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FX Options Weekly Report

Macro and Vol Commentary

The impact of coronavirus has been felt across the world. Now, governments worldwide are looking to inject major stimulus measures into suffering economies, with the Fed already paving the way. This week, we are taking a look at a USDCNH pair, and what direction it can go from here.

China and Impacts of the Virus

- As of March 5th, more than 95,000 cases have been registered across the world, with 80,000 of those cases remaining in mainland China.
- Risk assets sold off originally, with the Shanghai Composite Index losing 11.80% at the beginning of February.
- More recent rises are attributed to the optimism of stimulus injection by global central banks
- According to Nomura Holdings, China's GDP growth rate is forecast to contract by 2.5% q/ in Q1 2020
- G7 chiefs reaffirmed their commitment to act against the impacts of coronavirus, however, no specific measures have been listed
- Global supply chains suffered a massive blow due to the impacts of the virus
 - _ The manufacturing PMI plunged from 50 in January to 35.7 in February, the lowest level on record
 - _ According to Bloomberg, Chinese factories were operating at 60-70% of capacity in the last week of February
 - _ About 91% of factories claim to restart operations by the end of March
- The major manufacturing and services indexes are seen to recover after Q1 2020; however, support from the government will strengthen
 - _ PBOC strengthened daily reference rate by -0.36%, the most since January 14th to 6.9811
 - _ Increasing levels of fiscal support
 - _ Cuts to reserve requirement ratios for banks and lower borrowing costs
 - _ Reduction of corporate taxes and cutting government expenses
- If the outbreaks in the rest of the world lead to substantial shutdowns, then we might expect more of a

U-shaped reversal than V

US Data

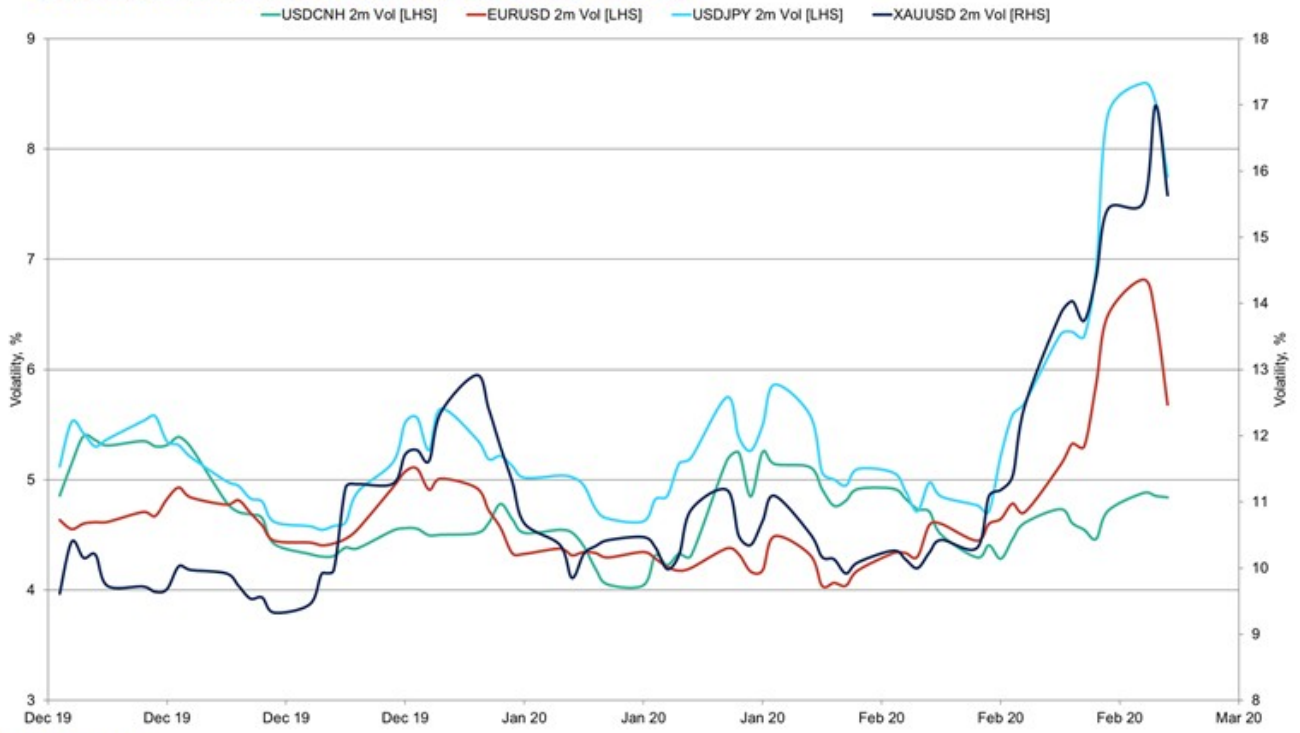
- US stock markets marked significant losses in the last week of February, losing 11%, before finding support on the back of the Fed cut
- US February ISM Factory Index fell to 50.1 from 50.9 in January, below estimations.
- For 2020, OECD has cut US growth forecast to 1.9% from 2.3%
- Super Tuesday results show better-than-expected performance from Biden, urging stocks and dollar rally
- The downside risks prevail as we await the corporate earnings release that would highlight the real economic impact of the virus

