

FRIEDBERG'S

COMMODITY & CURRENCY COMMENTS

Friedberg Commodity Management Inc.



Volume 20, No. 2 March 28, 1999

Looking in all the wrong places, or how inflation will take (nearly) everyone by surprise

"The wrong war," blazed the heading of a recent article penned by Robert Reich, former US secretary of labor, adding that "like generals preparing to fight the old war, the world's central bankers are still obsessed with inflation. They should be looking forward to the real enemy: deflation."

He was not alone. Not a day goes by without some prominent institution, economist, publication, or government official offering its views on the existence and/or the dangers of "spiralling" global deflation. These opinions – couched in learned or not so learned terms or dropped in matter-of-fact fashion by investment professionals – have become so well accepted that they have taken the hue of dogma. Anyone disagreeing with this thesis must be considered mentally unfit.

The deflation dogma is a highly convenient credo. After Federal Reserve Chairman Alan Greenspan remarks on March 9 that "despite the tautness in labor markets, there have been no obvious signs of emerging inflation pressures," financial observers pointed out that his comments reinforced views that the Fed would not need to raise interest rates. Because low interest rates allow the greatest stock market bubble in history to live on, the belief in continuing global deflation, or better yet, the dangers of accelerating global deflation (in the US, rather than deflation, it is merely disinflation), are *de rigueur* on and off Wall Street. Self-serving. Naive. Fallacious. And downright dangerous.

The overwhelming majority of the disinflation proponents have used the cost-push theories of price fluctuations to explain their thesis. As we saw earlier, Greenspan's himself noted that "despite the tautness of the labor market" – a situation that should cause unit labor costs to rise – "there have been no obvious signs of emerging inflationary pressures." That is to say, inflationary pressures are caused by wages rising faster than productivity; moreover, rising unit labor costs are the tell-tale signs that inflationary pressures are rising.

On the same day that Greenspan made these remarks, it was announced that the increase in productivity for the fourth quarter of 1998 was revised to show an annualized rate of 4.6% compared with the initial 3.7% estimate. The associated

decline in unit labor costs was revised to -1.1% from -0.2%. These exceptionally constructive numbers were being used to vindicate the proponents of the new economic paradigm (including, strangely enough, the majority of the current members of the Board of Governors of the Federal Reserve). With productivity growing and average hourly earnings stabilizing at the recent pace of 3.6% (the lowest rate since 1986), core inflation was a cinch to come in under the 2.4% of 1998.

In a recent article published in the Federal Reserve Bank of Richmond *Economic Quarterly* entitled "Historical Origins of the Cost-Push Fallacy," economist Thomas M. Humphrey surveys and then critiques the intellectual foundations of the cost-push theory of price movements, a view that goes back to at least the middle of the eighteenth century.

He concludes with three points: "First, current cost-push theories are essentially the same as their nineteenth- and early-twentieth-century counterparts and suffer from the same defects. Second, the critics had it right: Monetary policy, rather than cost-push, is what determines the path of the general price

In this issue

- 2 Observer**
A brief update on global economic conditions
- 3 Europe**
Euroland, high hopes, and emerging doubts
- 4 China**
The Chinese wild card
- 4 Japan**
Still refusing to deal with reality
- 5 Japan**
JGB time bomb

Contributions by Albert D. Friedberg, Steve H. Hanke, and Tadashi Nakamae.

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

level. Third, despite its flaws, cost-push theory survives today because of its simplicity, its appeal to those whose knowledge is primarily microeconomic, and its gratifying implication that the stock of monetary purchasing power can safely be allowed to expand to meet the needs of trade."

Rather than looking at wages, or even the price of oil, the Fed ought to pay attention to last year's extraordinary growth of the monetary aggregates. From the fourth quarter of 1997 to the fourth quarter of 1998, M2 increased 8.5%, placing it well above the upper bound of its 1% to 5% monitoring range. M3 expanded even faster than M2, posting an 11% rise on a fourth-quarter to fourth-quarter basis. Significantly, last year's growth was the fastest since 1981 (when inflation was much higher) and left the aggregate well above the top end of its 2% to 6% growth range. While in recent months these aggregates have slowed down somewhat, year-on-year figures remain stuck at an unacceptably high 8.2% and 10.4% pace, respectively.

