



AlternativChronicle

Dear Mister President....

A few simple ideas to stop and reverse the credit crisis

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A Good Cause:

As some of you know, I am raising funds for research to cure **Alzheimer's Disease** by playing in the Baycrest Pro-Am Hockey Tournament on April 23-25.

Knowing my abilities, I might make a fool of myself. But, it's for a really good cause!

I want to say thanks to the many donors who offered their generous support. So far, I've raised \$4,700 and hope to exceed \$6000.

To those who would like to contribute, my web-link is in the red box (*just press CTRL and RIGHT CLICK the mouse once the cursor is above link*).

Thank-You Again,

..... **GMK**

As pundits compare our current situation with the Great Depression and media headlines trumpet each negative economic statistic, policy-makers are desperately seeking a workable solution to reverse the financial meltdown.

Unquestionably, authorities have responded quickly with a wide variety of innovative rescue programs including conservatorship for Freddie and Fannie, forced shotgun mergers for weak financial institutions, TARP, TALF, and the Capital Purchase Program.

The Federal Reserve created TAF, TSLF, PDCF, and slashed overnight rates (ZIRP). Now they're injecting liquidity to lower longer term rates by purchasing over \$1 trillion of Treasury bonds.

Policy-makers should be complimented on their rapid response. There's one catch; aren't these initiatives really expensive? My calculations suggest they add up to many TRILLIONS! And despite the recent jump in stock markets around the world, there is no visible end to the crisis in sight.

Let me suggest a slightly out-of-the box alternative for consideration. It can be implemented fast, has an immediate positive economic impact, and most importantly, it makes sense.

The idea stops home values from falling, encourages auto sales and increases personal consumption. Best of all, it costs ZILTCH. One caveat however; it requires real political leadership.

Interested? Here's the idea; since the credit crisis really started with housing, (con't on pg. 2)

Please help raise funds for important research. Visit my web-page at:

<http://my.e2rm.com/personalPage.aspx?SID=2028368>

Baycrest Pro-Am Hockey in Support of Alzheimer's Disease

Further Insights to the Credit Crisis

Special Guest Columnist.....**Ross Ferguson**

This is a follow-up to "Anatomy of this Credit Crunch" which I believe can be expanded upon, especially after noting the words "Heart of Darkness" which appear in the title. I think these words are the key, or certainly point us in the direction of what really happened in US financial markets in the last few years. As the author notes "...global regulatory reform can yield positive results, but it is not enough". In fact, my view is that lack of regulatory oversight was not the primary cause of the sub-prime meltdown. The primary cause was incompetence and fraud which effectively undermined the US and ultimately world financial markets.

We have seen evidence of this before, whether it be in misleading equity research, the backdating of stock options, insider trading, mutual fund and insurance company malfeasance, etc. Typically, it takes two or more parties to create a financial instrument which eventually blows up. One example that comes to mind is the structures created by Enron and sanctioned by Arthur Anderson, which resulted in jail time for some of the participants, the collapse of Arthur Anderson, and possibly the creation of Sarbanes-Oxley. (con't pg.2)

why not fix this problem first. How? Offer immediate conditional U.S. citizenship to foreign families willing to buy homes within 90 days of arrival. Cap the program at say 1 million homes (which translates to roughly 5 million new citizens). This would quickly absorb excess inventories and put a floor under home prices.

The program might prioritize families where the breadwinners are fluent in English and have specialized skills (such as engineers, solar energy specialists, medical technicians, educators, etc.). Admittedly, it would favour educated or entrepreneurial types, which does however, lessen the risk that criminal or terrorist elements enter the USA. The new immigrants remain "on probation" to ensure they contribute economically and abide by applicable laws. After 5 years, those honouring their obligations get full citizenship.

Now admittedly, suddenly allowing 5 million immigrants into America from many regions may prove challenging for Homeland Security. So here's a second variation.

Currently, according to reliable sources, it's estimated 10 to 11 million illegal aliens reside in the U.S. Many have worked in the country for years, often in factories, fields or



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manually intensive jobs. The highest concentrations are in California, Arizona, Texas and Florida where the largest home price declines have occurred.

Presently, illegal aliens earn income but pay no taxes. They're already in the U.S., but in political-economic-social limbo. Worse, they are easily exploited by unscrupulous types, with dire consequences. How about a partial amnesty? Provide green cards and watch consumption skyrocket (autos, homes, large appliances, etc.) as well as tax revenues. Ironically, this may prove far more cost effective than deportation efforts.

Yes, this is very controversial. But so is doling out taxpayer money to financial institutions or rescuing firms deemed "too big to fail". Moreover, neither of those addresses the real underlying problem. Mr. President, solve the housing problem and you truly solve the crisis.

Some further thoughts. While home ownership is a noble and desirable goal, the game of home speculation is not. Flipping real (or financial assets) cannot be the way America re-affirms her global

leadership. Consequently, stronger affordability testing is needed for those seeking mortgages, even if in the future, mortgages continue to be securitized.

There are many ways of avoiding a repetition of the recent housing bubble. The

first is by designating one's main dwelling as a tax free asset (no capital gains tax on disposition). The second is by discouraging the supersizing of mortgages, which then reduces the likelihood homes morph into ATMs. Lastly, full mortgage interest deductibility, which encourages people to be perpetually indebted, is worth re-considering.

In Canada, where mortgage deductibility does not exist and the principal residence is tax exempt, home ownership remains a goal for most. People select properties where they will live for long periods. House flipping was not as rampant as in the U.S. Then again, neither was banks willingness to lend to virtually anyone with a pulse.

These ideas are controversial. But then again, so are all the new programs with funny acronyms that seem to spend unlimited amounts of taxpayer dollars.

With best wishes, GMK □

Further Insights to the Credit Crisis (continued)

In the sub-prime fiasco, there was a complete chain of players, starting with mortgage borrowers who in many cases must have known they could not afford the mortgage payments. Such borrowers were encouraged by mortgage brokers who hired appraisers that occasionally provided market values in excess of the true value of the homes. Local lenders often accepted these mortgage applications with little or no verification of income or assets ('ninja' loans). Wall Street then packaged these loans and sent them to the rating agencies, who appear to have rated them without the kind of rigorous stress testing and due diligence that investors were led to expect. If modeling was used in assigning these ratings, it was clearly inadequate. Modeling is helpful, but cannot replace accumulated market knowledge and cover all the 'what if' scenarios that may occur (i.e. 'black swans').

One broken link in this chain may have been enough to prevent the outcome, but clearly this was not the case. What is really needed is for borrowers, lenders and other interested parties to take their responsibilities more seriously. No amount of regulation can make up for poor market practice and short cuts in the due diligence process. Clearly, market participants did not learn from the Enron affair, which itself was based on off-balance sheet structures. I believe we have now learned our collective lesson, but only time will tell! □

Ross is a partner with a financial advisory company in Toronto. He is a 30-year veteran of the capital markets.