

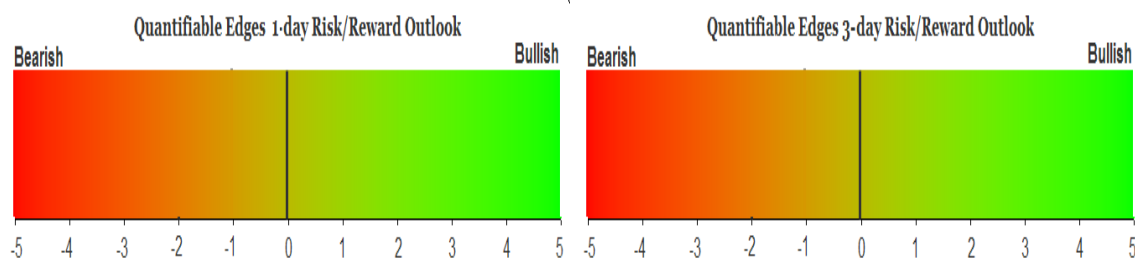
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 1, 2012

Volume 5 Issue 41

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 trading day of the month is typically bullish. This edge has been more prominent above the 200ma, but less prominent in March.
- Wednesday's outside reversal day is not a pattern that typically marks an intermediate-term top.
- With the new POMO schedule out I provide projected values for the QE Buying Power Index for March.

Short-term Outlook

The Bottom Line

The current market setup is not one that I find compelling. Therefore, I am sidelined and awaiting a more favorable entry opportunity.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
March 1, 2012	1st Day of Month	1 day	Bullish	
February 29, 2012	Russell down 3 days. SPX 3-day high.	1-6 days	Bullish	3.95%
February 28, 2012	SPX & VIX up 2 in a row	1-3 days	Bearish	-1.35%
Active - Long Term				
March 1, 2012	10-high then outside day down > 200	1-12 days	Bullish	2.70%
February 29, 2012	Russell dn 3 days. SPX 3-day high.	1-10 days	Bullish	5.10%
February 1, 2012	Golden Cross	int term	Bullish	
January 17, 2012	Nasdaq leading SPX	int term	Bullish	
December 5, 2011	POMO activity flat to negative	int term	Bearish	

