FRIEDBERG'S
COMMODITY & CURRENCY COMMENTS
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The international money game

Even the most casual observers are aware of the important role that Japan plays in international trade. In contrast, few appreciate the less visible, but perhaps more important, role that Japan plays in the international money game. We address this matter and its implications.

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To understand Japan's role in the international money game, we must first look at the relationship between gross savings and investment in the United States. Allowing for statistical errors, the difference between domestic savings and investment (or what is called net domestic financial savings) must equal the balance on our international current account. If domestic savings are less than domestic investments, then the current account must be in deficit by an equal amount, and this deficit must be filled by importing savings from abroad. Or, to put it in different words, a current account deficit must be financed by foreigners.

The savings investment picture in the US is shown in Chart 1. In 1987, gross domestic savings were $566.4 billion, while gross domestic investments were $716.4 billion. Hence, foreigners had to finance US deficiency of $150 billion in net domestic financial savings.

Since 1982, foreigners have been net purchasers of financial and real assets in the US (see Chart 1). In consequence, US net external debts have been rising, the ratio of these debts to US GNP has been rising, and payments to foreigners of interest, dividends, and profits as a percent of GNP have been rising.

Although external debt levels and debt servicing aren't intolerably high in the US, its current account deficits are still large and its net external debt to GNP ratio is on an explosive path (see Chart 2). The Japanese are a mirror image of the US: While the US has been piling up external debt in an explosive manner, the Japanese have been busily piling up external assets.

It is important to mention that foreigners can finance the US current account deficit on a voluntary or involuntary basis. Voluntary transactions include those made by private investors, while involuntary transactions are those made by central banks. That the US external debt growth is on an explosive, unsustainable path is indicated by the fact that private foreign investors have been, over the past two years, financing a smaller and smaller portion of the US current account deficit.

With limited US current account improvement in sight, private investors have become increasingly reluctant to increase their holdings of US dollar assets. The foreign investment slack has been picked up by the central banks. Last year, for example, central bank foreign exchange reserves grew to $790 billion from $559 billion, with about two thirds of the growth accounted for as a by-product of attempts to support the dollar on foreign exchange markets.

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To understand Japan's role in the international money game, we must consider Japan's overall capital account. In the 1980s, surpluses in the current account (domestic savings over domestic investment) and in the short-term capital account (including authorized foreign exchange banks' account) have financed a long-term capital outflow and the official accumulation of external short-term assets.

The short-term capital account has not exhibited a pronounced trend. However, it is of interest to note that in 1987 this account turned from a deficit to a surplus, indicating that the nonbanking sector increased its short-term borrowing from abroad. The banking sector also increased its net imports of short-term capital. If we count errors and omissions as short-

In this issue

We bet against the US greenback — no surprise there. The bear is alive and well and living in the stock market. We look at bottlenecks in copper, speculators in platinum, and ho-hum performance in gold. We stand aside in crude oil and wait for Opec to crumble. Contributions by Albert D. Friedberg, Steve H. Hanke, Daniel A. Gordon, and Michael D. Hart.

term capital transactions, Japan's private sector, as a whole, imported short-term capital of $14 billion, $59 billion, and $90 billion in 1985, 1986, and 1987, respectively. Hence, Japan's private sector has been borrowing short and lending long in recent years. Put in other words, Japan's long-term capital outflow has been financed not only by a current account surplus but also by a short-term capital inflow.

The official (public) sector has been busy accumulating assets ($44 billion in 1987). Most of this was due to an increase in foreign exchange reserves ($40 billion).

Capital outflows from Japan have been rising steadily, while foreigners' long-term investments in Japan have been rather stable in the 1980s. Hence, there has been a large increase in net long-term outflows. Most of the increase in foreign investments by the Japanese has been in foreign securities. Most of these investments have been concentrated in foreign bonds, which are in turn concentrated in the US.

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One of the fundamental questions in the international money game is, Under what conditions will the Japanese continue to be significant players in the US bond market? The answer is rather straightforward. If US interest rates exceed those in Japan by enough to compensate Japanese investors for expected declines in the value of the dollar (foreign exchange risk), Japanese investors will participate in the US bond market.

To analyze the magnitude of the interest rate differential required to induce the Japanese to invest in US securities, we must evaluate the relationship between savings and investment in the US. To do this, we return to Chart 1 and make a forecast for 1988. Since we don't want to be unduly pessimistic, we employ the Reagan Administration's "baseline" projections.

The administration's forecast shows personal savings increasing by $25 billion, gross business savings increasing by $30 billion, and total government remaining unchanged. On the gross investment side of the ledger, domestic investment is forecast to increase by $40 billion. In consequence, the current account will improve by about $15 billion, reducing the amount of foreign financing required.

Accepting the "baseline" forecast, we anticipate a movement in the "right" direction. However, the magnitude of the movement is small, implying that it will take some time to put the US external debt growth on a sustainable path. In consequence, unless the US economy slows down (something that isn't anticipated in the "baseline" forecast), we anticipate continued downward pressure on the dollar because the current account, while improving, isn't anticipated to improve rapidly enough. That this is a correct line of reasoning is revealed, in part, by the sustained central bank intervention on behalf of the dollar; a sure sign that the currency is under pressure.

With these dollar fundamentals, Japanese investors expect a further slide in the dollar. Hence, if they are to voluntarily invest in US securities, they will have to continue to receive an interest rate differential on US investments. This is perhaps even more true now than in the past, because over the past two years the interest rate differential has not been great enough to fully compensate Japanese investors for the decline in the value of the dollar. In short, Japanese investors have taken a bath on US bonds and as a result are a bit more gun shy about the US market now than they were in 1985 and 1986. (Note that Japanese foreign bond investments in 1987 were actually lower than in 1986.)

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Given the present and anticipated fundamentals, the US must set a monetary policy that maintains the current, if not wider, US-Japanese interest rate differential. The US policy will be dictated, in part, by the Bank of Japan because Japanese rates will set a floor above which US rates must rise. In consequence, to anticipate the course of US monetary policy, we must pay particular attention in the coming months to the actions taken by the Bank of Japan.

The Bank of Japan could give the Federal Reserve some room for maneuver if it loosened Japanese monetary policy. However, even though inflation hasn't reared its ugly head in Japan, the Japanese are sensitive to this possibility. Recall that the Japanese had to contend with severe inflation in the 1970s. Given that monetary policy is already loose, that the Japanese economy is robust, and that speculative activity is on the rise, the Bank of Japan does not appear to be in a mood to further loosen monetary policy.

