FRIEDBERG'S
COMMODITY & CURRENCY COMMENTS

Friedberg Commodity Management Inc. Volume 7, No. 3 March 23, 1986

Is inflation really dead?

The notion that inflation is dead has captured the imagination of Wall Street's gurus and Washington's policymakers. Larger than expected declines in popular price indices have recently lent support to the "Inflation is Dead" thesis. For example, earlier this month the Labor Department reported that the Producer Price Index fell by 1.6% in February. This represents the largest monthly decline since this index was first calculated in 1947.

The euphoria about the prospects for inflation have resulted in a free fall in long-term interest rates, with Treasury bond rates falling by over 350 basis points since March 1985. Lower long rates have, of course, propelled the bond and stock markets to record heights.

Given what we believe to be Washington's new economic policy and our analyses of the economy's underlying fundamentals, we don't share the same optimism. Barring some unforeseen policy changes, inflation, and consequently long-term interest rates, will move upward over the next two years.

In 1980, policymakers were primarily concerned with inflation. With their success in bringing inflation rates down, policymakers have become complacent about controlling inflation and have shifted their attention to stimulating economic growth through credit expansion.

The first evidence of a policy shift occurred in late September, 1985. At that time, officials from the so-called G-5 (France, Germany, Japan, The United Kingdom, and The United States) agreed to a coordinated currency intervention strategy aimed at driving down the value of the dollar. The G-5's intervention initially clobbered the dollar and injected a good bit of wariness into the foreign exchange market. But, the G-5's ultimate success in achieving a lower value dollar will require the rate of inflation in the United States to be higher, on a sustained basis, than in other industrial countries. This will require a relatively high level of credit expansion in the United States.

Shortly after the September 22, 1985, meeting of the G-5, US Treasury Secretary James A. Baker III travelled to Seoul, South Korea, where, on October 8, he addressed a joint meeting of the World Bank and the International Monetary Fund. Secretary Baker argued that the industrialized countries should help the less developed nations cope with their huge debt problems. His solution, the so-called "Baker Plan," is a credit expansion plan to lend the 15 largest debtors $29 billion at favorable terms, over the next three years.

The most recent evidence of a shift in policy towards credit expansion aimed at spurring economic growth rather than squeezing inflation came on February 24, 1986. For the first time during his tenure as Chairman of The Federal Reserve Board, Paul Volcker was outvoted. By a margin of 4 to 3, the Board of Governors voted to lower the discount rate to 7% from 7.5%, with all of President Reagan's appointees — Preston Martin and Martha Seger as well as Wayne Angell and Manuel Johnson, who were both sworn in only last month — favoring the rate reduction.

In a face-saving maneuver Mr. Volcker persuaded the Board to defer action until a worldwide rate cut could be arranged. After arm-twisting by Chairman Volcker, the West German Bundesbank put the ball into play by lowering its discount rate on the evening of March 6. This move was followed by other major central banks, and the next morning the Federal Reserve Board, in a 6-0 vote (Governor Seger was absent at the time of the vote), reduced its rate.

The new economic growth policy rests, in large part, on the premise that inflation is dead. It also stems from the threat of protectionism, falling employment levels in some manufacturing industries, and concern about the health of the real estate, agricultural, and energy sectors of the economy. There is also a desire to ease monetary policy and stimulate the demand for primary products so that debtor nations can handle their obligations with less difficulty.

Inflation is ultimately a monetary phenomenon. In consequence, inflation can occur on a sustained basis only if monetary policy is sufficiently expansive to consistently generate

In this issue

Metals are climbing, especially gold, and we remain long. Do the Saudis have a scheme to put a lid on crude at $10/bbl.? We stay long-term bears. We prefer to be long gold rather than currencies, and we probe the short side of T-bonds. And we look at lumber and sugar — two relatively new games in town. Contributions by Steve H. Hanke, Albert D. Friedberg, and Daniel A. Gordon.

aggregate demand that exceeds the nations' productive capacity. Last year, the growth in the money supply was 11.6%, which was the largest annual increase since World War II. Even though the economic impact of this money growth was blunted by an unusually low money velocity — 5.5% (the ratio of gross national product divided by the money supply, M1) — monetary growth generated an aggregate demand that exceeded the nation's real growth, 2.5%. This resulted in consumer price increases of about 3.5%.

We believe that The Federal Reserve will continue to adhere to an expansive monetary policy in 1986. Also, we anticipate that the forces that pushed velocity down last year will reverse themselves in 1986. Since the economy's real growth will not match the growth in aggregate demand (nominal GNP) that will be generated by the monetary expansion, inflation will result. (For our forecast, read on.) So, inflation is not dead and will not die in 1986.

Many hold a contrary view because they harbor fundamental misunderstandings about (1) the distinction between changes in relative prices and changes in the general price level (inflation) and (2) the distinction between transitory effects on prices and the underlying trend in inflation. To understand the consequences created by these misunderstandings, consider the recent freefall in crude oil prices.

Most have concluded that this will cause the general price level to drop. But, if the Federal Reserve doesn't take offsetting action to restrain the growth in the money supply — and we don't believe that it will — the sharp drop in oil prices will have the following consequences: First, reported price indices will temporarily fall below their underlying trends, which are determined by monetary policy. Second, these indices will move back in line with their underlying trends because consumers will have more money available for non-energy uses. In consequence, the demand for non-energy products, such as industrial commodities, will increase and so will their prices. Hence, relative prices will be altered, but ultimately the general price level will be unaffected because the decline in energy prices will be offset by increases in non-energy product prices. If these adjustments could take place instantly, there would, of course, be an immediate shift in relative prices and the reported inflation indices would not depart from their underlying trends. In short, falling oil prices cannot change the underlying trend in the general price level. Only monetary authorities can accomplish this.

Changes in the value of the dollar also cause temporary deviations from the underlying trend in inflation. For example, the dollar soared by nearly 70% from the end of 1980 to the end of 1984. In consequence, this reduced the price of US imports and kept the reported inflation indices from fully reflecting the underlying inflation that was associated with monetary growth during this period. With the sharp fall in the dollar since February 1985, this process has been reversed, so that import prices will rise and reported inflation indices will tend to be higher than their underlying trends.

