

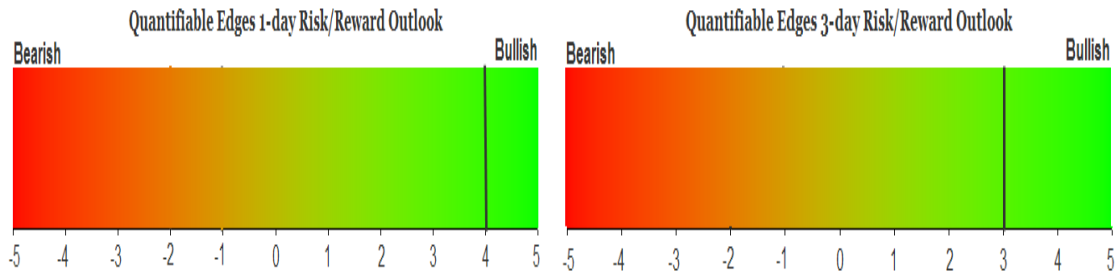
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 2, 2015

Volume 8 Issue 21

## Market Overview



## Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing
Long	100% Long XIV	Flat

## Tonight's Research Points

- During uptrends, moves down at the end of the month will often lead to a move up on the 1<sup>st</sup> day of the new month.
- The January Barometer shows that years with a poor January have been inconsistent the remainder of the year.
- SOMA shrunk for the 2<sup>nd</sup> week in a row – a potential intermediate-term negative.

## *Short-term Outlook*

### *The Bottom Line*

Evidence is still leaning bullish and the market remains short-term oversold. I am partially long and looking to get longer.

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

Study Date	Description	Time span	Bias	Avg Run-up	Avg DrawDn	Avg DrawDn - 1 Std Dev
<b>Active - Short Term</b>						
February 2, 2015	Selloff at end of month	1 day	Bullish			
January 29, 2015	Fed Day. SPY dwn 2 in row.	1-6 days	Bullish			
January 29, 2015	Dn 2% from high on Fed Day	1-4 days	Bullish			
January 23, 2015	VIX 10% up to 10% dn blow ma	1-8 days	Bullish	2.50%	-1.00%	-1.95%
<b>Active - Long Term</b>						
January 26, 2015	NASDAQ leading SPX	int term	Bullish			
November 3, 2014	Best 6 Months	6 months	Bullish			
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
February 1, 2012	Golden Cross	int term	Bullish			

**The Evidence**

The market had a tough day on Friday. The SPX declined 1.3%, the NASDAQ lost 1.0%, and the Russell 2000 fell 2.1%. Breadth was negative as the NYSE Up Issues % came in at 32% and the Up Volume % was 26%. Total NYSE volume spiked higher as traders seemed to be panic selling as the day came to a close.

