

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

January 9, 2017

Volume 10 Issue 5

Market Overview



Signals Overview

Aggregator	Aggressive VIX	QE Buy Pwr / SOMA Swing
Flat	50% Long XIV	Short

Tonight's Research Points

- Friday's breakout with low volume looks bullish.
- The NASDAQ is now showing strength versus the SPX, which is an intermediate-term positive.

Short-term Outlook

The Bottom Line

Not much change from Thursday night. The Aggregator is again neutral. I see no edge strong enough to pursue at this time.

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						
January 9, 2017	50-day high breakout on lower volume	1-5 days	Bullish			
January 4, 2017	Unfilled up gap < 10ma > 200ma	1-4 days	Bullish			
Active - Long Term						
January 9, 2017	NASDAQ Leading	int term	Bullish			
December 29, 2017	1st 10-low in 30+ days	1-10 days	Bullish			
November 11, 2016	SPX 20-high. NDX biggest drop in 20.	1-50 days	Bullish			
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			

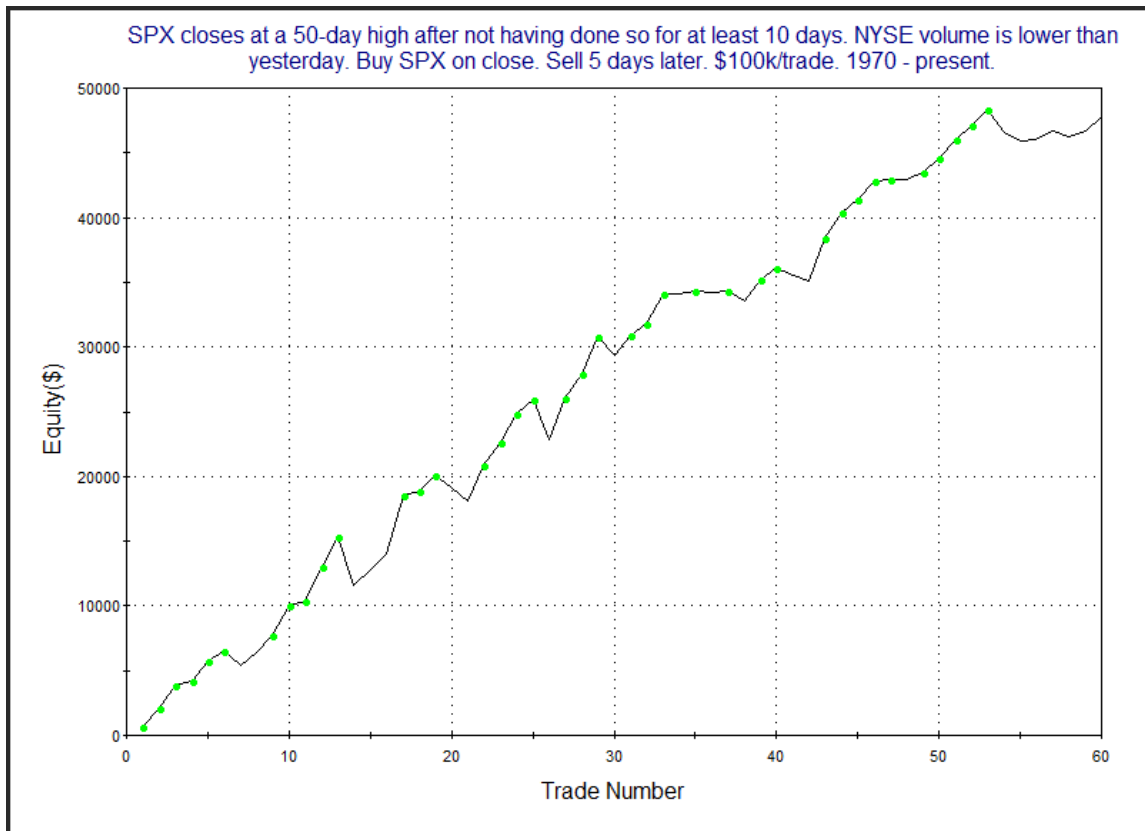
The Evidence

Friday was a mixed day for the market. SPX rose 0.35%, the NASDAQ gained 0.6%, and the Russell 2000 sold off 0.3%. Breadth was negative as the NYSE Up Issues % was 47% and the Up Volume % came in at 44%. NYSE volume declined some from Thursday's level.

