

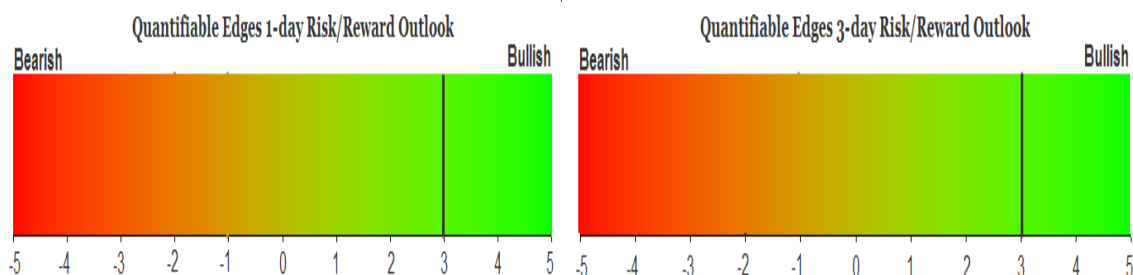
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

September 5, 2012

Volume 5 Issue 171

## Market Overview



## Signals Overview

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

## Tonight's Research Points

- The SPX down close on solid breadth suggests a short-term upside edge.
- The Russell 2000 rising > 1% while SPX closes lower also suggests a short-term upside edge.

## Short-term Outlook

### The Bottom Line

I'm still partially long and expecting higher prices over the next few days. I may begin selling if we move higher tomorrow.

## 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 5, 2012	SPX down. NYSE Up Issues % > 55%	1-2 days	Bullish	
September 4, 2012	Post Labor-Day negative seasonality	1-4 days	Bearish	-1.30%
September 4, 2012	Early-month oversold in uptrend	1-5 days	Bullish	2.20%
August 31, 2012	QE Buying Power Swing System	1-3 days	Bullish	1.80%
<b>Active - Long Term</b>				
August 22, 2012	Key Downside Reversal from High	1-12 days	Bullish	
August 10, 2012	SPX & TNX 50-day highs.	1-20 days	Bearish	
July 30, 2012	SPX 50-day high on 90% up vol	1-50 days	Bullish	
July 16, 2012	POMO modestly bullish	int term	Bullish	
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***

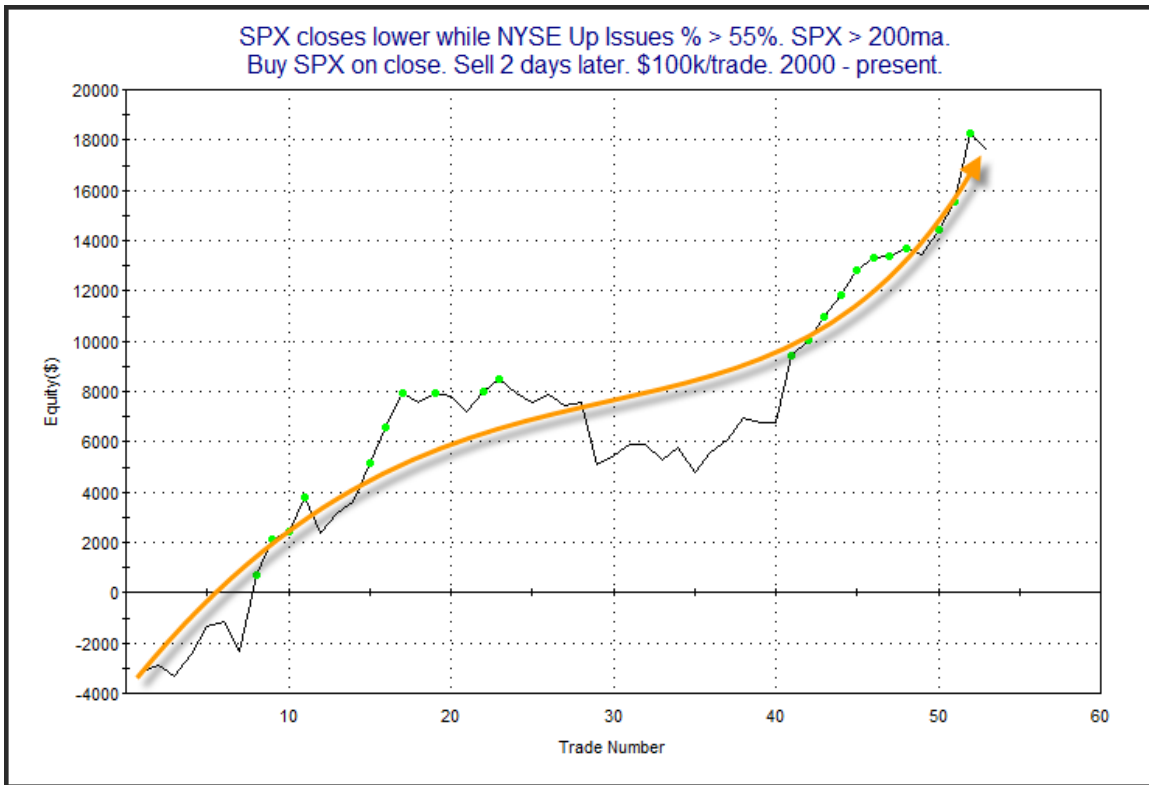
Morning selling petered out around 11am and the market bounced back to finish mixed. The SPX lost 0.1%, the Nasdaq rose 0.3% and the Russell 2000 closed up 1.2%. Breadth was positive as the NYSE Up Issues % was 59% and Up Volume % came in at 51%. Total NYSE volume dipped some from Friday’s level.

