FRIEDBERG'S

COMMODITY & CURRENCY COMMENTS

FRIED-BERG

Friedberg Commodity Management Inc. Volume 6, No. 3 March 24, 1985

Gold: A time to buy

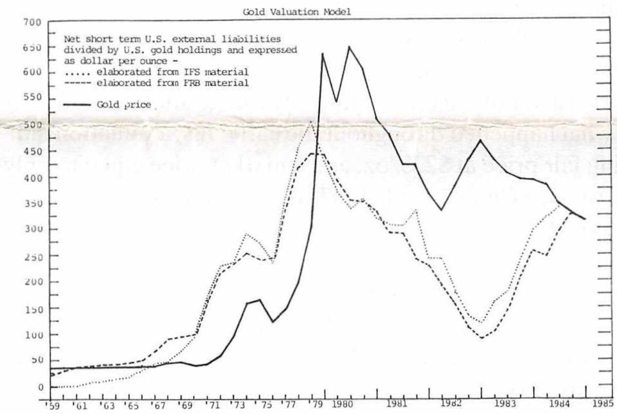
That was the title of our *Comments* on November 4, 1976. The dollar had once again begun to weaken, the IMF gold auctions were a reality, and as the world economy took hold, prospects for future inflation loomed ominously over the Western world. Our single most important cue was technical: The long-term downtrend line connecting the December '74 highs to the subsequent rally tops was decisively broken in October as spot gold advanced through the $118-$120/oz. barrier. In our *Comments*, we wrote: "Needless to say, the significance of the upside breakout, in the face of continuing pessimism is enormous." In the background of those fateful months, leading economic publications such as the London *Economist* and Citibank's *Economic Week* were discussing gold's dim prospects and the possibility that it could sink to as low as $60/oz. Wryly we commented that "such deep pessimism, in retrospect, is the forerunner of bull markets."

Coming back to March 1985, we find that on the very morning gold leaped $10/oz. higher (March 18), the *Wall Street Journal*, in its "Outlook" column, reported that inflationary expectations are dying, even among the participants at the Committee for Monetary Research and Education annual conference. What is even more startling is how much sentiment on precious metals had soured, even among those hard-money advocates. In a telephone interview (he was not able to attend the conference), Dr. Hans Senholz, economics professor at Grove City College in Pennsylvania (well-known for his Austrian views on money and inflation), informed the WSJ reporter that he did anticipate some acceleration of inflation from the recent annual pace of 4%, but that he no longer expected torrid inflation.

Prodded to express his views on gold and silver, he reported that "I've been selling it short, and silver too." This deliciously ironic statement was made 48 hours before gold and silver advanced a stunning 16%, the largest two-day gain in nearly three years — and a sign that gold had no friends left.

Can March 1985 be compared with November 1976? Not exactly. Unknown to us at the time, our monetary gauge for gold indicated that in the fall of 1976, bullion was deeply undervalued, possibly by as much as $110/oz. (see Chart 1). The computation assumes the US to be the "world's banker": On the liability side, we find central bank international reserves denominated in US dollars and nonresident US-dollar deposits with the US banking system; on the asset side, gold, SDRs, and foreign exchange holdings of the Treasury.

Chart 1



Since a sound banker's short-term assets and liabilities are matched, we ask: What value should we put on gold to equalize the equation? It is this value that we have tracked since 1959 and found highly reliable as a predictor of market values. Notice how starting in 1967, as a result of mounting payments deficits, the implicit value of gold rises far ahead of its market (official) price of $35/oz. The undervaluation persists right up to late 1979/early 1980 when euphoria overtakes the yellow metal, and it skyrockets well past its equilibrium value. In retrospect, the 1974-76 decline was a mere correction in an ongoing bull market.

In this issue

A weaker US dollar coming up — and how to play it. We remain bearish on stock indexes — and short. Whither crude oil? We're puzzled — and sidelined. Contributions by Albert D. Friedberg and Daniel A. Gordon.

Not so the 1980-85 episode. Gold's implicit value, based on this banking concept, led the way down. At times, the "over-valuation" was as much as $300/oz. (Fourth quarter of 1980, first quarter of 1983); at other times, the "overvaluation" narrowed to about $90/oz. (Fourth quarter of 1981). Nevertheless, and unlike 1974-76, gold was continuously overvalued during the past five years, proving to be, as a result, an extremely poor investment.

In late 1984, a bullish crossover took place. The widening US current account deficit, financed primarily by private borrowings (as well as a sharp reduction of net US claims on foreigners), began to swell the liability side of our world banker. From January 1983 to November 1984 (the last month for which we have statistics), net short-term external liabilities shot up $57 billion, with preliminary figures showing an $11 billion jump for November alone! If these figures are current, *they reflect an alarming situation: the US current account deficit is now being financed solely via indebtedness*, as opposed to a substantial mix of debt and equity inflows in the earlier period. Simple extrapolation of present current account trends yield a minimum $150 billion increase in net short-term external liabilities for the coming year, which, in turn, yields an incredible $900/oz. equilibrium value for gold by the end of 1985!

We rubbed our eyes. Is it not possible, we asked, that market prices will lag equilibrium prices by many months (years?) and remain undervalued by a large amount? Was this not what happened throughout the early '70s, a valuation indicating fair price at $225/oz. and a market price equal to only $60/oz. (see Chart 1, end of 1972)? Yes, it is possible. Is it also not possible that the US current account deficit narrows or disappears in the next 12 months? Possible (anything is), but highly improbable. Finally, is it not possible that the necessary capital inflows come in the way of equity rather than debt? Again possible, but highly unlikely, as business and speculative profit opportunities in the US diminish relative to Western Europe and the rest of the world.

Combining a large discount with a slightly narrower current account deficit (the result of a US recession?) and 80/20 debt/equity mix in the capital inflows, produces a possible market price of close to $500/oz. The odds are stacked dramatically in favor of the bulls, or so it seems.

What about the downside? In the framework of our valuation model, there is little room at this time for downside risk, although, admittedly, the possibility of a long delay before the market perceives the new bullish situation is ever present. Nevertheless, one should hardly care about timing (at least when speaking about a one- to three-year horizon) when promised a potential move to $900/oz. or even $500/oz. — particularly, given the leverage of the futures markets.

There is, however, one disquieting possibility: that is that our valuation model is a figment of the imagination and any resemblance to real life is merely coincidental, as Twentieth Century Fox would put it. We are then left with an unsupported argument for gold at these levels: Inflation is relatively low; commodity prices have been in a free fall for nearly nine months; the Fed has learned the game of bailing out an insolvent financial institution without creating inflation; the LDC debt situation is still admittedly serious, although it is dormant, for now. Then why buy gold? Because the US dollar is, at least, in a major corrective phase (see Currency section), and its weakness should aid gold prices. Gold is then a currency play with a long-term shot at the moon.

