

FRIEDBERG'S

COMMODITY & CURRENCY COMMENTS



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Will the Quiet Crisis Lead to a Powerful Crunch?

Hardly a week passes that another financial institution does not undergo a shotgun marriage. Savings and loans (S&Ls), whose net worth falls below 2 per cent of deposits, are forced to be absorbed by other S&Ls, whose financial condition is anything but creditworthy. Aggregate net worth as a percentage of liabilities has fallen continuously since December 1979, to 4.47 per cent at the end of 1981 from 5.91 per cent, and probably stands at just under 4 per cent by the end of the first quarter of 1982. And it could not be otherwise. Cost of funds for these institutions averaged 11.53 per cent in the last half of 1981 versus a mortgage portfolio yield of barely 10 per cent.

On April 14, the Federal Home Loan Board and California state officials, in an as yet unprecedented move, took control of Fidelity Savings and approved the formation of a new association to assume its property, deposits and loans, totalling \$2.93 billion. As usual, the Federal Savings and Loan Insurance Corporation (FSLIC) undertook to make good on deposits of up to \$100,000, thus protecting depositors and wiping out shareholders.

Just a few weeks earlier, Richard Pratt, chairman of the Federal Home Loan Bank Board, predicted that as much as 25 per cent of the industry, approximately 900 savings and loans institutions, would exhaust their capital funds if interest rates remained close to current levels over the next two years. Incredibly enough, even if short-term rates were to drop 3 percentage points, as many as 714 S&Ls would see their net worth drop below the critical level of 2 per cent by the end of 1982.

And that is not all. While book losses resulting from negative yield spreads incurred during the particular period under review may well exceed \$5 billion, the present value of such losses, assuming *present* money market rates, has been variously estimated at *anywhere between 50 and 100 billion dollars*, two to four times the present aggregate net worth of S&Ls and seven to 14 times the book value of the FSLIC fund.

Just one month earlier, Treasury Secretary Donald Regan objected to a private forecast that drew similar conclusions to those expressed by Mr. Pratt. The Administration argued that interest rates would, very conveniently, drop sufficiently over the next twelve months to bail out the industry. Mr. Regan understands fully the implications of screaming "fire" in a crowded theatre. Unfortunately, Mr. Regan also believes there is no fire in the theatre.

An analysis that merely projects a drop in net worth, albeit a very large one, merely understates the gravity of the situation. Depositors do not live in a static environment and are not ready to block their assets, notwithstanding assurances from the FSLIC. Witness the extraordinary outflow of more than \$70 million from Fidelity Savings in the week ended April 5. During 1981, withdrawals at the S&Ls and about 400 mutual savings banks exceeded deposits by no less than \$39 billion, while their combined net worth dropped \$6 billion.

While these funds are not lost to the financial system as a whole, massive S&L withdrawals tend to have the following effects: (a) accelerate bail-out efforts by the Federal

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Gold: It looks like just a bear market rally . . .

Contributors

Albert D. Friedberg

Michael Beech

Home Loan Bank and FSLIC, possibly forcing the use of federal funds and thus aggravating immediate budgetary problems; (b) spread fear in the financial markets, threatening to force a collapse of weak financial and nonfinancial corporations; and (c) at the very least, increase the credit-worthiness spread in market rates, thus further threatening to topple weak borrowers.

It should be noted that (a), above, could have devastating effects on inflation psychology should market participants begin to perceive the magnitude of the potential call on federal funds. As a result, long-term rates of interest would remain substantially higher than otherwise justified by supply and demand considerations.

Can Mr. Regan be right in hoping for a substantial drop in short-term rates? Hardly. Recent flow of funds statistics exculpates the federal government from the charge of being the main cause of high interest rates. Chart 1 shows that credit markets in the previous recession year of 1975 handled rather well the extraordinary 129 per cent jump in government borrowings. This \$62.6 billion increase was more than compensated by a spectacular \$85.4 billion drop in private sector short-term borrowings. On the other hand, in the 1980/1981 recession, government borrowing increased a mere 12.4 per cent, by \$17.2 billion, but private sector short-term borrowing increased too, by a whopping \$71.4 billion, or 57 per cent. Furthermore, total government borrowing, at \$155.9 billion, represents in real terms a substantial drop from the \$111 billion of 1975. The budget deficit *panic*, as so many other press favorites, is much ado about nothing. The real culprit is the private sector illiquidity and its (inelastic and) voracious demand for credit.

S&Ls, other financial institutions and the great majority of American corporations have not only become progressively more illiquid (as we discussed last month) but they have, almost unanimously, taken a massive short position in interest rates futures by simply betting that it will be far more profitable to get locked in long-term rates tomorrow

rather than today.

Now then, these corporate citizens' market position in respect to interest rates is very much akin to that of a massive and widely identified short (or long) position in the commodities markets by someone who is found bucking the trend. Such positions have never been forgiven; they have *always* been forced to liquidate just before becoming insolvent (and in some cases forced into insolvency) and just before the market turns around.

Our short memory recalls some of the most notorious examples, such as the squeeze on the long cocoa position held by Mr. Erhard's Swiss unit of the UCB bank (1970) and its bankruptcy, and the squeeze on the Hunt brothers' long silver position (which led to the liquidation of their silver futures positions, their disposal of huge chunks of real estate, oil and gas interests, as well as a restrictive refinancing operation through Placid Oil).

From a purely technical point of view, we must conclude that the US financial system's short position will have to be covered with losses so substantial as to border on generalized insolvency.

As the run on financial institutions gathers momentum and begins to exact too heavy a toll in terms of social costs, the US government will inevitably mount a bail-out operation. The mood of austerity reigning on Capitol Hill, as well as official pronouncements that all is well with our financial system, presage that the ultimate reflation is still some time away.

STRATEGY: Sharp increases in the adjusted Monetary Base are beginning to show up in higher-than-expected money supply figures. The Fed will be forced to rein in just at a time when the US financial system is approaching a powerful crunch whose first signs are an accelerated bleeding of S&Ls and mutual savings banks.

