7:00's Report

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

March 26th, 2014

Pre 7:00 Look

- U.S. Futures are slightly higher as are most international markets after a relatively quiet night of news.
- Both Asian and European stocks rallied overnight, following the U.S. higher and on chatter of possible economic stimulus in both China and Europe.
- In Europe, Italy released two economic reports and the results were mixed. Retail Sales missed (0.0% vs. E: 0.1%), but Consumer Confidence beat expectations (101.7 vs. E: 98.1)
- Econ Today: Durable Goods Orders (E: 1.0%)

Market	Level	Change	% Change
S&P 500 Futures	1863.50	4.25	0.23%
U.S. Dollar (DXY)	80.22	.132	0.16%
Gold	1315.10	3.70	0.28%
WTI	99.33	.14	0.14%
10-year	2.735	.002	0.07%

Equities

Market Recap

Stocks bounced back Tuesday and recouped most of Monday's losses, helped by stabilization in the "momentum" sectors that sold off so hard Monday (and really for the past 2+ weeks). The S&P 500 rose 0.44%.

Stocks sprinted higher right after the open on a combination of chatter regarding Chinese stimulus and "dovish" Fed-speak by Philly Fed President Charles Plosser (he said the Fed didn't change policy last week) and by Bundesbank President Jens Weidmann (he said QE in Europe was a possibility).

But, the strength didn't last very long. Stocks slowly started to bleed lower 45 minutes after the open, as the short-covering rally in the "momentum" sectors evaporated. The S&P was flat by lunchtime, before buyers once again stepped up. The market rallied for the next hour before spending the afternoon in a tight range. Stocks closed basically dead in the middle of the daily range.

Trading Color

It seems as though we are seeing a bit of a rotation at the moment, more so than anything else in this market. Growth and "high beta" again underperformed yesterday (Russell 2000 was actually fractionally lower, while the Nasdaq, QNET (Internet index) and NBI (biotechs) all lagged and finished near flat) while value and "low beta" continues to relatively outperform.

Sector-wise, the rotation was evident yesterday: Consumer staples, REITs, healthcare and energy all rallied close to 1% while banks and consumer discretionary were the only two sectors to finish the day lower. But, this rotation was very evident in tech, thanks to the massive recent underperformance of the "growth" tech sectors like cloud computing, mobile and Internet, and the recent outperformance of "value" super-cap tech names: MSFT, CSCO, AAPL, INTC and IBM, all of which have seen strong rallies over the past several days despite the stagnant market.

A New York State Of Mind

I'm traveling to NYC today through the end of the week for meetings with clients and colleagues, and this afternoon I'll be back on the floor of the NYSE for the first time since I left nearly a decade ago. Sadly, though, I won't be able to see my old post (Post 9) as it is now a CNBC set! Bittersweet, indeed.

Market	Level	Change	% Change
Dow	16,367.88	91.19	0.56%
TSX	14,299.49	20.94	0.15%
Brazil	48,180.14	186.72	0.39%
FTSE	6,641.83	36.94	0.56%
Nikkei	14,477.16	53.97	0.37%
Hang Seng	21,887.75	155.43	0.72%
ASX	5,376.75	40.13	0.75%

Prices taken at previous day market close.

What this rotation means for the broader market is unclear at this point – it very well could be a defensive move ahead of earnings season or an unintended consequence of forecasted higher interest rates negatively affecting the ultra-growth stock valuation. But, it is a trend that bears watching as it appears to be gaining steam (especially in tech).

Market	Level	Change	% Change
DBC	25.92	.17	0.66%
Gold	1311.80	.60	0.05%
Silver	19.985	-.082	-0.41%
Copper	2.993	.0475	1.61%
WTI	99.19	-.41	-0.41%
Brent	106.89	.10	0.09%
Nat Gas	4.414	.138	3.23%
RBOB	2.885	-.0059	-0.20%
DBA (Grains)	28.06	.02	0.07%
Prices taken at previous day market close.			

The other notable sector movement yesterday came from basic materials and global miners, as anything "China related" continues to bounce back on hopes of more stimulus from the PBOC or the Chinese government itself.

Volumes were light again yesterday and below Monday's levels, and the trend of low-volume rallies continues (although again, that's been with us for a while and it hasn't meant anything negative yet).

More broadly, though, the S&P 500 remains in the middle of the 1,850-1,880 range it's been in for 4+ weeks now. Until we break decisively out of that range, a lot of these small daily gyrations are little more than trading "noise."

Economics

There were several reports on the different components of the housing market yesterday, including the FHFA House Price Index, the S&P Case-Shiller Home Price Index and the one most closely watched by the markets, New Home Sales. The results of all were relatively in-line with expectations, but there were a few key takeaways worth mentioning.