Short of loosening monetary policy, the Bank of Japan could act as a substitute (on a sterilized basis) for private Japanese investors, and accumulate more US assets on its accounts. In fact, it looks as though the Bank anticipates the use of this option, because the Ministry of Finance recently announced that it has projected a 33% increase in the amount of money that can be used to intervene in foreign exchange markets, to $60 billion. If used, the substitution of involuntary, for voluntary, purchases of US assets would reduce the required interest rate differential from what it would be without involuntary purchases.

Given the current state of Japanese policy, the Federal Reserve will be forced to bias its policy towards tightness, if it wants to avoid a full-blown currency crisis. This bias will become stronger, if the US economy continues to perform well (particularly if the real GNP exceeds the high end of the Fed's real GNP forecast of 2.5%).

A tighter monetary policy does have its drawbacks, however, and these have been duly noted by the Fed. Namely, it would increase the risk of a recession, which is not desired, particularly by the incumbent political party. It would increase the risk of spooking an already spooky stock market. It would create new problems for the LDC debtors. And it would increase the risk of sending troubled US banks, and savings and loan associations into a more magnified crisis. On balance, while the Fed will ultimately be forced to tighten, so that the current account can adjust more rapidly and be financed, it will follow this course reluctantly.

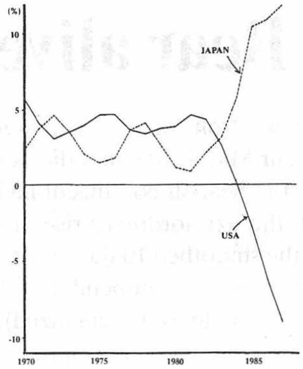
— Steve H. Hanke

Chart 1
US gross savings and investments
(US $ billions)

	Gross savings			Gross investment	
Year	Personal savings	Gross business savings	Total government surplus or deficit	Gross private domestic investment	Net foreign investment
1978	110.2	298.9	-0.4	416.8	-10.1
1979	118.1	327.7	11.5	459.8	2.6
1980	136.9	341.5	-34.5	437.0	13.0
1981	159.4	391.1	-29.7	515.5	10.6
1982	153.9	403.2	-110.8	447.3	-1.0
1983	130.6	461.6	-128.6	502.3	-33.5
1984	164.1	509.5	-105.0	664.8	-90.9
1985	127.1	537.2	-132.9	641.6	-115.9
1986	130.6	549.3	-147.8	671.0	-143.9
1987	120.2	553.4	-107.2	716.4	-156.8

Note: "Gross private domestic investment" minus "Gross savings" does not equal "Net foreign investment" because of "Statistical discrepancy."

Chart 2
Net international investment position of the USA and Japan
(as a ratio to nominal GNF)



Betting against the buck

February balance of trade figures confirm our long-standing thesis: The US dollar devaluation, by itself, cannot "turn" the current account deficit. Only when the US undergoes a substantial adjustment and savings rise dramatically can the growing external indebtedness process come to a halt. This implies a severe recession.

Paradoxically, the US dollar is quite undervalued. It will remain weak as long as the economy continues to expand. It will strengthen substantially as soon as the US enters a recession and the trade deficit disappears. The need for high interest rates is therefore obvious — not merely to defend the dollar but, rather, to bring about a serious adjustment in US domestic demand.

STRATEGY: *Heavy intervention has kept the US dollar from falling below DM1.65 and ¥124. Continuous disappointment in the trade figures will make this one-way speculation irresistible; neither the Bank of Japan nor the Bundesbank can afford to inflate their monetary base by the sums required to effectively lock the US dollar at these levels.*

Remain long yen, British pound, and EMS currencies (see Hotline Update April 14). Raise stops to 79.00, basis June yen, close only. Apply same stop to the other long currency positions.

Chart 3

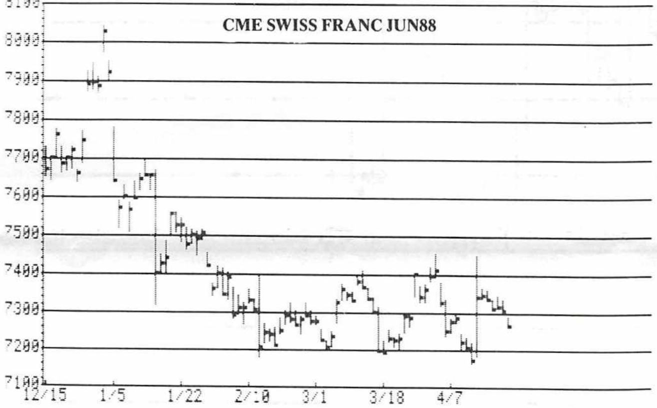


Chart 4

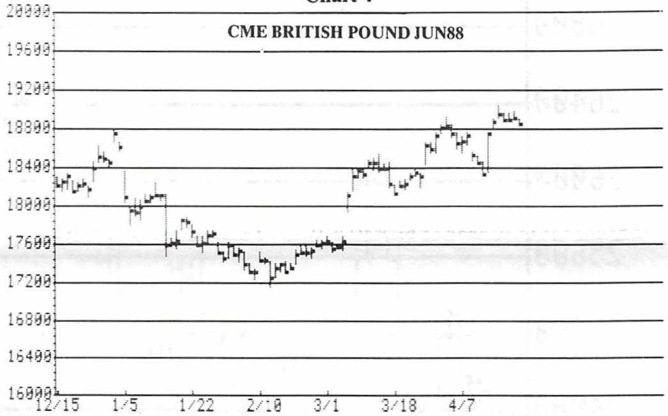


Chart 5

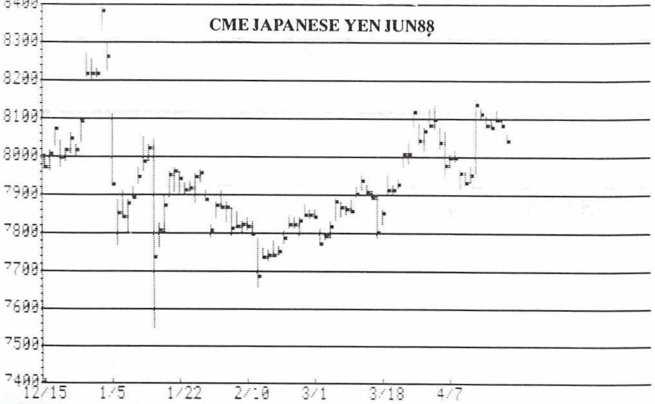
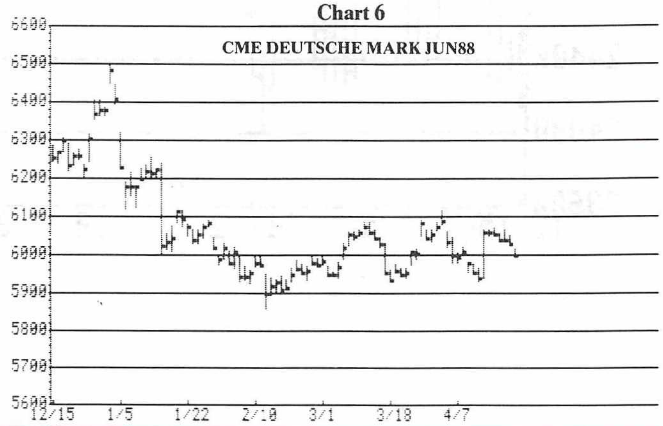


Chart 6



STOCK INDEXES

Bear alive and well and pushing down

The breakdown from the bearish "wedge" anticipated last month (see our March 20 issue) did not follow through, simply because the bearish contingent had become too numerous. In fact, the extraordinary rise of odd-lot short selling, which took the smoothed 10-day moving average up to 75,000 shares, alerted us to an impending rally (it seems that the ghost of 1930 is quite well recognized), and prompted us to advise profit-taking in our put options (see Hotline Update for April 15).

