"THE TRUTH BEHIND THE FINANCIAL CRISIS"

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MR. TOM FITTON: Good afternoon, everyone, and welcome. I'm Tom Fitton. I'm president of Judicial Watch. Judicial Watch is a conservative, non-partisan educational foundation dedicated to promoting transparency, accountability, and integrity in government, politics and the law.

Through its educational endeavors, Judicial Watch advocates high standards of ethics and morality in our nation's public life, and seeks to ensure that political and judicial officials obey the law and do not abuse the powers entrusted to them by the American people. Judicial Watch does not endorse or oppose candidates for public office.

Our topic this afternoon is "The Truth behind the Financial Crisis." In the last few months, our country has traveled far down the road to perdition of what I'll charitably call socialism, or charitably, National Socialism in response to the financial crisis.

And here's my take on the true source of the financial meltdown in the home mortgage industry, which led to the collapse of Fannie Mae and Freddie Mac and today's attendant financial crisis. I think we should follow the money back several years and let me quote from an article from the September 30th, 1999, edition of the *New York Times*.

"In a move that could help increase homeownership rates among minorities and low-income consumers, the Fannie Mae Corporation is easing the credit requirements on loans that it will purchase from banks and other lenders."

The *Times* says, "The action, which will begin as a pilot program involving 24 banks in 15 markets, including the New York metropolitan region, will encourage those banks to extend home mortgages to individuals whose credit is generally not good enough to qualify for conventional loans. Fannie Mae, the nation's biggest underwriter of home mortgages, has been under increasing pressure from the Clinton administration to expand mortgage loans among low and moderate-income home people and felt pressure from stockholders to maintain its phenomenal growth in profits."

That's the *New York Times* again in 1999.

The article goes on to predict that such a strategy might not cause problems during times of economic prosperity, but that Fannie Mae could run into serious financial difficulty during an economic downturn. And so now the financial markets are in crisis and the federal government has expanded its power in a way unparalleled in recent American history.

Now, while the Clinton administration is certainly culpable for getting the ball rolling on these high-risk loans, there is plenty of blame to go around. Fannie Mae led a bid for points by Clinton's former budget director, Franklin Raines, and former Obama campaign advisor, Jim Johnson, took Clinton's risky gamble and then doubled down. The pair allegedly cooked the books at Fannie, created a market for these dubious mortgages, and then took huge bonuses before leaving the company.

Both men have also been accused of accepting special mortgage deals from Countrywide, a co-conspirator in this financial mess. Johnson resigned from his official position with the Obama campaign over the scandal, though he, like Raines, may still be advising him.

And to be sure, these companies – and I use the term companies loosely – contributed generously to Republicans and kept many Republicans on the payroll and on their boards. Some will point to Rick Davis, McCain's campaign manager, as another example of someone who had his hand in the proverbial Fannie Mae cookie jar.

Politicians on Capitol Hill were no better. For example, Senate Banking Chairman Chris Dodd, Democrat from Connecticut, who was also nabbed in the Countrywide mortgage scandal, took more money in campaign contributions from Fannie Mae and Freddie Mac than anyone else in the U.S. Senate.

And when reform proposals, unsurprisingly for Fannie and Freddie were put before Dodd, he called them, quote, "ill advised." Barack Obama, with only four years in the Senate under his belt, is close behind Dodd in terms of donations received from Freddie and Fannie. McCain, I think, is way down there and I guess, Sheila, you can provide some more information as to where they stand in terms of contributions from this specific industry.

Despite their accounting problems and dire warnings of crisis, these government-sponsored enterprises with the support and protection of liberals in Congress, and special interest groups like ACORN, pushed for more subprime lending for their politically correct constituencies they served, and calculating financial institutions, too many of which had corrupt relationships with these very same politicians, were happy to play along. Now our country, if not the entire world, is facing a financial disaster.

Any lessons learned? Not in this town. Fannie Mae and Freddie Mac are raring to reinvigorate the ruinous business of making subprime loans to those who can't handle them. And you can bet Congress is eager to take, quote, "profits," unquote, from the bailout scheme from the taxpayer and give them to government programs designed to push yet more risky mortgage loans.

Judicial Watch is investigating some of the corruption issues I've raised above. Certainly, both parties deserve scrutiny. And the FBI, a day late and a dollar short, is investigating, too.

Most Americans are not fools when it comes to this issue. Judicial Watch, this week, released the results of a Zogby poll sponsored on this topic. Our poll found 81.7

percent – those are real numbers – 81 percent of Americans believe political corruption plays a, quote, “major role,” unquote, in the financial crisis. And our poll also found in a related matter that nearly three-quarters of Americans think bigger government leads to more corruption. And nine in 10 Americans think corruption is a significant problem in Washington.

Americans seem to get what the problem is, but because what everyone, unquote in Washington is involved, you only hear a peep about it from the city's establishment. Arguably, the financial crisis is part of the biggest government corruption scandal in our nation’s history and it doesn’t get much bigger than Fannie Mae or Freddie Mac, which dominates the $12 trillion home loan market, especially now that the federal government is running the whole show.

The companies took care of both political parties, took more risk with the urging of their allies in Congress and taxpayers are left holding the bag.

So that’s my take on – to the limited extent, it is a take on the issue and I want to see what our panel thinks.

Joining me here today are experts I think I can fairly describe as critics of the ways of Washington. John Berlau – I’m glad to see you were able to make it, John – is director of the Competitive Enterprise Institute's Center for Entrepreneurship. John focuses on the impact of public policy on entrepreneurship. He was previously Washington correspondent for *Investors Business Daily* and a staff writer over at *Inside* magazine. And in 2002, he received the Sandy Hume Memorial Award for Excellence in Political Journalism from the National Press Club.

Sheila Krumholz is the Center for Responsive Politics executive director. Sheila became executive director back in 2006, having served eight years as their research director. She first joined the staff in 1989 as assistant editor of its very first edition of Open Secrets, the Center’s flagship publication.

And John Tamny is editor of RealClearMarkets. RealClearMarkets.com, I guess it’s better to say. And he’s a senior economist also with H.C. Wainwright Economics and a senior economic advisor to Toreador Research and Trading.

And also joining us is Alan Reynolds, who is a senior fellow at the Cato Institute and was formerly director of economic research at the Hudson Institute. He served as a research director with the National Commission on Tax Reform and Economic Growth and an advisor to the National Commission on the Cost of Higher Education, and was a member of the OMB transition team in 1981.

And of course, you can read most of our panelists' thoughts on these and other issues all over the internet. Their columns and writings appear at their respective websites and elsewhere, or in the newspaper sometimes.

And the way the panel will work is that our panelist will give us their opening thoughts for no longer than 10 minutes or so, I hope, and then we'll have a discussion with our panel and then we'll open it up to the floor for questions and comments. And if we could speak into the microphone, that would be better for our recordation purposes. And I will begin with John Tamny.

MR. JOHN TAMNY: Thanks, Tom, and thanks for everyone in attendance today, and thanks to Judicial Watch for putting this on. And to everyone in attendance, I guess I'd like to apologize that I'm not Billy Joel – (inaudible), but obviously, the problems right now in the markets and the economy are related to policy. And as Chuck (Caleck?) has always said, "Old markets don't die of old age. They die of major policy failure," and it's definitely policy failure this time around.

Now, the question is what were the major policy drivers that brought us to where we are today to the real estate boom and subsequent bust? Republicans, of course, talk up the Community Reinvestment Act passed by Jimmy Carter and also, of course, like to talk about the empowerment, the greater empowerment of Fannie Mae and Freddie Mac under Bill Clinton. And to show that they'll throw the blame around anywhere to absolve themselves, they also blame Alan Greenspan for bringing the fed funds rate target down to 1 percent for a year in 2003.

