

Department of Economics and the Centre for Macroeconomics  
**Assessing Global Financial Stability: where do we stand?**

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# A Framework for Assessing Global Financial Stability

LONDON SCHOOL OF ECONOMICS

FRIDAY, OCTOBER 27, 2017

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# Outline



- ▶ The GFSR
  - The IMF's assessment of risks to global financial stability
- ▶ Growth-at-Risk
  - Mapping financial stability risks into macroeconomic performance
- ▶ Going forward
  - Strengthening the analytical framework for financial stability



# Fall 2017 GFSR

IS GROWTH AT RISK?

# Near term global financial stability risks are improving

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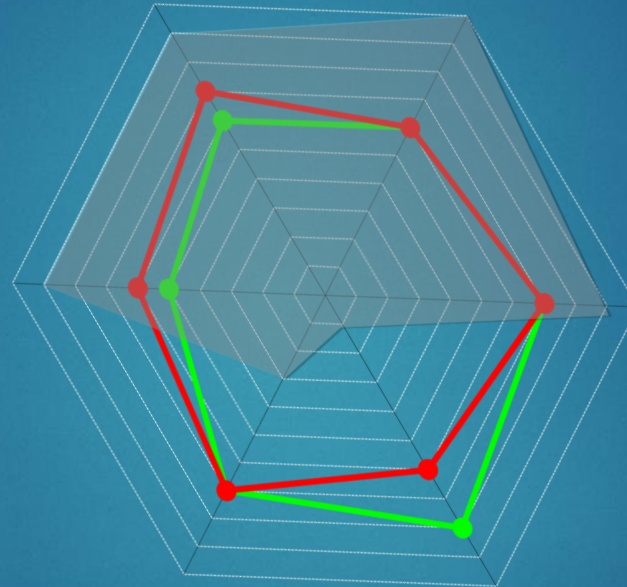
Emerging market risks

Risks

Credit risks

Macroeconomic risks

Market & liquidity risks



Apr 2017 GFSR



Oct 2017 GFSR



Global Financial Crisis

Away from center signifies higher risks, easier monetary and financial conditions, or higher risk appetite

Monetary & financial

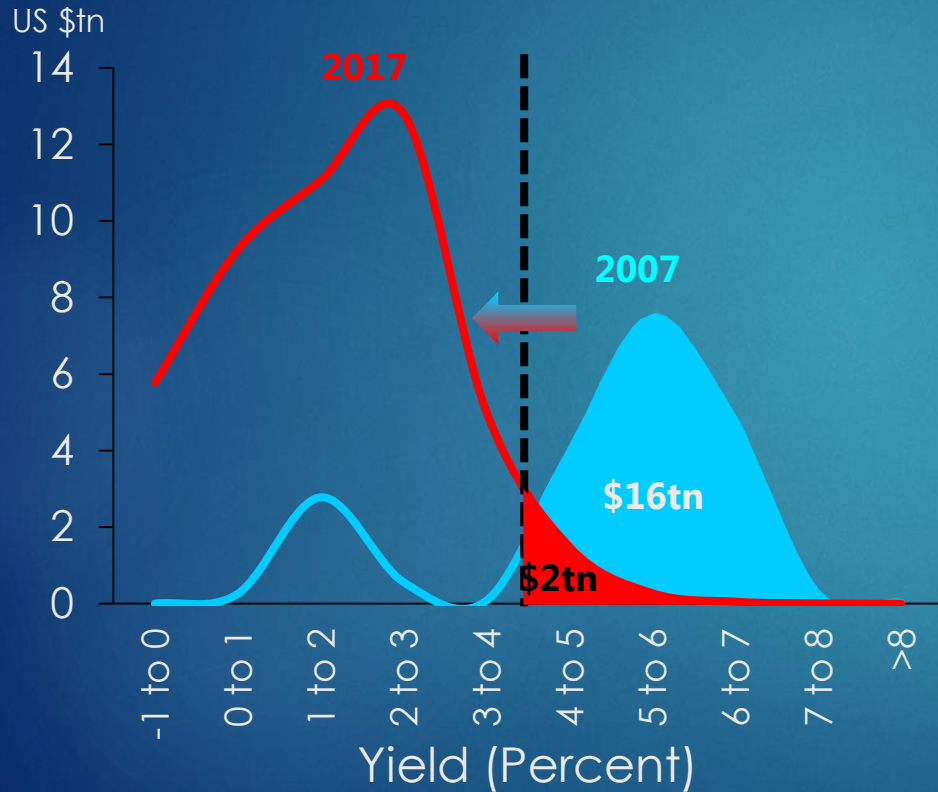
Conditions

Risk appetite

# Too much money chasing too few yielding assets

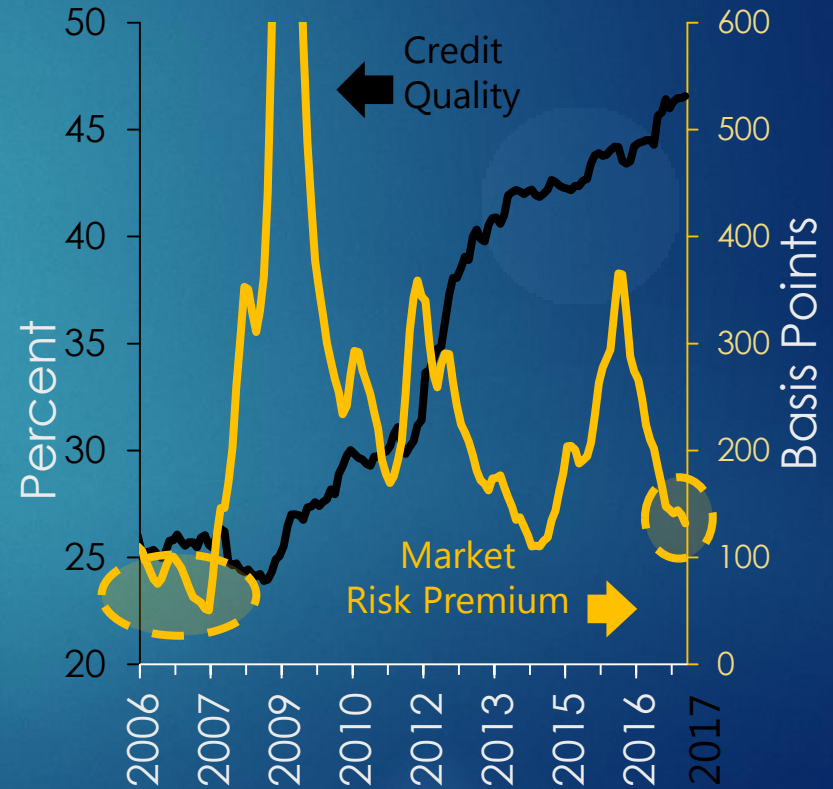
## Fewer Yielding Assets...

