Macro Dev

Macroeconomics and development

JANUARY 2026 | N° 72

SEMESTRIAL PANORAMA 2026 #1

International economy: Groundswells in relatively calm waters

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ÉDITIONS AFD
AGENCE FRANÇAISE DE DÉVELOPPEMENT

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Editorial

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"Gold is everything, and the rest, without gold, is nothing"
Diderot, Rameau's Nephew

Amidst a geopolitical environment undergoing reconfiguration, many economic paradigms once thought to be immutable are now shifting before our eyes. This paper aims to provide a brief overview of them, or at least some of them.

The relative resilience of global growth in 2025, seen across both advanced and emerging and developing economies, could well continue into 2026 within a landscape of apparent continuity. But in reality, the ingredients of this growth are changing. And while growth has been on a downward trend since the 2008 financial crisis, it is far from certain that the new recipe will be enough to reverse this trend.

The first ingredient is that real interest rates have (almost) turned positive again everywhere (normalization is underway in Japan, although it will take time). However, the fact remains that this return to a form of monetary orthodoxy is holding back growth. In addition, after starting to cut its rates, the Fed is already considering using its balance sheet again as a driver to support financial liquidity, which is being tested by the growing financing needs of the U.S. Treasury.

But the other ingredients are far less tried-and-tested, pointing instead to a new recipe, which will take some time to cook before yielding a finished product.

In October 2025, the bankruptcy of the auto parts company First Brands, with over $11 billion in outstanding liabilities, entirely held through non-bank financing and likely partly due to fraudulent transactions, offered a glimpse into how non-bank finance was beginning to affect major players. It also suggested that the lower level of supervision compared to the traditional banking sector could generate risks whose systemic impact remains difficult to gauge.

Following the passage of the GENIUS Act in July 2025, which established a legal framework for stablecoins, the profound shift this could bring to global money markets has begun to emerge. Collateralized by T-bills, stablecoins are proving to be both a windfall for financing the U.S. public deficit and a tool to re-dollarize a portion of global transactions and reserves. However, they could potentially destabilize portfolio investment flows to emerging economies.

Beyond the financial sphere, artificial intelligence is providing a powerful catalyst for these radical changes. The accelerating technological race, between major tech players in the U.S. and within a less transparent context in China, is striking for the scale of the investments. It also raises questions about the time required to convert them into productivity gains and return on investment. Meanwhile, at the end of 2025, OpenAI's valuation stood at around $500 billion, with revenue estimated at $13 billion, representing a multiple of 38, despite the company not yet reaching break-even. In December 1999, Amazon, which was also not profitable, was valued at approximately 22 times its sales.[1]

[1] Market capitalization as at 10 December 1999 of USD36 billion (source: StatMuse – 1999 high) compared to a revenue of USD1.64 billion (source: Amazon Annual Report 1999).

By further broadening the scope of analysis, the transformation from a globalized to a multipolar world undergoing regionalization is a parameter shift unseen since the establishment of the WTO in 1995. Bilateral and regional trade agreements are now expected to take precedence over WTO rules, at least in the medium term. Geopolitical confrontations and the calling into question of multilateralism further reinforce this logic of blocs and transactions.

Finally, the very reality of planetary boundaries is being called into question, in the wake of the White House's climate-skeptic stance, with massive consequences (which we can only hope can still be reversed) for international cooperation, transition trajectories, and investment in adaptation.

Is the fabric of the global economy thus changing in nature at very different levels, from corporate finance to international cooperation for climate and biodiversity? The inertia inherent to economic activity is limiting the effects for the time being, but there is no doubt that they could be significant in the long term.

Is it for this reason that gold, a safe haven investment when benchmarks disappear, was the most profitable asset class in 2025, appreciating by 67%? This represents a level almost twice as high as that of the second asset class – European equities – that still holds some promise for the real economy?[2]

[2] MSCI Europe index performance in 2025: + 36% ; source Macrobond.

International economy

In the eye of the storm?

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Is the global economy in the eye of the storm (the calm before the storm), or could a gradual easing of trade tensions trigger a new, more peaceful (geo)economic cycle? At the same time, should we fear a new global financial shock, and what would be the consequences for emerging and developing countries (EDCs), given the overt exuberance in the U.S. over tech (AI) and crypto-asset valuations, and the potential systemic risks associated with non-bank financial institutions (NBFIs)?

