

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 18, 2016

Volume 9 Issue 137

Market Overview



Signals Overview

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

Tonight's Research Points

- Solid gains during opex week are often reversed the following week.
- The SPY gap and reversal on Friday after an unfilled gap up on Thursday suggests an upside edge for Monday.
- 5 days higher to a 50-day high rarely sees the move up end abruptly.
- Fed liquidity is expected to be weak (negative) over the next week and a half.

Short-term Outlook

The Bottom Line

There now appears to be a bit of a bullish edge, but it is somewhat weak and expected to be short-lived. It is not something I have great interest in trying to take advantage of.

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						
July 18, 2016	5 up to 50-high then 1 down day	1-10 days	Bullish	2.00%	-1.10%	-2.20%
July 18, 2016	3 higher highs, lows, close. Dn close	1 day	Bullish			
July 18, 2016	Opex week rises 1%-2%	1-5 days	Bearish	-1.35%	0.80%	1.60%
July 15, 2016	Top 10% 10-day range pre-opex	1-4 days	Bearish	-1.20%	0.80%	1.50%
July 15, 2016	Unfill gap up. 20-high. C<O	1-3 days	Bullish			
July 14, 2016	3 higher highs, lows, close. Dn close	1-4 days	Bullish	1.40%	-0.70%	-1.50%
July 11, 2016	SPX 50-low to 50-high in 2 weeks	1-6 days	Bullish			
Active - Long Term						
July 18, 2016	5 up to 50-high then 1 down day	1-10 days	Bullish	2.00%	-1.10%	-2.20%
July 11, 2016	NASDAQ leading	int term	Bullish			
July 11, 2016	SPX 50-low to 50-high in 2 weeks	1-17 days	Bullish			
July 11, 2016	SPX 50-high breakout 90% up volume	1-35 days	Bullish			
July 1, 2016	Up Issue % > 70% 3x	1-85 days	Bullish	10.70%	-4.90%	-11.70%
April 26, 2016	Golden Cross	int term	Bullish			
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			
Dropped Tonight						
July 11, 2016	SPY unfilled gap up breakout	1-5 days	Bullish			