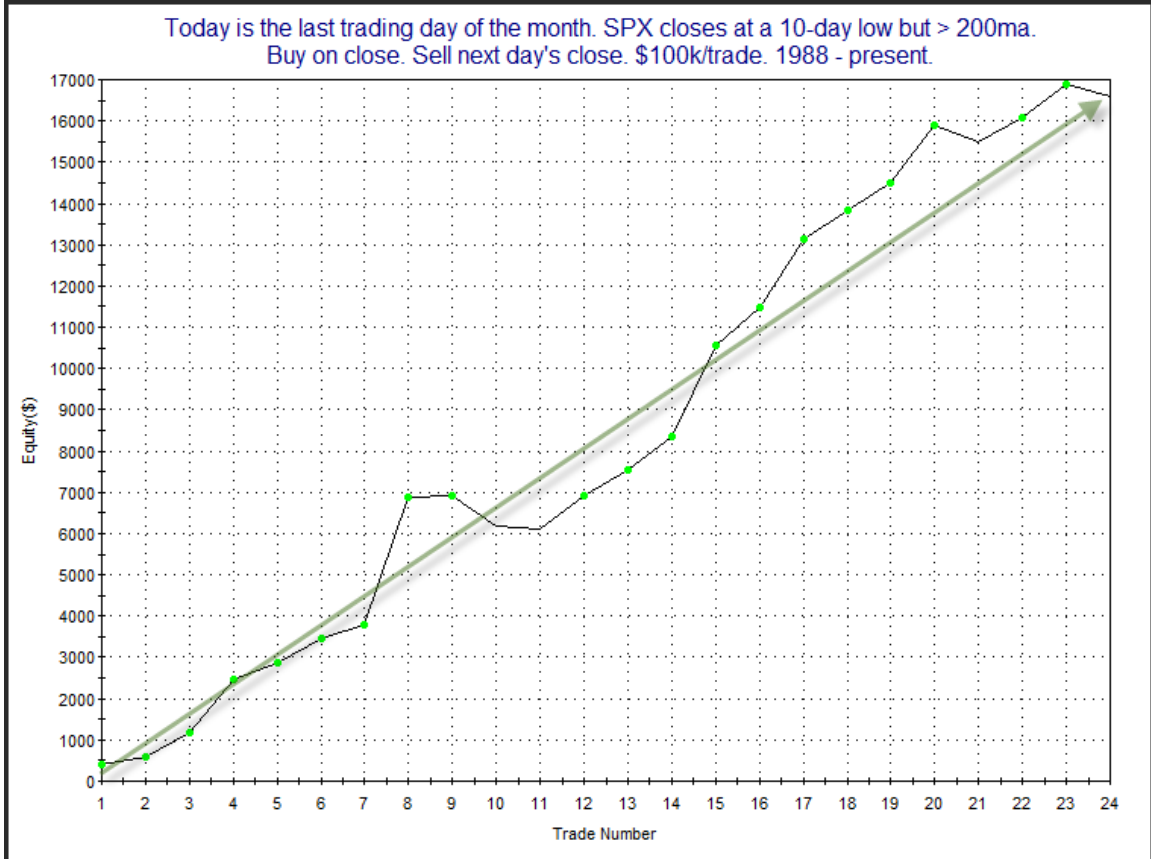
A good number of studies triggered in the Quantifinder, and most of them were related to the turn of the month. Since the late eighties (and the popularization of 401(k) plans) the 1<sup>st</sup> trading day of the month has had a strong propensity to rise. This edge has primarily exerted itself during bull markets. But over the last few years there has been deterioration in this “1<sup>st</sup> day of month” bullishness. I discussed this in Thursday night’s letter and also [in the blog on Friday](#). The bullish tendency has been well documented over the years and it is not a well-kept secret. Because of this it is unusual to see such a strong selloff to close out the month. But when months have ended poorly, that’s made the Day 1 upside edge even stronger. And the studies I examined tonight aren’t showing the same level of deterioration that has appeared otherwise over the last 4 years. So let’s review the ones I consider the most compelling.

This 1<sup>st</sup> study is from the 8/1/14 letter. It examines instances where SPX closes at a 10-day low, but above the 200ma on the last day of the month.

Today is the last trading day of the month. SPX closes at a 10-day low but > 200ma.  
Buy on close. Sell next day's close. \$100k/trade. 1988 - present.

TradeStation Performance Summary				Collapse 
<b>All Trades</b>				
Total Net Profit	\$16,603.97	Profit Factor	12.26	
Gross Profit	\$18,078.50	Gross Loss	(\$1,474.53)	
Total Number of Trades	24	Percent Profitable	83.33%	
Winning Trades	20	Losing Trades	4	
Even Trades	0			
Avg. Trade Net Profit	\$691.83	Ratio Avg. Win:Avg. Loss	2.45	
Avg. Winning Trade	\$903.93	Avg. Losing Trade	(\$368.63)	
Largest Winning Trade	\$3,119.10	Largest Losing Trade	(\$731.58)	

The numbers here are all very strong. It's interesting that over the last 27 years there have only been 24 prior instances, which speaks again to the fact that months rarely end so poorly. Not only did 83% of the instances close up the next day, but the winning days were more than twice the size of the losing days. Below is a profit curve showing how it has played out over time.



The nice, steady rise is impressive. And while the August instance did not play out, it hardly impacted the curve. This study seems well worth consideration.

This next study was seen just a month ago in the 1/2/15 letter. It looked at times the SPX dropped at least 1% on the last day of the month and closed above its 200ma.

Today is the last trading day of the month. SPX closes down > 1% but > 200ma.  
Buy on close. Sell next day's close. \$100k/trade. 1988 - present.

