7:00's Report

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

March 10th, 2014

Pre 7:00 Look

- Futures are flat this morning after a mixed performance internationally that saw Asia trade lower while Europe is slightly higher.
- Asian stocks are lower because of data: Chinese trade balance badly missed expectations (although not as bad as it seems) while Japanese Q4 GDP was revised lower to 0.7% vs.1.0%.
- Geo-politically tensions are rising again in Ukraine as Russia is taking a hard line, but broadly the situation is stable.
- Econ Today: No reports. Fed Speak: Evans (12:40 PM).

Market	Level	Change	% Change
S&P 500 Futures	1877.00	-1.00	-0.05%
U.S. Dollar (DXY)	79.755	.033	0.04%
Gold	1336.10	-2.10	-0.16%
WTI	101.44	-1.14	-1.11%
10-year	2.789	-.001	-0.03%

Equities

Market Recap

Stocks traded to new all-time highs again last week thanks to de-escalation in the Ukrainian crisis, decent economic data, and investor positioning (as underinvested fund managers chased stocks higher). The S&P 500 rose 1% last week and is up 1.61% year-to-date.

Stocks were lower Monday mostly on Ukraine angst, but the declines were quickly undone Tuesday as the situation de-escalated. Markets "squeezed" higher to new all-time highs, as the S&P 500 finally and decisively broke through that 1,850 resistance area.

Stocks drifted Wednesday ahead of the two major catalysts for the week (ECB interest-rate decision and U.S. jobs report), before rallying Thursday despite the ECB remaining on hold and the ISM non-manufacturing PMI badly missing expectations. Stocks went into the jobs report basically on the all-time highs, but despite the beat from the jobs report, we saw a "sell the news" reaction. Stocks finished trading Friday almost perfectly flat on the day, but again up 1% on the week.

Trading Color: Sentiment and Positioning were the true drivers of last week's rally

The economic data and Ukraine de-escalation were positives, but last week's rally had a "squeezy" feel to it, as underinvested managers—again caught by surprise at the strength of the market—reluctantly added exposure to get "more long."

There were two "tells" that served as the main forces behind the rally. First, there was much more activity and buying in ETFs and index futures than in single stocks (a sign investors are just looking to "throw on" broad long exposure). Second, Tuesday especially felt "squeezy" as each leg higher in stocks seemed to elicit another flurry of buy orders.

The reason I point this out is because, as I said Friday, these types of "squeezy" rallies usually don't have a lot of legs. We may see a pause in the market in the short term, as there are now a lot of "late and weak" longs in the market, and they tend to violently de-risk at the first sign of trouble.

Another sign we may see a pause in this rally came from market internals. Late in the week we saw healthcare, which has been one of the big market leaders so far in 2014, put in a bearish "outside reversal." Meanwhile,

Market	Level	Change	% Change
Dow	16452.72	30.83	0.19%
TSX	14299.08	27.16	0.19%
Brazil	46244.07	-849.06	-1.80%
FTSE	6,736.32	23.65	0.35%
Nikkei	15,120.14	-153.93	-1.01%
Hang Seng	22,264.93	-395.56	-1.75%
ASX	5,411.52	-50.79	-0.93%
Prices taken at previous day market close.			

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cyclical indices like the Russell 2000 and Nasdaq both lagged Thursday and Friday thanks to weakness in biotech, cloud computing and semiconductors.

Again, that anecdotally implies we may be seeing some money rotate out of the "high flyers" and either go to cash, or be reinvested into underperforming sectors (like banks, which rallied 0.8% Friday and played "catch up" big time last week thanks to the increase in Treasury yields).

Market	Level	Change	% Change
DBC	26.29	-.12	-.45%
Gold	1339.50	-12.30	-.91%
Silver	20.89	-.69	-3.19%
Copper	3.08	-.13	-4.15%
WTI	102.69	1.13	1.11%
Brent	108.23	-.77	-0.71%
Nat Gas	4.63	-.04	-.77%
RBOB	2.950	-.0238	-0.80
DBA (Grains)	28.38	.06	.21%
Prices taken at previous day market close.			

On the charts you know the drill: Resistance in the S&P 500 is at all-time highs at 1,883.57, while support lies lower at 1,867, 1,850 and then the 50-day MA at 1,826.

