Sucden Financial

Non-independent Research

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FX Options Weekly Report

Macro and Vol Commentary

The USD has weakened against a basket of currencies; the NZD is no exception. This week we look at the economic state of New Zealand and what are the looming risks the rally.

New Zealand Data

- Business PMI improved once again in June to 56.3, up from 39.8 the month before
  - New orders rebounded strongly to 58.6, with production and finished stocks also rising to 56.6 and 58.6 respectively
  - Employment was still contractionary in June at 48.5, up from 39.2
  - Unadjusted PMI was 54.9 in June; the production PMI was positive for the first time since February at 56.3
  - On a region by region basis, Canterbury rebounded the strongest to 61.6 in June whereas Otago, central and northern regions were less positive at 50.3, 50.1, and 54.9 respectively
  - The index outlines that the recovery is starting to take shape, however, employment is still on the back foot, and we need to see more from this sector
- Preliminary business confidence in July improved on a month on month basis to -29.8 from -34.4; the activity outlook improved on a month on month to -6.8 from -25.9 we expect this to improve further into August
- Monthly employment figures showed filled jobs up 1.8% y/y in June with the seasonally adjusted rise at 0.8% m/m to 2.20m. This is the second month of recovery after the decline in April
  - There has been an increase in jobseekers and CIRP number in the last month, approximately 65,000 more than in March according to the treasury
  - We expect the employment market to improve, however, due to the lack of tourism and reduced capacity as a result of COVID restrictions, gains will be less pronounced
- Credit card spending growth has slowed, up 14% m/m in June, down from 54.3% m/m. Year on Year credit card spending is down on -9.2%, an improvement on the May -20.6%
- The trading balance 12 month YTD for New Zealand improved in June to NZD- 1,196m, up from NZD -

1,327m tonnes.

- The balance for June was 416m NZD, as exports slipped slightly to 5.07bn from 5.39bn, as imports increased to 4.64bn NZD
    - _ The weaker exports suggest New Zealand's trading partners are still suffering from COVID and this may be exemplified by their close ties with Australia
- New Zealand has suspended the extradition agreement with Hong Kong, and this follows similar actions from western economies
- While there is a risk to Australia's economy with Chinese trade tensions due to exports of grains and iron ore and coal to China, this could cause some flows out of AUDUSD into New Zealand
- However, China is New Zealand's largest trade partner with the annual amount exceeding $21bn, and the escalation of trade tensions may result in some headwinds to NZDUSD
- The government has committed $62.1bn of fiscal support, supporting workers and businesses. Approximately $12.9bn has been paid out in Wage Subsidy Extension, this is in addition to the Small Business Cashflow Scheme which has paid out $1.47bn to nearly 90,000 applicants.
- This will aid the stimulus provided by the central bank, who reduced their OCR to 0.25%, this rate is expected to remain low for 0.25% for some time
- The reserve bank has committed to purchasing $60bn of government debt in the next year

The economy is showing signs of recovery, but the recent tensions with China could provide headwinds to the currency if things escalate further. The export market ex-china is still weak, and although we have seen commodity prices start to increase of the lows, the NZ commodity export index remains below January levels except for fruit. The government stimulus is finding its way into the economy, and wage subsidies should help support consumer spending, however, the savings ratio will be a headwind. With tourist revenue down, this will leave a hole in the government's books, but bond yields are positive compared to negative rates in other economies. In the near term, we anticipate further support for NZD over USD, especially if the Australia and Chinese tensions continue to escalate.

