latest chapter in the socialization of risk and its corollary, moral hazard. Anyone who works long enough on Wall Street knows, at least subconsciously, that this is the way things work: if the going gets tough, a small coterie of unelected and mostly unaccountable officials in Washington will probably decide that your employer is too important to fail. In an effort to keep that from happening, wages, savings, fixed-income streams, and Social Security checks will be inflated away to "ensure the stability of the financial system." Creative destruction is the mantra until things threaten to get creative in the Hamptons.

Just because the Fed understood the implicit obstacles to funding a classic, sustaining bailout of Bear Stearns doesn't mean the temptation wasn't there. The media almost always misses an important reality: monetary policy can effect a *de facto* bailout, particularly for Wall Street, almost as easily as a direct handout. In the weeks leading up to the Bear Stearns debacle, the Fed wasn't bashful at the levers of policy. One such lever is temporary open-market operations, which the Fed uses on a daily basis to target short-term interest rates. When the Fed adds reserves to the banking system, the salutary effects of the associated liquidity spill over into other instruments, including stocks and commodities. In early February, the value of this temporary liquidity pool was $15 billion. As stress increased in the financial markets, the Fed boosted that to a high of $77 billion on March 12— just as trading-desk rumors about a possible bank failure peaked and two days before the intervention to support Bear Stearns.

The Fed was busy in other ways. That same week, on March 11, it announced formation of the Term Securities Lending Facility, to accept lower-quality collateral from primary dealers, of which Bear Stearns was one. This was just one new program whereby the Fed takes

DEEP BACKGROUND

Israel is the only country in the world that has a policy of "directed assassinations" of its enemies and U.S. Director of National Intelligence Mike McConnell is apparently prepared to go along with Tel Aviv's efforts to conceal that activity. Israel has denied that it was behind the assassination of Hezbollah Deputy Secretary General Imad Mughniyeh in Damascus on Feb. 12, a claim supported by McConnell, who suggested the death was probably the result of internal conflicts within Hezbollah. But the CIA investigation of the bombing has revealed that the Israelis carried out the killing using Palestinian refugees they had recruited. The assassination quickly became an open secret in Tel Aviv, with Prime Minister Ehud Olmert congratulating the head of Mossad. And the Syrian government may have been complicit, allowing the operation to proceed because Mughniyeh was becoming an embarrassment. After attending a diplomatic reception at the Iranian Embassy, he had been returning to his parked car when another vehicle behind his exploded, killing him instantly. The use of remote-controlled explosives is well within the capabilities of every intelligence service in the Middle East, but the set-up for the operation raises a number of questions. Mughniyeh normally traveled with a Syrian government-provided armed bodyguard. The guard was absent that night. Also, foreign embassies in Damascus have police details outside, making it impossible to park the bomb vehicle without it first being inspected and cleared. Mughniyeh had been implicated by the CIA in the deaths of several Agency personnel in Lebanon and also Chief of Station William Buckley, but he was thought to be semi-retired and had more or less fallen off our screen—but not Israel's.

❖

It appears to be no coincidence that President Bush, Sen. John McCain, Gen. David Petraeus, and Vice President Dick Cheney have all again been denouncing Iran. President Bush's declaration that Iran wants "a nuclear weapon to destroy people" was later qualified by a spokesman insisting that Bush was only "speaking in shorthand," but Iran-bashing is once more officially in season. Some intelligence officers opposed to an Iranian adventure are nervous that something is afoot, reportedly because the White House has asked for some "new initiatives" against the mullahs. Sources in the White House are saying that the security card will be played heavily in the lead up to the November elections.

❖

An unidentified U.S. Navy nuclear submarine stationed in the Red Sea has joined the fight against international terrorism. On March 3, three Tomahawk cruise missiles were launched against a target in the Somalian town of Dobley, which straddles the border with Kenya. According to local mayor Ali Hussein, three civilians were wounded, a house damaged, and three cows and a donkey killed. The target of the attack, Saleh Ali Saleh Nabhan, a Kenyan who was allegedly involved in attacks on Israeli tourists in Mombasa, Kenya in 2002, was not present. Nabhan is not even an identified terrorist. He is only on the FBI list for questioning in connection with the Mombasa attacks. Tomahawk cruise missiles cost $1.5 million each.

Philip Giraldi is a former CIA officer and fellow at the American Conservative Defense Alliance.

bad decisions off the books of Wall Street firms by accepting riskier paper for longer periods of time.

