

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 17, 2017

Volume 10 Issue 135

Market Overview



Signals Overview

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

Tonight's Research Points

- Breakouts to new 50-day highs often lead to more buying in the short-term. This is especially true when there has been a run-up into the breakout and the breakout occurs on lower volume. Both conditions were present Friday.
- The NASDAQ retook a leading position, which helps the bullish case for the intermediate-term.
- SOMA flows should help the bulls through Wednesday, but then turn sour.

Short-term Outlook

The Bottom Line

Friday's breakout looks pretty good. I am neutral but could easily turn bullish if the market pulls back a little in the next day or so.

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 17, 2017	3 up, 50-high breakout on low volume	1-5 days	Bullish	1.70%	-0.90%	-2.00%
Active - Long Term						
July 17, 2017	NASDAQ Leading	int term	Bullish			
June 24, 2017	Hindenburg Omen cluster	1-35 days	Bearish	-7.00%		
June 2, 2017	SPX closes above 50-day Bollinger Band	1-50 days	Bullish	4.90%	-4.10%	-7.80%
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 solid up day that led to new highs in the Dow, SPX, and Russell 2000. The SPX closed up 0.5%, the NASDAQ gained 0.6%, and the Russell 2000 rose 0.2%. Breadth was positive as the NYSE Up Issues % was 70% and the Up Volume % came in at 72%. NYSE volume declined for the 3rd day in a row.

Friday was the 1st time since June 19th that the SPX closed at a new high. The new high triggered a number of studies in the Quantifinder. I have shown numerous times before that breakouts to new highs show a better chance of following through if they are occurring after a decent basing period of at least 1-2 weeks. Some other studies that triggered showed evidence that to some people might seem counter-intuitive. One study showed that breakouts that occurred on declining volume have followed-through much better than breakouts accompanied by rising volume. Another study showed that when the breakout has come after the market had already risen for at least the past 2 days, then it has done a better job of carrying that momentum forward.

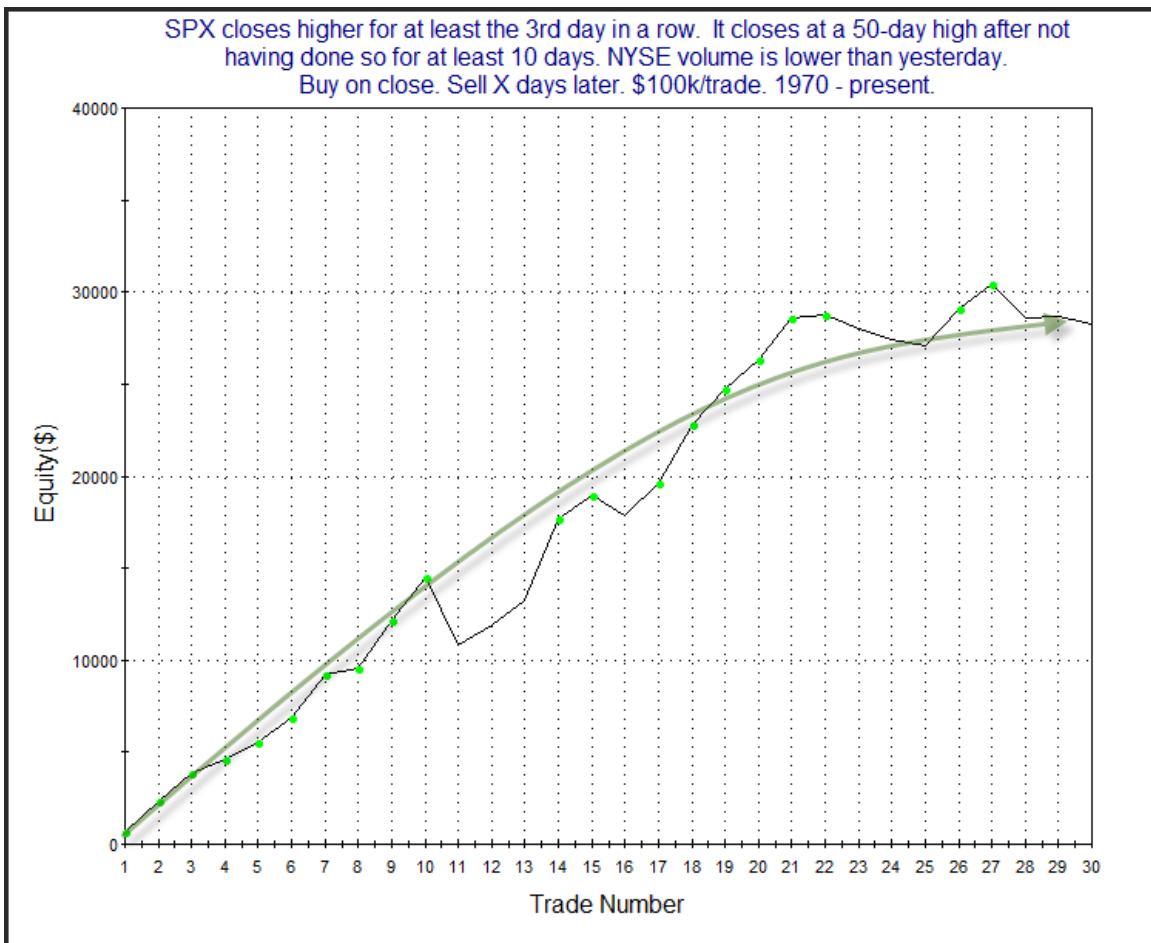
In the 4/27/15 Letter I combined these concepts and published the following study. (All stats are updated.)

