7:00's Report

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

January 2nd, 2015

JNK: A bottom or rolling over? Like XLE, one of the first key question of 2015 is whether junk bonds have bottomed, or are rolling over after a extended bounce.

Pre 7:00 Look

- Futures are higher on the first trading day of 2015 as markets bounce from Wednesday's declines. Globally stocks were mixed as Asia broadly rallied while Europe is lower.
- Most of the news o/n was in Europe. ECB President Mario Draghi made more dovish comments while the EMU December PMI was revised slightly lower to 50.6 from 50.8. The euro broke below 1.21 vs. the dollar on the news.
- Econ Today: ISM Manufacturing Index (E: 57.5).

Market	Level	Change	% Change
S&P 500 Futures	2059.00	6.50	0.32%
U.S. Dollar (DXY)	91.035	.388	0.43%
Gold	1183.30	-.80	-0.07%
WTI	53.45	.158	0.34%
10 Year Yield	2.170	-.020	-0.91%

Equities

Market Recap

Stocks fell modestly on the final day of 2014 as year end positioning and new lows in oil weighed on the markets. The S&P 500 ended down 1.03% but up 11.39% for 2014.

Stocks were lower almost from the outset Wednesday, as an early drop in oil, lack luster Pending Home Sales, and a disappointing Chicago PMI weighed on markets. But, it does need to be said that trading was slow and volumes were light.

News evaporated shortly after the economic data at 10 AM Wednesday and stocks were left to follow oil and oil stocks for the remainder of the session, and as oil and XLE traded lower, so too did the broad averages. News flow was very quiet in the afternoon and stocks continued to slip, hitting their lows of the day during the final hour of trading, although all the price action Wednesday came on predictably low volume. But, very quietly the S&P 500 is down more than 1% on the week as we start 2015.

Trading Color & Bottom Line

Given it was the last trading day of the year and subject to extreme last minute tax selling, positioning, rebalancing, etc. again there's not a lot to read into the internals.

Oil seemed to be the dominant influence on sector trading Wednesday as energy stocks and industrials lagged, while retail, consumer names and transports all outperformed. But, again, none of the moves were material.

Looking ahead to the start of 2015 we can expect today to again have "holiday like" trading. Positioning and al-

Market	Level	Change	% Change
Dow	17,823.07	-160.00	-0.89%
TSX	14,632.44	-7.60	-0.05%
Brazil	50,007.41	-586.41	-1.16%
FTSE	6,563.54	-2.55	-0.04%
Nikkei	17,450.77	-279.07	-1.57%
Hang Seng	23,85.82	252.78	1.07%
ASX	5,435.93	24.93	0.46%
Prices taken at previous day market close.			

location of new money will be the driver of trading in a thin market today, as everyone won't truly get back to work until Monday.

Oil, JNK and the ruble remain the leading indicators of this market, and now that end of year shenanigans are over, the key will be whether the bottom is truly "in" in those names, or whether we are rolling over again. So, like in mid-December, watch XLE, JNK, RSX (or the ruble if you have Bloomberg) in that order.

Market	Level	Change	% Change
DBC	18.44	-.15	-0.81%
Gold	1184.00	-16.40	-1.37%
Silver	15.675	-.601	-3.69%
Copper	2.8215	-.0325	-1.14%
WTI	53.74	-.38	-0.69%
Brent	57.65	-.25	-0.43%
Nat Gas	2.918	-.176	-5.69%
RBOB	1.4815	.0104	0.71%
DBA (Grains)	24.859	-.221	-0.88%
Prices taken at previous day market close.			

Economics

Pending Home Sales

- November Pending Home Sales Index rose 0.8% vs. (E) 0.5%.

Takeaway

Pending home sales helped to break a streak of disappointing November housing data. Prior to the Pending Home Sales report, every November housing indicator had missed versus expectations.

November Housing Indicators	Actual	Expectation
Existing Home Sales (M)	4.93M	5.20M
Housing Starts (M)	1.028M	1.038M
Housing Permits (M)	1.035	1.060
New Home Sales (k)	438	460
Cash-Shiller HPI (Y/Y)	4.50%	4.50%
Pending Home Sales	0.80%	0.50%

This hasn't been covered much with all the focus on oil, Russia and year end, but the data definitely implies we are seeing the housing recovery level off.

That sentiment was echoed by Robert Shiller on CNBC Wednesday, but before we get worried about housing, some context is necessary.

While the housing market may indeed be levelling off, the simple fact is that it's still on solid footing, and with rising wages (hopefully) in 2015 and the strengthening job market, economic fundamentals don't point to any material risks for housing (yes, rates will likely start to rise in 2015 but that isn't a causal negative on housing as long as wages and the job market continues to improve).

