Globalization is the Greatest Reorganization of the World Since the Industrial Revolution.

Globalization affects all our lives and will be of even greater significance to our children and grandchildren.

These three excerpts were released in in light of the global financial crisis. These snapshots reinforce the fundamentals that we precicted would lead to the crisis, and the basic prescriptions needed to move forward.

Please send any additional information or links you would like to contribute to the widely referenced Web site: <u>www.mkpress.com/Flat</u>

> Ms. Scottie Jacob sjacob@mkpress.com

The World is Flat?

A Critical Analysis of the New York Times Bestseller by Thomas Friedman

Ronald Aronica Mtetwa Ramdoo

Excerpts:

Debt and The Financialization of America America's Former Middle Class A Paradigm Shift for America

> For more information and readings visit: www.mkpress.com/Flat To Receive Periodic Updates (usually quarterly) Send email to info@mkpress.com with Subject: Flat Updates

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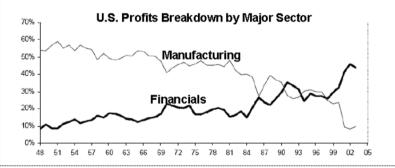
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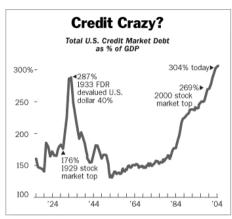
4. Debt and The Financialization of America

Globalization has an underbelly that Friedman chiefly ignores. Globalization isn't just about what serf-like wages in China and India are doing to America, it's also about what American transnational corporations and neoliberals are doing to Americans, or more precisely what deregulated media and financial services companies are encouraging Americans to do. That is consume, consume , consume —no matter what—and do it on credit.

It's called "financialization," a state where financial services becomes the dominate component of a nation's gross domestic product (GDP). Economics commentator, Kevin Phillips defines financialization as a process whereby financial services, broadly construed, take over the dominant economic, cultural, and political role in the national economy. Phillips writes, "Part of what propelled financial services were the profits gained from providing American households with artificial purchasing power—the loans that many took out to splurge on consumption or to restore income levels they could no longer attain from shrinking manufacturing or back-office wages."¹ Here's what it looks like in the U.S.



Source: Bridgewater Associates



Source: Clapboard Hill Investment Partners; Barron's Magazine

In 2004, total credit market debt reached 304% of America's gross domestic product. In 1980, Americans collectively saved 7.4% of national income, by 1990, it had fallen to 4.5%, and in 2005, the savings rate went negative!

In "Debt and Denial," New York Times columnist and economist, Paul Krugman, wrote, "Last year America spent 57 percent more than it earned on world markets. That is, our imports were 57 percent larger than our exports.

"How did we manage to live so far beyond our means? By running up debts to Japan, China and Middle Eastern oil producers. We're as addicted to imported money as we are to imported oil. But this time our overseas borrowing isn't financing an investment boom: adjusted for the size of the economy, business investment is actually low by historical standards. Instead, we're using borrowed money to build houses, buy consumer goods and, of course, finance the federal budget deficit.

"In 2005 spending on home construction as a percentage of G.D.P. reached its highest level in more than 50 years. People who already own houses are treating them like A.T.M.s, converting home equity into spending money: last year the personal savings rate fell below zero for the first time since 1933. And it's a sign of our degraded fiscal state that the Bush administration actually boasted about a 2005 budget deficit of more than \$300 billion, because it was a bit lower than the 2004 deficit.

"It all sounds unsustainable. And it is."

Consider the remarks of Paul Volcker, Former U.S. Federal Re-

serve Bank Chairman, on April 10, 2005, "Under the placid surface [of the economy], there are disturbing trends: huge imbalances, disequilibria, risks—call them what you will. Altogether the circumstances seem to me as dangerous and intractable as any I can remember, and I can remember quite a lot."²

Deregulation of the financial services industry is one part of the growing neoliberal power structure in the United States, and the growing financialization of the country. And it starts at an early age in one's life. In "Don't Leave College Without It," Taylor Loyal wrote, "Jon Selden never had a credit card before he went to college. But a few weeks after arriving at Brigham Young University, he received an offer mailed to his dorm room for a preapproved Citibank card. Before Selden even managed to find a job or establish a credit history, he was running up thousands of dollars in debt.

