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A DC&C publication,
featuring MJT's timing methodology



DC&C
DIAPASON CURRENCIES & COMMODITIES



DIAPASON CURRENCIES AND COMMODITIES MACRO ANALYSIS

A Monthly Macro and Asset Review
Featuring MJT's Timing Methodology



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In contrast to previous waves of political risk – which were often concentrated in less developed, lower-income countries and which subsided with the return of economic growth – Vox Populi risk is manifesting itself in middle-income emerging market and industrialized countries which are deeply integrated into the global economy and financial system and where growth is recovering after the recent crisis. Vox Populi risk is therefore becoming less localized and more potentially systemic. The new Vox Populi risk is being fuelled by growing perceptions of income inequality and anxiety about globalization, particularly among middle classes. In developed markets, this has resulted largely in increased appetite for alternative political parties, which have seen an unprecedented spike in support. This has sapped political capital from governments, prompted fragile multi-party governing coalitions and often surprised markets by producing unexpected election outcomes.”

Tina Fordham, Chief Global Political Analyst at Citi.

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Executive Summary

05/ So the Fed raised policy rates 25 bps: this tightening regime should not last very long - "The slightly accelerated tempo (two further rate hikes this year) just puts the Fed back to where they started in 2016, except that (after the debacle of the December 2015 tightening), the Fed expects this "gradual" tightening to actually work out this time ... One implicit reason for the Fed's resuming the tightening regime is that growth will be "Stable"- but this assumption may be tested in a few weeks when Q1 2017 GDP growth will be reported."

07/ Timing and Tactical Insight: Yield curve - While the US yield curve has started to flatten since December on the back of the US rate hike anticipation and consolidating oil prices, we believe that this situation is transitory. We expect a slight steepening in April, renewed flattening in May/June, before the long end of the curve accelerates up in H2 2017, while the short end remains capped by the maturing business cycle (i.e. commodity-led inflation overruns US growth in H2).

12/ The political cycle: Will the winds of change keep on blowing over France? - "For the past 10 months, the political cycle of elections has come with its elements of surprises ... However, if we look at the capital markets' reaction it seems that those elections have created an increase of volatility through market corrections ... but have not derailed the underlying reflation trend ... The markets have so far been focused on the all-important presidential election but the answer might come with the national assembly ... if Mrs Le Pen were to be elected, her actions would be constrained."

14/ Timing and Tactical Insight: French election - Despite the looming French election, European equity markets seem very well positioned to carry on their trends until end 2017 – early 2018. In terms of protection, we look at alternatives to the OAT – Bund spread, which seems crowded, or the DAX vs CAC pair trade which is already Overbought on our long term charts. We would consider Gold as an asymmetric protection for now, although its trend seems promising beyond May if one can cope with the volatility that could arise from the binary outcome of the election. EUR crosses are reversing up, hence a sell-off on a Mrs Le Pen election would be counter-trend and short lived.

21/ Core CPI will decline soon, as credit creation slows and the housing market starts to peak - "As the housing market starts to peak, as mortgages rates continue to rise, the rent component of Core CPI will start to fade. But the situation is exacerbated by the fact that recent price increases have been entirely in goods that consumers cannot go without – gasoline and rent. Slow economic growth combined with the "bad" kind of inflation is not a recipe for a happier consumer."

23/ Timing and Tactical Insight: Inflation sensitive assets - Inflation sensitive assets (and Oil) make a come back in April before a new sell-off in May/June. Gold is more defensive and should resist better towards late Q2 2017. The second half of the year should see Oil accelerate on the upside, while Gold follows once US growth and the US Dollar deceive.

27/ Equity prices and bond yields moving contra to each other: look for liquidity factors to explain the move – "The yield on the-10year Treasury bond has gone above 2.6 percent ... a level "Bond King" Bill gross considers to be a "tipping point" for future interest rate levels ... The equity market was not saved from speculations that rising rates will "destroy" valuation. The Nobel Prize of Economics winner Robert Shiller was also talking about the US stock market being overvalued ... The situation is better understood as a liquidity issue ... The election is now history, and so the US Treasury has embarked in an effort to offset all the liquidity that was meant to influence the election ... We expect those dynamics to cause a sharp sell-off in the equity markets and a sharp decline in bond yields in late April."

29/ Timing and Tactical Insight: Equities and Bond Yields - Equities and Bond Yields should find support between now and early April to then extend up at high levels until the end of April. A correction on the downside should materialize into May/June.

35/ MJT 's "Splicing the markets": Inflation vs the Dollar in H2 2017- EUR/USD should confirm a significant bottom between now and late Q2 2017. During the second half of the year, it could accelerate up towards 1.15 – 1.22, while US to European yield spreads narrow, inflation sensitive assets outperform equities and World markets outperform US equities (a dangerous cocktail where US inflation overruns US growth, not dissimilar to the run-up to the Great Financial Crisis).

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So the Fed raised policy rates 25 bps: this tightening regime should not last very long

So the Fed raised rates 25bps, an outcome that was pre-ordained as long as a week ago, after the February jobs data exceeded expectations and following a round of Fedspeak in the week prior to the blackout period. The only drama left of the FOMC meeting was what signal the Fed sends with the statement, the nuances expressed during the press conference, and the rearrangement of the so-called “SEP dots.” The Fed did not disappoint the monetary policy hawks with the overall message signalling general confidence in the economic outlook while providing assurances that the Fed is neither behind the curve nor intends to fall behind the curve. The Fed took the optimal route, giving itself room to tighten policy at a gradual pace if they so desire. Given the Fed’s pent-up desire to normalize policy, and given the cover that they were provided by the labor data set, two further hikes this year is indeed gradual as viewed from the Fed’s perspective and many market participants. But basically, the slightly accelerated tempo just puts the Fed back to where they started in 2016, except that (after the debacle of the December 2015 tightening), the Fed expects this “gradual” tightening regime to actually work out this time.

But we ask: “gradual” relative to what? And what makes them so sure (otherwise, they would not have raised rates) that there will be no repeat of the post-December 2015 climbdown? We have serious doubts that this long, so-called “gradual” tightening regime will gain much traction in the light of developments happening in the yield curve space and in some of the underlying data that matters. One feature of the bond markets that was brought about by the repression of the short-term rate since the Great Financial Crisis (GFC) is that most movements in the 3M/10Y yield curve now occur at the long end of the curve. Prior to the GFC, it was the other way around due to the sensitivity of short-term Treasury bond yields to adjustments in monetary policy.

Nonetheless, the negative comovement in the changes between the 3M/10Y and the Fed Funds Rate has remained – and is a testament to the flat nature of the short end rate – most of the changes in the curve is accounted for by the long rate which is a strong discounter of future events. And the crucial element in the relationship is that changes in the yield curve tends to lead the changes in the policy rate, exactly due to the anticipatory characteristic of the now more active long rate (see chart below). We routinely use the 3-month Treasury bill rate as a proxy for the Fed’s policy rate (the Fed Funds Rate, FFR). Therefore, it makes sense that if you juxtapose the yield curve against the FFR, changes in the yield curve provides a view of what to expect from the FFR future moves, with a lead of at least one quarter (see first chart on next page).

The usual narrative about the slope of the yield curve that you read in the media has not been “upgraded” by the fact that the Quantitative Easing (QE) programs conducted by the Fed as a response to the GFC has changed the nuances in the relationship of many financial variables. The narrative remains the same. “Raising short end rates does not shift long-term yields. As a result, the yield curve becomes flat

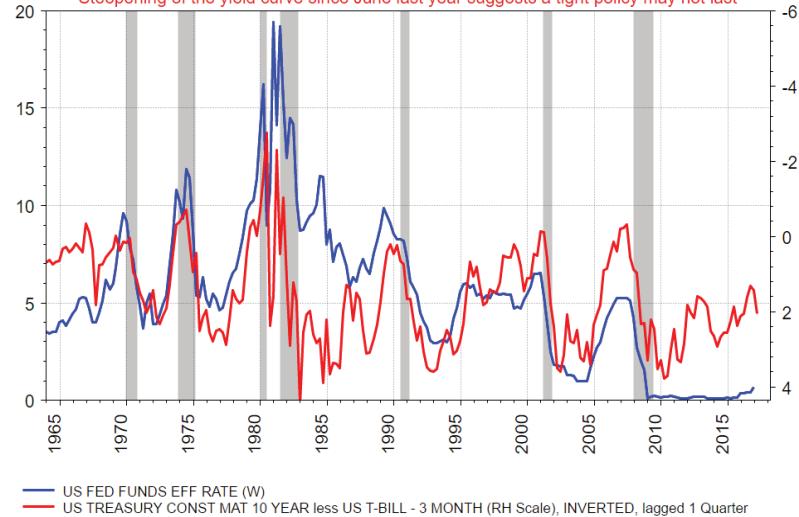
and in some cases, inverted. This is important as an increase of spreads usually indicates that investors are optimistic about the growth rate of the economy while, on the other hand, a narrowing of spreads implies a weakening economic outlook.” This interpretation is not essentially incorrect, but it misses the important nuances in the signalling process provided by the yield curve on monetary policy. Steepening of the yield curve does not necessarily imply that investors are optimistic about the economy – the shift in the orientation of the slope from flat to steep merely means that investors began to anticipate that the tightening regime of the Fed is about to end, or is not going to last long if the steepening happens at the start of a tighter policy regime. And that curve steepening opens a can of worms insofar as economic growth is concerned, and investors have no reason to cheer a steeper curve if its implications to credit supply and to job creation are properly understood.

One implicit reason for the Fed’s resuming the tightening regime is that growth will be “stable” – but this assumption may be tested in a few weeks when Q1 2017 GDP growth will be reported. It is looking a little grim, if the Atlanta Fed’s GDP Nowcast is to be believed. Its real

The negative comovement between 3M/10Y yield curve and Fed Funds Rate

Flatter curve since 2010 suggests policy has been tightening since then despite a flat FFR

Steepening of the yield curve since June last year suggests a tight policy may not last



GDP growth (seasonally adjusted annual rate) Nowcast in the first quarter of 2017 is at 0.9%. Another reason for concern is a development, which may or may not be linked, to this grim growth outlook being projected by the Atlanta Fed growth model -- a sudden collapse in loan growth in general, and in the crucial Commercial and Industrial Loan segment in particular. It is a collapse which has the normally staid Wall Street Journal describing it as an «ominous economic signal.» Total loans and leases by U.S. commercial banks are currently rising at an annual pace of about 4.6%, which is down from a 6.4% pace for all of 2016, and from the peak rates of circa 8% during mid 2016. This is the slowest pace of debt creation since early 2014. The WSJ noted that «is at odds with the idea of a stronger economy and rising sentiment,» as deceleration has been broad-based among business, real estate and consumer lending. The decline in growth rates and in nominal volumes have been particularly sharp in the Commercial and Industrial loan category, which has unexpectedly fell to just 4.0% as of the latest week, relative to the pace of growth of 10% during the first half of 2016. The falloff was circa 50% lower than the 7% growth posted earlier in the year. The current loan growth is the lowest pace since July 2011.

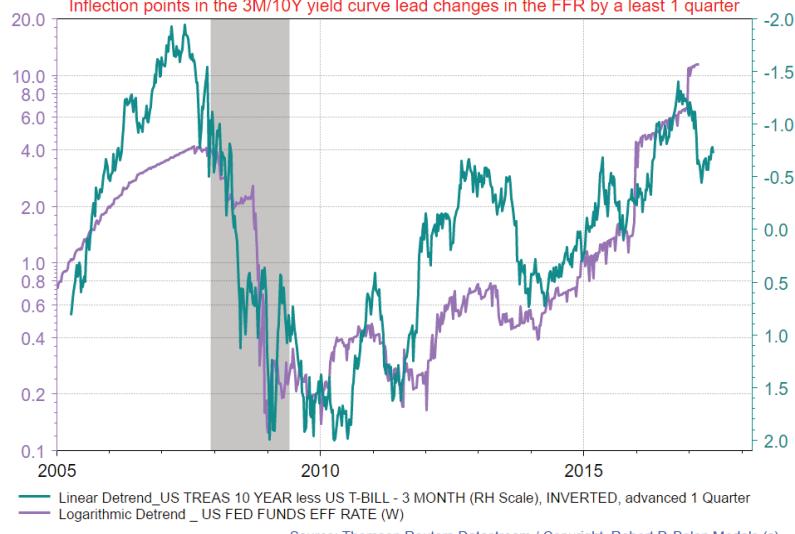
Simply put, the banks did hit the brakes on lending, and it has something to do with the improvement in their Net Interest Margins (NIMs). The current improvement in NIMs has something to do with the steeper yield curve which we saw from June 2012 to January 2014. It takes a while before the steeper curve translates into wider NIMs, which started to expand since Q2 last year. In a sense, the current fall-off is a stronger response into that widening, and bank lending drought will continue for some time, perhaps until at least late Q3 this year. But the flatter yield curve between July 2015 and September last year should bring relief to the loan situation shortly. The lags between the yield curve and actual changes in micro-data are long, at least 5 quarters even 7 quarters in some cases, so it is easy to overlook the rationale for a micro-event that is happening now. There is no “efficient economy hypothesis” for yield curve related financial phenomena.

The impact of the yield curve-NIM dynamics does not stop with the banks’ credit-creation process. If we go back to First Principles and identify

The 3M/10Y yield curve (inv) tends to signal changes in the Fed Funds Rate

A steeper curve signals the markets’ unease with the Fed’s tightening regime

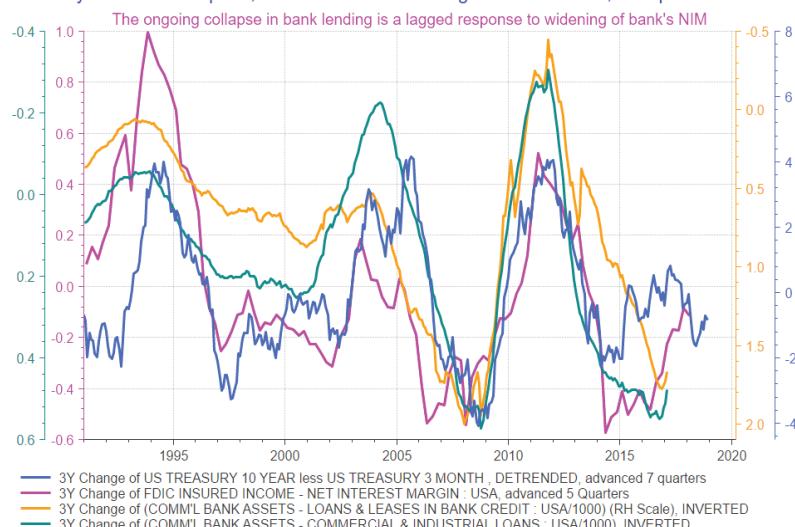
Inflection points in the 3M/10Y yield curve lead changes in the FFR by a least 1 quarter



Source: Thomson Reuters Datastream / Copyright: Robert P. Balan Models (c)

The impact of the yield curve on banks' NIMs and loan portfolios

As the yield curve steepens, banks' Net Interest Margin become wider, loan portfolios shrink



Source: Thomson Reuters Datastream / Copyright: Robert P. Balan Models (c)

the crucial data sets which influence the jobs market in the core, there nothing more primary in this regard than credit extended by commercial banks, the steepness of the yield curve, and the banks’ consequent Net Interest Margin (NIM) – and now this foundation of the current job phenomenon is under attack. To understand how this comes about, we have to follow the narrative from the outset (see second chart above). Collectively, if banks’ non-performing assets are high, their NIM will go down if the interest earning assets are steeply reduced by non-performing assets, and vice versa. A steeper yield curve provides better conditions for the banks’ NIM to rise, which reduces the need for larger portfolios for riskier loans – hence loan levels fall when the yield curve steepens. The linkage to the job sector flows from the steepness of the yield curve to the amount of

lending then to the jobless insurance claims and the unemployment rate. Put another way, when the yield curve steepens, commercial lending volume falls, and the tighter credit situation impacts hiring and payroll growth after a lag, with concomitant effects on unemployment and jobless insurance claims.

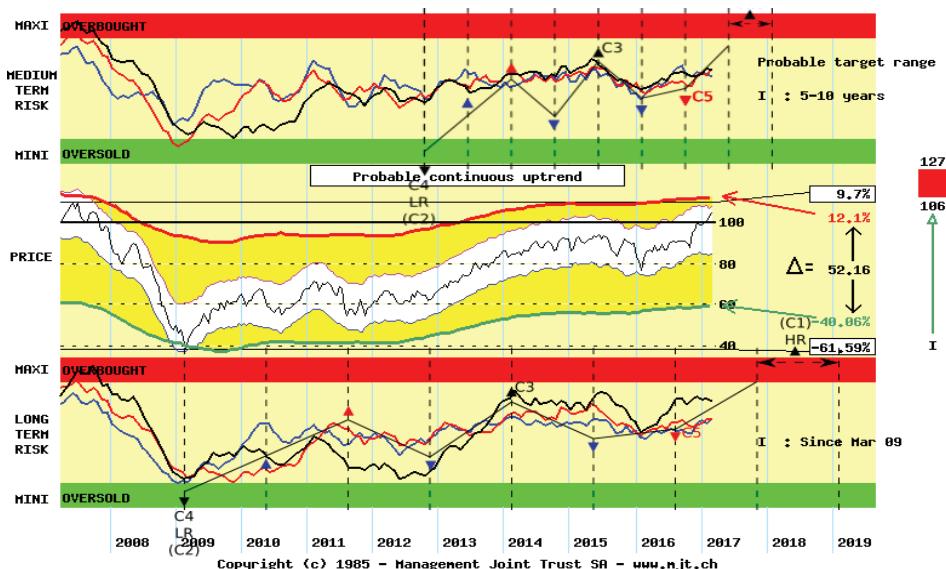
Developments in lending usually take several quarters to manifest in the jobs market, so it may be that we have a few more months of jobs growth. But it is increasingly becoming clear that the upswing phase of the current Business Cycle is starting to show signs of aging. Under these conditions, we do not expect the Fed to be able to tighten policy for as long and as quickly as they have indicated in their current Summary of Economic Projections (SEP) dot plots.

7 / TIMING AND TACTICAL INSIGHT

Mild flattening of the Yield Curve, before it steepens again in H2 2017

The FED's move to hike this week was labeled as "Dovish hike" as it gave little guidance as to where rates were headed in the long run. Concomitantly, with Oil on the correction path, many analysts are viewing these developments in the yield curve as a "Bearish flattening" (the short end rising faster than the long end). We believe that this situation is transitory.

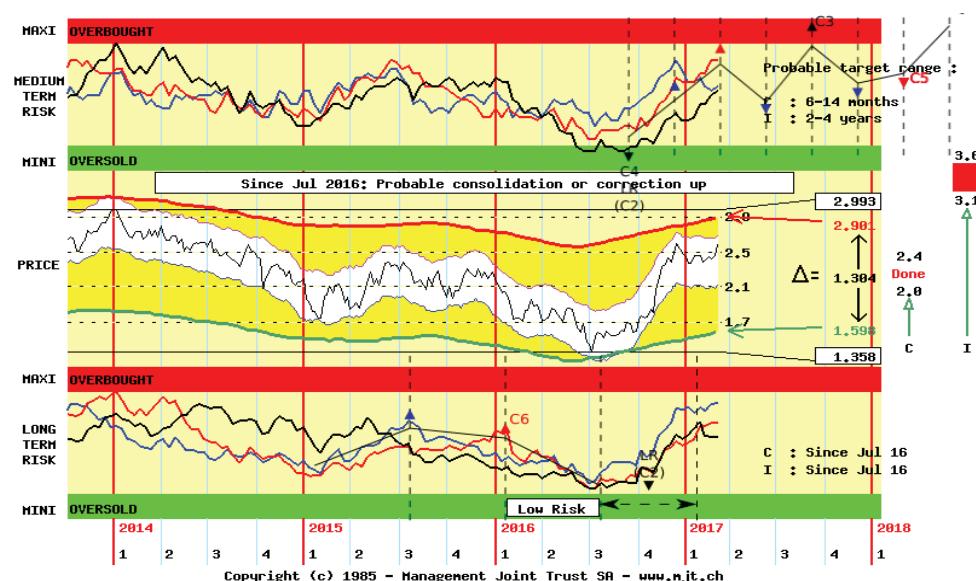
S&P500 vs Treasury Notes 10 Years Contract (Mar) (Bi-monthly chart or the perspective over the next 1 to 2 years)



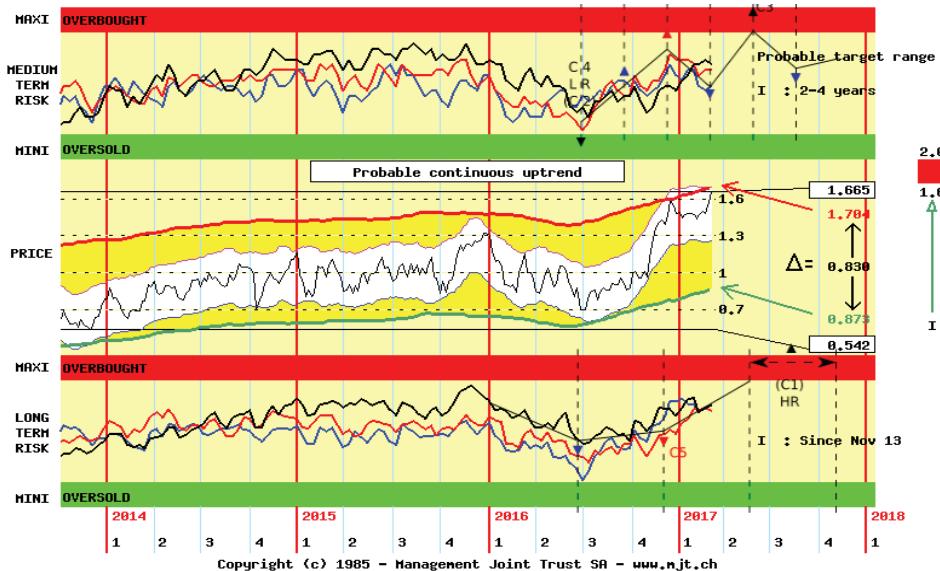
We use this equity to Bonds ratio as a revealing agent of reflationary and dis-inflationary periods. Following the lows made in Q1 2016, the long term trend is heading up again. The sequences on both our oscillators series (lower and upper rectangles) point to further acceleration in the reflation path until tops are made towards late 2017 or into H1 2018. The potential for Equities versus Bonds during this period (targets, right-hand scale) suggests an out-performance that could reach 10% to 20%.

