

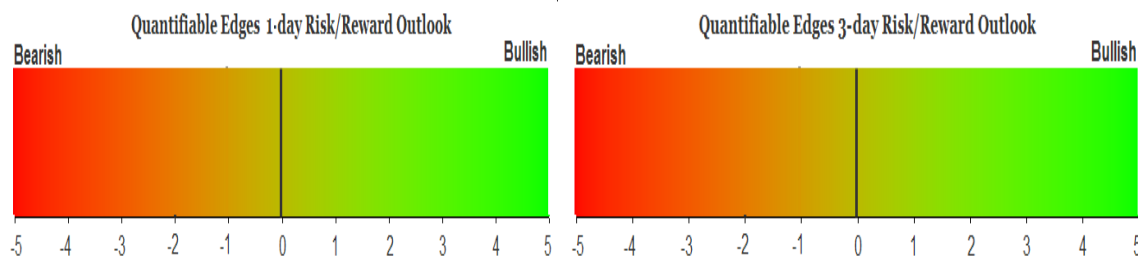
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 13, 2012

Volume 5 Issue 9

Market Overview



Signals Overview

Aggregator	Aggressive VIX	Conservative VIX	NDX Trend Timer
Flat	50% Long XIV	Flat	Flat

Tonight's Research Points

- A very low VIX:VXV ratio with the SPX at a 50-day high suggests increased short-term risk.

Short-term Outlook

The Bottom Line

The slow grind up at new highs continues. Complacency suggests some extra short-term risk, but expectations remain mildly bullish. With the market overbought the Aggregator is neutral. I'm still waiting for a better entry opportunity.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
January 13, 2012	VIX:VXV < 0.85.	1 day	Bearish	
January 12, 2012	Breakout then inside day	1-5 days	Bullish	1.50%
January 12, 2012	SPX 50-high. VIX up midweek.	1-2 days	Bearish	-0.80%
January 11, 2012	Breakaway gap	1-5 days	Bullish	1.70%
Active - Long Term				
January 4, 2012	2 of 3 days Up Issue %>75. 10-high.	1-18 days	Bullish	
December 28, 2011	5 Days Up > 200 no 50-high	1-15 days	Bullish	
December 5, 2011	POMO activity flat to negative	int term	Bearish	
October 30, 2011	SPX & bond yields hit 50-day highs	1-50 days	Bearish	
October 19, 2011	FTD on strong breadth/20day high	int term	Bullish	
Dropped Tonight				
January 10, 2012	Overbought w/out POMO support	1-4 days	Bearish	-2.70%

