

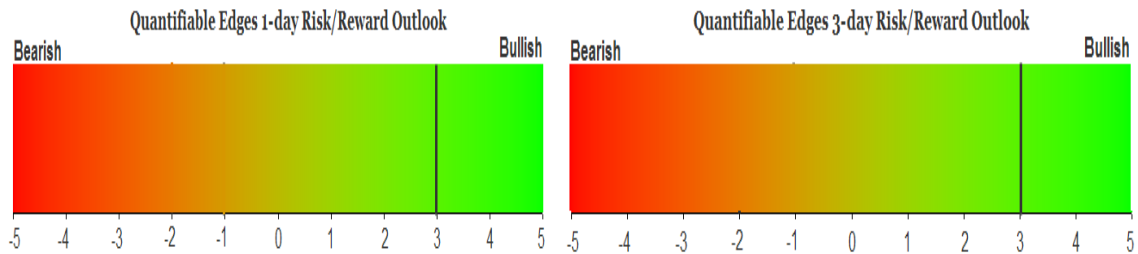
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 1, 2012

Volume 5 Issue 21

Market Overview



Signals Overview

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

Tonight's Research Points

- When Turnaround Tuesday fails, it is often temporary.
- Selloffs at month end typically get bought early in the new month.
- Tuesday's strong breadth was a good sign for the short-term.
- Tuesday's Golden Cross was a good sign for the long-term.
- The low 3/10 Offset HV suggests a big move could be on tap.

Short-term Outlook

The Bottom Line

Though mild, the pullback is now at a point where an upside edge seems apparent. I am partially long and will consider adding to my position if the pullback deepens.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
February 1, 2012	Selloff at month end	1-5 days	Bullish	2.35%
February 1, 2012	SPX down. Up Issues % > 55%.	1-2 days	Bullish	
January 31, 2012	SPX 1st close < 10ma in under 25 days	1-4 days	Bullish	1.80%
January 31, 2012	SPY 3-day pullback. Today is Monday.	1-4 days	Bullish	2.30%
January 26, 2012	SPX 100-day high on Fed Day	1-6 days	Bullish	1.60%
Active - Long Term				
January 31, 2012	SPX 1st close < 10ma in under 25 days	1-20 days	Bullish	4.70%
January 17, 2012	Nasdaq leading SPX	int term	Bullish	
December 5, 2011	POMO activity flat to negative	int term	Bearish	
October 19, 2011	FTD on strong breadth/20day high	int term	Bullish	
Dropped Tonight				
January 23, 2012	SPX up 1%-2% op-ex week	1-4 days	Bearish	

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

The Evidence

A solid gap higher was quickly met with selling that turned indices negative. After some back and forth the indices finished relatively unchanged. The SPX closed down 0.05%, while the Nasdaq and the Russell 2000 both finished up less than 0.1%. Breadth was modestly positive as the NYSE Up Issues % came in at 57.5% and the Up Volume % was 50.3%. Total NYSE volume rose to the highest level of 2012.

Last night I showed a Turnaround Tuesday study that indicated when the market is down 3 days in a row going into a Tuesday that it has a strong tendency to bounce. Of course there have been instances over the years where it hasn't. When it doesn't bounce on Tuesday what does that mean for Wednesday and beyond? The test below is updated from the 4/13/11 Letter and it answers that question.

Today is Tuesday. SPX closes lower for exactly the 4th day in a row.
Buy on close. Sell X days later. \$100k/trade. 1980 - 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	58,632.19	35	29	6	82.86	2,437.09	-2,007.25	1.21	5.87	1,675.21
9	61,470.49	35	31	4	88.57	2,228.28	-1,901.52	1.17	9.08	1,756.30
8	68,526.80	35	30	5	85.71	2,548.90	-1,588.06	1.61	9.63	1,957.91
7	59,310.82	35	29	6	82.86	2,402.07	-1,724.85	1.39	6.73	1,694.59
6	59,331.63	35	28	7	80.00	2,464.57	-1,382.33	1.78	7.13	1,695.19
5	50,873.05	35	27	8	77.14	2,320.17	-1,471.44	1.58	5.32	1,453.52
4	48,217.75	35	26	9	74.29	2,338.59	-1,398.40	1.67	4.83	1,377.65
3	31,830.90	35	27	8	77.14	1,623.42	-1,500.17	1.08	3.65	909.45
2	19,438.95	35	21	14	60.00	1,355.24	-644.36	2.10	3.15	555.40
1	14,712.50	35	24	11	68.57	898.20	-622.21	1.44	3.15	420.36

30 of 35 instances (86%) closed above the entry price at some point in the next week.