The transitory impact of the oil price declines and the drop in the dollar's value will work to offset each other. But, the magnitude of the impact of the dollar's decline on price indices will be somewhat greater than that of the oil price decline, and their timing will be quite different. The transitory oil price decline will be transmitted through the economy much more swiftly than the dollar's decline. Hence, in the near-term, reported price indices will tend to be lower than the underlying inflation trends, while the reported indices will be higher than the underlying trends in 1987.

It appears that the analytical confusion surrounding (1) the distinction between changes in relative prices and changes in the general price level and (2) the distinction between transitory effects on prices and the underlying trend in inflation has caused Wall Street's gurus and Washington's policymakers to adopt a myopic view of inflation. By focusing on the recent decline in oil prices and the transitory effects that it is already having on reported price indices, these soothsayers have incorrectly concluded that inflation is dead. With these expectations about the prospects for inflation, the free fall in long-term bond rates should not be surprising. We believe that this expectational overreaction to oil price declines will be altered shortly as the transitory impact of the dollar's decline begins to take hold and the underlying inflation trend comes into focus once again.

Reported inflation in 1986 will be about 0.5% higher than for 1985 and the 1987 rate will be 1.5% to 2% higher than 1986. These reported inflation rates will dramatically alter inflation expectations and drive long-term bond rates up from current levels by at least 100 basis points by the end of 1986. Measured from current levels, long bond rates should be 250 basis points higher by the end of 1987.

STRATEGY: *We continue to favor precious metals, namely gold and platinum. Some industrial commodity markets will strengthen. We like copper. We also like the short side of bonds. Inflation expectations and bond rates could turn around at any moment.*

— By Steve H. Hanke

Metals

Gold

Backing and filling but with a steady upward tilt, bullion prices are doubtless reacting to the weakened dollar and the extremely accommodative Fed posture. The market now enjoys *solid* support at the 340 level, basis June '86, and is about to challenge the 360-370 congestion area formed in January.

STRATEGY: *We remain* extremely *bullish. Long-term investors should continue to accumulate on $15-$20 dips (as occurred in February). Short-term traders should now add on crossing 371, basis June '86. Our next near-term target is $400-$420/oz., basis spot.*

Chart 1

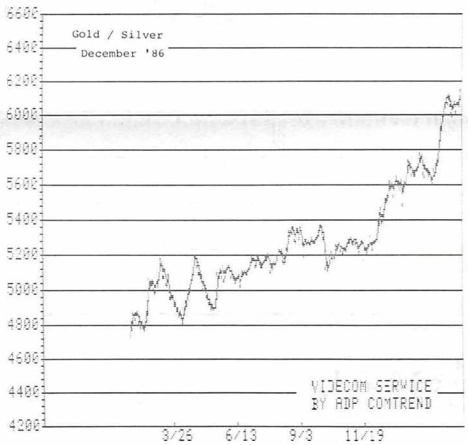
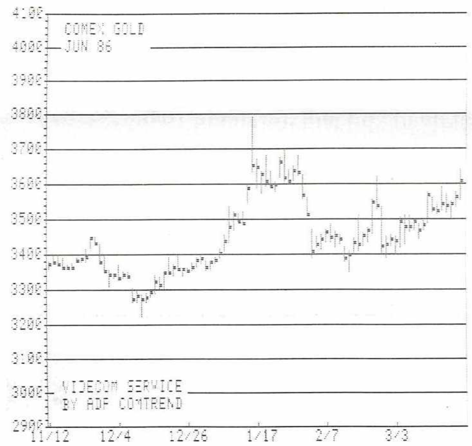


Chart 2



Platinum

The spectacular $120/oz. advance since late 1985 has been accompanied by rising open interest and some dramatic bullish consensus numbers, especially in the past four weeks. This combination points to heavy speculative interest and the possibility of severe and unannounced shakeouts. Nevertheless, the fundamentals are intriguing enough (output interruptions in South Africa and a strong and successful marketing effort of small-sized bars) to warrant not disturbing our long positions. It is interesting to note this market is almost flat going out to April '87, perhaps an early sign of spot shortages.

STRATEGY: *Remain long, keeping a generous stop at 385, basis July '86, close only.*

Chart 3

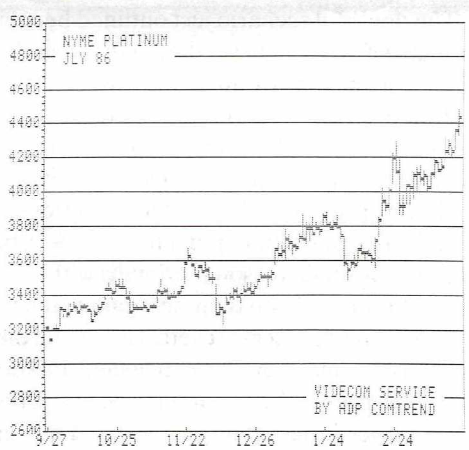
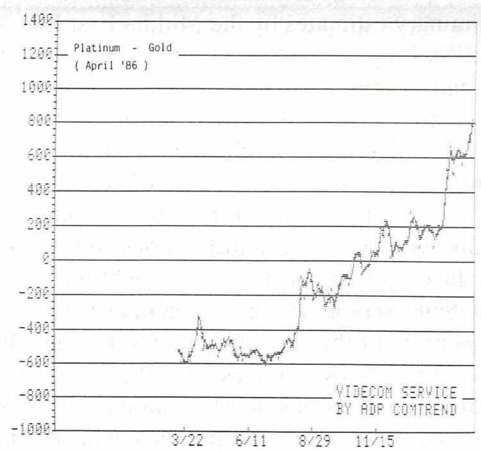


