

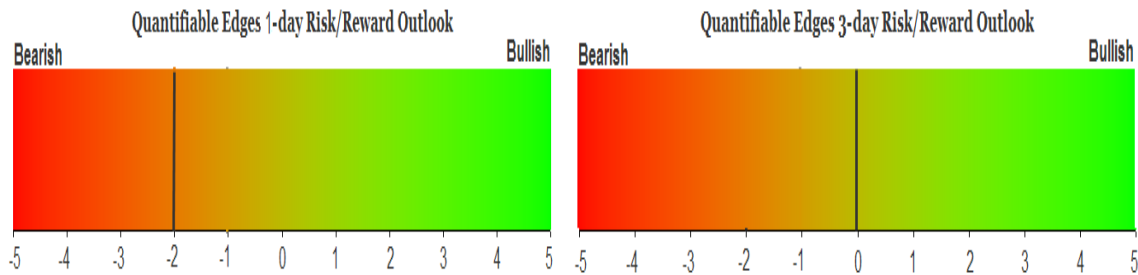
QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 30, 2014

Volume 7 Issue 124

Market Overview



Signals Overview

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

Tonight's Research Points

- A gap up and reversal down followed by a gap down and reversal up suggests a bearish short-term edge when SPY is uptrending.
- Friday's mild up close near the top of its range suggests a bearish 1-day edge.

Short-term Outlook

The Bottom Line

Bearish studies today are making Monday look risky, but overall evidence still suggests we could be higher by Wednesday. But with the market now overbought the Aggregator is neutral. I don't see a high-probability setup right here.

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

Study Date	Description	Time span	Bias	Avg Max Move
Active - Short Term				
June 30, 2014	SPY up < 0.25% and top 10% range	1 day	Bearish	
June 30, 2014	Gap reverse 2x > 10ma > 200ma	1 day	Bearish	
June 25, 2014	20-day intraday high. Close bottom 10%	1-8 days	Bullish	2.00%
June 19, 2014	100-day high on Fed Day	1-8 days	Bullish	1.90%
Active - Long Term				
June 24, 2014	5 up to 50-high then down	1-10 days	Bullish	
June 2, 2014	NASDAQ leading SPX	int term	Bullish	
April 28, 2014	Sell in May	6 months	Bearish	
December 23, 2013	QE Tapering	int term	Neutral	
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish	
February 1, 2012	Golden Cross	int term	Bullish	
Dropped Tonight				
June 13, 2014	Unfilled gap dn 2 days in row > 200	1-10 days	Bullish	
June 9, 2014	RSI(2) > 99	1-15 days	Bullish	2.40%
June 23, 2014	1%-2% Rise during opex week > 200	1-5 days	Bearish	-1.40%

