TECHNICAL STRATEGY NOTE:
CROSS-ASSET CLASS:
ROOM FOR DISAPPOINTMENT IS HUGE

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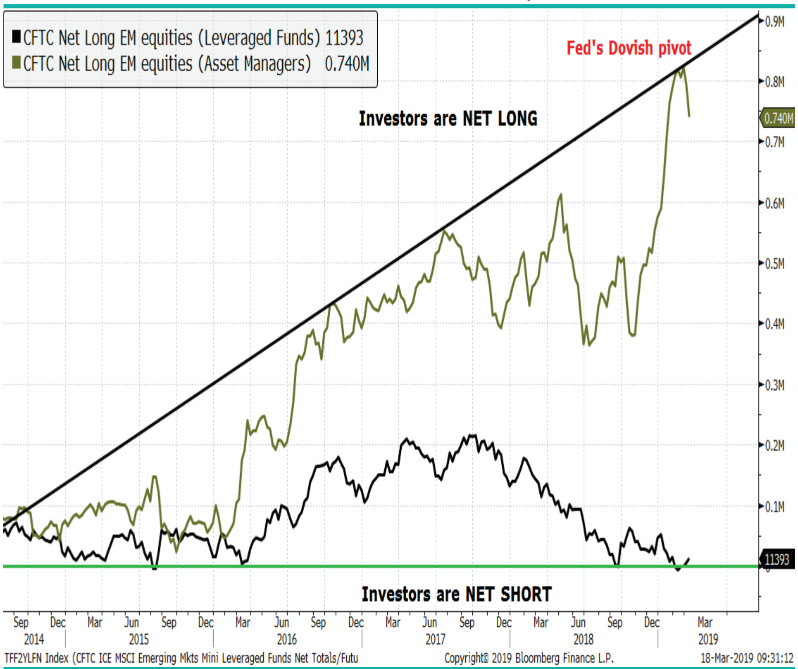
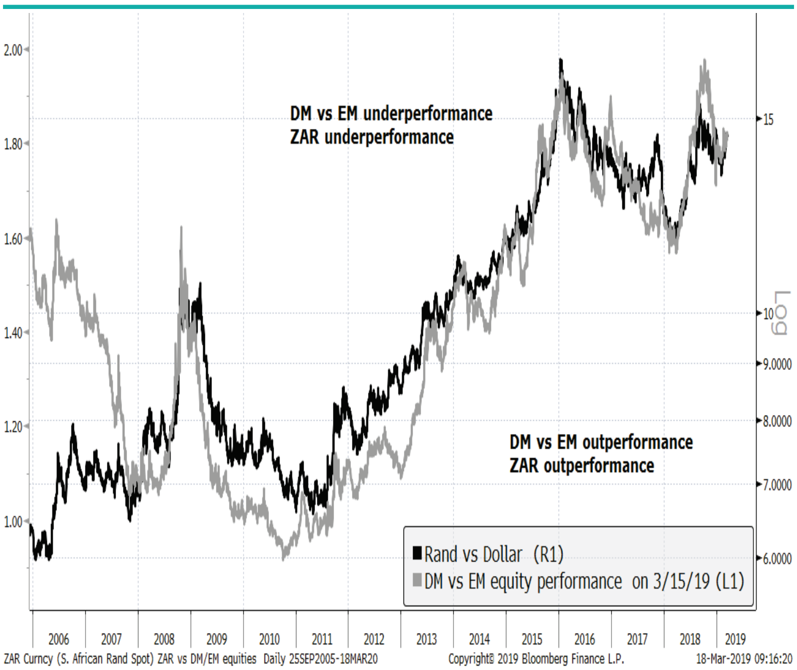
CAN BULLISH INVESTOR POSITIONING TOWARDS EM EQUITIES BE SUSTAINED?



Source: Bloomberg, Nedbank CIB

- Global growth is slowing and China's financial system is "clogged" (the relationship between reserve requirements and M1 has broken down). Also, our measure of **Global $-Liquidity** remains in negative territory; hence, downside risks for SA/EMs remain intact.
- Investors have priced in that the **Fed** is likely to leave interest rates on hold for the rest of year, especially after the Fed's sudden dovish pivot late last year. However, room for disappointment is huge, as the Fed would need to signal that its **balance sheet runoff or quantitative tightening will end sooner than later**. Should the Fed fail to signal this on Wednesday, we could expect a risk-off phase to materialise.
- That said, should the Fed signal that its balance sheet runoff will end soon, we would expect a further rally in risk assets. We, however, do not expect the rally to be sustainable (as was the case in 2016 and 2017), as the macro-environment still faces many headwinds.
- **We maintain our view that the USD will remain strong as the year progresses.**

RAND IN SEARCH OF A LIQUIDITY INJECTION AS MOMENTUM WANES



Source: Reuters, Nedbank CIB

- **SA perspective:** There is a strong relationship between the rand and EM/DM equity market performance. Should the Fed manage to deliver a positive outcome for investors, we could expect further portfolio flows into EMs, which would bode well for SA assets and the rand. The sustainability of this rally would, however, depend on macroeconomic developments both internationally and domestically.
- **Scenarios and anticipated levels to watch for:**
  - Risk-on targets: USD/ZAR 13.94-13.80, R186 8.35-8.22% and Top-40 (52,200 to 54,000).
  - Risk-off targets: USD/ZAR 15.00, R186 9.12-9.25% and Top-40 (43,300).

