

## DOTZOUR'S TAKE ON PROPOSED BAILOUT

COLLEGE STATION (Real Estate Center) – As negotiations continue over the proposed \$700 billion bailout of the nation's financial system, Dr. Mark Dotzour, chief economist for the Real Estate Center at Texas A&M University, offers his perspective:

“It's a sad day in America when the federal government (the American taxpayer) has to bail out homeowners who purchased homes they couldn't possibly afford. It's sad because of the vast majority of Americans who live within their means and pay their mortgages on time are now being asked to pay for other people's mistakes.

“It's a sad day in America when we have to spend billions to bail out financial institutions that made loans to those people, then sold those loans to pension funds and endowment associations that had no idea of the risk they were taking when they bought the 'complex and sophisticated' bonds. 'Complex and sophisticated' is just a euphemism for 'I have no earthly idea what I'm buying.'

“Now for the pragmatism. If we don't bail out the banks, the American economy grinds to a halt. Many U.S. businesses are financed with short-term notes that mature in 90 to 180 days. This is called commercial paper. What happens when your 90-day note matures, and nobody will refinance it? Just ask Fannie and Freddie, who had \$225 billion in short-term notes mature and nobody would refinance them. Hasta la vista. The commercial paper market is virtually frozen, and many businesses are in the same boat as Fannie was.

“The smartest people working in the global financial system say that this \$700 billion is a good first step, that it might help to thaw the frozen credit markets but that the devil is in the details. Some say it might take another \$500 billion later.

“The fact is that there is a market for these bad loans. It's about 22 cents on the dollar. The problem is that nobody wants to sell for that price as long as the taxpayers will pay a higher price. So the federal government will buy these assets for a higher price, and it's possible that they can sell them later and make a profit. It's possible that the net cost to the taxpayer will be very little. The bottom line is that we are in uncharted waters, and this \$700 billion plan is the best plan that seems to have some hope of temporarily solving the problem.

“The long-term problem is still on the table, and that is the simple fact that the U.S. government can't keep spending more money than it has. Even governments can go bankrupt. The long-term solution for the U.S. government and every American household is to live within their means.

“Who is going to want to invest in mortgage bonds in the future if the federal government can freeze the interest rates below what was promised? Who is going to want to invest in mortgage bonds if the government can cram down the principal on the bonds you bought? Until the federal government can restore some confidence in the global investment community that if you buy a mortgage bond you have a reasonable certainty of getting your principal and the promised interest, the problems will linger.

“The bailout is inevitable and has to happen. Expect more to come. These are just bandages on a gaping wound. Hopefully lessons will be learned, and we will begin to address the illness and not just put on more bandages.”