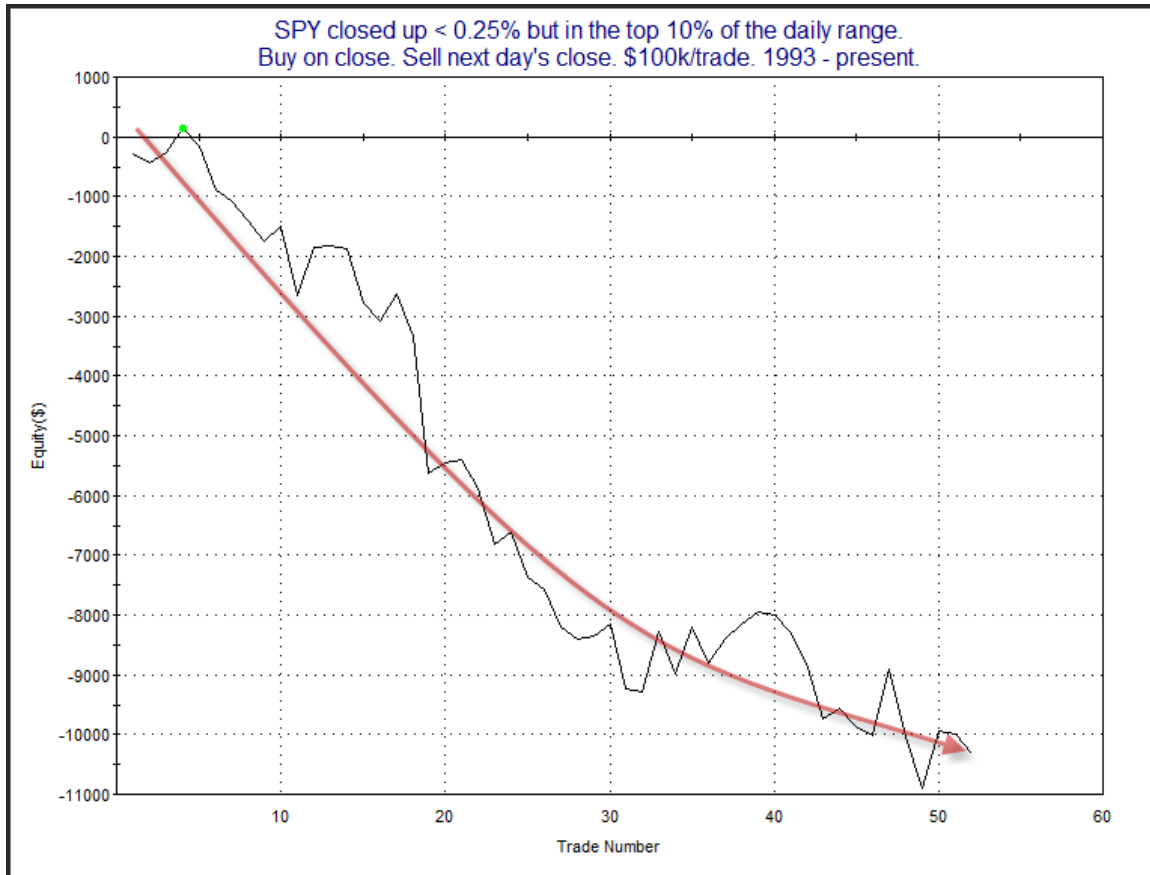
The Evidence

On Friday the market recovered from morning weakness and the major indices all posted gains. The SPX rose 0.2%, the NASDAQ rallied 0.4%, and the Russell 2000 gained 0.7%. Breadth was positive as the NYSE Up Issues % came in at 65% and the Up Volume % was 59%. Total NYSE volume rose quite a bit from Thursday's level.

Though the action was fairly mild, we did see a few interesting studies appear in the Quantifinder. The first study was seen recently in the 6/11/14 subscriber letter. It suggests that when SPY closes strong (in the top 10% of its range) but still only manages a small gain on the day, that the next day has a downside tendency. Stats are updated.

SPY closed up < 0.25% but in the top 10% of the daily range. Buy on close. Sell next day's close. \$100k/trade. 1993 - present.			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	(\$10,330.56)	Profit Factor	0.43
Gross Profit	\$7,710.00	Gross Loss	(\$18,040.56)
Total Number of Trades	52	Percent Profitable	36.54%
Winning Trades	19	Losing Trades	33
Even Trades	0		
Avg. Trade Net Profit	(\$198.66)	Ratio Avg. Win:Avg. Loss	0.74
Avg. Winning Trade	\$405.79	Avg. Losing Trade	(\$546.68)
Largest Winning Trade	\$1,093.35	Largest Losing Trade	(\$2,290.72)

As you can see there appears to be a bit of a bearish inclination. Below is a profit curve showing how the edge has played out over time.



