

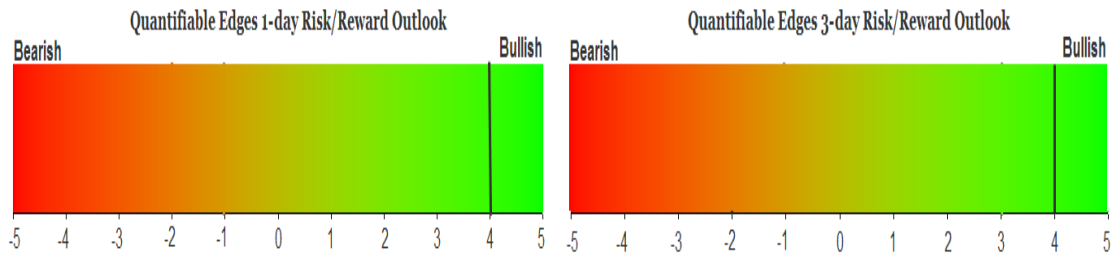
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 1, 2011

Volume 4 Issue 146

Market Overview



Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Long	100% Long XIV	100% Long XIV	Long

Tonight's Research Points

- Selloffs at the end of the month are often reversed when the new month begins.
- The extremely low TICK Tomoscillator is suggesting a short-term bounce.
- The SPY pattern of a gap down and close above the open but still negative appears to suggest bullish implications.
- The VIX is near a level that would strongly suggest a short-term SPX rally.
- POMO indicators are still quite a bit above 0 even though QE2 is no longer an influence.

Short-term Outlook

The Bottom Line

The market remains primed for a bounce. I am positioned to take advantage of it and may increase my long holdings further if opportunity allows.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
August 1, 2011	SPY gap dn and partial reverse	1-3 days	Bullish	1.50%
August 1, 2011	Tomoscillator < -200. SPX 5-day low.	1-2 days	Bullish	1.70%
August 1, 2011	Down last 3 days of month	1-5 days	Bullish	2.60%
July 29, 2011	4 lower lows. 20-day low. Close >200	1-8 days	Bullish	2.40%
July 28, 2011	2% drop. Weak close.	1-3 days	Bullish	
July 28, 2011	system 110524	1-6 days	Bullish	
July 28, 2011	3 dn. Big drop.	1-5 days	Bullish	
Active - Long Term				
July 22, 2011	Up Issue% > 75% 2 of 3. Close 10 high.	1-20 days	Bullish	5.50%
July 5, 2011	QE2 Over	int term	Bearish	
July 5, 2011	3 days higher. Up vol % > 90% today.	1-20 days	Bullish	5.00%
June 22, 2011	FTD with Up Issues % 1-yr Rank > 95%	int term	Bullish	
May 31, 2011	4 Weeks Down. Close > 40ma.	1-10 weeks	Bullish	9.00%
March 22, 2011	3 Days Up Issues % > 70%	8 months	Bullish	19.00%
October 25, 2010	SPX Golden Cross	int term	Bullish	
Dropped Tonight				
July 22, 2011	Up Issue% > 75% 2 of 3. Close 10 high.	1-6 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

After filling a large gap down in the morning the market suffered another afternoon fade and closed in the lower half of its range. The major indices all finished lower again as worries about government negotiations have weighed on the market all week. Final numbers showed the SPX down 0.7%, the NASDAQ fell 0.4%, and the Russell 2000 dropped 0.3%. Breadth was also weak as the NYSE Up Issues % came in at 33% and the Up Volume % was 29%. Total NYSE volume spiked to the highest level in July.

The selling has become extreme enough over the last few days that a large number of bullish studies triggered in the Quantifinder. I'll review the most substantial ones below.

