

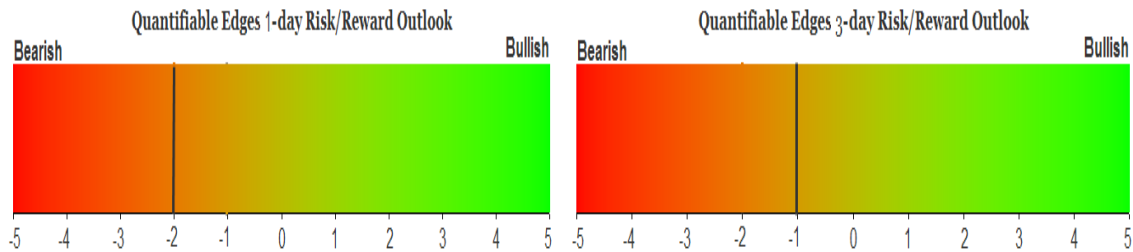
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 29, 2010

Volume 3 Issue 187

## Market Overview



## Tonight's Research Points

- Outside days hitting new highs on good volume often lead to a pullback.
- The rise in the VIX could also be a short-term warning.
- The Aggregator System flipped remained short.
- The NDX Aggressive Trend Timer remained long.

## Short-term Outlook

### The Bottom Line

While the Aggregator is still suggesting a short-side edge, the market is in a tricky spot. I'll be looking to take on a little short exposure under the right conditions.

## 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>				
September 29, 2010	Outside day 50-high	1-3 days	Bearish	-1.10%
September 28, 2010	Nasdaq Spyx < 0. QQQQ 10-day high.	1-4 days	Bearish	-1.75%
September 27, 2010	1% gap-n-go to a 50-day high	1-3 days	Bearish	-1.50%
<b>Active - Long Term</b>				
September 20, 2010	Nas/SPX RS favors Nasdaq	int term	Bullish	
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	
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*

A morning selloff saw a quick turnaround and the major indices all put in gains for the day. The SPX rose 0.5%, the Nasdaq was up 0.4% and the Russell 2000 posted a 1.1% gain. Breadth was strong as the NYSE Up Issues % came in at 68% and the Up Volume % was 56%. Total volume rose and also came in above average.

Tuesday's price & volume action had a lot of characteristics that would appear bullish. These include the fact that it posted an outside day and closed higher. It also made a new 50-day intraday high. The SPX is in a long-term uptrend and trading above its 200ma. Lastly, the volume rose Thursday as the market rallied. Sometimes it can be interesting to take a number of market observations like these that would seem to obviously suggest a bullish edge and run them through the wayback machine. I did just this in the 1/8/2010 blog. Below I have updated that study:

SPY posts an outside day and makes a 50-day intraday high. It closes higher than yesterday and above the 200ma. Volume > yesterday. 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	-7,702.79	24	14	10	58.33	924.73	-2,064.91	0.45	0.63	-320.95
4	-5,738.14	26	13	13	50.00	789.90	-1,231.29	0.64	0.64	-220.70
3	-7,504.64	26	11	15	42.31	794.69	-1,083.08	0.73	0.54	-288.64
2	-2,553.83	27	12	15	44.44	662.53	-700.28	0.95	0.76	-94.59
1	-719.31	27	11	16	40.74	507.24	-393.69	1.29	0.89	-26.64

**23 of 27 instances (85%) posted a close below the entry price at some point in the next 3 days.**

Rather than combining for a bullish edge it appears the scenario above has often been followed by downside.

Other notable action identified by the Quantifinder tonight was that despite the rise in the market, the VIX also rose. Often when this happens it brings about bearish studies. But when it happens mid-week and above the 200ma, results have looked pretty neutral. I looked at this even closer in the 11/12/09 subscriber letter. Below is an excerpt. (Studies not updated.)

What's interesting about today, though is not only that the SPX is above its 200ma, but also that it closed at a new high. I further broke the above study down to look at instances that were at new highs versus those that weren't. First – times where the market was NOT at new highs.

SPX & VIX both close higher on a Tuesday, Wednesday, or Thursday. Close > 200ma but below a 50-day high. 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	7,851.19	42	24	18	57.14	1,435.64	-1,478.01	0.97	1.30	186.93
4	2,581.86	42	22	20	52.38	1,367.94	-1,375.64	0.99	1.09	61.47
3	-1,316.30	44	25	19	56.82	1,081.42	-1,492.20	0.72	0.95	-29.92
2	5,386.08	45	26	19	57.78	957.14	-1,026.29	0.93	1.28	119.69
1	-1,278.65	46	23	23	50.00	694.31	-749.90	0.93	0.93	-27.80

No edge apparent here. Now times like today with the SPX at new highs.

SPX & VIX both close higher on a Tuesday, Wednesday, or Thursday. Close > 200ma and at a 50-day high. 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	-14,562.80	36	17	19	47.22	683.01	-1,377.57	0.50	0.44	-404.52
4	-10,833.53	38	14	24	36.84	921.44	-988.91	0.93	0.54	-285.09
3	-6,291.18	38	16	22	42.11	752.26	-833.06	0.90	0.66	-165.56
2	-9,224.51	38	11	27	28.95	669.26	-614.31	1.09	0.44	-242.75
1	-4,146.32	45	21	24	46.67	252.04	-393.30	0.64	0.56	-92.14

**92% of instances closed lower than the entry price at some point in the next week.**

These stats suggest an apparent downside edge. Apparently the VIX should not be on the rise when the SPX is hitting new highs. The fact that it rose today implies a short-term pullback.

