

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 22, 2016

Volume 9 Issue 34

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr Swing
Short	100% Long VXX	Short

Tonight's Research Points

- The stretched VXO is suggesting a downside edge.
- The recent breadth thrust suggests an intermediate-term upside edge.
- SOMA has been positive and that could persist through Wednesday, but not beyond that.

Short-term Outlook

The Bottom Line

Evidence continues to point lower. Odds suggest more downside in the coming days. But a move lower on Monday could turn SPX “oversold”, which would lead me to take profits on my short position.

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						
February 22, 2016	VXO 15%-20% stretch	1-2 days	Bearish			
February 18, 2016	1% up day 2 days in a row. 10 high < 200	1-4 days	Bearish			
February 18, 2016	QE Buying Power Short Signal	1-6 days	Bearish			
Active - Long Term						
February 18, 2016	Up Issue % > 70% 3x	1-85 days	Bullish	10.70%	-5.10%	-12.10%
February 1, 2016	290% up days in 1 week	1-9 months	Bullish	23.10%	-6.60%	-15.10%
January 19, 2016	NASDAQ 100-day low. UpIss EMA < 37.5	1-19 days	Bullish			
November 2, 2015	Best 6 months	Nov-Apr	Bullish			
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			

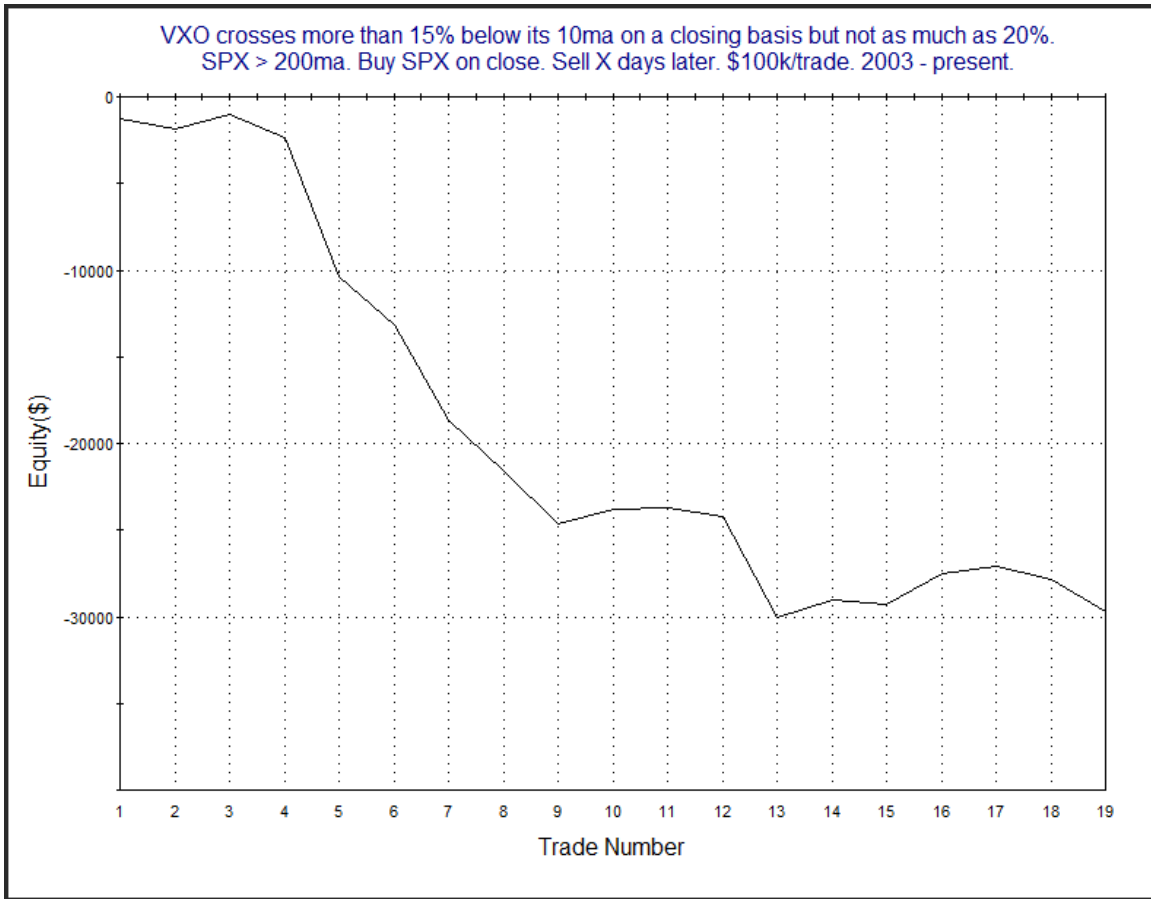
The Evidence

Friday started off poorly but finished mixed and mild. The SPX lost a mere 0.05 points, but the NASDAQ rose 0.4%, and the Russell 2000 gained 0.5%. Interestingly, breadth was negative as the NYSE Up Issues % was 49% and the Up Volume % came in at 33%. Total NYSE volume rose a little from Thursday's level, but was still quite light for an opex Friday.

Despite the SPX closing down slightly, the VXO (old version of the VIX) also closed down, and is now stretched quite far below its 10ma. This triggered the study below, which was last seen in the 12/1/11 subscriber letter. Results have been updated.

VXO crosses more than 15% below its 10ma on a closing basis but not as much as 20%. SPX > 200ma. Buy SPX on close. Sell X days later. \$100k/trade. 2003 - 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	-15,697.34	16	7	9	43.75	1,503.85	2,439.39	-2,913.81	-4,850.27	0.52	0.40	-981.08
4	-6,868.94	17	7	10	41.18	1,436.41	2,464.27	-1,692.38	-4,056.12	0.85	0.59	-404.06
