7:00's Report

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

August 29th, 2014

Pre 7:00 Look

- Futures are modestly higher this morning while international markets were mixed o/n.
- Economically, there were several "misses" in Japan which weighed on the Nikkei o/n (-0.23%). In Europe, EU HICP met expectations (0.3%) but other data disappointed which is buoying EU shares on more ECB speculation.
- Geopolitically, there were not any material changes in the current "spotlight" conflicts, but the markets clearly remain sensitive to the headlines.
- Econ Today: Personal Income and Outlays (E: 0.3%)

Market	Level	Change	% Change
S&P 500 Futures	2000.50	3.75	0.19%
U.S. Dollar (DXY)	82.495	-.021	-0.03%
Gold	1286.60	-3.80	-0.29%
WTI	94.95	.40	0.42%
10 Year	2.334	-.027	-1.14%

Equities

Market Recap

Stocks forfeited the 2,000 level yesterday as geopolitical angst outweighed good economic data. The S&P 500 fell -0.17%.

Stocks opened sharply lower yesterday thanks to deterioration in the conflict between Russia and Ukraine. Specifically, headlines that quoted Ukrainian president Poroshenko saying that Russia was "invading" caused futures and international markets to fall sharply in early trade.

Crude oil futures are rebounding from the recently established lows of the year and were able to break a 5 week downtrend yesterday.

But when more information was released on the issue and traders realized the headlines were blown out of proportion (and that there was not an actual invasion in progress by Russia), there was some relief in the markets.

Then, as has become the recent habit, focus shifted from geopolitics to economic data. The three major releases yesterday (jobless claims, GDP and pending home sales), were all encouraging and stocks recovered much of the morning losses by midday. From there, stocks drifted sideways into the end of the day and closed below 2,000 for the first day in three.

Trading Color

It was a fairly typical "risk off" day in the stock market yesterday. The Nasdaq finished down -0.26% and the Russell 2000 fell -0.58%, both underperforming the S&P 500 again. High-beta stocks (SPHB) sold off -0.38% while their safer, low-volatility counterparts (SPLV) actually rallied +0.14%.

Looking to the sector movement, utilities were (not sur-

Market	Level	Change	% Change
Dow	17,079.57	-42.44	-0.25%
TSX	15,558.17	-44.48	-0.29%
Brazil	60,290.87	-659.70	-1.08%
FTSE	6,814.50	8.70	0.13%
Nikkei	15,424.59	-35.27	-0.23%
Hang Seng	24,742.06	1.06	0.01%
ASX	5,625.90	1.49	0.03%
Prices taken at previous day market close.			

prisingly) the best performer again yesterday as interest rates continued to fall. Once again the falling rates put pressure on the financials, causing them to be the worst performers.

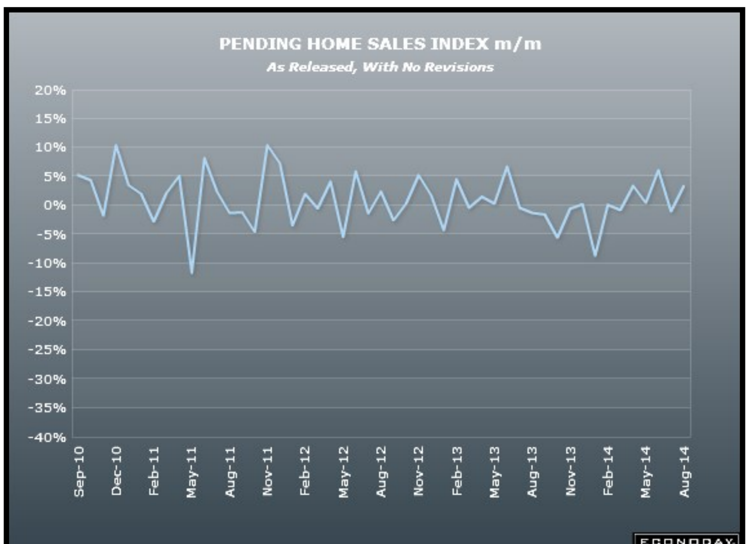
Market	Level	Change	% Change
DBC	24.974	.014	0.06%
Gold	1291.70	8.30	0.65%
Silver	19.620	.145	0.74%
Copper	3.1510	-.0475	-1.49%
WTI	94.58	.70	0.75%
Brent	102.49	-.23	-0.22%
Nat Gas	4.050	.047	1.17%
RBOB	2.5931	.0026	0.10%
DBA (Grains)	26.395	.205	0.78%
Prices taken at previous day market close.			

The only other notable mover was the energy sector. It edged up +0.08% as the second best performer behind utilities thanks to the strength in crude oil and natural gas futures, which both broke through the resistance levels mentioned in yesterday's report.

