The Renewal and Evolution of Economic Security During the U.S. Financial Crisis

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The evidence of pain, hardship and fear are clear. Even for the most optimistic of people, the United States' economic condition is frightening. With rapidly rising unemployment, a relentlessly declining stock market, growing anxiety and shrinking confidence among its citizens, it's indisputable that the United States is mired in a deep recession. And while the extent of the recession is not yet known, the eerily similar comparisons between the Great Depression and the current economic crisis are alarming and worrisome. Gross domestic product (GDP) is contracting, the financial sector has been brutally beaten, companies which once stood as pillars of America's economy have been critically weakened, and in some cases destroyed, and a sense of dread has spread throughout the country. The facts and figures of suffering are abundant and alarming. The economy has lost 4.4 million jobs in just over a year and recently witnessed the unemployment rate exceed 8% for the first time in 25 years (Torres). Moreover, the combination of plummeting house values and 50% deterioration of the stock market have severely reduced the wealth of most Americans, causing significant financial stress and hardship. In the 4th quarter of 2008 alone, American households lost $5.1 trillion, or 9 percent, of their wealth, the largest drop ever in a single quarter since the Federal Reserve (the "Fed") starting keeping such data in 1952(Baijaj). Meanwhile the number of foreclosures in 2008 set a single year record by surpassing 3 million, an 81% increase from 2007 and 225% from 2006. One in 54 homes received at least one foreclosure filing during this dreadful year. Retirement funds have disappeared, job security has become nonexistent and houses are being foreclosed at fearful rates. As a result masses of Americans are facing financial peril and uncertainty at levels once reserved only for memories of the Great Depression. Even more disheartening, key economic indicators and the consensus opinion among economists suggest that the economy, and its citizens, will experience more pain and hardship before any substantial recovery occurs. Clearly America and its people have come under attack, only this time the threat is not physical, but economic. As the devastation of the financial crisis has unfolded, the economic security of Americans has become jeopardized.

The deterioration of the American economy and suffering of its citizens has not progress due to a lack of government effort and innovation. Rather, in the past two years the United States government has made extraordinary and radical efforts to stabilize the financial sector and avoid an economic upheaval. In attempting to protect its economy and citizens, the government has acted with boldly and with little regard for expense or the precedent of *laissez-faire* economic policy. Billions of tax payer dollars have been injected directly into the banking system, private companies have received massive bailouts, and President Obama has recently signed a nearly $800 billion dollar stimulus bill (Economic Stimulus). Additionally, the Federal Reserve has slashed interest rates essentially to zero, implemented innovative credit lending programs to provide direct capital to numerous institutions and markets and permitted its balance sheet to triple in value to over $2 trillion (Robb). While the merit and benefits of these actions can be debated, the incredible magnitude and boldness of these actions is undeniable. More importantly, the size and scope of the response has been as extremely revealing and illustrative of how the government has recognized and confronted the current threat to economic security America and its people are experiencing. Defending its citizens, institutions and nation from threats, both foreign and domestic, and maintaining stability and security has always been a primary concern for countries. Normally such threats and issues of security are regarded as nearly exclusively in physical terms. National security is traditionally considered the physical protection of the nation. However, the severity and speed of damage inflicted by the financial crisis and subsequent recession have dramatically altered the priority of pursuing and maintaining economic security. From bailouts to stimulus packages, the recent actions taken by the U.S. government reflects a paradigm shift in the perception of national security. Whereas national security used to be primarily concerned with physical security, the protectionist and economic nationalist actions taken by the government exemplify the overwhelming power of economic threats and the importance of government in maintaining economic security. In the shadow of the financial crisis, America has been forced to recognize the renewal and evolution of economic security.

To fully grasp the significance of the recent actions taken by the U.S. government, and understand why a paradigm shift has occurred, one must only compare the stark difference between the principal economic policies which reigned supreme for decades before the crisis and the current economic picture. For years America was one of the biggest lobbyist and steadfast proponents of market-driven capitalism. Trade liberalization, privatization, deregulation, and the virtues of market forces were touted by America as the keys to economic growth and prosperity. America not only held these beliefs to be good for their own country, but believed that they should be adopted by the rest of the world. Often referred to as the “Washington consensus,” America championed free-market capitalism as the greatest means for ensuring economic security and prosperity the world over. The World Trade Organization (WTO) and the North American Free Trade Agreement (NAFTA) were created to promote this form of capitalism and discourage acts of economic nationalism or protectionism. While reality deviated slightly from rhetoric, the lines between business and government were clearly drawn.

Businesses either successes or failed on their own merit, not because of government exploits. The market was deemed sacred and, when free from government intervention, the most capable system for determining true and fair value. The American financial sector was hailed as the pinnacle of innovation and efficiency, self regulated by market forces and brilliant rational self interested actors. America's dedication to free-market capitalism was most evident in its willingness to permeate into the healthcare and retirement services. As opposed pro-capitalist European nations, America dismissed national healthcare system and condemned pensions, favoring instead private insurance companies and stock market invested 401K plans. The government still considered economic security important; it just thought free-market, government-free, capitalism was the best means for achieving this goal.

