

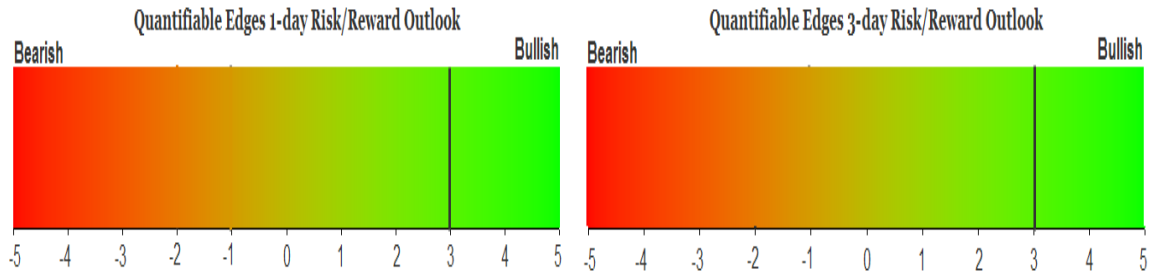
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

April 16, 2013

Volume 6 Issue 72

Market Overview



Signals Overview

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

Tonight's Research Points

- The big drop in SPX is suggesting a bounce.
- The large spike in the VIX also suggests a market bounce.

Short-term Outlook

The Bottom Line

A scary selloff on Monday appears to have set the market up for a bounce in the next few days. I am partially long and will add more exposure on Tuesday if more selling ensues.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
April 16, 2013	VIX > 25% above 10ma	1-2 days	Bullish	1.90%
April 16, 2013	2% drop. 10-low > 200. Close low in rng	1-3 days	Bullish	1.90%
April 15, 2013	April Opex / Tax Day bullsih	1-3 days	Bullish	1.90%
April 12, 2013	%b > 115 last 2 days	1-5 days	Bullish	1.80%
Active - Long Term				
January 14, 2013	Breadth Divergence (from Tops Study)	int term	Bearish	
September 17, 2012	QE3	int term	Bullish	
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.

