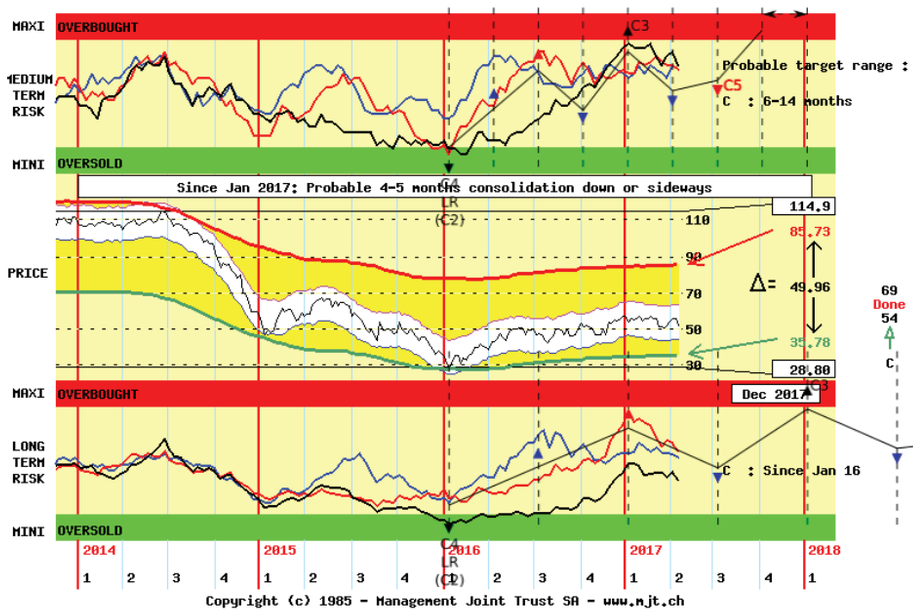
11 / TIMING AND TACTICAL INSIGHT

"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.

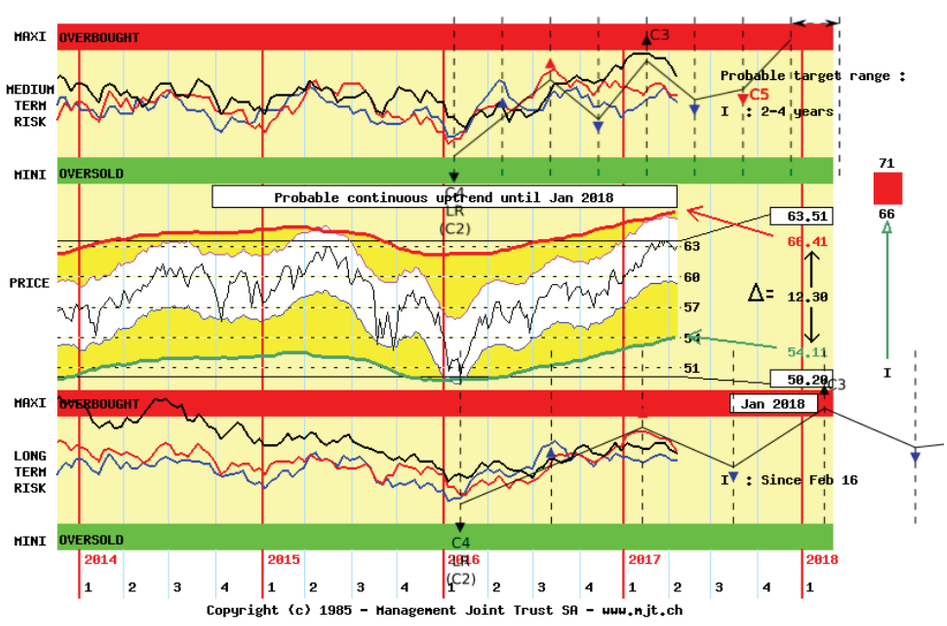
Brent (Weekly graph or the perspective over the next 2 to 4 quarters)



