

FRIEDBERG'S

COMMODITY & CURRENCY COMMENTS

Friedberg Commodity Management Inc.



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Looking through rose-colored glasses?

The reaction of financial market to the commencement of armed hostilities in the Gulf has taken on surrealistic tones. Otherwise intelligent, thinking individuals, at a loss to justify the explosive rise in stock prices, shrug it off by assuming that the market "knows" something they don't. Others, not so intelligent, advance a simplistic theory: The Fed's aggressive easing is bound to turn the economy around — hasn't history proved it? Finally, the technicians join the parade, unconcerned with the whys, mesmerized by the sheer power of the rally.

Stock markets have become mere games of baseball. Screens spit out the statistical record of each player as he comes to bat. He's just a number. We find rules such as "two tumbles and a jump" — when the Fed cuts the desired rate twice, the stock market climbs. According to the newsletter *Market Logic*, this has happened only 18 times before. In the 12 months following the second tumble, the median gain in stock prices has been 31%.

Or even the more esoteric Breadth Stampede (a 2 to 1 ratio of advances to declines on a 10-day moving average basis). As propounded by Martin Zweig, a Breadth Stampede must occur within plus or minus three months of the Fed's initial move towards ease to attain a very bullish signal. There have been only 10 prior Double-Barrelled buys since 1926. A month later, the S&P 500 Index had risen 7.5%; three months later, the S&P was up 12.5%; six months later, 19%+; a year later, up 26% and 18 months later, the S&P had gained 38.3%. And finally, according to Laszlo Birinyi of Birinyi Associates, the stock market's 10-day advance-decline line, a measure that looks at the number of stocks going up versus those going down, has reached levels seen only five times in the last decade: August and October 1982, January 1985, and January 1987. The months following these periods were all bullish for stocks. On February 11, with the Dow Jones average gaining 71.5 points, advancing stocks outnumbered declining issues by...10 to 1!

The greater the stampede, the more bullish the implications. The logic eludes us. Are we to believe that *smart money* acts in such haste, buys with such abandon? Is it possible that the revealed truth appears simultaneously to hundreds of institutional investors who for months professed a deep atheism? Or is it — as is more likely — that only one Seer received the Truth, and his blind followers jumped aboard? Should

we, then, be impressed by the fanaticism of his followers just because they are rich?

There are those who argue that the very same skepticism was expressed by the non-believers in August 1982 — and they were left out of the greatest bull market since the '20s. 'Tis true. But one bad call does not automatically imply a second bad call. In fact, it is quite likely that the non-believers learned their lesson and are now better prepared to defend their disbelief. They have had to *think*. Not so the believers. They just follow the leader.

It is by now painfully clear on which side the writer sits. He's a non-believer and he'd rather go down in flames *thinking* than reach a fool's paradise. The writer does not believe, because:

a) Stock prices do not represent value by any stretch of the imagination. They trade at 16.8 times earnings, 2.48 times book value, and they yield 3.3%.

b) Earnings expectations on the part of analysts surveyed by Standard & Poor's and Merrill Lynch continue to exceed the wildest imagination; a highly abnormal occurrence at bear market lows. Analysts expect S&P 500 earnings to be up 21.6% (!) in 1991. And yet, aggregate fourth quarter earnings for the Dow Jones Equity Market Index of more than 700

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Contributions by Albert D. Friedberg, Daniel A. Gordon, and Michael D. Hart.

Futures and options trading is speculative and involves risk of loss. Past trading results are not indicative of future profits.

stocks were 7.6% below expectations according to Zacks Investment Research. Fifty-five of the 81 stock groups in the index had negative surprises, while only 26 groups reported earnings as expected or better.

c) Lack of realism. Corporations are acting as if the turnaround is imminent; a great many of them *borrow to pay dividends*. In the US, General Motors had been *borrowing* to pay its \$1.8 billion annual dividend before the Board agreed to cut the dividend by 47%. With all that, institutional managers prodded management to take a longer view of this cyclical correction. In the words of John Neff, manager of the \$9 billion Windsor Fund, "If this is going to be a disastrous year, you have to take a harder look. But even so, there is 1992 and 1993. These aren't normal times. You try to declare a dividend relative to normal times."

In the UK, during 1990, the corporate financial deficit widened further. The cumulative deficit in the first quarter of the year, at £22 billion, was already equal to the deficit for all of 1989. With profitability plunging and income gearing reaching the highest level of the post-war period (see Chart 1), the Bank of England remarks rather caustically "it is perhaps surprising that dividend payments remain high with the amount paid in the third quarter of 1990 only marginally less than the *record first quarter figure* and 8.7% up on a year earlier, despite a 3% fall in normal profits."

The refusal to cut dividends is maybe fatal. Do we no longer believe in death? In the face of scores of companies' filing Chapter 11 bankruptcies, on a daily basis, we act unconcerned, and recklessly plunge ahead to expend the remains of liquidity. London, the old bastion of financial conservatism, leads the way in this worldwide degenerative disease called illiquidity — at the end of the third quarter of 1990 current assets supported barely 60% of current liabilities (see Chart 2).

Are we not closer to a worldwide financial breakdown than we think?

d) Contrary to popular belief (and Fed dogma) credit crunches are good. In fact, a credit crunch is to easy credit what fever is to an infection.

Wasn't easy credit the cause of all the billions of dollars of developer and corporate waste that litters the US? Manufacturing capacity utilization peaked in January 1989 at 85.1%, the lowest major top of the post-WWII era. It was already down to 80% in November, and in the opinion of *Industry Forecast* (IF) it may well hit a postwar low below 70% before 1991 ends. The national office vacancy rate, close to 20%, will, according to IF, be rising towards 25%.

Can these idle resources be rescued with more or cheaper credit or should we, as eventually we must, "liquidate" them, i.e., hammer them down, in a fire sale, to realistic price levels? Lower prices — and at times dramatically lower prices — will help restart the circular flow of income in the US economy.

