

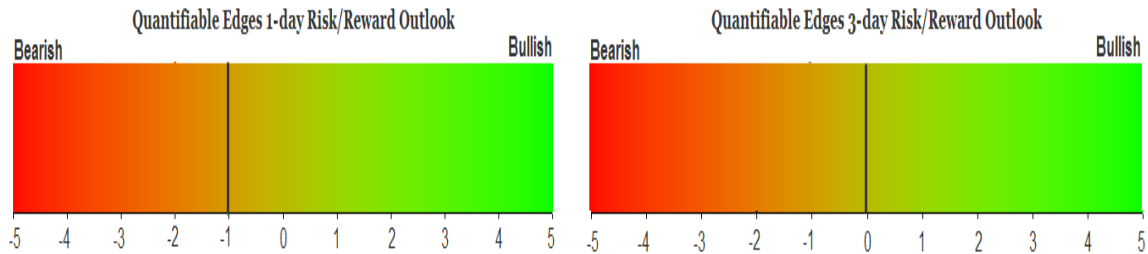
# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

June 6, 2016

Volume 9 Issue 107

## Market Overview



## Signals Overview

<b>Aggregator</b>	<b>Aggressive VIX</b>	<b>QE Buy Pwr Swing</b>
<b>Flat</b>	<b>50% Long XIV</b>	<b>Short</b>

## Tonight's Research Points

- Relatively strong drops from 50-day highs have consistently been followed by bounces.
- Unfilled gap patterns from high levels like we saw on Wednesday will often be followed by another day of selling.

### *Short-term Outlook*

#### *The Bottom Line*

Like yesterday, evidence is slightly bullish but the market is a little overbought. This leaves me short-term neutral.

**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>						
June 6, 2016	Big drop from 50-high	1-4 days	Bullish	1.10%	-0.80%	-1.60%
June 6, 2016	Unfilled gap from 50-high	1 day	Bearish			
May 31, 2016	SPY breakaway gap	1-5 days	Bullish	1.50%	-1.00%	-2.00%
<b>Active - Long Term</b>						
May 31, 2016	NASDAQ Leading	int term	Bullish			
May 24, 2016	Bounce from 20-low then inside day dn.	1-10 days	Bullish	5.00%	-2.85%	-6.75%
May 17, 2016	20-low to 4-high	1-20 days	Bullish	3.80%	-2.10%	-4.55%
April 26, 2016	Golden Cross	int term	Bullish			
March 2, 2016	FTD & 20-day high	int term	Bullish			
February 18, 2016	Up Issue % > 70% 3x	1-85 days	Bullish	10.70%	-5.10%	-12.10%
February 1, 2016	2 90% up days in 1 week	1-9 months	Bullish	23.10%	-6.60%	-15.10%
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
<b>Dropped Tonight</b>						
June 2, 2016	Gap and reverse 2x	1-2 days	Bearish			