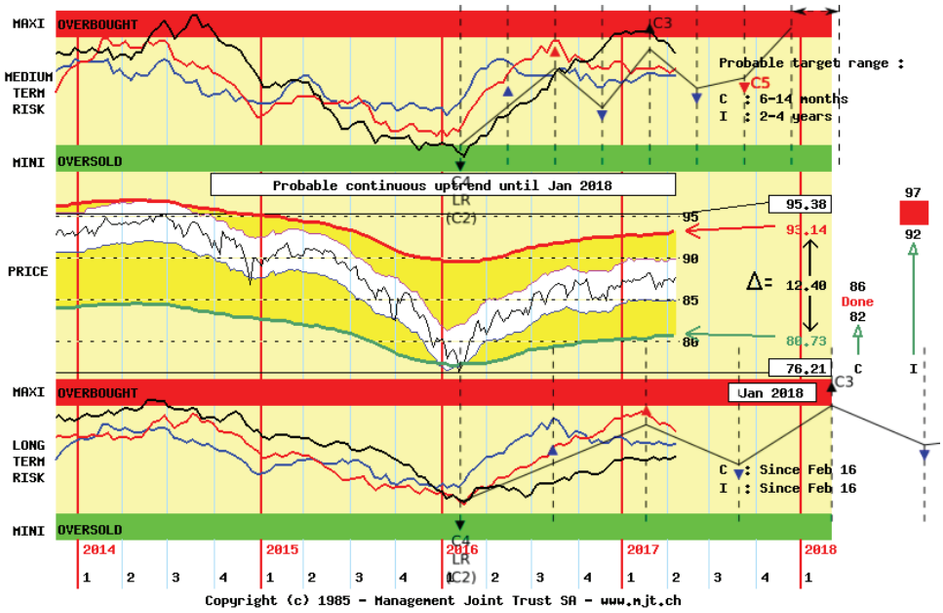
On both our oscillator series an intermediate top was made early in 2017 (lower and upper rectangles). These situations usually result in 4 to 5 months of consolidation or correction to the downside as mentioned by our automatic messaging system. Looking at the models, we project on both our oscillator series, we expect that **this consolidation would probably last into June.** Following that, a new uptrend should materialize in H2 2017 and should at least test the higher end of our corrective targets up in the high 60s towards yearend (right-hand scale).

ACWI - iShares MSCI ACWI Index Fund (Weekly graph or the perspective over the next 2 to 4 quarters)

World Equity markets topped out early March 2017. **The intermediate correction to the downside currently underway could last into June on our medium term oscillator** (upper rectangle) before making a higher low during the Summer in sync with the end of the correction period we project on our longer term oscillator series (lower rectangle). Following that, world equity markets should accelerate up again toward a new top in early 2018. The potential up during H2 2017 and into early 2018 is between 5% to 15% above the tops which were recently made.



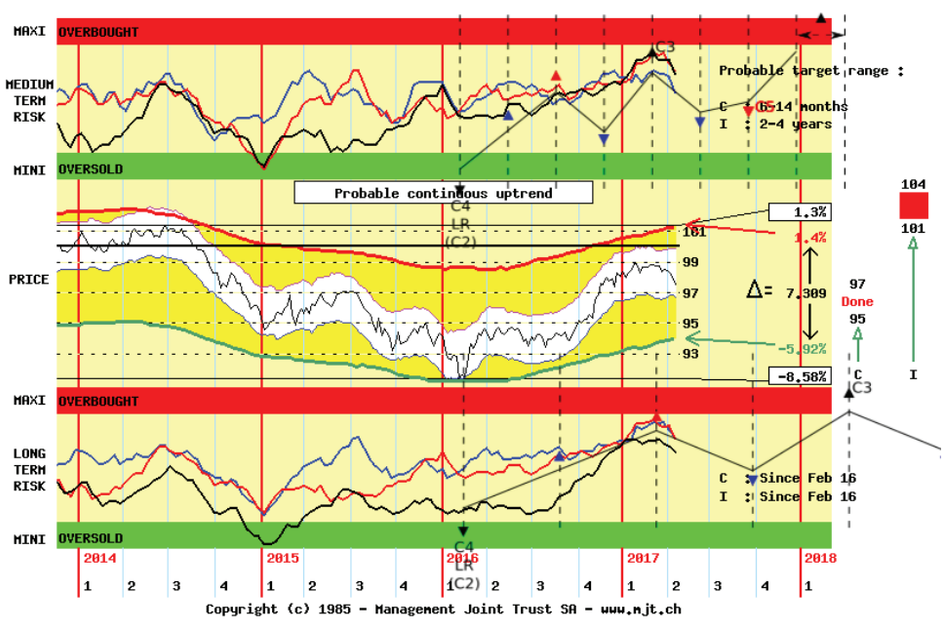
HYG - iShares iBoxx $ High Yield Corporate Bond ETF
(Weekly graph or the perspective over the next 2 to 4 quarters)



US High Yield bonds topped out in late February and corrected down in March. As we suggested in our last newsletter (22nd March) Inflation sensitive assets (which include High Yield) could make a come back during April. This is currently happening. That said, **we believe that another period of retracement to the downside lies ahead probably from May into June** as suggested by the lows we expect on our medium term oscillators (upper rectangle). Following that, these medium term oscillators suggest a higher low during late Summer in sync with the end of the consolidation period we expect on our long term oscillators (lower rectangle) before an acceleration to the upside until Q1 2018 ("I" Impulsive targets up for this move between 5% and 10% from current levels, right-hand scale).