TradeStation Performance Summary <span style="float: right;">Collapse ^</span>			
All Trades			
Total Net Profit	\$8,850.66	Profit Factor	6.70
Gross Profit	\$10,403.61	Gross Loss	(\$1,552.95)
Total Number of Trades	15	Percent Profitable	73.33%
Winning Trades	11	Losing Trades	4
Even Trades	0		
Avg. Trade Net Profit	\$590.04	Ratio Avg. Win:Avg. Loss	2.44
Avg. Winning Trade	\$945.78	Avg. Losing Trade	(\$388.24)
Largest Winning Trade	\$2,225.00	Largest Losing Trade	(\$731.58)

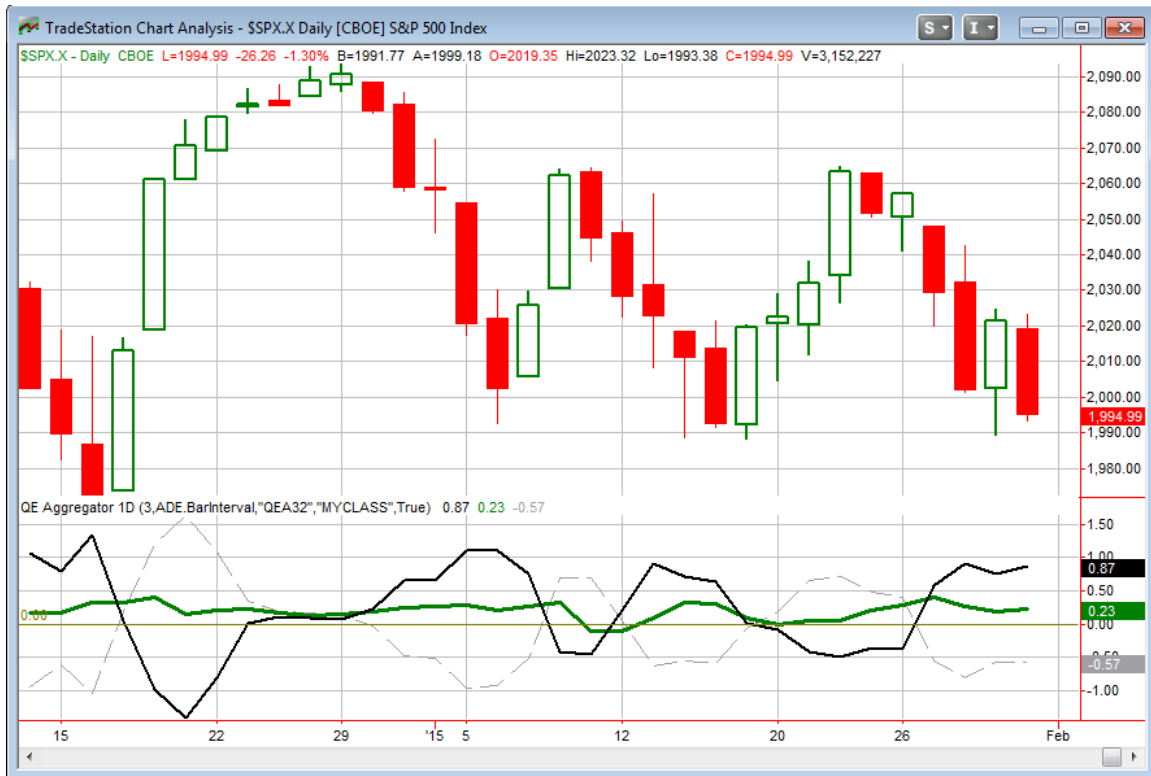
Though the number of instances is low the results again appear bullish. Below is the full list of instances.

