7:00's Report

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

April 11th, 2014

IMPV: Imperva isn't a big stock, but it is a "momentum" stock, and 40% plunge yesterday spooked people and helped cause the carnage in tech.

Pre 7:00 Look

- Futures are little changed this morning while international markets are sharply lower following yesterdays steep selloff in the U.S.
- Economically, Chinese CPI and PPI were released last night and the results were largely inline with estimates.
- In Europe, German CPI also met expectations but EU markets are primarily focused on yesterday's weakness in U.S. markets.
- Econ Today: PPI (E: 0.1%)

Market	Level	Change	% Change
S&P 500 Futures	1826.75	-.25	-0.01%
U.S. Dollar (DXY)	79.455	.005	0.01%
Gold	1323.00	2.50	0.19%
WTI	103.29	-.11	-0.11%
10-year	2.628	-.056	-2.09%

Equities

Market Recap

Stocks plunged Thursday and broke support at 1,840 after selling resumed in momentum sectors, which dragged down the entire market. The S&P 500 fell 2.09% and had its worst day of 2014.

Markets were marginally weaker on the open Thursday, but there wasn't any fundamental reason for the selling other than the market being very slightly oversold given the Tuesday/Wednesday rally. Chinese trade balance was soft but not terrible, and jobless claims—which were great on the headline—were largely ignored.

Instead, trading early Thursday was again dominated by positioning and sentiment. As the "momentum" sectors again began to sell off, the rest of the market followed on the way down.

The single-best credible explanation of "why" yesterday's sell-off occurred was Imperva (IMPV). IMPV is a data security company, and while it's not exactly the poster child for tech, it is considered a "momentum" name. And, yesterday IMPV missed on sales estimates (they guided to $31 million - $31.5 million for the recent quarter vs. expectations of $36 million - $37 million). As a result, the stock plummeted nearly 44% (no that's not a typo). Although the collapse in IMPV didn't cause yesterday's sell-off, any implosion like that is undoubtedly going to cause angst toward the rest of the sector. Given the nervous sentiment toward tech, that result sparked another round of selling, obviously.

The S&P 500 tried to stabilize around 2:00, but a big sell imbalance on the close and sellers dumping into any lift

Market	Level	Change	% Change
Dow	16,170.22	-266.96	-1.62%
TSX	14,308.00	-127.58	-0.88%
Brazil	51,127.48	-57.92	-0.11%
FTSE	6,555.94	-86.03	-1.30%
Nikkei	13,960.05	-340.07	-2.38%
Hang Seng	23,003.64	-183.32	-0.79%
ASX	5,428.65	-52.10	-0.95%
Prices taken at previous day market close.			

saw stocks crash through support at 1,840. Markets sold off during the last hour before bouncing slightly into the bell.

Trading Color

Momentum and tech sectors got crushed again yesterday and, in a troubling development, both NBI and QNET both made new lows, implying this drop in momentum sectors isn't over.

Market	Level	Change	% Change
DBC	26.39	.01	0.04%
Gold	1318.30	12.40	0.95%
Silver	20.04	.27	1.37%
Copper	3.038	.001	0.03%
WTI	103.33	-.27	-0.26%
Brent	107.34	-0.64	-0.59%
Nat Gas	4.634	.048	1.05%
RBOB	3.0066	-.0018	-0.06%
DBA (Grains)	28.78	.04	0.14%
Prices taken at previous day market close.			

And, perhaps more importantly, the selling in the momentum sectors yesterday definitely spread to other sectors with positive performance. Banks and semiconductors, the two sectors I said to watch for signs of the selling spreading, dropped 2.9% and 3.16% respectively and traded to multi-week lows.

So, clearly this purge in momentum isn't over and there are signs it is spreading, which is a negative for the market overall.

More broadly, all 10 S&P 500 sub-sectors were lower yesterday and growth definitely lagged. As mentioned, banks and tech plunged 3% each, but consumer discretionary, healthcare and basic materials also traded down 2% (in-line with the market).

Defensive sectors relatively outperformed but couldn't hold up against the selling. Utilities were down 0.38%, while REITs and consumer staples traded down 0.9%.

Volumes weren't super-heavy yesterday but they were bigger than the Tuesday/Wednesday rally and in-line with the Friday/Monday sell-off. This backs up the "dead cat bounce" thesis being used to explain the midweek rally.

On the charts it's pretty clear—support at 1,840 (the lower end of the range and the 50-day moving average) broke. Unless we can get back above that level in the next day or so, the next level of support is 1,800 in the S&P 500.

Bottom Line

Yesterday was a painful day, to be sure. But stepping back, this market remains dominated by positioning and short-term sentiment, not changing fundamentals. And, because of that, I don't think yesterday was necessarily a "de-risking" situation.

