7:00's Report

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

August 26th, 2014

Pre 7:00 Look

- Futures are flat and most int'l markets are lower this morning as geopolitics weigh on sentiment. The notable exception is the FTSE which is "playing catch up" to yesterday's global rally after being closed for a bank holiday.
- There were no global economic reports released o/n.
- Geopolitically, Ukraine reportedly captured Russian soldiers on its territory just hours before Putin and Poroshenko were scheduled to meet which will obviously weigh on expectations for any progress to come from the talks.
- Econ Today: Durable Goods Orders (E: 5.1%)

Market	Level	Change	% Change
S&P 500 Futures	1997.50	2.50	0.13%
U.S. Dollar (DXY)	82.56	-.033	-0.04%
Gold	1288.40	9.50	0.74%
WTI	93.60	.25	0.27%
10 Year	2.387	-.016	-0.67%

Equities

Market Recap

Stocks rallied to fresh all-time highs yesterday on European stimulus speculation. The S&P 500 gained +0.48% to close just shy of the milestone 2,000 mark.

Stocks opened slightly higher and proceeded to rally out of the gate yesterday as global shares were mostly higher overnight on Mario Draghi's dovish comments from late last week. Also the geopolitical backdrop remained largely static, which helped stocks move higher. After the initial "pop" the S&P steadily drifted higher over the

The S&P 500 traded through the 2,000 mark yesterday, a new intraday high.

course of the morning and broke through the 2,000 level for the first time in history by midmorning. But the bulls ran out of steam and the rally stalled with stocks hovering just above 2,000 through lunchtime. Then, as we entered the second half of the session, there was some short-term profit-taking (probably driven by fast-money funds and day traders), but the selling was light and stocks closed quietly, just below the milestone at 1,998.

Trading Color

Yesterday's rally to fresh all-time highs was broad as every sub-sector of the S&P 500 closed higher. But both the Nasdaq and Russell 2000 underperformed, albeit only slightly as the respective indexes added +0.41% and +0.42% compared to the S&P's gains of +0.48%. We did however see outperformance by SPHB (+0.68%) vs. SPLV (+0.46%), so some appetite for risk in the market was encouraging to see.

Sector performance was a bit of a mixed bag as energy, financials, utilities and healthcare all outperformed, while industrials, consumer discretionary and tech were

Market	Level	Change	% Change
Dow	17,076.87	75.65	0.44%
TSX	15,598.74	63.19	0.41%
Brazil	59,735.17	1,327.85	2.27%
FTSE	6,786.82	11.57	0.17%
Nikkei	15,521.22	-92.03	-0.59%
Hang Seng	25,074.50	-92.41	-0.37%
ASX	5,637.62	2.74	0.05%
Prices taken at previous day market close.			

among the worst performers. So, not exactly the cyclical outperformance you would like to see on day of new all-time highs, but it was a new all-time high after all, so I guess we can't complain.

Bottom Line

Looking at the European news headlines yesterday—which included the resignation of the French government, another apparent invasion attempt of the Ukraine by Russia, as well as a 4th consecutive "miss" in the well-followed German IFO survey (106.3 vs E: 107)—you would have expected to see substantial losses in global equities, namely in Europe. But, that was not the case as the DAX in Germany rose +1.83% while the French CAC rose +2.1% in spite of the weak economic data and political drama, respectively. (Note: Later in the session the "political drama" was perceived as a market positive, as investors saw the move as a step in the right direction.)

Market	Level	Change	% Change
DBC	24.895	.025	0.10%
Gold	1279.00	-1.20	-0.09%
Silver	19.36	-.026	-0.13%
Copper	3.2215	.017	0.53%
WTI	93.31	-.34	-0.36%
Brent	102.66	.37	0.36%
Nat Gas	3.936	.096	2.50%
RBOB	2.7534	.015	0.55%
DBA (Grains)	25.85	-.08	-0.31%
Prices taken at previous day market close.			

German bunds and most European equities rallied yesterday (the FTSE in England was closed for a bank holiday) as investors continued to focus on and digest Mario Draghi's speech from Jackson Hole last week. Draghi's comments raised expectations that the ECB was prepared to take further steps (such as outright QE) to ease policy further and get the European economy expanding again. More specifically, Draghi was quoted as saying the ECB was "prepared to respond with *all* of its available tools, should inflation drop further." And, the comments were interpreted by most to mean some sort of QE program.

So, the real reason stocks were higher yesterday was again because of central bank policy speculation. This time, it was Draghi's late-afternoon comments on Friday that drove international markets higher on Monday, and U.S. stocks followed suit.

Bottom line is international markets remain largely fixated on central banks, and as a result sentiment and trader positioning/speculation are still the primary drivers of the market.

Economics

New Home Sales

- New Home Sales for July fell 2.4% to 412K SAAR vs. (E) 430K.

Takeaway

New home sales slipped -2.4% in July to an annualized rate of 412K vs. (E) 430K. But, the disappointment in the headline was offset by the details of the report, namely the revisions to prior months. The headline figure for June was encouragingly revised up to 422K from an initial read of 406K while the May data were also revised higher. Tight supplies and high prices have been weighing on home sales so far this year; however the July report showed some relief in those metrics. Monthly supply grew to 6.0 from 5.6 in June and the median home price fell back 3.7% month-over-month.

