BUYING STOCKS EASIER THAN REAL ESTATE

REAL MONEY column for The Santa Fe New Mexican
By Rob Rikoon

September 6, 2011

Buying stocks is so much easier than buying real estate. Whenever the market goes down, all that is required to make it bounce back up is a news conference in Washington or an optimistic report out of New York. It almost makes my job of managing money as an investment advisor a piece of cake. We are well into our second decade of market intervention, ostensibly undertaken out of a good hearted desire to keep folks from suffering too much.

Many believe that a majority of Americans vote based on their pocketbooks, which may best be represented by how much a gallon of gasoline costs or what their retirement accounts are worth. My view is that the largest determinate of how confident people feel in their financial future is the value of their home and other real estate. What leads to solid home values is the multi-billion dollar question presently in front of economists.

Even though corporations are reporting record earnings and interest rates are as low as anyone can remember, there just isn't enough economic activity without a robust housing market to get unemployment down or rekindle consumer optimism, which are the lynch pins of a sustainable recovery. With trumpets flourishing, once more into the breach rides our government by contemplating forced mortgage refinancing at current low rates for everything insured by the government sponsored entities (GSE's), such as Fannie Mae and Freddie Mac , who are the guys that blew it big time 3 years ago and who have been on taxpayer life support since then.

It sounds great but only on the surface. People's mortgage payments would go down, due to a 1/3rd reduction in the amount of interest due. But would they owe any less on their homes? No. If they are out of work or underemployed, will they have a better chance of finding a decent job? No. Would they have more money to spend on big ticket items? I don't think so, given the dim prospects for future earnings, most folks will use the savings to pay off their past due high interest rate credit cards. Does the economy get a boost – not really.

Who pays for the reduction in interest rates? A minor portion gets charged to the banks who can afford it the least so we likely will see more bailouts. Some gets charged back to the government, who owns Fannie and Freddie, and this part eventually shows up in the federal deficit. Private investors who own bonds, i.e., savers and retirees, would take the biggest hit through reduced earnings on their portfolios. Does the real estate market get a boost? No, because although foreclosure sales drop way off, borrowers in bad shape still need to unload their overpriced and over leveraged real estate but they have less incentive to be realistic and cut their asking prices. The result is the housing recovery may be delayed by another 3 or 5 or 10 years. Construction of new homes and remodeling activity will remain suppressed because the status quo will reign.

Buying real estate is a messy business. It is hard to predict future costs of management and maintenance and the hassle factor is high. If the government gets in the business of renting 1 million homes that turn out to be financial losses, it will probably turn into another big hole in the federal budget. Allowing people to fail and start over again is another way of rectifying the problem. If we allow the market to fall freely and find its own bottom, then and only then will new owners appear on the scene. They will do so in order to take advantage of the newly created economic opportunities by investing their capital and time so as to turn bad situations into good ones in order to achieve capital gains. This was the American Way before we got used to looking to someone to save us. Markets are, by definition, brutal. Shielding the impact of its cyclical blows makes things worse for everyone.

Rob Rikoon is the lead portfolio manager at The Rikoon Group, a registered investment advisory firm in Santa Fe. He can be reached at rob.rikoon@rikoongroup.com