New Home Sales data were the most widely watched yesterday, and the results were exactly in-line with analyst expectations. Sales fell to 440K in February from a January number that was revised lower to 455K from 468K. The slight slowdown in new home sales helped the historically low supply levels build marginally to 5.2 months vs. 5.0 months in January (the low number of houses for sale has inflated prices and generally restricted sales so the slight increase in inventories should be considered a good thing for now).

Bottom line is that the housing market remains an area of concern in the greater economic recovery. Housing simply isn't bouncing back the way everything else in the economy has. And, based on yesterday's housing data, it didn't bounce back in February either. For now it is not a problem, but it is certainly something we need to keep a close eye on.

Commodities

Commodities markets were rather quiet yesterday, with only copper and natural gas moving more than 1% (both of those moves were to the upside). Thanks to the outperformance in both copper and natural gas, DBC rallied 0.62% on the day.

Beginning with the metals, copper futures rallied 1.8% as they broke to 2-week highs and reclaimed the important psychological $3.00 level we mentioned in yesterday's Report. Copper rallied thanks to speculation that the Chinese government will move to provide some sort of further economic stimulus, as well as on news of violent protests at a Chilean copper mine owned by Anglo American PLC. The protest disrupted local operations, which in turn sparked some supply fears in yesterday's trading session, but the situation seems to be under control and business is set to resume as normal today. Bottom line is that copper continues to stabilize and regain some of the lost ground from earlier in the month, but we will need to see a few more closes above the $3 mark to really confirm the move has some conviction.

Elsewhere in the metals, gold futures dipped to a new 6-week low at $1,306 shortly after the open, but buyers quickly stepped in and futures traded comfortably higher for the remainder of the session. This tells me two things:

- First, gold doesn't seem finished with testing support at the $1,300 level.
- Second, there are plenty of buyers looking to get into the market around $1,300/oz .

So that, paired with the risk/reward setup (risk $10 for

$65+), further supports the thesis of buying gold at these levels **with a stop at that $1,300 level**.

The best way to get long is either through futures contracts, or the well-known gold ETF, GLD, as well as GDX, the gold miners ETF (who will clearly benefit with the rising price of gold).

Moving to energy, natural gas prices rallied 3.2% yesterday after falling 3 sessions in a row. The jump in futures was due to the late-season snowstorm that is set to hit the Northeast today. The story in the nat gas market is essentially the same as it has been for a couple weeks, though (i.e., pressured supply levels, but demand slipping as we come out of the "draw" season). Prices are set to continue to grind sideways, with $4.20 being the support level to watch. Bottom line is that natural gas prices remain about 30% higher than they were in the beginning of the winter, which continues to support the argument behind the natural gas exploration-and-production stock ETFs, XOP and FCG.

Elsewhere in energy, WTI crude was little-changed on the day again as it remains pinned between two widely followed moving averages—the 50-day, which is supporting at $99.16, and the 200-day above at $100.34. Traders will be looking to the EIA inventory data along with the Durable Goods Report which are both due out later this morning, and if there is a material surprise in either report (specifically the durable goods report as energy futures have shown more sensitivity to economic data recently), expect a move through one of those technical levels, otherwise, futures will continue their grind sideways.

There have been a lot of headlines this week concerning this weekend's oil spill that caused the Houston Ship Channel to close for a couple days. What you need to know is that the closure has not and will not materially affect crude oil or product futures prices. We wont see the effects of the closed channel until next Wednesday's report, at which point it will already be priced in anyway.

Market	Level	Change	% Change
Dollar Index	80.085	.006	0.01%
EUR/USD	1.3823	-.0015	-0.11%
GBP/USD	1.6529	.0033	0.20%
USD/JPY	102.25	.02	0.02%
USD/CAD	1.1158	-.0033	-0.29%
AUD/USD	.9162	.003	0.33%
USD/BRL	2.3095	-.0125	-0.54%
10-year Yield	2.735	.002	0.07%
30-year Yield	3.579	.007	0.20%
Prices taken at previous day market close.			

Currencies & Bonds

Currency markets were mostly quiet yesterday in aggregate, although the flattish results hide some decent intraday volatility, especially in the euro. The euro was down small (0.1%) on a combination of "dovish" central banker rhetoric and the German IFO business expectation survey missing expectations. But, the euro did close well off the lows (more on that below). The Dollar Index was unchanged as markets largely ignored the housing data (it was mostly in-line) and Fed-speak. (Plosser on CNBC said the Fed didn't hawkishly change policy last Wednesday, but the market knows that already.) The yen was also flat in quiet trading.

Commodity currencies were the big movers Tuesday and enjoyed a nice rally as part of the overall "China/ commodity" bounce that we saw in equities and copper, and the Aussie pushed closer to a three-month high at $0.9134. That level was broken overnight and as I am typing this, the high tick in Aussie futures is already $0.9184. I imagine this will cause another wave of short-covering push the Aussie higher into the low- to mid-$0.90s, which will make my Aussie short call a bit more painful in the short term.