US 10 years Benchmark Bond Yield (Weekly chart or the perspective over the next 2 to 4 quarters)

Having reached a Low Risk position last July (lower rectangle), long term yields have risen rapidly during H2 2016. This move could take a pause until late Q2 2017 as an intermediate top is forming (upper rectangle). The first move up took US 10 year benchmark yields above the resistance of their "C" corrective targets up (right hand scale), the second one should see them accelerate towards 3.5% in H2 2017 ("I" impulsive targets up).



US 3 years Benchmark Bond Yield (Weekly or the perspective over the next 2 to 4 quarters)

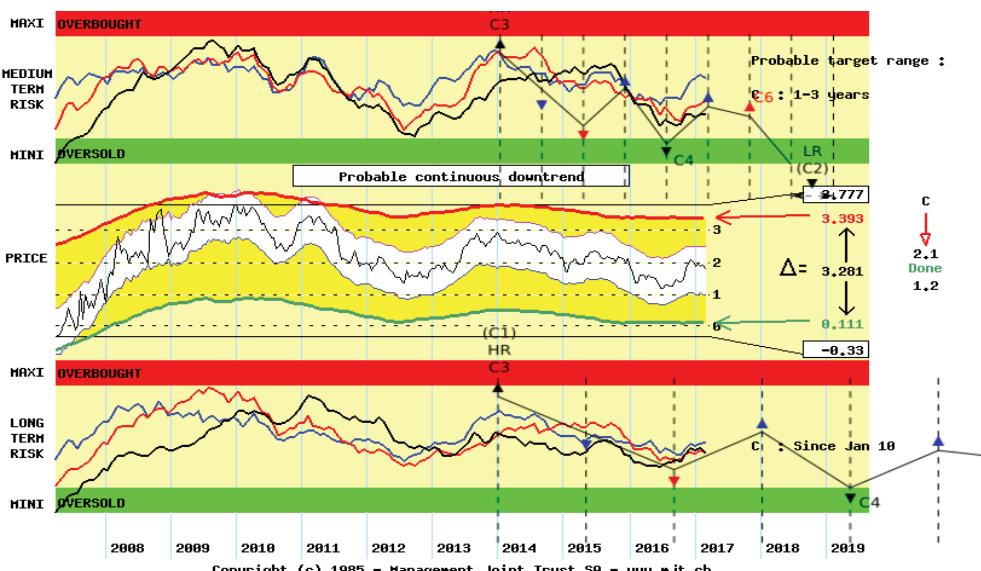


Yields on shorter term US benchmark tenures also accelerated up during H2 2016. The move started from higher levels and the "I" impulsive potential up left is now more limited in comparison to long term yields (towards 2%, right-hand scale). Indeed, the trend (and effective tightening) has been ongoing since May 2013, when Bernanke made his famous "tapering speech". This 2% target would theoretically leave room for another 2 rate hikes before shorter term yields top out during H2 2017 (the

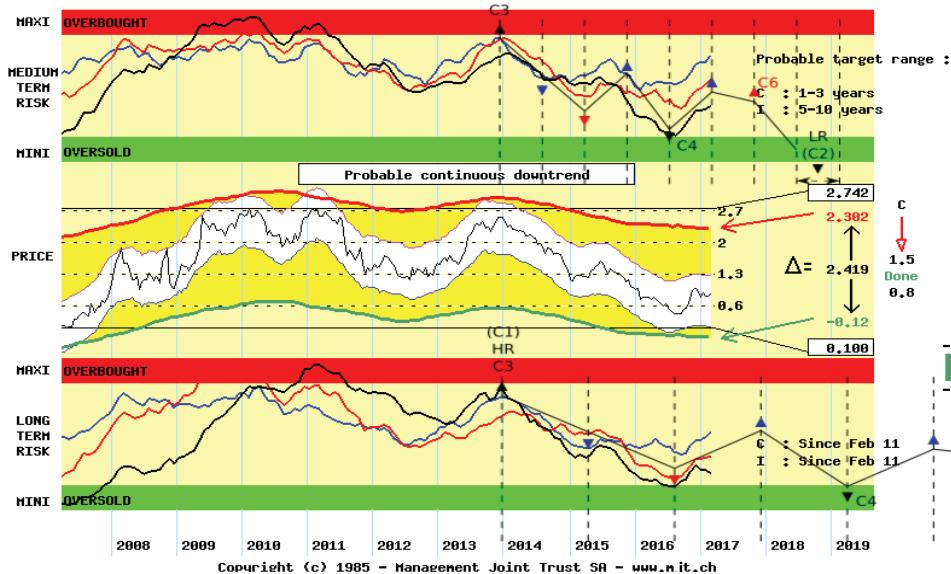
sequences on both our oscillator series; lower and upper rectangles). Hence, our view is that dovish hikes could continue until they are ultimately halted towards late Summer.

US 10 years Benchmark Bond Yield - US 3 Months benchmark Bond Yield (Bi-monthly chart or the perspective over the next 1 to 2 years)

A Flattening yield curve announces that a recession may be coming, while a Steepening yield curve (market tightening of financial conditions) just precedes it / triggers it. This was the case in 2013, with a slight lag into 2014 prior to 2nd EURO crisis, in 2011 prior to the 1st EURO crisis and just before the GFC in 2007. The curve has made a first leg up during H2 2016 and could be already rolling over (our medium term oscillators, upper rectangle). Yet, the sequence on our long term oscillators (lower rectangle) suggests that it could move up again in H2 2017, i.e. our preferred scenario for now. We expect a slight flattening on the current top into late Q2 2017 and then a renewed steepening towards end 2017.

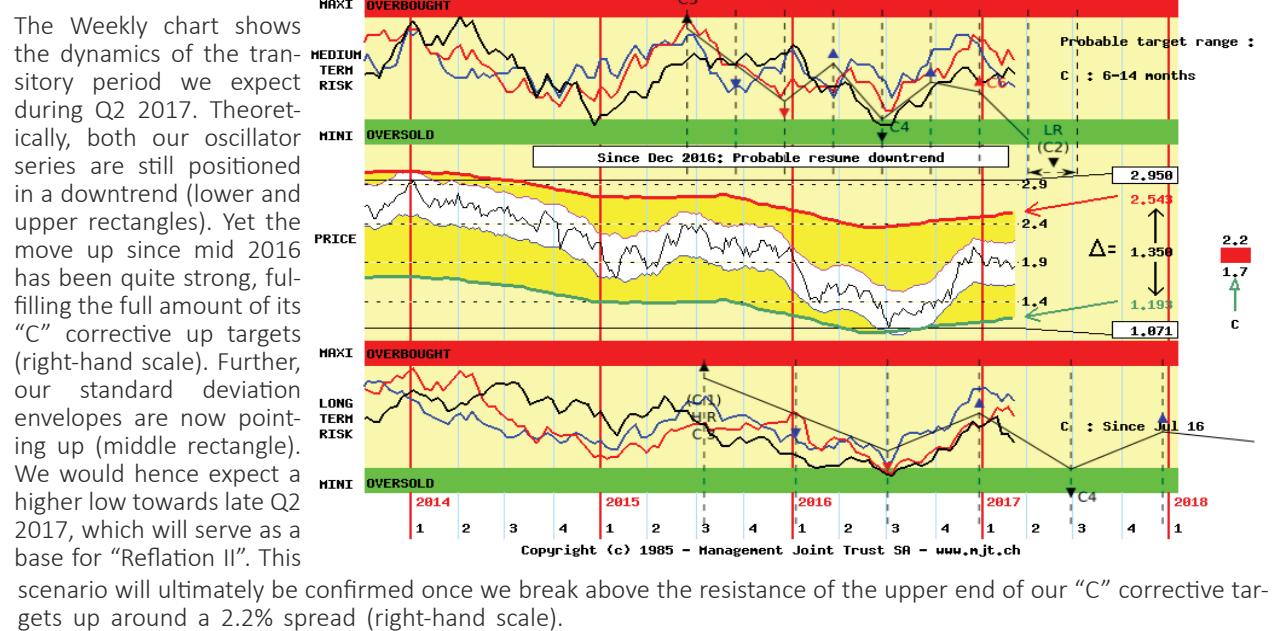


USD Swap Rate 10 Years - USD Swap Rate 2 Years (Bi-monthly chart or the perspective over the next 1 to 2 years)

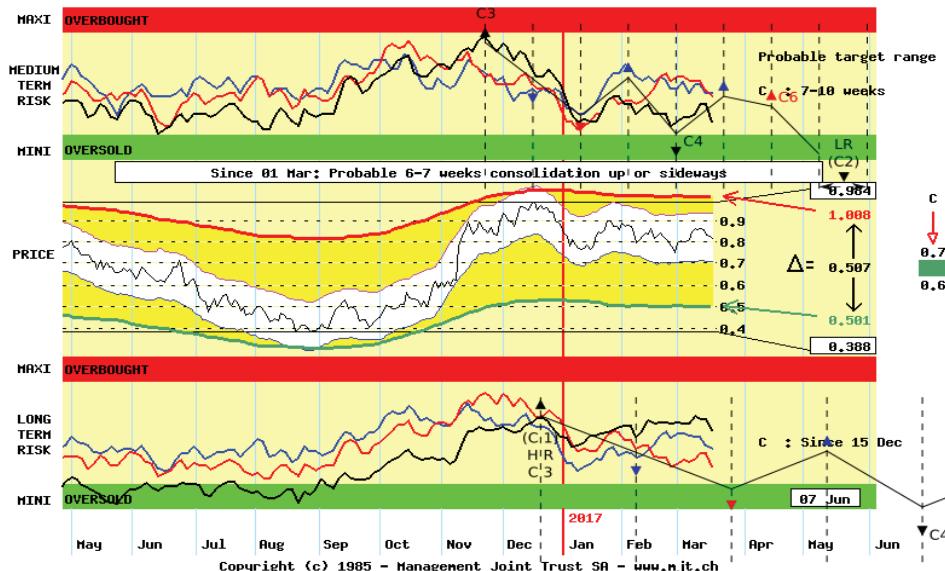


The swap rate curve made an more pronounced bottom in mid 2016 (our longer term oscillator series; lower rectangle) than the benchmark bonds one, raising the probability that the latest steepening move is only a first leg up and that a second one could materialize during H2 2017. We would label this period "Reflation II" as the dynamics may prove slightly different from the period we just saw.

US 10 years Benchmark Bond Yield - US 3 Months benchmark Bond Yield (Weekly chart o the perspective over the next 2 to 4 quarters)



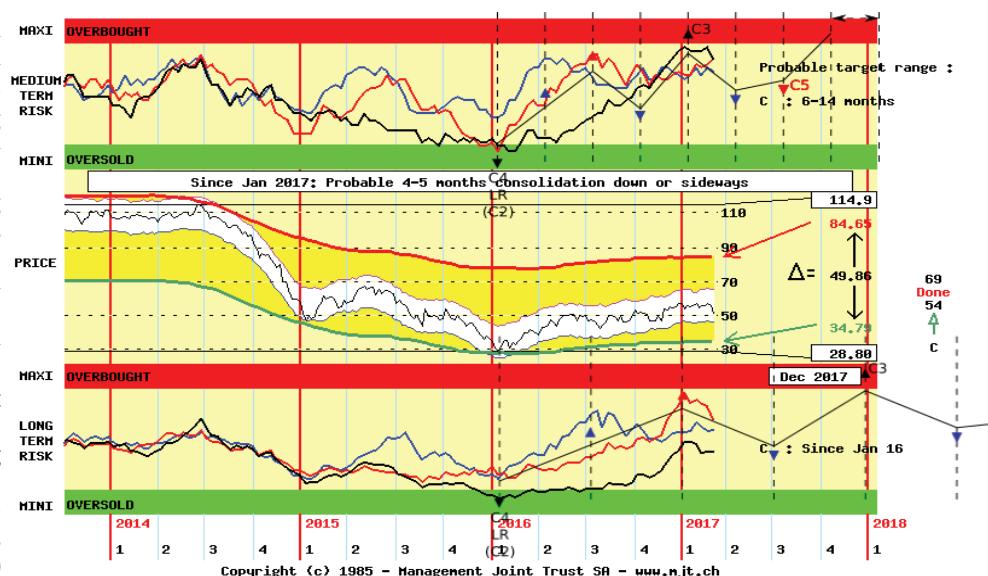
USD Swap Rate 10 Years - USD Swap Rate 2 Years (Daily chart or the perspective over the 2 to 3 months)



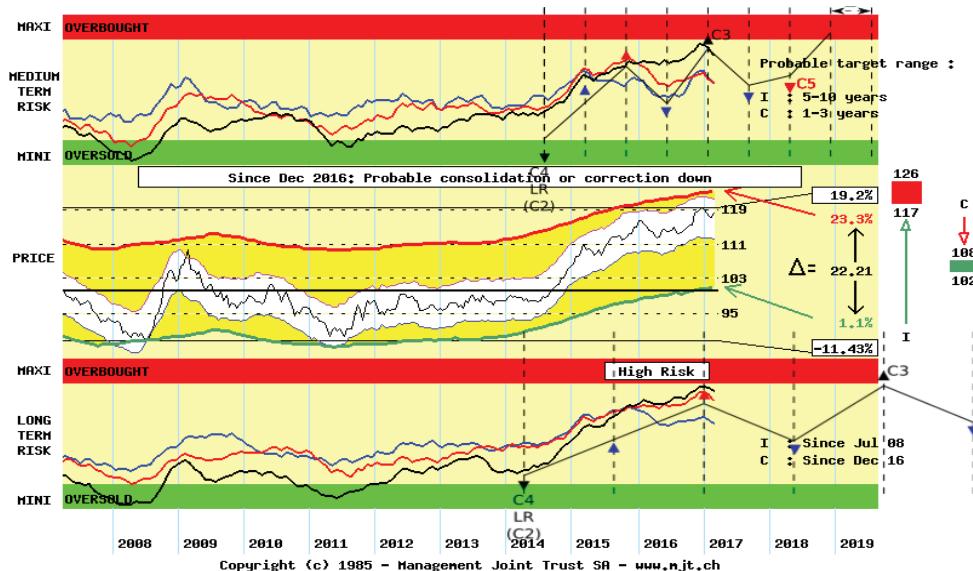
expect this flattening to make new lows, potentially retracing towards the support of our corrective targets down around 0.7% – 0.6% (or 10 to 20 bps lower on the spread), hence creating a nice base to move higher in H2 2017.

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

Oil has been the key reflation asset during “Reflation I” and will prove crucial again in fomenting “Reflation II”. As we expected in our last letter, oil is now consolidating down following the tops recently made on both our oscillator series (upper and lower rectangles). We believe it should resume its uptrend from late Q2 2017 to go test the upper end of our “C” corrective targets during H2 2017 (USD 69 / barrel). Above those levels, the next price target range is between USD 90 and 100 a barrel.



Trade Weighted Dollar (TWD) – simulated using effective weightings (Bi-monthly chart or the perspective over the 1 to 2 years)

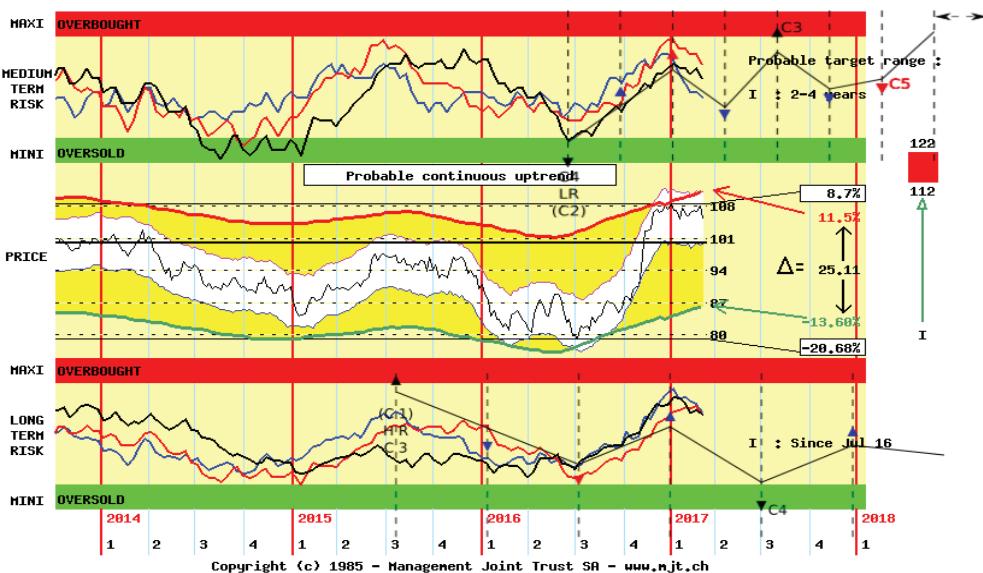


This is the Dollar the FED monitors as it is the one, the US consumers actually feel. On this long term chart, both oscillator series (lower and upper rectangles) have confirmed a potential top. "I" impulsive targets up (right-hand scale) were reached while the "C" corrective potential down now indicates a range from minus 10% to minus 20%. We believe this correction to the downside could accelerate from late Q2 2017 towards year-end (while, as we mentioned above, oil moves up

again). Inflation expectations should also increase, long term rates should follow suit, while the short end could be capped by the maturing business cycle (i.e. the worst kind of inflationary pressures, not dissimilar to what was seen during 2007).

KBE – S&P Bank ETF vs S&P500 Index (Weekly chart or the perspective over the next 2 to 4 quarters)

Banks are a great proxy for the trajectory of the yield curve. As it steepens, margins on their lending business improve, allowing them to shift some resources to less risky fee generating businesses. This is why they are often considered late cycle movers. Their Weekly relative chart to the S&P500 is very similar to the one of the Yield Curve (10Y-3M) above. Similarly, we expect a mild retracement of their outperformance towards late Q2 2017, before they accelerate up again in H2 2017.



Concluding remarks:

We've reached the eye of the storm as far as reflation goes. During this transitory period, we expect some retracement of reflation trades until late Q2 2017. Following that, a second leg of the reflation trend should materialize in H2 2017 ("Reflation II"), fueled by a new rise in oil prices, a weakening Dollar, higher inflation expectations and a maturing business cycle. It will ultimately lead to further steepening of the yield curve.

12/The political cycle: Will the winds of change keep on blowing over France?

"Political language is designed to make lies sound truthful and murder respectable, and to give an appearance of solidity to pure wind" G. Orwell

For the past 10 months, the political cycle of elections has come with its elements of surprises, where mass manipulation through the media and polls have failed. The populations of England and the US have turned against their elite systems and have expressed their vote of discontent in a way that was unexpected by the media and the establishment. This has led to results for the English referendum and the US election that were far out of the consensus. One reason behind this gap might be that our world and political order has started to shift, with the old order (the one of the past 25 years) falling apart and a new world starting to shape up on the back of a generational shift. In many ways, this is reminding us of these transition periods described in the *World of Yesterday* by S. Zweig, where an old order is disappearing and a new one is shaping up. On the political side, the changes are drastic. However, if we look at the capital markets' reaction to them, it seems that those elections have created an increase of volatility through market corrections or set backs in equities and commodities, but have not derailed the underlying reflation trend which at that time was progressing fairly unnoticed (see graph on this page). The surprised Brexit vote lead to a sharp equity sell offs (minus 10% from April to June in the Footsie 100 and 5% in the S&P500), a 20% collapse in Sterling and a bond rally of 10% (US10y) on the news. Yet, it also proved to mark the low point of interest rates and triggered a spike in Gold which created the high point of the gold market for 2016. Nevertheless, thereafter, the early existing trends of reflation reasserted themselves. Similarly, the Trump election created a correction in equity markets, a short spike in gold and a small fall in rates, only to be followed by a strong risk-on period, where equities rallied, rates rose while

Gold, Yen and volatility collapsed.

Today with the markets having adjusted significantly following the Trump election, our task is to try to evaluate if in this context, there is room for surprise in the French election, which once again could create a sharp pricing adjustment in many asset prices.

Now, if we look at the current set up for the French election, some concerning elements have started to build as we approach the vote period which will take place in 2 stages: on the 23rd of April to determine the last 2 contenders for a final round and on the 7th of May to decide between them. At this stage, 3 candidates (with various probabilities) stand a clear chance to be France's next president: Marine Le Pen from the National Front party, Francois Fillon, an ex prime minister from les Républicains, the conservative party equivalent in France, and Emmanuel Macron, the ex-economy and finance minister of the socialist president Hollande, who created a new political movement ("En Marche"), an initiative meant to detach himself from the poor legacy of the current socialist government.

As market participants, our main concern has always been to establish where the consensus is, and from there, what are the

probabilities for results to come out away from this consensus as well as try to estimate their impact on asset prices.

As this is written, and dialoguing with many of our correspondents in France, the clear consensus is that Marine Le Pen would win the first round only to be defeated without any doubt in the second round by either Mr Macron or Mr Fillon. This situation is very close to the situation to the Brexit or Clinton/Trump perception before the election. The Opinion way/ Orpi polling institutes (17th of March) are considering that Mrs Le Pen would receive 28% of vote, Mr Macron would gather 25% and Mr Fillon 20% in the first round. For the second round, Mrs Le Pen would lose 41%/59% vs Mr Macron and 45%/55% vs Mr Fillon. In a way, the consensus is a repeat of the 2002 election results where Mrs Le Pen's father, Mr Jean-Marie Le Pen contended Mr Jacques Chirac in the second round. Mr Chirac easily won with a 82.21% vs 17.79% vote.