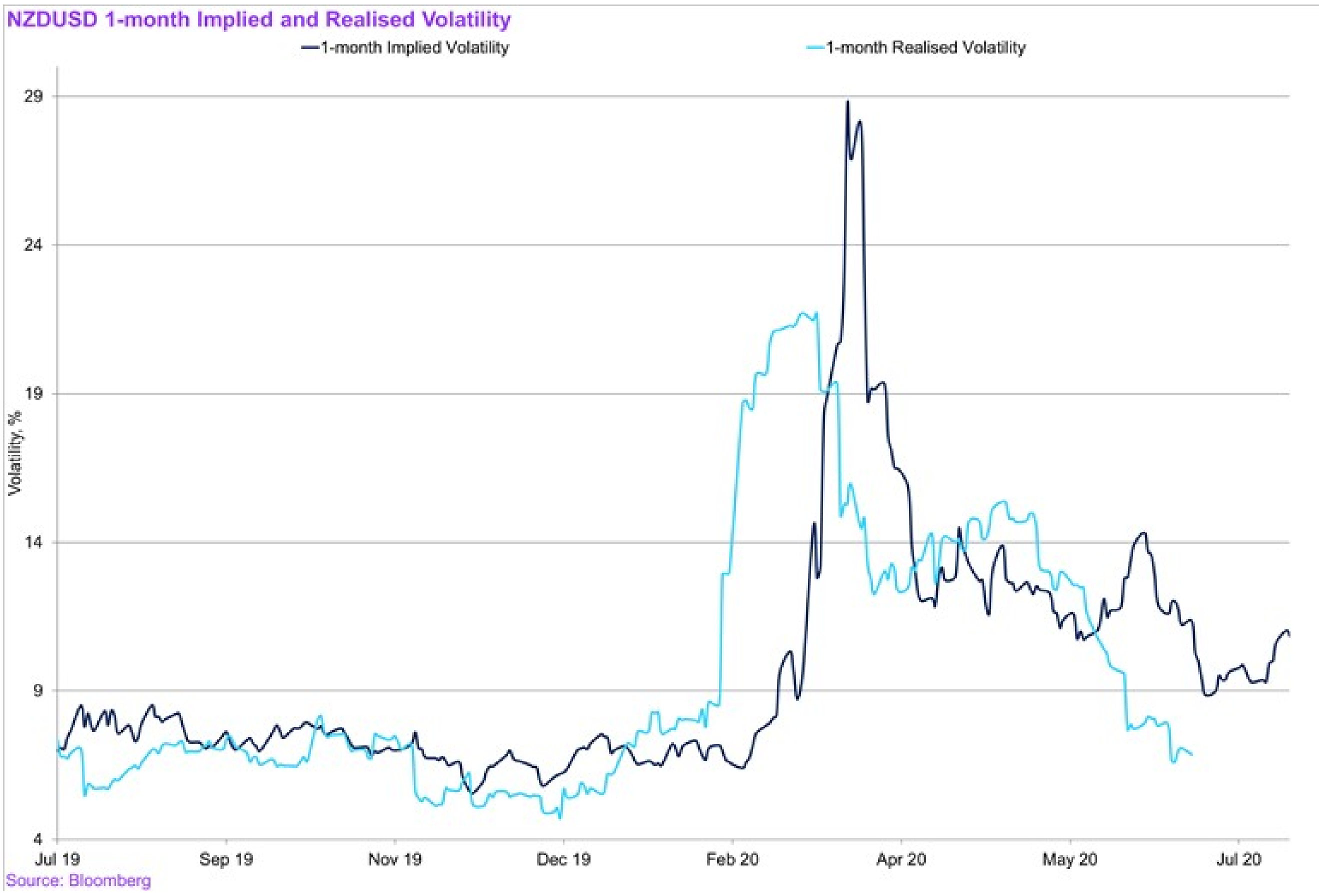
Volatility Commentary

General Vol

Recently macro news has been mixed. We have seen risk-on sentiment news, such as EU leaders agreeing to a stimulus package to help bolster EU economic recoveries, but on the other side, we have seen a further worsening of the East-West relations with the US Govt. Now, the UK Govt increasingly hardening their stance on China over a variety of issues. With this, we have seen Macro FX vols generally creeping up and a weakening dollar amidst the US CV19 second wave.