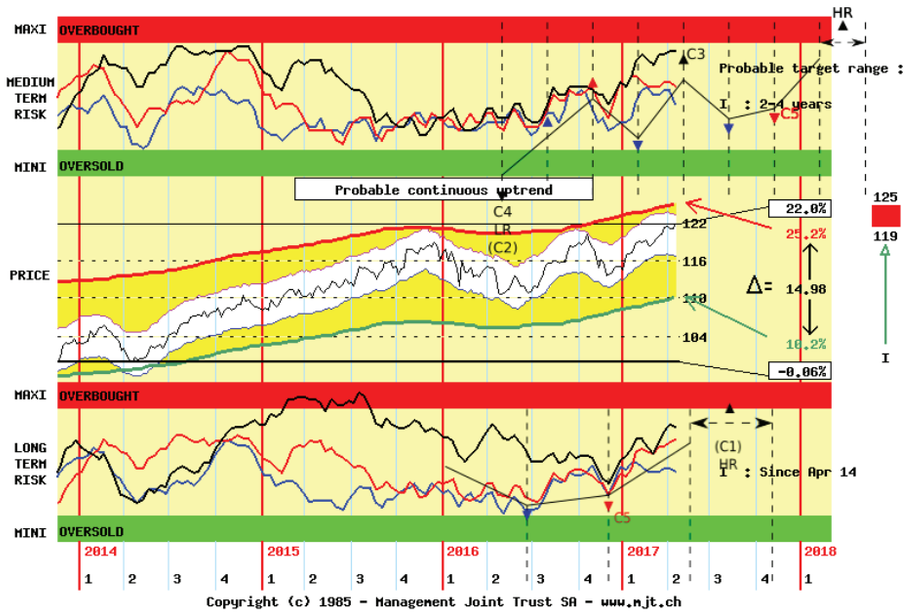
TIP - iShares TIPS Bond ETF / IEF - iShares 7-10 Year Treasury Bond ETF
(Weekly graph or the perspective over the next 2 to 4 quarters)

The ratio of Inflation protected government bonds vs treasuries of the same duration represented by the two trackers above, translates investors appetite to seek inflation protection. **This measure topped out 3 months ago in February. We now expect it to correct down probably towards late Q2** (as suggested by our medium term oscillators; upper rectangle) before making higher lows late Summer in line with the end of the consolidation to the downside shown on our long term oscillators (lower rectangle). Following that, the ratio should resume its uptrend until early 2018 suggesting that inflation concerns will come back in H2 2017.



Now, going back to our late February newsletter, we suggested that we would see a mild consolidation down on equities (between 4 and 7% on the S&P500), stressing however that it would be heavily influenced by, and differentiated throughout the sectors. Hereunder, we review the current outlook for these various intra-market thematics.

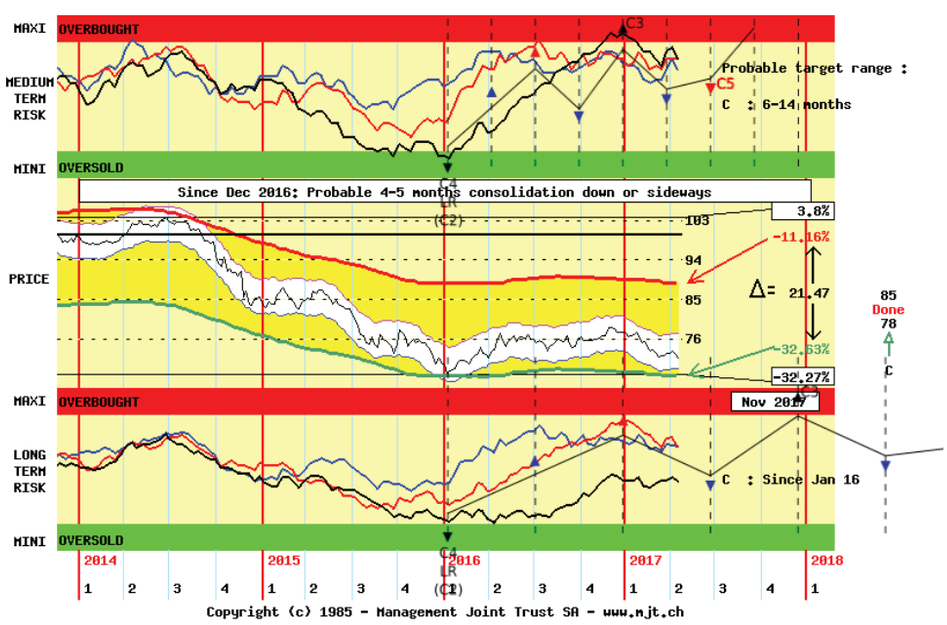
QQQ - PowerShares QQQ Trust, Series 1 / SPY - SPDR S&P 500 (Weekly graph or the perspective over the next 2 to 4 quarters)



