

QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

July 24, 2017

Volume 10 Issue 140

Market Overview



Signals Overview

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

Tonight's Research Points

- The mild moves the last couple of days have left short-term evidence somewhat lacking.
- SOMA flows are expected to be down or flat the next couple of weeks, which will not help the bull case.

Short-term Outlook

The Bottom Line

Evidence is pointing mildly higher, but the market is a little overbought. Reward/risk is not great and there does not appear to be a strong edge in either direction at the moment.

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 21, 2017	Down close and RSI2 > 90.	1-2 days	Bullish			
Active - Long Term						
July 20, 2017	RSI2 crosses over 99. SPX > 200ma.	1-15 days	Bullish	2.30%	-1.40%	-2.70%
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			

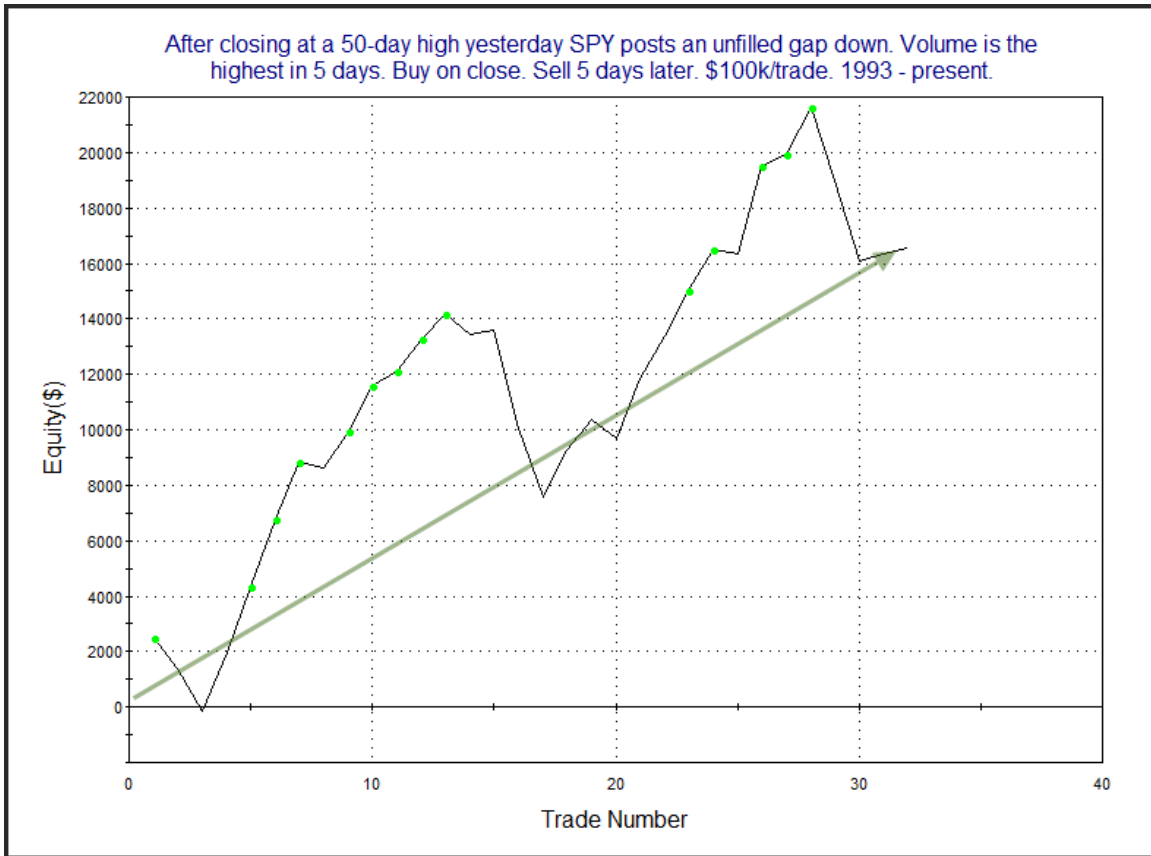
The Evidence

Friday saw most of the indices gap lower and then finish with mild losses near the top of their intraday range. The SPX closed down 0.04%, the NASDAQ also lost 0.04%, and the Russell 2000 fell 0.45%. Breadth was negative as the NYSE Up Issues % was 46% and the Up Volume % came in at 37%. NYSE volume came in higher as it typically does on opex Friday.

