7:00's Report

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

January 10th, 2014

Pre 7:00 Look

- Futures and international markets mostly higher ahead of todays jobs report while economic data o/n was mixed.
- Chinese exports rose 4.3% slightly missing analyst estimates, while imports surged 8.3% vs. (E) 5.0%.
- UK Industrial Production unexpectedly stalled, missing estimates for 0.4% growth m/m.
- There were no revisions to final estimates for Q3 GDP in the EU.
- Econ Today: Employment Situation Report (E: 205K).
- Fed Speak: Lacker (8:45 AM), Bullard (1:05 PM).

Market	Level	Change	% Change
S&P 500 Futures	1839.50	6.50	0.35%
U.S. Dollar (DXY)	81.15	.015	0.02%
Gold	1233.10	3.70	0.30%
WTI	92.61	.95	1.04%
10 Year	2.963	-.030	-1.00%

Equities

The stock market sold off shortly after the open yesterday, as most investors were sidelined, looking ahead to this mornings jobs report. But the S&P 500 was able to rally back and close marginally higher. It finished the day essentially unchanged, closing up just 0.03%.

Market Recap

As expected, yesterday was another quiet day in the stock market ahead of both the official start to earnings season with the release of Alcoa's (AA) earnings after the close and, of course, the big jobs number due out at 8:30 ET this morning. Real-money investors stayed out of the market again yesterday, leaving day traders and algos to dictate price action. Despite the lack of real money in the market, the Nasdaq Composite was able to trade to a new 52-week high intraday, but only briefly as Apple (AAPL) and Google (GOOG) came for sale shortly after the market opened. With trading very slow and liquidity very thin stocks have been able to make sharp moves because of fast money funds but those moves are little more than trading noise as there has not been a convicted move in either direction yet this year.

Trading Color

Within the S&P 500, Telecom and tech both underperformed yesterday, while regional banks, airlines, and healthcare all traded ahead of the tape.

Banks continue to outperform, as the bank index, BKX has rallied 5 consecutive sessions now, led higher by the regional banks.

Airline stocks caught a bid reports were released from United– Continental (UAL) that passenger revenue per seat was better than expected in the month of December, while falling crude prices also helped lift prices. UAL prices gained as much as 12.6% yesterday in intraday trading.

Retail stocks were some of the worst performers and broadly weighed on the market following disappointing earnings from both Bed Bath & Beyond (BBBY) and Family Dollar (FDO). There was also weakness in the Semis following several analyst downgrades within the space.

Bottom Line

The key takeaway from yesterday's "boring" session is that the stock market remains just ticks away from all-time highs and is poised to continue rallying.

Market	Level	Change	% Change
Dow	16,444.76	-17.98	-0.11%
TSX	13,629.41	14.78	0.11%
Brazil	49,321.68	-1,254.96	-2.48%
FTSE	6,750.88	59.54	0.89%
Nikkei	15,912.06	31.73	0.20%
Hang Seng	22,846.25	58.92	0.26%
ASX	5,312.38	-12.03	-0.23%
Prices taken at previous day market close.			

However, investors fear that the Fed may consider a more-aggressive approach to tapering QE if this morning's jobs data comes in better-than-expected (too hot scenario). So, with investors nervously waiting on the sidelines, we have been stuck in a stalling pattern since the beginning of the year.

Market	Level	Change	% Change
DBC	24.705	-.195	-0.78%
Gold	1227.80	2.30	0.19%
Silver	19.59	.051	0.26%
Copper	3.2965	-.046	-1.38%
WTI	92.13	-.20	-0.22%
Brent	106.58	-.57	-0.5%
Nat Gas	4.017	-.199	-4.72%
RBOB	2.648	-.0083	-0.31%
DBA (Grains)	24.10	-.22	-0.90%
Prices taken at previous day market close.			

As long as the employment situation is within the wide, acceptable range of 150K-250K jobs added, the path of least resistance (once the dust settles after any knee-jerk reactions) will be for a continuation of the 2013 rally.

Remember that the market fundamentals remain the same as they were in December, which suggests the rally in equities can continue as long as interest rates rise in a controlled manner and investors continue to have faith in the Fed's Zero Interest Rate Policy (ZIRP).

Earnings Season Starts With a Bit of a Thud

Although Alcoa shares gained roughly 38% in the fourth quarter, it seemed to "stub its toe" kicking off earnings season last night. AA shares fell 3.7% in high-volume, after-hours trading after reporting weaker-than-expected quarterly results.

Analysts wanted to see 6 cents per share on revenues of $5.36 billion. But, the recently exiled Dow Industrials component reported adjusted fourth-quarter earnings of 4 cents per share on revenues of $5.59 billion (down from $5.90B in Q4 2012). Part of the 33% miss on the bottom line was a result of federal officials demanding $384 million in fines to the SEC and the Justice Department for foreign bribery violations — fines that will be spread out over several payments, which the company said is "manageable."

