

am  
FX

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## Current Views

**Short USDSEK @ 9.8350**

Stop loss 10.0110  
Take profit 9.5510

**Long AUDUSD @ 0.7135**

Stop loss 0.7049  
Take profit 0.7245

## Plotting the Fed

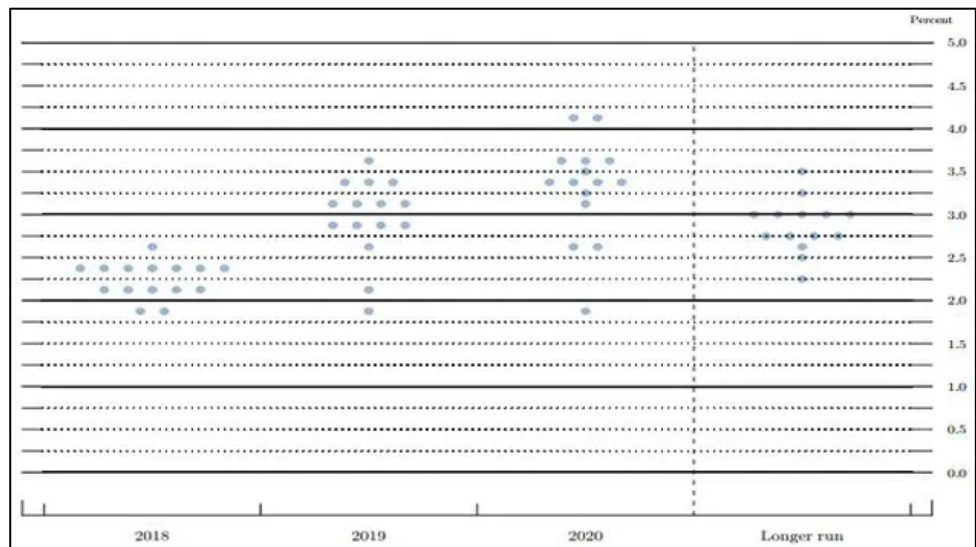
I continue to believe that today's FOMC meeting will sound dovish relative to the hawkish psychology going in. This does not mean the Fed will pause its hiking campaign or push back on pricing, it just means that there is a lot of tightening in the market and the Fed has regained some credibility.

My mantra throughout this cycle has been that the market determines the pace and timing of hikes more than the Fed. Though obviously there is an interplay between Fed communications and market pricing, the Fed hiked 25 in March because 25 was priced and they will hike 50 today because 50 is priced.

Also, my belief is that this normalization cycle will consist of two stages. First, the Fed wants to get to neutral and then reevaluate financial conditions and inflation at that point. Then, they will go to restrictive much more hesitantly as the system is so heavily geared to low rates. Restrictive policy brings much greater danger than the return to neutral. Whether the second stage (moving to restrictive rates) ever happens is a valid question. For now, the first stage is to get to neutral, then chill.

In 2018, the neutral rate according to Fed communications at the time, and the median of the longer-run dot on the Fed's dot plot, was 3.00. [This post by Dallas Fed hawk](#) suggested 2.75/3.00 as neutral. Here is the dot plot from the June 2018 meeting:

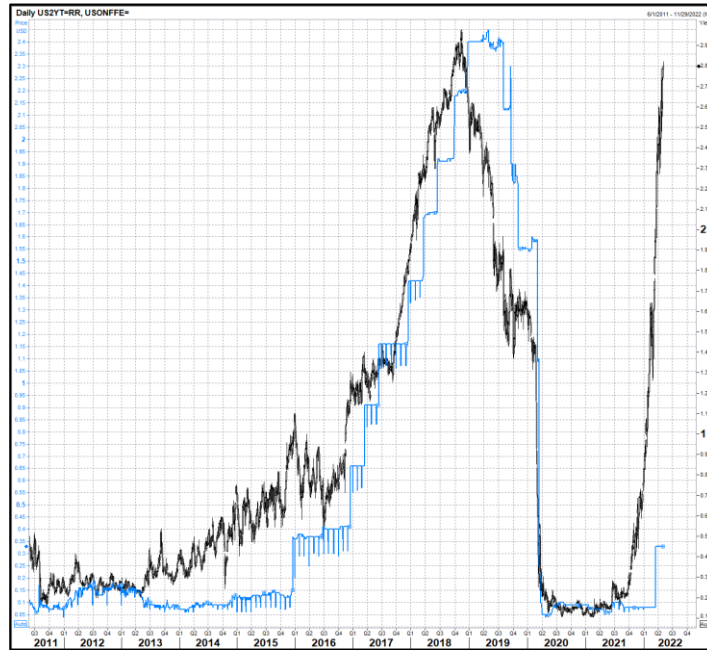
Fed dots in June 2018



Not coincidentally, US 2-year yields peaked at 2.977%. Now, the neutral rate is thought to be closer to 2.5% and US 2-year yields are already 2.8%. As such, I think it's tough to get much more juice. If Fed policy is simply following 2-year rates, we are at a point where it will require something new and significant to trigger another leg higher in US rates.

On the next page, I show a chart of 2-year yields and Fed effective. I think the most likely scenario now is a period of digestion where 2-year yields consolidate in the 2.6/2.9 zone as we try to figure out what's next. This would be in contrast to the persistent series of substantially higher monthly yield moves this year. 2-year yields jumped 42bps in January, +25 in February, +88 in March, and +39 in April. My guess is we end May with no change in 2-year yields (i.e., close the month around 2.75%).

