13.02.2024

Qi Market Spotlight: Look Up!

Be fearful when others are greedy. The S&P 500 has posted the best 3mth risk adjusted returns since the tech bubble

Through the Qi lens there are signs that crowded trades are increasingly vulnerable

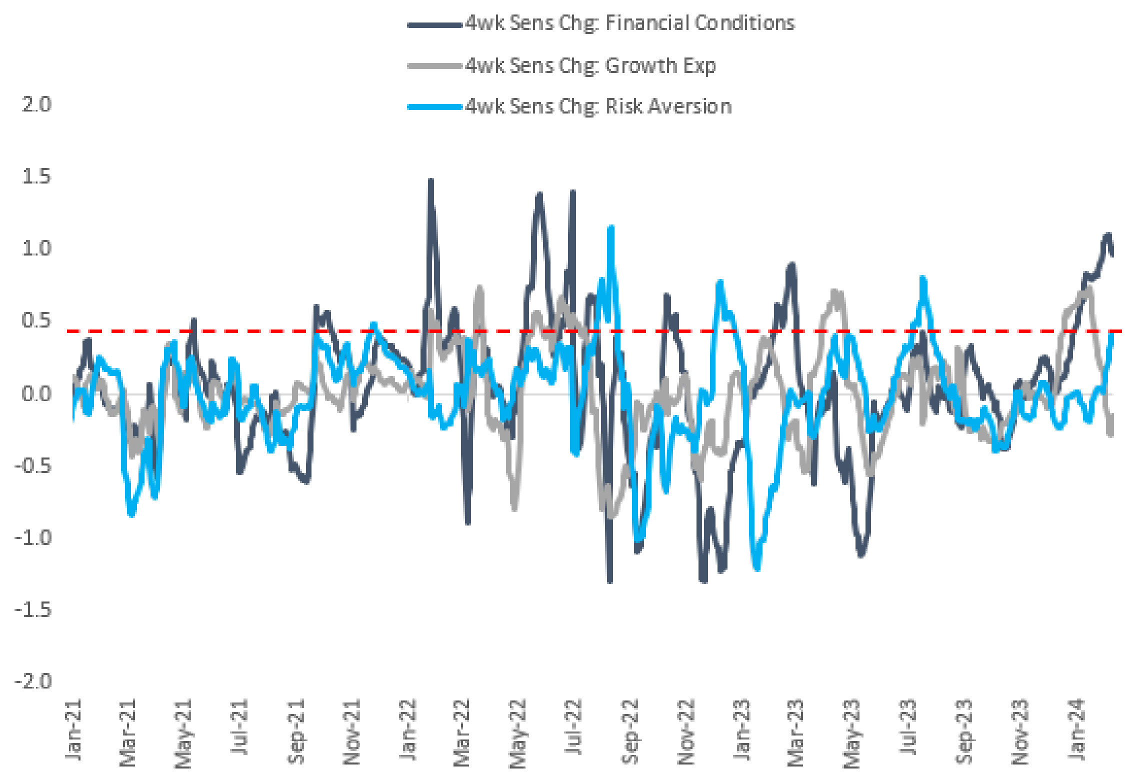
The S&P 500 sensitivity to risk appetite is becoming extended - questioning whether prevailing market momentum can be sustained

The S&P 500 screens rich to US Treasuries while bond vol is also screening macro-cheap Styles synonymous with the current Goldilocks narrative, Momentum & Growth, are trading macro-rich also. By definition, Momentum performance reflects the returns of the most popular trades. When momentum is extended, it would deem views are crowded

1/ The sensitivity to risk appetite macro drivers has accelerated sharply - what can go wrong?

Qi identifies an asset's sensitivities to a large macro driver information set. Broadly, these macro drivers can be bucketed into financial conditions (e.g. credit spreads, real rates, USD TWI), growth expectations (e.g. GDP Nowcast, metals, energy) and risk appetite (e.g. VIX, gold / silver ratio).