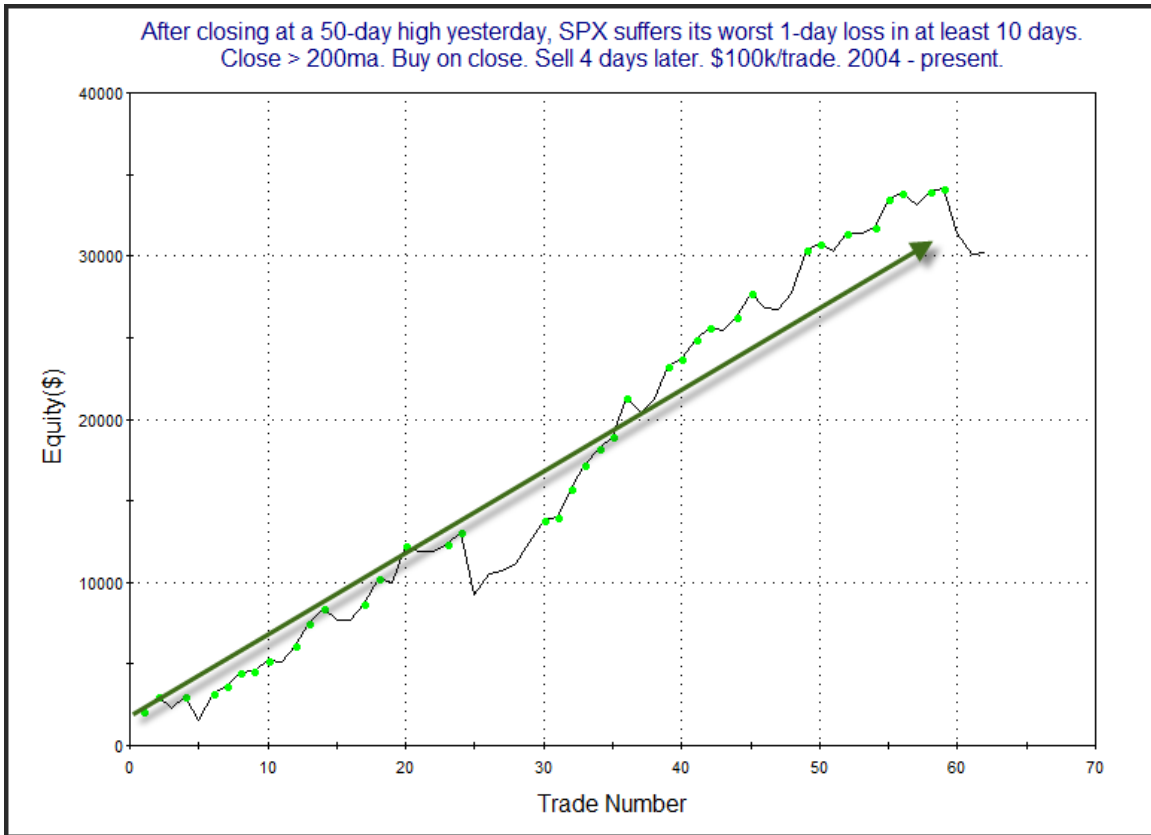
**The Evidence**

The employment report got Friday off to a rough start, and it never fully recovered. The SPX lost 0.3%, the NASDAQ fell 0.6%, and the Russell 2000 also dropped 0.6%. Breadth was mixed though as the NYSE Up Issues % was 53% and the Up Volume % came in at 48%. NYSE volume came in light.

The pullback triggered a couple of interesting (and conflicting) studies. The one below was last seen in the 4/22/16 Letter. It looks at *relatively* large drops from intermediate-term highs. I have updated all the stats.

After closing at a 50-day high yesterday, SPX suffers its worst 1-day loss in at least 10 days. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 2004 - 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	24,202.10	58	40	18	68.97	1,265.57	3,149.37	-1,467.82	-3,454.00	0.86	1.92	417.28
4	30,242.15	62	44	18	70.97	1,032.50	2,725.38	-843.76	-3,895.76	1.22	2.99	487.78
3	22,445.71	63	45	18	71.43	811.17	2,192.40	-780.95	-1,808.21	1.04	2.60	356.28
2	12,953.75	64	35	29	54.69	816.28	2,437.50	-538.49	-1,777.55	1.52	1.83	202.40
1	5,327.29	64	36	28	56.25	528.65	1,521.72	-489.43	-1,354.59	1.08	1.39	83.24

Over the last 12+ years the stats are impressive. And the 3-4 day consistency is strong. Below is a profit curve that assumes a 4-day holding period.