(Global Investment-Grade Fixed Income Instruments)



## ... Compressing Premiums As Credit Quality Worsens

(Market Risk Premium, Share of IG BBB Bonds)

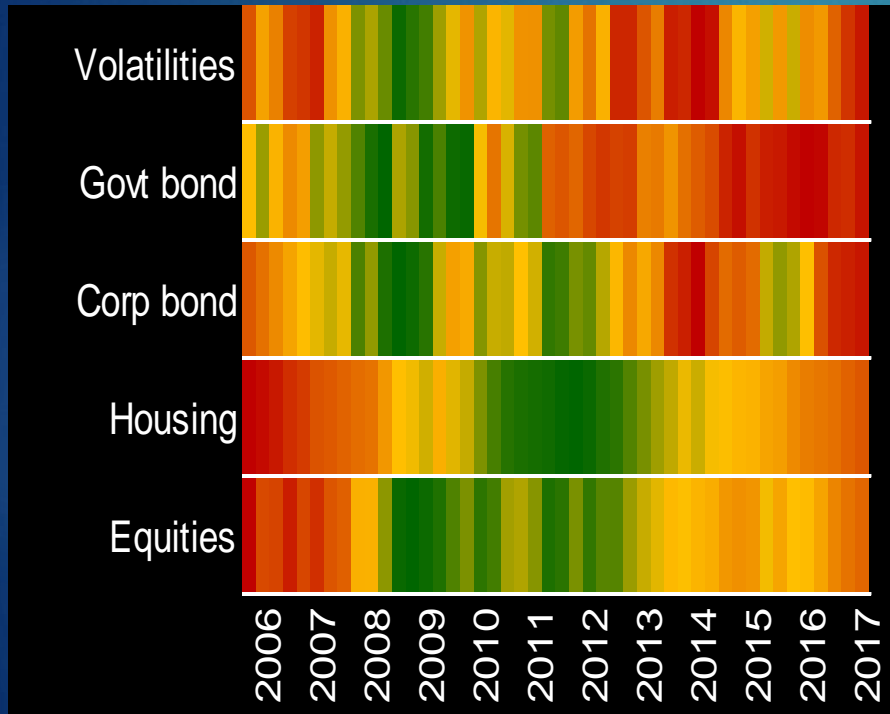




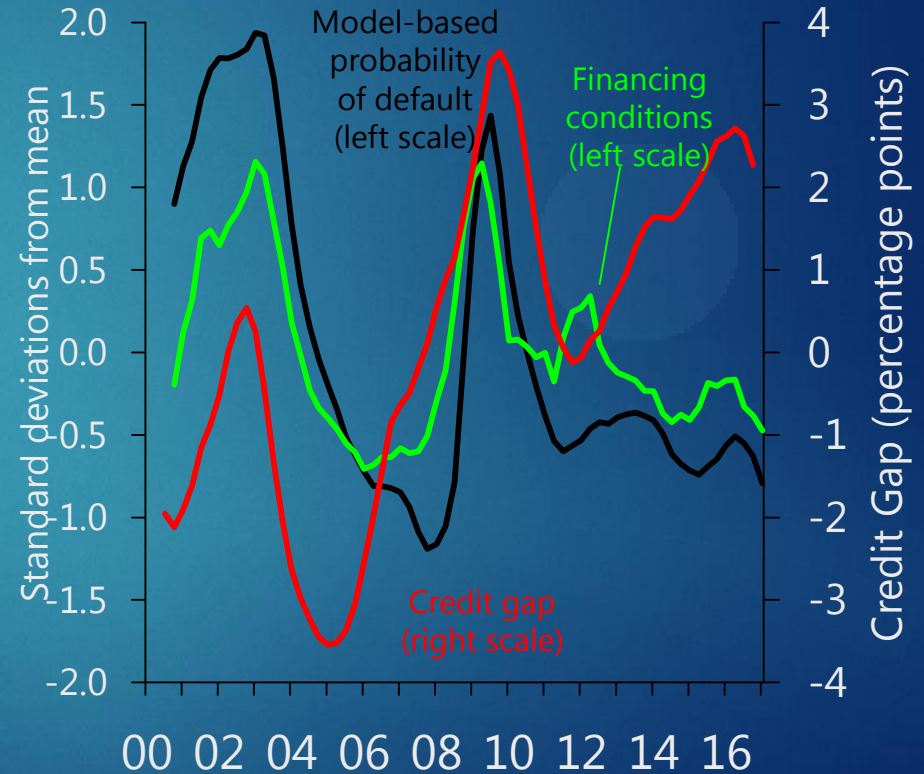
# The volatility paradox: low volatility breeds complacency

3

Low Volatility and Rising Valuations...  
(AE Assets, Percentile Rank)



