

## — OLD AND RIGHT —

usual, American neoconservatives manage to miss the point. Whining about London's more austere defense budget, Council on Foreign Relations writer Max Boot argues that it "means that even more of the burden of defending what used to be called the Free World will fall on our overstretched armed forces."

But they are overstretched only because U.S. leaders have been following the policy prescriptions of Max Boot and his cohorts. Even the notion of a "Free World" reflects obsolete thinking. A Free World arrayed against what? A Soviet empire that disappeared two decades ago? A motley collection of stateless terrorists? Such rhetoric tries to mask the dubious goal of interventions in strategically marginal places for obscure objectives.

Nation-building missions and armed democracy-promotion ventures are not essential to America's security. We do not need, and should not want, any more Iraqs or Afghanistans. More than 5,000 dead Americans and nearly \$2 trillion down the drain ought to deter Washington from pursuing similar schemes in the future.

It was bad enough during the Cold War when the United States appointed itself global policeman, but in recent years our nation has become the world's armed social worker. U.S. leaders will find that to be an increasingly lonely role. Even America's professed allies no longer have the military capabilities or the desire to join us as junior partners. Instead of berating them for a lack of loyalty, we ought to emulate their wisdom and restraint. ■

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BE NOT UNGRATEFUL to the achievements of scientific materialism and to the insights of many pragmatists. In practice you are living every day on the benefits of those achievements and those insights, even if you greet them with an affectation of pseudomedieval scorn. No church is going to rip out its telephones and electric lights because they are a product of scientific materialism. But though gratitude is overdue, enough is enough. Civilization depends today on conserving, against the nihilistic brand of scientific relativism [the] principle of a central common law. It alone protects all against the centrifugal special laws of class ego, nation ego, and individual ego.

Powerful psychological safeguards are needed to prop up common law at a time of toppling values. But not all safeguards are compatible with the human dignity that alone justifies their use. The safeguard most compatible with human dignity is not external brute force but a deeply entrenched inner check.

The most effective, most automatic way to enforce the ethical check is to formalize and institutionalize it, even at the painful but unavoidable price of sacrificing a certain amount of inspiration to institution. Some of the spirit must always be sacrificed to some of the letter of the law. The price must be paid. Whether grudgingly or with eager faith, you can never get around paying it—unless you take the anarchist position that civilization does not depend on organized society but can survive with no more framework than the natural goodness of man.

Because every human being is a cave man by nature, capable of every insanity and atrocity, you must prefer art and artifice, classicism and formalized social convention, to the cults of natural goodness, progressive education, and instinctive self-expression. For the same reason you must prefer the "conservatism" symbolized by the pruned and patterned gardens of Versailles to the "anarchism" symbolized by the romantic barbarous jungle. But if you can disprove this view of social stability, then you are entitled to be a philosophical anarchist. An idealistic pacifist anarchism (Thoreau, Kropotkin, Gandhi, George Orwell), rather than liberalism or socialism, would be the most logical and most attractive alternative to conservatism, in case the latter's pessimistic premises about human nature were proved wrong.

To make people live the ethical check instead of only theorizing it, the best sanction is the community's experience of having lived it for centuries, the feeling of it "always" being so and being there: just as "so" and just as "there" as the sky and earth that form the roof and stage of the innately ethical drama of man. Whether your source for your ethical code is natural or supernatural or that blurred borderline to which both science and religion tend, only this conservative experience of communal tradition will turn it from abstraction to a way of life.

Liberals favor universal suffrage horizontally in time. Conservatives favor it also vertically. If you have become convinced that freedom depends on the unbroken continuity of communal ethical tradition, then you must give the vote also to your ancestors.

—Peter Viereck, *Shame and Glory of the Intellectuals*, 1953

# Bernanke's Bad Bet

The Fed sacrifices Main Street's wealth to Wall Street.

