7:00's Report

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

March 6th, 2014

Pre 7:00 Look

- Futures are again flat this morning after another uneventful night as focus turns to the ECB meeting.
- Nothing new o/n from the Ukraine—all sides are talking at this point and the situation remains stable.
- Economically is was another good night. German manufacturers orders beat (1.2% vs. (E) .7%) while Aussie exports rose sharply (20.1% yoy) and retail sales beat estimates.
- Econ Today: BOE Rate Decision (7:00), ECB Decision and Press Conference (7:45, 8:30). Jobless Claims (E: 338K), Fed Speak: Dudley (8:30 AM), Lockhart (6:00 PM).

Market	Level	Change	% Change
S&P 500 Futures	1874.25	1.75	.09%
U.S. Dollar (DXY)	80.105	-.012	-.01%
Gold	1334.40	-5.90	-.44%
WTI	101.18	-.27	-.27%
10-year	2.698	.007	0.26%

Equities

Stocks closed little-changed on Thursday as the market impressively held onto Wednesday's gains despite soft economic data. The S&P 500 declined just 0.01%.

For the first time in over a week, economic data was the primary market driver yesterday, although the net effect wasn't very big because stocks closed flat. The market opened flat Tuesday as good international economic data (European and Chinese composite PMIs) helped support futures, while stocks largely shrugged off the ADP employment report miss.

At 10 AM the market dipped temporarily on the surprisingly weak ISM non-manufacturing index, but the S&P only fell a few points and recouped those losses by lunchtime, despite the lack of any positive catalysts.

The afternoon was busy from calendar standpoint as The Fed Beige Book was released at 2 PM and Fed Chair Yellen spoke, but neither event really moved markets. Stocks rallied a few points off the Beige Book release, as the report cited weather as a large contributing factor to recent soft economic data. But, the slightly rally couldn't gain any momentum and stocks drifted in a tight range throughout the final hours of trading. Stocks dipped slightly into the close, but overall the afternoon was a pretty quiet one.

Geopolitically, there were headlines related to Ukraine hitting the wires throughout the day (Secretary of State John Kerry and Russian Foreign Minister Sergey Lavrov spoke in Paris, and Kerry made a statement during the last hour of trading). But to be honest, the market has "moved on" from Ukraine in its current state.

Trading Color

After a day of excitement on Tuesday, low trading volume and activity returned yesterday (and the volume numbers were artificially inflated because apparently there were several secondaries yesterday). Given the jobs report loomed less than 48 hours away yesterday, it seemed the entire market went into "wait and see" mode, and that will likely continue today.

Trading in the indices didn't reveal much (the Russell declined marginally, down 0.22%, while the Nasdaq caught a small bid), although the sector trading implied that yesterday was a deceptively positive day.

Cyclical sectors (and the banks in particular) outperformed while defensive sectors lagged, although to be

Market	Level	Change	% Change
Dow	16,364.55	-31.33	-0.19%
TSX	14,303.43	13.57	0.09%
Brazil	46,589.00	-505.40	-1.07%
FTSE	6786.68	11.26	.17%
Nikkei	15134.75	237.12	1.59%
Hang Seng	22702.97	123.19	.55%
ASX	5445.89	-0.34	-.01%
Prices taken at previous day market close.			

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fair, none of the moves were that big outside of the 1% jump in the XLF (financials ETF). Financials, consumer discretionary, tech and basic materials all rallied, while utilities, REITs and consumer staples lagged.

So, point being, we are seeing continued recent leadership from cyclical sectors (especially the financials), and that's an underlying positive.

Market	Level	Change	% Change
DBC	26.19	-19	-0.74%
Gold	1338.80	.90	0.07%
Silver	21.215	-.007	-0.03%
Copper	3.203	-.0115	-0.36%
WTI	101.14	-2.19	-2.12%
Brent	107.77	-1.53	-1.40%
Nat Gas	4.574	-.093	-1.99%
RBOB	2.941	-.0443	-1.48%
DBA (Grains)	28.37	.41	1.47%

Prices taken at previous day market close.

Bottom Line

Yesterday was a deceptively impressive day for stocks, considering that 1) The S&P 500 was able to close flat despite the big Tuesday rally and soft economic data, and 2) the S&P 500 never really dipped the entire day, not even in the morning (when you would have expected sellers to take a shot and see if they could get things moving to the downside).

Today should be quiet as everyone looks ahead to the jobs report, unless we get some major surprise from the ECB.

Jobs Report Preview

Given the importance of tomorrow's jobs report, I like to offer a preview a full 24 hours before it, as not everyone gets to the Report before 8:30 AM EST every morning.

The "official" expectation for the jobs report is 150K, although in light of the "miss" from the ADP data, the "whisper number" has dropped a bit to around 140K-ish.

