

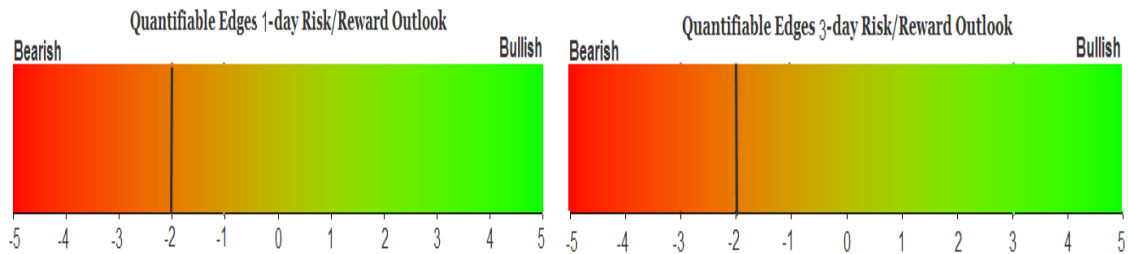
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 17, 2010

Volume 3 Issue 179

Market Overview



Tonight's Research Points

- Strongly overbought going into op-ex has historically suggested a downside edge.
- The Aggregator System remained short.
- The NDX Aggressive Trend Timer remained flat.

Short-term Outlook

The Bottom Line

Again...some more bearish studies extended the downside outlook another day. I'm still waiting for a pullback or a change in the Aggregator before exiting.

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				
September 17, 2010	Top 10% of 10-day range prior to op-ex	1-5 days	Bearish	
September 16, 2010	SPX Up VIX Up. 10 high > 200. Mid-wk	1-2 days	Bearish	-0.80%
September 16, 2010	SPY 10 days > 5ma & 10 day high	1-4 days	Bearish	-1.50%
September 13, 2010	AAII Spread Spike Up 40% in 2 weeks	1-9 days	Bullish	2.60%
September 8, 2010	SPX dn 1%. Decliners double advancers	1-9 days	Bullish	3.65%
Active - Long Term				
September 13, 2010	Low Vol 20. Low range 20. Close < 200	1-18 days	Bearish	
September 8, 2010	Tues after Labor Day lowest volume 5	1 month	Bearish	
September 2, 2010	2 90% Up Vol days in 1 week	1-20 days	Bullish	
September 1, 2010	August down > 4%	1 month	Bearish	
August 30, 2010	AAII Survery very bearish	1-30 days	Bullish	
August 16, 2010	1 (borderline) Hindenburg Omen Day	int term	Bearish	
July 20, 2010	Down 1 week after FTD	int term	Bearish	
July 7, 2010	McClellan Oscillator Bottom Divergence	int term	Bullish	
Dropped Tonight				
September 9, 2010	NDX Up 1%. SOX down. Buy SPX	1-6 days	Bearish	-3.20%
September 13, 2010	Low Vol 10. Low Range 10. > 10ma < 200	1-4 days	Bearish	-3.20%
September 10, 2010	SPY 20-hi close. < 200. Vol lower.	1-5 days	Bearish	-2.40%
September 10, 2010	SPY 2 Unfilled Up Gaps < 200ma	1-5 days	Bearish	-2.50%

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

The Evidence

A late-afternoon surge left the market mixed on Thursday after being down most of the day. The SPX closed down 0.04%, the Nasdaq was up 0.08% and the Russell 2000 lost 0.71%. Breadth was a little weak as the NYSE Up Issues % came in at 42% and the Up Volume % was 47%. Total NYSE volume dropped for the 3rd day in a row.

The late surge eliminated a few studies that were shown in the intraday Quantifinder as the gap filled and the range was no longer as tight. The ones that remained were a bit iffy as they were mostly only significant if trading below the 200ma.

One study from the Quantifinder tonight looked at times the Nasdaq rose while the Nasdaq Up Issues % was less than 40%. This had previously appeared to suggest a short-term bearish edge. When I went to update the 7/9/2009 study tonight I found that the bearish edge was no longer apparent – especially over the last year or so. I'll be removing this one from the Quantifinder.

But even without much help from the Quantifinder tonight I did find one study with interesting results. While op-ex week is often positive, it is unusual to go into options expiration day *this* overbought. I ran some statistics on other times the market was trading at the top end of its 10-day range just before option expiration.