Today is the last trading day of the month. SPX closes down > 1% but > 200ma.  
Buy on close. Sell next day's close. \$100k/trade. 1988 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
12/31/96	Buy	\$740.74	(0.51%)	\$279.45
01/02/97	Sell	\$736.99		(\$1,510.65)
03/31/97	Buy	\$757.12	0.33%	\$576.84
04/01/97	Sell	\$759.64		(\$773.52)
07/31/98	Buy	\$1,120.66	(0.73%)	\$99.68
08/03/98	Sell	\$1,112.44		(\$914.92)
11/30/98	Buy	\$1,163.62	1.00%	\$1,042.10
12/01/98	Sell	\$1,175.28		(\$1,132.20)
03/31/99	Buy	\$1,286.37	0.57%	\$621.39
04/01/99	Sell	\$1,293.72		(\$282.59)
11/30/99	Buy	\$1,389.07	0.62%	\$784.55
12/01/99	Sell	\$1,397.72		(\$119.99)
09/30/03	Buy	\$995.97	2.23%	\$2,225.00
10/01/03	Sell	\$1,018.22		\$0.00
02/28/06	Buy	\$1,280.66	0.83%	\$868.92
03/01/06	Sell	\$1,291.24		\$0.00
07/31/07	Buy	\$1,455.27	0.72%	\$891.48
08/01/07	Sell	\$1,465.81		(\$1,066.24)
10/30/09	Buy	\$1,036.19	0.65%	\$1,535.04
11/02/09	Sell	\$1,042.88		(\$653.76)
12/31/09	Buy	\$1,115.10	1.60%	\$1,670.53
01/04/10	Sell	\$1,132.99		\$0.00
04/30/10	Buy	\$1,186.69	1.31%	\$1,548.96
05/03/10	Sell	\$1,202.26		\$0.00
05/31/13	Buy	\$1,630.74	0.59%	\$590.48
06/03/13	Sell	\$1,640.42		(\$489.22)
07/31/14	Buy	\$1,930.67	(0.29%)	\$340.68
08/01/14	Sell	\$1,925.15		(\$729.30)
12/31/14	Buy	\$2,058.90	(0.03%)	\$646.08
01/02/15	Sell	\$2,058.20		(\$617.28)

Both August and January saw slight declines. Prior to that this setup had been on a real hot streak. To me it still seems worthy of consideration. One strong gain and this one will be right back on track.

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



Once again tonight the green Aggregator Line held strongly above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line also remained above 0. The positive Differential Line reading means the SPX is oversold versus recent expectations. So expectations are positive and the SPX is oversold. This is considered a bullish configuration. Bullish configurations are visible on the chart whenever both lines close above 0. Therefore the Aggregator signal stayed long at the close.

Based on the current active studies, expectations are set to remain bullish on Monday. That could change if compelling bearish evidence emerges. The Differential Pivot will be 2021.23 on Monday. That is 1.3% above Friday's close. This means that in order for the Differential Line to cross below 0 (signaling SPX moving from "oversold" to "overbought") it would need to close up at least 1.3% on Monday. That would be a pretty strong 1-day move.

All of the short-term studies remain bullish. They represent a combination of price action, seasonality, and VIX-based sentiment. The market is also oversold. Currently I am partially long an index position and I will be looking to add to that position if I can get a favorable fill on Monday. Odds here certainly suggest a bounce, but it is not a sure thing (it never is). I would prefer to see the CBI above 0. And since the end of the Fed's QE program, we have certainly seen selloffs become more volatile. So I will continue to

wade into this position slowly, keeping some ammunition ready in case the selling kicks in harder.

