

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 9, 2012

Volume 5 Issue 216

Market Overview



Signals Overview

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

Tonight's Research Points

- More strong selling failed to generate much fear as measured by the VIX. This suggests downside risk.
- A consistent indication of a bounce is the 2 weak breadth days we've just seen consecutively.

Short-term Outlook

The Bottom Line

Strong selling has the SPX as oversold versus expectation as it has been in months. The edge remains up, but evidence is still mixed and out classic panic measurements (VIX & CBI) are not showing signs of extreme worry..

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
November 9, 2012	SPX < Bollinger. VIX < 5% stretch	1-2 days	Bearish	
November 9, 2012	33% Up Issue% 2x < 200ma	1-2 days	Bullish	
November 8, 2012	20-low big drop high vol > 200	1-5 days	Bullish	
November 6, 2012	Double big reversal days > 200 < 10	1-4 days	Bullish	1.60%
Active - Long Term				
October 25, 2012	20-low > 200ma on a Fed Day	1-9 days	Bullish	
October 24, 2012	SPY dn 1% and SOX up	1-20 days	Bullish	
October 15, 2012	Breadth not diverging at top	int term	Bullish	
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
November 8, 2012	SPY unfill gap up then dn	1-2 days	Bearish	
November 8, 2012	7 high to 7 low	1-2 days	Bearish	

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

The Evidence

The post-election selloff continued on Thursday. The SPX fell another 1.2%, the Nasdaq dropped 1.4%, and the Russell 2000 lost 1.4%. Breadth was again strongly negative as the NYSE Up Issues % was 27% and the Up Volume % came in at 19%. Total NYSE volume declined from Wednesday's high level.

One interesting note about the day's action is that the SPX closed below its 200ma for the 1st time in over 100 trading days. I examined the drop through the 200ma a number of ways, and really found nothing substantial suggesting a short-term edge. There were some studies that triggered in the Quantifinder though. And like last night we saw studies with both bullish and bearish inclinations.

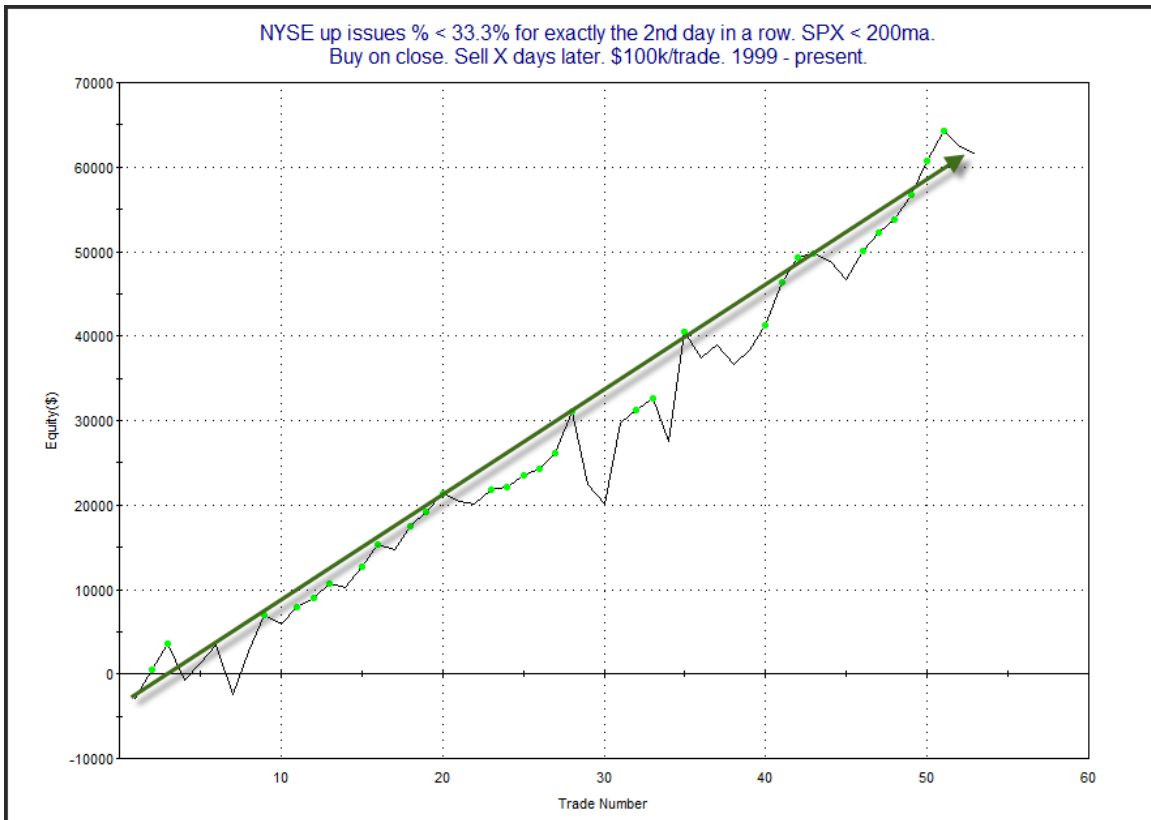
On the bullish side, Thursday was the 2nd day in a row of lopsided negative breadth and a close under the 200ma. I last showed it in the 12/14/11 letter. All stats are updated.