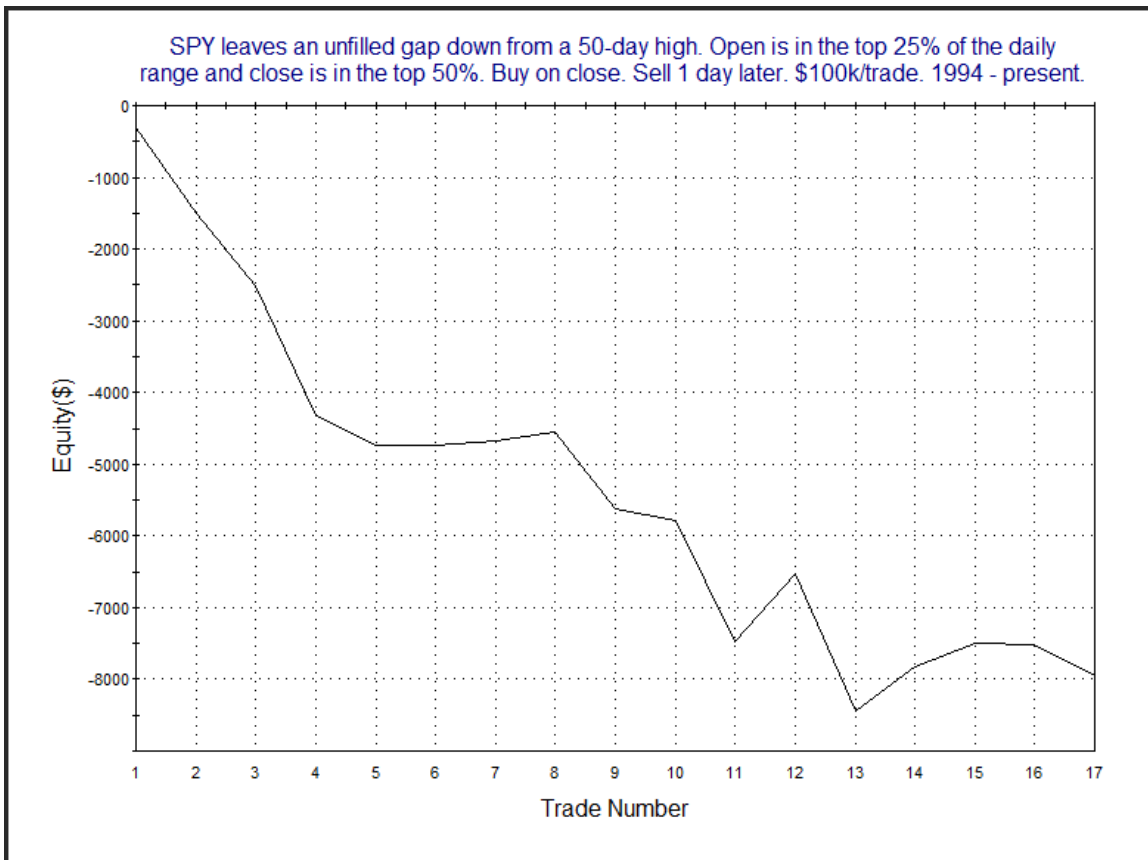
Despite the struggles in the last few instances, the steady upslope seems to confirm the bullish inclination.

This next study examined action like we saw in SPY on Friday. It looked at unfilled gaps down from high levels that both open and close in the upper part of the day's range. It was last seen in the 10/24/13 Letter and has been updated below.

SPY leaves an unfilled gap down from a 50-day high. Open is in the top 25% of the daily range and close is in the top 50%. Buy on close. Sell 1 day later. \$100k/trade. 1994 - present.

