

CONTENTS

Preface	ix
Executive Summary	xi
Chapter 1. Stabilizing the Global Financial System and Mitigating Spillover Risks	1
A. Global Financial Stability Map	1
B. Global Deleveraging and its Consequences	4
C. The Crisis has Engulfed Emerging Markets	8
D. The Deteriorating Outlook for Household and Corporate Defaults in Mature Markets and Implications for the Financial System	23
E. Stability Risks and the Effectiveness of the Policy Response	32
F. Costs of Official Support, Potential Spillovers, and Policy Risks	44
Annex 1.1. Global Financial Stability Map: Construction and Methodology	49
Annex 1.2. Predicting Private “Other Investment” Flows and Credit Growth in Emerging Markets	58
Annex 1.3. Spillovers Between Foreign Banks and Emerging Market Sovereigns	60
Annex 1.4. Debt Restructuring in Systemic Crises	64
Annex 1.5. Methodology for Estimating Financial Writedowns	67
References	72
Chapter 2. Assessing the Systemic Implications of Financial Linkages	
[Available online at http://www.imf.org/external/pubs/ft/gfsr/2009/01/pdf/chap2.pdf]	
Summary	
Four Methods of Assessing Systemic Linkages	
How Regulators Assess Systemic Linkages	
Policy Reflections	
Annex 2.1. Default Intensity Model Estimation	
References	
Chapter 3. Detecting Systemic Risk	
[Available online at http://www.imf.org/external/pubs/ft/gfsr/2008/02/pdf/chap3.pdf]	
Summary	
What Constitutes “Systemic” Risk?	
“Fundamental” Characteristics of Intervened and Nonintervened Financial Institutions	
Market Perceptions of Risk of Financial Institutions	
Identifying Systemic Risks Through Regime Shifts	

CONTENTS

Role of Global Market Conditions During Episodes of Stress	
Policy Implications	
Conclusions	
Annex 3.1. Financial Soundness Indicators	
Annex 3.2. Groups of Selected Financial Institutions	
Annex 3.3. List of Intervened Financial Institutions	
References	

Glossary

Annex: Summing Up by the Acting Chair

Statistical Appendix

[Available online at <http://www.imf.org/external/pubs/ft/gfsr/2009/01/pdf/statappx.pdf>]

Boxes

1.1. Near-Term Financial Stability Challenges and Policy Priorities	2
1.2. Cross-Border Exposures and Financial Interlinkages within Europe	12
1.3. Effects of the Global Financial Crisis on Trade Finance: The Case of Sub-Saharan Africa	15
1.4. Enhanced IMF Lending Capabilities and Implications for Emerging Markets	20
1.5. Modeling Corporate Bond Spreads: A Capital Flows Framework	29
1.6. Recent Unconventional Measures of Selected Major Central Banks	41
1.7. Forecasts for Charge-Offs on U.S. Bank Loans	71
2.1. Network Simulations of Credit and Liquidity Shocks	
2.2. Quantile Analysis	
2.3. Default Intensity Model Specification	
2.4. Basics of Over-the-Counter Counterparty Credit Risk Mitigation	
2.5. A Central Counterparty as a Mitigant to Counterparty Risk in the Credit Default Swap Markets	
3.1. Modeling Risk-Adjusted Balance Sheets: The Contingent Claims Approach	
3.2. <i>Option</i> -iPoD Measures of Risk Across Financial Institutions	
3.3. Higher Moments and Multivariate Dependence of Implied Volatilities from Equity Options as Measures of Systemic Risk	
3.4. The Consistent Information Multivariate Density Optimizing Approach	
3.5. Spillovers to Emerging Markets: A Multivariate GARCH Analysis	
3.6. The Transformation of Bank Risk into Sovereign Risk—The Tale of Credit Default Swaps	

Tables

1.1. Macro and Financial Indicators in Selected Emerging Market Countries	10
1.2. Potential Writedowns and Capital Needs for Emerging Market Banks by Region	17
1.3. Estimates of Financial Sector Potential Writedowns (2007–10) as of April 2009	28
1.4. Bank Equity Requirement Analysis	34
1.5. Policy Measures to Address Troubled Assets	37
1.6. Tentative Easing in Credit Conditions	38
1.7. Bank Wholesale Financing and Public Funding Support	39