Ominously, narrow money, M1, increased 1.75% over the same period, its first annual increase since 1994. This is quite significant in view of our findings (see "Money, money, money everywhere: can inflation be far behind?" in our Feb. 22, 1998, issue) that M1 velocity had resumed its predictable reacceleration and was trending upwards at more than 7% per annum.

Where our inflation forecast went wrong last year (projecting an 8% growth in nominal income and broken down into 4% real growth and 4% inflation) was in failing to incorporate into the equation a widening current account deficit that had the effect of "absorbing" over two percentage points of nominal income. Interestingly, our forecast/assumption for real growth, at 4%, came very close to the mark (actual: 4.2%) and was presupposed on the basis of the rapid acceleration of M1 velocity that we had observed.

A 9% growth of M1-plus-velocity in the context of a 3% current account deficit and a 3% rate of growth for real GDP (as we approach capacity constraints in the labor market) spell a prospective inflation rate of 3%. This forecast could turn out to be conservative should M1 be allowed to grow by more than 2% per annum.

Tentative signs of inflation have begun to appear. While wages remain well behaved, commodity prices seemed to

have turned the corner. Most industrial commodities are well off their lows, with oil and some base metals in the forefront, and our diffusion index, having refused to confirm CRB index lows, has now turned upwards. The year-on-year rate of decline of the Journal of Commerce Industrial Index has been slowing from almost 15% last November to 7% now. Climbing above year-ago levels will signal the onset of re-accelerating inflation.

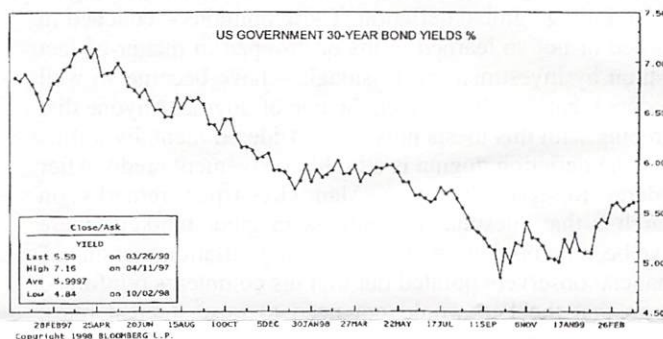
Even the bond market has begun to sense a change in the winds: "Bullish" wage costs and productivity news have been unable to arrest the gentle rise in long-term yields, now more than 70 basis points above their 1998 lows.

As inflation accelerates in response to rapid monetary expansion, long-term yields will rise and financial asset prices will fall. The Fed will once again be put on the spot: Lower rates to try to stave off financial collapse – and risk stoking the flames of inflation – or stand aside as an economic depression unfolds (brought about by the decline in stock prices).

Heretofore, prices were well behaved, and the Fed had the luxury of intervening on the side of the angels. Interest rates were cut, and cut again, and money supply expanded. Stock prices exploded as euphoria gripped the land. Cost push theorists propounded their views – and asked for more rate cuts. The Fed obliged. Finally, accelerating money growth took hold. It is now about to claim its price.

The Fed is looking in the wrong places. It does not realize, as yet, that it has lost all room to maneuver.

Chart 1 – US Government 30-Year Bond Yields



OBSERVER

A brief update on global economic conditions

Appearances notwithstanding, global economic conditions continue to deteriorate. As we pointed out almost one year ago ("The Coming Global Contraction," May 24, 1998), "downward revisions are the hallmark of incorrect data, or, more often, incorrect analysis and diagnosis. That events turn out worse than anticipated all the time tells us that events are not being diagnosed correctly. Specifically, in the predicament of the 1998 global economy, it means that officialdom and the press have been too optimistic about the corrosive impact on real economic activity of easy money and excessive credit creation."

