

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 26, 2012

Volume 5 Issue 143

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Long	100% Long XIV	Flat	Flat

## Tonight's Research Points

- 3+ days down with today being the mildest drop suggests an upside edge.
- A strong move up by the SOX while the Nasdaq declined hint at strength for Thursday..

## Short-term Outlook

### The Bottom Line

The outlook remains bullish. I'm still looking to get long that 2<sup>nd</sup> lot.

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

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
July 26, 2012	SOX up 1%. Nasdaq down.	1 day	Bullish	
July 25, 2012	3 dn from 50-hi. Under 10ma > 10-low	1-4 days	Bullish	1.90%
July 24, 2012	2 unfilled down gaps >200ma. 5 low	1-5 days	Bullish	1.80%
July 23, 2012	Big drop from 50-day high	1-4 days	Bullish	1.20%
<b>Active - Long Term</b>				
July 16, 2012	POMO modestly bullish	int term	Bullish	
June 13, 2012	FTD with modest breadth & vol	int term	Bearish	
February 1, 2012	Golden Cross	int term	Bullish	

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

***The Evidence***

The market made a few attempts to rally Wednesday, but could only manage a mixed finish. The SPX lost less than 0.1%, the Nasdaq dropped 0.3% and the Russell 2000 rose 0.2%. Breadth was also mixed as the NYSE Up Issues % came in at 53% and the Up Volume % was 49%. Total NYSE volume dipped some from Tuesday’s level.

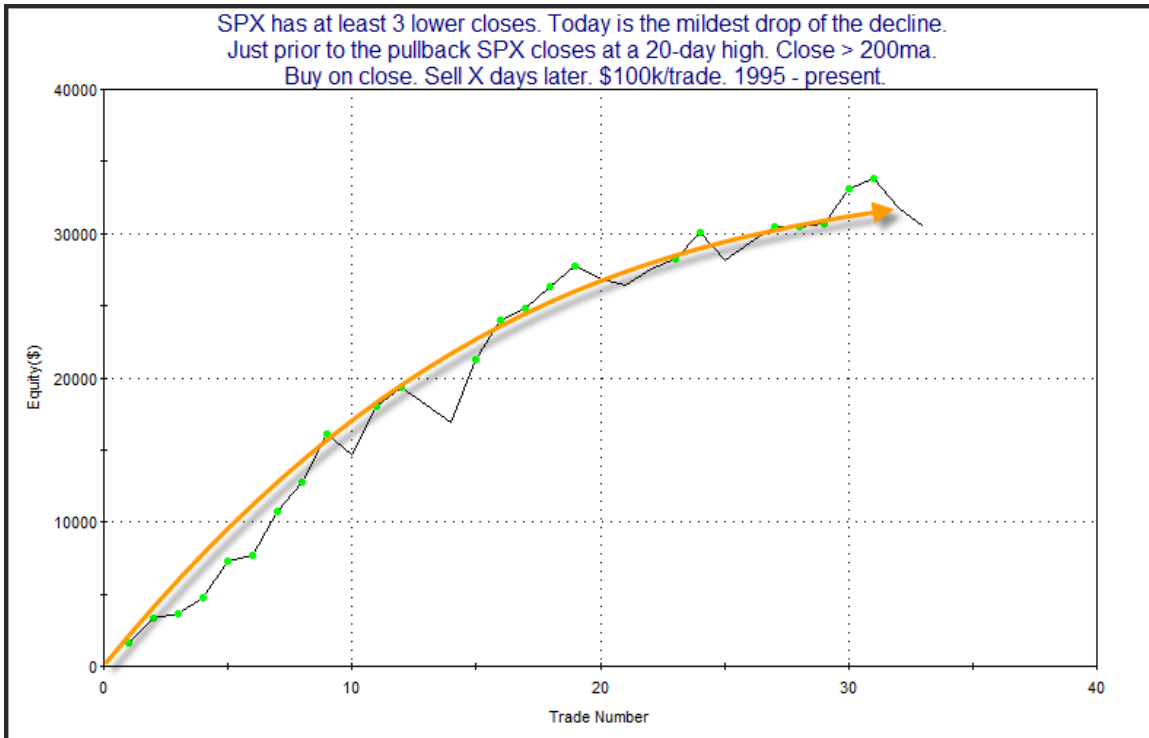
The 1<sup>st</sup> study I want to review tonight was last seen in the 4/9/12 letter. It examines 3+ day selloffs and looks for a relatively small drop to occur on the last day. This can suggest sellers are running out of steam. The stats table has been updated below.

