7:00's Report

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

June 24th, 2014

Pre 7:00 Look

- Futures and most global markets are slightly weaker this morning as summer doldrums set in and everyone continues to digest the rally of the past month.
- In Iraq the situation remains the same. Kerry is calling for a new Iraqi government, but it is not clear that will really improve anything in the near term.
- Economically, the German IFO Business Climate Index was the only release, and it joined other recent German data in missing expectations (109.7 vs. (E) 110.4).
- Econ Today: New Home Sales (E: 441K). Fed Speak: Plosser (8:05 AM), Dudley (2:00 PM).

Market	Level	Change	% Change
S&P 500 Futures	1948.75	-4.25	-0.22%
U.S. Dollar (DXY)	80.285	-.053	-0.07%
Gold	1324.40	6.00	0.46%
WTI	106.24	.07	0.07%
10 Year	2.621	-.003	-0.11%

Equities

Stocks started the week flat in relatively quiet trading, as multiple news items Monday largely canceled each other out. The S&P 500 declined -0.01%.

Despite it being a pretty slow trading day, there were several pieces of information pushing and pulling on the market yesterday, but the net result was they offset each other. Positive flash manufacturing PMIs from Asia (specifically China) were offset by disappointing PMIs from Europe (mainly France). In Iraq, ISIS made gains over the weekend to control multiple border crossings

30 Year Treasury: The wait continues for us bond bears, as the long bond is trading worse and worse, but still hasn't broken the 2014 uptrend.

between Iraq and Syria and Iraq and Jordan. This is important because they can now more freely transport arms and people. But, despite their gains, they haven't moved any further south. Additionally, John Kerry is now in Baghdad (that's supposed to be a positive) and the hope is that he can help galvanize a united response from the Sunnis, Shiites, Iranians, etc. to halt the ISIS advance.

All these different events resulted in basically a flat open yesterday, at which point the market's focus turned toward the economic data (flash PMIs and existing home sales).

Despite the fact that both beat expectations and stocks rallied to the highs of the day off the news, the positive momentum couldn't be sustained. In what is now becoming a very familiar pattern, stocks sold off into the European close (at 11:30) before bottoming shortly thereafter at the lows of the day. (This exact trading pattern happened numerous times last week, so clearly there is some large money exiting the U.S. stock market and heading across the pond.)

The afternoon was quiet as focus again turned toward

Market	Level	Change	% Change
Dow	16937.26	-9.82	-0.06%
TSX	15105.63	-3.34	-0.02%
Brazil	54210.05	-428.14	-0.78%
FTSE	6780.90	-19.66	-0.29%
Nikkei	15376.24	6.96	0.05%
Hang Seng	22880.64	7583	0.33%
ASX	5432.78	-20.52	-0.38%
Prices taken at previous day market close.			

the World Cup, and stocks slowly drifted higher before closing flat in quiet trading.

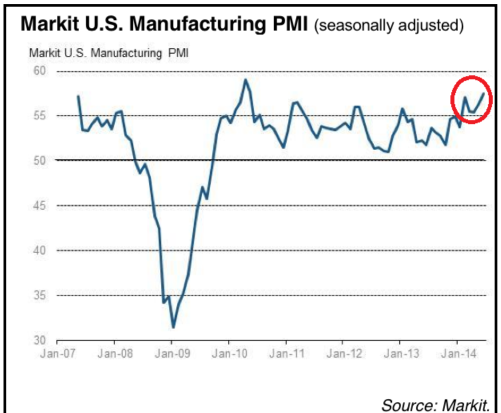
Trading Color

Most of the major indices were little-changed yesterday, although the Russell 2000 slightly underperformed (down -0.3%) on some profit-taking in biotech names. Markets seemed to be more in a mood to digest recent gains than attempt to extend the rally.

Market	Level	Change	% Change
DBC	26.82	-.10	-0.38%
Gold	1317.50	.90	0.07%
Silver	20.88	-.069	-0.33%
Copper	3.1445	.023	0.74%
WTI	106.10	-.73	-0.68%
Brent	114.02	-.79	-0.69%
Nat Gas	4.448	-.083	-1.83%
RBOB	3.1033	-.0244	-0.78%
DBA (Grains)	27.80	-.01	-0.04%
Prices taken at previous day market close.			

Tech outperformed (the Nasdaq finished very slightly positive) thanks in part to continued merger mania (ORCL bought MCRS for 5.3 billion). Energy also continued to trade well (XLE hit yet another 52-week high yesterday despite oil prices taking a breather).

