STRATEGY NOTE:

EQUITIES

THE OUTLOOK REMAINS BEARISH

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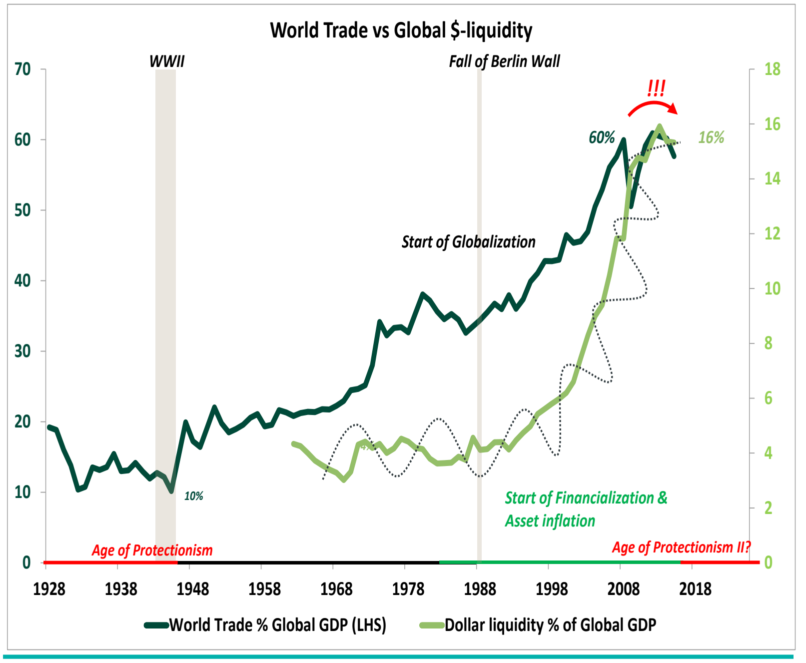
NEDBANK CIB

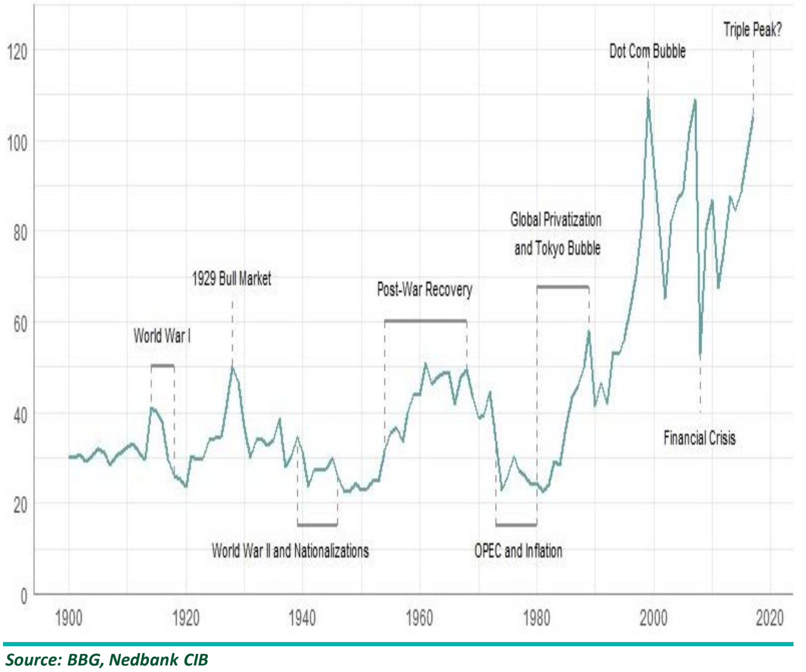
US DOLLAR MONETARY BASE AS % OF GLOBAL GDP



Source: Reuters, Nedbank CIB

- As we wrote in our special report on the dollar (Special Report: The US Dollar Is More Important Than You Think).
- Most investors understand that as the money supply explodes it will lead to higher consumer inflation as the value of money falls.
- Yet most equity investors believe the price of an asset is only derived from the demand and supply of the underlying product or service of that specific corporate.
- The change in money and credit and the price thereof has a major impact on asset prices. As the interest rates converged to the zero lower bound the changing quantum of money has become the dominant driver of asset prices and currencies.
- The dollar monetary base, which is basically the US trade deficit, exploded over the last 30 years. This growth has been a major contributor of asset inflation. Ask yourself, "how is it possible that assets can out-perform the GDP over such an extended period?"
- The global dollar monetary base has been contracting since 2014 and assets other than IT-stocks have failed to deliver any returns.

