FRIEDBERG'S
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US$: Sailing into troubled waters

For some months now (February, "Aborted rallies," and January, "Illusory strength"), we have been espousing a somewhat contrarian thesis regarding the US dollar: It will disappoint the bulls.

On the surface, the case for a higher dollar could not be more compelling. The US economy is recovering, while Europe and Japan are stagnating at best, or heading into recession. On a purchasing power basis and on anecdotal evidence, the US dollar "feels" cheap; more "scientific" studies have shown a relative undervaluation of around 20%. International money managers and professional traders agree. The former have increased their net exposure to US-dollar assets to near its highest level in more than three years (see Chart 1). The latter have continued to forecast significantly lower U.S. dollar levels.

The latest *Economist Intelligence Unit* poll reveals an even stronger preference for US dollars than three months earlier (see Chart 2). Remarkably, these forecasts exceed by a wide margin the levels "predicted" by forward rates; if they're right, literally everyone could become rich.

Instead, the US dollar has been weakening, albeit slowly in recent weeks to stand 1.9% lower against the DM and 3.8% against the yen than at March 31 and 2.5% and 11.4% respectively lower than on December 31, 1992.

What's wrong?

Marginal changes in the perception of economic growth. And a too-loose monetary policy.

While it is true that the US economy has been on a recovery since the first quarter of 1991, growth rates have disappointed. Productivity increases have lagged well behind those achieved in other post-war recoveries. The answer may very well lie in that modern day plague that threatens all capitalist societies: increased regulatory burdens.

In a provocative study entitled *Cost of Regulation* (Rochester Institute of Technology 1991), Thomas D. Hopkins has shown broad evidence to support the view that increased regulatory burdens have a highly detrimental effect on real GDP. As Chart 3 shows, strong economic growth in the 1982-88 period was, not uncoincidentally, accompanied by a continued fall in regulatory costs, while the reversal of the latter, rising between 2.3% and 2.7% each year from 1988 to 1992 may have been decisive in the attainment of a measly growth rate of 1.1%.

What is more, this table may underestimate the true rise in regulatory costs in recent years, as it does not take into account the burdensome 1990 amendments to the Clean Air Act that became effective for the years 1992 and beyond. For other horror stories, see the next article.

Under the present, interventionist Administration, the cost of regulatory compliance is sure to rise rather dramatically. Moreover, sharp prospective increases in marginal taxation will certainly have an added detrimental effect on growth in years to come.

Big government plus a still overly-indebted economy add up to no growth. (While debt increases have slowed down, income has slowed down too, leaving the crucial Debt/GNP ratio unchanged at an all-time high — see Chart 4). In retrospect, the 4Q 1992-1Q 1993 spurt in activity may have more to do with easy credit and unexpected inflation than with genuine increases in demand.

Be that as it may, however, beyond the noise of current quarter GNP figures, the markets have begun to sense secular stagnation. *At the margin,* expectations for US growth are being revised downwards.

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Contributions by Albert D. Friedberg, Neil Reynolds, David B. Rothberg, Llewellyn H. Rockwell, Jr., and Michael D. Hart.

Across the Atlantic, the gloom over the continuing recession may be a bit overdone. In the first place, the UK economy is giving unmistakable signs of improvement: The volume of retail sales rose by a seasonally adjusted 0.5% between February and March and was running 4.1% above the level of the same period last year.

Secondly, while there are signs that Germany's economy is still slumping — unemployment rose to 2.17 million in March from 2.10 in February, industrial orders fell 2.2% in February from January and retail sales were down 8% in January from a year ago — it is also true that the German economy is much less vulnerable than the Anglo-Saxon or Japanese economies. Private debt, as a percentage of disposable income in Germany is at 18% compared with 32% for the UK, 25% for the US, and 20% for Japan.

Moreover, speculative activity prior to the onset of the recession was relatively subdued. As a result, Germany is not likely to suffer the crippling balance sheet problem experienced by the US, UK, and Japan. In its February *Monthly Report* the Bundesbank comments that, "present economic conditions appear too gloomy if one pays attention to the manufacturing sector alone. Developments in the construction sector, just as in numerous service sectors, are much more favorable than in the industrial enterprises, which are especially hard hit by the export losses — a fact that is occasionally not heeded sufficiently in the debate on economic policy."

Mindful of stubborn inflation, the Bundesbank is likely to ease at a snail's pace. Significantly, it concludes that "all experience goes to show that it is not possible to achieve stabilisation of the economy as a whole by means of a deliberately *anti-cyclical interest rate policy,* such as has been recommended in some quarters. Rather, that would lead to a 'stop-and-go policy,' which would be fraught with considerable risks for long-term interest rates, the exchange rate of the deutschemark and the level of employment."

In short, Germany's economy may be able to perform better than the consensus estimate (which now sees a contraction of 2.4% for the year) and is likely to persist indefinitely with a cautious monetary policy, avoiding the anti-cyclical interest rate policy practiced by the US and the UK.

Here, too, then, a change is occurring *at the margin,* and expectations are, slowly, about to be *revised upwards.*

With regards to Japan, on the other hand, more economic weakness is bullish for the yen, bearish for the dollar, as the current account surplus is certain to grow. The fiscal package had the effect of temporarily lifting upwards expectations of growth; closer examination of the proposal, however, reveals that it contains little stimulus (see Dr. Steve Hanke's article "Smoke and Mirrors" elsewhere in this issue). And so, once again, expectations for growth, at the margin, are likely to be scaled down (with bearish connotations for the US dollar).

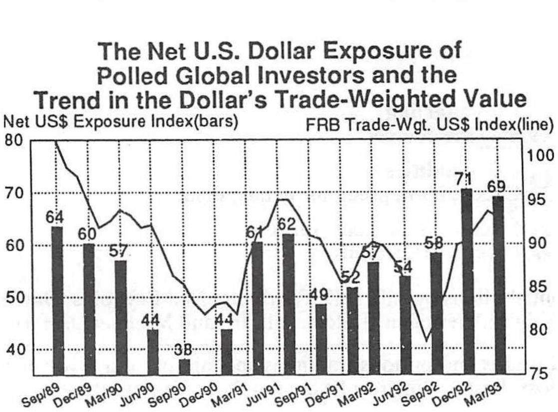
In sum, the expectations for a widening divergence in economic activity between the US and Europe (principally Germany and the UK), which underpinned a bullish US dollar scenario, may be changing at the margin. At the same time, negative US short-term interest rates and the still-wide yield curve tell us that we're in the presence of an inflationary monetary policy.

We conclude that in the medium term, the US dollar will continue to weaken.

STRATEGY: *After three aborted attempts to capitalize via purchases of DM and yen on the coming weakness of the US dollar, we settled on a new buy recommendation of the Swiss franc. Improving fundamentals and cheapness* vis à vis *the DM (see DM/SF cross rate) should provide us with a double-barrelled gain: Up against the DM, which in turn, should rise against the US dollar.*

Long June Swiss franc at 67.30, as per Flash Update of Thursday, April 8. Raise stops to 66.90, close only.

