

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

November 21, 2016

Volume 9 Issue 226

Market Overview



Signals Overview

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

Tonight's Research Points

- The SPY gap and reversal on Friday after an unfilled gap up on Thursday suggests an upside edge for Monday.
- Relatively strong drops from 50-day highs have consistently been followed by bounces.
- Thanksgiving week has been seasonally bullish

Short-term Outlook

The Bottom Line

The Aggregator is bullish. I would prefer a bit more of a pullback before considering a long 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						
November 17, 2016	Unfilled gap dn from 20hi after unfill up	1 day	Bearish			
November 8, 2016	20 low yesterday. 4 high today.	1-8 days	Bullish			
Active - Long Term						
November 11, 2016	SPX 20-high. NDX biggest drop in 20.	1-50 days	Bullish			
November 8, 2016	20 low yesterday. 4 high today.	1-20 days	Bullish	3.80%	-2.10%	-4.50%
April 26, 2016	Golden Cross	int term	Bullish			
November 3, 2014	Quantitative Easing Ends	int term	Bearish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			
Dropped Tonight						

The Evidence

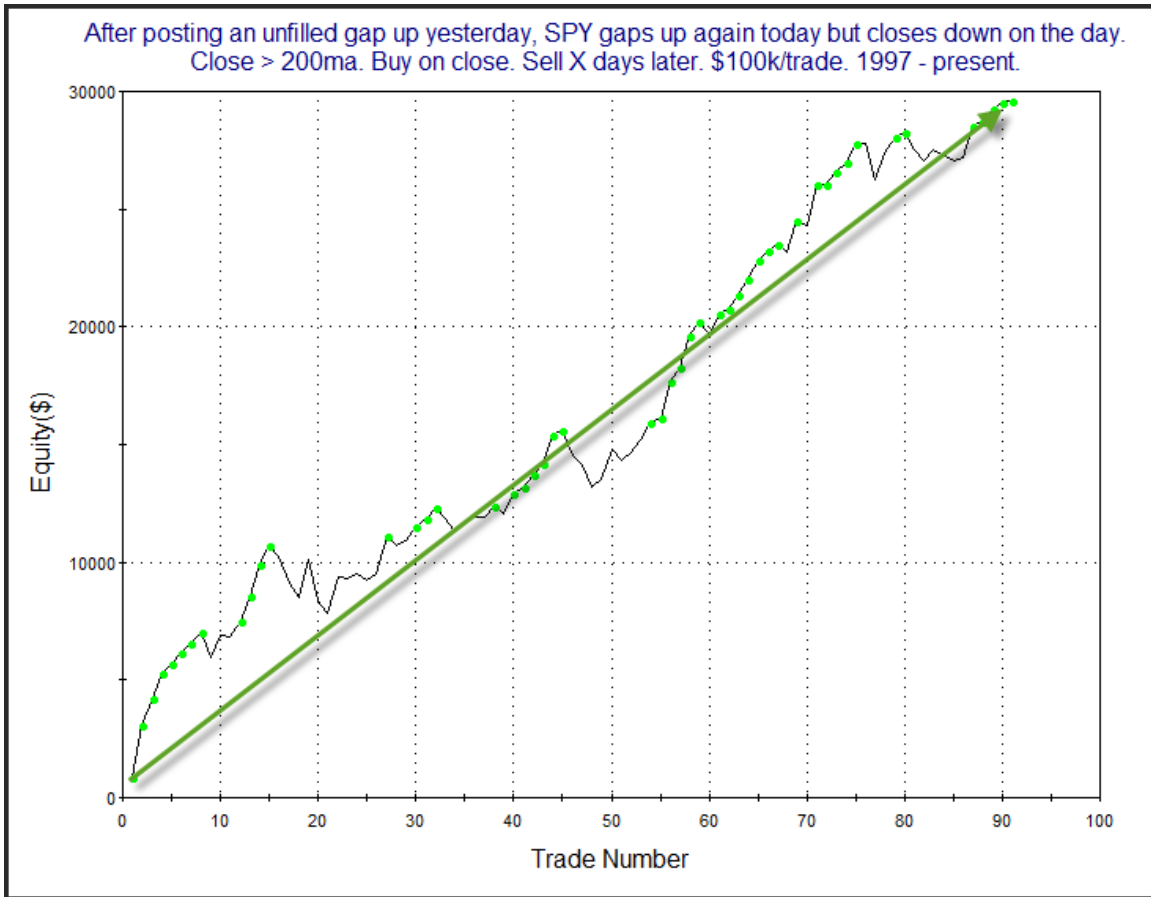
Friday saw mixed returns. The SPX lost 0.2%, the NASDAQ fell 0.2%, and the Russell 2000 was rose 0.5%. Breadth was negative as the NYSE Up Issues % was 47% and the Up Volume % came in at 44%. NYSE volume rose a little from Thursday's level.

