Financial Immunities

Spotlight on Market Volatility and Implications for Hedging

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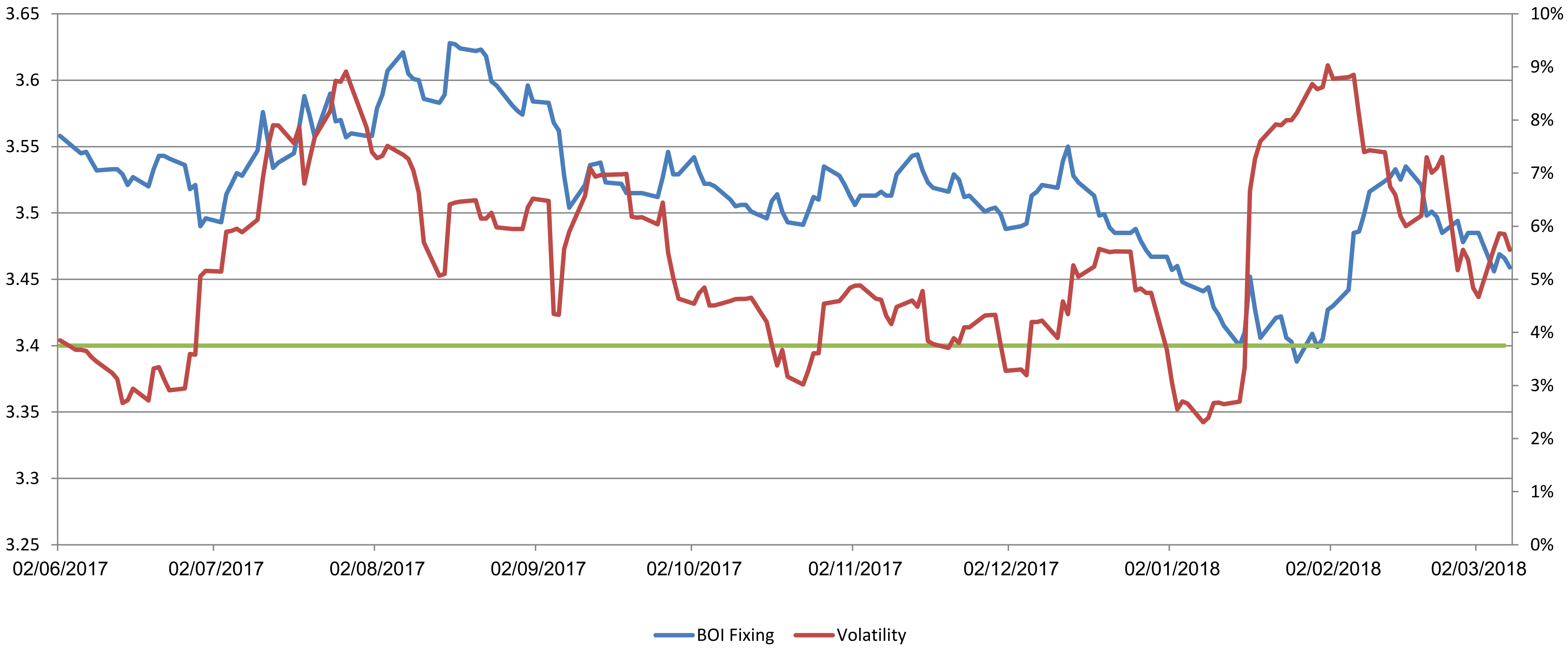
USDILS Market Volatility

- As we move closer to the psychological level of 3.4, there seems to be an increase in market volatility, which spiked to 9% in February

