

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

October 24, 2016

Volume 9 Issue 206

## Market Overview



## Signals Overview

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

## Tonight's Research Points

- When the VIX moves from 10% above the 10ma to 10% below the 10ma in less than a week it has been typically followed by gains.
- SPY's mild up close near the top of its range suggests a bearish 1-day edge.
- SOMA is expected to come in flat to lower over the next few weeks.

## *Short-term Outlook*

### *The Bottom Line*

Evidence is mixed but pointing higher and the SPX is a bit oversold. If it sells off an more on Monday I'll be looking to get long.

*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>						
October 24, 2016	SPY up < 0.25% but top 10% of range	1 day	Bearish			
October 24, 2016	VIX 10% above to 10% below 10ma in 4	1-5 days	Bullish			
October 19, 2016	20 low yesterday. 4 high today.	1-8 days	Bullish	2.30%	-1.50%	-3.10%
<b>Active - Long Term</b>						
October 19, 2016	20 low yesterday. 4 high today.	1-20 days	Bullish	3.80%	-2.10%	-4.50%
July 11, 2016	NASDAQ leading	int term	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	290% 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>						
October 18, 2016	20-low on a Monday	1-4 days	Bullish			

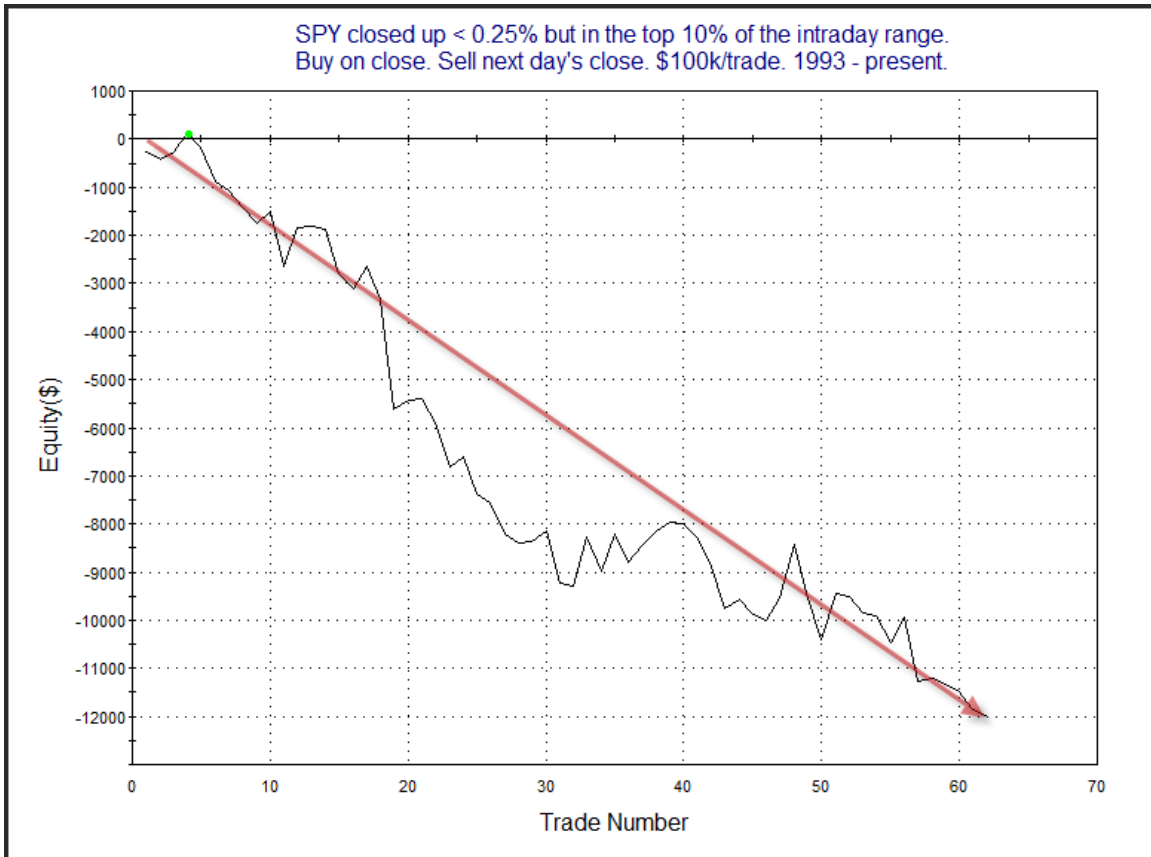
**The Evidence**

Friday was a mixed and mild day for the market. The SPX finished the day a mere 0.18 points, the NASDAQ gained 0.3%, and the Russell 2000 declined 0.1%. Breadth was a little negative as the NYSE Up Issues % was just under 50% and the Up Volume % came in at 45%. NYSE volume rose from Thursday's level as it typically does on opex Friday.

