

ASEAN+3 FINANCIAL STABILITY REPORT 2023



**Navigating High Debt in
Low Visibility**



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Table of Contents

Message from AMRO Director	x
Foreword from the Chief Economist	xi
Acknowledgements	xii
Abbreviations	xiii
Executive Summary	1
Financial market stability under multiple trials	2
Low visibility of challenges to financial stability	4
Higher debt spurred by ample liquidity and pandemic measures	5
Financial stability risks and vulnerabilities from higher debt	6
Policy recommendations	7
Chapter 1. Market Conjunctural – Low Visibility of Challenges Ahead	8
Highlights	9
I. Recent Developments	10
Global financial conditions have eased, although risks linger	10
ASEAN+3 markets have weathered the storm from global markets	11
The pace of monetary policy tightening has generally slowed	15
Portfolio investments ebb and flow	18
II. Risks	21
Inflation may persist and see a resurgence	21
Markets may need to adjust to the “higher-for-longer” new normal	23
ASEAN+3 markets have avoided US and Europe banking stress but risks linger	24
US dollar funding remains ample though is receding at the margin	26
Technological advancements present new opportunities and challenges	28
III. Policy Discussion	31
References	37
Chapter 2. Navigating High Debt in Low Visibility – Assessing Private Debt Vulnerabilities	39
Highlights	40
I. Overview	41
At what level is debt too high?	42
II. Corporate Debt	43
Which firms are more vulnerable?	43
What drives corporate debt in ASEAN+3?	45
How are corporate profitability and liquidity performing?	45
What drives change in corporate financing vulnerabilities?	46
Are higher interest rates putting firms under stress?	50
What are the recommended policy responses?	51
III. Household Debt	53
What drives the dynamics of household debt in ASEAN+3?	53
How do higher interest rates affect household debt burdens?	54
What are the risks of a major real estate correction?	56
Household debt vulnerabilities and macroprudential policies	60
References	72

Chapter 3. Navigating High Debt in Low Visibility – Assessing Public Debt Vulnerabilities 74

Highlights	75
I. Introduction	76
II. Assessing Financial Stability Risks from Fiscal Debt in ASEAN+3	77
Does a higher debt-to-GDP ratio increase the likelihood of fiscal crisis?	77
How vulnerable is ASEAN+3 fiscal debt to a worsening in financial market conditions?	78
III. Policy Implications	84
References	91

Chapter 4. Navigating High Debt in Low Visibility – Assessing Resilience of Financial Intermediaries 92

Highlights	93
I. Introduction	94
II. Banks	94
Banks are major providers of credit in the region	94
Broadly, ASEAN+3 banking sectors are relatively sound	96
Some shifts in financing sources are occurring for ASEAN+3 banks	98
Banks should strengthen liquidity buffers to better insulate from external shocks	100
Elevated interest rates are a double-edged sword for banks	106
Policies can safeguard financial stability in ASEAN+3 banking	107
III. Nonbank Financial Intermediaries	110
The development of NBFIs varies across ASEAN+3	111
NBFIs give rise to risks to financial stability	114
Policies to contain risk to financial stability from NBFIs	115
References	121

Boxes

Box 1.1	Correlations of ASEAN+3 Asset Prices with US and China Markets	14
Box 1.2	Valuations of Regional Equity and Bond Markets	19
Box 1.3	The Uptick in Commodity Prices	22
Box 1.4	Cryptocurrencies and Banking Sector Connectedness	29
Box 1.5	Impacts of Federal Reserve Policy Tightening on the ASEAN+3 Economies	33
Box 1.6	The Impact of Green Lending on Financial Risk	35
Box 2.1	US Dollar Debt of Chinese Corporates	48
Box 2.2	Behind Korea's Housing Market Cycle	58
Box 4.1	Beta Analysis of Banks and NBFIs	102
Box 4.2	Impact of Rising Interest Rates on Malaysian Banks' Liquidity	104
Box 4.3	NBFI Financing in Thailand	113
Box 4.4	Dollar Finance in ASEAN+3	116

Annexes

Annex 2.1	Estimation of Nonfinancial Debt Thresholds	62
Annex 2.2	Policies to Facilitate MSME Financing	64
Annex 2.3	Methodology for Identifying Correlates of Credit Growth	67
Annex 2.4	Empirical Study to Assess the Drivers of Corporate Bonds	68
Annex 2.5	Machine Learning for Early Prediction of Corporate Distress	69
Annex 2.6	Empirical Study on The Drivers of Household Credit	70
Annex 2.7	House Price Misalignment Model	71
Annex 3.1	How Does the Government Debt-to-GDP Ratio Affect Fiscal Crisis Likelihood?	86
Annex 3.2	How Does the Composition of Government Debt Holders Impact Sovereign Default Risk in ASEAN+3?	88
Annex 4.1	Bank Simulation Exercise – Implications of Higher Interest Rate Environment	117
Annex 4.2	Methodology: Early Identification of Banking Crisis	119

