

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

February 27, 2017

Volume 10 Issue 37

Market Overview



Signals Overview

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

Tonight's Research Points

- When the Russell has fallen for 3 days while SPX has closed at a 3-day high then the market has rallied over the next couple of days and weeks.
- Thursday's mild up close near the top of its range suggests a bearish 1-day edge.
- SOMA is expected to be flat or down the next couple of weeks, making thing more difficult for the bulls.

Short-term Outlook

The Bottom Line

The Aggregator is bullish, but the evidence is mixed and the market is extended by most metrics. I am not inclined to get involved until we see a pullback for the SPX.

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						
February 27, 2017	SPY top 10% range. Up < 0.25%	1 day	Bearish			
February 27, 2017	RUT down 3. SPX 3-day high.	1-4 days	Bullish	2.35%	-0.60%	-1.35%
February 23, 2017	SOMA Swing Short	1-6 days	Bearish			
February 23, 2017	Relatively big drop from 50-day high	1-4 days	Bullish			
February 16, 2017	SPX > Bollinger Band 4 days in a row	1-8 days	Bullish			
Active - Long Term						
February 27, 2017	RUT down 3. SPX 3-day high.	1-10 days	Bullish	3.90%	-1.00%	-2.10%
February 17, 2017	SPX up 5 to 50 high then down 1	1-10 days	Bullish			
January 9, 2017	NASDAQ Leading	int term	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			

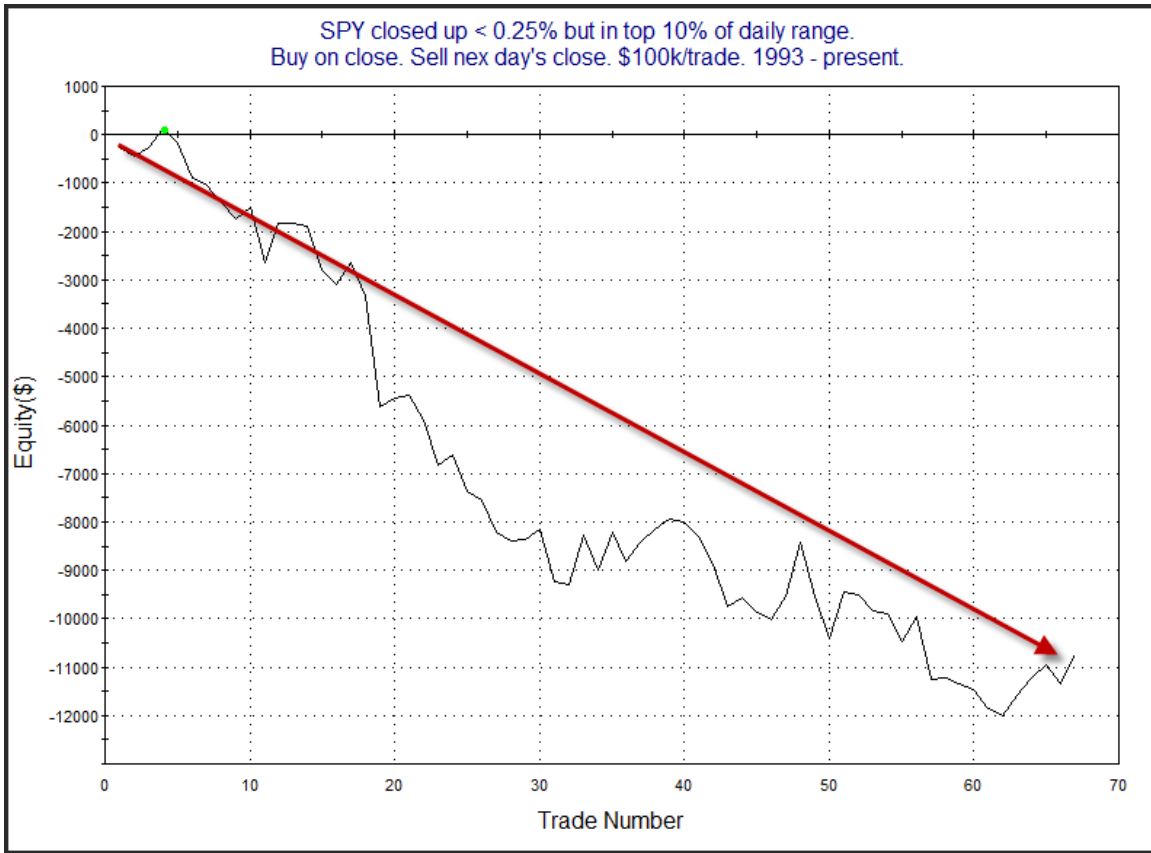
The Evidence

Friday had a bad start to the day, but rallied to finish mixed. The SPX gained 0.15%, the NASDAQ rose 0.17%, and the Russell 2000 finished down a mere 0.01%. Breadth was negative as the NYSE Up Issues % was 49% and the Up Volume % came in at 36%. NYSE volume rose to the highest level of the week.

