

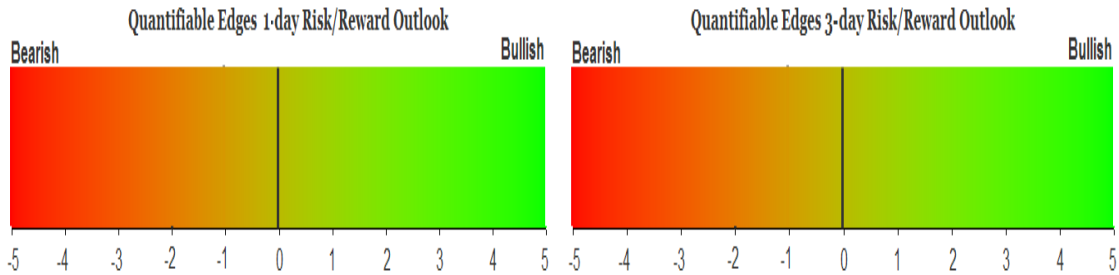
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 15, 2013

Volume 6 Issue 134

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing	NDX Trend Timer
Flat	50% Long XIV	Flat	Flat

## Tonight's Research Points

- SPY hitting 10-day highs after closing  $> 5ma$  for at least 10 straight days suggests extended condition likely to pull back.

## *Short-term Outlook*

### *The Bottom Line*

The Aggregator is still neutral. Expectations remain positive but the market is too strongly overbought for me to consider a short-term position. I continue to wait.

*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 15, 2013	10 closes > 5ma. Close 10-high	1-2 days	Bearish	
July 12, 2013	SPY breakaway gap	1-5 days	Bullish	1.65%
July 11, 2013	5 up > 200 but < 50-high	1-10 days	Bullish	
<b>Active - Long Term</b>				
July 11, 2013	5 up > 200 but < 50-high	1-15 days	Bullish	
July 10, 2013	RSI(2) crosses over 99. SPX > 200ma	1-15 days	Bullish	2.40%
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.

