

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 5, 2012

Volume 5 Issue 128

Market Overview



Signals Overview

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

Tonight's Research Points

- Extremely strong breadth over the last few days is suggesting more short-term price gains.
- The consistent closes in the upper part of the daily range are an indication of excessive optimism and suggest a possible short-term pullback.

Short-term Outlook

The Bottom Line

The short-term Differential reading is suggesting the market is as overbought now as it has been all of 2012. Expectations, remain positive, though, so I am still standing aside awaiting better risk/reward.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
July 5, 2012	8-day avg closing range > 75%	1-2 days	Bearish	-1.40%
July 5, 2012	75% Up Issues 2 of 3 & 10-high. > 200	1-6 days	Bullish	2.40%
June 29, 2012	SPY closes month at a high	1-5 days	Bullish	2.35%
Active - Long Term				
June 18, 2012	POMO modestly bullish	int term	slight bull	
June 13, 2012	FTD with modest breadth & vol	int term	Bearish	
February 1, 2012	Golden Cross	int term	Bullish	

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

The Evidence

The market put in a strong move in a shortened session on Tuesday. The SPX rose 0.6%, the Nasdaq gained 0.8%, and the Russell 2000 rallied 1.3%. Breadth was solidly positive as the NYSE Up Issues % came in at 75% and the Up Volume % was 77%. Total NYSE volume was light as would be expected with the shortened session prior to a holiday.

The Quantifinder saw a huge number of studies trigger but nearly every one of them was related to the abnormally low volume. On a normal day, I would take these studies into consideration. On a half-day prior to a holiday – they mean nothing. So I ignore them all. There were a couple of non-volume related studies that were worth examining though.

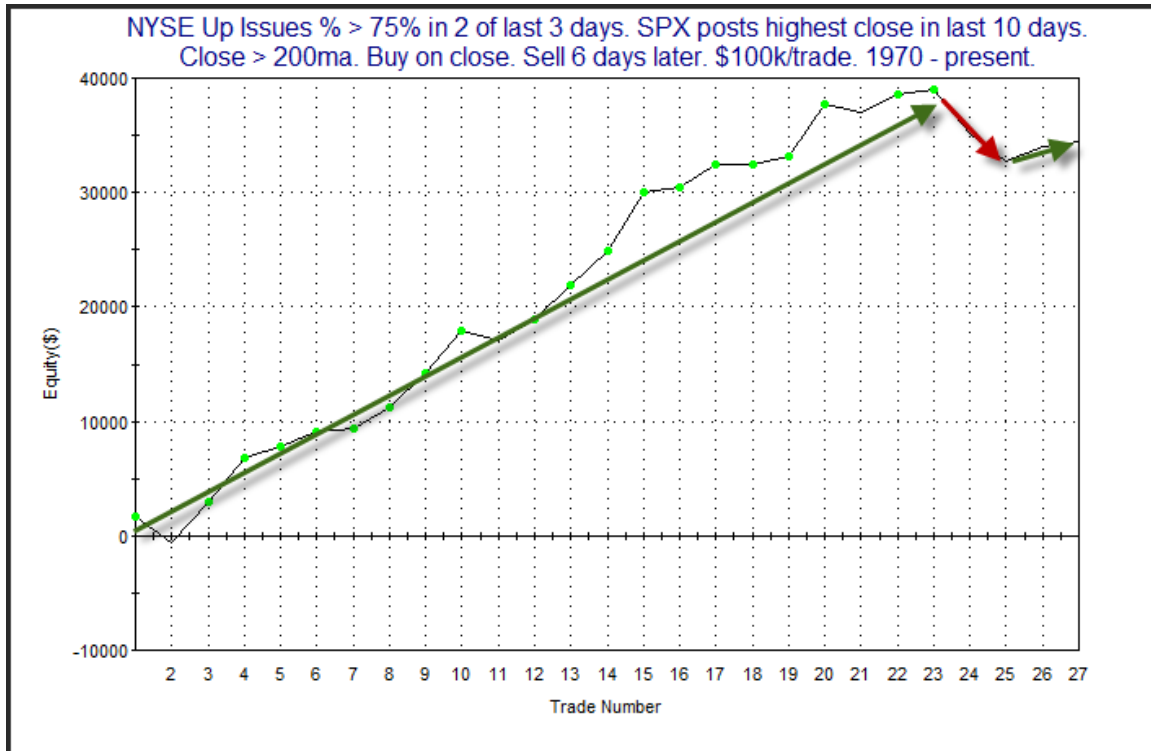
One study that appeared in the Quantifinder examined the strong breadth we have now seen in 2 of the last 3 days, and the fact that the market closed at a 10-day high. It was last seen in the 1/4/12 subscriber letter and has been updated below.

