

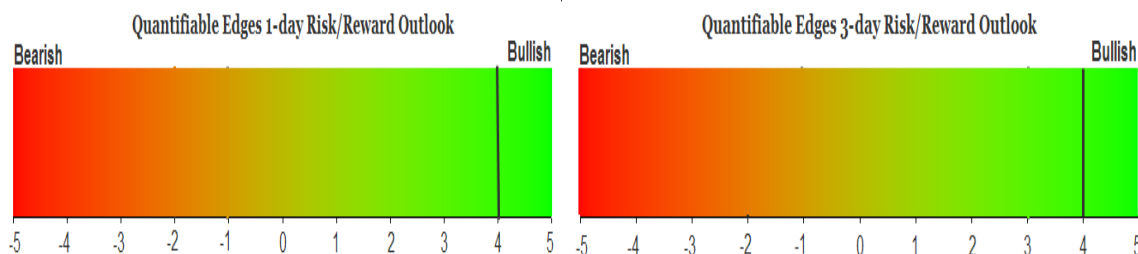
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 17, 2011

Volume 4 Issue 52

Market Overview



Tonight's Research Points

- 5 Lower lows and a 50-day low suggest an upside edge – except above the 200ma.
- Breadth continues to register extremes suggesting a bounce.
- The VIX spike 20% today and is now 35% above its 10ma – both of which suggest a short, immediate bounce.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

News has dominated and historical norms have been run over. Still, probabilities strongly suggest a bounce is coming very soon. I'm holding long and even adding a little more exposure via Catapults to take advantage of that bounce.

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				
March 17, 2011	VIX up 25% & more than 25% > 10ma	1-2 days	Bullish	
March 16, 2011	5 Gaps Down	1-3 days	Bullish	
March 16, 2011	2 Unfilled Down Gaps > 200ma	1-5 days	Bullish	
March 16, 2011	McClellan 50-day Bounded Low 4 days	1-5 days	Bullish	
March 16, 2011	SPY 1% > open but down on day	1-2 days	Bullish	
March 16, 2011	VIX 100-high. SPX no 100-low	1-6 days	Bullish	
March 14, 2011	Sweet spot bounce	1-5 days	Bullish	3.10%
March 14, 2011	Outside day frm sh-term low in uptrend	1-6 days	Bullish	2.00%
March 14, 2011	March Op-ex Week	1-4 days	Bullish	1.70%
March 11, 2011	20-day low. High vol. Lrg drop. >200.	1-7 days	Bullish	2.65%
Active - Long Term				
November 22, 2010	High number of POMO Days recently	int term	Bullish	
October 25, 2010	SPX Golden Cross	int term	Bullish	
Dropped Tonight				
March 11, 2011	Triangle Breakdown > 200ma	3-4 weeks	Bullish	
March 2, 2011	Outside 2 days and 3-day low close	4-10 days	Bullish	

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

The Evidence

Bad news continues to reign supreme. And despite numerous indications that the market is (and has been) primed for a bounce, the bad news continues to scare participants, causing the market to tumble. On Wednesday the SPX dropped nearly 2.0%, the Nasdaq was down 1.8% and the Russell 2000 fell 1.2%. Breadth was extremely weak as the NYSE Up Issues % came in at 23% and the Up Volume % was 9%. Total NYSE volume spiked to the highest level of 2011.

Several studies again triggered Wednesday afternoon. They all suggested in one way or another that the market is severely oversold and a sharp bounce is highly probable. On the whole I didn't find today's studies to be as compelling as the ones I showed in last night's letter. The most compelling studies tonight involved the VIX. I will get to those a little lower down. There are a few others I would like to discuss first.

This first one was from the 5/18/09 Subscriber Letter. It looked at other times the SPX made five consecutive lower lows and a 50-day low. Results are updated.