There were a few interesting studies that triggered in the Quantifinder. In the 4/22/15 letter I examined similar price action in SPY with regards to how it gapped and finished. I found that gains had been pretty consistent the next day after similar action. The study is updated below.

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

TradeStation Performance Summary				Expand ▾
All Trades				
Total Net Profit	\$29,585.86	Profit Factor		3.01
Gross Profit	\$44,340.87	Gross Loss		(\$14,755.01)
Total Number of Trades	91	Percent Profitable		71.43%
Winning Trades	65	Losing Trades		26
Even Trades	0			
Avg. Trade Net Profit	\$325.12	Ratio Avg. Win:Avg. Loss		1.20
Avg. Winning Trade	\$682.17	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.



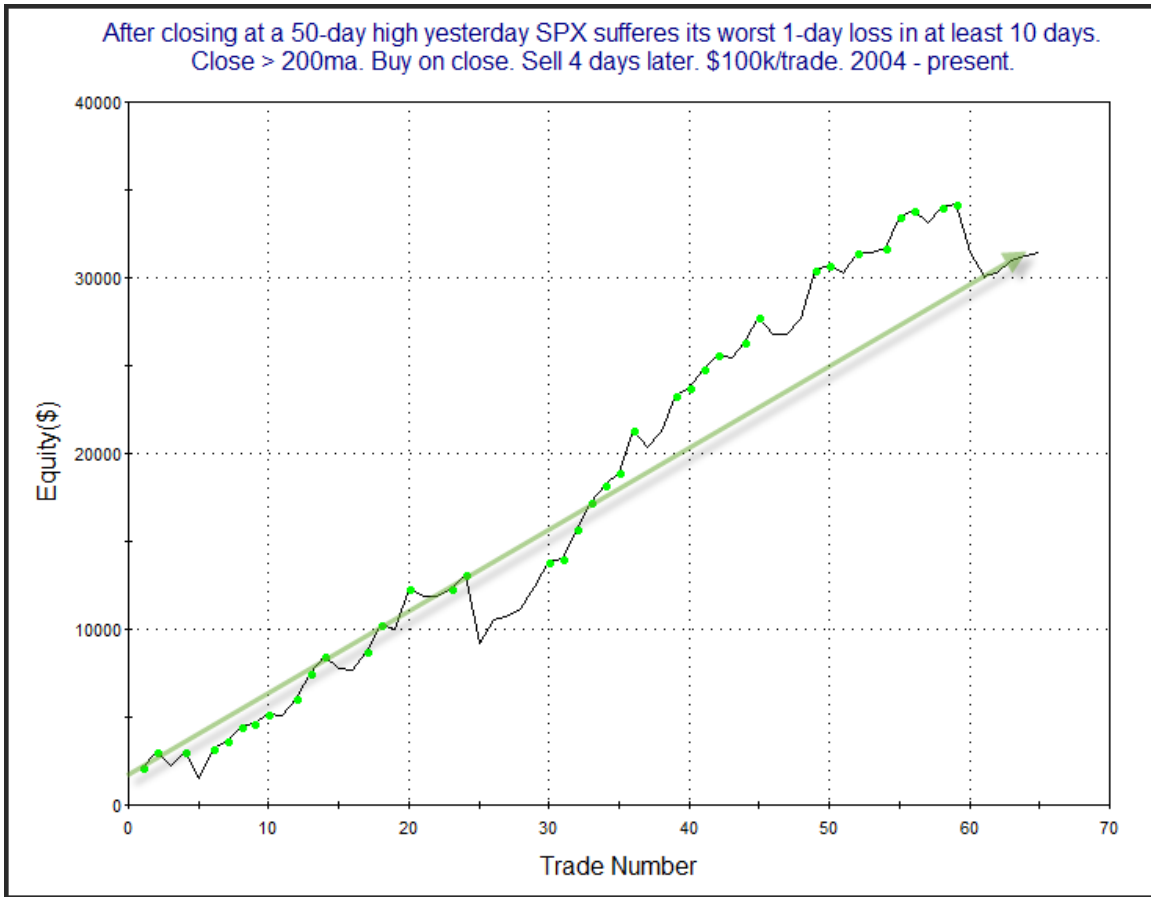
The strong, steady upslope is encouraging. Based on the action of the last 2 days, it appears an up day on Monday is fairly likely. I have included this study on the Active List tonight.

