7:00's Report

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

March 28th, 2014

Pre 7:00 Look

- U.S. Futures and European markets are higher this morning while Asian markets were mixed overnight
- There were several economic reports in both Japan and the EU but Spanish CPI was the main driver of the markets
- European bond yields fell to 3wk lows (Spanish 10yr yields actually hit an 8 yr low) after an unexpected dip in Spanish inflation which supports investor hopes of seeing the ECB ease policy next week as the threat of EU zone deflation continues to rise
- Econ Today: Personal Incomes & Outlays (E: .2%) Fed Speak: George (1:15 PM)

Market	Level	Change	% Change
S&P 500 Futures	1845.75	5.25	0.29%
U.S. Dollar (DXY)	80.325	.073	0.09%
Gold	1296.6	1.80	0.14%
WTI	101.77	.49	0.48%
10-year	2.670	-.031	-1.15%

Equities

Stocks spent the day oscillating back and forth around the flat mark as momentum stocks continued looking for a bottom. The S&P 500 finished the day down 0.19%

Stocks immediately sold off on the open yesterday but bounced off support near 1,840 and began to rally. Economic data was relatively in-line with expectations (GDP slightly missed, Weekly Jobless Claims slightly beat, and Pending Home Sales met expectations). But the market seemed to largely shrug off the economic reports, showing more concern for "micro trends," namely the sharp selling we've seen in biotech and big-momentum tech stocks.

The morning volatility was short-lived, though, as both the low and high of the day were established in the first hour of trading. Despite the bounce off the lows early in the session, based on the sideways grind we saw over the rest of the day, it was clear that buyers remained hesitant and sidelined. Some colleagues on the floor mentioned some vanilla mutual funds continuing to lighten up on exposure to momentum stocks, but nothing was overly concerning.

Trading Color

Sector-wise, energy and utilities were the only subsectors of the S&P to close higher. They did so in a material way, as they gained about 0.75% apiece. The worst performers were financials, tech and consumer discretionary stocks.

The strong outperformance in energy was again a result of rallying oil and product prices. (Crude oil and RBOB futures added over 1% while nat gas futures gained 3%.) Utilities outperformed thanks to a continuation of the rotation out of momentum and growth stocks and into value and defensive sectors.

Financials were the worst performers yesterday thanks to the results of the Fed's "stress test," which were released overnight on Wednesday. C along with 5 other banks had capital return plans rejected by the Fed that included increasing dividend payments and stock buybacks.

Meanwhile, the other 25 of the 30 "stress test" participants had their plans cleared by the Fed (both BAC and GS had to make last-minute adjustments to get the passing grade, though). The results triggered a "sell the news" response in the banks, but in reality it was a non-

Market	Level	Change	% Change
Dow	16,264.23	-4.76	-0.03%
TSX	14,178.84	-5.26	-0.04%
Brazil	49,646.79	1,681.18	3.50%
FTSE	6,622.58	34.26	0.52%
Nikkei	14,690.03	73.14	0.50%
Hang Seng	22,065.53	231.08	1.06%
ASX	5,366.94	16.85	0.31%

Prices taken at previous day market close.

event. The banks who *failed* now have 90 days to re-evaluate and make changes to their plans in order to meet the requirements. Regardless, it was an excuse to sell the financials yesterday, which is why they were the worst performers.

Market	Level	Change	% Change
DBC	26.16	.26	1.00%
Gold	1292.80	-10.60	-0.81%
Silver	19.69	-.09	-0.46%
Copper	2.994	.0285	0.96%
WTI	101.26	1.00	1.00%
Brent	107.83	.80	0.75%
Nat Gas	4.546	.144	3.27%
RBOB	2.9389	.03	1.03%
DBA (Grains)	28.455	.325	1.16%
Prices taken at previous day market close.			

Bottom Line

There were some signs yesterday that the selling in these momentum sectors (represented by QNET and NBI) is getting exhausted, although it's a bit to early to call a bottom in those names.

Part of the markets inability to mount much of a rally over the past few days is in part because of the calendar (the S&P is almost perfectly flat year to date and there's no reason to add any material long exposure with two days left in the quarter). So, what happens Tuesday (April 1) will be interesting to see as that's when you'd expect "dip buyers" to move into these beaten up growth sectors, given its a new quarter.

QNET and NBI remain to key indicators to watch, but the key to this markets remains focusing on the "micro." Banks got hit because of the stress tests but any material dip is likely a "buy," while coal and natural gas E&Ps (and energy broadly) continues to act very well despite the flat overall market.

Economics

Weekly Jobless Claims

- Jobless Claims were 311K vs. (E) 323K
- 4-Week Moving Average fell 9.5K to 317,750.