SPX closes higher for at least the 3rd day in a row. It closes at a 50-day high after not having done so for at least 10 days. NYSE volume is lower than yesterday.
Buy 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
5	28,265.79	30	23	7	76.67	1,607.34	4,482.50	-1,243.28	-3,693.73	1.29	4.25	942.19
4	18,974.72	30	23	7	76.67	1,166.09	4,440.00	-1,120.76	-2,145.44	1.04	3.42	632.49
3	18,290.73	30	20	10	66.67	1,200.28	3,950.00	-571.48	-1,082.79	2.10	4.20	609.69
2	13,077.74	30	22	8	73.33	881.37	2,133.10	-789.04	-1,312.40	1.12	3.07	435.92
1	8,147.14	30	21	9	70.00	556.36	1,384.02	-392.92	-893.32	1.42	3.30	271.57

27 of 30 instances (90%) closed above the entry price at some point in the next week.

Stats here are very impressive. And the average follow-through was over 1.7% during the next 5 days. This is with a setup where the SPX is already extended! The consistency is impressive as well. Below is a look at the profit curve assuming a 5-day holding period.



While the last couple of instances have not done great, I still like the curve enough to include the study on the Active List.

To demonstrate the importance of the 3-day rise and the low volume on the breakout, I reversed both of those criteria and re-ran the study.

SPX closes at a 50-day high after not having done so for at least 10 days. It closed down either yesterday or the day before. NYSE volume is higher than yesterday. Buy 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
5	11,169.62	78	39	39	50.00	1,582.48	8,516.82	-1,296.08	-6,088.44	1.22	1.22	143.20
4	3,785.89	78	41	37	52.56	1,269.74	6,716.71	-1,304.69	-5,585.56	0.97	1.08	48.54
3	13,296.28	78	43	35	55.13	1,218.64	6,740.50	-1,117.29	-5,361.06	1.09	1.34	170.47
2	13,814.22	78	44	33	56.41	941.13	4,028.44	-836.23	-4,166.72	1.13	1.50	177.11
1	10,558.15	78	45	33	57.69	566.78	2,731.56	-452.93	-2,722.61	1.25	1.71	135.36

Breakouts under these conditions have seen essentially no edge over the next few days.

I have updated the Aggregator chart below.



With the new breakout evidence to consider tonight the green Aggregator line moved above zero. Positive readings mean net expectations from the Active List are for upside over the next few days. Meanwhile, the black Differential Line remained 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 0. 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 compelling new bearish studies could change this. The Differential Pivot will be 2458.38 on Monday. That is less than 1 point below Friday's close. So SPX would only need to close down about 1 point on Monday in order to move from overbought to oversold versus recent expectations.

The breakout looks pretty good, but the Differential Line suggests the market is a bit extended. Monday could fix this quite easily if we get even a small pullback. And if that pullback is accompanied by more bullish evidence, then there is a good chance I would look to become a buyer. Therefore, I'll be keenly interested in Monday's action along with any new Quantifinder studies that trigger.

