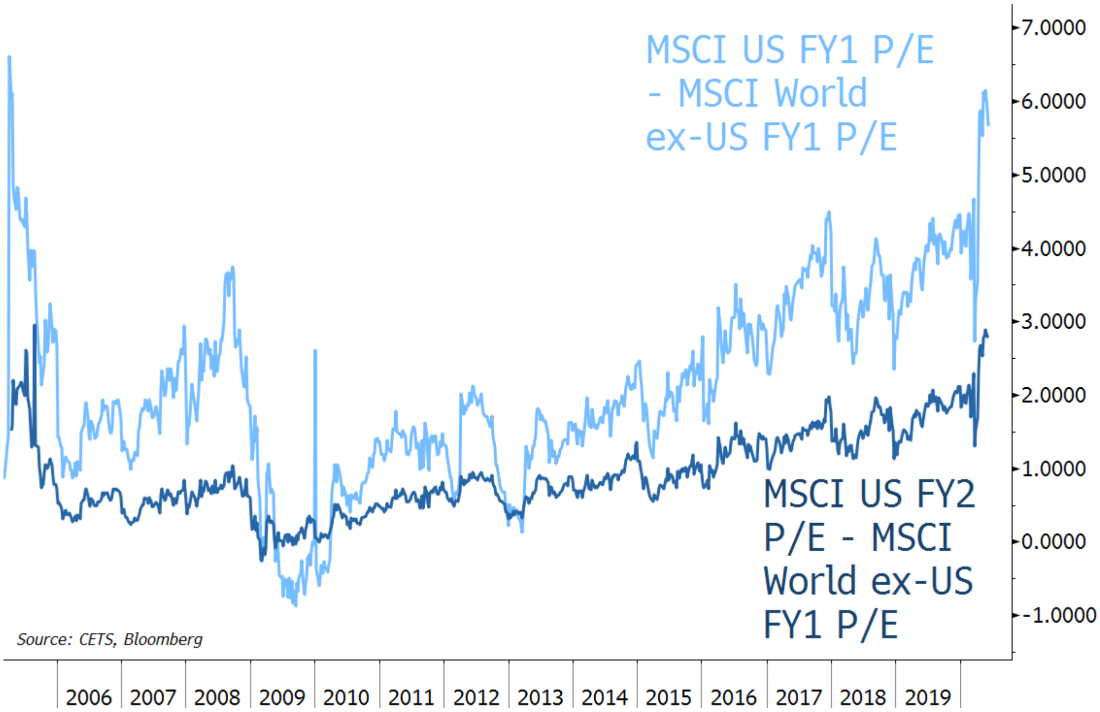
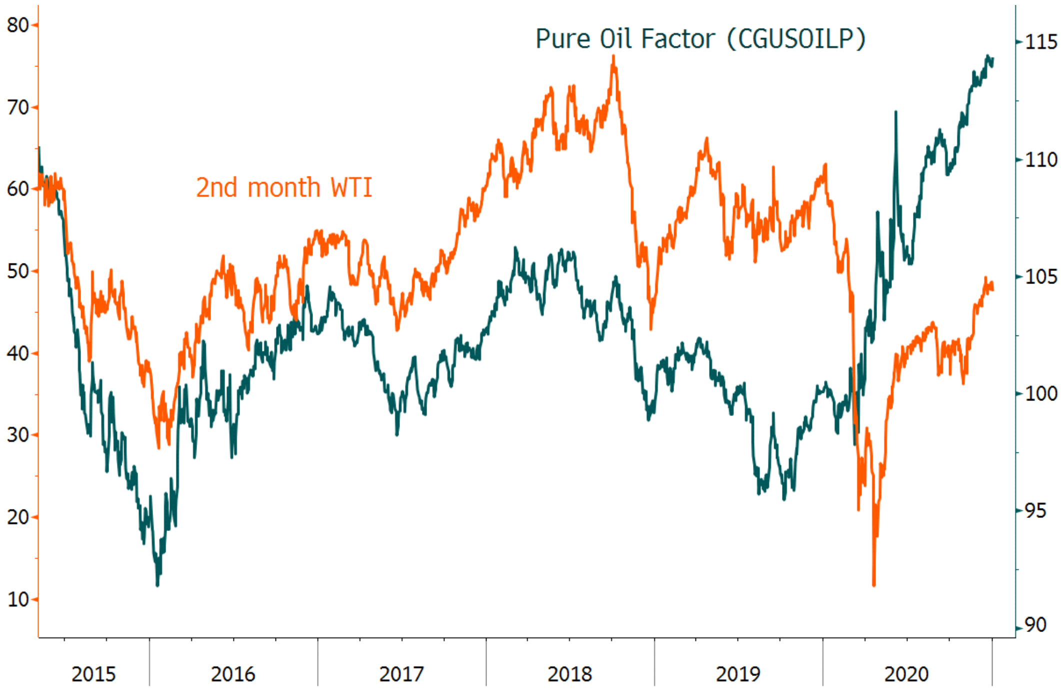
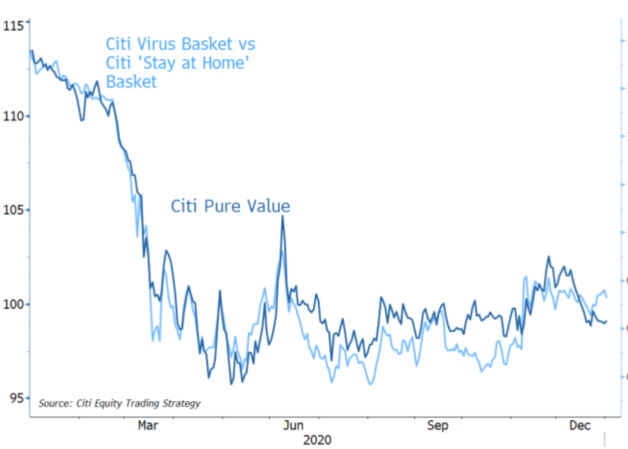
Happy new year everyone – I sincerely hope you all managed to get some quality downtime with your loved ones over the holiday period as we kick of 2021 with a bang. And I suppose the starting point for the year is one of tongue-in-cheek déjà vu as we grapple with a spreading virus, and tensions between Iran and the US start to escalate. Of course, the similarities between today and this time last year pretty much end there, with perhaps the largest difference being the contrast of financial conditions/monetary policy, as well as the overall market valuation; SPX trailing P/E is now on 29.5x (*on par with the peak valuation during dotcom*) versus 21x in Jan'20, whilst both the 1yr forward and 2yr forward P/E differential between SPX and *everything else* stands at the highest level since at least 2005.