Political, economic and financial developments in the U.S. are, more than ever, at the heart of the concerns of the rest of the world. Ten months after "Liberation Day" on 2 April 2025, which saw the U.S. launch a "universal trade war", the negative impact on the global economy is materializing only gradually. The reorganization of supply chains to redirect trade flows, the negotiation of trade agreements between various countries (including China) and the U.S., and the overall moderation of retaliatory measures against the U.S. preserved world trade in the first half of 2025.

Despite signs of an economic and trade slowdown in the second half of the year, global economic growth proved more resilient than expected over the year as a whole, though it remained below the outlook projected at the end of 2024. Indeed, the relative weakness of the dollar, the easing of international financial conditions (monetary easing and narrowing of sovereign risk premiums), and the generally strong performance of commodity prices have supported economic activity and macro-financial stability in emerging and developing countries (EDCs). However, this relative lull is set against a backdrop of extreme uncertainty, driven by the ongoing series of erratic measures and U-turns of the Trump administration, which is expected to continue into 2026.

Ultimately, the destabilizing factors facing the global economy and macro-financial risk factors will continue to persist in the short and medium term, given the global imbalances and strong interdependencies:

- Potential escalation of the trade war, notably between China and the U.S., turning into a currency war, implementation of non-tariff trade barriers (control of export licenses) and mechanisms such as the European Union's Carbon Border Adjustment Mechanism (CBAM) and the deforestation regulation, triggering retaliatory measures;
- Heightened geopolitical conflict, imperialist drift, notably from the U.S., with the risk of open confrontations (U.S.-China in the South China Sea, Russia-European Union, Middle East, Latin America, and other regional and cross-border conflicts);
- Undermining of the independence, credibility, or even the monetary sovereignty of central banks, starting with the Fed, faced with a monetary policy dilemma in a context of fiscal dominance, given the scale of public deficits and debt (in both developed countries and EDCs) and the boom in crypto-assets;
- Bursting of the tech financial bubble surrounding AI and/or a bond market crash in the U.S., which could be triggered by a crisis among non-bank financial institutions (NBFIs), which are less regulated than the banking system, or by stablecoins backed by U.S. T-bills;
- A marked slowdown of the Chinese economy, a key player in manufacturing value chains in Asia (and beyond) and in the global commodity market, whose downturn would have major implications for EDCs, especially the most fragile African and Latin American countries in terms of public finances and external positions;
- Consequences of the "drill, baby, drill" policy in the U.S. on oil supply and prices (driven downward), especially for certain EDCs that are highly dependent on hydrocarbons for their economic development;
- Adverse socio-economic or even socio-political consequences for the same EDCs resulting from the cuts in Official Development Assistance (ODA);
- Consequences for the global decarbonization trajectory of the U.S. withdrawal from the Paris Agreement and, more broadly, numerous multilateral institutions.

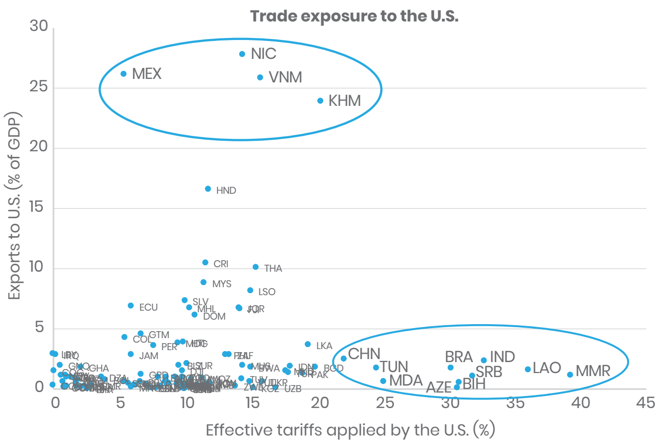
Resilience of world trade and economic growth