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

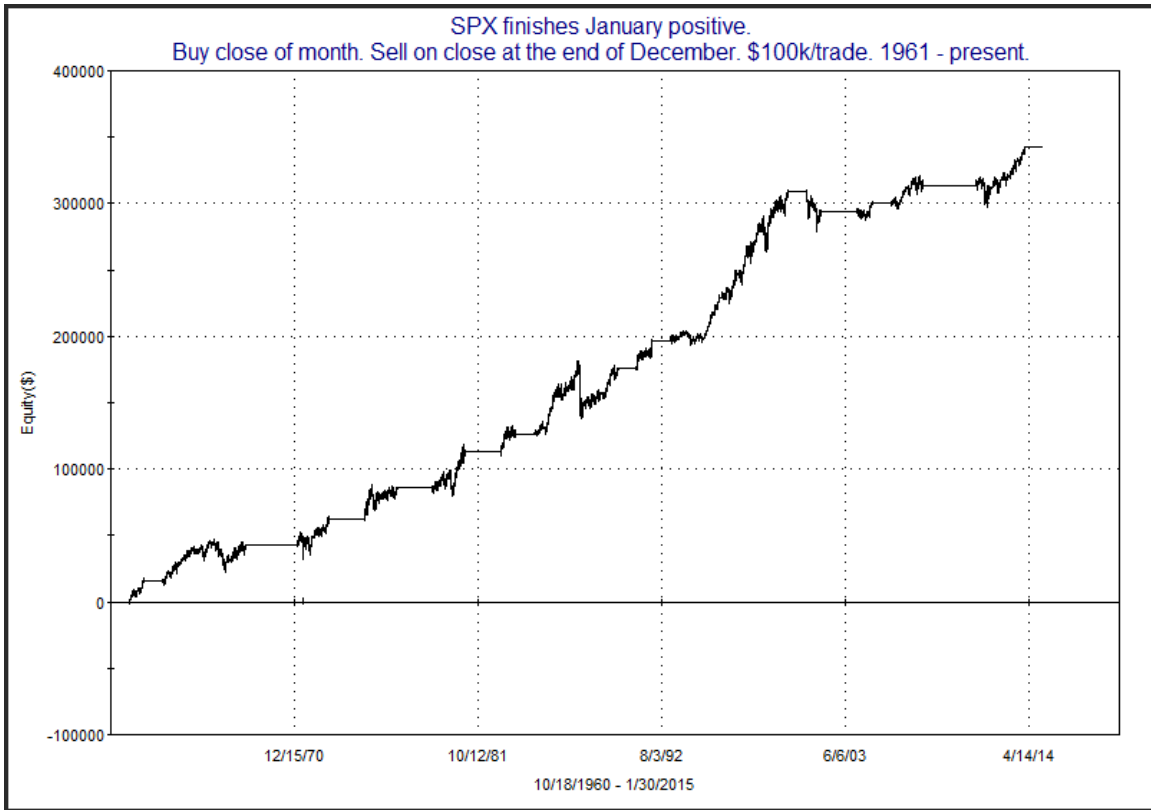
Combo #1	Combo #2	Combo #3
Long	Long	Long

Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. 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 12/31/71 – 3/7/14 in [Lesson 11, Course Downloads](#). (You must go through the course first in order to access the Downloads.)

The January Barometer is a fairly famous study from the Stock Traders Almanac. It says that “as goes January, so goes the year”. In other words, a positive January will typically lead to a positive year, while a negative January can be a warning. So, as I did in the 2/3/14 letter, let’s look at how the SPX has done for the remaining 11 months of the year based on how January performed.

SPX finishes January positive. Buy close of month. Sell on close at the end of December. \$100k/trade. 1961 - present.			
TradeStation Performance Summary			Collapse ^
All Trades			
Total Net Profit	\$343,009.51	Profit Factor	8.45
Gross Profit	\$389,070.62	Gross Loss	(\$46,061.11)
Total Number of Trades	33	Percent Profitable	84.85%
Winning Trades	28	Losing Trades	5
Even Trades	0		
Avg. Trade Net Profit	\$10,394.23	Ratio Avg. Win:Avg. Loss	1.51
Avg. Winning Trade	\$13,895.38	Avg. Losing Trade	(\$9,212.22)
Largest Winning Trade	\$30,848.12	Largest Losing Trade	(\$15,908.89)

The numbers show that in years that January has done well, the rest of the year has typically fared well also. Below is a profit curve.



That is a nicely steady upslope. Now let's look at how Feb-Dec has done after a down January.