The study below looks at strong breadth on a day the SPX declines. It appeared just last week in the 8/29/12 letter. Results are updated again.

SPX closes lower while NYSE Up Issues % > 55%. SPX > 200ma. 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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	24,757.23	47	27	20	57.45	2,084.80	7,183.08	-1,576.62	-4,406.82	1.32	1.79	526.75
9	28,135.46	47	32	15	68.09	1,804.71	5,597.64	-1,974.36	-4,873.44	0.91	1.95	598.63
8	25,701.48	47	33	14	70.21	1,660.63	5,105.16	-2,078.53	-4,715.80	0.80	1.88	546.84
7	18,037.71	47	32	15	68.09	1,450.88	4,736.88	-1,892.69	-6,585.48	0.77	1.64	383.78
6	15,057.55	48	33	15	68.75	1,370.13	3,398.72	-2,010.45	-9,589.14	0.68	1.50	313.70
5	20,975.32	48	31	17	64.58	1,391.12	3,616.92	-1,302.91	-4,012.80	1.07	1.95	436.99
4	20,039.99	50	31	19	62.00	1,334.24	3,429.00	-1,122.18	-2,921.28	1.19	1.94	400.80
3	19,665.77	52	36	16	69.23	975.92	3,373.50	-966.70	-2,852.01	1.01	2.27	378.19
2	17,602.89	53	37	16	69.81	850.88	3,025.12	-867.48	-3,119.03	0.98	2.27	332.13
1	14,616.69	55	34	21	61.82	726.35	2,484.00	-479.97	-1,348.29	1.51	2.45	265.76

**88% of instances closed above the entry price at some point in the next week.**

The edge isn’t huge, but it does appear to be high-percentage. The equity curve below gives a better idea of how the edge has played out over time.



