

In the Western, “Hang 'Em High”, a posse capture Jed Cooper, played by Clint Eastwood, and accuse him of rustling cattle and murder. Rather than bother with a trial, they decide to lynch Cooper on the spot. But the vigilantes made two mistakes. They hung the wrong man and they didn't finish the job. Cooper comes back as a marshal and gets his revenge.

As the crisis in global credit markets continues, a lot of people are saying that it's time for a hangin'. Although the origins of the crisis are far away in the subprime mortgage market in the United States, the effects of the turmoil are being felt by property markets around the world—especially here in Ireland. For starters, the slump in the US housing market may yet drag America's economy into recession. If that happens, our goose will be well and truly cooked, given our reliance on the US. In addition, the crisis has prompted a tightening of lending terms and standards. The days of a homebuyer being able to borrow an amount equivalent to ten times income are gone. The knock-on effects on the housing market are obvious. Loans to buy commercial property will also be harder to get.

It's not surprising then that financial commentators have put together a posse and got themselves some rope. What is surprising, however, is that the man that many are blaming for the crisis is my ex-boss Alan Greenspan, former head of the US Federal Reserve—America's central bank. What Greenspan's accusers are now saying is that he cut interest rates to inappropriately low levels in 2001 and held them there for too long. US monetary policy was far too lax between 2001 and 2004, they argue, and we're paying the cost today. I think they are making a mistake.

Let's start with the facts. The Fed slashed interest rates from 6½ per cent in late 2000 to just 1 per cent by mid-2003. The Fed began to tighten monetary policy in mid-2004, pushing interest rates back up to 5¼ per cent by mid-2006. Putting the critics in Greenspan's shoes, I wonder what they would have done differently.

When the Fed began to cut interest rates in early 2001, US economic growth had already plummeted to only 1 per cent from roughly 5 per cent in 2000. In the aftermath of the dot.com bust, investment was tanking and unemployment was rising. By late August 2001, interest rates stood at 3½ per cent, hardly an irresponsibly low level. Without monetary easing, the stock market crash would surely have induced a severe economic contraction.

And then 9/11 happened. Economic activity ground to a halt and the financial system seized up. Additional interest rate cuts were clearly needed to avert a financial crisis and avoid a deep recession. The Fed responded with four more cuts, lowering interest rates to 1¾ per cent by the end of the year. What would the armchair critics have done?

In 2002, growth picked up moderately. But by the fourth quarter of that year, the economy was about to stall, depressed by the effects of the corporate governance scandals, high oil prices, and blows to confidence stemming from the prospects of war in

Iraq. The labour market remained in the doldrums. Not exactly ingredients for a robust recovery. Did these shocks not merit a monetary policy response?

Meanwhile, the spectre of deflation (that is, falling consumer prices) had raised its ugly head. The rate of inflation slipped to below 1 percent in 2003. Japan's experience with deflation in the 1990s had served as a warning that an economy could become trapped in a downward spiral of falling prices and weakening spending.

The stimulus worked. Economic activity began to show signs of a sustained recovery in late 2003. The recovery in the labour market lagged the recovery in output, but the economy was showing enough vitality by mid-2004 for the Fed to begin monetary tightening.

Critics might argue that the strength of the economic recovery showed that Greenspan need not have cut interest rates as sharply as he did. But this is false logic. It is like saying that all the money spent on the Y2K problem was wasted because no major computer systems failed and no planes dropped out of the sky on 1 January 2000.

All told, those looking for someone to blame for the current credit crisis ought to be pointing the finger at someone else. At the subprime mortgage lenders in the US, perhaps, whose lending standards were abysmally low. Or at the subprime borrowers who took out mortgages that in many cases they had no hope of servicing. Or at the rating agencies that stamped "high-grade" on what were effectively junk bonds. Or at the investors who bought these bonds without fully understanding the risks involved.

In Alan Greenspan, the critics are surely rounding on the wrong man. And when his \$8.5 million memoir, "The Age of Turbulence", is released soon, I reckon the Maestro is going to have his revenge.

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