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TRADING CURRENCY FUTURES ON THE INTERNATIONAL MONETARY MARKET

Trading in foreign currency futures on the International Monetary Market of the Chicago Mercantile Exchange began on May 16, 1972.

The purpose of this report is to acquaint potential users of foreign currency futures with the manner in which they will utilize the International Monetary Market (hereinafter designated the IMM). Among the potential users are:

1. Individuals as speculators
2. Importers and exporters
3. Multinational companies, as hedgers
4. Banks foreign exchange brokers and securities dealers.

MONEY MARKET BANKS, THE IMM AND THE CHICAGO MERCANTILE EXCHANGE INC.

Although the large money market banks in cities such as New York, London, Zurich and Toronto are engaged in forward operations in dollars, pounds or deutschmarks already, the market is primarily professional. Only very large corporations and individuals with substantial lines of credit are able to utilize these facilities.

The reluctance on the part of banks to deal with individual non-commercial (perhaps speculative) accounts naturally leads the latter to shy away from banks, the more so because banks tend to have a slightly wider bid/asked spread on the further forward (12-18 months) positions that speculative accounts prefer.

In addition, speculators greatly prefer to deal on a liquid publicly-quoted market where, even at times of major price movements some bids or offers are likely to emerge. In dealing on a non-public market speculators always fear that their counterpart will, at times of major price change, refuse to quote any price at all or, perhaps even more anxiety-provoking to the speculator's desire for reliable liquidity, quote a price he considers manifestly unfair.

Finally, most of that large group of individuals (believed to number well over two hundred thousand) who currently trade commodities will undoubtedly, if they find foreign exchange futures of interest, use this market rather than banks for they already maintain accounts with commodity brokers and probably have little or no access to foreign exchange departments of banks.

In order that the foreign exchange futures market be as broad and thus as liquid and deep as possible, it is essential that the trading occur on the floor of a large organized exchange which has hundreds of floor brokers and direct phone lines to brokerage.

houses all over the United States and the world. For this reason the market would be where the largest number of floor brokers, commodity houses, and speculators converge and this is certainly Chicago, home both of the Chicago Mercantile Exchange and the Chicago Board of Trade, the oldest and largest commodity exchanges in the United States.

The Chicago Mercantile Exchange has over 500 members, 200 active floor brokers and 80 clearing members which simultaneously trade in eight commodities including pork bellies, cattle, eggs, potatoes, hogs, lumber. As a measure of its success in 1971 over three million contracts with a gross value of over forty billion dollars were traded on this exchange.

TRADING UNITS MARGIN REQUIREMENTS AND COMMISSION RATES.

At the present time, seven currencies enjoy futures trading at the IMM and these are:

Currency	Contract Size	Initial Margin Requirements	Maintenance	Minimum Fluctuation	Daily Limit
British Pound	50,000	2,500	2,000	.002 (\$10)	.014(\$700)
Mexican Peso	1,000,000	1,500	1,000	.00001 (\$10)	.0005 (\$500)
Canadian dollar	200,000	2,000	1,500	.00005 "	.0035 (\$700)
Deutschemark	500,000	2,500	2,000	.00002 "	.0014 "
Swiss Franc	500,000	2,500	2,000	.00002 "	.0014 "
Italian Lira	50,000,000	2,000	1,500	.0000002 "	.00001 (\$500)
Japanese Yen	25,000,000	2,000	1,500	.0000004 "	.00003 (\$750)

Initial margin requirement (or Security deposit) is the minimum amount of money per contract required to institute a currency position. Maintenance is the minimum amount of money required to be maintained for each contract position figured to the market.

Daily limit is the maximum daily movement, up or down, and reckoned from the previous day's close permissible under Exchange rates. In case of large revaluations or devaluations, currencies on the IMM will adjust to their new parities by moving up or down the 'limit' a number of days in succession, provided such an event was not already discounted by the futures.

Currency	Overnight ¹		COMMISSIONS Day Trades ²	Spreads	
	IN	OUT*		In	Out*
British Pound	\$20	\$20	\$ 25.00	\$40	\$10.00
Mexican Peso	\$20	\$20	\$ 25.00	\$40	\$10.00
Canadian Dollar	\$20	\$20	\$ 25.00	\$40	\$10.00
Deutschemark	\$20	\$20	\$ 25.00	\$40	\$10.00
Swiss Franc	\$20	\$20	\$ 25.00	\$40	\$10.00
Italian Lira	\$20	\$20	\$ 25.00	\$40	\$10.00
Japanese Yen	\$20	\$20	\$ 25.00	\$40	\$10.00

1. Trades not offset the same day
2. Trades offset the same day
3. Spreads consist of the assumption of a long (purchase) and a short (sell) position on the same business day in the same or related currencies for the same account.

* "Out" may include offset by delivery.

TRADING EXAMPLE:

Suppose that on May 16th you asked us to buy for your account 1 July contract of Canadian dollars. You reasoned that substantially higher short term interest rates in Canada would continue to attract foreign capital and that, as a consequence, the Canadian dollar was bound to move up in relation to the U.S. dollar. In order to buy the Canadian dollar contract you deposited a \$ 2,000 margin (see Margin schedule).