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

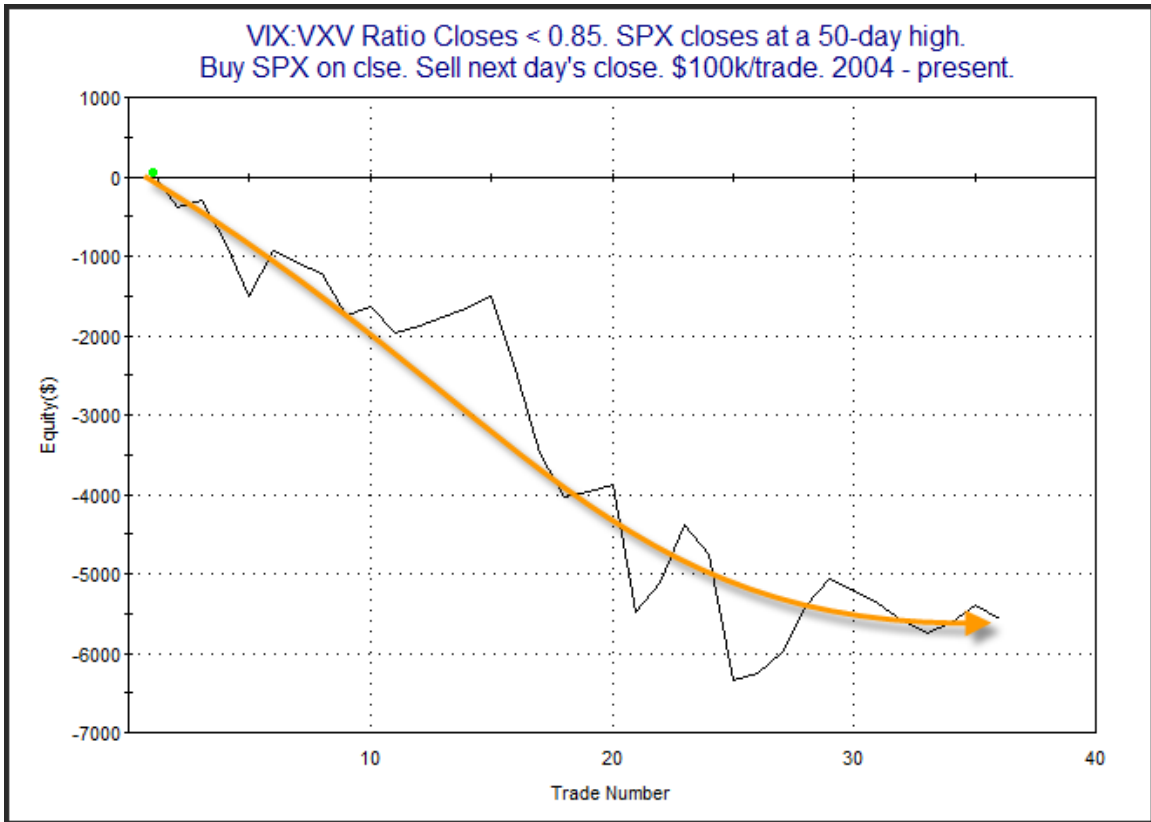
The Evidence

Thursday was another fairly quiet day that saw the major indices creep higher. The SPX gained 0.2%, the Nasdaq was up 0.5% and the Russell 2000 rose 0.4%. Breadth was moderately positive as both the NYSE Up Issues % and Up Volume % came in at 60%. Total NYSE volume rose just slightly from Wednesday's level.

The slow grind up the last several days have done little to inspire new studies. So there isn't much to discuss tonight. One observation that was noted by the Quantifinder was that the VIX:VXV ratio has now declined to below 0.85 while the SPX is at a new high. This was a setup that was shown last in the 4/29/11 subscriber letter. It showed a mild downside inclination over the next few days, though the bulk of the edge played out on day 1. Below I have updated the results for 1-day holds.

