

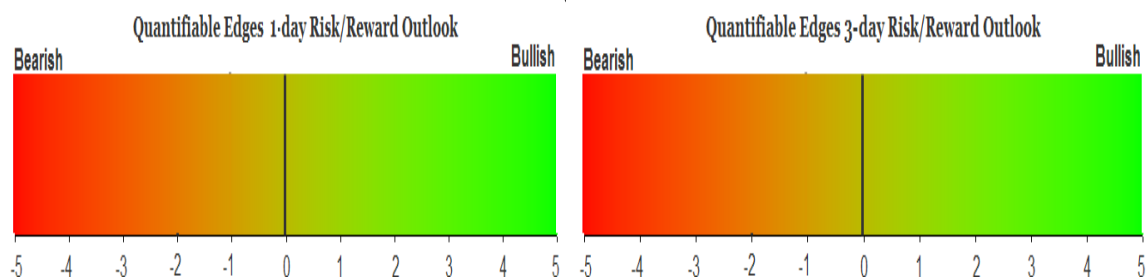
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 3, 2012

Volume 5 Issue 64

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Flat	50% Long XIV	Flat	Long

Tonight's Research Points

- SPX & VIX up 2 days in a row and SPX at a 50-day high suggests a pullback.
- A SOX decline combined with a strong NDX has often been followed by a market pullback over the last 12 years.

Short-term Outlook

The Bottom Line

The Aggregator is now neutral, and there is some evidence tonight suggesting we could see a pullback in the next few days. I've decided to take profits on my index positions and await the next favorable opportunity.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
April 3, 2012	NDX up > 1%. SOX down.	1-6 days	Bearish	-3.20%
April 3, 2012	VIX up SPX up 2x & 50-day high.	1-3 days	Bearish	-1.30%
April 2, 2012	1st Week In April Seasonally Strong	1-4 days	Bullish	2.10%
April 2, 2012	SPX 3-day high. Nas/Rus down 3 days.	1-10 days	Bullish	4.30%
March 23, 2012	3-day pullback from 50-high	1-6 days	Bullish	2.60%
Active - Long Term				
March 14, 2012	SPX & TNX hit 50-day highs	1-50 days	Bearish	
March 14, 2012	50-day high on strong breadth	1-50 days	Bullish	8.00%
March 5, 2012	Negative breadth divergences	int term	Bearish	
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

Despite a fade late in the day, the market still put in solid gains to start April. The SPX rose 0.7%, the NASDAQ rallied 0.9%, and the Russell 2000 gained 1.2%. Breadth was strong as the NYSE Up Issues % came in at 74% and the Up Volume % was 79%. Volume was a bit light.

The SPX and VIX both closed higher for the 2nd day in a row. This triggered a number of bearish studies tonight. On its own, 2 up days for both has suggested a bearish edge. But when you throw in a 50-day high close as I did in the 2/28/12 subscriber letter, the downside edge is even more compelling. Below I have updated the results for that study.

SPX and VIX both close higher the last 2 days. SPX closes at a 50-day high. Buy SPX on close. Sell X days later. \$100k/trade. 1998 - present.												
X Days	All: Net Profit	All: Total Trades	All: % Profitable	All: Winning Trades	All: Losing Trades	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	-2,411.21	15	60.00	9	6	1,059.62	3,434.08	-1,991.31	-4,149.36	0.53	0.80	-160.75
4	-6,556.48	15	46.67	7	8	844.82	1,907.36	-1,558.78	-4,240.48	0.54	0.47	-437.10
3	-7,799.48	15	33.33	5	10	767.20	1,433.12	-1,163.55	-4,423.40	0.66	0.33	-519.97
2	-5,269.30	15	33.33	5	10	584.78	1,078.48	-819.32	-2,752.74	0.71	0.36	-351.29
1	-2,039.86	18	38.89	7	11	275.05	415.16	-360.47	-924.70	0.76	0.49	-113.33
The 12/21/10 instance was the only one NOT to close below the entry price at some point in the next 3 days.												

Stats remain squarely bearish. Below I have listed all 15 instances assuming a 3-day exit strategy.