1.8. Public Debt and Stabilization Costs, end-2009	44
1.9. Mature Market Sovereign Credit Default Swap Spreads and Debt Outstanding	45
1.10. Expected Guaranteed Debt Issuance	46
1.11. Changes in Risks and Conditions Since the October 2008 <i>Global Financial Stability Report</i>	49
1.12. Distress Dependence Matrices: Sovereigns and Banks	62
1.13. Estimated Bank Portfolio Composition by Type of Asset	68
1.14. Estimated Bank Portfolio Composition by Origin of Assets	69
1.15. Estimated Regional Distribution of Bank Writedowns and Cumulative Loss Rates	70
2.1. Taxonomy of Financial Linkages Models	
2.2. Simulation 1 Results (Credit Channel)	
2.3. Post-Simulation 1 Capital Losses	
2.4. Simulation 2 Results (Credit and Funding Channel)	
2.5. Post-Simulation 2 Capital Losses	
2.6. Conditional Co-Risk Estimates, March 2008	
2.7. Conditional Co-Risk Estimates, September 2008	
2.8. Distress Dependence Matrix	
2.9. Summary of Various Methodologies: Limitations and Policy Implications	
3.1. Selected Indicators on Fundamental Characteristics in Financial Institutions	
3.2. Taxonomy of Credit Risk Models	
3.3. Correlations Among 45 Financial Institutions During Different Stress Periods	
3.4. Cluster Analysis	
3.5. Summary of Various Methodologies: Limitations and Policy Implications	

Figures

1.1. Global Financial Stability Map	3
1.2. Heat Map: Developments in Systemic Asset Classes	4
1.3. Ratio of Debt to GDP Among Select Advanced Economies	4
1.4. Bank Credit to the Private Sector	5
1.5. Private Sector Credit Growth	5
1.6. Bank for International Settlements Reporting Banks: Cross-Border Liabilities and Exchange-Rate-Adjusted Changes	6
1.7. Bank for International Settlements Reporting Countries: Cross-Border Assets as a Proportion of Total Assets	6
1.8. Emerging Market Net Private Capital Flows	7
1.9. Net Foreign Equity Investment in Emerging Economies	7
1.10. Emerging Market Hedge Funds: Estimated Assets and Net Asset Flows	8
1.11. Heat Map: Developments in Emerging Market Systemic Asset Classes	8
1.12. Emerging Europe: Real Credit Growth to the Private Sector and Output	9
1.13. Emerging Market Performance of Credit Default Swap Spreads and Equity Prices	9
1.14. Cross-Currency Basis Swap Spreads	11
1.15. Emerging Market Real Credit Growth	16
1.16. External Debt Refinancing Needs	16
1.17. Emerging Market Corporate Bond Spreads	17
1.18. Aggregate Emerging Markets Bond Index Global Spread	18
1.19. Distress Dependence Between Emerging Market Sovereigns and Advanced Country Banks	18