One interesting study to appear in the Quantifinder was the one below, which was last seen just last week in the 2/21/17 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				Expand ▾
All Trades				
Total Net Profit	(\$10,741.60)	Profit Factor		0.49
Gross Profit	\$10,421.75	Gross Loss	(\$21,163.35)	
Total Number of Trades	67	Percent Profitable		38.81%
Winning Trades	26	Losing Trades		41
Even Trades	0			
Avg. Trade Net Profit	(\$160.32)	Ratio Avg. Win:Avg. Loss		0.78
Avg. Winning Trade	\$400.84	Avg. Losing Trade	(\$516.18)	
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.



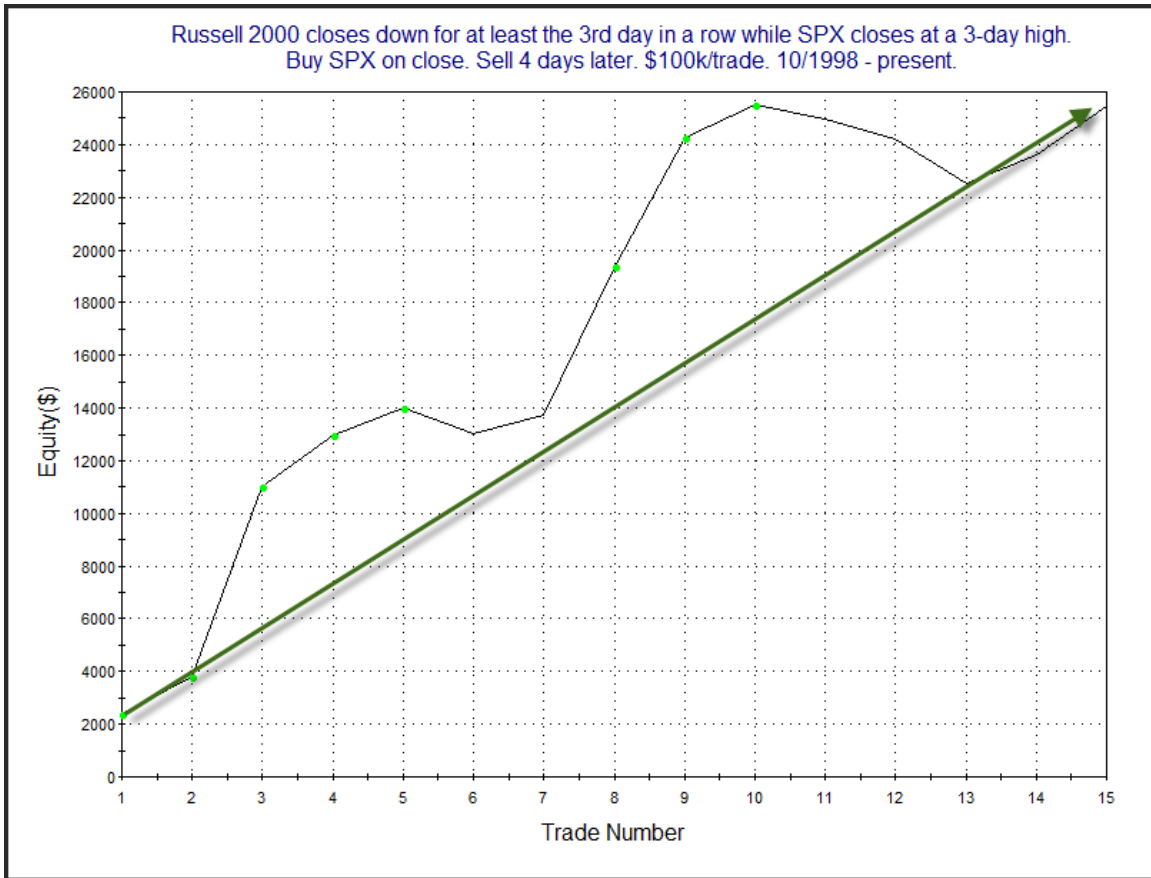
It appears that when the market needs to expend a fair amount of energy just to squeak out a small gain, that its lack of momentum is often followed by a swing back in the opposite direction the next day.

