

MARKETS ARE EFFICIENT—NOT WEB BUZZ 2007.10.01

It is amazing what sparks common stock rallies. First it was the surprise 50 basis point cut in the Federal Funds Rate, and then the rumor that Warren Buffett was coming to the rescue of Bear Stearns.

To the above, we would make the following comments. The cut in the Federal Funds Rate will not help the housing market, as it will have no effect on the repricing of teaser rates taken out over the last three years or so. As a matter of fact, long-term fixed mortgage rates have moved upward since the cut. It does not make the \$1T of “toxic waste” in collateral debt obligations any more secure. It does, however, give a psychological boost to market participants as the Fed is seen as being near “God-like”. The rumor that Warren Buffett is flying to the rescue for Bear Stearns, in our opinion, suggests that things are more serious than even we thought. Mr. Buffett is a “bottom fisher” in that it’s either his way or the highway. We know of a recent instance where he thought a very profitable company was not a good buy at \$8 per share, but within six months or so, sold for 50% more. All this happened before buyout prices really went into the stratosphere. If he is the ultimate white knight in the Bear Stearns case, rest assured they were near desperate for money.

There is no question but what Buffett is one of the great investors of all time. But even he has trouble from time to time. It is our understanding that he and Bill Gates bought into the housing stocks around the time of “recovery” as shown on the following chart of one of the leading housing company’s stocks. This is an illustration only, as we do not know of the specifics in this case. On the other hand, we had first-hand knowledge of the \$8 deal mentioned previously.

Again, psychology is at play in the rallies, which only goes to prove that financial markets are not, and have never been, efficient. We wonder if these “experts” who invented structured debt obligations will some day come to that same conclusion.



Taken from Bloomberg.com