

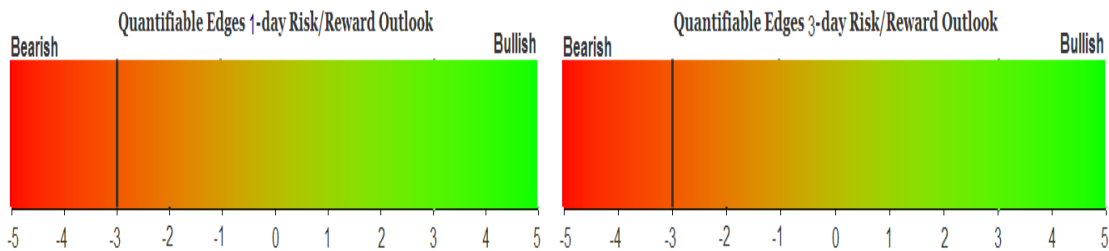
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 18, 2011

Volume 4 Issue 34

Market Overview



Tonight's Research Points

- When the market closes near an intermediate-term high just before op-ex it suggests a downside edge.
- Friday prior to President's Day has been seasonally bearish over the last 19 years.
- The Aggregator System is short.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

Bearish inclinations continued to be ignored and the market trudged higher. Still, the action is again suggesting a historical downside edge. I am looking to take advantage of it with a conservatively-sized short position.

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				
February 18, 2011	Friday Before Pres Day	1 day	Bearish	
February 18, 2011	Upper end of range prior to op-ex	1-4 days	Bearish	
February 17, 2011	SPY 10 days > 5ma & 10-day high	1-2 days	Bearish	-1.20%
February 17, 2011	SPX 50 high VIX up midweek	1-2 days	Bearish	-0.80%
February 16, 2011	SPY 5 gaps lower	1-3 days	Bullish	2.50%
February 16, 2011	Unfilled gap from 10 high. Opn&cls high	1-3 days	Bearish	-1.70%
Active - Long Term				
January 21, 2011	SPY 1st close < 10ma in over 25 days	1-20 days	Bullish	
January 19, 2011	SPX 20-day high. Vol 20-day high.	int term	Bullish	
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	