Chart 4

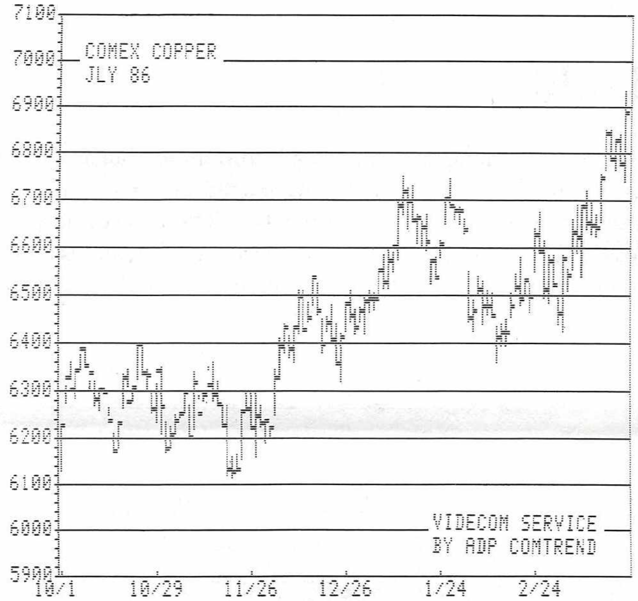


Copper

The very orderly and steady climb promises to carry this market to substantially higher levels. At the very least, one would expect the dollar price of copper to reflect the 30%-plus depreciation of the greenback over the past 12 months, especially in view of the continuous draw-downs of LME/Comex warehouse stocks.

STRATEGY: *Remain long. Raise stops to 64.00, basis July '86, close only.*

Chart 5



Energy Futures

"We agreed to defend the price structure at $28/barrel and to carry out all the necessary measures to gradually reach that level again... (Opec's 13 members would adopt) a series of measures that would be made public in due time... (while the five non-Opec countries would) decide by themselves the most convenient approach." With these words Arturo Hernandez Grisanti, Venezuela's oil minister and the conference president, tried to reconcile that which is irreconcilable: a desire to maintain unrealistically high prices in the face of mounting supply and shrinking demand.

Opec's crude oil output averaged 16.65 million barrels per day (mb/d) for the first two months of 1986, according to preliminary estimates by the Middle East Economic Survey (MEES). Projections for March indicate that Opec production had increased to some 17.3 mb/d, which could bring the first quarter's average to 16.87 mb/d. Since Libya, Algeria, Iran, and Nigeria are producing substantially less than their "quotas," the latter two because of "technical" difficulties, one could argue that all or most of the remaining nine Opec members are cheating: hardly a constructive omen at a time that the oil-producing nations are fighting for economic survival. Saudi Arabia's netback deals have cleverly pre-empted and captured other members' markets, a situation that will spell yet much lower prices once the four "abstainers" (and Mexico, which has lost market share to the tune of 300,000-400,000 b/d) force their output on to a buyers' market.

It is obvious that the perverse supply curve that we postulated in previous issues is alive and well: As prices drop, more and more producers are tempted to increase output to make up for lost revenues. Those few that rein in production have a variety of reasons: political motives (very soon, of course, they will have to abandon their ideological stand); simply because they have not been able to ship out the crude, (i.e., Iran); or because they have been too slow to react to a fast-falling market (i.e., Nigeria), in which case a little bit of panic will help. Since the Saudis are no longer neither willing nor capable (see following discussion) of acting as swing producers, any self-imposed cutback would have to be proportional, hardly a probability, given the attitude of at least seven Opec members (everyone except the four "abstainers," Kuwait, and Saudi Arabia).

The doubtful scenario just outlined becomes even more improbable if, as we believe, the Saudis have changed their oil strategy to a) maximize output and revenues, b) stimulate consumption over the medium- to long-term horizon, c) shut in high-cost producers, d) eliminate new exploration and development, and e) defeat Iran. All these objectives can be met by first allowing prices to collapse to absurdly low levels, and then later to be in a position to put a lid on at $10/barrel. This, in our view, is the main reason the Saudis withheld their 1986-87 budget: a desire to keep their new game plan under wraps.

The belated strategic reversal is costing the Saudis dear: $22 billion over and above the anticipated drawdown of $10-$12 billion. At this rate, the Saudis may be out of (liquid) international reserves in less than two years. They are, therefore, gambling that they can raise production rather substantially and sell somewhere between $5 and $10/barrel, so as to slow down their foreign exchange drain.

Assuming that the Kingdom can ultimately sell 11 mb/d at $8/barrel, its revenue would fall short of the 1985-86 budget estimate by approximately $12 billion. This shortfall can be made up by a combination of further budget cutbacks and a relatively modest devaluation. Over the longer term, the Saudis gamble on a substantial pick-up in demand, an increase in capacity and output, and a slight increase in price. Depending on the magnitude and speed of the adjustment, the Kingdom may yet remain solvent. Our belief is based on the fact that the Saudis have learned the lesson of the past six years well: Carrying on their shoulders the restriction of output is a sure way to insolvency.

STRATEGY: *At this writing, there are noises emanating from Opec sources indicating that a "broad understanding" has been reached to cut output to 14 mbd. In light of our previous discussion, this scenario is either totally improbable or absolutely impossible.* Nevertheless, it may serve to "goose" the market higher over the next few days, particularly since the general view is that prices in 1986 probably will stabilize around $15/barrel.

Long-term traders should rest assured that the bear market is far from over and that eventually prices will break the $5/barrel mark. In the interim, prices reached our first target of $12/barrel and may recover further on news of an apparent Opec agreement. Closes above $14.50, basis May '86, will signal some further firming to the $17/barrel range and could be used for short-term trading against one's basic long-term bearish position.

