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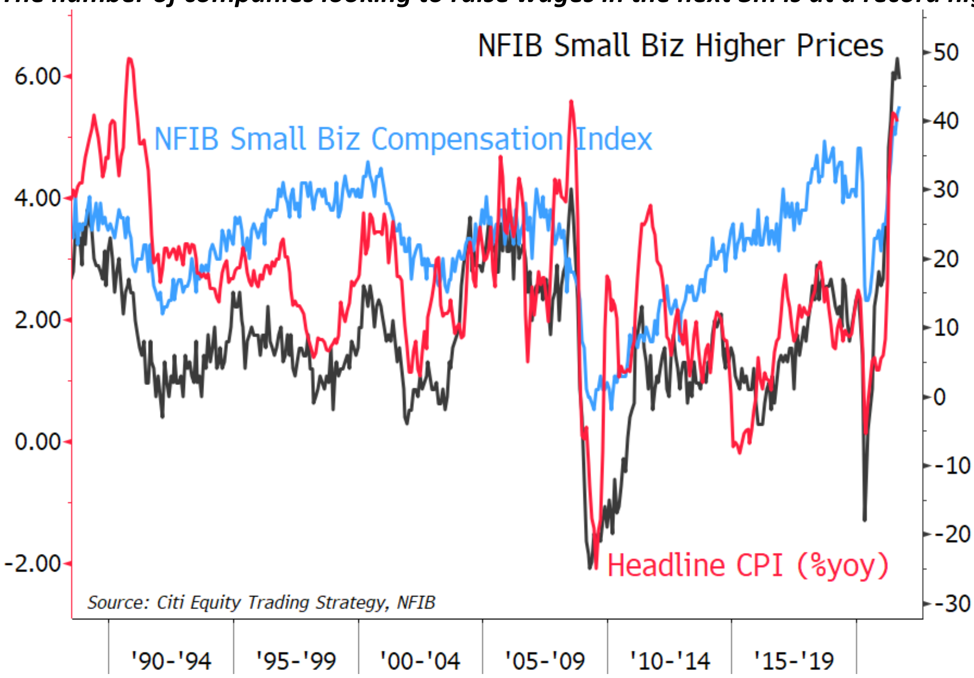
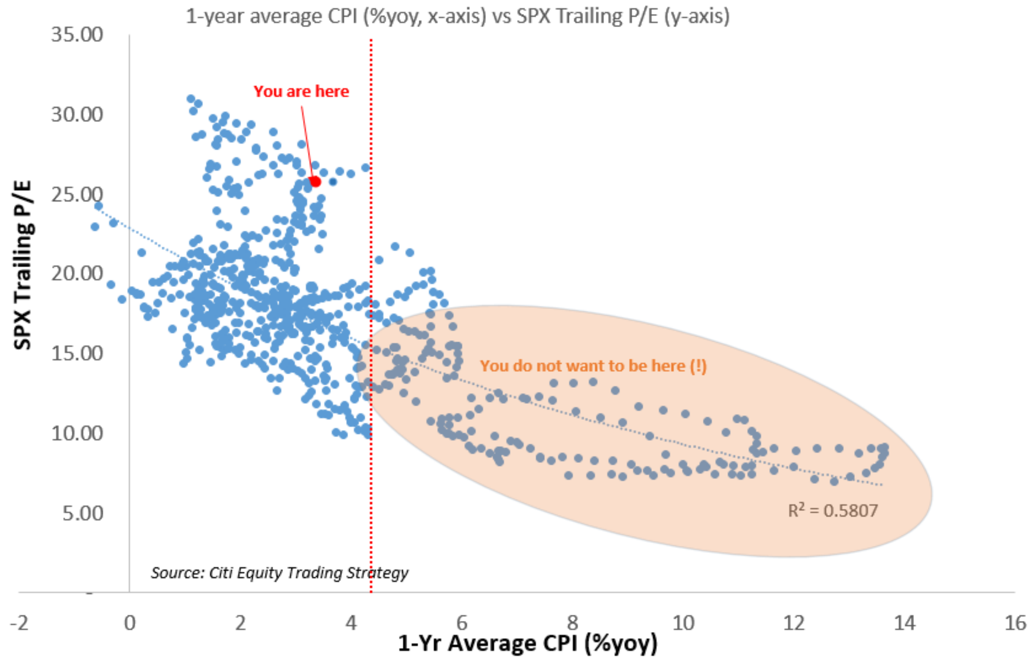
The brief hiatus in EOD since last Friday has had more to do with a lack of real incremental drivers more than anything else, and today was ultimately an extensive of that (non)narrative: SPX is ding dong unchanged over a rolling five day period, despite the 3-session consecutive losing streak. However, despite the poor showing of Value (-80bps today), sector leadership continues to be definitively pro-inflationary with Energy, Real Estate and Materials all featuring as market outperformers, and going some way to reinforcing the somewhat subliminal message that equities have been sending for most of 2021; **inflation is hanging around longer than we all think.** If today's NFIB data was anything to go by, then the good news is that plenty of employers will be dishing out some pay rises in the coming 3-6 months…