Results here have been very strong over a long period. It seems the “Turnaround Tuesday Failure” is likely a temporary setback.

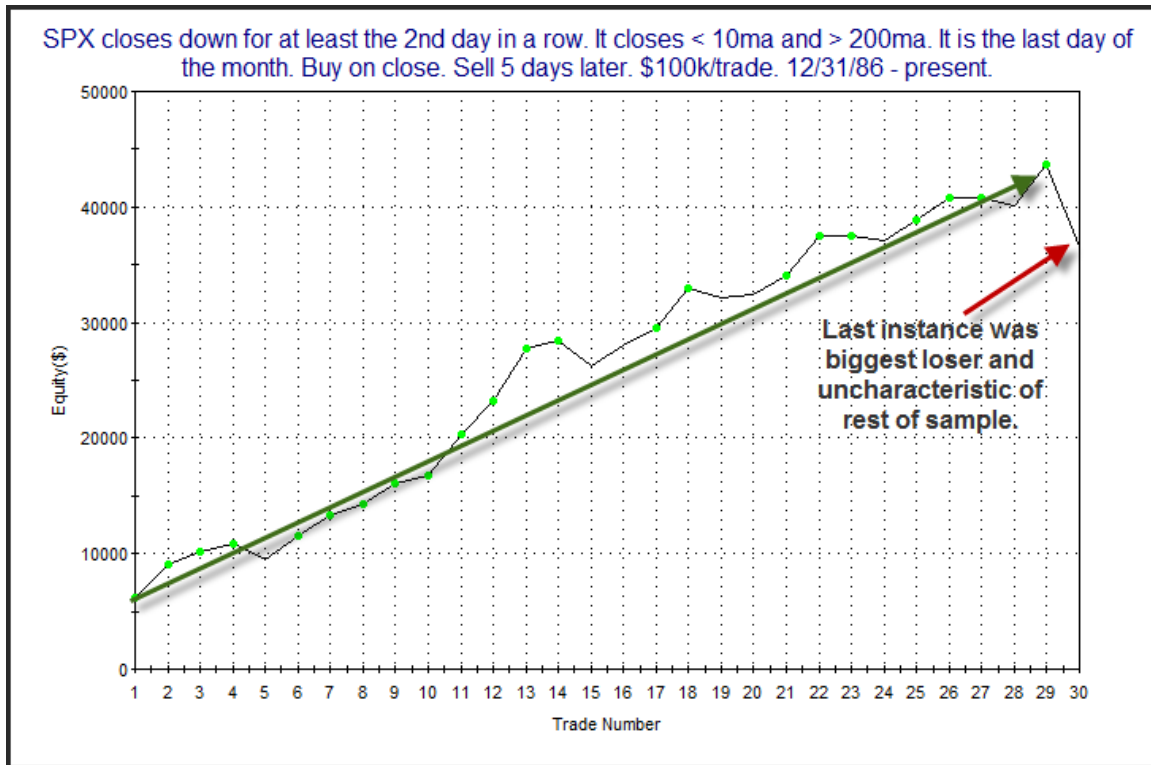
Perhaps more significant than the day of the week is the fact that Wednesday is the 1st day of the month. I have documented many times some strong tendencies for the market to perform well on the 1st day of the month. The study below looks at what has happened when the market was short-term oversold during a long-term uptrend at the turn of the month. It was last seen in the 8/1/11 letter.

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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	49,666.62	30	24	6	80.00	2,592.04	9,607.84	-2,090.41	-8,737.19	1.24	4.96	1,655.55
9	48,470.29	30	23	7	76.67	2,800.58	8,433.64	-2,277.58	-9,212.28	1.23	4.04	1,615.68
8	40,243.79	30	24	6	80.00	2,413.84	7,325.36	-2,948.06	-13,207.04	0.82	3.28	1,341.46
7	41,706.00	30	24	6	80.00	2,356.03	7,473.68	-2,473.14	-9,220.75	0.95	3.81	1,390.20
6	31,789.28	30	23	7	76.67	2,293.92	6,822.72	-2,995.85	-13,307.14	0.77	2.52	1,059.64
5	36,579.98	30	24	6	80.00	2,052.23	6,229.44	-2,112.26	-7,153.30	0.97	3.89	1,219.33
4	30,100.51	30	23	7	76.67	1,835.89	5,426.04	-1,732.15	-7,100.17	1.06	3.48	1,003.35
3	27,601.83	30	21	9	70.00	1,863.91	4,371.32	-1,282.25	-2,459.38	1.45	3.39	920.06
2	24,001.92	30	22	8	73.33	1,488.49	4,132.36	-1,093.10	-2,995.78	1.36	3.74	800.06
1	16,809.19	30	22	8	73.33	949.18	3,119.10	-509.10	-2,559.62	1.86	5.13	560.31

27 of 30 instances (90%) posted a close above the entry price at some point in the next week.

