

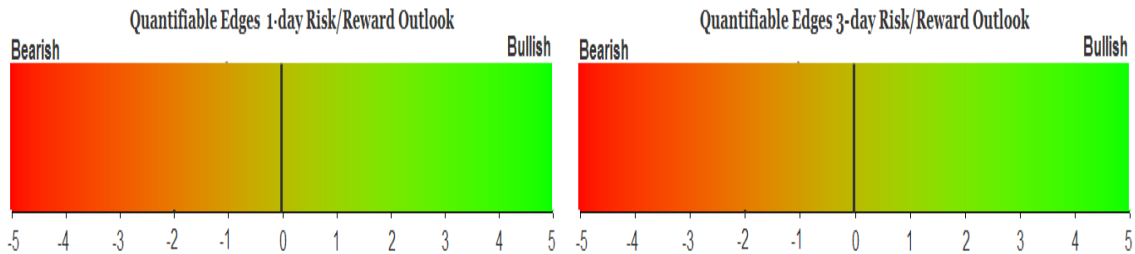
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 1, 2011

Volume 4 Issue 40

## Market Overview



## Tonight's Research Points

- The 1<sup>st</sup> day of the month has generally contained an upside edge. This edge is not apparent March. It is also not apparent when the SPX has just closed higher the last 2 days.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

## Short-term Outlook

### The Bottom Line

Evidence is bullish but the market is still overdone. I'm demanding a more favorable setup before looking stepping back in to an index trade.

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>				
February 28, 2011	Bounce from low still not overbought	1-4 days	Bullish	1.60%
February 25, 2011	3 days dn. Drop slowing.	1-4 days	Bullish	2.00%
February 24, 2011	Down 1.75% and the between .25-.75%	1-5 days	Bullish	
<b>Active - Long Term</b>				
February 23, 2011	From 20 hi to 1st 5low in 10 days.	1-11 days	Bullish	
November 22, 2010	High number of POMO Days recently	int term	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	
<b>Dropped Tonight</b>				
<b>February 25, 2011</b>	<b>SPY gap dn and partial reverse</b>	<b>1-3 days</b>	<b>Bullish</b>	<b>1.50%</b>

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

## The Evidence

Despite being slightly overbought, bullish influences were able to push the market higher on Monday. Large-caps led the way as the SPX gained 0.6%, the NASDAQ gained less than 0.1%, and the Russell 2000 rose 0.2%. Breadth was solidly positive as the NYSE Up Issues % came in at 67% and the Up Volume % was 64%. Total volume rose from Friday's levels and was a bit above average.

Monday's action wasn't particularly telling. Very little appeared in the Quantifinder. One study that did appear examined the bullish seasonal tendency that has been apparent on the first trading day of the month since the mid to late 80s. In the 7/1/09 blog I broke this tendency out by month. March appeared as having one of the three weakest "1<sup>st</sup> day" tendencies - both in terms of net gains and winning percentage.

SPX performance on the 1st day of March. \$100k/trade. 1987 - 2010.			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	\$1,465.91	Profit Factor	1.17
Gross Profit	\$10,011.07	Gross Loss	(\$8,545.16)
Total Number of Trades	24	Percent Profitable	50.00%
Winning Trades	12	Losing Trades	12
Even Trades	0		
Avg. Trade Net Profit	\$61.08	Ratio Avg. Win:Avg. Loss	1.17
Avg. Winning Trade	\$834.26	Avg. Losing Trade	(\$712.10)
Largest Winning Trade	\$2,254.50	Largest Losing Trade	(\$4,660.72)

As you can see, over the last 24 years there hasn't been an edge to speak of. But we know the first day of the month has generally been bullish, so I decided to examine the current setup another way as well. In recent months I've shown how a pullback leading up to the first day of the month (or quarter) has typically served to strengthen first-day tendencies. One example simply looked at first day of month performance if the last two days of the previous month had closed down. The implications in that case appeared especially bullish. But right now the market is at a point where the SPX has instead closed **up** the last two days. I decided tonight to look at this scenario as well.

SPX closes up the last 2 days of the month.  
Buy on close. Sell next day's close. \$100k/trade. 1987 - present.