SPX and VIX both close higher the last 2 days. SPX closes at a 50-day high.
Buy SPX on close. Sell 3 days later. \$100k/trade. 1998 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
12/30/99	Buy	\$1,464.47	(4.44%)	\$920.04
01/04/00	Sell	\$1,399.42		(\$4,558.72)
03/24/00	Buy	\$1,527.57	(1.25%)	\$458.90
03/29/00	Sell	\$1,508.52		(\$1,957.80)
05/28/03	Buy	\$953.22	1.45%	\$2,692.56
06/02/03	Sell	\$967.00		(\$726.96)
09/02/03	Buy	\$1,021.99	(0.06%)	\$712.95
09/05/03	Sell	\$1,021.39		(\$368.60)
12/30/03	Buy	\$1,109.64	1.13%	\$1,131.30
01/05/04	Sell	\$1,122.21		(\$410.40)
03/16/06	Buy	\$1,305.33	(0.62%)	\$421.80
03/21/06	Sell	\$1,297.23		(\$722.76)
09/18/06	Buy	\$1,321.18	(0.24%)	\$551.25
09/21/06	Sell	\$1,318.03		(\$675.75)
09/28/06	Buy	\$1,339.15	(0.38%)	\$54.02
10/03/06	Sell	\$1,334.11		(\$891.70)
04/18/07	Buy	\$1,472.50	0.57%	\$955.42
04/23/07	Sell	\$1,480.93		(\$538.01)
05/19/08	Buy	\$1,426.63	(2.26%)	\$0.00
05/22/08	Sell	\$1,394.35		(\$2,647.40)
04/23/10	Buy	\$1,217.28	(2.13%)	\$206.64
04/28/10	Sell	\$1,191.36		(\$2,924.12)
10/26/10	Buy	\$1,185.64	(0.20%)	\$326.76
10/29/10	Sell	\$1,183.26		(\$1,170.96)
12/21/10	Buy	\$1,254.60	0.23%	\$378.41
12/27/10	Sell	\$1,257.54		(\$246.48)
02/09/12	Buy	\$1,351.95	(0.11%)	\$102.20
02/14/12	Sell	\$1,350.50		(\$1,065.80)
02/27/12	Buy	\$1,367.59	0.48%	\$762.85
03/01/12	Sell	\$1,374.09		(\$275.94)

The record appears fairly impressive. Risk/reward favors the bears nicely with the average drawdown (-1.3%) about 2x the average run-up (0.65%). This study is a bit more powerful than last night's VIX study that just considered both the SPX and VIX closing up on a Friday. I have therefore replaced last night's study on the Active List with this one.

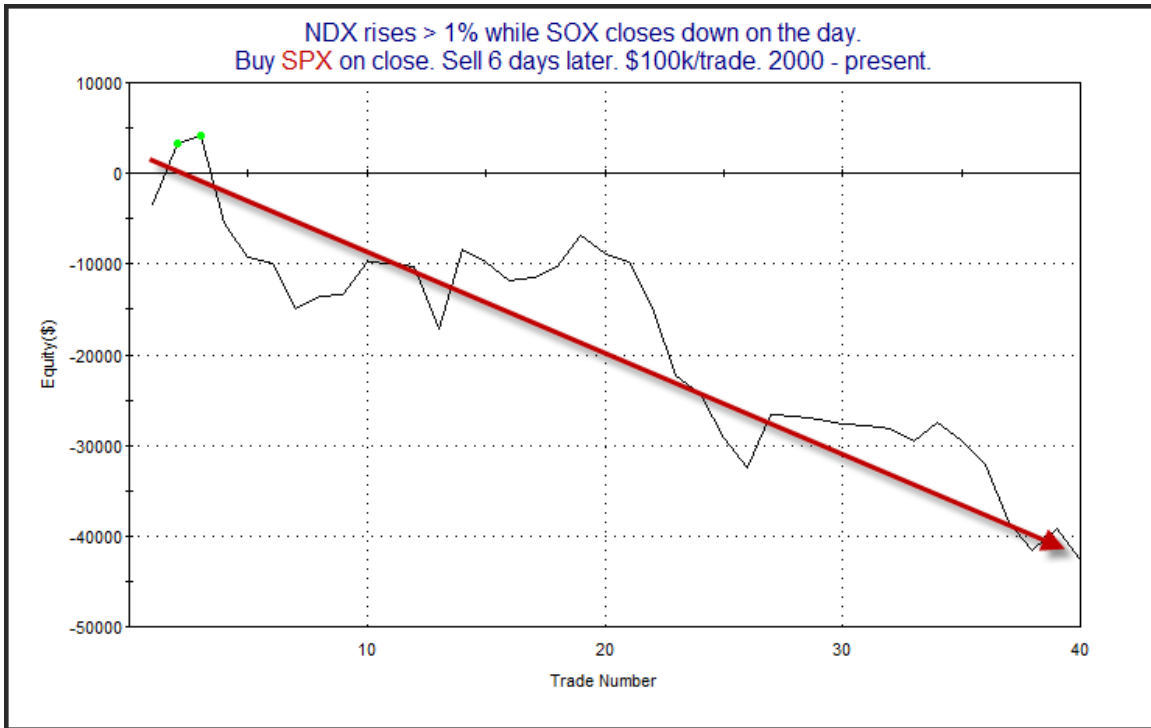
Also interesting on Monday was the discrepancy between the NDX and the SOX. While the NDX rose 1.1% on Monday, the SOX declined slightly - which is very unusual action. It brought about a study last seen in the 9/9/10 Letter which I have updated below.