What the Fed fails to realize is that generalized reflation does not augment purchasing power — it merely shifts upward the cost and prices of everything, leaving real income unchanged. What needs to be done is to allow overpriced

assets (as well as overpriced wages or services, or what have you) to fall in price relative to corporate and household income, thus enhancing the latter's purchasing power. The banks must be forced to mark to market and then liquidate nonperforming assets; as the tragedy of the S&Ls demonstrated, liquidation is the answer, not forbearance.

Fighting credit crunches with exhortations to lend more and more freely, accompanied by soaring reserve creation will only cause inflation, leaving intact the wreckage of bad investments and prolonging the agony.

There can be no meaningful recovery without first undergoing a full-fledged bout of liquidation. 1991 is not 1982, because USA 1982 did not suffer from the crippling overcapacity of the '90s.

e) Contrary to popular belief (and Fed dogma) neither interest rate declines nor money supply reacceleration pull an economy out of a recession; a concept that we have discussed *ad nauseam* in past issues. Second to the automatic adjustment discussed in (d) above, Keynesian pump-priming is the correct prescription for an economic recovery, either by way of increased public spending or through tax relief. In the last two recessions, tax relief was the answer. The 1975 tax cut was equal to 2.2% of personal income, while the 1981 tax cut was equal to 2.8% of personal income, implemented over a 20-month period. An equivalent tax relief in 1991 would amount to approximately \$100 to \$130 billion; instead, personal taxes are going up \$20-30 billion! What is more, Congress and the Administration are not likely to allow the budget to swing anti-cyclically much above \$300 billion; new cuts in spending and/or increased taxes will surely be forthcoming.

Can 1991 *really* be 1982?

f) In some mysterious way, forecasters now believe that the US slump will end sometime this spring. A quarterly survey of 35 seers by the Federal Reserve Bank of Philadelphia found that only four of the forecasters believed that the odds are greater than 50% that the recession will persist into the third quarter. This despite the fact that they have revised downward their December forecast for the first quarter 1991, from -0.9 to -1.9%.

If in December 1990 they equivocated about the first quarter of 1991, what makes them so unanimously sure now about the third quarter of 1991?

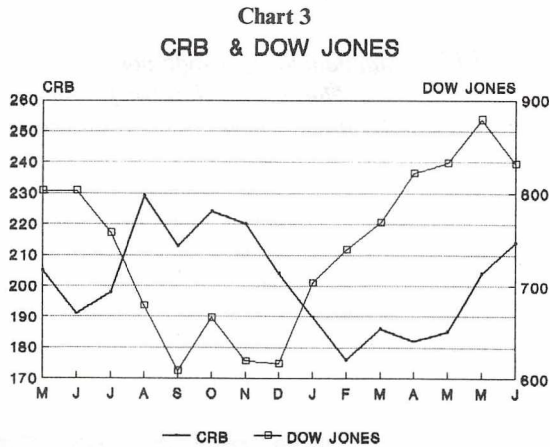
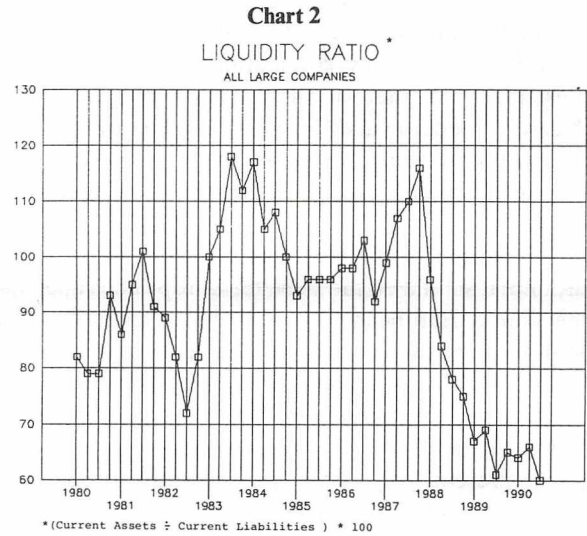
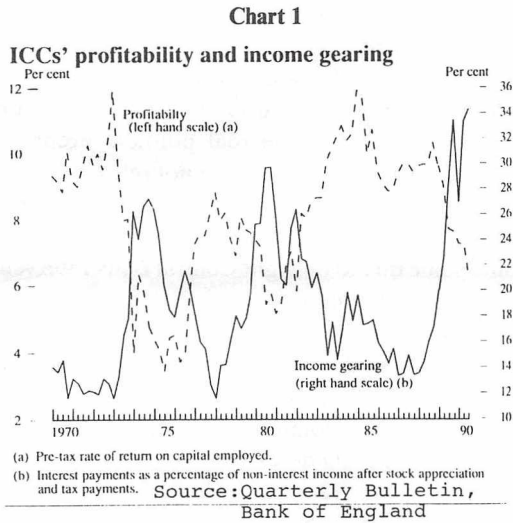
Perhaps, the stock market itself. And so we find the absurdity that professional economists deify the Wall Street Oracle, assuming that *it* must know something they don't.

f) If the economy is in fact turning, commodity prices should confirm it. A look at the record supports the view that commodity prices are sensitive enough to signal the end of a recession. Charts 3, 4, 5, 6 are instructive. In 1975, commodity prices turned up a full five months after Wall Street (but coincided with the trough in industrial activity). In 1982, commodity prices bottomed two months after Wall Street (and three months earlier than the trough in industrial production). In 1987, despite Wall Street's crash, commodity prices continued their upward climb, refusing to confirm Wall Street's premonition of a recession.

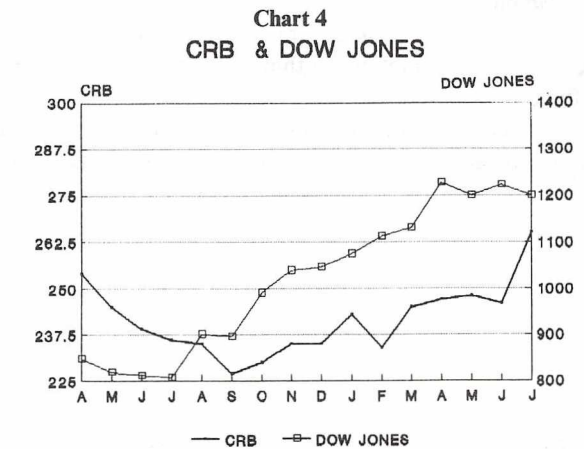
It has been four months since Wall Street recorded its so-called bear market low — yet commodity prices are in a free fall, giving nary a hint of an economic turnaround. We'll see.

