

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

March 2, 2015

Volume 8 Issue 40

Market Overview



Signals Overview

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

Tonight's Research Points

- 3 down days from a 50-day high that closes < 10ma but above 10-day low suggest an upside edge.
- The 1st drop below the 10ma after an extended period above it is often short-term buyable.
- 3 days down into the end of the month during uptrends has commonly been followed by a strong start to the next month.

Short-term Outlook

The Bottom Line

Expectations have turned positive and the market is now a bit oversold. This leaves the Aggregator bullish and me looking to start taking on some long exposure.

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
Active - Short Term						
March 2, 2015	Dn 3 > 200 end of month	1-5 days	Bullish	2.50%	-1.10%	-3.30%
March 2, 2015	15 day > 10ma. Now below. > 200ma	1-3 days	Bullish	1.20%	-0.80%	-1.60%
March 2, 2015	Dn 3 > from 50-high. < 10ma but > 10-l	1-4 days	Bullish	1.40%	-1.20%	-2.40%
February 24, 2015	WR10 up then NR10 low vol	1-5 days	Bearish			
Active - Long Term						
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			
Dropped Tonight						
February 23, 2015	SPX up 1-2% opex week	1-5 days	Bearish	-1.40%	0.80%	1.60%

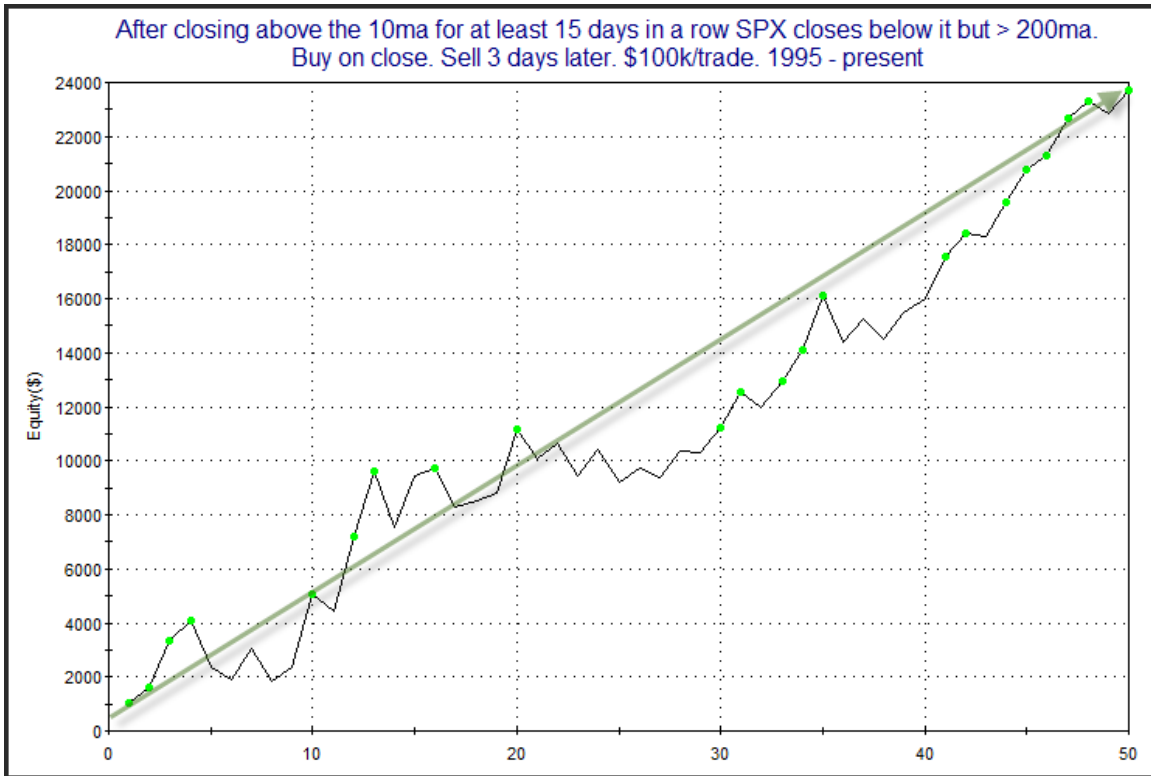
The Evidence

Friday was a weak end to the month. The SPX declined 0.3%, and the NASDAQ and Russell 2000 each lost 0.5%. Breadth was actually mixed though as the NYSE Up Issues % came in at 51% and the Up Volume % was 46%. Total NYSE volume rose for the 4th day in a row.

