

# QUANTIFIABLE EDGES SUBSCRIBER LETTER

ASSESSING MARKET ACTION WITH INDICATORS AND HISTORY

December 26, 2017

Volume 10 Issue 248

## Market Overview



## Signals Overview

<b>Aggregator</b>	<b>Aggressive VIX</b>
<b>Flat</b>	<b>50% Long XIV</b>

## Tonight's Research Points

- The SPY gap and reversal on Tuesday after an unfilled gap up on Monday suggests an upside edge for Wednesday.
- SOMA increased this past week, but is still badly lagging the announced schedule over the last 2+ months.

## *Short-term Outlook*

### *The Bottom Line*

The Aggregator is now neutral. Expectations remain bullish and seasonality is positive over the next several days. But the market is now overbought, and it has been overbought by some measures for an extended period. I do not believe there is currently a strong short-term directional edge

*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
<b>Active - Short Term</b>						
December 26, 2017	Unfill gap up. Gap up reverse down.	1 day	Bullish			
December 20, 2017	Twice 3 Nights Before Christmas	1-8 days	Bullish	2.50%	-1.10%	-2.20%
<b>Active - Long Term</b>						
November 30, 2017	SPX 50-intraday high. NDX big down 50	1-50 days	Bullish			
November 29, 2017	SPX breaks 50-day Upper Bollinger Band	1-50 days	Bullish	4.85%	-4.10%	-7.80%
November 14, 2017	SPX top 25% 20day rng. RUT bottom 25	1-40 days	Bullish	5.60%	-2.80%	-5.50%
November 13, 2017	Hindenburg Omen Cluster	1-35 days	Bearish			
October 24, 2017	SPX 20-high. NDX big drop	1-50 days	Bullish	6.30%	-2.80%	-5.50%
October 2, 2017	SOMA reduction begins	int term	Bearish			
April 26, 2016	Golden Cross	int term	Bullish			
July 22, 2013	New High Divergence (Study of Tops)	int term	Bearish			

**The Evidence**

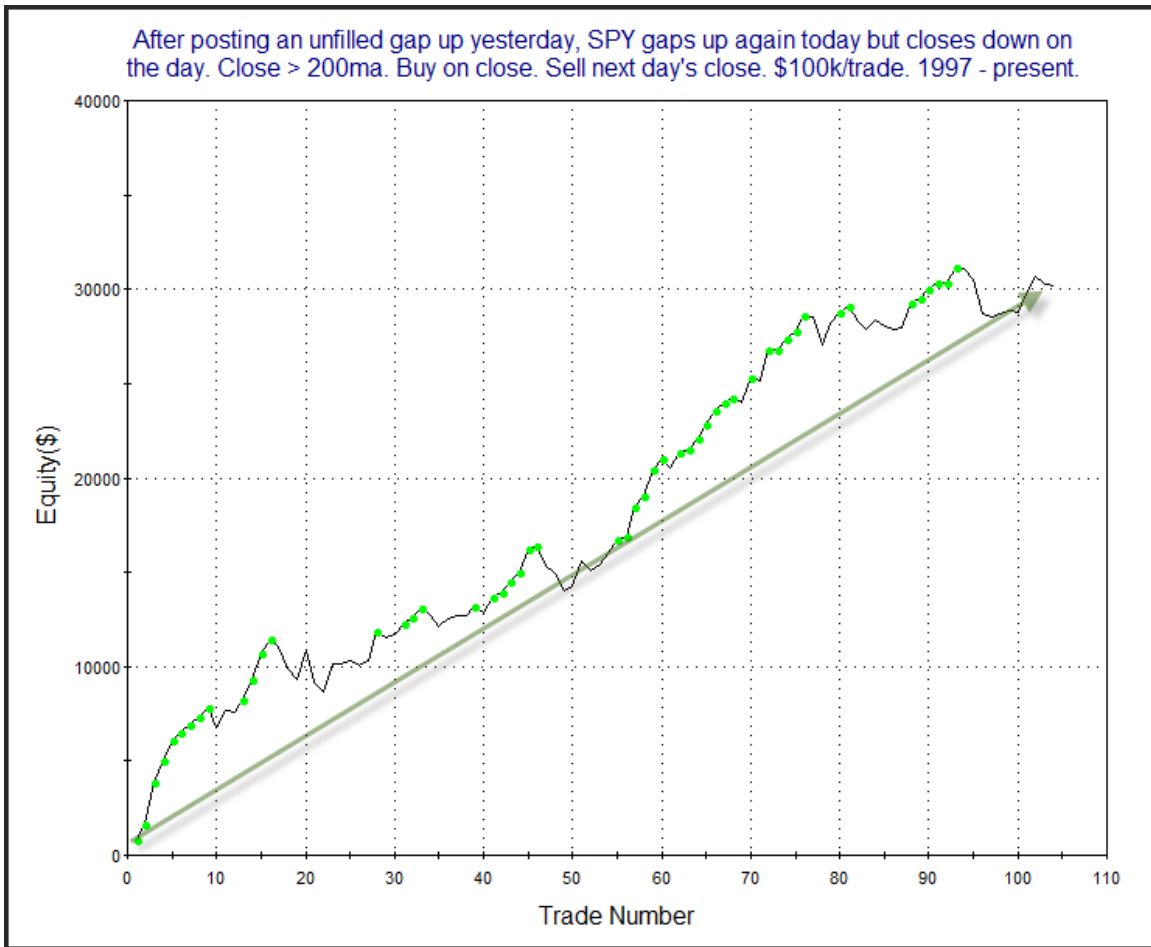
Friday saw mild declines for the major indices. The SPX dipped 0.05%, the NASDAQ lost 0.08%, and the Russell 2000 fell 0.27%. Breadth was positive as the NYSE Up Issues % was 50.3% and the Up Volume % came in at 53%. NYSE volume came in light ahead of the long weekend.

