Although still on mandatory leave last week, Friday's price action was enough to jolt both me (and seemingly many investors) out of peaceful slumber, even from a poor cellular signal corner of Mexico apparently. Jimmy covered both the price action and de-grossing exercise in several missives last week, and whilst I am exercising the right to be patient in ramping up thoughts post a two-week absence, there are a few standout points worth flagging on day 1 despite the fact that SPX is within 20pts of where I last wrote an EOD:

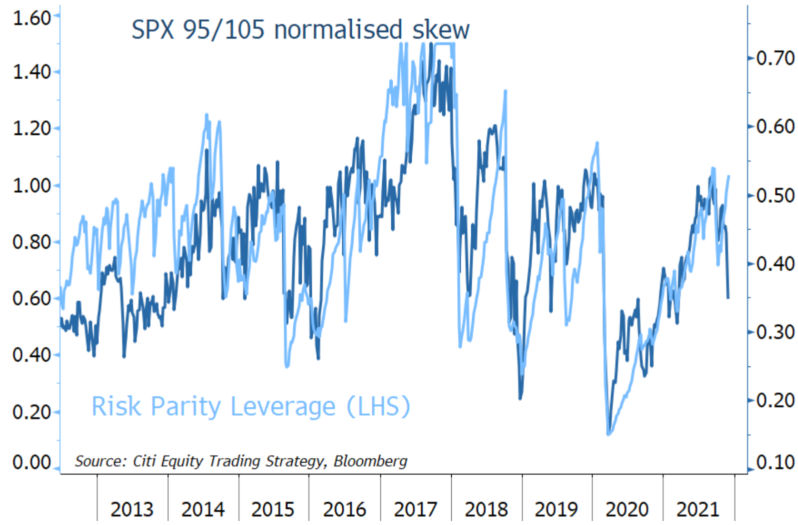
1) **POLLS was flashing a warning level of complacency back on 10th November (with a negative SPX return since – see [The POLLS warning is back]) and has now hit a level of 16 again after today's close.** The hit rate/return dynamics can be found in the above link from earlier in the month but the fact that this model has not moderated illustrates that the market dip on Friday may be less of an opportunity than today's knee-jerk response suggests. The current POLLS model composition can be found in the table below, which to me is illustrating an ongoing degree of positioning extremity that still leaves equity markets vulnerable to liquidity-driven downside shocks, most likely from exogenous headlines (such as Friday**). The second illustration below shows that risk parity leverage is virtually back to pre-September levels – a stark contrast to the usual pattern of tracking SPX index skew – and reinforces the view that systematic equity positioning remains elevated despite Friday's price action.**

