



May 2023

FX Market Structure Monthly

CHANGES IN SPREAD AND VOLATILITY FOR MAJOR MARKET PAIRS

Are rising rates impacting FX spreads? In May, we observed the second consecutive month of significantly narrower spreads across the 23 pairs that we monitor, accompanied by a smaller but noticeable decrease in intra-day volatility. These developments appear to be more than a seasonal shift associated with the arrival of summer. Notably, central banks in the EU, US, Australia, New Zealand, Britain, Norway and Sweden have tightened rates since April 1. We speculate that these adjustments have reduced the risk associated with dealer inventory, allowing them to provide narrower spreads to traders. As a result, market participants are experiencing improved trading conditions and potentially benefiting from the reduced transaction costs.

READING THE RESULTS

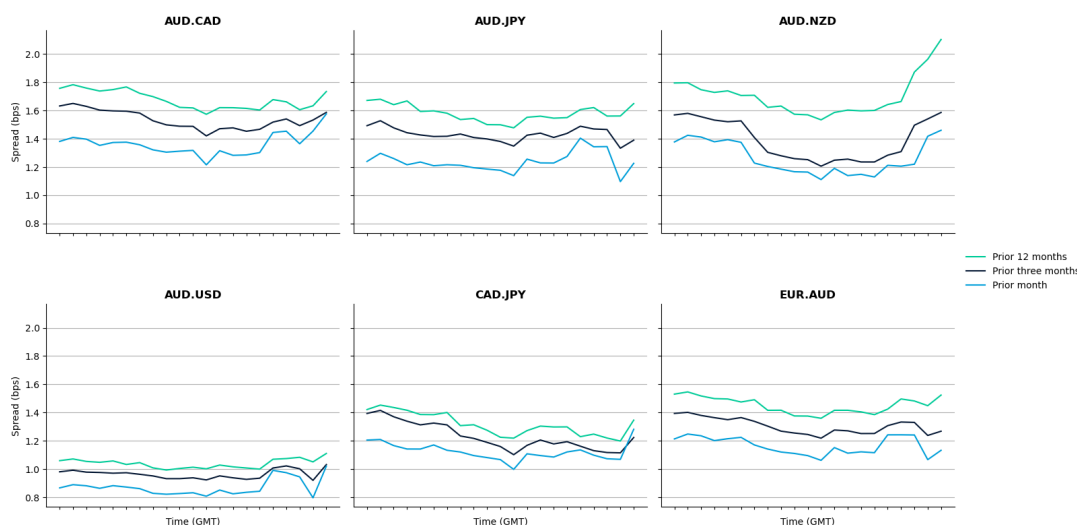
On the intraday charts, the green line represents the average spread or volatility for the past 12 months, the black line represents the past three months, and the blue line represents the past month. On the daily charts, the green area represents the 95th percentile confidence interval for the spread and volatility, showing the stability of the calculated median value.

SPREADS

On an intraday basis, spreads narrowed for all pairs that we monitor except EUR/USD, which saw spreads quoted about 2.5 pips wider throughout the London and New York trading hours. The AUD pairs recorded the largest tightening in spreads. In comparison to the other six major pairs, spreads were an average 10 pips narrower than in April. Looking at the 12:00-16:00 GMT trading window, only the EUR/USD recorded wider spreads compared to May. As mentioned in last month's note, intra-day spreads in May were narrower than six months ago for all pairs. During the pre-WMR trading window, spreads in May were narrower than three, six or 12 months ago for all pairs.

G-10 Currency Pairs: Average Hourly Spread, 00:00-20:00 GMT

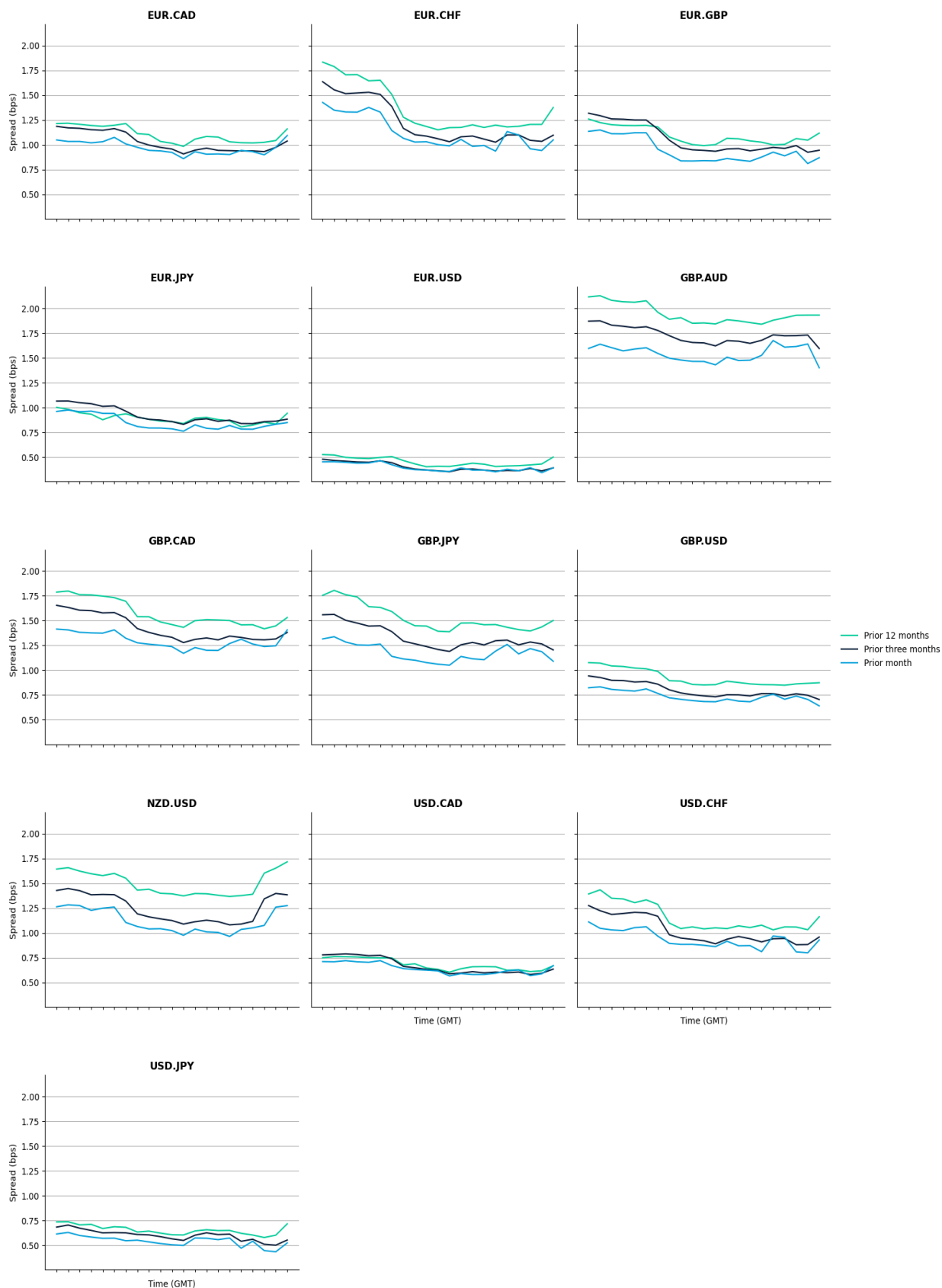
Comparison over the past month, three months and year