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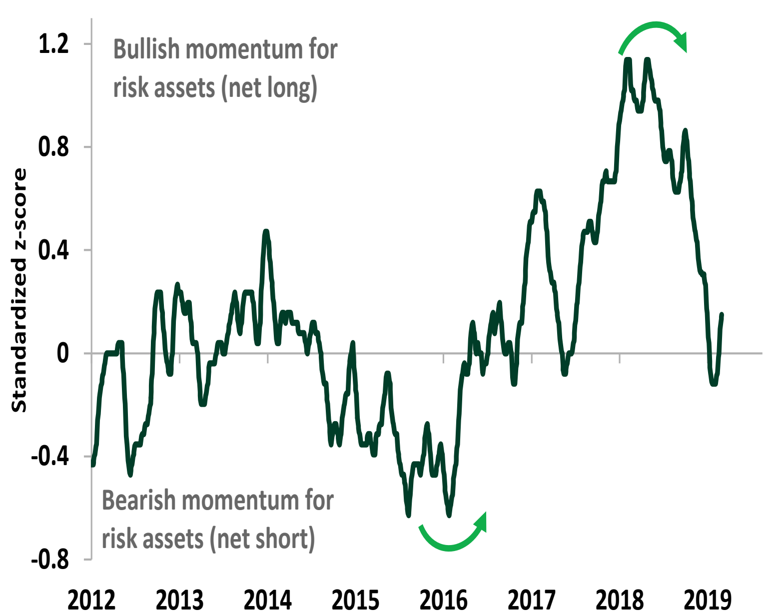
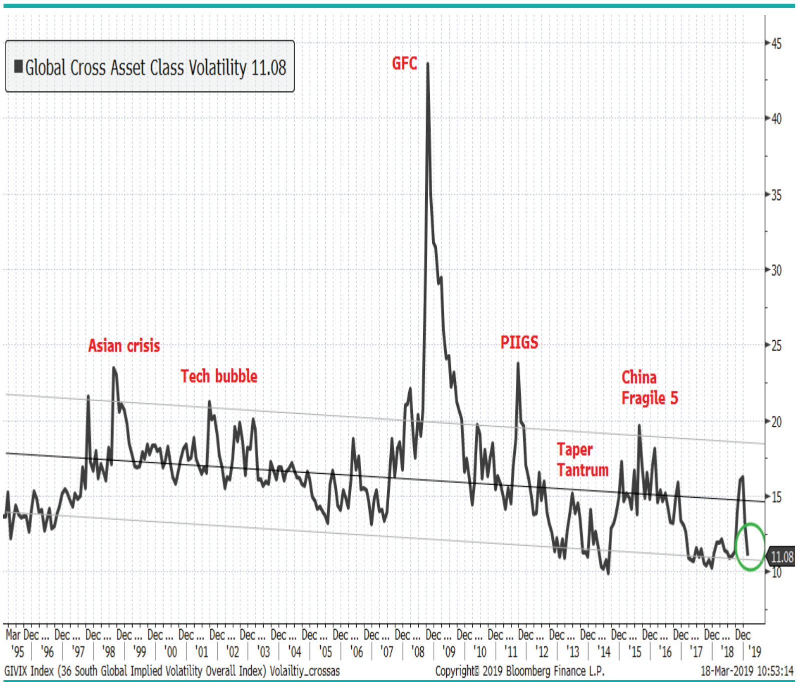
OUR REFLATION INDICATOR NEEDS A LIQUIDITY INJECTION



**Reflation position indicator is net long positions of SPX, Brent crude, copper minus long USD and short US 10-year; Source: DS, Nedbank CIB, CFTC*

- Our ***Reflation Indicator (CFTC net long risk assets)** is a representation of investor sentiment towards risk assets.
- This risk indicator was contracting through 2018 but reversed after the Fed's dovish pivot surprise. However, further improvement would depend on whether policy makers can reflate the global economy/financial system via easier global financial conditions. This will most likely require **a liquidity injection** and not just **"jawboning"**.

GLOBAL ASSET CLASS VOLATILITY: "STABILITY BREEDS INSTABILITY"



Source: Bloomberg, Nedbank CIB

- **Longer term:** One of the biggest unintended consequences of the central banks' ultra-easy monetary policy, in our view, has been the compression in volatility and risk premium. **As a result, the low volatility has fuelled risk taking and distorted asset prices.**
- **Central banks' (CBs')** primary job is consumer price stability, but since the 1990s, the markets have also required that the CBs ensure asset price stability. A credit-fuelled financial system is by nature a volatile system, but CBs kept policy rates below the Taylor rule for many years, helping to compress risk premiums and allowing more risk taking. This led to high debt levels and the perception that CBs are in complete control. We warn that CBs tend to be reactive and not proactive. Ultimately, sentiment and money supply drive financial markets and the global economy.
- **Global cross-asset class volatility (implied vol of bonds, commodities, currencies and equities)** is too compressed and complacency among investors is high given the macro headwinds the global economy is facing.
- Hence, our view remains that in order for financial markets to rally further, a liquidity injection is required and sooner rather than later.