7:00's Report

"Everything you need to know about the markets by 7a.m. each morning, in 7 minutes or less."™

September 10th, 2013

DXJ: First it was the yen breaking its 3 month long uptrend last week, and now DXJ has broken through resistance, further implying the next stage of the "long Japan" trade may be starting.

Pre 7:00 Look

- Futures & international markets higher thanks to more good economic data and increased probability of no military action against Syria.
- Chinese economic data o/n again beat expectations, as August retail sales and industrial production grew more than expected.
- No new news broke on Syria o/n, but the plan to have Syria hand over chemical weapons gained a lot of momentum.
- Econ Today: No reports today, Obama speech on Syria (9:00 PM EST).

Market	Level	Change	% Change
S&P 500 Futures	1677.75	8.75	.51%
U.S. Dollar (DXY)	81.925	.129	.16%
Gold	1372.00	-14.70	-1.06%
WTI	108.69	-.83	-.76%
10 Year	2.897	-.041	-1.40%

Equities

Market Recap

Stocks started the week off strong, rallying thanks to more good economic data out of Asia and a feeling that military action in Syria will be, at worst, "unbelievably small" and, at best, non-existent. The S&P 500 rose 1.00%.

Strong Chinese export growth, benign Consumer Price Index data, and much better than expected Japanese 2Q GDP helped markets start Monday strong.

But, stocks took another leg higher yesterday on a trifecta of "positive" Syria developments. First, it's becoming more and more likely that President Obama will not have the votes to pass his "Strike Syria" resolution through the House of Representatives. Second, in his latest gaffe, Secretary of State John Kerry described any impending military action in Syria as "unbelievably small" while discussing the matter in London. And finally, hopes are rising that there will be no military action at all, thanks to a suggestion by Kerry that turned into a proposal by the Russians to have Syria hand over chemical weapons to international authorities. Late Monday the Syrian government backed the proposal, and the White House is "considering it" (which isn't surprising, seeing that this is a potential bailout for the administration, which has painted itself into a corner). Signaling the situation is fluid, Senate Majority Leader Harry Reid delayed a vote in the Senate authorizing a "Syria strike."

Those events helped stocks move higher, and the rally once again caught pessimistic investors off-guard. It was a "painful" rally, as funds and investors once again seem to be underinvested. Stocks moved higher throughout

Market	Level	Change	% Change
Dow	15063.12	140.62	.94%
TSX	12854.64	33.72	.26%
Brazil	54251.85	502.43	.93%
FTSE	6582.13	51.39	.79%
Nikkei	14423.36	218.13	1.54%
Hang Seng	22976.65	226.00	.99%
ASX	5201.17	19.70	.38%

Prices taken at previous day market close.

the afternoon and went out basically at their highs.

Trading Color

Cyclicals continued to lead markets higher, as the Nasdaq hit a new high for the year (and a new multiyear high) and the Russell 2000 and Dow Transports outperformed yesterday.

From a sector standpoint, all 10 S&P 500 subsectors were higher yesterday. There was once again clear outperformance by cyclical names, as basic materials and industrials rallied hard on the strong Asian economic data. Homebuilders rallied nearly 3% after Hovnanian (HOV) reported an earnings miss but made positive comments on the conference call.

Market	Level	Change	% Change
Gold	1386.90	.20	0.01%
Silver	23.715	-.176	-0.74%
Copper	3.2785	.017	0.52%
WTI	109.45	-1.08	-0.98%
Brent	113.77	-2.35	-2.02%
Nat Gas	3.602	.072	2.04%
Corn	463.75	-4.50	-0.96%
Wheat	640.50	-7.25	-1.12%
Soybean	1356.25	-11.50	-0.84%
Prices taken at previous day market close.			

Despite the rally in bonds, "bond proxy" and safety sectors continued to lag as utilities, consumer staples and healthcare all finished higher, but lagged the major averages. REITs, oddly enough, were one of the outperforming sectors, benefiting from the positive housing commentary from HOV. The Vanguard REIT Index ETF (VNQ) looks like it could have put in a "double bottom" at the $63.50 level.