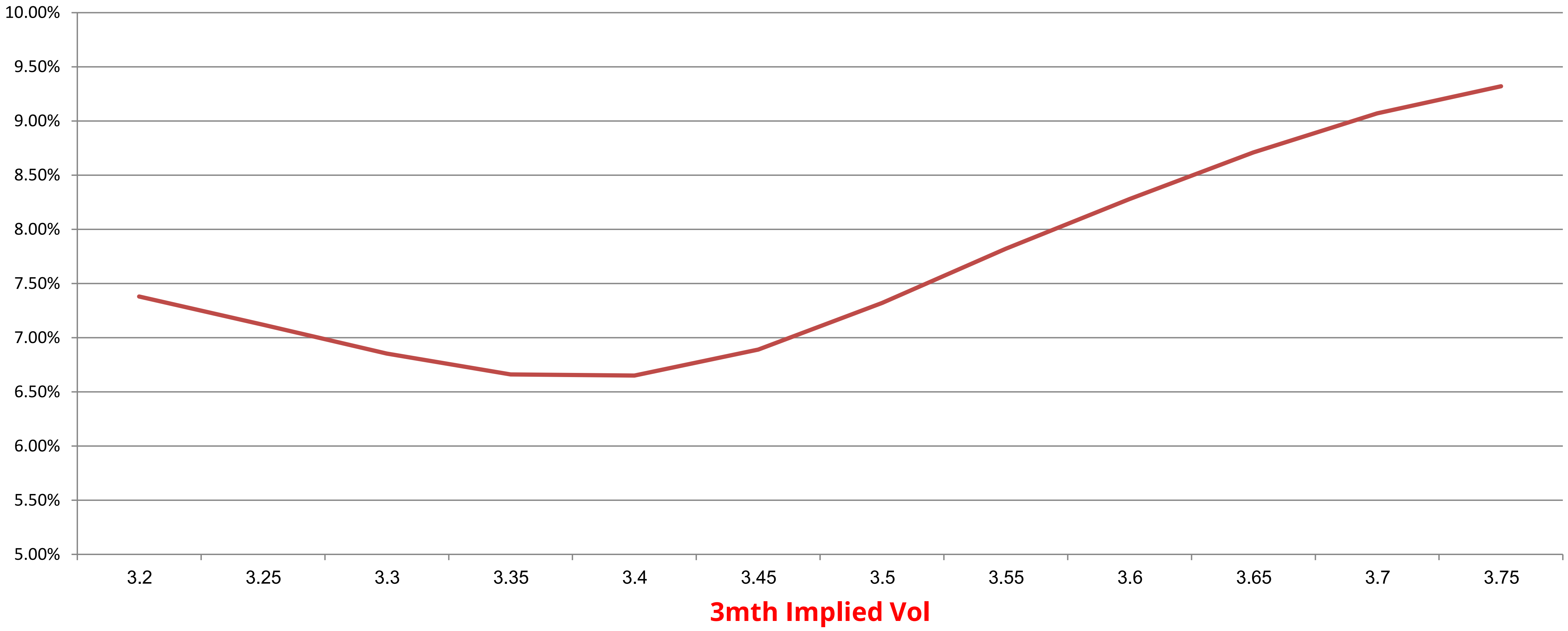
- The 3.4 level is key for several reasons:
  1. Historically, the BOI has intervened in this level (notable examples are 2008, 2011, 2014 episodes as well as last January)
  2. Market positioning :Hedging needs of market makers who will presumably try to defend the 3.4 level due to short Put positions.
  3. Intense speculative activity was a main factor in the strengthening of the shekel in 2017. A move beyond 3.4 might exacerbate this trend.

- Looking at the options prices (implied volatilities) , it seems that the market is willing to pay a premium to buy protection against USDILS depreciation rather than USDILS appreciation (Calls trading over Puts)

Realized Volatility



Option Prices (Implied Volatility)



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Hedging Implications

Player	Preferred Hedge Instrument
Exporter	Risk Reversals/Naked Put
Importer	Forwards

- Risk reversal strike choice for exporters should be as wide as possible due to the skewness of the vol curve (higher call prices as we move away from the spot rate)