



International Monetary Fund

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COVID-19 Pandemic— Financial Stability Implications and Regional Cooperation

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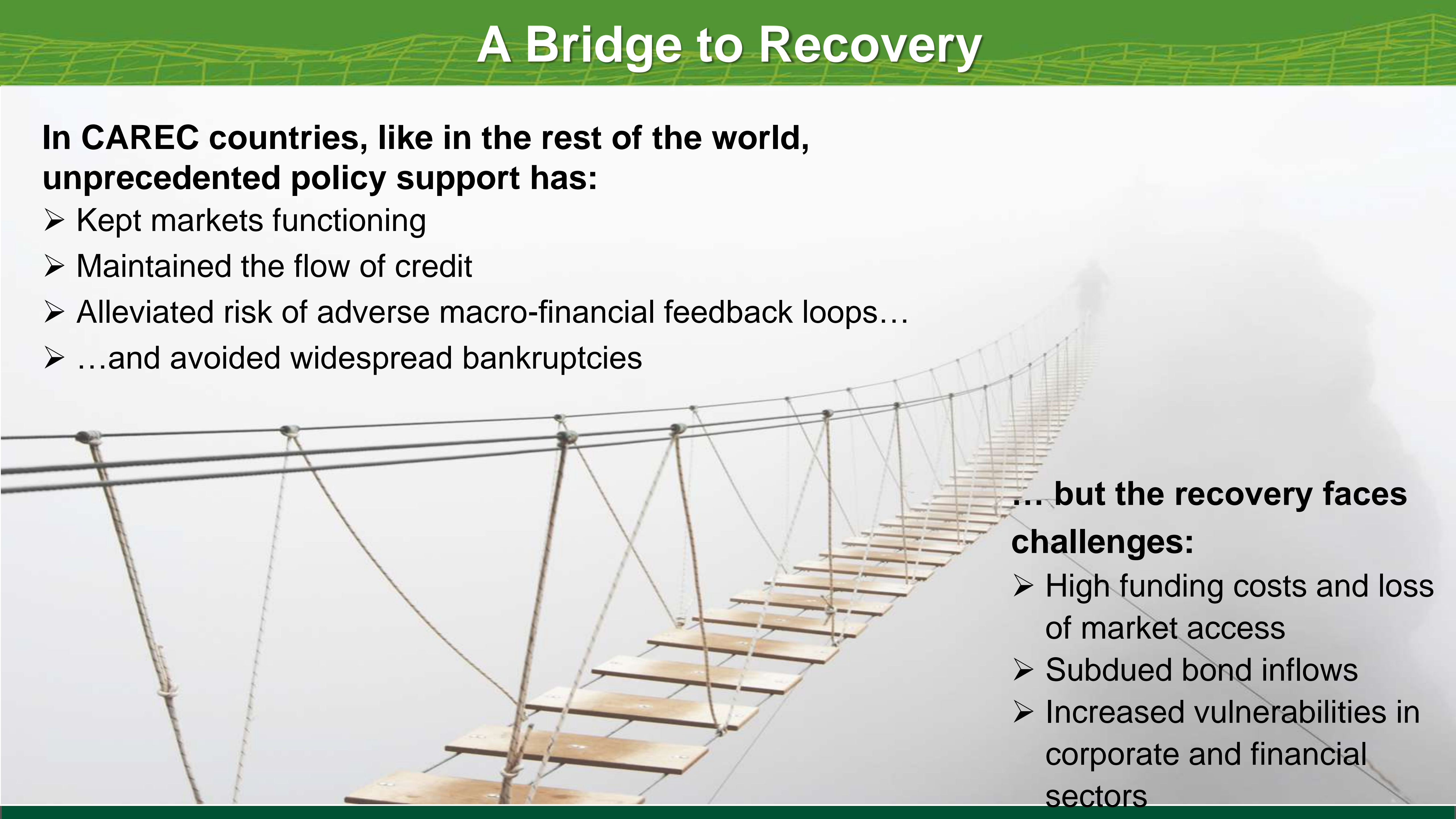
A Bridge to Recovery

In CAREC countries, like in the rest of the world, unprecedented policy support has:

- Kept markets functioning
- Maintained the flow of credit
- Alleviated risk of adverse macro-financial feedback loops...
- ...and avoided widespread bankruptcies

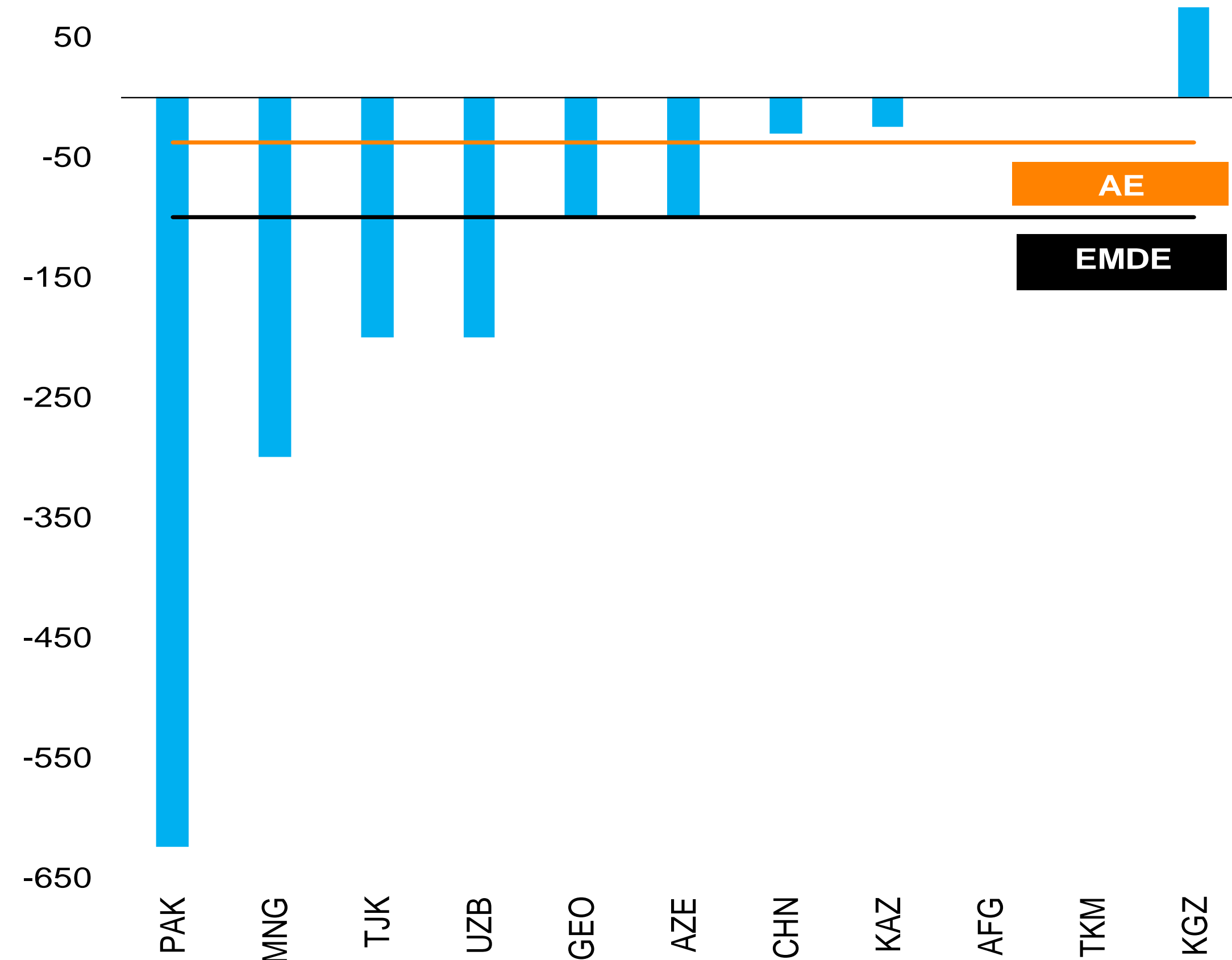
... but the recovery faces challenges:

