7:00's Report

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

September 26th, 2013

Pre 7:00 Look

- US futures and international markets largely unchanged, again, on more Washington paralysis.
- The Nikkei was the star performer o/n, rallying 1.2% as a report from Kyodo News furthered implied the Abe government will cut corporate taxes.
- Economic data o/n was largely inconsequential, as EU money supply and UK GDP met expectations.
- Econ Today: 2Q Final GDP (E: 2.7%). Jobless Claims (E: 330K). Fed Presidents Stein (10:10AM), Kocherlakota (12:15PM), and George (9:15PM) speak .

Market	Level	Change	% Change
S&P 500 Futures	1687.25	1.50	.07%
U.S. Dollar (DXY)	80.53	.087	.11%
Gold	1335.20	-1.0	.07%
WTI	102.74	.08	.08%
10 Year	2.614	-.039	-1.47%

Equities

Market Recap

Stocks declined for a fifth day during another see-saw session as uncertainty emanating from Washington and some lackluster economic releases weighed on stocks. In testament to Washington's ability to ruin a good time, the last time the S&P 500 fell five days in a row was during the "Fiscal Cliff" drama in late 2012. Yesterday the S&P fell 0.27%.

In a similar pattern to Tuesday, stocks opened slightly lower, with the durable goods number the cited reason.

30 Year Treasuries: How High Can They Rally? Well, a true Fibonacci retracement of the declines since May lies substantially higher, so this counter trend rally likely has more room to run.

Then they rallied on the new home sales beat and continued to move higher throughout the late morning and early afternoon. But, just like Tuesday, the rally stalled mid-afternoon and stocks drifted lower into the close, again exhibiting the fact that this market acts "tired."

Trading Color

Once again participation and volumes were light yesterday, as investors and traders remain in a Washington-induced holding pattern. And, although the market is off more than 2% from last week's all-time highs, the declines are much more the result of a "buyers' strike" than aggressive selling—and that's been evident this week as stocks fade into the close thanks to a lack of bids. Sentiment is much more "let's wait and see" than it is outright negative.

Looking at the market internals yesterday, consumer staples were the worst-performing sector. That was thanks in large part to Wal-Mart (WMT) weakness, which was the result of a negative inventory story from Bloomberg, which was then refuted by the CEO on

Market	Level	Change	% Change
Dow	15273.26	-61.33	-.40%
TSX	12836.71	-12.18	-.09%
Brazil	54261.11	-169.91	-.31%
FTSE	6544.13	-7.40	-.11%
Nikkei	14799.12	178.59	1.22%
Hang Seng	23125.03	-84.60	-.36%
ASX	5294.46	18.52	.35%
Prices taken at previous day market close.			

CNBC. (Media war!)

Despite the move lower in bond yields (the 10-year yield is threatening to break below 2.60%), utilities and other "bond-proxy" sectors didn't rally. This again implies we are not seeing the wholesale reversal of the "out of bond-proxy, into cyclical" sector rotation that defined summer trading.

Market	Level	Change	% Change
Gold	1334.30	18.00	1.37%
Silver	21.82	.22	1.04%
Copper	3.2720	.0155	.48%
WTI	102.31	-.82	-.80%
Brent	107.95	-.69	-.64%
Nat Gas	3.502	.01	.29%
Corn	4.55	.06	1.34%
Wheat	6.71	.12	1.86%
Soybean	13.21	.09	.70%
Prices taken at previous day market close.			

In fact, financials bounced yesterday as Deutsche Bank comments at a Bank of America Merrill Lynch conference weren't as bad as feared. Basic materials, telecom and homebuilders (new home sales were good enough) were also in the green yesterday.

Volumes were again very, very light, and on the charts the S&P 500 is fast approaching support at the 50-day which sits at 1,680.

Washington Update

Despite the theatrics of the Ted Cruz quasi-filibuster, the "clean" continuing resolution (CR)—which strips the language of de-funding Obamacare—passed a procedural vote and apparently will be voted on by the full Senate on Friday. The bill will return to the House Saturday … leaving 3 days to get it through the House.