Intermediate-term Outlook (2 weeks – 2 months) – updated 7/17 –somewhat bullish

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

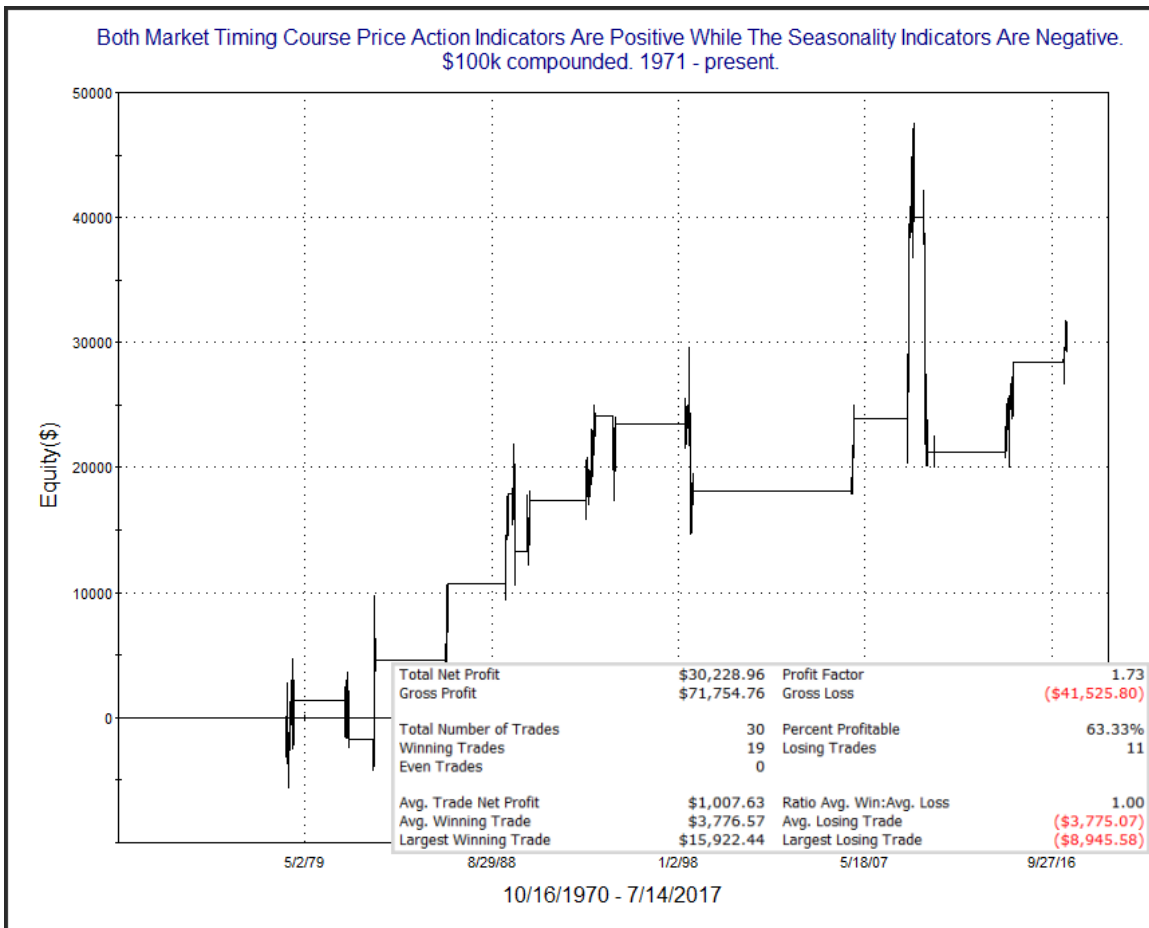
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#), 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 Combo Systems #2 & #3 both switched back from “Flat” to “Long”.*

The SPX put in solid gains this week by closing 1.4% higher than last Friday. The NASDAQ did even better. The relative outperformance of the NASDAQ helped it to retake a leading position based on our NASDAQ/SPX Relative Strength Indicator. This was after just 2 weeks of it falling into a lagging position. Below is a chart of the indicator from the website.



