Currency Correlation in Forex [Correlation Coefficient and Risk Management]

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

LIVEWORKSHEETS

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**.

LIVEWORKSHEETS

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.

LIVEWORKSHEETS



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.

LIVEWORKSHEETS

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.

Sources:

1.our website link :
https://tradingfinder.com/education/forex/what-is-correlation-in-forex/

2.all Education :
https://tradingfinder.com/education/forex/

3.TradingFinder Support Team (Telgram):
https://t.me/TFLABS


TradingFinder


Educational link




TradingFinder


tradingfindercom

LIVEWORKSHEETS