

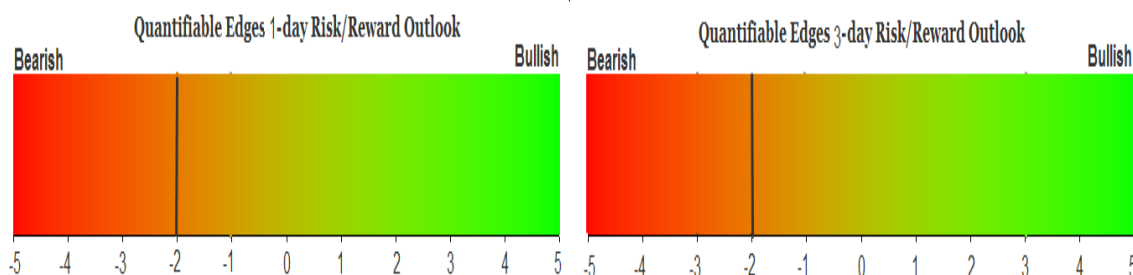
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 3, 2012

Volume 5 Issue 85

Market Overview



Signals Overview

| Aggregator | Aggressive VIX | QE Buy Pwr Swing | NDX Trend Timer |
|------------|----------------|------------------|-----------------|
| Short | Short 100% SPY | Flat | Long |

Tonight's Research Points

- While the volume pattern over the last 4 days may seem bearish to some traders, it hasn't been.

Short-term Outlook

The Bottom Line

Evidence continues to point south. I'm content to sit on my small short position at these levels.

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

| Study Date | Description | Time span | Bias | Avg Max Move |
|---------------------------|--|-----------|---------|--------------|
| Active | | | | |
| May 2, 2012 | 1st Day of May was up | 1-4 days | Bearish | -3.00% |
| May 1, 2012 | Unfilled gap dn from 10-high. Long tail. | 1-3 days | Bearish | |
| April 30, 2012 | SPY 10-high on 20-low vol. | 1-4 days | Bearish | -1.40% |
| Active - Long Term | | | | |
| April 30, 2012 | Nasdaq/SPX RS favors Nasdaq | int term | Bullish | |
| March 14, 2012 | SPX & TNX hit 50-day highs | 1-50 days | Bearish | |
| March 14, 2012 | 50-day high on strong breadth | 1-50 days | Bullish | 8.00% |
| March 5, 2012 | Negative breadth divergences | int term | Bearish | |
| February 1, 2012 | Golden Cross | int term | Bullish | |
| December 5, 2011 | POMO activity flat to negative | int term | Bearish | |
| Dropped Tonight | | | | |
| April 30, 2012 | SPX & VIX up Friday. SPX > 200ma | 1-3 days | Bearish | -1.30% |

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

The Evidence

After a poor start, prices generally improved throughout the afternoon on Wednesday. Still, the market only managed to finish mixed. The SPX fell 0.25%, while the NASDAQ and the Russell 2000 each gained 0.3%. Despite the smallcap outperformance, breadth numbers were negative as the NYSE Up Issues % came in at 43% and the Up Volume % was 33%. Total NYSE volume rose above the levels of the last few days.

Over the last four days the market has flipped back and forth, rising on lower NYSE volume, and declining on higher NYSE volume. Many traders believe that such action should be interpreted as bearish. They also believe it is preferable to see up days come on rising volume and down days on lower volume. On October 21, 2009 I showed the study below, which considers the current 4-day pattern.

