

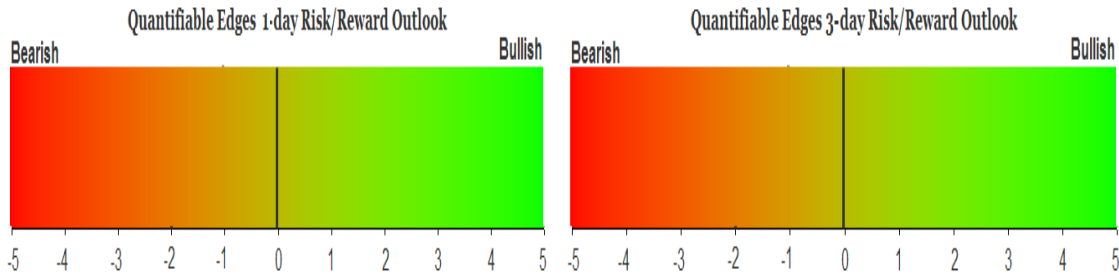
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 29, 2013

Volume 6 Issue 144

Market Overview



Signals Overview

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

Tonight's Research Points

- A 2-day rise in SPY that fails to make up the losses of the previous day has often been followed by more short-term buying when the market has been in an uptrend.
- Breadth measures are still diverging, setting up a condition where a major intermediate-term decline is possible.
- Liquidity flows are still strong and acting as a nice wind at the market's back.

Short-term Outlook

The Bottom Line

The Aggregator is still neutral. Action the last few days has done nothing to generate a substantial edge. I'm sidelined and awaiting a more favorable setup.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active				
July 29, 2013	SPY up 2 but < 3 ago	1-2 days	Bullish	
July 26, 2013	SPY gap & reverse 2 days > 10 & 200	1-4 days	Bearish	-1.20%
July 25, 2013	1st 5-low in 10 days	1-4 days	Bullish	1.60%
July 23, 2013	50-high. Inside day. 50-high.	1-5 days	Bearish	-2.00%
Active - Long Term				
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish	
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 4, 2013	Hindenburg Omen cluster	1-50 days	Bearish	-8.60%
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				
June 28, 2013	SPY up 3 days on lower volume	1-19 days	Bearish	-4.00%
July 24, 2013	SPX down. NYSE Up Issue > 55%	1-3 days	Bullish	1.20%

