FRIEDBERG
MERCANTILE
GROUP

SECOND QUARTER REPORT 1999

FRIEDBERG
MERCANTILE
GROUP

SECOND QUARTER REPORT 1999

Dear Investor,

It was an uneven quarter, marked by progress in some sectors and setbacks in others. Moving along the spectrum of our funds, the more conservative vehicles performed reasonably well while the more speculative vehicles stumbled. Most of the funds were structured around the manager's growing unease that existing bubble conditions would soon affect the global economy.

The comments inside describe the stance taken and the tactics and strategies followed to cope with - and eventually to profit from - what will be, in the opinion of the manager, a once-in-a-generation economic and financial disturbance.

We remain highly optimistic. We have re-focused our sights and tightened up risk management procedures with the objective of earning returns, albeit modest ones, even if our scenario continues to be delayed for yet a few more quarters.

Thanking you for your trust,

Albert D. Friedberg

FRIEDBERG
MERCANTILE
GROUP

CONTENTS

FOREIGN BONDS

Friedberg Foreign Bond Fund
Friedberg Total Return Fixed Income Fund Ltd.
Friedberg Total Return Fixed Income LP
Toronto Selected International Bonds Trust

It has been a positive quarter, with gains anywhere from 0.6% to 1.9% in US-dollar terms, despite some of the most difficult trading conditions in years. The relentless rise in interest rates during these past few months marked down bond prices rather severely, with the result that most bond portfolios showed negative total returns.

While, fortunately, we anticipated most of this rise and maintained low duration exposure during the quarter, a number of situations had a negative impact. Our inflation-indexed Treasury securities (TIPS) performed well during this bond rout, though, in the end, they too provided sub-par (but positive) total returns. Also affecting our returns were the soon-to-expire S&P 500 index-linked notes, representing between 7.6% and 10% of our various portfolios. Via embedded put options, these notes offer a leveraged bear bet on the US stock market with a floor at 95% of parity and a very modest interest rate (the present coupon is 3.775%). Unfortunately, the bear bet has not yet paid off and we have borne the opportunity cost of carrying this note. Overall, our New Zealand convertible securities provided a positive but meager return as a result of the slight fall of the currency.

Our outlook calls for more inflationary pressures in coming months resulting in an ever tighter monetary policy, and eventually an inflationary business depression. As a result, we are anxious to liquefy our portfolio further, lower duration and, once again, increase credit quality. At this moment, our modified duration is approximately 3.42 (adjusting the TIPS to one quarter of the beta of long Treasuries), and our overall credit rating is slightly better than AA-. Given this posture, it is not likely that we will be able to offer returns that are much higher than 6% to 7% per annum. Nevertheless, we believe that, with our strong and liquid portfolio, we will be in an unusually privileged position to take advantage of special situations as the financial bubbles around the world begin to burst.

DIVERSIFIED TRADING PROGRAM

Friedberg Diversified Fund
Friedberg Diversified Pool
Toronto Specialized Trust-Selected Commodities Fund

Ironically, the slight losses for the quarter were a reflection of trying too much rather than too little.

We were principally affected by two factors. The first was slippage, mainly bid/ask spreads, which we estimated at around 5.4% of initial equity, or a little more than our total quarterly loss. The second was pursuing a trade that was based on sound fundamentals but that clashed with a deteriorating technical condition, namely the purchase of Nikkei contracts. We constructed a bullish case for Japanese securities, based on the fact that the Bank of Japan would continue to flatten the yield curve and succeed in bringing interest rates down to zero even as far out as two years. The abundance of liquidity and the meager returns available in the money market would, we felt, spill into the stock market *even if stock prices were still far from representing fair value*. Our basic lack of conviction in the bull case coupled with the market's poor breadth (the rally was led primarily by manufacturers and telecom/internet providers) sidelined us on the first reaction. Interestingly, the market has gone on to make new recovery highs, even as we are writing, while breadth continues to lag. Even more importantly, the financial sector is not participating in the rally, supporting our view that the recovery is not all that broad-based nor all that permanent.

The moral of the story is that one ought never to enter a trade unless one's heart is fully set on it. This idea should also protect us from over-trading, which, as we saw, cost us too much money. Easier said than done. .

