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## COMMODITY COMMENTS

July 24th, 1973

The past few weeks have seen an incredible surge in commodity prices, perhaps unequalled in modern history. At the end of June, the Reuters Commodity Index first topped the 1,000 mark, ten times its base of 100 on September 18th, 1931.

Yesterday's index of 1,107.1 against 577.5 on the corresponding Monday last year means that the index rose 477.5 points in the entire period from Sept. 18th, 1931 to July 24th, 1972 & then soared another 529.60 points in the past 12 months. Since June 29th, the day of the D-Marks latest revaluation, the pace quickened to a torrid annual rate of 165 percent. As we have previously commented, the commodity bull market has been the other side of the currency, particularly the U.S. Dollar, bear market. In the words of the Federal Reserve Bank of New York, the February devaluation & subsequent flight from the dollar were " a shattering blow to confidence."

The flexible exchange rate system is in great part responsible for the general debasement in currencies. We have conclusively proven that exchange rates will not, on their own, find an equilibrium level conpatible with trade considerations. In the first place, exchange rates are a function of interest rate arbitrage, & interest rate arbitrageurs, as money market dealers know, do not care in the least about the absolute level of Sterling or D-Mark. so long as the swap or covered transaction is profitable. This will tend to move huge amounts of short term capital from one country to another regardless of apparent undervaluations or overvaluations. The proof to the pudding lies in the British Pound - when the Bank rate soared above 11%, Sterling firmed to 2.5850 ( from 2.35 less than 2 months earlier ) despite it being highly overvalued on trade considerations. With the Bank rate down to 7.5%, Sterling began falling & hit 2.5305 before the Bank of England raised its rate again to 9%. Even that rate is low in relation to prevailing Eurodollar rates; therefore the downside pressure on Sterling (obviously Sterling is a good short given present interest rate structure). Again, the recent easing of D-Mark interest rates on deposit, was the main influence in halting the sliding U.S. Dollar at 2.3050 despite the fact that the D-Mark is also obviously overvalued on trade considerations.

The second reason why floating rates are not self-equilibrating is that they are self-fulfilling. A devaluating currency eventually brings internal purchasing power down to justify that lower external level. That is the lesson of the depreciating dollar vis a vis soybean, cocoa, cotton or even livestock. While everyone cites the well know statistic that U.S. inflation is lower than European, we predict that the depreciating U.S. Dollar will reverse this " obvious truth " & American inflation will surpass European before year end.

What can be done? Raise the price of gold to make U.S. short term liabilities convertible - that may be anywhere in the area of $150 to $250/oz. Secondly, redeem *these liabilities & do away once & for all with the double-counted greenback which has been fuelling inflation here & abroad. Support these moves with a tight monetary policy that will bring interest rates up to realistic levels - i.e. more compatible with present rates of inflation. Weeks ago we suggested that at 9%. Eurodollars & CD's were still behind by 3 percentage points. In fact, today at 11½% for six months we are still behind by 2 or 3 percentage points. Subsequent to the major gold revaluation allow the U.S. dollar to move up ( which we think it might do quite strongly ) & then fix the exchange rates within a narrow 1% band.*

*What can be expected? Nothing of the above. More temporizing & more threats will be the result. Swap arrangements will be exhausted ultimately & a short squeeze on the Federal Reserve may take place when the Fed moves to cover its short D-Mark & S-Franc commitments. Therefore, buy D-Mark & S-Franc if they penetrate previous highs (44.40 & 37.30 respectively ) as this will indicate that a squeeze is on. Unilateral gold sales on the part of the U.S. will not be undertaken as such is considered foolhardy even by U.S. Treasury officials. A concerted selling effort, on the other hand, by a few large central banks, although quite unlikely, could force gold lower in the short run. Since such action will go unannounced at first, only go by the "tape". Therefore sell gold if it breaks below $114 basis London Fixing & you might sell D-Marks & S-Francs too. In the short run, a good profit could be made.*

*Not being prophets, we have then established the parameters for action in the international monetary arena. Do not try to outguess the market but rather act on the facts as shown by the "tape".*

| WOULD SUGAR #11 | | | |
|---|---|---|---|
| | September | '73 | 9.95 |
| | March | '74 | 9.17 |

*F. O. Licht, European sugar authority, forecast a global carryover stock ( on September 1st ) of 16.2 million metric tons, down 800,000 tons from a year earlier & the smallest since 1964. Production is estimated at 77.458 million metric tons against consumption at 78.450 million tons, thus completing the third deficit year in a row.*

*Rough estimates for the coming 1973-74 season indicate an increase in production of just under 4 million tons ( an optimistic appraisal ), evenly divided between Brazil's cane production & the European beet crop. Additionally, some allowance is being made for increased output in counties such as Australia & India.*

