7:00's Report

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

November 24th, 2014

Pre 7:00 Look

- Futures are slightly positive and international markets are higher as hopes for more stimulus from China grew over the weekend and EU economic data beat expectations.
- Asia outperformed (up 1% generally) following a Reuters article that said the PBOC was considering doing "more."
- In Europe, the German IFO Business Expectations Index beat estimates, confirming last week's good ZEW Survey.
- Nuclear negotiations between Iran and the P5+1 failed to reach an agreement and are set to resume in December.
- Econ Today: PMI Services Flash (E: 57.8).

Market	Level	Change	% Change
S&P 500 Futures	2066.25	4.50	0.22%
U.S. Dollar (DXY)	88.32	-.085	-0.10%
Gold	1195.00	-2.70	-0.23%
WTI	76.19	-.32	-0.42%
10 Year	2.321	-.014	-0.60%

Equities

Market Recap

The rally continued last week as the S&P 500 rose to another all-time high, thanks to decent economic data and rising expectations for QE in Europe. The S&P 500 rallied 1.1% last week and is up 11.6% year-to-date.

Stocks started the week quietly last Monday as a handful of conflicting catalysts offset each other, leading stocks to finish flat for the 5th consecutive session. (Very disappointing Japanese GDP was offset by "dovish" Mario Draghi comments and M&A from HAL/BHI and ACT/AGN.) Tuesday, the rally resumed as stocks marched steadily higher over the course of the session thanks to a good German ZEW Index and Japanese PM Abe officially delaying the tax increase and calling for snap elections.

Wednesday stocks actually declined (the only day last week) in what we called a "failed sell-off." Profit-taking and general Washington angst after the announcement of President Obama's executive order on immigration weighed slightly on stocks, but mostly in-line FOMC minutes helped stocks finish down marginally. Thursday, it as another "failed sell-off" as stocks dipped initially on soft global PMIs, but dip-buyers were there immediately and stocks recovered and closed broadly higher.

Friday the rally continued thanks to the surprise Chinese rate cut and more dovish comments by Draghi. But in total opposition to every other day last week, stocks acted tired. Equities popped at the open but then drifted lower throughout the day to finish up, but well off the best levels of the day.

Trading Color: Europe Outperforms

Stocks rose last week but it wasn't the highest quality rally, as Friday's fade implied. The Russell 2000 was again flat on the week. It again underperformed, as the S&P 500 continues to be pushed higher mainly by outperformance in large-cap tech (AAPL, MSFT, CSCO, INTC), meaning this isn't as broad a rally as we would want it to be.

Europe was the big story of last week, as HEDJ rallied more than 3%, breaking its three-month downtrend and now challenging a longer-term downtrend.

The main reason Europe heavily outperformed was Draghi making comments throughout the week that more forcefully alluded to the ECB doing "QE." As a result, European stocks rallied primarily because the mar-

Market	Level	Change	% Change
Dow	17,810.06	91.06	0.51%
TSX	15,111.13	0.00	0.00%
Brazil	56,084.04	2,681.23	5.02%
FTSE	6,750.89	0.13	0.01%
Nikkei	17,357.51	56.65	0.33%
Hang Seng	23,893.14	456.02	1.95%
ASX	5,361.80	57.50	1.08%

Prices taken at previous day market close.

ket is more confident the ECB may actually do QE (investors are starting to believe the ECB). Finally, while the flash PMIs were disappointing, the German ZEW Index was a positive surprise and there are some economic "green shoots" in Europe.

Market	Level	Change	% Change
DBC	21.70	.19	0.88%
Gold	1198.90	8.00	0.67%
Silver	16.40	.263	1.63%
Copper	3.031	.0115	0.38%
WTI	76.43	.58	0.76%
Brent	80.15	.82	1.03%
Nat Gas	4.275	-.214	-4.77%
RBOB	2.053	.0254	1.25%
DBA (Grains)	25.70	.07	0.27%
Prices taken at previous day market close.			

Domestically, most of the sector trading action was due to specific news and not a greater macro trend or rotation.

Retailers (RTH) outperformed last week on good earnings from TGT, BBY, TJX and LOW, plus increased expectations for holiday spending. Healthcare also rallied on M&A (ACT/AGN). And energy (XLE) showed more signs of life; XLE broke through the 50-day MA to the upside for the first time in over two months. Fundamentally, Iranian crude negotiations appear to be breaking down and OPEC meets Thursday, so there are some potential tailwinds forming for energy stocks shorter term.