... Leading to Rising Leverage And Complacency

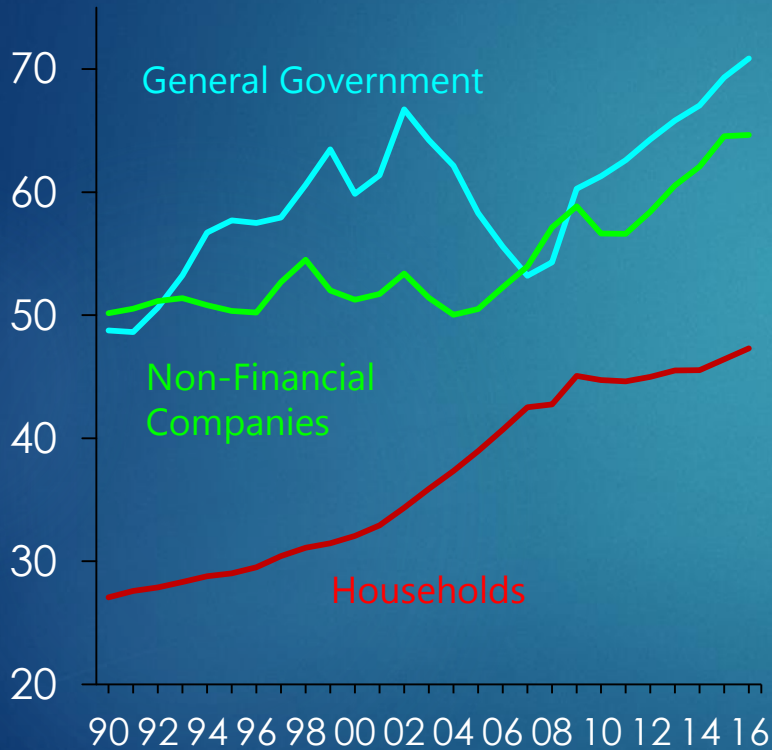


# Higher leverage and debt service challenges

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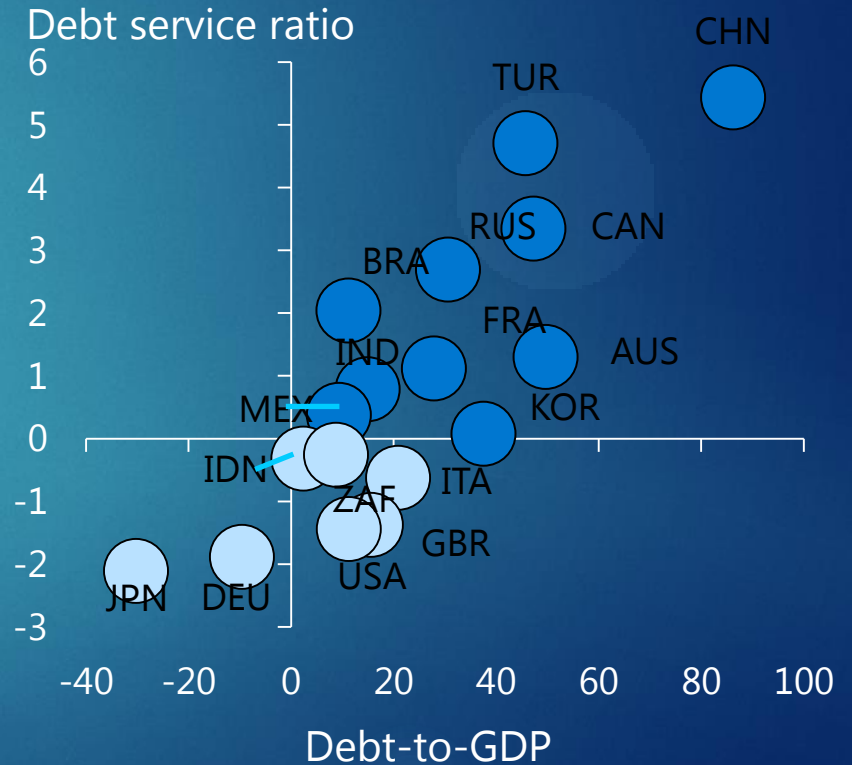
## Debt Continues To Rise...

(Average Debt-to-GDP Ratios for G20 Economies, Percent)



## .. Increasing Debt Service Burdens

(Deviation From Mean, Percentage Points, 2016)

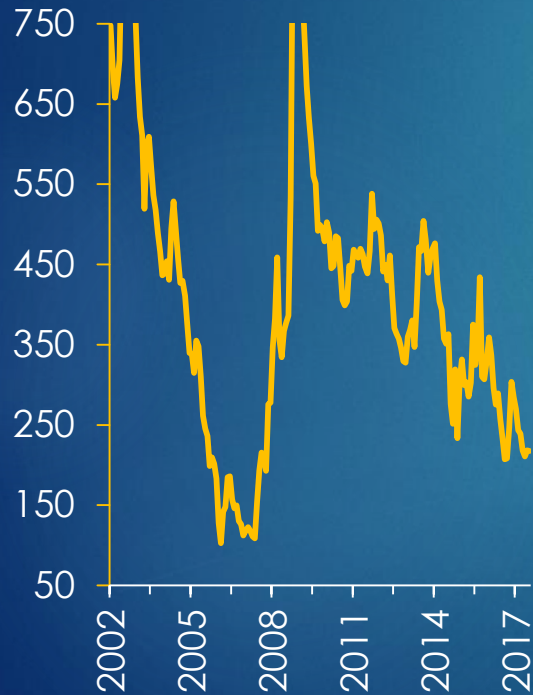




# Benign external conditions; EM vulnerabilities remain

## Risk Premiums Have Compressed

(Market Risk + Term Premium, Basis Points)



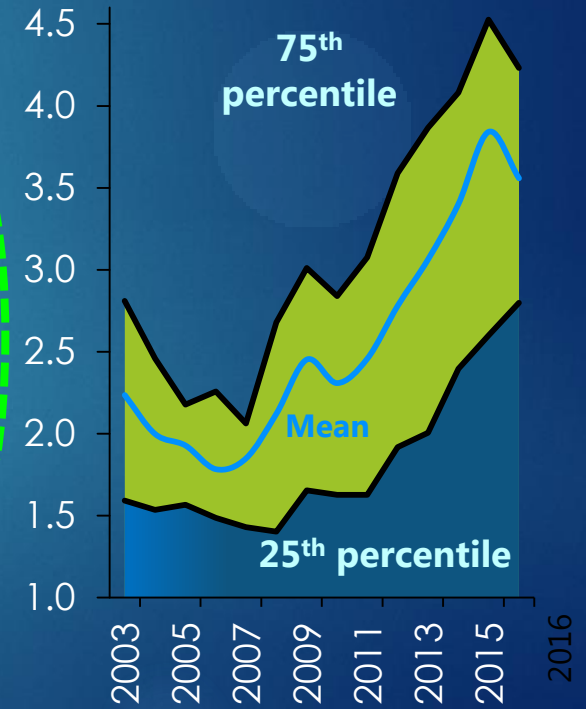
## Portfolio Flows Have Rebounded

(Billions of USD, Four-quarter Rolling Sum)



