

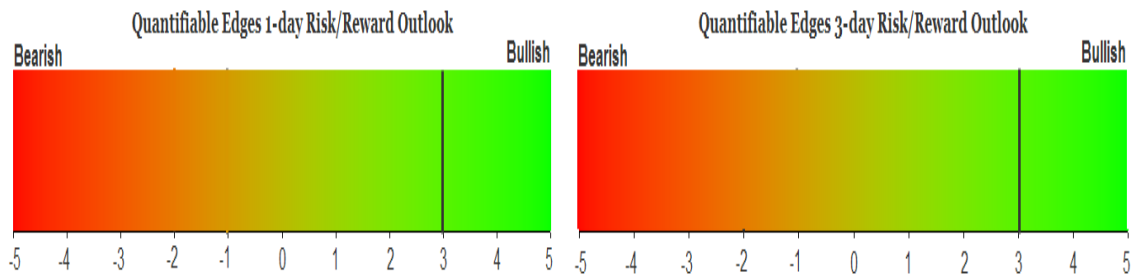
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 8, 2012

Volume 5 Issue 46

Market Overview



Signals Overview

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

Tonight's Research Points

- The unfilled gap up in SPY helped create a bullish pattern.
- The low volume Wednesday ups the odds of the bounce continuing in the next few days.
- Persistently low McClellan Oscillator readings are suggesting a short-term bullish edge.
- The QE Buying Power Index will hit 3 on Thursday.

Short-term Outlook

The Bottom Line

The bounce looks good so far, and there are several studies suggesting it should continue further over the next few days. The SPX is still oversold. I have some long positions that I'm looking to ride a bit further.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
March 8, 2012	3 donw. Unfilled gap. 10-low.	1-2 days	Bullish	1.80%
March 8, 2012	Bounce from RSI(2)<5 on lower volume	1-2 days	Bullish	1.35%
March 8, 2012	McClellan Osc % Rank 4-day sum < 5	1-5 days	Bullish	2.20%
March 7, 2012	3 donw. Unfilled gap. 10-low.	1-2 days	Bullish	
March 7, 2012	TICK TomOscillator extreme	1-2 days	Bullish	
March 6, 2012	SPY 5-day low 1st time in 10 days	1-4 days	Bullish	1.35%
Active - Long Term				
March 5, 2012	Negative breadth divergences	int term	Bearish	
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	
Dropped Tonight				
February 29, 2012	Russell down 3 days. SPX 3-day high.	1-6 days	Bullish	3.95%

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

The Evidence

A small gap up never filled and the market went on to make solid gains on Wednesday. The SPX rallied 0.7%, the Nasdaq rose 0.9%, and the Russell 2000 gained 1.1%. Breadth was strongly positive as the NYSE Up Issues % came in at 78% and the Up Volume % was 80%. Total NYSE volume came in quite a bit lower than Tuesday.