The mild action did not trigger much in the way of new studies. SPY's unfilled gap down from a high the day before combined with the higher volume did trigger the study below. It was last seen in the 7/28/14 letter. Stats are all updated.

After closing at a 50-day high yesterday SPY posts an unfilled gap down. Volume is the highest in 5 days. Buy on close. Sell X days later. \$100k/trade. 1993 - 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	16,560.30	32	22	10	68.75	1,479.79	3,192.86	-1,599.51	-3,564.68	0.93	2.04	517.51
4	10,923.76	32	22	10	68.75	1,247.54	2,725.92	-1,652.20	-4,021.24	0.76	1.66	341.37
3	4,617.58	32	18	14	56.25	974.63	2,214.81	-923.27	-3,618.23	1.06	1.36	144.30
2	905.60	33	18	15	54.55	891.81	1,949.79	-1,009.80	-4,109.04	0.88	1.06	27.44
1	3,701.87	33	18	15	54.55	825.83	1,404.00	-744.20	-2,738.12	1.11	1.33	112.18

So the stats seem to favor a bit of an upside edge. The profit curve using a 5-day hold can be found below.



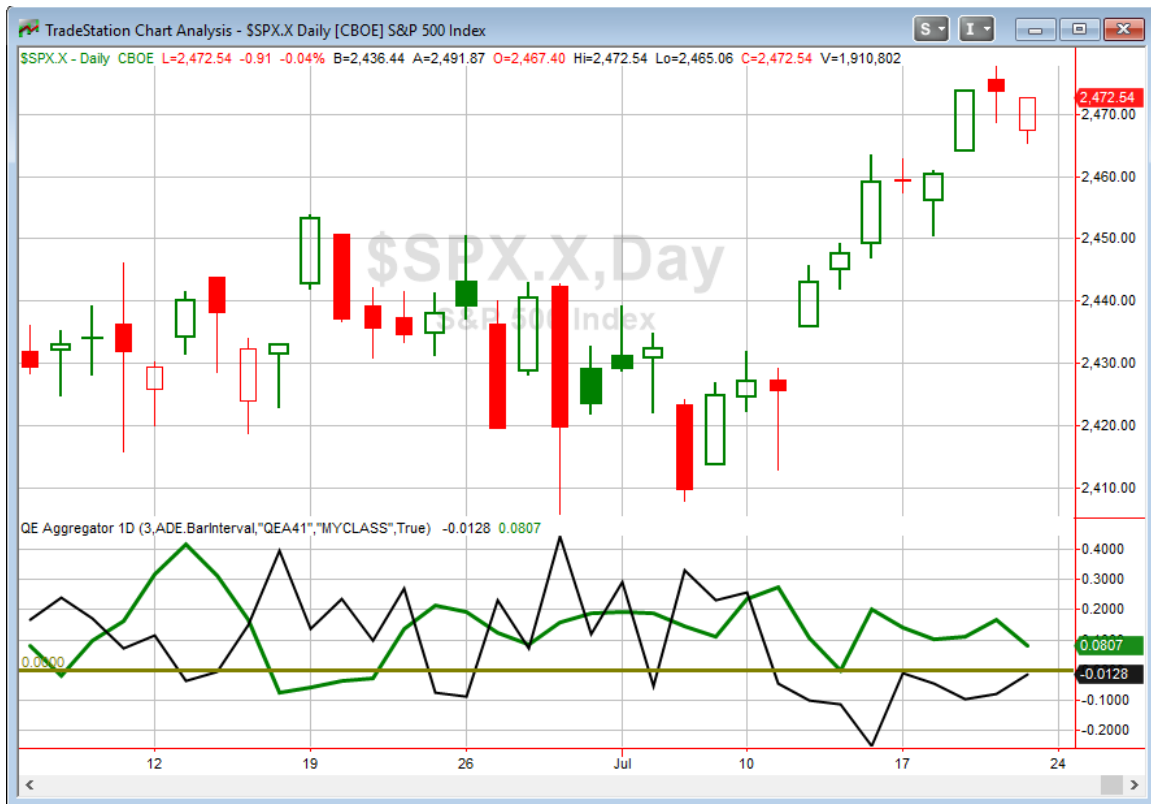
There were a couple of recent instances that have put the curve in a bit of a drawdown. One additional concern I had about this study is the volume requirement. Being that it was opex Friday, high volume is typical, and not indicative of anything else. So I am a bit concerned that it is a “false” reading. I decided to look at other times the setup triggered on opex Friday.