## Corporate Leverage Remains High

(Total Debt to EBITDA, Multiple)

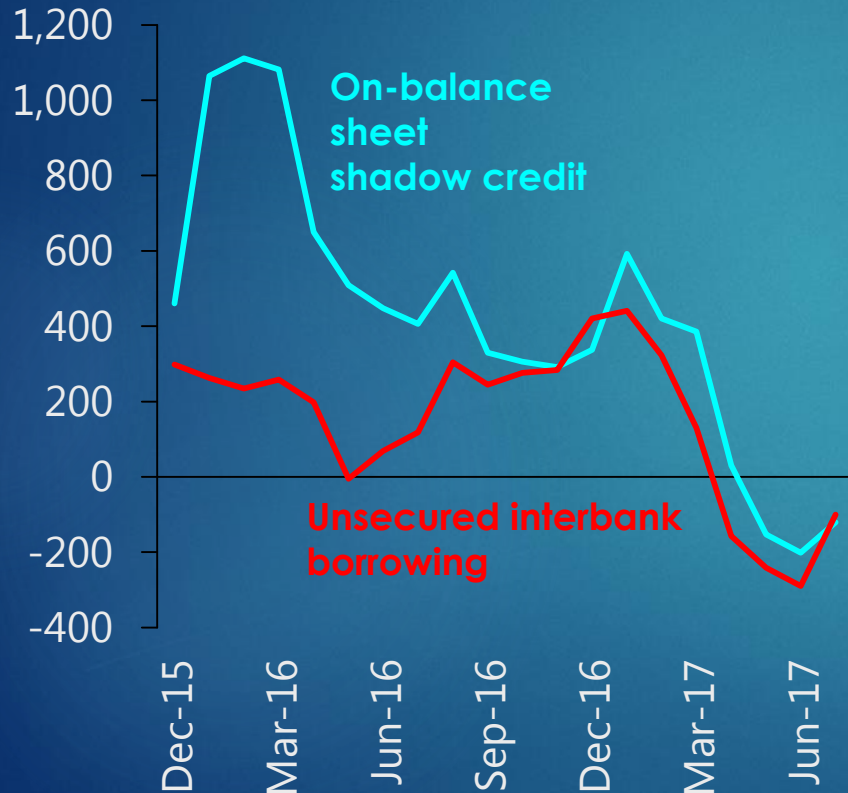


# China: A delicate balancing act

6

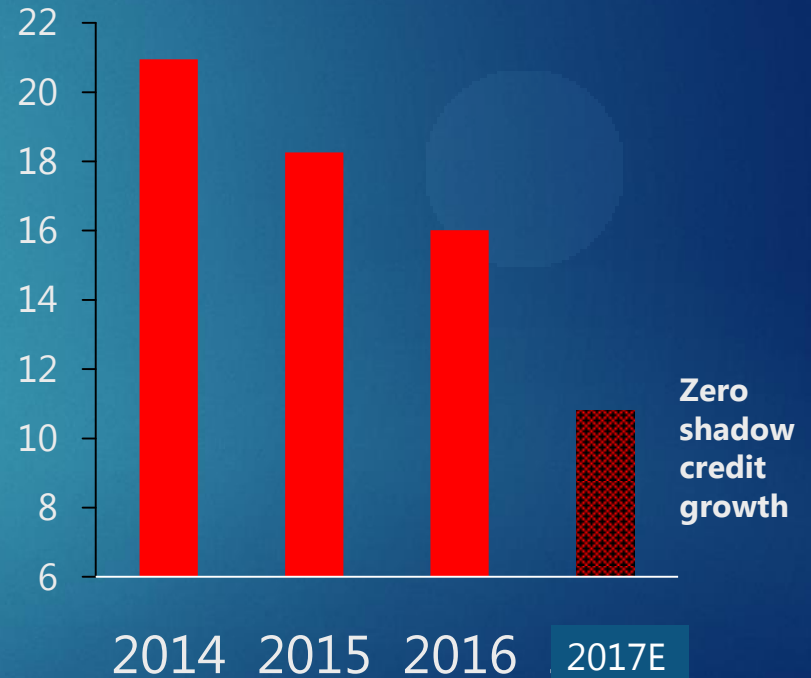
## Regulatory Tightening of Small and Medium Sized Banks...

(Monthly Change, Three Month Average, Billions of RMB)