- High funding costs and loss of market access
- Subdued bond inflows
- Increased vulnerabilities in corporate and financial sectors

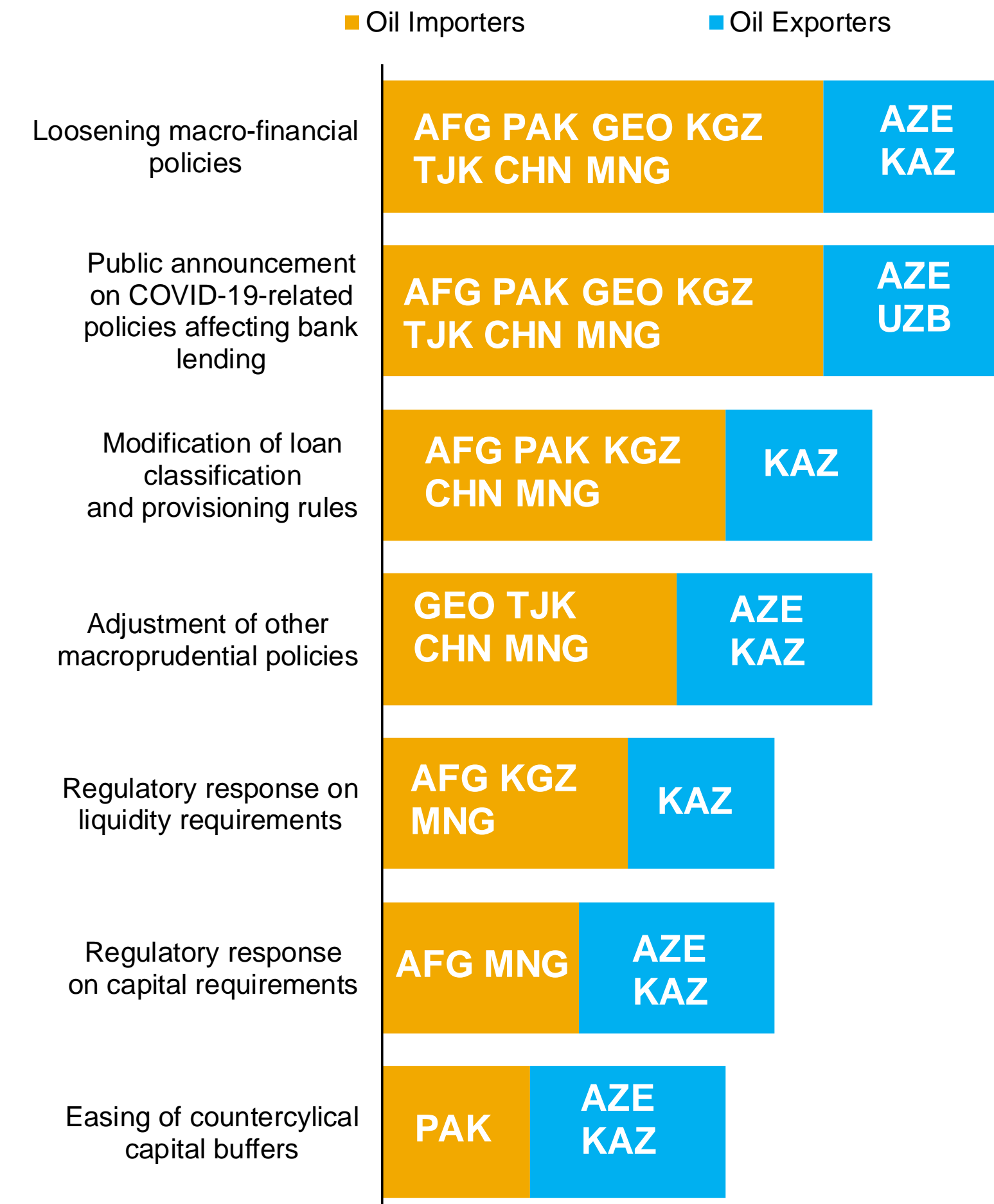


Unprecedented Policy Response to Stabilize Financial Markets

CAREC: Monetary Policy Rate Adjustment
(Change in bps since end-2019)

