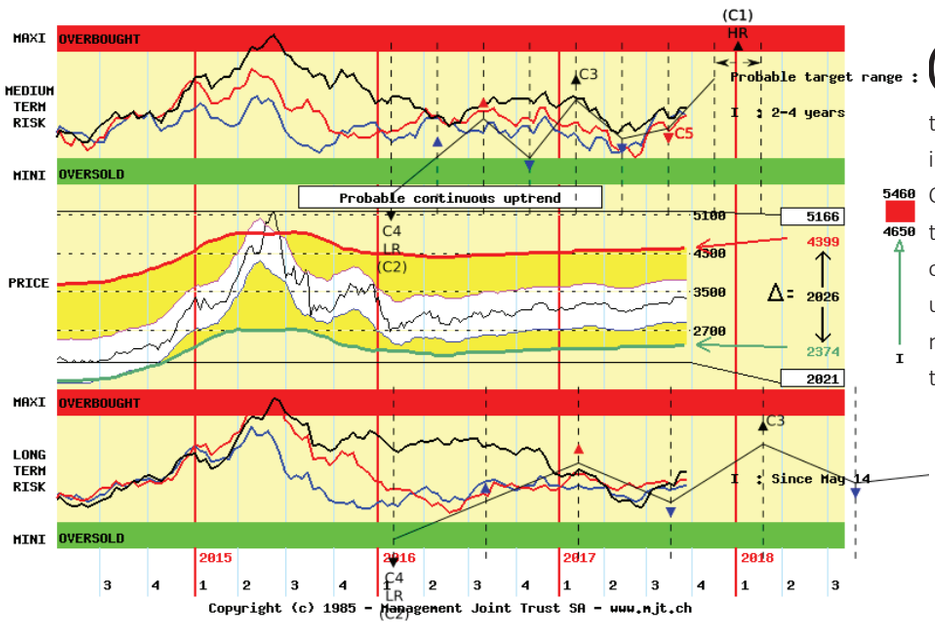
38 / MJT - TIMING AND TACTICAL INSIGHT

Oil should retrace during October before it resumes its uptrend towards year-end.

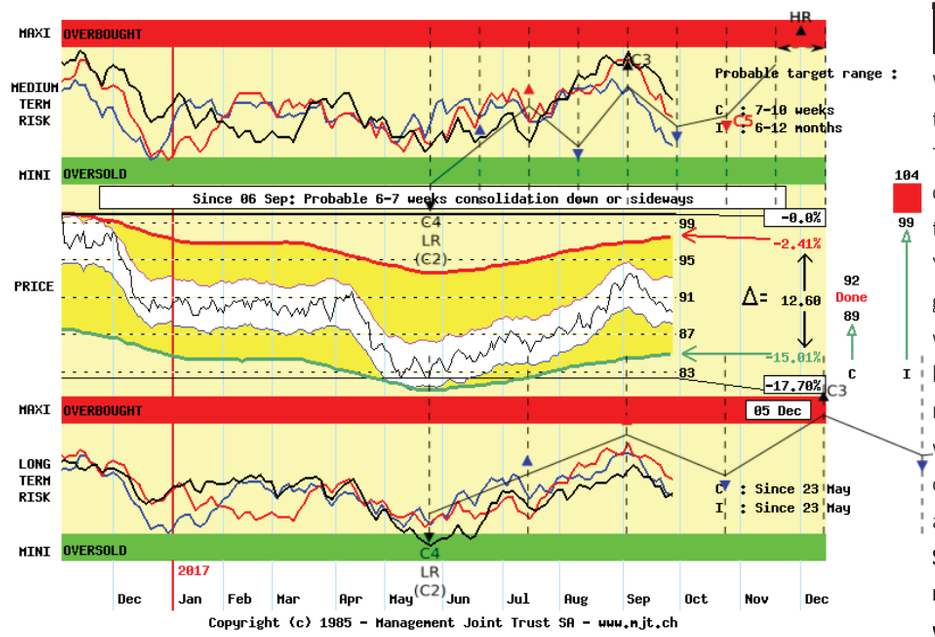
According to our projections, led by China, Oil has started to move up in June and has since accelerated up. We believe it has now reached an intermediate top and should start to retrace down into October. We would see a further buying opportunity late October, early November to seize the strong year-end rally we expect.