Results here appear strongly bullish for the early part of the upcoming month. Below is an updated equity curve using a 5-day exit strategy.



The August 2011 instance saw a sharp decline. Traders may recall that this was the first time in history in which US debt was downgraded, and the market reacted with a mini-crash. At this point it looks like an anomaly rather than representative of typical behavior.

In that 8/1/11 letter I also looked at 3 lower closes going in to the end of the month. That study also triggered again and has been updated 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: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	26,260.70	16	13	3	81.25	2,786.39	9,607.84	-3,320.80	-8,737.19	0.84	3.64	1,641.29
9	26,851.34	16	12	4	75.00	3,124.14	8,433.64	-2,659.57	-9,212.28	1.17	3.52	1,678.21
8	19,915.55	16	13	3	81.25	2,657.06	7,325.36	-4,875.43	-13,207.04	0.54	2.36	1,244.72
7	23,756.06	16	13	3	81.25	2,622.94	7,473.68	-3,447.40	-9,220.75	0.76	3.30	1,484.75
6	14,880.72	16	13	3	81.25	2,390.63	6,822.72	-5,399.15	-13,307.14	0.44	1.92	930.05
5	21,089.56	16	14	2	87.50	2,072.31	6,229.44	-3,961.40	-7,153.30	0.52	3.66	1,318.10
4	16,314.75	16	14	2	87.50	1,689.04	5,426.04	-3,665.90	-7,100.17	0.46	3.23	1,019.67
3	18,323.53	16	12	4	75.00	1,936.34	4,371.32	-1,228.15	-2,459.38	1.58	4.73	1,145.22
2	11,249.11	16	12	4	75.00	1,296.00	4,132.36	-1,075.73	-2,943.71	1.20	3.61	703.07
1	9,878.53	16	13	3	81.25	821.50	2,143.68	-266.97	-411.18	3.08	13.33	617.41

The only instance NOT to close above the entry price at some point in the next 4 days was the most recent one in the beginning of August 2011.

Results here also remain strongly bullish despite the drubbing the market took the last time this triggered.

This next study considers the solid Up Issues % despite the decline in the SPX. I last showed it just 2 days ago in the 1/30/12 letter. Below is an excerpt. I have updated the tables and chart.

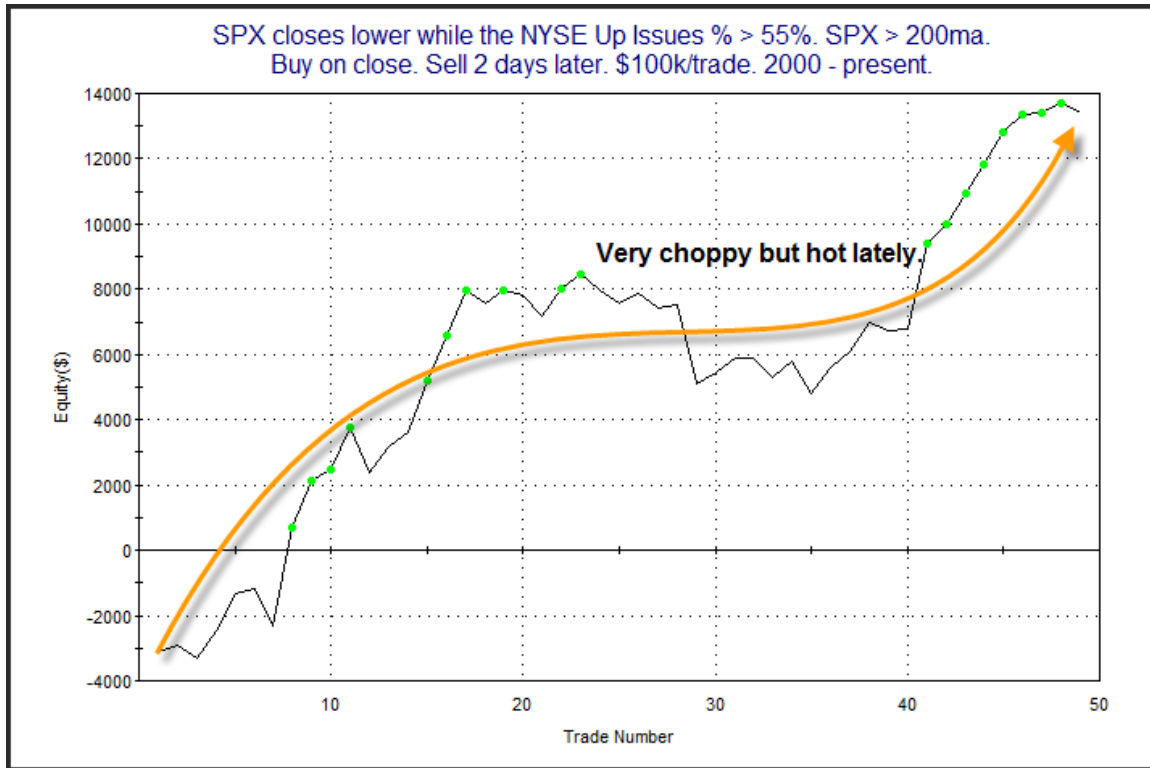
One study identified by the Quantifinder suggests a bit of an upside edge. It considered the strong breadth on a day the SPX declined...Results are updated.