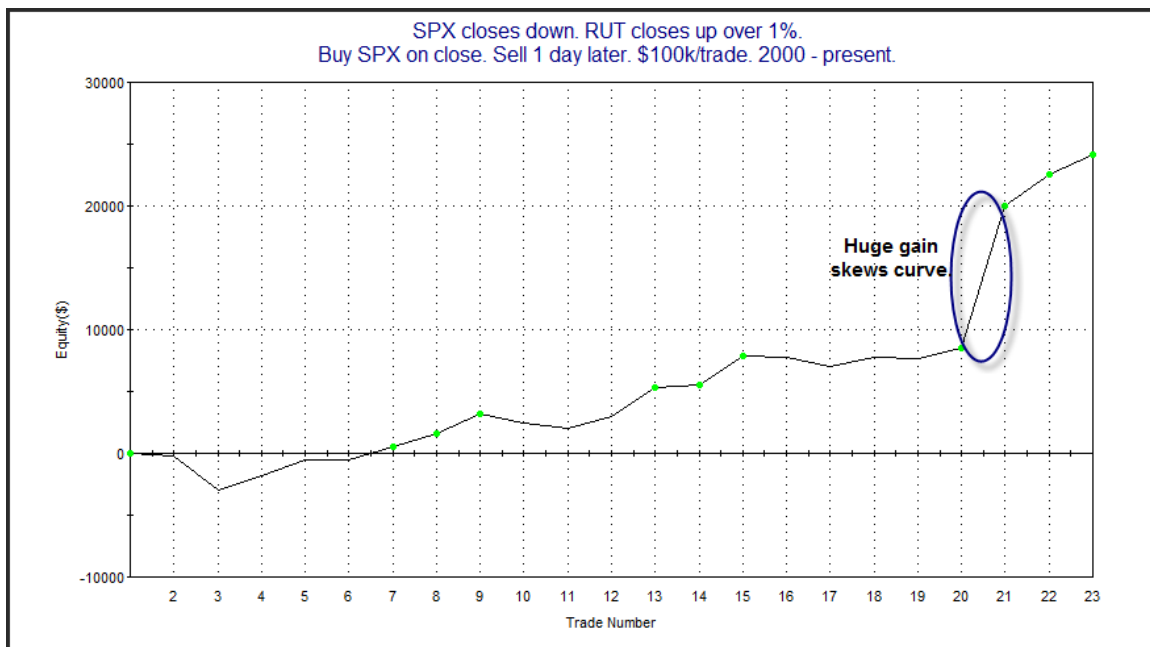
While the curve certainly appears choppy, the edge has been very strong lately. The 3-5 day charts don't see quite as pronounced of a dip in the middle, which also alleviates some concern. I believe this study is worth taking into consideration and I've again included it among the active studies.

I also ran a study tonight that looked at other times the Russell 2000 closed up over 1% while the SPX closed down. There appeared to be possible bullish consequences for the following day, but not beyond that. Below are some stats assuming a 1-day holding period.

SPX closes down. RUT closes up over 1%.  
Buy SPX on close. Sell 1 day later. \$100k/trade. 2000 - present.