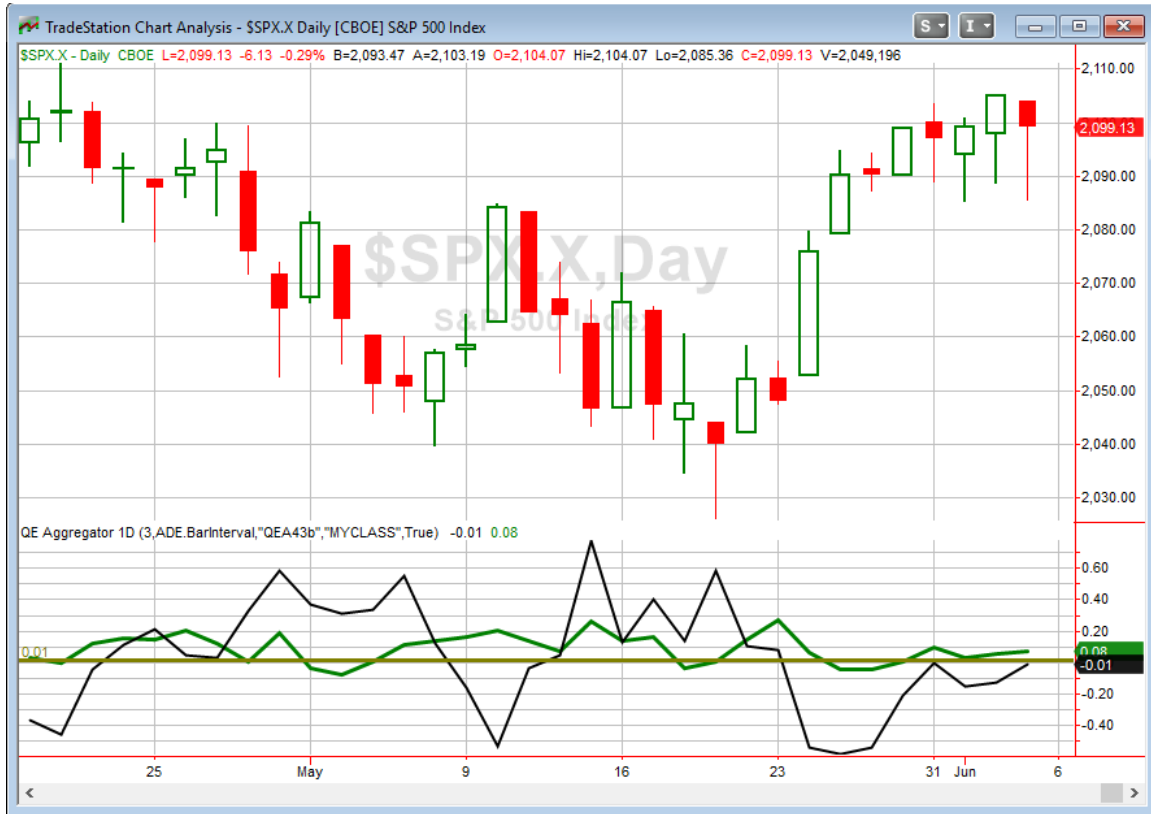
TradeStation Performance Summary <span style="float: right;">Expand ▾</span>			
All Trades			
Total Net Profit	(\$7,942.13)	Profit Factor	0.21
Gross Profit	\$2,092.70	Gross Loss	(\$10,034.83)
Total Number of Trades	17	Percent Profitable	29.41%
Winning Trades	5	Losing Trades	12
Even Trades	0		
Avg. Trade Net Profit	(\$467.18)	Ratio Avg. Win:Avg. Loss	0.50
Avg. Winning Trade	\$418.54	Avg. Losing Trade	(\$836.24)
Largest Winning Trade	\$938.96	Largest Losing Trade	(\$1,922.82)

The numbers look bearish. Let's also examine the profit curve.



There has been a little bump recently but the overall downslope is pretty good. I have included this study on the Short-Term Active List.

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



With tonight's studies included the green Aggregator Line held a little above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line held just a little below 0. The negative Differential Line reading means SPX is overbought versus recent expectations. So expectations are positive but 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. Therefore, the Aggregator signal stayed flat at the close.

With the current list of active studies, expectations are poised to remain positive on Monday. Of course this could change if new bearish evidence emerges. The Differential Pivot will be *slightly inverted* at 2102.18 on Monday. That is 0.15% *above* Friday's close. An inverted pivot means that the Differential Line will cross through zero if SPX closes flat. In this case SPX will need to close up at least 0.15% in order to remain overbought. Anything short of that and it will be considered oversold versus recent expectations.

Evidence is mixed. The market is a little overbought but headed towards a little oversold. Everything appears pretty neutral. I am not seeing a compelling reason to take on new exposure right here. I would prefer to wait until a more favorable reward/risk scenario emerges.

