

September 22, 2008

Dear President Bush:

A Plan to End the Financial Crisis and Preserve Capitalism:

Step 1. Require all banks to re-appraise the assets securing their problem mortgage loans. Any loan-to-value greater than 80% must be written down to 80%. These charge-offs will be a big hit to bank capital and hurt. To offset some of the pain, give banks a break by allowing two times the actual write-down to be expensed for tax purposes. A tax break will give a boost to otherwise healthy banks and provide a small cushion to their capital ratios. Assets with no economic value can be put directly to the Fed/Treasury program.

Step 2. Houses put to the Fed/Treasury program should be de-constructed. There are too many houses in the wrong places around the U.S. They need to be taken off the market...so knock them down. Ridding the housing market of excess will put a floor under the appraised values in step 1, and reduce the probability for future charge offs – which are coming if nothing is done to shrink supply. Create a government agency to hire and train displaced construction workers to carry this out. Excess building materials must be gotten rid of as well to prevent undercutting suppliers. Donate used materials to lesser developed areas of the U.S. or ship to other spots in need around the globe. Should this prove too costly, then burn them.

Step 3. Get rid of mark-to-market accounting rules for banks. Fundamental valuation works and it is inherently more stable than mark-to-market. The market isn't always right. In fact, it's hardly ever exactly right. And when the market is right, it doesn't last long. Fundamentals change much more slowly than the market. Therefore, require banks to conduct a discounted cash flow (DCF) appraisal of assets underlying their mortgage-backed and other related financial investments. Their assumptions should be published in SEC reports, similar to the way pension assets and liabilities are already reported. Investors can determine whether or not individual company appraisals are any good and their opinion will be reflected in the company's stock price. Fundamental valuation of financial assets is necessary to stabilize and preserve bank capital – assuming DCF analysis yields greater asset values than mark-to-

market. Plus, mark-to-market does not work. We have seen how quickly things snowball using non-DCF measures so let's use a method that will work in good markets and bad.

Step 4. Encourage well-capitalized banks and financial companies around the world take over failing banks. Tax incentives will help here as well.

All of this will be painful and take time. But following this route not only will put people to work and end the financial crisis, it will preserve some form of capitalism in our society where risk in the financial system is properly measured and rewarded.

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