Figures

Figure E.1.	Selected Advanced Economies: Financial Conditions Index (FCI)	2
Figure E.2.	US: Volatility in Key Assets and Corresponding Long-Term Averages	2
Figure E.3.	US and Euro Area: Banking Sector Stock Indices	3
Figure E.4.	Selected Advanced Economies: Balance Sheets of Major Central Banks	3
Figure E.5.	Selected ASEAN+3: Changes in Financial Markets, 2022 and 2023	3
Figure E.6.	Selected ASEAN+3: Policy Rate Changes, 2022 and 2023	3
Figure E.7.	Market and Fed's Projected Policy Rates Since the Start of the US Hiking Cycle	4
Figure E.8.	US and Selected ASEAN+3: Drawdown and Recovery in Banking and Financial Index after the Banking Turmoil	4
Figure E.9.	US and ASEAN+3: Market Betas for Banking and NBFIs Sectors	4
Figure E.10.	World: Nonfinancial Sector Debt-to-GDP by Region	5
Figure E.11.	Selected ASEAN+3: Nonfinancial Sector Debt-to-GDP Ratios, 2022	6
Figure 1.1.	Selected Advanced Economies: Financial Conditions Index (FCI)	10
Figure 1.2.	Selected Advanced Economies: 10-Year Nominal, Inflation Expectations and Real Government Bond Yields	10
Figure 1.3.	Selected Advanced Economies: Equity, Foreign Exchange and Bond Market Indices	11
Figure 1.4.	US: Volatility in Key Assets and Corresponding Long-Term Averages	11
Figure 1.5.	US: Banking Sector Stock Indices	11
Figure 1.6.	Selected Advanced Economies: Balance Sheets of Major Central Banks	11
Figure 1.7.	Selected ASEAN+3: Changes in Financial Markets, 2022 and 2023	12
Figure 1.8.	Selected ASEAN+3: Realized Returns and Volatility in Financial Assets, 2020–2021 versus 2022–Now	13
Figure 1.9.	Selected ASEAN+3: Market Stress Indicator	13
Figure 1.10.	Selected ASEAN+3: Contributors to Change in Market Stress in 2022	13
Figure 1.11.	Selected ASEAN+3: Contributors to Change in Market Stress in 2023, January to October	13
Figure 1.12.	Selected ASEAN+3: Size of Foreign Exchange Reserves	16
Figure 1.13.	ASEAN+3: Reserve Adequacy	16
Figure 1.14.	Selected ASEAN+3: Policy Rate Changes, 2022 and 2023	17
Figure 1.15.	Selected Advanced Economies: Size of Balance Sheets of Central Banks	17
Figure 1.16.	China: Key Interest Rates	17
Figure 1.17.	US: Market-implied Policy Rates at Forthcoming FOMC Meetings	17

Figure 1.18.	Selected ASEAN+3: Market-implied Changes in Policy Rates	17
Figure 1.19.	Emerging Markets: Annual Portfolio Flows	18
Figure 1.20.	Emerging Markets: Monthly Portfolio Flows	18
Figure 1.21.	Selected ASEAN+3: Monthly Equity Flows	18
Figure 1.22.	Selected ASEAN+3: Monthly Debt Flows	18
Figure 1.23.	Selected ASEAN+3: Headline and Core Inflation, Inflation Targets	21
Figure 1.24.	Market and Fed's Projected Policy Rates since the Fed's Hiking Cycle Started	23
Figure 1.25.	Projected (at the Start of Year) versus Actual (at the End of Year) Policy Rates	23
Figure 1.26.	Intra-Meeting Change in Market Projections	23
Figure 1.27.	US: Inflation Expectations and Real Rates since 2008	24
Figure 1.28.	Selected ASEAN+3: Sensitivity of Asset Prices to US Inflation Expectations and Real Yields	24
Figure 1.29.	US and Selected ASEAN+3: Drawdown and Recovery in Banking and Financial Index after the Banking Turmoil	25
Figure 1.30.	US and ASEAN+3: Market Betas for Banking and NBFIs Sectors	25
Figure 1.31.	Selected ASEAN+3 and Selected Advanced Economies: Share of Banking Sector Loans and Securities, Q2 2023	25
Figure 1.32.	Selected ASEAN+3: Composition of Deposits, Q2 2023	25
Figure 1.33.	US: Proxies for Surplus US Dollar Liquidity	27
Figure 1.34.	US: Selected Interest Rate Spreads	27
Figure 1.35.	US: Outstanding Public Debt and US Treasury Inventory with Primary Dealers	27
Figure 1.36.	US: Selected Liquidity Facilities Provided by the Fed since 2019	27
Figure 1.37.	Selected Major Currencies: Cross Currency Swaps	27
Figure 1.38.	Selected ASEAN+3: US Treasuries Held by Entities based in ASEAN+3	27
Figure 1.39.	ASEAN+3: Share of US Dollars in External Assets and Liabilities of Banks	28
Figure 1.40.	ASEAN+3: Share of US Dollars in Foreign Currency Bond Issuances	28
Figure 2.1.	Selected ASEAN+3: Corporate, Government and Household Debt	41
Figure 2.2.	Selected Regions: Share of Nonfinancial Debt of Corporates, Governments, and Households	41
Figure 2.3.	Selected Regions: Annual Growth in Corporate Debt	41
Figure 2.4.	Selected Regions: Corporate Debt	41
Figure 2.5.	Selected ASEAN+3: Private Debt	42
Figure 2.6.	Selected Regions: Household Debt	42
Figure 2.7.	Selected ASEAN+3: Household Debt	42
Figure 2.8.	Selected ASEAN+3: Nonfinancial Debt-to-GDP Ratio and Standard Deviation	43
Figure 2.9.	Selected ASEAN+3: Share of Corporate Debt by Firm Type, 2022	44
Figure 2.10.	Selected ASEAN: Interest Coverage Ratio	44
Figure 2.11.	Plus-3: Interest Coverage Ratio	44
Figure 2.12.	Selected ASEAN+3: Share of Corporate Debt by Sector, 2022	44
Figure 2.13.	Selected ASEAN: Corporate Credit Ratings	44
Figure 2.14.	Plus-3: Corporate Credit Ratings	44
Figure 2.15.	Selected Regions: Decomposition Analysis of Change in Credit-to-GDP, Pre-COVID	45
Figure 2.16.	Selected Regions: Decomposition Analysis of Change in Credit-to-GDP, COVID	45
Figure 2.17.	ASEAN+3: Median Return on Assets by Sector	46
Figure 2.18.	ASEAN+3: Median Return on Assets by Economy	46
Figure 2.19.	ASEAN+3: Median Current Assets to Current Liabilities by Sector	46
Figure 2.20.	ASEAN+3: Median Cash Cover by Sector	46
Figure 2.21.	Selected ASEAN+3: Share of Corporate Credit in Bonds	47
Figure 2.22.	Selected ASEAN+3: Share of Corporate Credit in Corporate Bond by Economy, Pre-COVID versus COVID	47
Figure 2.23.	Selected ASEAN+3: Share of Corporate Bond by Maturity	47