After having closed above its 10-day moving average for 17 days in a row, SPX finally managed to close below it on Friday. In the 3/14/14 letter I looked at other instances where SPX closed below its 10ma after having spent at least 15 days above it. I have updated that study below.

After closing above the 10ma for at least 15 days in a row SPX closes below it but > 200ma. Buy on close. Sell X days later. \$100k/trade. 1995 - 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	30,653.96	50	31	19	62.00	1,531.52	3,505.74	-885.44	-2,959.70	1.73	2.82	613.08
4	30,252.77	50	34	16	68.00	1,402.98	3,206.40	-1,090.53	-3,078.40	1.29	2.73	605.06
3	23,731.60	50	34	16	68.00	1,140.86	2,805.12	-941.10	-2,062.10	1.21	2.58	474.63
2	14,483.45	50	31	19	62.00	1,070.61	2,682.72	-984.49	-2,185.60	1.09	1.77	289.67
1	13,466.54	50	30	20	60.00	756.26	2,097.92	-461.07	-1,542.24	1.64	2.46	269.33
88% of instances closed above the entry price at some point in the next week.												

The numbers here all look solidly bullish over the next week. I highlighted the 3-day holding period because it had a more appealing equity curve than the four or five-day. You can see its profit curve below.



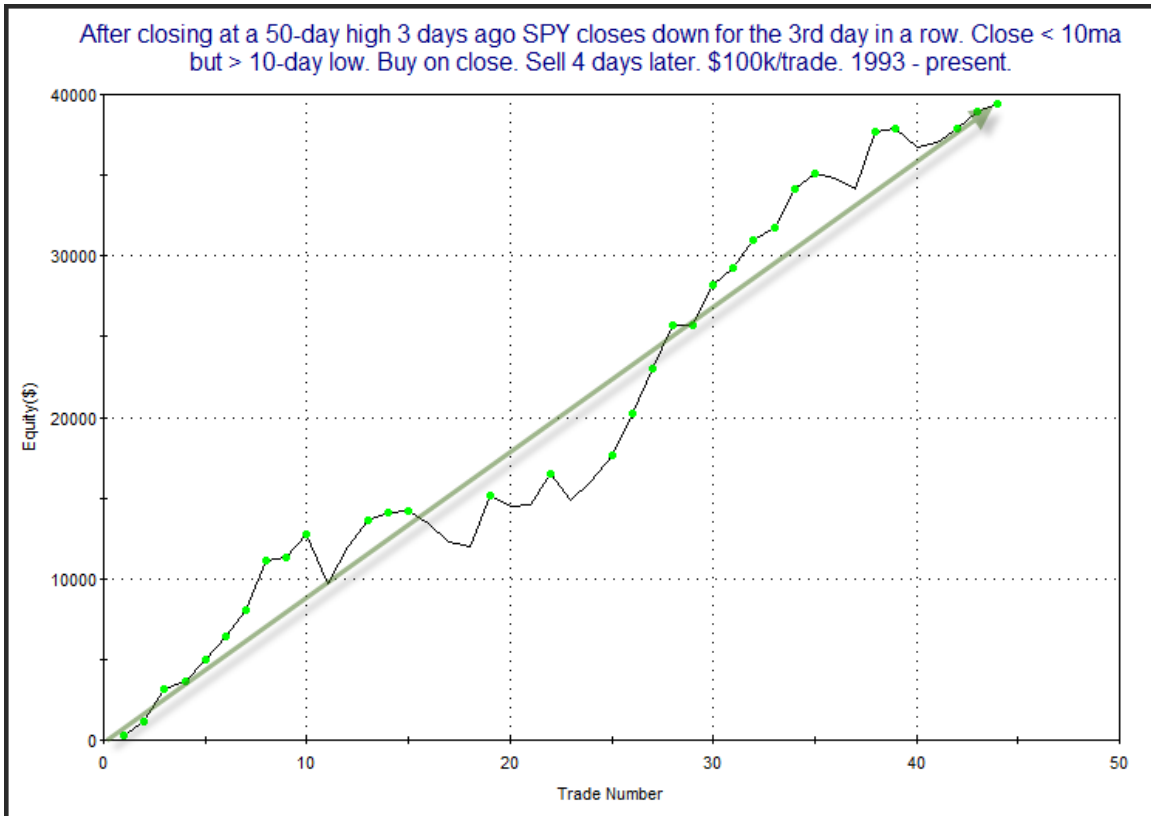
The strong upslope serves as some confirmation of the bullish edge.

