



Vj g
O wj ngpnc o r
O go qt c p f w o

O wj ngpnc o r 'U 'Eqo r c p f . 'Ipe0
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K a n g ' 5 3 . ' V j k f " S w e t v g t ' 3 ; ; 6

S w e t v g t n f ' N g w g t

V j g ' u g e q p f ' s w e t v g t ' q h ' 3 ; ; 6 ' y k p g u u g f ' u j c t r ' r t l e g ' o q x g u
k p ' c ' p w o d g t ' q h ' o c t n g v u 0 ' X c t k q w u ' u q e m u . ' d q p f u .
e q o o q f k k g u ' c p f ' e w t g p e k u j ' c f ' k p v g t g u k p i ' u y k p i u 0
U q o g ' o q x g f ' k p ' e q p e g t v ' y k j ' q v j g t u ' k p ' y c { u ' k p x g u q t u j ' c x g
e q o g ' v q ' g z r g e v . ' y j k g ' q v j g t u ' c e v g f ' * q t ' t g c e v g f + k p ' y c { u ' v j c v
y g t g ' u w r t k u k p i 0

Y g ' j c x g ' e q p u k u g p v n f ' u c k f ' v j c v ' c ' 3 2 ' ' r t l e g ' e q t t g e v k p p ' k p ' v j g
u q e m i o c t n g v ' * c e w e m f ' k p ' c p { ' o c t n g v + e c p ' q e e w t ' c v ' c p { ' v k o g 0
N c u v h c m y g ' u c k f ' u w e j ' c ' e q t t g e v k p p . ' k h ' u c t v g f ' c v ' v j c v ' k o g .
y q w f ' o q u v h k n g n f ' d g ' t k i i g t g f ' d { ' c ' e q t t g e v k p p ' k p ' v j g ' d q p f
o c t n g v 0 ' Y g ' j c x g ' j c f ' u w e j ' c ' e q t t g e v k p p 0 ' U q e m i ' j c x g
f g e n k p g f ' t q w i j n f ' 3 2 ' 0 ' D q p f u j ' c x g ' f g e n k p g f ' 4 2 ' ' c p f
w k r k k g u j ' c x g ' f g e n k p g f ' 5 2 ' 0 ' V j g ' c f f k k q p c n i ' 4 2 ' ' f g e n k p g ' k p
w k r k k f ' u q e m i ' q e e w t t g f ' d g e c w u g ' q w t ' H g f g t c n i q x g t p o g p v
e j c p i g f ' v j g ' t w g u ' h t ' g r e v t k e ' w k r k k g u . ' h t e k p i ' v j g o ' v q
e q o r g v g ' y k j ' q p g ' c p q v j g t ' k p ' v j g ' r t q f w e v k p p ' c p f ' u c n g ' q h
r q y g t 0

V j g ' f g e n k p g ' k p ' v j g ' d q p f ' o c t n g v ' y c u ' g z c e g t d e v g f ' d { ' v j g ' t g e g p v
f g e n k p g ' k p ' v j g ' f q m c t ' c p f ' v j g ' h x g t c i g f ' r q u k k q p u ' y j k e j

Q p ' L w n f ' . : 3 ; ; 6 ' v j g ' P g v ' C u u g v ' X c n w g ' q h ' V j g ' O w j n g p n c o r ' H w p f
y c u ' 3 9 0 8 : ' f q y p ' 5 0 3 ' ' { g c t ' v q ' f c v g 0 ' C l i c k h e r e ' v q ' u g g ' v j g '
e w t t g p v ' P g v ' C u u g v ' X c n w g ' h q t ' v j g ' O w j n g p n c o r ' H w p f 0