In the big picture, we still believe that inflation is heating up - witness that commodity prices have been stable for a good part of the past nine months. This will eventually bring about tradable up-trends in commodity prices (instead of the choppy markets we have been experiencing), rising interest rates and bear cycles in financial markets. These notions will erupt on the scene in a surprising fashion. It's the stuff of home runs. We are certainly due for one.

CURRENCY PROGRAM

FRIEDBERG CURRENCY FUND
FRIEDBERG CURRENCY FUND LTD.
FRIEDBERG FOREX LP
FRIEDBERG SPECIALIZED TRUST-CURRENCY FUND

Here, too, we tell a story of trying too hard. A lack of interesting opportunities induced the manager to create trades, some of them based on positive carries, some on the notion that so-called commodity currencies would improve along with the better tone in commodity markets, and some on the low-risk/ high-reward bet of selling fixed-rate currencies.

The first two categories of trades were fairly conventional and were unlikely to produce dramatic returns. In fact, that is exactly what happened: selling euros and Swiss francs against the purchase of sterling and the Norwegian krona produced a grand total profit equal to just less than 1%

of initial equity. The commodity trade, where we bought Canadian, Australian and New Zealand dollars, yielded a negative 0.21% of initial equity. These trades provided fodder for the market-makers but left us dry.

The limited-risk trades entailed selling the Hong Kong dollar and the Saudi ryal. These out-of-pocket bets unfortunately did not bear fruit. We would do them again (in fact, we are still short these currencies), though we rate the probability of devaluation as still very low.

In other assorted trades, we probed the long side of two Asian currencies on the assumption that economic recovery would lift their exchange rates. They barely moved. In the meantime, transaction costs (wide bid/ask spreads on the Thai baht) left us in the red.

The major currencies are in no-man's land. The euro is too low to sell and too high to consider buying, especially in view of the rising strains inside Euroland. The yen has been contained in a fairly narrow range, thanks to heavy Bank of Japan intervention. While the path of least resistance points up for the yen, buoyed by deflationary pressures and a small amount of economic recovery, the evidence is not entirely clear.

Sooner or later, the US dollar will begin to head south, burdened by a growing current account deficit and an overly expansive monetary policy. At that time, our trading horizons will certainly broaden and opportunities will spring. We bid you to be patient, as we will try to be ourselves.

FRIEDBERG FUTURES FUND

The Futures Fund combines the Currency and Diversified programs in approximately equal weights. Please refer to our earlier comments regarding these programs.

FRIEDBERG GLOBAL OPPORTUNITIES LTD.

INTERNATIONAL FUND

The Global Opportunities Fund comprises the Diversified Trading Program and the International Fund. Comments in this section will cover the International Fund only.

Three bets, only one of which has been closed, accounted for the lion's share of our continuing losses. The closed position was the yield curve trade, short the two-year versus the ten-year Treasury. We had hoped the spread would widen in view of the Fed's hesitation to raise rates despite an overheating economy. Subsequent to Mr. Greenspan's speech of June 17, the spread narrowed and took us out of the position, even before the Fed was able to implement the first increase in rates. The Fed's unusually quick about-face at its June 30 meeting, however, where its bias changed to neutral from tightening, is likely to lead to a widening of the spread after all. Re-entering the trade, however, would pit us against the Fed's extraordinary ability to implement policy verbally, a course of action fraught with danger, as we have seen. Better to be short bonds outright and bet on rising rates, however they may occur, than to second-guess the Fed's true grit.

Still open but slightly underwater are the Treasury index-linked securities (TIPS) carry trade and the long Russell 2000/short S&P 500 spread. We intend to maintain these positions and believe that they will ultimately prove quite profitable.

We retained our selective short position in Japanese second-tier regional banks in the face of a spectacular 12.3% rally in the benchmark Nikkei index, with no material adverse effect. This under-performance has convinced us that all these banks are practically insolvent and that they will be closed in the very near future.

Minor gains in the New Zealand stock market were offset by equally marginal losses in Germany and Sweden. We intend to maintain, and perhaps add to, this partial macro spread, given obvious valuation differentials.