More generally we did see some profit-taking in the defensive sectors as utilities (down -0.35%), healthcare (down -0.55%) and consumer staples (down -0.55%) were the only S&P 500 sub-sectors to decline other than industrials. But, after the recent run these defensive sectors have had, a little profit-taking is frankly healthy (and if I was heavy on these stocks, I'd be moving stops up).



The June Flash Manufacturing PMI rose to the highest level since May of 2010.

Bottom Line

Despite being a pretty sleepy day, there were some important takeaways from yesterday. First, the China data were better than the market's reaction to them, and the strong uptick in the PMIs all but confirms that Chinese economic growth has stabilized. That's important because it removes yet another potential macro headwind.

And, while the China bears will continue to warn of the impending collapse of the Chinese banking system (citing the copper lending news as the latest proof China is going to imminently collapse), the bottom line is (at least according to the data) the Chinese economy is stabilizing somewhere between 7% and 7.5% annual GDP growth. As long as that's the case, China won't be a destabilizing macro event.

Conversely, the market overreacted to the French June flash PMIs. Not to be cynical, but does anyone realistically expect the French to work in June? Seriously, though, it was a bad number but the bigger deal is that the ECB is fully engaged in trying to help the EMU economy. While France has its problems (many of which are structural) and Germany has seen some growth slow, the ECB is active and committed to being more active. So, I would view any further dip in European shares as a buying opportunity, especially for the PIIGS (EWP, EIRL, EWI).

Here in the U.S., focus continues to turn toward the Fed potentially being "behind the inflation curve" as there was an article in the WSJ about it and also in Business Insider. And, given the way the bond market has traded since the FOMC that's a legitimate concern, although it's still in the very early stages.

Bottom line is economic data continue to improve, and the market does need to consolidate. But unless we get a geopolitical shock that results in an oil price spike, or a disorderly rise in interest rates that stems from the market viewing the Fed as massively behind the curve, the path of least resistance for stocks is higher.

Economics

There were two important data points yesterday, June Flash Manufacturing PMI and Existing Home Sales, and both beat expectations and further implied the US economic recovery is accelerating.

Existing Home Sales

- Existing Home Sales in May increased to 4.89M vs. (E) 4.75M

Takeaway

We got another good housing data point yesterday, as May existing home sales were stronger than expected, jumping +4.9% to 4.89M. In addition to the headline being strong, there were positive revisions to the April reading. The details of the May report were also strong. (Single-family home sales increased +5.7% to 4.3M in May, accounting for the entire increase in the headline as the multi-family component was unchanged.)

Bottom line, this is another positive housing data point that implies housing is finally playing "catch-up" with the rest of the economy, which is a good thing.

Commodities

Commodities began the week mostly lower yesterday, led down by energy while copper handily outperformed the space. The benchmark commodity tracking index ETF, DBC, reversed sharply off of fresh 2014 highs yesterday, falling -0.4%.

Beginning with the outperformer, copper continued to quietly grind higher yesterday, adding +0.75% thanks to the better than expected Chinese flash PMI, which actually hit a 7-month high (50.8 vs. E 49.7). The increase in the flash PMI suggests the government's "mini-stimulus" programs are having a positive effect on the economy. An expanding Chinese economy is clearly bullish for copper as it is the largest global consumer of the industrial metal, accounting for 40% of total demand.

Looking to the charts, copper futures have recovered nearly all the losses that resulted from the "financing scare" in early June. They are now trading back above the original uptrend line that was supporting futures since the multi year lows were established back in March. Going forward, it appears we will see copper futures begin to trade as a proxy to the Chinese economy again. If data remain "good" to better than expected, then copper futures have room to extend recent gains. (Note: Copper has been up 7 straight sessions, so some profit-taking this week should not be alarming.) Technically speaking there is support between $3.10 and $3.12 again while resistance is above at $3.18.

Market	Level	Change	% Change
Dollar Index	80.35	-.091	-0.11%
EUR/USD	1.3602	.0003	0.02%
GBP/USD	1.7019	.0009	0.05%
USD/JPY	101.92	-.14	-0.14%
USD/CAD	1.0725	-.0032	-0.30%
AUD/USD	.9413	.0027	0.29%
USD/BRL	2.2165	-.012	-0.54%
10 Year Yield	2.621	-.003	-0.11%
30 Year Yield	3.448	-.004	-0.12%
Prices taken at previous day market close.			

Moving to the precious metals, trading in gold was very uneventful yesterday, as futures traded in a tight $5 range throughout the primary session. Now that gold traders are more heavily focused on inflation, we will likely see traders look ahead to the Core PCE reading due out in Thursday's Personal Income and Outlays report. And, as we mentioned yesterday, a higher than expected inflation reading could initiate another leg higher in gold. On the charts, the story remains the same: $1,300 is the first level of support (the 100-day moving average happens to be sitting just below) while $1,330 is resistance.