Chart 6

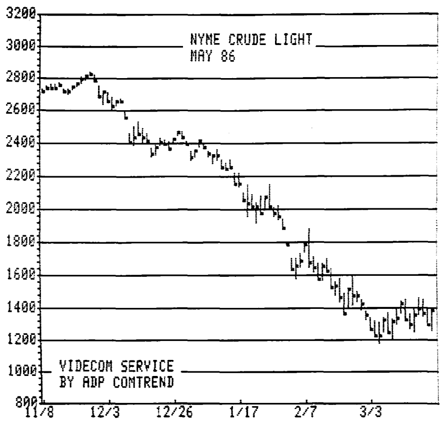


Chart 7

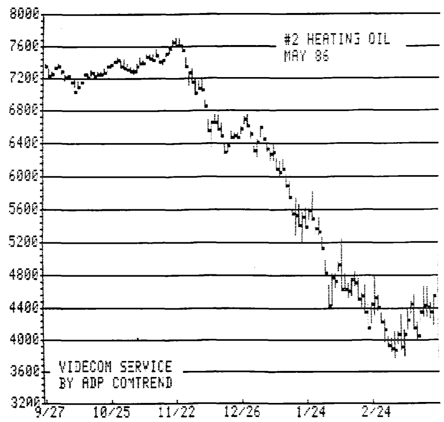
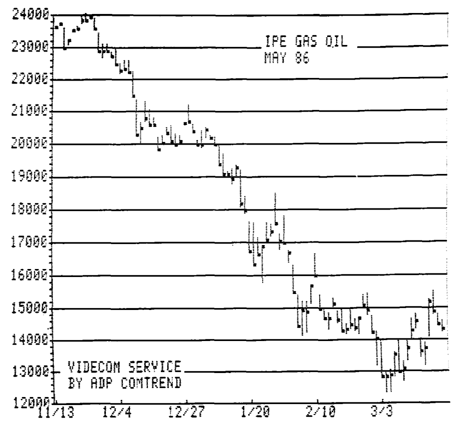


Chart 8



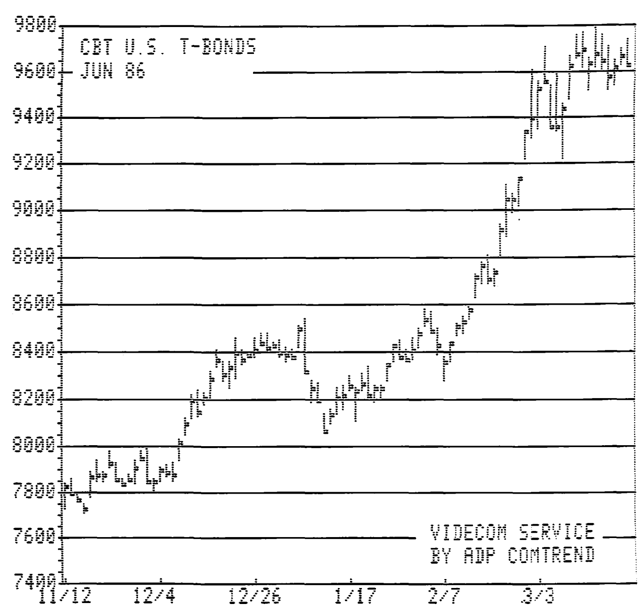
Interest Rate Futures

T-bond futures are tracing a massive top. For the past 14 trading sessions, 50,000 outright short positions have been mercilessly closed out and/or hedges lifted without causing any upward impact on prices. In fact, June '86 has remained locked in a 95-98 trading range with most closes bunched around the 95½-96½ area.

While it is possible that prices can still go a little bit higher, we believe this is most unlikely. All the favorable news, particularly in oil, has been discounted. On the other hand, the extreme dollar weakness has as yet not produced a current account financing crisis (which will necessitate higher interest rates), but it soon will, and bond traders have as yet to discover the rapid rise of some commodity prices (see previous section). The confluence of these factors will cause a collapse of bond prices, an avalanche that will be accelerated by early redemption of shares in bond mutual funds, sales of which hit insane annual rates of $150 billion in the recent months.

STRATEGY: *We'd like once more to probe the short side with a limited risk of 98.01, basis June '86, close only.*

Chart 9

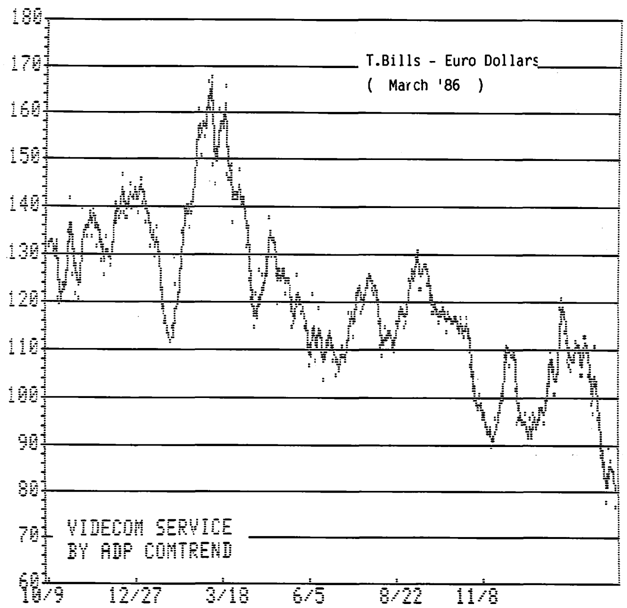


Ted Spread

The short March '86 Eurodollar/long March '86 T-bill spread (Ted spread) did not widen, as the Mexican threat of default was politely pushed aside by the administration. Another chance, another day.... We did not deem it advisable to roll over to June '86, because we are still torn over the validity of the trade. After all, the deposits of the 10 largest US banks are (are they?) government-guaranteed and should not (?) carry a risk premium. Our intention was merely to take *quick* profits as the default scenario hit the headlines.

STRATEGY: *Stand aside.*

Chart 10



Stock Index Futures

And the music goes on. While stock prices may not seem expensive in relation to earnings, they are incredibly expensive in relation to dividends. In fact, at 29 times dividends, stock prices are more expensive than at the 1929 highs and come close to the highest peak recorded in the century. Since the rationale for buying common stock is the expectation of a steady stream of future dividends that betters expected returns from fixed-income deposits and/or securities, one wonders how long this insane valuation can go on. (In our next issue we hope to expand somewhat on the dividend approach to market valuation.)

Rarely do markets advance to such extremes without casting a troublesome shadow ahead. Although we intuitively know this to be true, we are confused by the nature of the impending threat. A sharp inflationary bout accompanied by sharply rising interest rates? A deep recession, triggering worldwide defaults? Stocks are extremely vulnerable, as they are now as expensive as they ever were during this century.