SPX closes in the top 10% of its 10-day range. Tomorrow is options expiration. Buy on close. Sell X days later. \$100k/trade. 1988 - 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	-24,128.71	68	30	38	44.12	1,230.61	-1,606.50	0.77	0.60	-354.83
4	-21,153.04	68	28	40	41.18	1,047.09	-1,261.79	0.83	0.58	-311.07
3	-20,342.12	68	31	37	45.59	717.72	-1,151.12	0.62	0.52	-299.15
2	-16,961.52	68	30	38	44.12	687.79	-989.35	0.70	0.55	-249.43
1	-6,749.12	68	33	35	48.53	495.98	-660.47	0.75	0.71	-99.25

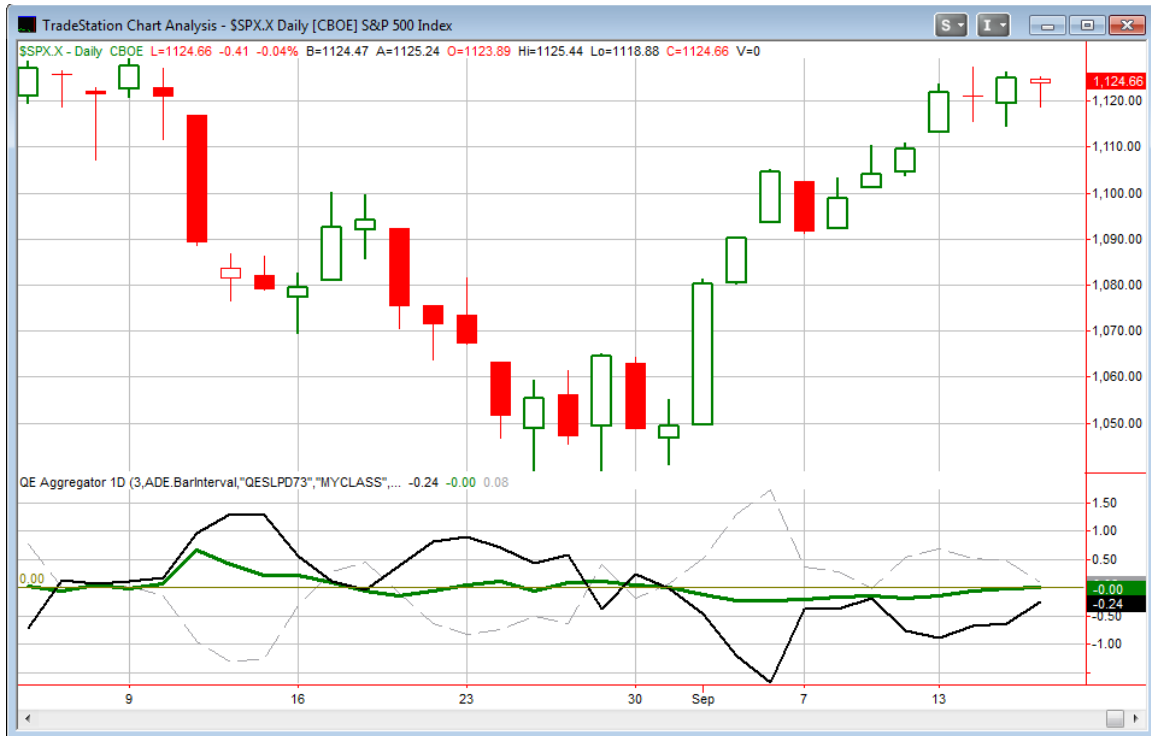
Based on these numbers there appears to be a bit of a downside edge. I also ran the test using a 200ma filter to see if it still looked bearish during an uptrend.

SPX closes in the top 10% of its 10-day range. Tomorrow is options expiration. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1988 - 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	-25,271.04	54	23	31	42.59	1,152.99	-1,670.64	0.69	0.51	-467.98
4	-17,503.78	54	23	31	42.59	927.85	-1,253.05	0.74	0.55	-324.14
3	-16,572.11	54	24	30	44.44	729.91	-1,136.33	0.64	0.51	-306.89
2	-12,011.34	54	24	30	44.44	532.80	-826.62	0.64	0.52	-222.43
1	-6,340.74	54	27	27	50.00	397.59	-632.43	0.63	0.63	-117.42

The 200ma seems to make almost no difference whatsoever. The apparent edge here is not thanks to the % Profitable, but rather due to the fact that the losers were substantially larger than the winners.

One other seasonal note is that September post op-ex week has historically been the worst week of the year. I'll show details on this in this weekend's letter. While seasonals (and everything else) has been ignored lately, it's something to keep in mind as next week approaches.

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



The Aggregator chart is still barely hanging on to its negative outlook. The green Aggregator line remains just fractionally below zero. The negative value indicates the net expectation from the Active Studies over the next few days is for flat to down movement. Meanwhile the black Differential line is also below 0. This means the SPX has outperformed expectations over the last few days. So we have slightly negative expectations and a market that is overbought versus recent expectations. Historically, this has provided a downside edge. The condition is represented by both lines closing below 0. Due to this the Aggregator System remained short.