Monday marked the 3rd close lower in a row for SPY. Three-day pullbacks will often trigger a few bullish studies. I found the one below especially compelling because it also considered the fact that the 3-day pullback was occurring right after a high was hit. Additionally, it required that the pullback was deep enough to put it below the 10ma, but *not* deep enough to see it at a 10-day closing low. It was last seen in the 9/24/13 subscriber letter, and I have updated the stats.

After closing at a 50-day high 3 days ago SPY closes down for the 3rd day in a row. Close < 10ma but > 10-day low. 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
10	51,051.32	43	30	13	69.77	2,469.10	7,242.70	-1,770.89	-6,933.13	1.39	3.22	1,187.24
9	41,937.92	43	31	12	72.09	2,220.26	6,322.56	-2,240.85	-8,192.92	0.99	2.56	975.30
8	45,851.55	43	32	11	74.42	2,145.08	6,358.08	-2,071.90	-4,499.25	1.04	3.01	1,066.32
7	40,761.14	43	31	12	72.09	2,041.95	6,322.56	-1,878.28	-4,354.31	1.09	2.81	947.93
6	42,727.80	43	31	12	72.09	1,929.28	5,375.36	-1,423.32	-2,140.14	1.36	3.50	993.67
5	34,744.37	44	30	14	68.18	1,660.93	3,522.94	-1,077.39	-3,453.71	1.54	3.30	789.64
4	39,431.65	44	35	9	79.55	1,400.26	3,543.50	-1,064.14	-3,076.63	1.32	5.12	896.17
3	27,149.44	44	31	13	70.45	1,298.34	3,543.50	-1,007.63	-2,027.68	1.29	3.07	617.03
2	12,732.71	44	29	15	65.91	982.97	2,332.48	-1,051.55	-2,781.35	0.93	1.81	289.38
1	9,526.77	44	28	16	63.64	783.81	2,060.16	-776.25	-2,031.09	1.01	1.77	216.52

Under these circumstances, it appears bounces have been both reliable and powerful. While much of the edge was realized in the first 4 days, there does seem to be some follow through as far out as 2 weeks. Below is a look at the profit curve assuming a 4-day exit technique.



The curve appears to provide confirmation of the bullish tendency suggested by the stats table.

It is also notable that the 3 lower closes has occurred going in to the end of the month. I noted recently that the first trading day of the month on its own has not been as strong in recent years. But pullbacks into month-end still look very compelling. There were a number of studies that appeared in the Quantifinder that suggested this. I thought the 3-day pullback one below had the most appeal. I haven't shown it in the letter since 2/1/12, but decided to update it here.

