

FRIEDBERG'S

COMMODITY & CURRENCY COMMENTS

Friedberg Commodity Management Inc.



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1989: The year in review

As we predicted in February, interest rates soared to record all-time highs of 30% overnight. Of course, we were there. The international equity markets collapsed in "it's only the beginning" fashion, and actually were recording negative numbers. Our suggestion to be outright short as well as to purchase puts made us a second runner up for *Time Magazine's* traders of the year award.

Inflation truly was real *and* imagined: An unpleasant choice was real, and the Fed's dilemma was only imagined.

The global debacle in wheat left farmer Billy Bob with the only remaining wheat stock, while we were long futures and calls.

Our patience once again showered us with profits. We were the only kids on our block who were short the Saudi Arabian riyal, which devalued daily as the newest oil minister was quoted as saying, "I should have driven a V8."

We devoted two cover stories to the Canadian dollar's plight, and that too is relegated to history. In other words the answer to the query "When will they ever learn?" is "What was the question?"

And finally, every financial institution in America had an involuntary holiday as we penned prolific prose about the banking mess. Actually, as it happens, 1989 was a successful, albeit moderately forgettable, year for us. Anyway, we still have some awards to give out, as we do every year. So here goes...

Come-back Award

Our performance in the stock market, for all our in-depth analysis, fell somewhere close to the average mark. At the start of the year, we were long S&P puts which expired worthless. We turned aside to see if we would have better luck spreading, and we found ourselves short the Kansas City Value Line and long the S&P Index, as well as long Treasury bonds and short the S&P Index. Both spreads ended up on the editor's cutting-room floor.

By February, we charted a course short again, which ended on the sidelines. By April, we were again trading the beast from the long side outright as well as via options. In June, this trade resulted in hefty profits. When it was last seen, we were buying put options in September, putting us in a good position for the next big market move — which is *down*. Stay tuned!

Best-Box-Office-Draw-for-a-Remake Award

Trading sugar through the year was to our definite advantage. And although we were stopped out each time, we traded with prudent and reasonable stops, netting a tidy profit four out of five trades. (Outstanding box office success.)

High-Drama-Without-a-Climax Award

The good news is that we hardly mentioned the Saudi Arabian riyal this year except for two words on the back cover of every letter, which states our undying faith in the eventual outcome: "Remain short."

The bad news: We remained short. Stay posted.

Remake-of-a-Classic Award

During the first half of 1989, we repeated recent history by shorting our nemesis, crude oil, twice. Twice we were stopped out. We turned our energies to put options, which expired worthless. The real, and we hope nonrecurring, nightmare came in July, when we rather sarcastically thanked Harvard University for predicting a \$50/barrel price by the year 2000. As good contrarians, we were grateful and short again... until September. We liquidated our short position and put options and could not quite get used to the feeling of our tails between our legs. The real reason we have not traded crude

In this issue

- 3 The Economy**
Ease over.
- 4 Canadian Dollar**
On the consequences of Canada's squeeze.
- 5 Currencies**
Fun and games in cross trading.
- 6 Stock Indexes**
Bear in full swing.
- 7 Friedberg Capital Markets**
Alliant Computer convertible bond update.
- ★ **Friedberg's LDC Debt Comments**
Special pull-out section

With contributions by Albert D. Friedberg, Dr. Steve H. Hanke, Daniel A. Gordon, and Michael D. Hart.

since July is that we were waiting for someone at Harvard University to say...you're welcome.

Best-Short-Subject Award

We commenced the year being long copper and very profitably rolled forward, before being compensated once again.

Epic War Classic

Act one: Platinum rumbled in February, and we heard the call. To the long side we ran. (Fade to black.)

Act two: Again two months later, the ground moved, and we took up the bullish position. (Fade to black.)

Act three: It was May this time when we jammed an army boot in our mouth by announcing that platinum on the long side had "a profit potential of more than 100/oz." (Wait for laughter.)

Act four: We shall rearm and attack by spread, going long two platinum against the sale of the one gold. (Fade to the sound of "Elvis has left the auditorium").

Bad-timing Award

Wednesday morning, October 25, 1989, we decided to take hefty profits on our short sterling cross. As carmic synchronicity would have it, Wednesday afternoon, October 25, 1989, was also the day that Nigel Lawson chose to resign. Timing is everything, bad timing is 3% less.

Best Performer

Our January recommendation to buy the yen, DM, and SF, because although we were dollar bulls, we were "reversing on a dime whenever the weakness in the economy perception disappeared." This turned out to be the only unprofitable currency trade we made all year, and we soared higher and higher toward a grand finale.