But, the RBA remains on the side of a weaker Aussie, and I'd imagine they will start to intervene (either rhetorically or by actual policy) if we see the Aussie get into the mid-$0.90s. I stand by my belief that we'll see $0.85 in the Aussie before $0.95 (although I'm going out a limb there, given how "short" this market is, bearish fundamentals notwithstanding). Unless I'm wrong about the RBA intentions, the upside on the Aussie should be capped, although there is the possibility for a bit more of a rally.

In bonds, both the 30-year and 10-year Treasury fell marginally yesterday, despite "dovish" Fed-speak and the Fed buying $1.154 billion worth of 30-year bonds. Bonds were actually sitting on modest declines until mid-day, when a strong 2-year Treasury auction occurred. The result was an average bid to cover (measure of demand) of 3.20, but an actual yield that was 1 basis point below the "when issued" yield, implying those who were bidding were doing so aggressively. So, it would appear that a higher 2-year yield (up 13 points from last month's auction) boosted demand.

Daily auctions aside (there is a 5-year auction today and a 7-year tomorrow), bonds more broadly continue to consolidate recent economic data and FOMC-induced volatility. Like the dollar, Treasuries have largely ignored dovish "Fed-speak" since the Wednesday FOMC meeting. Regardless of what the Fed says, any erring of policy going forward will be toward the hawkish, not the dovish, unless we get a material downshift in the economic data.

The Bundesbank is Turning Dovish, and Other Stories of Pigs Miraculously Getting Wings.

The euro was in focus yesterday as surprising comments by Bundesbank President Jens Weidmann about the possibility of QE caught the markets by surprise and resulted in an early euro sell-off. But, what seems too good to be true usually is. Despite the headlines implying the staunchly anti-inflationary Germans were warming to the idea of QE, the reality remains the ECB isn't about to ease policy in the near future, regardless of the rhetoric.

Weidmann caught markets by surprise when he said that an ECB QE program was not out of the question. That's particularly important and shocking because the Germans are seen as the primary obstacle to the ECB using QE. So, it would appear on the surface that, in the face of a growth dis-inflation threat, the Germans are coming around.

That's not what happened, though. First, Weidmann said that no further action by the ECB was needed at the moment (so that pours water on the QE idea). Second, if you read the interview, it's pretty obvious that Weidmann is trying to use rhetoric and "ECB-speak" to help provide incremental accommodation instead of actual policy tools like lower interest rates or QE. And, the reason we've seen this recent campaign of "verbal easing" from numerous ECB officials is because of the rising euro.

Remember, the euro hit a new multi-year high a few weeks ago, and seems intent on moving toward 1.40 vs. the dollar. In an economy that already has a dis-inflation problem thanks to the EU crisis of the last several years, a very strong euro is a big risk to growth, because the strong currency 1) reduces exports (especially for export-driven countries like Germany) and 2) acts as another deflationary force on the EU economy.

So, Weidmann, Mario Draghi and others (Finnish central bank governor Erkki Liikanen said yesterday that negative deposit rates aren't out of the question, either) aren't so much trying to "talk growth up" in the EU as they are trying to "talk the euro down." But, it's not working. The only thing that has caused a hiccup in the rally in the euro over the past three weeks has been the "hawkish" Fed. And, that likely will continue until the ECB actually moves to ease policy further.

I've said it before and I'll say it again: The market wants the ECB to do QE, and it'll keep causing more pain (by pushing up the euro) until the ECB decides to prove it's willing to use "unconventional measures" to stimulate the EU economy. Until then, expect the euro to continue to be buoyant. (Given the Fed is tapering, I don't expect a runaway rally in the euro. But it's not going down materially, either, unless something changes.)

The ECB got away with calming the market with rhetoric two summers ago when Draghi's "whatever it takes" comment broke the euro-zone crisis. But, this time the market wants action, and it'll keep pressure on the ECB until 1) they ease further or 2) the EU economy sees growth materially improve. Neither are very likely at this point.

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	**Bullish**	**Bullish**	**Bullish**	*The S&P 500 continues to bounce between 1850 and 1880 as geo-political and China concerns are a headwind, but 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.* *Support remains in the 1850 area for the S&P, with resistance at 1880.*

Trade Ideas

Long Market "Losers": **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 and banks. I think coal stocks (KOL, ACI) are now attractive, given positive fundamentals thanks to 1) high natural gas prices, 2) low inventories and 3) an attractive entry point due to China related basic materials sell off last week. 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 & Add Around $1300: **With a reduction in geo-political risk and a surprisingly hawkish FOMC statement, we are seeing some of the recent "froth" taken out of gold, as it's traded down towards $1300. I would look to buy or add to positions on this dip with a stop at $1300.**

	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.**