



# Can Crazy-Calm Continue?

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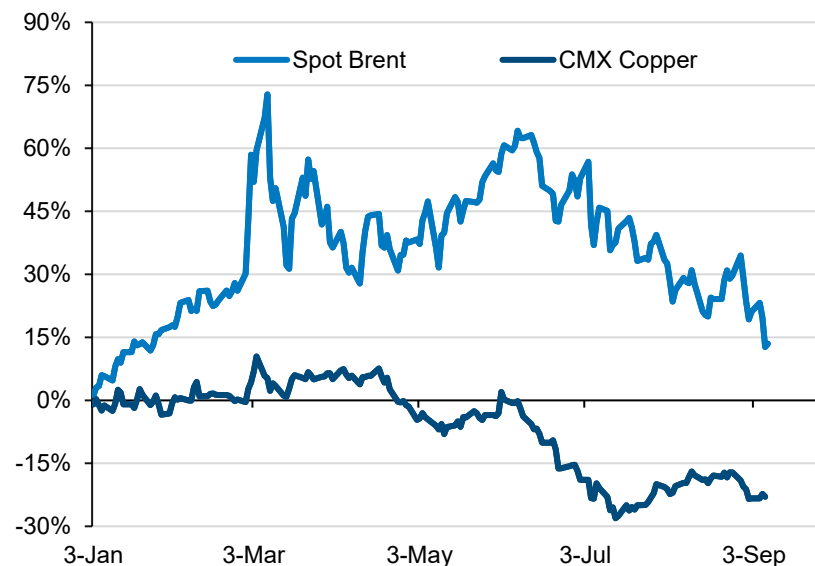
# Crazy Price Action in FX-Related Macro Markets

## MSCI World and WGBI YTD Returns



Sources: BMO CM, Bloomberg

## Spot Brent Crude and COMEX Copper Prices

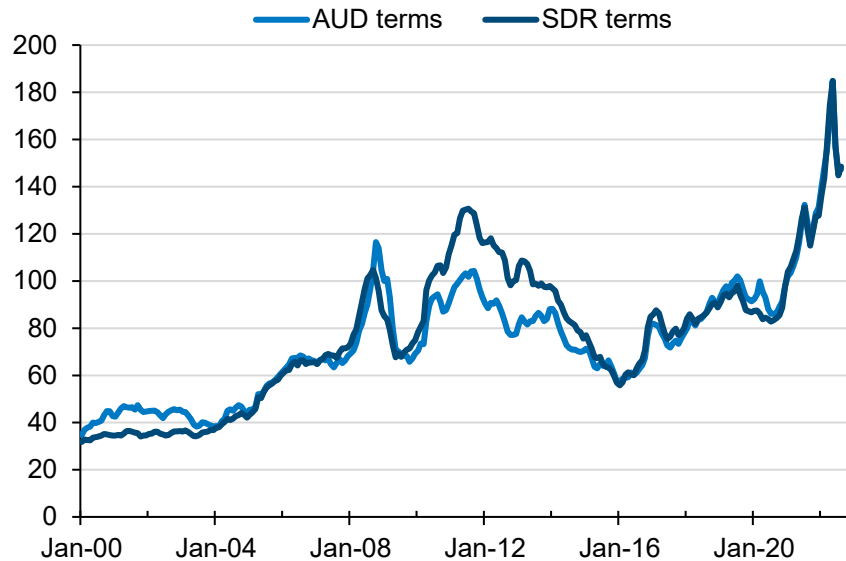


Sources: BMO CM, Bloomberg

- **FFZ2 was** at 99.24 (**0.76%** Dec-22 Fed Funds rate) on 31-Dec-2021; **yesterday** it closed at 96.33 (**3.67%**)
- **MSCI World** (USD-denominated) return **-17.5% YTD** through 07-Sep (not including dividends)
- **WGBI** (USD-denominated) return **-18.3% YTD** through 07-Sep (not including interest)
- **Brent** \$77 on 03-Jan, \$138 intraday high on 08-Mar 8, \$120 June average, \$87 on 07-Sep
- **Copper** \$446 on 31-Dec, \$493 on 04-Mar, \$321 on 14-Jul, \$344 on 07-Sep
- **XBT** \$47.3k on 01-Jan, \$48.2k on 28-Mar, \$17.6k on June 16, \$19.4k on 07-Sep