NYSE Up Issues % > 75% in 2 of last 3 days. SPX posts highest close in last 10 days. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1970 - 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
20	53,050.00	23	18	5	78.26	4,649.92	10,448.44	-6,129.71	-15,033.10	0.76	2.73	2,306.52
19	54,613.82	24	19	5	79.17	4,351.47	10,910.56	-5,612.80	-11,094.08	0.78	2.95	2,275.58
18	54,523.09	24	20	4	83.33	3,983.29	8,727.84	-6,285.70	-11,176.96	0.63	3.17	2,271.80
17	52,935.40	24	20	4	83.33	3,910.71	9,187.20	-6,319.72	-10,308.94	0.62	3.09	2,205.64
16	52,425.03	24	20	4	83.33	3,876.03	9,539.88	-6,273.87	-12,209.26	0.62	3.09	2,184.38
15	42,525.96	24	18	6	75.00	3,900.12	8,941.56	-4,612.69	-12,665.84	0.85	2.54	1,771.91
14	35,038.57	24	20	4	83.33	3,267.28	7,807.79	-7,576.75	-16,504.96	0.43	2.16	1,459.94
13	38,607.50	25	19	6	76.00	3,311.90	8,597.16	-4,053.10	-12,673.98	0.82	2.59	1,544.30
12	33,157.06	26	19	7	73.08	3,270.48	7,623.04	-4,140.29	-16,601.16	0.79	2.14	1,275.27
11	42,265.34	26	20	6	76.92	3,084.34	7,783.28	-3,236.92	-10,687.08	0.95	3.18	1,625.59
10	34,798.10	26	20	6	76.92	2,883.71	7,954.00	-3,812.70	-10,636.02	0.76	2.52	1,338.39
9	35,478.63	26	19	7	73.08	2,909.26	8,085.92	-2,828.18	-6,176.04	1.03	2.79	1,364.56
8	31,897.73	26	19	7	73.08	2,433.26	6,037.28	-2,047.75	-6,641.50	1.19	3.23	1,226.84
7	34,331.05	26	19	7	73.08	2,406.16	6,145.92	-1,626.56	-4,207.64	1.48	4.02	1,320.42
6	34,494.31	27	22	5	81.48	2,028.56	5,002.50	-2,026.80	-3,812.48	1.00	4.40	1,277.57
5	28,667.44	27	19	8	70.37	1,952.94	4,482.50	-1,054.81	-3,191.62	1.85	4.40	1,061.76
4	19,488.17	28	21	7	75.00	1,392.87	6,138.16	-1,394.58	-3,595.13	1.00	3.00	696.01
3	10,516.26	28	18	10	64.29	1,253.36	4,376.64	-1,204.43	-5,105.87	1.04	1.87	375.58
2	7,732.86	31	19	12	61.29	984.48	4,399.92	-914.36	-3,149.67	1.08	1.70	249.45
1	6,080.94	33	20	13	60.61	596.07	1,848.00	-449.26	-1,564.34	1.33	2.04	184.27

All 33 instances posted a close above the entry price at some point in the next 6 days.

As noted at the bottom, the consistency suggesting at least some short-term follow through is incredible. While the edge appears to persist for 3-4 weeks, a large portion of

that edge has played out over the 1st 6 days. Below is a profit curve that assumes a 6-day exit.

