

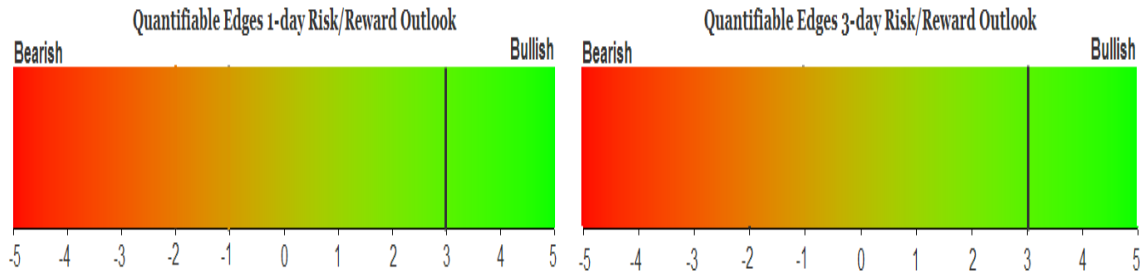
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

May 24, 2013

Volume 6 Issue 100

Market Overview



Signals Overview

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

Tonight's Research Points

- SPY has closed at a 5-day low for the 1st time in over 2 weeks. This suggests a short-term upside edge.
- The big gap down and partial reversal suggest more upside in the coming days.

Short-term Outlook

The Bottom Line

Expectations are getting more positive and SPX is getting more oversold. I am partially long and may take on more exposure if we see further selling on Friday.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
May 24, 2013	1st 5-low is > 10 days	1-4 days	Bullish	1.55%
May 24, 2013	Big gap down. Partial reversal.	1-2 days	Bullish	3.50%
May 23, 2013	Big drop from 50-day high	1-4 days	Bullish	1.20%
May 23, 2013	3-hi. 3-low. 3-low close. Close > 200.	1-5 days	Bullish	2.10%
May 23, 2013	Double Outside Day	1-5 days	Bullish	1.90%
May 17, 2013	SPX up 1%-2% opex week	1-5 days	Bearish	-1.40%
Active - Long Term				
May 23, 2013	3-hi. 3-low. 3-low close. Close > 200.	1-15 days	Bullish	4.10%
May 10, 2013	5 days up to 50-high, then 1 down	1-10 days	Bullish	2.00%
May 9, 2013	Breadth Confirms Rally (Study of Tops)	int term	Bullish	
May 6, 2013	Nasdaq leading SPX	int term	Bullish	
April 29, 2013	Sell in May unless Jan-April strong	1-6 months	Bullish	6.80%
April 29, 2013	6 months higher in a row	1-10 months	Bullish	14.30%
September 17, 2012	QE3	int term	Bullish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
May 21, 2013	SPX dn. Up Issue% > 55%.	1-2 days	Bullish	