## US 2-year yield vs. Fed Funds Effective rate, 2011 to now



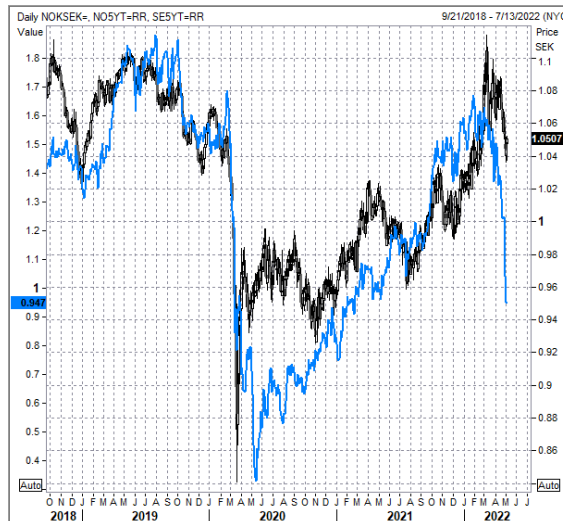
You can see how 2-year yields show the way for Fed Funds.

My dovish FOMC view yesterday got mostly negative feedback as the data do not support a dovish Fed. JOLTS, especially! The thing is, the Fed has regained a certain amount of credibility at this point and expectations are hawkish. I don't think the message will be outright dovish, but it will be measured enough to douse the fires of risk aversion and trigger a relief rally. Again, market psychology into this Fed meeting is wholly different from where it was.

If you agree with me, best candidates for a relief rebound are: USDSEK lower, AUDUSD higher, NZDUSD higher, NASDAQ higher and BTC higher. The dollar looks expensive relative to rate differentials in many pairs, specifically AUDUSD and USDSEK.

People asked yesterday why I didn't choose USDNOK instead of USDSEK and the answer is: "rates". Norway is further into their cycle while the Riksbank is just getting going. This is most clear when you look at NOKSEK vs. rates:

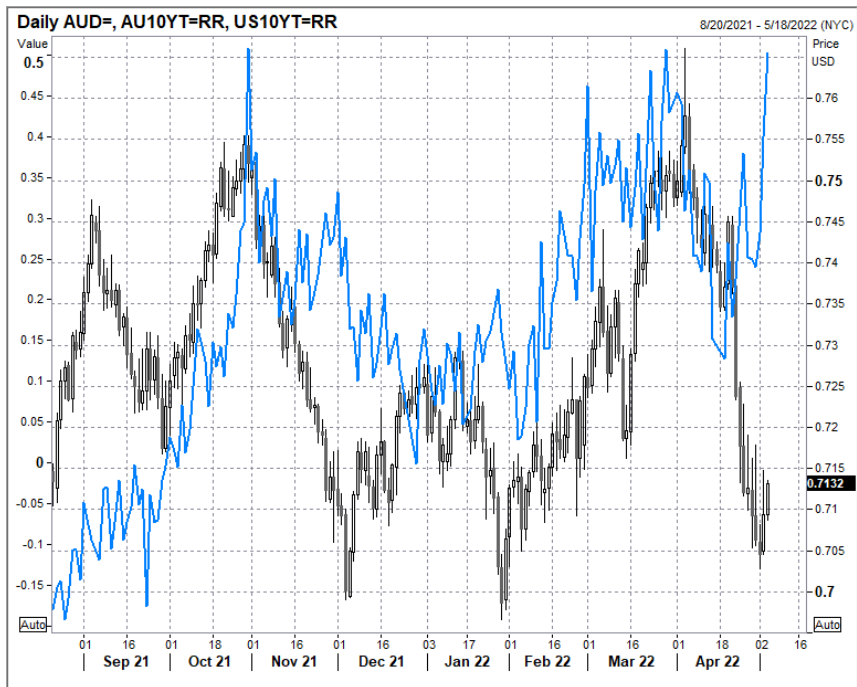
## NOK/SEK vs. Norway/Sweden 5-year rate differential



**One more chart**

Here's AUDUSD vs. 10-year rate differentials as another example of how the USD appears to me to have overshot. **I added long AUDUSD as another dovish Fed trade.** Full details in sidebar on page 1.

**AUD/USD vs. AU/US 10-year rate differential**



**Self-awareness**

Someone sent me an email about gold miners yesterday. Here is what he wrote before the analysis that he sent over:

I'm not a huge fan of this sentiment service, since a lot of what they do is financial market technical trivia with half-assed conclusions, but since this one fits my gold bias, I like it!

I thought that was a good example of self-awareness. The person knew they were suffering from confirmation bias, but were aware of it, and sent it over. Funny.

**Closing thoughts**

Check out [my latest crypto piece](#), where I interview Gemini VP of Trading, Clark Read. He comes from a traditional finance background and as such, his insights are useful if you are at the intersection of the TradFi/Crypto Venn.

Have a surprising day.

good luck ↑↓ be nimble



*Doh*

Man who never wanted to ride in fighter jet accidentally ejects himself

<https://www.mercurynews.com/2020/04/13/man-who-never-wanted-to-ride-in-fighter-jet-accidentally-ejects-himself/>

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