

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 13, 2014

Volume 7 Issue 30

Market Overview



Signals Overview

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

Tonight's Research Points

- The VXO's extended stretch below the 10ma suggests the SPX should decline in the next 1-2 days.
- When an overbought market pulled back as little as it did today, it may not want to pullback at all, and has often continued higher over the next 1 to 2 days.
- 5 higher highs under similar circumstances in the past has often been followed by a pullback.

Short-term Outlook

The Bottom Line

The market remains overbought, but the weight of the evidence still favors more upside. The Aggregator is neutral. I am too.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active - Short Term				
February 13, 2014	SPX down but RSI(2) > 90	1-2 days	Bullish	
February 13, 2014	SPX 5 higher highs. No 20-high.	1-5 days	Bearish	
February 13, 2014	VXO 15% downstretch 3 days	1-2 days	Bearish	
February 12, 2014	SPX up 4 days. 3 > 1%. Close > 200ma	1-3 days	Bullish	1.70%
February 10, 2014	VIX high stretch to low stretch	1-8 days	Bullish	2.70%
Active - Long Term				
January 27, 2014	2 unfilled dn gaps & 5-low > 200	1-10 days	Bullish	
December 23, 2014	QE Tapering	int term	Neutral	
December 2, 2013	Nasdaq leading SPX	int term	Bullish	
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish	
February 1, 2012	Golden Cross	int term	Bullish	

The Evidence

Wednesday the market posted another higher high, but it failed to hold those gains through the end of the day. In the end the SPX closed down 0.49 points, the Nasdaq gained 0.2%, and the Russell 2000 rose 0.3%. Breadth was mixed as the NYSE Up Issues % came in at 52% and the Up Volume % was 48%. Total NYSE volume sank some from Tuesday's level.

Though the numbers appear moderate as compared to the last few days, Wednesday triggered a fair amount of studies worth talking about, and the indications from those studies were mixed.

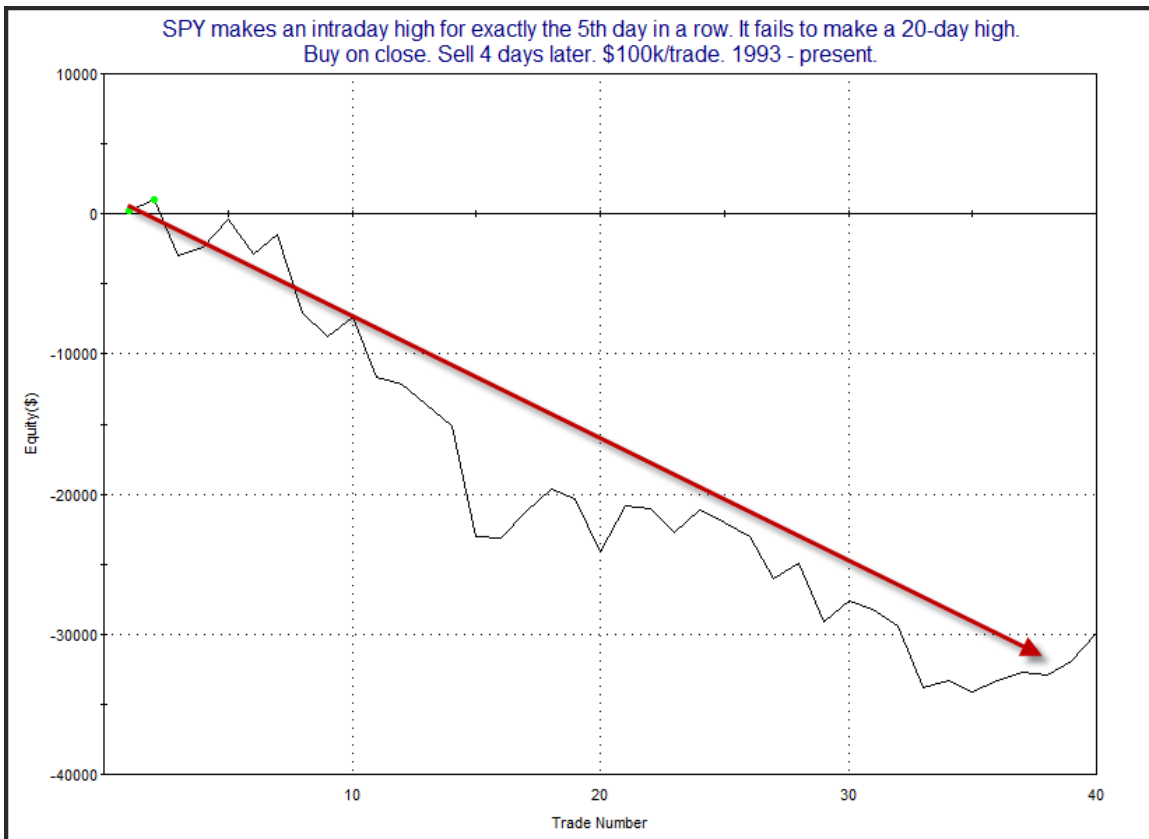
Wednesday marked the fifth day in a row that the S&P 500 made a higher high. Often after this occurs, the market will either pause or pullback. There were a few studies that looked at instances of five higher highs in the Quantifinder tonight.