In all, we remain stout nonbelievers. Strangely, we can't help but feel that once, exactly 61 years ago, the US Financial Markets lived through the same euphoria...

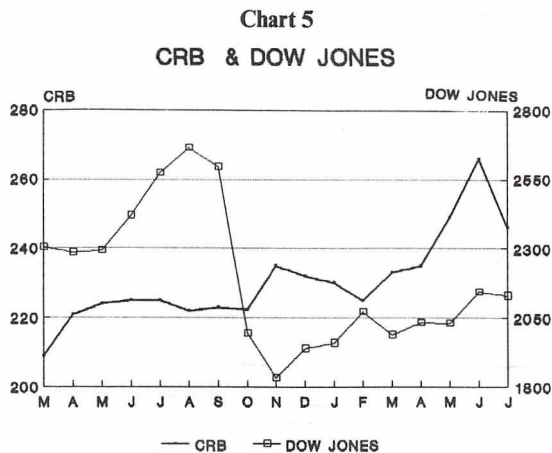
STRATEGY: Retain long Value Line/short S&P spread. Buy September 1991 S&P puts at market. See our dollar discussion in the next section.



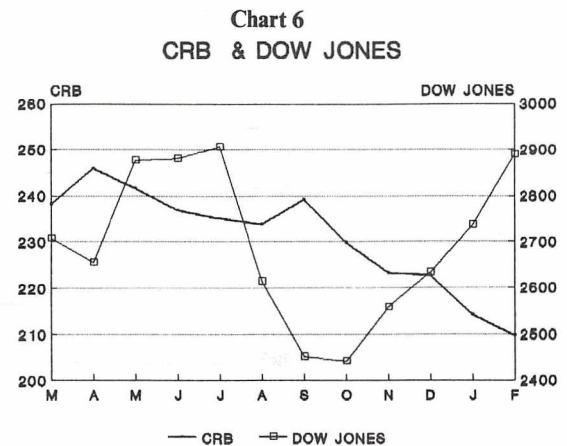
1974-1976



1982-1983



1987-1988



1990-1991

CURRENCIES

We're dollar bears

A strange kind of logic has crept in the foreign exchange markets since about two weeks ago, and runs something like this: An end to the Gulf war will restore much-needed confidence in the US economy, stimulating, in conjunction with the present drop in interest rates, an economic recovery. In which case, Greenspan and Co. will stop easing money, interest rates will rise, and the dollar will rise.

Those advancing this view conveniently ignore the following:

1) If the end of the war, in fact, spells an economic turnaround, it should do the same for Europe and Japan (has anyone seen a European airport or hotel recently?). The economic recovery in Europe (where the UK, Sweden, Italy, and France are already in various stages of recession) would logically maintain the present interest rate spread in favor of Europe and Japan.

2) At present, the interest rate spread between three-month DM deposits and US\$ deposits, on a *nominal* basis, is 250 basis points (and 300 basis points *vis à vis* ECU deposits). On a *real* basis, the spread is at least 500 basis points. The US is a long way from attaining interest rate parity, a situation that may require much more than the resolution of the Gulf conflict.

3) Since the US recession antedates the Gulf war, and more importantly, is due to far more serious reasons — a long

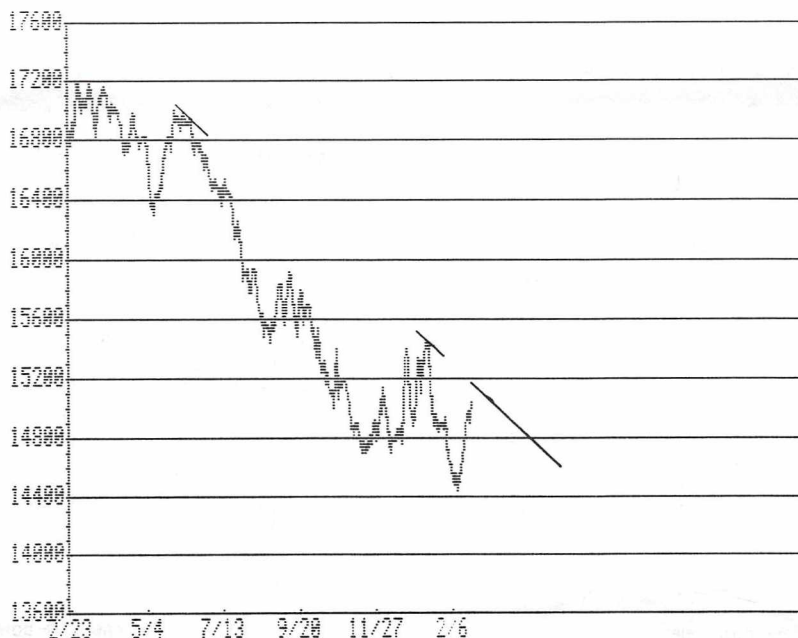
and steady erosion of corporate profits, too much household and corporate leverage, a moribund banking system, etc. — it is highly unlikely that the mere end of the war would stimulate a recovery.

The fact *is* that the dollar continues its long downtrend (see Chart 7). Fluctuations around the downtrend are due to a number of factors, some real political events, such as Schevardnaze's resignation), some not relevant (geopolitical conclusions about the above event), some imaginary (expectations of a turnaround in the economy after the end of the war), and some due to outright Central Bank intervention (as occurred two weeks ago).

The main argument for our bearish view on the dollar rests on the state of the US economy: It is weak and shows no signs of recovery. While, thanks to this weakness, the current account deficit is becoming smaller month by month (an otherwise encouraging development), the capital account is likely to deteriorate dramatically in coming months as investment opportunities onshore disappear, bank confidence deteriorates, and real interest rate differentials remain so large.

