7:00's Report

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

April 3rd, 2014

Pre 7:00 Look

- Futures are flat while international markets are mixed after a busy night of data.
- China announced it will accelerate the construction of railways, providing some economic stimulus. But, this was largely expected and it is not the big "stimulus" announcement the market seems to be hoping for.
- Economically data was mixed o/n. China service PMIs beat estimates, while data from Europe was mixed (German and EU composite PMIs were basically in line).
- Econ Today: ECB Meeting (7:45), Press Conference (8:30). Weekly Jobless Claims (E: 320K), ISM Non-Manufacturing Index (E: 53.3).

Market	Level	Change	% Change
S&P 500 Futures	1885.25	2.00	0.11%
U.S. Dollar (DXY)	80.415	.043	0.05%
Gold	1286.90	-3.90	-0.30%
WTI	99.18	-.44	-.044%
10-year	2.803	.044	1.59%

Equities

Market Recap

Stocks extended the rally Wednesday, logging small gains in a quiet tape as everyone looked ahead to the two major catalysts for the week (ECB today and jobs report tomorrow). The S&P 500 rose 0.29%.

Stocks were mildly higher out of the gate Wednesday, helped by fresh "China stimulus" announcements and an in-line ADP employment report (although the revisions to last month were positive and big).

Comments by St. Louis Fed President James Bullard on Bloomberg Radio gave the market a boost midday when he said he thought inflation was "about to head higher." But, the comments weren't a major catalyst and, like Tuesday, stocks spent most of the afternoon meandering in quiet volume. Stocks sprinted higher into the close to again go out at the highs of the day (although that "sprint" came on non-existent volume and was more a factor of market-on-close "buy" orders and no offers than it was any panic buying into the close).

Trading Color

"Momentum" and growth sectors took a break yesterday but the market didn't mind all that much, which Is encouraging given the past two week. QNET and NBI were little-changed, while the Russell and Nasdaq traded in-line with the S&P and Dow Industrials.

Market leadership yesterday came instead from some of the recent laggards, as retail was the best-performing S&P 500 sub-sector. Industrials also traded higher while recent market "winners" paused (banks and semiconductors both finished mildly lower).

But, overall yesterday was a very slow, thin day, so there's not a lot to read into it from an internals standpoint, especially with the jobs number looming less than a day away.

On the charts the S&P 500 held the breakout above 1880, and it looks like unless we get a surprisingly bad jobs number, the S&P 500 will make a run at 1,900. Near term support sits at 1,880, 1,870 and 1,850.

Bottom Line

The grind higher continues, and it seems more "painful" than joyous. Once again, these new highs are being met with more disbelief and skepticism than celebration, and

Market	Level	Change	% Change
Dow	16,573.00	40.39	0.24%
TSX	14,459.11	123.80	0.86%
Brazil	51,701.05	1,430.68	2.85%
FTSE	6,649.81	-9.23	-0.14%
Nikkei	15,071.88	125.56	0.84%
Hang Seng	22,565.08	41.14	0.18%
ASX	5,409.89	6.59	0.12%
Prices taken at previous day market close.			

as a result in the short term the "pain trade" remains higher.

Perhaps the biggest positive influence on stocks yesterday was the sell-off in bonds, which are finally starting to confirm the "better economic growth/better business activity" story we've been hearing for a while. The jobs number obviously is a wild card, but if the 10-year yield continues to creep higher in an orderly fashion, that will be a tailwind for stocks (the key word there being "orderly").

Market	Level	Change	% Change
DBC	25.76	-.04	-0.16%
Gold	1291.20	11.20	0.88%
Silver	20.00	.312	1.58%
Copper	3.0395	.005	0.16%
WTI	99.67	-.07	-0.07%
Brent	104.82	-.80	-0.76%
Nat Gas	4.367	.091	2.13%
RBOB	2.8675	-.0022	-0.08%
DBA (Grains)	27.82	-.37	-1.31%
Prices taken at previous day market close.			

Jobs Report Preview

As is my normal process, I'm including the jobs report preview one day early, as I know not everyone can get to the Report before 8:30 EST each day.

The consensus expectation is for 195k jobs added, although given economic data and yesterday's ADP report, the "whisper number" has crept above 200k.