The study below was last updated in the 10/12/11 subscriber letter. It looks for times that the five higher highs failed to register a 20-day high. All statistics are updated.

SPY makes an intraday high for exactly the 5th day in a row. It fails to make a 20-day high.
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	-14,730.72	40	21	19	52.50	1,589.94	8,382.48	-2,532.60	-6,714.00	0.63	0.69	-368.27
4	-29,929.81	40	17	23	42.50	1,295.38	3,317.60	-2,258.75	-7,879.83	0.57	0.42	-748.25
3	-9,366.55	40	22	18	55.00	1,242.34	4,059.44	-2,038.78	-4,560.85	0.61	0.74	-234.16
2	-473.92	40	19	21	47.50	1,178.75	5,364.26	-1,089.06	-2,373.84	1.08	0.98	-11.85
1	-605.54	40	20	20	50.00	702.91	3,057.76	-733.18	-2,245.23	0.96	0.96	-15.14

Here we see what appears to be a bit of a downside edge. The profit curve using a 4-day exit strategy can be found below.



The equity curve has curled up a bit lately, and that is something to keep watch on. But for now I have decided to place the study on the Active List.

Wednesday we again saw the VIX and VXO close well below their recent mean. Such stretches suggest a collapse in fear among investors. The study below was last seen in the 12/27/13 subscriber letter. It looks for stretches of 15% or more that have persisted for three days.

VXO closes over 15% below its 10ma for exactly the 3rd day in a row. Buy SPX on close. Sell X days later. \$100k/trade. 1987 - 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	-24,902.76	24	12	12	50.00	799.12	2,073.06	-2,874.35	-10,448.88	0.28	0.28	-1,037.62
4	-18,864.38	24	12	12	50.00	799.60	2,331.45	-2,371.64	-5,673.45	0.34	0.34	-786.02
3	-14,629.49	24	11	13	45.83	983.38	1,904.75	-1,957.43	-8,395.18	0.50	0.43	-609.56
2	-16,589.97	24	6	18	25.00	924.84	1,737.55	-1,229.95	-5,164.42	0.75	0.25	-691.25
1	-15,932.65	24	6	18	25.00	651.62	1,990.25	-1,102.35	-4,980.56	0.59	0.20	-663.86

Just 4 instances failed to close below the entry price on either day 1 or day 2. All 4 continued higher and did not post a close below the entry price any time in the next month. The 4 instances took place on 7/18/94, 10/19/98, 10/2/01 & 10/18/13.

Based on the stats table there appears to be a downside inclination. I find the note at the bottom of the study to be especially interesting. Nearly every case has experienced an almost immediate pullback, but those that didn't went without pulling back for a long time. Below I have listed all instances assuming a 2-day exit strategy.

VXO closes over 15% below its 10ma for exactly the 3rd day in a row.
Buy SPX on close. Sell 2 days later. \$100k/trade. 1987 - present.