So Washington went all out trying to buttress Wall Street and particularly Bear Stearns. But there were consequences. On Feb. 6, with the Fed's liquidity pool at that restrained level of $15 billion, oil traded at $87 a barrel. On March 12, responding to the Fed's extraordinary measures, it closed over $109. Gold, in its role as monetary watchdog, was active as well. During the first week in February, it traded at $887 an ounce. A few days after the Fed's liquidity efforts peaked, it was well over $1,000. The dollar recoiled in horror at the Fed's onslaught. The dollar index, a measure of the dollar's value against a basket of major currencies, plunged from $77 on Feb. 7 to $71 on the day of the Bear Stearns news, tracking the Fed's work almost perfectly and anticipating further interest-rate cuts. The digits on those gas pumps off the West Side Highway flickered by faster and faster.

The overarching goal of those cuts, which began last year, has been to steepen the yield curve, which plots the yield on Treasury debt from maturities of three months to 30 years. Banks are more profitable with a steeper curve because they borrow short and lend long and pocket the difference. The Fed's strategy has shown incipient signs of working. On March 18, just a few days after the Bear Stearns news, both Goldman Sachs and Lehman Brothers announced better than expected earnings. Their stocks gained by 16 and 46 percent respectively. The next day, Morgan Stanley also surprised on the upside, and its stock rose by 36 percent over the next three days. Visa's initial public offering on March 19 was a huge success, with the stock jumping 28 percent on its first day.

But what about the public? So far, the results haven't been as promising. Former Fed governor Lyle Gramley said, "In all past recessions, I was always quite sure that if the Fed stomped hard on the gas pedal, the economy would turn around and start to grow. But they've now stomped hard on the gas, and credit is not more available, it's less available." It's not hard to understand the sour mood. In a March CNN/Opinion Research poll, 91 percent of respondents said they were somewhat or very concerned about the rising rate of inflation. That exceeded the proportion of people worried about jobs, the stock market, or falling home values. They aren't delusional. In late February, the government reported that wholesale prices over the previous 12 months posted their sharpest rise since 1981.

Ludwig von Mises once wrote, "No emergency can justify a return to inflation. Inflation can provide neither the weapons a nation needs to defend its independence nor the capital goods required for any project. It does not cure unsatisfactory conditions. It merely helps the rulers whose policies brought about the catastrophe to exculpate themselves." Yet the universe of "emergencies" has been expanding to include elections, natural downturns in the business cycle, inconvenient stock market weakness, and bad decisions by Wall Street firms—with predictable results.

Inflation's defining characteristic is expediency. It obviates sacrifice and postpones pain. That makes it a natural complement to many political ventures, particularly unpopular wars. As early as 1965, Lyndon Johnson's economic advisers worried about rising inflationary pressures. As Johnson resisted calls for new taxes, the deficit for fiscal 1967 came in at $9.8 billion. By the time Congress and the White House finally agreed on a tax increase in 1968, after years of escalation in Vietnam, the deficit was $25.2 billion and inflation was rampant.

Of course, it would get far worse over the next decade. Even as the seeds of inflation planted in the mid-1960s grew, Richard Nixon put pressure on Fed Chairman Arthur Burns to goose the economy for the 1972 election. That dynamic continued and worsened during the 1970s. By the early 1980s, Ronald Reagan was dealing with the consequences of decisions made by Johnson and Nixon over a decade earlier. Part of Reagan's legacy is the latitude he gave Paul Volcker, as risky and painful as that was, to deal with those problems. Unless one believes the next president will want to take the hit for Bush's decisions, or that someone with Reagan's mandate and courage is about to appear, whoever is in the White House a decade from now will probably confront the economic fallout from current policies. But by that time will anyone remember how it all started? How many cursed LBJ or Nixon in 1979? The White House not only knows the answer, it's counting on the nation's forgetfulness.

Federal Reserve officials, safe in the arcana of their craft, might not have to depend on the public's short memory. The opaque nature of monetary policy could do the trick. For this article, I asked customers at a gas station in New York City one question: "What's the main reason for the high price of gas?" Five blamed either Bush or Cheney. Four blamed oil companies. Three said they did not know. Three claimed price gouging by gas stations. Two said, "Everything is going up." Two cited "inflation," with one mentioning the dollar. Two pointed to the campaign in Iraq. One said, "We're running out of oil." One blamed "big cars." One blamed "the Arabs." One apparently upscale customer driving a late-model car blamed "too much money being printed right now." When pressed further, he named Alan Greenspan.

For Ben Bernanke and the current Fed, so far it looks like mission accomplished. ■

Wilson Burman is the pen name for the New York City investment professional who writes The Cunning Realist blog.