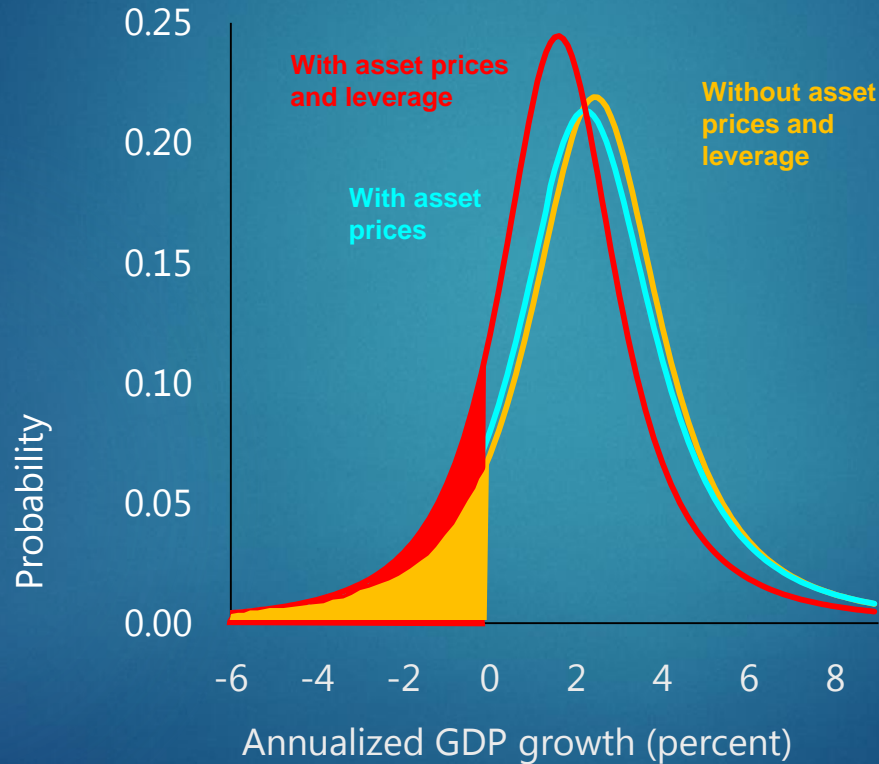
## ... Could Impact Credit Growth

(Credit Growth Under Shadow Credit Growth Assumption; Percent)



## Rising Leverage Foresees a Riskier Outlook

(Probability Density Forecasts for GDP Growth Made One Year Earlier)

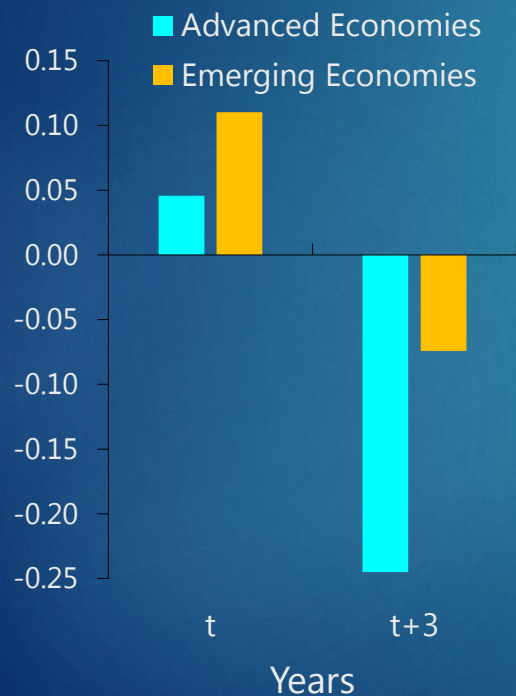


# Rising household debt could challenge growth

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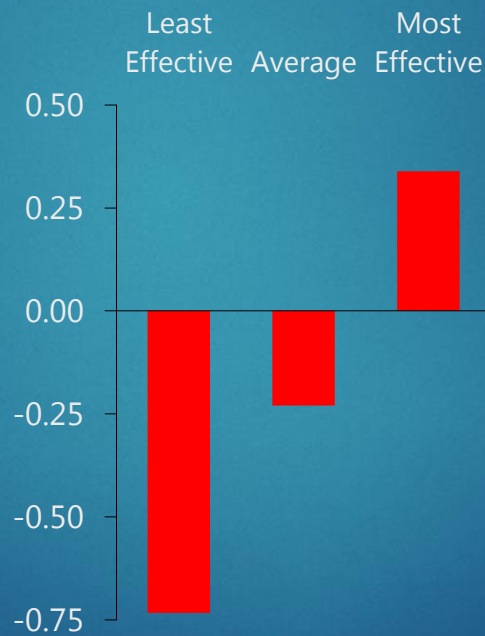
## Short Term Expansions May Pose Future Risks to Growth

(Growth Effect of a 1 Percent Increase in HH Debt to GDP, Percent)



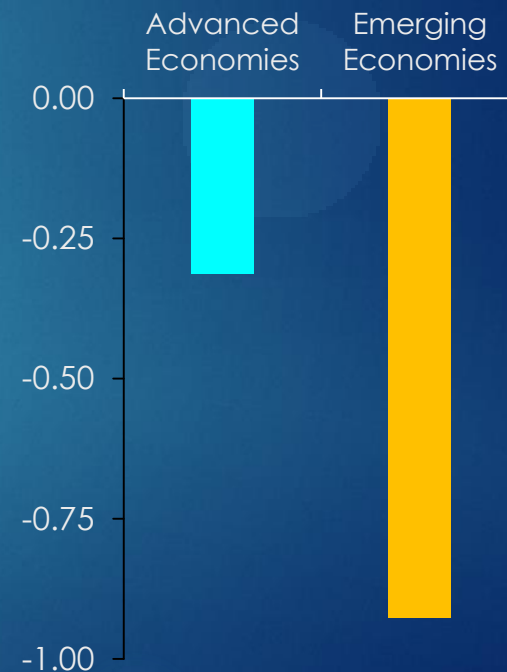
## Effective Policies & Institutions Could Mitigate These Risks

(Growth Effect at t+3 of a 1 Percent Increase in HH Debt to GDP, Percent)