| Today SPX falls on higher NYSE volume. Yesterday it rose on lower volume. The day before it fell on higher volume. The day before that it rose on lower volume. 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: Max Winning Trade | All: Avg Losing Trade | All: Max Losing Trade | All: Win/Loss Ratio | All: ProfitFactor | All: Avg Trade |
| 10 | 3,449.38 | 34 | 21 | 13 | 61.76 | 2,138.10 | 6,050.36 | -3,188.51 | -8,443.58 | 0.67 | 1.08 | 101.45 |
| 9 | 15,848.25 | 34 | 22 | 12 | 64.71 | 2,187.79 | 6,806.88 | -2,690.25 | -7,223.74 | 0.81 | 1.49 | 466.13 |
| 8 | 11,541.88 | 34 | 21 | 13 | 61.76 | 2,206.14 | 6,287.49 | -2,675.92 | -7,042.67 | 0.82 | 1.33 | 339.47 |
| 7 | 22,115.89 | 34 | 23 | 11 | 67.65 | 1,982.26 | 6,040.41 | -2,134.20 | -6,394.63 | 0.93 | 1.94 | 650.47 |
| 6 | 8,110.88 | 34 | 23 | 11 | 67.65 | 1,645.16 | 5,371.68 | -2,702.53 | -6,613.82 | 0.61 | 1.27 | 238.56 |
| 5 | 8,099.62 | 35 | 22 | 13 | 62.86 | 1,614.04 | 6,093.68 | -2,108.41 | -5,289.15 | 0.77 | 1.30 | 231.42 |
| 4 | 10,810.11 | 35 | 23 | 12 | 65.71 | 1,470.44 | 4,938.48 | -1,917.50 | -4,183.67 | 0.77 | 1.47 | 308.86 |
| 3 | -3,034.92 | 35 | 20 | 15 | 57.14 | 1,129.09 | 5,010.68 | -1,707.77 | -5,331.20 | 0.66 | 0.88 | -86.71 |
| 2 | -9,725.20 | 36 | 19 | 17 | 52.78 | 888.08 | 2,620.86 | -1,564.63 | -4,026.36 | 0.57 | 0.63 | -270.14 |
| 1 | -2,333.88 | 36 | 18 | 18 | 50.00 | 704.92 | 2,180.44 | -834.58 | -1,875.72 | 0.84 | 0.84 | -64.83 |

I do not see evidence that the price/volume action is bearish. In fact, once you are out between 4-7 days it almost appears bullish. (Not bullish enough to include on the Active List though.)

Tonight I thought it would also be interesting to examine the results of times the volume pattern was reversed. So down days occurred on light volume and up days on higher volume. Those results over the same time period can be found below.

Today SPX falls on lower NYSE volume. Yesterday it rose on higher volume. The day before it fell on lower volume. The day before that it rose on higher volume.
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: Max Winning Trade | All: Avg Losing Trade | All: Max Losing Trade | All: Win/Loss Ratio | All: ProfitFactor | All: Avg Trade |
|--------|-----------------|-------------------|---------------------|--------------------|-------------------|------------------------|------------------------|-----------------------|-----------------------|---------------------|-------------------|----------------|
| 10 | -38,076.70 | 54 | 22 | 32 | 40.74 | 2,072.64 | 4,809.54 | -2,614.84 | -15,203.76 | 0.79 | 0.54 | -705.12 |
| 9 | -29,570.06 | 54 | 22 | 32 | 40.74 | 1,984.09 | 4,561.04 | -2,288.13 | -9,739.60 | 0.87 | 0.60 | -547.59 |
| 8 | -25,166.61 | 55 | 22 | 33 | 40.00 | 2,210.20 | 8,408.28 | -2,236.09 | -10,610.08 | 0.99 | 0.66 | -457.57 |
| 7 | -14,553.85 | 55 | 25 | 30 | 45.45 | 1,860.05 | 8,184.42 | -2,035.17 | -8,265.92 | 0.91 | 0.76 | -264.62 |
| 6 | -3,811.63 | 55 | 22 | 33 | 40.00 | 2,043.33 | 7,253.31 | -1,477.73 | -4,466.66 | 1.38 | 0.92 | -69.30 |
| 5 | -5,728.09 | 56 | 30 | 26 | 53.57 | 1,479.20 | 6,803.13 | -1,927.08 | -10,448.88 | 0.77 | 0.89 | -102.29 |
| 4 | -6,321.73 | 56 | 29 | 27 | 51.79 | 1,288.98 | 3,454.95 | -1,618.60 | -5,597.28 | 0.80 | 0.86 | -112.89 |
| 3 | -12,219.49 | 56 | 29 | 27 | 51.79 | 1,021.29 | 3,003.66 | -1,549.51 | -4,215.12 | 0.66 | 0.71 | -218.21 |
| 2 | 3,846.84 | 56 | 30 | 26 | 53.57 | 915.41 | 2,166.72 | -908.29 | -2,574.60 | 1.01 | 1.16 | 68.69 |
| 1 | -7,299.77 | 56 | 30 | 26 | 53.57 | 601.00 | 3,265.23 | -974.22 | -4,980.56 | 0.62 | 0.71 | -130.35 |

These numbers aren't convincing enough to compel me to short, but they are substantially worse than the previous volume pattern. So while I am not confident enough to claim the current price/volume pattern is bullish, it does appear to provide the bulls more hope than if the volume pattern was reversed.

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



Without anything new making the Active List the green Aggregator line remains solidly negative. Readings below 0 mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line is still hanging below zero. This suggests the SPX is short-term overbought versus expectations. So net expectations are bearish and the SPX is overbought versus recent expectations. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below 0. This meant the Aggregator System remained short at the close. This was indicated as likely on the systems page shortly before the bell.

