

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

August 1, 2016

Volume 9 Issue 147

Market Overview



Signals Overview

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

Tonight's Research Points

- The first trading day of the month is often bullish, but current circumstances are not favorable.
- Friday's move up on strong volume is a positive sign for the next couple of weeks.
- SOMA is expected to be flat over the next week and a half, so bulls will not be helped out by Fed liquidity flows.

Short-term Outlook

The Bottom Line

Evidence is suggesting a solid bullish edge. But the market is near overbought versus expectations. I have some (non-index) long exposure already. I don't intend to take on any index positions unless the market gives at least a little bit of a pullback in the next few days.

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 28, 2016	3-High 3-Low Close 3-low	1-5 days	Bullish			
July 28, 2016	Back to back outside days	1-3 days	Bullish			
July 28, 2016	1st close < 10ma in 15 days	1-3 days	Bullish			
July 28, 2016	50-high, then 5 days sideways	1-3 days	Bullish			
July 18, 2016	5 up to 50-high then 1 down day	1-10 days	Bullish	2.00%	-1.10%	-2.20%
Active - Long Term						
August 1, 2016	Highest volume 20 on up day. Not opex.	1-10 days	Bullish	2.40%	-1.60%	-3.10%
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 29, 2016	Gap and reverse 2x	1 day	Bearish			

The Evidence

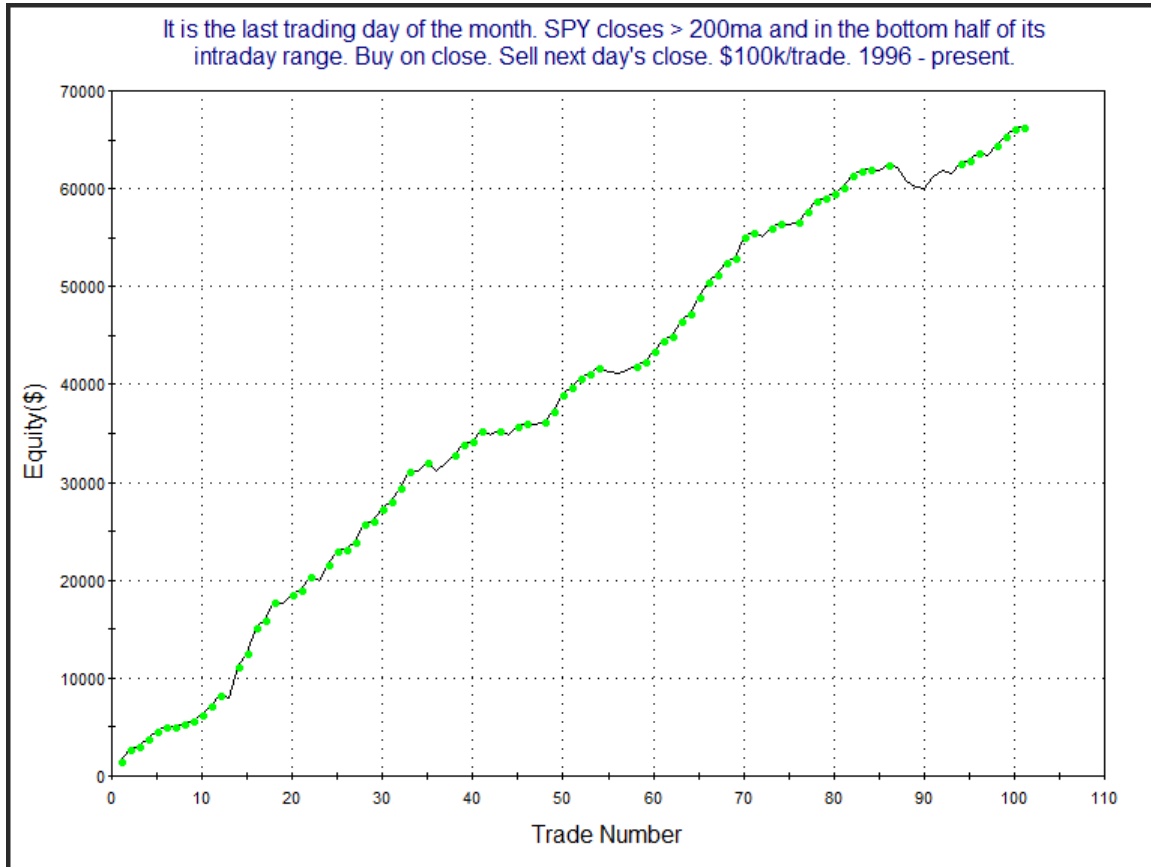
Friday saw the market scratch out small gains. The SPX closed up 0.2%, the NASDAQ rose 0.1% and the Russell 2000 climbed 0.2%. Breadth was positive as the NYSE Up Issues % was 63% and the Up Volume % came in at 61%. NYSE volume rose to the highest level in a long time.

