SEVENS REPORT

EVERYTHING YOU NEED TO KNOW ABOUT THE MARKETS BY 7AM EACH MORNING IN SEVEN MINUTES OR LESS

January 2, 2024

Pre 7:00 Look

- Futures are slightly lower to start 2024 amid concerns about China's economy and rising geopolitical tensions.
- Economically, China's government-issued PMI fell to 49.0 vs. (E) 49.6 in December while President Xi Jinping made some cautious comments on the state of the economy. In Europe, the December PMI rose to 44.4 vs. (E) 44.2.
- Geopolitical tensions sent oil prices higher after the U.S. Navy sunk three Iran-backed Houthi vessels this weekend.
- Econ Today: Final December Manufacturing PMI (E: 48.2), Construction Spending (E: 0.6%). No Fed speakers today.

Market	Level	Change	% Change
S&P 500 Futures	4815.50	-4.50	-0.09%
U.S. Dollar (DXY)	101.663	.330	0.33%
Gold	2084.10	12.30	0.59%
WTI	73.32	1.67	2.33%
10 Year Yield	3.946	.086	2.28%

Equities

Market Recap

The S&P 500 drifted slightly higher last week in very quiet trade and finished 2023 with a large 24.23% gain.

Trading last week was very quiet and largely devoid of any noteworthy catalysts as there was no important economic data, Fed/central bank speak or geopolitical events. As such, positive momentum largely drove markets as the newswires were quiet and investors and traders wanted to simply end a very positive 2023 without any surprises or upsets.

The S&P 500 drifted higher on Tuesday thanks mostly to a drop in short-term Treasury yields following a solid 2-year Treasury auction. Wednesday and Thursday saw the S&P 500 never stray too far from the unchanged level with minimal news and volatility. On Friday the S&P 500 dipped modestly (down 0.4%) but that was due mostly to year-end positioning and not in reaction to any substantial news.

The week between Christmas and New Years is usually quiet, especially when the market is up substantially, and that was true again this time as investors and traders finished a strong bounce-back year.

Five Market Assumptions to Know As We Start 2024

The S&P 500 is starting 2024 trading at a very lofty 19.5X valuation and while I'm not going to say that valuation is unjustified, I will say that valuation makes several key, positive assumptions about critical market influences in the coming year. And how reality matches up with those assumptions will determine whether stocks extend the rally (and the S&P 500 hits new highs and makes a run at 5,000) or gives back much of the Q4 Santa Claus rally.

As such, I want to start 2024 clearly defining the five most important assumptions investors are making right now, because it's how these events occur vs. these assumptions, and not absolute values, that will determine if stocks and other assets rise or fall in Q1 and 2024.

Market	Level	Change	% Change
Dow	37,689.54	-20.56	-0.05%
TSX	20,958.44	29.06	0.14%
Stoxx 50	4,536.38	14.73	0.33%
FTSE	7,731.67	-1.57	-0.02%
Nikkei	33,464.17	-75.45	-0.22%
Hang Seng	16,788.55	-258.84	-1.52%
ASX	7,627.79	36.97	0.49%
Prices taken at previous day market close.			

Assumption 1: Fed cuts rate six times for 150 basis points of easing and a year-end fed funds rate below 4.0%. The main factor behind the S&P 500's big Q4 rally was the assumption that the Fed was done with rate hikes and would be cutting rates early and aggressively in 2024. *How do we know this is a market assumption?* Fed fund futures. According to fed fund futures, there's a 70%-ish probability the fed fund rates ends 2024 between 3.50% - 4.00%.

Market	Level	Change	% Change
DBC	22.04	-.12	-0.54%
Gold	2075.20	-8.30	-0.40%
Silver	24.05	-.33	-1.34%
Copper	3.8945	-.0300	-0.76%
WTI	71.46	-.31	-0.43%
Brent	77.04	-.11	-0.14%
Nat Gas	2.495	-.062	-2.42%
RBOB	2.0838	-.0014	-0.07%
DBA (Grains)	20.72	-.33	-1.57%
Prices taken at previous day market close.			