Friday we saw SPX breakout to new highs. One measurement that can provide clues when SPX breaks out to a new high after a basing period is volume. I've discussed volume on breakouts a number of times in the past, including in the 2/28/14 letter. For a breakout to have a good chance of success you generally want volume to come in either 1) lower than the day before (like Friday), or 2) extremely high. Moderate but increasing volume is the worst scenario. To see why I say this, take a look at the 3 studies below. The first one examines new breakouts like the current one that occur on declining volume.

SPX closes at a 50-day high after not having done so for at least 10 days. NYSE volume is lower than yesterday. Buy SPX on close. Sell X days later. \$100k/trade. 1970 - 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	32,112.67	56	32	24	57.14	2,606.88	11,088.84	-2,137.81	-8,157.10	1.22	1.63	573.44
19	32,775.14	57	33	24	57.89	2,518.34	9,628.99	-2,097.09	-9,056.82	1.20	1.65	575.00
18	34,364.59	57	35	22	61.40	2,468.17	11,076.80	-2,364.61	-9,094.80	1.04	1.66	602.89
17	31,409.49	57	35	22	61.40	2,461.79	10,017.28	-2,488.78	-8,682.96	0.99	1.57	551.04
16	36,256.47	57	36	21	63.16	2,455.68	10,944.36	-2,483.24	-9,243.81	0.99	1.70	636.08
15	29,864.70	57	37	20	64.91	2,216.12	8,166.13	-2,606.59	-9,354.92	0.85	1.57	523.94
14	34,591.84	59	40	19	67.80	1,997.26	7,314.30	-2,384.13	-6,525.68	0.84	1.76	586.30
13	35,982.82	60	38	22	63.33	2,032.68	7,780.85	-1,875.42	-5,160.09	1.08	1.87	599.71
12	21,610.64	60	33	27	55.00	2,014.41	5,996.75	-1,661.67	-4,539.14	1.21	1.48	360.18
11	15,470.98	60	31	29	51.67	1,947.64	5,809.60	-1,548.48	-6,029.07	1.26	1.34	257.85
10	16,369.20	60	31	29	51.67	1,876.80	5,960.00	-1,441.78	-4,324.52	1.30	1.39	272.82
9	22,671.77	60	38	22	63.33	1,546.64	5,147.20	-1,640.93	-5,812.26	0.94	1.63	377.86
8	28,963.62	60	42	18	70.00	1,375.69	5,096.00	-1,600.85	-4,186.55	0.86	2.01	482.73
7	31,543.56	60	39	21	65.00	1,379.75	4,655.00	-1,060.32	-3,211.35	1.30	2.42	525.73
6	46,698.10	60	42	18	70.00	1,445.23	5,002.50	-777.87	-3,563.65	1.86	4.34	778.30
5	47,832.89	60	45	15	75.00	1,418.22	4,482.50	-1,065.79	-3,693.73	1.33	3.99	797.21
4	32,104.67	60	43	17	71.67	1,169.88	4,440.00	-1,070.59	-2,913.85	1.09	2.76	535.08
3	30,323.82	60	40	20	66.67	1,134.73	3,950.00	-753.27	-1,802.37	1.51	3.01	505.40
2	18,880.61	60	40	20	66.67	804.44	2,212.98	-664.85	-1,912.60	1.21	2.42	314.68
1	8,362.82	60	39	21	65.00	452.37	1,384.02	-441.88	-1,921.32	1.02	1.90	139.38

Numbers here appear pretty solid, with add-on buying typically coming in during the next week. Below is a look at a profit curve.



The move from lower left to upper right is encouraging. Next let's look at times where there was extremely strong volume (20-day high volume).

