Research Report I 30th Annual Session

Group of Twenty

Implementing measures to prevent a global financial crisis

MODEL UNITED NATIONS

THE INTERNATIONAL SCHOOL OF THE HAGUE

Romeo Buet

Forum:	Group of Twenty (G20)
Issue:	Implementing measures for preventing a global financial crisis
Student Officer:	Romeo Buet
Position:	President

Introduction

Throughout history, from America's first crash, in 1792, to the world's biggest, in 1929, financial and economic crises have risen at times of economic , throwing wealthy powerful nations into crushing debt. Since the beginning of the industrial revolution in the late 18th century, financial crises have become more severe, causing more chaos as more of society is incorporated within the framework's financial system. Financial crises can occur due to multiple reasons; one primary causation of financial crises are if institutions or assets are overvalued, and can be exacerbated by irrational or herd-like investor behavior. A rapid string of selloffs can result in lower asset prices, prompting individuals to dump assets or make massive savings withdrawals when a bank failure is rumored.

The ongoing unpropitious consequence, particularly on development, of the 2008 world crisis, highlights the long-lasting harsh impact financial and economic crisis upon the modern global economy. It only began within a crisis in the US banking sector. However, it went on to unleash the deepest global recession since the Great Depression, leaving a sinking legacy of unemployment and debt.

Even though global growth is returning, there is a need to sustain recovery, fragile and uneven, and continue to address systemic fragilities and imbalances within the system. Unemployment and underemployment levels persist high in many countries, especially with the younger generations. Sustained, inclusive, and equitable economic growth would generate employment leading to poverty eradication, fostering sustainable development, and strengthening social cohesion that needs to be fostered.

Definition of Key Terms

Finance

Finance is, in its simplest terms, the study of money, comprised of the management, creation, and investments of money. It can be categorized into three areas, public finance, corporate finance, and personal finance.

Financial Crisis

A financial crisis is a situation where asset prices see a steep decline in value, businesses, and consumers are unable to pay their debts, and financial institutions experience liquidity shortages. A financial crisis is often associated with a panic or a bank run during which investors sell off assets or withdraw money from savings accounts because they fear that the value of those assets will drop if they remain in a financial institution.

Gross Domestic Product

Gross Domestic Product or GDP, as it is more commonly referred to, is the total value of all the goods and services produced within a nation's borders. GDP is often used as a means of measuring annual economic growth.

Debt

Debt is an amount of money borrowed by one party from another; the borrowing party is allowed to borrow money conditioned to be paid back at a later date, most often with interest. Many corporations and individuals use debt as a method of making large purchases that they would not be abke to afford under normal circumstances.

Assets

An asset is a resource with economic value that an individual, corporation, or country owns or controls with the expectation that it will provide a future benefit.

Interest rates

The interest rate is the money amount a lender charges for the use of assets expressed as a percentage of the principal. The interest rate is typically

noted on an annual basis known as the annual percentage rate. The assets borrowed could be anything with value.

Supply and Demand

The law of supply and demand is a theory on the interaction between the sellers of a resource and the buyers for that resource. The theory defines the effect of the relationship between the availability of a particular product and the demand for that product has on its price. Generally, low supply and high demand increase prices and vice versa.

Recession

A recession refers to a significant decline in overall economic activity in a specific region, lasting usually more than a few months, it is visible through real GDPand income, employment, industrial production, etc.

Inflation

Inflation is a measure of the rate at which the average price level of a basket of selected goods and services in an economy increases over time. It is the rise in the level of prices where a unit of currency effectively buys less than it did in prior years.

Liquidity

Liquidity refers to the ease with which an asset, or security, can be converted into ready cash without affecting its market price.

Monetary Policy

Monetary policy refers to the actions undertaken by a nation's central bank to control the money supply to achieve macroeconomic goals that promote sustainable economic growth.

Exchange rate

An exchange rate is the value of one nation's currency versus the currency of another nation or economic zone. For example, how many pounds sterling does it take to buy one euro.

