



What Happened to Market Discipline?

This Is Not a Story of Private Enterprise but Cynical Political Opportunism.

Opinion by JOHN STOSSEL

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Barack Obama says, "[Today's economic problems are] a stark reminder of the failures of ... an economic philosophy that sees any regulation at all as unwise and unnecessary".

What? Does that mean that until last week the Bush administration embraced the free market? Nonsense. Governments at all levels have regulated and subsidized the housing and financial industries for years. Nothing changed under President Bush.

The government-backed Fannie Mae and Freddie Mac were created precisely to *interfere* with the housing and mortgage markets. In effect, Freddie and Fannie diverted money to people who wouldn't have qualified for mortgages in a real private market.

Had actual private companies performed these activities, they would have been subject to market checks. But they were not. The results were predictable.

Now that it's all tumbling down, the politicians and pundits blame the free market.

It's not simply misunderstanding. It's demagoguery by people who will never admit that their "progressive" social policies have spawned a taxpayer bill that boggles the mind.

This is a story not of private enterprise but of cynical political opportunism. Moral hazard -- the poisonous mix of private profits and taxpayer-covered losses -- is what you get when politicians indulge their hubris to redesign society. The bailout of those companies holding bad mortgages -- big-business socialism -- sets us up for the next crisis.

Maybe the Republican presidential candidate will dissent? Not a chance:

John McCain says, "We are going to fight the greed and irresponsibility on Wall Street. These actions [leading to crisis] stem from failed regulation, reckless management and a casino culture on Wall Street. & We need strong and effective regulation & ".

He proposes a new bureaucracy, the Mortgage and Financial Institutions Trust (MFI), which he says will "provide troubled institutions with an orderly process to identify bad loans, provide funding and eventually sell them at a profit. & The MFI will supervise the sale of loan assets at market prices and *purchase them as necessary*".

A government agency is going buy bad loans and make a profit selling them. Give me a break!

Irresponsibility induced by government-created perverse incentives is the culprit. For decades politicians of both parties have relieved big companies of the responsibility that market discipline would have imposed. The promise -- explicit or implicit -- to bail out companies "too big to fail" weakens market discipline. That invites recklessness.

What if the government cut Freddie, Fannie, Bear, AIG and the others loose and let them do what other businesses do on hard times: renegotiate with creditors and revalue assets? Would there be another Great Depression? Not likely. What turned a recession into the Great Depression was the Federal Reserve's contraction of the money supply. I doubt they'd make that mistake twice.

Public officials say the big companies must be saved to prevent a devastating credit "lock." Really? Without a federal bailout, lending wouldn't have resumed? The market wouldn't have sorted it out? Prices wouldn't have found a more solid floor? We'll never know.

We do know that the taxpayer will buy -- Probably for too much money, because the private sellers will fool the government managers -- at least \$700 billion in "illiquid" assets. Where will this money come from: taxation, borrowing or the printing press? What will that do to our economic well-being?

Crisis is the friend of the State. The politicians are desperate to be seen as "showing leadership," so we're surely in for a new round of government interventions. Watch for the equivalent of the Sarbanes-Oxley Act. There'll be much posturing about how the new regulations "will keep this from ever happening again," but that's more nonsense because the root problem is not lack of regulation. It's government social engineering of the housing market, which will be unchanged.

This is the path to stagnation and poverty. As Nobel Laureate F.A. Hayek taught, markets are too complicated for planners to know enough to plan them. The relevant information, scattered unspoken among billions of market participants, is beyond the bureaucrats' reach.

We do need protection from reckless businessmen. But there is only one way to provide that: market discipline. That means: no privileges, and no bailouts.

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