SPECTRA MARKETS

Monday, March 14, 2022

Always and everywhere

Happy π day. There are certain flawed stimulus/response muscle memory speculator behaviors in markets that are incredibly difficult to unlearn. One of those is “sell USDJPY on weak equities.” This pervasive habit comes from the two-step empirical process that often <u>but not always</u> plays out like this: 1) bonds are usually a safe haven 2) USDJPY trades in line with interest rates 3) when stocks get hit, bonds rally and USDJPY falls.

Since bonds often rally on equity weakness, it feels sensible to sell USDJPY when stocks sell off. But whenever bonds are <u>not</u> trading as a reliable safe haven (like now) … The transmission from step one to step two is broken, and USDJPY has no corr to equities.

While cross/JPY almost always has some beta to equities, the driver of <u>USDJPY</u> is US interest rates. This was true in 2007 when Bear Stearns got bailed out and the Fed cut the discount rate (USDJPY sold off because of the rate move and ignored the equity rally). And it’s true in 2022 during an inflation scare and supply-shock / war. **USDJPY is always and everywhere a rates phenomenon.** Yes, if stocks and bonds are positively correlated, JPY will appear to be correlated to stocks. But that correlation is illusory and driven by a third variable.

Here’s USDJPY correlation since 2021 and since January 2022:

USDJPY correlation to various markets, served two ways

		01JAN21 to now	01JAN22 to now
Rates *corr to price, not yield*	US 2 year	(0.49)	(0.40)
	US 10 year	(0.51)	(0.56)
	EDZ3	(0.53)	(0.55)
	BAZ2	(0.58)	(0.39)
Equities	S&P 500	0.07	0.06
	NASDAQ	0.05	0.01
	Russell	0.08	0.12
Other	Bitcoin	0.24	0.04
	NYMEX Crude	(0.06)	0.16

I know many people understand this but still… I keep getting the question: “Why hasn’t USDJPY sold off? There’s a war gosh darnit!” That question is valid only insomuch as this question is valid “Why have bonds not rallied? There’s a war gosh darnit!”. I suppose the ex-post answer to that second question is pretty obviously that the war is triggering an explosive commodity rally, which is inflationary.

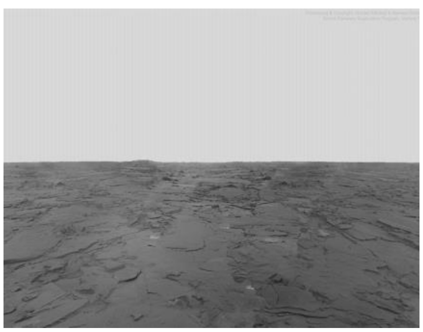
Lifers and oil importers bought USDJPY again overnight and both EURUSD and USDJPY have now made big moves on low spec participation. First EURUSD (down) and now USDJPY (up) have been driven by large real money and hedging flows. March 15 and 16 are seasonally two of the worst days of the year for USDJPY and with FOMC Wednesday there's not much point chasing the USD higher here unless you have a strong view on the Fed.

am

FX

Brent Donnelly

bdonnelly@spectramarkets.com
(212) 398-6230



The surface of Venus

Current Views

Flat

My view is that FOMC risk is hawkish as the market is leaning toward fear which makes dovish feel more natural. ECB showed the way, trying to at least pretend the inflation targets still matter. I think in times of risk aversion our natural inclination is to believe the Fed will bail us out. That is, we subconsciously or consciously think they will be dovish in the face of risk aversion. But the current fear trade is an inflationary sort of risk aversion and rates are recklessly low.

SNB

The SNB bought about 2 billion EURCHF last week to stabilize the pair (probably near 1.00). The action is somewhat meaningless as it runs opposite to monetary policy and is not likely to be market stopping for long. The last time there were headlines about SNB sight deposits increasing was January 10th at 1.0400 in EURCHF.

Inflation is above the SNB cap so huge intervention is not in the mix. Occasional smoothing sure, but nothing more. Whether you are bullish or bearish EURCHF, I don't think the SNB purchases change the story.

