

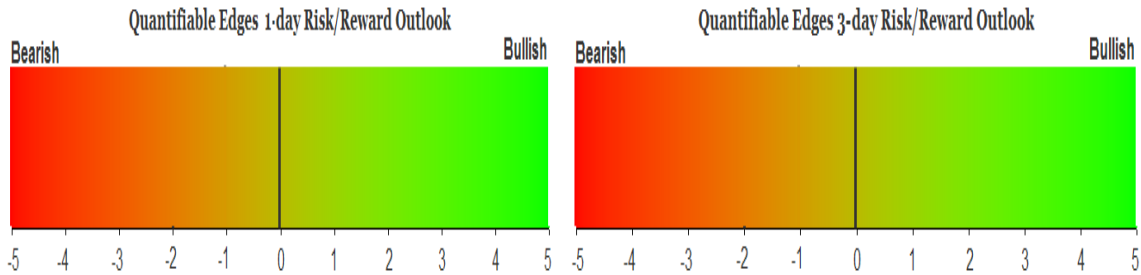
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 1, 2013

Volume 6 Issue 61

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Flat	50% Long XIV	Flat	Flat

Tonight's Research Points

- The first few days in April have been especially strong over the last 19 years.
- Liquidity flows are expected to remain strong in April, but on a relative basis they will not be as strong as we have seen in recent months.

Short-term Outlook

The Bottom Line

Expectations are increasingly positive, but the market is increasingly overbought. So I am generally neutral and am not looking to add exposure on Monday.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
April 1, 2013	Early April strong	1-4 days	Bullish	2.00%
March 27, 2013	Low volume breakout	1-5 days	Bullish	
Active - Long Term				
March 13, 2013	5 days up to 50-high, then 1 down	1-10 days	Bullish	2.00%
January 14, 2013	Breadth Divergence (from Tops Study)	int term	Bearish	
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
March 28, 2013	Holy Thursday	1 day	Bullish	

