

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 30, 2013

Volume 6 Issue 210

Market Overview



Signals Overview

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

Tonight's Research Points

- SPX and VIX up 2 days in a row with SPX at a 50-day high suggests a pullback.
- Bullish Fed Day inclinations have not held true when the market has closed at a 20-day high and in the upper part of its daily range.
- 10 days above the 5ma and a new 10-day high suggest the market is due for a brief pullback.

Short-term Outlook

The Bottom Line

Same story as the last couple of days. The Aggregator continues to point bearish, but risk is high, liquidity is strong, and the intermediate-term outlook is bullish. So I will not be attempting a short trade at this point.

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 30, 2013	VIX up. SPX 50-high. Mon / 2 Days	1 day	Bearish	
October 30, 2013	SPY > 5ma for 10 day. High close 10.	1-2 days	Bearish	
Active - Long Term				
October 25, 2013	SPX > 50,2 Bollinger Band	1-50 days	Bullish	
October 24, 2013	5 up to 50-high, then 1 down	1-10 days	Bullish	2.00%
October 21, 2013	70% Advancing Issues 3 Days In Row	1-75 days	Bullish	10.60%
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	
Dropped Tonight				
October 28, 2013	8-day avg %R crosses over 75%	1-2 days	Bearish	

The Evidence

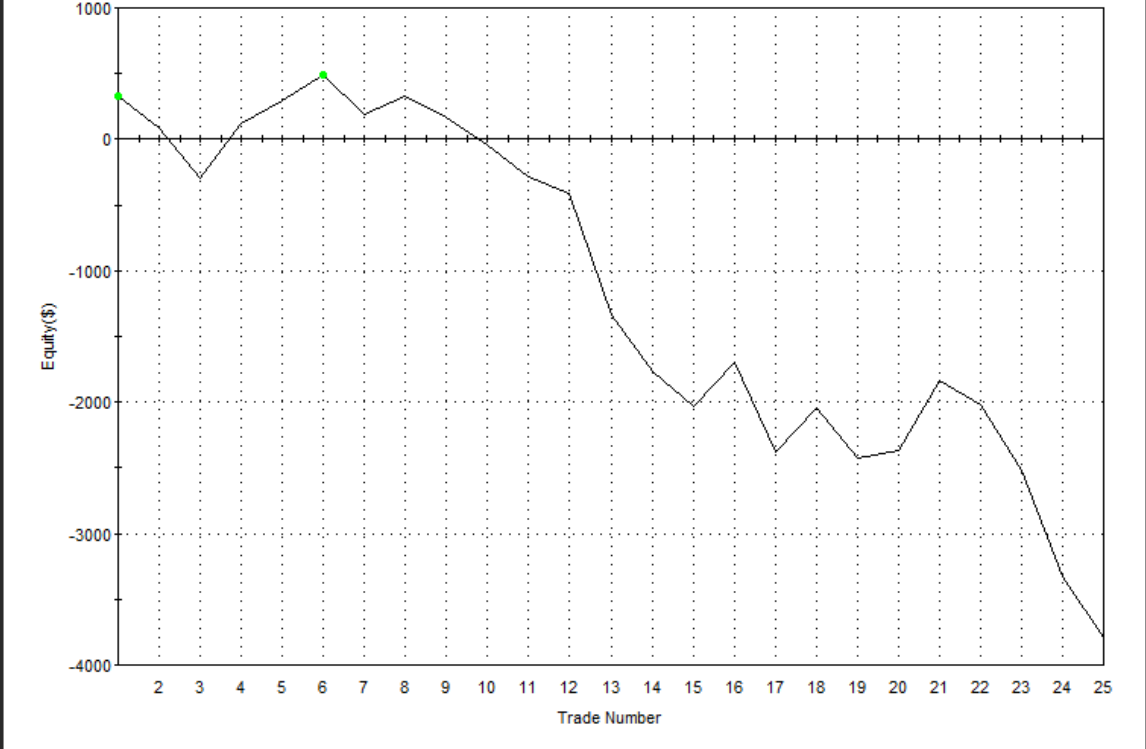
The major indices are not worried about the Fed announcement on Wednesday. They rose again on Tuesday like they have almost every day lately. The SPX closed up 0.6%, and the Nasdaq and Russell 2000 each gained 0.3%. Breadth was positive as the NYSE Up Issues % was 60% and the Up Volume % was 64%. Total NYSE volume declined some from Monday's level.

