

am
FX

Brent Donnelly

bdonnelly@spectramarkets.com
(212) 398-6230



The original Chad

Current Views

Short USDJPY @ 115.00

Stop 115.76
Take profit 113.81

Bullish EURGBP

Long 18MAR 0.8550 EURGBP digital
call at 24% (spot ref. 0.8426)

Bullish AUDCAD

Long 22FEB 0.91 AUDCAD call
Cost 26bps, spot ref 0.9050

Risky safe havens

We are witnessing unorthodox behavior of G10 FX, bonds, and EM through the equity ups and downs over the past year. The old paradigm of crude oil or emerging market currencies as risky assets, for example, has not applied.

To investigate the current status of various markets as risky assets or safe havens, I studied four distinct periods over the last year or so:

1. BULLISH The big reflation move 13MAY21 to 22NOV21
2. BULLISH The final leg up 13OCT21 to 25NOV21
3. BEARISH Risk aversion on Fed 05JAN22 to 23JAN22
4. BEARISH Risk aversion on Russia 10FEB22 to 21FEB22

Since the windows I'm studying are different lengths, I normalized all the moves by volatility (using z-scores), then divided by number of days in the period to get a reading I'll call "z-scores per day." The idea is not to create a statistically valid metric, it's to simply to find a heuristic that allows me to look at what direction assets moved in each period, and how much they moved per day. The assets in the table are sorted from riskiest to safest based on their scores.

	Full reflation move	Last leg of reflation move	Risk aversion (Fed)	Risk aversion (Russia)		
	13MAY to 22NOV 2021	13OCT to 25NOV 2021	5JAN to 23JAN 2022	10FEB to 21FEB 2022	Risky asset	Safe haven
SPX	0.12	0.28	(0.75)	(0.75)	TRUE	FALSE
NASDAQ	0.12	0.23	(0.78)	(0.67)	TRUE	FALSE
XET	0.03	0.15	(0.45)	(0.35)	TRUE	FALSE
XBT	0.03	0.06	(0.37)	(0.37)	TRUE	FALSE
CADJPY	0.00	0.01	(0.16)	(0.27)	TRUE	FALSE
AUDJPY	(0.02)	(0.03)	(0.39)	(0.05)	FALSE	FALSE
EURCHF	(0.13)	(0.27)	0.01	(0.78)	FALSE	FALSE
TLT (bonds)	0.07	0.08	(0.00)	(0.01)	TRUE	FALSE
HG3 (copper)	(0.03)	0.09	0.08	(0.14)	FALSE	FALSE
CAD	(0.08)	(0.11)	0.18	(0.17)	FALSE	FALSE
AUD	(0.08)	(0.12)	(0.09)	0.09	FALSE	FALSE
EUR	0.03	(0.26)	(0.05)	0.17	FALSE	FALSE
JPY	0.05	(0.08)	0.16	0.24	FALSE	FALSE
MXN	(0.05)	(0.18)	0.02	0.18	FALSE	TRUE
CL1 (crude)	0.06	(0.03)	0.37	0.15	FALSE	FALSE
XAU	(0.00)	0.07	0.11	0.51	FALSE	FALSE
ZAR	(0.10)	(0.23)	0.50	0.08	FALSE	TRUE

"Risky asset = TRUE" means it went UP in the two bullish periods and DOWN in the two bearish periods. Safe haven is the exact opposite condition.

There are many takeaways here. Here's what I see:

- ZAR and MXN are trading like safe havens. Amazing. As money flows out of US assets, it needs to go somewhere. It's not going into bonds because inflation is high, and the market keeps pricing more and more Fed hikes. Emerging market central banks are generally ahead of the curve compared to the Fed so perhaps this preference for EM kind of makes sense?
- EURCHF is the dream safe haven on bad geopolitical news out of Europe. Makes sense! Note the perfect touch of 1.0600 in EURCHF confirms that as a critical level. That is the Brexit low and the SNB zone of interest before they abandoned this most recent chapter of the EURCHF intervention policy.

- Crypto is like the NASDAQ. It's a levered ecosystem full of speculative money.
- Bonds trade like a risky asset! This is not great for bonds and should have investors with 60/40 portfolios mildly trembling. 60/40 portfolio investors should consider EM bonds as a replacement for US fixed income unless they are hopeful on disinflation. Then again, US 10s make a lot more sense in a 60/40 portfolio now they're back at 2.0% so perhaps this is the worst possible time to extrapolate.
- Crude is trading like both an inflation and a geopolitical hedge. Or... A thing that goes up no matter what.
- AUD has no relationship to risk right now.

AUD is particularly interesting because if you look at the correlation of AUD to SPX since January 1, 2021, it's around 44% (correlation of daily changes) but if you chart that relationship, you get the graphic at right.

I highlight this because it's a great example of how correlation can be useless. Since correlation does not factor in magnitude of moves, you can have positive correlation and massive divergence like this, and hedging and correlation trading strategies can get blown out of the water.