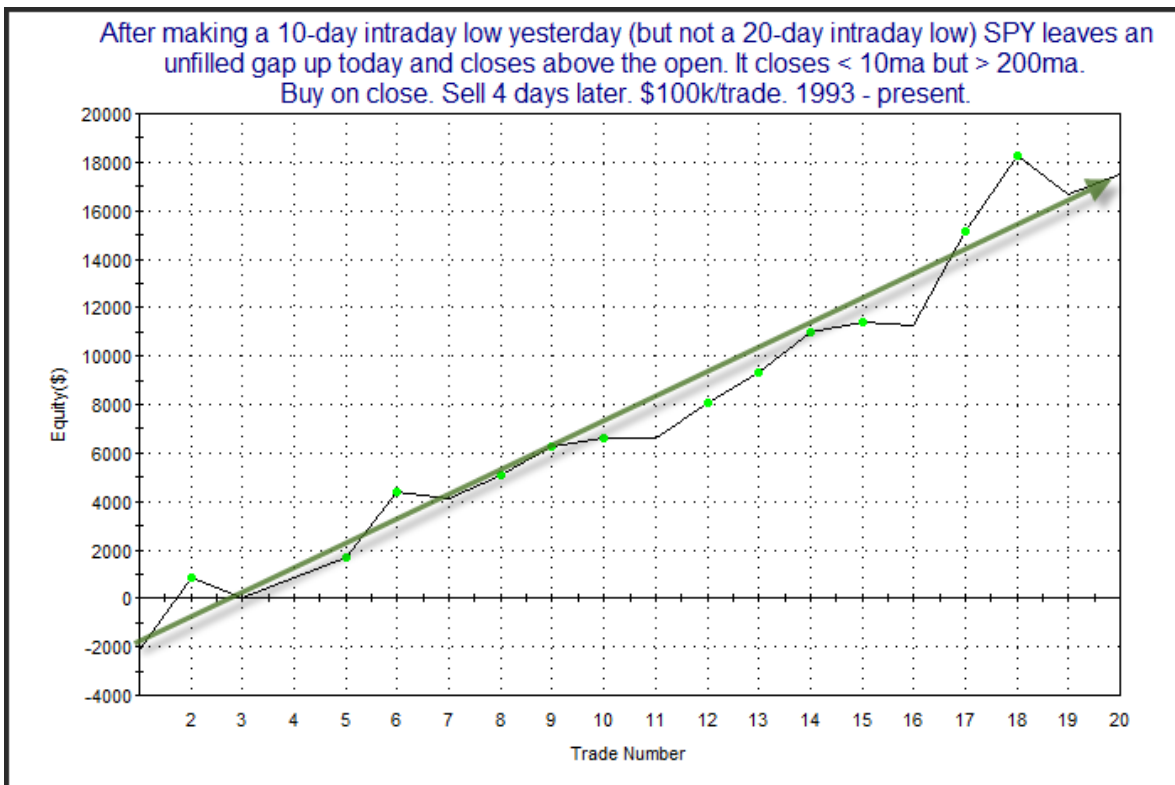
The price action in SPY showed some real strength in that it gapped up, never filled, and closed above the open. When the market is coming off an oversold level in an uptrend and is still not overbought, this pattern will often be followed by further gains. This was demonstrated in the 6/10/11 subscriber letter. In that letter I also found that when the SPY pattern occurs following a short-term low it appears to provide a bullish edge, but when it occurs after an intermediate-term low then the bullish inclinations no longer hold true. The current setup is bullish and I have updated the stats below.

After making a 10-day intraday low yesterday (but not a 20-day intraday low) SPY leaves an unfilled gap up today and closes above the open. It closes < 10ma but > 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
10	16,199.32	20	13	7	65.00	2,283.83	5,666.72	-1,927.20	-4,060.20	1.19	2.20	809.97
9	20,559.98	20	11	9	55.00	2,876.12	6,522.72	-1,230.82	-3,329.90	2.34	2.86	1,028.00
8	22,796.53	20	14	6	70.00	2,326.35	5,468.09	-1,628.73	-5,654.80	1.43	3.33	1,139.83
7	21,681.87	20	14	5	70.00	2,385.85	5,136.00	-2,344.00	-9,172.30	1.02	2.85	1,084.09
6	17,323.00	20	13	7	65.00	2,027.91	5,589.68	-1,291.40	-3,309.80	1.57	2.92	866.15
5	17,431.96	20	15	5	75.00	1,457.13	4,106.63	-885.01	-1,949.70	1.65	4.94	871.60
4	17,528.23	20	14	6	70.00	1,615.38	3,904.83	-847.84	-2,096.99	1.91	4.45	876.41
3	11,771.02	21	13	8	61.90	1,416.67	3,914.92	-830.71	-1,874.00	1.71	2.77	560.52
2	8,098.21	21	13	8	61.90	1,227.38	2,828.00	-982.21	-2,183.21	1.25	2.03	385.63
1	-191.98	21	10	10	47.62	786.22	1,431.89	-805.42	-2,895.33	0.98	0.98	-9.14

All 21 instances closed above the entry price at some point in the next week.

100% reliability is comforting and the size of the moves are impressive as well. Below is an equity curve that assumes a 4-day holding strategy.