We fearlessly sold the currencies in April and claimed our pound of flesh in May. One short week later we were back on location on the short side of the JY, SF, and DM. These currencies received equal billing in our recommendations, but we stated ever clearly our bias for the yen. As it progressed, we got nervous about protecting our profits, and by November we hedged our short JY with the purchase of SF. Both sides of the short are shining stars.

In July and August we suggested two new spread positions. We purchased 4 DM and sold 3 JY and bought 3 DM against the sale of 2 BP respectively. Our sterling cross was liquidated at the end of October, and the results were outstanding.

Where-Are-They-Now Award

At the beginning of 1989 we recommended being long wheat,

soybeans, and soymeal. We even further promoted our wheat position two months later. All these trades were stopped out before they reached the box office. Wheat married an accountant in Nebraska and runs a meager auto body business. Soybeans and soymeal joined forces and switched to purely period movies as extras.

Much-Ado-About-Nothing Honorarium

We promoted two cover stories about the intrepid Canadian buck, and talked at length about paying high and rising rates of interest, raised levels of taxation, the disastrous April budget, looming foreign exchange crisis, fiscal deficits still growing faster and fiscal capacity to repay, debt charges increasing...and fiscal profligacy (whatever that was). We recommended trading outright short as well as purchasing one-year put options. The shorts were of course stopped out, and the options were left waiting in the wings for curtain calls.

Scalpers' Corner

In September we purchased T-bill and T-bond calls, and took quick profits on both of these by November. It simply wasn't that inspiring after our weighty comments.

B-Rated Flop

Our analysis of Euro-rates and Eurodollar futures were a little off the mark, and although we finessed our position, we did nothing worth talking about in this trade.

Continuity Award

The starworthy CRB/gold spread insisted on staying with us almost all year and was finally stopped out mid-November. This spread made quite a bang at the box office, but never really received the notoriety it deserved. This one spread was among the most profitable trades of the whole year.

Curtain Call/Reprise

When it's all said and done, and swept into the pages of someone's dusty ledger, 1989 was in some ways typical of all years in our business. We had trades that were better off not made (short crude, short Canadian dollar), trades that brought us profits but not spectacular ones (long sugar, short sterling cross), and trades that made up for all our shortfalls and more (selling JY, DM, SF, and all EMS currencies... and later hedging by buying the SF and doing a short JY/long DM spread). In other words, in the business of speculation/trading, after a period of time it is the rule and not the exception that *one* trade makes the period so profitable, and all bad forecasts forgivable. Let's hope to be in that one trade next year.

THE ECONOMY

Ease over

In past issues of *FC&CC*, we have written about Professor Knut Wicksell's brand of economics. That was necessary because the Fed is using a neo-Wicksellian apparatus to formulate monetary policy.

To evaluate the future course for Fed policy, it is instructive to look at yield curves and what they imply about economic growth. Recall that yield curves are part of the Fed's neo-Wicksellian apparatus (the others are commodity prices and foreign exchange rates). Hence, an analysis of yield curves should provide insights into the Fed's thinking and future policies.

For the period 1990.1 to 1991.1, the economy will grow at a weak 1.65% rate.

This conclusion is based on our analysis of yield curves. When short rates are below long rates, yield curves are positively sloped, and market participants anticipate an economic expansion, whereas they anticipate a slowdown when yield curves are negative. Indeed, negative spreads have preceded the last four recessions.

To put some meat on these general statements, we have developed a yield curve equation for the US. As Chart 1 shows, GNP predictions based on the yield curve equation have performed well. The yield curve equation indicates that when three-month rates in the most recent quarter equal 10-year yields (the yield curve is flat), the US economy over the next year will grow on a year-over-year basis at a 1.89% rate (see Chart 2). As short rates move higher than long yields, the economy will grow at a rate less than the 1.89% rate.

Alternatively, as short rates fall below the long yields, the economy will grow at a rate that exceeds the 1.89% rate. As a rough approximation, each 100 basis point change in the spread between short rates and long yields will require about a 1.0% adjustment to the 1.89% GNP growth rate. In consequence, if short rates exceed long yields by 100 basis points, growth in the next year would be about 0.89%. If short rates were less than long yields by 100 basis points, growth would be about 2.89%.