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

The Evidence

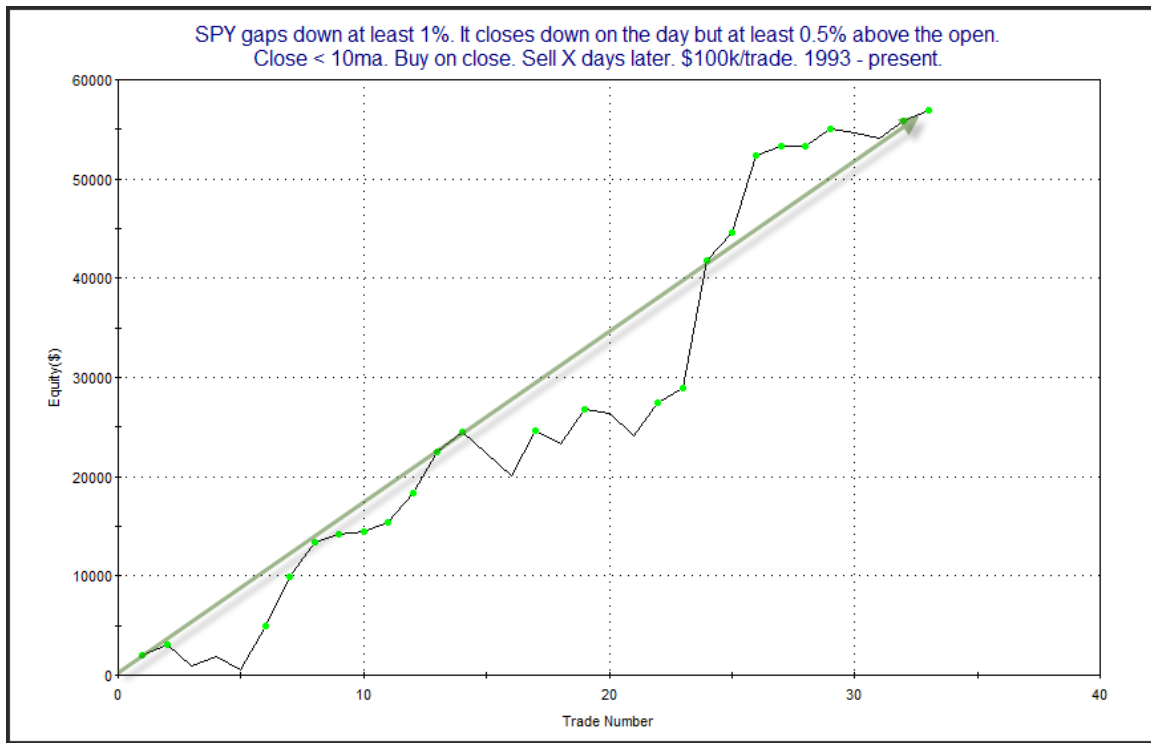
The day started off with a big gap down, but by the end the indices were mixed. SPX lost 0.3%, and the Nasdaq fell 0.1% while the Russell 2000 rose 0.2%. Breadth was negative as the NYSE Up Issues % was 40% and the Up Volume % was also 40%. Total NYSE volume sank from Wednesday's level.

There were a couple of interesting studies that appeared in the Quantifinder today. This first one was from the 8/2/10 Subscriber Letter. It looked at other times that a large gap down partially reversed but couldn't quite make it back to close at breakeven on the day. In that letter I found that when it has triggered with SPY closing above its 10ma then results were choppy, but closes below the 10ma showed strong results. I have updated the study below.

SPY gaps down at least 1%. It closes down on the day but at least 0.5% above the open. Close < 10ma. 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	43,031.43	31	19	12	61.29	3,728.40	11,238.92	-2,317.34	-6,614.24	1.61	2.55	1,388.11
4	45,616.14	32	20	12	62.50	3,396.14	10,630.48	-1,858.88	-6,725.16	1.83	3.04	1,425.50
3	33,762.79	33	21	12	63.64	2,594.37	6,933.92	-1,726.58	-5,355.22	1.50	2.63	1,023.11
2	56,886.16	33	24	9	72.73	2,911.50	12,814.15	-1,443.32	-2,251.30	2.02	5.38	1,723.82
1	37,425.04	33	21	12	63.64	2,636.57	14,507.65	-1,495.24	-3,576.07	1.76	3.09	1,134.09

88% of instances closed above the entry price at some point in the next 5 days.

Some powerful bounces occurred over the next few days. Below is an equity curve to see how this setup has played out over time.



A little choppy, but the persistently higher profit levels are impressive. This study certainly seems worth inclusion on the Active List.