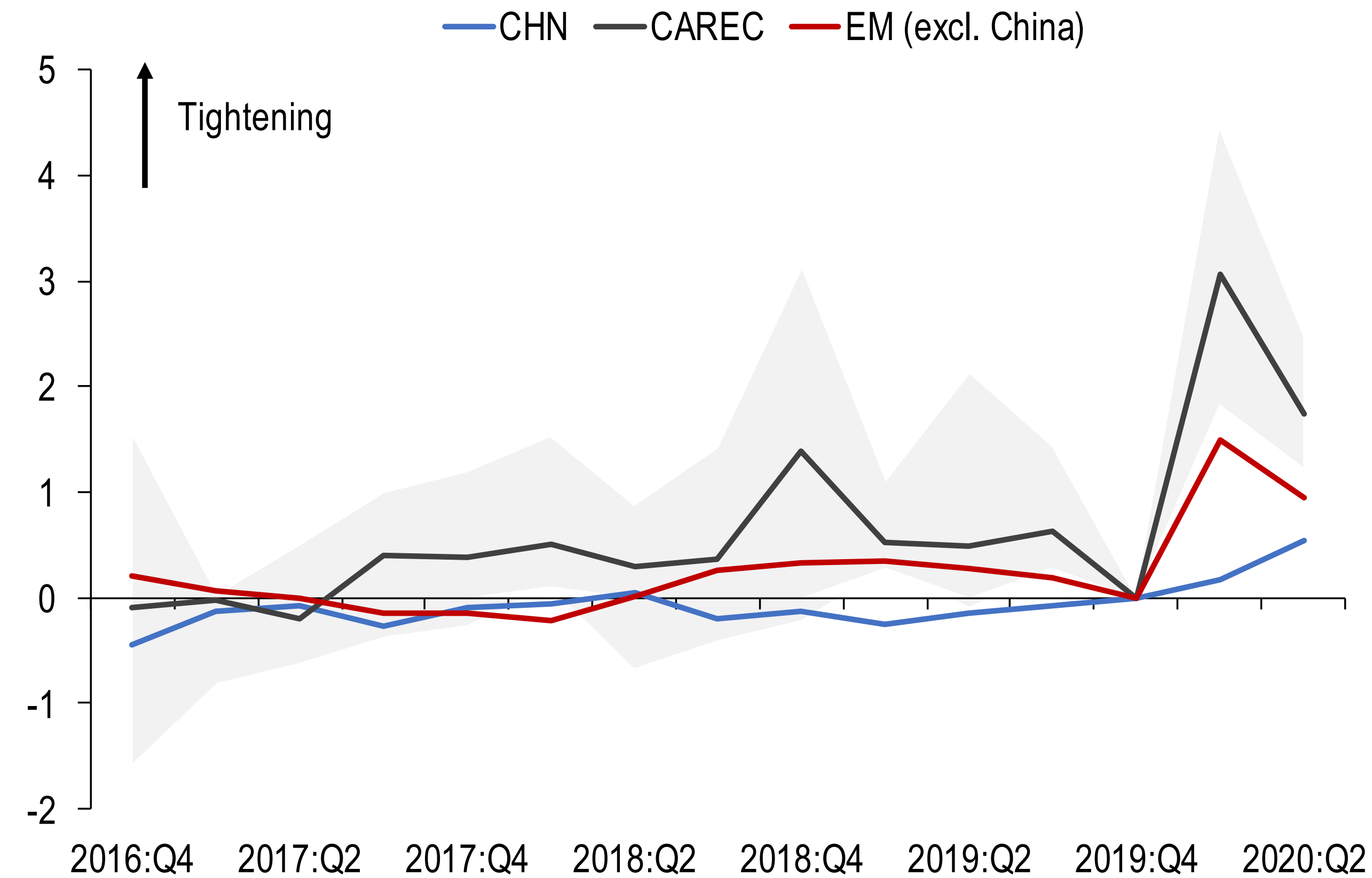


CAREC: Macro-Financial Policy Responses to COVID-19

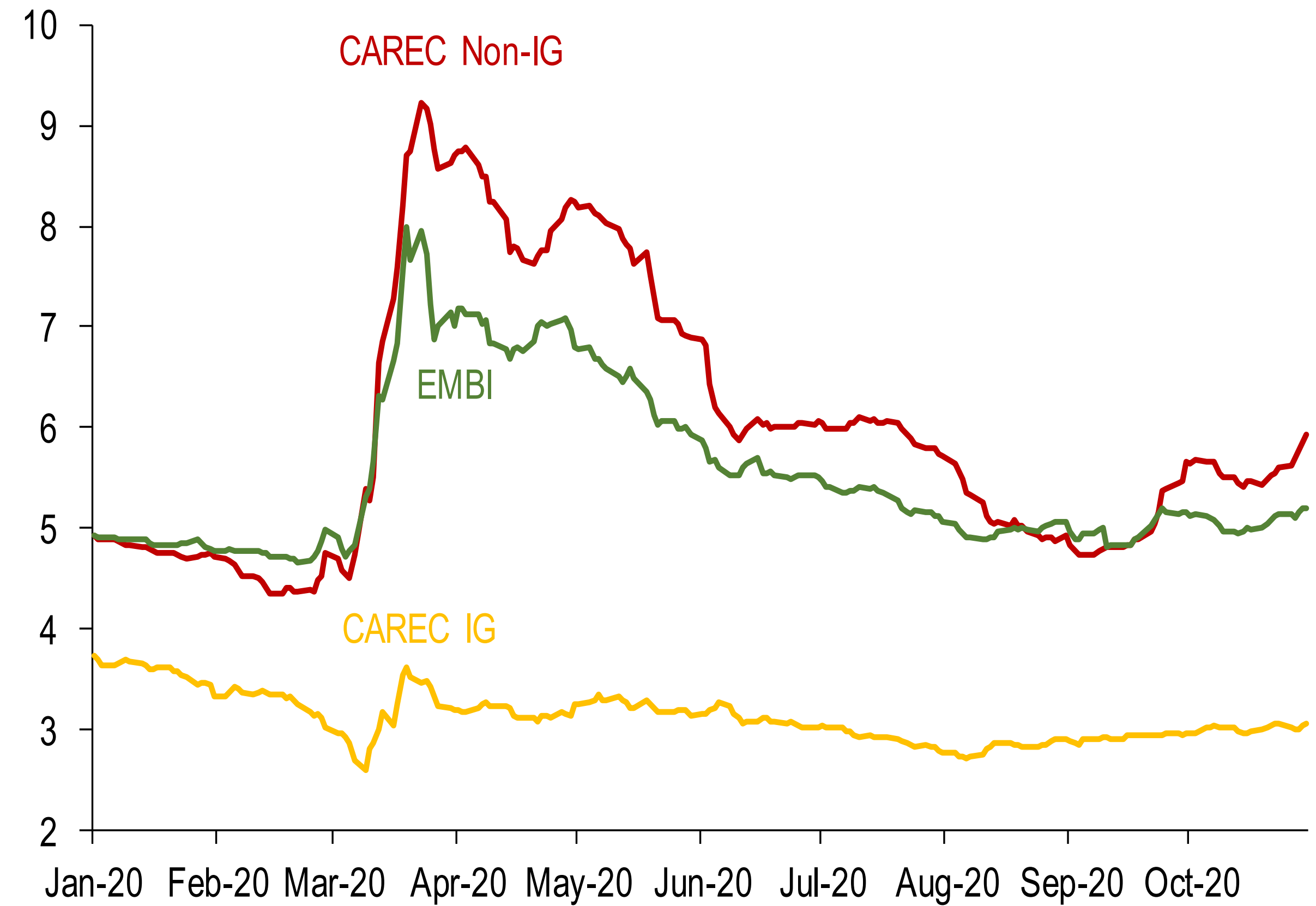


Financial Conditions Eased at a Slower Pace in CAREC Economies

EM and CAREC Financial Conditions Indices
(Standard deviations from 2019Q4)

