UBS

Equities Sales Trading Commentary

Technical Analysis

Weekly Comment

Global

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US Market Overbought ... Bullish Reversal in Gold

- **US Trading**: With last week's sideways trading in the Russell and the Friday reversal in the SPX, the technical picture in the US has not changed. The breakout to new all-time highs in the SPX, Russell-2000, and transport are medium-term bullish and confirming our underlying bullish view into Q1 but from a pure timing aspect the early October breakout surprised us. Having said that, despite being too cautious in recent weeks, our short-term call is unchanged. With an intact number of divergences in our indicator work (momentum, market breadth and volatility), the SKEW/VIX ratio hitting a new record, and with continuing to trade in the time window of a 2-month cycle top, we still see the SPX vulnerable for a pullback into deeper/later October before starting its next bounce higher into November. So, although we underestimated the suggested September bounce, we are sticking to our recent call and would use weakness to buy instead of chasing the SPX above 2509.

- With last week's extension, the SPX has reached the upper end of the June bull trend channel at 2550, which should be limited further upside. Key trading support is unchanged at 2509 to 2491, which we expect to be tested into later October. On the sector front, most cyclical themes are overbought (initial reversals in XOI and DJT) and we expect pullbacks into later October, whereas in defensives we can see a bounce short-term. Irrespective of any short-term rotation, from a trend perspective we remain underlying bullish cyclicals and would still use dips to buy/add.

- **US Strategy:** In our cyclical model, the break of the SPX August 8th top at 2491 triggered a new medium-term long signal in our cyclical model into Q1, but this does not mean that on a short-term basis we will not see tactical pullbacks on the way higher. However, (and as we said over the last 3 weeks) with an intact rotation on the sector front (cyclicals and particularly banks and energy outperforming versus defensive underperforming), the SPX should remain well-supported into potential early Q4 weakness. So, although we continue to see the US market short-term vulnerable for a pullback into deeper/later October, and as long as trading above its medium-term pivotal August 21st low at 2417, we remain underlying bullish into Q1, which was and remains our preferred time window for an important and major market top of the underlying 2016 wave 5 bull cycle, and where ahead of this potential top we should see further increasing selectivity in the US and global equities.

- **European Trading**: After the stronger than expected September rally (DAX posted its 3rd strongest September since 1965!!), the move has been losing momentum last week, with most markets trading sideways and an initial reversal in the FTSE MIB. Again, in the bigger picture we have clear evidence that wave 5 of the 2016 bull cycle is underway, which confirms our underlying bullish bias into Q1. However, on a short-term basis, Europe is overbought and the DAX, OMX, CAC and FTSE-100 are facing strong resistance. In this context, we continue to expect a pullback into October, which should bring us higher lows with support in the Euro Stoxx at 3555/3520 into later October, as the setup for the next bounce into November. Although on a very short-term basis we expect the EUR to bounce, with expecting further EUR weakness (wave c) into November, we continue to see Europe and cyclical themes outperforming, which remain a buy into dips whereas defensives we continue to see underperforming.

- **Inter Market Analysis**: The picture on the macro side is unchanged. In bonds, the early September low in US 10-year yields is a major tactical bottom. On a short-term basis, bonds are oversold and despite last week's extension of the September move, we expect a pullback in yields (reflecting a pullback in risk) into later October, whereas medium-term we remain bearish bonds into later Q4/early Q1, where we expect the US 10-year Treasury to still reach 2.60% to 2.80% and weighing on rate sensitive themes.

- In FX, last week we got a marginal extension of the September bounce in the DXY towards 94.14, which is an important short-term resistance. However, with the sharp Friday reversal, we see the DXY on track to completing its first rebound wave a as part of a larger corrective a-b-c pattern into deeper Q4 before starting another and potential final bear wave into later 2017/early 2018. On a very short-term basis, a USD pullback is bullish metals and should trigger a bounce in EMs, where we nonetheless see any strength as an opportunity to sell, since in more and more Asian/EM pairs we think a major USD low is already in place.

- After last week's stabilization and sharp Friday bull reversal, gold is on track with our short-term trading buy call for a wave b rebound into later October before we expect more corrective weakness into November, where, from a cyclical aspect, we see gold moving into its next bigger tactical buying opportunity. A bounce can reach $1308/$1320 to best case $1350. Into November we see an undershooting towards $1250, which however, would leave our underlying bullish bias into 2018 unchanged.

US Equity Market Update:

Chart 1.) S&P-500 Daily Chart

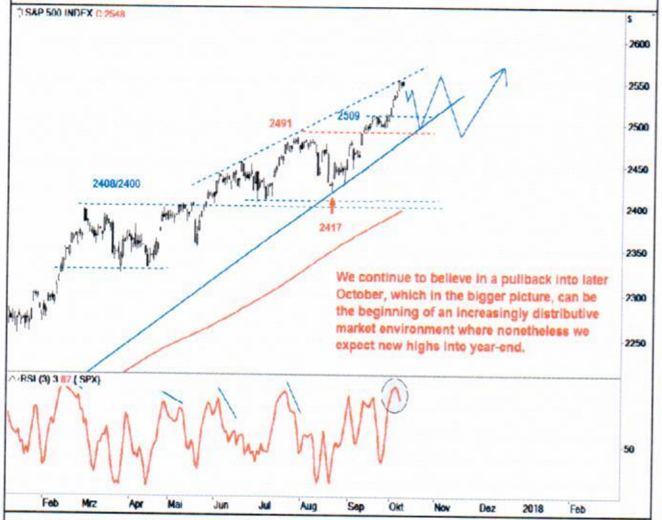
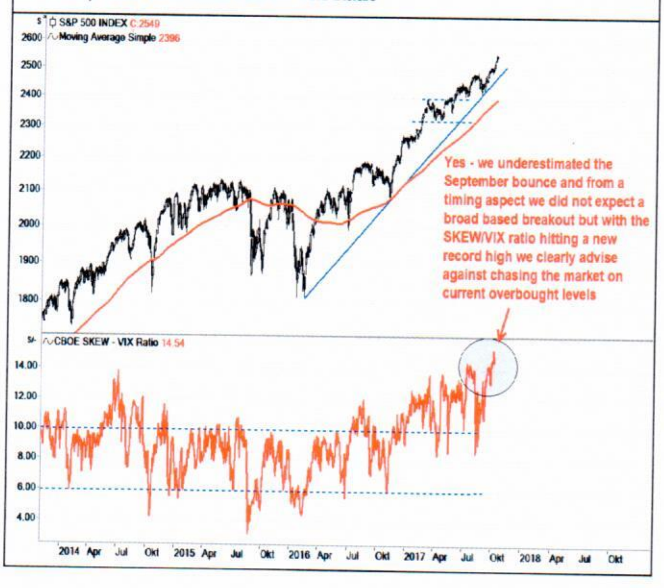


Chart 2.) S&P-500 with NYSE McClellan Oscillator Daily Chart

Chart 3.) S&P-500 with SKEW/VIX Ratio



SPX Facing Trend Resistance

Despite last week's continued overshooting, the technical picture in the US and therefore also our short-term market is unchanged. The breakout to new all-time highs in the SPX, Russell-2000, and transport are medium-term bullish and confirming our underlying bullish view into Q1, which was and remains our preferred timing for an important and potential major top in the US market.