Though the action was fairly mild, we did see a mix of interesting studies appear in the Quantifinder. The first study was last seen in the 8/19/16 subscriber letter. It suggests that when SPY closes strong (in the top 10% of its range) but still only manages a small gain on the day, that the next day has a downside tendency. Stats are updated.

TradeStation Performance Summary <span style="float: right;">Expand ▾</span>			
<b>All Trades</b>			
Total Net Profit	(\$12,010.67)	Profit Factor	0.42
Gross Profit	\$8,782.24	Gross Loss	(\$20,792.91)
Total Number of Trades	62	Percent Profitable	35.48%
Winning Trades	22	Losing Trades	40
Even Trades	0		
Avg. Trade Net Profit	(\$193.72)	Ratio Avg. Win:Avg. Loss	0.77
Avg. Winning Trade	\$399.19	Avg. Losing Trade	(\$519.82)
Largest Winning Trade	\$1,093.35	Largest Losing Trade	(\$2,290.72)

As you can see there appears to be a bit of a bearish inclination. Below is a profit curve showing how the edge has played out over time.



It appears that when the market needs to expend a fair amount of energy just to squeak out a small gain, that its lack of momentum is often followed by a swing back in the opposite direction the next day. One concern I have with the current setup is that while SPY did close up slightly, SPX did not. Still, I have included this study on the Active List for tonight.

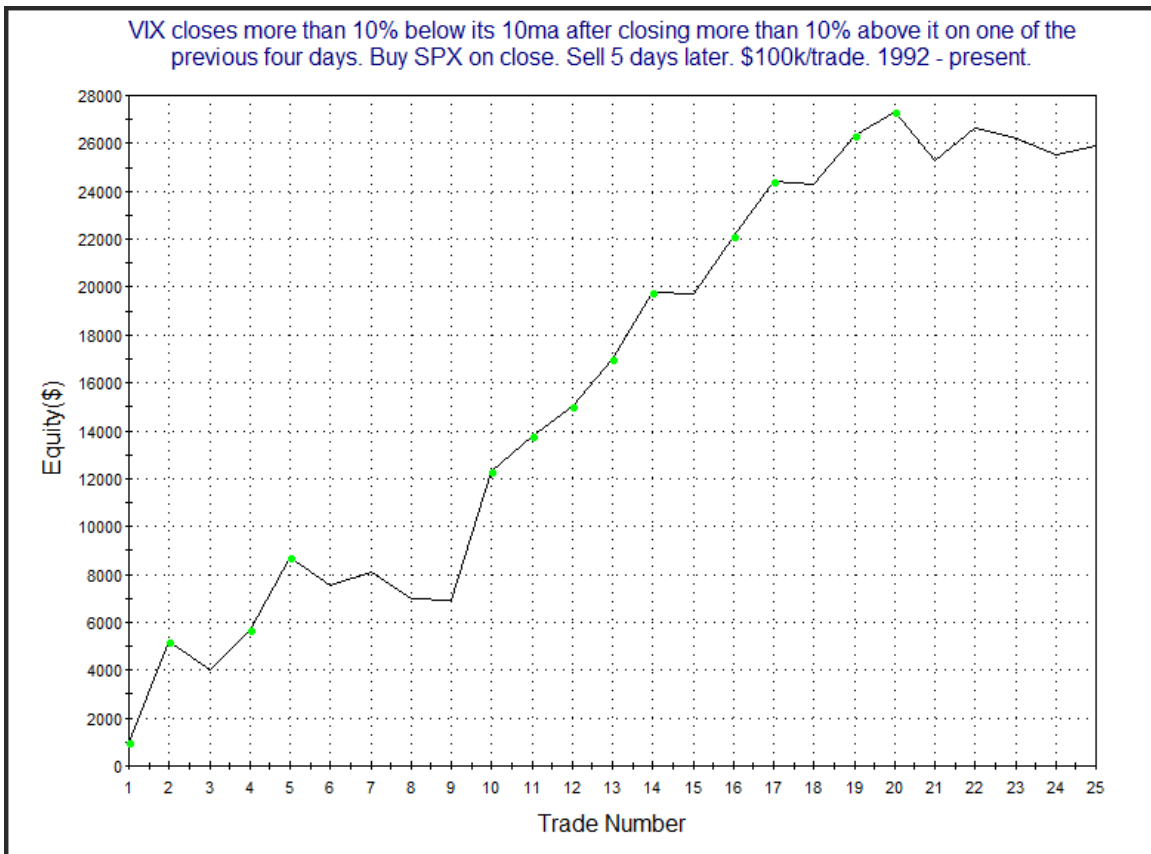
After closing at 16.21 on Monday, the VIX closed Friday at 13.34. The VIX is a measure of expected volatility in the market, and it tends to move up and down counter to the SPX. The Quantifinder study below considered the sharp drop in the VIX over the last few days after previously being extended upwards. It was last seen in the 9/22/16 subscriber letter. The results are updated.