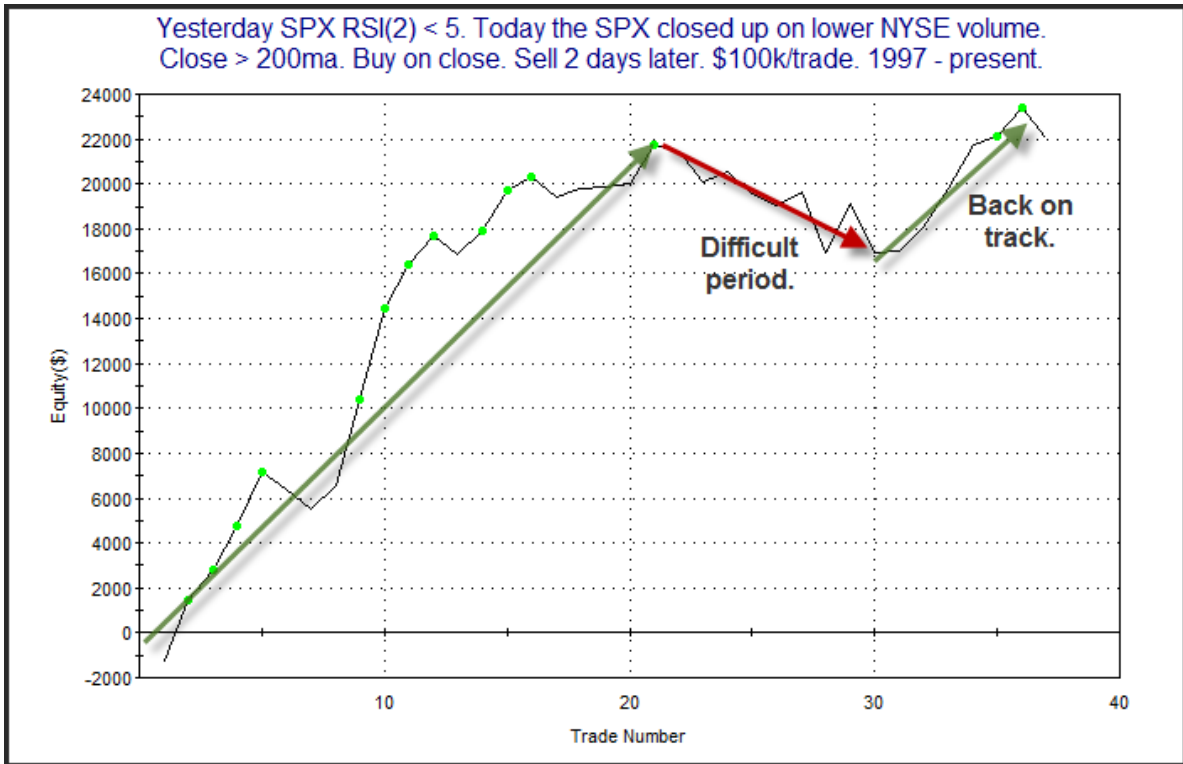
The upslope appears very consistent as well. This study is very compelling and I have included it on the Active List.

Another study, from the 3/18/11, considered volume's impact on a short-term oversold bounce. It also utilized a long-term trend filter. I have updated the results below.