The Fed Rate Cut

- After cutting rates three times in 2019, the Fed has conducted an emergency rate cut of 50bps as a response to increased risks of coronavirus
- 10- and 30-year US bond yields dropped to record lows of 0.9440 and 1.5770 respectively
- We estimate that the cut alone will not be a cure-all for economic pain, given the expansion of the virus in the US, as both supply and demand could remain subdued
- More importantly, constant liquidity to small and medium-sized companies could alleviate those pressures off supply chains

The Covid-19 along with the impacts of the Fed cut could continue to add pressures on USD, that has already adjusted to looser monetary policy stance after Jerome Powell's announcement to "act as appropriate to support the economy". Stimulus injection in China should offset the impacts of disappointing manufacturing and service data, alleviating possible pressures of the USDCNH pair. We believe that the Fed cut will provide support to the yuan in the short-term. However, the contamination of the virus in China should provide tailwinds to the rally.

USDCNH, EURUSD, USDJPY, XAUUSD 2-month Volatility



Source: Bloomberg

USDCNH Vol comment

Following last week's Coronavirus fear-fuelled stock sell-off, we've seen a surprise from the Fed with a 50bps cut having been announced. Alongside this, we've seen many short-mid date FX Vols spike off this, from Feb's low spiking on Monday with 2m expiries EURUSD vol rise from at 6.5 vols, USDJPY at circa 8.5 vols and XAUUSD at circa 16.5 vols (these have come off slightly, at time of writing).

Despite this Coronavirus news (and China being the centre), USDCNH vols have stayed comparatively steady over this period in comparison with the pairs mentioned above, with 2m vol generally staying between 4.0 and 5.5 vols since the start of the year (currently circa 4.835). With implied vols in USDCNH being comparatively low compared to other pairs and with the Fed having cut and showing a willingness to ease further (with 100-125 bps of rate cut room), we favour being long USDCNH vol at these levels with positions benefiting from USDCNH weakening.

Trade Idea

- Buy USDCNH EKI Put option in 05/05/2020 expiry (just over 2m to capture Mar & Apr Fed meeting) priced in 10m USD Notional
- With strikes of 6.9000 and barrier 6.8000
- Doing so results in premium cost of circa 38k USD (note vanilla equivalent is circa 56k, barrier providing approx. 18k reduction)

Charts and Tables

FX Expiries

Currency Pair	Thursday 5 th	Friday 6 th	Monday 9 th	Tuesday 10 th	Wednesday 11 th
GBP/USD					
USD/JPY	860mio @ 107.9	700mio @ 109.65		500mio @ 105 1.18bio @ 109.05	
EUR/USD	655.72mio @ 1.098 527.97mio @ 1.1175 525.62mio @ 1.1225		914.92mio @ 1.093		
EUR/GBP	570mio @ 0.86				
USD/BRL	110mio @ 4.4915 100mio @ 4.52 406.1mio @ 0.655	110mio @ 4.49 100mio @ 4.55	100mio @ 4.4436 100mio @ 4.447		
AUD/USD	100.61mio @ 0.656 149.81mio @ 0.6675 112.93mio @ 0.673	201.52mio @ 0.655	396.97mio @ 0.66 100.53 @ 0.6665	100.23mio @ 0.6585	
USD/ZAR	300mio @ 15.25				
USD/INR	100mio @ 72.5				