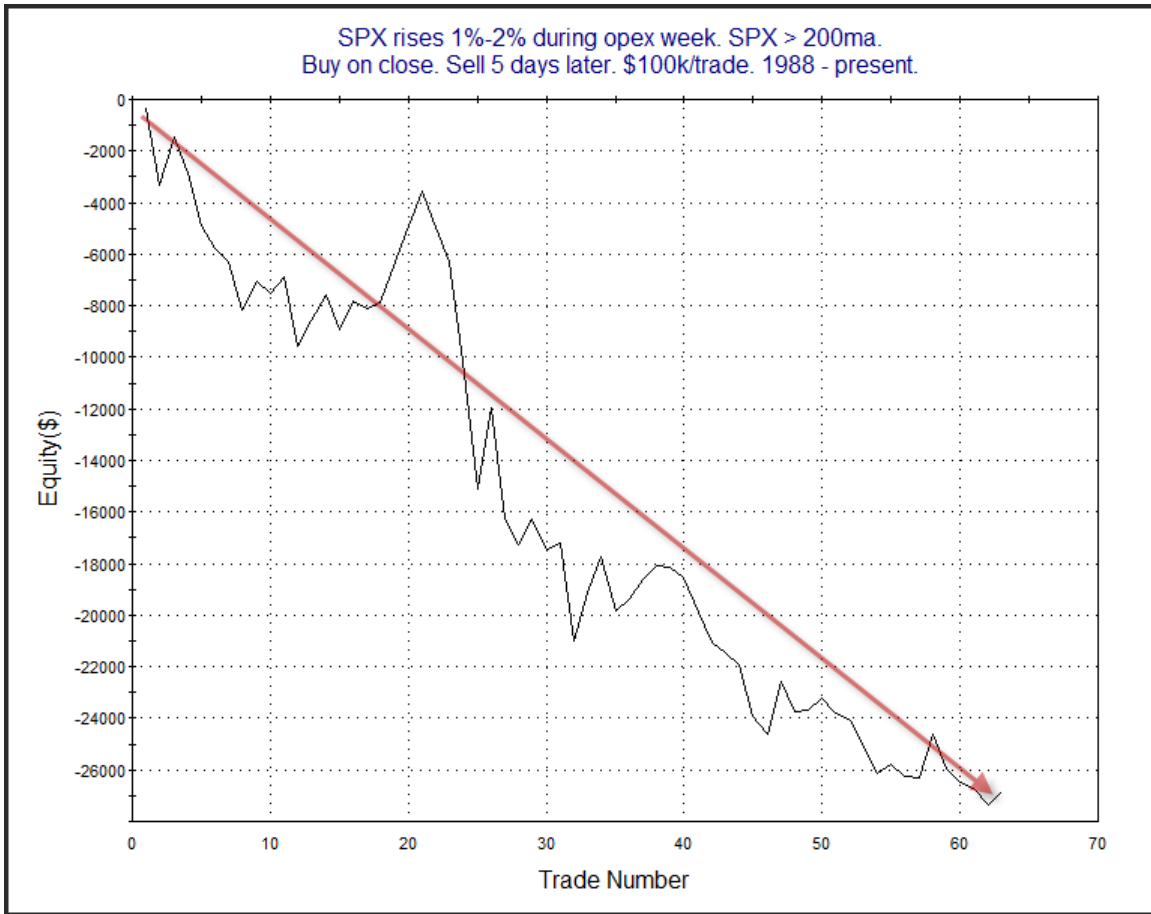
The Evidence

Friday's action was mixed and mild. The SPX and NASDAQ each fell 0.1% while the Russell 2000 rose 0.3%. Breadth was mildly positive as the NYSE Up Issues % was 55% and the Up Volume % came in at 50%. NYSE volume declined from Thursday's level, and was quite light for an options expiration day.

Despite Friday's slight down close, the SPX still posted solid gains on the week. Strong moves higher on opex week will often be followed by a pullback the following week. This is something we last saw in the 4/18/16 subscriber letter. I have updated the study from that letter below.

SPX rises 1%-2% during opex week. SPX > 200ma. Buy on close. Sell X days later. \$100k/trade. 1988 - 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	-26,811.54	63	24	39	38.10	1,069.38	3,146.64	-1,345.55	-4,961.56	0.79	0.49	-425.58
4	-24,469.83	63	22	41	34.92	925.06	3,212.16	-1,093.20	-4,046.70	0.85	0.45	-388.41
3	-6,762.07	63	30	33	47.62	792.02	3,403.68	-924.93	-2,765.00	0.86	0.78	-107.33
2	-9,042.71	63	31	32	49.21	575.35	1,590.30	-839.95	-2,917.60	0.68	0.66	-143.54
1	-5,014.49	63	26	37	41.27	497.93	1,739.10	-485.43	-2,470.65	1.03	0.72	-79.60

The stats suggest a short-term downside edge. Below is a profit curve assuming a 5-day holding strategy.