NDX rises > 1% while SOX closes down on the day. Buy NDX on close. Sell X days later. \$100k/trade. 2000 - present.												
X Days	All: Net Profit	All: Total Trades	All: % Profitable	All: Winning Trades	All: Losing Trades	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	-78,873.15	38	39.47	15	23	5,096.58	18,826.33	-6,753.12	-13,954.56	0.75	0.49	-2,075.61
9	-73,004.79	38	31.58	12	26	5,916.14	22,154.89	-5,538.40	-15,780.45	1.07	0.49	-1,921.18
8	-69,471.62	39	28.21	11	28	6,598.24	30,307.45	-5,073.30	-13,288.50	1.30	0.51	-1,781.32
7	-83,330.41	40	22.50	9	31	8,368.69	31,628.02	-5,117.70	-17,436.00	1.64	0.47	-2,083.26
6	-111,506.22	40	22.50	9	31	7,540.46	23,421.19	-5,786.14	-21,090.48	1.30	0.38	-2,787.66
5	-79,955.45	41	34.15	14	27	4,343.50	12,749.43	-5,213.50	-12,790.08	0.83	0.43	-1,950.13
4	-49,043.26	41	46.34	19	22	3,178.98	11,322.33	-4,974.72	-12,796.24	0.64	0.55	-1,196.18
3	-28,519.25	42	40.48	17	25	4,487.37	15,615.69	-4,192.18	-15,779.50	1.07	0.73	-679.03
2	-4,718.21	44	45.45	20	24	3,551.89	16,624.43	-3,156.50	-9,160.50	1.13	0.94	-107.23
1	-2,955.38	46	45.65	21	25	2,759.28	9,397.52	-2,436.01	-6,256.64	1.13	0.95	-64.25

Six days out 78% of the instances were losers and the average occurrence was nearly a 3% loss. That seems to be a fairly substantial edge. I also updated how the SPX performed while this was all going on.

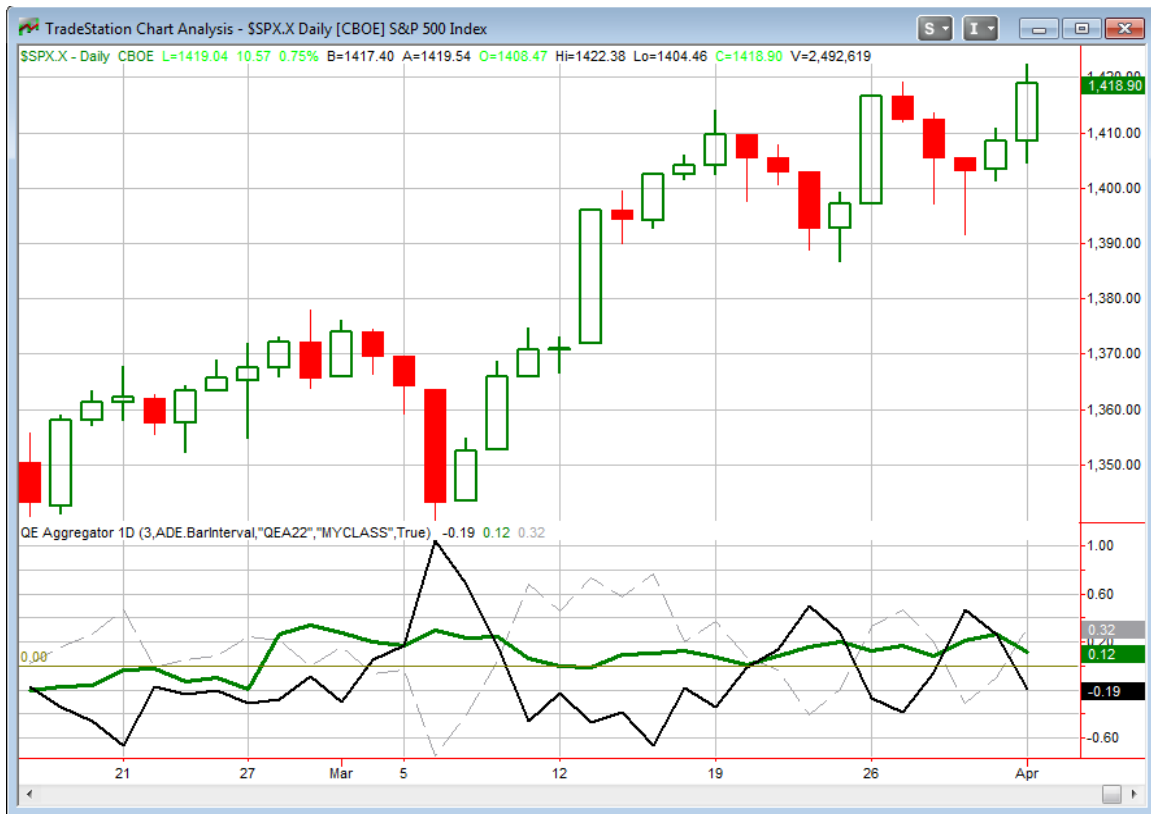
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10	-17,016.11	38	42.11	16	22	2,937.20	9,774.70	-2,909.61	-8,478.02	1.01	0.73	-447.79
9	-23,010.50	38	44.74	17	21	2,729.14	9,278.30	-3,305.04	-8,963.07	0.83	0.67	-605.54
8	-29,747.59	39	46.15	18	21	2,297.00	9,165.45	-3,385.41	-7,574.41	0.68	0.58	-762.76
7	-38,955.32	40	45.00	18	22	2,198.05	10,101.57	-3,569.10	-11,391.59	0.62	0.50	-973.88
6	-42,523.73	40	30.00	12	28	3,031.02	8,753.07	-2,817.71	-9,589.14	1.08	0.46	-1,063.09
5	-37,617.75	41	41.46	17	24	1,803.11	6,877.04	-2,844.61	-7,519.22	0.63	0.45	-917.51
4	-23,770.26	41	48.78	20	21	1,707.54	5,068.10	-2,758.15	-11,917.40	0.62	0.59	-579.76
3	-12,302.67	42	45.24	19	23	1,940.00	6,877.26	-2,137.51	-9,480.90	0.91	0.75	-292.92
2	-5,958.29	44	43.18	19	25	1,660.54	5,842.98	-1,500.34	-6,411.90	1.11	0.84	-135.42
1	3,635.41	46	50.00	23	23	1,321.04	5,396.04	-1,162.98	-2,692.80	1.14	1.14	79.03