The study below looks at *relatively* large drops from intermediate-term highs. It was last seen in the 8/17/16 letter. 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	24,700.43	61	42	19	68.85	1,220.60	3,149.37	-1,398.14	-3,454.00	0.87	1.93	404.93
4	31,428.85	65	47	18	72.31	991.84	2,725.38	-843.76	-3,895.76	1.18	3.07	483.52
3	24,160.14	66	48	18	72.73	796.19	2,192.40	-780.95	-1,808.21	1.02	2.72	366.06
2	14,180.10	68	39	29	57.35	764.01	2,437.50	-538.49	-1,777.55	1.42	1.91	208.53
1	6,872.20	68	40	28	58.82	514.41	1,521.72	-489.43	-1,354.59	1.05	1.50	101.06

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 recent struggles, the steady upslope seems to confirm the bullish inclination. This study is on the Active List tonight.

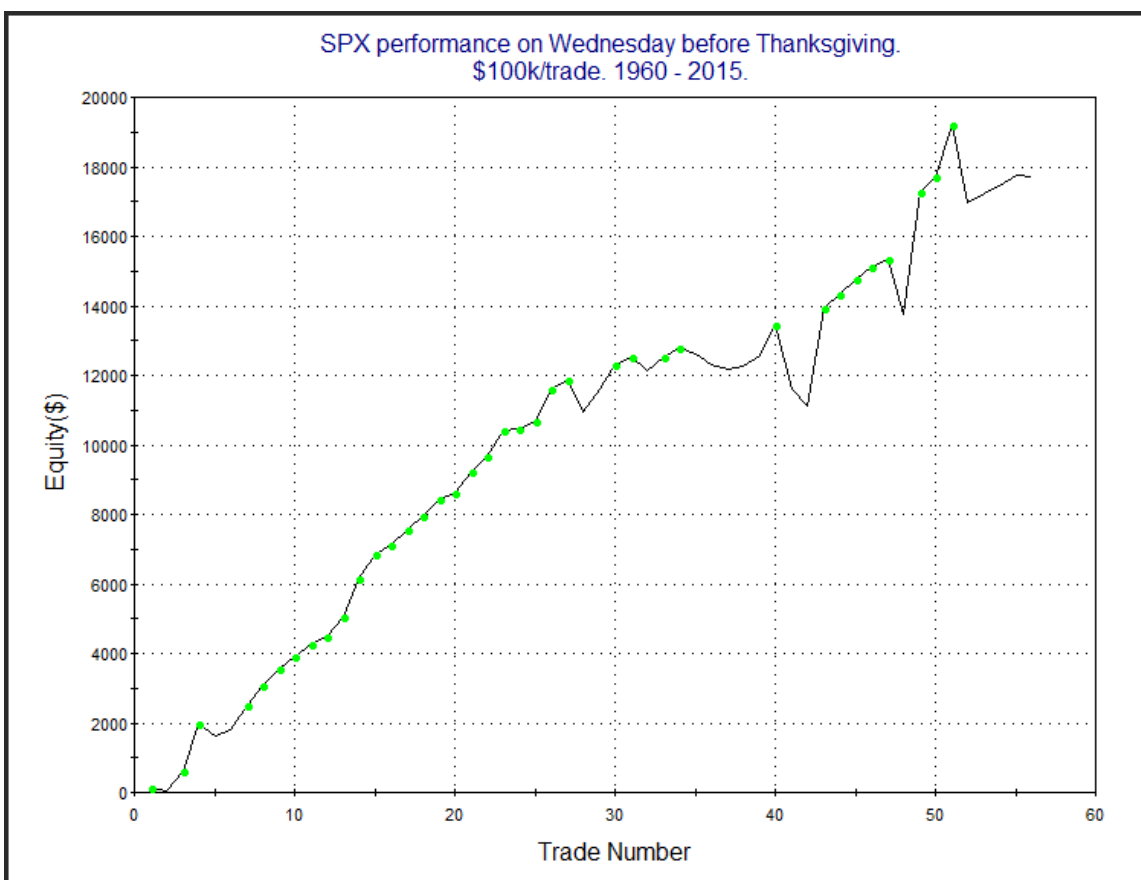
Thanksgiving week has shown some strong seasonal tendencies over the years. This is something I last showed in the 11/23/15 subscriber letter. I have re-run those studies and updated them below.

This first one breaks down performance during Thanksgiving week by day.

