1/25/2024

SEVENS REPORT

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

January 25, 2024

Pre 7:00 Look

- Futures are little changed following a mixed night of earnings and ahead of the ECB rate decision.
- Earnings were mixed overnight with cautious TSLA guidance (TSLA down –7% pre-market) offsetting other solid tech results from IBM, NOW and others.
- Econ Today: ECB Rate Decision (E: No change), Durable Goods (E: 1.0%), Advanced Q4 GDP (E: 2.0%), Jobless Claims (E: 200K), New Home Sales (E: 650K).
- Earnings: AAL ($0.06), LUV ($0.11), VLO ($2.95), SHW ($1.80), INTC ($0.48), V ($2.33), TMUS ($1.90), COF ($2.50).

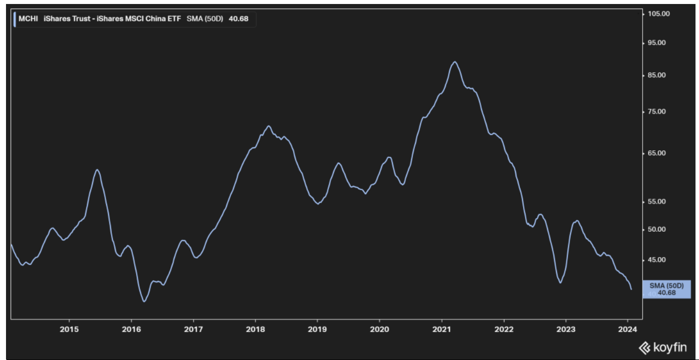
Market	Level	Change	% Change
S&P 500 Futures	4,900.75	2.75	0.06%
U.S. Dollar (DXY)	103.22	-0.01	-0.01%
Gold	2,017.30	1.20	0.06%
WTI	76.19	1.10	1.46%
10 Year Yield	4.16%	-0.02	-0.51%

Equities

Market Recap

Stocks advance to new highs yesterday amid strong mega-cap earnings and surprise stimulus measures announced in China. But hawkish money flows in the back half of the U.S. session saw the S&P 500 retreat from 4,900 to close with only an incremental gain of 0.08%.

Stocks gapped up to yet another set of fresh record highs yesterday morning amid optimism about stimulative rate cuts from the People's Bank of China aimed at stabilizing the economy and supporting new growth, while economic data out of Europe was underwhelming



MCHI: There's not much in the markets that's trading at 10 year lows, but Chinese stocks are. And with the government possibly getting serious about stimulus, there could be an opportunity for a solid rally.

(again) rekindling hopes for sooner-than-later rate cuts from the ECB. On earnings front, NFLX was up 10% in the pre-market thanks to strong subscriber numbers that further bolstered the tech space, which has led markets higher so far in 2024.

Traders faded the early gains ahead of the only notable economic report in the U.S. yesterday, the Flash Composite PMI for January, which came in quite a bit stronger than expected sending yields higher and stocks retreating modestly from early session highs.

Stocks were quick to stabilize, however, and the S&P 500 started to rally with oil in late-morning trade after a fundamentally mixed but bullishly received EIA report combined with optimistic commentary from the Bank of Canada's Macklem, who said he did not think a recession was needed to get inflation back to target.

Stocks sprinted to new highs with the S&P 500 briefly pushing beyond the 4,900 level before the market abruptly reversed lower at the top of the 1 p.m. hour due to a very weak 5-Yr Treasury Note auction. The bid-to-cover, a measure of demand, fell to 2.31 from 2.50 at the previous auction while the yield awarded was

Market	Level	Change	% Change
Dow	37,806.39	-99.06	-0.26%
TSX	21,025.78	-8.81	-0.04%
Stoxx 50	4,553.78	-10.33	-0.23%
FTSE	7,515.63	-12.04	-0.16%
Nikkei	36,236.47	9.99	0.03%
Hang Seng	16,211.96	312.09	1.96%
ASX	7,555.36	36.17	0.48%
Prices taken at previous day market close.			

4.055%, a full 2 basis points below the pre-auction, when-issued yield. Both statistics show very weak demand and triggered a spike in both Treasury yields and the dollar, which poured cold water on the squeeze rally in the front half of the session.

Market	Level	Change	% Change
DBC	22.34	.19	0.86%
Gold	2,014.00	-11.80	-0.58%
Silver	22.79	.33	1.46%
Copper	3.8740	.0805	2.12%
WTI	75.16	.79	1.06%
Brent	80.10	.55	0.69%
Nat Gas	2.679	.229	9.35%
RBOB	2.2150	.0049	0.22%
DBA (Grains)	21.51	.17	0.80%
Prices taken at previous day market close.			

