7:00's Report

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

December 5th, 2014

Pre 7:00 Look

- Futures are drifting slightly higher while international markets are enjoying broad gains on good economic data and ongoing stimulus hopes.
- European stocks are outperforming thanks to a much stronger than expected German Manufacturers' Orders report (2.5% vs. E: 0.5%) paired with optimistic comments from the German President who said current economic weakness will likely be overcome in the near term.
- Econ Today: Employment Situation (230K), Factory Orders (E: -0.3%) Fed Speak: Mester (8:45 AM), Fischer (2:45 PM)

Market	Level	Change	% Change
S&P 500 Futures	2073.50	1.50	0.07%
U.S. Dollar (DXY)	88.91	.175	0.20%
Gold	1202.60	-5.10	-0.42%
WTI	66.25	-.56	-0.84%
10 Year	2.257	-.030	-1.31%

Equities

Market Recap

Stocks whipsawed down, then up to fresh all-time highs on ECB headlines before finishing the day slightly in the red. The S&P 500 closed down 0.12%.

Europe was driving U.S. markets essentially all day yesterday. First, stocks fell sharply after European Central Bank President Mario Draghi failed to deliver the stimulus measures the market was looking for (sovereign QE). Draghi's comments easily masked the "market friendly" weekly jobless claims report that met expectations, falling back below the round 300K mark.

Then stocks reversed hard off the lows and quickly saw the S&P 500 trade up to a fresh all-time high. This was thanks to a Bloomberg report citing two unnamed ECB officials who said a QE program was being prepared for January.

But, the rally lost steam in the afternoon as energy stocks declined further and retail stocks traded heavy. ARO, DG and EXPR all sunk on disappointing earnings, leading the S&P to fade into the close.

Trading Color

Looking at market internals, yesterday's "flat" close in the S&P was not very encouraging. Small caps handily underperformed, falling 0.51%, while the Nasdaq almost matched the S&P, down 0.11%. High-beta stocks also underperformed their low-volatility counterparts by about 15 basis points.

As for sector trading, there was no definitive cyclical or defensive outperformance, but oil continues to have a heavy influence on the market. Yesterday's drop in oil prices weighed on the energy sector. XLE was the worst performer in the S&P, falling 0.87% to essentially match the declines in WTI futures. Industrials were a close second, dropping 0.50%.

Conversely, lower oil prices led the airlines to be among the best performers yet again yesterday, with some of the big names (DAL, UAL) adding upward of 4% on the day.

Basic materials and financials also outperformed.

Meanwhile Tech, Consumer Staples, Utilities, healthcare and consumer discretionary all traded in line with the S&P.

The S&P 500 traded to yet another all time high as the

Market	Level	Change	% Change
Dow	17,900.10	-12.52	-0.07%
TSX	14,469.95	-284.11	-1.93%
Brazil	51,426.87	-893.61	-1.71%
FTSE	6,717.63	38.26	0.57%
Nikkei	17,920.45	33.24	0.19%
Hang Seng	24,002.64	170.08	0.71%
ASX	5,335.33	-33.47	-0.62%
Prices taken at previous day market close.			

rally continues to demand respect. Initial support lies below at the 2062-2065 band.

Bottom Line

Yesterday's hectic day of European Central Bank news stirred up the markets and despite trading back in from their intra-day extremes both the Euro and HEDJ closed in the direction of the initial hawkish reaction, which for HEDJ was lower. And, although there may be some near term consolidation, we believe any material weakness should be seen as an opportunity to open new or add to existing HEDJ long positions as we continue to believe European equities are poised to outperform the S&P over the medium term.

Market	Level	Change	% Change
DBC	20.22	-.06	-0.30%
Gold	1208.00	-.70	-0.06%
Silver	16.545	.133	0.81%
Copper	2.914	.042	1.46%
WTI	66.72	-.66	-0.98%
Brent	69.59	-.33	-0.47%
Nat Gas	3.649	-.156	-4.10%
RBOB	1.7951	-.0119	-0.66%
DBA (Grains)	25.36	.08	0.32%
Prices taken at previous day market close.			

Jobs Report Preview (in case you missed it yesterday)

The importance of these jobs reports from a Fed policy standpoint is on the rise, and the risk to stocks is for the numbers to run too "hot" and pull forward Fed interest rate increases. As a result, wage increases and the unemployment rate are now just as important as the headline jobs number.

Wage Increases: 2.0% yoy - 2.2% yoy. If wage increases decline to below 2.0% (or stay at 2.0%) this will be slightly dovish. Conversely, if they spike above 2.2% (which is very unlikely given other data), that will be hawkish, as it'll imply the labor market is tightening significantly.

Unemployment Rate: < 5.8%. The unemployment rate is already low enough to justify a more "hawkish" stance on the surface, so a further decline in the headline UE rate or the U-6 (which measures underemployment) will be mildly "hawkish" as it'll further imply the labor market is structurally healing further.