## Macprudential Policies Can Curb Household Credit Growth

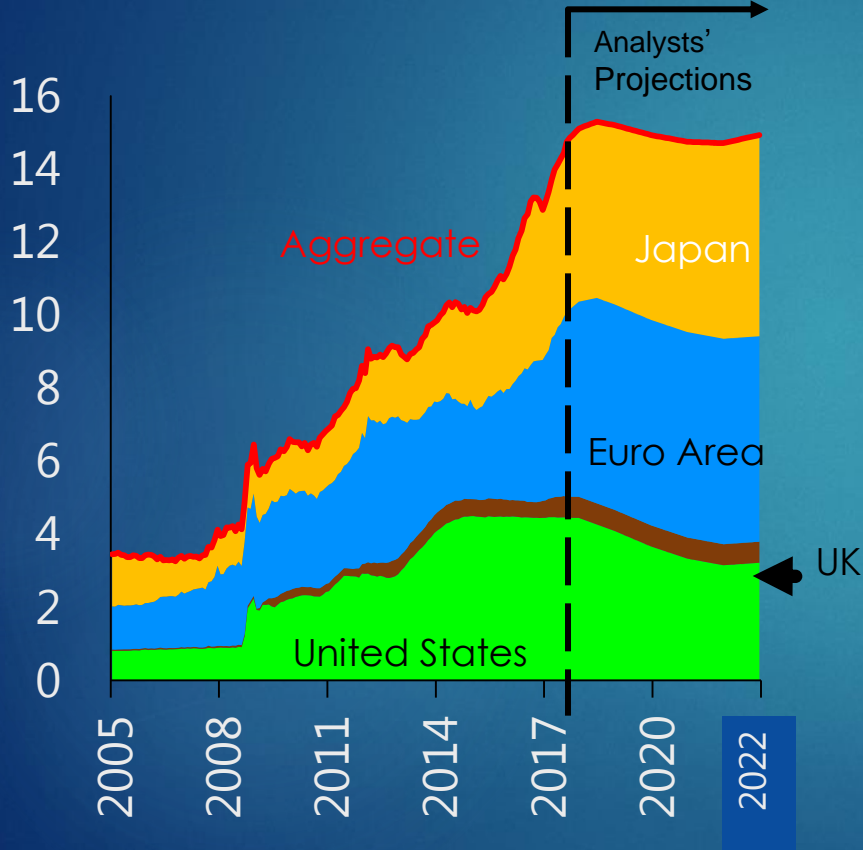
(Impact of a Tightening on Real Household Credit Growth, Percentage Points)



# Monetary policy support: Still needed

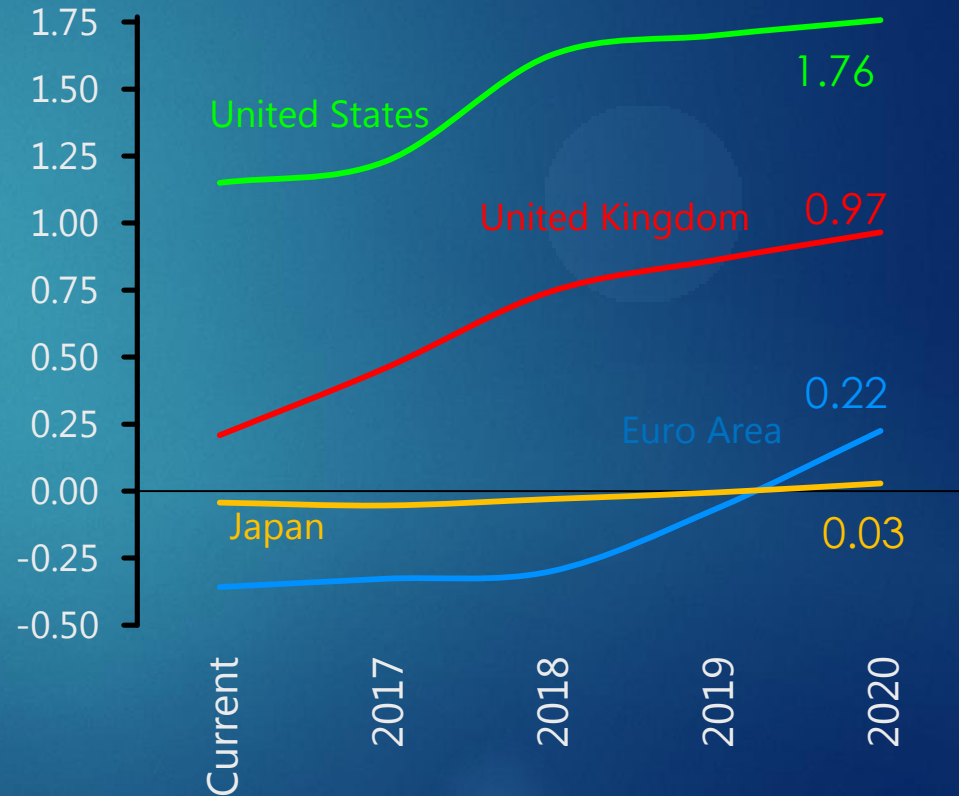
## Gradual Central Bank Balance Sheet Reduction

(Central Bank Outstanding Assets, Trillions of USD)



## Prolonged Low Policy Rates

(Market Implied Policy Rates, Percent)