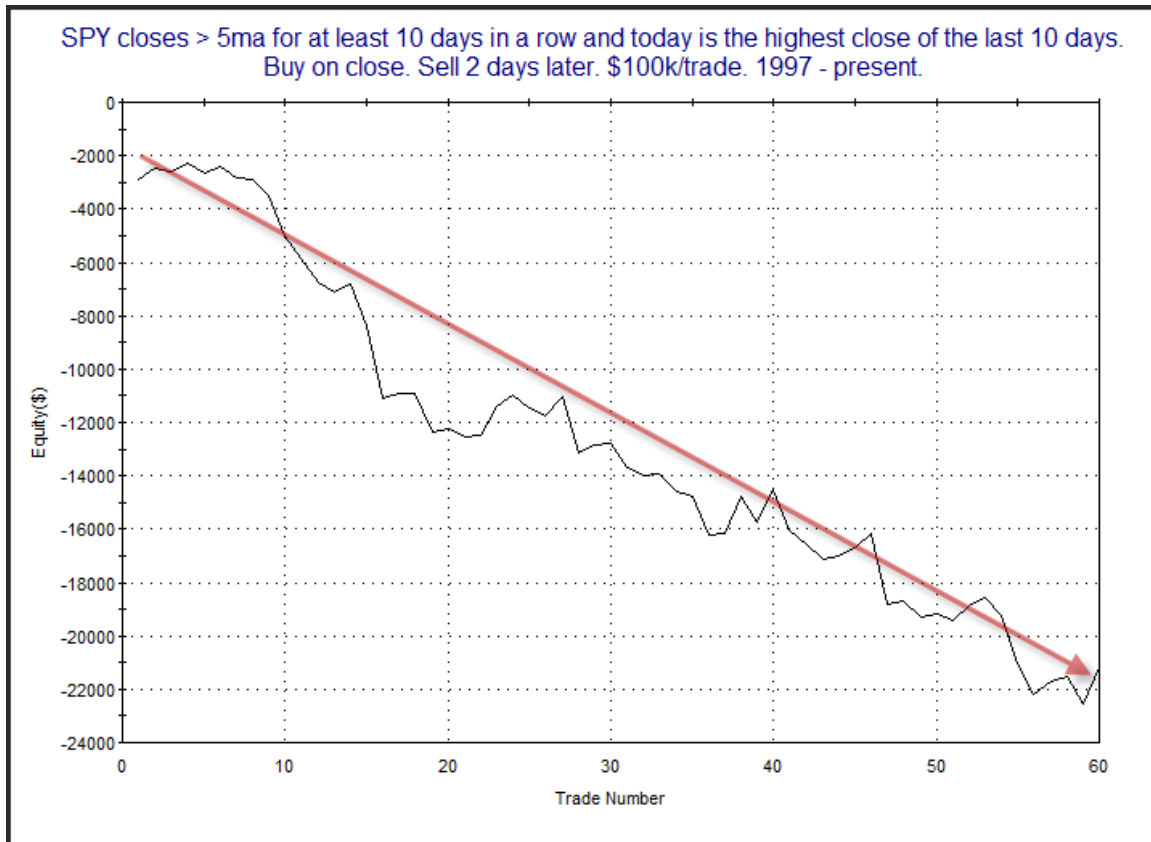
**The Evidence**

Trading was quiet on Friday, and for a good portion of the day it appeared that the market would close lower. But a late rally put it in positive territory once again. The SPX and Russell 2000 each rose 0.3%, while the Nasdaq climbed 0.6%. Breadth was near breakeven as the NYSE Up Issues % was 49% and the Up Volume % was also 49%. Total NYSE volume came in light.

SPY has now gone 12 days without closing below its 5ma. That's an unusually long period of time to hold above such a short-term moving average. The study below was last seen in just 2 days ago in the 7/11/13 subscriber letter. It looks at other instances in which the market has traded above the 5ma for at least 2 weeks and is now closing at a 10-day high. All results are updated.

SPY closes > 5ma for at least 10 days in a row and today is the highest close of the last 10 days. Buy on close. Sell X days later. \$100k/trade. 1997 - 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	-12,913.21	40	21	19	52.50	738.86	2,516.52	-1,496.28	-4,014.40	0.49	0.55	-322.83
4	-17,281.44	44	18	26	40.91	656.27	1,428.90	-1,119.01	-3,723.20	0.59	0.41	-392.76
3	-18,947.57	51	18	33	35.29	604.01	1,294.25	-903.63	-3,235.65	0.67	0.36	-371.52
2	-21,171.81	60	26	33	43.33	422.43	1,403.60	-974.39	-2,870.40	0.43	0.34	-352.86
1	-21,781.13	84	34	50	40.48	316.27	1,361.25	-650.68	-2,817.32	0.49	0.33	-259.30
<b>89% of instances closed below the entry price at some point in the next week.</b>												

In the past this setup has almost always been followed by a short-term pullback. The downside edge doesn't last long, though. It seems to pretty much play itself out over the first 2 days. Below is an equity curve showing how the edge has evolved over time. It uses a 2-day exit strategy.