Shanghai Composite Index
Weekly graph or the perspective over the 2 to 4 quarters



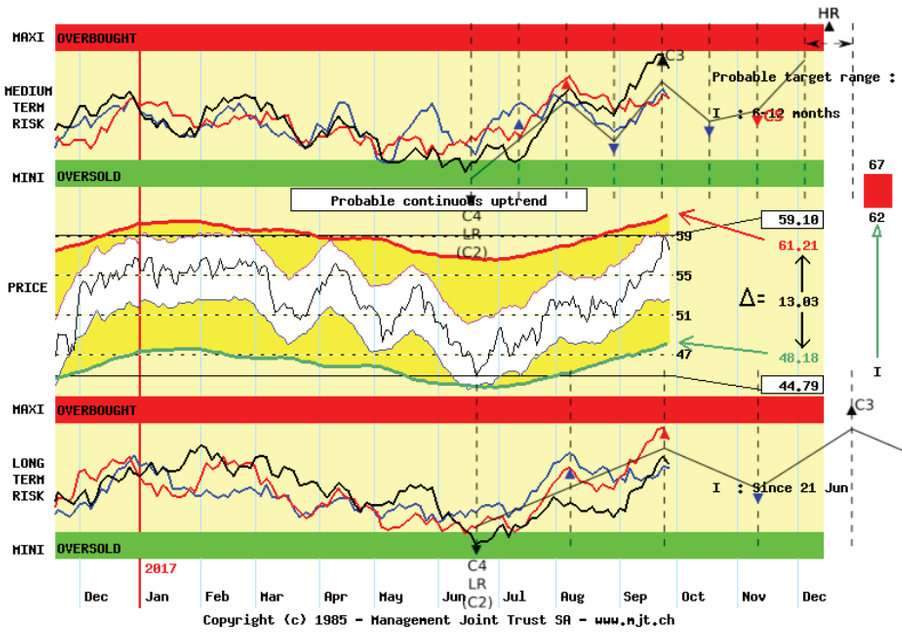
China led Oil up in 2016 and again was probably the cause of its retracement in H1 2017. Since June, the Chinese market has started to move up again and on both oscillator series (lower and upper rectangles), we would now expect it to continue up towards early next year.

Shanghai Composite Index vs MSCI WORLD INDEX
Daily graph or the perspective over the next 2 to 3 months



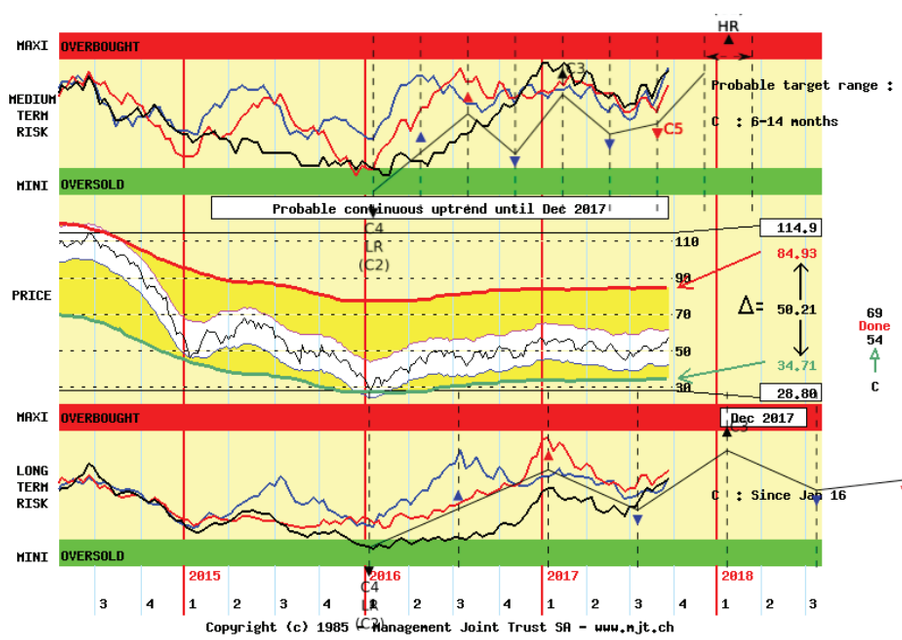
Looking at the Shanghai Composite vs the MSCI World Index, we can monitor the progression since June. This ratio is not hedged for currency and hence includes the effect of a strengthening Yuan vs USD. In fact, the progression of Chinese equity vs world markets is quite firm as both the market and the currency are moving up vs the world and the USD. On both our oscillator series (lower and upper rectangles), **the Shanghai Composite has made an intermediate top vs the MSCI World Index early September and is now retracing down. The ratio should find a retracement low between now and late October to resume its uptrend towards year end. The 'I' Impulsive targets to the upside for China's outperformance towards year-end are still substantial (right-hand scale; middle rectangle), between 10 and 15%.**