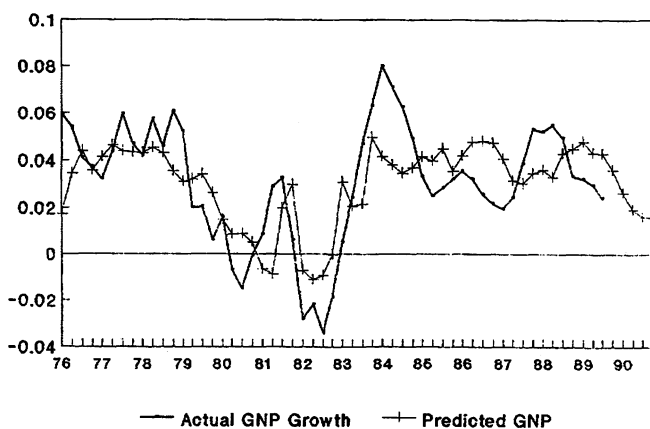
The three-month rates in 1984.4 were 8.1339% and 10-year yields were 7.9033%, so the yield curve was negative by 23 basis points. Hence, the base growth rate of 1.89% (with a yield spread of zero) must be reduced by 0.24%. This adjustment yields our 1990.1-1991.1 forecast for GNP growth of 1.65% (see Chart 2).

IMPLICATIONS: As the economy continues to slow and moves toward a 1.65% growth rate, the neo-Wicksellians at the Fed will relax short rates ever so slightly, if at all. The low end of acceptable year-over-year GNP growth for the Fed is 2.5%. (Note that this could be changed in February, when the Fed submits its annual "Monetary Policy Report to Congress.") To achieve this minimum target, all the Fed would have to do is allow the yield spread to become slightly positive at about 60 to 70 basis points. Given that the current spread has recently been positive at about 50 basis points, the Fed will probably be reluctant to ease much more than it already has.

— Dr. Steve H. Hanke

Chart 1

Real GNP Growth (1976.1 - 1991.1)
Yield Spread Model



$$\text{ChGNP}(t+1:t+5) = a + b \cdot Yd(t)$$

Chart 2

US Yield Curve Equation Calculations

1. Yield curve equation estimated with 1976.1-1989.3 data:

$$\text{Change in GNP next year} = 0.0189 + [1.1209 \cdot \ln(1 + 10\text{-year yield} / 1 + 3\text{-month rate})]$$

This equation explained about 46% of the variance in GNP over the 1976.1-1989.3 period (see Chart 1).

2. To make a forecast of GNP from the 1990.1-1991.1 period, calculate the yield spread for 1989.4: average 3-month rate was 8.13% and average 10-year yield was 7.90%; $\ln(1.0790/1.0813)$ is -0.0021; and substituting this into our yield curve equation is

$$\text{Change in GNP (1990.1-1991.1)} = 0.0189 + [(1.1209)(-0.0021)] = 0.0165 = 1.65\%$$

CANADIAN DOLLAR

On the consequences of Canada's squeeze

We last analyzed the Canadian economy in the June and July issue of *FC&CC*. Since those reports, Mr. Michael Wilson's fiscal policy has remained lax and anti-supply side. Conversely, Mr. John Crow has become one of the most resolute central bankers in the Western World, and the Bank of Canada has applied a steady squeeze policy. In consequence, Canadian short rates have remained relatively high, the yield curve has remained decidedly negative, "hot money" has continued to pour into Canada, and the Canadian dollar has remained strong.

The "hot money" has financed "excessive" consumption and a relatively large current account deficit. Indeed, foreign capital has been sucked in at a record rate, reaching 18% of available domestic savings. To facilitate this financing, the Canadian Treasury-bill market has ballooned, and is now the world's third largest.

These trends cannot continue. Mr. Crow will ultimately face an unmanageable set of economic factors that will force an unwarranted hard landing.

Flagging economy

A flagging economy is the most likely factor that will force Mr. Crow's hand. Indeed, the Canadian economy has already begun to decelerate, and we anticipate that over the next year (1990.1-1991.1), the economy will register a year-over-year negative growth rate of -0.29% (see Charts 2 and 3).

Our forecast is based on the fact that yield curves determine, in large part, the course of the economy. When three-

month rates in the most recent quarter equal 10-year yields (the yield curve is flat), the Canadian economy will grow on a year-over-year basis at a 2.56% rate (see Chart 3). When monetary policy is squeezed, and the short rates exceed the long yields (the yield curve and yield spreads are negative), the economy over the next year will grow at a rate less than 2.56%.

The magnitude of the slowdown caused by the negative yield spreads depends on the intensity of the monetary squeeze. As a rough approximation, each 100 basis-point increase in the negative spread reduces the GNP by about 1.0%. Since the yield spread in 1989.4 was -254 basis points, the base growth (with a yield spread of zero) of 2.56% must be reduced by 2.85%. This adjustment produces our estimated growth of -0.29% from 1990.1 to 1991.1.

— Dr. Steve H. Hanke

STRATEGY: Grim economic prospects have put the Bank of Canada in a difficult position. It can't lower rates without triggering a massive sell-off of the currency (witness the 3.3% drop in the Canadian dollar in the last 10 days), and it shouldn't lower the rates in view of the widening current account deficit and the explosive recent growth in money supply. And yet, the clamor for lower rates will intensify as the economy skirts (and dips) into recession.