Right now the large expectation is for the House to pass the "clean" CR bill from the Senate, and then we all move to the debt-ceiling fight. But, here is the risk: There is a chance that John Boehner may attach some amendment to the clean CR bill and send it back to the Senate. Those potential attachments include: a one-year delay of the individual mandate in Obamacare, a permanent removal of the employer mandate, approval for the Keystone pipeline and others. If there is something attached to the "clean" CR bill, the odds of a government shutdown will rise dramatically and risk assets will decline, probably sharply, as we'll start this process all over again. But, right now that remains a small probability. (But with this group, meaning both parties, you never know.)

Bottom Line

Markets hate uncertainty, especially uncertainty from governments, and we seem to have a bull market in that right now. So, until Washington gets out of the way, I don't expect stock prices to go anywhere. Let's just hope no "jack in the box" pops out that results in aggressive selling, because there are no buyers willing to step in at these levels.

As an aside, just in case you think passage of the continuing resolution results in a relief rally, consider this: The CR bill being debated only funds the government through Nov. 15. So, if they don't address a new CR in the debt-ceiling fight, we get to do this again in about six weeks. Point being, more uncertainty.

One more thing to consider: It's October (basically). If you're a money manager sitting on double digit gains year-to-date, my question is, what's the potential upside over the next three months compared to the risks? Do you stay "risk-on" and let government nonsense potentially take your good year away if Washington creates a sell-off? At some point all this uncertainty will make profit taking more attractive based on the calendar, and that's another potential headwind on markets to watch for.

Economics

There were two economic releases that thankfully gave us some actual hard data to look at, as opposed to the word choice of some Fed governors. Unfortunately, both durable goods and existing home sales were generally lackluster. Durable goods was the more-important number, and I cover it in greater detail below. But the summary is that new home sales were basically in line with expectations, prices dropped slightly and supply remains tight at five months' worth (down from July's 5.2).

But, the important takeaway is that the housing data this month shows that, while the housing recovery is losing some momentum, it isn't falling off a cliff. This is an underlying positive for the economy, although the market didn't trade that way Wednesday.

Durable Goods Orders

- August Durable Goods rose 0.1% vs. (E) -0.5%
- New Orders for Non-Defense Capital Goods excluding Aircraft (NDCGXA) rose 1.5%.

Takeaway

Durable goods' headline new orders number beat expectations and turned positive again for the fourth time in five months. (However, last month was a bit gloomy at minus 8.1%.)

The most important number in the release, and the best indicator of business investment, is the new orders for non-defense capital goods excluding aircraft. This increased 1.5% in August, a positive sign. However, the three-month moving average for NDCGXA declined for a second month in a row ... which is a touch concerning from a business-investment standpoint, and potentially implies some downside risks to Q3 GDP from current expectations. That matters because Fed President William Dudley so much as said GDP growth is now the main metric with regard to when the Fed will taper QE.

Bottom line is August durable goods was "OK" but the trend in the data is a touch concerning. Nothing in the report will make QE tapering any more likely than it was Tuesday.

Commodities

Commodities rallied modestly Tuesday as the less-than-inspiring economic data resulted in a weaker dollar, which in turn resulted in an oversold bounce in commodities. In testament to the economic data being the main driver of commodity prices yesterday, precious metals led the rally while industrial commodities lagged.

Market	Level	Change	% Change
Dollar Index	80.420	-.27	-0.33%
Euro	1.3526	.0047	0.35%
Pound	1.6070	.0073	0.46%
Yen	.010165	.0000410	0.40%
CAD $	.9677	-.0013	-0.13%
AUD $	.9315	-.0028	-0.30%
Brazilian Real	.4425	-00585	-1.30%
10 Year Yield	2.614	-.039	-1.47%
30 Year Yield	3.648	-.024	-.65%
Prices taken at previous day market close.			

Gold and silver were the best performers yesterday, rallying 1.5% and 1.3% as the economic data inspired a short-squeeze in a quiet market. But, more broadly the outlook for the metals remains challenging. Bulls will point to the fact that the pre-FOMC lows of last week (which are basically $1,300/oz.) appear to have held—but bears will more forcefully point out that the dollar is down multiple percentage points since the FOMC's surprise announcement, and gold has seen virtually no bounce.