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

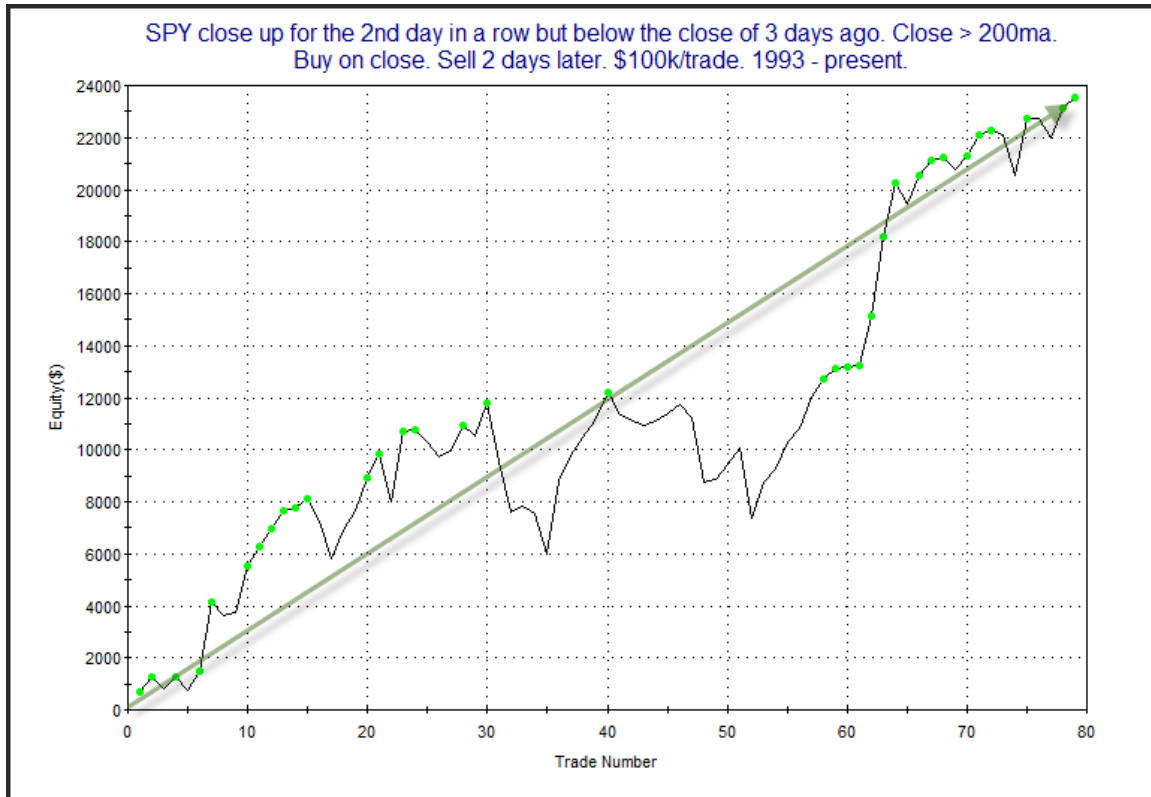
The Evidence

Friday was a lot like Thursday in that a weak morning saw a bounce back in the afternoon and a positive close for the SPX and Nasdaq. The SPX gained 0.1%, and the Nasdaq closed up 0.2%. But the Russell 2000 did not follow suit and declined 0.5%. Breadth was mildly negative as the NYSE Up Issues % was 47% and the Up Volume % was 48%. Total NYSE volume came in at the lightest level in over a week.

The study below was last seen in the 10/3/12 Letter. It looked at times the SPY bounced up 2 days in a row but still failed to close above the close of 3 days ago. It triggered again on Friday and I have updated it below.

