7:00's Report

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

April 29th, 2014

Telecom: 2014 has been the year of the defensive sectors, so far. But, while utilities, REITs and consumer staples are at 52 week highs, telecom has lagged badly YTD.

Pre 7:00 Look

- Futures are higher this morning on earnings and follow through buying from yesterday's afternoon rebound. Geo-politically things were quiet o/n.
- Europe is modestly higher despite economic data o/n missing expectations (Europe is trading off earnings and M&A this morning).
- EU M3 money supply growth, Italian retail sales, European economic sentiment and UK Q1 GDP all slightly missed estimates (although nothing was too bad).
- Econ Today: Case-Shiller HPI (E: 0.7%).

Market	Level	Change	% Change
S&P 500 Futures	1872.25	6.25	.33%
U.S. Dollar (DXY)	79.715	-.052	-.07%
Gold	1290.40	-8.60	-.66%
WTI	101.24	.40	.40%
10-year	2.677	.011	0.41%

Equities

Market Recap

Stocks ended a volatile day modestly higher, as the market was able to rebound from another "momentum" sector sell off. The S&P 500 closed higher by .32%.

Stocks opened higher yesterday morning on positive M&A news (PFE/AZN) as well as reports that the sanctions issued against Russia were in line with expectations (and mostly ineffectual). Stocks then accelerated higher shortly after the open on the release of the Pending Home Sales report, which handily beat expectations and helped calm some nerves following last week's big miss in the New Home Sales report.

But, internet stocks, which have been the anchor on this market lately, were heavy all morning, and by mid-day the plunge in QNET again brought the entire market lower, and stocks hit their lows in the early afternoon down more than fifty basis points (QNET was down more than 2% at the lows yesterday).

But, the market showed some resiliency and support held at 1850 in the S&P 500 and the shorts began to cover, spurring a steep rally into the close. Stocks went out just ticks away from the highs of the day, in a victory for the bulls.

Trading Color

"Momentum" was the story of the day Monday as it sold off again yesterday and QNET actually made a new intraday low, as Internet stocks got walloped again (AMZN especially). On the bright side, however, both QNET and NBI finished well off the lows. More broadly, the Nasdaq and Russell 2000 were also down sharply intra-

Market	Level	Change	% Change
Dow	16448.74	87.28	.53%
TSX	14530.91	-2.66	-.02%
Brazil	51383.68	-15.67	-.03%
FTSE	6736.13	35.97	.54%
Nikkei	14288.23	-141.03	-.98%
Hang Seng	22453.89	321.36	1.45%
ASX	5486.58	-49.50	-.89%
Prices taken at previous day market close.			

day. (The Russell dropped nearly 2% and briefly broke through the 200-day moving average again, although it managed to close well off the lows.)

Market	Level	Change	% Change
DBC	26.44	-.13	-0.49%
Gold	1297.60	-3.20	-0.25%
Silver	19.55	-.141	-0.72%
Copper	3.0975	-.027	-0.86%
WTI	100.87	.27	0.27%
Brent	108.12	-1.46	-1.33%
Nat Gas	4.777	.119	2.55%
RBOB	3.0377	-.0374	-1.22%
DBA (Grains)	28.99	-.11	-0.39%
Prices taken at previous day market close.			

Outside of "momentum" trading lower, banks were the worst-performing sector in the S&P 500. That was largely due to the 6% drop in BAC following the reversal of its planned dividend increase and share buyback, following the math error that led to a change in its regulatory capital ratios. (Although, of note, it didn't alter the financial results. If this washout continues, I'd look to be a buyer.)

Sector-wise, the trend of defensive sector outperformance continued. Consumer staples rallied 1.2% (best performing S&P 500 sub-sector) while REITs, healthcare and industrials all relatively outperformed. Conversely, semiconductors, banks and consumer discretionary were the only S&P 500 sub-sectors to finish in the red (so again, not super-healthy sector trading).

From a volume and activity standpoint it wasn't exactly an encouraging day, as we didn't see volume move materially higher as stocks rebounded (the move off 1,850 was mostly short-covering once this support held).

On the charts the S&P 500 held support at the 1,850 level, and closed again near resistance at 1,880. But, the broader 1,880-1,840 range remains intact.