With the possible exception of South Korea, all economic

prognostications to date have turned out worse than expected. Chart 2, prepared by no less an authority than the IMF, tells it all. Since October 1997, growth forecasts for the world economy have been revised downwards each time the *World Economic Outlook* has been published.

Despite their consistently poor forecasting record, staff economists remain optimistic, pointing out that "the modest scale of the further downward revision to the world growth projections for 1999 may reasonably be viewed as indicating that the global economic situation and near-term prospects have begun to stabilize." These words were written while Brazil, under the (mis-) guidance of the IMF was still trying

to forestall a full-scale financial crisis. Subsequent events vindicated our observation that officialdom has little or no understanding of what causes financial crisis and economic contractions. In fact, both the IMF and the OECD (specifically with regards to Euroland) have been quite forthright in recent weeks in calling for still lower interest rates as world economic growth comes to a near standstill.

Easy money has gotten the world into its present predicament. A continued dosage of easy money – though relieving and even pleasurable at first – can only make matters worse in the long run. (Sea water quenches but kills the thirsty.) A resurgence of inflation will enormously complicate matters, but it will surely end officialdom's fascination with the putatively regenerative powers of money creation.

It is not all that difficult to predict that the next IMF's

World Economic Outlook will continue to revise downwards its 1999 and 2000 projections. Rest assured: The coming world economic contraction is still coming.

Chart 2
Revisions to World Growth Projections

<i>(Percent change in world real GDP)</i>				
<i>World Economic Outlook Issued</i>	1997	1998	1999	2000
October 1997	4.2	4.3	4.4	4.6
December 1997	4.1	3.5	4.1	4.4
May 1998	4.1	3.1	3.7	3.8
October 1998	4.1	2.0	2.5	3.7
December 1998	4.2	2.2	2.2	3.5

EUROPE

Euroland, high hopes, and emerging doubts

By Steve H. Hanke

With the launch of the European Monetary Union (EMU) on January 1, the currencies in the 11 member states, the EU-11, were fused with irrevocably fixed exchange rates, and the euro became Euroland's unit of account. A new currency, the euro, will be issued in January 2002. The new notes and coins will circulate alongside existing currencies until July 2002. After that, German marks, French francs, and other Euroland currencies will be relegated to the dustbin of history.

This grand scheme has replaced 11 central banks with one, the European Central Bank (ECB). The ECB is the EMU's sole master of monetary policy, with the euro floating against the dollar, yen, and other major currencies. The euro has not floated on a sea of tranquility, however. It has lost almost 10% of its value relative to the greenback. In consequence, the high hopes for the euro have begun to be eroded by emerging doubts and confusion.

According to conventional wisdom, the euro will challenge the dollar as an international money. This opinion rests on the fact that Euroland will constitute an extended optimum currency area. The countries belonging to the European Union (EU) constitute a larger economy than the United States, and EU exports to the rest of the world exceed US exports. Therefore, it is asserted that the euro's influence will extend well beyond the political borders of the EU and that the euro will be a match for the mighty dollar because of the EU's huge economic size and international trade connections.

Even though Euroland represents an economic unit that can match the US, it does not follow that the euro will be able to go toe-to-toe with the greenback as an international money. The world economy needs a unit of account, means of payment, and store of value for both governments and private enterprises. At present, the dollar serves this purpose and is a true international money. As such, it is a vehicle currency that possesses natural monopoly characteristics, which limit the scope for another currency to serve as a true international money.

To appreciate the dollar's dominant international role and why it will be so hard to dislodge, consider that the dollar

enters one side of 90% of all interbank foreign exchange transactions in the world. This allows banks to cover both their forward exchange and option exposures efficiently, with great savings in transaction costs. The pattern for trade in primary commodities is much the same, with about 90% of these commodities being priced in dollars.

With private interbank foreign exchange and commodity markets organized to use the dollar as the vehicle and invoice currency, exchange market intervention by governments naturally follows the same pattern, because intervention can be more conveniently handled by just using dollars. Not surprisingly, then, the dollar dominates as the intervention and reserve currency used by central banks. Apart from gold, the dollar accounts for 70% of all official reserves of central banks outside the EU.