Counter-trend rallies are sharp and short-lived but clearly lacking in teeth. Volume is unable to expand on the rise, the new highs list is pathetic, and the market's attention is almost completely occupied with a number of multi-billion dollar takeover plays. Aside from this arbitrage activity, the *brokerage* business is becoming duller by the day, a sure sign of a bear market.

As we stated last month, the market is no longer oversold. It has met and crossed a (still) descending 30-week moving average line, and almost 65% of all NYSE stocks are trading above their own 30-week moving averages, up from less than 5% in the October/November period. As a result, it's unlikely that one could obtain a short-selling entry point much above 265, basis the cash S&P 500 index. This level would bring the market into line with our least conservative theoretical path.

Chart 8 illustrates two paths. The more conservative one assumes a three-year bear market and thus a 1.66% per month decline; the least conservative, a two-year bear market and thus a 2.5% per month decline. Both paths take the S&P 500 down to 135, or roughly a total 60% decline. In Dow Jones terms, our bear market should return to 1100, its long-term real equilibrium level (see *FC&CC* Feb. 21, 1988 page 6).

STRATEGY: *Reinstate September 270 S&P 500 puts on dips to the 15-17 level.*

Chart 7

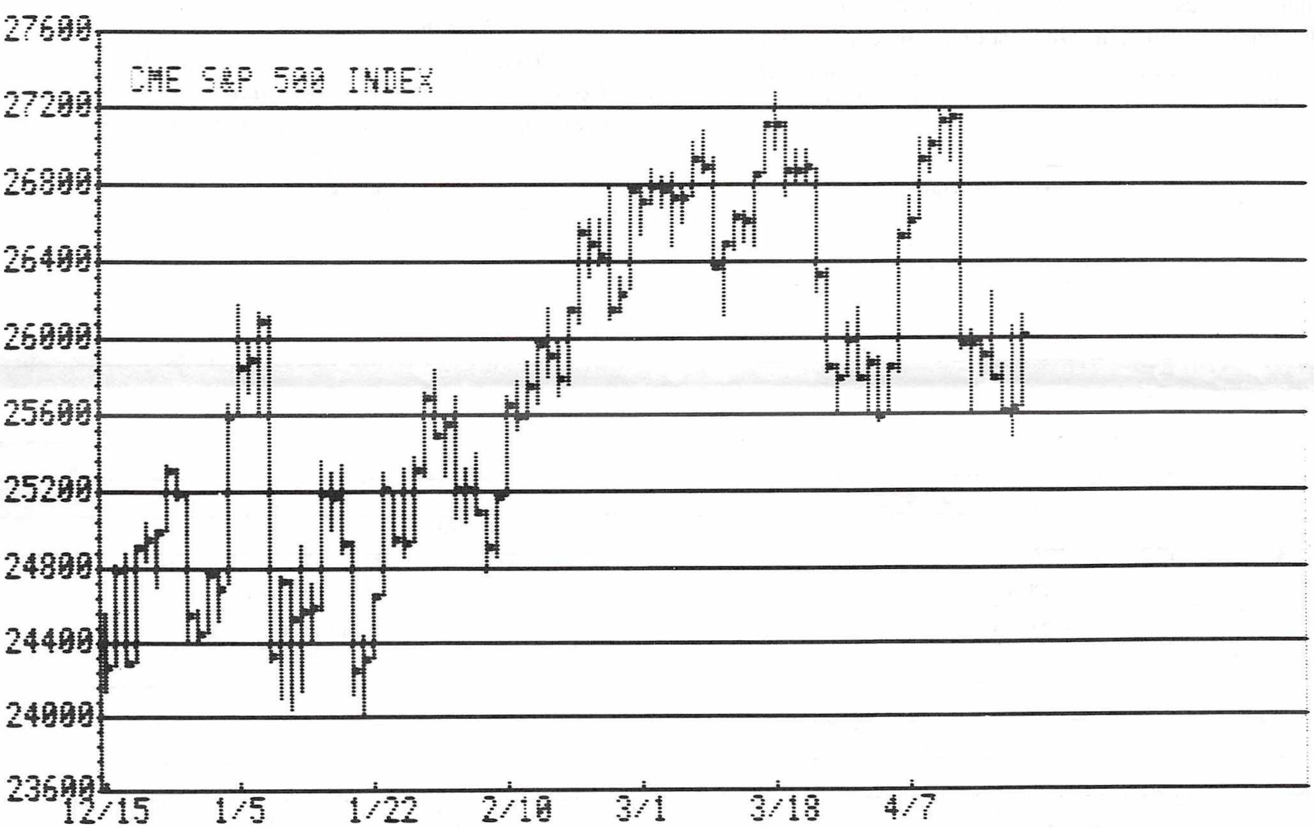
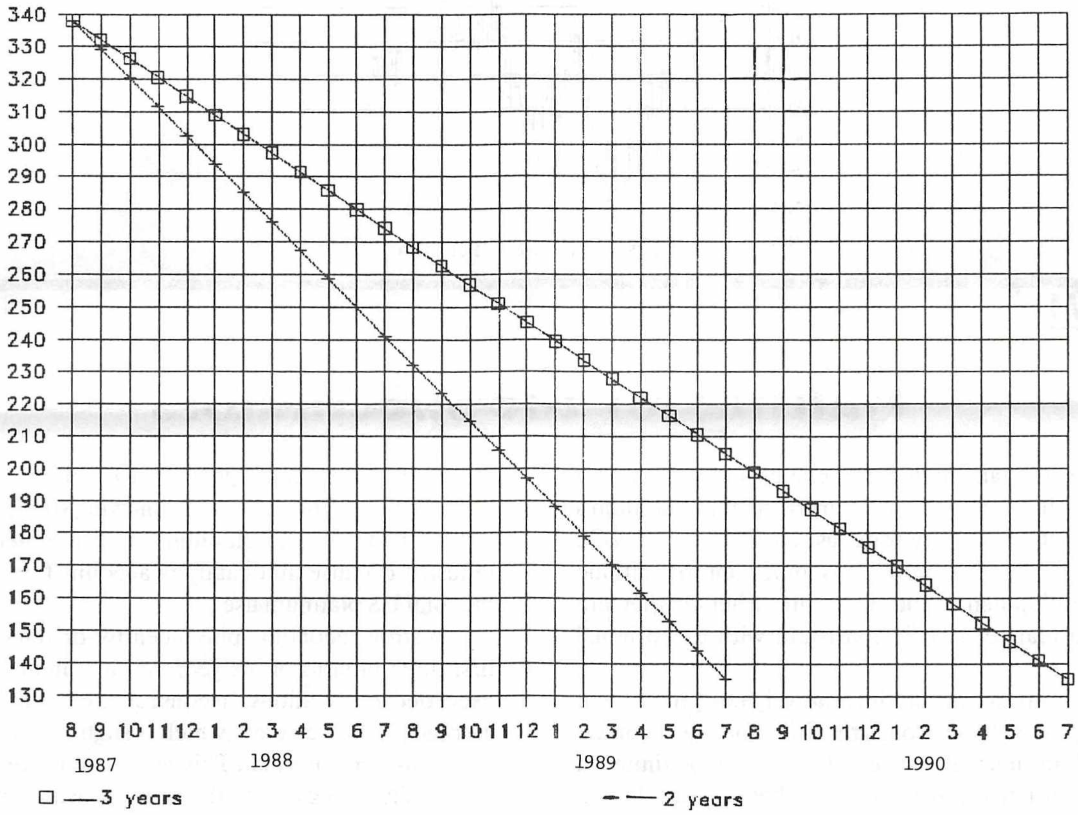


