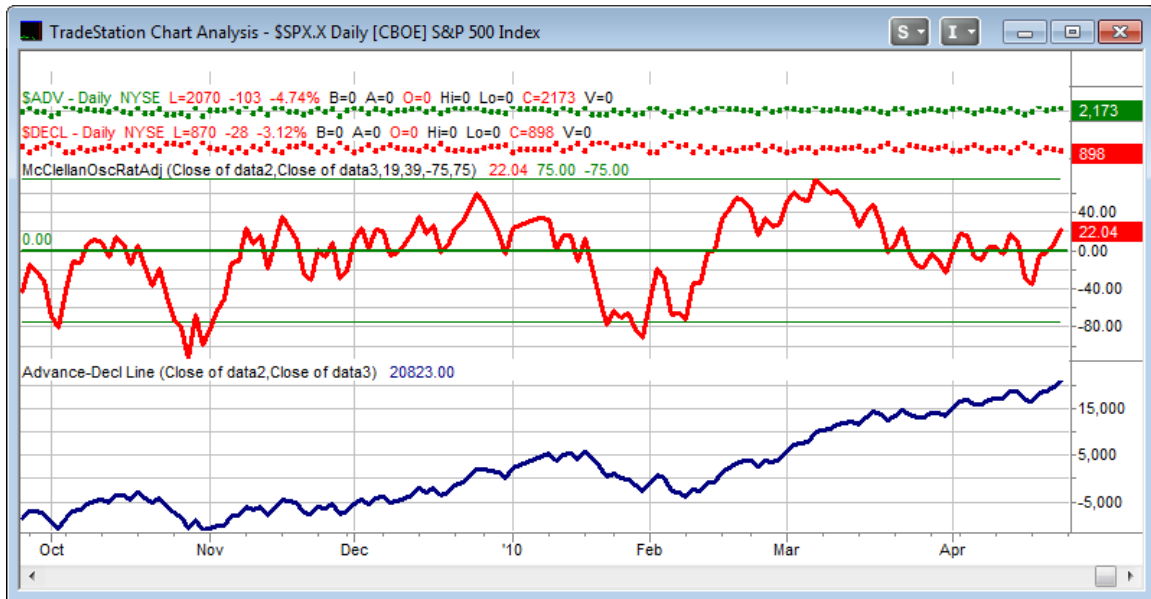
I did look to find the longest streak that ended with the first dip marking an intermediate-term top. 1944 was the winner with a streak of 41 days. That chart is below.



So 1944 could be considered our lone exception as a long streak ended abruptly. Of course it wasn't as long as the current rally or any of those others that went on to further gains.

Another bit of evidence to keep an eye on is the % of 52-week highs on the NYSE. As I've discussed a number of times over the last six months, all SPX tops since 1970 have seen a divergence lasting at least 2 months in either the A/D line or the % of stocks hitting new 52-week highs prior to the ultimate price high. A move higher early this

week has the potential to see the 52-week NH % hit a new high. Below is a chart with the NYSE A/D line shown in blue in the bottom panel.



There are a few intermediate-term studies active with bearish implications. They are related to bond action and option ratios. To this point they haven't made a difference. We will get an intermediate-term decline at some point here but for now evidence appears to favor continued upside. It's been a tough trend to fight and I wouldn't suggest it at this point.

Catapult and Capitulative Breadth Statistics

(Catapult Presentation Part 1) (Catapult Presentation Part 2)

Open Catapult Triggers

MON 1/3 position @ \$64.73 limit (not filled)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 1 (MON)

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. Too overbought for me to want new longs. A pullback early this week could set up a nice long trade going into Wednesday's Fed Day. We'll see how it plays out...

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