To highlight this counterintuitive math fact, the second chart shows two series with 100% correlation (r-squared = 1), but one is going up and one is going down. Again, since correlation only cares about direction and not magnitude, you can get these counterintuitive situations where AUD and SPX are strongly correlated but not really moving together due to asymmetry of daily moves in each direction.

For trading I would say **the main takeaway is to forget about AUD, NZD, and EMFX as risky assets**. It's a reflex that is old and outdated. As we transition away from US exceptionalism, money is flowing out of overpriced US stocks and into cheaper alternatives and commodity exporters. TINA was a siren, calling investors towards the rocks (see final chart, bottom right).

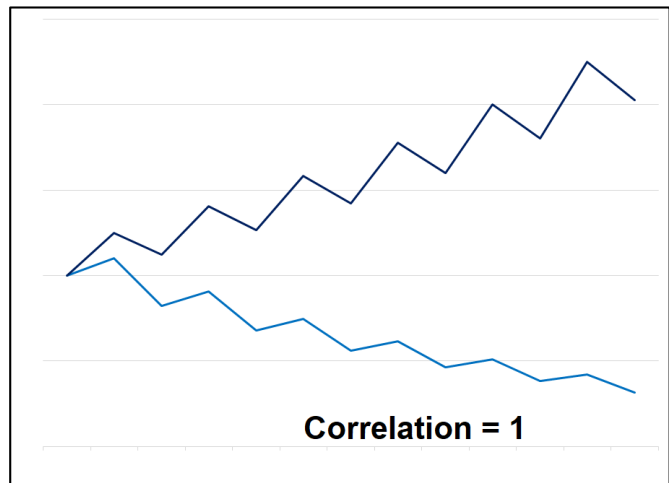
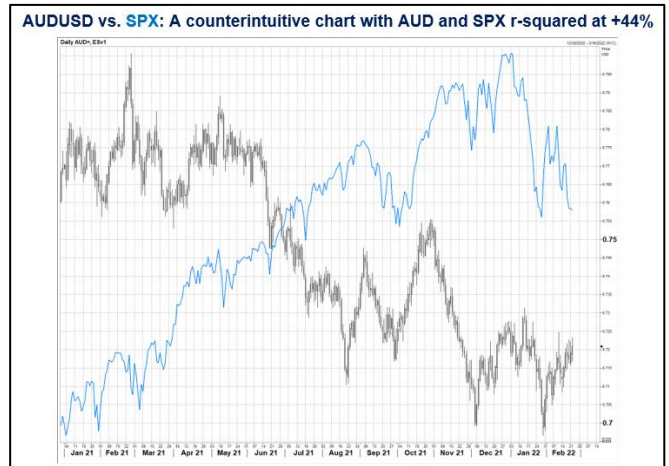
Trades update

The AUDCAD option has expired today, deep in the money with spot at 0.9183. The 0.9100 option cost 26bps so that was a good trade. AUD sentiment has become a tad exuberant with the miner dividends front and center in the conversation, but I don't see any reason to be bearish. Bullish or neutral still seems right in AUD and NZD. The USDJPY trade is fine; I will stick to the original plan though I admit it's hard to get excited about JPY in either direction.

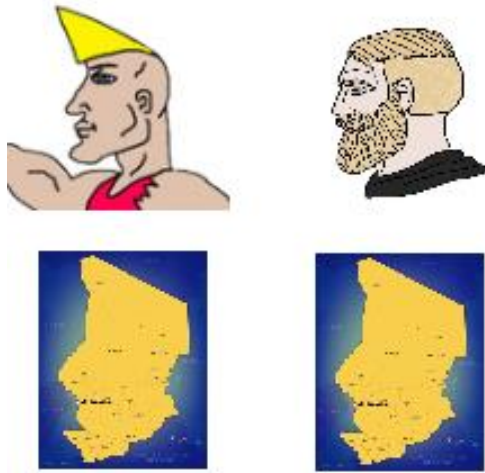
I am generally bearish USD as I think the money flow story will be negative for the USA going forward and Russia has been a USD-positive red herring. I am tempted to get short USDCAD here, but I will wait because **there is a chance we see a repeat of last month's mutant month end USD buying**.

Have a handsome day.