When compared to what has transpired since the financial crisis emerged in 2007, it is evident that a fundamental shift in strategy and abandonment of ideology to preserve economic security was occured. The sink or swim mantra of free-market economics has been discarded with General Motors (GM) and Chrysler, two of America's largest companies, receiving federal assistance of $13.4 billion and $4 billion respectively (Bunkley). In defending the bailout, the government highlighted the negative economic ramifications if the auto industry collapsed and downplayed the bailout's protectionist nature. Federal bailouts and partial nationalization of private companies has been even more pronounced in the financial sector. American International Group (AIG) has received $173.3 billion of government funding in exchange for an 80% equity stake in the company. Mortgage lender giants Fannie Mae and Freddie Mac has been placed under conservatorship, and injected with direct capital and guarantees on future losses (Goldfarb). And of course, using the Troubled Asset Relief Program

(TARP), the Treasury has allocated $700 billion dollars for bank bailouts. Additionally, the Federal Reserve has begun purchasing mortgage-backed securities, commercial paper and long term Treasury bills, measures that have considerably expanded the Fed's operation beyond its traditional functions and focus on monetary policy. Furthermore, a nearly $800 billion stimulus package has been passed, including the highly controversial "Buy American" clause. All of these actions spew economic nationalism, favoritism, and protectionism. They completely contradict the fundamentals of *laissez-faire* economics and free-market idea. They are seemingly un-American. Yet these actions were justified, and rightly so, as being necessary for maintaining economic security, both for the citizens and nation as a whole. Without them, America would definitively be worse off today. In other words, the dramatic government policies enacted in response to the financial crisis economic threat to the U.S. economy and its citizens' wellbeing illustrated America's recognition of economic security's renewal of importance.

Before further analysis of this paradigm shift in America's understanding of security can be completed, however, the financial crisis and governmental response must be address further. In order to fully understand the profound impact of the financial crisis on economic security in America it is essential to fully discuss and examine the various aspects and events surrounding the issue. First, the concept of economic security must be investigated. Despite being the justification for the radical action undertaken by the government, the term remains vague and open to debate. Nonetheless, the concept of economic security has a few distinct and incontestable attributes that must be identified to formulate the framework necessary to evaluate the current crisis, the government response and the evolution of economic security in America. Second, this paper will look at the economic crisis and America's response. As the financial crisis unfolded, and the recession began to develop, America's government took extraordinary and direct measure aimed at countering the mounting crisis. Unfortunately a complete account of all the causes and problems of the crisis cannot be provided because the proceedings; involved extremely complex financial operations, are subject to interpretation and debate, and would require extensive elaboration beyond what is necessary for our analysis. Not all the causes of the crisis will be mentioned nor will all the government's actions be discussed. Rather only those action and causes that are critically important and exemplify the situation will be included. Each introduced measure will be followed by explanation of why these actions were considered essential for either creating or maintaining economic security. Finally combining these three elements, an enlightening picture will emerge illustrating how the current economic crisis has commanded government action and how, along with the crisis itself, these actions have profoundly altered the perception of economic security in America.

Economic Security

The worth and significance of national security are obvious. Moreover, that the government should consider pursuing measures and policies that achieve national security is assume to be given truth. However, what is not as obvious is what exactly constitutes national security and what areas in incorporates. *Security* can be loosely defined a "condition that results from the establishment and maintenance of protective measures that ensure a state of inviolability from hostile acts or influences" (Nesadurai). Hence the concept of national security would be the achievement of security for a given nation. A more formal definition for national security is given by the late political scientist Hans Morgenthau, who described national security as "the integrity of the national territory and its institutions" (Morgenthau). Combining the two for mentioned definition a relatively simple yet straight forward concept emerges. National security is the protecting the integrity of a country from hostile attacks.

Traditionally the notion of protection of integrity and hostile attacks has been considered primarily as a physical issue. The attacks which must be prevented or defended against are physical in nature and threaten the physical safety of the nation and its people. This is especially true for the United States, where security and physical protection are often considered interchangeable in describing national security. Alternatively, the concept of economic security is often neglected when discussing national security. Whereas physical security is considered both a macro and micro, with the army protecting the countries safety and law enforcement individual safety, economic security is rarely considered to be a national issue. Rather, economic security is often contained to micro assessment of an individual or company's financial security. Companies attempt to maintain economic security by implementing sound business practices and strategies, properly managing their assets and liabilities, and striking a proper balance between supply, demand and price. Individuals' economic security involves saving, protecting against risk, planning for retirement, managing finances and maintaining employment. For both companies and individuals economic security has always enjoyed a stable place under the umbrella of security. Furthermore, when talk of economic security is enlarged to an entire country's economy as a problem of national security, it is often in context of a developing economy and country. And in these cases the issue is usually "economic i*nsecurity*" rather than economic security. As defined by Helen E. S. Nesadurai, economic insecurity is the "vulnerability of states, societies, groups and individuals to economic events, particularly economic shocks and crisis that disrupt material well-being". Accordingly, the topic of economic insecurity examines now developing states are vulnerable to economic attacks and how they can institute reforms to ensure greater protection.