VIX closes more than 10% below its 10ma after closing more than 10% above it on one of the previous four days. Buy SPX on close. Sell X days later. \$100k/trade. 1992 - 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	29,235.32	25	17	8	68.00	2,470.25	8,115.80	-1,594.86	-3,412.50	1.55	3.29	1,169.41
9	28,359.40	25	16	9	64.00	2,294.07	8,397.40	-927.30	-2,403.36	2.47	4.40	1,134.38
8	31,746.24	25	18	7	72.00	2,082.54	8,076.20	-819.92	-1,858.85	2.54	6.53	1,269.85
7	29,664.43	25	18	7	72.00	2,025.62	7,749.50	-970.96	-2,030.40	2.09	5.36	1,186.58
6	26,760.63	25	17	8	68.00	2,007.09	5,305.30	-919.98	-3,271.68	2.18	4.64	1,070.43
5	25,928.33	25	16	9	64.00	2,041.19	5,361.40	-747.86	-2,011.20	2.73	4.85	1,037.13
4	15,137.39	26	19	7	73.08	1,356.84	4,981.90	-1,520.36	-2,927.52	0.89	2.42	582.21
3	6,077.03	27	16	11	59.26	1,106.23	3,799.40	-1,056.61	-3,629.81	1.05	1.52	225.08
2	4,263.60	27	15	12	55.56	1,025.09	3,839.00	-926.06	-5,300.66	1.11	1.38	157.91
1	4,937.27	27	16	11	59.26	760.90	2,952.40	-657.91	-3,572.94	1.16	1.68	182.86

The market condition that would typically accompany such VIX movement is one where you see a strong rebound from a sharp decline during a long-term uptrend. That is not really the case in this instance. Results of the study appear especially strong and consistent between days 4 and 8. Below I have provided the profit curve assuming a 5 day holding period.

VIX closes more than 10% below its 10ma after closing more than 10% above it on one of the previous four days. Buy SPX on close. Sell 5 days later. \$100k/trade. 1992 - present.



Despite recent struggles this curve appears pretty good. It seems to support the idea of an upside edge. I have included this study on the Active List tonight.

I have updated the Aggregator chart below.



With the mix of new evidence tonight the green Aggregator Line 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 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. Therefore, the Aggregator signal stayed long at the close.

If nothing new emerges on Monday, net expectations will remain positive. It would take some strong bearish evidence on Monday to change this. The Differential Pivot will be 2157.91 on Monday. That is 0.8% above Friday's close. Therefore, SPX would need to close up at least 0.8% on Monday in order to move from oversold to overbought versus recent expectations.

So Monday is “iffy” based on the 1<sup>st</sup> study I showed above. But there does appear to be an upside edge over the next few days. And there is some room to profit before the SPX would turn overbought versus recent expectations. If Monday does close lower as that study suggested is likely, then that would mean a 3-day pullback going into a Turnaround Tuesday. And that would certainly generate some bullish studies. I am not going to look for index exposure right here, but I do want to get into a trade Monday afternoon if the market suffers another down day. Of course more aggressive traders could look to take advantage of the potential short-term bullish edge ahead of Monday’s close.