General Overview

Financial crises have devasting social, political, and economic impacts; even the most developed countries take several years to recover while others suffer the harsh consequences.

Across the world, many governments and national banks were mobilized to mitigate the significant financial crisis of 08', forced to rescue banks that were too large to come up short, to cut loan fees close to zero, and pump liquidity into the economy. It took nations the vast majority of the decade to readjust to that procedure before a definite return to development was made over most developed nations. The IMF has cautioned that governments and regulators neglected to implement the reforms and policies required to shield the global economy from negligent behavior, which, as seen previously, led to an increase in bond interest rates due to the perceived risk of the countries debt.

Causes of 2008 economic crisis

The 08' financial crisis started from a financial market turmoil caused mainly by losses from US sub-prime loans and related securitized products such as mortgage-backed securities (MBS). It then grew into a full-scale financial crisis with significant cumulating losses provoked by financial institutions across a wide spectrum of products and loan portfolios. Market shareholders searched for higher yields without a sufficient appreciation of the risks and overlooked proper due diligence. Ineffective underwriting standards, illogical risk management applications, and increasingly complex financial products resulted in excessive leverage creating vulnerabilities in the system.

In some developed nations, policymakers, regulators, and supervisors did not adequately apprehend and adress the risks of building up in financial markets, maintaining with the pace of financial innovation, or taking into account the systemic implications of federal regulatory policies. The situation's significant underlying factors were inconsistent and insufficiently coordinated monetary policies and inept structural reforms led to unsustainable global financial outcomes.

IMF estimates total losses for the global financial system rose up to 2.2 trillion US dollars as of January 2009. Major global financial groups, including E.U and FSB, have each posted cumulative losses of tens of billions of dollars.

Global Recovery

Global recovery was slow and strenuous, with severe stress and loss of confidence in the global financial markets creating market paralysis and causing a global credit crunch. For several months, governments and central banks worked closely to implement measures to restore consumer confidence and stabilizing the financial system, including public capital injection, nationalization, full protection of bank deposits, credit guarantees, and purchase of toxic assets. However, conditions in the credit markets remained extremely tight for nearly two years.

The cost of bailing out banks and the decline in tax revenues because of lower economic activity or fiscal stimulus struggles worsen government finances. In the case of countries such as Greece and Cyprus, the initial crisis led to rising concerns about the sustainability of public funds. The outcome was a sovereign debt crisis above the recession. The increase in sovereign debt risk added then played back into further increasing the private sector costs of financing and more economic uncertainty. Fiscal cutbacks striving to uphold sovereign debt risk generated even more significant contractions in financial activity short-term. The compound effect of a financial crises alongside a debt crisis in one of the wrolds major economic area in a few years' delay has contributed to output losses of a degree equaling the great depression of the 1930s.

Current situation

Business analysts have stated that we are moving towards conditions of a financial crisis, with a risk of a worldwide recession. It is of great concern as administrations do not have the policy opportunities they had in 2008 to forestall a budgetary fall, and global debt levels are considerably higher than during the last crisis.

Furthermore, even after extensive global action to prevent another global financial crisis, the ILO and World Bank have made it abundantly clear that changes need to be made surrounding the implementation of measures taken by international bodies and nations worldwide, in order not to replicate the issues listed in the introduction. Nevertheless, states still choose to impose their national regulations on top of the global standards or deviate from them on implementation, pushing th global economy closer to another downfall.

Several initiatives have been taken by public and private institutions to mitigate the adverse effects of a possible crisis of the financial sector on its ability to supply trade finance to support trade at an affordable rate. International

transactions comprise a greater level and number of risks, such as the exchange rate risk, the political and non-payment risks. Internationally operating firms have more substantial financing obligations, illustrated in particular by the time lag among actual production of the good and its delivery.