Assumption 2: No Economic Slowdown. Markets haven't just priced in a soft landing, they've priced in effectively no economic slowdown as investors expect growth to remain resilient and inflation to decline, the oft-mentioned "Immaculate Disinflation," a concept that's possible, but to my knowledge has never actually happened. *How do we know this is a market assumption?* The market multiple. The S&P 500 is trading at 19.5X the $245 expected S&P 500 earnings expectation. A 19.5X multiple is one that assumes zero economic slowdown (if markets were expecting a mild slowdown, a 17X-18X multiple would be more appropriate).

Assumption 3: Solid earnings growth. Markets are expecting above average earnings growth for the S&P 500 to help power further gains in stocks. *How do we know this is a market assumption?* The consensus expectations for 2024 S&P 500 earnings per share are mostly between $245-$250. That's nearly 10% higher than the currently expected $225 per share earnings for last year (2023), which points to very strong annual corporate earnings growth.

Assumption 4: No additional geopolitical turmoil. Despite the ongoing Russia/Ukraine war, Israel/Hamas conflict and escalating tensions between the U.S. and Iranian-backed militias throughout the Middle East, the market's assuming no material increase in geopolitical turmoil. *How do we know this is a market assumption?* Oil prices. If markets were nervous about geopolitics, Brent Crude prices would be solidly higher than the current $77/bbl. Oil prices in the high $80s to low $90s reflect elevated geopolitical concern while prices above $100/bbl reflect real worry.

Assumption 5: No domestic political chaos. 2024 is an election year in the U.S. The Republican front runner, Donald Trump, is facing a long list of various civil and criminal charges along with challenges to whether his name will be on the ballot in certain states. Meanwhile, there has been no long-term compromise on funding the government so shutdown scares remain a real possibility. And that's before we get into the heart of election season later this year. *How do we know this is a market assumption?* Treasury yields. A 3.80%-ish yield on the 10-year Treasury does not reflect much domestic political angst. If markets become nervous about the U.S. political situation and/or fiscal situation in the U.S., the 10-year yield would be sharply higher than it is now (well above 4.00%, like we saw in the late summer/early fall).

Bottom line, these market assumptions aren't necessarily wrong. Events could unfold the way the market currently expects. But these assumptions are aggressively optimistic and it is how events unfold versus these expectations and not on an absolute scale that will determine how stocks and bonds trade to start the year.

Economics

Last Week

There was little economic data last week and what few reports we did get didn't alter the current market outlook of 1) No significant economic slowdown and 2) A continued decline in inflation. That said, there were hints of disagreement in last week's reports, especially in the last week of a very positive year.

The most notable report from last week was jobless claims, which rose 218k, above the 210k estimate. Meanwhile, continuing claims rose to 1.875 million from 1.861 million last week. But while both numbers showed some small deterioration in the labor market, neither number was enough to imply we are seeing real softening in the labor market and as such, neither number moved markets. As we start a new year, for these indicators to signal some real deterioration in the labor market we'd need to see jobless claims rise towards and above 250k while continuing claims rise above 1.90M.

The other notable economic indicator from last week was the Case-Shiller Home Price Index, which registered a new all-time high in national home prices. The index rose 0.6% m/m and met estimates and 4.9% y/y vs. (E) 5.0%. As we start the year, falling shelter prices are the key assumption underlying expectations for a continued decline in inflation. But many housing metrics remain, generally speaking, buoyant. So, while it's reasonable to expect some downward movement in shelter costs, the reality is housing prices are not declining substantially and if CPI does not decline as expected in early 2024 that will jeopardize expectations for Fed rate cuts early this year.