As long as there is reasonable confidence in US monetary policy, the dollar will remain king. And the new euro will become queen, the world's most important regional currency.

Will the queen be strong? According to conventional wisdom, the EMU will create a continental capital market, which will enhance rates of return on capital in Euroland. In consequence, capital will be drawn into Euroland from the rest of the world, and the euro will appreciate.

Not surprisingly, this story has been peddled by investment banks with an interest in promoting Euroland capital markets and the notion that the spirit of Michael Milken is about to burst forth in Europe. It is a neat tale, but hardly a plausible one. It implies that the EU would have to clone the US setup, one characterized by a strong federal system of government and more importantly Anglo-Saxon capitalism.

The EMU will not serve as a liberalizing force that will produce an EU economic renaissance in which entrepreneurs are favored over rent-seekers. The political establishment in Euroland and the citizens it represents have a distaste for Anglo-Saxon capitalism. That is why the blueprints for EMU hark back, almost word-for-word, to the plans of the European fascists of the 1930s and 1940s. The EMU is seen by Europeans as a way

to strengthen the corporatist-socialist policies in the EU and to allow them to be projected internationally.

Much as a hygienist strives to exterminate a pestilential bacillus, the continental euro-enthusiasts want nothing less than to use EMU to exterminate Anglo-Saxon capitalism. The real *raison d'être* for the EMU is to change the world social and economic model. Indeed, the Europeans want to make the US a clone of Europe, not the other way around.

If all goes according to plan, therefore, the corporatist-socialist European model, not the rate of return on capital, will be enhanced by the EMU. In consequence, it is hard to see how the euro will avoid long-term pressures for a real depreci-

ation, particularly if the US eschews the Third Way.

So much for the long-term pressures for a real decline in the euro's value. What about the here and now? The euro's early, unanticipated weakness might be getting a bit ahead of reality. As the dollar-euro rate approaches parity, the prudent speculator should take a good hard look at buying the euro. Not for a buy-and-hold position, of course.

Steve H. Hanke is a Professor of Applied Economics at The Johns Hopkins University, a regular columnist of Forbes magazine, and vice chairman of Friedberg Mercantile Group, Inc., of New York.

CHINA

The Chinese wild card

By Steve H. Hanke

The world economy is slowing down. This is confirmed by the steady stream of downward revisions in economic growth forecasts for the world's major economic regions. Indeed, just last week the Organization for Economic Cooperation and Development in Paris cut its 1999 economic growth forecast for Euroland to 2.0% from 2.5%. The collateral damage from the currency explosions in Asia, Russia, and Brazil continues to inflict pain. Whether it intensifies or gradually dies away will depend on China, the only remaining emerging-market wild card.

Will China devalue the renminbi? Earlier this month, the financial press went into high gear as rumors spread that the authorities were once again considering a devaluation. I continue to be unmoved by all the devaluation hype (see: "Will China Devalue," in our Jan. 31, 1999, issue).

In the face of huge illegal capital flight in 1998 – estimated to be \$67 billion by the Economist Intelligence Unit – the official reserve position of China continued to improve, increasing by \$6.4 billion to \$149.2 billion. No problem here, even with the illegal leakage. Indeed, if there had not been massive illegal capital flight, official reserves would have soared by \$73.4 billion, putting pressure on the authorities to revalue.

The external accounts are also in good shape. The trade balance for the past 12 months through February was on the plus side by a huge \$40 billion. And the current account for 1998 was in the black by \$31.1 billion, or about 3% of GDP.

Foreign direct investment did take a 10% hit in 1998, falling to about \$40 billion. And it will probably fall further in 1999 because of increasing questions about the worth of gov-

ernment guarantees on returns to foreign joint-venture partners. But this slowdown will not be life-threatening and should not be the basis for a devaluation.

External debt remains small by international standards at 15% of GDP. And official reserves exceed short-term debt by a ratio of 5 to 1. Again, there is nothing in these usual devaluation suspects to raise eyebrows.