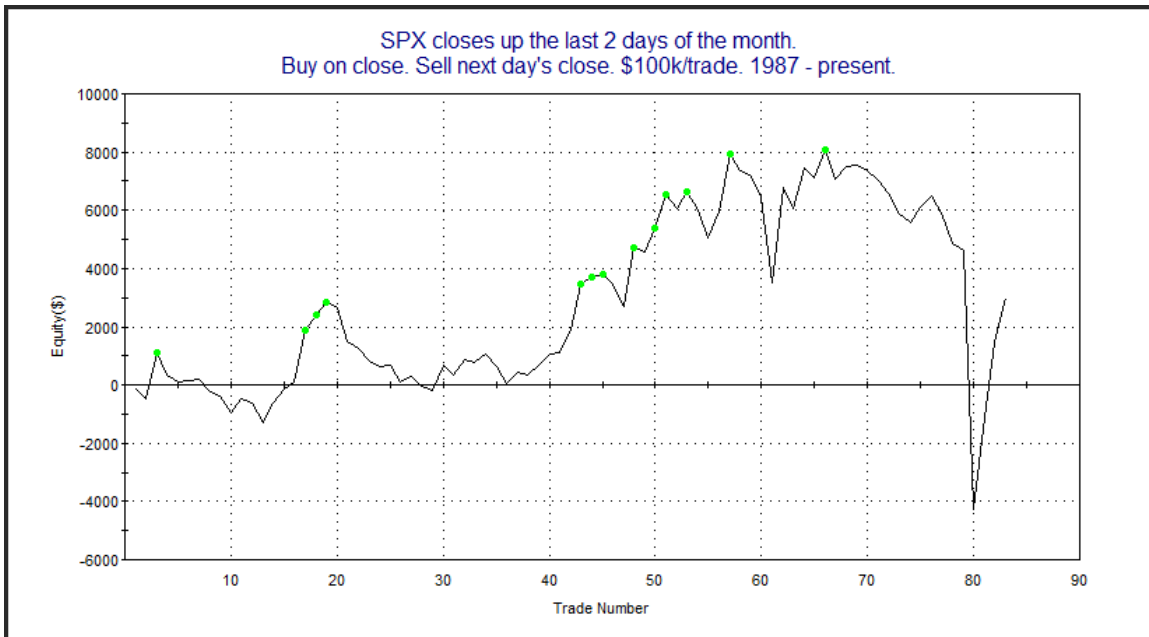
**TradeStation Performance Summary**

[Collapse ^](#)

**All Trades**

Total Net Profit	\$2,975.23	Profit Factor	1.10
Gross Profit	\$33,761.59	Gross Loss	(\$30,786.36)
Total Number of Trades	83	Percent Profitable	46.99%
Winning Trades	39	Losing Trades	44
Even Trades	0		
Avg. Trade Net Profit	\$35.85	Ratio Avg. Win:Avg. Loss	1.24
Avg. Winning Trade	\$865.68	Avg. Losing Trade	(\$699.69)
Largest Winning Trade	\$3,300.73	Largest Losing Trade	(\$8,883.33)

Sample size is ample here. There does not appear to be evidence that any longer supports the bull case when the market is already short-term overbought going in to the 1<sup>st</sup> trading day of the month. Below is an equity curve showing how this setup has evolved over time.



This would seem to confirm the idea that a reliable edge does not exist under these conditions.

Of course the possibility exists that I am getting too fine with this analysis. Perhaps the fact that it is March and the fact that the market is short-term overbought will not matter in the least. The SPX has risen on the 1<sup>st</sup> day of the last 7 months. Perhaps it is that momentum that matters most.

Either way the argument is academic. There are no short-term studies with bearish inclinations at the present. Therefore net expectations are going to be bullish either way.

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



The green Aggregator line is still well above 0. The positive value means the net expectation from the Active Studies List is for upside over the next few days. This is no surprise since all the active short-term studies are bullish. Meanwhile the black Differential line is still squarely negative. Readings below 0 mean the SPX has outperformed expectations over the last few days. So net expectations are for upside but the SPX has outperformed recent expectations. This is considered a neutral configuration. It can be seen on the chart whenever both lines are on opposite sides of zero. Due to this the Aggregator System remained flat at the close.

Based on the current active studies the green Aggregator line is set to remain above 0 on Tuesday. This could change should strong bearish evidence emerge. Meanwhile the Differential Pivot will be at 1,309.55. This is over 1.3% below Monday's close. So for the Differential line to rise back above 0 the SPX would need to drop at least this much.