"Credit card companies like Citibank aren't the only institutions profiting from student spending. Like other colleges and universities across the country, Brigham Young has done a lucrative business with big lenders, enhancing university revenues at the expense of students. BYU received an estimated \$70,000 last year in exchange for stuffing offers for Citibank cards into 1 million shopping bags at the university bookstore. The University of Tennessee has a sevenyear, \$16.5 million deal with First USA that gives the company the names and addresses of alumni, employees, and more than 40,000 students. The University of Michigan and Michigan State have struck similar deals with MBNA, the self-proclaimed 'world's largest independent credit card issuer,' worth an estimated \$14 million.

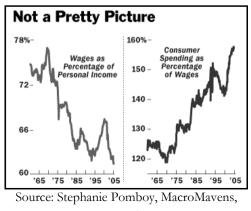
"By the time Jon Selden graduated from Brigham Young last year, he had accumulated \$8,000 in debt. Now enrolled in law school, he lives with his parents and waits tables rather than filing for bankruptcy. 'Was I stupid to run up that debt?' says Selden. 'You bet. But I was 18.' Selden may have been stupid, but others ended up less than stupid.

"Every major university also has students burdened by massive debts that they have little hope of paying off. Sean Moyer, a National Merit Scholar, racked up more than \$12,000 on 12 credit cards while enrolled at the universities of Oklahoma and Texas. In 1998, even though he was working two jobs to pay off the cards, he believed his debt would prevent him from attending law school. 'He just said he felt like he was a failure,' recalls his mother, Janne O'Donnell. Nine days after confessing his fears, the 22–year-old Moyer hung himself in his bedroom closet." ³

In "A New Domestic and Global Strategy," Thea Lee writes, "The United States is running a current account deficit of more than \$700 billion a year to fund consumption we can't afford. This is not financially sustainable. Meanwhile, many workers in developing countries work twelve to sixteen hours a day, in dangerous conditions, without the right to form an independent union, at poverty pay, so that transnational corporations can boost their bottom line. That is not politically sustainable.

"That the national debt is currently over \$8 trillion is only the tip of the iceberg. There has also been an explosion of corporate debt, state and local bonded debt, international debt through huge trade imbalances, and consumer debt (mostly in the form of credit-card balances and aggressively marketed home-mortgage packages). Taken together, this present and future debt may exceed \$70 trillion."⁴

In his blog,⁵ Barry Ritholtz, Chief Market Strategist for Ritholtz Research, wrote, "The remorseless decline in wages as a percentage of personal income has reached an historic low of 62%. Meanwhile, consumer spending as a percentage of wages continues to spiral upward. In the past three years, Stephanie Pomboy of MacroMavens reckons, shop-happy consumers, cheerfully determined to live beyond their means, leaned a lot more heavily on borrowings (\$675 billion of non-mortgage debt) than paychecks (\$530 billion) to cover the \$1.3 trillion increase in their spending. This may be great while it lasts, but it cannot go on forever. Trigger points for stopping America's consumption spree include higher interest rates, record-high gasoline prices and the rising cost of just about everything. And then, or course, when foreign lenders decide they are holding too many dollars, all hell could break loose as 'free money' disappears."⁶



Baron's; April 25, 2005.

In *The Indebted Society*, economists James Medoff and Andrew Harless advance the argument that as debt burgeoned in the 1980s, it also realigned political power. When debt becomes more important in society, lenders become more important, making them more powerful. They then tend to influence policy, and today's deregulated financial services companies are free to entice debtors with low interest rate consolidation packages, and then jack up interest rates to *usury* levels after the first late payment. By 2005, household debt reached such high levels that it triggered the enactment of tough new federal bankruptcy laws—to protect lenders, not debtors. We now have what economists Noriel Roubini and Brad Setser have coined as "the borrower-industrial complex," led by credit-card companies and other lenders that have grown up around ever-more desperate borrowers and their ever-growing needs.

In April, 2004, Brett Arends of *The Boston Herald* attended a private presentation to a select group of fund managers, by Stephen Roach, the chief economist at Morgan Stanley. In his report on the presentation, Arends wrote that Roach predicted, "America has no better than a 10 percent chance of avoiding economic Armageddon."