Chart 8

PROBABLE BEAR MARKET PATH
S&P 500



COPPER

Bottlenecks to reappear

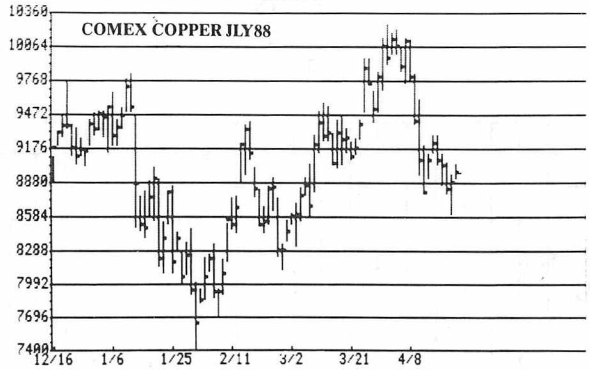
News that the US Mint's tender for 4,500 tonnes of copper had been well received and that Cerro Colorado's winning offer was for metal at a small 2.5 cent/lb. premium on May upset copper bulls and drove nearby May to a mid-week low of 89 cents/lb. Supplies were, after all, not as tight as warehouse stocks had suggested. On this subject, combined warehouse stocks (Comex and LME) declined last week to a new low, 57,619 tonnes, resuming the downtrend that prevailed through late 1987. The market was unimpressed, speculating that producer stocks outside exchange warehouses had been on the rise.

In previous issues we have posited that a very sharp backwardation, such as the one that existed in the November '87 — January '88 period, would do a reasonable job in mobilizing idle copper inventories. It therefore is not unusual to see a slight relaxation of the extreme copper tightness of last December. Backwardation can only redistribute supplies and push forward least-essential demand; it cannot create new copper nor can it permanently suffocate consumption. "Cheap" forward prices will discourage new production and encourage consumption.

If our thesis is correct, new supply bottlenecks will begin to reappear in the not-too-distant future, especially because middlemen's inventories are at less than four weeks' supply, and the main industrialized economies are still expanding with no signs of entering an early slump.

STRATEGY: *We are long July 96 and 98 calls. Outright traders bought July '88 copper, were stopped out, and reentered at a slightly lower price (see Hotline Update for April 20) with stops at 8600, good anytime.*

Chart 9



PLATINUM

Waiting for the speculators

A commodity's fundamentals rarely change course during a month. Hence, it shouldn't be too surprising that platinum's fundamentals remain as they were last month (see: *FC&CC* March 1988). This said, however, it is important to continue to monitor developments, and determine whether they are unfolding in a manner that is consistent with our original analysis.

Our primary thesis is that the relatively low yen price of platinum, coupled with the strong growth in Japanese incomes, has generated an unusually strong demand for platinum in Japan. This is of particular importance because the Japanese, even in normal times, are the dominant buyers of platinum.

During the past month, data have been reported that support our thesis. For example, Japanese platinum imports in February were 369,778 ounces. This not only exceeded our expectations but also exceeded the previous, all-time, monthly high of 282,960 ounces, which occurred in November of 1987.

To put the Japanese imports into perspective, consider that if their 1988 imports were at a rate that equalled the November-February rate, the Japanese would import about 95% of the world's projected 1988 supply.

Another point that we raised last month was that the demand for platinum jewelry (along with speculative demand for platinum bars) was causing the surge in Japanese imports. During the past month, the Platinum Guild International in Tokyo has confirmed this point, and has informed us that it has raised its forecast for 1988 jewelry demand to 996,793 ounces from 965,000 ounces (the amount we reported last month). This is equal to about 31% of the projected total world supply for 1988.

The Guild has also indicated that investor demand will probably be given some added support because of changes in the Japanese tax code. On April 1, 1988, the Japanese abolished a tax exemption that covered certain savings accounts. The thinking in Japan is that some of these funds will make their way into the platinum market.

In the United States, a recent series of favorable economic reports has given support to the thesis that we presented in "Inventories: Ps versus Qs" (*FC&CC* February 21, 1988). For the time being, the economy is showing strength. The significance of this for the platinum market centers on the auto industry because autocatalysts account for roughly 55% of the total US platinum use.

A strong economy, plus incentive-driven sales during the first three months of the year, resulted in auto sales that far exceeded expectations. In consequence, auto inventories are averaging about 58 days, which is slightly below the 60 to 65 days considered normal. This fact, as well as the fact that sales are usually strong during the spring season, caused domestic auto makers to boost their second-quarter auto production plans twice during the past month. At the time of writing, US producers expect to assemble 4.4% more autos and 7.8% more trucks in the April-June quarter than they did a year ago. This should be constructive for the platinum market.

Yet another constructive feature of the US market is the fact that platinum stocks in New York continue to drift downward (see Chart 10).

Although platinum prices have moved up since our last market letter, they have done so without the benefit of significant speculative interest. This is shown by the fact that there has been no significant change in open interest. Hence, from a technical point of view, the contracts have tended to move into "stronger hands." Again, this feature of the market is constructive.