SPY gapped up and closed lower Friday after leaving an unfilled up gap on Thursday. Just a few days ago in the 12/20/17 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 next day's close. \$100k/trade. 1997 - present.

TradeStation Performance Summary				Expand ▾
All Trades				
Total Net Profit	\$30,214.40	Profit Factor		2.69
Gross Profit	\$48,141.07	Gross Loss		(\$17,926.67)
Total Number of Trades	104	Percent Profitable		68.27%
Winning Trades	71	Losing Trades		33
Even Trades	0			
Avg. Trade Net Profit	\$290.52	Ratio Avg. Win:Avg. Loss		1.25
Avg. Winning Trade	\$678.04	Avg. Losing Trade		(\$543.23)
Largest Winning Trade	\$2,194.38	Largest Losing Trade		(\$1,772.16)

The numbers here all look solidly bullish. Below is the profit curve.



Despite the recent dip, the strong, long-term upslope is fairly encouraging. Based on the action of the last 2 days, it appears an up day on Tuesday is fairly likely. I have included this study on the Active List tonight.

I have updated the Aggregator chart below.



With tonight's study included 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 dipped below 0. The negative Differential Line reading means SPX is overbought versus recent expectations. So expectations are positive and 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 turned flat at the close.

Based on the current active list, expectations are slated to remain bullish on Tuesday. Of course, this could change if compelling new bearish evidence emerges. The Differential Pivot will be *slightly inverted* at 2684.32 on Tuesday. That is about 1 point *above* 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 up about a point on Tuesday in order to remain overbought versus recent expectations. Any smaller rise or any decline will turn SPX oversold as of Tuesday's close.

So the Aggregator is neutral. And not only is the SPX overbought, but as I have been mentioning recently, it has been overbought for an extended period of time. In fact, SPX has closed above its 10ma now for 23 days in a row. That is the longest such streak since going 34 days from late Feb to early April 2016. So bullish evidence and strong seasonality against the backdrop of overbought and overdue for a pullback all leaves me uninspired about taking new index positions. I'll continue to wait for a more favorable reward/risk setup.