"To finance its current account deficit with the rest of the world, he said, America has to import \$2.6 billion in cash. Every working day.

"That is an amazing 80 percent of the entire world's net savings.

"Sustainable? Hardly.

"Meanwhile, he notes that household debt is at record levels. Twenty years ago the total debt of U.S. households was equal to half the size of the economy. Today the figure is 85 percent.

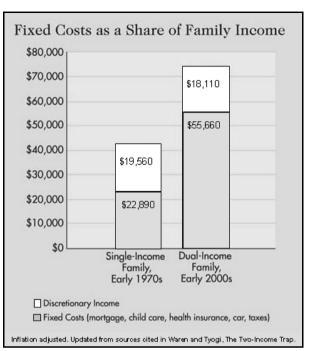
"Nearly half of new mortgage borrowing is at flexible interest rates, leaving borrowers much more vulnerable to rate hikes. Americans are already spending a record share of disposable income paying their interest bills. And interest rates haven't even risen much yet."⁷

Although Friedman largely ignores the debt "externality," debt and the financialization of America are indeed menacing aspects of his flat world. And if Roach is right, these issues cannot be ignored much longer.

5. America's Former Middle Class

Congressman Bernie Sanders, the only Independent in the House of Representatives, reflects a growing concern about globalization and America's working families, "The decline of the American middle class is not just one of the issues out there. It is *the* issue in the United States today. In terms of its impact on middle income and working families, there can be no debate that our unfettered free trade policy is an unqualified disaster. Millions of jobs have been lost. Wages are being pushed lower. Fringe benefits are being scaled back significantly. American workers are being forced to compete with desperate workers living in countries with very little political or economic rights who are paid as little as \$0.20 an hour. Free trade with the U.S. also lowers the standard of living for workers abroad as well, as demonstrated by the Mexican experience under NAFTA. The big Money interests are delighted. Working Americans are deserted and they know it."⁸

In "The Middle Class on the Precipice," in *Harvard Magazine*,9 Harvard's Elizabeth Warren writes, "Why are so many moms in the workforce? Surely, some are lured by a great job, but millions more need a paycheck, plain and simple. In just one generation, millions of mothers have gone to work, transforming basic family economics. The typical middle-class household in the United States is no longer a one-earner family, with one parent in the workforce and one at home full-time. Instead, the majority of families with small children now have both parents rising at dawn to commute to jobs so they can both pull in paychecks.



"Today's family has no margin for error. There is no leeway to cut back if one earner's hours are cut or if the other gets sick. There is no room in the budget if someone needs to take off work to care for a sick child or an elderly parent. The modern American family is walking a high wire without a net. Income risk has shifted in other ways as well. Incomes are less dependable today. Layoffs, outsourcing, and other workplace changes have trebled the odds of a significant interruption in a single generation. The shift from one income to two doubled the risks again, as both Mom and Dad face the possibility of unemployment. Their basic situation is far riskier than that of their parents a generation earlier. If anything—anything at all goes wrong, then today's two-income family is in big trouble."

In "The Collapse of the Middle Class," Rep. Sanders summarizes that flattening, "The corporate media doesn't talk about it much, but the United States is rapidly on its way to becoming three separate nations.

"First, there are a small number of incredibly wealthy people who own and control more and more of our country. Second, there is a shrinking middle class in which ordinary people are, in most instances, working longer hours for lower wages and benefits. Third, an increasing number of Americans are living in abject poverty going hungry and sleeping out on the streets.

"There has always been a wealthy elite in this country, and there has always been a gap between the rich and the poor. But the disparities in wealth and income that currently exist in this country have not been seen in over a hundred years. Today, the richest 1 percent own more wealth than the bottom 95 percent, and the CEOs of large corporations earn more than 500 times what their average employees make. The nation's 13,000 wealthiest families, 1/100th of one percent of the population, receive almost as much income as the poorest 20 million families in America.

"While the rich get richer and receive huge tax breaks from the White House, the middle class is struggling to keep its head above water. The unemployment rate rose to a nine-year high of 6.4 percent in June 2003. There are now 9.4 million unemployed, up more than 3 million since just before Bush became President. Since March 2001, we have lost over 2.7 million jobs in the private sector, including two million decent-paying manufacturing jobs—ten percent of our manufacturing sector. Frighteningly, the hemorrhaging of decent paying jobs is now moving into the white-collar sector. Forrester Research Inc. predicts that at least 3.3 million information technology jobs will be lost to low-wage countries by 2015 with the expansion of digitization, the Internet and high-speed data networks.