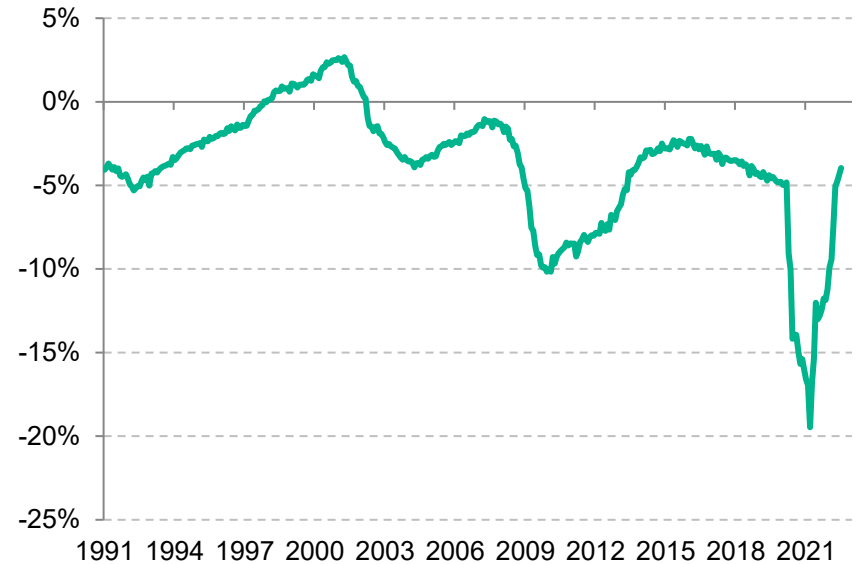
# Many Crazy Developments in Traditional FX 'Fundamentals'

## RBA Export Commodity Price Indices



Sources: BMO CM, Bloomberg, Reserve Bank of Australia

## US Federal Budget Balance (rolling 12M % of GDP)



Sources: BMO CM, Bloomberg, US Treasury

- **Full-scale war** in Ukraine with tens of thousands of casualties and unreliable news about war developments
- US and Europe attempt to **seize and freeze Russian assets** and bankrupt major Russian institutions
- **Boris Johnson and Mario Draghi exit stage left** while Jair Bolsonaro threatens to not exit if he loses in re-election
- **FOMC's median end-2022 dot** goes from 0.9% in December to 3.4% in June (and probably higher in 2W)
- **Inflation** in the UK hits triple digits (July CPI 10.1% YoY)
- **Eurozone** develops its first **trade deficit** in 10 years (monthly deficits in April, May, and June with June's -USD131bn)
- RBA's **commodity export price indices hit all-time highs** 40-50% beyond previous highs from 2008 and 2011
- The **US's rolling 12M federal budget deficit** closes to just USD962bn or 4.0% of GDP in July from USD4095bn or 19.5% of GDP in March 2021

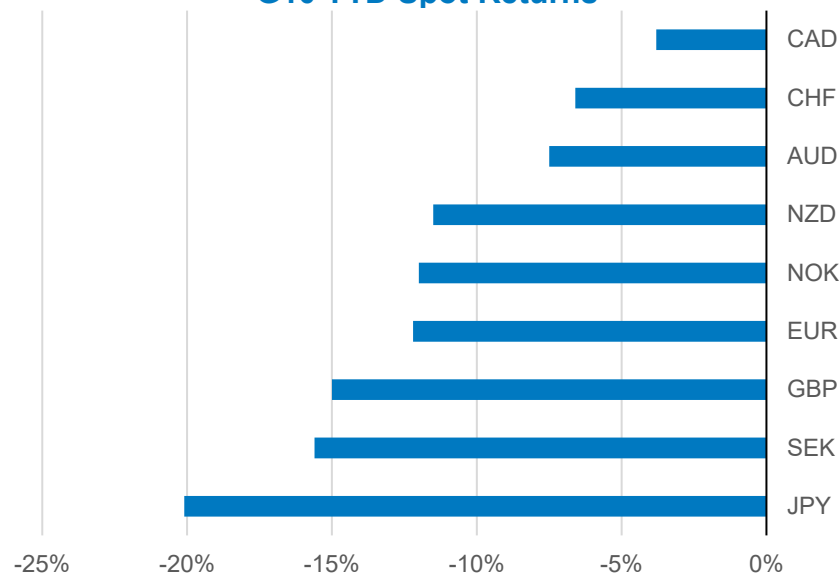
# Big Gains and Historic Levels for the USD

## Fed's Monthly Broad Real Trade Weighted USD Index



Sources: BMO CM, Bloomberg, Federal Reserve

## G10 YTD Spot Returns



Sources: BMO CM, Bloomberg

- **BBDXY up 11% YTD** and 16% since the June 2021 FOMC
- **Fed broad real USD index** at a new high since 1986 and presently **17% above** its post Bretton Woods **average**
- FX Majors **sticker shock**: EURUSD below 1.00; GBPUSD below 1.15; USDJPY to 144.99
- All G10 currencies showing declines against the USD with **JPY** showing a **20% decline** (despite risk-off)
- A **myriad of USD-positive factors** at play in 2022: Risk-off, Fed-on, energy independence, FDI/reshoring inflows, twin deficit improvement