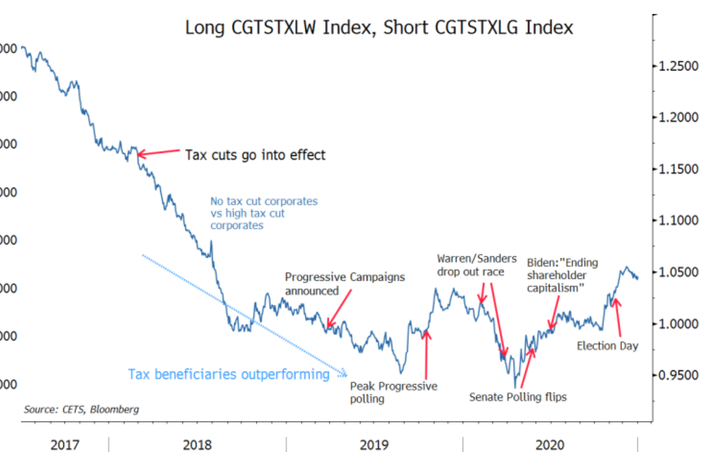


The best performer of the day was the Energy sector: +13bps, and the only sector in the green. Despite some sluggish performance during the back half of December, the sector remains the best performer over the past month (+4%) and past three months (+30%). I needn't repeat the themes and rationale as to why **this sector continues to appeal to me**, but I continue to note the sizeable dislocation between what our US Oil Factor is indicating as to the trajectory of oil prices over the medium term. And whilst today's price action may have been more a reflection of concerns over any Iran escalation (*although note that crude itself was down c2.5%*), there remains a medium-term story of consolidation and cost cutting for the larger names in the sector (i.e. XLE) even if some of the more **distressed energy companies** may ultimately perish during this cycle.