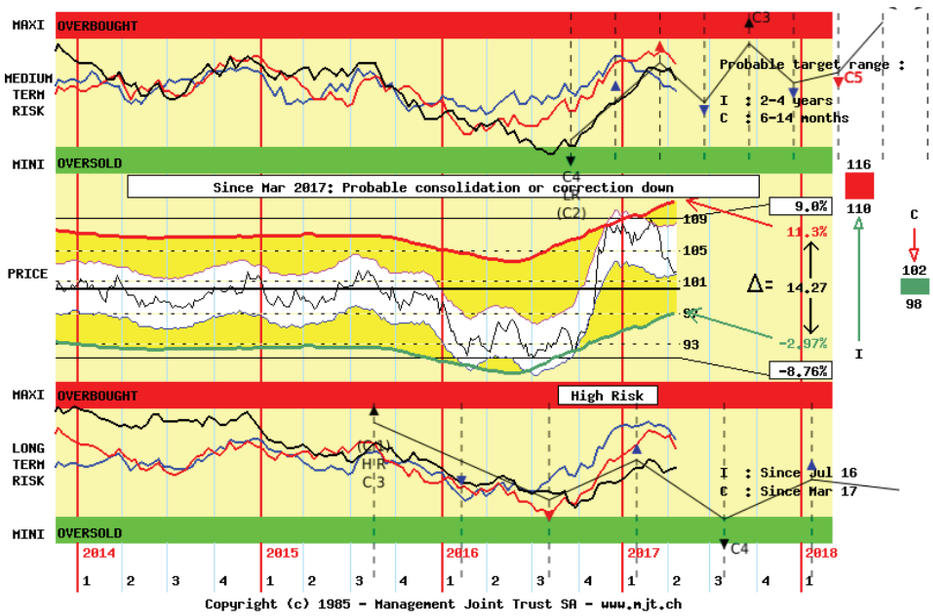
The Nasdaq 100 and big growth stocks more specifically, were as we suggested the winners of the mild consolidation which materialized during March and early April. Going forward, we believe the trade is gradually reaching exhaustion: our "I" impulsive targets up have pretty much been met (right-hand scale), our medium term oscillators (upper rectangle) are probably close to an intermediate top and our longer term oscillators will soon reach a High Risk zone (lower rectangle). If, as we believe, the markets experience a second leg of consolidation to the downside from May into June, their high beta vs the S&P500 could see them start to correct down on a relative basis.

Commodity sectors, equal weighted: XLE (SPDR Energy ETF), XLB (SPDR Materials ETF) (Weekly graph or the perspective over the next 2 to 4 quarters)

We earmarked these sectors in February as being the ones that should bare the most of the correction to the downside expected on equity markets. We then believed that they would probably remain weak "well into Q2 2017". **We now re-confirm this view and expect these sectors** (of which the Energy sector is clearly the weakest, as it is currently retesting relative historical lows) **to remain weak until mid year vs the S&P500**, as shown by the model we project on our longer term oscillators (lower rectangle). Following that, these commodity sectors could make a comeback in H2 2017 along with other reflationary assets.