SPX makes 5 lower lows and today is the lowest low of the last 50 days.
Buy on close. Sell X days later. \$100k/trade. 1978 - 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	104,473.83	29	21	8	72.41	6,170.08	-3,137.24	1.97	5.16	3,602.55
19	116,403.77	30	24	6	80.00	5,841.51	-3,965.43	1.47	5.89	3,880.13
18	107,953.15	30	23	7	76.67	5,773.03	-3,546.64	1.63	5.35	3,598.44
17	103,444.87	30	23	7	76.67	5,482.68	-3,236.68	1.69	5.57	3,448.16
16	94,501.02	30	23	7	76.67	4,986.25	-2,883.25	1.73	5.68	3,150.03
15	74,791.62	30	21	9	70.00	4,903.92	-3,132.30	1.57	3.65	2,493.05
14	71,822.39	30	20	10	66.67	5,006.95	-2,831.66	1.77	3.54	2,394.08
13	52,720.59	30	20	10	66.67	4,868.24	-4,464.43	1.09	2.18	1,757.35
12	58,553.77	30	19	11	63.33	5,123.59	-3,526.77	1.45	2.51	1,951.79
11	42,357.13	30	19	11	63.33	3,957.55	-2,985.12	1.33	2.29	1,411.90
10	50,412.53	30	18	12	60.00	4,713.87	-2,869.77	1.64	2.46	1,680.42
9	57,349.29	30	20	10	66.67	3,987.05	-2,239.17	1.78	3.56	1,911.64
8	51,181.77	30	18	12	60.00	4,429.46	-2,379.04	1.86	2.79	1,706.06
7	49,855.64	30	19	11	63.33	3,904.30	-2,211.46	1.77	3.05	1,661.85
6	34,759.58	30	19	11	63.33	3,347.82	-2,622.63	1.28	2.20	1,158.65
5	20,942.99	30	18	12	60.00	2,901.67	-2,607.25	1.11	1.67	698.10
4	39,344.61	30	20	10	66.67	3,334.35	-2,734.23	1.22	2.44	1,311.49
3	39,996.84	30	18	12	60.00	3,113.01	-1,336.45	2.33	3.49	1,333.23
2	29,484.54	30	19	11	63.33	2,624.12	-1,852.16	1.42	2.45	982.82
1	29,829.66	30	19	11	63.33	2,285.85	-1,236.51	1.85	3.19	994.32

This study appears to be suggestive of a bounce in both the short and intermediate-term. What is unusual about the current situation though, is that while we are at a 50-day low the SPX is still above its 200ma. I decided to peek and see how other instances fared with the 200ma filter applied.

SPX makes 5 lower lows and today is the lowest low of the last 50 days. Close > 200ma.
Buy on close. Sell X days later. \$100k/trade. 1978 - present.