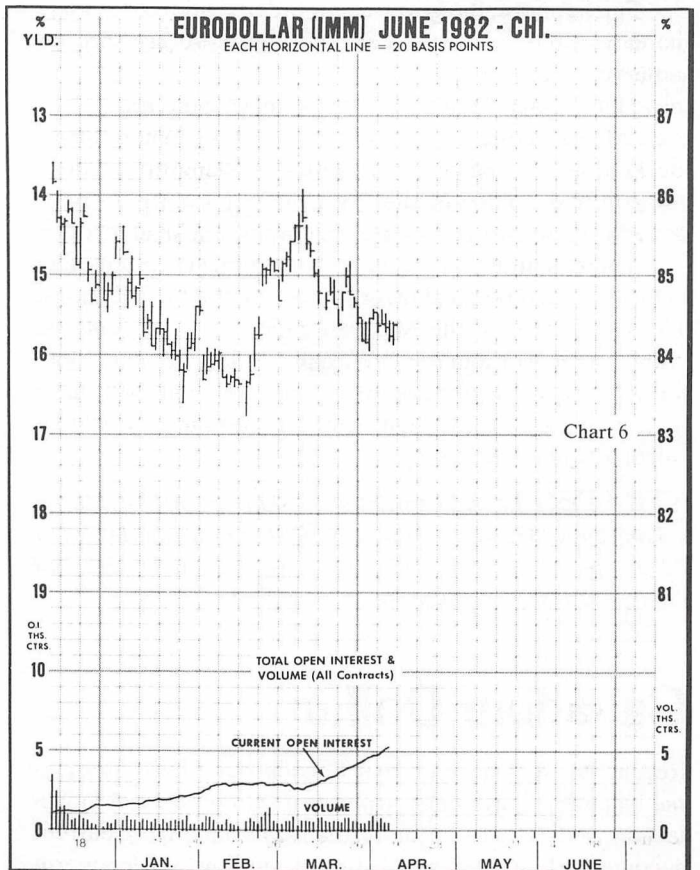
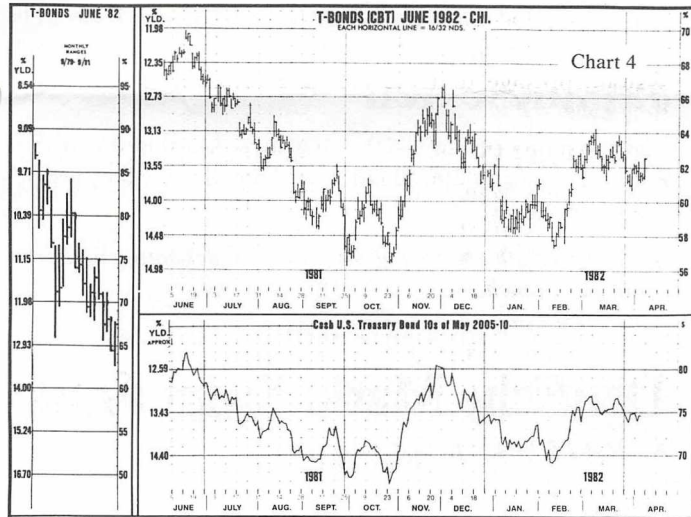
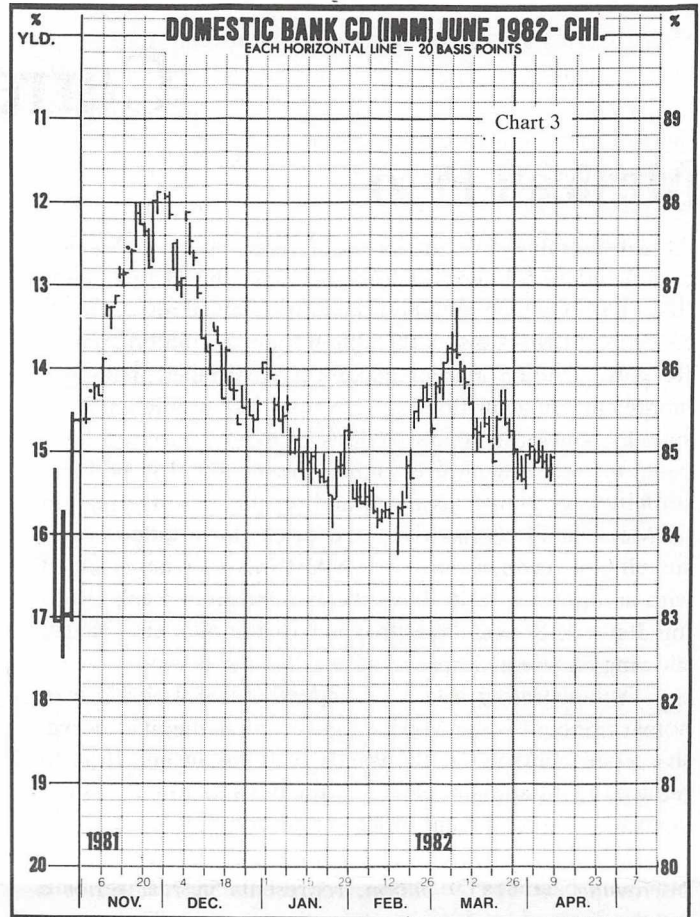
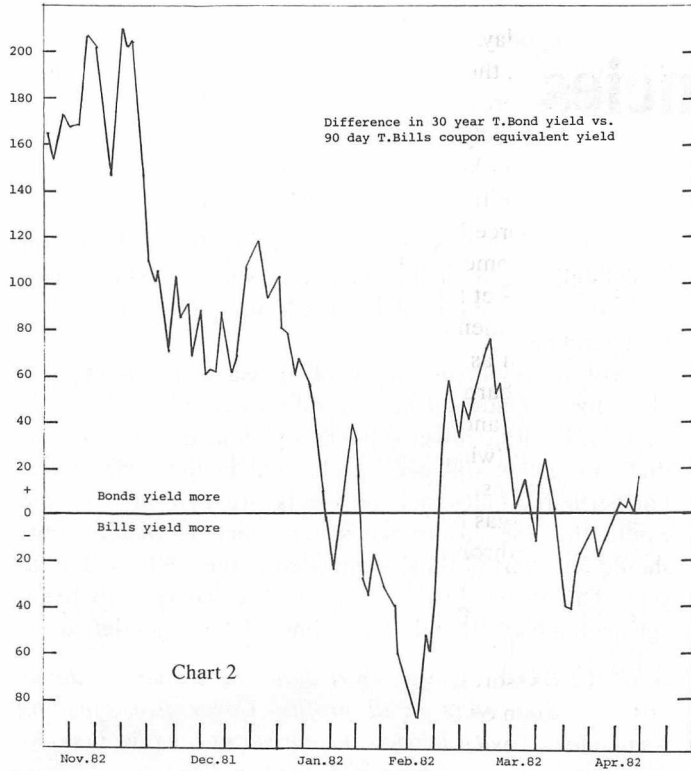
Remain short Eurodollars, Certificates of Deposit, T-bills and T-bonds, in that order of preference, with stops at 86.07, 86.72, 88.33 and 64 9/32, all basis June '82, close only.