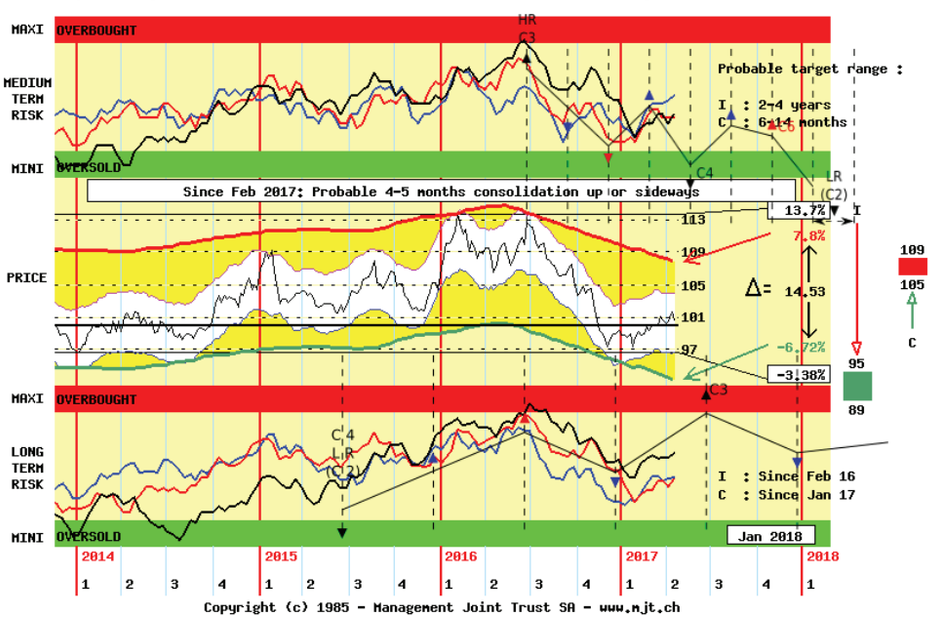
XLF (SPDR Financials ETF)
(Weekly graph or the perspective over the next 2 to 4 quarters)



In February, we had expected Financials to consolidate to the downside vs the S&P500 until late March / early April before potentially moving up again towards mid year. Given our current oscillator configuration (upper and lower rectangles), we hereby revise this view and **would now expect the correction to the downside to last until mid year** before moving up again in H2 2017. We expect that the ratio should find support towards the lower end of our "C" corrective targets down or 3 to 4% lower on a relative basis (right-hand scale).

Defensive Sectors, equal weighted, vs the S&P500 Index, XLP (SPDR Staples ETF), XLV (SPDR Healthcare ETF), XLU (SPDR Utilities ETF)
(Weekly graph or the perspective over the next 2 to 4 quarters)

Invertedly to Financials vs the S&P500, **we had expected in February that defensive sectors continue their correction up vs the S&P500 until late Q1 2017. The models we now project on both our oscillator series** (upper and lower rectangles), **now suggest that this move could continue until late Q2 2017** as risk assets consolidate to the downside once more from May into June. The "C" corrective potential up (right-hand scale) could see them outperform another 4 to 7% during this period. H2 2017 should see them weaken again on a relative basis as reflation trades are reinstated.



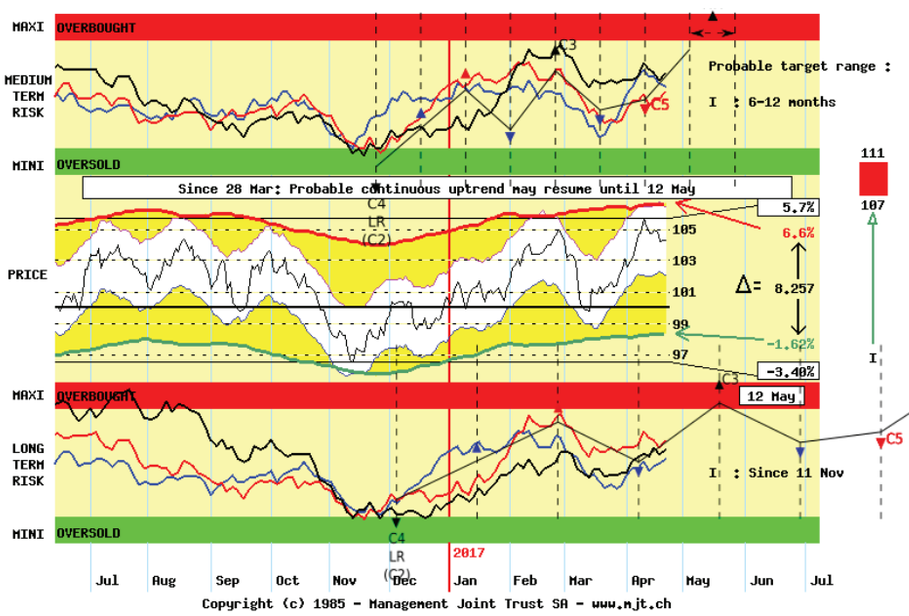
Concluding remarks:

The correction to the downside on reflation trades we had expected from mid Q1 2017 into late Q2 2017 is underway. The first leg down into April has been quite mild and the sectors we then favored (Growth and Defensives) have outperformed, while Energy was particularly weak, as expected. Although we had warned that Financials would correct, they have proven less resilient that we expected. **Going forward, we would extend our call for prudence as we believe a second leg down on equity markets could materialize from May into June, possibly midyear, favoring Defensives over Commodity sectors, over Financials and even over the Nasdaq 100.**

Second leg down in risk assets from early / mid May into June

In our March newsletter (22nd March), we had expected inflation sensitive and more generally risk assets to bounce/hold/extend in April (with limited potential up) before correcting down again in May/ June. Although the outcomes have been broadly in line, some risk assets have been less resilient that we could have expected.

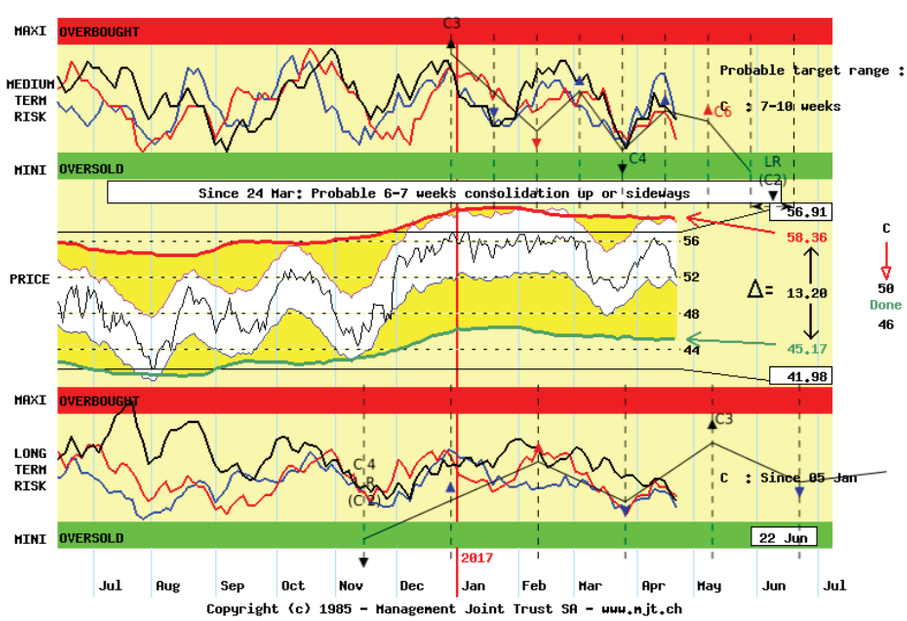
Inflation sensitive portfolio
(Daily graph or the perspective over the next 2 to 3 months)



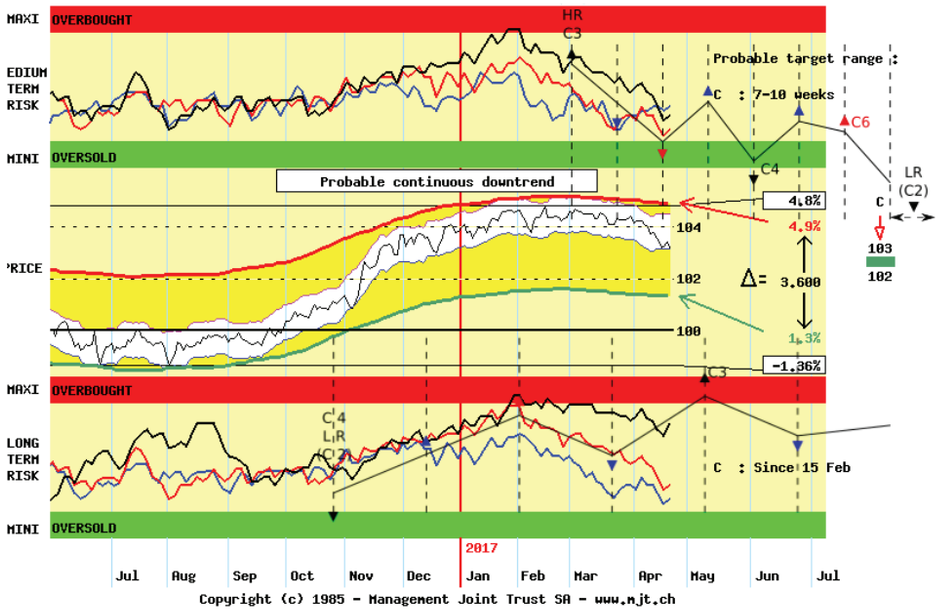
This portfolio we showed last month (equal weighted between Gold, TIPs, REITs, Lumber, High Yield Bonds and Oil) **has been particularly strong as expected**. Given our projections on both oscillator series (lower and upper rectangles) and our automatic messaging (Probable continuous uptrend until 12 May; middle chart), **we expect it to top out in the first half of May** before correcting to the downside towards June and possibly mid year.