A few VIX related studies triggered once again. The VIX most often will trade opposite SPX. But today it rose along with it. That's not too unusual for one day, but the same thing also happened yesterday. This triggered the study below which was last seen just a week ago in the 10/23/13 subscriber letter, and has been updated.

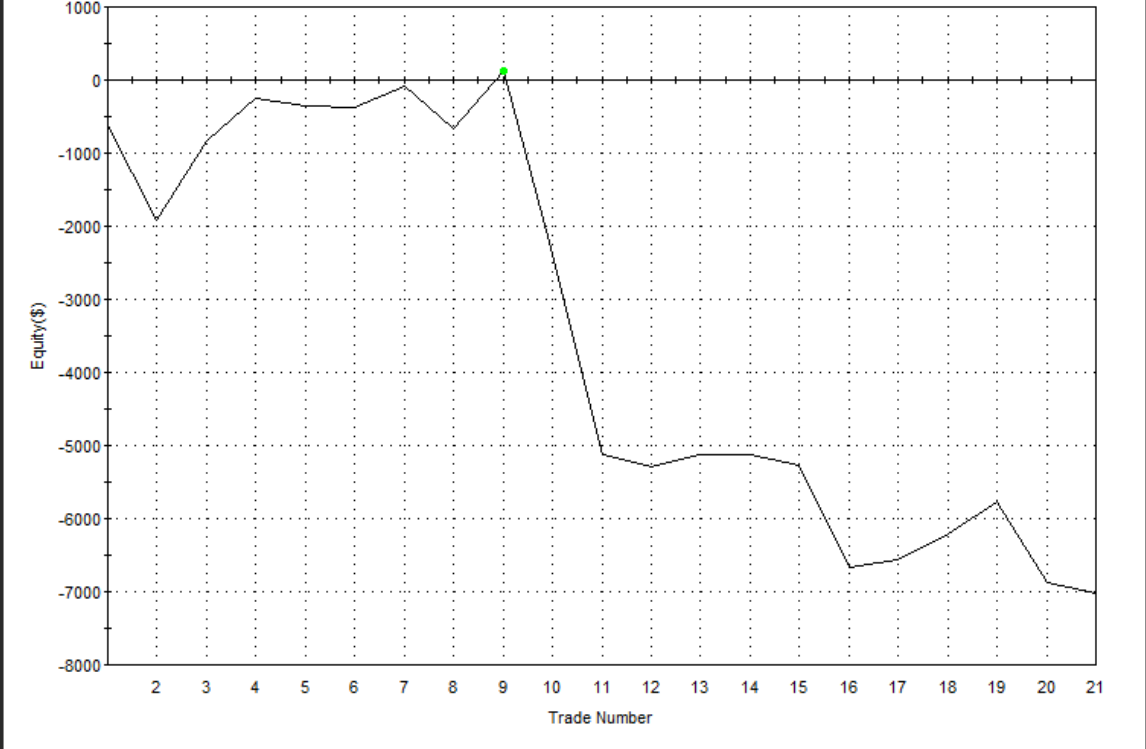
SPX and VIX both closed higher the last 2 days. SPX closed at a 50-day high. Buy SPX on close. Sell X days later. \$100k/trade. 1998 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Max Losing Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-5,470.71	20	12	8	60.00	908.72	3,434.08	-4,221.70	-2,046.92	0.44	0.67	-273.54
4	-7,955.74	21	11	10	52.38	692.76	1,907.36	-4,240.48	-1,557.61	0.44	0.49	-378.84
3	-8,494.48	21	9	12	42.86	639.16	1,433.12	-4,423.40	-1,187.24	0.54	0.40	-404.50
2	-7,013.94	21	8	13	38.10	477.63	1,078.48	-2,752.74	-833.46	0.57	0.35	-334.00
1	-3,793.26	25	9	16	36.00	280.48	537.24	-924.70	-394.85	0.71	0.40	-151.73