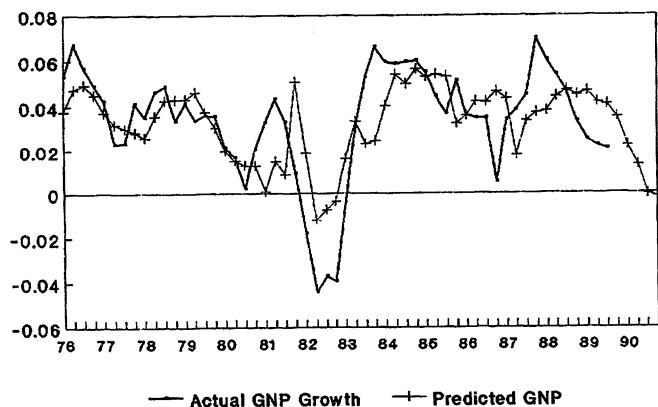
Interest rates have recovered most of the 25 basis-point drop; the dollar's drop has been overdone. Retain puts but wait for a better outright selling opportunity.

Chart 3
Canadian Yield Curve Equation Calculations

1. Yield curve equations estimated with 1976.1 - 1989.3 data:
Change in GNP next year = $0.0256 + [1.2438 \cdot \ln(1 + 10\text{-year yield} / 1 + 3\text{-month rate})]$
This equation explained about 42% of the variance in GNP over the 1976.1 - 1989.3 period (see Chart 4).

2. To make a forecast of GNP from the 1990.1 - 1991.1 period, calculate the yield spread for 1989.4: average 3-month rate was 12.21% and average 10-year yield was 9.67%; $\ln(1.0967/1.1221)$ is -0.0229; and substituting this into our yield curve equation is
Change in GNP (1990.1 - 1991.1) = $0.0256 + [(1.2438)(-0.0229)] = -0.0029 = -0.29\%$

Chart 4
Canadian Real GNP Growth (76.1 - 91.1)
Yield Spread Model



$ChGNP(t+1:t+5) = a + b \cdot Yld(t)$
89.4-91.1 are out of sample forecasts

CURRENCIES**Fun and games in cross trading**

Ever since the fun went out of trading dollars — perhaps it became too politicized or perhaps the market became too efficient given the huge attention it attracts — intelligent traders have shifted their sights to cross-trading.

Cross-trading — yen against marks, marks against Swiss francs or pounds, or any combination that respects the basic rule that the currencies in question must be of countries that are trading partners (Greek drachmas versus South Korean won's will, clearly, not do) — is far more sensitive to "true fundamentals" and far less affected by "bandwagon psychology" than dollar trading. As our 1989 review suggests, one such trade, long DM/short yen (see Chart 6) was responsible for turning a lackluster year into a winner. In between, we refined the basic cross with two other crosses: substituted DM for Swissies and lire, adding salt and pepper... and more profits.

What of the yen, our short leg? Last month we suggested that sooner or later and probably sooner, the Bank of Japan would take steps to rein in the country's monetary explosion. We wondered whether the new governor, Mr. Yashusi Mieno, would have the courage to tighten policy in the face of serious financial repercussions. We said, "if, as we suspect he is, then Japanese interest rates are likely to soar in coming months, setting off a collapse in real estate values and stock prices but strengthening the yen *vis à vis* the US dollar and perhaps even the European currencies." We concluded by saying that we were maintaining the short leg of the cross trade but that being concerned, we would be monitoring closely the Bank of Japan's interest rate policy.

In the last 30 days since publication of the December *FC&CC*, interest rates in Japan have risen rather dramatically — but it was *not* the doing of the Bank of Japan. The benchmark 10-year Japanese government bond collapsed in price to yield as high as 7.03%, later to recover to yield 6.48%, still an impressive spike in yields of 110 basis points in the short span of four weeks.

The inverse yield curve, which stood at a four-year peak of 140 basis points (10-year government less three-month Euro-yen) in late 1989, has flattened to a mere 50 basis points, an indication that a) the Bank of Japan has become *less tight* and

b) the market has become quite anxious about (asset) inflation.

The tug of war between the MOF and the BOJ continues.

The Ministry of Finance remains extremely sensitive to falling stock and real estate prices, believing that it can engineer a soft landing via moral suasion and the already-achieved rise in interest rates. The Bank of Japan, on the other hand, knows there is no tearless way of ending asset inflations. While the sharp recent fall in stock prices is likely to strengthen, *temporarily*, the hand of the Ministry of Finance, the falling bond market and the soaring money supply (M2 up 10.6% year-on-year) will, eventually, unnerve the Bank of Japan sufficiently to force it to put on the brakes. A genuine shift to a tighter monetary stance, however, may still be months away.