Funds Raised in Credit Market

Chart 1

	1974	1975	Year-over-year Change		Annualized 1979 IV Qtr.	1981	Net Change	
	bil.\$	bil.\$	bil.\$	%	bil. \$	bil.\$	bil.\$	%
Total	230.8	221.5	- 9.3	- 4.03%	448.3	479.9	+31.6	+ 7.05%
U.S. Government Securities & State + Local Obligations	48.4	111.0	+62.6	+129.34	138.7	155.9	+17.2	+12.4
Corporate & Foreign Bonds	24.9	36.7	+11.8	+47.39	26.9	29.4	+2.5	+ 9.29
Mortgages	60.5	57.2	- 3.3	- 5.46	152.3	96.5	-55.8	-36.64
Consumer Credit, Bank Loans N.E.C., Open-Market paper & Other Loans	91.4	6.0	-85.4	-93.44	124.8	196.2	+71.4	+57.21

Source: Flow of Funds Accounts



Currencies

Mexican Peso

At considerable cost (in terms of rising spreads) Mexico completed \$3.8 billion of foreign borrowing in this year's first quarter, which included the controversial and difficult \$2 billion PEMEX and \$400 million Banrural jumbo credits. Recently, leading market makers have stopped making a market in Mexican floating rate note issues (FRNs). Reasons are obvious: (a) projections of export earnings have been revised downwards rather drastically; (b) political stability is no longer assured; and (c) the effective margin on Mexican FRNs has risen and prices have fallen correspondingly. As an example, the NAFINSA 1986 notes issued with a ¼ point spread above the London Inter-Bank Offering Rate (LIBOR), have dropped to the 97½-97¾ range, showing an effective spread of nearly 1 per cent.

Demonstrating a lack of understanding of basic economic principles, the Mexican government slapped pervasive price controls on thousands of items in an effort to reduce the inflationary effects of the devaluation. It has not occurred to government officials that inflation is beneficial to Mexico's balance of payments, as it "absorbs" excess monetary balances (i.e., reduces real balances), thus blunting the demand for foreign exchange.

Furthermore, the government ordered additional wage increases of 10 to 30 per cent, putting more pressure on industry's profit margins. In a move specially designed to move public finances and deficits well beyond present levels, the authorities offered to absorb up to 42 per cent of losses incurred by companies in currency exchange operations and will allow many of the firms the opportunity to postpone for up to two years taxes on corporate global income.

There is little doubt that the government is attempting to buy time and political favor just before the July elections. The true extent of the Mexican catastrophe will only be visible to the world in the latter half of 1982, by which time foreign credits will have dried up, inflation will have reached close to triple digit numbers, and the peso will be worth less than one penny.

STRATEGY: Add to deferred short positions (March '83 and June '83) with enthusiasm. Risk is minimal (less than \$2,000 per contract), while rewards are still substantial (\$6,000-\$7,000 per contract).

Canadian Dollar

Recent statistics indicate that Canada ran a fairly substantial balance of payments surplus in 1981 (net official monetary movement was up more than C\$2 billion). A current account deficit and a substantial outflow of long-term

capital were offset by an even more significant short-term capital inflow, attracted by high domestic interest rates and profitable conversion of US funds for purposes of local bank lending.

For the moment, the Bank of Canada continues to allow for a significant interest rate differential in favor of Canada, ignoring adverse public opinion. It would appear that this policy will not be changed in the near future. Furthermore, budgetary prospects are favorable to the extent that the government's net financing requirements should fall short of those demanded in the 1981/1982 fiscal year. This development should be viewed constructively against the background of a widening US budget deficit.

STRATEGY: Cover short June '82 Canadian dollar positions, accepting small profits. Cover five June '82 Canadian T-bonds, leaving the spread at long 30 June '82 US T-bonds/short 36 June '82 Canadian T-bonds.

Japanese Yen

The proximity of the Y250/dollar level has reinforced the Bank of Japan's determination to halt the decline, lest it turns into a rout.

STRATEGY: Cover short positions, accepting a \$1,500 profit per contract.

Deutsche Mark, Swiss Franc

STRATEGY: Remain sidelined.

British Pound

The Falkland Island affair is threatening to upset rather seriously the Exchequer's borrowing requirements for 1982/1983, with undesirable side effects on inflation. Nevertheless, anticipating a peaceful end to the conflict, Sterling has held remarkably steady at the DM 4.25 level.

STRATEGY: For basic reasons, related to Sterling's overvaluation (basis the effective real rate of exchange), we remain of the opinion that the pound is the best vehicle for participating in the continued strength of the US dollar. A military outcome to the Falkland Islands conflict would obviously reinforce our bearishness, while a peaceful settlement may offer us a chance to add to our short positions at slightly above 1.80.

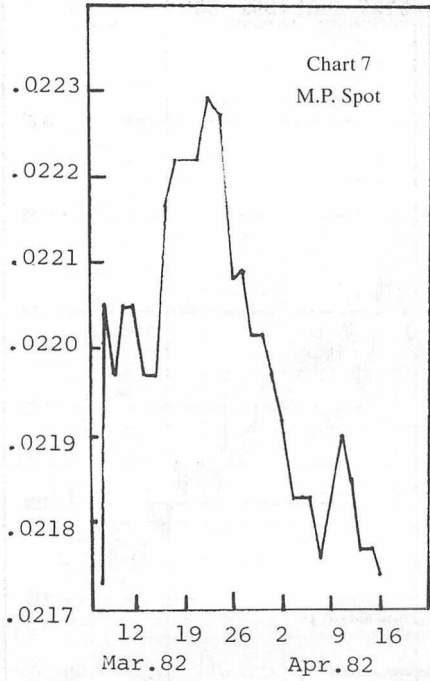


Chart 8
Mexican Peso

Forward Discount Annual Basis %	Jun.82	Sep.82	Dec.82	Mar.83	Jun.83
Spot	48.02	42.39	35.81	33.82	31.31
Jun.82		41.60	34.50	33.33	31.0
Sep.82			30.58	32.59	30.65
Dec.82				37.46	33.23
Mar.83					32.00

INTEREST ARBITRAGE: 3-MONTH FUNDS
DIFFERENTIAL: PLUS(+), INDICATES FAVOR DOLLAR ASSETS
AVERAGES FOR WEEK ENDING WEDNESDAY