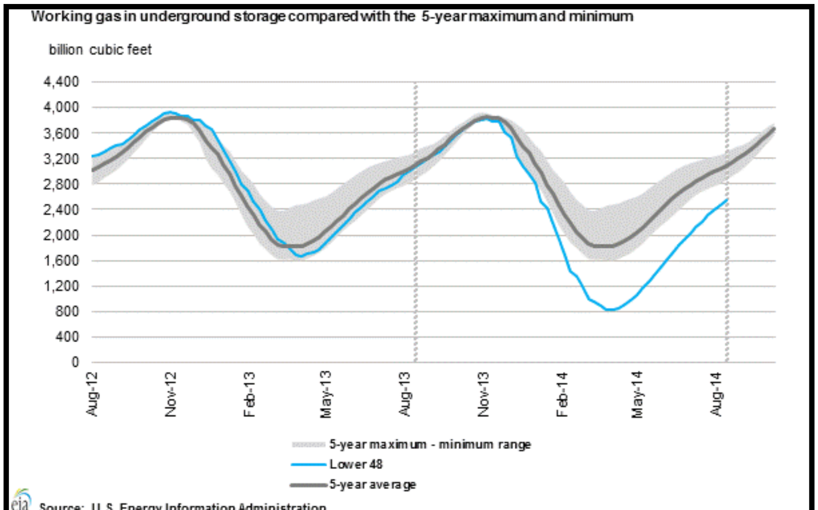
Shortly after the release of the relatively "Goldilocks" report, the S&P 500 traded up through the 2,000 mark for the first time ever. Bottom line, the report was good and helped reassure investors that the housing market is "ok," although it certainly remains an area that needs to be watched as housing has been one of the weakest components to the economic recovery.

Commodities

Commodities were mixed in quiet trading to start the week yesterday. Natural gas was the notable outperformer, up over +2% on warmer weather forecasts while most other commodities finished the day within 0.3 percentage points of where they opened. The broad-based commodity tracking index ETF, DBC, added .10% on the day.

Beginning with the best performer, natural gas made a run toward the $4 mark yesterday as futures gained +2.5% to close comfortably above $3.90 for the first time in two weeks. The move higher was mostly a result of updated weather forecasts that suggested temperatures will likely be warmer than initially thought over the next two weeks.

Over the near term, weather will continue to be the primary influence in the natural gas market, with low supply levels remaining a concern as we quickly approach the draw season. Nat gas stocks are currently sitting 17.3% below the 5-year average, and in order to make it to the levels seen as "normal" or "healthy" for entering the draw season (3.8 trillion Bcf), we would need to see an average weekly build of roughly 124.5 Bcf (the rolling 4-week moving average is currently +84 Bcf). So, bottom line, if we are going to see warmer than average temperatures potentially extending into September, which will restrict supply builds as energy demand rises, the path of least resistance remains higher in nat gas futures.



Natural Gas Stocks Remain Well Below the 5-Yr Avg. And, With Warm Weather on the Way, Supply Builds May be Limited in Coming Weeks.

Elsewhere in energy, crude oil futures chopped sideways in a narrow 90-cent range yesterday, closing down just -0.31%. There are several geopolitical situations that traders are eyeing at the moment. These include the ongoing conflict in Iraq, as well as news out of Libya that the Tripoli airport was seized by Islamist militias. But, futures showed little reaction to either situation as production capabilities are not in immediate jeopardy at this time.

Going forward we will look to the charts for direction as WTI is approaching a "tipping point" on the daily time frame. In the bulls' favor, there was a bullish outside reversal on Thursday last week and $93 has proven to be fairly solid support since the October contract became the "active" contract last week.

Market	Level	Change	% Change
Dollar Index	82.585	.208	0.25%
EUR/USD	1.3192	-.0050	-0.38%
GBP/USD	1.658	.0011	0.07%
USD/JPY	103.97	.05	0.05%
USD/CAD	1.0981	.0037	0.34%
AUD/USD	.9294	-.0016	-0.17%
USD/BRL	2.286	.009	0.40%
10 Year Yield	2.387	-.016	-0.67%
30 Year Yield	3.135	-.022	-0.70%
Prices taken at previous day market close.			

But, the bears still have the momentum on their side as two sharp downtrends remain intact on the daily time frame. We will look for the steeper of the two to break before we get overly bullish, but until then, $92.50 is the "line in the sand" for the bulls.

Moving to the metals, copper continued to rally yesterday, rising +0.5% to mark the 4th gain in a row since commodities titan Glencore released a bullish research report on industrial metals last Wednesday. Copper has however become slightly overbought after rallying +4.5% in less than a week. So, over the near term, we could potentially see some profit-taking here in the mid-low-$3.20s as traders close long positions. But looking at the longer time frame, a well-defined uptrend dating back to the March lows has formed on the charts and copper should continue to perform well based on the steadily (albeit slowly) improving global economy.