Bottom line, in order for the broader economic recovery to continue, housing needs to at least be stable (so these housing numbers are important with regards to supporting material further gains in stocks in 2015). But, any belief that these disappointing numbers represent a material threat to the economy (like we saw 6-7 years ago) are overblown. Housing needs to continue to get better to help stocks move materially higher, but if housing stagnates or even comes in a bit, it does not mean a recession is coming, as some are warning.

Jobless Claims

- Weekly Claims rose to 298K vs. (E) 286K

Takeaway

Weekly jobless claims rose 17K to 298K vs. (E) 286 last week causing the 4 week moving average to edge up a slight 250 to 290.75K. But, the weekly report is taken with a grain of salt this time of year as the holidays can skew the figures. So, bottom line, the overall trend in jobless claims remains favorably lower which is consistent with other measures of the job market.

Commodities

Commodities were lower across the board on Wednesday largely thanks to end of the year positioning. The commodity ETF, DBC, fell 0.83%.

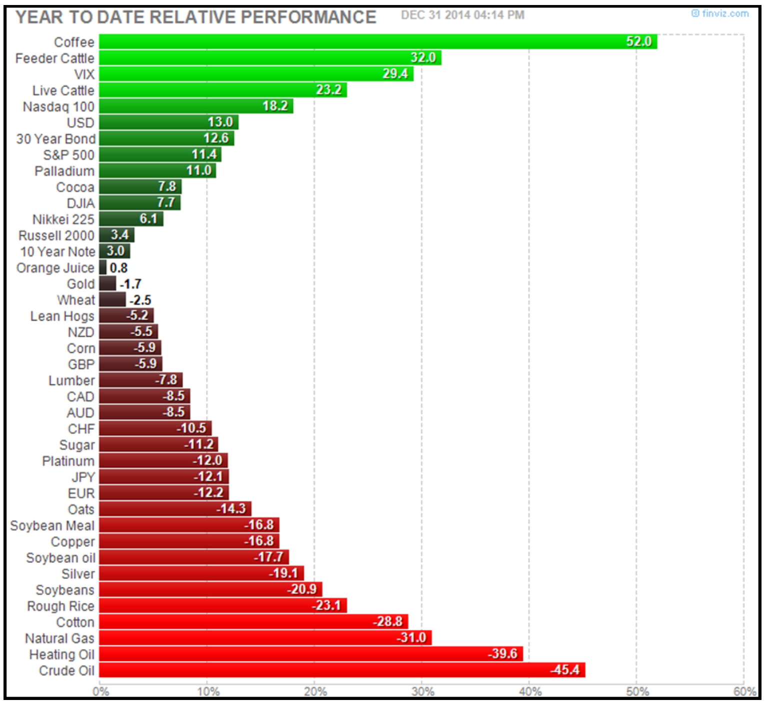
It was inventory day for the energy space Wednesday including crude oil, the refined products and also natural gas thanks to the holiday (nat gas is usually a Thursday report).

Beginning with crude oil and the products, the data reported by the EIA was mixed. Crude oil supplies fell 1.8M barrels last week vs. (E) -600K (slightly bullish), RBOB gasoline inventories rose 2.9M bbls vs. (E) 1.6M (bearish), and Distillate supplies rose 1.8M bbls vs. (E)

1.4M (slightly bearish. The report spurred a sharp rally as shorts covered in thin volume, however the bids ran out near trend resistance towards $53.75 and futures fell back towards session lows.

Bottom line, crude oil and the refined products are still in a well defined downtrend confirmed by bearish technicals, most notably the fresh multi year lows we saw Wednesday.

As for the EIA's natural gas report, it was bearish. Natural gas inventories reportedly fell just –26 Bcf last week vs. (E) -47 Bcf, a much smaller draw than the week priors –49 Bcf.



The mild temperatures across the country for the month of December saw natural gas futures fall suddenly and sharply into a bear market over the last month, and those losses were extended on Wednesday as some end of the year selling amplified the weakness. But, forecasts for January suggest we could see an uptick in heating driven demand which could potentially spur an early 2015 rally in natural gas, but we will remain cautiously bearish until the market conditions change.

The dollar surged up to fresh highs on Wednesday which put pressure on industrial and precious metals alike. Copper futures, which had been drifting lower in choppy trade for most of the month of December continued to do so Wednesday, falling 1.10% on the day. The trend in industrial metals remains lower for the near term as investors continue to question the health and growth potential of the global economy while the dollar continues to rally to multi year highs.