The stats appear somewhat bearish. While, 2-3 days have seen larger drops, their equity curves were not terribly appealing. Below are both the 2-day and 1-day profit curves.

SPX and VIX both closed higher the last 2 days. SPX closed at a 50-day high.
 Buy SPX on close. Sell 1 day later. \$100k/trade. 1998 - present.



SPX and VIX both closed higher the last 2 days. SPX closed at a 50-day high.
 Buy SPX on close. Sell 2 days later. \$100k/trade. 1998 - present.

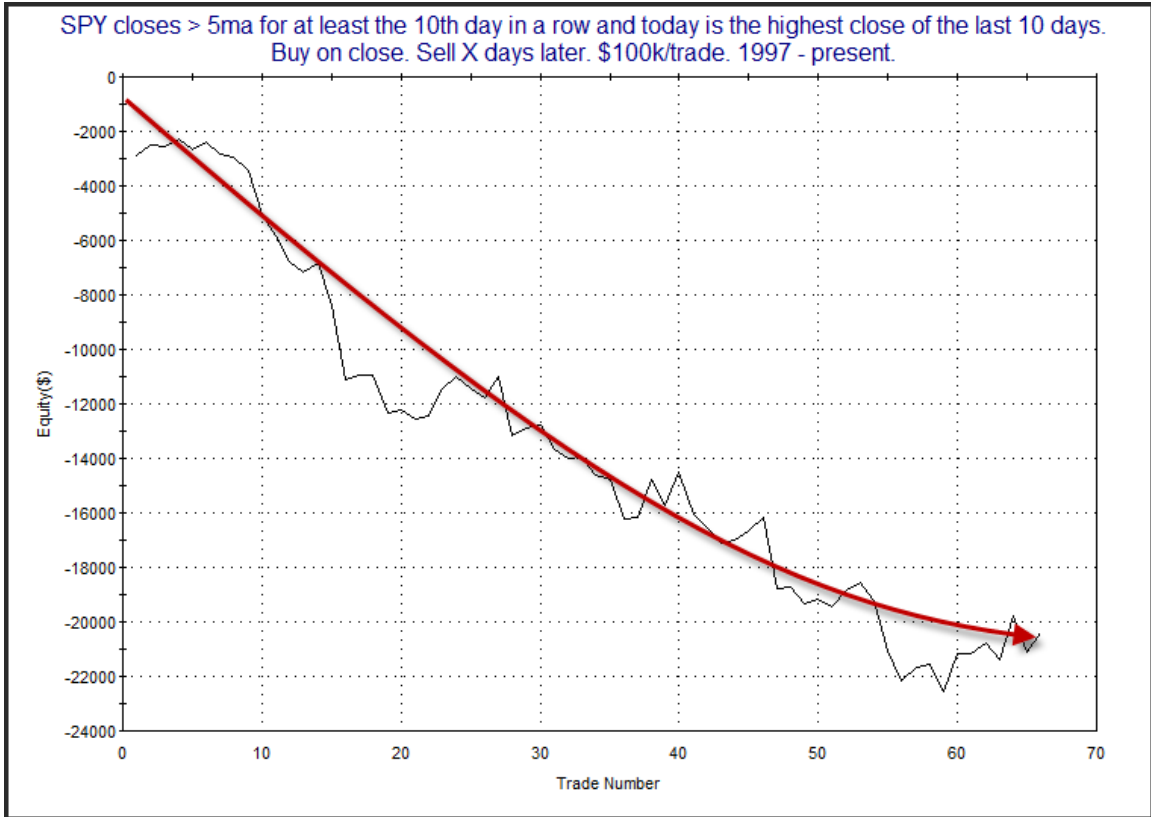


As you can see, the 1-day curve appears much steadier, and it is the timeframe that I decided to use for the study on the Active List. Of course we also had a study still active from last night looking at SPX 50-days highs on a Monday when the VIX was closing up. I just combined this one and that one's projections for purposes of the Aggregator and treated them as one study.