On the charts, the S&P 500 closed the day right in the middle of the 1,995-1,997 support band yesterday, and that will be the level to watch today. Also, the traders who are not already out of town for the holiday weekend will obviously be eyeing the 2,000 mark as well.

Bottom line

Economic data continue to trump geopolitics. Yesterday's in-line weekly jobless claims report, the better than expected GDP, and much-improved pending home sales index all fell into the "Goldilocks" category for economic data. Again, Goldilocks data show the economy is continuing to improve, but not so quickly that the Fed will need to make adjustments to policy such as hiking rates sooner than is currently priced into the market.



Pending Home Sales rose more than expected in July, +3.3% vs. E: +0.5%, another positive indication that the housing market, a key concern of the economy, is gradually improving.

For that reason, the morning sell-off in stocks did not materially escalate over the course of the day. This simply further confirms this market's primary focus is central banks, and it will take a serious geopolitical development to change that.

Economics

Weekly Jobless Claims

- Weekly claims fell to 298K vs. (E) 300K
- The 4 Week Moving Average dropped 1.25K to 299.75K.

Takeaway

Weekly jobless claims fell a modest 1K to 298K from last week's revised figure of 299K. The 4-week moving average, which offers a smoother look at the sometimes-volatile report, dipped back below 300K to 299.75K from 301K the week prior. The report was released in tandem with a solid GDP report; yet, markets showed little interest as traders fixated on geopolitics.

Bottom line, jobless claims are hovering near post-recession lows with the 4-week moving average coming in below 300K for 4 of the last 5 weeks. This continues to suggest further improvement in the labor market. Based on claims data for the month of August, the BLS Employment Situation Report due out next Friday should follow the recent trend and show monthly job creation around 200K+.

GDP

- Revised Q2 GDP was 4.2% vs. (E) 4.0%

Takeaway

The second estimate for Q2 GDP released yesterday morning came in better than the initial report showed. The headline, Real Gross Domestic Product, increased at an annual rate of 4.2% vs. (E) 4.0%. The two notable changes between the advanced look and the revised look were a higher than initially expected non-residential fixed investment figure and a smaller than initially reported increase in private inventory investment. But the net of the report is that the increase in Q2 GDP suggested an uptick in personal consumption expenditures.

So, the takeaway is, the rebound from the weather-driven weakness of Q1 was stronger in the second quarter than most expected. Although, following the durable goods report earlier in the week, that was already somewhat priced in to the market. Specifically, personal spending and business investment showed improvement, which was encouraging and further supports the "comeback" thesis. Bottom line, yesterday's revisions to Q2 GDP were consistent with the general consensus that the economy is picking up steam again, albeit only gradually.

Commodities

Commodities were moving on geopolitics yesterday as the situation between Ukraine and Russia escalated. Gold, oil, natural gas and wheat (which, remember, is very sensitive to any news out of Ukraine/Russia) were all bid up while concerns over the economic impacts of a more-serious conflict weighed on copper prices. DBC rose +0.1%.

Crude oil futures finally broke out of consolidation yesterday, rallying +0.75% to close above the steep downtrend line that has been in place for nearly 5 weeks. Yesterday's close was the first above $94 since August 15th. It was the geopolitical fear bid that first pushed futures up through resistance; however, another round of positive economic data also contributed to the gains.

The "Goldilocks" reports (weekly jobless claims, GDP, and pending home sales) support the bullish, demand-based argument that, as the economy (specifically the job market) continues to improve, demand for crude oil and the refined products will also rise.

Market	Level	Change	% Change
Dollar Index	82.495	.046	0.06%
EUR/USD	1.3182	-.001	-0.08%
GBP/USD	1.6588	.0013	0.08%
USD/JPY	103.66	-.19	-0.18%
USD/CAD	1.0849	-.0014	-0.13%
AUD/USD	.9353	.0017	0.18%
USD/BRL	2.2413	-.0053	-0.24%
10 Year Yield	2.334	-.027	-1.14%
30 Year Yield	3.072	-.037	-1.19%
Prices taken at previous day market close.			

On the charts, initial support has been moved up to $94 while there is more material support below at $93.50. As for resistance, it is pretty wide open, but there is a gap in the chart to $95.28. Once that is filled, we could see some short-term profit-taking from that level (and we are already within reach this morning).

Natural gas was one of the best performers in the space again yesterday, rallying an even +1% to close at $4.04. It was inventory day for nat gas, with the EIA reporting an injection of 75 Bcf to national stockpiles vs. (E) 80 Bcf. The "miss" spurred a knee-jerk (algo) spike in futures, which hit $4.10 before reversing sharply.

