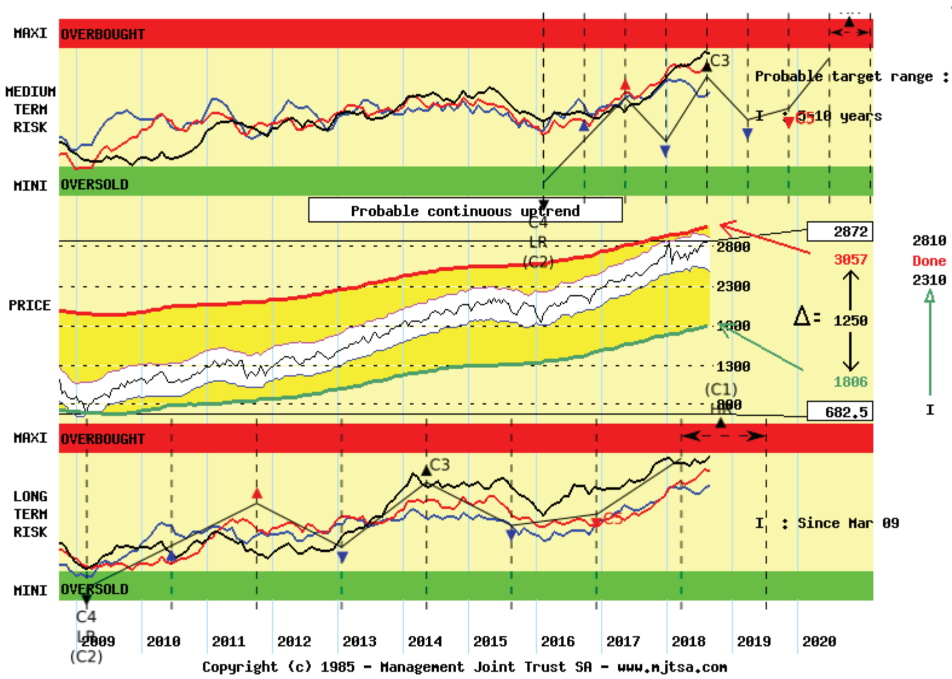
51 / Splicing the markets – This time is probably not that much different

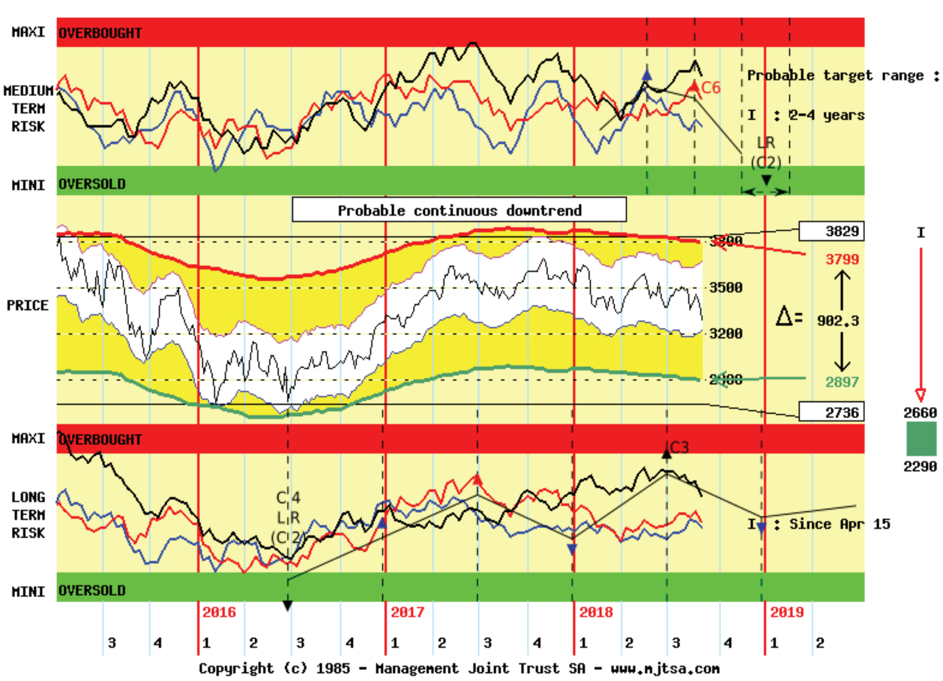
Our medium to long term cross-asset scenario is turning more defensive, and while we were explaining it over the last few weeks, we were getting more and more of the "this time is different" type of argument. Indeed, as they say, the US is still growing strongly, the Emerging markets crisis seems contained for now, interest rates are still relatively low by historical standards and, most importantly, the FED is acting gradually and seems to be in control. In this context, our downside targets do seem aggressive to these professionals, which given the resilient Bull market we've been in since 2009, is probably understandable. In this section, we review and explain the downside targets we currently calculate for the main equity markets.