Chart 1



Currency & Bond Market Trends, Merrill Lynch

Chart 2

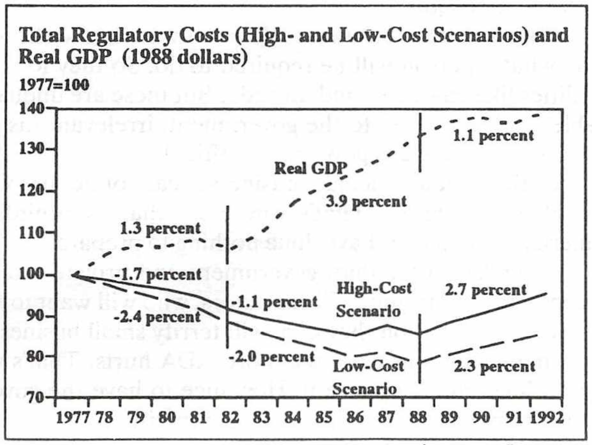
Exchange-rate forecasts

April 20th		EIU April consensus units of currency per $ 3 months	6 months	12 months
Yen 111	mean	116	118	120
	range	110-124	112-130	105-135
DM 1.60	mean	1.66	1.71	1.73
	range	1.55-1.75	1.65-1.83	1.60-1.85
FFr 5.41	mean	5.59	5.75	5.84
	range	5.20-6.00	5.55-6.15	5.47-6.22
Lire 1532	mean	1624	1654	1676
	range	1568-1732	1596-1760	1536-1856
£* 1.54	mean	1.49	1.48	1.47
	range	1.39-1.63	1.35-1.65	1.33-1.59
C$ 1.26	mean	1.26	1.26	1.26
	range	1.25-1.30	1.21-1.30	1.19-1.30
Ptas 116	mean	119	122	124
	range	116-125	117-132	118-140
A$ 1.39	mean	1.42	1.40	1.37
	range	1.38-1.47	1.35-1.47	1.30-1.47
SKr 7.39	mean	7.78	7.92	8.05
	range	7.56-8.30	7.61-8.73	7.58-9.02
SFr 1.46	mean	1.52	1.56	1.57
	range	1.48-1.61	1.51-1.67	1.48-1.68

*$ per £

The Economist

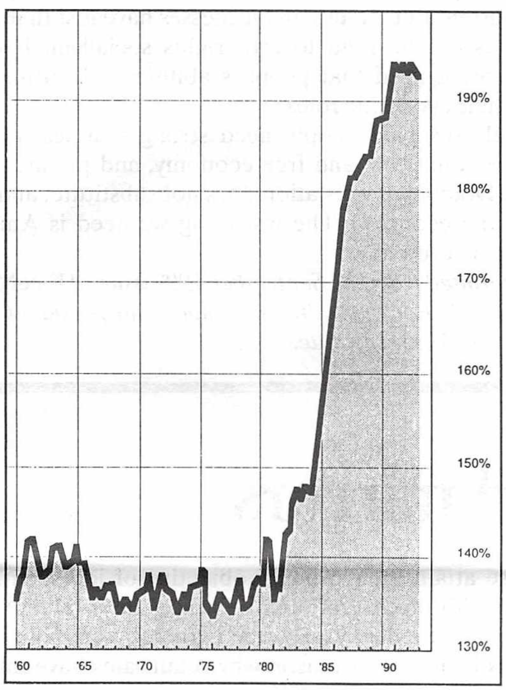
Chart 3



National Economic Trends,
Federal Reserve Bank of St.Louis

Chart 4

Total Debt as a % of GDP [1960-1992]



THE FRC MONEY-FORECAST LETTER

Chart 5 – CME SWISS FRANC JUN '93

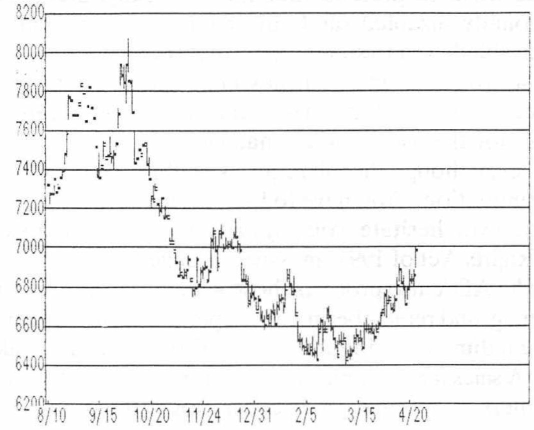


Chart 6 – SF per DM

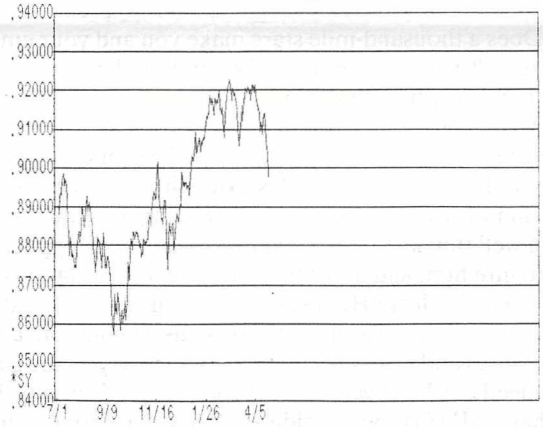
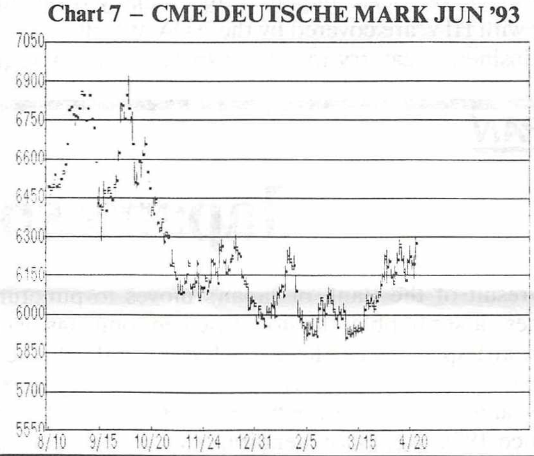


Chart 7 – CME DEUTSCHE MARK JUN '93



COMMENT

Disabling the economy

by Llewellyn H. Rockwell, Jr.

If we are looking for the reason our "recovery" is indistinguishable from a recession, regulatory legislation like the Americans With Disabilities Act (ADA) is a good place to start.

Leftists have long based social policy on the idea that all people are exactly alike, or should be forced to behave as if they were. But with the most wacky piece of egalitarian legislation in history, the feds have surpassed themselves.