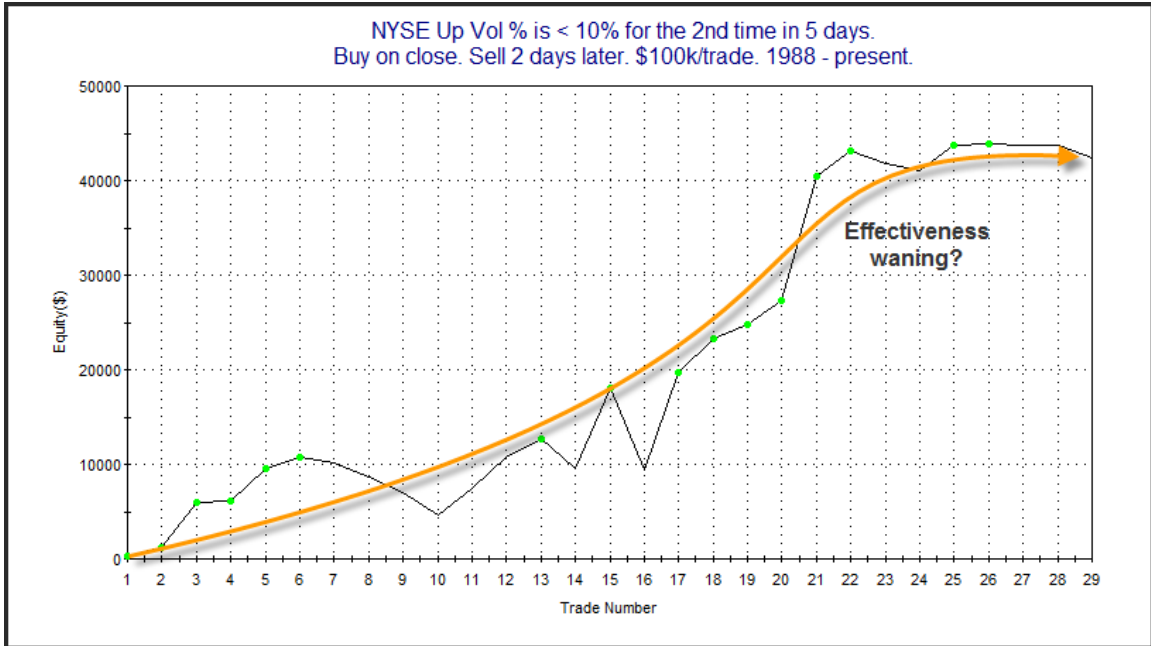
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	-4,724.19	4	1	3	25.00	1,784.86	-2,169.68	0.82	0.27	-1,181.05
9	-3,859.24	4	1	3	25.00	613.13	-1,490.79	0.41	0.14	-964.81
8	-10,621.42	4	0	4	0.00	0.00	-2,655.36	0.00	0.00	-2,655.36
7	-6,579.40	4	1	3	25.00	1,579.86	-2,719.75	0.58	0.19	-1,644.85
6	-4,455.24	4	2	2	50.00	640.43	-2,868.05	0.22	0.22	-1,113.81
5	-3,006.37	4	1	3	25.00	1,395.17	-1,467.18	0.95	0.32	-751.59
4	-3,401.53	4	1	3	25.00	2,129.33	-1,843.62	1.15	0.38	-850.38
3	-1,200.48	4	1	3	25.00	1,597.33	-932.60	1.71	0.57	-300.12
2	-2,220.19	4	1	3	25.00	1,036.07	-1,085.42	0.95	0.32	-555.05
1	-2,695.29	4	1	3	25.00	27.93	-907.74	0.03	0.01	-673.82

It's important to keep in mind that there are only four instances here. Solid conclusions cannot be drawn from four instances. The fact that they struggled so much does suggest to me that perhaps the conclusions drawn from the first study may not be accurate. This second study does not suggest a bearish edge, but it does incite me to ignore the first study.

Another interesting study from the 6/25/10 Subscriber Letter examined the fact that today was the second 90% down volume day in a week. I have updated that study below.

NYSE Up Vol % is < 10% for the 2nd time in 5 days. 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	59,133.77	24	16	8	66.67	4,331.56	-1,271.40	3.41	6.81	2,463.91	
4	41,432.96	25	18	7	72.00	3,414.33	-2,860.71	1.19	3.07	1,657.32	
3	24,277.00	26	15	11	57.69	3,305.13	-2,299.99	1.44	1.96	933.73	
2	42,425.78	29	19	10	65.52	3,370.60	-2,161.56	1.56	2.96	1,462.96	
1	35,177.46	29	18	11	62.07	2,523.15	-930.84	2.71	4.44	1,213.02	
93% of instances closed above the entry price at some point in the next week.											

Results here seem to suggest a short-term upside edge. Much of the edge is realized in the first 2 days. My initial reaction to these results was not to make a fuss over them since I showed a similar oversold breadth study last night that used the McClellan Oscillator. In any case I decided to take a peek at the equity curve using a two day exit strategy. What I saw is below.



While the edge appeared strong for quite some time, the last eight or nine instances really haven't added anything. The chart suggests to me that the edge may be waning. I'm not incorporating this study in the Aggregator tonight either.

