4/ Executive Summary

07/ As presented earlier this year the "Trump/Reflation Trade" has been pausing, allowing better market re-entry during late Q2-early Q3 2017 - there is still strong belief in the markets that the Trump administration will be able to push through three big initiatives -- tax reform, deregulation, and infrastructure spending. That hope has further extended by the presumption that these initiatives will succeed in rousing the moribund US economy, as well as prop up current market valuations. After the current April relief rally, we believe that the market optimism may be misplaced in the short-term -- there are more «shocks» in the pipeline which could further undercut risk asset valuations .

11/ Timing and Tactical Insight: Trump/Reflation Trade could retrace further into midyear - As mentioned in our January newsletter, we expected reflationary assets to make an intermediate top mid Q1 2017 and retrace during 3 to 6 months depending on assets. This consolidation period which indeed started early March, could extend into midyear. A second leg down on risk assets could materialize from May into June / midyear, favoring Defensives over Commodity sectors, over Financials and even over the Nasdaq 100.

18/ The Yen as a safe haven play: will it last? Yes, it will - The yen hit five-month highs against the dollar and the euro last week as concerns over heightened geopolitical tensions. The yen is also strengthening in the back of a US Dollar stumble following sharp declines in US bond yields on "flight-to-quality" bids on US Treasury debt. Fundamentals in Japan have improved tremendously over the past several quarters. As the US growth cycle peaks, economies that were before in the periphery will take over the baton. Japan will be one of the beneficiaries of that growth rotation … Volatility will be deadly for other risk assets, but it be favorable for the Yen.

21/ Timing and Tactical Insight: The Yen will continue to accelerate up on risk-off considerations - The rather market friendly 1st round of the French election yesterday is fueling a bounce on USD/JPY and EUR/JPY. Over the course of the next few weeks however, we believe the Yen could resume its uptrend vs both the Dollar and the Euro and probably remain strong into the Summer. This further Yen strength, as well as further contracting of the USD-JPY interest rate differential into Q3 2017 should continue to fuel a risk-off environment in Japan, negatively influencing the performance of the Nikkei 225 vs other markets, vs Japanese small caps as well as vs Japanese Government bonds.

27/ Gold: A reappraisal, as the precious metal leads the risk off movement with the JPY - Gold is a Veblen good; as such, the higher the price of gold goes, the higher the demand. Supply-demand-price balance and linkages are USELESS in forecasting the future price of gold – except for mine production. But gold's price behaviour owes to factors that have more to do with currencies than with other commodities. In fact, gold movement over the past few decades were more as an inverse manifestation of the US Dollar. It is generally assumed (wrongly, as it turns out) that there is a positive correlation between long-term interest rates and the US Dollar. In the longer-run, rising rates, in due time, will negatively impact the US currency when domestic growth slows down. Gold, the antiDollar, fits very well into the matrix: rising interest rates should push up Gold prices after a distributed lag of 6 months, as the USD weakens. gold prices should be rising for the rest of the year with acceleration phases taking place during the risk off phases.

30/ Timing and Tactical Insight: Gold, a reflationary asset with a defensive bias - Gold is a reflationary asset with a defensive twist: it underperforms other commodities during risk-on phases and outperforms them during risk-offs. From a pricing perspective, following a slight retracement down into early May, we would expect Gold to remain quite strong until mid year. In terms of targets, we would first need to clear USD 1'290/oz. Above that, the next levels of targets we can calculate would lead us to retest 2016 highs (around 1'370) and possibly move into the USD 1'400s/oz. … We expect Gold mines to perform well into midyear following the metal up.

37/ Beware of the impact of Fed tightening by increasing IOR, a new dynamic at play - in late 2008, the Federal Reserve added two items to its tool kit that will fundamentally affect monetary policy making going forward. First, the Fed started to pay interest on reserves (IORs). Second, the Fed amassed an enormous balance sheet. The Fed now attempts to control policy and short-term rates primarily by changing the rate it pays on those abundant reserves, rather than by controlling the quantity of reserves via open market operations, as was previously done. The Fed´s paying market rates for reserves to implement monetary policy may however be self-defeating in one aspect. The correlations among the FFR, Yield Curve and 10yr yield have all become positive. The more the Fed tightens policy (by increasing the IOR), the more the 10yr yield will fall, and the USD weakens.

41/ Timing and Tactical Insight: The yield curve may flatten further before it bounces later in H2 2017 - The FED's recent rate hikes seem to have been counter-productive once again. Indeed, the yield curve has reversed course (now flattening again) and we would expect that it continues this rapid flattening into midyear. US 10Y yields are holding up slightly better, yet they need to hold 1.9% to justify a linear continuation of the uptrend initiated last year. Both point to a new risk-off period ahead, which according to the US equity to Bonds ratio, could start between early and mid May and extend into late June.

44/ MJT 's "Splicing the markets": One last focus on the French Election, … hopefully - Given the polls poor track record recently (Brexit vote, Trump election), the widespread discontent among French voters and a sense of revolutionary feeling against the elite, a surprise win by Mrs Le Pen, although unlikely, is not impossible. Yet Markets are anticipating a Macron victory. Short term, asymmetric protection may still be warranted in the unlikely event of a Le Pen victory.

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