SPECTRA MARKETS

Monday, January 24, 2022

am
FX

Brent Donnelly

bdonnelly@spectramarkets.com
(212) 398-6230

The treachery of images
Magritte, 1929

Current Views

Long TYH2 @ 127^24
Stop loss 126^24
Exit at 4 p.m. today

Long 03FEB CADJPY
90.00 put
Spot ref: 90.80 /// Price 75 pips
(stale for now, but you never know!)

Ripe for a dead cat bounce

INT. INVESTMENT BANK TRADING FLOOR – DAY

The red-soaked equity heatmap on INTERN EMMA's monitor reflects in her $365 Prada glasses as she turns to NANCY, Director and Head of Equity Trading. INTERN EMMA is still finding her way as she just started in 2020.

Nancy notices Emma turning to her and so she quickly clicks away from coingecko.com where she was surreptitiously checking crypto prices despite the avalanche of client requests waiting on her Bloomberg chats.

INTERN EMMA
So boss, quick question. Why are stocks lower?

NANCY
To me, it looks like a major correction--

INTERN EMMA
What's a correction?

Where are all the bears?

I still find it surprising and kind of alarming how few bears there seem to be out there. There is a cohort that would generally be all-in short cross/JPY or short S&Ps on this set up and yet the predominant inbound query I am still getting is not "should I double down on my shorts?" it's "I want to buy more, any Turnaround Tuesday thoughts?"

I was already receiving questions about tomorrow's potential for Turnaround Tuesday by late last week! This says to me that we are at the point of the cycle where short positions in stocks have been such a bad trade for so long, people just can't bring themselves to do it this time. That is the sentiment setup I observe here, though BAML data show the market is mega underweight tech and mega overweight commodities.

While people like to read the BAML survey as contrarian… It's not. The consensus has called the correct direction on tech stocks for years and was short commodities the whole way down 2013-2016. People have been piling into tech for 10 years. The moment they turn bearish, it's certainly not contrarian.

Bigger picture, I continue to believe you sell rallies in risky assets, but we are getting a confluence of short-term indicators that suggest we are now ripe for a bounce. For the past few weeks, I have been going on about the lack of fear and how that is extremely bearish. My ex-ante view was you can't be long risky assets until we get at least two of the following three outcomes:

- Crypto down 15% in one day. CHECK
- VIX at 35 CHECK
- NASDAQ down 5% in one day. Not yet

Done! Time to cover shorts and wait for the next huge rally to sell.

Hey! TT Guy!

The metagame around Turnaround Tuesday is getting super complicated and it's even more complicated for me specifically because I am slowly becoming a go-to for questions about it, so my sample is biased. The 2 p.m. to 4 p.m. window for stocks has been hairy of late, with ETF madness, margin calls, and other factors at play. To me, the metagame suggests that everyone will buy at 1 p.m. and get rinsed into the close. If you're bullish, I would wait until 4 p.m. to buy for TT and not try to position early.

Stocks are massively oversold, FOMC is coming up, and Turnaround Tuesday lurks… If you are bullish risky assets, you will rarely see a better short-term setup than this. You just have to plug your nose and press BUY.

Given my concerns about market fragility as the Fed slams the monetary brakes at the same time as the US government slams on the fiscal brakes and the Web3 bubble bursts… My conviction on the countertrend bullish trade is minimal. This setup is like "If you were bullish already, it's one heck of a setup." But it's not a standalone reason to be bullish in such a horrendous macro backdrop, two days ahead of a major event. If you're playing the rebound, be prudent with your risk management.

Dollar view

My general view on the USD is that fading US exceptionalism will lead to significant dollar weakness soon.

BUT! And it's a very big but… The quantity of USD to be bought into this month end could be epic. I will offer the disclaimer that the month end model has not performed well recently, so keep that in mind. But the ginormity of the moves in US equities suggest extreme caution with short USD positions over the coming week. Corporate month end (buy USD) is Thursday and real money month end is next Monday. Expect furious bouts of USD buying off and on into and on those days. Random bursts of mutant USD buying will be a feature over the next six sessions.

There is, of course, that FOMC thing on Wednesday, along with BoC and some other events. There is more happening in the next six days than just flow. But the flow picture is extremely USD positive for the next week. Foreign investors (like all investors in the past few years) have been gobbling up NASDAQ and growth for years. Now, they just gave back 13% in a month and their short USD hedges are way, way too big.

