amFX

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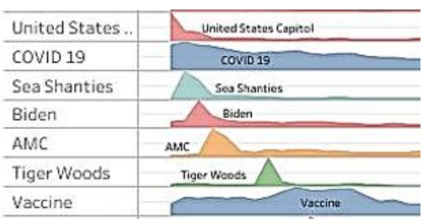


Sea shanties!

https://twitter.com/TheRealHoarse/status/1348995617889132545?s=20

Current Views

Short ES @ 4684
Stop loss 4682 / Take profit 4444

Short ETHUSD @ 4210
Stop loss 4902 / Take profit 3010
(From MacroTactical Crypto #4)

Loose as Burns

I have been excited about this Fed meeting and have been suggesting long USD into it as the market does a classic runup trade. Runup trades occur when the market moves in the direction of the "obvious" trade into an event. It worked well in USDCAD and most currencies are weaker vs. the USD this week. Now, it's crunch time.

My view remains that the interesting outcome is the hawkish one, though as expectations have become more hawkish and the USD has rallied this week (and the COVID situation is looking worse) I think the boring, down-the-middle, as expected outcome is the most likely result now. Here is my grid of outcomes, with the probability I attach to each and the best trades.

Fed outcomes and reactions grid

	Dovish		Neutral		Hawkish	
Median number of hikes	1	5%	2	70%	3	25%
Taper ends in	June 2022	5%	March 2022	70%	Before March (they end MBS buying today?)	20%
Total hikes for 23 and 24	6	30%	7	40%	8*	30%
Implied liftoff	September 2022	10%	June 2022	50%	March/May 2022	40%
Best trade	Long AUDUSD		Sell vol until year end		Long USDCAD	Long USDMXN
	Why?		Why?		Why?	
	High beta, RBA pivoting		Need to wait for CPI and jobs in January		BoC dovish, policy divergence	Nice entry, hawkish Fed bad for EM

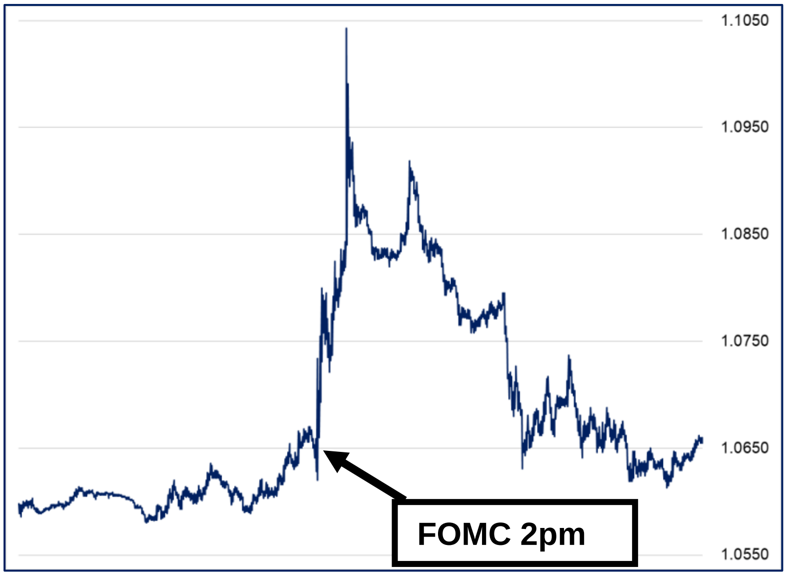
small outlier possiblity of more than 8, which would signal extreme hawkishness, faster pace

The interesting outcome is the hawkish one on the right. That is because a) it's consistent with a very aggressive Fed pivot, a raging hot labor market and 40-year high inflation and b) it will move the market. The dovish section is certainly tradable, I just don't think it's going to happen. The middle section is the meat of the distribution, and the market has converged almost unanimously into that zone, so that outcome is boring.

From a risk management point of view, I think you have to be ready for the dovish outcome, even though it's rather unlikely, because the market is certainly positioned hawkish. Remember March 2015, we had a similar set up at a similar point in the cycle and the Fed dropped a dovish Hammer of Thor on the market. Big difference this time though is that inflation then was around 2% and now it's around 7%. Therefore, I don't think that analogy works here, but the vibe around this meeting and the March 2015 meeting do feel similar so risk managing a dovish outcome is an important consideration if you go in long USD or short ED or similar.