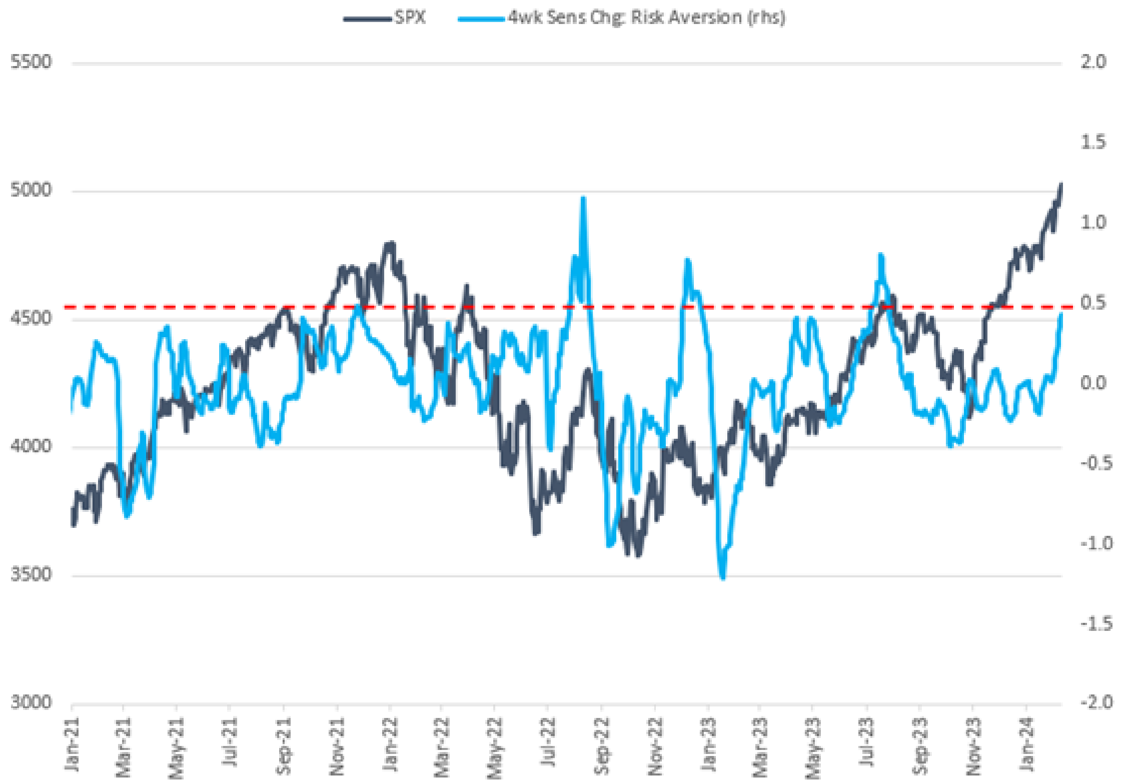
Below, we show the 4wk change in those bucket sensitivities for the S&P 500 – we refer to these 4wk changes as the market's macro beta impulse to these specific drivers. This highlights the focus on financial conditions but **what has caught our eye this week is the increasing attention to risk appetite.**