u q o g ' k p x g u q t u j ' c f ' v c n g p ' k p ' v j g ' d q p f ' o c t n g v ' k u g r i 0 ' O c t i k p
e c m i ' q p ' v j g u g ' r q u k k q p u ' t g u w n g f ' k p ' h q t e g f ' u g m k p i ' q h ' d q p f u
y j k e j ' c r r g e t u ' v q ' j c x g ' e n k o c z g f ' k p ' O c t e j ' q h ' : ; 6 0 ' V j g ' h e n k p i
f q m c t ' c p f ' e w t g p e { ' h g t u ' t g u w n g f ' k p ' c p ' c f f k k q p c n i ' q w p f ' q h
u g m k p i ' k p ' r e v g ' L w p g 0 ' C v ' v j k u ' r q k p v . ' v j g ' u g m k p i ' r t g u u w t g u ' u g g o
v q ' j c x g ' c d c e v g f 0 ' D w ' c p q v j g t ' u j q g ' e c p ' c n y c { u ' f t q r 0 ' U q ' y g
e c p o ' u c { ' y k j ' e g t v c k p v f ' v j c v ' v j g ' f g e n k p g ' k u ' q x g t 0

O g e p y j k g . ' o q u v ' e q o r c p l g u ' c t g ' k p e t g e u k p i ' k p ' g e q p q o k e ' x c n w g
c v ' c ' t e v g ' q h ' : / 3 2 ' ' r g t ' { g c t 0 ' Y g ' f q ' p q v ' u g g ' k p h e v k p p ' i g w k p i
o w e j ' y q t u g ' q t ' v j g ' W U ' g e q p q o { ' f g e n k p i ' c p { v k o g ' u q p p 0 ' U q
k p x g u o g p v ' x c n w g ' j c x g ' k p e t g e u g f 0 ' U q o g ' c p c n f u w ' c t g ' h q n k p i
h q t ' c ' r e t i g t ' f g e n k p g ' c p f ' d g w g t ' x c n w g u . ' y j k e j ' o c { ' q t ' o c { ' p q v
j c r r g p 0 ' H c p m f . ' v j g ' d g u v f g u e t k r v k p p ' q h ' o c t n g v ' y j k e j ' K
j c x g ' u g g p ' r e v g n f ' y c u ' c ' e q n w o p ' d { ' O k n g ' T q { n q ' v k n g f .
o G e a p q o k e u ' 3 2 3 0 6 ' ' O t 0 T q { n q ' e q p e n f g f ' v j c v ' ' c m q u v
c p { v j k p i ' e c p ' j c r r g p = o q u v ' v j k p i u ' r t q d c d n f ' y q p o v ' * j c r r g p =
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c p q v j g t 0 ' D q w q o ' h k p g . ' y g ' l w f i g ' e w t t g p v ' x c n w g u ' v q ' d g ' i q q f
g p q w i j ' v q ' d g ' d w { k p i ' u q e m i ' c p f ' c f f k p i ' v q ' q w t ' j q r f k p i u 0

* Invitation *



Ron Muhlenkamp will host an investment seminar **July 28th** at the **Greentree Holiday Inn in Pittsburgh**. The topic of the seminar will be **"Investing for the 90's."** Please call (412) 935-5520 for times and reservations.

G u c {

k p ' t g e g p v p g y u r w g t u . ' y g ' j c x g ' y t k w g p ' g z v p u k x g n f ' q p ' q w t ' e t k g t k e ' h q t ' g x c n w c k p i ' u q e m i ' c p f ' d q p f u 0 ' k p ' v j g
h q m y k p i . ' y g ' y k n i f k x g ' { q w ' c ' h e y ' e w t t g p v ' v j q w i j u ' q p ' v j g ' f q m c t = d w ' h t u v . ' y g ' p g g f ' v q ' t g x l e y ' u q o g ' v j q w i j u
v j c v ' e r r n f ' v q ' c m i o c t n g v u 0