While I prefer "Europe" to the U.S. broadly, from a domestic sector exposure standpoint, I continue to think energy is an attractive risk/reward trade here via XLE going into the OPEC meeting. Our "return of the U.S. consumer" thesis also still has legs (SYF, LEAF, RTH).

Upcoming Calendar

Although we are late in the year, it's not "over" yet. There are still several events with the potential to cause some volatility into year-end, both here and in Europe.

A quick reference:

ECB Meeting 12/4 — Jobs Report 12/5 — Next ECB TLTRO Offering 12/11 — U.S. Continuing Resolution expires 12/11— FOMC Meeting 12/17.

Of these events, the FOMC meeting in December (risk of it being "hawkish") and the TLTRO offering (important for confidence in a European recovery) are the two that have the potential to be a surprise negative on stocks.

Bottom line

Last week the market was again resilient but, at the same time, Friday's trading implied we may be running out of near-term momentum. We maintain the last 40-50 points in the S&P 500 have come as a series of unexpected but positive headline events (BOJ surprise easing, Republican "landslide" in midterms, Abe suspending tax hike, China surprise rate cut) exacerbated the fact that—following the October sell-off—many managers were underinvested. The result: Those managers have chased stocks higher and bought on every 5- to 10-point dip in the S&P 500.

Importantly, we do not think the last 40-50 points have been because of fundamental improvement in the outlook for U.S. stocks. At these levels, current and foreseeable market fundamentals are very fully appreciated.

As a result, we remain cautious on how much upside remains. I'm not a bear on the U.S. equity market, but in the near term I think a lot of "weak and late" longs have been pulled into the market. We are now at risk of a correction, which will provide a better entry point in the S&P 500.

I continue to espouse the virtues of Europe and I'm encouraged with the way that region traded last week. On a go-forward basis, if global markets continue to "melt up" into year-end, then HEDJ will offer a better return than SPY or some similar fund. I know I'm sounding repetitive on this call, but it's because I like the risk/reward in Europe over the near and medium term.

Economics

Last Week

Last week it was a story of underwhelming economic data vs. more central bank stimulus. Given the rally in stocks, clearly the banks prevailed again. And, we are seeing that continue this morning as the main positive catalyst over the weekend was a Reuters article implying more China stimulus ahead (link here).

Starting with the data, though, it was generally underwhelming. First, the flash global manufacturing PMIs were all misses vs. expectations. Chinese and German manufacturing PMIs both declined to 50.0, missing expectations, while broad EMU manufacturing PMI was 50.4 and the U.S. number fell to 54.7 vs (E) 56.5.

Despite the soft readings and the German and Chinese numbers now teetering on contraction below 50, the market viewed these numbers as disappointing ... but not as signaling the global recovery is failing, which is an important distinction. Last week's numbers, while bad, weren't bad "enough" to put the global recovery into doubt—especially in context of central bank policies going forward. That's why they didn't cause a sell-off.

It's important to realize just how important the actions (and expected actions) by global central banks ex-USA are on the market right now. The BOJ's surprise stimulus of three weeks ago is still fresh in investors' minds. Mario Draghi seems to be on the tape every day hinting the ECB will do QE. And, Friday the PBOC cut rates.

So, the way to look at the current macro environment right now is: Yes, the global recovery is feeble, but central banks are going to get more accommodative. So, the current soft data is taken with a very large grain of salt.

There are two risks to this setup: First, the expectations that central banks will do "more" to stimulate growth gets removed (i.e., central banks are out of bullets). Second, it's for the economic data to get worse from here, which would imply central bank tactics are now ineffective and their policies impotent. Those are the two macro risks we need to watch going forward, because both are negative for stocks.

Turning to the U.S., the economic data were mixed, but the bottom line is that most signs point to the economic recovery continuing to gain momentum.

As mentioned, the flash manufacturing PMIs fell more than expected, but at 54.7 the absolute level is still well in expansion territory. This soft reading was partially offset by a blowout Philly Fed manufacturing survey, which rose above 40 (although that number is almost certainly too good to be true).

But, other U.S. economic data last week were good: Both New Home Sales and Existing Home Sales beat expectations and jobless claims hit a 14-year low. The only real disappointment last week was October Industrial Production, as the manufacturing sub-component rose 0.2% vs. (E) 0.3%, and previous months were revised lower. But, that reading was largely overshadowed by the other data.