Complacency again elevated with POLLS at 16

Current Level: 16			Recent Market Peaks				
	29-Nov-21	22-Nov-21	Sep '21	Oct '20	Caution	Danger	Description
Market Indicators							
% Rally in 21 Days	1.5%	3.0%	2.3%	3.8%	2.2%	5.9%	
Vol/Spot Correlation	6	6	4	5	3	5	# of vol up spot up days in last month
ToB Liquidity % Rank	76%	78%	93%	50%	20%	10%	Percent rank based on 12-month lookback
CDX HY % Rank	99%	98%	6%	17%	20%	10%	Percent rank based on 6-month lookback
Probability of Default % Rank	76%	55%	89%	3%	70%	85%	Percent rank based on 6-month lookback
Real Yields % Rank	28%	50%	19%	33%	80%	90%	Percent rank based on 6-month lookback
Low Risk Factor % Rank	62%	36%	84%	6%	80%	90%	Percent rank based on 6-month lookback
Data							
US Soft - Hard Data	Positive	Positive	Positive	Positive	Negative	Negative & Falling	Differential between CESI Hard - Soft dataset
Sentiment							
Levkovich Index	1.41	1.39	0.98	0.69	0.3	0.38	Research Strategy Composite Market Indicator
VXX Rolldown	0.0625	0.5625	1	0.25	0.5625	0.25	Does not prefer rolldown
Vol Indicator	33	33	17	-33	-33	0	Neutral
CGUSOVER	-29	-24	-1	-1	60	75	CETS Proprietary Overbought/Oversold Indicator
Positioning							
Mutual Fund Beta	1.02	1.07	0.87	1.06	1.1	1.2	Beta of Aggregate Mutual Funds to SPX
Hedge Fund Beta	1.02	1.14	0.90	1.16	1.15	1.25	Beta of top HF holdings to SPX
Short Interest	0.7%	0.7%	0.8%	0.8%	1.4%	1.3%	% of SPX Market Cap that is held short
CTA Positioning	24.6	26.6	18.0	18.0	15	21	$ Notional SPX Length
CTA Distance from Sell Signal	2.5%	3.9%	3.9%	3.0%	3.0%	1.0%	% move lower required to trigger CTA selling
Financing Rate	39	39	37	14	20	30	S&P 3mL financing rate
Net Short Vega Positioning % Rank	38%	38%	55%	100%	80%	90%	CFTC Net Non-Commercial VIX positioning
Signals							
Caution	2	2	4	6			
Danger	14	12	12	10			
Total Warnings	**16**	**14**	**16**	**16**			
Total Warnings %	**42%**	**37%**	**42%**	**42%**			

Source: Citi Equity Trading Strategy

Risk parity leverage did not decline last week and leaves equities vulnerable to downside shocks



2) **Omicron is a slow-burn story that lacks identifiable catalysts but the forthcoming DC agenda (government shutdown, debt ceiling, budget reconciliation) may be more urgent with a hard timetable during December.** Is anyone talking about this? I get it, the past few days have illustrated that the world is still living with the aftershocks of a pandemic earthquake, and that the initial thesis eighteen months ago of a '90% Economy' may ultimately prove to still be holding water as parts of society remain unable to entirely return to normal. However, whilst there may be much hand wringing over vaccine efficacy or transmutability, market participants are ultimately at the mercy of health officials' rhetoric and knee-jerk government responses, which makes the narrative extremely difficult to trade. On the other hand, the issue of passing another stopgap measure (Dec 3 deadline) to avoid a government shutdown, or raising the debt ceiling ahead of Yellen's Dec 15th deadline (which **our economists** believe is closer to Jan 3rd in reality) are real events that equity markets may decay into. Recall September saw this kind of price action and the POLLS model may actually be sending a risk signal around these catalysts, rather than specifically COVID-19 variant risk.

December

Dec 3:
- Current government funding extension expires; Deadline for Congress to pass either another continuing resolution or new funding legislation to avoid government shutdown

Dec 15:
- Treasury Secretary Yellen's estimate for when the nation will exhaust its use of 'extraordinary measures' to fund debt obligations

Dec 24:
- Loose deadline for lawmakers to pass Biden's ~$2trln tax and spending bill in the Senate ahead of the holidays