Major Parties Involved

International Monetary Fund (IMF)

The IMF, established in 1945, headquartered in Washington, D.C., United States, consists of 187 member countries. It aims for financial stability, to develop global monetary cooperation and facilitate international trade, as well as reduce poverty and maintain sustainable economic growth around the world.

The IMF is a key player in the global economy, it acts as a mediator for discussions providing a structured framework for the creation of legislations. It offers the possibility fo emergency loans to developing countries that are hit the harderst by the financial crisis. In the last financial crisis, it was the paramount institution which took action the most efficiently, bailing out several major institutions.

World Bank (WB)

The World Bank is like a cooperative, made up of 189 member countries, it was established in 1944 and is headquartered in Washington, D.C. The World Bank Group is comprised of five different institutions managed by their member countries, who act international policymakers. These five organizations are the International Bank for Reconstruction and Development, the International Development Association, the International Finance Corporation, the Multilateral Investment Guarantee Agency, and the International Centre for Settlement of Investment Disputes. The World Bank is a vital resource for financial and technical devlopment and provinding assitance to developing countries around the world.

The World Bank, similarly to the IMF, is a key organization within the international community as it is uniquely positioned to tackle the complex issues and to play a leading role in the response through its l ending, investments, knowledge, and convening capacity. With financial crises requiring decisive, collective action and innovation, the World Bank acts to aid those in need, in partnership with UN agencies, international financial institutions, and bilateral

partners. In 2099 it was seen to be stepping up its financial assistance to help its member countries mitigate the impact of the crisis, establishing magnitudes of $100 billion for IBRD, $42 billion for IDA, and $36 billion for IFC.

European Union (EU)

The EU is a political and economic union of 27 member states that are located in Europe. It has created a single market through a set system of laws that apply to all member states, in matters where members have agreed to act as one. EU policies intend to assure the free movement of people, goods, services and capital within the domestic market, establish legislation in justice and maintain common policies on trade, development, etc.

The European Union has been heavily involved in providing asistance to country in debt due to financial crises, it was particularly solicited during the eurozone debt crisis where many E.U countries suffered heavy debt, like Greece, Ireland and Cyprus. It rescinded a previous act that banned countries from providing bail-out to other E.U members, and set up a framework for the countries most heavily affected to be aided.

World Trade Organization (WTO)

WTO was founded in 1995 taking the place of the General Agreement on Tariffs and Trade, due to its bias in favor of developed countries. WTO was formed as a global international organization dealing with the rules of international trade among countries. The main objective of the 153 members of the WTO is to help the global organizations to conduct their businesses, to provide technical cooperation to less developed and developing countries, to set a forum facilitating the implementation of multilateral trade agreements, and more.

WTO has remained active in the matter implementing regulatory issues and financial-sector rescue programs to aid governements and institutions in the unstable economic times. As well as, pouring billions of dollars into developed nations to prop up their banks in the crisis amounted to unfair subsidies.

United Nations Conference on Trade and Development (UNCTAD)

The UNCTAD, was established in 1964, it is the principal organ of United Nations General Assembly. It provides a forum where the developing countries can discuss the problems related to economic development. UNCTAD is

headquartered in Geneva, Switzerland and has 193 member countries. UNCTAD was founded due to the existing institutions, such as GATT, IMF, and World Bank lack of action with the economic issues faced by developing countries. UNCTAD's central goal is to formulate policies related to areas of development, such as trade, finance, transport, and technology.

Most of the UNCTAD actions as mainly directed towards developing world, as it is its principal target. It formed a series of mandatory policies addressing all institutions and governements, including policies such as DEEs should not incur heavy burden in order to respond to fallouts from a crisis they cannot be held responsible for.

Financial Stability Board (FSB)

The FSB is an international insitution that tracks and makes recommendations about the global financial system. The FSB fosters international financial stability, thourgh coordinating national financial authorities and international standard-setting bodies to work toward developing secure regulatory, supervisory and other financial sector policies. It maintains a level playing field by encouraging coherent implementation of these policies across sectors and jurisdictions.

