FOREWORD

Since we last published the *Global Financial Stability Report* (GFSR) in October 2024, financial stability risks have increased. With elevated economic policy uncertainty, financial market volatility has risen and investor confidence has turned to concern. Substantially elevated equity and bond market has tightened global financial conditions, indicating global financial markets may be at a turning point. While the role of the GFSR is not to predict future shocks, it does identify vulnerabilities that can propagate and amplify when downside risk realizes. Financial stability assessments are squarely focused on downside risks, akin to the perspectives of risk managers for the global financial system.

In recent years, the global financial system has been able to absorb a protracted series of shocks. These include the COVID-19 pandemic in 2020, the global surge of inflation beginning in 2021, and Russia's war in Ukraine starting in 2022. More recently, uncertainty about economic policies, notably tariffs, is again testing the resilience of the global financial system. In addition, elevated levels of sovereign debt are a worry, given the interaction of financial sector imbalances and government debt. Financial imbalances can amplify adverse shocks.

The financial system's ability to weather shocks has been bolstered in recent years by the prudent management of the financial sector. Banks around the world remain at the core of the financial system and have seen substantially increased levels of capital and liquidity, enhancing their capacity to absorb losses during difficult periods. Going forward, the continued, timely, and consistent implementation of Basel III and other internationally-agreed-upon bank regulatory standards will help ensure a level playing field across jurisdictions and guarantee continued ample capital and liquidity to withstand future shocks. We view the increased focus on the proactive supervision of the largest institutions globally as a key contributor to stability. To increase efficiencies in credit provision, a proportionate approach consistent with the Basel Core Principles for Effective Banking Supervision should be considered. That means hat smaller banking institutions should be supervised and regulated in a proportionate manner, simplifying requirements while strengthening resilience to shocks.

As we move into new analysis in this April 2025 GFSR, we highlight the growing role of nonbank financial intermediation (NBFI) and the increased exposure of banks to NBFIs. Nonbank financial institutions cover a broad array of intermediation activity, including insurance companies, pension funds, investment funds (mutual funds, exchange-traded funds, hedge funds, private equity, and private credit), and finance companies. The linkages between banks and nonbanks have been growing, increasing the NBFI's influence on systemwide financial stability.

In light of these considerations, improving the regulation of NBFIs should remain a priority. Important advances have been made to reinforce their soundness, including reforms to money market funds, limits to liquidity risks in mutual funds, margin-setting in central counterparties, counterparty risk management practices for broker-dealers, and trading rules in exchanges and electronic trading platforms. However, data gaps preclude a complete and timely assessment of vulnerabilities. The data gaps are challenging sound decision making for private sector participants and for policy makers. To harness the benefits from the growth of NBFIs, it is paramount to strengthen data availability for risk monitoring and assessment. This will enable the private sector and supervisors to have a systemwide view of risks and single out poorly governed institutions that take excessive risks. Better data will also ensure that national authorities have the appropriate tools to manage these risks effectively. International standard setters are planning further work in this regard, including examining cross-border and cross-sector interconnectedness and enhancing international coordination.

In financial markets, sound trading arrangements and infrastructures are essential for maintaining macrofinancial stability. A resilient global financial system requires financial "plumbing" to operate smoothly so that the movements of securities, derivatives, and payments can continue during periods of market volatility. To ensure the efficient and reliable operation of payment and settlement systems, it is necessary to prioritize the interoperability of various platforms, particularly across borders. Embracing innovative technologies—such as blockchain and artificial intelligence—can significantly enhance the efficiency and security of these systems, ultimately contributing to a more stable financial environment.

Even well-regulated financial systems may face shocks so severe that they lead to systemic crises. Crisis preparedness, alongside proactive regulatory policies, remains foundational for financial stability. Drawing on insights from the March 2023 banking turmoil, we can make some clear assessments. First, it is crucial for supervisors with the willingness, legal authority, and ability to act to intervene early in weak institutions. Second, stabilizing the financial system may require a large and rapid provision of liquidity to financial institutions. Central banks should further develop their frameworks for emergency liquidity assistance during regular periods so that they are well prepared for potential intervention in a crisis. Third, even small banks can pose risks to financial stability. It is essential to make further progress in implementing recovery and resolution frameworks to effectively address the challenges posed by weak or failing financial institutions, with the goal of minimizing the need for public funding.

Drawing lessons from the past will continue to guide our efforts in strengthening future preparedness. It is key that we closely monitor evolving financial vulnerabilities for banks and nonbanks alike. The interactions of capital markets and the banking system could be tested if financial conditions were to tighten further. To keep a watchful eye on these risks to global financial stability is the purpose of this report.

Tobias Adrian
Financial Counsellor