The S&P 500 bled steadily lower into the final hour before ending what was initially a very strong session at new record highs, essentially unchanged.

Trading Color

Wednesday resembled most of last week as strength in the tech sector made the performance of the S&P 500 look much better than what actually occurred in the "rest" of the market and that was evident on an index and sector level.

On an index level, the Nasdaq outperformed and rose modestly (0.4%)% while the tech heavy S&P 500 rose 0.08%. The less-tech-heavy Dow Industrials declined 0.3% while the Russell 2000 fell 0.7%. All four major indices finished well off the intraday highs.

On a sector level, only four of the seven sector SPDRs were higher on the day and three of them were driven by either earnings or oil inventory data. Energy was the best performer and the only sector SPDR to rise more than 1% and the reason was clear: Higher energy prices. Oil rallied solidly and natural gas surged more than 8% and the net result was a short-term rally in XLE, which gained 1.43%.

Tech and tech-related sectors also traded well thanks to ASML earnings boosting the entire semiconductor space (NVDA and AMD both rallied in sympathy with ASML and helped send XLK higher by 0.7%) while the strong subscriber adds in NFLX boosted the communications sector (XLC gained 0.6%). Financials were the only non-tech/non-energy sector to rally as XLF rose a modest 0.4% on continued bank earnings momentum.

Turning to the laggards, defensive sectors and materials declined the most as Real Estate (XLRE) dropped 1.4% while Utilities also fell 1.4%. There wasn't any specifically damning news for either sector, but the stronger-than-expected flash PMIs caused recent money to continue to rotate out of defensive sectors and towards pockets of strength (tech). The remaining four sectors declined modestly (Consumer Discretionary down 0.4% thanks to strength in tech names) while Consumer Staples fell 1.2% on that aforementioned rotation).

Like much of last week, the S&P 500 logged a gain but the broader market did not perform well and that's evidenced by RSP dropping 0.5% compared to the slight gain for SPY. That weakness is due to 1) Higher yields and 2) Mixed earnings (tech earnings have been better than feared but the verdict on this earnings season remains out for now). However, momentum remains higher and tech is doing the heavy lifting, although that makes solid tech earnings now important to supporting the very recent gains.

China Cut Reserve Requirements: Is It A Buy Now?

Sometimes one gets lucky with timing and that's the case this week, as on Tuesday I focused on the rout in Chinese shares and stated that they were 1) Due for a bounce, but for that bounce to be sustainable I'd want to see 1) Reserve ratio cuts and 2) More business friendly rhetoric and practices from China's government.

Well, two days ago a solid bounce in Chinese shares started and it continued on Wednesday as Chinese authorities announced a 50-basis-point reduction to reserve requirement ratios, fulfilling one of the two conditions I'd want to see in order to buy this "value" in Chinese shares.

So, is something like MCHI, KWEB or FXI worth some capital here? If one is a risk taker and looking for a contrarian investment, then "yes," I think they are, simply because it appears, after the extreme rout in Chinese shares, that authorities are becoming serious about stimulating the economy.

However, I'd keep position sizes small and look to add to any initial positions once there's further confirmation that China is taking more pro-growth, pro-business stance. Specifically, that would look like 1) Rate cuts to short- and medium-term interest rates and 2) More specific rhetoric that the tech sector will see reduced regulatory scrutiny (which is still lacking).

But while it's still a higher-risk position, for clients looking for value and a contrarian opportunity, the risk/reward in China has turned more attractive with these moves, although broadly speaking there's more work to be done before investors can sound a relative "all clear" for China exposure.

Economics

December Flash PMIs

- The December flash manufacturing PMI rose to 50.3 vs. (E) 47.7.
- The December flash services PMI rose to 52.9 vs. (E) 51.0.

Takeaway

The first national economic reading for January was Goldilocks as activity in both manufacturing and the service sectors rose, but not by so much that it would make the Fed rethink rate cuts.

Manufacturing activity contradicted both the abysmal reading we saw in the Empire report last week and the soft Philly reading, and instead showed an increase in activity that was slightly in expansion territory, but also comfortably above the expectation. The service sector, meanwhile, also accelerated and put some distance between it and the expansion/contraction line of 50, rising just below 53.0.

Meanwhile, commentary on pricing was positive as numerous respondents stated that selling price inflation was running around 2% or pre-pandemic levels, and that anecdotally matches recent Fed commentary that on a three- and six-month basis, inflation is back at the 2% y/y reading.

Bottom line, this was a positive data point and it reinforces the market's expectation for a soft landing. So, while there are signs that economic momentum is slowing, so far, the major economic reports continue to point towards consistent, but not spectacular, growth and that's helping stocks broadly rally.