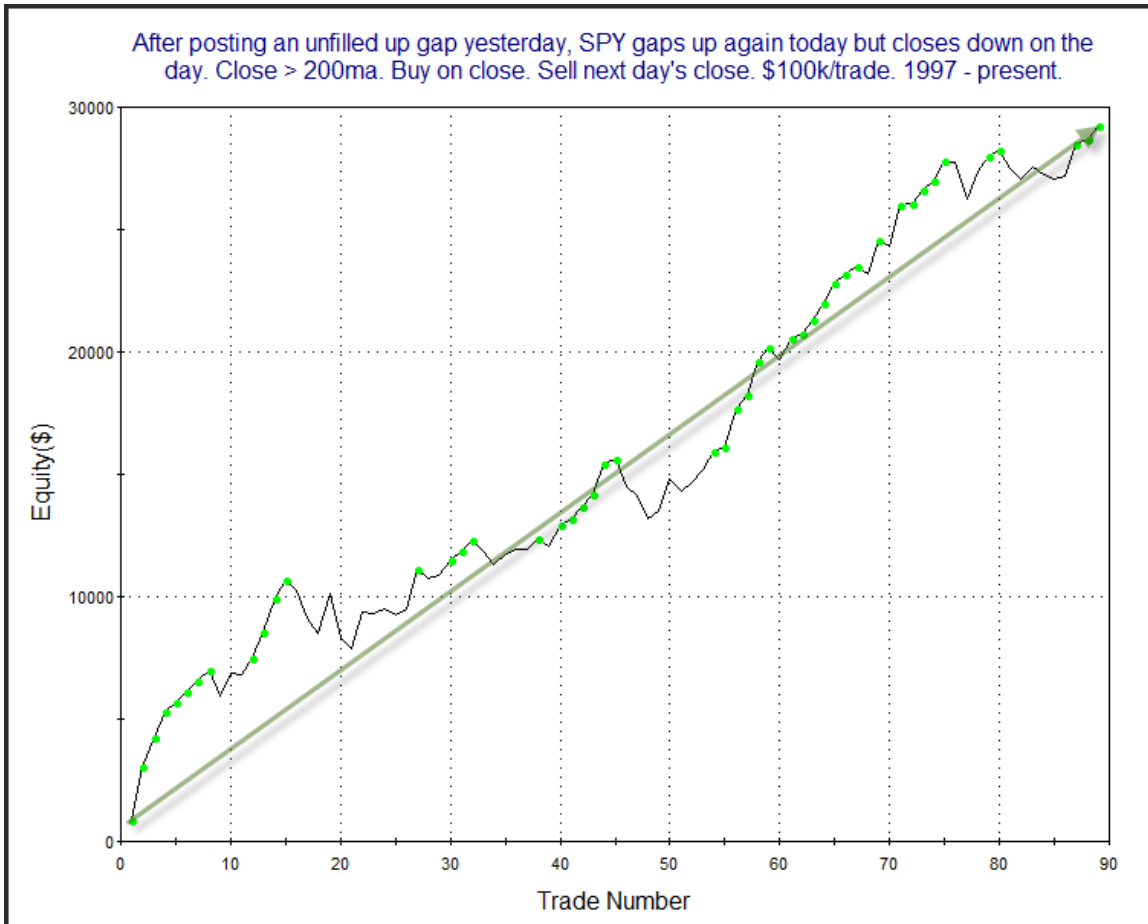
This is an impressive curve. The downside edge has persisted for a long time.

But we also saw some bullish evidence emerge. The study below is from the 4/22/15 letter. It examined action similar to the last 2 days with regards to how SPY gapped and finished. Results showed that gains had been pretty consistent the next day after similar action. Stats are updated.

After posting an unfilled up gap yesterday, SPY gaps up again today but closes down on the day. Close > 200ma. Buy on close. Sell next day's close. \$100k/trade. 1997 - present.

TradeStation Performance Summary			Expand ▾
All Trades			
Total Net Profit	\$29,257.78	Profit Factor	2.98
Gross Profit	\$44,012.79	Gross Loss	(\$14,755.01)
Total Number of Trades	89	Percent Profitable	70.79%
Winning Trades	63	Losing Trades	26
Even Trades	0		
Avg. Trade Net Profit	\$328.74	Ratio Avg. Win:Avg. Loss	1.23
Avg. Winning Trade	\$698.62	Avg. Losing Trade	(\$567.50)
Largest Winning Trade	\$2,194.38	Largest Losing Trade	(\$1,764.00)

The numbers here all look solidly bullish. Below is a look at profit curve.