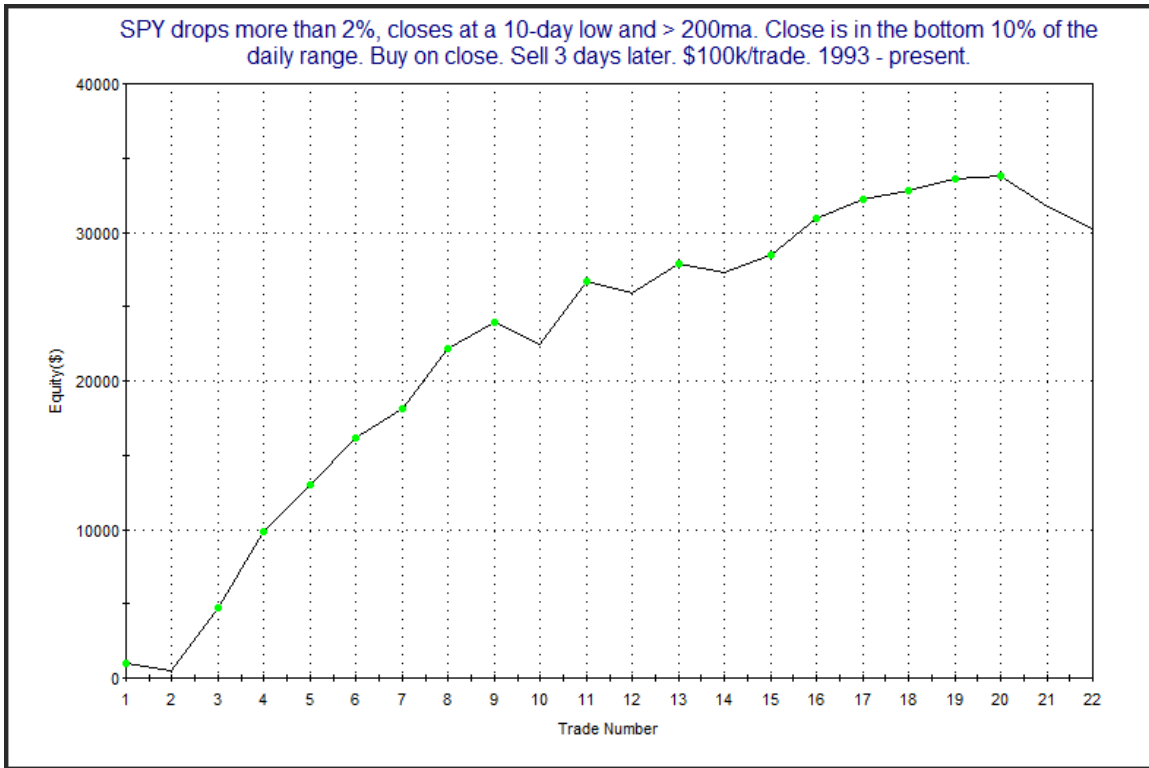
The Evidence

It was a terrible day in Boston and a bad one for the stock market as well. More about Boston lower down. The SPX declined 2.3%, the Nasdaq fell 2.4%, and the Russell 2000 lost 3.8%. Breadth was extremely negative as the NYSE Up Issues % was 12% and the Up Volume % came in at 8%. Total NYSE volume spiked to the highest level in weeks.

Several studies triggered in the Quantifinder today. They primarily looked at either large price drops or large VIX spikes. Below I have chosen two of the most compelling ones to highlight. This first study examines large drops in SPY, and was last seen in the 7/28/11 subscriber letter. I have updated all stats below.

SPY drops more than 2%, closes at a 10-day low and > 200ma. Close is in the bottom 10% of the daily range. 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	21,050.15	20	11	9	55.00	4,645.48	9,282.24	-3,338.90	-14,007.15	1.39	1.70	1,052.51
9	35,032.31	22	15	7	68.18	3,873.23	7,585.77	-3,295.17	-10,036.80	1.18	2.52	1,592.38
8	33,160.29	22	16	6	72.73	3,928.83	7,858.26	-4,950.17	-14,030.10	0.79	2.12	1,507.29
7	37,931.50	22	17	5	77.27	3,430.15	8,324.13	-4,076.21	-8,047.80	0.84	2.86	1,724.16
6	36,144.54	22	16	6	72.73	3,108.90	7,873.02	-2,266.32	-7,910.10	1.37	3.66	1,642.93
5	33,902.32	22	15	7	68.18	2,964.04	8,239.74	-1,508.32	-3,388.95	1.97	4.21	1,541.01
4	26,283.58	22	16	6	72.73	2,424.17	5,581.02	-2,083.86	-3,909.15	1.16	3.10	1,194.71
3	30,289.77	22	16	6	72.73	2,319.91	5,117.85	-1,138.12	-2,145.14	2.04	5.44	1,376.81
2	24,867.07	22	16	6	72.73	1,948.17	5,477.88	-1,050.60	-1,430.00	1.85	4.94	1,130.32
1	19,277.65	22	18	4	81.82	1,171.43	5,764.38	-452.02	-916.56	2.59	11.66	876.26

Results here certainly appear bullish. Much of the bullish tendency is realized in the first 1-3 days. Below is a profit curve examining 3-day performance.