However, **from a pure timing aspect the early October breakout surprised us, as after the August pullback and our suggested bounce into September, we believed in a second pullback leg (wave c) of an a-b-c corrective pattern into October before starting another rally into November and into year-end. As we said last week, with the broad-based breakout this pattern is off the table, but it does not mean we will not see a pullback in October; although, on the back of a renewed rotation on the sector front, a pullback should remain shallow, thus, in our September 19th weekly report we revised our previous 5% to 7% pullback call.**

On a short-term basis the technical setup is unchanged to last week. On the indicator side, **we still have an intact larger number of non-confirmations in our medium-term momentum work** (NYSE McClellan Oscillator), on the volatility side (VIX has confirmed the breakout in the SPX) and if we look at the market internals. Ironically, **despite the strength on the index side, below the surface, we still have an intact picture of a tight breadth where the number of new 52-week highs in the SPX continues to produce lower highs.** Together with the SKEW/VIX ratio at a new record high, and with the SPX still trading in the time window of a 2-month cycle top, we see the SPX vulnerable for a pullback into later October before starting its next bounce higher into November. So, although we underestimated the suggested September bounce, we are sticking to our recent call and would use weakness into later October to buy instead of chasing the SPX above 2509.

Conclusion: With last week's extension, the SPX has reached the upper end of the June bull trend channel at 2550, which should limited further upside. **With last week's Friday reversal, we see the market at the beginning of a short-term top building process where a reversal below 2540 would be initial evidence that a short-term top is forming.** Key trading support is unchanged at 2509 to 2491, and **we continue to expect minimum a test of the steep 2016 bull trend in the SPX into later October.**

US Equity Market Update:

Weakening Momentum in Global Equities

Over the last 3 weeks we got a new breakout in more or less all major headline indices in the US and together with new highs in the transport sector and a new reaction high in the semiconductor sector we have also early cyclical themes confirming the recent breakout in the SPX, which is structurally bullish, which is confirming our underlying bullish bias we had and continue to have into minimum Q1. **Again, irrespective of any tactical pullback calls, before we do not see any bigger divergence between early cyclical themes and the SPX or divergences between major headline indices it is too early to anticipate any bigger top or get bearish in the US market.**

However, despite the broad-based breakout in US headline indices, the market breadth below the surface is not as strong as the picture on the index front suggests and this is a phenomenon we also see on the global basis. In the US, the number of new 52-week highs in the SPX continues to produce lower highs, and even the new high momentum breakout in the Russell-2000 has produced a lower number of new 52-week highs versus the December top. On a global basis, we have a similar effect - where we see a deteriorating number of equity markets hitting a new 52-week high *and/or* with an intact golden cross (100-day moving average trades above the 50-day moving average).

Conclusion: The trend picture in the US and global equities is intact and without any bigger divergences between headline indices and/or early cyclicals it is definitely too early to get bearish. However, tactically, the continued deterioration in breadth and also the deteriorating momentum/increasing divergences in global equities is something we normally see ahead of important tactical tops and generally speaking in the mature phase of a bull market.

Chart 4.) MSCI World with New 52-Week Highs

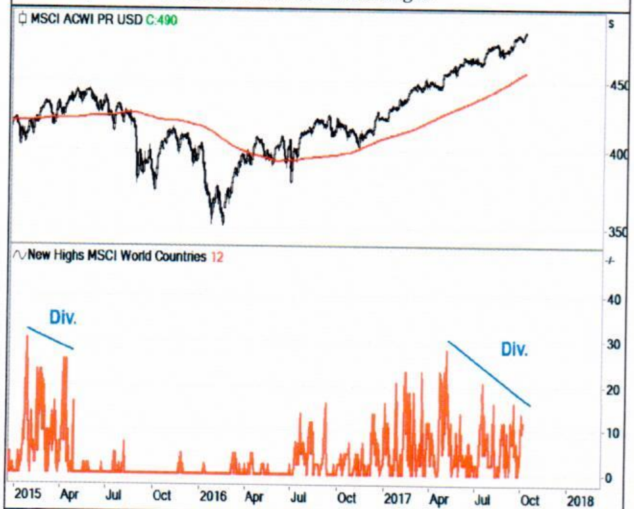


Chart 5.) MSCI World with Intact Golden Cross

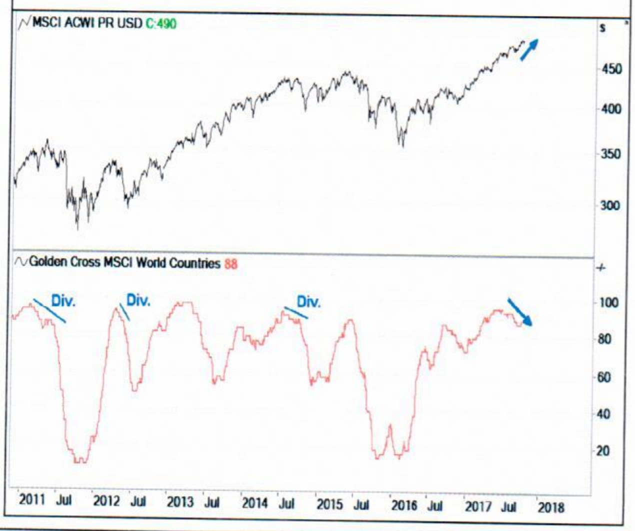


Chart 6.) Russell-2000 with New 52-Week Highs

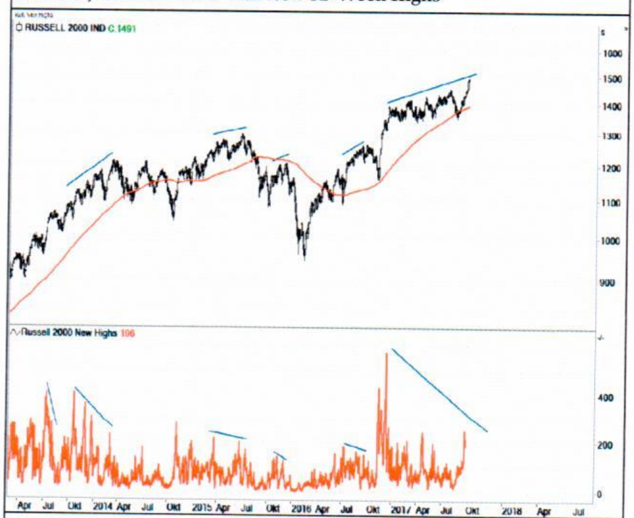
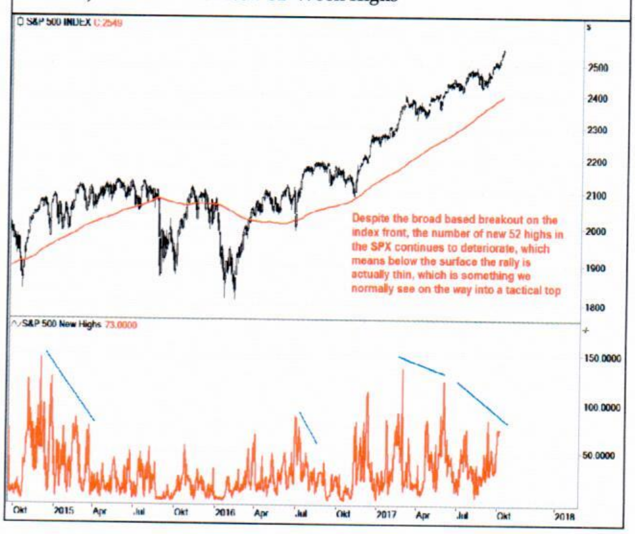


Chart 7.) S&P-500 with New 52-Week Highs



US Equity Market Update:

Intact Trends in Cyclicals but Tactically Overbought

The picture on the sector front in the US has not really changed from last week. From a trend perspective, we have an intact reflation trade, where we expect the underlying outperformance trend of cyclicals versus defensives to continue into later 2017 and into Q1 2018. Having said that, although **financials were still able to extend their September bounce, with deteriorating momentum of the rally and initial reversals in oil stocks and transport, cyclical themes are pretty much stretched and pullback candidates into October.**

In defensives, the picture is also unchanged, where particularly consumer staples remain the weakest link. With the continued relative underperformance of the last few weeks, the sector has broken a multi-year support versus the SPX; where short-term we can see bounces but with our view to see higher rates on the macro side, we would still use any strength to sell, where also in absolute terms we think the sector is not far from breaking its 2009/2010 bull trend. **Again, it was a key call of our 2017 strategy that in a boom and bust bull market it will be ironically the heavy-weighed and still over-positioned defensive sectors, which will break the bull market's neck.**

Other than that, we have healthcare and utilities in a better position but healthcare and biotech are overbought and therefore due for a pullback. After the initial break of the September pullback, we also see a bounce in utilities actually more as a selling opportunity instead of chasing the sector on the upside.

