

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 27, 2011

Volume 4 Issue 143

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 low QQQ volume doesn't appear to have the same bearish inclinations that low SPY volume indicates.

Short-term Outlook

The Bottom Line

Expectations are turning more positive and the SPX is now short-term oversold. I am partially long and looking to hold that position for now.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
July 26, 2011	SPY unfilled gap from 10-high	1-2 days	Bearish	-1.00%
July 22, 2011	Up Issue% > 75% 2 of 3. Close 10 high.	1-6 days	Bullish	2.70%
Active - Long Term				
July 22, 2011	Up Issue% > 75% 2 of 3. Close 10 high.	1-20 days	Bullish	5.50%
July 5, 2011	QE2 Over	int term	Bearish	
July 5, 2011	3 days higher. Up vol % > 90% today.	1-20 days	Bullish	5.00%
June 22, 2011	FTD with Up Issues % 1-yr Rank > 95%	int term	Bullish	
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%
October 25, 2010	SPX Golden Cross	int term	Bullish	
Dropped Tonight				
July 25, 2011	10-day high on 20-day low volume	1-2 days	Bearish	-1.10%

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

The Evidence

The market opened just a little below breakeven but could never muster a decent rally on Tuesday. It sold down near its lows for the day at the close and the major indices finished mostly lower. (The NDX was up.) The SPX lost 0.4%, the Nasdaq was down 0.1% and the Russell 2000 dropped 0.8%. Breadth was weak as the NYSE Up Issues % came in at 34% and the Up Volume % was 38%. Total NYSE volume increased for the 2nd day in a row but still appeared near average.

Nothing terribly compelling stood out in the Quantifinder tonight. A couple of studies noted the fact that the QQQ posted its lowest volume in a month. It also closed at a new short-term high. Readers will likely recall that it was just a couple of days ago in the 7/25/11 subscriber letter that I showed results of SPY hitting a 10-day high on a 20-day low in volume (while above the 200ma). I ran the same test on the QQQ tonight. Results are below.

QQQ posts its highest close in 10 days on the lightest volume in 20 days. Close > 200ma. Buy 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
10	-4,444.74	33	18	14	54.55	2,373.51	-3,369.14	0.70	0.91	-134.69
9	-15,746.41	33	18	15	54.55	2,129.51	-3,605.18	0.59	0.71	-477.16
8	-12,205.81	35	17	18	48.57	2,426.89	-2,970.16	0.82	0.77	-348.74
7	-11,086.60	36	21	15	58.33	1,879.09	-3,369.83	0.56	0.78	-307.96
6	716.99	36	18	18	50.00	1,882.09	-1,842.26	1.02	1.02	19.92
5	-5,921.57	37	19	18	51.35	1,403.64	-1,810.60	0.78	0.82	-160.04
4	7,967.15	37	23	13	62.16	1,168.01	-1,453.61	0.80	1.42	215.33
3	13,582.41	39	24	15	61.54	1,338.83	-1,236.63	1.08	1.73	348.27
2	1,896.61	42	25	17	59.52	952.27	-1,288.83	0.74	1.09	45.16
1	6,170.81	45	26	19	57.78	674.70	-598.49	1.13	1.54	137.13

With SPY there was an obvious and compelling downside edge. Here we see the same setup with QQQ doesn't appear to provide any edge at all. Some traders might look at this and be led to believe that it was a problem with the setup. That perhaps it had worked well on SPY due to luck and not due to solid technical reasons. This is not my opinion. And in fact I was not at all surprised to see that a downside edge was not suggested by the setup for the QQQ.

I believe the primary reason is the two indices simply behave different. It's something I've seen over and over when designing systems. The SPX tends to more often favor mean reversion while the QQQ is more inclined to carry momentum. The reason may be that the SPX is a much broader index. There is a lot of push and pull within it as money flows from financials to industrials or consumer staples or one of the other sectors. The NDX on the other hand is heavily weighted towards one sector – technology. More narrow indices will often show a higher propensity to carry momentum from one day to the next, while broader indices succumb to the push and pull of diversification and will have a higher propensity for reversion. This is something system designers should keep in mind when determining the best indices to trade their systems. Unfortunately, it doesn't tell us much about the current short-term inclinations of the market.