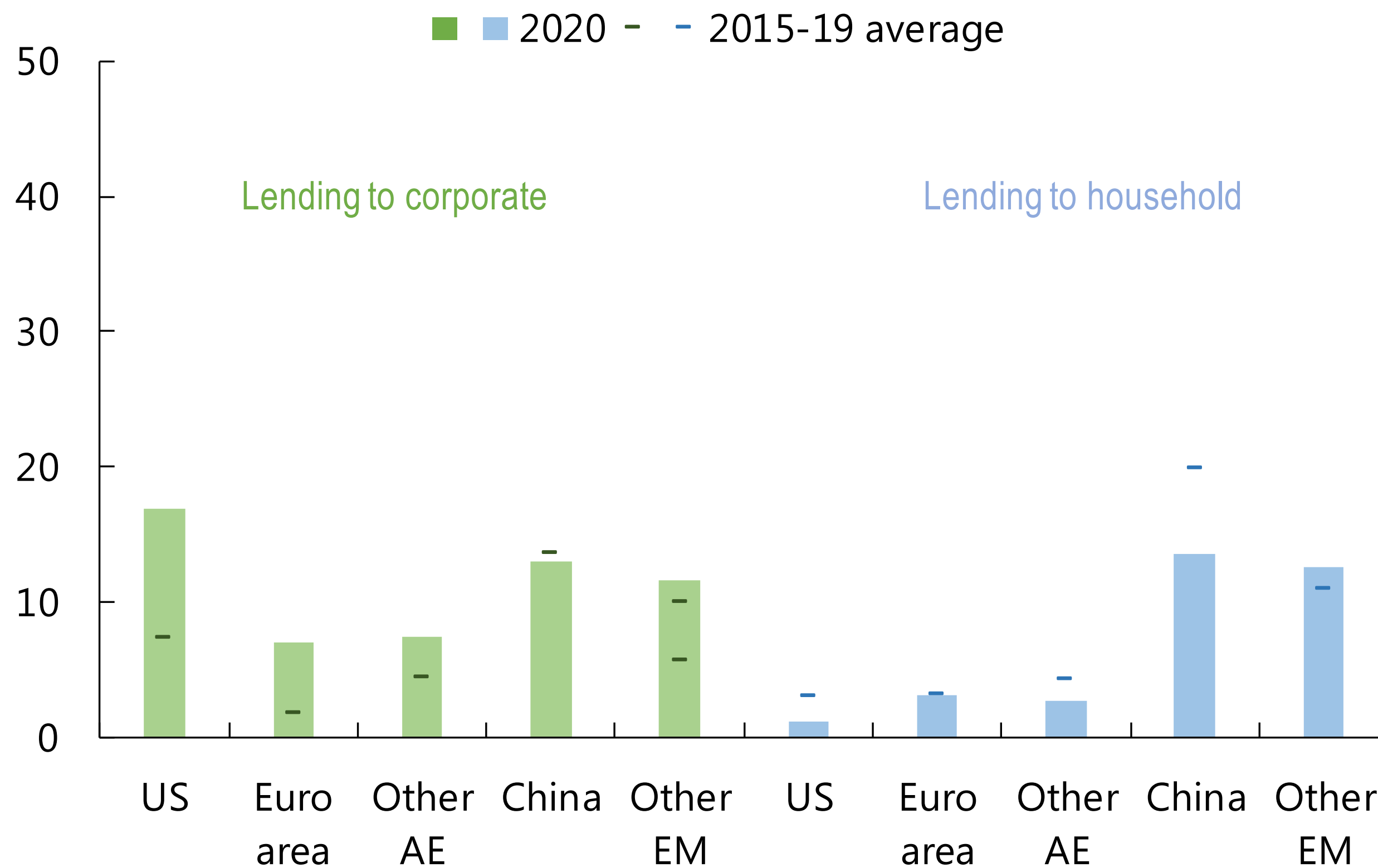


Hard Currency Bond Yields in EMs and CAREC Economies
(Percent)

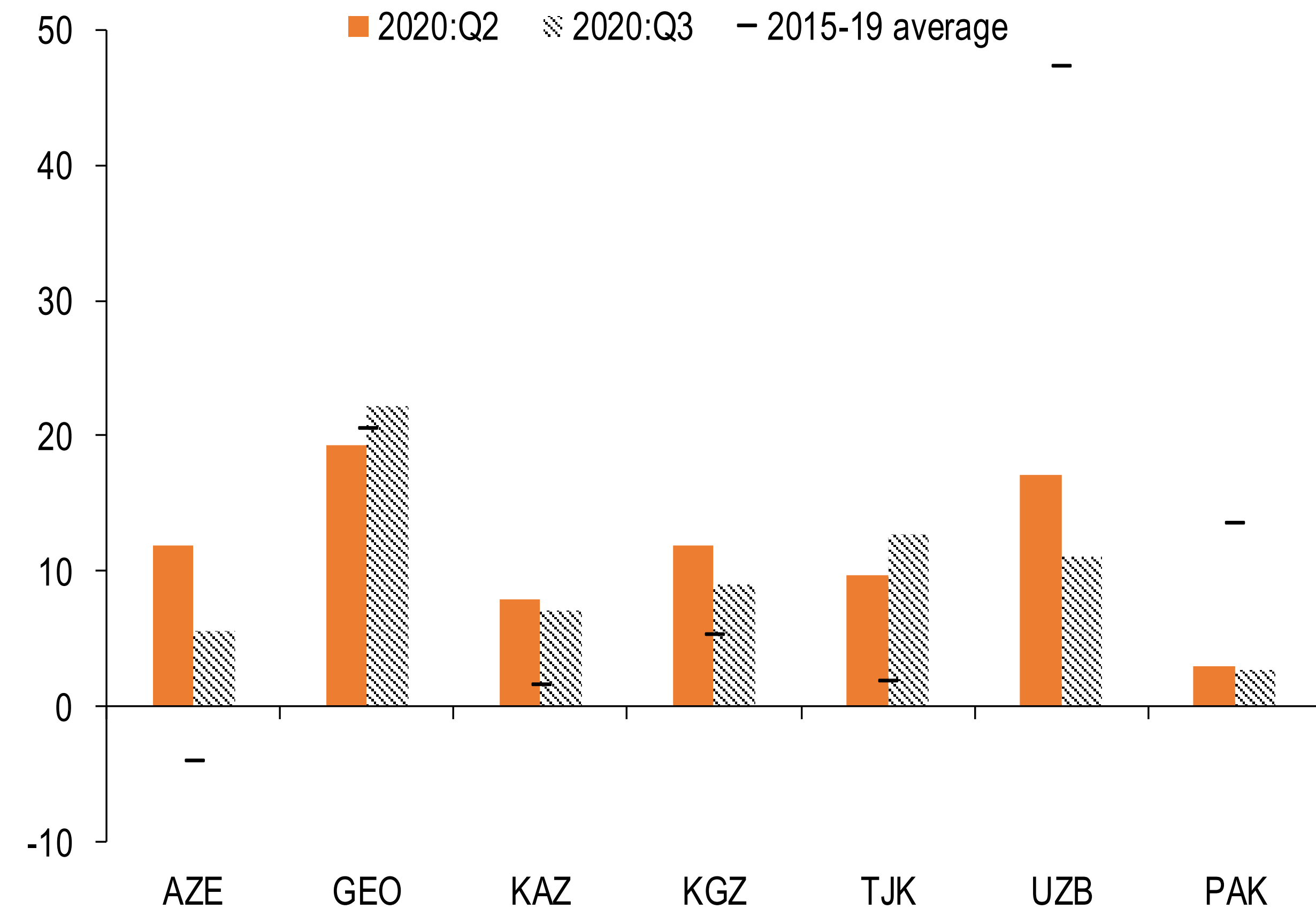


The Flow of Credit to the Economy Has Been Maintained

Bank Credit Growth in AEs and EMs, 2020:Q2
(Percent)