STRATEGY: *Retain June S&P puts.*

Lumber

It's a relatively new game in town. Brought on by rising residential construction, lumber prices have skyrocketed upward in recent weeks, thus beginning the fourth up cycle in the past 15 years. Deferred positions trade at substantial discounts to spot (May/November '86 is at $23 premium May) and offer an interesting speculation on the revival of price inflation. We caution that the market is relatively thin and extremely volatile — not for the faint-hearted.

STRATEGY: *Buy November '86 at market. Place initial stops at 160, close only.*

Chart 11

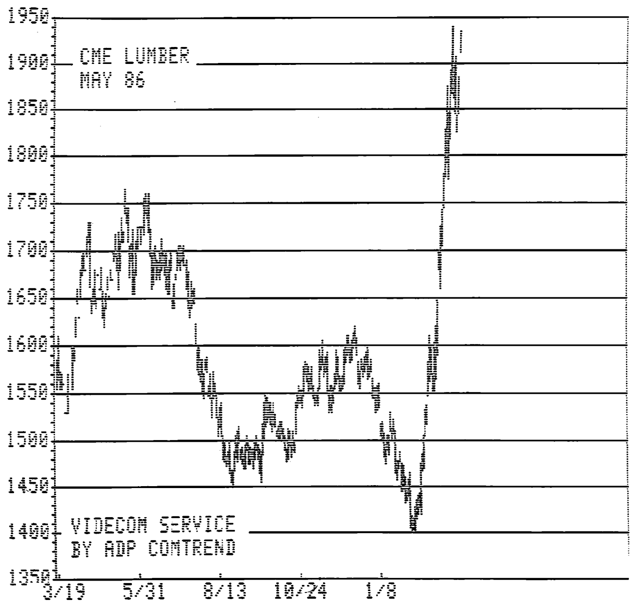
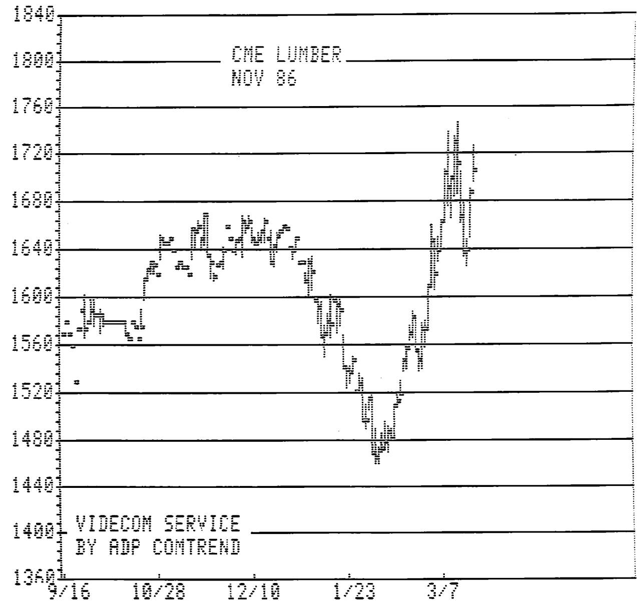


Chart 12

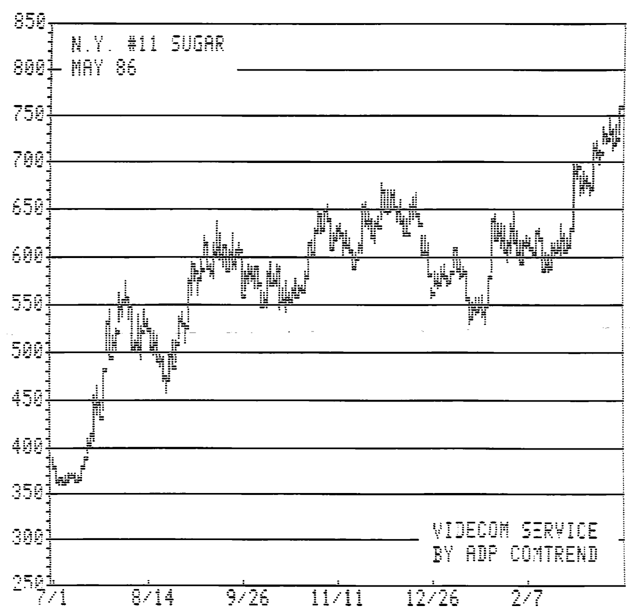


Sugar

Here too, a steady and quite orderly advance is picking up wide speculative support. Inevitably, shakeouts will be sharp and unexpected.

STRATEGY: Modest *long positions can be established at these levels with the hope of increasing them on setbacks. We set our near-term sights at the 13¢ level, which represented the high of the 1983 bull move.*

Chart 13



Currencies

The recent cut in the US discount rate following similar cuts in West Germany and Japan has been carefully orchestrated to minimize its impact on the US dollar. Mr. Volcker continues to believe that the dollar has entered a "danger zone"; a glance at some of the previously discussed commodities supports this view.

Further downward pressure on the dollar is likely to encounter strong resistance, particularly from the Bank of Japan. Should intervention fail to slow the bandwagon, monetary policy in the US would have to be tightened, thus triggering a wholly undesirable chain of events. Nevertheless, the consequence of playing with fire is getting burned....