On the charts the S&P 500 got back above its 50-day moving average and now sits just over 2% from the all-time highs. Volumes were elevated yesterday as it seems people are finally back to work. Certainly some of the rally was due to money being put back to work in the market for the stretch run into the end of the year as things were definitely busier yesterday than they had been in some time.

Bottom Line

While Syria dominates the news, I think continued skepticism toward this market and emerging-market calm remain the "real" reasons for the surprise rally yesterday and the reason the market is up 7 out of the last 8 days. Sentiment remains negative and cautious, which is a tailwind, but most importantly we've seen stabilization in the emerging markets. Depending on what happens with Syria, I'd not be shocked if this market heads up and takes a look near those old highs in the near future, as long as EMs can behave.

One Offshoot of Declining Bonds

Big trends (trends that take quarters and years) like the decline we're seeing in the bond market, have all sorts of offshoots that provide opportunities to make money. When I was at the commodities fund in the mid-2000s, the primary "commodity bull market" thesis led to a rally in commodities. But there were also all these peripheral investments that provided an opportunity to profit in addition to just being "long commodities." To name a few, Canadian and Australian stock markets hugely outperformed, the Loonie and Aussie rallied nearly 50% over several years vs. the dollar, and seats on the CME, NYMEX and COMEX surged in value. So, like a big river with many tributaries, big trends like we're seeing in the bond market will have several "offshoots" that can potentially be profitable.

To that end, it seems as though the "end of low rates" is starting to "pull forward" a lot of M&A, as companies think about the future rising cost of capital. The low cost of debt financing was cited as a reason Verizon (VZ) bought Vodafone's (VOD) stake in Verizon Wireless recently, and Apple (AAPL) issued ridiculously cheap corporate debt to help finance a buyback. These are two examples, but it got me thinking—will M&A-focused investment banks stand to benefit from this more so than the rest of the financials?

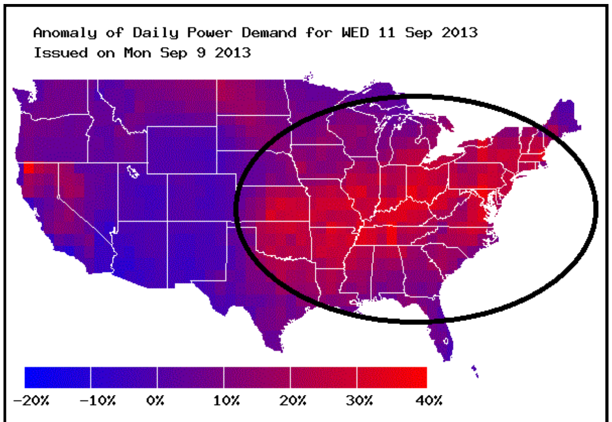
Obviously, one way to play this uptick in M&A and corporate finance is through the major investment banks: MS, GS, JPM, BAC, DB, etc. But, there are also some smaller "purer plays" on M&A like LAZ, GHL and EVR.

LAZ has always seemed to outperform whenever we've seen a substantial uptick in M&A, as they seem to always get parts of deals. Obviously more research needs to be done, but maybe one of the short-term offshoots of the end of the bull market in bonds is increased M&A fees for the investment banks. Food for thought.

Is Larry Summers a Casualty of Syria?

One of the more interesting things I was reading yesterday had to do with the topic of Chairman Bernanke's successor. Over the past two weeks, the market had largely become resigned to the fact that Larry Summers would become the next Fed chair, which was viewed as an incrementally "hawkish" event. Acceptance of that fact is something that I think helped push Treasury yields to their recent highs.

But, I'm hearing a lot of chatter that, because President Obama has spent so much political capital on getting this Syria resolution passed (which incidentally may not even be voted on now) he may not have enough left to get Summers into the Fed chair. (Summers remains Obama's #1 pick, but there is a lot of opposition in Congress.)



Warmer than normal temperatures are moving east this week, resulting in an expected uptick in cooling demand in heavily populated areas.

At a minimum, the announcement of a new Fed chairman, which prior to Syria many were penciling in for early to mid-September, will inevitably be delayed due to the Syria resolution.

Bottom line is the market "thought" it was Summers all along, but if Janet Yellen gets the nod, that will be a "dovish" event compared to current expectations, and I'd expect to see Treasurys rally off that news.