There were a few studies that appeared in the Quantifinder related to Monday being the 1st of the month. The simple breakdown below appear to be the most substantial. It last appeared in the 9/2/14 letter. It looked at all 1st days of the month and broke them down by whether the previous day closed in the top or bottom half of the daily range. First let's look at times (unlike Friday) where the market closed in the bottom half of its range on the last day of the month.

It is the last trading day of the month. SPY closes > 200ma and in the bottom half of its intraday range. Buy on close. Sell next day's close. \$100k/trade. 1996 - present.

TradeStation Performance Summary				Expand
All Trades				
Total Net Profit	\$66,346.95	Profit Factor		10.25
Gross Profit	\$73,521.56	Gross Loss		(\$7,174.61)
Total Number of Trades	101	Percent Profitable		81.19%
Winning Trades	82	Losing Trades		19
Even Trades	0			
Avg. Trade Net Profit	\$656.90	Ratio Avg. Win:Avg. Loss		2.37
Avg. Winning Trade	\$896.60	Avg. Losing Trade		(\$377.61)
Largest Winning Trade	\$3,295.88	Largest Losing Trade		(\$1,353.69)

The stats here are phenomenal. Gains absolutely blow away losses in every category. Gross gains are over 10x the size of gross losses. That's an incredible stat when you are looking at a sample size of 101 instances. And here is the profit curve.