SPX has at least 3 lower closes. Today is the mildest drop of the decline.  
 Just prior to the pullback SPX closes at a 20-day high. Close > 200ma.  
 Buy on close. Sell X days later. \$100k/trade. 1995 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Max Winning Trade	All: Max Losing Trade	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	41,835.30	31	23	8	74.19	7,183.08	-7,026.10	2,373.15	-1,593.39	1.49	4.28	1,349.53
9	42,824.38	31	24	7	77.42	6,685.72	-7,816.60	2,286.80	-1,722.69	1.33	4.55	1,381.43
8	40,823.08	31	24	7	77.42	6,017.68	-4,389.40	2,236.90	-1,837.51	1.22	4.17	1,316.87
7	34,076.70	32	22	10	68.75	6,121.80	-3,690.70	2,268.96	-1,584.05	1.43	3.15	1,064.90
6	34,775.24	32	21	11	65.63	5,533.56	-1,803.70	2,046.04	-744.68	2.75	5.25	1,086.73
5	31,473.82	33	24	9	72.73	5,769.16	-3,304.80	1,809.23	-1,327.52	1.36	3.63	953.75
4	30,633.64	33	20	13	60.61	4,989.40	-2,876.40	2,067.77	-824.75	2.51	3.86	928.29
3	30,459.54	33	25	8	75.76	4,373.80	-2,085.27	1,641.31	-1,321.66	1.24	3.88	923.02
2	24,835.27	34	26	8	76.47	3,583.44	-2,803.79	1,326.23	-1,205.82	1.10	3.57	730.45
1	10,586.79	37	26	10	70.27	1,767.00	-2,214.00	748.31	-886.91	0.84	2.19	286.13

**Only 2 instances failed to close above the entry price at some point in the next week.**

Results here are strong and are in line with the 3-day pullback studies I looked at last night. A 3-day profit curve can be found below.



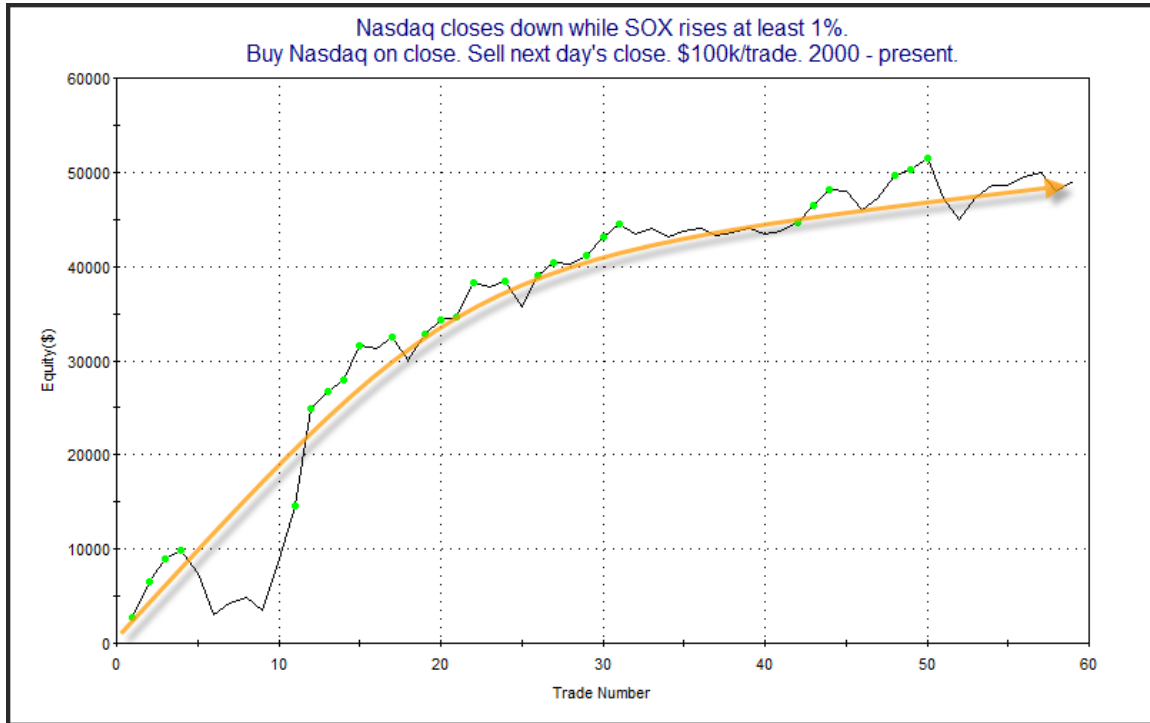
This curve is decelerating a little bit. The study still appears solid and worth consideration. I did not add it to the Active List though since it is so similar to last night's studies.