Figure 2.24.	ASEAN+3: Drivers of Corporate Bonds, 2012–22	47
Figure 2.25.	Selected ASEAN+3: Share of Corporate Bond by Currency	47
Figure 2.26.	Selected ASEAN+3: Share of Corporate Bond by Currency, Q1 2023	47
Figure 2.27.	Selected ASEAN+3: Share of Firms Under Stress, 2022 (Simulation Results)	50
Figure 2.28.	Selected ASEAN+3: Share of Debt Under Stress, 2022 (Simulation Results)	50
Figure 2.29.	Selected ASEAN+3: Importance of Indicators to Predict ICR<1.25X by Economy	51
Figure 2.30.	Selected ASEAN+3: Importance of Indicators to Predict ICR<1.25X by Sector	52
Figure 2.31.	Selected ASEAN: Change in Share of Distressed Firms	52
Figure 2.32.	Plus-3: Change in Share of Distressed Firms	52
Figure 2.33.	Selected Regions: Average Tightening of Macroprudential Policies	52
Figure 2.34.	Selected Regions: Average Loosening of Macroprudential Policies	52
Figure 2.35.	Selected ASEAN+3: Contribution to Macroeconomic Driver to Household Credit Growth	54
Figure 2.36.	Selected ASEAN+3: Correlation of Household Debt Growth and Foreign Bank Inflows	54
Figure 2.37.	World and ASEAN+3: Capital Inflows from Banks	54
Figure 2.38.	Japan and Korea: Household Debt-to-GDP, Debt Service Ratios, and Interest Rate	55
Figure 2.39.	Selected ASEAN+3: Estimated Debt Burden, Household Debt to GDP, and Interest Rate	55
Figure 2.40.	World and Selected ASEAN+3: Housing Price Growth	57
Figure 2.41.	Selected ASEAN+3: Real House Price versus Predicted Value from a Model of Fundamental House Prices	57
Figure 2.42.	Selected ASEAN+3: Drivers of House Price Growth	57
Figure 2.43.	ASEAN+3: Change in Stance of Macroprudential Policies Targeting Household Debt	61
Figure 2.44.	Selected ASEAN+3: Loan-to-Value Ratio	61
Figure 3.1.	Selected ASEAN+3 and Rest of World: Share of Public Debt in Total Debt Stock	76
Figure 3.2.	World and ASEAN+3: Trend of Public Debt-to-GDP Ratios	76
Figure 3.3.	World and Selected ASEAN+3: Level of Public Debt-to-GDP Ratios	77
Figure 3.4.	World and Selected Economies: Average Annual Change Rate of Public Debt-to-GDP Ratios	77
Figure 3.5.	World and Selected ASEAN+3: Predictive Probability of A Fiscal Crisis Happening at Different Public Debt-to-GDP Levels	78
Figure 3.6.	Selected ASEAN+3, US, UK and Germany: Weighted Average Remaining Maturity of Government Bonds	79
Figure 3.7.	Selected ASEAN+3 and US: Maturity Profile of Government Bonds	79
Figure 3.8.	Selected ASEAN+3: Central Government Debt Securities by Instrument	80
Figure 3.9.	Euro area, US and Selected ASEAN+3: US 10-Year Treasury Bond Yield and Bond Price Indices Movement	80
Figure 3.10.	Selected ASEAN+3: Example of Interest Rate Risk for Banks Holding Government Debt	80
Figure 3.11.	World and Selected ASEAN+3: Foreign Currency Debt Securities Ratio in General Government Debt Securities	81
Figure 3.12.	Selected ASEAN+3: General Government Foreign Currency Debt Securities-to-Foreign Currency Reserves Ratio	81
Figure 3.13.	Selected ASEAN+3: Investor Composition of General Government Gross Debt	82
Figure 3.14.	Selected Regions: Share of General Government Gross Debt Held by Foreign Investors	82
Figure 3.15.	Selected ASEAN+3: Contributions to Change in CDS Spreads	82
Figure 3.16.	ASEAN-4: Contributions to Change in CDS Spreads	82
Figure 3.17.	Selected ASEAN+3 and US: Turnover Ratio of Government Bonds	83
Figure 3.18.	Selected ASEAN+3: Average Bid-Ask Spreads for On-The-Run Government Bonds	83
Figure 3.19.	Selected Advanced Economies: Liquidity Indices of Treasury Bond Market	83
Figure 4.1.	Selected Regions: Share of Financial Assets by Type of Financial Institution, 2021	95
Figure 4.2.	Selected Regions: Credit-to-GDP Ratio	95
Figure 4.3.	Selected Regions: Credit-to-GDP Gap	95