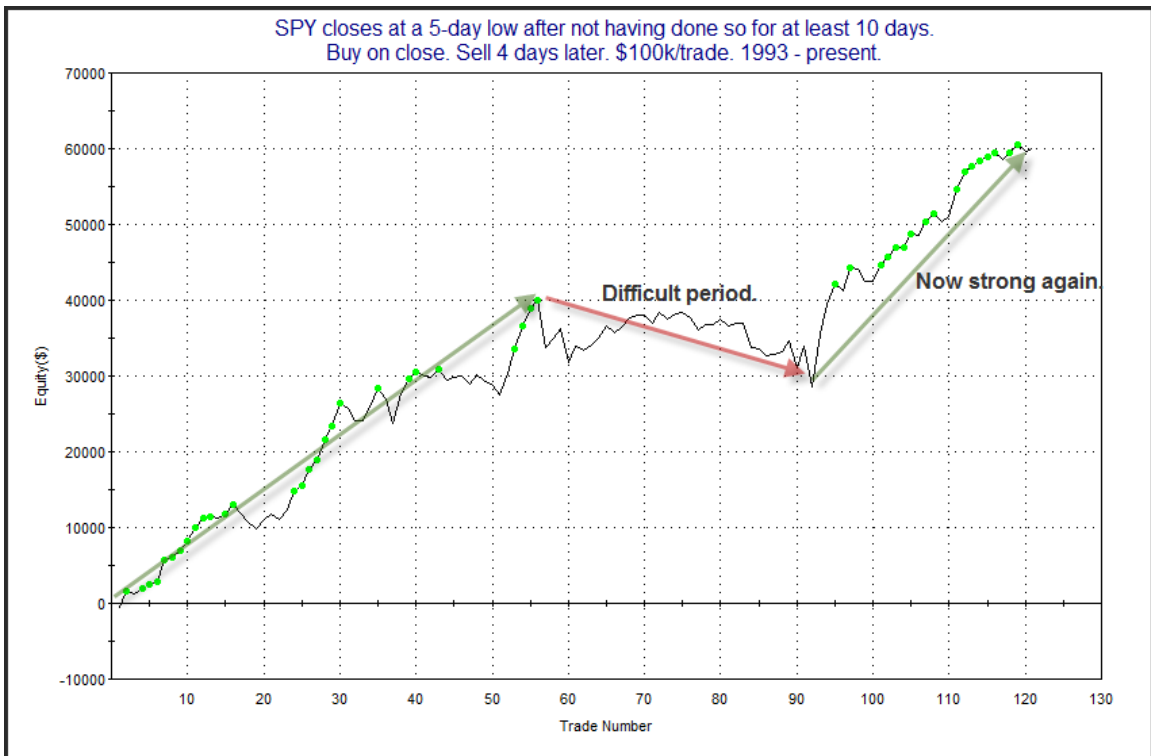
Thursday was the 1st time the SPY managed to close at a 5-day low in after a whopping 24 days without doing so. In the 8/24/12 subscriber letter I showed a study that examined results when the SPY closed at a 5-day low for the 1st time in over 2 weeks. I have updated that study below.

SPY closes at a 5-day low after not having done so for at least 10 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	100,367.63	121	82	39	67.77	2,143.28	8,925.10	-1,932.86	-8,623.54	1.11	2.33	829.48
9	86,561.84	121	82	39	67.77	1,940.81	8,933.76	-1,861.15	-6,709.56	1.04	2.19	715.39
8	80,100.61	121	81	39	66.94	1,871.80	8,908.38	-1,833.71	-7,113.48	1.02	2.12	661.99
7	63,881.07	121	80	41	66.12	1,785.28	8,851.52	-1,925.39	-7,790.40	0.93	1.81	527.94
6	52,817.56	121	78	43	64.46	1,630.86	6,523.92	-1,729.99	-9,559.44	0.94	1.71	436.51
5	49,763.69	121	76	44	62.81	1,559.27	6,103.89	-1,562.30	-4,906.44	1.00	1.72	411.27
4	60,009.77	121	80	41	66.12	1,424.39	6,941.43	-1,315.65	-6,244.56	1.08	2.11	495.95
3	36,311.34	121	74	47	61.16	1,291.94	5,888.16	-1,261.53	-5,295.84	1.02	1.61	300.09
2	23,621.61	121	67	53	55.37	1,111.86	3,809.72	-959.87	-3,737.28	1.16	1.46	195.22
1	13,030.35	121	67	54	55.37	845.27	2,812.20	-807.46	-3,909.03	1.05	1.30	107.69