The Aggregator remains neutral. There do appear to be bullish inclinations still in play tomorrow, regardless of whether you consider the 1<sup>st</sup> day of March to be a positive or not. I would not be at all surprised to see the market extend the rally of the last couple of days. Still, with the SPX short-term overbought, risk/reward is not where I would want it to initiate new positions. I have some long exposure via the Catapult trades, though that will be cut in half at the open. For now I'll wait for a more favorable setup before looking to take on more exposure.

**Intermediate-term Outlook (2 weeks – 2 months)– updated 2/28 - bullish**

This week was the 1<sup>st</sup> in which the SPX failed to make a new high since November. Prior to this it had been 12 straight weeks of higher intraweek highs. I took a look at other times such streaks existed and what happened after they ended.

After making a higher high for at least 12 weeks in a row, SPX fails to do so this week. Buy on close. Sell X weeks later. \$100/trade. 1961 - present.										
X Weeks	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
13	13,100.76	5	5	0	100.00	2,620.15	0.00	100.00	100.00	2,620.15
12	9,579.51	5	4	1	80.00	2,640.27	-981.56	2.69	10.76	1,915.90
11	10,875.23	5	5	0	100.00	2,175.05	0.00	100.00	100.00	2,175.05
10	14,113.96	5	5	0	100.00	2,822.79	0.00	100.00	100.00	2,822.79
9	9,505.39	5	4	1	80.00	2,867.63	-1,965.12	1.46	5.84	1,901.08
8	7,833.41	5	3	2	60.00	3,794.92	-1,775.68	2.14	3.21	1,566.68
7	8,288.25	5	2	3	40.00	5,233.05	-725.95	7.21	4.81	1,657.65
6	2,747.41	5	2	3	40.00	3,065.90	-1,128.13	2.72	1.81	549.48
5	8,325.31	5	3	2	60.00	3,344.10	-853.50	3.92	5.88	1,665.06
4	6,536.42	5	3	2	60.00	2,990.58	-1,217.66	2.46	3.68	1,307.28
3	5,310.43	5	3	2	60.00	2,325.31	-832.75	2.79	4.19	1,062.09
2	537.56	5	1	4	20.00	1,644.98	-276.86	5.94	1.49	107.51
1	2,913.38	5	3	2	60.00	1,534.25	-844.69	1.82	2.72	582.68

**The 5 instances were 11/5/65, 3/17/72, 1/8/93, 8/15/97, and 4/17/98.**

I wouldn't try and draw too much from just 5 instances. Early indications suggest the market is not immune from a short-term pullback, but that past instances have not marked major tops. I decided to also loosen the criteria a bit and see how the results looked.

After making a higher high for at least 10 weeks in a row, SPX fails to do so this week.  
Buy on close. Sell X weeks later. \$100/trade. 1961 - present.