All chart sources: Virtu Financial, 2023. Spread and volatility calculations are derived from sources that Virtu believes to be reliable, but Virtu does not make any claims to its accuracy. USD.NOK, USD.SEK, EUR.NOK and EUR.SEK are shown in separate exhibits.

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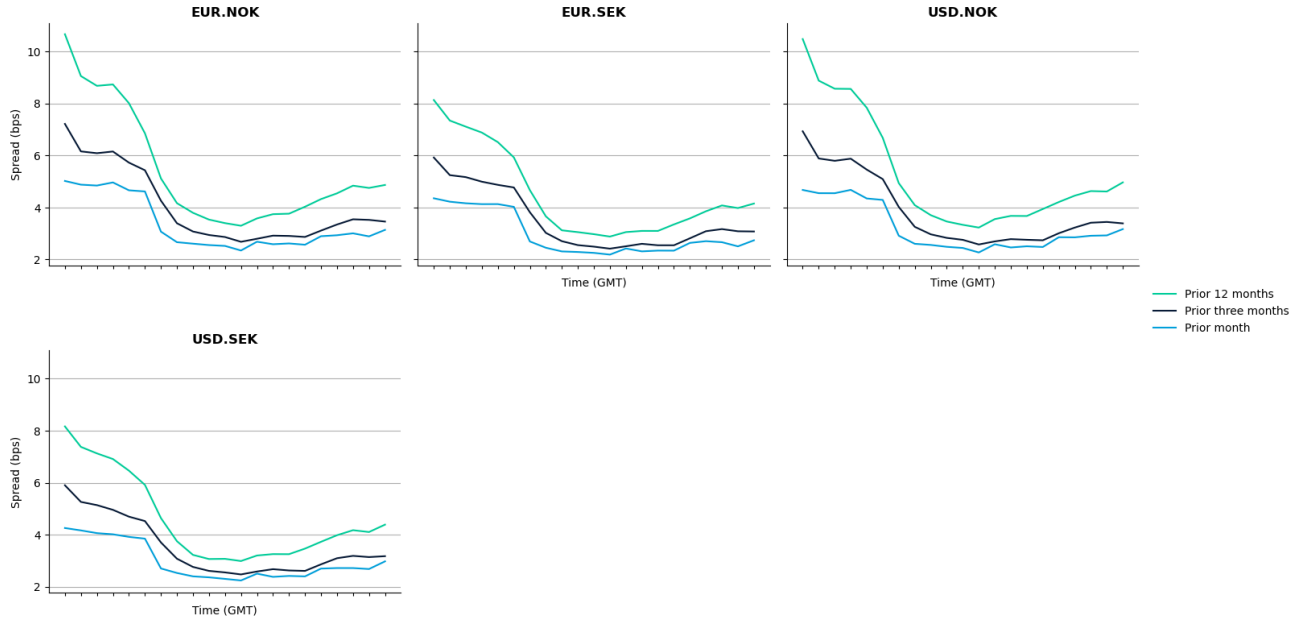
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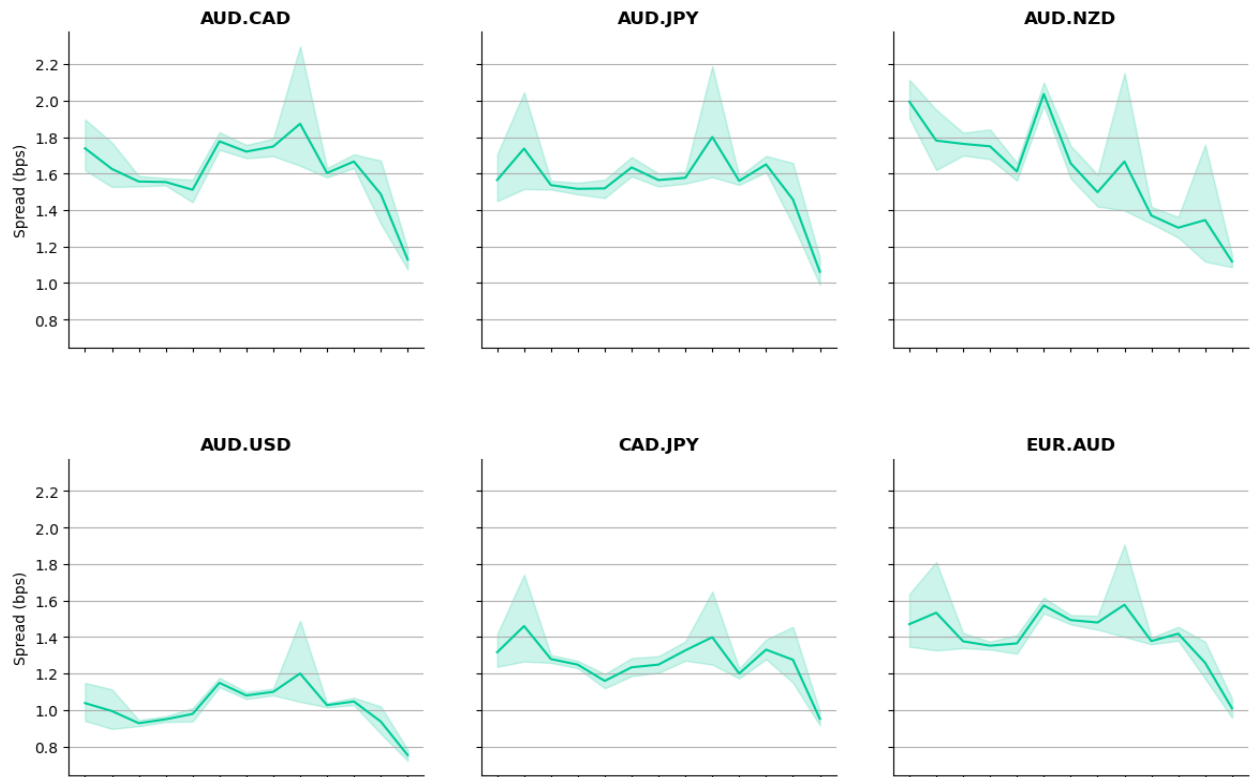
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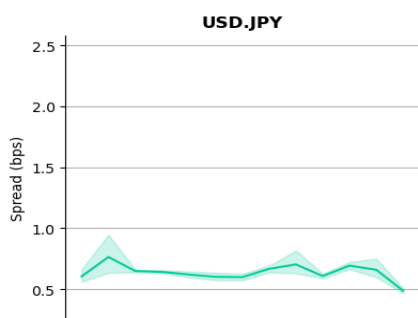
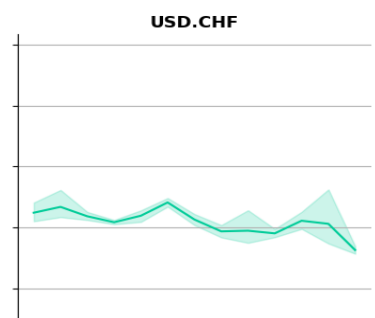
