

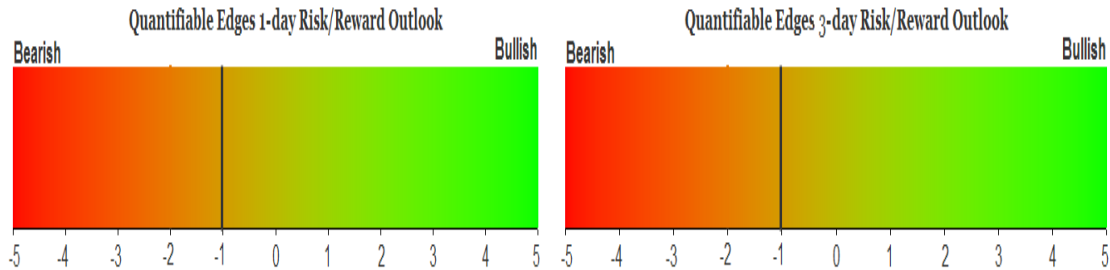
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 8, 2013

Volume 6 Issue 129

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Short	100% Short SPY	Flat	Flat

## Tonight's Research Points

- The unusual strength for both SPX and UUP (US dollar ETF) has been followed by short-term weakness in the past, but under vastly different circumstances.

### *Short-term Outlook*

#### *The Bottom Line*

The Aggregator is suggesting a bit of a downside edge. But the edge is small, and I am still not inclined to play the short side in this 2013 liquidity-driven environment.

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

Study Date	Description	Time span	Bias	Avg Max Move
<b>Active</b>				
July 5, 2013	SPX up. NYSE Up Issues < 40%	1-3 days	Bearish	-1.50%
July 1, 2013	Enf of month. SPX < 10ma & > 200ma.	1-5 days	Bullish	2.20%
<b>Active - Long Term</b>				
June 28, 2013	70% Advancing Issues 3 Days In Row	1-85 days	Bullish	10.60%
June 28, 2013	SPY up 3 days on lower volume	1-19 days	Bearish	-4.00%
June 4, 2013	Hindenburg Omen cluster	1-50 days	Bearish	-8.60%
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	

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

**The Evidence**

The market put in a strong price move on Friday and finished near its high. SPX and Nasdaq both rose 1.0%, while the Russell 2000 gained 1.4%. Breadth was just moderately positive though as the NYSE Up Issues % was 57% and the Up Volume % was 66%. Total NYSE volume was extremely light with many traders (like myself) taking the day off.

Quite a few studies triggered in the Quantifinder, but most of them were related to the low volume. When volume is low due to a holiday I do not find it is worth putting any faith into. So I won't be discussing any of them.

One interesting study that triggered is one that I have not seen since 2009, in the 8/10/09 letter. It looked at instances of both SPX and UUP (the dollar bullish ETF) rising more than 1% on the day. I have updated that study below.

SPX rises 1% while UUP (dollar bullish ETF) also rises 1%. Buy SPX on close. Sell X days later. \$100k/trade. 2008 - 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	-24,861.64	9	3	6	33.33	2,308.35	2,762.25	-5,297.78	-14,309.75	0.44	0.22	-2,762.40
9	-28,881.73	10	3	7	30.00	2,755.84	4,014.81	-5,307.04	-13,855.85	0.52	0.22	-2,888.17
8	-41,130.45	10	2	8	20.00	2,087.02	4,063.17	-5,663.06	-22,706.90	0.37	0.09	-4,113.05
7	-30,400.71	10	2	8	20.00	3,217.27	3,968.31	-4,604.41	-21,797.40	0.70	0.17	-3,040.07
6	-28,583.54	10	1	9	10.00	2,497.05	2,497.05	-3,453.40	-15,420.70	0.72	0.08	-2,858.35
5	-24,027.45	10	3	7	30.00	947.92	1,916.73	-3,838.74	-14,461.05	0.25	0.11	-2,402.74
4	-12,893.32	10	5	5	50.00	1,135.83	2,964.84	-3,714.49	-9,304.95	0.31	0.31	-1,289.33
3	-8,252.09	11	4	7	36.36	1,828.23	3,403.82	-2,223.57	-5,706.05	0.82	0.47	-750.19
2	-8,818.74	11	3	8	27.27	2,677.03	3,811.00	-2,106.23	-8,004.64	1.27	0.48	-801.70
1	-6,615.77	12	5	7	41.67	731.44	1,527.75	-1,467.56	-4,686.30	0.50	0.36	-551.31

Results here appear to be strongly bearish. I do have some concerns though. Let's first take a peek at the individual instances and then I'll discuss them.

