7:00's Report

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

January 29th, 2014

Pre 7:00 Look

- Futures are slightly negative ahead of the Fed, despite a strong global rally thanks to the Turkish Central Bank.
- The Turkish Central Bank took bold action to defend its currency, raising interest rates 425 basis points vs. (E) 200 basis points. The move sparked a "risk on" rally globally.
- Economic data o/n was light, with UK Home Price Index meeting expectations.
- Econ Today: FOMC Meeting Announcement (2:00 PM)
- Earnings Today: BA (E: 1.59), DOW (E: .43), FB (E: .28), QCOM (E: 1.18).

Market	Level	Change	% Change
S&P 500 Futures	1789.00	.75	0.04%
U.S. Dollar (DXY)	80.65	-.007	-0.01%
Gold	1256.70	6.20	0.50%
WTI	97.05	-.36	-0.37%
10 Year	2.746	-.020	-0.72%

Equities

Market Recap

Stocks rallied Tuesday for the first time in nearly a week thanks to emerging market serenity and strong earnings. The S&P 500 rose 0.69%.

Stocks opened slightly higher thanks mostly to earnings (DD, PFE, DHI, CMCSA all bullish) and shrugged off the soft durable goods report once the Street discovered the report wasn't all that bad. Shortly after the open, sellers tried to push the market lower but failed to turn the S&P 500 negative. Once the selling dried up, stocks began a

Mexico: An emerging market baby out with the bath water? Things in Mexico are improving, but the Mexico ETF has gotten dragged down by emerging market angst, and it is now at multi year support.

methodical rally higher that lasted into the last hour of trading. News-wise things were quiet during the afternoon session, and the market approached session highs before selling off a touch into the close.

Trading Color

Despite the rally in equities, there was no conviction to the move. And, although the emerging markets having a calm day was nice, this was little more than an oversold bounce and trader positioning ahead of the FOMC. Yesterday's price action did not imply this decline is definitively over, as the "reasons" for the rally were more excuses to explain an oversold bounce.

Market-wise, cyclicals bounced back as we saw the Transports in the Dow and R2K outperform the S&P but not by a huge amount, which implies we didn't see investors materially adding risk to their portfolios yesterday. And, that would make sense ahead of the FOMC meeting announcement this afternoon.

Sector-wise, we saw a bit of a reversal of the last two days as cyclicals and other recent outperforming sectors

Market	Level	Change	% Change
Dow	15,928.56	90.68	0.57%
TSX	13,696.66	114.37	0.84%
Brazil	47,840.93	139.88	0.29%
FTSE	6,589.43	17.10	0.26%
Nikkei	15,383.91	403.75	2.70%
Hang Seng	22,141.61	180.97	0.82%
ASX	5,229.01	53.90	1.04%
Prices taken at previous day market close.			

rallied the most. Financials, biotechs, homebuilders and industrials all rallied close to, or more than, 1%. Defensives lagged but still mostly finished in the green. Meanwhile tech, which was weighed down by AAPL, underperformed and was the only major sub-sector to finish lower.

On the charts, the 1,775-1,785 support level appears to have held for now, while 1,800 is the first level of resistance.

Market	Level	Change	% Change
DBC	25.03	.12	0.48%
Gold	1251.20	-12.30	-0.97%
Silver	19.525	-.268	-1.35%
Copper	3.2525	-.0065	-0.20%
WTI	97.38	1.66	1.73%
Brent	107.45	.76	0.71%
Nat Gas	5.038	.191	3.94%
RBOB	2.6333	.0116	0.44%
DBA (Grains)	24.32	.04	0.17%
Prices taken at previous day market close.			

Concerns Shifting From the EMs to Economic Growth

Yesterday's durable goods miss is now the fourth "major" data point in a row to miss expectations. And, while the durable goods report wasn't horrible, the consistency of the misses is starting to make people a bit nervous about the pace of the recovery. The moving target of market concern is shifting from the emerging markets to domestic growth.

Since the start of January, the jobs report, auto sales, flash manufacturing PMI and now durable goods have all missed estimates. Taken in the context of a Fed that seems intent on further tapering QE, that represents a potential "nightmare" scenario for equity investors of a Fed tapering into a slowing economy.

But, the pace of economic growth was widely expected to slow in December, for no other reason than November economic data was very, very strong, and some moderation is to be expected. And, importantly there are no signs, yet, that the loss of economic momentum is anything other than that.

But, as always the market is focused on the rate of change, not the absolute data. For those investors still looking to re-position or de-risk, every economic data point that misses estimates will be an excuse to sell more.

