

EM Alpha

Buy 1y USDHKD 7.7670/7.8500 call spread

Key takeaways

- Forward points in HKD is very low given the outperformance of HK vs US rates following the increase in US banking sector risk
- The vol-adjusted return of holding spot US\$ is declining as USDHKD will see occasional large declines inside the band
- Overall we expect spot USDHKD to stay near 7.85 throughout 2023 as our US economists do not expect any cuts by the Fed

1-year HKD forward points are very low at -835 pips

As discussed in [Asia FI & FX Strategy Watch: Why are HKD forward points at record low? 28 March 2023](#), forward points in HKD have pushed to a very deep level because of the recent outperformance of Hong Kong rates versus US rates following the increase in US financial sector risks. The market is pricing out additional material drain from the aggregate balance as the Fed turns dovish and the market expects a limited number of Fed hikes remaining in the cycle.

Prefer to long HKD carry via option structure vs spot

Given the late cycle dynamics of the Fed and the current level in the aggregate balance, we think the best way to continue pocketing the HKD carry is via option structure. Spot USDHKD will likely remain volatile and with occasional blow-up in front-end HIBOR fixings resulting in USDHKD to decline inside the band. However, for the remainder of 2023, our US economists do not see the Fed cutting rates at all and the cuts the market priced in for the Dec 2023 FOMC meeting is increasingly being priced out. As such, we expect the gap between HONIA-SOFR to stay wide and spot to remain sticky at 7.85.

We buy 1y USDHKD 7.7670/7.8500 call spread **paying 37bps in premium** with a max pay-out of 2.95 to 1. Risk to the trade would be an aggressive rally in US rates that significantly closes the HONIA-SOFR spread.

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GEM FI & FX Strategy
Emerging Markets Global

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For a complete list of our open trade recommendations, as well as our trade recommendations closed over the last 12 months, please see [Global Emerging Markets Weekly: The art of engineering dovish hikes 24 March 2023](#)

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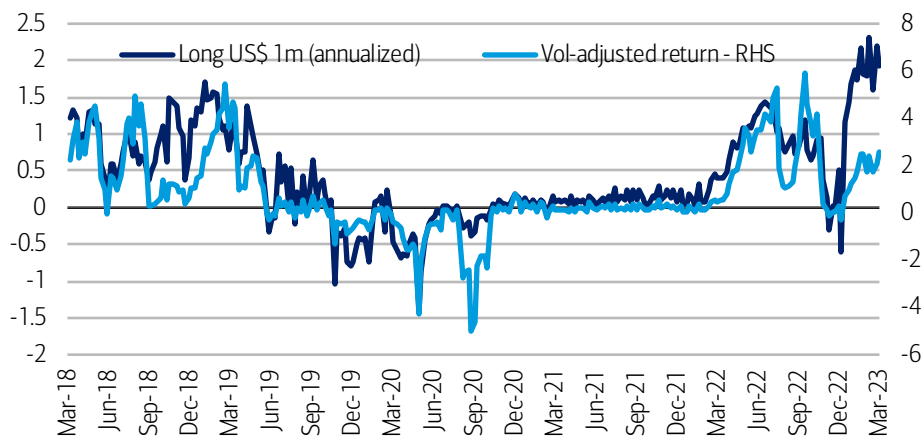
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Exhibit 1: US\$HKD carry (long US\$): Outright and vol-adjusted

The vol-adjusted return on holding spot US\$HKD has declined; hence, we like to pick up the carry via option structure



Source: Bloomberg

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