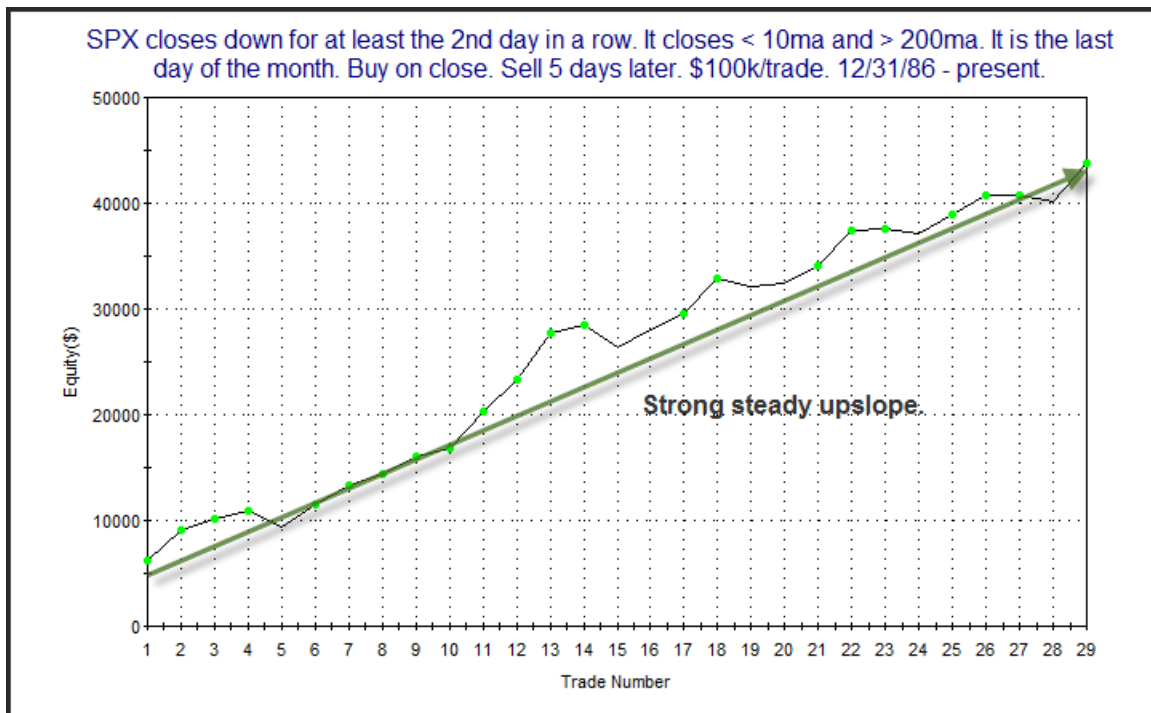
In the 12/1/10 subscriber letter I showed a few studies that examined early month performance when the previous month had closed poorly. One study I showed looked at times there were at least two down closes to finish the month and the final close was below the 10ma but above the 200ma. I have updated results for that study below.

SPX closes down for at least the 2nd day in a row. It closes < 10ma and > 200ma. It is the last day of the month. Buy on close. Sell X days later. \$100k/trade. 12/31/86 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	72,066.42	29	26	3	89.66	2,837.08	-565.90	5.01	43.45	2,485.05
11	64,901.32	29	26	3	89.66	2,594.13	-848.65	3.06	26.49	2,237.98
10	58,403.81	29	24	5	82.76	2,592.04	-761.05	3.41	16.35	2,013.92
9	57,682.57	29	23	6	79.31	2,800.58	-1,121.80	2.50	9.57	1,989.05
8	53,450.83	29	24	5	82.76	2,413.84	-896.26	2.69	12.93	1,843.13
7	50,926.75	29	24	5	82.76	2,356.03	-1,123.62	2.10	10.06	1,756.09
6	45,096.42	29	23	6	79.31	2,293.92	-1,277.30	1.80	6.88	1,555.05
5	43,733.28	29	24	5	82.76	2,052.23	-1,104.05	1.86	8.92	1,508.04
4	37,200.68	29	23	6	79.31	1,835.89	-837.48	2.19	8.40	1,282.78
3	30,061.21	29	21	8	72.41	1,863.91	-1,135.11	1.64	4.31	1,036.59
2	26,945.63	29	22	7	75.86	1,488.49	-828.72	1.80	5.64	929.16
1	17,220.37	29	22	7	75.86	949.18	-523.08	1.81	5.70	593.81

27 of 29 instances (93%) posted a close above the entry price at some point in the next week.

