# Fixing the Crisis is Not So Easy

Five Problems Block Government Success

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New York OCT 27: Most Americans know the phrase, "if it ain't broke don't fix it." In the good times, when the economy boomed and Wall Street prospered, it looked like nothing was broke. The free market, we were told, was working like magic insuring prosperity and progress.

But then it happened, out of sight and out of mind, an upward trajectory turned in the other direction. In what was for many an unbelievable chain of events, markets started melting down, banks began writing down portfolios clogged with asset-backed securities that had no assets behind them. Confidence shattered. Suddenly, believers in unregulated transactions realized something was very, very wrong.

Alan Greenspan was "shocked" and said he was wrong to support deregulation of financial markets. As headlines conjured up breadlines and recession, with "something worse" threatening, the government was pressed to act.

Over a year later, after eight interest rate cuts, with one more promised, and the injection of trillions into credit markets and banks worldwide, little has changed. Markets are volatile and trending down while banks are still not lending despite frequent projections of massive unemployment and stagflation.

At the same time, we live in a country that believes that whenever there are problems, there must be solutions. And in the case of the financial crisis, there is no shortage of proposals especially because the whole system—if not capitalism itself—seems at risk. (Even the NY Times ran an editorial on "Rescuing Capitalism.") This is not a situation that inspires confidence in token reforms and minor adjustments. There seems to be a consensus that this crisis is systemic and structural even as the candidates reduce it all to tax policy.

That hasn't stopped the government from dipping into its tool bag and throwing everything it has at the problem—bailouts on an unprecedented scale, including, now, of insurance companies and auto lenders There have been pro-business rule changes even partial nationalizations of banks, mortgage companies, and insurance combines.

Together, the Treasury Department and the Federal Reserve Bank seem to be fighting on every front. They appear to be giving away money. Is it working?

"Scarcely a day goes by with out some dramatic new initiative," writes The New Yorker's financial columnist James Suriwieki, "even as market chaos makes each new idea soon seem like ancient history."

Why is that? Surely the people in command are smart, savvy and know the system well. What are they missing? They now know its broke (and many of them are broke too) but they can't seem to fix it.

Here are five views on what they are getting wrong.

l. THE SYSTEM NEEDS TO COLLAPSE

That's the view of a perennial bear investor Marc Fabor who "thinks the market was primed for a technical rally but is not keen on the long-term prospects for the US economy:

"The governments in this world have no other option but to print money. That will lead down the road to inflation," Faber said. "You don't need to be an economist graduated from Harvard to know we're already in a recession. They will just put white paint on a crumbling building….

"To rebuild economic health in the United States, you need a serious recession that will last several years," he said. "The patient that got drunk on credit growth needs to go into rehabilitation. To give him more alcohol, the way the Fed and the Treasury propose to do, is the wrong medicine."

2. CONSUMERS ARE NOT SPENDING

Bloomberg reports:" The big concern is that households, spooked by the turmoil in financial markets, will cut back rapidly and sharply, plunging companies into bankruptcy and deepening a recession that many economists say has already begun.

"If we did have a quick cut in spending, it could turn a pretty nasty recession into possibly the worst downturn we've seen in the postwar period," says Michael Feroli, a former Federal Reserve official now at JPMorgan Chase & Co.

3. MORAL HAZARD: THEY ARE BAILING OUT THE WRONG PEOPLE

There is something fundamentally wrong in rewarding the people who are responsible for the problem. Worries William Buitner, a financial historian at the London School of Economics, that this will lead to more collapses in the future: "by boosting the incentives for future reckless lending to elephantesquely large financial enterprises. Unless not only the existing shareholders of the banks benefiting from these capital injections but also the holders of the banks' unsecured debt (junior and senior) and all other creditors of the bank (with the possible exception of retail depositors up to some appropriate limit) are made to pay a painful penalty for investing in excessively risky if not outright dodgy ventures, we are laying the foundations of the next systemic crisis, even as we are struggling to escape from the current one." The bailout was sold deceptively.

A New York Times investigation found it was Intended to foster bank consolidation, not loans. Journalist Sam Smith wrote:

"Never in the history of the United States has so much public money been spent with so little accounting of where it is right now and where it's going next. Never has so much public money been spent by order of officials who helped to create the crisis the money is supposed to resolve. Never has so much public money been spent by officials for the benefit of so many former colleagues. Never has so much public money been spent with so little explanation by the media. And never has so much public money been spent with so little debate over possible alternatives.”

4, FINANCIAL SCAMMERS AND CRIMINALS ARE GOING UNPUNISHED

The FBI announced that it lacks the staff to fully investigate the pervasive crimes on Wall Street.

5. GOOD PEOPLE ARE LEAVING IN DISGUST

Some of the best and the brightest are giving up, rejecting businesses based on flimflams and deceptive marketing. Two years ago, a very successful investor, Andrew Ladhe, started returning money to his investors. “Our entire banking system is a complete disaster,” he wrote. “In my opinion, nearly every major bank would be insolvent if they marked their assets to market.”

In October 2008 he closed his firm all together explaining:

> “Recently, on the front page of Section C of the Wall Street Journal, a hedge fund manager who was also closing up shop (a $300 million fund), was quoted as saying, “What I have learned about the hedge fund business is that I hate it.” I could not agree more with that statement. I was in this game for the money. The low hanging fruit, i.e. idiots whose parents paid for prep school, Yale, and then the Harvard MBA, was there for the taking. These people who were (often) truly not worthy of the education they received (or supposedly received) rose to the top of companies such as AIG, Bear Stearns and Lehman Brothers and all levels of our government. All of this behavior supporting the Aristocracy only ended up making it easier for me to find people stupid enough to take the other side of my trades. God bless America.”

These are just five reasons why “the quick fixers” are unlikely to succeed. Notes Harpers, we a need more than tinkering. They call for a fundamental reconstruction at a time when we are also “menaced by dwindling energy supplies and accelerating climate change.”

Also, the Captain Ahabs in charge should admit defeat and step down as was suggested by this comment on a financial website:

> “Perhaps Bernanke and Greenspan should see if there is an opening for the captain of the Exxon Valdees, job requirements: asleep at the switch.”te>

Still to be answered: can the system be saved from itself?

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