Another aspect of recent market action that is interesting and suggestive of an upside edge is the fact that despite the rise in the SPX, the Russell 2000 closed lower for the third day in a row. The study below was last seen in the 2/9/17 Subscriber Letter. Stats are updated.

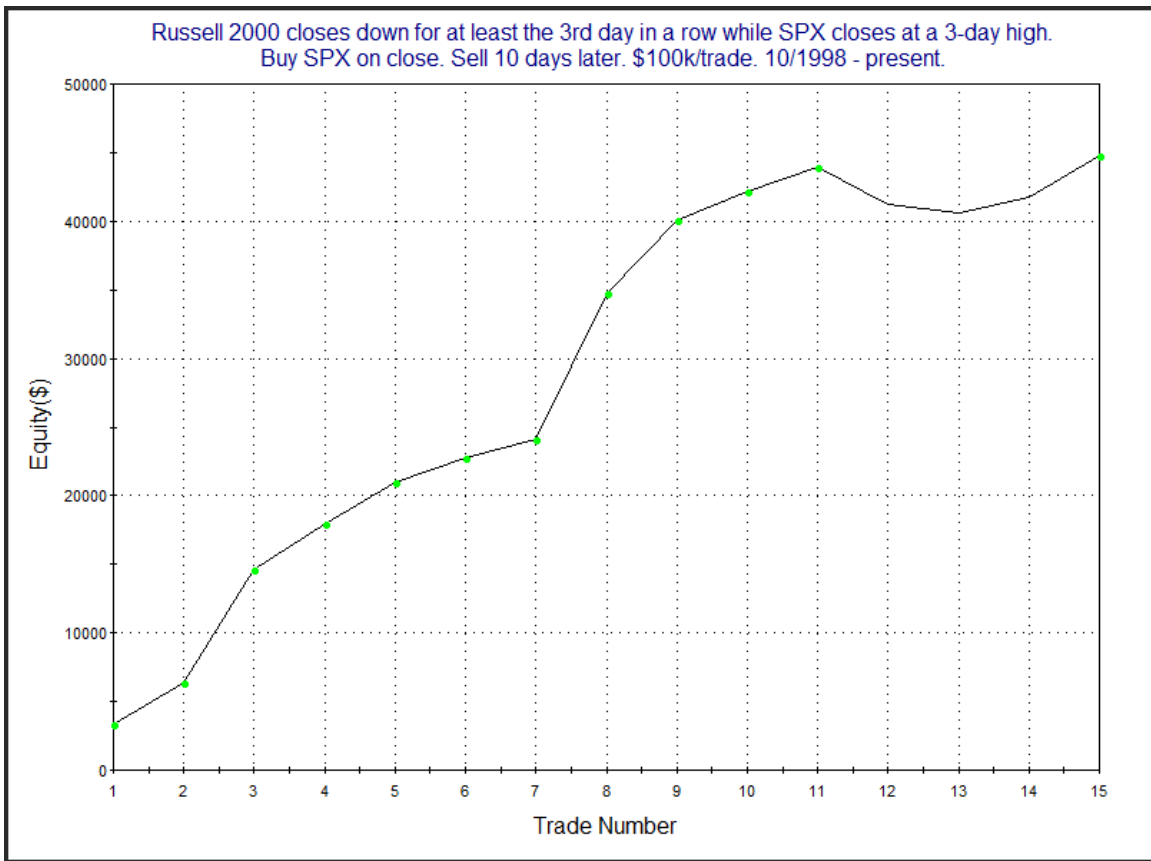
Russell 2000 closes down for at least the 3rd day in a row while SPX closes at a 3-day high.
Buy SPX on close. Sell X days later. \$100k/trade. 10/1998 - present.