3	-27,345.26	19	6	13	31.58	1,308.39	2,333.37	-2,707.35	-6,326.26	0.48	0.22	-1,439.22
2	-29,707.09	19	6	13	31.58	828.27	1,728.80	-2,667.44	-8,004.64	0.31	0.14	-1,563.53
1	-5,721.29	19	7	12	36.84	1,117.16	4,063.35	-1,128.45	-4,418.09	0.99	0.58	-301.12

The numbers all appear to lean bearish. I have posted below the profit curve assuming a two day holding period.



The curve continues to head lower and seems to offer some confirmation of the downside edge suggested by the numbers. Not evident above but still notable is that the Avg Drawdown has been about 3x the size of the Average Run-up for these trades.

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



With tonight's study being considered the green Aggregator Line held below zero. Negative readings mean net expectations from the Active List are for downside over the next few days. Meanwhile the black Differential Line is also below 0. The negative Differential Line reading means SPX is overbought versus recent expectations. So expectations are negative and SPX is overbought. This is considered a bearish configuration. Bearish configurations are visible on the chart whenever both lines close below 0. Therefore, the Aggregator signal stayed short at the close.

Expectations on Monday are primed to remain bearish. Of course this could change if new bullish evidence emerges. The Differential Pivot will be *slightly inverted* at 1917.96 on Monday. That is *just 0.18 points above* Friday's close. An inverted pivot means that the Differential Line will cross through 0 if SPX closes flat. In this case, in order for SPX to remain "overbought" it is going to need to close up at least 0.18 points. Anything less than that and it will be considered "oversold" versus recent expectations as of Monday's close.

So evidence is suggesting more downside is likely. But the inverted pivot makes the potential downside reward somewhat limited. This is because if the market does close lower on Monday as expected, that will leave SPX oversold and the Aggregator will no longer have a short signal. On the other hand, if SPX closes higher, there is a good chance the short signal will persist. Because of this I often view inverted pivots as opportune times to take profits. In this case I will look to cover my short position if we approach Friday's lows at any point during the day.