There was a time when [2 down days would be enough to suggest a long-side edge](#). That has not been the case now since around mid-2009. So with Tuesday having failed to provide strong directional hints, we need to rely on the studies of the past few days in order to set expectations.

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



With the elimination of one of the bearish studies tonight the green Aggregator line rose further. It is strongly positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the Differential Line crossed 0 and is also now positive. A positive Differential reading means the SPX has underperformed expectations over the last few days. So net expectations are positive and the SPX is oversold versus recent expectations. Historically this combination has provided a bullish edge. It can be seen on the Aggregator chart whenever both lines are above 0. Due to this the Aggregator System turned long at the close.

With the current studies the green Aggregator line is again set to close above 0 on Wednesday. This could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,350.36. This is about 1.4% above Tuesday's close. This means that it would take a rally of at least this much in order to flip the Differential Line back to negative.

The last 2 days have played out perfectly according to form. A pullback was anticipated and now expectations are looking for a bounce. Hopefully the market continues to behave in accordance with historical norms. The new Aggregator buy signal has me short-term bullish. As I laid out in last night's letter, I took some long exposure at the close on Tuesday. Since new bullish evidence failed to materialize on Tuesday I won't be looking to increase this exposure on Wednesday. Instead I'll look to consider any evidence Wednesday's action may provide and reevaluate my position again tomorrow evening.

Intermediate-term Outlook (2 weeks – 2 months)– updated 7/25 – moderately bullish

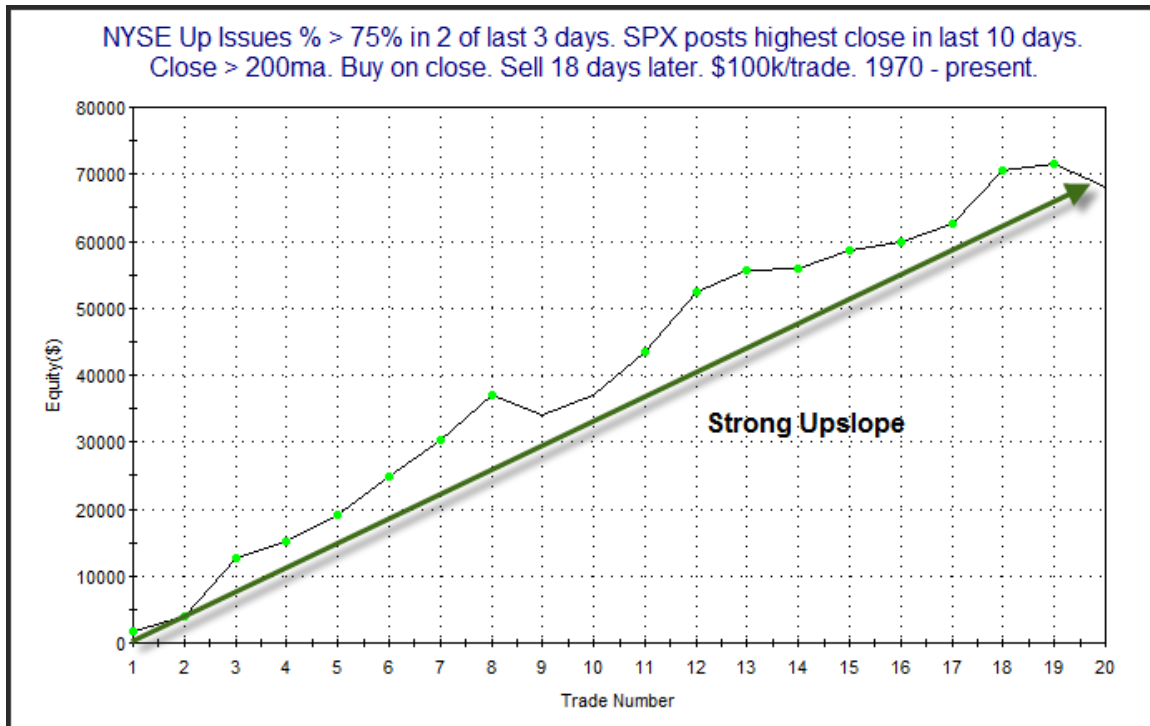
After a dip to new short-term lows on Monday the market gathered itself and finished out with a nice week. The SPX is now less than 1% from its July high and within 2% of its May high. An intermediate-term study triggered on Thursday that suggested that these levels should be taken out. Below I have copied the results from Thursday night's letter.