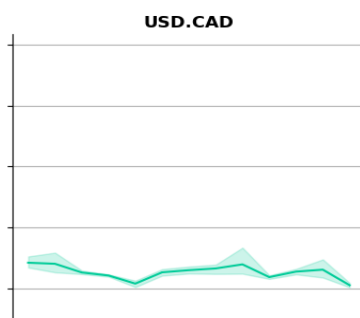
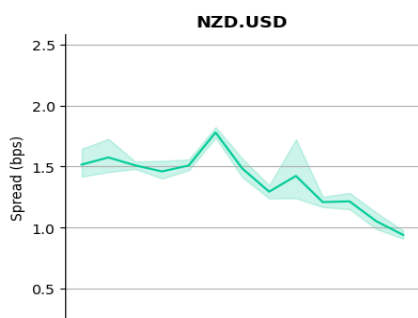
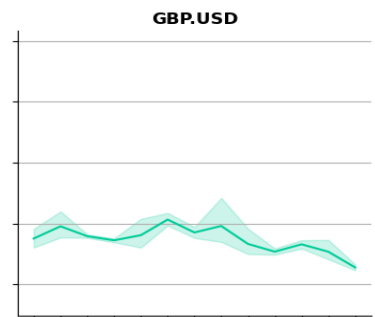
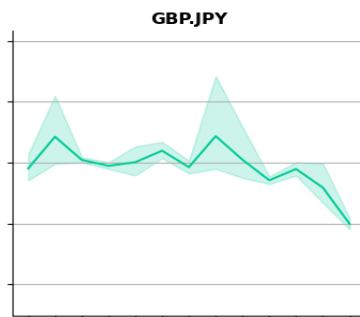
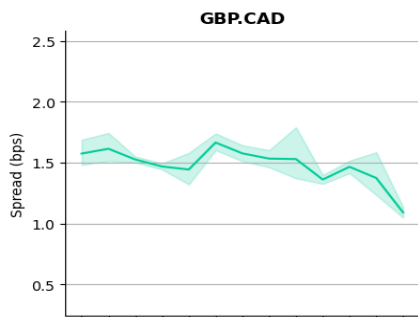
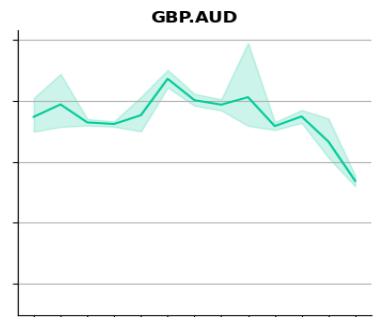
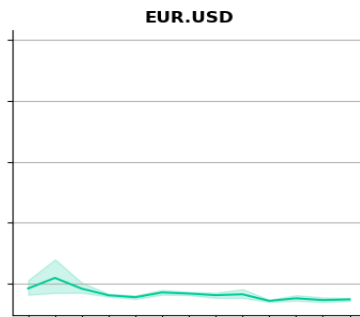
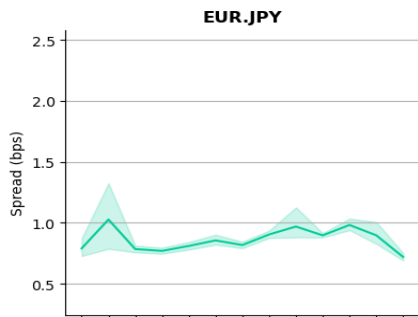
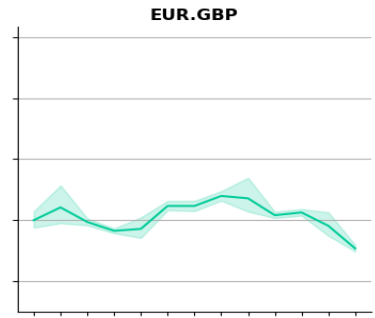
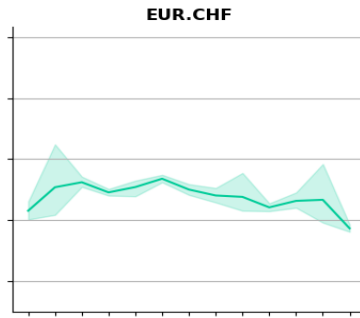
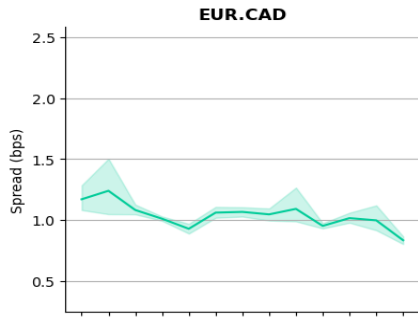
Scandinavian G-10 Currencies: Average Hourly Spread, 00:00-20:00 GMT Comparison over the past month, three months and year