NYSE up issues % < 33.3% for exactly the 2nd day in a row. SPX < 200ma.
Buy on close. Sell X days later. \$100k/trade. 1999 - 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	67,099.46	47	34	13	72.34	3,163.89	8,609.40	-3,113.30	-9,314.08	1.02	2.66	1,427.65
4	40,033.75	50	30	20	60.00	3,143.24	8,810.76	-2,713.18	-6,869.52	1.16	1.74	800.68
3	49,495.50	53	32	21	60.38	3,573.20	13,853.40	-3,087.94	-11,502.27	1.16	1.76	933.88
2	61,576.43	53	36	17	67.92	2,924.22	13,116.84	-2,570.32	-8,631.00	1.14	2.41	1,161.82
1	42,027.19	53	34	19	64.15	2,004.42	10,716.03	-1,374.89	-6,633.36	1.46	2.61	792.97

50 of 53 instances (94%) closed above the entry price at some point in the next week.

For the considerable sample size and low number of criteria these results are astonishingly consistent. The stat at the bottom of the table is what seems most striking. Below is an equity curve using a 2-day exit.

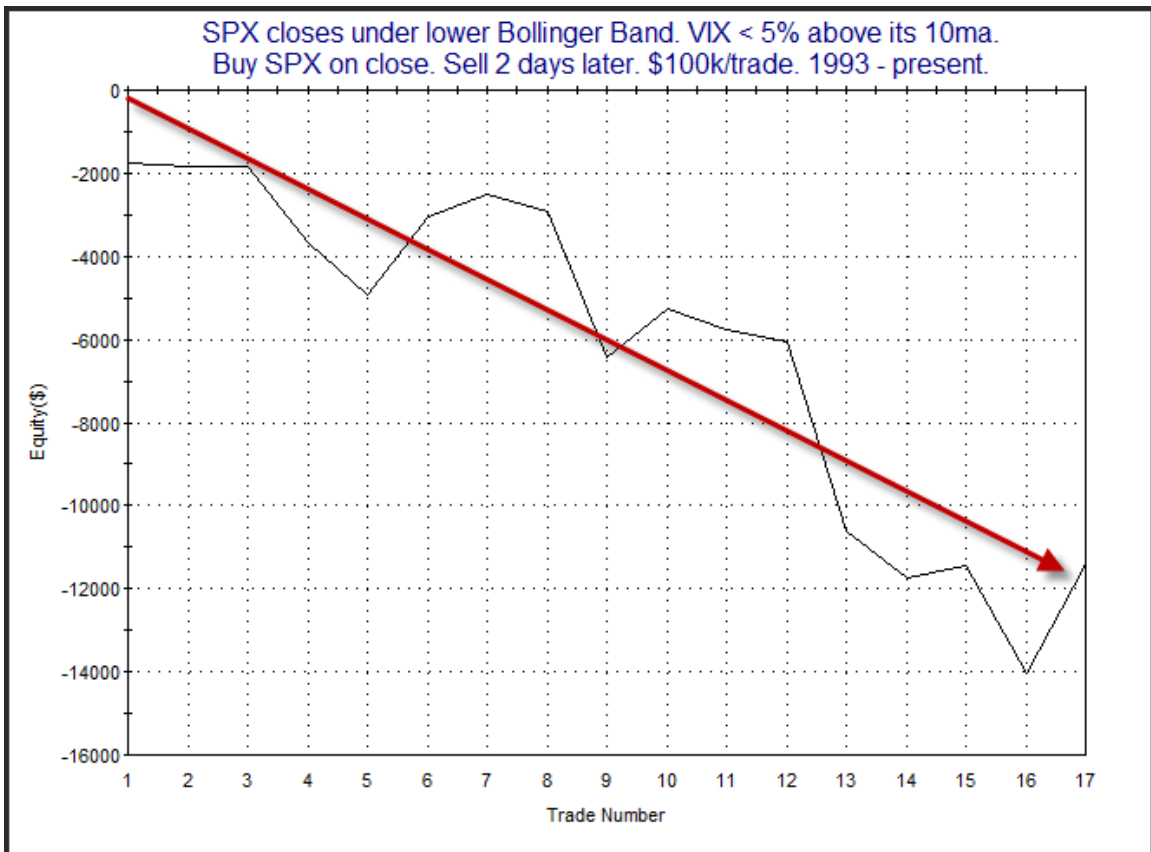