STRATEGY: *Last month's April '85 Comex gold and July '85 silver buy recommendations were subsequently stopped out at 296.50 and 609.80 respectively with only minor losses. Fortunately, we renewed the advice to purchase gold and silver on Friday, March 15, after the close (see Hotline Update), allowing listeners to catch the full jump on March 18 and 19. We stay long: The odds have shifted* significantly *to the bull side. Raise stops to 301 and 6.10 respectively, basis June '85 Comex gold and July '85 Comex silver, close only. Please note that we* do *have a strong preference for gold over silver.*

Chart 2

Gold

(In Swiss franc terms)

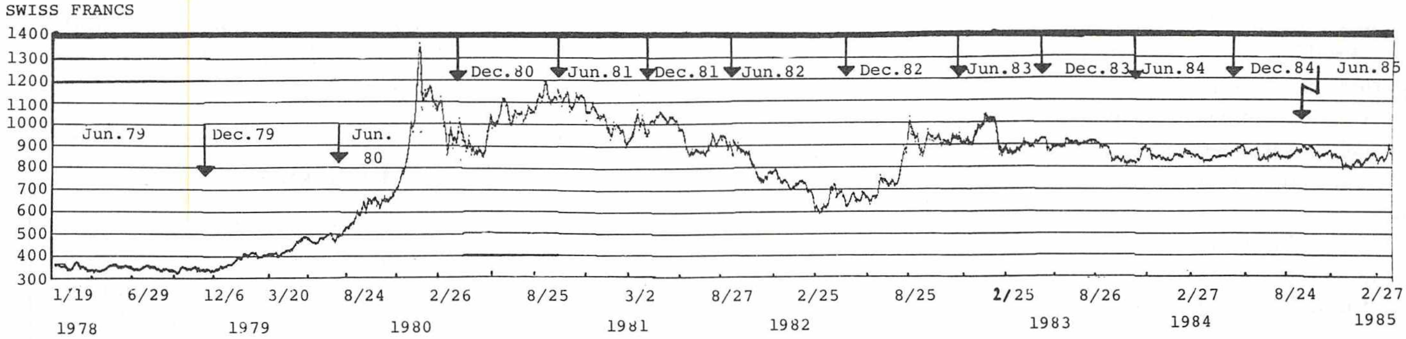


Chart 3

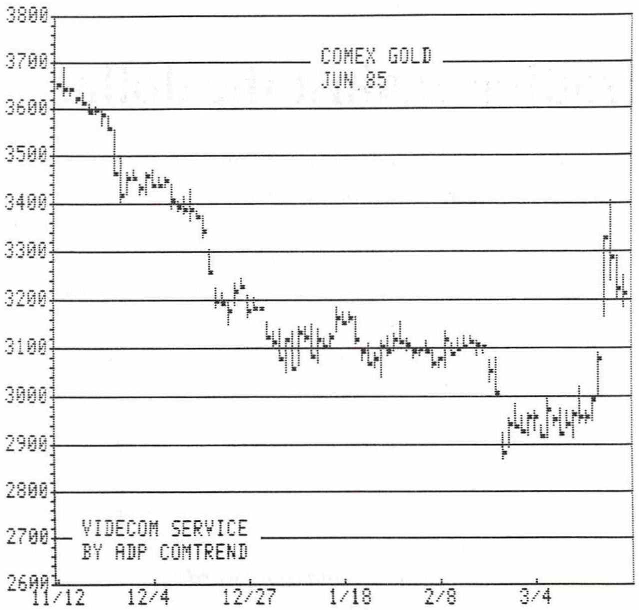
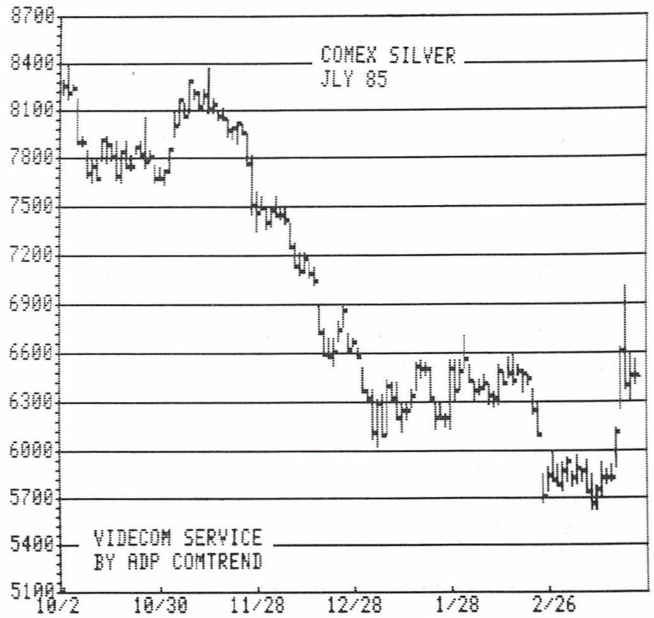


Chart 4



Currencies

The US Dollar

The only thing that has driven more men mad than love is the currency question

—Benjamin Disraeli

It had to be. We warned last month that the stage was set for a strong bout of concerted intervention that would reverse the dollar's bandwagon effect. Little did the unsuspecting bulls realize the extent of the intervention: probably as much as $11 billion, it is now believed. What is more, the bull arguments were getting stale — so presumably the (near) efficient market had been able to (finally) discount it. Finally, there was no one left to buy dollars, as (nearly) everyone was long.

Interestingly enough, as the correction unfolded, the bullish sentiment continued to prevail, unlike the famous correction in early 1984, which saw traders, economists, and government officials join the dollar-is-dead chorus. As always, the market managed to trap the biggest possible number of latecomers. A survey of multinationals conducted by the Bank of America revealed that 70% of those polled expected the dollar to set new highs *over the next three months:* The survey was conducted Tuesday March 12, *following* several days of aggressive speculative dollar selling, during which the dollar plummeted almost 14 pfennigs against the Deutschemark! Only 20% of the 30% bearish contingent (6% of the total!) expected the dollar to trade below 3.20 DM, and clearly, that's where it is heading.

The coming interlude may turn out to be a *mirror image* of the 1973-75 period. The DM spiked upward in mid-1973, climaxing a nearly five-year rise against the US dollar, and then fell back rather sharply, so that by early 1974, it had fallen somewhere between 20% and 25%. For those too young to remember the "setting" in which this spike occurred, we allowed ourselves to quote rather freely from Charles A. Coombs' *The Arena of International Finance:* "... shortly after the turn of the year (1973) ... a series of troublesome events suddenly snowballed into a new crisis of confidence that left the Smithsonian Agreement (The US devaluation of December 18, 1971) in ruins ... The Swiss franc immediately came under speculative buying pressure ... the Swiss authorities decided to allow the franc to float temporarily ... Speculation then spread to other currencies, including the mark ... The Bundesbank was swamped the following week by hot money inflows approaching $6 billion ... Meanwhile no defensive policy action by the Nixon administration was forthcoming ....