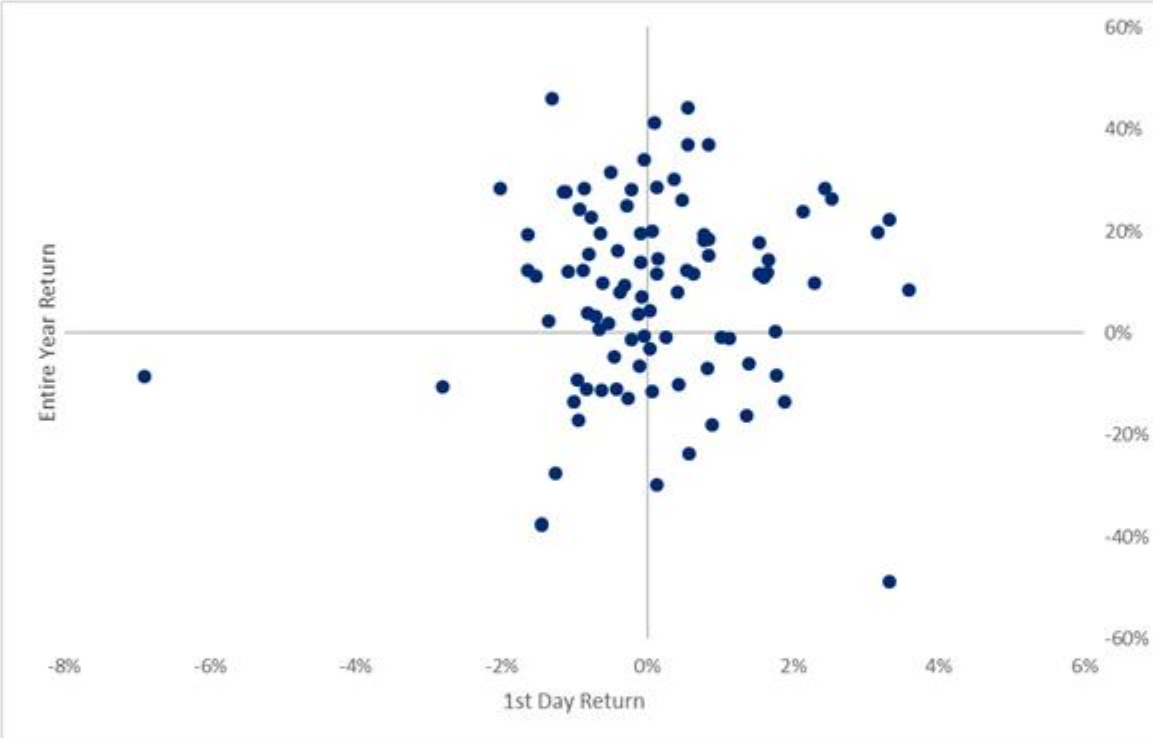


Much of today was spent undoing the damage of not checking emails during the two-week mandatory absence, so I did not a chance to check in with many of you. However, I did receive a several queries as to why markets took a 2% tumble, with speculation swirling around the resurgence of (mutated) COVID-19 strains hitting the US, through to nervousness around the Georgia runoff tomorrow, and potential retail selling in order to avoid the tax hit during the 2020 fiscal year. Truthfully, none of those really stack up in isolation, although perhaps at the margin it could have been a combination of all three factors: our Viral vs Stay at Home basket pair (**CGTSVRL2** vs **CGTSSTAY**) only moved approx. 0.7 stdev lower during the session, whilst our Senate 'blue sweep' proxy of the Tax winners vs Tax Losers (**CGTSTXLW** vs **CGTSTXLG**) was up a meagre 30bps (around 1 stdev). And as for retail selling, yes, Tech underperformed by 20bps today but it wasn't like the more speculative names were disproportionately pummeled, and the EV ecosystem names were mostly up on the session. Using some Alty mad maths, I could account for approximately 100bps of today's move on the above three factors (*even if the tax one is tenuous in my opinion*), and the rest perhaps a function of many investors still being 'out of office', even if both futures and cash volumes today were in fact pretty robust.