Now, the Democrats, of course, seem to blame deregulation. The Democrats – if we only had more Washington oversight over the housing and bank industries, everything would be fine today.

Now, in my opinion, both sides get it impressively wrong. The Democrats, as mentioned, blame deregulation, but if you look at the biggest freeze so far in this mortgage meltdown, it's been Fannie Mae and Freddie Mac. And if we ignore, first of all, the fact that both parties were, to varying degrees, literally horizontal in bed with these guys, the idea that they didn't have oversight of their activities is laughable. Then you add to it the Office of Federal Housing Enterprise Oversight was created to regulate these two, but despite all this regulation, they still had to be seized by the federal government at the cost of taxpayers.

Now, if you think of the banks and investment banks, it would be hard to find two industries that are more regulated than they are. The investment banking area has had the SEC breathing down its neck going back to the 1930s, not to mention opportunist politicians from Rudy Giuliani to Elliot Spitzer have regularly forwarded their political careers by going after these guys in the most devious ways possible.

And if you think of the banking industry, from the FDIC, the comptroller of the currency in the Federal Reserve, to the various state agencies that oversee banks, it's just purely laughable to assume that banks were not heavily regulated. And I'd add one thing to this. It is the regulated industries and companies that always fail.

Think about it. Look west to Silicon Valley and find me one company out there that is ever too big to fail. That's never the case because those are unregulated. Their failures were on their own. It's the regulated industries and the companies that always cause these problems that bring us to where we are today.

So the question is what was the cause of the housing boom and subsequent bust? And I think it's fairly simple. I think you could look in your pocket and find out it has to do with a weak dollar and the question is, why was this the cause?

Real estate is very commodity-like and just as commodities always do well when the dollar is weak, so does real estate, and with housing making big gains upward in nominal terms in recent years, Americans logically chased this performance and piled it in the housing sector.

But many of you are probably skeptical and a lot of people, for one, have read the *Wall Street Journal*'s account that it was Greenspan's fault for bringing the fed funds rate down to 1 percent in 2003. But according to empirical research done at the firm I work for, H.C. Wainwright Economics, there's no historical evidence backing up that claim.

If you look at nominal home prices since 1976, in periods when the fed funds rate was raised over 200 basis points, that's when housing actually did invest in nominal terms. It's when the fed funds rate was dropped by over two and half basis points, that housing did worse. And the paradox here, of course, is that historically, currencies have weakened the most when the central bank was raising rates and have actually strengthened the most when the central bank was cutting rates. But if you need anecdotal evidence supporting the dollar claim or currency claim that I'm making, we could look back to the '70s.

Nixon and Carter arguably presided over housing loans that were very similar to the ones that we experienced this decade. If you look at Nixon's presidency back in '71, as many of you know, he took us off the Gold Standard, and the result was the dollar plummeted. Over this period, the fed funds rate rose from 5.5 percent to 10 percent from 1971 to 1973. Despite the fact that interest rates rose like this, as Rice University economic historian Allen Matusow wrote at the time, "Housing emerged as the most dynamic sector in the early 1970s."

When we moved to Jimmy Carter's presidency from a low of 5 percent in 1976, the fed funds rate rose all the way to 13 percent in 1980, but despite this housing boom – (unintelligible) – the Carter administration had a very explicit weak dollar policy. And to just give you a description of the housing market back then, I think the best one comes from George Gilder, who wrote about this in *Wealth and Poverty* in 1981. Here's how he described it.

"What happened was that citizens speculated on their homes. Not only did their houses tend to rise in value about 20 percent faster than the price index, but with their small equity exposure, they could gain higher percentage returns than all but the most phenomenally lucky shareholders."

Gilder could have written this sentence three years ago and no one would blinked an eye. History repeated itself.

Now, to show how this same way contrarian rate in currency concept is not endemic to the United States, we need only go over to England in the early 1970s. The pound was in free fall in the early '70s also and during that time, the bank rate rose from 5 percent to 9 percent. But as Dave Smith wrote in the *Rise and Fall of Monetarism*, "The sector which investors chose above all others was property development."

And reflecting on the pound's crisis years later, the June 1978 Bank of England *Quarterly Bulletin* explained that there was no other general area of economic activity which seemed to offer as good a prospective rate of return to an entrepreneur as property development. And this was the case owing to the belief that property was the inflation hedge par excellence. Property always does well. People pile into it when the – (unintelligible) – the currency.

So while the existence of Fannie and Freddie and – (unintelligible) – this decade all manner of housing subsidies had certainly helped to make real estate the preferred asset class, history says the biggest driver of this boom was, in fact, an – (unintelligible) – account or a weak dollar. So why the sudden decline in home prices and all these problems, despite the weak dollar?

I think first of all, a lot of that is misinformation. The broadest measure of housing is done by – (inaudible) – price is done by the Office of Federal Housing Enterprise Oversight. And you look at their statistics and year-over-year housing hasn't really fallen very much. But what happened was, I think, families and speculators saw an opportunity to get into a mortgage much bigger than you could afford, and you find out you can't afford it down the line, it will be easy to sell the house later on. The problem is prices in all markets eventually catch up to the money illusion and the problem with inflation that drives up home prices is this also eviscerates incomes.

You guys saw it all in the price of the gasoline you bought over this decade, with the dollar weak, oil, and all sorts of commodities rose, and so people faced more onerous mortgage payments because their paychecks didn't go very far, not to mention they probably got more mortgages that were too large.

So it's interesting to me. The Republicans are in complete denial trying to throw around blame here and the Democrats, unsurprisingly, don't get that the real blame for this, I think, lies with the Bush administration for its treasury policy under three secretaries, which was all about devaluing the dollar. And now, I'll hand it over to Tom.

MR. FITTON: Thank you. Alan Reynolds.

MR. ALAN REYNOLDS: Oh. (Laughter.) There's a real panic going on here in D.C., the District of Corruption. (Laughter.) And there's a lot of flailing about by the Treasury, the fed, and now Congress willing to commit money they don't have to fixing something they haven't defined very well. And everybody assumes it's housing and housing caused banks to collapse and the banks aren't lending. And therefore, that's why Europe is in a recession. I don't know – (laughter) – I missed something about it.

Anyway, we were told that the problem is we have too much debt and not enough credit. I think that's what they're saying. We're told that in something – the financial markets are freezing up or melting down. (Laughter.) And because of this, the Treasury – in his wisdom, the Treasury Secretary began intervening in what we call bailouts and being a stockholder, I tend to call them wipeouts. He told the stockholders of Bear Stearns, "You are compelled, I decree, to sell your shares at $2 a share to another bank. Now, I pick the bank." Nice deal for that bank. I'd have been willing to pay $2.50 share, but nobody asked me. I had to leverage up a little for that one.

AIG got in trouble and said, we need a $85 billion loan. They said, "Sure, we'll give it to you; we'll only charge you about 14 percent. By the way, even though you're a trillion dollar company, the government's going to take over 80 percent of your equity."

This sort of thing began to scare stockholders a little bit and even Fannie and Freddie, who I'm not about to say anything nice about, but Fannie Mae stock had sort of been recovering up $4, $5, $6, $7 a share. And then one Sunday – weekends became very scary – they decided to nationalize it, take it over 100 percent. Stockholders were literally wiped out and when asked why, they said, "Well, Freddie Mac was cooking the books and they said, well, Fannie Mae wasn't cooking the books."

And it got down to capital requirements. You didn't have enough capital requirements. Guess what their capital requirements are now? Zero. That's why they're back in the business again, lending out lots of money that they don't have, so the taxpayer is bearing that risk. The fed began lending money to all sorts of institutions on any kind of collateral, which is kind of a spooky sort of thing, and when asked about that, everybody – you'll go on CNBC, they'll say, "We have to get banks lending again. How can we get banks lending again?"