"At that Sunday afternoon meeting of the badly shaken central bank governors, I felt as never before the tragic and unnecessary depreciation of the dollar ... But there were still further depths to be plumbed ... within a week, the dollar had fallen to its new floor against the mark, the French franc, the guilder, and the Belgian franc ... On Thursday, March 1, 1973, a new flight from the dollar forced the Continental central banks to take in more than $3.6 billion in maintaining the ceiling rates on their currencies. That night, they announced that their exchange markets would remain closed until further notice . . . Emergency meetings of the European Economic Committee and the G-10 finance ministry were convened."

The decision was to float upward as a bloc against the dollar. Later that month in Paris, the G-10 finance ministers, including Secretary Schultz, reiterated "their determination to ensure jointly an orderly exchange-rate system. The ministers agreed in principle that official intervention in the exchange markets might be useful at appropriate times to help maintain orderly conditions . . . the markets were officially reopened March 19, 1973 . . . But by mid-May a new speculative attack on the dollar had erupted . . . In the frenzy that now gripped the market, a moderate-sized offer that in normal conditions could have been handled without any discernible rate movement was now passed like a hot potato from one dealer to the next . . . By early July 1973, the dollar was plunging each day by 2 percent or more against the European currencies . . . .

"As these speculative pressures reached a climax on July 6, the German mark had been bid up by some 30 percent above the central rate established in February . . . . At a meeting of the BIS group of central banks in Basel on the following weekend, I completed earlier negotiations providing for major increases in the Federal Reserve swap lines . . . . On Sunday night, July 8, 1973, the governors issued a statement noting that all the necessary technical arrangements had been made for official intervention to maintain orderly markets . . . .

"The stage was now set for a dollar bear squeeze that might have restored some degree of market faith in the ability of central banks to maintain orderly markets. The market in fact seemed to be anticipating such a squeeze. By the following Tuesday afternoon, when the Federal Reserve announced an increase in the swap network from $11.7 billion to nearly $18 billion, a strong recovery of the dollar was under way." Then came the late 1973 oil crisis, which initially favored the dollar, as it was thought that the US could more readily cope with supply restrictions. "Suddenly the dollar was in strong demand . . . Sharply rising dollar exchange rates were accelerated by large-scale unwinding of long-standing speculative positions in foreign currencies. By mid-January 1974, the German mark and the Swiss franc had fallen by roughly 23% from the peak levels of July 1973."

There it is. Who says that official intervention is not effective? We repeat, it is highly effective when concerted and in a vulnerable market. In the Coombs account, we could substitute the DM for the US dollar and see repetition of these events today. For a graphic illustration of Coombs account, see Chart 5.

What now? The US dollar is likely to lose further ground, at least until such time as a large percentage of the dollar believers convert. The (slow-approaching) US recession should finally convince the dollar bulls that the dollar has had it. Then, and only then, one might consider moving back into the US dollar.

Trading against the dollar

Commercial hedgers, of course, should see that their long dollar exposure is reduced or eliminated.

As for speculators, there are a number of ways of playing the "weak" dollar scenario. One could adopt a conventional view and go long Swiss francs, DM, and Sterling, staying away from the overvalued yen. Perhaps more intriguing is a long position on other continental currencies such as the Italian lire, Belgian franc, or Danish krone due to the discounts *available on forward positions.*

We particularly like the South African rand because: a) we are bullish on gold, its major export commodity; b) it is extremely cheap on a purchasing-power basis; c) the recent budget was deflationary and likely to bring the current account into a sizable surplus; and d) forward rates are running at a 9% per annum discount, which is another way of saying that rand deposit rates are extremely attractive.

Finally, we believe that both the Australian dollar and the Canadian dollar are attractive short-term speculations and should recover, in weeks ahead, a good portion of their recent decline. Raise stops on long June '85 C$ (see Hotline Update) to 71.50, close only.

Mexican peso

As expected, the daily rate of devaluation was moved from 17 to 21 centavos per day, making our previously established short positions safer.

As the government moves to privatize 236 "nonpriority" state-run companies, details continue to be withheld; cynics believe that there is little substance behind this announcement. As an example, they point out that at least five of the parastate firms listed for sale — all sugar mills — are nonexistent and were created in 1970 as paper companies purely for accounting purpose. Of the "real" companies already listed for sale, little is known about the percentage of the firms to be sold and the economic viability of such firms.

The growing drug problem in Mexico has considerably strained relations with the US which is already alarmed at the number of violent deaths met by US citizens in 1984 (54) and the staggering number of assaults against Americans (1,475).

STRATEGY: *Forwards have widened out considerably in recent weeks; it is now advisable to withhold from further sales. Remain short.*