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

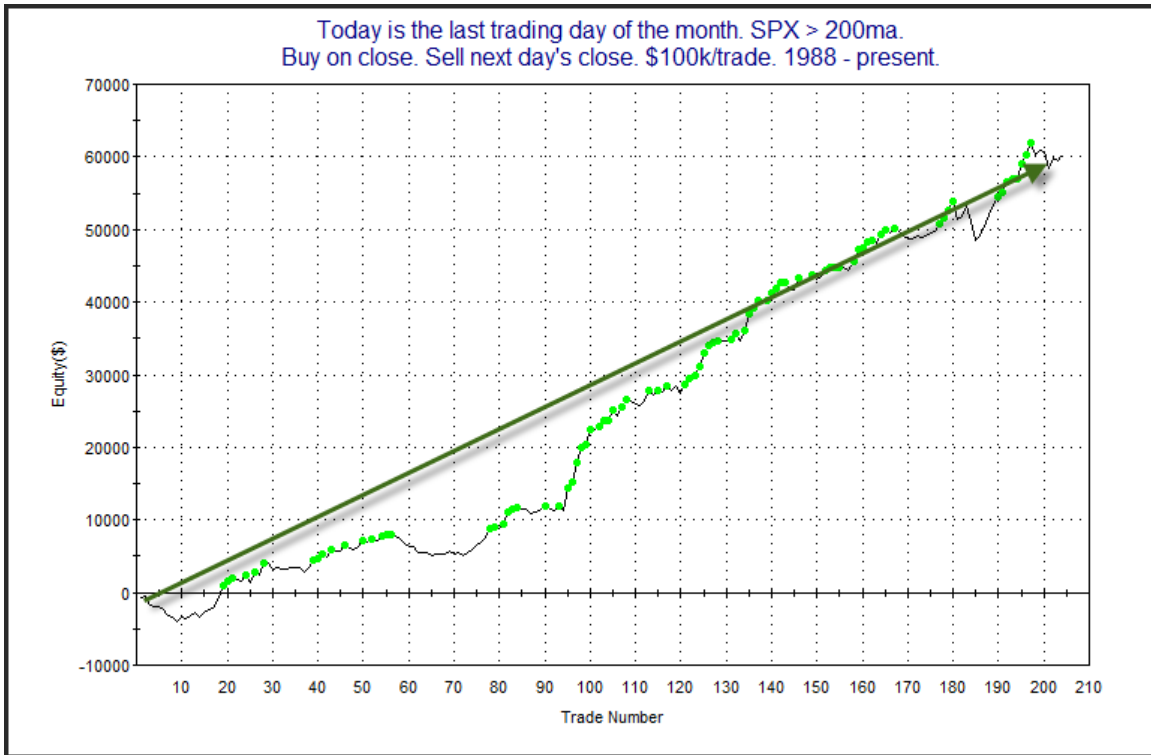
The Evidence

The 3/10 Offset HV last night suggested an increase in volatility was likely and we got it on Wednesday, with the major indices all closing down. The SPX lost 0.5%, the Nasdaq fell 0.7%, and the Russell 2000 dropped 1.6%. Breadth was solidly negative as the NYSE Up Issues % came in at 35% and the Up Volume % was 29%. Total NYSE volume spiked to the highest level so far in 2012. I looked at the big volume with the SPX coming off a long-term high and it did not seem to provide a directional clue.

There are a few new bits of evidence to consider tonight. The first, and perhaps most obvious potential edge to explore is the bullish seasonality that often occurs on the first day of a new month. In the 10/3/11 subscriber letter I showed that this bullish tendency primarily occurred during uptrends. I have updated the statistics for uptrends below.

Today is the last trading day of the month. SPX > 200ma. Buy on close. Sell next day's close. \$100k/trade. 1988 - present.			
TradeStation Performance Summary			Collapse
All Trades			
Total Net Profit	\$60,302.06	Profit Factor	2.53
Gross Profit	\$99,619.39	Gross Loss	(\$39,317.33)
Total Number of Trades	204	Percent Profitable	62.75%
Winning Trades	128	Losing Trades	76
Even Trades	0		
Avg. Trade Net Profit	\$295.60	Ratio Avg. Win:Avg. Loss	1.50
Avg. Winning Trade	\$778.28	Avg. Losing Trade	(\$517.33)
Largest Winning Trade	\$3,119.10	Largest Losing Trade	(\$2,617.60)

As you can see, the raw numbers appear quite encouraging. Below is a profit curve that shows how the edge has played out over time.



The strong steady upslope acts as confirmation of the upside edge. I've also shown in the past that the edge appears to be more prominent in some calendar months versus others. March historically has not shown a consistent upside edge. This can be seen in the study below.

Today is the last trading day of February.
Buy on close. Sell next day's close. \$100k/trade. 1988 - present.

TradeStation Performance Summary Collapse ^			
All Trades			
Total Net Profit	\$316.85	Profit Factor	1.03
Gross Profit	\$10,011.07	Gross Loss	(\$9,694.22)
Total Number of Trades	24	Percent Profitable	50.00%
Winning Trades	12	Losing Trades	12
Even Trades	0		
Avg. Trade Net Profit	\$13.20	Ratio Avg. Win:Avg. Loss	1.03
Avg. Winning Trade	\$834.26	Avg. Losing Trade	(\$807.85)
Largest Winning Trade	\$2,254.50	Largest Losing Trade	(\$4,660.72)