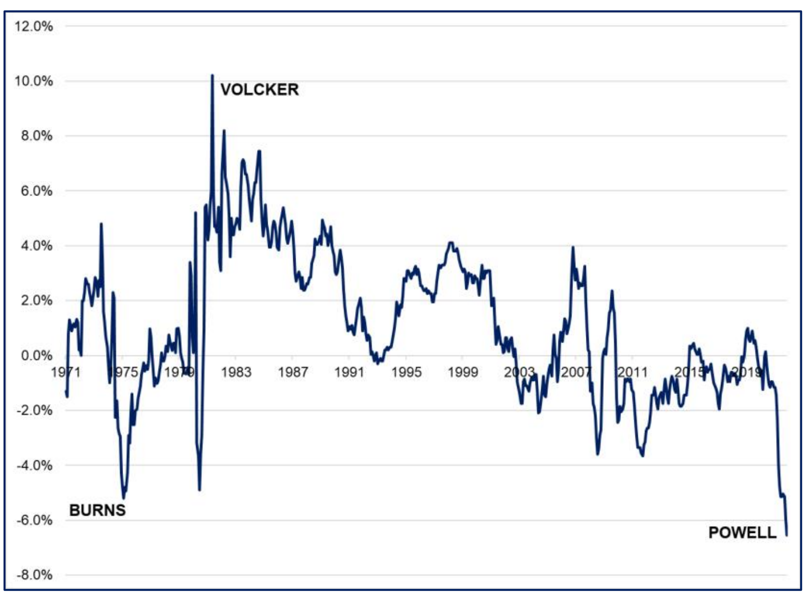
Here is EURUSD in the 48 hours surrounding the March 2015 FOMC meeting. Note the 400-pip rally!

EURUSD, 18 and 19 March 2015

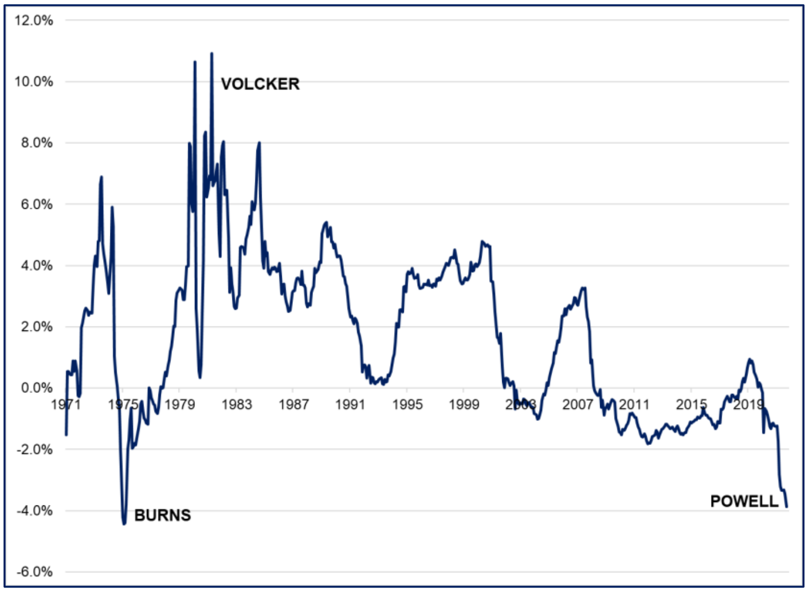


If you look at Fed Funds minus CPI or Core PCE, Jay Powell is running Arthur Burns style policy right now (see next two charts). There are less simplistic ways of looking at the current policy setting that show less dramatic results but these charts give you a sense of how we are living through history right now.