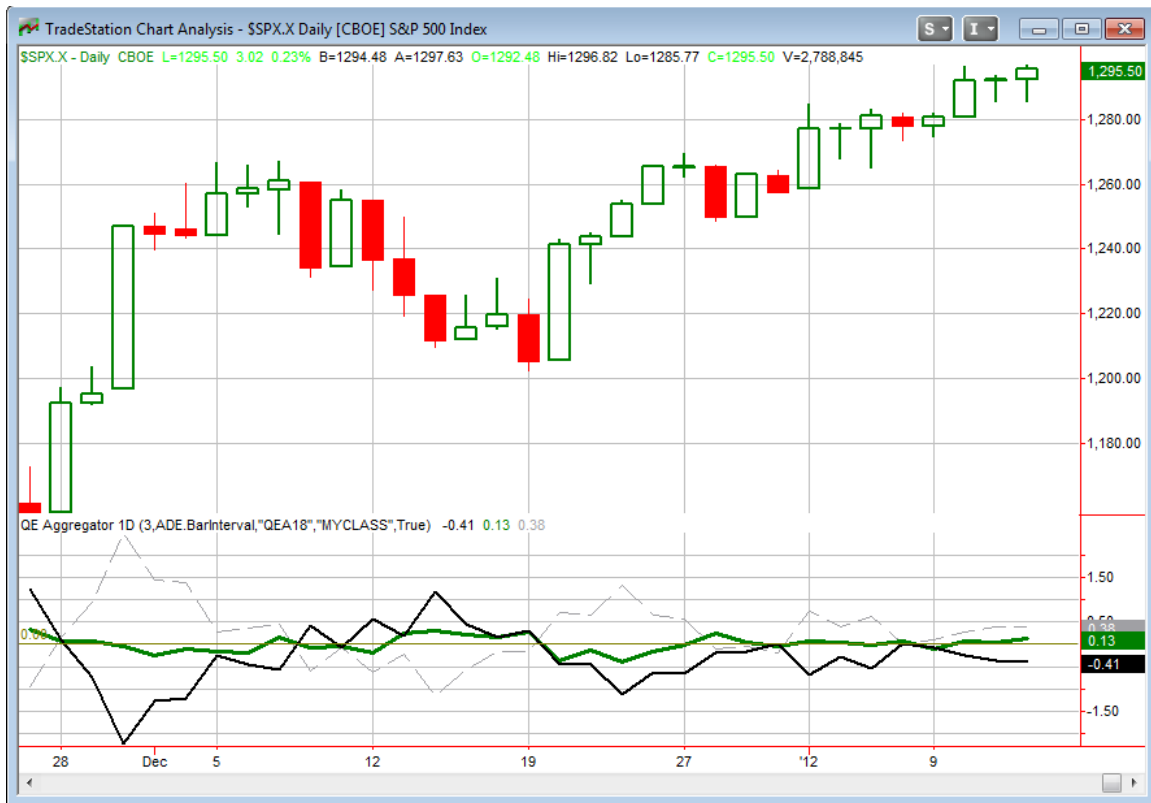
VIX:VXV Ratio Closes < 0.85. SPX closes at a 50-day high. Buy SPX on close. Sell next day's close. \$100k/trade. 2004 - present			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	(\$5,561.39)	Profit Factor	0.43
Gross Profit	\$4,146.49	Gross Loss	(\$9,707.88)
Total Number of Trades	36	Percent Profitable	50.00%
Winning Trades	18	Losing Trades	18
Even Trades	0		
Avg. Trade Net Profit	(\$154.48)	Ratio Avg. Win:Avg. Loss	0.43
Avg. Winning Trade	\$230.36	Avg. Losing Trade	(\$539.33)
Largest Winning Trade	\$708.05	Largest Losing Trade	(\$1,602.28)

The odds are 50/50 but the losers have been more than twice the size of the winners. This suggests the complacency we are seeing at these high levels is more likely to lead to a big down day than be followed by a big up day. To see how the edge has played out over time I have posted the profit curve below.



The equity curve seems to have flattened out a bit lately. While I did include it on the Active List, I'm certainly putting this one on watch.

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



Despite the mild bearish study tonight the green Aggregator line is still positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line is still a little below 0. A negative Differential reading means the SPX has outperformed expectations over the last few days. So net expectations are bullish but the SPX is already overbought versus recent expectations. 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 active studies, expectations are scheduled to remain positive on Friday. Of course this could change if more bearish evidence emerges. The Differential Pivot will be 1,292.30 on Friday. This is only 0.25% below Thursday's close. So with just modest gains the last 2 days it won't take much of a decline on Friday for the SPX to be considered underperforming versus expectations.

My outlook remains neutral. While expectations are positive, the SPX remains overbought and signs of complacency suggest increased risk. At this point I'm waiting for a pullback to enter long or compelling bearish evidence to enter short.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/9 – neutral

The intermediate-term outlook was last updated in the 1/9/12 letter. It may be accessed using the link below:

[2012-01-09 QE Subscriber Letter.pdf](#)

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

MO – bought 1/3 @ \$28.40 (filled)

Catapult for ETF's Trades

None.

Broad Market Large Cap CBI – 1(MO)

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
MO(1/3)	1/5/2012	\$28.40	\$28.84	1.55%	\$28.09	Catapult
VZ(1/3)	1/9/2012	\$38.33	\$38.99	1.72%		Sold on open

MO needs to trade up to about \$28.95 intraday or close at an estimated \$28.91 or higher in order to hit its exit target. If either of these things happens then it will be exited on Monday's open.

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