The FSB works closely with other financial institutions such as the IMF, however it does also produce important solutions itself, like after the 2008 crisis. It collected through various studies, analysized and modelled quantative data, into reports that came very useful to other international institituions when performing risk-assement test on debt relief and bail-outs.

Committee on Payments and Market Infrastructures (CPMI)

CPMI is an international body that promotes, monitors and makes recommendations about development of safe and efficient payments, clearing, settlement and related arrangements, thereby supporting financial stability and the wider economy. Moreover the CPMI serves as a forum for central bank cooperation over looking policy and operational matters, like the stipulation of central bank services.

The CPMI looked heavily into recovery planning along with the IOSCO, producing several reports outlining the key tools needed for re-establishing economic stability. It assessed risk and failure possibilities, looking at usage of

national authorities, especially focused on the allocation of losses and liquidity shortage.

International Organization of Securities Commissions (IOSCO)

The IOSCO is the international organization that joins together the world's securities regulators and is perceived as the global norm setter for the securities sector. IOSCO promotes, implements and supports adherence to internationally sanctioned standards for securities regulation. It operates intensively with the G20 and the Financial Stability Board (FSB) on the global administrative reform agenda.

Timeline of Key Events

Date	Description of event
1780s	Industrial Revolution began
April 1792	The buttonwood agreement took place, where traders met on Wall Street to form a private trading club after public trading was banned earlier that year
Crisis of 1837 and	Financial crisis that touched off a nationwide recession, which lasted until the mid-1840s, causing a down fall in profits, prices, wages and an increase in unemployment
Panic of 1866	First large international financial downturn that accompanied the failure of major banks in several financial hubs at the time
1873-1896	Long Depression an unprecedented worldwide price and economic recession, beginning in 1873 and running till 1896 in some countries. The most severe in Europe and the United States, which had been experiencing strong economic growth.
1929-1939	Great Depression was a longest, deepest, and most severe worldwide economic depression of the 20th century, started in the United States after a major fall in stock prices, causing chaos among investors, which rapidly spread to other cities around the world and had devastating effects in both rich and poor countries.
1973/1979	Energy crisis occurred when the Western world faced

	substantial petroleum shortages and surge of oil prices, causing stagnant economic growth in many countries as oil prices surged
1990s	Economic downturn affecting much of the Western World, caused by restrictive monetary policy enacted by central banks primarily in response to inflation concerns, the loss of consumer confidence
2007-2009	The first true global financial crisis caused by excessive risk-taking by banks combined with a downturn in the subprime lending market in the United States. The crisis sparked a global recession, the largest of its kind since the great depression.
2009-	European debt crisis, a multi-year debt crisis that taking place in the European Union since the end of 2009. Several member states were unable to repay or refinance their government debt or to bail out over-indebted banks without the assistance of third parties.
July 21, 2010	Dodd–Frank Wall Street Reform and Consumer Protection Act, was enacted to promote the financial stability of the United States by improving accountability and transparency in the financial system.

UN involvement, Relevant Resolutions, Treaties and Events

- G20 Summit on Financial Markets/World Economy, November 15, 2008
- Global Jobs Pact, International Labour Conference, 19 June 2009
- Conference on the World Financial and Economic Crisis, General Assembly Resolution 63/303
- Recovering from the crisis: a Global Jobs Pact, General Assembly, Resolutions 2009/5 - 2010/25 – 2011/37

Previous Attempts to solve the Issue

In simple terms, the Global Jobs Pact is a major step in the right direction and can act as a foundation for what is to follow. However, more action is necessary in order to surely prevent another financial crisis and erase all the impacts of the previous crises. Multiple resolutions have been passed within different UN committees, all aimed at recovering and fostering economic stability.