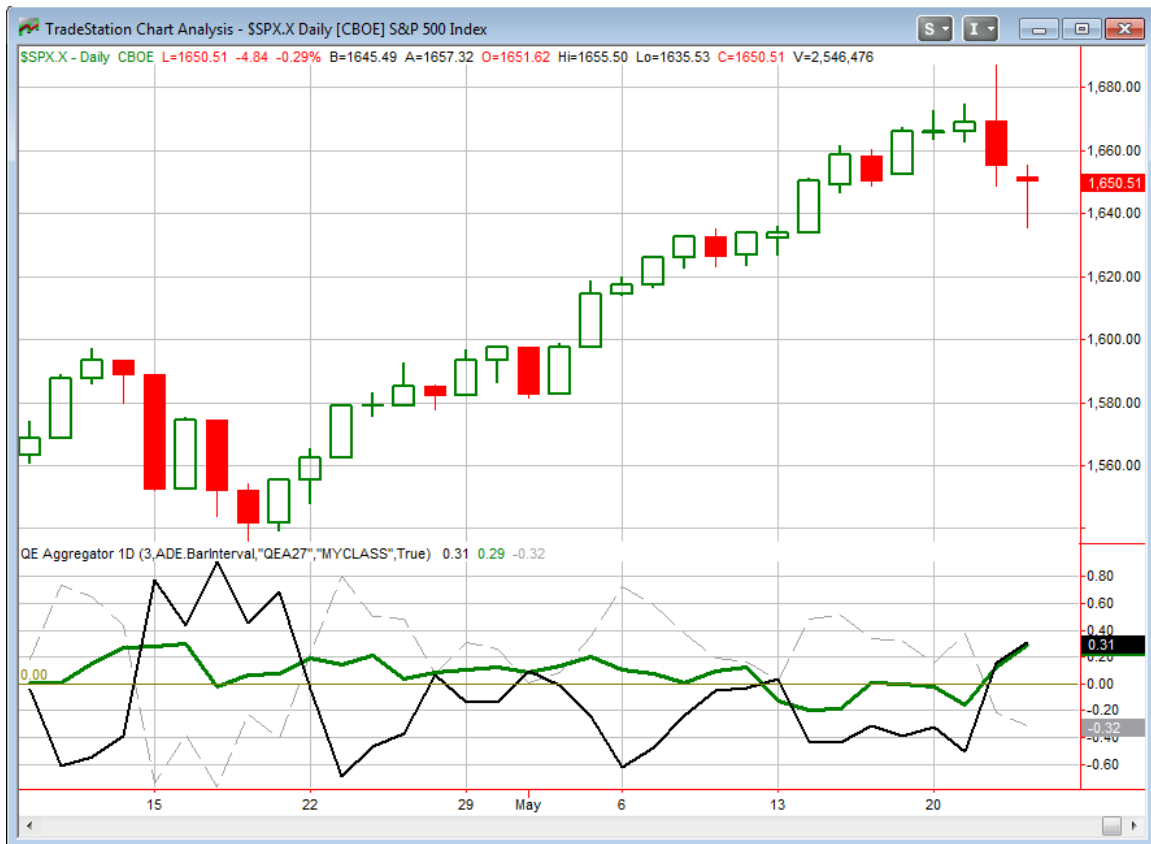
106 of 121 instances (88%) closed above the entry price at some point in the next 5 days.

Results here suggest a moderate upside edge. With the 4-day exit appearing to be compelling from a % Profitable, Avg Trade, and Profit Factor standpoint I ran an equity curve with it.



After showing a pretty consistent upside edge for nearly 60 instances, it chopped a bit. Over the last 30 trades or so the edge seems to have reasserted itself. Persistent uptrends normally wither before they die, rather than turn on a dime.