**Intermediate-term Outlook (2 weeks – 2 months) – updated 12/26– somewhat bullish**

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

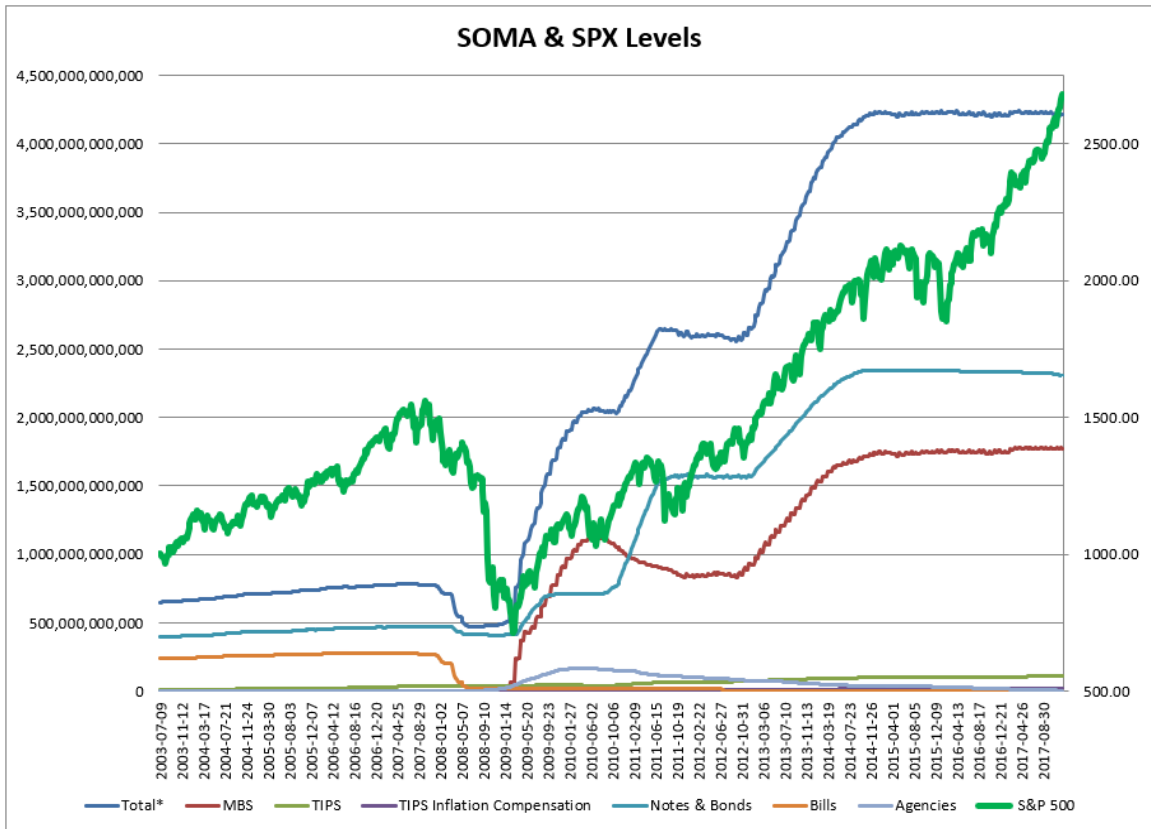
Above is the status of the different Combination Signals from the Quantifiable Edges Market Timing Course. Signals are long-term in nature. All 3 can be either flat or long. None of them look to short. More information on these signals can be found in the [Quantifiable Edges Market Timing Course](#),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

Though the market consolidated the last few days, new highs were again made this past week, leaving little doubt the long-term uptrend remains intact. Despite the new highs, there were no new intermediate-term studies that triggered this past week.