Another study I found worth reviewing was from the 5/29/12 subscriber letter. It looked at times where the NASDAQ composite declined while the SOX rose at least 1%. I have updated all the stats below.

Nasdaq closes down while SOX rises at least 1%.  
 Buy Nasdaq on close. Sell next day's close. \$100k/trade. 2000 - present.

TradeStation Performance Summary <span style="float: right;">Collapse ↕</span>			
All Trades			
Total Net Profit	\$49,137.08	Profit Factor	2.72
Gross Profit	\$77,679.92	Gross Loss	(\$28,542.84)
Total Number of Trades	59	Percent Profitable	71.19%
Winning Trades	42	Losing Trades	17
Even Trades	0		
Avg. Trade Net Profit	\$832.83	Ratio Avg. Win:Avg. Loss	1.10
Avg. Winning Trade	\$1,849.52	Avg. Losing Trade	(\$1,678.99)
Largest Winning Trade	\$10,390.72	Largest Losing Trade	(\$4,353.48)

Results here seem to suggest a 1-day upside edge for the Nasdaq. The “% Profitable”, “Profit Factor” and “Avg Trade” are all impressive. Below is a profit curve.



There appears to be some flattening in the curve as some of the biggest winners appeared early on. Still, the slope remains generally up and the study seems to be worth consideration.