The big (and perhaps bigger) struggle AA has been facing recently is the lower cost of aluminum. In the post-earnings conference call, management stated it has a bearish outlook on aluminum prices in 2014. That's because supply is poised to outpace demand this year, as new capacity is expected to come online and production out of China will almost certainly increase.

Bottom line is, lower aluminum prices mean lower earnings for AA. But, that should not be taken as an indication of weakness in the manufacturing sector but rather that the specific market is simply being saturated. All data continues to indicate strength in the broad manufacturing sector.

Economics

Weekly Jobless Claims

- Claims fell to 330K vs. (E) 331K
- The 4 Week Moving Average was down 9.75K to 349K.

Takeaway

Weekly jobless claims were largely in line with analysts' estimates—falling to 330K, the lowest reading in over a month. Claims were down 15K from the week prior, which was revised up to 345K. The four-week moving average fell for the first time in five weeks to 349K.

The weekly report has been more or less "written off" by the markets recently because of inconsistent/skewed seasonal data. The past two weeks have been moderately more "under control" but, nonetheless, there was no real market reaction to the report.

Bottom line is that the report remains largely ignored by investors who are looking ahead to this morning's official BLS employment situation report. Estimates for this morning's report are for the most part between 200K and 205K jobs added in December, consistent with continued growth in the job market. Note that once the markets digest the employment situation report this morning, Wall Street will shift its attention back to earnings season.

Commodities

Commodities were mostly lower as the energy space remained under pressure for the second day in a row. The key difference, however, was that the dollar was essentially flat on the day (as opposed to materially higher on Wednesday), and therefore had no effect on commodities prices. Precious metals were the sole out-performers. The PowerShares DB Commodity Index Tracking ETF (DBC) fell 0.8% to $24.70, establishing a fresh 18-month low.

Gold traded better again yesterday, continuing the recent trend of "less bearish" behavior as it closed up a modest 0.19%. The dollar rallied sharply in response to "dovish" commentary by ECB president Mario Draghi and, although this has no fundamental impact on the value of gold, in recent history gold would have responded by materially selling off. The fact that gold investors and traders alike are overlooking such moves in the greenback is supportive of the $1,200 area continuing to hold in gold. Gold futures ended up rallying back toward session highs into the close, further solidifying $1,200 as a solid support level.

Nymex WTI crude oil opened well below $93 per barrel yesterday and continued to trend lower throughout the session. WTI futures closed the day down 0.22%, trading to a new seven-month low.

There are several reasons being cited for the recent sell-off in WTI prices. First, looking to the fundamentals, crude oil production has been surging here in the U.S.—climbing to the highest level since 1988 while, at the same time, current inventories are sitting near a 30-year seasonal high (which explains the lack of a bid in the market when the EIA printed draws in supply the past six weeks in a row). Also, supply levels are continuing to build in both refined products, RBOB gasoline and distillates (heating oil), which is weighing on demand forecasts for crude oil. And, on a technical note, the major trendline that has been in focus recently finally failed Wednesday, and was confirmed by the sharp sell-off yesterday. Looking ahead, psychological support at the $90 per barrel level is not expected to hold, so the first near-term target is $87.50 while the back side of the broken trendline will offer some resistance just above $93.

Natural gas turned out to be, by far, the worst-performing commodity yesterday as it crashed through the first level of support in the $4.20 range. Nat gas futures fell 4.65% yesterday despite the fact that the EIA reported a draw of 157 Bcf in supply, which was in line with analysts' estimates. Nat gas futures very briefly dipped down to $3.999 in the always-hectic primary close of Nymex trading. $4 is a very important level to watch, not only because of the psychological support it offers but also because it is the approximate location of the 50-day moving average along with some additional technical "trend support." Fundamentally speaking, the term structure in natural gas remains bullish, with front-month prices trading at a premium to back-month futures prices (called backwardation), showing strong immediate demand for physical delivery.

Currencies & Bonds

Currencies were slightly more-active yesterday thanks to both the ECB and BOE meetings. However, the movement turned out to be nothing more than "knee-jerk" reactions. The Dollar Index ended the day essentially unchanged at -0.01%.

In Europe, Draghi stirred things up when he made some "dovish" remarks following the ECB meeting. The euro sold off sharply in reaction to his comment that he may consider lowering the benchmark interest rate to offer extra accommodation. But, shortly after selling off, the euro rebounded back to even for the day.

The BOE announced yesterday that it planned to leave policy unchanged, which was widely expected. However, the pound was able to rally a modest 0.12% against the dollar. Some reports said this was possibly due to the fact that the ECB was more dovish, while the BOE was not, causing a brief spike. But, that is a stretch.

