THE SHORT AND LONG

Weekly Bulletin

Positioning Resets as Inflation Risks Linger

NOVEMBER 10, 2026

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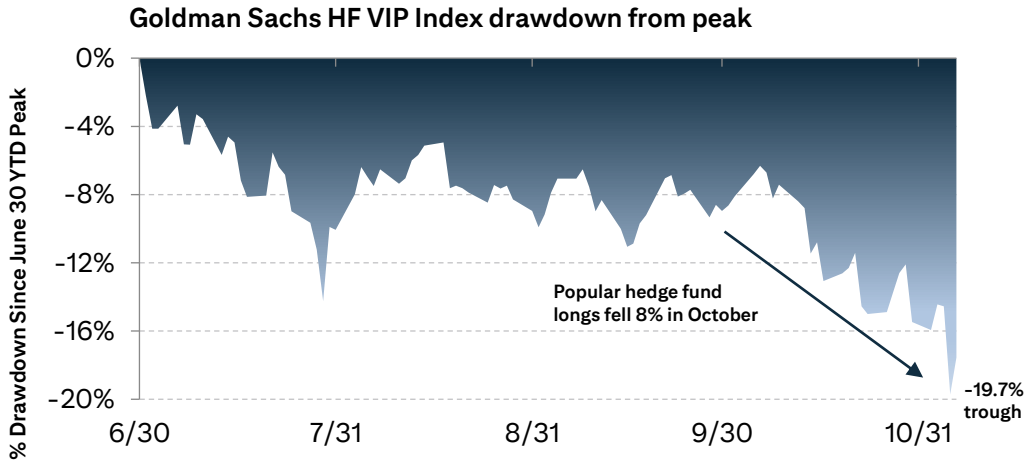
Hedge funds, systematic strategies, and retail investors all reduced risk last week, triggering liquidations in many of the market's most crowded positions. Importantly, this positioning reset could create a tailwind for equities as investor exposure normalizes. Looking ahead, we believe the growing use of AI-driven research will make position crowding a more persistent feature of market structure.

Investor sentiment has fallen into fear territory, but several underlying indicators remain constructive. Market breadth improved ahead of the recent selloff, and the number of stocks reaching new 12-month highs increased last week. In our view, investors are rotating within equities rather than exiting the asset class altogether. Historically, periods of extreme fear have created attractive entry points for long-term investors.

In our view, inflation risks remain underestimated by markets, and we believe the U.S. Federal Reserve (Fed) missed an opportunity to hike interest rates at its last meeting. Tuesday's Consumer Price Index (CPI) was a reminder that pipeline pressures may require the Fed to hike more than is currently priced into markets.

THIS WEEK IN CHARTS

FIGURE 1: Crowded hedge fund positions unwound



Source: Bloomberg as of November 6, 2026. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

LOOKING CLOSER

The Goldman Sachs Hedge Fund VIP index consists of the 50 companies that appear most frequently as top ten hedge fund holdings. The index achieved all-time highs on June 30, 2026, and fell nearly 20% by November 5, 2026, due to a sentiment-driven positioning unwind.

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CROWDED TRADES UNWIND AS AI CONCENTRATES CAPITAL

Citi Wealth CIO considers four pillars when evaluating potential investment opportunities: macro regime, fundamentals, positioning and sentiment, and valuations. This week, we focus on positioning and sentiment because they explain most of last week's volatility. Thursday produced the third-largest intraday VIX[1] spike since 1990, underscoring the speed and magnitude of the risk reduction across markets. At the same time, the market experienced its third major momentum unwind of the AI era[2]. We view these mini boom-bust cycles as a natural byproduct of a technological transformation of this scale, particularly as investors crowd into the same themes and positions.

Hedge funds, systematic strategies, and retail investors all reduced risk simultaneously. Retail investors entered the selloff with crowded positions, particularly semiconductors, and unwound much of that exposure last week. Hedge funds cut net exposure sharply as well (Figure 1). In a classic sign of forced liquidation, the most heavily shorted quintile of stocks returned 7% in October, more than double the return of the least shorted stocks.

