

IMF warns AI in capital markets could raise speed and volatility under stress

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Global Financial Stability Report, October 2024 - Steadying the Course: Uncertainty, Artificial Intelligence, and Financial Stability

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Source details Canonical URL Global Financial Stability Report, October 2024 - Steadying the Course: Uncertainty, Artificial Intelligence, and Financial Stability Other formats Markdown version Structured JSON version Bundle manifest Bibliographic details Published: October 22, 2024 Overall assessment and key highlight Financial stability risks remain contained in the near term, although rising economic and geopolitical uncertainty increases the likelihood of adverse shocks, exposing fragilities. Accommodative financial conditions have remained in place with an expectation that monetary policy will continue to ease globally; on net, emerging markets have remained resilient and asset price volatility has stayed low. Accommodative conditions that keep near-term risks contained also facilitate the buildup of vulnerabilities, including: lofty asset valuations, the global rise in private and government debt, increased use of leverage by nonbank financial institutions. The widening disconnect between elevated economic uncertainty and low financial volatility increases the probability that adverse shocks will be amplified by these mounting vulnerabilities. Pressures on the commercial real estate sector remain acute, and some midsize companies' borrowings are becoming increasingly strained. The slowing growth outlook in China, together with fragilities in its financial system, is identified as a key downside risk to the global economy. Policymakers face urgency to address these vulnerabilities. Chapter 1 — Steadying the Course: Financial Markets Navigate Uncertainty Near-term financial stability risks have remained contained, but mounting vulnerabilities could worsen future downside risks by amplifying shocks. Financial conditions: accommodative, with expectations of continued monetary policy easing globally. Observed resilience: emerging markets have remained resilient; asset price volatility has stayed low, on net. Key vulnerabilities highlighted: lofty asset valuations, global rise in private and government debt, increased use of leverage by nonbank financial institutions, strained borrowings of some midsize companies, acute pressures in the commercial real estate sector. Amplification mechanism: the widening disconnect between elevated economic uncertainty and low financial volatility increases the probability that shocks will be amplified. Downside external risk: slowing growth outlook in China and fragilities in its financial system may constrain access to funding for economies with weaker fiscal buffers. Chapter 2 — Macroeconomic Stability Amid High Global Economic Uncertainty Context: uncertainty regarding global economic outcomes and policies has been higher since the COVID-19 pandemic amid inflation shocks, rising geopolitical tensions, emerging technologies, and climate-related disasters. Main finding: high macroeconomic uncertainty can significantly raise downside tail risks to future output growth, asset prices, and bank lending growth. Conditional strengths of the relationships: The relationship between macroeconomic uncertainty and downside tail risks is stronger when debt vulnerabilities are elevated. The relationship is stronger when financial market volatility is low (during episodes of a macro-market disconnect). Cross-border effects: macroeconomic uncertainty can trigger cross-border spillover effects through trade and financial linkages. Policy responses and resilience measures recommended: more credible policy frameworks, building resilience through adequate macroprudential policies and reserve buffers, reducing fiscal vulnerabilities. Chapter 3 — Advances in Artificial Intelligence: Implications for Capital Market Activities Scope: assesses recent developments in AI and Generative AI and their implications for capital markets using new analytical work and results from a global outreach to market participants and regulators. Adoption signals: evidence from labor markets and patent filings suggests that adoption of AI in capital markets is likely to increase significantly in the near future. Potential market-structure effects: AI could cause large changes in market structure through the greater and more powerful use of algorithmic trading and novel trading and investment strategies. Potential benefits: enabling superior risk management, deepening market liquidity, improving market monitoring by both participants and regulators. Potential new risks: increased market speed and volatility under stress, more opacity and monitoring challenges of

non-bank financial institutions, increased operational risks due to reliance on a few key third-party AI-service providers, increased cyber and market manipulation risks. Regulatory stance: Many of these risks are addressed by existing regulatory frameworks, Important new and unforeseen developments may still arise. Suggested stance for authorities: consider additional policy responses to ensure preparedness for potentially transformative changes.

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