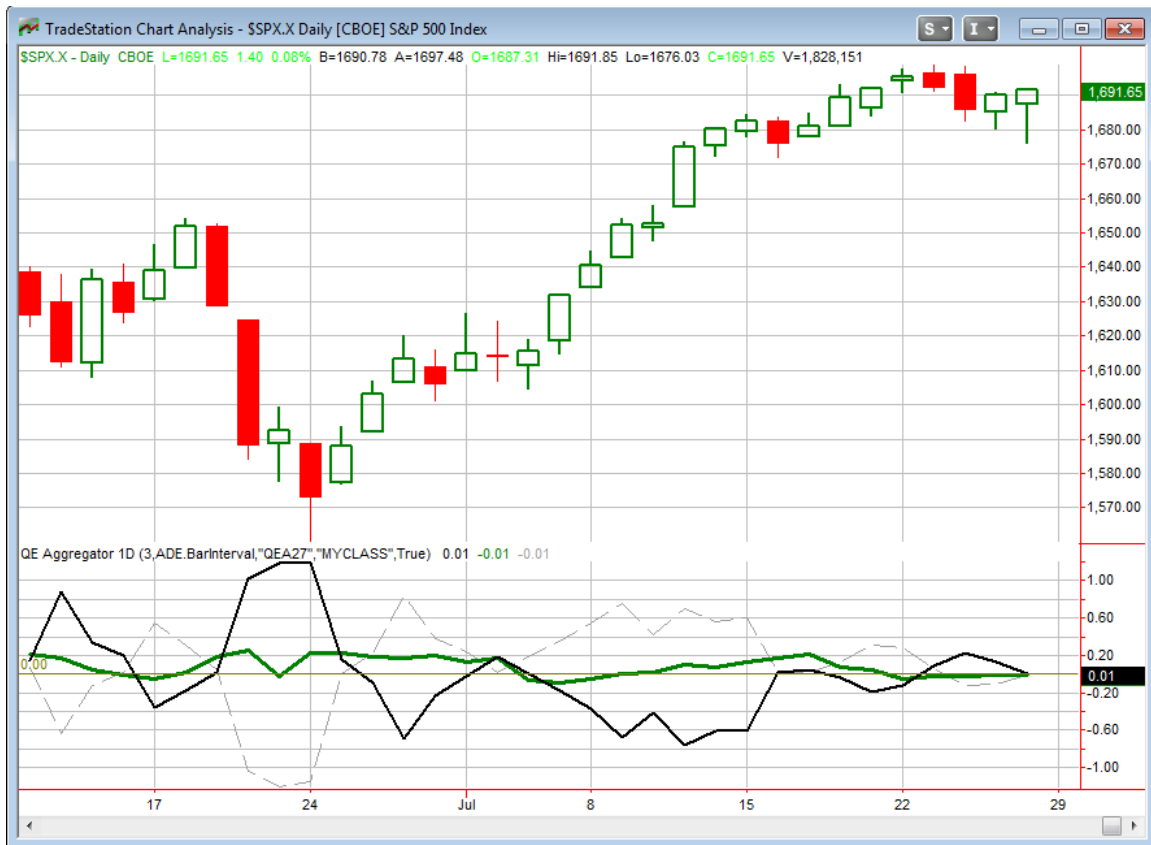
SPY closes up for the 2nd day in a row but below the close of 3 days ago. Close > 200ma. Buy on close. Sell X days later. \$100k/ trade. 1993 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: /Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	12,940.42	74	43	30	58.11	1,491.78	4,717.70	-1,706.86	-6,549.84	0.87	1.25	174.87
4	15,974.72	75	46	29	61.33	1,392.27	4,698.60	-1,657.58	-4,384.89	0.84	1.33	213.00
3	11,254.53	76	45	31	59.21	1,243.71	3,000.00	-1,442.33	-4,092.24	0.86	1.25	148.09
2	21,648.32	76	51	25	67.11	892.40	3,010.00	-954.57	-2,673.44	0.93	1.91	284.85
1	3,570.09	76	44	30	57.89	569.63	2,173.64	-716.46	-1,777.90	0.80	1.17	46.97

The stats appear to suggest a mild upside edge over the 1st 2 days. Below is an equity curve using a 2-day exit strategy.



There have been a few dips in the curve but overall it seems good enough to include the study on the Active List.

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



With both lines now so close to zero it is impossible to decipher the green Aggregator Line reading, but it is barely negative. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line is just barely above 0. The positive Differential Line reading means the SPX is mildly oversold versus recent expectations. So expectations are a little negative but the SPX is slightly oversold. 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 ever so slightly bearish on Monday. In other words, expectations will be largely dependent on what new studies emerge on Monday. The Differential Pivot will be *inverted* at 1,684.33 on Monday. That is 0.4% *below* Friday's close. An inverted pivot means the Differential Line will cross through 0 if SPX closes flat. So for SPX to remain "oversold" versus expectations, it is going to need to close lower by at least 0.4%. Otherwise, it will register "overbought".