STRATEGY: *Maintain long outright positions in DM with stops at 64.00, basis March '91, close only. Maintain long DM/short yen cross trade (see the section on the Japanese yen).*

Chart 7 – DM Spot



YEN, JAPANESE BONDS & NIKKEI INDEX

Our yen for the DM

Years of excessive monetary growth have created an inertial inflationary push, reflected first in rising asset prices and later in rising wage settlements.

The year's spring wage negotiations ("Shunto"), which will determine pay scales for the year to come, is worrying the Bank of Japan. Last year's Shunto produced wage gains of 5.9%; this year it promises to produce higher gains as the trade union confederation seems to be gunning for increases of 8% to 9%. Helping along their demands is the tighter state of the labor market: unemployment hovers around 2.1%, among the lowest in the world.

As a result, the BOJ has maintained a moderately restrictive policy, with overnight rates around 7.75% versus 10-year paper yields of 6.75%. Broad money, M2 + CD, has decelerated markedly in recent months, standing 7.3% higher than one year ago while narrow money (M1) has risen 4.7% over one year ago. Both of these figures are positive in real terms, hardly bespeaking a monetary "squeeze" as some observers would have it.

Asset and wage inflation remain stubbornly high in Japan, and there is a real danger that it will become ingrained in the price structure. Any easing by the BOJ at this time is absolutely premature.

Monetary policy in Japan, when measured in terms of the recent growth of aggregates and the slope of the yield curve, is slightly more restrictive than in West Germany, for which, when measured in the absolute level of short-term deposits, the reverse is true. The crucial difference lies, however, in: a) the length of monetary excesses — Japan's easy money policy from the mid-eighties on is legendary, and its

effects will be long in coming; and b) in relation to its loose fiscal position, West Germany's monetary policy is restrictive; this is not the case for Japan.

In conclusion, we remain convinced that the DM will outperform the yen in coming weeks and months.

STRATEGY: Retain the long DM/short Yen cross trade, risking a close below 86 Yen/DM, basis March '91.

Retain short positions in Nikkei futures with stops at 26,000, basis cash index only.

Chart 8
DM March/Yen March

**CANADIAN DOLLAR**

Liquidate long positions now

Canada's economy continues to weaken significantly. Real GDP declined 1 percentage point in the third quarter of 1990, following a 1.1 percentage point decline in the second quarter. Available data for the last months of 1990 suggest that a further decline in output is likely in the fourth quarter. Unemployment is rising rather sharply, particularly in the industrialized centers of Quebec and Ontario, affecting 9.3% of the labor force.

The inflation picture, however, is not encouraging. January '91 CPI rose 6.8% over the year-ago period, helped by the introduction of the goods and services tax. More ominously, wage settlements and unit labor cost (Charts 9 and 10) paint a picture of built-in inflation that will undoubtedly hinder con-

siderably economic recovery. It should be noted that the cumulative increase in Canadian unit labor costs has exceeded that in the US by 7% since early 1987, a serious loss of competitiveness. A devaluation will serve only to validate this inflation, making it a very poor option for stimulating economic revival.

The Bank of Canada has continued to follow money markets rates lower, narrowing, if ever so slightly, the interest rate differential *vis à vis* the US. The rate of growth of M2, year-over-year continues to decelerate (see Chart 11), a welcome development. A closer look, however, indicates that the two most important monetary aggregates, M1 and M2, are beginning to grow at a double digit pace in the most recent

three months, a sign that the Bank may be forced, once again, to hold the line on rates and perhaps even back up somewhat.

The BOC is thus caught in a straightjacket: On one hand, the recession is worsening, with no sign of a bottom; on the other hand, inflation remains extremely stubborn, especially at the labor front, and monetary aggregates are beginning to speed up, well beyond BOC targets. An independent central bank, whose sole (or at least primary) function was to achieve zero inflation would have to choose among the following three courses of action: a) Monetarist — keep M2 growing indefinitely at 6% per annum; b) Wicksellian — maintain the yield curve slightly negative to flat (as now); or

c) maintain a steady trade-weighted dollar. Any one of these three policy courses will produce, *if sustained for long periods of time*, a near-zero rate of inflation.

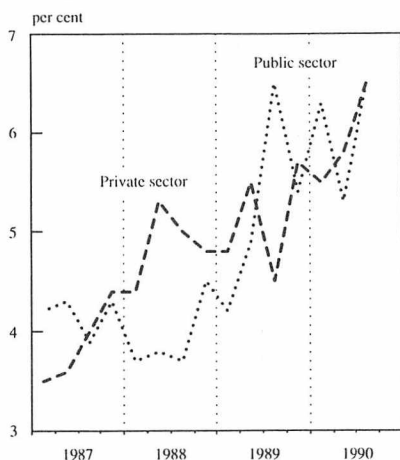
Will the BOC care?

The Bank's intervention below the 1.15 level indicates that for now, they would like to keep the Canuck buck from rising further — an event we anticipated in our last issue. We therefore recommended liquidating long C\$ positions (see Hotline Update for Feb. 21), accepting handsome profits.

