SEVENS REPORT

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

July 18, 2024

Semiconductors: SOXX (iShares Semiconductor ETF) collapsed 7% on Wednesday on a combination of underwhelming guidance from ASML and geopolitical worries, marking it the worst day for the ETF this year. SOXX is now sitting on important support at the 50-day MA.

Pre 7:00 Look

- Futures are slightly higher as tech stocks bounce modestly following better than expected earnings overnight.
- Taiwan Semiconductor (TSM) posted solid earnings and the stock is modestly higher pre-market and that's helping the tech sector to bounce and support futures.
- Economically there were no important reports overnight.
- Econ Today: ECB Rate Decision (E: No Change), Jobless Claims (E: 230k), Philly Fed (E: 3.0). Fed Speak: Logan (1:45 p.m. ET), Daly (6:05 p.m. ET), Bowman (7:30 p.m. ET).
- Earnings Today: TSM ($1.37), NFLX ($4.70), PPG ($2.48).

Market	Level	Change	% Change
S&P 500 Futures	5,645.25	6.25	0.11%
U.S. Dollar (DXY)	103.79	0.05	0.05%
Gold	2,468.20	8.30	0.34%
WTI	82.72	-0.18	-0.22%
10 Year Yield	4.19%	0.04	1.07%

Equities

Market Recap

The rotation from tech to cyclicals continued Wednesday, although yesterday we saw broad weakness in the S&P 500 as it was weighed down by a significant drop in tech stocks. The S&P 500 fell 1.39%.

S&P 500 futures were lower from the start on Wednesday and the reason was clear: Tech stock weakness. Disappointing ASML guidance, concerns about export controls for semiconductors and Trump's bellicose rhetoric on Taiwan weighed on semiconductor stocks and the tech sector more broadly. That, in turn, weighed on S&P 500 futures. But while the S&P 500 was weak thanks to tech stock declines, the Dow Industrials was resilient, in part because of earnings and it spent the entire day in positive territory.

Shortly after the open, the S&P 500 tried to rally in part due to Goldilocks economic data (that showed solid growth) and after New York Fed President Williams and Vice Chair Waller said the Fed was "close" to being able to cut rates (which reinforced expectations for a September rate cut).

However, tech stocks and the S&P 500 couldn't hold the bounce and instead drifted steadily lower throughout the day and the selling eventually dragged the Russell 2000, which has been the star performer over the past several days, lower as well.

The declines continued in quiet trade throughout the afternoon as investors sold tech and that sector acted as an anchor on the broader market and the S&P 500 fin-

Market	Level	Change	% Change
Dow	41,198.08	243.60	0.59%
TSX	22,851.17	-144.12	-0.63%
Stoxx 50	4,892.93	1.47	0.03%
FTSE	8,240.33	52.87	0.65%
Nikkei	40,126.35	-971.35	-2.36%
Hang Seng	17,778.41	39.00	0.22%
ASX	8,036.52	-21.37	-0.27%
Prices taken at previous day market close.			

ished near the lows of day, as the selling in tech was simply too much to overcome for the benchmark index.

Market	Level	Change	% Change
DBC	23.06	.00	0.00%
Gold	2,461.60	-6.20	-0.25%
Silver	30.49	-.97	-3.09%
Copper	4.4115	-.0380	-0.85%
WTI	82.88	2.12	2.63%
Brent	85.08	1.35	1.61%
Nat Gas	2.042	-.146	-6.67%
RBOB	2.5022	.0247	1.00%
DBA (Grains)	23.91	.01	0.02%
Prices taken at previous day market close.			

What Caused This Rotation from Growth to Value

Last Thursday's CPI report ignited a massive and violent rotation that has seen small caps, cyclical sectors and non-tech sectors rally hard, with small caps rallying more than 10% in just six trading days while the equal weight S&P 500 (RSP) surged higher and substantially narrowed the performance gap between it and the SPY (that performance gap has declined from nearly 14% to 9%, again in just a few trading days).

Given many investors were overweight tech, and rightly so given the 2024 rally has been primarily tech driven, understanding why this rotation is happening and if it can continue is important from an outperformance standpoint.

There is one major, and two minor, reasons this rotation occurred. The major reason is clear: The start of a rate cutting cycle became a certainty in the minds of investors. We covered this in Friday's report, but last Thursday's better-than-expected CPI made a September rate cut all but a guarantee in the minds of investors. **But much more importantly, it allowed investors to begin to position for a rate cutting cycle (so not just one rate cut, but numerous rate cuts over the coming year-plus).**

That is the main cause of this rotation, because the parts of the market that have recently outperformed (small caps, cyclicals, value, RSP) are 1) Beneficiaries of lower rates and 2) More sensitive to economic growth, and because investors think rate cuts will make a soft landing more likely, it's just adding attractiveness to those cyclical parts of the market.

