

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 26, 2011

Volume 4 Issue 79

Market Overview



Tonight's Research Points

- The very-low volume in an uptrend is not encouraging for the bulls.
- The after multiple higher highs, lows, and closes, a close-only pullback is often followed by a rise in prices.
- The Aggregator System is flat.
- The NDX Aggressive Trend Timer is flat.

Short-term Outlook

The Bottom Line

The Aggregator is neutral tonight but could easily turn bullish tomorrow as long as we don't close stretched at a new high. Wednesday being a Fed Day provides more bullish fuel. I may look to add some long exposure on Tuesday.

Summary of Recent Active Studies (see Letters from listed dates for details)

Study Date	Description	Time span	Bias	Avg Max Move
Active				
April 26, 2011	Low vol 20. SPX >10ma & 2--ma.	1-2 days	Bearish	-1.10%
April 26, 2011	3 higher highs, lows, closes. Dn close.	1-4 days	Bullish	1.40%
April 25, 2011	VIX < lower BB 2 in a row. SPX >200ma	1-2 days	Bearish	-1.05%
April 21, 2011	Unfilled gap up. 2nd day up. No 10 high	1-3 days	Bullish	
April 20, 2011	WR7 Down High Vol then NR7	1-5 days	Bullish	2.10%
April 19, 2011	1% drop & decliners double advancers	1-9 days	Bullish	3.00%
Active - Long Term				
April 25, 2011	Nas/SPX relative strength favors Nas	int term	Bullish	
April 11, 2011	QQQ 5 lower lows. Today worst day.	1-20 days	Bullish	13.00%
March 22, 2011	3 Days Up Issues % > 70%	int term	Bullish	19.00%
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.

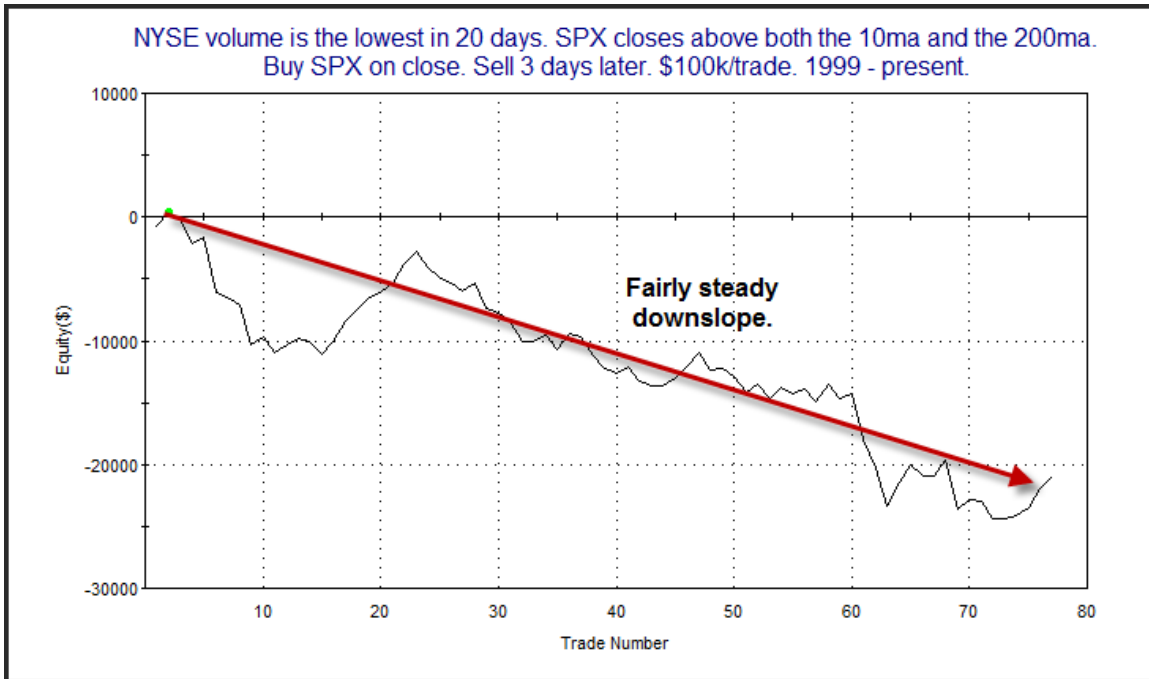
The Evidence

Monday was very quiet. The indices finished mixed as prices barely moved. The SPX and Russell 2000 each declined 0.2% while the Nasdaq rose 0.2%. Breadth was somewhat weak as the NYSE Up Issues % came in at 46% and the Up Volume % was 39%. Total NYSE volume came in at the lowest level in a few months.

Studies are mixed based on Monday's action. On the negative side, the low volume is not encouraging. The study below was last seen in the 10/25/10 Subscriber Letter and triggered again on Monday. I have updated the stats.