The other two cross trades are simpler to analyze. The long Swiss/short DM spread is predicated on the historically strong anti-inflationary basis shown by the Swiss National Bank. In an effort to combat rising inflation (an annual 5% year-on-year rise in consumer prices) and a deteriorating exchange rate, the Swiss National Bank has raised three-month Euro-Swiss rates to 9 $\frac{7}{8}$ %, a full 150 basis points higher than Euro-DM. While the Bank may allow for a slight *real* appreciation of the DM, given the recent events in Eastern Europe, we believe that the cross will nevertheless settle around 85 SF per 100 DM from the present 88.50 SF/DM and from our initial entry point of 91.50 SM/FM. You get paid for waiting, as points are in our favor.

As we explained in our Hotline of Jan. 9, the Italian lira was devalued relative to the ECU by 3% while foregoing the wide 6% EMS band for the standard 2.25% band. In the process, the lira strengthened, as we had expected, moving from LIT 748-750/DM to Friday's closing of LIT 743.50/DM. At this time, the lira is at the top of the EMS, where we expect it to stay for some time. Here again, the higher interest rates in lire makes the trade attractive.

STRATEGY: *Remain long Swiss franc/short DM and long lire/short DM. A corollary to these two spreads is that our basic long DM/short yen spread has turned into a long Swiss franc/short yen and /or long lire/short yen spread.*

Chart 6 – March DM/March JY

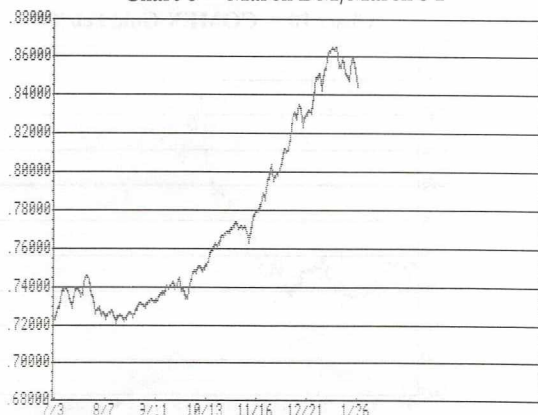
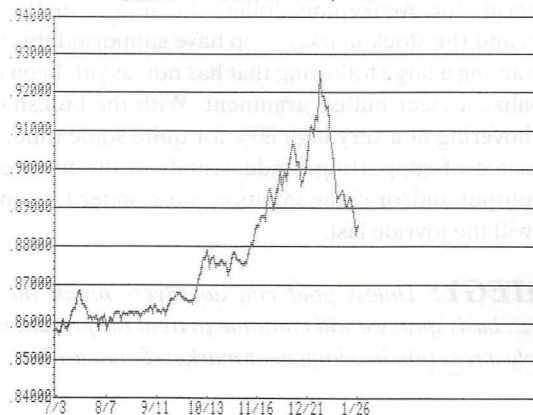


Chart 7 – March CM/March SF



STOCK INDEXES

Bear in full swing

It is a feature of bear markets that earnings have to be continuously revised downward (the opposite is true in bull markets). This phenomenon is a product of the rosy expectations associated with many years of a bull market. As one example, the "bottom-up" consensus of analysts polled by Zacks, an institutional research firm, was for an 8.9% gain in fourth-quarter S&P 500 profits as recently as last October. By early January, these estimates had been shaved to about 1.5% and while fully 74% of analysts polled by Zacks have revised downward their 1990 earnings estimates, they still believe that the S&P 500 will see a 14% gain for 1990.

1990 first-quarter earnings (10% year-on-year), a modest 2% drop in the second quarter, and a strong recovery in the last two quarters. If analysts are unable to predict even three months ahead — witness the October 1989 to January 1990 revisions — how credible can they be six to 12 months ahead?

Recession or no recession, corporate profits — the lifeblood of any capitalist economy and the force guiding Wall Street capital allocation — is in a clear and ominous downtrend.

At the same time, as our "Ease over" article points out, interest rates in the US are unlikely to ease much more for quite some time (and if Japanese interest rates continue to rise, they are likely to force US rates higher), removing the only prop under stock prices.