After closing at a 50-day high yesterday SPY posts an unfilled gap down. Volume is the highest in 5 days. It is opex Friday. Buy on close. Sell X days later. \$100k/trade. 1993 - 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	-600.34	5	2	3	40.00	1,846.20	2,074.68	-1,430.91	-3,401.73	1.29	0.86	-120.07
4	-3,917.52	5	2	3	40.00	569.16	734.40	-1,685.28	-3,893.97	0.34	0.23	-783.50
3	-3,577.24	5	1	4	20.00	660.96	660.96	-1,059.55	-1,837.32	0.62	0.16	-715.45
2	-1,365.85	5	3	2	60.00	425.15	761.94	-1,320.65	-1,859.28	0.32	0.48	-273.17
1	1,210.64	5	3	2	60.00	924.02	1,248.18	-780.71	-1,010.16	1.18	1.78	242.13

As you would expect, there have been very few instances. But the fact that they have struggled combined with the recent drawdown in the curve has me wary. I decided *not* to include this study on the Active List tonight.

I have updated the Aggregator chart below.



Without any new compelling 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 remained slightly 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 easily change this. The Differential Pivot will be *inverted* at 2482.60 on Monday. That is 0.4% *above* Friday'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 0.4% on Monday in order to remain overbought.

Anything less than that and it will be considered “oversold” versus expectations at Monday’s close.

The market has lost steam the last couple of days, but it is hardly the kind of pullback that appears to be offering a low-risk entry point for a swing trade. And with evidence light, I am not interested in taking a stand with my hard-earned money. So I am neutral and alert, waiting for the next favorable reward/risk opportunity.

Intermediate-term Outlook (2 weeks – 2 months) – updated 7/24 – 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 there was no change in the Combo Systems. Combo Systems #2 & #3 both remained “Long” while #1 is “Flat”.*