So I looked at the fed data and I said, "Gee, they seem to be going up;" the commercial industrial homes, $3.6 trillion in July, $3.64 in August, $3.66 in September. That didn't seem to be falling particularly dramatically. Consumer loans, 8.39 in July, 8.45 in August, 851.9 in September and nobody talks about bank lending. There is a problem in the credit markets, but it's not in banks. Banks have this – big banks are in trouble; so the small banks are picking it up.

So rather than look at these numbers, we began to hear – I ran into Bill Crystal at Fox TV and he said, "Aren't you worried about the TED spread?" And I said, "Oh, yeah, the TED spread." That very actively predicted the recession of 1988 and the recession of 1995. Unfortunately, we didn't have recessions in '88 and '95.

The reason is that this is a spread between T-bills and euro dollars. And all of those things – these spreads are telling you is that everybody was rushing into Treasury bills for security. They're not telling you anything you don't already know and people got worried about LIBOR, interbank lending rate. U.S. banks don't have to get into LIBOR. They go to the fed. The fed will lend them money on anything and don't charge as much. Anyway, interbank lending getting dry. It's all a made-up story and it's all just designed to whip up some sort of frenzy so they can spend another 100 billion and another 100 billion.

And you were asking me what the total cost was. People forget this. You really have to start with the first stimulus plan. I don't – I forget the cost of that, but it wasn't peanuts. Bob Schiller, who's the famous housing bear, calls out a bailout and it is an indiscriminate bailout. You're going to give money – (unintelligible) – to people who didn't pay taxes so that they will take their few hundred bucks and go out and buy a new car or a new house.

Well, they don't. They go to Wal-Mart, pick up a few things and at best, that stimulates spending in one period of the expense – (unintelligible) – another dum-dum stuff. And we're going to do it again, of course. Who cares? It's borrowed money and that stimulates something. That stimulates traders in Treasury bonds. They're busy and the Treasury bond yield went up.

There was an October 15th *Washington Post* piece. It was a pretty good piece on what went wrong, but it said in the midst of the biggest economic crisis since the Great Depression. This is where maturity comes in. We need to be a senior fellow. I happen to have lived through '73, '75. I was writing then and I lived through '80 to '82 and I'm telling you, those are crises. You've got a 16 percent mortgage rate? That's unpleasant. You've got an unemployment rate of 10.8? That's something to worry about.

We now – there is a finance problem. The unemployment rate in finance in United States has gone from 3 percent at the beginning of the year to 4 percent. (Laughter.) Okay. It's a problem for Wall Street, but sympathy for bankers can only go so far. I used to be one. (Laughter.)

Now, it might be the biggest financial crisis so far, but the other two – we need to remember – one was the S&L crisis, which stretched from the '86 to early '90s, '95, lost a couple of thousand banks. We've lost about 13 or 14 this year, some big ones, a couple of thousand S&Ls and other kinds of banks. And the growth rate throughout that crisis – the economic growth rate was 2.9 percent. That includes some mild recession, which had nothing to do with the S&L crisis; it had to do with the price of oil spiking, as it usually does.

The second big crisis was October 1987, when stocks fell in one day almost as much as they have this year, all kinds of gloom and doom predictions being made at the time. I took out a home equity loan and called my broker and said, "Should I buy stocks or bonds?" I said, "Yes." (Laughter.)

Financial crises aren't necessarily economic crises. Are we in recession? Probably. We know the rest of the world is. The real GDP fell 1.3 percent in France in the second quarter, 2 percent in Germany, 3 percent in Japan, 5.5 in Hong Kong, 6 percent in Singapore.

Now they'd all like to blame that on U.S. housing. That's – for me, that's a bit of a stretch and they don't all own U.S. paper either. That's a stretch too. The one thing we do have in common, like every other recession, is there was big spike in oil prices. That's not the sole cause, but it happens there have been nine previous – ten now – nine spikes in oil prices. I covered this in the *Financial Times* January 3 – I highly recommend it, Cato.org – and so there just happened to have been nine times when the oil prices like tripled or more, and every single time within a year, the economy is in recession. And the world was – (unintelligible) – recession.

Well, that's kind of good news because what you really want is for somebody else to go into recession. The oil price goes down, but if we all go in recession, one way or another, the demand for oils falls and that helps you get out from under things.

Recessions happen. If energy prices get too high; they need to come down. If home prices get too high, they need to come down. If homebuilders build too many houses, they have to stop building for a while until they get the inventory down. And recessions do affect finance. It's not just the other way around.

I heard Sarah Palin, in the vice presidential debate, said – she meant to say, I think, "Wall Street is starting to affect Main Street." But she said, "Main Street is starting to affect Wall Street." That's absolutely right. It goes both ways.

There was no boom bust in housing in Detroit. There was just a bust, then another bust, and another bust. There was – the problem that they're having in the suburban Silicon Valley with housing is because Silicon Valley's not doing very well. So it is – it's a mutual downturn. Recessions happen.

If the governments really knew how to stop, prevent, alleviate recessions, why do we keep having recessions? Fiscal stimulus – from 1992 to 1999, Japan lost 10 huge fiscal stimulus plans. The government – the ratio of government debt to GDP went from 60 percent to 105 percent of GDP. It didn't do a darn thing except to put taxpayers deeply in debt, for which they are still paying interest – a big mistake.

I think I want to close with the immortal words of George Bernard Shaw who said, "Any government that robs Peter to pay Paul can count on the support of Paul." (Laughter.) The trouble is when you rob Peter to pay Paul, you end up with a nation of pallbearers. (Laughter.)

MR. FITTON: Sheila, the Center for Responsive Politics.

MS. SHEILA KRUMHOLZ: Thanks, Tom and thanks to Judicial Watch for bringing me here. I want to frame the issues in terms of money, political money, and take a close look at key votes and look at the context and concerns about this money.

The Center for Responsive Politics is a non-partisan research group that tracks campaign finance money in politics and that's the lens sort of which I'm looking at this today.

So a little bit of background. The financial sector, finance insurance of real estate, is the biggest campaign contributor, bar none. This includes some of the biggest givers in politics, commercial banks and S&Ls, credit unions, securities investment, venture capital hedge funds and private equity insurance, real estate, mortgage bankers and brokers and accountants.

The numbers – $2 billion dollars given since 1989. I know these figures don't mean as much now – (laughter) – now with those bailouts, but $2 billion for the last 20 years, $373 million this cycle so far, $190 million of that going to Congress. Obama is the top recipient with $28 million and McCain follows with $25 million. Of that amount of the money so far this cycle, $123 million comes from Wall Street, securities and investments, of which Obama again tops with $11 million, McCain with $8 million.

Mostly finance hedges that are bets. They give – the finance sector has given 50 percent to Democrats, 49 percent to Republicans so far this cycle, and it's a 44-55 split back in time.

Securities and investment favoring Democrats this cycle, but 50-50 right down the line back in time. So this is, I think, typical of corporate donors hedging their bets, giving to the party in power, and over time, that balances out.

Lobbying is the other side of the coin, of course. Finance spent $415 million in last year, $86 million for securities. This year, already we're on par to surpass that with $231 million so far through June. And that's the second – finance is the second highest sector following health care. Health care actually spends more on lobbying generally; $3.2 billion for the past decade. So $3.2 billion on lobbying alone for 10 years, $2.2 billion for campaign contributions back 20 years. So in finance, as is often the case, far more is spent on lobbying than on political contributions.

Top contributors by organization – about half of them are from finance. The top corporate donor is Goldman Sachs – we all know it – with $5 million already this cycle, 73 percent to the Democrats, leaning heavily Democratic. And in fact, all top financial givers favored Democrats this cycle, with the exception of Merrill Lynch and the Bankers Association.