Figure 4.4.	ASEAN: Sectoral Credit, 2022	95
Figure 4.5.	Plus-3: Sectoral Credit, 2022	95
Figure 4.6.	ASEAN+3: Improvement in Bank Vulnerability Index (BVI) Factors, 2013–22	96
Figure 4.7.	Selected Regions: Total Capital Adequacy Ratio (CAR)	96
Figure 4.8.	Selected Regions: Tier 1 Capital Adequacy Ratio (CAR)	97
Figure 4.9.	Selected Regions: Nonperforming Loan (NPL) Ratio	97
Figure 4.10.	Selected Regions: Return on Asset	98
Figure 4.11.	Selected Regions: Interest Margin to Gross Income	98
Figure 4.12.	Selected Regions: Bank Liabilities	99
Figure 4.13.	Selected Regions: Share of Bank Liabilities	99
Figure 4.14.	ASEAN: Share of Foreign Claims on Banks by Counterparty Economy	99
Figure 4.15.	Hong Kong and Singapore: Share of Foreign Claims on Banks by Counterparty Economy	99
Figure 4.16.	Plus-3 Excluding IFC: Share of Foreign Claims on Banks by Counterparty Economy	99
Figure 4.17.	Selected ASEAN+3: Cross Border Bank Loans, Q4 2022	99
Figure 4.18.	Selected ASEAN+3: Cross Border Bank Borrowings, Q4 2022	100
Figure 4.19.	ASEAN+3: Quarterly Growth Rate of Cross Border Bank Borrowings	100
Figure 4.20.	ASEAN+3: Cross Border Bank Loans by Foreign Currencies, 2022	100
Figure 4.21.	ASEAN+3: Cross Border Bank Borrowings by Foreign Currencies, 2022	100
Figure 4.22.	Selected Regions: Loan-to-Deposit Ratio	101
Figure 4.23.	Selected Regions: Average Liquid Asset-to-Short-Term Liabilities, Pre-COVID and COVID	101
Figure 4.24.	ASEAN+3: Improvement in Average Bank Vulnerability Index (BVI) Liquidity Factor, Pre-COVID and COVID	101
Figure 4.25.	Selected ASEAN+3: Effect of 100bps Increase in Interest Rate on NPL Ratios	106
Figure 4.26.	Selected ASEAN+3: Effect of 100bps Increase in Interest Rate on Growth in Net Interest Income	106
Figure 4.27.	Selected ASEAN+3: Estimated Probability of Crisis	107
Figure 4.28.	World and Selected ASEAN+3: Estimated Probability of Crisis, 2020 versus 2022	107
Figure 4.29.	World and ASEAN+3: Number of Macroprudential Policy Use, 2010–21	108
Figure 4.30.	ASEAN+3: Bilateral Currency Swap Agreements	109
Figure 4.31.	World and Selected ASEAN+3: Financing of Nonfinancial Private Sector by Banks and NBFIs	110
Figure 4.32.	Selected Economies: Financial Assets of Banks Relative to NBFIs	110
Figure 4.33.	Selected ASEAN+3: Banks and NBFIs Financing of Nonfinancial Private Sector	111
Figure 4.34.	Selected ASEAN+3: Credit Intermediation of NBFIs	112
Figure 1.1.1.	Spillovers from the US to ASEAN+3 Markets	14
Figure 1.1.2.	Spillovers from China to ASEAN+3 Markets	14
Figure 1.2.1.	US, Euro area, and Selected ASEAN+3: Forward Looking Price-to-Earnings Ratio	19
Figure 1.2.2.	US, Euro area, and Selected ASEAN+3: Equity Risk Premium	19
Figure 1.2.3.	Euro area and Selected ASEAN+3: 10-year Yield against 10-year US Treasury Yield	20
Figure 1.2.4.	Euro area and Selected ASEAN+3: FX Hedged 10-year Yield against 10-year US Treasury Yield	20
Figure 1.3.1.	Major Commodity Groups: Price Trends since 2020	22
Figure 1.3.2.	Selected Commodities: Price Trends since 2022	22
Figure 1.3.3.	Selected Commodities: Net Positions of Money Managers in Futures and Options	22
Figure 1.3.4.	Oil Prices: Decomposition of Price Changes in Supply and Demand Factors	22
Figure 1.4.1.	Cryptocurrencies Connectedness to G-SIBs	30
Figure 1.4.2.	G-SIBs Connectedness to Cryptocurrencies	30
Figure 1.4.3.	Single G-SIBs Maximum Connectedness to Cryptocurrencies and Another G-SIB	30
Figure 1.5.1.	Selected ASEAN+3: Impacts from US Fed's Policy Tightening on GDP, Inflation and Capital Flows	34