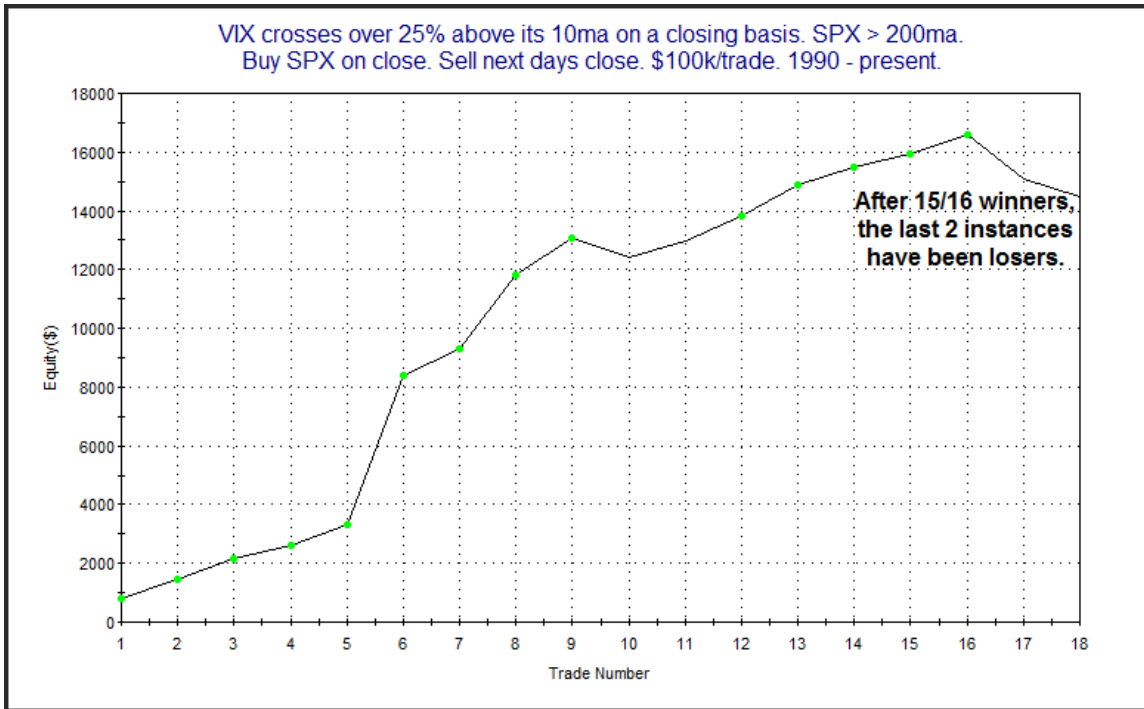
There were two VIX-related studies that I did find compelling. This first one below was from the 5/5/10 subscriber letter. It examined other times the VIX got stretched more than 25% above its 10ma while the SPX was above its 200ma.

VIX crosses over 25% above its 10ma on a closing basis. SPX > 200ma.
Buy SPX 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
6	22,533.80	18	13	5	72.22	2,092.88	-934.72	2.24	5.82	1,251.88
5	17,199.06	18	10	8	55.56	2,529.57	-1,012.08	2.50	3.12	955.50
4	24,529.95	18	13	5	72.22	2,222.36	-872.16	2.55	6.63	1,362.78
3	17,603.81	18	15	3	83.33	1,344.31	-853.62	1.57	7.87	977.99
2	19,740.64	18	13	5	72.22	1,692.69	-452.86	3.74	9.72	1,096.70
1	14,472.96	18	15	3	83.33	1,151.17	-931.53	1.24	6.18	804.05

17 of 18 instances posted a close above the entry price within the next 3 days. All 18 did within 6 days.

Implications here appear strongly bullish, but really only for a day or two. An equity curve is shown below.



The two recent failures are somewhat concerning, but at this point the edge still appears intact.