***Intermediate-term Outlook (2 weeks – 2 months) – updated 10/24 – bullish***

<b>Combo #1</b>	<b>Combo #2</b>	<b>Combo #3</b>
<b>Long</b>	<b>Long</b>	<b>Long</b>

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”.*

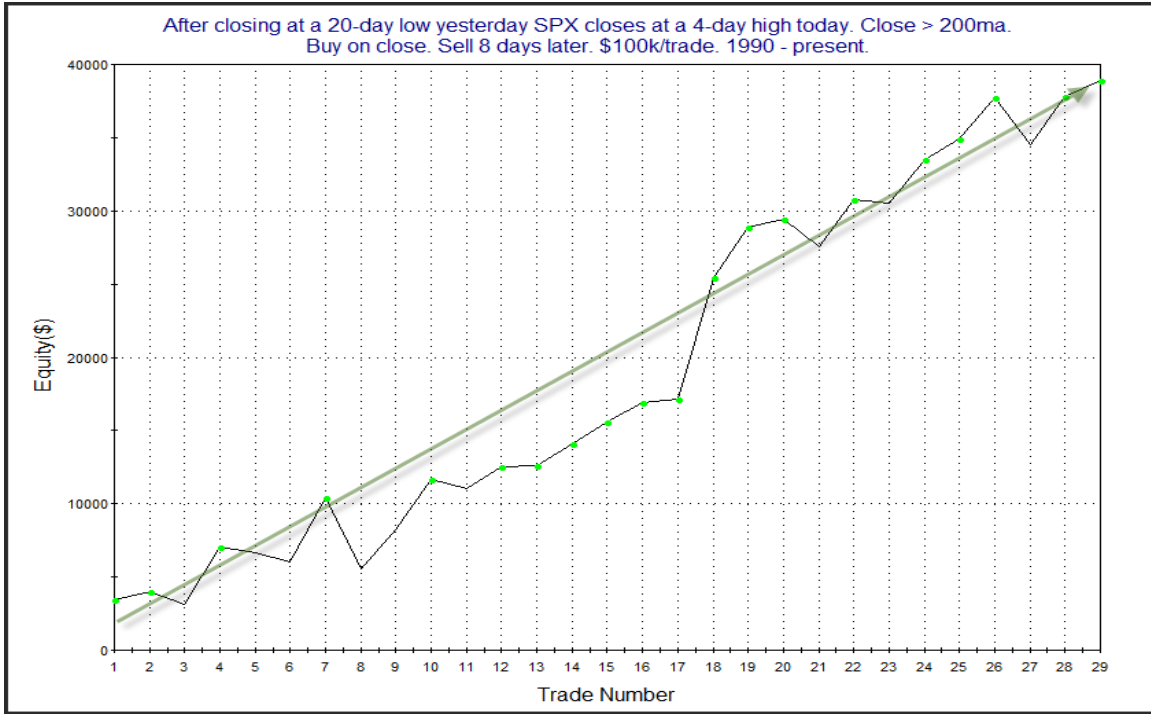
The SPX finished the week up 0.4%. The trend appears pretty questionable, but most long-term measures we look at are still pointing higher. There was one new study with intermediate-term implications that emerged this past week. It was seen in Tuesday night’s letter. I have copied it below.

*Tuesday was a strong enough move that we saw SPX go from closing at a 20-day low on Monday to closing at a 4-day high on Tuesday. In the 5/17/16 letter I looked at other times in which the market put in a strong thrust off a 20-day low. There I required a close of at least a 4-day high. I have updated the results below.*

