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• One Man's Opinions - Spring 2009

ONE MAN'S OPINIONS – Spring 2009

Since my last newsletter ninety days ago, the financial sector has continued quite volatile and tumultuous, although not as bad as last fall. The stock market staged a second bear market (defined as a 20% down move) after President Obama took office, to add to last years' 38% drop. The market was not demonstrating any faith at all in the new administration, nor, to be fair, in the Democrat leadership of the Congress. This changed, however, on March 23, 2009 when the Obama administration finally announced a new plan to buy up to $500 billion of "toxic" assets from banks, insurance companies, and various other financial institutions.

The stock market promptly shot up six percent, adding to a 15% earlier bounce from its March 5 lows. This largely made up for the losses since the Obama inauguration. The first rally was apparently in reaction to several positive developments in the economy, as well as a 180 degree shift by the administration, from predictions of catastrophe to ones of recovery and prosperity as the various stimuli take effect. This sudden shift was overdue in this observer's opinion, as "talking down the economy" by Obama and his team seemed counterproductive once he took office.

I remain convinced that the U.S. government will eventually prevail. There is too much money being thrown at the economy by the Federal Reserve for it not to result in an eventual recovery. But the path has been hilly and rocky almost beyond belief. Let us review the past few months. The Bush administration asked for $700 billion to stabilize the financial sector by buying up toxic assets and injecting fresh capital into failing institutions. Last fall we were told that $700 billion was necessary to shore up failing financial institutions and to buy up toxic debt. Instead, after an infusion of government money buttressed their capital positions, banks and other financial institutions lost any interest in selling mortgages which had no market, but which were current in their interest and principal payments and certainly worth a great deal more than 28 cents on the dollar, what Merrill Lynch settled for in a distress sale of such assets prior to merging with Bank of America. But these "toxic" assets are still on bank books, limiting their available capital and, thus, their lending. Treasury Secretary Paulsen then switched to other actions to cure the moribund economy, which were also mostly unsuccessful.

Exit the Bush administration; enter the Obama administration; which has had a terrible problem staffing the U.S. Treasury with experienced, qualified people. This failure was largely self-inflicted. The standards for choosing appointees were overly cautious. At the same time they seemed to be picking people who had back tax problems! As this is written, there are still 14 vacancies in the 19 positions at the Treasury which need Senate approval, those serving directly under the new Secretary, Timothy Geithner. Surely the lack of people in these key positions contributed to the two month delay (some would say four months, since Obama's election) to come up with their targeted plan to get the economy going again. The blame belongs at the White House, not across the street in the Treasury Dept.

The United States government is now engaged in attempting to spend its way out of a recession, on top of trying to spend its way out of a financial crisis, this on top of attempting to spend its way out of a sub-prime mortgage mess. It has not worked well! It never has. Both the Hoover and Roosevelt administrations attempted it during the Great Depression and were not successful. The advent of World War II finally bailed out the economy. The Japanese tried it in the 1990s, with little to show for it. We are now approaching $2 trillion dollars of stimulus spending, either in the hopper or being planned. But at least our Congress is proving it does one thing very well - spending our tax dollars and those of our descendants without restraint. So far these massive efforts have not shown much results. The Congressional Budget office recently estimated that we will have budget deficits of NINE TRILLION dollars over the next eight years. We clearly cannot afford to run deficits this large!

What the government has done is raise fears that the massive debt of United States will grow so large that we will not be able to finance it, that few will want to buy our bonds. These fears appear way overblown as there are no signs of a lack of buyers for our debt, even with interest rates from 1/4% to 2%! China and other foreign governments continue to have voracious appetites for our bonds. Between them, China and Japan bought over $21 billion worth in January alone. It would appear that the full faith and credit of the United States of America is intact.

The stock market hates uncertainty, yet our government, under both administrations, Republican and Democrat, has contributed nothing but uncertainty in its efforts to alleviate the damage done by the meltdown of the credit markets.

The new administration, after quickly pushing Congress to commit spending another $800 billion, in its first two months did not come up with a specific plan to attack our underlying economic challenges. They finally offered a “new” plan, to buy up toxic assets! It seems we have been here before, and not long ago. Add to this the Obama administration’s focus on its promises to change health care, education, and energy programs to a more liberal bias; all the while apparently largely ignoring the economic meltdown which was threatening to sink the ship entirely. Until recent days, there has been very little from the administration to encourage citizens that our economy will work its way out of trouble any time soon. Some of this is due to an inexperienced president with inexperienced key personnel, who together face a huge crisis at the very start of their watch.

This is to be expected; most presidencies stumble a few times while finding their way. The current president is further handicapped by having virtually NO management experience. By contrast, President Bush, who was widely criticized for his poor leadership by Democrats and the media from the very start, has a Harvard MBA, and had been a successful businessman and governor of a large state. He and his team still made many mistakes. I find it an interesting coincidence that both presidents have undergraduate degrees from Yale and postgraduate degrees from Harvard, Obama with a law degree. The Ivy League is still providing leadership after two hundred years.

I believe we need to give President Obama some slack as both he and his team settle in for their four year term. They have a lot to learn, including things of which most voters have no knowledge. Rightly or wrongly this is the leader a majority of voters selected to run the country. We can cheer their actions and decisions or disagree with them vociferously, but these are the ones we, collectively, put in charge. I pray for them daily.

It is time for my annual diatribe about the financial media, especially the electronic media. Recently on the Fox News Channel, normally a reasonably good source for financial news, a young woman anchor reported (breathlessly) that the number of workers now unemployed in the U.S. was “higher than at any time since 1967!” This is a great example of factual reporting which is misleading. Why? Because there are now 50% more people in the U.S. than 42 years ago. So the percentage of unemployed is only two thirds of what it was then.

The media is constantly reporting things like this without proper perspective. The print media, especially the more liberal newspapers and newsmagazines, constantly distorts the real picture. My all time misleader, CNBC, with relatively few viewers, around 200,000 most of the time, focuses on very short term financial news and opinions. Many of these opinions are faulty, in my opinion, and others are true but misleading simply because most investors should not be focused the next few days or weeks, but on the long term, years down the road. My advice is, take financial reporting with several grains of salt. Very few journalists are financial experts! But Steve Forbes and his team of writers come to mind, Neal Cavuto on Fox News, the Wall Street Journal and Barron’s teams, are all good sources. I am sure there are others. But ordinary mainstream journalists are just that, journalists. Their focus is attracting viewers, listeners, or readers. So bad news sells, good news is boring. Keep that in mind.

It is my expectation that the economy will bottom in the next 90-180 days, that the stock markets are discounting the improving outlook, and that the lows of March 5, 2009 will prove to be the bottom. Stocks are not likely to be this cheap again in my lifetime! Feel free to call or email us for advice and/or sympathy. Handholding is our specialty!

My weekly blogs will resume April 10.

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