

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 14, 2011

Volume 4 Issue 177

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Flat	Flat	Flat	Long

## Tonight's Research Points

- No new compelling evidence tonight.
- Unless strong bullish evidence emerges or the market tanks on Wednesday, it appears we could be nearing a short signal.

## Short-term Outlook

### The Bottom Line

the aggregator remains neutral and I'm not ready to commit new capital just yet, but if the SPX closes up again on Wednesday, I anticipate beginning to build a short position.

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

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
September 13, 2011	SPY gap down and reverse.	1-3 days	Bearish	-3.80%
September 13, 2011	SPX up. VIX up. Monday < 200ma	1-5 days	Bearish	-3.60%
<b>Active - Long Term</b>				
September 12, 2011	Nasdaq leading SPX	int term	Bullish	
September 6, 2011	1% drop prior to 3-day US weekend	1-20 days	Bearish	
August 24, 2011	IBD Follow Through Day strong breadth	int term	Bullish	
August 16, 2011	SPY up 3. Vol down 3 days.	1-20 days	Bearish	
July 5, 2011	QE2 Over	int term	Bearish	
March 22, 2011	3 Days Up Issues % > 70%	8 months	Bullish	19.00%
<b>Dropped Tonight</b>				
September 13, 2011	Weak bounce after 2% drop.	1 day	Bearish	
September 12, 2011	33.3% Up Issues. SPX < 200ma.	1-2 days	Bullish	3.00%
September 12, 2011	SPX down 2.5% on Friday	1-2 days	Bullish	2.70%

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

### ***The Evidence***

Bulls won out on Tuesday on relatively quiet action. The SPX gained 0.9%, the Nasdaq was up 1.5%, and the Russell 2000 rose 1.7%. Breadth was strongly positive as the NYSE Up Issues % came in at 70% and the Up Volume % was 76%. Total NYSE volume declined for the 2<sup>nd</sup> day in a row.

The moderate gains, the choppy action recently, and the fact that the market is near the middle of its recent range all contributed to a dearth of the new evidence. The Quantifinder failed to identify anything new and compelling tonight. The wild market action of late has given us plenty to talk about. I think this may be the first time since July but I'm not publishing any studies in the letter, so it seems unusual. But under the kind of conditions we are now experiencing that I listed above it isn't uncommon to see a lack of compelling evidence. As I sometimes say, edges are more prevalent on the edges. In other words, there often isn't a strong short-term directional advantage in the middle of a trading range.

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



Without any new studies the green Aggregator line barely budged today. It remains negative. Levels below 0 mean net expectations from the Active List are for downside over the next few days. Meanwhile, the Differential Line fell slightly but is still above 0. A positive Differential reading means the SPX has underperformed expectations over the last few days. So net expectations are negative but the SPX is oversold versus recent expectations. This is considered a neutral configuration. Neutral configurations can be seen on the chart whenever both lines close on opposite sides of 0. Due to this the Aggregator System changed from long to flat at the close.

Based on the current active studies the green Aggregator line is poised to close below 0 again on Wednesday. Of course this could change if bullish studies emerge. Meanwhile, the Differential Pivot will drop to just 1,151.44 on Wednesday. This is 1.8% *below* Tuesday's close. In other words, the Differential Line is now poised to turn negative on Wednesday. To prevent that from happening, the SPX will need to close down below the 1,151.44 pivot.

Setups like tonight are always interesting. We don't have a clear and obvious downside edge at the moment, but that is what appears to be setting up. To avoid a short signal tomorrow we will need to see either strong bullish evidence or a large decline. Of course it is difficult to anticipate what studies will trigger before the day begins, but here are a

few scenarios that seem reasonable. A decent sized drop of say 1%-1.5% would likely trigger some bullish studies. This would keep the signal flat. A larger decline that sees the SPX close down below the Differential Pivot could potentially generate enough bullish evidence to trigger a long signal. If the SPX pulled back just a small amount tomorrow, then substantial evidence in either direction could be lacking, in which case bearish expectations may remain and we could potentially see a short signal. Of course the other option is an up day. This would be the third day higher a row. When trading below the 200ma, three consecutive up days are often accompanied by bearish studies. It seems unlikely that enough bullish evidence would emerge under this scenario that it would overwhelm both new and existing bearish evidence. The likely result of an up day therefore appears more clear-cut than what a down day might provide. If the SPX finishes higher tomorrow I anticipate a short signal will probably trigger.

Based on this conjecture I will look to begin scaling into a short position if there is a higher close tomorrow. I will put a caveat on this trade idea that if the intraday Quantifinder identifies strongly bullish evidence with the market in positive territory and I publish a "flat" signal on the systems page tomorrow as we approach the bell, then the trade idea will be canceled. I've listed it this way in the trade ideas section below.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 9/12 – slightly bearish***

The losses Thursday and Friday were steep, and likely a great disappointment to the bulls that rushed into the market between Tuesday's open and Wednesday's close. From a studies standpoint there wasn't much that appeared this week with intermediate-term consequences.