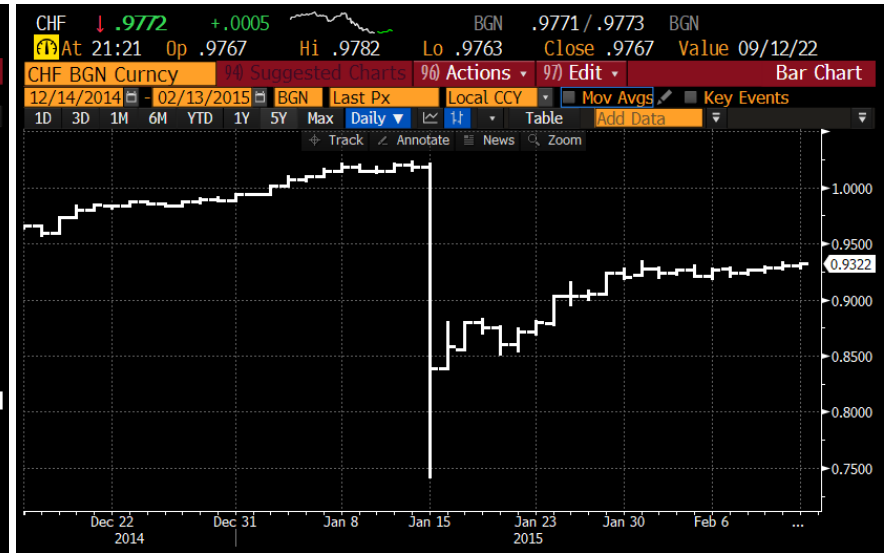
# But No Historic 'Fireworks' Events in G20 FX (yet)

## GBPUSD in the 48H Surrounding 2016 Brexit Vote



Source: Bloomberg screen pic

## USDCHF in the 2015 EURCHF Floor Removal



Source: Bloomberg screen pic

- Over the past decade, we have seen **10%+ intraday moves** in major currencies.
- The **Brexit vote** move in GBPUSD was from 1.50 to 1.32 within the span of a few hours.
- The **SNB removed the EURCHF floor** was from 1.20 to 0.74 within the span of a few hours.
- This year's responses in major currencies to **shocking monetary news and shocking geopolitical news** have been tepid in comparison.
- **USDPJY implied 1M vol** has evolved from around 6 at the start of the year to about **14 now**, but it **was 25+** after similar spot moves in **1998**. It reached 38 in Oct-08 and 21 in Mar-20.
- **EURUSD cross currency basis** from the FX forward markets has been **tame** relative to Q4 2019, let alone previous crisis periods.
- In G20 currencies, **extreme FX pressures** have really **only** been seen in **RUB**. Even TRY has been well ordered.

