

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 26, 2010

Volume 3 Issue 164

## Market Overview



## Tonight's Research Points

- Wednesday's mild bounce brought about a bearish study.
- The Aggregator System turned flat.
- The NDX Aggressive Trend Timer remained long.

## Short-term Outlook

### The Bottom Line

My gut says we bounce a little further. My studies say there is no longer an upside edge. I'm looking to reduce my long exposure.

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
<b>Active</b>				
August 26, 2010	SPY gap dn 10-low reverse up	1-3 days	Bearish	-3.70%
August 25, 2010	SPX down 1%. Decliners 2x advancers	1-9 days	Bullish	3.00%
August 24, 2010	3 lower closes into Turnaround Tuesday	1-9 days	Bullish	3.70%
August 24, 2010	HV low SPX no highs	1-8 days	Bearish	-3.20%
<b>Active - Long Term</b>				
August 16, 2010	1 (borderline) Hindenburg Omen Day	int term	Bearish	
August 3, 2010	50 high 90% volume	1-25 days	Bullish	
July 20, 2010	Down 1 week after FTD	int term	Bearish	
July 7, 2010	McClellan Oscillator Bottom Divergence	int term	Bullish	

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

### *The Evidence*

After a tough opening and early morning the market finally turned up a bit today. The low was made a little after 10am and it rallied most of the rest of the day. In the end the SPX gained a mild 0.3%, but the Nasdaq rallied 0.8% and the Russell 2000 shot up 1.6%. Breadth was mildly positive as the NYSE Up Issues % came in at 60% and the Up Volume % was 56%. Total volume declined from yesterday's level.

For the last couple of days we've seen some bullish studies appear suggesting a bounce was likely. The evidence was compelling enough to warrant a trade in my eyes but not overwhelming. For instance, while there were signs that the market was oversold, there were not strong signs of capitulation. In fact the Quantifiable Edges Capitulative Breadth Indicator has remained at 0 throughout this entire selloff.

So what this has meant is that without a strong number of studies suggesting a bounce, there's a better chance that some new bearish studies could turn the Aggregator negative. If there were a lot of studies saying the market was going to bounce, then 1 or 2 bearish studies wouldn't have a massive affect.

When the market is oversold and begins to bounce we often see the Quantifinder identify several bounce-related studies. Many times a bounce will provide strong hints as to whether it is likely to succeed on its 1<sup>st</sup> day. In general, strong bounces have a better chance of following through while weak bounces often roll over and fail. Wednesday's bounce wasn't terribly strong. A few studies emerged from the 2/6/09 Subscriber Letter that showed mixed results. I used the concepts from those studies, added a trend filter, and described the current action for closer study. The result was the below study.

SPY gaps down at least 0.25% and makes a 10-day low. It closes positive and at least 0.5% above the open. Close < 200ma. Buy on close. Sell X days later. \$100k/trade. 1993 - 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	-33,260.48	16	4	12	25.00	4,379.42	-4,231.51	1.03	0.34	-2,078.78
9	-36,858.65	17	5	12	29.41	2,932.40	-4,293.39	0.68	0.28	-2,168.16
8	-37,880.49	17	5	12	29.41	2,910.18	-4,369.28	0.67	0.28	-2,228.26
7	-16,324.26	18	7	11	38.89	2,539.08	-3,099.80	0.82	0.52	-906.90
6	-21,345.94	19	8	11	42.11	2,612.22	-3,840.34	0.68	0.49	-1,123.47
5	-30,115.19	20	7	13	35.00	2,547.85	-3,688.47	0.69	0.37	-1,505.76
4	-25,403.99	20	7	13	35.00	2,393.83	-3,243.14	0.74	0.40	-1,270.20
3	-27,577.34	21	6	15	28.57	2,015.39	-2,644.64	0.76	0.30	-1,313.21
2	-23,315.75	23	7	16	30.43	1,794.25	-2,242.22	0.80	0.35	-1,013.73
1	-16,116.21	23	7	16	30.43	1,738.64	-1,767.92	0.98	0.43	-700.70

21 of 23 instances (92%) closed below the entry price at some point in the next 4 days.

As I'll show below, with the relatively low number of bullish studies active this study is actually able to flip the Aggregator below 0 all by itself. But I have several systems I utilize that are all suggesting the market is likely to revert to its short-term mean and that Wednesday's bounce didn't do it so there should be more upside to come. These include some of the numbered systems that triggered last night.