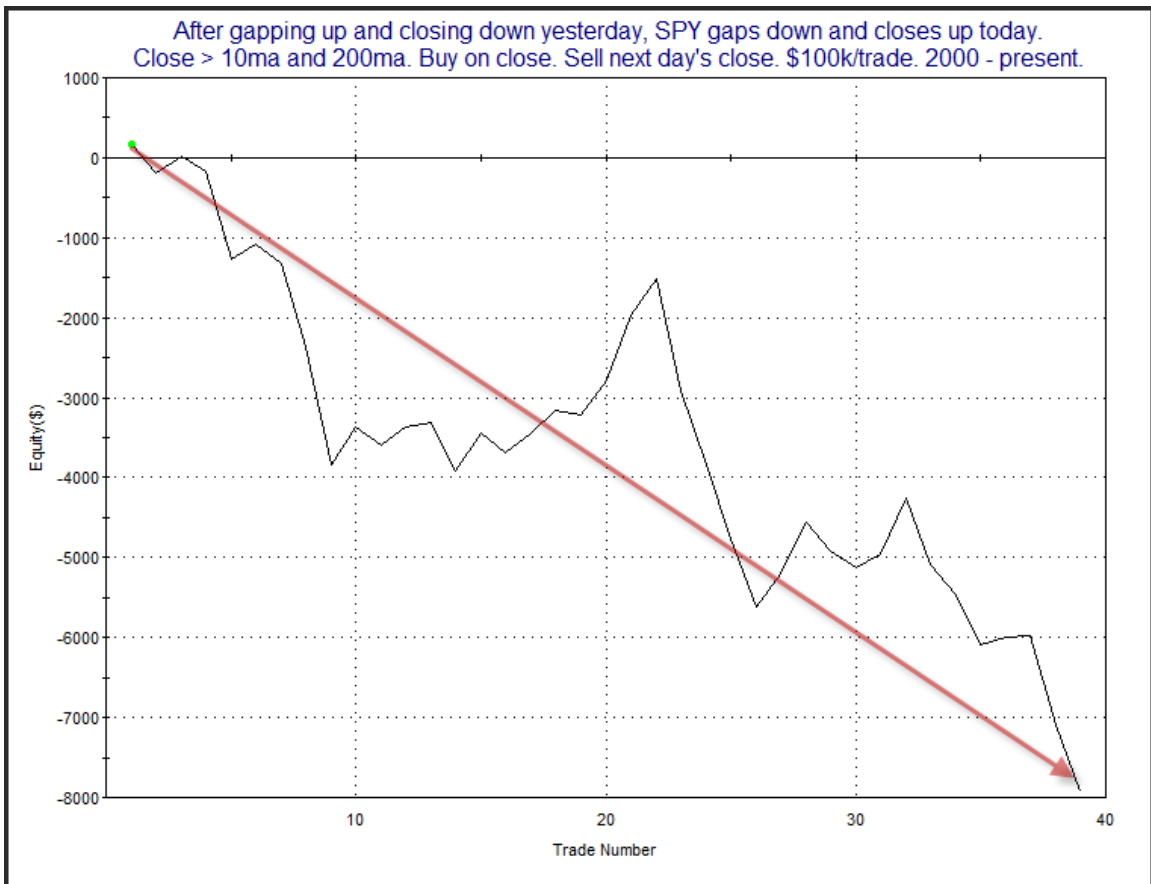
It appears that when the market needs to expend a fair amount of energy just to squeak out a small gain, that its lack of momentum is often followed by a swing back in the opposite direction the next day. The bearish edge here too may be waning a bit, but I have included this study on the Active List for tonight.

Additionally, the way SPY has gapped and reversed the last couple of days is reminiscent of a study I showed in the 3/21/14 letter. I re-ran the stats for that gap and reverse study and posted them below.

After gapping up and closing down yesterday, SPY gaps down and closes up today.
Close > 10ma and 200ma. Buy on close. Sell X days later. \$100k/trade. 2000 - present.