Brent
Daily graph or the perspective over the next 2 to 3 months



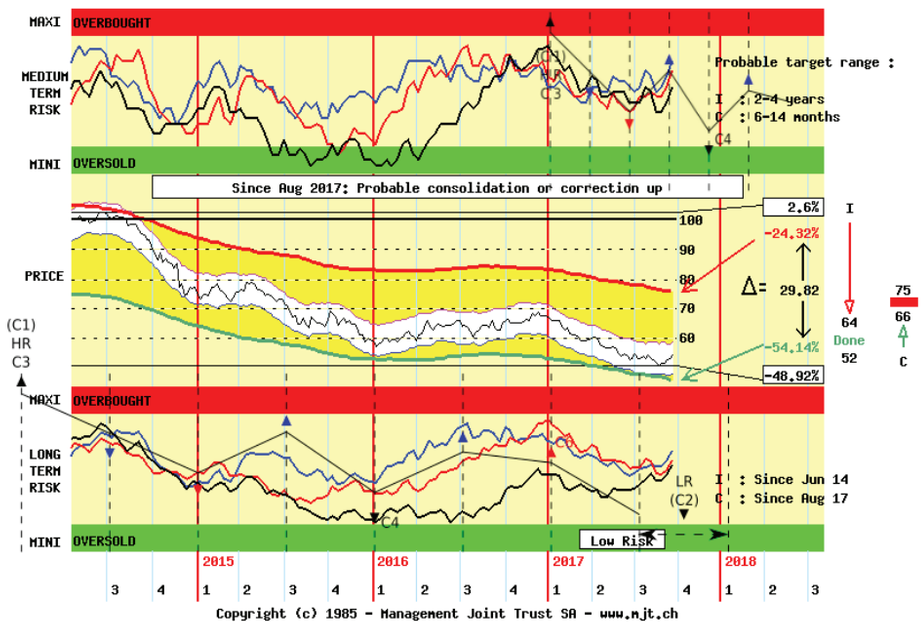
Turning to Brent Oil, it started up a few weeks after China had turned and interestingly also seems to be topping out now with a similar delay. On both our oscillator series (lower and upper rectangles), we would now expect **Brent to retrace down into late October, early November.** Given our current historic volatility measure "Delta" at 13.06 USD (right-hand side; middle rectangle), **Oil could retrace between 6.5 and 10 USD from its recent highs during that period** (the calculation uses "Delta" and multiplies by 0.5 to 0.8 to get a corrective price target potential). Following that, and from November into year-end, the 'I' Impulsive targets to the upside are between USD 62 and 67 USD/barrel (right-hand scale; middle rectangle).

Brent
Weekly graph or the perspective over the 2 to 4 quarters



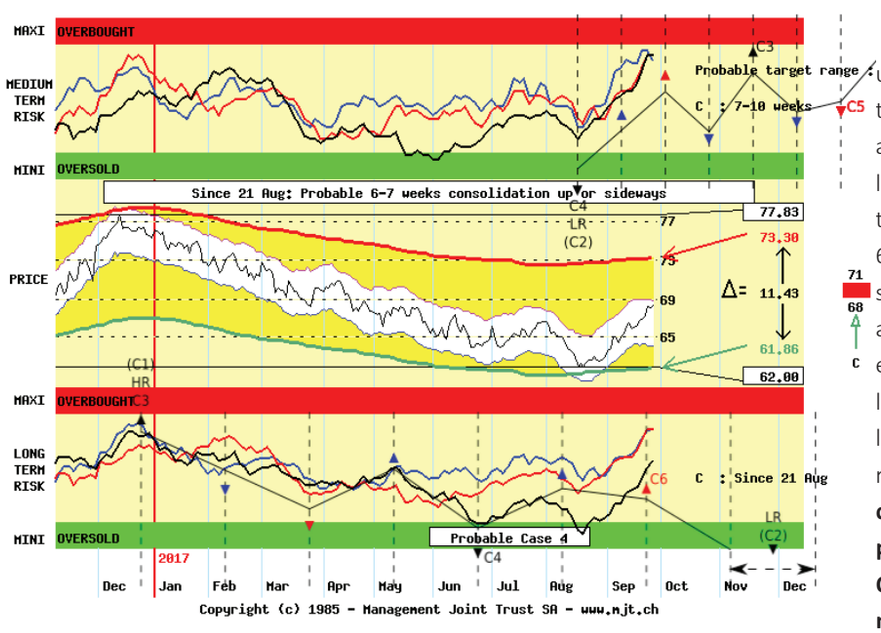
The longer term perspective for Oil is however still very encouraging towards year-end and early 2018. On both our oscillator series (lower and upper rectangles), **we are now in "resume uptrend" situations, which should lead us up into Q1 2018**. The move up since 2016 is still corrective, yet the upper end of its 'C' corrective targets already **extends up to the high 60s USD/barrel** (right-hand scale; middle rectangle). **These targets pretty much match our Daily targets above and are the targets we are considering towards early next year.**

