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The information content in the offshore Renminbi foreign-exchange option market: Analytics and implied USD/CNH densities

Abstract

In line with the deepening of the derivative foreign-exchange market in Hong Kong, we recover risk-neutral probability densities for future US dollar/offshore renminbi exchange rates as implied by exchange rate option prices. The risk-neutral densities (RND) approach is shown to be useful in analyzing market sentiment and risk aversion in the renminbi market. We include a forecasting exercise that confirms market participants were able to forecast the shape of the actual densities correctly for short horizons, even if their exact location could not be determined.

Keywords: offshore renminbi, options, risk-neutral densities, real-world densities, forecasting

JEL Classification: C53, F31, F37

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