Takeaway

Weekly jobless claims fell 10K to 311K last week, which is the lowest level since before the government shut down back in October '13 (excluding the week of Thanksgiving, which was obviously skewed by the holiday break). The data from the week prior was revised marginally higher from 320K to 321K. Last week's drop in claims has brought the 4-week moving average to the lowest level since the first week of October, matching the drop in the headline number.

Bottom line is that, lately, weekly jobless claims have transitioned from being largely range-bound to now apparently trending lower. The change of seasons and subsequent better weather was cited as one of the potential reasons for the recently improving trend in the labor market.

One key takeaway from the report is that early estimates for the official March jobs report will almost certainly tick higher, thanks to the improvement we have seen in weekly claims this month. And, if we start to see the job market advance (evident by a strong March Employment Report), then that will clearly be a positive for risk assets going forward.

Pending Home Sales

- The Pending Home Sales Index fell 0.8% to 93.9 in February, in-line with analyst estimates.

Takeaway

The existing Home Sales Index fell to 93.9 last month from 94.7 in January. The drop in the index was the 8th in a row. Overall there were no surprises in the report, as the decline of 0.8% was exactly in-line with analyst expectations. The excuse of weather, however, was less applicable based on the regional results, which cited weakness in all four regions, including the West and South where the winter has been fairly mild.

Bottom line is yesterday's pending home sales report did not materially change the view on the housing market. But, it certainly was another "straw" on the camel's back, and the housing market remains an area of concern that requires monitoring. As we continue to transition from winter to spring and get a look at "clean" data that is unaffected by extreme weather, holidays or other unforeseen events, we will have a better idea about the condition of the housing sector.

Commodities

Commodities were mostly higher yesterday in an active day of trading. The space was led up by gains in the energy sector while the metals were mostly weaker in technical trading. The benchmark commodity tracking index ETF, DBC, gained 1%.

The metals traded mostly lower yesterday as gold fell 0.81%, silver slipped 0.46% and palladium dropped 3%. Gold was obviously in the spotlight as the $1,300 level was violated overnight. Buyers stepped in and tried to reclaim that critical $1,300 level in the first hour of trading, but they failed and the price fell to fresh session lows in the low-$1,290s.

Gold futures closed down near the lows at $1,292.80 and in turn the technical situation materially changed for the worse. Gold closed below all four of the supporting technicals that were based our low-risk/high-reward trade earlier in the week (the already-broken uptrend line, both the 50- and 200-day moving averages, and obviously the psychological $1,300 level).

But I would like to remind you that gold is famous for throwing big head-fakes, and this could be one of them. I'm still holding my positions and will do so until gold breaks $1290, and the reason I'm saying that is because 1) gold stocks (GDX) closed higher yesterday—and that almost never happens when gold is about to sharply decline. 2) The sell off in gold is happening in low liquidity, after hours trading, so I'm giving the stop a little more leeway than I normally would seeing as traders are trying to run the stops after hours.

If $1290 is broken (at which point I'll be out) on the charts the next line of support is at the 100-day moving average that lies below at $1,273.60 while resistance is now the former critical support level of $1,300. For now the bears are in the driver's seat but, if futures are able to rally back and close 2-3 times above $1,300, a rally could ensue.

Market	Level	Change	% Change
Dollar Index	80.265	.096	0.12%
EUR/USD	1.3745	-.0036	-0.26%
GBP/USD	1.662	.0035	0.21%
USD/JPY	102.12	.09	0.09%
USD/CAD	1.1031	-.0068	-0.61%
AUD/USD	.9255	.0036	0.39%
USD/BRL	2.2617	-.042	-1.82%
10-year Yield	2.670	-.031	-1.15%
30-year Yield	3.507	-.044	-1.24%
Prices taken at previous day market close.			

Copper was able to buck the trend yesterday, outperforming every other metal. It was actually able to log a gain for the day, adding 0.96%. The rally despite the weakness in the space was promising for the industrial metal. Futures did fail to close above the important $3 mark again, but on the charts, the technicals remain favorable as the daily range had yet another "higher low," which is obviously bullish.

Despite the technicals leaning in favor of the bulls, the story remains the same: Copper is trading as a proxy to the Chinese economy and without material news (whether it be good or bad), copper futures are stuck range-bound between last week's multi-year lows and resistance at the $3 level.

Bottom line is that if we see a copper break to the upside, I would be interested in buying into the Chinese equity markets for an outperformance opportunity.