XLE - Energy Select Sector SPDR Fund vs SPY - SPDR S&P 500
Weekly graph or the perspective over the 2 to 4 quarters



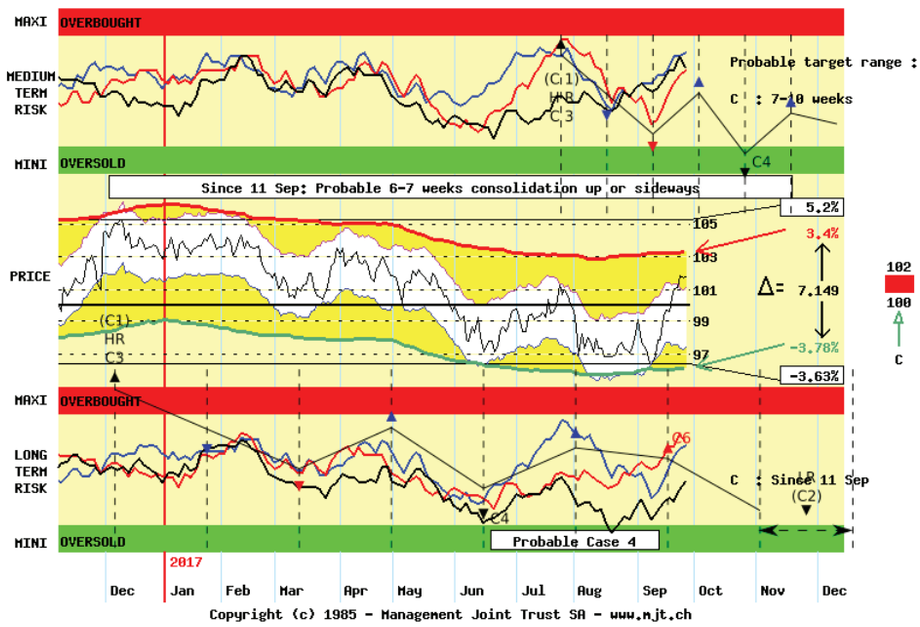
The Energy sector has however underperformed Oil. This relative graph compares the US Energy ETF XLE vs the S&P 500 SPY ETF. Following a bounce in 2016, it actually made new lows in 2017 and may still be lingering down lower. On our long term oscillators (lower rectangle), **it has now reached a "Low Risk" position**, an interesting situation that usually leads to a bounce. On our medium term oscillators (upper rectangle), **we can still expect one last period of underperformance into mid Q4 (retest) before the ratio really starts to rebound** into early next year. On the price target front, our 'I' Impulsive targets to the downside are exhausted, while **our 'C' Corrective targets to the upside could deliver as much as 20 to 40% outperformance** into early next year, once the rebound is underway (right-hand scale; middle rectangle) – **the Energy sector is indeed very volatile vs the general market.**

XLE - Energy Select Sector SPDR Fund
Daily graph or the perspective over the next 2 to 3 months



The sector on a stand-alone basis has been correcting up rapidly since mid September. That said, it is already approaching the resistance levels of our 'C' Corrective targets to the upside between 68 and 71 USD (right-hand scale; middle rectangle). This and the intermediate top we expect between now and early October on both our oscillator series (lower and upper rectangles) confirm the **retracement/re-test down we expect for the sector into late October, possibly even into mid November.**

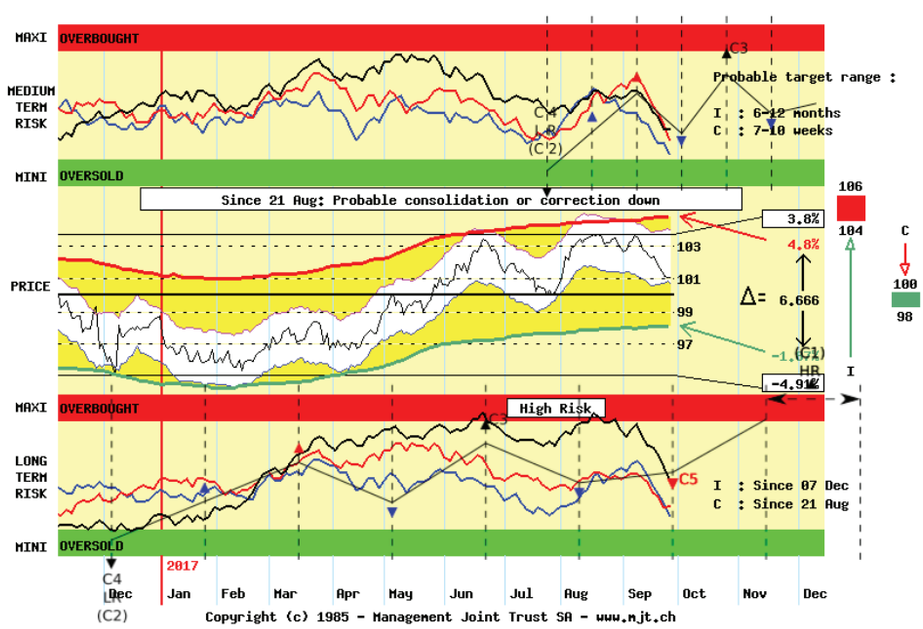
IEO - iShares Oil & Gas Exploration & Production ETF vs XLE - Energy Select Sector SPDR Fund
Daily graph or the perspective over the next 2 to 3 months