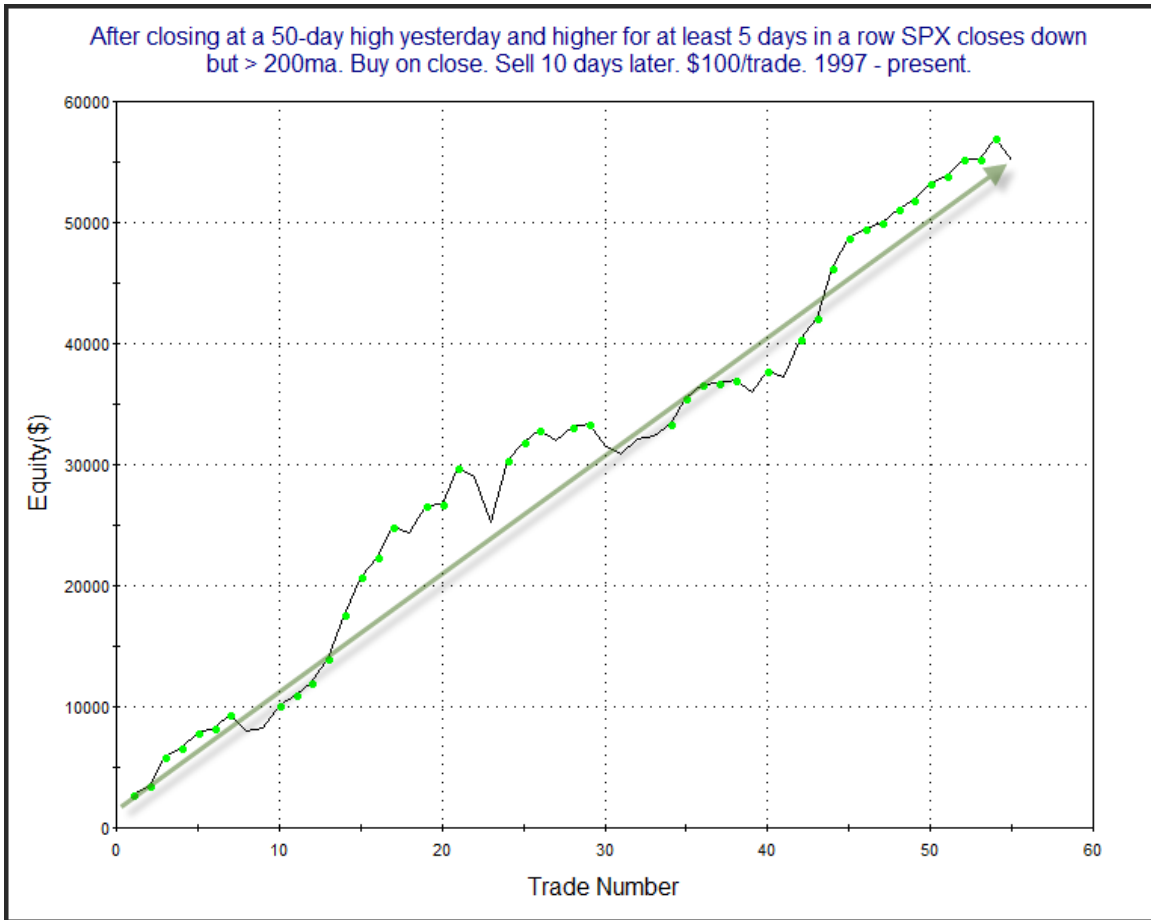


The strong, steady upslope is encouraging. Based on the action of the last 2 days, it appears an up day on Monday is fairly likely. I have included this study on the Active List tonight.