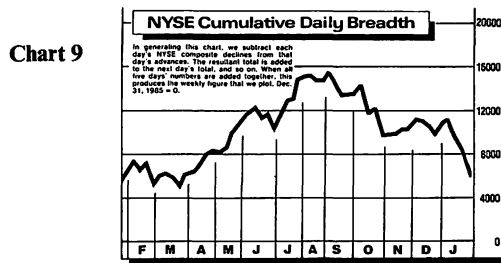
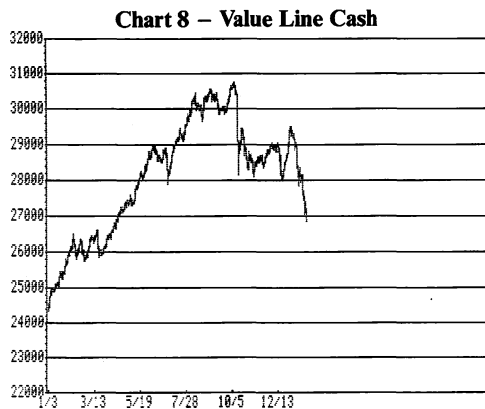
Wall Street's bear market is in full swing. A look at two measures of breadth (Charts 8 and 9) should convince even the hardest bull. Also a reading of prevailing sentiment reveals that we are far from a bottom. We pointed out last month that odd-lot short sales were quite low; remarkably, despite the 200-point drop in the Dow Jones Industrials, odd lot short sales remain unusually low, averaging under 10,000 shares per day.

Investors Intelligence reports that, finally, there were more bears (44.6%) than bulls (39.3%) with 16.1% looking for a correction, but the margin is hardly overwhelming and, after all, we are in a bear market!

Lastly, earnings projection, as we pointed out above, continue to reflect an unrealistic and unhealthy degree of

optimism (14% to 17% gain in earnings for the S&P 500 during 1990). Only downward revisions can follow such buoyant expectations. And, by definition, downward revision spells lower prices.

STRATEGY: Last month we stated that "the next major move is DOWN and it will be BIG." So far we are on target — and it is only the beginning. Retain short positions in March '90 Value Line. While at-the-money implied volatilities in the S&P 500 options have risen to 23.5% — a relatively high reading — we advise retaining previously purchased puts. Even sophisticated option writers have not grasped as yet the nature of the upcoming "air-pocket."

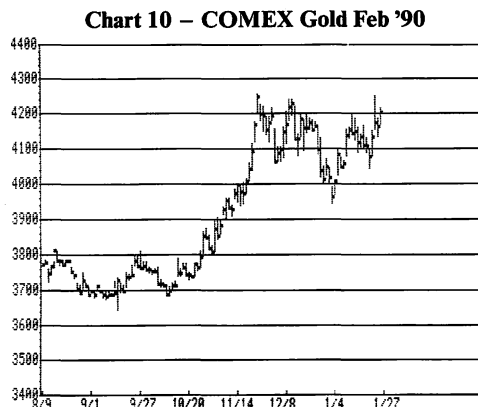


GOLD

Neither here nor there

Short term, the weakening dollar, the unrest in Eastern Europe, and the stock market drop have supported this market, attracting a large following that has not, as yet, been able to verbalize a clear bullish argument. With the bullish consensus hovering at a very high 80% for quite some time, and the absence of supporting fundamentals in the manner of falling output and/or rising inflation, we wonder how much longer will the joyride last.

STRATEGY: Unless gold can decisively break through \$435/oz., basis spot, we will continue to treat the present more as merely a reaction in a long bear market. Stand aside.



FRIEDBERG CAPITAL MARKETS

Alliant Computer convertible bond update

Wall Street analysts expect that the company's new super-computer, the Fx-2800, will be available within three months. The product is priced from \$500,000 to \$2 million and carries a significant profit potential for the company.

We currently offer Alliant Computer's 7¼% (semi) 15/5/2012 convertible bond at \$48¾, to yield 16.07%.

New Zealand dollar bonds	5%
US dollar high-yield convertible bonds	20%
Argentina Bonex	5%
US dollar floating-rate notes	35%
US zero coupon bonds	15%
Danish krone bonds	20%

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Chart 12 – Foreign Currency Bonds

Date: January 25, 1990
We offer the following bonds subject to change without prior notice:
Min. a/c US\$5000.

