

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 10, 2011

Volume 4 Issue 89

Market Overview



Tonight's Research Points

- The low SPX volume does not appear to be much of a concern.
- SPY up 2 days but still below the close of 3 days ago appears to provide a bullish edge.
- The Aggregator System is long.
- The NDX Aggressive Trend Timer is long.

Short-term Outlook

The Bottom Line

This bounce looks like it has further to go. I'm long but will clean house if we get another up day tomorrow.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
May 10, 2011	SPY up 2x but below 3 days ago	1-2 days	Bullish	1.00%
May 9, 2011	VIX up. SPX up on Fri.	1-3 days	Bearish	-1.30%
May 6, 2011	Down 4 days. Today's is the worst.	1-5 days	Bullish	2.10%
May 5, 2011	SPY 1st 5-day low in 10 days	1-4 days	Bullish	1.60%
May 2, 2011	SPX > Upper BB 4 days	1-8 days	Bullish	1.90%
Active - Long Term				
May 2, 2011	SPY up 3 days all lower volume	1-19 days	Bearish	
April 25, 2011	Nas/SPX relative strength favors Nas	int term	Bullish	
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	
Dropped Tonight				
May 9, 2011	Down 4 days. Then weak bounce	1 day	Bullish	

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

The Evidence

After a tight morning consolidation the market broke higher around noon. The rally lasted less than half an hour and then it formed another tight range for the rest of the day. The SPX finished up 0.5%, the Nasdaq rose 0.6%, and the Russell 2000 led the way with a 1.1% gain. Breadth was solidly positive as the NYSE Up Issues % and Up Volume % both came in at 68%. Total NYSE volume dipped to the lowest level in about 2 weeks. Part of the volume dip can be attributed to the large reverse split in Citigroup. It was the highest volume stock on the NYSE prior to the split, but now the same dollar volume is 10x less shares thanks to the 1 for 10 reverse split.

There was one volume-related study that appeared in the Quantifinder tonight. It looked at NYSE volume 2-week lows occurring on SPX up days and was last published in the 2/2/10 Subscriber Letter. While, I was a little hesitant to worry much about volume today I decided to take a closer look. But rather than just rerun the old test I decided to include a 200ma filter. Those updated results are below.

SPX closes higher on lightest NYSE volume in 10 days. Close > 200ma. Buy 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	-4,313.40	105	56	49	53.33	1,481.48	-1,781.15	0.83	0.95	-41.08
4	1,594.21	109	58	51	53.21	1,284.16	-1,429.16	0.90	1.02	14.63
3	-15,383.13	115	61	54	53.04	1,053.87	-1,475.36	0.71	0.81	-133.77
2	-7,245.92	121	60	61	49.59	881.57	-985.91	0.89	0.88	-59.88
1	-7,509.89	137	69	68	50.36	580.08	-699.05	0.83	0.84	-54.82

The original study showed what appeared to be a mild downside edge. These results are even less compelling. There still may be a downside edge, but it is hardly strong enough to make it worth pursuing. But what if I also require that yesterday saw the SPX close up as well?

SPX closes higher on lightest NYSE volume in 10 days. It also closed higher yesterday.
Close > 200ma. Buy 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	13,163.21	60	35	25	58.33	1,367.10	-1,387.41	0.99	1.38	219.39
4	10,501.08	60	36	24	60.00	1,125.64	-1,250.91	0.90	1.35	175.02
3	9,866.41	60	38	22	63.33	1,016.22	-1,306.82	0.78	1.34	164.44
2	-655.59	64	34	30	53.13	916.01	-1,060.00	0.86	0.98	-10.24
1	-232.72	74	38	36	51.35	540.78	-577.29	0.94	0.99	-3.14