Market	Level	Change	% Change
Dollar Index	103.07	-.33	-0.32%
EUR/USD	1.0886	.0032	0.29%
GBP/USD	1.2725	.0038	0.30%
USD/JPY	147.57	-.78	-0.53%
USD/CAD	1.3523	.0061	0.45%
AUD/USD	.6580	.0000	0.00%
USD/BRL	4.9297	-.0213	-0.43%
10 Year Yield	4.178	.036	0.87%
30 Year Yield	4.413	.035	0.80%
10's-2's	-20 bps		
Date of Rate Cut	May 2024		
2024 YE Fed Funds	4.10%		
Prices taken at previous day market close.			

Commodities

Commodities traded with a risk-on bias yesterday as oil hit new 2024 highs thanks to bullish EIA data and China stimulus optimism, the latter of which also supported gains in industrial metals. Gold was the laggard as a combination of rising yields and a stronger dollar weighed on the safe haven. The commodity ETF, DBC, gained 0.86%.

Starting with the metals, copper surged by 2.11% making it the best performer among major commodity futures products as it revisited the early 2024 highs. The reserve rate cuts by the PBOC were the catalyst for the gain and the renewed strength in copper is supportive of the otherwise broad risk-on rally underway across asset classes. Gold lagged, posting a decline of 0.59% as the U.S. Flash Composite PMI handily beat estimates sparking some hawkish money flows early in the day that were exacerbated by a dismal Treasury auction in the afternoon. Gold notably held above the psychological $2,000/oz. level, which has offered support so far in 2024.

EIA Data and Oil Update

The oil market was volatile in the wake of this week's EIA inventory data as there were some significant surprises in the release, some bullish, some bearish. WTI crude oil futures rallied to fresh 2024 highs after the initial volatile reaction to the release but ended the day off the highs, up 0.97%.

On the headlines, commercial crude oil stockpiles fell a staggering -9.2 million barrels vs. (E) -1.4MM (API: -6.67MM), gasoline supply jumped +4.9MM bbls vs. (E) +1.5MM (API: +2.18MM), and distillate inventories fell -1.4MM bbls vs. (E) -700K (API: -245K). The only aspect of those headlines that did not favor the bears was the build in gasoline inventories.

The most attention grabbing detail of the report was a 1 million b/d drop from a record high level of domestic oil production to, 12.3MM b/d, the lowest since July of last year. The fact that refinery use dropped a hefty 7.1% to just 85.5% should have resulted in big drawdowns in refined products if there weren't any other big changes in the physical market dynamics. But gasoline supplied, one of our preferred measures of demand, dropped another 388K b/d to 7.88M b/d, a one-year low, and well off the fall 2023 high of 9.5MM b/d. That drop in demand contributed to the gasoline build.

Bottom line, adverse winter weather impacted the oil and refined product markets the most since the Great Texas Freeze sent markets into a frenzy in February 2021. The two key factors to watch going forward are 1) How quickly oil productions comes back online; the faster the more bearish for prices, and 2) Whether consumer demand for refined products recovers back to normal seasonal levels, and the sooner, the more bullish for prices. Outside the U.S. geopolitics continue to keep a fear bid in the market and the recent return to backwardation in the term structure of the oil futures market suggest undersupply is a the main concern for oil right now with risks of WTI rallying to $80 rising.

Currencies & Bonds

The direction of the dollar and Treasury yields diverged on Wednesday thanks to an ugly 5-year Treasury bond auction that sent yields higher while the dollar declined on Goldilocks data. The 2-year and 10-year yields both rose 3 bps while the Dollar Index declined 0.35%.

Both the dollar and yields started the day modestly lower and the reason was economic data. The flash PMIs from Europe showed a modest uptick in activity, boosting the euro and pound and pressuring the dollar while the U.S. flash PMIs were better than expected, but also pretty Goldilocks when we consider the inflation commentary. Point being, the flash PMIs didn't make Fed rate cuts any less likely so while the dollar drifted slightly higher following their release, it wasn't a significant positive catalyst as the dollar ended lower.

By midday, Treasury yields were lower by 1-2 basis points, the Dollar Index was down 0.4% and the euro and pound were both higher by 0.3%, just as the data implied.

Then the 5-year Treasury auction hit and the results weren't good. The auction was for $61 billion in 5-year paper, which tied for the largest auction ever and demand was underwhelming. Bidding was not aggressive (the actual yield was 2 basis points above the "When Issued" yield, which is a large margin) and the bid to cover, a broader measure of demand, was 2.31X vs. 2.50X last month. Finally, indirect bidders (foreign buyers) were much lower at 60.9% vs. 70.6% last month, the lowest since September 2022. That soft demand pushed Treasury yields higher and the 2- and 10-year yields closed with modest gains (and the reversal in yields weighed on stocks during the afternoon).