Chart 8.) US Banking Index (BKX) Daily Chart

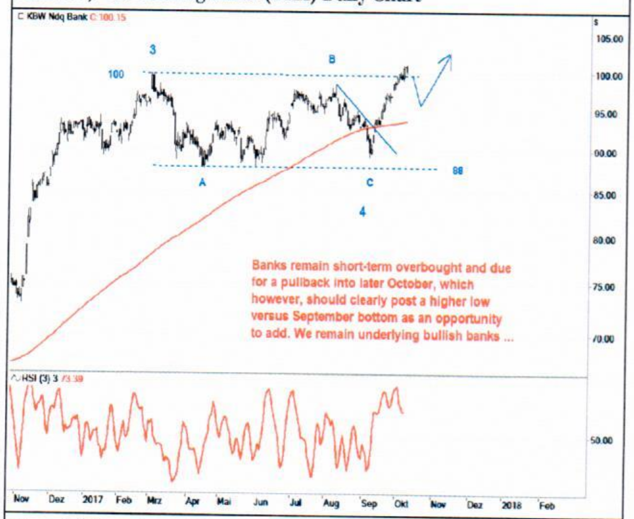


Chart 10.) S&P Consumer Staples Weekly Chart

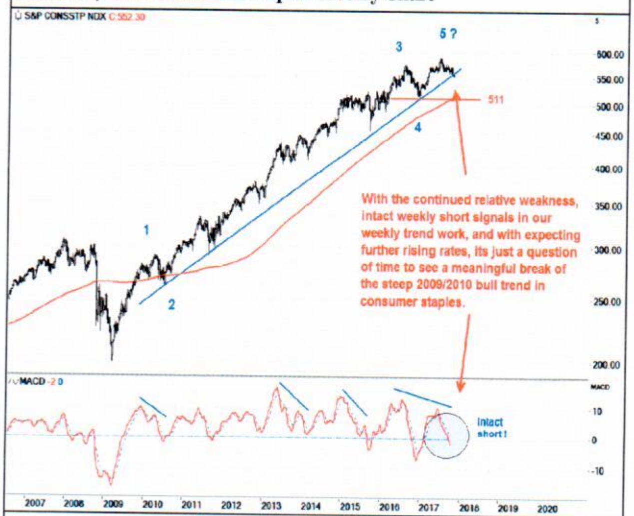


Chart 9.) Dow Jones Transport Daily Chart

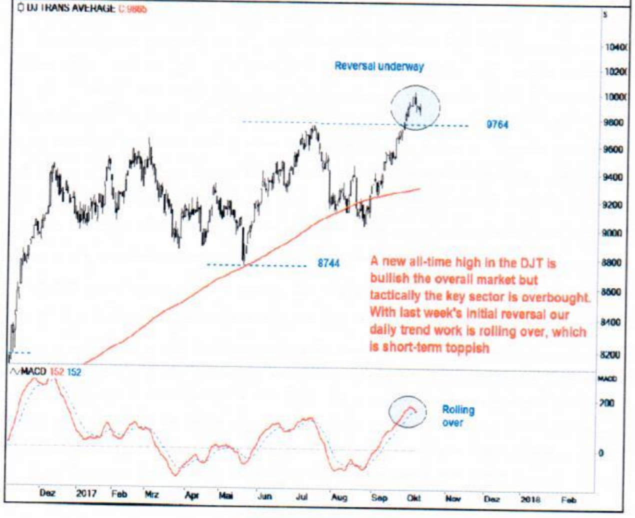
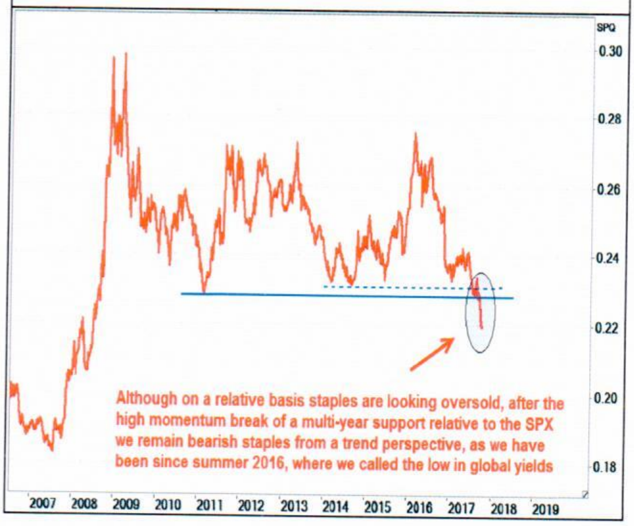


Chart 11.) S&P Consumer Staples versus S&P-500



Inter Market Update:

Initial Reversal in DXY ... Wave B Pullback Underway!

The picture on the macro side is unchanged. In FX, last week, we saw a marginal extension of the September bounce in the DXY towards 94.14, as the ideal target of the September bounce. With the sharp Friday reversal and a fresh short signal in our daily trend work, the DXY is cementing a divergence on the indicator side, which is short-term bearish and suggests our expected initial rebound wave a (as part of a larger corrective a-b-c pattern) is complete. **Again, after calling a tactical bottom in September, we continue to see the US dollar trading in a corrective rebound pattern into all in all deeper November before starting another and potential final bear wave into later 2017/early 2018. In such a pattern, on a short-term basis, we would expect a pullback in the DXY lasting ideally into later October before starting its next up-leg into November.** From a price perspective this **pullback can bring us** both either a re-test of the September low or a higher low, which we clearly prefer and which from a pattern standpoint would form the **right shoulder of a potential inverted head & shoulder bottom, which would also mean that into November the DXY and several key pairs would move into a make or break set up.**

On a very short-term basis, a USD pullback is bullish metals and can trigger a bounce in EMs, where we nonetheless see any strength as an opportunity to sell, since in more and more Asian/EM pairs and also in the commodity block (TRY, INR, SGD, CAD, NZD) we think a major USD low is already in place.