Taking a look at the presidential race, the financial sector is heavily tied to both main presidential candidates. It's the top sector for both, of course. The industries within the sector are among top donors. Five of Obama's top 10 industries are financial, Wall Street. McCain is more reliant. All of his top donors are financial and seven of his top 10.

Merrill Lynch is number one for McCain very heavily, leans heavily Republican and Goldman Sachs is number two for Obama. That's a switch after the University of California had surged education. It has been surging for Democratic candidates over the last couple of cycles – so professors with money they don't know what to do with.

And their advisors, of course, have worked for these companies. McCain's campaign manager was essentially a lobbyist for Freddie Mac. Former Fannie Mae executive, Jim Johnson, led Obama's Veep search until he was forced to resign.

The big presidential bundlers work for these kind of pathetic campaigns – work for these companies, sorry. McCain's Wall Street – McCain's top source for bundlers – 70 bundlers already in the cycle raising $11 million – real estate is number two.

And Obama refuses to disclose his bundlers' employer occupations, unlike McCain, but securities and investment appears to be his second source in bundlers after lawyers. Fifty-six of his bundlers have raised $8 million at least. Overall, finance, the fire sector, finance insurance and real estate bundlers have hauled in the most for both candidates, $30 million for McCain, $13 million for Obama.

The names in the news recently, AIG, Lehman – I always said Lehman – thank you – AIG, Lehman, Fannie Mae, Freddie Mac, Merrill Lynch, all these are big contributors consistently over time. Merrill Lynch is one of our heavy bidders, one of the top 100 organizations, giving back to '89, when we started (counting?) donors, giving $14 million back to '89, AIG $9 million. Lehman Brothers is the 13th top donor already this cycle and Fannie Mae – Freddie Mac giving $9.7 and Fannie Mae giving $8.2 million back in time – again, hedging their bets primarily. Freddie Mac has given 57 percent to Republicans. Fannie Mae has given 54 percent to Democrats.

Current members of Congress have received more than $4.8 million from Fannie and Freddie, the Democrats receiving the majority of that, 57 percent. And lawmakers themselves are invested in these companies. They've invested up to $1.7 million of their own money in these two companies.

So where does the political money come from? It comes from individuals. The companies cannot themselves give directly anymore. Now the soft money is banned. It's given by employees, mostly executives. These are the individuals that we can examine, that are itemized. And they're giving either directly to the candidates or they're giving through their political action committees for the company.

And for presidential candidates, employees of these companies are giving virtually all the money. Packs are not a factor with presidential campaigns. And what does it buy? Well, it buys access to decision-makers and open doors. Everybody knows that, but it may influence a politician's thinking and here's an example why.

For instance, we know that in some cases, industry lobbyists will make pledges of support, but withhold their checks until the end of the session, the presumption being that they'll reward good behavior and punish bad. And in the case of the bailout, the money seems to have helped keep Congress' hand off these industries, although we can, I guess, debate the point. And when a lot is at stake, the millions spent on contributions and lobbying can be a small cost of doing business.

I can't tell you how many times we get requests from academics to get a massive dump of all 25 million of our data points, so that they can see whether or not this is a wise investment on the part of corporations because I think that the sense is that it often is not. But it is a small cost relative to the profits that can be gained if they play the game wisely.

And the money is especially influential, obviously, when they issues are arcane, where like credit swaps and derivatives are not commonly understood across America. And so that is where – when the public is not paying close attention, that is where, I think, the industries and corporations that have access stand to benefit the most.

For specifically for the recent key votes, when Congress passed Gramm-Leach-Bliley in 1999, the legislation that repealed Depression-era regulations, there was a coalition member who supported – that measure received more than twice as much money from those interests as the lawmakers who opposed the measure and the difference was especially large on the Democratic side. Similarly – and we didn't look at the Commodity Futures Modernization Act because that was an omnibus spending bill and there was no way to really isolate that piece of it.

In the recent Emergency Economic Stabilization Act of 2008, again, money from the sector was soundly on the side of the bill supporters. In the original House bailout vote, those who voted for the bill received 51 percent more from finance than those who voted against the bill and there was an especially high correlation, again for Democrats. In the final House bailout bill, those who voted for the bill received 41 percent more over their congressional careers than those who – (inaudible).

And in the Senate vote, the campaign contributions from the finance sector were especially high, 139 percent more than those who voted against it, but that includes the candidates who are running for the presidential bid this year. So there, finance contributed twice as much money to senators who supported the bailout than those who opposed it.

The lobbying effort on the bailout has been brief, but intense. To make up for time they do not have, interest groups have undoubtedly capitalized on relationships they built over many years. And in Congress, campaign contributions are an especially useful tool for building relationships.

MR. FITTON: Well, thank you. Okay. John Berlau, last, but not least.

MR. JOHN BERLAU: I hope not least. Tom, thank you so much for having me here and it's a pleasure to be on this panel and I enjoyed hearing from John and Alan and Sheila. And let me first get some shameless self-promotion out of the way. If you want more information on these causes, critiques of the bailouts and causes of the crises, you could go to CEI.org, our main website, OpenMarket.org, our blog site, and also a new site we have, co-hosting with the National Taxpayers Union, BeyondBailouts.org.

And I think we should – Alan's right, we should have failures. Failure is a part of capitalism. Small businesses fail all the time. If you take risks and your responsibility – if the risk doesn't pay off, and big businesses should be subject to the same rules there. I think the bailout/nationalization, where they decide, as Alan pointed out, that shareholders will get $2, or in the case of AIG, nothing, but then all of the big derivative traders, the sophisticated derivative traders, will get their credit fully bailed out, has just created confusion, made the crisis worse, and has scared off investors as much as what the credit markets do for what the – will the government nationalize this company?

And so I said, failures are a part of capitalism. The economist, Joseph Schumpeter, talked about that, and calling it creative destruction, but a systemic failure, as in this one, I think, as John said, the confluence of bad policies.

I'm going – and I think among those were, in addition to monetary policy, the weak dollar, as John mentioned – having Fannie Mae and Freddie Mac and the hybrid public-private structure, plus the government's decision to tilt the finances from – (unintelligible) – housing that homeownership, above all else, was the highest goal, rather than something – creating more gap, rather than something – building more savings and investment among the poor and middle class, but you had a home even if you were – it didn't happen – and even if you were owing out the wazoo on the mortgage and you were still part of the ownership society – been sort of a narrow definition of the ownership society.

Fannie and Freddie were sort of the worst of both worlds. They could, as Sheila said, lobby like the private sector could do, but they also were created by Congress and had this built-in government support, where they had a $2 billion line of credit for the past – since they were created, a $2 billion line of credit with the Treasury Department that made investors think, and it turned out were practically, that if anything happened, they would be bailed out by the government.

And there is an article out there by my boss, Fred Smith, the head of the Competitive Enterprise Institute, where he testified in 2000 before Congress and was pooh-poohed when he said, "This $2 billion could turn into $200 billion tomorrow if anything goes wrong," and they said no.

But the Fannie Mae added systemic – (unintelligible) – group, members of Congress on that. Fannie Mae added systemic risk. It was – they talk about investment companies with a leverage ratio of 30 to one, whereas Fannie and Freddie were more like a – the leverage was more like $50 for every $1.

So also the fact – they had a regulator, but they were never limited by Congress, which they were created by their charter, as far as they kept being bigger and bigger into how much loans they could buy, where they were actually competing with banks and buying $5 trillion worth – having 5 to 7 trillion worth of mortgages and was backed by the – implied – (inaudible) – by the government, now explicit. Investors weren't as concerned about the risk, and you could see that Fannie Mae even if it – it argued it was taking prudent (correction?) for its own risk, just having it there, a government-backed entity buying trillions of dollars of mortgages adds extra liquidity to the system for some of the bad mortgages.