The "Too Hot" Scenario: >250K. Unlike last month's report, there is a bit of a short-term risk of a number that is "too good." A very strong jobs number may result in an acceleration of Fed tapering of QE and sooner-than-expected interest rate increases (maybe this year). That will cause a short-term negative reaction in most assets, as it simply isn't priced in at these levels.

If This Happens: Bonds and gold would sell off hard (maybe very hard); the dollar would rally very hard; and stocks would trade flat to down (although that dip would be a buying opportunity beyond the very short term as better growth is more bullish for stocks than Fed policy at this point).

The "Just Right" Scenario: 250K-150K. This is exactly what the market largely expects, and it wouldn't have any effect on perceived economic growth in '14 or on Fed policy (still a $10 billion taper per meeting and first rate increase in mid-'15).

If This Happens: The only thing that will likely trade off this result is bonds, which should see their recent sell-off accelerate. Commodities, the dollar and stocks likely won't react to a number in this range unless there is something odd in the revisions.

The "Too Cold" Scenario: <150K. "Whisper" numbers for this report have been creeping up all week (and ADP added some upward pressure to them yesterday), so a number below 150k here would be a big disappointment. While it won't by itself alter the outlook for growth and Fed policy, it will call into question the health of the economy, and that is definitely not priced into markets at these levels.

If This Happens: Stocks will sell off, potentially hard. The dollar will drop, while bonds and gold will rally (potentially hard).

Economics

ADP Employment Report

- Private Payrolls increased by 191K vs. (E) 193K in March
- Private Payrolls data for February was revised substantially higher from 139K to 178K

Takeaway

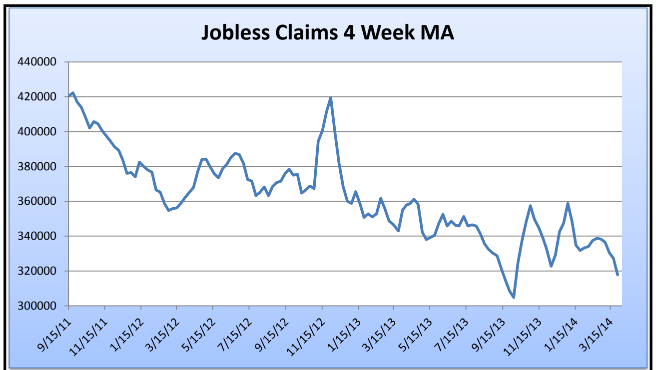
The ADP reported that private payrolls grew by 191K in the month of March, which was largely in-line with analyst expectations of 193K. Last month's data, however, was revised sharply higher from an initial reading of 139K up to 178K. With yesterday's headline matching expectations and the positive revisions to the February data, we can expect the "whisper number" for tomorrow's official government jobs number to be bumped slightly higher to somewhere between 205K and 215K.

Commodities

Commodities were mixed yesterday as copper continued to grind higher in step with the Chinese equity markets while there was weakness in the energy and grain markets. The benchmark commodity tracking index ETF (DBC) fell 0.16%.

Copper caught a big partially off the huge earthquake that hit Chile on Wednesday (Copper is the largest copper producing nation) although it's unclear at this point how much of an effect that will have on supply (initial estimates appear to imply not that much).

The big story in the commodity space remains copper as prices continue to show correlation with the Chinese economy and in turn, equity markets.



Weekly jobless claims are making multi-month lows and implying we are seeing improvement in the labor market.

Copper futures have been trending higher ever since falling to a multi-year low back in the middle of March. Yesterday morning, copper futures rallied to a 3-week high of $3.074, before short-term traders started to take some profits off the table. Despite the selling, futures closed higher by 0.16% and closed above the important $3.00 mark. We will continue to keep a close eye on both copper and Chinese economic data, as a potential long is becoming more attractive.

Moving to precious metals, gold futures bounced back yesterday, adding 0.88% to close at $1,291.20/oz. The move began pre-market as the sellers became short-term exhausted and a short-covering rally ensued, and the buying was fueled by Bullard's "inflation is about to head higher comments." But, despite the jump, futures mostly drifted sideways for the remainder of the day and gold is back below $1290 this morning, as selling pressure remains.

We don't expect any material moves before Friday's official jobs report other than some positioning. However, the number itself could spur a substantial move one way or another as all eyes (including HFTs/algos) will be on the release (as I said in the Jobs Report Preview, a "too hot" scenario could initiate substantial selling in gold, and vice versa). $1,300 was a pretty "magnetic" number in the fall of last year and it will be interesting to see if it has that effect as we begin the second quarter.