So what does SPX being down on the first day of the year indicate for the equity performance for the rest of the year? In a word 'nothing'. I've sadly been around markets long enough to see the speculative commentary being recycled that markets trading down on the first day of the year usually means we will have a poor showing in equities through to December, but the truth is that using almost 100 years of data has shown this stat belongs with Brian Fantana from Anchorman. Going back to 1928, we found that there is essentially no relationship between day 1 performance and the yearly performance, although our US Equity Strategy team continue to take a relatively cautious view on US markets in 2021, with the latest piece being found **here**.

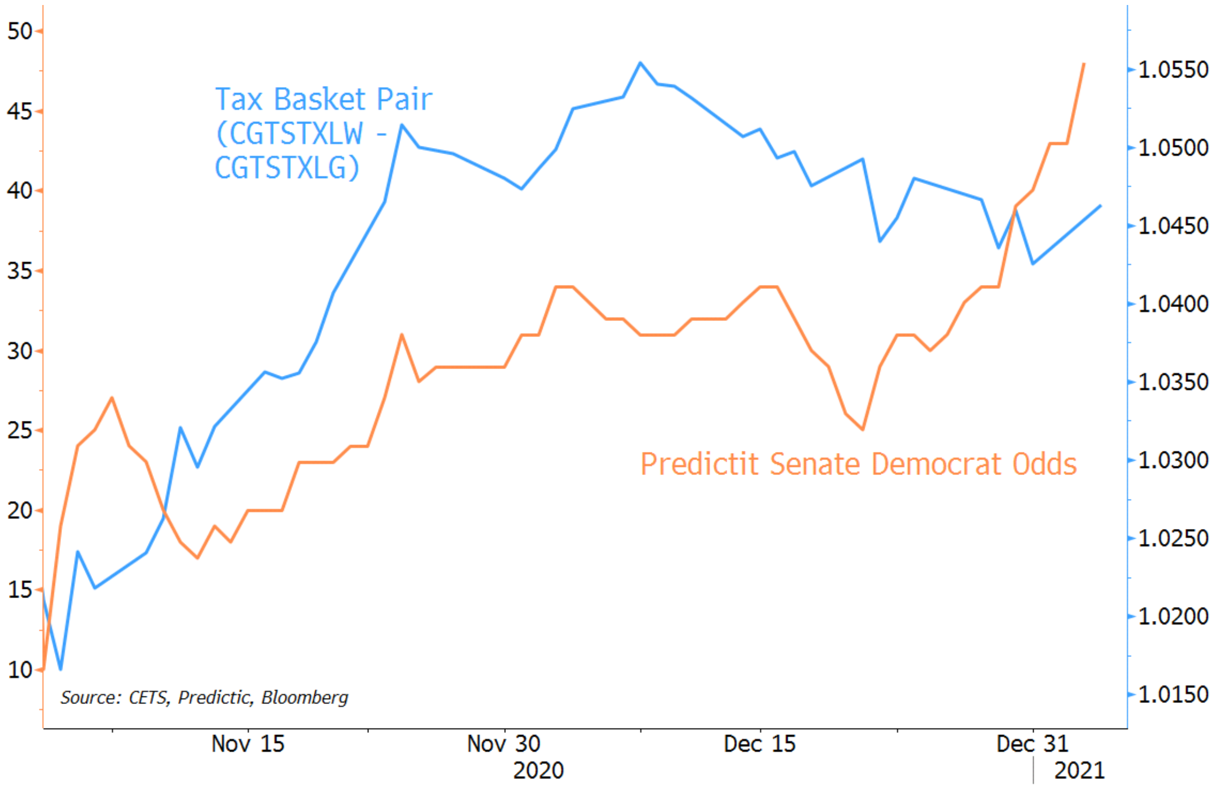


Source: Citi Equity Trading Strategy

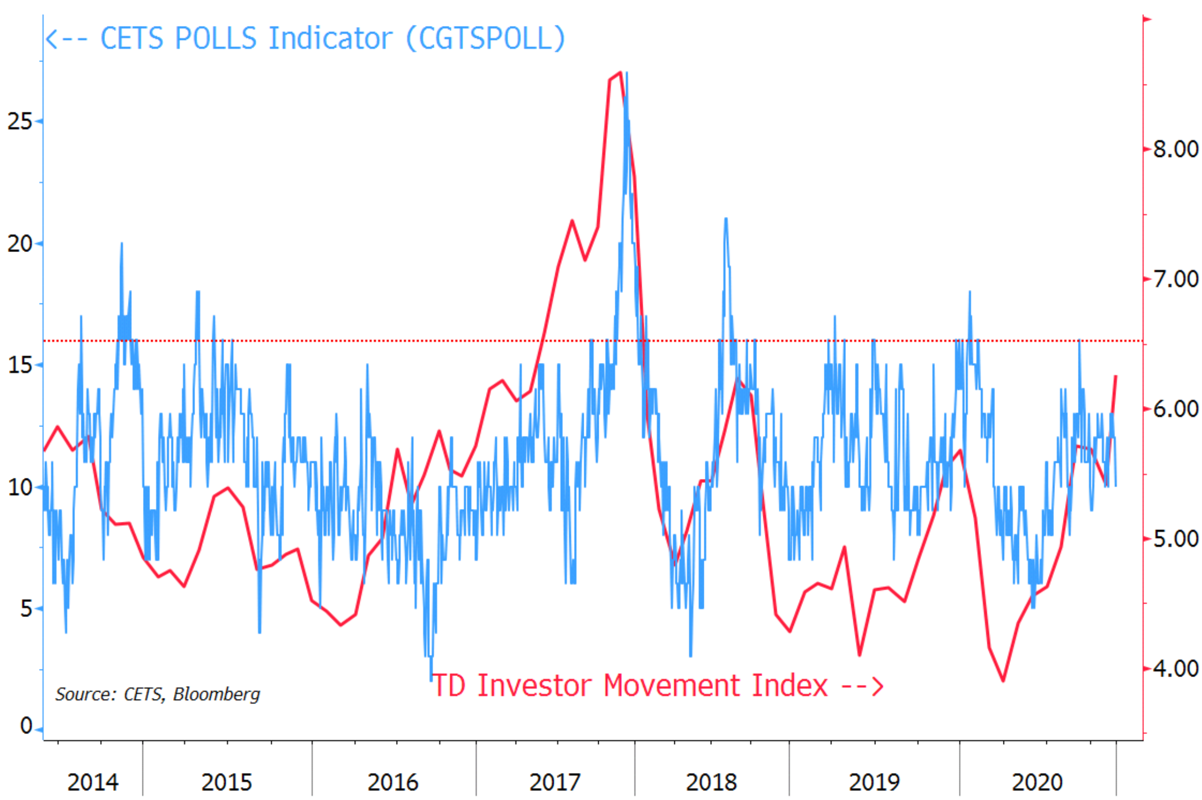
So on to this week's elephant in the room; the runoff election(s) tomorrow. In anticipation of some questions likely coming in, CETS assembled a quick FAQ.