Bottom line is from a "real economy" standpoint, there's nothing alarming in the economic data. But, don't be surprised if, once emerging markets calm down, the focus of market angst turns quickly to the lackluster economic data. And, until we get a couple of "beats," stocks may have a hard time rallying.

Economics

Durable Goods Orders

- December New Orders fell 4.3% vs. (E) 1.6%
- December NDCGXA rose 0.21% vs. 0.27% in November

Takeaway

Durable goods joined the growing chorus of economic data points to miss expectations, although the report wasn't as bad as the headline. With durable goods in particular, you can generally ignore the headline as it's massively influenced by airplane orders, and that was again the case this month.

Instead, the key number to watch is new orders for Non-Defense Capital Goods Ex-Aircraft (NDCGXA). That also declined in December (down 1.3%) and the November reading was revised lower from 4.1% to 2.6%. So, certainly this report reflected more-subdued capital expenditures by business in December, but more important than the single data point was the fact that the three-month rolling average of new orders for NDCGXA continued to move higher, rising 0.21% to a six month high. So, like most recent data, December saw slower-than-expected activity, but overall the trends remain positive.

Stocks initially dropped sharply on the headline miss, but shortly thereafter stabilized and largely ignored the "weak" report for the remainder of the trading day as stocks hit their highs later that afternoon. The durable goods report should have no effect on the Fed meeting today or their anticipated schedule of tapering QE.

FOMC Preview (Repeat from yesterday).

I put this preview in yesterday's Report but given the meeting is today thought it would be useful to include again.

The broad consensus expectation is for:

- Another taper of $10 billion per month, reducing the

QE program to $65 billion/month.

- Like in December, the taper will be split evenly between Treasuries and MBS (Mortgage-Backed Securities).

With regard to "Forward Guidance," expect the Fed to again emphasize its ZIRP (zero interest rate policy) but specifically look for the Fed to focus more on the risk of low inflation, and downplay the 6.5% unemployment rate threshold. That will most likely be the way the Fed tries to make the statement "dovish."

Finally I've heard some chatter that the weak December jobs report or the recent turmoil in the emerging markets may cause the Fed to "taper" the taper. At the risk of making myself look foolish, that has almost zero chance of happening. It would be a huge (and upsetting) shock to the system, as the Fed will have confused everyone just like they did in September .

Bottom line is this meeting has been pretty well-telegraphed, so unless there's a huge surprise it could wind up being a non-event.

Commodities

The commodities space was mixed yesterday and although there was some volatility in the market the entire sector was moving on technicals as there was no new fundamental news in the markets yesterday. The PowerShares DB Commodity Index Tracking Fund (DBC) increased 0.48%.

Natural gas was the largest outperformer yesterday, rallying more than 5% in early trading and closing with a 3.94% gain on the day. But, the move was deceiving and nothing more than a bounce in a currently range-bound market. The recent volatility and resulting big swings in the market have been largely a result of higher volumes due to more spec traders taking positions, looking to make a quick buck on the large moves in the market.

Market	Level	Change	% Change
Dollar Index	80.655	.043	0.05%
EUR/USD	1.3668	-.001	-0.01%
GBP/USD	1.658	-.0004	-0.02%
USD/JPY	102.90	.36	0.35%
USD/CAD	1.1152	.0039	0.35%
AUD/USD	.8773	.0038	0.44%
USD/BRL	2.4258	.0053	0.22%
10 Year Yield	2.746	-.020	-0.72%
30 Year Yield	3.672	-.008	-0.22%
Prices taken at previous day market close.			

Natural gas trading is largely dominated by weather forecasts and technical trading as it continues to consolidate and digest the recent, substantial rally. On the charts, support lies at the $4.70-ish level while light resistance has developed on the chart just above $5.10.

Precious metals were the worst-performing commodity yesterday as the trend of trading inversely to the stock market continues. Gold and silver fell 0.97% and 1.35%, respectively, as the S&P added 10 handles on the day.

As I said on CNBC Monday evening, stocks are currently "driving the precious metals bus." But that will likely change if there are any surprises out of the FOMC announcement or we see overly dovish/hawkish chatter or rumors out of the Fed.

Gold did hold support at the $1,250 level but that's not enough for the bulls to celebrate as the futures price has been drifting lower the past few sessions. For now, $1,250 can be considered the first level of support, but I wouldn't be surprised to see that level violated especially if the Fed does something very unexpected.