WORLD EQUITY MARKET CAP AS % OF GLOBAL GDP



Source: BBG, Nedbank CIB

- Simultaneous with the above trend of growth in the monetary base since 1988, the credit creation in the financial system evolved and bank gearing went up from 14 times to over 40 times.
- This explosion in money and credit triggered a break higher in this relative out of a 80-year old band.
- Unfortunately the highly geared financial system also made the markets very vulnerable to frequent shocks as is evident on this relative.
- The relative is currently close to the previous highs.

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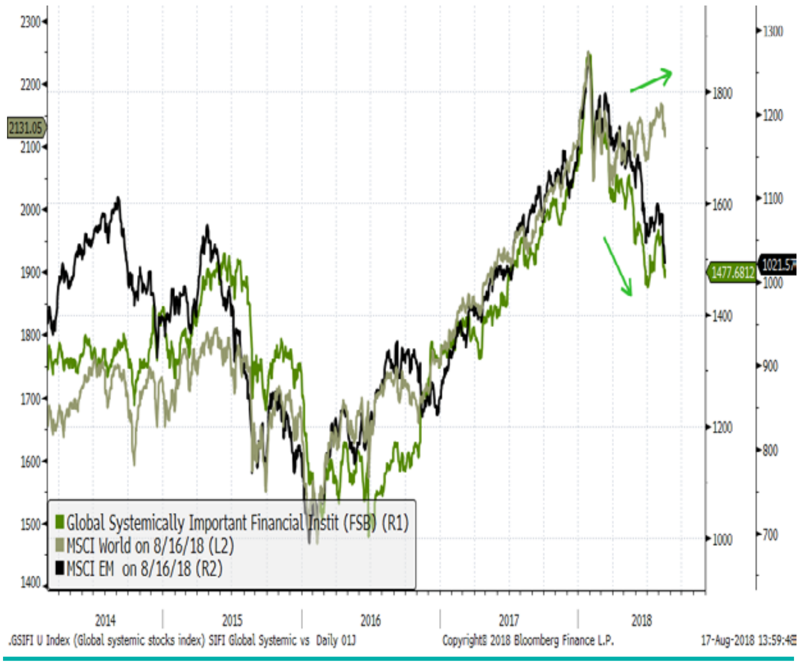
GLOBAL SYSTEMICALLY IMPORTANT FINANCIAL INSTITUTIONS (G-SIFI)



Source: Reuters, Nedbank CIB

- The first warning signal came in early 2018 when the market cap of the G-SIFI's started to correct.
- This is a strong signal that the velocity of money in the real economy and the velocity of collateral in the shadow banking system is falling. This is a consequence of the contracting $-liquidity which is also covered in depth in our special report on the dollar.
- The risk assets especially the EM currencies, bonds and equity markets responded immediately to this change.
- The world index has remained strong but this strength has an extremely narrow breadth as it just the FAANG stocks.
- If we strip the US and the FAANG stock out the DM equity markets it is also under pressure.

MSCI-WORLD WAVE B IS MOST PROBABLY COMPLETED

Source: BBG, Nedbank CIB

- The price action since the February low is too overlapping to be a bull trend. It is a major correction phase and it is not a question of if the market will break down out of this pattern, but rather a question of when.
- The price action is taking place around a very important resistance line from the 2000 high. A break below 2092 will confirm the rally above this line December and January was a false break.
- A break below 2092 targets a move to 1926 where wave C will be equal to wave A.

