7:00's Report

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

October 16th, 2014

As if we needed more bad news, Greek 10 Year Yields are spiking again this morning as fears are rising about their ability to exit the EU bailout.

Pre 7:00 Look

- Futures are sharply lower after getting a (bad) blast from the past. Greek bond yields are surging and Spain had a sloppy debt offering this morning, which is causing more concern in Europe.
- Actual data was light o/n and what did come was mostly in-line (final EU HICP and EU Trade balance).
- Econ Today: Jobless Claims (E: 290K), Industrial Production (E: 0.4%), Philly Fed Survey (E: 20.0). Fed Speak: Plosser (8:00 AM), George (12:15 PM), Lockhart (12:30 PM), Bullard (1:00 PM), Kocherlakota (2:30 PM)
- Earnings Today: GS (E: 3.22), UNH (E: 1.53), AMD (0.04), GOOG (E: 6.53), SLB (E: 1.56).

Market	Level	Change	% Change
S&P 500 Futures	1824.00	-22.75	-1.23%
U.S. Dollar (DXY)	85.405	.169	0.20%
Gold	1243.00	-1.80	-0.17%
WTI	80.24	-1.54	-1.88%
10 Year	2.090	-.116	-5.26%

Equities

Greece Update

Markets are again sharply lower this morning on funding concerns for Greece. The need to know is this: The current Greek administration is in trouble in the pools, with the nationalist, anti-EU party gaining fast. The current Greek administration wants a guarantee of a clear release from the bailout programs (and austerity requirements) next year, so they can say they are free to the people, and shore up support at the polls. The "Troika" which gave Greece the bailout is not agreeing to that, and as a result fears are rising there will be a vote of no confidence in Greece, and this anti-EU, pro nationalist party will win, at which point the question of Greece staying in the EU becomes much more real (again).

In all likelihood this will settle itself out positively (the Troika will probably fold) but for now it's adding more angst into Europe, which is exactly the opposite of what we need right now.

Market Recap

Stocks slumped again Wednesday on news of the AbbVie /Shire merger breakup and economic concerns, although importantly, stocks finished well-off their worst levels of the day. The S&P 500 fell -0.81%.

Futures were initially up Wednesday morning early, but then a series of headlines took futures negative before the open. Then, frankly, things snowballed from there.

News of a second Ebola patient, bad economic data (retail sales, PPI and Empire State manufacturing all missed) and finally news of the potential AbbVie/Shire

Market	Level	Change	% Change
Dow	16,141.74	-173.45	-1.06%
TSX	13,869.88	-166.80	-1.19%
Brazil	56,135.27	-1,880.19	-3.24%
FTSE	6086.35	-125.29	-2.02%
Nikkei	14738.38	-335.14	-2.22%
Hang Seng	22900.94	-239.11	-1.03%
ASX	5254.89	9.28	0.18%
Prices taken at previous day market close.			

merger breakup weighed on stocks. By the time the market opened, it was a borderline panic.

Market	Level	Change	% Change
DBC	21.97	-.28	-1.26%
Gold	1238.80	4.50	0.37%
Silver	17.430	.027	0.16%
Copper	3.0085	-.0815	-2.64%
WTI	81.55	-.29	-0.35%
Brent	84.18	-1.23	-1.44%
Nat Gas	3.804	-.012	-0.31%
RBOB	2.1520	-.0282	-1.29%
DBA (Grains)	26.28	-.40	-1.50%
Prices taken at previous day market close.			

Stocks sunk on the open as bonds surged the most in years. At one point the Dow was down more than 400 points and the S&P 500 dropped more than 50.

After the initial hour of trading, things stabilized deeply in the red and churned through the European close. But then methodical selling began again. When a headline broke that the second Ebola patient had flown on a Frontier Airlines jet Monday, stocks gapped lower again and hit their lows of the day right before 1:30.

Stocks began to lift off the lows thanks in part to a headline that said Fed Chair Janet Yellen told G-30 members over the weekend that she still felt good about growth. As small caps and energy began to rally in the afternoon, the broader market followed to close off the worst levels of the day.

__Trading Color & Bottom Line__

Yesterday may have signaled the end to the selling, at least in the short term, as several of the key sub-sectors that have led on the way down reversed and closed positive.

First, the Russell 2000 was buoyant all day, and closed up +1%.

Second, energy outperformed despite crude finishing the day mildly lower, as the XLE rallied +0.76%.

Third, the semiconductor index (SOX) reversed midday and closed up +0.48% despite disappointing results from LLTC Tuesday night.

Additionally, I said earlier in the week that I would like to see an almost-panicked open, where we could wash out all the weak-handed longs and then try and establish some sort of a tradable bottom.

Obviously with so much potential bad news looming out there, making any sort of a call is a fool's errand. But we get paid for opinions here, so I will say that I think yesterday likely marked an end to this pace of selling we've seen and market obliteration—at least in the short term. Frankly speaking, things haven't gotten *this* bad this quickly, and this market is now deeply oversold short term.

Part of that conclusion is based on the abovementioned internals. The other part is that I think the Shire/AbbVie breakup lobbed a "bomb" into the hedge fund community that was already hurting. As a result, yesterday we saw a lot of funds "throw in the towel" for 2014. So, it exacerbated the selling, especially in the morning.

