



EconoMag

The Show that demystifies Economics

China's Stock Market Crash ©

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Welcome to another edition of EconoMag on EnglishWaves.

We're only a couple of weeks into 2016 and there are already economic problems. This time, they're not in Europe or the United States, but in China! The country's growth has slowed, which has an impact on the global economy, and of course, first and foremost, on the Chinese market.

This summer, Beijing was the victim of its first stock market crash. It started around mid-June, and finished at the end of August. In about one month, the stock market collapsed, falling 32%. This had a huge impact on Chinese business, and consequently the international stock markets as well. This crash may be explained in part by the financial bubble that began in China at the end of November 2014.

To counter the negative effects of the crash, the Chinese government decided to put in place new rules, which included limiting short-selling and closing the stock market to new businesses. The government also ran a propaganda campaign about the wellbeing of the stock exchange. As 80% of investors are individuals, it is important that they continue to buy more stock. The People's Bank of China also devalued the Yuan, reaching ¥6.3975 per US dollar on August 14th. The crash had a global effect: the CAC40 in France, the NYSE in New York, and the FTSE100 in Britain all plunged by 2-5%, resulting in trillions in losses. Oil prices, which had finally started to rise again, also fell.

There are many possible causes of this summer's crash. First, China's middle class is expanding, and many of these individuals put a great deal of money into the stock market, as encouraged by the government. Also, China's economy has begun starting to shift from an industrial economy to a service economy. The effect of this change slowly decreases growth, even if it remains very high. The market was priced way beyond its real value, so the slightest dip leads to a domino effect until the market gets corrected again. After huge losses in July, both Shanghai and Shenzhen's markets managed to stabilize before plunging by another 8% on August 24th.

Six months later, at the start of a new year, another crash occurred. This time, the Chinese government was prepared with new regulations. One of these new rules is that when the losses reach a 7% threshold, the market mechanism is halted. In other words, if the stock market goes down by more than a certain amount, it automatically closes to avoid losing more value, therefore protecting investors. The main reason for this New Year's crash was the release of China's PMI (Purchasing Managers Index), an index of manufacturing activity. It is graded from 0 to 100: if the score is over 50, manufacturing activity is increasing; below 50 means that it is decreasing. In this case, China's score was 48.2. Another drop occurred on January 7th, and the stock exchange closed after just 27 minutes. The government devalued the Chinese currency, and this once again put world markets in the red. The German index (the DAX) fell below 10,000, which is a significant threshold. The French CAC40 also fell by 3%.

This economic chaos is very problematic and future prospects are not particularly encouraging. Last summer's crash was really just a warning for what was and is yet to come. There are around 90 million Chinese individuals who frequently invest in the stock market. This is problematic because they don't leave their money invested for long, as compared to banks or insurance companies, which makes the market very volatile. The Chinese government's experimental and over-correcting actions aren't helping either: On the 8th of January, the Yuan was raised slightly for the first time and the market finally got back to the black.

2016 is shaping up to be a very complicated year for the country as its policies of military expansion have raised many questions. The most recent example is the opening of Chu Thap, a man-made island built by the Chinese to try to extend their EEZ (Economic Exclusive Zone), and to show off their military power. This has raised concerns of all the surrounding countries, as well as of the United States. 2016 might see the start of a new kind of economic war between the two world superpowers.

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