Unlike the expensive Clean Air Act, for example, the ADA is not industry specific. It affects every business in the country with 25 employees or more (and 15 or more by 1994), forcing them to pretend that the physically, mentally, and emotionally disabled (and "disabled") are identical to the non-disabled, and to spend to make it so.

Say you're a small businessman, barely alive thanks to the recession and high taxes, and a man who cannot see applies for the job of office manager. You cannot turn him down, even though the job requires reading, for that would be "discrimination." You have to hire another employee to read to him. If you hesitate, you pay back wages and, thanks to the Civil Rights Act of 1991, massive damages.

The ADA also protects those who have trouble learning, reasoning, and remembering. If a supermarket manager refuses to hire a dimwit to ring the cash register, he can be taken to court. A sales manager may prefer salesmen who can remember customers' names and preferences, not to mention products, but discrimination against the memory impaired is not allowed.

People with emotional problems (which do not include being driven crazy by radical egalitarianism) are included as well. Does a thousand-mile stare make you and your employees uneasy? You're out of luck, for this is no longer a chilling quirk but a certified disability.

Would you rather not hire a warehouseman with a history of drug use? If he's off crack this week, he's on your payroll.

Say the applicant is a dyslexic with a history of drug addiction who not only has trouble reading, but can't learn or reason well thanks to minor brain damage. If he applies, you have to hire him, and make necessary accommodations.

Thanks to Jesse Helms, the ADA (until it's amended in the Clinton Administration) allows discrimination against transvestites and transsexuals. But not to worry — the gender challenged can be covered under some other disability. They may have AIDS or be considered loony. Or perhaps they're fat or ugly; the scale impaired and facially disabled, like those with HIV, are covered by the ADA as well.

Businesses can try to escape some of this by requiring certain abilities in a written job description, but they must be able to show, in a court of law, that the requirements are essential to the job.

Unfortunately, businesses do not always know ahead of time what a person will be required to do. So they look for qualities like character and attitude. But these are unquantifiable, and therefore, to the government, irrelevant (as you can tell by visiting any government office).

Until the courts decide, businesses cannot be sure what compliance requires. That's why more than two-thirds of American companies have done nothing to prepare.

To make up for that, government and private interest groups will use "testers." These actors, who will want to find all the discrimination they can, will terrify small businesses. The smaller the business, the more ADA hurts. That's why big business didn't oppose it. How nice to have the government clobber your up-and-coming competition.

How could this legislation have passed? In Washington, D.C., economics takes a back seat to special interest lobbying. Both the Bush administration and the Democrats favored the bill, and few dared to speak the truth.

A free market means allowing owners to hire, fire, promote, and pay based on their assessment of an employee's contribution. But American businesses have lost that ability, setting us on the road to civil rights socialism. Even the Soviets recognized that people's abilities and attitudes affected their economic roles.

Truly disabled people need strong families, personal initiative, a growing and free economy, and private acts of charity. Draconian legislation does not substitute, and it can cripple the economy. The last thing we need is American business on crutches.

Reprinted from the September 1992 issue of FreeMarket. *Llewellyn H. Rockwell, Jr., is founder and president of the Ludwig von Mises Institute.*

JAPAN

Japan's smoke and mirrors

As a result of the Bank of Japan's moves to puncture the Japanese asset bubble, the domestic economy has been in a downward spiral since the end of 1990. Indeed, the gross domestic product (GDP) is now registering negative year-over-year growth. That's the first time negatives have popped up since 1974. Capital expenditures have been contracting since the first quarter of 1992. Retail sales have moved up sharply into negative territory. Exports have remained flat as the international economy has remained weak and the yen has soared.

Interestingly, unemployment has moved up to only 2.3% today from 2% a year ago. That remarkably good performance has been the result of Japan's flexible wage contracting system. Only about 65% of wages received by Japanese workers is guaranteed. The remainder is dependent on company profits.

In good times, workers receive fat bonuses, and in lean times those bonuses are slashed. Consequently, wages fluctuate with changes in company profits in Japan, but employment remains rather stable. This is the way in which the Japanese attain their primary objective of job security. At present, with profits contracting, wages have fallen rapidly. Indeed, over the last year, wage earnings have fallen about 5%. This is the major reason why retail sales have fallen by 5.5% over the same period.

Japan's recession and deflation — producer prices are falling at a negative 2.3% measured year-over-year — shouldn't surprise us. Fiscal policy has been very tight, and more importantly monetary policy has been supertight, with the M2 + CD measure of money supply currently contracting at about a 4% annual rate.

Facing intense pressure from other members of the G-7, particularly the Clinton Administration, the Japanese government announced its second stimulus package within the last year. Chart 8 shows the elements of the package and the Ministry of Finance's projections of what the package is intended to do for the economy.

Like the August 1992 package, the April 1993 package is little more than smoke and mirrors. Indeed, given the magnitude of Japan's deflation and its tight fiscal and monetary policies, the latest package is peanuts. The new package, like the one before it, will not be enough to pull the economy out of its downward spiral.

Independent analysts agree with that assessment. For example, the Sakura Research Institute estimates that the package will add 1.2% to nominal gross national product (GNP), the Dai-Ichi Kangyo Bank 1.3%, and Baring Securities 0.8%. Those independent estimates are probably too generous. Consequently, even with the second stimulus package, Japan's economy will remain mired in a recession or very slow growth at best.

That pessimistic conclusion will materialize because there is virtually nothing in the package to stimulate money growth. Moreover, the Bank of Japan gives no indication that it wants to allow any gas to be injected into the "speculative bubble." Without significant growth in Japan's money supply, Japan will go nowhere fast. Indeed, even if the money supply is boosted, it will take a year or so before nominal GNP picks up.

The domestic economy and particularly the all-important private sector in Japan can't become motivated until the money supply and credit begin to grow. To further appreciate that, consider that outstanding commercial bank loans expanded by only 1.3% in March, the slowest growth on record, and a sign that banks are incapable of fresh lending and/or that the demand for corporate funds is still in decline.

The only way that the banks can expand credit to support more private investment expenditure is if those debt-burdened institutions are reliquified. That would require Japan's relatively flat yield curve to become much more positively sloped, which implies that the Bank of Japan would have to further cut short-term interest rates, much the same way the US Federal Reserve did over the past year and a half. That said, it is important to stress that there has been no indication that the Bank of Japan has any intention of aggressively reducing short rates, as that would jeopardize its entire bubble deflation strategy.

So, with a peanuts fiscal package, negative (or flat) money growth, and no reliquification of banks via a more steeply sloped yield curve, Japan's domestic economy will remain in the tank during 1993. But won't growth in the export sector be enough to pull Japan out of its slump? No!

Japan's exports have been flat in recent quarters and will remain so. The soaring yen, which has appreciated 11% *vis à vis* the US dollar in recent months, will see to that. Indeed, with Japan's huge current account surpluses exceeding its private sector capital outflows, the yen has only one way to go: up! (For the complete analysis of the yen's fundamentals, see our February issue.)