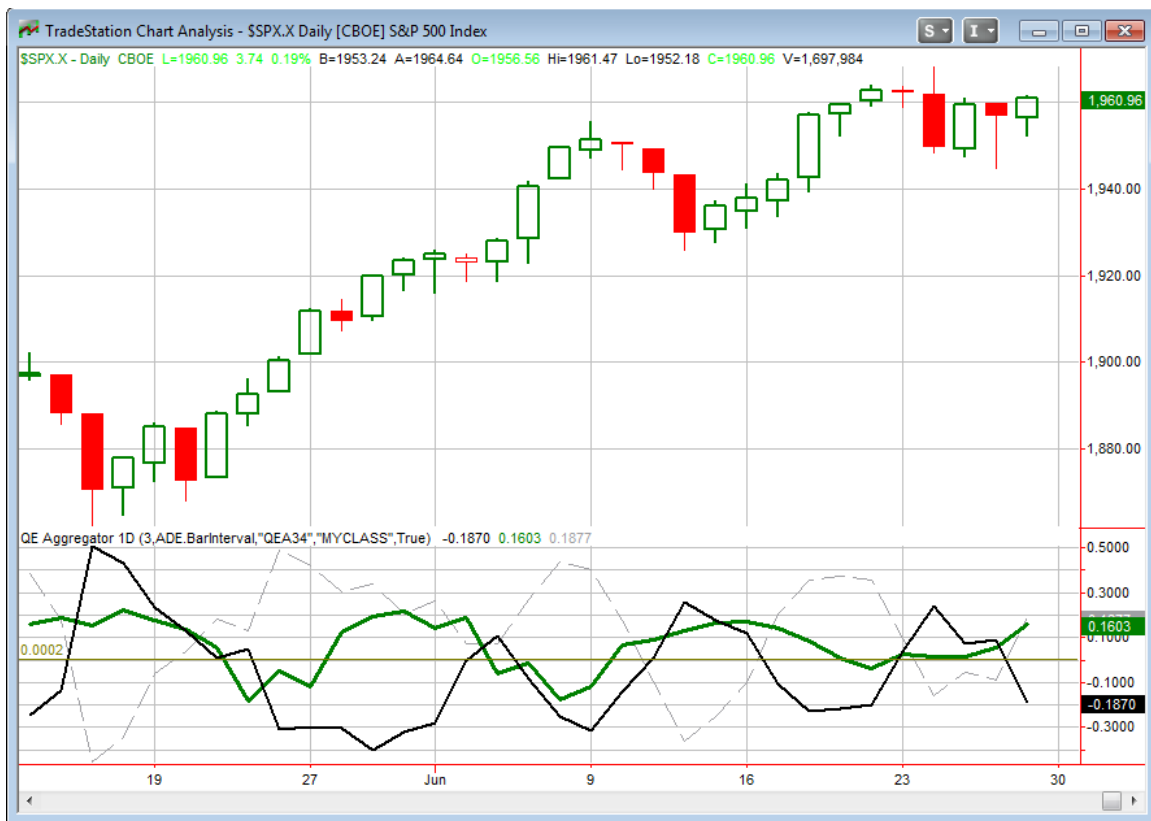
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
5	-7,753.04	35	19	16	54.29	839.20	1,775.87	-1,481.12	-4,262.13	0.57	0.67	-221.52
4	-11,276.96	36	15	21	41.67	878.79	1,803.51	-1,164.70	-3,226.86	0.75	0.54	-313.25
3	-7,881.35	37	16	21	43.24	806.29	1,784.12	-989.62	-2,098.04	0.81	0.62	-213.01
2	-8,635.11	39	17	21	43.59	609.77	1,935.96	-904.82	-3,107.14	0.67	0.55	-221.41
1	-7,918.06	39	18	21	46.15	338.88	805.00	-667.52	-1,485.70	0.51	0.44	-203.03

The edge isn't huge but risk/reward has seemed to favor the bears under these circumstances. Much of the downside has been realized by the end of day 1, so I elected to show the profit curve for that holding period below.



No one would call this a smooth curve, but it does seem to be working its way lower. I decided to include it on the Active List again tonight.