Data from the past month support our optimistic view about the platinum market. It seems that the only thing lacking is speculative interest. Perhaps the South African sanctions bill that is making its way through the Congress will ignite a spark? If not, we remain confident that the real market fundamentals will eventually motivate the speculators.

STRATEGY: *Retain long July platinum (2)/short June gold (1) spread. Places stops at $35oz. platinum premium, on close only.*

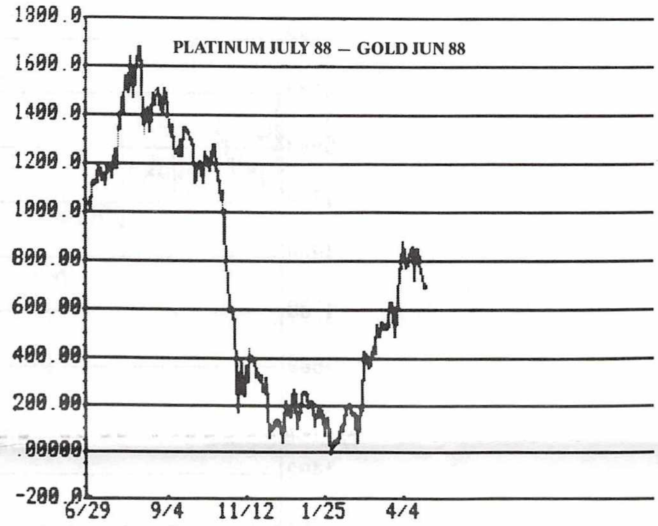
— Steve H. Hanke

Chart 10
Platinum stocks
(New York Mercantile Exchange)

Date	Ounces
May 1987*	377,800
Dec. 4, 1987	292,700
Dec. 11	292,300
Dec. 18	292,000
Dec. 24	291,000
Dec. 31	291,000
Jan. 8, 1988	291,200
Jan. 15	281,200
Jan. 22	280,900
Jan. 29	277,550
Feb. 5	247,750
Feb. 12	233,750
Feb. 19	230,850
Feb. 27	230,850
March 4	224,850
March 11	231,450
March 18	231,450
March 25	231,450
March 31	231,450
April 8	228,450
April 15	218,750
April 22	213,100

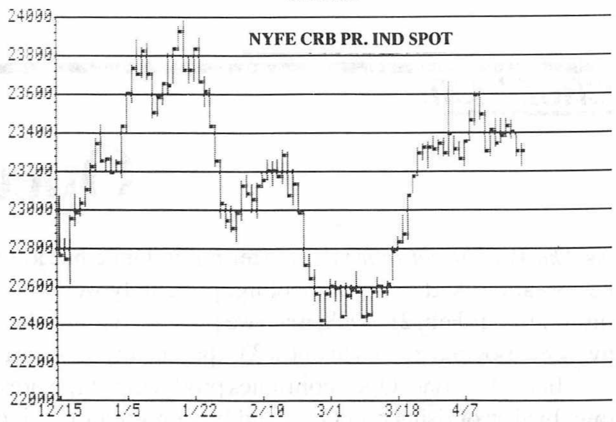
*Note: Average for the month of May, which was the high month for 1987.

Chart 11



CRB INDEX

Chart 12



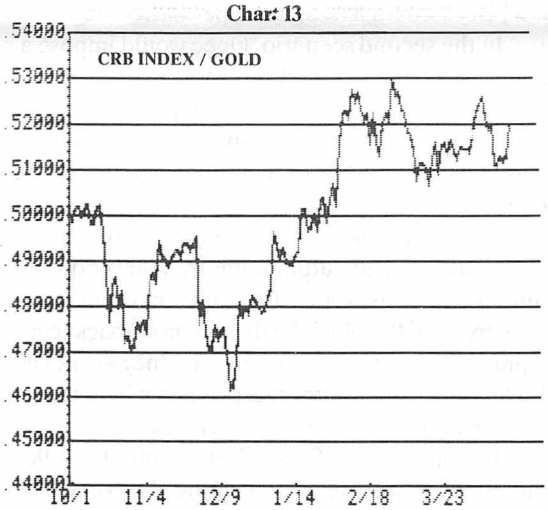
Upside breakout in the wind

The market continues to trade in a narrow, frustrating range, bound approximately by 220-240. Our advance/decline line points to an upside breakout in the not-too-distant future.

STRATEGY: *We are long, once again, CRB deferred contracts. Place stops at 22750, basis cash index, close only.*

GOLD

Chart 13



Humdrum performance

Relative behavior (*vis à vis* CRB index, Chart 13, and *vis à vis* platinum, Chart 11) remains unimpressive. We are *not* saying that gold is heading lower. We *are* saying that in all likelihood, the CRB index and/or platinum will *outperform* gold, at least in the near future.

STRATEGY: *Retain spread long 1 CRB/short 2.5 gold contracts. Raise stops to 0.49.*

Chart 14

CRUDE OIL

Opec au revoir

As *The Wall Street Journal* reporter put it, Opec has found a new weapon: setting up a meeting, preferably well into the future. In our Feb. 21, 1988, issue we presented three alternative scenarios and gave each one a 33% probability of occurring.

In the first one, Opec continues producing at the present rate. In view of rising non-Opec and Iraq production, this output level of $\pm$15 million barrels per day (b/d) is excessive. Prices would drift lower and challenge the early 1986 lows. Eventually, low prices would cause cheating, output would increase, and prices would fall to the $5 per barrel area.

In the second scenario, Opec would impose a new, lower ceiling, and prices would return to the $17-$18/barrel area. Recent events, however, have shown that the Kingdom of Saudi Arabia has no desire to recommend any cutbacks (given the alarming deterioration of their financial situation) *even if they are shared by all Opec members.*

The Saudis have to believe that despite protestations to the contrary, Opec output (cum Iraq) never drops below 16.5 million b/d consistently (because there are always enough cheaters), and therefore, further quota cutbacks can only mean, in practice, lower Saudi output. Yet, they are not averse to use the *threat* of lower output, especially when it can be done in the context of non-OPEC cooperation.

This may be the Saudis last attempt to "talk up" prices. Should the Saudis detect "cheating" by non-Opec producers (who have seen their production rise dramatically over the past five years, while Opec has exercised self-restraint), they will, in all probability, move to our third scenario.