**SPX closes down for at least the 3rd day in a row. It closes > 200ma. It is the last day of the month.
Buy on close. Sell X days later. \$100k/trade. 12/31/86 - 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	26,260.70	16	13	3	81.25	2,786.39	9,607.84	-3,320.80	-8,737.19	0.84	3.64	1,641.29
9	26,851.34	16	12	4	75.00	3,124.14	8,433.64	-2,659.57	-9,212.28	1.17	3.52	1,678.21
8	19,915.55	16	13	3	81.25	2,657.06	7,325.36	-4,875.43	-13,207.04	0.54	2.36	1,244.72
7	23,756.06	16	13	3	81.25	2,622.94	7,473.68	-3,447.40	-9,220.75	0.76	3.30	1,484.75
6	14,880.72	16	13	3	81.25	2,390.63	6,822.72	-5,399.15	-13,307.14	0.44	1.92	930.05
5	21,089.56	16	14	2	87.50	2,072.31	6,229.44	-3,961.40	-7,153.30	0.52	3.66	1,318.10
4	16,314.75	16	14	2	87.50	1,689.04	5,426.04	-3,665.90	-7,100.17	0.46	3.23	1,019.67
3	18,323.53	16	12	4	75.00	1,936.34	4,371.32	-1,228.15	-2,459.38	1.58	4.73	1,145.22
2	11,249.11	16	12	4	75.00	1,296.00	4,132.36	-1,075.73	-2,943.71	1.20	3.61	703.07
1	9,878.53	16	13	3	81.25	821.50	2,143.68	-266.97	-411.18	3.08	13.33	617.41

The only instance NOT to close above the entry price at some point in the next 4 days was was the most recent one in the beginning of August 2011.

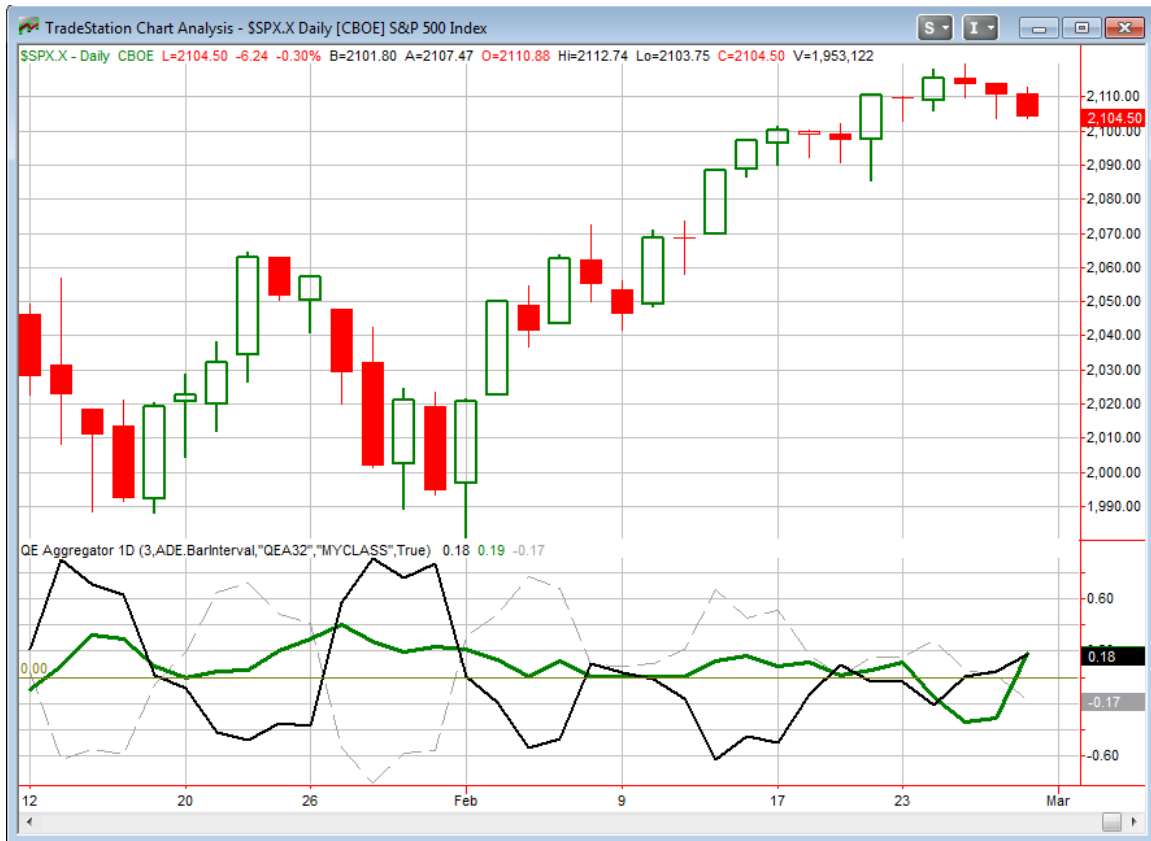
Results here appear strongly bullish. I've also listed out all the instances below assuming a 5-day holding period.