January

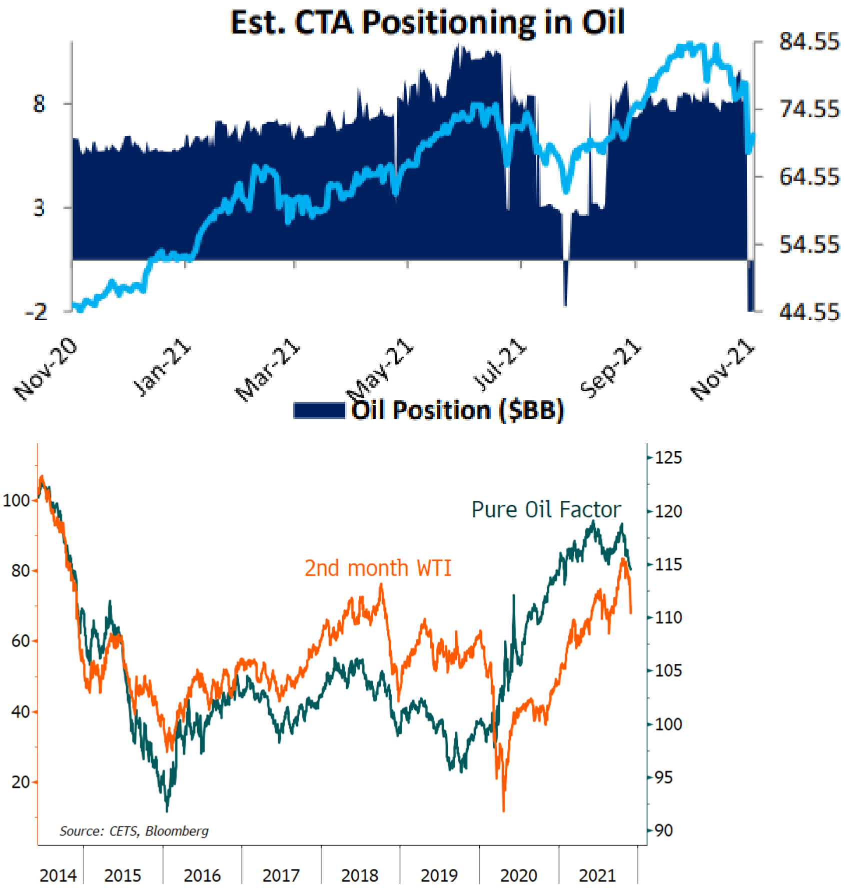
Jan 3:
- Citi US Economists' estimate for when the Treasury will reach its debt limit under the Oct 14 increase

Source: Citi Equity Trading Strategy

3) **Oil and OPEC – is the production quota already priced?** Given the SPR announcement by the Administration during my absence, OPEC's meeting this Thursday has garnered more attention in anticipation that the cartel may curb back their production quota increase. Indeed, my Energy colleague, Mike Matus, conducted a quick survey this afternoon to get a pulse of what is expected in terms of output and the overwhelming majority of responses expected no additional barrels to be added in January (presumably exacerbated by Omicron newsflow as well). So is it in the price? Well the good news is that our **CTA model** has now flipped net short in CL1, suggesting that some of Friday's price action was driven by systematic selling rather than a structural shift in oil demand, and should provide a degree of positioning support for the black stuff. The bad news is that our Oil replication basket (the Oil Factor) is back at the lowest level since February, somewhat confirming a view that

crude prices may actually struggle to make gains from here; admittedly the ‘basis’ between the equity interpretation and actual WTI moves can be extremely large (see 2018 for details), but the turning point in the factor is worthy of mention.

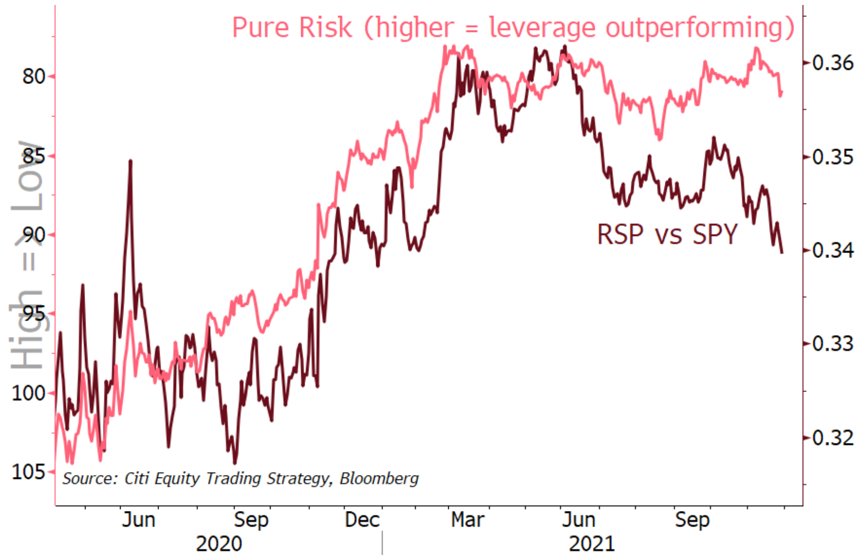
Short systematic positioning helpful for crude into OPEC, but equities are starting to take a less positive structural view on WTI