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



Tonight's studies helped keep the green Aggregator Line above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line also shot above 0. The positive Differential Line reading means the SPX is oversold versus recent expectations. So 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 slated to remain positive on Friday. Of course this could change if strong new bearish evidence emerges. The Differential Pivot will be 1666.03 on Friday. This is about 0.9% above Thursday's close. So SPX will

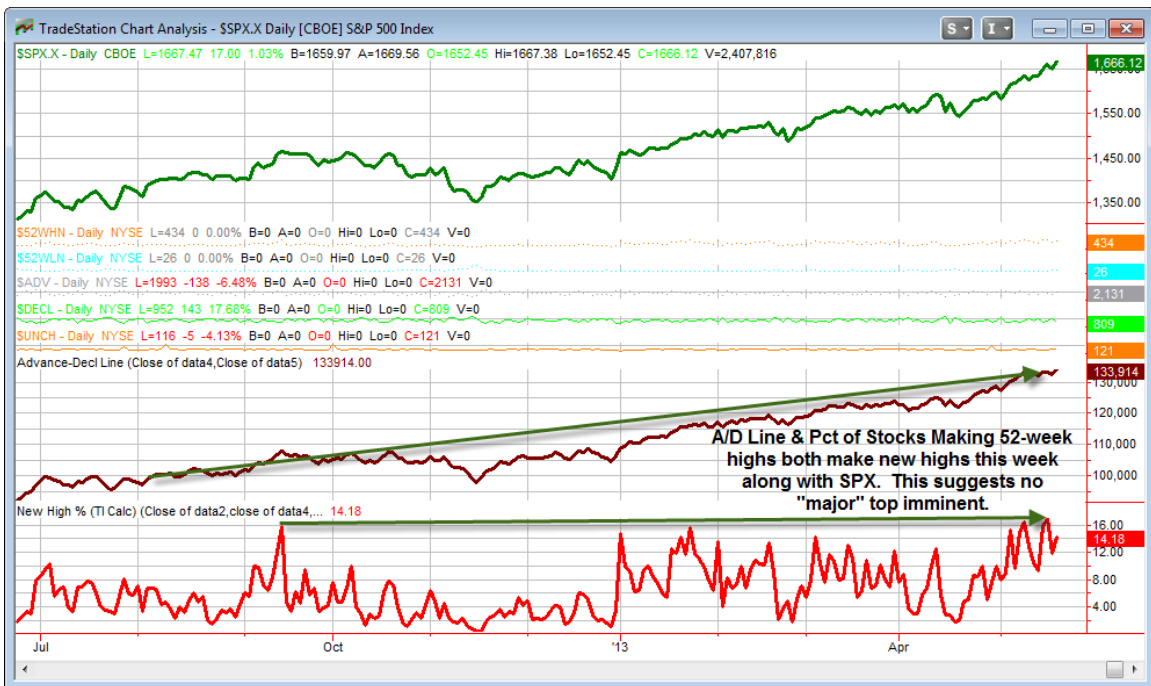
need to close up at least this much in order for it to move from oversold to overbought versus expectations.

I took some long exposure on Thursday, and with evidence continuing to build, and SPX getting more oversold, I'm inclined to add to that long position on Friday if we sell down a bit more. Details are in the Trade Ideas section near the bottom of the letter.

Intermediate-term Outlook (2 weeks – 2 months)– updated 5/20 –bullish

The market put in another strong week, and is *again* at new highs, erasing any doubt of an uptrend. The persistent move higher has been impressive. And while no new intermediate-term studies emerged this week, the open ones continue to all favor a further rally.

One very positive sign was that a couple of breadth indicators we track again made new highs this week. Those were the NYSE Advance/Decline Line, and the percent of stocks hitting new 52-week highs. In the Quantifiable Edges Study of Tops (always available on the Downloads page for subscribers) I went through every major top since 1970. For purposes of that study I defined a “major top” as any top that was followed by a decline of at least 20%. I found that in every case, there was a divergence in % of NYSE issues hitting new 52 week highs, and that the divergence was in effect for at least 2 months before any market top. Here is an updated chart with that indicator.