However, during the last 15 years the spirit of the times has changed a lot and today, the winds of discontent are fed by poor growth (see first graph on next page) due to the failed socialist policies, high unemployment level due to lack of structural reforms (see second graph on next page), high debt, poor political leadership, heavy taxation, distrust of the political class

S&P 500 Comp Index vs FTSE 100 Index



and worries about immigration and terrorists issues. Those issues are feeding the discontent vote and the key question is how much of this will translate into votes for this election.

Two factors, which are also key to account for at this stage, are that according to polls, 30% of voters remained undecided, while 75% of Le Pen supporters say they would not change their minds. Only 51% of potential voters for Macron said the same.

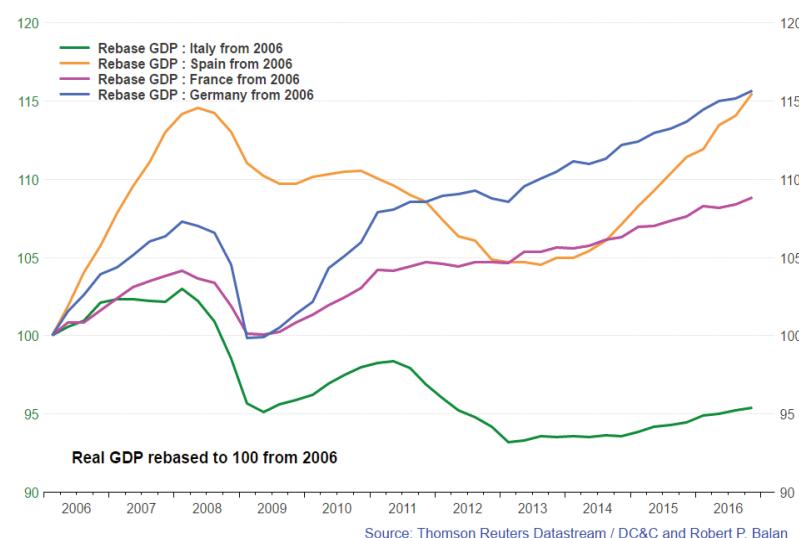
Situation with the candidates: Mr Fillon is representing conservative values, but he is embroiled in a scandal over allegations that his wife was paid for an allegedly fictitious job. This is clearly a political coup which was meant to affect the candidate and shift voters to Mr Macron and Mrs Le Pen. Mr Macron is a young candidate (39) with limited political experience who has never been elected before. He is pure product of the establishment (ENA education) backed by media and banking lobbies, a pure fabrication. He is a kind of French Tony Blair 20 years too late who thinks this election could be won with the 3rd way. Mrs Le Pen is a national front party candidate known for her clear anti-immigration and anti-Europe positions, opposed to free trade and autarky and seems to be gathering a significant part of the protest vote.

However, it is important to remember that while this presidential election is battled in 2 stages, the governing organisation of the country is fought out in 3 stages with the election of the national assembly coming a few weeks later on the 11th and 18th of June.

The markets have so far been focused on the all-important presidential election but the answer might come with the national assembly. The current political fragmentation and election system make it likely that moderate parties remain those with the majority. And if Mrs Le Pen were to be elected, her actions would be constrained as she would not have control of the assembly. This would also probably apply to Mr Macron. So, at worst at this stage, what might happen is that the electorate might rock the boat but will not sink the ship. Hence, a Le Pen victory would translate into sharp short term corrective moves for the French and global equities markets and particularly for the banking sector. Euro crosses would also suffer, particularly versus the yen and swiss franc. The OAT Bund spread would fly, along with Gold. We believe these sharp moves would be of short term nature and that past the initial shock, the global macro forces of reflation and global growth acceleration might reassert themselves and provide support for global risk assets for the second part of 2017.

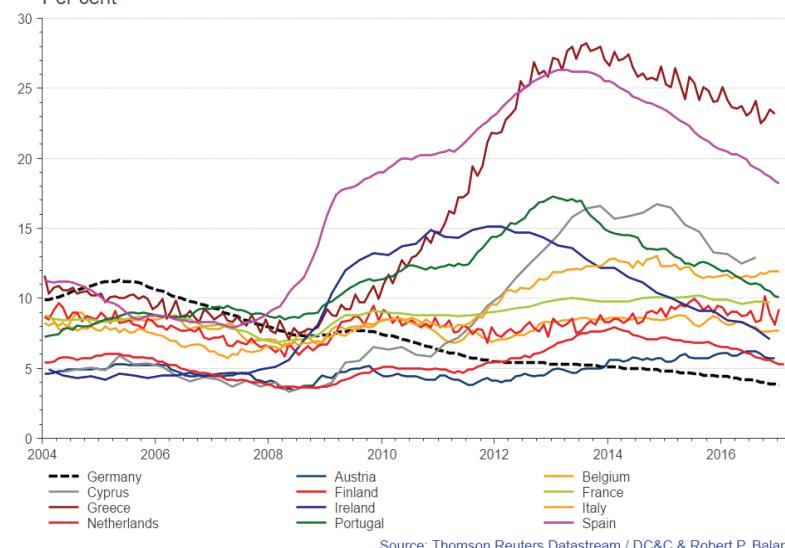
Germany vs France, Italy and Spain

Comparative GDP growth



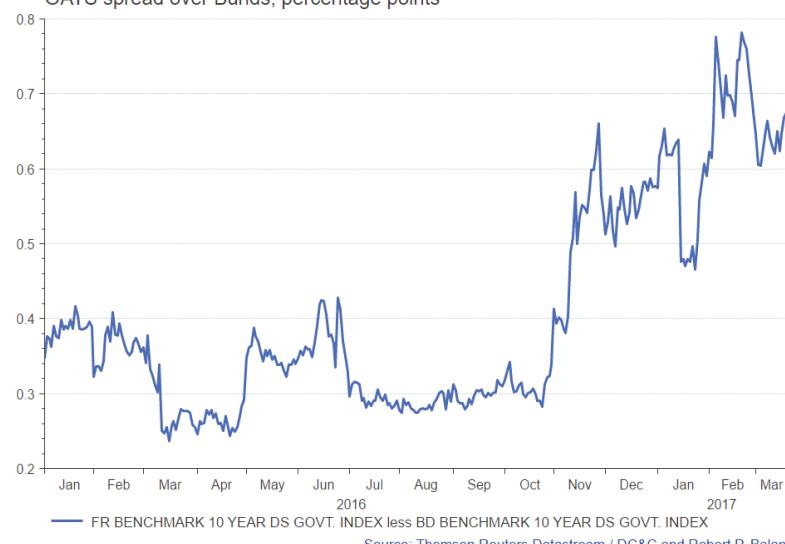
Eurozone unemployment rate

Per cent



Sovereign 10Y government bonds: France vs Germany

OATS spread over Bunds, percentage points

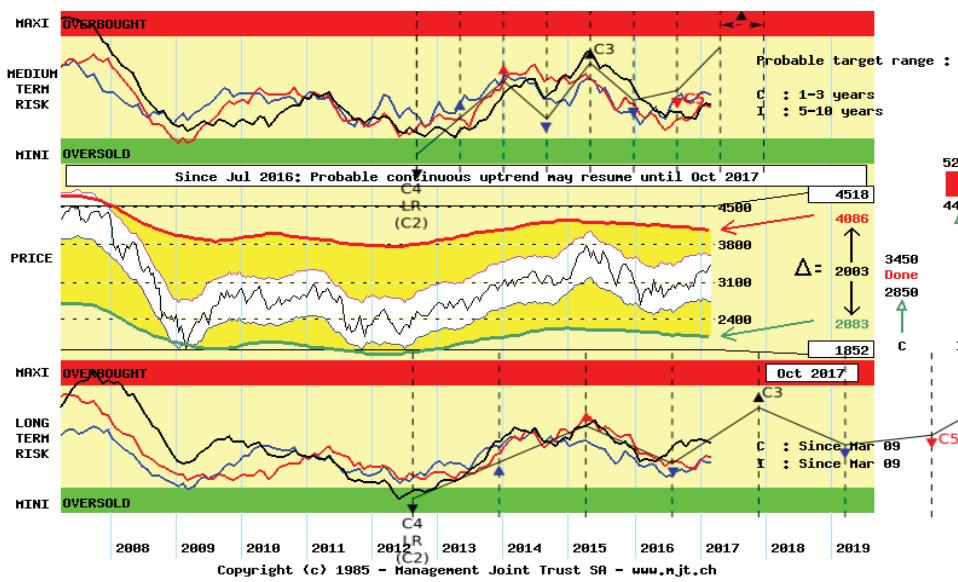


14 / TIMING AND TACTICAL INSIGHT

Europe equities still strong towards end 2017

Given all that political risk ahead (and behind us), the continued acceleration up of European equity markets is revealing.

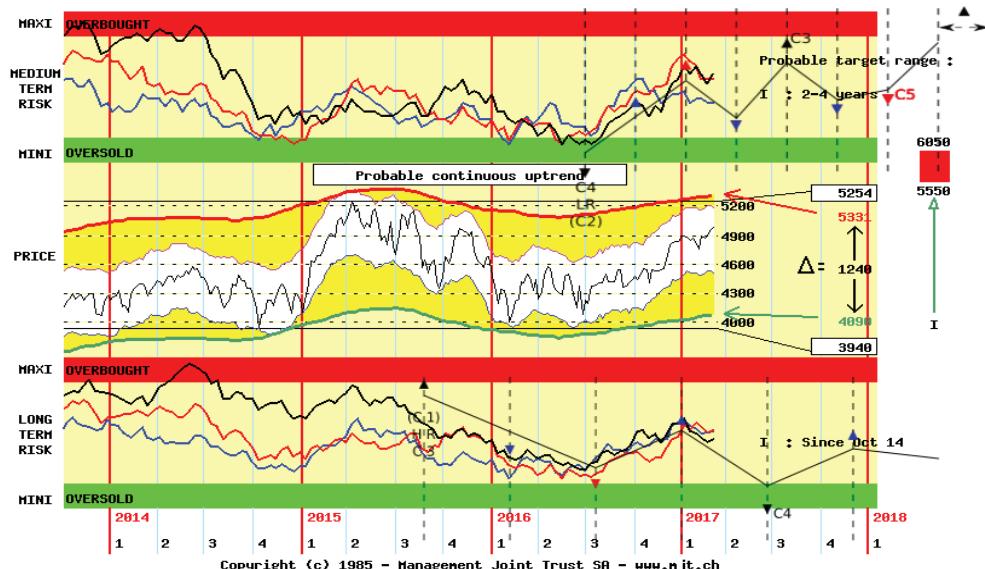
Dow Jones EURO STOXX 50 (SX5E) (Bi-monthly chart or the perspective over the next 1 to 2 years)



Both our oscillator series (lower and upper rectangles) are pointing towards a continuation of the current uptrend until late 2017. Prices have now reached the resistance of the upper end of our "C" corrective targets up (3'450; right-hand scale). Although we could expect some work around these levels, we believe that once they are taken out, SX5E could accelerate towards its "I" impulsive targets up somewhere between its 2007 (4'500) and 2000 (5'400) historical highs.

CAC40 Index (Weekly chart or the perspective over the next 2 to 4 quarters)

As with the Weekly graph of the Yield Curve or the one for US Banks vs the S&P500, both mentioned in a previous chapter of this document, we expect some mild consolidation on the CAC40 into mid/late Q2 2017, i.e. between end April (upper rectangle) and June (lower rectangle). Following that, the index should re-accelerate into year-end towards its "I" impulsive targets up between 5'550 and 6'000.



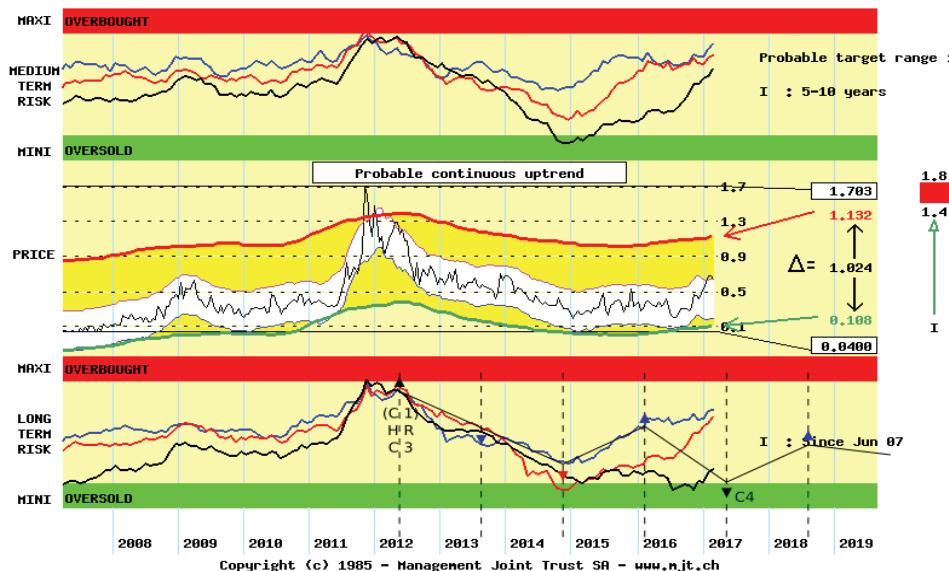
Concluding remarks:

European political risk is much more Bark than Bite for now. We believe that this situation should continue throughout the year. Hence, hedging for the French presidential race should probably be structured in an asymmetric way. Another alternative would be pick out trends, which may prove a protection or neutral if Mrs Le Pen gets elected, yet would also be positive longer term beyond May.

European Sovereign credit spreads

Possible alternatives to the OAT / Bund yield spread.

France 10 years Benchmark Bond Yield - Germany 10 years Benchmark Bond Yield (Bi-monthly chart or the perspective over the next 1 to 2 years)

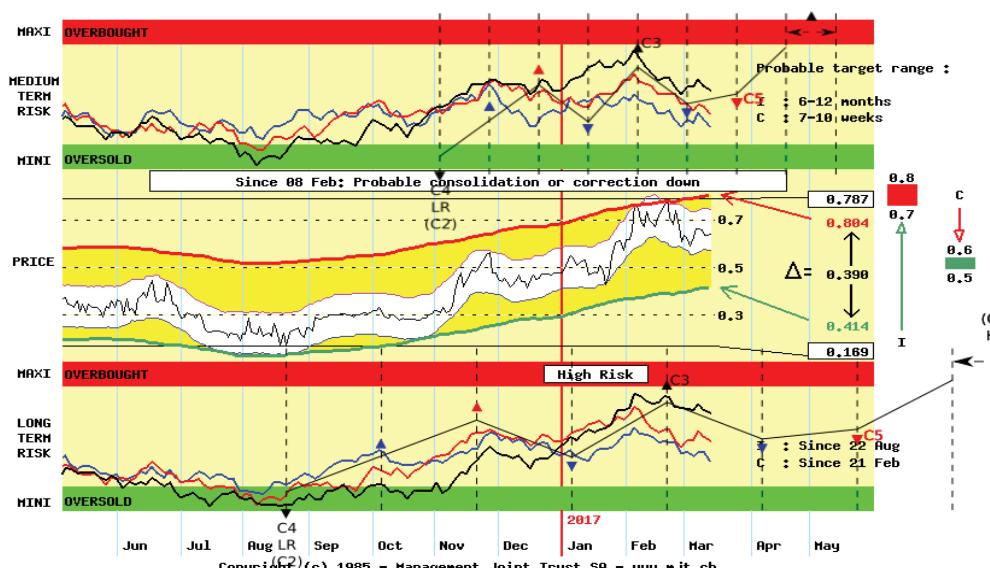


The OAT / Bund spread is currently the talk of the street. According to our long term oscillator sequence (lower rectangle), it was oversold from mid last year, yet may have turned a bit early (i.e. artificially) as the French presidential election appeared on the radar screen. If Mrs Le Pen does get elected, the "I" impulsive targets up are indeed considerable (right-hand scale), i.e. towards the highs made during the 2011 Euro crisis. Yet for now, probabilities still are that

a mainstream candidate wins the election. Hence, although a widening spread would be coherent with the reflation trend, the move in respect to our model seems to have gotten ahead of itself, which means it could retrace quickly following the election. We would consider any positioning in a pure asymmetric way.

France 10 years Benchmark Bond Yield - Germany 10 years Benchmark Bond Yield (Daily chart or the perspective over the next 2 to 3 months)

On our Daily chart, this FREXIT protection trade already feels quite crowded with a 65bps move from August to February. That said, given the slight correction since February, entering it now seems appropriate in terms of timing (as shown by the sequences on both our oscillators series; lower and upper rectangles). We would watch out though, as the outcome of the election will be binary in nature.



France 2 years Benchmark Bond Yield - Germany 2 years Benchmark Bond Yield

(Daily chart or the perspective over the next 2 to 3 months)

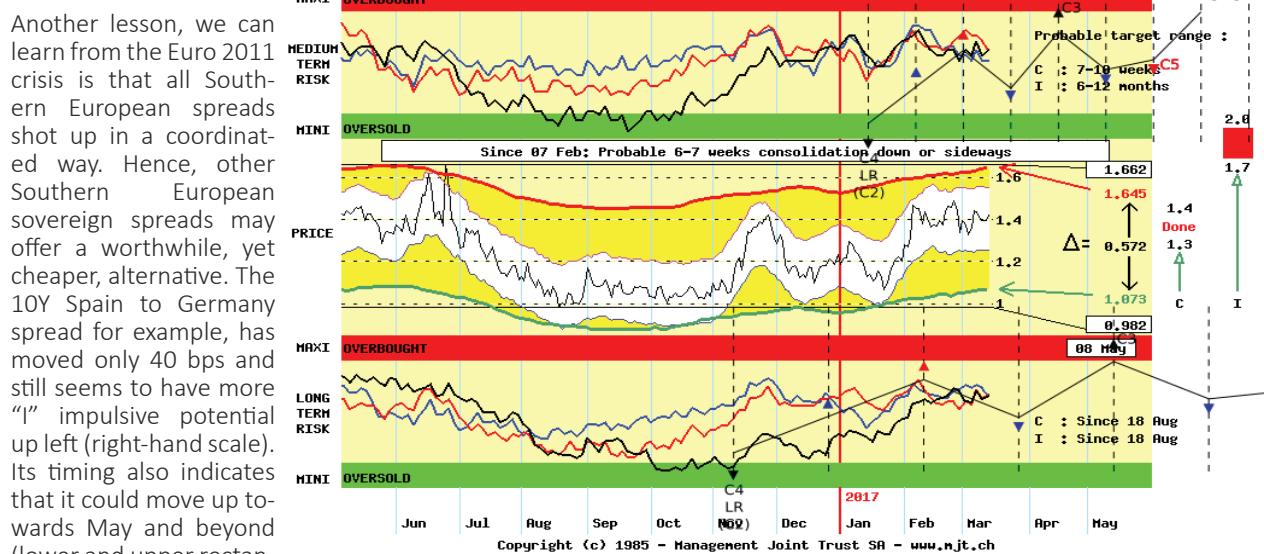


On the short end of the spread curve, the move up (+40 bps) has been less pronounced for now. Yet, during the 2011 Euro crisis, the short end of the curve actually overshot the long one: for example, the Spanish curve flattened substantially, while the Italian and Portuguese ones even inverted. The timing also looks appropriate to enter on both oscillator series (lower and upper rectangles) following the slight consolidation since late February. Hence, the short

end may provide a slightly cheaper alternative than the 10 year spread in terms of risk/reward. Please note, that in normal market conditions, we would consider this move to be exhausted in terms of targets (right-hand scale).

Spain 10 years Benchmark Bond Yield - Germany 10 years Benchmark Bond Yield

(Daily chart or the perspective over the next 2 to 3 months)

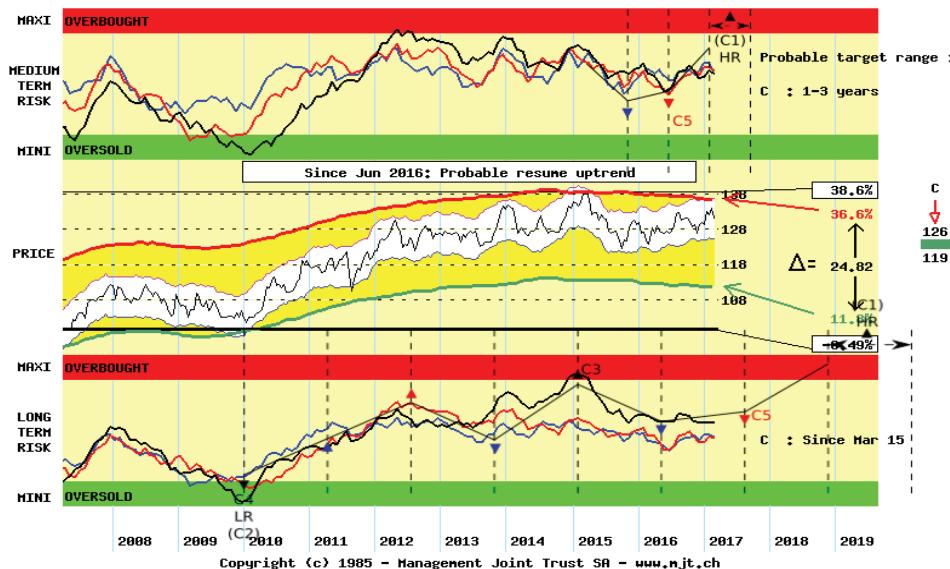


Another lesson, we can learn from the Euro 2011 crisis is that all Southern European spreads shot up in a coordinated way. Hence, other Southern European sovereign spreads may offer a worthwhile, yet cheaper, alternative. The 10Y Spain to Germany spread for example, has moved only 40 bps and still seems to have more "I" impulsive potential up left (right-hand scale). Its timing also indicates that it could move up towards May and beyond (lower and upper rectangles). Finally, this trade is also a natural reflation trade: as the situation in Europe improves, the bond buying program by the ECB is meant to be gradually phased out, which should lift rates in its main beneficiaries.

Equity - country arbitrage going into the selection

The trend is your friend.