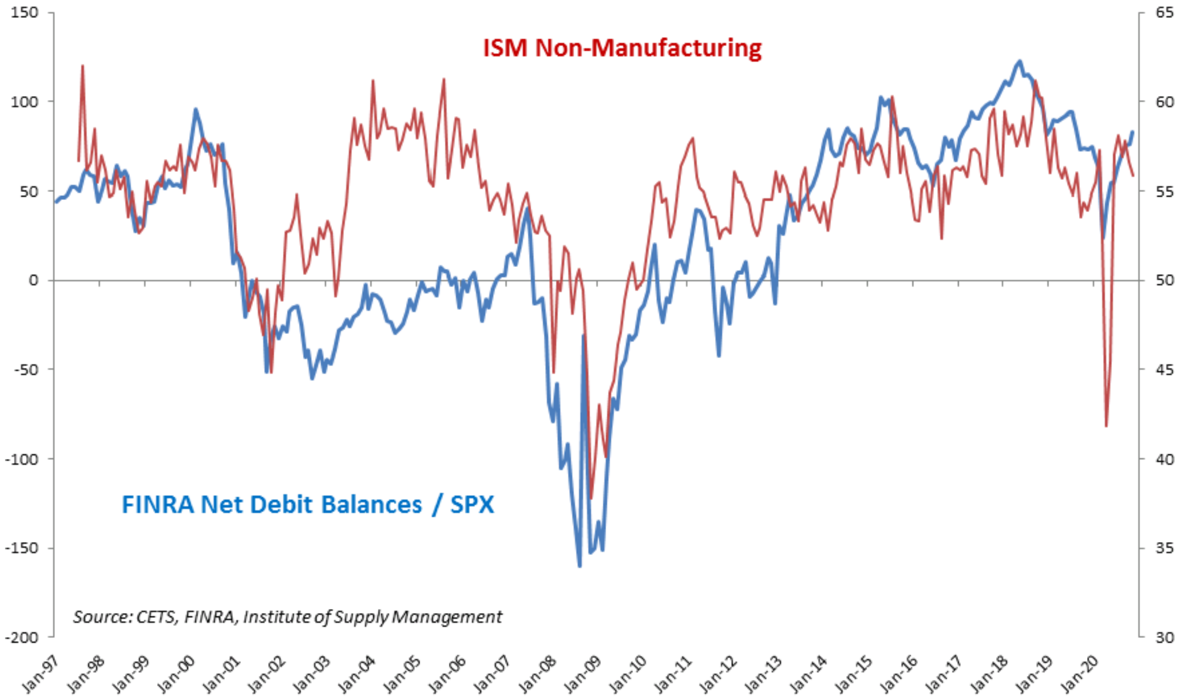
What time do polls open and close tomorrow? They're open between 7am and 7pm on January 5th
Where are the pollsters predicting, and where are the betting markets? Statewide polls have been patchy, but the average of current polls have Ossoff (D) leading Perdue (R) by 1.4pts, whilst Warnock (D) is ahead of Loeffler (R) by 2pts. Note both of these are well within the margin of error, so we can just call it a coinflip at present. Equally, the betting markets have significantly repriced the Democrat odds of taking the upper chamber, now at 48% versus 30% at my last update on the subject in December (see **Why are equities still pricing higher taxes?**)
How is turnout looking? **Enormous**. Three million early votes have already been cast, which is 1mm more than the total number of votes submitted in Georgia's last runoff, and equates to a 30-40% turnout district by district. Of that 3mm, two thirds are in-person early votes, and one third is early/absentee ballots.
What does the distribution of turnout tell us about voting intentions so far? From **data** provided, it would appear that African American votes have picked up by 3-4 points versus the general election in November. Turnout so far appears to be lagging in rural areas, although this can quickly change given GOP voters are more likely to vote on election day itself.
What is the recount threshold? 0.5%. Let's hope we don't have to do it three times…
When will we get a definitive outcome? With Georgia being one of the states that cannot count mail-in/early votes until election day itself, investors should brace for a mini-repeat of November; i.e. it could be 2-3 days before we get a definitive outcome (and longer if recounts are required). Given the **leaked call** between Trump and Raffensperger over the weekend, we should at least expect GA authorities to attempt to make the counting process as quick and transparent as possible.

As mentioned before, our tax basket was up on the session but has lagged the recent shift in betting odds. I would expect this basket pair to continue to perform well over the next couple of sessions if the market continues to reprice the Democrat odds in Georgia.



Lastly, just a quick update on positioning as we start the year as we enter a period with election and Brexit uncertainty behind us (*…sort of…*). A quick check on our POLLS model is still showing a pretty contained reading of 10 (versus 16 needed for us to get nervous), although corroborating that with things like **systematic CTA positioning** (*that is now max long and within 3.5% of the first sell signal to the downside*), and retail positioning that now appears to be the most long since Sep'18 in outright terms, I do not think it would take much to tip the scales for our POLLS model to move up into danger territory here. As a reminder, Research Strategy's Panic Euphoria model reached the highest level *ever* back in December, and remains at levels last seen during the height of the dotcom boom.





Good luck this year.

Alty

Alexander Altmann

Head of US Equity Trading Strategy

Office +1 212 723 1999

Market Commentary and a not a product of Research. Intended for Institutional use.

All charts/data sourced from CETS, Bloomberg and Citi, unless otherwise indicated.