

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 12, 2011

Volume 4 Issue 8

Market Overview



Tonight's Research Points

- The current consolidation isn't providing much in the way of clues.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

The market bounced, but not enough. I'm giving my partial long position one more day and am hoping to take profits on Wednesday.

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				
January 11, 2011	3 Days Down with extras	1-4 days	Bullish	2.60%
January 11, 2011	SPY 1st 5-day low in 10 days	1-4 days	Bullish	1.60%
January 3, 2011	SPX down last 2 days of up quarter	1-8 days	Bullish	2.90%
Active - Long Term				
January 10, 2011	Nas/SPX RS Indicator favors Nas	int term	Bullish	
January 4, 2011	SPX up 1st day of year	1-13 days	Bearish	
January 3, 2011	SPX down last 2 days of up quarter	1-15 days	Bullish	
December 30, 2010	SPX closes > 10ma every day of month	1 month	Bullish	
December 16, 2010	2 Hindenburg Signals	1-50 days	Bearish	
December 9, 2010	SPX & TNX 50-day highs	1-50 days	Bearish	
November 22, 2010	High number of POMO Days recently	int term	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	
Dropped Tonight				

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

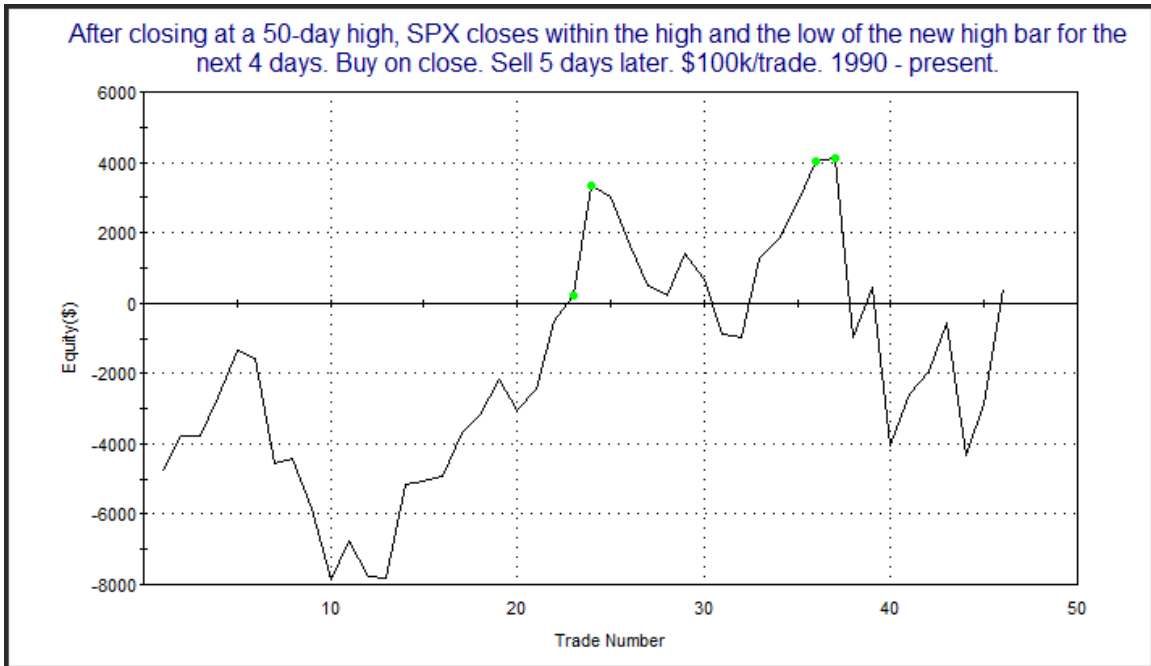
The Evidence

Turnaround Tuesday arrived as anticipated, but without much oomph. The major indices opened strong, sold off in the early afternoon and then rallied into the close to finish near the middle of the day's range. In the end the SPX and Russell 2000 each gained about 0.4% and the NASDAQ rose 0.3%. Breadth was modestly positive as the NYSE Up Issues % came in at 59% and the Up Volume % was 65%. Total NYSE volume dropped for the second day in a row.

