TRINITY SMF

STUDENT MANAGED FUND

Shorting the Turkish Lira
Trading Idea Report

December 2020

Shorting the Turkish Lira

Overview

- Short *now.* COVID19's tourist restrictions, plummeting domestic activity, and Turkey's economic mismanagement has left the Lira exposed to international shock.
- We foresee a currency crumble contingent on a US-Turkish bust-up within 1 year over Erdogan's policies that will go against a Biden administration priority that will result in US sanctions and a decline in investor appetite in Turkey.

Thesis

- National Turkish currency sits at a precarious position in the International Currency Market

Some factors include:
- High Inflation
- Low interest rates
- Depleting Central Bank reserves
- Imprudent governing
- Volatile political relations internationally

- Given Erdogan's poor geopolitical management and stubborn posture on Central Bank policy, we foresee further deterioration over the coming months, irrespective of economic reforms given ruination of central bank reserves.

Valuation

Indicator	Value	Expectations	Effect on Currency
Gross Domestic Product (GDP)	$755 billion 2019 -11% Q2 2020	Worse than expected	Negative
Consumer Price Inflation (CPI)	487.38 Oct from 477.21 Sep 2020	Worse than expected	Negative
Trade Balance	-4827.67bn	Better than expected	Positive
Current Account	Median poll response of 10 economists was for a deficit of $33 billion (Reuters)	Worse than expected and deficit will only grow with various Covid response	Negative
Central Bank benchmark rate	15.75%	Lower than expected leading to continued economic fallout	Negative
ISM Manufacturing Index	53.90 50< which represents a growth in manufacturing and production	In line with expectations.	Positive
Central Bank FX Reserves	41.91 billion (Lowest since 2005)	Worse than expected	Negative

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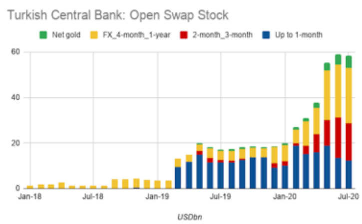
USD/LRY TTM

Turkish Central Bank: Open Swap Stock



Catalysts

President Erdogan
- Unorthodox economy policy, preferences for low interest rates and easy access to credit which he believes will lower inflation
- Whilst he has temporarily committed to higher interest rates to boost investor confidence, we believe he will revert to form in the medium term with an eye to a Presidential election in 2023.

Almost no FX reserves left
- 10's of billions of dollars have been burnt through in the maintenance of an unofficial currency plug .
- Central bank has spent $65bn on supporting the currency this year alone.

Foreign Policy
- Turkey has pursued a foreign policy that has pivoted away from its traditional US and European allies towards a more aggressive posture. Aspects of this include:
  - S400 purchase from Russia
  - Aggression against Kurds in Northern Syria
  - Posture against Greece in the Eastern Mediterannean
  - Use of refugees as leverage against the EU
  - Incursion into Libya

Risks and Logistical Concerns

- Potential for restrictions on borrowing, making it hard to short; up till 11th of November the cost of borrowing was extremely high; potential for this to re-emerge
- Turkish CB set a one-week repo rate of 15.75% which resulted in some short-lived recovery, now pared back to a just 1.9% increase against the dollar compared to before the announcement
- Change in Turkey's foreign policy stance based on potential for Biden administration pushback