Moving to energy, crude oil was able to break out through resistance yesterday, gaining an even 1% on the day. The 200-day moving average was proving to be solid resistance up until yesterday when WTI futures opened nearly 70 cents above it. We pointed out that the price action into the close Wednesday was very strong, as futures broke to new two-week highs in the last few minutes of the primary session. And, we noted that the strength going into the close is bullish and could very well be an indication that prices are set to rally back toward the highs of the February price range at $103-$105. That is exactly what seems to be in the works. On the charts, the former resistance level of the 200-day moving average ($100.38) is now support while resistance hovers above at the $103/bbl level.

Elsewhere in energy, natural gas rallied 3.27% to close above $4.50 yesterday thanks to the EIA inventory release that indicated a draw of 57 Bcf in supplies, which matched expectations. Despite matching expectations, the draw was 9 Bcf larger than the week prior, which raised some concerns because next week's report will reflect the heightened demand of this week due to the late-season snowstorm. The natural gas E&P ETFs were up 2.82% (FCG) and 1.8% (XOP) yesterday thanks in part to the rally in nat gas futures. This led them to handily outperform the broader markets, which oscillated around the flat mark for most of the day.

Currencies & Bonds

The Dollar Index was again only slightly higher Thursday (up 0.1%). Like Wednesday, the small gain was the result of euro weakness rather than broad U.S. dollar strength.

The euro dropped 0.3% yesterday on continued pressure from dovish rhetoric from the ECB. This time, it was an article by the FT that implied the ECB was working to help revive the asset-backed security market in Europe. Asset-backed securities (which got a bad name in the crisis) are a way for companies to access capital. Generally speaking, investment firms pool loans from companies backed by assets (a house, factory, inventory, etc.), and then sell the pools to investors. Having a robust and liquid ABS market makes banks more likely to lend, because they can then sell those loans and lay off the risk.

The ECB is looking to relax capital rules for insurance companies, and in doing so that would free up capital to buy higher-yielding (albeit riskier) asset-backed securities. And, ECB Chief Mario Draghi even hinted that, if the ABS market could be revitalized, the ECB may even be interested in buying A-B Securities as a way to help stimulate the economy and fight deflation (again, a veiled reference to QE-type action by the ECB).

So, the "chatter" about the ECB doing more to stimulate the EU economy and push down the value of the euro continues, and it is meeting with some success. But, the market will still demand some actual action before the euro can trade materially lower. The longer the "chatter" goes on with no action, the less effective it will be. The euro is near a one-month low vs. the dollar, but unless economic data suddenly turns south in the EU or geopolitical tensions flare up again, I'd be surprised to see material downside from here in the coming weeks.

Staying in Europe, the British pound rallied nicely against the dollar yesterday (up 0.2%) on the back of stronger-than-expected retail sales data. But the commodity currencies were the big winners vs. the dollar yesterday. Both the Aussie and Loonie continued their recent rally, as all things "China related" continue to bounce. The Aussie rallied to 0.35% to trade above $0.92 vs. the dollar, a 4-month high. And, while I'm still a fundamental "Aussie" bear, it's obviously broken out to the upside, and this short-covering rally could continue into the mid-$0.90s. But based on the RBA and the likely trajectory of Chinese growth, I maintain that selling the Aussie anywhere with a "0.9" handle should be a profitable trade in the coming months. It's just painful right now.

Bonds continued their rally yesterday, and I'm surprised by the strength in the long bond here – and that's one of those "non-confirming" indicators that's making me a bit nervous in stocks. With the labor market picking up (at least, according to jobless claims), and the economic data signaling that the economic slowdown in the winter was largely weather-related, combined with the FOMC acknowledging higher rates in the future, bonds *should* be declining – but they are not.

There are two reasons for this that I can think of: First, the outlook for Fed policy is more "dovish" than we think, as the Dollar Index isn't really strong (remember it's going up because the euro is going down, not because of people's desire to allocate to dollars). But, I don't think that's the case, given that the Fed seems committed to tapering QE and raising interest rates in mid-2015. Second, money is moving into bonds because they are anticipating some sort of an economic slowdown or correction in the equity market. And, while I don't readily see the catalyst, the bond market is the "smartest market," so this illogical strength in long bonds has my attention.

Longer term, the thesis remains the same: I do believe the bond bull market ended last year, and that the direction of rates over the coming months and quarters (and years) will be higher, not lower. But, clearly we've been in a long counter-trend rally, and while I think it's done, if the 30-year trades much higher from here (say above 135'00), then I'll have to acknowledge that this counter-trend rally isn't over and reduce positions to just a "maintenance" short bond allocation. Until that happens, though, I continue to view this as an attractive entry point for "short bond" positions that have a good risk/reward setup in the short and long term.

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.**

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: **Gold has broken through $1300, and unless it can trade back above that level today (or trades down through $1290), then I'll look to exit my long positions as the outlook for gold will have changed materially.**

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."**

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.**