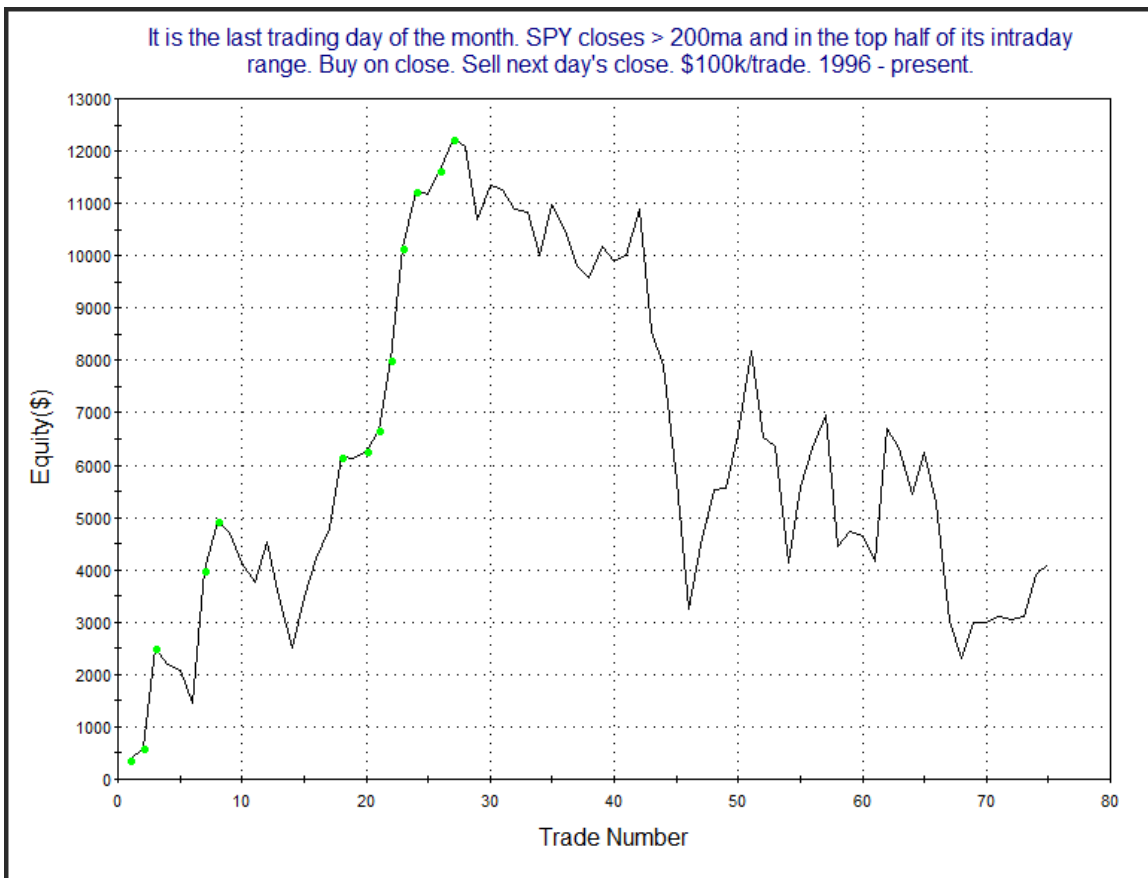


That's a pretty amazing curve. Unfortunately, SPY closed in the upper half of its range on Friday. So let's look at the implications of that finish.

It is the last trading day of the month. SPY closes > 200ma and in the top half of its intraday range. Buy on close. Sell next day's close. \$100k/trade. 1996 - present.

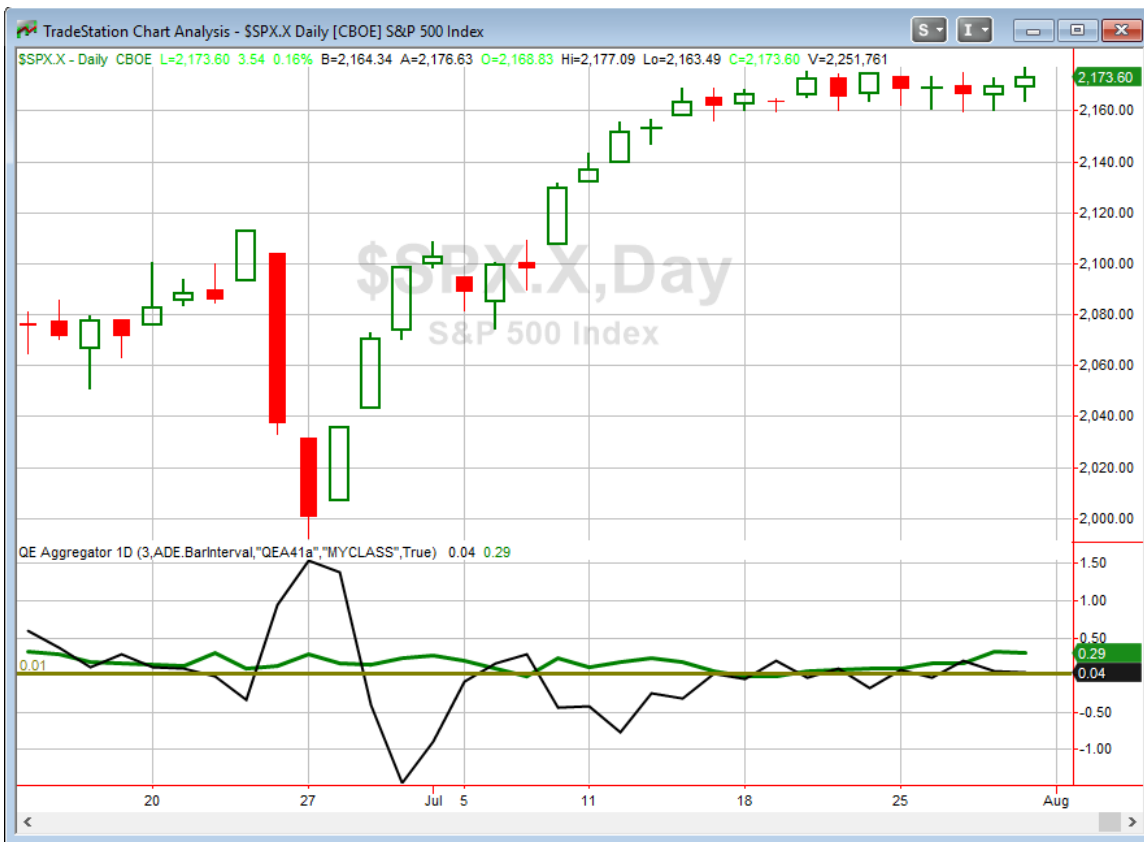
TradeStation Performance Summary Expand ▾			
All Trades			
Total Net Profit	\$4,112.88	Profit Factor	1.14
Gross Profit	\$33,009.15	Gross Loss	(\$28,896.27)
Total Number of Trades	75	Percent Profitable	52.00%
Winning Trades	39	Losing Trades	36
Even Trades	0		
Avg. Trade Net Profit	\$54.84	Ratio Avg. Win:Avg. Loss	1.05
Avg. Winning Trade	\$846.39	Avg. Losing Trade	(\$802.67)
Largest Winning Trade	\$2,562.30	Largest Losing Trade	(\$2,515.60)