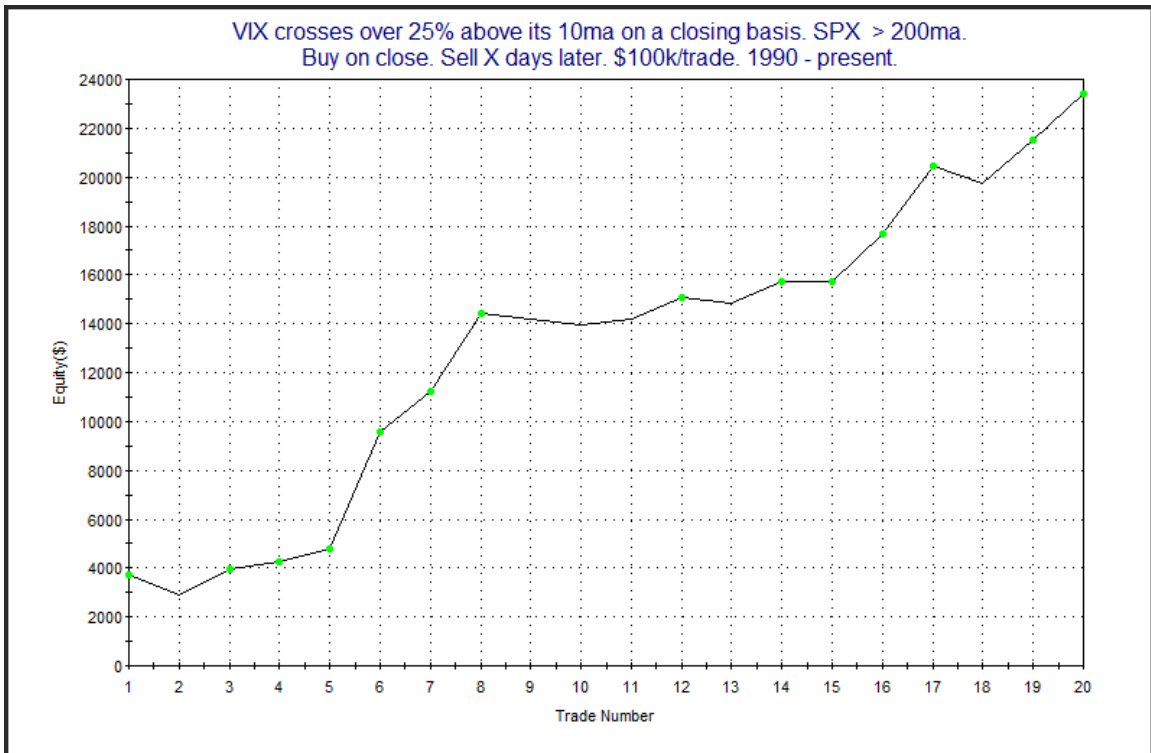
This curve looked a bit more enticing before the last couple of instances, but it still appears to suggest an upside edge, though perhaps not as strong as the numbers in the stats table suggest. I have included it on the active list, though with somewhat reduced expectations.

With terrorist attacks occurring not far from the trading close, fear spiked dramatically. The VIX closed up over 43%, and finished over 28% above its 10-day moving average. In the 8/1/11 subscriber letter I looked at other instances where the VIX crossed more than 25% above its 10-day moving average. Below are updated results.

VIX crosses over 25% above its 10ma on a closing basis. SPX > 200ma.
Buy on close. Sell X days later. \$100k/trade. 1990 - present.

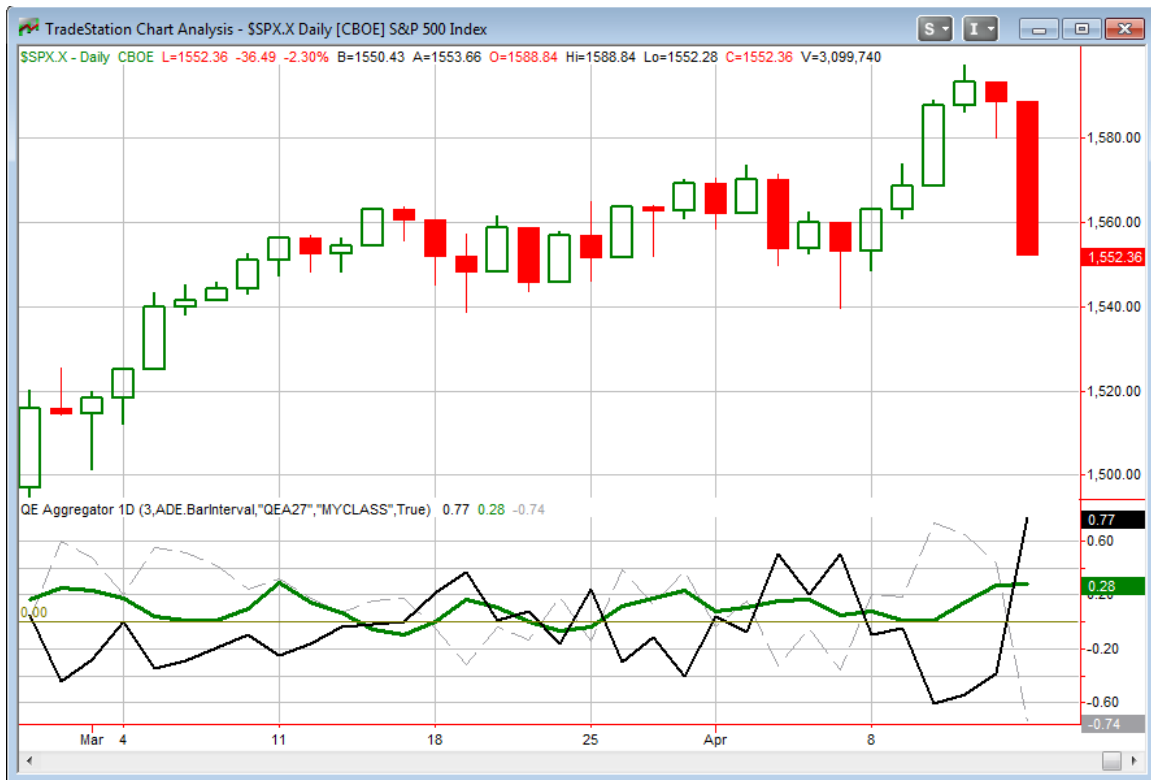
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	22,913.65	20	12	8	60.00	2,584.19	7,070.28	-1,012.08	-1,759.84	2.55	3.83	1,145.68
4	29,477.71	20	15	5	75.00	2,255.90	4,690.50	-872.16	-1,776.42	2.59	7.76	1,473.89
3	22,679.92	20	17	3	85.00	1,484.75	3,940.55	-853.62	-1,067.49	1.74	9.86	1,134.00
2	23,390.09	20	15	5	75.00	1,710.29	4,809.66	-452.86	-835.20	3.78	11.33	1,169.50
1	16,412.35	20	17	3	85.00	1,129.82	5,117.46	-931.53	-1,519.76	1.21	6.87	820.62