SPX closes down for at least the 3rd day in a row. Close > 200ma. It is the last trading day of the month. Buy on close. Sell 5 days later. \$100k/trade. 1986 - present.

Date/Time	Signal	Price	% Profit	Run-up Drawdown
12/31/86	Buy	\$242.16	6.24%	\$6,229.44
01/08/87	Sell	\$257.28		\$0.00
06/30/89	Buy	\$317.97	2.86%	\$2,857.40
07/10/89	Sell	\$327.07		(\$178.98)
09/30/93	Buy	\$458.93	0.05%	\$915.74
10/07/93	Sell	\$459.18		(\$125.86)
12/31/93	Buy	\$466.45	0.74%	\$815.34
01/07/94	Sell	\$469.90		(\$447.26)
03/31/95	Buy	\$500.71	1.14%	\$1,289.52
04/07/95	Sell	\$506.42		(\$101.49)
02/29/96	Buy	\$640.43	2.06%	\$2,580.24
03/07/96	Sell	\$653.65		(\$847.08)
08/30/96	Buy	\$651.99	1.81%	\$1,802.34
09/09/96	Sell	\$663.76		(\$1,227.06)
02/28/97	Buy	\$790.82	1.79%	\$2,188.62
03/07/97	Sell	\$804.97		(\$650.16)
02/26/99	Buy	\$1,238.33	3.00%	\$2,988.00
03/05/99	Sell	\$1,275.47		(\$1,784.00)
04/30/99	Buy	\$1,335.18	0.74%	\$1,439.30
05/07/99	Sell	\$1,345.00		(\$1,309.80)
08/31/99	Buy	\$1,320.41	1.80%	\$3,073.50
09/08/99	Sell	\$1,344.15		(\$1,170.75)
11/30/99	Buy	\$1,389.07	1.45%	\$4,142.85
12/07/99	Sell	\$1,409.17		(\$119.99)
04/30/04	Buy	\$1,107.24	(0.77%)	\$1,845.00
05/07/04	Sell	\$1,098.69		(\$774.90)
04/30/07	Buy	\$1,482.37	1.83%	\$1,918.21
05/07/07	Sell	\$1,509.48		(\$379.89)
11/30/10	Buy	\$1,180.55	3.66%	\$4,578.00
12/07/10	Sell	\$1,223.75		\$0.00
07/29/11	Buy	\$1,292.28	(7.19%)	\$1,162.70
08/05/11	Sell	\$1,199.38		(\$9,562.63)
01/31/12	Buy	\$1,312.40	2.64%	\$2,799.84
02/07/12	Sell	\$1,347.05		\$0.00

The 2011 instance saw the market get crushed. This was largely due to US debt being downgraded for the 1st time ever, and it was a historically extreme selloff. But even with that instance included in the overall results, the stats remain strong. The setup certainly seems worth taking into consideration.

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



The new studies tonight flipped the green Aggregator Line above 0. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line moved further 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 turned long at the close.

If nothing new triggers, then expectations are set to remain positive on Monday. Of course this could change if strong bearish evidence emerges. The Differential Pivot will be 2105.88 on Monday. That is only a little over a point above Friday's close. So it is only going to take a small bounce in order for SPX to move back from oversold to overbought versus expectations.

The studies tonight looked at pullbacks 1) after extended run-ups, 2) from intermediate-term highs, and 3) at the end of the month. They appeared to confirm each other nicely in that the current pullback appears to be a high-probability setup. And with SPX now short-term oversold, I am interested in taking on some long exposure in order to benefit from a possible bounce. The one issue I have with the current setup is that the Differential Pivot is so close by. That means a move up on Monday will turn the

Aggregator signal back to flat. So upside is somewhat limited here. But I like the evidence so much I have decided to take on a small amount of index exposure.