SPX closes at a 50-day high after not having done so for at least 10 days. NYSE volume is the highest in at least 20 days. Buy SPX on close. Sell X days later. \$100k/trade. 1970 - 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	18,538.22	40	22	18	55.00	3,632.58	8,953.20	-3,409.92	-8,308.32	1.07	1.30	463.46
19	13,685.17	40	23	17	57.50	3,409.41	8,942.40	-3,807.72	-7,980.00	0.90	1.21	342.13
18	24,595.39	40	23	17	57.50	3,674.90	9,613.50	-3,525.13	-7,323.36	1.04	1.41	614.88
17	20,613.97	40	24	16	60.00	3,274.62	9,069.84	-3,623.55	-8,144.90	0.90	1.36	515.35
16	25,570.48	40	23	17	57.50	3,530.65	8,048.82	-3,272.62	-8,109.35	1.08	1.46	639.26
15	20,775.66	40	23	17	57.50	3,424.99	7,668.00	-3,411.72	-8,358.20	1.00	1.36	519.39
14	21,212.29	40	23	17	57.50	3,302.74	8,128.38	-3,220.63	-8,338.45	1.03	1.39	530.31
13	25,626.24	40	24	16	60.00	3,054.35	7,478.64	-2,979.88	-8,251.55	1.02	1.54	640.66
12	21,979.40	40	23	17	57.50	2,796.65	7,352.31	-2,490.79	-8,757.15	1.12	1.52	549.49
11	28,371.52	40	26	14	65.00	2,514.89	6,782.40	-2,643.98	-6,975.70	0.95	1.77	709.29
10	31,145.17	40	24	16	60.00	2,487.82	6,199.20	-1,785.15	-3,730.08	1.39	2.09	778.63
9	27,897.57	40	24	15	60.00	2,272.85	6,418.16	-1,776.73	-3,113.22	1.28	2.05	697.44
8	29,663.58	40	24	16	60.00	2,245.80	6,220.34	-1,514.73	-2,943.34	1.48	2.22	741.59
7	30,443.70	40	25	15	62.50	2,017.12	5,264.21	-1,332.29	-2,946.00	1.51	2.52	761.09
6	33,597.45	40	28	12	70.00	1,753.17	4,695.76	-1,290.94	-3,093.30	1.36	3.17	839.94
5	29,863.77	40	26	14	65.00	1,655.48	4,771.60	-941.33	-2,562.72	1.76	3.27	746.59
4	21,201.24	40	26	14	65.00	1,266.35	3,165.12	-837.42	-1,948.21	1.51	2.81	530.03
3	17,575.07	40	26	14	65.00	1,086.30	2,989.36	-762.04	-2,188.15	1.43	2.65	439.38
2	27,508.43	40	27	12	67.50	1,181.81	3,813.53	-366.70	-1,259.60	3.22	7.25	687.71
1	15,102.12	40	29	11	72.50	648.11	2,755.52	-335.73	-1,292.50	1.93	5.09	377.55