Looking to the precious metals, trading in gold was downright boring yesterday as futures were corralled in a roughly $4 range for the majority of the session. Gold futures finished the day down -0.15%. At the risk of sounding like a broken record, the story in gold is largely the same as it has been all month. Over the near term, the stronger dollar is going to continue to weigh on gold. However, with the underlying threat of inflation still looming, there are plenty of speculators willing to take a shot on the long side here, which is why we continue to hold gold in longer time frame accounts. Having said that, the level to watch remains longstanding trend support at $1,273.

Currencies & Bonds

Beginning with the bond market, Treasuries rallied yesterday as the 30-year gained +0.22% while the 10-year note finished the day up a more modest +0.06% with a yield back below 2.4% (2.387%). U.S. bond prices rose in sympathy with German bunds and most European equities (again, the FTSE was closed for a bank holiday in England) as investors remained focused on the ECB. European bonds were up yesterday morning on Draghi's comments from Friday, which, as we already discussed, led to speculation that the ECB is poised to ease further and may even be forced to initiate a round of QE. And, when the soft German IFO numbers hit, bunds surged and 10-year yields spiked down to fresh all-time lows below 0.95%.

Bottom line, Treasuries are going to have a very hard time selling off with bunds being as strong as they are. And, that was confirmed here at home yesterday in our domestic markets as stocks traded up to all-time highs (S&P briefly breaking above the 2,000 mark) but bonds failed to sell off, and actually gained on the day.

Going forward, bond investors will continue to look to the central banks for direction. Unless we see the expectations for rate hikes from the Fed moved forward or the expectations of "pace" quickened, the bond market will likely remain painfully well-bid, despite the long-term bearish fundamentals.

On that note, Friday's personal incomes and outlays report will be closely watched because if the PCE Price Index (the Fed's preferred measure of inflation) comes in hot, that may have an effect on one or more of the aforementioned policy expectations.

Looking to the currency markets, the biggest developments were in Europe yesterday as the euro fell -0.36% thanks to the Draghi comments. The euro opened at a nearly 12-month low Sunday evening, drifted higher overnight, and then dropped to fresh lows well below 1.32 when the weaker than expected German IFO survey was released early yesterday morning. Looking ahead, with all of the chatter about further stimulus, the path of least resistance is clearly lower over the medium term. On the charts, the euro/dollar pair is getting rather oversold, so a short-covering bounce could be expected, but any material rally should be looked as an opportunity to sell the euro.

In England, the pound rallied yesterday, adding +0.07%. But a fair portion of the move was largely a result of speculative forex traders shorting the euro against the pound (again because of the Draghi comments), which would obviously require buying the pound or pound futures to hold the full position. This was supported by the fact that the pound spiked higher against the euro upon release of the German IFO survey. Also, the only "real" news out regarding the pound yesterday was a comment from BoE policy-maker Ben Broadbent, who said the central bank "would not raise rates before wage growth was guaranteed." So, bottom line, trading volume in the EUR/GBP overshadowed the dovish CB-speak in England, but that will likely be corrected when English traders return to their desks today. On the charts, the pound is still in search of a bottom as the trend remains lower and bears have momentum on their side, but there is fairly solid support toward the 1.6485-1.6500 area.

In Asia the yen was flat yesterday, but there is a slew of data due out later in the week including CPI, unemployment rate, household spending, and industrial production. So, expect trading to be dictated by positioning as those reports approach (all of them hit Thursday night).

Have a good day,

Tom

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.			

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Asset Class Dashboard

(Updated 8.25.14)

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	**Bullish**	**Bullish**	*The S&P 500 traded to new highs last week as economic data was strong and the outlook for Fed policy remained stagnant. Positioning was the main reason stocks were higher last week, as investors chased and added long exposure. A period of consolidation is necessary (again) but the trend remains higher.*
Best Idea: Buy Regional Banks (KRE). **Best Contrarian Idea:** Buy Small Caps (IWM).			
Commodities	**Neutral**	**Bullish**	*Commodities traded lower again last week as WTI Crude is again acting as an anchor on commodity indices. But, most other commodities also declined given the reduction in geo-political tensions and after lack luster Chinese and EU economic data, which is casting some (small) doubt on the global recovery.*
Best Idea: Long Oil (USO), Long Copper (JJC) **Best Contrarian Idea:** Buy Grains (DBA)			
U.S. Dollar	**Bullish**	**Bullish**	*The Dollar Index surged to new highs for the year last week on good data and a not dovish Fed. The Dollar Index is now above 82, and while we need to see some sort of consolidation in the Dollar, with the path of policy between the US and Europe diverging materially, the trend in the Dollar should stay higher.*
Best Idea: Sell the Yen (YCS) **Best Contrarian Idea:** Long Canadian Dollar (FXC)			
Treasuries	**Bullish**	**Bearish**	*Treasuries actually declined last week but only marginally so, despite more strong data and a "not dovish" Fed. But, this market isn't being governed by fundamentals at this point, and as long as German Bunds continue to rally, the short term trend in Treasuries will be higher.*
Best Idea: Short "long" bonds (TBT) **Best Contrarian Idea:** Short High Yield Bonds (SJB)			