Tomorrow's jobs report is going to be critical for two reasons: First, it's going to help further resolve the question of whether the economic sluggishness in January and February was really just temporary and weather-induced, or if it is becoming something more. So far, data in February has shown some uptick in activity, but if we get a third-consecutive weak jobs number, people will begin to view this slowdown as something more than temporary. Second, this jobs report will likely be key in influencing the Fed's decision on whether to continue to "taper" QE at its meeting later this month.

Here's the rundown on potential outcomes.

The "Too Hot" Scenario: There isn't one. The market wants good economic data, so even if this number shocks everyone and prints north of 200K jobs added (which is all but impossible) stocks will rally hard, and bonds and gold will sell off. "Good" data is "good" for the market, plain and simple.

The "Just Right" Scenario: >130K. This jobs report will get a partial "pass" versus expectations thanks to the weather. So, even if it misses the 150K estimate, as long as it's above the 130K-ish level, the market shouldn't really miss a beat—even if the previous month's data is revised lower (again, weather will be the excuse). If we see a number in the "just right" range, don't expect a big reaction from equities, bonds, the dollar or gold. That's because a "just right" number is largely priced in and won't materially alter the outlook for the economy or Fed policy (meaning they will still taper).

The "Too Cold" Scenario: <100K. This is what we need to be afraid of. Different analyst reports I've read have this "too cold" number a bit higher (say, less than 120K). However, the last few jobs reports have shown the market to be more tolerant of a "miss" than the experts thought, so I'm dropping my threshold a bit.

If we see a sub-100K number, Friday could be an ugly day. "Bad news" is bad for the market, and a print this low will call into legitimate question whether the Fed will "taper the taper" at the meeting later in March. If this number prints sub-100K, stocks will get hit and bonds and gold will rally hard.

A Potential Hedge for a Bad Jobs Report.

For those of you looking for a potential short-term "hedge" against a weak jobs report and subsequent market sell-off, look to gold. I'm not a big fan of hedging apples with oranges (hedging stocks with a commodity), but gold has been the primary beneficiary of this recent weakness in economic data since the beginning of the year. If the Fed's continued tapering of QE gets called into question on Friday because of a weak jobs report, gold will be the big winner and likely will rally hard.

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And, while it's not a 100% true hedge against the S&P 500, gold will trade with enough volatility to cushion any potential losses should the market decline sharply on a bad report (bonds will also rally, but not likely not with the same volatility as stocks). So, if you're looking for a hedge, consider GLD (or gold futures).

Economics

ISM Non-Manufacturing Index

- The ISM Non-Manufacturing Index fell to 51.6 vs. (E) 53.5

Takeaway

The ISM non-manufacturing index number for February was rather disappointing yesterday as the headline was down 2.4 points from January to 51.6, missing expectations of 53.5. The details within the report were better than the headline as the new orders component, the leading indicator in the report, rose 51.3 from 50.9 in January.

The employment component, however, was very poor, falling 8.9 percentage points to 47.5 from 56.4 in January. The sub-50 (contraction) reading was the first in 25 months. Although the employment reading was surprisingly soft, it is in-line with other jobs reports released this winter that have shown seasonal weakness, and that helped cushion the blow to a point.

As was the case with the ADP employment report, the market largely ignored the ISM service index data, as investors already have their sights set on the official government jobs report due out tomorrow morning.

Bottom line is that none of the economic data released today will change Fed policy, which is why there was a lack of response from the market.

Market	Level	Change	% Change
Dollar Index	80.13	-.053	-0.07%
EUR/USD	1.3727	-.0015	-0.11%
GBP/USD	1.6715	.0053	0.32%
USD/JPY	102.29	.09	0.09%
USD/CAD	1.1036	-.0055	-0.50%
AUD/USD	.898	.0031	0.35%
USD/BRL	2.3191	-.0215	-0.92%
10-year Yield	2.698	.007	0.26%
30-year Yield	3.644	.006	0.16%
Prices taken at previous day market close.			

Commodities

Commodities were almost universally weaker Wednesday as the space saw a second-straight day of profit-taking given the recent rally amidst continued calming of the Ukrainian situation. The commodity ETF DBC fell 0.8%.

Energy was the laggard Wednesday, as every major energy commodity declined by more than 1.5%. WTI crude finished the day 2% lower, breaking down through $102/bbl. The reduction of the geopolitical risk premium combined with bearish weekly inventory data to send WTI to two-week closing lows. Looking at the inventory data, WTI saw a build of 1.43 million barrels vs. (E) 1.0 million, but it was really the distillate data that got the entire energy space moving lower. Distillates saw a build of 1.4 million barrels vs. (E) -1.0 million barrels.

If there was one "reason" energy commodities have outperformed over the past two months, it would be the very low distillate inventories, courtesy of the cold winter. Those low inventories implied strong future refinery demand for WTI crude, as more heating oil and diesel would need to be produced to meet rising demand. Well, it would appear that, despite it still being cold, "heat" demand is starting to wane, and with it the implied demand for WTI crude.

