EDITORIALS OF THE TIMES

Bailout Needs Some Clarity

A month into the Bush administration's $700 billion bank bailout, the effort has become as fractured as the ad hoc rescues that it was supposed to replace. As a result, the modest easing the bailout initially brought about in the credit markets is now being reversed over doubts about the Treasury's stewardship of the plan.

The rates for loans between banks have begun edging up again, and consumer borrowing costs are also up — that is, assuming consumers can find a bank willing to lend.

President-elect Barack Obama's transition team is reportedly planning how the new administration will better manage the bailout. But two months is a long time to wait while the Bush Treasury burns through the bailout billions, with little to show in terms of enhanced stability and even less in terms of enhanced confidence.

Recently Treasury Secretary Henry Paulson outlined a complex new bailout strategy intended to promote consumer borrowing. Mr. Paulson defended this latest iteration, saying he would never apologize for changing his approach as the facts change. But it is not surprising that everyone else is feeling confused.

Before the bailout even got under way in October, Mr. Paulson had to sideline his original strategy — to buy up banks' bad assets — because, he soon came to realize, it was too complex and indirect to deliver the swift jolt the financial markets needed.

He indicated that he would return to that strategy later, but to get the bailout started, he opted instead to directly invest $250 billion in the nation's banks. The about face was necessary, but it raised uncertainty about whether the Treasury really had a firm grasp of the problem — exactly what shaky markets don't need.

Since then, the doubts have grown, among investors and the public. Mr. Paulson invested the taxpayers' money on terms so lenient that banks have felt free to hoard it, or to buy other banks — while refusing to bolster lending to consumers and small businesses.

He has diverted another $40 billion of the fund to American International Group, the reckless insurance company that had already received $85 billion in federal assistance. If government officials know where all that money is going, they haven't shared their knowledge with the public.

Mr. Paulson disappointed investors by ditching the plan to buy up banks' bad assets. Instead, he expanded the bailout to include investing money in nonbank financial companies, like GMAC, the lending arm of General Motors, and the other carmakers' lending units. He also announced that the Treasury and the Federal Reserve were considering a plan to use taxpayer money to jump-start consumer lending via credit cards, car loans and student loans. The Fed quickly said the plan was still in early development.

The one approach Mr. Paulson stubbornly refuses to consider is using bailout money to help homeowners avoid foreclosure. His reasoning — that the money is to be used to stabilize the financial system — inexplicably ignores the fact that the instability he is seeking to quell is rooted in the housing bust.

Over the next two months, Mr. Paulson must impose some coherence and clarity on the bailout. Otherwise he will only fan anxieties and mistrust, which will undermine the effectiveness of his good decisions and amplify the fallout of his bad ones. With markets gyrating wildly, and the economy deteriorating rapidly, the nation needs clear leadership and a sound plan.