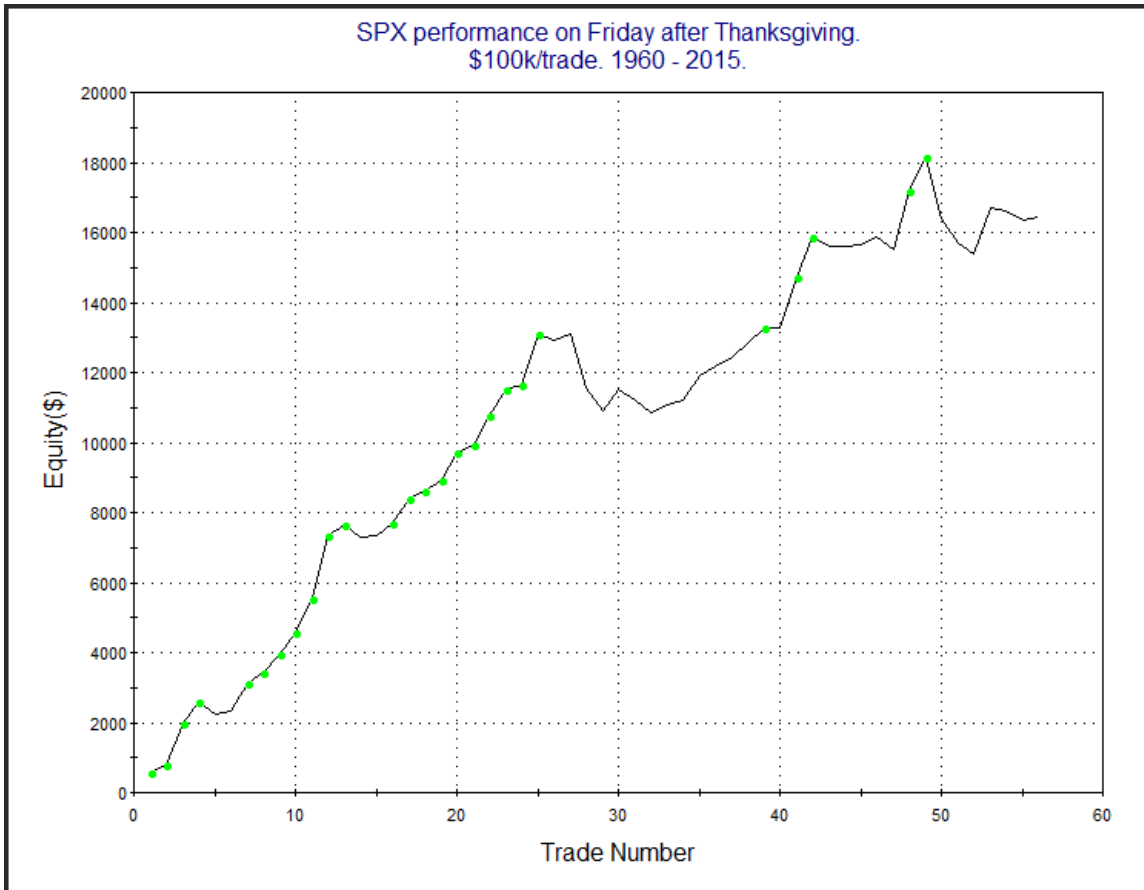
Thanksgiving Week Performance Broken Down By Day of Week.
Based on \$100k/trade in SPX. 1960 - 2015.

Day	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
Mon After	-20,544.72	56	20	36	35.71	911.59	2,913.68	-1,077.12	-8,883.33	0.85	0.47	-366.87
Fri	16,424.73	56	40	16	71.43	596.57	1,782.27	-464.87	-1,721.70	1.28	3.21	293.30
Wed	17,729.84	56	44	12	78.57	596.48	3,513.64	-709.59	-2,205.00	0.84	3.08	316.60
Tues	2,250.50	56	33	23	58.93	565.40	1,581.95	-713.38	-2,093.99	0.79	1.14	40.19
Mon	2,579.05	56	25	31	44.64	1,077.07	6,420.72	-785.41	-3,049.54	1.37	1.11	46.05