The "Too Hot" Scenario: >300K job gains. A jobs number this strong would likely result in a pulling forward of rate increase expectations, and the markets would react **hawkishly**: Stocks, bonds and commodities would all decline, and the U.S. dollar would continue to rally.

The "Just Right" Scenario: 180K - 290K job gains. This is the "sweet spot" for this report, as it implies a still-healing labor market but not one that's so strong it would pull forward the date of the first rate hike. A number in this range shouldn't elicit too much of a market reaction as it's mostly priced in.

The "Too Cold" Scenario: <180K job gains. Given all the other employment metrics released in November, the chances of this number being a big miss are very remote. But, even if this is a big miss, don't expect markets to move too much as it'll probably be discounted as a statistical aberration.

Economics

ECB Rate Decision and Draghi Press Conference

The ECB meeting announcement was a non-event as expected yesterday morning. Draghi's press conference and the following events, however, were not.

Policy-makers voted to leave rates unchanged and made no announcement of further non-conventional easing measures. There were a few notable changes, however.

First, there was a subtle change in wording as "expectation" was replaced with "intention" in reference to "seeing the ECB balance sheet grow to the levels of early 2012," a dovish change.

Second, Draghi made it clear that unanimity in the Council is not necessary for further easing measures to be implemented including sovereign QE (making it clear QE is an option without the Germans on board)—also dovish. However, he did say the "signaling effect" would be much stronger if a broader consensus existed among voting members.

Draghi's press conference, on the other hand, was not well-received by the markets. He mentioned revisions for the worse for the 2015 growth forecasts but "punted" declaring any action (notably QE) until next month's meeting. This, as you would expect, caused a very hawkish reaction with the euro surging and EU equities plummeting, dragging US stocks down with them.

But, shortly thereafter, Bloomberg broke a story that two unnamed ECB officials "leaked" that the ECB was preparing a broad-based QE package for the January meeting. This caused much of the morning moves to violently reverse direction.

Bottom line, investors were initially disappointed by Draghi's "kick the can" testimony. However the leaked news that a sovereign QE program was in the works eased some of the market turmoil. But, based on yesterday's price action, investors are not 100% confident that QE is *really* in the works. As a result, the market may try and *force* QE out of the ECB at next month's meeting.

Weekly Jobless Claims

- Claims fell 17K to 297K vs. (E) 295K last week
- The 4 Week MA rose 4.75K to 299K

Takeaway

Volatility has edged up in the weekly jobless claims data recently, likely as a result of the holidays as claims jumped 22K the week before last only to fall back 17K last week. Yesterday's report showed 297K people filed for unemployment last week vs. (E) 295K. Data from the week prior was revised slightly higher from 313K to 314K. The smoother look at the data in the form of the 4 week moving average moved up 4.75K to 299K but importantly remains below the 300K mark, albeit barely.

Bottom line, despite some wide swings in the recent data figures, the general trend in weekly jobless claims remains favorable. The four-week moving average is sitting just below 300K, down from nearly 360K from the beginning of 2014. But, looking at the very near term, the slight uptick in claims data and mild miss in the ADP report Wednesday may be weighing slightly on the whisper number for today's official government jobs report.

Commodities

Commodities were split yesterday as energy fell slightly (ex-nat gas, which sold off sharply), while industrial metals rallied on China optimism, and gold was steady ahead of this morning's jobs report. The benchmark commodity tracking index ETF, DBC, was little-changed on the day.

Oil is still in the commodity spotlight, however yesterday's moves were limited. Futures attempted to sell off through near-term support toward $66/barrel multiple times yesterday morning, but the bulls held on and futures closed well off the lows of the day, down 0.92%.

Oil was heavy in the morning and quite likely would have broken down through key support if it wasn't the broad risk-on reaction the market had to the leaked "European QE" headlines that hit midmorning. Despite the midday rally, crude oil prices remained heavy amid continued chatter (notably from the Saudis) that the price will "stabilize itself," which is leading most traders and analysts to believe futures will fall further. We share that mindset and think it is probable that WTI will break the spike low of $63.72 before the end of the year.

Natural gas was the biggest mover yesterday with futures falling 4.15%. The recent sell-off accelerated yesterday thanks to a smaller than expected draw in stockpiles, according to government data released midmorning. The EIA reported that stockpiles declined by -22 Bcf vs. (E) -41 Bcf. On the charts, natural gas futures are quickly approaching the lows for the year of $3.54 (established in late Sept) but in doing so are becoming massively oversold. Bottom line, momentum will likely carry futures lower; however the risk for a violent, "wash out" short-squeeze is growing quickly. So keep an eye out for a sharp move back toward $3.90 if any materially bullish news breaks.