EWG - iShares MSCI Germany Index Fund / EWQ - iShares MSCI France Index Fund (Bi-monthly chart or the perspective over the next 1 to 2 years)

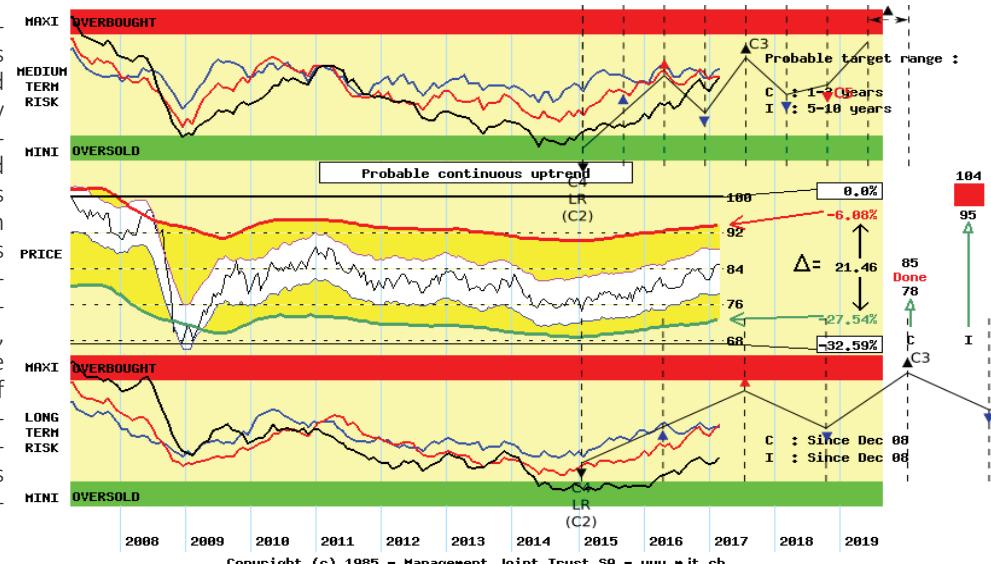


On the equity side, playing the German market vs the French one also seems natural. Yet, the long term trend on this index pair is quite advanced. Worse, both our oscillator series (lower and upper rectangle) are also anticipating a possible period of retracement into Autumn 2017, while our price targets (right-hand scale) are already signaling this correction ("C" targets down). This trend is hence extended (and weakening) and the election of a mainstream

candidate in France could provoke a rapid re-rating of French equities vs German ones.

EWN (Netherlands) equal weighted with EWO (Austria) ETFs vs EWQ - iShares MSCI France Index Fund (Bi-monthly chart or the perspective over the next 1 to 2 years)

Other Northern European markets such as The Netherlands and for example Austria may present a better alternative. They are indeed in accelerating uptrends vs the French market on both our oscillator series (lower and upper rectangle), whatever the election outcome. Although, we may also see some short term re-rating of French equities following the election, the relative potential up towards H2 2017 and beyond remains important.



Concluding remarks:

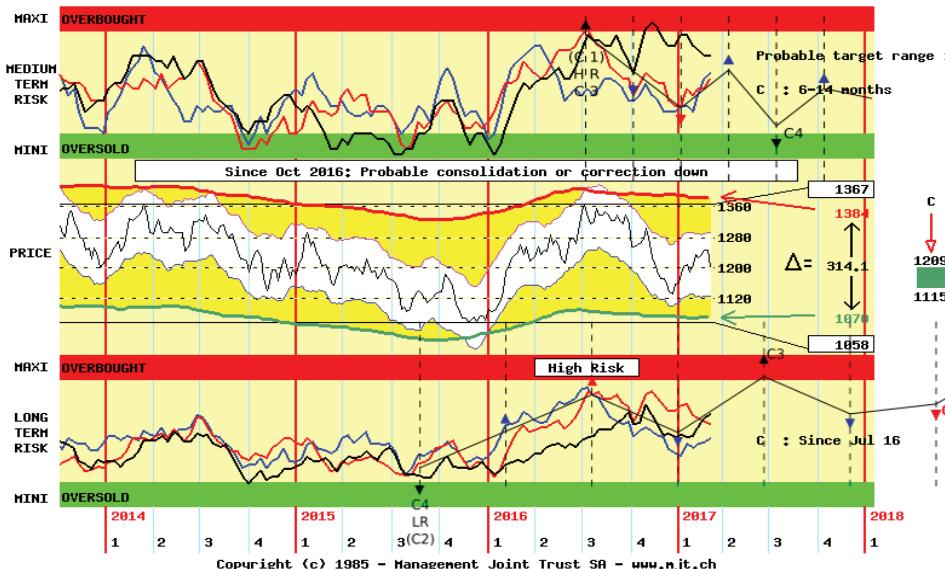
Look beyond the German vs French equities trade, as other Northern European countries may offer a better profile in terms of long term trend positioning.

Gold to hedge political risk

Political risk is only one of the drivers that would traditionally influence the price of Gold, along with inflation, interest rates, the US Dollar, systemic financial risk, seasonality and (de-)regulations.

Gold

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

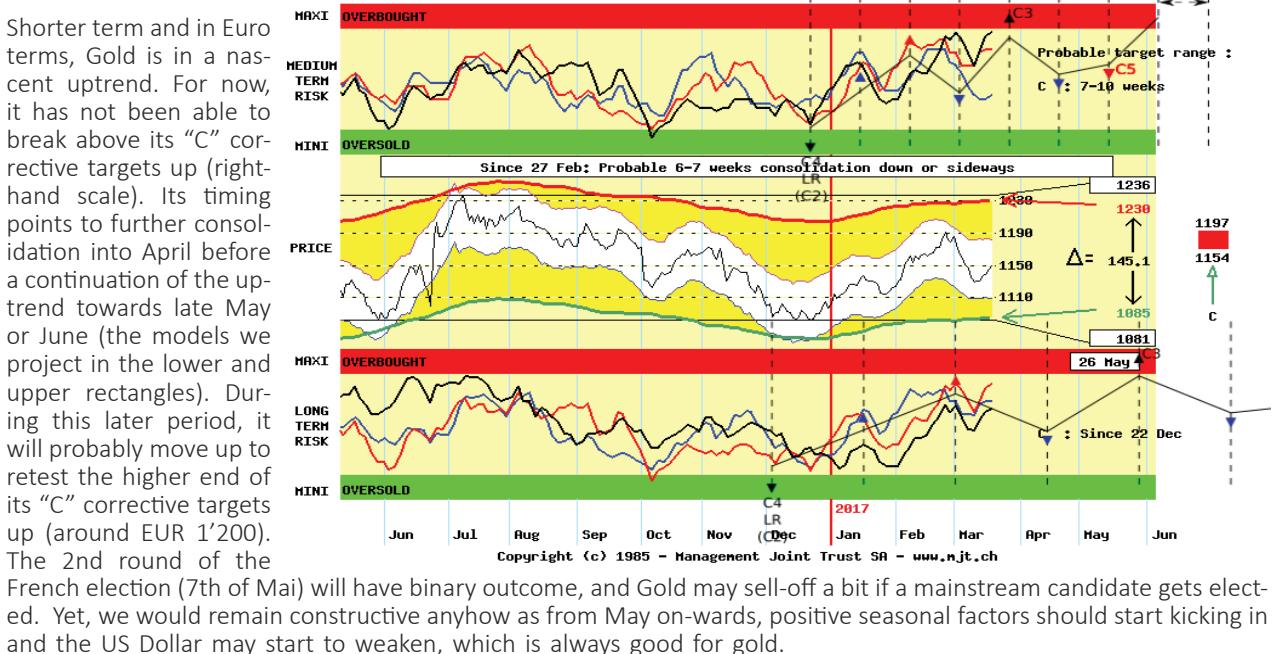


Our weekly chart of Gold is an interesting puzzle. On our medium term oscillators (upper rectangle), we can identify a downtrend sequence into mid year (which started with rising real interest rates from July to December 2016). The long term sequence (lower rectangle), however, would position the price fall we had during H2 2016 as a correction in the uptrend that started late 2015. We would point that this uptrend has now created an ascending base and could

be set to move higher. Given our general outlook, which is reflationary towards year-end, we would favor the later more positive alternative. The lower end of our corrective targets (at USD 1'115) provides a back-stop level for this scenario.

Gold in Euros

(Daily chart or the perspective over the next 2 to 3 months)



Concluding remarks:

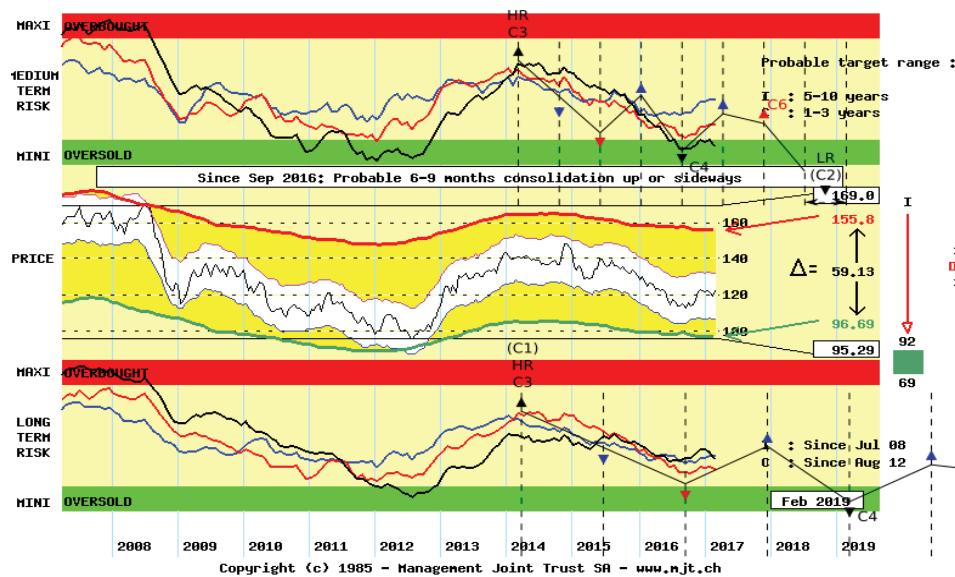
We are constructive, yet prudent on Gold, prior and following the French election. We would view levels around the lower USD 1'100s as backstops for this positive inclination.

EUR crosses are reversing up, Mrs Le Pen is counter-trend

Reflationary developments and the recent discussions around ECB tapering are helping the EUR initiate its reversal up vs most currencies.

EUR/JPY

(Bi-monthly chart or the perspective over the next 1 to 2 years)

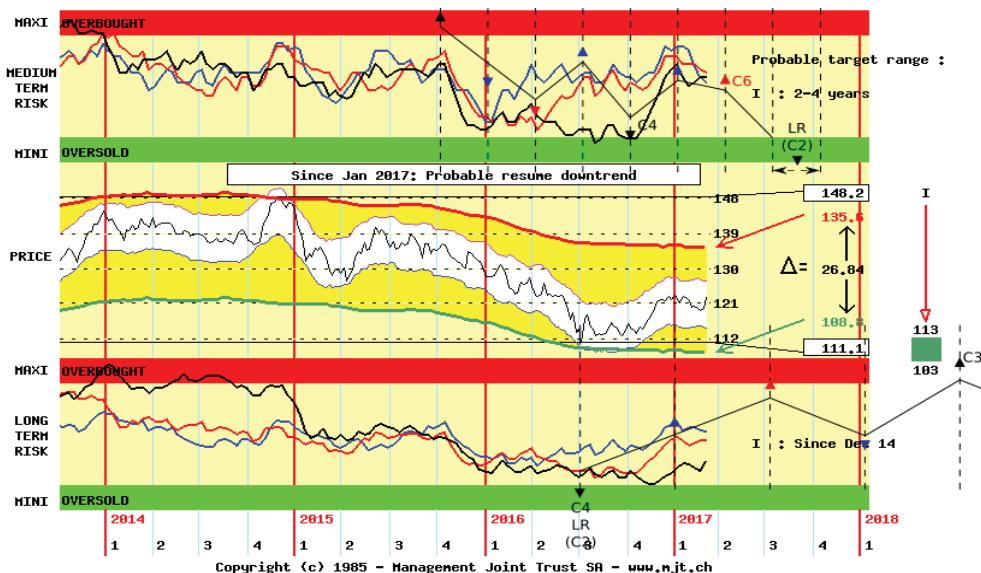


The graph is very similar to the US yield curve one we reviewed earlier up in this document. While both our oscillator series were positioned for a correction up from mid last year, the model on our medium term oscillators (upper rectangle) would see it reversing sooner than later. Given our general "Reflation II" scenario for H2 2017, we would rather favor a more lengthy correction up (lower rectangle) towards year-end and the upper end of our "C" corrective targets up (143; right-hand scale).

EUR/JPY

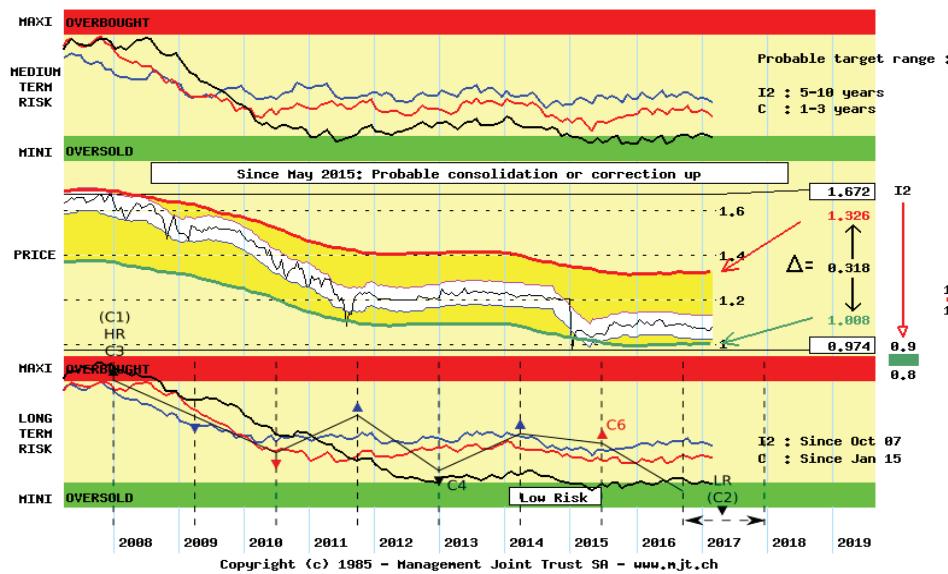
(Weekly chart or the perspective over the next 2 to 4 quarters)

Our envelopes (middle rectangle) are slowly reversing up, while prices have been quite resilient year to date. This is happening despite our medium term oscillators still signaling weakness into late Q2 2017 (upper rectangle). Although, we believe EUR/JPY could retrace some into Q2 2017, we would view this nascent uptrend as having the potential to move higher during H2 2017 and beyond (lower rectangle). The election of Mrs Le Pen and a sharp sell-off of EUR/JPY would constitute a counter-trend surprise (to be hedged for asymmetrically).



EUR/CHF

(Bi-monthly chart or the perspective over the next 1 to 2 years)

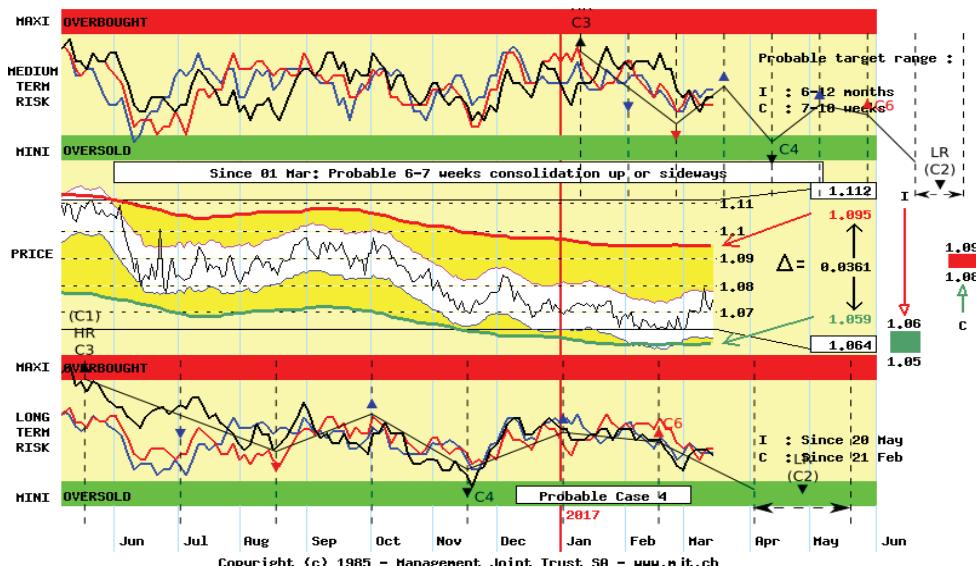


Since 2015 and the retrieval of the PEG, EUR/CHF has been forming a base. It is still in a Low Risk position on both our oscillator series (black oscillators Oversold; lower and upper rectangles). A victory of Mrs Le Pen could theoretically trigger a sell-off towards our "I2" impulsive targets down (0.9 - 0.8; right hand scale). Yet, we view this event as an asymmetric outcome and would favor a continuation of the correction up ("C" up corrective targets toward 1.13 - 1.23; right hand scale).

EUR/CHF

(Daily chart or the perspective over the next 2 to 3 months)

EUR/CHF has seen a slight tick up since early March following the last ECB press conference. This move will probably be retraced as EUR/CHF remains under pressure towards end April/May on both our oscillator series (lower and upper rectangle), i.e. in line with the French political agenda. Following that, we would expect EUR/CHF to start reversing up and test the resistance of the upper end of its corrective targets up ("C" Corrective targets up towards 1.09).



Concluding remarks:

EUR crosses are starting to reverse up on a long term basis, a trend that should be supported by our "Reflation II" scenario and early signs of tapering by the ECB. The election of Mrs Le Pen would constitute a counter-trend event and as such should be hedged asymmetrically. The sharp sell-off it could create in the EUR and its crosses would probably be short lived (i.e. again the Euro is already Oversold and has started its long term reversal process).

21/ Core CPI will decline soon, as credit creation slows and the housing market starts to peak

This month's CPI held some drama, not only because of last month's surprising spike, but also because the inflation data is coming during the same day (but earlier) that the FOMC will release their decision on policy rates. But it was clear that the data, whatever the outcome, was unlikely to change the decisions made by the FOMC committee, or even the tenor of the statement or post-meeting press conference.

The data set, after all, was less threatening than the January report, and so in that sense, was a much less-significant than last month's release. February Core CPI was at 0.21%, higher than consensus expectations of 0.15% , but significantly lower than last month's 0.31% m/m, which was far far above consensus. As for the headline CPI, it increased 2.74% in February 2017 over February 2016. That was the highest inflation rate registered in this format since February 2012.

As has been the case for the past three months, the acceleration of headline inflation can be attributed almost exclusively to the sharp

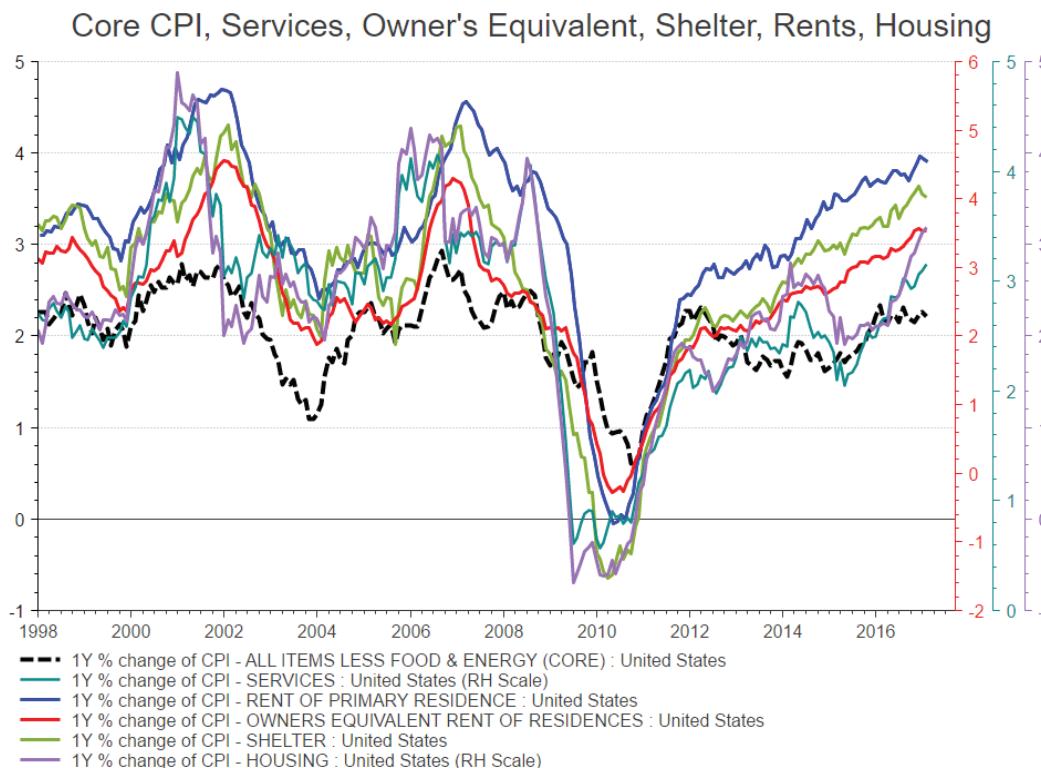
increase in oil prices as compared to the lowest levels last year (base effects). Underlining that, the energy price index was up 15.6% year-over-year, relative to an 11.1% increase in January.

The gamma of energy (simplistically, the rate of change of the monthly change) and therefore the CPI is already falling, after oil prices were stuck at 54-52\$ during January and February. If the WTI price meanders around 48\$, the inflation data provided by the current month (March) will be the last to incorporate any significant acceleration from oil. This is one indication that the inflation ogre is receding. The other stems from the behavior of Core CPI -- it was up 2.1% in February, the fifteenth straight month where the core increase was either 2.2%, 2.1.% or 2.3%. The last time the core rate (stripped of energy) accelerated even slightly was during the second half of 2015. The issue stemming from rising Core CPI originates from rising rent prices. The rent component of Core CPI rose 4.2% in February. Over the past eighteen months, this component has risen

sixteen times above 4.0%, and the remaining two months were just less than 4.0%.