Figure 2.1.1.	Chinese NFCs' Offshore US Dollar Bond Issuance	49
Figure 2.1.2.	US Dollar Bond Defaults by Chinese NFCs	49
Figure 2.2.1.	Monthly Change in Housing Price and Housing Price Gap	59
Figure 2.2.2.	Housing Affordability Index (HAI)	59
Figure 2.2.3.	Financing Conditions and Housing Prices	59
Figure 2.2.4.	Demand and Supply Condition in the Jeonse (Leasehold) Market Conditions	59
Figure 2.2.5.	Housing Demand and Supply	59
Figure 4.1.1.	ASEAN+3: Market Betas for Banks	103
Figure 4.1.2.	ASEAN+3: Market Betas for NBFIs	103
Figure 4.1.3.	Selected ASEAN+3: Market Betas of Banking and NBFi Sectors	103
Figure 4.1.4.	Selected Plus-3 Markets: Market Betas for Banks and NBFIs	103
Figure 4.1.5.	IFCs and Thailand: Market Betas for Banks and NBFIs	103
Figure 4.1.6.	Selected ASEAN: Market Betas for Banks and NBFIs	103
Figure 4.2.1.	Overnight Policy Rate (OPR) and Short-term Market Rates	104
Figure 4.2.2.	Loan and Deposit Growth	104
Figure 4.2.3.	Loans-to-Fund Ratio of Malaysia's Banking System	105
Figure 4.2.4.	Liquid Assets-to-Total Asset Ratios of the Eight Largest Banks in Malaysia	105
Figure 4.2.5.	Fixed Deposits by Tenor	105
Figure 4.2.6.	Share of Individual Deposits	105
Figure 4.2.7.	Liquidity Coverage Ratio	105
Figure 4.2.8.	Deposit and Lending Rates	105
Figure 4.3.1.	Financing to Corporates by Type of Financial Institution	113
Figure 4.3.2.	Lending to Households by Type of Financial Institution	113
Figure 4.3.3.	Share of Bond Holdings by Corporate Bondholders, 2013	113
Figure 4.3.4.	Share of Bond Holdings by Corporate Bondholders, Q2 2023	113
Figure 4.4.1	ASEAN+3: Dollar Financing of Banks and NBFIs	116
Figure A2.2.1.	Summary of the Mechanism of CGSs	64
Figure A2.5.1.	ASEAN+3: Share of Feature Importance	69
Figure A3.2.1.	Selected ASEAN+3: Composition of Government Bonds by Holders and Debt-to-GDP	90
Figure A4.1.1.	Overview: Steps to Conduct the Simulation Exercise	117
Figure A4.1.2.	Coefficient Estimates	118
Figure A4.1.3.	Selected ASEAN+3: Nonperforming Loan Ratios	118
Figure A4.1.4.	Selected ASEAN+3: Total Capital Adequacy Ratios	118
Figure A4.1.5.	Selected ASEAN+3: Tier 1 Capital Adequacy Ratios	118
Figure A4.2.1.	Probability of Banking Crisis over the Next Five Years under a 1-Percentage Point Increase in Credit-to-GDP Gap Scenario	119
Figure A4.2.2.	Selected ASEAN: Estimated Probability of Banking Crisis Within Three Years	120
Figure A4.2.3.	Plus-3: Estimated Probability of Banking Crisis Within Three Years	120

Tables

Table 1.1.	ASEAN+3: Local Currency Promotion Schemes	28
Table 2.1.	Macroprudential Policy Tools Targeting Risks from Household Debt	60
Table 2.2.	ASEAN+3: Gaps in Data Needed for Effective Surveillance of Risks from High Household Debt	61
Table 4.1.	ASEAN+3: Year of Basel III Implementation	97
Table 4.2.	Selected ASEAN+3: Summary of Regulatory Forbearance Policies	98
Table 4.3.	Selected ASEAN+3: Summary of Deposit Insurance	109
Table 4.4.	Plus-3 and IFCs: Total Financial Asset Breakdown of NBFIs	112
Table 4.5.	Summary of Role and Risks of NBFIs Engaged in Maturity Transformation	115
Table A2.1.1.	Estimation of Nonfinancial Debt-to-GDP Thresholds	62
Table A2.1.2.	Regression Results	63
Table A2.1.3.	Summary Statistics of Debt-to-GDP Ratio	63
Table A2.2.1.	Selected ASEAN+3: Overview of CGSs	65
Table A2.2.2.	Selected ASEAN+3: Summary of Policy Banks	66
Table A2.3.1.	Empirical Results: Determinants of Change in Credit-to-GDP Ratio	67
Table A2.4.1.	Empirical Results: Determinants of Corporate Bond Share	68
Table A2.5.1.	List of Indicators	69
Table A2.6.1.	Regression Results of Panel Regression on Drivers of ASEAN+3 Household Credit	70
Table A2.7.1.	Panel Regression Results on House Price	71
Table A3.1.1.	Panel Logit Regression Results on Fiscal Crisis (Random Effects Model)	87
Table A3.1.2.	Average Marginal Effects of Variables on the Probability of a Fiscal Crisis (Global, Model 1)	87
Table A3.2.1.	Panel Regression Results on 5-year CDS Spreads (Cross Section Fixed Effects Model)	89
Table A4.1.1.	Selected ASEAN+3: Bank Solvency Test Results	118

