

ASEAN+3 FINANCIAL STABILITY REPORT 2023



**Navigating High Debt in
Low Visibility**



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The factual information covers data for the period up to 31 October 2023, except when stated otherwise.

© 2023 ASEAN+3 Macroeconomic Research Office
ISSN: XXXX-XXXX

Printed in Singapore

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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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Chiang Yong (Edmond) Choo and Leilei Lu coordinated the production of the publication, with editorial assistance from James Unwin; Qin Jie, Andrea Abellon, Hui Shan Seah, Lynn Tan and Karen Wilkinson coordinated communications and outreach.

The authors would like to thank members of AMRO's Advisory Panel, chaired by Diwa C. Guinigundo, for their useful input; private sector and official counterparts during the financial surveillance missions for their insightful observations on country and regional developments; and member authorities for their factual corrections and comments.

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
ADB	Asian Development Bank
ADBC	Agricultural Development Bank of China
AE	Advanced Economy
AFSR	ASEAN+3 Financial Stability Report
Agrobank	Bank Pertanian Malaysia Berhad
AMC	American Multi-Cinema
AREO	ASEAN+3 Regional Economic Outlook
ASEAN	Association of Southeast Asian Nations
ASEAN-4	Indonesia, Malaysia, the Philippines, and Thailand
ASEAN-5	Indonesia, Malaysia, the Philippines, Thailand, and Singapore
ASEAN-6	ASEAN-5 plus Vietnam
AT1	Additional Tier 1
BAAC	Bank for Agriculture and Agricultural Cooperatives
BCLMV	Brunei Darussalam, Cambodia, Lao PDR, Myanmar, and Vietnam
BDPC	Brunei Darussalam Deposit Protection
BICS	Bloomberg Industry Classification Standard
BIS	Bank for International Settlements
BN	Brunei Darussalam*
BNM	Bank Negara Malaysia
bps	Basis points
BOE	Bank of England
BOJ	Bank of Japan
BOK	Bank of Korea
BOP	Balance of Payments
BSA	Bilateral Swap Agreement
BSN	Bank Simpanan Nasional
BTFP	Bank Term Funding Program
BPMB	Bank Pembangunan Malaysia Berhad
BVI	Bank Vulnerability Index

CAR	Capital adequacy ratio
CDB	China Development Bank
CDS	Credit default swap
CCB	Countercyclical capital buffer
CCPT	Climate Change and Principle-Based Taxonomy
CEXIM	Export-import Bank of China
CGB	China government bond
CGS	Credit guarantee scheme
CHF	Swiss franc
CIV	Collective Investment Vehicles
CLMV	Cambodia, Lao PDR, Myanmar, and Vietnam
CMIM	Chiang Mai Initiative Multilateralisation
CN	China
CNY	Chinese renminbi
COVID-19	2019 coronavirus disease
CP	Commercial paper
CPI	Consumer price index
DBJ	Development Bank of Japan Inc.
DE	Germany
DICJ	Deposit Insurance Corporation of Japan
DIV	Deposit Insurance of Vietnam
DLP	Digital Leaders Programme
DPA	Deposit Protection Agency
DPO	Deposit Protection Office
D-SIB	Domestic Systemically Important Banks
DSR	Debt service ratio
DSTI	Debt-Service-to-Income Ratio
DXY	US dollar index
EA	Euro area
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