Chart 12.) Trade Weighted US Dollar (DXY) Daily Chart

Chart 14.) USDSGD Daily Chart

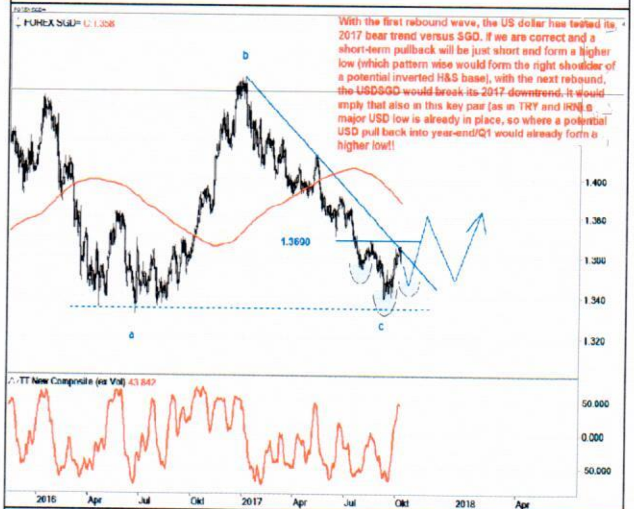


Chart 13.) EURUSD Daily Chart

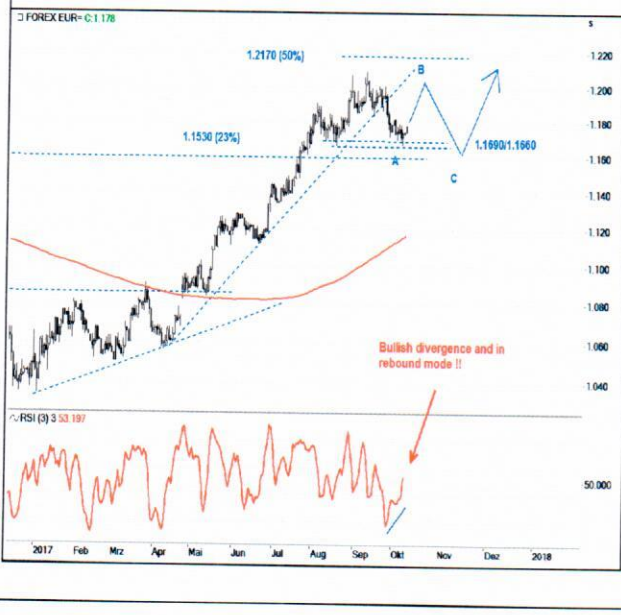
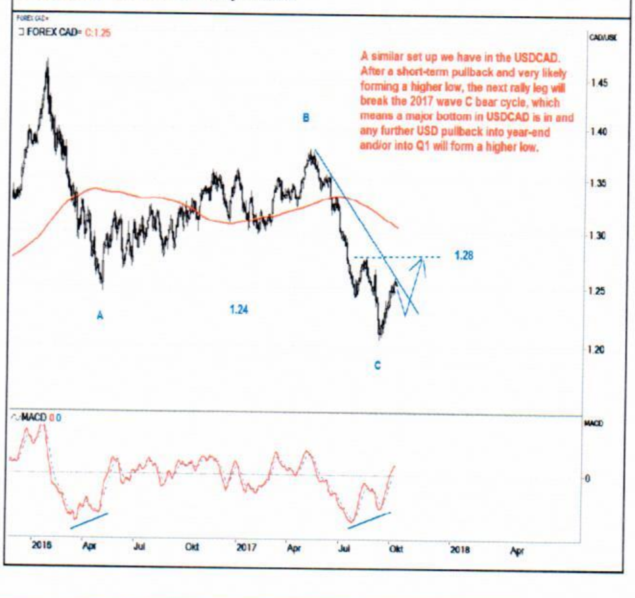


Chart 15.) USDCAD Daily Chart



Inter Market Update:

Chart 16.) US 10-Year Treasury Yield Daily Chart

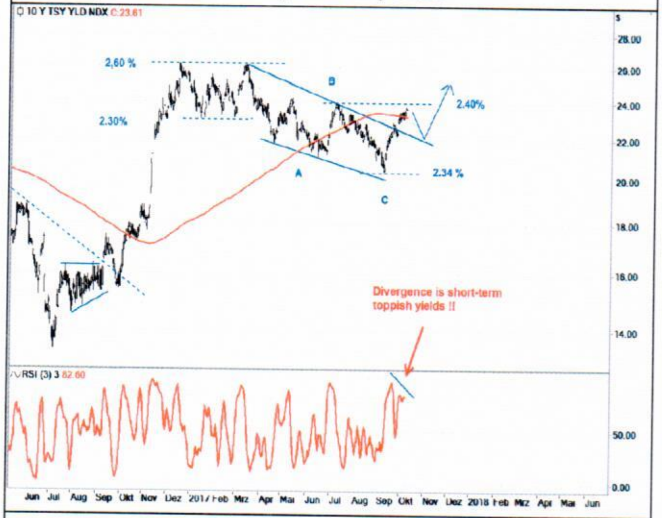


Chart 17.) Gold Daily Chart

Chart 18.) Gold Bugs Index Daily Chart

Bonds short-term oversold

In bonds, the early September low in US 10-year yields is a major tactical bottom. On a short-term basis, the rebound in yields has been extending last week and the US 10-yer Treasury has reached its first important resistance at 2.40%. Again, on a very short-term basis, bonds are oversold and with a divergence in our momentum work forming we expect a pullback in yields (reflecting a pullback in risk) into later October, before starting its next bigger move higher. Our underlying long- to medium-term view is unchanged where we remain bearish bonds into later Q4/early Q1 with target 2.60% to 2.80%, which would certainly weigh on rate sensitive themes and in particularly on Emerging Markets.

Bull Reversal in gold

After last week's stabilization and sharp Friday bull reversal, gold is on track with our short-term trading buy call for a wave b rebound into later October before we expect more corrective weakness into November, where, from a cyclical aspect, we see gold moving into its next bigger tactical buying opportunity.

A bounce can reach $1308/$1320 to best case $1350. Into November we cannot rule out an undershooting towards $1250, which however, would leave our underlying bullish bias into 2018 unchanged and in this context we sticking to our long standing call to buy/add into weakness.

On the gold mining side, the gold bugs index has taken out an initial resistance at 204, which completes a short-term trading bottom and together with a fresh buy signal in our momentum work this is short-term bullish with targets/resistance at 210 and 220, which is the upper end of the major 2017 sideways trading range.

Inter Market Update:

Strong Cyclical Leadership in Europe ...

As in the global context, in summer 2016, together with calling a major bottom in European yields, we called a major bottom in European cyclicals versus defensives, and where we have been in particularly bullish banks. Tactically, we called an important top in cyclical outperformance in late December. Although our suggested Q1 mean reversion rebound in defensives (cyclical underperformance) extended into deeper Q2, with the late June relative bottom and the subsequent trend of the H1 underperformance trend, we are pretty much on track with our underlying cyclical outperformance call, where in the meantime we also got a relative breakout and catch up rally of late cyclical oil stocks. Generally, from a pattern standpoint, and similar to the US, we see the June outperformance cycle in cyclicals as a wave 5, which means that the 2016 outperformance cycle is getting mature and very likely on the way into an important top in H1 2018.