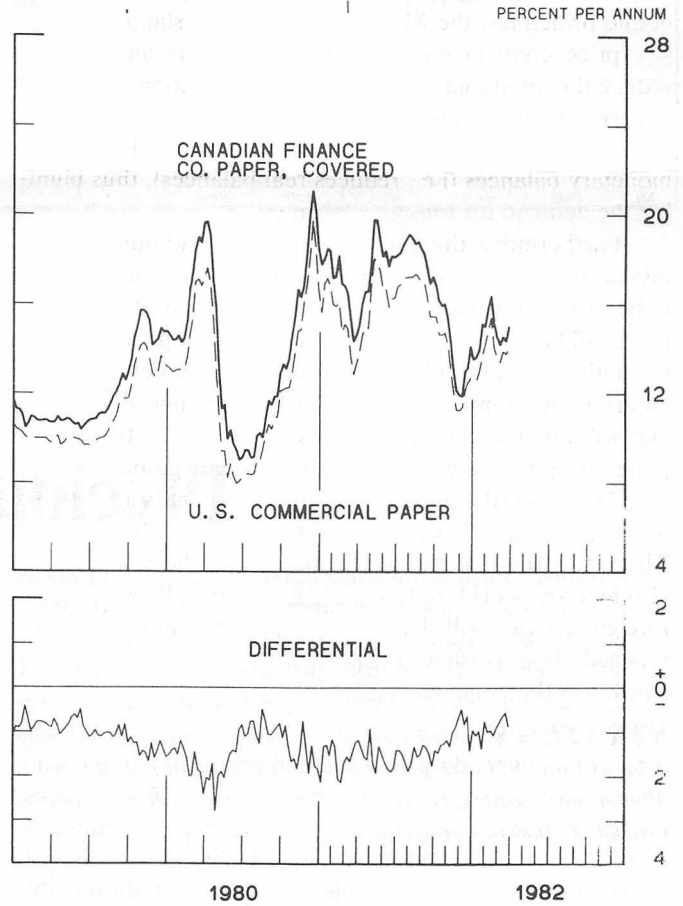
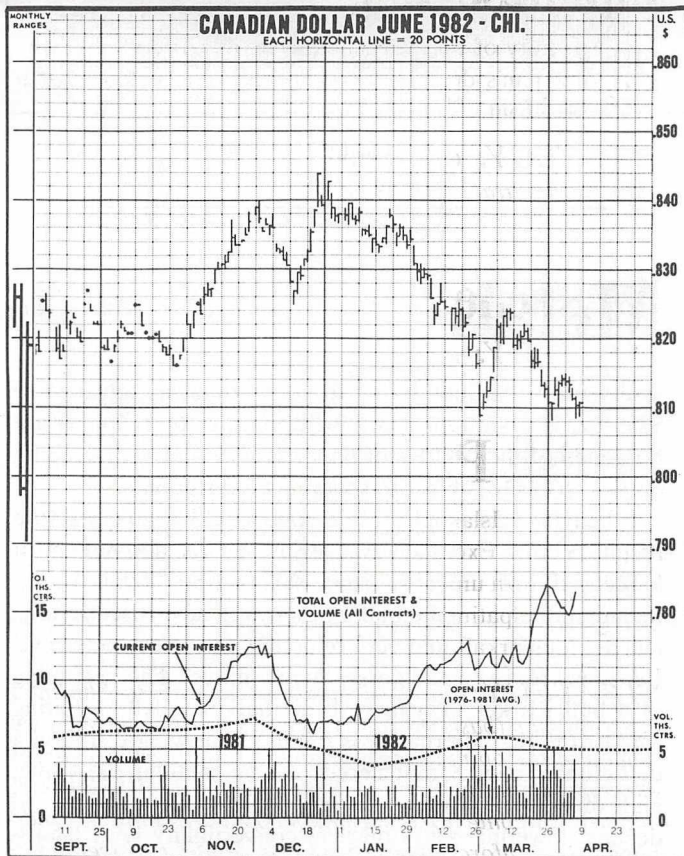


Chart 10

Chart 9

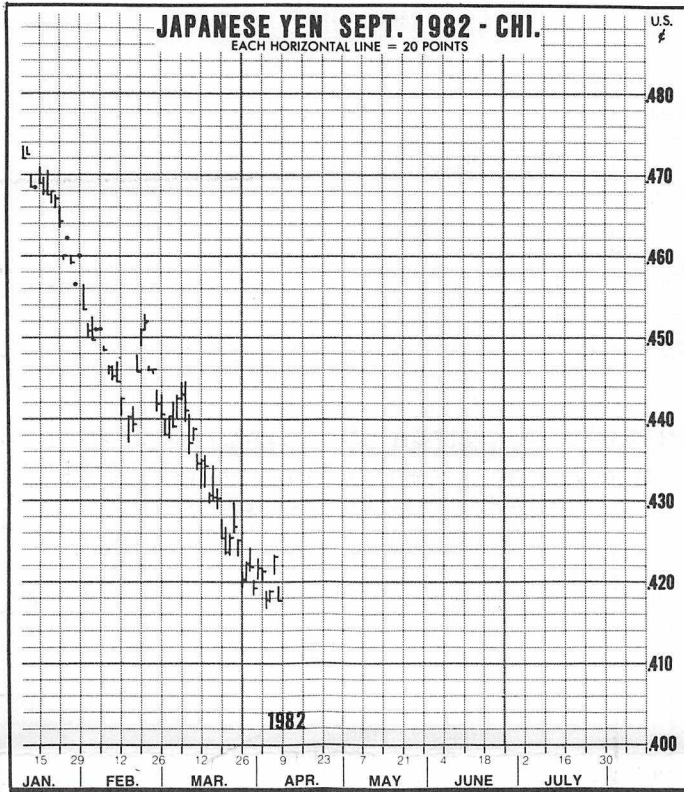


Chart 11

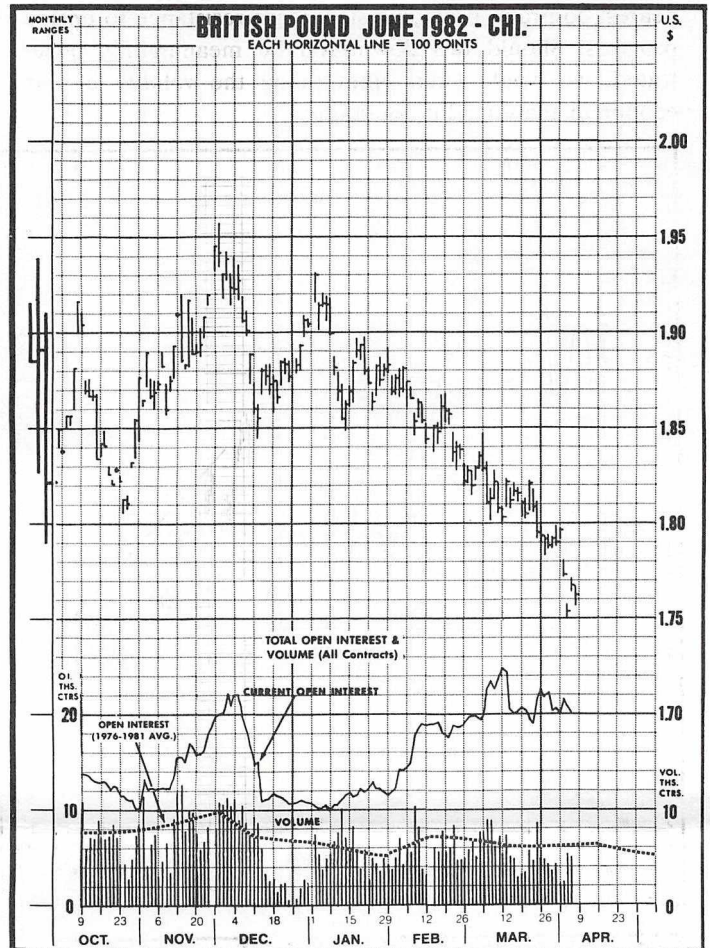


Chart 12

Precious Metals

To everyone's surprise (at least, ours) gold erupted upwards from a classical pennant formation bound by the contract lows of 319, basis June '82, recorded in early March and the recovery high of 342, recorded just 10 days later (see Chart 14). Unquestionably, the market (as well as the CIA, British Intelligence and the local Argentinian peso market) was aware of an impending international crisis, for it stubbornly held above life-of-contract lows for over three weeks, despite extraordinary bearishness evidenced by analysts, newsletter writers and members of the public (bullish consensus figures dipped below 20 per cent during this period).

