

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 15, 2012

Volume 5 Issue 157

Market Overview



Signals Overview

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

Tonight's Research Points

- The tight consolidation near a 50-day high suggests an upside edge.
- The strongly rising VIX with the SPY also up is something that has often been followed by market gains.

Short-term Outlook

The Bottom Line

Story hasn't changed. This non-action just isn't creating a compelling edge. I'll remain sidelined.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
August 15, 2012	SPY up. VIX up > 6%.	1-3 days	Bullish	1.60%
August 15, 2012	SPY 50-high then 5-day inside range	1-3 days	Bullish	1.10%
August 14, 2012	3/10 Offset HV < 0.3 4th day in row	1-4 days	Bullish	
August 14, 2012	Up 5 in row to 50-high, then down	1-2 days	Bullish	
August 14, 2012	Multiple days of very low vol near high	1-2 days	Bearish	
Active - Long Term				
August 10, 2012	SPX & TNX 50-day highs.	1-20 days	Bearish	
July 30, 2012	SPX 50-day high on 90% up vol	1-50 days	Bullish	
July 16, 2012	POMO modestly bullish	int term	Bullish	
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

More dull trading on Tuesday – unless you were watching the VIX. The SPX lost a measly 0.01% (but the SPY finished just above breakeven), the Nasdaq fell 0.18%, and the Russell 2000 declined 0.33%. Breadth was slightly negative as the NYSE Up Issues % came in at 49% and the Up Volume % was 46%. NYSE volume rose but was still pretty pathetic.

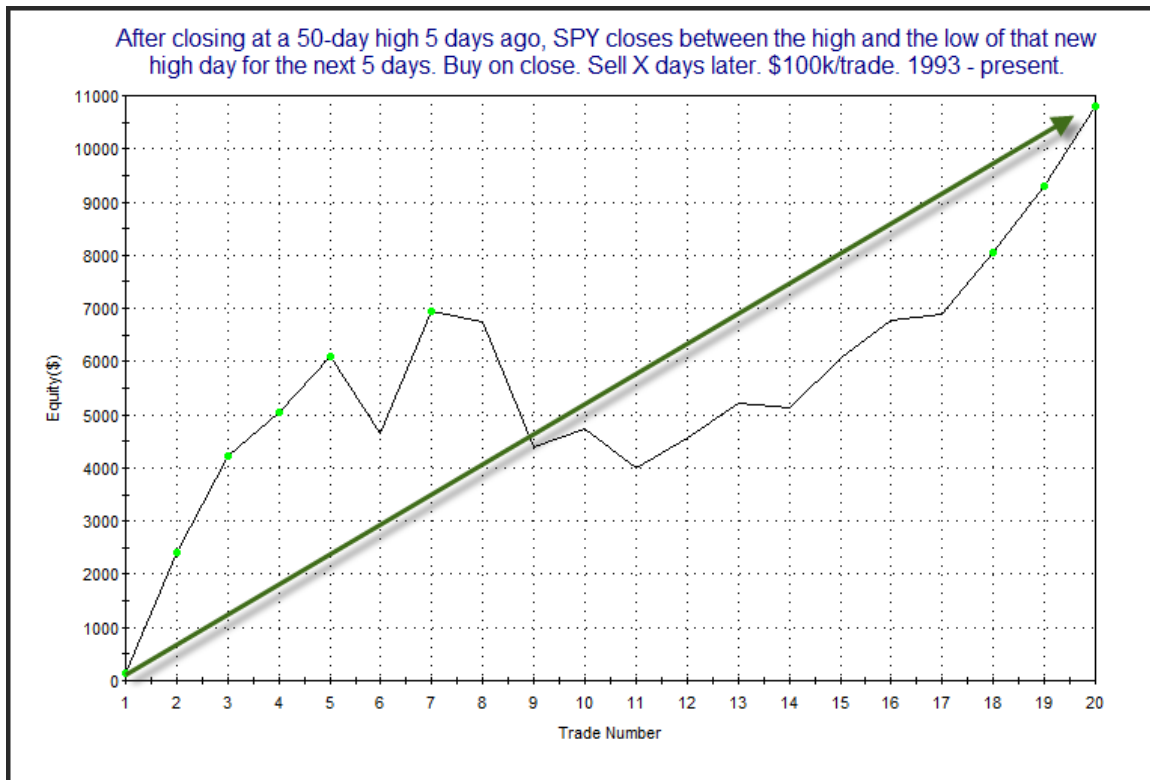
The range over the last week has been extremely tight. Every SPY close in the 5 days since 8/7 has been within the daily range of that 8/7/12 bar. It is said that consolidations are often resolved in the direction of the trend. This guideline suggests that we're more likely to see another leg up from here than a breakdown. Last night I showed a study that used the persistently low 3/10 Offset HV to suggest the tightening in the uptrend suggested an upside edge. The study below is a similar concept – looking for a tight range in an upmove. It was last seen in the 2/2/12 letter and has been updated.

