

What can cultural economic
sociology tell us about market crises

Constitutive Approach (Markets Are Culture)

- Calculative agencies
- Creation of commodities
- What makes Liquidity

Attention to the
cultural constitution of
markets

Complementary Approach (Markets Have Culture)

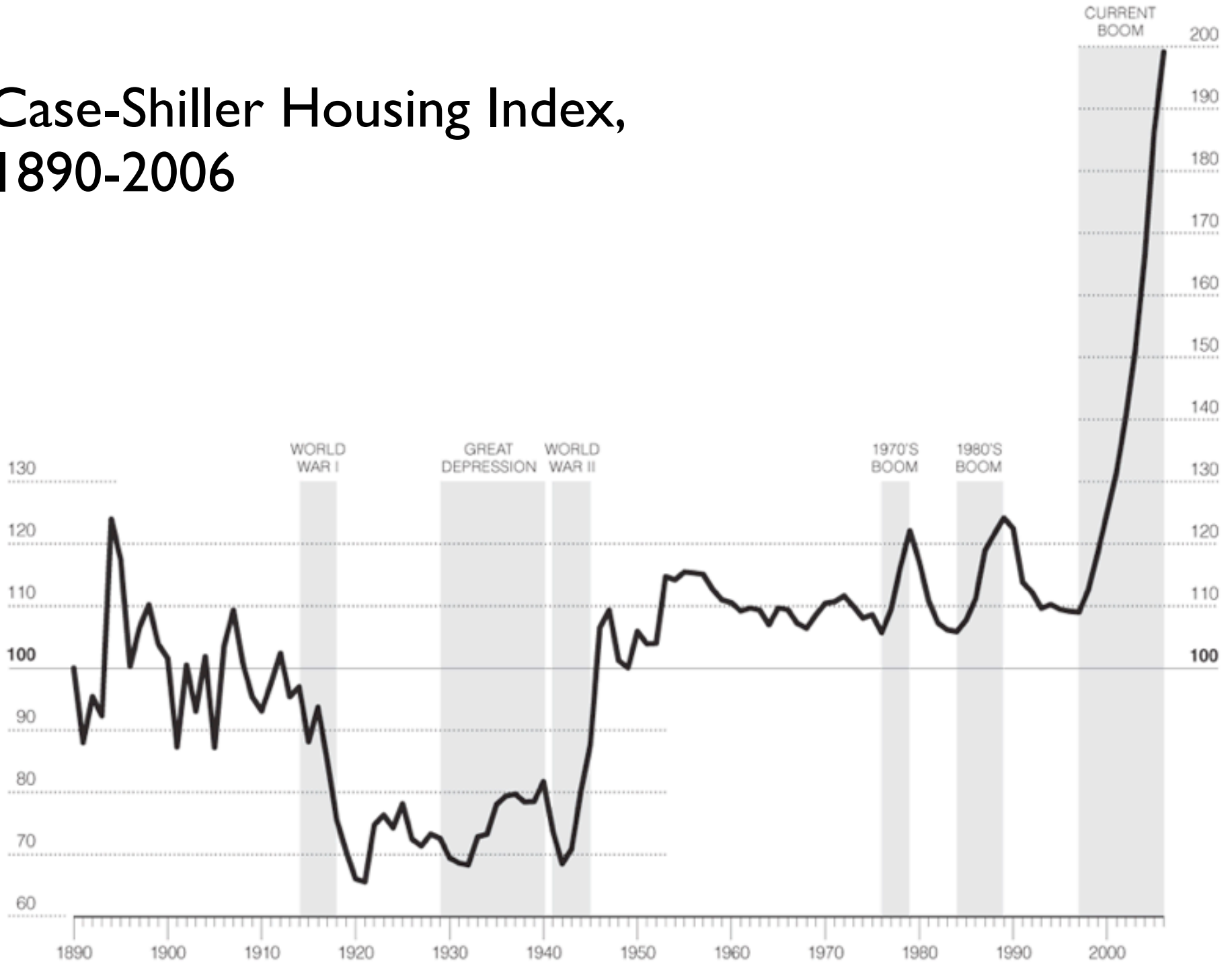
- Network effects on volatility and price
- Market identities over 'economic man'
- Political culture affects market development