For context, here are the worst months for the NASDAQ since 1990.

Months where NASDAQ lost 10% or more since 1990

Date	1-month change	NASDAQ
11/30/2000	-22.9%	2,597.93
2/28/2001	-22.4%	2,151.83
8/31/1998	-19.9%	1,499.25
10/31/2008	-17.7%	1,720.95
9/28/2001	-17.0%	1,498.80
4/28/2000	-15.6%	3,860.66
3/30/2001	-14.5%	1,840.26
9/29/2000	-12.7%	3,672.82
1/21/2022	-12.0%	13,768.92
5/31/2000	-11.9%	3,400.91
9/30/2008	-11.6%	2,091.88
8/31/2001	-10.9%	1,805.43
9/30/2002	-10.9%	1,172.06
11/28/2008	-10.8%	1,535.57
2/28/2002	-10.5%	1,731.49
3/31/2020	-10.1%	7,700.10

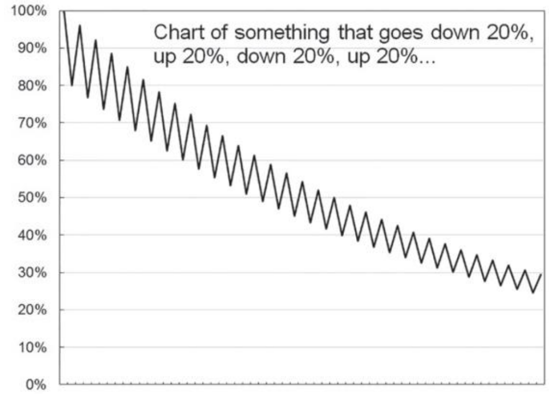
A few things stand out on that table. First of all, the NASDAQ is down almost 2,000 points this month. That's the entire NASDAQ in both 2000 and 2008! We just lost an entire NASDAQ![1] Amazing how gigantic the nominal appreciation

[1] Not really but.. Kind of?

has been. Generational. The other thing that jumps out is the fact that volatility comes in clusters. This is an observation made as far back as 1963 when Mandelbrot wrote:

> At closer inspection, one notes that large price changes are not isolated between periods of slow change; they rather tend to be the result of several fluctuations, some of which "over-shoot" the final change. Similarly, the movement of prices in periods of tranquility seem to be smoother than predicted by my process. In other words, **large changes tend to be followed by large changes—of either sign—and small changes tend to be followed by small changes,** so that the isolines of low probability of [L(t, 1), L(t - 1, 1)] are X- shaped.

In a bear market, you get a ton of down 10% months and you get a ton of monster short squeeze rally months. But of course, as explained nicely by one of my favorite charts of all time… If something keeps going up and down by the same percentage over and over, you get this:



From Alpha Trader (used with author's permission)

Russia

This Gideon Rachman article from the FT (Russia and China's plans for a new world order) is a useful, in-depth analysis of the current geopolitical state of play between USA, Russia, and China. I have no edge on geopolitics but it's hard to ignore the moves in RUB and Russian assets in combination with a bunch of embassy evacuations. The people with the best information are getting the heck out of Kyiv. Not bullish.

Trades Update

I plan to exit the TY trade at 4 p.m. today. I don't want that risk through FOMC and while my big picture view is sell rallies in risky assets, I respect the TT effect enough to get out ahead of it. The CADJPY option is now smalls in the money and I'm holding onto that as I continue to cling to my now out of consensus view that the Bank of Canada will not hike this week. I honestly really love the view but acknowledge the intellectual and market pricing momentum for a hike has moved a lot in recent weeks. Still, **I do not think they hike**, even though it's around 70% priced in.

Two reads

Finance related
The Price Action Lab blog is always excellent and this book they produced is a lesser-known finance gem. Their latest piece is simple and super logical: https://www.priceactionlab.com/Blog/2022/01/strategy-fund-performance/.