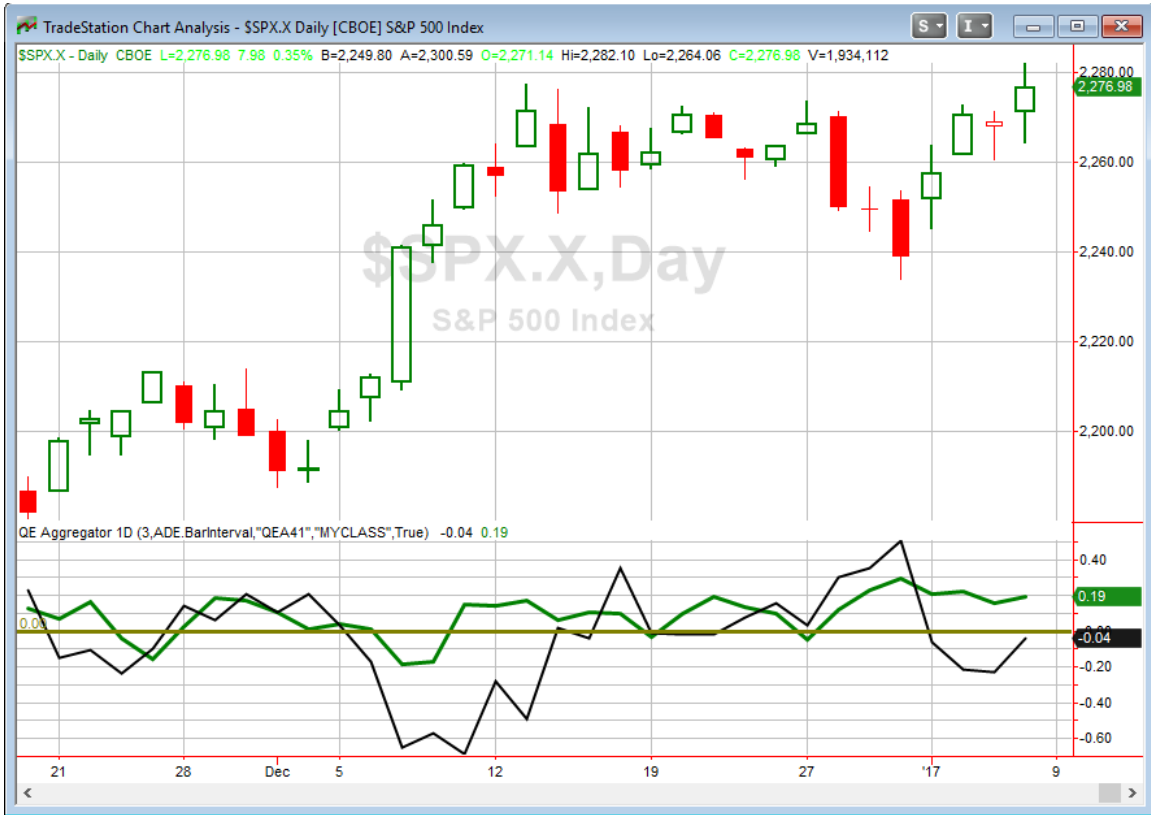
Numbers here are quite similar, with the first week getting solid follow-through buying once again. Lastly, let's look at rising but moderate volume.

SPX closes at a 50-day high after not having done so for at least 10 days. NYSE volume is higher than yesterday but < 20-day high. Buy SPX on close. Sell X days later. \$100k/trade. 1970 - 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	-757.98	97	46	51	47.42	3,351.74	13,401.70	-3,038.00	-11,541.15	1.10	1.00	-7.81
19	8,582.81	97	49	48	50.52	3,127.85	9,135.36	-3,014.20	-11,854.89	1.04	1.06	88.48
18	14,668.13	98	52	46	53.06	2,936.91	9,503.00	-3,001.11	-10,293.66	0.98	1.11	149.67
17	7,209.09	98	52	46	53.06	2,820.38	9,962.68	-3,031.54	-9,419.67	0.93	1.05	73.56
16	2,454.98	100	53	47	53.00	2,650.28	8,910.72	-2,936.38	-9,482.88	0.90	1.02	24.55
15	10,536.66	100	52	48	52.00	2,595.03	8,150.48	-2,591.77	-9,608.60	1.00	1.08	105.37
14	-2,729.97	100	55	45	55.00	2,334.17	7,702.40	-2,913.54	-10,120.46	0.80	0.98	-27.30
13	-3,810.87	100	52	48	52.00	2,345.30	7,911.80	-2,620.13	-9,725.34	0.90	0.97	-38.11
12	-10,331.74	100	53	47	53.00	2,195.41	10,197.98	-2,695.50	-9,869.02	0.81	0.92	-103.32
11	-4,455.17	100	50	50	50.00	2,338.23	10,380.37	-2,427.34	-9,482.88	0.96	0.96	-44.55
10	-11,484.33	100	48	52	48.00	2,211.49	10,515.18	-2,262.23	-8,683.66	0.98	0.90	-114.84
9	-6,980.60	100	46	54	46.00	2,179.78	8,413.73	-1,986.12	-6,878.68	1.10	0.93	-69.81
8	-10,683.84	100	52	48	52.00	1,714.82	8,532.68	-2,080.30	-7,076.24	0.82	0.89	-106.84
7	6,673.66	100	51	49	51.00	1,766.23	6,337.26	-1,702.12	-7,255.84	1.04	1.08	66.74
6	4,957.32	100	55	45	55.00	1,478.63	6,819.80	-1,697.05	-7,103.18	0.87	1.06	49.57
5	1,213.16	100	48	52	48.00	1,545.06	8,516.82	-1,402.88	-6,088.44	1.10	1.02	12.13
4	-4,917.27	100	53	47	53.00	1,253.22	6,716.71	-1,517.83	-5,585.56	0.83	0.93	-49.17
3	7,122.37	100	57	43	57.00	1,131.43	6,740.50	-1,334.17	-5,361.06	0.85	1.12	71.22
2	912.38	100	58	42	58.00	770.62	4,028.44	-1,042.47	-4,276.16	0.74	1.02	9.12
1	7,701.98	100	55	45	55.00	519.95	2,731.56	-464.34	-2,722.61	1.12	1.37	77.02