Bottom line, the next week will be an important in deciding the next 20-basis-point move in Treasury yields as we will get important updates from the ECB (today), inflation (Core PCE tomorrow), the Fed (next Wednesday) and the economy. Broadly speaking, higher yields are still a headwind on stocks and the higher yields go, the stronger the headwind. Calm movement in yields over the next week is the best outcome for stocks.

Have a good day,

Tom

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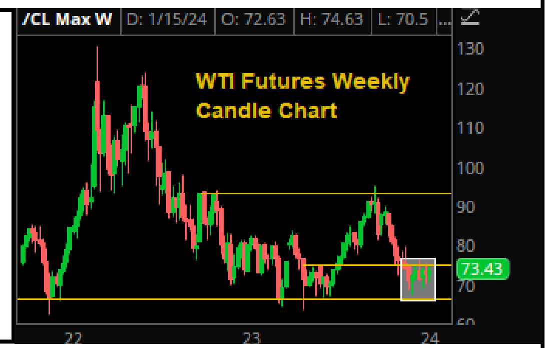
Technical Perspectives
(Updated 1/21/2024)

S&P 500

- Technical View: **The medium-term trend in equities remains bullish** confirmed by the latest run to all-time highs in the benchmark equity index.
- Dow Theory: **Bullish (since the week of July 10, 2023)**
- Key Resistance Levels: 4875, 4900, 4950
- Key Support Levels: 4783, 4697, 4598

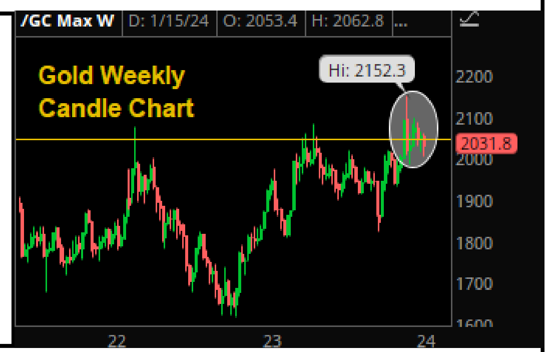
WTI Crude Oil

- Technical View: The oil market has stabilized to start 2024 but futures remain well off the 2023 highs above $90/barrel.
- Proprietary Model: **Neutral (since the week of November 6, 2023)**
- Key Resistance Levels: $75.43, $77.72, $79.60
- Key Support Levels: $70.91, $69.87, $68.73



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: $2076, $2094, $2152
- Key Support Levels: $2009, $1995, $1950

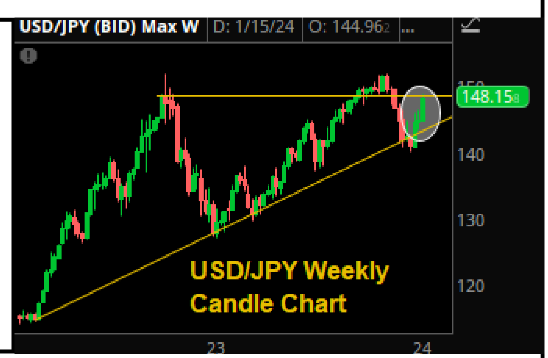


10-Year T-Note Yield

- 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: 4.206, 4.274, 4.352
- Key Support Levels: 3.907, 3.789, 3.608

Dollar/Yen

- Technical View: The USD/JPY recovered a longstanding uptrend line to start 2024, however, the heavy price action in late 2023 leaves the outlook neutral.
- Proprietary Model: **Neutral (since the week of December 25, 2023)**
- Key Resistance Levels: 148.67, 149.57, 151.38
- Key Support Levels: 146.15, 144.62, 142.37



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Fundamental Market View
(Updated 1/21/2024)

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%**	*The S&P 500 hit a new all-time high last week recouping the past two years' declines despite a rise in Treasury yields as strong earnings and positive economic data pushed stocks higher.*

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 modestly last week on a combination of a stronger dollar, soft Chinese growth and lingering demand concerns for oil.*
US Dollar	**Neutral**	*The Dollar Index rallied nearly 1% last week thanks to strong retail sales and low jobless claims while Fed officials pushed back on expectations for a March rate cut.*
Treasuries	**Turning Positive**	*Treasury yields rose sharply last week as Fed officials pushed back on the idea of imminent rate cuts while the economic data showed no significant signs of slowing growth.*

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.

An Approved CE Provider CFP