Intermediate-term Outlook (2 weeks – 2 months) – updated 2/22 – neutral

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

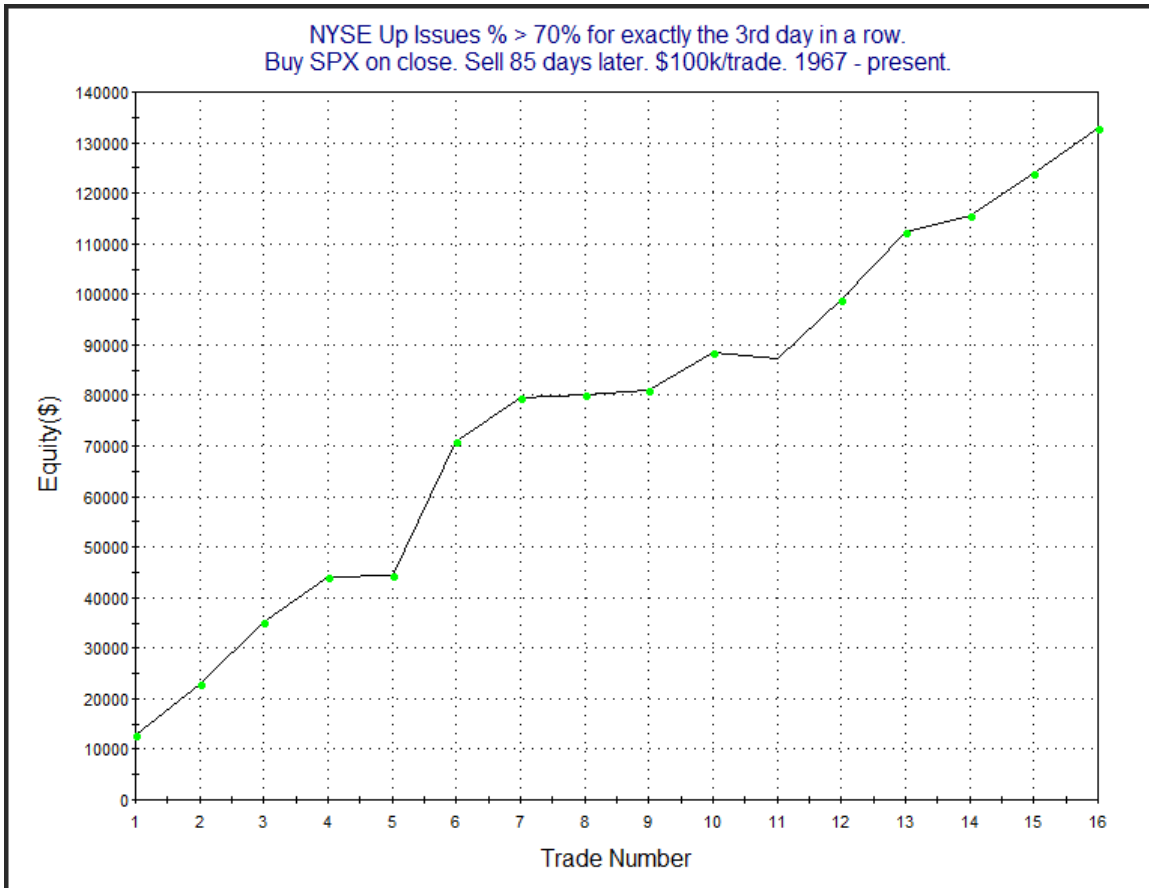
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), 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.) *There were no changes to the Market Timing Course indicators this week and all 3 combo systems remained flat.*

With Tuesday and Wednesday so strong the market was able to post solid gains this past week. It is now attempting to mount a rally and establish a new uptrend. Indications of whether this rally may succeed are mixed, but the strong 3-day bounce that lasted through Wednesday did trigger a study with possible intermediate-term implications. It was seen in Wednesday night’s letter and I have copied it below.