What's especially impressive about this study is that it has posted such consistently bullish returns despite the "downtrend" filter. That's fairly unusual to see.

So we have seen some evidence the last few days that the SPX is primed for a bounce. But one thing that is concerning is the lack of worry shown by the VIX. The study below addresses this. It was last seen in the 11/25/11 Letter. Results are updated.

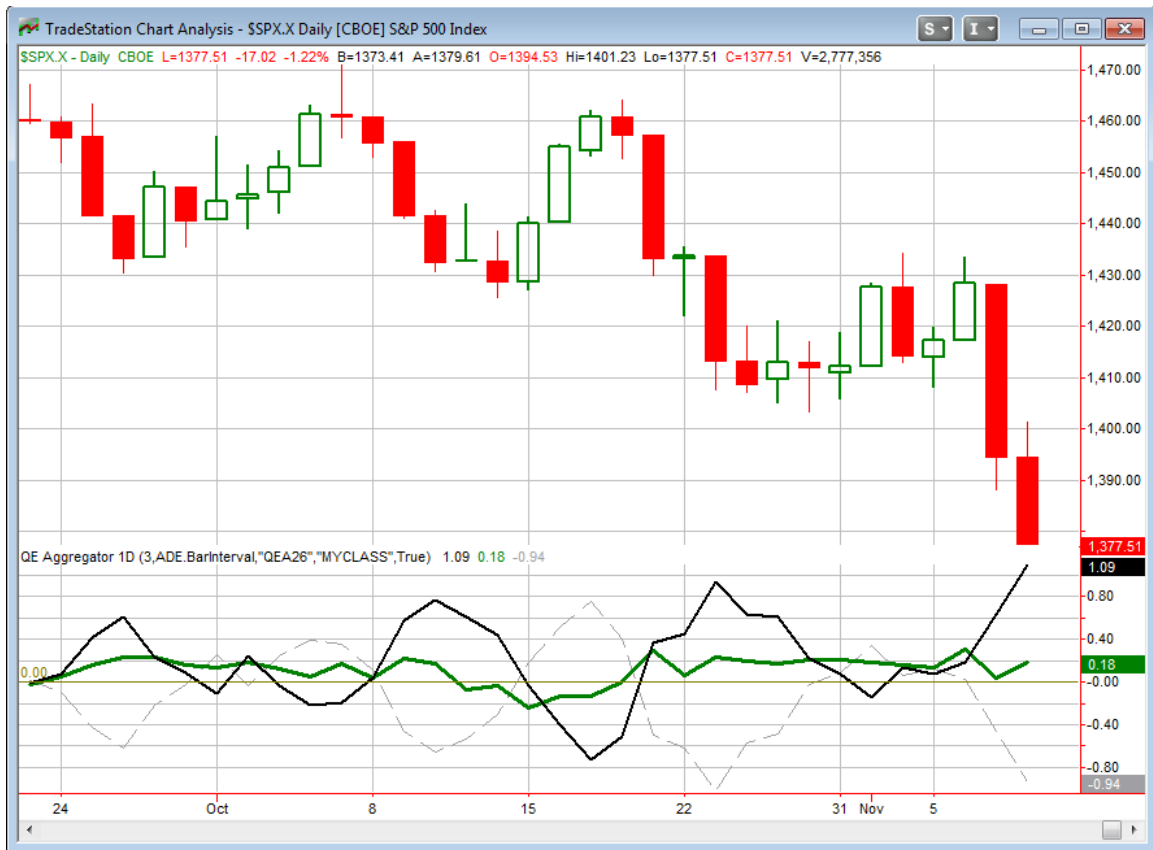
SPX closes under lower Bollinger Band. VIX < 5% above its 10ma. Buy SPX on close. Sell X days later. \$100k/trade. 1993 - present.													
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade	
5	-11,153.92	14	5	9	35.71	2,025.30	5,396.71	-2,364.49	-4,700.22	0.86	0.48	-796.71	
4	-8,891.92	14	5	9	35.71	1,663.96	3,291.12	-1,912.41	-4,256.00	0.87	0.48	-635.14	
3	-9,839.30	15	7	8	46.67	954.52	2,343.71	-2,065.11	-3,701.20	0.46	0.40	-655.95	
2	-11,387.92	17	6	11	35.29	1,082.96	2,645.36	-1,625.97	-4,558.08	0.67	0.36	-669.88	
1	-7,556.90	20	6	14	30.00	970.08	2,842.84	-955.53	-2,205.00	1.02	0.44	-377.84	