This Week

Ukraine and the Chinese economic data Thursday will be in focus this week. The Ukrainian situation remains fluid, with the Crimean vote to join Russia looming this coming Sunday. In China we get the latest round of economic data Thursday.

On the micro front it's pretty quiet except for a few retail earnings (URBN, DKS, DG) throughout the week.

Overall if the Ukrainian situation doesn't devolve and the China data isn't awful, it should be a pretty quiet week from a catalyst standpoint.

Bottom Line

The macroeconomic backdrop remains supportive of stocks prices generally although, as you can guess, I think this market may have gotten a bit ahead of itself. A correction or consolidation may be in order in the short term. So I wouldn't be adding blanket long exposure to stocks at these levels.

Instead, I'd continue the drill: Look to allocate to sectors of the market that have underperformed and at least offer some relative "value." Banks (via KBE) retail (via RTH) global miners (via PICK) and industrials (DIA) seem more attractive.

Additionally, I think the "bond short" trade is back in gear, and as I've been saying, TBT and TBF are still attractive at these levels. But don't forget the offshoots of the "high rate" trade: Banks are the primary beneficiaries, while utilities and REITs lag—so if you've got some nice year-to-date profits in those sectors, consider booking them.

Economics

Last Week

Economic data last week broadly met or exceeded expectations, and 1) Solidified that the global economic recovery is ongoing, 2)Strongly implied the economic weakness in the U.S. in Dec/Jan is temporary, and 3)Ensured the Fed will continue to taper the QE program by another $10 billion at the March meeting a week from Wednesday.

From a practical investment standpoint, the last week's data reinforces that the global economic backdrop remains a general tailwind on equities, although there certainly are risks to monitor.

Starting with the jobs number, we all know by now that it was a surprisingly strong report, at 175K jobs added in Feb. vs (E) of 150K and "whisper numbers" of around 130K-ish. And, in addition to the positive February data, there were positive revisions of 37K jobs added in December and January (11K and 26K, respectively).

Looking a bit deeper into the number, while the headline was a strong beat, the details of the jobs number weren't quite as good. Specifically, critics are pointing to the fact that the average workweek fell from 34.3 to 34.2 hours, missing estimates and falling for the second-straight month. That's somewhat important because the average workweek is a leading indicator for employment. (As employers get busier, they work their current employees more before hiring additional staff, so an uptick in average workweek usually precedes increased hiring.)

I'll let the economists debate the minutiae and validity of the report, but the bottom line from a market standpoint is this: The jobs report was a positive because the weakness in hiring in December and January stopped

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and the "weather excuse" appears more valid, and, combined with other data, it shows the slowdown in the U.S. economy so far this year isn't gaining momentum and appears, for now, to be temporary.

The other big reports out last week were the ISM manufacturing and non-manufacturing (services) PMIs. And, the results were, on balance, positive.

ISM manufacturing rebounded from that big drop in January, bouncing to 53.2 vs (E) 51.9. ISM non-manufacturing, though, dropped to 51.9 vs. (E) 53.5, and the employment sub-index fell to 47.5, the first sub-50 reading for that number in over two years, although that sub-index was obviously overshadowed by the government report.

Internationally, data was also supportive. China remains the No. 1 "macroeconomic" risk to the global recovery, but last week the data largely met expectations and, while the Chinese economy is slowing, so far it appears to be slowing about as everyone expected (which is "OK" as that won't de-rail the global recovery).

Indeed, much to the despair of the China bears, China remains a crisis that hasn't materialized. Manufacturing and composite PMIs met expectations and importantly stayed above the 50 level. And, although there was a disappointing trade balance report out Friday night (exports plunged), a lot of that was because exports were "pulled forward" by the Chinese New Year, so that soft data point will get a "pass" of sorts.

Europe was actually the area with the best data last week, as manufacturing and composite PMIs beat, as did EU retail sales. This in part led the ECB to make no changes to policy, and to strongly imply that the ECB was "on hold" for the foreseeable future (which is very positive for European bonds, and I continue to think PIIGS' bonds remain some of the most-attractive options in the bond markets today.)