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

While Oil has led other inflation sensitive assets from end March to mid April, it has since started to correct down again. **We would await some resilience and a bit of a comeback towards early May** as shown on the models we project on both our oscillator series (lower and upper rectangles), yet expect **more downside during May and June**, possibly testing our "C" corrective targets down between USD 50 and 46 per barrel (right-hand scale).



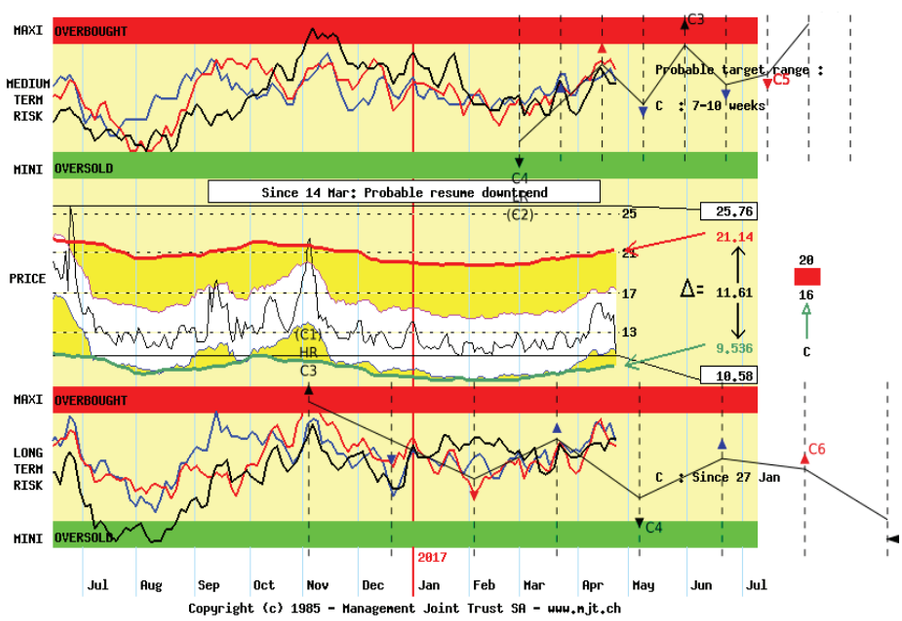
TIP - iShares TIPS Bond ETF / IEF - iShares 7-10 Year Treasury Bond ETF
(Daily graph or the perspective over the next 2 to 3 months)



While inflation sensitive assets were making a comeback in April, sentiment in the bond market, however seems to have reversed. The ratio above, which again, represents investors appetite to protect their bond portfolios against inflation has continued its slide started in mid February. As shown on the models we project on both our oscillator series (lower and upper rectangles), **we expect a slight bounce into early May before the downtrend continues into June and possibly mid year.**

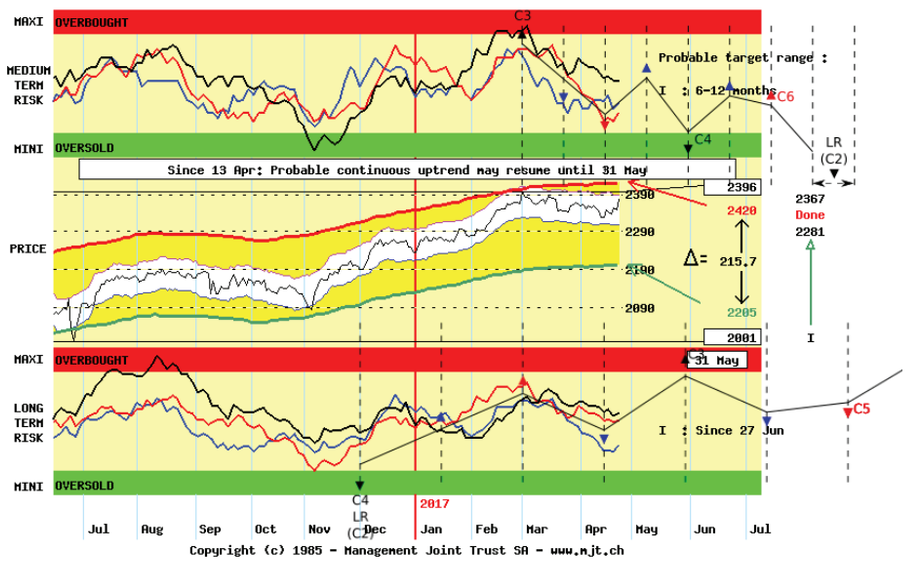
VIX CBOE Volatility Index
(Daily graph or the perspective over the next 2 to 3 months)