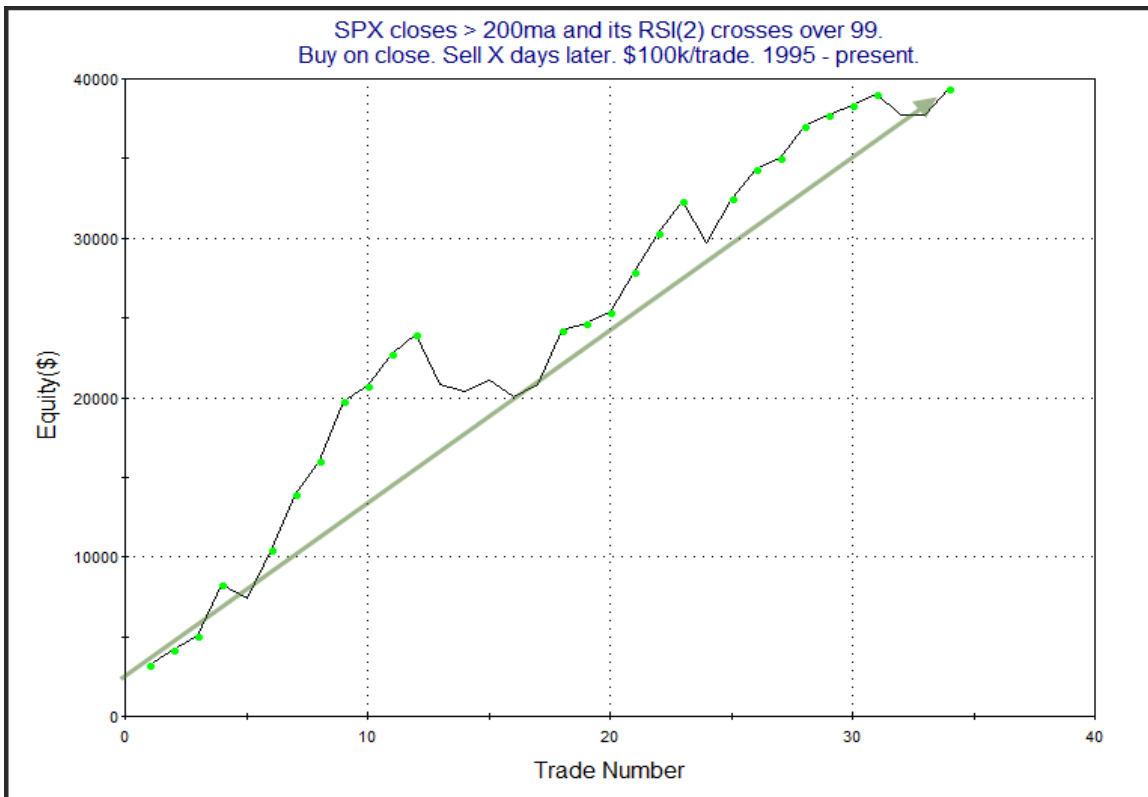
Despite the slight losses the last 2 days, the SPX finished the week up 0.5% and made new highs in the process. The NASDAQ did even better, posting a 1.1% gain on the week. There was one study with intermediate-term implications that was shown in the 7/20 letter. I have copied it below.

The rally over the last several days has been impressive, and it has left the market short-term overbought. Of course short-term overbought often triggers some studies that suggest a downside edge, like it did last night. But when the overbought condition gets very strongly overbought, then those downside edges often disappear. And rather than strength leading to weakness the strength will beget more strength. The strong move higher over the last several days has turned the market so overbought that we are seeing this scenario begin to unfold. It is exemplified in the study below from the 8/19/14 Letter, which uses RSI(2).

SPX closes > 200ma and its RSI(2) crosses over 99.
Buy on close. Sell X days later. \$100k/trade. 1995 - 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
15	39,384.69	34	27	7	79.41	1,802.89	3,782.11	-1,327.63	-3,063.60	1.36	5.24	1,158.37
14	33,813.69	34	26	8	76.47	1,735.31	4,461.36	-1,413.04	-2,699.52	1.23	3.99	994.52
13	33,744.42	35	28	7	80.00	1,606.76	3,989.82	-1,606.42	-3,320.01	1.00	4.00	964.13
12	32,227.83	35	27	8	77.14	1,561.67	4,058.61	-1,242.16	-3,175.53	1.26	4.24	920.80
11	34,997.33	35	28	7	80.00	1,612.15	4,106.40	-1,448.99	-2,523.21	1.11	4.45	999.92
10	27,848.15	36	27	9	75.00	1,487.34	3,770.55	-1,367.79	-2,793.28	1.09	3.26	773.56
9	24,324.17	36	26	10	72.22	1,395.83	3,453.27	-1,196.74	-3,440.07	1.17	3.03	675.67
8	25,400.02	36	25	11	69.44	1,438.53	3,547.80	-960.29	-3,460.32	1.50	3.40	705.56
7	18,557.61	37	24	13	64.86	1,279.71	3,564.39	-935.03	-4,153.62	1.37	2.53	501.56
6	9,809.01	37	23	14	62.16	1,117.93	2,634.36	-1,135.96	-5,296.92	0.98	1.62	265.11
5	6,210.45	37	24	13	64.86	884.49	1,782.39	-1,155.19	-3,596.40	0.77	1.41	167.85
4	5,235.76	37	25	12	67.57	837.42	2,442.90	-1,308.30	-3,039.18	0.64	1.33	141.51
3	-591.01	38	23	15	60.53	699.90	1,982.20	-1,112.58	-2,880.45	0.63	0.96	-15.55
2	1,285.83	38	23	15	60.53	630.08	1,998.39	-880.39	-2,348.76	0.72	1.10	33.84
1	1,689.34	38	20	18	52.63	554.68	2,096.10	-522.46	-3,515.37	1.06	1.18	44.46