China's 1998 growth rate was 7.8%, the lowest since the early 1990s. And 1999 will not match the 1998 figure. Here we have a potential argument for devaluation. Why not devalue and use the external account to boost growth? Such a competitive devaluation would buy the Chinese a pack of trouble just as it was attempting to join the World Trade Organization and to be viewed as an anchor of regional stability.

But what about the rotten fundamentals in China's banking system? The Chinese banks are poorly regulated and have piled up an enormous amount of bad loans to overleveraged state-owned enterprises. In a market-oriented financial system, pressures usually force a rapid adjustment when banks are perceived to be insolvent. These adjustments can set off a currency crisis. However, these market mechanisms don't fully operate in China. Banks continue to operate regardless of balance sheet weaknesses, because of government support. Therefore, it is hard to see how a banking crisis spawned by China's rotten banks could spill over into a currency crisis or give justification for a devaluation, at least in the short or medium term.

Downgrade the Chinese wild card. A devaluation is not imminent.

JAPAN

Still refusing to deal with reality

Daily occurrences of verbal interventions with the purpose of managing expectations and levels in the foreign exchange and money markets underline what is still wrong with Japan and its woeful inability to bite the bullet.

Nowhere is this more apparent than in the area of indebtedness: Lending by Japanese banks stands today at the same level as it stood in 1989, the last year of the Great Bubble – an

incredible 100% of nominal GDP. Yet a great percentage of these loans are under water and should have been liquidated long ago. And now, courtesy of Japan Inc., state-owned Japan Development Bank (JDB) has emerged as a lender of last resort for firms that should be allowed to fail. Its loan disbursements have jumped almost 50% year on year, to ¥1.6 trillion, not a trifling sum when compared with the dramatic bank

rescue involving ¥7.4 trillion. Finally, a Reuters story reports that a new government loan guarantee scheme has allocated over ¥13 trillion(!) to 676,000 firms by the end of February, significantly reducing the number of corporate bankruptcies in recent months (though 86 firms had gone bust even after obtaining loan guarantees). Government officials have indicated that the loan guarantee scheme could be expanded to more than ¥30 trillion. All these reports under-

score the Japanese government's absolute inability to deal with the aftermath of one of the greatest credit booms in the history of modern capitalism

Genuine economic recovery will elude the authorities for as long as they avoid taking unpleasant measures. The following article examines a related problem. The writer is more hopeful than we are about Japan's ability to regain fiscal discipline. The choices are tough and the omens, thus far, are very poor.

JAPAN

JGB time bomb

By Tadashi Nakamae

Reprinted with permission of The International Economy © 1999. All rights reserved.

The Japanese public debt market is a time-bomb, but it is a time-bomb whose ticking will have a very positive influence on policy, coercing Japan in the direction of smaller government and renewed fiscal discipline.

The time-bomb has four basic ingredients. The first ingredient is Japan's ongoing structural adjustment, in which resources are being released from the flagging old economy in order to be absorbed by the service-based economy of the future. The second ingredient is the government's inappropriate attempt to respond to the structural adjustment by boosting demand in the old economy through fiscal stimulus packages. The third ingredient is the imminent drainage of money from the postal savings system. The fourth ingredient is the aging of Japan's population. The element which threatens to set off the time bomb – the detonator – is Japan's financial Big Bang.

On the one hand, Big Bang has accelerated the structural adjustment. The resulting economic contraction, together with the cost of successive stimulus packages, has set the budget deficit soaring. On the other hand, Big Bang has increased the potential for the flight of Japanese capital: in particular, the possibility that Japanese savers will desert the postal savings system *en masse* in the years 2000 and 2001 has presented the government with an urgent funding problem.

The structural adjustment, at least in the non-financial private sector, is now progressing much faster than anyone expected. The correction of excess capital investment and excess employment is finally proceeding in earnest, largely as a result of Big Bang: the globalization of financial markets has forced Japanese corporations, particularly those in old, inefficient, mature manufacturing-oriented industries ("the old economy") to aim for a return on their shareholders' equity commensurate with the international standard.