Chart 5

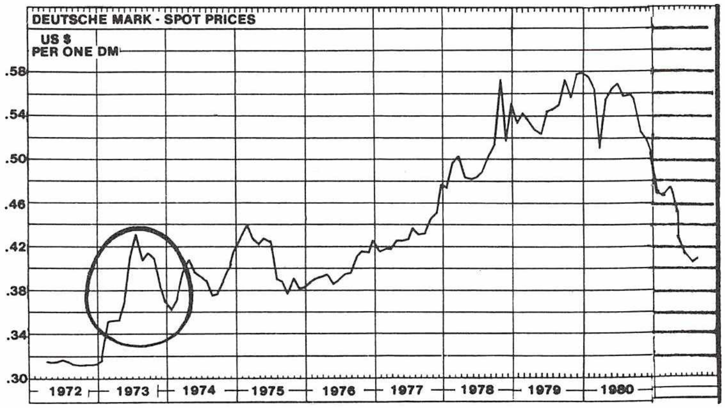


Chart 6

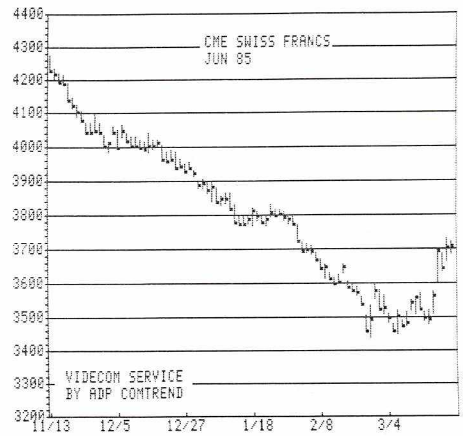


Chart 7

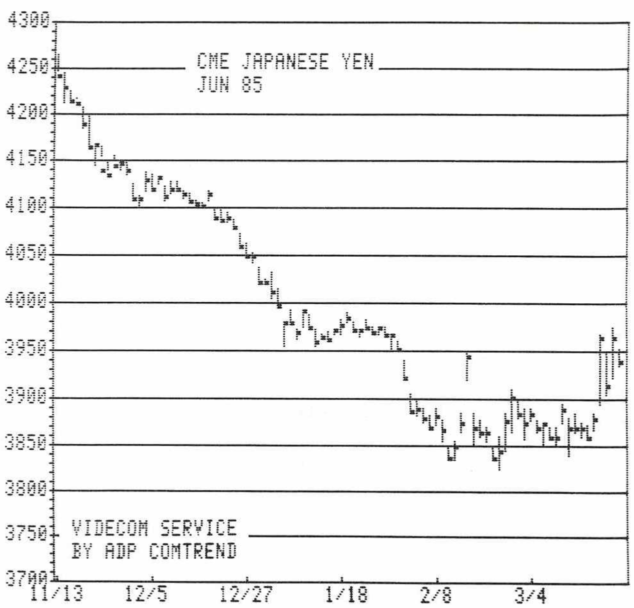


Chart 8

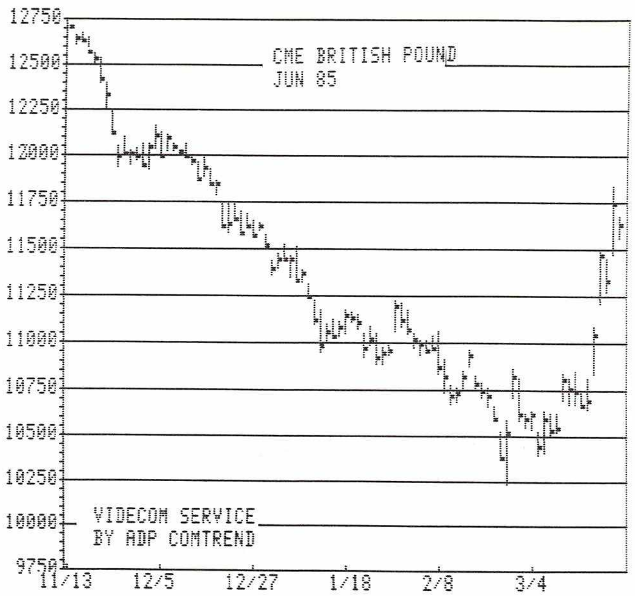


Chart 9

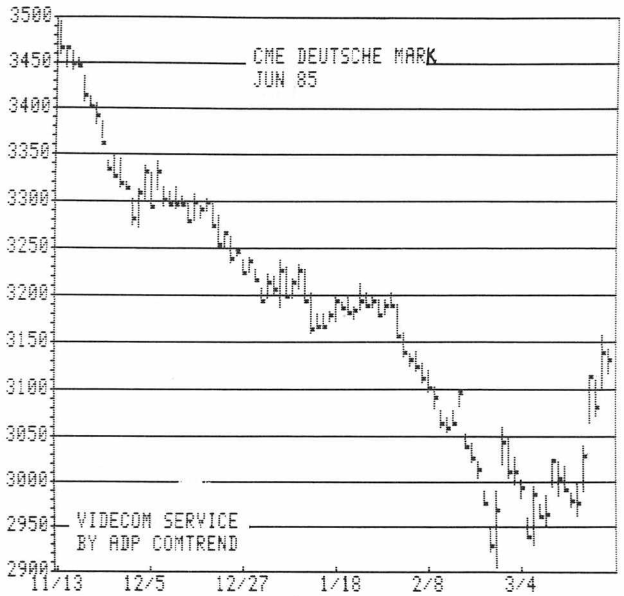


Chart 10

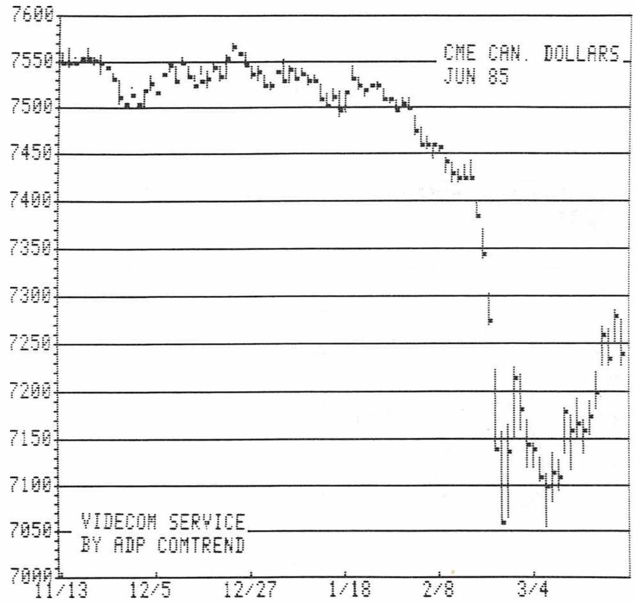


Chart 11

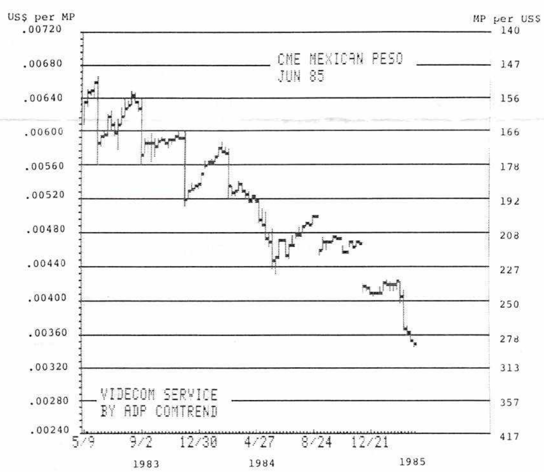


Chart 12 (South Africa)