# Growth at Risk

A CONCEPTUAL FRAMEWORK FOR FINANCIAL STABILITY RISKS AND  
MACROECONOMIC PERFORMANCE



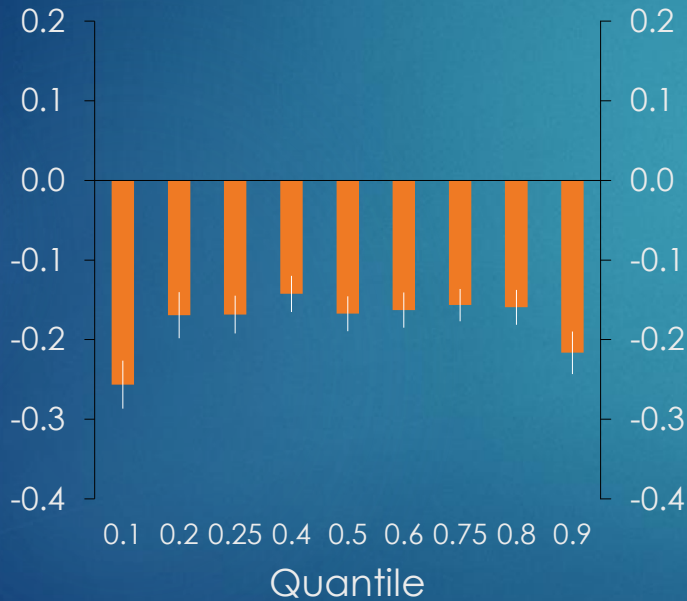
# Thinking through financial stability



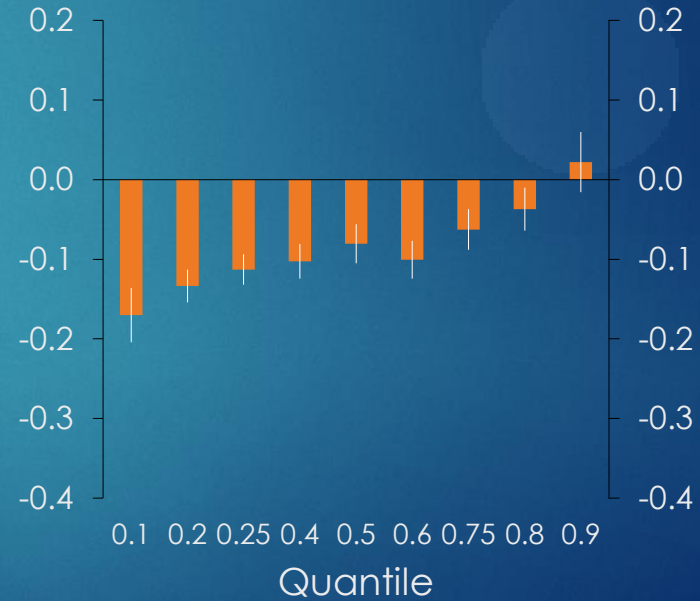
- ▶ Defining financial stability
  - ▶ Measuring financial stability
- 

# Rising leverage signals higher downside growth risks at longer time horizons

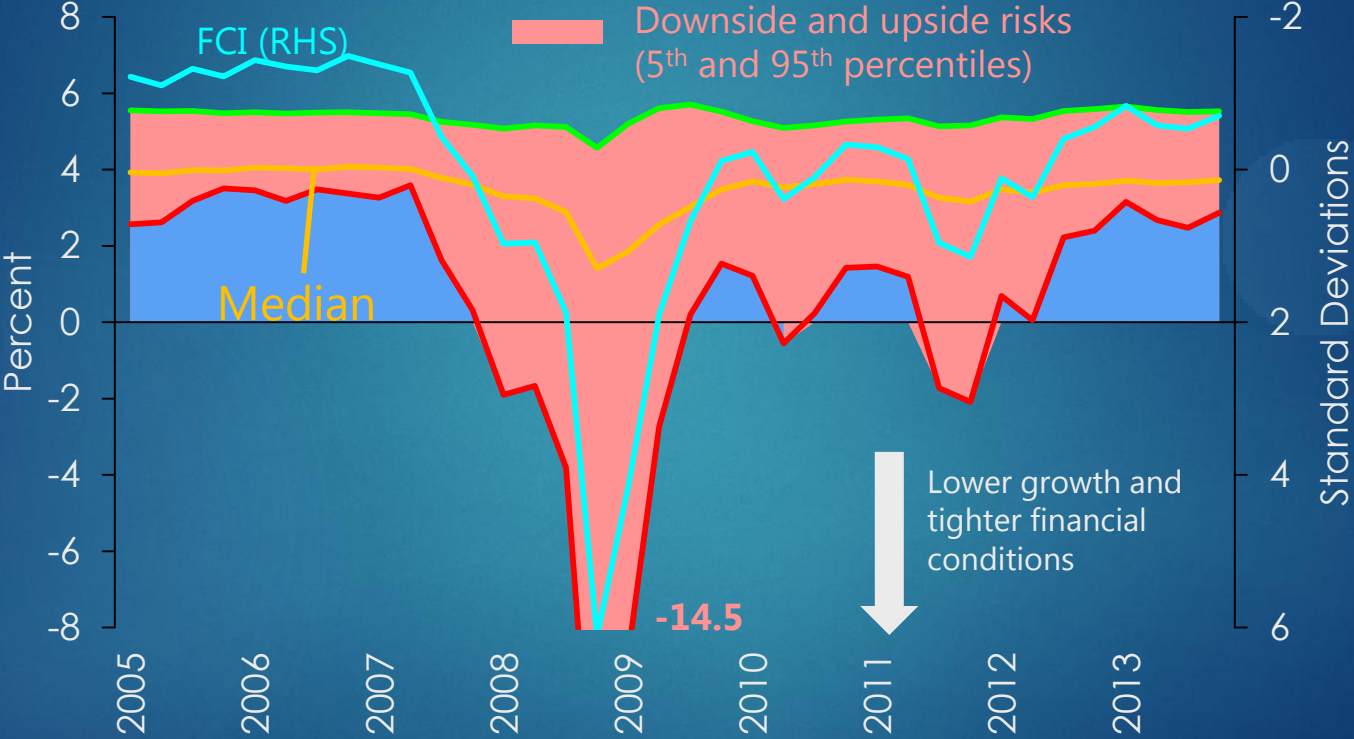
Advanced economies: three years ahead



Emerging market economies: three years ahead



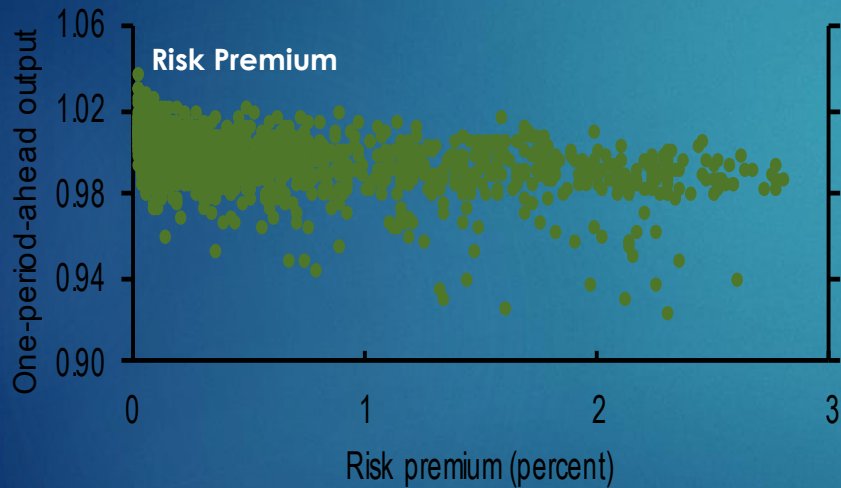
# Tighter financial conditions forecast greater downside tail risk to global growth