This compares to the period leading to the peak of the housing bubble, when the rent component of Core CPI increased at a better than 4.0% for nineteen months going to early 2008. In the early 2000s, there were twenty-five 4.0% or better increases in this component.

Summary: despite the worrying uptrend in rental prices, the situation is nowhere near what we saw in this component going into the peak of the housing bubble -- a painful reminder of the current underlying weakness in the real economy. As the housing market starts to peak, as mortgage rates continue to rise, the rent component of Core CPI will start to fade. But situation is exacerbated by the fact that recent price increases have been entirely in goods that consumers cannot go without -- gasoline and rent. Slow economic growth combined with the «bad» kind of inflation is not a recipe for a happier consumer.

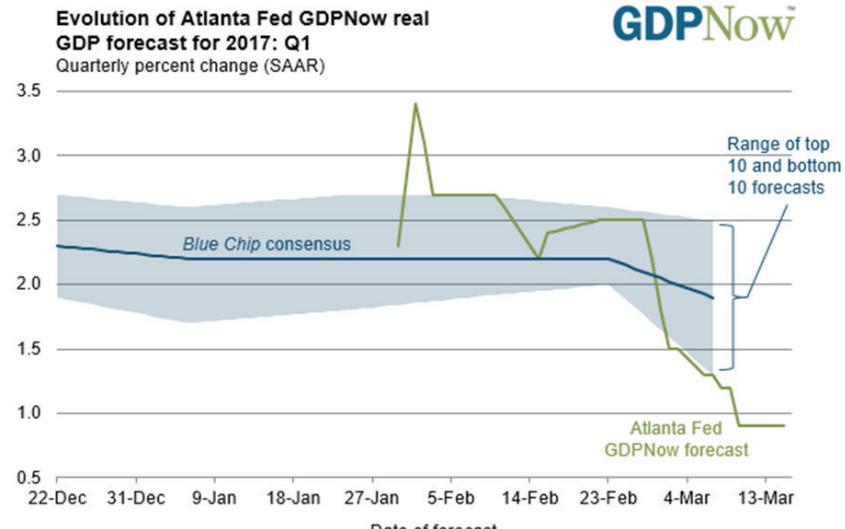


Source: Thomson Reuters Datastream / Copyright: Robert P. Balan Models (c)

The tame outlook in inflation, at least in the near-term, poses some questions as to the alacrity of the Fed in raising rates this week. Going by their dual mandate, growth is not so hot, if we can believe the Atlanta Fed's Nowcast of 0.9% GDP growth for Q1 2017 (see first chart on the right). And with inflation not an imminent threat, the reasons for the Fed tightening policy in March has to originate from other sources than the remit given to them by Congress.

The mechanisms for inflation to continue rising are being undercut. Although money growth is still brisk, the outlook of lower bond yields post-FOMC meeting can only mean money velocity will fall. Changes in inflation responds to the changes in Money Velocity and GDP growth after a very long lag. Using this measure, Core CPI should start to roll over very soon, although inflationary pressures could push Core back higher into Q4 2017. But by and large, Core CPI should be lower in 2017 and into Q2 2018 (see the second chart on this page).

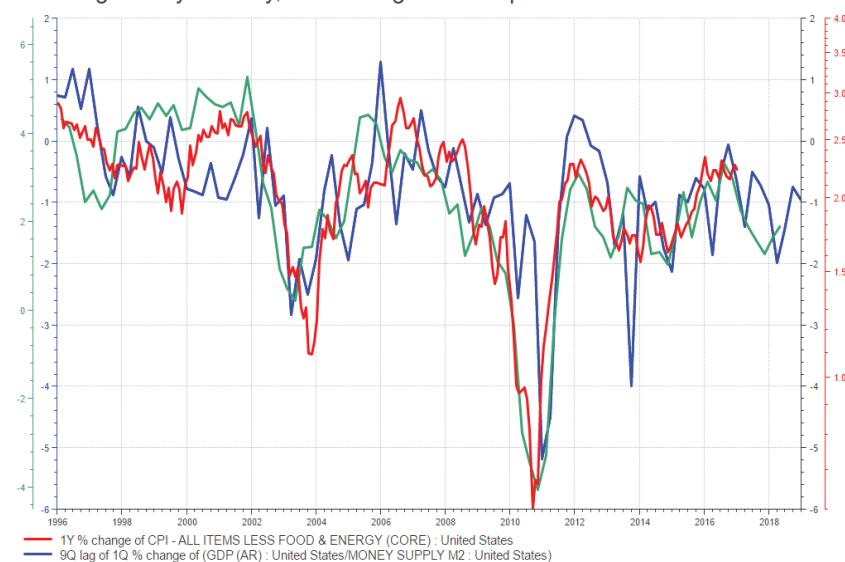
Moreover, with bank loans being curtailed at a fast clip, credit and money creation process will fall significantly over the near-term at least. That will seriously dent the uptrend of Core CPI in the near-term (see the third chart on this page).



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

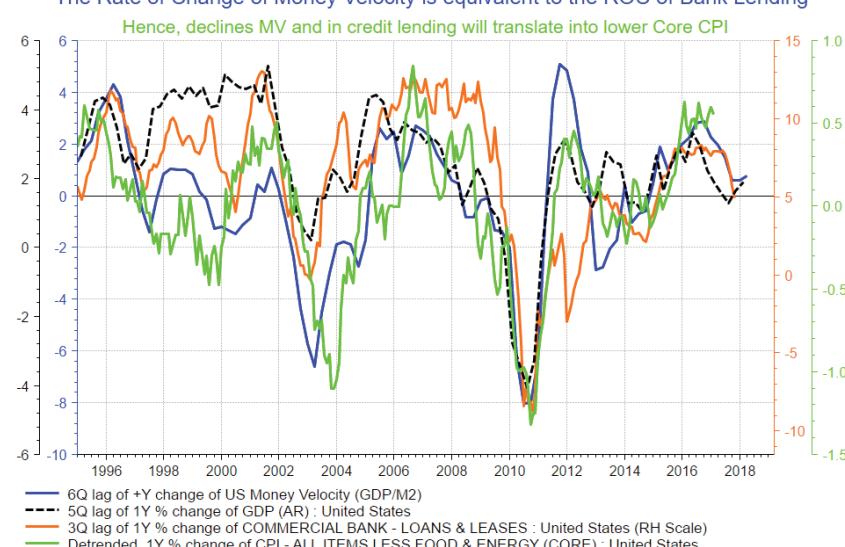
Note: The top (bottom) 10 forecast is an average of the highest (lowest) 10 forecasts in the Blue Chip survey.

Falling Money Velocity, soft GDP growth keeps Core CPI subdued in 2017



Source: Thomson Reuters Datastream / Copyright: Robert P. Balan Models (c)

Velocity of Money vs Bank Loans and Liabilities vs GDP vs Core CPI The Rate of Change of Money Velocity is equivalent to the ROC of Bank Lending



Source: Thomson Reuters Datastream / Copyright: Robert P. Balan Models (c)

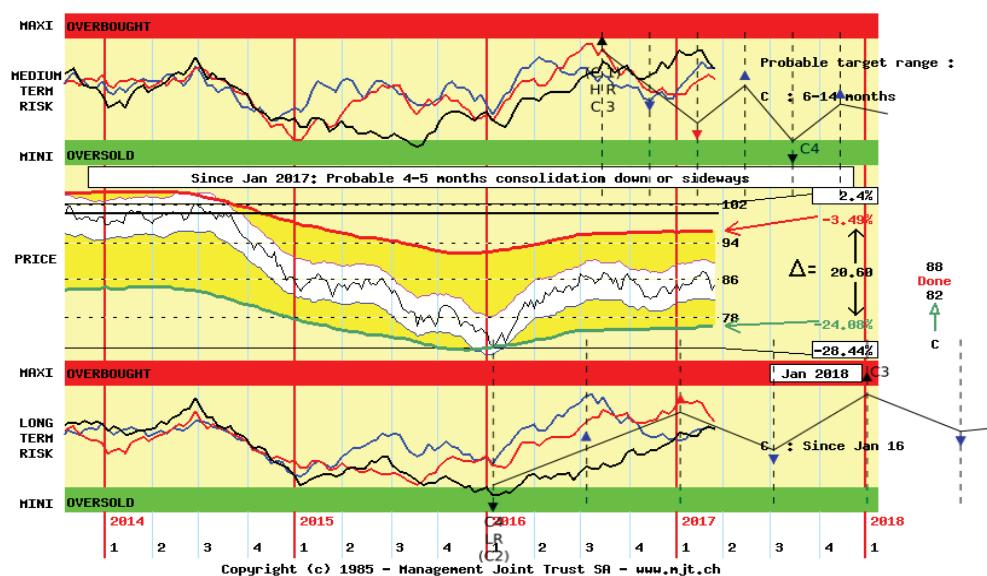
23 / TIMING AND TACTICAL INSIGHT

Inflation sensitive assets could bounce in April

Inflation sensitive portfolio

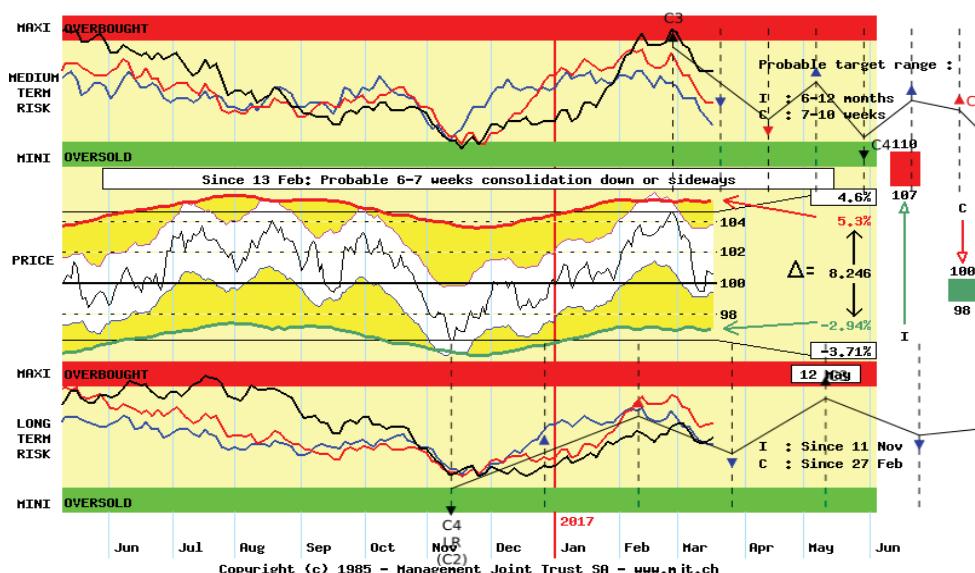
(Weekly chart or the perspective over the next 2 to 4 quarters)

This inflation sensitive portfolio is meant to protect investors against inflation. It is equal weighted between Gold, Tips, REITs, Lumber, High Yield Bonds and Oil. On our medium term oscillators (upper rectangle), it could hold up into mid Q2 2017 before correcting down towards July/August. Following that, both our oscillators series (lower and upper rectangle) suggests that the portfolio should resume its uptrend towards end 2017 or early 2018.



Inflation sensitive portfolio

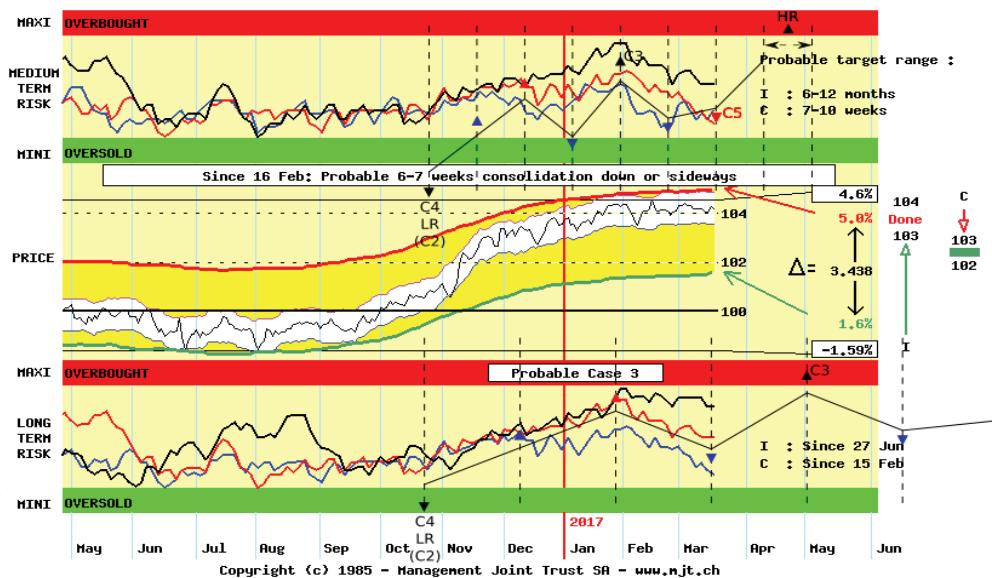
(Daily chart or the perspective over the next 2 to 3 months)



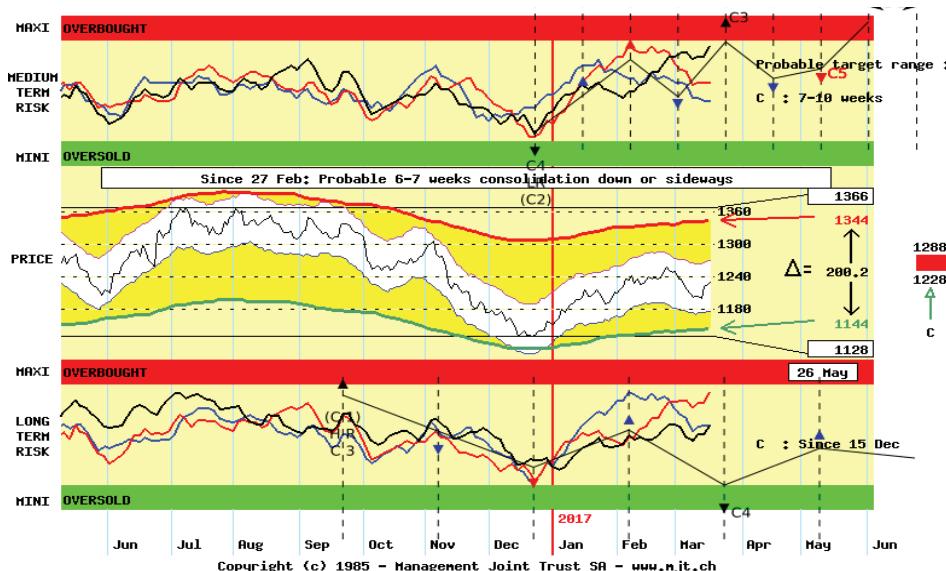
Whatever the scenario, a resume uptrend situation from end March (lower rectangle) or the beginning of a down-trend from the recent tops made end February (upper rectangle), inflation sensitive assets could bounce from end March / early April into early May. Following that, in May, they should start correcting downwards into June, possibly July.

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

Inflation protection appetite represented here by the ratio of TIPs vs Treasuries of similar duration is at the top of our Daily range with limited potential left ("I" impulsive targets "done"; right-hand scale). Interestingly, the ratio has seen little impact from the recent drop in oil prices. The models we project on both our oscillator series (lower and upper rectangles) suggest that the ratio may hold/extend at high levels until late April / early May before starting to reverse down.



Gold (Daily chart or the perspective over the next 2 to 3 months)

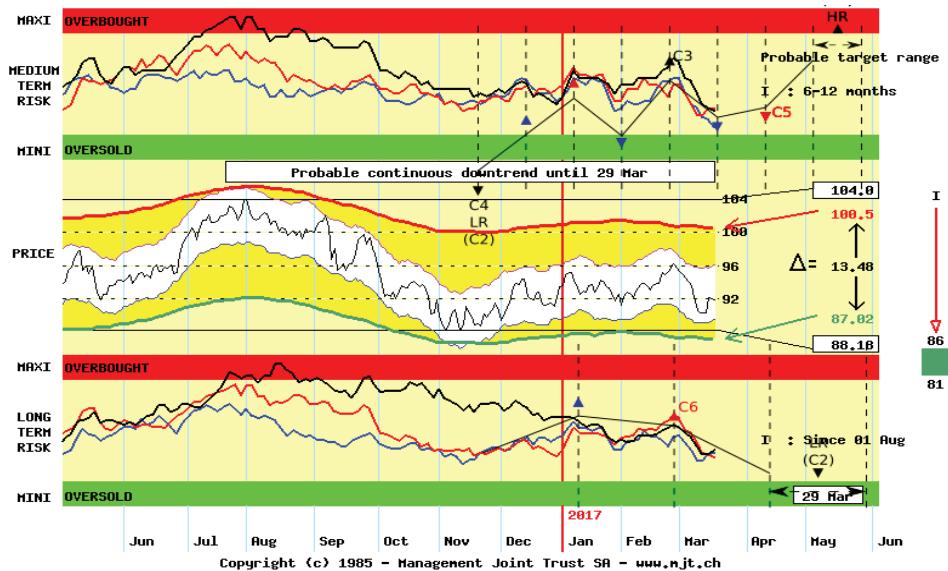


Gold is making a base with higher lows towards end March as presented on our long term oscillator series (lower rectangle). This base should support Gold prices during April even if the medium term oscillators (upper rectangle) should correct down into mid April. In general, the dynamics of Gold are more defensive than other inflation sensitive assets. It may hence be a late starter in April, yet could continue up while other inflation sensitive assets correct down during

May (upper rectangle). Possible price targets are in the high 1'200s at least ("C" corrective targets up; right-hand scale). Above that, the next target range points to above 1'400 ("I" impulsive targets up; not shown yet).

RWR - SPDR DJ Wilshire REIT ETF

(Daily chart or the perspective over the next 2 to 3 months)

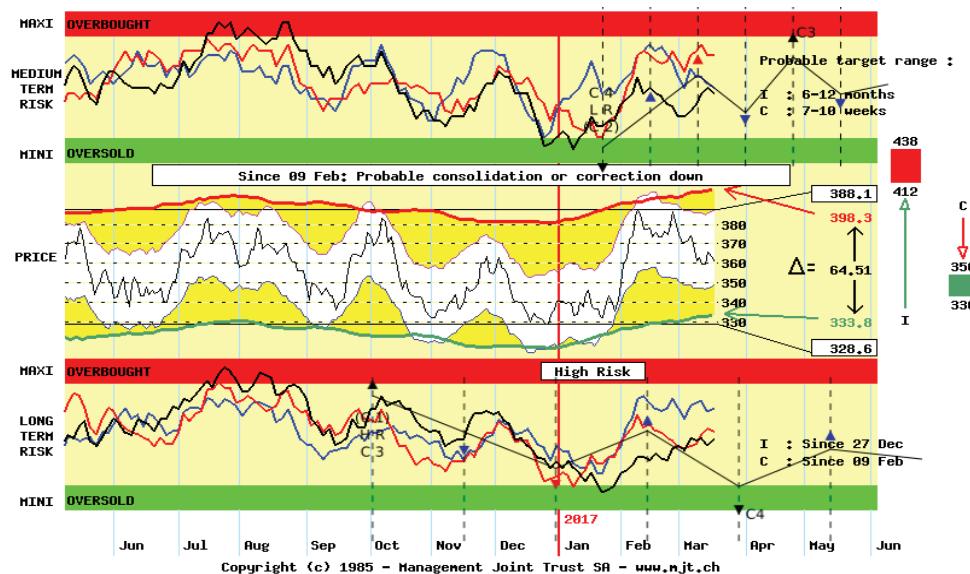


The correction up in REITs since November has been weaker than the ones on other inflation sensitive assets. We hence cannot exclude a continuation of the sell-off towards end April / May (model projection in our lower rectangle). Yet, as with other inflation sensitive assets, we would favor a more positive scenario (although it may prove quite subdued), where REITs find a base end March / early April and move higher towards May (our medium term oscillator series; upper rectangle).

Lumber Three Months (May)

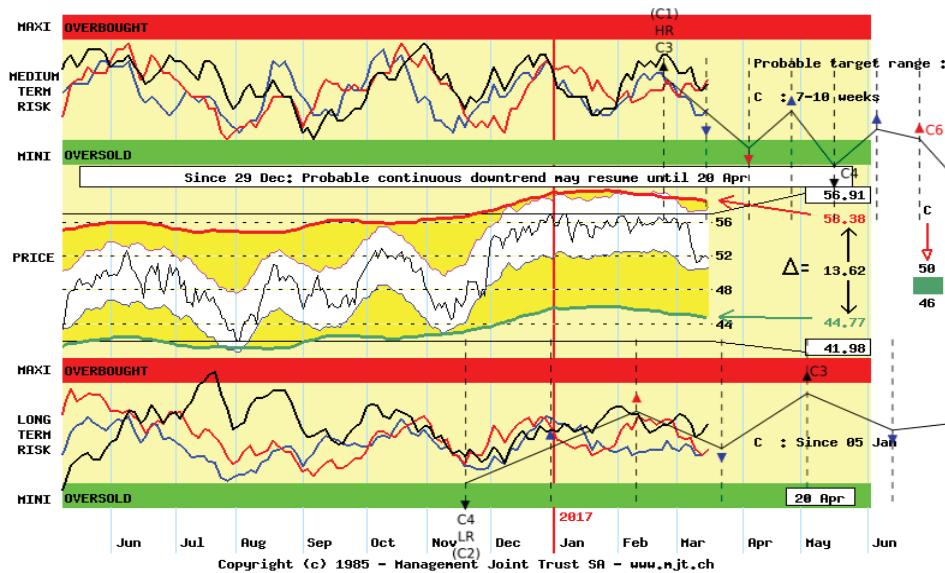
(Daily chart or the perspective over the next 2 to 3 months)

Lumber would confirm the more positive scenario on inflation sensitive assets. As with Gold, it is also forming a base at higher levels on our long term oscillator series (lower rectangle) and from end March should see a new move up materialize into end April (model on our medium term oscillator series; upper rectangle).