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

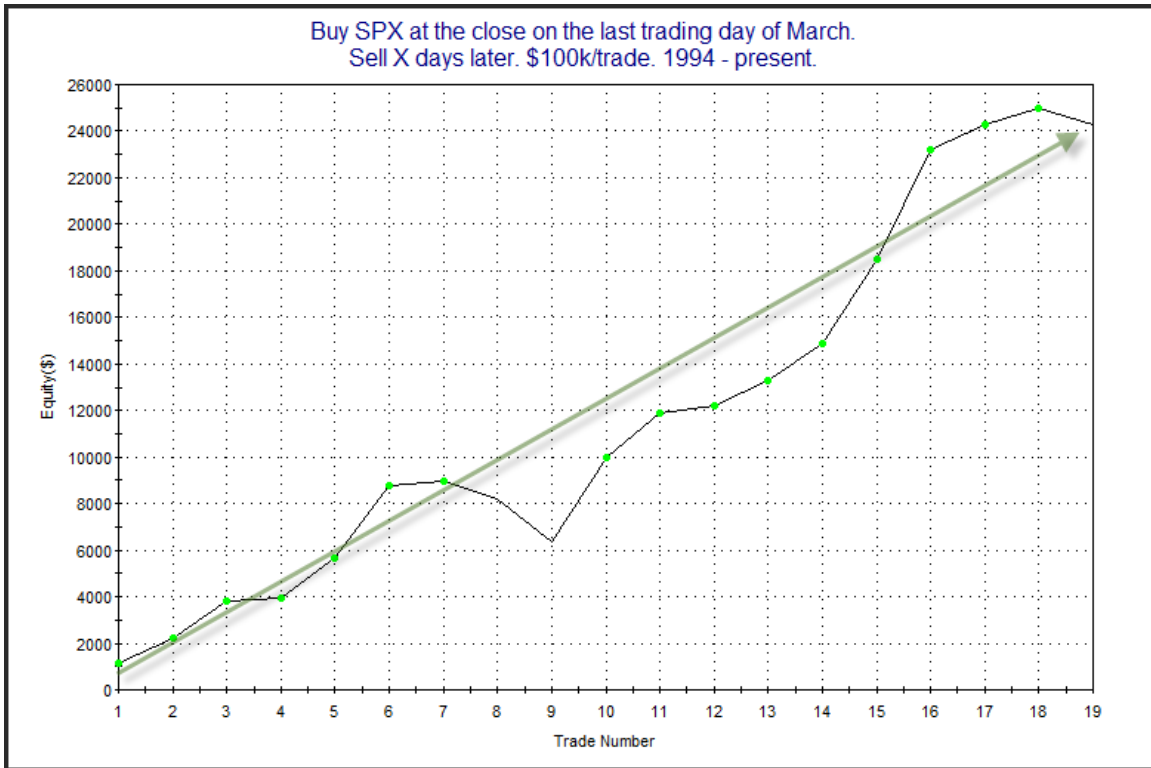
The Evidence

All time highs. Only 4 years after the “666” bottom, SPX closed at 1569.19 and new all-time highs. Not all indices did the same but they did rise on Friday. The SPX finished up 0.4%, the Nasdaq rose 0.3% and the Russell 2000 gained 0.1%. Breadth was positive as the NYSE Up Issues % was 64% and the Up Volume % came in at 63%. Total NYSE volume came in at the highest level in about a week and a half.

Despite the market closing at new highs, no bearish Quantifinder studies appeared suggesting SPX is so overbought that it is likely to pull back short-term. There were a number of bullish studies that triggered related to Monday being the 1st trading day of the