The attention and focus on economic security of the entire nation, however, seldom garners significant attention when compared to physical security. This is certainly true with the United States. When the issue of national security arises, especially after the terrorist attacks of September 11th, 2001, the assumption was the desired security was physical. Nevertheless the importance of economic security as an essential part of national security is undeniable. While the physical security of territory, citizens and interests should not be undervalued, the protection of the economy, its institutions, companies and workers should not be underestimated. This is particularly true in the modern global order. Whereas historically countries military might was used to equate their strength, the modern global order with an emerging global market and singular economy, economic size and influence is often cited as a determinant of a country's strength. Germany, United Kingdom and Japan are deemed major actors in worldly affairs, and enjoy significant power and influence. Yet none of these countries posses the military might of Russia, India or the Democratic People's Republic of Korea. Instead, they draw their power from their economic might. Plainly, the value of a country's economic strength cannot be denied. This is true with the United States. Although this US has a large military, much of its global power is derived from its economic strength. Nonetheless, governmental actions in the name of national security has remained focused more on physical threats and attacks than on economic ones.

Recognizing the importance of economic security for countries, the obvious question becomes, what exactly is economic security in terms of national security? Although any characterization or understanding will be subject to debate, I believe there is a basic definition that can serve as a basis for comprehending the essential nature of economic security. Furthermore, while assuring the obtainment of basic necessities, including food, energy and raw materials, to ensure the persistence business and individuals must be included in any discussion about economy security; it fails to capture the broader answer. Instead, I consider a country's economic security to be a condition that results from the establishment and maintenance of protective measures that defend a country's economy integrity against economic hostility and attacks. So, while GDP growth, unemployment, inflation and current account balances are economic indicators that characterize a country's economic health, its economic security is a broader concept that reflects an economy's vulnerability to hostility and attacks. High GDP growth, low unemployment and low inflation may result from a country achieving economic security, but these measurements cannot alone measure the level of economic security enjoyed by a country. Rather, a county's economic security is measured by its resistance to and ability to coup with difficult economic situations. Also, similar to physical national defense, where weakness is most visible during an attack, economic security is best evaluated when an economy is suffering from some form of hostility. Moreover, this definition contains a role for government in achieving economic security for its country. By establishing and maintaining of protective certain measures a government can alter its economic security. Purposely this definition is vague. It provides, however, a framework for analysis government's actions taken to further or uphold economic security.

The Economic Crisis and America's Response

The financial crisis that engulfed the United States as well as the subsequent recession is not a simple situation with simple explanations. Many elements and forces acted in concert to create and strengthen the crisis. The analogy to a "perfect storm", while cliché, is an accurate description of the situation that has all ready inflict catastrophic damage on the financial sector, the broader economy and the America people. Additionally, describing the financial crisis as a single event and problem is naively false. Similarly to how the Great Depression and New Deal where umbrella terms that captured many fragmented parts, the financial crisis is a loosely connected network of problems and events. The essential problems and aspects of the financial crisis, however, can be determined and highlighted without much incongruity. In order to properly frame and full understand the primary issues associated with the financial crisis one must first examine the causes of the crisis. No single event or financial action or government measure can claim complete responsibility for causing the crisis. Likewise, no one person or industry or institution can be blamed for creating the problem. Instead, one must concluded that the government, Wall Street, the Federal Reserve and the consumers all share responsibility for inciting the problem. Economists and historians alike are certain to dedicate countless essay and books to the causes of the crisis, with each vilifying a different actor and assigning blame on that actor more than the others. While this is a worthy debate, for the time being it's safer to assign blame across the spectrum and focus on outlining the role each actor played, rather than attempting to indentify a main culprit. What's more, although the crisis cannot be blamed on a single actor, what started the financial fiasco is obvious.

During the first half of the 2000's two simultaneous events occurred, the inflation of the housing bubble and increased complexity and interdependency in the American financial system. The former ultimately triggered the financial crisis and credit crunch; while the later enhanced its harmful reach and amplified the vicious cycle the crisis set off. The steep rise is housing prices that defined the market bubble had many causes; four of which are most cited as contribution factors.

First, ample and easy credit was abundant in the early 2000's due in large part to low interest rates set by the Federal Reserve. With a stock market still reeling from the collapse of the "dot-com" bubble in the late 1990's, and fearing a recession following the terrorist attacks on September 11th, former Federal Reserve Chairman Alan Greenspan decided to lower interest rates in an attempt to promote economic activity. From December 2001 till December 2004 the Federal Funds rate was kept at or below 2% (Federal Reserve Historical Data). Although the Fed's expansionary monetary policy was intended to stimulate investment and growth, it also inadvertently, contributed to the inflating of the housing bubble. By dramatically lowering the cost of borrowing, mortgages rates were reduced and Wall Street was able to borrow profusely, increasing their total leverage. This was also evident by the shift away from low yield conservative investments to higher risk assets. With interest rates low, investors need to find alternative to Treasury Bills and other low yield investments. Simultaneously, the prolonged period of low interest rate provided both consumers and investors with the false sense that credit would remain easy to acquire in the future. When the initial shock of September 11th wore off, and yet the Fed did not raise interest rates, investors began to believe that rates would remain low. Therefore, they made calculation assuming a prolonged lower rate of borrowing.