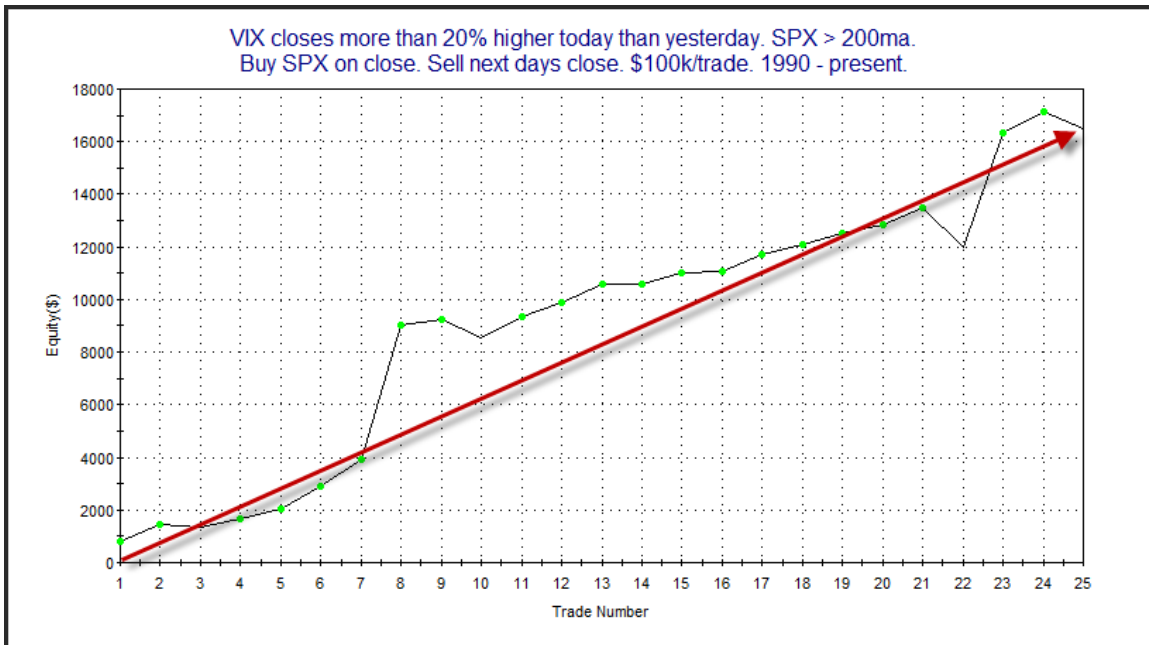
This last study also looked at today's VIX action. It was last seen in the 1/31/11 subscriber letter. I have updated this one as well.

VIX closes more than 20% higher today than yesterday. SPX > 200ma.
Buy SPX 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	29,598.89	20	15	5	75.00	2,436.40	-1,389.42	1.75	5.26	1,479.94
9	29,365.50	22	16	6	72.73	2,431.99	-1,591.06	1.53	4.08	1,334.80
8	32,707.04	24	18	6	75.00	2,446.62	-1,888.69	1.30	3.89	1,362.79
7	33,810.07	24	19	5	79.17	2,364.94	-2,224.74	1.06	4.04	1,408.75
6	31,057.15	24	16	8	66.67	2,507.85	-1,133.56	2.21	4.42	1,294.05
5	22,771.76	24	16	8	66.67	2,117.83	-1,389.18	1.52	3.05	948.82
4	20,200.48	24	17	7	70.83	1,757.68	-1,382.87	1.27	3.09	841.69
3	20,154.43	24	20	4	83.33	1,226.03	-1,091.57	1.12	5.62	839.77
2	22,267.33	24	16	8	66.67	1,606.38	-429.34	3.74	7.48	927.81
1	16,503.68	25	21	4	84.00	925.54	-733.15	1.26	6.63	660.15

The only instance NOT to close above the entry price at some point in the next 3 days triggered on 5/17/06.

From a consistency standpoint these appear to be the best results of all. An equity curve can be found below.



This equity curve also appears compelling and serves to confirm the numbers in the table. I have taken the VIX studies under consideration with regards to the Aggregator.

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



The green Aggregator line is again very strongly above 0. The positive value means the net expectation from the Active Studies List is for upside over the next few days. As has been the case lately, all the active short-term studies remain bullish. Meanwhile the black Differential line is now extremely stretched. Readings above 0 mean the SPX has underperformed expectations over the last few days. So net expectations are for upside and the SPX is more oversold than it has been in a long time. Historically this combination has provided an upside edge. It can be seen on the chart whenever both lines are above zero. Due to this the Aggregator System remained long at the close.