Based on the current studies, expectations will remain negative on Thursday. Meanwhile, the Differential Pivot will be 1,392.50 on Thursday. This is about 0.7% below Wednesday's close. If the SPX can manage to close down at least this much then the black Differential Line will flip back to positive. This would mean the end of the short signal.

My short order from last night did not get a fill on Wednesday and I remain holding just 1 small lot short. I'm not inclined to try another entry Thursday without more compelling evidence.

Trading has been boring lately. The choppy black and forth action has kept strong edges from appearing the last several days and overnight gaps have prohibited favorable entries. Boring markets can be dangerous for traders. I've discussed this before, but traders often feel they need to be trading. Doing nothing doesn't feel right. But looking for action typically means you're being less selective than is advisable. Doing so can subject traders to greater risks and larger losses. It's tough to make much in a boring market. The key is to make sure you don't lose much, so that the next time strong edges emerge, you can put substantial capital behind those edges. So I am currently content to simply hold my small short position.

Intermediate-term Outlook (2 weeks – 2 months)– updated 4/30 – neutral

Price action was positive this week as the SPX rose 4 out of 5 days and put in solid gains for the week. The early April highs are now less than 2% away, so we are not far from seeing a resumption of the uptrend.

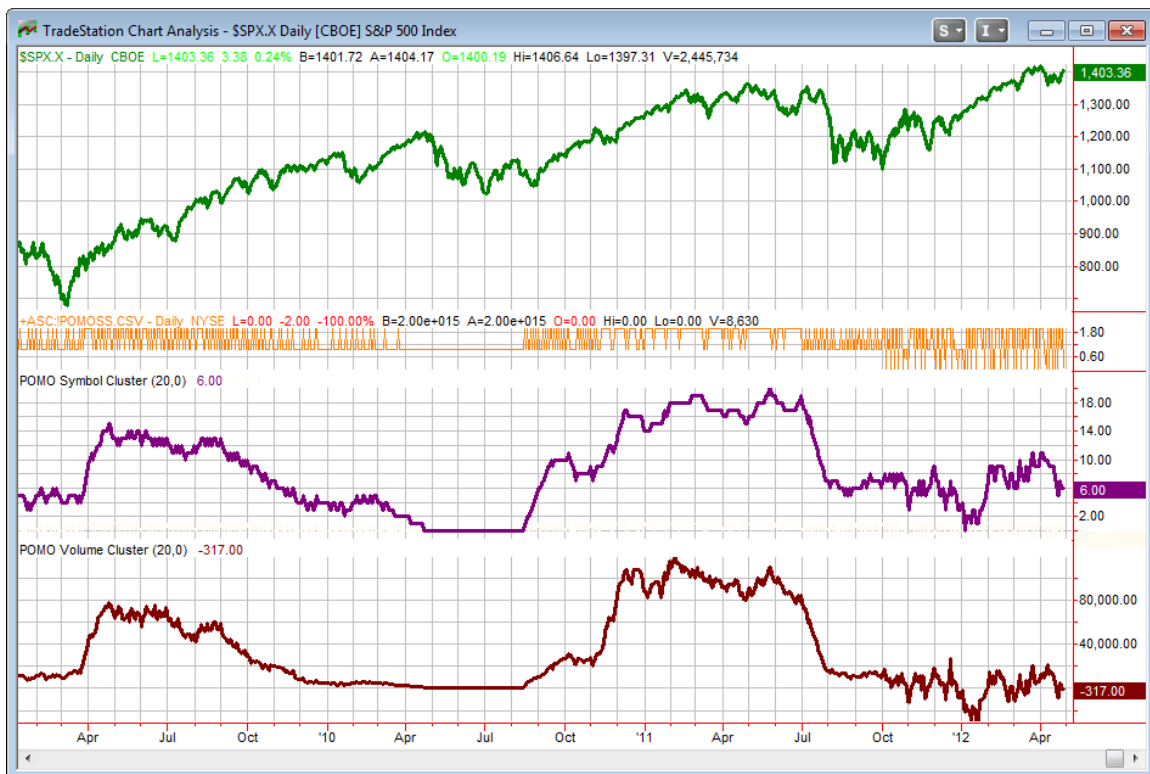
One bit of good news this week is that the NASDAQ was able to regain its leadership position after lagging for just one week. This is based on the SPX/NASDAQ Relative Strength Indicator that can be found on the charts page. I discussed this in some detail last week. The bottom line is that since the inception of the Nasdaq the SPX has made all of its gains and more when the Nasdaq has been in a leading position (as measured by this indicator). More information on the indicator may be found [in this old blog post](#).