The rapid shift to ROE management is why private sector capital investment is now declining at an annual rate of 20 percent. This alone will reduce nominal GDP this year by an expected 2.8 percent, or 14 trillion yen – much more than enough to offset any stimulative impact from the latest fiscal package which, despite its nominal value of 24 trillion yen, has only around 7 trillion yen of real water. The correction in capital investment, if it continues at its present pace, may be complete even before the end of 1999. This is good news for the long term, but in the short term it means that fiscal 1999 will be the third successive year of negative economic growth.

As the economy continues to contract, receipts from both corporate and income tax are falling steadily. Meanwhile government expenditure, due to successive fiscal stimulus packages, has increased sharply. As a result, Japan's budget surplus of around 3 percent of GDP in the early 1990s, has turned into a deficit which is expected to be around 10 percent of GDP in fiscal 1998 and over 12 percent in fiscal 1999. It is a sobering fact that the U.S. budget deficit in the late 1980s and early 1990s, when concerns about the U.S. twin deficits reached fever pitch, never rose above 4 percent of GDP.

The reason the Japanese economy has not responded well to massive public works spending is that, in inefficient old-economy industries such as construction, demand growth simply cannot be sustained. Sustainable growth will be possible only when resources start to shift to the underdeveloped new service economy, growth of which awaits supply-side reforms to encourage small entrepreneurs. The attempt to boost demand in the old economy through fiscal stimulus packages has been counterproductive to the structural reform process, and has been a lamentable waste of Japan's national resources. The Japanese people have become increasingly aware of this waste, and thanks to new financial freedoms afforded by Big Bang, they now have the opportunity to make their displeasure felt through the public debt market.

A significant portion of the budget deficit is currently being financed from public funds, primarily through the mediation of the Trust Fund Bureau of the Ministry of Finance, and secondly through the Bank of Japan. The Trust Fund Bureau has drawn heavily on money invested in the postal savings system, not only to help central and local governments finance their deficits, but also, through the Japan Development Bank, to support financially strapped corporations. The problem now bearing down on the Trust Fund Bureau is that in 1990 and 1991 combined, when the interest rate for 10-year fixed-term time deposits was around 6 percent, a huge total of 107 trillion yen flooded into these postal savings products. In 2000 and 2001 when these deposits mature, with a value of 191 trillion yen, half of that money is expected to be diverted from postal savings, firstly because the interest rate for re-investment will be relatively meager one or two percent, and secondly because the deposit limit of 10 million yen per person will preclude many investors from re-investing all of their available funds. Thus, before the end of 2001, the postal sav-

ings systems stands to lose nearly 100 trillion out of total deposits of 250 trillion yen.

The most calamitous alternative would be for the government to escalate its existing effort to monetize the deficit through the Bank of Japan. If the government continues to finance wasteful spending programs in this way, at the expense of the quality of Bank of Japan assets, Japanese savers will be all the more likely to register their displeasure by re-investing their money in overseas securities such as U.S. Treasuries and European government bonds. But a still more fundamental objection to monetizing an expanding deficit is that it would set Japan up for a balance of payments crisis with disastrous implications for the real economy. In fiscal 1997 Japan's budget deficit was 6.8 percent of GDP and the current account surplus was 2.4 percent. Therefore, in order to finance the expected rise in the budget deficit to 12 percent of GDP without sending the current account crashing into deficit, household savings would have to increase from their fiscal 1997 level by 2.8 percent of GDP (other things, such as the investment to savings balance in the corporate sector and disposable income in the household sector, being equal). Such an increase in savings would require a catastrophic cut in consumption of almost 5 percent. I hope this rough analysis serves to highlight that continued fiscal laxity financed by monetizing of the budget deficit would be truly disastrous: it would push Japan onto the slipper slope down which economies of the rest of Asia and Latin America have already slid.

Raising taxes in an attempt to reduce the deficit from the revenue side would also be disastrous: the structural adjustment, because it necessitates corporate cost-cutting, is inherently deflationary, and the strong yen is adding deflationary pressure. Depressing consumption by raising taxes would be another sure way to intensify the deflationary spiral.