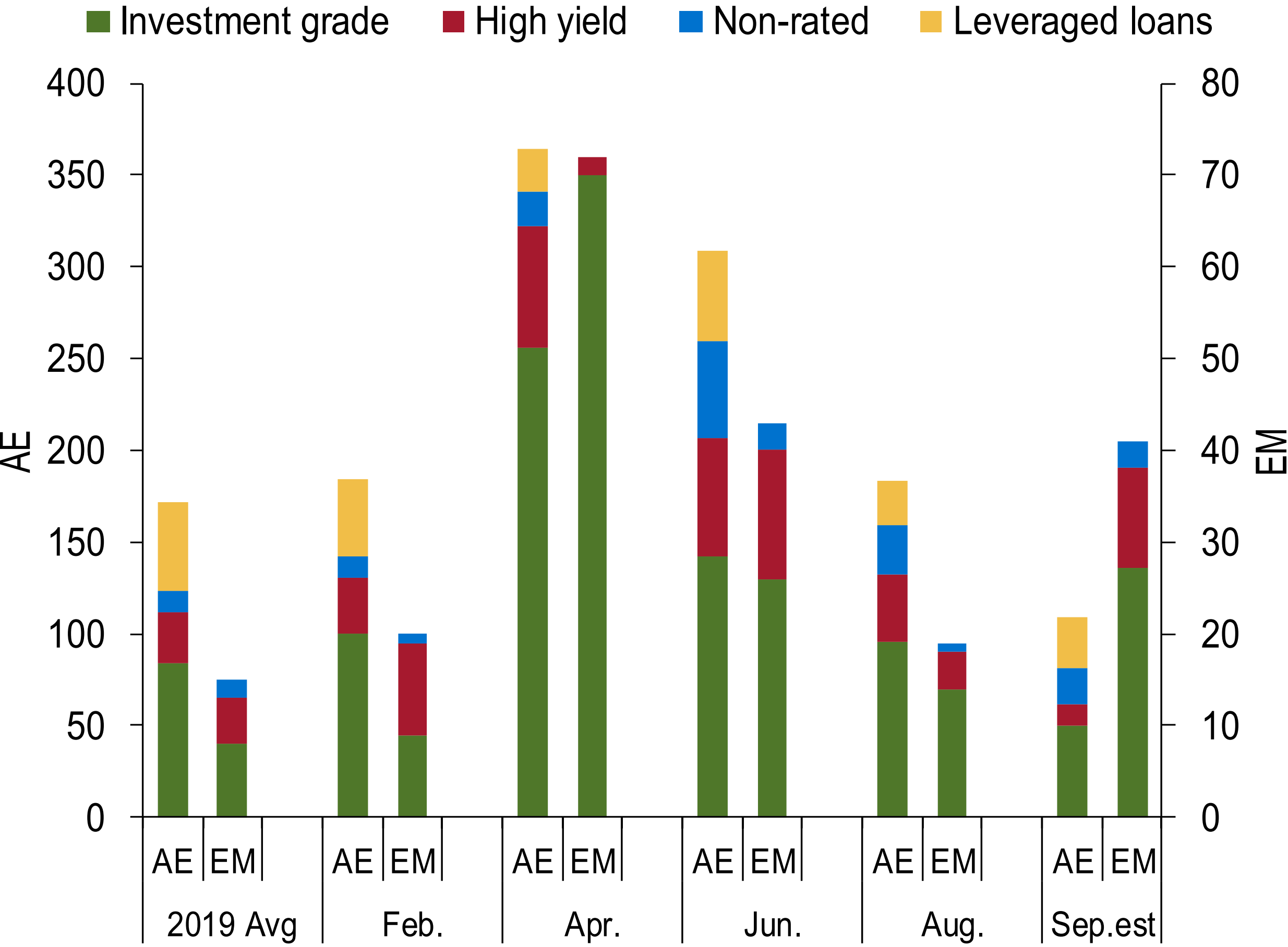


Bank Credit Growth in Selected CAREC Economies, 2020
(Percent)