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



Despite the bearish studies tonight the green Aggregator Line actually moved a little further above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line dropped sharply below 0. The negative Differential Line reading means the SPX is overbought versus recent expectations. So expectations are positive but the SPX is now overbought versus expectations. This is considered a neutral configuration. Neutral configurations are visible on the chart whenever both lines close on opposite sides of 0. Therefore the Aggregator signal turned flat at the close.

Based on the current active studies, expectations are slated to remain positive on Monday. Of course this could change if more bearish evidence emerges. The Differential Pivot will be 1960.66 on Monday. That is only 0.3 points below Friday's close. This means SPX will remain overbought on any up close, and will be considered oversold versus expectations on just about any down close on Monday.

So the Aggregator is now neutral. Monday appears as though it could struggle. The studies are making 1-day expectations negative, and the 1-day risk/reward outlook at the top of the letter reflects this. Of course the 3-day is neutral. I took off my index

exposure on Friday and will be awaiting the next favorable risk/reward opportunity before getting positioned in an index trade again.

Intermediate-term Outlook (2 weeks – 2 months) – updated 6/30 – slightly bullish

Quantifiable Edges Market Timing Course Combo Signals Overview

Combo #1	Combo #2	Combo #3
Flat	Long	Long

SPX did not manage a new closing high this past week, but it did manage a new intraday high on Wednesday. So the uptrend certainly appears intact at this point.

I've shown the status of the different Combination Signals from the Quantifiable Edges Market Timing Course above. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), which is included with all annual subscriptions. Detailed descriptions of these combination approaches can be found in [Lesson 8](#). Subscribers may also download detailed hypothetical historical performance reports covering 1/1/71 – 3/7/14 in [Lesson 11, Course Downloads](#). (You must go through the course first in order to access the Downloads.)

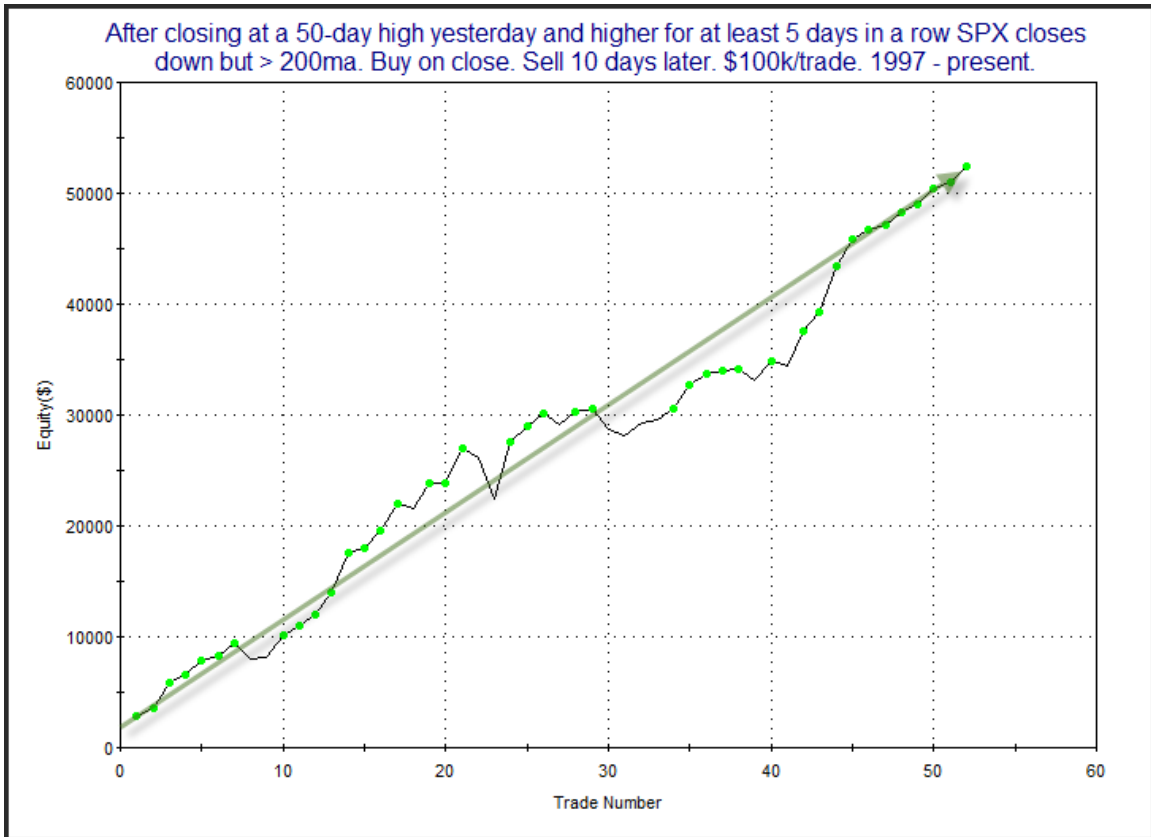
There was one new intermediate-term study that emerged during the week. It was published in the 6/24/14 letter. I have copied it below.