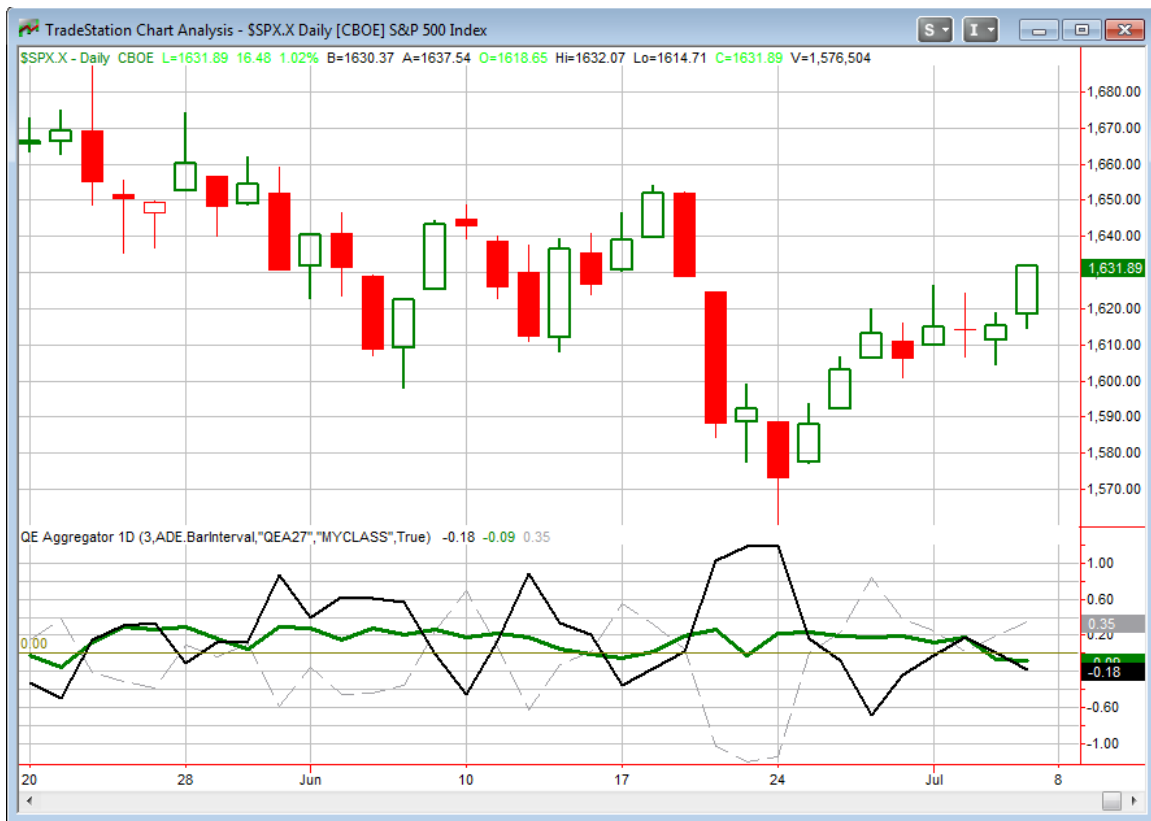
SPX rises 1% while UUP (dollar bullish ETF) also rises 1%. Buy SPX on close. Sell 6 days later. \$100k/trade. 2008 - present.				
Date/Time	Signal	Price	% Profit	Run-up Drawdown
03/18/08	Buy	\$1,330.71	(0.37%)	\$2,172.75
03/27/08	Sell	\$1,325.77		(\$2,661.75)
04/01/08	Buy	\$1,370.15	(1.14%)	\$1,194.48
04/09/08	Sell	\$1,354.49		(\$1,452.96)
08/08/08	Buy	\$1,296.31	(1.36%)	\$1,296.68
08/18/08	Sell	\$1,278.64		(\$1,678.60)
08/22/08	Buy	\$1,292.18	(1.13%)	\$836.22
09/02/08	Sell	\$1,277.56		(\$2,230.69)
09/16/08	Buy	\$1,213.57	(2.27%)	\$4,227.10
09/24/08	Sell	\$1,186.02		(\$6,565.74)
09/30/08	Buy	\$1,166.36	(15.55%)	\$56.95
10/08/08	Sell	\$984.94		(\$16,608.15)
10/31/08	Buy	\$968.75	(5.11%)	\$3,992.28
11/10/08	Sell	\$919.21		(\$7,108.03)
11/26/08	Buy	\$887.68	(1.31%)	\$959.84
12/05/08	Sell	\$876.07		(\$8,062.88)
08/07/09	Buy	\$1,010.48	(3.04%)	\$260.68
08/17/09	Sell	\$979.73		(\$3,133.06)
11/05/09	Buy	\$1,066.63	2.52%	\$3,602.82
11/13/09	Sell	\$1,093.48		(\$657.51)