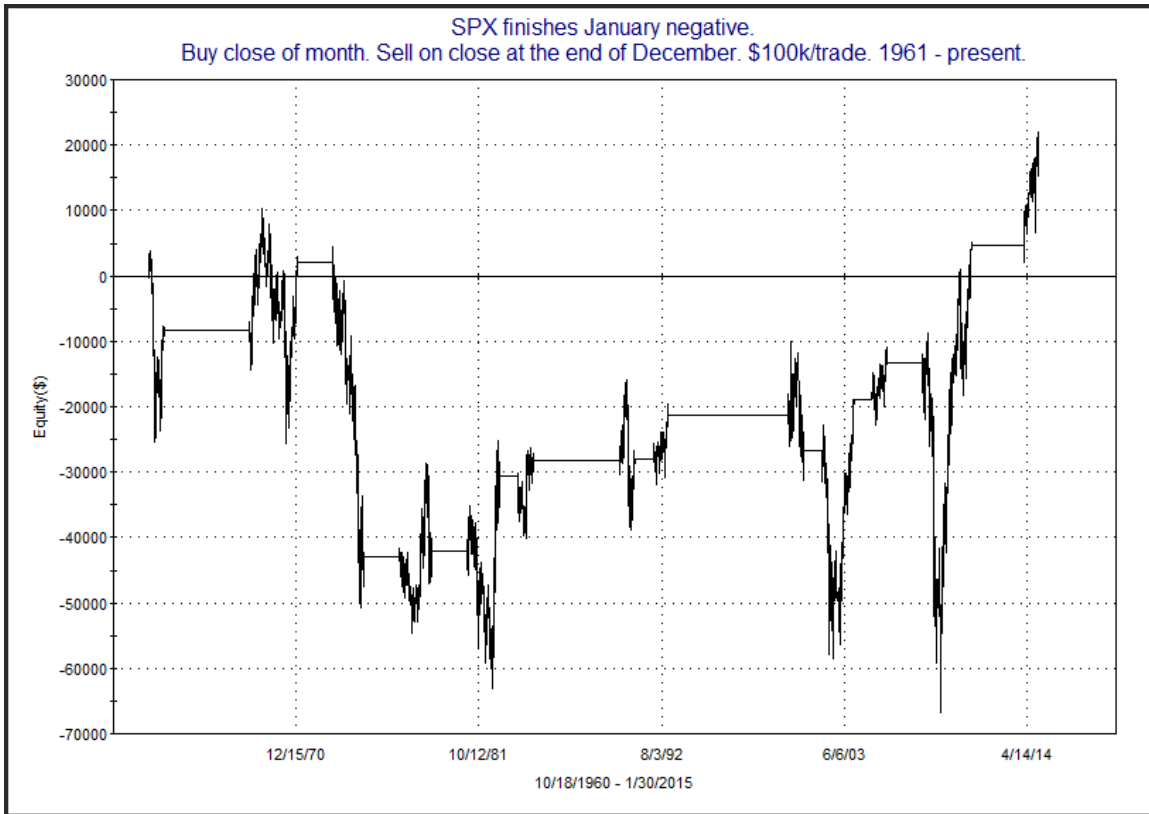
SPX finishes January negative.  
Buy close of month. Sell on close at the end of December. \$100k/trade. 1961 - present.

**TradeStation Performance Summary** Collapse ↕

All Trades

Total Net Profit	\$20,057.05	Profit Factor	1.15
Gross Profit	\$157,627.35	Gross Loss	(\$137,570.30)
Total Number of Trades	21	Percent Profitable	57.14%
Winning Trades	12	Losing Trades	9
Even Trades	0		
Avg. Trade Net Profit	\$955.10	Ratio Avg. Win:Avg. Loss	0.86
Avg. Winning Trade	\$13,135.61	Avg. Losing Trade	(\$15,285.59)
Largest Winning Trade	\$34,995.62	Largest Losing Trade	(\$34,208.64)

Not as many instances, but there does not appear to be the same kind of bullish tendency here. More of a crapshoot. Below is a curve.