In anticipation of the tariff shock, exporting/importing firms ramped up their activity in the first months of 2025. Global industrial production rose by 3% year-on-year (yoy) over the first nine months of the year (3.9% in EDCs and 1% in developed countries), and global exports in volume increased by 4.7% yoy over eight months. Chinese exports rose by 7.7%, given that a large portion of exports exposed to prohibitive tariffs were swiftly redirected toward Europe and EDCs. However, EDC exports have been stagnating since the summer (Graph 1). Certain countries highly dependent on exports to the U.S., such as Cambodia and Vietnam, managed to negotiate a reduction in tariffs (26 October 2025), as did China, for which the OECD estimates the rate actually paid at 22% in December 2025. Other countries such as Azerbaijan, Bosnia, Brazil, India, Laos, Myanmar and Serbia remain subject to coercive tariffs in excess of 30% (Graph 2). Leading activity indicators, such as the manufacturing PMI (S&P Global), remain broadly expansionary, notably in the U.S. and China, neutral in the euro area, and are contracting in certain countries, including Brazil, Mexico and Türkiye. Global growth is expected to slow in the second half of this year, with only a partial recovery next year, depending notably on the easing or rise in the level of trade friction. Based on the latest IMF projections (Table 1) compared to October 2024, the cumulative loss of global output is estimated at around 0.2% by the end of 2026.

Graph 1 - Slowdown in world trade following strong momentum in H1 2025

Source: World Bank, AFD calculations.

Graph 2 - U.S. tariff discrimination toward EDCs



Source: OECD (2 December 2025).

Table 1 - Robust short-term global growth projections

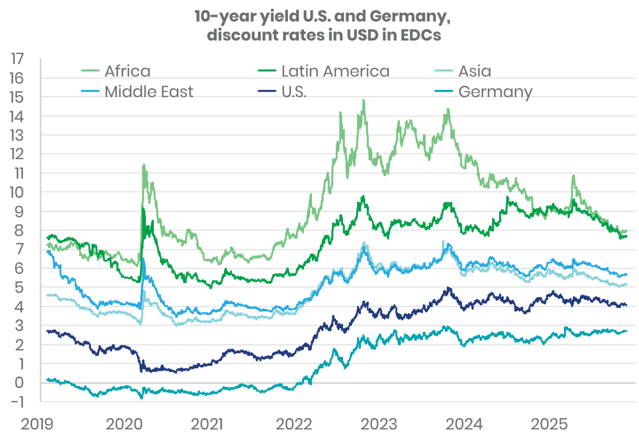
Region/country	2024	2025 (April 2025)	2025 (Oct. 2025)	2026 (April 2025)	2026 (Oct. 2025)
World	**3.3**	**2.8**	**3.2**	**3.0**	**3.1**
Advanced economies	**1.8**	**1.4**	**1.6**	**1.5**	**1.6**
U.S.	2.8	1.8	2.0	1.7	2.1
Euro area	0.8	0.8	1.2	1.2	1.1
Emerging and developing countries (EDCs)	**4.3**	**3.7**	**4.2**	**3.9**	**4.0**
EDCs Asia	5.3	4.5	5.2	4.6	4.7
China	5.0	3.9	4.8	4.0	4.2
India	6.5	6.2	6.6	6.3	6.2
EDCs Latin America	2.4	2.0	2.4	2.4	2.3
Brazil	3.4	2.0	2.4	2.0	1.9
Mexico	1.4	-0.3	1.0	1.4	1.5
Colombia	1.6	2.4	2.5	2.6	2.3
Middle East, North Africa & Central Asia	2.6	3.0	3.5	3.5	3.8
Türkiye	3.3	2.7	3.5	3.2	3.7
Morocco	3.8	3.9	4.4	3.7	4.2
Egypt	2.4	3.8	4.3	4.3	4.5
Sub-Saharan Africa	4.1	3.8	4.1	4.2	4.4
Nigeria	4.1	3.0	3.9	2.7	4.2
South Africa	0.5	1.0	1.1	1.3	1.1
Kenya	4.7	4.8	4.8	4.9	4.9

Source : FMI

Relatively favorable conditions for EDCs in the short term

The relative weakness of the dollar (6% depreciation in the real effective exchange rate in 2025) is a positive factor in terms of keeping domestic inflation under control in EDCs, monetary easing, the easing of domestic financing conditions for governments and the private sector, as well as for alleviating the external debt repayment burden of EDCs. Despite (re)financing conditions on international markets that are still higher than before 2022 (excluding the Covid-19 shock in 2020), yields on U.S. dollar sovereign bonds declined in 2025, notably in Latin America and Africa (Graph 3). In the context of resistance to the downward movement of bond yields in the U.S., this financial upturn for EDCs is thus due to a narrowing of risk premiums (sovereign spreads), associated with more favorable risk-return trade-offs and a more positive assessment of the sustainability of public finances in certain countries, including those that underwent external debt treatment under the Common Framework (Ethiopia, Ghana, Zambia) or outside the Common Framework (Sri Lanka, Suriname). For quite different reasons, countries such as Senegal and Ukraine were exceptions to this positive trend in 2025, among the 60 or so EDCs listed in the J.P. Morgan indexes.