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 1878.88 points when the NASDAQ has been leading versus 478.29 points when the NASDAQ has lagged. The difference for the NASDAQ has been even more dramatic, with the point gains being 5916.85 vs. just 287.24. 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) “Worst” 6 months in effect. Below are updated stats showing SPX performance during this alignment.



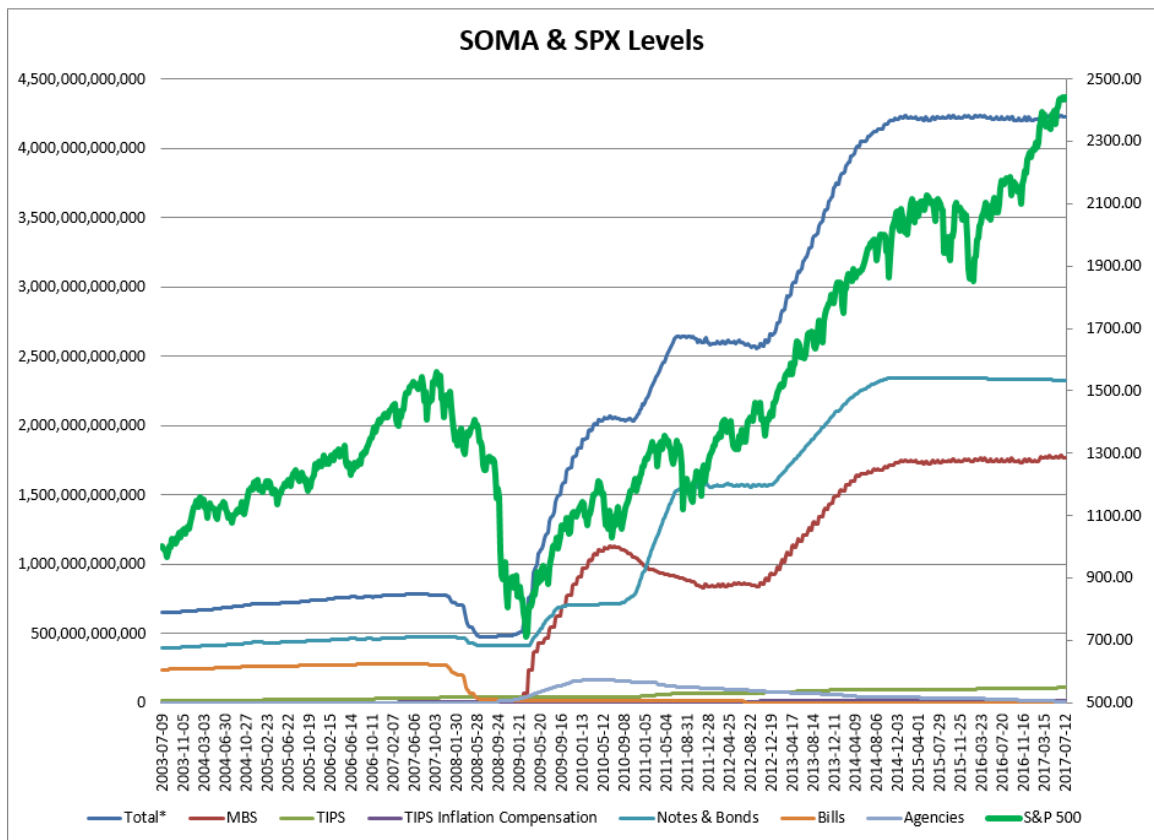
We see here that similar formations have seen gains in the past. It is notable though that this chart has failed to make any progress over the last 20 years. So perhaps the setup could be viewed as bullish, or perhaps your interpretation would be neutral. In any case, it does

not appear to be bearish. And as you can see near the top of this section, with both Market Timing Course price indicators still positive, two of the 3 “Combo” systems we track are still “Long”.