"But understanding the pain and anxiety of the middle class requires going beyond the unemployment numbers. There are tens of millions of fully employed Americans who today earn, in inflation adjusted-dollars, less money than they received 30 years ago. In 1973, private-sector workers in the United States were paid on average \$9.08 an hour. Today, in real wages, they are paid \$8.33 per hourmore than 8 percent lower. Manufacturing jobs that once paid a living wage are now being done in China, Mexico and other low-wage countries as corporate America ships its plants abroad.

"With Wal-Mart replacing General Motors as our largest employer, many workers in the service economy not only earn low wages but also receive minimal benefits. Further, as the cost of health insurance and prescription drugs soar, more and more employers are forcing workers to assume a greater percentage of their health care costs. It is not uncommon now that increases in health care costs surpass the wage increases that workers receive—leaving them even further behind. With the support of the Bush Administration many companies are also reducing the pensions they promised to their older workers-threatening the retirement security of millions of Americans.

"One of the manifestations of the collapse of the middle class is the increased number of hours that Americans are now forced to work in order to pay the bills. Today, the average American employee works, by far, the longest hours of any worker in the industrialized world. And the situation is getting worse. According to statistics from the International Labor Organization the average American last year worked 1,978 hours, up from 1,942 hours in 1990—an increase of almost a week of work. We are now putting more hours into our work than at any time since the 1920s. Sixty-five years after the formal establishment of the 40-hour work week under the Fair Labor Standards Act, almost 40 percent of Americans now work more than 50 hours a week.

"And if the middle class is having it tough, what about the 33 million people in our society who are living in poverty, up 1.3 million in the past two years? What about the 11 million trying to make it on a pathetic minimum wage of \$5.15 an hour? What about the 42 million who lack any health insurance? What about the 3.5 million people who will experience homelessness in this year, 1.3 million of them children? What about the elderly who can't afford the outrageously high cost of the prescription drugs they need? What about the veterans who are on VA waiting lists for their health care?

"This country needs to radically rethink our national priorities. The middle class is the backbone of America and it cannot be allowed to disintegrate. We need to revitalize American democracy, and create a political climate where government makes decisions which reflect the needs of all the people, and not just wealthy campaign contributors. We need to see the middle class expand, not collapse."

Bye, bye, Miss American Pie, drove my Chevy to the levee but the levee was dry.

A Paradigm Shift for America

As Thomas Paine wrote in December 1776, "These are the times that try men's souls. The summer soldier and the sunshine patriot will, in this crisis, shrink from the service of their country; but he that stands it now, deserves the love and thanks of man and woman. Tyranny, like hell, is not easily conquered; yet we have this consolation with us, that the harder the conflict, the more glorious the triumph."

Today's politicians and policymakers still work from a globalization mindset largely in place since the end of WWII. Few have updated their thinking around the assumptions underpinning Ricardian theories where economies of scale and the free flow of labor and capital were not part of the equation of comparative advantage. We find ourselves trying to solve today's problems with solutions that largely created the problems inherent in twenty-first century globalization. The time has come for a paradigm shift, for the world has changed.

Whatever the answers, we all need to understand far better the forces of twenty-first century globalization. America leads today, but the foundations of its leadership were forged out of the aftermath of WWI when America was the only fighter left still standing. Turning to Wikipedia for a quick recap, "The U.S. held a majority of investment capital, manufacturing production and exports. In 1945, the U.S. produced half the world's coal, two-thirds of the oil, and more than half of the electricity. The U.S. was able to produce great quantities of ships, airplanes, vehicles, armaments, machine tools, and chemicals. The U.S. also held 80% of gold reserves and had not only a powerful army but also the atomic bomb.

"As the world's greatest industrial power and one of the few nations unravaged by the war, the U.S. stood to gain more than any other country from the opening of the entire world to unfettered trade. The U.S. would have a global market for its exports, and it would have unrestricted access to vital raw materials.