STRATEGY: *Remain sidelined, awaiting further signals from the BOC.*

Chart 9

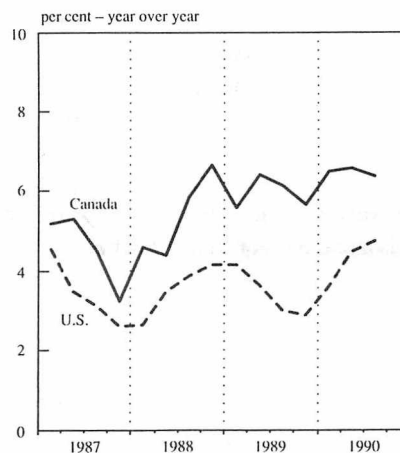
Wage Settlements



Source: Quarterly Economic Review, Dept. of Finance, Canada

Chart 10

Growth of Unit Labour Costs
Canada - U.S. Comparison



Source: Quarterly Eco. Review Dept. of Finance, Canada

Chart 11

CANADA : M2
YEAR-OVER-YEAR % CHANGE

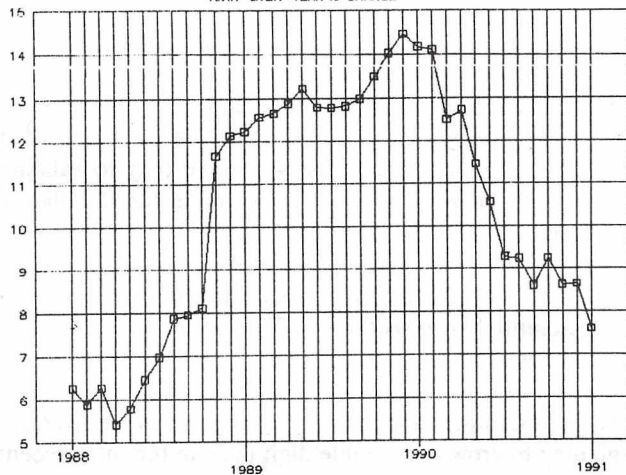


Chart 12
Canadian Dollar Spot



CRUDE OIL

The wreckage of the Middle-East

The steady and anticipated downdrift of oil prices has been accompanied by a sharp return towards contango (see Chart 13) as spot prices have fallen to a minuscule 30¢/barrel premium to six-month positions. Clearly, speculatively-built stocks are reflowing back into the normal circuit and now threaten to topple the price structure to levels below those seen prior to August 2, 1990.

At the same time, the refining margin basis September 1991 continues to narrow, an indication that the fall in product prices is lagging the fall in crude — and a sign that genuine consumer demand is flagging.

It is noteworthy that the Saudi financial position continues to deteriorate rapidly, to the point that the Saudis have been forced to arrange, for the first time in their history, a US\$3.65 billion loan from private banking sources. War expenditures are likely to push them further into deficit. The logical conclusion is that the Saudis will continue an aggressive oil marketing policy for the foreseeable future.

While there is little doubt about the successful outcome of the war, it is surprising how little has been said about the financial consequences of the war on the Gulf regime.

Iraq's reckless military gamble has, without a doubt, economically ruined the Gulf States for all time. The logic is straightforward: Reconstruction costs for both Kuwait and Iraq will easily exceed \$100 billion. Add to this war costs borne by Saudi Arabia and Kuwait — say another \$25 billion. Iraq reparation payments to private and official partners *outside* Kuwait and Saudi Arabia (so as not to double count), to take a wild guess — can easily exceed \$20 billion. (Will the Allies force Iraq to cover their cost of the war?) The total bill could approach \$150 billion *over and above current, day-to-day budgetary requirements*.

The Gulf States are *not* Western Europe after WWII. They are a one-commodity economy with little or no prospects for industrialization and export diversification. Bridge loans and supplier credits will look for repayment out of a future stream of oil revenues, which means in effect that the Gulf States will be moving to maximize production in a competitive race to extract the highest possible total revenue.

While the Kuwaitis may be in a position to dip into reserves and cover their cost — albeit at the expense of consuming a substantial portion of this semi-private kitty — Saudi Arabia is not in such a position, as mentioned above. Moreover, Iraq, already financially bankrupt, will need to increase oil production by a few million barrels per day above their OPEC quota to cover even a small part of their financial requirements.

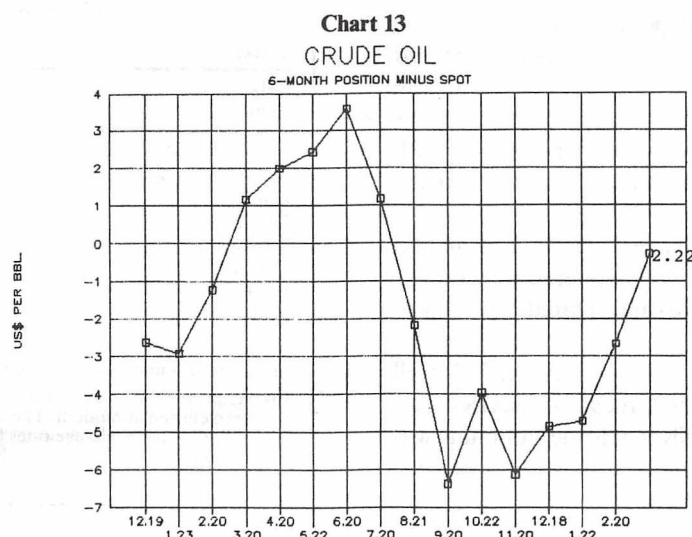
Since the demand for oil is relatively elastic in the medium term, it appears sensible for the high-capacity, financially pressed Gulf producers to maximize production and allow volume to compensate for falling prices. With all that, however, it will be nearly impossible for these countries to ever recover from Saddam Hussein's mad adventure.

The extraordinary accretion to Arab wealth resulting from soaring oil prices in the '70s *peaked* in 1980-81 as a consequence of a sharp falloff in demand. The gentle decline gathered some speed after the 1986 collapse in prices.

What remained of Arab wealth the war has destroyed — mostly transferred to the Western defense, construction, and engineering industries.

Over time, oil is headed to the low single-digit numbers.

STRATEGY: *Remain short deferred contracts.*



FRIEDBERG CAPITAL MARKETS

ECU bonds

In the international bond markets, prices have advanced recently (due mostly to interest rate cuts), but there is another factor at work that is not often noted: A limited supply of Eurobonds has lately added to upward price movements.

As the demand for a given issue rises, the float dwindles and prices rise. At some point, market makers can quote bids — only on bonds that have become illiquid, unless they are willing to go short, which can be very dangerous if they are forced to cover.

This problem, which has appeared more often in Swiss franc and ECU bonds, is obviously more acute with smaller issues, and not a factor in the large issues.

The ECU's popularity with investors has been steadily growing over the past few years, and finally a "super-issue" has been launched. A "super-issue" is Euromarket lingo for a bond whose sheer size makes its liquidity comparable to the liquidity found in treasuries. The recently issued United Kingdom ECU bond is a 2½ billion ECU issue (approximately US\$3.5 billion) and has been received very favorably in the Euromarkets as the first and so far only ECU bond that supplies investors with superior liquidity.

