



>: WAMU WA-BUSTED!

Friday, November 2, 2007 / Teeka Tiwari

Washington Mutual (WM) joins the growing ranks of financial companies caught up in the web of subprime lies.

It seems that its appraisal company, First American Corp (FAF), is being sued by the NY Attorney General for inflating home values. The NY AG also alleges that First American Corp colluded with Washington Mutual to use a list of preferred *proven appraisers?* that would provide inflated appraisals on homes.

Washington Mutual's response made me laugh out loud so hard I had tears in my eyes. They came out and said, *We have absolutely no incentive to have appraisers inflate home values?*

Hold on a second. They book huge profits from upfront fees by originating mortgages that they get to book in that quarter's earnings. Those inflated earnings are used to determine executive stock-based compensation, and you mean to tell me that they didn't have a vested interest in jamming as much business into each quarter as possible?

Are you kidding me?

Friends, this is the tech wreck all over again. This is just a rehash of the same sorry lies and greed run amok that we witnessed from 2000 ? 2003. These bigwig CEOs are all in CYA mode. Don't be surprised to see some very high profile corporate names going down in flames and some very big executives going off to jail.

Check out Citigroup (C). These guys may have to raise THIRTY BILLION bucks to bail themselves out of their subprime hole. Thirty billion dollars! That's insane! How do guys, supposedly so smart, get to be so wrong? I'll tell you how: It's greed, plain and simple.

These players knew that the party was coming to an end, but Wall Street is such a short-term earnings-driven culture that they didn't care. There was money to be made and bonuses to be had.

Hey, don't get me wrong. I like to get a bonus just like anybody else, but I've learned that it never makes sense to jeopardize the long-term prospects of my business just to generate a one-time gain. These guys in the banks and the brokers just don't think like that because *they are renters, not owners*. You, the long-term stockholder, you're the owner and you are getting the muddy end of the stick from these guys, big time.

They know that, between the investing public and the public purse (*think Fed*), they will get bailed out. The Fed's recent rate cut is all the proof we need to see this old-boy network hard at work once again.

But you know what?

I don't think it's going to work.

As I explained [last week](#), the subprime borrower is getting squeezed between rising mortgage rates in their adjustable rate mortgages and declining housing prices. I first tipped *tycoon Report* readers onto this story back in February of this year. I wrote an article called [Beware of Sub Prime Mortgage Stocks](#)". The article was chillingly prescient (if I do say so myself).

Forget the Fed for a second; the Fed doesn't underwrite mortgages. If you are in the mortgage business, you are going to want a much higher return for all the extra risk you are taking. So how much influence can the Fed really have over mortgage rates?

The key to the subprime mess is that housing prices are declining, and if the asset that you have pledged to secure a loan goes below the value of the loan, you can't refinance. If you can't refinance, you can't repay the loan. If you can't repay the loan, you default.

These rate cuts are not going to boost housing prices, and that's what needs to happen if you are going to stem the subprime bleeding.

The reality is that housing and the subprime market is in a death spiral; nothing can stop it from crashing. There isn't a force on earth that can turn this housing bear market into a bullmarket.

Long story short, it's still too early to start bottom fishing in this sector. Stay away! Yesterday's action indicates that we are now entering the second leg lower in the financials.

Remember what you learned from the tech wreck. Just because something looks cheap doesn't mean it can't get cheaper. They will be a buy at some point, but not yet.

A handwritten signature in cursive script that reads 'Teeka Tiwari'.

Teeka Tiwari
Chief Investment Officer

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