And they were some of the biggest arbiters among some of the failed mortgage lenders like Countrywide, but also had more than 50 percent of the loan of – (inaudible) – Star Financial, places like that. And then you also had the Community Reinvestment Act where they actually said to disregard – you actually had the Federal Reserve Bank of Boston and others actually saying disregard additional underwriting loans to fill loans of underserved communities. Again, the goal is housing, rather than building assets and savings.

And the Federal Housing Administration under Bill Clinton, HUD Secretary Andrew Cuomo was able – created programs to get around the down payment requirement where home sellers would set up foundations and then give that to – the down payment to the homeowner, and then bill the taxpayers for everything.

And then Bush Secretary, Alphonso Jackson, who resigned earlier this year under a cloud of ethics questions, said, we have to – we're losing our market share to the private sector, and that's never something – so they competed head-on with the subprime loans, and for a while, their delinquency rates were actually higher there.

But I think also the fascinating thing is it's the support for housing policy, and also in some ways, we were after the S&L crisis and Enron, sort of fighting the last war. There is a rule called the mark-to-market accounting rule which I – I have an article from *Wall Street Journal* that's out there now, where even healthy banks are disproportionately affected by bad bank sales, because sometimes, banks will sell their loans and sometimes, more traditional community banks will hold those to maturity.

And sometimes, banks will decide if the market's bad, well, we won't sell the loans, but now, even if you have no plan to sell the loans, even if the loans haven't gone delinquent, you still have to write that down as a loss on your books even if you're still being paid by the loans and being held to maturity.

Now, everyone from Newt Gingrich to liberal members of Congress like Peter DeFazio or Oregon and Democrat – and Macy Kaptur of Ohio have criticized these rules, and the SEC says they'll do something about it, but they just came out and papered it over and said, yes, there are some instances where you don't have to do mark-to-market accounting, but this is no safe harbor.

So this is sort of – mark-to-market accounting is one of the reasons why you still – the delinquency rate is about 7 percent with all these bad policies by both Washington and Wall Street. Yet, every healthy bank is affected by a bad bank's laws and makes it more systemic. And I would be happy to take more questions about these policies.

MR. FITTON: John, thank you very much, and I thank all of our panelists here. Let's talk about what the reaction ought to be. Is it a big deal what the government's been doing, either going on the line for over $1 trillion in additional liability, the potential profit, I guess, on the upside, given – what should be the reaction, with the propriety of what they've done, the government has done? And I guess – Henry Paulson was saying, well, I agree with Tom Fitton. We shouldn't do this, but we have to do this because it will work. It's a pretty broad question, and I think we'll start with Alan on that, and go to John, then John.

MR. REYNOLDS: I think the reaction ought to be moral outrage and not so much the money issue, but the notion that the government can virtually expropriate private property so capriciously. And Congress and the House were stampeded into the $700 billion investment, if you will – a blank check, if you won't – because the S&P 500 had fallen to 1,100. A lot of us would love to see it rise to 1,100, thank you very much. It's closer to 900 right now. And if you're going to spend $700 billion to have an effect on the daily stock price, well, I guess you could do that, but it didn't work in the direction they expected it to.

My point was that what they did before that bill, what Treasury did before that bill, clearly made people like me – and I am an investor, and I am still net long – (unintelligible) – shorts, but I couldn't. The SEC, in its wisdom, banned that for a while. It said to me, when they wiped out the shareholders and so many companies in surprised fashion like that, that said to me, I don't want to hold financial stocks unless, of course, I can short others.

So when they stopped the shorting, that made it really bad. It also made it very easy to short financial stocks. There's an exchange rated fund called SKF and that continued to trade just fine while the formal shorting wasn't allowed and it was basically just a money machine, ultra-short.

MR. FITTON: Can you explain what shorting is?

MR. REYNOLDS: Oh, you basically – you're betting stock goes down. That's all you need to know. You can bet the stock goes down. And a common hedge fund strategy, and one I employ personally, is that I might short what seems to me the weakest – it's called (peering?) – the weakest of two stocks.

Now, you would never – suppose the two stocks were Goldman Sachs and Morgan Stanley. You would never short Goldman Sachs because the Treasury – either Goldman Sachs is a branch of the Treasury, or the Treasury a branch of Goldman Sachs. I'm not sure which it is, but you know too, the last guy standing was going to be Goldman Sachs. This was a no-brainer but what he was willing to do to old enemies like Bear Stearns, that's another matter entirely – just nasty stuff.

MR. FITTON (?): Do you think he had a conflict of interest?

MR. REYNOLDS: Did I suggest that?

MR. FITTON (?): I mean, there's a conflict of interest in theory. I don't know if there's one in actuality either, that if you are required by law to recuse yourself from the decision, do you think it's going to that level?

MR. REYNOLDS: The last time I saw – the *New York Times* had a piece on how much stock these various ex-CEOs had in their own company, and JP Morgan were doing okay and almost everybody else was wiped out. He had $500,000 million in Goldman Sachs stock. That certainly focuses the mind, I would think, and that was after it had gone down.

MR. FITTON (?): Paulson still has stock at Goldman Sachs?

MR. REYNOLDS: Yes, you can't touch it. That's one of the reasons they go to work for the government. When he put it in the blind trust, there's no capital gains tax payment. So one of the reasons Goldman goes in and out is you don't have to pay capital gains while it's in the trust. Well, I can tell you it is a District of Corruption. (Laughter.)

MR. FITTON: John.

MR. BERLAU: Well, this is interesting. I didn't know until – I had thought – I think that's the phrase about the former CEOs and business executives and in fact, that's what I wanted to say the (Hume?) award for here was Charles (Rizzoti?), a Clinton appointee and Bush holdover who was retaining his stock in the computer company, and then the IRS would have him working at that computer company.

But I didn't know it until Alan brought it up that Paulson still had substantial – (unintelligible) – of stocks. I thought it – I guess some – (unintelligible) – and that sort of thing really needs to be looked at, and I do think it's interesting that they let Lehman fail, which they should have done, but that's eliminating a competitor. And also, they bail out AIG, which I think – Goldman, I think – (unintelligible) – mortgage in the *New York Times* article that Alan mentioned said that Goldman was the biggest counterparty.

But overall, I don’t see why nationalization here would do partial or full – partial nationalization or full nationalization would do any more to bring about economic stability than nationalization does in countries such as Cuba and Venezuela. And I’m wondering if we would be seeing a different role if they had just let Bear fail, let the creditors work it out. And they let Enron fail and it didn’t bring – early in the Bush administration, and it didn’t bring the economy crashing down. And I think Enron was twice or three times as big and had created derivatives just like Bear does.

So maybe if they said, we’re going to let it fail, the creditors would have been more forgiving, or even in a bankruptcy. Shareholders were still pretty wiped out, so I don’t see, in many of these cases, how bankruptcy, dividing the assets among the creditors in a bankruptcy court could have been much worse. So I mean, yes, I think it has just added more fuel to the fire.

MR. REYNOLDS (?): So let’s get shareholder approval.

MR. FITTON: Yes, exactly. John probably – what do you think the – (off mike) – what do you think the government – what is the government doing? First, the goal is to buy mortgage-backed securities. Then the goal is to inject money into the banks. Now the goal is to – or yesterday, the goal was to shore up the money markets. This morning, on the way to work, I heard the goal was to give banks incentive to rework loans to $250 billion. Am I misperceiving the government’s erratic nature or is it working at all?

MR. TAMNY: The government, by definition, doesn’t have a clue. The idea that they have – and it's irrespective of party – a hotline to the future somehow know have fixed problems in advance or afterwards is just laughable and the senators are all wrong. I think it’s Richard Brookhiser who used to say, deep down, the Republicans know they’re wrong, and the point there was that Republican voters believed in the policies, but people they elect do not believe in them.

