

>: U.S. Taxpayers Taking in the Fannie (and Freddie)

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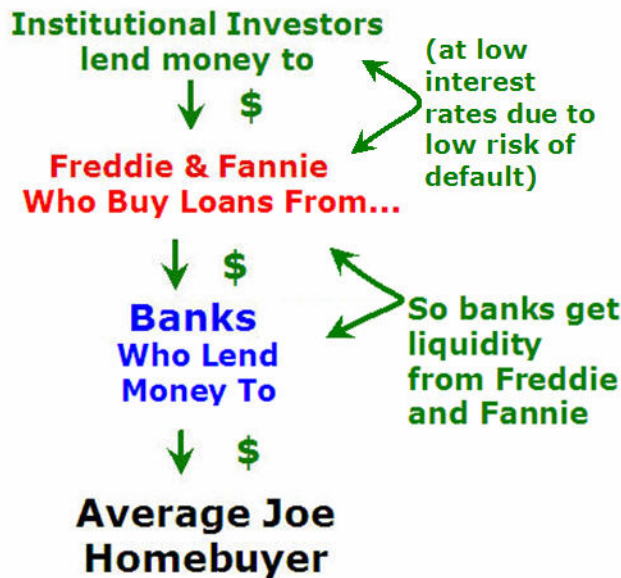
Yeah, I said it. Somebody has to say it!

Congratulations! You (if you are a U.S. taxpayer) are now the proud owner of about \$5 trillion dollars in mortgage debt! Hey, it's diversified - What ever could go wrong?!

By now you've heard the news about the U.S. government buying (or bailing out) the nation's largest mortgage lenders, Fannie Mae (FNM) and Freddie Mac (FRE). Today I'm going to talk about how to profit from the bailout, but first - very quickly - here are the basics...

Most people who have had a mortgage end up making the monthly payment to a different bank than the one who originally gave them the loan. Sound familiar? A loan is a bond and when your mortgage lender changes hands, the banks are basically trading a bond created based on your debt.

Fannie Mae and Freddie Mac purchase home mortgage loans from banks and repackage those loans as mortgage-backed securities by pooling a large number of loans together, thus reducing the risk of default of any single borrower. They either hold the loans on their books, or they sell them to investors around the world. Together, Fannie Mae and Freddie Mac own about half the nation's total.



What's the significance of the government's buyout/bailout?

Here's the lower half (see image above) of the equation:

When banks, which are used to selling over half of their loans to Freddie and Fannie, suddenly don't know if either one will be able to buy loans that the banks write, the banks will be reluctant to lend money. Therefore, they will require a higher interest rate from the borrower (home buyer) to compensate for their incurred risk or they won't be willing to make home loans at all.

When the money doesn't move around, banks lose money due to less activity and housing prices go down as it becomes more and more difficult to borrow enough money to buy a home.

On the flip side, when the bank is able to sell the loans they made (to home buyers) to Fannie or Freddie, they are able to get their money back to make more loans, which in turn keeps the money moving through a healthy system.

Here's the upper half of the equation:

Since the government is backing up Fannie and Freddie, investors are more willing to buy debt issued by the two (more willing to buy their bonds - in other words, more willing to lend Fannie and Freddie money which they, in turn, lend to home buyers in order to capture a spread on the interest rate).

Again, this is important because if institutional investors are less willing to buy debt backed by Fannie and Freddie (without the government

backing) they will require the two to pay a higher interest rate to compensate for the risk of default or they will simply stop buying Fannie's and Freddie's debt. That trickles down to the home buyer who would have to pay higher rates to their mortgage lender.

So because the government is now backing the debt, you can expect the net effect to be reduced mortgage rates because basically the government is the one lending the money. (By the way, that means you - if you are a taxpayer - are the one lending the money. Isn't that nice of you?! You are helping to bail out people who made bad investment decisions.)

Foreign investors own about \$1.5 trillion of the debt issued by Fannie and Freddie so the news sent overseas markets ripping higher as confidence is restored that they won't get the short end of the stick. (U.S. taxpayers are.)

- Japan's Nikkei: up 3.4%
- Germany's DAX: up 3.2%
- France's CAC-40: up 4.4%
- Hong Kong's Hang Seng: up 4.3%

So just remember, when your tax dollars are there to bail out those who don't want to take responsibility for their own actions, people run wild and make big messes. Hey, don't worry, because everyone else will clean it up for you, right?

This is a hard pill to be force fed, folks, but the alternative is obviously much worse.

Okay, let's get back to the way to turn this into a profit...

I know what you are thinking. You think I'm going to tell you to play real estate stocks somehow, or perhaps an ETF of some sort. Well you are right. But first let me talk about the general market.

- First the bears closed out bearish (short) positions,

The market is at a critical point right now. We appear to have bounced off of a very important support level.

- But THEN, strong bulls kept buying stock while nervous bears exited their bearish positions, causing a great big rally in U.S. markets.

Here's why yesterday's action can be used to see the cards the Bulls & Bears are holding:

The U.S. market opened up 2-3%, dipped down to a 0.05% gain, and rallied back up, closing up 2-2.6%.

That tells us that:

This happened on strong volume, confirming Friday's bullish reversal pattern. That means the overly aggressive bears (which add selling pressure to an advancing market) as well as nervous bulls (who also add selling pressure to an advancing market) were just shaken out. This is great for bulls... for now.

Here's what the intraday action look



Don't think for one second that this stabilizes the housing market. We still have nearly a year's worth of inventory, record foreclosures and rising unemployment to deal with. (Imagine if taxes are increased by our next president at a time like this? Geesh, the timing would be awesome - just as long as you are 100% bearish - profiting from large downside moves!)

Either way, Tycoon Report readers can profit; so election SHMELECTION.

Don't think the stock market has put in a long-term bottom either. Maybe it has (though I doubt it), or maybe it hasn't, but that is irrelevant to me. I

look for confirmation first and I don't make assumptions until I see it.

Finally, this isn't very surprising to investors (the institutional ones which are the ones that move the stock market). Everyone knows the two mortgage giants are government sponsored and knew the bailout was imminent when the Federal Housing Finance Agency was created by Congress this summer to regulate Fannie and Freddie.

This tough pill to swallow is probably just a painkiller the stock market gobbled up like Pac-man. But the ghosts won't take long to start flickering and then the chase will be on once again.

Want to run after the ghosts and gobble up as many as you can? It's a risk, but here you are...

Real Estate Companies That Look Decent

Annaly Capital Management, Inc. (NLY)

Boston Properties Inc. (BXP)

Kimco Realty Corp. (KIM)

Public Storage (PSA)

Simon Property Group Inc. (SPG)

Vornado Realty Trust (VNO)

I can't give exact buy recommendations (entry or exit prices) here because it wouldn't be fair to members of [The Trend Rider](#). But I can say that I would wait for a slight pullback to buy any of the stocks mentioned above. I would also remind you that when it is time to get bearish (or exit bullish positions) you should do it with zero emotion whether you are up or down. Remember, I am bullish only in the intermediate-term, but bearish on the long-term trend.

Please feel free to leave your comments by clicking below. How does it feel to own your new bond?

?Profit from the Trend?



Chris Rowe

Chief Investment Officer

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