Extends study of markets
by adding sociological
variables

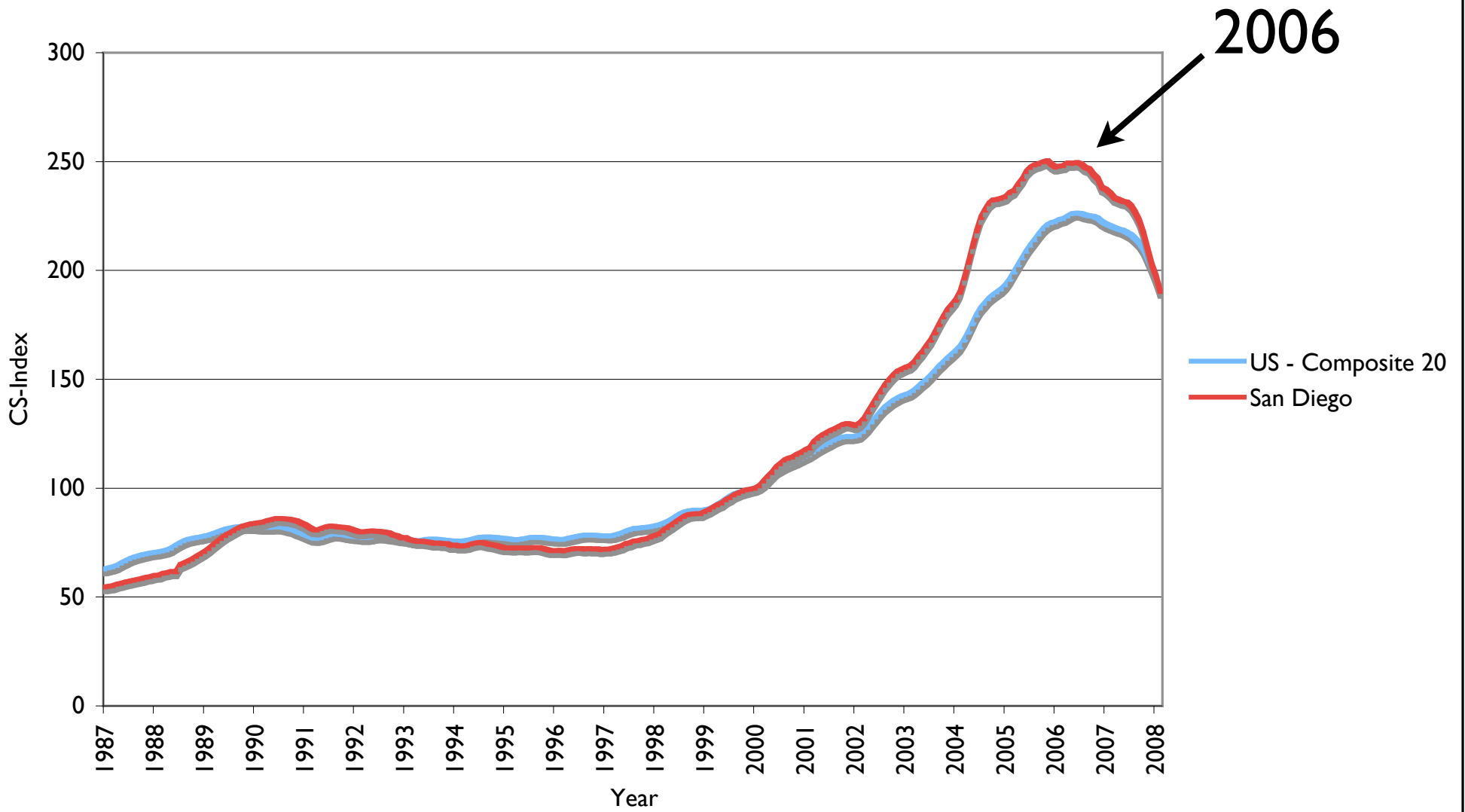
Analyzing the sub-prime crisis:

What do these two
approaches do for us?

Case-Shiller Housing Index, 1890-2006



Case-Schiller Index for US (20 Urban areas) and San Diego, 1987-2008



Bank Losses Linked to Sub-prime Derivatives

Merril Lynch	\$23.0 billion
UBS	\$18.4 billion
Morgan Stanley	\$10.8 billion
Citigroup	\$17.4 billion
Bank of America	\$5.1 billion
HSBC	\$3.4 billion
Bear Stearns	\$2.6 billion

Bank Losses Linked to Sub-prime Derivatives

Total loss estimates range from \$300-\$600 billion, up to \$945 billion, with 40% of losses from derivatives market.