Market	Level	Change	% Change
Dollar Index	81.15	-.012	-0.01%
EUR/USD	1.3587	.0013	.10%
GBP/USD	1.6466	.0019	0.12%
USD/JPY	104.77	-.06	-0.06%
USD/CAD	1.0864	.0046	0.40%
AUD/USD	.8887	-.0014	-0.16%
USD/BRL	2.3902	-.0062	-0.26%
10 Year Yield	2.963	-.030	-1.00%
30 Year Yield	3.873	-.030	-0.77%

Prices taken at previous day market close.

Moving to Asian currencies, the yen took a bit of a breather from its trend lower yesterday as it continues to consolidate near the 105 level ahead of this morning's U.S. jobs report. Keep in mind the yen is just ticks away from its recently established multi-year lows, and some consolidation can be expected. But the trend lower for the yen remains intact and, if we get a “too hot” reading in the employment situation report this morning, we could potentially see a break to new lows in the yen (highs in the USD/JPY pair) as the dollar will rally.

The Aussie dollar traded lower yesterday as a result of some mixed economic data. Australian retail sales beat expectations while building approvals were worse than analysts’ estimates. The Aussie remains in a downtrend, reinforced by the Reserve Bank of Australia’s goals to devalue the currency with a target of 85 cents to the greenback. Look to 90 cents for resistance while, seeing as we can’t argue with a central bank, 85 cents will offer support.

As for the bond market, yields were essentially unchanged to start the day yesterday while the curve didn't move much ahead of the 30-year bond auction. But that changed when the auction turned out to be surprisingly strong after lackluster three- and 10-year note auctions earlier in the week. The better-than-expected auction sent both the 10s and 30s to intraday highs. The bid to cover was a solid 2.57, up from just 2.35 at the December auction, indicating higher-than-average demand. The “yield awarded” was a full basis point higher than the “bid at the auction deadline,” showing solid demand based on the yield as well. It is worth noting that ECB president Draghi’s “dovish” commentary helped to lift German Bund prices. This in turn helped U.S. Treasuries to bounce off the morning lows.

Remember to look to the bonds for the best read on the jobs report this morning, as they are now the best “Fed indicating asset,” taking over the honor from gold.

Have a good weekend,

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 opened 2014 with a thud, but that was more positioning than anything else. Skeptical sentiment towards the rally and a strengthening economy remain tailwinds on the market, and as long as the short end of the yield curve remains anchored, the path of least resistance remains higher.*

Trade Ideas

Long Japan: **The yen has broken through 104 yen/dollar level, and DXJ is at multi-month highs. Although we could see a pause, that trend should continue over the coming months, and there remains more money in this trade.**

Long Deep, multi-national Cyclicals and Global Miners: **Domestically, I'd look to allocate to deep cyclicals like industrials (XLI), basic materials (IYM) and global industrial miners (PICK). It's a bit of a contrarian idea, and over the past few weeks these sectors have lagged. But, they most exposed to the "global economic recovery" thesis.**

Long Natural Gas E&Ps: **Term structure in the natural gas markets has turned bullish, as its in backwardation out nearly a year, implying a structural increase in demand. But, natural gas equities remain under pressure, and could potentially offer some value in the market over the medium/longer term. FCG and XOP are the two "pure play" ETFs in the natural gas E&P space.**

Commodities	**Bullish**	**Neutral**	**Neutral**	*The outlook for commodities remains mixed, as the global economy remains mired in stagnant growth. Given the severe underperformance of commodities this year, though, the asset class remains on of the last corners of value in the market, if the global recovery can accelerate.*

Trade Ideas

Long Industrial Commodities: **Industrial commodities have stalled lately, as economic data, especially in the US, has shown a loss of some positive momentum, and it bears close watching as to whether this is a temporary blip, or a bearish game changer. But, if you believe the global economy Is recovering, the commodity space, and the ETF DBC, is one of the best "values" in the market, and a pretty contrarian idea right now.**

Long Gold: **I'm dipping back into the well here with the gold trade. The near term outlook is mixed to negative, but medium term I think $1200 represents a fair risk/reward set up on an acceleration of inflation. I would initiate a small long position around the $1200 level with a stop at the old lows ($1179).**

U.S. Dollar	**Neutral**	**Neutral**	**Neutral**	*The Dollar Index rallied last week, but mostly thanks to a weak euro. The Dollar Index should remain largely range bound, as a stubbornly strong euro caps any material upside.*

Trade Ideas

Short: **Japanese Yen. The yen has been supported mostly by extreme dollar weakness, and with tapering expectations being pulled forward, the yen should resume its decline vs. the dollar. YCS remains the best non-futures way to play the trade.**

Treasuries	**Bearish**	**Bearish**	**Bearish**	*With the Fed tapering QE and shift to "forward guidance" as the main policy tool, the case for the bond bears has gotten stronger. Continue to short any rallies in the bond market.*

Trade Ideas

Buy: **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.**