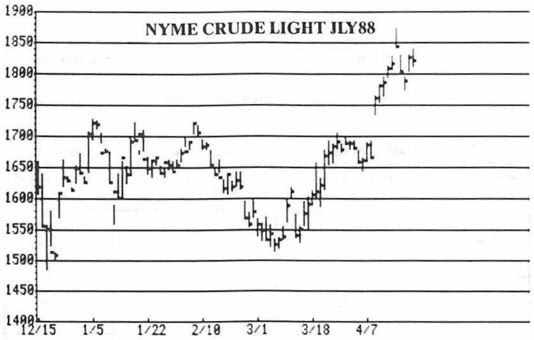
In this alternative, the Saudis and possibly a number of other Gulf producers, pull away from Opec and raise output to full capacity. No longer intimidated by Iran — whose military effort is beginning to crumble — the Saudis will choose to regain market share, and in the process a) bankrupt Iran and end the war, b) discourage new oil and gas exploration, c) reduce non-Opec supplies dramatically, and d) encourage long-term consumption gains. This strategy would spell sharply lower prices at first, and eventually some sort of equilibrium around the $7-$8 barrel mark.

It should be noted that Opec has had the benefit of a five-year worldwide economic expansion. In the next recession, whenever it comes, global demand will possibly fall off 2% to 5% per annum, for at least two years. In the context of present consumption, this represents 1-2.5 million b/d less demand. Since the entire adjustment will fall on Opec, and since the Saudis no longer wish to reduce their 4.35 million b/d quota, Opec is certain to receive the final *coup de grâce.*

STRATEGY: *Chances are fair that some sort of cosmetic accommodation will be reached with Opec and with other non-Opec nations. Whatever the outcome, time and circumstances are bringing us ever closer to our third scenario. This one spells dramatically lower prices.*

We were stopped out. Stand aside and wait for new reentering advice.

Chart 15



FRIEDBERG CAPITAL MARKETS

The Danish krone comeback

The little-known Danish economy has emerged from its relative obscurity to the limelight of some exchange and bond market stages. This increased visibility results from the improving Danish economy combined with high nominal rates of interest compared with most other European Monetary System (EMS) rates. As discussed in last November's *FC&CC*, the Dkr is moving closely with the West German deutschemark, but offers investors 350 to 400 basis points above DM rates. This obviously can be a windfall for an investor who believes in the hard currency mark for more than just the yield pickup.

In the wake of US dollar buying in early January 1988, the DM was disproportionately sold off in relation to other European currencies. While the Dkr traded down *vis à vis* the US dollar, it actually gained against the DM by approximately 1% in the same period. Perhaps 100 basis points doesn't seem like much for a currency to revalue, but within EMS this is a rare event.

We offer the following Danish krone denominated issue: *City of Stockholm 10 5/8% 10/11/91, rated AAA, currently priced to yield 9.88%

Foreign Currency Bonds

Date: April 21

We offer the following Bonds <u>subject to change without prior notice</u>: Minimum amount US $5,000 (Cdn. $7,000)

ISSUER/MTY.DATE/COUPON	BID OFFER	CURRENT ANN. YIELD TO MTY	LAST PAY DATE	NEXT PAY DATE
NEW ZEALAND DOLLAR DENOMINATED BONDS				
COCA COLA 16/06/89 18%	101 1/4 — 102 1/4	15.53	16/06/87 —	16/06/88
HONDA INT'L 20/9/89 16 3/8%	101 1/4 — 102	14.47	20/09/87 —	20/09/88
HONDA INT'L 28/5/90 16%	101 1/2 — 102 1/4	14.62	28/11/86 —	04/06/93
TOURIST HOTEL CORP. (N.Z.) 4/6/93 zero coupon	48 1/2 — 50 1/2	14.33	matures	04/06/83
BANK OF NOVA SCOTIA 15/9/89 18 1/2% RRSP eligible	102 — 103	15.64	15/09/87 —	15/09/88
WELLS FARGO (semi-ann.) 12/5/89 16 1/8%	99 3/4 — 100 1/2	16.17	12/11/87 —	20/11/88
KODAK (semi-ann.) 15/2/89 17%	100 5/8 — 101 3/8	15.57	15/02/88 —	15/08/88
TORONTO DOMINION 2/4/90 18% RRSP eligible	104 1/4 — 105	14.78	02/04/88 —	02/04/89
AUSTRALIAN DOLLAR DENOMINATED BONDS				
CAN. IMP. BANK OF COMMERCE 13/3/91 13% RRSP eligible	101 —		13/03/88 —	13/03/89
WORLD BANK 15/3/93 12 3/4% RRSP eligible	104 — 104 3/4	11.41	15/03/88 —	15/03/89
DANISH KRONE DENOMINATED BONDS				
WORLD BANK 20/11/92 9 3/4% RRSP eligible	100 1/8 —		20/11/87 —	20/88/88
STOCKHOLM 10/11/91 10 5/8%	101 1/4 — 102	9.88	10/11/87 —	10/11/88
DEUTSCHE MARK DENOMINATED BONDS				
GOVT. OF BELGIUM 29/4/96 5 1/2%	98.40 — 99.15	5.63	29/04/87 —	29/04/88
QUEBEC HYDRO 1/5/96 5 1/2 RRSP eligible	97 5/8 — 98 3/8	5.92	01/05/87 —	01/05/88
SWISS FRANC DENOMINATED BONDS				
GOVT. OF AUSTRALIA 30/10/98 5%	103 1/4 — 104	4.51	30/10/87 —	30/10/88
JAPANESE YEN DENOMINATED BONDS				
GOVT. OF CANADA 23/7/93 5 5/8% RRSP eligible	104 3/8 — 105 1/8	4.50	23/07/87 —	23/07/88

US DOLLAR DENOMINATED FLOATING RATE NOTES

ISSUER	MAT. DATE	COUPON	BID OFFER	CURRENT COUPON	
UNITED KINGDOM	7/10/92	3 mo. LIBID (quarterly)	99.81 — 100.11	6 15/16%	07/04/88 — 07/07/88
UNITED KINGDOM	24/9/96	3 mo. LIBID - 1/8 (quarterly)	99.56 — 99.86	6 5/8%	24/03/88 — 24/06/88
BANCO CENTRAL DE CHILE	12 mo.	(restructured) LIBOR + 1 1/8 (annually)	61 1/2 — 65 1/2	9.0625%	20/01/88 — 20/01/89

Chart 17

FOREIGN CURRENCY BOND INVESTMENT YEARLY PERFORMANCE
March 31, 1987 - March 31, 1988

For a Cdn$ Based Investor

Denominated in	Had you invested on March 31, 1987 in	% appreciation/ depreciation due to currency fluctuation	% appreciation/ depreciation due to price of bond interest rate fluctuaiton X currency appreciation	Nominal Coupon X currency appreciaiton	Total Return in U.S. $ *
NEW ZEALAND DOLLAR	Wells Fargo 16 1/8% 5/12/89	+ 6.89%	+ 6.89%	+ 17.24%	+31.02%
WEST GERMAN DEUTCHEMARK	Quebec Hydro 5 1/2% 1/5/96	+ 2.71%	+ 3.47%	+ 5.65%	+11.83%
JAPANESE YEN	Canada 5 5/8% 23/7/93	+10.93%	.84	+ 6.11%	+17.88%
SWISS FRANC	Australia 5% 30/10/98	+ 4.16%	+ .26%	+ 5.21%	+ 9.63%
AUSTRALIAN DOLLAR	C.I.B.C. 13% 13/?/91	- 1.77%	+ 5.63%	+12.77%	+16.63%

*Assumes that all coupons were reinvested fully.