One of the EU's prominent responses after the 08' crisis is the European Market Infrastructure Regulation (EMIR), a body of European legislation for the regulation of over-the-counter derivatives, which played a significant role in the financial crisis. It is evident that it was necessary for a regulatory framework to be put in place to improve the transparency of derivatives, apply central clearing, and impose collateral requirements on bilateral transactions to cover market and counterparty risks. All EU central counterparties (CCPs) were authorized under the implementation of EMIR, six trade repositories have been set up and are currently fully functionning to provide transparency on EU derivatives trades, and European Securities and Markets Authority (ESMA) had already figured out how interest rate swaps will need to be centrally cleared.

Before the 08' global financial crisis, securitizations had become too complicated and together with far too positive ratings, which contributed to the spreading of the financial crisis. Requirements for improved transparency around securitizations have been agreed upon and are currently being implemented. In addition, the three regulations issued in the past years introduce a wide range of measures regarding credit ratings, including bringing credit rating agencies (CRAs) under supervision. Such regulations would help to minimize the reliance on credit ratings and mitigate the "cliff effects" through which downgrades would worsen a financial crisis.

All hedge funds were not regulated prior to the financial crisis, which is blamed for being one of the leading causes of the previous crisis. Nevertheless, a comprehensive framework for the supervision and prudential oversight of alternative funds and private equity in the EU was created amidst. Which not only increased the transparency for investors, but it equipped national supervisors, and the ESMA with the information and tools essential to track and react to risks to the stability of the financial system that would be prompted or amplified by the enterprises of alternative investment funds, for instance through excessive leverage.

Possible Solutions

The possible solutions for the issue can be effectively split into two different types. Those set by international bodies directed in the best interest of all nations, and those set by governments primarily aimed at maintaining their country's prosperity or recovery.

The first possible solution is called devaluation. It involves the reduction of the value of your exchange rate. For example, after the financial crisis, Iceland devalued Krona by 35% in 2008. This considerably aided Iceland because Icelandic exports became less costly, leading to increased demand for exports and giving an opportunity to higher economic growth. Devaluing the exchange rate will invariably make exports cheaper, which effectively helps boost growth. For countries within the E.U., restore their currency would lead to a considerable fall in their exchange rates and make the economy more competitive. However, many countries are still reluctant to opt for this method of financial recovery and implement it as a significant impact on the population. Negatively as the import prices go up, consumers who rely on imported goods will fall into the standard of living.

The second possible solution to solve this problem involves placing risk back into the private sector. Eliminating the subsidies banks rely on, will make the debt more expensive, simply meaning that equity holders will lose money on dividends, and the cost of credit would climb. Diminishing excessive deposit insurance brings out credulous investors who make homogenous investments in unreliable and volatile banks could see significant losses. As regulators implement a new set of reforms in the wake of the latest crisis, the opportunity arises to reverse the trend towards the ever-greater entrenchment of the state's role in finance. Nevertheless, weaning the industry off government support is not simple.

Thirdly, another solution would be inflation to boost aggregate demand in the economy to create higher economic growth, cutting interest rates, and printing money, which would lead to a rise in the money supply and help stimulate economic activity. The government could pursue a fiscal stimulus, involving higher government spending, along with lower tax-financed by higher government borrowing. For example, in the 2009 recession, the U.K. and U.S. governments pursued expansionary fiscal policy. Also, it is easier for the government to pay back debt and bondholders lose out because their savings are worthless after the inflation.

Moreover, a similar measure that could be implemented by governments would be default, which alludes to the choice by the government to quit reimbursing part or the entirety of its debt. This will make it hard for it to borrow later on, yet it allows for there to be no aggressive cut in spending to reduce borrowing. At the point when governments borrow as the % of GDP rises quickly, it turns out to be very hard to control borrowing. So as to meet interest repayments and reduce the debt burden, the government may be bound to follow through with fiscal austerity. Nevertheless, cutting spending in a recession can make it worse, as seen by previous attempts, the deficit continues to rise and creates social instability. A better option may be to admit that the country is going to struggle to repay its debt and default on their bonds earlier, meaning investors in national bonds would lose some money. However, it gives the government the framework to boost economic growth, and in the long run, offers a more beneficial deal for bondholders. Rather than automatically default, along with also having a more extended period of economic decline.