NYSE Up Issues % > 75% in 2 of last 3 days. SPX posts highest close in last 10 days.
Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1970 - 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	72,673.56	19	16	3	84.21	4,912.07	-1,973.20	2.49	13.28	3,824.92
19	70,576.96	20	17	3	85.00	4,593.61	-2,504.78	1.83	10.39	3,528.85
18	68,169.46	20	18	2	90.00	4,150.05	-3,265.74	1.27	11.44	3,408.47
17	65,698.31	20	18	2	90.00	4,089.68	-3,957.99	1.03	9.30	3,284.92
16	64,695.52	20	18	2	90.00	4,015.19	-3,788.93	1.06	9.54	3,234.78
15	54,962.15	20	16	4	80.00	4,043.82	-2,434.73	1.66	6.64	2,748.11
14	50,742.27	20	18	2	90.00	3,381.83	-5,065.35	0.67	6.01	2,537.11
13	48,932.78	21	17	4	80.95	3,442.08	-2,395.64	1.44	6.11	2,330.13
12	48,351.39	22	17	5	77.27	3,423.88	-1,970.90	1.74	5.91	2,197.79
11	50,348.14	22	18	4	81.82	3,193.65	-1,784.37	1.79	8.05	2,288.55
10	45,265.78	22	18	4	81.82	3,002.75	-2,195.91	1.37	6.15	2,057.54
9	43,659.47	22	17	5	77.27	3,118.12	-1,869.70	1.67	5.67	1,984.52
8	38,392.06	22	18	4	81.82	2,516.31	-1,725.40	1.46	6.56	1,745.09
7	38,493.16	22	17	5	77.27	2,580.25	-1,074.22	2.40	8.17	1,749.69
6	39,010.37	23	20	3	86.96	2,145.86	-1,302.27	1.65	10.99	1,696.10
5	32,659.62	23	18	5	78.26	1,996.35	-654.95	3.05	10.97	1,419.98
4	25,157.02	24	19	5	79.17	1,497.08	-657.52	2.28	8.65	1,048.21
3	16,066.83	24	16	8	66.67	1,382.97	-757.59	1.83	3.65	669.45
2	10,142.47	27	17	10	62.96	1,072.59	-809.16	1.33	2.25	375.65
1	5,976.39	29	17	12	58.62	692.62	-483.18	1.43	2.03	206.08

All 29 instances posted a close above the entry price at some point in the next 6 days.

The intermediate-term implications appear strongly positive. I showed a short-term equity curve on Thursday. Today I have run an intermediate-term curve, which can be found below.

