



# DailyFX

## Weekly Range-Breakout Barometer

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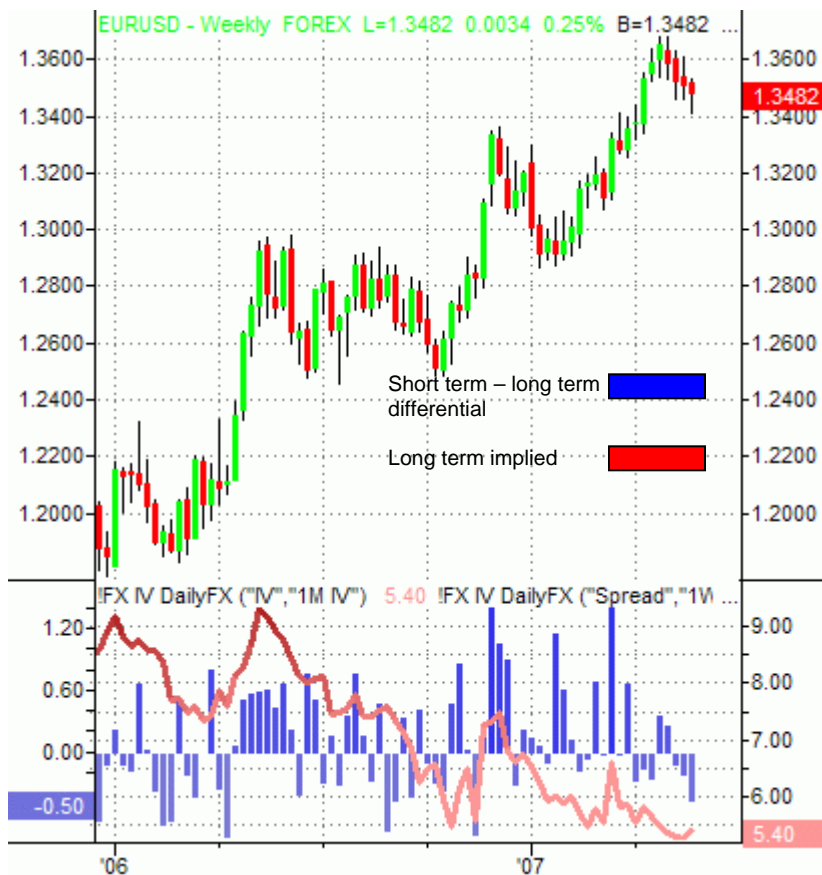
May 23, 2007

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	1.3480	Breakout
GBPUSD	1.9876	Breakout
USDJPY	121.55	Breakout
USDCAD	1.0815	Range
AUDUSD	0.8247	Range



### EURUSD

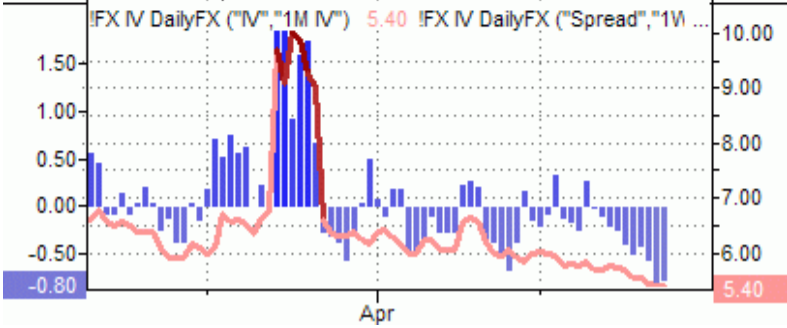
Euro implies perked up during the course of the week, with the longer term measure rising to price at 5.4 percent, slightly above the 5.28 percent figure from last week. Incidentally, with the shorter term taken aback slightly, the long-short differential dipped below the zero line, to price in at a negative 50 basis point wide spread. Given the extreme drop in the implieds over the past year, both components continue to suggest a short term breakout scenario formulating. As a result, technical levels at this point will serve crucial, notably with the price action hovering at the 1.3600 figure in the near term. Event risk will likely boost the measure next week when traders focus on inflationary data scheduled for next week.

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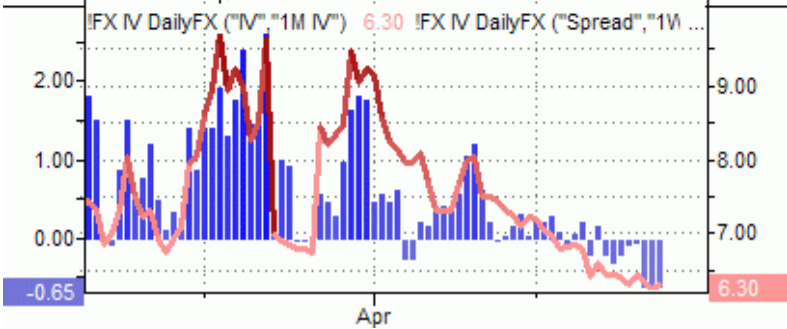
**GBPUSD**

Implieds on both components reached extremely low levels, helping the underlying spot price to pop in the thin market condition in the New York morning. Still low, the longer term component remains under water at 5.4 percent. With the short term measure dip over the course of the week, the long-short differential now stands further below the zero line, trading a negative 80 basis points wide. Subsequently, the continued softness in the measure lends to further notions of a breakout in the pound sterling. Technical formations are in line with the notion as the current channel looks to be broken to the upside, injecting some activity into the currency pair. Event risk will likely rise on the expectation of next week's manufacturing reports.