We see here the upside edge nearly completely wiped away. Here is a picture of the profit curve.



This paints an even bleaker picture. While it may seem odd that this simple filter appears so impactful, let's consider why it might be. The 1st of the month has had a bullish tendency for many years. Among traders it is no longer a secret. Even closes in the top half appeared bullish for a period of time. But as the edge became more known, I suspect more and more traders have tried to front-run it. This front-running is apparent when the market rallies going into the end of the month and closes strongly on the last day. Obviously, when the market is selling off and closing poorly on the last day of the month, the edge is not being front-run by many. When the front-run occurs, it seems to exhaust much of the edge for the next day. And when it doesn't, the edge still remains. With Friday's strong close, it does not appear seasonality is likely to be a help on Monday.

I have updated the Aggregator chart below.



The green Aggregator Line tonight again held above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile the black Differential Line also remained (barely) 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 stayed long at the close.

Based on the current active list, expectations are poised to remain positive on Monday. This could change if strong new bearish evidence emerges. The Differential Pivot will be 2175.48 on Monday. That is just 0.1% above Friday's close. So SPX will only need to close up 0.1% in order to move from oversold to overbought at Monday's close.

So evidence is still pointing higher. And there is probably an upside edge here. But with the SPX already up 2 days in a row and near an all-time high, and the Differential Pivot so close by, the potential upside reward appears pretty limited compared to potential risk. I already have a little long exposure. I'm not terribly interested in adding to it until the market pulls back a little.

Intermediate-term Outlook (2 weeks – 2 months) – updated 8/1 – 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 again see all 3 combo signals are "Long".*