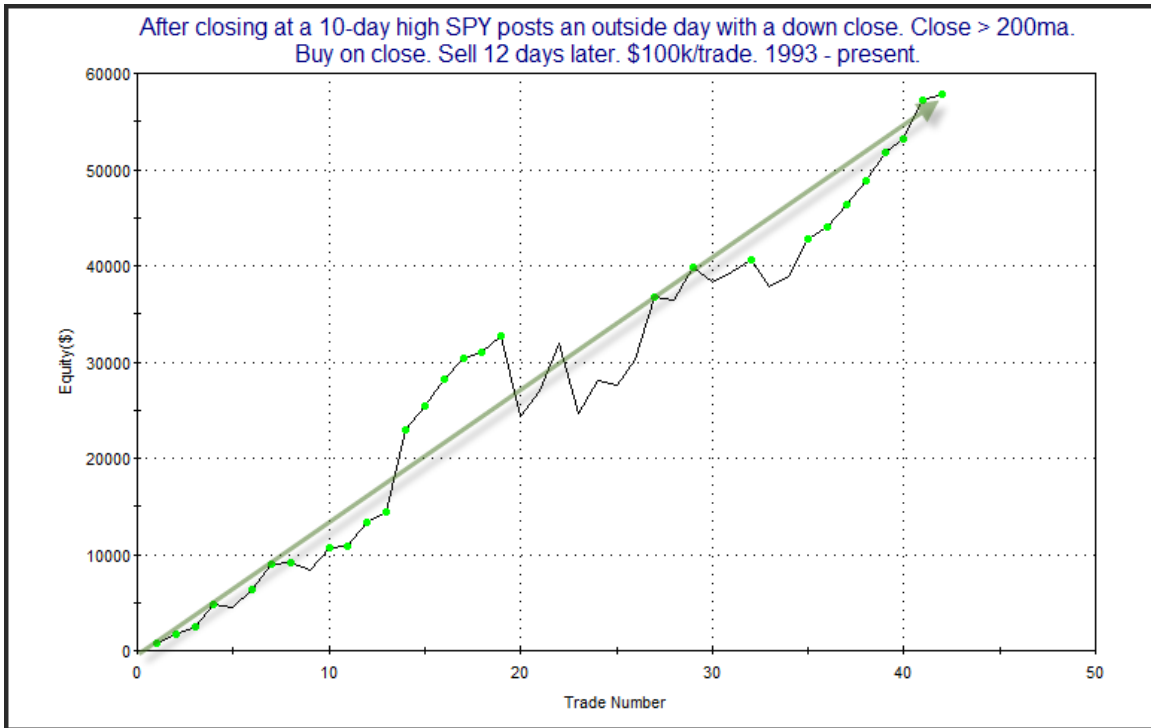
So, first of the month is generally a good thing, and it has been even better when the SPX is in an uptrend, but those tendencies have generally not worked out as well in March.

Personally, I believe seasonality is helping to provide an upside edge tomorrow, but that edge is reduced versus other, more consistent months.

In the 5/3/11 subscriber letter I examined this next study. It considered results following instances where SPY posted an outside day with a down close immediately following a short-term closing high during an uptrend. Results were interesting in that the outside day often lead to a small amount of additional selling over the next few days, but rarely did this “reversal signal” ever actually mark an intermediate-term high. I have updated the results table below.