The Quantifinder came up with a rare blank tonight, though it isn't too surprising considering the tight consolidation over the last few days. One common belief with tight consolidations is that they often resolve themselves in the direction of the trend. I looked at the current setup a number of ways and found no evidence of a substantial tendency suggesting which way the current consolidation would break. Below is an example.

After closing at a 50-day high, SPX closes within the high and the low of the new high bar for the next 4 days. Buy on close. Sell X days later. \$100k/trade. 1990 - 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	3,302.46	45	27	18	60.00	1,833.76	-2,567.17	0.71	1.07	73.39
9	5,231.57	45	27	18	60.00	1,671.98	-2,217.32	0.75	1.13	116.26
8	5,649.66	45	25	20	55.56	1,682.42	-1,820.54	0.92	1.16	125.55
7	1,655.72	46	27	19	58.70	1,435.31	-1,952.51	0.74	1.04	35.99
6	-2,598.36	46	24	22	52.17	1,394.66	-1,639.56	0.85	0.93	-56.49
5	400.56	46	27	19	58.70	1,207.74	-1,695.18	0.71	1.01	8.71
4	6,323.48	46	29	17	63.04	1,124.75	-1,546.72	0.73	1.24	137.47
3	3,801.08	46	27	19	58.70	968.83	-1,176.71	0.82	1.17	82.63
2	-3,860.08	47	24	23	51.06	777.78	-979.43	0.79	0.83	-82.13
1	-4,200.10	47	27	20	57.45	572.22	-982.50	0.58	0.79	-89.36

The percent profitable column appears to give a slight edge to the bulls, but that is entirely offset by the negative win/loss ratio. So the profit expectancy over the next several days is essentially 0. I created an equity curve to see what any possible edge may have looked like over time.



It appears there has never been a reliable edge with regards to this setup.

The short-term Active List is therefore unchanged tonight. Expectations are little changed as well.

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



With the short-term Active List only showing bullish studies, the green Aggregator line remains strongly above 0. The positive value means the net expectation from the Active Studies List is for upside over the next few days. Meanwhile the black Differential line is also above 0. The positive value means the SPX has underperformed expectations over the last few days. So net expectations are for upside and the SPX has underperformed recent expectations. This leaves both lines above zero. Historically this configuration has provided an upside edge. Due to this the Aggregator System remained long at the close.

The green Aggregator line tomorrow is set up to remain above 0. Of course this could change if substantial bearish evidence emerges. Meanwhile the Differential Pivot will be 1,269.83. This is almost 0.4% below Tuesday's close. This means that unless the SPX falls at least this much, the black Differential line will flip from positive to negative. With that in mind, traders may want to consider approaching Wednesday's action with a "profit taking" mindset. Trailing stops up as the market moves higher may be appropriate since you will be looking for an exit on a positive (or mildly negative) close anyway.