IMPLICATIONS: *Japan's domestic economy as well as its export sector will remain depressed for 1993. Consequently, the price of Japanese long bonds will move up, and the prices of Japanese equities will move down. As for the yen, flows of international capital will continue to dictate further yen appreciation.*

Dr. Steve H. Hanke

Chart 8 – Japan's Fiscal Packages

	April 1993 measures (¥bn)	August 1992 measures (¥bn)
Increase in public investment		
Public works	4,170	4,450
Investment in education & social welfare	1,150	550
Investment by local government	3,600	2,800
Housing loans	1,800	800
	10,620	8,600
Lending by financial institutions		
Measures for small and medium-sized firms	1,910	1,200
Promotion of private equipment investment	520	900
	2,430	2,100
Total	13,050	10,700
Multiplier effect in per cent of GNP	2.6%	2.4%

Source: *Ministry of Finance*

NIKKEI INDEX

A classic bull trap

The Nikkei's spectacular six-week and 24% runup — aided and abetted by a well orchestrated manipulation of NTT shares (see our March comments), which rose an incredible 74% during this span of time — is now over.

In the five months to March, volume had been so light that for all practical purposes, the exit had been denied. The excitement generated by the rise, however, allowed many trapped institutions to lighten their holdings. A classic bull trap.

Who were the hapless souls who so generously and so gallantly extended their cloak over the wet pavement? None other than foreign investors and Japanese individuals *buying on margin* (see Chart 10).

STRATEGY: *Maintain long positions in Amex put options.*

Chart 10

Net sales (-)/purchases on Tokyo, Osaka, Nagoya stock exchanges*

Feb. 25 - April 7	**¥/bn**
Financial companies/trusts	-815
Other companies	-310
Retail — cash	-228
— margin	568
Foreign	613

Source: *Nikko Research Institute*

*First and second sections

Chart 11 – CME JAPANESE YEN JUN '93

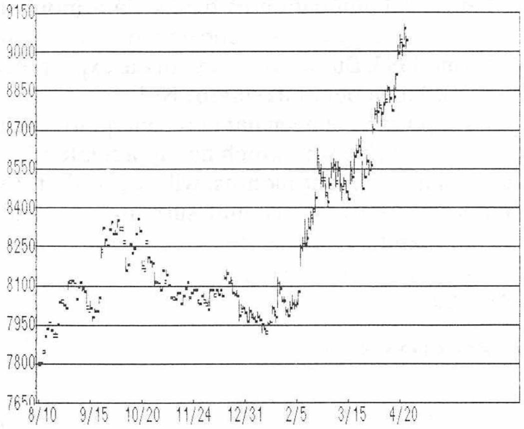
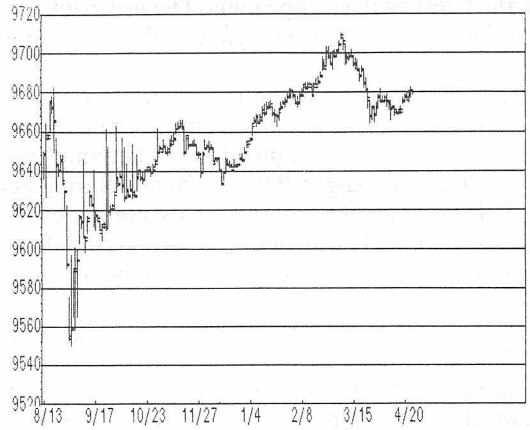


Chart 12 – SIMEX EUROYEN SEP '93



CANADA

Spending out of control

As economists know, all that people really want is more. More is relative. Psychological studies show that people who live in high-growth, low-income countries often deem themselves better off than do people who live in low-growth, high-income countries. Momentum determines mood. People are motivated and optimistic, whatever their incomes, when more labor produces more reward. This psychological dynamic helps explain the profound grumpiness that pervades some of the world's wealthiest nations.

Paradoxically, the wealth of a nation isn't always a reliable measure of the wealth of its people. By the standard of per capita GDP, Canada is wealthy and getting wealthier. By the standard of real, per-worker income, Canadians are getting poorer. Real per-worker income peaked in 1976, fell by 10% in the recession of the early 1980s, gained back more than half of the loss in the boom years that followed, and then fell back again in the recession of 1991-92. It's a bear market in Canadian per-worker income. The down cycle has lasted 17 years.

Consumption is the ultimate objective of all economic activity. Are people moving forward, or are they moving backward? Are they moving at all? In the long run,only real productivity gains can increase real per-worker incomes; and statisticians appropriately measure productivity on a per-worker basis. Examined from this perspective, what's actually happening in Canada is the prolonged spinning of many wheels. Canada is a Cadillac on blocks.

After almost two decades of going nowhere, the illusion of motion persists. GDP has risen inexorably, and money has circulated in greater and greater abundance. From 1983 to 1990, the public demand for $1,000 bills grew at an average annual compound rate of 17% — the credit card economy not withstanding. The proportion of two-income households doubled, and family incomes rose.

The paradox, though, remains. Canada appears to have grown richer as a nation as its labor force, its working citizens, have grown poorer — another year older, annually for 17 years, and deeper in debt. In one way or another, in other words, the State itself has consumed *all* of the country's productivity-generated advances since 1976.

Constant dollar statistics across the past 40 years document this acquisitive process:

	Real GDP Growth	Real government expenditure growth
1950s	3.3%	4.7%
1960s	5.4%	6.5%
1970s	4.4%	5.1%
1980a	3.3%	3.6%

Thus, in the '50s, Canadian governments expanded expenditures by a margin 42% greater than GDP growth; in the '60s, by a margin 20% greater; in the '70s, by a margin 15% greater; in the '80s by a margin 25% greater.

The phenomenal rise in Canadian government expenditures in the '50s and '60s reflected the assembly of the post-war welfare state, and roughly tracked the expansion of government spending in other Western countries. This public sector expansion took place from a low base: The combined expenditures of all Canadian governments in the early '50s required only 20% of GDP. By 1980, government expenditures needed 40% of GDP; and direct, personal taxes alone consumed 400% more of people's disposable incomes (up from 6% in 1950 to 24%). Two recessions, one boom, and a decade of government "restraint" later, government spending claims 50% of GDP; and although much of the recent increase has been financed by debt, taxes have continued to spiral.

Governments cannot forever increase spending at rates that exceed the growth of the economies they purport to manage. Contrary to our nostalgic recollection now, as the numbers above show, Canadian governments were most grasping of GDP in the '50s; they took proportionately less GDP in each succeeding decade. If there's good news anywhere, it's this relative decline in grasp. The fact remains, however, that Canadian governments are still confiscating GDP at a faster clip than the nation can produce it. Even in an atmosphere of unprecedented crisis, Canadian governments are unable to produce, even for a single year, a budget with no new grasping.

