7:00's Report

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

April 24th, 2014

Pre 7:00 Look

- Futures are higher this morning thanks to better than expected earnings reports after the close yesterday, namely tech giants AAPL and FB.
- International markets were mixed with Europe trading higher while Asian shares were mostly lower.
- There were no notable economic reports o/n.
- Econ Today: Durable Goods Orders (E: 2.0%), Weekly Jobless Claims (E: 313K)
- Earnings Today: AZN (E: $1.20), CAT (E: $1.25), GM (E: $0.47), AMZN (E: $0.22), MSFT (E: $0.62), P (E: $ -0.19).

Market	Level	Change	% Change
S&P 500 Futures	1881.00	8.00	0.43%
U.S. Dollar (DXY)	79.925	-.01	-0.01%
Gold	1279.20	-5.40	-0.41%
WTI	101.69	.25	0.25%
10-year	2.686	-.040	-1.47%

Equities

Market Recap

Stocks saw mild declines Wednesday as earnings and economic data largely came in "in-line" with expectations. The S&P 500 fell 0.22%.

Stocks started slightly lower as markets digested recent gains. Earnings pre-open were largely better-than-expected (T being the notable exception), but none of them really moved the broader markets.

Stocks dipped to the lows of the day shortly after the big New Home Sales miss at 10 AM, but recovered within an hour. The S&P 500 spent the rest of the day mostly treading water (the trading range after 1 o'clock was a whopping 3 points) ahead of some big earnings after the close (AAPL and FB).

Trading Color

"Momentum" gave a bit back yesterday as NBI and QNET fell 1.5% and 1.8%, respectively. Internet names were weak on profit-taking (NFLX saw selling after the AMZN/HBO content-sharing agreement, and VMW had disappointing results). Also, Greenlight Capital's David Einhorn's comments that we were in another tech bubble were repeated about 1,000 times on CNBC, reminding everyone of some of the valuation concerns in the Internet space. Biotechs also declined on profit-taking, but also earnings results were lackluster (AMGN and BIIB specifically).

The Nasdaq and the Russell 2000 had much worse days than the S&P 500 and Dow, falling 0.7% and 0.8%, respectively. Sector trading was mixed at best.

Most of the sector trading was the result of earnings, as industrials (thanks to good earnings from BA, IR and others) rose 0.4%. Along with banks, industrials were the best-performing sub-sector, while energy and basic materials were also higher (again mostly on earnings).

Homebuilders, following the horrid New Home Sales headline, dropped 1.3%, and tech and consumer discretionary also traded modestly lower. Finally, telecom also underperformed courtesy of the T drop (the stock was down 3.7%, and that's a big move for T).

Volumes were light yesterday away from specific earnings situations, as the calendar gets pretty quiet for the rest of the week on a "macro" level.

Market	Level	Change	% Change
Dow	16,501.65	-12.72	-0.08%
TSX	14,533.39	-22.58	-0.16%
Brazil	51,569.69	-407.17	-0.78%
FTSE	6,719.50	44.76	0.67%
Nikkei	14,404.99	-141.28	-0.97%
Hang Seng	22,562.80	53.16	0.24%
ASX	5,531.00	13.24	0.24%
Prices taken at previous day market close.			

On the charts the story remains the same: 1,880-1,840 is the range in the S&P 500.

Bottom Line

Market	Level	Change	% Change
DBC	26.51	-.03	-0.11%
Gold	1284.90	3.80	0.30%
Silver	19.43	.069	0.36%
Copper	3.059	.0055	0.18%
WTI	101.49	-.26	-0.26%
Brent	109.12	-0.15	-0.14%
Nat Gas	4.738	-.001	-0.02%
RBOB	3.0919	-.0033	-0.11%
DBA (Grains)	29.20	.20	0.71%
Prices taken at previous day market close.			

Many macro factors are now out of the way and earnings season is starting to fade into the background. (Today is going to be very busy, but generally people have a decent feeling for results because they've been better than feared.) So, barring some major surprises, earnings shouldn't really influence the broad market too much going forward.

Instead, keep an eye on those momentum sectors. Sentiment and positioning remain the key to this market, and they are the proxies for that. And, if they are going to roll back over, it'll happen in here. More broadly, "good" sectors that offer value continue to trade well, and sector selection remains the best way to outperform this year.

Economics

New Home Sales

- New Home Sales in March fell to 384K (saar) vs. (E) 455K (saar).

Takeaway

The headline on new home sales was a big miss, dropping 14.5% from February levels and hitting an eight-month low. The big drop was partially offset by a positive 20K revision to both January and February data. But obviously, in the face of a 65K drop from February to March, that's not going to offset it.