Conclusion: Although on a short-term basis **cyclicals are pretty much stretched** and we expect a pullback into later October, from a trend perspective we remain bullish cyclicals (**particularly as we expect more EUR weakness into November**), so where **dips are still an opportunity to buy/add into intact outperformance trends in autos, chemicals, industry, banks, financials service, technology, oil & gas and basic resource.** On the other hand we have intact underperformance trends in media, personal, retail, telecom, travel, utilities as well as in real estate where any short-term bounce is in our view an opportunity to sell. More importantly, **we still think that the break of the 2008 long-term outperformance trends in healthcare and food have not really reached the investors' minds let alone the over positioning in these sectors and together with expecting rates to further rise, this leaves the door open for negative surprises.**

Chart 19.) European Cyclical versus Defensives

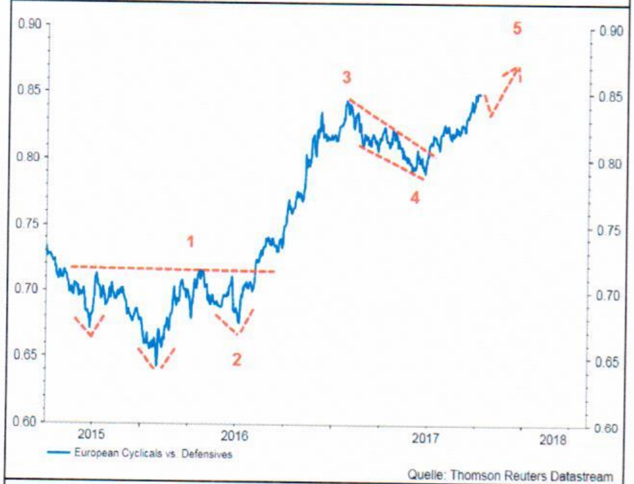


Chart 21.) STOXX Healthcare versus STOXX-600

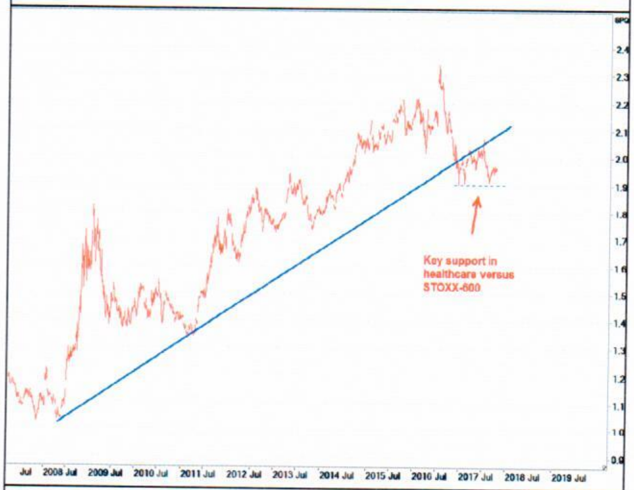


Chart 20.) STOXX-600 Auto (SXAP) Daily Chart

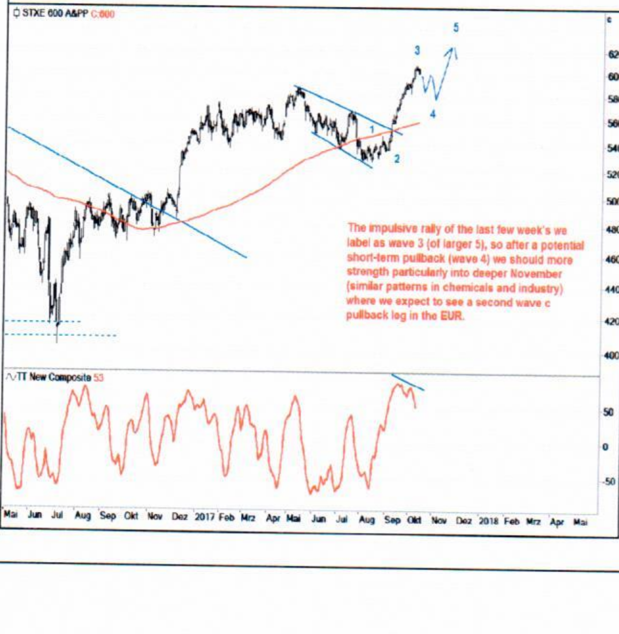
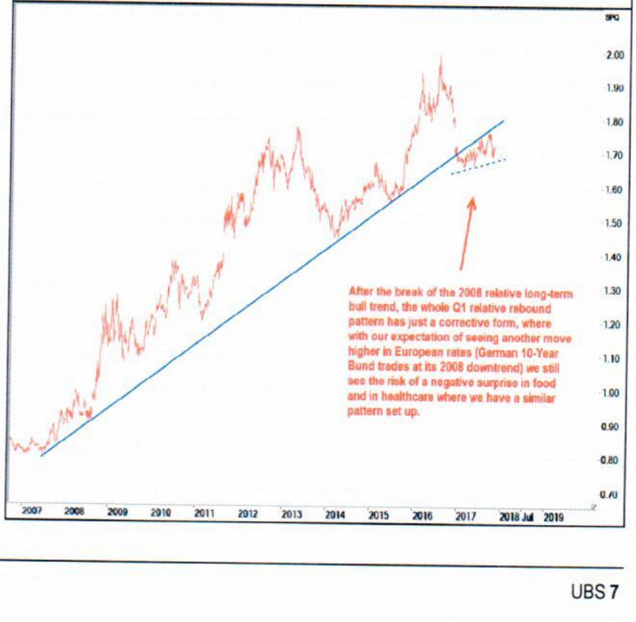


Chart 22.) STOXX Food & Bev. Versus STOXX-600



European Equity Market Update:

Europe Overbought and Due For Pullback

After the stronger than expected September rally (DAX posted its 3rd strongest September since 1965!!), the move has been losing momentum last week, with most markets trading sideways and an initial reversal in the FTSE MIB. Again, in the bigger picture we have clear evidence that wave 5 of the 2016 bull cycle is underway, which confirms our underlying bullish bias into Q1. However, on a short-term basis, Europe is overbought and the DAX, OMX, CAC and FTSE-100 are facing strong resistance. In this context, we continue to expect a pullback into October, which should bring us higher lows with support in the Euro Stoxx at 3555/3520 into later October, as the setup for the next bounce into November. Although on a very short-term basis we expect the EUR to bounce, with expecting further EUR weakness (wave c) into November, we continue to see Europe and cyclical themes outperforming, which remain a buy into dips whereas defensives we continue to see underperforming.

Chart 23.) Euro Stoxx 50 Daily Chart

Chart 24.) OMX-30 Daily Chart

Euro Stoxx 50:

With the momentum in the leading cyclical and financial sectors deteriorating, last week the Euro Stoxx treaded water at around 3600 points. Despite the intact outperformance trends, we have virtually all cyclical and financial key sectors heading towards multi-month resistance levels, and given the overbought situations and the vertical short-term pictures, we label the deteriorating momentum as the early stages of a tactical top building. With the index side remaining at tactically stretched levels and the daily momentum at a toppish stance, a price reversal at around 3600 remains the favored short-term outcome as the basis for a pullback campaign to work off the overbought situation with support at 3555/3520 and the basis for starting a new bounce higher into November.

OMX-30:

The September rally in the Swedish market was nearly vertical and therefore also clearly stronger than expected, as well as from a timing standpoint we saw the move earlier than favored. Nonetheless, on a short-term basis the market is clearly overbought and with facing strong and obvious resistance at 16657 we expect a short-term pullback into later October as the basis for another move higher into November where a break is very likely.

European Equity Market Update:

Chart 25.) FTSE-100 Daily Chart

FTSE-100:

With the GBP retreating further towards the 1.30 threshold, the FTSE remained supported and bounced further. With a tactical reversal in the USD forming, the FTSE is expected to remain capped below the overhead resistance at 7600, keeping the index in a neutral trend condition. With the daily momentum turning in overbought territory, we remain a buyer into the expected later October weakness within the trading range with a big support zone at 7200/7100.

Chart 26.) DAX-30 Daily Chart

DAX-30:

With cyclical key sectors such as chemicals, industrials and autos showing signs of deteriorating momentum, the rally stalled last week at around the round number at 13000, which almost coincides with the May reaction high. The overbought daily momentum is turning short so that a price reversal at around 13000 as the starting point of a pullback into deeper October remains favored. Given the impulsive style of the September rally, retracing the last wave towards 12600/12500 must be taken into account before the real breakout attempt becomes more realistic later in Q4.

