

Deutsche Bank
Identifier



ECB FXCG

FX Derivatives

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Outline

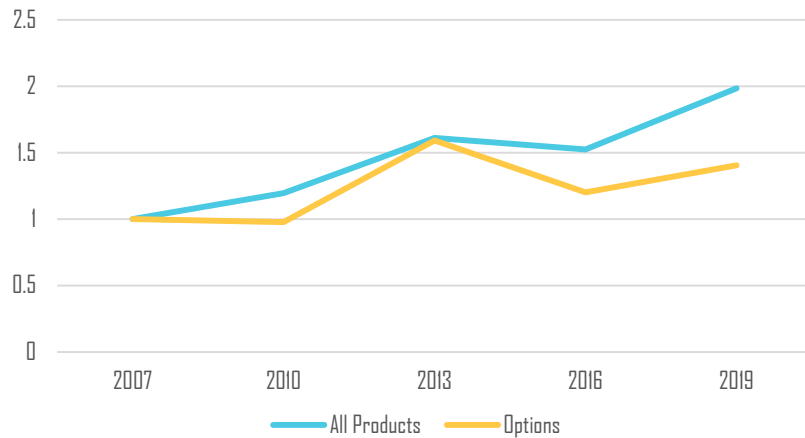


1. Market Overview
2. Recent Evolution in Market Structure
3. Client Activity
4. Liquidity
5. Predictive power of the FX Option market

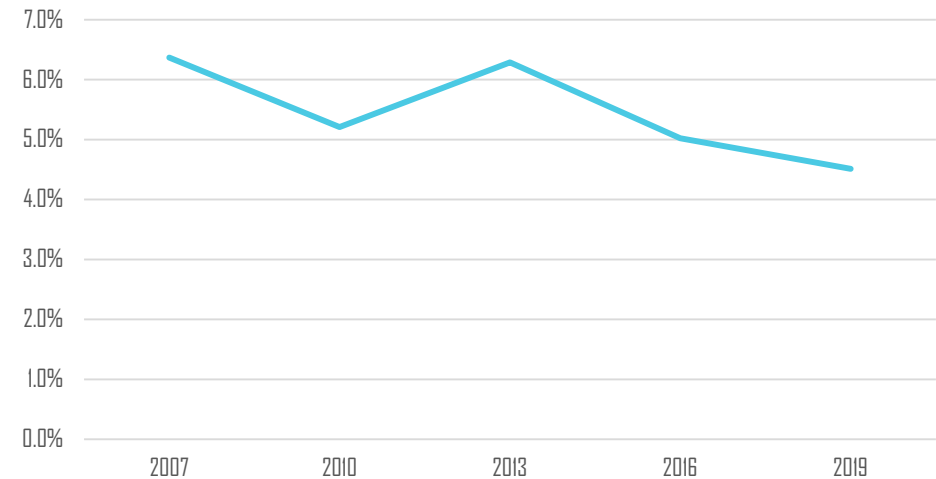
FX Derivatives – Market Overview



Relative BIS Survey FX Volumes

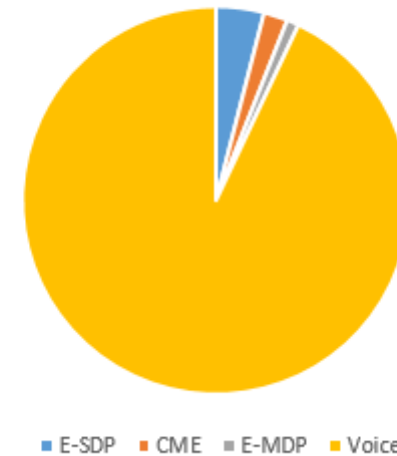


FX Derivatives as a percentage of FX Market turnover



- FX Derivatives make up less than 5% of FX market, a share that has dropped over time.
- Not much more than 5% of this is traded in a way that isn't 'voice.'
- Not where we thought we would be – electronification has thus far had a very limited impact on the market as a whole.

Derivative Volumes by Channel



FX Derivatives – evolution

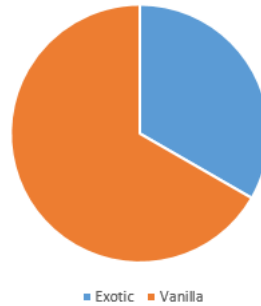


... Big efforts placed into electronic price distribution across the market.