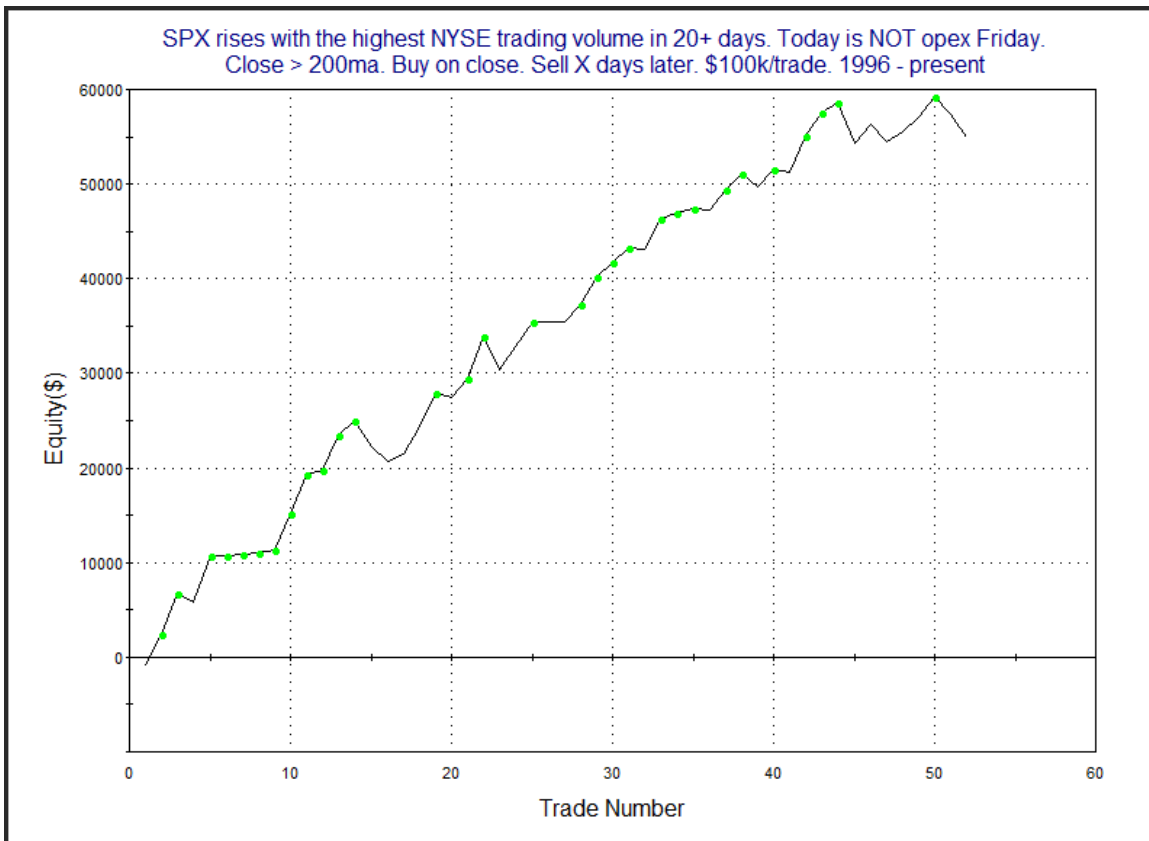
This was a choppy, sideways week for the market. The net for the SPX was a tiny loss of less than 1.5 points. The intermediate-term trend still appears to remain up.

From a research standpoint, the high volume on Friday provided an interesting bit of evidence. When the market has risen on extremely high volume on a day other than op-ex Friday, that has typically been a good sign. Below is a study last shown in the 12/18/14 subscriber letter that demonstrates this.

SPX rises with the highest NYSE trading volume in 20+ days. Today is NOT opex Friday.
Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1996 - 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	54,994.23	52	36	16	69.23	2,151.72	4,885.00	-1,404.23	-4,242.42	1.53	3.45	1,057.58
9	49,717.45	52	37	15	71.15	1,969.23	5,451.25	-1,542.93	-5,429.38	1.28	3.15	956.10
8	48,781.51	52	39	13	75.00	1,827.88	4,174.09	-1,731.20	-5,492.28	1.06	3.17	938.11
7	37,247.97	54	37	17	68.52	1,861.80	4,869.18	-1,861.09	-5,526.30	1.00	2.18	689.78
6	36,958.26	57	37	20	64.91	1,858.36	5,552.91	-1,590.06	-4,857.36	1.17	2.16	648.39
5	26,495.82	57	37	20	64.91	1,570.13	4,683.84	-1,579.95	-4,459.24	0.99	1.84	464.84
4	23,220.21	60	37	23	61.67	1,417.50	4,518.75	-1,270.75	-4,368.22	1.12	1.79	387.00
3	14,932.43	62	40	22	64.52	1,119.79	3,216.85	-1,357.23	-3,332.96	0.83	1.50	240.85
2	5,161.65	63	38	25	60.32	834.85	2,830.24	-1,062.51	-3,844.10	0.79	1.19	81.93
1	7,887.44	75	42	33	56.00	638.35	2,368.66	-573.44	-2,302.95	1.11	1.42	105.17

The statistics appear to suggest a solid bullish edge over the next couple of weeks. Below is an equity curve using a 10-day exit strategy that shows how the edge has played out over time.