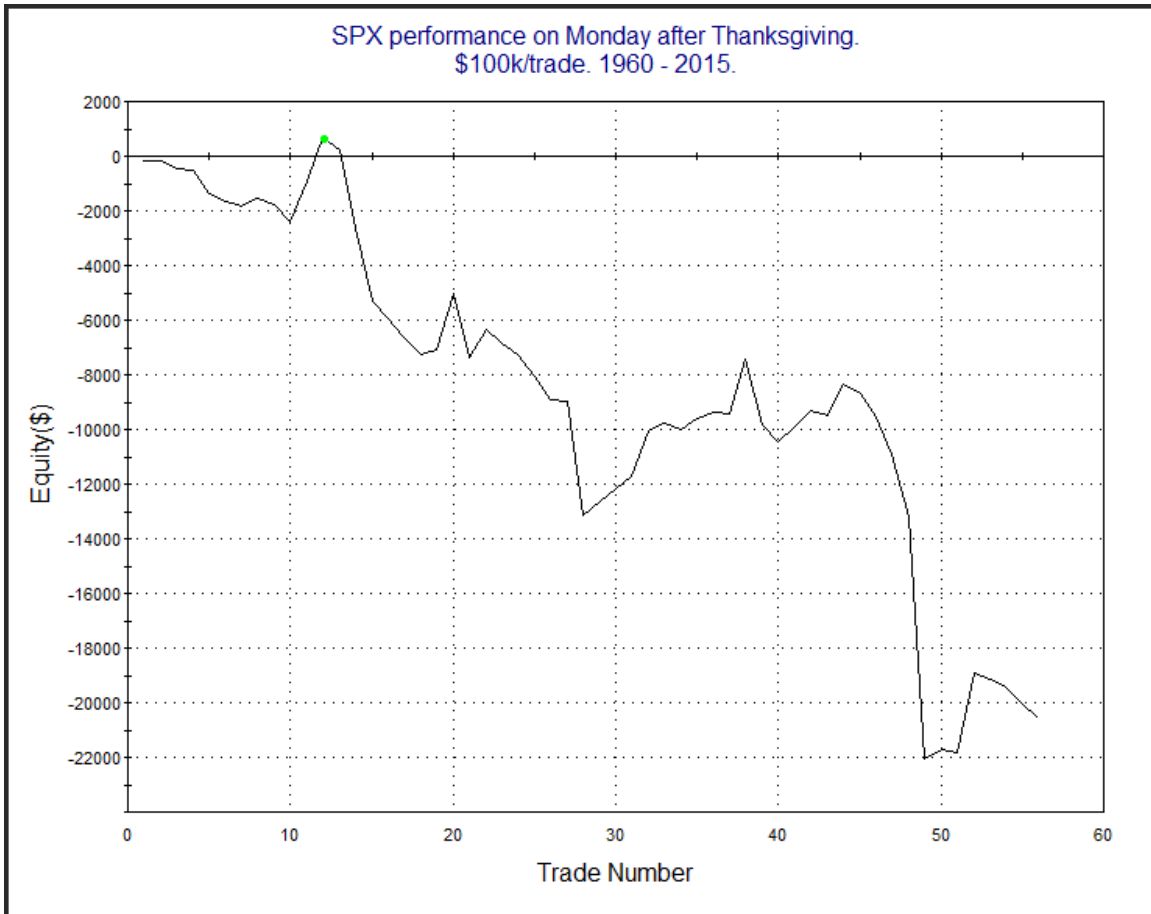
Monday and Tuesday don't show anything suggesting an edge. Wednesday and Friday, on the other hand, appear to be strongly bullish. And the Monday after Thanksgiving appears to exhibit a possible bearish edge. But before we jump to conclusions, let's examine the profit curves for Wednesday, Friday, and the following Monday. First below is Wednesday.



This curve looks to be strong. While there were a few bad Wednesdays, they were overwhelmed by the good ones. The next chart looks at Fridays after Thanksgiving.



This curve doesn't appear quite as strong as the Wednesday curve. Still, the general upslope still appears to be intact. To me it appears both Wednesday and Friday contain a seasonal upside edge. Now let's look at what has happened on the Monday after Thanksgiving.