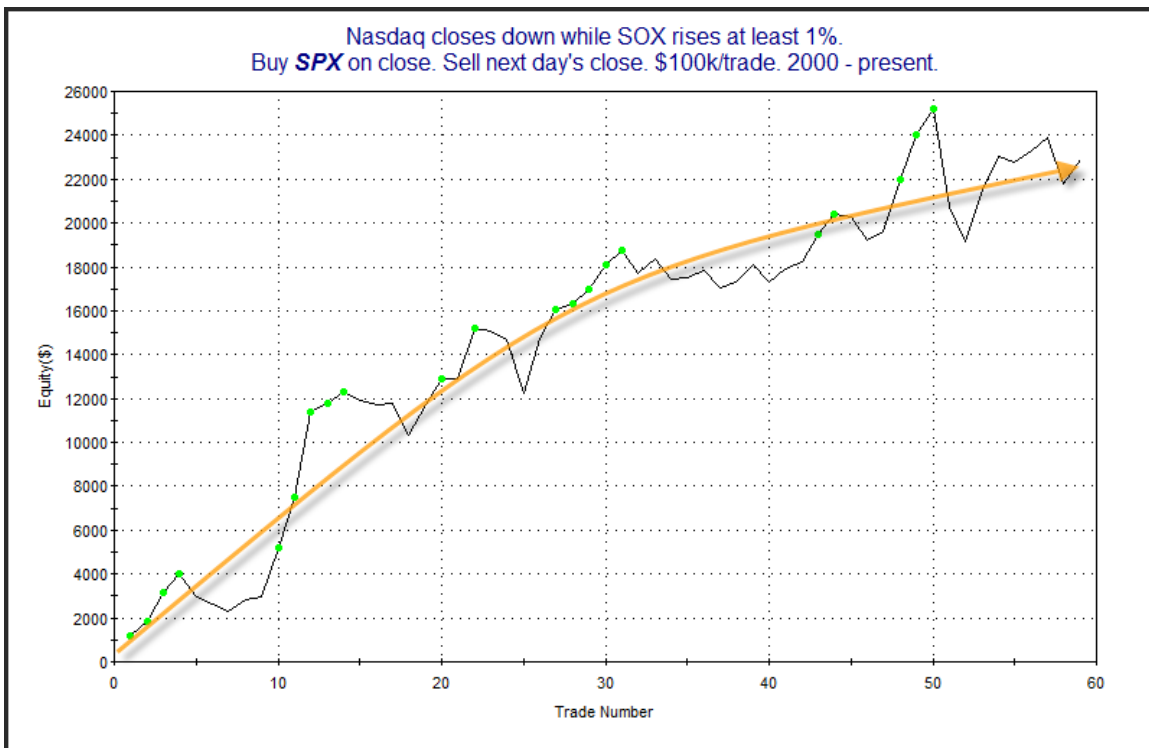
Of course the Aggregator anticipates SPX movement not Nasdaq movement, though the two are highly correlated. I decided to see how the SPX has performed when the setup triggered.

Nasdaq closes down while SOX rises at least 1%.  
Buy **SPX** on close. Sell next day's close. \$100k/trade. 2000 - present.

TradeStation Performance Summary <span style="float: right;">Collapse ▲</span>			
All Trades			
Total Net Profit	\$22,912.68	Profit Factor	2.14
Gross Profit	\$42,933.93	Gross Loss	(\$20,021.25)
Total Number of Trades	59	Percent Profitable	66.10%
Winning Trades	39	Losing Trades	20
Even Trades	0		
Avg. Trade Net Profit	\$388.35	Ratio Avg. Win:Avg. Loss	1.10
Avg. Winning Trade	\$1,100.87	Avg. Losing Trade	(\$1,001.06)
Largest Winning Trade	\$3,863.25	Largest Losing Trade	(\$4,520.40)