This Week

The year starts off with a proverbial "bang" from an economic standpoint as we get the three most important economic reports of each month over the next four days. And now that the Fed has dovishly pivoted, "bad" data won't remain "good" for stocks very long, so expect the markets to begin to react negatively to soft reports here. And the reason why is clear: Now that the Fed has pivoted, bad economic data just means an increased chance of an economic slowdown, something that is not priced into markets with the S&P 500 trading at a 19X multiple.

The key report this week is Friday's jobs report and while we'll have our regular preview in Thursday's Report, the key will be a solid, yet unspectacular, number of job adds with a slight drift higher in the unemployment report. Put simply, markets continue to need Goldilocks jobs data to support stock prices, but the margin for error of the report is much smaller now that the Fed has dovishly pivoted.

The next most important economic reports this week come tomorrow and Friday via the ISM Manufacturing and Services PMIs. The ISM Manufacturing PMI remains below 50 and is expected to stay there while the ISM Services PMI remains slightly above 50. The reason these two reports are important is because if both of these reports drop below 50 for a few months, that's a very accurate historical indicator of a looming economic slowdown. Point being markets will want to see improvement in the ISM Manufacturing PMI and stability (so staying comfortably above 50) in the Services PMI.

The final important economic reports of the week are labor market related via tomorrow's JOLTS (Job Openings and Labor Turnover Survey) and Thursday's weekly jobless claims. As mentioned, the labor market broadly remains strong but not too hot and markets will want to see data that reinforces strong employment, but not so strong it increases wages and a bounce in inflation.

Bottom line, now that the Fed has dovishly pivoted, investors will want to see stability in the economic data above all else in Q1, because if economic data starts to roll over from here, more expected Fed rate cuts won't help (they'll be too late) and with the S&P 500 trading above 19X next year's earnings, there simply is zero economic slowdown priced into stocks (although Treasuries would rally in the face of soft economic data).

Market	Level	Change	% Change
Dollar Index	100.97	.06	0.06%
EUR/USD	1.1046	-.0015	-0.14%
GBP/USD	1.2753	.0020	0.16%
USD/JPY	141.00	-.41	-0.29%
USD/CAD	1.3230	.0001	0.01%
AUD/USD	.6819	-.0011	-0.16%
USD/BRL	4.8527	-.0041	-0.08%
10 Year Yield	3.866	.016	0.42%
30 Year Yield	4.019	.031	0.78%
10's-2's	-38 bps		
Date of Rate Cut	March 2024		
2024 YE Fed Funds	3.85%		
Prices taken at previous day market close.			

Commodities

Commodities declined broadly last week thanks mostly to declines in oil as geopolitical tensions eased slightly. The commodity ETF, DBC, fell 1% last week and declined 10.6% for 2023.

Oil was volatile last week on geopolitical headlines as two weeks ago U.S. forces struck Iranian-backed militias in retaliation for attacks on U.S. forces and that increased the geopolitical risk premium in oil.

However, there was no follow through from the U.S. or Iran and news that Maersk would resume transiting the Suez Canal midweek pressured oil and most other energy commodities and crude ended last week solidly lower, down by 3%. Notably, Maersk announced over the weekend they were again suspending movement though the Suez Canal given attacks on its ships over the past few days and that will keep tensions elevated.

Looking forward, geopolitics will remain an important influence on oil but, barring a major escalation in the Russia/Ukraine war or Israel/Hamas conflict, the larger supply/demand picture will drive oil prices and as we start the year there remain real concerns 1) If global demand can stay resilient (there are hints the global economic is slowing) and 2) If OPEC+ can remain disciplined on supply (they're actions late last year underwhelmed traders) and as such the outlook for oil prices remains mixed over the longer term.

The best performer in the energy space last week was Natural Gas, which rose nearly 3% thanks to a larger-than-expected storage draw and forecasts for colder-than-expected temperatures over the coming weeks.