Results here strongly suggest that early month seasonality combined with an oversold market during a long-term uptrend typically makes for a very bullish combination. Below is an equity curve that shows how the edge has played out over the long-term.



The strong steady upslope serves as confirmation of the bullish edge. In the 12/1/10 subscriber letter I also looked at a similar setup that required three down days instead of just two. I have also updated that study below.

SPX closes down for at least the 3rd day in a row. It closes < 10ma and > 200ma. It is the last day of the month. Buy on close. Sell X days later. \$100k/trade. 12/31/86 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	39,202.48	13	10	3	76.92	4,090.02	-565.90	7.23	24.09	3,015.58
11	32,281.07	13	11	2	84.62	3,137.29	-1,114.57	2.81	15.48	2,483.16
10	32,205.01	13	11	2	84.62	3,039.11	-612.60	4.96	27.29	2,477.31
9	33,816.60	13	10	3	76.92	3,524.26	-475.34	7.41	24.71	2,601.28
8	31,361.82	13	11	2	84.62	2,980.10	-709.62	4.20	23.10	2,412.45
7	31,596.47	13	11	2	84.62	2,974.36	-560.73	5.30	29.17	2,430.50
6	26,634.70	13	11	2	84.62	2,684.09	-1,445.16	1.86	10.22	2,048.82
5	27,052.32	13	12	1	92.31	2,318.48	-769.50	3.01	36.16	2,080.95
4	21,955.51	13	12	1	92.31	1,848.93	-231.62	7.98	95.79	1,688.89
3	19,325.17	13	10	3	76.92	2,177.84	-817.74	2.66	8.88	1,486.55
2	12,764.40	13	10	3	76.92	1,412.36	-453.07	3.12	10.39	981.88
1	9,552.90	13	11	2	84.62	903.88	-194.87	4.64	25.51	734.84

All 13 instances posted a close above the entry price at some point in the next 4 days.

While the number of instances is reduced, three down days has produced more reliable and more bullish results. One filter that struck me as potentially unnecessary today is the 10ma filter. Three down days will most often put the SPX below its 10ma. Therefore I decided to run the above test without that filter and examine those results as well.

SPX closes down for at least the 3rd day in a row. It closes > 200ma. It is the last day of the month. Buy on close. Sell X days later. \$100k/trade. 12/31/86 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	42,106.11	15	12	3	80.00	3,650.32	-565.90	6.45	25.80	2,807.07
11	35,502.10	15	13	2	86.67	2,902.40	-1,114.57	2.60	16.93	2,366.81
10	34,997.89	15	13	2	86.67	2,786.39	-612.60	4.55	29.57	2,333.19
9	36,063.62	15	12	3	80.00	3,124.14	-475.34	6.57	26.29	2,404.24
8	33,122.59	15	13	2	86.67	2,657.06	-709.62	3.74	24.34	2,208.17
7	32,976.81	15	13	2	86.67	2,622.94	-560.73	4.68	30.41	2,198.45
6	28,187.86	15	13	2	86.67	2,390.63	-1,445.16	1.65	10.75	1,879.19
5	28,242.86	15	14	1	93.33	2,072.31	-769.50	2.69	37.70	1,882.86
4	23,414.92	15	14	1	93.33	1,689.04	-231.62	7.29	102.09	1,560.99
3	20,782.91	15	12	3	80.00	1,936.34	-817.74	2.37	9.47	1,385.53
2	14,192.82	15	12	3	80.00	1,296.00	-453.07	2.86	11.44	946.19
1	10,289.71	15	13	2	86.67	821.50	-194.87	4.22	27.40	685.98

All 15 instances posted a close above the entry price at some point in the next 4 days.

As you can see eliminating the filter only added two more instances. Both of them were followed by gains just as most of the others were. Lastly I decided to see how this setup might look if the market was in a long-term downtrend. Those results are below.

SPX closes down for at least the 3rd day in a row. It closes < 200ma. It is the last day of the month. Buy on close. Sell X days later. \$100k/trade. 12/31/86 - present.