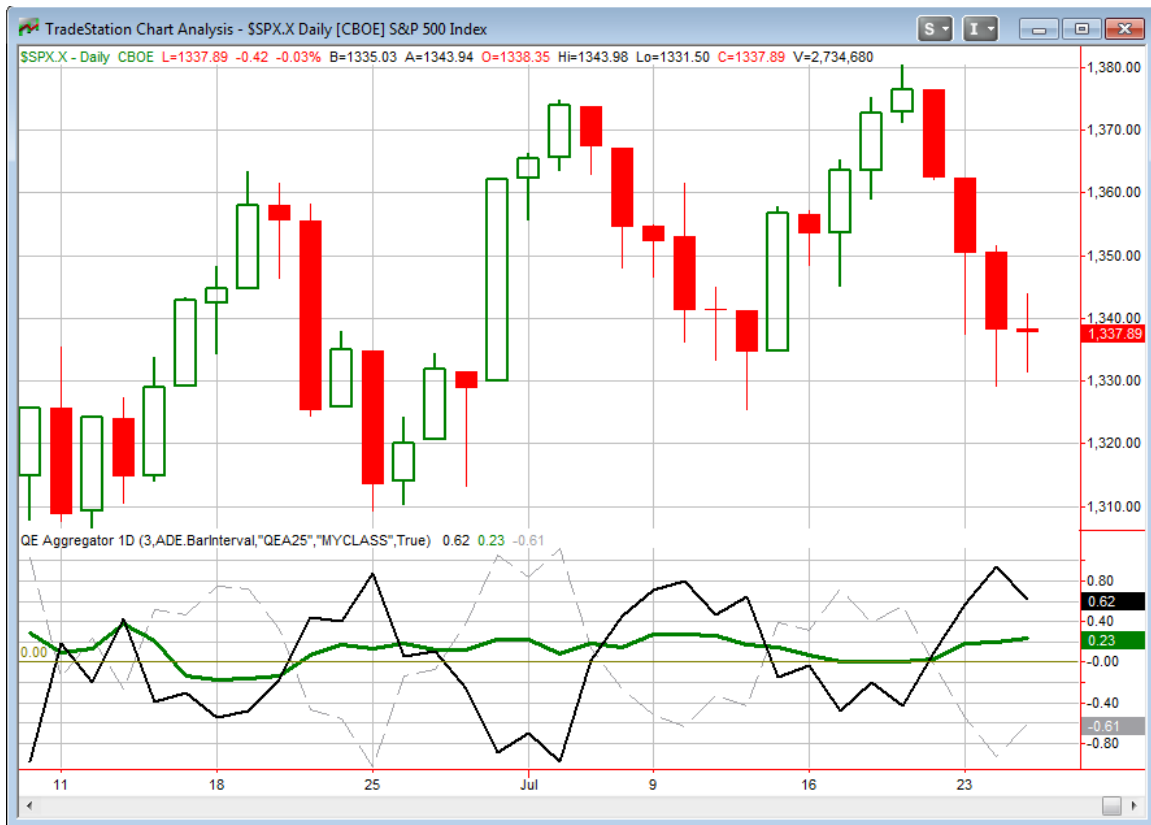
Based on these results it appears the SPX has benefitted as well. The strength of the upside edge isn't quite as strong though. The average instance sees a rise of about 0.4% instead of the 0.8% shown in the Nasdaq results. Traders looking to take advantage of the setup could consider trading the Nasdaq rather than the S&P in cases like this.

I also ran the SPX profit curve and have included it below.



The curve here appears similar to the Nasdaq profit curve without as much flattening.

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



With tonight's study factored in the green Aggregator Line again climbed further above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line pulled back a little but is still strongly above 0. This means the SPX is very oversold versus expectations. So net expectations are bullish and the SPX is strongly oversold versus recent expectations. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This meant the Aggregator System remained long at the close.

Based on the current studies, expectations are slated to remain bullish on Thursday. Of course that could change if bearish evidence emerges. The Differential Pivot will be 1,353.24 on Thursday. This is 1.15% above Wednesday's close. That's a fair amount of

ground to make up in just 1 day. A more likely scenario would be a multi-day rally or consolidation to work off the oversold condition.

Evidence continues to point higher, but evidence was ignored the last couple of days. Still, with the Aggregator suggesting a bounce and the QE Buying Power Index now at 3, I'm optimistic. I'll again look to take on a 2<sup>nd</sup> lot of SPY tomorrow if I can get a favorable entry price.

I'll also note that while the CBI is still 0, strong selling in the next couple of days could see it quickly spike. There are 5 or 6 stocks that could trigger Catapults as early as Thursday if they undergo much more selling. So while I was somewhat tempted to start picking trade ideas from the triggers sheet, I instead decided to wait for some Catapults and make another try for a favorable SPY entry.