S&P 500 Index
Bi-monthly graph or the perspective over the next 1 to 2 years



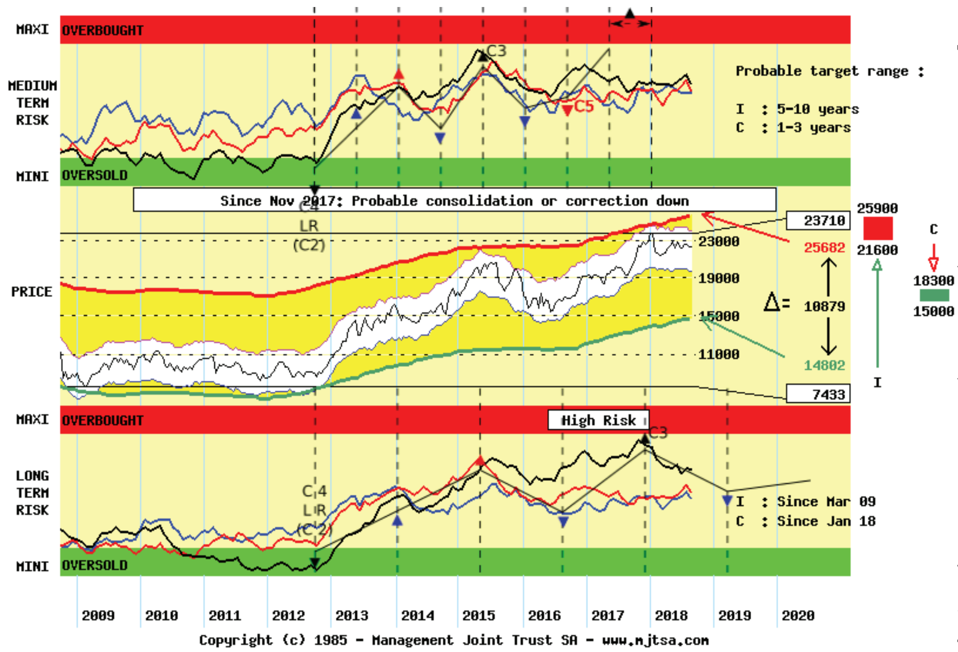
The S&P500 Index is still in an uptrend, yet on both our oscillators series (lower and upper rectangles), it is reaching important tops. Our envelopes (middle rectangle) are touching each other, which is a sign of exaggeration, and our I impulsive targets to the upside have been achieved (right-hand scale). **Taking profit at these levels is rather comfortable in our view, as in general the risk/reward to the upside does seem exhausted. Yet, will the market really start to sell off? We believe so, as the current tops we are expecting on this bi-monthly graph are probably the most important ones since the 2009 recovery.** Indeed, our long term oscillators (lower rectangle) are getting to the end of their uptrend model. **We call these situations "High Risk", and on a bi-monthly graph, they usually trigger 1 to 2 years of a downside correction while achieving our C Corrective targets to the downside. We currently calculate these between 2'247 to 1'872 or 22% to 35% below current levels** (0.5 to 0.8 times our historical measure of volatility "Delta" – here at 1'250; middle rectangle, right-hand side – subtracted from the graph's highest point). When considering market history over longer periods of time, such correction phases are rather standard.