Bush's Black List

ON READING George W. Bush's discourse to the New York Economic Club last week, Cicero's insight came to mind: "To be ignorant of what occurred before you were born is to remain always a child."

With the Iraq War entering its sixth year, the dollar sinking to peso levels, the economy careening into recession, and 12 to 20 million illegal aliens roosting here, Bush alerted us to what really worries him: "I'm troubled by isolationism and protectionism ... [and] another 'ism,' and that's nativism. And that's what happened throughout our history. And probably the most grim reminder of what can happen to America during periods of isolationism and protectionism is what happened in the late—in the '30s, when we had this America First policy and Smoot-Hawley. And look where it got us."

Let us try to sort out this dog's breakfast. First, America was never isolationist. From its birth, the Republic was a great trading nation with ties to the world. True, in 1935, 1936, and 1937, a Democratic Congress passed and FDR signed neutrality acts to keep us out of the Italo-Abyssinian and Spanish Civil wars. And FDR did say, "We are not isolationist except insofar as we seek to isolate ourselves completely from war." But how did staying out of Abyssinia and Spain hurt America?

As for Smoot-Hawley, it was a tariff enacted in June 1930, nine months after the Crash of 1929, which occurred, as Milton Friedman won a Nobel Prize for proving, when the stock-market bubble, caused by the Fed's easy-money policy, burst. Smoot-Hawley had nothing to do with a Depression that began in 1929 and lasted through FDR's first two terms. This is a liberal myth, probably taught to Mr. Bush by New Deal Democrats at the Milton Academy.

America First was an organization of 800,000 anti-interventionists formed at Yale in 1940 by patriots like Gerald Ford, Potter Stewart, and Sargent Shriver, backed by John F. Kennedy, to check FDR's drive to war. Herbert Hoover supported it, and its greatest spokesman was the Lone Eagle, Charles Lindbergh.

But America First did not make policy. FDR did. And it was FDR who, by cutting off Japan's oil in July 1941, rebuffing Prince Konoye's offer to meet him in the Pacific or Alaska, and issuing a virtual ultimatum on Nov. 26, 1941 to get out of China, propelled Japan to its fatal decision to attack Pearl Harbor on Dec. 7.

Isolationist is an epithet used to smear those patriots who adhere to George Washington's admonition to stay out of foreign wars, Thomas Jefferson's counsel to seek "peace, commerce and honest friendship with all nations, entangling alliances with none," and John Quincy Adams's declaration that America "goes not abroad, in search of monsters to destroy." Does Bush regard these statesmen as blinkered isolationists?

Protectionism is the structuring of trade policy to protect the national sovereignty, ensure economic self-reliance, and "prosper America first." It was the policy of the Republican Party from Abraham Lincoln to Calvin Coolidge. America began that era in 1860 with one half of Britain's production and ended it producing more than all of Europe put together. Is this a record to be ashamed of?

Compare protectionism's success to Bush's record. Since 2001, he has presided over the seven largest trade deficits in history, the loss of 3.5 million manufacturing jobs and the collapse of the dollar, and added but one-fifth of the private sector jobs Bill Clinton created. Gold has gone from $260 an ounce to $1,000, oil from $28 a barrel to $100.

"Nativism" is another smear term, dating to the early 1850s and the Know-Nothing Party, which sought to halt immigration after millions of Irish flooded in following the famine of 1845. It carries a connotation of xenophobia, the fear and hatred of foreigners.

Thus does Bush tar critics who deplore his dereliction of duty in failing to defend this nation's borders against a Third World invasion that may turn this Republic into a Tower of Babel.

From 1924 to 1965, there was indeed little immigration. Does that make Coolidge, Hoover, FDR, Harry Truman, Dwight Eisenhower, and Kennedy knuckle-dragging nativists? When JFK took office, we were as united and strong a country as we have ever been. How did we suffer from not having 12 to 20 million illegal aliens here?

In smearing as nativists, protectionists, and isolationists those who wish to stop the invasion, halt the export of factories and jobs to Asia, and stop the unnecessary wars, Bush is attacking the last true conservatives in his party. Which is understandable. For after the judges and tax cuts, what is there about Bush that is conservative? His foreign policy is Wilsonian. His trade policy is pure FDR. His spending is LBJ all the way. His amnesty for illegals is Teddy Kennedy's policy.

Two-thirds of the nation says we are on the wrong course. Two-thirds rejects NAFTA and amnesty. Two-thirds wants out of Iraq. Two-thirds rejects Bush. Bush says that people are being misled by those wicked old isolationists, protectionists, and nativists. At least he and Poppy will have something to agree on in retirement. ■