Another system that could be implemented and would be beneficial to prevent the global financial crisis is an early warning system and prompt corrective action scheme based on capital adequacy and other indicators of risk. It would also bring in public administration the possibility of insolvency and liquidity shortage with the use of a bridge bank scheme. Along with a deposit insurance system and other safety net provisions to protect depositors, with the chance make use of public funds in recapitalizing banks, or to nationalize a bank.

In order to fix the political issues regarding the implementation of international regulations would be, in addition to the previous solutions, would be a practical usage of national and international institutions as communication to set up these legislations. Authorities should aim to establish trust and institutionalized cooperation, limiting the need for unduly burdensome local capital and liquidity requirements, which would lead to cut-off pools of resources and restrain the flexibility of banks to react to the next crisis.

Following the idea above, nations should continue to promote and make full use of the Global Jobs Pact and implement the policy options contained within. Considering the financing and capacity-building of developing economies that lack the fiscal space to adopt appropriate response and recovery policies require particular support, with the cooperation of multilateral organizations and other international partners to provide funding, including existing crisis resources, the implementation of those recommendations and policy options.

Finally, international bodies such as the IMF, the World Bank and International Labour Organization as well as the FSB and CPMI to research

further measures to promote systemwide policy coherence in the area of decent work and sustained, inclusive and equitable economic growth, need to be encouraged and spread to ensure that financial crises are prevented in the future, or their effects are highly mitigated.

It is important to consider that financial crises can take place at any moment especially in times of uncertainty such as today. Therefore, all delegates should keep up to date on the subject as things may stand differently by the time of the MUNISH.

Bibliography

"The slumps that shaped modern finance." *The Economist*, The Economist Magazine, 8 November 2017, www.economist.com/news/essays/21600451-finance-not-merely-prone-crises-it-shaped-them-five-historical-crises-show-how-aspects-today-s-fina

"Preventing financial crisis in developing countries." World Bank, 2 May, 2019, http://documents.worldbank.org/curated/en/600471468127172589/310436360_20050012034200/additional/multi0page.pdf.

Magnus Ohman."Political Finance Regulations around the World." *The International IDEA,* International Institute for Democracy and Electoral Assistance, 1 June 2012, www.idea.int/publications/catalogue/political-finance-regulations-around-world-database-overview.

"Can private-equity firms turn a crisis into an opportunity?" *The Economist*, Economist Magazine, 30 March 2020, www.economist.com/finance-and-economics/2020/05/30/can-private-equity-firms-turn-a-crisis-into-an-opportunity.

"Trade Finance in Periods of Crisis: What Have We Learned In Recent Years?." *WTO,* World Trade Organization Economic Research and Statistics Division, 1 January 2013, www.wto.org/english/res_e/reser_e/ersd201301_e.pdf.

Chuck Finder-Wust."How we can prevent another financial crisis." *Futurity*, Futurity, 25 March 2018, www.futurity.org/financial-crises-regulation-insolvency-1712122/.

"Regulatory measures to prevent another crisis." *European Securities and Market Authorities*, 19 November 2014, www.esma.europa.eu/sites/default/files/library/2015/11/2014-1382.pdf.

“Recovering from the world financial and economic crisis: a Global Jobs Pact.” 2011/37 - *Economic and Social Council* - United Nations, ec.europa.eu/clima/citizens/eu_en.

Ross Chainey.“An economist explains what happens if there’s another financial crisis.” Worl Economic Forum, 30 Apr 2019, www.weforum.org/agenda/2019/04/an-economist-explains-what-happens-if-there-s-another-financial-crisis/.

Additional resources

"Dictionary." *Investopedia* , www.investopedia.com/terms/c/cagr.asp

"The IMF's response to the global crisis." *IMF* , www.imf.org/external/np/exr/facts/pdf/changing.pdf