k p ' v j g ' n p i ' t w p . ' r t l e g u ' c t g ' f g v g t o k p g f ' d { ' v j g ' g e a p q o k e ' x c n w g ' q h ' c u u g u 0 ' N q p i / v g t o ' k p x g u q t u ' h e w u ' q p ' v j k u ' x c n w g ' c p f ' c w g o r v ' v q
d w f ' c u u g u ' y j g p ' v j g f ' c t g ' r t l e g f ' y g m i d g n y ' x c n w g ' c p f ' u g m i y j g p ' v j g f ' c t g ' r t l e g f ' y g m i c d q x g ' k 0 ' Y c t t g p ' D w h g w u ' r j t c u g ' h t ' v j k u ' k u <
o N q p i / v g t o . ' v j g ' o c t n g v ' k u ' c ' y g l i j k p i ' o c e j k p g 0 ' Y c m i ' U t g g v ' t g h e t u ' d t q c f n f ' v q ' v j k u ' f k e k r k p g ' c u ' o h w p f c o g p v c i 0 ' D e p ' I t e j c o a u
d q q m o U g e w t k f ' C p c n f u k u . \$ ' h t u v ' r w d k u j g f ' k p ' 3 ; 5 6 . ' k u ' i g p g t c m f ' e a p u k f g t g f ' v j g ' d c u l e ' v e z v ' k p ' f g h k p i ' j q y ' v j g u g ' x c n w g ' e c p ' d g
e c r e w e v g f 0 C u ' k p h e v k p p ' t c p ' w r ' k p ' v j g ' g c t n f ' - 9 2 a u . ' K h q w p f ' k ' p g e g u a c t { ' v q ' c f l w u v ' k u ' e t k g t k e ' h q t ' v j g ' f g r t g e k c k p i ' x c n w g ' q h ' v j g ' f q m c t =
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U q . ' c m p i ' y k j ' g e a p q o k e ' x c n w g . ' r t l e g u ' j c x g ' c ' j w o c p ' q t ' g o q v k p c n e a p v g p v 0 ' V j k u ' e a p v g p v ' e c p ' d g ' r q u k k x g . ' c f f k p i ' v q ' v j g ' g e a p q o k e
x c n w g = q t ' k ' e c p ' d g ' p g i c v k x g . ' u w d t c e v k p i ' h t q o ' v j g ' g e a p q o k e ' x c n w g 0 ' V j q u g ' y j q u g ' x l e y ' q h ' v j g ' o c t n g v ' k u ' i j q t v v g t o ' e a p e n f g ' v j c v
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k p ' v j g ' n c u v ' y g p v { ' g c t u ' c ' h v ' q h ' r g q r n g . ' y g m i c t o g f ' y k j ' e q o r w g t u . ' j c x g ' u w f k g f ' t g e g p v r t l e g ' j k u q t k u ' c p f ' c w g o r v g f ' v q ' h q t g e c u v
h w w g ' r t l e g u ' h t q o ' v j g ' r c w g t p u ' y j k e j ' v j g k t ' e q o r w g t u ' h k p f 0 ' V j g u g ' o g v j q f u ' c t g ' c w i j v v q ' c ' r e t i g ' p w o d g t ' q h ' r g q r n g ' k p ' d w u k p g u u
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f c { ' g s w k x c n g p ' v q h ' u q r l i q u u ' q t f g t u 0 C p f ' k y ' q t n g f ' / ' w p v i ' v q q ' o c p { ' r g q r n g ' w u g f ' v j g o ' / / ' i k k p i ' w u ' v j g ' y q f c { . ' 4 2 ' ' f g e n k p g ' q h
Q e v a d g t ' 3 ; : 9 0

The Muhlenkamp Memorandum

(Essay continued)

We believe that the dollar will appreciate over time. But, early this year, too many people made that bet on too high margins. A small dollar decline resulted in the forced selling of March 1994. Although fundamental and technical analysis are thought by many to be competing philosophies, we believe they are largely complementary and that a knowledge of both is necessary to understand markets.

We have said for some time that the pressures created by the US Federal Deficit would find an outlet someplace, but not necessarily in the form of higher inflation. It now appears that these pressures are finding an outlet in the value of our currency. Some commentators expect this alone to result in inflation, others expect higher interest rates even without inflation.

This brings us to currencies, specifically the dollar. In a free economy, market prices continually reflect the values which consumers place on various goods and services as well as the costs of producing them. Both parts of this equation must be taken into account, otherwise it is difficult to understand why air is free and cosmetics are expensive.

When trade occurs freely between countries and economies, the relative values of their currencies gravitate toward purchasing power parity. That is, if the Canadian dollar is quoted at 70 cents US, you would expect that an item which cost \$7.00 in Detroit would cost C\$10 in Windsor, Ontario.