As you can see, such sharp reactions are often overreactions. SPX has done quite well in the first few days following similar big scares. Below is a profit curve assuming a 2-day holding strategy.



This curve appears quite encouraging, and I have also added this study to the short-term Active List.

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



Tonight's bullish studies helped push the green Aggregator Line further above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line spiked way up above 0. The positive Differential Line reading means the SPX is oversold versus recent expectations. So expectations are bullish 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 turn long at the close.

Without any bearish short-term active studies, expectations are slated to remain positive on Monday. Of course this could change if compelling bearish evidence emerges. The Differential Pivot will be 1,594.91 on Tuesday. This is a whopping 2.7% above Monday's close. It is unlikely we will see a rise of that much on Tuesday. A more likely scenario to work off the oversold condition would be a multi-day rally or consolidation.

Some long exposure was taken with the trade idea from last night. Personally, I did very little since I knew my mind was having trouble grasping the events near the close. It does appear that Monday's strong move down will likely be followed by a bounce at some point in the next few days. Should the market close lower again on Tuesday, I will look to add more long exposure near the close.

Personal Notes

As many subscribers are aware, I live and work near Boston. I am on vacation the next few days and was on the ski slope when I heard the news. My wife called me at about 3:25 PM. At the time I was about halfway down the mountain, skiing with my son, in shorts, on a beautiful, warm spring day. She told me that a bomb had gone off in Boston near the marathon and not much else was known. We were planning on that being our last run anyway, so we skied to the bottom and I got on the computer to try and figure out what was going on.

Patriots' Day in Boston really is a big deal. There is always a Red Sox game in the morning, schools and colleges are closed, and the entire city seems to be celebrating. I've never run a marathon, but I have spent many a Patriots' Day enjoying the festivities. The atmosphere is always incredible, especially when the weather is nice like it was today.

For those that have seen the coverage on TV of the explosion, the first one occurred right in front of a brick building with black glass windows. I worked in that building for two years after graduating college, and lived a few blocks from there at the time.

I had several e-mails to read through when I turned on my computer. A roommate of mine whom I lived with for six years during and after college was at the marathon today with his family. He left shortly before the explosions, but his wife and nine-year-old daughter were directly across the street and saw the whole thing happen. They quickly got out of there, and were not injured. Another friend of mine ran the marathon. He was already done and clear of the scene when the bombs went off. At this point, I do not believe I know anyone that was injured. My heart goes out to all those who were deeply affected by this tragedy.