Moving to the energy space, natural gas was the worst performer yesterday, falling -1.83% for the 5th daily loss in a row. Natural gas was down thanks to some follow-through selling after the EIA reported the 6th consecutive weekly supply build of 100 Bcf or more. Initially during this build season, nat gas futures remained elevated because there was concern over the pace of supply builds being enough to satisfy next winter's demand. But the recent string of 100+ Bcf builds is helping ease those concerns, and we are seeing some longs unwind as a result. Mild extended-weather forecasts also added downward pressure on natural gas futures.

On the charts, natural gas futures are testing the lower end of the broad uptrend channel that has been in place now since early February (around the time the late-winter "froth" that sent prices over $6 began to come out of the market). The lower end of the trend channel remains support at $4.45, and that is a level to watch closely because a close below it would be a bearish technical sign.

Crude oil prices rallied on Friday as shorts closed positions going into the weekend, which almost always happens when there is an ongoing geopolitical conflict like Iraq. And yesterday, we saw some shorts return to the market combined with some longs taking profits. There were no material developments overseas, which caused a -0.7% drop in WTI futures.

Brent also traded down .7% yesterday as news of the resumption of Libyan oil shipments weighed on the oil markets. The amount exported (700k bbls Saturday and 600k bbls Sunday) aren't material (Libya used to produce 1.6 million barrels per day), but it does paint a potentially positive picture that shipments will continue to accelerate, and given the run we've seen on Iraq concern, it's not surprising the news led to a mild sell off yesterday.

For now, though, the oil market remains focused primarily on Iraq and the possibility of supply/production disruptions that could occur if ISIS is able to advance south (but chances of that are slim). On the charts, support is below at $105-$105.25 while resistance is above at $108.

Currencies & Bonds

The Dollar Index and euro traded opposite of their respective news yesterday, as the Dollar Index fell -0.13% despite good economic data, while the euro rose +0.07% despite disappointing economic data and dovish comments from ECB President Mario Draghi. He said he expects interest rates to stay at current levels for the next 2 ½ years. The counterintuitive performance more reflects the fact that 1) trading volumes were very low yesterday and 2) both currencies are still digesting the recent "dovish" moves by both the ECB and Fed.

Going forward we can probably expect more of a similar drift from the dollar and euro as the market digests dueling "easy" central banks – but if inflation pressures slowly continue to build and economic growth continues to accelerate, the dollar rally will resume, so I remain dollar-bullish. But, for now, we can expect a meandering drift.

In Asia things were much more logical: The Aussie dollar rallied +0.32% and was the best performer vs. the U.S. dollar yesterday, as stronger than expected flash Chinese manufacturing PMIs helped lift the "Aussie." Although the influence of Chinese economic growth on the Aussie has been reduced from recent years (when the Aussie traded as a proxy for the Chinese economy), there is still a heavy influence. Aussie is now back into resistance at $0.94 vs. the dollar, a level it's failed to break through three separate times. And, given the RBA's inclination to keep the Aussie low, I'd be selling at this level via futures or CROC (short Aussie dollar ETF).

Finally, the yen was up small after Japanese flash manufacturing PMIs increased more than expected (51.1 vs. 49.9), although it was mostly random trading noise and really the focus remains on the forthcoming details of Abe's "3rd Arrow" of structural financial reform. And, even though a formal announcement of the plans may come later this week (and likely will), the detail on the critical parts (the corporate tax cut and pension reallocations) may not be announced as they may still require political wrangling.

Regardless, the outlook for Japan and the yen remains unchanged: Either the economy and inflation accelerate (which is good for DXJ and bad for the yen), or they don't and the BOJ acts further to stimulate the economy (which will be good for DXJ and bad for the yen). I'm not saying it's a no-lose trade, as nothing ever is, but I continue to think money in DXJ and YCS remains relatively sheltered from any major disruptions, and worst-case scenarios are a likely continued churn.

Bonds closed flat yesterday as the drama surrounding whether this bond rally really is done played out for another day. Treasuries were stronger yesterday despite Wilbur Ross' warnings that sovereign debt was the "ultimate bubble." But, despite their gains, bonds again didn't trade very well. The 30-year Treasury opened basically on the highs of the day and bled steadily lower, closing virtually on the lows.

Once again the bond market ignored the strong economic data (flash manufacturing PMIs and existing home sales) as bonds didn't really sell off on either release. But, there was clearly constant selling pressure throughout the day, and bonds drifted consistently lower throughout the trading session.

For what was now the 5th day in a row, the 30-year continued to test the 2014 uptrend. But as has been the case despite trading poorly, it remains above critical support. Until that trend line is broken, the uptrend, while weakening, remains intact.

