

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 9, 2013

Volume 6 Issue 6

Market Overview



Signals Overview

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

Tonight's Research Points

- 2 unfilled down gaps under similar circumstances has commonly been followed by a bounce over the next few days.

Short-term Outlook

The Bottom Line

While the pullback is still shallow, I like the upside evidence and will look to begin scaling in to a long position.

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

| Study Date | Description | Time span | Bias | Avg Max Move |
|---------------------------|-----------------------------------|-----------------|----------------|--------------|
| Active | | | | |
| January 9, 2013 | 2 Unfilled SPY Gaps Dn & 5-low | 1-5 days | Bullish | 1.90% |
| January 7, 2013 | Up Issue % > 75% 2 of last 3 days | 1-6 days | Bullish | |
| January 3, 2013 | 50-day high breakout | 1-5 days | Bullish | |
| Active - Long Term | | | | |
| January 3, 2013 | 50-day high breakout. 90% up vol | 1-25 days | Bullish | |
| January 3, 2013 | VIX high stretch to low stretch | 1-8 days | Bullish | |
| January 3, 2013 | SPX & TNX high 50-day highs | 1-20 days | Bearish | |
| December 24, 2012 | Nasdaq Leading SPX | int term | 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 | | | | |
| January 7, 2013 | VXO 15% below 10ma 3 days | 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

Tuesday looked a lot like Monday with an unfilled gap down and mild selling. The SPX lost 0.3%, the Nasdaq fell 0.2%, and the Russell 2000 dropped 0.1%. Breadth was moderately negative as the NYSE Up Issues % was 49.6% and the Up Volume % came in at 37%. Volume rose a little from Monday.

One notable aspect of the price action over the last 2 days is that both Friday and Monday posted unfilled gaps down – never reaching breakeven at any point during the day. This triggered a few studies from the 12/26/12 Letter.

This first study looked at other instances where SPY left 2 unfilled down gaps while trading above the 200ma. I have updated it below.

| SPY leaves an unfilled gap down for the 2nd day in a row. It closes > 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 | |
| 5 | 23,181.21 | 22 | 18 | 4 | 81.82 | 1,741.16 | 3,940.02 | -2,039.94 | -3,627.12 | 0.85 | 3.84 | 1,053.69 | |
| 4 | 15,328.70 | 22 | 16 | 6 | 72.73 | 1,375.68 | 4,388.28 | -1,113.69 | -3,342.64 | 1.24 | 3.29 | 696.76 | |
| 3 | 7,743.21 | 22 | 14 | 8 | 63.64 | 1,153.53 | 3,325.14 | -1,050.78 | -2,747.01 | 1.10 | 1.92 | 351.96 | |
| 2 | 2,863.80 | 22 | 10 | 12 | 45.45 | 1,170.57 | 2,948.14 | -736.83 | -2,436.12 | 1.59 | 1.32 | 130.17 | |
| 1 | 978.92 | 22 | 11 | 11 | 50.00 | 838.74 | 1,974.15 | -749.75 | -1,849.26 | 1.12 | 1.12 | 44.50 | |
| 20 of 22 instances (91%) closed above the entry price at some point in the next week. | | | | | | | | | | | | | |

