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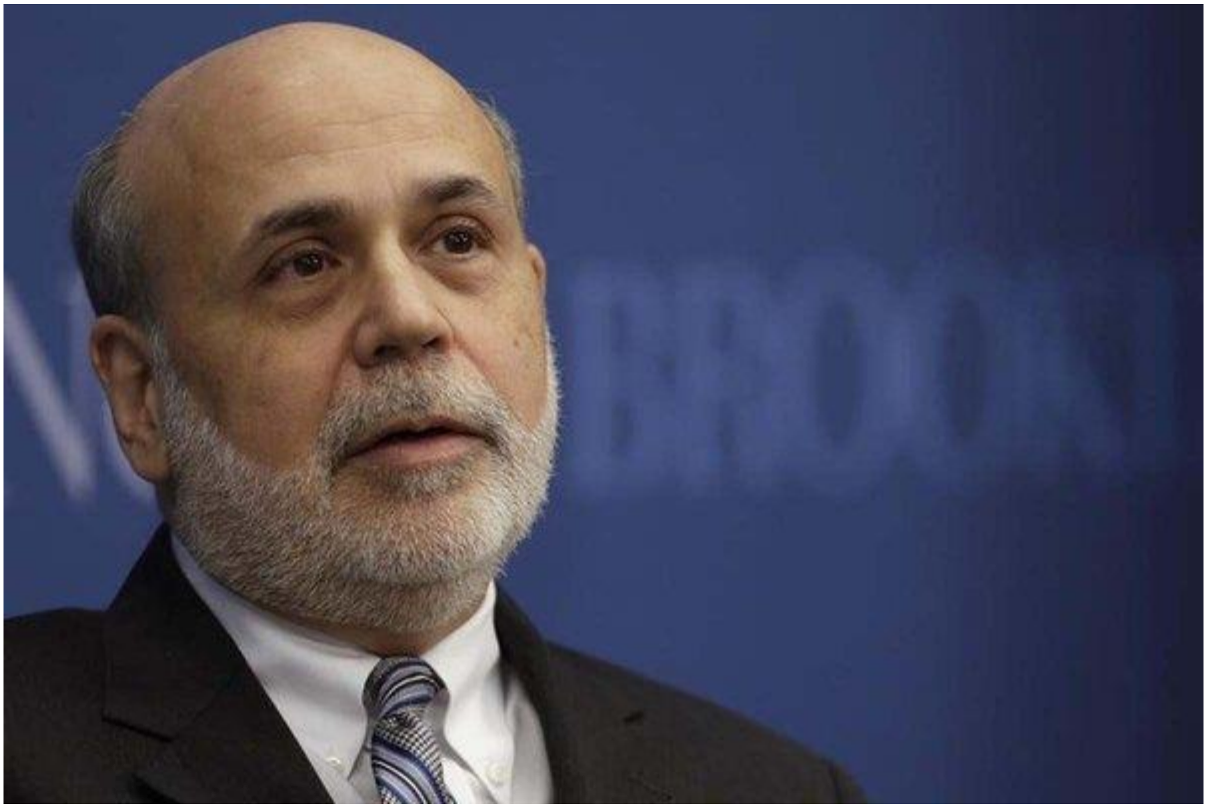

Ben Bernanke participates in a discussion at the Brookings Institution in Washington on Jan. 16, 2014. Gary Cameron / Reuters

Mr. Right

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Former Federal Reserve Chairman Ben Bernanke was due at the Philadelphia Free Library this weekend to promote his new book, and I was lucky to be chosen as his interlocutor. The book recounts his experiences running the central bank during the worst financial crisis and recession since the Great Depression.

We owe Bernanke much gratitude for his service. He was the right person, in the right place, at the most critical of times. His careful study of the Depression as a Princeton academic made him uniquely qualified to lead monetary policymaking through the near-collapse of the financial system and economy in 2008-09. Without his decision-making, our economy would be in a measurably worse place today.

A key dictum of central banking is to take bold steps in times of crisis. When banks are panicked and markets are seizing up, the central bank must respond with force. No one else has the ability or credibility to soothe jagged nerves.

In the weeks after investment bank Lehman Brothers failed, the Fed injected massive amounts of liquidity into the financial system. It opened the cash spigot not only to commercial banks, with whom it normally deals, but with a wide array of financial institutions.

The Fed also went way outside of its traditional box when it poured cash into commercial paper markets - where large nonfinancial firms borrow money short-term - and into asset-backed securities markets, where credit-card, auto-loan and student loans are financed. It also gave central banks across the world access to a lot more dollars that were in big demand by nervous financial institutions.

Policymakers provided this liquidity at a high interest rate, so that those institutions that took the Fed's cash quickly gave it back once the financial system stabilized. Most did so within a few months.

The Fed also spearheaded the bank stress-testing process. It was clear that most banks lacked the financial strength to withstand a serious financial crisis, and the stress tests were designed to figure out what the banks needed to ensure that they could. This is now part of normal bank practice, and the result is our banking system is as strong today as it has ever been.

Critics have argued that these actions bailed out Wall Street, and not only were bankers unworthy of help because they caused the crisis, but helping them also would only encourage more risk-taking.

There is truth in these sentiments, but, unfortunately, there was no way to save Main Street without rescuing Wall Street. If banks can't make loans, then businesses that need them have no choice but to keep cutting jobs. And it is hard to argue that bankers didn't feel the pain of their bad decisions, or that their takeaway is that they can take bad risks and not be penalized.

While the Fed's actions averted a collapse of the system, they weren't enough to spare the economy. The damage was serious, as millions of jobs were lost and unemployment soared to double digits.

The Bernanke Fed quickly dropped the interest rate it controls to zero, and started buying long-term bonds to reduce mortgage rates and the interest rates businesses pay when they borrow. This bond-buying, called quantitative easing or QE, while highly controversial, also has been very successful.

QE has lowered borrowing costs, and has been key to ending the housing crash and turning around house prices. It is also why stock prices have soared since the recession and, despite the recent correction, are still near record highs. This has lifted consumer spirits and their spending.

It is obvious that worries that QE would stoke runaway inflation have been misplaced; inflation remains too low for comfort. Others have argued that QE would create bubbles in financial markets, like the technology stock bubble. That hasn't happened, either.

The Fed didn't get it entirely right. Bernanke's decision not to save Lehman Brothers from failure arguably was the blow that triggered a deeper financial crisis. He argues that Lehman was insolvent, and the Fed is not permitted to lend to a failed financial institution.

This is a strained argument, since whether an institution is solvent depends on how its assets are valued, and that was impossible to do in real time during the crisis. Policymakers have this problem in all financial crises, and it's why historically they have shown mercy to "too big to fail" firms.

Fortunately, policymakers learned a lesson from this, and in the Dodd-Frank legislation that was passed in the wake of the crisis, there is now a clearer process for resolving troubled institutions. "Too big to fail" remains a problem, but not nearly as serious a one.

There will no doubt be future financial crises. It is human nature to take on risk, and ultimately too much risk. But we've learned some critical lessons. And there is no one better than Ben Bernanke to teach us those lessons.

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