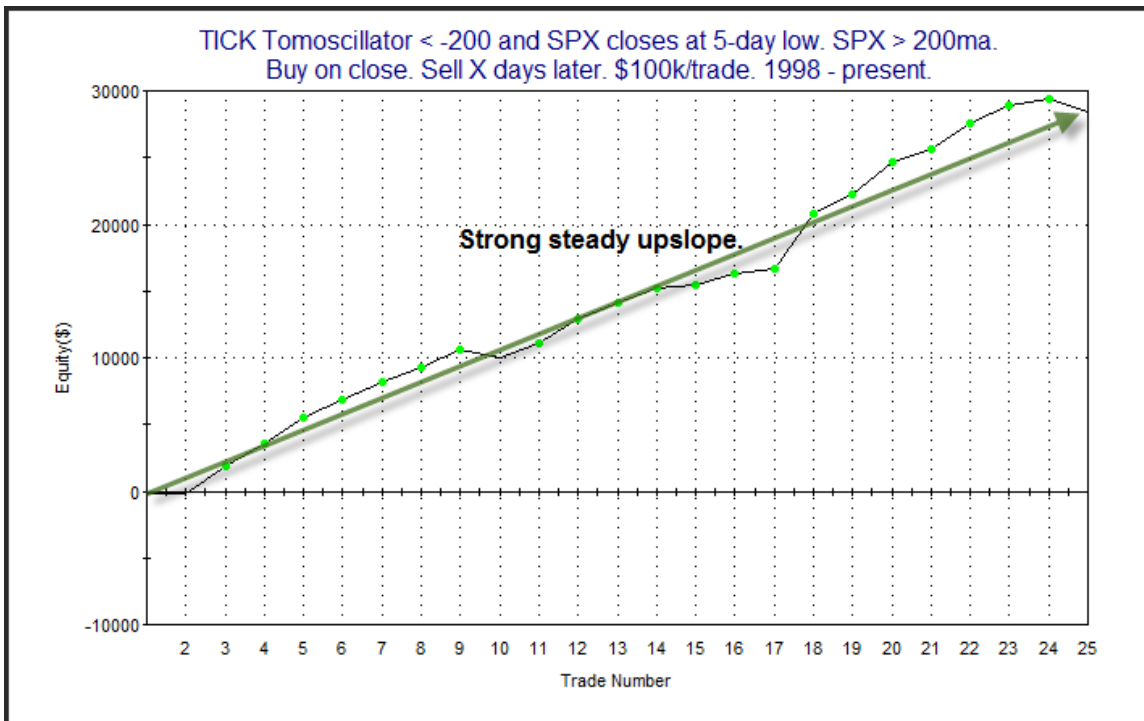
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	30,513.95	10	8	2	80.00	4,733.42	-3,676.70	1.29	5.15	3,051.39
11	26,218.71	10	7	3	70.00	5,131.05	-3,232.87	1.59	3.70	2,621.87
10	28,794.12	10	7	3	70.00	5,206.24	-2,549.86	2.04	4.76	2,879.41
9	22,267.74	10	7	3	70.00	4,161.06	-2,286.57	1.82	4.25	2,226.77
8	12,825.36	10	6	4	60.00	3,763.63	-2,439.11	1.54	2.31	1,282.54
7	13,710.22	10	6	4	60.00	3,117.99	-1,249.42	2.50	3.74	1,371.02
6	6,762.03	10	6	4	60.00	3,593.35	-3,699.52	0.97	1.46	676.20
5	6,765.87	10	5	5	50.00	4,034.58	-2,681.40	1.50	1.50	676.59
4	784.51	10	5	5	50.00	3,212.52	-3,055.62	1.05	1.05	78.45
3	1,829.95	10	5	5	50.00	2,345.62	-1,979.63	1.18	1.18	183.00
2	5,045.79	10	6	4	60.00	2,311.92	-2,206.44	1.05	1.57	504.58
1	761.71	10	7	3	70.00	1,413.41	-3,044.05	0.46	1.08	76.17

While not as compelling when below the 200ma, there still appears to be a seasonal tendency for short-term oversold markets to bounce at the beginning of the month.