YEAR	U.S. DOLLAR PER SOUTH AFRICAN RAND (PERIOD END)	U.S. 1968=1.00	U.S. 1977=1.00	BASKET (U.S. 26%, U.K. 21%, Germany 19%, Japan 22%, Switzerland 12%) 1968=1.00	BASKET 1977=1.00
1967	1.4018	0.9715	0.9557	0.9767	0.7697
1968	1.3898	1.0000	0.9838	1.0000	0.7881
1969	1.3988	1.0149	0.9984	1.0219	0.8053
1970	1.3943	1.0335	1.0167	1.0382	0.8181
1971	1.3068	1.0899	1.0722	1.1749	0.9259
1972	1.2773	1.0835	1.0660	1.1528	0.9085
1973	1.4900	0.9001	0.8855	0.9984	0.7868
1974	1.4501	0.9180	0.9031	1.0728	0.8454
1975	1.1500	1.1155	1.0974	1.2680	0.9993
1976	1.1500	1.0612	1.0440	1.1841	0.9332
1977	1.1500	1.0165	1.0000	1.2689	1.0000
1978	1.1500	0.9925	0.9764	1.3151	1.0364
1979	1.2094	0.9280	0.9129	1.2875	1.0146
1980	1.3402	0.8355	0.8219	1.1788	0.9290
1981	1.0454	1.0265	1.0098	1.2635	0.9958
1982	0.9314	1.0657	1.0484	1.2114	0.9547
1983	0.8185	1.1145	1.0964	1.1884	0.9366
1984 (1Q)	0.8093	1.0902	1.0725	1.1646	0.9178
1984 (2Q)	0.7380	1.1661	1.1471	1.1984	0.9444
1984 (3Q)	0.5988	1.4100	1.3871	1.3769	1.0851
1984 (4Q)	0.5038	1.6334	1.6069	1.5401	1.2137

Above 1.00 = undervalued
Below 1.00 = overvalued

Chart 13 (South Africa)

YEAR	FOREIGN ASSETS (Mln US$)	CURRENT ACCOUNT As % of GNP %	CUMULATIVE 12 QTR Current Account (Mln US$)
1970	917	- 7.65	-1,545
1971	554	- 7.70	-3,090
1972	1,158	- 0.60	-2,816
1973	1,199	- 0.30	-1,685
1974	945	- 4.19	-1,662
1975	287	- 6.65	-4,107
1976	- 700	- 5.55	-5,897
1977	- 655	1.43	-3,906
1978	1,549	3.51	190
1979	4,758	6.34	5,479
1980	7,475	4.65	8,450
1981	2,302	- 5.76	2,541
1982	1,640	- 4.41	-3,933
1983	911	- 0.42	-7,119
1984 (1Q)	469		
1984 (2Q)	555		
1984 (3Q)	263		

Chart 14 (South Africa)

HARD CURRENCY COVER (In millions of U.S. Dollars)

Reserves* + Previous 12-months current Account *** = 2,027

(Reserves + 12-months C/A) M1** = 2027/12518 =16.2%

(Reserves + 12-months C/A) Broad Money ** = 2027/21899 = 9.2%

*As at Dec. 1984 ** Nov. 1984 *** Jan-Dec. 1984 (Estimated)

Figures in millions of U.S. Dollars

	ML (Converted to U.S. Dollars)	Broad Money (Converted to U.S. Dollars)
1973	4884	10,838
1984 (Nov.)	12518	21,899
% Increase (decrease)	156.30%	102.05%
Corresponding % increase in the United States	104.22%	159.69%

(a) 1983 Imports as percentage of GNP 18.90%
(b) 1974-1983 Imports as percentage of GNP 23.31%
1983/(1974-1983 average) = (a)/(b)= 81.00%

Source: IFS

RATES	SPOT	1 MONTH	3 MONTH	6 MONTH	12 MONTHS
	.5130-.5160	.5060-.5110	.4950-.5020	.4815 -.4895	.4670-.4720

Stock Indexes

Continued concern over corporate profits has put the US stock markets on the defensive. The well-documented plight of the computer companies, including IBM, whose first quarter will be down for the first time since the recession of 1981, and semiconductors is now being joined by a growing number of manufacturing enterprises, trucking companies, and — more of the same — financial institutions.

The smaller-than-expected first-quarter GNP "flash" report (at 2.1% annual rate) has begun to vindicate our view that there is nary a sector in the economy healthy enough to sustain the economy's upward momentum. It is worthwhile pointing out that consumer spending, excluding installment credit (which, again, rose last month at a near-20% annual rate), is running flat on a real basis and is showing the smallest current-dollar gain since the early '60s. Hardly a boom. In addition, import penetration is now all pervasive and has become a major drag on corporate profit margins and the economy. Nonresidential construction, unaffected as yet by the squeeze on tradeables, should begin sobering up as office vacancies mount to the highest levels in the post-war period.

Fundamentals are now firmly on the side of the bears. Leveraged buyouts continue to transform equity (of questionable value) into debt (which must be serviced with highest-on-record real interest rates). It is incredible that sophisticated LBO players like Forstmann Little can offer $59 per share for the shares of McGraw-Edison, which traded as low as $4 per share in the last major recession (1974-75) and whose erratic earnings performance averaged less than $2.75 per share over the past five years. The sum-of-the-parts-is-greater-than-the-whole myth is just one aspect of the greater fool theory so prevalent at the end of the last stock market mania (1969). Can it go on forever? The liquidation of City Investing is proving that we may be nearing the end of the game: First thought to bring in $48-$50/share and later $45/share, it is now doubtful that it can fetch more than $38/share.

Finally, the great king of value, the son of Graham-Dodd, Warren Buffet seems to have succumbed to the buyout mania: He advances over a half-billion dollars to Capital Cities for the latter to take over ABC — a mediocre broadcasting network that traded last year at less than half the buyout price. In exchange, he receives stock in Capital Cities at $175 per share, exactly 7 times the price prevailing in 1979, and 17.5 times the price touched at the bottom of the 1974 bear market. In the process, Capital Cities must borrow $2.2 billion, increasing its *own* debt by a factor of 11.

The arbitrage between high private market valuation — the rationale for the recent buyouts — and apparently discounted public companies *must*, at some point, put downward pressure on the former but, more importantly, must call into question the breadth and liquidity of such private markets. At any rate, it seems anomalous that private and public markets, run by the same investors, should show such valuation gaps.