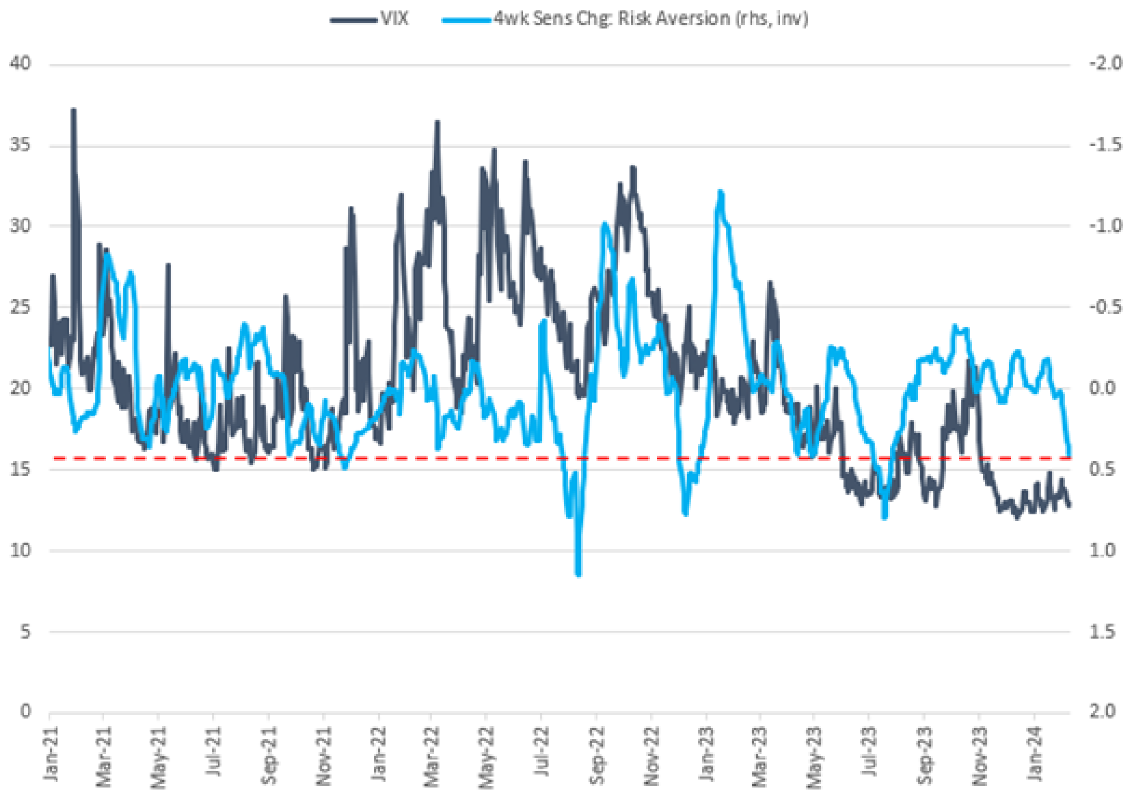


The sensitivity to risk appetite has accelerated as VIX has descended below 13. Reliance on low equity volatility rises as the market accelerates. However, **as this reaches close to multi-year**

highs, the premise presumably is that everyone is close to "all in" on the prevailing narrative.

The charts below plots the sensitivity to risk appetite vs. the S&P 500 and to VIX itself (sensitivity inverted on rhs axis). The simple point is that when sensitivity to risk appetite is becoming extended, it questions whether prevailing market momentum can be sustained. Perhaps no surprise, after the best 3mth risk adjusted return since the tech bubble.