Is the Tech Sell Off Turning Into A Tech Rotation?

One bright spot I do want to mention was that "old/value" tech was again one of the star performers in the market yesterday as MSFT, ORCL, IBM and AAPL rallied more than 2%. This rotation out of "growth" tech (big data, social media, and Internet names) and into "old/value" tech continues. And, that's an important distinction to make. Three weeks ago when QNET and the internet/big data stocks went into free fall it took the entire tech sector and market with it. But, yesterday (and late last week) "old/value" tech was able to hold up, implying this phase of selling in the internet names is repositioning within tech, not just reduction of exposure, and that's an important and potentially bullish development.

The end of the month may be exacerbating this rotation as PMs dump the internet names post earnings. But, this rotation appears to be picking up steam and its something I think can last for a while longer.

Bottom Line

Around the world for sport again. This market remains frustratingly flat but having money in the right names/sectors continues to pay dividends, and that likely will continue for the foreseeable future.

1880-1840 remains the dominant range, and at some point the S&P 500 will break out of it, but it's going to take a change in the economic outlook (deviating from 3%) or a material earnings revision, neither which appear on the horizon at the moment.

Economics

Pending Home Sales Index

- March Pending Home Sales Index increased by 3.4% vs. (E) 0.6%.

Takeaway

After nine straight monthly declines, the Pending Home Sales Index reversed in the month of March, surging by 3.4% to 97.4. The headline was much better than analysts' expectations of a mere 0.6% rise. Also, February data was revised for the better, up to -0.5% from -0.8%. The stronger-than-expected data triggered a broad "risk on" move in the markets (stocks higher; Treasuries, gold and the yen lower). But that strength was clearly short-lived, as all of those moves were given back by late morning.

Bottom line here is that yesterday's Pending Home Sales data for the month of March was the first sign of strength we have seen in the housing market this year. Housing has been one of the key areas of concern in 2014, as it remained weak while most other economic indicators largely bounced back from the weather-driven weakness we saw this winter (namely manufacturing data). Also, it is worth noting that Pending Home Sales obviously "lead" New Home Sales, so yesterday's report eased some of the concerns over last week's disappointing New Home Sales report.

Commodities

Commodities were mostly lower yesterday with the notable exception of natural gas. The PowerShares DB Commodity Tracking Index ETF (DBC) fell 0.5% on the day.

WTI crude oil was higher by more than a dollar in early trading Monday as there was a broad "risk on" feel to the market. But, futures reversed shortly after the NYMEX open and traded into negative territory before finding support at the 200-day moving average ($100.62).

For now, the "supply bears" remain in control of the market, as traders are largely ignoring the geopolitical issues between the Ukraine and Russia, which was helping to support the price of WTI in recent weeks. On the charts, the 200-day moving average is the first line of support at $100.62/barrel. But it has been tested two days in a row now, and the technicals are indicating there is room to move lower. So, the benefit of the doubt remains with the bears in the near term, and the next key support level to watch is $99.15.

Brent futures were lower yesterday, down 1.33% thanks to some bearish supply news that Libya has ended suspensions of crude exports from several key terminals. While Libya still has a way to go before getting back to the pre-Qaddafi (February 2011) output levels of 1.6M barrels a day, the trend of higher output is gaining momentum, and that will continue to become a stronger bearish headwind on Brent Crude prices going forward.

Elsewhere in energy, natural gas futures were the best performer yesterday, moving sharply higher, up 2.55%. The jump in prices was a result of several things.

First, a national weather report was released showing that weather could be cooler than initially expected in the Midwest, and hotter than expected in California—both of which are triggers of higher energy demand.

Second, the "new" sanctions imposed on Russia include several energy companies and therefore have brought about a bit of a fear bid in the market.

And, lastly, there was renewed chatter regarding natural gas supply levels being near critical levels at an 11-year low, approximately 1 trillion cubic feet below the 5-year average. Bottom line is, futures are trading back toward the $5 mark and that remains supportive of the natural gas E&P ETFs XOP and FCG. On the charts, support lies below at the 50-day moving average ($4.68), while there is some resistance toward $4.90.