CONTENTS

1.20. U.S. Loan Charge-Off Rates: Baseline	23
1.21. Delinquency Rates on U.S. Residential Mortgage Loans	23
1.22. Spreads on Commercial Mortgage-Backed Securities	24
1.23. Spreads on Consumer Credit Asset-Backed Securities	25
1.24. Global Corporate Default Rates	25
1.25. Average Recovery Rates on Defaulted U.S. Bonds	26
1.26. Corporate Credit Default Swap Spreads	26
1.27. Estimates of Economic Growth and Financial Sector Writedowns	27
1.28. U.S. and European Bank and Insurance Company Market Capitalization, Writedowns, and Capital Infusions	32
1.29. U.S. and European (including U.K.) Bank Earnings and Writedowns	35
1.30. Commercial Bank Loan Charge-Offs	35
1.31. European Securitization Gross Issuance	38
1.32. Refinancing Gap of Global Banks	39
1.33. Pension Funds of Large U.S. and European Companies: Estimated Funding Levels	40
1.34. Insurance Sector Credit Default Swaps Spreads	40
1.35. Large Economy Credit Default Swap Spreads	46
1.36. Benchmark Five-Year Government Bonds	46
1.37. Swap Spreads of Government-Guaranteed Bonds	47
1.38. Global Financial Stability Map: Monetary and Financial Conditions	50
1.39. Global Financial Stability Map: Risk Appetite	52
1.40. Global Financial Stability Map: Macroeconomic Risks	53
1.41. Global Financial Stability Map: Emerging Market Risks	54
1.42. Global Financial Stability Map: Credit Risks	56
1.43. Global Financial Stability Map: Market and Liquidity Risks	57
1.44. Impulse Responses	59
1.45. Net Private Other Investment Flows to Emerging Markets	59
1.46. Emerging Market Real Credit Growth	60
1.47. Emerging Market GDP Growth	60
1.48. Default Probabilities Implied by Credit Default Swap Pricing	63
1.49. Distress Dependence	63
2.1. Network Analysis: A Diagrammatic Representation of Systemic Interbank Exposures	
2.2. Network Analysis: Number of Induced Failures	
2.3. Network Analysis: Country-by-Country Vulnerability Level	
2.4. Network Analysis: Contagion Path Triggered by the U.K. Failure	
2.5. AIG and Lehman Brothers Default Risk Codependence	
2.6. A Diagrammatic Depiction of Co-Risk Feedbacks	
2.7. U.S. and European Banks: Tail-Risk Dependence Devised from Equity Option Implied Volatility, 2006–08	
2.8. Legend of Trivariate Dependence Simplex	
2.9. Annual Number of Corporate and Banking Defaults	
2.10. Actual and Fitted Economy Default Rates	
2.11. Default Rate Probability and Number of Defaults	
2.12. Quarterly One-Year-Ahead Forecast Value-at-Risk at 95 Percent Level	
2.13. Capital Adequacy Ratios (CAR) After Hypothetical Credit Shocks	
2.14. Basic Structure of the Systemic Risk Monitor Model	

- 2.15. RAMSI Framework
- 3.1. Capital-to-Assets Ratio
- 3.2. Ratio of Short-Term Debt to Total Debt
- 3.3. Return on Assets
- 3.4. Dendrogram
- 3.5. U.S. and European Banks: Joint Tail Risk of Implied Volatilities
- 3.6. Higher Moments and Multivariate Dependence of Implied Equity Volatility
- 3.7. Joint Probability of Distress (JPoD) and Banking Stability Index (BSI):
Core 2 Group
- 3.8. Joint Probability of Distress (JPoD) and Banking Stability Index (BSI): By
Geographic Region
- 3.9. Daily Percentage Change: Joint and Average Probability of Distress, Core 2 Group
- 3.10. Probability of Cascade Effects
- 3.11. Markov-Regime Switching ARCH Model: Joint Probability of Distress and
Banking Stability Index
- 3.12. Euro-Dollar Forex Swap
- 3.13. Markov-Switching ARCH Model of VIX
- 3.14. Markov-Switching ARCH Model of TED Spread
- 3.15. Markov-Switching ARCH Model of VIX, TED Spread, and Core 2 Banking
Stability Index

The following symbols have been used throughout this volume:

- . . . to indicate that data are not available;
- to indicate that the figure is zero or less than half the final digit shown, or that the item does not exist;
- between years or months (for example, 1997–99 or January–June) to indicate the years or months covered, including the beginning and ending years or months;
- / between years (for example, 1998/99) to indicate a fiscal or financial year.

“Billion” means a thousand million; “trillion” means a thousand billion.

“Basis points” refer to hundredths of 1 percentage point (for example, 25 basis points are equivalent to 1/4 of 1 percentage point).

“n.a.” means not applicable.

Minor discrepancies between constituent figures and totals are due to rounding.

As used in this volume the term “country” does not in all cases refer to a territorial entity that is a state as understood by international law and practice. As used here, the term also covers some territorial entities that are not states but for which statistical data are maintained on a separate and independent basis.