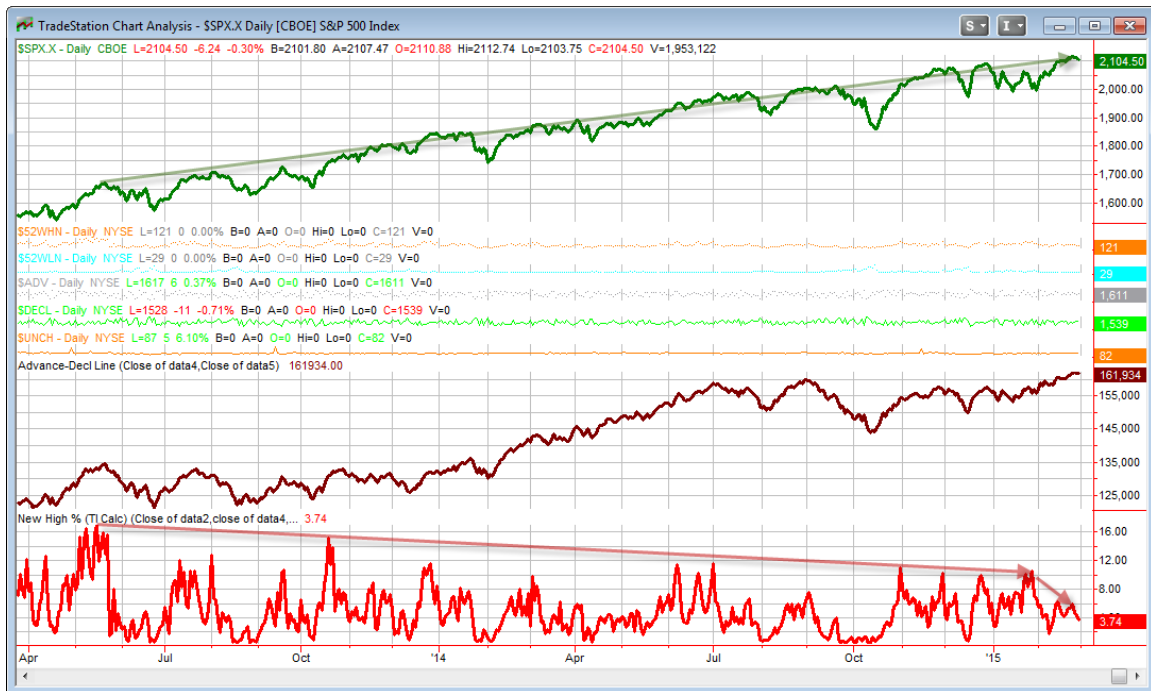
Intermediate-term Outlook (2 weeks – 2 months) – updated 3/2 – somewhat bullish

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.)

With the 3-day pullback to finish off the week, SPX finished down a mild 0.3% on the week. It did close at a new high on Tuesday, and to this point the long-term uptrend certainly seems to be intact.

While new highs were reached for SPX the number of new stocks making new highs continued to diverge badly. This can be seen on the chart below, which is similar to the one found on the QE charts page.



As I wrote the last couple of weeks...

...not only is the New High % diverging, it is still very far below the May 2013 level. And as I discussed in the Study of Tops (available for Gold & Silver subscribers on the special reports downloads page) and have reiterated here a number of times, the divergent New High % is a condition that has preceded every major SPX decline since 1970.