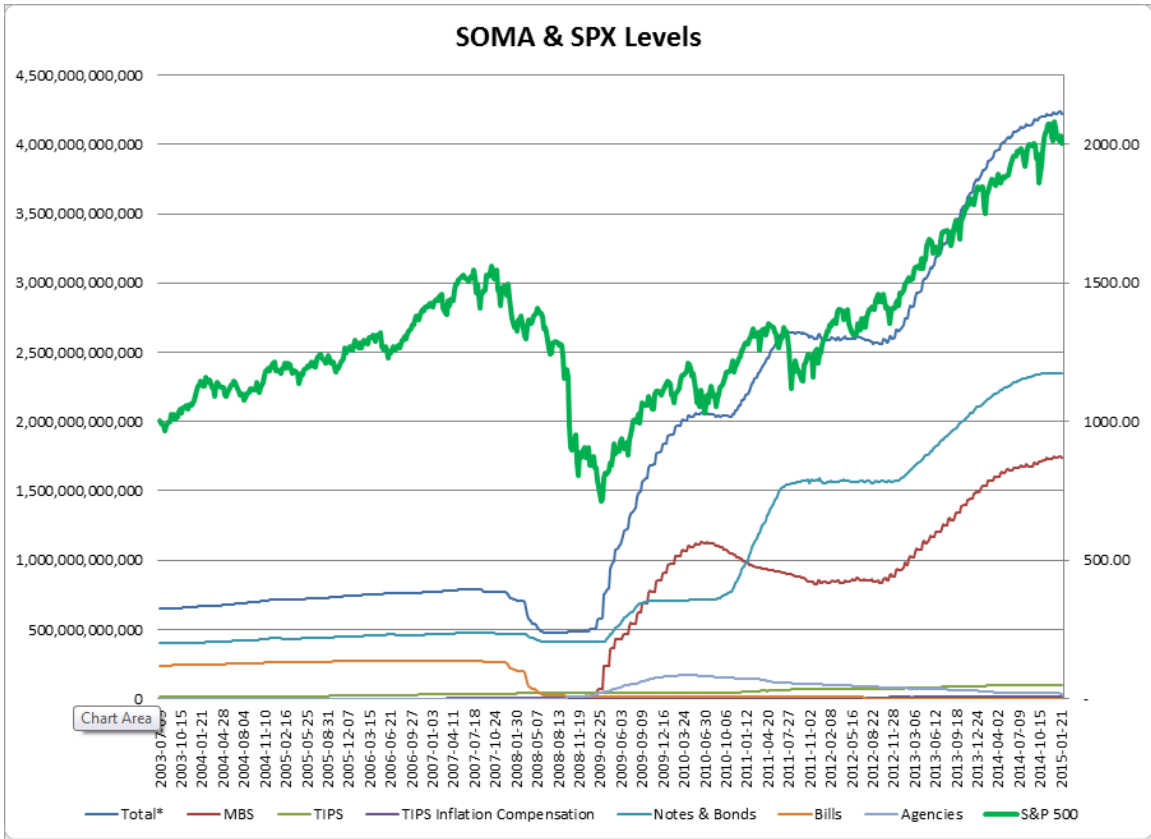


Certainly not a chart to trade off of. So it would have been nice if January finished positive. But it is not a sign of impending doom. Just that we don't have the kind of momentum that would be preferable.

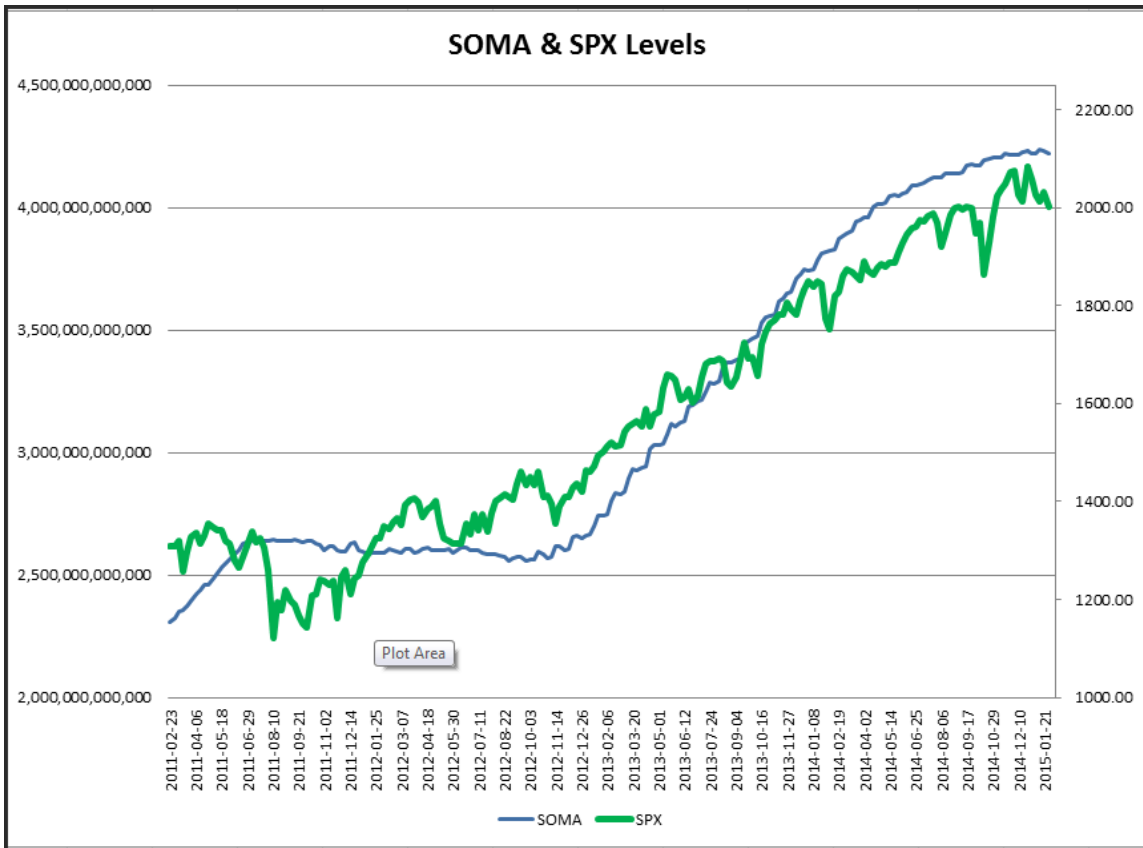
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