G-10 Currencies: Average Daily Spread, 12:00-16:00 GMT May 2022-May 2023



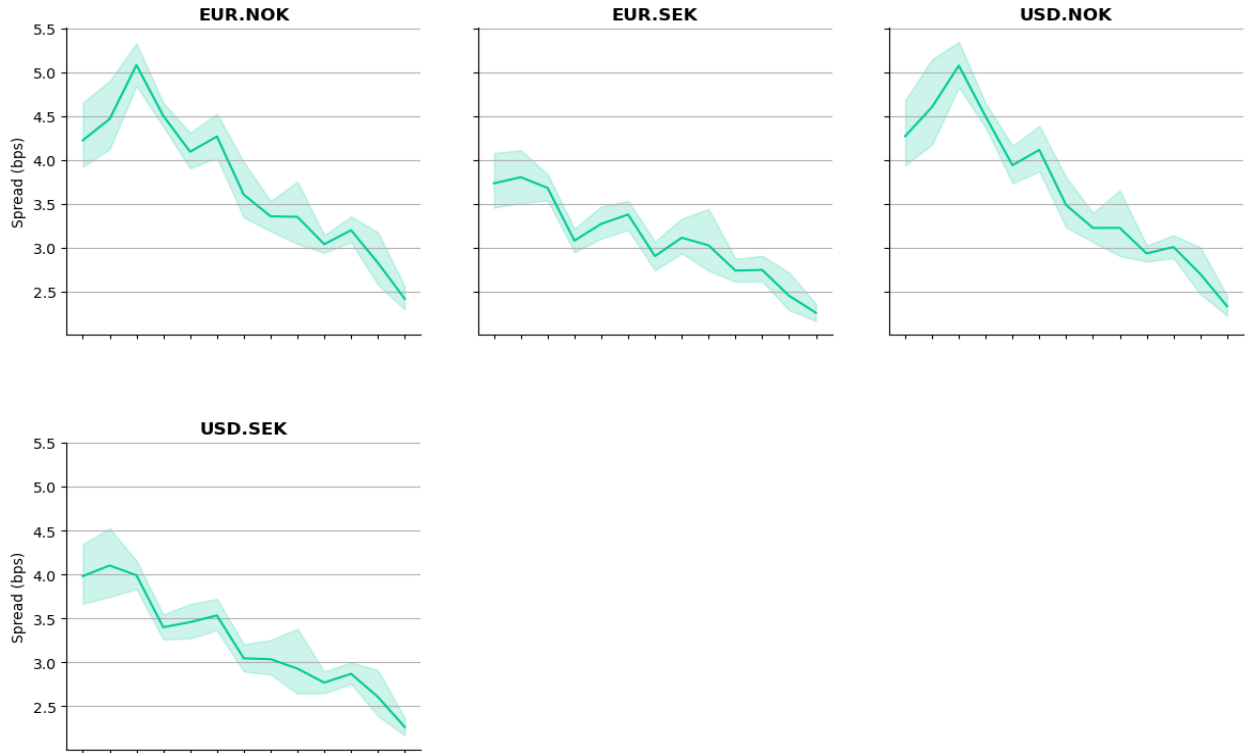
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Scandinavian G-10 Currencies: Average Daily Spread, 12:00-16:00 GMT May 2022-May 2023