One potential positive for the bulls is that the Nasdaq is now outperforming the SPX. Below is the SPX/Nasdaq Weekly Relative Strength chart from the charts page.



I've circled the reading at the bottom of the chart. It is now appearing in green rather than red, indicating the line color is about to change because the Nasdaq has now taken over the lead from the SPX. This is important because since near the end of 1971 (which is the 1<sup>st</sup> possible new signal after the inception of the Nasdaq) the SPX generated over 100% of its positive performance when the Nasdaq has been leading. Over that time the SPX has gained 1,268.41 points when the Nasdaq has been in the lead. Since the SPX only sits at 1,154.23 today you can easily see how important a leading Nasdaq has been over the last 40 years. More details on this indicator can be found in the blog posts below.

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

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

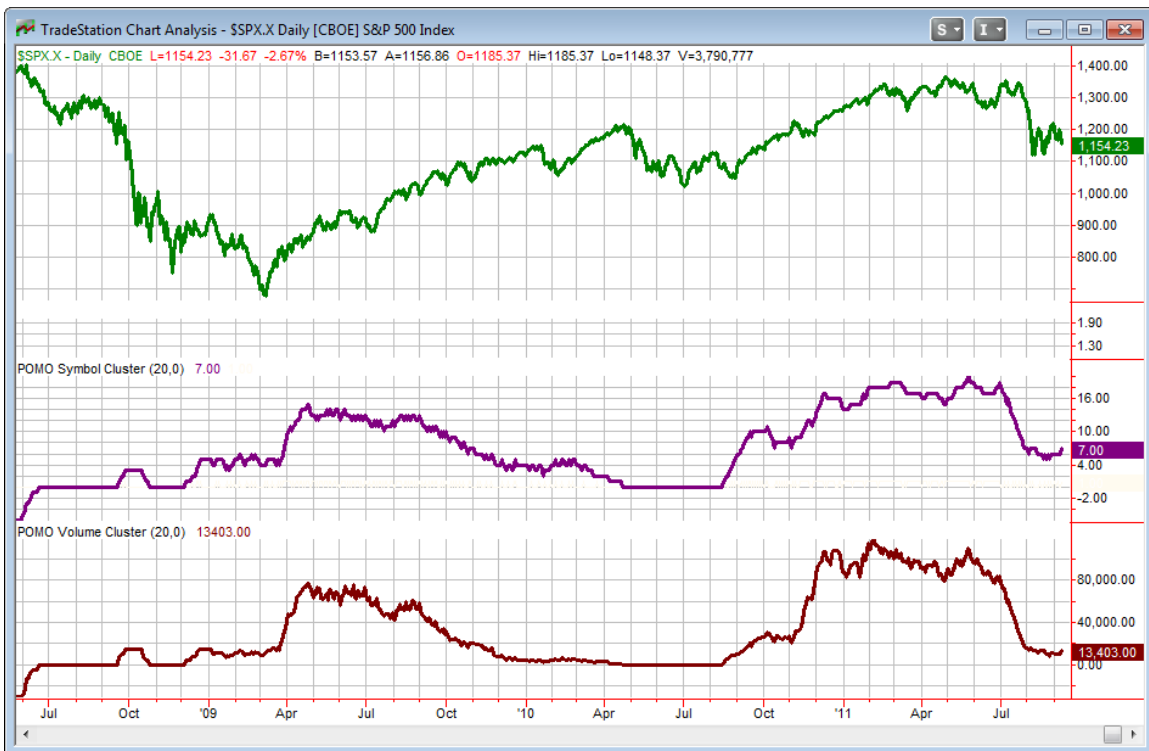
Additionally, for those subscribers that are interested in exploring this indicator more on their own, they may download the model in either Excel or Tradestation format from the downloads page of the members site at any time.

<http://www.quantifiableedges.com/members/memdownloads.php>

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 3<sup>rd</sup> POMO presentation linked below. (Not available for trial users.)*

<http://www.quantifiableedges.com/members/pomo.php>



POMO indicators remain relatively low. After spending the last few weeks at levels quite a bit below the Fed’s published schedule, purchases over the last month are extremely close to the \$14billion number shown on the Fed’s website. Stimulus still remains well below the levels that helped propel the market higher during QE1 and QE2. We keep waiting for the market to prove it can rally without substantial stimulus. So far it has not managed to do so.

While indicators remain mixed, I’m still inclined to slightly favor the short side. Bearish studies are associated with volume, liquidity (POMO), and seasonality. Bulls may find

hope in the August FTD study, the breadth study from several months back, and now the leading position of the Nasdaq. Though I'm not wed to either direction I remain inclined to play the short side a little more aggressively and take a more conservative approach to longs.

### **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 – short @ \$117.75 LIMIT ON CLOSE. Cancel if the Aggregator signal on the systems page reads “flat” when it is updated around 3:50pm.** This is based on the short-term outlook above.*

### **Current Open Trade Ideas**

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
<i>SPY(1/4)</i>	<i>9/12/2011</i>	<i>\$114.47</i>	<i>\$117.05</i>	<i>2.25%</i>		<i>sold on open</i>

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