PAY ISSUER/INT./DATE/COUPON	BID	OFFER	CURRENT ANNUAL YIELD TO BUY	LAST PAY DATE	NEXT PAY DATE
CANADIAN DOLLAR DEPRECIATED BOND	99.90	- 100.10			Matures-01/02/90
GOVERNMENT OF CANADA (semi annual)			Money market		
01/02/90 12 1/4%					
NEW ZEALAND DOLLAR DEPRECIATED BOND	99 3/4	- 100 1/2	13.04%	02/04/89-02/04/90	
TORONTO DOMINION BANK					
02/04/90 10% RESP eligible					
TOURIST HOTEL (N.Z.)	63 1/4	- 64	14.29%	matures	-04/06/93
04/06/93 zero coupon					
AUSTRALIAN DOLLAR DEPRECIATED BOND					
CORPORATE BANK OF AUSTRALIA	98 3/8	- 99 3/8	14.13%	01/07/89-01/07/90	
01/07/94 14%					
WORLD BANK	98	- 99	13.13%	15/03/89-15/03/90	
15/03/93 12 3/4% RESP eligible					
CAN. IMP. BANK OF COMMERCE	96 1/2	- 97 1/2	15.51%	13/03/89-13/03/90	
13/03/91 13% RESP eligible					
DANISH KRONER DEPRECIATED BOND	98 7/8	- 99 5/8	10.81%	10/11/89-10/11/90	
STOCKHOLM					
10/11/91 10 5/8%					
FINNISH MARK DEPRECIATED BOND	89 1/4	- 90 1/4	13.27%	14/04/89-14/04/90	
KUOPIS					
14/04/93 9 3/8%					
FINNISH MARK DEPRECIATED BOND	88	- 89	7.78%	01/05/89-01/05/90	
QUEBEC HYDRO 5 1/2%					
1/5/96 RESP eligible					
EUROPEAN INV. BANK 5 1/2%	91 3/4	- 92 1/2	8.01%	09/08/89-09/08/90	
9/8/93					
FINNISH MARK DEPRECIATED BOND	88 3/8	- 89 3/8	6.64%	30/10/89-30/10/90	
GOV. OF AUSTRALIA 30/10/90 9%					
JAPANESE YEN DEPRECIATED BOND	98 7/8	- 99 5/8	5.73%	23/07/89-23/07/90	
GOV. OF CANADA					
23/07/93 5 5/8% RESP eligible					
U.S. DOLLAR DEPRECIATED FIXED CONVERTIBLE BOND					
PACIFIC SCIENTIFIC 7 3/4% 15/06/03(semi)	09 1/4	- 71 1/4	12.52%	15/12/89-15/06/90	
CV \$839.75 p/ah					
SUNSHINE MEDICAL INC. 7.25% 26/6/96	72	- 77 1/2	12.54%	26/06/89-26/06/90	
CV \$817 5/8 p/ah					
ALLIANT COMPUTER 7.25% 15/05/12(semi)	46 3/4	- 48 3/4	16.07%	15/05/89-15/11/90	
CV \$839.75 p/ah					
COOPER CO'S. 10 5/8% 01/03/05(semi)	66 3/4	- 68 3/4	16.88%	01/09/89-01/03/90	
CV \$827.45 p/ah call in 1995 \$100					
SIEMENS ELECTRONICS 5.5% 1/3/12 (semi)	43 1/2	- 45 1/2	13.53%	10/06/89-10/06/90	
CV \$839.50 p/ah					
U.S. DOLLAR DEPRECIATED ZERO COUPON BOND	47 3/8	- 48 1/8	8.97%	matures	-06/08/98
KINGDOM OF DENMARK					
6/6/98					
U.S. DOLLAR DEPRECIATED FIXED RATE BOND	97.90	- 98.65	8.17%	09/12/89-09/12/90	
ALBERTA 7 3/8%					
9/12/91 RESP eligible					
SOFTWARE CORP. 10 7/8% 1/11/89 (semi)	-	-	-	-	N/A
U.S. DOLLAR DEPRECIATED FLOATING RATE BOND					
UNITED KINGDOM 24/9/96	99.08	- 100.18	8 1/4%	28/12/89-28/03/90	
3 mo. LIBID-1/8 (qly)					
REPUBLIC OF ITALY 30/4/93	99.35	- 99.75	8 4/8%	31/10/89-31/01/90	
3 mo LIBOR(qly)					
REPUBLIC OF PORTUGAL 8/12/93	99.78	- 100.08	8.2375%	08/12/89-08/06/90	
6 mo LIBOR + 5 B.P.(semi)					
DANISH CROWN 16 CILLE 20/1/94	62	-	10 11/16%	22/01/90-22/01/91	
12 mo LIBOR + 13/16 (annual)					
** current yield					
ARGENTINA BONEX series 82	79	- 80 1/2	** 8.3654%	15/08/89-15/02/90	
6 PD LIBOR (semi)			** 36.85%		
*** 1BR					
Annualized 1/12 principal/year					

For further information and current prices please call:
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Chart 11
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. **January 25, 1990.**