We are now offering the following:

United Kingdom 9½%, due 21/2/2001, priced to yield 9.05% in ECU. Rated AAA by S&P and Moody's.

NOTE: The ECU is a hard-currency "cocktail" made up of the currencies shown in Chart 14.

Convertible bonds

Sunrise Medical convertible 7.25%, due June 26, 1996, recent bid 129.

Sunrise Medical just completed its eighth consecutive quarter of record sales and earnings.

The company continued to experience robust sales and earnings growth in the second fiscal quarter. Sales increased 17% to \$47.8 million, while net income reached \$1.45 million, a gain of 65%. On a per share basis, fully diluted earnings grew 47% to 28¢ versus 19¢ last year. We are pleased with these results, as this is seasonally a modest quarter for us in both sales and earnings.

First-half results set a record pace. Sales of \$95.9 million ran 20% ahead of prior year, while net income climbed 81%, to \$3.15 million. Earnings per share (fully diluted) rose 58% to 60¢ compared with 38¢ last year.

The Sunrise common is currently trading at \$23.75, well above conversion of \$17%. You will recall we advised purchasing the bonds in the mid-'50s when the common was trading at \$3.50. The bonds are callable at 102, which may force holders to convert prematurely.

STRATEGY: Short of a forced conversion we prefer to remain long, as the capital gains prospects remain excellent while we still enjoy a yield of 5.5% at the current bid price (and over 18% on historical cost).

* * * * *

In keeping with our investment philosophy of purchasing high-yield undervalued convertible bonds that trade at or close to their investment floor (and consequently offer conversion privileges for free), and that enjoy relatively good interest coverage and asset coverage ratios (providing as well some financial comfort), we present the following convertible bonds:

Burnup & Sims convertible, 12%, due Nov. 15, 2000, recent price 63½. Yield to maturity 22%. Traded US over-the-counter market

Conversion terms: 51.948 shares per \$1,000 bonds or convertible at \$19.25 per share. Recent stock price \$8.00.

Burnup & Sims Inc. was founded in 1929 and together with its subsidiaries currently provides a wide range of cable design, installation, and maintenance services to telephone, CATV, and utility service customers throughout the US. These services are rendered through various subsidiary companies located principally in California, Florida, Georgia, Mississippi, South Carolina, and Texas.

In addition, Burnup & Sims is one of the principal manufacturers of power supplies for the CATV industry. Through its General Products segment, the company operates a motion picture theater chain in the Southeastern US and also provides commercial printing and graphic arts services. Chart 15 is a quick snapshot of Burnup & Sims financials.

Chart 14 – Composition of the ECU

Currency	Amount (a)	Weight (b)
Belgian franc	3.431	8.1
French franc	1.332	19.3
Lira	151.8	9.8
Dutch guilder	0.2198	9.4
Deutschemark	0.6242	30.2
Danish krone	0.1976	2.5
Irish punt	0.008552	1.1
Peseta	6.885	5.3
Drachma	1.44	0.7
Sterling	0.08784	12.8
Escudo	1.04741	0.8
		100.0

(a) These amounts have applied since September 1989.
 (b) Weights based on exchange rates on 12 October 1990. This date has been chosen at random. The weights in the ECU will of course change as the exchange rates for the component currencies are determined by forces of supply and demand

Source: IMF Oct. 1989

Chart 15

Net Income (after tax) (000's)	1987 6,374	1988 5,634	1989 7,714
Cash flow available to support debt service has been adequate:			
	6 months ended Oct. 31/89	6 months ended Oct. 31/90	
Net income before income tax	2,455	3,528	
Add back:			
Interest expense	3,701	3,376	
Depreciation and amortization	5,087	4,496	
Amortization of goodwill and other intangibles			
Total	11,243	11,400	
Debt service	3,701	3,376	
Excess	7,542	8,024	
Coverage ratio	3.03:1	3.37:1	
Other relevant statistics (Year ended April 30, 1990)			
Current assets		\$81,236	
Current liabilities		29,509	
Long-term debt		39,216	
Current ratio		2.75:1	
Long-term debt/total market capitalization		42.7%	
CV Bonds outstanding \$29,755	issue size — \$32,380		
Rating B2 by Moody's			
Earnings per share (trailing 12 months)		\$0.98	
Stock price (25/2/91)		9½	

Chart 16
Foreign Currency Bonds

Date: February 21, 1991

We offer the following Bonds: subject to change without prior notice: Minimum amount US\$5000 (Cdn.\$7,000)

