

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 22, 2013

Volume 6 Issue 204

Market Overview



Signals Overview

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

Tonight's Research Points

- VXO's extended stretch below the 10ma suggests SPX should dip in the next day or so.

Short-term Outlook

The Bottom Line

Nothing really has changed since last night. The market is too overbought for a short-term buy and the studies are not suggesting a strong downside edge. So I'll continue to wait for a better setup.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active - Short Term				
October 22, 2013	VXO 15% below 10ma 3+ days in row	1 day	Bearish	
October 21, 2013	Up Iss % > 70 for 3 days	1-2 days	Bullish	
October 21, 2013	8-day Avg %R > 75	1-2 days	Bearish	
October 18, 2013	Top 10% 10-day range. Tmrw opex	1-5 days	Bearish	
October 18, 2013	SPX 50-high breakout, low vol	1-5 days	Bullish	
October 18, 2013	NYSE Up Iss % Rank > 90 2x & 60-high	1-4 days	Bullish	
Active - Long Term				
October 21, 2013	70% Advancing Issues 3 Days In Row	1-75 days	Bullish	10.60%
October 14, 2013	VIX big swing	1-8 days	Bullish	
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish	
May 6, 2013	Nasdaq leading SPX	int term	Bullish	
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	

The Evidence

The market traded in a tight range on Monday and finished mixed. The SPX finished up less than 0.1%, the Nasdaq gained 0.2%, and the Russell 2000 lost 0.2%. Breadth was negative as the NYSE Up Issues % was 47% and the Up Volume % was 42%. Total NYSE volume dropped substantially from Friday's opex level.

The most intriguing bit of market action right now is the persistently low VXO readings. VXO closed down again on Monday and more than 20% below its 10-day moving average for the third day in a row. Below is a listing of all other instances have seen three consecutive closes of more than 20% < 10ma.

VXO closes more than 20% below 10ma for at least the 3rd day in a row.
Buy SPX on close. Sell next day's close. \$100k/trade. 1987 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
11/02/87	Buy	\$255.75	(1.93%)	\$0.00
11/03/87	Sell	\$250.82		(\$5,075.18)
11/03/87	Buy	\$250.82	(0.74%)	\$71.64
11/04/87	Sell	\$248.96		(\$1,787.02)
11/04/87	Buy	\$248.96	2.21%	\$2,859.13
11/05/87	Sell	\$254.47		(\$497.24)
11/05/87	Buy	\$254.47	(1.60%)	\$1,070.16
11/06/87	Sell	\$250.41		(\$1,881.60)
11/06/87	Buy	\$250.41	(2.90%)	\$0.00
11/09/87	Sell	\$243.16		(\$2,956.59)
10/14/11	Buy	\$1,224.58	(1.94%)	\$0.00
10/17/11	Sell	\$1,200.86		(\$2,108.43)
01/04/13	Buy	\$1,466.47	(0.31%)	\$0.00
01/07/13	Sell	\$1,461.89		(\$669.80)
01/07/13	Buy	\$1,461.89	(0.32%)	\$0.00
01/08/13	Sell	\$1,457.15		(\$697.00)

1/4/ & 1/7/13 were only two instances that took place > 200ma.

At first glance there appears to be quite a bit of red in the "% Profit" column. But closer examination shows that five of those instances came in 1987 a few weeks after the crash. The 2011 instance also occurred with the market in a downtrend. Only the two instances from early January appeared to occur under market conditions similar to those we currently have. So I loosened the days criteria a little bit and looked at all instances that were at least 20% stretch to the downside for two days in a row (and with SPX >200ma). Those results are below.