As you can see, the consistency and magnitude of the moves have been impressive. But nearly all of them took place in 2008 (and none since 2009). During much of 2008 there was a strong positive correlation between SPX and UUP. Since then the correlation has more often been negative. And recently, there has been no strong correlation. Additionally, most of these instances came when SPX was below its 200ma – not when it was near new all-time highs.

I am of the belief that this study represented an environmental edge that was present during 2008. I am not convinced that the edge is still present in the very different environment we are currently in. So I have decided not to include this study on the Active List tonight, though I will still take an interest in tracking its results.

So despite the good number of studies that triggered in the Quantifinder, none of them were worthy of the Active List tonight. And while I am not including the SPX/UUP study as a factor in setting my trading bias, I still wanted to present it. Readers are certainly welcome to take evidence such as this into account for their own decision making if they find it more compelling than I do.

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

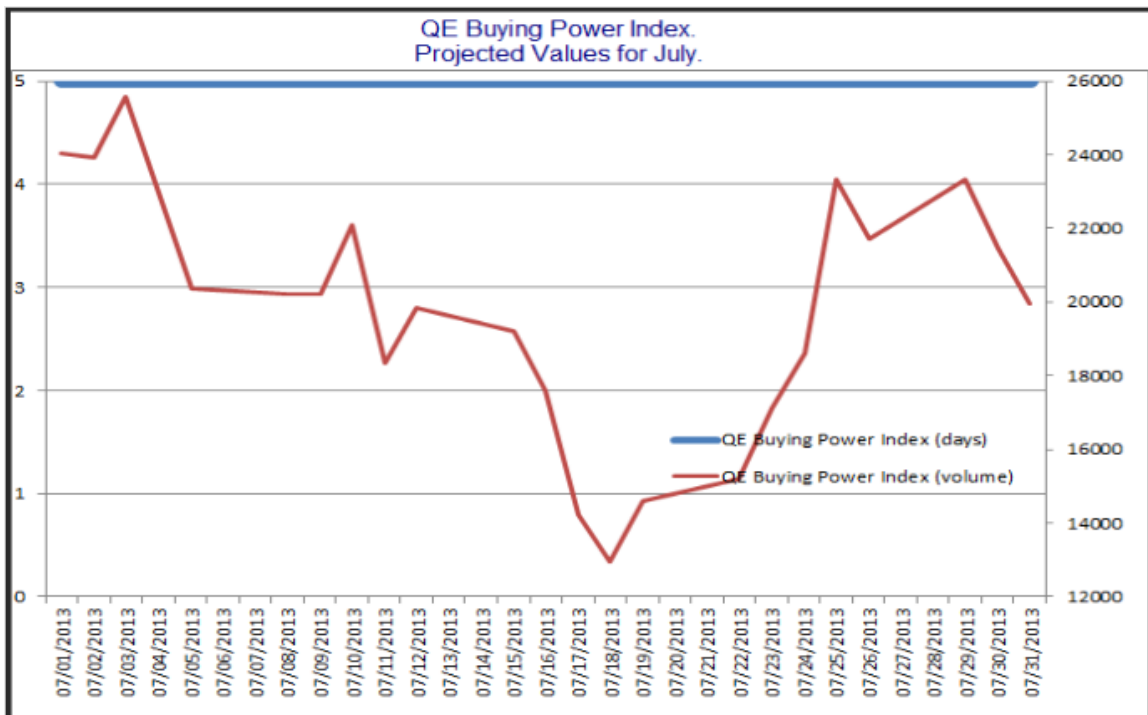


The green Aggregator Line again closed below zero. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line also remained below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are negative and SPX is overbought. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below 0. This caused the Aggregator system to remain short at the close.

Based on the current studies, expectations are slated to remain negative on Monday. Of course this could easily change if new bullish evidence emerges. The Differential Pivot will be 1,621.99 on Monday. This is about 0.6% below Friday's close. So it would take

a close lower of at least this much in order to move SPX from overbought to oversold versus expectations on Monday.