With the resignation of Mr. Preston Martin, we believe the Fed will be successful in putting up a defense against further dollar depreciation — at least until a new governor is installed. The expansionist governors of the Fed live under a dangerous illusion. *Being long gold, rather than currencies, is still a preferred strategy.*

Chart 14

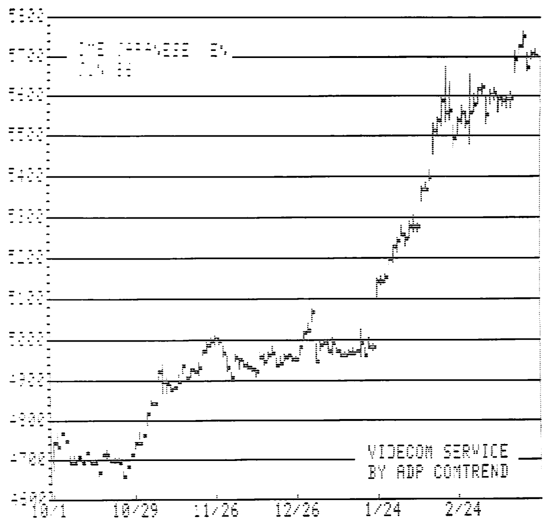


Chart 15

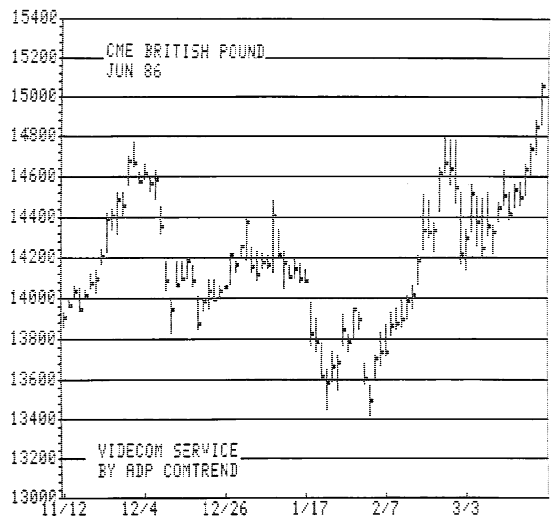


Chart 16

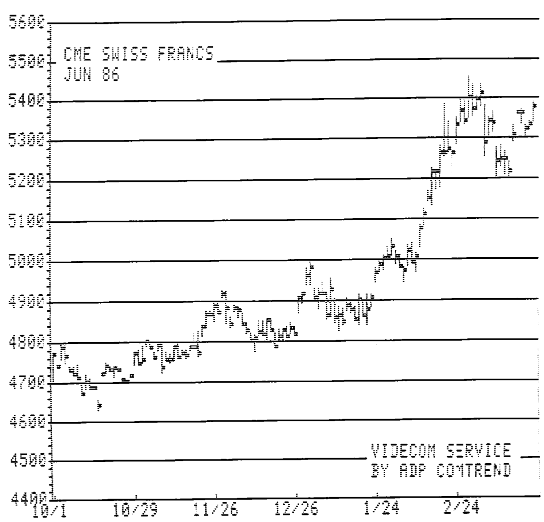


Chart 17

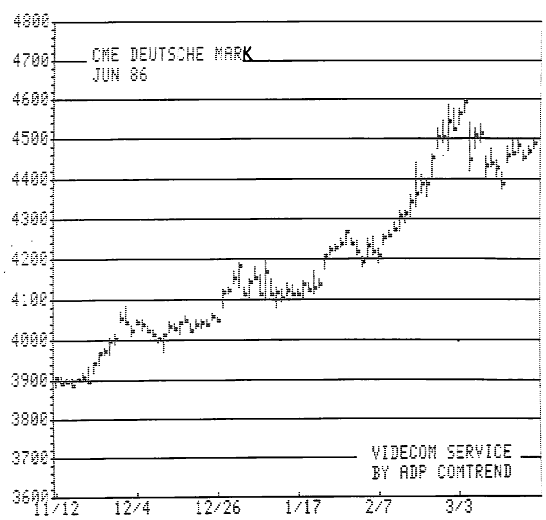
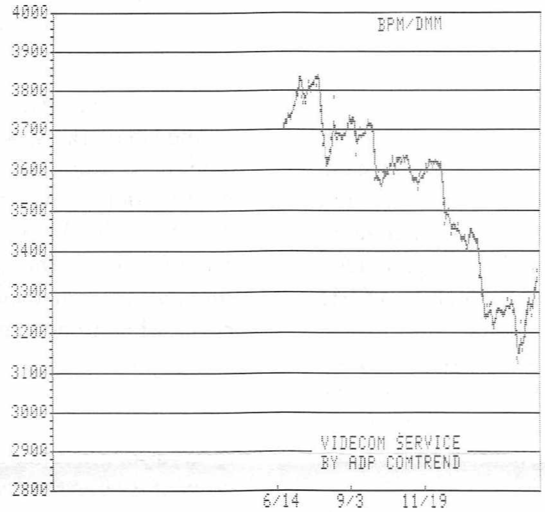


Chart 18



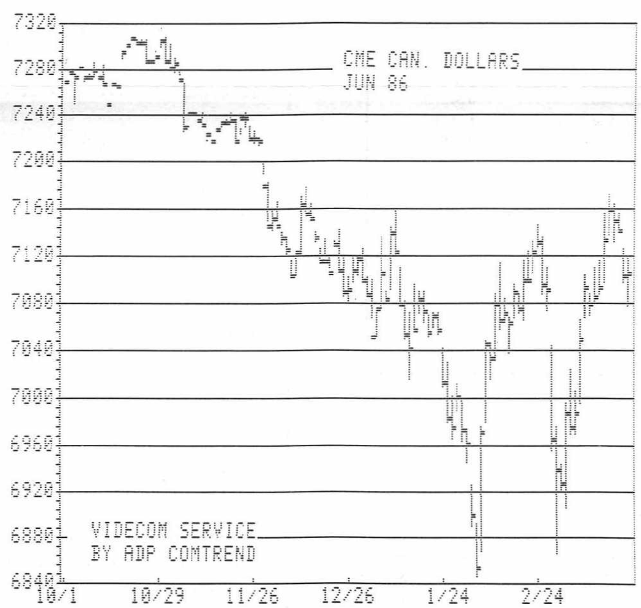
Canadian dollar

In last month's special report, we pointed out that Canada would be facing some unusually large outflows during 1986, led by a prospective current account deficit of $10 billion. We suggested that a combination of a lower Canadian dollar (3%-5% ? from 1985's average) and a wide interest spread (300-400 basis points) might bring the external accounts into equilibrium.

