**The prevention of the international impact caused by rapidly spreading economic bubbles.**

Economic and Financial Committee

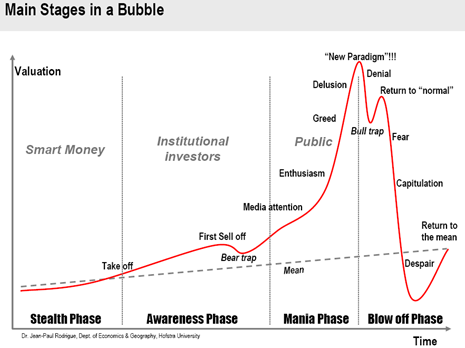
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**What is an economic bubble**:

An economic or speculative bubble is defined as an economic cycle characterized by rapid expansion followed by a contraction.

This cycle is characterized by a surge in the market caused by speculation regarding a commodity which results in an explosion of activity in that market segment causing vastly overinflated prices. Bubbles occur when excess money flows into an asset or asset group causing its price to rise beyond a reasonable level.



**The Global Economy is facing speculative bubbles threats**:

In the world history many economic bubbles have burst. Since 1621 the global economy have suffered from over thirty bursting speculative bubbles. The most recent and destructive one is known as the “Housing Bubble” burst in 2008 in the United States and it was the trigger of the world financial crisis. Even though the national economies affected by the crisis have started a slow growth process, many are the threats that countries have to be worried about.

Recent financial turbulences have affected ten of the most important stock markets of the world; not only USA, but also equity markets in China, Japan, Brazil, India, Russian Federation, Germany, United Kingdom, France and Italy have lost capital inflows.

**Global impact of Chinese crisis:**

Last year was a milestone in Chinese economy: in 12 months, Chinese stock markets rose enough to create $6.5 trillion of value. No stock markets in history have ever grown so much in one-year period. Some call this the world’s largest stock market bubble since the “dot-com” boom in 1990s

On June 12th 2015, the Chinese stock market bubble broke out. The Shanghai stock market had fallen over 30 percent over three weeks as more than 1400 companies filed for a trading halt in order to attempt future losses.

The peculiarity of the Chinese stock market is that more than 80 percent of investors are small retail investors, while other markets investors are mostly institutional.

The core problem is that individual investors borrow money from brokers to buy securities. As brokerages have lapped up people’s appetite for borrowed money and stock market bets, more households have become exposed to the risk of a stock market correction.

The Chinese government has taken several measures over the past months to try to slow down the fall, but it was not enough; it has banned some very wealthy investors to sell their shares, encouraged small investors to borrow money to invest in stocks and carried out a very important change regarding the national currency, making the Yuan able to float freely according to the will of investors. The problem is that China's financial market is still underdeveloped, given the size of the country, the rules often change and are badly communicated, and there is still less freedom than in Western markets.

The threat is also coming from the real economy side. In earlier 2015 China has seen its slowest growth economy rate since 2009. Imports have fallen and the slow-down in economic growth has played as a negative tool in the property market.

The global worry is that the Chinese crisis will have a negative global impact on many others stock and real markets.

The contagion has already reached some Asian countries, which have strong trade links with China. Also, Australia has started feeling the effects due to the fallen of commodity prices and the pressure on the Australian dollar. The Chinese turmoil is affecting also western markets such as the U.S and the Eurozone.

**What’s behind economic bubbles?**

**Robert Shiller and Eugene Fama points of view.**

“Being essentially socio-psychological phenomena, the bubbles are, by their nature, difficult to control. Regulatory measures taken after the financial crisis could limit the risk in the future, but the fear of bubbles could magnify the psychological contagion, producing even more fulfilling prophecies. A problem of the word "bubble" is that it creates the image of a bubble that is increasing and is bound to burst, suddenly and irrevocably. But in fact the bubbles are more complicated: sometimes deflate because it changes the story that gave rise to them, and then return to swell. It seems more accurate to compare these phenomena to epidemics.

The influenza case teaches us that may suddenly appear even as a new epidemic outbreak earlier is receding, or you see a new form of the virus or some environmental factor increases the rate of infection. The same happens with the bubbles: if it emerges a new story on the economy and whether this new story has a narrative power enough to trigger a new outbreak in the minds of investors, then enters a new speculative bubble.”

*Robert J. Shiller - Nobel Prize in Economics*

A complete opposite theory about markets and bubbles was made by Eugene Fama (Nobel Prize in Economics in the same year of Shiller and Hansen).

Eugene Fama is among the most intransigent defenders of freedom of financial markets and of their complete deregulation. Fama, is the most important proponent of the denies that bubbles exist. As he put it in a interview with John Cassidy for The New Yorker, he said “ I don’t even know what a bubble means. These words have become popular. I don’t think they have any meaning”

**Some of the most famous economic bubbles in history:**

* Tulipmania (1634-1638)
* The Mississipi Bubble (1719-1720)
* The South Sea Bubble (1720)
* Railway Mania (1840s)
* The Roaring Twenties stock-market Bubble (1922-1929)
* Japanese asset price bubble (1980s)
* The Dot-com bubble (1995–2000)
* Uranium bubble (2007)
* United States housing bubble (2007)

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**Useful Questions:**

While preparing to this topic each delegate should think about:

* Has my country ever suffered from an economic or speculative bubble?
* How does the national stock market works in my country?
* How is my country linked to the Chinese economy? How is the Chinese crisis affecting the national economy?
* Which is the rate of import/export between my country and China?
* How about the Western Economies? How does Western Economies influence my country ?
* Is the national economy strong enough to counteract possible future bubbles bursts? If not, what would be needed?

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