Copper fell 0.86% yesterday but continues to trade comfortably above support at the 50-day moving average ($3.07). Copper futures remain in a well-defined uptrend on the daily chart, but on a fundamental note, Chinese economic data due out overnight tonight could potentially move the market sharply.

Elsewhere in the metals, gold broke down through support at $1,300 upon release of the much better than expected pending home sale data, and is continuing to trade lower this morning ($1290 as of this writing). Gold continues to trade largely in this $1270—$1300 band. Fundamentally, the Commitments of Traders report released by the CFTC indicated a slight move higher in Net Longs held by money managers. Net longs increased by 4,116 to 77,106, which is neither bearish nor bullish, and I'd expect gold to continue to trade in the current range until we get more clarity in Ukraine and the economy (inflation).

Market	Level	Change	% Change
Dollar Index	79.79	-.028	-0.04%
EUR/USD	1.3849	.0018	0.13%
GBP/USD	1.6807	.0004	0.02%
USD/JPY	102.53	.38	0.37%
USD/CAD	1.1021	-.0016	-0.14%
AUD/USD	.9258	-.0017	-0.18%
USD/BRL	2.2235	-.021	-0.94%
10-year Yield	2.677	.011	0.41%
30-year Yield	3.459	.020	0.58%
Prices taken at previous day market close.			

Currencies & Bonds

Currency markets finished the day relatively flat after a day of positioning as currency traders look ahead to a plethora of data and economic events later this week. The dollar index closed down .04% ahead of the FOMC meeting which starts this morning.

The dollar sold off early yesterday morning because of strength in the Euro, but upon release of the stronger than expected Pending Home Sales Report, the dollar rallied back to nearly flat where it ended the day.

In Europe the Euro was up .23% also thanks to trader positioning ahead of the Eurozone HICP flash (their equivalent of our CPI report) due out early tomorrow morning.

In Asia, the Aussie was down .18% ahead of the Chinese Manufacturing PMI, scheduled to be released Wednesday night.

Meanwhile the yen was trading with almost perfect negative correlation to the U.S. stock market yesterday, closing lower by .34% (almost exactly opposite the .32% gain seen in the S&P on the day). Traders were looking ahead to the BOJ meeting announcement that will be released tomorrow morning. The consensus expectation is for no policy change, however the key focus will be on the semi-annual growth and inflation update.

I'd expect another day of treading water in the currency markets today ahead of the catalysts Wednesday.

Is The Bond Market Trading Off Housing?

Bonds sold off hard on the pending home sales beat, much more so than you would have expected. Bonds dropped 0.5% at the morning lows (after going into the release only fractionally lower).

That reaction is important to note because it implies the bond market remains unconvinced about the Fed's continued tapering, and may be more skeptical than most analysts. The reason I say that is because the recent weakness in housing (and really its inability to rebound from the winter dip like the rest of the economy) remains the doves' best hope for the Fed to suspend tapering of QE.

But, if housing shows signs of rebounding, then there really isn't much the doves can credibly point to that will make the Fed suspend the tapering of QE this year.

So, if Pending Home Sales is implying a spring rebound in housing, then based on yesterday's initial reaction, bonds will need to re-price the Fed outlook and sell off from current levels (assuming, of course, the stock market doesn't tank in the meantime).

So, bottom line is that *if* yesterday's moves in the bond market do reflect that bonds are trading more off housing than the broader economy, *then* if there is resumption of the recovery in the housing market, bonds are way expensive for the economic reality, and they'll have to decline sharply. It's not definitive yet, by any measure, but it's worth keeping an eye on.

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**	*Gradual economic improvement domestically and globally is a tailwind on stocks, and as earnings season has largely com in "ok," the path of least resistance remains broadly higher. But, "momentum" sectors remain under pressure and QNET and NBI need to be watched closely for signs of a potential breakdown.* *The S&P 500 remains in the 1880-1840 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 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, 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 $1277 in futures or $123.11 in GLD.**

	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**	*Bonds remain surprisingly buoyant despite economic data confirming the winter slowdown in the economy was temporary, while the Fed has confirmed it intends to continue tapering. The longer term trend remains lower, but the counter trend rally in bonds is continuing in the short/medium term.*

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.**