Those two fundamental shifts then combined with an extremely stretched technical conditions in tech (oversold/over owned) and cyclicals (under owned) to create a stampede by investors who rushed not to exit the market, but to gain more exposure to these cyclical sectors.

While investors positioning for a rate cutting cycle is the major reason for this rotation, there are also two minor ones at work: The first has to do with the quickly changing political landscape. As markets price in a Republican sweep, they are making knee-jerk assumptions about what sectors will be in favor in a Trump administration. And given Trump's rhetoric, that's led investors to industrials, energy and other cyclical sectors, thereby exacerbating the rotation that was occurring due to investors pricing in rate cuts.

The other minor influence has been recently negative tech headlines. Caution has been building, quietly, in recent weeks about the growth of super-cap tech earnings (they are still growing solidly, but can they meet lofty expectations). Those concerns were compounded on Wednesday by ASML guidance, which underwhelmed. Then, tech investors were reminded that there are policy and geopolitical risks around the tech sector, courtesy of Trump's Businessweek interview where he used bellicose rhetoric towards Taiwan (a link to that entire interview is here for those interested).

Bottom line, this massive rotation from tech and tech-related sectors (consumer discretionary and communication services) was caused primarily by investors positioning for a rate cutting cycle and secondarily by anticipation for a Trump administration and negative tech news. But the intensity of it was absolutely turbocharged by the historically crowded trade of "long mega-cap tech," which is making this rotation out of tech and into cyclicals, value and the "rest of the market" more intense.

Can This Rotation Continue?

Yes, in the short term. Certainly, some digestion of the rotation is required after the massive moves of the past trading week. But whether the rotation can continue will be determined by 1) Economic data and 2) Earnings.

Goldilocks economic data since the CPI report has helped to fuel the rotation because it's made cyclicals more attractive. **If growth stays Goldilocks over the coming weeks (so just meets expectations) then the**

rally can continue as cyclicals are attractive in the environment of 1) Falling rates and 2) Stable growth.

However, if growth begins to 1) Accelerate or 2) Deteriorate, then the rotation will stall because either markets will reduce rate cut expectations or they will begin to price in a slowdown—and that will not be positive for cyclicals and value. Instead, it'll be positive for mega-cap tech and/or defensive sectors (SPLV/XLU/XLP/XLV).

Regarding earnings, if there's any weakness in the guidance from mega-cap tech companies, that will also keep the rotation in place as the tech sector has become historically overcrowded and over allocated. And if earnings disappoint at all, it'll just encourage investors to return more balance to their portfolios. That said, if tech earnings are stronger than expected, look for the rotation to pause.

Given the facts as we see them now, I believe the most likely outcome is that this rotation can continue for the next several weeks, as economic data remains, mostly, Goldilocks, tech is still "over owned" putting a technical tailwind behind the rotation and tech earnings, while not likely to be material disappointments, have a high bar to impress investors. As we said in Friday's report, VTV and RSP (up 2.4% and 2.6% since Thursday) are the easiest ways to increase broad cyclical and value exposure.

Beyond the near term (meaning next several weeks) I do remain concerned about economic growth and as such, I am not in favor of aggressive allocations to cyclicals here for anything other than tactical capital, because while the market is convinced lower rates will prevent a slowdown, corporate earnings and Fed commentary continue to imply investors are too complacent when it comes to slowdown risks.

Market	Level	Change	% Change
Dollar Index	103.43	-.52	-0.50%
EUR/USD	1.0938	.0039	0.36%
GBP/USD	1.3010	.0036	0.28%
USD/JPY	156.15	-2.20	-1.39%
USD/CAD	1.3687	.0014	0.10%
AUD/USD	.6728	-.0006	-0.09%
USD/BRL	5.4852	.0562	1.04%
Bitcoin	64,696.83	-464.38	-0.71%
10 Year Yield	4.146	-.021	-0.50%
30 Year Yield	4.359	-.015	-0.34%
10's-2's	-28 bps		
Date of Rate Cut	September 2024		
2024 YE Fed Funds	4.81%		

Prices taken at previous day market close.

Economics

Industrial Production

- June Industrial Production rose 0.6% vs. (E) 0.3%.

Takeaway

Wednesday's Industrial Production report was the third Goldilocks economic report of the week and it further reduced any anxiety that the U.S. economy is suddenly and quickly losing momentum.