Brent Oil

(Daily chart or the perspective over the next 2 to 3 months)

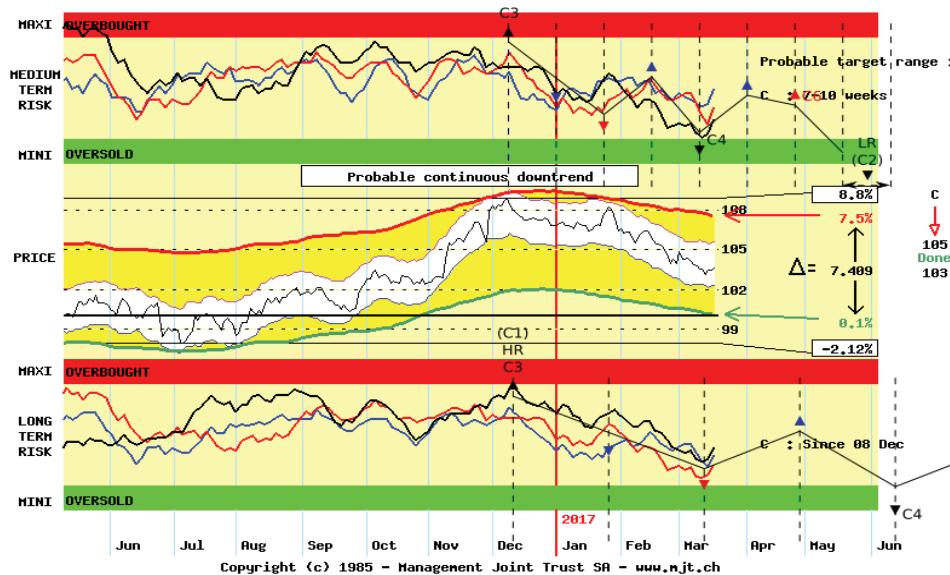


Our automatic messaging on Brent Oil is quite negative ("resume downtrend until 20 April"; middle rectangle). Yet, considering our projections on other inflation sensitive assets above, which should rise during April, we would favor a more positive outcome for now. Whatever the scenario, a resume uptrend situation from end March (lower rectangle), or the beginning of a downturn from the recent tops made end February (upper rectangle), Brent Oil could bounce from end March / early April

into late April / early May. Following that, we would expect it to correct back down into June, possibly July with targets down below USD 50 per barrel (right-hand scale).

Mid cycle sectors vs Defensive sectors

(Daily chart or the perspective over the next 2 to 3 months)



We find a further confirmation of this April bounce by comparing an equal weighted portfolio of the Mid Cycle sectors (Industrials, Materials, Energy) vs Defensive ones which had been quite strong since December (Staples, Healthcare, Utilities). The bounce could start now into early April on our medium term oscillators (upper rectangle) and possibly extend to end April on our longer term oscillators (lower rectangle). May and June should then see further weakness.

Concluding remarks:

Provided they can hold current levels, inflation sensitive assets could bounce in April before they correct down again towards May/June and possibly July. H2 2017 should see some of them re-accelerate (see the projections on our Weekly graphs for Oil on pGW 10 and Gold on page 18 further up in the document).

27/ Equity prices and bond yields moving contra to each other: look for liquidity factors to explain the moves

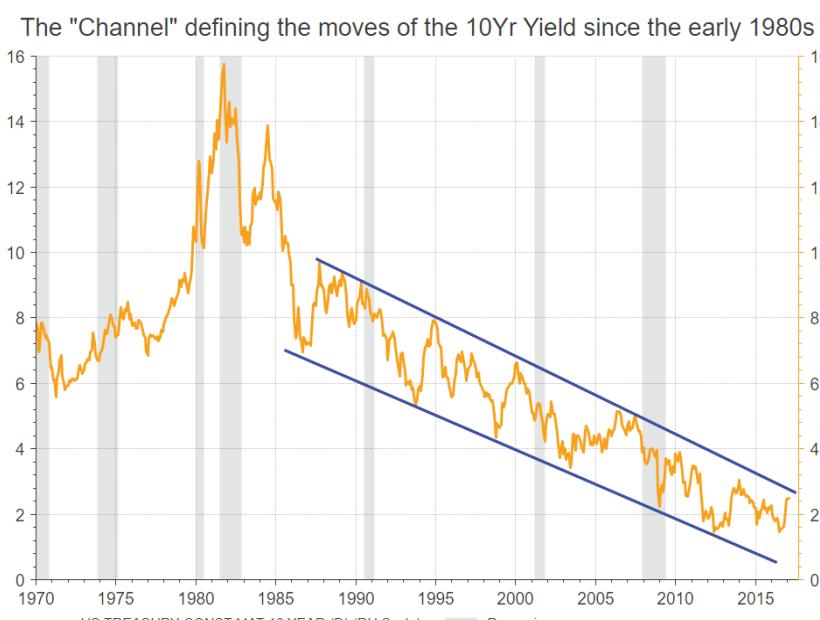
The yield on the 10 year Treasury bond has gone above 2.60 percent this week (prior to the FOMC meeting) -- a level «Bond King» Bill Gross considers to be a «tipping point» for future interest rate levels. He believed that if 10yr yields breached those levels, it means that the bond bull market has basically ended. In fairness to Mr. Gross, prior to the Wednesday's FOMC meeting, it was an almost universal meme that long rates are going to rise, along with the policy (Fed Funds) rate. Mr. Gross has argued that the yield on the 10 year Treasury, once it broke the 2.60 percent channel barrier would soon jump to a much higher range. He was not alone – many others have also claimed that the era of low, longer-term interest rates connected with the Great Moderation is over. These sentiments are of course tied to the imminent rise in short term rates, after the Fed provided virtually explicit notice that policy will be tightened during the March FOMC meeting.

The equity market was not saved from speculations that rising rates will «destroy» valuation. The Nobel Prize of Economics winner Robert Shiller was also talking about the US stock market being overvalued, and the timing was suspiciously tied to the expected outcome of the FOMC meeting. Mr. Shiller

was pointing out that his measure of stock market performance, the Cyclically Adjusted Price Earnings index or CAPE, is at about the same level it was before the stock market collapse of 1929, as well as rising close to the levels reached in 2000 after which the stock market corrected. The CAPE measure is said to provide an important measure of the quantitative valuation of current stock market prices, but no one can tell exactly what that might set off a correction, if at all. The almost-universal thinking was that the Fed tighter policy regime will push interest rates higher, probably beyond 3.0%, and that would cause equity prices to crash. Some analysts refined that argument, saying that if the increase in the yield beyond this level is due to a significant rise in actual or inflation expectations, this could influence the reaction function of Federal Reserve members and result in policy rate increases as actual inflation moved above Fed targets. Those speculations have not even come close in describing the performance of risk assets, post the FOMC meeting.

To summarize, pre-FOMC market expectations was for sharply higher rates and correspondingly lower equity markets. That is not what happened immediately after the decision was released publicly:

longerterm rates fell sharply, and the stock market rose. And the market considered the correlated move an artefact of the Fed's statement, or for some, a conundrum. Is it? The situation is better understood as a liquidity issue. The Fed's objective of having two more policy hikes in 2017 implied that systemic liquidity will remain accommodative. Note that the Fed's previous definition of «gradual» tightening has been four tightening episodes in one year, so four hikes in 2017 could still be gradual in Ms. Yellen's view. More so, Chair Janet Yellen said the Fed will continue to reinvest from maturing Treasuries and agency RMBS. This will keep the liquidity issue at the forefront. Why is this especially significant at this time? Models of liquidity flows have had success in tracking the movements of asset prices. Significantly, the models have tracked the gyrations in the stock and bond markets, pre-Brexit, before and after Mr. Donald Trump's election as president of the US, and have mirrored the markets' indecision during the days that lead to the crystallization of the Fed's decision to tighten policy this week. More importantly, the models have successfully tracked the denouement of this week's FOMC meeting (see the first two charts on the next page). Usually there is a very high degree of seasonality, and thereby predictability, in the amount or scale of liquidity entering the US financial system, and the most significant ones are those originating from the Federal Reserve and the US Treasury. But since September last year, a massive amount of liquidity was infused into the system by the Treasury, for what seemed to be an effort to prime the markets ahead of the US presidential election (see last chart on next page). It did make a lot of difference as the equity market took off immediately before and after the election. Mr. Trump's win was used as an excuse for the "Trumplation" trades, but a rational analysis will show that the market rally owes its zing to the massive infusion of liquidity which was designed and intended

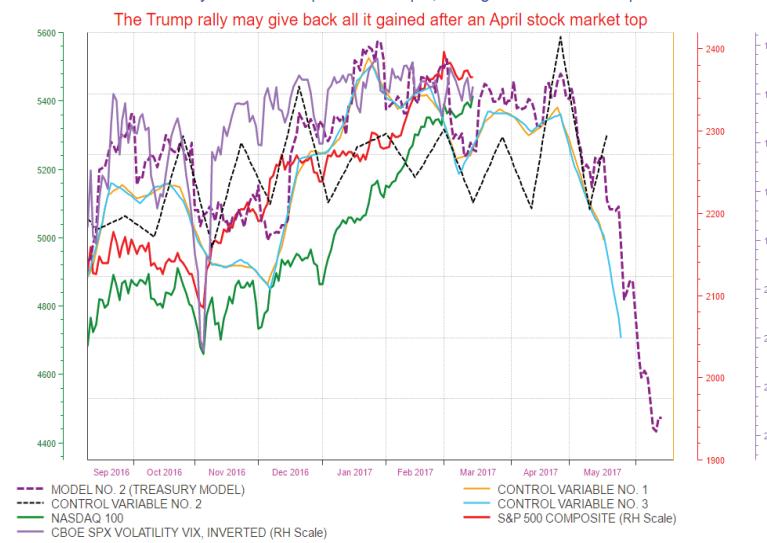


to help elect his rival, Mrs. Hilary Clinton. The election is now history, and so the US Treasury has embarked in an effort to offset all the liquidity that was meant to influence the election. The Treasury is leaving mere crumbs on the table after the mop up, and this will hurt the equity markets correspondingly after a short lag (see the red line on the third chart on the right). How will this impending disaster come about? The Treasury did not merely neutralize the liquidity surfeit during the election, but went overboard by using the withdrawn cash to pay for maturing bills and notes, instead of borrowing in the market as has been the standard procedure until now. An example was last year, during the same 47 day period which covered the withdrawal process, the Treasury funded mainly the operating deficit of 253\$ billion by new borrowings of 157\$ billion, which covered 62% of the shortfall. Its cash balance was 223\$ billion on 7 March 2016, which compares with the cash balance of just 66\$ billion last week, and targets 23\$ billion – mere crumbs relative to the normal spending schedule of the Treasury. In fairness, the Treasury has had to cut its cash balance to 23\$bn from 400\$bn over the past three months, since it is not allowed to hold a buffer going into the debt ceiling's reinstatement. Ironically, by using its own cash to fund the operating deficit, the Treasury allowed the Fed dealers to keep the amount (which would be used to buy new debt issuance, otherwise), and will undoubtedly be plowed-back into the markets and should help support a rally to an April top. It is money that is going the equity market's way instead of going into the bond market.

But the sting is in the kicker – as cash holdings disappear, the Treasury has to resort to its emergency operating procedure: it has to borrow from trust funds so it can pay for maintenance. When the new budget of the Trump administration is approved, the Treasury will have to sell debt to pay the funds borrowed and to acquire funds to pay for government expenditures – to the tune of a ballpark number of circa 500\$ billion. And it will be done in a matter of days. Government bond dealers will be hard-pressed to acquire wherewithal to finance the new paper issued by the Treasury. It is easy to imagine that equities and lower-grade assets will be sold by the bond dealers to accommodate the Treasury. We expect those dynamics to cause a sharp sell-off in the equity markets and a sharp decline in bond yields in late April. A large number of government bond dealers chasing paper offered by the Treasury at the same, in large quantities, should push up bond prices and depress bond yields sharply accordingly.

Liquidity Models and Flows vs S&P 500 Comp Index, Nasdaq 100, VIX

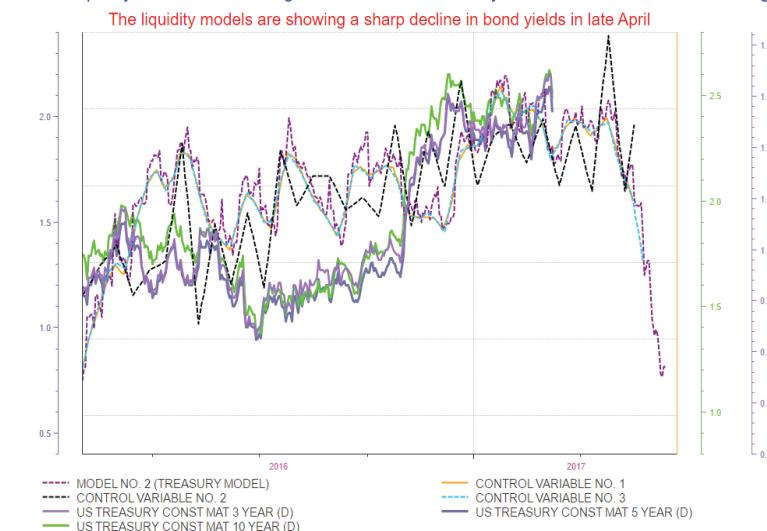
A bottom in mid-March may still hit a new peak in late April, but significant declines expected thereafter



Source: Thomson Reuters Datastream/ Robert P. Balan's Models (c)

Liquidity Models and Flows vs Bond Yield (10Y, 5Y, 3Y, 3M)

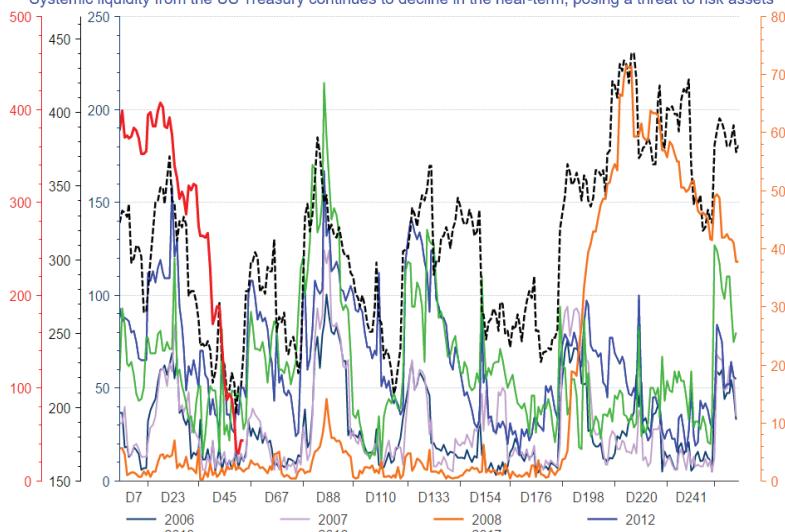
The bond liquidity models are tracking the movements of bond yields well after the FOMC meeting



Source: Thomson Reuters Datastream/ Robert P. Balan's Models (c)

SEASONALITY OF MODEL NO. 2 (Jan to Dec, year by year)

Systemic liquidity from the US Treasury continues to decline in the near-term, posing a threat to risk assets



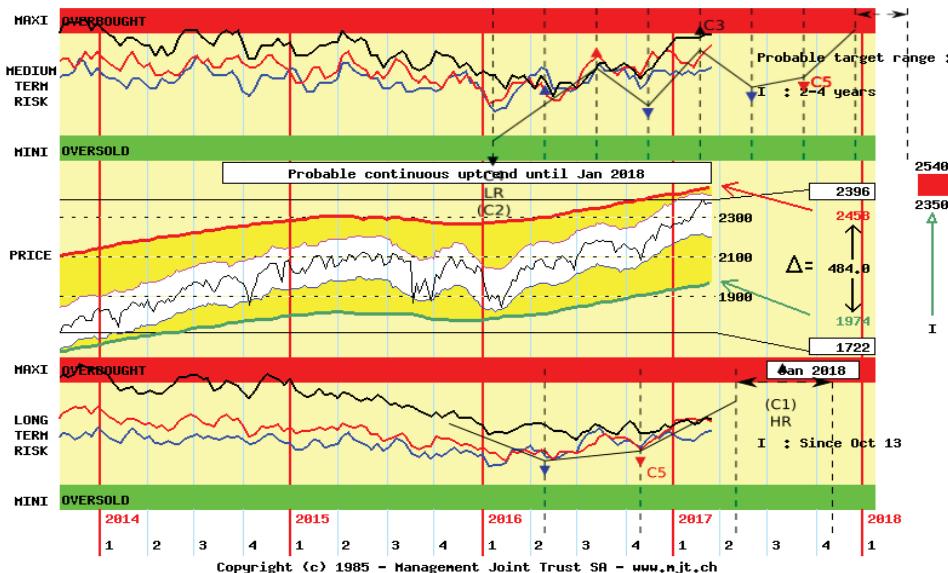
Source: Thomson Reuters Datastream / Robert P. Balan Models (c)

29 / TIMING AND TACTICAL INSIGHT

Equities and Bond yields could extend at high levels, for how long?

S&P500 Index

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



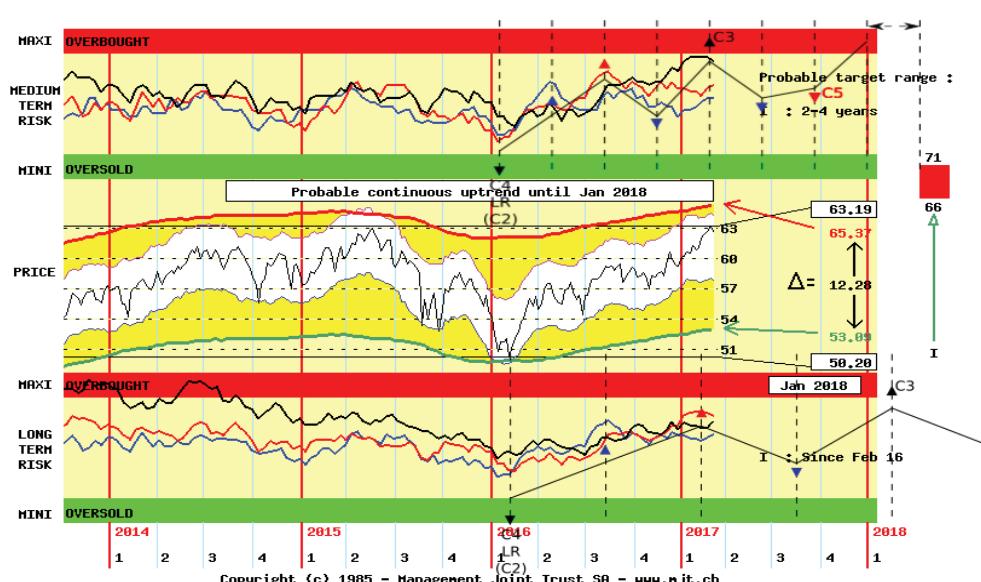
On our medium term oscillator series (upper rectangle), the S&P500 just made a Case 3 intermediate top, which should cap its potential over the next few months. On our long term oscillators (lower rectangle), however, the effect of the Case 5 (rapid acceleration up) made in Q4 2016 are still being felt. Give these contradictory signals, we would maintain our mild consolidation scenario into late Q2 2017 before prices continue their uptrend in H2 2017. "I" impulsive

price potential up towards January 2018 is less than 10% (right-hand scale), i.e. the US market is probably quite expensive already.

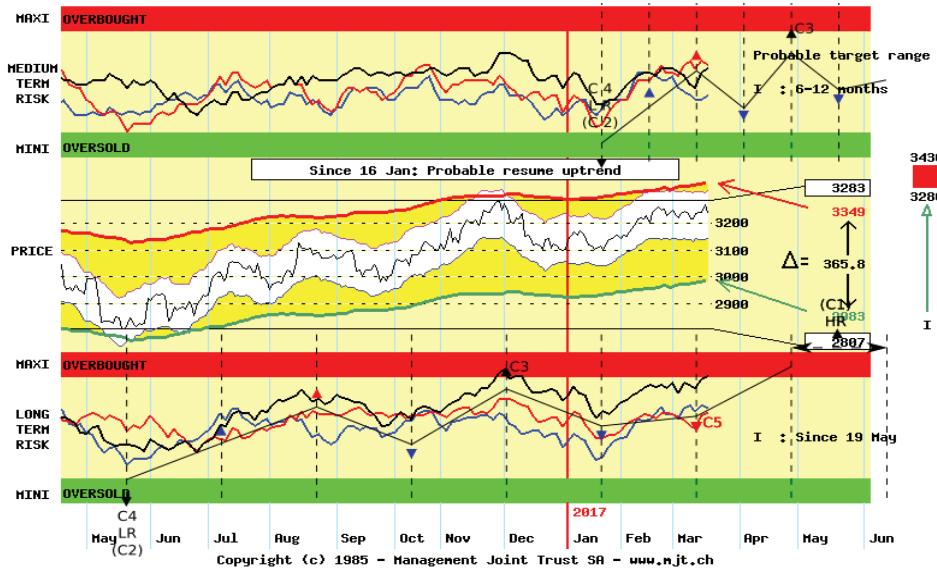
ACWI - iShares MSCI ACWI Index Fund

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

The world index (in USD terms) has also reached an intermediate top. It is clearly visible on both oscillator series (lower and upper rectangles). It should cap the potential up over the next few months (into late Q2 2017). From mid 2017, we expect it to resume its uptrend towards early 2018. "I" impulsive price potential up indicate that world equity market could move up by 10% to 15% towards January 2018, i.e. in USD terms, we see more potential up abroad than in the the US for H2 2017.