In 1993-94, government spending will probably rise to 55% of GDP. In British Columbia and Ontario, where socialist

NDP governments are pressing the pedal to the metal, government spending will grow by a growth-plus margin that makes governments of the '50s look like Sunday drivers.

British Columbia and Ontario produce more than half of Canada's GDP. Thus far in the '90s, the two provinces have increased government spending by precisely the same proportion — on a per capita basis, by 36%. In 1992-93, British Columbia increased spending by 14%, or three times its growth in GDP; for 1993-94, in delivering what the government described as a tough budget, the province will increase spending by 6%, or twice the expected growth in GDP.

A two-year span in one province is not as useful a guide as a 10-year span in the country, but it's still illuminating. In these two budgets, British Columbia will have increased spending by a growth-plus margin of 60%.

The same revving up of public spending is taking place in Ontario, although the province's panic over its deficits have obscured its increases in expenditures. The deficit problems are real enough. Excluding nations, Ontario is the world's biggest borrower. Its 1992-93 deficit, budgeted at $10 billion, will be closer to $14 billion. Finance Minister Floyd Laughren has warned that the 1993-94 deficit could hit $17 billion; that the accumulated deficits in the next four years could reach $80 billion.

Ontario attributes its deficit problem to a revenue problem. It asserts that revenues have collapsed (although lower than the government had projected, they are rising) and that higher taxes are needed to restore them. Yet in an economy expected to grow in 1993-94 by 3%, the provincial budget in May will probably increase government spending in real-dollar terms.

The government has proposed a public-sector wage freeze of some sort (which they've termed the "social contract") and a wide range of tax increases. A rollback of public-sector payroll is self-evidently appropriate. In zero-growth 1991, when it took office, the NDP engineered a one-year, 12% increase in its payroll costs; it gave nurses a 17% pay increase over two years. Such reckless acts of largesse have cost the province an amount of money roughly equal to its 1993-94 deficit gap, the difference between the deficit it wants ($10 billion) and the deficit it doesn't want ($17 billion).

Ontario's "social contract," however, will now come at very high cost. The public-sector unions will cooperate only if the government imposes what they regard as comparable private-sector suffering. In particular, they want tax increases on businesses and on "wealth." Here, the government has already obliged. One example: In 1993-94, it will arbitrarily reduce medicare payments to Ontario's 22,000 doctors by $275 million, or $12,500 each. In the inevitable controversy that follows, though, the central issue may well be lost. In the past, government-imposed wage controls have proven to be a good indicator that *the worst is yet to come.*

What does Ontario propose to do with its increased share of GDP? As dictated by current interventionist theory, it proposes to invest it. Government investment is a classic oxymoron, a contradiction in terms. The government, nevertheless, proposes to form an economic "partnership" with corporate Ontario; to set up shop as Ontario's venture capitalist of last resort; to function as Ontario's low-interest lender of last resort. Predictably it proposes to invest in unproductive plants to preserve uneconomic jobs. In other words, Ontario will increase taxes and invest the proceeds in the further absorption of what's left — a leveraged buyout, really, of the remnants of the province's private sector economy.

This process must further impoverish the province. Government investment can build expressways, but it can't produce better Cadillacs. In its economic analysis, Statistics Canada assumes zero real productivity growth in the entire public sector. In many cases, of course, zero productivity growth is a wildly charitable premise. In Ontario, one worker in five is now a public-sector employee, a significant proportion of a labor force to excuse from the imperative of productivity. And, following due legislative reflection, it is this unproductive public service that administers all government investment.

Governments err as investors because they regard investment as an economic end in itself. Investment, though, is only a means; economic growth itself is only a measurement of a means. GDP measures all investment, productive or not. Investments that do not yield productive gains, however, do not increase real per-worker incomes. Unless investments do yield productive gain, they must by definition destroy wealth, erode real per-worker income, and, eventually, reduce consumption.

In the past 17 years, the average annual per-worker increase in productivity has been 1%. In the past century, almost all of the increase in per-worker income has come from productive investment in processes and equipment that conserved human labor. Governments invariably invest to preserve the present. In doing so, they stall the future.

Canadian economist Dan Usher has calculated the negative-productivity return of Canadian government spending and Canadian government investment at $1.35 in deadweight losses for each additional $1 gain in expenditure.

This is relevant for investors who are trying to assess Ontario's ability to pay its debts. Its importance, though, transcends dollars and cents. As governments direct progressively larger portions of GDP, at what precise point of private-sector erosion does a market economy discover that it is not primarily a market economy any longer? That it is now primarily a socialist economy? No one knows. Many economists, though, would say that 35% of GDP signals long-term danger and that 40% signals imminent danger.

Many OECD governments have passed these markers with apparent immunity. Time will tell; perhaps, in many of these cases, time is already telling. Canada, incidentally, surged past the 35% marker, and into the danger zone, in 1976.

Political determination of investment must result in progressively lower gains in productivity and in lower real per-worker incomes. It must result in chronic economic stagnation. As capitalist equity gives way to socialist equity, it must ultimately lead to social unrest and physical conflict.

Public command and control of GDP, in other words, must ultimately destroy the market economy and imperil democracy. As Professor Usher has persuasively argued, "the trend to ever-greater political assignment of income must lead to an economic organization no longer consistent with democratic government."

It's government spending that matters here, not whether the spending is funded by tax increases or by public debt. And government spending in Canada remains out of control.

– Neil Reynolds

CANADIAN DOLLAR

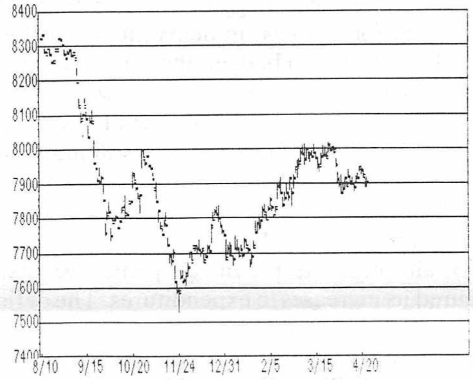
Too early to short

The bank has managed to stabilize the currency while *short term fundamentals* improve, reflecting the cheaper currency and a disciplined monetary policy.

We'd love to short it, but we sense it's still too early.

STRATEGY: *Stand aside.*

Chart 13 – CME CAN. DOLLARS JUN '93



STOCK INDEXES

Timid bears

If markets are not compartmentalized — and there's no reason why they should be — then the foreign exchange market's apprehensions (see our opening article) about the buck should spill over into the US equity markets.

In effect, are 23x multiples and 2.9% yields justified in an environment of no growth (at best), a weak currency, and rising inflation (see our Commodities section)?

If the answer is no, you ought to be short the S&P 500.