Significantly, the market's major move (and the gap breakout from the pennant) took place the Monday following the Argentinian invasion, perhaps a delayed reaction but most probably a direct result of the British freeze of Argentinian assets held in London. The last such "money grab" took place in late 1979 when the US froze Iranian

assets and subsequently led to gold's runaway advance to \$850/oz. Not without some logic, market participants are reminded of the frailties of paper money and bookkeeping entries so easily subject to sovereign interference.

Leaving philosophy aside, one could argue that the recent \$55/oz. advance was every bit as dizzying as it looked, if only because most sellers (the Soviet Union included) had done the bulk of their well advertised selling, and anxious bids found very reluctant and sparse offerings. But how are we to categorize such a move? The beginning of a bull market or a mere bear market rally? Militating against the first alternative is the fact that we are still on a deflationary course, that a credit crunch is still in the offing, and that US external short-term liabilities continue to decline, lowering gold's magical convertibility level (short-term assets minus short-term liabilities divided by the 11 million ounces sitting in Fort Knox).

Furthermore, a powerful year-long downtrend (see

Chart 13) intersects at about \$375/oz., basis New York's nearest contract, providing significant resistance to upside progress. Should this downtrend be meaningfully penetrated, we would begin questioning the validity of our economic analysis. But not before.

STRATEGY: Stopped out profitably of our July '82 silver short positions, at 7.75, as per last month's advice. Sell June '82 COMEX gold, risking closes above 381, close only.

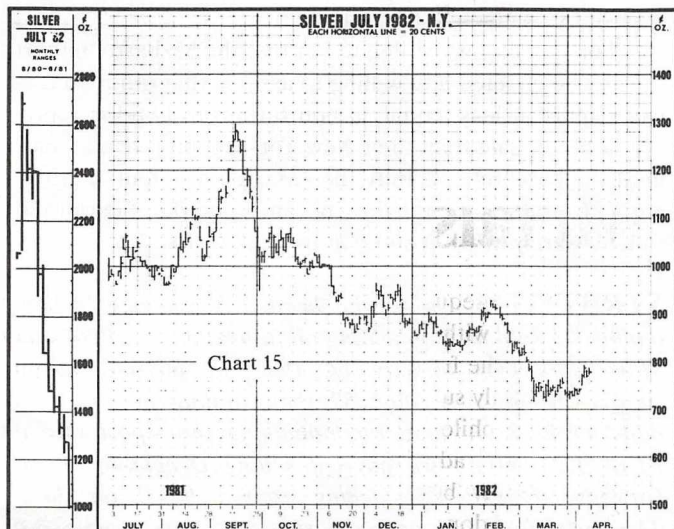
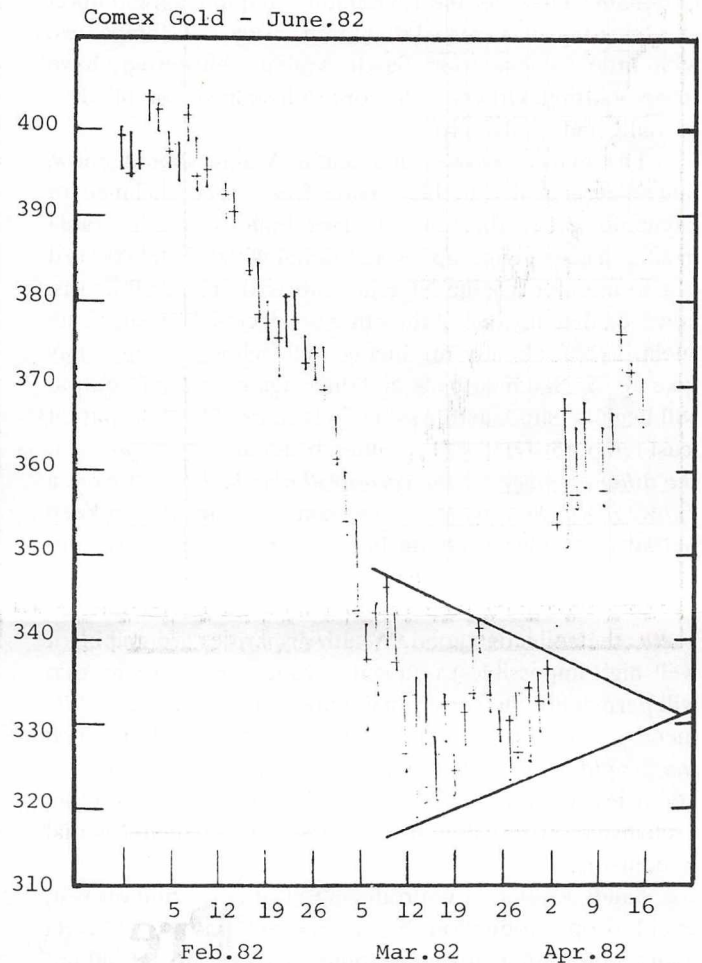
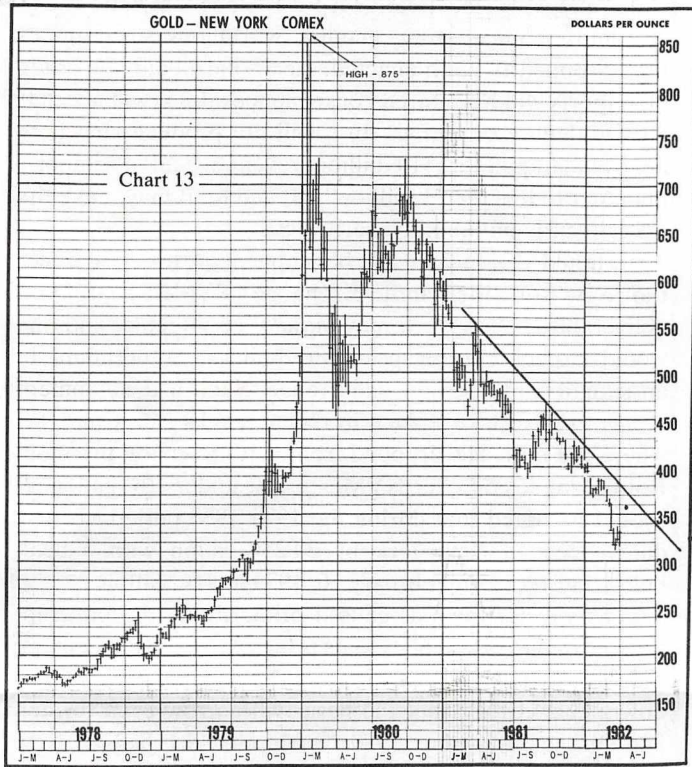


Chart 14

Heating Oil

The mortally wounded bull takes a final run at the matador in the mistaken notion that avenging itself will save its life. The matador knows better, and rather than stand in its way, he bides his time — patience will reward him. The OPEC

cartel is the mortally wounded bull; the wounds — conservation and substitution — are not imaginary, for they will surely kill it; the final charge is the threat of blacklisting those oil companies that stop lifting Nigeria's oil; the

matador is the market.