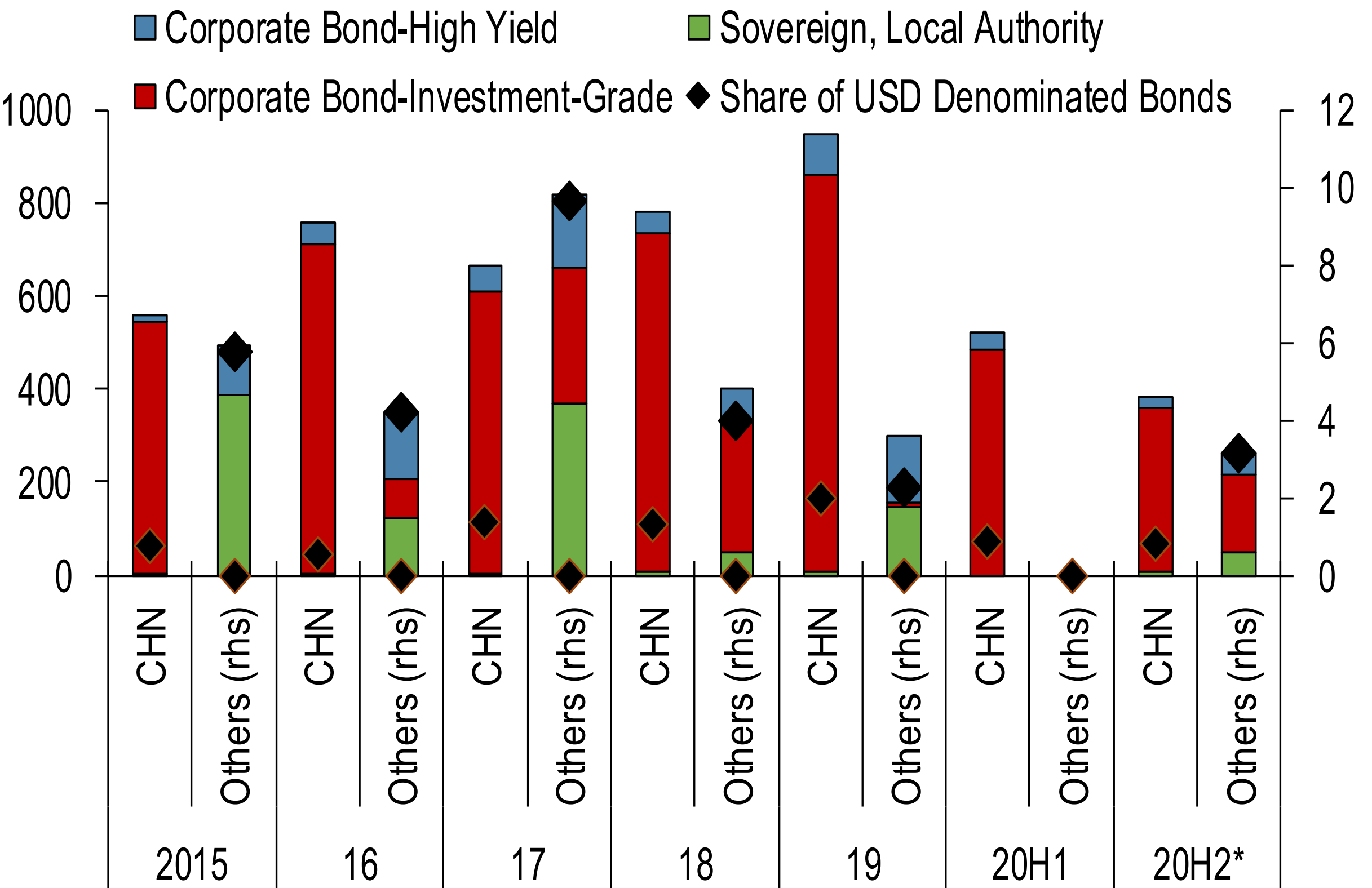


Risky Firms Face Loss of Market Access Despite Bond Market Recovery

AE Corporate Bond and Leverage Loan Issuance
EM Corporate and Sovereign Bond Issuance
(Billions of US dollars)

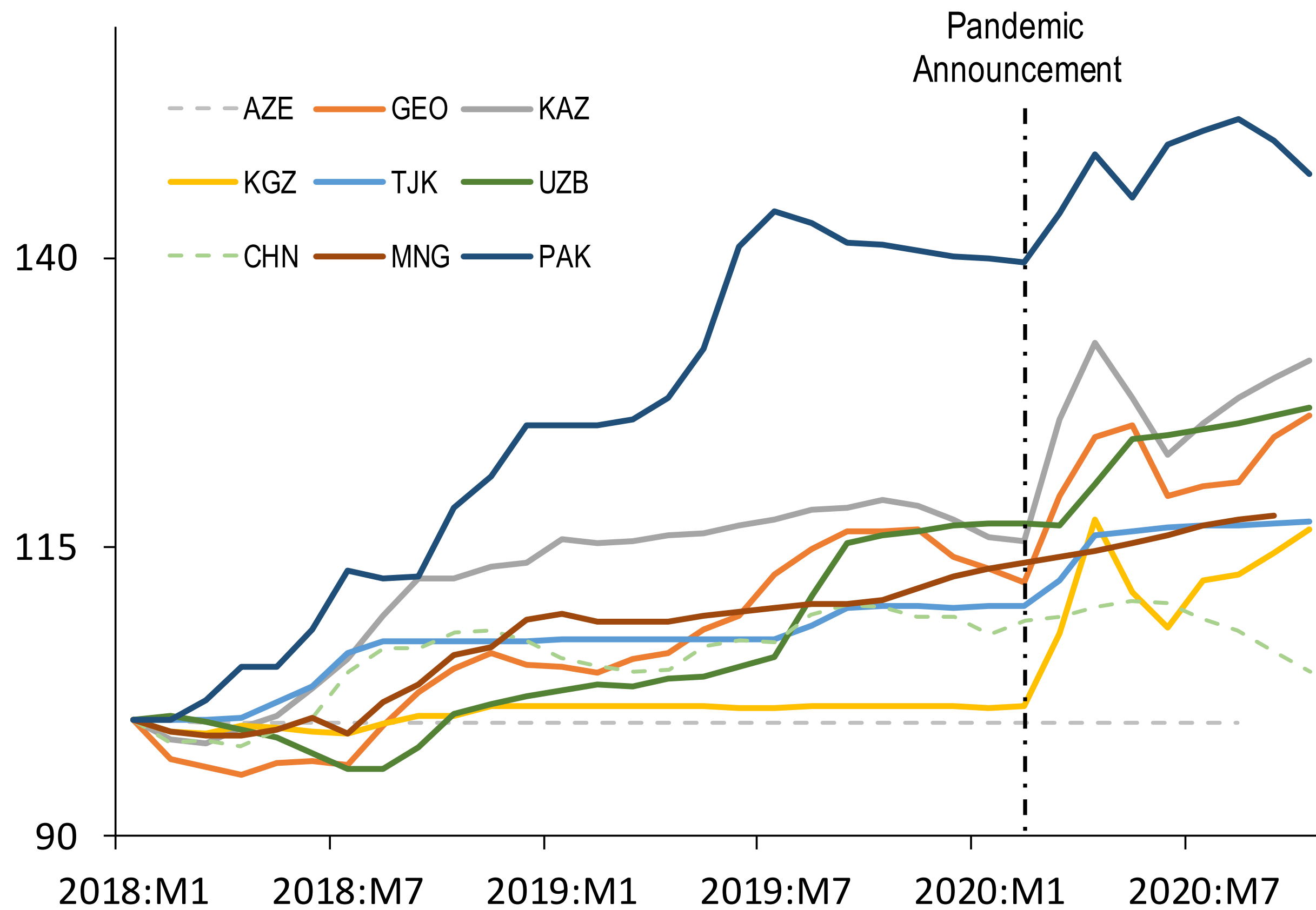


CAREC Economies Corporate and Sovereign Bonds
Issuance Amount by Types and Currency Denominations
(Billions of US dollars)