Source: Bloomberg DTCC Data 2% from spot levels as of 04/03/2020 close

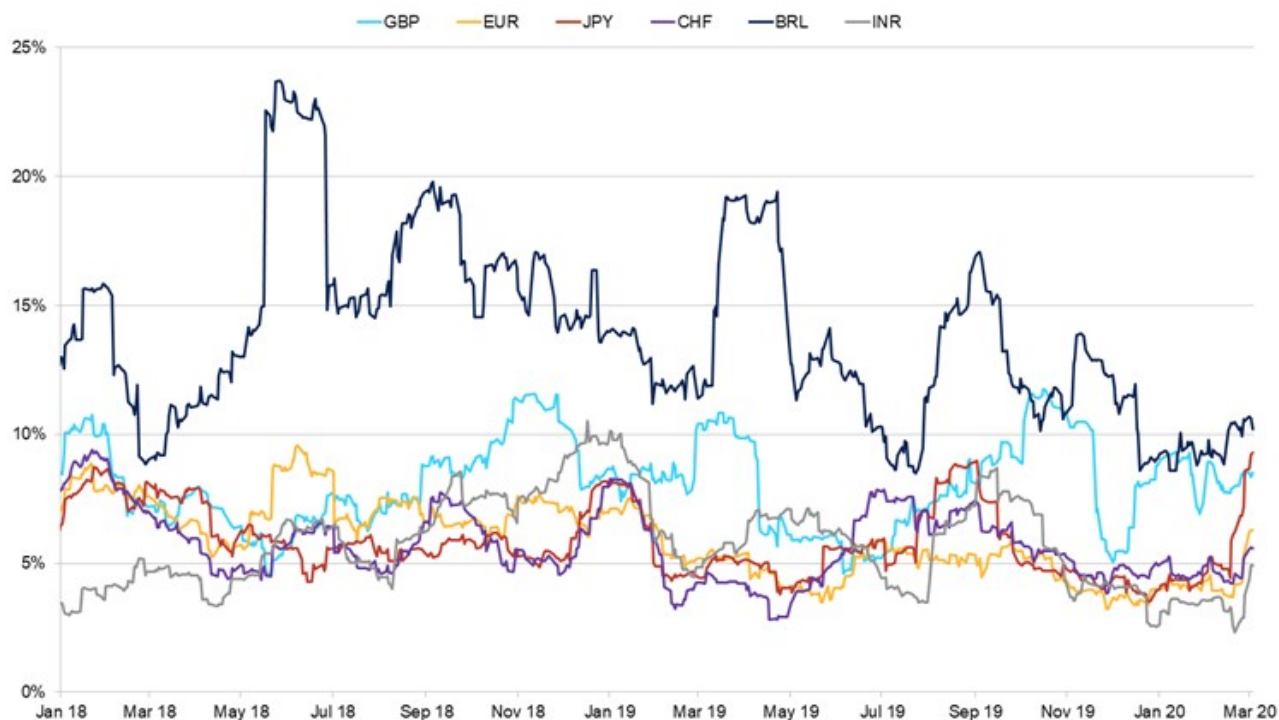
FX Volatility Grid

Time	EURUSD			GBPUSD			USDJPY			EURGBP		
	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	25d BF	ATM
1W	0.77	0.22	6.67	-0.16	0.17	7.48	-2.26	0.35	9.36	0.40	0.17	8.61
1M	0.68	0.26	6.08	-0.17	0.20	6.78	-2.46	0.35	8.26	0.48	0.22	7.55
2M	0.64	0.26	5.67	-0.24	0.21	6.46	-2.45	0.33	7.73	0.52	0.21	6.96
3M	0.62	0.27	5.60	-0.31	0.24	6.50	-2.48	0.36	7.39	0.59	0.25	6.88
6M	0.59	0.30	5.55	-0.49	0.27	6.74	-2.45	0.36	7.12	0.75	0.25	6.76
1Y	0.55	0.31	5.70	-0.76	0.32	7.33	-2.45	0.36	7.09	1.01	0.29	6.83