We now turn to the US Energy sector segments to confirm this view. **We first focus on Oil Production and Exploration vs the wider XLE index. This segment is indeed more volatile (risk-ON for Energy)**. This relative graph have rebounded aggressively since early September. We believe that on both our oscillator series (lower and upper rectangles), **it is now approaching potential tops that should trigger a new period of underperformance into late October and possibly mid November**.

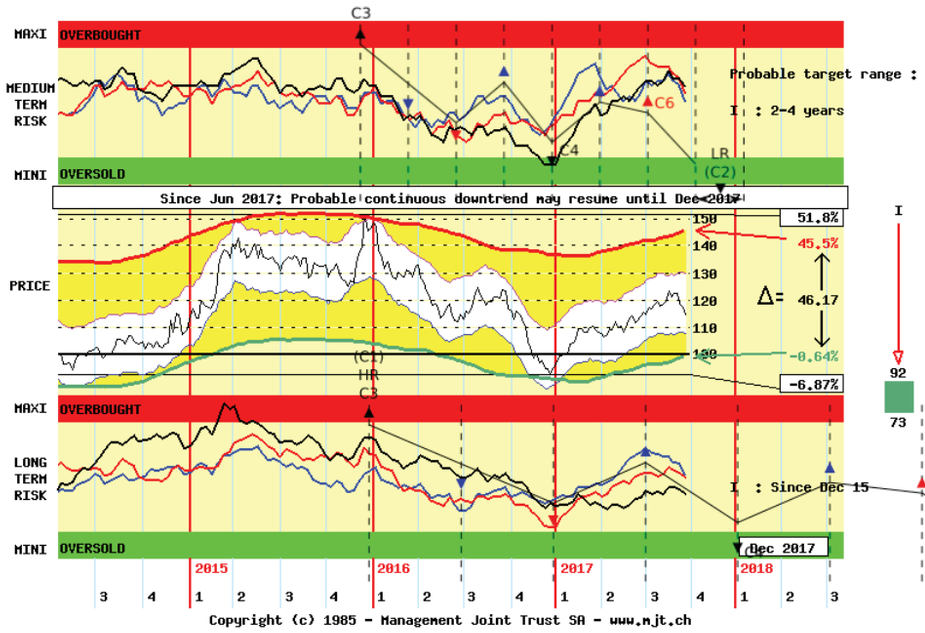
In this context, the rebound potential is already getting exhausted. Indeed, our 'C' Corrective targets to the upside (right-hand scale; middle rectangle), which usually serve as an initial strong resistance, have been reached.

S&P Integrated Oil & Gas vs S&P Energy (Sector)
Daily graph or the perspective over the next 2 to 3 months