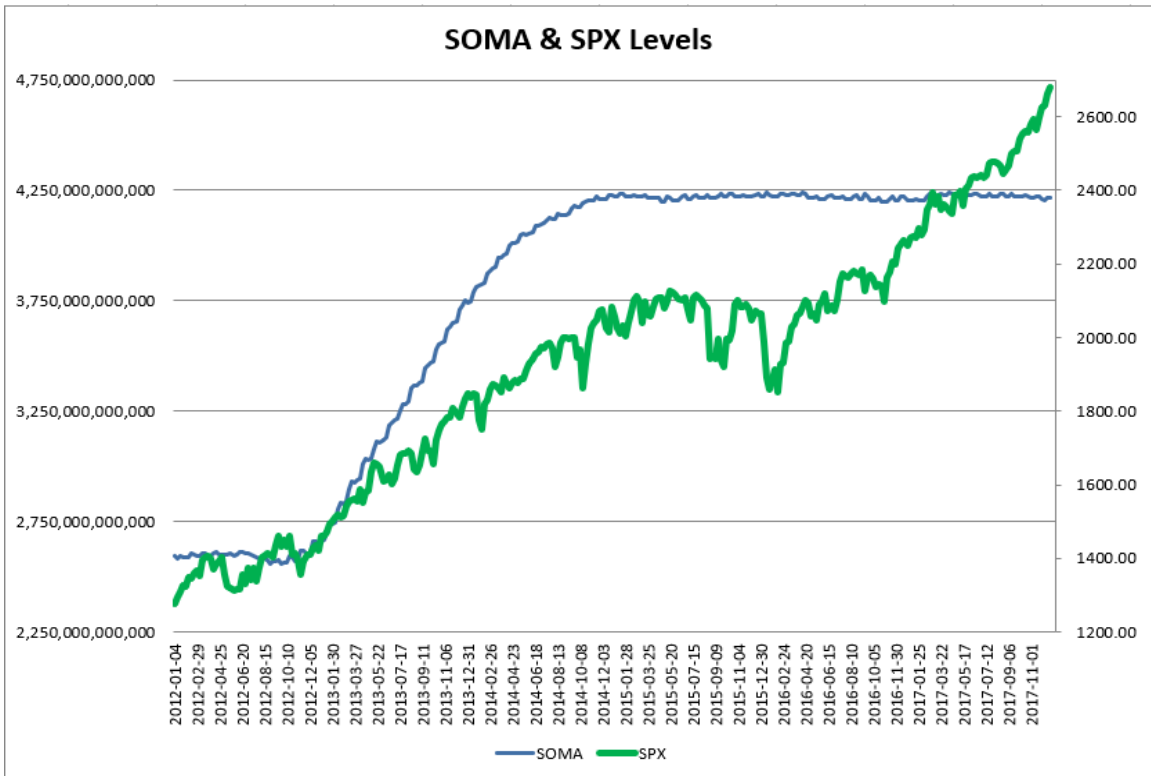
As I do each week, I have updated our Fed SOMA charts below. Below is a description for those who are new to these charts or who may want a refresher.