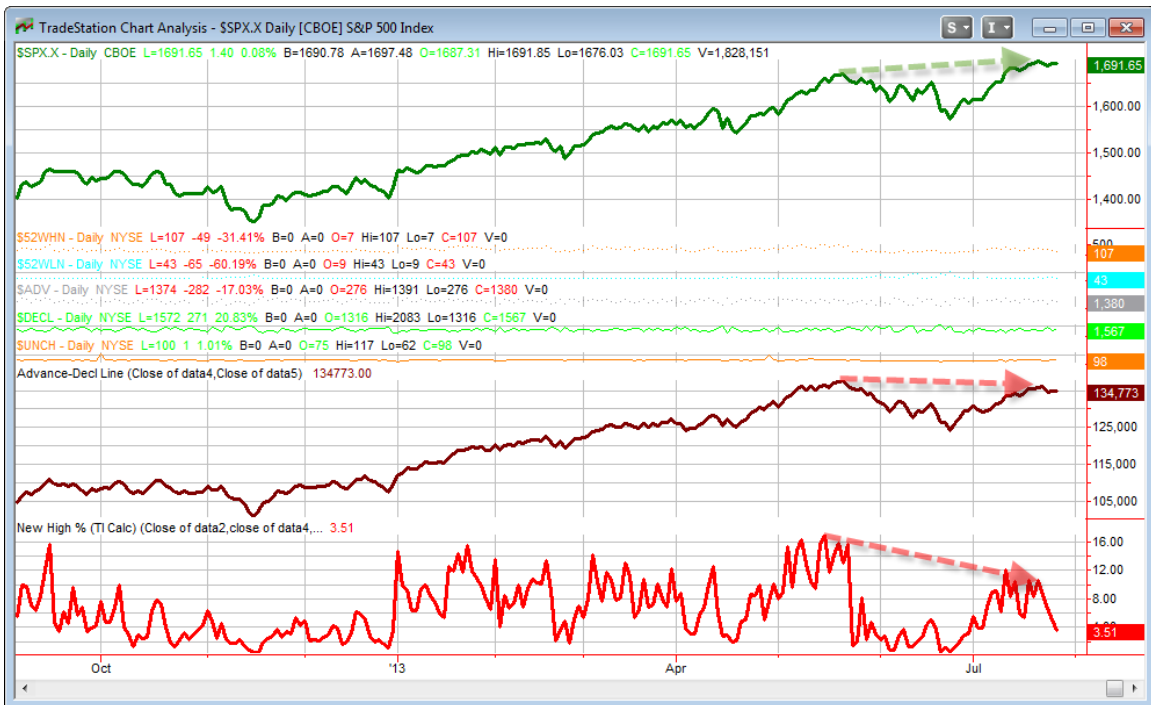
Not only is the Aggregator chart neutral with both lines closing on opposite sides of zero, but both lines are also very, very close to 0. It does not get any more neutral than this on

a short-term basis. So again there is little for me to do other than sit and wait for the next favorable opportunity.

Intermediate-term Outlook (2 weeks – 2 months)– updated 7/29 – somewhat bullish

While the SPX made new intra-week highs, the close on Friday was down a little less than 0.5 points from the previous Friday. But I am not seeing any strong signs that the uptrend is over. With much of the action this week being of the sideways variety, it is not too surprising that no new intermediate-term studies emerged.