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	44,770.78	15	13	2	86.67	3,700.82	10,577.93	-1,669.96	-2,723.00	2.22	14.40	2,984.72
9	37,738.51	15	12	3	80.00	3,400.94	8,209.02	-1,024.26	-2,674.70	3.32	13.28	2,515.90
8	35,210.94	15	12	3	80.00	3,140.30	9,347.15	-824.21	-1,463.00	3.81	15.24	2,347.40
7	35,517.34	15	10	5	66.67	3,963.99	9,614.11	-824.52	-2,783.20	4.81	9.62	2,367.82
6	30,883.76	15	11	4	73.33	3,386.46	9,598.49	-1,591.81	-3,491.60	2.13	5.85	2,058.92
5	25,132.91	15	11	4	73.33	2,867.53	7,700.66	-1,602.48	-2,075.04	1.79	4.92	1,675.53
4	25,457.57	15	11	4	73.33	2,674.77	7,217.86	-991.23	-1,680.10	2.70	7.42	1,697.17
3	19,540.67	15	11	4	73.33	1,981.70	4,839.33	-564.51	-887.22	3.51	9.65	1,302.71
2	18,814.32	15	12	3	80.00	1,653.42	5,134.01	-342.23	-551.73	4.83	19.33	1,254.29
1	12,159.83	16	11	5	68.75	1,274.16	4,708.01	-371.19	-764.46	3.43	7.55	759.99

As you can see, stats are overwhelmingly bullish right off the bat, and they stay strong through the first two weeks. Instances are a little bit low, but the stats at this point are very impressive. Below is a profit curve using a 4-day exit.

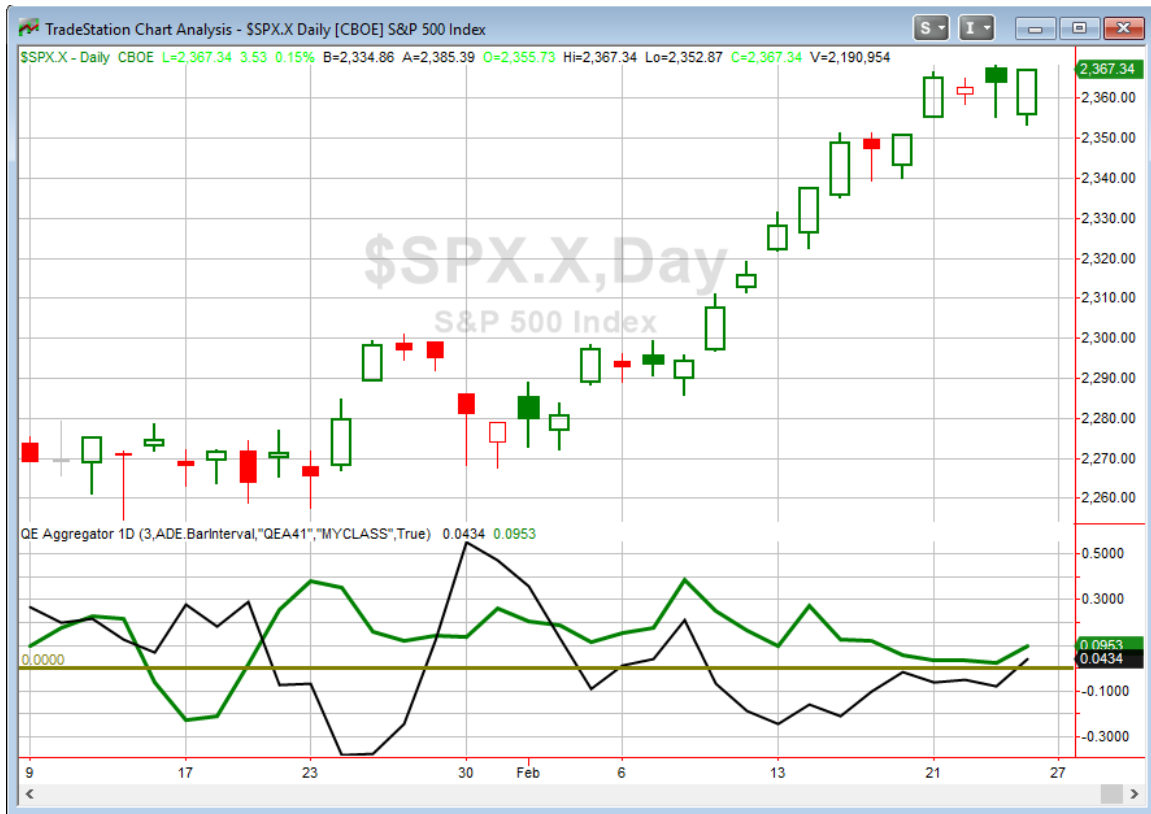


This looks pretty solid. I also produced a profit curve for a 10-day holding period.