The market did not close at a 50-day high Tuesday, but it only missed doing so by less than 1 point, so perhaps the VIX action may serve as a slight short-term negative.

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



Not much change to the Aggregator configuration again tonight. The green Aggregator line remains 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 also remains below 0. This means the SPX has outperformed expectations over the last few days. So we have negative expectations and a market that is overbought versus recent expectations. This is considered a bearish configuration. It is reflected on Aggregator chart when both lines are below 0. Due to this the Aggregator System remained short at the close.

The green Aggregator line is set up to close below 0 again tomorrow but that could change should bullish studies arrive. Meanwhile the Differential pivot will be 1,149.99 tomorrow. It would take an SPX close at or below this level to flip the black Differential line positive. This means even a small rise in the SPX would allow it to move to “oversold versus expectations”. The only way the Aggregator short signal could stay active is if the SPX closes at 1,150 or higher.

Overall action has been odd the last several days. We've consistently seen bearish (or neutral) studies on both up and down days. There are a lot more bullish studies in the Quantifinder than there are bearish ones when the market is above the 200ma, so to go without any short-term bullish indications is unusual. With all this bearish evidence I will look to enter a small short position. I will need to get a favorable entry though, especially considering the short signal could come off unless the SPX closes above the 1,150 level. Details in the trade idea section below.

**Intermediate-term Outlook (2 weeks – 2 months)– updated 9/27 – bullish**

The SPX is now up over 9% for September. I thought it would be interesting to look and see how the market had performed in the past following other months that saw strong rallies. This first study looks at months that gained at least 9%.

SPX closes up 9% for the month. Buy on close. Sell X months later. \$100k/trade. 1960 - present.										
QE monthly: daysin	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
6	79,152.18	11	7	4	63.64	14,543.47	-5,663.04	2.57	4.49	7,195.65
5	69,084.50	11	8	3	72.73	11,347.75	-7,232.50	1.57	4.18	6,280.41
4	33,914.95	11	6	5	54.55	9,669.03	-4,819.84	2.01	2.41	3,083.18
3	30,579.97	12	7	5	58.33	7,969.35	-5,041.10	1.58	2.21	2,548.33
2	22,253.30	13	7	6	53.85	6,467.01	-3,835.96	1.69	1.97	1,711.79
1	4,555.36	13	6	7	46.15	3,443.40	-2,300.72	1.50	1.28	350.41

Over the next few months there hasn't been a real strong inclination but mild upside has been the net result. What if we isolate the front month and look at a range the market rises the month before?

SPX closes up X% for the month. Buy on close. Sell X months later. \$100k/trade. 1960 - present.										
QE monthly: pctup	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
9	4,555.36	13	6	7	46.15	3,443.40	-2,300.72	1.50	1.28	350.41
8	35,476.75	21	14	7	66.67	3,684.41	-2,300.72	1.60	3.20	1,689.37
7	40,058.45	35	23	12	65.71	3,333.55	-3,051.10	1.09	2.09	1,144.53
6	59,273.29	45	32	13	71.11	3,161.21	-3,221.95	0.98	2.42	1,317.18
5	83,775.30	74	54	20	72.97	2,782.18	-3,323.12	0.84	2.26	1,132.10

Results are generally good across the board. It does appear that when the % rise is very large that the edge for the next month is reduced some. Perhaps those very large gains need to be consolidated a bit before the move up can continue. I also filtered using the

10-month moving average. I did this because a good amount of the time the market made very large advances it was bouncing back from a very oversold level.

SPX closes up X% for the month. It closes > 10-month ma. Buy on close. Sell X months later. \$100k/trade. 1960 - present.										
QE monthly: pctup	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: WinLoss Ratio	All: ProfitFactor	All: Avg Trade
9	4,591.03	11	5	6	45.45	3,075.75	-1,797.96	1.71	1.43	417.37
8	20,484.44	17	11	6	64.71	2,842.93	-1,797.96	1.58	2.90	1,204.97
7	15,325.50	27	16	11	59.26	2,913.84	-2,845.08	1.02	1.49	567.61
6	25,015.41	35	23	12	65.71	2,677.54	-3,047.34	0.88	1.68	714.73
5	52,860.71	60	42	18	70.00	2,571.86	-3,064.29	0.84	1.96	881.01

There still appears to be a small upside edge present here. It does seem to be greatly reduced from the results that include times the market closed below its 10-month moving average.

Overall the market is acting well. In the SPX this week the pullback held above the 200ma. The 1,114 – 1,123 level should act as support. There are presently a few levels of price support as well as the 200ma right in that area.

The intermediate-term studies remain mixed. Volume and seasonality are favoring the bears while breadth and leadership structure favor the bulls. We're overbought here short-term, but as long as we continue to make new highs and the studies at least remain split, I'll be favoring the long side. At this point I will be a bit extra conservative with my short trades and a bit more aggressive with my long trades

**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.*

*SPY – short 1/4 index position @ \$115.50 LIMIT ON OPEN. If not filled then cancel order and look to short on a SPX close of 1,150 or higher. Based on Aggregator configuration and short-term outlook.*

### **Current Open Trade Ideas**

None.

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