7:00's Report

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

August 19th, 2014

Nasdaq has totally recouped all the July/August losses and hit a new high for 2014 yesterday (which is also a 14 year high inching closer towards 5000).

Pre 7:00 Look

- Futures are little changed while international markets were mostly higher o/n, rallying in sympathy with the US.
- Economically the only material release was Great Britain July CPI, which declined more than expected (-0.3% vs. (E) -0.2%). That further reduced "hawkish" expectations on the BOE and the pound is down nearly .5% this morning.
- Geo-politically it was another quiet night as there have been no new developments in Ukraine while Kurdish fighters continue to make progress vs. IS in Iraq (a positive).
- Econ Today: CPI (E: 0.1%), Housing Starts (E: 963K).

Market	Level	Change	% Change
S&P 500 Futures	1969.75	2.25	0.11%
U.S. Dollar (DXY)	81.75	.119	0.15%
Gold	1301.30	2.00	0.15%
WTI	94.11	.36	0.38%
10 Year	2.387	.042	1.79%

Equities

Market Recap

Last week's rally continued on Monday, as stocks traded to three-week highs on the back of growing expectations of the "dovish" Yellen at the Jackson Hole conference, a further reduction in geopolitical stresses and more mergers. The S&P 500 rose +0.85%.

Stocks were higher from the outset Monday, as positive geopolitical news over the weekend led to higher markets in Asia and Europe. From an "event" standpoint, further progress of the Ukrainian military and news of cease-fire talks helped the bulls, as did a better than expected Housing Market Index report. Finally, on the micro front, there is now a bidding war for Family Dollar (FDO), as Dollar General (DG) bid $78.50 for the shares Monday, trumping Dollar Tree's (DLTR) $74.50.

Stocks opened sharply higher and stayed there the entire day, as the S&P 500 traded in a small 4-point range basically from 10:30 till the end of the day. This implies we saw some covering and chasing right at the open, but buyers aren't willing to chase the market materially higher unless we get some new, positive news.

The late morning and afternoon were quiet with no new events in Russia/Ukraine or Iraq, and it was a pretty slow trading session after lunch. The market caught a little bit of a bid into the bell and closed just off the best levels of the day.

Trading Color

It was a broad, cyclicals-led rally yesterday. The Russell 2000 continued to play catch-up, rallying +1.5%, nearly double the S&P 500. Meanwhile, the Nasdaq moved to a

Market	Level	Change	% Change
Dow	16838.74	175.83	1.06%
TSX	15338.47	34.23	0.22%
Brazil	57560.72	597.07	1.05%
FTSE	6770.71	29.46	0.44%
Nikkei	15449.79	127.19	0.83%
Hang Seng	25122.95	167.49	0.67%
ASX	5623.78	36.68	0.66%
Prices taken at previous day market close.			

new high for the year (which, incidentally is also a 14-year high). Sector-wise, there was cyclical outperformance but also a bit of a "higher rate" trade as financials and banks particularly outperformed on the sell-off in bonds, while utilities were the only S&P 500 sector to finish negative on the day, and broadly they continue to trade poorly. Consumer discretionary, basic materials, tech and industrials were all the outperformers, so you don't get more cyclical than that.

Market	Level	Change	% Change
DBC	24.74	-.20	-0.80%
Gold	1300.20	-6.00	-0.46%
Silver	19.65	.125	0.64%
Copper	3.1095	.0065	0.21%
WTI	93.75	-1.57	-1.65%
Brent	101.66	-1.87	-1.81%
Nat Gas	3.792	.016	0.42%
RBOB	2.6565	-.0421	-1.56%
DBA (Grains)	26.21	-.06	-0.21%

Prices taken at previous day market close.

Regional banks, which I continue to be a bull on, also traded well yesterday, rallying +1.7% and appearing to have decisively broken a downtrend line in place since the early July highs. With so much Fed communication coming later this week (minutes and Jackson Hole), there's risk of volatility. But more broadly I think that regional banks continue to offer value here if you want exposure to a sector that can profit from rising rates and a recovering economy (whenever the former actually comes). In the meantime you're buying a "beat up" space, so there's some value protection.