Also notable is that Wednesday was the 3rd day in a row that provided strong breadth readings. In the past, 3 days of strong breadth has led to further short-term upside...Intermediate-term implications of this study are also very compelling. I have included them below.

NYSE Up Issues % > 70% for exactly the 3rd day in a row. Buy SPX on close. Sell X days later. \$100k/trade. 1967 - 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
100	121,663.29	16	13	3	81.25	10,310.56	35,228.25	-4,124.64	-9,681.98	2.50	10.83	7,603.96
95	112,836.31	16	14	2	87.50	8,816.96	27,455.01	-5,300.59	-7,569.87	1.66	11.64	7,052.27
90	131,796.43	16	14	2	87.50	9,851.97	30,991.65	-3,065.58	-5,123.16	3.21	22.50	8,237.28
85	132,867.55	16	15	1	93.75	8,945.36	26,681.37	-1,312.89	-1,312.89	6.81	102.20	8,304.22
80	122,090.92	16	15	1	93.75	8,554.27	28,597.05	-6,223.12	-6,223.12	1.37	20.62	7,630.68
75	114,298.87	17	16	1	94.12	7,733.85	27,786.57	-9,442.75	-9,442.75	0.82	13.10	6,723.46
70	92,659.21	17	16	1	94.12	6,324.46	24,277.56	-8,532.18	-8,532.18	0.74	11.86	5,450.54
65	84,787.45	17	14	3	82.35	7,039.01	27,455.01	-4,586.24	-12,438.75	1.53	7.16	4,987.50
60	94,743.23	18	15	3	83.33	7,543.81	30,604.83	-6,137.98	-14,330.51	1.23	6.15	5,263.51
55	95,731.08	19	15	4	78.95	7,724.32	30,696.93	-5,033.43	-13,424.22	1.53	5.75	5,038.48
50	88,198.68	19	15	4	78.95	7,767.57	23,080.26	-7,078.71	-16,443.76	1.10	4.11	4,642.04
45	81,399.80	19	16	3	84.21	6,925.99	28,118.13	-9,805.37	-22,705.40	0.71	3.77	4,284.20
40	67,212.93	19	16	3	84.21	6,330.04	23,992.05	-11,355.88	-25,195.29	0.56	2.97	3,537.52
35	65,994.61	20	16	4	80.00	5,621.20	18,677.88	-5,986.16	-16,976.62	0.94	3.76	3,299.73
30	65,653.67	20	15	5	75.00	5,848.26	15,257.06	-4,414.06	-15,261.41	1.32	3.97	3,282.68
25	67,506.23	20	16	4	80.00	5,127.75	14,072.88	-3,634.44	-6,624.37	1.41	5.64	3,375.31
20	63,211.48	20	16	4	80.00	4,962.15	14,045.25	-4,045.75	-11,381.59	1.23	4.91	3,160.57
15	48,517.24	20	17	3	85.00	3,670.47	12,387.45	-4,626.90	-10,189.61	0.79	4.50	2,425.86
10	29,946.60	21	16	5	76.19	3,133.32	8,961.33	-4,037.30	-8,739.76	0.78	2.48	1,426.03
5	20,869.71	21	15	6	71.43	2,389.52	8,344.26	-2,495.50	-6,523.10	0.96	2.39	993.80

The results table suggests a strong consistent edge has followed this setup. Below is a performance graph showing performance assuming an 85-day holding period.