Interestingly, while I was at the commodities conference earlier this week, virtually everyone was long-term bullish of gold, and at the same time short-term cautious.

But, there was widespread consensus among analysts that confirms what I've been saying: Gold needs inflation to mount any material rally, and until that appears in earnest, gold will have a hard time rallying. $1,375 is the level to watch (it's last week's high). If gold can break that, then the rally may be back on, but for now I'd not participate on the long side.

WTI crude fell to new lows yesterday, and my bullish thesis on oil's uptrend is being put to the test—hard.

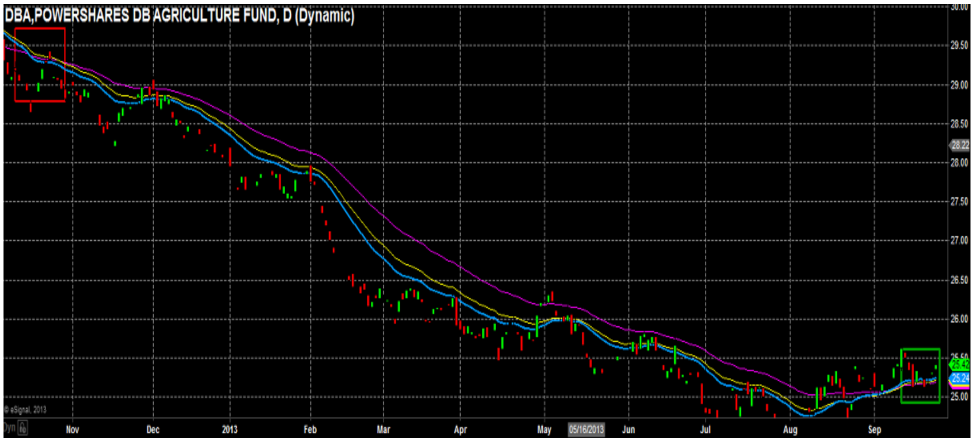
WTI declined yesterday mainly off the bearish inventory data, although the lackluster economic data didn't exactly help, either. The weekly build in crude inventories was much larger than expected, as the EIA reported a 2.6-million-barrel increase vs. expectations of a 900K-barrel draw. That large build basically reverses the bullish supply data we saw last week.

WTI is now threatening to break that uptrend line from April, and if it does decisively break it, I won't consider that a positive for other risk assets. This doesn't appear to be a "healthy decline" because it's not being prompted by a significant supply surge. Instead it's driven by demand concerns. (Yesterday's build not withstanding, oil globally remains relatively "tight" from a supply standpoint.)

Are the "Ags" Bottoming?

I spent five-plus years trading the agricultural commodities in the mid-2000s. But this year, given the enormous crop sizes coming, I've largely ignored the space in the Report because I haven't thought there was much opportunity there. But, yesterday the "ags" were universally strong, with wheat up 2% and corn up 1.5%.

In this space, I watch the agricultural commodity ETF, the PowerShares DB Agriculture Fund (DBA). While I'm not a market technician, one technical signal that I do look for in commodity markets is when the 23- and 30-day exponential moving averages cross the 50-day EMA to the downside (bearish) or upside (bullish). Over my years of commodity trading, it's been a very good indicator in signaling a trend change in commodities.



It has piqued my interest, then, that DBA a bullish cross earlier in September, as the 23- and 30- crossed the 50.-day And, while DBA itself is an ETF, it's based on commodity futures, so I'm thinking the principle holds.

I've got to look at what's happening with the near-record crops we're expecting this fall, and see whether the fundamentals have, at a minimum, stopped getting more bearish, as they've done for months. But, DBA seems to be about the only thing in the market that isn't totally dominated by the Fed outlook—so, perhaps the "ags" offer some opportunity here. I'll investigate further and let you know what I find.

Currencies & Bonds

The Dollar Index bounce from last Wednesday's post-FOMC collapse ended Wednesday, as weak economic data led to a sell-off. Durable goods and new home sales, which are normally not exactly market-movers, carried more weight than normal amidst quiet trading.