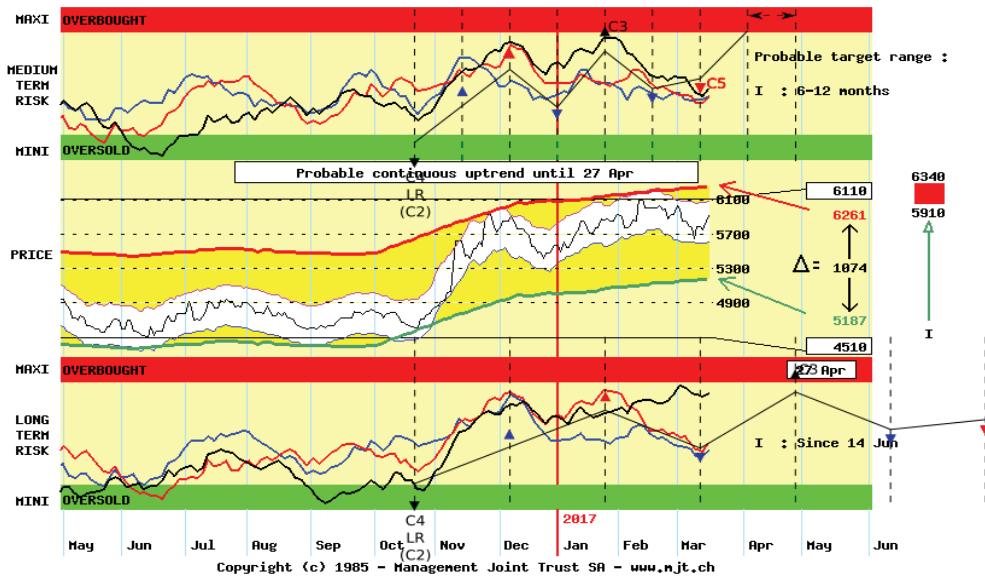


Shanghai Composite Index (Daily chart or the perspective over the next 2 to 3 months)

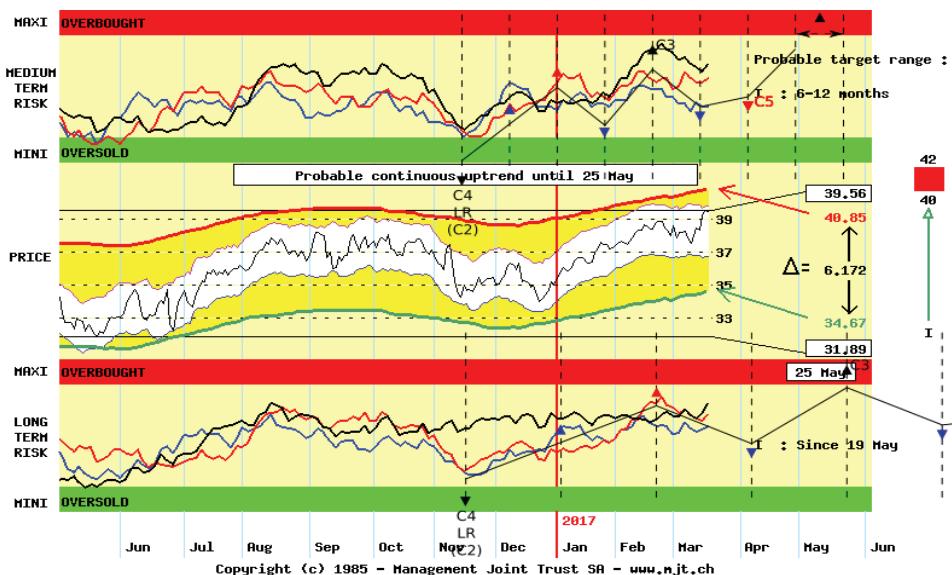


Copper Spot (London Metal Exch.) (Daily chart or the perspective over the next 2 to 3 months)

Copper confirms this extension. It has been consolidating down since February (from late January on both our oscillator series; lower and upper rectangles) and could now be getting ready to resume its uptrend into late April (as per our model projections). "I" impulsive price potential up indicates that it could make new highs above 6'300 USD/t (right-hand scale).



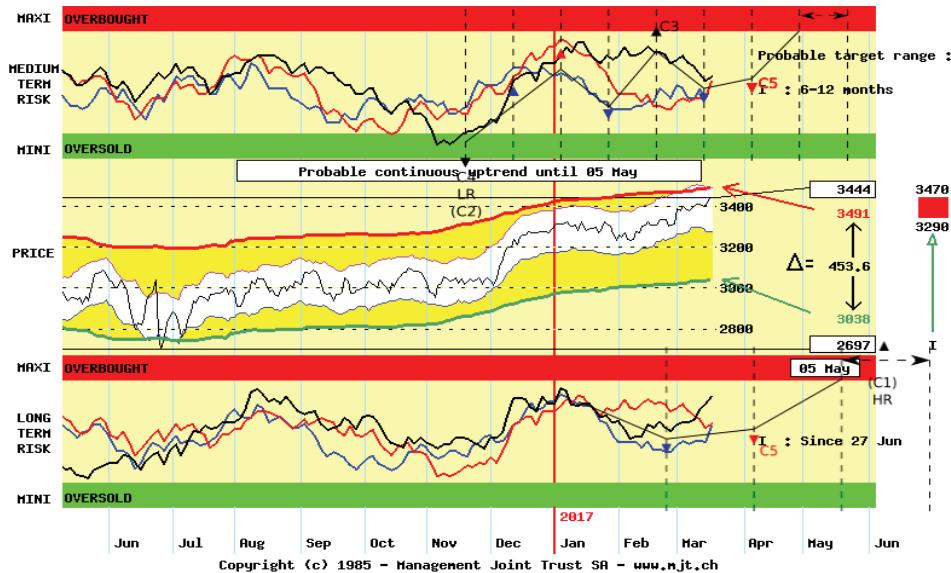
EEM - iShares MSCI Emerging Index Fund (Daily chart or the perspective over the next 2 to 3 months)



Emerging markets seem to extend even further (towards late April and possibly end May). Given both oscillator series (lower and upper rectangles), we would ideally consider them from early April, as they may have gotten ahead of themselves short term. The "I" impulsive price target potential up points to a 5% performance over the next couple of months. It is interesting to note that emerging markets often thrive when the Dollar weakens.

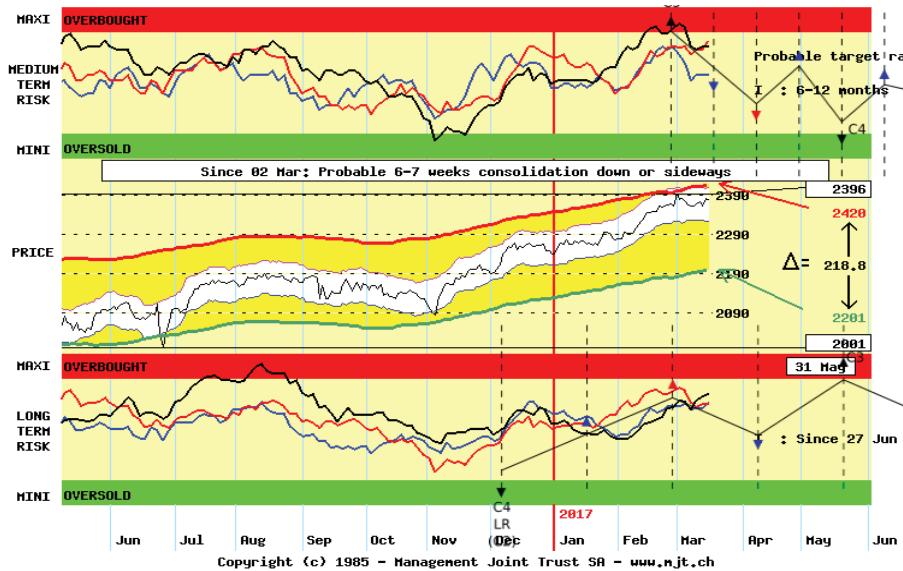
DJ EURO STOXX 50 (Daily chart or the perspective over the next 2 to 3 months)

Short term, Europe also seems extended with our "I" impulsive potential price targets up having been met (right-hand scale). While we may expect some retracement into early April on both our oscillator series (lower and upper rectangles), prices should then continue up towards end April / early May. Again, the potential up does seem limited at this stage.



S&P500 Index

(Daily chart or the perspective over the next 2 to 3 months)



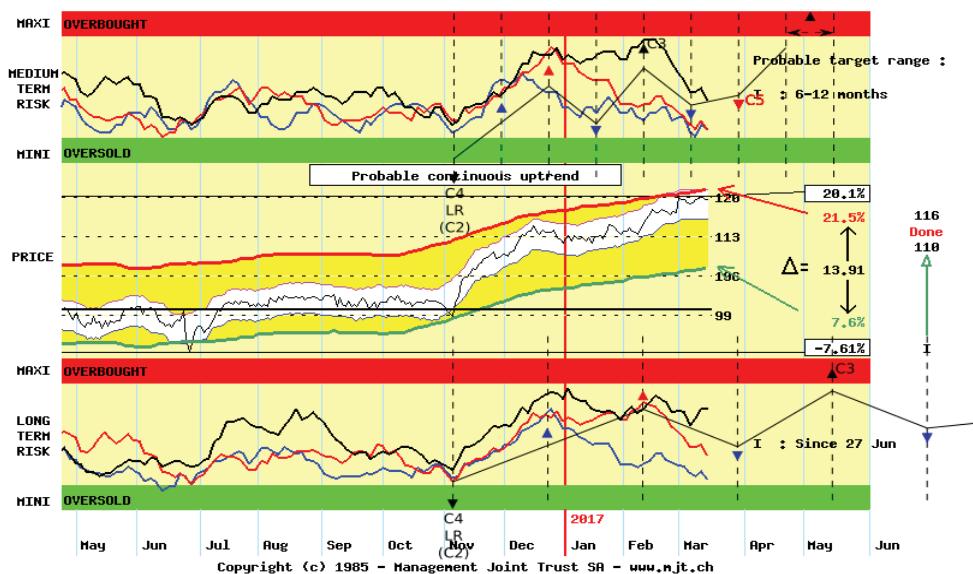
We've decided to take a balanced view on the S&P500. Indeed, with our Weekly chart possibly on an intermediate top (see chart on page 29), the Daily chart also on an intermediate top ("red top", lower rectangle) and our "I" impulsive up price targets potential having been fulfilled (right-hand scale), we don't believe that at this stage, the risk/reward is advantageous anymore. Whatever the scenario we consider, i.e. a correction down and a last move up towards May

(lower rectangle), or the beginning of a downtrend from the recent tops made end February (upper rectangle), we would potentially expect some retracement into early April, a new rally during April before price roll over again into May and June.

VIX CBOE Volatility Index

(Daily chart or the perspective over the next 2 to 3 months)

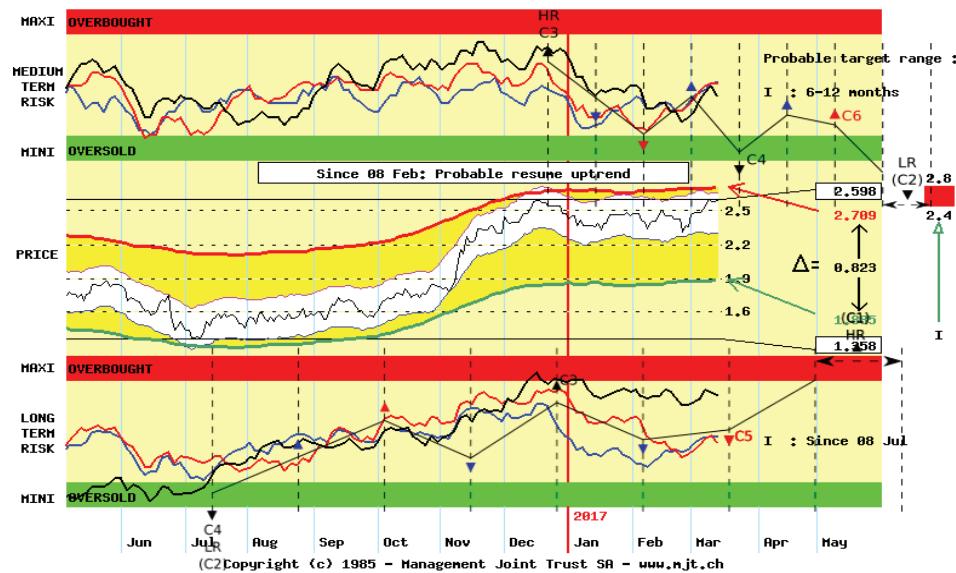
SPY - SPDR S&P 500 / IEF - iShares 7-10 Year Treasury Bond ETF (Daily chart or the perspective over the next 2 to 3 months)



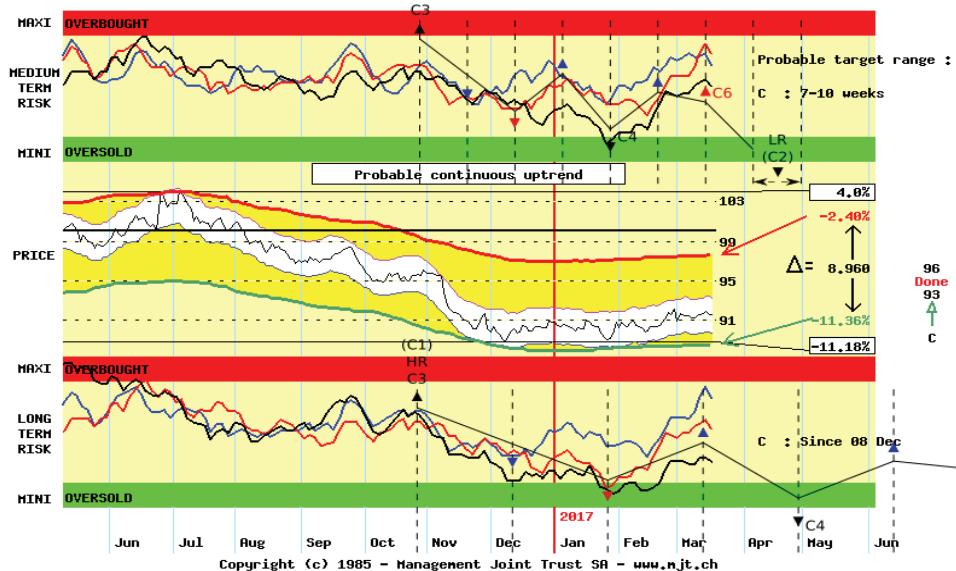
The ratio of equities to bonds also looks extended with our “I” impulsive potential price targets up having been exceeded (right-hand scale). A last move up could materialize towards end April / early May, yet in the meantime we would expect some retracement into end March.

US 10 years Benchmark Bond Yield (Daily chart or the perspective over the next 2 to 3 months)

US 10 year Benchmark bond yields are well within their "I" impulsive targets up (right-hand scale). Hence, the potential to move much higher over the next few months is limited. Whatever the scenario we consider on our oscillator series, a nascent downtrend (upper rectangle) or a continuing uptrend (lower rectangle), rates do seem to hold up during April before they reach tops and roll over from end April / early May into June. Given current volatility (measured by our delta = 0.823%; right-hand scale), the corrective price potential down into June could be between 40 and 60 bps (0.5 to 0.8 times our delta).

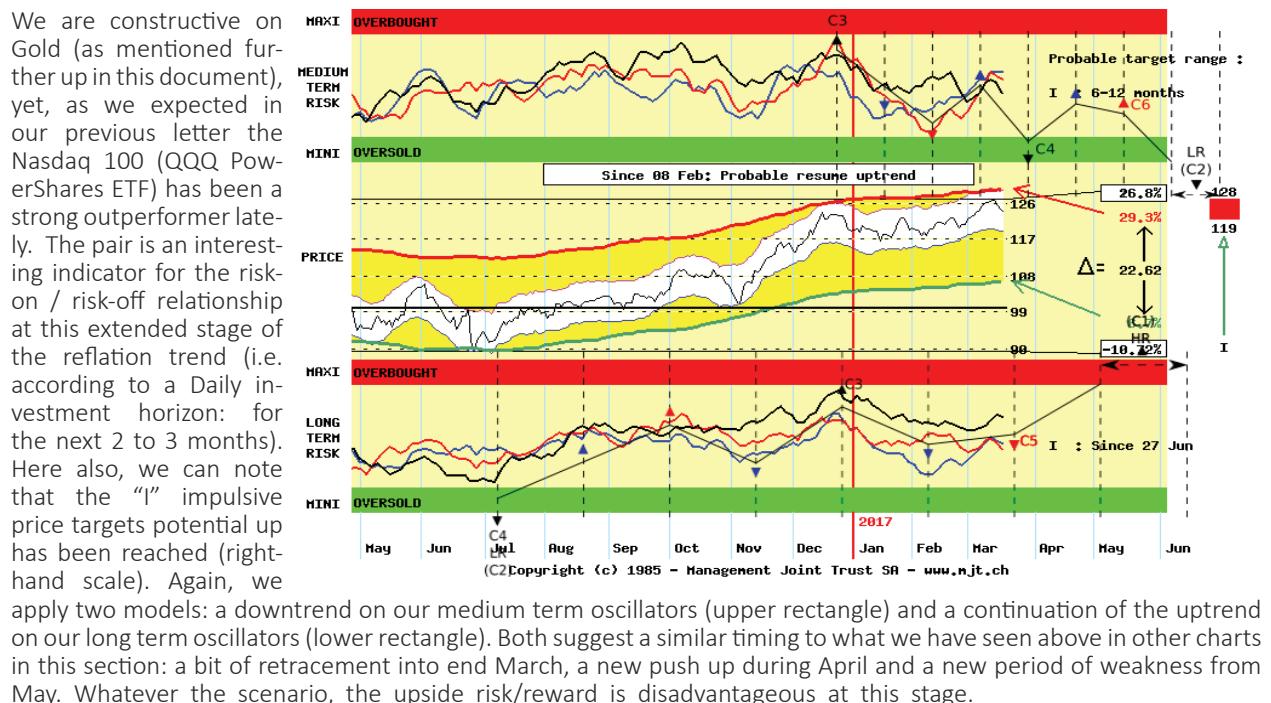


Defensive sectors vs SPY - SPDR S&P 500 (Daily chart or the perspective over the next 2 to 3 months)



US defensive sectors have made a come-back vs the general market since December. When we consider an Equal weighted portfolio of Healthcare (XLV SPDR ETF), Staples (XLP SPDR ETF) and Utilities (XLU SPDR ETF), they may be in the process of resuming down towards late April vs S&P500 ETF (the models we project on both our oscillator series ; lower and upper rectangles)

QQQ - PowerShares QQQ Trust, Series 1 / Gold Spot (USD/Oz) (Daily chart or the perspective over the next 2 to 3 months)



We are constructive on Gold (as mentioned further up in this document), yet, as we expected in our previous letter the Nasdaq 100 (QQQ PowerShares ETF) has been a strong outperformer lately. The pair is an interesting indicator for the risk-on / risk-off relationship at this extended stage of the reflation trend (i.e. according to a Daily investment horizon: for the next 2 to 3 months). Here also, we can note that the "I" impulsive price targets potential up has been reached (right-hand scale). Again, we apply two models: a downtrend on our medium term oscillators (upper rectangle) and a continuation of the uptrend on our long term oscillators (lower rectangle). Both suggest a similar timing to what we have seen above in other charts in this section: a bit of retracement into end March, a new push up during April and a new period of weakness from May. Whatever the scenario, the upside risk/reward is disadvantageous at this stage.

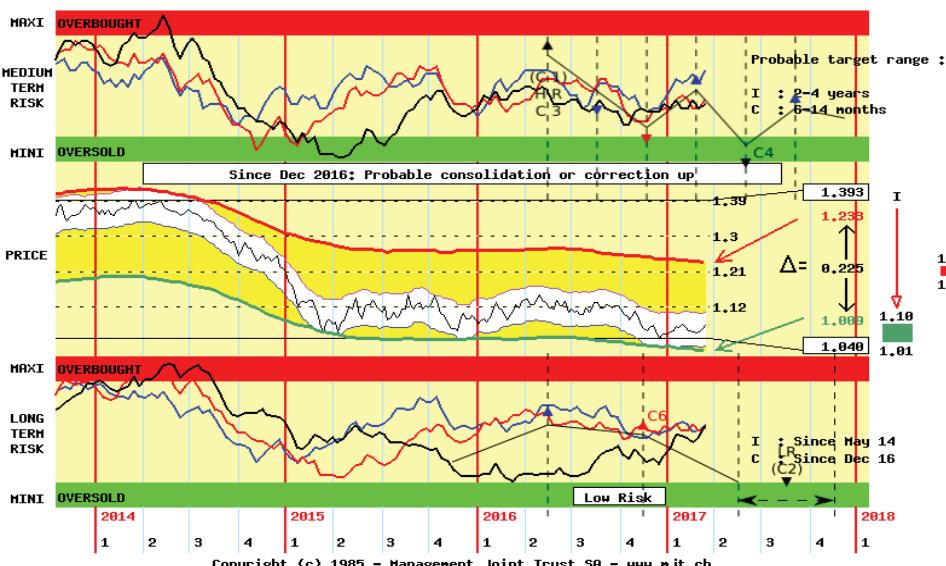
Concluding remarks:

Although at very high level, most risk and reflationary assets correct up / hold / extend during April, before consolidating down into May/June. Impulsive targets up have widely been achieved, hence we expect limited potential. Short term lows for this extension should be found during late March, early April.