EuroStoxx 50
Weekly graph or the perspective over the next 2 to 4 quarters



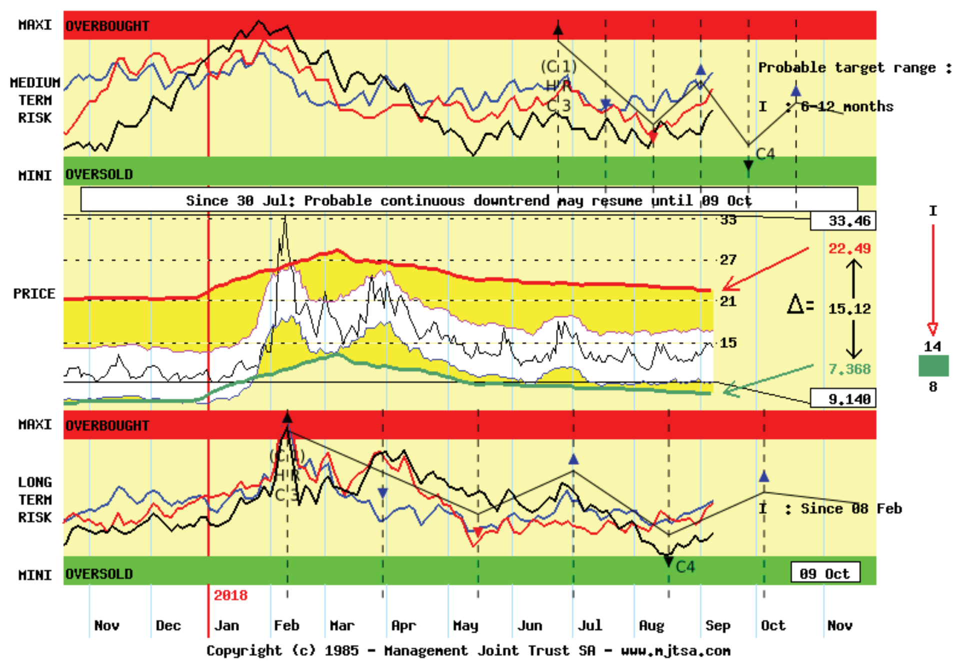
For the EuroStoxx50, we have chosen the Weekly graph. Indeed, compared to the S&P500, its downtrend seems to have already started, while its price targets to the downside are already impulsive (right-hand scale). Both our oscillators series (lower and upper rectangles) suggest that **a first move down will probably materialize into year-end. Following that, the downtrend may then extend into late 2019**. Our downside targets until then (mid/late 2019) are suggesting that **the EuroStoxx 50 could move down to the 2'660 – 2'290 range** (right-hand scale). **This would be 20 to 30% below current levels and below its 2016 lows**. Since 2009, such corrections have happened before, in 2011 and in 2015.

Nikkei 225
Bi-monthly graph or the perspective over the next 1 to 2 years



So far, the Japanese market seems relatively immune to contagion from China and other Asian Emerging markets. Indeed, although it topped out in January, it held up rather well during the Summer. That said, both our oscillators series (lower and upper rectangles) are suggesting that important tops have probably been made, and that the **Nikkei 225 could now continue to consolidate into 2019.** While our I Impulsive targets to the upside have been achieved (right-hand scale), our C Corrective targets to the downside are **suggesting initial downside targets in the 18'300 – 15'000 range. These are circa 20 to 35% below current levels and in line with what we are projecting on the S&P500 and the EuroStoxx 50. For this correction to the downside, Japan may have an additional trigger.** Indeed, if our defensive scenario materializes, the Yen, which is a defensive currency, will probably start to strengthen vs most currencies, and even against the Dollar. **During such periods in the past, when the Yen has strengthened, the Nikkei 225 typically underperformed other developed markets (2009 – 2012 or H1 2016).**

VIX CBOE Volatility Index
Daily graph or the perspectives over the next 2 to 3 months



Throughout this document, we have been writing that we expect equity markets to start a new leg down probably between now and late September. The VIX S&P500 Volatility index seems to show these perspectives in reverse. Indeed, on our long term oscillators (lower rectangle), an intermediate bottom was made mid August and the VIX has since been moving higher. On the other hand, our medium oscillators (upper rectangle) suggest that the VIX may retest down once more over the next couple of weeks. Following that, it should also start to resume up. Combining both, we believe that the **VIX could be bottoming out soon, and that during the leg up we expect during October and November, equities markets and risk assets in general could see another leg down.**

Concluding remarks :

Given the long standing linear Bull market on US equities, a correction that could reach beyond minus 20% would feel like a surprising anomaly. Yet, such corrections have happened in the past and not so long ago in Europe, Emerging Markets or Japan. Financial crisis usually come from left-field and unexpectedly. This time may not be that much different and the current set-up, where, longer term, our oscillators on most markets are reaching important tops, or are already descending, seems quite right for it to happen again.