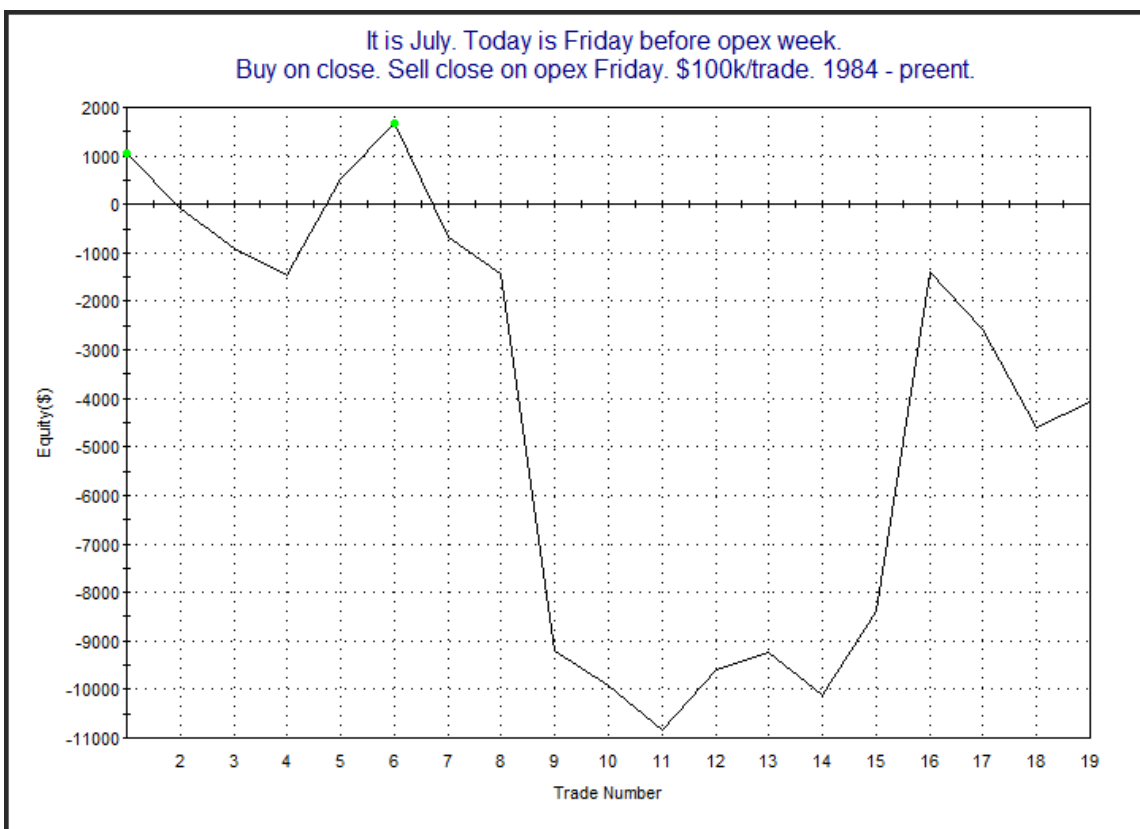
The last 2 days the market has continued higher, but the strong steady downslope seems to confirm the bearish edge.

This upcoming week is opex week. Opex week has typically been somewhat bullish. But some months have shown stronger seasonality than others. And of all the months, July has been the weakest. The table below is copied from the 3/11/13 letter. It shows opex weeks returns broken down by month. It has NOT been updated.