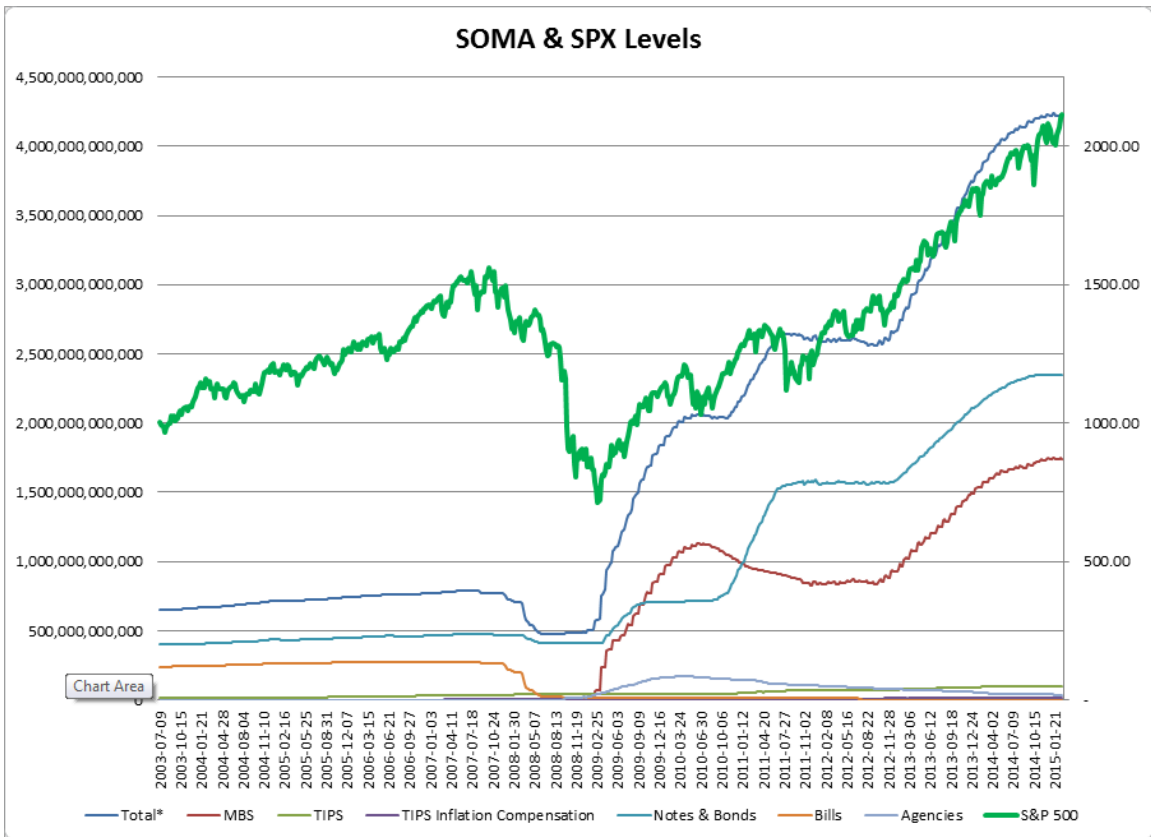
This opens up the possibility of a major top being put in. Note I said possibility, not probability. It needs to be understood that while the narrowing of New Highs and/or the turn down in the Advance/Decline Line has been a prerequisite for a top to take place, these breadth conditions have not been very useful in timing the tops. Often such divergences have persisted for many months, or even years (as in this case). I therefore view these breadth divergences as possible warning signs – not as timing signals. The current divergence is over 18 months old. It hasn't mattered yet, but if it persists, then it will matter at some point.

If the market continues higher and the New High % rallies to new highs as well, then that would suggest the market is unlikely to reach a major price top for at least another 2 months. I'll continue to keep an eye on it. For now it remains highly divergent. So the rally is occurring with fewer and fewer stocks making new highs. And from this point it will likely take quite a bit of work to get the New High % back to the May 2013 level, or even levels we saw at the end of October.