The market does not stand in the way of the bull. Oil companies have resumed lifting Nigeria's oil, whose production has risen to 950,000 barrels per day (b/d) after a dramatic slump to about 630,000 b/d at the end of March. The market's patience and determination will erode the attacker; even after the threat, Nigeria's output is expected to remain well under the 1.3 million b/d quota agreed upon at a meeting in Vienna last month. Some oil companies, with little to lose from Saudi Arabia's blustering, have stopped lifting. Others with more to lose have complied — partially and grudgingly.

The market knows, and Saudi Arabia should know, that Nigeria will crumble. Aside from *direct* balance of payments aid to the tune of many billions, Saudi Arabia must consider giving up an additional 400,000-500,000 b/d just to attempt to plug Nigeria's shortfall. The problem is, however, that any one of the other producers, Kuwait, Venezuela, Lybia, already producing well below capacity, may take up the Saudi cutback and once again, Nigeria's output will begin to slip. Saudi Arabia, in fact, *could* cut output (at least temporarily) to 4 to 5 million b/d, *but it is not sure that the other members of the cartel will play ball*. Saudi Arabia *knows it will be double-crossed*, and so it decides to keep output at around 7 million b/d, an amount that is sure to send prices spiralling down in the very near term.

The cartel now faces the eternal problem: self interest versus the collective good. Wealth disparities are making it well nigh impossible to allocate production in a way that will perpetuate the cartel's fixed price. Ten of the 13 OPEC members are already producing *below the level at which they could balance their current account*. Four of these 10 countries are on the edge of losing their entire foreign exchange reserves within three months (among them Nigeria, of course).

Saudi Arabia, now producing at about 7 million b/d, could drop production below 6.4 million b/d, a level compatible with a current account balance, but it could not be assured that the 10 "poor" members, or even the four desperate members of OPEC, would not cheat on their production quotas. Sheik Yamani knows that it is better to produce and sell 7 million b/d at \$20/barrel than 5 million b/d at \$20/barrel, given that he knows that the 2 million b/d will, in any event, be forthcoming from other sources. This simple arithmetic exercise is reason enough to dismiss the rumor circulating in London last week that the Saudis were contemplating a cutback to 4.5 million b/d because "they could afford it." They may be able to afford it, but they are no fools.

An extremely bearish development for the oil market is

the possible imposition of a \$5/barrel duty on US imports of crude oil. Veteran commodity observers point to the depressive effects on the world market observed after an increase in the import duty of sugar into mainland USA. In the most recent example, US import fees for raw sugar were raised almost 1¢/lb. effective April 1. Since that date, and in an almost compensating manner, world raw sugar prices have dropped 1¢/lb. If enacted, the \$5/barrel duty on crude oil imports will have three consequences: (a) it will accelerate the demise of OPEC; (b) it will not produce anywhere near the hoped-for \$10 billion revenue gain as imports plummet to less than 1 million b/d; and (c) it may make the US self-sufficient in oil by early 1983.

Should the import fee be slapped on product prices too, New York Mercantile Exchange (NYME) heating oil deliverable in New York may *initially* be affected, and one would expect current prices to build in a premium in anticipation of such an occurrence. Such a development seems to have taken place in recent weeks (see Chart 17) where the basis has dropped from a 16.7¢/gallon premium Rotterdam gas-oil over NYME to just under 10¢/gallon. It should be noted that during the 1979/1980 period, Rotterdam exceeded New York by 20-25¢/gallon with a peak being registered on February 16, 1979 at 41¢/gallon.

This distortion was caused primarily by the interruption of Iranian oil supplies to its principal European centers, notably West Germany. Should the Iran-Iraq war wind down, chances are that the basis will narrow even further. During the December 1980 to March 1981 period, New York heating oil futures *exceeded* the Rotterdam spot market by as much as 8¢/gallon.

For speculators willing to bet that the \$5/barrel import fee will be enacted and willing to assume that other factors will remain at least equal, gas-oil futures in London represent a better sale than their New York counterpart, at least until the basis reflects fully the 12¢/gallon potential differential, from the time the duty became a market factor (mid to late March, when it stood at its peak of 16.7¢/gallon).

STRATEGY: *Those who heeded our advice in September '81 sold nearby heating oil futures between 96¢ and \$1.03/gallon. On January 17, 1982, we advised partial shortcovering, with May '82 then trading at 90.63. In mid-March we covered the remaining short positions at 70.41. Last month we advised selling December '82 at between 82¢ and 85¢, placing stops at 90.00, on close. These stops were triggered last week. Nevertheless, we continue to believe that December '82 heating oil will trade at 62¢ or less and strongly suggest reentering short side at present levels, placing new stops at 95.00, close only.*