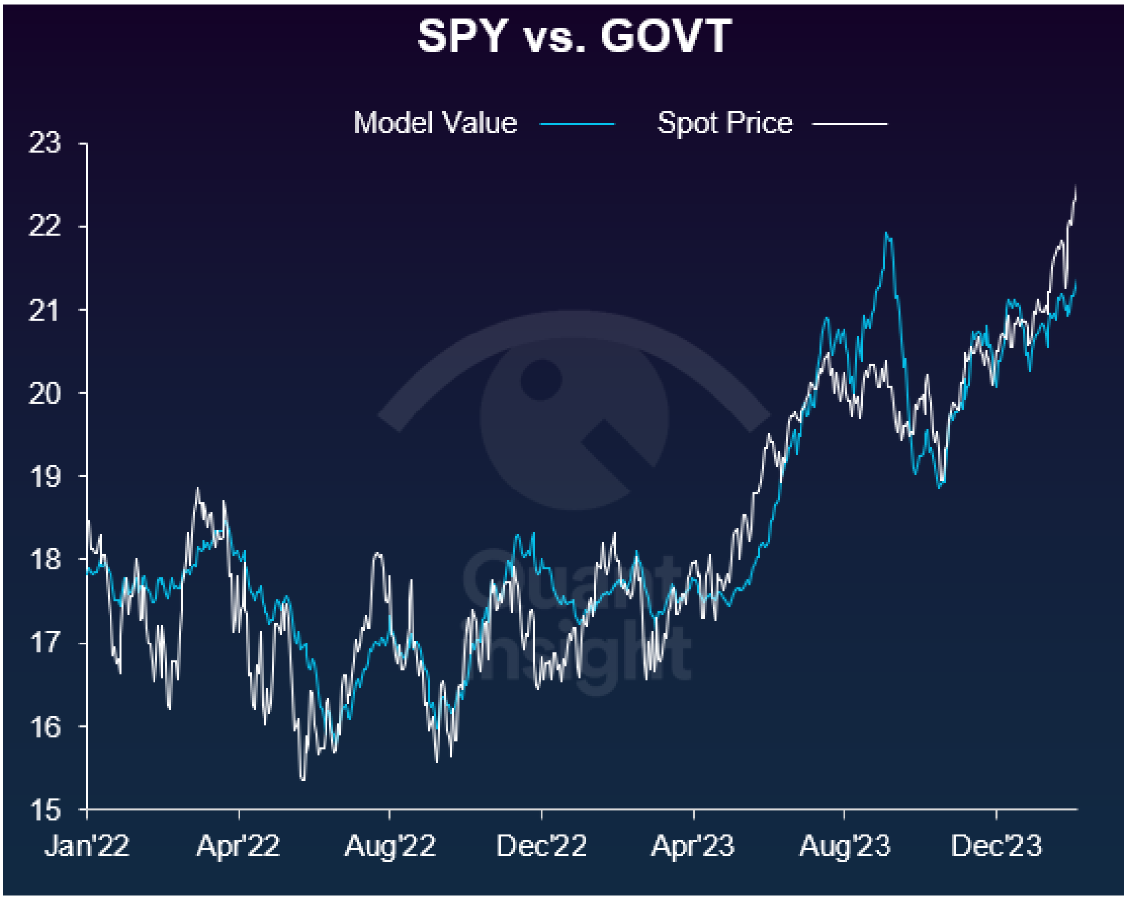


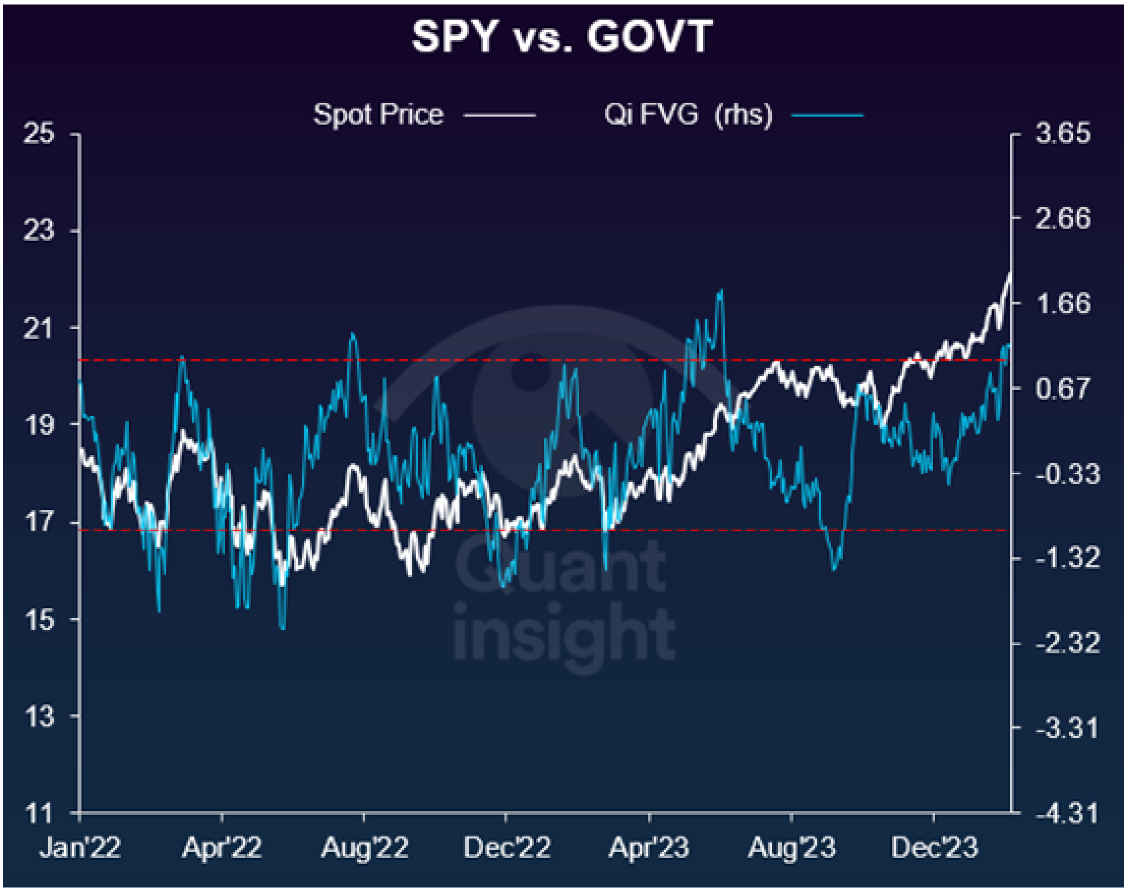


2/ Equities screening rich to bonds & bond vol screening cheap

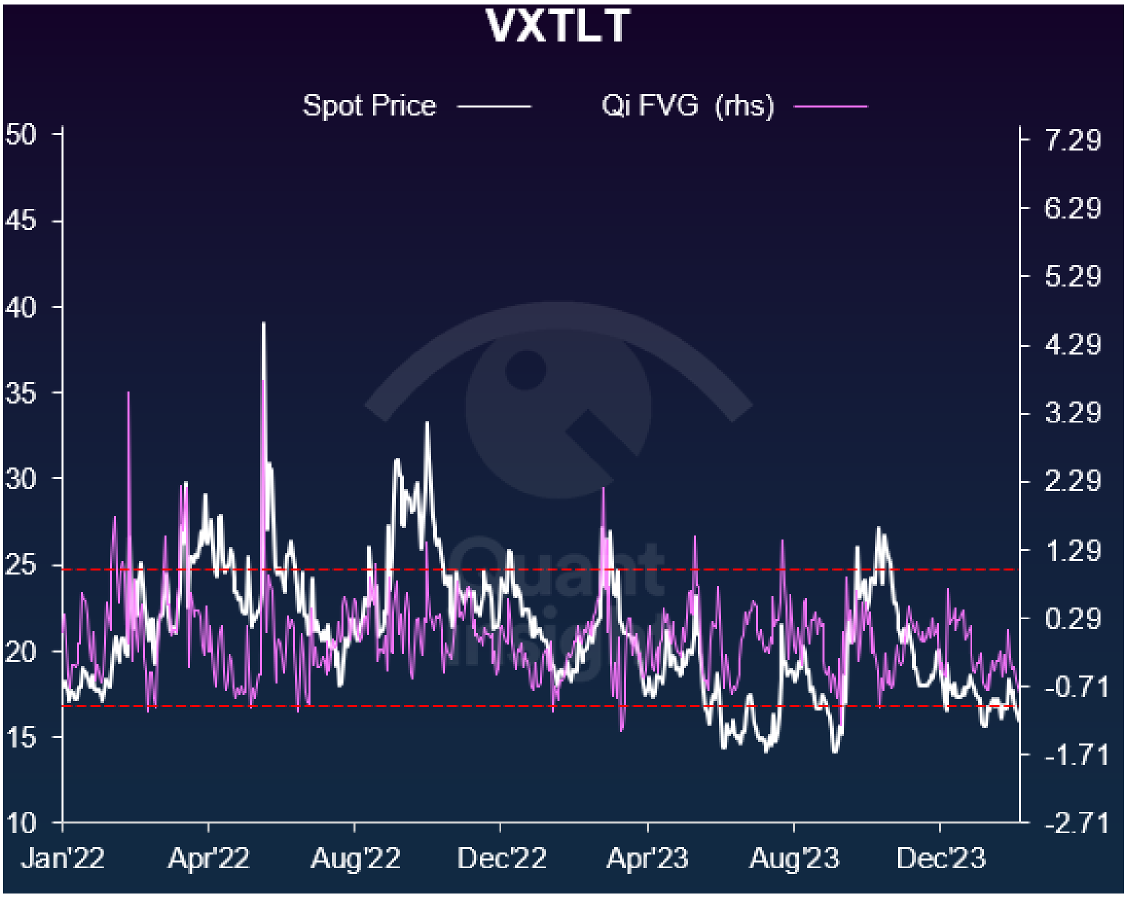
Below we show Qi's model value vs. spot for the SPY ETF relative to the GOVT ETF (iShares US Treasury Bond ETF). The second chart shows the current dislocation in terms of the fair value gap vs. the spot price (+1.2 sigma).

Of late, commentators have noted that the correlations between equities and bond prices have started to wane i.e. growth is deemed strong so the level of rates matters less. However, Qi has picked up on that dislocation, arguing in the short term, the move looks over-extended.