Another Quantifinder study that appeared looked at the short-term low combined with the strongly oversold TICK Tomoscillator. It last triggered just a couple of days ago in the 7/28 letter, so it will likely look familiar to many of you.

TICK Tomoscillator < -200 and SPX closes at 5-day low. SPX > 200ma. Buy on close. Sell X days later. \$100k/trade. 1998 - present.										
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	31,997.91	20	16	4	80.00	2,301.32	-1,205.79	1.91	7.63	1,599.90
9	32,708.07	20	17	3	85.00	2,223.54	-1,697.36	1.31	7.42	1,635.40
8	34,557.36	20	17	3	85.00	2,188.86	-884.41	2.47	14.02	1,727.87
7	27,269.69	20	16	4	80.00	2,011.61	-1,229.03	1.64	6.55	1,363.48
6	23,335.30	21	17	4	80.95	1,903.75	-2,257.13	0.84	3.58	1,111.20
5	20,193.35	21	15	6	71.43	1,871.87	-1,314.12	1.42	3.56	961.59
4	19,420.63	21	15	6	71.43	1,732.32	-1,094.02	1.58	3.96	924.79
3	27,605.89	24	19	5	79.17	1,812.79	-1,367.43	1.33	5.04	1,150.25
2	28,430.36	25	22	3	88.00	1,372.89	-591.10	2.32	17.03	1,137.21
1	20,818.62	31	23	8	74.19	1,186.99	-810.26	1.46	4.21	671.57

While the last instance didn't play out as usual, there has been a strong propensity for the market to bounce over the next 2 days. Below is an equity curve that shows how the edge has played out over time.



Here again we see the equity curve confirm the edge suggested by the stats table.

The next group of studies considered the SPY gap down and partial (end of day) recovery. They last appeared in the 6/6/11 subscriber letter. Both have been updated. This first one requires SPY close at a 10-day low the day before.

Yesterday SPY closed at a 10-day low. Today it gapped down & closed above the open but below yesterday's close. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. '93 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	8,439.18	10	7	3	70.00	1,767.60	-1,311.34	1.35	3.15	843.92
4	5,365.28	10	7	3	70.00	1,118.08	-820.42	1.36	3.18	536.53
3	5,129.23	10	8	2	80.00	903.27	-1,048.48	0.86	3.45	512.92
2	1,458.44	10	7	3	70.00	1,113.85	-2,112.84	0.53	1.23	145.84
1	830.07	11	8	3	72.73	652.08	-1,462.18	0.45	1.19	75.46

6/3/11 was the only instance not to post a close above the entry price at some point in the next week.