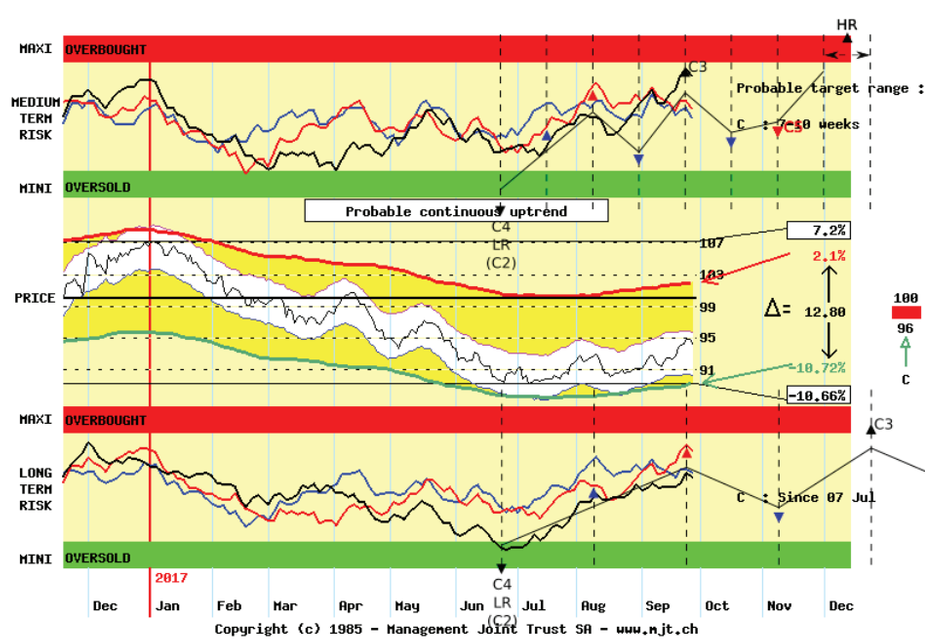
On the contrary, the Integrated Oil & Gas segment is considered more defensive within the wider Energy sector. It has indeed been progressing quite nicely vs XLE since Energy topped out last December, yet topped in August on a relative basis, when the sector started to rebound. On both our oscillator series (lower and upper rectangles), we believe, **it is now getting ready to resume its uptrend and extend to the upside into late October, possibly mid November. This is a sign that the Energy sector may be getting ready to retrace once more.**

ICLN - iShares S&P Global Clean Energy Index Fund vs IXC - iShares Global Energy ETF
Weekly graph or the perspective over the next 2 to 4 quarters



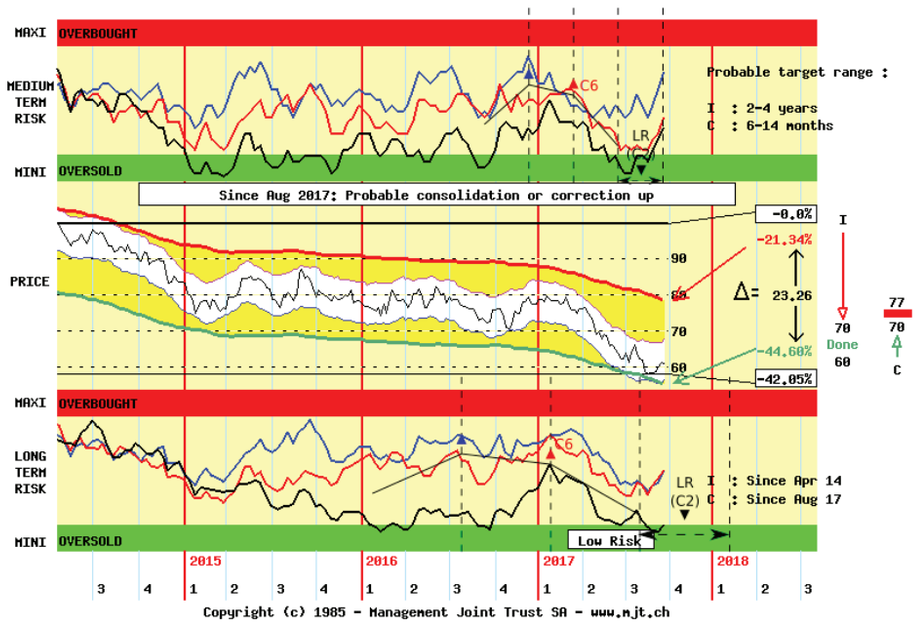
Another very defensive segment within the Energy sector is alternative Energy. We consider it here vs the wider Energy sector (both on a global basis). This relative graph confirms that beyond the retracement we expect on Energy over the next month or so, **the wider Energy sector should continue up vs Alternative Energy into year-end and possibly early 2018 (down rectangle on this graph)**. This is shown by both our oscillators series (lower and upper rectangles). We believe its also a nice proxy for the underperformance we expect for Growth assets (alternative energy) vs reflationary assets (energy) as we approach year-end.