**Op-Ex Week Performance by Month. 1984 - present. \$100k/trade.  
(Excludes September 2001)**

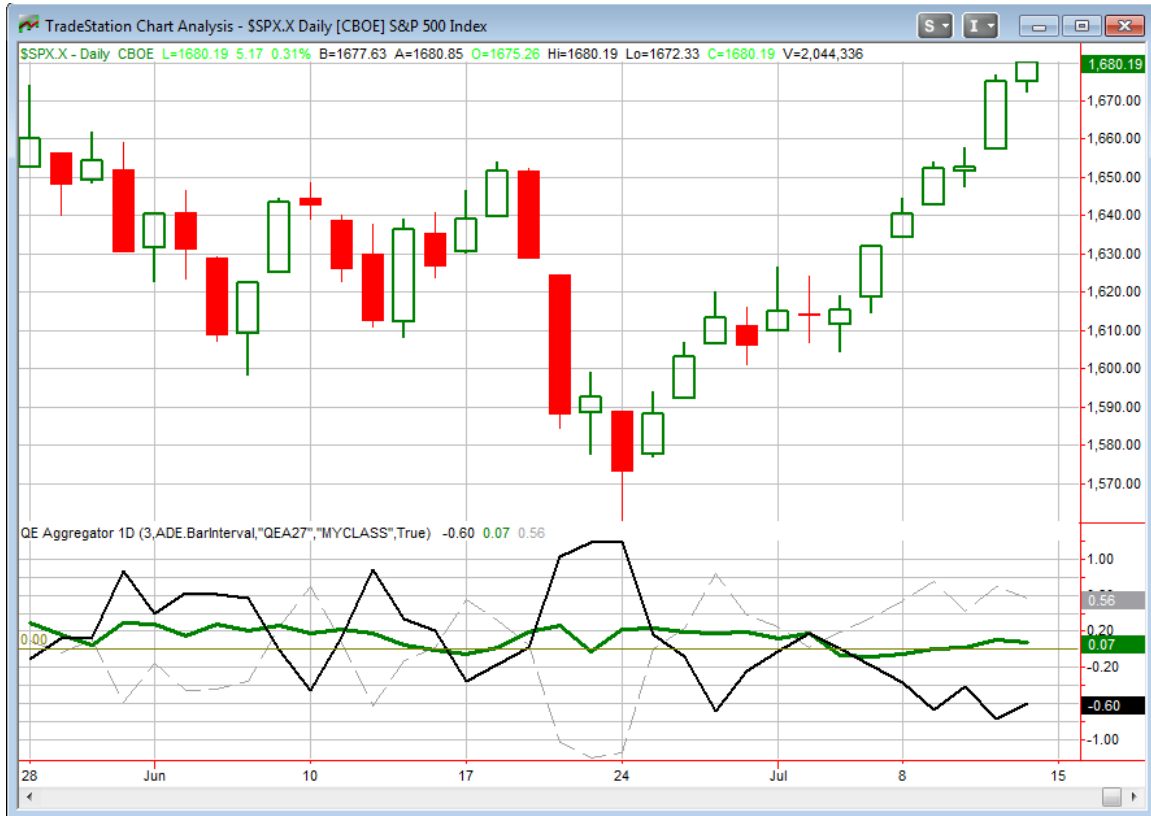
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
12	22,772.93	29	23	6	79.31	1,358.61	5,868.16	-1,412.53	-4,176.33	0.96	3.69	785.27
11	-828.54	29	17	12	58.62	1,355.92	3,718.25	-1,989.93	-8,351.64	0.68	0.97	-28.57
10	22,735.08	29	21	8	72.41	2,335.39	7,282.10	-3,288.50	-9,109.98	0.71	1.86	783.97
9	10,714.77	28	17	11	60.71	1,610.77	5,313.08	-1,515.30	-4,975.04	1.06	1.64	382.67
8	5,258.03	29	17	12	58.62	1,445.89	4,329.72	-1,610.18	-4,643.52	0.90	1.27	181.31
7	-4,108.73	29	13	15	44.83	1,531.20	6,921.25	-1,600.96	-7,953.12	0.96	0.83	-141.68
6	-879.88	29	16	13	55.17	1,257.62	3,786.09	-1,615.52	-3,998.19	0.78	0.96	-30.34
5	185.01	29	14	15	48.28	2,029.21	4,850.40	-1,881.60	-4,959.45	1.08	1.01	6.38
4	28,080.18	29	19	10	65.52	2,271.86	5,731.96	-1,508.53	-3,580.15	1.51	2.86	968.28
3	24,281.92	29	19	10	65.52	2,117.29	7,515.60	-1,594.66	-6,711.66	1.33	2.52	837.31
2	7,110.33	30	17	13	56.67	1,440.68	3,096.72	-1,337.02	-6,814.80	1.08	1.41	237.01
1	8,366.68	30	15	15	50.00	2,177.49	5,389.00	-1,619.71	-5,383.93	1.34	1.34	278.89

As you can see, July has been the weakest month for opex weeks. It is the only month with both more losing weeks and negative total returns. Below is a profit curve showing July opex week returns over the years.



Returns have been very inconsistent and don't suggest any kind of reliable edge.

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



Despite the bearish study tonight the green Aggregator Line remained above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is still well below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are positive but SPX is overbought. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. This caused the Aggregator system to stay flat at the close.

Based on the current active studies, expectations are set to remain bullish on Monday. The Differential Pivot will be 1,651.77 on Monday. That is 1.7% below Friday's close. So unless there is a very strong selloff Monday, SPX will remain overbought.

For me the story remains the same as it has the last few days. While the studies generally are leaning towards more upside, the market is so overbought that risk/reward is poor. So there is really nothing for me to do other than wait for a better risk/reward scenario.

I will also note that risk may be increased over the next several days because we are entering a period of low Fed-induced liquidity readings. The level of pumping expected this upcoming week is lower than any week so far in 2013. Of course, there is still pumping going on. And any pumping should provide some positive influence. But when the market is used to much higher levels, then the bullish impact may be very weak. So with the market overbought, extended on a times basis, and also without a strong liquidity wind at its back, we could see bears step up here a little bit. I'm not looking to short, but I expect we'll see a pullback fairly soon. And there is a decent chance it could provide another short-term buying opportunity.