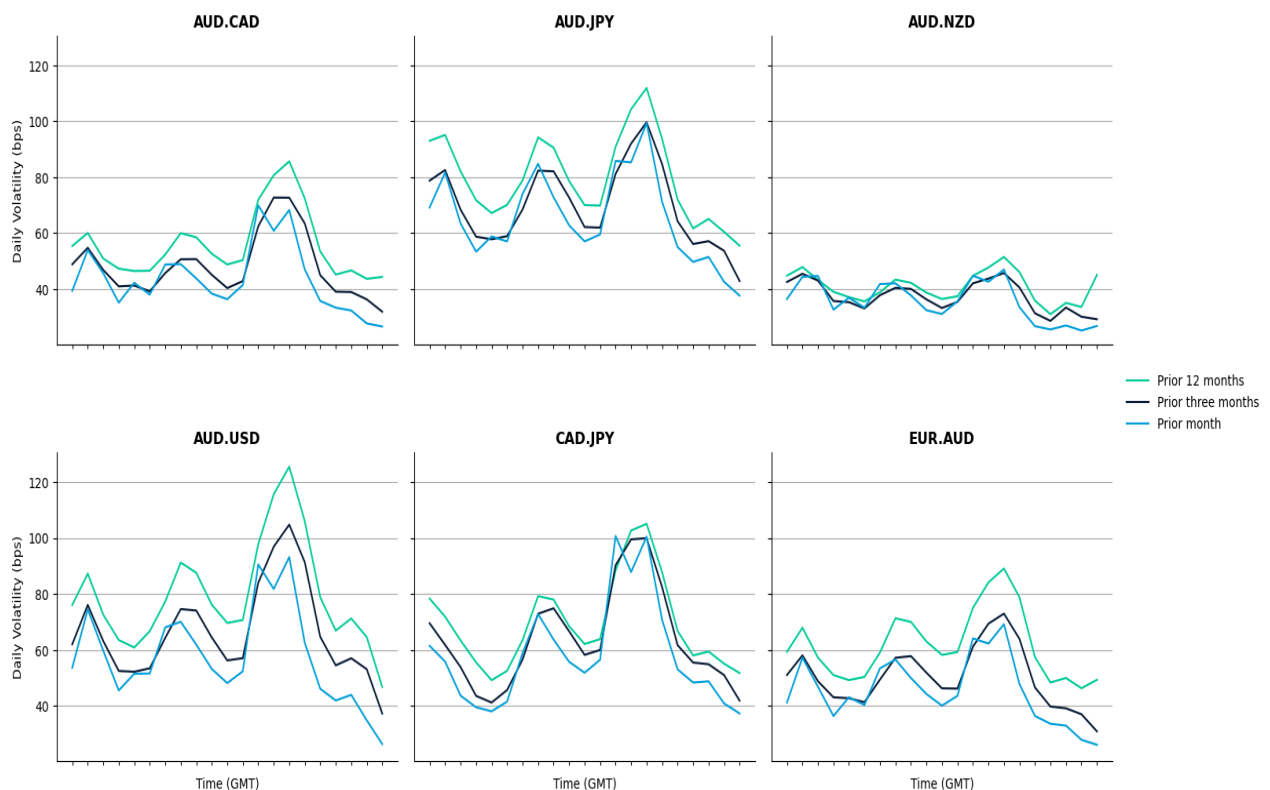
VOLATILITY

In May, FX spot volatility experienced a moderate decline, although not as steep as the drop observed in April. During the 12:00-16:00 GMT pre-WMR trading window, volatility increased for six currency pairs, compared to only two pairs in April. Notably, GBP/USD and USD/CAD, which had lower volatilities three months ago, recorded higher volatilities during this window. It's worth mentioning that pre-WMR volatility is lower for all pairs compared to the same period twelve months ago.