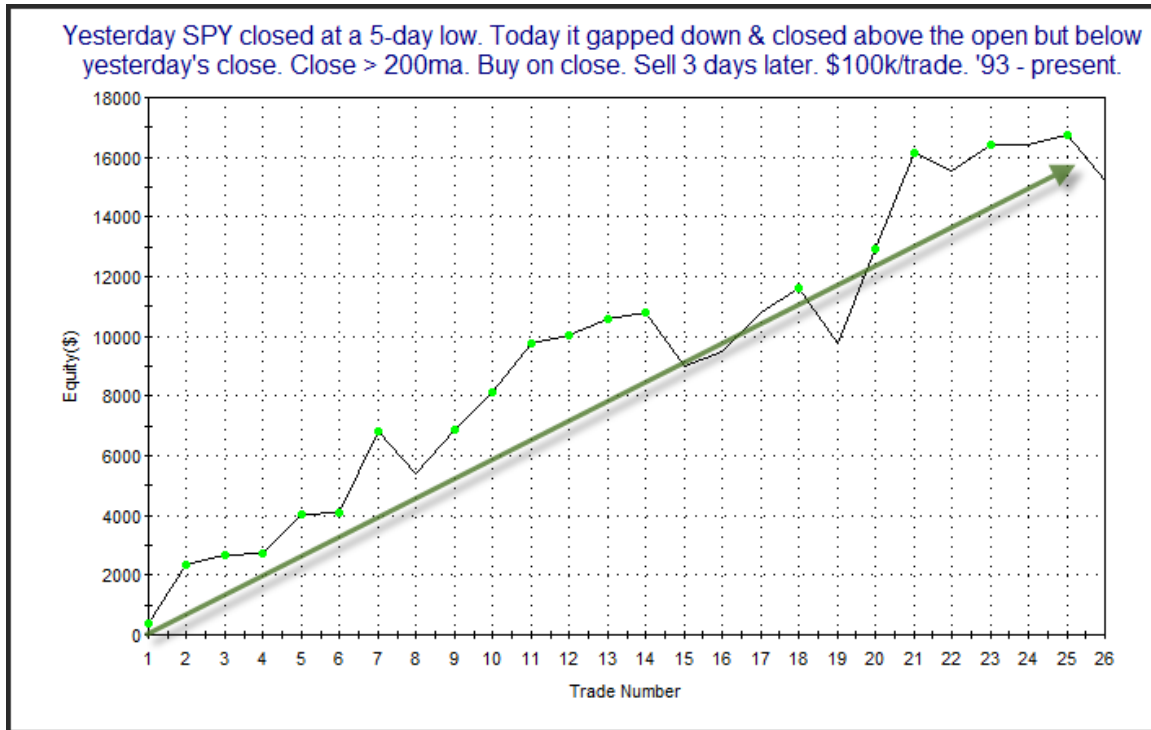
The last instance was a loser and the number of instances is low but the stats still appear to favor the bulls. This next one only requires a 5-day low.

Yesterday SPY closed at a 5-day low. Today it gapped down & closed above the open but below yesterday's close. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. '93 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	40,159.96	25	18	7	72.00	3,140.02	-2,337.20	1.34	3.45	1,606.40
9	39,436.15	26	21	5	80.77	2,630.56	-3,161.11	0.83	3.50	1,516.77
8	38,877.68	26	19	7	73.08	2,696.92	-1,766.26	1.53	4.14	1,495.30
7	28,592.94	26	18	8	69.23	2,290.73	-1,580.03	1.45	3.26	1,099.73
6	21,713.65	26	15	11	57.69	2,203.51	-1,030.82	2.14	2.91	835.14
5	17,726.80	26	18	8	69.23	1,640.52	-1,475.32	1.11	2.50	681.80
4	15,154.98	26	17	9	65.38	1,541.62	-1,228.06	1.26	2.37	582.88
3	15,213.95	26	21	5	80.77	1,065.60	-1,432.73	0.74	3.12	585.15
2	12,240.11	26	19	7	73.08	1,198.90	-1,505.58	0.80	2.16	470.77
1	5,001.42	28	19	9	67.86	855.84	-1,251.06	0.68	1.44	178.62

24 of 28 instances (86%) posted a close above the entry price at some point in the next week.

Here again we see the stats appear to suggest an upside edge. Below is an equity curve using a 3-day holding period.



This equity curve isn't as smooth as the others we looked at tonight but it still appears to suggest a fairly consistent upside edge.

Several people may have noticed that the VIX closed at its highest level since March. It also closed about 22.6% above its 10ma. A couple of weeks ago in the 7/15 letter I discussed VIX stretches of this magnitude. The first study I showed was actually last updated in the 3/17 subscriber letter. While it doesn't qualify today I did update it. It requires a stretch of at least 25% above the 10ma.

VIX crosses over 25% above its 10ma on a closing basis. SPX > 200ma.
Buy on close. Sell X days later. \$100k/trade. 1990 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	20,411.20	19	11	8	57.89	2,591.62	-1,012.08	2.56	3.52	1,074.27
4	27,444.26	19	14	5	73.68	2,271.79	-872.16	2.60	7.29	1,444.43
3	20,882.31	19	16	3	84.21	1,465.20	-853.62	1.72	9.15	1,099.07
2	21,504.71	19	14	5	73.68	1,697.79	-452.86	3.75	10.50	1,131.83
1	15,803.32	19	16	3	84.21	1,162.37	-931.53	1.25	6.65	831.75

18 of 19 instances posted a close above the entry price within the next 3 days. All 19 did within 6 days.

