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DailyFX

Weekly Range-Breakout Barometer

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Implied volatility is one of the most tried and true methods for objectively measuring expected volatility in the spot market. Derived from currency options with different maturities, implied volatilities are used to help predict potential movements in the spot market and is one of the most popular strategies of systems traders and other professional hedge funds.

At its most fundamental, the basic and intuitive interpretation of this implied data is often the most telling for traders. Taken alone, a steady rise in the longer-term implied volatility (**the red line**) is indicative of a strengthening trend; while inversely, a decline often reveals that a period of range or consolidation in spot is ahead or already in place. Additionally, the histogram or spread between the shorter and longer-term implied volatilities (**the blue colored bars**) tells a different perspective. As the histogram rises, volatility is expected to pick up faster in the near future relative to the longer-term range. Ultimately, this increases the probability of a breakout scenario in the underlying currency.

Volatility Situation

Currency	Spot Price	Barometer Reading
EURUSD	1.3513	**Breakout**
GBPUSD	1.9769	**Breakout**
USDJPY	120.77	**Breakout**
USDCAD	1.1032	**Range**
AUDUSD	0.8242	**Range**

EURUSD

Implieds continue to fall in both the long and short term, leaving the suggestion of a breakout in the underlying euro currency pair intact. For the week, price action has remained relatively rangebound, teetering between both the 1.3500 and 1.3600 figures, failing just above the resistance ceiling in mid week action. Long terms have dipped to 5.28 percent, 10 basis points lower than the 5.38 seen last week, with short term vols paring back quite a bit. Previously trading above the zero line at 22 basis points wide, the differential now has plummeted to trade 38 under the zero line. As a result, market traders will likely continue to focus on cheap implieds, as a break of either current support and resistance may help to inject some energy.

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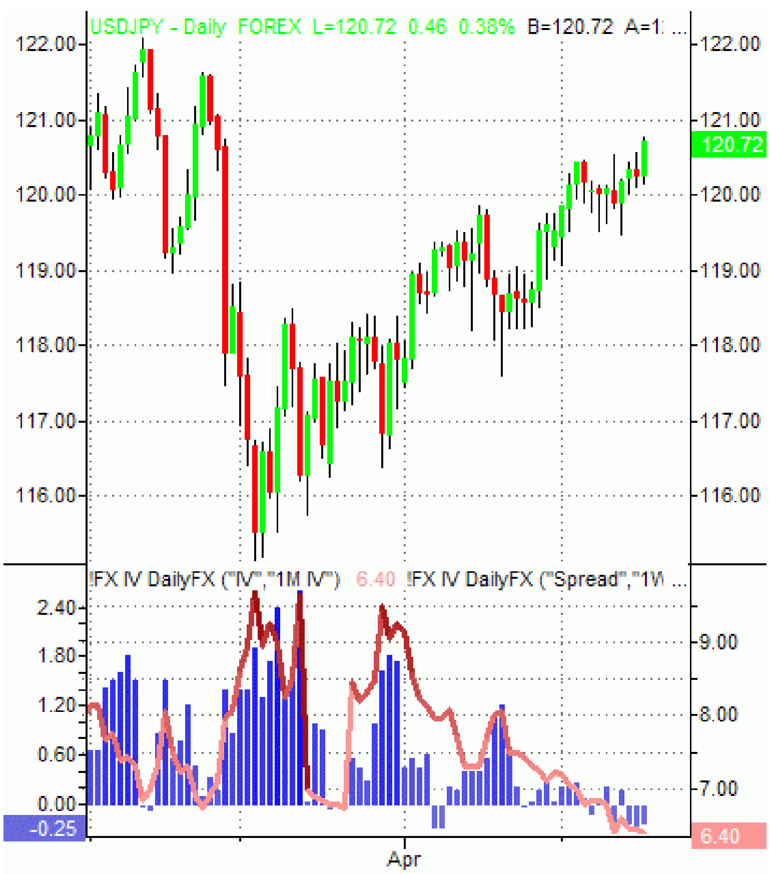
GBPUSD

Sterling implieds additionally remained relatively grounded, coming in at an unimpressive 5.7 percent versus the 5.85 that was witnessed last week. Subsequently, the short long differential also remained underwater, trading at 30 basis points in favor of the longer term. Given the rather expected decision by the central bank last week, current conditions are a simple reflection of the rather lackluster round of day over the course of the week. However, some interest may be rounded up as the schedule offers UK retail sales data ahead of the weekend, expected to come in rather supportive. Extremes in the figures would help in supporting some activity in the underlying currency. However, it seems that the current technical support or resistance will need to be broken in confirming the underlying model suggestion.



USDJPY

Japanese yen volatilities plummeted to far below the previous week's measurement, pricing in at 6.4 percent compared to last week's 6.9 percent. Incidentally, the differential has also turned lower, trading at 25 basis points wide on weaker short term figures. The suggestion, combined with the rather range bound trading in the currency pair, is adding to the underlying sentiment that a further breakout or breakdown may be expected in the short term for the currency. The notion will be put the test as the Bank of Japan is expected to announce their rate decision in the overnight, adding to speculation of a near term rate hike decision.

USDCAD

After predicting the lengthy fall in the underlying currency, our volatility model purports a likely consolidation phase in the USDCAD currency pair as traders position themselves on the string of positive Canadian economic data. However, with the pair already moving at an extreme pace, there remains the higher likelihood that the currency pair will be restricted to a more range bound environment. The implied suggestions confirms the notion as the longer term component continues to remain lofty at 6.33 percent with the short long differential coming in slightly lower at 17 basis points wide. However, further activity should not be precluded, especially on a break of the 1.1000 figure.

AUDUSD

Aussie vols have pulled back considerably as the underlying currency remains in a relatively range bound environment. Although the swings are wide, the underlying price action has been restrained in the longer term, putting the wave length in perspective. For the record, the component is considerably lower than last week's print, dipping to 7.35 percent as the short long differential trades 5 basis points wide on the week. Although neutral, lending to the range bias, a short term pop may be in order as the currency is coming up on 8200 support tests. Should the level fail to hold, we may have a revisit of the jump in price action all but two weeks ago.

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