

DB FX Trade Idea

EURZAR-USDZAR Correlation Swap

Trade Idea

- Sell 6m EURZAR-USDZAR correlation swap at 80% (USD payout)
- Sell 1y EURZAR-USDZAR correlation swap at 80.5% (USD payout)

Rationale

- EURZAR-USDZAR implied correlations are close to the highest levels since 2007 (see graph 1)
- This has been driven by ZAR implied volatilities trading at their highest levels relative to EURUSD volatility since the financial crisis (see graph 2)
- Since 2007 the highest 6m realized correlation is 94% and the lowest is 41%. For 1y the highest is 93% and the lowest is 48%. Looking at shorter dated metrics, 3m realized correlation has fallen from recent highs to now sit close to current strikes (see graphs 3 & 4)
- The correlation swap provides a limited loss way of fading elevated ZAR volatilities and buying cheap EURUSD volatility, which could perform in the event of any Eurozone concerns such as the Italian election

Graphs

Graph 1: EURZAR-USDZAR implied correlation at highs

100%
40%
50%
60%
70%
80%
90%

Graph 2: ZAR vols elevated compared to EURUSD vols

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017

EURZAR-USDZAR 6m implied corr

EURZAR-USDZAR 1y implied corr

Graph 3: 6m realized correlation vs. strike

100%
20%
30%
40%
50%
60%
70%
80%
90%
-20
-15
-10
-5
0
5

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017

EURUSD-EURZAR 1y implied vol spread

Graph 4: 1y realized correlation vs. strike

100%

EURZAR-USDZAR 6m real corr

EURZAR-USDZAR 3m real corr

80.0%

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017

20%

30%

40%

50%

60%

70%

80%

90%

EURUSD-USDZAR 1y implied vol spread

EURZAR-USDZAR 1y real corr

EURZAR-USDZAR 3m real corr

80.5%

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017

Sources: Deutsche Bank, Bloomberg Finance L.P.

Disclaimer: <http://globalmarkets.db.com/new/content/3045.html>