

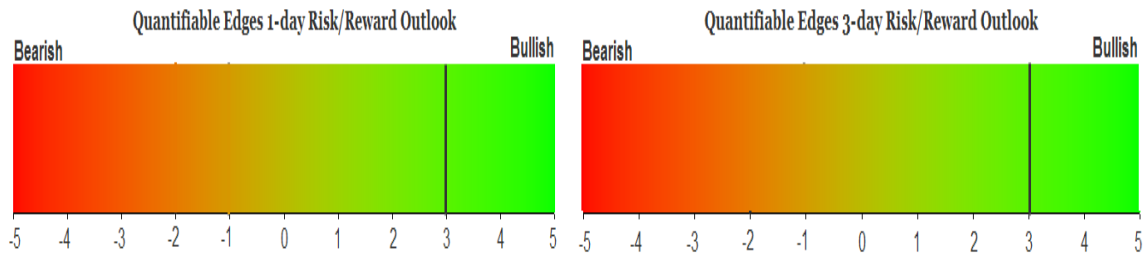
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 17, 2011

Volume 4 Issue 116

Market Overview



Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Long	100% Long XIV	100% Long XIV	Flat

Tonight's Research Points

- The weak breadth on a bounce-back day suggests a move lower.
- Large VIX spikes when the SPX rises have led to short-term up moves.

Short-term Outlook

The Bottom Line

Studies are a bit mixed today but still favor the bullish case overall. I'm heavily long and looking for more of a bounce before I exit.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
June 17, 2011	VIX up 6% while SPX up.	1-3 days	Bullish	
June 17, 2011	Breadth < 45%. Up day after 1.5% drop.	1-2 days	Bearish	
June 16, 2011	SPX 50-low. VIX spike.	1-2 days	Bullish	2.80%
June 15, 2011	SPX up 2 days, below close 3 days ago.	1-3 days	Bullish	
June 13, 2011	McClellan Osc % Rank < 2%. SPX 50 low	1-6 days	Bullish	3.70%
Active - Long Term				
May 31, 2011	4 Weeks Down. Close > 40ma.	1-10 weeks	Bullish	9.00%
March 22, 2011	3 Days Up Issues % > 70%	8 months	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				
June 14, 2011	NYSE Up Issues % < 40%. SPX up.	1-3 days	Bearish	

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

The Evidence

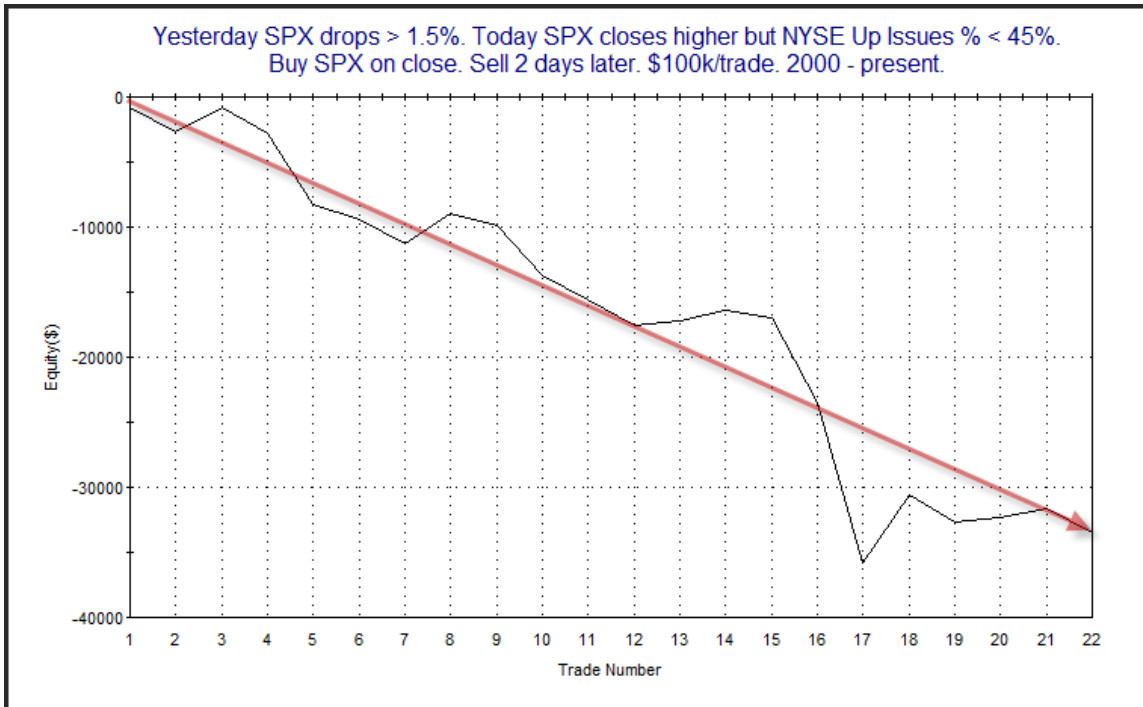
The market was all over the place on Thursday, and in the end it finished mixed. The SPX rose 0.2% and the Russell 2000 gained 0.25%, but the Nasdaq lost 0.3%. Breadth was weak for an up day as the NYSE Up Issues % came in just under 45% and the Up Volume % was 48%. Total volume retreated from Wednesday's levels.