***Intermediate-term Outlook (2 weeks – 2 months)– updated 7/15 – somewhat bullish***

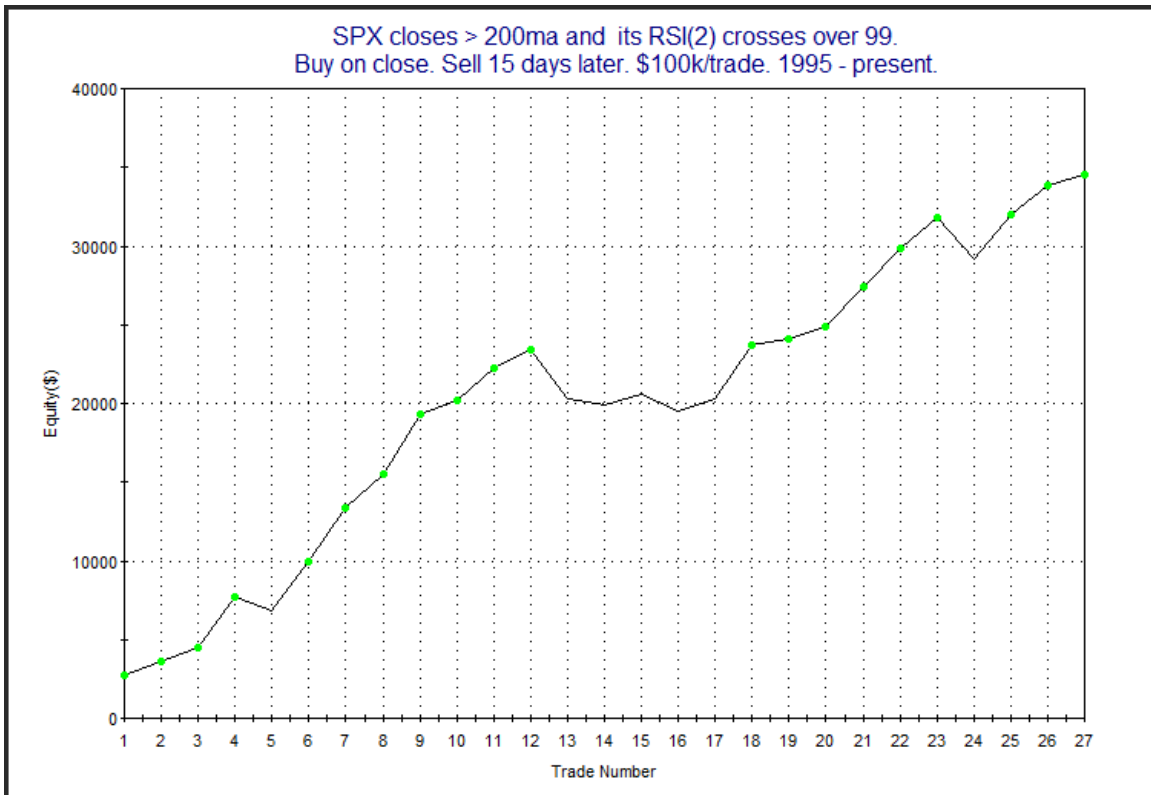
This week could not have been much smoother for the bulls, with the market rising every day. And though SPX has not yet surpassed its intraday high of 1687.18, set in May, it did finish the week at a new closing high. We also saw a couple of intermediate-term studies trigger. The basic premise behind both of them was the same – that the market became SO overbought short-term that the strength it was exhibiting suggested more strength. Below is an excerpt from the 7/10 letter:

*When the market starts to get short-term overbought we often see studies pop up that suggest a downside edge. But when the overbought condition gets very strongly overbought, then those downside edges often disappear. And rather than strength leading to weakness the strength will beget more strength. The strong move higher over the last several days has turned the market so overbought that downside edges are no longer prevalent. The study below exemplifies the kind of extreme short-term overbought scenario we now find ourselves in.*