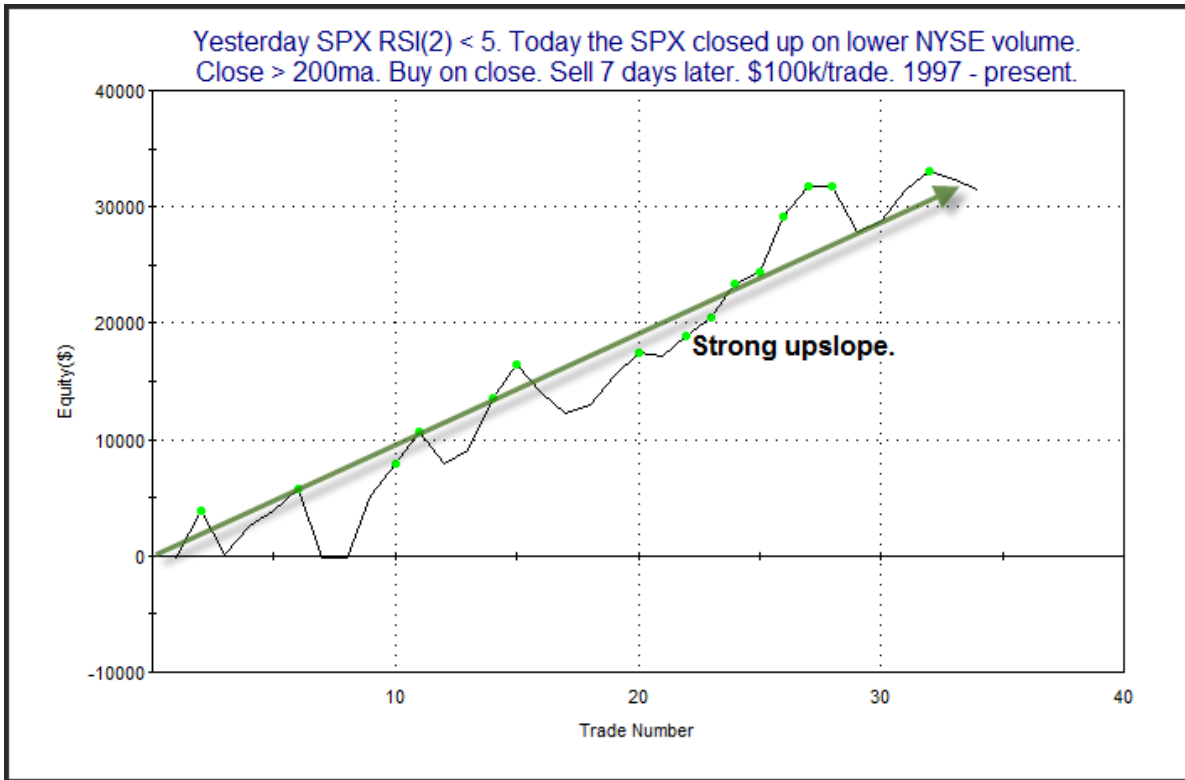
Yesterday SPX RSI(2) < 5. Today the SPX closed up on lower NYSE volume. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	19,514.73	33	16	17	48.48	3,366.38	6,440.94	-2,020.43	-7,402.88	1.67	1.57	591.36
9	27,314.91	34	22	12	64.71	2,654.91	6,371.46	-2,591.10	-6,195.44	1.02	1.88	803.38
8	16,873.19	34	23	11	67.65	2,167.48	6,486.48	-2,998.07	-7,580.04	0.72	1.51	496.27
7	31,471.84	34	23	11	67.65	2,348.25	5,418.09	-2,048.89	-5,975.16	1.15	2.40	925.64
6	27,994.71	35	23	12	65.71	2,089.88	5,668.38	-1,672.71	-3,510.00	1.25	2.39	799.85
5	23,603.35	35	20	15	57.14	2,400.93	5,396.71	-1,627.69	-8,178.56	1.48	1.97	674.38
4	21,130.91	37	22	15	59.46	1,901.65	4,223.34	-1,380.35	-2,736.28	1.38	2.02	571.11
3	16,558.66	37	21	16	56.76	1,586.79	4,457.43	-1,047.74	-3,490.90	1.51	1.99	447.53
2	22,079.00	37	25	12	67.57	1,442.48	4,001.40	-1,165.25	-2,735.64	1.24	2.58	596.73
1	12,464.93	37	24	13	64.86	961.41	2,842.84	-816.07	-2,782.56	1.18	2.17	336.89

89% of instances closed above the entry price at some point in the next week.

Like the results of the first study we saw, these also suggest there should be more upside to this bounce. Statistics are impressive looking out several days. The 2-day and the 7-day holding periods appear especially compelling. I generated profit curves for both of them below. First let's take a look at the 2-day holding period.



After looking strong and steady for quite a while, there was a brief difficult period, recent instances suggests the edge remains on track. Now let's look at the 7-day holding period.