Based on the current active studies the green Aggregator line is set to stay above 0 on Thursday. This could change should strong bearish evidence emerge. Meanwhile, the Differential Pivot will be 1,307.17. This is about 4% above Wednesday's close. This all means that it is highly unlikely the Aggregator long signal will close tomorrow. It is now looking for a multi-day bounce.

I'm quite long at the moment in anticipation of this bounce. As you'll see below 4 new Catapults triggered. I am looking to enter them. I am not looking to put on the last part of my SPY position just yet. The CBI is now 8, and I would like it to be at 10 or higher before going "all in". This most likely would happen if we get another down day tomorrow.

Fear is not only palpable when looking at the sharpness of the intraday selloffs or the VIX, but I have also heard from many traders and subscribers who are deeply concerned about the selloff. Often times the most difficult trades are the ones that end a nice winning streak. Even with a solid bounce from here there's a decent chance that many of the current trade ideas will finish in the red. But let's not lose perspective on the long term, and let's also not lose perspective on the present. It's very easy to get emotional when your position is going against you. This is especially true when the TV is constantly discussing dire news stories and the market is suffering multiple down days. From a personal standpoint, I have endured selloffs far worse than what has occurred in the last week or so. Even so, I too feel frustration and anxiety when watching my position go against me and seeing the things going on in the world.

It's very important not to make rash decisions on positions. This means don't get scared out of them and don't get sucked in to taking on too much leverage because you're trying to make up for unrealized losses. I make most of my decisions at night. Rarely will I adjust a large position during the day unless I have already thought it through the night before. For me the nightly research is cleansing and allows me the opportunity to step back and take an objective view of the market each and every night while it is closed. By doing so I am able to devise and execute a plan with a clear head and in an optimal manner. I would strongly suggest to all traders that they have a plan each day before they go into the day, and that they follow that plan. By trading with a clear head you will be able to maintain a more objective perspective.

And while the present selloff and situation "feels" tough, the actual damage to this point isn't that large. Even if someone were to trade the Aggregator System using an "all in" methodology, the current signal was only down 4% as of Wednesday's close. Obviously I expect the trade will close out better than a 4% loss (or I wouldn't still be in it), but even if it falls farther from here and ends up bouncing back and closing out with a 4% loss, that still isn't a huge loser. It's a loss that could be overcome with just a couple of good trades. It's frustrating to have profits eaten into and it's frustrating to suffer drawdown, but dealing with drawdown is just part of trading. So if you're feeling "stuck long", don't despair. Trade consistently and with an edge and in the long run you'll be fine.