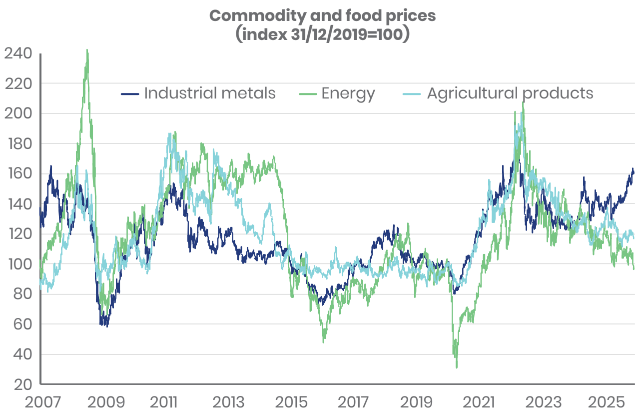
Graph 3 - Easing of international financial conditions in 2025



Source: J.P. Morgan, AFD calculations.

The external position of EDCs that are highly dependent on commodity exports, particularly in Africa and Latin America, generally benefited from the strong performance of commodity prices, especially for minerals and metals (Graph 4). The oil market is characterized by structural downward pressure on barrel prices. Global supply is fueled by the “drill, baby, drill” policy in the U.S. In addition, in late November 2025, OPEC+ decided to keep production quotas unchanged for the first quarter of 2026, following a strategy to regain market share by increasing production in 2025, due to uncertainties over seasonal demand and market balance. The International Energy Agency (IEA, World Energy Outlook, November 2025) estimates that global oil production rose by 3 Mb/d in 2025 and will increase by 2.4 Mb/d in 2026, while demand is projected to increase by "only" 0.8 Mb/d in 2025 and 2026. This trend is therefore positive for the many importing countries, both in terms of trade balance and domestic energy prices.

Graph 4 - Strong performance for mineral prices, downward pressure on oil

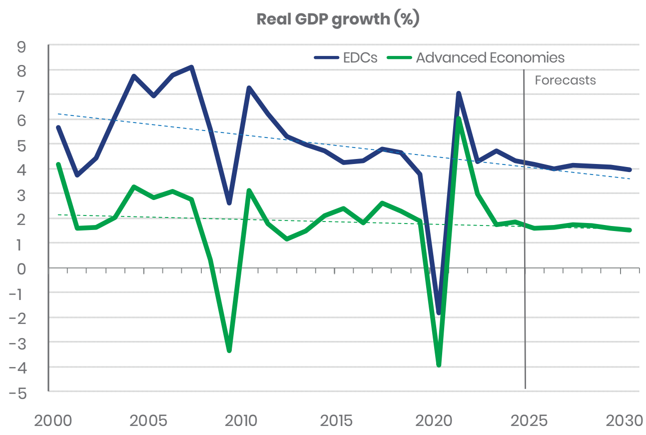


Source: Macrobond, AFD calculations.

Medium-term outlook dimmed by the prospect of a lasting conflictual geo-economic order

In the longer term, economic growth prospects, which have deteriorated in recent years (Graph 5), will depend on the capacity of countries, which has been reduced or is structurally weak in many of them, to support investment in education, public research, infrastructure, good governance, a regulatory environment that balances the need for flexibility and innovation in the private sector, effective international cooperation, and technology diffusion. This scenario is by no means taking shape, given the economic decoupling and the emerging battle over standards (*c.f.* "China Standards 2035" strategy). The AI revolution is viewed as a technological race between major powers, a source of productivity gains, and a means to compensate for labor shortages (demographic decline in China, restrictive migration policy in the U.S.), while simultaneously raising concerns over job destruction and the downgrading of many workers in advanced economies and EDCs. The development of non-tradable goods and services is becoming a key factor to consider in public policies.

Graph 5 - Downward trend and outlook for global economic growth



Source: IMF.