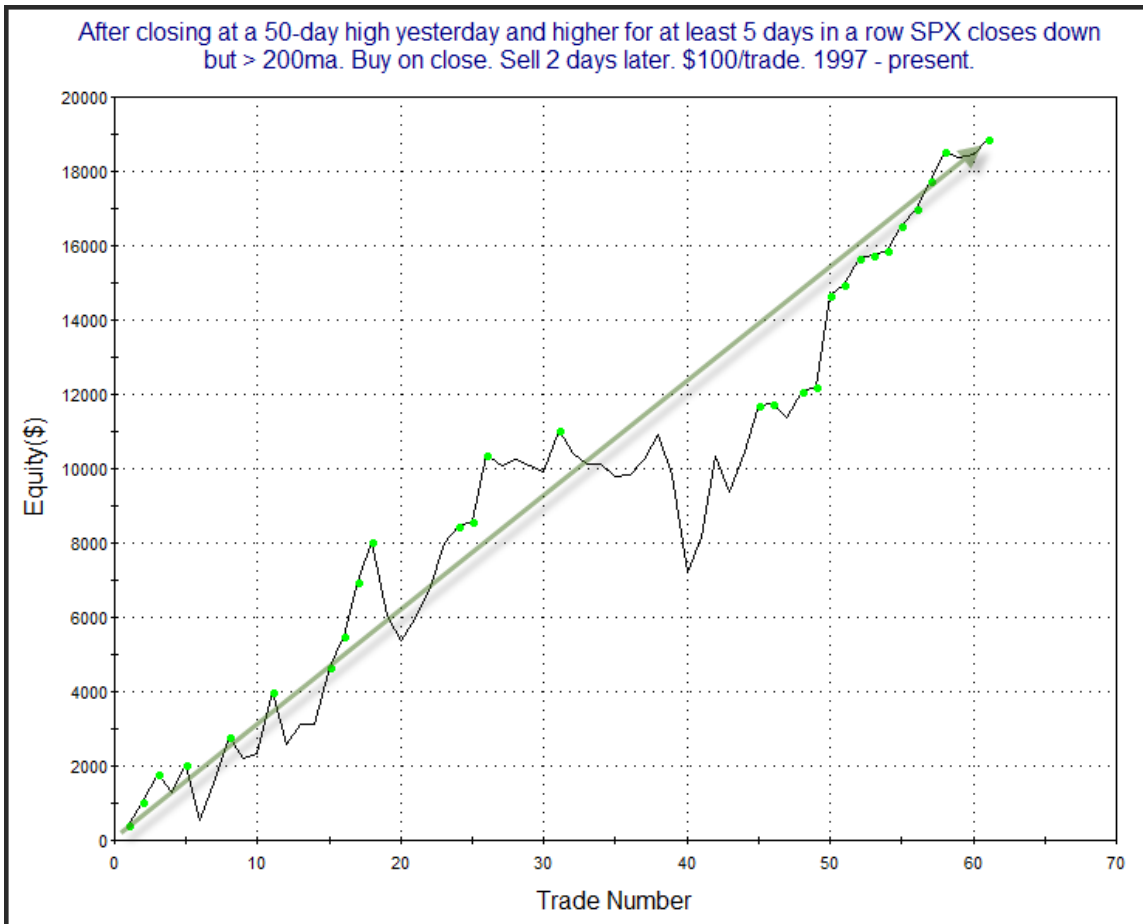
Another compelling study that triggered tonight suggested the recent persistent upmove is unlikely to abruptly end. (This is a theme we have seen many times over the years.) It considers what happens after the market moves up at least 5 days in a row to a 50-day high, and then pulls back. It was last seen in the 11/13/14 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. \$100/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	55,186.86	55	45	10	81.82	1,513.62	5,131.35	-1,292.59	-3,672.90	1.17	5.27	1,003.40
9	53,023.96	57	46	11	80.70	1,482.69	5,023.20	-1,379.97	-4,151.40	1.07	4.49	930.24
8	44,189.51	58	40	18	68.97	1,663.54	4,878.08	-1,241.79	-4,874.10	1.34	2.98	761.89
7	33,731.56	59	39	20	66.10	1,515.99	3,874.76	-1,269.59	-3,912.48	1.19	2.33	571.72
6	33,888.91	61	41	20	67.21	1,372.06	4,307.20	-1,118.27	-3,637.71	1.23	2.52	555.56
5	25,973.69	61	37	24	60.66	1,218.03	4,252.50	-795.56	-2,466.75	1.53	2.36	425.80
4	29,757.21	61	38	23	62.30	1,239.78	3,843.00	-754.54	-3,003.39	1.64	2.71	487.82
3	19,036.75	61	39	22	63.93	903.78	2,472.85	-736.84	-1,992.34	1.23	2.17	312.08
2	18,868.03	61	43	18	70.49	757.97	2,437.50	-762.49	-2,614.95	0.99	2.37	309.31
1	10,547.79	61	40	20	65.57	523.15	1,751.19	-518.91	-1,744.10	1.01	2.02	172.91

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 both the 10-day and 2-day exit profit curves. First, the 10 day.



The strong upslope appears to confirm the bullish edge. Next let's look at the 2-day curve.



Results are choppy. But even with more whipsaws this one appears worthy of consideration. I have included this study on both the short-term and intermediate-term active lists. So there is a mix of new evidence that seems worth consideration.

I have updated the Aggregator chart below.



With tonight's studies included the green Aggregator Line held just slightly above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line inched back above 0. The positive Differential Line reading means SPX is oversold versus recent expectations. So expectations are positive and 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.

Based on the current active list, expectations are poised to turn slightly negative on Monday. This could change if new bullish evidence emerges. The Differential Pivot will be 2163.15 on Monday. That is less than 2 points above Friday's close. So for SPX to move from oversold to overbought versus expectations it will only need to close up a small amount on Monday.