Case in point, sectors with solid fundamentals that aren't over-owned relatively outperformed yesterday (i.e., global industrial miners, coal, natural gas, energy). And, those are macro-sensitive sectors that you would normally expect to get hit hard in a down-2% day in the markets.

And, we didn't see any of the other "risk off" metrics spike: WTI crude was off small, bonds rallied but not all that much, and gold didn't budge from the morning rally despite the sell-off. Point being, this was not some larger "risk off" move that would require a wholesale reduction in equity exposure.

But, clearly this sell-off isn't done yet, either. If the S&P 500 can't get back above 1,840 in the next day or so, we may be looking at another potential 5%-6% dip like we saw in January/February. So, from a strategy standpoint, I'd hold positions in "value" sectors. If you are very nervous, hedge with an SPY short, as that trade worked yesterday. (Long KOL/FCG/XOP, short SPY would have been positive yesterday, and long "Europe" short SPY would have been flat.)

Finally, something else to consider: Yesterday was the last day to sell stock and have it clear by tax day (this coming Tuesday).

Did that cause the sell-off? Of course not. But, it is something consider, because there was no "reason" for yesterday's steep drop.

Economics

Weekly Jobless Claims

- Weekly Jobless Claims fell to 300K vs. (E) 318K
- The 4 Week Moving Average dropped 3.75K to 315.75K

Takeaway

Weekly jobless claims fell by 32K to an even 300K last week, which was much better than analyst expectations that called for a more modest dip to 318K. The 4-week moving average resumed its trend lower after rising last week for the first time in 6 weeks. The 4-week MA, which offers a smoother look at the often-volatile (or skewed) weekly data, declined 3.75K to 315.75K—the lowest reading since the week before the government shutdown in October.

The 4-week average is now sitting 14.75K below where it was a month ago, and 21.75K below readings from 2 months ago. The data suggest that jobless claims are trending for the better, which is largely in-line with the improving monthly government jobs report as the labor market recovers from the severe weather we saw this winter.

The market reaction to the report was light, as the Easter holiday was cited in possibly skewing the data as employers hire additional workers to accommodate seasonal demand. Bottom line is, the trend of falling weekly jobless claims appears to have resumed last week after a slight pullback the week prior, and better employment data is obviously bullish for risk assets going forward.

Commodities

Commodities were mixed yesterday as the metals outperformed on the details of the Chinese trade data, and the energy sector was little-changed as Wednesday's gains were digested. The benchmark commodity tracking index ETF, DBC, was little-changed.

Natural gas was the strongest-performing commodity yesterday, rising 2% to a 1-month high following the weekly EIA inventory report. The EIA reported that supply levels rose for the first time this year, increasing by 4 Bcf vs. (E) +12 Bcf. We mentioned in yesterday's Report that any build below analysts' estimates (or a surprise draw) would likely initiate some buying. And, as expected, there was a sharp rally in nat gas futures upon release of the report. In fact, futures rallied more than 11 cents in the first minute after the report. (HFT conspiracy theorists were all over this one.) On the charts, the resistance level we were watching ($4.65) was broken in that one-minute rally and became support for the remainder of the day. Going forward we will look to that level, $4.65, for further support, and to the 50-day moving average as the first line of resistance at $4.75.

Market	Level	Change	% Change
Dollar Index	79.48	-.073	-0.09%
EUR/USD	1.3884	.0029	0.21%
GBP/USD	1.6779	-.0013	-0.08%
USD/JPY	101.47	-.50	-0.49%
USD/CAD	1.0923	.0046	0.42%
AUD/USD	.9411	.0025	0.27%
USD/BRL	2.1885	-.01	-0.45%
10-year Yield	2.628	-.056	-2.09%
30-year Yield	3.503	-.062	-1.74%
Prices taken at previous day market close.			

Elsewhere in energy, crude oil and the products were little-changed. WTI crude, RBOB gasoline and heating oil futures all drifted sideways throughout the day as Wednesday's gains, due to the EIA report, were further digested. Again, it appears that gasoline is replacing heating oil as the supporting component to the energy space (which makes sense based on the calendar). With the summer driving season just around the corner and demand only set to rise, we expect the energy space to also stay elevated. On the charts, crude oil futures have support down toward $101.50 while $105 remains the near-term ceiling (as well as the level to beat for the bulls).

Moving to the metals market, both the industrial and precious varieties were higher yesterday, with the two most-notable being copper and gold.