One study that triggered tonight suggested the recent persistent upmove is unlikely to abruptly end. (This is a theme we have seen many times over the years.) It considers what happens after the market moves up at least 5 days in a row to a 50-day high, and then pulls back. It was last seen in the 10/24/13 Letter. I have updated the stats in the table below.

After closing at a 50-day high yesterday and higher for at least 5 days in a row SPX closes down but > 200ma. Buy on close. Sell X days later. \$100k/trade. 1997 - present.

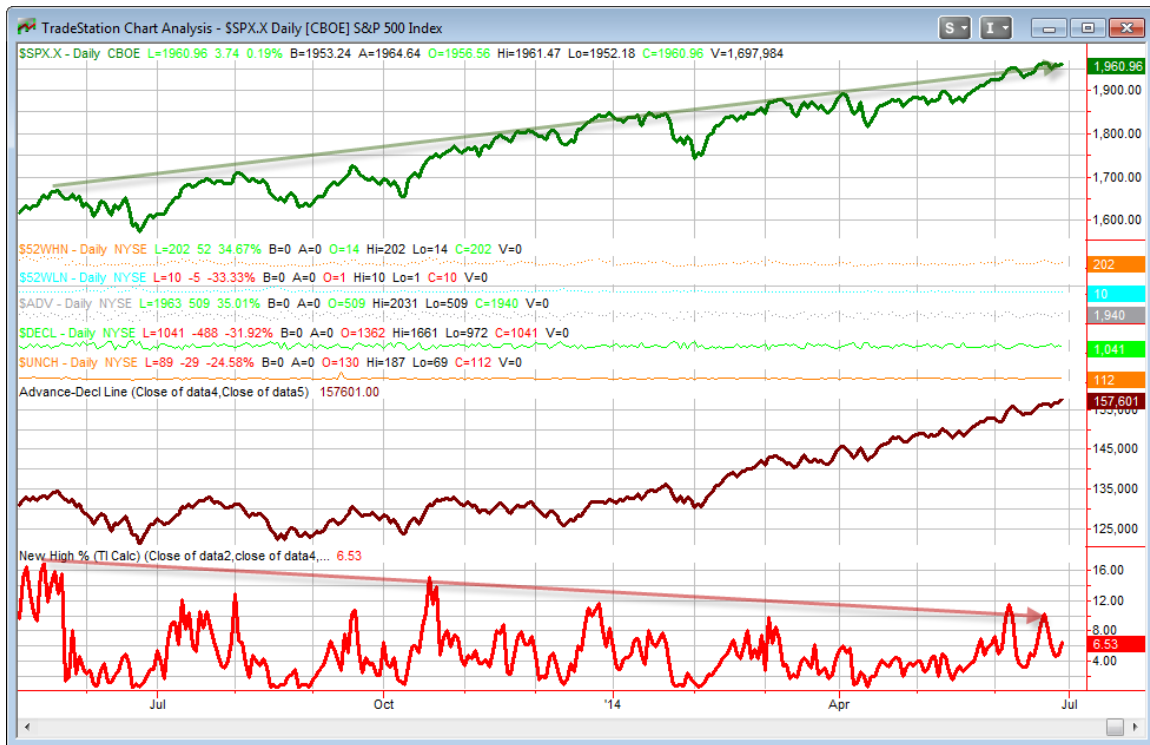
X Days	All: Net Profit	All: Total Trades	All: Winning Trades	All: Losing Trades	All: % Profitable	All: Avg Winning Trade	All: Max Winning Trade	All: Avg Losing Trade	All: Max Losing Trade	All: Win/Loss Ratio	All: ProfitFactor	All: Avg Trade
10	52,396.96	52	43	9	82.69	1,477.76	5,131.35	-1,238.51	-3,672.90	1.19	5.70	1,007.63
9	51,888.62	55	45	10	81.82	1,469.35	5,023.20	-1,423.22	-4,151.40	1.03	4.65	943.43
8	45,708.37	56	39	17	69.64	1,676.24	4,878.08	-1,156.77	-4,874.10	1.45	3.32	816.22
7	36,868.70	57	38	19	66.67	1,538.31	3,874.76	-1,136.15	-3,912.48	1.35	2.71	646.82
6	36,686.11	59	40	19	67.80	1,402.73	4,307.20	-1,022.26	-3,637.71	1.37	2.89	621.80
5	27,561.10	59	37	22	62.71	1,226.99	4,252.50	-810.80	-2,466.75	1.51	2.55	467.14
4	29,631.12	59	37	22	62.71	1,255.34	3,843.00	-764.39	-3,003.39	1.64	2.76	502.22
3	17,624.14	59	38	21	64.41	923.60	2,472.85	-832.03	-1,992.34	1.11	2.01	298.71
2	16,922.86	59	41	18	69.49	782.90	2,437.50	-843.10	-2,614.95	0.93	2.12	286.83
1	9,894.53	59	38	20	64.41	540.59	1,751.19	-532.39	-1,744.10	1.02	1.93	167.70