KRE (Regional Bank ETF): The ETF rode resistance on a long standing uptrend line the last 2 weeks, and appears to be trying to break out, back above the technical level.

Finally, it's going to be a big week for retailers. It started with a bang with the DG/DLTR/FDO news yesterday, but there are a lot of retailer earnings coming later this week. Watch RTH (the retailer ETF). This remains a sector that is broadly underweight on the Street, and if it can break above $61.00, it'll be at the highs for the year, and we could see some chasing/short-covering.

Bottom Line

This market remains all about the Fed, and positioning has been the main driver of stocks the last 3+ weeks, not geopolitics. The market simply got too negative and pessimistic about the future "hawkishness" of the Fed, and the soft data from last week and other events caught investors off-guard. Over the last few trading sessions, investors have chased to re-apply long exposure.

But, the easy lifting is over, as sentiment is much more balanced and we're into some actual "hard" data that will shape the Fed outlook going forward.

I would be surprised if markets can move materially higher through resistance at 1,985 unless we get some more "Goldilocks" data (starting with today's CPI) or the FOMC minutes are more dovish than expected. So, while I remain a bull, I'm not sure this 6-week correction (which really started 7/2) is over just yet.

Economics

There were no economic reports yesterday.

Commodities

Commodities were mixed yesterday as crude oil again traded lower, gold slipped as traders positioned ahead of data, while natural gas and the industrial metals rallied. The benchmark commodity tracking index ETF, DBC, fell -0.86% as a result of the heavy weight that energy carries in the index (namely Brent and WTI crude contracts).

The sellers maintained the momentum in the energy sector as Brent and WTI crude oil prices fell -1.8% and -1.55%, respectively. The primary reasons behind the continued weakness include the ongoing improvements in multiple geopolitical conflicts (namely Iraq), as well as reports that Libya is set to begin exports out of its largest oil port (Es Sider) after a year of being inactive.

The Libyan bearish supply news comes after shipments resumed out of Ras Lanuf last week, which is another key port for oil exports and obviously also bearish for global crude prices.

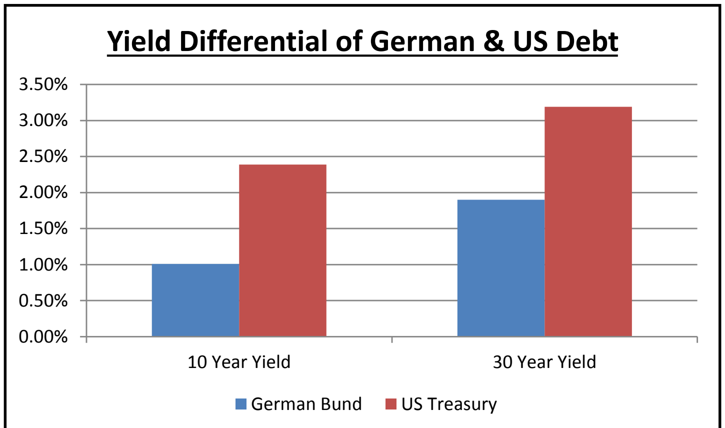
Lastly, disappointing economic data have driven a lot of the speculative buyers from the market as they question the potential for less demand going forward as economic growth may be slowing. So, the threat of higher supply and doubts about demand should be a near term negative on prices, and indeed they are.

Looking specifically at the WTI contract, however, there was some bullish, supply-side news yesterday (even though it wouldn't appear that way on the charts). News broke that domestic crude oil supplies may be set to fall this week by more than is normal for this time of year, as offloading of imported crude shipments may be interrupted at the Louisiana Offshore Oil Port due to a leak. The "LOOP" accepts roughly 16% of all U.S. imports, so a disruption in operations would in turn lead refiners—which are currently operating at over 94% capacity—to resort to drawing oil from stored supplies to satisfy refined product demand.