STRATEGY: *We remain bearish. Short positions on the June '85 S&P were reinstated as per the Hotline Update. Leave stops at 186.00, close only. Also June '85 S&P 500. Put options with a strike of 7180 have been purchased at around the 3.00-3.25 level and represent excellent value.*

Chart 15

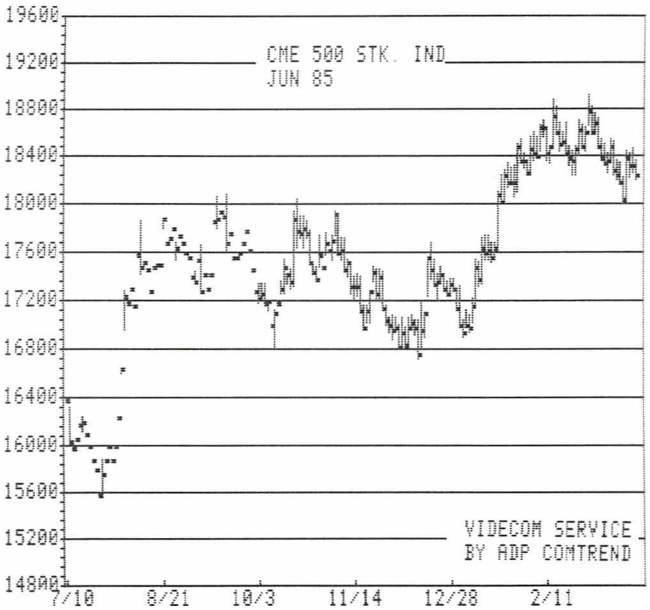
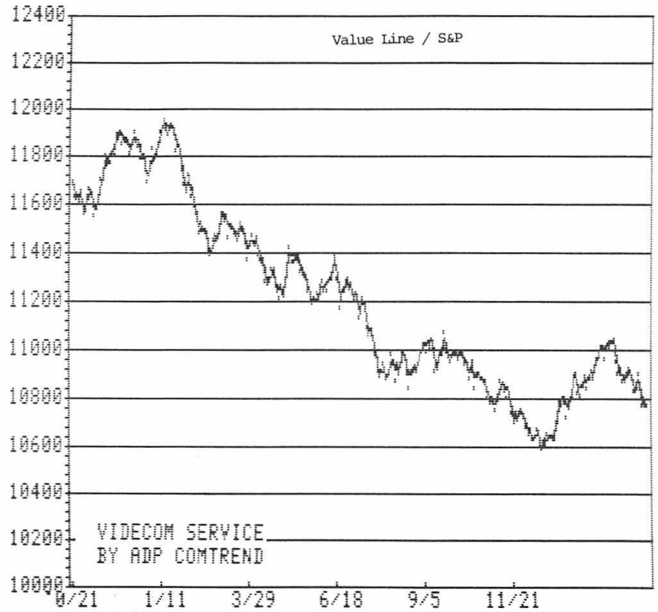


Chart 16



Crude Oil

Relatively low US stocks of distillates and gasoline have firmed product prices, which in turn has had a favorable effect on crude prices. Netbacks have expanded dramatically (Chart 17) and should begin to impact refining runs and imports, which have remained quite weak.

The strong inversion (or backwardation) in the US futures markets has caused us to become more cautious, near term, and in fact we recommended covering all short positions on March 13 at about 27.50, basis May '85. Backwardations represent a tug-of-war between consumers, who prefer to live hand-to-mouth and disciplined producers. There is little doubt that *some* destocking is taking place, although the size of it is surely much smaller than expected by Opec. Backwardations also imply an excessively bearish position. Contrarian traders should beware. At any rate, it is no fun to sell into a backwardation as the May-June spread (Chart 18) attests.

The inversion has us puzzled: Is Opec's marginal production of 15.8-16.0 million barrels per day (mb/d) just right to maintain a relatively well-balanced market? It does not seem possible. Moreover, neither Brent nor Arab Light are showing exceptional strength or comparable inversions. Is a squeeze play developing in the US market? Surely it cannot carry too far as foreign supplies will begin to flood the market. At this moment, West Texas Intermediate sells approximately $1.10/barrel higher than Brent — historically a fairly wide margin.

Before reinstating short positions, we would like to see the steep inversion collapse — a sign that complacency has once again overtaken this market. And also a sign that the condition of relative tightness of supplies in the US has improved.

STRATEGY: *Having covered all short positions (as per Hotline Update of March 13), we remain sidelined looking for a good opportunity to reinstate them. Patience is a virtue.*

Chart 17

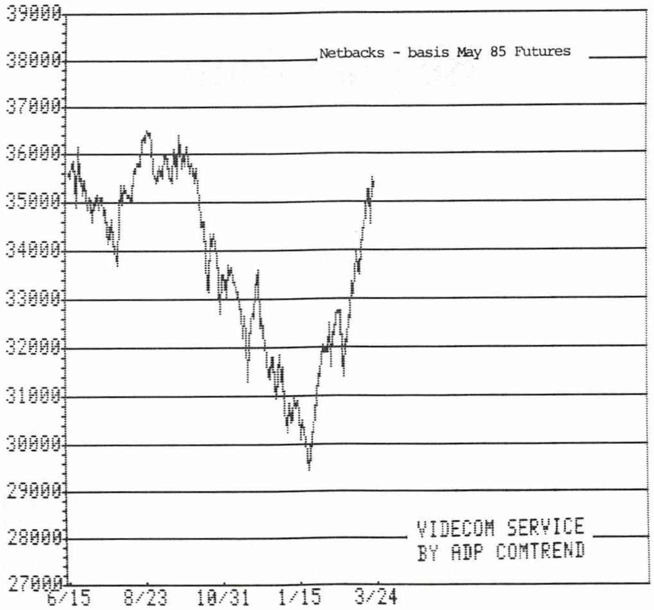


Chart 18

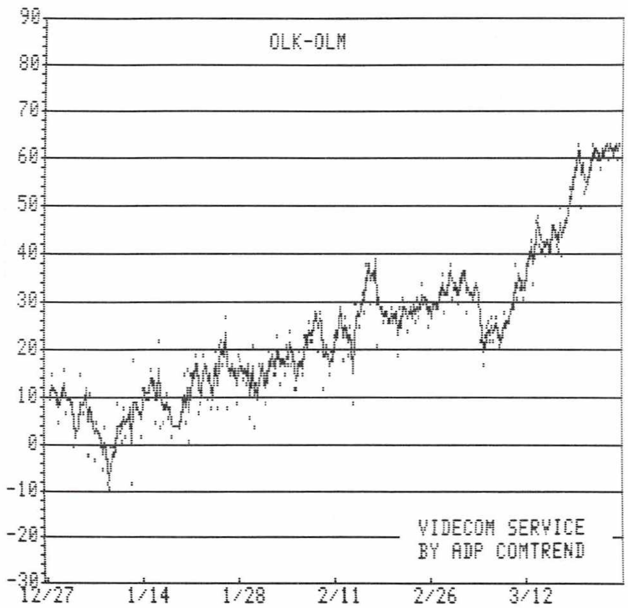
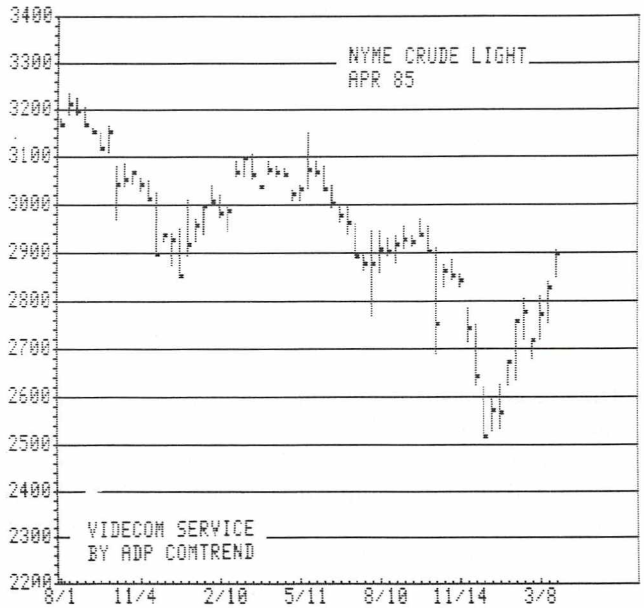