SPY has now gone 14 days without closing below its 5ma. The study below is repeated from just 2 days ago in the 10/28/13 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 the 10th day 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: Max Losing Trade	All: Avg Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-11,430.95	43	23	20	53.49	748.75	2,516.52	-4,014.40	-1,432.62	0.52	0.60	-265.84
4	-15,838.32	47	20	27	42.55	673.16	1,428.90	-3,723.20	-1,085.24	0.62	0.46	-336.99
3	-15,131.10	55	22	33	40.00	667.67	1,790.80	-3,235.65	-903.63	0.74	0.49	-275.11
2	-20,413.18	66	30	35	45.45	455.45	1,608.38	-2,870.40	-973.62	0.47	0.40	-309.29
1	-19,486.18	94	41	53	43.62	336.62	1,361.25	-2,817.32	-628.07	0.54	0.41	-207.30

In the past this setup has commonly 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.



This one has been headed lower for a long time. The persistency is impressive. The recent bump up bears watching but is not of great concern just yet.

Of course Wednesday is a Fed Day, and as I have documented over and over, Fed Days have a bullish tendency. But current Fed Day inclinations do not appear as strong as they typically are. Both closes in the upper part of the daily range, and intermediate-term highs can reduce the upside edge. In the 5/1/13 subscriber letter I looked at the combination of a close in the upper end of the daily range along with a 20-day closing high. Results below are all updated.

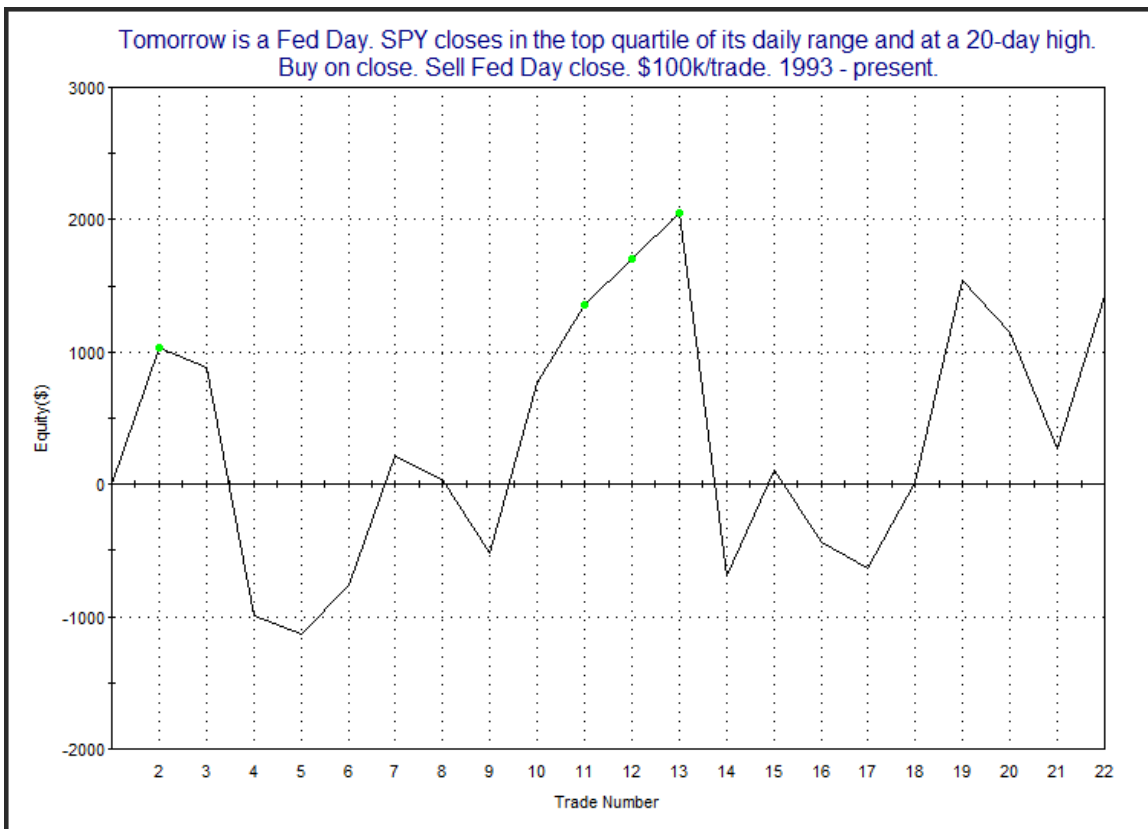
Tomorrow is a Fed Day. SPY closes in the top quartile of its daily range and at a 20-day high.
Buy on close. Sell Fed Day close. \$100k/trade. 1993 - present.