NYSE volume is the lowest in 20 days. SPX closes above both the 10ma and the 200ma. Buy SPX on close. Sell X days later. \$100k/trade. 1999 - 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	-14,367.42	69	35	34	50.72	1,201.20	-1,659.10	0.72	0.75	-208.22
4	-18,405.96	75	39	36	52.00	839.41	-1,420.64	0.59	0.64	-245.41
3	-20,901.69	77	36	41	46.75	836.32	-1,244.12	0.67	0.59	-271.45
2	-17,726.94	82	39	43	47.56	694.73	-1,042.36	0.67	0.60	-216.18
1	-6,031.08	99	55	44	55.56	462.76	-715.52	0.65	0.81	-60.92

The numbers suggest a possible bearish edge over the first 1-3 days. Below is an equity curve using a 3-day exit strategy.



The steady downslope is pretty impressive considering the setup includes a long-term uptrend filter. This study appears worthy of inclusion on the Active List.

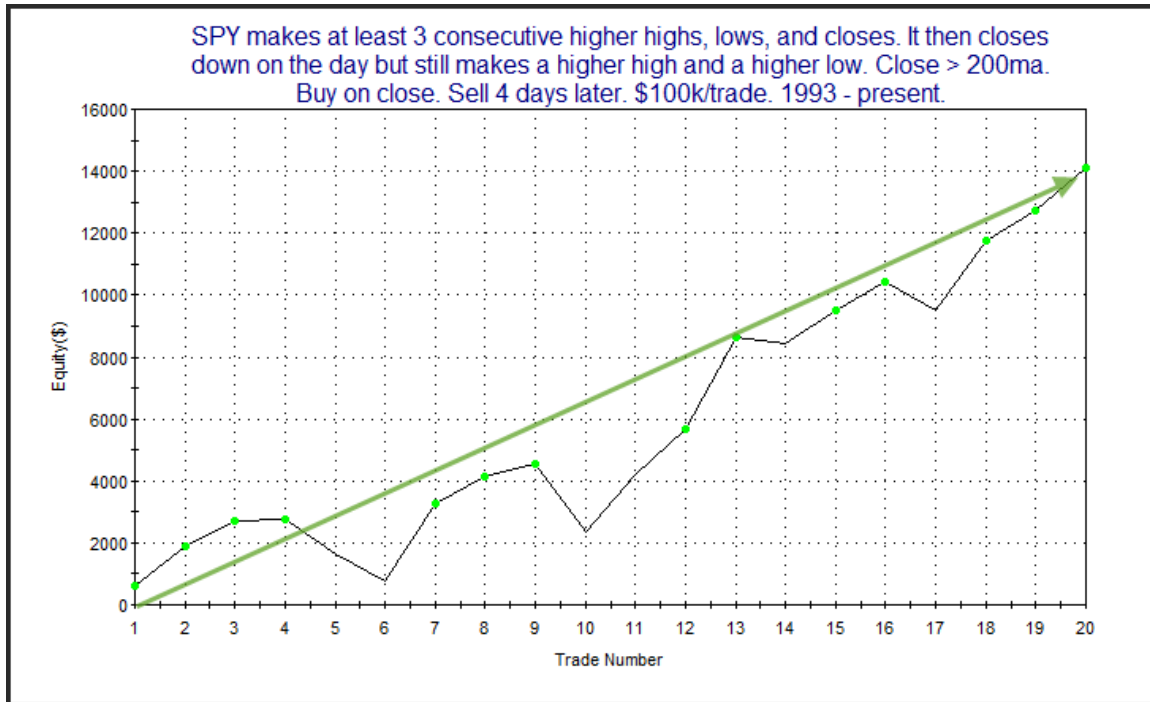
But while volume action is a little discouraging, price action over the last few days looks positive. After making a series of higher highs, lows, and closes, SPY closed lower today but still managed to make a higher high and higher low. This is a pattern I last looked at in the 12/7/10 Subscriber Letter. I updated that study again tonight.

SPY makes at least 3 consecutive higher highs, lows, and closes. It then closes down on the day but still makes a higher high and a higher low. Close > 200ma.
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	10,559.51	20	13	7	65.00	1,441.49	-1,168.55	1.23	2.29	527.98
4	14,115.41	20	15	5	75.00	1,294.87	-1,061.53	1.22	3.66	705.77
3	7,141.75	20	14	6	70.00	952.41	-1,032.00	0.92	2.15	357.09
2	5,021.92	20	16	4	80.00	618.26	-1,217.55	0.51	2.03	251.10
1	3,364.70	20	12	8	60.00	508.10	-341.56	1.49	2.23	168.24

18 of 20 instances (90%) posted a close above the entry price at some point in the next 4 days.

The stats appear strongly bullish. The bullish momentum seems to carry through on a regular basis. Below is an equity curve using a 4-day exit.