DB Trades by Channel

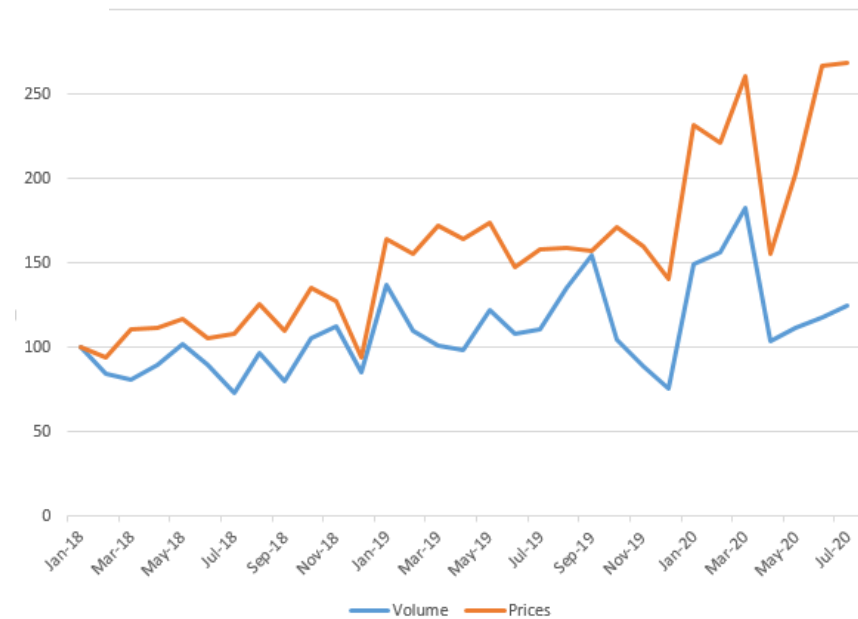


DB Trades by Type



- 4 out of every 5 trades DB trades is electronic
- 19 out of every 20 prices DB makes are electronic
- 1 in 3 trades is 'exotic'

- Unprecedented requests and volume in 2020
- Optimism for 'Virtuous' cycle

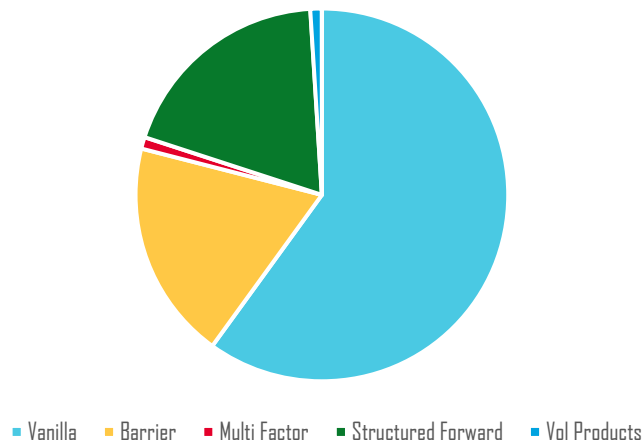


FX Derivatives – Client Activity



	Motivation	Vanilla	Barrier	MultiFactor	Structured Forward	Vol Product	Yield Enhancement
Corporate	Hedging, managing FX Flows	✓	✓		✓		
Private Bank	Speculation, yield enhancement, hedging	✓	✓		✓		✓
Hedge Fund	Speculation	✓	✓	✓		✓	
Real Money	Speculation, managing exposures	✓					
Example Trade		Vanilla	Knockout Option	Dual Digital	Target Profit Forward	Volatility Swap	Dual Currency Deposit

FX Derivatives Product Popularity



- Most client segments are active across both vanilla and exotic space
- Mix of volatility buying and selling across clients.

FX Derivatives – Liquidity Overview



	Vanilla	Vol Swap	Parity	Long Dates
EURUSD	Very Good	Very Good	Very Good	Good
USDJPY	Very Good	Very Good	Good	Good
AUDUSD	Good	Good	Good	OK
USDCNH	Very Good	OK	OK	Poor
USDBRL	Good	OK	OK	Very Poor
USDZAR	OK	Poor	Poor	Very Poor

- Liquidity in Derivative markets is dependent upon both what is available in the underlying markets today and expectations on what will be there in the future

1. Exotic liquidity is principally determined by vanilla liquidity
2. For EM currencies, rehedging costs increase exotic spreads. Good vanilla liquidity now doesn't guarantee it in the future.
3. Potential gap risks in spot will increase parity spreads
4. All else equal, long dated parity is lower spread than short dated
5. Most EM currencies have very poor liquidity beyond 2y

FX Derivatives – Predictive power?



- A common question is the degree to which the option market activity is predictive of future spot market moves
- Our research, using public market transaction data, indicates that there has historically been directional information in the asymmetry of option activity.

- Option flow indicators are estimated using data from the Depository Trust and Clearing Corporation (DTCC).

For a given currency pair, it is computed daily as follows:

1. We calculate option deltas for all European options expiring in less than one year, and select options whose (absolute) deltas range between 0.25 and 0.75.
2. We calculate the difference between notional volumes, traded on aggregate over the past 4 weeks, of the calls and puts from Step (1). This smoothed measure controls for noise and gives us the base notional volume imbalance.
3. We standardise the imbalance measure calculated from Step (2) by dividing it by its 1-year historical volatility.