The move up has been impressive. I have included this study on both the short-term and the intermediate-term active list.

I have updated the Aggregator chart below.



With tonight's studies considered 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 inched above 0. The positive Differential Line reading means SPX is *oversold* versus recent expectations (despite being at a new high). 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 set to remain modestly bullish on Monday. Of course, this could change if new bearish evidence emerges. The Differential Pivot will be *inverted* at 2365.96 on Monday. That is 0.06% *below* Friday's close. An inverted pivot means that the Differential Line will cross through zero if SPX closes flat. In this case, SPX is going to need to close down at least 0.06% on Monday in order to remain "oversold" versus expectations. Anything less than that and it will be considered overbought as of Monday's close.

We are in one of those unusual situations where the market is posting new highs, but doing so at a slower rate than the studies expected. So it is considered "oversold" by the Differential metric. Of course, there is nothing else that would consider the SPX "oversold". And the market has gone an extended period of time without a substantial pullback. For SPY, it has closed above its 10-day moving average for 15 days in a row.

For QQQ, it has now been a whopping 38 days. We are now in one of those momentum-driven markets where a pullback is overdue, making it dangerous to go long. But momentum is strong, making it dangerous to go short. It is unlikely I will do much of anything until we get at least a short-term pullback that allows the market get back into more “normal” oscillations.

Intermediate-term Outlook (2 weeks – 2 months) – updated 2/27 – bullish

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

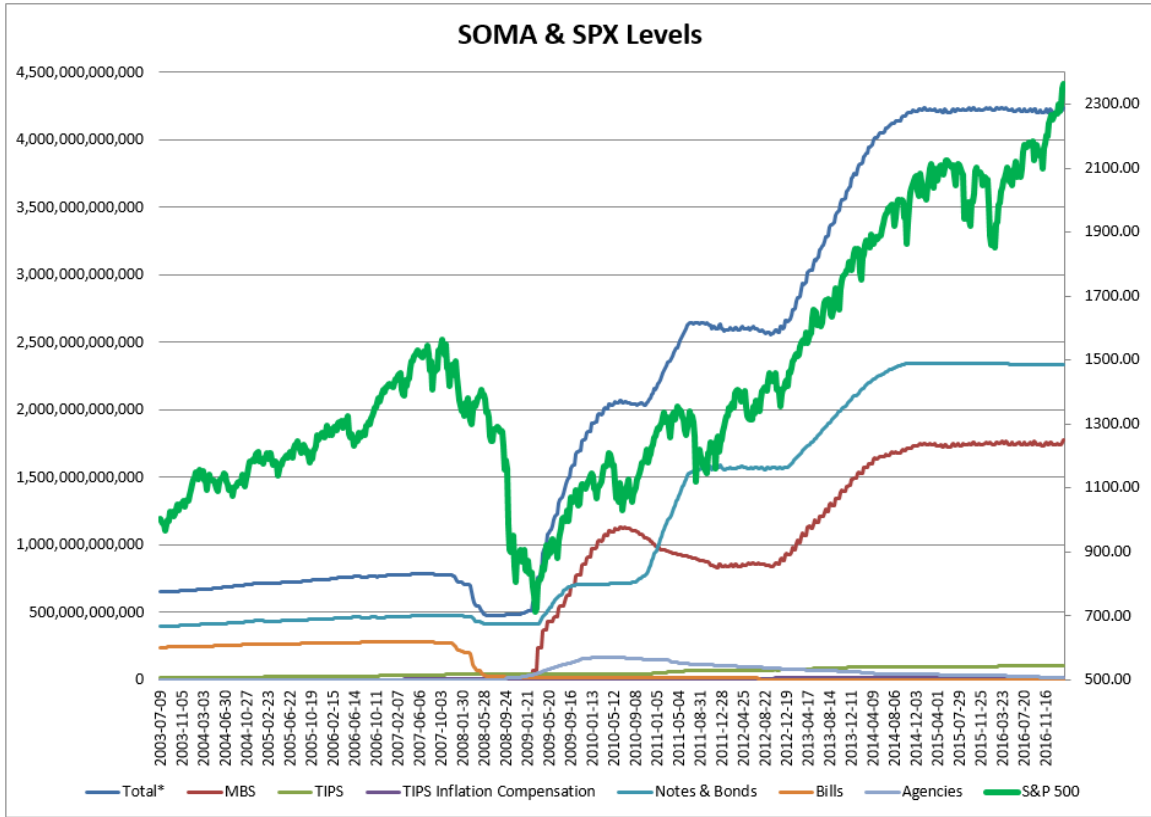
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#),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

This past week was another good one for the bulls. The SPX closed up 0.7%. And with major indices at new highs the long-term uptrend remains intact. And tonight’s SPX/RUT study from above provided additional intermediate-term bullish evidence.