The persistent upslope acts as confirmation of the bullish edge.

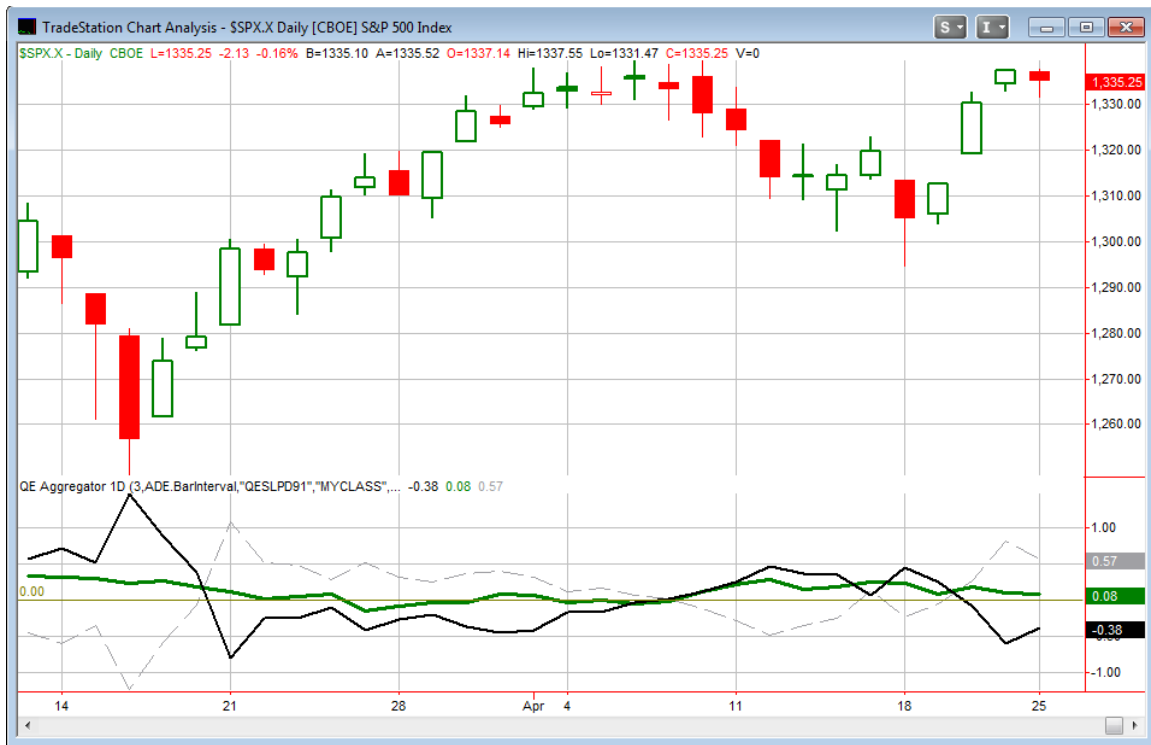
It is also worth keeping in mind that Wednesday is a Fed announcement day. In the past I have published a lot of work on Fed Days. You can find a good number of studies on the blog using the below link.

<http://quantifiableedges.blogspot.com/search/label/Fed%20Study>

For a more complete look at Fed Day edges there is the [Quantifiable Edges Guide to Fed Days](#). A big determinate in how a Fed Day performs is market action on the day before a Fed Day. Here are a few of things to consider tomorrow. For one, Fed Days that occur immediately after a 20-day high have not shown the bullish propensity that occur without a 20-day high immediately preceding. Second, where the SPY closes within its daily range has greatly influenced the magnitude of the Fed Day edge. In general, the worse the close the more pronounced the upside edge for the Fed Day. Third, the upside Fed

Day inclination is apparent from the close of the day before up until announcement time. After the announcement has been made around 2:15, performance has been much more random.

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



The green Aggregator line barely budged tonight and remains well 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 still below 0. Readings below 0 mean the SPX has outperformed expectations over the last few days. So net expectations are for upside but the SPX is already overbought. This is considered a neutral configuration. A neutral configuration is visible on the chart whenever the green Aggregator and black Differential lines finish on opposite sides of zero. Due to this the Aggregator System remained flat.

The green Aggregator line is again set to close above 0 on Monday. This could change if more bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,337.09. This is about 0.2% above Monday's close. So unless the market rises at least this much on Tuesday the black Differential line will turn positive.

I will sometimes play Fed Day edges even without a supporting Aggregator. If the SPX closes below the Differential Pivot tomorrow then it seems likely that the Aggregator System could trigger a long. In any case, I'll look to take advantage of Wednesday's Fed Day as long as the SPX closes below the Differential Pivot (and a 20-day high) and in the bottom half of its daily range. Details in the Trade Ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 4/25 – bullish

After 2 down weeks the market made some nice gains this past week. One encouraging sign in addition to prices rising is that the Nasdaq is now taking leadership back over from the SPX. For relative strength I use a 10-week measure. The chart below is updated each week on the charts page. Detailed write-ups for those who would like a refresher may be found using the following links.