ISSUER/MATURITY DATE/COUPON	BID	OFFER	CURRENT ANN. YIELD TO MTY.	NEXT PAY DATE
<u>DEUTSCHE MARK DENOMINATED BONDS</u>				
KINGDOM OF SWEDEN 7 1/4% 1/2/95	96	- 96 3/4	8.25%	01/02/92
QUEBEC HYDRO 5 1/2% 1/5/96 RISP eligible	84	-		01/05/91
PROVINCE OF QUEBEC 6% 1/4/97 RISP eligible	84	1/2 -		01/04/91
EUROPEAN INV. BANK 5 1/2% 9/8/93	93	1/2 - 94 1/4		09/08/91
BANK OF NOVA SCOTIA 5 5/8% 07/05/96 RISP eligible	84	-		07/05/91
WORLD BANK 5 7/8% 4/2/97 RISP eligible	87	1/2 - 88 1/4	8.47%	04/02/92
<u>SMISS FRANC DENOMINATED BONDS</u>				
GOVT. OF AUSTRALIA 30/10/90 5%	89	- 91	6.52%	30/10/91
<u>DANISH KRONER DENOMINATED BONDS</u>				
KINGDOM OF DENMARK 9% 20/11/92	98	1/2 - 99 1/4	9.44%	20/11/91
<u>FCU DENOMINATED BONDS</u>				
UNITED KINGDOM 9 1/8% 21/02/01	99	3/4 - 100 1/2	9.05%	21/02/01
<u>BRITISH POUND DENOMINATED BONDS</u>				
RGM of SWEDEN 14/4/93 9 3/8%	96	- 97	11.00%	14/04/91
<u>FRANC DENOMINATED BONDS</u>				
EUROPEAN INV. BANK 8 3/4% 12/1/95	98	1/2 - 99 1/4	8.94%	12/07/91
<u>JAPANESE YEN DENOMINATED BONDS</u>				
GOVT. OF CANADA 23/7/93 5 5/8% RISP eligible	95	5/8 - 96 3/8	7.30%	23/07/91
<u>CANADIAN DOLLAR DENOMINATED BONDS</u>				
GOVERNMENT OF CANADA (semi annual) 01/09/91 9%	99.35	- 99.65	9.96%	01/03/91
<u>NEW ZEALAND DOLLAR DENOMINATED BONDS</u>				
CDN. IMP. BANK OF COMMERCE 27/07/92 14% RISP eligible	101	1/2 - 102 1/4	12.02%	27/07/91
<u>AUSTRALIAN DOLLAR DENOMINATED BONDS</u>				
General Electric 11/07/92 14 1/4% (semi)	102	3/4 - 103 1/2	11.71%	11/07/91
COMMONWEALTH BANK OF AUSTRALIA 01/07/94 14%	104	- 104 3/4	12.12%	01/07/91
WORLD BANK 15/03/93 12 3/4% RISP eligible	101	1/2 - 102 1/4	11.44%	15/03/91
<u>U.S. DOLLAR DENOMINATED FIXED CONVERTIBLE BONDS</u>				
PACIFIC SCIENTIFIC 7 3/4% 15/06/03(semi)	68	1/4 - 70 1/4	12.95%	15/06/91
CV @\$38 p/sh				
SUNRISE MEDICAL INC. 7.25% 26/6/96	129	- 135 1/4	5.36%	26/06/91
CV @\$17 5/8 p/sh				
ALLIANT COMPUTER 7.25% 15/05/12(semi)	19	- 23	34.14%	15/05/91
CV @\$39.75 p/sh				
COOPER CO'S. 10 5/8% 01/03/05(semi)	71	1/2 - 73 1/2	15.84%	01/03/91
CV @\$27.45 p/sh call in 1995 @100				
DICEON ELECTRONICS 5.5% 1/3/12 (semi)	27	- 30 1/2	19.91%	01/03/91
CV @\$39.50 p/sh				
BURNUP & SIMS 12% 15/11/00 (semi) CV @19.25 p.s.	59	- 63 1/2	22.00%	05/15/91
<u>U.S. DOLLAR DENOMINATED FIXED RATE BONDS</u>				
ALBERTA 7 3/8% 9/12/91 RISP eligible	99	3/4 - 100 1/2	6.60%	09/12/91
SOUTHMARK 12% 10/8/97 (semi)	40	- 44	13.57%	10/08/91
<u>U.S. DOLLAR DENOMINATED FLOATING RATE NOTES</u>				
UNITED KINGDOM 24/9/96				
3 mo LIBID-1/8 (qly)	99.80	- 100.10	7 15/16%	28/03/91
REPUBLIC OF ITALY 30/4/93				
3 mo Limean(qly)	98.92	- 99.32	7 3/32%	30/04/91

For further information and current prices please call: FRIEDBERG CAPITAL MARKETS (416) 364-2700

Although we monitor these issues specifically, we also can fill any order in any foreign currency bond.

Chart 17
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\$, DM, JY, DKr, BP, FFr, ECU) or revalue (for SF) before the interest rate advantage/disadvantage is overcome by currency depreciation/appreciation. Rates as of ?, 1991.

	U.S. \$	NEW ZEALAND \$	AUSTRALIAN \$	DEUTSCHEMARK	SWISS FRANC	JAPANESE YEN	DANISH KRONE	BRITISH POUND	FRENCH FRANC	EUROPEAN CURRENCY UNIT
1 year	6.26%	CIBC 14% 27/7/92, yields 12.02% (.568 NZ/US)	General Electric 14 1/4% 11/7/92, yields 11.71% (.7490 A\$/US)				Denmark 9% 20/11/92, yields 9.44% (5.892 US/Dkr.)			
2 year	6.88%		World Bank 12 3/4% 15/3/93, yields 11.44% (.7255 A/US)	EIB 5 1/2% 9/8/93, yields 8.16% (1.522 US/DM)		Canada 5% 23/7/93, yields 7.30% (131.90 US/JY)		Sweden 9 3/4% 14/4/93 yields 11.00 % (1.818 US/BP)		
3 year	7.10%		CBA 14% 1/7/94, yields 12.12% (.6858 A/US)							
4 year	7.30%			Sweden 7 1/4% 1/2/95, yields 8.25% (1.548 US/DM)					EIB 8 3/4% 12/7/95, yields 8.94% (5.404 US/FFr)	
7 year	7.74%				Australia 5% 30/10/98 yields 6.52% (1.1734 US/SF)					
10 year	7.85%									U.K. 9% 21/2/01 yields 9.05% (1.1501 US/ECU)
Spot Exchange Rate	N/A	.5998	.7883	1.4862	1.2707	130.87	5.7212	1.9615	5.0565	1.3856

*For example, since a US\$-based investor would receive 95 basis points (825-730) by holding the Sweden "DM" bond, the US/DM can depreciate to 1.522 US/DM from the present spot exchange rate of

1.4862 US/DM over the next 4 years for the DM investment to break even with current US\$ rates of interest. Assumes that bonds are held to maturity, and coupons are reinvested.

THE EXOTICS

Portugese escudo

Portugal has made some halting progress in its effort to liberalize the economy and the preparation for its eventual entry into the EMS.

While progress was made in the fiscal front, having shrunk the deficit from 11% of GDP in 1987 to 8.2% of GDP in 1988 and to 4.8% of GDP in 1989, some backtracking has taken place in 1990, primarily a result of the rise of interest rates and its effect on the public debt.

The fiscal deficit for 1990 is therefore estimated to rise to 7.5% of GDP. Nevertheless, the cyclically adjusted budget balance is in surplus by 1%, thus indicating that the stance of fiscal policy is towards restraints. Clearly, the government is trying to do its best to land into the EMS in better macro-economic balance.