This does not appear to suggest any edge over the next 1-4 weeks. Perhaps it was fortunate that Friday's breakout occurred on declining volume.

I have updated the Aggregator chart below.



With the breakout studies considered the green Aggregator Line remained 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 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 zero. Therefore, the Aggregator signal stayed flat at the close.

Based on the current active studies, expectations are set to remain bullish on Monday. Of course this could change if new bearish evidence emerges. The Differential Pivot will be *inverted* at 2287.38 on Monday. That is 0.5% *above* Thursday's close. An inverted pivot means that the Differential Line will cross through 0 if SPX closes flat. In this case SPX is going to need to close up at least 0.5% in order to remain overbought. Otherwise it will be considered oversold versus expectations as of Monday's close.

This breakout looks pretty good. But I would still prefer a bit of a pullback or at least a consolidation that could offer a more favorable reward/risk setup for new entries. I'll be keeping a close eye on the market over the next several days to see how action unfolds and what new evidence emerges as a result. All I can say right now is that I do not see a favorable enough opportunity to make me want to take new positions on Monday.

Intermediate-term Outlook (2 weeks – 2 months) – updated 1/9 – 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 change so that all 3 are now “Long” vs two “Long” and one “Flat” last week.*

SPX posted strong gains this week of 1.7%. It also finished the week at an all-time high. This leaves no doubt that the uptrend is still intact. The NASDAQ had an even stronger week than the SPX, rising 2.6%. The relative outperformance of the NASDAQ helped it to retake a leading position based on our NASDAQ/SPX Relative Strength Indicator. This is the first time the indicator has been positive since the end of October. Below is a chart of the indicator from the website.

NASDAQ/S&P 500 Relative Strength Weekly



The movement of the red line (which is about to turn green) above the blue line is our indication that the NASDAQ is in a leading position. Since 1971, the market has performed substantially better when the NASDAQ has been leading. Over that time, the SPX has gained 1737.60 point when the NASDAQ has been leading versus 437.28 points when the NASDAQ has lagged. The difference for the NASDAQ has been even more dramatic, with the point gains being 5410.98 vs. and almost breakeven 1.7. More on this indicator can be found in the Market Timing Course, or on its page (which can be found by clicking on the chart on the charts page). <http://quantifiableedges.com/nasdaq-weekly-strength-model/>

I decided tonight to take a look at how the market has done when all 4 Market Timing Course indicators have been aligned as they are now. That means: 1) a leading NASDAQ, 2) SPX “Golden Cross” in effect, 3) unfavorable Presidential Cycle, and 4) “Best” 6 months in effect. Below are stats showing SPX performance during this alignment.