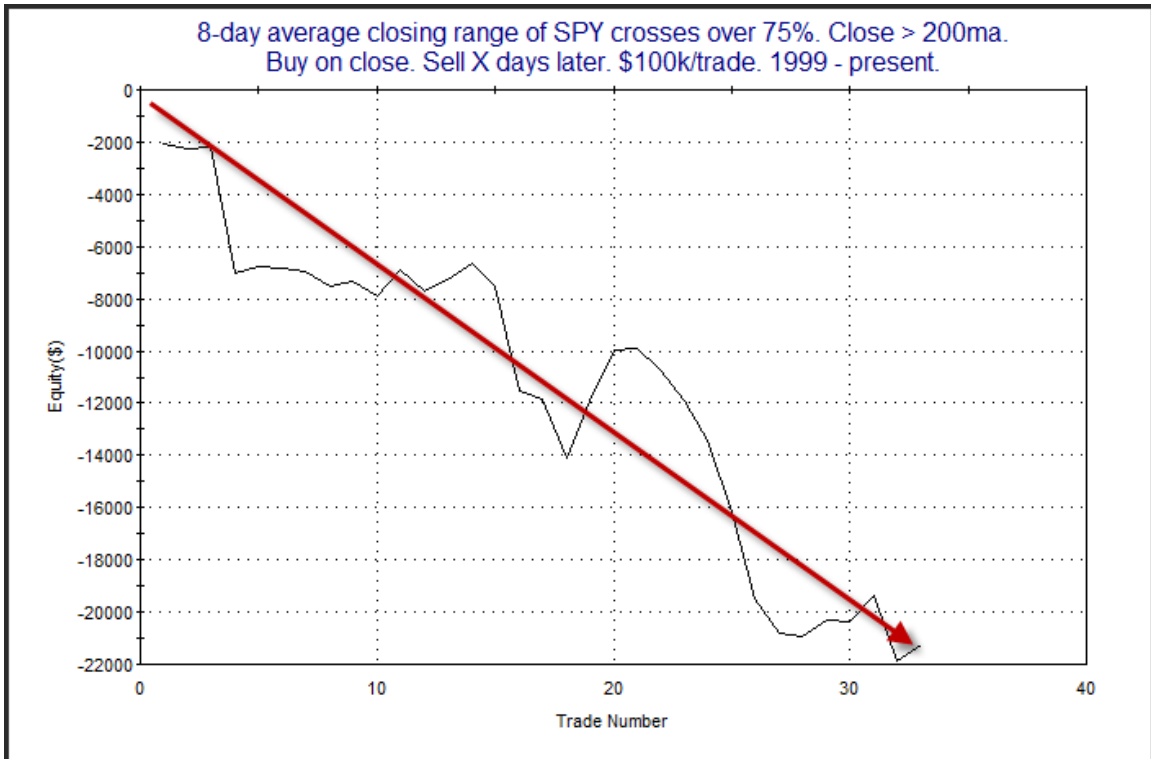


This profit curve was extremely straight for a long period of time, but saw a minor stumble last year for the 6-day period. With the last 2 instances now falling into line, I am not terribly concerned about that dip.

The market has seen a lot of strong finishes lately. When it consistently closes near the high of the day it suggests optimism on the part of traders. This optimism is now at a level that suggests it is a bit overdone and there is a good chance of a pullback. The study below from the 2/13/12 subscriber letter exemplifies this concept. I have updated all of the statistics.