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

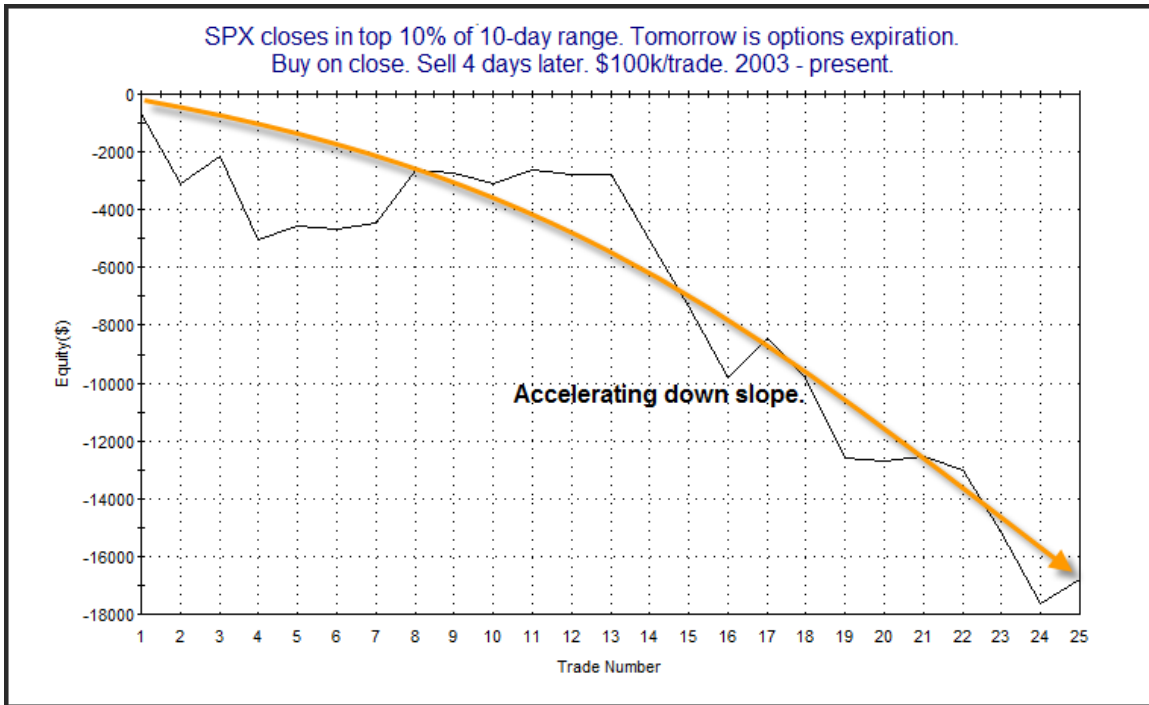
The Evidence

Once again the market managed to shake off morning weakness and finish the day near its high. Major indices were mostly higher. The SPX rose 0.3%, the Nasdaq was up 0.2% and the Russell 2000 gained 0.7%. Breadth was positive with the NYSE Up Issues % coming in at 62% and the Up Volume % at 69%. Volume again dipped as the market rallied, coming in at a very low level.

Bearish studies are once again coming to the fore this evening. While I examined several fresh ideas tonight, I was unable to come up with anything compelling outside of those identified by the Quantifinder. This first one is from the 9/17/10 Subscriber Letter. On 9/17 I ran the study back to 1988. Upon closer examination tonight I found the edge has become more pronounced starting in 2003. Below are the numbers going back to 2003.

SPX closes in top 10% of 10-day range. Tomorrow is options expiration. Buy on close. Sell X days later. \$100k/trade. 2003 - 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	-17,345.20	25	8	17	32.00	1,042.23	-1,510.77	0.69	0.32	-693.81
4	-16,768.32	25	8	17	32.00	794.80	-1,360.39	0.58	0.27	-670.73
3	-7,128.39	25	13	12	52.00	606.72	-1,251.31	0.48	0.53	-285.14
2	-8,154.03	25	14	11	56.00	459.26	-1,325.78	0.35	0.44	-326.16
1	-4,265.03	25	12	13	48.00	405.83	-702.69	0.58	0.53	-170.60

Numbers here are moderately compelling. To confirm the downside edge, I also ran an equity curve. This curve is based on a 4-day exit strategy.



This curve would seem to confirm the downside edge suggested by the stats table.

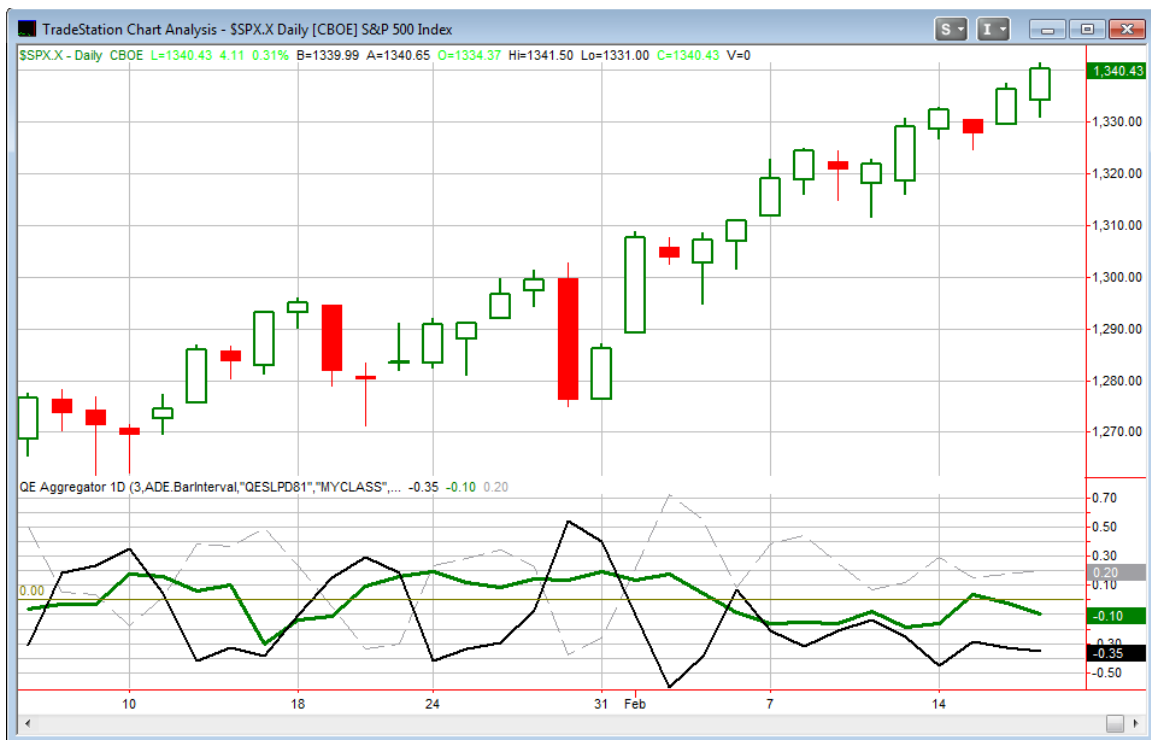
Friday is also the last day before the President's Day holiday. Over the last 19 years the Friday before President's Day has been a poor performer. I showed this last year in the 2/12/10 Subscriber Letter. I have updated the results in the table below.