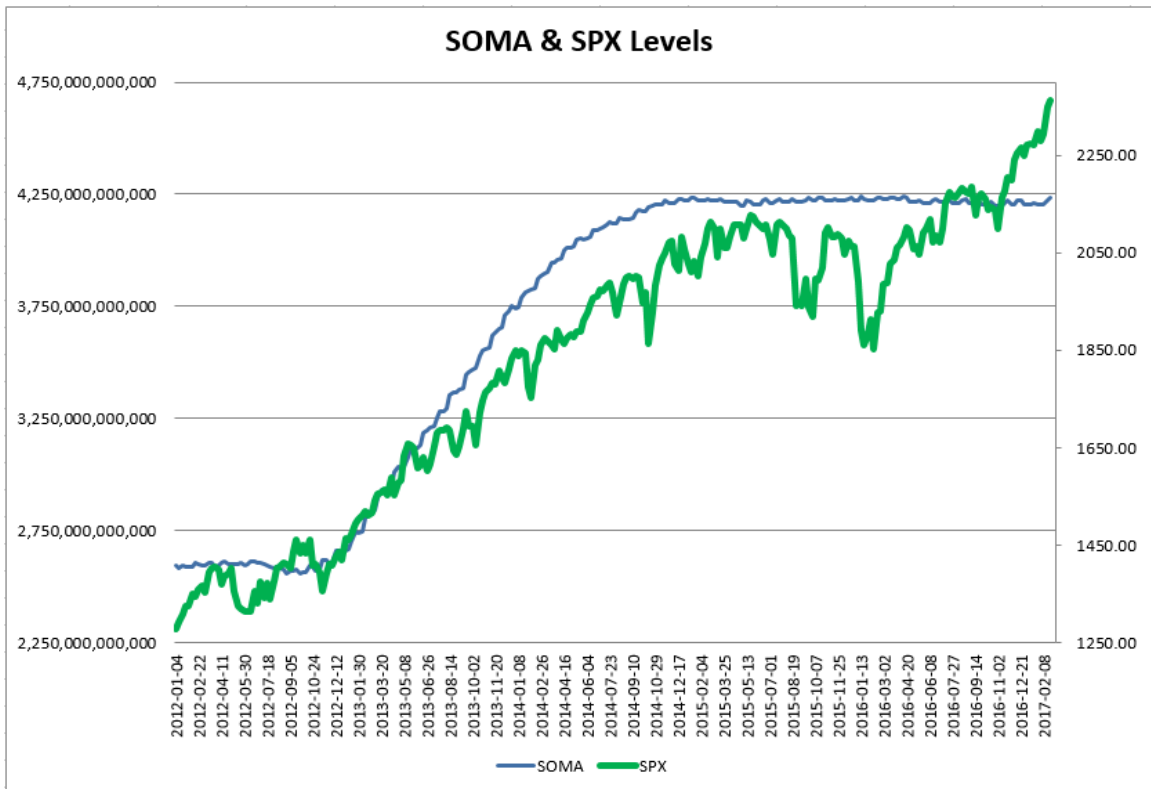
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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) again came in higher with a solid rise of 0.29%. This was in line with expectations based on the Fed's SOMA schedule. The 0.58% rise for the SPX over this period was fairly typical for an expansion week. Since the beginning of 2015 SPX has risen 68% of the time for a sum total of 13.30% during the 37 weeks in which SOMA expanded at least 0.01%. During the 75 other weeks SPX has only risen 48% of the time and has gained a sum total of just 2.01%. Based on the reinvestment schedule the Fed has stuck to over the last two years, this current week appears likely to see the SOMA remain flat or decline some. And the following week it appears the SOMA will likely remain flat. So the bulls are not likely to have Fed-induced liquidity on their side for the foreseeable future. This could open up an opportunity for the bears to halt the momentum and perhaps generate some kind of selloff or pullback.

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

It is not easy to be much other than bullish with the market continually making new highs. Today's SPX/RUT study added to the bullish evidence. The market is still in an uptrend, and 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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