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Currency Correlation in Forex [Correlation Coefficient and Risk Management]

Categories: Forex Education Fundamental Analysis Education

Article Level: Intermediate



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Modified: Apr 27, 2025

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Some currencies have **positive** or **negative correlations** with other assets due to their **risk-on** or **risk-off nature**.



Understanding the correlation between forex currency pairs is crucial for risk control and avoiding excessive account exposure

Currency correlation and its underlying reasons are vital for **risk management, avoiding overexposure, swing trading,** and other strategies.

What Is Currency Correlation in Forex?



In the **Forex market**, currencies like **AUD** and **NZD** share similar characteristics and often move together. Thus, currency pairs may exhibit similar or opposite price movements. This synchronization or divergence is called **correlation**.

Example of Currency Correlation in Forex

For instance, when **AUD/USD** is bullish, **NZD/USD** is also likely to rise, as the drivers of **AUD** and **NZD** are highly similar.

Understanding Currency Nature to Grasp Pair Correlation

Currencies with **similar natures** tend to move alike, and trading them simultaneously in the same direction is **high-risk**. **ForexCurrency Characteristics:**

Risk-On Currencies	Risk-Off Currencies	Neutral Currencies
AUD	JPY	EUR
NZD	USD	GBP
CAD	CHF	–

From this table, during **risk-off** market conditions (strengthening of safe-haven currencies), the **CAD/CHF** pair may correct while **USD/CAD** trends upward.

These pairs often have a **negative correlation coefficient** and move **in opposite directions**.

Volatility in Correlated Currency Pairs

In the above example, if SNB turns **dovish Stance** while the Fed stays hawkish (assuming strong U.S. **GDP rate** growth), USD/CAD's rise could outweigh CAD/CHF's fall.

What Is the Correlation Coefficient?

The **correlation coefficient** between two assets ranges from **-1** to **+1**, indicating their relationship's **strength** and type (positive/negative). **Interpreting the Coefficient:**

- ⚡ **+1: Perfect positive correlation** — the assets move **identically**;
- ⚡ **0: No correlation** — the assets have **no linear relationship**;
- ⚡ **-1: Perfect negative correlation** — the assets move **inversely**.

For example, the correlation coefficient between **NZD/USD** and **AUD/USD** in February 2025 was **+0.94**, indicating a **strong positive correlation**.

To analyze forex pair correlations, use TradingFinder's **Forex Correlation Tool**.

The Role of Currency Correlation in Risk Management

Ignoring **currency nature** and **pair correlations** can lead to unintended **risk accumulation**.

Example of Unintended Risk Exposure

EUR/USD and **GBP/USD** are **highly positively correlated**. If a trader opens simultaneous sell positions on both, they face amplified risk because a **fundamental factor** (e.g., a strong U.S. economic report) could weaken both pairs.



High correlation in EUR and GBP; Source: TradingView

In essence, buying 1 lot of **EUR/USD** and 1 lot of **GBP/USD** is similar to buying **2 lots of EUR/USD**

Currency Correlation and Hedging

Traders can mitigate risk by leveraging **currency correlations** and **market sentiment**.

For example, during **geopolitical tension** (risk-off), a trader might long **gold** and **CHF** while opening a position in a **risk-on asset** to balance exposure.

Conclusion

Understanding **currency correlation** is key for **hedging**, **risk control**, and strategies like **swing trading**. Currency pairs with **positive correlations** tend to move in the same direction, so opening positions on both simultaneously increases risk exposure.

FAQs

What is forex currency pair correlation? ▼

Some pairs correlate due to shared base/quote currencies or economic ties, meaning their price movements align.

What is the correlation coefficient? ▼

The correlation coefficient shows how similar or opposite two items are in their movement:

If the correlation coefficient is 1, the two items move precisely alike;

If it's -1, it means the two items move in completely opposite directions;

If it's 0, it means there's no relationship between the movements of the two items.

The suitable trading pair is determined based on market sentiment and fundamental analysis of economic data. For example, if one currency has stronger economic growth than another, it may strengthen more significantly.



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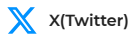


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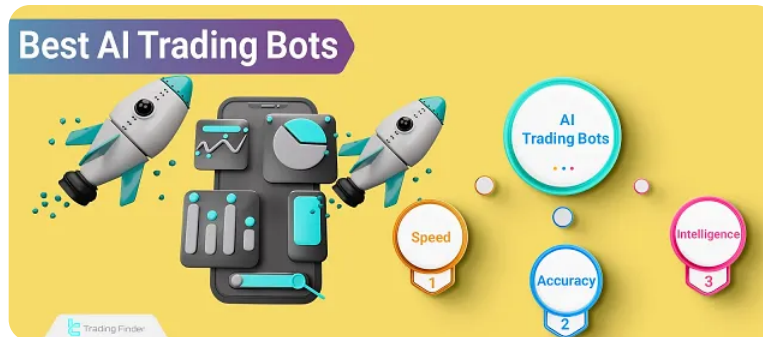
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