# The Money Hunt

*With the right policymaking, the United States can emerge from this recession sooner than you think.*

*By David Smick*

**THE LAST QUARTER CENTURY** of liberalized global financial markets and free trade produced a wealth-creating machine. Following the economic malaise of the 1970s, the Dow Jones Industrial Average jumped from 800 to over 11,000. (To match that performance in the next 25 years, the Dow would have to exceed 160,000.) The downside, of course, is that today's global economy has produced a roller coaster ride of financial terror.

Our financial regulators will now compensate by overregulating; Washington, D.C., is becoming the new financial capital of the United States. Terrified by the seizing up of world credit markets, the Treasury followed its UK and European counterparts with a rescue plan of government guarantees, direct taxpayer bank stock purchases and other financial market interventions not seen since the 1930s.

At issue is whether any of this taxpayer-funded market backstop will actually induce banks to start lending again. Government guarantees always sound reassuring in the midst of a panic, but every government intervention brings unintended consequences. In this case, the most dire consequence is likely to be a consolidation of credit in the hands of those that need it the least—the powerful industrialized economies, big corporations and money-center banks—at the expense of nonbank financial firms, emerging markets and the entrepreneurial sector. In 2009, money is going to be both expensive and scarce.

The problem is not that the world lacks money, but that the world's money is sitting on the sidelines. More than $6 trillion is sitting in idle global money market funds alone. Capital from sovereign wealth, hedge and private equity funds will stream back to the U.S. once we seem headed out of a recession. But the holders of this capital will want to know where our financial system is headed. Will we try a fruitless attempt to return to the horse-and-buggy days of finance? Or will we apply surgically precise reforms to fix the current system? Most important, will the funding of entrepreneurial risk-taking and innovation continue?

If our leadership thinks boldly and creatively in devising a game plan of reform, global capital will surge into the U.S. economy.

The G-20 summits that began November 15 are a start in determining new ways to reestablish trust and get capital flowing again. The U.S. leadership will confront the views of Sarcozy, Merkel and other European Union leaders who believe the U.S. financial system, now knocked down and bleeding, should be restructured to resemble Western Europe's sluggish, tightly regulated system. That system doesn't provide the strong incentives for lending that encourage entrepreneurial risk: In the last several decades the U.S. has created more than 30 million net new jobs, while Western Europe's system has created no more than a handful.

What I hope we will see is a public/private consortium where central banks and private banks together manage the flow of global capital and determine appropriate levels of financial leverage. The world needs a vehicle to assure transparency through the standardization of those mysterious securitized paper instruments, so that future investors can figure out what is actually in them.

Another outcome should be a well-thought-out balance between risk and effective regulation. There is an important difference between regulation and supervision. Bankers have shown that even with regulation they are too greedy to be trusted, and the regulators are no match for Wall Street wizards' financial sophistication. Before the subprime crisis broke, regulations were in place to force the banks to set aside rainy day capital in the event of a crisis. The banks skirted those requirements yet the bank regulators seemed unaware of what was happening. That is why both the regulators and market participants, working jointly, are vital for regulatory success.

If we follow this path, then the United States, the first to enter this economic crisis, could well be the first to emerge from it.

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