The sentiment in the US equity market also seems to have shifted, at least that's what the upside progression during April of the VIX (implied volatility index on the S&P500) is telling us. On the models we project on both our oscillator series (lower and upper rectangles), we expected a retracement of this move into early May. We now know that this has happened on the back of the rather positive results of the 1st round of the French election (which places Mr Macron, a mainstream candidate in pole position).



We now expect VIX to move up again during May and possibly June to reach back above 16, possibly towards 20 (our "C" corrective targets up; right-hand scale).

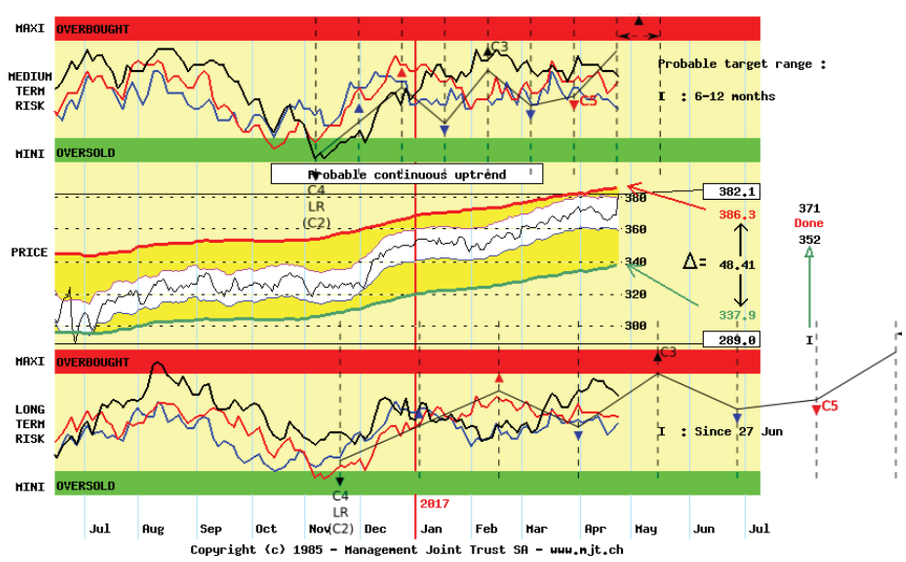
S&P500 Index
(Daily graph or the perspective over the next 2 to 3 months)



The S&P500 Index has been in a slight consolidation to the downside since President Trump's speech to Congress on February 28th. **We were expecting a bounce into early May**, possibly retesting highs as shown by our medium term oscillator series (upper rectangle). Again, this syncs relatively well with the rather market friendly result of the 1st round of the French election. **Following that, we would expect a new leg down to materialize, possibly into June and towards our "C" corrective targets down (2288-2223; calculated not shown yet)**. We favor this scenario over the one shown on our longer term oscillators (lower rectangle) considering the positioning of other risk assets and given that our "I" impulsive targets up have been achieved (right-hand scale).

Dow Jones EURO STOXX 600
(Daily graph or the perspective over the next 2 to 3 months)

European stocks are also extending up on the back of the 1st round of the French election. It is also very interesting to consider how strong they have remained in the run up to this very disputed first round. That said the upward sequences on both our oscillator series (lower and upper rectangles) could soon be coming to an end and **we would expect European markets to top out early/mid May before consolidating to the downside towards June and possibly mid year**. The "C" corrective potential down could then be between 5 and 10% from the highs we will achieve.



Concluding remarks:

Following the rather market friendly 1st round of the French election, the extension we expected in our latest newsletter is materialising. It should continue into early/mid May. Following that, we believe a new period of consolidation to the downside should materialize into June and possibly until midyear.