The world's two leading economic powers are rigging the rules of international trade and are embarked on a strategy for the predation of global resources, but China is making every effort to be perceived as a more reliable trading partner than the U.S. Xi's China and Trump's U.S. are also two sides of a capitalist economic model in which private actors are dependent on interventionist and arbitrary political power. In this context, Germany is preparing to break with decades of free-trade orthodoxy by calling for more "European patriotism" and protectionist measures to support industry in the face of Chinese competition, while simultaneously supporting the EU-Mercosur trade agreement. At the same time, some countries are taking steps to maintain open trade through initiatives such as the Future of Investment and Trade (FIT) Partnership, which could include about ten countries (Costa Rica, Malaysia, Morocco, Norway, Panama, Paraguay, Rwanda and Uruguay) centered around New Zealand, Singapore and the United Arab Emirates, as the primary founding members.

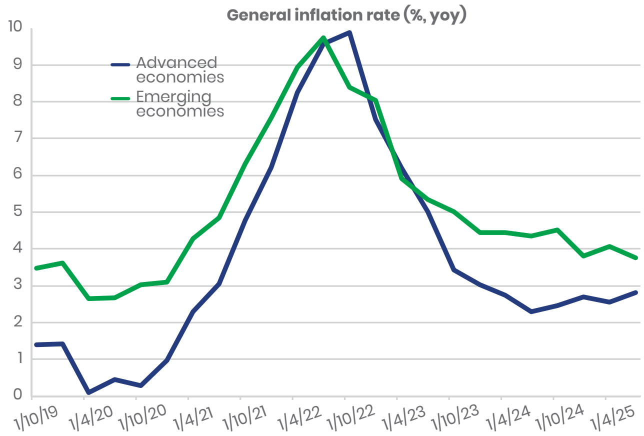
China's dominant position in critical and strategic metals gives it considerable market and bargaining power with the U.S., particularly for semiconductors, telecommunications, electric vehicles and defense. The Trump-Xi summit on 30 October 2025 resulted in reciprocal concessions for one year: a reduction in U.S. tariffs in exchange for China resuming imports of soybeans and other agricultural products, efforts to limit the shipment of fentanyl precursor chemicals and an easing of export restrictions on rare earths. This short-term window of stability does not eliminate the risk of escalation, including a currency war targeting a renminbi deemed undervalued by the U.S. (similar to the yen during the 1985 Plaza Accord).

All eyes more than ever on the U.S.

With less than a year to go before the mid-term elections (November 2026), the Trump administration's protectionist policy has shown its first negative effects on the cost of living in the U.S. and on certain producers, particularly in the agriculture sector. The most striking example is the soybean sector, a significant portion of whose markets was previously secured by the Chinese market (until China shifted more toward Brazil and Argentina), and whose potential production surpluses were redirected toward EDCs through USAID, which has since been dismantled. The White House issued an executive order on 14 November eliminating tariffs for certain agricultural products. This announcement came as the Supreme Court was preparing to rule on the legal legitimacy of the tariff policy justified under the Emergency Economic Powers Act of 2 April 2025 (up to USD150 billion in tariff refunds to the companies concerned according to the U.S. Treasury), and as the U.S. was emerging from the longest government shutdown in its history following stalled budget negotiations in Congress, which opinion polls largely attributed to the Republican camp.

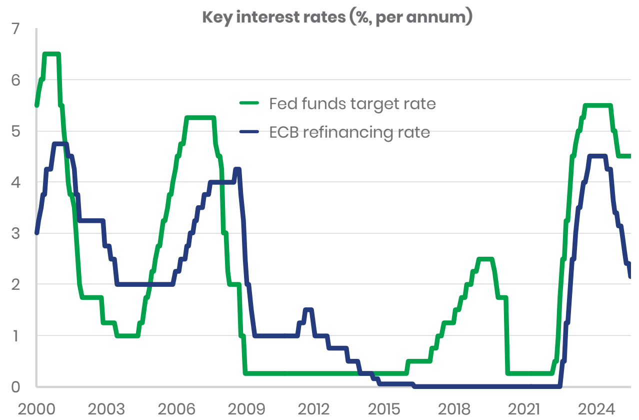
The climate of uncertainty has a major impact on monetary policy stances. Persistent inflationary risks, especially in the U.S. (Graph 6), in particular related to tariffs, stalled the Fed's pace of monetary easing until the summer, before deciding on three 25 bp rate cuts since September 2025, against a backdrop of economic slowdown and labor market concerns (Graph 7). The federal government's financing needs ($1.372 trillion borrowed over the first nine months of 2025) are absorbing substantial liquidity, which is pushing short-term rates upward. In response, on 29 October 2025, the Fed announced that it would cease the active reduction of its Treasury securities portfolio as of 1 December. It might resume the expansion of its balance sheet in the event of increased liquidity pressures in money markets. Stablecoins, backed by T-bills, are another source of monetary financing for the U.S. Treasury and for the attractiveness of the dollar, offsetting the recent blows to its dominance. However, this could eventually pose a crowding-out risk for other short-term financing needs, especially in the emerging markets most dependent on portfolio investment flows. At the same time, in China, monetary and regulatory easing has continued under deflationary pressures (GDP deflator negative for three years) and weak domestic demand. Elsewhere, the relative weakness of the dollar and disinflation facilitated monetary policy easing in the Euro area and most other countries during the first half of 2025. Central banks have now reached a potential turning point, characterized by a lack of visibility and monetary policy stances highly dependent on data.