The green Aggregator line may flip to positive tomorrow depending on market action and studies. Meanwhile the Differential pivot will be 1,116.53 tomorrow. It would take an SPX close at or below this level to flip the black Differential line positive. That's about a 0.8% decline from Thursday's closing level.

It's been a very frustrating rally to sit through the last several days. Each day's action has seemed to bring about more bearish studies, and other than a sentiment-based study from Sunday night we haven't seen any bullish results all week. If the rally was accompanied by strong breadth, strong volume, or very strong price action we likely would be off the short easily by now. For the most part it has been a slow slog higher. At some point soon all these bearish studies are going to start to matter again. Until then I'll remain patient and alert for signs that the market could be gaining steam.

Intermediate-term Outlook (2 weeks – 2 months)– updated 9/13 – neutral

A couple of weeks ago I looked at the [AAII Investor Sentiment Survey](#). It had become extremely bearish. The study showed bullish intermediate-term inclinations following such extreme bearishness. These inclinations generally played out over the next 30 days. Over the last 2 weeks though as the market has rallied there has been a large swing in sentiment from extremely bearish to slightly bullish. I wondered whether this swing might mean the anticipated rally was already nearing its end. So I devised a study that looked at other similar instances in the past.

The reading 2 weeks ago was 29% net bears. This week it came in at 12% net bulls. So I looked for other times there was a spike of 40% or more in the bull spread over a 10 (trading) day period.

AAII Sentiment Survey Bull-Bear Spread jumps more than 40 points in the last 10 days. Buy SPX on close. Sell X days later. \$100k/trade. 1987 - 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	-5,560.14	16	10	5	62.50	2,859.66	-6,831.35	0.42	0.84	-347.51
19	4,896.14	15	7	8	46.67	3,190.41	-2,179.59	1.46	1.28	326.41
18	8,222.21	15	8	7	53.33	2,663.42	-1,869.30	1.42	1.63	548.15
17	9,835.26	15	9	6	60.00	2,211.39	-1,677.88	1.32	1.98	655.68
16	15,684.17	15	8	7	53.33	3,433.25	-1,683.12	2.04	2.33	1,045.61
15	14,606.83	15	8	7	53.33	3,424.62	-1,827.16	1.87	2.14	973.79
14	9,311.34	15	8	7	53.33	2,373.14	-1,381.97	1.72	1.96	620.76
13	13,669.17	15	11	4	73.33	1,710.25	-1,285.90	1.33	3.66	911.28
12	18,115.21	15	9	6	60.00	2,267.62	-382.23	5.93	8.90	1,207.68
11	18,095.66	15	10	5	66.67	2,192.92	-766.70	2.86	5.72	1,206.38
10	24,095.45	15	13	2	86.67	1,916.84	-411.74	4.66	30.26	1,606.36
9	25,969.57	16	14	1	87.50	1,858.47	-49.00	37.93	530.99	1,623.10
8	24,696.64	18	14	2	77.78	1,890.22	-883.19	2.14	14.98	1,372.04
7	14,624.26	19	11	6	57.89	1,972.87	-1,179.56	1.67	3.07	769.70
6	14,880.88	19	12	6	63.16	1,808.03	-1,135.92	1.59	3.18	783.20
5	15,042.21	19	9	8	47.37	2,329.92	-740.88	3.14	3.54	791.70

I ran these results out much further as well. It appears the rush of people from bearish to bullish often kept the market momentum going for a couple of weeks, but beyond that there was no discernable edge. Looking out as far as 70 days the net "Avg Trade" never

got much above the 1.6% gain realized in the first 2 weeks. So I don't see any reason to take the AAI study from a few weeks ago off the board just because the bulls jumped. In fact, I've added this new one to the short-term list.

But while the AAI remains active, the long-term active list studies has slowly been looking more bearish. The August 3rd new high on strong breadth study has expired. And today's low range, low volume study was the 2nd bearish one in a row to make the list. At this point factors such as breadth and sentiment are suggesting upside in the coming weeks while seasonality and the low volume are suggesting a pullback. Momentum certainly favors the bulls but we are now bumping up against resistance in the form of the 200ma and the August highs. With all this conflicting evidence I'm not strongly inclined to favor either side at this point. I'll be looking equally at both long and short opportunities.

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.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)(s)	9/2/2010	\$109.47	\$113.05	-3.27%		Aggregator
SPY(1/4)(s)	9/3/2010	\$110.54	\$113.05	-2.27%		Aggregator
SPY(1/4)(s)	9/3/2010	\$110.54	\$113.05	-2.27%		Aggregator
SPY(1/4)(s)	9/13/2010	\$112.58	\$113.05	-0.42%		Aggregator

Unless I send out an intraday update to the contrary I'll look to cover the entire SPY position at the close tomorrow if the SPX finishes at 1,116.53 or lower.

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