The numbers here are basically neutral for the first week or so. On a short-term basis there is no edge apparent. But once you get out 2-3 weeks, it appears the strength has re-asserted itself and the market is often higher. Below is a profit curve showing a 15-day holding period.

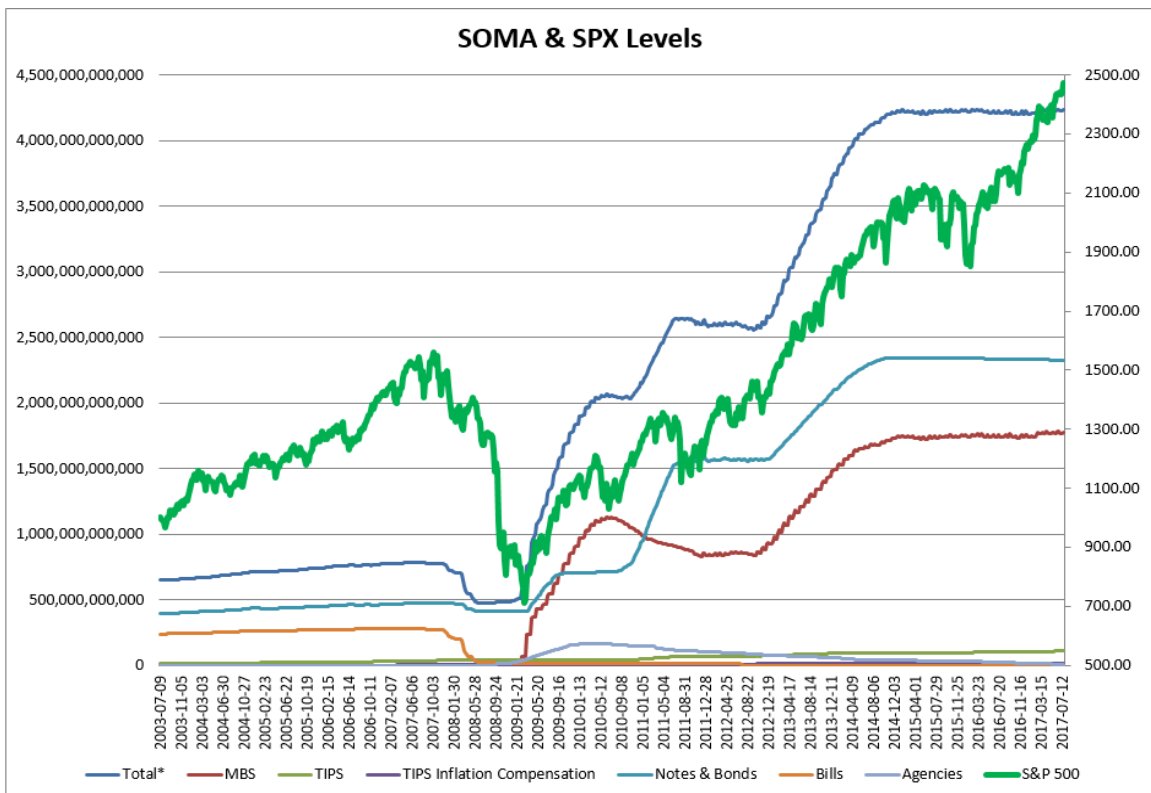


The upside edge has been apparent for a while and still appears to be intact. Obviously this study does not help us with the short-term, but I have added it to the intermediate-term list.