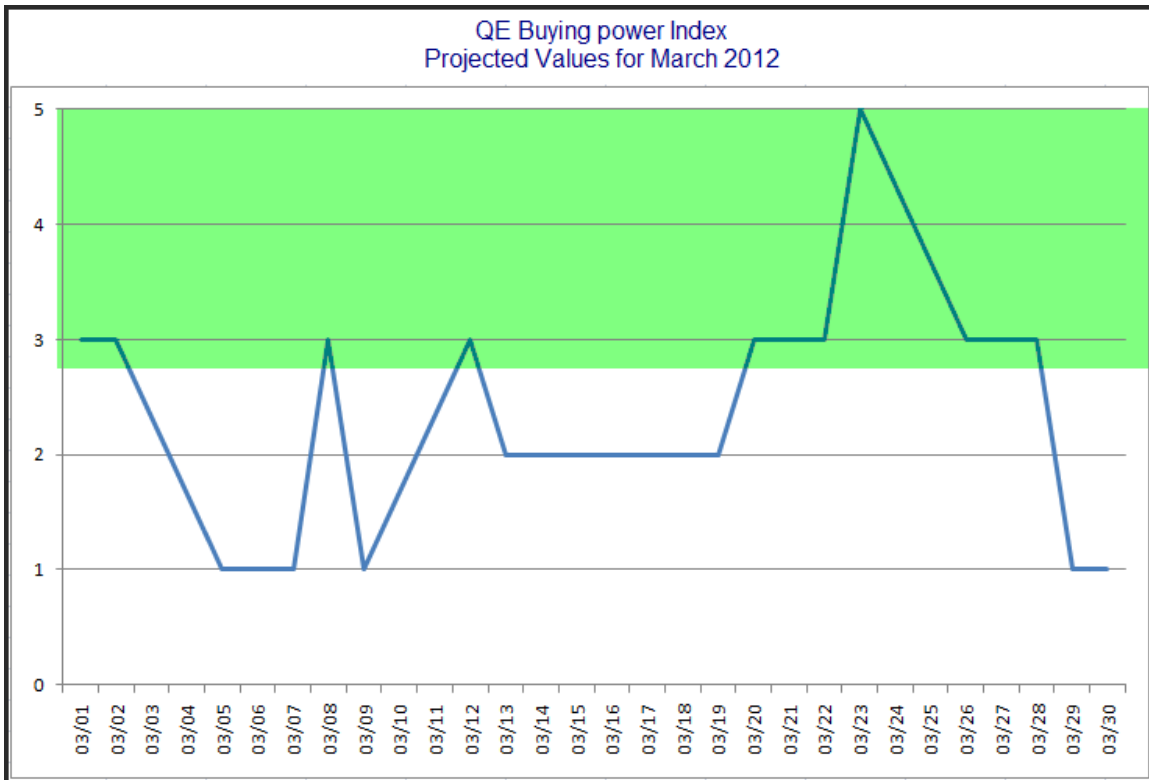
After closing at a 10-day high SPY posts an outside day with a down close. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1993 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	57,858.78	42	34	8	80.95	2,348.03	8,494.78	-2,746.79	-8,389.36	0.85	3.63	1,377.59
11	50,925.49	42	34	8	80.95	2,085.28	6,726.11	-2,496.74	-9,630.04	0.84	3.55	1,212.51
10	42,150.04	43	33	9	76.74	1,824.79	5,990.24	-2,007.56	-5,992.40	0.91	3.33	980.23
9	35,269.79	44	31	13	70.45	1,853.94	5,267.28	-1,707.88	-5,764.17	1.09	2.59	801.59
8	41,679.18	45	30	15	66.67	2,101.66	7,603.99	-1,424.71	-4,587.23	1.48	2.95	926.20
7	34,569.60	46	29	17	63.04	2,027.83	7,694.36	-1,425.74	-4,962.72	1.42	2.43	751.51
6	33,588.41	47	31	16	65.96	1,818.80	5,189.82	-1,424.65	-4,591.36	1.28	2.47	714.65
5	26,054.93	51	33	18	64.71	1,441.81	4,428.81	-1,195.82	-4,346.17	1.21	2.21	510.88
4	6,635.68	51	27	24	52.94	1,412.52	3,915.78	-1,312.60	-4,228.43	1.08	1.21	130.11
3	-7,297.17	51	25	26	49.02	1,133.44	2,930.57	-1,370.51	-5,283.03	0.83	0.80	-143.08
2	-9,827.12	52	22	30	42.31	919.56	2,361.64	-1,001.91	-3,737.28	0.92	0.67	-188.98
1	-6,899.89	52	26	26	50.00	574.42	1,601.91	-839.80	-3,909.03	0.68	0.68	-132.69

The strongest edges here appear to be the bullish ones that look out a couple of weeks. I also tried some different parameters here (using a 50-day closing high for instance). Below is an equity curve assuming a 12-day exit strategy.



