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The Right Roosevelt?

By David Ignatius
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There has been a lot of speculation about whether Barack Obama can be another Roosevelt, but I wonder if we're talking about the right Roosevelt. In fixing the financial crisis, Obama could use a little less of FDR's affection for economic giantism and a little more of TR's zeal for trust-busting.

This week's $30 billion supplementary bailout for insurance behemoth AIG is a case in point. Keeping this insolvent monster on life support doesn't make sense. The company should have been dismantled when the crisis first hit last year, when the healthy parts could have been sold for a decent price. Treasury says that after this latest bailout, AIG should shrink and remake itself in smaller pieces. Better late than never, I guess.

Even AIG knows it's too big. "AIG's conglomerate structure is too complicated, unwieldy and opaque," said Edward Liddy, the company's new chief executive, who came in last fall to try to clean up the wreckage. The tragedy is that this was clear a few years ago, and nobody did anything about it. A former regulator remembers that AIG's transactions were so tangled and incomprehensible that it couldn't close its books on time -- yet nobody thought to call a halt.

Treasury and Federal Reserve officials have continued to operate on the assumption that in finance, bigger is better -- and safer. The argument for these huge, diversified financial institutions has been that in pooling different kinds of risks, they would increase the portfolios' overall stability. That rationale helped create the monstrosity called Citigroup. It was like the argument for securitization of subprime mortgages -- put enough of them together and the danger of default would be less. That didn't work out too well.

And yet the authorities have continued to act as if greater size will provide greater stability. That was the rationale for pushing a healthy Bank of America to acquire a sick Merrill Lynch last fall. A better response to Merrill's sickness would have been to leach out the toxic assets and then encourage an orderly breakup of the brokerage firm; it was too big already.

A case study for today's regulators is President Theodore Roosevelt's response to the financial shenanigans of 1902, when the railroad barons tried to combine the Great Northern and Northern Pacific lines into a huge holding company called Northern Securities Co. Roosevelt wanted to file an antitrust suit to stop the deal. The financiers threatened that the lawsuit would cause a panic on Wall Street, to which TR's attorney general, Philander G. Knox, memorably replied: "There is no stock ticker at the Department of Justice."

When Roosevelt ignored the threats and moved to file the trustbusting suit, he received a hasty visit from J. Pierpont Morgan, the reigning financial titan. "If we have done anything wrong, send your man to my man and they can fix it up," offered Morgan. TR responded unflinchingly, "That can't be done."

Sad to say, but since this crisis began last year, Treasury and Fed officials have been rushing to "send your man to my man" to fix things up in hastily concocted weekend deals. The big financial trusts of our day have been threatening the regulators with ruin, and the regulators have been caving. They don't want another Lehman Brothers. But the authorities should have explored whether, as an alternative to failure, they could dismantle the giants into smaller, more manageable parts that could work their way to solvency.

Historian Walter Lord, in his 1960 book "The Good Years," wrote of Morgan and the other plutocrats: "These men were not naturally callous. They had no evil intent. But they had lost touch. The vastness of the operations, the complexity of their corporate structures kept them from their employees and the people they served." That's a perfect description of the executives at Citigroup, AIG and the other behemoths that brought the financial crisis down on our heads.

The Obama team has been lauded for emulating Franklin Roosevelt's bold response to the Great Depression of the 1930s. And as calls grow for nationalization of Citi and other giant banks, they may be tempted to go where even FDR feared to tread. But financial giantism -- private or public -- isn't the answer. The challenge is how to reconstruct our broken financial system. Let's give Franklin a rest for a while and ponder Teddy's progressive philosophy: When it comes to finance, smaller really is beautiful.

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