

Author who predicted crisis sees inflation ahead

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- * Author sees commodity cycle resuming after recession
- * Says Democrats as beholden to Wall St as Republicans
- * Taxpayer, small investor unprotected "and that's rotten"

By Daniel Trotta

NEW YORK, April 8 (Reuters) - An author who saw the global financial crisis coming fears the next bubble will come in the form of inflation and has little confidence U.S. President Barack Obama's team is up to the challenge ahead.

"The Democrats have replaced the Republicans as the big benefactors to the financial community," said Kevin Phillips, author of "Bad Money: Reckless Finance, Failed Politics, and the Global Crisis of American Capitalism."

"The financial community is donating more to Democrats than ever before and you've got more Democrats in the financial community, creating a very powerful pattern there. I don't think you're going to see the Obama administration and Congress willing to be tough enough in dealing with these things," he told Reuters.

Phillips, a former strategist in the Nixon White House who has turned highly critical of the Republicans and voted for Obama in 2008, published "Bad Money," his 13th book, a year ago.

The paperback edition came out March 31 with a revised preface and afterward, interpreting the events of the past year, but the prescient body of "Bad Money" remains unchanged.

A year ago, he warned of a the pending explosion of a 25-year "multibubble" that started in the 1980s, when the financial sector accounted for 10 percent to 12 percent of the U.S. economy and started metastasizing into an "arguably crippling" 20 percent to 21 percent by the middle of this decade.

Overleveraging and easy credit was bound to create disaster, he warned.

Phillips assigns much of the blame to former U.S. Treasury Secretary Henry Paulson, but perhaps even more on Federal Reserve Chairman Ben Bernanke, who he calls a "disaster," and his predecessor, Alan Greenspan.

Phillips calls Paulson a Wall Street insider who was looking out for his own and Bernanke an academic misguidedly trying to refight the 1930s Great Depression. Together they formed the wrong team at the wrong time whose ad hoc approach threw away hundreds of billions of dollars and more than doubled the Fed's balance sheet, he says.

"What you're seeing Bernanke do is he's trying to create a bailout reflationary bubble, which he can't describe as a bubble, just as Greenspan couldn't describe the housing mortgage bubble as a bubble. What we're seeing by Bernanke is a covert attempt to rebubble," Phillips told Reuters.

Moreover, a 10- to 15-year commodities cycle probably started early in this decade and is only being masked now by recession, Phillips says, presaging a repeat 1970s style inflation, he said.

"The danger is that the great unwind -- the unraveling of the mammoth buildup of debt -- is under way. If that predominates, Bernanke's theory is you're going to have deflation," Phillips said.

"My theory is that if we are in a commodities cycle, what you will get will be more like 1973-74-75 ... where as soon as the recovery begins you get rising inflation because you're going to play havoc with all money supply and liquidity that's been unleashed," he added.

Meanwhile, the taxpayer and small investor have little defense.

"The average person is going to be on the periphery of concern and I think that's rotten," Phillips said.

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