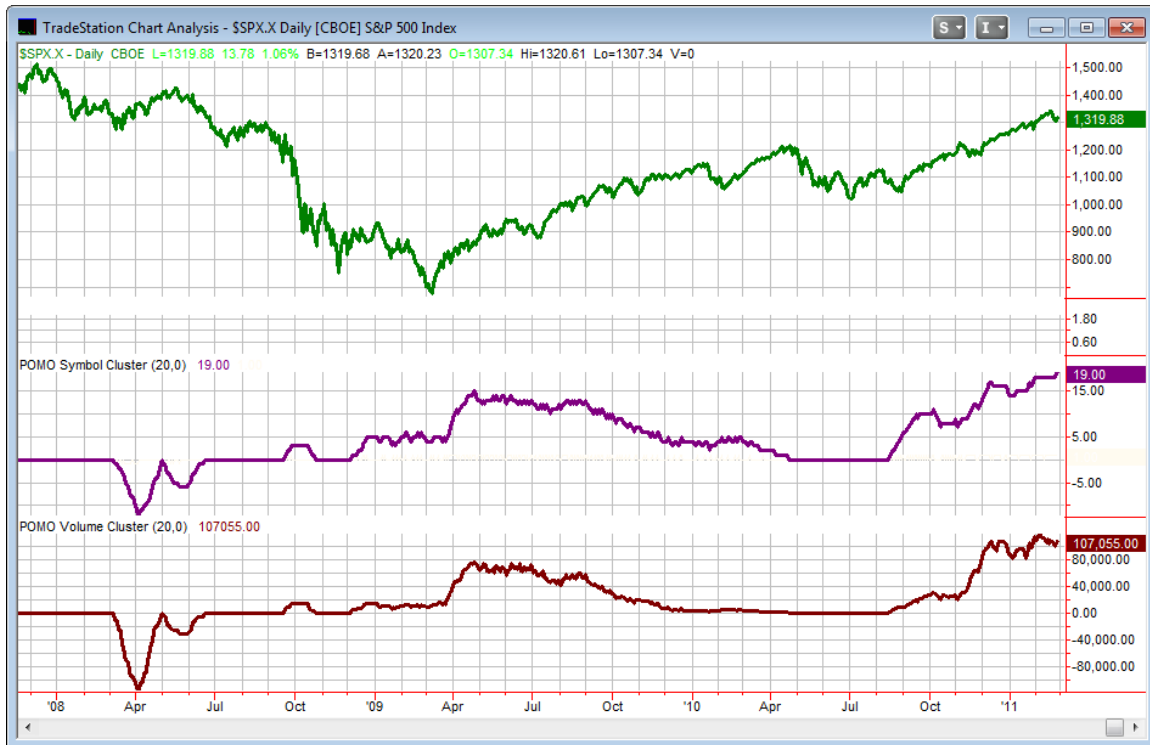
X Weeks	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
13	67,421.97	13	12	1	92.31	5,938.01	-3,834.09	1.55	18.58	5,186.31
12	55,142.15	13	10	3	76.92	5,990.29	-1,586.92	3.77	12.58	4,241.70
11	61,513.42	13	11	2	84.62	5,613.39	-116.93	48.01	264.05	4,731.80
10	57,749.01	13	12	1	92.31	4,871.87	-713.40	6.83	81.95	4,442.23
9	47,972.48	13	10	3	76.92	5,126.18	-1,096.43	4.68	15.58	3,690.19
8	42,950.42	13	9	4	69.23	5,201.66	-966.13	5.38	12.11	3,303.88
7	35,810.03	13	8	5	61.54	5,151.16	-1,079.85	4.77	7.63	2,754.62
6	29,305.82	13	9	4	69.23	3,951.44	-1,564.28	2.53	5.68	2,254.29
5	30,275.76	13	10	3	76.92	3,391.07	-1,211.64	2.80	9.33	2,328.90
4	24,184.17	13	10	3	76.92	2,814.11	-1,318.98	2.13	7.11	1,860.32
3	18,712.83	13	10	3	76.92	2,094.60	-744.38	2.81	9.38	1,439.45
2	7,111.18	13	6	7	46.15	1,970.84	-673.41	2.93	2.51	547.01
1	13,005.40	13	11	2	84.62	1,335.89	-844.69	1.58	8.70	1,000.42

Inclinations don't appear much different based on this table.

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 3<sup>rd</sup> POMO presentation linked below. (Not available for trial users.)*

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



The POMO Days indicator hit a new high on Monday as 19 of the last 20 days have now seen POMO buying. The POMO Volume indicator is also still hovering near all-time highs. POMO activity is expected to remain strong as every one of the next 8 days is scheduled for buying according to the tentative operations schedule. This should continue to put a nice wind at the market's back.

[http://www.newyorkfed.org/markets/tot\\_operation\\_schedule.html](http://www.newyorkfed.org/markets/tot_operation_schedule.html)

Intermediate-term evidence continues to point higher. POMO, trend, momentum, and price patterns all suggest the rally is not over. While the market got a bit of a scare this past week it seems unlikely that this will mark the end of the rally. I still favor a bullish outlook. 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***

*HPQ – buy 1/3 @ \$43.59*

*HPQ – buy 1/3 @ \$42.17*

***Catapult for ETF's Trades***

*None*

## **Broad Market Large Cap CBI – 2 (HPQ-2)**

### **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 am stepping away from looking for a fill on the 2<sup>nd</sup> part of HPQ for now.)*

There is quite a bit more on the triggers page tonight.

### **Current Open Trade Ideas**

<b>Symbol</b>	<b>Entry Date</b>	<b>Entry Price</b>	<b>Current Price</b>	<b>% Gain/Loss</b>	<b>Stop</b>	<b>Notes</b>
SPY(1/4)	2/24/2011	\$130.00	\$132.82	2.17%		sold on open
GE(1/3)	2/24/2011	\$20.12	\$20.92	3.98%		sell on open
HPQ (1/3)	2/24/2011	\$43.16	\$43.63	1.09%		Catapult

GE should be sold on the open Tuesday.

SPY was sold at the open on Monday.

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