ENERGY - Dow Jones STOXX (EPI) vs Dow Jones STOXX (EPI)
Daily graph or the perspective over the next 2 to 3 months



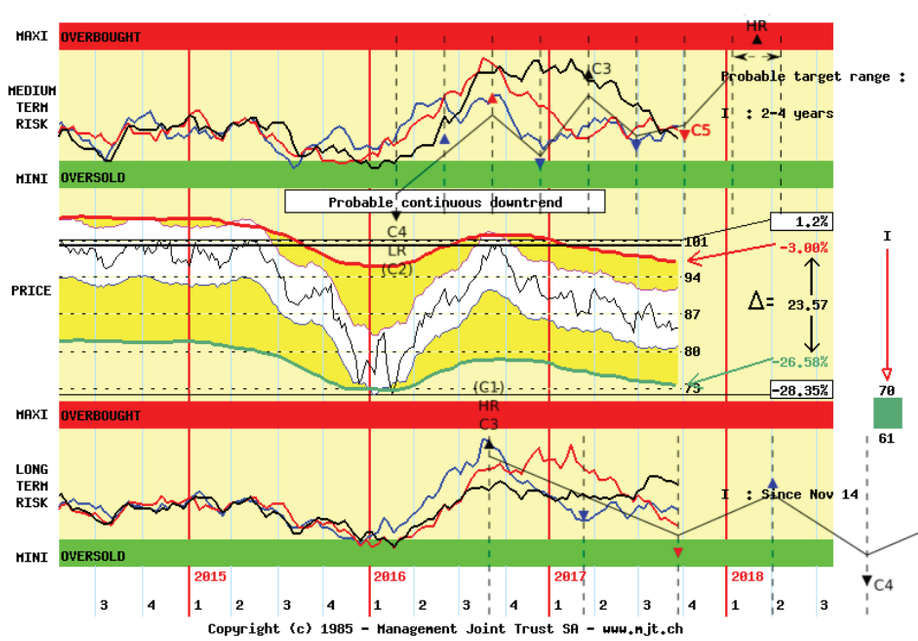
In Europe, the Daily graph of the Energy sector vs the general market is showing very similar dynamics than Oil itself, although with less volatility. Indeed, it bottomed out in June and following three months of outperformance is now approaching an intermediate top on both our oscillator series (lower and upper rectangles). **We would now expect it to underperform European markets into late October, early November**. The move up since June is still corrective (below our 'C' corrective targets to the upside; right-hand scale; middle rectangle) and **hence vulnerable to strong retracements and re-tests**.

OSX - PHLX Oil Service Sector vs XOI - Oil Index (NYSE Arca)
Weekly graph or the perspective over the next 2 to 4 quarters



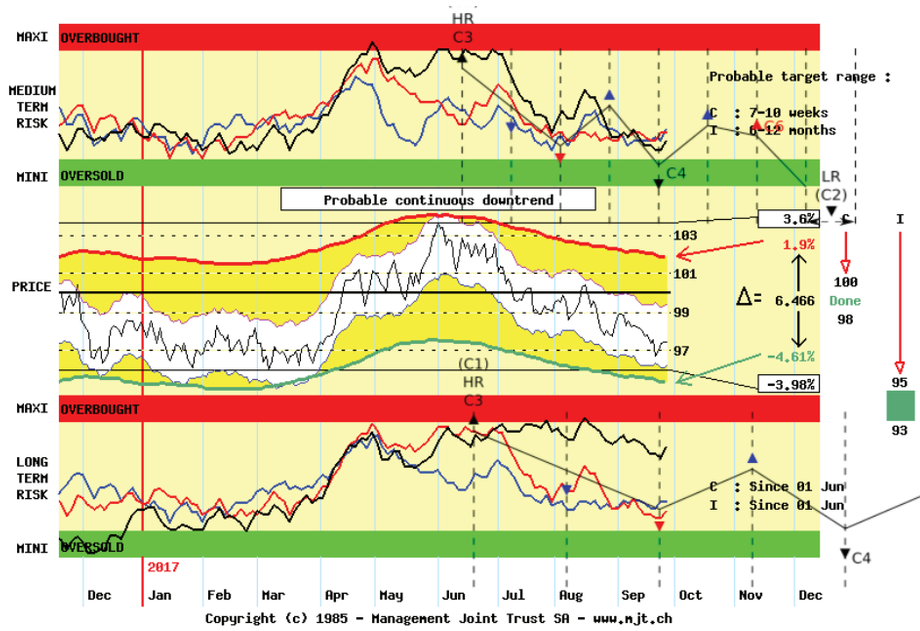
Taking a slightly longer term view, we look at Energy segments, which are usually quite volatile, yet have been beaten down quite strongly since early this year and the retracement of the Oil market. We believe they may constitute **interesting "high beta" opportunities once the retracement we expect comes to an end, late October, early November. We first look at US Oil services vs the more general Oil Index**. Indeed, on this Weekly graph and on both our oscillator series (lower and upper rectangles), it has now reached **an interesting "Low Risk" position vs the wider Energy sector**. We expect it start to outperform from November into Q1 2018 and according to our 'C' corrective targets to the upside (right-hand scale; middle rectangle) , it could do so by as much as 15 to 25% (on top of the sector's own outperformance vs the general market).