The 7-day holding period never underwent a rough patch and the upslope has remained strong and steady for the last 15 years.

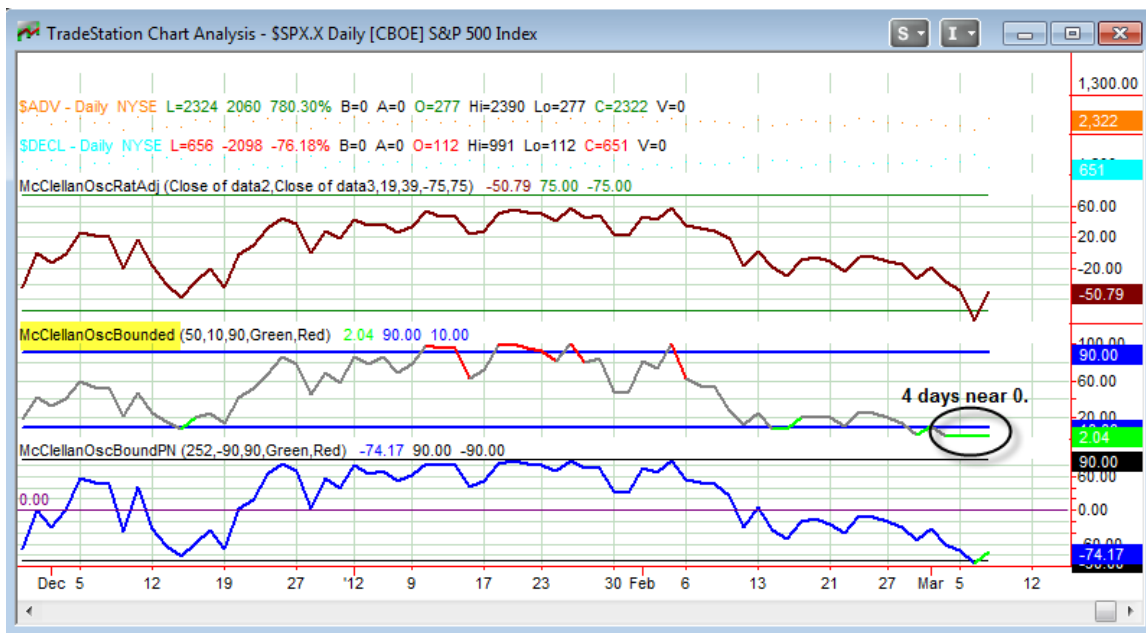
But does the low volume really matter? To answer this I ran the same study below but flipped the volume requirement and insisted volume come in higher.

Yesterday SPX RSI(2) < 5. Today the SPX closed up on **higher** NYSE volume. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - 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	7,323.15	17	11	6	64.71	1,978.73	4,446.73	-2,407.14	-5,944.39	0.82	1.51	430.77
9	7,536.93	17	9	8	52.94	2,249.33	5,134.01	-1,588.39	-4,749.38	1.42	1.59	443.35
8	5,198.93	17	11	6	64.71	1,528.61	4,174.09	-1,935.97	-4,567.61	0.79	1.45	305.82
7	1,272.97	19	10	9	52.63	2,012.64	4,869.18	-2,094.83	-3,822.96	0.96	1.07	67.00
6	-1,658.32	19	9	10	47.37	1,925.65	5,552.91	-1,898.92	-4,199.69	1.01	0.91	-87.28
5	-2,071.07	19	9	10	47.37	1,342.26	3,532.25	-1,415.14	-2,969.64	0.95	0.85	-109.00
4	-4,197.57	20	11	9	55.00	929.63	2,587.95	-1,602.61	-2,541.13	0.58	0.71	-209.88
3	-10,722.45	20	6	14	30.00	1,234.45	3,939.79	-1,294.94	-2,517.13	0.95	0.41	-536.12
2	-8,343.62	20	8	12	40.00	705.60	2,794.56	-1,165.70	-1,962.36	0.61	0.40	-417.18
1	-6,590.57	20	8	12	40.00	347.28	761.76	-780.74	-1,774.60	0.44	0.30	-329.53

Volume accompanying a move can sometimes signify enthusiasm for the direction of the move. Short-term oversold bounces sometimes remind me of junior high school girls. Back when I was in school, if you wanted a girl to like you then you had to make sure she didn't think you liked her. Showing any enthusiasm would scare them off quickly. You had to play it cool, man. It appears that is what the bounce did today - it played it cool, man. And now it's chances are better.