But, for all the gnashing of teeth we saw on CNBC following the report, the number isn't quite as ominous as it seems.

First, new home sales are very volatile, so the drop isn't totally out of the ordinary. Second, the reason for the drop has to do with affordability, not overall housing demand. The median price for new homes rose to 290K (a record high) and that obviously reduced demand (just as it should). Low inventories also reduced sales, although the months' worth of supply rose to 6 months from 5 in February.

However, that was due to the drop in the pace of sales, not an increase in inventory. So, the big drop is more a function of a normally functioning housing market, not some huge drop in demand.

I'm not trying to say this report can be dismissed. But compared to pending or existing home sales, new home sales is much more important for homebuilders' profit outlook than it is representative of overall housing demand and the broad housing market.

Stocks did move on the release, and actually hit the lows of the day following the report, mostly due to initial "sticker shock" from the headline. But, the market recouped the losses within an hour of the release after that initial shock wore off.

Flash Manufacturing PMI

- April Manufacturing PMI was 55.4 vs. (E) 56.3.

Takeaway

National manufacturing activity in April was basically unchanged from March, but while the headline was a slight miss vs. expectations, the details of the report were pretty strong. New orders, the leading indicator of the report, rose to 58.9 from 58.1 in March, while output also rose to 58.2, both near highs for the recovery.

The important takeaway here is the March manufacturing PMI further confirms the recovery in the U.S. economy continues to progress, which is exactly what the market was looking for. Stocks didn't really react to the report, as it was basically in-line.

Commodities

Commodities markets were again a wash yesterday, as energy was weaker and industrial metals were higher. This left the benchmark commodity tracking index ETF, DBC, essentially unchanged. It was down 0.06%, lower by just 0.2% on the week.

Energy markets were lower yesterday following the EIA's bearish weekly inventory report, released mid-morning. WTI crude oil fell 0.25% yesterday. The recent trend of overall builds in crude oil supply (up 13 of the last 14 weeks)—but dips in Cushing, Okla., inventories (down 11 of last 12 weeks)—continued.

This is almost exclusively due to the southern leg of the Keystone XL pipeline coming online in the beginning of 2014. It sends crude oil from Cushing to storage facilities on the Gulf Coast. Just a reminder, Cushing is where the oil comes from to satisfy settled futures contracts on the New York Mercantile Exchange. So, although national supply levels are the highest since the EIA started collecting data in 1981, Cushing inventories are sitting at a four-year low, which traders see as supportive of futures prices, despite the "big-picture glut."

From a demand standpoint, economic data continues to favor the bulls, as more jobs equals more drivers (and more demand for gasoline). And, with the summer driving season around the corner, many analysts are calling for above-recent-average gasoline demand, which is obviously bullish for crude as well.

Also, the escalating situation in the Ukraine is helping to support prices thanks to the geopolitical fear bid that has returned to the market.

Bottom line is, there is currently a battle for control of the market going on between the "demand-bulls" and the "supply-bears," and futures are sitting on a technical "tipping point."

The 50-day moving average and a supporting technical uptrend line are within ticks of each other near $101.30. Whether or not that level holds (or breaks) in the next few sessions will likely decide where the price goes in coming weeks.

Market	Level	Change	% Change
Dollar Index	79.94	-.055	-0.07%
EUR/USD	1.3814	.0011	0.08%
GBP/USD	1.6778	-.0044	-0.26%
USD/JPY	102.47	-0.13	-0.13%
USD/CAD	1.103	.0007	0.06%
AUD/USD	.9284	-.0083	-0.89%
USD/BRL	2.2225	-.0147	-0.66%
10-year Yield	2.686	-.040	-1.47%
30-year Yield	3.469	-.034	-0.97%
Prices taken at previous day market close.			

Natural gas futures were also lower yesterday, falling by 0.1% ahead of the EIA report due out this morning (10:30 EDT). Analysts are expecting a 57 Bcf build in supplies. Natural gas remains comfortably above support at the 50-day moving average ($4.70). But, as has been the case for weeks, any big surprises on the headline number will materially move markets either through support, or up toward the $5 mark, with better chances for seeing the latter.

Gold futures were lower early yesterday morning but then caught a bid to close higher by 0.3% on the disappointing New Home Sales data. Rising tensions in the Ukraine are also lending support to gold, and I continue to recommend taking a shot on the long side here with a tight stop just below Tuesday's lows ($1,275/oz).

Currencies & Bonds

Currency markets traded with some volatility yesterday for the first time all week. Both the Dollar Index and euro ended basically flat, but that underscores the intraday volatility in both currencies.

