

## Friday, September 19, 2008

**Financial Crisis:** There have been other things going on in Washington this week, but nothing is as important or urgent as the financial crisis. The situation has deteriorated significantly in the last few weeks. Basically, the markets for virtually all forms of cash or debt are frozen and non-functional worldwide. There is simply a lack of confidence or, more accurately, fear about who can meet their commitments and who can't. That has locked up normal trading. This is not just a Wall Street problem. If this situation continues, every single American and probably every single citizen of any industrialized nation will be affected.....and not in a good way. The value of your savings account, your pension plan, your stocks or your mutual funds, depends on a functioning, transparent and liquid market. The market, right now, is arguably none of these things.

Yesterday, John McCain blamed SEC Chairman Christopher Cox. Nancy Pelosi blamed President Bush. A group of Republicans held a press conference to blame President Clinton and Democratic leadership. Barack Obama seemed to blame every Republican office holder in the last 14 years.

They are all wrong. And they are all right. Virtually no one saw this situation becoming this severe until the last few months. If they had, they would have proposed something that would have forestalled the problem. No one, including me, did that. As you know, I do not hesitate to blame Democratic leadership when I believe the problem can be laid at the foot of their policies. In this case, neither Republicans nor Democrats got it right. None of them caused this, but none of us had the solution that would have prevented it either until it was too late.

So, what now? The problem is very, very severe. We must take action that is substantial, complete and immediate to restore confidence to markets. The problem is still caused by the incredible mistakes and excesses of the subprime lending wave and the related drop in housing prices. The Treasury is proposing that the federal government basically buy all the bad loans (mortgage backed securities) that exist out there and take all of that uncertainty out of the markets. The details of this proposal are still being worked out. This could easily amount to \$500 billion which would have to be financed through the issuance of more Treasury Bills. Eventually, the government would recover most and perhaps all of this money if the economy stopped deteriorating and people paid their mortgages or home values stabilized.

All you regular readers of this missive know how fiscally conservative I am. But this is an extraordinary situation. I believe that we as a society have no option but to do this. And it must be done at such a magnitude that it completely solves the problem. We had all hoped that the Fannie/Freddie rescue would fix the problem. It didn't. We need to make sure that this is big enough to do it.

And then, the entire regulatory structure of the financial markets worldwide will need to be blown up and rebuilt. We are living with a regulatory structure that was set up after the depression. Let's hope that we can avoid more financial calamity before we change this outdated system.

**Other things:** House Democrats passed an offshore drilling bill that really would not result in much if any offshore drilling. The Senate will not even take up that bill. The Senate has 3 different drilling bills, none of which are expected to get the necessary 60 votes over there. So, it is unlikely that any energy legislation will be passed before the election. But, the offshore drilling ban will probably be allowed to expire on October 1st, because there are not enough votes to continue it. Pelosi is hoping that a President Obama will immediately replace the ban upon taking office. I hope she's wrong.

There is still lots of talk about a "Stimulus II" package, the continuing resolution to fund the government through next February, and an extension of a bunch of expiring tax credits including the current "patch" that keeps the Alternative Minimum Tax from applying to nearly every Californian.

But all of this will take a back seat to fixing the current financial crisis.

I will keep you informed.

Until then, I remain respectfully,

Congressman John Campbell