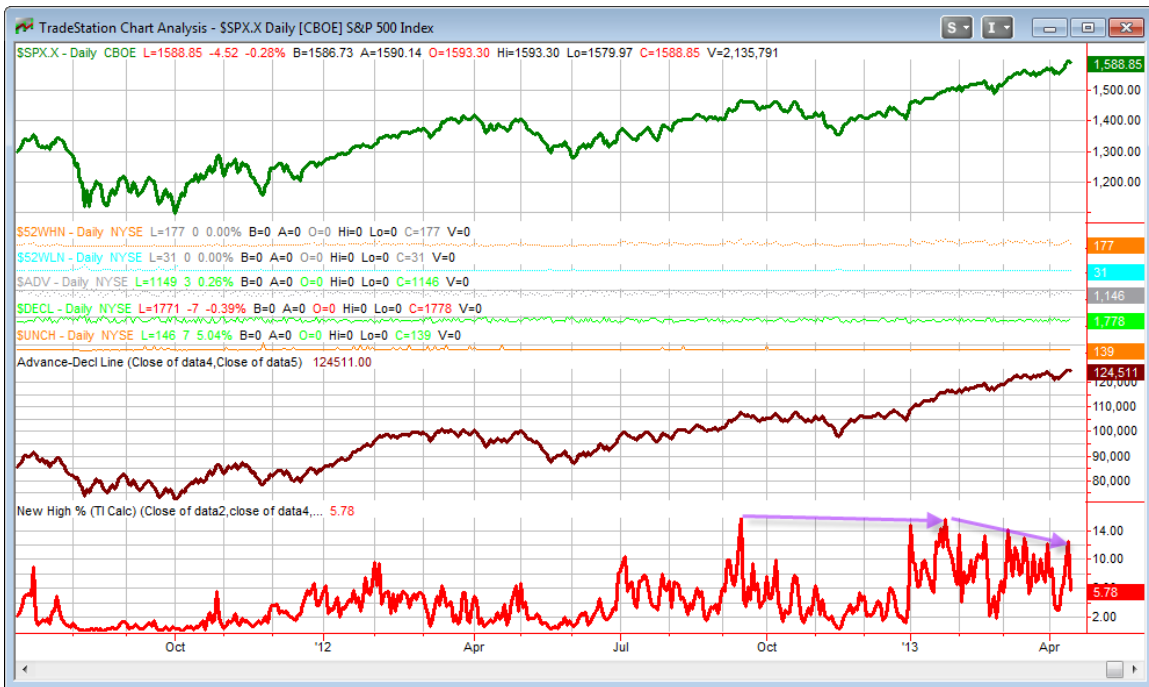
Lastly, below is a picture taken today. It is not of carnage or tragedy. My brother took it from the chairlift when he and my son spotted this mother bear and her cub crossing the ski slope below them.



Intermediate-term Outlook (2 weeks – 2 months)– updated 4/15 – somewhat bullish

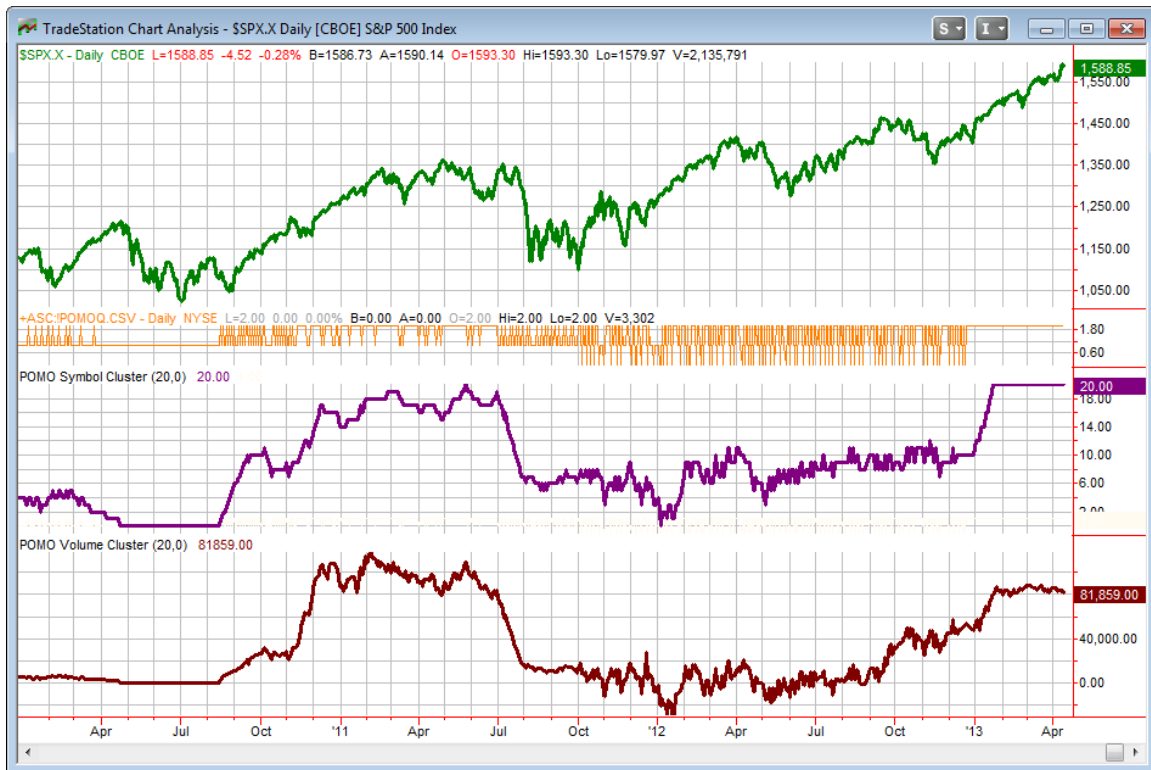
New all-time highs were again achieved on Tuesday, but by Friday the SPX put in a losing week. As mentioned above, SPX has reversed direction a record-tying 12 days in a row, so over the last couple of weeks neither the bulls nor the bears have exhibited clear control. And as a result, there has been a dearth of new intermediate-term studies triggering.