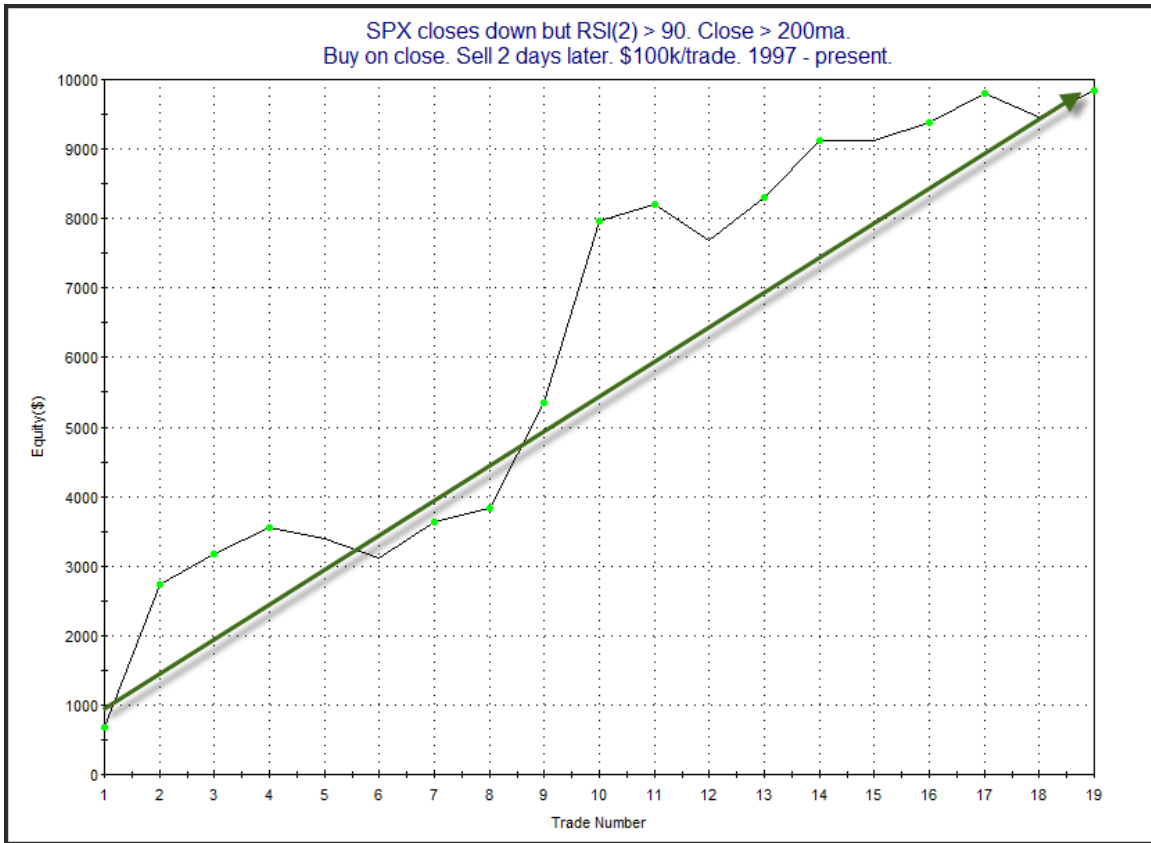
Date/Time	Signal	Price	% Profit	Run-up Drawdown
11/02/87	Buy	\$255.75	(2.65%)	\$0.00
11/04/87	Sell	\$248.96		(\$5,075.18)
12/23/87	Buy	\$253.16	(3.00%)	\$0.00
12/28/87	Sell	\$245.57		(\$3,543.15)
11/14/90	Buy	\$320.39	(1.02%)	\$0.00
11/16/90	Sell	\$317.12		(\$1,687.92)
01/25/91	Buy	\$336.07	(0.07%)	\$395.01
01/29/91	Sell	\$335.84		(\$537.57)
07/18/94	Buy	\$448.55	0.68%	\$1,498.50
07/20/94	Sell	\$451.60		\$0.00
12/16/94	Buy	\$458.80	(0.37%)	\$0.00
12/20/94	Sell	\$457.10		(\$527.31)
10/19/98	Buy	\$1,062.40	0.71%	\$2,035.10
10/21/98	Sell	\$1,069.90		(\$404.20)
12/23/98	Buy	\$1,228.54	(0.25%)	\$241.38
12/28/98	Sell	\$1,225.48		(\$597.78)
10/02/01	Buy	\$1,051.33	1.74%	\$3,115.05
10/04/01	Sell	\$1,069.62		(\$935.75)
07/31/02	Buy	\$911.62	(5.20%)	\$0.00
08/02/02	Sell	\$864.24		(\$6,286.03)
08/19/02	Buy	\$950.70	(0.14%)	\$93.45
08/21/02	Sell	\$949.36		(\$2,034.90)
08/24/07	Buy	\$1,479.37	(3.18%)	\$0.00
08/28/07	Sell	\$1,432.36		(\$3,173.12)