Gold was little changed on the week as there was little data or Fed speak to trade off. Midweek dollar declines helped boost gold but the impact was modest, although gold remains within striking distance of the new all-time highs hit in early December. Looking forward, we can expect gold to continue to trade inversely off the U.S. dollar and as long the dollar remains broadly under pressure the outlook for gold will remain positive.

Currencies & Bonds

The dollar extended its decline last week and briefly traded below 101 for the first time since last summer. The Dollar Index lost 0.4% last week and was down 2.1% for 2023.

The Dollar Index has been rightly under pressure since the Fed's dovish pivot in mid-December and that continued last week thanks mostly to momentum and after jobless claims rose more than expected (although they remained low on an absolute basis). However, with little else to trade off, the rise in claims combined with downward momentum to push the dollar lower.

As we start 2024, markets view the Fed as the most likely major central bank to cut rates first (currently expected to cut in March) and until that changes the dollar will be unable to rally and it's likely only a matter of time until it tests 100. Now, that perception the Fed will be the most-dovish major central bank can change in one of a few ways. The Fed gets more hawkish and pushes back against March rate cut expectations, U.S. economic data or inflation rebounds, EU or BOE officials suddenly get dovish and forecast rate cuts in early 2023, or economic data nosedives in the EU or UK. However, barring any of those events the path of least resistance for the dollar is lower.

In Treasuries, yields were little changed last week as the 10 year dipped modestly midweek but recovered to decline just 2 basis points over the past five days, while the 2-year Treasury yield fell further, declining 8 basis points as markets reacted to the uptick in jobless claims.

Also impacting yields were mostly strong Treasury auctions, specifically solid 2- and 5-year auctions earlier in the week that reinforced strong international demand for short-term U.S. debt. A less-positive 7-year auction late last week pushed the 10-year yield higher although again it's a mistake to look too much into just one auction result. For the full year 2023, there was extreme volatility in Treasury yields but the 2-year yield finished 2023 close to where it started the year while the 10-year yield finished about 30 bps higher.

Looking forward, with the Fed now having pivoted, data will be the key influence on yields. And unlike 2023, large and consistent declines in yields will not be the positive for stocks they were in 2023 because the Fed has already pivoted. Instead, continued large declines in yields will be viewed as providing an economic warning and the best case for yields as we start 2024 is that they drift sideways to slightly lower amidst Goldilocks economic data (i.e., not so good the Fed gets less dovish and not so bad it increases recession worries).

Have a good week,

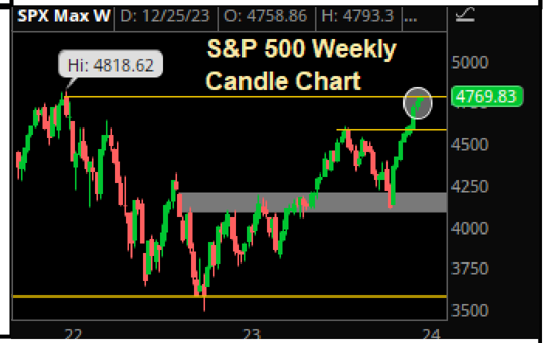
Tom

SEVENS REPORT

Technical Perspectives (Updated 12/31/2023)

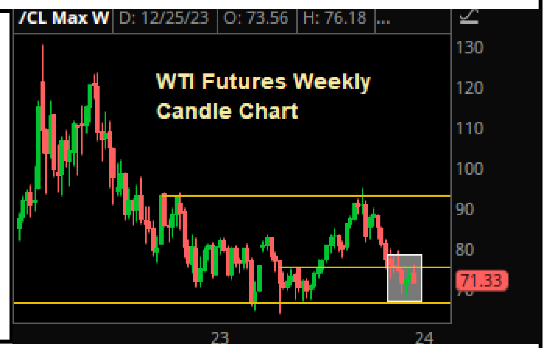
S&P 500

- Technical View: **The medium-term trend in equities flipped bullish** to start December as the S&P 500 rallied to fresh 2023 highs.
- Dow Theory: **Bullish (since the week of July 10, 2023)**
- Key Resistance Levels: 4783, 4818, 4850
- Key Support Levels: 4555, 4496, 4415