Since the new round of high-octane quantitative easing kicked in at the beginning of 2013, I have not been inclined to take any short trades. We will soon be entering a period where the positive liquidity stimulus will weaken. In fact, it will hit its weakest levels of 2013 (measured by the QE Buying Power Index) on 7/18/13. From now until then it will see a slow decline. This does not mean it will be a negative liquidity event, but it simply will not be as strong as it has been the rest of the year so far. Below is a copy of the projected July values from the QE Buying Power Index page.



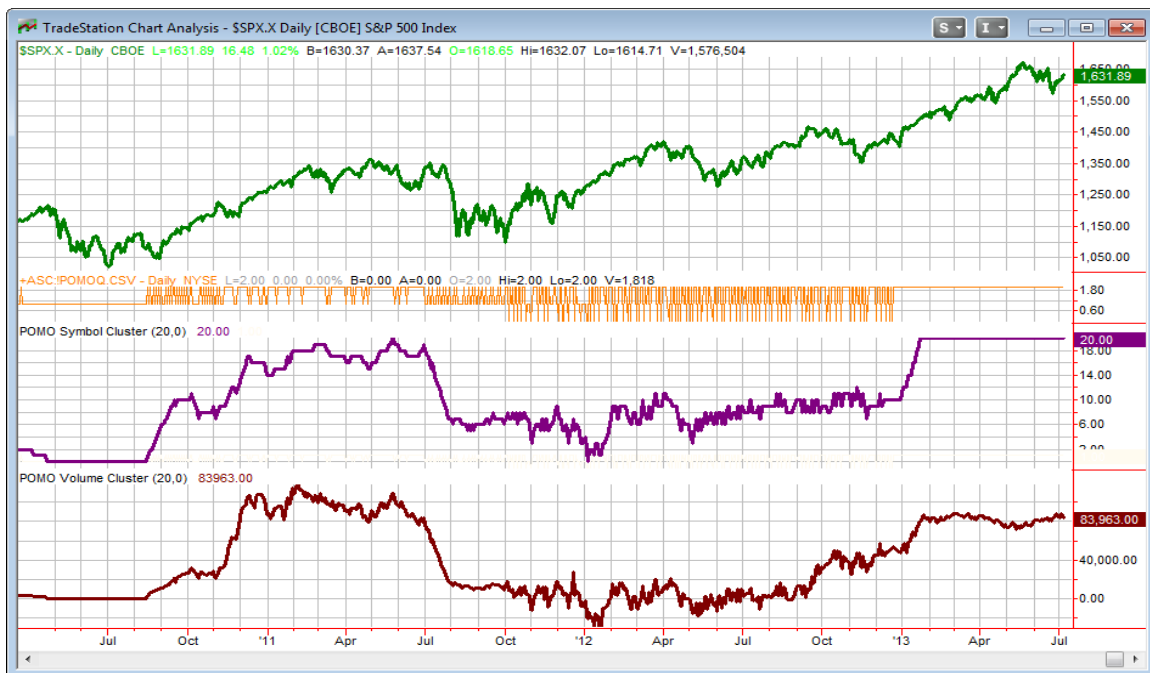
So this upcoming week liquidity will still be fairly strong. And though the Aggregator is showing a bearish indication, there is still just the one short-term bearish study. For me to consider a short, I would need more compelling studies. And I would also wait until we get closer to the 18<sup>th</sup>. At that time I may consider an outright short. For now, I would only use this Aggregator signal to possibly lighten up on existing longs or hedge against them.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 7/8 – somewhat bullish***

There was not a lot of volume this past week, but the market still managed to make its way nicely higher. It was the 2<sup>nd</sup> week in a row that it closed higher, and the SPX now stands just a little more than 3% below its May highs. As will often happen during light, holiday trading, nothing substantial emerged from an intermediate-term standpoint.

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 remains in its 2013 range. 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 \$17 billion, which isn't bad considering it was only a 4-day week.

This week is expected to see POMO and AMBS inflows of about \$19.8 billion. That is also a decent amount, and about average for 2013. But the following week is the one we will be looking out for, when inflows are expected to only reach about \$14.6 billion.

There is really no change in my outlook from last week. I am still leaning bullish. There seems to be more evidence pointing in that direction. Studies based on price action, breadth, and liquidity are all pointing higher. The bears can point to the Hindenburg Omen and the “SPY rise on declining volume” study from June 28th as hints to more downside. I am leaving the outlook at “somewhat bullish” again this week. From a trading standpoint that means I will be favoring longs and being extra selective about any shorts.

### **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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