

EXTEND AND PRETEND

*"I see the bad moon arising.
I see trouble on the way.
I see earthquakes and lightning'.
I see bad times today.*

*Don't go around tonight,
Well, it's bound to take your life,
There's a bad moon on the rise.*

- John C. Fogerty
Creedence Clearwater Revival

The age old question of is the glass half full or half empty no doubt depends on what side of the glass you are on. Are you filling it, are you drinking from it or did you come upon it? How do you know unless you yourself are filling it or drinking from it?

My former brother-in-law was a well-known handicapper of horses in Southern California. He knew the horse business inside and out and enjoyed the profits of his endeavors. I asked him once how he picked winners. He laughed and said he didn't - he identified the losers - whatever was left was a potential winner.

Even winners drew substantial scrutiny from his deep analysis because not all winners are profitable. Betting on the favorites or as it is known in the parlance of horse racing, "Betting the chalk," may be heartwarming and adrenalin building but it is not necessarily a moneymaker. Professional handicappers are in it for the money not for the good feeling about winning.

I have found that this principle applies well to business too. One's success frequently depends more on identifying the losers than finding winners. Real losers are easy and quick to identify. Others look and sound good but upon further scrutiny become highly questionable.

What is left is a much smaller group for analysis. Sometimes there is a winner worth pursuing, sometimes there is not. For the professional, losing is often not an option. Knowing when to say no may well be the most important thing to know in business.

Another aspect to asking and answering these questions is what you read and how you analyze it. It's based on your own experience, education, knowledge as well as your willingness to question what you are being told.

Another is one's own perception of reality. One local commercial property owner recently told me "There is no such thing as distressed properties, only distressed property owners." Indeed, a man with cash in hand can solve all kinds of problems.

In the real world it is all about cash flow. It is the air that flows under the economic wing. Without it everything stalls.

Individuals do not enjoy the ability to move funds within a closed financial system like large corporations and governments without any real money leaving the bank. No, we are stuck with cash in and cash out - a simple theory that most of us learn early in life. Unfortunately, too many people forgot or pretend that this simple lesson does not apply to them.

The mortgage banking term “extend and pretend” refers to a lender who changes the terms of a stressed loan and extends the payoff date or other terms into the future in the hope that the borrower will pay and/or the economy will improve.

James Quinn’s recent article “U.S. Economy Extend and Pretend is Coming To An End” brings to light the growing problem of bad retail mortgage and commercial loans coming due that have already been extended because of diminished cash flow and lower real estate prices.

In Quinn’s article, “Extend and Pretend is Wall Street’s Friend,” he claims that there was “A systematic plan to create the illusion of stability and provide no-risk profits to the mega Wall Street banks was implemented in early 2009 and continues today.” He adds, “This master plan has funneled hundreds of billions from taxpayers to the banks that created the greatest financial collapse in world history.”

Continuing, Quinn says, “Part two of the master cover-up plan has been the extending of commercial real estate loans and pretending that they will eventually be repaid.”

Today, there is no shortage of those reporting good news. According to some, things are getting better and not to be concerned. Yet there are others who warn of a pending and very significant financial disaster on the horizon, perhaps as soon as mid - 2014. My personal accountant and tax advisor falls into the latter group. “Dig in and stand by” is their advice. Another says to “think long term.”

Who do you believe, those who say things are ok – the glass is half full, or those who are now yelling warnings of pending doom – the glass is half empty?

Like most things the answer lies somewhere in the middle. It depends too on your own financial picture. Do you have cash in your pocket? Do you have a positive cash flow with your personal finances? What if you get sick? What if you lose your job? What if there is an unexpected emergency? What if...?

But having cash in your pocket and in the bank may indeed provide a false sense of security. Recent reports from some public officials and financial pontificators would have us believe that things are improving and no doubt in many cases they are. However, what about the profound

pension deficits and billions of dollars in unattended infrastructure repairs as well as pending litigation settlements to name a few. Suddenly the winner is a loser after all.

As we focus on finances we tend to be pulled away from other factors that are even more alarming. For example: The “Baby Boomers” are retiring. Their parents are dying and the greatest transfer of wealth in human history is now underway.

As the Boomers leave the work force who will replace them? Who is going to pay the taxes and benefits to support millions upon millions of retirees who will be expecting the proceeds of their labors?

Extend and pretend has been alive and well with pension systems and Social Security. Projected revenue of the past into these programs was nothing short of delusional. What do you suppose is going to happen over the next twenty years as more and more Boomers take their cut from the pot they paid into? What do you suppose they are going to do if they do not receive what they feel they deserve? More importantly and to the point, what are you going to do?

Automation and technology will solve many of the labor challenges ahead. Machines can work without breaks or compliance with a myriad of labor laws. Machines and computers do not complain, call in sick, litigate or create political firestorms.

The growing labor concern quickly translates to immigration and is a growing challenge for most of the industrial world. Iwao Nakatani’s recent article “Drastic Change in Immigration Policy Off the Japanese Election Agenda” opens bluntly: “Anything short of a major reversal in Japan’s population growth will see Japan’s population decline dramatically, exacerbated by falling birthrate and an aging society. For this reason, Japan’s basic immigration policy – to welcome ‘highly skilled professionals’ like researchers and skilled workers while strongly regulating the entry of unskilled labor – is indeed in need of desperate reform.”

The same can be said of the United States. Between those who are retired and will be retiring coupled with those who can-not or will not work, not many are left to pay the bills. Even in cash rich areas there may well not be enough to stay solvent.

The glass half full or half empty – you must decide. As for the winners and the losers, the list seems to be growing rapidly as to who the losers are despite their preoccupation to convince us otherwise.

Translated, the question is do we have good times or bad times ahead? I suppose it boils down to if you are filling the glass or drinking from it.