09/20/07	Buy	\$1,518.75	(0.07%)	\$789.10
09/24/07	Sell	\$1,517.73		(\$169.00)
12/26/07	Buy	\$1,497.66	(1.28%)	\$0.00
12/28/07	Sell	\$1,478.49		(\$1,713.36)
11/05/08	Buy	\$952.77	(2.29%)	\$0.00
11/07/08	Sell	\$930.99		(\$5,515.12)
02/22/10	Buy	\$1,108.01	(0.25%)	\$51.30
02/24/10	Sell	\$1,105.24		(\$1,424.70)
06/17/10	Buy	\$1,116.04	(0.25%)	\$1,351.91
06/21/10	Sell	\$1,113.20		(\$694.20)
03/25/11	Buy	\$1,313.80	0.43%	\$451.44
03/29/11	Sell	\$1,319.44		(\$649.04)
07/01/11	Buy	\$1,339.67	(0.03%)	\$93.98
07/06/11	Sell	\$1,339.22		(\$647.50)
10/12/11	Buy	\$1,207.25	1.44%	\$1,423.52
10/14/11	Sell	\$1,224.58		(\$1,366.94)
06/20/12	Buy	\$1,355.69	(1.52%)	\$188.34
06/22/12	Sell	\$1,335.02		(\$2,283.44)
01/04/13	Buy	\$1,466.47	(0.64%)	\$0.00
01/08/13	Sell	\$1,457.15		(\$1,008.44)
10/18/13	Buy	\$1,744.50	0.58%	\$845.31
10/22/13	Sell	\$1,754.67		(\$218.31)
12/26/13	Buy	\$1,842.02	(0.05%)	\$154.98
12/30/13	Sell	\$1,841.07		(\$175.50)
Avg run-up: \$530.94 Avg Drawdown: -\$1,694.52				

