The Reckoning

- In 2006, the school board in Whitefish Bay, Wisconsin needed to figure out a way to fix the teachers’ retirement plan
- Financial planner suggested borrowing overseas in a complex plan with “guaranteed” returns
  - C.D.O – collateralized debt organization

The Reckoning

- The planner didn’t really explain the CDO process right
  - Schools’ money actually used as insurance on $20 Billion in corporate bonds
  - Registered in the Cayman Islands, & managed by Royal Bank of Canada, AGA in New York, & UBS in Switzerland

The Reckoning

- If just 6 percent of the debts went bad, the Wisconsin schools would lose all of their money
- If none defaulted, the schools would receive about $1.8 million a year

Intro to globalization

- The Reckoning – From Midwest to M.T.A., Pain From Global Gamble
- Duigg & Dougherty, Nov. 1, 2008
The Reckoning

‡ Depfa started out in 1922 as a little German bank
• In 2002 moved to Dublin to take advantage of low corporate taxes
• Became immensely profitable global bank with executives earning about $33 million a year in 2006
• Fueled by an arrogant CEO, Depfa and other European banks went for riskier deals

‡ The New York Metropolitan Transportation Authority (MTA)
• At the same time the Wisconsin schools were borrowing money from Depfa, New York Subway officials were encouraged to essentially take out variable rate loans

‡ Borrowed money at interest rates that changed every day

The Reckoning

‡ The New York Metropolitan Transportation Authority (MTA)
• Traditionally the MTA raised money by issuing simple bonds with fixed interest rates
• Bankers suggested the adjustable-rate loans
• But they would only be issued if a bank like Depfa would have to sign on as a “buyer of last resort”

‡ Worldwide, Depfa was the largest buyer of last resort in 2006
• As Depfa continued to grow, it needed more short-term loans to keep profitable
• Even so, CEO able to sell Depfa to the German owned Hypo Real Estate for $7.8 Billion

‡ His cut was $150 Million

The Reckoning

The investment started going bad in 2008
• Wisconsin School Districts’ investments were declining

‡ Would likely lose the full $200 million
• The schools would not be able to repay Depfa

‡ Crisis at the bank
  • Defaulting on these loans
  • Billions Depfa was borrowing to cover its own loans
‡ Depfa had a debt of $81 Billion

‡ Sept. 2008, US bank Lehman Brothers went bankrupt
• Short-term lending stopped
‡ Depfa in big trouble
• Hypo Real Estate received a $64 billion bailout from Germany
The Reckoning

Back to the MTA
• Had $3.75 Billion in debt
• Depfa problems = downgraded
• Investors dumped the MTA bonds
  ‡ Depfa had to buy $150 million worth

‡ But if Depfa bought bonds, the cities had to pay a higher interest rate!
• The MTA alone suddenly had a debt that could balloon by about $12 million a year
• This wouldn’t be a big problem if the economy was stable...
  ‡ But tax receipts are down with foreclosures, etc.
• MTA now faces a $900 million budget shortfall

Currently
• The MTA is exploring options to reduce debt
  ‡ Oct. 2011 debt was $32 mil.
• Other states and cities are facing similar problems
  ‡ California, Connecticut, Illinois, and South Dakota directly related to Depfa
  ‡ Florida, Massachusetts and Montana have had to cut budgets because of CDOs and similar risky investments
• Hypo Real Estate
  ‡ Now nationalized by Germany
• Wisconsin School Districts
  ‡ Suing the Royal Bank of Canada and Stifel Nicolaus investment firm for misrepresentation

The Reckoning

So What is Globalization?
Main concepts
• Deterritorialization
• Interconnectedness
• Speed of society
• Inevitable (?)

Deterritorialization
National boundaries & distances are seen as increasingly irrelevant to economics and communication
• The Internet was crucial for such a globalized world to exist

Interconnectedness
‡ Almost cliché to announce that geography is dead & we no longer need nations...
‡ We are connected to what happens in the world
Speed of society

The speed at which we communicate & interact is a necessary component to globalization

- We are increasing the pace of life and overcoming spatial barriers

Speed of society

The result is "time-space compression"

- As time required to connect two places is reduced, space is "compressed" or "annihilated"
- This alters our everyday experiences and makes us more connected to the world

Dependence

‡ Flights cancelled from Eyjafjallajokull eruption

Inevitability

‡ The natural outcome of capitalism?
‡ Removing government barriers to allow free markets to flourish?

McDonaldsization?

‡ Globalization does not mean that we live in a homogeneous world of chain stores
- Globalization is a social force, but it should not be confused with creating a placeless society
New Means of Production

Fordism → Post-Fordism

Fordism

‡ 1920s - 1970s
‡ Multinational manufacturing corporations
  • Headquarters in the country of origin
  • Used plants that they owned in other parts of the world

Post-Fordism

Just-in-time inventory
Not maintaining an extensive inventory of raw materials or components
‡ Saves on warehouse costs, improves employee productivity

Post-Fordism

Outsourcing
• Rather than own manufacturing capabilities, contract with other factories
• Multiple factories supply the same parts

Post-Fordism

Outsourcing
• Rather than own manufacturing capabilities, contract with other factories
• Multiple factories supply the same parts

Post-Fordism Examples

Nike
• Does not own a single manufacturing plant
• Contracts with 900 factories & 660,000 workers in more than 50 countries
• Legal/ideological alibi for dangerous labor conditions, low wages, & anti-union practice?
The World is Flat

Thomas Friedman’s 2005 book
• Level playing field
• Technology advances = national boundaries aren’t as important to economic success
• Flattening refers to the increasingly connected supply chains

The World is Flat

Friedman is a supporter of globalization and thinks it’s a positive step
• Many people see such leveling as being “the apex of democracy”
• The US needs to accept globalization rather than grumble about it.

The World is Spiky

Richard Florida
• Physical location is still very important
  ‡ Yes, globalization means Indian workers can handle US phone support
  ‡ But ‘the second, less obvious side to globalization is the tendency for higher-level economic activities such as innovation, design, finance, and media to cluster in a relatively small number of locations.’ (Who’s Your City, p. 19)

The World is Spiky

So it does matter where you live
• Major cities in the world are still the place of innovation and economic development
The Power of Place

"Earth may be a planet of shrinking functional distances, but it remains a world of staggering situational differences."

Texas reported 64 cases of dengue fever. 3 Mexican states bordering Texas reported 62,514 cases.

† Windows screens & air conditioning rare on the Mexican side, making it easier for mosquitoes to spread the disease.
‡ Availability of medical services too

Greece’s debt bigger than GDP

- Credit rating lowered – struggles to pay bills with higher interest rates
Instructor: M. Pesses

Greek Crisis

Contagion Effect
- Spreads to rest of EU?
  ‡ Portugal, Spain, Italy & Ireland

Greek Crisis

Loans
- April, 2010 – Germany, IMF

Greek Crisis

‡ Collaborative effort to cut Greek debt by over 50%

2010-2011 Austerity measures
- Reduce deficit by more than €10 billion ($13.7 billion).
- Raised taxes on fuel, tobacco and alcohol
- Raised the retirement age by two years
- Public sector pay cuts
- New tax evasion regulations.
Getting Tense

Prime Minister Alexis Tsipras
- Germany should pay reparations to Greece for the crimes of Nazis.
- Will seize German assets in Greece

Germany suggested
Greece pays for Alexander the Great