We see here a decent edge that becomes stronger and more consistent as you look out over the next several days. The 9-10 day time frame shows exceptional stats. The 2-day timeframe suggests a quick little boost is also likely. Let's take a look below at the 10-day profit curve.



The strong upslope appears to confirm the bullish edge.

Despite the new highs this week, the number of stocks hitting new 52-week highs did not expand. It also remained substantially below the peak seen in May 2013. This divergence is still a bit of a concern. The chart below can also be found on the QE charts page.

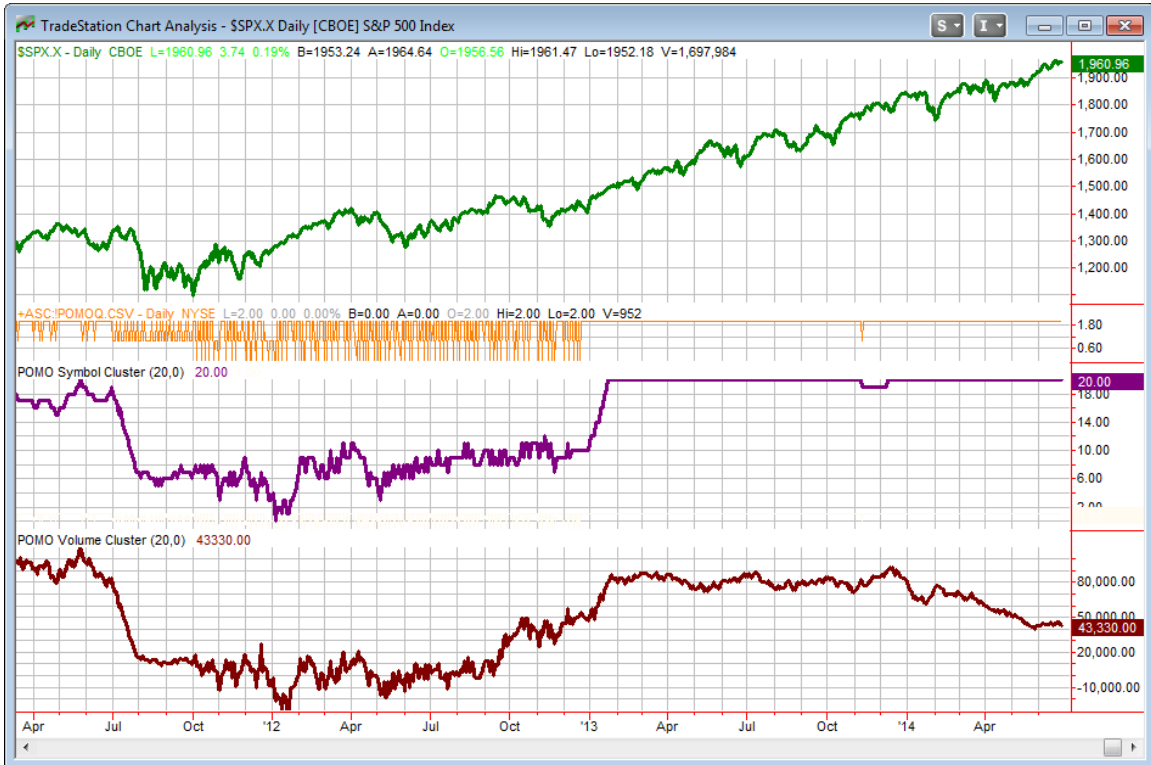


Subscribers that would like more info on this chart should check out the Study of Tops (available for Gold & Silver subscribers on the special reports downloads page). Until this divergence is resolved with new highs increasing beyond the May 2013 level, the market remains at risk of topping out. If the divergence is resolved, then it would be highly unlikely that the market would top out and begin a major decline any time in the next couple of months.

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 days indicator is still riding along at 20, where it spent most of 2013 and 2014 so far. The volume indicator is about where it was the last couple of weeks. With July about to start we should see this indicator begin dipping lower. We estimate net inflows this past week to have been about \$11 billion. That was about average for June. To this point the reduced liquidity has still been positive enough to provide a decent wind at the market's back.