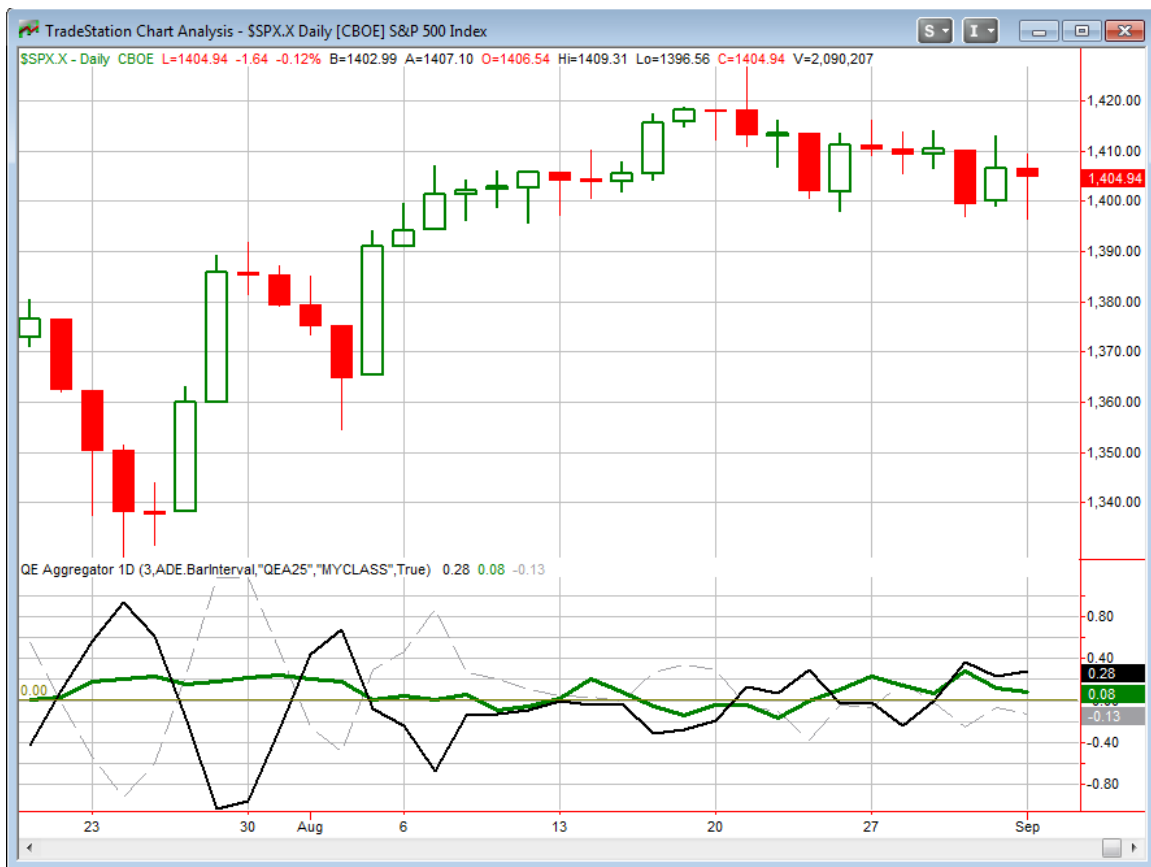
TradeStation Performance Summary <span style="float: right;">Collapse ^</span>			
All Trades			
Total Net Profit	\$24,169.65	Profit Factor	5.63
Gross Profit	\$29,384.29	Gross Loss	(\$5,214.64)
Total Number of Trades	23	Percent Profitable	69.57%
Winning Trades	16	Losing Trades	7
Even Trades	0		
Avg. Trade Net Profit	\$1,050.85	Ratio Avg. Win:Avg. Loss	2.47
Avg. Winning Trade	\$1,836.52	Avg. Losing Trade	(\$744.95)
Largest Winning Trade	\$11,558.43	Largest Losing Trade	(\$2,722.05)

Stats here are very strong, but there was one big gain that skewed the curve. This can be seen below.



If we take out that one gain the average trade is still nearly 0.6%, so while the edge is exaggerated in the stats table, there does appear to be one. Since I am using another study that looks at the smallcap / largecap divergence I did not include this among the active studies. Still the confirmation is comforting.

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



With tonight's study factored in the green Aggregator Line remained above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is also still squarely positive. This means the SPX is oversold versus recent expectations. So net expectations are bullish and the SPX is currently oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This lead the Aggregator to remain long at the close. This was indicated as likely on the systems page shortly before the bell.