Results here were strongly suggestive of a short-term bounce. The next study looked at times like the present when the VIX spiked up to over 20% above the 10ma, but didn't reach the 25% threshold. It was last updated in the 7/15 letter and again tonight.

VIX crosses over 20% above its 10ma on a closing basis but does NOT close more than 25% above its 10ma. SPX > 200ma. Buy on close. Sell X days later. \$100k/trade. 1990 - present.

X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	13,916.30	19	13	6	68.42	1,645.00	-1,244.78	1.32	2.86	732.44
4	3,548.31	19	12	7	63.16	1,321.51	-1,758.54	0.75	1.29	186.75
3	-8,078.88	22	13	9	59.09	863.84	-2,145.42	0.40	0.58	-367.22
2	2,190.08	22	13	9	59.09	1,010.25	-1,215.90	0.83	1.20	99.55
1	2,441.46	22	13	9	59.09	761.79	-829.08	0.92	1.33	110.98

Any edge here is much more mild, and in my estimation not worth consideration. So while the VIX is close to a level that would suggest a strong short-term edge, it isn't quite there. To finish 25% above its 10ma on Monday would require a VIX close of 25.69 or higher.

In all, there is quite a bit tonight pointing to a short-term bullish edge.

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



With tonight's bullish studies the already strongly positive green Aggregator line rose even further. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the Differential Line is as far above 0 as it has been in a long time. A positive Differential reading means the SPX has underperformed expectations over the last few days. So net expectations are strongly positive and the SPX is extremely oversold versus recent expectations. Historically this combination has provided a bullish edge. It can be seen on the Aggregator chart whenever both lines are above 0. Due to this the Aggregator System remained long at the close.

With the current studies the green Aggregator line is again set to close above 0 on Monday. This is highly unlikely to change. Meanwhile, the Differential Pivot will be 1,315.76. This is about 1.8% above Friday's close. This means that it would take a rally of at least this much in order to flip the Differential Line back to negative. That's certainly possible but it may take a multi-day move to exhaust the oversold conditions.

I'm quite long at this point. Evidence is certainly compelling, but I'm not quite ready to put on the last piece of my index position. The government debt situation is creating an extra layer of risk, and while the selloff is triggering a number of bullish studies fear is not quite as pronounced as I would prefer. The CBI is still zero and the VIX isn't quite at the 25% stretch threshold that appears significant.

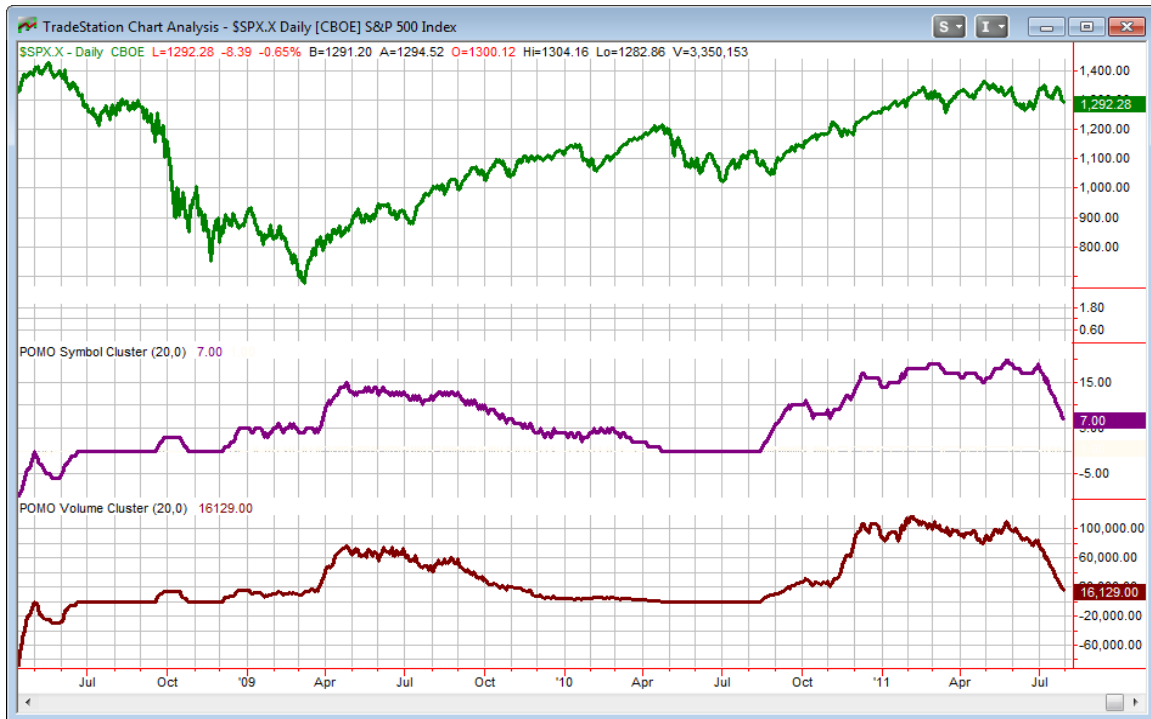
Intermediate-term Outlook (2 weeks – 2 months)– updated 8/1 – moderately bullish