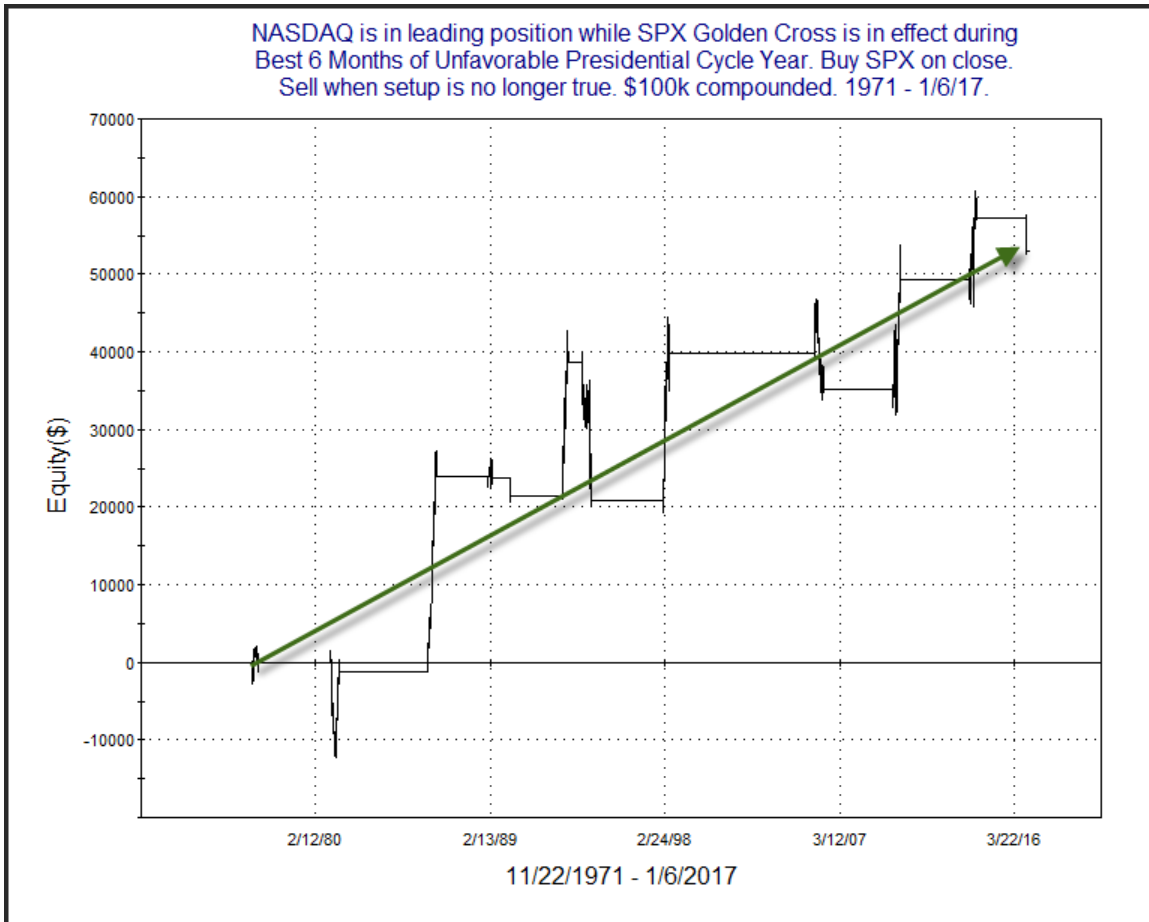
NASDAQ is in leading position while SPX Golden Cross is in effect during Best 6 Months of Unfavorable Presidential Cycle Year. Buy SPX on close. Sell when setup is no longer true. \$100k/trade. 1971 - 1/6/17.

TradeStation Performance Summary Expand ▾			
All Trades			
Total Net Profit	\$35,698.37	Profit Factor	2.17
Gross Profit	\$66,240.06	Gross Loss	(\$30,541.69)
Total Number of Trades	30	Percent Profitable	46.67%
Winning Trades	14	Losing Trades	16
Even Trades	0		
Avg. Trade Net Profit	\$1,189.95	Ratio Avg. Win:Avg. Loss	2.48
Avg. Winning Trade	\$4,731.43	Avg. Losing Trade	(\$1,908.86)
Largest Winning Trade	\$14,725.36	Largest Losing Trade	(\$5,116.74)

Stats here appear nicely favorable as this alignment has shown some strong gains over the years. Gross gains have been over 2x times the size of gross losses. Of course we learned in the Market Timing Course that when the NASDAQ was leading, it also generally continued to outperform the S&P 500. That holds true in this case as well. It can be seen in the table below.