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Collateralized Mortgage Obligations (CMOs) are Securitized Mortgages

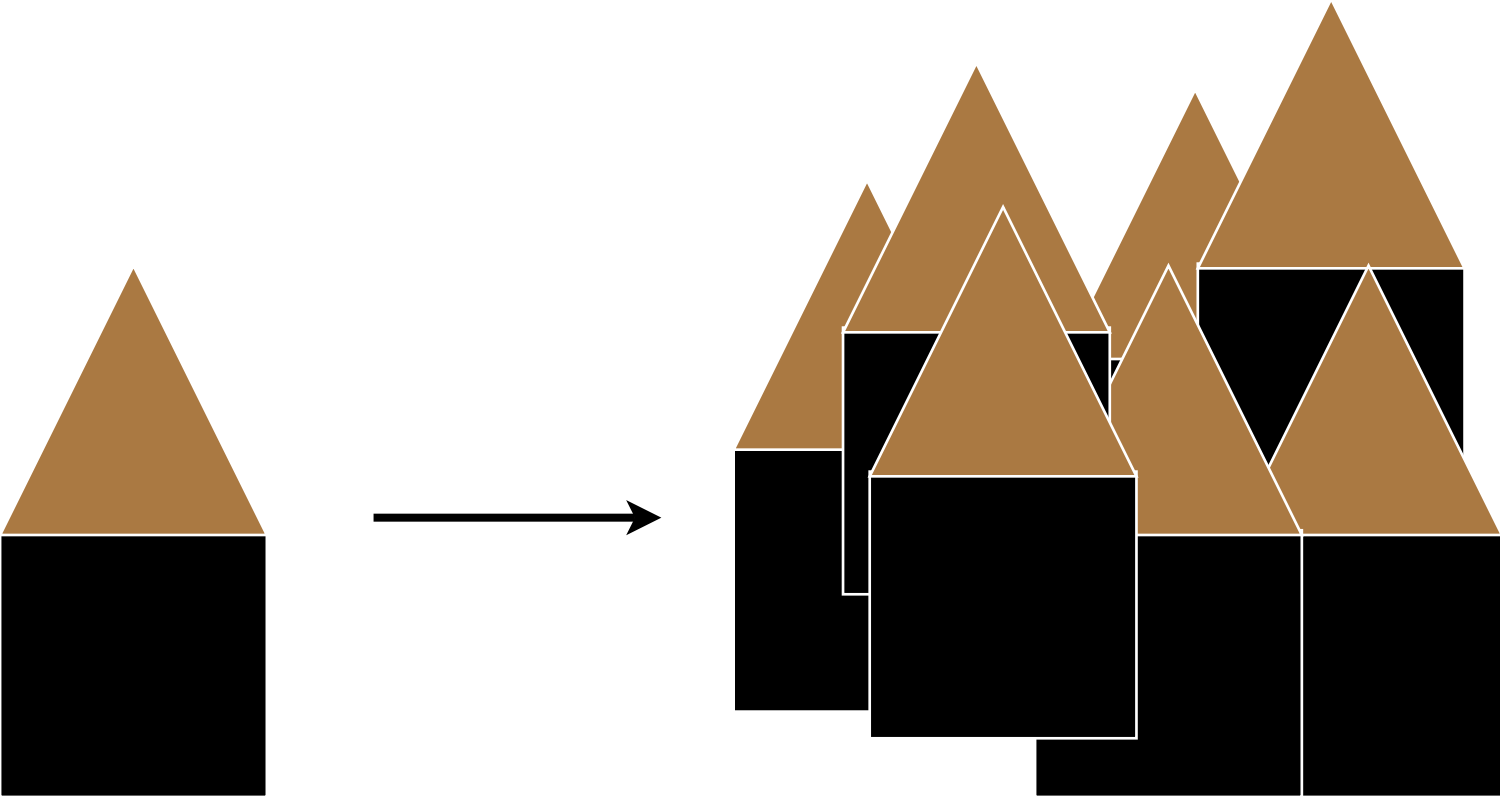
Bank lends you money to pay
back over 30 years (mortgage)

Collateralized Mortgage Obligations (CMOs) are Securitized Mortgages

Risks:

1. You will default (credit risk)
2. Money will become cheaper (interest rate risk)
3. You will 'pre-pay' (time risk)

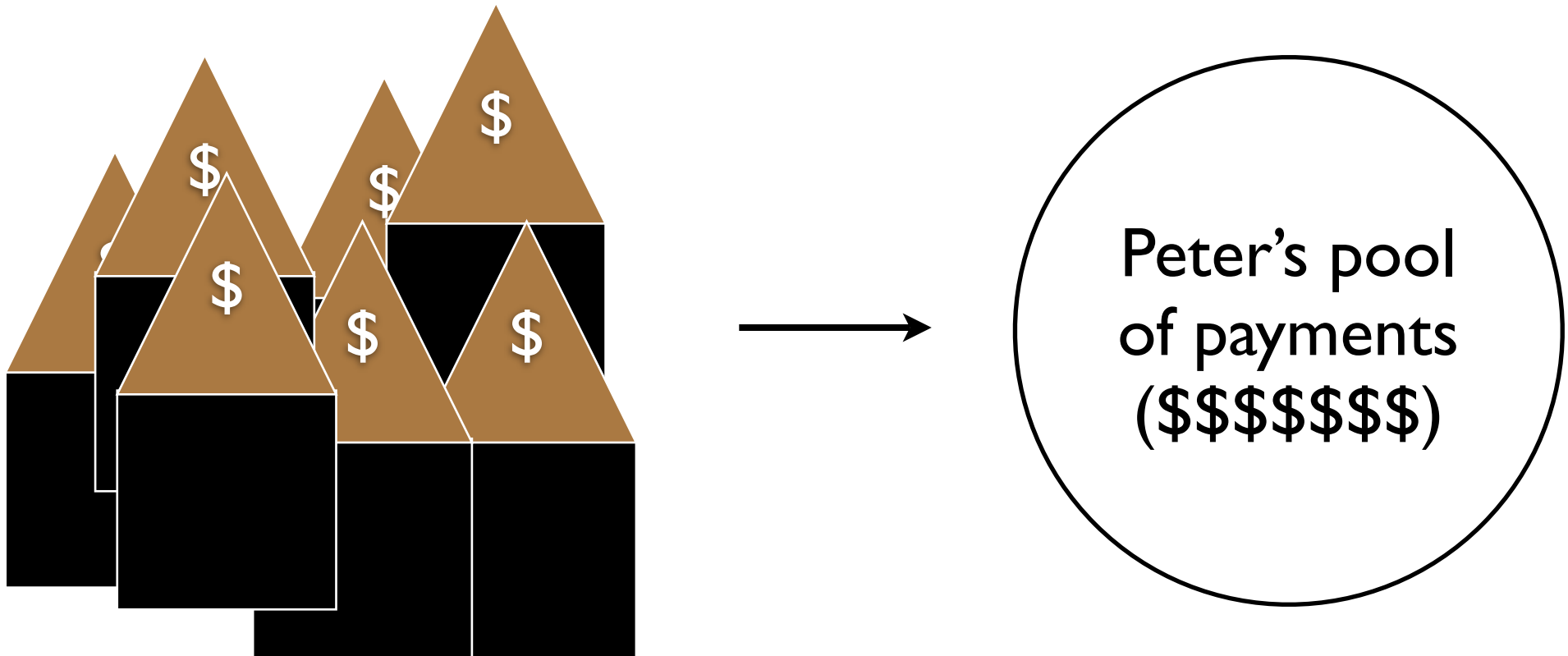
Banks don't want the hassle (but want fees)