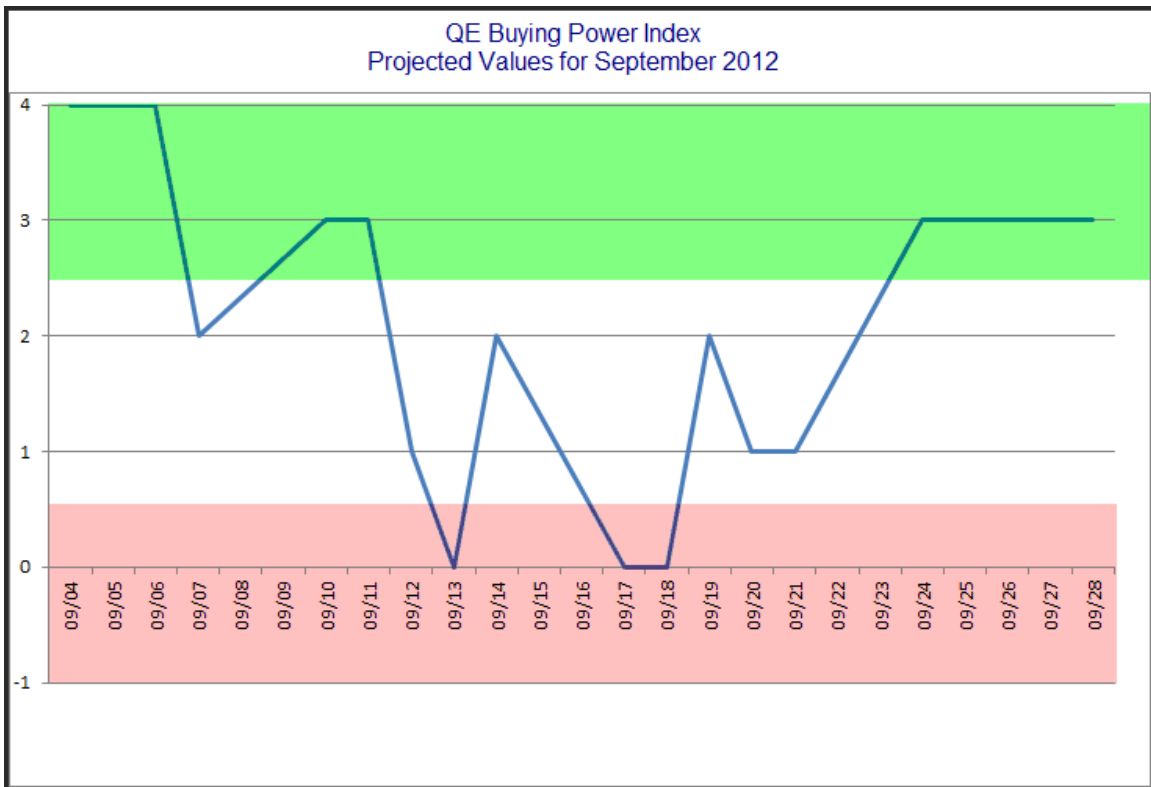
Based on the current open studies, expectations are scheduled to remain positive on Wednesday. Of course this could change if more bearish evidence emerges. The Differential Pivot will be 1,406.52 on Wednesday. This is just 0.1% above Tuesday's close. So just about any close higher would move the SPX back into overbought territory.

There still appears to be some more room left in this bounce. I'll look to ride it another day. If we do move higher as expected and close above the Differential Pivot, then I will take profits on my SPY position.

**Intermediate-term Outlook (2 weeks – 2 months)– updated 9/4– bullish**

For the 2<sup>nd</sup> week in a row the SPX underwent a mild pullback. Action for most of the week was very mild and it failed to generate any studies of intermediate-term significance. But the September POMO schedule was announced and that made for some interesting liquidity flow data.

Based on the POMO schedule I have generated the QE Buying Power Index chart for September. It can be found on the QE Buying Power Index page at any time. I've also copied the chart below.