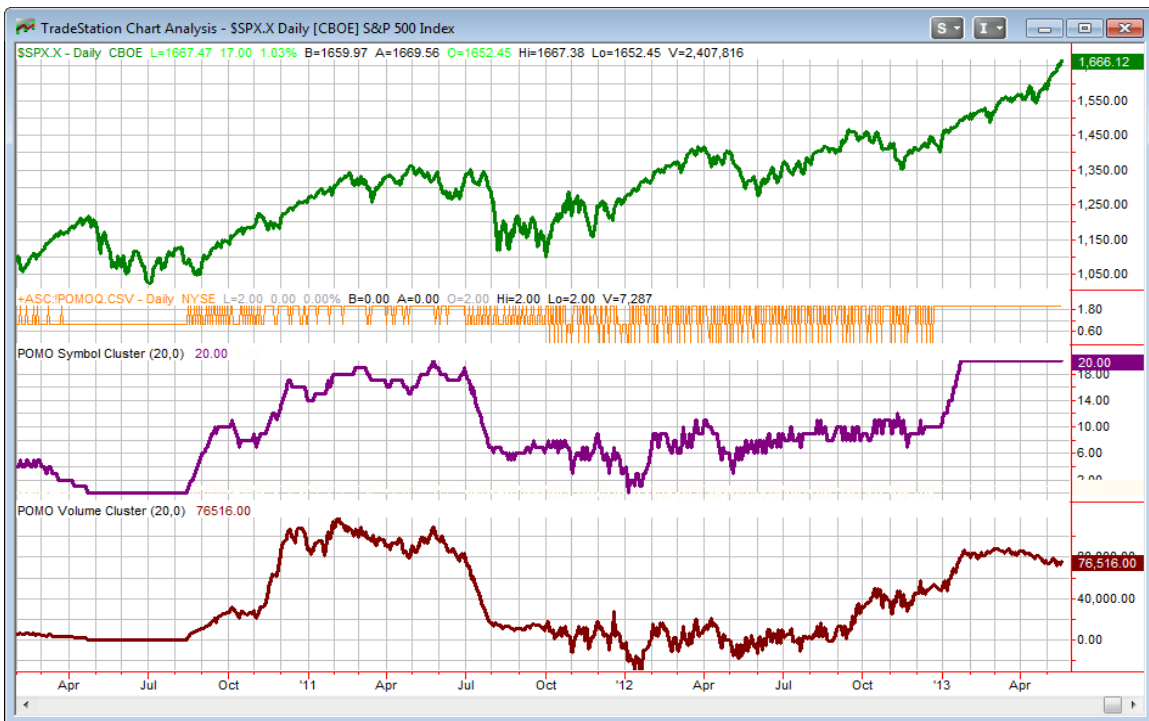


While the market is always capable of doing something new, Wednesday's high readings appear to greatly reduce the risk of a bear market beginning in the next 2 months. For a view of all tops since 1970, please refer to the Study of Tops. Here is a link for your convenience.

[QEStudyOfTops.pdf](#)

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 curled back up a little this week. 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 \$20.2 billion, which is an impressive amount. In the past, inflows of this magnitude have typically been bullish looking out over the next several days.

This upcoming week we expect to see liquidity flows of about \$18.6 billion. While lower, this should continue to keep the liquidity environment positive.

Bullish studies continue to dominate the intermediate-term. The leading Nasdaq, the “6 up months” study and the “Sell in May unless there hasn’t been a 5% pullback” studies all listed among the Active Studies at the top of this letter all support the bullish case. And of course, the factor I consider to be most important is liquidity flows. The Fed pump is still on. And as long as the Fed is pumping strongly it does not seem advisable to bet against the market. So my intermediate-term outlook remains bullish again this week. From a trading standpoint that generally means I will be more aggressive from the long side, and very conservative about shorting.

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 @ \\$164.25 LIMIT ON CLOSE.](#) Based on the short-term outlook above, I will look to scale in a bit more if SPY suffers a decent-sized down day on Friday.

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)	5/23/2013	\$165.45	\$165.45	0.00%		bought on close

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