Moving to the metals, gold was largely range-bound yesterday and finished the session essentially unchanged. Gold was quiet despite broad moves in the dollar. However, because of the fact those moves were driven by trading in the euro due to the ECB—and not any material changes in our own Fed's policy outlook or economic data—gold trading remained quiet ahead of this morning's jobs report. The levels to watch in gold futures are Monday's high of $1,221 and a level of initial

Market	Level	Change	% Change
Dollar Index	88.695	-.298	-0.33%
EUR/USD	1.2373	.0063	0.51%
GBP/USD	1.5674	-.0011	-0.07%
USD/JPY	119.77	.00	0.00%
USD/CAD	1.1383	.0021	0.18%
AUD/USD	.8379	-.0022	-0.26%
USD/BRL	2.5907	.0392	1.54%
10 Year Yield	2.257	-.030	-1.31%
30 Year Yield	2.958	-.035	-1.17%

Prices taken at previous day market close.

(albeit weak) support at $1,190.

Industrial metals were broadly higher yesterday, led by copper which added 1.41%. Copper futures rose with Chinese equities yesterday on investor hopes for another rate cut by the PBOC after the central bank refrained from normally scheduled operations meant to remove money from the banking system. The PBOC in turn hopes to spur lending by banks. The technical picture of copper, however, remains rather bearish after futures broke down to a new 4-year low last week. Bottom line, copper fundamentals remain neutral at best while the technicals are decidedly bearish, and until we see a material break of downtrend resistance ($2.98), the path of least resistance will remain lower.

Currencies & Bonds

Currency markets were dominated by Europe yesterday as the ECB initially disappointed markets, causing a sharp move higher in the euro and a subsequent dip in the Dollar Index before those moves were reversed thanks to a Bloomberg article that discredited Draghi's comments during the press conference, suggesting that the ECB is preparing for full-blown QE to be announced in January. When the dust settled, the Dollar Index finished the day down 0.39%.

As we said earlier, the ECB meeting announcement was a non-event as expected but Draghi's testimony after the release was digested as rather hawkish, causing a sharp rally in the euro. But then, as fast as the rally began, the euro reversed on the leaked "QE in January" chatter from two anonymous European central bankers via Bloomberg. The euro finished the day up 0.60% yesterday.

As we mentioned in the *Economics* section, it is possible the market is going to "test" Draghi and the ECB here as investors are not fully confident he and the other policymakers will really follow through with sovereign QE in January. So, a near-term rally in the euro up until the January meeting toward as much as 1.27 is a distinct possibility.

Moving over to Asia, the yen sold off yesterday morning ,quietly touching 120 for the first time since July 2007. Part of the reason for the move were early poll results that were favorable for PM Abe (which also contributed to the NKY gains). Looking ahead, the shorts are still in control of the market; yet, the 120 level was a target for a lot of currency analysts and because of that we could see a profit-taking rally in the yen. However, such a move would likely be limited to somewhere between 118-119.

Commodity currencies were lower yesterday as the Loonie fell 0.18% and the Aussie was down 0.26%. There was no material catalyst for the mild sell-off; however both currencies remain pressured as global commodity prices continue to slide.

Moving to the bond market, Treasuries traded higher yesterday as they remain attractive to international investors on a relative basis. The 10-year note and 30-year bond rose 0.26% and 0.66%, respectively.

As we warned might be the case, Treasury futures seem to have "head faked" us again this week, rallying back above trend support after initially and moderately breaking down through that level on Tuesday.

Trader positioning also likely played a role in yesterday's rally as weak-handed shorts threw in the towel ahead of this morning's government jobs report. Especially, once Treasuries started to rise on the ECB announcement and Draghi press conference.

Bottom line (and at the risk of sounding like a broken record), international investment continues to trump the fundamentals of the U.S. bond market, propping up Treasury prices. And unfortunately it appears that is set to continue over the near term.

Have a good weekend,

Tom

Position Sheet

7:00's REPORT

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

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.			
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.			
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 fundamentals.			

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Asset Class Dashboard

(Updated 12.1.14)

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 hit new all time highs last week but declined marginally by weeks end thanks to a Friday dip that was due mainly to the collapse in oil prices. The general macro back drop remains positive for stocks, but we continue to be cautious about adding additional capital at current levels, as we think most of the good news out there is already priced in.*

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

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

Commodities	**Bearish**	**Bullish**	*Commodities collapsed, again, late last week as oil went into free fall following a "do nothing" OPEC meeting. There was massive general selling in the commodity space and a surging dollar weighed on precious and industrial metals. The near term outlook for commodities remains very negative.*

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

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

U.S. Dollar	**Bullish**	**Bullish**	*The Dollar Index closed flat last week thanks to a big Friday rally. The euro sold off Friday (but finished the week positive) following lack luster HICP data, while the yen weakened Friday after economic data missed estimates. Finally commodity currencies got crushed last week on lower oil and at or near multi-year lows.*

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

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

Treasuries	**Neutral**	**Bearish**	*Treasuries rallied last week thanks to a good 5 year Treasury auction and continued strength in German Bunds. Despite some indications EU economic data is starting to get better, Bunds remain well bid, and as long as they do, Treasuries will stay buoyant.*

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

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