The fact that the average drawdown is over 3x the size of the average run-up is also worth considering. All in all it appears the stretched VXO is suggesting a short-term pullback. I have included this study on the active list

But not everything favored the bears. The recent string of positive closes has some oscillators strongly overbought short-term. With such a small decline on Wednesday the SPX is still strongly overbought as measured by the 2-day RSI. The 2-day RSI is a very sensitive indicator so it would take a very small decline from a very overbought position in order for it to remain above 90 on a down day. This is what happened on Wednesday. It therefore triggered the below study from the 12/30/13 letter, which I have updated.

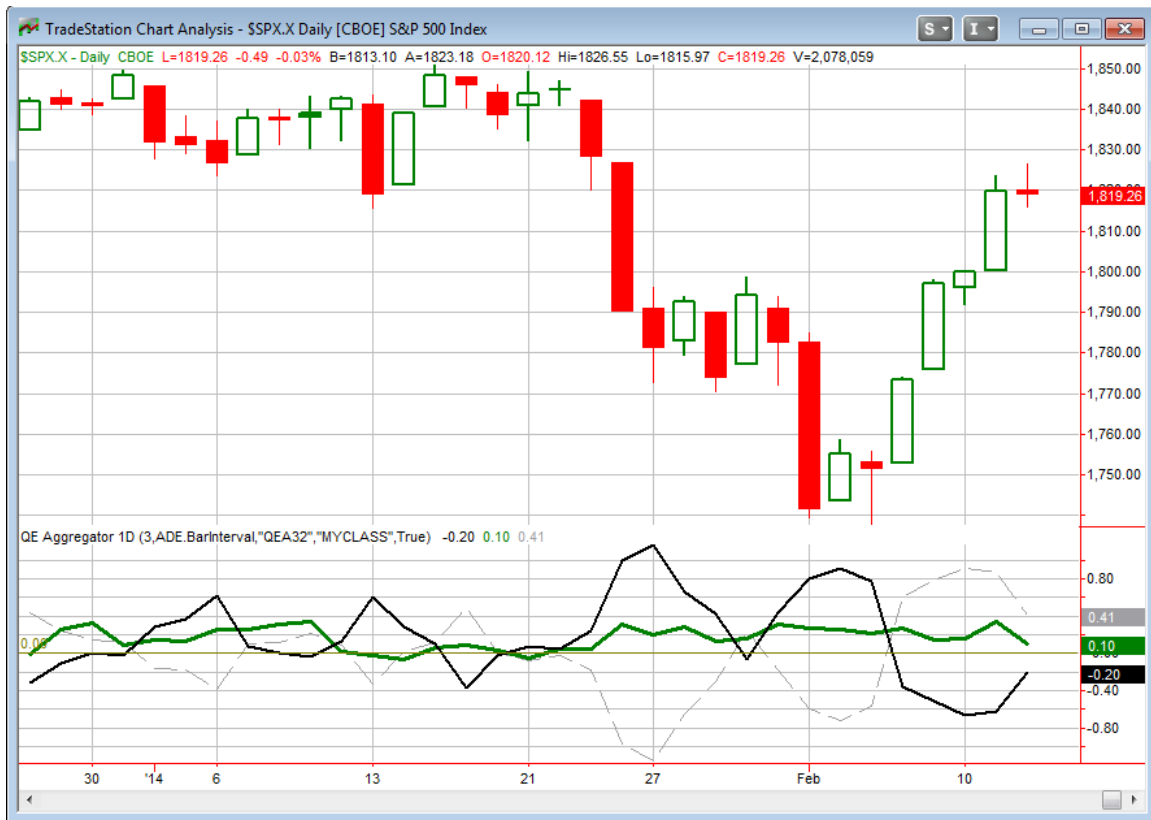
SPX closes down but RSI(2) > 90. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - present.												
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	2,128.96	17	6	11	35.29	1,771.65	4,121.28	-772.81	-2,008.73	2.29	1.25	125.23
4	4,184.33	18	9	9	50.00	1,208.11	3,806.46	-743.18	-1,717.70	1.63	1.63	232.46
3	9,426.79	19	11	8	57.89	1,139.00	2,923.44	-387.78	-1,123.50	2.94	4.04	496.15
2	9,844.19	19	14	5	73.68	795.23	2,619.76	-257.80	-525.07	3.08	8.64	518.12
1	4,841.30	19	14	5	73.68	460.67	2,310.88	-321.61	-704.76	1.43	4.01	254.81

The stats here are all appealing over the 1-2 day period. Winning %, win/loss ratio, and profit factor all strongly favor the bulls. Below is a profit curve assuming a 2-day holding period.



Results here are impressive. I have added this study to the Active List.

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



The mixed evidence tonight caused the green Aggregator Line to dip some, but it still remains 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 remain flat.

Based on the current open studies, expectations are slated to remain positive on Thursday. Of course this could easily change if more bearish evidence emerges. The Differential Pivot will be 1809.95 on Thursday. That is 0.5% below Wednesday's close. So it will take a close lower of at least this much in order for SPX to flip from overbought to oversold versus expectations.

The mild market movement and the mix of studies has the Aggregator – and me – still with a neutral outlook. I still have no interest in getting involved on the long side with the market this overbought, and no interest in the short-side unless bearish evidence strengthens. So it remains a waiting game for me.

Intermediate-term Outlook (2 weeks – 2 months) – updated 2/10 – neutral

The intermediate-term outlook was last updated in the 2/3 Letter. It can be found in the most recent weekly letter on the website.

<http://quantifiableedges.com/current-weekly-letter/>

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 [numbered systems 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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