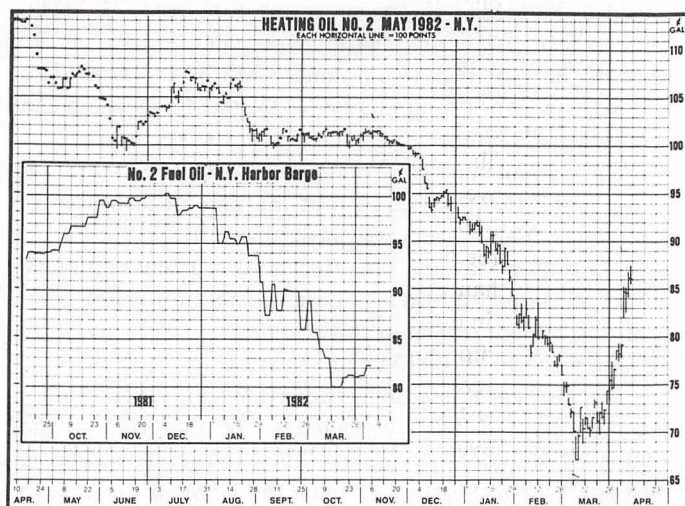
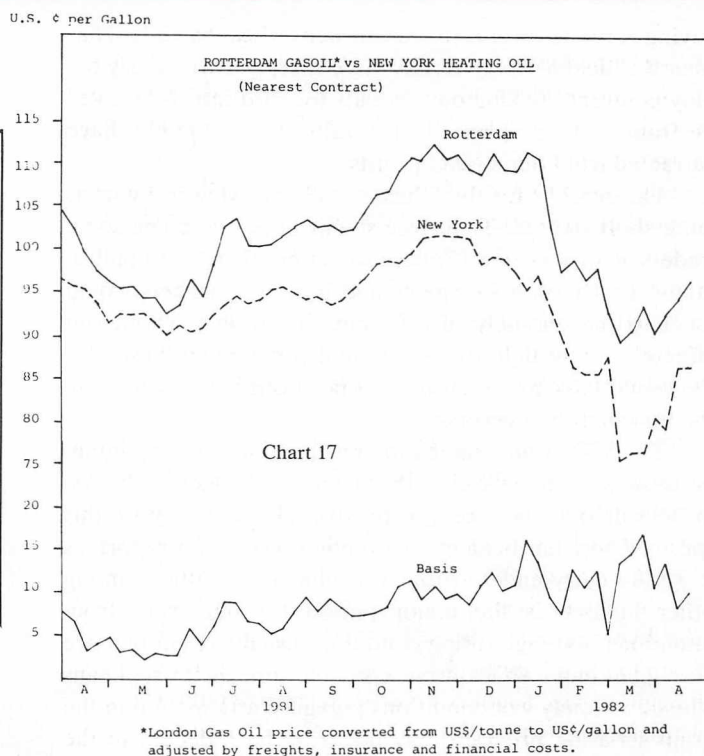


Chart 16



*London Gas Oil price converted from US\$/tonne to US¢/gallon and adjusted by freights, insurance and financial costs.

Grains

Participation in the acreage set-aside programs in the US has been much higher than initially expected, reflecting depressed grain prices. Expectations of participation when the programs were announced were as follows: wheat (announced January) 37 per cent; feedgrains (including corn, soybean, oats and barley; announced February) about 30 per cent. As of April 9, the USDA reported that participation in the set-aside program was 62.8 per cent of the base acreage for wheat and about 52 per cent of the base acreage for feedgrains. The sign-up period ends April 16.

With a 15 per cent acreage set-aside for wheat, a 65 per cent participation rate would reduce overall wheat acreage in the US by about 9 per cent. Similarly, with a 10 per cent acreage set-aside for feedgrains (of which corn comprises over 70 per cent) a 55 per cent participation rate would result in overall feedgrain acreage being reduced by approximately 5.5 per cent.

The final tally of acreage removed from sowing to wheat and corn thus becomes a significant factor in our grain trading strategy. Only farmers participating in the acreage reduction program are eligible for price support loans and target price protection, with wheat and feedgrain farmers also eligible for the farmer-owned reserve.

Chart 18 shows the development in the acreage abatement programs for major grain producing states for March 19 and April 7. If one examines the percentage of land base that has been enrolled for eastern and western wheat-

producing states, our projection from last month (that participation would be much higher for western — hard, basis Kansas City — wheat than for eastern — soft, basis Chicago — wheat) is quite evident in the actual results. For example, in the largest eastern wheat producing state by acreage — namely, Illinois — enrollment to April 7 was only 34.13 per cent of land base. However, for Kansas, by far the largest western wheat producing state by area, the participation rate was 60.66 per cent by April 7.

The difference occurs for the reasons outlined last month — a greater sacrifice in returns brought about by higher yielding land in the east compared with the west if farmers participate in the program (which necessitates ploughing-under or grazing of the set-aside land); a higher initial investment in the east than the west, caused by heavier fertilizer application rates; and, less winter-kill damage in the east than the west. Therefore, the direct loss through participation is much greater for easterners than for westerners.

The result? Higher participation rates in the west. This is very important for our long Kansas City/short Chicago wheat spread. Production of hard wheat will be significantly lower in proportion to the 1981 crop than will soft wheat. This will favor our spread between the major wheat markets.

As indicated last month, free stocks of soft wheat are relatively low, even though total (including government-controlled) stocks are very high. This, coupled with recent

buying activities in soft (basis Chicago) wheat by China, has caused Chicago wheat to rally quite sharply, particularly the May contract. Rolling our spreads forward into July saved us from a large part of this rally, which would have detracted from our spread profits.

The reasons for the Chicago rally are viewed by us as quite short-sighted. Tight free stocks have overcome some traders, who also view Chinese wheat purchases as a bullish factor. Last month we speculated how the markets would react to the anomaly of different short-run and long-run effects; namely, tight free stocks and very large total stocks. We would look to establish short positions in soft wheat on the first signs of a reversal.

The USDA announced the results of its planting intentions survey on February 18. Owing to budget cutbacks, there will only be one prospective plantings report this spring. There has been much skepticism over this report, as it was so early and so subject to change. Weather, among other factors, is the major reason for departure from intentions. Average spring conditions usually result in more corn plantings, while farmers switch acreage to soybeans when extremely wet conditions prevail. Participation in the grain set-aside program may not truly be reflected in the estimates, because some farmers received the survey before the set-aside program for feedgrains was announced. Chart 19 shows planting intentions as derived from this survey, including its faults.

When higher-than-expected participation in the acreage reduction programs are combined with planting intentions, wheat should be reduced in acreage quite significantly more than corn (which is shown by planting intentions in Chart 19). However, a rough estimate of 1982 grain acreages as a percentage of 1981 would be wheat 96 per cent and corn 98 per cent.

The amount of corn in the grain reserve as of March 31 totalled 1.13 billion bushels compared with 1.06 billion bushels a month ago. These figures include about 40 million bushels of 1980 crop corn entered into the reserve during the 1981/1982 season. The size of the corn reserve is approaching the 1.25 billion bushel level forecast in February by the USDA. The US has not yet indicated that a 2.0 billion bushel limit on the size of the farmer-owned grain reserve (corn and wheat) may be imposed, but existing legislation enables this.

The USDA *again* changed its forecast of exports of corn in the 1981/1982 (October-September) season. As of April 13, corn exports are forecast at 2,175 million bushels versus a downward revised 2,125 million bushels last month. Accordingly, stocks forecast on September 30, 1982, are adjusted downward from 2,076 to 2,026 million bushels. Domestic use is forecast at 5,035 million bushels, unchanged from last month. Wheat export, stocks, and domestic use levels are unchanged from last month.

The USDA's adjustment in corn export and stocks

forecasts is largely due to continued purchasing by the Soviets. The USSR is expected to import a record 44 million metric tons (MMT) of grain in 1981/1982 (July-June). This includes 24 MMT of coarse grains (up from 23 MMT forecast last month, and nearly 33 per cent larger than the level of the past two years) and 19 MMT of wheat. The USSR has, to April 8, purchased 6,023,300 MT of wheat and 7,751,000 MT of corn from the US in the recording year October-September. This compares with 5.86 MMT of wheat and 7.16 MMT of corn at the time of last month's *Comments*. The Soviets still have almost 1.7 MMT of US grain to ship in May and June to clear up current contracts, including about 1.0 MMT of corn. Soviet imports of grain from the US are expected to be about 1.9 MMT in April, including about 275,000 MT of wheat.