In the post-FOMC surprise, we've learned through Ben Bernanke's presser and Dudley's comments that basically the Fed is now looking at GDP as the main "threshold" to taper QE, not unemployment (although it's still important). Weaker durable goods means downside risks to GDP, so in this Fed-dominated market, durable goods carries more weight than usual. At least, that's the perception.

Likewise, housing is a critical part of the recovery, and the Fed is nervous about the effect of higher mortgage rates on home sales, and likely won't taper until they are reasonably sure higher rates won't kill the housing rebound. (Which it won't, at least not at sub-5% mortgage rates. I got my mortgage in 2010, when the economy was way worse, and I'm paying 5 1/8%.) But, the "in line" new home sales report, which reflects some normal cooling of the housing market, again certainly isn't prompting the FOMC to taper any sooner. So, in a thin market, both reports are dollar-bearish, marginally.

Every major currency pair rallied vs. the dollar yesterday as the euro, pound and yen rose just under 0.5% each vs. the dollar—again because of dollar weakness, not any foreign-currency strength.

Treasuries rallied again Wednesday, rallying 0.4%, which makes sense given the weak economic data (weak data + no tapering = good for bonds). Also helping Treasuries move higher was a well-received five-year Treasury auction that saw a bid to cover of 2.67, which was much higher than last month's 2.34%. But, then again, demand for near-term Treasuries has remained pretty solid even throughout the longer-dated bond declines of the summer.

The big question everyone is asking is, "How high can Treasuries rally?" Depending on the Fed, I think the answer is "Pretty high," before rolling over again. The chart on page one shows the Fibonacci retracement for the decline in bonds since May, so if the 30-year retraces 50%-62% of that move, which absolutely can happen, then we've got a while to go. Point being, it's all obviously Fed-dependent, but I don't think it's time to step back in on the short bond trade yet.

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	*Stocks shot to all time highs on a surprisingly dovish "no taper" Fed decision but concerns are growing about the Fed's credibility and plan to unwind QE. At this point, though, the benefit of the doubt remains with the bulls, and performance chase into month/quarter end will be a short term tailwind on stocks.* *Markets have fallen nearly 2% from recent highs. Major support sits at the 50 day MA, which is at 1679.*

Trade Ideas

Long/Overweight: **International markets continue to remain attractive based on improving economic data, and looming political and monetary clouds in Washington. Internationally, European economic data shows the EU economy 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" as its broken through resistance, and I'd initiate or add to any positions at these levels or on any dip.**

Domestically, I'd look to allocate to deep cyclicals like industrials (XLI) and basic materials (IYM), as they should benefit from continued Fed stimulus.

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, and the Fed's decision not to taper QE only will serve to stoke inflationary fires and benefit hard assets as the US Dollar declines.*

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. I'd look to buy oil or "energy" in general on any further dip to between $105—$107.**

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	Neutral	Neutral	Neutral	*The US Dollar plunged after the Fed's "No taper" surprise and broke a multi-year up trend. The dollar had risen in anticipation of Fed tapering, and with that out for now, there will be little in the news to push the dollar higher, although I don't envision a continued sell off either, as the FOMC will taper at some point (Oct or Dec).*

Trade Ideas

Long: **Emerging market currencies (ETF is CEW) such as the Brazilian Real (BZF), Indian Rupee (ICN) or Mexican Peso, as those currencies should see a large rally after the Fed's "no taper" surprise.**

Treasuries	Neutral	Bearish	Bearish	*The Fed's "no taper" surprise has likely marked the end of this initial leg down in Treasuries. Although the fundamentals long term remain negative, we should see a bounce of some sort, although I would look at that longer term as a great entry point on a bond short. If you missed the intial leg down, now's your chance to get back in over the coming weeks/month.*

Trade Ideas

Buy on a significant dip: **TBF (unleveraged short 20+ year Treasurys) and TBT (2X leveraged short 20+ year Treasury). Finally, with the Fed committed to holding down near term rates, the yield curve will steepen dramatically, so STPP should continue to do well.**