Economics

No economic reports yesterday.

Commodities

Market	Level	Change	% Change
Dollar Index	81.755	-.412	-0.50%
Euro	1.3267	.0085	0.64%
Pound	1.5708	.0074	0.47%
Yen	.010042	-.000035	-0.35%
CAD $	.9644	.003	0.31%
AUD $	.9232	.0047	0.51%
Brazilian Real	.4311	.00395	.92%
10 Year Yield	2.897	-.033	-0.85%
30 Year Yield	2.897	-.041	-1.40%
Prices taken at previous day market close.			

Commodities saw modest declines to start the week as a reduction of angst toward Syria led to a sell-off in oil. This pulled commodity indices lower despite more strong Chinese economic data and a weaker U.S. dollar.

Energy, excluding natural gas, was weak Monday, with WTI and Brent crude falling 0.9% and 1.9% respectively. Some of the geo-political premium is coming out of oil, thanks to the Kerry "unbelievably small" comments and news that Russia is trying to persuade al-Assad to hand over his chemical weapons to international agencies.

Fundamentally, though the news was good for oil yesterday and this morning—increased export growth from China, especially from the U.S. and Europe, provides more anecdotal evidence the global economy is turning.

But right now the oil market is all about Syria, and we're seeing a reduction in geo-political premium. Nonetheless, it seems the range in WTI crude has moved higher, perhaps to $105-$110 from the previous $103-$108. So, I'd look to be a buyer of crude or energy on a dip to the $105—$107 range.

Natural gas was the best performing commodity yesterday, rallying 1.5%, as hot temperatures moving east over the next few days are causing shorts to cover. But, it'll take more than just a few days of heat to get natural gas through the highs from last week of $3.72.

Turning to the metals, copper rallied 0.6% off the positive Chinese economic data, and looks like it's starting to move higher again after consolidating the recent breakout.

Yesterday gold and silver were flat and down 0.7% respectively, and that's pretty discouraging as the Dollar Index dropped sharply. The weakness has carried over to this morning as both gold and silver are both sharply lower on a perceived reduction of Syria risk.

Fundamentally, the latest Commitment of Traders report released Friday didn't show any great changes in the "speculative net longs." The numbers increased marginally for gold and silver, but remain well below levels you would consider "frothy" on the long side.

Bottom line, though, is the "easy money" in gold and silver has been made, in that the rally from $1,180 to here has been almost entirely short-covering. For gold to continue this rally we've got to see longs get added, and that will take people expecting inflation. I think over the coming months that happens, but we may be stuck in a bit of a range in gold for a while until it does. $1,357 and then $1,347 remain key support levels.

Commodities in aggregate continue to consolidate gains, but the revival in global growth remains a powerful tailwind that favors industrial commodities most directly.

Currencies & Bonds

There were "dovish" underpinnings in the currency and bond markets yesterday thanks to a multitude of factors: reduced probability of a Syria attack, rumors Larry Summers may no longer be the favorite for Fed chairman and, speaking of "unbelievably small," the Fed tapering is now expected to be minimal thanks to the disappointing jobs report and Esther George's comments about a max $15 billion taper.

Treasuries continued their bounce from Friday, although they closed yesterday well off their highs. But, given how oversold bonds are and the growing expectation of 1) no Summers as Fed chair and 2) a very small tapering, I continue to think we've seen the highs in bond yields for at least a few weeks.

Treasuries, like everything else, are waiting to see what happens with Syria, although we will get some insight into fundamental demand given there is a 10-year auction Wednesday and a 30-year auction Thursday. (There's a 3-year auction today, but I expect demand will remain strong for near-dated issues.)

Turning to currencies, the Dollar Index declined 0.44% with the euro, pound and Aussie dollar all rallying about 0.5%. While the euro and the pound rallied on dollar weakness, the Aussie actually caught a bid from some positive fundamental news.

First, the positive China data helped peripherally. (Although as an aside, Chinese imports missed expectations mostly due to higher raw materials prices causing importers to cut demand, so it's not quite as Aussie-bullish as you would think.)

The real bullish news came after Australia's elections this weekend, which saw a pro-business coalition led by Tony Abbott sweep to victory on a pledge to repeal the recently enacted carbon tax and cut a 30% mining profits tax instituted by the outgoing Labour Party several years ago.