Message from AMRO Director

The ASEAN+3 region is a bright spot in the world economy despite unprecedented risks and challenges. Having navigated the challenges posed by the Asian Financial Crisis and subsequent headwinds, our region has demonstrated wisdom and resilience through collective efforts aimed at fostering economic and financial stability.

Nonetheless, the risks and challenges are always lurking. The financial environment is changing rapidly and growing in complexity. As global and regional integration deepens, spillovers and contagion risks are on the rise.

Given the swiftly evolving global financial landscape and its substantial reverberations on the region, the significance of financial surveillance in ASEAN+3 cannot be overstated.

Enhancing financial surveillance plays a critical role in crisis prevention by facilitating the detection and assessment of financial vulnerabilities and risks. It reinforces the resilience of financial systems, ensuring the capacity to withstand shocks, in turn fostering economic growth and development within the region.

As the only international organization established under the ASEAN+3 Finance Process, AMRO must step up as a trusted policy advisor to our members, and strongly position itself as a thought leader with regional focus and global influence.

I am pleased to introduce the inaugural issue of AMRO's second flagship report, the *ASEAN+3 Financial Stability Report (AFSR)*. As the pioneer regional financial stability report in the ASEAN+3 region, the AFSR is a unique publication, embodying the principle 'of the region, for the region, and by the region'. Its release underscores our continuous commitment to monitor, protect, and enhance the financial stability of the ASEAN+3 region, a focus sharpened since the Asian Financial Crisis.

This flagship publication underscores our common objective to safeguard the financial stability of our region. It provides an extensive analysis of the current financial sector status, highlights risk factors, and delves into policy measures to address them effectively.

The AFSR launch is a substantial move toward reinforcing our core functions in financial surveillance, aligning with AMRO's Strategic Direction 2030. Under this framework approved by our Executive Committee in 2022, AMRO is set to contribute more significantly to secure the region's macroeconomic and financial resilience and stability. And the AFSR is among our high-priority initiatives in the coming years.

In light of the more complex and challenging financial landscape, we must continue to strengthen our surveillance capabilities, remain vigilant, and be ready to respond swiftly and decisively when needed to new shocks. Only then will we be able to navigate the treacherous journey ahead with confidence. We can expedite this journey by working together and supporting each other along the way.

Finally, I would like to take this opportunity to extend my heartfelt appreciation to AMRO's member authorities, Advisory Panel, and all who have contributed to this pivotal initiative.

As always, I look forward to hearing your feedback.

Kouqing Li
AMRO Director

Foreword from the Chief Economist

ASEAN+3 financial systems have been tested on multiple trials during the past two decades after the Global Financial Crisis but have remained resilient given the strengthened macroeconomic fundamentals, and improved regulatory and external buffers since the Asian Financial Crisis in the late 1990s.

Chapter 1 — *Market Conjunctural – Low Visibility of Challenges Ahead* — discusses recent market developments and notes the risks facing the ASEAN+3 economies within an evolving financial landscape. Over the last decade, global financial conditions have oscillated between tightening and easing, driven by factors such as the taper tantrum, Trump election, Brexit, COVID-19 pandemic, supply chain disruptions, rising inflation, and geopolitical events. However, since early 2022, global central banks led by the Federal Reserve, have responded to the escalation in headline inflation by rapidly tightening monetary policy, resulting in a marked shift from a state of “low-for-long interest rate with ample liquidity” to one characterized by “higher-for-longer interest rate with receding liquidity.” This has led to spikes in risk aversion, market sell-offs and capital outflows, and large currency depreciation against the US dollar in both advanced and emerging markets, including those in ASEAN+3. Policymakers have responded to these heightened volatilities by intervening judiciously in the markets, providing liquidity as needed to avoid disorderly market conditions and an overshoot of exchange rates and bond yields.

Despite recent disinflation, the persistence or potential resurgence of inflation has raised concerns about prolonged high interest rates and their impact on financial stability. While the spillover effects from the recent banking stress in the US and Europe have been limited, concerns over the health of the banking sector in the US linger. The possible emergence of US dollar funding stress, particularly if investor confidence falters amid global monetary tightening and elevated market volatility, is also an area of concern. Furthermore, accelerated cross-border capital flows, driven by greater financial market integration and digitalization, can rapidly transmit shocks, creating new challenges for policymakers.