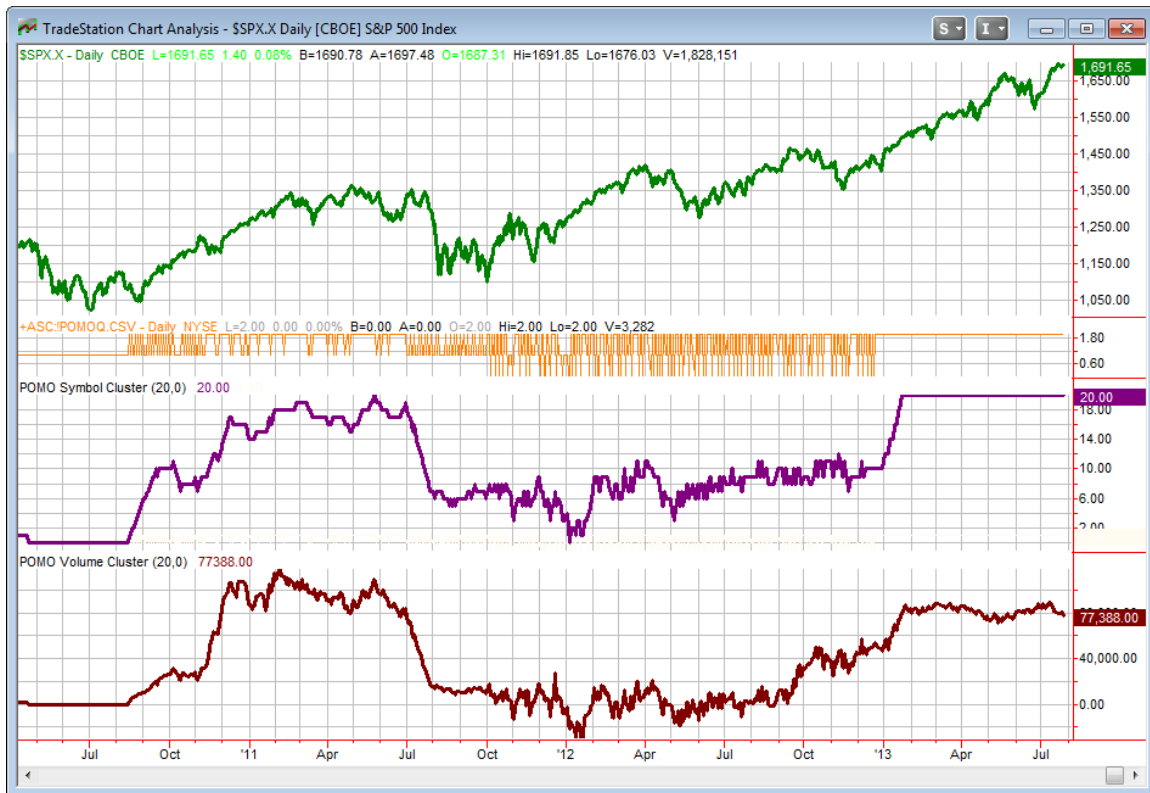
Last week I discussed the bearish divergence we are seeing in two breadth indicators – the Advance/Decline Line and the % of NYSE stocks hitting new highs. In the Quantifiable Edges Study of Tops (always available on the Downloads page for subscribers) I went through every major top since 1970. For purposes 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 the % of NYSE issues hitting new 52 week highs, and that the divergence was in effect for at least 2 months before any market top. The % of NYSE stocks making new highs peaked on May 15 at a level of 16.96%. The highest it has reached in the last couple of weeks has been 10.61% on Monday the 22nd. So the divergence is here more than 2 months after the New High % reading of 16.96% in May. This can be seen in the chart below, which is similar to those shown in the Study of Tops.



The indicator on the bottom is the NYSE % of stocks making new 52-week highs. The divergence there is clear. The maroon indicator above that, which is also in a divergence, is the Advance/Decline Line. It is important to keep in mind that these divergences can persist for months, and even years, before the market eventually begins its major decline. They are not a good timing device. But they are something to be aware of, and they provide a condition from which the market is capable of beginning a major decline. Without a divergence in place, we could feel comfortable (as we did in May) that the next major decline was highly unlikely to begin for at least a couple of months. I'll continue to watch this indicator closely going forward.

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 \$22 billion, which is a high number, and even a little higher than expected.

This upcoming week is still a little bit of a mystery. Monday and Tuesday we expect to see sizable inflows. Wednesday, which is both the last day of the month and a Fed Day, is expected to only see AMBS flows – nothing from POMO. Also Wednesday the August POMO schedule will be released. So we will learn not only what to expect on Thursday and Friday, but also for the rest of August.

The overall intermediate-term outlook is still leaning bullish. The breadth divergences we are now seeing along with the Hindenburg Omens from early June are providing some bearish evidence. But the majority of the other studies, including those related to trend, momentum, and liquidity, all point higher. I'm on the lookout for any evidence that would change (or confirm) my somewhat bullish stance. But for now, I still believe it is appropriate. I will continue to look to the long side for most of my trades until my outlook worsens.

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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