*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.*

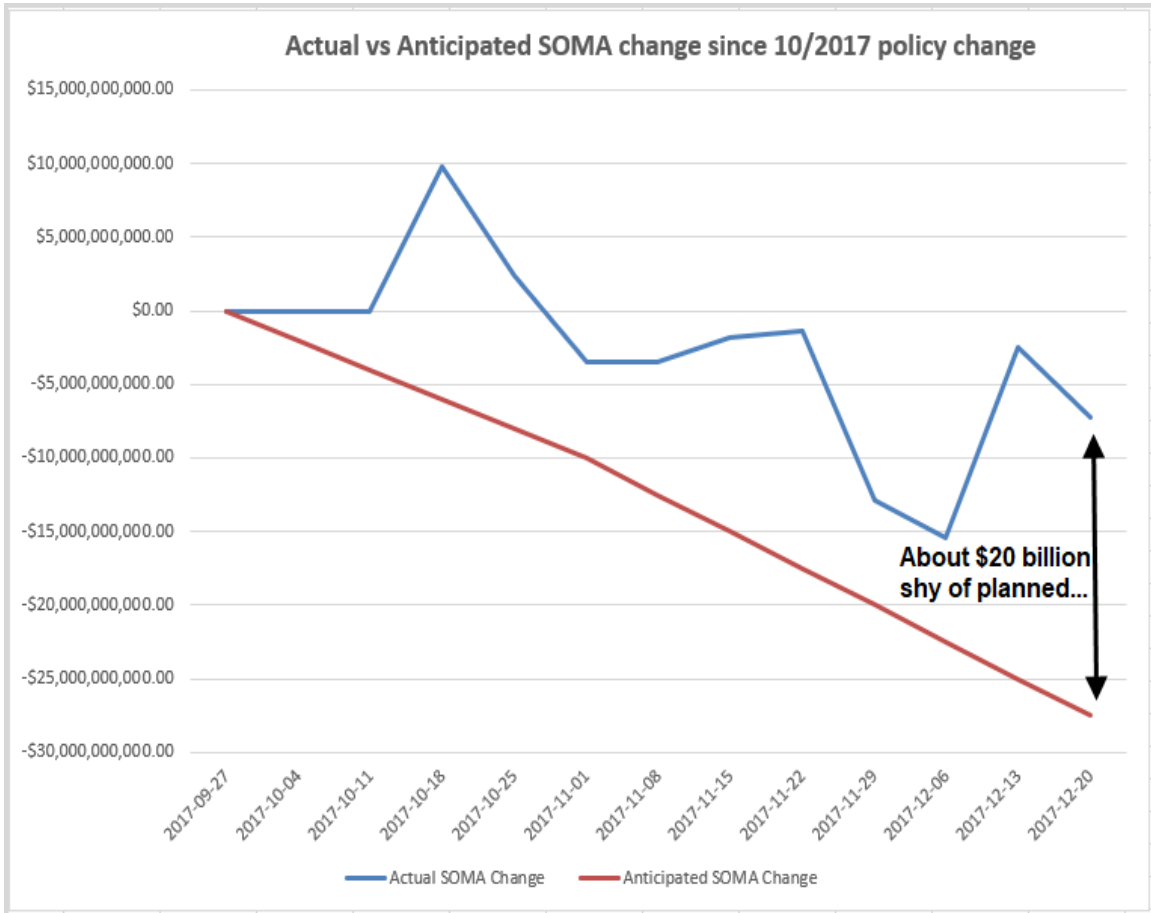
*While the Fed is not making new QE purchases any longer, it is continuing to reinvest maturities. Therefore, the total assets in their System Open Market Account (SOMA) has not begun to dive like the old Quantifiable Edges POMO indicators did. Below are long and short-term views of SOMA and SPX. First, the long-term view (back to 2003).*



And now the zoomed-in view (2012 – present).



The Fed's SOMA this past week (Wednesday to Wednesday) saw a reduction of about \$4.8 billion, or 0.11%. This still leaves it net positive about \$5.7 billion so far in December. In September the Fed announced they would be reducing the SOMA at a rate of about \$10 billion per month starting in October. But in the 2.5 months since the start of October the SOMA has only declined a TOTAL of \$7.3 billion. As we can see in the charts, the market has typically done well when the Fed has expanded the SOMA and it has struggled when there have been substantial contractions. So the market continuing to rally in a period of strong seasonality and net SOMA expansion over the last 3 weeks is not a surprise. Nor is it a surprise that the market has continued to flourish while the SOMA has remained fairly firm the last couple of months. What is as surprise is that the Fed has not been shrinking the SOMA in accordance with their stated policy. I created a chart that shows actual SOMA changes versus anticipated since the beginning of October based on the stated Fed policy.



It did play a little bit of catch-up this past week with the \$4.7 billion reduction, but it remains far off the pace overall. I will continue to watch the SOMA growth/shrinkage to see if it begins to consistently shrink. If that happens, I anticipate a headwind for the bulls. Right now the bulls have strong momentum and seasonality and the anticipated Fed headwind just isn't there. I'll continue to monitor SOMA flows and market action in response to them.

Evidence still appears to be favoring the bulls. There are several intermediate-term bullish studies that remain active. We are in a period of strong seasonality through early January. Additionally, the trend is clearly up, and 2 of 3 Market Timing Course Combo Systems are "long". On the downside, the Hindenburg Omen signals remain. Of course Fed policy, and its implications, are still my biggest concern. There are no signs of a market correction starting just yet. My outlook is again somewhat bullish, and basically unchanged from last week. I will therefore continue to be a bit more aggressive with long trades and a bit more conservative when considering short 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**

*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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