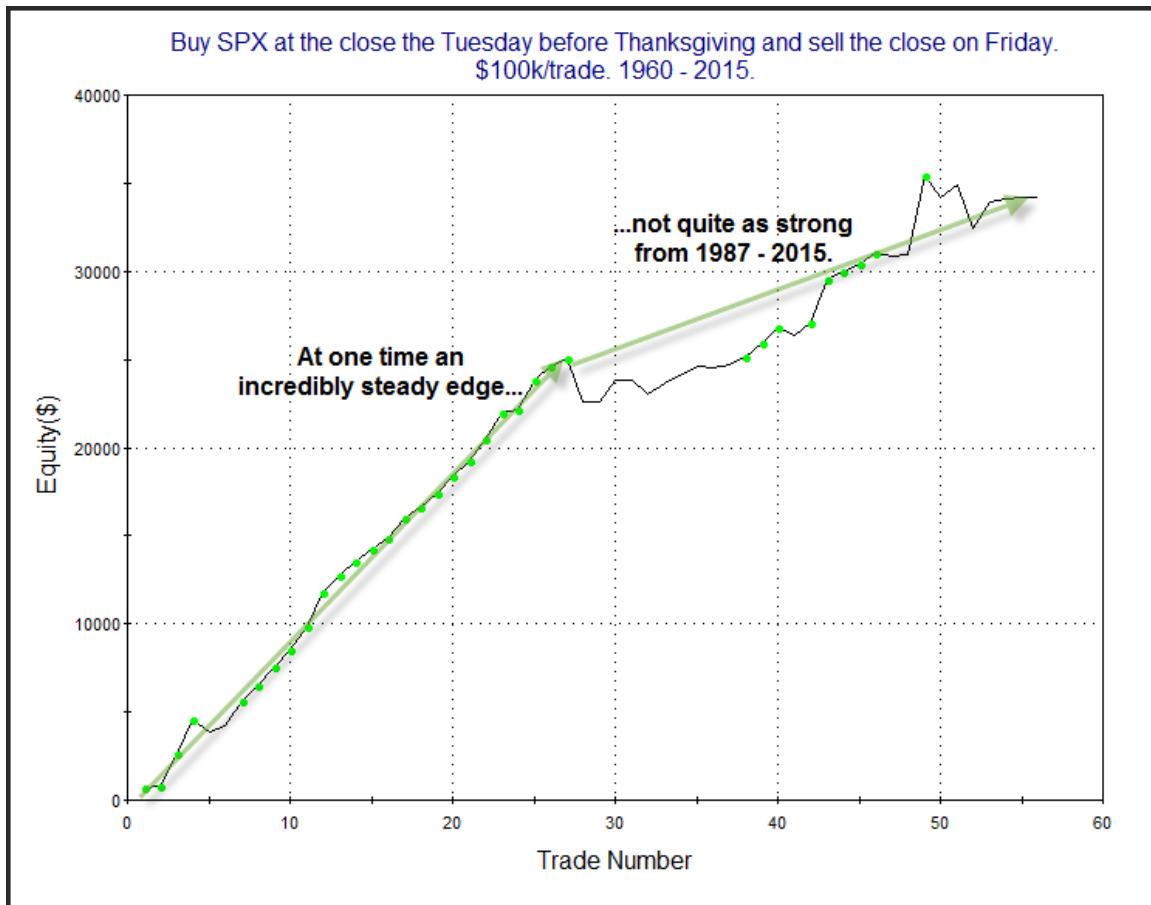
The numbers from the results table were extremely negative, but as you can see the downside edge has not been steady at all. While the trend has been down pretty much the entire time, a large portion of the downside move is thanks to a 9% drop in 2008. This suggests a seasonal downside edge does exist, but it is perhaps not as strong as the raw numbers would suggest.

With Wednesday and Friday both showing seasonal strength an obvious play would be to buy on Tuesday's close, and then sell at Friday's close. This strategy was first suggested by Yale Hirsch many years ago. I looked at it the last few years and have updated the results again below.

Buy SPX at the close the Tuesday before Thanksgiving and sell the close on Friday.
\$100k/trade. 1960 - 2015.

TradeStation Performance Summary Expand ▾			
All Trades			
Total Net Profit	\$34,222.00	Profit Factor	5.15
Gross Profit	\$42,459.02	Gross Loss	(\$8,237.02)
Total Number of Trades	56	Percent Profitable	83.93%
Winning Trades	47	Losing Trades	9
Even Trades	0		
Avg. Trade Net Profit	\$611.11	Ratio Avg. Win:Avg. Loss	0.99
Avg. Winning Trade	\$903.38	Avg. Losing Trade	(\$915.22)
Largest Winning Trade	\$4,506.60	Largest Losing Trade	(\$2,467.08)

As you can see the numbers are extremely strong. Below is an equity curve.



From 1960 through 1986 this trade would've worked fantastically. There was only one year during this period when it would have failed to make money. From 1987 to the present it has continued to do well, but not to the same degree as it had before. There have in fact been seven losing years over this time period. Still, the curve looks nicely positive and traders could consider a trade along these lines if other indicators also seem to be lining up.

I will also note that there has been a vast difference in performance during recent times depending on how the market moved leading up to Wednesday. To examine this, I used SPY instead of SPX, because SPY has better intraday data. Since 1993, I found that years in which SPY closed in the top half of its intraday range on Thanksgiving Tuesday posted a 7-5 record from Tuesday's close to Friday's close. When SPY closed in the bottom half of its range on Tuesday the performance over Wednesday to Friday was 10-1. And the average instance posted a 0.8% gain these years versus a 0.1% average gain the other years. So Tuesday's action appears worth watching as we approach this potentially seasonally bullish period.

