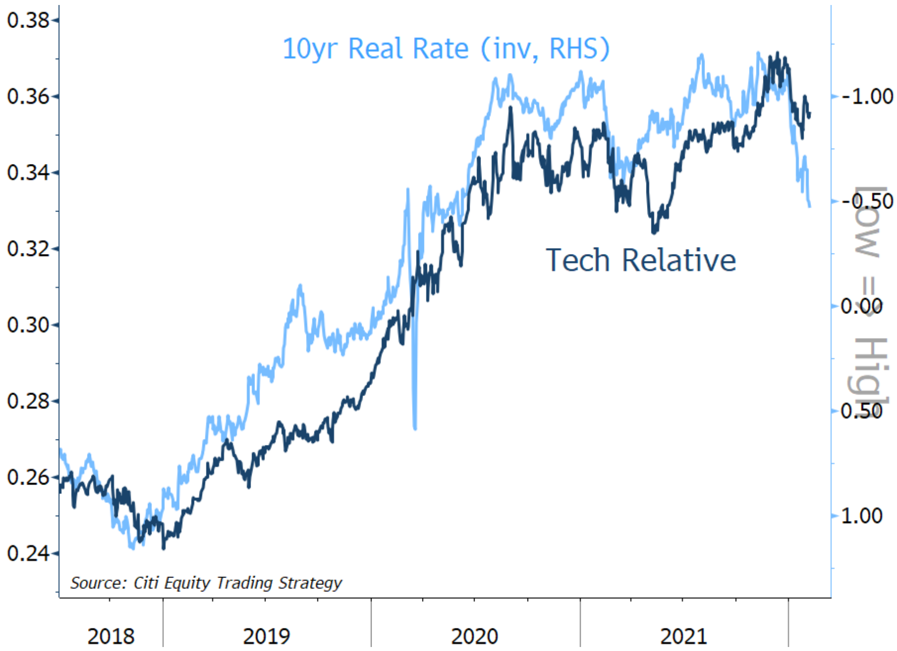
By virtue of the number of enquiries today along the lines of '*why are we going higher?'* is probably sufficient anecdotal evidence to support why markets…went higher. There is plenty of data to suggest positioning (and indeed sentiment) are towards the lower end of historical ranges, and although this author **pulled away** from a conviction bullish view on markets at the end of last week, it was caveated that low liquidity + vol in the 20s is still a recipe for index overshoots in either direction. That's certainly what **Citi's Technicals team** believe too.

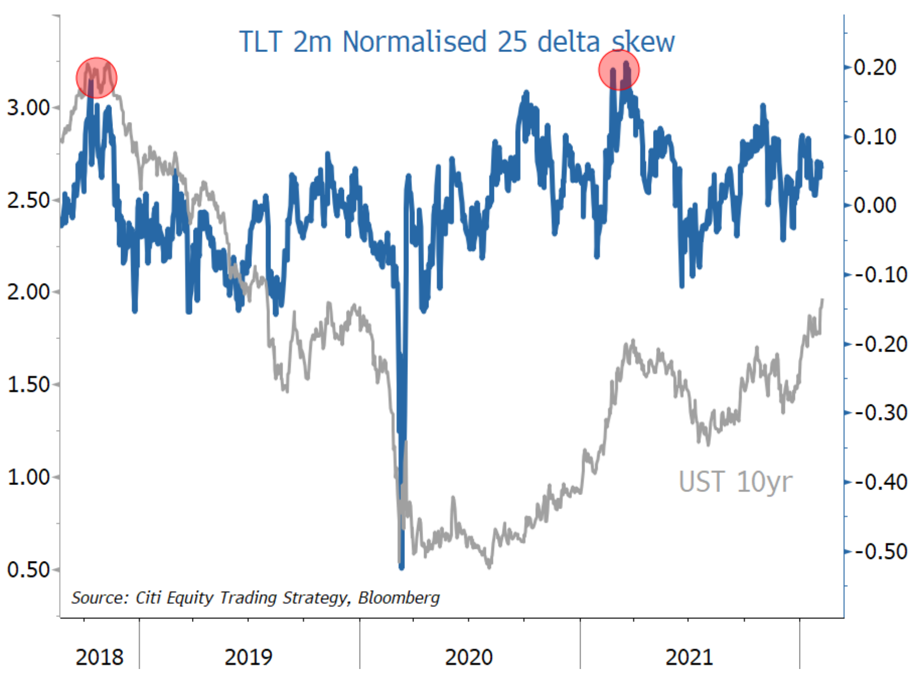
It is understandable that investors would be reticent to build back into risk positions here. Notwithstanding the prevailing levels of index/sector volatility that prohibits larger capital deployment, factor vol continues to be stubbornly high too. Ironically the most encouraging aspect of this is in the realm of Low Risk (**CIISLRUT Index**) that fell a mighty 100bps during today's session, pulling the index down to the 64%ile of last six-month observations, although I would caveat that the index has observed 10 days of 1% moves or more over the past two months, and that has only been seen during the GFC… so perhaps take the recent drop with a slight pinch of salt, even if it will likely provide some short-term respite to US equity indices.