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

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

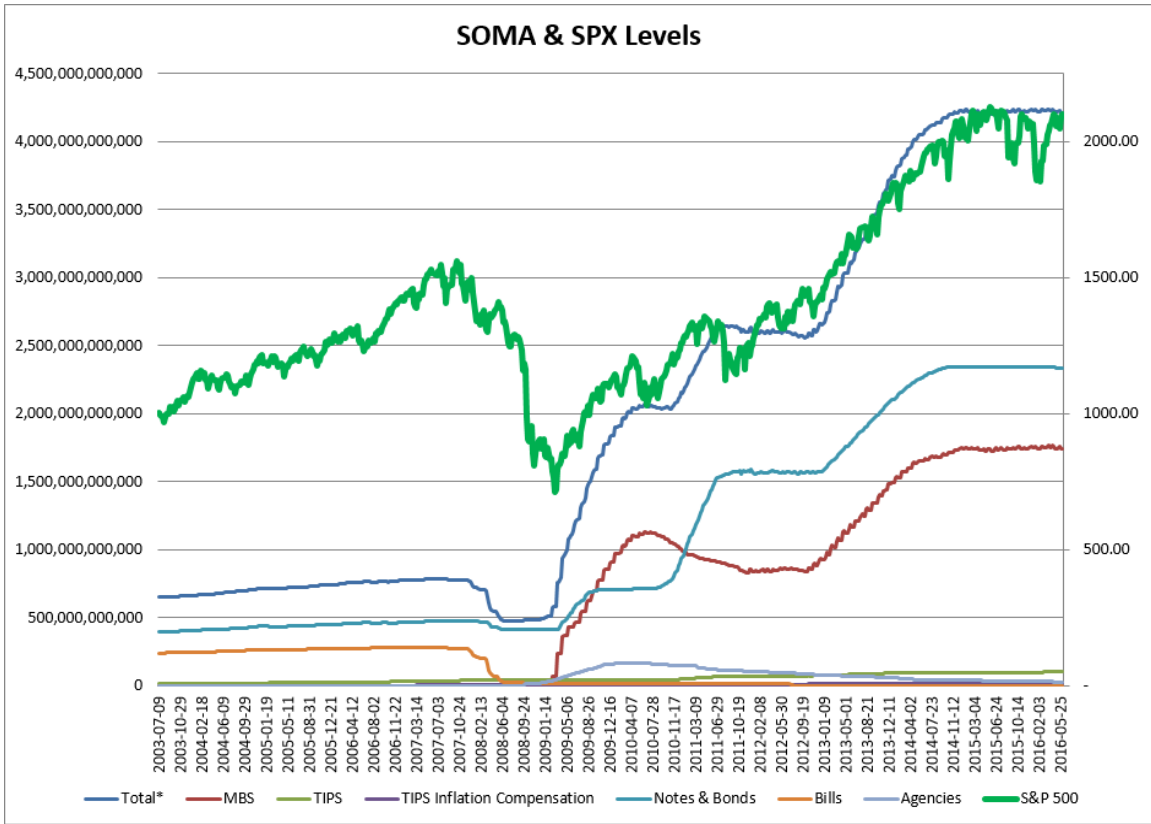
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#),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

This was a consolidation week for the market, as it traded in a fairly tight range and saw very little movement from last week. The SPX finished Friday up a mere 0.07 points from the Friday before. The mild action this week did nothing to generate compelling new evidence from an intermediate-term standpoint.