For many, it was just platitudes, and I think we’re seeing it right here. How is it that you’ve lost so much confidence in basic economics? How is it that the ’80s were spent denationalizing industries? How was it that England – that was the big story, the Thatcher area, is they got out of business. That was the idea of the Reagan revolution – let the individual thrive. How is it we’ve all these confidence to do this?

And what kills me even more than Washington is even if you thought – I mean, they keep saying, well, trust in us to fix this; trust in us to use the money in such a way that will make things better. The markets are already telling you that they don’t believe it. They’re down to 40 percent and I thought it was amazing that Bernanke said last week, we’ve been working on this for over a year.

Well, as near as I can tell, the S&Ps are down about 45 percent during that year. So the markets don’t believe it, but you still have people in Wall Street who are saying, well, we’ve just got to do this to fix things. We just need it this time. The way you should be thinking is what an awful thing to suddenly have the government inserting private money that does not want to be in this marketplace to begin with, taking it from the private sector, round tripping it from Washington and then reinserting it, that somehow that would work. And by definition, it can't work and it frustrates me that both sides can't trust their instincts on this at all, but they don't have a clue.

MR. FITTON: We're talking about the money and their return on investment. My guess is the financial sector, as you defined it, is looking at their investment and thinking, my gosh, we're going to have to spend more money. If there's $700 billion, $1.5 trillion at stake, we're not going investing more money in the government. We're not investing enough money influencing policy.

Do you think – what's your perception as to how – is there going to be a fire sale in terms of the chairmen of these committees and the minority leaders of these committees coming out and telling this industry and – (inaudible) – we're making the world anew, and if you want a seat at the table – are folks prepared to spend more money now or are they kind of nervous?

MS. KRUMHOLZ: I think they are. The presidential election aside, there's always two steps forward and one step back between the presidential and midterm election, but from everything I can tell, I expect that they are going to continue doubling down, spending more money on campaign contributions and even more money on lobbying, because they see that they're in Congress' sights and this is the only way they know to battle it.

So there's probably going to be some contracting of campaign contributions, because this is coming from the individual partners and vice presidents on Wall Street, whereas, I think, again, the lobbying is going to be as much, or more, in the next year in particular.

MR. FITTON: John Tamny, I guess you – a (class test?) of what you think should be done, but what do you think should have been done in response to the crisis or non-crisis or market conditions in the last few months by the government? What should have they been doing, if anything?

MR. TAMNY: If I were a dictator, which I'm not, but if you could do it without encumbrances, I think there are some fairly basic things to do. If we had a problem with investment, as the people did not – were not interested in these toxic assets, the idea there, I think as you say, engage in a little industrial policy, maybe long-term policy and say, we're going to treat these investors with zero percent capital gains, so you could actually drive private capital and – (inaudible).

Secondly, I think probably a lot of you remember that Wal-Mart was very interested in getting into the banking industry several years ago. Sheila Bair, the wonderful FDIC chairman, made that very difficult for them to do. There are a lot of businesses out there that are cash-rich, that want to be in banking. So get rid of antitrust laws and get rid of the bank holding laws and yes, regulations, so that these cash-rich businesses can get in there.

And the third thing of course, is I'll go to my grave saying, you don't have these massive periods of mal-investment like this unless there are currency problems. I think if we had a dollar defined in terms of something real, it was very stable, I think it would be pure fantasy to say we'd be where we are today. So this is the third thing I would do is have Treasury define the dollar.

MR. FITTON: Alan, when you're invited to the White House on November 15th to consult with President Bush and the world's leaders on how to remake the new world economic order, what would you say they should have done and what should they do?

MR. REYNOLDS: The last time I was invited to the White House – and I am; I am. I came late and I explained to them that I was held up because the security guards have discovered I'm one-fourth French. (Laughter.) The best I could do on short notice.

Now, and I have been e-mailing an advisor to one of the presidential candidates, Barack Obama's adviser, one of them, and he not listening to me. So that doesn't look too good, so I wrote a long paper, which is on Hillsdale College's website on what kind of problems they have.

Look, the crazy thing is we're in recession. We'll probably be in a recession for a while. It's hard to call because of the second quarter pop in GDP which makes it for the national bureau – usually, you don't have to have two quarters. That's a made-up thing, but to have GDP up and when other indicators are down, it would make it hard to time it.

We're probably in a recession, probably halfway through a recession. When the next president comes in, he's going to be facing a budget deficit certainly north of $1 trillion. That focuses your attention and they have pretty grandiose spending plans. I think Obama's short of financing his by several trillion over a 10-year period, which is what the paper's about. They're going to have their hands full, but sooner or later, if they just would leave us alone, we'll get out of this just fine. Markets correct very nicely.

The fact that the investment banks became commercial banks was clever, and by the way, was made allowed by the 1999 deregulation because the 1933 barrier between those two left the investment banks as a separate entity, meaning they couldn't take deposits, and therefore, they weren't part of the FDIC. Therefore, they weren't regulated and all that kind of stuff.

And the 1999 bill was intended to make commercial banks into investment banking but also to let investment banks into commercial banking. That ends up what was done. That was actually – (inaudible). Now, they're regulated like crazy, but their leverage will be less.

The Basel capital requirements said to these banks, what you really want – you have to have high capital requirements against risky assets, but you don't have to have high capital requirements against, say, mortgage-backed securities. Oh, I mean, regulation has been very ineffective, dangerous even, and the mark-to-market is an example of regulation being very dangerous.

And the deregulation of 1999 was a good thing that allowed us to survive. These institutions would have gone belly-up. The thing that really terrorizes me is that we will get a president in there who's a bad person doing bad things and the economy will recover anyway and he will get credit for it.

MR. BERLAU: Some of the problems won't be there, but as a government agency, just tilting the economy toward housing and inflating housing and creating these bubbles, I think it's still (better?) and now, you've got press reports that's under Paulson, that Goldman Sachs under Secretary Paulson, Fannie and Freddie are buying some of these things that the bailout was originally created to; whereas the bailout is now directly investing or nationalizing banks because there seems to be – there's less scrutiny if Fannie and Freddie actually buy some of the troubled assets. So some lessons have been learned, but I don't think enough.

MR. FITTON: I mean, what's disturbing to me is the extraordinary lack of accountability in the processes we've been observing, and we can talk about socialism, but let's have regular procedures. And there's no regularity in what the government is doing here and there's virtual – no transparency as to what the government is doing in terms of the decision.

And we've asked for documents about this meeting that Paulson had with the bankers where he forced them into taking this money. I'm sure he didn't have to twist their arms too hard, but an extraordinary meeting that took place that, as John will point out, if Hugo Chavez was running the meeting, we'd all be screaming about it. And yet, Henry Paulson does it, and everyone, everyone yawns; everyone yawns.

Well, I want to open up the floor up to questions and comments and invite our audience to participate. And I think we have a microphone that you could use. And raise your hand and I'll point to you and wait for the microphone and we have a question right up front here, second row.

Q: Well, I couldn't agree with Alan more.

MR. FITTON: Wait for the microphone, please. Thank you.

Q: The absence of moral outrage is shocking, and why there was no sort of immediate legal action taken by stockholders or the banks, it seems to me that they could have gotten some sort of intervention by a federal judge to stop the federal takeover of the banks. Could they not have?

MR. FITTON: (Unintelligible) – that allows – does the law allow the government to do whatever it wants in this area? Is it – (unintelligible) – the problem is they can't do it?

MR. REYNOLDS: I'm not a lawyer, I'm proud to say, with all due respect, but my first thought was this is constitutional? And we have some people at Cato, Bob Levy being one of them, who seriously doubts that. Bob Levy, by the way, is the genius behind the fight against gun control in D.C.

If it's legal, then we need to change the law so it is isn't legal anymore. You can't have this kind of capricious intervention without shareholder approval or anything like that. Why did they take the money, the nine banks in the last tranche? Well, it was a 5 percent interest rate. That's below market. Other banks have gone in there and done their own thing with Warren Buffet and others were paying 10.