The move in Low Risk may be supportive to US indices in the near term

But the counterpoint to all this – and perhaps a consideration more as a Post It to keep on your desk rather than an actionable trade today – is that against the backdrop of light positioning and poor investor sentiment is the reality touched on **yesterday** that the march higher in real yields creates an ever-growing headwind to the path of the broader equity complex. Since this topic was mentioned under 24 hours ago there need not be an extensive repeat at this juncture, but the fact that real yields continued to rise to fresh 18-month highs today defies more the fact that NDX/Tech/Growth has managed to stabilize the relative performance against SPX when any kind of metric suggests it this cohort of the market should still be materially underperforming. Whether this is a market conundrum at present, or just a timing issue for investors needing to be patient is left to the judgement of the readers for now, but it is certainly an anomaly that I am struggling to reconcile.



One argument that could be made is that we're at the point of peak bearishness for long-end USTs and that real yields may have topped out near term as we approach 2%. I'll leave the more nuanced aspects of this argument to my rates colleagues (who have a target of 2.25% in 10s anyway), but from this perch that argument does not really stack up. Yes, 2% may be considered a psychological/temporary barrier for 10y USTs but I would personally consider the zero bound for Bunds a far larger one… and look how that **turned out**. Moreover, from a positioning perspective – and I believe my colleagues in Rates Strategy would agree with me on this – UST shorts are far from crowded, as evidenced by 10y swaption skew, or TLT skew as a rough-and-ready proxy. You can see from the chart below that the current move in yields has not been accompanied by an aggressive shift in 25 delta options pricing (unlike Q1'21, for example) and so from this angle it is hard to argue that this move in yields is ripe for a near-term correction, absent surprises via Thursday's CPI or something of the like.



That prompted a refresh of US sector and ETF sensitivity to changes in both nominal and real yields. The table below is not new and has been used extensively in these columns over the past year, but serves as a reminder that even on days where both XLE and crude drop 2% (*on some Franco-Russian* ***headlines*** *that immediately prompted a re-watch of a recently-released Netflix wartime movie featuring Jeremy Irons*), investors who still believe in a path higher for nominal/real yields will continue to find a degree of insulation in areas like Energy, Financials, and even SMID (aka Value). These remains the areas that should prompt legitimate dip buying in a world of higher interest rates and/or continued Value outperformance, and indeed that's exactly what we have finally been seeing since the end of last year.

		Sensitivity to 10y Nominal		Sensitivity to 10y Real		Sensitivity to 10y BE	
Ticker	Code	Beta	Rank	Beta	Rank	Beta	Rank
S5ENRS Index	Energy	20.6	1	18.3	1	19.7	1
EWZ US Equity	EWZ	9.8	2	6.7	5	11.2	2
S5FINL Index	Financials	9.7	3	10.4	2	7.3	4
IWM US Equity	IWM	5.5	4	2.5	9	8.0	3
S5INDU Index	Industrials	4.5	5	3.3	8	5.2	5
EWU US Equity	EWU	4.3	6	6.5	6	1.2	11
EWW US Equity	EWW	3.4	7	1.4	11	4.6	7
EWC US Equity	EWC	2.6	8	0.4	15	4.7	6
EZU US Equity	EZU	2.1	9	1.8	10	2.0	10
S5MATR Index	Materials	1.7	10	0.6	12	2.7	9
FXI US Equity	FXI	1.3	11	9.4	3	-8.2	16
EEM US Equity	EEM	1.2	12	3.8	7	-2.0	14
EWJ US Equity	EWJ	0.0	13	7.8	4	-9.4	19
S5TELS Index	Communications	-1.3	14	-2.6	17	0.5	12
S5COND Index	Consumer Discretionary	-1.5	15	-5.8	19	3.8	8
S5INFT Index	Info Tech	-3.0	16	-4.9	18	-0.4	13
S5HLTH Index	Health Care	-4.1	17	0.4	14	-8.8	17
S5CONS Index	Consumer Staples	-4.4	18	0.6	13	-9.4	18
S5UTIL Index	Utilities	-7.0	19	0.0	16	-13.8	20
S5RLST Index	Real Estate	-7.7	20	-6.5	20	-7.8	15

Source: Citi Equity Trading Strategy, Bloomberg

GICS 1 US Energy Long Only Sector Flows

Source: Citi Equity Trading Strategy

Alty

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