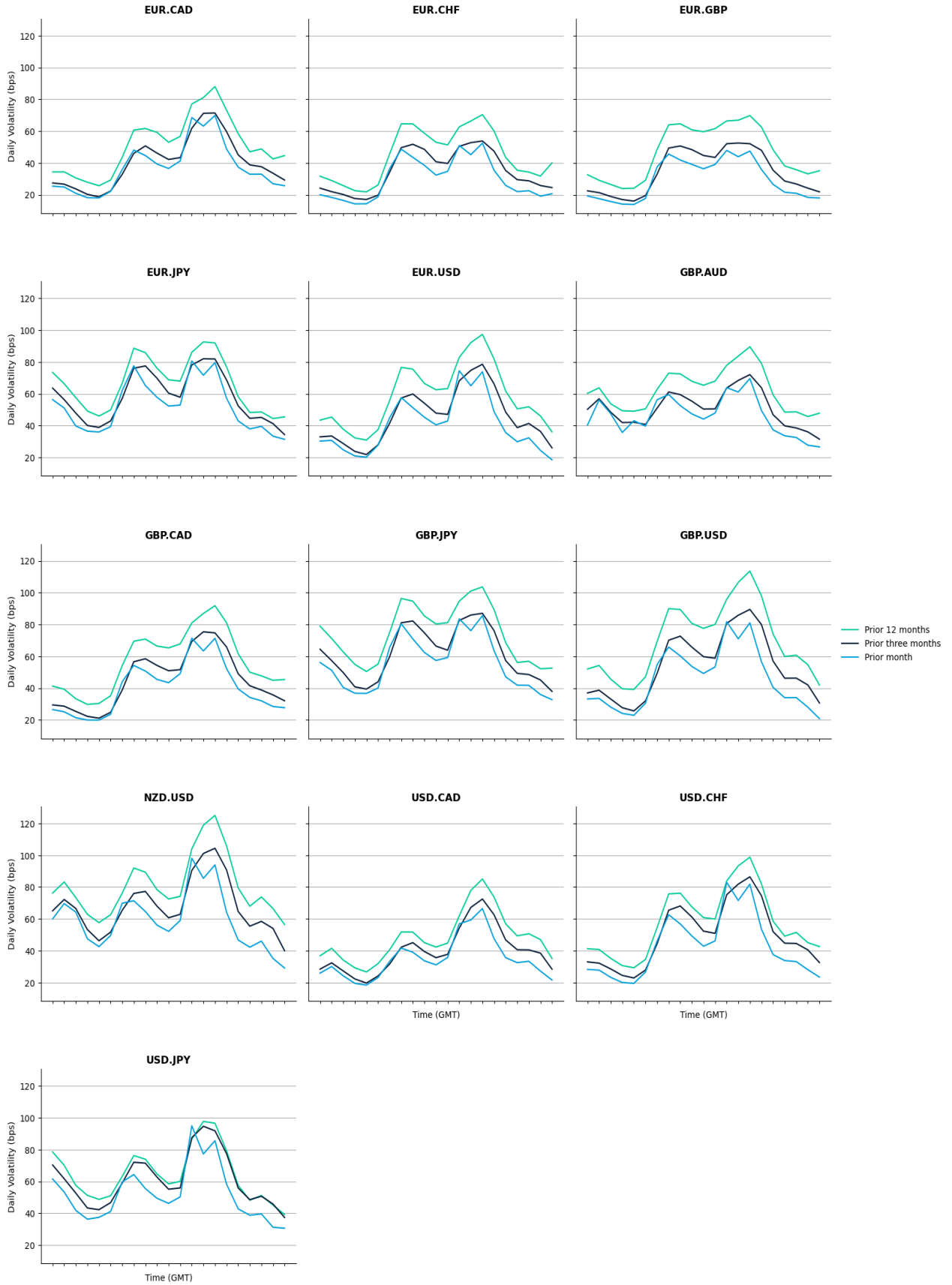
On an intraday basis, volatility was higher for 15 out of 23 pairs during the Tokyo market hours of 02:00-07:00 GMT. Subsequently, volatility picked up after the WMR fixing, from 16:00-18:00 GMT, for 16 pairs.

Earlier, we speculated that increasing central bank rates may lead to tighter spreads and lower volatility. While FX rates react to interest rate differentials, the impact on spreads is uncertain. Finance theory suggests that spreads and volatility should decline as risk declines. Does rising rates reduce risk? Perhaps not, but nearing the end of a rising cycle could reduce market risk. The central banks' rate increases were well-telegraphed in advance, but higher than expected inflation, along with geopolitical risks, introduced uncertainty about future rate courses. Approaching the end of a rate tightening cycle reduces the risk of further rate moves. The reduced chance of a surprise news from central banks we believe may be why spreads have narrowed substantially over the past two months.

G-10 Currencies: Average Hourly Volatility, 00:00-20:00 GMT Comparison over the past month, three months and year