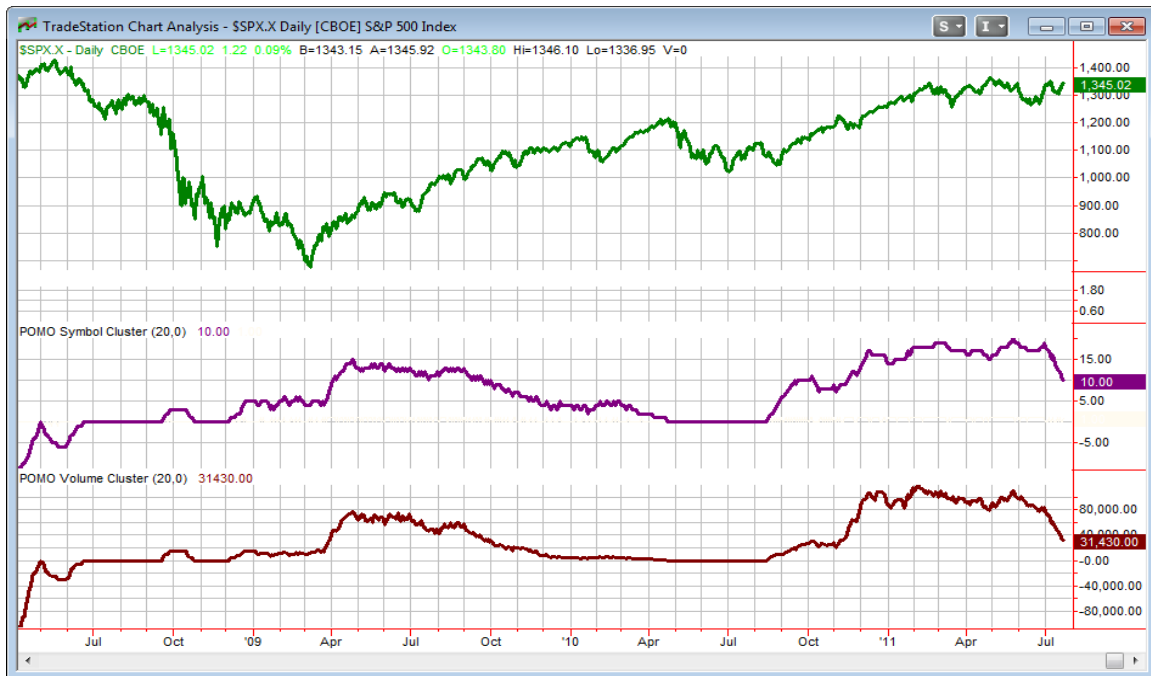


The strong upslope creates greater confidence in the upside edge.

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>



There were again 2 days of POMO buying this past week. They were extremely light days from a volume perspective. In looking at the upcoming schedule it appears 2 days a week may be par for the course for a while. So even without QE2, there will still be a decent amount of liquidity pumping occurring. It certainly isn't at the levels that the market was accustomed to, but it does not appear the POMO indicators above will be hitting 0 any time soon. The "Days" indicator may even settle in around 7-8, which is far higher than I originally anticipated. Below is a link to the upcoming schedule.

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

With buying so light this past week it will be interesting to see where the POMO volume indicator begins to level off. Action over the next couple of weeks will be especially interesting as the QE2 program completely falls out of the backwards-looking calculation.

There remain a number of intermediate-term market positives that can be pointed to. Breadth seems to be the #1 indication of higher prices. Thursday's study created the 3rd active intermediate-term breadth-thrust study. The other 2 were from March 22nd and July 5th. There is also still a high-probability Follow-Through Day signal active, the Nasdaq is leading the SPX, and price action and momentum are providing positive indications as well. The big concern remains the rapidly weakening POMO activity. The combination of evidence is enough to keep me slightly favoring the bull side for the time being.

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
SPY(1/4)	7/26/2011	\$133.33	\$133.33	0.00%		bought on close

This report has been prepared by Hanna Capital Management, LLC and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy securities. While information contained herein is believed to be accurate at the time of publication, we make no representation as to the accuracy or completeness of any data, studies, or opinions expressed and it should not be relied upon as such. Robert Hanna, Hanna Capital Management, LLC or clients of Hanna Capital Management, LLC may have positions or other interests in securities (including derivatives) directly or indirectly which are the subject of this report. This report is provided solely for the information of Hanna Capital Management, LLC clients and prospects who are expected to make their own investment decisions without reliance upon this report. Neither Hanna Capital Management, LLC nor any officer or employee of Hanna Capital Management, LLC accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. This report may not be reproduced, distributed or published by any recipient for any purpose without the prior express consent of Hanna Capital Management, LLC.

Copyright © 2011 Hanna Capital Management, LLC.