WTI Crude Oil

- Technical View: The price action in oil deteriorated in H2'23 but continues to hold above the 2023 lows, leaving the outlook neutral.
- Proprietary Model: **Neutral (since the week of November 6, 2023)**
- Key Resistance Levels: $73.82, $75.02, $77.72
- Key Support Levels: $71.15, $69.87, $68.01



Gold

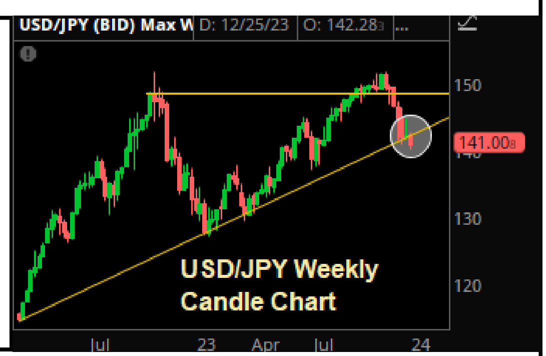
- Technical View: Gold futures broke out to fresh all-time in late 2023 shifting the technical outlook decidedly in favor of the bulls.
- Proprietary Model: **Bullish (since the week of November 27, 2023)**
- Key Resistance Levels: $2089, $2108, $2152
- Key Support Levels: $2033, $2000, $1967

10-Year T-Note Yield

- Technical View: The 10-year yield has pulled back considerably since the October highs, but the "V-shaped" top has not seen a bearish "lower low" established yet.
- Proprietary Model: **Bullish (since the week of August 21, 2023)**
- Key Resistance Levels: 3.908, 4.033, 4.121
- Key Support Levels: 3.789, 3.608, 3.405

Dollar/Yen

- Technical View: The USD/JPY violated a longstanding uptrend line to end 2023 shifting the technical outlook from bullish to neutral.
- Proprietary Model: **Neutral (since the week of December 25, 2023)**
- Key Resistance Levels: 142.11, 143.83, 145.46
- Key Support Levels: 140.18, 138.78, 137.70



SEVENS REPORT

Fundamental Market View
(Updated 12/31/2023)

Near-Term General U.S. Stock Market Outlook

This is designed to provide a snapshot of our near-term (1 month) outlook for stocks. For general equity market exposure, we use a mix of SPHB (S&P 500 High Beta) and SPLV (S&P 500 Low Volatility) to create an aggressive, neutral or defensive stance on general equity market exposure.

Near Term Stock Market Outlook: **Cautious** **SPHB: 25% SPLV: 75%**	*Stocks were little changed last week in very quiet trade as investors wanted a quiet end to a very strong 2023 as the S&P 500 rose more than 24% on the year.*

Tactical Allocation Ideas:

- **What's Outperforming: Growth factors, tech, consumer discretionary and communication services, the worst performers in 2022, have outperformed YTD. However, higher yields remain a headwind and as such we don't think this outperformance will last over the longer term.**
- **What's Underperforming: Defensive sectors and value have underperformed YTD, but are still massively outperforming since the bear market started in 2022, and since our primary concern in 2023 is economic growth, we think this underperformance will be temporary.**

Long Term Fundamental Outlook for Other Asset Classes

	Fundamental Outlook	Market Intelligence
Commodities	**Neutral**	*Commodities declined slightly following a reduction in geopolitical tensions and despite a continued decline in the U.S. dollar.*
US Dollar	**Neutral**	*The Dollar Index dropped further to fresh multi-month lows last week thanks to momentum and a slight uptick in weekly jobless claims.*
Treasuries	**Turning Positive**	*The 2-year Treasury yield fell modestly on strong short-term auction demand while the 10-year yield was little changed as there was no notable economic data or central bank speak.*

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.