Second, previously uninterrupted economic growth and housing price appreciation provided investors and consumers with a false sense that the future could remain as prosperous as the past. Nearly everyone believed housing prices could not fall and that real estate investment was safe. Consumers naively began taking out mortgages they simply could not afford. Typical of any asset bubble, rapidly rising housing prices lulled consumers into believing their house would only appreciate in value. This behavior is often referred to as rational exuberance. Even when in the midst of an asset bubble, and fully aware of such, it is reasonable to belief that the bubble will continue to rise. So even if consumers and investor knew homes were overpriced, they assumed they could get in and out before the burst. Consequently, consumers purchased homes they could not afford assuming that they would continue to increase in value. Homing became seen as an investment opportunity. For this reason, people purchased homes with little money down or perceived ability to pay the mortgage. All that mattered was that the price was supposed to continually increase.

Third, various government programs and actions established to promote home ownership unintentionally contributed to the housing market escalation. Persuaded by the benefits of homeownership, both for the individual and community, the government established numerous programs and institutions to encourage the “American Dream” of owning a home. Thus, not only were consumers, investors, and lenders to blame for the impending economic collapse, but the government played a key role as well by encouraging irresponsible borrowing and lending practices. Chief among these actions were the creation and manipulation of Fannie Mae and Freddie Mac. As government sponsored enterprises (GSEs) mortgage lending giants Fannie and Freddie enjoyed an implicit guarantee from the U.S. federal government. This allowed them to borrow at artificially low interest rates because creditors assumed the U.S. government would never permit either company to default. As a result, Freddie and Fannie were able to lower mortgage rates. Additionally, Fannie and Freddie were subject to pressure from law makers to expand homeownership among lower income families and minority groups. Along with other government programs, Fannie and Freddie were encouraged to provide lending support for these groups. Although the concept of expanding homeownership was admirable, these actions further exacerbated the bubble and often provided mortgage to people who could not afford to make the payments.

While these three factors meaningfully contributed to the housing bubble's rise, it was, arguably, the financial sector that played the most significant role in its inevitable burst. First off, there was a markedly significant increase in capital flow into the American financial system before and during housing bubble. Alan Greenspan defends that it was not the Fed that deserves blame for the bubble, but the improper handling of large amounts of capital inflows from abroad. Such large capital inflows from abroad, he argued, tended to further increase the assets prices, including mortgage related asset. More often cited as the greatest factor, however, was the rise of securitization of mortgage loans and the expansion the subprime mortgages market.

Traditionally, the mortgage business was a simple exchange between a borrower and lender and the process followed a clearly defined order of operations. Potential borrowers seeking a mortgage would approach a bank in search of securing a mortgage for a house. Upon proving the credit worthiness of the borrower, the bank would supply the capital and retain the borrower's mortgage as an asset on their balance sheet. While there were no inherent problems with this conservative system, it limited the amount of capital available to the mortgage market because banks were constrained in the number of loans they could facilitate. Advances in technology and financial innovation, however, drastically altered this process and introduced the practice of securitization, in particular the creation of mortgage backed securities. Securitization, in its simplest form, is the process whereby cash flow-producing financial assets, in this case mortgages, are pooled together, repackaged, and sold to investors. By pooling together various mortgages into a single mortgage backed security (MBS) to sell to investors, bankers were able free up capital for additional mortgages. This allowed banks to increase their loans, and, thus, their profits. Meanwhile, confident that pooling mortgages together mitigated risk, investors eagerly purchased MBS, judging them to be the next great financial innovation. In theory, MBS were a revolution in financial efficiency and risk management. Consequently MBS quickly became a hot commodity on Wall Street, either every trying to join the MBS bandwagon and promised profits.

MBS were not flawless however. The quick proliferation of the MBS had a profound, and unexpected, impact of the mortgage market. By moving mortgage off the bank's balance sheets, capital was freed-up, allowing the banks to make more loans. The negative side was that banks and mortgage lenders no longer had an incentive to perform due diligence on mortgage seekers. Since mortgages could quickly be securitized and sold off to investors, mortgage lenders no longer had a reason to worry about default risk and plenty of incentive to write as many mortgage as possible. This problem intensified as the MBS market grew and demand escalated. Eager to make a profit, banks and other mortgage lenders turned to the subprime market. Subprime borrowers are defined as borrowers will credit scores below 600, indicating a higher likelihood of default. Unsurprisingly, an expansion of the subprime mortgage market followed. Subprime borrowers were provided mortgages with superficially good deals, often requiring little money down and interest rates that began low but increased over time. The use of these teaser rates enticed subprime borrowers to sign off on mortgages they did not fully understand and were incapable of paying. Many times they believed the deal they were receiving was too-good-to-be-true. Unfortunately, frequently it was just that. This newly tapped market provided Wall Street with more investment opportunities. As a result, the demand and prices for these assets continued to increase as investors continued to leverage bets against what they thought was a foolproof way to generate profits.