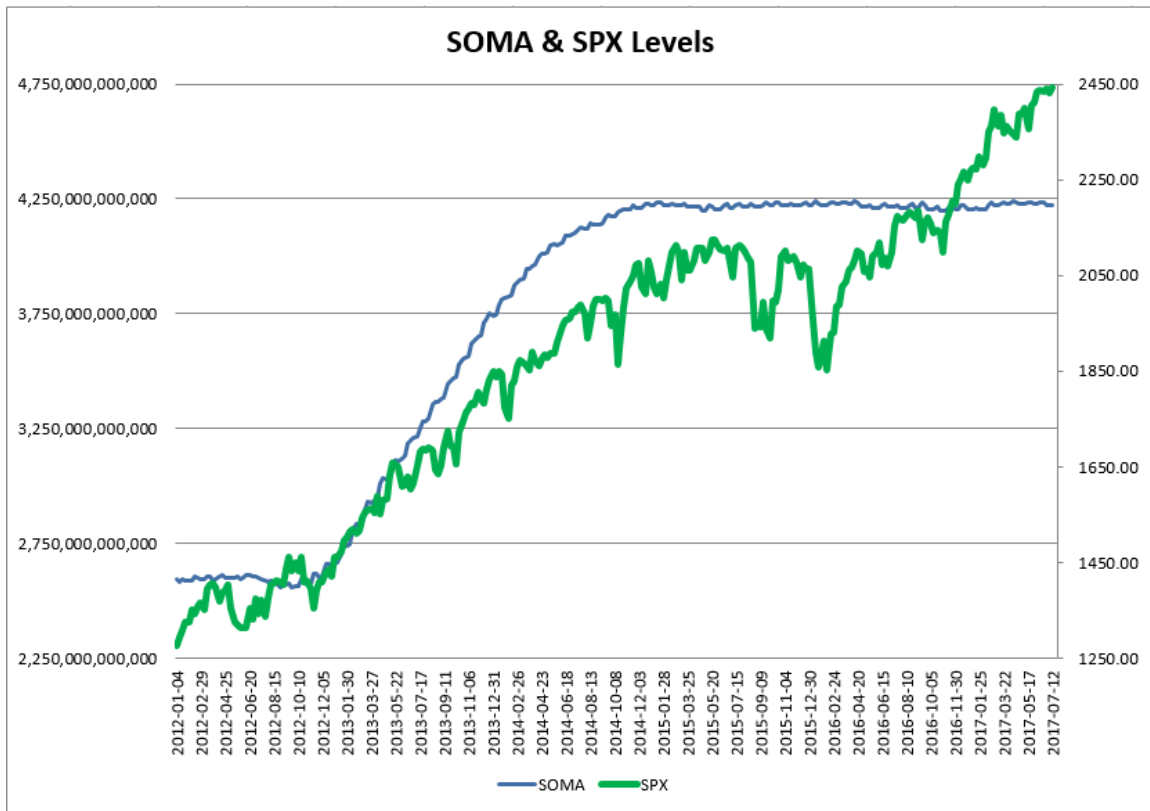
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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).



The Fed's SOMA this past week (Wednesday to Wednesday) put in a very slight decline of less than 0.01%. This was in line with expectations based on the Fed's SOMA schedule. The 0.44% gain for the SPX over this same period was fairly strong. Since the beginning of 2015 SPX has risen 65% of the time for a sum total of 12.79% during the 43 weeks in which SOMA expanded at least 0.01%. During the 87 other weeks (like this one) SPX has only risen 51% of the time and has gained a sum total of just 5.97%. That's less than half the gains in twice the time. Based on the reinvestment schedule the Fed has stuck to over the last two+ years, this current week is likely to see the SOMA rise. But the following week, which starts this upcoming Thursday, is set to show a decline. So bulls should only have a few more days of help from Fed liquidity before it again turns against them.

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 and a half years and we have not seen any strong derivations. That is expected to change at some point this year, and I will be keeping a close eye out to see when it does. I expect liquidity analysis to remain a vital tool for us.

The new highs and the NASDAQ retaking a leading position has brightened my outlook a bit from last week. We also have 50-day Bollinger Band study still active from early June. Bears can point to overall weak Fed support, weak seasonality, a long-term divergence of new highs, and an active Hindenburg Omen cluster to point to. So I am wary of taking a strong bullish stance. But I have decided to move back to “somewhat bullish” for now. This means I will be a little more aggressive with longs and less aggressive with shorts, but am still willing to take either for short-term trades.

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

Symbol	Entry Date	Entry Price	Current Price	% Gain/Loss	Stop	Notes
<i>COST(1/3)</i>	<i>7/11/2017</i>	<i>\$151.00</i>	<i>\$154.26</i>	<i>2.16%</i>		<i>sold on open</i>

COST was exited at the open as indicated in Thursday night’s letter.

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