We have been looking for a position to take advantage of the coming, inevitable downturn in global equity markets without taking extraordinary hits to our equity. This is no mean feat: option premiums are extremely expensive and require exquisite timing. Taking outright short positions in the more overextended markets, on the other hand, is the equivalent of standing in front of a moving freight train. The direction that we are taking is to find pair trades that can minimize our downside yet give us a good shot at cashing in on a global downturn. The long Russell 2000/short S&P 500 spread is one such pair trade (see our discussion of this position in the equity hedge section). Long New Zealand/short Germany and Switzerland and short Japanese second-tier regional banks is another. The trick, of course, is to be able to make a case that the long side of the spread will provide protection even if markets continue to rise. In other words, bet on some rational form of rotation whereby investors shift their attention to the more undervalued sectors of the global derby. We will persevere in this effort. At this point, we remain convinced that the bear side of stock markets offers a much better reward/risk payoff than the bull side.

EQUITY HEDGE PROGRAM

FRIEDBERG EQUITY HEDGE FUND LTD.
FRIEDBERG EQUITY HEDGE FUND

We are happy to report a significant turnaround in our operations. After recording five sequential monthly losses (though the loss in May was only marginal), the portfolio showed a solid 4.3% gain in June, moving us into positive territory for the quarter (+0.6 to +2.2%, depending on the fund).

As reported in our last communication, we had commenced to de-leverage the portfolio, taking it from approximately 2.7 times capital down to 2.15 by the end of March. This gave us some time to find the reasons for our under-performance and, ultimately, develop a more promising strategy. By early May we had hit upon what we thought was the problem: our search for long candidates, motivated solely by our desire to keep a hedged profile within our portfolio, was quite dispirited and unexciting. Since we believed that stock prices were wildly overvalued, we found ourselves having to accept purchases that evidenced very little creativity. In short, we were trading away our competitive advantage in the false hope of finding winners when there weren't any. Superior investment performance can come only from marrying skill and conviction. Lacking conviction on our long selection it became clear to us that we could not win.

How, then, were we to satisfy our portfolio balance? By slowly replacing stopped out or discarded long positions with Russell 2000 index contracts. The index of the market's lowest capitalizations had begun to stir from its dramatic five-year-long sleep, having fallen a staggering 45% in relation to the S&P 500. We can make a persuasive case for a lasting turnaround in this small-cap index: small companies' earnings do better in the latter stages of an economic expansion and valuation discounts of 35% to 40% versus large-caps are too tempting for most professional money managers to resist. Moreover, should we enter a bear cycle, the poor market liquidity enjoyed by these low-caps militates against their being sold - at least in the initial stages. Finally, the use of a derivative allows us to significantly reduce slippage costs, a major plus in an actively traded portfolio interested in obtaining some exposure to a number of relatively illiquid issues. Thanks to this tactical shift, we have become confident enough to restore our leverage ratio back to a more normal level of 2.5.

We are now free to pursue an aggressive posture on the short side, knowing that our flank is well protected. We have targeted internet retail (Amazon.com, Bid.com, Priceline.com), internet software (America Online, Yahoo) and internet brokers (Schwabb, Ameritrade), all selling at raving mad valuations. Our largest loser on the short side, Revlon, has been in merger discussions for the past few months, lifting the stock more than 100% during this time. We believe that a merger will not take place or, if it does, that it will not take place above present levels. The stock is simply too rich and the company's debt too onerous. In fact, a failure to find a buyer for part or all the company could conceivably push Revlon into receivership. As a result, we have maintained our position.

The universe of potentially lucrative shorts is, in our opinion, very large and growing. Our success lies in patiently and confidently exploiting the extraordinary excesses of this bull market, while, at the same time, finding comfortable refuge in the ignored and relatively undervalued low-cap sector.

As promised, during this past quarter we have met all redemption requests from our own resources so as not to burden the funds and their unit-holders with liquidation costs. We will uphold this policy for the coming quarter as a further sign of our growing optimism

NEW ZEALAND

FRIEDBERG NEW ZEALAND FUND LIMITED
NEW ZEALAND EQUITIES FUND
FCMI KIWI EQUITIES FUND
TORONTO NZ EQUITY TRUST

We are happy to report profitable results for the past quarter despite lackluster performance of the overall market. In fact, our 2.4% gain bested the decline of 1.56% in the New Zealand 40 and the decline of 1.3% in the New Zealand Mid-Cap index (all measured in US dollars). The slight 1.27% drop in the value of the currency adversely affected the results of our US dollar-based investors.