Chapters 2 to 4 of the AFSR are thematic studies focusing on more in-depth analysis of the risks facing the region. For this inaugural issue, we have chosen the theme of *Navigating High Debt in Low Visibility* to assess the financial stability implications from higher debt in the region. The zero interest rate and abundant liquidity unleashed by the Quantitative Easing policy of the Fed and ECB in the aftermath of the Global Financial Crisis and European Sovereign Debt Crisis, had resulted in a low-for-long interest rate environment which enabled many businesses, households, and governments in this region to take on large amounts of debt at low costs. The exceptionally large monetary and fiscal stimulus measures during the COVID-19 pandemic fueled further increases in debt-to-GDP ratios in ASEAN+3. However, the phasing out of financial relief and regulatory forbearance policies and the shift to a higher interest rate environment, have led to concerns over the risk of financial distress and insolvencies, particularly in the context of the much higher level of debt stock in the region. Furthermore, the resilience of some banks and nonbank financial intermediaries (NBFIs) may be tested and could potentially exacerbate vulnerabilities in the financial market.

The higher debt levels amid tighter monetary conditions have created the potential for financial stability risks to emerge. Addressing these challenges effectively necessitates a well-balanced policy mix across monetary, fiscal, and prudential policy frameworks, with concerted efforts among authorities. Central banks should prioritize price stability while striving to maintain financial stability and support growth. Monetary authorities should stand ready to provide targeted liquidity support to financial institutions with clear communication during times of stress. The soundness of financial intermediaries, including NBFIs, must be ensured through strengthening regulatory, supervisory, and risk management. Furthermore, regional cooperation and external buffers are essential to ensure access to US dollar liquidity in times of crisis and reduce dependence on the US dollar in the long term.

In response to rising nonfinancial private debt and potential systemic financial risks, policymakers can employ macroprudential tools to manage household debt and curb excessive property developer leverage. For corporate debt, it is necessary to promote responsible corporate lending, foster independent ownership, and mitigate credit risks of small and medium enterprises with credit guarantee schemes. To mitigate financial stability risks stemming from high public debt, strategies should include medium-term fiscal consolidation, maintaining a robust debt structure, and diversifying the investor base.

Amid these turbulent times, the internal and external macrofinancial conditions surrounding the ASEAN+3 region are still subject to high uncertainty and volatility. The financial landscape is swiftly changing into a new normal with potentially higher inflation and higher interest rates. In this situation, the region must come together as one and strive for macroeconomic and financial resilience and stability. AMRO holds high hopes that our *ASEAN+3 Financial Stability Report* will play a pivotal role in our collective efforts, making a substantial contribution toward achieving this objective.

Hoe Ee Khor
Chief Economist

Acknowledgments

This report provides AMRO staff's assessment of both the conjunctural and structural financial stability issues facing the ASEAN+3 region. It covers the short-term developments, risks, vulnerabilities, and challenges facing member economies, as well as the policy options taken by or that are available to their authorities. It also presents staff's studies on longer-term issues that are pertinent to sustained financial stability in the region.

The analysis in this report was prepared by the Financial Surveillance team led by Kevin C. Cheng. The report was peer-commented by economists from AMRO's Country Surveillance, Fiscal Surveillance, Regional Surveillance, Macro-Financial Research, and Policy Review Group. The report was reviewed and cleared by Chief Economist, Hoe Ee Khor. It has also benefited from the guidance of AMRO Director Kouqing Li and other members of the Senior Management team.

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Finally, the views expressed in this report are those of AMRO staff and do not necessarily represent those of AMRO member authorities.

Abbreviations

A+3, ASEAN+3	ASEAN plus China (including Hong Kong), Japan, and Korea	CAR	Capital adequacy ratio
ADB	Asian Development Bank	CDB	China Development Bank
ADBC	Agricultural Development Bank of China	CDS	Credit default swap
AE	Advanced Economy	CCB	Countercyclical capital buffer
AFSR	ASEAN+3 Financial Stability Report	CCPT	Climate Change and Principle-Based Taxonomy
Agrobank	Bank Pertanian Malaysia Berhad	CEXIM	Export-import Bank of China
AMC	American Multi-Cinema	CGB	China government bond
AREO	ASEAN+3 Regional Economic Outlook	CGS	Credit guarantee scheme
ASEAN	Association of Southeast Asian Nations	CHF	Swiss franc
ASEAN-4	Indonesia, Malaysia, the Philippines, and Thailand	CIV	Collective Investment Vehicles
ASEAN-5	Indonesia, Malaysia, the Philippines, Thailand, and Singapore	CLMV	Cambodia, Lao PDR, Myanmar, and Vietnam
ASEAN-6	ASEAN-5 plus Vietnam	CMIM	Chiang Mai Initiative Multilateralisation
AT1	Additional Tier 1	CN	China
BAAC	Bank for Agriculture and Agricultural Cooperatives	CNY	Chinese renminbi
BCLMV	Brunei Darussalam, Cambodia, Lao PDR, Myanmar, and Vietnam	COVID-19	2019 coronavirus disease
BDPC	Brunei Darussalam Deposit Protection	CP	Commercial paper
BICS	Bloomberg Industry Classification Standard	CPI	Consumer price index
BIS	Bank for International Settlements	DBJ	Development Bank of Japan Inc.
BN	Brunei Darussalam*	DE	Germany
BNM	Bank Negara Malaysia	DICJ	Deposit Insurance Corporation of Japan
bps	Basis points	DIV	Deposit Insurance of Vietnam
BOE	Bank of England	DLP	Digital Leaders Programme
BOJ	Bank of Japan	DPA	Deposit Protection Agency
BOK	Bank of Korea	DPO	Deposit Protection Office
BOP	Balance of Payments	D-SIB	Domestic Systemically Important Banks
BSA	Bilateral Swap Agreement	DSR	Debt service ratio
BSN	Bank Simpanan Nasional	DSTI	Debt-Service-to-Income Ratio
BTFP	Bank Term Funding Program	DXY	US dollar index
BPMB	Bank Pembangunan Malaysia Berhad	EA	Euro area
BVI	Bank Vulnerability Index	EBIT	Earnings before interest and taxes
		ECB	European Central Bank
		EEU	Eastern Europe