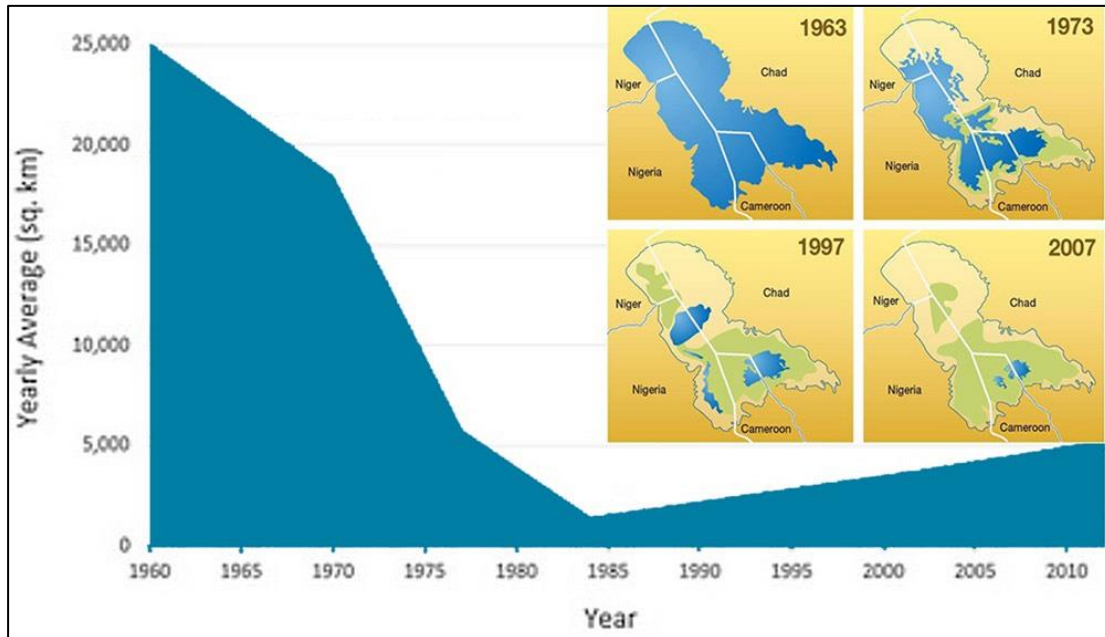
good luck ↑↓ be nimble



The Chad memes have heads shaped like the land-locked Republic of Chad



Chad fact 2: Lake Chad has receded significantly since 1963 but has remained stable for decades



<https://bigthink.com/strange-maps/95-the-incredible-shrinking-lake-chad-that-is/>

[Click here to subscribe to am/FX](#)

Markets and Trading Commentary Disclaimer

This material has been provided by Spectra Markets, LLC (“Spectra Markets”). This material is confidential and therefore intended for your sole use. You may not reproduce, distribute, or transmit this material or any portion thereof to anyone without prior written permission from Spectra Markets.

This material is solely for informational and discussion purposes only. Spectra Markets is not a registered investment advisor or commodity trading advisor. This material should not be viewed as a current or past recommendation or an offer to sell or the solicitation to enter into a particular position or adopt a particular investment strategy. Spectra Markets does not provide, and has not provided, any investment advice or personal recommendation to you in relation to any transaction described in this material. Accordingly, Spectra Markets is under no obligation to, and shall not, determine the suitability for you of any transaction described in this material.

To be clear: Your individual circumstances have not been assessed. You must determine, on your own behalf or through independent professional advice, the merits, terms, conditions, risks, and consequences of any transactions described in this material. Securities described in this material may not be eligible for sale in all jurisdictions or to certain categories of investors. This material may also contain information regarding derivatives and other complex financial products. Do not invest in such products unless you fully understand and are willing to assume the risks associated with such products. Neither Spectra Markets nor any of its directors, officers, employees, representatives, or agents, accept any liability whatsoever for any direct, indirect, or consequential losses (in contract, tort or otherwise) arising from the use of this material or reliance on information contained herein, to the fullest extent allowed by law.

The opinions expressed in this material represent the current, good faith views of the author at the time of publication. Any information contained in this material is not and should not be regarded as investment research or derivatives research as determined by the U.S. Securities and Exchange Commission (“SEC”), the U.S. Commodity Futures Trading Commission (“CFTC”), the Financial Industry Regulatory Authority (“FINRA”), the National Futures Association (“NFA”) or any other relevant regulatory body. The author is currently employed at a trading desk. The opinions may not be objective or independent of the interests of the author. Additionally, the author may have consulted with various trading desks while preparing this material and a trading desk may have accumulated positions in the financial instruments or related derivatives products that are the subject of this material.

Spectra Markets does not guarantee the accuracy, adequacy or completeness of the information presented in this material. Past performance and simulation data do not necessarily indicate future performance. Predictions, opinions, and other information contained in this material are subject to change continually and without notice of any kind and may no longer be true after the date indicated. Any forward-looking statements speak only as of the date they are made, and Spectra Markets assumes no duty to and does not undertake to update forward-looking statements. Forward-looking statements are subject to numerous assumptions, risks, and uncertainties, which change over time. Actual results could differ materially from those anticipated in forward-looking statements. The value of any investment may also fluctuate as a result of market changes.

Spectra Markets is affiliated with Spectra FX Solutions LLC, an introducing broker that is registered with the NFA; Spectra FX Solutions LLP, which is a registered entity with the U.K.’s Financial Conduct Authority; and SpectrAxe, LLC, a swap execution facility that is currently in the process of registering with the CFTC. The disclosures for Spectra FX Solutions LLC and Spectra FX Solutions LLP related to the separate businesses of Spectra FX can be found at <http://www.spectrafx.com/>.