

Wall Street Deserves Its Scrubbing

By Cella Quinn
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Advisor's opinion: "The system isn't broken, but it is getting scrubbed up. A good housecleaning never hurt anyone, and Wall Street is a master at it."

(Editor's note: Who better to comment on today's events than advisors on the front line trying to explain it all to their clients? From time to time, we'll showcase some of the more eloquent and insightful posts made by advisors.

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Today's market looks a lot like the dot-com fallout from March 2000 to Oct. 9, 2002. In those 19 months, the market plummeted 47%. Investors in the dot-com technology companies (remember Level 3?) took a beating, and many have never recovered.

Those who owned good, quality mutual funds during the dot-com bust had their money diversified globally over many different companies in many different industries. Their accounts went down, but not nearly so much as the accounts of investors who had portfolios full of technology. Ahem, remember Level 3?

What I love about the free enterprise system of business is that sooner or later the excesses fall apart and the good, solid companies persevere.

There is more than enough greed to go around:

1. The couple who lied about their income to buy the \$300,000 house they knew they could not afford if one of them lost their job. (And, possibly even the Realtor who overstepped her/his good judgment and talked them into a home above their means.)
2. The mortgage lender who knew full well the couple was lying and let it go so he/she could get a commission.
3. The mortgage company that said, "Who cares? We're going to sell this turkey off to Freddie Mac/Fannie Mae anyway."
4. The Mac/Mae duo that sold the mortgage to a Wall Street firm who bundled up the mortgages that they knew were subprime and resold them as investments to their clients.
5. The client who was told, "You'll earn 8% to 10% plus, and this is government guaranteed" by a greedy broker and his brokerage firm. The client, also a bit greedy, invested in those mortgage securities *knowing* he was getting way more than market rates.

Anytime it looks too good to be true, it probably is.

Remember the technology and dot-com bust? Well, if you didn't have money in that particular sector, your funds dipped but you didn't get hurt all that much if you stayed in. Those who continued to put money in and buy at the lower levels especially benefited.

Going through a market like this reminds me again why I like mutual funds so much better than individual stocks. The magic of mutual funds is that they compound. When the market is down, the compounding happens at lower prices. Funds are unique in this regard. Nor is there much compounding when money is invested into real estate like farmland or an apartment building. Your maintenance costs with real estate can be significant, and the liquidity is zip.

Something I don't understand: The headlines blaze about all the money being lost. There are always two sides to a trade. Along the way a lot of money has been made on these subprime home loans. See Items 1 through 5 above—those individuals and companies earned money with every transaction. I'd love to have someone add that up. What happened to all of that?



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