Unfortunately as quickly as the bubble inflated it burst. The housing market had become over priced, over saturated, and in need of a dramatic market correction. The symbiotic relationship of rising default rates and depreciating housing prices began to develop, whereby decreasing housing prices caused an increase in defaults which in turn further decreases housing prices. While this cycle is a natural market correction, the new found role of mortgages in the financial market and the importance of mortgages to individuals' person finance resulted in an overwhelming implosion of the American economy. The various MBS and other innovative instruments, which once seemed immune to risk because of their supposed

AAA credit rating and diversified risk, were now rapidly declining in price because the mortgages that formulated their underlying composition and source of value were faltering. As defaults and foreclosures rose, especially in the subprime market, MBS turned toxic as demand quickly disappeared and their value. Holders were stuck with an asset with rapidly decreasing value and no market in which to sell it. As fear of toxic assets and ensuing losses grew, financial institutions and investors began to deleverage and a massive credit crunch ensued. Again a vicious cycle emerged. As fear and the credit crunch escalated, investors rapidly with withdrew their funds in a flight to safety. This only exasperated the credit crunch and further fueled the panic. It was President George Bush who best summarized the problems plaguing Wall Street when he noted that, “there’s no question about it. Wall Street got drunk… and now it’s got a hangover.” While President Bush was referring specifically to the great profits, and subsequent losses, experienced by Wall Street executives as a result of the bursting of the housing bubble and MBS, his words also highlighted Wall Street’s poor judgment in assuming that the housing market would continue its strong and robust upward trend... Increasing Wall Street greed and poor judgment, coupled with deregulation and lack of government oversight, ultimately resulted in a deadly situation for Wall Street.

By the fall of 2007 fear and uncertainty in the financial sector had intensified to a frightening degree. Banks, worried about the creditworthiness of other institutions and their own potential losses, stopped loaning to each other. Fundamentally dependent on access to credit, the financial sector began to fall apart. Without access to credit financial instructions run the risk of not meeting capital requirements or repaying debts and obligations. Credit had come to a frozen standstill. Ironically, the concept of free flowing credit and capital mobility is the primary function of a financial sector. And prior to this crisis, America's financial sector's ability to mobilize capital with maximum efficiency was lauded as the ideal financial system. Now, however, Wall Street and the financial sector were anything but laudable. The stock market was hobbling. Anxiety was increasing. And worst of all, speculation. Speculation that highly leveraged financial instructions with sizeable bets on MBS and other housing related assets were facing possible insolvency compelled creditors to call in their loans and banks to stop lending to one another. In hindsight, this envied system was as much a "house of cards" as a model for financial efficiency. In effect, a market-wide "run on the bank" occurred, with everyone hoarding cash and recalling debts. As President Obama explained, "In a climate of fear, banks were unable to replace their losses by raising new capital on their own, and they were unwilling to lend the money they did have because they were afraid that no one would pay it back." What's worse, the mayhem and commotion on Wall Street had infected Main Street.

Although there were numerous factors and forces that contributed to the economic recession, the effects emanating from the financial crisis were pivotal. Officially beginning in the fall of 2007, the economic recession that still plagues the U.S. economy is directly connected to the financial crisis in two different, yet united, ways. First was the negative impact upon the supply side of the economy. As the credit crunch intensified, banks ceased lending money to businesses. Even business with perfect credit histories and high credit rating began struggling to secure credit. Smaller businesses were even more affected by the freezing of credit because they often lacked a perfect credit rating or significant collateral. Even when businesses were not showing any signs of weakening or potential problems, banks were raising interest rates on loans for fear that their balance sheets were weakening. The result was a suffocation of business activity, and the start of a vicious negative feedback loop. President Obama accurately depicted the situation when he stated that; “suddenly businesses can't get credit, they start carrying back their investment, they start laying off workers, workers start pulling back in terms of spending,” and the negative feedback loop begins. Meanwhile, the demand side of the economy was also severely weakened due to the financial crisis. As businesses felt the squeeze form the credit crunch, they began firing workers and reducing salaries. Unemployment began to increase and consumer confidence decreased markedly. In addition, substantial declines in housing prices and a historic stock market collapse inflicted massive financial losses. American family’s wealth plunged nearly 18% in 2008 as U.S. households’ net worth tumbled by $11 trillion. Unsurprisingly, the worst single year decline in personal wealth, rising unemployment, and increasing pessimism resulted in a significant drop in demand for goods and services. Simply put, people stopped shopping. The result was another negative feedback loop. As Americans stopped shopping, businesses suffered further losses and were forced to lay off more workers, leading to even less consumer shopping. The financial crisis that had begun with the bursting of the housing bubble had quickly spread from Wall Street to Main Street.

The Response

With an economy in rapid recession and a financial sector on the verge of imploding, America was hastily confronted with the reality of an economic attack of historic proportions. Up till March of 2008, the crisis had not yet warranted a radical shift in the government’s policy ideology or methodology. The Bank of England had had to provide direct capital to a British bank, North Rock, but the notion of the Federal Government intervening in the U.S. banking sector was still incomprehensible. Quickly things changed. As Wall Street speculators began predicting that America's investment banks were overleveraged and under capitalize, they became the target of ruthless short sellers. The first target was Bear Sterns. Speculation that Bear was potential insolvent resulted in a massive decline in the stock price. Ironically, not until the stock was beat down did it become is trouble of insolvency. Nevertheless, by March of 2007 it became apparent that the government would have to act.