So, yes, this looked like a good deal to them, but they talk about this as adding capital, but insofar as it scares common shareholders like me, six of one and half a dozen of another, what I'm saying about those interventions prior to the $700 billion announcement, which I have some opinions on, a national view, was they were causing – they were at least aggravating problems and maybe causing them, because if you take over this bank, I short the stock, I sell the stock, or I short the stock, the stock goes down. The incomes of Moody's and S&P – and they downgraded the bank now because it has too much debt relative to equity. It hasn't added any debt, so equity's down.

So now, they have a bad credit rating and their capital requirement is up, because even though the capital requirement said it's good to hold these mortgage papers, now they say you have to mark them to market. And so they're in this accounting squeeze and regulatory squeeze and the real squeeze was regulation. We can prove that very obviously because as soon as you deregulated Fannie and Freddie by making them part of the U.S. government, they're back doing what they were doing before, buying up mortgages.

And I do want to make the point that this is not just a subprime issue. It never was. It is an issue of having a $300,000 mortgage on a house that drops at $200,000, and people who say we ought to fix that are saying, what are they saying? Taxpayers should come up with $100,000? So you can't fix that. And if I pay too much for anything, that's the way it goes. And prices got too high on these homes in San Diego, and in Vegas condos, and some of these other things.

And when that happens, they've got to come down, and I hear economists having proposals of how to shore up the housing prices. I don't get it. The housing affordability index, after looking bad, it's starting to look good again. Young people can actually buy houses. House sales are up in California, at a low price, but they're up. The market could solve these problems. Government is just making it worse.

MR. BERLAU: I think that was a very good question and in return for the money the banks – they had to issue a new class of preferred stock which dilutes common shareholders and puts further restrictions on issuing more stock and also increasing dividends. What I was wondering is, yes, doesn't it need shareholder approval, putting aside whether the government does is constitutional, wouldn't that need shareholder approval under some of the stock exchange rules or state law?

Also isn't it – even if it's so-called blank check or preferred stock, doesn't the board of directors at the very least need to approve that, that the CEOs can't sign a piece of paper in a day meeting without going to their boards? And maybe there was some rubber-stamp process by the boards afterwards. Anyone who has information, I'd love to hear it, but yes, that's the thing. Under basic state corporate law, it doesn't seem like you could do that. I hope there are laws for that.

MR. FITTON: John Tamny, do you have any insight on the power of a board or the shareholders to approve or disapprove of the actions of their CEOs?

MR. TAMNY: I think as owners, they would have – (unintelligible). I guess the other thing I would add to this – probably two things. I think the law that needs to be made here is that Congress has to have a three-month cooling off period before they pass any laws. That's the first problem. But secondly, I think people forget also the '70s were about booming home prices. It was an impoverishing idea. The last thing you want is the government putting people into houses because capital moves fast in the world we live in, and if you're stuck in Michigan in a house, you're not able to move to Dallas to chase new opportunity.

So why the government would ever be in housing has got to be the most foolish idea. And for Republicans to embrace it, it goes against the Adam Smith, the John Stewart – (unintelligible) – supply side concept they claim to embrace. What they always said is when you buy a house, you put money into the ground. When you buy a mutual fund, you provide capital to entrepreneurs and new business. Why the Republicans want to the save the housing industry is the most economically backward and contradictory concept I can ever think of.

MR. FITTON: Yes.

Q: I have a somewhat different question. For years, we've been running a foreign trade deficit account. This year, we owe over $500,000 billion. Is this something to concern us? We have not been concerned in the past.

MR. FITTON: Alan?

MR. REYNOLDS: The hard-landing scenario, that this is going to knock us down any day now – we have a current account deficit chronic whenever the economy is doing well, and it goes away, by the way, in recession. So look at the bright side. It probably will go away. There's a hard landing coming. The government is – look what happened if foreigners stopped buying our debt because if you have a current account, if you have a deficit in a current account, you have a surplus in capital account, meaning foreigners want to buy your assets. Well, they obviously do because now, it has been going up, so that's an interesting angle on that.

The hard-landing scenario is brought back over and over again. The closest we ever came to actually seeing it might have been at the stock market crash of '87, but it didn't have any real effects. What happens if a foreign official purchases – central bank purchases of U.S. assets dry up? That's actually happened several times. Nothing happened. Private investors walked up and picked up whatever the central bank was selling, so it's kind of hypothetical.

I think that there's a case to be made for saying that the country, in many respects, and the government in particular are living beyond their means, but the current account deficit doesn't really tell you that. And the countries we most used to emulate for running chronic surpluses, Japan and Germany, haven't really done all that well with their surpluses and they certainly haven't created jobs as a result of them.

MR. FITTON: Yes. My take on this is that the concern about it – I appreciate your pointing out that we shouldn't be as concerned about the foreign ownership, but my concern is that there are people who are overly concerned about it in our government. And I remember some Wall Street Journal reporting in terms of the AIG takeover where the Treasury was calling up seemingly its foreign sovereign wealth funds, and it seemed to me like there was a foreign policy component. They were worried that these sovereign wealth funds would be hurt and there was a sensitivity to that, or that's how I read it, which I think is somewhat scandalous that this was a foreign policy movement that we were going to take care of the Chinese by taking care of AIG. And critics of the *Wall Street Journal* reporting that, but I haven't seen anyone follow up on that yet.

John, am I being too conspiratorial in suggesting that our government was more concerned about being in the good graces of Dubai's sovereign wealth fund and the Chinese assets than the stewards of taxpayer money?

MR. TAMNY: As a big investor as the U.S. government, they probably want to fit in with some of the sovereign wealth is all I can think, wanting to be part of the gang, but generally, I would just say about trade more broadly is there's no such thing as a trade deficit. It all has to balance. I run trade deficits with my bartender and my landlord, but I run a surplus with my employers.

And we've got a great deal with China, whereby they make things not in their economic interest to make, and that gives us time to create the Googles and Intels and Microsofts for the world. I can't think of a more economically harmonious relationship than that. So I hope they continue just to sign the capitals coming their way.

Q: May I respond just slightly?

MR. FITTON: Sure, go ahead.

Q: I don't want to take up your time, but living here in Washington, if you go to the supermarket, chances are your dollar is going to a European firm. If you go down to the corner to buy an automobile, chances are your dollar is going to a Japanese firm. Gradually, our entire economy seems to be disappearing. There are not that many American things one can buy any longer in the stores. As you point out, you personally run a trade deficit with the barber, but you make it back somewhere else. We do not make it back somewhere else.

MR. TAMNY: The point there is that I don't think you make the clothes you're wearing or most of the things that you buy. Does that make your economy worse? It doesn't make it worse at all. How it can it make a country's worse? Thank goodness people make things for us like cars, and toothpicks, and T-shirts, and socks, because if we had to make those, we'd be a very poor country. It's because people will do those things for us that we once again have time to create really valuable businesses. What an awful thing if China was wiped off the face of the earth, because we suddenly have to start doing some work that would really impoverish us.

MR. FITTON: Alan, you wanted to say something?

MR. REYNOLDS: Yes. First of all, a lot of those cars are made here. They just have foreign labels on them.

MS. KRUMHOLZ: And they're non-unionized.

MR. REYNOLDS: I wasn't going to say that, but the – look, you buy something from the classic deficit in goods would be New York City versus just about anyplace else. They don't have any goods come out of New York City except a few bagels or something. They have services. Some of those services turn out to be dysfunctional, but that's another matter, but we are a world exporter of services.

Anyway, a foreign country – I buy something from a foreign country. They end up with dollars. The next question is what are they going to do with those dollars? They can only do two things because they're only legal tender here. They either buy goods and services from us or they invest from here and they do.