STRATEGY: *Two unsuccessful attempts to short outright the market have restored our humility. We now prefer to be characterized as* timid bears *(until we fully understand what makes this market tick) who appreciate the safety and comfort of cheaply-priced put options.*

Long December 400 S&P 500 put options at around 7.50.

Chart 14 – CME S&P 500 INDEX

LIRA/STERLING

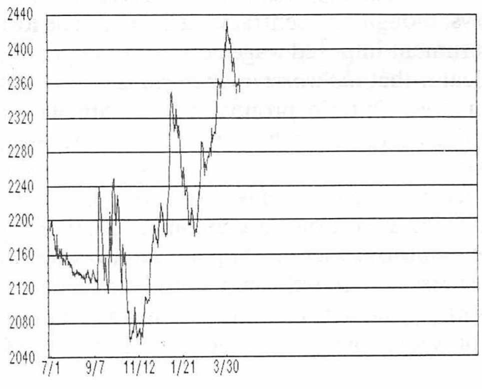
Stay the course!

With the referendum out of the way, it now remains to be seen if the Italian people are as sensible in economic matters as in political matters.

We want Amato!

STRATEGY: *Stay long the lira/short Sterling, as the latter can't stand prosperity.*

Chart 15 – LIRA PER £



COMMODITIES

Commodity prices retreated marginally since last writing in the wake of economic news that on balance indicated the US economy was performing somewhat more weakly than was generally assumed. The Commodity Research Bureau Index (CRB), which is our benchmark, and our current portfolio follow:

Commodity	Change in Month
CRB	- 0.7%
Corn	- 1.9%
Cocoa	0.9%
Silver	6.1%
Gold	3.9%
Sugar	1.3%

We remain of the opinion commodity prices are in the incipient stage of an inflationary phase. Weakness in the grain and meat sectors has been counterbalanced by strength in the soft commodities; cocoa, orange juice, coffee, and sugar. Declining base metals' prices have been nicely compensated for by rising precious metals' prices.

In addition to the healthy rotation, a majority of commodity markets have now tilted their way out of downtrends. Finally, the recent weakness of the US dollar has priced dollar-denominated commodities extremely attractively.

These factors, coupled with the monetary argument from which we constructed our thesis for rising commodity prices back in October 1992, lead us to conclude the current weakness is temporary. We advise overall portfolios be between 4% and 5% invested in commodities.

Cocoa

First quarter 1993 grindings figures indicate robust demand. The US and UK grinds are up by 21.3% and 11.9% respectively. Dutch grindings were also reported higher. The global grind for the whole (cocoa) year (which ends in September) is estimated at a record 2.4 mln tonnes.

The strong demand comes in response to the extreme price weakness of recent years. The price weakness, of course, has come in response to the frustratingly large supply overhang. This year, production is estimated at 2.31 mln tonnes. Extreme dryness is expected to hinder Brazilian exports. However, the dry conditions that were expected to imperil West African crops appear to have been alleviated as evidenced by Ghana's cocoa (COCOBOD) predicting the crop in that country will total some 280,000 tonnes, or some 2% higher than predicted earlier.

The supply situation up to this point in the year is governed by Ivory Coast's ban on sales of its mid-crop, which is harvested from May through September. The crop has been put as high 150,000 tonnes compared with the five-year average of 120,000 tonnes. So far, despite trade scepticism that the ban can be effectively maintained, the crop has yet to find a market. Undoubtedly the question is only one of timing: Either the mid-crop ban will be derailed by cheating or mid-crop beans will be sold with the main crop later this calendar year. Until the issue is resolved clearly, volatility will result.

The West African crop situation in general testifies to the continuing supply burden. Although the past several years of low prices have discouraged any new plantings, plantings made during the 1980s in the Ivory Coast, Malaysia, and Indonesia are just now approaching their maximum yield stage. As a result, it will take a surprise dislocation — a weather-related problem for example — to create a bull market of any major proportion.

Nonetheless with prices trading at more than 25% beneath the average production cost of the commodity (according to the Goldman Sachs *Commodities Analyst* of March 1993) and near technically very-firm support zones, cocoa is the most undervalued and least-risky commodity on the board.

STRATEGY: *We are staying long with stops still at 800, basis cash.*

Corn

Spring planting intentions call for 76,500 million acres devoted to corn compared with 79,000 million acres estimated at this time last year. In addition the late and wet spring has delayed plantings. Export sales have been brisk and are expected to total some 3% to 5% higher this year than last.

Nevertheless, more average yields and diversion of flax acreage to corn at the expense of soybeans are expected to ultimately result in substantially increased production and year-ending stocks.

The current rally is the risk premium users must pay as insurance against irrecoverable losses that might result from any interminable delays to putting the crop in the ground.

STRATEGY: *At this point we would take profits if the rally can carry prices to the 245 area, basis July. Stops remain at 217, basis May.*

Precious metals

Over the last three years, silver supplies have fallen short of consumption by 37 mln ounces, 46 mln ounces, and (an estimated) 53 mln ounces respectively. With consumption in the 550 mln ounce range, the current deficit approximates better than 10% of usage. At the same time, silver prices remain 10% less than the average cost of production (according to Goldman Sachs).

Such a condition cannot persist. We believe silver prices must continue the rise we have enjoyed since February. Silver — along now with gold — remain critical assets in our commodities portfolio.

STRATEGY: *Stops at 325 ,basis cash gold and 345, basis cash silver.*

Sugar

A typo in last month's letter obscured our sugar strategy. We had intended to advise buying calls on the October position if that delivery fell to 10.50. October fell to 10.75. Nonetheless we again want to be long futures. Our reasons follow.

The full effects of the drought on the Thai sugar crop are now known. Production is reliably forecast to drop from 47.5 mln tonnes to 34.85 mln tonnes. Thailand exports 12.2% of total world trade in sugar and is the world's second largest sugar exporter behind Cuba. The crop disaster means that Thai exports will be some two-thirds less than they were last year.

Cuban sugar exports are expected to shrink as production in the beleaguered Island nation is forecast to decline by perhaps as much as 1.5 mln tonnes over last year.

In addition, exports from Brazil will be curtailed by 500,000 tonnes in the wake of that country's decision to process the sweetener into methanol rather than import more of the fuel additive.

It seems likely that this year there will be a sugar deficit of as much as 2.0 mln tonnes. More importantly, the deficit comes specifically as a result of crop difficulties experienced by the world's principal exporters. Although there are ample supplies of sugar warehoused from previous surplus years, it is now not unlikely that temporary dislocations will occur unless the price rises to seduce those supplies to market.