XNG - Natural Gas Index (NYSE Arca) vs VDE - Vanguard Energy ETF
Weekly graph or the perspective over the next 2 to 4 quarters



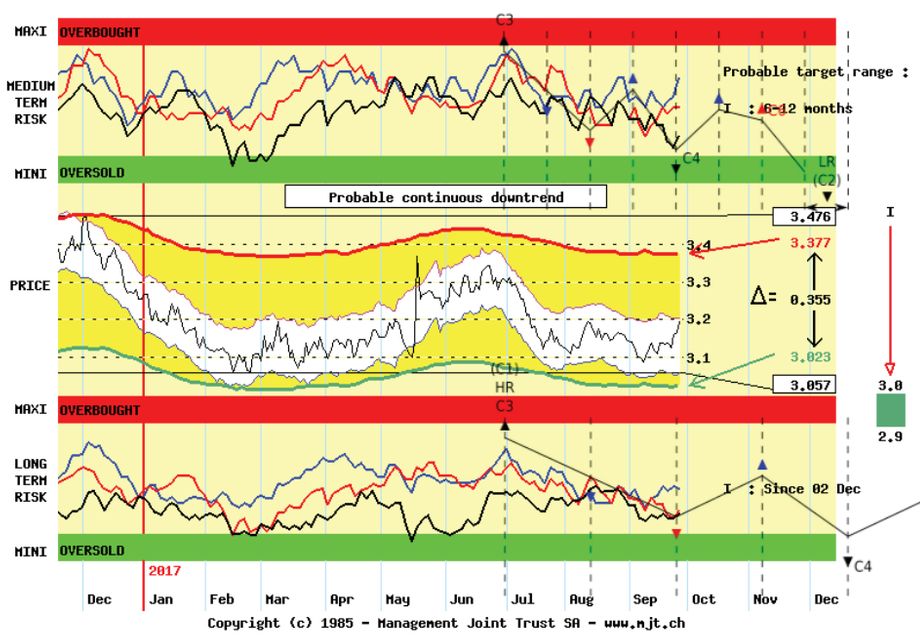
Similarly, we look at The Natural Gas segment vs the wider Energy Index. It's outperformance was particularly strong during the first phases of the oil market rebalancing last year and we now believe this could happen again. Indeed, on both oscillator series (lower and upper rectangles), we are approaching a potential retracement low that should see **the segment outperform the wider Energy sector again into Q1 2018**. We will not post potential outperformance targets on this one as the risk/reward is still hard to define (we are in the middle of the range with our 'I' Impulsive targets down still quite menacing), **yet the timing looks compelling and we consider that this segment is something to look at closely come mid November.**

TRAVEL & LEISURE - Dow Jones STOXX (EPI) vs Dow Jones STOXX (EPI)
Daily graph or the perspective over the next 2 to 3 months



Finally, we consider 2 counter-cyclical bets, at least as far as Oil is concerned. First, **the European Transport sector vs the wider European market. It has been particularly hit by the re-acceleration of the price of Oil to the upside since June. As with other oil counter-cyclical assets, it is currently approaching an intermediate low** on both our oscillator series (upper and lower rectangles) and **should start correcting up vs the market into late October, early November.** As with other Defensive trades, mentioned a separate article further up in this document, we would see **a rebound of the Transport sector vs the market during October as an ultimate opportunity to exit the sector** before cyclical assets and oil start to re-accelerate up towards year-end.

Brazilian Real per U.S. Dollar
Daily graph or the perspective over the next 2 to 3 months



We've been strong advocates of the Brazilian Real since June. Indeed, it correlates very well to Oil: the Dollar vs the Real has been declining quite substantially since Oil bottomed-out in June. On both our oscillator series (lower and upper rectangles), **we have just reached an potential intermediate low for the Dollar vs the Real. We now expect a correction to the upside during October for USD/BRL, before it starts to accelerate down again from November to year-end (this inversely confirms our view on Oil)**. This graph also allows us to confirm that the Dollar is probably the least reflationary of the reflationary currencies, i.e. from mid November, the Dollar could start to move up again vs other majors (EUR, GBP, JPY, CHF), yet **the true winners from November into Q1 2018 will be Commodity Currencies.**

Concluding remarks

Following its reversal and a 3 monhs rallying since June, Oil has reached an intermediate top, which should see it correct into late October, early November. This retracement should be experienced on all oil related trades and should also affect higher beta segments within the Energy sector on a relative basis. That said, we believe this retracement period in only transitory, and that from November, Oil should accelerate up again towards year-end and early 2018. High beta segments (Exploration & Production, Oil Services, NatGas equities) and oil related currencies will probably be great addition to a portfolio during that year-end period.