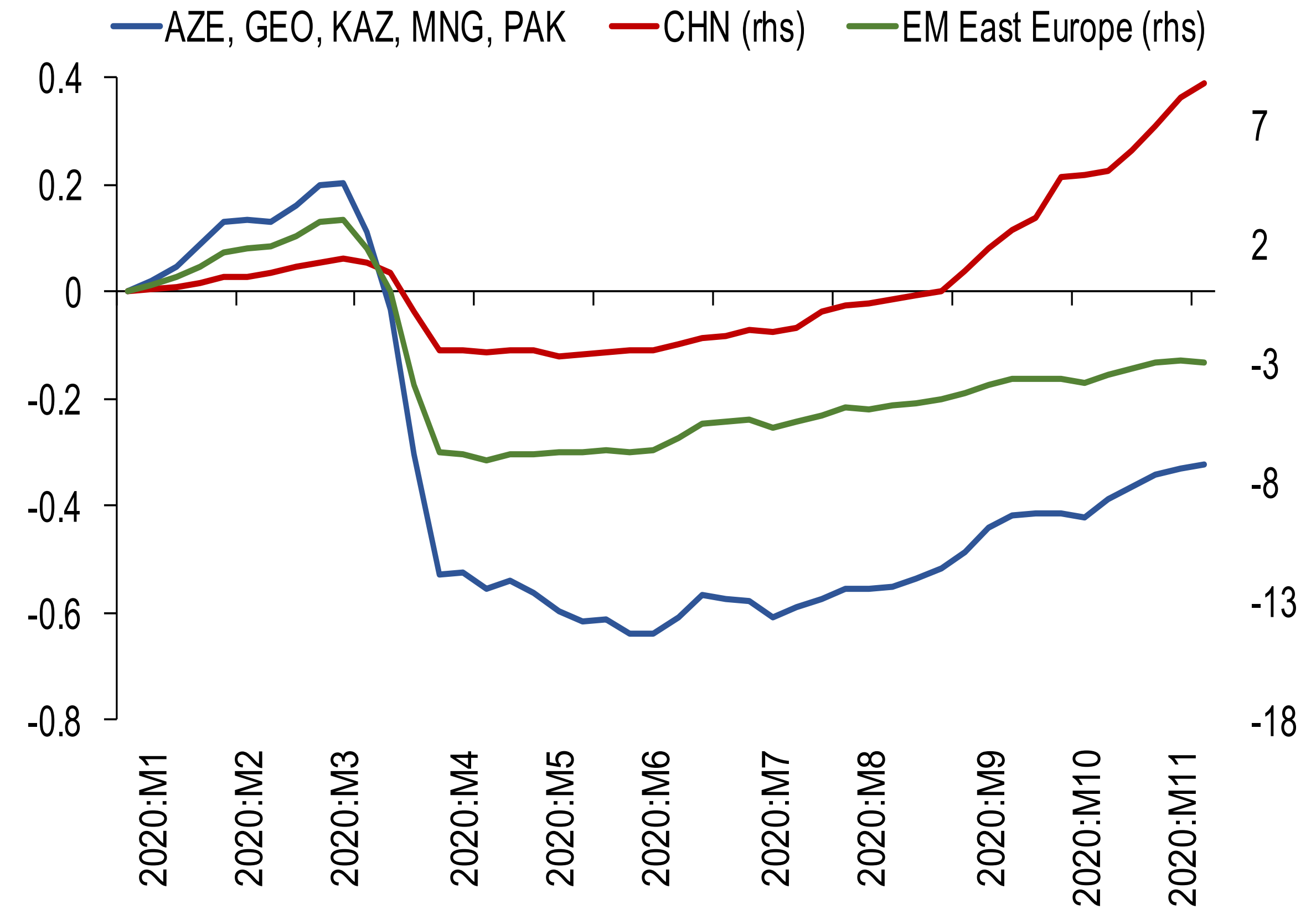


FX Depreciation Pressure Persists and Bond Inflows Are Sluggish

Nominal Exchange Rate
(Local currency per USD, 2018M1 = 100)



Bonds Fund Flows to CAREC Economies
(Cumulative, year to date, billions of US dollars)



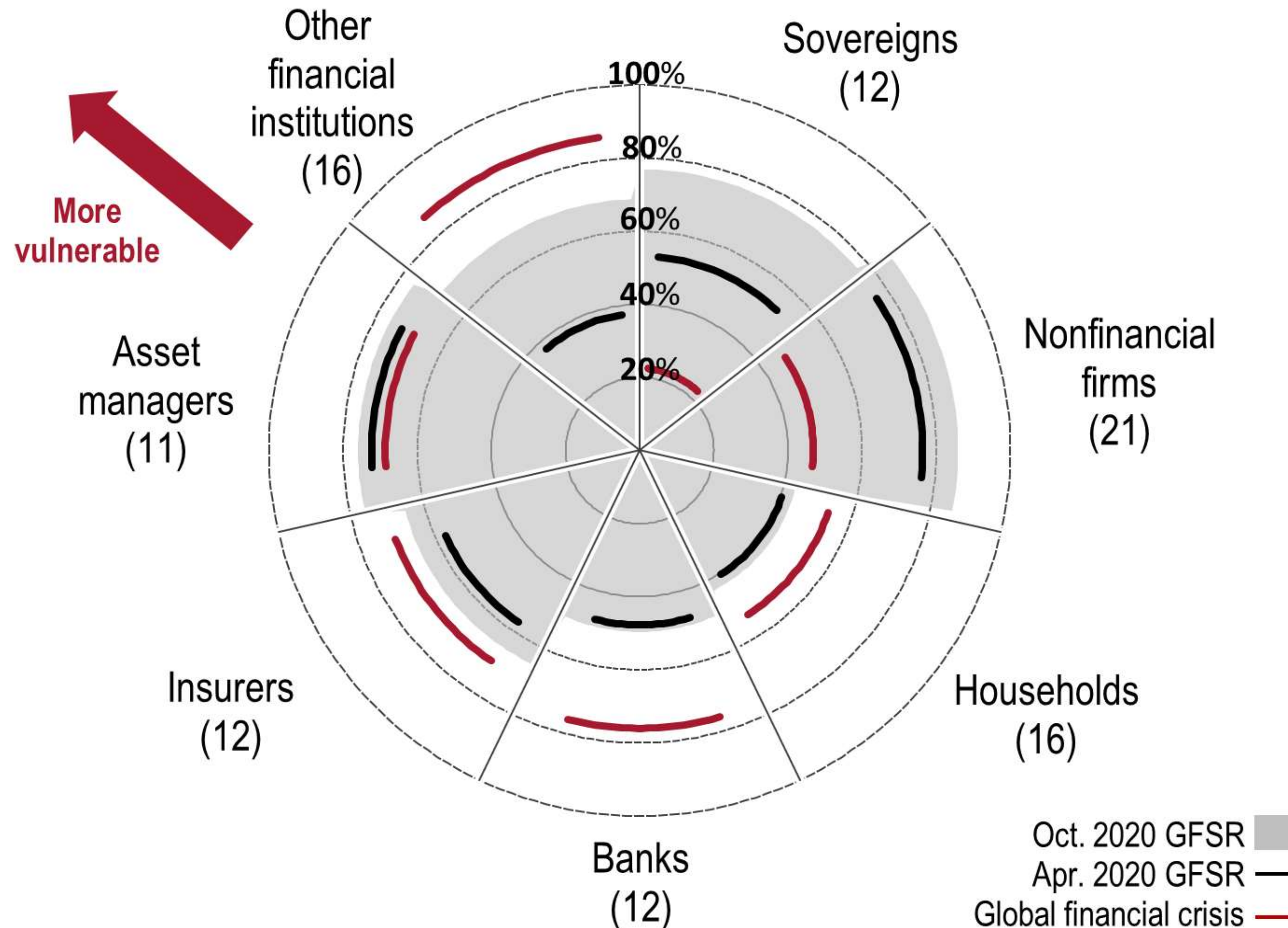
Vulnerabilities are rising...