An interesting breadth study also triggered tonight. It was from the 3/16/11 subscriber letter and used the 50-day McClellan Oscillator % Rank indicator that I show on the charts page each night. The chart below is taken from the charts page and illustrates what I am looking at. The middle indicator is the 50-day McClellan Oscillator % Rank indicator. When it falls to zero that means the McClellan Oscillator is at its lowest point of the last 50 days. It was at zero on Friday, Monday, and Tuesday. On Wednesday it edged up just slightly to 2. These very weak readings indicate an oversold breadth condition.



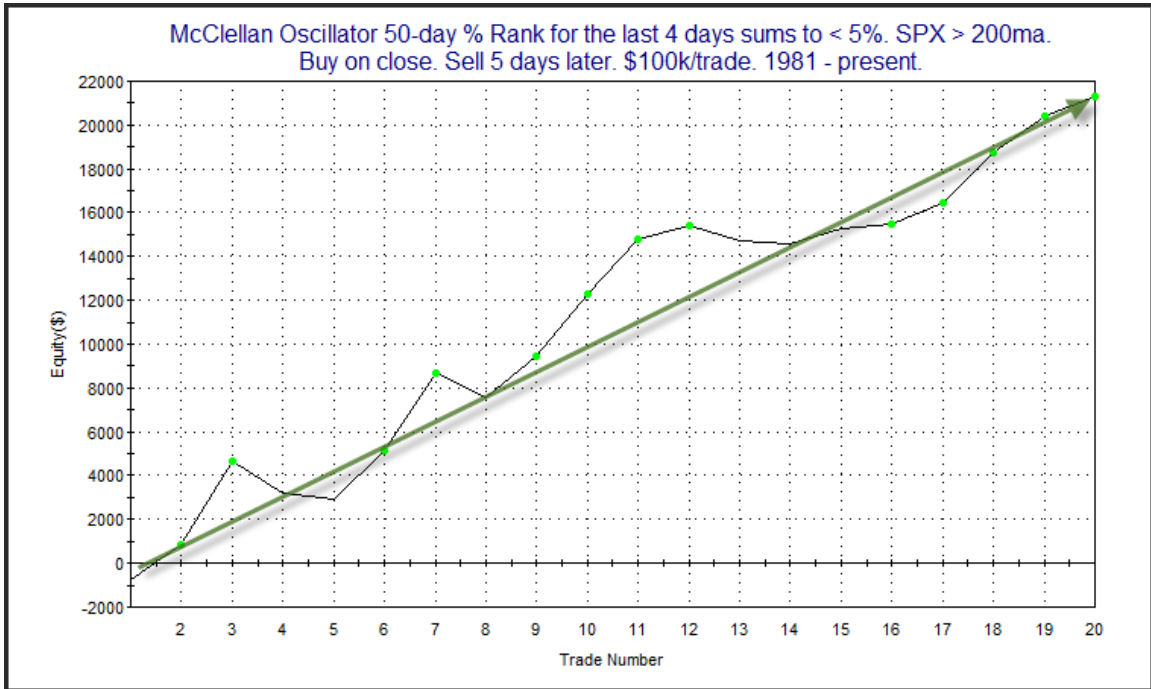
The study below looks at the sum total of the 50-day McClellan Oscillator % Rank indicator over the last four days. If the sum is < 5% an entry is triggered. All results are updated.