TradeStation Performance Summary Collapse ↕

All Trades

Total Net Profit	\$1,426.15	Profit Factor	1.19
Gross Profit	\$9,064.77	Gross Loss	(\$7,638.62)
Total Number of Trades	22	Percent Profitable	50.00%
Winning Trades	11	Losing Trades	10
Even Trades	1		
Avg. Trade Net Profit	\$64.83	Ratio Avg. Win:Avg. Loss	1.08
Avg. Winning Trade	\$824.07	Avg. Losing Trade	(\$763.86)
Largest Winning Trade	\$1,522.40	Largest Losing Trade	(\$2,739.69)

Results here suggest no edge whatsoever. Below is the equity curve.



Fed Days under these conditions don't seem to provide the bullish edge they typically do otherwise.

So a couple of very short-term studies with mild bearish implications are being added to the Active List tonight.

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



Tonight the green Aggregator Line remained below 0. Negative readings mean net expectations from the Active List are for downside 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 negative and the 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 signal to remain short at the close.

Based on the current studies, expectations are set to remain negative on Wednesday. Of course this could easily change if new bullish evidence emerges. The Differential Pivot will be 1758.16 on Wednesday. That is 0.8% below Tuesday's close. So SPX would need to decline at least this much in order to turn oversold on Wednesday.

There are a lot of crosswinds right now. Short-term the market is overbought, overdue for a pullback, and providing some evidence to suggest that is likely to play out in the next couple of days. The 3/10 Offset HV, which I discussed in detail last night, remains very low, which suggests a sharp move could be on tap. Additionally, we have a significant event that is going to occur on Wednesday in the form of an FOMC announcement. The lead-up to the announcement is normally bullish, but as we saw in the study above, the bullish lead-up may have already exhausted itself. Of course all of this is coming in an environment which has both very strong liquidity and momentum – an environment that has punished shorts over and over.

My approach to trading is to basically wait for high probability scenarios with favorable risk/reward to emerge and then look to take advantage of them. This just does not appear to be one of those scenarios. So I will continue to wait. And I will likely miss a sharp move tomorrow when the Fed makes their announcement. But since I am not confident in the direction of that move, I have no desire to bet on it. The most frustrating periods of time for me over the years were the ones where I got chewed up trying to trade environments where my strategies had no substantial, quantifiable edge. So I gave up doing that a while ago, and both my account and my psyche have benefitted. In other words, I'm just going to see how tomorrow plays out, and then I'll evaluate all over again. No new positions are likely to be initiated at my desk.

Intermediate-term Outlook (2 weeks – 2 months) – updated 10/28 – somewhat bullish

The intermediate-term outlook was last updated in the 10/28 Letter. Link below:

[2013-10-28 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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