Time	USDINR			USDTRY			AUDUSD					
	25d RR	25d BF	ATM	25d RR	25d BF	ATM	25d RR	ATM	25d RR	25d BF	ATM	
1W	1.59	0.21	9.47	3.20	0.66	13.10	1.22	0.17	13.85	-0.94	0.25	8.61
1M	1.80	0.24	8.15	4.37	0.82	13.51	1.55	0.27	12.81	-1.12	0.26	7.98
2M	1.77	0.28	7.55	4.69	0.89	13.64	1.57	0.31	11.97	-1.16	0.28	7.73
3M	1.78	0.31	7.34	5.05	0.92	14.06	1.67	0.35	11.95	-1.21	0.30	7.75
6M	1.82	0.33	7.32	5.74	1.06	15.19	1.79	0.41	11.81	-1.32	0.32	7.83
1Y	1.89	0.39	7.28	6.68	1.24	16.56	1.98	0.51	11.67	-1.43	0.34	8.00

Source: Sueden Financial

Historical Spot FX Volatility (30D Rolling)



Source: SucdenFinancial, Bloomberg

FX Matrix (today)

	USD	GBP	EUR	JPY	CHF	CAD	AUD	NZD
USD	-	1.29	1.1145	0.009336	1.0474	0.7461	0.6632	0.6319
GBP	0.7751	-	0.86396	0.7237	0.8119	0.5784	0.51409	0.4898
EUR	0.8972	1.1575	-	0.83762	0.9397	0.6694	0.595	0.5669
JPY	107.12	138.186	119.39	-	112.182	79.926	71.04	67.687
CHF	0.9549	1.2318	1.06423	0.8914	-	0.7124	0.6332	0.6034
CAD	1.3402	1.729	1.49372	0.0125116	1.4038	-	0.8888	0.8469
AUD	1.5081	1.9452	1.68054	1.4077	1.5791	1.1251	-	0.9528
NZD	1.5827	2.0416	1.7638	0.01477	1.6574	1.1808	1.0496	-

Source: Bloomberg

Weekly Change

	USD	GBP	EUR	JPY	CHF	CAD	AUD	NZD
USD	-	0.10	1.31	2.31	1.34	-0.07	0.96	0.19
GBP	-0.13	-	1.20	2.19	1.23	-0.19	0.85	0.06
EUR	-1.30	-1.20	-	0.98	0.03	-1.38	-0.37	-1.12
JPY	-2.25	-2.16	-0.97	-	-0.94	-2.34	-1.33	-2.07
CHF	-1.32	-1.22	-0.03	0.95	-	-1.43	-0.39	-1.13
CAD	0.08	0.19	1.39	2.38	1.43	-	1.05	0.27
AUD	-0.93	-0.85	0.35	1.34	0.38	-1.03	-	-0.77
NZD	-0.18	-0.08	1.12	2.07	1.15	-0.27	0.78	-

Source: Bloomberg

Key Events & Releases

Region	Date	Time	Indicator	Period	Survey	Prior
US	05/3	13:30	Initial Jobless Claims	Feb 29	215k	219k
US	05/3	15:00	Factory Orders	Jan	-0.1%	1.8%
US	05/3	15:00	Durable Goods Orders	Jan	-0.2%	-0.2%
US	06/3	13:30	Trade Balance	Jan	-\$46.4b	-\$48.9b
US	06/3	13:30	Change in Nonfarm Payrolls	Feb	175k	225k
US	06/3	15:00	Wholesale Inventories MoM	Jan	-0.2%	-0.2%
CN	07/3		Trade Balance	Feb	\$29.30b	
JP	08/3	23:50	GDP QoQ	4Q	-1.7%	-1.6%
JP	08/3	23:50	BoP Current Account Balance	Jan		¥524.0b
CN	10/3	01:30	CPI YoY	Feb	5.2%	5.4%
EU	10/3	10:00	GDP YoY	4Q		0.9%
UK	11/3	09:30	Industrial Production	Jan		0.1%
UK	11/3	09:30	Manufacturing Production MoM	Jan		0.3%
US	11/3	12:30	CPI YoY	Feb	2.2%	2.5%
EU	12/3	12:45	ECB Deposit Facility Rate	Mar 12		-0.500%

Source: Bloomberg

Risk warning

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