*Once again we believe (just as we firmly believed in cocoa & events bore us out ) that consumption is the largely overlooked & most critical consideration. Most analysts prefer to project a 2 - 2½% growth rate in consumption for 1973-1974, just below the recent annual increase of 3½%. At a total level of 78.0 million tons consumption for 1972-1973, a 2½% increase would mean just under 2.0 million tons, a 3½% growth rate would indicate a consumption increase of 2.7 million tons, both figures well under the expected increase in production. We prefer to think that consumption will resume its long term growth rate of 3½% & therefore will tend to make up for the 2 - 2½% growth rate achieved during 1972 - 73. The reason is simply inflation & the U.S. Dollar devaluation. A case can easily be made that sugar prices today, at 9½ - 10 ¢, are lower than the past season's 8¢ average ( with a peak of 10¢ ) when considering a 30% dollar devaluation & the huge rise of other commodity* *prices ( see Reuters Index story mentioned above ). A more realistic projection would be 4½% while 5½ would not be totally impossible ( consider 1965/66 when prices in real terms dropped ). At 78.0 million tons consumption for 1972 - 1973, a 4½% growth rate would indicate 3.5 million tons while a 5½% rate would result in a jump to 4.3 million tons.*

*The above figures could mean a standstill regarding carryover stocks for the 1973 - 74 season, but the increased level of consumption would drop the critical "stock as a % of consumption" below 20%, a level reached only in the formidable bull market of 1962 - 63. Such an event, in our view, would support a price well in excess of 14¢/lb.*

*Technically, the market has formed a terrific high level consolidation with an upside barrier,basis the nearest contract, of 10½ - 11¢. An attempted breakout took place yesterday in the distant delivery months accompanied by heavy turnover; if the upmove persists & betters 9.60 basis March '74, we will have entered into one of the last incipient bull markets of the year.*

*Contract consists of 112,000 lbs, margin required is $1,500 & round turn commission is $62. London call optionsare available with March '74 being quoted at £10.75 per ton ( 50 ton contract). Call options are highly recommeded for high risk averters.*

## *TECHNICAL TRENDS*

*COCOA:* | *September '73* | *84.90 b.*
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 | *December '73* | *76.90 b.*

*The spectacular uptrend continues without an end in sight. Our objective of 75¢/lb. has been easily surpassed. Open interest remains flat but volume & volatility are on the rise.*

*Remain long for the last short squeeze.*

*N. Y. SILVER:* *December '73 305.70*

*Our aggressive posture is paying off handsomely. Remain long with protective stops at 2.90 basis Dec. '73.*

*COPPER:* *December '73 88.10*

*Like we said before "no doubt we are still headed higher".*
*Be long but careful ( American export controls could hurt this market).*

*CORN:* *December '73 2.44 ½*

*Another spectacular mover. Sell Dec. '73 on a move above 2.50.*

COTTON: Dec. '73 61.30

Our June 27th suggestion: " a new bull move has begun which should take price to the low 60's in fairly short order".

Is 3 weeks short enough?

Remain long & place stops belos 58.20 basis Dec. '73.

| | | |
|---|---|---|
| LIVE CATTLE | Feb. '74 | 55.27 |
| LIVE HOGS | Feb. '74 | 53.60 |
| BELLIES | Feb. '74 | 77.02 |

On June 27th prices were 48.75, 43.40 & 62.55 & we said "there has been no easier way to make money than riding the huge bull market in livestock. Investing in livestock futures still remains are of the finest inflation hedges anywhere".

Keep in close contact as we might indicate a selling point anytime in the next few days.

| CANADIAN SILVER COINS | | |
|---|---|---|
| | Sept. '73 | 1420 - 1580 |
| | Dec. '73 | 1450 - 1610 |
| | Mar. '74 | 1480 - 1640 |
| | July '74 | 1520 - 1680 |

As we have been predicting for the past few months this market is getting increasingly "tight". Disappearance & illegal operations have slowed retail offerring to a trickle & rising dealers' bids are unable to dislodge hoarders.

The magic 1500 has been bid for March'74 & July '74 traded today as high as 1700. Discount to bullion has continued to narrow & now stands at less than 8½%. The discount should disappear before the end of September should bullion continue firm.

Deferred positions can still be bought with the doubleobjective of playing the "discount" & the silver bull move.

| RUBBER: | | |
|---|---|---|
| | Oct./Dec. '73 | 43.25 - 43.75 |
| | July/Sep. '74 | 40.40 - 40.75 |

In our last comments we suggested adding to long positions in the 30.00-32.00 area basis Oct./Dec. '73. Such an opportunity presented itself in the subsequent week & then prices literally exploded on the upside. A sharp setback took place last Friday & Monday with Oct./Dec. '73 dropping from over 44 p./per kilo to just over 39.25 but the upside momentum remains; at the close of today new contract highs are being reached in the forward positions.

This market can still be bought but only on sharp setbacks. Roll over Oct./Dec.'73 & concentrate on Jan./Mar. '74.

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Past Commodity Comments are now available on request.
An irregular printing schedule will be followed for the rest of the summer but should return to the normal semi-monthly issue by the Fall.
All statement made herein, while not guaranteed, are based on information considered reliable and are believed by us to be accurate.

Albert D. Friedberg
Vice-President
Commodity Futures