SPX closes > 200ma and its RSI(2) crosses over 99.  
Buy on close. Sell X days later. \$100k/trade. 1995 - 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
15	34,512.42	27	22	5	81.48	1,931.79	3,782.11	-1,597.39	-3,063.60	1.21	5.32	1,278.24
14	28,533.54	27	21	6	77.78	1,846.81	4,461.36	-1,708.26	-2,699.52	1.08	3.78	1,056.80
13	26,642.59	28	22	6	78.57	1,701.62	3,989.82	-1,798.84	-3,320.01	0.95	3.47	951.52
12	24,794.49	28	21	7	75.00	1,633.76	4,058.61	-1,359.21	-3,175.53	1.20	3.61	885.52
11	26,358.22	28	21	7	75.00	1,738.15	4,106.40	-1,448.99	-2,523.21	1.20	3.60	941.36
10	20,657.71	29	20	9	68.97	1,648.39	3,770.55	-1,367.79	-2,793.28	1.21	2.68	712.33
9	16,176.32	29	19	10	65.52	1,481.25	3,453.27	-1,196.74	-3,440.07	1.24	2.35	557.80
8	17,854.08	29	18	11	62.07	1,578.74	3,547.80	-960.29	-3,460.32	1.64	2.69	615.66
7	10,612.67	30	17	13	56.67	1,318.34	3,564.39	-907.62	-4,153.62	1.45	1.90	353.76
6	2,710.06	30	17	13	56.67	1,060.43	2,634.36	-1,178.25	-5,296.92	0.90	1.18	90.34
5	856.08	30	19	11	63.33	808.13	1,782.39	-1,318.04	-3,596.40	0.61	1.06	28.54
4	1,338.68	30	20	10	66.67	789.89	2,442.90	-1,445.92	-3,039.18	0.55	1.09	44.62
3	-3,048.86	31	18	13	58.06	726.76	1,982.20	-1,240.82	-2,880.45	0.59	0.81	-98.35
2	-2,041.09	31	17	14	54.84	654.78	1,998.39	-940.88	-2,348.76	0.70	0.85	-65.84
1	754.93	31	15	16	48.39	659.89	2,096.10	-571.46	-3,515.37	1.15	1.08	24.35

The numbers here are basically neutral for the first week or so. On a short-term basis there is no edge apparent. But once you get out 2-3 weeks, it appears the strength has re-asserted itself and the market is often higher. Below is a profit curve showing a 15-day holding period.



The upside edge has been apparent for a while and still appears to be intact. Obviously this study does not help us with the short-term, but I have added it as an intermediate-term study.

This next excerpt was from the 7/11 letter, and it shows another similar study.

The study below is one of those that suggests SPX is overbought, and it is likely to continue moving higher. It was last seen in the 4/26/13 subscriber letter. All stats are updated.