Any subscriber who wants to download the model may do so on [the Downloads page](#). The data in the Excel version has not been updated in a while, but the calculations are all there.

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 (purple) pane is the net rolling number of days in the last 20 that have been POMO days. In other words, a day the Fed buys on the market will add +1 while a day of selling will count as -1. The bottom pane is the total amount of money infused into (or taken out of) 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.)

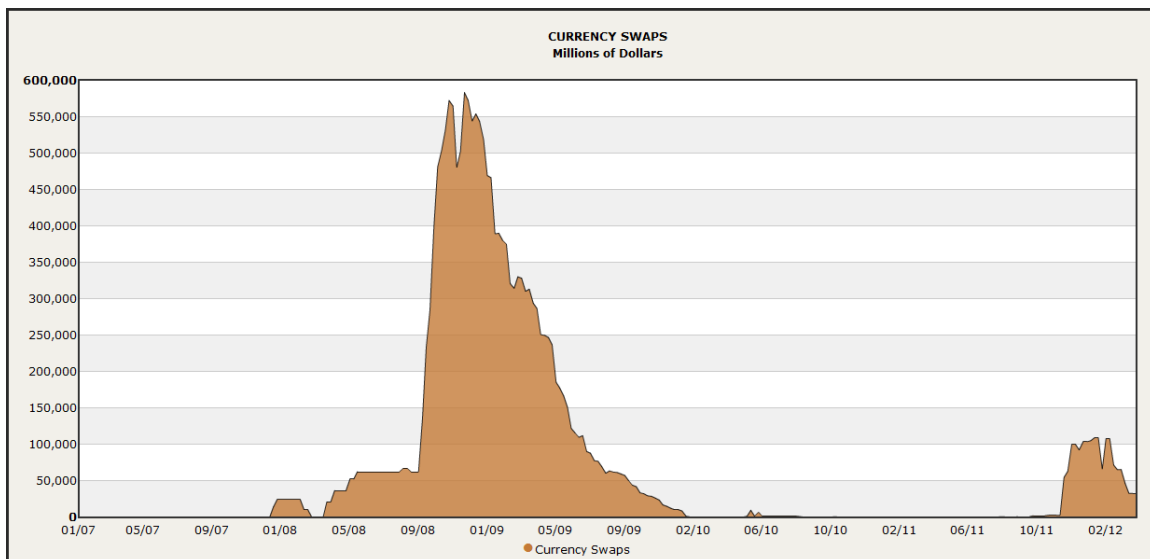
<http://www.quantifiableedges.com/members/pomo.php>



Despite 3 days of buying and only 1 day of selling this past week, the net result was a small (\$0.2 billion) outflow. The intermediate-term POMO indicators are now near the low end of their recent range. This suggests very little POMO stimulus from the Fed.

Until December the SPX chart had followed the intermediate-term POMO measurements very closely for 6 years. In December the market began a rally without strong POMO support. I noted in January that the Fed had begun to aggressively lend via currency swaps, primarily to aid Europe. This liquidity stimulus appeared to have a positive influence on the US market as well as the market rallied strongly through the end of March. This past month has been slightly negative. Below is an updated chart of open currency swaps taken from the Cleveland Fed's website.

http://www.clevelandfed.org/research/data/credit_easing/index.cfm



As you can see this stimulus has begun to be taken away, perhaps leading to the recent market struggles.

We will learn more about the timing of POMO activity when the Fed releases the May schedule on Monday afternoon, but the net stimulus is expected to be nominal with Operation Twist still in effect. Overall, from a liquidity standpoint, indications are neutral. Neutral levels of stimulus have led to market struggles over the last several years. The market has only produced strong rallies during times of strong stimulus.

Aside from the weak POMO schedule, we also need to be mindful of the weak net new highs, and possible negative impacts from rising interest rates. Intermediate-term bullish studies are still active. They consider the long-term trend, the breadth thrust in March,

and now again the leading Nasdaq. I remain neutral this week. I'm not seeing compelling enough evidence to produce strong a conviction about the intermediate-term. I will continue to play both the long and the short side fairly 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.

None tonight

Current Open Trade Ideas

| Symbol | Entry Date | Entry Price | Current Price | % Gain/Loss | Stop | Notes |
|----------|------------|-------------|---------------|-------------|------|------------|
| SPY(1/4) | 4/26/2012 | \$139.19 | \$140.32 | -0.81% | | Aggregator |
| | | | | | | |
| | | | | | | |
| | | | | | | |

I will cover my SPY lot on an SPX close \leq 1,392.50.

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 © 2012 Hanna Capital Management, LLC.