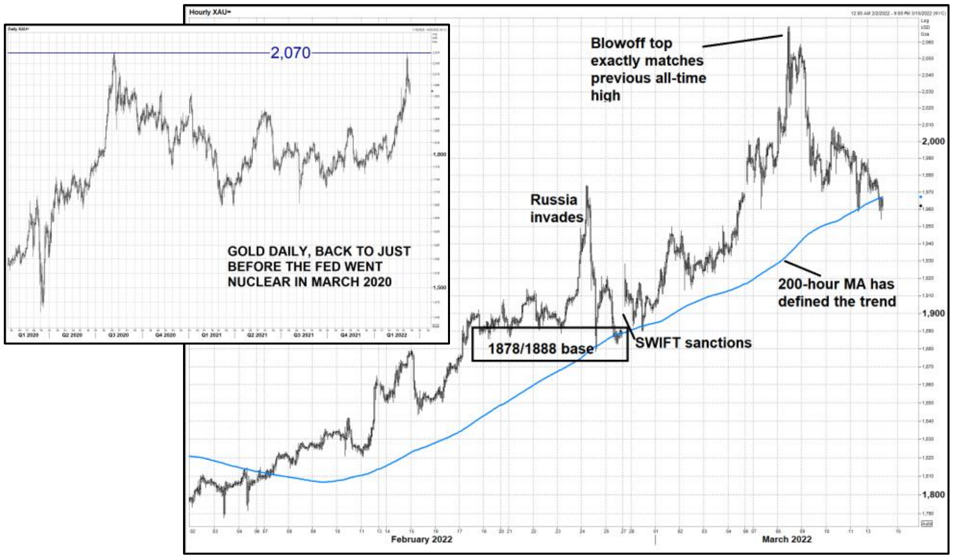
Gold

There is a tricky timing mismatch in gold right now as many in the market are long on a persuasive multiyear thesis: "FX reserves are not money so China will be selling their USD reserves to buy gold and protect themselves". This is probably an investable theme in the long run (sell paper, buy hard assets) but these can be really hard to trade as some specs want the 10-year upside with a 2% stop loss. Also, if the idea is wrong, you never really know when to bail because it always just feels like you're early, not wrong.

Chart-wise, it's interesting: we made a perfect double top at 2070. The first top was on Fed behind the curve / inflation fears in mid-2020 and the second top touched 08MAR on the Russia / sanctions fears. The bulls are still in control for now but a move through 1920 would be problematic and a drop through 1878/1888 looks fatal.

Here is the hourly chart, with some important points marked and a daily chart embedded top left so you can see the double top in all its glory. The 200-hour moving average has been a good measure of slope for this rally and you can see we have now spent four straight hours below it. The major equilibrium zone before and after sanctions were announced was 1878/1920 so that is really the mega support now.

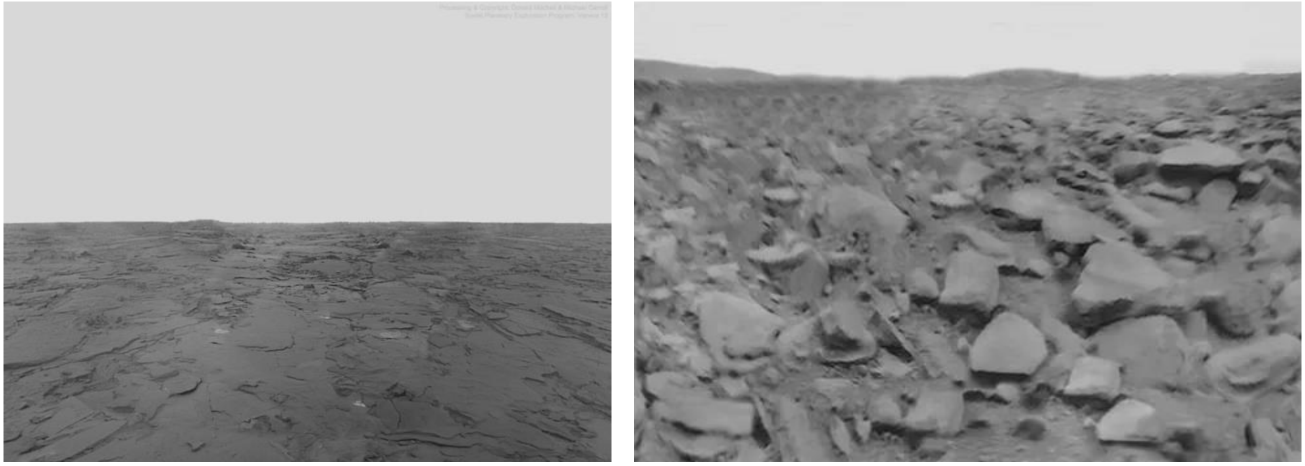
The gold hourly chart shifts from bullish to neutral



I'm between strong views right now as my guess is that the USD continues higher into and through the Fed, but the entry points are not good and I whiffed on the USDJPY higher trade. Have a galactic day.

good luck ⇅ be nimble

Venus from 12000 miles out



The surface of Venus

[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/.