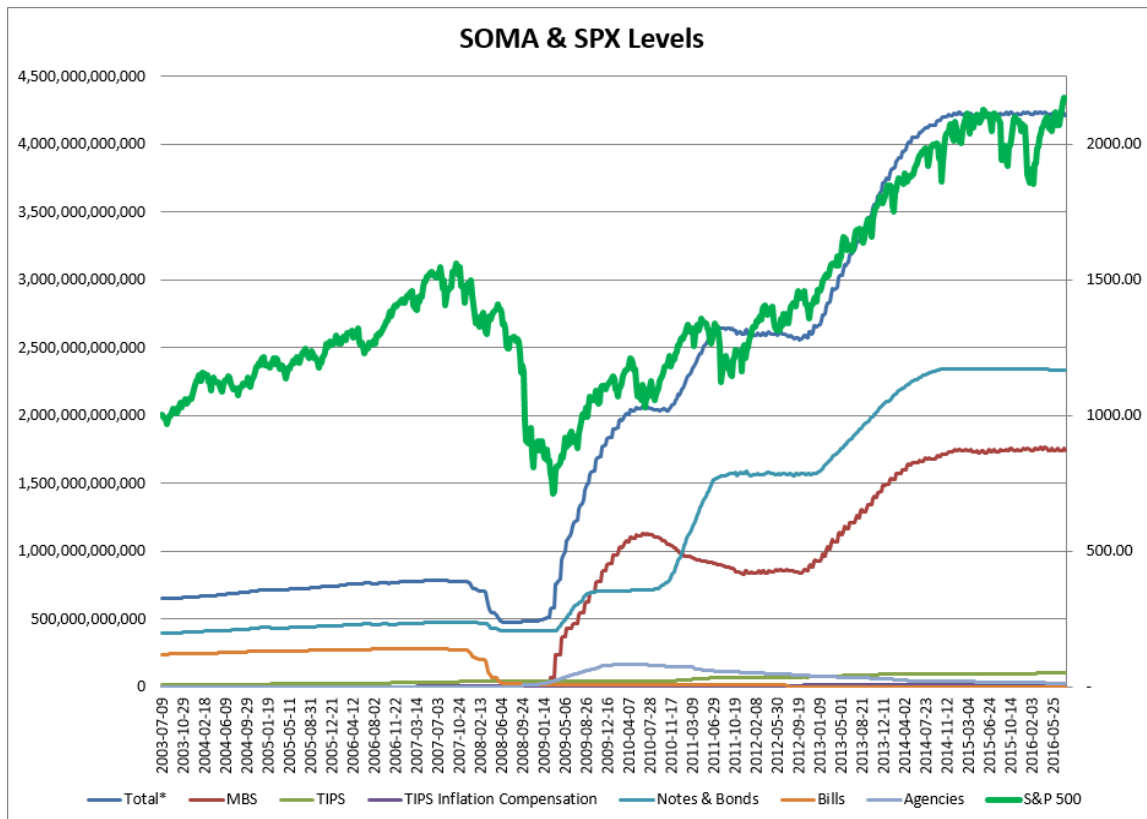


There has been a little bit of a struggle lately, but the overall profit curve is impressive enough that I have included this study on the intermediate-term active list tonight.