But, that said, it is still much too early to tell if this is a market bottom we need to buy.

The European inspired weakness in futures this morning is obviously calling my opinion into doubt, but if we can still hold yesterday's lows (1817) early in trading and stocks can churn sideways today, this still could signal a short term exhaustion to the selling. If we do that, then we can start to talk about this market putting in a potential bottom.

For those itching to do something now, though: I will say that, as the chart shows, XLE bounced hard off near-term support. And, while I'm not a fan of catching falling knives, for those looking to buy something on that dip, a position in XLE now has a decent setup, with a clear stop on it (yesterday's spike lows and that multi-year uptrend). So, you've got a potentially good risk/reward setup here.

Another idea, for those in the options universe, is to consider selling a put spread on small caps or the broader market in general. It takes advantage of the massive volatility we've seen, and can offer limited risk. Food for thought.

Bottom line: We still need to see oil and Europe (EWG) bottom before we can declare an "all clear" and we're not there yet—but yesterday I hope did mark the peak of the panic-selling we've seen these last 2+ weeks, at least for a little while.

Economics

The economic reports yesterday were universally disappointing, and while none were important or recent enough to cause a material downgrade of the U.S. economy, the drop in retail sales and business inventories will put slight downward pressure on Q3 GDP expectations. And, the soft Empire State manufacturing survey made this market's confidence problem worse.

Retail Sales

- September Retail Sales fell –0.3% vs. –0.1%.

Takeaway

This was a disappointing number, but it wasn't quite as bad as it seemed given the backdrop. As expected, consumer spending did slow, but the key "Control Group" (which is retail sales minus autos, gasoline and building materials) fell just -0.2%, although the previous month's gains were revised slightly lower.

With oil and gas plunging in October (keep in mind this was a September report), October is key to watch as a good gauge on the health of the consumer. Again, though, for a market with a confidence problem, this report wasn't exactly welcomed . It does not, though, imply consumer spending was markedly changed in September.

Commodities

It was more of the same in the commodities space yesterday as energy underperformed again with crude oil, and the refined products dipped to fresh lows while the metals continued to rally on fear bids and stock-market hedging. The benchmark commodity ETF, DBC, fell -1.3%

Crude oil prices slumped to fresh lows yesterday morning, testing support at the psychological $80 mark. But, support held and futures bounced nearly $2.50 before drifting in a wide sideways range into the close to finish down -0.32%. WTI futures managed to rally back to nearly flat after-hours as the stock market rebounded in the afternoon.

Equities and oil prices continue to trade with a high level of correlation as growth fears remain one of the primary focuses of the global markets. Technically, yesterday's low of $80.01 will be viewed as a "line in the sand," as there are surely "stop loss" orders clustered below. Meanwhile resistance lies above at $84. Looking ahead, this could potentially be the beginning of a near-term bottom; however, we will need to see confirmation via a rebound in the stock market.

Natural gas was little-changed, down -0.31%, after trading in a tight 5-cent range yesterday. Nat gas futures did slip down to a 5-week low of $3.76 during the session, and bounced back up above $3.80 into the close. On the charts, natural gas futures continue to trade with a heavy tone; however, support at $3.80 remains intact for now. Today, focus will be on the EIA inventory report, for which analysts are expecting a build of 86 Bcf (not that much lower than last week's build of 105 Bcf).

Gold traded higher yesterday thanks to fear bids during the morning bloodbath that took place in the global equity markets. But, around the time stocks reversed from the lows, gold futures turned back from the highs and fell toward the key $1,240 level. Gold finished the day just below resistance at $1,240 for a +0.45% gain on the day.

Market	Level	Change	% Change
Dollar Index	85.08	-.861	-1.00%
EUR/USD	1.2806	.0148	1.17%
GBP/USD	1.5972	.0069	0.43%
USD/JPY	106.04	-1.00	-0.93%
USD/CAD	1.1256	-.0037	-0.33%
AUD/USD	.8812	.01	1.15%
USD/BRL	2.454	.0545	2.27%
10 Year Yield	2.090	-.116	-5.26%
30 Year Yield	2.876	-.081	-2.74%
Prices taken at previous day market close.			

Currencies & Bonds

Yesterday was nothing other than a historic day in the bond market, as that type of volatility will (hopefully) be the most any of us sees for a very, very long time.

At one point yesterday, the 30-year Treasury was up over +2.4%, while the yield on the 10-year crashed through 2.0%, hitting a low of 1.86%

before rebounding to close at 2.09%.

That is easily the most volatility I've seen since the darkest days of the fall of 2008. Simply put, unless the world is truly descending into a global deflationary spiral, then yesterday will have been a "blow-off" top in the bond market.

Now, I'm not saying the move in bonds wasn't unfounded. Expectations for Fed policy are shifting rapidly. Fed Fund futures now are pricing in the first rate hike in December 2015, a big shift from June (that's happened in less than 2 weeks).