McClellan Oscillator 50-day % Rank for the last 4 days sums to < 5%. SPX > 200ma.
Buy on close. Sell X days later. \$100k/trade. 1981 - 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	15,088.57	20	10	10	50.00	3,227.41	7,040.07	-1,718.56	-3,143.25	1.88	1.88	754.43
9	10,310.64	20	11	9	55.00	2,535.92	6,008.75	-1,953.83	-4,105.91	1.30	1.59	515.53
8	11,258.90	20	13	7	65.00	1,771.24	6,288.43	-1,681.02	-4,132.58	1.05	1.96	562.95
7	16,554.11	20	14	6	70.00	1,773.23	5,938.83	-1,378.53	-2,922.27	1.29	3.00	827.71
6	19,560.29	20	18	2	90.00	1,315.00	4,145.52	-2,054.82	-3,242.31	0.64	5.76	978.01
5	21,298.42	20	14	6	70.00	1,837.35	3,775.68	-737.42	-1,410.50	2.49	5.81	1,064.92
4	20,480.90	21	15	6	71.43	1,858.24	4,190.40	-1,232.13	-2,405.60	1.51	3.77	975.28
3	16,340.37	21	14	7	66.67	1,884.08	5,471.10	-1,433.82	-2,514.10	1.31	2.63	778.11
2	10,421.74	24	15	9	62.50	1,386.47	4,041.90	-1,152.81	-2,735.64	1.20	2.00	434.24
1	12,714.36	35	24	11	68.57	857.32	4,396.50	-714.67	-1,949.22	1.20	2.62	363.27

Every instance posted a close above the entry price at some point in the next 6 days.

Such oversold breadth in the midst of a long-term uptrend has consistently led to further upside market action over the next 1-6 days. With every instance over the last 30+ years leading to short-term higher prices, reliability has been outstanding. Below is a profit curve that assumes a 5-day holding period.



The curve appears to be extremely straight and persistent. This serves to confirm the upside edge.

Of course the current situation is a little odd in that prices actually rose on Wednesday. I filtered to look at other instances that occurred on a rise in price. When I examined those results I found them very similar to the unfiltered results (with substantially fewer instances). This provided some comfort that the edge remained true even after the market has started to bounce like we saw on Wednesday.

One last observation is that the QE Buying Power Index is set to close at 3 on Thursday and again on Monday. A close in the bottom 20% of the 10-day range on either of these days would trigger a long signal in the QE Buying Power Swing System.

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



With tonight's bullish studies the green Aggregator line remained 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 is still well above 0. 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 on the Systems page before the bell.

Based on the current evidence, expectations are scheduled to remain positive on Thursday. This appears unlikely to change but could if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,372.87 on Thursday. This is 1.5% above Wednesday's close. So it would take a strong move up on Thursday to move the Differential Line below 0, signaling an SPX move from oversold to overbought. Unless there is a strong move higher or strong bearish evidence emerges it appears the Aggregator long signal will last at least into Friday.

The unfilled gap up (in both SPY and CAT) meant I was not able to get filled on as much as I wanted. Fortunately I set an aggressive entry for the 1st SPY lot and got filled within \$0.02 of the low. There still appears to be a substantial upside edge, but I am not inclined to chase the price up here. Instead I'll simply manage the exposure I currently have. Details on open trade ideas are in the Trade Ideas section near the bottom of the letter.

Intermediate-term Outlook (2 weeks – 2 months)– updated 3/5 – moderately bullish

The intermediate-term outlook was last updated in the 3/5/12 letter. A link is below:

[2012-03-05 QE Subscriber Letter.pdf](#)

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

CAT – buy 1/3 position @ \$112.49 limit (filled at \$111.55)

CAT – buy 1/3 position @ \$110.09 limit (filled at \$106.57)

CAT – buy 1/3 position @ \$105.93 limit (not filled)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 3/1(CAT-3)

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.

No new trade ideas tonight.

I have taken the limit order for the 3rd lot of CAT off the table for now. Depending on action I may reinstitute that order in the next few days.

No other open orders remain active either.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
CAT(1/3)	3/5/2012	\$111.55	\$108.28	-2.93%		Catapult
CAT(1/3)	3/6/2012	\$106.57	\$108.28	1.60%		Catapult
XIV(1/2)	3/6/2012	\$8.48	\$8.76	3.30%		Aggressive VIX
SPY(1/4)	3/7/2012	\$134.95	\$135.71	0.56%		bought at limit

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