Bottom line is that, while you can argue that the economic data last week had its gives and takes (there are legitimate points for the bears to remain bearish), it did help positively resolve the question of "is the global and domestic recovery faltering?") with a pretty definitive "no."

Bottom line from last week is this: Economic data remains broadly supportive of stock prices, and if this rally is going to break in the near future, it won't be because of economic growth concerns.

This Week

After an exhausting week of data last week, we all get a rest this week. The calendar is very light domestically, with retail sales and jobless claims (both Thursday) the only reports to watch.

Internationally it's almost equally quiet, although we do get some Chinese data Thursday morning (industrial production and retail sales). Given the ongoing concern about China, the data will be watched, but even if it "misses" I don't think it'll materially change people's outlook on China. (The expectation remains for between 7.0% and 7.5% GDP growth.)

Commodities

Commodities were strong early last week but almost universally faded Wednesday-Friday on a combination of warmer weather, inventory data and better than expected economic reports. The commodity ETF DBC hit a seven month high last Monday but consolidated those gains for the rest of the week and ended up just .6%.

Starting with the metals, gold rallied to a four month high mid-week, breaking temporarily above $1350 in anticipation of a soft jobs number and, potentially, a pause in Fed tapering of QE. But, obviously the jobs number was stronger than expected, and gold traded down 1% to close up just .7% on the week.

Market	Level	Change	% Change
Dollar Index	79.79	.068	0.09%
EUR/USD	1.387	-.0006	-0.04%
GBP/USD	1.6656	-.0055	-0.33%
USD/JPY	103.33	.08	0.08%
USD/CAD	1.1109	.0028	0.25%
AUD/USD	.9033	-.0038	-0.41%
USD/BRL	2.3452	.0049	0.21%
10-year Yield	2.789	-.001	-0.03%
30-year Yield	3.725	.003	0.08%
Prices taken at previous day market close.			

If you don't own any gold or GLD and are looking to get something on, these levels are "ok," although as I've been saying for a while, I prefer to buy a further dip in gold, and that opinion still stands. I think

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we'll see more weakness over the next few days, although the Ukrainian situation remains a wild card.

Staying in the metals, copper absolutely imploded Friday and that selling is continuing this morning, thanks to the weak Chinese trade balance numbers and the violation of major support at 3.15. Clearly my "long copper" trade was stopped out on Friday as copper traded within a penny of the 52 week lows below $3.00 early this morning. What this copper wash out means for the global economy is unclear, but it's something that needs to be watched, as I don't like it when copper simply goes into free fall for no specific supply/demand related reason.

Turning to energy, it was a largely ineffectual week despite some volatility. Natural gas traded flat on the week despite some gyrations, but the fundamental situation there remains firmly bullish (natural gas inventories are now nearly 40% below the 5 year average).

WTI Crude Oil temporarily broke through $105/bbl. late Monday on Ukraine concerns, but then traded lower mid-week thanks to bearish weekly inventory data, especially in heating oil. Low inventories of heating oil, courtesy of the cold winter, have put a bid under the entire energy complex for 2+ months, and with that situation starting to change (heating oil inventories are building, meaning less refining demand for WTI Crude), that will act as a headwind for WTI, which remains range bound between 100.08 (the200 day MA) and $105ish.

Commodities have enjoyed a strong rally so far in 2014 thanks mainly to the weather and geo-politics (Ukraine). Both appear to be calming down, which could put a temporary headwind on the asset class, so I'd look to be a buyer of broad commodities (something like DBC) after a bit of a correction.

Currencies & Bonds

The Dollar Index declined marginally last week despite the better than expected jobs report, as a very strong euro weighed on the index. The euro surged late last week to a two and a half year high above 1.39 vs. the dollar after the ECB made no changes to policy at their rate meeting Thursday, signaled they had little intention to ease further in the future, and sounded surprisingly upbeat about the EU economy. Clearly the ECB isn't as worried about dis-inflation as the market is, and the fact that they are "on hold" from a policy standpoint remains de-facto bullish for the euro and enthusiastically bullish for higher yielding European government debt (PIIGS bonds especially).