As Bear Stern speed toward obliteration, the Federal Reserve observed that the failure of Bear Sterns would pose a systemic risk to the financial sector. Designated as "lender of last resort," the Federal Reserve had always possessed the authority and ability to provide emergency funds to banks via the discount window. This power and service was one of the primary reasons for the Fed's creation and a vital function for maintaining stability in the early 1900's. What's more, the function of "lender of last resort" is not an uncommon power among central banks. The trouble for the Fed, however, was the Bear was not a bank holding company, but an investment bank. AS a result, they had no prior precedent or authority to provide Bear with capital. Nevertheless, it was clear that immediate intervention was necessary if a collapse of the banking system was to be avoided. On March 12, the Fed attempted to funnel Bear money through J.P. Morgan Chase. Instead of calming the smolders, this only stocked the flames. Two weeks later, and with Bear in imminent danger, the Fed arranged an emergency acquisition of Bear by Chase. To close the deal, the Fed agreed to form a separate limited liability company called Maiden Lane, which would purchase $30 billion of toxic assets Chase had inherited from Bear. In retrospect, the $30 billion was a paltry sum, but the obligation placed on the Fed to save Bear form bankruptcy and their willingness to implement radical policies to do so were telling of the coming evolution and renewal of economic security for America. To ensure the nation's economic security in the face of an evolved threat to the banking sector the Fed was forced to evolve its policy responses by stretching the traditional rules guiding its authority and introduce a few innovative policy tricks.

The near failure of Bear Sterns and the Fed's dramatic intervention into the market denoted the start of the crisis' epicenter and the government's national defense. America's financial system, once considered the pinnacle of financial innovation and efficiency, was now severely crippled and suddenly threaten the health and security of the entire economy. Banks and other financial intuitions were on the brink of insolvency. Businesses were sinking from worsening credit conditions and falling demand from consumers. Citizens were watching their retirement accounts disappeared in the stock market collapse, there house values plummet and the jobs vanishing. Suddenly the free-market solution of permitting crisis to runs its course was impossible. This was not a "run-of-the-mill" recession that would be ended by natural economic forces. Rather, this was a severe economic attack upon that warranted government intervention and response. The threat posed by a 21st century financial sector, which had greatly expanded in size, complexity and interdependence was looming large for the government and its people. Eerily similarities with the Great Depression were beginning to be made. This ominous and frightful sign introduced the possibility of a second Great Depression. *Laissez-faire* economic policies and the America ideals of limited government intervention were going to be disregard. This had evolved from a credit crunch and recession to an economic security threat that warranted a government response appropriate of national defense. America and its people were under economic attack.

At the front and center of this effort to combat the financial crisis has been the Federal Reserve. Normally, the Federal Reserve fulfills its mandate from Congress, achieving price stability and maximum unemployment, and its role as central bank by controlling the United States' monetary policy. By manipulating interest rates, the Fed attempts to control the pace of the economy to promote full employment and price stability. While this is conducted by intervening in the markets by buying and selling short term Treasury bills, the level of intervention is minimal. During the financial crisis, however, the Fed has drastically expanded its operations and consequently its balance sheet. It has provided direct capital to private banks, actively engaged in asset markets and profoundly reshaped the central banks role in the economy. What's more, the crisis has highlighted the need to strengthen and expand the Fed's scope of regulation and operations to maintain stability. Often criticized as a negative influence in the finical market and an impediment to financial innovation, during the financial crisis the Fed has been able to maintain stability and order, and in the process, demonstrated its vital significance in protecting economic security.

As the credit crisis began to intensify, and credit markets began to freeze, the Fed began responding using the standard method of decreasing the Federal Funds Rate. In response to the intensity of the credit crunch, the Fed slashed interest rates from 3.00% in March of 2008 to a target range of 0-0.25% by December 2008. This action was designed to provide liquidity and unfreeze credit markets. Although this rate cut was dramatic, it was not outside the realm of normal central bank activity. The lowering of interest rates in a recession was the text book response for stimulating consumption and growth.

Despite lowering the Federal Funds Rate to essentially zero, however, the credit crunch deepened and the crisis escalated. As Fed Chairman Ben Bernanke noted in his remarks at the National Press Club Luncheon on February 18th, 2009, “Conventional monetary policies, which focus on influencing short-term interest rates, have proven insufficient to overcome the effects of the financial crisis on credit conditions and the broader economy.” In response to the weak results of “conventional monetary policy,” the Fed began the process of “quantitative easing.” Simply put, quantitative easing equated to directly injecting capital into various credit markets and institutions. The financial system depends upon free flowing capital. When these markets stop functioning, the finical system suffers. By exchanging capital for less-liquid collateral in the commercial paper, money, and mortgage backed securities markets, the Fed tried to unfreeze credit markets. In addition, the Fed initiated the Term Asset-Backed Securities Loan Facility (TALF) and the Term Auction Facility (TAF). These programs provided short term funding to depository institutions in the form of collateralized loans. In addition, the Fed has provided billions of dollars in support to AIG, Citigroup, Bank of America and other financial institutions. As a result, the Fed’s balance sheet had ballooned to over $2 trillion, a fact that demonstrates the massive amount of liquidity the Fed has injected into the economy. This radical expansion of the Fed’s operations would once have been called authoritative and undesirable in a free-market economy. This is especially true for the Fed’s programs for purchasing long term treasury bills and MBS. Normally, engagement in these markets by the Fed would have been seen as an artificial fore that will negatively alter the market. In the face of the financial crisis, however, the intervention has been beneficial and necessary.

