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# Money for Nothing

*Who caused the financial collapse? Just about everyone.*

By: Lewis E. Lehrman – January 14th, 2013

To appreciate this landmark work it is necessary to know a bit about the author's background.

John Allison is not only a banker-entrepreneur; he is also a recognized intellectual leader of American business. Moreover, Allison's financial expertise is a product of his personal biography: In a mere two decades, he built BB&T (Branch Banking & Trust Co.), a comparatively small Southern bank of $4.5 billion in assets, into a $152-billion financial enterprise, making it one of America's largest and most profitable banks. But unlike many overpaid, underperforming CEOs, Allison focused his leader-manager skills—at modest compensation—on behalf of his employees, customers, and shareholders.

Briefly stated, Allison's core principles begin with an unapologetic dedication to customer-oriented banking and carefully managed risk-taking as sound and effective means to long-term profitability and high returns on capital. BB&T deploys an uncommon means to sustain the bank's dedicated corporate culture: continuous, serious, systemic employee education aimed at the formation of leaders, executives, and well-trained employees at every level. A core goal of every employee must be to focus on making every client profitable and successful on a risk-adjusted financial basis—that is, through conservative banking. False financial products were neither fabricated nor widely distributed during the bubble years (such products having been an important cause of the financial crisis). Monthly employee readings in philosophy and economics are mobilized to reinforce the core principles.

At the center of this banking philosophy is the development of the full potential of each employee, and each client, of the bank: This strategy, Allison argues, is the optimum path to shareholder, customer, and employee enrichment. Many firms pretend to such a strategy; Allison earned a national reputation because he actually carried it out, and successfully, in a banking system engaged during the bubble years in a "race to the bottom."

In a free-market society, it is hard to exaggerate the importance of such a corporate culture. And in business, the individual conscience, dedicated to long-term rational self-interest, is the indispensable condition of a minimally regulated free market. It is striking that Allison's strategy was vindicated by good returns on capital; it is equally striking that BB&T's corporate culture was proven right in the financial crisis and Great Recession, as BB&T experienced not a single quarterly loss during the financial earthquake of 2007-2009.

It is necessary to know all this in order to understand the importance of *The Financial Crisis and the Free Market Cure*. As the head of a major American bank, Allison was witness to the decisions of government, Federal Reserve leaders, and banking CEOs that led to a huge speculative bubble and the collapse of the financial system, including Fannie Mae, Freddie Mac, virtually the entire cartel of big banks and brokers, and major companies. Allison guides us, with a gimlet eye, through taxpayer-subsidized bailouts of these wards of the state, focusing on a reckless, insolvent, privileged financial oligarchy—subsidized by a feckless Fed, a dilatory Treasury, and a politicized FDIC. The coercive power of the federal government, and the moral hazard of excessive regulation, is dissected and debunked.

Allison pulls no punches when identifying causes and culprits. He names names. He also tells us that "the vast majority of the explanations for the crises . . . presented in the popular press are not true." This is because journalists and historians rely on anecdotes and indirect reports from participants, whereas Allison was a key insider, observing the ongoing maelstrom, day-to-day, for two decades. Here we see a financial malignancy metastasize in the hands of hapless surgeons in Congress, in the White House, and in the Treasury and the Federal Reserve.

The only way there could have been a bubble in the residential real estate market was if the Federal Reserve created too much money. It would have been mathematically impossible for a misinvestment of this scale to have happened without the monetary policies of the Fed.

Of course, the press ignored Allison's interpretation of the crisis since the Fed is a totem of the economic, journalistic, and intellectual elite. "Unfortunately, in [Alan] Greenspan's case, power not only corrupted him, but also destroyed his integrity." In the lead-up to the collapse, Greenspan "created a structure of negative real interest rates," forcing rates down to 1 percent, encouraging and providing incentives to banks and borrowers to buy and sell poisoned products—and to take on vast amounts of shaky debt and leverage which could not be sustained if higher real interest rates returned.

Enter Ben Bernanke, former Princeton economist and Fed vice chairman under Greenspan: "After he became chairman [in 2006] Bernanke rapidly raised interest rates and created an inverted yield curve" (higher short-term rates than the high long-term rates). But homeowners, businesses, and banks, lured by the Fed into leverage and cheap loans, could not finance the Greenspan interest-rate increases, followed by Bernanke's abrupt move to raise the federal funds rate (the interest rate the Fed charges banks) to 5.25 percent.

The impact of such an interest rate move (from 1 percent to 5.25 percent) must be thought of as a price increase of 500 percent plus—similar to an increase in the price of a loaf of bread from $2.50 to $15. Remember that Americans (and consumers worldwide) had borrowed and leveraged themselves during the period in which Alan Greenspan forced the federal funds rate down to 1 percent, giving rise to subprime homebuyers who were publicly encouraged by Greenspan to take on low-rate, "interest-only" mortgages. Global financial institutions subsidized by the Federal Reserve aggressively fabricated shaky loans, repackaged them, and sold them worldwide to individual and institutional client investors who trusted the lenders.

Then Bernanke "held the inverted yield curve for more than a year (from July 2006 to January 2008), one of the longest yield-curve inversions ever." And inverted yield curves historically lead to recessions. In a word, according to Allison, the Federal Reserve was both the fundamental cause of the real estate bubble and the agent of its collapse. But Bernanke "was adamant that there would not be a recession."

Allison's conclusion?

In my career, the Fed has a 100 percent error rate in predicting and reacting to important economic
turns . . . [because it] is trying to arbitrarily set the single most important price in the economy—the price of money.

And yet, as we know, setting wage and price controls, from the time of Diocletian to Richard Nixon, has proven in every case a disaster for economies and the people entrapped by them. Only totalitarian regimes have compelled and sustained comprehensive price and wage controls—until national collapse. In peacetime, free individuals will not long sacrifice themselves and their families to the arbitrary, gratuitous coercion of the state.

So does Allison have a solution for the distortions, subsidies, and money-printing exercises of the Fed? He is an advocate of the policies of the late Austrian economist Ludwig von Mises, and a persuasive, principled advocate of a purer free market, through which we can reform our overregulated economy.

For monetary order, Allison's explicit proposal is a "private banking system" free of Fed manipulation and incompetent regulation (the Fed being the ultimate monetary cause of booms and busts). Allison's free monetary order "operates on a market-selected monetary standard, which would probably be gold," and that monetary standard, he argues, like any honest system of weights and measures, must be a reliable and trusted standard of measurement. Allison's analysis is that the standard, namely the dollar, should be expressed as a defined weight-unit of gold and institutionally associated with a private banking system. In the absence of FDIC subsidies, sound banks would be based on earned trust, disciplined by competitive solvency requirements. These free-market institutional arrangements would be reinforced by effective bankruptcy laws, and by laws, strictly enforced, against force and fraud.

Of course, any one of Allison's 25 chapters can be cited for his candid and authoritative analysis of the problems of the American economy. There are shrewd inquiries into the labor market and unemployment, into FDIC incompetence and political influence, the SEC and TARP. Only in a truly free market, he writes, shorn of crony capitalism, may the individual choose the purpose-driven life of a dedicated calling, the sole road by which he can gain authentic self-esteem.

For the American problem, in Allison's view, goes beyond economics:

The causes are far deeper, longer-term in nature and far more destructive. Our educational system, especially our "elite" universities, played a far more significant role in the destruction of wealth than greed on Wall Street did. The ideas that these elite

universities are currently teaching our future leaders pose a fundamental threat to our long-term prosperity.