

Classification: For internal use only

I like USDCAD call options to position for further weakness in CAD. Spot FX is currently 1.095.

Over the course of the past week the interest rate curve has started pricing in a small amount of rate cuts - this development is significant and clearly a beginning of a pain trade. I believe it can go further. Lower CAD rates from here will drive USD CAD higher.

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The limited downside play I like best in USDCAD is buying a 3month expiry 1.10 / 1.13 call spread on USDCAD but where the short 1.13 call position only exists (knocks-in) if USD trades at 1.17 trades in the market before the option expires, otherwise the option payoff is the same as a 1.10 call option.

It costs 1% of USD notional. I believe the buyer is well compensated for the knock-in component. If USDCAD rises to 1.15 the option payout is 5 big figures. If 1.17 trades before expiry the payout is limited to 3 big figures.

Max loss is premium paid.

We can price other structures to fit the risk tolerance (higher or lower) of clients - let us know

#### Key Macro Highlights

- The economy clearly lags the US. Dec13 unemployment unexpectedly rose last Friday to 7.2%
- South of the border demand for USDCAD is declining as the US heads towards energy independence
- Low inflation and weak exports are likely to preclude any rate hikes in 2014

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Best,  
Nav

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