Market	Level	Change	% Change
Dollar Index	90.620	.341	0.38%
EUR/USD	1.2098	-.0058	-0.48%
GBP/USD	1.5583	.0026	0.17%
USD/JPY	119.84	.38	0.32%
USD/CAD	1.16	-.001	-0.09%
AUD/USD	.8172	-.0009	-0.11%
USD/BRL	2.657	-.0449	-1.66%
10 Year Yield	2.170	-.020	-0.91%
30 Year Yield	2.749	-.009	-0.33%

Prices taken at previous day market close.

Meanwhile, gold futures fell back 1.42% on Wednesday thanks to a better than expected housing report, the stronger dollar, and general year end positioning noise. We remain cautious bears on gold as we believe the strengthening dollar will continue to weigh on precious metals. However I say we are "cautious" because when the bearish gold trade gets crowded, the risk for short squeezes materially increases. Prime examples being the three waves of short squeezes we saw in December on 12/1, 12/9 and 12/26. Point being, the general trend remains lower, but if you're looking to get short, wait for one of these squeezes to lay out those positions.

Currencies & Bonds

The Dollar finished 2014 on a high note (and literally at the highs of the year) in quiet trading. The strength in the Dollar Index came mostly from the drop in the euro, which fell .45% and hit new multi-year lows on the last trading day of 2014 (and that weakness is continuing this morning).

The reason for the weakness, other than year end positioning, was commentary by ECB member Peter Praet, who said that lower oil prices raise the potential for "more" QE in the EU because inflation expectations are dangerously low.   Those comments were re-enforced by Mario Draghi overnight who cautioned the EU has a growing price stability problem.

Going back to Praet's comment, though, it didn't reveal anything new, but it was the fact that it was from a German that weighed on markets. Bottom line, the general drum beat towards QE in the EU is beating more loudly, and even despite Greek political uncertainty, the expectation is for QE to be announced by the ECB on January 22nd.

Outside of the euro declines, Wednesday was a quiet day in the currency markets as news was light and none of the other major currencies moved more than .30%.

The bond markets were also mostly quiet on Wednesday (bond markets closed early) as the thirty year finished up .24% while the ten year rose .19%. Bonds largely ignored the economic data (Pending Home Sales and Chicago PMIs).

Getting a bit more granular, junk bonds and the ruble (both of which are a barometer of oil contagion) declined Wednesday. JNK the junk bond ETF) is now down 3 days in a row while the ruble traded back through 60/ dollar.

I point that out only because, like energy stocks and XLE, it's not definitive that oil or the oil contagion assets have bottomed, and if this past 2 week rally was just a bounce in a still downward trending market, then it may be an ugly start to 2015 for stocks.

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*
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 fundamen-			

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Asset Class Dashboard

(Updated 12.29.14)

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 rallied just under 1% last week mostly on year-end positioning. The move higher extended the rally to over 100 points in less than 8 trading days, as a stabilization in oil prices and the Russian Ruble has led to massive short covering and buyers chasing into year end.*

Best Idea: Buy Retail (RTH).

Best Contrarian Idea: Buy Energy (XLE)

	Near Term Trend	Long Term Trend	Market Intelligence
Commodities	**Bearish**	**Bullish**	*Commodities were lower again last week as oil resumed its declines, although it did not make new lows. Oil continues to try and put in a bottom here, but it's unclear if a bottom is truly "in." Gold was the only commodity to finish higher last week higher, as it rallied in low volume trading Friday on general geo-political concerns.*

Best Idea: Buy Natural Gas (UNG)

Best Contrarian Idea: Buy Grains (DBA)

	Near Term Trend	Long Term Trend	Market Intelligence
U.S. Dollar	**Bullish**	**Bullish**	*The Dollar Index again hit new multi-year highs last week following the very strong GDP report, which further highlighted the growing disparity between the US economy (getting stronger) and everyone else (stagnant). Because of that, we expect the dollar rally to continue.*

Best Idea: Sell the Yen (YCS)

Best Contrarian Idea: Long British Pound (FXB)

	Near Term Trend	Long Term Trend	Market Intelligence
Treasuries	**Neutral**	**Bearish**	*Treasuries declined again last week following the strong GDP report, although there remains plenty of support for Treasuries and this failed Greek election will further support Treasuries in the near term. But, it does appear that markets are starting to consider negative domestic bond fundamentals, although again we need some progress in Europe before we will see any material downside in Treasuries.*

Best Idea: Short "long" bonds (TBT)

Best Contrarian Idea: Short High Yield Bonds (SJB)