Copper was higher as a bid came into the market after Chinese trade data was released Wednesday night. Although the headlines (namely exports) were a miss, the details within the report cited strong industrial demand that led to an increase in copper imports. But, because of the "statistical noise" that was cited as skewing the data, the market hesitated to materially react to the trade report, especially with more data in the pipeline. Chinese CPI and PPI were released last night largely meeting expectations (but more importantly they didn't miss expectations), which may be part of the reason for the .6% rally in copper were seeing this morning.

Technically copper is now in a sideways range, but it has been able to remain comfortably above the critical $3 mark, which is promising for the bulls. On the charts, the $3 level has become solid support while last week's high tick of $3.074 is the level to beat.

As I mentioned earlier, gold did not react at all to the substantial sell-off we saw in equity markets yesterday, which was rather unusual since gold has been trading inversely to stocks for most of the year. Gold futures were up $15 in pre-market trading (while stock futures were flat) but then drifted sideways for the remainder of the day. Gold finished the session up 0.95%. On the charts, futures were able to close well above the 50-day moving average ($1,312.70), which can now be looked to for support while the next level of resistance is above at the $1,330/oz. mark.

Currencies & Bonds

Currency markets were active early yesterday morning but, unlike the stock market, action mostly faded before noon. The commodity currencies were higher thanks to the Chinese trade data getting a pass while the yen traded higher once U.S. stocks began to sell off.

The dollar traded to a fresh 5-month low despite the better-than-expected Weekly Jobless Claims report. The Dollar Index fell 0.09% on the day.

In Asia, the yen rallied to a 3-week high against the dollar in a broad, "risk-off" trade as the stock market plummeted. But, on the charts, the yen is up against several resistance levels, including a multi-month downtrend line, a Fibonacci retracement and a "triple-top."

In Australia, the Aussie rallied 0.27% yesterday thanks to a stronger-than-expected jobs report that showed unemployment had fallen to the lowest level since November. But, the Aussie came off the highs when the details of the report revealed the data was not as strong as initially thought. Most of the new jobs came from part-time workers, and full-time jobs actually fell. This morning the Aussie is higher, but off fresh five month highs thanks to the sell off in stocks.

The biggest "news" in the currency markets came vi a comments from ECB member Peter Praet, which he all but confirmed what we've been saying about the ECB and quantitative easing. Praet said in a speech that the important thing right now is that the market knows the ECB is unanimous about using some for of QE in the future, if things get worse on the dis-inflation front. So, that confirms what we've suspected—that the ECB is trying to "rhetorically ease" policy by threatening QE, while actual deployment of QE remains well in the future, if ever.

The euro rallied off the comments to fresh three week highs, but don't expect the comments to result in a lot more euro strength, as again Praet only confirmed what most of us already knew.

Moving to the bond market, Treasuries were higher yesterday, as you'd expect when stocks plunge as they did, but the Treasury gains weren't substantial (.5% in the thirty year) and that again implies we aren't seeing a larger "risk off" move in the markets, and the angst in stocks is staying confined to stocks, for now. Also adding to the strength in Treasuries was a 30-year auction yesterday, and the results were fairly strong. The yield was 3.525%, a half a basis point below the "when issued" yield — indicating strong demand. The bid to cover was up to 2.52 from 2.35 and 2.27 in the two prior auctions, which also shows solid demand.

Bottom line is Treasuries remain stubbornly buoyant, and 135'00 remains the level in the 30 year that tells me I'm wrong about this being one big counter trend rally in an otherwise down trending bond market. Until that level is breached, I maintain this is just a great entry point for medium and longer term bond shorts.

Have a good weekend,

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	*Stocks hit new highs last week but saw a nasty reversal on Friday, as renewed selling in growth and momentum sectors pushed markets lower. But,. 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.* *The S&P 500 gave us a head fake last week, so the range remains 1880-1840. .*

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: **"Hawkish" comments by BOJ Governor Kuroda sent the yen spiking higher vs. the dollar and DXJ near the lows for the year. I remain a fundamental bull on Japan, but a decisive break of 44.66 in DXJ will see me exit this trade, despite the fundamentals.**

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

Gold: **The outlook for gold remains unclear, and I'm not sure last week's jobs report was as "dovish" as Friday's reaction. But, gold has acted as a decent equity hedge all of 2014, so if you're nervous about the stock market here, buying gold isn't the worst idea. Use a stop at $1277.**

	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. **Similarly to DXJ, the yen caught a big rally this week after nearly breaking down to new lows just two weeks ago. If the yen were to trade below the low for the year, 100.26 yen/dollar, I would exit this trade as the trend will have clearly changed.**

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 longer term 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.**

Buy A Steepening Yield Curve: **STPP and KBE give positive exposure to a steepening yield curve, as the 10's-2's spread appears to have bottomed and should rally from here. 2.20% in that spread is my stop on STPP and KBE longs.**