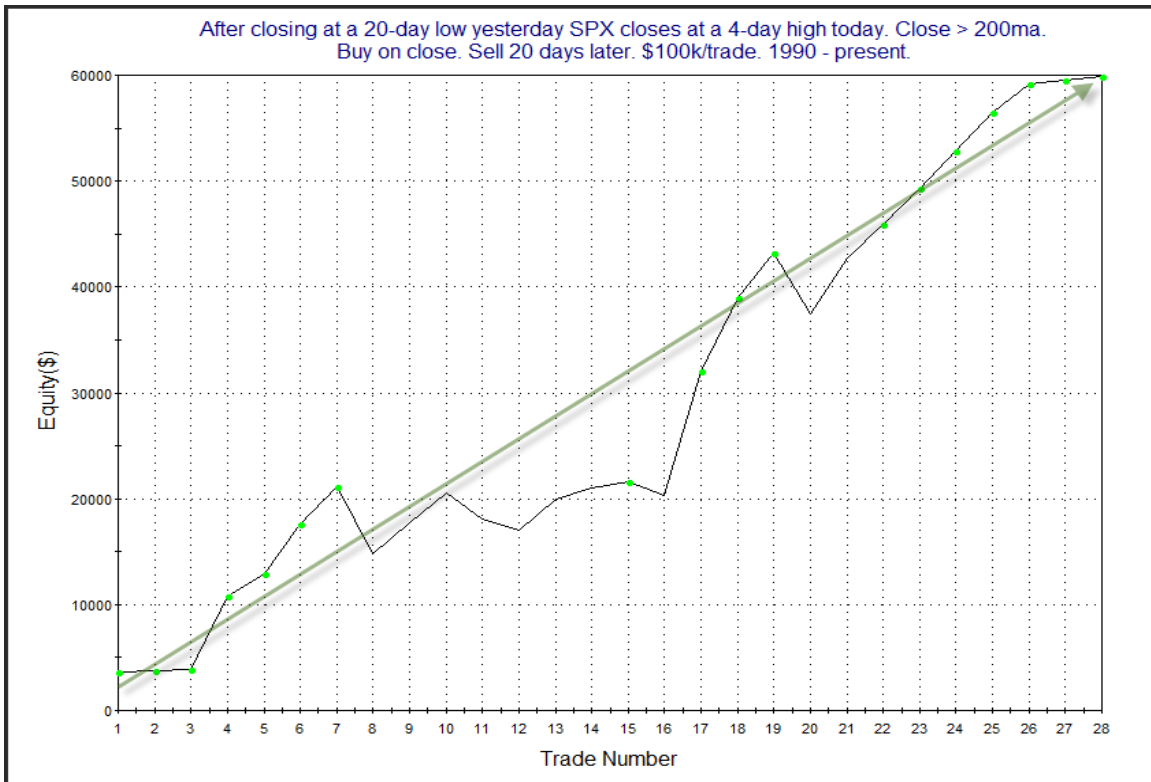
After closing at a 20-day low yesterday SPX closes at a 4-day high today. Close > 200ma.  
Buy on close. Sell X days later. \$100k/trade. 1990 - present.

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
20	59,908.44	28	23	5	82.14	3,337.94	11,665.50	-3,372.85	-6,379.08	0.99	4.55	2,139.59
19	58,955.86	28	21	7	75.00	3,657.85	12,037.30	-2,551.29	-6,347.80	1.43	4.30	2,105.57
18	53,917.52	29	23	6	79.31	2,984.68	10,563.30	-2,455.00	-4,148.97	1.22	4.66	1,859.22
17	54,026.31	29	23	6	79.31	3,036.60	11,183.70	-2,635.90	-4,247.96	1.15	4.42	1,862.98
16	51,627.88	29	22	7	75.86	3,005.47	11,506.00	-2,070.35	-4,320.78	1.45	4.56	1,780.27
15	49,212.83	29	21	8	72.41	3,027.88	11,173.80	-1,796.58	-4,723.96	1.69	4.42	1,696.99
14	47,642.58	29	23	6	79.31	2,786.69	9,507.30	-2,741.90	-7,897.52	1.02	3.90	1,642.85
13	40,159.00	29	22	7	75.86	2,544.33	9,427.00	-2,259.47	-7,363.04	1.13	3.54	1,384.79
12	39,261.12	29	20	9	68.97	2,666.97	8,151.00	-1,564.24	-5,686.84	1.70	3.79	1,353.83
11	45,183.52	29	23	6	79.31	2,454.04	8,642.70	-1,876.57	-5,722.20	1.31	5.01	1,558.05
10	41,233.40	29	22	7	75.86	2,548.76	8,924.30	-2,119.89	-8,745.48	1.20	3.78	1,421.84
9	40,470.60	29	21	8	72.41	2,458.57	8,603.10	-1,394.91	-6,371.60	1.76	4.63	1,395.54
8	38,933.14	29	21	8	72.41	2,463.00	8,276.40	-1,598.74	-4,917.08	1.54	4.04	1,342.52
7	28,175.42	29	20	9	68.97	2,262.21	5,832.20	-1,896.53	-4,106.50	1.19	2.65	971.57
6	23,209.06	29	18	11	62.07	2,196.70	5,888.30	-1,484.69	-5,306.50	1.48	2.42	800.31
5	18,655.11	29	17	12	58.62	2,024.90	5,508.80	-1,314.02	-5,320.00	1.54	2.18	643.28
4	19,747.00	30	20	10	66.67	1,760.67	4,326.30	-1,546.65	-4,559.50	1.14	2.28	658.23
3	15,843.77	30	20	10	66.67	1,568.49	4,365.90	-1,552.60	-4,707.50	1.01	2.02	528.13
2	12,894.75	31	22	9	70.97	1,149.11	3,479.30	-1,376.19	-3,138.00	0.83	2.04	415.96
1	364.27	31	14	17	45.16	806.72	2,536.10	-642.93	-2,034.00	1.25	1.03	11.75