$n=1$

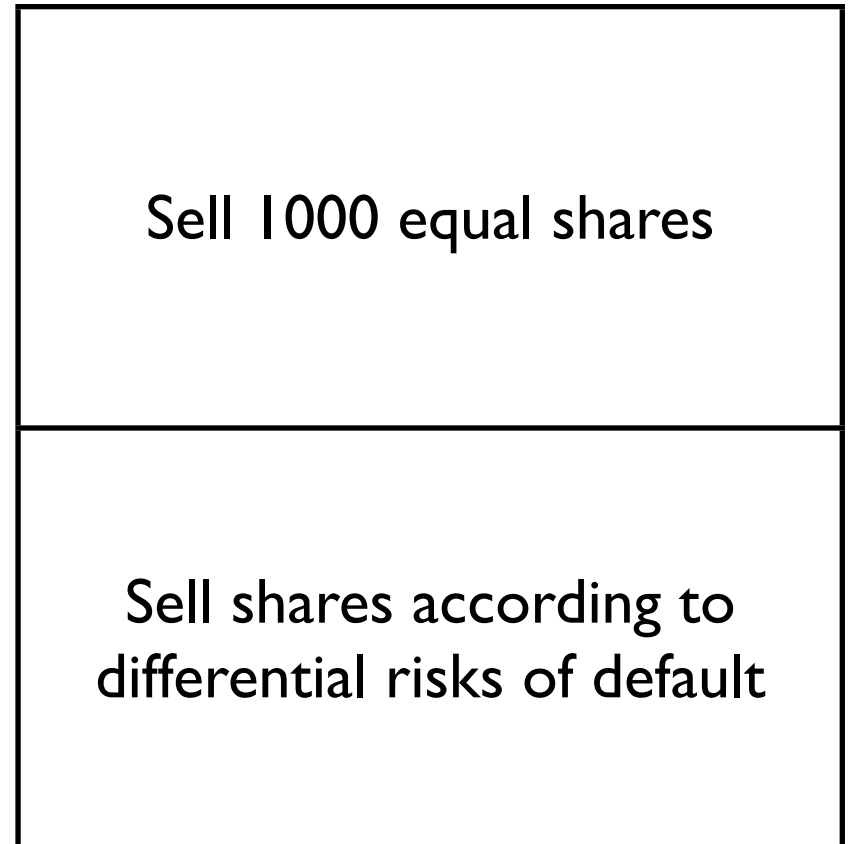
Pooled mortgages

Enter Fannie Mae

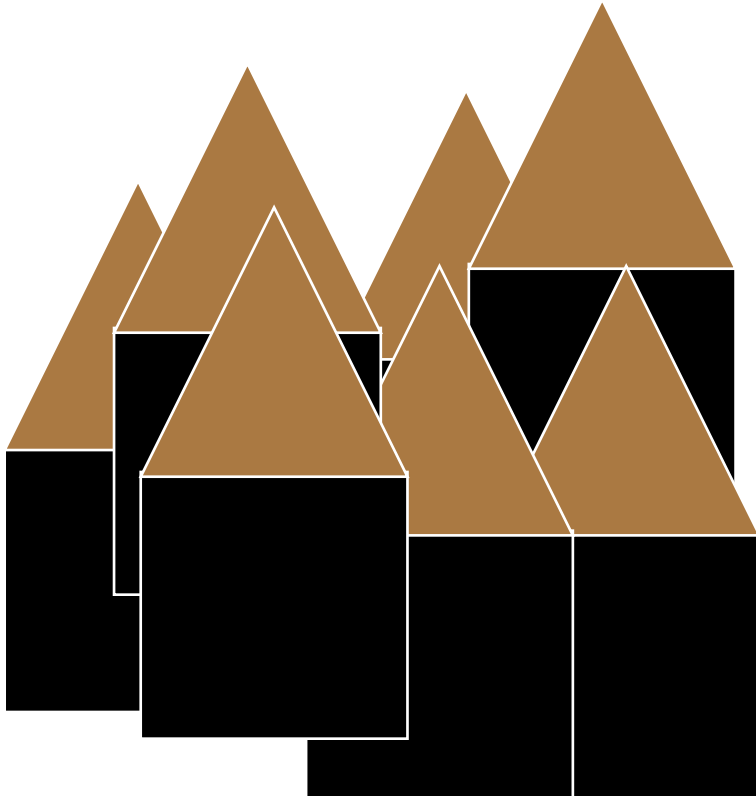


These entities (PPP) comprise
Collateralized Mortgage Obligations.
They can be sold to investors.

CMOs can be Sliced and Diced



But what happens after the fall?