Have a good day, Tom

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Position Sheet

Tactical Trading/Investment Account (Time frame of a few weeks to months).

Date	Position	Open Price	Stop	Strategy
6/11/14	VGK EWP EIRL EWI	61.24 43.58 37.42 18.14	60.58 42.22 35.41 16.89	*Long Europe. Part of the "Post ECB Decision" portfolio of what should outperform if bond rally is done. Original Issue*
6/11/14	SPHB KBE	32.73 33.40	30.32 31.97	*Long domestic cyclicals. Part of the "Post ECB Decision" portfolio of what should outperform if bond rally is done. Original Issue*
6/11/14	UUP EUO	21.55 17.46	21.13 17.13	*Long Dollar. Part of the "Post ECB Decision" portfolio of what should outperform if bond rally is done. Original Issue*
6/11/14	TBT STPP REK	63.41 38.32 23.00	59.53 36.83 22.33	*Short Bonds. Part of the "Post ECB Decision" portfolio of what should outperform if bond rally is done. Original Issue*
4/30/14	IYZ	28.99	28.32	*Telecom trading at a value to the market, has lagged other safety sectors. Original Issue*
3/3/14	XLI IYM PICK DIA	52.19 83.06 19.48 164.28	None	*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. Original Issue*
12/13/13	FCG XOP	18.97 65.62	None	*Natural gas supplies low, increased demand, E&Ps at a value. Original Issue.*

Longer Term Macro-Trend Investment Account (Long term time frame of months/quarters).

Date Initiated	Strategy	Position (s)	Investment Thesis
November 2012	**Long Japan**	**DXJ/YCS**	*The election of Prime Minster Abe in late 2012 resulted in massive monetary and fiscal stimulus designed to break Japan out of decades long deflation and stagnation. The resulting efforts will be yen negative/Japanese stock spositive for yeasr to come.*
Strategy Update (6/4/14): Focus on this trade has shifted to Abe's "3rd Arrow" of fiscal reforms, and if enacted, it could lead to a material decline in the yen/rally in DXJ.			
April 2013	**Short Bonds**	**TBT/TBF/ STPP/KBE**	*The 30 year bull market in bonds is over, as the Fed begins to gradually remove stimulus, the economy recovers, and inflation slowly begins to increase.*
Strategy Update (6/5/14): The ECB decision to stimulate the EU economy should end the massive inflow of foreign money into Treasuries, which should result in a gradual resumption of the decline in bonds/rise in yields.			

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Asset Class Dashboard

(Updated 6.23.14)

This page is meant to provide a general outlook for the path of each major asset class and is updated at the start of each week.

Near Term Trends are provided primarily for tactical and trading accounts (Time Horizon of weeks and months).

Long Term Trend is provided for longer term asset allocation models/retirement accounts (Time Horizon of Months/Quarters).

The "Best Idea" represents our best idea at the moment. Not all best ideas are trades we make—they are provided for idea generation.

	Near Term Trend	Long Term Trend	Market Intelligence
Stocks	**Higher but slightly Overbought**	**Bullish**	*The S&P 500 traded to new highs again last week after a "dovish" Fed ignited a broad rally. Generally the outlook for stocks remains positive, as global central banks remain accommodative, valuations are stretched but not expensive, and the global recovery is ongoing. Sentiment is getting a touch too bullish, but beyond the very short term things look good for stocks.*

Best Idea: Long Europe (VGK/EIRL/EWP/EWI)

Best Contrarian Idea: Buy Retailers (XRT)

Commodities	**Neutral**	**Neutral**	*Gold jumped back above $1300 on rising inflation expectations and a dovish Fed, while Iraq uncertainty kept a bid under WTI Crude. Commodities generally benefitted from a shift in focus from economic growth to inflation, and if that continues, it could be a positive for the entire commodity complex.*

Best Idea: Long Oil (USO)

Best Contrarian Idea: Buy Gold (GLD)

U.S. Dollar	**Neutral**	**Bullish**	*The Dollar Index declined last week thanks to the dovish FOMC, and given their apparent increased tolerance for higher interest rates, the outlook for the dollar has become more neutral in the short term.*

Best Idea: Buy the Pound (FXB).

Best Contrarian Idea: Long Canadian Dollar (FXC)

Treasuries	**Neutral**	**Bearish**	*Treasuries have traded heavier since the ECB decision two weeks ago, and there are signs that the influx of foreign capital is ending, which should be bond bearish. But, the uptrend in place since January again held last week, so until 135'07 is broken in the 30 year, the shorter term trend remains higher.*

Best Idea: Short long bonds (TBT)

Best Contrarian Idea: Short High Yield Bonds (SJB)