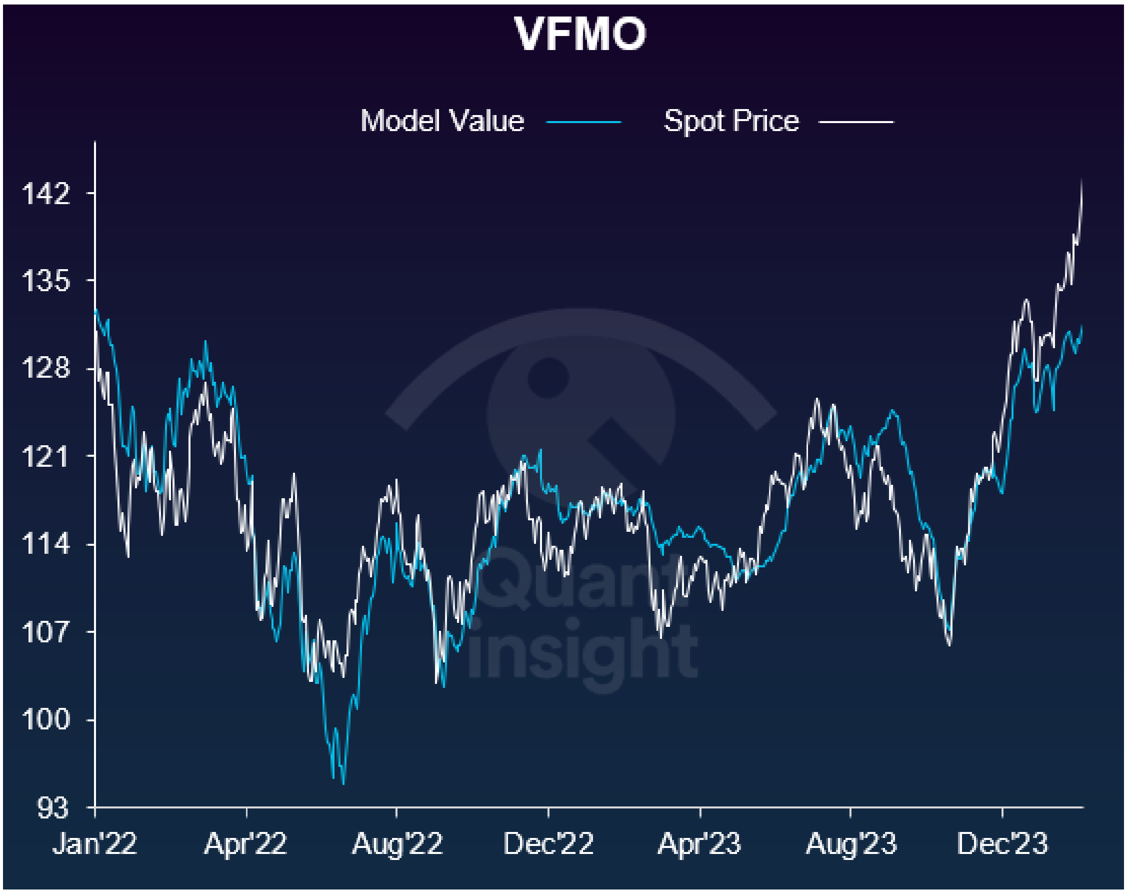


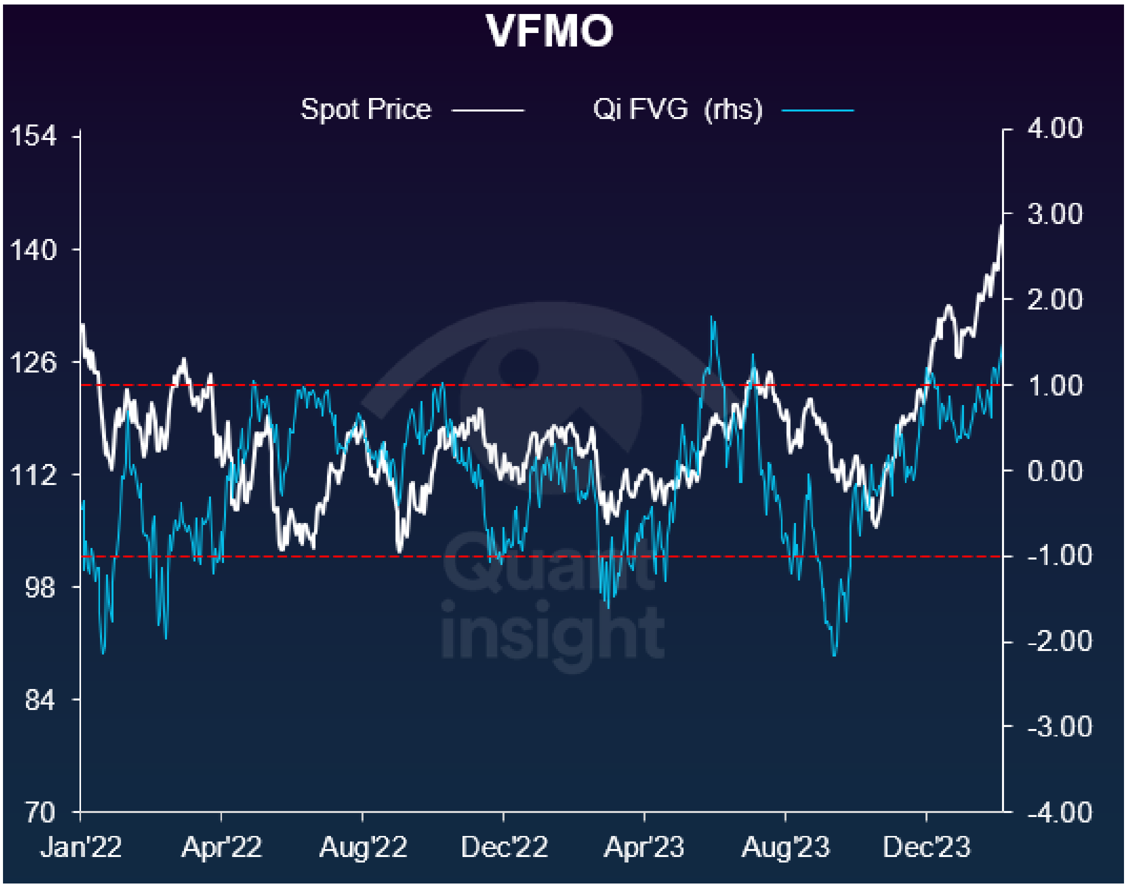
In contrast, Treasury Bond vol as proxied by VXTLT is screening below its Qi macro-warranted value (-0.8 sigma):