Often working in conjunction with the Federal Reserve, the Treasury Department has played a principal role in the battle against the financial crisis. Its actions also have demonstrated the government's decision to protect the economic security of the country at whatever cost, both financially and ideologically. Moreover, the programs spear headed by the Treasury have been the most opposed to the free-market ideologies and guided government policy before the crisis. The most extraordinary and historic of the measures taken by the Treasury has been the $700 billion Troubled Assets Relief Program (TARP). TARP , commonly referred to at the bailout of Wall street, was created as a drastic and radical measure to boost confidence in the financial system by shoring up the banking system and injecting capital directly into the banks in exchange for equity stakes. After the government elected not to save Lehman Brothers from bankruptcy, fearing it would create a moral hazard and send a bad message that the government would pay for the mistakes made by private companies, the financial sector tiptoed to the brink of financial annihilation. The shock wave sent by Lehman failing caused severe damage to the interconnected financial system. This was illustrated by the massive collapse in the stock market and increased speculation that major banks were insolvency. As Former Treasury Secretary Henry Paulson stated during his announcement of the policy,"there is a lack of confidence in our financial system – a lack of confidence that must be conquered because it poses an enormous threat to our economy. Investors are unwilling to lend to banks, and healthy banks are unwilling to lend to each other and to consumers and businesses."

As indicated by its name, TARP's original purpose was to relieve the banks of their "troubled" or "toxic" assets. The eventual execution of the program, however, was simply a direct capital injection into the banking system. In other words, a bailout of Wall Street. The government took an equity stake in nine of the largest banking intuitions in America, including J.P. Morgan, Citigroup, Bank of America, Wells Fargo, Goldman Sachs, Morgan Stanley, Bank of New York Mellon and State Street Bank. The Treasury hoped TARP would provide the banks with adequate capital to weather the storm and resume lending in the economy. Acting on the understanding that credit markets were frozen because banks were concerned with the balance sheets of other banks, TARP was intended to reassure banks that counterparties would not default. Regardless, the plain fact was that TARP amounted to subsidization and partial nationalization of the American's banking system. The government effective became an owner in the nine largest banks in America. Free-market ideals would have dictate that banks that made unwise decisions should fail. Traditionally the U.S. government has agreed. Each year numerous banks fail. Normally the government allows market forces to determine which institutions survive and which fail. But the breath and potential damage presented by the failure of these institutions was too great for the government to permit. For better or worse, these institutions had become too-big-to-fail. Had they been permitted to fail, the financial sector would have been left and shambles, and more importantly, the economic security of America, its business and its citizens would have been destroyed. The decision to use tax payer money to prop up the private banking sector was greeted with outrage and disgust, but the Treasury had little choice. In the shadow of economic securities evolution and renewed importance, the government felt compelled to act.

The final major component of the government's policy response to the financial crisis has been the American Recovery and Reinvestment Plan, also known as the stimulus package. Based on the Keynesian economic theory that government intervention and spending is required to revive an economy during a recession, the Obama Administration's nearly $800 billion stimulus seeks to stimulate the economy by creating jobs and providing tax cuts. In a recession, a Keynesian economist would argue, a negative feedback loop will create slack in the economy as investment and consumption decline. The only way to break this vicious cycle is through government spending. The current version of the stimulus plan includes a combination of short and long-term measures calculated to revitalize the U.S. economy. By providing tax breaks and creating jobs, the stimulus aims to promote private consumption and investment in the immediate future. President Obama argues that the stimulus also includes long-term investment measures that will ensure the future growth and stability of the economy. He describes projects involving education, infrastructure, transportation, energy, and health care, as critical investment in the future.

While the merits and potential benefits of the stimulus package have been fiercely debated, the protectionist and economic nationalist nature of the spending is undeniable. Government spending is inherently protection and nationalistic. This is personified by the "buy American" clause that was originally included in the plan. The purpose of a stimulus package is to revitalize and jump start a country's economy. By creating jobs and increasing government spending, a stimulus package hopes to increase private consumption and investment. The "buy America" clause that was purposed would have stipulated that goods and services being purchased by stimulus money would have to be spending on America goods and services. This makes perfect sense. If a stimulus package is to benefit a country, the money must go to its citizens and businesses. What's the point of spending tax payer funds if the tax payer is not going to reap the benefit? Yet this clause was met with strong opposition because it signaled protectionism and could have started international trade disputes. While this criticism is fair, it avoids the essential fact that a stimulus is only effective if the people in the country benefit. The U.S. stimulus is a deliberate attempt to step into the free-market and stimulate consumption and production of its citizens and businesses. Stimulus packages are inherently protectionistic. Any time government spends money it's a form of economic nationalism. For this reason, the size and scope of the U.S. package has demonstrated the government desire to protect the U.S. economy and maintain economy security.

Conclusion

On Sunday, March 15, during an exclusive interview with *60 Minutes* Federal Reserve Chairman Ben Bernanke stated that he foresaw a stabilizing of the economy and recovery beginning in 2010. "We'll see the recession coming to an end probably this year. We'll see recovery beginning next year. And it will pick up steam over time," Chairman Bernanke stated. Similar optimism was voice by President Obama two days earlier as he addressed the nation. Obama confidently declared, "if we are keeping focused on all the fundamentally sound aspects of our economy all the outstanding companies, workers, all the innovation and dynamism in this economy, then we're going to get through this. And I'm very confident about that." While both men's optimism was refreshing and somewhat reassuring, they each added a significant caveat to their optimistic prediction. In Chairman Bernanke opinion the economic recovery will only occur if financial markets and institutions are stabilized and return to normalcy. When asked when "does this end," the Chairman replied "It depends a lot on the financial system." He continued;

> "the lesson of history is that you do not get a sustained economic recovery as long as the financial system is in crisis. We've seen some progress in the financial markets, absolutely. But until we get that stabilized and working normally, we're not gonna see recovery. But we do have a plan. We're working on it."