Chart 27.) Swiss Market Index Daily Chart

Swiss Market Index:

After a better start into last week, the SMI traded sideways, mainly in-line with a couple of other indices in Europe. Pattern-wise, the early October upside extension has the character of a wave 5 of a minor degree and daily momentum is toppish so that last week's sideways trading could already be part of a minor top building.

With the current extension taking the shape of a wave 5 of a minor degree, the near-term risk is a wave 5 retracement move towards 9070. However, a pullback in October should be of a corrective nature following the previous impulsive move.

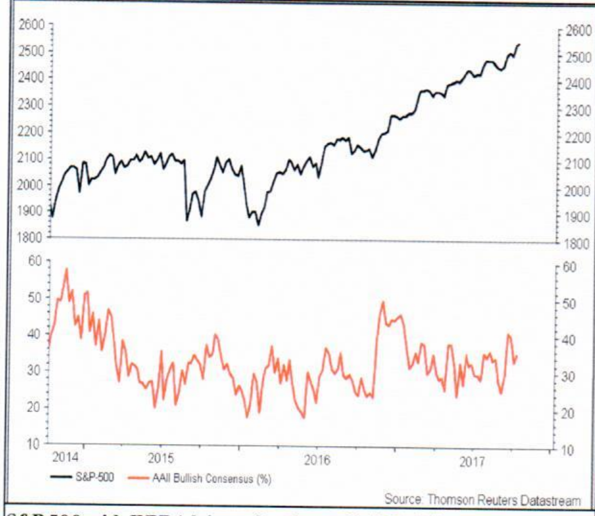
Sector-wise, we continue to favor the cyclical and financial sectors, which are now overbought so that an October pullback should offer opportunities to add.

STOXX Europe 600 Index Sector Overview:

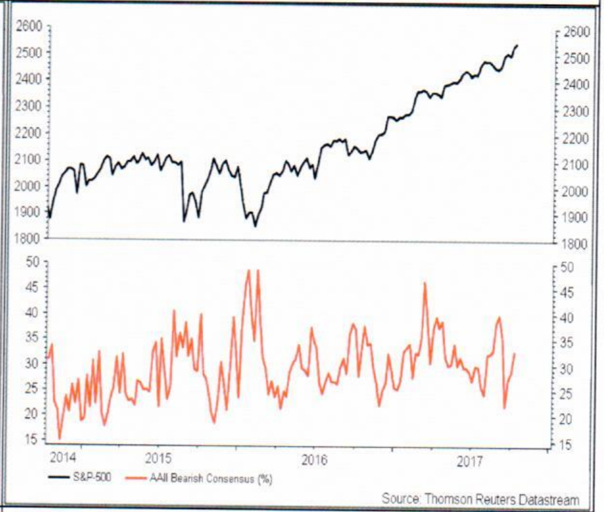
	RIC	Trading at	Trend (weekly MACD)	Rel. Strength according to the spread chart
Industrial Goods & Services	SXNP	532.16	↗	Outperforming
Basic Resources	SXPP	438.96	↗	Outperforming
Chemicals	SX4P	952.93	↗	Outperforming
Automobiles & Parts	SXAP	604.33	↗	Outperforming
Oil & Gas	SXEP	306.48	↗	Outperforming
Financial Services	SXFP	487.53	↘	Outperforming
Technology	SX8P	443.04	↗	Neutral
Constructions & Materials	SXOP	461.7	↗	Neutral
Healthcare	SXDP	761.77	↗	Neutral
Banks	SX7P	187.79	↘	Neutral
Utilities	SX6P	300.31	↘	Neutral
Insurance	SXIP	286.31	↘	Neutral
Personal & Household Goods	SXQP	851.19	↘	Underperforming
Food & Beverage	SX3P	671.7	↘	Underperforming
Travel & Leisure	SXTP	252.02	↘	Underperforming
Real Estate	SX86P	168.81	↘	Underperforming
Telecommunications	SXKP	286.64	↘	Underperforming
Retail	SXRP	302.77	↘	Underperforming
Media	SXMP	270.74	↘	Underperforming

Weekly Technical Indicators: (Source: Pinnacle Data, Datastream) Charts: Tradesignal

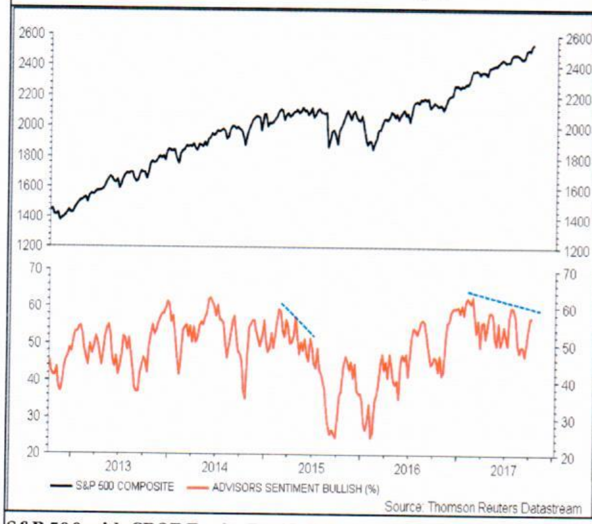
S&P 500 with AAII Bullish Consensus (%)



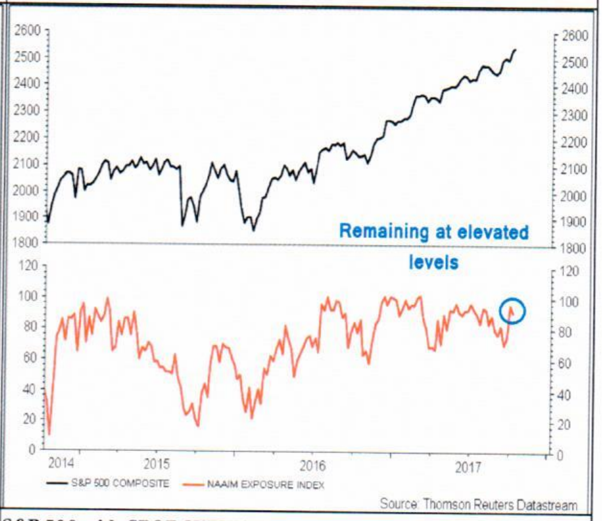
S&P 500 with AAII Bearish Consensus (%)



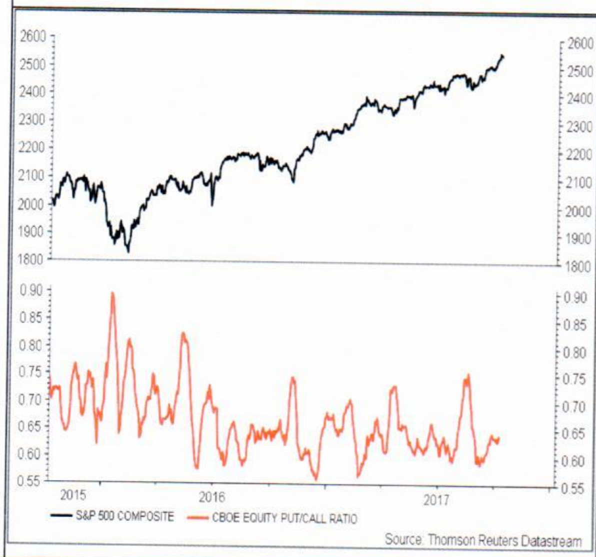
S&P 500 with INVI Advisors Sentiment Bullish (%)