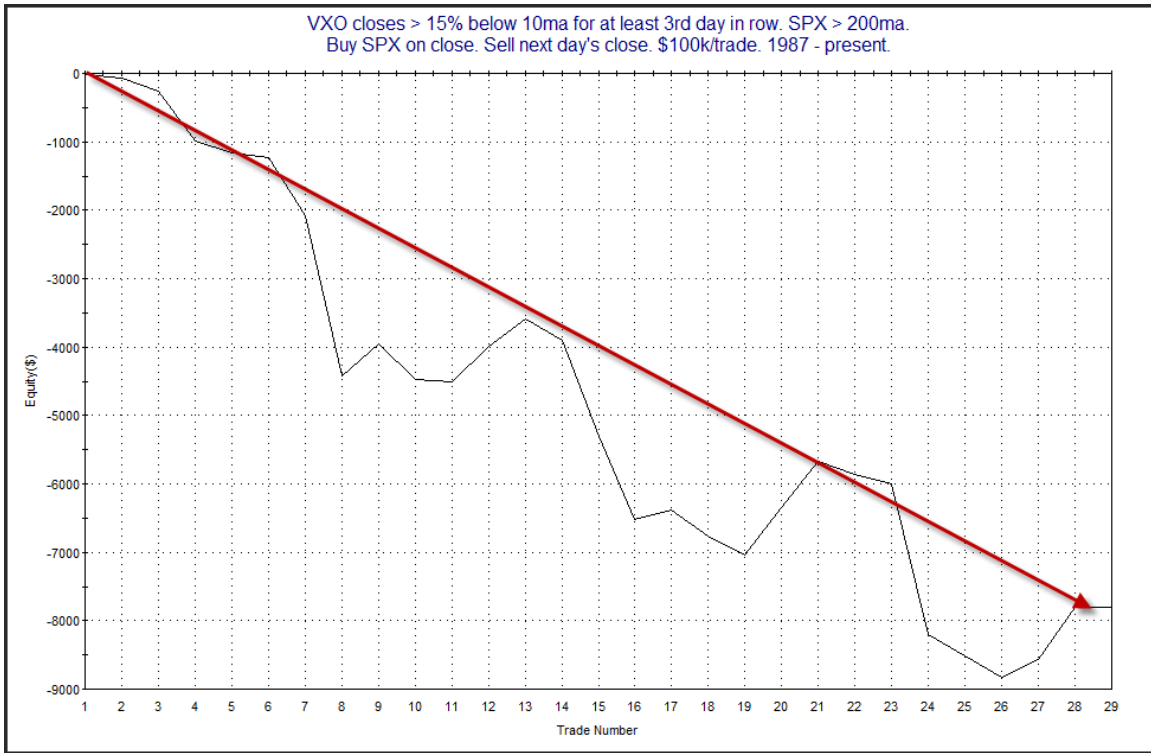
VXO closes more than 20% < 10ma for at least the 2nd day in a row and SPX > 200ma. Buy SPX on close. Sell next day's close. \$100k/trade. 1987 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
01/03/13	Buy	\$1,459.37	0.49%	\$582.76
01/04/13	Sell	\$1,466.47		(\$25.84)
01/04/13	Buy	\$1,466.47	(0.31%)	\$0.00
01/07/13	Sell	\$1,461.89		(\$669.80)
01/07/13	Buy	\$1,461.89	(0.32%)	\$0.00
01/08/13	Sell	\$1,457.15		(\$697.00)
10/18/13	Buy	\$1,744.50	0.01%	\$187.53
10/21/13	Sell	\$1,744.66		(\$218.31)

These filters don't appear to provide any kind of compelling results. Last night I showed a study that used a 15% stretch and required it to be exactly the third day in a row with a stretch of that size. I decided to change the requirements from “exactly” the third day to "at least" the third day. This gave a decent number of instances. Results can be found below.

VXO closes > 15% below 10ma for at least 3rd day in row. SPX > 200ma. Buy SPX on close. Sell next day's close. \$100k/trade. 1987 - present.			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	(\$7,801.39)	Profit Factor	0.33
Gross Profit	\$3,898.46	Gross Loss	(\$11,699.85)
Total Number of Trades	29	Percent Profitable	31.03%
Winning Trades	9	Losing Trades	20
Even Trades	0		
Avg. Trade Net Profit	(\$269.01)	Ratio Avg. Win:Avg. Loss	0.74
Avg. Winning Trade	\$433.16	Avg. Losing Trade	(\$584.99)
Largest Winning Trade	\$754.80	Largest Losing Trade	(\$2,341.24)

The numbers here suggest a possible downside edge. I also ran a profit curve to see how the edge played out over time.



The downslope appears fairly steady and seems to confirm the bearish edge.

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



Despite the bearish study tonight, the green Aggregator Line remained above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line is still below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are positive but the 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 signal to turn flat at the close.

Based on the current active studies, expectations are slated to remain positive on Tuesday. Of course this could change if more bearish evidence emerges. The Differential Pivot will be 1735.54 on Tuesday. That is 0.5% below Monday's close. So it will take a drop of at least this much for SPX to turn oversold.

The Aggregator is neutral, and I am too. I'm not seeing much to get me overly excited about either the long or short side. This market has simply been too strong to consider shorting, and it is now too overbought to consider going long. So I will wait until that changes before looking to take on new exposure.

Intermediate-term Outlook (2 weeks – 2 months) – *updated 10/21 – somewhat bullish*

The intermediate-term outlook was last updated in the 10/21 letter. Link below.

[2013-10-21 QE Subscriber Letter.pdf](#)

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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