Graph 6 - Latent inflationary risks in developed countries, particularly in the U.S.



Source: OECD.

Graph 7 - Strong uncertainty complicates forward guidance on monetary policy

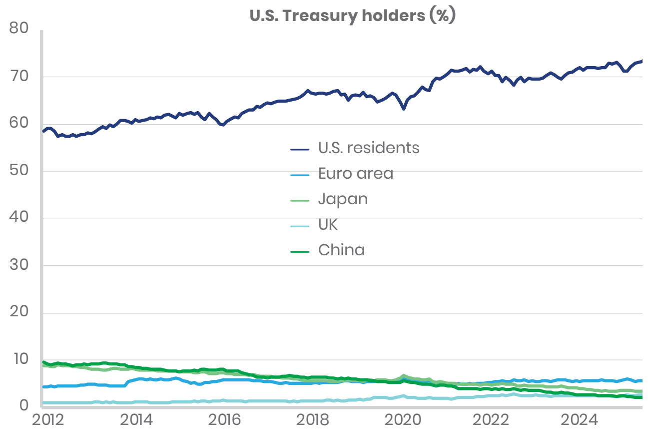


Source: Federal Reserve, ECB.

With the upcoming appointment of Jerome Powell's successor as Fed Chair (May 2026), the independence and flexibility of U.S. monetary policy are being challenged by the executive, pressure on public finances, financial market volatility, and the boom in crypto-assets. In addition to repeated attacks by Donald Trump, the appointment to the Fed's Board of Governors of Stephen Miran, Chair of the White House Council of Economic Advisers (CEA) who conceptualized the Mar-a-Lago Accord,[3] raises questions. Furthermore, the increase in public deficits and a heavier debt burden create the risk of fiscal dominance over monetary policy. This would force the Fed to act more depending on fiscal policy developments (redemption of securities and rate cuts) to contain any risk of a U.S. public debt crisis. The steepening of the yield curve, linked to the higher term premium, is a sign of the uneasiness of the markets. This is especially because the quantitative tightening has increased the proportion of Floating Rate Notes, making the market more dependent on volatile investors (mini crash of April 2025). A demonetization of the benchmark risk-free asset would cause global financial destabilization. China has continued to reduce its holdings of U.S. T-bonds (USD700 billion of securities held in September 2025, or 2% of the total, against USD1.3 trillion in 2013), unlike investors in the Euro area (5.5%), Japan (3.3%) and the UK (2.4%). The stability of the U.S. bond market is more broadly dependent on resident investors, whose share of T-bond holdings increased in 2025, rising from 60% to 74% in a decade (Graph 8).

[3] Full of contradictions and posing a risk to global economic and financial stability, this plan does not, at this stage, reflect the official vision of the Trump administration. It advocates for a dollar depreciation "concerted with partners" through an agreement reminiscent of the 1985 Plaza Accord. The objective is to support industrial competitiveness, employment and the country's strategic autonomy without harming the dollar's hegemony as the international reserve currency, while preserving the U.S. consumerist model, even if it means forcing the rest of the world to continue to finance its twin deficits on favorable terms (exchanging debt for long-term bonds), under threat of tariffs or the withdrawal of security guarantees.