STRATEGY: *Buy July with stops at 1025.*

– David B. Rothberg

Chart 16
N.Y. #11 SUGAR JLY '93

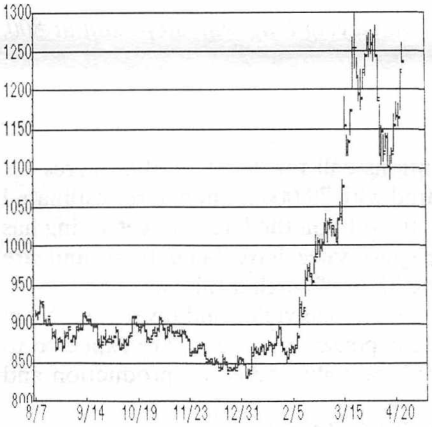


Chart 17
COMEX GOLD JUN '93

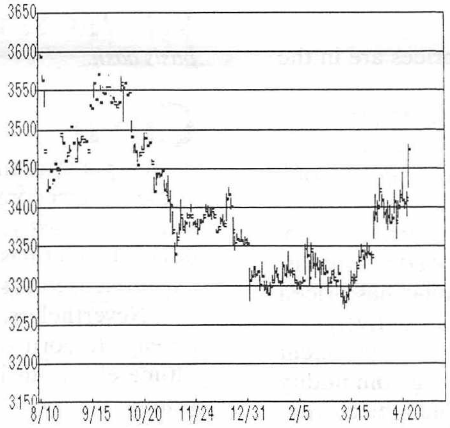
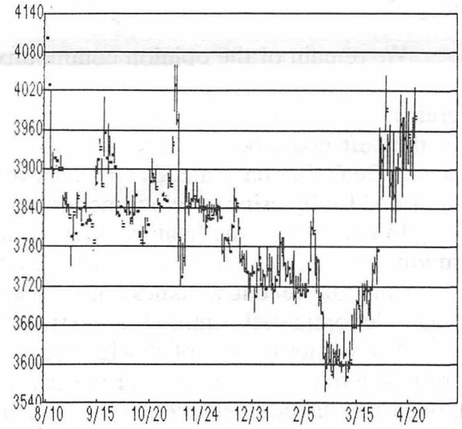


Chart 18
COMEX SILVER JLY '93



FRIEDBERG CAPITAL MARKETS

Diceon Electronics

The company announced financial results for the second quarter ended April 3, 1993.

Net sales decreased to $23,305,000 for this fiscal year compared with $25,875,000 in the second quarter of fiscal 1992. Diceon recorded a net loss of $8,394,000, or $1.63 per share, compared with a net loss of $2,980,000, or 58¢ per share, for the second quarter of fiscal 1992.

The main factors causing the loss were the continuing slowdown of business from the telecommunications sector and the closure of the Chatsworth operating facility for which the company has accrued a one-time charge of $3,000,000 recognized in this quarter.

In connection with the closure, Diceon reduced its workforce by approximately 100 employees and transferred the majority of the advanced fabrication to Irvine and the company's New Hampshire facility.

Business continues to disappoint. Gross margins have once again become negative.

The company's working capital deteriorated slightly more than $7,000,000 in the past six months. Total debt to market capitalization at 5.2x is an ominous sign.

We are placing the securities on alert as signs of financial stress begin to mount. No more purchases are recommended at this time pending the outcome of the present restructuring efforts and perhaps more drastic ones yet to come.

Chart 20

Recommended bond portfolio allocation for new portfolios

For new portfolios, we recommend the following investments:

Finnish Markka fixed rate bonds	15%	Argentina BICV	22%
Italia Lira fixed rate bonds	25%	New Zealand 5 year Govt. Stock	13%
US $ high yield CV bonds	25%		

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$, A$, DM, SF, DKr, BP, FFr, ECU, CD, SAR, ITL, ARG, FIN) or revalue for SF, JY before the interest rate advantage/disadvantage is overcome by currency depreciation/appreciation. **Rates as of Thursday, April 22, 1993.**

	U.S. $	NEW ZEALAND	AUSTRALIAN $	DEUTSCHEMARK	SWISS FRANC	JAPANESE YEN	DANISH KRONE	BRITISH POUND	FRENCH FRANC	EUROPEAN CURRENCY UNIT	CANADIAN DOLLAR	SOUTH AFRICAN RAND**	ITALIAN LIRA	ARGENTINEAN PESO	FINNISH MARKKA
1 year	3.15%		C.B.A. '94 yields 5.68% (.6937 A$/US)									ESCOM 11% '93 yields 11.95% (.1975 US/SAR)			
2 year	3.72%						Denmark '94, yields 8.72% (6.764 Dkr/US)		Credit Lyon '96 yields 7.32% (5.8048 Ffr/US)						Finland '95 yields 8.11% (6.0287 FM/US)
3 year	4.12%			Bk. N.S. '96 yields 6.47% (1.7178 US/DM)		World Bk '96 yields 3.76% (108.90 US/JY)		Sweden '96 yields 7.07% (1.4249 BP/US)			Ont. Hydro '96 yields 7.31% (1.3827 US/CD)		GE '95 yields 9.28% (1.7597 ITL/US)		
4 year	4.57%	NZ '97 yields 7.07% (.4904 NZ/US)		World Bk. '97 yields 5.67% (1.6752 US/DM)							Eksport Fin '97 yields 7.46% (1.4085 US/CD)		NIB '96 yields 10.08% (1.869 ITL/US)		
6 year	5.11%				Australia '98, yields 4.58% (1.413 US/SF)										
8 year	5.71%			World Bk '00 yields 6.43% (1.6962 US/DM)						U.K. '01 yields 7.61% (1.0543 ECU/US)				BIC V '01 yields 17.15% (2.27 US/ARG)	
Spot Exchange Rate	–	.5390	.7107	1.6065	1.4565	110.04	6.156	1.5495	5.4220	1.2158	1.263	.2143	1.522	.998	5.549

*For example, since a US$-based investor would receive 516 basis points (928-412) by holding the General Electric ITL bond, the ITL/US can depreciate to 1.7597 ITL/US from the present spot exchange rate of 1.522 ITL/US over the next 3 years for the ITL investment to break even with current US$ rates of interest. Assumes that bonds are held to maturity, and coupons are reinvested.

**NOTE: These bonds pay interest in commercial rand, which presently trades at a premium to the financial rand used for this table.

HOTLINE UPDATE

Tuesday, March 30:
A typographical error occurred in our last market letter in the sugar strategy. It should read as: "We would advise the purchase of October sugar calls below 1050."

The market letter is in the mail.

Flash Update, Friday, April 2, 2:00 p.m.:
Unfortunately, we were stopped out of our short S&P positions as the market moved earlier this week above 455.00

Our new recommendation: Sell S&P futures at the market, place initial stops at 446.00, good anytime.

Friday, April 2:
This is a recap of recommendations for the week.

On Tuesday, March 30 we made a correction in our last market letter in the sugar strategy. It should read as: "We advise the purchase of October sugar calls below 1050."

For Friday, April 2, based on our flash update earlier this afternoon, we sold June S&P futures at approximately 443.70, establishing a new short position. We placed initial stops at 446.00, good anytime.