The Aggregator is suggesting a bullish edge. But it is a pretty weak edge. First of all, expectations are only slated to remain positive for one day here. That does not give much time for gains to be had. And if SPX gains over 2 points, the market will turn to overbought, which would also mean the end of the bullish configuration. So while nimble traders could look to take advantage of a move higher on Monday, it is not a strong enough edge for me to consider swing trading ideas to share in the letter. I will wait to see how things play out and hope for a more substantial edge to emerge.

Intermediate-term Outlook (2 weeks – 2 months) – updated 7/17 – bullish

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

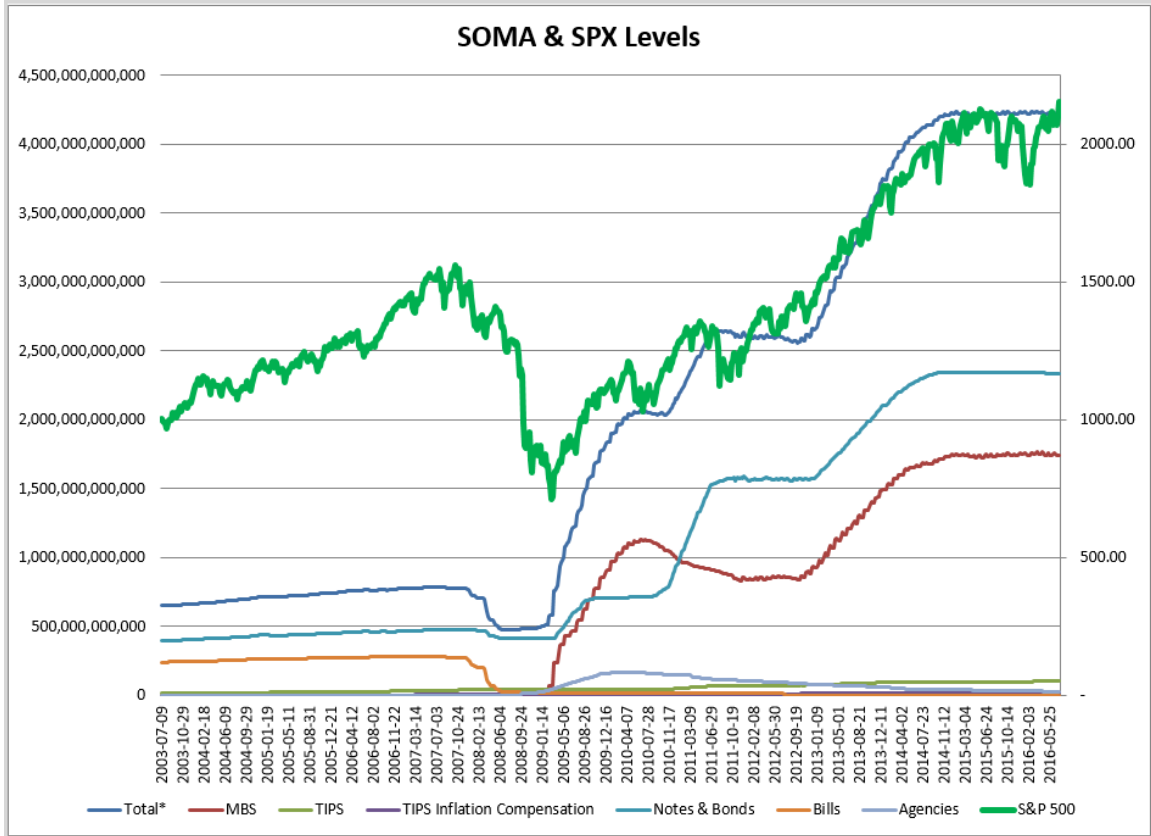
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), 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.) *We now see all 3 combo signals are “Long”.*

The market saw new highs and SPX finished the week up 1.5%. The intermediate-term trend remains up. Other than the study above that looked at moves down from a 50-day high following a 5-day run-up, there was nothing new that emerged from an intermediate-term standpoint.