By Charles Hugh Smith

WOULD YOU CALL sacrificing \$6 trillion of America's household wealth to inflate the stock market by \$2 trillion a good deal? Few would, but the Federal Reserve obviously thinks it's a bargain, for this tradeoff is the explicit result of the central bank's latest round of quantitative easing, the grandly named QE2.

From the time Fed officials began outlining QE2 in June—a plan to buy \$600 billion in U.S. Treasury bonds and inject that stupendous sum into the banking sector—the U.S. dollar plummeted by 15 percent. (It has since recovered a little.)

The mainstream financial media studiously ignored the downside of this beggaring of the dollar. The \$43 trillion worth of non-stock assets held by U.S. households—real estate, bonds, cash deposits—are denominated in dollars, so a 15 percent depreciation in the currency knocked about \$6 trillion off the purchasing power of those assets.

Given that the Fed's zero-interest rate policy (ZIRP) has lowered the yield on cash to almost zero—earn a big 1/10th of 1 percent on your cash—the predictable result of the latest easing was a mad rush into risk assets such as precious metals, commodities, and stocks, which jumped 19 percent from June to early November.

That was the intent, as Fed Chairman Ben Bernanke recently made clear: "Higher stock prices will boost consumer wealth and help increase confidence, which can also spur spending [that] will lead to higher incomes and profits that, in a virtuous circle, will further support economic expansion."

In other words, the Fed threw the dollar into the shredder in an attempt to

create a stock-market wealth effect that assumes consumers who see their portfolios rising will borrow and spend more, igniting the moribund U.S. economy.

What QE2 has already sparked is not growth but skyrocketing agricultural commodities prices. Though Chairman Bernanke has claimed QE2 won't cause inflation, the average bloke can see that a 70 percent increase in the cost of wheat will end up raising the price of bread. Paying more for essentials while household incomes stagnate is a recipe for impoverishment, not growth.

There is a more than a whiff of desperation in this stock market wealth-effect gambit, and that says volumes about the fundamental flaws in the Fed's policies. Why would the Federal Reserve make such a risky bet? Is making such bets really the central bank's job?

The Federal Reserve's mandate is limited to "maintaining monetary and credit aggregates commensurate with the economy's potential to increase production, so as to promote the goals of maximum employment, stable prices, and moderate long-term interest rates." In plain English, the Fed is supposed to manage the nation's supply of money and credit, not its economy or stock market. Yet the latter is precisely what the Fed is trying to do by boosting the stock market to engineer a wealth effect.

There are two fatal errors in this policy: one is a fundamental misunderstanding of capitalism, and the other is a misunderstanding of the stock market.

In a capitalist business cycle, "animal spirits" reach euphoric heights in a strongly expanding economy, and even-

tually people borrow a lot of money to speculate on future growth: betting, in effect, that trees will grow to the sky.

At the peak, too much credit is extended, too much money is borrowed, too much capacity is built, and too many speculative bets are placed. In the inevitable cooling of the economy that follows rapid expansion, the overleveraged find they cannot service their debt or roll it over into new loans, and an overhang of buildings and capacity cannot be rented or sold for a profit.

In this phase of the business cycle, the overleveraged and over-indebted go belly up, and lenders and investors take losses as empty buildings and factories are sold for pennies on the dollar. Balance sheets are cleaned up as assets are liquidated and uncollectible debts are written off. The Federal Reserve's role in this contraction-of-credit phase is to provide sufficient liquidity for qualified borrowers to roll over their debt into new loans and for new buyers to purchase distressed assets.

This contraction phase is the process of capitalism known as creative destruction, and it is the essential foundation for future growth. Malinvested money is lost, risky speculations go bust, and patient capital eventually ends up owning the distressed assets. The process is painful in the short term. But the sooner the bad debt is cleared and the overcapacity shuttered or sold off, the sooner new enterprises and sound credit can expand.

Sometime after the deep 1981-82 recession, Fed policymakers decided to revoke the painful part of the business cycle and maintain only the happy part of