TradeStation Performance Summary Expand ▾			
All Trades			
Total Net Profit	\$46,956.33	Profit Factor	2.23
Gross Profit	\$85,119.12	Gross Loss	(\$38,162.79)
Total Number of Trades	30	Percent Profitable	50.00%
Winning Trades	15	Losing Trades	15
Even Trades	0		
Avg. Trade Net Profit	\$1,565.21	Ratio Avg. Win:Avg. Loss	2.23
Avg. Winning Trade	\$5,674.61	Avg. Losing Trade	(\$2,544.19)
Largest Winning Trade	\$14,152.70	Largest Losing Trade	(\$8,185.60)

As you can see, the Avg Trade is quite a bit better here. I also looked at compounding the returns rather than investing a flat \$100k/trade. Results there can be seen in the chart below.

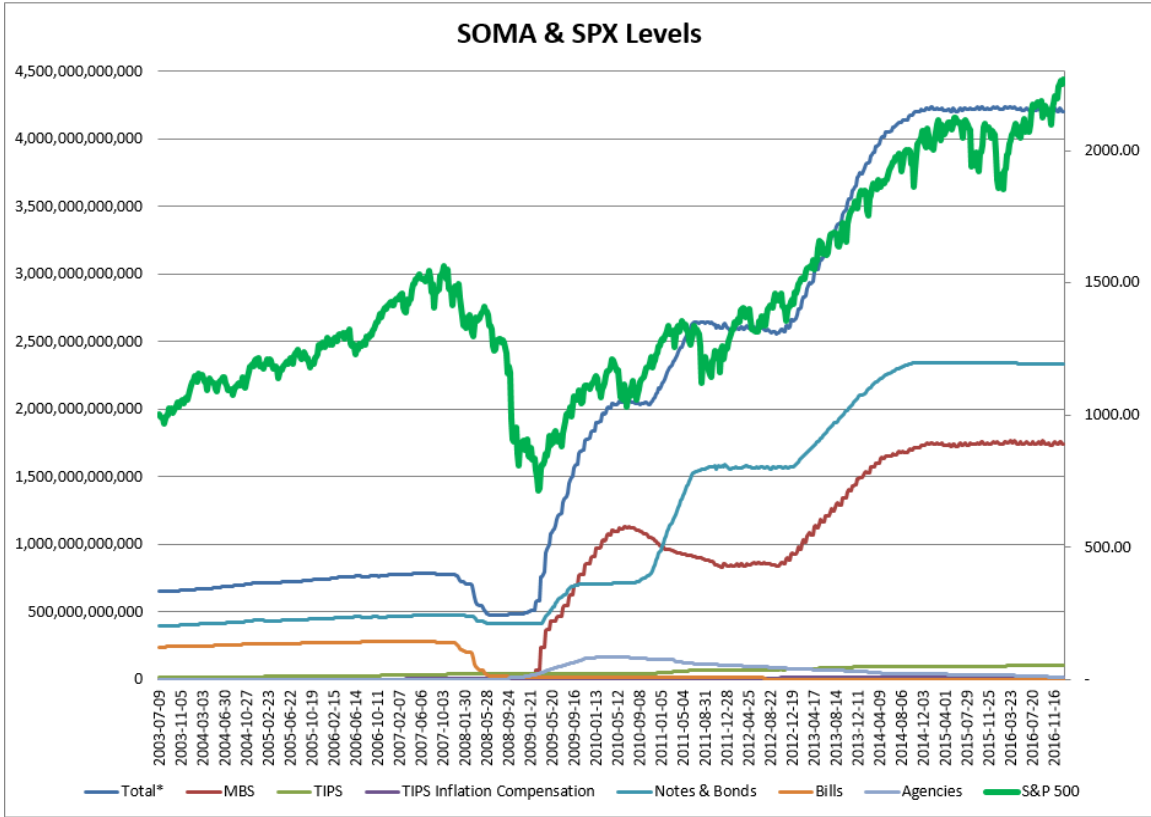


That's a solid looking profit curve. The now-leading NASDAQ certainly appears to be good news for the bulls.