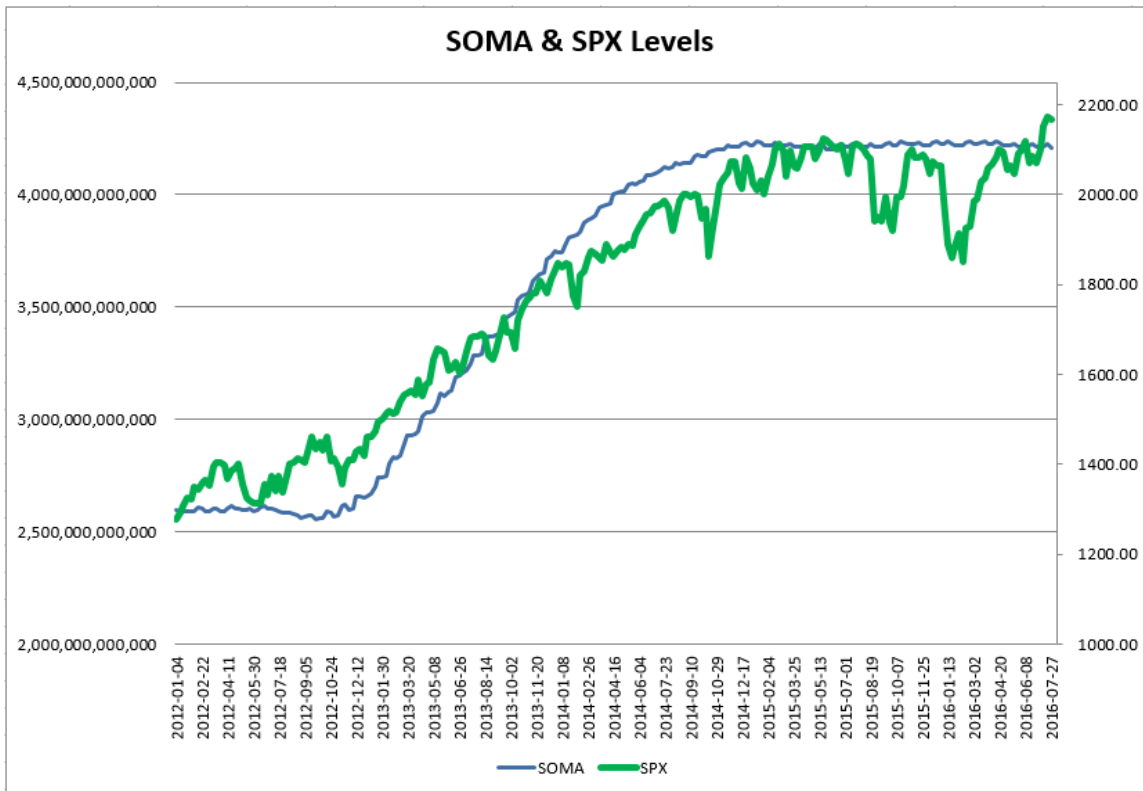
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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 declined this past week (Wednesday to Wednesday) a fairly large 0.38%. I indicated in last week's letter that I expected a decline based on the Fed's past reinvestment schedule. The 0.3% loss for the SPX over this period is in accordance with a week that the SOMA posts losses. Since the beginning of 2015 SPX has risen 67% of the time for a sum total of 10.58% during SOMA expansion weeks (of at least 0.01%). During all other weeks SPX has only risen 45% of the time and has *lost* a sum total of 4.15%. 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 come in pretty flat. And the following week the SOMA is expected to come in flat again. So it appears the bulls won't be getting much liquidity support from the Fed 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. This weekend's high volume study appears to be encouraging. And some breakout studies from a few weeks ago suggest 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 though, including overall weak Fed support and the long-term new-high breadth divergence. With all this to consider and the market again near 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

MO @ \$66.76 (buy 1/3 at limit)

Broad Market Large Cap CBI – 1(MO)

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	\$33.69	36.40%		Aggressive VIX
MO(1/3)	7/28/2016	\$66.75	\$67.70	1.42%		Catapult

Market expectations are bullish and contango is extremely high at over 18%. Those things continue to favor XIV. I'll look to ride it until the outlook worsens.

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.