In the interim, Dome Petroleum has announced that it will suspend debt services on $1.4 billion of unsecured debt and it would tie interest payments on secured debt to cash flow — putting further pressure on Canadian chartered banks already troubled by heavy LDC debt. Advances from the Bank of Canada have risen to a new high, averaging $4.48 billion for the week to March 12. The Continental Bank and the Bank of British Columbia are thought to be receiving Central Bank aid. Another insolvency would surely rock further confidence in the Canadian unit.

STRATEGY: *At this time, the Canadian dollar seems to be locked in a range of 72.25-69.25, giving few clues to its final destination. We still believe the breakout is likely to be on the downside. Remain short. Cover on a spot close above 72.25.*

Chart 19



The Exotics

Venezuelan bolivar

Venezuela is facing some tough times ahead. The sharp decline in oil prices is likely to reverse the 1985 current account surplus of $3.9 billion to a deficit of perhaps as much as $4 billion. Under the recently signed rescheduling agreement, Venezuela is committed to make annual payments of $4-$5 billion to its creditors. In view of the disastrous turn for the worse in the current account, Venezuela is likely to succeed in demanding better rescheduling terms, with only minimal annual downpayments. Nevertheless, the basic problem of being a mono-exporter, and of a declining commodity to boot, remains.

In the long run. Venezuela must be able to diversify its exports, taking advantage of its good strategic location vis à vis the US markets. As a first step, the government must validate the substantially higher free market rate for the dollar. As a matter of fact, the extraordinary divergence between the official 7.50 bolivares to the dollar and the free market rate of 19.00 to the dollar is quite counterproductive, as it stimulates overinvoicing of imports and underinvoicing of exports, while impeding local manufacturers from benefitting from a more remunerative exchange rate.

STRATEGY: *Forward rates remain much too expensive to allow for attractive short sales, especially in view of the government's large reserve hoard, which it is likely to make use of from time to time. Remain sidelined.*

Chart 20

YEAR	VENEZUELAN BOLIVARES PER: U.S. DOLLAR (PERIOD END)	U.S. 1970=1.00	U.S. 1978=1.00
1967	4.45	0.9152	0.9239
1968	4.45	0.9423	0.9514
1969	4.45	0.9686	0.9779
1970	4.45	1.0000	1.0096
1971	4.35	0.9881	0.9976
1972	4.35	0.9943	1.0038
1973	4.28	0.9971	1.0067
1974	4.28	1.0215	1.0313
1975	4.28	1.0132	1.0229
1976	4.29	0.9978	1.0073
1977	4.29	0.9851	0.9945
1978	4.29	0.9905	1.0000
1979	4.29	0.9800	0.9894
1980	4.29	0.9155	0.9242
1981	4.29	0.8713	0.8796
1982	4.29	0.8421	0.8502
1983	4.30	0.8195	0.8273
1984	7.50	1.3287	1.3415
1985 (1Q)	7.50 *	1.2347	1.2465
1985 (2Q)	7.50 *	1.2389	1.2508
1985 (3Q)	7.50 *	1.2299	1.2417
1985 (1Q)	14.00 **	2.3047	2.3269
1985 (2Q)	14.00 **	2.3126	2.3348
1985 (3Q)	14.00 **	2.2958	2.3178

* Average of all rates, rate used by IFS
** Approximate free market rate.

Above 1.00 = undervalued
Below 1.00 = overvalued

Chart 21

Year	Foreign Assets (Mln US$)	CURRENT ACCOUNT As % of GNP %	CUMULATIVE 12 QTR. Current Account (Mln US$)
1970	899	-0.09	-518
1971	1,389	0.00	-335
1972	1,612	-0.07	-216
1973	2,387	5.34	756
1974	6,413	22.53	6536
1975	8,807	7.85	8808
1976	7,961	0.08	8185
1977	8,081	-8.78	- 754
1978	6,701	-14.61	- 8660
1979	8,124	0.07	- 8564
1980	7,383	7.94	- 657
1981	8,870	5.97	9078
1982	9,708	- 6.40	4482
1983	11,889	6.90	4181
1984	10,317	10.96	5479
1985 (Aug)	10,716	-	-

Chart 22

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

Reserves * + Previous 12-months current Account *** = 17,329
(Reserves + 12-months C/A)/MI ** = 17,329/11,213 = 154%
Reserves + 12-months C/A)/Broad Money ** = 17,329/22,641 = 76%
* As at October 1985 ** August 1985 *** 1985 E.

Figures in millions of U.S. Dollars

	MI (Converted to U.S. Dollars)	Broad Money (Converted to U.S. Dolllars)
1974	3,735	6,064
1985 (Aug)	11,213	22,641
% Increase (decrease)	200	273
Corresponding % increase in the United States	111.6	165.5

(a) 1984 Imports as percentage of GNP 15.0%
(b) 1975 - 1984 Imports as percentage of GNP 19.3%
1984/(1975 - 1984 average)= (a)/(b) = 77.7%

Source: IFS

Chart 23

RATES	SPOT	1 MONTH	3 MONTH	6 MONTH	12 MONTH
	18.80-18.90	18.90-19.15	19.10-19.35	19.40-19.90	20.10-20.90

Dutch guilder

The Christian Democratic liberal coalition has been relatively successful in narrowing the grotesque budget deficit to 7% of GNP from 11% of GNP. In recent months, though, some concern has been evidenced by virtue of the fact that natural gas prices have fallen considerably and could impact government revenue in 1986 by as much as 2% of GNP. Prime Minister Lubbers has already warned that some further tax increases and expenditure cutbacks may have to be implemented to redress these imbalances. In the meantime, the country's unemployment rate remains stubbornly high at 15.4%, with only a very minor improvement vis à vis 1984. It should be noted that more than half of the unemployed have been out of work for more than one year, a situation that cannot last indefinitely.

STRATEGY: *The external position remains healthy as the country continues to record sizable current account surpluses. In the near-term, we do not expect currency changes vis à vis the DM.*

Remain long against the DM to pick up forward discounts.