Numbers here appear to favor the bears. Below is a profit curve using a 2-day holding period.



So the mild VIX action is of some concern. While it isn't always necessary I typically like to see the VIX spiking to confirm an oversold condition is being washed out. Another indicator that I pay attention to when selling gets fierce is the CBI, which is still just at 2 (a neutral reading).

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



The green Aggregator line is well 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 as high as it has been in months. This means the SPX is strongly oversold versus recent expectations. So net expectations are bullish and the SPX is very oversold. 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.

Based on the current studies, expectations are set to remain bullish again on Friday. Of course this could change if more bearish evidence emerges. The Differential Pivot will

be 1,435.22 on Friday. This is over 4% above Thursday's close. I don't see that happening in just 1 day. It is going to take a multi-day rally or consolidation to work off this oversold condition.

So we have an extremely oversold market, and some pretty good signs that we are (over)due for a bounce. But the thing that is missing is panic confirmations from either the VIX or CBI. So there is a chance that things still could get worse before they get better. Though my entries were not very good, my index exposure is about where I would like it to be. So I am going to wait a night before taking on more index exposure. There was a Catapult that triggered (T) and I will look to take that in the Trade Ideas section down below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 11/5– bullish

The intermediate-term outlook was last updated in the 11/5 letter. Link below:

[2012-11-05 QE Subscriber Letter.pdf](#)

Catapult and Capitulative Breadth Statistics

Catapult & CBI Presentation Link

Open Catapult Triggers

ALL – 1/3 @ \$38.56 (bought @ limit)

New

T – 1/3 @ \$33.20 (buy at limit)

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 2(ALL, T)

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.

***T – buy 1/3 Catapult position @ \$33.20 LIMIT.** This is a Catapult trade idea.*

Those unfamiliar with the catapult trades are encouraged to review the Catapult and CBI video, which can be found on the [videos page](#). There is also a perma-link near the top of the catapult section above. Additional and more recent information can also be found in the "Catapult Exit Designer" presentation and tools, which are available for subscribers on the [downloads page](#). Bottom line with the Catapults is that while they have performed quite well as a whole over time, they can be very volatile and I rarely trade them with stops, so position sizing is critical for managing risk.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	10/22/2012	\$143.15	\$138.04	-3.57%		Aggregator
ALL(1/3)	11/5/2012	\$38.21	\$38.68	1.23%		Catapult
SPY(1/4)	11/8/2012	\$139.70	\$138.04	-1.19%		bought on open

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