The number of companies looking to raise wages in the next 3m is at a record high



Source: Citi Equity Trading Strategy, NFIB

We obviously have CPI (and Fed Minutes) tomorrow, although with consensus already expecting a 5.3% headline YoY print and 0.3% MoM, it may be a tall order to expect any kind of upside surprise from these numbers; SPX one-day straddles were priced at c60bps during today's session, so it would appear that there's little that can really rattle the market from an inflation narrative currently, and with a proper two-way pull with regard to the 'transitory vs sticky' debate that will unlikely be resolved before the end of the year, investors are stuck looking for other clues as to how markets should respond to the current paradigm of higher prices. Here's a tip (chart) from the note sent earlier today: if inflation is still printing 5% by year end, then it would be enough to tip us into a 4% trailing 12-month CPI environment, and that's not exactly a great setup for the market multiple into 2022 and may erode some of that EPS momentum next year.



On the above basis, I can understand not only why many client conversations express a high degree of caution at present. Indeed many have openly mentioned how they either have, or are in the process of de-grossing in light of the current Q4 'wall of worry', or indeed the 2022 outlook. I admit there is a difficult juxtaposition of an inflation narrative that can depress an equity multiple versus **a current tactical bullish bias that CETS carry**, and yet it is *because* of this conservative positioning dynamic and the depressed market sentiment currently that ironically creates a more constructive near-term backdrop for markets. We have Q3 results starting in earnest this week with the Banks reporting, and as my CETS colleague Kai Lu highlighted in a separate **note** published yesterday, the reset in earnings expectations and nervousness around supply-chain bottlenecks is arguably already somewhat discounted into parts of the market.

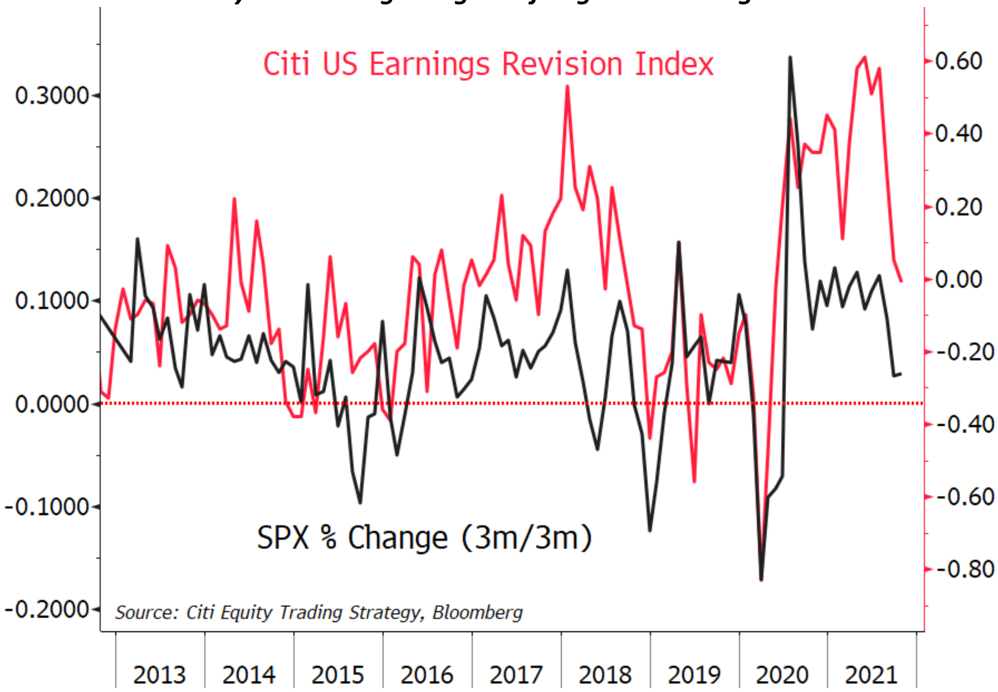
Expectations for earnings both QoQ and YoY are already quite low