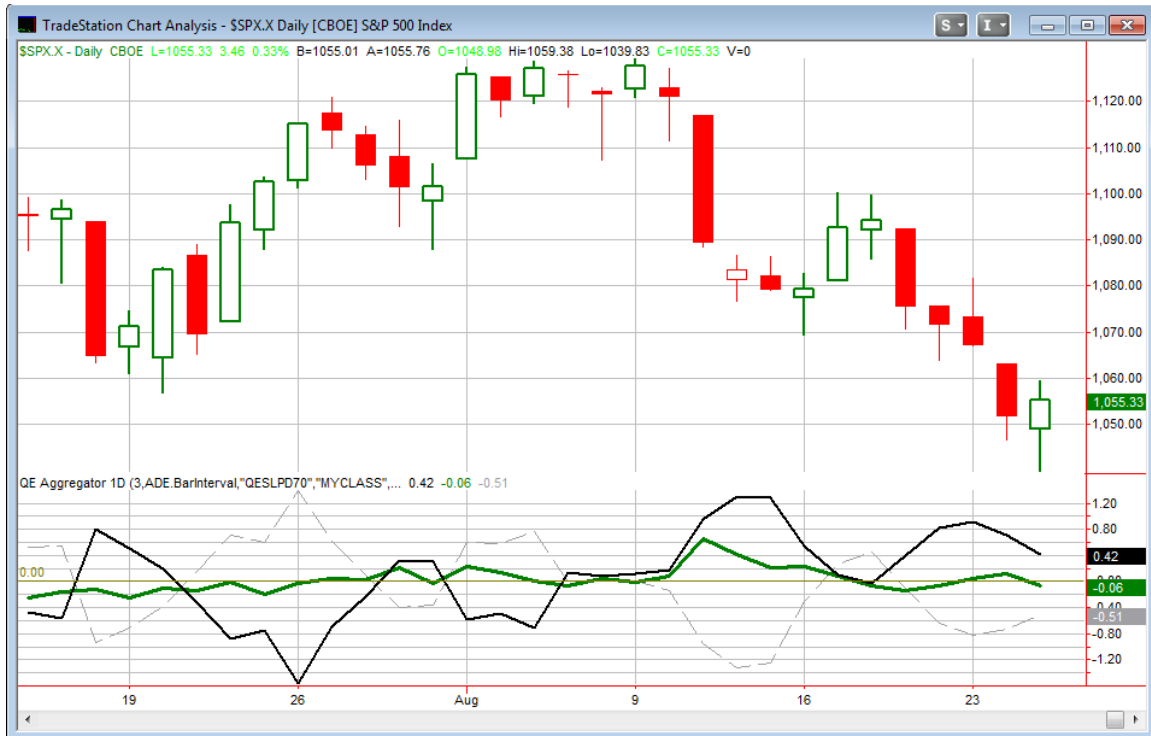
But that kind of logic isn't always the best way to evaluate the market. For instance, if you use a system that says buy when the RSI(2) hits 5 or lower and sell when it moves back to X or higher, that might give you a good exit target to follow based on your entry point. But it doesn't mean a mild bounce is likely to succeed. So I set up a little test using RSI2 and that mimicked the last few days' action.

Yesterday SPY closed at a 10-day low and RSI(2) < 5. Today RSI(2) closed between 25 and 35. Buy on close. Sell X days later. \$100k/trade. 1993 - 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	-1,187.46	8	4	4	50.00	2,565.31	-2,862.18	0.90	0.90	-148.43
4	3,071.14	8	5	3	62.50	2,351.30	-2,895.13	0.81	1.35	383.89
3	1,616.53	9	6	3	66.67	1,837.93	-3,137.01	0.59	1.17	179.61
2	-2,789.77	9	5	4	55.56	1,772.30	-2,912.82	0.61	0.76	-309.97
1	1,620.29	9	5	4	55.56	1,058.54	-918.11	1.15	1.44	180.03

The number of instances is extremely low but at this point there is neither a bullish nor bearish inclination suggested.

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



With tonight's study the green Aggregator has fallen below 0. The negative value indicates the net expectation from the Active Studies over the next few days is for downside. Meanwhile the black Differential line is strongly above 0. This means the SPX has underperformed expectations over the last few days. So we have negative expectations and a market that is oversold versus recent expectations. This is considered a neutral configuration and can be seen on the chart whenever both lines are on opposite sides of zero. Due to this the Aggregator System turned back to flat at the close.

Currently the green Aggregator line is set up to remain negative tomorrow. This could change depending on what studies emerge. Meanwhile the Differential pivot will be 1,065.64 tomorrow. This means the SPX would need to close about 10 points higher in order to flip the black Differential line back to negative.

**Intermediate-term Outlook (2 weeks – 2 months)– updated 8/23 – neutral to bullish**

It turned out to be mostly a week of churning in the market. The SPX finished down slightly and the Nasdaq and Russell were up slightly. No compelling studies emerged with intermediate-term significance. Intermediate-term studies are now split. If I had to bet, I would bet that the market will continue its move up from the early July lows rather than continue down and make another substantial leg lower. I don't have to bet for or against that though. At this point the market is in a position where I'm comfortable taking short-term trades on either the long or the short side. And until I have stronger intermediate-term conviction, that's just what I intend to do.

**Catapult and Capitulative Breadth Statistics**

[Catapult & CBI Presentation Link](#)

**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. I'll give new purchases a rest here for a day. Those looking for action should check out the triggers spreadsheet. There are several stocks and ETFs that triggered today.

**Current Open Trade Ideas**

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
IJR	8/9/2010	\$57.50	\$53.57	-6.83%		System 90609
SPY(1/4)	8/12/2010	\$107.65	\$105.94	-1.59%		
SPY(1/4)	8/24/2010	\$105.58	\$105.94	0.34%		sell @ \$105.94 limit
CMCSA	8/24/2010	\$17.29	\$17.33	0.23%		System 80402
UTX	8/25/2010	\$65.14	\$65.26	0.18%		System 80509

As noted above, with the Aggregator turning flat, I'm going to take off 1 lot here. I'll look for more of a bounce here before exiting the 2<sup>nd</sup> lot. I may look to start trailing a stop should the bounce continue higher.

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