What is particularly revealing in this passage is the Chairman's final line, "We're working on it." The Chairman is referring to the extraordinary efforts being implemented by both the Federal Reserve and Treasury Department with the goal of stabilizing the financial market and returning normalcy. Chief among these are the innovative credit programs designed by the Federal Reserve to provide liquidity to the financial system, the slashing of the Feds Fund Rate down to between twenty-five basis points and zero, numerous billion dollar capital injections for institutions as well as various other maneuvers undertaken. For President Obama, one of the keys to an economic turnaround is the effective implementation of the $789 billion stimulus package. In campaigning for the bill's passage, Obama routinely declared that the stimulus bill will create or save 3 million jobs, jump-start the economy and invest in the future so America's economy can continue to prosper.

Both President Obama and Chairman Bernanke predict America will experience economic recovery in the near future. However, as previously discussed, both believe that strengthening of the economy can only be achieved by the continuation of governmental support and action. This shared believe is immensely important and informative because although the cause of the financial crisis is debatable, the size and scope of the government's reaction is hard to deny. In fact, the U.S. government's remarkable response, both in terms of its monetary sum and unusual nature, has been as shocking as the crisis itself. During the past 18 months, not only has the U.S. committed massive amounts of funding to the U.S. economy, but it has completely dismissed the ideology of free-market capitalism and minimum government intervention. Eighteen months ago the government largest role in financial markets was through regulation and the Federal Reserve actions regarding monetary policy. Today, the government owns and operates the nation's two largest mortgage lenders, Freddie Mac and Fannie Mae. Through TARP, the Troubled Asset Relieve Program, and other capital injection actions the government has invested billions of dollars directly into the financial system, including over $40 billion injection into both Citigroup and Bank of America and over $180 billion to the American International Group (AIG) (Credit Crisis Bailout Plan). What's more, the U.S. government now possesses a 36% equity stake in Citigroup and 80% in AIG. Additionally, the Federal Reserve has drastically expanded its operations in the financial markets. Invoking emergency powers, the Fed has implemented various credit lending programs, such as the Term Auction Facility (TAF) and Term Asset-Backed Securities Loan Facility (TALF). Furthermore, the Fed has begun to purchase commercial paper and mortgage-backed securities. These actions have resulted in a tripling of the Fed's balance sheet and a radical change in the Fed's role in the economy.

Before the crisis erupted, the United States economic ideology prescribed a minimum amount of government intervention in the economy, both in the financial sector and private business. Government ownership of banks, subsidies to companies, bailouts, and other protectionist measures were discouraged upon. Yet during the current crisis the government has performed all of the both actions, and more. Bailouts, bank ownership, stimulus packages; these are all extremely protectionist and nationalistic measures, once reserved for economy's of the developing world. But why? What could have caused such a dramatic change in the economic ideology and strategy of the United States? Once a champion of free-market capitalism and limited government intervention, the U.S. has propped up an ailing auto industry, saved failing banks and pledge billions of tax payer dollars to a massive spending agenda. Obviously the reason for such dramatic action has been the financial crisis and economic recession. If neither of these events had developed, it's extremely doubtful we would have witnessed the expansion of government that has transpired. However, the financial crisis alone can't explain why the government acted as it has. The government could have decided not to intervene, let the financial crisis work itself out. The U.S. could have allowed AIG, Citigroup, GM and other companies to fail. The Fed could have stuck with only traditional monetary policy, instead of invoking emergency powers. The President did not have to enact an enormous stimulus bill using tax payer dollars. Yet all of these protectionist and nationalist actions were taken. Furthermore, the justification and reasoning for all of these actions was the same, economic security.

As previously stated, I consider a country's economic security to be a condition that results from the establishment and maintenance of protective measures that defend a country's economy integrity against economic hostility and attacks. What occurred during the financial crisis and economic recession was an economic attack upon the United States.

Comparable to any physical attack, the country was met with a hostile situation that threatened the protection and integrity of the economy. As the credit crunch intensified and the housing market continued to collapse, the financial sector and economic activity was exposed to greater risk. What's more, the speed and destructive power of the crisis illustrated the U.S. economy's economic insecurity. As pillars of the financial sector and economy began to fall, such as Lehman Brothers and GM, the vulnerability of the economy became all too evident. America was under economic attack and showing signs of rapid deterioration. Noticing the severity of the threat and fading economic security, the U.S. government was force to respond. In order to ensure the protection and integrity of the economy the government was compelled to establish and maintain these protectionist measures. Not since the Great Depression had the concept and importance of economic security been as apparent. Whether these measures have been effective can only be determined over time and by backward looking historian. Moreover, the debate about the justification and reasoning of the government's response will remain open to debate. However, it is clear that the light that the crisis has shed on the need for government to incorporate the concept of economic security into their understanding and planning of national security.

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