**SPX closes lower while the NYSE Up Issues % > 55%. SPX > 200ma.
Buy 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
5	17,100.81	45	29	16	64.44	1,346.84	3,616.92	-1,372.34	-4,012.80	0.98	1.78	380.02
4	16,109.12	46	28	18	60.87	1,325.91	3,429.00	-1,167.57	-2,921.28	1.14	1.77	350.20
3	15,364.12	48	33	15	68.75	928.51	2,923.44	-1,018.46	-2,852.01	0.91	2.01	320.09
2	13,419.79	49	34	15	69.39	782.71	3,025.12	-879.49	-3,119.03	0.89	2.02	273.87
1	9,613.38	51	30	21	58.82	656.42	2,310.88	-479.97	-1,348.29	1.37	1.95	188.50

88% of instances posted a close 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.

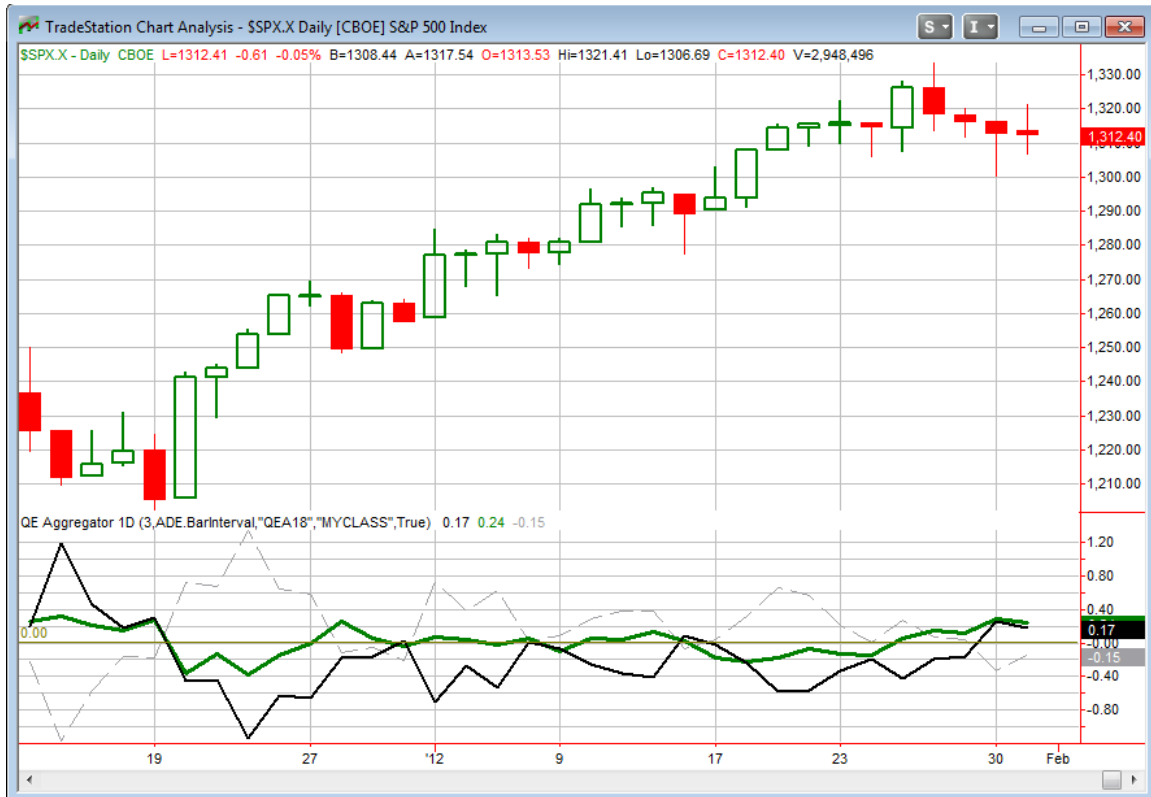


While the curve certainly appears choppy, the edge has been quite strong lately. The 3-5 day charts don't see quite as pronounced of a dip in the middle, which also alleviates some concern. I believe this study is worth taking into consideration and I've included it among the active studies.

Also notable about current conditions is that the 3/10 Offset Historical Volatility Indicator came in at an extremely low 0.16 on Monday. I first introduced this indicator in July of 2009. It essentially takes a short 3-day measure of Historical Volatility and compares that to the 10-day measure of 3-days ago. Low readings indicate there has been a contraction in volatility. High numbers indicate there has been an expansion. Anything at or below 0.25 is regarded as extremely low. Often after sharp contractions like this we see a volatility expansion take place. These big moves may happen in either direction but more often occur in the direction of the Aggregator.

It is also worth pointing out that the SPX did complete its Golden Cross as I mentioned was likely in Sunday night's letter. This suggests an intermediate-term bullish environment. More research on the Golden Cross may be found in the 1/30/12 intermediate-term section.

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



Additional bullish evidence kept the green Aggregator line strongly positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line also held firm. A positive Differential reading means the SPX has underperformed expectations over the last few days. So net expectations are bullish and the SPX is oversold versus recent expectations. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. This caused the Aggregator System to remain long at the close. This was indicated as likely on the systems page shortly before the bell.

Based on the current active studies, expectations are scheduled to remain positive on Wednesday. This could change if strong bearish evidence emerges. Meanwhile, the

Differential Pivot will be 1,320.47 on Wednesday. This means the SPX will need to rise about 0.6% in order to turn the Differential Line negative.