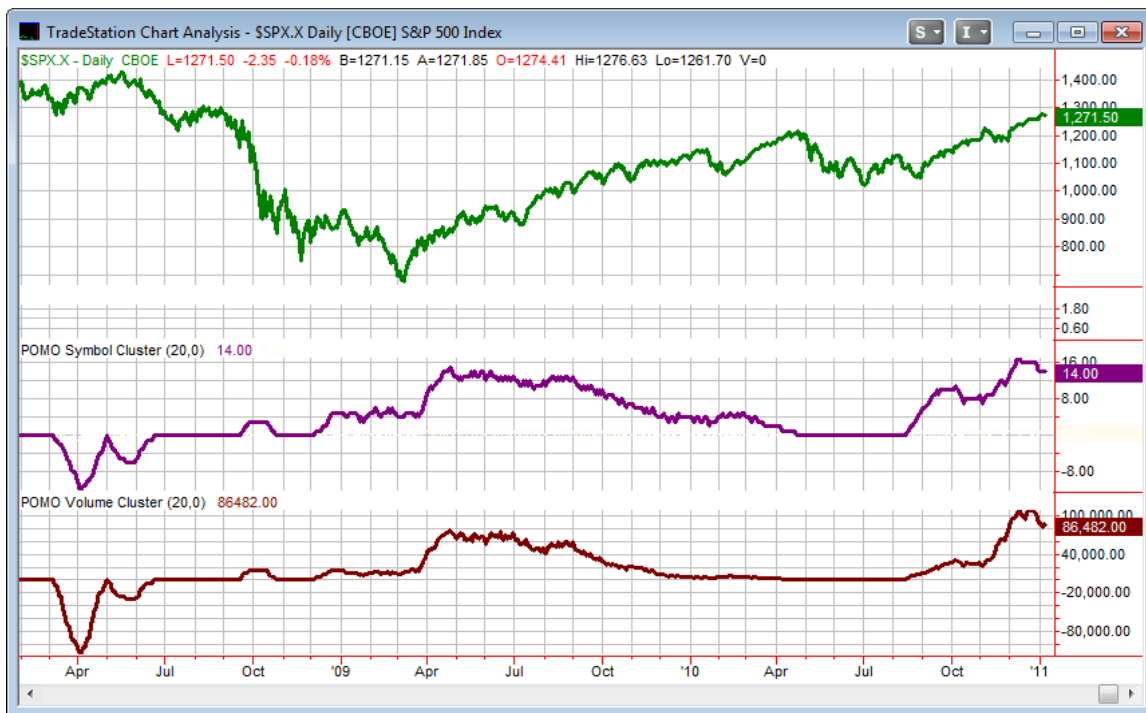
If my intermediate-term outlook was more bullish then I would've considered adding to the long position more aggressively. There are just too many intermediate-term bearish studies and the market has been overbought for so long that I am wary of a correction. I'll be looking to take any profits on the open trade idea as of Wednesday's close.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/3 – neutral to slightly bullish

Intermediate-term indications remain mixed. New highs continue to be made each week, and until price weakness is evident I will likely continue to favor the bullish outlook.

I've been updating the POMO chart each week in the Letter. For those who may not recall below is a brief refresher on POMO. Beneath that I have updated our POMO indicator chart.

POMO stands for Permanent Open Market Operations and it is how the Fed goes into the open market to buy securities. The net effect of this buying is an influx of cash into the system. It appears a portion of that cash makes its way to the stock market and works as a bullish influence. A “POMO Day” is simply a day where these operations take place... The chart below (shows a couple of POMO indicators). The top pane is the S&P 500. The middle pane is the rolling number of days in the last 20 that have been POMO days. The bottom pane is the total amount of money infused into the system over the previous 20 days.



Fed POMO activity picked up again this past week. The 20-day totals are off their peak levels but still very high. Monday and Tuesday are both scheduled for additional Fed buying. Wednesday is not, but the Fed schedule for the next month will be released on Wednesday at 2pm EST. This should provide a nice clue as to the potential tailwind that

the Fed might be providing to the markets in the coming weeks. Right now the recent POMO activity is high and that should still continue to act as a positive for a bit longer.

Subscribers should note that I gave a special presentation to gold subscribers this past week on the construction of the POMO indicators. I also answered questions on them, shared the Tradestation code, and provided links to the Fed website where the complete data history can be found. Both gold and silver subscribers may view the video and download the Tradestation code by visiting the POMO Video on the videos page of the website. For your convenience, I have also posted a link below.

<http://www.quantifiableedges.com/members/pomo.php>

One other intermediate-term positive is that the SPX/Nasdaq Relative Strength indicator that I track on the charts page has now flipped and the Nasdaq is again in a leading position. Since the inception of the Nasdaq in 1971, the SPX has made all its gains when the Nasdaq was in a leading position. More details on this indicator can be found in the 5/26/09 blog. Subscribers can also download the models (both Excel and Tradestation) from the downloads page.

So POMO, momentum, and relative strength continue to favor the bull case. The negative intermediate-term studies are based on seasonality, breadth, and bond action. This means there is still quite a mix of studies and indicators for the intermediate-term. With the trend still favoring the bulls I'm inclined to give them the slight edge. I will continue to look for trades in both directions but will trade the short side with a bit more caution.

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)	1/10/2011	\$126.98	\$127.43	0.35%		Aggregator

I will exit the SPY position on any close of \$126.99 or higher.

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