Crude oil caught a decent bid yesterday, moving higher by 1.73%. However, the move in WTI was like the moves in the other commodity markets I have discussed in that it was unimpressive. Crude began to rally right out of the gate, but then the buyers lost their momentum and became exhausted before they were able to send the price above last week's highs. There is also a new downtrend line being tested, which is offering additional resistance. Crude remains largely range-bound here between $98 and $92 per barrel. The EIA will report weekly inventory data tomorrow with estimates for crude oil inventory to rise by 2.2 million barrels and RBOB gasoline inventory to rise by 1.1 million barrels, while distillates are expected to fall by 2.6 million barrels.

Currencies & Bonds

Emerging markets calmed down yesterday as two central banks moved to defend their currencies while the political situation in the Ukraine improved. First, the Turkish central bank held its emergency meeting and moved decisively to strengthen the lira by raising interest rates 425 basis points, much more than the 200 basis point increase that was expected.

The move helped ignite a huge rally in the Lira (it had the biggest single day increase in 5 years) and in global stock markets. The move by the Turkish central bank is helping to stem the tide of emerging market concern, although it's too early to say this latest iteration of an emerging market "crisis" is over. Focus now shifts to the Central Bank of South Africa is expected to make a rate announcement (although it's not clear what policy steps they will take). The rand was under pressure ahead of the meeting later today and the market will be watching to see if the South African CB "defends" the rand the way the Turkish central bank "defended" the lira (if they take no action, that likely won't be well received by risk assets).

The Reserve Bank of India also moved to help strengthen the rupee by somewhat surprisingly raising interest rates 25 basis points (the move wasn't a total shock). Also, the Ukrainian prime minister stepped down, which was one of the core demands of the protestors, and that is helping to cautiously raise hope that the situation there will finally start to settle down.

Finally, things remained quiet in Argentina, where the peso was off fractionally vs. the greenback. As a result of this positive news, CEW, the best ETF to measure emerging market currencies, rose 0.3%.

Emerging markets remain one of the three areas of potential concern for the market (Chinese economic growth, emerging market stresses, and potential slowing growth domestically). While EM issues are far from resolved, the fact that we are seeing central banks start to act decisively is encouraging.

At its core, the emerging markets are only a problem if we start to see contagion among them, which heretofore we have not. And, the steps taken by the Turkish central bank will help further reduce the chance of contagion, so that is a positive. But "emerging market forex contagion" remains a buzz phrase to watch for. If you start to see that a lot in what you're reading or hearing, then my opinion on these emerging market issues will change from "not as bad as advertised" to a "bearish game-changer." For now, though, we seem to be in the clear.

Turning to the developed market currencies, things were quiet ahead of the FOMC meeting, as the Dollar Index was unchanged, the euro was flat on no real news, and the pound was also unchanged as Q4 '12 UK GDP largely met expectations. Even the yen was flat (down 0.14%) ahead of the FOMC.

Turning to bonds, Treasuries caught a bid yesterday (both the 10- and 30-year gained 0.2%) thanks to some light short-covering ahead of the FOMC later today. Also helping in the rally was the Fed buying $3 billion worth of 8-10 year notes at 11 a.m. yesterday. Obviously all eyes in the domestic bond market are on the Fed meeting today, so it makes sense that bonds, like the U.S. dollar, were little-changed. With an additional $10 billion taper of QE already priced into bonds at these levels, looks for the FOMC statement to be the major influence over the bond market today.

On the fundamental side of things, there was a 2-year Treasury bill auction that surprisingly wasn't very well-received. The bid to cover (a measure of demand) was 3.30, down from 3.77 in December. Although that reflects just one auction, we are seeing more signs that bond investors are starting to act like we are indeed in a new reality of falling bond prices and rising yields. The yield on this 2-year offering was lower compared to the auction in December. If I were a bond PM, I'd be content to wait out this auction given that it's much more likely I'll be able to buy higher-yielding paper in a month or two.

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	*The market got hit last week on concerns about Chinese growth and emerging markets, and stocks suffered their worst weekly declines in over a year. But, the positive fundamental back drop remains largely in place, and so far none of the events of last week are bearish "game changers."* *Important support sits at the 1780ish range, while 1812 (the 50 day MA) is resistance.*

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: **Gold is now threatening to break out of a months long downtrend, but given gold has rallied as a "crisis" hedge, I'm skeptical the move can last. A few more closes above the $1260 level would make me more bullish in the short term.**

U.S. Dollar	Neutral	Neutral	Neutral	*The Dollar Index largely range bound as the market has priced in Fed tapering, while the question of what, if anything, the ECB will do to combat rising dis-inflation remains unanswered.*

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, including the one we are seeing now thanks to emerging market concerns.*

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.**