Much like the Retail Sales report on Tuesday, not only was the headline reading better than expected but the details were strong as well, as the manufacturing sub-index (which is the most important part of the Industrial Production report because it strips out power generation by utilities) rose 0.5% vs. (E) 0.0%.

Bottom line, the data so far this week doesn't refute the idea that the U.S. economy is losing momentum, it clearly is. But it does push back on the idea that growth is suddenly slowing and because of that, the data so far this week has been generally positive for risk assets (although it obviously wasn't enough to overcome the negative tech-related news yesterday).

Commodities

Commodities were mixed again on Wednesday, but the roles were reversed from earlier in the week as oil logged a solid rally while gold (and most other commodities) declined. The commodity ETF, DBC, was unchanged.

Oil was the standout on Wednesday and the reason was clear: Bullish inventory data. The weekly inventory data showed a decline of 4.9 million barrels of oil last week compared to the expectation for a 540k barrel increase and that reduction in supply sent oil solidly higher and once again comfortably above the $80/bbl level.

Notably, the bullish oil inventory data pulled both heating oil and RBOB gasoline higher despite larger-than-expected supply builds in both of those products and heating oil finished the day slightly positive while RBO gasoline rose 1.4%.

Stepping back, the weekly inventory data can always inject some short-term volatility but beyond the short term, the outlook for energy will be dependent on demand and growth and, for now, growth is holding generally steady (but for energy to sustain a real rally, we've got to see better demand data because OPEC production cuts are unlikely).

Staying in the energy patch, natural gas collapsed and continued a horrid week, plunging more than 6.7% on expectations for a break from the oppressive summer heat and with it, reduced energy demand via air conditioners. Natural gas is now down more than 10% on the week and at a near-three-month low and if natural gas drops below $1.90 (currently $2.04) then a test of the lows for the year at $1.65 isn't out of the question. For natural gas to stabilize, markets need a return of sweltering national weather.

Turning to metals, gold digested the recent gains on Wednesday and declined modestly, falling 0.25%. Notably, the dollar decline came despite a moderate drop in the U.S. dollar. The reason that decline didn't boost gold was because the decline in the dollar was due mostly to strength in the pound and yen, not because of anything dollar negative. As such, gold ignored it.

Stepping back, gold remains just off the new all-time highs and the path of least resistance remains lower as this environment of looming rate cuts and geopolitical uncertainty remains positive for the yellow metal.

Currencies & Bonds

The dollar dropped moderately on Wednesday thanks mostly to hotter-than-expected foreign inflation data and more central bank intervention in the currency markets. The Dollar Index fell 0.5%.

The yen was, by far, the biggest mover in the currency space yesterday as the yen rose 1.4% vs. the dollar. The reason for the leap higher should be familiar: Bank of Japan intervention. The BOJ has been repeatedly intervening to support the yen ever since it rose above 160 vs. the dollar and that continued early on Wednesday morning as the yen leapt higher vs. the dollar. And with the BOJ now engaged, a continued rally in the yen vs. the dollar is reasonable, although it's not going to cause a sustainable move higher (for that to happen, we'd need to see the BOJ get more hawkish or the Fed get more dovish).

The stronger yen was one reason the Dollar Index declined Wednesday and a strong pound was the other, as the "cable" rose 0.2% and above 1.30 vs. the dollar for the first time this year, following a hotter-than-expected UK CPI Report. UK core CPI rose 3.5% vs. (E) 3.4% and that pushed back on the idea of a September rate cut from the Bank of England. That, in turn, pushed the pound higher vs. the dollar as it again rose to a one-year high as currency traders begin to consider the BOE may now by the least dovish global central bank (potentially taking that title from the Fed).

Bottom line, the Dollar Index dropped to the lowest level since March, below 104, not because of any specifically negative dollar news but instead because of strength in the yen and pound. However, these two forces are again unlikely to materially pressure the dollar and the broad 103-106 trading range should remain intact (which again keeps the dollar neutral for stocks).

Turning to Treasuries, yields were initially little changed but reversed and declined slightly into the afternoon as the 10-year yield fell 2 basis points. Fed Governor Waller further confirmed rate cuts are coming in September (he said the Fed was close to being able to cut rates but not there yet, which means September not July). Additionally, a 20-year Treasury bond auction provided no material surprises.

So, with stocks down, a reminder of looming rate cuts and no warning signs on foreign demand for Treasuries, yields drifted slightly lower as the 10-year yield again closed below 4.20% and again comfortably in the stock positive 3.75%-4.25% range.