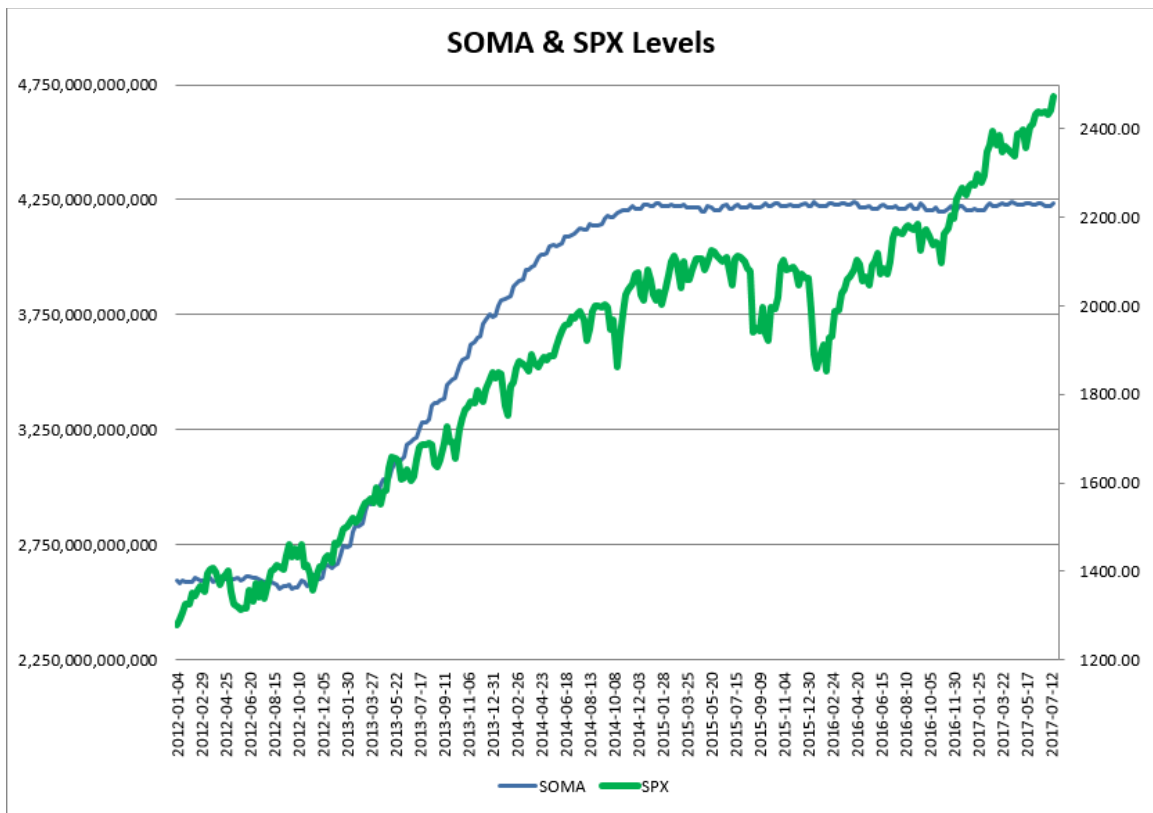
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

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) rose 0.22%. This was in line with expectations based on the Fed's SOMA schedule. The 1.25% gain for the SPX over this same period was fairly strong, but not unexpected. Since the beginning of 2015 SPX has risen 66% of the time for a sum total of 14.04% during the 44 weeks in which SOMA expanded at least 0.01%. During the 89 other weeks 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 decline. And the following week, which starts this upcoming Thursday, is likely to be about flat. So bulls will not have Fed liquidity to help them out in the near future.

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.

For now the bulls appear to be in control. New highs in the major indices show the trend remains up. And the strongly overbought RSI(2) study from this past week suggests the upwards momentum is likely to continue. We also have 50-day Bollinger Band study still active from early June, and 2 of the 3 Market Timing Course Combo Systems are “Long”. Bears can point to overall weak Fed support, weak seasonality, a long-term divergence of new highs, and an active Hindenburg Omen cluster. I think the bullish evidence is trumping the bearish for the time being, and don’t see that immediately ending. So I will be taking a more aggressive approach to longs, and will be extra selective with any short trades until the bullish outlook changes.

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.

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