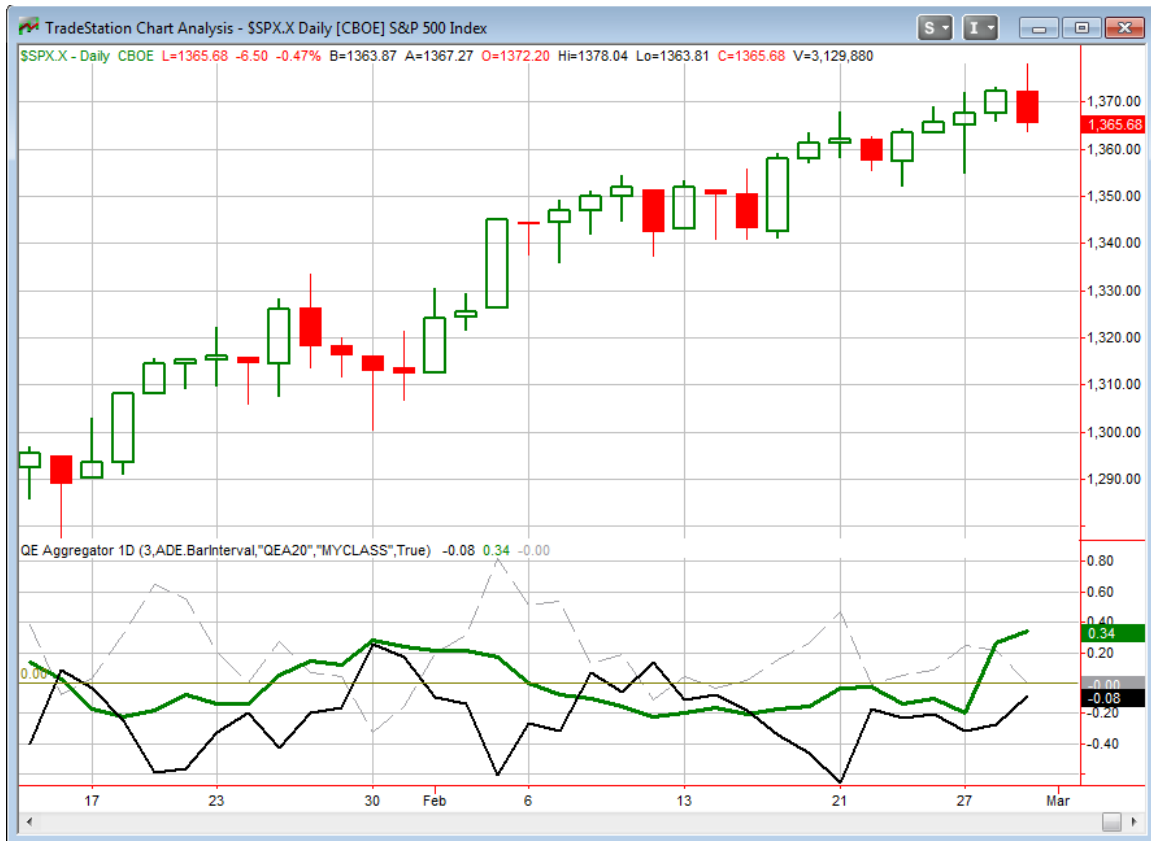
The curve here is very appealing. I am not going to include this study on the short-term active list, but I have placed it on the intermediate-term list.

The Fed did a few things today. For one, they may have helped trigger some of the selling by quashing hopes of QE3 occurring anytime soon. QE periods have led to strong upmoves, so from strictly a trader's standpoint, that's too bad. But Operation Twist continues and the short-term flows associated with that may continue to aide us in timing some entries and exits. And Wednesday afternoon the Fed released its operations schedule for March. I used that schedule to produce projected values for the QE Buying Power Index over the course of the month. This can be seen in the graphic below.



This chart can be found on the QE Buying Power Index information page through the end of March. (<http://www.quantifiableedges.com/members/qebuyingpower.php>) As a quick refresher, the QE Buying Power Index is a simple measure of the number of buying days minus selling days the Fed has embarked on over the last 5 days. Values of 3 or higher have led to a substantial upside edge over the next few days. Values of 0 or lower have led to a downside edge. The chart here suggests that a continued pullback over the next couple of days could present a favorable buying opportunity. After Friday there are only two other days between now and March 20th where POMO flows might provide a buying edge. Liquidity near the end of the month is much stronger and pullbacks between the 20th and 28th would also likely provide favorable entries. Interesting about March is that the QE Buying Power Index never drops to zero or below. This suggests shorting may be tricky.

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



The green Aggregator line is now very positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line remains 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 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. This was indicated on the Systems page before the bell.

Based on the current evidence, expectations are scheduled to remain positive on Thursday. Of course this could change if bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,361.72 on Thursday. This is 0.3% below Wednesday's close. So SPX would need to close down at least this much in order for a long signal to be possible.

The Aggregator is neutral and so am I. The SPX is still too overbought for me to consider getting long. That could change as early as Thursday's close. With evidence somewhat sparse after Thursday, I'll see what emerges before considering taking on new positions as early as Friday morning.

Intermediate-term Outlook (2 weeks – 2 months)– updated 2/27 – bullish

The intermediate-term outlook was last updated in the 2/27/12 Letter. You may use the link below to access it.

[2012-02-27 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.

None tonight.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
<i>GILD(1/3)</i>	<i>2/21/2012</i>	<i>\$46.50</i>	<i>\$45.89</i>	<i>-1.31%</i>		<i>sold on open</i>
<i>SPY(1/4)(s)</i>	<i>2/24/2012</i>	<i>\$136.93</i>	<i>\$137.75</i>	<i>-0.60%</i>		<i>covered @ limit</i>

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