Monday we will get to see the Fed's buying schedule for July. While we already know the total purchases should be about \$35 billion, the release of the schedule will allow us to see the daily amounts, and how those purchases are going to be laid out throughout the month. This will allow up to post the QE Buying Power Index for July to the QE Buying Power Index Information Page. I discussed Fed-based liquidity in some detail last week. Subscribers may refer to last week's letter for a longer discussion.

Overall, liquidity remains positive but is becoming more and more concerning and the Fed continues to taper. The leading NASDAQ is providing a plus, and the uptrend is certainly intact. The pullback study from the 6/24 letter is providing more upside evidence. So the bulls have a fair amount in their favor. The bears are banking on the shrinking New High % divergence and the weak seasonality (and at some point in the next few months the lack of Fed stimulus.) I am keeping my outlook at slightly bullish this week. I will continue to trade longs a bit more aggressively than shorts for the time being.

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

New

PM – 1/3 @ \$84.85 Limit

Catapult for ETF's Trades

None

Broad Market Large Cap CBI – 1(PM)

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.

PM – Buy 1/3 Catapult position @ \$84.85 limit. This is from the Catapult section above. Catapults have been strong performers over the years, but have also been very volatile. More information on Catapults, including a detailed webinar, can be found on the Catapult System page in the members area of Quantifiable Edges. <http://quantifiableedges.com/catapult-system/>

Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
<i>SPY(1/4)</i>	<i>6/25/2014</i>	<i>\$194.25</i>	<i>\$194.97</i>	<i>0.37%</i>		<i>stopped out intraday</i>

SPY was exited on a stop equal to the low of the 1st 1/2 hour of the day per the instructions in the 6/27/14 letter.

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