And, the economic data yesterday were bond-positive, as universally weak economic data, a continued plunge in Europe and chatter about "QE 4" or a cut to the IOER (Interest on Excess Reserves) got much louder. Throw in a collapsing stock market and that is a perfect recipe for higher Treasuries, but not *that* much higher.

I can only assume that the vast, vast majority of people who were short Treasuries are now out and licking their wounds.

And, I don't think we're about to see an imminent decline in the Treasury market (at a minimum, Treasuries will not decline until German bonds stop going up). But the shorts have to be cleared out, and this is now a much more balanced market.

And, for all of our sakes, the closing lows yesterday in the 30-year and 10-year need to hold going forward, because if yesterday *wasn't* a "blow-off' top in bonds, then as I said yesterday, stocks are headed much, much lower. I, for one, believe it was that blow-off top.

Turning to currencies, everything was up vs. the dollar yesterday—it was just a question of "how much" as the dollar rally continues to unwind.

And, like bonds, the news was dollar-negative, as Fed expectations got more dovish and economic data were universally disappointing. But it wasn't *that* negative and the Dollar Index falling -1% through support at 85.50 was more a factor of it still being a crowded "long" trade than it was materially changing fundamentals.

The list of best performers vs. the dollar was generally driven by the currencies that traders are most "short," as yesterday was a short-covering rally in most currencies.

The euro was the best performer vs. the dollar, rallying +1.25% on dollar weakness and growing concerns about ECB ineffectiveness. The euro broke through resistance at the 20-day moving average, and if data in the U.S. and Europe continue to disappoint, there's nothing to stop a run higher to 1.2986 (the 50-day MA).

The Aussie was the next-best performer, rallying +1.18% after lackluster Chinese inflation data (which give Chinese authorities more scope to ease policy), while the yen rallied +0.77% on general "risk off" sentiment and short-covering (there was no real news there).

Although it violated support at the 50-day moving average intraday, 106.04 in dollar/yen is support. And although there is downward pressure, the case can be made for trying to buy this dip in the short term with a stop on that support level (lower risk/high reward).

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
9/11/14	EUM	24.05	None	*Short Emerging Markets. With the dollar surging higher and the global bond yields rising, this should put pressure on the emerging markets, as money rotates out of those economies back towards developed markets. Original Issue*
9/4/14	HEDJ EUFN EWI EWP	59.35 24.67 16.44 41.34	None	*"Long Europe" Portfolio. The move by the ECB to start a private market QE program, combined with the impending TLTROs, should give the European economy a significant boost over the coming months. HEDJ remains the best way to hedge out a falling euro, while higher beta sectors of the EU economy (financials, Italy, Spain) should rally the hardest. Finally, the moves should end the German bond mania, which should weigh on Treasuries. Original Issue*
7/21/14	UNG	20.98	None	*Natural gas is a supply/demand based trade. While injections over the summer have replenished supply, we are still 15% below historical levels, with the winter heating season drawing near, Natural gas in the highs $3.00's appears to be a value. 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 (10/13/14): The yen hit our target of 110 vs. the dollar and DXJ traded basically to its all time highs in early October, but now we are seeing a much needed correction. Longer term, I remain a bull on Japan/bear on the yen, but this trend will likely pause for some time, and I'd book any profits in those positions for accounts that don't have a very long time frame (and can stomach a correction).			
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 (10/13/14): Treasuries are once again at new highs for the year, as a floundering European economy and worries about a stock market correction trump better economics here in the US. The fundamentals for this trade remain decidedly negative, but once again money flows have trumped fundamentals in the near term.			

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Asset Class Dashboard

(Updated 10.13.14)

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	**Neutral**	**Bullish**	*The S&P 500 had its worst week in years last week as concerns about global growth, dis-inflation and the end of QE pushed stocks below key support levels. The markets re-siliency can't be discounted, but stocks are acting "different" than previous corrections, and we advise caution in shorter term, more tactical accounts.*
Best Idea: Buy Regional Banks (KRE). **Best Contrarian Idea:** Buy Consumers Stocks (XLY)			
Commodities	**Bearish**	**Bullish**	*Oil continued to drag commodities lower last week. Global growth concerns continued to weigh on the space, although with the dollar declining we are seeing some dichoto-my: grains and gold are trading better, but energy remains a major concern.*
Best Idea: Buy Natural Gas (UNG) **Best Contrarian Idea:** Buy Grains (DBA)			
U.S. Dollar	**Bullish**	**Bullish**	*The Dollar Index traded lower for the first time in 13 weeks, as a dovish FOMC minutes broke the dollar rally fever. The Dollar needs to correct, and although it'll be supported somewhat if the stock sell off continues, I believe we're seeing the start of a needed correction in the US Dollar.*
Best Idea: Sell the Yen (YCS) **Best Contrarian Idea:** Long Canadian Dollar (FXC)			
Treasuries	**Neutral**	**Bearish**	*The Treasury bounce accelerated last week and the 30 year traded to a new 52 week high, as worries about global growth (especially in Europe) sent money pouring into Treasuries, as money flows again trump deteriorating economic fundamentals.*
Best Idea: Short "long" bonds (TBT) **Best Contrarian Idea:** Short High Yield Bonds (SJB)			