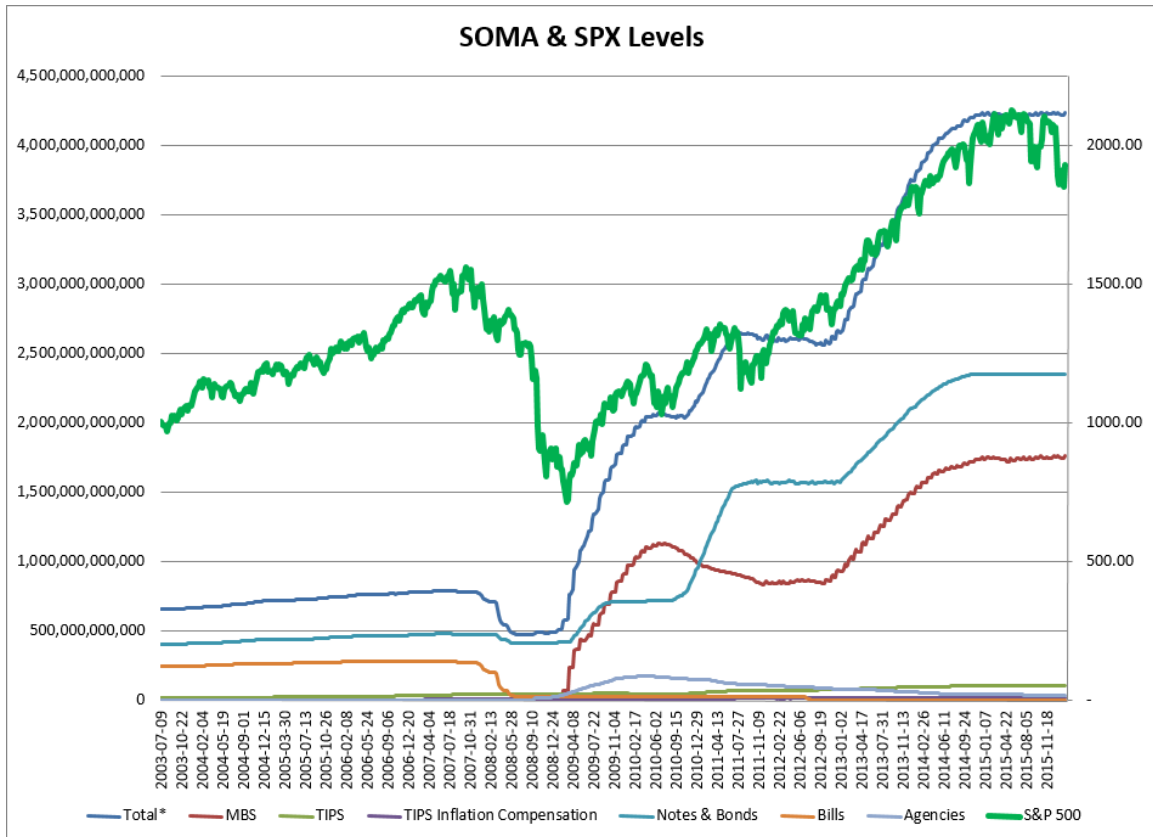
The curve appears to serve as further confirmation of the upside edge. The strong, steady upslope is very impressive.

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.

