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## EURUSD – a roadmap

“European stocks’ outperformance has fundamental underpinnings” – Bloomberg.

“Goldman Sachs no longer expects recession in euro zone in 2023” – Reuters.

- And so it begins. Lower energy prices and China’s re-opening are two of the key factors cited in a host of articles suggesting the narrative around Europe is shifting. For many this leads to the conclusion that long EURUSD is the right call for early 2023.
- On Qi, the market has already run slightly ahead of fundamentals. EURUSD screens as 0.7 std dev (1.9%) rich to model. That is not a big Fair Value Gap by historical standards. But that begs the question where is level where the single currency’s rally starts to look overextended? The table below shows the results of back-testing various Qi FVGs as sell signals for EURUSD and the answer is clear – the sweet spot is when the cross gets one sigma rich to model.

|                       | +0.7 $\sigma$ | +1.0 $\sigma$ | +1.25 $\sigma$ | +1.5 $\sigma$ |
|-----------------------|---------------|---------------|----------------|---------------|
| <b>Hit Rate</b>       | 76.5%         | 84.2%         | 50.0%          | 66.7%         |
| <b>Avg Return</b>     | +0.8%         | +1.7%         | +1.1%          | +1.2%         |
| <b>Trade duration</b> | 15            | 13            | 13             | 13            |
| <b>No of trades</b>   | 34            | 19            | 8              | 3             |
| <b>Win/Loss</b>       | 0.9           | 1.3           | 3.4            | 2.1           |

- But remember FVG alone is not the only variable we consider when it comes to acting on a signal. What model value is doing is equally important. Currently it is trending higher; it has risen 3.3% over the last month - macro conditions are indeed supportive of Euro appreciation
- A rich FVG simply shows the market has moved quicker than macro fundamentals - some of the good news has already been priced in. It is only when model value has stopped rising / rolled over that a rich Fair Value Gap becomes an actionable signal.
- In effect, it's at that point we have a divergence pattern - the market is rich and macro conditions have stalled / started to deteriorate.

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