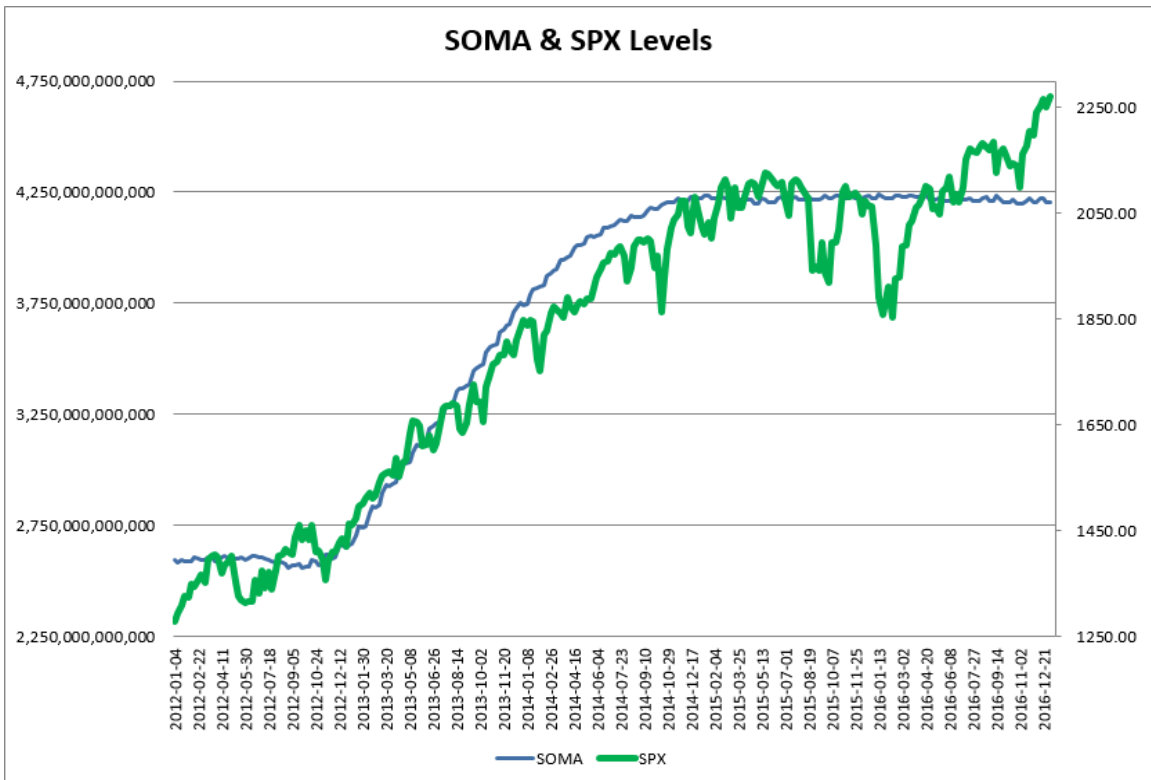
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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) came in basically flat, posting a gain of less than 0.01%. This was in line with expectations based on the Fed's SOMA schedule. The 0.93% gain for the SPX over this period was much stronger than typical. The market has generally performed poorly during weeks that the SOMA has failed to expand at least 0.01%. Since the beginning of 2015 SPX has risen 68% of the time for a sum total of 10.50% during SOMA expansion weeks (of at least 0.01%). During all other weeks, like this past one, SPX has only risen 46% of the time and has gained a sum total of just 0.80%. Based on the reinvestment schedule the Fed has stuck to over the last two years, this current week appears likely to show almost no change in the SOMA. But the following week we will likely see a moderate rise in the SOMA. So the bulls may get some help from Fed Liquidity after Wednesday.

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.

The late December/early January strong seasonal period is over. But the bulls still appear to be in charge. The market is clearly still in an uptrend, and with the NASDAQ now leading that brightens the picture further. That means 3 of the 4 Market Timing Course indicators are in "bull" mode. Bears will note that Fed support is lacking and new highs have been diverging for years now. I am still inclined to favor the long side and I remain intermediate-term bullish. That means I intend to trade longs more aggressively than shorts, and will be extra-selective with any short plays.

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

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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