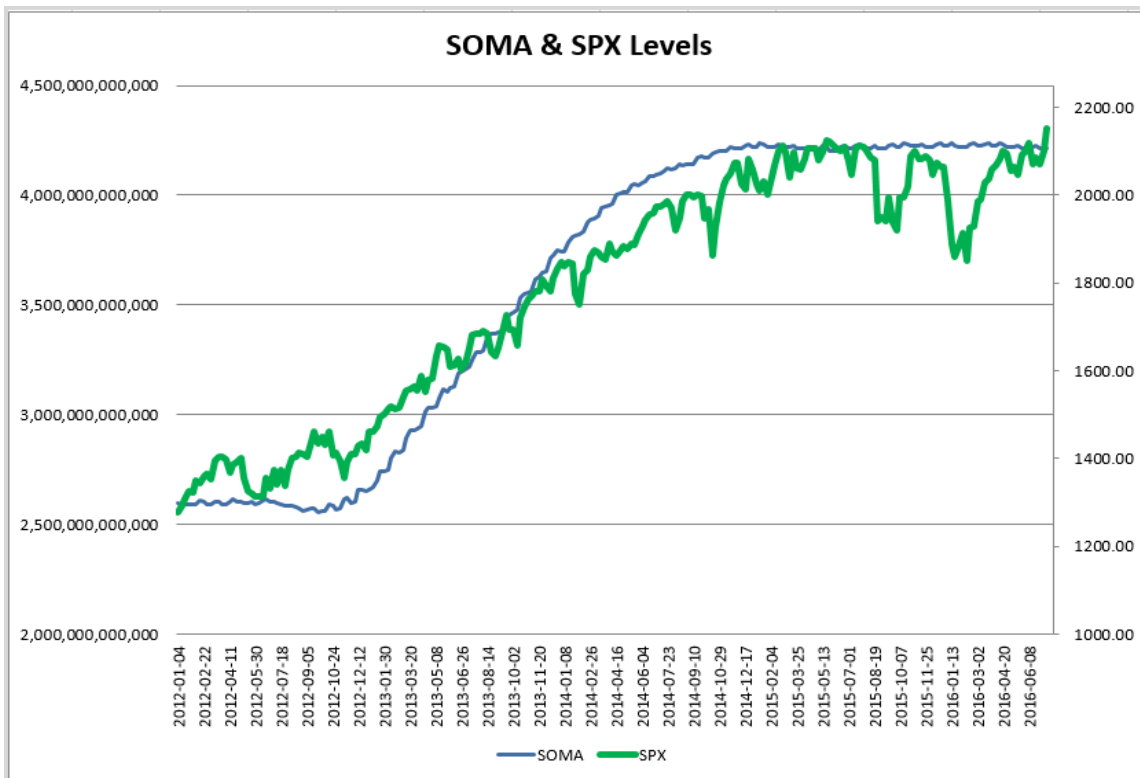
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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) remained basically flat, with just a miniscule rise of less than 0.01%. Based on the Fed’s reinvestment schedule I was expecting a rise of a bit more. The 2.5% gain for the SPX over this period is unusually large for a week with only a minuscule advance. Most often the SPX will suffer during weeks that the SOMA fails to expand much. Since the beginning of 2015 SPX has risen 65% of the time for a sum total of 9.62% during SOMA expansion weeks (of at least 0.01%). During all other weeks SPX has only risen 46% of the time and has *lost* a sum total of 3.86%. Based on the reinvestment schedule the Fed has stuck to over the last year and a half, this current week, which ends on Wednesday, appears likely to post a loss. But with reinvestments so low this past week, perhaps some were pushed forward a day or so. There would seem to be a chance that we will not see the decline we have seen in other similar weeks. The following week the SOMA is also expected to decline. So if it does not happen this week, it almost certainly will the next. Therefore the bulls will likely be facing a bit of an illiquidity headwind for the next week and a half or so.

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.

Most of evidence we are seeing from an intermediate-term perspective continues to point north. We have seen some studies the last couple of weeks suggesting the breakout is strong and that the market is likely to continue higher. Additionally, 3 of our 4 Market Timing Course indicators are bullish, which has historically been quite promising. There are also some past breadth thrust signals that are still active. There is still some bearish evidence as well, including overall weak Fed support and the long-term new-high breadth divergence. With this week's new bullish evidence and the fact that the market is again challenging new highs I am keeping my intermediate-term outlook bullish. I will be looking to trade the long side more aggressively and will be extra-selective with possible short trades.

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)	6/14/2016	\$24.70	\$29.47	19.31%		Aggressive VIX

Expectations are positive and 1-2 month futures contango is again extremely strong. I like my XIV position and will look to ride it a while longer.

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