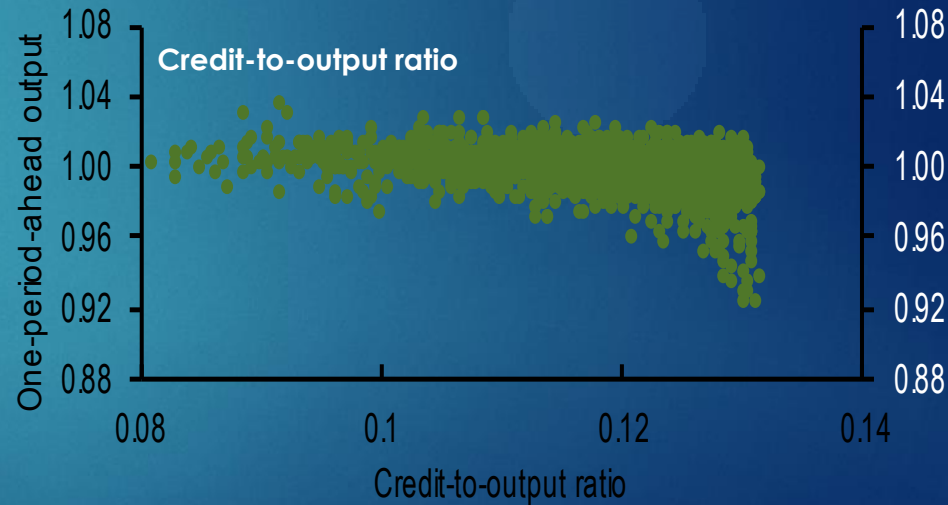
# One-period-ahead GDP and financial conditions

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Increasing risk premia signal a more pessimistic growth outlook ...



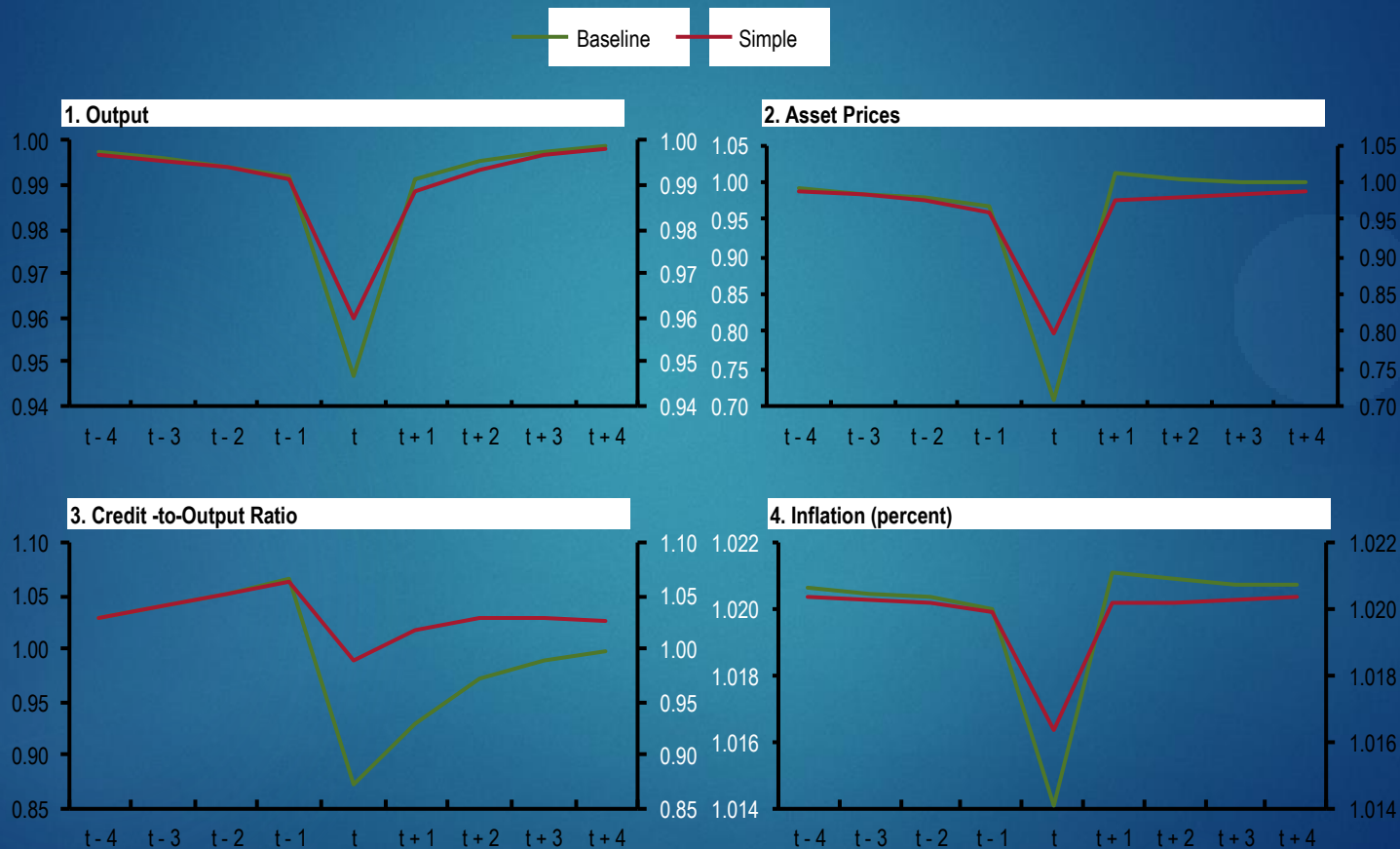
... as does elevated leverage



Source: IMF staff estimates.

Note: Values are normalized with steady state = 1.

# Simple debt tax ameliorates risk of leverage-induced recessions



Source: IMF staff estimates.

Note: Values are normalized with steady state = 1, except for inflation (in percent).

Thank you



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