The Soviets appear to have contracts for virtually all of the 44 MMT of grain expected to be imported in the 1981/1982 (July-June) year, according to the USDA. From October 1981 to September 1982, the USSR is forecast to import a record 45 MMT of grain from all sources, of which about 35 MMT are now contracted. If current Soviet purchasing levels continue (3.7:1, corn over wheat, from US sources), corn futures will tend to advance relative to wheat futures. In fact, we are looking for a 15¢ to 20¢ rally in new crop (December 1982) corn futures.

Recent estimates of Soviet grain production in 1981 have been made by officials within the Soviet Union at from 140 to 160 MMT. This is significantly lower than the USDA's 175 MMT projection, which they continue to adhere to. As a result of this, and rumors of problems with the 1982 grain crop due to planting problems resulting from wet weather, we envisage extremely high imports of grain by the Soviets to continue for the duration of the 1981/1982 season and into the 1982/1983 season.

Farmers often examine deferred futures (upcoming harvest season) as a method of price forecasting. Currently, November soybeans are trading at only a 9.5¢ premium to July (6.66½ November; 6.57 July). As this carrying charge fails to cover the costs storage for soybean and the opportunity costs imputed by interest over this period, farmers would tend to sell stored soybeans now rather than store them until November or later. This would cause nearby soybean futures to fall relative to the deferreds.

STRATEGY: *As our corn/wheat spread failed to break the 80¢ level, it should have been closed out sometime during the last month, during which the price differential rose back to almost 97¢. Close out any existing positions, as Chicago wheat is presently trending against this spread. Maintain long Kansas City/short Chicago wheat spread, and in fact add to positions in July or September. Buy December corn, looking for advances of 15 to 20¢. Spread soybeans, short July/long September or November, looking for the price differential to widen to more normal levels.*

ENROLLMENT IN ACREAGE SET- ASIDE PROGRAMS (major states)

State	Corn/Sorghum land base * acres	% of land base enrolled		Wheat State	land base * (acres)	% of land base enrolled	
		April 7	March 19			April 7	March 19
Illinois	11,423,294	46.61	24.75	Colorado	3,616,812	56.96	28.64
Indiana	6,181,557	38.46	19.86	Illinois	2,001,486	34.13	17.51
Iowa	14,782,163	47.04	24.19	Kansas	13,918,346	60.66	30.51
Kansas	6,047,580	56.45	27.97	Minnesota	3,880,644	47.87	12.77
Michigan	2,739,138	38.27	21.06	Missouri	3,280,167	28.45	15.41
Minnesota	7,072,804	31.24	11.22	Montana	6,248,681	66.22	34.17
Montana	3,510,527	31.16	15.52	Nebraska	3,133,337	58.08	25.41
Nebraska	10,065,182	48.87	23.85	North Dakota	12,529,992	52.27	20.02
North Carolina	2,136,236	10.70	4.45	Oklahoma	7,526,111	48.95	23.19
Ohio	3,492,887	40.37	19.47	South Dakota	4,598,752	57.32	24.62
South Dakota	4,270,877	47.41	19.49	Texas	7,157,074	40.35	14.04
Texas	6,757,732	39.56	10.29	Washington	3,104,041	82.52	67.69
Wisconsin	3,928,963	25.03	11.56				

* Essentially equal to 1981 plantings.

Chart 18

PLANTING INTENTIONS - 1982 ACREAGE OF CROPS (thousand acres)

Chart 19	indicated	planted	1982 as per cent
	1982	1981	of 1981
corn	84,735	84,153	100.7
soybean	69,535	68,000	102.3
all wheat	88,013	88,864	99.0
spring wheat	17,097	17,071	100.2

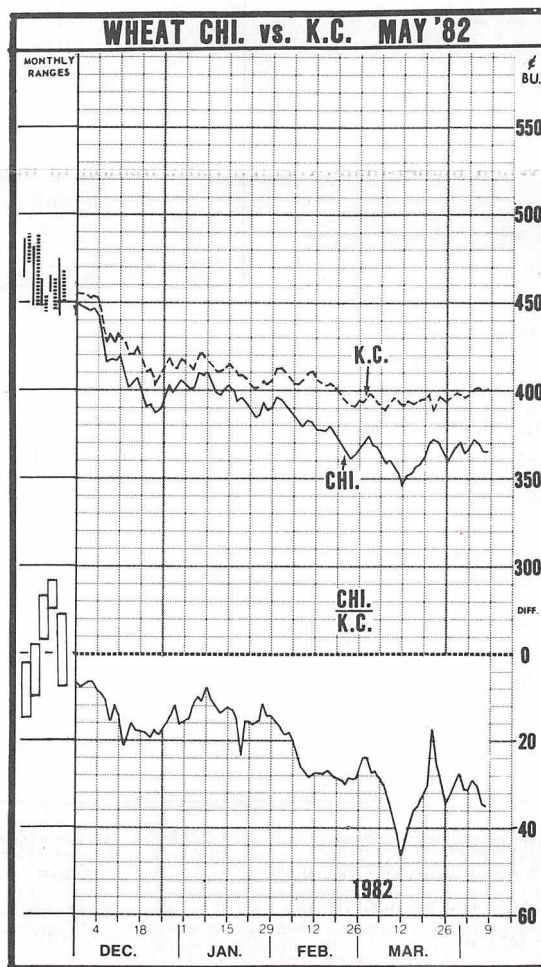


Chart 21

Livestock

Live hog futures have risen virtually non-stop since the late December hogs report by the USDA indicated reduced fallowings in the late fall of 1981 and early 1982, and reduced fallowing intentions in 1982, when these periods are compared with the previous year. At the time of the USDA report, livestock was quite oversold. June, July and August hogs have since advanced from about 42¢ to over 55¢.

Several factors would tend to sustain this rise. Hog fallowings were reduced sharply during the cold winter month, resulting in a reduced availability of pigs during the summer months, relative to demand.

Secondly, hog prices were relatively low through most of 1981, with the result that breeding stock was cut back.

Current increases in breeding stock tend to offset future marketings in the interim. Fairly high prices at present cause producers to hold back hogs for breeding purposes.

Thirdly, marketing of cattle is at a low level at present, resulting in higher cattle prices. Demand for pork as a substitute particularly as beef rises above \$1.00 to \$1.10 per pound on a carcass weight basis, increases substantially.

Such conditions are leading to greater demand for pork this season relative to last year. We expect that the current bull market in hogs will continue for some time.

STRATEGY: Buy June, July, or August live hog futures. Place stops at 53.5 cents for all months, with an initial target price of 61¢.



Chart 22

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