There were 2 studies tonight that I found especially compelling. Unfortunately they were at odds with each other. I'll show each below.

This first study looks at weak breadth days and suggests a downside edge. It last appeared in the 4/20/10 subscriber letter and I have updated the results below.

Yesterday SPX drops > 1.5%. Today SPX closes higher but NYSE Up Issues % < 45%. Buy SPX on close. Sell X days later. \$100k/trade. 2000 - 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	-23,892.06	22	6	16	27.27	3,911.45	-2,960.05	1.32	0.50	-1,086.00
4	-23,796.82	22	5	17	22.73	3,409.89	-2,402.72	1.42	0.42	-1,081.67
3	-29,882.06	22	6	16	27.27	2,660.41	-2,865.28	0.93	0.35	-1,358.28
2	-33,496.08	22	7	15	31.82	1,681.58	-3,017.81	0.56	0.26	-1,522.55
1	-27,272.83	22	4	18	18.18	2,043.03	-1,969.16	1.04	0.23	-1,239.67

Since the turn of the century, action such as we saw Thursday has consistently led to a quick selloff. The edge has basically been played out in the 1st 2 days, though. Below is an equity curve showing how the edge has evolved over time.



My only concern with this particular study is that breadth barely qualified. Still, I'm including it.

While the major indices finished the day with mixed moderate moves, the VIX moved quite a bit higher. It finished 6.7% above Wednesday's close. It's very unusual to see the VIX spike up on a day the SPX also closes higher. This is especially true on a day other than Monday, since Mondays show a tendency for a rising VIX. The study below addresses this.

VIX closes up over 6% while SPY closes positive. Today is not Monday.
Buy SPY 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	16,638.85	14	12	2	85.71	1,472.48	-515.48	2.86	17.14	1,188.49
4	16,986.59	14	12	2	85.71	1,478.28	-376.36	3.93	23.57	1,213.33
3	13,755.96	14	13	1	92.86	1,065.23	-91.98	11.58	150.55	982.57
2	9,160.21	15	11	4	73.33	1,024.54	-527.43	1.94	5.34	610.68
1	3,249.10	16	10	6	62.50	611.20	-477.14	1.28	2.13	203.07

100% of instances closed above the entry price at some point in the next week.

Instances are a little low but appear overwhelmingly bullish. Below I have listed all instances using a 3-day exit strategy.