35 / SPLICING THE MARKETS - Inflation vs the Dollar in H2 2017

Since mid last year, US data has lead the way and the Dollar has accompanied/led the reflation trades up. We believe that during the later parts of Q2 2017, the relationship may revert, which would confirm our view that during H2 2017 reflation goes global. Here's why (the similarities between the next three charts are very clear):

EUR/USD (Weekly chart or the perspective over the next 2 to 4 quarters)

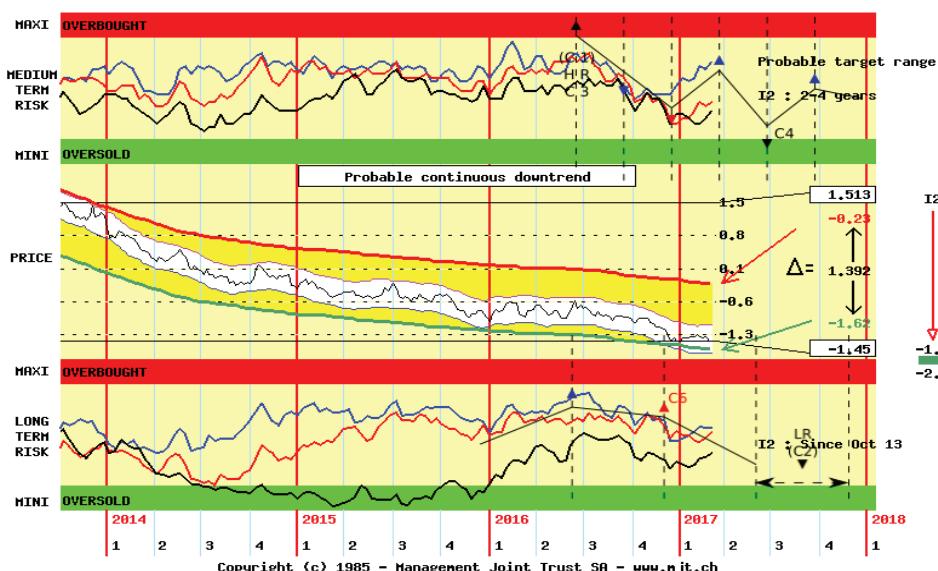


EUR/USD has reached a Low Risk zone as signaled by our automatic messaging (lower rectangle). At the same time, our "I" impulsive price targets down have been met (right-hand scale). Since December indeed, the EUR/USD rate has been showing signs of reversing. That said, given the models we project on both our oscillator series (lower and upper rectangles) and the context of the French election, we cannot exclude a last push down towards mid/end Q2 2017. Following

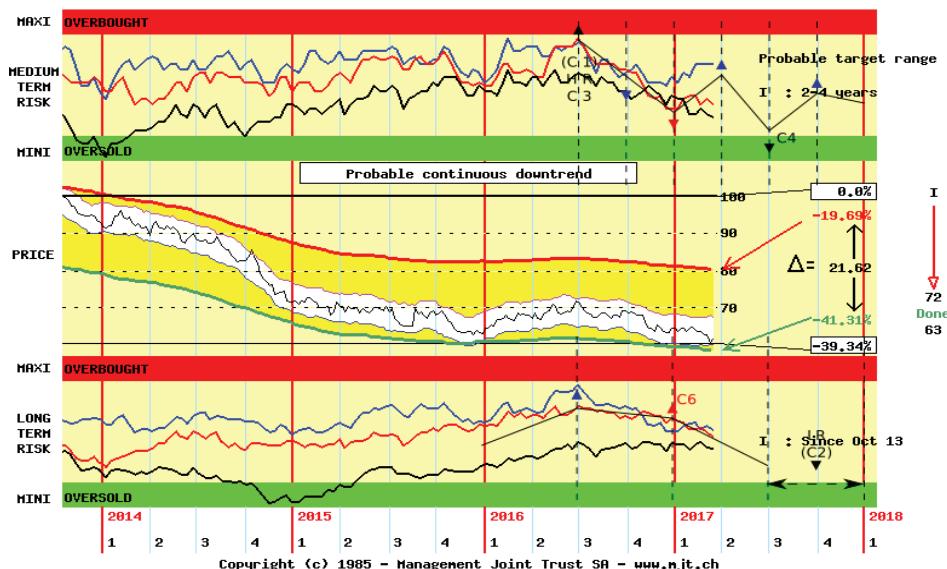
that, we believe EUR/USD could start accelerating up in H2 2017 to reach its "C" corrective targets up towards 1.15 – 1.22 (right-hand scale).

Spain 2 years Benchmark Bond Yield - US 2 years Benchmark Bond Yield (Weekly chart or the perspective over the next 2 to 4 quarters)

Over the last few years, one of the themes behind EUR/USD weakness has been the interest rate spread differential. We believe that as with the EUR/USD, it may be getting ready to reverse (ECB tapering and such forth, an indirect result of reflation as European data improves). We've avoided France or German Sovereign yields vs US ones, as these are probably distorted by the French election. We've hence decided to focus on Spanish benchmark yields vs the US ones as an example (possibly less distorted). Our oscillator configurations are very similar to the ones on EUR/USD (lower and upper rectangles), which would mean that Spanish yields could start to narrow back up vs US ones in H2 2017.



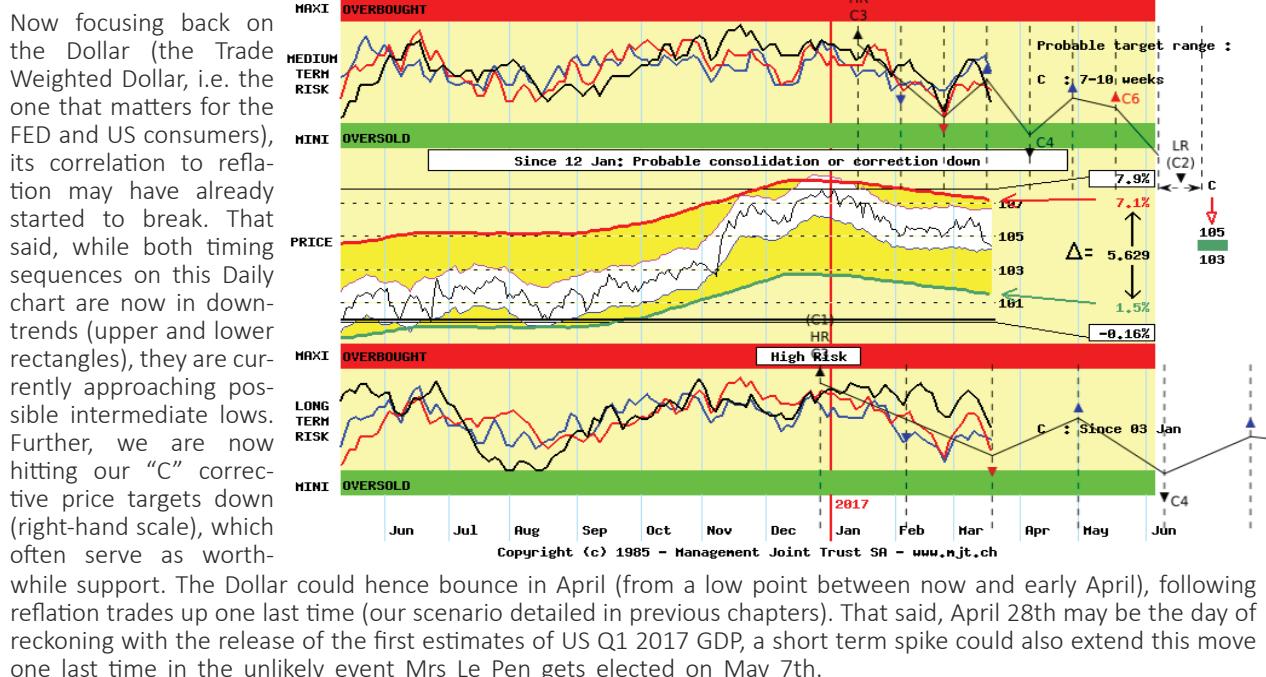
Inflation sensitive assets vs the SPY - SPDR S&P 500 ETF (Weekly chart or the perspective over the next 2 to 4 quarters)



In a previous letter (January 2017), we had mentioned that the inflation differential between the US and Germany was wide apart (higher inflation in the US) and that this situation was likely to mean revert triggering a reversal in EUR/USD. We now look at our inflation sensitive portfolio (mentioned earlier in this document) vs the S&P500. The chart is again very similar to EUR/USD. A reversal would imply that inflation sensitive assets accelerate up vs US equities in H2 2017. This, for

example could result from disappointments in US GDP data, while Commodities accelerate up. A scenario that would certainly underpin the Dollar. In fact, the MSCI World Index vs the S&P500 in USD terms (not shown) is in the exact same situation (getting ready to reverse up).

Trade Weighted Dollar (TWD) – simulated using effective weightings (Daily chart or the perspective over the next 2 to 3 months)



Now focusing back on the Dollar (the Trade Weighted Dollar, i.e. the one that matters for the FED and US consumers), its correlation to reflation may have already started to break. That said, while both timing sequences on this Daily chart are now in down-trends (upper and lower rectangles), they are currently approaching possible intermediate lows. Further, we are now hitting our "C" corrective price targets down (right-hand scale), which often serve as worth-

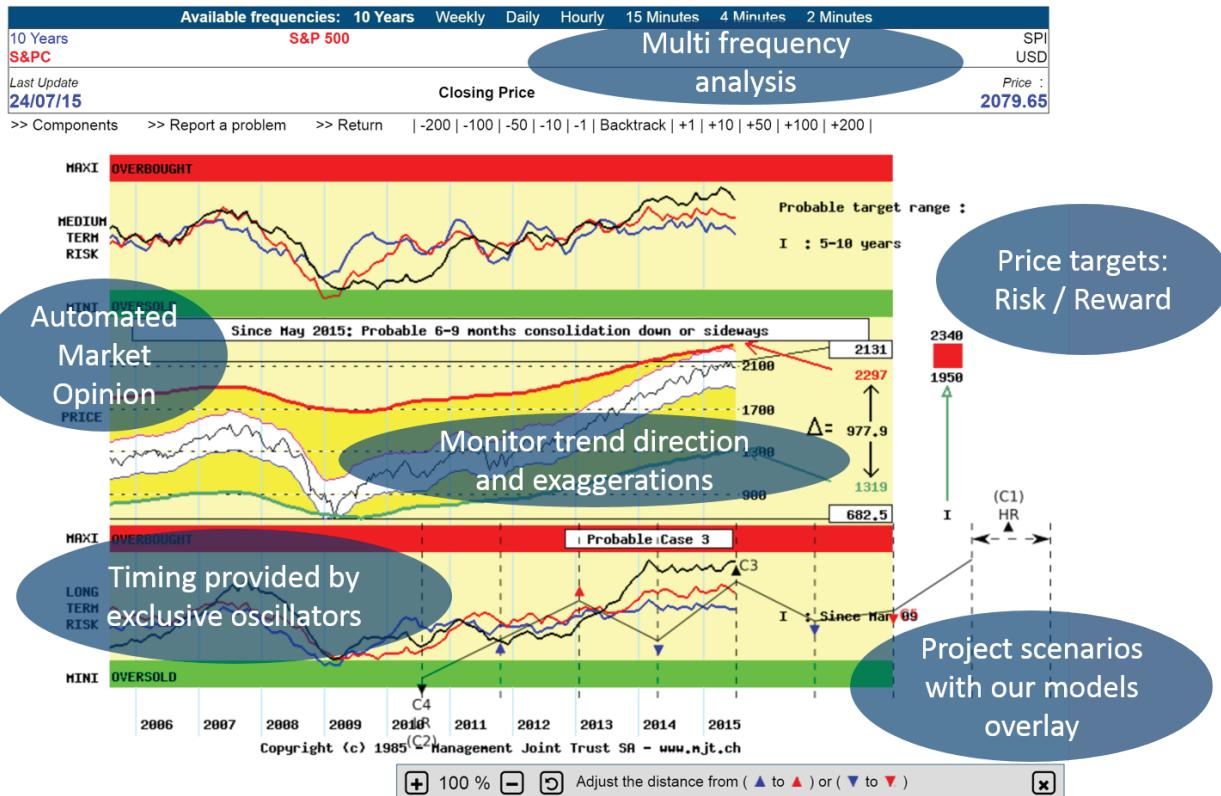
while support. The Dollar could hence bounce in April (from a low point between now and early April), following reflation trades up one last time (our scenario detailed in previous chapters). That said, April 28th may be the day of reckoning with the release of the first estimates of US Q1 2017 GDP, a short term spike could also extend this move one last time in the unlikely event Mrs Le Pen gets elected on May 7th.

Concluding remarks:

Since early 2016, reflation has mostly been a US centric story. Our analysis and projections throughout this document may suggest that this is likely to change in H2 2017, as the US business cycle matures, as Dollar weakness and related commodity led inflation materialize, as the FED is taken back-footed, as the yield curve further steepens, as US markets underperform. A cocktail not dissimilar to 2007 and the run-up to the GFC.

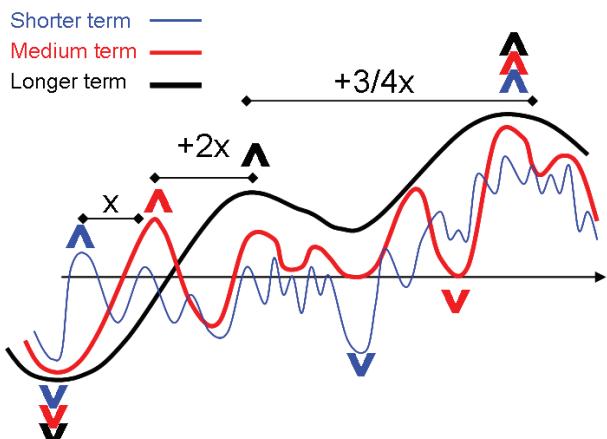
37/ METHODOLOGY

MJT's proprietary methodology uses Timing Oscillators to help investors position themselves either in an uptrend or downtrend. It will hence allow them to anticipate and project the future sequence of events. Coverage extends over 5'000 instruments, long term to intraday, across all asset classes. Relative charts, Opportunity filters, Multi charts monitoring screens and a Portfolio Simulation tool complete the functionality set. See below a description of What's on the Chart, a Methodological brief and an outline of the ideal Uptrend/Downtrend Models (read more on www.mjtsa.com).

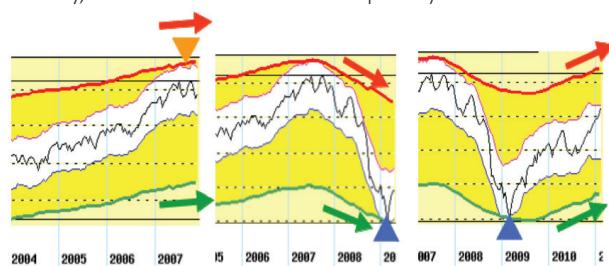


Timing oscillators: Different price cycles are captured by our 3 Timing oscillators. Monitor how their relative positioning defines specific situations (Cases) to always know where you stand within the Trend (e.g. please see below the ideal Uptrend Case succession sequence)

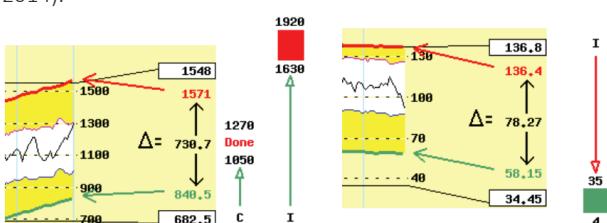
Trend direction: the direction of FinGraphs' large envelope will help you decide either to apply an uptrend or a downtrend model. Contacts between the wider and thinner envelopes will help you anticipate and confirm market turning points (e.g. S&P500 bi-monthly, extracts from the 2005-2011 period).



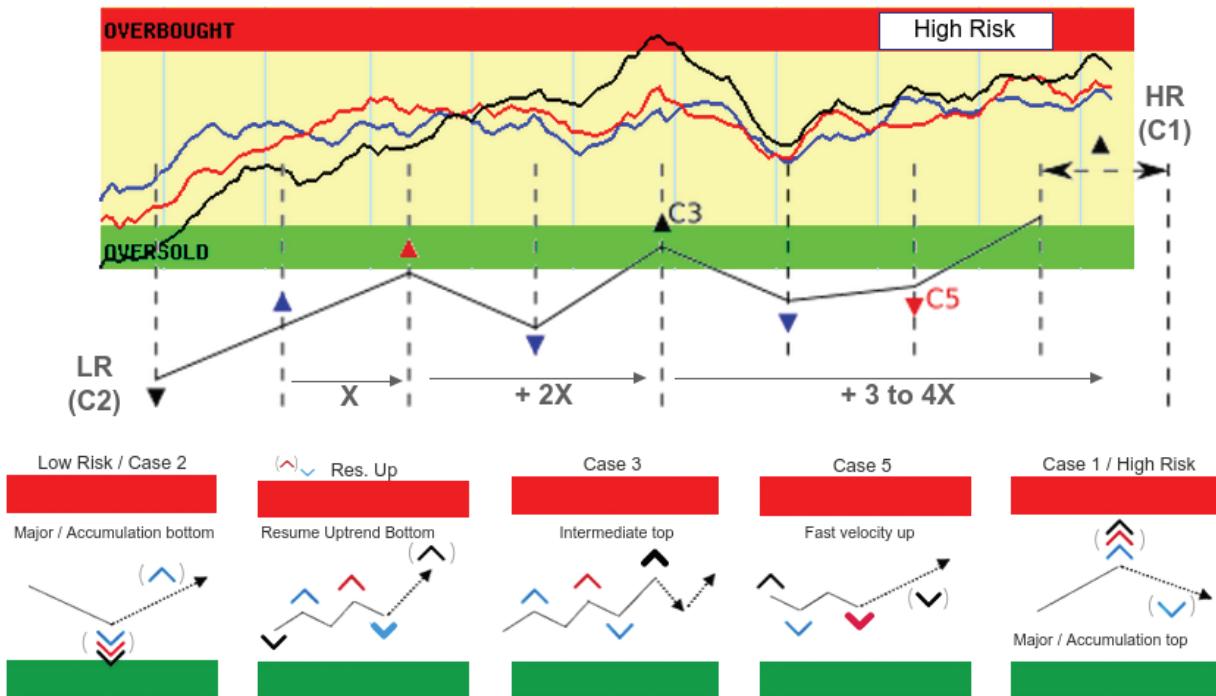
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Price targets: based off historical volatility, they can highlight price potential or risk and, once achieved, define take profit or stop loss areas (e.g. below S&P500 in early 2011, Brent in October 2014).



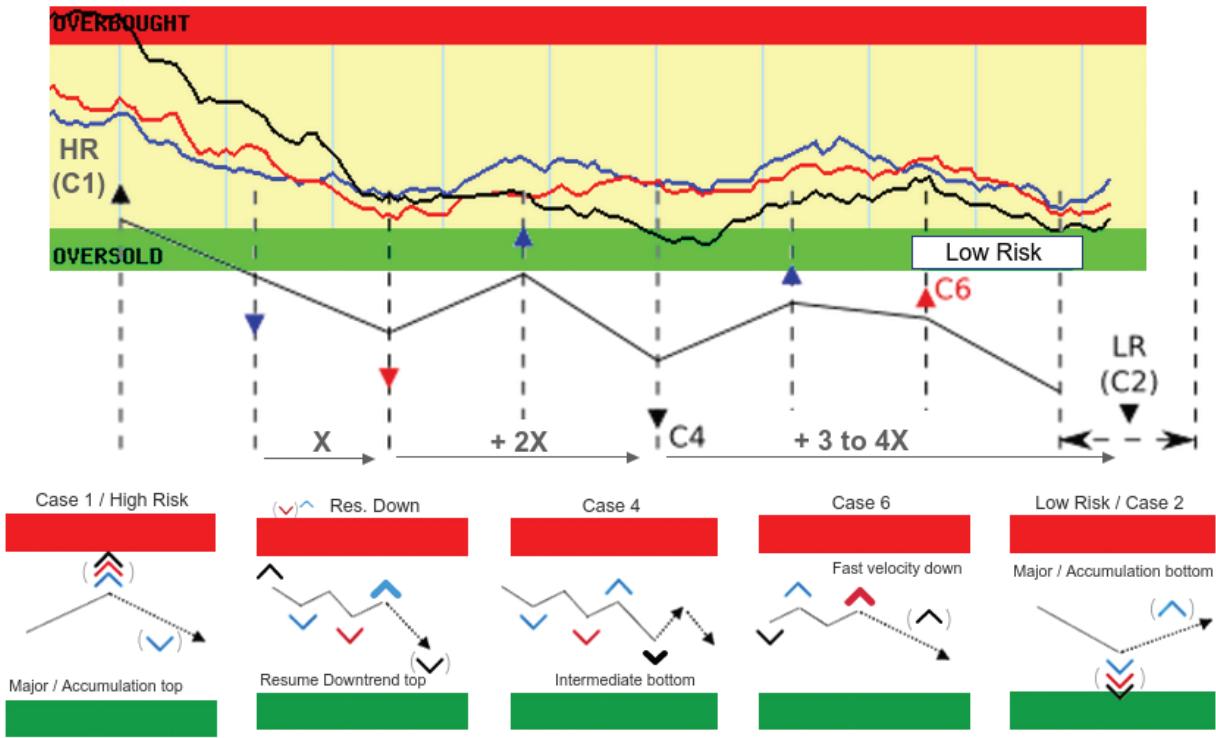
Ideal Uptrend Model



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(left to right) from an oscillator black bottom (usually a Low Risk or a Case 2), the oscillators and prices will start moving up. An uptrend is confirmed once a red top can be made above a blue one. The correction down that follows delivers a buying opportunity ("Resume Uptrend") followed by an intermediate top (Case 3). A new period of consolidation down or sideways then starts, ending with a Case 5 acceleration up towards an important top (usually a High Risk or a Case 1). For each time frame, a fixed time unit separates each timing incidence, so that the distance between a blue and red top is usually X, the distance from the red to the black top is then 2X and the distance between the first and second black top is 3 to 4X.

Ideal Downtrend Model



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(left to right) from an oscillator black top (usually a High Risk or a Case 1) the oscillators and prices will start moving down. A downtrend is confirmed once a red bottom can be made below a blue one. The correction up that follows delivers a selling opportunity ("Resume Downtrend") followed by an intermediate bottom (Case 4). A new period of consolidation up or sideways then starts, ending with a Case 6 acceleration down towards an important bottom (usually a Low Risk or a Case 2). For each time frame, a fixed time unit separates each timing incidence, so that the distance between a blue and red bottom is usually X, the distance from the red to the black bottom is then 2X and the distance between the first and second black bottom is 3 to 4X.

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Management Joint Trust S.A.
Rue de Hesse 1
P.O.Box 5337
1211 Geneva 11
Switzerland

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