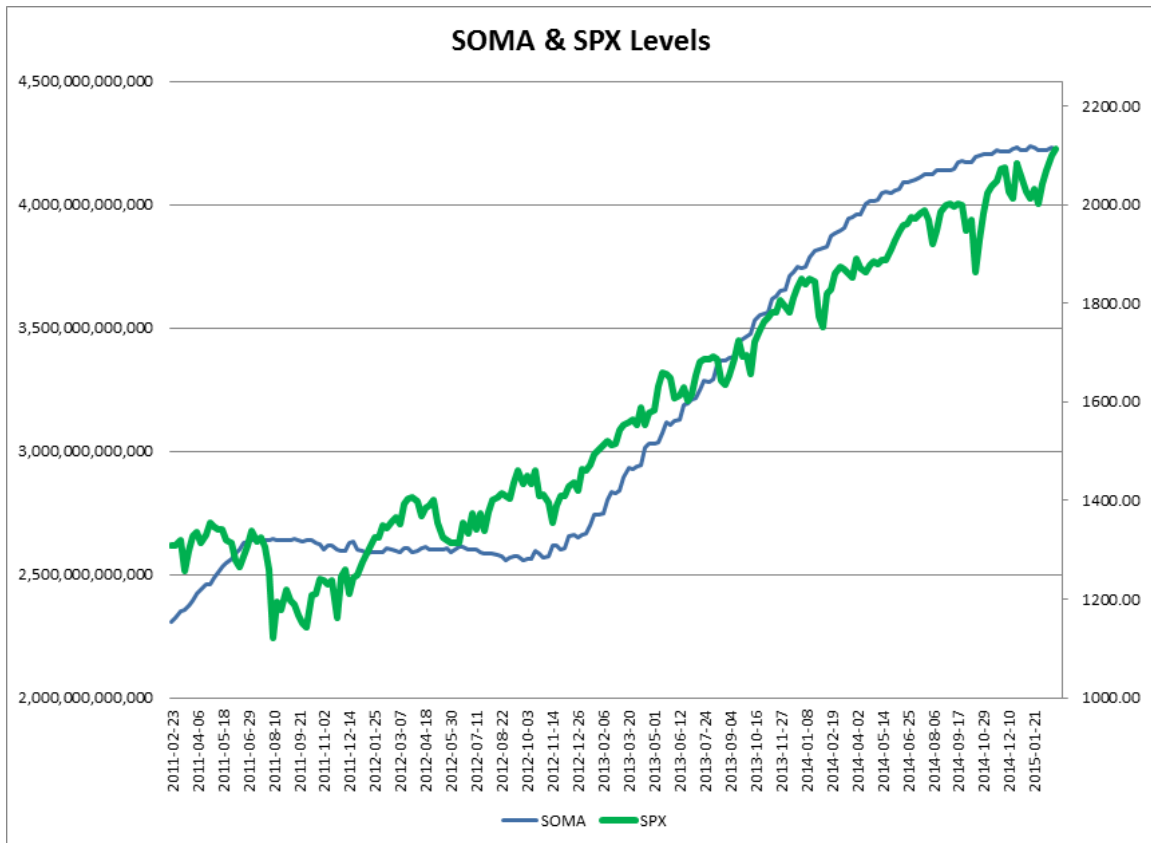
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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).



SOMA declined slightly this past week after having risen slightly the week before. SOMA has definitely flattened out, but it has not yet rolled over. Of course, in looking at the 1st chart you'll note that even flat SOMA readings have led to difficult markets over the last several years. Since quantitative easing ended in October the market has seen much choppier action, with more pronounced down moves than we saw during QE. But it has still managed new highs. And perhaps flat SOMA is enough for now. I doubt a steadily declining one would provide much support for the market. So as I have been doing, I will continue to keep a close eye on Fed action and SOMA levels.

The intermediate-term outlook from last week remains largely unchanged. One factor pointing to possible trouble is the limited amount of Fed stimulus. This can be seen in the SOMA account levels discussed above. The continually floundering number of stocks hitting new highs since spring of 2013 is also a potential warning sign.

Bulls can point to strong seasonality (Best 6 Months) as well as a continuing uptrend (Golden Cross) and a leading NASDAQ. More details on the influence of these factors and how different combinations have performed can be found in the Market Timing Course. (Included free with all annual subscriptions.) Additionally, the evidence from the 3 days down from the 50-day high study from above also suggests a 2-week edge and has been added to the intermediate-term Active List.

Overall, the bullish evidence is still outweighing the bearish. I am keeping the intermediate-term outlook at “somewhat bullish” as it has been for some time now. I remain more inclined to take on long positions than short ones, but will take either if short-term evidence is compelling enough.

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 @ \$210.66 limit. Based on the short-term outlook above I will look to take on some long exposure if I can get a decent fill. With the Differential Pivot close by, I am not going to pay up should the market gap up in the morning.

XIV – buy ½ position @ \$32.50 limit. In addition to the bullish index bias, the Aggressive VIX System is also long with VIX futures contango now as large as it has been in a while. I will look to get long XIV if it pulls back some on Monday.

Current Open Trade Ideas

None

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