Chart 24

BASKET: U.S. 11%, Belgium 20%, Germany 41%, UK 14%, France 14%

YEAR	DUTCH GUILDER 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	3.5960	0.9959	1.3388	0.9952	1.7664
1968	3.6060	0.9907	1.3318	0.9998	1.7747
1969	3.6240	0.9911	1.3324	0.9880	1.7538
1970	3.5970	1.0000	1.3443	1.0000	1.7750
1971	3.2581	0.9601	1.2907	0.8799	1.5618
1972	3.2265	0.9076	1.2201	0.8351	1.4823
1973	2.8245	0.8411	1.1307	0.7189	1.2760
1974	2.5065	0.7979	1.0727	0.6458	1.1463
1975	2.6885	0.8053	1.0826	0.6843	1.2147
1976	2.4570	0.7163	0.9630	0.6072	1.0778
1977	2.2800	0.7439	1.0000	0.5634	1.0000
1978	1.9690	0.7127	0.9581	0.5026	0.8922
1979	1.9055	0.7677	1.0320	0.5192	0.9216
1980	2.1295	0.8930	1.2005	0.6184	1.0977
1981	2.4685	0.8960	1.2045	0.7417	1.3166
1982	2.6245	0.8856	1.1905	0.7898	1.4019
1983	3.0645	0.9497	1.2767	0.9259	1.6436
1984	3.5495	0.9609	1.2918	1.0832	1.9227
1985 (1Q)	3.4820	0.9879	1.3280	1.0694	1.8982
1985 (2Q)	3.4485	1.0087	1.3560	1.0612	1.8836
1985 (3Q)	3.0165	0.9581	1.2880	0.9352	1.6600
1985 (4Q)	2.7720	0.9179	1.2339	0.8643	1.5342

Above 1.00 = undervalued
Below 1.00 = overvalued

Chart 25

Year	Foreign Assets (Mln US$)	CURRENT ACCOUNT As % of GNP %	CUMULATIVE 12 QTR. Current Account (Mln US$)
1970	3,458	-1.51	-355
1971	4,622	-0.28	-439
1972	5,767	2.94	762
1973	7,215	3.99	3664
1974	9,000	3.11	5990
1975	10,165	2.40	6628
1976	10,984	3.00	6939
1977	11,004	0.55	5341
1978	13,164	-1.04	1915
1979	13,744	-1.31	-2885
1980	13,773	-2.35	-6480
1981	15,470	2.06	-2138
1982	15,736	2.69	3632
1983	16,508	2.92	10483
1984	22,090	4.03	10364
1985 (1)	24,055	-	10254
1985 (2)	25,092	-	-
1985 (3)	27,419	-	-

Chart 26

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

Reserves * + Previous 12-months current Account *** = 29,514

(Reserves + 12-months C/A)/MI ** = 29514/28360 = 104%

Reserves + 12-months C/A)/Broad Money ** = 29514/88016 = 33.5%

* As at November 1985** Sept. 1985 *** 1985 (2) -1986 (1)

Figures in millions of U.S. Dollars

	M1 (Converted to U.S. Dollars)	Broad Money (Converted to U.S. Dolllars)
1974	15,731	39.88
1985 (Sept)	28,360	88,016
% Increase (decrease)	80.2%	120.7%
Corresponding % increase in the United States	114.1	166.8

(a) 1984 Imports as percentage of GNP 44.3%

(b) 1975 - 1984 Imports as percentage of GNP 39.5

1984/(1975 - 1984 average)= (a)/(b) = 112.1%

Source: IFS

Chart 27

RATES	SPOT	1 MONTH	3 MONTH	6 MONTH	12 MONTH
	2.5370 - 2.5380	2.5327- 2.5340	2.5243- 2.5258	2.5123 2.5143	2.4880 2.4910

Forex rates & Update

Currency	*Spot*	*3-Month*	*12-Month*	*Comments vis à vis US$*	*Comments vis à vis DM (Spot DM 2.2500)*
Australian dollar	.7130-.7140	.6980-.6995	.6675-.6695	Remain long	Remain long
Belgian franc	46.00-46.10	46.26-46.43	46.35-46.60	Neutral	Remain long
Danish krone	8.29-8.30	8.29-8.31	8.29-8.33	Neutral	Neutral
Greek drachma	139.60-139.90	144.10-146.10	158.60-168.90	Remain short	Remain short
Italian lira	1528-1529	1531-1533	1538-1541	Neutral	Neutral
Kuwaiti dinar	.28665-.28695	.28653-.28746	.28637-.28912	Remain short	Remain short
Malaysian ringgit	2.5400-2.5420	2.5635-2.5685	2.6000-2.6270	Remain short	Remain short
Mexican peso	478-483	Not available	Not available	Remain short	Remain short
New Zealand dollar	.5350-.5370	.5170-.5205	.4770-.4890	Neutral	Neutral
Norwegian krone	7.08-7.09	7.18-7.20	7.47-7.50	Neutral	Neutral
Portugese escudo	147-148	152-160	162-188	Neutral	Neutral
Saudi Arabian riyal	3.6490-3.6500	3.6590-3.6620	3.6840-3.6950	Remain short	Remain short
Singapore dollar	2.1620-2.1630	2.1515-2.1535	2.1170-2.1380	Remain short	Remain short
Spanish peseta	141.35-141.45	143.05-143.85	147.35-148.95	Neutral	Neutral
Swedish krona	7.16-7.17	7.22-7.24	7.33-7.37	Neutral	Neutral

Explanatory Notes

*Indicates change in recommendation from last issue

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 liquidate short position but does not imply a new buy recommendation	Cover	
Term used to indicate sale advice of previous long position, but does not imply a new short sale recommendation.	Liquidate	

Hotline Update

Tuesday, February 25: There are no changes. The market letter is in the mail. Next update Friday Feb. 28.

Friday, February 28: There are no changes or new recommendations.

Tuesday, March 4: There are no changes or new recommendations.

Friday, March 7: There are no changes or new recommendations.

Tuesday, March 11: There are no changes or new recommendations.

Friday, March 14: There are no changes or new recommendations.

Tuesday, March 18: There are no changes or new recommendations.

Friday, March 21: There are no changes or new recommendations.

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