Fed Funds rate minus CPI YoY, 1971 to now



Fed Funds rate minus Core PCE, 1971 to now

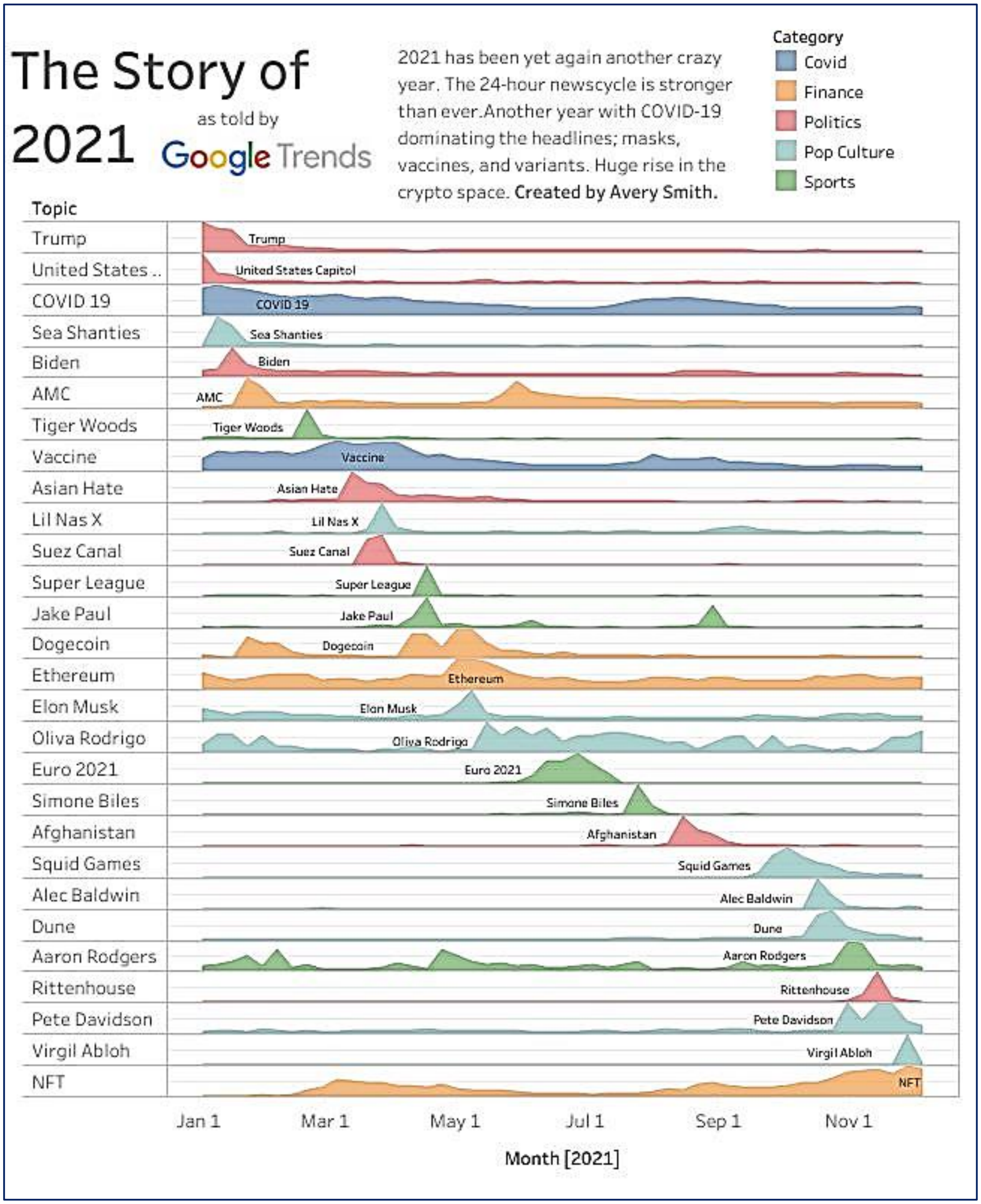


Trades update

With the S&P short now 50+ handles in the money, I don't want it to turn into a popcorn trade, so I'm moving the stop loss to just below the entry point (4682) so that I will most likely get stopped out at flat (including slippage) in the worst-case scenario. I also lowered the TP a fair bit so that I can optimize a full-scale risky asset dump if it's an extreme hawkish outcome. New parameters are 4444 / 4682.

Have a pivotal day.

good luck ⇅ be nimble



By Avery Smith, via LinkedIn

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