Monetary aggregates continue to expand rapidly, with M1 rising at an 18.6% annual rate (August 1990 over August 1989)

and liquid assets rising at a 16.5% rate over the same period. As a result, inflation continues high with year-on-year consumer prices rising by 14.4% (October 1990 to October 1989).

The Bank of Portugal seems unable to contain the large inflow of capital, which has had the effect of causing inflation and increasing the real rate of exchange. An early entry into the EMS may compound this problem: A tight monetary policy used to bring down inflation will, however, attract an increasing amount of speculative capital from other EMS currencies, defeating the initial attempt. Portugal may require a drastic fiscal shock and a more prolonged period of tight money before it could successfully join the EMS.

STRATEGY: *Despite the relatively elevated level of its real rate of exchange, we favor long positions in deferred escudo (six-month to one year) vis à vis both the deutschemark and US dollar.*

Chart 18 - Rates

Spot	1 Month	3 Month	6 Month	12 Month
130.70 -	131.30-	132.9--	135.40-	140.70
130.90	131.80	133.90	136.90	144.90

Current bond portfolio allocation

In the interest of minimizing transaction costs, we advise current portfolios to remain invested as follows:

DM fixed-rate bonds	35%
US dollar high-yield and convertible bonds	25%
British pound fixed-rate bonds	12.5%
Danish krone fixed-rate bonds	17.5%
Japanese yen bonds	10%

Recommended bond portfolio allocation for new portfolios

For new portfolios, we recommend the following investments:

DM and/or ECU fixed-rate bonds	50%
US dollar high-yield and convertible bonds	25%
Danish krone fixed-rate bonds	25%

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FOREX RATES & UPDATE

<i>Currency</i>	<i>Spot</i>	<i>3-Month</i>	<i>12-Month</i>	<i>Comments vis à vis US\$</i>	<i>Comments vis à vis DM (Spot DM: 1.5000)</i>
Australian dollar	.7843-.7853	.7750-.7765	.7514-.7537	Neutral	Neutral
Belgian franc	30.65-30.70	30.83-30.92	31.26-31.45	Remain long	Neutral
Danish krone	5.7400-5.7450	5.7875-5.7975	5.9000-5.9225	Remain long	Neutral
Dutch guilder	1.6670-1.6680	1.6866-1.6881	1.7105-1.7140	Remain long	Neutral
Greek drachma	159.60-159.90	165.10-169.40	177.60-193.90	Neutral	Neutral
Hong Kong dollar	7.7910-7.7920	7.7860-7.7890	7.7950-7.8065	Neutral	Neutral
Irish punt	1.7840-1.7850	Not available	Not available	Remain long	Neutral
Italian lira	1113-1114	1128-1130	1168-1173	Remain long	Neutral
Malaysian ringgit	2.7005-2.7015	2.7025-2.7065	2.7100-2.7250	Neutral	Neutral
New Zealand dollar	.5970-.5980	.5895-.5910	.5670-.5700	Neutral	Neutral
Norwegian krone	5.8300-5.8350	5.8865-5.8965	6.0410-6.0635	Remain long	Neutral
Saudi Arabian riyal	3.7500-3.7510	3.7510-3.7540	3.7550-3.7610	Neutral	Neutral
Singapore dollar	1.7202-1.7212	1.7135-1.7165	1.6977-1.7087	Neutral	Neutral
Spanish peseta	92.70-92.80	94.38-94.55	98.82-99.07	Remain long	Neutral
Swedish krona	5.5630-5.5680	5.6355-5.6455	5.8310-5.8535	Neutral	Remain short

Explanatory Notes

Currency expected to firm against both currencies.	Buy	Buy
Currency expected to strengthen against US\$ and weaken against DM.	Buy	Sell
Currency expected to weaken against both major currencies.	Sell	Sell
Currency expected to weaken against US\$, but strengthen against DM.	Sell	Buy
Term used to 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

Flash update, Monday, January 21, 10:45 a.m.:

Sell long February leg of crude oil straddle, leaving short the deferred contracts.

Tuesday, January 22:

One new recommendation, as per our flash update of yesterday. Sell the February long leg of the crude oil straddle, remaining short the deferred contracts. The market letter is in the mail.

Friday, January 25:

Repeat as per January 22.

Tuesday, January 29:

No changes or new recommendations.

Friday, February 1:

No changes or new recommendations.

Flash update, Tuesday, February 5, 2:30 p.m.:

Reinstate short positions in S&P 500 futures. Sell March S&P at market. Place initial stops at 356.00, close only. Maintain the very profitable long KC Value Line/short S&P spread.

Flash update, Thursday, February 7, 1:30 p.m.:

1. Reinstate short position in March S&P at market. Place stops at 365.10, good anytime.
2. As per our update on Friday, January 4, you are long KC Value Line against short S&P. To balance this spread on a dollar basis, adjust contract numbers to long four KC Value Lines against short three S&P if the position held is large enough to allow this fine tuning. If not, retain one long KC Value Line against one short S&P.

Friday, February 8:

Wrap-up of week's activities.

1. Reinstate short position in S&P at market. Place stops at 365.10, good anytime. Maintain the very profitable long KC Value Line/short S&P spread.
2. As per our update on Friday, January 4, you are long KC Value Line against short S&P. To balance this spread on a dollar basis, adjust contract numbers to long four KC Value Line, against short three S&P if the position held is large enough to allow this fine tuning. If not, retain one long KC Value line against 1 short S&P.

Tuesday, February 12:

No changes or new recommendations.

Friday, February 15:

As the end of the war nears — a matter of weeks and perhaps days rather than months — crude oil prices will accelerate their downward motion. Future reconstruction and reparation costs will guarantee a veritable flood of oil in 1991-92. Therefore, add to existing short positions in the deferred months at market.

Tuesday, February 19:

No changes or new recommendations.

Flash update, Wednesday, February 20, 9:40 a.m.:

Reinstate short positions in March S&P at market, risking 369.05 stop, good anytime.

Flash update, Thursday, February 21, 1:15 p.m.:

Accept profits on long C\$ positions. Sell March C\$ at market.

Friday, February 22:

As per our update yesterday, we recommended liquidate long March C\$ positions, accepting profits.

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