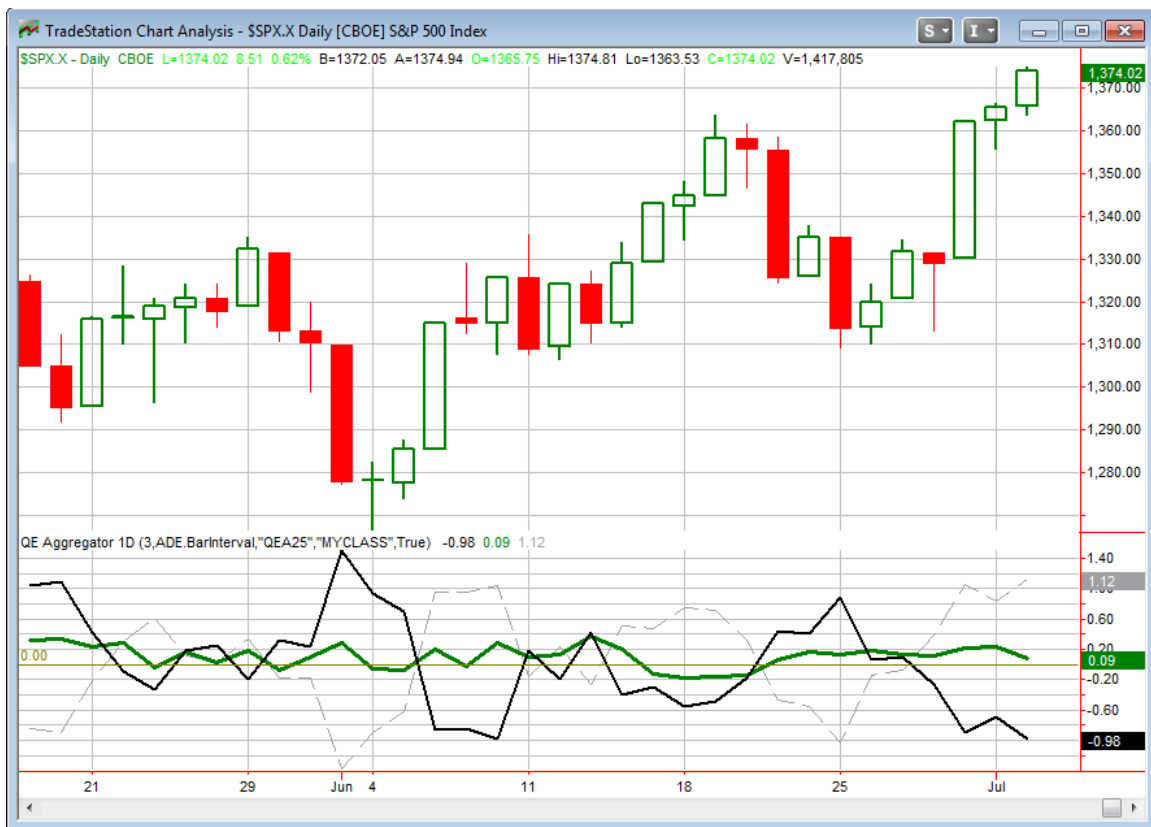
8-day average closing range of SPY crosses over 75%. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1999 - present.												
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5	-23,200.84	29	14	15	48.28	949.66	2,426.72	-2,433.07	-4,637.61	0.39	0.36	-800.03
4	-19,087.76	29	13	16	44.83	997.68	2,907.88	-2,003.60	-4,807.86	0.50	0.40	-658.20
3	-18,988.07	30	12	18	40.00	833.67	2,604.54	-1,610.67	-3,618.23	0.52	0.35	-632.94
2	-21,263.08	33	12	21	36.36	746.67	2,186.14	-1,439.19	-4,848.40	0.52	0.30	-644.34
1	-9,192.44	33	15	18	45.45	332.24	1,029.30	-787.56	-2,738.12	0.42	0.35	-278.56

While the downside edge appears to remain in place for a full week, most of the edge has been realized over the 1st 2 days. Below is an equity curve showing how the edge has played out using a 2-day exit strategy.



It hasn't been the most consistent edge but it has moved from upper left to lower right and it appears worthy of consideration. So we have a mix of studies being added to the Short-Term Active List tonight.

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



With tonight's studies factored in the green Aggregator line dipped a little but remained 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 now as far above 0 as it has been at any point in 2012. This means the SPX is strongly overbought versus expectations. So net expectations are bullish but the SPX is extremely 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 meant the Aggregator System remained flat at the close.

Based on the current active studies, expectations are set to remain positive on Thursday. Of course this could change if more bearish evidence emerges. Meanwhile, the Differential Pivot will be 1,368.43 on Thursday. This is only about 0.4% below Tuesday's close. A decline of this amount would flip the Differential Line back above zero, signaling the SPX is no longer short-term "overbought". It could also trigger a long Aggregator signal.

Even if the Differential Line turns positive I would probably want to see a bit more of a pullback before becoming a buyer. I also anticipate scaling in as I often do. For now I am taking it one day at a time. Rather than anticipate what Thursday's action may bring, I'll simply wait and see, and then consider taking a position Friday depending on what plays out.

Intermediate-term Outlook (2 weeks – 2 months)– updated 7/2 – slightly bullish

Intermediate-term outlook was last updated in the 6/25 letter. A link is below:

[2012-07-02 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

None

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