Have a good day,

Tom

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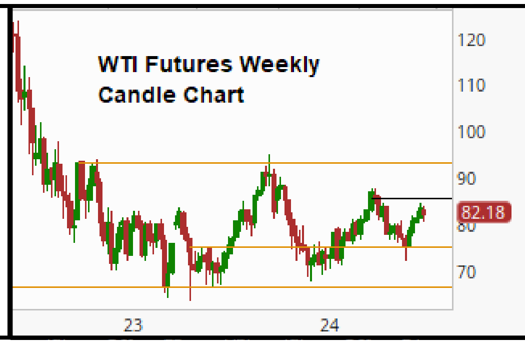
Technical Perspectives (Updated 7/14/2024)

S&P 500

- Technical View: **The medium-term trend in the S&P 500 remains bullish** as stocks have consistently rallied to fresh record highs in mid-2024.
- Dow Theory: **Bullish (since the week of July 10, 2023)**
- Key Resistance Levels: 5633, 5656, 5700
- Key Support Levels: 5585, 5509, 5448

WTI Crude Oil

- Technical View: The trend in oil has begun to turn sideways in mid-2024; however, the higher lows established in H1 ’24 leave the benefit of the doubt with the bulls.
- Primary Trend: **Bullish (since the week of February 12, 2024)**
- Key Resistance Levels: $83.44, $84.45, $85.34
- Key Support Levels: $81.81, $80.59, $78.49

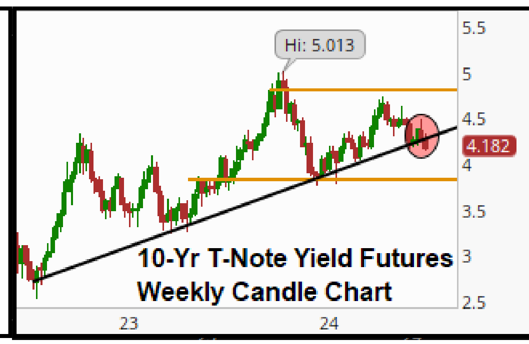


Gold

- Technical View: Gold rallied back towards the 2024 record highs in the mid-$2,400 range to start Q3 leaving the long-term uptrend intact.
- Primary Trend: **Bullish (since the week of November 27, 2023)**
- Key Resistance Levels: $2421, $2438, $2454
- Key Support Levels: $2339, $2310, $2257

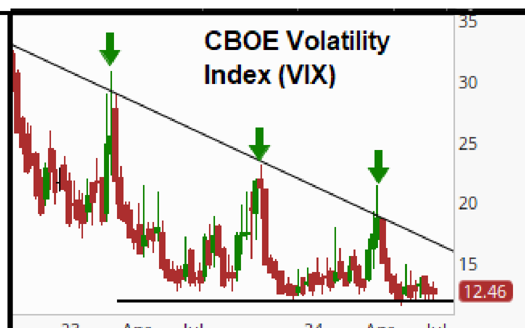
10-Year T-Note Yield Futures

- Technical View: The 10-year yield violated a multi-year uptrend line last week, a step towards a shift in trend from bullish to neutral with the late-2023 lows in focus.
- Primary Trend: **Bullish (since the week of August 21, 2023)**
- Key Resistance Levels: 4.275, 4.358, 4.454
- Key Support Levels: 4.088, 3.935, 3.798



CBOE Volatility Index (VIX)

- Technical View: The VIX has stabilized after a sharp decline in late-April and early May and the “fear gauge” has been sideways since, despite new highs in the S&P.
- Primary Trend: **Neutral (since the week of May 6, 2024)**
- Key Resistance Levels: 13.33, 13.85, 14.47
- Key Support Levels: 12.37, 12.03, 11.86



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Fundamental Market View
(Updated 7/14/2024)

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 yet another record high last week as CPI rose less than expected and boosted investor expectations for a September rate cut and two rate cuts in 2024.*

Tactical Allocation Ideas:

- **What's Outperforming: Defensive sectors, minimum volatility and sectors linked to higher rates have relatively outperformed recently as markets have become more volatile.**
- **What's Underperforming: Tech/growth and high valuation stocks have lagged as yields have risen.**

Long Term Fundamental Outlook for Other Asset Classes

	Fundamental Outlook	Market Intelligence
Commodities	**Neutral**	*Commodities declined modestly last week despite a weaker U.S. dollar, as global growth worries weighed on oil while gold saw a modest rally thanks to the lower dollar.*
US Dollar	**Neutral**	*The Dollar Index declined again last week following the better-than-expected CPI report, as markets more fully priced in two rate cuts in 2024.*
Treasuries	**Turning Positive**	*Treasury yields declined moderately last week as the smaller-than-expected increase in CPI pressured yields, and the 10 year fell back into the 3.75%-4.25% "stock positive" range.*

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.