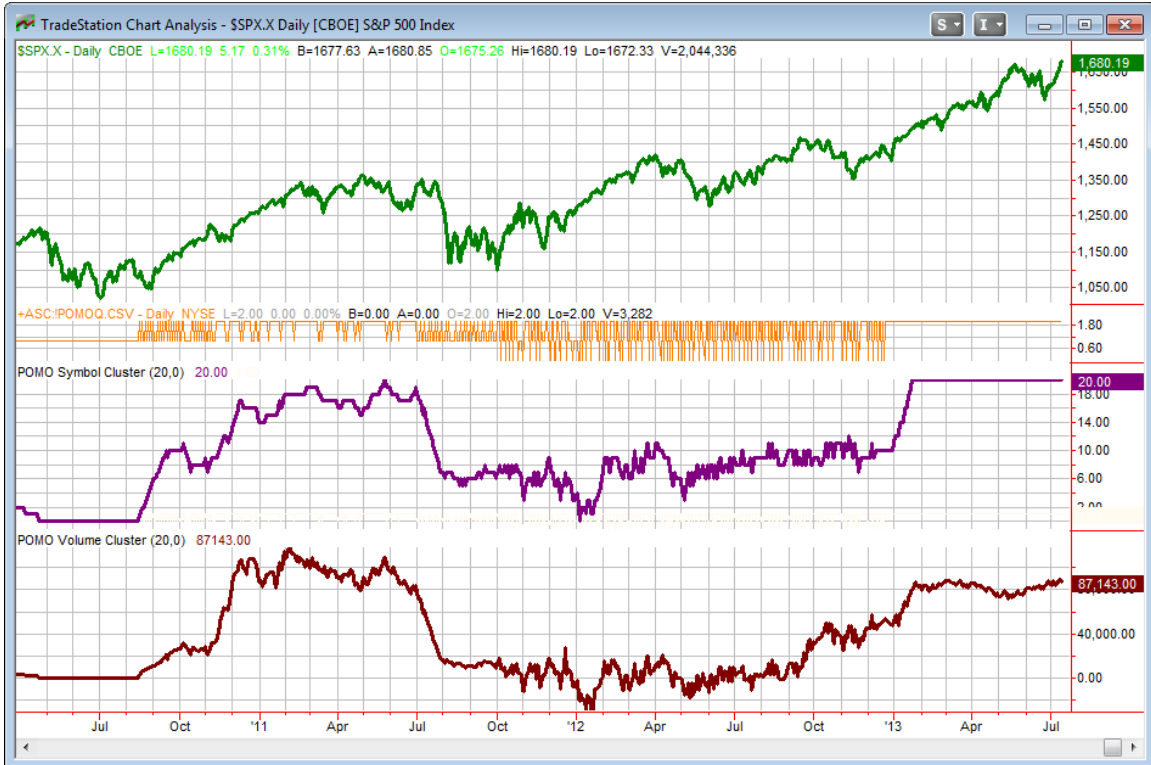
SPX closes up for exactly the 5th day in a row. Close > 200ma but < 50 day high. Buy on close. Sell X days later. \$100k/trade. 1960 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
15	113,231.39	77	53	24	68.83	2,828.94	8,288.00	-1,529.28	-4,879.10	1.85	4.09	1,470.54
14	100,757.42	77	52	25	67.53	2,687.94	8,272.60	-1,560.61	-4,738.50	1.72	3.58	1,308.54
13	100,260.26	77	57	20	74.03	2,434.29	6,401.50	-1,924.72	-3,773.44	1.26	3.60	1,302.08
12	89,488.55	79	57	22	72.15	2,241.45	5,925.50	-1,739.74	-3,661.77	1.29	3.34	1,132.77
11	75,943.79	80	54	26	67.50	2,096.53	6,110.00	-1,433.41	-4,887.00	1.46	3.04	949.30
10	77,107.29	80	57	23	71.25	1,870.98	5,675.25	-1,284.30	-4,684.28	1.46	3.61	963.84
9	73,017.08	80	53	27	66.25	1,945.35	5,228.75	-1,114.31	-4,910.55	1.75	3.43	912.71
8	65,224.12	81	57	24	70.37	1,615.52	5,146.50	-1,119.20	-3,376.64	1.44	3.43	805.24
7	57,618.38	81	53	28	65.43	1,664.93	5,698.75	-1,093.68	-3,500.70	1.52	2.88	711.34
6	48,953.60	81	58	23	71.60	1,379.35	5,134.75	-1,349.94	-3,359.36	1.02	2.58	604.37
5	41,004.45	81	57	24	70.37	1,220.01	4,476.75	-1,189.00	-3,716.53	1.03	2.44	506.23
4	28,897.62	81	54	27	66.67	1,031.22	3,983.25	-992.15	-3,494.78	1.04	2.08	356.76
3	25,624.37	81	53	28	65.43	998.64	2,796.50	-975.12	-3,359.36	1.02	1.94	316.35
2	12,467.20	81	51	30	62.96	769.03	2,479.25	-891.78	-3,748.50	0.86	1.47	153.92
1	6,920.66	81	49	32	60.49	508.32	2,211.54	-562.09	-2,193.72	0.90	1.38	85.44

These results appear to suggest a pretty consistent upside edge over the next 1-3 weeks.

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 \$20.2 billion, which is about average for 2013.

This week is expected to see POMO and AMBS inflows of just \$14.6 billion. This would be the lowest number so far in 2013. This week is also unusual in that there is NO POMO buying scheduled on Wednesday and Thursday (though there should be AMBS buying). Most non-POMO days so far this year have occurred around holidays or Fed announcement days. This week is neither so it is interesting to see this break in the buying schedule. Over the next 1-2 weeks we may get a preview of what tapering could feel like, since we are going to see reduced flows. Of course REAL tapering won't come with the expectation of increased flows the following week, which is what we currently expect for July.

The story remains largely the same. I am still leaning bullish. There is more evidence pointing in that direction. Studies based on price action, breadth, liquidity, and now momentum 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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