Chart 19



The Exotics

Belgian franc

BASKET			
U.S.	8%	Italy	6%
U.K.	13%	France	22%
Germany	29%	Netherland	22%

YEAR	BELGIUM FRANC per: U.S. DOLLAR (PERIOD END)	U.S. 1970=1.00	U.S. 1977=1.00	BASKET 1970=1.00	BASKET 1977=1.00
1967	49.62	0.9500	1.6039	0.9548	1.1711
1968	50.08	0.9726	1.6421	0.9694	1.1890
1969	49.66	0.9806	1.6556	0.9841	1.2070
1970	49.67	1.0000	1.6884	1.0000	1.2265
1971	44.75	0.8989	1.5177	0.9876	1.2113
1972	44.12	0.8694	1.4680	0.9570	1.1738
1973	41.32	0.8086	1.3653	0.9655	1.1842
1974	36.12	0.6953	1.1739	0.8844	1.0847
1975	39.52	0.7370	1.2443	0.8964	1.0994
1976	35.98	0.6506	1.0985	0.8013	0.9829
1977	32.94	0.5923	1.0000	0.8153	1.0000
1978	28.88	0.5345	0.9025	0.7979	0.9786
1979	28.04	0.5528	0.9334	0.8545	1.0481
1980	31.52	0.6615	1.1169	0.9850	1.2082
1981	38.46	0.8283	1.3985	1.0274	1.2602
1982	46.92	0.9855	1.6639	1.1285	1.3841
1983	55.46	1.1168	1.8855	1.1551	1.4167
1984 (1Q)	53.08	1.0512	1.7749	1.1061	1.3567
1984 (2Q)	56.68	1.1190	1.8893	1.1147	1.3672
1984 (3Q)	61.37	1.2115	2.0455	1.1295	1.3854
1984 (4Q)	63.08	1.2430	2.0987	1.1101	1.3615

Above 1.00 = undervalued
Below 1.00 = overvalued

Year	Foreign Assets (Mln US$)	CURRENT ACCOUNT As % of GNP %	CUMULATIVE 12 QTR. Current Account (Mln US$)
1970	2.11	2.75	987
1971	2.93	2.22	1605
1972	3.34	3.60	2659
1973	3.68	2.99	3319
1974	3.53	1.43	3447
1975	3.96	0.28	2332
1976	3.81	0.63	1390
1977	3.42	-0.69	62
1978	2.24	-0.84	-936
1979	-1.61	-2.77	-4448
1980	-1.90	-4.15	-8839
1981	-6.12	-4.27	-12196
1982	-7.49	-3.12	-11788
1983	-9.00	-0.93	-7605
1984 (1)	-9.93		-7031
1984 (2)	-9.74		
1984 (3)	-9.29		
1984 (4)			

HARD CURRENCY COVER (In millions of U.S. Dollars)

Reserves * + Previous 12-months current Account *** = 5649
(Reserves + 12-months C/A)/M1 ** = 5649/14834 = 38%
(Reserves + 12-months C/A)/ Broad Money ** = 5649/32923 = 17.1%
*As at Jan. 1985 **Sept. 1984*** April 1983 - March 1984

Figures in millions of U.S. Dollars

	M1 (Converted to U.S. Dollars)	Broad Money (Converted to U.S. Dollars)
1973	12591	21,190
1984 (3)	14834	32,923
%Increase (decrease)	17.8%	55.3%
Corresponding % increase in the United States	101.4%	155.3%

(a) 1983 Imports as percentage of GNP 57.35%
(b) 1974-1983 Imports as percentage of GNP 48.41
1983/(1974-1983 average) = (a)/(b) = 118.46%

Source: IFS

RATES	SPOT	1 MONTH	3 MONTH	6 MONTH	12 MONTHS
	65.00 - 65.10	65.10 - 65.20	65.21 - 65.33	65.30 - 65.44	65.37 - 65.55

Outlook and recommendation: Among European currencies, the Belgian franc stands out as quite undervalued — at least on a purchasing power parity basis. The heavy current account deficits of 1979 through 1982 caused external debt to soar. As a result, debt service charges impose severe budgetary and balance-of-payments constraints. Nevertheless, there has been a dramatic shift in the current account, which now may be in equilibrium. Also, the center-right ruling party has created a far more favorable environment for capital. On a relative basis, the BF is a better long position than the DM. Buy!

Italian lira

				=========== BASKET ===============	
				U.S. 13%	Belgium 6%
				U.K. 10%	France 26%
				Germany 31%	Netherland 7%
					Switzerland 7%
YEAR	ITALIAN LIRA per: U.S. DOLLAR (PERIOD END)	U.S. 1970=1.00	U.S. 1977=1.00	1970=1.00	1977=1.00
1967	623	0.9400	1.0059	0.9489	0.7554
1968	623	0.9635	1.0310	0.9645	0.7678
1969	625	0.9958	1.0656	0.9993	0.7955
1970	623	1.0000	1.0701	1.0000	0.7961
1971	594	0.9456	1.0119	1.0249	0.8159
1972	582	0.9089	0.9726	0.9908	0.7887
1973	607	0.9079	0.9715	1.0705	0.8522
1974	649	0.9043	0.9677	1.1375	0.9055
1975	683	0.8888	0.9511	1.0715	0.8530
1976	875	1.0303	1.1025	1.2512	0.9961
1977	871	0.9345	1.0000	1.2562	1.0000
1978	829	0.8535	0.9133	1.2393	0.9865
1979	804	0.8017	0.8579	1.1960	0.9521
1980	930	0.8689	0.9298	1.2354	0.9834
1981	1200	1.0501	1.1237	1.2749	1.0148
1982	1370	1.0919	1.1684	1.2366	0.9844
1983	1659	1.1910	1.2745	1.2364	0.9843
1984 (1Q)	1618	1.1093	1.1871	1.1693	0.9308
1984 (2Q)	1716	1.1624	1.2439	1.1669	0.9289
1984 (3Q)	1883	1.2716	1.3607	1.2025	0.9573
1984 (4Q)	1935	1.2849	1.3750	1.1736	0.9342