The pullbacks haven't been quite as reliable or as strong as the NDX but there still appears to be a decent downside edge. Below is an equity curve that assumes a 6-day holding period.



While choppy, it has persisted lower and continues to make new lows. Overall, this study appears worthy of consideration.

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



Despite the 2 bearish studies tonight the green Aggregator Line remained nicely positive. Readings above 0 mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line took a dive and is now 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 oversold 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 meant the Aggregator System changed from long to flat at the close. This was noted on the systems page before the bell.

Based on the current studies, expectations are scheduled to remain positive on Tuesday. Of course this could change if strong bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,409.77 on Tuesday. This is 0.6% below Monday's close. So it will take an SPX decline of at least this much to move the Differential Line back above zero.

After last night's strongly bullish study based on the NDX, I was considering trying to ride my QQQ position for a few days. But now we have a study tonight that largely counters it and casts doubt on the short-term market direction. Rather than press my luck with a neutral Aggregator signal, I will simply look to get flat my index position on Tuesday.

Intermediate-term Outlook (2 weeks – 2 months)– updated 4/2 – moderately bullish

The intermediate-term outlook was last updated in the 4/2/12 letter. You may use the link below to access it:

[2012-04-02 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
XIV(1/2)	3/6/2012	\$8.48	\$12.29	44.93%	\$9.49	Aggressive VIX
<i>HPQ(1/3)</i>	<i>3/23/2012</i>	<i>\$23.03</i>	<i>\$23.89</i>	<i>3.73%</i>		<i>sold on open</i>
<i>SPY(1/4)</i>	<i>3/29/2012</i>	<i>\$140.23</i>	<i>\$141.80</i>	<i>1.12%</i>		<i>sold on close</i>
QQQ(1/4)	4/2/2012	\$67.46	\$68.25	1.17%		sell @ \$68.25 limit

QQQ – If QQQ gaps down and does not fill within the 1st half hour I may use a stop or simply exit at that point. If I decide to do so I will send out an intraday update.

XIV – It's notable that the VIX futures term structure has flattened out quite a bit recently. As of Monday's close the 2nd month VIX futures are priced about 10.8% above the front month. This is still a nicely favorable roll for XIV, but not nearly as favorable as a couple of weeks ago when the difference between the front and 2nd months were over 20%. So while there still appears to be an edge in holding XIV, it is not as prevalent as it was. This term-structure situation bears watching. If contango continues to wither, then I will likely exit all or part of the position. (If any of this does not make sense to you, then I would recommend watching the VIX-based ETFs and the Quantifiable Edges Aggregator video from March 30, 2011 on the videos page.)

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