VIX closes up over 6% while SPY closes positive. Today is not Monday. Buy SPY on close. Sell 3 days later. \$100k/trade. 1993 - present.				
Date/Time	Signal	Price	% Profit	Run-up Drawdown
03/31/94	Buy	\$44.60	0.47%	\$695.02
04/06/94	Sell	\$44.81		(\$2,802.50)
10/12/94	Buy	\$46.69	0.56%	\$1,370.24
10/17/94	Sell	\$46.95		\$0.00
11/23/94	Buy	\$45.25	0.91%	\$1,104.50
11/29/94	Sell	\$45.66		\$0.00
01/03/95	Buy	\$45.79	0.59%	\$1,004.18
01/06/95	Sell	\$46.06		(\$87.32)
05/04/95	Buy	\$52.25	0.54%	\$1,147.80
05/09/95	Sell	\$52.53		(\$325.21)
05/31/95	Buy	\$53.05	1.56%	\$1,903.85
06/05/95	Sell	\$53.88		\$0.00
12/05/95	Buy	\$62.14	0.05%	\$643.60
12/08/95	Sell	\$62.17		(\$579.24)
12/22/95	Buy	\$61.21	0.34%	\$751.18
12/28/95	Sell	\$61.42		\$0.00
02/06/96	Buy	\$64.77	1.65%	\$2,484.23
02/09/96	Sell	\$65.84		(\$108.01)
03/19/96	Buy	\$65.23	(0.09%)	\$475.23
03/22/96	Sell	\$65.17		(\$889.14)
09/03/96	Buy	\$65.75	0.29%	\$1,520.00
09/06/96	Sell	\$65.94		(\$1,109.60)
05/27/97	Buy	\$85.13	0.18%	\$504.82
05/30/97	Sell	\$85.28		(\$2,348.00)
03/17/00	Buy	\$146.94	2.14%	\$2,652.00
03/22/00	Sell	\$150.09		(\$1,659.20)
10/26/00	Buy	\$136.69	4.58%	\$5,117.00
10/31/00	Sell	\$142.95		(\$43.86)

The one concern I have when examining the individual trades is that all the instances occurred between 1994 and 2000. This is the 1st occurrence in about 11 years. Still, results appeared strong enough that I decided to include it on the Active List.

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



The green Aggregator Line is once again solidly above 0. Readings above 0 mean net expectations from the active list are for upside over the next few days. Meanwhile, the black Differential Line is also well above 0. This means the SPX has underperformed expectations over the last few days. So net expectations are positive and the SPX is oversold versus recent expectations. While the last 2 weeks have been rough, historically this has provided an upside edge. This configuration 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 Friday. This could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,293.28. This is about 2% above Thursday's close. So it would take a very strong move higher on Friday to see the Differential line fall into negative territory.

Overall it appears the spike in fear we have seen in the last couple of days could be the catalyst that finally allows this market to deliver a bounce. I'm all-in from an index standpoint so I won't be looking to add more tomorrow. The open Catapult trades are fairly close to hitting their target prices and I have provided approximate exit targets in the Trade Ideas section below.

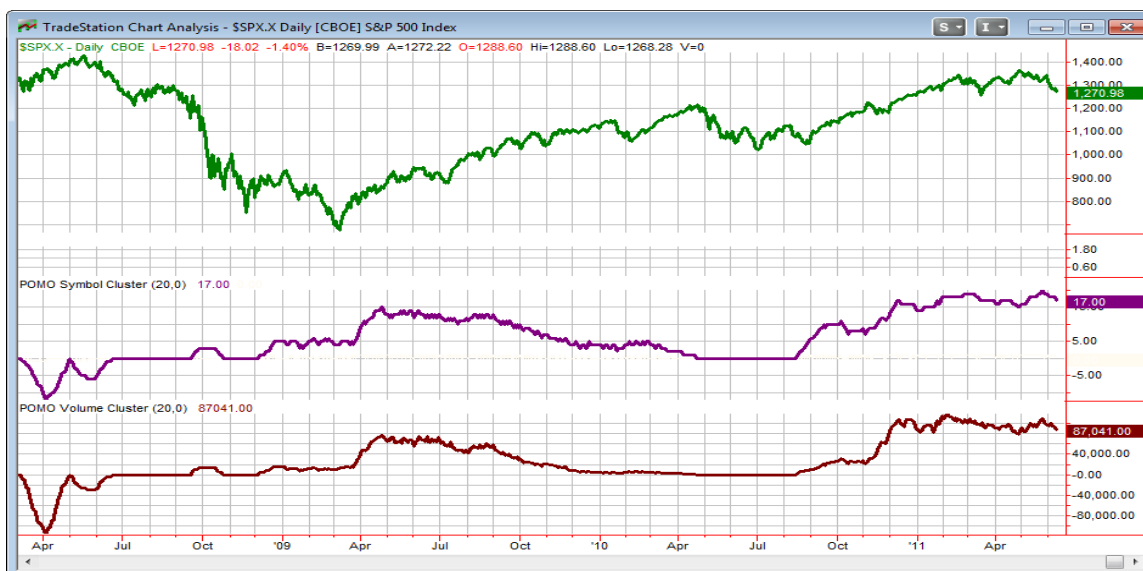
Intermediate-term Outlook (2 weeks – 2 months)– updated 6/13 – neutral