Chart 18

FOREIGN CURRENCY BOND INVESTMENT YEARLY PERFORMANCE
March 31, 1987 - March 31, 1988

For a US $ Based Investor

Denominated in	Had you invested on March 31, 1987 in	% appreciation/ depreciation due to currency fluctuation	% appreciation/ depreciation due to price of bond interest rate fluctuaiton X currency appreciation	Nominal Coupon X currency appreciaiton	Total Return in U.S. $ *
NEW ZEALAND DOLLAR	Wells Fargo 16 1/8% 5/12/89	+13.41%	+13.41%	+18.29%	+45.11%
WEST GERMAN DEUTCHEMARK	Quebec Hydro 5 1/2% 1/5/96	+ 8.97%	+ 3.68%	+ 5.99	+18.64%
JAPANESE YEN	Canada 5 5/8% 23/7/93	+17.34%	+16.30%	+ 6.60%	+40.24%
SWISS FRANC	Australia 5% 30/10/98	+10.60%	+ .28%	+ 5.53%	+16.41%
AUSTRALIAN DOLLAR	C.I.B.C. 13% 13/?/91	+ 4.18%	+ 5.98%	+13.54%	+23.70%

*Assumes that all coupons were reinvested fully.

Chart 19

Breakeven exchange rates for US$ — based investor

This analysis shows a "snapshot" of the relationship between interest rate differentials and rates of exchange. The breakeven rate measures how far the foreign currency has to devalue (for NZ$, A$, DKr) or revalue (for DM, SF, JY) before the interest rate advantage/disadvantage is overcome by currency depreciation/appreciation. **Bond yields and rates of exchange as of**

	U.S. $	NEW ZEALAND $	AUSTRALIAN $	DEUTSCHEMARK	SWISS FRANC	JAPANESE YEN	DANISH KRONE
1 year	7.02%	Bk Nova Scotia 18½, 89 (Yields 15.64% (.615 NZ/US)**					
3 year	7.85%						Stockholm 10⅝, 91 Yields 9.88% (6.77 US/Dkr)
4 year	8.11%	Tourist Hotel 0, 93 Yields 14.33% (.564 NZ/US)	World Bk 12¾%, 93 Yields 11.41% (.686A/US)			Canada 5⅝, 93 Yields 4.50% (112.2US/JY)	
8 year	8.62%			Belgium 51½, 96 Yields 4.51% (.92 US/SE)			
10 year					Australia 5, 98 yields 4.51% (.92US/SF)		
Spot Exchange Rate	N/A	.665	.7512	1.6674	1.377	1.243	6.4055

**For example, in parentheses, since a US$ based investor would receive 862 basis points (1564 — 702) by holding the Nova Scotia 18½% bond, the NZ$ can depreciate to .615 from the present spot exchange rate of .665 NZ/US over the next 1 year for the NZ$ investment to break even with current US$ rates of interest. Assumes that bonds are held to maturity, and coupons are reinvested.

THE EXOTICS

Irish punt

Ireland has finally gotten down to serious business. The insidious rise in government current expenditures, which took total government expenditure as a percentage of GNP from 50.4% in 1980 to 56.6% in 1986, has finally been reversed, falling to 55.2% in 1987. In addition the 1988 budget contemplates a public expenditure cutback of £600 million, with the dismissal of 9,000 jobs in the civil service and a freeze on pay rises for other government employees.

Exchequer borrowing requirement will be down to £1.44 billion, or 8.2% of GNP, the lowest such number since 1977. Improvement is already on the way. For the first three months of this year, overall borrowing requirements have fallen to £536 million compared with nearly £700 million in the same period last year.

The distasteful part of this austerity plan is that over 230,000 self-employed workers, mainly farmers, will be brought into the tax net for the first time. The underground economy promises to mushroom.

Ireland has been extremely successful in attracting major multinational corporations and developing a strong manufacturing base by providing a very favorable tax rate scheme (protected until the year 2000), of no more than 10%, and other very generous grants and preferential treatments. These subsidies have obviously come at the expense of the Exchequer, but they have tended to mitigate the extremely rapid rise in manufacturing costs in Ireland. In fact, these have risen by 46% since 1980 in currency-adjusted terms as opposed to 31% in neighboring UK during the same period.

One could even argue that these very same subsidies have created structural distortion in the labor market, artificially raising real wages throughout the economy and becoming a major cause for Ireland's present 19% unemployment. In effect the tragic labor situation is the fruit of a mindless drive to industrialize at any cost.

The beneficial side to this industrialization has been the dramatic rise in exports over the past seven years, which in volume terms, have increased over 78%, far exceeding the UK's performance of a mere 25%. The trade balance surplus has been growing. The trade surplus for February 1988 reached £223.7 million, four times the level in February 1987. The current account is expected to be in surplus to the tune of $250 million, or 1.5% of GNP during 1988.

The Irish punt may be in the early stages of a turnaround, but forwards do not compensate us enough for taking the risk.

STRATEGY: *Remain neutral vis à vis the US dollar and DM.*

Chart 20

BASKET: U.S. 18%, U.K. 56%, France 11%, Germany 15%

YEAR	Irish punts per U.S. DOLLAR (PERIOD END)	U.S. 1975 =1.00	U.S. 1981=1.00	BASKET 1975=1.00	BASKET 1981 =1.00
1971	2.4441	1.1704	1.1729	1.0213	0.9066
1972	2.5018	1.0869	1.0893	1.0038	0.8911
1973	2.4522	1.0576	1.0599	0.9955	0.8837
1974	2.3390	1.0521	1.0543	0.9862	0.8755
1975	2.2218	1.0000	1.0022	1.0000	0.8877
1976	1.8062	1.1026	1.1050	1.0095	0.8962
1977	1.7455	1.0694	1.0717	1.0206	0.9060
1978	1.9195	0.9721	0.9742	1.0115	0.8979
1979	2.0475	0.8958	0.8978	1.0261	0.9109
1980	2.0580	0.8555	0.8573	1.0852	0.9634
1981	1.6167	0.9978	1.0000	1.1265	1.0000
1982	1.4222	1.0282	1.0304	1.0441	0.9269
1983	1.2482	1.0943	1.0966	0.9995	0.8873
1984	1.0871	1.2065	1.2091	0.9966	0.8847
1985	1.0656	1.2088	1.2114	0.9936	0.8821
1986	1.3415	0.9428	0.9448	0.8762	0.7779
1987 (1Q)	1.4520	0.8665	0.8684	0.8508	0.7552
1987 (2Q)	1.4817	0.8550	0.8569	0.8842	0.7849
1987 (3Q)	1.4554	0.8754	0.8773	0.8859	0.7864
1987 (4Q)	1.5635	0.8211	0.8229	0.8925	0.7923