month. In the 4/2/12 letter I showed that April has not only shown a propensity for a strong 1st day, but the first week has generated impressive numbers. I have updated that study below.

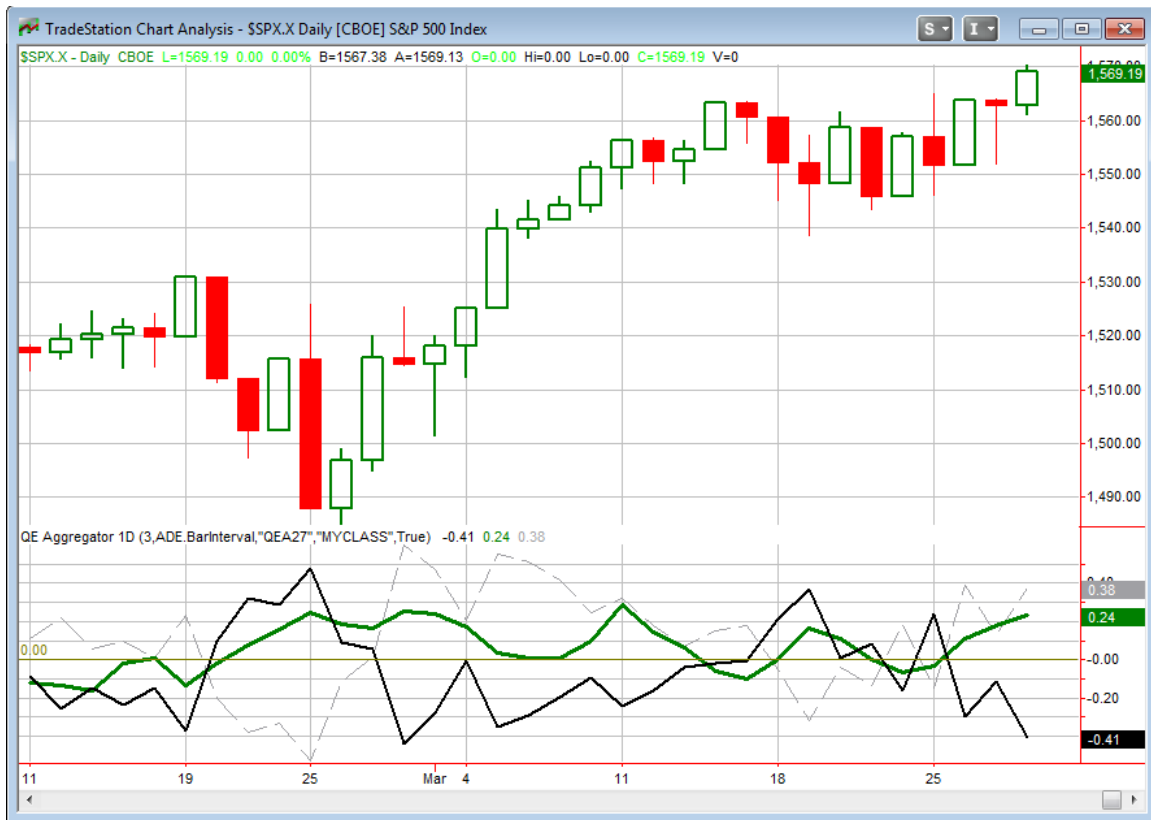
Buy SPX at the close on the last trading day of March. Sell X days later. \$100k/trade. 1994 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	17,020.44	19	15	4	78.95	1,596.26	4,435.97	-1,730.87	-2,745.12	0.92	3.46	895.81
4	24,279.98	19	16	3	84.21	1,725.14	4,701.25	-1,107.44	-1,831.35	1.56	8.31	1,277.89
3	18,714.78	19	15	4	78.95	1,806.73	5,578.75	-2,096.54	-4,909.74	0.86	3.23	984.99
2	17,738.87	19	14	5	73.68	1,775.46	4,563.75	-1,423.51	-4,638.84	1.25	3.49	933.62
1	9,344.62	19	15	4	78.95	855.96	3,559.50	-873.71	-1,532.16	0.98	3.67	491.82