# Could USDJPY do a 1998 Repeat?

USDJPY Daily Bar Chart for Mar-Dec 1998



Sources: BMO CM, Bloomberg

USDJPY Daily Bar Chart for Mar-Dec 2022

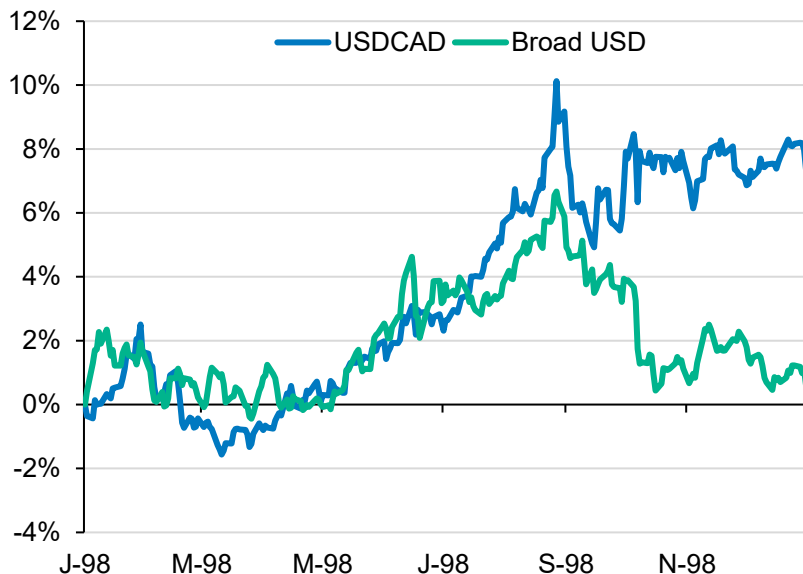


Sources: BMO CM, Bloomberg

- In **1998**, the USDJPY exchange rate moved from **125 in early March** to **147 in August**
- It turned out the move was **speculative excess** when USDJPY **dropped from 135 to 111** in less than a week
- In **2022**, the USDJPY exchange rate has moved from **114 in March** to **144.99 in September**
- In **2022**, there are **no signs of speculative excess** in CFTC Commitment of Traders data on leveraged funds and bank prop desks are a relic of the past
- Implied vols and risk reversals aren't hinting at a market beset by speculative excess
- Japan was a **trade surplus country in 1998** but it is a **trade deficit country in 2022**
- A repeat of 1998's hard reversal seems highly unlikely, but **who really knows what would happen if a sudden financial institution failure were to cause the Fed to cut its base rate?**

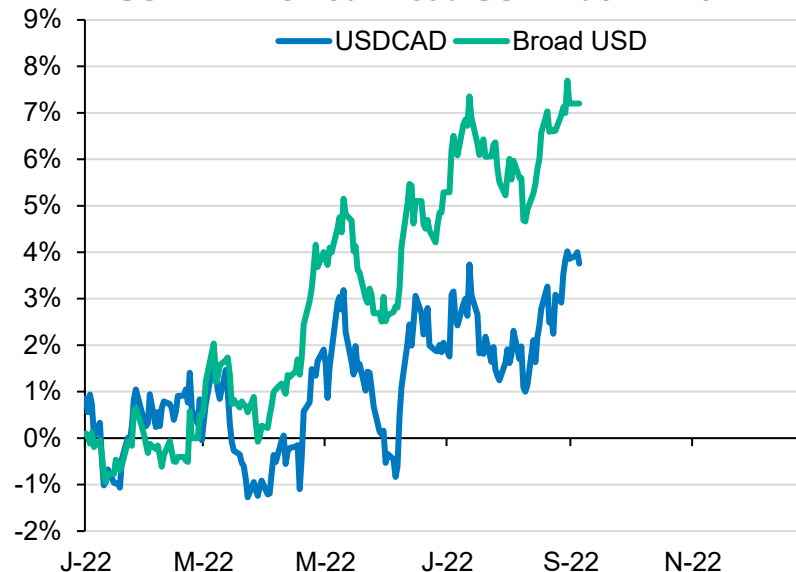
# Why USDCAD is so Different in 2022 from 1998

USDCAD vs Fed Broad USD Index in 1998



Sources: BMO CM, Bloomberg

USDCAD vs Fed Broad USD Index in 2022



Sources: BMO CM, Bloomberg

- In **1998**, USDCAD moved 8% higher through Q3 while the Fed's broad USD index moved 4% higher. The annualized daily standard deviation for USDCAD was 6.1% while for the index it was 5.5%. **Canadian peso jokes were prevalent** in the FX market.
- In **2022**, USDCAD has moved 4% higher through early September while the Fed's broad USD index is up 7%. CAD is the best performing G10 currency, although USDCAD realized volatility is still higher than the index's at 7.5% vs 5.8%. Canada and the **loonie s increasingly seen as a safe haven**.
- **Canada was a fiscal mess in 1998**. It ran central government budget deficits of 4% of GDP or greater from 1982 to 1996. The IMF has net government debt at 59% of GDP in 1998. **For 2022, Canada appears to be a poster child of fiscal discipline** with net debt-to-GDP at 33% and deficits below 4% for the century until the pandemic.
- Canada was a net **debtor country in 1998**. It is a huge **net creditor country now**. With that in mind, CAD outperformance during risk-off makes sense. It does not seem to be due solely to hawkish BoC or to oil.

# So Can Crazy-Calm Continue?

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- An old market saying in reference to central bank liquidity is that ‘a rising tide lifts all boats’
- The mirror reflection of that adage is that ‘a receding tide sinks unstable boats’
- While the tide has begun to recede and no FX boats have sunk yet, [mariners beware](#)
- The displacement of one ship sinking on a crowded sea can perturb waters in unpredictable ways
- Seemingly stable ships can be dragged under in such an instance
- When surveying other ships above the surface, it’s hard to know which have unstable hulls (even for central banks)
- [Crazy FX fundamentals and calm FX market dynamics may not be able to cohabitate much longer](#)
- USDCAD seems an unlikely avenue for crazy FX action, but watch your CAD crosses



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