We believe AI may intensify this dynamic. As investors increasingly turn to AI tools for research theses and trade ideas, those tools may steer capital toward the same potential opportunities. AI may democratize research, but it may also concentrate capital, and we expect crowding to become a structural feature of markets rather than a cyclical one.

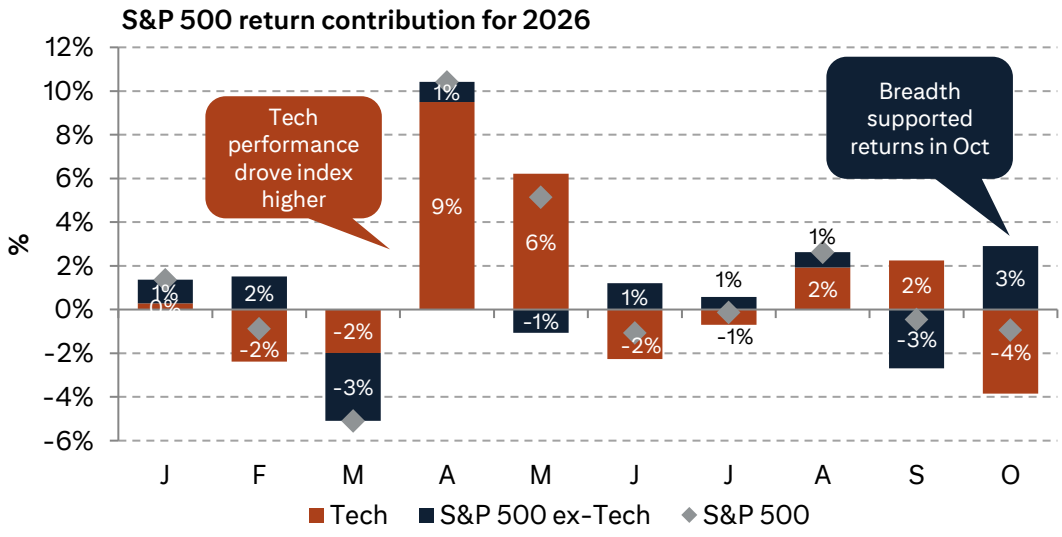
If forced liquidations run their course, positioning could shift from a headwind to a tailwind. We believe last week's washout has moved markets closer to that turning point.

Bottom line: Crowded retail positioning, systematic selling, and hedge fund deleveraging drove last week's liquidations, and AI may make crowding a lasting market feature. With positioning now reset, we believe market structure may shift from a headwind to a tailwind in the near term.

FEAR RISES AS MARKET BREADTH IMPROVES

Breadth was improving before the selloff began. In October, 76% of S&P 500 constituents outperformed the index, the strongest reading in more than two years[3]. Technology drove index gains earlier in the year, but broad participation supported returns in October (Figure 2).

FIGURE 2: 76% of S&P 500 constituents beat the index in October, the highest mark in over two years



Source: Bloomberg as of November 6, 2026. Tech is a broader way to measure the tech ecosystem than just the Technology sector alone. It combines the S&P 500 Information Technology sector with S&P 500 Broadline Retail and Interactive Media & Services industries that capture the remaining megacap tech names. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

Leadership broadened from growth into value and defensive sectors. This year has brought swings between growth and value, and between mega-cap technology and defensive sectors such as Healthcare and Consumer Staples. In our view, this is not a story of investors abandoning equities, rather one of investors rotating within them.

[1] The CBOE Volatility Index (VIX) is a real-time market index that measures the U.S. stock market's expectation of 30-day forward-looking volatility.
[2] The "AI era" runs from late November 2022 to the present.
[3] Bloomberg as of November 6, 2026.

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Additionally, November 4-5 produced the highest number of new 12-month highs in the Russell 3000 index since late July. Markets entering a more durable, fundamentally driven downturn do not typically show this pattern.

Sentiment, by contrast, has deteriorated sharply. Demand for protection pushed an S&P 500 sentiment and positioning indicator we reference deeper into fear territory, with Friday's reading below our fear threshold. Historically, periods of extreme fear have often marked compelling entry points rather than reasons to exit.