The euro was the main driver of trading yesterday, as the policy outlook for the ECB trumped actual data. The euro was modestly higher vs. the dollar Wednesday morning, courtesy of the stronger-than-expected German and EU manufacturing PMIs. But, a Reuters report that implied the ECB may act if May HICP comes in light again weighed on the euro, and it closed only fractionally higher on the day.

The price action in the euro underscores the fact that the main concern in the euro isn't the economy anymore—it's dis-inflation and deflation. And, because we have a recovering economy amidst a potentially more accommodative central bank, the case for European equities continues to get stronger (VGK or FEZ).

The biggest mover in the currency markets yesterday was the Aussie dollar, which fell 0.8% after March inflation data missed analyst expectations. The Aussie traded back down through $0.93 vs. the dollar, but it's a little premature to say this counter-trend rally in the Aussie is over. I think a break of $0.91 vs. the dollar is needed to "press" Aussie shorts, despite the longer-term trend remaining lower.

Again, for those who can stomach it and be patient, selling the Aussie in the low- to mid-$0.90s (say above $0.93) remains one of the more fundamentally sound trades out there at the moment.

Staying in Asia, the yen rebounded yesterday but finished off its best levels of the session vs. the dollar. Traders continue to position in the yen ahead of a critical day next Wednesday, although the reason for the rally yesterday was a quasi-"hawkish" WSJ article and somewhat "hawkish" comments BOJ President Kuroda made yesterday.

The bottom line here is that, over the past few days, there have been strong implications that the government outlook on inflation (to be released Wednesday) is going to be higher-than-expected. That obviously reduces the need for more immediate stimulus. Whether that proves out remains to be seen, but it seems like there's a pretty blatant P.R. campaign designed to "talk up" the yen into the release next week, which could set up a potential "sell the news" reaction.

We're getting to a tipping point in this trade, clearly. But until the facts change and the BOJ proves it's unwilling to do more stimulus, the benefit of the doubt remains with the bears. I'm holding DXJ and could look to sell any rallies in the yen with a stop at the yearly highs (100.74).

Bonds were strong again yesterday, as they rallied off the economic data (which wasn't really disappointing, but this bond market remains strong so that was the excuse for the rally).

A Potentially Good Sign (I Hope).

I spoke earlier this week about potential money flows from Europe being the force behind this seemingly absurd bond strength (the other reason being a soon-to-falter economy). Last night we may have gotten some anecdotal evidence that there is a European influence in the bond market.

The 30-year Treasury & the Euro: Treasuries reversed and accelerated yesterday following the release of European data

The rally in the 30-year Treasury started last night at almost exactly 4:00 AM, right after the euro took a big leg higher following the release of the German manufacturing PMIs at 3:30 AM and the EU PMIs at 4:00 AM.

The PMIs on the surface were strong and would imply the ECB isn't going to ease any further. But, keep in mind this is about inflation, not economic growth. So, if we step back from the minutiae, clearly the ECB isn't raising rates anytime soon, regardless of the PMIs. The rally in Treasuries could have been money moving *back* into Treasuries following the report.

Also of note, the Treasury market hit its highs of the day right before 11:30 AM, which coincidentally is the European close. It's just one day, and certainly nothing conclusive. But the price action is notable, as nothing else was going on at 4 in the morning Wednesday to cause Treasuries to totally reverse earlier declines.

I obviously hope (for my short bond trade and all of our equity positions) that this bond strength is a result of European money flows—but I'm not "talking my book." The facts are the facts and it could go either way. But, yesterday did give me anecdotal hope that money from Europe is flowing into the long end, and that this bond strength is not some greater commentary on soon-to-be-slowing economic growth.

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**	**Neutral**	**Bullish**	*The S&P 500 saw a nice rebound last week off support at 1,815, and is now back in the middle of a month long trading range. Gradual economic improvement domestically and globally is a tailwind on stocks, and unless earnings season is very, very disappointing, the path of least resistance remains broadly higher.* *The S&P 500 remains in the 1,880-1,840 trading range.*

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) are now attractive, given positive fundamentals thanks to 1) high natural gas prices, 2) low inventories and 3) an attractive entry point due to the 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 it's 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 one of the last corners of value in the market, if the global recovery can accelerate.*

Trade Ideas

Gold: **The outlook for gold remains unclear, 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. I added a long gold trade Wednesday with a stop at $1,277 in futures or $123.11 in GLD.**

U.S. Dollar	**Neutral**	**Neutral**	**Neutral**	*The Dollar Index remains largely range-bound, as a stronger euro will hamper any ability for the U.S. 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."**

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 Treasuries) 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.**