Increasing tax revenues through higher nominal growth, even if it could be achieved, would not work either, because in the international economy since the beginning of the 1980s nominal growth rates and nominal long-term interest rates have been converging. The ratio of Japan's national debt to GDP has already exceeded 100 percent, compared with around 60 percent in the United State and the major European economies. This being so, any course involving a rise in the long-term interest rate will not provide a solution to the government's funding problem: it will only make the national debt more costly to service.

So there is no alternative: the time-bomb ticking in bond market dictates that the government must eliminate the budget

deficit by cutting the equivalent of 12 percent of GDP from government expenditure. If the government fails to slash its expenditure now, Japan's national debt will go on rising as the population goes on aging, creating a financial burden which will bring the economy to its knees, probably even before the onset of the silver society in around 2020.

Lest the above sounds too pessimistic, let me finish by expressing my strong and positive belief that market forces, provided they are allowed to work, will get Japan back on track for sustainable growth in the next century. The new financial rigor that Big Bang has brought to the corporate sector has already realized a change for the better in Japanese corporate behavior, releasing resources from the old economy. Now it is time for market forces to impose financial restraint on the government so that resources currently being wasted by the public sector can be released into the emerging new economy. Growth of the new economy can be promoted only by supply-side policies centered on tax reform, continued deregulation, and smaller government. The deterrence of the time-bomb in the public debt market will therefore help to push the Japanese government in the right direction.

In this connection, it is worth remembering what a strongly beneficial influence the bond markets have had on the U.S. and U.K. economies, through the encouragement of fiscal discipline, in the 1980s and 1990s. The 364 British economists who wrote an open letter to protest the tightening of U.K. fiscal policy in the 1981 budget proved to be glaringly mistaken: the gilt market entered a bull run, and the costs to the U.K. economy of fiscal tightening were easily outweighed by the benefits of a lower long term interest rate. Japan will reap similar benefits from a U-turn in fiscal policy. Government downsizing will not only accelerate the all-important process of supply-side structural reform, but will also be rewarded by the bond market in the form of stabilization of the long term interest rate.

In conclusion, I am confident that the Japanese government will recognize the need for renewed fiscal discipline—notwithstanding pressure from too many self-appointed consultants around the world who have successfully argued for fiscal excess and who are now pressing the government to monetize the deficit. It is a time for cool heads. Providing that reason and restraint prevail, the time-bomb in Japan's public debt market can be defused.

Tadashi Nakamae is President of Nakamae International Economic Research, Tokyo, Japan.

Friedberg's Commodity & Currency Comments (ISSN 0229-4559) is published by Friedberg Commodity Management Inc., P.O. Box 866, Suite 250, BCE Place, 181 Bay Street, Toronto, Ontario, M5J 2T3. Contents copyright © 1999 by Friedberg Commodity Management Inc. All rights reserved. Reproduction in whole or in part without permission is prohibited. Brief extracts may be made with due acknowledgement.

Subscription Enquiries for Friedberg's Commodity & Currency Comments P.O. Box 866, Suite 250 BCE Place, 181 Bay Street Toronto, Ontario, Canada M5J 2T3 (416) 364-1171

Managed Accounts
All enquiries concerning managed accounts should be directed to:
In Canada
Friedberg Mercantile Group
P.O. Box 866, Suite 250
BCE Place, 181 Bay Street
Toronto, Ontario M5J 2T3
(416) 364-2700
In U.S.
Friedberg Mercantile Group Inc.
67 Wall St., Suite 1901
New York, N.Y. 10005
(212) 943-5300

All statements made herein, while not guaranteed, are based on information considered reliable and are believed by us to be accurate. Futures and options trading is speculative and involves risk of loss. Past trading results are not indicative of future profits.

The U.S. broker-dealer, Friedberg Mercantile Group, Inc. NY, takes full responsibility for the contents of this market letter. U.S. residents wishing to effect any transactions in any security discussed in this report should contact Friedberg Mercantile Group, Inc. NY, toll-free at 1-800-474-2663.