Market	Level	Change	% Change
Dollar Index	80.385	.136	0.17%
EUR/USD	1.3763	-.0029	-0.21%
GBP/USD	1.6626	-.0003	-0.02%
USD/JPY	103.78	.14	0.14%
USD/CAD	1.1027	.0006	0.05%
AUD/USD	.9240	-.0005	-0.05%
USD/BRL	2.2727	.0124	0.55%
10-year Yield	2.803	.044	1.59%
30-year Yield	36.49	.045	1.25%
Prices taken at previous day market close.			

Moving to energy, WTI crude oil futures traded down for the 3rd day in a row but were able to close well off the lows of the day. WTI slipped just 0.07% on the day. The inventory data released by the EIA were more-bullish than expected. Crude inventories fell for the first time in nearly 3 months, down 2.4M barrels versus analyst expectations that called for a 700K-barrel build. But, daily gyrations aside, the story remains the same though in WTI. Futures remain range-bound between $97-$105/barrel, and until we get a break of one of those levels, there's no real trend in WTI to trade at the moment.

Currencies & Bonds

Currency markets were quiet yesterday, and that's to be expected when we look at the next 48 hours. The Dollar Index was up small (0.15%) while the euro was off small (0.17%) thanks to positioning ahead of the ECB decision this morning (the ADP report didn't really move the dollar as it was mostly in-line).

The pound was flat as were the commodity currencies (Aussie and Loonie).

The one currency where there was something to talk about yesterday was the yen, which fell small (down 0.17%) but importantly traded to a 2+ month low vs. the dollar. The yen is threatening to break 104 vs. the dollar, thanks to the lower-than-expected inflation expectations from corporations contained in Tuesday's Tankan survey.

We all know the BOJ's target for inflation is 2.0%, but corporations in Japan saw multi-year inflation at just 1.7%, reflecting the fact that inflation expectations aren't rising like the BOJ wants. And, anecdotally, that increases the chances the BOJ will ease further sometime in the next few months.

Clearly there is some support for the yen at 104, though, because there were buyers there overnight. But, I continue to expect the BOJ to ease further, and for the "Short yen/Long DXJ" trade to be back "on" in the near future.

As a colleague (and subscriber) said to me in NYC last week, "I knew Abe and Kuroda were crazy when they started this, and I hope they aren't crazy enough to stop now." I don't think they are crazy enough to stop.

Treasuries saw decent declines yesterday, which made the equity bulls happy. The 30-year fell 0.5% and the 10-year dropped 0.37%, so the yield curve continued to steepen. And, the 10-year yield closed above 2.80% for the first time since late January. Unless we see a shockingly horrid jobs report tomorrow morning, I think we're going to see this bond decline/rise in rates begin to accelerate. The time to buy "value" in TBT/TBF/STPP and, to a point, KBE may be drawing thin.

ECB Preview

The big question for today's meeting is "Will the ECB ease policy further?" That's important because if they do, then that will cause an acceleration higher in European equities (which we would then want to buy).

The Street seems more divided on this than usual, but I think the consensus is for no policy changes from the ECB this morning. The flash HICP number from Monday certainly disappointed, but I doubt it's enough to get the ECB to ease policy further. Frankly, they don't really have any good tools to do so, unless they unleash QE or negative deposit rates (which, despite the rhetoric, are still a ways away, if they ever happen).

So, the ECB, to a point, is stuck. They are basically at the "lower bound" on interest rates (which is academic-speak for "They are at 0% already so they can't go any lower"). Any other measures taken (like some miniscule cut to interest rates of 10 basis points won't have any meaningful impact on reducing the threat from disinflation.

Given that, I think the dovish rhetoric campaign of the past week to 10 days was meant to potentially make dovish comments by Mario Draghi today more credible in an attempt to "verbally ease" policy. Point being, if Bundesbank President Jens Weidmann says that QE is a possibility, the market may be inclined to believe Draghi if he threatens it at the press conference later this morning.

So, expect a lot of dovish rhetoric and discussion about QE and negative deposit rates. But at the end of the day nothing will be done (most likely), and despite the dovish rhetoric, the euro most likely won't decline beyond a brief spike on some comments.

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 again traded to new highs this week as 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 is at new highs while support sits at 1870 and 1850.*

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

Neutral on all commodities currently.

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.**

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.**