* For brevity, "Brunei Darussalam" is referred to as "Brunei" in the text.

EM	Emerging Market
ESG	Environmental, social, and governance
EU	European Union
EUR	Euro
EXIM	Export-Import Bank of Thailand
FCI	Financial Conditions Index
FCY	Foreign currencies
FDI	Foreign direct investment
Fed	US Federal Reserve
FI	Financial Institution
FIMA	Foreign and International Monetary Authority
FMI	Financial Market Intermediary
FOMC	Federal Open Market Committee
FR	France
FSB	Financial Stability Board
FX	Foreign exchange
GBP	Pound sterling
GDP	Gross domestic product
GFC	Global Financial Crisis
GHB	Government Housing Bank
Govt.	Government
GSB	Government Savings Bank
G-SIB	Global Systematically Important Bank
HAI	Housing affordability index
HK	Hong Kong, China*
iBank	Islamic Bank of Thailand
IBK	Industrial Bank of Korea
IC	Investment company
ICR	Interest coverage ratio
ICT	Information and communications technology
ID	Indonesia
IDIC	Indonesia Deposit Insurance Corporation

IFC	International Finance Corporation/ international financial center
IFI	Independent fiscal institution
IFS	IMF International Financial Statistics
iMaPP	IMF Integrated Macprudential Policy database
IMF	International Monetary Fund
IMF WEO	IMF World Economic Outlook database
IMF COFER	IMF Official Foreign Exchange Reserves database
IO	International organization
JGB	Japanese government bonds
JBIC	Japan Bank for International Cooperation
JP	Japan
JPY	Japanese yen
KBW	Keefe, Bruyette, and Woods
KDB	Korea Development Bank
KDIC	Korea Deposit Insurance Corporation
KEXIM	Export-Import Bank of Korea
KH	Cambodia
KLIBOR	Kuala Lumpur interbank offered rate
KR	Korea
LAT	Latin America
LA, Lao PDR	Lao People's Democratic Republic
LIBOR	London interbank offer rate
LCR	Liquidity coverage ratio
LGfV	Local government financing vehicles
LLP	Loan loss provision
LTV	Loan-to-value ratio
MGS	Mutual guarantee scheme
MM	Myanmar
MMF	Money market funds
MSME	Micro, small and medium sized enterprise
MY	Malaysia

* For brevity, "Hong Kong, China" is referred to as "Hong Kong" in the text.

MYR	Malaysian ringgit
MYOR	Malaysia overnight rate
NACF	National Agricultural Cooperative Federation
NAR	North America
NBB	Nayoby Bank
NBFI	Nonbank financial institution/ intermediary
NDRC	National Development and Reform Commission
NEER	Nominal effective exchange rate
NFC	Nonfinancial corporate
NFFC	National Federation of Fisheries Cooperatives
NIM	Net interest margin
NPL	Nonperforming loan
OLS	Ordinary least squares regression
OPR	Overnight policy rate
OTH	Others
PBC	People's Bank of China
PDIC	Philippine Deposit Insurance Corporation
P/E	Price-to-earning ratio
PH	The Philippines
PIDM	Perbadanan Insurans Deposit Malaysia
Plus-3	China (including Hong Kong), Japan, Korea
PPP	Public-private partnership
REER	Real effective exchange rate
ROA	Return on assets
ROW	Rest of the world
RRP	Reverse repo program
S&P	Standard and Poor's
SBGFC/SBC	Small Business Guarantee and Finance Corporation
SD	Standard deviation

SDIC	Singapore Deposit Insurance Corporation
SFI	Specialized financial institution
SFV	Structured finance vehicle
SG	Singapore
SGD	Singapore dollar
SGS	Singapore Government Securities
SGSS	Special Singapore Government Securities
SIFI	Systemically important financial institutions
SIFMA	The Securities Industry and Financial Markets Association
SME	Small and medium sized enterprise
SOE	State-owned enterprise
SOFR	Secured overnight financing rate
SSGS	Special Singapore Government Securities
SSO	Social Security Office
SuNWEI	Systemic Network of World Expected-Losses of Institutions
SVB	Silicon Valley Bank
TCG	Thai Credit Guarantee Corporation
TH	Thailand
T-bill	Treasury bill
UK	United Kingdom
US	United States
USD	US dollar
VBSP	Vietnam Bank for Social Policies
VDB	Vietnam Development Bank
VIX	Volatility Index
VN	Vietnam
WB	World Bank
WEU	Western Europe
YTD	Year-to-date
Δ	Change in