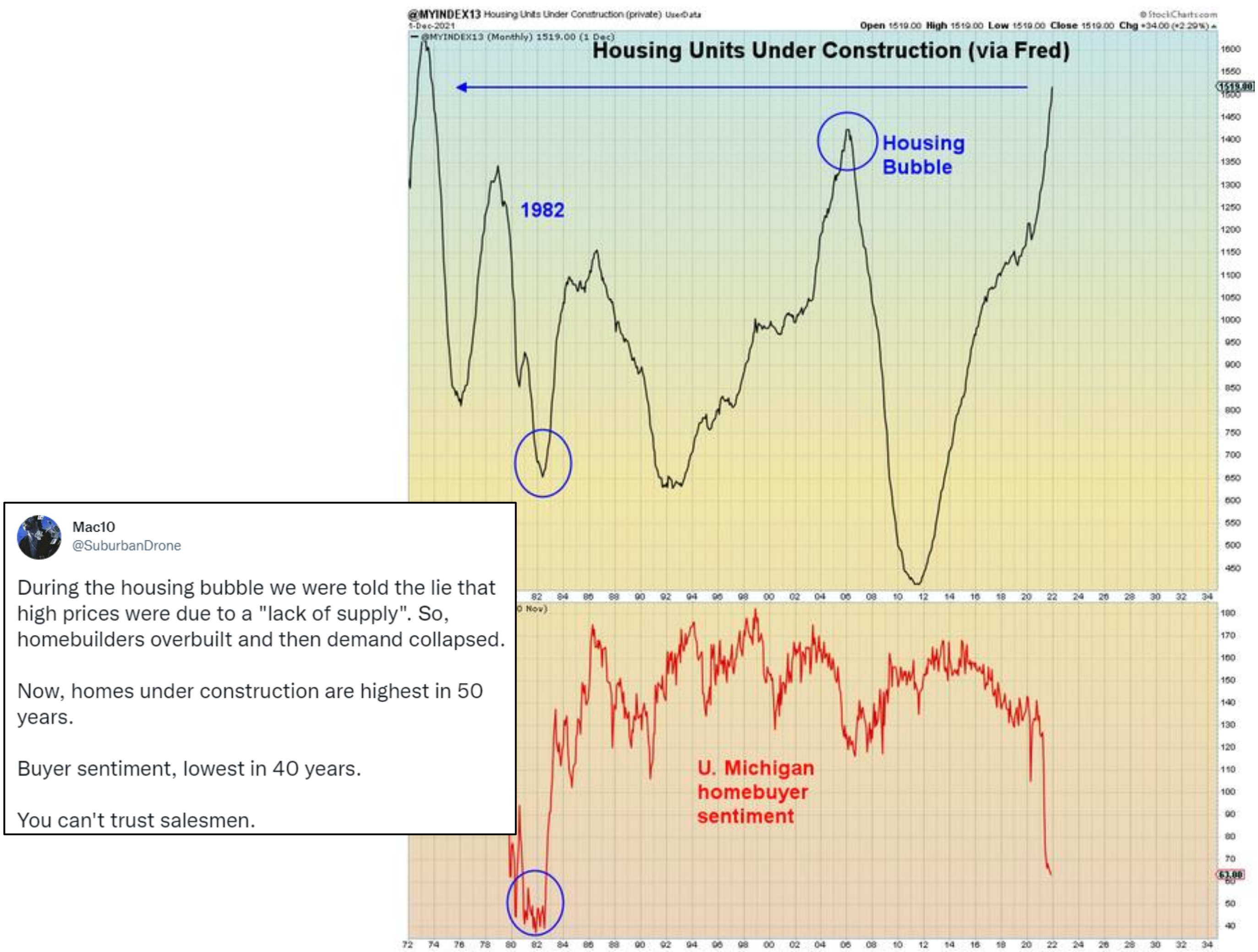
Not finance related
This Cormac McCarthy essay from 2017 is super cool: https://nautil.us/the-kekul-problem-6082/. Full disclosure: I am a Cormac McCarthy Stan, and this is only interesting if you are a language or cognition nerd.

Have a bubbly day.

good luck ⇅ be nimble

I think the global housing boom makes sense from a supply and demand point of view and it's probably not a bubble. It's more likely a generational transfer of wealth from commercial to residential as work from home becomes a permanent option for a meaningful percentage of the global workforce.

But I do love to look at alternative hypotheses. I suppose it's worth thinking about whether it's just another spec boom like crypto as leveraged investors pile in across the world and individuals stretch to buy less house with more money. Here's a reasonable-sounding take from FinTwit:



https://twitter.com/suburbandrone/status/1484894381064794117?s=21

Hat tips to the OG Ark and Neb Tnuh today for their inspiration.

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