

## **Bailout bonanza**

### *Flim-flam artists line up for the dole*

*December 26, 2008* – It’s the gift that keeps on giving. The US Troubled Asset Relief Program (TARP) – the monumental US\$700 billion (and growing) bailout pork barrel – is quickly becoming the miraculous answer to the fervent prayers of executives and managers at every bank that ever made a bad loan decision, every car company with parking lots full of never-to-be-sold SUVs, every ethanol producer who’s seen the price of oil collapse – in short, every con man, flim-flam artist, huckster, and fast-buck artist capable of filling out a TARP request.

And the flim-flam artists are now coming out in droves. The most sensational cases involve high profile financiers like Bernard Madoff and Marc Dreier, who are accused by prosecutors of defrauding investors of billions of dollars. But some would say these guys were just a little too early – they got caught before the US government made bad investment and management decisions legal, and in fact, began rewarding them with lucrative bailout packages.

The most recent of these came last week. Hard on the heels of multi-billion-dollar bailout loans from the Canadian and US governments the week before, General Motors Corp. got another Christmas present last week. The US Federal Reserve Board will allow GMAC Financial Services to become a bank holding company, which will let it apply for a share of TARP funds.

GMAC, which is 51% owned by Cerberus Capital Management LP, is a lending institution that provides financing for car dealers and customers, and also dabbles in home mortgages. GM holds the other 49% but wants to reduce its share to 10%. As part of any bailout, Cerberus, which also owns Chrysler Corp., would have to reduce its stake to 33% and inject more capital into the company.

To its credit, the Canadian government hasn’t been quite as aggressive in shifting bad investment decisions into taxpayers’ balance sheets, though it has pandered sufficiently to the media-driven political winds to provide some handsome bailout funding to carmakers, mortgage pools, and holders of frozen Canadian non-bank asset-back commercial paper. The Minister of Finance, Jim Flaherty, assures Canadians that this money – being in the form of loans – will all be “paid back.” That’s another convenient fiction – a sop to those few voices of prudence in the current fiscal wilderness who object to the government’s ad hoc repeal of the iron rules of risk and reward.

We can say very little with any degree of certainty about what the future has in store for markets or for the economy. We can make educated guesses, and these often turn out to be not too far from the mark.

But what we can say with a very high degree of certainty is that none of the bailout “loans” currently being extended to prop up failing enterprises around the world will *ever* be “paid back.” The only “paying” that will be done will be by taxpayers who will foot the bill for ballooning government debt and fiscal deficits. Oh yes, taxpayers will also be paying in a far more insidious way – through the erosion of purchasing power as the current bout of easy money manifests in some serious inflationary consequences not too far down the road.

Meanwhile, the US housing market continues to seek a bottom as sales of new homes in November dropped, this time to a 17-year low. The housing market is a barometer of the broader economy because it’s so tied in with the financial health of the US consumer. With job losses mounting and credit still very tight, the US housing market looks set to remain in poor shape well into 2009. By the same token, though, it is likely to spring back to life once the current round of easy credit (federal funds rate now near zero) and massive liquidity injection begins to take hold, probably sometime past the middle of next year. Around the same time, equity markets are likely to pop.

So despite the prevailing doom and gloom, and our uneasiness about the longer-term effects of this latest round of monetary mischief, we think that equity investors, after some anxiety in the first two quarters of 2009, will be in for a pleasant surprise through the second half of the year.

With the holiday season at full steam, stock markets saw thin trading last week as all but the keenest investors and money managers (or those with absolutely no work/life balance) gave in to the spirit of the season and left their trading desks to make merry. The S&P/TSX Composite Index ended a three-day trading week on Christmas Eve with a 2.8% loss. Wall Street was back in business on Boxing Day, but with only a skeleton staff, as both the Dow Jones Industrial Average and the S&P 500 Composite Index closed Friday flat week-over-week on very light trading.

We’d like to take this opportunity to wish all our readers the very best of the holiday season and a healthy and prosperous New Year! ■

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