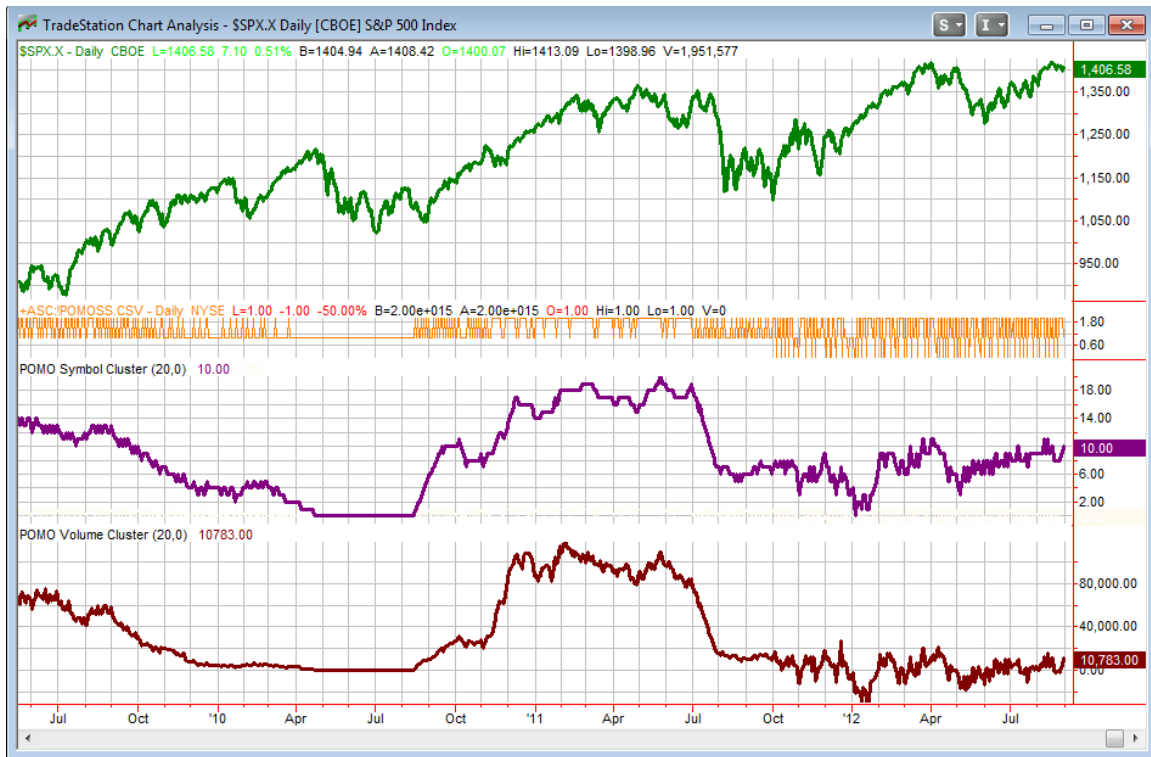
There appear to be 3 distinct periods to keep an eye on in September. The early part of the month is showing strongly positive flows. We could see the market rally during this time. During the middle of the month POMO flows will be negative. If we are going to see a selloff during September, this would seem to be the most opportune time for the bears to push the market lower. Once the last week of the month arrives flows will turn positive once again and act as a wind to the market's back.

On a net basis September is expected to see \$45 billion in buying and \$38 billion in selling. The \$7 billion difference would mean the largest monthly liquidity infusion since Operation Twist began last October, topping the \$6 billion of July and August. As I mentioned above it is front and back loaded though. The first 3 days of September are scheduled for \$13 billion in buying. Then from the 7<sup>th</sup> – 20<sup>th</sup> there will be net selling of over \$13 billion. Finally, between the 21<sup>st</sup> – 30<sup>th</sup> we'll see \$7 billion in buying.

I've updated the intermediate-term POMO chart each weekend in the letter. For those who may not recall below is a brief refresher on it. Beneath that is the 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>



This past week saw 4 days of POMO buying and 0 days of selling. The net result was a \$13.1 billion liquidity infusion. The intermediate-term indicators are both now near their highs for the last few months.

This upcoming week is scheduled to see strong buying Tuesday-Thursday. Friday will mark the beginning of the mid-month selling period. The net for this week is expected to be about a \$5.6 billion inflow, which could help the market into the following week. For anyone that would like to review the current schedule, below is a link to the fed's website.

[http://www.newyorkfed.org/markets/tot\\_operation\\_schedule.html](http://www.newyorkfed.org/markets/tot_operation_schedule.html)

We had 2 intermediate-term studies expire this week, leaving the bond-rate study as the only bearish one on the board. The bulls can look to a few positives. The uptrend is firmly intact. Momentum is positive, the Nasdaq is in a leading position, and we have existing breadth and price-related studies pointing higher. Lastly, POMO flows are positive and will continue to be so for the next few days. I remain bullish for the next few days, but will likely move toward neutral next week as POMO flows turn south.

## **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
XIV(1/2)	8/28/2012	\$13.88	\$14.01	0.94%		Aggressive VIX
SPY(1/4)	8/31/2012	\$140.49	\$141.03	0.38%		sell on SPX close>1,406.51

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