**USDJPY**

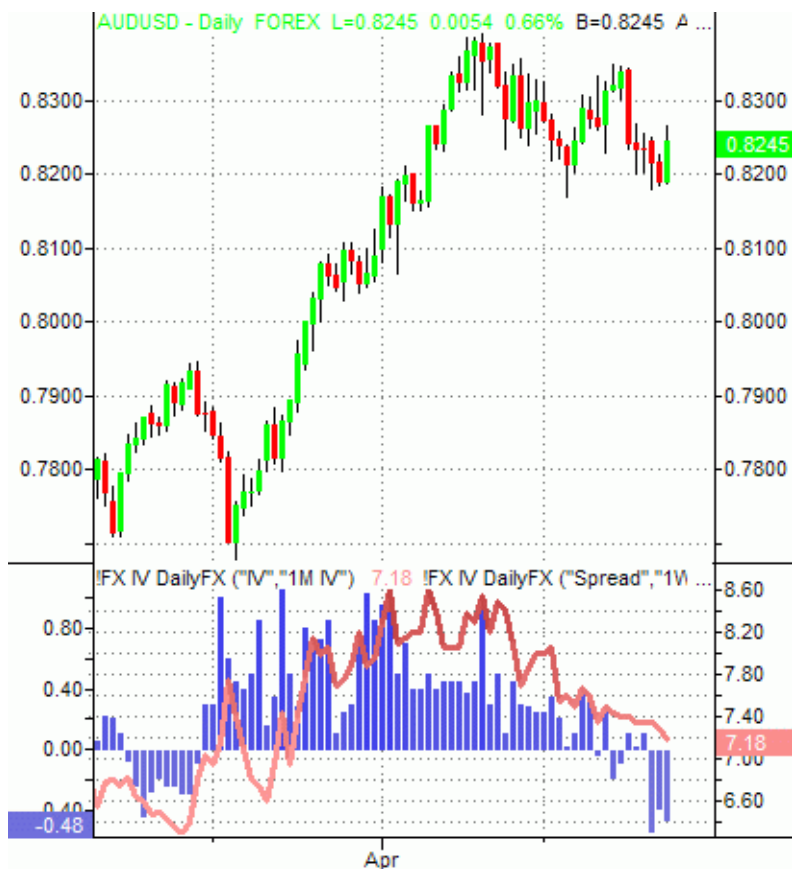
Breakout suggestions also remain in the USDJPY currency pair as implieds continued lower in both aspects of the spot price. Short term vols plunged lower on the week, by almost 40 basis points to trade at a negative 65 wide spread against longer terms. Incidentally, long terms additionally continued lower in the week, down another 10 bps to trade at 6.30. The implied picture, in tandem with both the EUR and GBP, is setting the spot up for a breakout scenario as a result, in conjunction with technical levels. Currently, traders continue to eye the 122 figure as major resistance, and will likely spark some activity on a break above or failure below. Manufacturing and sales data sets up next week's event risk.





## USDCAD

Implieds peaked over the last five sessions following increased speculation that the Bank of Canada may elect to raise interest rates towards the end of the year. However, the jump was most reflected in the longer term, with short term implieds plunging through the floor. Now, longer terms look to be consolidating at the 6.4 percent, with the long-short differential trading slightly lower by 10 basis points below the zero line. Although the implied picture is lending to a more consolidative tone, there remains a chance for some upside room heading into next week. Helping the notion to become a reality is the upcoming Bank of Canada rate decision. Although most suspect an unchanged benchmark, speculation and volatility would revisit upside should there be any changes.



## AUDUSD

Although dipping well below the 0.8300 figure, the Australian dollar remains in relative consolidation ahead of the 0.8200 level in the near term. Subsequently, well in line with expectations from last week, price action has remained restricted as the vol measure on both components continue to decline from extremely high levels. Longer terms have incidentally pared back for the week quite a bit, now trading at 7.18 percent. The decline in short terms on lackluster activity in the pair has also helped the long-short spread narrow significantly, now trading 48 basis points wide on the side of short term weakness. With still a ways to go, consolidation, and as a result ranging conditions, are likely to persist at this point. However, with plenty of manufacturing data on the horizon for release, short term jumps won't be precluded.

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