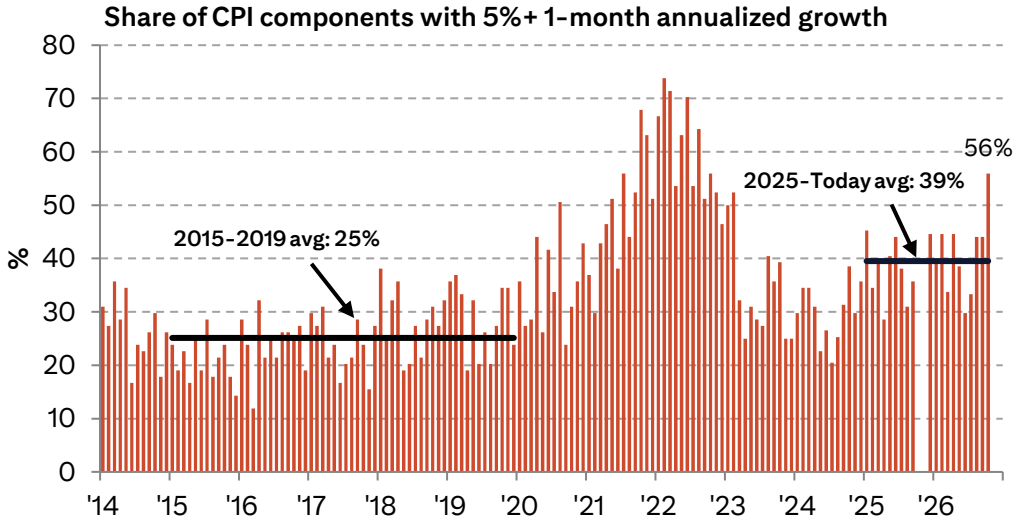
The key distinction is fundamentals remain resilient even as sentiment weakens. Sentiment and crowd positioning, not fundamentals, are driving today's volatility. For investors, this reinforces the importance of separating emotional reactions from the underlying economic reality.

Bottom line: Market participation is broadening, not disappearing, as investors shift capital across sectors, even as fear grips sentiment. Extreme fear has historically been a statistically advantageous entry point alongside resilient fundamentals, which we believe remain intact today.

INFLATION RISKS REMAIN UNDERESTIMATED BY MARKETS

In our view, the Fed missed an opportunity to hike interest rates at its prior meeting given inflation pressures continue to build within the Producer Price Index (PPI) pipeline and inflation breadth remains elevated and inconsistent with price stability near the 2% target. Tuesday's CPI data confirmed our view as the share of CPI components rising 5% or faster jumped to 56% in October from 44% in September (Figure 3). As a result, October's share is the highest since August 2022.

FIGURE 3: Underlying inflation breadth remains elevated and rising relative to pre-Covid norms



Source: Haver Analytics as of November 10, 2026. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

Additionally, so called "supercore" inflation, which excludes both housing and energy-sensitive categories and better captures underlying services inflation, rose another 0.4% in October and has increased at a 5.5% annualized pace over the past three months. In other words, broad based services inflation, not energy prices or tariffs, continues to drive price pressures higher. Notably, Fed officials have largely stopped emphasizing supercore inflation as a policy metric as those readings continue to move in the wrong direction.

Bottom line: In our view, pipeline pressures signal inflationary pressures have not yet peaked, and inflation remains too broad-based to square with price stability or a return to the 2% target. The Fed may need to raise rates more than markets currently expect.