Day 1 is a bit iffy, but after that there appears to be a strong and consistent edge over the next 4 weeks. This suggests a good chance that Tuesday's rally was the beginning of a continued move higher. I produced profit curves for the 8-day and 20-day holding periods highlighted above. First, the 8 day...



*The strong, steady upslope for the 8-day period is impressive and serves as confirmation of the upside edge. Now the 20-day curve.*



*This one is a little choppier, but it sure has been strong lately, with 11 of the last 12 instances all closing higher. In the 5/17/16 letter I also looked at bounces that did **not** reach 4-day highs the 1<sup>st</sup> day. I have updated that table below as well.*

After closing at a 20-day low yesterday SPX up but < 4-day high today. Close > 200ma. Buy on close. Sell X days later. \$100k/trade. 1990 - 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
20	98,679.41	81	57	24	70.37	3,086.91	12,927.20	-3,219.78	-9,587.72	0.96	2.28	1,218.26
19	90,223.25	81	57	24	70.37	2,856.93	13,564.52	-3,025.90	-12,375.24	0.94	2.24	1,113.87
18	97,662.29	83	57	26	68.67	2,998.46	13,895.61	-2,817.31	-13,625.69	1.06	2.33	1,176.65
17	87,679.80	84	57	27	67.86	2,916.34	13,554.35	-2,909.31	-10,959.00	1.00	2.12	1,043.81
16	84,288.88	84	54	30	64.29	3,055.21	11,842.40	-2,689.75	-9,466.89	1.14	2.04	1,003.44
15	84,025.77	87	57	30	65.52	2,830.87	11,759.91	-2,577.80	-7,655.72	1.10	2.09	965.81
14	82,029.17	87	59	28	67.82	2,580.23	10,449.11	-2,507.29	-7,789.32	1.03	2.17	942.86
13	88,034.30	88	59	29	67.05	2,580.22	10,954.22	-2,213.74	-6,510.77	1.17	2.37	1,000.39
12	55,309.90	91	56	35	61.54	2,473.99	11,243.50	-2,378.10	-8,570.72	1.04	1.66	607.80
11	64,376.68	94	59	35	62.77	2,451.06	10,913.54	-2,292.46	-8,225.72	1.07	1.80	684.86
10	53,837.91	96	59	37	61.46	2,344.81	10,577.93	-2,283.95	-11,602.12	1.03	1.64	560.81
9	69,963.51	98	63	35	64.29	2,212.16	8,067.07	-1,982.94	-6,195.44	1.12	2.01	713.91
8	77,974.15	101	71	30	70.30	2,014.04	8,124.70	-2,167.42	-7,580.04	0.93	2.20	772.02
7	100,751.69	103	74	29	71.84	2,056.10	7,734.85	-1,772.42	-5,195.64	1.16	2.96	978.17
6	84,654.10	107	75	32	70.09	1,908.65	6,520.10	-1,827.95	-5,822.32	1.04	2.45	791.16
5	69,451.38	111	72	39	64.86	1,896.10	6,560.78	-1,719.69	-5,937.53	1.10	2.04	625.69
4	56,432.27	118	78	40	66.10	1,467.14	5,650.00	-1,450.12	-5,345.28	1.01	1.97	478.24
3	44,596.07	125	80	45	64.00	1,171.24	3,939.79	-1,091.18	-6,154.38	1.07	1.91	356.77
2	41,254.89	139	86	53	61.87	1,029.09	3,644.28	-891.46	-2,742.74	1.15	1.87	296.80
1	22,535.05	139	83	56	59.71	771.99	2,937.71	-741.79	-2,525.60	1.04	1.54	162.12