Does that mean we're all of a sudden bearish on WTI? No; it remains range-bound between roughly $99.80 and $105. But in the short term, the picture may be turning less bullish, so I'd be more interested in buying a further dip than I would be at these levels.

On the opposite side of the spectrum, gold and silver both traded pretty well yesterday, with both metals closing virtually flat. Gold was initially lower Wednesday but caught a bid on the soft ADP and ISM non-manufacturing index data. And, again, I was impressed by gold's ability to "hang in" given the continued removal of geopolitical risk from other assets (like WTI crude).

With the jobs report looming, I wouldn't expect much of a move in gold today. And despite the potential for the jobs report to "miss" estimates, I'd prefer to add any outright long positions on gold a little bit lower than current levels. That is, unless you're using it for the aforementioned hedge against a weak jobs number and likely

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declining stock market.

Bottom line is broadly we're seeing some consolidation in the commodity markets, which is to be expected given the big recent rally. But, recent economic data (including yesterday's composite PMIs) imply the global recovery is still ongoing, and that's an unappreciated tailwind for commodities. The sector in general remains very much "unloved" despite the good performance year to date.

Currencies & Bonds

The dollar spent most of the day modestly lower yesterday thanks to the weaker-than-expected economic releases (both the ISM service index and the ADP employment report missed expectations) but gained back most of those losses once the Fed's Beige Book was released (the Fed cited weather as a major factor in the weaker-than-expected economic data this winter). The dollar finished the day down -0.08%.

In Europe, the euro was flat despite better-than-expected economic data being released in the form of the European service PMIs and the retail sales beat. The euro did not rally on the news, though, because traders were hesitant to take positions ahead of the ECB's announcement/press conference (8:30 am this morning).

As I said in yesterday's Report, the expectation is that the ECB will remove "sterilization" from SMP purchases, which may be mistakenly interpreted as "dovish" by many traders and investors. However, as I mentioned before, it is not, and any sell-off in the euro on the news should be looked at as a buying opportunity. At the end of the day, not "sterilizing" SMP purchases won't reverse the disinflation creeping into the euro zone, and that is by default euro-bullish.

Elsewhere in Europe the pound was higher against the dollar, closing the day up 0.31% on the stronger-than-estimated service PMIs that the rest of Europe seemed to disregard. I also stand by my recommendation to buy the pound on dips as, given the current situation, the Bank of England will be the first CB to raise interest rates, which is obviously supportive of the currency. Buying the pound via futures or the ETF, FXB, are the best ways to get into the trade.

Interestingly, the biggest movers in the currency space yesterday were the commodity currencies, as the Aussie rallied 0.26% and the Loonie gained 0.48%.

The Aussie rallied as a result of the GDP report printing a touch better than expected at 0.8% vs. (E) 0.6% m/m and 2.8% vs. (E) 2.3% y/y. And, that rally is continuing this morning thanks to strong Australian export and retail sales data. Aussie has now traded through the .90 level versus the dollar, which I believe is a great entry point to open, or add to, short Aussie positions. Quite simply, I don't think the Reserve Bank of Australia will allow appreciation in Aussie materially past the $0.90 mark. You can either short outright Aussie dollar futures or shorts FXA, or buy the ProShares UltraShort AUD ETF (CROC); however it is "trade by appointment" at an average of between 10K and 20K shares traded a day.

The Loonie moved higher following the Bank of Canada's decision to leave rates unchanged at its rate meeting, which was expected. However, most analysts expected more dovish commentary regarding the direction of policy in near future. The BOC statement was surprisingly more neutral than it was accommodative (dovish), which led to a rally in the currency as weak, speculative shorts closed positions.

Bottom line is we could see an extension of the short-covering rally in the commodity currencies, but those are rallies to short, as the "golden era" of the commodity currencies has ended, and both are heading much lower over time.

Bonds were essentially flat yesterday as trading mirrored that of the Dollar Index rather closely. The soft economic data caused a small rally but the Beige Book reversed those gains and sent Treasuries back toward the flat mark. The bond market, like most other asset classes, is looking ahead to tomorrow's official government jobs report.

Have a good day,

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 "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. 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.**

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 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.**

	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 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 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 above $1300 on the long side and feel more comfortable around the mid-$1200's, but 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 DOlar 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.**

	Fundamental Outlook	Technical Outlook	Overall	Comments
Treasuries	**Bearish**	**Bearish**	**Bearish**	*Treasuries are stalemated in the short term as weak economic data is supportive, but the Fed clearly favoring continued tapering of QE, baring a big drop in economic data, has caused the counter trend rally to stall. Longer term, though, fundamentals remain negative and I view current levels as great entry points for short bond positions.*

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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