Graph 8 - Decline in the share of U.S. federal debt held by non-residents



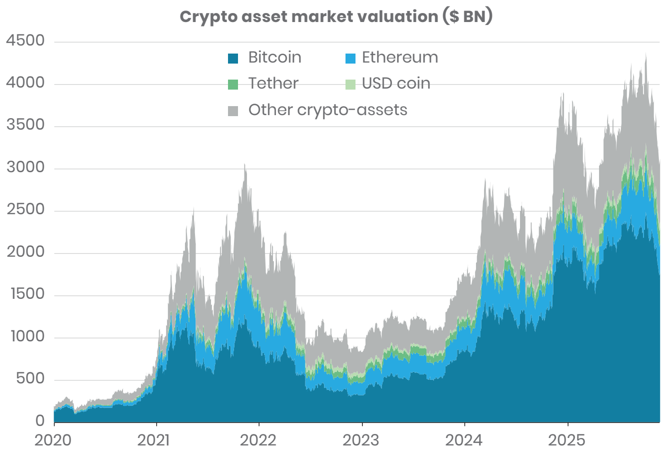
Source: U.S. Department of Treasury.

In parallel with the surge in the world price of gold, a safe haven asset and a source of diversification away from the dollar for central banks, the boom in U.S. stock markets, driven by tech and crypto-assets, has reached a level that has raised concerns about a bubble risk and overvaluation since last fall (Graph 9). The technological race led sector giants like Amazon, Alphabet, Meta and Oracle to issue a total of USD81 billion in debt between September and November 2025 to build data centers (Bank of America). At the same time, the crypto crash (-30% for Bitcoin since October) is due to a withdrawal of USD1.2 trillion from the market in just a few weeks (Graph 10). Vaunted by the occupant of the White House, crypto-assets, and specifically stablecoins (a market estimated at nearly USD300 billion in November 2025), can cause financial instability through the issuing companies (Tether, Circle), which generate revenue from T-bills and may be forced to sell these assets in case of difficulties, particularly liquidity pressures. This issue of private currencies raises the question of monetary sovereignty and the need for central bank digital currencies (CBDCs). Rejected by the Trump administration, the creation of CBDCs is underway in many countries (including China, Ghana, Kenya, Japan, Nigeria, South Africa, South Korea, as well as in the Euro area). This is also aimed at improving financial inclusion, reducing transaction costs and securing payments, much to the dismay of commercial banks, which see a direct threat to their role as financial intermediaries, their margins, and the stability of their deposit base.

Graph 9 - Exuberance of U.S. stock markets and bond market tensions

Source: U.S. Department of Treasury, S&P Global.

Graph 10 - Volatility of crypto-assets

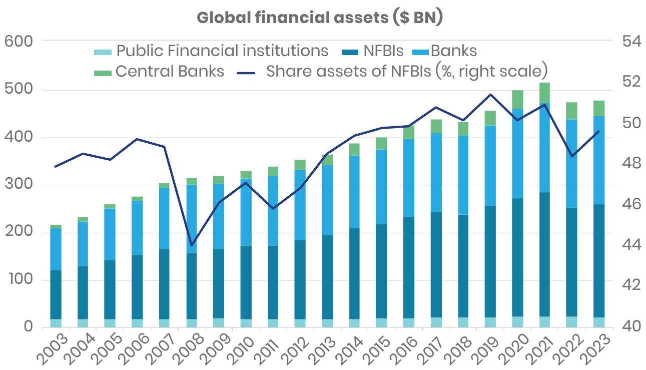


Source: OECD.

NBFIs, key players in international finance

While not a new topic, the role of non-bank financial institutions – NBFIs (including investment funds, insurance companies, asset managers, private credit and microfinance) in the global financial architecture has recently drawn specific attention from the IMF (Global Financial Stability Report, October 2025), the OECD (Economic Outlook, December 2025), and the Bank for International Settlements (Banks' Interconnections with Non-bank Financial Intermediaries, July 2025). NBFIs hold approximately half of global financial assets on their balance sheets (USD238 trillion, or 49% in 2023) (Graph 11). They play a major role in foreign exchange markets (one-third of spot transactions and strong growth in derivative markets), private credit markets,[4] real estate and cryptocurrencies, which diversifies their risks but complicates oversight.

Graph 11 - Non-bank financial institutions at the heart of the global financial architecture



Source: OECD.