Monday, April 5:
This is a repeat of Friday, April 2 recap of the week.

On Tuesday, March 30 we made a correction in our last market letter in the sugar strategy. It should read as: "We advised the purchase of October sugar calls below 1050."

For Friday, April 2, based on our flash update, we sold June S&P futures at approximately 443.70, establishing a new short position. We placed initial stops at 446.00 good anytime.

The next Hotline Update will be on Thursday, April 8.

Flash Update, Thursday, April 8, 9:23 a.m.:
Cover short Canadian dollar positions at the market, currently trading at .7932, and in addition buy June Swiss franc at the market, currently trading at 6730. Keep in touch for stop level in the Swiss franc.

Thursday, April 8:
This is a repeat of this morning's flash update to cover short Canadian dollar positions at the market, then trading at 7932, basis June.

Also, buy June Swiss franc at the market, then trading at 6730. Place stop on the Swiss franc at 6621, close only.

Please note Friday, April 9 the office is closed. The next Hotline Update is Wednesday, April 14.

Wednesday, April 14:
There are no changes or new recommendations.

Flash Update, Thursday, April 15, 5:20 p.m.:
Sell August crude oil at the market, adding to outstanding put option positions. Place initial stop at 2115, good anytime.

Friday, April 16:
This is a recap of recommendations for the week.

On Thursday, April 15, via flash update we recommended to sell August crude oil at the market, adding to outstanding put option positions; place initial stop at 2115, good anytime.

Tuesday, April 20:
There are no changes or new recommendations.

Flash Update, Friday, April 23, 10:00 a.m.:
Buy December S&P 400 strike put options at the market, currently trading at 7.50.

Friday, April 23:
This is a complete summary since our last market letter dated March 28 of all liquidations of open positions and new recommendations that remain outstanding.

On Thursday, April 8 we covered short Canadian dollar positions at approximately 7932, and we purchased June Swiss franc at approximately 6730. Stop on the Swiss franc was placed at 6621, close only.

On Thursday, April 15 we sold August crude oil at approximately 2040. Stop on the crude oil was placed at 2115, good anytime.

On Friday, April 23, via flash update, we bought December S&P 400 strike put options at approximately 7.50.

Chart 21

Date: April 22,1993

WE OFFER THE FOLLOWING BONDS SUBJECT TO CHANGE WITHOUT PRIOR NOTICE: MINIMUM US $5,000 (CDN. $7,000)

ISSUER/MATURITY DATE/COUPON	BID	OFFER	CURR. ANNUAL YLD. TO MTY.	NEXT PAYMENT INTEREST DATE
DEUTSCHE MARK DENOMINATED				
BANK OF NOVA SCOTIA 5⅝% 07/05/96 RRSP eligible	97	97 3/4	6.47%	May 07
WORLD BANK 5⅞% 4/02/97 RRSP eligible	99.90	100.65	5.67%	Feb. 04
WORLD BANK 9% 13/11/00 RRSP eligible	114.15	114.90	6.43%	Nov. 13
FINNISH MARKKA DENOMINATED BONDS				
REP. OF FINLAND 11% 15/6/95	104.65	105.40	8.11%	Jun. 15
ITALIAN LIRA DENOMINATED BONDS				
NORDIC INV. BANK 12⅜% 19/04/96	104¼	105	10.33%	Apr. 19
GENERAL ELECTRIC 11½% 7/02/95	102¼	103	9.52%	Feb. 07
SWISS FRANC DENOMINATED BONDS				
GOVT. OF AUSTRALIA 5% 30/10/98	100	102	4.58%	Oct. 30
DANISH KRONE DENOMINATED BONDS				
KINGDOM OF DENMARK 9% 15/11/94	99.55	100.30	8.72%	Nov. 15
ECU DENOMINATED BONDS				
UNITED KINGDOM 9⅛% 21/02/01	107.90	108.65	7.61%	Feb. 21
BRITISH POUND DENOMINATED BONDS				
KGDM OF SWEDEN 8¾% 29/5/96	103 3/4	104½	7.07%	May 29
FRENCH FRANC DENOMINATED BONDS				
CREDIT LYONNAISE 9½% 23/12/96	105.95	106.70	7.32%	Dec. 23
JAPANESE YEN DENOMINATED BONDS				
WORLD BANK 5¾% 7/8/96 RRSP eligible	105¼	106	3.76%	Aug. 07
CANADIAN DOLLAR DENOMINATED BONDS				
ONTARIO HYDRO 10⅞% 08/01/96 (semi annual)	108 1/8	108 7/8	7.31%	Jul. 08
EKSPORTFINANS 7¾% 5/11/97	100¼	101	7.46%	Nov. 05
ROYAL BANK OF CANADA 9⅛% 7/1/97	103 3/8	104 1/8	7.77%	Jul. 07
SOUTH AFRICAN RAND DENOMINATED BONDS				
ESCOM 11% 31/10/93 (semi)	98.80	99.55	11.95%	Apr. 30
AUSTRALIAN DOLLAR DENOMINATED BONDS				
COMMONWEALTH BANK OF AUSTRALIA 14% 01/07/94	108 3/8	109 1/8	5.68%	Jul. 07
NEW ZEALAND DOLLAR DENOMINATED BONDS				
NEW ZEALAND GOV'T 10% 15/7/97 (semi)	109.80	110.55	7.07%	Jan. 15
ARGENTINEAN PESO DENOMINATED BONDS				
ARGENTINA BIC V FIXED/FLOATING 1/05/2001 callable in full on every interest date	88.15	88.90	17.19 IRR	4th day of mth.
U.S. DOLLAR DENOMINATED FIXED CONV. BONDS				
DATAPOINT CORP. 8⅞% 1/6/06 CV @ $18.11 p/sh (semi)	78¼	80¼	12.24%	Jun. 01
DICEON ELECTRONICS 5½% 1/13/12 (semi) CV @ $39.50 p/sh	20	25	24.45%	Mar. 01
BURNUP & SIMS 12% 15/11/00 (semi) CV @ $16.79 p/sh	86	88	15.22%	May 15
ATARI CORP. 5¼% 29/4/02 CV @ $16.31 p/sh	44½	46½	17.46%	Apr. 29
COEUR D'ALENE 6% 10/6/02 CV @ $26.56 p.sh	91¼	93¼	7.03%	Jun. 10
COEUR D'ALENE 7% 30/11/02 CV @ $15.87 p/sh	115½	117½	4.77%	May 31
U.S. DOLLAR DENOMINATED FIXED RATE BONDS				
FARM CREDIT CORP. 7¾% 10/06/96 RRSP eligible	109.10	109.85	4.30%	Jun. 10
U.S. DOLLAR DENOMINATED FLOATING RATE NOTES				
UNITED KINGDOM 24/09/96 3 mo. LIBID-⅛ (qtly) *callable @ 100	99.85	100.15	3 1/16	Mar. 31

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

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