It was another tough week in the market. We are now down 6 weeks in a row. Perhaps the biggest development is that the POMO schedule was released on Friday and we can now see the end of QE2.

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>



Both the POMO Days and POMO Volume indicators remain at high levels. Still, they are beginning to trend lower. The current schedule calls for steady buying until the end of the month, but after that there will be little in the way of Fed stimulus. Starting July 1

we will see these indicators begin to head back towards the 0 line. There are 2 small days of buying currently scheduled in July which is associated with the reinvestment of principal payments rather than the \$600billion of QE2 money. The past few times POMO stimulus was halted, it took the market about a month after the halt until prices began to decline.

For those that would like to view the current schedule I have provided a link below.

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

Intermediate-term studies are still slightly in favor of the bulls, but that may not last long with POMO exiting the equation. The bears may also point to the divergence in the number of new highs in the NYSE that I discussed a couple of weeks ago. The studies found on the intermediate-term active list at the top of this letter consider breadth, momentum, and intermediate-term mean reversion. I expect we will get a bounce here in the short-term as suggested by the short-term section above. That bounce could carry forward for another few weeks. I don't have great confidence that it will surpass the May highs. After the next few weeks the picture becomes less clear in my eyes. I'm moving the intermediate-term outlook to neutral. I will approach both longs and shorts with some caution but at this point I am willing to bet either way should short-term evidence suggest an edge.

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

LOW – 1/3 position @ \$23.59

LOW – 1/3 position @ \$23.40(2nd lot)

AEP – 1/3 position @ \$37.51

LOW – 1/3 position @ \$22.87(3rd lot)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 4(2)(LOW(3), AEP)

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
SPY(1/4)	6/2/2011	\$131.87	\$127.30	-3.47%		Aggregator
SPY(1/4)	6/3/2011	\$130.15	\$127.30	-2.19%		Aggregator
LOW(1/3)	6/3/2011	\$23.18	\$22.68	-2.16%		Catapult
LOW(1/3)	6/6/2011	\$23.07	\$22.68	-1.69%		Catapult
AEP(1/3)	6/6/2011	\$37.43	\$37.35	-0.21%		Catapult
SPY(1/4)	6/6/2011	\$129.04	\$127.30	-1.35%		Aggregator
LOW(1/3)	6/8/2011	\$22.72	\$22.68	-0.18%		Catapult
XIV	6/13/2011	\$170.38	\$152.32	-10.60%		
SPY(1/4)	6/16/2011	\$127.02	\$127.30	0.22%		Aggregator

Both remaining Catapults are near an exit. Exit triggers estimates are below for both.

LOW would need to hit (approx.) \$23.05 intraday, or close \geq \$22.87.

AEP would need to hit (approx.) \$37.56 intraday, or close \geq \$37.45.

There is a good chance I would send an intraday update and exit at least part of these positions at the close rather than waiting for Monday's open if the exit triggers are hit.

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