The story remains largely the same as stockpiles are still 16.5% below the 5-year *range*. To be clear, that means 16.5% *below* the *lowest* of the past 5 years. And, stockpiles still need to increase an additional 1.2 trillion cubic feet (roughly) by late October to be at the "normal" level for entering the draw season. That's 9 weeks straight of builds averaging more than 130 Bcf. (The current 4-week average of weekly supply injections is about 81 Bcf …)

So, if the pace of injections doesn't materially accelerate, we will enter the draw season with below-average natural gas stockpiles. And, if this winter is anything like last, demand will again be very strong … and prices will be substantially higher than they are currently.

Moving to the metals, gold rallied sharply on the fear bid that was stirred by the Ukraine and Russia headlines early yesterday morning, trading within $3 of the $1,300 mark. But, as has been the case recently, nothing developed beyond the "hearsay" media headlines and dramatic Twitter posts, and economic data took center stage in the gold market. The better than expected reports caused gold prices to retreat and close well off the highs, but still up +0.58%.

Positioning ahead of the "big" report of the week, personal incomes and outlays, also played a part in gold action yesterday. And, the PCE Price Index remains the catalyst to watch today. The reaction, however, could go either way. After all, despite the fact that rising inflation is gold-bullish, right now it's all about Fed policy. If a "hot" report means a hawkish policy adjustment by the Fed, we could see support at $1,275 tested again.

Copper futures fell a steep -1.5% yesterday, also as a result of the Russia-Ukraine debacle. And, copper will remain volatile as the situation goes on because of the potential economic impacts of further sanctions between Russia and the West (which are rather likely at this point) ... or, even worse, an official military conflict/ invasion of Ukraine. While we wait to see how things play out, we will look to the charts for direction. The first level of support is at the 100-day moving average ($3.14), near yesterday's lows.

Currencies & Bonds

Currency trading was relatively quiet yesterday but there was some movement on geopolitics as well as economic data. The dollar finished the day little-changed and still within reach of multi-month highs.

Early yesterday morning the euro was trading lower on another round of poor economic data, specifically the August economic sentiment report that missed expectations (100.6 vs. E: 101.5) and caused further speculation that the ECB will be forced to ease very soon. Then the euro made another leg down thanks to the overly dramatic "Russian invasion statement" that Ukrainian President Poroshenko released to the press. But, once everyone realized there was not a *real* invasion, the sell-off stopped and some shorts covered. This left the euro only slightly lower on the day, down -0.10%.

Technically, the euro is still rather oversold so the risk of a short-covering rally still exists. Again, any move toward 1.335 or higher should be seen as an opportunity to short the euro either against the dollar or the pound.

Speaking of the pound, the British currency rallied a meager +0.06% against the greenback yesterday, but it is quietly testing very important trend resistance and threatening to end its two-month counter-trend sell-off. Looking ahead, a close toward 1.66 would be a rather bullish technical breakout, and would be a signal to get long with limited downside risk. But for now we will remain sidelined as the break has not yet been completed.

The Canadian dollar continued to rally yesterday, although much more modestly than Wednesday's move, adding just +0.13%. But, the low-risk/high-reward technical trade setup still exists, especially if the PCE Price Index in the personal incomes and outlays report runs hot and the dollar sees another hard rally.

Looking overseas, the yen rallied in Japan as a part of the "fear trade" theme in the markets yesterday. But as was the case with the other components of the geopolitical trade, the yen closed well off the highs of the day—up +0.20%. The "line in the sand" in the dollar/yen pair remains 103.49, which is the low of the recent consolidation. A break below that level could see the pair move back to 103 even while 105 remains the upside target.

Looking to the bond market, Treasuries rallied as you would expect them to given the geopolitical "angst" that influenced the markets yesterday. The 30-year bond gained another +0.36% on the day while the 10-year note added +0.15%, causing the yield curve to flatten.

There was a 7-year note auction; however the results were pretty status quo. The "when issued" yield came in as expected at 2.045% and the bid to cover, a measure of demand, almost exactly matched the average of the previous 10 auctions at 2.57. There was little reaction to the results as most bond traders were preoccupied with the geopolitically fueled rally that was already in progress. Nonetheless, the outcome of an auction of $29 billion of Treasury notes is worth noting.

Bottom line, if the absurd strength of the German bund wasn't already enough to keep Treasuries afloat for the near term, geopolitics have made it pretty clear. But, one thing that will be very important to keep an eye on this morning (as I mentioned before with regard to gold), and could potentially trigger a sell-off, is the PCE price index within the personal income and outlays report. And, I may be hyping this up a little too much, because if it is relatively in line, the market reaction will almost surely be limited. However if we see the Fed's preferred measure of inflation unexpectedly rise, we could see a strong hawkish reaction across asset classes.

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
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).**

	Near Term Trend	Long Term Trend	Market Intelligence
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)**

	Near Term Trend	Long Term Trend	Market Intelligence
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)**

	Near Term Trend	Long Term Trend	Market Intelligence
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)**