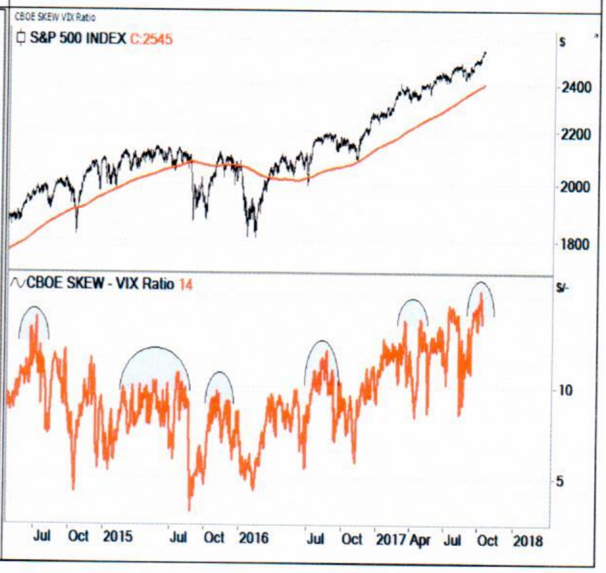
S&P 500 with NAAIM Exposure Index



S&P 500 with CBOE Equity Put/Call Ratio

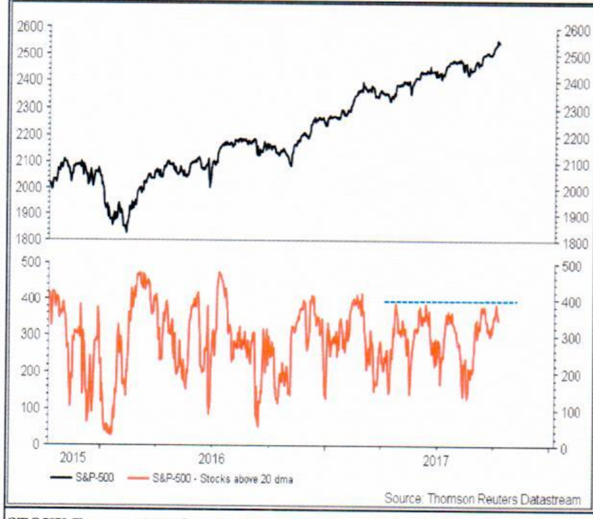


S&P 500 with CBOE SKEW/VIX Ratio

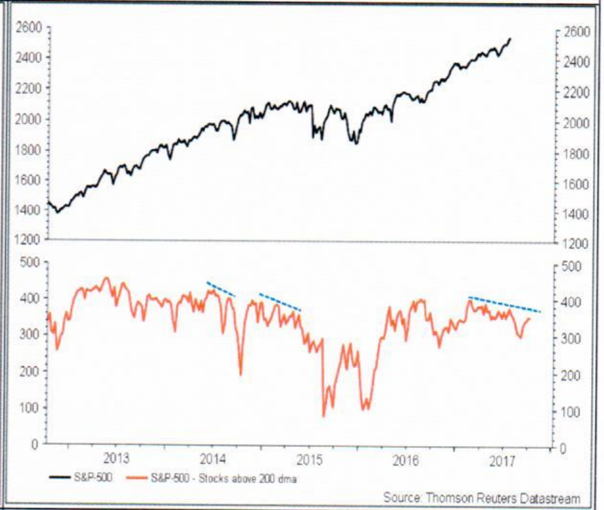


Weekly Technical Indicators: (Source: Pinnacle Data, Datastream) Charts: Tradesignal

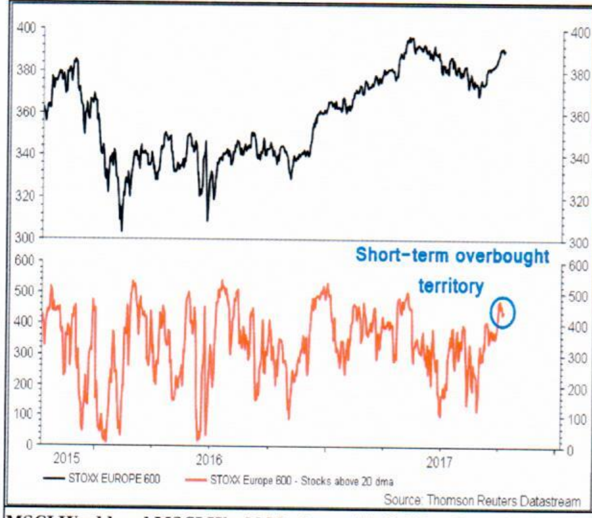
S&P 500 Stocks above 20 day moving average



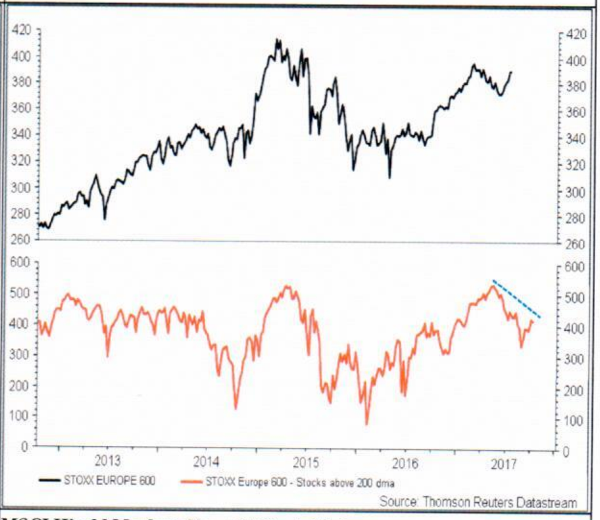
S&P 500 Stocks above 200 day moving average



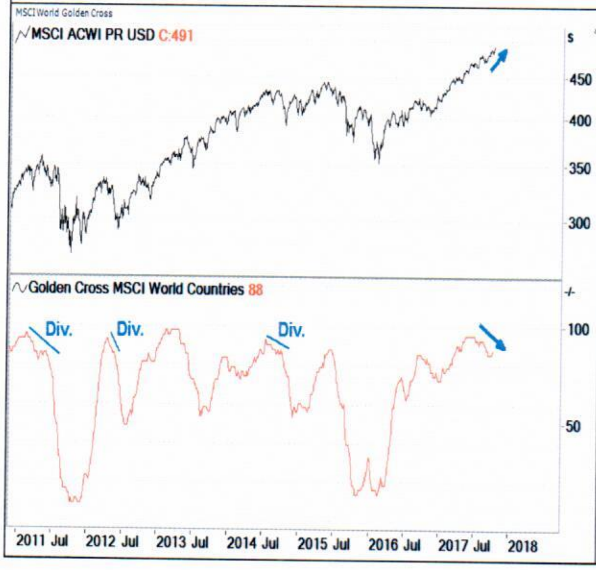
STOXX Europe 600 Stocks above 20 day moving average



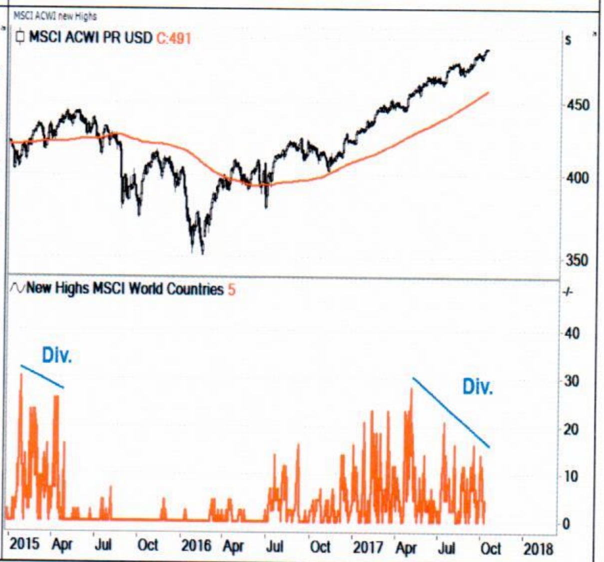
STOXX Europe 600 Stocks above 200 day moving average