Last April we saw a strong day 1, but after that there was a sharp pullback for the rest of the week. Still, the numbers here are quite impressive. The edge appears to max out on day 4. Below is a profit curve using a 4-day exit strategy.



The strong, steady upslope appears to confirm the bullish edge. This is much preferable to a large percentage of the gains occurring on a small percentage of trades. And at this point last year looks like nothing more than a minor blip.

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



With strong early-April seasonality factored in, the green Aggregator Line rose 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 is well below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are bullish but the SPX is already overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. This caused the Aggregator system to remain flat at the close.

Based on the current studies, expectations are slated to remain bullish on Monday. Of course that could change if new bearish evidence emerges. The Differential Pivot will be 1,563.92 on Monday. This is just 0.3% below Thursday's close. So it would not take much of a pullback to move SPX from overbought to oversold versus expectations. And if it should happen, we could see a short-term buying opportunity.

But while a pullback might get me to add long exposure, I am not ready to do so just yet. I will instead wait for a setup with a more favorable risk/reward outlook. Buying when the market is already short-term extended would leave me open to that pullback. And I would prefer to avoid at least part of it. So there is nothing for me to do but wait a day or so and see what evolves.

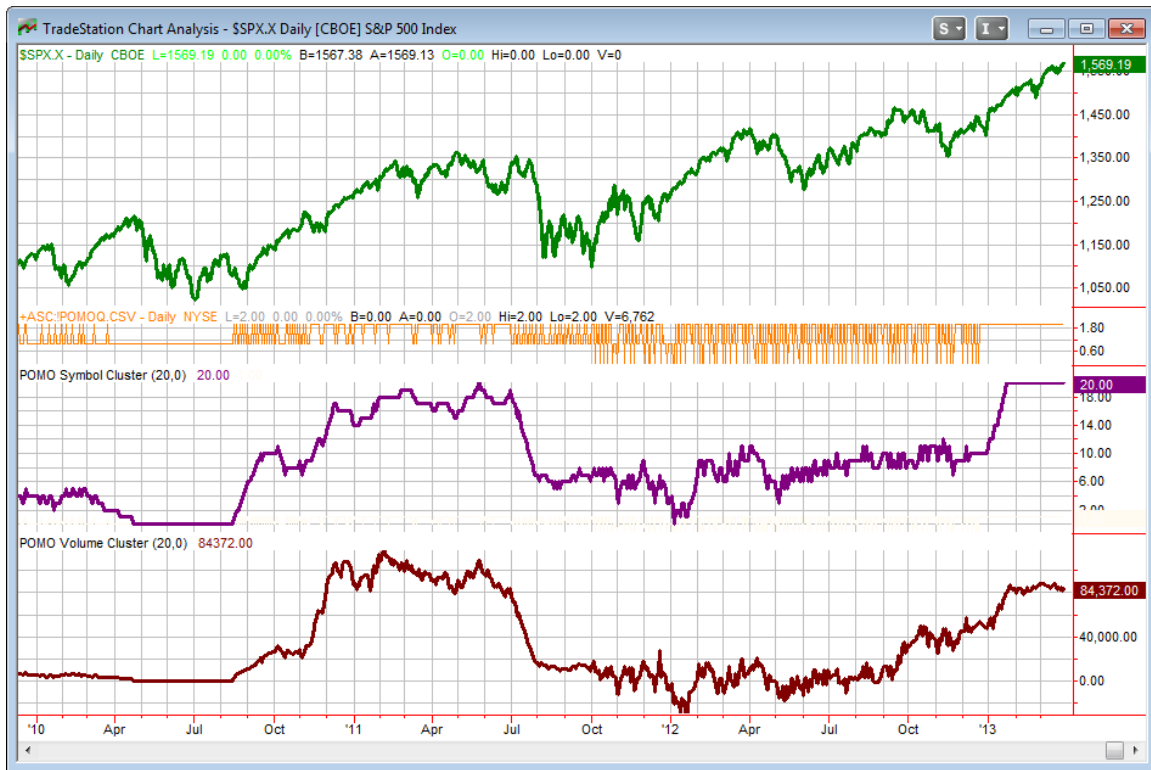
Intermediate-term Outlook (2 weeks – 2 months)– updated 4/1 – bullish

Closing at an all-time high is generally a good way to settle any debate as to whether the market is in an uptrend or a downtrend. Rarely will I battle trend on an intermediate-term basis, and especially a trend that has been as strong and persistent as this one. But it is still wise to continually look for cracks under the hood.

Since I updated the QE Study of Tops in January (it can be found on [members download page](#)) I have been keeping a close eye on the number of new highs being made on the NYSE. And while SPX is now at an all-time high, the number of individual issues hitting new highs remains in a divergence. On Thursday there were 374 issues that hit a new high. This is far under the both peak number of 483 back on September 14th as well as the 476 hit on January 24th. So the divergence remains in place for now, leaving open the possibility that a top could form leading to a major decline. An expansion of new highs above the 483 level (or more precisely, the % of NYSE stocks hitting a new high reaching above 15.73%) would greatly reduce the possibility of a major decline beginning in the next few months.

I update the intermediate-term POMO/QE chart each week. For those not familiar, below is a brief description.

POMO stands for Permanent Open Market Operations and it is how the Fed has gone into the open market to buy securities over the last several years. 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 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. Since the Sept 13, 2012 QE3 announcement the POMO numbers are also adjusted to reflected the Fed’s new approach of buying AMBS securities. Therefore, prior to that date the indicators just look at POMO, since that date it is a combination of POMO and AMBS flows.