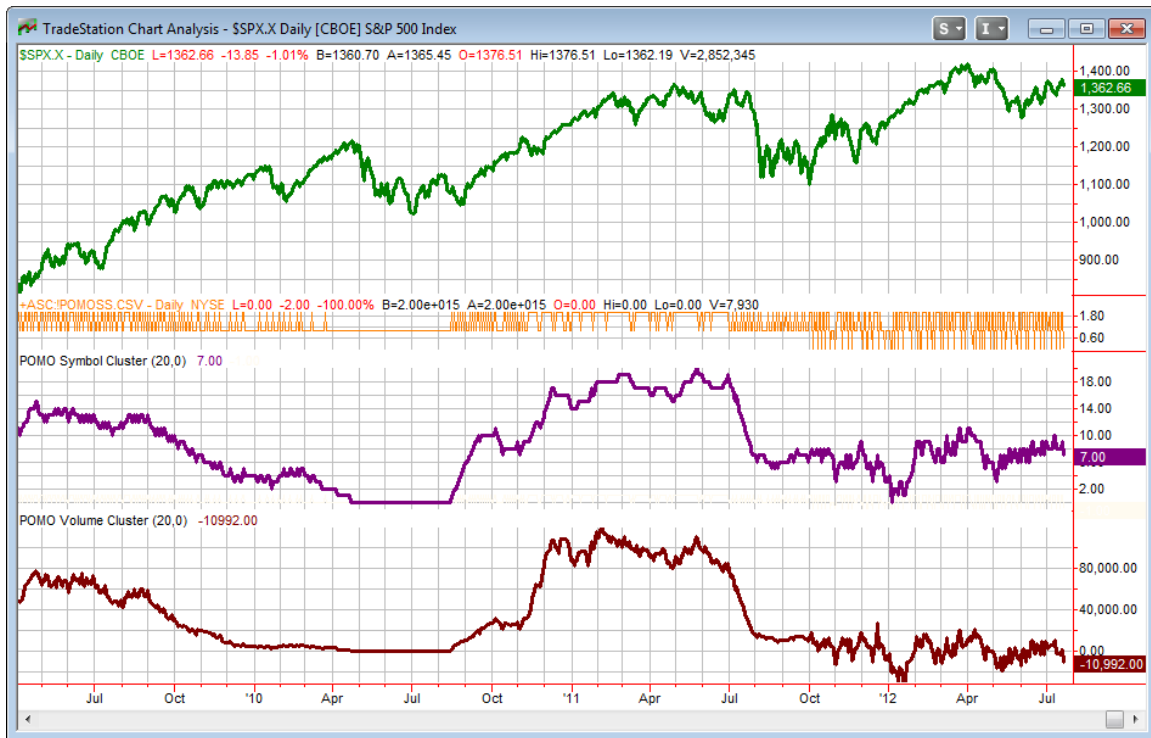
***Intermediate-term Outlook (2 weeks – 2 months)– updated 7/16 – slightly bullish***

Back and forth trading this week left the market up a mild 0.4%. Making a new 50 day high was somewhat encouraging, but strong upside evidence and momentum are still lacking.

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

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



As expected there were three days of POMO buying and two days of selling this past week. But the net outflows were larger than expected and amounted to \$7.5 billion. This left the intermediate-term indicators at their lowest points in quite a while, so it's not surprising to see that the market has made little progress over the last four weeks.

But from here through the end of the month POMO flows are expected to improve dramatically. There is only one selling day scheduled during the next seven trading days, with the rest all scheduled to see liquidity inflows. The net result of this buying is estimated to be about a \$12 billion inflow. The impact of this inflow is anticipated to be felt near the end of the month and the beginning of August.

Intermediate-term evidence remains mixed. I am feeling just slightly more bullish this week since we are now beyond last week's bout of POMO selling. Of course liquidity flows don't typically have an immediate impact and selling we saw this past week could continue to exert itself for several more days before the positive influence of the upcoming inflows takes over. While choppy, the trend also appears to favor the bullish case. So as has been the case recently, I am still more willing to buy oversold than I am to short overbought.

## **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 – buy ¼ index position @ \$133.50 LIMIT ON OPEN. If NOT filled on open, cancel order and look to enter this lot @ \$134.00 LIMIT ON CLOSE.*** This is based on the short-term outlook above. I am looking to get long a 2<sup>nd</sup> lot of SPY.

## **Current Open Trade Ideas**

<b>Symbol</b>	<b>Entry Date</b>	<b>Entry Price</b>	<b>Current Price</b>	<b>% Gain/Loss</b>	<b>Stop</b>	<b>Notes</b>
SPY(1/4)	7/23/2012	\$135.09	\$133.96	-0.84%		Aggregator

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