*SOMA stands for System Open Market Account. It is the account at the Fed that contains all of its bond purchase holdings. We have tracked Fed purchases for several years, and as is evident in the charts below, the stock market has consistently reacted positively when the Fed has been buying securities in the open market and increasing the size of its account. When the account has declined, the market has struggled. The obvious takeaway has been "don't fight the Fed". As far as intermediate-term indicators go, this has been as good as anything in recent years.*

*While the Fed is not making new QE purchases any longer, it is continuing to reinvest maturities. Therefore, the total assets in their System Open Market Account (SOMA) has not begun to dive like the old Quantifiable Edges POMO indicators did. Below are long and short-term views of SOMA and SPX. First, the long-term view (back to 2003).*



And now the zoomed-in view (2011 – present).



This was the 2<sup>nd</sup> week in a row in which we saw a decline in SOMA. Since quantitative easing ended in October the market has seen much choppier action, with more pronounced downmoves than we saw during QE. The liquidity support is just not what it was. Still, up until a couple of weeks ago the small SOMA increases seemed to provide enough support to allow the SPX rally to continue. A declining SOMA could be a difficult obstacle for the market to overcome, and could lead to some substantial selling. It will be important to see if the blue line representing SOMA levels can work its way higher, or if the recent decline continues.

The January Barometer was a little bit of a wet rag this week, and the declining SOMA is somewhat concerning. But NASDAQ leadership, the long-term trend, and favorable seasonality all continue to favor the bulls. The bears are still banking on potential breadth and liquidity issues. I am keeping my outlook at “somewhat bullish” this week. I still would need to see further price breakdowns in order to move to bearish. At this point I will continue to trade longs a bit more aggressively than shorts.

## 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.

**SPY – buy ¼ index position @ \$199.44 LIMIT ON OPEN. If NOT filled on open, then cancel order and look to buy @ \$199.44 LIMIT ON CLOSE.** Based on the short-term outlook above. I will look to buy into any gap down on Monday. But if the market does not gap down and offer a “bargain”, I will sit out until the close. An intraday selloff could get ugly and I would rather take my entry at 4pm EST than to get run over in an intraday stampede.

## Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
XIV(1/2)	12/11/2014	\$34.03	\$24.97	-26.62%		Aggressive VIX
SPY(1/4)	1/29/2015	\$200.14	\$199.45	-0.34%		Aggregator

This report has been prepared by Hanna Capital Management, LLC and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy securities. While information contained herein is believed to be accurate at the time of publication, we make no representation as to the accuracy or completeness of any data, studies, or opinions expressed and it should not be relied upon as such. Robert Hanna, Hanna Capital Management, LLC or clients of Hanna Capital Management, LLC may have positions or other interests in securities (including derivatives) directly or indirectly which are the subject of this report. This report is provided solely for the information of Hanna Capital Management, LLC clients and prospects who are expected to make their own investment decisions without reliance upon this report. Neither Hanna Capital Management, LLC nor any officer or employee of Hanna Capital Management, LLC accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. This report may not be reproduced, distributed or published by any recipient for any purpose without the prior express consent of Hanna Capital Management, LLC.

Copyright © 2015 Hanna Capital Management, LLC.