Based on "fundamental" economic factors, such as purchasing power parity and the current strength of the US economy, the dollar is currently undervalued and should be appreciating. And, in fact, the dollar is appreciating relative to most currencies, with the glaring exception of the Dmark and the yen. What makes these two currencies special is that, since 1945, both countries have become major factors in world trade and both currencies have earned the trust and respect of international traders.

A major function of any currency is to facilitate trade and commerce. It is particularly convenient if both parties to any trade use the same currency. If any haggling is to occur, this allows them to haggle only over the price of the goods, not the price of the currency. If you live near the border of a country, you know that most merchants will quote their price in both currencies or at least display the relative currency value.

When a lot of trade occurs between two nations, it becomes convenient to conduct the trade in just one currency. The currency of choice is usually the one of the larger economy, provided that the currency's value is trusted by both parties. Prior to W.W.II, the currency of choice for international trade was the British Pound. Since W.W.II, the currency of choice has been the US dollar.

The convenience of quoting prices in a single currency is so great that some international commodities, such as oil, are priced in dollars throughout the world. When a French company buys oil from Saudi Arabia, the contract is not in francs or riyadhs, but in dollars. But international confidence in the US dollar was badly shaken when we inflated the dollar from 1965 to 1982. During that time, the US created new dollars at a rate much faster than we produced goods so the purchasing power of the dollar fell by 70%. (This was a major reason OPEC raised the dollar price of oil.) Other countries, specifically Germany and Japan, did not inflate their money supply; and their money earned the trust of their trading partners. As their economies gradually came to dominate their regions of the world (some economists argue that their economic strength is largely because their currencies can be trusted), their currency came to be accepted throughout the region. Today, you can travel throughout Europe using Dmarks as currency, and you can travel throughout Asia using only yen as currency. And we are now seeing that Dmarks and yen are increasingly viewed as alternatives to the dollar throughout the world.

For years, the US has had a budget deficit of over \$200 billion which means the US treasury must borrow that money. Also, the US has had a trade deficit of over \$120 billion which means we are spending that much more outside this country than we are selling. Foreign holders of dollars earned in trade have essentially two options: either accumulate dollar assets, or exchange the dollar for some other currency. Not all this trade deficit is with Japan, of course, but a fair amount of it is, and we will use Japan as an example. In the late '80's, many of the dollars we sent to Japan came back here as purchases of Los Angeles real estate, Pebble Beach and Rockefeller Center. The dollar price of these assets have since fallen by 2/3, and the decline is greater in yen. So, the Japanese are not in a big hurry to buy more real estate. More recently, many of these dollars have bought US Treasury Bonds; thereby helping to fund our deficit. Since last fall, the price of treasury bonds have declined 20% in dollars, and even more in yen. So the Japanese have backed off on the purchase of treasuries. They and other international traders are now exchanging dollars for yen, causing the price of the dollar to fall.

Adding to the current momentum against the dollar, the US investing public has discovered international investing and sent over \$50 billion to other countries. So the "momentum" of currency flows has been out of dollars. Much of the decline in the dollar versus the yen, and the rise in US interest rates, dates from mid-February. At that time, shortly after putting forth a major effort to pass the North American Free Trade Agreement (NAFTA) the Clinton Administration resumed bashing the Japanese on trade. In many respects, President Clinton's position today is that of the person who has borrowed a lot of money from friends and neighbors, then gone around town denigrating those who lent him money (bashing Japan on trade and showing no signs of cutting back on his spending). Now he doesn't understand why they want a higher interest rate to lend him more money. Telling the US public what we want to hear may get you elected in this country; but the stature of the US and the US dollar throughout the world is heavily influenced by our actions in foreign affairs. This is the problem that President Clinton is now facing.

* A F o l l o w U p *

A quick follow up to a concern we raised in Issue 28 of the Muhlenkamp Memorandum. Writing in January, 1994, we said "Beware of life insurance....the rate is not fixed. If you bought a policy five years ago, you have seen the premium (or the number of premiums) go up. It will happen again." Enclosed is an article from the June 30 issue of the *Wall Street Journal*, page C1. Titled "Insurer Warns of Premiums that 'Vanish'", it discusses why premiums have gone up. However, the article does not make clear that it is likely to happen again.