I have updated the Aggregator chart below.



With tonight's studies to consider, 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 rose 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 zero. Therefore, the Aggregator signal turned long at the close.

Based on the current active studies, expectations are primed to remain positive on Monday. Of course this could change if compelling new bearish evidence emerges. The Differential Pivot will be 2188.26 on Monday. That is 0.3% above Friday's close. Therefore, SPX will only need to close up 0.3% to move from oversold to overbought versus expectations.

So the Aggregator is suggesting a bullish edge. Evidence looks pretty good. And we are entering a strong seasonal period this week. But there are two moderate concerns: 1) The strong seasonality has only played out in recent years when the market has struggled going into Tuesday afternoon, and 2) the market is only "oversold" slightly vs expectations. By most every other method it would still be considered overbought. SPX closed Friday in the top 10% of its 2-week range. And it also closed above its 10-day moving average for the 10th day in a row. So it is a bit of a stretch to view it as oversold at this point. Still, I may look to take on some long exposure if SPX sells off over the next day or two.

Intermediate-term Outlook (2 weeks – 2 months) – updated 11/20 – somewhat bullish

Combo #1	Combo #2	Combo #3
Long	Long	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.) *This week we saw the combo systems remain with one "Flat" while the other two stayed "Long".*

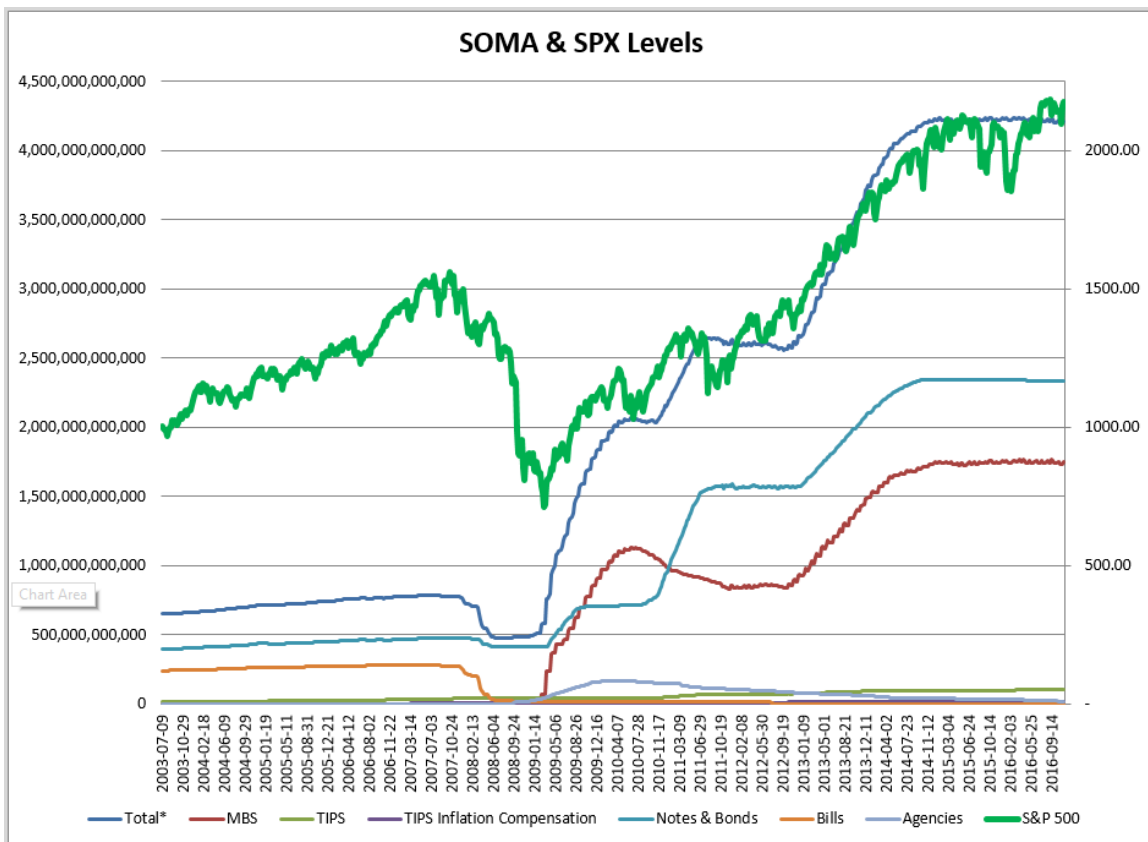
The SPX had a few strong up days this week and it resulted in a 0.8% gain for the week. And with it just slightly off an all-time high, and the Russell 2000 at a new long-term high,

the uptrend certainly seems to be intact. There were no new studies of intermediate-term significance that emerged this past week.