After closing at a 50-day high 5 days ago, SPY closes between the high and the low of that new high day for the next 5 days. 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	28,190.29	20	17	3	85.00	2,004.97	6,287.04	-1,964.71	-5,182.56	1.02	5.78	1,409.51
9	24,483.73	20	18	2	90.00	1,520.31	6,322.56	-1,440.95	-2,251.44	1.06	9.50	1,224.19
8	22,940.31	20	17	3	85.00	1,610.64	6,287.04	-1,480.21	-2,060.28	1.09	6.17	1,147.02
7	15,727.83	20	15	5	75.00	1,552.02	5,339.84	-1,510.50	-3,472.29	1.03	3.08	786.39
6	7,179.15	20	13	7	65.00	1,274.49	3,362.56	-1,341.32	-2,992.38	0.95	1.76	358.96
5	9,543.88	20	11	9	55.00	1,487.13	3,031.04	-757.17	-2,425.20	1.96	2.40	477.19
4	11,758.79	20	13	7	65.00	1,245.46	2,806.08	-633.16	-1,541.60	1.97	3.65	587.94
3	10,787.66	20	15	5	75.00	1,039.42	2,296.96	-960.73	-2,368.80	1.08	3.25	539.38
2	4,680.96	20	13	7	65.00	784.79	1,817.10	-788.75	-1,627.93	0.99	1.85	234.05
1	257.26	20	11	9	55.00	536.94	1,433.49	-627.68	-1,100.97	0.86	1.05	12.86

-17 of 20 instances (85%) closed above the entry price at some point in the next 3 days.
- All instances closed above the entry price at some point in the next 2 weeks.
-17 of 20 instances (85%) also posted a new 50-day high at some point in the next weeks.

It certainly appears to confirm both the old technical adage and last night's study. Results favor the long side over the immediate 3-day period and they are even more impressive when looking out 8 to 10 days. And with 85% of instances seeing a new 50-day high within the next 2 weeks I'd say this past week's action seems to favor the bulls for the short-term. Below is an equity curve to see how the edge has played out over time.



While mostly up the curve is a bit choppy. Of the 5 losses, two of them were fairly large. This suggests perhaps a little more risk in this setup than in some others we examine. Over the 3-day period the average run-up was 1.1% and the average drawdown was 0.8%. That is a comparatively large drawdown. It isn't very surprising though. Risks tend to be higher when you are trading near the upper end of a range. And a tight consolidation near a 50-day high seems to qualify. All considered, I still find this study appealing and believe it is worth considering over both very short and intermediate-term timeframes. I considered not including it because the concept was somewhat similar to last night's Offset HV study, but upon close examination I found that there were zero overlapping instances. So I decided to include it.

The VIX also provided some notable action on Tuesday as it spiked over 8% while SPX finished down slightly and SPY closed up a few pennies. It's fairly remarkable to see such a large spike in the VIX on a day where the SPY failed to decline. The study below was last seen in the 1/18/12 letter. It looked at non-Mondays that saw the VIX spike up > 6% despite the SPY also rising. I have updated the results table below.