Intermediate-term Outlook (2 weeks – 2 months)– updated 3/14 - bullish

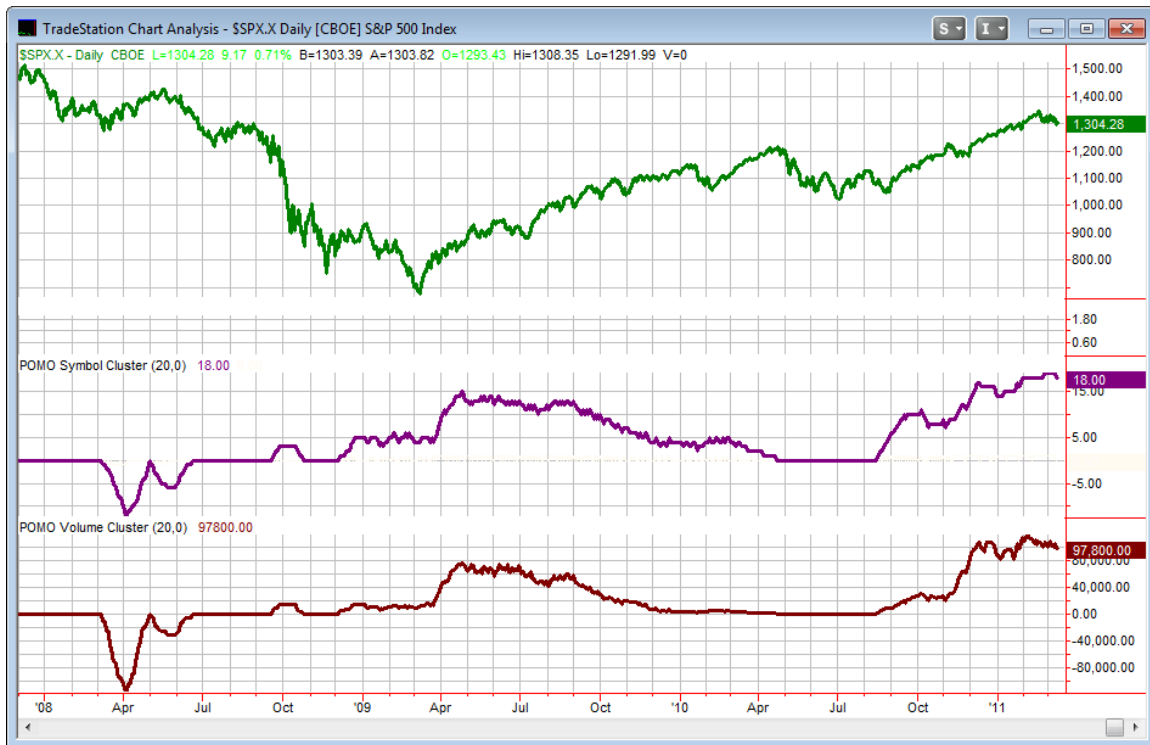
It was a difficult week for the market. From a technical standpoint the big news was the triangle breakdown on Thursday. This was seen by many as a potential topping event indicating further selling. This is not what my research showed though. The triangle breakdown study I published Thursday night suggested a strong intermediate-term upside

bias. All (non-trial) subscribers can find the triangle studies, as well some additional performance reports and Tradestation code in the [downloads section of the website](#).

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>



The POMO Days indicator is still extremely elevated at 18. The Fed released the new tentative operations schedule on Thursday. It doesn't appear quite as busy as the last couple of months but there is still buying scheduled for around 4 days per week. This upcoming week Tuesday is the only non-POMO day. The POMO Volume indicator has dipped a little bit but is still at a very elevated level, with plenty of money having gone in to the system over the last month. I expect POMO to continue to provide a steady wind at the market's back. For those that would like to view the upcoming schedule I have provided a link below.

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

I still feel odds favor a continued rise over the next several weeks. POMO, trend, momentum, and price patterns (including the new triangle breakdown study) all suggest the rally is not over. There also continues to be a complete lack of intermediate-term bearish evidence. Due to this, 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 – 1/3 @ \$43.59

HPQ – 1/3 @ \$42.17

XOM – 1/3 @ \$81.31

CSCO – 1/3 @ \$17.39

NEW

MO – 1/3 @ \$24.29

PM – 1/3 @ \$61.87

CSCO – 1/3 @ \$17.05 (2nd lot)

PG – 1/3 @ \$59.73

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 3 (HPQ-2, XOM)

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.

I'll be looking to enter the following Catapults (all 1/3 positions size) at the limits listed:

MO – 1/3 @ \$24.29

PM – 1/3 @ \$61.87

CSCO – 1/3 @ \$17.05

PG – 1/3 @ \$59.73

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
HPQ (1/3)	2/24/2011	\$43.16	\$40.14	-7.00%		Catapult
SPY(1/4)	3/8/2011	\$131.43	\$126.18	-3.99%		Aggregator
SPY(1/4)	3/11/2011	\$129.52	\$126.18	-2.58%		Aggregator
HPQ (1/3)	3/11/2011	\$41.42	\$40.14	-3.09%		Catapult
XOM(1/3)	3/11/2011	\$81.02	\$79.31	-2.11%		Catapult
SPY(1/4)	3/16/2011	\$128.15	\$126.18	-1.54%		Aggregator
CSCO(1/3)	3/16/2011	\$17.33	\$17.05	-1.62%		Catapult

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