Short term implications aside, though, the sharp downtrend that has been in place since mid-June needs to break before we get outright bullish on oil. But, based on the greater trend in global data, the world economies remain relatively healthy and the recovery is ongoing. So, unless we see a continuation of the very recent economic weakness, crude oil is a value at these levels.

Natural gas was among the best-performing commodities yesterday, with futures rising +0.42% on the session. The move higher came in spite of weather reports that continue to suggest temperatures will be milder than initially thought (which was part of the reason prices rallied above the $4 mark last week) as people are beginning to focus more on the inventory situation (which remains bullish longer term).

Moving to the metals, industrials traded well yesterday as copper added +0.21% while silver gained +0.6%. But the real focus in the metals market this week is gold as traders await important catalysts. It fell below $1300/oz. yesterday and it sitting on that level this morning, but the upcoming CPI/Fed Minutes and Yellen Jackson Hole speech will be the next major catalysts. Broadly, support sits at $1295ish/oz. while major resistance is around $1330ish, and one of those two levels will need to be decisively broken to end this two month long chop in gold.



Bonds: It's pretty simple. Until yields in German bunds start to move higher, it'll be very difficult for Treasuries to materially decline because they are just too attractive on a risk/reward basis compared to German debt.

Currencies & Bonds

Treasuries traded lower yesterday and the yield curve steepened as the 30-year fell -0.62% while the 10-year was down -0.23% with a yield of 2.387%. Bonds were lower as a part of a general "risk on" move in the markets yesterday (ex-oil, which remains in a sharp downtrend). It was a combination of easing geopolitics, namely the progress being made in the Ukraine but also Iraq supported the "risk on" play.

High-yield bonds rallied yesterday, leading the ETF JNK to rise a notable +0.32% as the appetite for risk returned to the market. JNK is now sitting comfortably above the $41 mark, which we pointed out two weeks ago would be an indication that the rally in equities would likely resume. Taking a closer look, JNK closed above $41 on the 13th, which was the day before the S&P 500 broke out above technical resistance at 1,950. Going forward JNK will continue to be a key leading indicator for the market as we approach the next "tipping point"

Market	Level	Change	% Change
Dollar Index	81.63	.161	0.20%
EUR/USD	1.3361	-.0037	-0.28%
GBP/USD	1.6727	.0033	0.20%
USD/JPY	102.54	.20	0.20%
USD/CAD	1.0884	-.0009	-0.08%
AUD/USD	.9320	.0004	0.04%
USD/BRL	2.2584	-.0009	-0.04%
10 Year Yield	2.387	.042	1.79%
30 Year Yield	3.194	.059	1.88%

Prices taken at previous day market close.

this week with the FOMC minutes and Yellen's speech in focus.

The Dollar Index started the week higher, rising +0.2% Monday, although most of that rally came as a result of a decline in the euro, as opposed to anything dollar-bullish (the Housing Market Index didn't really pull in any buyers).

Starting with the euro, the main negative catalyst yesterday came via comments from the Bundesbank. The German central bank voiced concern about the negative influence of Russian sanctions on the German economy, specifically exports. Other than the obvious, that sanctions reduce economic activity, the warning was important for two reasons.

First, as Germany goes, so goes the EU (to a large degree). If the German economy really begins to gather downside momentum, that's a major negative for the EU economy as a whole. Second, the Bundesbank (and the German contingent more broadly) is an impediment to the ECB following the other major developed-market central banks (Fed, BOE, BOJ) in enacting some sort of QE. So, if the ECB is ever actually going to do QE, then they will need the Bundesbank to sign off on it. That didn't happen yesterday, but common sense tells us if they are starting to sound the alarm about the German economy, they would likely be more open to QE.

Regardless, near-term focus now shifts the TLTRO (Targeted Long-Term Refinance Operation). I'll cover this more as we get closer to the launch date, but basically this is a way for the ECB to pump liquidity into the EU economy and ensure it goes to businesses, and doesn't sit on bank balance sheets (like happened initially here in the U.S. with QE).

