

The Global Real Estate Bubble Is Beginning To Blow

by Helga Zepp-LaRouche

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If a patient shows symptoms of acute sickness in several critical organs at the same time, a radical operation is required, or else soon any solution will be too late. The current situation of the world financial system can be described in these terms.

It takes the same approach to deal with the apparently totally different problems of the real estate market bubble; the threatening bankruptcy of the whole American auto sector; the enormous difficulties in reaching a compromise on the European Union (EU) budget; or finding a solution at the Hong Kong summit of the World Trade Organization (WTO): They are expressions of the ongoing collapse of the system of globalization.

For the first time ever in post-war German history, a so-called “open-ended property fund” was closed on Dec. 13. The fund, named “Grundbesitz Invest,” had 300,000 investors and belongs to DB Real Estate, Deutsche Bank’s real estate subsidiary. Its total capital amounts to 6 billion euros, invested mostly in commercial buildings, of which two-thirds are located in Germany. The fund’s capital had already shrunk significantly in the recent few years.

On Dec. 9, DB Real Estate announced that, due to the need for an overall “re-evaluation” of the real estate owned by Grundbesitz Invest, the fund would no longer accept new investors. According to immediate market rumors, the “re-evaluation”—which could last until February—would likely result in a value write-off of 10% or more. Because shares in open-ended property funds can be traded freely, the prices of such shares dropped precipitously by 10%. On Dec. 12 and 13,

several thousand investors of Grundbesitz Invest withdrew all their capital, so that the fund was running out of cash. At that point, it was closed.

Why would Deutsche Bank take such measures, and risk creating a panic in the entire real estate market?

The leader of the German financial supervision agency BaFin, Jochen Sanio, raised the alarm by demanding daily information on any German public real estate fund, concerning capital inflows and redemptions. Deutsche Bank claims that it had informed BaFin in time. However, it was leaked to the media that BaFin officials are upset about Deutsche Bank’s decision, and are demanding an explanation by Deutsche Bank head Josef Ackermann. German legislation allows the closing of such a fund only under “extraordinary circumstances.”

Lyndon LaRouche commented on the situation as follows: “The damage is already done. The problem lies in the fact that all the banks are in a situation similar to that of Deutsche Bank. They will have to handle this very quickly. This should not come to the point of panic. We find ourselves at a point where the entire system can collapse. We must admit that this crisis is also in effect at Freddie Mac and Fannie Mae in the U.S. The fact that the real estate bubble in Loudoun County, Virginia is beginning to collapse, is part of this same picture.”

Global Repercussions

The case of Deutsche Bank has ominous implications for the entire financial sector. The financial press has for months been concerned about the global real estate bubble being on the verge of an immediate collapse. But the size of this bubble in Germany is much smaller than, for example, in the United

States, Great Britain, Australia, or Spain. There has already been a stepwise devaluation of up to 20% in the real estate sector. But if now the unsecured investors should also pull their investment out of other funds, they could shake the prices in the real estate market still further downward.

Then the question of the effects on the hedge funds, which in recent times have proceeded wildly to buy up everything in sight: *Mittelstand* [small and medium-sized] enterprises, houses, apartments, office space, castles, simply everything, comes onto the table. And these hedge funds are operating, on the other hand, on an international basis and in all directions, and even if the situation comes to a relatively less “blown-out” result in Germany, the effect on the international scene could be a chain reaction.

BaFin head Sanio briefly expressed his concerns at one of the conferences organized by Goldman Sachs earlier in 2005, saying that the question of an explosion of the hedge funds was not a question of “if,” but only a question of “when,” and his nightmare was that no one was prepared for this catastrophe.

Above all, the real estate speculation exposes how much the whole system is built on sand, or papier-mâché. Because the investors are not simply people who want in some way to realize the dream of a single family house, but are people who invest in these funds in order to get the highest possible profit, whether those profits cohere with reality or not. So, Deutsche Bank Real Estate had to already put the sale of shares into another of their funds, the “Grundbesitz Global,” because the investor interest was so large that no more rentable properties could be found.

In the United States over recent years there has been no such problem. Because the building regulations usually allow unrestricted growth and have maximum speculation as their objective, over the last years literally millions of so-called “McMansions” have sprung up out of the ground. In this way homes are put up in a couple of weeks, with walls of papier-mâché, but with several hundred square feet of living space and golden faucets in the bathrooms, houses which are many times overvalued as luxury villas, often saddled with two or three mortgages. If the situation is now approaching a collapse in real estate prices—which is inevitable—many of these people will be left with mortgages which are many times more expensive than what the real estate will then be worth.

EU Expansion Crisis

Simultaneously, the European Union summit in Brussels showed that the whole concept of EU expansion under the current policy of the Maastricht Treaty (1992), the regulatory changes of the Treaty of Amsterdam (1997), the budgetary and investment constraints on EU member economies imposed by the Stability Pact (1999), and the European Currency Union cannot function without political union. The wage differential among the ten new EU members in relation to the core countries, for example, means a difference of 6 to 1,

which makes admission of these countries into the euro-zone absolutely impossible.

Because the whole concept of Maastricht, which amounted to intentionally weakening the German economy and making Germany into the paymaster of Europe, has now led to their bad intention boomeranging. Germany has been milked to the limit of its capability. Great Britain will not give up its “British rebate,” France needs its farm subsidies, the new Eastern countries want their part of a shrinking pie. The only reason the EU summit didn’t collapse, was that all the problems were put off until 2008.

But also the WTO summit, which took place a few days later at the other end of the world, with 149 states participating, had to fail. The reason simply lies in the fact that globalization always thrusts the majority of the world’s population—and that majority now lives in the poorer countries, especially in the Southern hemisphere—further into poverty, and therefore there already arose at the earlier WTO summits, such as the last one in 2003 in Cancun, an unbridgeable conflict between the supposed interests of the so-called industrial nations, and those of the other countries.

If one now takes into account the threatened insolvency of the American auto sector and the dramatic consequences of globalization in Europe (AEG, Conti, Telekom, and so forth), then only a blind man could overlook the fact that not only a few real estate funds have fallen into a pit, but the whole system of globalization as well. If a building does not have stability, then the balcony hangs down after a while, and breaks off, as the roof is broken through, the windows break, and finally the whole construction collapses.

Thus, there can only be one conclusion: We need another, better construction of the world order. We need re-regulation of prices and markets, the protection of the common good and the social state. If the United States turns back again to the better tradition of the American Revolution, as this is signified by the dramatic change in the Democratic Party, therein lies the point of orientation. President John Quincy Adams developed the idea of an alliance of sovereign republics, which are bound together through the common interests of mankind. These concepts go back to the thought of Nicholas of Cusa and Leibniz. In this spirit, we must put on the agenda the question of a new financial architecture and a just new world economic order, before it is too late.

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