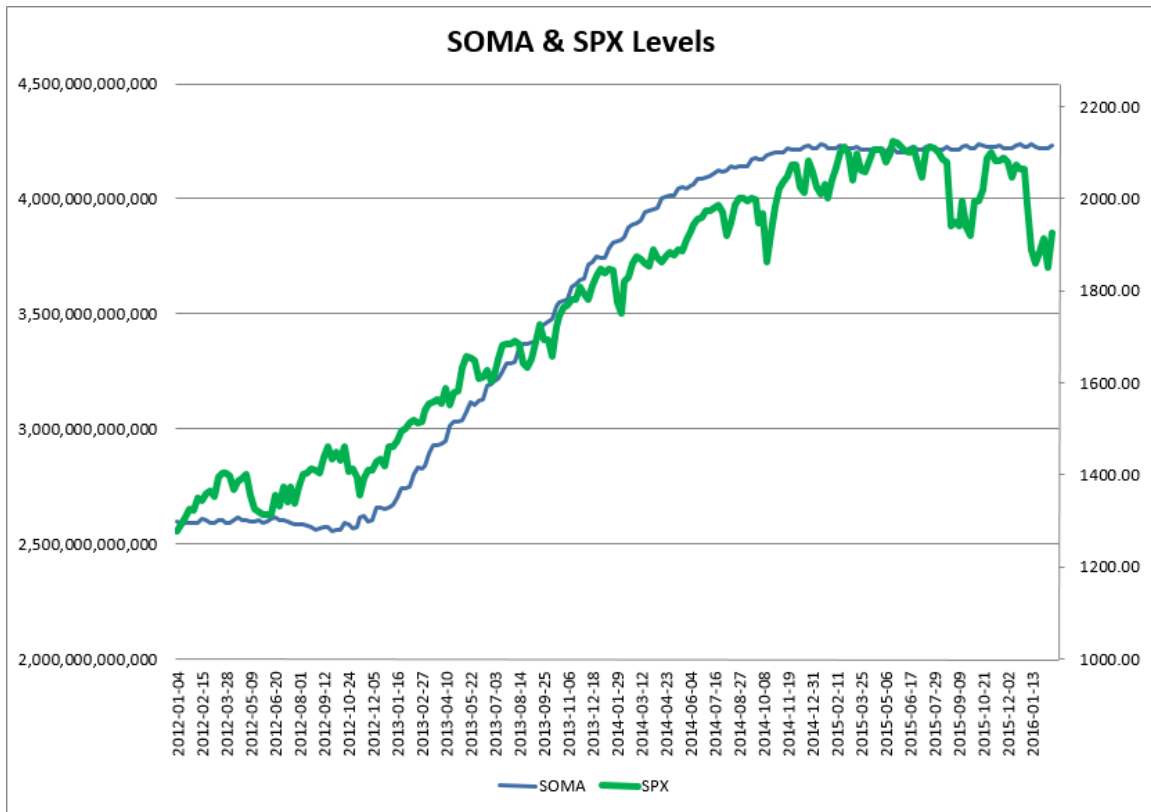
SOMA stands for System Open Market Account. It is the account at the Fed that contains all of its bond purchase holdings. We have tracked Fed purchases for several years, and as is evident in the charts below, the stock market has consistently reacted positively when the Fed has been buying securities 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 (2012 – present).



SOMA this past week (Wednesday to Wednesday) popped higher by 0.3%. This was expected based on the SOMA reinvestment schedule. The SPX rose 4.05% during that week and took advantage of the liquidity infusion as it often does. Since the beginning of 2015 SPX has risen 8.72% during strong SOMA expansion weeks. During all other weeks SPX has lost a sum total of 14.22%. The SOMA reinvestment schedule is not cut and dry this upcoming week, but it appears that we could see more modest gains, and then a large dip in the SOMA starting the week after this upcoming Wednesday.

As I often discuss, flat or declining SOMA readings have typically led to market struggles. But a rising SOMA has consistently led to gains. It will be important to monitor SOMA activity, including the monthly reinvestment schedule so that we may quickly identify any change in policy and take steps to adjust our strategies. I expect liquidity analysis to remain an important tool for us.

One thing I will be keeping an eye out for this upcoming week is a Follow Through Day (FTD), since we did not get one this past week. I have done a lot of research on FTDs over the years. I have found that they are not nearly what they are often hyped to be, but that they can often provide nice clues about whether a rally is likely to succeed or fail. A lot of research on FTDs can be found [on the Quantifiable Edges blog](#).

Intermediate-term evidence remains mixed. Bulls can point to long-term seasonal forces, and a few breadth-thrust studies including the one that just triggered this past week. But trend, leadership, and Fed policy are still pointing towards a long-term downtrend. With this mix I am still neutral. This means I am open to trading in either direction if compelling enough short-term evidence suggests an edge.

Catapult and Capitulative Breadth Statistics

[Catapult & CBI Presentation Link](#)

Open Catapult Triggers

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

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
SPY(1/4)(s)	2/17/2016	\$191.16	\$192.00	-0.44%		see below

I will look to take profits on SPY @ \$190.75 LIMIT. If not hit during the day, I will look to cover @ \$192.00 LIMIT ON CLOSE.

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 © 2016 Hanna Capital Management, LLC.