Inside Business
The Hampton Roads Business Journal • Insidebiz.com
Volume 14 • Number 42 October 20 - 26, 2008 • $1.00

No silver lining in sight right now

Many expect $700 billion bailout to do little to stop falling home prices

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Don't expect a silver lining from this financial mess. And don't expect the $700 billion bailout plan approved by Congress to curb foreclosures and falling home prices any time soon.

In fact, local observers are pessimistic, concluding that the fallout from the collapse of Wall Street's finest may linger for a while despite the triage the government is attempting in order to stem the bleeding.

Consumers may not see any breaks, at least until the poisonous assets are revalued, sold and the lenders start lending again.

At least that's the scenario unfolding after failed attempts to get lenders to start lending again.

Those attempts have ranged from Federal Reserve short-term loans to shore up the commercial paper market, where companies go for short-term loans of less than a year to pay employees and buy equipment, to another rate cut in the key interest rate by the Federal Reserve.

"I'm not sure if there's a silver lining in all of this," said George Walker, a partner with the accounting firm of Goodman & Co.

Walker, who advises community banks in Virginia, isn't sure how long it will take before the market reverses course and lenders start lending again. But he contends that the $700 billion bailout will have zero impact on foreclosures and hence consumers, at least for now.

"There doesn't appear to be any silver lining at this point in time," said Mike Howlett, a partner with the accounting firm of Cherry, Bekaert and Holland.

"There is still way too much uncertainty in the marketplace and with the problem now seeming to be spreading worldwide, I think the jury is still out on the effect of the bailout."

"Just after passage of the bailout package, I would have given positive responses to your questions on foreclosures and stabilization of home prices," he said last week. "Now, I don't see where the bailout bill is going to have the desired effect."

Howlett said the rescue plan is either not

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enough action on behalf of the government or needs more time to see if it will work.

But if the plan provides liquidity – or the ability to borrow and lend money – to financial institutions, they will, in turn, lend money to consumers to buy houses, which will stop the freefall in housing prices.

Timing is everything.

"With respect to timing, I don't think six months from now will look much different than today for either the struggling homeowners or the scared bondholders, except for those bondholders who get bought out at a loss," said Jim Flinchum, the managing principal of Bay Capital Advisors in Virginia Beach. "The purpose of the bailout/rescue bill was to flush out the plumbing in the credit market for mortgage-backed securities, not to help the struggling homeowners or the frightened bondholders."

Howlett does not see any evidence that the bailout package alone is going to be enough to solve the liquidity crisis.

"I think more action is going to be needed before we see positive results," he said.

Howlett contends that direct infusion of money into banks and government ownership of banks may be needed to restore some stability to the marketplace, a proposal put forth by Treasury and implemented already in the United Kingdom.

"Just buying up mortgage-backed securities doesn't necessarily put the government in a position to renegotiate mortgages, especially if there are minority bondholders," Flinchum said. "They will have to work through the servicing agents, who are already maxed out."

Flinchum fears that will turn into another gigantic bureaucratic morass.

"Theoretically, once the pipes are flushed out, more mortgage loans can be made to purchase more houses, which would increase home values," Flinchum said.

He was glad the bill passed "because it did address an important issue and bought us a little time."

"Since then, other issues have overwhelmed the significance of that bailout/rescue bill, such as overleveraged big banks, collapsing markets worldwide, virtual shutdown of the commercial paper markets," he said.

The plan calls for Treasury to buy these poisonous assets – but at what price?

Walker said he believes Treasury could get burnt if they pay the wrong price for the toxic assets.

"No one knows how much they are worth," Walker said. "There's not a market for these assets."

Walker said that there's a piece of real estate that backs the bad securities. In the beginning, he backed the bailout package, believing it would stabilize markets.

"Now people are saying it's full of loopholes," he said.

The markets reacted all right. The Dow Jones plunged below 10,000 in a week. Overseas markets suffered the same fate.

Walker said the plan will not work quickly for what it was designed – to restore investor confidence and prick banks into lending.

"All of our community banks are effectively insulated from any of these assets," Walker said. But he added, "community banks are suffering peripherally from liquidity issues."

"I think they are healthy and ready to go," he said. "They have good balance sheets."

But community banks have been buffeted by competition from the major banks for depositors, which has pressured what they pay depositors and at what rate they lend money.

If a major bank like Wachovia is offering a 4 percent return on a one-year certificate of deposit, community banks will have to compete or let those deposits go, he said. IB