SPX performance on the Friday before President's Day.
\$100k/trade. 1992 - 2010.

Date/Time	Signal	Price	% Profit	Run-up DrawDown
02/13/92	Buy	\$413.68	(0.29%)	\$38.56
02/14/92	Sell	\$412.47		(\$600.09)
02/11/93	Buy	\$447.65	(0.69%)	\$8.92
02/12/93	Sell	\$444.58		(\$684.61)
02/17/94	Buy	\$470.34	(0.56%)	\$159.00
02/18/94	Sell	\$467.69		(\$905.24)
02/16/95	Buy	\$485.22	(0.67%)	\$0.00
02/17/95	Sell	\$481.97		(\$669.50)
02/15/96	Buy	\$651.34	(0.52%)	\$12.24
02/16/96	Sell	\$647.98		(\$665.55)
02/13/97	Buy	\$811.83	(0.42%)	\$45.51
02/14/97	Sell	\$808.45		(\$452.64)
02/12/98	Buy	\$1,024.14	(0.40%)	\$0.00
02/13/98	Sell	\$1,020.08		(\$623.71)
02/11/99	Buy	\$1,254.03	(1.91%)	\$0.79
02/12/99	Sell	\$1,230.13		(\$2,251.50)
02/17/00	Buy	\$1,388.25	(3.04%)	\$0.00
02/18/00	Sell	\$1,346.09		(\$3,090.96)
02/15/01	Buy	\$1,326.61	(1.90%)	\$0.00
02/16/01	Sell	\$1,301.47		(\$2,507.25)
02/14/02	Buy	\$1,116.48	(1.10%)	\$54.29
02/15/02	Sell	\$1,104.18		(\$1,179.25)
02/13/03	Buy	\$817.37	2.14%	\$2,137.44
02/14/03	Sell	\$834.89		(\$285.48)
02/12/04	Buy	\$1,152.11	(0.55%)	\$410.22
02/13/04	Sell	\$1,145.81		(\$763.68)
02/17/05	Buy	\$1,200.75	0.07%	\$180.11
02/18/05	Sell	\$1,201.58		(\$282.20)
02/16/06	Buy	\$1,289.38	(0.17%)	\$6.93
02/17/06	Sell	\$1,287.24		(\$408.87)
02/15/07	Buy	\$1,456.81	(0.09%)	\$0.00
02/16/07	Sell	\$1,455.54		(\$356.32)
02/14/08	Buy	\$1,348.86	0.08%	\$84.36
02/15/08	Sell	\$1,349.98		(\$794.02)
02/12/09	Buy	\$835.19	(1.00%)	\$504.56
02/13/09	Sell	\$826.84		(\$1,187.62)
02/11/10	Buy	\$1,078.47	(0.27%)	\$0.00
02/12/10	Sell	\$1,075.51		(\$1,426.00)
Avg Trade: -0.6% Avg Runup: 0.2% Avg Drawdown: -1.0%				

Inclinations appear squarely bearish. Among the 3 up years, only one of them has posted a gain of over 1%. And with drawdown/runup ratio coming in at over 5:1, risk/reward strongly favors the bears.

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



Tonight's bearish studies helped to keep the green Aggregator line below 0. The negative value means the net expectation from the Active Studies List is for downside over the next few days. Meanwhile the black Differential line is still below 0. Readings below 0 mean the SPX has outperformed expectations over the last few days. So net expectations are for downside and the SPX has outperformed recent expectations. Historically this configuration has suggested a bearish edge. It is evident on the chart whenever both lines are below zero. Due to this the Aggregator System remained short at the close.

Based on the current active studies the green Aggregator line is set to remain below 0 on Friday. This could change if bullish evidence emerges. Meanwhile the Differential Pivot will be at 1,323.65. This is about 1.25% below Thursday's close. For the Differential Line to move above zero it would require the SPX to drop at least this much.