	U.S. \$	NEW ZEALAND \$	AUSTRALIAN \$	DEUTSCHEMARK	SWISS FRANC	JAPANESE YEN	DANISH KRONE	BRITISH POUND
2 year	8.21%		CIBC 13% 13/3/91, yields 15.51% (.667 A\$/US)				Stockholm 10%, 10/11/91, yields 10.81% (6.83 US/DK)	
3 year	8.29%	Tourist Hotel 0% 4/6/93, yields 14.29% (.506 NZ/US*)		Euro Inv. Bk. 5½% 9/8/93, yields 8.01% (1.675 US/DM)		Canada 5% 23/7/93, yields 5.73% (134.2 US/JY)		Sweden 9% 14/4/93, yields 13.27% (1.45 BP/US)
4 year	8.29%		CBA 14% 1/7/94, yields 14.13% (.616 A\$/US)					
6 year	8.33%			Hydro Quebec 5½% 1/5/96, yields 7.78% (1.636 US/DM)				
8 year	8.37%				Australia 5% 30/10/98, yields 6.64% (1.307 US/SF)			
Spot Exchange Rate	N/A	.5945	.7597	1.687	1.4877	144.21	6.52	1.6585

*For example, since a US\$-based investor would receive 600 basis points (1429-829) by holding the Tourist Hotel bond, the NZ\$ can depreciate to .506 NZ/US from the present spot exchange rate of

.5945 NZ/US over the next 3 years for the NZ\$ investment to break even with current US\$ rates of interest. Assumes that bonds are held to maturity, and coupons are reinvested.

FOREX RATES & UPDATE

<u>Currency</u>	<u>Spot</u>	<u>3-Month</u>	<u>12-Month</u>	<u>Comments vis à vis US\$</u>	<u>Comments vis à vis DM (Spot DM: 1.6850)</u>
Australian dollar	.7600-.7610	.7455-.7660	.7130-.7155	Neutral	Neutral
Belgian franc	33.36-35.40	35.51-35.62	35.91-36.20	Remain long	Neutral
Danish krone	6.5450-6.5500	6.6035-6.6135	6.7370-6.7580	Remain long	Remain long
Dutch guilder	1.9110-1.9120	1.9135-1.9145	1.9195-1.9220	Remain long	Neutral
Greek drachma	157.90-158.20	162.50-166.30	172.90-188.20	Remain short	Remain short
Hong Kong dollar	7.8100-7.8115	7.8110-7.8135	7.8195-7.8270	Neutral	Neutral
Irish punt	1.5650-1.5665	1.5507-1.5532	1.5175-1.5215	Remain long	Neutral
Italian lira	1257-1258	1270-1273	1307-1318	Remain long	Remain long
Kuwaiti dinar	.29090-.29140	.29070-.29160	.28960-.29140	Neutral	Neutral
Malaysian ringgit	2.7015-2.7030	2.6080-2.6910	2.6615-2.6180	Neutral	Neutral
New Zealand dollar	.5920-.5935	.5840-.5860	.5620-.5660	Remain long	Neutral
Norwegian krone	6.5300-6.5350	6.5810-6.5900	6.7110-6.7300	Remain long	Neutral
Portugese escudo	149.00-149.50	152.00-153.00	162.00-165.50	Neutral	Neutral
Saudi Arabian riyal	3.7500-3.7510	3.7460-3.7490	3.7430-3.7470	Remain short	Remain short
Singapore dollar	1.8695-1.8715	1.8645-1.8680	1.8485-1.8605	Neutral	Neutral
Spanish peseta	109.30-109.40	111.08-111.23	116.10-116.30	Remain long	Neutral
Swedish krona	6.1450-6.1500	6.1620-6.1750	6.2500-6.3000	Remain long	Neutral

Explanatory Notes

*Indicates change in recommendation from last issue.

Currency expected to firm against both currencies.

Currency expected to strengthen against US\$ and weaken against DM.

Currency expected to weaken against both major currencies.

Currency expected to weaken against US\$, but strengthen against DM.

Term used to liquidate short position but does not imply a new buy recommendation.

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

Buy	Buy
Buy	Sell
Sell	Sell
Sell	Buy

Cover

Liquidate

HOTLINE UPDATE

Thursday, January 4, 5:00 p.m.:

Reenter the long March SF/short March DM spread. Make sure the spread is weighted in equal dollar equivalents.

Friday, January 5:

A repeat of Thursday, January 4 update.

Tuesday, January 9:

A note to our subscribers. Re: Italian lira/DM cross trade. This trade was recommended when the cross was 749.70. At the time the EMS band in which it was allowed to trade in relation to the DM was 765.40 to 678.65, a 12% band with the central rate at 720.65. On Friday, January 5, 1990, due to pressure on the lira, the cross traded as low as 754.00. Today the cross has firmed to 747 following the 3% devaluation against the ECU to 1528.08. Now the maximum fluctuation has been also tightened to

4½% — the central rate cross being 742.31 and the allowable range 764.58 - 725.97. We believe this is very constructive for our long lira position.

Friday, January 12:

A repeat of Tuesday, January 9 update.

Tuesday, January 16:

No changes or new recommendations.

Friday, January 19:

No changes or new recommendations.

Tuesday, January 23:

No changes or new recommendations.

Friday, January 16:

No changes or new recommendations.

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