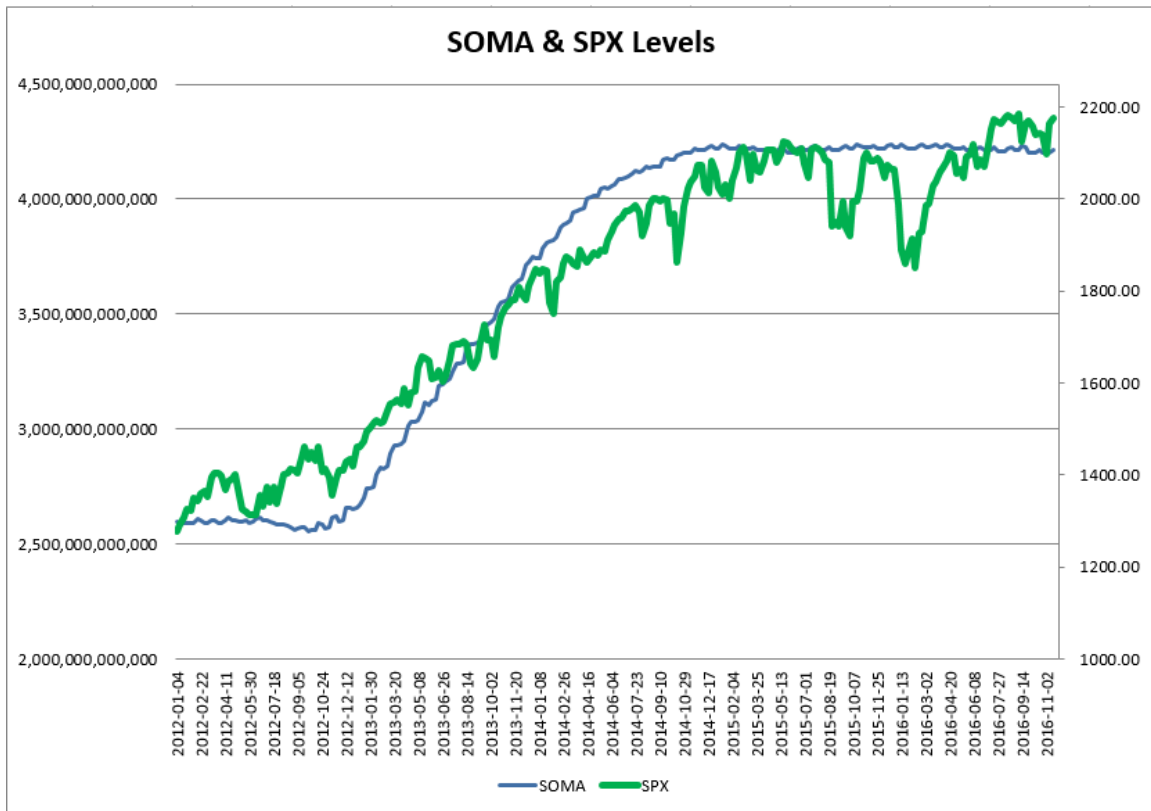
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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), managed a decent sized gain of 0.28%. This was in line with expectations based on the Fed’s SOMA schedule. The 0.63% rally for the SPX over this period was pretty typical. The market has generally done well during weeks that the SOMA has expanded. Since the beginning of 2015 SPX has risen 66% of the time for a sum total of 8.69% 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 1.65%. Based on the reinvestment schedule the Fed has stuck to over the last two years, this current week, which ends on Wednesday, should see the SOMA again post a gain. But the week after this will likely see a decrease in the SOMA. So Fed liquidity may help for the next few days. But after that the bulls will no longer have a liquidity wind at their back.

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 two years and we have not seen any strong derivations. I expect liquidity analysis to remain a vital tool for us.

Evidence continues to lean bullish. Studies from last week are still active. And there are still two of the four Market Timing Course indicators in “bull” mode. Bears will note that Fed support is temporary, the NASDAQ is lagging, and new highs have been diverging for years now. I will remain “somewhat bullish” overall. I am open to trading either side on a short-term basis. I will be more selective with shorts than longs.

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.

SPY = buy ¼ index position if SPX closes < 2169.47. This would put the SPX below its 10ma for the 1st time in a while. It would also put it low enough that would get me interested in trying to take advantage of a potential Thanksgiving week rally.

Current Open Trade Ideas

None

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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