<http://quantifiableedges.blogspot.com/2009/05/simple-powerful-timing-indicator.html>

<http://quantifiableedges.blogspot.com/2009/06/tweaking-nasdaq-leadlag-model.html>



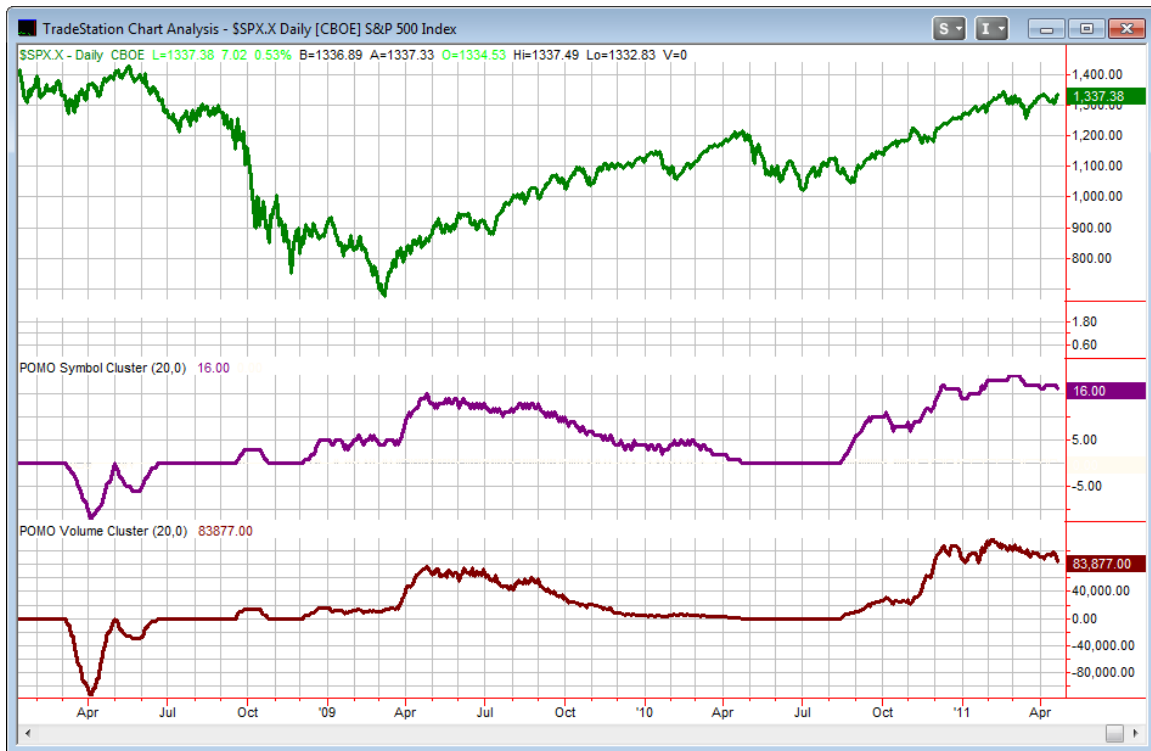
The basic idea is that the market tends to perform better when the Nasdaq leads the SPX. Historically, the SPX has made its money when the Nasdaq has been in leading position,

and struggled to make headway when the Nasdaq has lagged. Looking at the action over the recent 11 months or so in the above chart, you can see this tendency has generally held true. Therefore, I view the Nasdaq's recent leadership as an intermediate-term positive.

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 indicators have pulled back a little recently. The days indicator is at 16 and the POMO Volume indicator is down near the low end of its recent range. The schedule calls for buying every day this week except for Wednesday. And the 1st week in May there is buying scheduled every day. So with 9 of the next 10 days scheduled for buying I don't expect to see these indicators drift lower. I instead expect POMO to continue to act as a wind at the markets back. Monitoring POMO activity and news will become increasingly important as we near the end of the QE2 stimulus in June.

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

There is still a decided lack of intermediate-term bearish studies. Meanwhile, momentum, POMO activity, breadth, relative strength, and QQQ price action are all pointing higher. I remain intermediate-term bullish. For my own trading this means I will be more inclined to take bullish setups more aggressively and bearish setups 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 – buy ¼ index position on close if SPX closes < 1,337.10 and SPY closes in the bottom half of its daily range. Based on a combination of Fed Day edges and the Aggregator. I may look to exit this trade prior to the 2:15pm announcement on Wednesday.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
EPP	4/19/2011	\$48.85	\$50.59	3.56%		System 90609

EPP is nowhere near an exit based on system 90609.

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