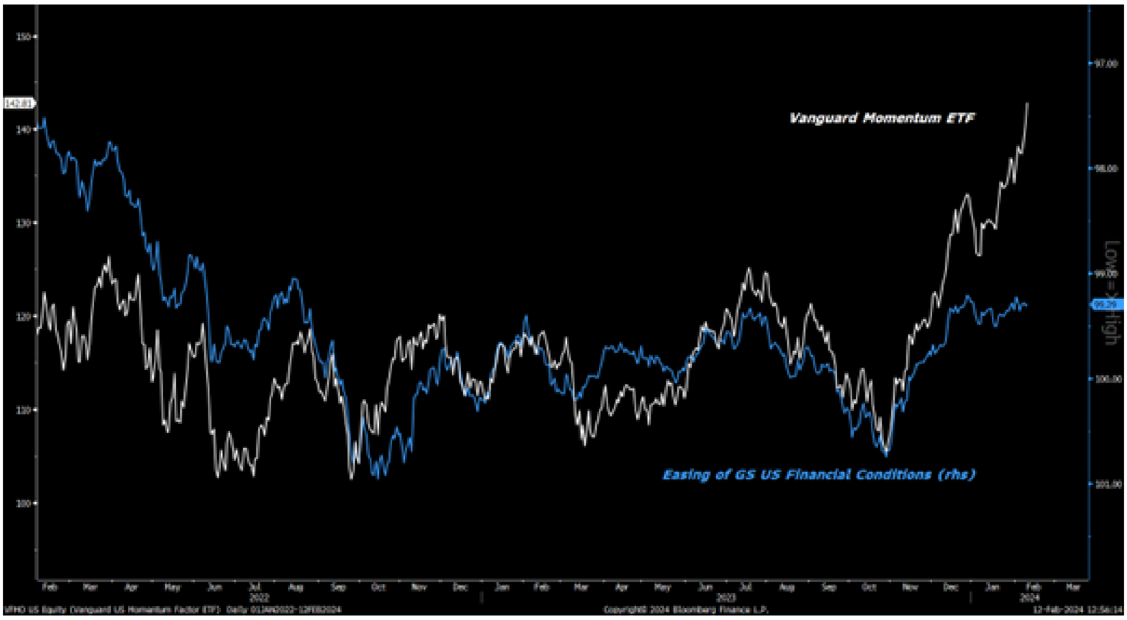


3/ Styles synonymous with the current Goldilocks narrative, Momentum & Growth, macro rich also

First, consider the VFMO Vanguard US Momentum Factor ETF. The biggest macro driver for Momentum has been financial conditions: a weaker dollar, lower real rates, tighter credit spreads. Below see Qi's macro model value vs. spot and secondly against the GS Financial conditions index. The third shows the same dislocation but in FVG terms.







Secondly, consider similar charts for growth (RPG Invesco Pure US Growth ETF) or long duration plays like Biotech (IBB iShares BioTech). Similar drivers, but the over-extension is concerning.

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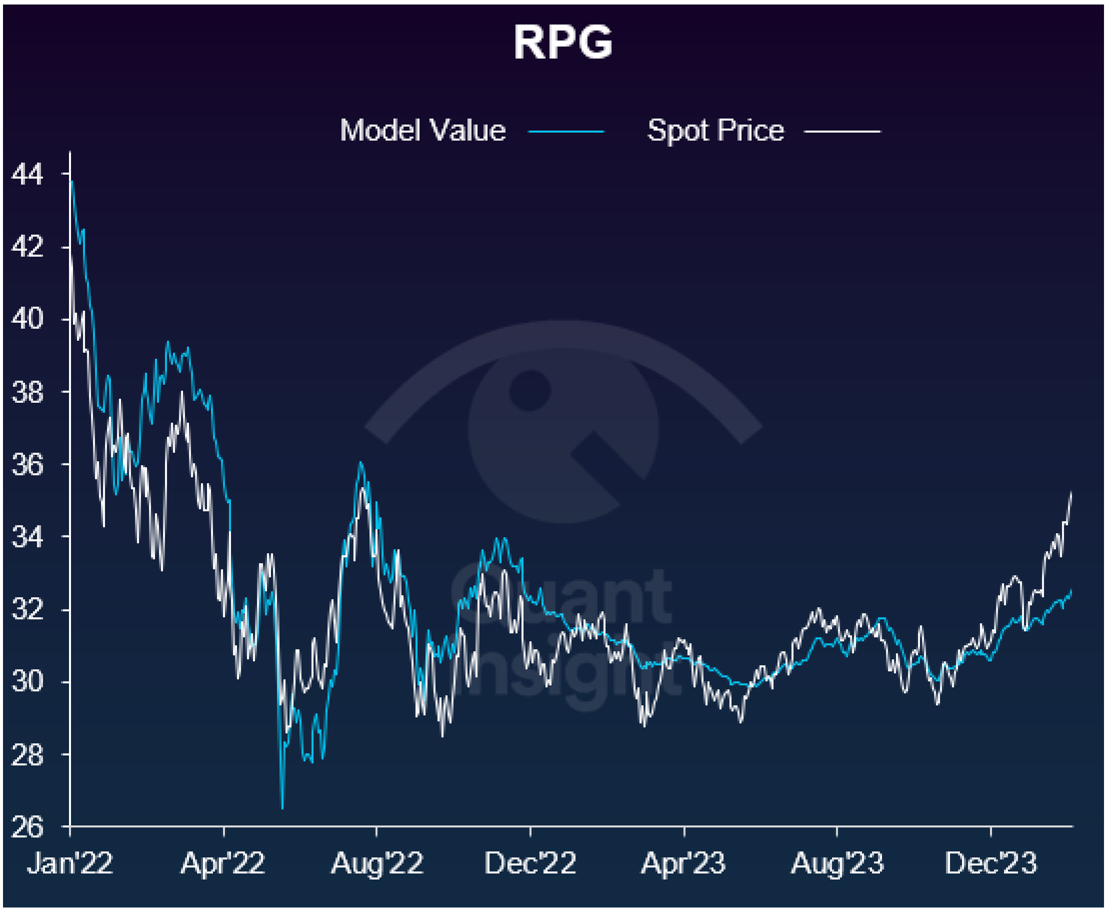