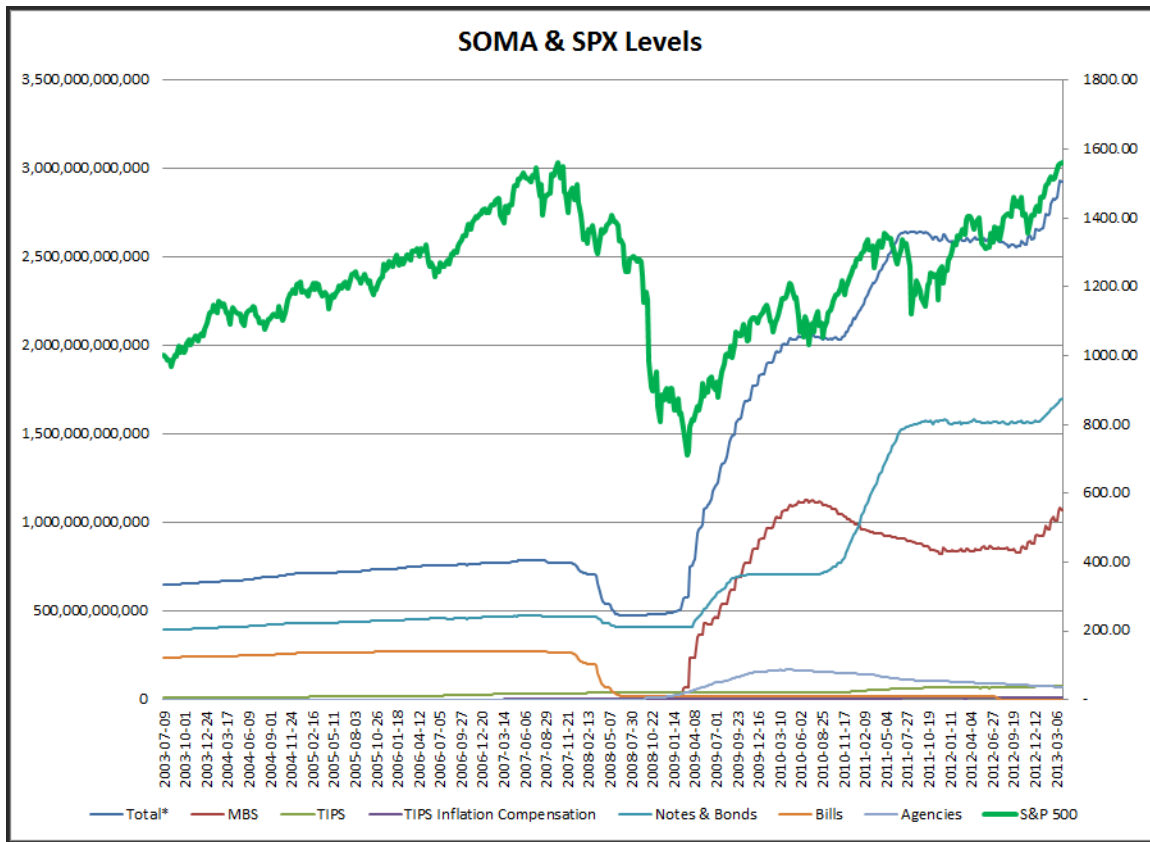


The POMO/AMBS volume indicator remained elevated in its 2013 range again this week. And the days indicator is *still* maxed out at 20, which was a rarity during past QE implementations, but has been the norm so far this year. We estimate net inflows this past week to have been about \$18.9 billion. That is again a strong week, especially for one with only 4 days. Numbers like this normally provide a nice bullish wind at the market's back in the following days.

This upcoming week is also expected to see fairly strong liquidity. Between POMO and AMBS we should see about an \$18.6 billion inflow. That is a little less than last week. And as I will discuss below, we can expect levels to remain a little lower during April. The liquidity environment is one that appears to continue to be bullish, but perhaps not quite as bullish as it has been recently.

With the release of the April POMO schedule on Thursday I was able to produce the projected QE Buying Power Index for April. The estimated totals for April remain the same as they have been for the last few months, with \$45 billion in POMO and another \$40 billion in AMBS purchases expected.

But while the net amounts are the same, there are some differences that could be worth consideration. The 1st concern is that the level of stimulus, while constant, is becoming smaller on a percentage basis. This can best be seen with the SOMA chart below, which I last showed about a month ago.



For those that do not recall, SOMA is defined below by the Fed.