With the Aggregator again still negative I am going to look to add another lot to my short position. As with most counter-trend trades, I'll be taking a conservative approach. It's unlikely I'll increase this position. The trend has been too strong and too able to withstand short-term bearish headwinds.

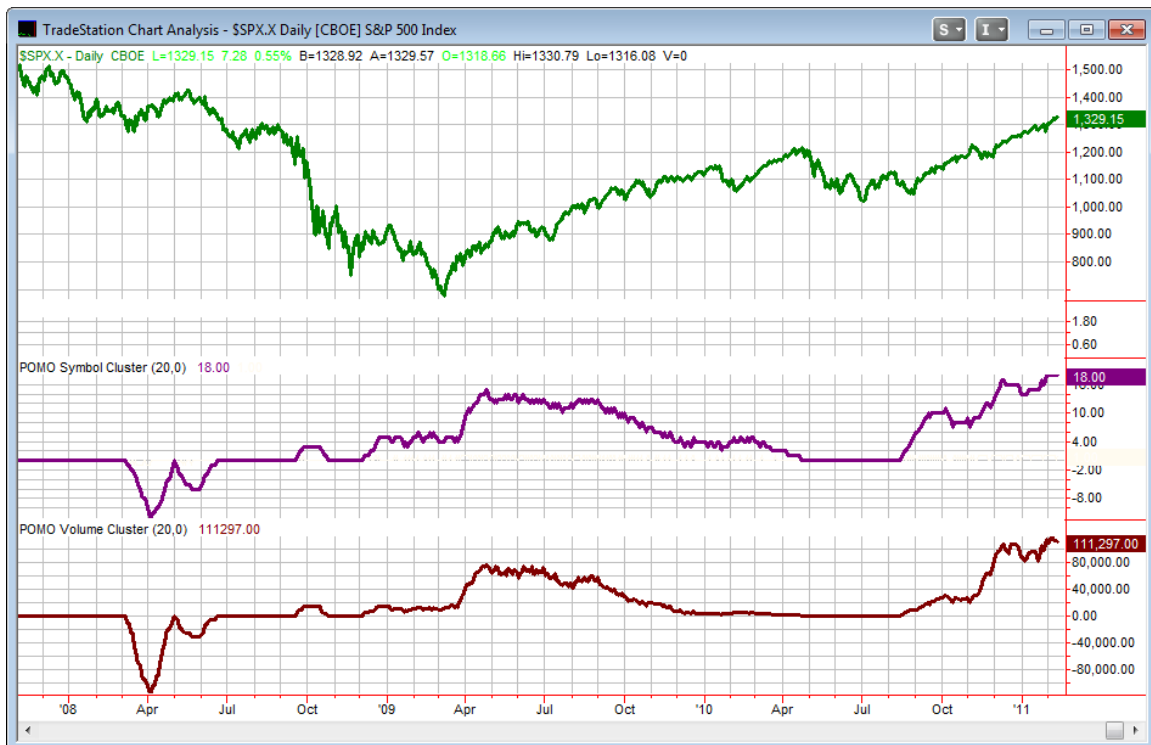
Intermediate-term Outlook (2 weeks – 2 months)– updated 2/14 - bullish

The market continues to make new highs. There can be no doubt we are in an intermediate-term uptrend. And while evidence is mixed, most signs continue to point up.

I've been updating the POMO chart most weekends 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. Information on acquiring the data and constructing the chart can be found in the January 3rd POMO presentation linked below. (Not available for trial users.)

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



POMO levels remain at or near all-time highs. This has almost certainly provided a strong boost to the market. On Thursday the Fed released its tentative operations schedule for the next month. A link to the schedule is below. After eyeballing it, it appears that POMO activity will be extremely strong. Operations are schedule for almost every day, and most days look to have a substantial amount of buying. This should continue to put a nice wind at the market's back.

http://www.newyorkfed.org/markets/tot_operation_schedule.html

Bulls still have POMO, trend, and momentum on their side, while the bears hopes continue to hinge on bond action. Short-term evidence is suggesting a pullback, but there is little suggesting that a pullback would mark the end of the uptrend. I'll continue to side with the bulls. From my standpoint this means I'll trade the long side more aggressively and the short side more conservatively.

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 ¼ index position @ \$134.25 LIMIT. Based on the short-term outlook above.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)(s)	2/17/2011	\$133.85	\$134.25	-0.30%		Aggregator

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