VIX closes up over 6% while SPY closes positive. Today is not Monday.
Buy SPY 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
5	19,062.61	16	14	2	87.50	1,435.26	4,501.60	-515.48	-810.06	2.78	19.49	1,191.41
4	19,816.75	16	14	2	87.50	1,469.25	4,225.18	-376.36	-446.12	3.90	27.33	1,238.55
3	17,144.31	16	15	1	93.75	1,149.09	4,576.06	-91.98	-91.98	12.49	187.39	1,071.52
2	11,112.97	17	13	4	76.47	1,017.13	2,807.04	-527.43	-790.40	1.93	6.27	653.70
1	4,158.24	18	11	7	61.11	656.12	1,893.29	-437.02	-1,546.98	1.50	2.36	231.01

100% of instances closed above the entry price at some point in the next week.

The edge here appears to be strong. Below is a list of all the instances along with their 3-day results.

VIX closes up over 6% while SPY closes positive. Today is not Monday.
Buy SPY on close. Sell 3 days later. \$100k/trade. 1993 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
03/31/94	Buy	\$44.60	0.47%	\$695.02
04/06/94	Sell	\$44.81		(\$2,802.50)
10/12/94	Buy	\$46.69	0.56%	\$1,370.24
10/17/94	Sell	\$46.95		\$0.00
11/23/94	Buy	\$45.25	0.91%	\$1,104.50
11/29/94	Sell	\$45.66		\$0.00
01/03/95	Buy	\$45.79	0.59%	\$1,004.18
01/06/95	Sell	\$46.06		(\$87.32)
05/04/95	Buy	\$52.25	0.54%	\$1,147.80
05/09/95	Sell	\$52.53		(\$325.21)
05/31/95	Buy	\$53.05	1.56%	\$1,903.85
06/05/95	Sell	\$53.88		\$0.00
12/05/95	Buy	\$62.14	0.05%	\$643.60
12/08/95	Sell	\$62.17		(\$579.24)
12/22/95	Buy	\$61.21	0.34%	\$751.18
12/28/95	Sell	\$61.42		\$0.00
02/06/96	Buy	\$64.77	1.65%	\$2,484.23
02/09/96	Sell	\$65.84		(\$108.01)
03/19/96	Buy	\$65.23	(0.09%)	\$475.23
03/22/96	Sell	\$65.17		(\$889.14)
09/03/96	Buy	\$65.75	0.29%	\$1,520.00
09/06/96	Sell	\$65.94		(\$1,109.60)
05/27/97	Buy	\$85.13	0.18%	\$504.82
05/30/97	Sell	\$85.28		(\$2,348.00)
03/17/00	Buy	\$146.94	2.14%	\$2,652.00
03/22/00	Sell	\$150.09		(\$1,659.20)
10/26/00	Buy	\$136.69	4.58%	\$5,117.00
10/31/00	Sell	\$142.95		(\$43.86)
06/16/11	Buy	\$127.30	1.69%	\$1,884.00
06/21/11	Sell	\$129.45		(\$565.20)
01/17/12	Buy	\$129.34	1.70%	\$2,017.53
01/20/12	Sell	\$131.54		(\$200.98)

Results appear very strong. The average run-up here (1.6%) was more than twice the average drawdown (-0.7%). Additionally, the only losing instance 3 days later was down less than 0.1%. I've also included this study on the Active List.

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



Tonight's studies put the green Aggregator Line more clearly above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is still a very small amount below 0. This means the SPX is mildly overbought versus recent expectations. So net expectations are bullish but the SPX is a little overbought. This is considered a neutral configuration. Bearish configurations are visible on the chart whenever both lines close below 0. This left the Aggregator System signal neutral.

Based on the current studies expectations will remain positive on Wednesday. This is unlikely to change unless we see a strong move higher and compelling bearish evidence. The Differential Pivot will be *slightly inverted* at 1,404.42 on Wednesday. An inverted pivot means the Differential line will move through 0 if the SPX closes flat. In this case it would take a rise of half a point or more in order to keep the overbought reading in place. So any down close would leave the SPX oversold and just about any up close would result in an overbought reading.

The Aggregator remains neutral and I remain patient. We could get a long trigger if the SPX declines on Wednesday. If that happens I'll evaluate it tomorrow night and then consider entry on Thursday if I feel compelled by what I'm seeing.

Intermediate-term Outlook (2 weeks – 2 months)– updated 8/13– slightly bullish

The intermediate-term outlook was last updated in the 8/13 letter. A link is below:

[2012-08-13 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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