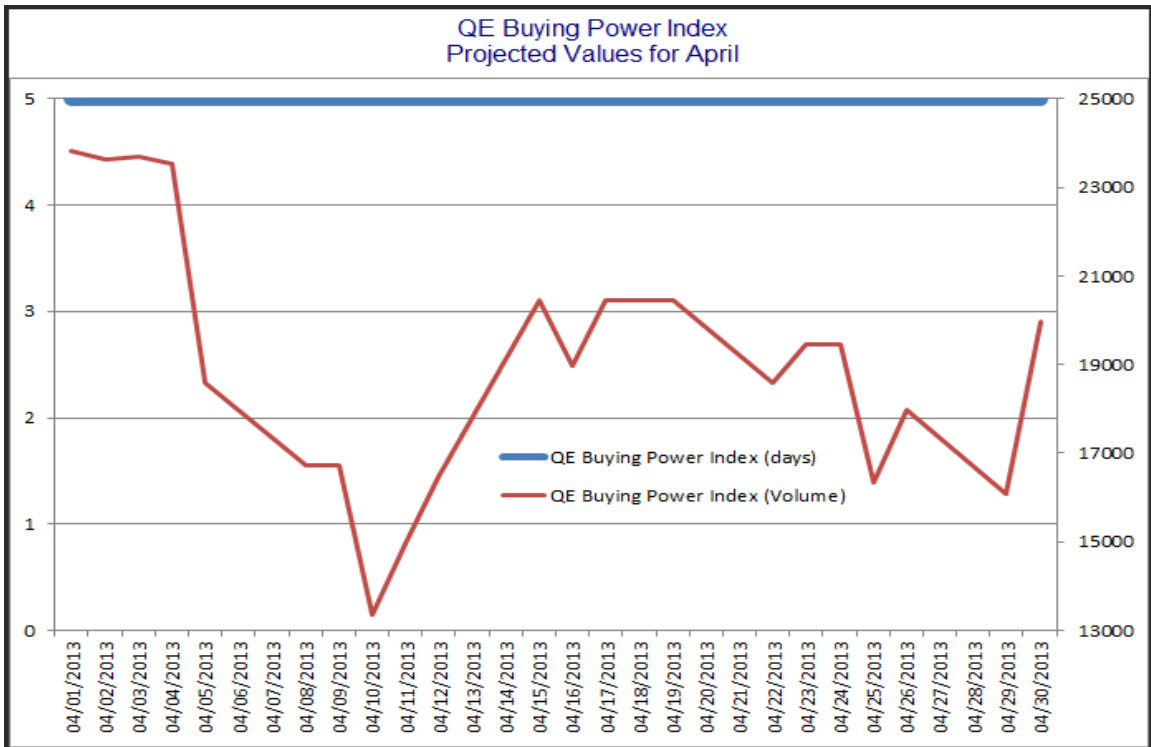
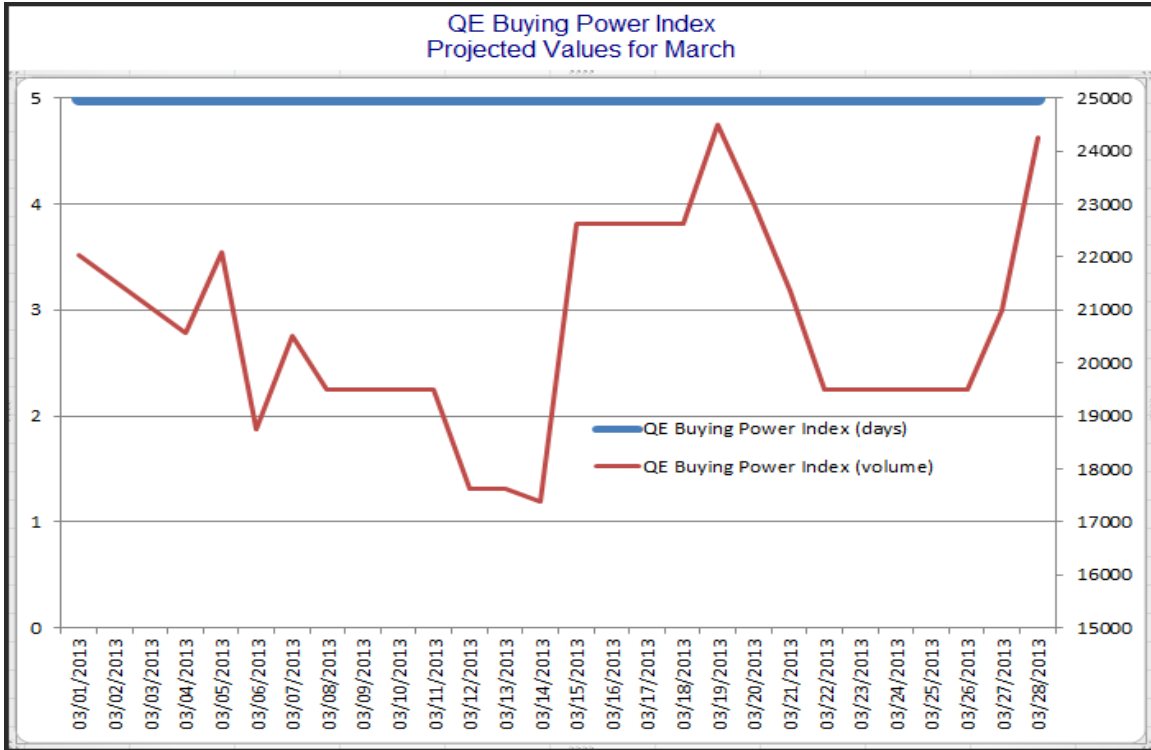
The System Open Market Account (SOMA), managed by the Federal Reserve Bank of New York, contains dollar-denominated assets acquired via open market operations. These securities serve three purposes:

- Collateral for U.S. currency in circulation and other reserve factors that show up as liabilities on the Federal Reserve System's balance sheet
- A tool for the Fed's management of reserve balances
- A store of liquidity in the event an emergency need for liquidity arises

The darker blue line represents the total SOMA account value. It is no surprise that the stock market has been performing so strongly this year as the size of the SOMA account has grown from \$2.65 trillion at the end of December up to \$2.93 trillion as of Wednesday. If the Fed pumps \$85 billion in April, that would represent about 2.9% of the size of the current SOMA account. In January that same number would've been 3.2%. So the same stimulus is being applied to a larger base, and at some point the impact will be lessened.

Another factor that could potentially lower the impact this month is the increased number of trading days in April. March had 20 trading days. February had 19. April the NYSE

will be open for 22 days. This reduces the size of the average day from \$4.25 billion to \$3.86 billion. Below are the projected QE Buying Power Index charts for both March and April, so that you may compare the volume sizes. (QE Buying Power Index Volume is a cumulative 5-day total of both POMO and AMBS transactions.)



Whereas March bottomed out above \$17 billion and was over \$20 billion on a fairly regular basis, April will spend most of the month below the \$20 billion level, and will also reach as low as \$13 billion on the 10th of the month.

Of course the anticipated stimulus for April remains high, and the market is much better off with this kind of wind at its back than if there were no stimulus, or if there was a tightening policy. But the size of the stimulus will be shrinking, both on a relative, and an average daily basis. And that *could* open the door for a possible pullback. Based on the QE Buying Power Volume indicator and the April seasonality study from the short-term section above, I would not expect a pullback to begin in the first few days of the month.

Overall, intermediate-term evidence is mixed but bullish in my view. On the negative side we are still cognizant of the breadth divergence from the Study of Tops. But liquidity and momentum are both positive and they have been difficult to bet against, even short-term, in 2013. Until I see evidence of a change in trend I'll continue to favor the long side.

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
BRF	3/22/2013	\$40.38	\$40.32	-0.15%		sell @ \$40.54 limit on CLS

BRF will trigger an exit on a close \geq \$40.54.

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