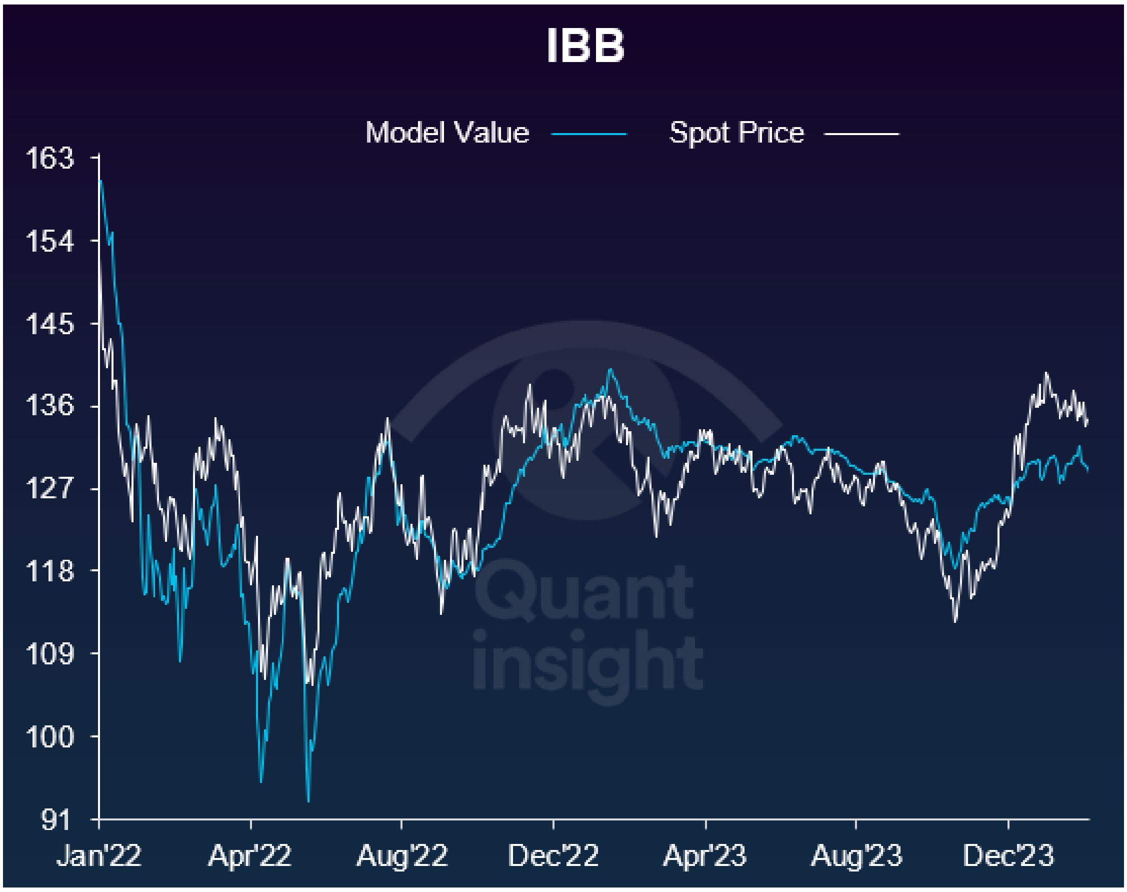

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