Many Countries Entered the Pandemic with Pre-existing Vulnerabilities

Ratio of Systemically Important Countries with Elevated Vulnerabilities, by Sector

(Percent of countries with high and medium-high vulnerabilities, by GDP [assets for banks, asset managers, other financial institutions and insurers]; number of vulnerable countries in parentheses)



Corporate Sector: Policy Tradeoffs

**From
“whatever it
takes”
today...**

More liquidity support today...

- Collapse in revenues led firms to increase borrowing
- Liquidity support kept bankruptcies at bay
- Impact uneven across countries and sectors

**...to
phasing out
extraordinary
policy
support**

... solvency risks postponed into the future

- Liquidity extended to nonviable firms
- Debt overhang
- Misallocation of resources

Banks: Policy Tradeoffs

**From
“whatever
it takes”
today...**

Greater use of buffers by banks today...

- Banks entered the crisis with reasonable capital & liquidity
- Borrower support policies and flexibility in regulatory frameworks have further supported bank lending

**...to
phasing out
extraordinary
policy
support**

... less capacity to lend tomorrow

With low profitability & rising NPLs ahead, depletion of capital & liquidity buffers may...

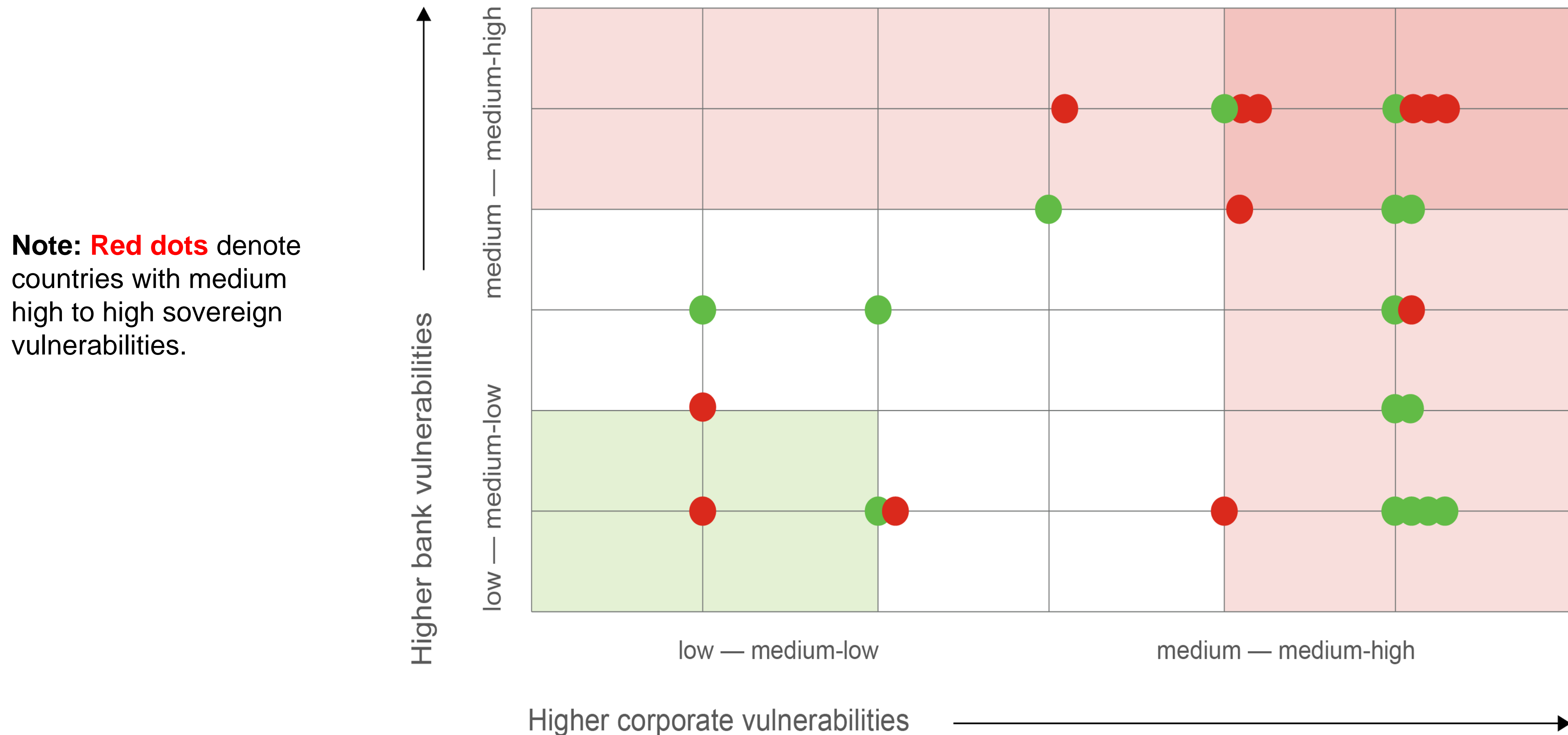
- leave banks vulnerable
- and force them to scale back lending

Policy Priorities



Vulnerabilities in Multiple Sectors; Policy Space Shrinking

Corporate, Bank, and Sovereign Vulnerabilities in the 29 Economies with Systemic Financial Sectors



A Bridge to Recovery: Policy Trade offs

Unprecedented policy support has:

- Kept markets functioning
- Maintained the flow of credit
- Avoided adverse macro-financial feedback loops...
- ...and widespread bankruptcies

... but may exacerbate future vulnerabilities:

- Real-financial disconnect
- Rising debt and insolvencies
- Depletion of buffers
- Excessive risk-taking

Near-Term Policies

- **Monetary policy:** maintain accommodation if possible
- **Liquidity support:** continue but adjust pricing to incentivize exit
- **Banks:** encourage the use of capital and liquidity buffers
- **Borrower support:** extend moratoria (if needed); facilitate debt restructuring; efficient out-of-court workouts
- **Sovereigns:** support EMEs and LIDCs with financing difficulties

Medium- and Longer-term Policies

- **Monetary** accommodation if possible until objectives achieved
- **Liquidity support:** withdraw gradually once pandemic under control
- **Banks:** rebuild buffers & reduce problem assets over time
- **NBFIs:** enhance the regulatory framework
- **Debt overhang:** recapitalize/restructure/resolve nonviable firms
- **Lower for longer:** contain excessive risk-taking via prudential policies

A Bridge to Recovery