MSCI World and MSCI World Markets with Golden Cross (%)

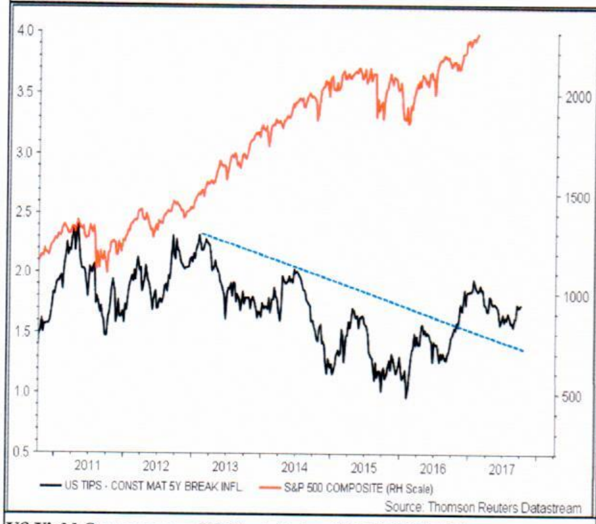


MSCI World Markets New 52-Week Highs

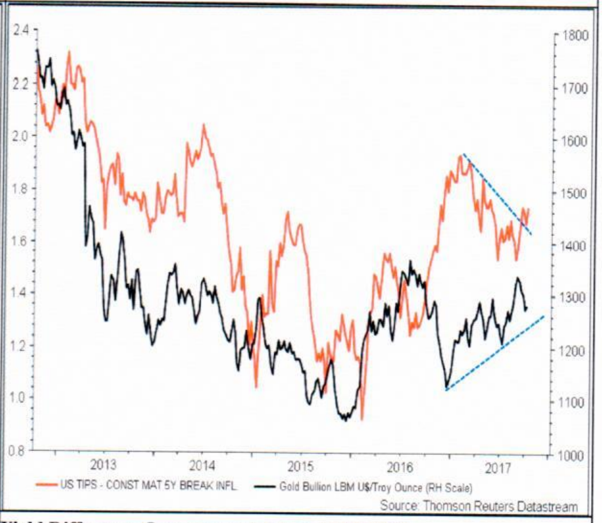


Weekly Technical Indicators: (Source: Pinnacle Data, Datastream) Charts: Tradesignal

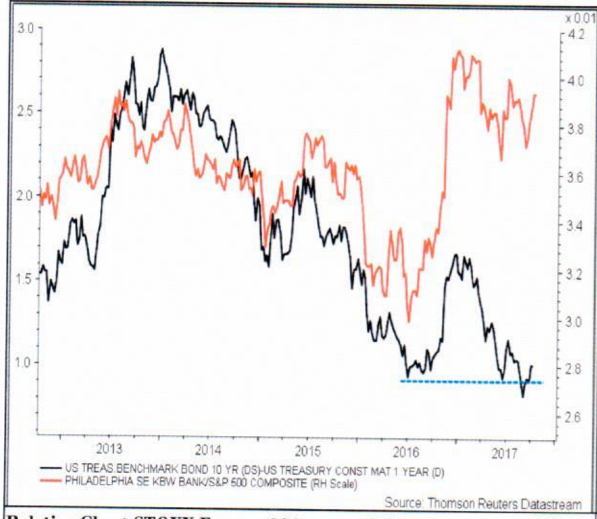
S&P 500 with Break-Even Inflation Rate



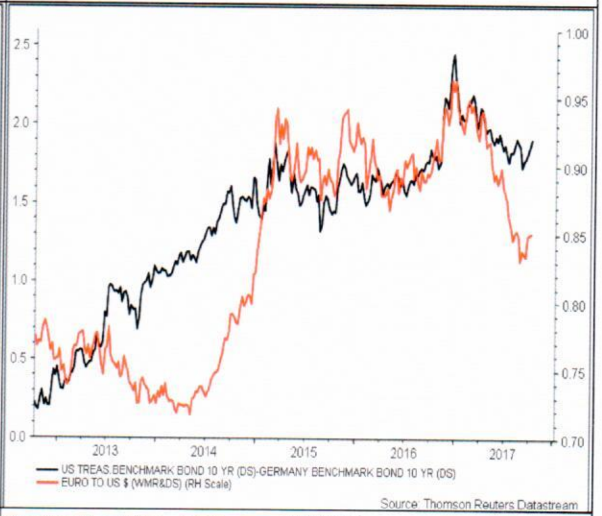
Gold with Break-Even Inflation Rate



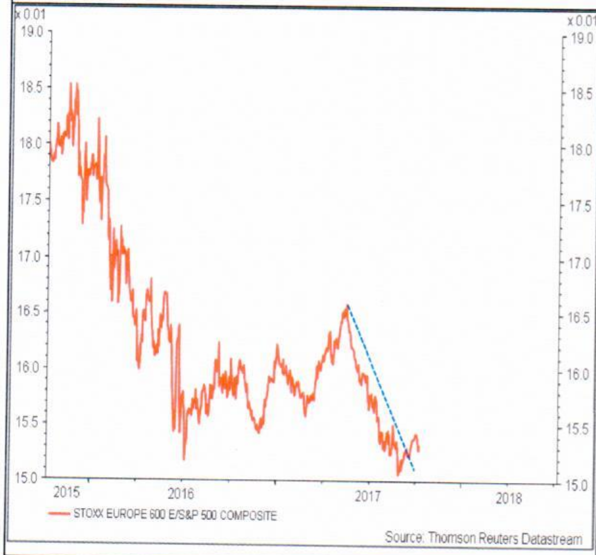
US Yield Curve versus US Bank Index (BKX)/S&P 500



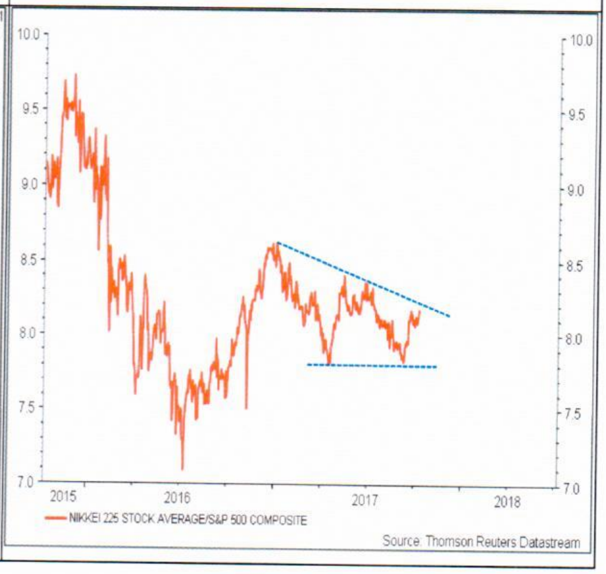
Yield Difference Germany vs USA and EURUSD



Relative Chart STOXX Europe 600 versus S&P 500



Relative Chart Nikkei 225 versus S&P 500



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