So I have a similar conundrum to the one I had last night. The bullish evidence is all very compelling, but the market sits in the same place. Despite closing lower 4 days in a row the SPX actually sits slightly above the midpoint of its 10-day range. Mid-range is not my favorite place to initiate entries, because from that point risk/reward are often roughly equal. The studies suggest good odds for a move up, so I still believe there is an upside edge. But risk is higher than I prefer. And adding to that risk is the very low 3/10 Offset HV. Low readings suggest a big move may be coming, and if it is down we have no strong technical support nearby. So with good odds but higher than normal risks I will remain cautiously bullish. If the market does decide to crater in the next day and it is accompanied by a spike in the VIX, then I may look to take advantage of opportunities in both SPY and XIV. Of course this assumes that expectations from the studies remain bullish.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/30 – bullish

The intermediate-term outlook was last updated in the 1/30/12 letter. A link is below:

[2012-01-30 QE Subscriber Letter.pdf](#)

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 @ \$130.25 LIMIT ON CLOSE. I am keeping last night's order active. Based on the short-term outlook above I will look to add another lot to my position if it closes down near the lower end of Monday's range.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	1/30/2012	\$131.37	\$131.37	0.00%		Aggregator

I will sell ½ of my SPY position on an SPX close \geq 1,320.47.

This report has been prepared by Hanna Capital Management, LLC and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy securities. While information contained herein is believed to be accurate at the time of publication, we make no representation as to the accuracy or completeness of any data, studies, or opinions expressed and it should not be relied upon as such. Robert Hanna, Hanna Capital Management, LLC or clients of Hanna Capital Management, LLC may have positions or other interests in securities (including derivatives) directly or indirectly which are the subject of this report. This report is provided solely for the information of Hanna Capital Management, LLC clients and prospects who are expected to make their own investment decisions without reliance upon this report. Neither Hanna Capital Management, LLC nor any officer or employee of Hanna Capital Management, LLC accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. This report may not be reproduced, distributed or published by any recipient for any purpose without the prior express consent of Hanna Capital Management, LLC.

Copyright © 2012 Hanna Capital Management, LLC.