Since I updated the QE Study of Tops in January (it can be found on [members download page](#)) I have been keeping a close eye on the number of new highs being made on the NYSE. And while SPX again posted all-time highs, the number of individual issues hitting new highs remains in a divergence. The chart below is an updated version of the one I showed in the study. The indicator on the bottom shows the % of NYSE stocks that are making new 52-week highs. As you can clearly see that number has continued to shrink even while the SPX makes all-time highs. It is well below both the January level and the slightly higher September level of 15.73%. An expansion of new highs above there would greatly reduce the possibility of a major decline beginning in the next few months. For now the divergence raises a yellow flag.



I update the intermediate-term POMO/QE chart each week. For those not familiar, below is a brief description.

POMO stands for Permanent Open Market Operations and it is how the Fed has gone into the open market to buy securities over the last several years. The net effect of this buying is an influx of cash into the system. It appears a portion of that cash makes its way to the stock market and works as a bullish influence. A “POMO Day” is simply a day where these operations take place. The chart below shows a couple of indicators. The top pane is the S&P 500. The middle (purple) pane is the net rolling number of days in the last 20 that have been POMO days. In other words, a day the Fed buys on the market will add +1 while a day of selling will count as -1. The bottom pane is the total amount of money infused into (or taken out of) the system over the previous 20 days. Since the Sept 13, 2012 QE3 announcement the POMO numbers are also adjusted to reflected the Fed’s new approach of buying AMBS securities. Therefore, prior to that date the indicators just look at POMO, since that date it is a combination of POMO and AMBS flows.



The POMO/AMBS volume indicator remained elevated in its 2013 range again this week. And the days indicator is *still* maxed out at 20, which was a rarity during past QE implementations, but has been the norm so far this year. We estimate net inflows this past week to have been about \$16.8 billion. While that is a sizeable number, it is the smallest weekly number we have seen so far in 2013. So while it is likely bullish, it is less bullish than we have grown accustomed to.

This upcoming week we expect to see liquidity flows rise to a more typical level compared to what we have seen in recent months. Between POMO and AMBS we should see about a \$20.5 billion inflow.

There is sometimes a lag in the impact of the POMO flows. So while the market held up strongly last week despite the lower inflows, it still may be a little more susceptible than usual to a pullback in the next week or so.

Overall, intermediate-term evidence is still mixed. I have kept my overall outlook at “somewhat bullish” this week for the 2nd week in a row. On the negative side we are still cognizant of the breadth divergence from the Study of Tops. The trend is still up, but price action has failed to generate any new bullish intermediate-term studies in recent weeks. And while liquidity flows are positive, they are weaker than they have been in a few months. So we could be entering a period here where bulls may struggle some. I

still favor a rising market, and am more inclined to play long trades than shorts, but some caution may be warranted here for the next few weeks.

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 @ \$154.75 LIMIT ON CLOSE.** Based on the short-term outlook above, I will look to scale in further if SPX closes down some on Tuesday.*

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	4/15/2013	\$155.12	\$155.12	0.00%		bought on open

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