MSCI WORLD EX-US ALREADY TRENDING LOWER

Source: Reuters, Nedbank CIB

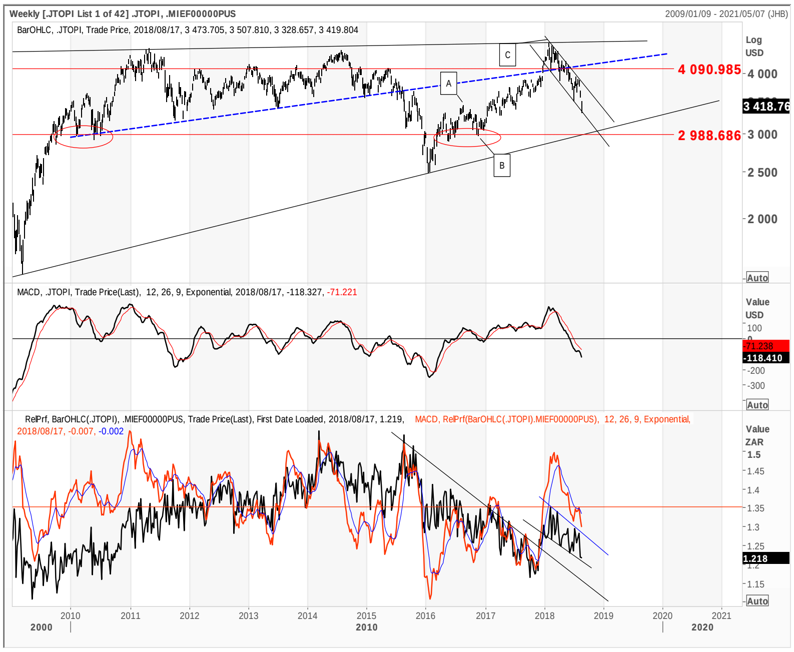
- The MSCI World ex-US Index is already forming a series of lower highs and lows indicating a bear trend.
- When the US markets runs out of steam, which we believe is not too far into the future (narrow leadership) this index will accelerate to the downside.
- Our target remains the bottom of the bear channel at 1762.

MSCI EM INFORMATION TECHNOLOGY INDEX HAS BROKEN DOWN

Source: BBG, Nedbank CIB

- The acceleration late last year in most asset prices was the blow-off phase of the liquidity fuelled bull market that started post the Global Financial Crisis.
- IT stocks were one of the major drivers of this acceleration phase. The break below the support lines at 512 now confirms the break above the well-established bull channel was a false break.
- This false break is in itself a confirmed sell signal. Our target for this correction is 410 and 376.
- The index is currently busy with a corrective rally. If the index fails at 512 it can be seen as a good-bye kiss and confirmation that the trend has reversed.

JSE TOP-40 IN USD IS NOW IN A WELL ESTABLISHED BEAR CHANNEL



Source: BBG, Nedbank CIB

- Foreign investors in the JSE have not made any returns since the 2011 high.
- We have to believe the market is targeting the major support line at 2988.
- Short-term the market is testing the support line of the bear trend and a short-term rally is likely. We expect this to come from a stronger rand and not just from the equity market side.

JSE TOPI WE EXPECT A BREAK TO THE DOWNSIDE OUT OF THE WEDGE

Source: Reuters, Nedbank CIB

- The counter-forces of the lower EM equity prices and the weaker rand has led to a wedge pattern formation. We however believe it is just a matter of time before the market breaks to the downside targeting the lows of 2014-2016.
- A break out of the wedge at 49195 below the previous highs will confirm the next wave to the downside has started.
- The MACD is also in the apex of the wedge and we expect the break to materialise within the next week or two. The MACD always break before the spot market. We will use this as an early warning whether our view correct or not on the direction of the break out of the wedge.

JSE RESI LIKELY TO BECOME A VICTIM OF THE FALLING COMMODITY PRICES

Source: BBG, Nedbank CIB

- The JSE Resi is grinding higher with the weaker rand but the MACD is not confirming these new highs.
- This divergence is an indication that the trend is losing momentum.
- The commodity prices has now fallen victim to the falling credit impulse in China and contracting $-liquidity.
- We therefore expect the Resi to top out at current levels for a correction phase to the bottom of the bull channel at 35 000.
- Our short-term outlook on Gold and Platinum stocks are more constructive as they will benefit from the weaker dollar we expect over the next few weeks.

JSE BANKS TARGETING 7500

Source: Reuters, Nedbank CIB

- The banks index is likely to consolidate between 9726 and 8757 as long as the dollar bull trend is taking a breather. But, as we have pointed out in all our FX reports, we expect another dollar bull phase later this year.
- Therefore we expect another wave to the downside (wave C) in the bank index to test the 38.2% retracement since the 2009 low at 7500. This level is also the support line from 2003.
- We would expect the major support at 7500 to remain intact. We however remain extremely concerned about the net shortage of dollars in EM banks which has grown from $500bn in 2008 to the current $1tn.
- If the $-liquidity conditions contract further EM banks will be under severe pressure, especially Asia.