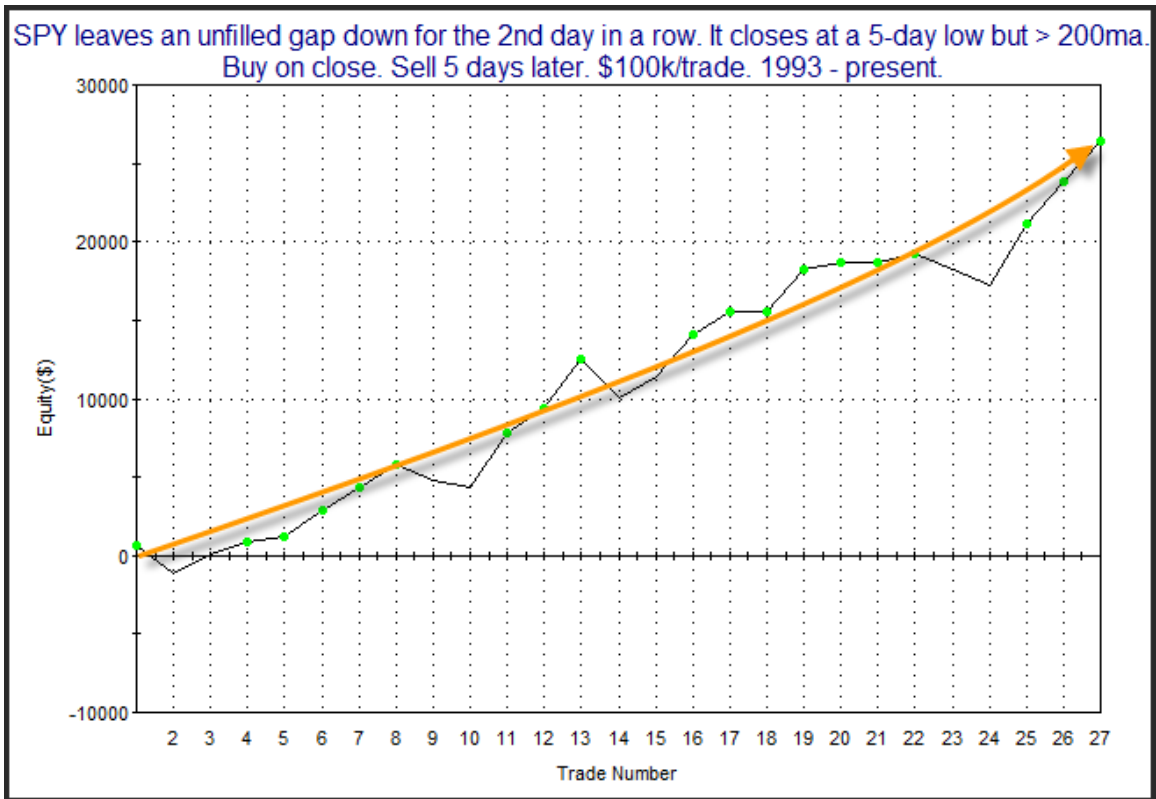
As you can see there has been a strong upside tendency to bounce over the next week. That tendency was not nearly as prominent prior to 1998, which is why the study does not look back further than that.

But if we also require a 5-day low close then we are talking about a setup that has suggested an upside edge since the inception of the SPY in 1993. I showed also this in the 12/26/12 letter and have updated the results below.

| SPY leaves an unfilled gap down for the 2nd day in a row. It closes at a 5-day low 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 |
| 5 | 26,433.67 | 27 | 21 | 6 | 77.78 | 1,632.60 | 3,940.02 | -1,308.48 | -2,465.95 | 1.25 | 4.37 | 979.02 |
| 4 | 20,038.58 | 27 | 20 | 7 | 74.07 | 1,350.66 | 4,388.28 | -996.38 | -1,920.60 | 1.36 | 3.87 | 742.17 |
| 3 | 13,149.90 | 27 | 18 | 9 | 66.67 | 1,145.16 | 3,325.14 | -829.22 | -1,645.38 | 1.38 | 2.76 | 487.03 |
| 2 | 5,992.46 | 27 | 16 | 11 | 59.26 | 998.29 | 2,948.14 | -907.29 | -2,436.12 | 1.10 | 1.60 | 221.94 |
| 1 | 205.25 | 28 | 15 | 13 | 53.57 | 692.47 | 1,974.15 | -783.21 | -1,849.26 | 0.88 | 1.02 | 7.33 |

Only 1 instance failed to close above the entry price at some point in the next 6 trading days. It triggered on 9/14/99.

Here again the numbers appear to suggest a strong tendency for a bounce in the next few days. This study also had impressive profit curves. Below is the profit curve assuming a 5-day holding period.



The steady upward slope acts as confirmation of the bullish edge. I have therefore included this study on the Active List

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



The green Aggregator line tonight remained 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 also in positive territory. The positive reading means the SPX is oversold versus recent expectations. So net expectations are positive and the SPX is 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 on Wednesday. This could change if compelling bearish evidence emerges. The Differential Pivot will be 1,468.64 on Wednesday. This is 0.8% above Tuesday's close. So it will take a close higher of at least this much in order for the SPX to move back into an overbought state.

The Aggregator is suggesting an upside edge, but like last night we are still looking at a very shallow pullback. But evidence is compelling enough that I am comfortable beginning to scale in to a long position with the intention of continuing to scale in if the pullback deepens. So Wednesday I will look to purchase 1 lot of SPY as detailed in the Trade Ideas section below.

Intermediate-term Outlook (2 weeks – 2 months)– updated 1/7– bullish

The intermediate-term outlook was last updated in the 1/7 letter. Link below:

[2013-01-07 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.

SPY - buy ¼ index position @ \$145.55 LIMIT. Based on the short-term outlook above. I will be looking to begin scaling long in SPY at a limit price of Tuesday's close.

Current Open Trade Ideas

None

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