Despite the tailwind from the ECB, though, I still don't expect we're going to see a period of protracted euro strength and Dollar Index weakness, because the Fed seems as intent on "tapering" QE as the ECB is on doing nothing, and I'd expect both currencies to remain broadly range bound versus each other around current levels.

Turning to the yen, it declined modestly versus the dollar last week, trading back through and above 102 yen/dollar on a reduction of the Ukrainian based "risk off" bid of the last two weeks, and on growing expectation that the BOJ will indeed ease policy further in the coming months, as the national sales tax is implemented in April. The long Japanese stocks/short yen trade has been somewhat forgotten this year, partly because it's underperformed (Japanese stocks are down close to 7% year to date and the yen is slightly stronger). But, the fundamentals remain supportive, and I continue to think the BOJ eases again this spring, and the "long DXJ/short yen" trade will come back "on" and that these levels represent attractive entry points if you can stomach the volatility.

In the bond market, the 30 year Treasury dropped to a two month low last week courtesy of the stronger data and the realization by the bond market that, as Fed Vice Chair Dudley said last week, the bar to pause tapering of QE is "pretty high." The ten year yield traded through 2.80% on Friday for the first time since early January, and it looks as though this multi-month counter trend rally in the bond market has indeed come to an end, and the primary downtrend in the Treasury market has resumed once again (although longer term these are still good levels to get "short" bonds via TBT or TBF). Given where stocks are in the shorter term, I continue to think the "short bond" trade is the most fundamentally sound idea in the market right now.

Have a good week,

Tom

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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	Bullish	Bullish	Bullish	*The S&P 500 traded to a new all time high last week, although the gains came on low volumes and with little conviction. But, the broadly speaking the positive backdrop for stocks (macro-economic calm, accommodative central banks, growing economic recovery, skeptical sentiment) remains, so the benefit of the doubt remains with the bulls.* *Resistance is now the all time highs at 1876, while support is the 50 day MA at 1820.*

Trade Ideas

Long Market "Laggards": **So far in 2014 the right strategy has been to buy beaten down sectors that offer some value, as opposed to the broad market. It has worked with utilities and most recently the retailers. Now, the banks seem to be the sector that has lagged recently, and if the market continues to rally, we should see them play catch up. KBE remains one of the "easiest" ways to get broad bank exposure. I'd also look to allocate to deep cyclicals like industrials (DIA), basic materials (IYM) and global industrial miners (PICK).**

Long Japan: **DXJ has gotten hit hard as the yen has rallied, due mostly to emerging market angst. But, the Japanese economy is improving, and seeing as I don't think this latest EM angst is a bearish game changer, I believe the yen will resume its declines and DXJ is not done rallying.**

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.**

	Fundamental Outlook	Technical Outlook	Overall	Comments
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 last 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 Gold: **Gold has now broken out above resistance at $1300/oz., as gold has benefitted from the recent dollar weakness due to soft economic data. Short term I'd only nibble around the mid-$1300's and would prefer to buy more towards $1300/oz. But, short term timing aside, it appears as though a longer term bottom is "in" in gold.**

	Fundamental Outlook	Technical Outlook	Overall	Comments
U.S. Dollar	Neutral	Neutral	Neutral	*The Dollar Index remains largely range bound, as a stronger euro will hamper any ability for the US Dollar Index to rally, despite continued tapering of QE.*

Trade Ideas

Short: Japanese Yen. **This year has been choppy for the yen as there have been several macro-inspired "risk off" episodes, most recently with the Ukraine. But, with the BOJ expected to ease policy further, fundamentals for a weaker yen remains in place, and I would view this rally as a longer term entry point in a still down trending yen.**

Short: Aussie Dollar. **Aussie saw a big short covering rally last week on better than expected data, but with risks to Chinese growth skewed to the downside and the Reserve Bank of Australia wanting a weaker Aussie, the trend remains lower. For those non-futures traders, shorting FXA or buying CROC is the easiest way to put this trade "on."**

	Fundamental Outlook	Technical Outlook	Overall	Comments
Treasuries	Bearish	Bearish	Bearish	*Economic data has turned a bit more positive and it appears as though the counter trend rally in the bond market is ending. The primary trend remains lower, as the Fed seems intent on further "tapering" of QE.*

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.**

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