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	844	- 5.0	-402
1971	1017	- 4.3	-602
1972	952	- 2.6	-548
1973	994	- 3.7	-604
1974	1150	- 9.7	-1092
1975	1378	- 1.4	-1066
1976	1630	- 5.1	-1240
1977	2165	- 5.3	-1074
1978	2492	- 6.7	-1799
1979	1833	- 13.4	-3471
1980	2194	- 11.5	-5081
1981	2070	- 6.1	-6849
1982	1226	- 10.9	-6683
1983	1116	- 7.2	-5768
1984	979	- 6.1	-4132
1985	1321	- 3.5	-2776
1986	1347	- 2.0	-2004
1987	2970	+ 1.1	- 742

Chart 22

Spot	1 Month	3 Month	6 Month	12 Month
1.5955-1.5970	1.5970-1.5995	1.5880-1.6010	1.5980-1.6010	1.6010-1.6065

FOREX RATES & UPDATE

Currency	*Spot*	*3-Month*	*12-Month*	*Comments vis à vis US$*	*Comments vis à vis DM (Spot DM: 1.6750)*
*Australian dollar	.7568-.7573	.7496-.7504	.7278-.7298	Remain long, raising stops to .7400, basis cash, good anytime	Neutral
Belgian franc	34.94-34.97	34.81-34.80	34.36-34.54	Remain long	Neutral
*Danish krone	6.4250-6.4300	6.4545-6.4655	6.5225-6.6525	Remain long	Buy
*Dutch guilder	1.8753-1.8763	1.8601-1.8615	1.8121-1.8146	Remain long	Remain short
Greek drachma	133.95-134.00	136.45-138.50	143.45-151.50	Remain short	Remain short
Hong Kong dollar	7.8110-7.8120	7.7620-7.7660	7.6460-7.6720	Remain short	Neutral
Italian lira	1242-1244	1252-1256	1279-1288	Remain long	Remain short
Kuwaiti dinar	.27315-.27335	.27170-.27233	.26750-.26929	Neutral	Remain short
Malaysian ringgit	2.5685-2.5695	2.5465-2.5495	2.4885-2.4995	Neutral	Neutral
New Zealand dollar	.6735-.6745	.6585-.6605	.6285-.6345	Neutral	Neutral
Norwegian krone	6.1575-6.1625	6.2575-6.2665	6.5250-6.5425	Remain long	Neutral
*Portugese escudo	136.50-136.90	138.00-139.50	141.50-144.90	Remain long	Buy
Saudi Arabian riyal	3.7500-3.7510	3.7465-3.7430	3.7430-3.7500	Remain short	Remain short
Singapore dollar	2.0025-2.0035	1.9848-1.9863	1.9325-1.9385	Neutral	Neutral
Spanish peseta	110.55-110.65	111.40-111.60	113.35-113.85	Remain long	Neutral
Swedish krona	5.8710-5.8760	5.9085-5.9165	5.9865-6.0040	Remain long	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, March 22: No changes or new recommendations.

Flash update, Thursday, March 24, 11:20 a.m.: The copper market is turning up once again and is likely to challenge former highs. Given the market's unusual volatility, we prefer using call options to establish our long position. Purchase July 96 or July 98 copper call options at market. Outright long positions must be able to risk a close below 80 cents, basis July.

Friday, March 25: 1. Sell June Nikkei Dow, traded on the SIMEX, at market. Place stops at 26,800, basis cash index, good anytime.
2. Tighten stops on short June T-bond positions to 92.20, close only.
3. As of yesterday's flash update, we recommended the purchase of July 96 and 98 copper call options. Buyers of outright positions must be able to risk 80 cents, basis July, on a closing basis.
4. Holders of outright long positions in copper as per our recommendations on Thursday, March 24, should raise stops to 90.20, on July close only.

Tuesday, March 29: As there are no new recommendations, I will repeat the message of Friday 25. (See Friday, March 25, comments.)

Thursday, March 31: One change: tighten stops on short June T-bonds position to 9116 good anytime.

Flash update, Tuesday, April 5, 10:35 a.m.: Liquidate long positions in SF, DM, and JY, as well as all EMS currencies at market. Also accept profits on September 270 S&P puts.

Tuesday, April 5: As per our flash update of this morning, we have liquidated long positions in SF, DM, and JY, as well as all EMS currencies at market. Also accept profits on Sept. 270 S&P puts. One other recommendation: tighten stops on short June T-bond positions to 90.12, good anytime.

Thursday, April 7: 1. As of Tuesday's update, we liquidated long SF, DM, and JY positions, as well as all EMS currencies.
2. As of Tuesday's update, we accepted profits on Sept. 270 S&P put options.
3. We were stopped out today profitably of short June T-bond positions at 9012, as per our Tuesday's recommendations.

Tuesday, April 12: No new recommendations as of today. Therefore, I will repeat our last broadcast of April 7th. (see Thursday, April 7, comments.)

Flash update, Thursday, April 14, 9:00 a.m.: Buy JY, SF, DM, BP, and all EMS currencies at market.
Place initial stops at 7840, close only, basis June JY. As well, liquidate all other currency positions if the June yen breaks 7840, on close.

Friday, April 15: There are no changes or new recommendations. I will now repeat our latest message, a flash update at 9:00, Thursday, April 14. (see Thursday April 14, comments).

Tuesday, April 19: There are no changes or new recommendations. I will now repeat our latest message, a flash update at 9:00 a.m., Thursday, April 14. (See Thursday April 14, comments.)

Flash update, Wednesday, April 20, 2:00 p.m.: We have two messages:
1. Reinstate short positions in July crude oil at market, risking 1830, good anytime.
2. We are long July copper call options and have been stopped out of outright longs. We now advise purchasing July copper at market, risking 8600, good anytime.
Obviously, if tomorrow, April 21, opening is below 8600, disregard this recommendation.

Sunday, April 23: We apologize for no new taped message on Friday. There are no changes. I now repeat our last message, containing specific recommendations, which was announced Wednesday at 2:00 p.m.:
1. Reinstate short positions in July crude oil at market, risking 1830, good anytime.
2. We are long July copper call options and have been stopped out of outright longs. We now advise purchasing July copper at market, risking 8600, good anytime.

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