NZDUSD Vol

In the last few months, New Zealand has managed to keep its Coronavirus countdown to the point of it being functionally eradicated in the country. With that, NZDUSD spot has benefited strongly from the domestic economy having fully opened up and a weak dollar with vol realising at pre-CV19 levels (though implied vol is still a little higher than pre-CV19 levels and seen a small pick up recently). We're favouring short NZDUSD vol/gamma for shorter date expiries at these levels.



NZDUSD Trade Idea

- Priced in 10m a leg
- Short NZDUSD straddle with 1month expiry and delta hedge short gamma position
- Sell for circa 10.00 vols, trade gives short vega of approx 22.5k NZD Vega (about 15k USD equivalent)
- Note this strategy is only suitable for investors who are set up and capable to dynamically delta hedge short vega/gamma positions

Charts and Tables

FX Expiries

Currency Pair	Wednesday 29th	Thursday 30th	Friday 31st	Monday 3rd	Tuesday 4th
GBP/USD		740m @ 103.75 950m @ 106			
USD/JPY		878.27mn @ 1.15	1.32bn @ 1.155		1.16bn @ 1.165
EUR/USD					
EUR/GBP					
USD/BRL		340mn @ 5.1915	230mn @ 5.075 380mn @ 5.1 550mn @ 5.15 150mn @ 5.175 570mn @ 5.2 330mn @ 5.25	100mn @ 5.15	
AUD/USD		201.42mn @ 0.705	122bn @ 0.705		
USD/ZAR					140mn @ 16.55 120mn @ 16.81
USD/INR					500mn @ 75.04