Finally, there were FOMC minutes last week, but they didn't really elicit much of a reaction. They mostly confirmed that the FOMC is committed to normalizing policy, and at this point they don't view low inflation or slow global growth as a problem. There was no change to the current expectation of rate hikes in June.

This Week

The highlight of the holiday-shortened week is definitely the European flash HICP (their CPI) reading Friday. Europe is ground zero for the global recovery, and if this number is again weak (core HICP rising yoy less than 0.7%), then expect pressure on European stocks.

Almost all of the data domestically comes Wednesday given the Thanksgiving holiday.

October durable goods, New Home Sales, Pending Home Sales, weekly jobless claims and Personal Income and Outlays all come Wednesday morning. Of those releases, Personal Income and Outlays is the most important, because we will get an update on the "Core PCE Price Index," which is the Fed's preferred measure of inflation. CPI last week helped further dispel the notion of disinflation, so we'll look for that to be further confirmed this week.

Market	Level	Change	% Change
Dollar Index	88.355	.688	0.78%
EUR/USD	1.2394	-.0144	-1.15%
GBP/USD	1.5652	-.0041	-0.26%
USD/JPY	117.72	-.48	-0.41%
USD/CAD	1.1235	-.0063	-0.56%
AUD/USD	.8666	.005	0.58%
USD/BRL	2.5135	-.0583	-2.27%
10 Year Yield	2.321	-.014	-0.60%
30 Year Yield	3.029	-.024	-0.79%
Prices taken at previous day market close.			

Bottom line, the highlight of this week domestically and internationally is inflation, via the HICP and PCE Price Index. Upticks in both will be welcomed by the market. We need more inflation right now, not less (and I think we're going to get it eventually, good and hard).

Commodities

Most commodities caught a bid or at least found support last week despite the dollar hovering near recent, multi-year highs. Volatility spiked in the complex, however. Natural gas whipsawed up and down on inventory and weather data. Crude oil traders looked for direction in choppy trade that led futures to finish the week little-changed. And the metals saw sharp moves in response to economic data, central bank speak, and physical news. The benchmark commodities tracking index ETF rallied for the first week in three, adding 0.46%.

Trading in crude oil was largely dictated by day traders and fast-money algos last week as investors continued to look ahead to this week's OPEC meeting and, importantly, whether or not the decision-makers will agree on a production cut to curb the recent sharp declines in prices. Futures rallied a modest 1% on the week.

On the charts, some steep downtrend resistance was broken, which is obviously near-term bullish. Some further short-covering/positioning ahead of the meeting may see prices rise somewhat further into the upper-$70s. But I can't emphasize enough that this OPEC decision is one of the biggest potential catalysts in the crude oil markets this year, and the result could cause a substantial price move.

Natural gas rallied last week in **very** volatile trade to finish the week higher by 4.3%. The natural gas market continues to be dominated by momentum traders. And with no clear trend in the market right now, it is best to let them have it for now. Fundamentally, though, the colder than expected start to winter has caused a spike in demand for heating needs, so it is likely that prices will remain above the $4.00 mark … with the potential of trading up to fresh four-month highs as inventory draws begin to trend higher.

Precious metals were well-bid last week as the dollar largely traded sideways. Gold futures rallied for the third week in a row, closing up 1.14%. The counter-trend rally remains intact for now, and further gains are possible as the rally in the dollar has cooled recently. But, as soon as the dollar rally resumes, I believe the sell-off in gold will resume as well, pushing futures down to an initial target of $1,100/oz.

Shifting over to the industrial metals, copper futures chopped sideways for most of the week before surging up through an important resistance level at $3.04 Friday on the surprise news of additional stimulus by the Chinese. But, the bulls failed to sustain the gains and futures fell back to almost flat by the close, failing to break out above the aforementioned resistance level. Bottom line, copper continues to threaten to break out to the upside, but has failed multiple times. Until we see that downtrend resistance broken, we can expect more sideways trade with the potential for declines toward the $2.98-$3.00 support band.

Currencies & Bonds

The Dollar Index surged to new highs last week, up 1%, thanks almost entirely to weakness in the euro and yen. The euro declined over 1% following the litany of Draghi's "dovish" press conferences coupled with disappointing November manufacturing PMIs. The euro collapsed hard on Friday, falling through 1.24 and closing on the lows. It is now challenging support at 1.2361, as we get closer to the HICP release Friday.