Valuations remain extremely attractive. The median reading of our listed universe of 131 stocks shows a Market Cap/Revenue ratio of 0.95, a Price/Earnings multiple of 11.4, a Price/Cash Flow multiple of 6.6 and a Total Debt/Market Cap ratio of 0.34. The ratio of Price to Net Tangible Assets (a more conservative measure than book value) is an extremely low 1.37. By comparison, the Price/Book ratio for the S&P 500 is 7.4. The use of net tangible assets rather than book goes some way to offset the fact that the S&P 500 is weighted far more heavily with information-based companies, whose net tangible assets are close to nil. Finally, the dividend yield for the NZSE 40 is a juicy 5.9%, which compares rather favorably with the dividend yield of 1.2% for the S&P 500 and with New Zealand T-bill rates of 4.69%.

We present below our largest ten holdings and some valuation yardsticks:

Friedberg New Zealand Fund Ltd.

10 Largest Holdings in the Fund

		Price 30-jun-99	Price /Sales	Price /Earnings	Price /Cashflow	Price /NTA	Gross Dividend Yield
CDL HOTELS	CDL.NZ	0.34	0.57	16.51	5.85	0.63	3.29%
BRIERLEY INVESTMENTS	BRY.NZ	0.53	0.55	19.00	3.85	0.71	3.77%
FERNZ	FER.NZ	5.46	0.58	13.16	10.73	2.77	5.33%
FISHER & PAYKEL	FAP.NZ	6.00	0.91	17.20	8.13	1.91	5.22%
HALL GLASSON	HLG.NZ	2.33	0.89	13.65	10.62	4.02	10.25%
KIWI INCOME PROPERTY	KIP.NZ	1.06	N.A.*	11.53	13.73	0.91	11.03%
SANFORD	SAN.NZ	4.40	1.28	9.16	12.56	1.69	5.66%
ST LUKES	STL.NZ	1.80	N.A.*	13.40	19.40	1.29	7.94%
THE WAREHOUSE GROUP	WHS.NZ	7.35	1.40	19.61	19.24	6.57	3.63%
TRANS TASMAN PROP.	TTP.NZ	0.33	N.A.*	5.31	9.23	0.38	5.88%

*N.A. (Not applicable for property trust)

Weighted gross dividend yield 7.24%

The economic recovery is proceeding and inflation remains subdued. Monetary policy is on hold, providing a favorable backdrop to equity prices. The only fly in the ointment is the growing probability that Labour will win the October election. Taxes are likely to be raised for the upper brackets and social spending is certain to increase. Nevertheless, it appears that the market has already discounted such an event. A National (conservative party) win, on the other hand, could provide the much needed catalyst for a sustained advance.

New Zealand remains, by far, the cheapest equity market in the world.

FRIEDBERG ALLOCATION FUND LTD.

Neil Rackoff comments:

The Friedberg Allocation Fund Ltd. fell 1.29% for the quarter. For the year-to-date, it is down 4.40%.

At quarter-end, the fund was allocated as follows:

Friedberg Fixed Income Fund Ltd.	61%
Friedberg Currency Fund Ltd.	9%
Friedberg Global Opportunities Fund Ltd.	9%
Friedberg Equity Hedge Fund Ltd.	11%
Friedberg New Zealand Fund Ltd.	9%

Global credit spreads and equity valuations continue to offer neither true value nor attractive risk-reward opportunities on the long side, while probing the short side is a vocation that requires great patience and perseverance. It is interesting to note that our non-leveraged programs provided some interesting performance in comparison with their asset class peers (see Mr. Friedberg's comments on the Foreign Bond program and New Zealand).

A diversified exposure to the markets continues to smooth out some of the bumps in the road we're travelling. Fasten your seat belts.

NOTES

FRIEDBERG
MERCANTILE
GROUP

FRIEDBERG MERCANTILE GROUP
BCE Place, 181 Bay Street, #250
Toronto, Ontario M5J 2T3
Ph: (416) 364-1171
Fax: (416) 364-0572
htpp://www.friedberg.com