"The U.S. was not only able, it was also willing to assume this leadership role. Although the U.S. had more gold, more manufacturing capacity and more military power than the rest of the world put together, U.S. capitalism could not survive without markets and allies. William Clayton, the assistant secretary of state for economic affairs, was among myriad U.S. policymakers who summed up this point: 'We need markets – big markets – around the world in which to buy and sell.'

"The 1944 Bretton Woods Conference established and set forth the rules of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), now the World Bank, and provided for a system of fixed exchange rates. The rules further sought to encourage an open system by committing members to the convertibility of their respective currencies into other currencies and to free trade.

"The chief features of the Bretton Woods system were an obligation for each country to adopt a monetary policy that maintained the exchange rate of its currency within a fixed value – plus or minus one percent – in terms of gold; and the ability of the IMF to bridge temporary imbalances of payments. In the face of increasing strain, the system collapsed in 1971, following the United States' suspension of convertibility from dollars to gold. Until the early 1970s, the Bretton Woods system was effective in controlling conflict and in achieving the common goals of the leading states that had created it, especially the United States. Today, the World Bank and the IMF continue, but their role has changed in many ways, although still greatly influenced by special interests in the United States."

But now it is time to fast-forward to today and the decline of U.S. hegemony. The U.S. is no longer the dominant economic power it had been for almost six decades. As Clyde Prestowitz wrote, "Maintaining a unipolar, hegemonic leadership is out of the question. It is no longer possible nor desirable for the long-term welfare of Americans. But there is much America can and should do to mitigate the impact of wage competition, maintain the promise of opportunity at the heart of the American Dream, provide for a continually rising standard of living more equitably distributed, and continue to influence the course of global affairs.

"The first step is to recognize that there is a problem. America needs to realize that many of the assumptions guiding its economic policy are at odds with the realities of today's global economy. Its performance in a broad range of areas—including savings, education, energy and water conservation, critical infrastructure, R&D investment, and workforce upskilling—is far below the standard of many other nations. America needs to understand that its refusal to have a broad competitiveness policy is, in fact, a policy. And it gives leading U.S. CEOs no choice but to play into the strategies of other countries. This policy, according to its proponents, leaves decisions to the unseen hand of the market. Actually, however, it leaves them to highly visible hands of lobbyists and foreign policy makers. It is a policy that ultimately leads to impoverishment'¹⁰

The time has come for an American competitiveness strategy and policy—a paradigm shift in our thinking that correlates to the realities of twenty-first century globalization. Such shift in mindset must include recommendations from some of the thought leaders on globalization. Here's a sampling:

- 1. Establishing a Federal Competitiveness cabinet position;
- 2. Providing universal health care;
- 3. Establishing a viable wage for all;
- 4. Providing education subsidies, not farm subsidies;
- 5. Providing world-wide education via the Internet;
- 6. Reducing the Federal deficit;
- 7. Fostering increased savings, e.g., with automatic 401K plans;
- 8. Reducing U.S. consumption and increasing it in Asia;
- 9. Ending the dollar hegemony at a new Bretton Woods-style conference;
- 10. Energizing energy efficiency;
- 11. Upgrading the U.S.' infrastructure, e.g., water, telecommunications networks, rail, etc.;
- 12. Having government govern corporations versus the reverse as it is today;
- 13. Establishing true economic unions, not asymmetric trade agreements;
- 14. Establishing tripolar trading blocs, not American unipolar hegemony;
- 15. Reforming and strengthening the IMF, World Bank, and WTO to incorporate "fair" trade;
- 16. Separating public goods (the commons) from private goods;
- 17. Developing smart, gas-sipping cars and alternative fuels for them;
- 18. Rethinking and reorganizing America's sprawling suburbs;
- 19. Revising the Tax Code, e.g., consumption and value added taxes;
- 20. Globalizing health care, e.g., being able to spend Medicare dollars overseas;
- 21. Attracting and keeping foreign talent; and
- 22. Developing a U.S.-China energy/ecology/technology project to help protect the planet.

This book would be hundreds more pages in length if we expounded on these strategies and their rationales. So we turn that task over to our *Essential Reading List* in the next section of this book, where you'll find discussions and insights by Stiglitz, Prestowitz, Fingar, Sheth, Sisodia and others.

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