Source: Citi Equity Trading Strategy

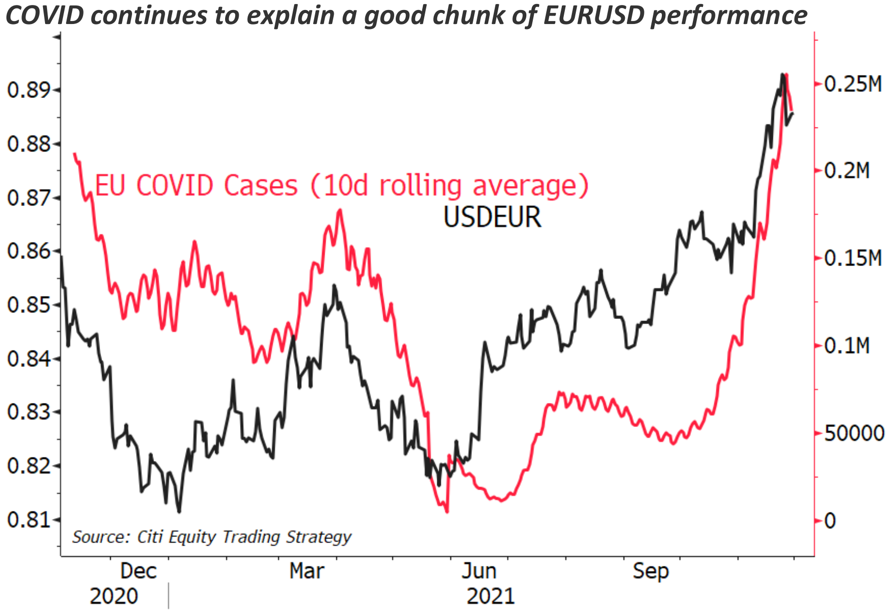
4) **Breadth is rubbish. But you already knew that.** No ‘return to work’ email would be complete without a mention on market breadth that was falling well before Friday’s selloff. Even today’s rally was accompanied by negative breadth and is reinforcing the above message from POLLS that not is all calm below the surface of equities at present. You would have no doubt seen several illustrations of degrossing via crowded HF longs vs shorts being unwound, or the meaningful bid to Quality at the expense of, say, small caps (*that are trading at the lowest relative level to SPX since the vaccine announcement this time last year!*), over the past week, but probably the best illustration of the narrow leadership in the market is simply looking at equal-weighted S&P500 (RSP) vs cap-weighted (SPY), which is now at YTD lows.

Breadth has deteriorated during November. Small caps have been especially hurt.



5) **USD and COVID – this chart continues to do all the talking.** My FX colleagues can articulate a much better view on their reasons to be bullish USD (see here), but having refreshed a *lot* of charts, I found the ongoing relationship between the overall change in European COVID cases as providing a helpful explanation for broader FX behavior. If you squint a little you can actually see an inflection in rolling EU COVID cases, which may provide some respite to recent EUR weakness, subject to Omicron evolution.

COVID continues to explain a good chunk of EURUSD performance



So that's a lot of unfiltered thought, but you'll forgive me after two weeks of ring rust. The bottom line for me is that the POLLS model is stopping me from suggesting buying this dip just yet, despite the aggressive calls of December seasonality. We may yet see a Christmas rally (*but maybe not a Chanukah one…*) but investors may well have to digest both the omicron *and* Washington headlines before a more healthy rally can resume. One thing that is quite apparent is that much to the chagrin of many investors, we may not have a quiet run into yearend…

Alty

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