Source: Bloomberg DTCC Data 2% from spot levels as of 28/07/2020

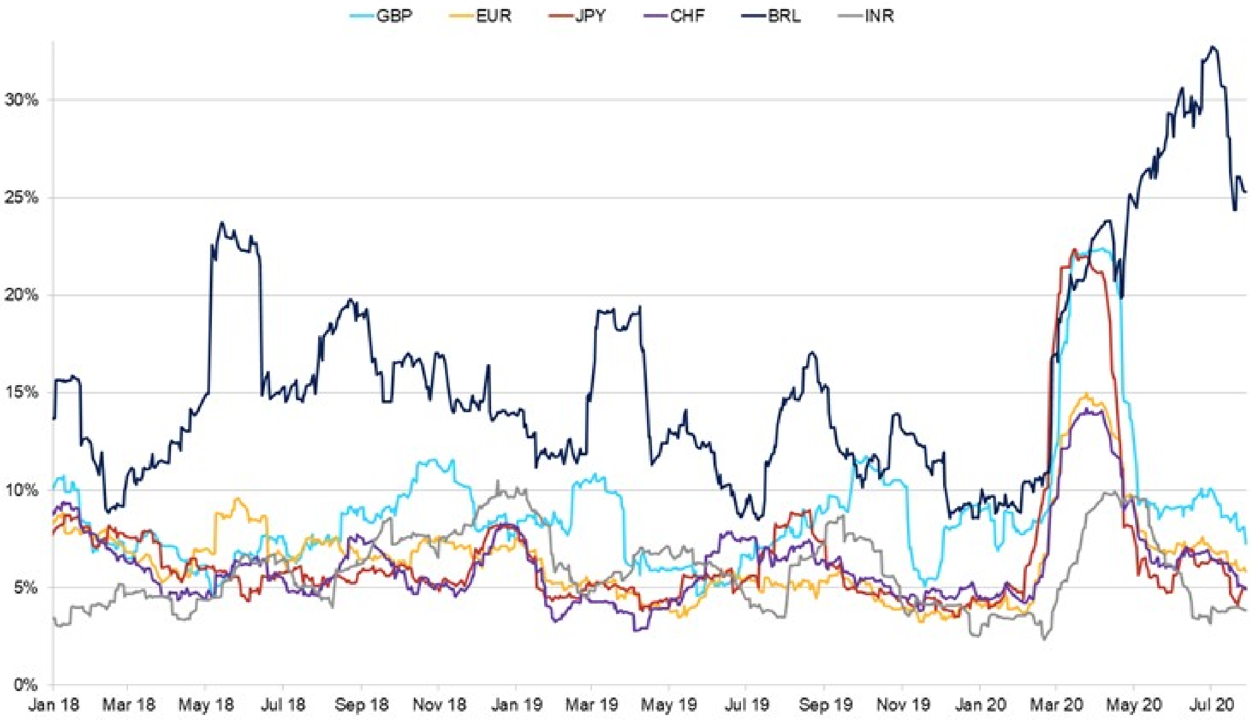
FX Volatility Grid

Time	EURUSD			GBPUSD			USDJPY			EURGBP		
Period	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM
1W	0.62	0.13	8.11	0.12	0.13	8.36	-0.98	0.15	7.16	0.36	0.12	7.46
1M	0.54	0.18	7.40	-0.21	0.15	7.86	-1.29	0.17	6.93	0.63	0.13	6.88
2M	0.48	0.20	7.41	-0.58	0.18	8.22	-1.53	0.20	7.17	0.82	0.16	7.08
3M	0.39	0.23	7.38	-0.86	0.22	8.47	-1.71	0.22	7.30	0.97	0.18	7.25
6M	0.23	0.29	7.37	-1.41	0.29	9.00	-2.25	0.26	7.92	1.30	0.24	7.49
1Y	0.07	0.32	7.17	-1.81	0.34	9.25	-2.46	0.29	7.78	1.60	0.28	7.67

Time	USDINR			USDTRY			USDJPY			AUDUSD		
Period	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM
1W	0.45	0.17	5.67	6.50	0.60	15.20	1.28	0.49	23.08	-0.70	0.18	10.56
1M	0.62	0.18	5.75	6.93	0.71	15.71	2.51	0.54	20.62	-1.01	0.23	9.96
2M	0.74	0.18	5.89	7.22	0.75	16.53	2.92	0.60	19.59	-1.23	0.25	9.93
3M	0.84	0.21	6.02	7.64	0.89	17.23	3.20	0.65	18.99	-1.42	0.26	9.95
6M	1.05	0.27	6.49	8.43	1.00	18.84	3.92	0.72	17.95	-1.74	0.29	10.19
1Y	1.19	0.30	6.55	9.13	1.13	20.84	4.61	0.82	16.91	-1.96	0.32	10.02

Source: Sucden Financial

Historical Spot FX Volatility (30D Rolling)



Source: Sucden Financial, Bloomberg

FX Matrix (today)

	USD	GBP	EUR	JPY	CHF	CAD	AUD	NZD
USD	-	**1.2994**	**1.1744**	**0.0095**	**1.0936**	**0.7453**	**0.7143**	**0.6625**
GBP	0.7695	-	0.9038	0.7323	0.8416	0.5736	0.5497	0.5099
EUR	**0.8515**	**1.1065**	-	**0.8104**	**0.9313**	**0.6347**	**0.6082**	**0.5642**
JPY	105.0800	136.5400	123.4000	-	114.9210	78.3220	75.0550	69.6170
CHF	**0.9144**	**1.1881**	**1.0738**	**0.8702**	-	**0.6815**	**0.6531**	**0.6058**
CAD	1.3416	1.7433	1.5756	0.0128	1.4673	-	0.9583	0.8888
AUD	**1.4000**	**1.8192**	**1.6442**	**1.3324**	**1.5312**	**1.0435**	-	**0.9275**
NZD	1.5094	1.9613	1.7726	0.0144	1.6508	1.1250	1.0781	-