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Tier 1: Get their money first

Tier 2: Get their money
second

Tier 3: Get what's left

Markets Are Culture

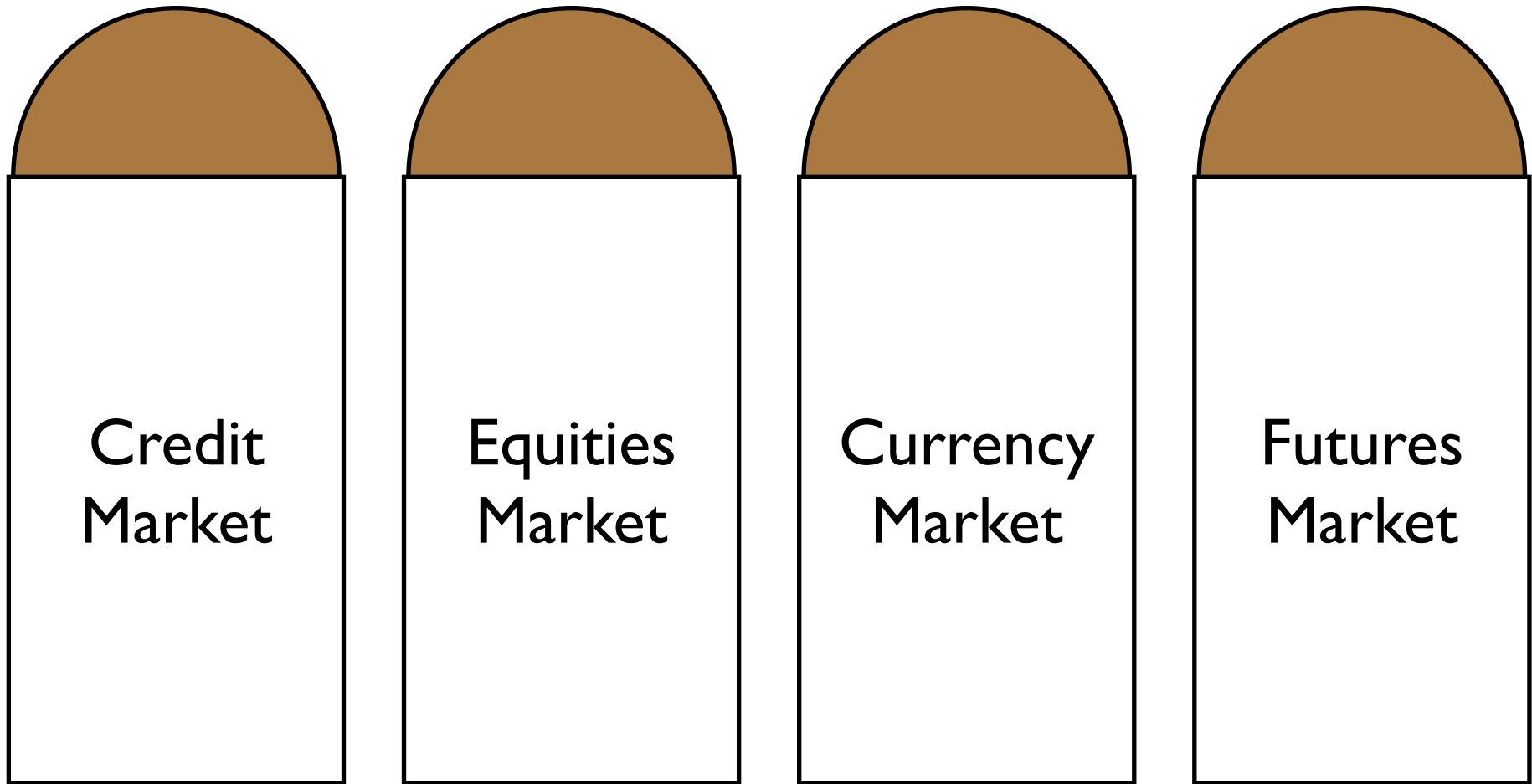
Markets Have Culture

CMOs are thoroughly modern products

1. Made possible by a technical infrastructure
2. Only priceable with intensive modeling

A new commodity: risk

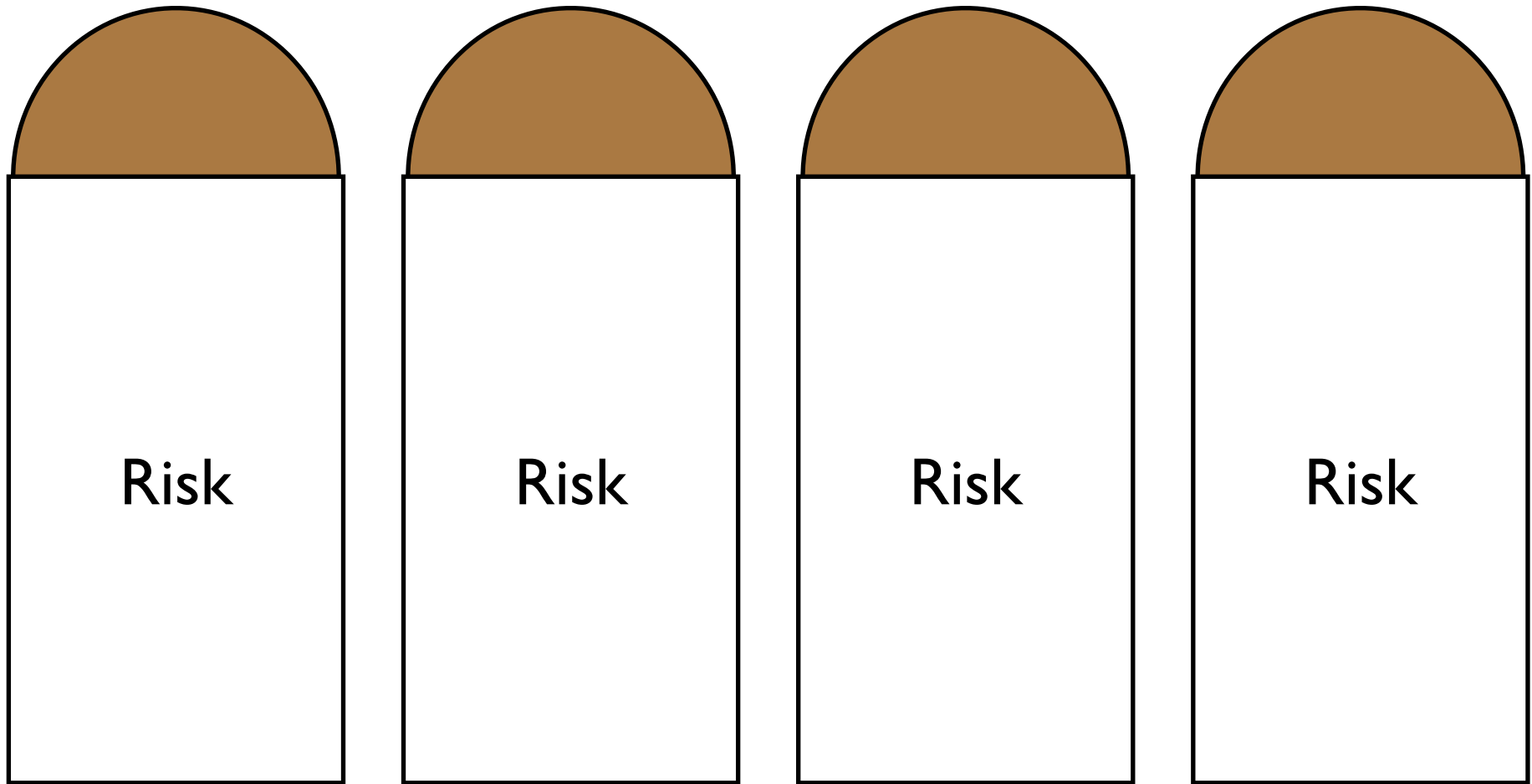
Historically, markets were silos



Electronic Trading

New technologies link across markets and exchanges

Now markets only appear as silos



Now everyone is trading the same thing...

Equities positions and credit derivatives used to be two distinct corners of global financial markets

Shift towards multi-dimensional strategies

... and everyone is trading the same way

Statistical Arbitrage
(fundamentals, reversion towards a mean)

Black Box Trading
(pattern recognition of risk opportunity)

Markets Are Culture

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A new commodity: risk

Markets Have Culture

Global financial markets no longer carry 'diversified' risks

1. Electronic Trading links markets and exchanges
2. Trading strategies have become isomorphic

A new systemic risk

The new object in financial markets (risk), leads to a change in the operation of markets (market linkages), which leads to new forms of incalculable, systemic risk

Systemic Risk

Bear Stearns' Losses
were \$2.6 billion

Systemic Risk

Value of their underlying positions
(notional value) was \$13.4 trillion

Systemic Risk

Top 10 investment banks are counterparties to 90% of trades in the global credit markets

Crises in Markets



Crises of Markets