Focus will soon turn to how much of the allotted amount banks borrow from the ECB, and we've already had conflicting reports. (MS had a report out that said there would be strong demand especially from PIIGS banks. Meanwhile economists surveyed by Bloomberg reduced their total they think will be borrowed compared to last month.)

Regardless, the next major talking point for the EU economy is the implementation of these TLTROs, which should theoretically help jumpstart the EU economy. But, the market wants QE in the EU, so even when these TLTROs start being offered (and it'll take several months or quarters for the positive effects to show up), we can expect continued calls for QE in the EU.

Staying in Europe, the pound rallied +0.19% yesterday thanks to some "hawkish" comments from BOE Governor Marc Carney during an interview that appeared in the Sunday Times. Basically Carney said interest rates would likely need to rise before wages fully recovered from the financial crisis. While that touches a nerve (wage inflation) with the market, he didn't say anything material. The fact that the pound was up just +0.19% after the beating it took last week tells me the market outlook for the BOE, which got more dovish last week, hasn't changed.

Looking at Asia, the yen declined -0.2% in mostly quiet trading, and the dollar/yen pair is creeping toward the upper end of the recent trading range (101-103). The yen remains broadly stalemated in that range for now, and will continue to remain that way until one of three things happens: 1. The BOJ enacts more stimulus (unlikely at this point), 2. PM Shinzo Abe pushes through more pro-business structural reforms (unlikely), or 3. We finally get some clarity on the changes to pension fund allocations, which would see funds move out of Japanese government bonds (yen-negative) and into Japanese and foreign stocks.

That third one is the likeliest to occur in the fall, and it's the next catalyst to watch for in this trade. Until then, more patience is required.

Have a good day,

Tom

7:00's REPORT

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

Position Sheet

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

Date	Position	Open Price	Stop	Strategy
7/28/14	DBC	25.65	None	*We are going to look to initiate long positions in DBC here as a low risk-high reward opportunity has presented itself. In DBC, support has formed at $25.50 while potential target to the upside is close to the $27 mark. So, you will be risking about 20 cents for a potential return of $2 dollars. Original Issue*
7/21/14	UNG	20.98	None	*We are replacing the "long copper" trade on the tactical sheet with our "long natural gas" call because of the time frames of the two trades. Copper is a long term fundamental play dependent on continued global economic growth (namely in China) while buying nat gas is a medium term trade based on smaller supply injections and warming weather patterns. "Long Copper" has been moved to the ACD. Original Issue.*
6/11/14	SPHB	32.73	30.32	*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	21.55	21.13	*Long Dollar. 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 positive for years 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 (7/21/14): Geo-political concerns and foreign money flows sent bonds to new highs for the year last week, and the gap between deteriorating fundamentals and price action is widening. For now, though, the trend is higher and more patience is required in this long term trade.			

7:00's REPORT

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

Asset Class Dashboard

(Updated 8.18.14)

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

Date	Position	Open Price	Stop	Strategy
7/28/14	DBC	25.65	None	*We are going to look to initiate long positions in DBC here as a low risk-high reward opportunity has presented itself. In DBC, support has formed at $25.50 while potential target to the upside is close to the $27 mark. So, you will be risking about 20 cents for a potential return of $2 dollars. Original Issue*
7/21/14	UNG	20.98	None	*We are replacing the "long copper" trade on the tactical sheet with our "long natural gas" call because of the time frames of the two trades. Copper is a long term fundamental play dependent on continued global economic growth (namely in China) while buying nat gas is a medium term trade based on smaller supply injections and warming weather patterns. "Long Copper" has been moved to the ACD. Original Issue.*
6/11/14	SPHB	32.73	30.32	*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	21.55	21.13	*Long Dollar. 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 positive for years 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 (7/21/14): Geo-political concerns and foreign money flows sent bonds to new highs for the year last week, and the gap between deteriorating fundamentals and price action is widening. For now, though, the trend is higher and more patience is required in this long term trade.			