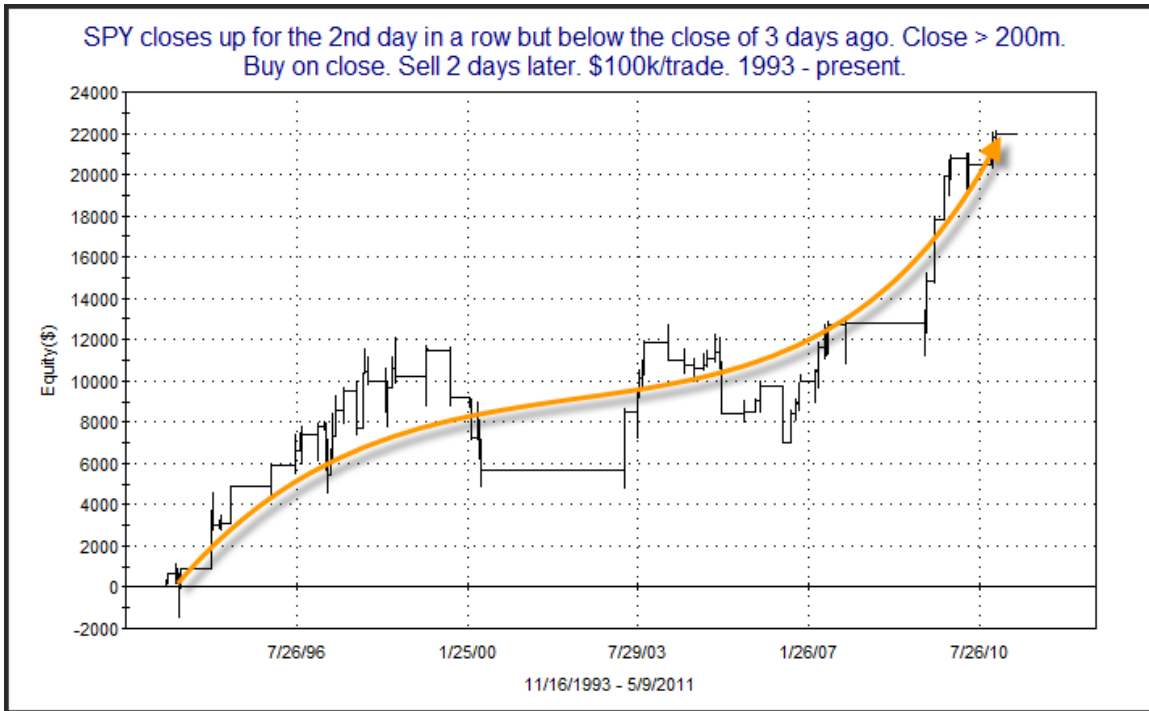
What once appeared to potentially suggest a downside edge, no longer appears to suggest anything.

There was one Quantifinder study, though that did seem to merit inclusion among the Active Studies. It was last published in the 11/19/10 Letter and it look at times the SPY bounced up 2 days in a row but still failed to close above the close of 3 days ago. I have updated that study below.

SPY closes up for the 2nd day in a row but below the close of 3 days ago. Close > 200m.
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	13,029.92	69	41	27	59.42	1,495.87	-1,788.92	0.84	1.27	188.84
4	17,178.83	70	45	25	64.29	1,353.21	-1,748.62	0.77	1.39	245.41
3	12,755.84	71	43	28	60.56	1,237.09	-1,444.25	0.86	1.32	179.66
2	21,963.08	71	50	21	70.42	866.30	-1,016.76	0.85	2.03	309.34
1	5,450.57	71	43	26	60.56	563.04	-721.54	0.78	1.29	76.77

The stats appear to suggest an upside edge over the 1st 2 days. Below is an equity curve using a 2-day exit strategy.



The flat lines occur when the market is below the 200ma for a period of time. There a dip during 2005 – 2006, but other than that the upslope appears strong.

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



With tonight's new study included the green Aggregator line remains squarely above 0. The positive value means the net expectation from the Active Studies List is for upside over the next few days. Meanwhile, as the market has rallied the last 2 days the black Differential line has dipped. Still it remains in positive territory. Readings greater than 0 mean the SPX has underperformed expectations over the last few days. So net expectations are for upside and the SPX is oversold versus recent expectations. Historically this configuration has provided a bullish edge. It can be seen on the chart whenever both lines close above 0. Due to this the Aggregator System remained long at the close.

The green Aggregator line is again set to close above 0 on Tuesday. This could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will dip to 1,343.08. This is 1/4% below Monday's close. This means that unless the SPX drops at least this much the Differential Line will drop down below 0. In other words, unless there is a decent-sized selloff I will be looking to exit my long index positions.

Configurations like the present allow for some flexibility with your trade management approach. This is because the Differential Pivot for tomorrow is actually below today's closing price. This effectively puts you into profit-taking mode. The exit trigger tomorrow is below the current price. So you could think about taking profits any time between now and tomorrow's close. The only thing that would stop the exit trigger from

occurring is if the market falls back below the Differential Pivot. (And of course if this happens you have the option of buying back your shares at a discount.)

One tactic you might consider would be to sell into a gap up on Tuesday morning. Another might be to sell into a morning rally. Or you could place a stop below an intraday congestion level and then exit any breakdown below that level.

My approach is typically to try and hold on through the end of the day. I do this because the studies and the Aggregator are still suggesting an upside edge and I want to catch as much upside as I can. Should a trend-day higher form on Tuesday, I want to benefit from that rally. At the same time I remain aware that there is no sense blindly holding on through the end of the day if the market is well above my exit trigger and forms an intraday topping pattern. I'd rather not give up a big chunk of my profits stubbornly holding on for the 4pm close. Therefore I will often trail a loose stop higher throughout the day. This is the approach I intend to take tomorrow. I will be out of the office some during the day, but I will try and send out notes to subscribers detailing my approach should I elect to institute or trail stops during the day.

