Obama's Perilous Compromise with Wall Street Looters

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President Obama has made a bad mistake: Instead of cracking down on serial looters and complicit regulators, he plans to reward them.

Looters have taken over America's Treasury. The executives who successfully ransacked their own banks, investment funds and insurance companies have set their eyes on Obama's stimulus. Tragically, the architects of the current economic fiasco have been placed in charge of America's recovery.

President Obama has made an enormous mistake. Instead of cracking down on serial looters and complicit regulators, he wants to guarantee the financial sector's obligations, which are several times larger than America's economy. This is a Ponzi scheme far beyond Bernie Madoff's imagination. Simply put: The government is breaking the rules of capitalism to reward the most reckless capitalists.

Is it unfair to criticize President Obama before he and his experienced team have a chance to enact new laws and regulations? For guidance on this question, let's turn to the father of capitalism, Adam Smith. Here's how Smith concludes Wealth of Nations, Book I:

> "The proposal of any new law or regulation of commerce which comes from this order [the capitalists], ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but most suspicious attention. It comes from an order of men, whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it."

Consider Obama's Economic Czar, Larry Summers, who comes fresh from heading a highly secretive hedge fund. As Clinton's Secretary of the Treasury, Summers championed the repeal of the Glass-Steagall Act, which led directly to the excessive risk-taking by newly enlarged financial entities deemed too big to fail when they failed. Additionally Summers and Robert Rubin lobbied intensely for legislation signed by Bill Clinton that forbid government oversight of derivatives, the toxic instruments that have poisoned balance sheets around the world. Summers' former deputy Tim Geithner, the new Secretary of the Treasury, has supervised more recent rip-offs. He bears significant responsibility for the Lehman Brothers' catastrophe and for the flawed Fannie Mae, Bear Stearns and AIG bailouts. At Geithner's confirmation hearing, he must be asked repeatedly why the looters were rewarded and why plans giving taxpayers more equity were rejected.

Sherlock Holmes was once famously asked by a Scotland Yard detective: "Is there any other point to which you would wish to draw my attention?" Holmes: "To the curious incident of the dog in the night-time." Detective: "The dog did nothing in the night-time." Holmes: "That was the curious incident."

Why haven't America's economists barked timely alarms? Are they blinded by their faith in markets? Perhaps the old saying should be reworked: In America, those who can, loot. Those who can't, teach wealth-friendly philosophies masquerading as hard science. In their mind-set, fraud is the province of Bernie Madoff, not Robert Rubin.

But what could be more criminal than Rubin's former employees, Hank Paulson and Tim Geithner, awarding the sweetest of all bailout deals to Citi, where Rubin sits as a highly-paid senior counselor and director. Throughout his career Rubin has pushed for more complex risk instruments and less government regulation. How stupid does the quintessential Wall Street/Washington wise man think people are when he claims never to have heard of Citi's most toxic assets? And to brag that he's been "very involved" at Citi, but blames the company's excessive risk-taking on a presentation made one day by an outside consultant? After confessing such failures of oversight, an honest man would have resigned his posts.

Yet it's not only Rubin's acolytes who are pushing Obama's recovery plan. Experts from both parties have also endorsed it. The only catch? These are the same experts who were blind-sided by the mortgage security frauds that led to the credit freeze that triggered the de-leveraging that's plunged the world close to a Depression.

Does all this sound like a simple-minded diatribe? Perhaps it is. But when analyzing America's financiers, a simple-minded (as opposed to a naïve) approach may be best. For example, Hank Paulson, Ben Bernanke and Tim Geithner thought that the banks they generously recapitalized with the taxpayers' money would begin lending again. Instead the banks used the bailout cash to buy other banks, issue dividends or simply profit on Treasury spreads – i.e., to make what bookies call their juice.

It's altogether possible that Barack Obama's recovery plan will bless sweetheart deals and generate enough public debt to destroy global confidence in our government's bonds. Foreigners, who own about half of all Treasuries, could stop funding America's deficit-driven recovery plan. During Obama's administration, the dollar might lose its reserve-currency premium.

Would all Americans then suffer equally? No. Those likely to profit most from Obama's stimulus before we go bust are his political allies, and especially his big donors. That's the nature of the doling-out beast. To minimize corruption, Obama must pro-actively prevent Chicago-style swindles. E.g., who owns the real estate adjacent to the infrastructure the government will build? What specific penalties will be incorporated into Obama's recovery plan to punish politically-connected profiteers?

If a spiraling out-of-control stimulus seems as if it's undermining the full faith and credit of the U.S. government, Obama's biggest donors will hedge their personal risk by parking some of their capital abroad. Have they've done so already? A senator should ask prospective nominees this question at their confirmation hearings.

Obama could be a different kind of president. His broad base of financial support ensures he won't lack funds for a reelection run. The dark side of Obama's presidency, however, is likely to come less from ethical failings than from his fondness for compromise.

You can't compromise with America's looters. They're too opportunistic. The economics team Obama assembled betrays his respect for elites and a caution that may doom his presidency. A bolder politician would stimulate the economy and simultaneously expose the moral violations at the core of our economic predicament. Leaders who sent the cops home need to be shamed, not promoted. Financiers who misled investors should be prosecuted, not bailed out. Attorney General nominee Eric Holder, the man who pardoned Marc Rich, doesn't seem likely to take up these tasks.

On Inauguration Day, President Obama will surely deliver an inspirational address. But the confidence he inspires will be worthless until he calls out and cuts off the thieves.

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