Above 1.00 = undervalued
Below 1.00 = overvalued

Year	Foreign Assets (Mln US$)	CURRENT ACCOUNT As % of GNP %	CUMULATIVE 12 QTR. Current Account (Mln US$)
1970	5.556	0.89	5996
1971	6.616	1.83	5347
1972	5.589	1.54	4934
1973	5.231	-1.64	1494
1974	1.116	-4.74	-8608
1975	- 964	-0.30	-11181
1976	4.228	-1.54	-11544
1977	9.016	1.13	-1041
1978	20.400	2.38	5776
1979	34.359	1.66	14091
1980	46.289	-2.47	1850
1981	39.340	-2.45	-12991
1982	30.884	-1.64	-24089
1983	37.517	0.17	-13691
1984 (1)	35.397		-10680
1984 (2)	32.617		- 9284
1984 (3)			
1984 (4)			

HARD CURRENCY COVER (In millions of U.S. Dollars)

Reserves * + Previous 12-months current Account *** = 21554

(Reserves + 12-months C/A/ M1 ** = 21554/128260 = 16.8%
(Reserves + 12-months C/A/Broad Money ** = 21554/220260 = 9.8%
*As at Jan. 1985 **Sept. 1984*** July 1983-June 1984

Figures in billions of U.S. Dollars

	M1 (Converted to U.S. Dollars)	Broad Money (Converted to U.S. Dollars)
1973	88.97	133.64
1984 (3)	128.26	220.26
%Increase (decrease)	44.19%	64.77%
Corresponding % increase in the United States	101.4%	155.3%

(a) 1983 Imports as percentage of GNP 21.48%
(b) 1974-1983 Imports as percentage of GNP 22.19%
1983/(1974-1983 average) = (a)/(b) = 96.80%

Source: IFS

Outlook and recommendation: Continued participation in the EMS seems assured in the near term, as the external payments position is fairly comfortable. Italy's greatest problem lies in the domestic fiscal sector where budget deficits continue to accumulate at an unsustainable pace. Forex rates reflect the unusually high interest rate structure — a result of relatively high inflation and those large government funding requirements. Therefore, long lira positions may be justified so long as the EMS complex enjoys a bullish trend. Long against DM and, for now, long against the US dollar.

RATES	SPOT	1 MONTH	3 MONTH	6 MONTH	12 MONTH
	2042-2046	2051-2057	2070-2078	2095 - 2110	2137 - 2149

Forex Rates & Update

Currency	*Spot*	*3-month*	*12-month*	*Comments vis-à-vis US$*	*Comments vis-à-vis DM*
Australian dollar	.7015-.7025	.6910-.6925	.6800-.6830	Remain long	Buy
Danish krone	11.52-11.54	11.57-11.59	11.53-11.57	Take profit: cover	Sell
Indonesian rupiah	1100-1105	1120-1175	N/A	Remain short	Sell
Kuwaiti dinar	.30335-.30355	.30215-.30335	.30135-.29850	Cover; reinstate at .295	Sell
Malaysian ringgit	2.5350-2.5450	2.5490-2.5620	2.5520-2.5925	Take profit: cover	Sell
Mexican peso	248-249	278-285	358-385	Remain short	Sell
New Zealand dollar	.4590-.4650	.4315-.4500	.3490-.4250	Neutral	Neutral
Norwegian krone	9.22-9.23	9.30-9.31	9.39-9.42	Neutral	Neutral
Portugese escudo	178-180	184-196	198-225	Buy	Remain long
Saudi Arabian riyal	3.6055-3.6085	3.6120-3.6195	3.6115-3.6245	Take partial profits: cover	Sell
Singapore dollar	2.2250-2.2350	2.2097-2.2207	2.1700-2.1950	Cover	Sell
Spanish peseta	178.50-178.75	180.25-180.75	183.50-184.75	Cover	Neutral
Swedish krona	9.23-9.24	9.33-9.34	9.46-9.50	Buy	Remain long
Venezuelan bolivar	13.10-13.20	13.12-13.25	13.70-14.60	Neutral	Neutral

Explanatory Notes

Currency expected to firm against both currencies.	Buy	Buy
Currency expected to strengthen against US $ and weaken against DM.	Buy	Sell
Currency expected to weaken against both major currencies.	Sell	Sell
Currency expected to weaken against US $, but strengthen against DM.	Sell	Buy
Term used to advise liquidation of previous short position but does not imply a new buy recommendation.	Cover	
Term used to advise sale of previous long position, but does not imply a new short sale recommendation.	Liquidate	

Hotline Update

February 27; 1:45 p.m.: Close out short positions in Canadian dollar and Deutschemark, accepting generous profits. Stand aside.

March 7: Due to technical difficulties, you may have had trouble reaching out hotline. We would like to tell you that our latest message was dated February 27/85, 1:45 p.m., and read as follows: "Close out short positions in Canadian dollars and Deutschemark, and accepting generous profits. Stand aside."

March 8, 1985; 4:20 p.m.: You may have been stopped out of the June '85 S&P as per our stop recommendation of 188.75, good anytime. If you did, reinstate short positions at the market, and place initial stops at 186.00, close only. Alternatively, you could purchase June '85 S&P put options striking 180, at present levels, a recommendation that was also made in our last newsletter as an alternative to outright short sales. There have been a number of questions regarding short crude oil positions. Our advice continues to be: Remain short.

March 13; 12:20 p.m.: We advise now to cover all short crude oil positions at the market, looking to reinstate short positions at higher levels via the very deferred contracts. Please keep posted.

March 15: Here is a recap of this week's Hotline Update, and three new recommendations: You are flat all crude oil short positions as of 12:20 p.m., March 13. We believe the market may still go a bit higher and hope to reinstate these short positions at a later date, preferably via the September/November months. The three new recommendations are: Buy June '85 Comex gold and July '85 Comex silver, risking 293 and 5.60, close only; buy June '85 Canadian dollar at market, risking 70.95, close only.

Friedberg's Commodity & Currency Comments (ISSN 0229-4559) is published monthly by Friedberg Commodity Management Inc., 347 Bay Street, Toronto, Ontario, M5H 2R7.

Subscription Enquiries
Friedberg's Commodity & Currency Comments
347 Bay Street
2nd Floor
Toronto, Ontario, Canada
M5H 2R7
(416) 364-1171

Trading Accounts
All enquiries concerning trading accounts should be directed to
Friedberg Mercantile Group
347 Bay Street
Toronto, Ontario M5H 2R7
(416) 364-2700
Cable: Friedco Toronto. Telex: 06-23446.