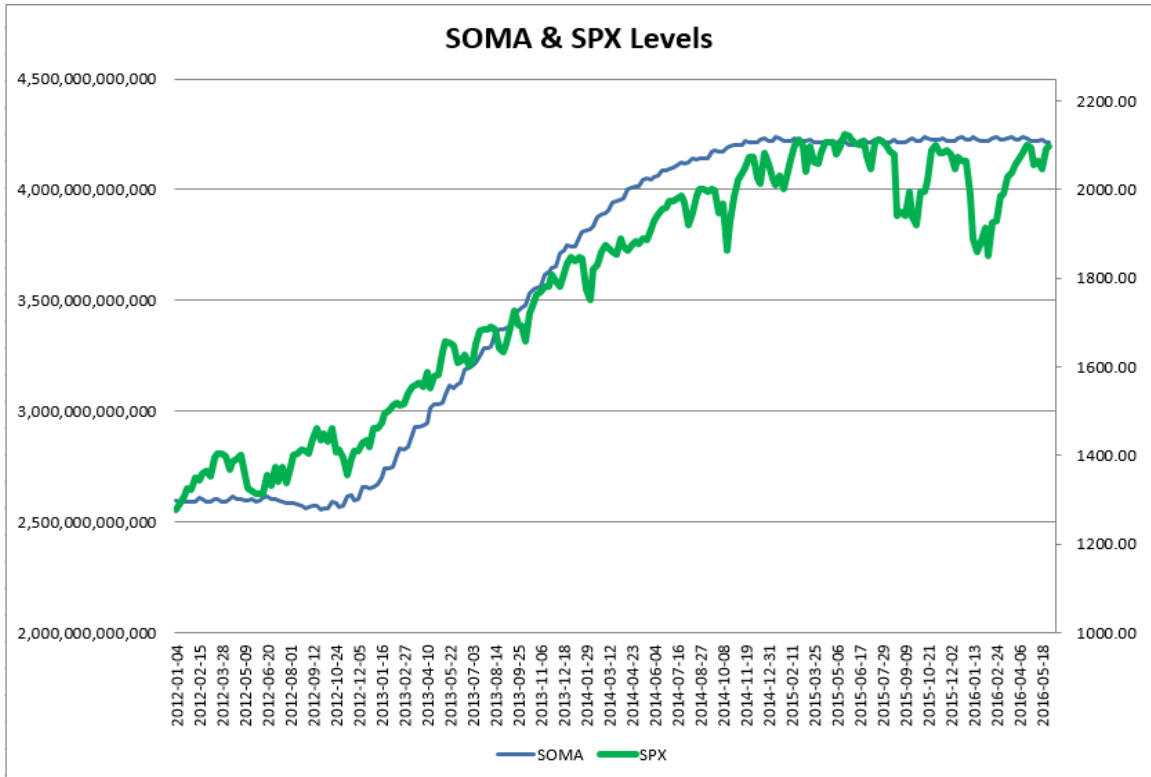
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

*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) was basically flat, with a rise of less than 0.01%. The flat SOMA is something I indicated was probable last week based on the Fed's reinvestment schedule. The 0.42% gain for the SPX over this period is strong. Most often the SPX will sell off during weeks that the SOMA does not expand. Since the beginning of 2015 SPX has risen 67% of the time for a sum total of 11.20% during SOMA expansion weeks. During all other weeks SPX has only risen 44% of the time and has lost a sum total of 8.00%. Based on the reinvestment schedule the Fed has stuck to over the last year and a half, this current week is likely to finish about flat. But the following week should see an increase in the SOMA. So after this upcoming Wednesday, bulls may get a short-term liquidity boost.

It continues to 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. To this point the Fed has kept to their schedule of the last year and a half and we have not seen any strong derivations. I expect liquidity analysis to remain a vital tool for us.

The intermediate-term outlook is basically the same as last weekend. Bears are counting on the weak Fed support, the "Worst 6 Months" and the long-term new-high breadth divergence. But 3 of the 4 Market Timing Course indicators are now bullish and that has generally been a strong positive for the market. Additionally, a few recent price-action based studies, multiple breadth-thrust studies from February and the bullish FTD study from March are all pointing higher. So with more favoring the bulls, I will continue to view the market with an intermediate-term bullish bias. In general my trades will primarily be long-focused, and it will take some strong evidence to get me interested in shorts.

### **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
XIV(1/2)	5/5/2016	\$26.20	\$33.00	25.95%		Aggressive VIX

VIX futures contango remains strong (just over 16% between 1<sup>st</sup> and 2<sup>nd</sup> month). That is helping our XIV position. I will look to ride it a bit further.

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