The market closed down every day this past week. Bulls failed to continue the previous week's rally and break the early July highs. As I showed above, this week's selling has brought about a strong short-term bullish edge. For the intermediate-term, not much of significance seemed to occur.

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 3rd POMO presentation linked below. (Not available for trial users.)

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



It has now been a full month since the end of QE2. This means our POMO calculations no longer include QE2 pumping. The levels we are seeing above are probably close to what we can expect moving forward. While it is well below the level of stimulus the market had received over the previous 10 months or so, there still appears to be a decent amount of liquidity pumping. Whether it is enough to support the market's rally going forward is unclear, but it is well above the "0" levels that were followed by such strong selloffs over the last several years.

As of now there is only one day of buying scheduled for this week, and one day the following week. The current schedule only runs through August 9. The next schedule is set to be posted on August 10. Below is a link to the current schedule.

http://www.newyorkfed.org/markets/tot_operation_schedule.html

There remain a number of intermediate-term market studies suggesting positive implications. Some of them are set to expire in the next week or so though. Breadth, a high-probability Follow-Through Day signal, Nasdaq leadership, and price action and momentum are providing positive indications. The big concern remains POMO activity. I should also note the SPX is now only barely above its 200ma. Should this level fail I will examine possible implications. Right now the combination of evidence is enough to keep me slightly favoring the bull side.

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

None

Catapult for ETF's Trades

FAA – buy @ \$30.49 limit (filled @ \$30.28).

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.

***XIV – buy on VIX (4pm) close of 25.69 or higher.** This level would mark a 25% stretch as noted above. Though the futures roll is currently negative, the strong directional edge suggested by the Aggregator makes this an appealing entry for me.*

***PG – buy @ \$61.49 limit ON CLOSE.** This is based on system 80509. Normally I would just use a simple limit order, but with the big gap up in the market that is apparent as I am writing I'm less inclined to buy a dip intraday and will instead look to enter if we get a close down here or below.*

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	7/26/2011	\$133.33	\$129.33	-3.00%		Aggregator
SPY(1/4)	7/28/2011	\$130.60	\$129.33	-0.97%		bought on open
SPY(1/4)	7/28/2011	\$130.22	\$129.33	-0.68%		bought on close
FAA	7/29/2011	\$30.28	\$31.06	2.58%		sell @ \$31.20

The FAA trade idea from Thursday night's letter did fill. Unfortunately, when I posted it I did not realize how low the volume in that security has been. It did qualify to make the ETF list under the volume guidelines I used when I created the list, but it is now well below where I would normally suggest an idea. The low volume may increase slippage for those looking to enter or exit the security. Therefore, I have decided to use a limit sell order to exit FAA a little early. Normally, I would just sell at the open of the day following an exit trigger. In this case I will instead post a limit order here, figuring it is easier for folks to exit on the way up than potentially the way down when volume is low. Apologies for the low-volume trade idea. I will try to suggest more "tradable" securities as I normally do going forward.

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