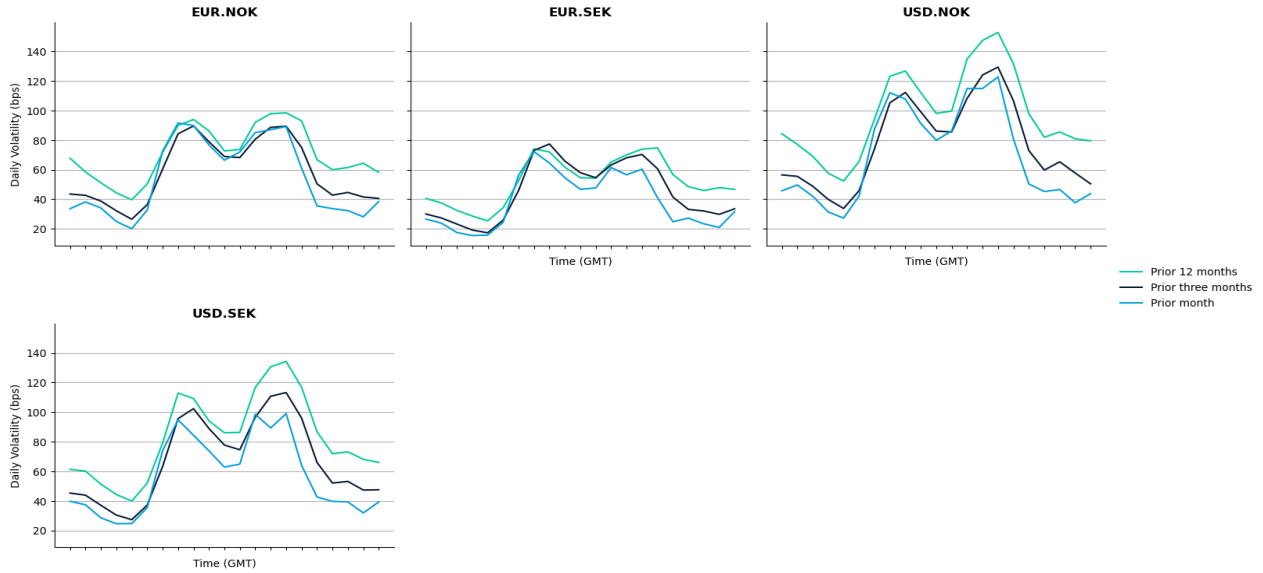
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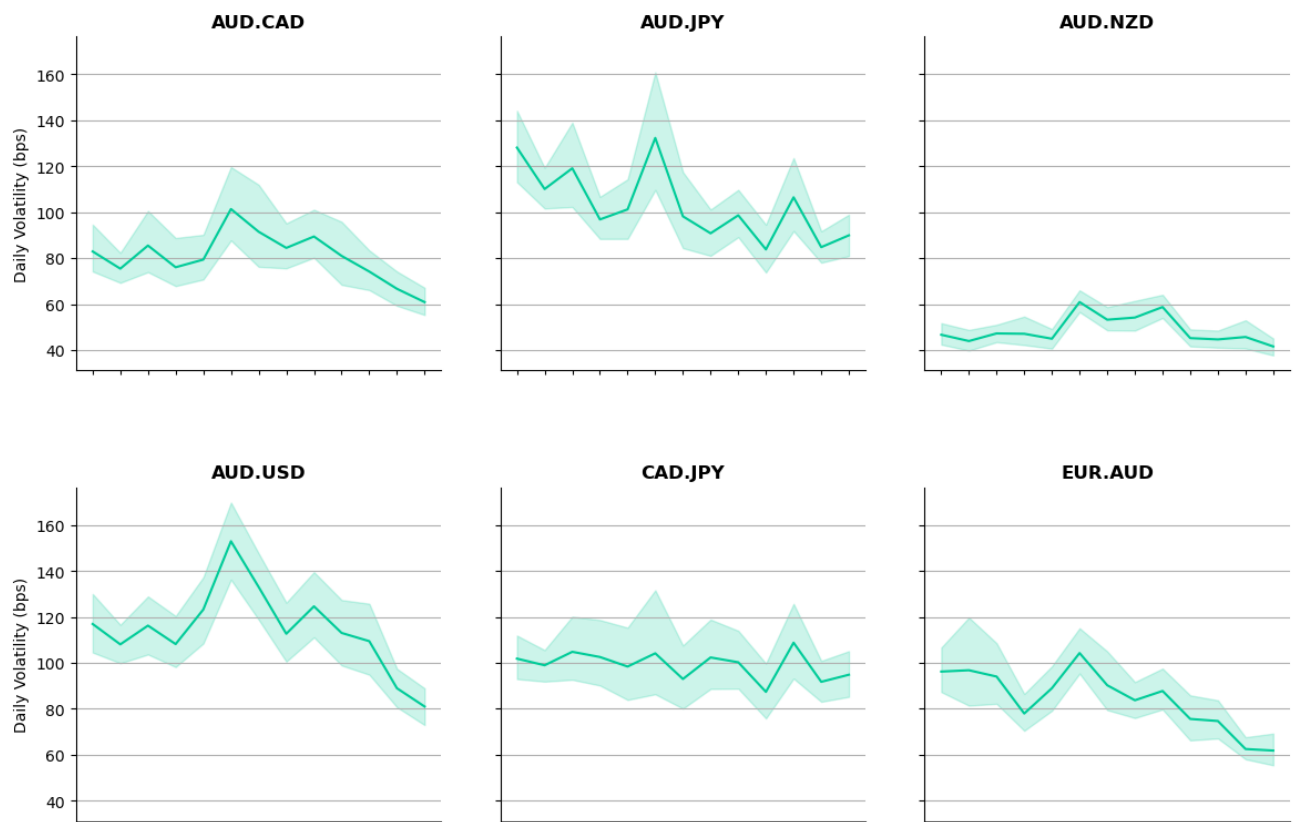
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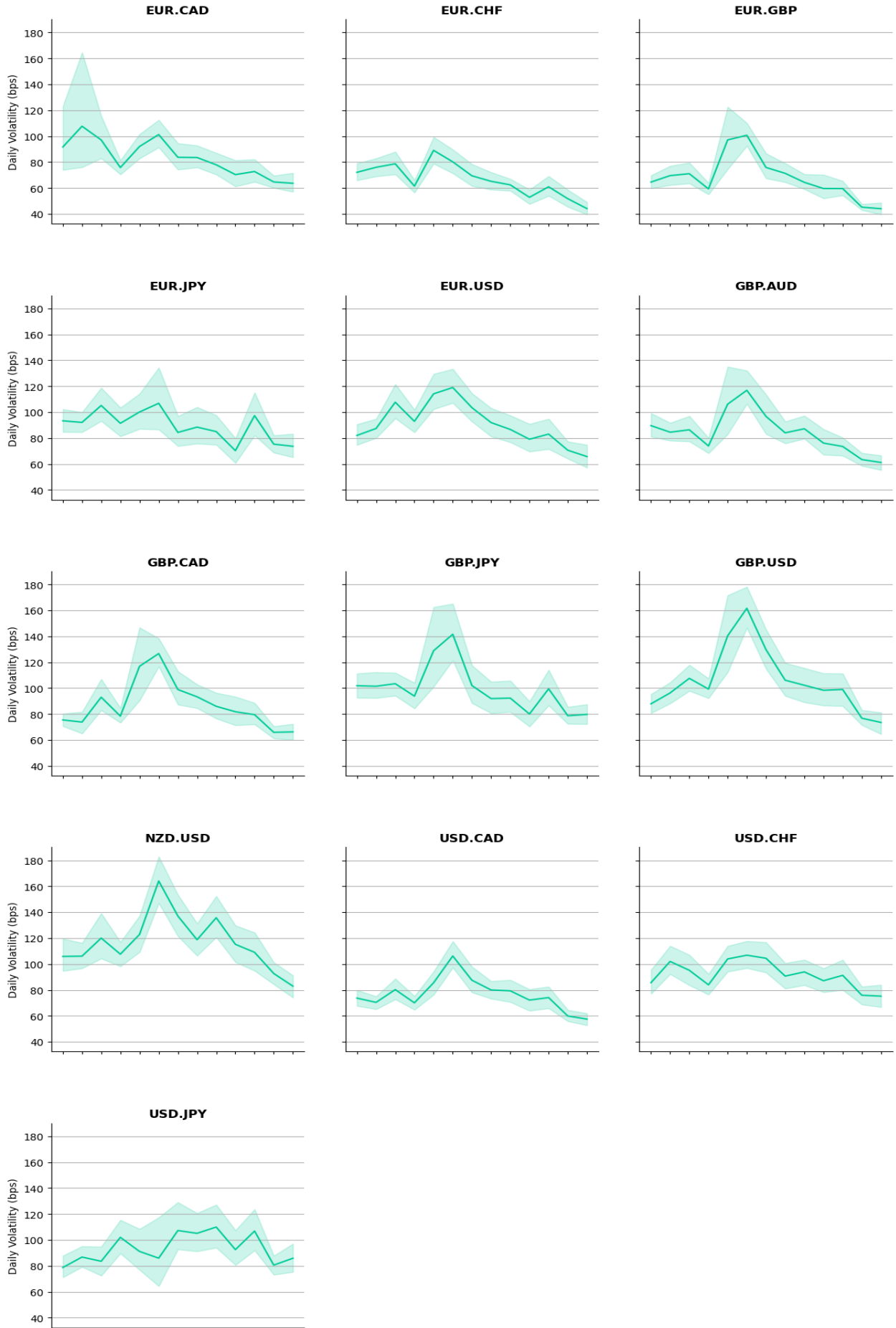
Scandinavian G-10 Currencies: Average Hourly Volatility, 00:00-20:00 GMT Past month, three months and year



