Research @ Citi Markets Edition: Deal or No Deal — The Market Consequences of a De-Escalation

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Transcript:

Intro: (00:00)
Research at Citi Markets Edition.

Alex Saunders: (00:04)
Welcome to Research @ Citi Markets Edition, where we break down global macro in 10 minutes or less. I am your host today, Alex Saunders, Head of Quant Macro Research, and I'm joined by Adam Pickett, our Head of Global Macro Strategy. Welcome to the show, Adam.

Adam Pickett: (00:22)
Thanks, Alex. It's great to be here with you.

Alex Saunders: (00:25)
We are recording this podcast at 10 a.m. on Monday, June 1, 2026. There's a lot to discuss, as always, and as has been the case in the last few months, not least in the Middle East, where at least the contours of a deal looked to be taking shape. Conditional on a deal — and the uncertainty remains high, there's been less encouraging news flow really coming out in the last few hours — that would be a relief for fixed income. We studied oil-price peaks, and we found that inflation comes off fast at the headline level, and more slowly on core. But rates unwind most of that move higher.

Adam Pickett: (01:06)
Interesting, Alex. And then I suppose one of the questions we often get asked is, “How do we differentiate between countries?” Because obviously, some places have inflation above target, some places are closer to inflation below target. Is there any way to differentiate the rates response function to the post-oil peak phase after that happens?

Alex Saunders: (01:32)
It's an important question, actually, Adam, and we differentiate on two axes, if you will.

Number one is, as you say, the country in question, whether inflation’s above or below target. And then the second vector to study really is the size of the oil-price sell-off. And if we look at our commodities team's latest views, that would be less than 20%, between a 10% and 20% potential sell-off. Those small sell-offs tend to favor countries with below-target inflation, so rates rally there, whereas the above-target countries, you'll typically see a sell-off.

However, it's somewhat interesting: That reverses slightly when you see these larger 20%-plus sell-offs in that environment, or in those instances. We see rates rally across the board, and actually the above-target ones rally, but they rally only slightly more than the below-target. So from our perspective, that leaves us with a bias really for countries where inflation is below target on the rate side.

Now, for the dollar, Adam, what's the view there?

Adam Pickett: (02:46)
Thanks, Alex. Somewhat similar to the study that you outlined — where the data backs up the market intuition that you want to receive the places with lower inflation than higher inflation in the event of the oil shock diminishing — I think in the U.S., given it looks like more of the rates repricing has been domestically driven by a reappraisal of the labor-market situation, the rates factor in our Eureka quant Eurodollar model will probably stay in the bullish-dollar camp. And as a reminder, that's just two-year rate differentials, the trended vs. the 55-day. And so I think in a resolution scenario, you'll probably unwind more ECB hikes than the Fed.

Relative equities, as we've described before, the AI thematic looks very resilient and quite long-lasting, and so I don't think the Iran situation will dramatically change what is already a relative equity factor pointing in favor of dollars.

And lastly, looking at the Citi data momentum indices, the U.S. vs. Europe gap is already so large that even a few surveys looking better in Europe after an Iran deal probably won't be enough to turn around that ship. The terms-of-trade factor, interestingly, is already in favor of euro over dollars, and that will naturally continue to push that way if oil does fall further.

But what I'm trying to get at is, from a quant perspective it looks like there's a decent risk that three out of four of our dollar signals are likely to stay pro-dollar into the summer. And so, our perspective is, if you get a knee-jerk dollar sell-off on an Iran resolution, ultimately that could be a dip in the dollar to buy.

Alex Saunders: (04:47)
Thanks, Adam. And then the other major asset class to cover would be equities. We looked at it from a positioning lens, and our equity quants have a high-frequency model. A couple of interesting points came out of that. More recently has been a move toward AI positioning, so that's markets in emerging Asia. And the Nasdaq, for example, in the U.S. became more popular. The Nasdaq in particular moved from having a short position to a long position. We did not see a bounce back as strongly — or at all, really — in some of the European markets.

The other point to make: There have been some worries and some client questions around the narrowness of recent performance, and the strong price momentum. We've studied that, and we don't think that's a problem in and of itself. The concern in terms of market worries that we found was more in large changes in time premium, or large sell-offs in rates as being — and it's the change, not the level that's important — much more of a limiting factor, I think, for equities. But overall, a deal would obviously be fixed-income-positive and probably equity-positive as well. Below-target inflation countries give you less of a scenario risk in terms of potential positions.

And I did want to flag one other indicator that we use very tactically on the equity side, which is our Markets team's POLLS indicator, which is flagging at least in the near term a little bit of exuberance, and would suggest some tactical caution on equities, particularly if we do get a deal and a bounce in equity markets.

So with that, thanks for joining us today.

This episode was recorded on June 1, 2026. I'm your host, Alex Saunders, with Adam Pickett, our Head of Global Macro Strategy. For more details, Citi clients can check out our report on the Citi Velocity portal.

Next week's Research @ Citi Markets Edition will be hosted by Scott Chronert, Citi's Head of U.S. Equity Strategy. And be sure to watch for our Research @ Citi podcast, which you can view on this same channel.

The macro strategy team will be back in two weeks. Stay sharp!