Source: Bloomberg

Weekly Change

	USD	GBP	EUR	JPY	CHF	CAD	AUD	NZD
USD	-	1.99	1.28	1.70	1.21	-0.05	0.63	-0.15
GBP	-1.95	-	-0.70	-0.29	-0.75	-2.02	-1.33	-2.07
EUR	-1.25	0.71	-	0.43	-0.05	-1.31	-0.64	-1.38
JPY	-1.67	0.29	-0.42	-	-0.48	-1.72	-1.05	-1.81
CHF	-1.20	0.76	0.06	0.48	-	-1.26	-0.58	-1.34
CAD	0.04	2.04	1.33	1.76	1.28	-	0.68	-0.09
AUD	-0.62	1.35	0.65	1.07	0.58	-0.69	-	-0.76
NZD	0.15	2.14	1.42	1.84	1.36	0.10	0.78	-

Source: Bloomberg

Key Events & Releases

Region	Date	Time	Indicator	Period	Survey	Prior
NZD	29/7	23:45	Building Permits MoM	Jun	0.0%	35.6%
JP	30/7	00:50	Retail Trade MoM	Jun	7.1%	2.1%
EU	30/7	10:00	Consumer Confidence	Jul	-15.0	-15.0
EU	30/7	10:00	Unemployment Rate	Jun	7.7%	7.4%
US	30/7	13:30	Core PCE QoQ	Q2	1.0%	1.7%
US	30/7	13:30	GDP Annualised	Q2	-34.1%	-5.0%
US	30/7	13:30	Continuing Jobless Claims	Jul 17	16.2m	16.197m
JP	31/7	00:50	Industrial Production YoY	Jun	-21.0%	-26.3%
CN	31/7	02:00	NBS Mfg PMI	Jul	50.7	50.9
EU	31/7	10:00	Core CPI YoY	Jul	0.7%	0.8%
EU	31/7	10:00	GDP YoY	Q2	-14.5%	-3.1%
US	31/7	15:00	Mchg Consumer Sentiment	Jul	73.0	73.2
US	03/8	15:00	ISM Mfg PMI	Jul	48.4	52.6
NZD	04/8	23:45	Unemployment Rate	Q2	3.8%	4.2%
CN	06/8	02:45	Caixin Services PMI	Jul	56.8	58.4
EU	05/8	10:00	Retail Sales YoY	Jun	-6.6%	-5.1%
US	05/8	12:00	MBA Mortgage Applications	Jul 31		-0.8%
US	05/8	14:45	Markit Services PMI	Jul	49.6	49.6

Source: FX Street

Technical Charts

JP Morgan Global FX Volatility Index

The index was bid below previous support at 7.63 last week which has prompted a break of the resistive moving averages. The index is now holding above 8.20 but remains below key resistance at 8.69. The stochastics are starting to fall, and the MACD diff is converging in positive territory suggesting that buying pressure is waning and we could see a correction to the downside in the near term. If support at the 200 DMA holds firm, this could strengthen the outlook in the long run through 8.69. A subsequent breach of the 200 DMA at 8.04 would set the scene for lower a move back towards the recent low, in order to confirm the trend on the downside, the index needs to take out the low. On the upside, we need to see the index break above 8.69 and then target 9.30 in order to suggest a change in trend.

Dollar Index

The index has continued to weaken, as selling pressure dominates the market. The index has been supported at 150% fib level, in order to confirm the inverted hammer the index needs to takeout resistance at 93.844. The MACD diff is positive and diverges on the upside suggesting higher prices. The stochastics are rising towards neutral territory, we could see a correction on the upside towards the 50 DMA at 94.507. We expect rallies to be sold and the trend to remain intact. On the downside, a rejection of prices at 94 would pave the way for a breach of support at the 150% fib level towards 92.

NZDUSD

The trend has been strong in favour of NZD in recent months, resistance has been taken out repeatedly. The indicators have started to weaken as the stochastics fall towards oversold and the MACD diff is negative and diverging suggesting lower prices. The rejection of 0.6700 and the weakening indicators suggest we could see lower prices in the near through support at 0.6612. Secondary support stands at 0.6580, before 150% fib level at 0.6529 a breach of this level would help confirm the double top and bearish engulfing candle. Conversely, if futures are supported at 0.6612 this could set the scene for a rested of 0.6715 A break of this level would confirm the trend on the upside.