G-10 Currencies: Average Daily Volatility, 12:00-16:00 GMT May 2022-May 2023



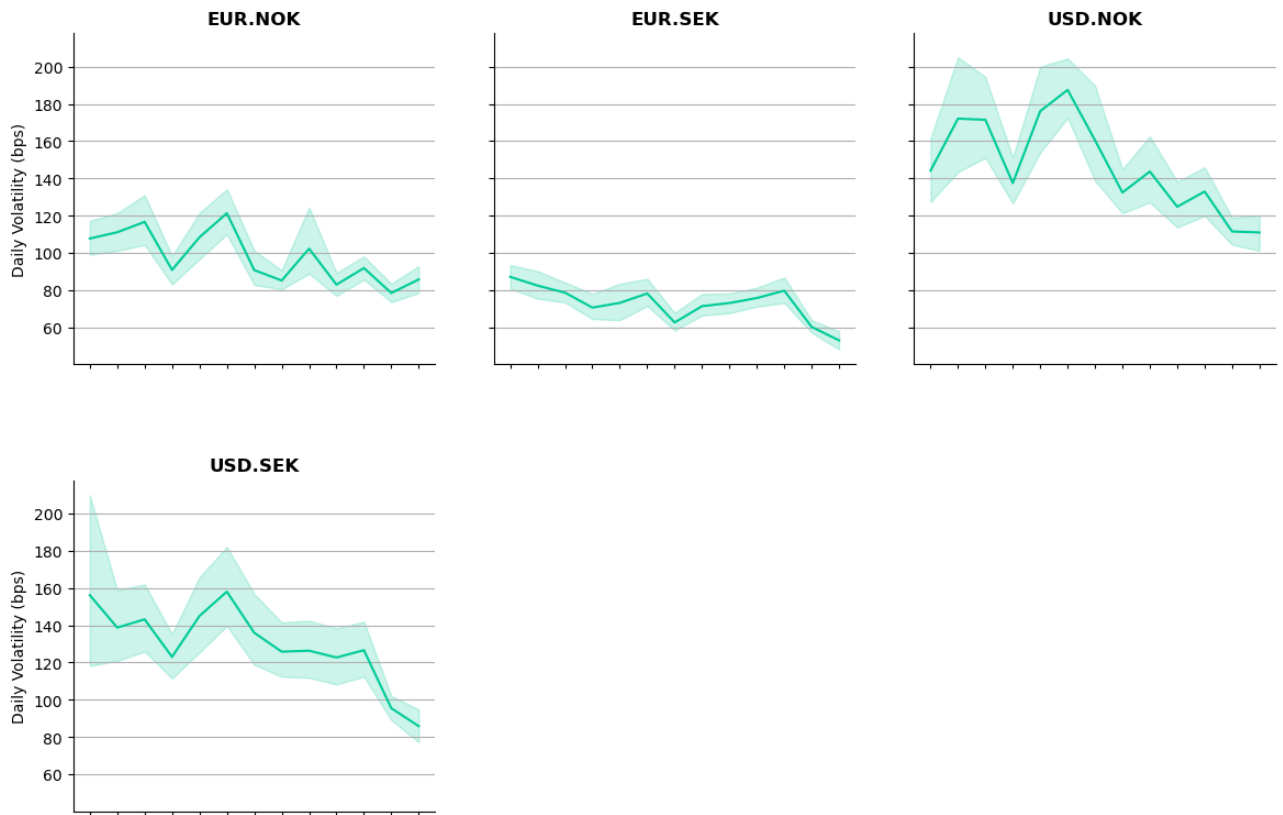
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Scandinavian G-10 Currencies: Average Daily Volatility, 12:00-16:00 GMT May 2022-May 2023



Have questions? To learn more, contact your regional Virtu Analytics representative.
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