

# Fears Causing Fed to Play Favorites?

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By John Ketzenberger

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**Indianapolis Star** - The Bear Stearns bailout is either a rich-get-richer story or a case of calming market jitters so the little guy doesn't get hurt.

The answer depends on whom you ask.

**"The guys who take the most risk get bailed out and the little guy that got talked into taking out the subprime loan in the first place gets fried out in the process."**

**That's Mark Maddox's take. The attorney and former Indiana securities commissioner understands the rationale Federal Reserve Chairman Ben Bernanke used to broker the deal with JP Morgan Chase & Co. to take over Bear Stearns. "He did it because the next few days in the market would be absolutely bloody."**

**But Maddox doesn't like the notion that any company should be considered too big or too important to fail. "You can't have your cake and eat it too when it comes to capitalism," he said.**

Despite its liquidity crunch, Bear Stearns still had profitable business segments, said Matt Will, a finance professor at the University of Indianapolis.

"They should be forced to go bankrupt. They should be forced to live with the decisions they made," Will said. "You don't think somebody would step in?"

Bear Stearns put the subprime lending crisis on the front page last summer when two of its hedge funds, heavily invested in the risky loans, failed. Even though investors stand to lose billions, those who made the bad decisions essentially walk, thanks to \$30 billion in federal loan guarantees. "Apparently those who live by the sword don't have to die by it," Will said.

The reason is simple, said Tod Perry, associate professor of finance at Indiana University Kelley School of Business. "There was an overriding concern that we don't want to see what happens if Bear Stearns fails."

The "contagion effect," he said, could cause other financial institutions to fail. That could zap investor confidence and the already weak economy.

The same rationale was used when the hedge fund Long Term Capital Management failed in 1998. Then several investors pumped \$4 billion into the fund, ran it for two years, then cashed out with a nice profit.

"A firm with the ability to provide liquidity is in a position to make a very good profit,"

said Kenneth Carow, Kelly School associate professor of finance.

Since the overall market remained stable, it appeared the Fed averted "a potentially scary domino effect," said Mike Bosway, City Securities Corp.'s CEO.

Bosway is no fan of Bear Stearns, but kept a long-term perspective. "I'm not sure this is different than any other crisis we've had in the last 100 years," he said. "It was all precipitated by excess, which is reverberating through the financial system. The markets and the economy will find equilibrium again."

One thing everyone agreed on: there will be a lot more hair-raising turns before that equilibrium is found.