Expected Earnings Growth vs Prior Periods	YoY 3Q21E vs 3Q20	QoQ 3Q21E vs 2Q21	Pre COVID 3Q21E vs 3Q19	vs Rolling 4Q Avg	3Q21E 4wk Change
SPX	24.5%	-6.9%	15.6%	6.8%	3.7%
Energy	#N/A	24.5%	52.3%	238.2%	2.7%
Materials	89.0%	-3.5%	86.1%	38.0%	-3.0%
Industrials	78.9%	3.3%	-10.9%	41.7%	11.0%
Information Technology	27.7%	-2.7%	39.1%	4.7%	0.3%
Communication Services	25.7%	-10.4%	30.3%	1.3%	-41.4%
Financials	17.6%	-23.8%	7.8%	-11.8%	14.8%
Health Care	10.0%	-5.6%	21.2%	3.4%	1.4%
Real Estate	7.8%	-7.6%	0.0%	0.8%	9.3%
Consumer Staples	1.6%	1.1%	9.4%	4.4%	-3.7%
Utilities	-1.7%	36.6%	-0.4%	25.8%	1.5%
Consumer Discretionary	-13.2%	-16.3%	-14.1%	-7.6%	2.2%

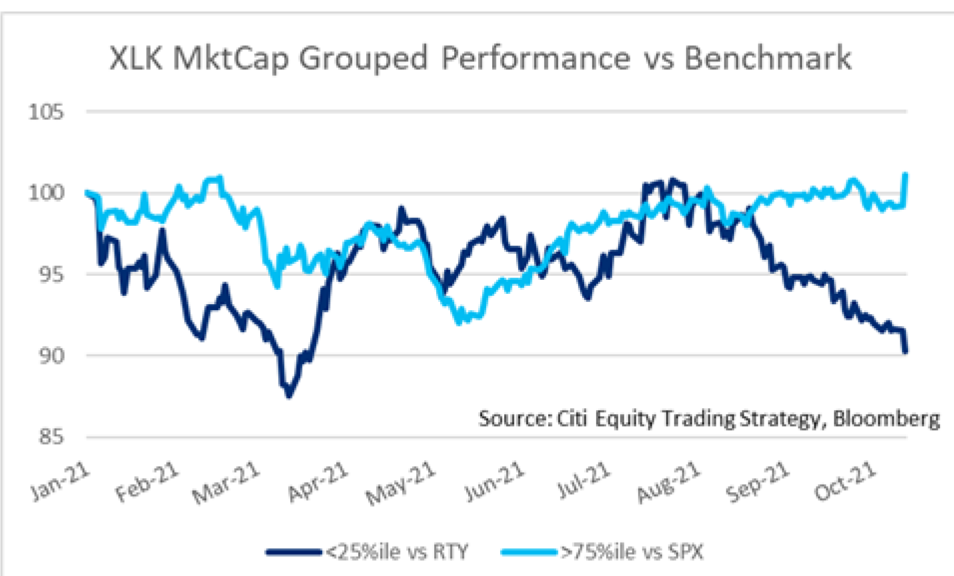
Source: Citi Equity Trading Strategy, Bloomberg

Moreover, if we examine the *net* earnings revisions in the US market at present, they are already recording the first negative readings since spring of last year. I suppose that could be spun as a positive or a negative in its own right, but if we compare the evolution of EPS revisions versus the change in SPX returns (chart below) then one could easily reinforce the argument that equities have already discounted this latest wave of negativity. I mean, even AAPL's **iPhone supply issue** is not exactly a shock to the investment community when it was already telegraphed before the phone had even been released.

Markets are already discounting a degree of negative earnings revisions



Lastly, I have received several enquiries over the past week as to why despite all this mooted rotation, we have yet to see Tech sell off in a meaningful way. To which I would like to provide two answers. Firstly, when Tech represents 28% of SPX (*and arguably closer to a third of SPX if we include parts of Comm Svcs and Discretionary that are 'tech' like*) then investors face a simple quagmire of 'what to buy?' if they choose to underweight core components of the broad index benchmark. Case in point; if an investor sold their entire AAPL stake (6% of SPX), then even owning EVERY energy company in the broad benchmark would only utilize 50% of their cash (!) Secondly, because these tech companies are such massive index weights in both the SPX and the GICS1 sector (*AAPL and MSFT combined occupy 43% of XLK*), it somewhat masks any behaviour that is going on at the tail end of the spectrum. If we break down the Tech sector by market cap (>75th %ile vs <25th %ile) to see if there is actually a degree of rotation going on, and then compare average performance versus an equivalent large cap/mid cap benchmark, it is quite clear to see that there is rotation happening as smaller (less profitable) Tech is being used as a source of funds, rather than the mega-cap names that continue to represent core holdings in many portfolios.



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