I said several weeks ago I thought the short in the Aussie dollar was over, and this election result only further confirms that notion. The removal of some of the regulations and red tape instituted by the Labour Party will help the Australian economy.

Although I think that the Aussie short trade is over, I wouldn't be inclined to get long either, as the Reserve Bank of Australia wants a weaker Aussie to help spur exports.

One thing I am interested in, potentially, is getting long Aussie shares via EWA. If we step back, the environment is becoming more favorable for Australian shares: China's economy appears to be stabilizing, the global economy is bottoming, the Aussie dollar is going to remain low thanks to the RBA, and a pro-business government just took hold. I want to do some more research on the group that just took control, but perhaps after years of a struggling economy, dawn is finally breaking in Oz.

Have a good day,

Tom

The 7:00's Report Asset Class Dashboard

(Outlook on the primary trend for major asset classes over the next month)

	Fundamental Outlook	Technical Outlook	Overall	Comments
Stocks	Neutral	Bullish	Bullish	*US equities have been consolidating recent gains and going through a typical correction. Emerging market turmoil has acted as a headwind, but stabilization last week in EM's helped stocks rally. But, for now, markets appear stalemated ahead of a mid-September FOMC meeting where tapering will be announced.* *The S&P 500 support is now around 1630ish while resistance is at 1660ish.*

Trade Ideas

Long/Overweight: **The biggest trend in the equity markets currently is the rotation out of "bond proxy" sectors and into sectors positively correlated to higher rates and more economic growth. So, banks are the most favored sector in that environment, followed by other typical cyclicals like tech, consumer discretionary, and energy. For those looking for a contrarian play, basic materials remains on of the biggest underperformers in the market, but offers value if the economic recovery turns global in the coming months.**

Internationally, European economic data shows the EU economic is finally stabilizing, so long EWU (UK ETF) or EIRL (Ireland ETF) are two ways to potentially get exposure to a recovery in Europe. Also, the "Long Japan" DXJ trade appears to be back "on" and I'd use any decent dip to initiate or add to positions.

Commodities	Bullish	Bullish	Bullish	*The commodity complex continues to see the environment turn more favorable. Global economic growth appears to be turning for the better, especially in China and Europe, while the Fed appears committed to tapering in very, very small increments.*

Trade Ideas

Long: **WTI crude remains one of the more bullish commodities, as increasing domestic demand should help push oil higher over the coming months. The Syrian conflict has resulted in WTI and Brent moving to multi-month highs, but I'd wait for a bit of a pull back as at this point any military strike will be a one off, as opposed to a greater intervention in the region.**

Copper has broken its months long downtrend as global growth appears to be stabilizing, and if that continues, industrial commodities offer some value, and an ETF like DBB will offer substantial upside. More broad based commodity ETF's (like DBC) are also a potential value at these levels, if growth continues to stabilize. Commodities and raw materials are the ultimate "contrarian" investment in the current market environment.

U.S. Dollar	Bullish	Bullish	Bullish	*The dollar index bounced off support over the past few weeks and is now at a one month high. I remain dollar bullish based on the marginal direction of monetary policy, but if the uptrend at 81.00 is decisively broken, I'll have to admit I'm wrong.*

Trade Ideas

Short**: Japanese yen (YCS) as three month long support has been broken, and the declines in the yen have once again begun. Short the euro (EUO) on any further bounce due as the ECB appears ready to act with more LTROs to combat the general lift we are seeing in interest rates as the Fed prepares to taper QE.**

Treasuries	Bearish	Bearish	Bearish	*Recent economic data has cemented the expectation of a small tapering of QE being announced in September. Bonds have sold off hard in anticipation of that announcement, so we may have seen a short term low in bonds, although the longer term trend is still negative.*

Trade Ideas

Buy: **TBF (unleveraged short 20+ year Treasurys) and TBT (2X leveraged short 20+ year Treasury). SJB (inverse junk bond ETF) is also rallying during this period of global uncertainty, and basically has acted as a hedge against falling equity prices. Finally, with the Fed committed to holding down near term rates, the yield curve will steepen dramatically, so STPP should continue to do well.**