	WHAT HAPPENED	WHAT'S AHEAD
ECONOMIC DATA	**U.S.** Nonfarm payrolls for October were +165K versus survey median of +70K. The prior two months were also revised up. The U.S. jobless rate for October fell to 4.1% in the prior month. ISM Services and Manufacturing data for October remain in expansionary territory; services missed expectations while manufacturing beat. ISM services employment strengthened in October while manufacturing employment pulled back slightly but remained at solid levels.	**U.S.** PPi for October
	Global Globally, services PMI numbers for October remained in expansionary territory; China was the notable miss at 50.8 versus survey estimate of 51.7, the Eurozone and UK came in slightly below estimates, India eased but remains strong, and Japan showed expansion despite some moderation from early-2026 highs. Eurozone inflation rose to a three-year high of 4% in October, according to flash estimates. The increase was largely driven by surging energy prices.	**Global** Eurozone Q3 GDP (2nd estimate) UK preliminary Q3 GDP Japan preliminary Q3 GDP
POLICY	**U.S.** Democrats won control of the U.S. House and Senate by significantly wider margins than anticipated in what is understood to be a strong repudiation of the Trump Administration, inflation, and the war with Iran. Following his party's midterm losses, President Trump softened rhetoric regarding escalation of the Iran war.	**U.S.** We will be attuned to Fedspeak regarding the pace of future rate hikes. Rhetoric on how newly appointed policymakers will regulate AI and its buildout.
	Global The Bank of England Monetary Policy Committee voted to lift rates by 25 bps to 4%. In prepared remarks, Governor Andrew Bailey stated that it is likely not the last hike if the Iran war persists.	**Global** The U.S., Russia, and Ukraine will hold peace talks in Abu Dhabi on November 10-11 in an effort to end the war.
MARKETS	**U.S.** Post-midterm election concerns about tighter regulation of AI triggered a powerful rotation out of AI and semiconductor stocks with the SOXX index experiencing its third-worst 20-day return in its history. The initial rotation quickly turned into a positioning-led liquidation and market risk-off event that saw the Nasdaq 100 fall 6.4% on Thursday. U.S. equity performance breadth strengthened this week with ~71% of S&P 500 members trading above their 50 dma (highest ratio since late July).	**U.S.** Light week of earnings with only 2% of the S&P 500 reporting. With ~80% of the S&P 500 reported. 83% are beating estimates with a surprise rate of 3.2%. The amount beating is slightly above average while the surprise is below the five- and ten-year average.
	Global The U.S. selloff spread with the Nikkei 225 falling 6.2% on Friday (worst day since April 2025).	**Global** Selloff in equities has been driven by sentiment of AI going forward but fundamentals remain healthy and any capex discipline would unlock further profitability.

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RELATED READING

November 3, 2026 | Rate-of-Change Season: Digesting Peak Growth in a Volatile Stretch

In last week's Bulletin, we looked at why the U.S. Federal Reserve kept rates unchanged despite building pipeline inflation and still loose financial conditions. Meanwhile, AI capex continued growing, pressuring parts of the AI supply chain reliant on that spend.

October 29, 2026 | The Short and Long Podcast

In episode five of Citi Wealth's The Short and Long, Chief Investment Officer Kate Moore takes a comprehensive look at the rapidly shifting global energy landscape. Her guests, Patrick Pouyanné, Chairman and CEO of TotalEnergies, and Alastair Syme, Head of Global Energy Research at Citi Research provide an assessment of rising global power demand, the structural costs of the energy transition, and the geopolitical forces redefining market risk. Watch now on YouTube, Apple, or Spotify and subscribe for future episodes.

October 7, 2026 | The Short and Long: Q4 Macro Investment View

Citi Wealth's quarterly report is designed to offer global, data-driven guidance to help investors navigate increasingly complex markets with confidence and clarity. The latest report delivers a breakdown of inflation, AI investment cycle, role of gold, natural resources, and portfolio resilience, and lessons from our key investment calls throughout 2026.

September 24, 2026 | Global Investment Council

The Citi Wealth Global Investment Council met September 24, 2026, and increased allocations to U.S. equities, Japanese equities, and the cybersecurity theme, funded by a reduction in the overweight to U.S. securitized fixed income. The Council also reviewed and endorsed the portfolio's drift, remaining comfortable with the market-driven increase in equity exposure relative to fixed income.

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Investment Grade			
Highest quality	Aaa	AAA	AAA
High quality (very strong)	Aa	AA	AA
Upper medium grade (Strong)	A	A	A
Medium grade	Baa	BBB	BBB
Not Investment Grade			
Lower medium grade (somewhat speculative)	Ba	BB	BB
Low grade (speculative)	B	B	B
Poor quality (may default)	Caa	CCC	CCC
Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	C	D	C
In default	C	D	D

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- potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized;
- absence of information regarding valuations and pricing;
- complex tax structures and delays in tax reporting;
- less regulation and higher fees than mutual funds; and
- manager risk.

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