Let us see how it worked: you purchased a July contract at 1.00735. On May 29th you decided to sell. Let us assume that you sold at 1.01480 (the close of the July contract on May 29). Your gross profit was 745 points ($1.01480 - 1.00735 = .00745$) or \$1,490 ($.00745 \times 200,000$). Your commission of \$ 40.00 would be deducted from your gross profit of \$ 1,490.00, leaving \$ 1,450.00 net profit. You made \$ 1,450.00 on a \$ 2,000.00 - investment in a period of 10 days.

This example was given with the sole intention of demonstrating the potential for speculative trading as well as the actual mechanics of the trade. It should not imply in any way that currency futures speculation is an easy endeavor. Individuals wishing to speculate must study very carefully all the major factors affecting the movements of exchanges and be abreast of all current economic and political events of importance.

FUNDAMENTAL FACTORS AND ANALYSIS

Major factors affecting foreign exchange are 1) balance of payments figures, 2) productivity (G.N.P), 3) government budgets and expenditures (fiscal policy), 4) the money supply and interest rates (monetary policy), 5) unemployment, and 6) political and social factors.

The most sensitive fundamental indicator in foreign exchange appears to be interest rates, as these affect the flow of currencies from one country to another, seeking the highest rate. Expectations of future changes in direction also affect the market both in spot and futures.

"If, for example, sterling is expected to depreciate, prospective recipients would sell it forward; speculators also would sell it forward. Banks and other dealers, in buying these forward sales contracts, build up their forward positions, in sterling. They may sell spot sterling to hedge their forward positions, thus putting downward pressure on the spot rate. Anticipation of a rising rate would tend to have the opposite effect.

Interest-rate differentials among international financial centers is another linkage between spot and forward rates. For instance, unless the spread between spot and forward rates for a foreign currency is such that the cost of covering the exchange risk is about equal to the difference in comparable interest rates in the United States and the foreign country, there is an inducement to shift funds to take advantage of the higher rates.

An outflow of funds to take advantages of a higher net return on British bills would tend to eliminate the profit opportunity. As already indicated, a United States purchaser of 90-day British bills would buy spot sterling to pay for them and sell 90-day futures to cover his exchange risks. The resulting increased demand for spot delivery and increased supply of forward sterling would widen the spread between the two rates and increase the cost of hedging an investment in British Treasury bills. The outflow of short term funds would tend to raise interest rates here and lower them in England. Thus, interest-arbitrage transactions tend to narrow the differential in interest rates and widen the spread between spot and forward rates"6 ("Defending the Dollar", The Federal Reserve Bank of Philadelphia, Philadelphia, 1970, p.22)

TRADING HOURS, MATURITIES AND DELIVERIES

Trading hours will be 9:30 A.M. - 2:30 P.M. Toronto time.

Bids, offers, and transactions occur for a particular "month" (the three months following the current month and each March, June, September, and December thereafter for total of eight different maturities). However, all contracts actually mature on the third Wednesday of those months. Thus, while the quotations may be for "December pounds", "March Yen", or the like, the former entails delivery of pounds sterling to the buyer's U. K. bank on December 18th against payment in dollars of specified sum of Continental Illinois National Bank and Trust Company of Chicago; the latter obviously entails payment in yen the buyer's Japanese bank of the third Wednesday of March against payment in dollars to Continental, the Exchange's clearing bank.

PROGRESS TO DATE

The first full week of trading on the IMF (May 16 - May 22) saw a spectacular 3,657 futures contracts traded (one of the most successful starts in the history of Commodity futures trading) with a total value of approximately \$ 622,380,000.

The Canadian dollar was by far the most heavily - traded, with 2,013 contracts worth about 405.6 million dollars, accounting for more than one-half of total volume and total value. The Deutschmark with 850 trades estimated at 129.6 million dollars in value came next, followed by British pound with 316 trades worth about 41.1 million, and the Japanese yen with 246 contracts valued at about 19.7 million. There were 167 trades in Swiss francs, 60 in Italian Lire, and 5 in Mexican Pesos.

A further measure of success of a newly established contract is the total open interest. Open interest is the total number of open or outstanding contracts; it refers to unliquidated purchases or sales and never to their combined total. Total open interest on May 26 stood at 2,022 contracts for the seven currencies traded with the Canadian dollar again holding top spot with 330 contracts and followed by the Deutschmark (505) and the British Pound (366). The Canadian dollar open interest represents over \$ 166 million.

Friedberg & Co. Ltd is a foreign currency dealer maintaining markets in the principal spot currencies.

As international commodity brokers, we provide trading facilities on all Commodity Exchanges in the U.S. and the London Metal Exchange. Trading on the IMF is conducted through our U.S. Correspondent Brody, White & Company Inc.

The latter is the commodity brokerage subsidiary of the internationally - known Mocatta Commodities Corporation, an affiliate of the Hambros Bank, one of London's oldest and largest merchant banks, and sister company to Hambros' wholly-owned bullion subsidiary Mocatta & Goldsmid, Ltd. which has since 1684 been a member of the London bullion market.

All statements made herein, while not guaranteed, are based on information considered reliable and are believed by us to be accurate.