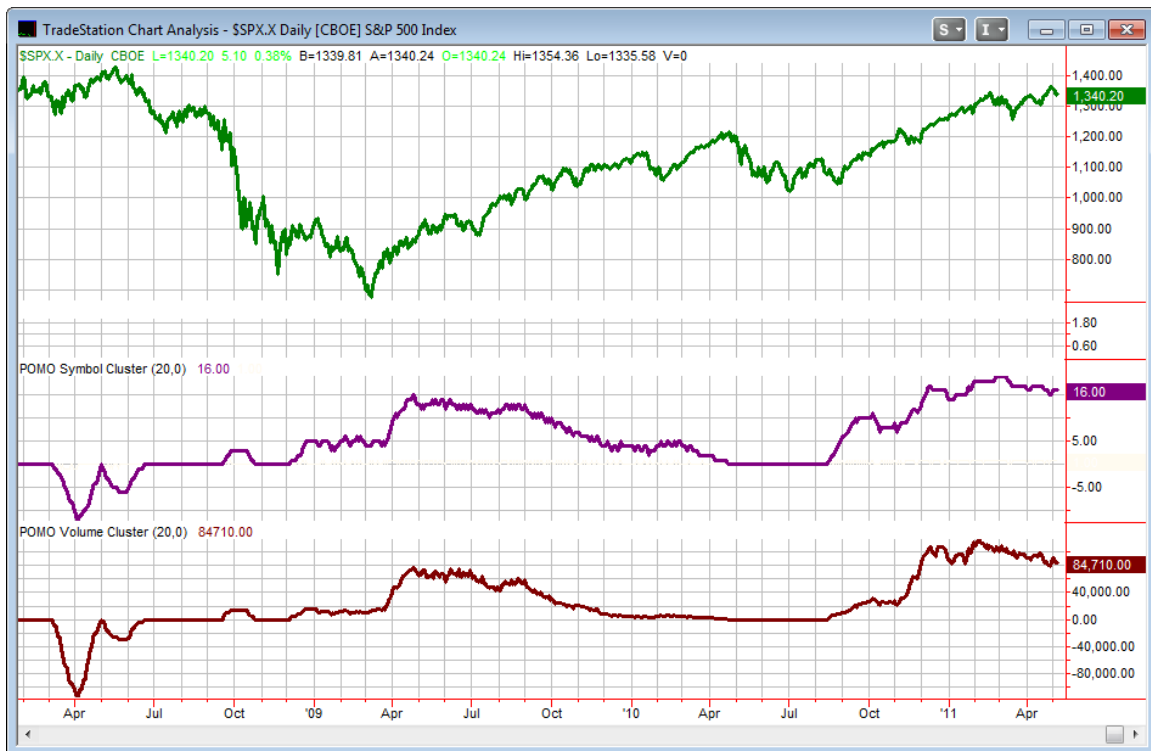
Intermediate-term Outlook (2 weeks – 2 months)– updated 5/9 – bullish

This wasn't a great week for the market. Monday morning marked the high and despite being up on Friday it was still at the low end of the week's range. Overall I am still seeing more positives than negatives and expect the move up isn't over. Still, this upcoming week could provide us with some very valuable insights – especially with regards to liquidity and POMO expectations.

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>



Despite 5 days of buying, the POMO indicators didn't make much headway this past week. The days indicator ticked up from 15 to 16 and the POMO Volume indicator is still near the low end of its recent range. The schedule calls for POMO buying for the next 3 trading days, and then a new schedule to be released on Wednesday.

June is when the QE2 buying is scheduled to end. It hasn't been announced whether that means June 1 or June 30 or somewhere in between. The schedule release on Wednesday could provide some indication of the Fed's intentions. I wouldn't be surprised to see the market get nervous as signs of the end approach. For now POMO activity seems to still be providing a positive influence. But that is not going to last too much longer.

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

Despite the pullback this past week, intermediate-term indications still appear to favor the bulls. At this point there is very little suggesting a top. So I remain intermediate-term bullish. This means I will play long trades more aggressively and short trade 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.

No new trade ideas tonight.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
EPP	4/19/2011	\$48.85	\$49.32	0.96%		System 90609
SPY	5/4/2011	\$135.67	\$134.72	-0.70%		Aggregator
SPY	5/5/2011	\$134.08	\$134.72	0.48%		sold on close
SPY	5/5/2011	\$133.61	\$134.72	0.83%		Aggregator

As indicated in last night's letter, 1 lot of the SPY was exited at the close.

Should the SPX close at or above the Differential Pivot of 1,343.08, I will exit both lots.

Per system 90609, EPP will be sold if it closes between \$48.86 and \$50.82 tomorrow.

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