Now, they could take it to their central bank and say swap it for something else, and when that happens, the dollar goes down. But lately, they've been saying, look, I've got euros, can I please have some dollars for them? So this is still an awfully good place to invest at least in relative terms and it will continue to be so.

And our manufacturing sector is as large as it's ever been in terms of output or share of GDP or real dollars. It's just these aren't made by people anymore. It's highly automated. We used to have a guy who would spray automobiles by hand. It was quite a nice craft. It still happens in an auto shop, but it's done by robots today.

MR. FITTON: Sheila, do you have any insights in the type of money that's at issue here in terms of foreign sovereign wealth funds or foreign corporations spending money in Washington to influence policy-making? I don't know if you have anything. I'm asking, hoping you do.

MS. KRUMHOLZ: We track money. We codify industry and we standardize it by organization. So we can see a growth in money going to politicians that has, at its root, a foreign source. It's coming from Americans. It would be illegal for it to come from foreigners, but these Americans increasingly, whether at home or abroad, work for foreign companies.

MR. FITTON: So the global economy for politicians is good. Any other questions? Just in the center here, with the glasses, yes.

Q: Just what is Judicial Watch doing about all this blasphemy? Do you have some –

MR. FITTON: Well, we always try to figure out what we can – we're trying to figure out what we can do in terms of leverage. As I said, we talked about the Freedom of Information Act and using that to expose some of what's going on here. We submitted the Freedom of Information Act request about the meeting with Henry Paulson, and it occurred to me that Fannie Mae and Freddie Mac are subject to the Freedom of Information Act, certainly now that they've been taken over by the government – certainly arguably, before then.

And I'm interested – and I think we're going to be initiating a Freedom of Information Act request about their giving. Who are they talking to in the government? How do they decide to give money to a certain politician? What do they expect in return? I think it would be a very interesting fight to get into over those documents, because I do think it's a terrible scandal.

And we may get over the hump of the economic crisis, but my concern is that we have this tremendous expenditure of taxpayers' resources, tremendous increase in the taxpayer liability, and it could have been prevented but for, I think, certain corrupt acts by some politicians, or at least it could have been mitigated. And I think there's some opportunities for us to figure out what's going on there.

I think a congressman or two might have the ability to challenge some of the delegation with their legislative authority and their ability to spend money, to designate the way it's spent is a strong argument as I'm sure – (unintelligible) – thinking that Congress has properly delegated its authorities to the Treasury Department in terms of giving them a check to spend this money.

But lawsuits like that – my experience as a non-lawyer, it is – (unintelligible) – by the courts because they don't like getting political questions like that, but I don't think this is over by a long shot. And Sheila and Barney Frank said the other thing that's going to be on the table next year and it's going to be a busy season in Washington just dealing with these topics I'm talking about.

MS. KRUMHOLZ: Yes, financial regulation is on the table, as well as healthcare and energy. I think those are going to the three primary charges for Congress and there's going to be a lot of money again rolling in, particularly through lobbying. And you can see – the good news is you don't have to – (unintelligible) – the information to see the campaign contributions. You can see now who the top recipients are, where the money is coming from say, for instance, from Fannie Mae and Freddie Mac now on our website, OpenSecrets.org.

There's more research that can be done about what specifically they were pushing for, but you can see in the lobbying documents, the details where they have provided them. They're not required to provide the specifics, but often, you will get a list of bills that their lobbyists were marching up to Capitol Hill to push for. So we and others, many others, are trying to make those connections for people so that you can, at a glance, pull up an organization and see both what they were pushing for and who their top targets were.

MR. FITTON: On so many big questions, do you think there's going to be any difference, substantively, between the way the Treasury Department handles things and the McCain administration versus an Obama administration? We'll start with you, John Berlau.

MR. BERLAU: The interesting thing I've been hearing – I think we'll be surprised – the interesting thing I've been hearing is that two of the contenders, two of the people that are being discussed for Senator Obama's Treasury department secretary – possible treasury secretary appointments are Jamie Dimon of JP Morgan Chase, who was in the government arrangement of that Bear Sterns takeover, and the government guarantee that Paulson got; and also Tim Geithner, who was originally a Clinton appointee under Robert Rubin at the Treasury Department, but because president of the New York Fed and arranged the Bear bailout.

So you've got a situation where a couple of Henry Paulson's cohorts in all of this could be the hand of the Obama Treasury Department. I think that's fascinating. And of course, Obama and McCain, unfortunately both backed the bailout, but we really don't know. You've got to hope that each of them will come to see the wisdom that the bailouts and nationalization don't work.

MR. FITTON: John Tamny, what do you think?

MR. TAMNY: A lot of people are pretty scared about what's ahead, particularly if it's Obama. My reaction coming from whether it's the Treasury Department is I don't see how you can do worse than what Paulson did. Just as Nixon was allowed to go to

China, very often, they allow Republicans to do really dumb things in Treasury because they've got a better reputation for economics.

And you think there's one positive thing we saw this week, Paul Volcker seems to get a lot of things wrong, but he's far more been the canvas, particularly in recent years, that he's like he's a fixed rate exchange kind of guy, stable currency kind of guy. My view is if Obama just does that, gets a Treasury secretary like a Larry Summers, who's supposedly in the running, who also believes in strong dollars, you love him or hate him, he's probably going to be a two-term president. Paulson was a weak dollar guy and look at Bush's presidency. If Obama gets this one thing right, as much as I find him distasteful in a lot of ways, he might actually do well.

MR. FITTON: Alan Reynolds, what do you think? Are you optimistic or pessimistic?

MR. REYNOLDS: About politics? (Laughter.)

MR. FITTON: I guess that's probably right. About Treasury appointees in the McCain and Obama administrations.

MR. REYNOLDS: That was an interesting set of Treasury secretaries. I said there were only two people on the *New York Times* list who ended up making a lot of money. He mentioned the other one, the guy at JP Morgan. He's made out like a bandit. He must be pretty good and he managed to swallow a couple of big outfits with some help from the Treasury.

Look, this problem is – I wrote in one piece that I didn't so much care if the Treasury bought up some dodgy paper from the banks that maybe they create a market for it or resell it at a profit. I do care when they start taking equity stakes. That is quasi-socialism. If it's 100 percent, it's 100 percent socialism – (unintelligible) – ownership. It's a means of production and a means of finance.

Now, this might be temporary. Maybe they're planning – I guess the banks at least have the right to buy their way back out. I know the guys at AIG want to get out from under that real bad. That is the major shareholders of AIG, which includes some mutual funds which we're all invested in, or many of us are invested in.

Changing people doesn't really change things much. We need to change the thought process. We need to criticize the whole notion. If people think that if anything goes wrong, the Treasury can do anything it damn pleases, then we're in trouble. If people think the Federal Reserve can debase its asset portfolio with any kind of second-rate IOUs, then we're in trouble because that's the backing for the U.S. currency. We've got to stand firm against foolish ideas, and I don't see either party doing that right now.

MR. FITTON: Thank you. This is, I think, a good place to wrap up. I'd like to thank John Berlau, Sheila Krumholz, John Tamny and Alan Reynolds. We eventually – we'll put this up on the Internet and have a special written report.

I encourage you to track all of these individuals' work at RealClearPolitics.com, CEI.org and the 75 websites that John mentioned, and John and Alan Reynolds over at Cato and newspaper, and the Center for Responsible Politics, their OpenSecrets.org and their main website. It's just an excellent resource, or excellent resources, for those trying to track who's giving money to who. And people can draw their own conclusions as to whether those transactions are corrupt, or lead to corruption, or give the appearance of corruption.

And obviously, JudicialWatch.org is our website. And I appreciate your time this afternoon, and we expect to have another panel this year after the election to talk about the economic – (unintelligible). So you'll be hearing from us again on that. Thank you for your time. I appreciated it.

(END)