The yen was also very weak vs. the dollar, falling early last week when PM Abe announced the delay in the tax increase and snap elections. Dollar/yen, at one point late last week, traded just under 119 as the declines started to get a bit out of control. That acceleration prompted Finance Minister Taro Aso to defend the yen verbally last Thursday night which seems to have stemmed the tide of selling, for now.

Dollar/yen of 120 as a medium-term target is still very reasonable (and probably conservative), but I would expect some sort of a rally here just because this market is so oversold. That's a rally to short, however.

Turning to bonds, Treasuries were flat last week as weakness was nearly offset by a big Friday rally in the 30-year note. U.S. economic data and the FOMC minutes didn't really move Treasuries very much last week, and instead Europe remains the main influence.

Despite Draghi's dovishness , German bunds aren't buying it and they remain well-bid. Until we get actually improving data from Europe, German bonds will be well-supported, which means Treasuries will, too. European money continues to trump worsening domestic bond fundamentals. Have a good week — Tom

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*
12/13/13	FCG XOP	18.97 65.62	None	*Natural gas supplies low, increasing 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
September 2014	**Long Europe**	**HEDJ**	*On a longer time frame, Europe is poised to outperform other major developed economies as the ECB is proving their unanimous commitment to increasing the Balance Sheet. HEDJ is the equivalent of Japan's DXJ ETF and is the best way to gain exposure to Europe while hedging against currency depreciation.*

Strategy Update (11/6/14): The ECB continues to slouch towards more stimulus and QE, and at the October ECB meeting Mario Draghi did as good of a job as possible to "speak" dovish and reiterate that the ECB remains unanimously for more stimulus if needed. Additionally, the ECB staff has begun work on modeling more stimulus, which is the most concrete sign yet the ECB is planning to do "more" in early 2015. We continue to view dips as buying opportunities.

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 (11/3/14): The Bank of Japan shocked markets last week by announcing massive new monetary stimulus. I have been a Japan bull since late 2012, and I never thought the BOJ would go this far. The trend lower in the yen/higher in DXJ has clearly resumed, with a reasonable target for the dollar/yen now 115-120. This is a trend that will outperform over the coming months/quarters as the yen devalues and the BOJ/GPIF buys Japanese stocks.

Date Initiated	Strategy	Position (s)	Investment Thesis
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 (11/6/14): Treasuries are finally beginning to roll over here on the charts. The fundamentals for this trade remain decidedly negative, but once again money flows (specifically European) have recently been trumping the fundamen-

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Asset Class Dashboard

(Updated 11.24.14)

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**	*Stocks moved to new highs again last week continuing the "V" recovery from the October sell off. Decent economic data and expectations of global central bank easing pushed stocks higher, although late last week the market started to feel a bit stretched in the near term, and some consolidation is likely during the holiday shortened week.*

Best Idea: **Buy Regional Banks (KRE).**

Best Contrarian Idea: **Buy Energy (XLE)**

Commodities	**Bearish**	**Bullish**	*Commodities rose last week as gold and oil rallied. The former rose despite a stronger dollar, as more global central bank easing helped push gold higher, while oil rallied mostly on an oversold bounce. Despite the bounce in commodities, though, the dollar remains strong so it'll be hard for commodities to generate and real upside momentum*

Best Idea: **Buy Natural Gas (UNG)**

Best Contrarian Idea: **Buy Grains (DBA)**

U.S. Dollar	**Bullish**	**Bullish**	*The Dollar Index surged to new highs last week (up 1%) thanks primarily to weakness in the euro and yen, both of which declined more than 1% respectively vs. the dollar. With central bank policies diverging so materially (Fed tighter, everyone else "easier") the dollar uptrend will continue even If there is some short term consolidation.*

Best Idea: **Sell the Yen (YCS)**

Best Contrarian Idea: **Long British Pound (FXB)**

Treasuries	**Neutral**	**Bearish**	*Treasuries were flat last week despite the global equity market rally. Treasuries remain dominated by Europe in the short term, and while ECB President Mario Draghi was "dovish" last week, German bunds remained well bid, and until we see a sell off in those bonds, Treasuries will stay buoyant.*

Best Idea: **Short "long" bonds (TBT)**

Best Contrarian Idea: **Short High Yield Bonds (SJB)**