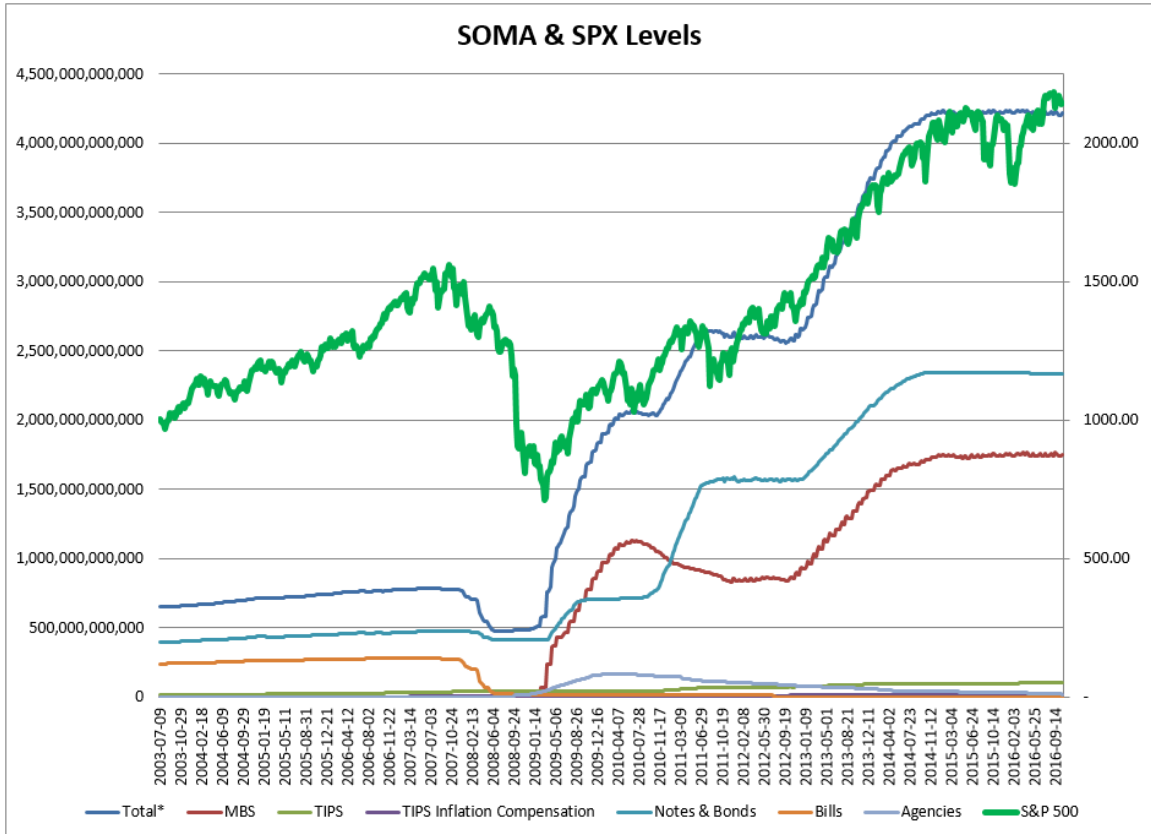
*Results here are pretty good and also seem to favor more upside. But if you compare the “Avg Trade” column on the far right you’ll find that from Day 2 – Day 19 the Avg Trade here was about **one-half to two-thirds** the Avg Trade when the 1<sup>st</sup> day jumped SPX up to a 4-day high. Overall, the 1st study above appears worthy of both the short and intermediate-term Active Lists.*

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.

