



Theme #10: Turning Up the Volume

- Trading volumes, one of the better proxy indicators for realized volatility, have been grinding higher
- Increased monetary divergence and abundant global liquidity could see this trend continue further, we like long volatility option plays

Spot trading volumes picking up

Trading volumes and volatility tend to closely track each other and volumes are now on the march. Last month's average Daily Volume (ADV) traded on the EBS platform for spot transactions averaged \$128.3bn a day, or 7% higher than the previous month. Looking at the disaggregated YtD trends, it can be seen that trading activity has been somewhat suppressed in the euro by the Cypriot banking crisis and broader Euro zone growth uncertainty, though was held up by the yen reflation trade and commodity currencies in Q1 (charts 2-4, relative trading volumes for other currencies are available on request).

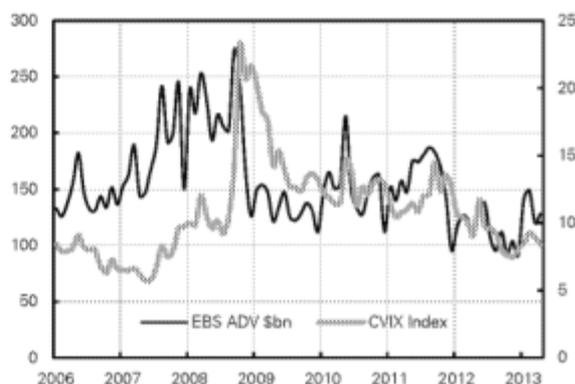
Options markets telling a similar story

The options market had signaled a similar pickup in 2013. ADVs for exchange traded options from the CME for April increased by 61% YoY. Excluding yen options, which accounted for two-third of the differences in contracts traded, the largest relative difference was in GBP, more than doubling (143% YoY) since last April despite the lowered spot transactions, followed by AUD (79% YoY) and CAD (16% YoY). Although these contracts represent a small sample of the derivatives market and are corporate biased, we find that these often correlate well to volatilities (chart 5). When taken together with spot data the broader picture emerges - higher overall volumes from the historical lows of 2012, followed by realized volatility.

Monetary divergence should help

In terms of whether the volume uptrend could be sustained in 2013, it appears that this trend is increasingly finding support from monetary divergence (one of the core drivers of FX volatility, in addition to volume) in an abundant global liquidity environment. A number of factors could contribute to this: Abenomics-related investor outflows from Japan have yet to materialize, although recent net outflows in Toshin investment is suggestive of the initial pickup. RBA's monetary stance remains closely tethered to global growth, while the rest of the dollar bloc and Scandinavia central bank policies are linked to domestic pressures. Elsewhere in the UK, stagflation remains a prominent issue, further, it is worth nothing that almost any policy response could conceivably push volumes higher given that GBP/USD spot volumes experienced one of the sharpest falls YtD within the

The bigger picture: Trading volumes and volatility



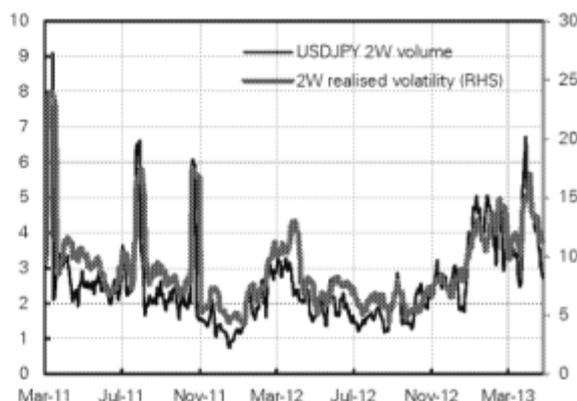
Source: EBS, Bloomberg Finance LP.

EUR/USD volumes down



Source: EBS, Bloomberg Finance LP.

But held up by yen



Source: EBS, Bloomberg Finance LP.