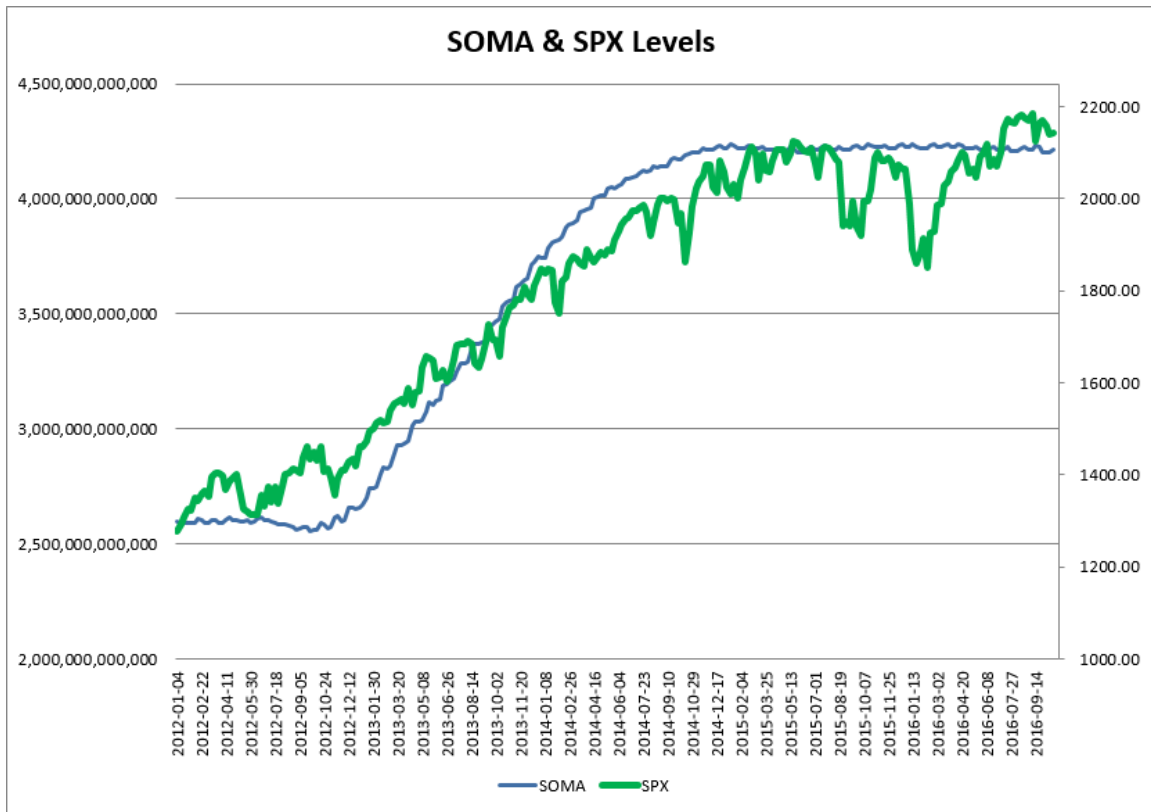
*SOMA stands for System Open Market Account. It is the account at the Fed that contains all of its bond purchase holdings. We have tracked Fed purchases for several years, and as is evident in the charts below, the stock market has consistently reacted positively when the Fed has been buying securities 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 saw a solid rise this past this past week (Wednesday to Wednesday), posting a gain of 0.28%. This was in line with expectations based on the Fed’s SOMA schedule. The 0.24% rise for the SPX over this period is typical for a week the SOMA rises. Since the beginning of 2015 SPX has risen 65% of the time for a sum total of 8.06% 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 2.60%. Based on the reinvestment schedule the Fed has stuck to over the last year and a half, this current week, which ends on Wednesday, should see the SOMA decline some. And the week after that is likely to either come in flat or down a little. So Fed liquidity will be lacking for at least the next week and a half.

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.

Overall, the intermediate-term outlook remains positive. Three of our four Market Timing Course indicators are bullish, which has historically been quite promising. And this week’s study that examined the strong bounce from the 20-day low appears encouraging. There are also some past breadth related studies that suggest that the market is likely to continue higher. There is still some bearish evidence though, including overall weak Fed support

and the long-term new-high breadth divergence. With the new evidence this week I have moved my outlook back from “somewhat bullish” to “bullish”. I will be looking primarily at the long side for trading opportunities, and will be extra selective with possible short trades.

### **Catapult and Capitulative Breadth Statistics**

*Catapult & CBI Presentation Link*

#### ***Open Catapult Triggers***

PFE @ \$32.66 (bought 1/3 at limit)

PFE @ \$32.50 (buy 1/3 at limit) – not filled – try again on Monday

*New*

T @ \$37.49 (buy 1/3 at limit)

#### ***Broad Market Large Cap CBI – 3(PFE-2, T)***

### **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.*

**PFE – buy 1/3 Catapult position @ \$32.18 LIMIT.** This is from the Catapult section above. It is the 2<sup>nd</sup> of 3 possible lots for PFE.

**T – buy 1/3 Catapult position @ \$37.49 LIMIT.** This is from the Catapult section above. It is the 1<sup>st</sup> of 3 possible lots for T.

**SPY – buy ¼ index position @ \$213.98 LIMIT ON CLOSE.** Based on the short-term outlook above, if SPY closes flat or down on Monday, I will be a buyer.

### Current Open Trade Ideas

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
PFE(1/3)	10/17/2016	\$32.58	\$32.18	-1.23%		Catapult

A complete list of Quantifiable Edges trade idea results since the inception of the letter in 2008 [can be found here](#).

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