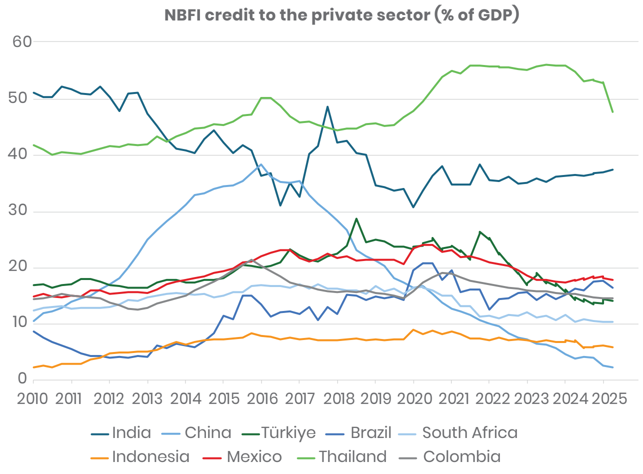
[4] The case of First Brands, while remaining manageable for the U.S. financial system, reveals the growing vulnerabilities of the private credit segment, which is currently valued at between USD1 trillion and USD2 trillion, and points to a widespread risk linked to the development of these weakly regulated debts. On 10 October 2025, First Brands Group, an auto parts conglomerate, filed for bankruptcy under U.S. bankruptcy law. Structurally fragile due to its substantial debt, the Group has suffered from commercial difficulties since the beginning of the year, notably related to tariffs, which may have been the spark that triggered the company's liquidity crisis. The losses are concentrated in private debt funds and investment banks exposed through structured credit instruments.

However, a distinction should be made between pension funds and insurance companies, which have a long-term vision and are less dependent on market volatility, with a strong presence in Asia, and mutual funds, which have a more short-term investment horizon and a relatively strong presence in Latin America. These players are not subject to the same prudential constraints as banks, which makes them less transparent in terms of assets, leverage and liquidity. The IMF and BIS warn against their strong interconnection with the banking sector (whether or not as subsidiaries). As of October 2025, bank financing to NBFIs accounted for 13% of loans allocated by U.S. banks and 7% of their assets, a doubling in three years, against 4% and 6% in the Euro area, respectively. The IMF also points to high valuations for NBFI assets (including shares, credit and real estate). It recommends improving fund governance, strengthening market infrastructure, and better planning sovereign debt issuance and management strategies to limit the risks of shocks amplified by NBFIs (liquidity risk and forced sales during periods of financial stress).

In terms of EDCs, the growing presence of NBFIs (both resident and non-resident) in domestic bond and stock markets increases absorption capacity and market liquidity by broadening the institutional investor base. Systemic risks surrounding the sovereign-NBFI-bank nexus still appear generally moderate in most EDCs. Investment funds remain minor players in financial systems still largely dominated by commercial banks, which are the primary holders of T-bills and financiers of the private sector. The development of long-term savings, funded pension systems through pension funds and an insurance culture are still far from the levels observed in advanced economies and remain uneven across EDCs. In most low-income countries (LICs) and lower-middle-income countries (LMICs), governments thus remain dependent on international savings and Official Development Assistance through external financing from donors on concessional terms, whereas there are fears that it will dry up or at least be tightened.

Faced with a trend toward the concentration of banks' asset portfolios in a few large public or private companies, and the crowding-out effect of public securities on SME and personal finance, NBFIs have a role to play in financial inclusion. The weight of their financing to the private sector is thus quite significant in many countries (Graph 12). From Chinese shadow banking[5] (which has been reduced over the last decade) to consumer credit companies, microfinance institutions and credit unions in many countries in Asia, Africa and Latin America, non-bank credit takes many forms. The past excesses, which could lead to over-indebtedness among many clients (small entrepreneurs and farmers) and the (non-systemic) failure of financial institutions,[6] highlight the ongoing challenges of financial education (learning curve), regulation and supervision. The same is true now with the boom in digital finance, seen as a tool for promoting competition, financial inclusion and lower costs for clients, but not without risks in the absence of an appropriate and effective legal framework.

Graph 12 - Significant weight of non-bank credit in emerging countries



Source: BIS.

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[5] The boom in shadow banking in China dates back to the 2008 credit crunch. Some companies with cash reserves found it more profitable to lend than to finance productive investment, thus giving rise to NBFIs. As State-owned banks were caught up by the constraints of regulatory capital requirements, local governments rapidly turned to trust companies, one of the primary forms of Chinese shadow banks. Measures taken since 2017 have led to a slowdown in the use of the parallel financial system.

[6] Microfinance crises, more or less localized and sectoral, were recorded in the 20th century, notably in Bolivia, Cambodia, Cameroon, Ghana, India, Mexico, Morocco, Nicaragua, Pakistan and Sri Lanka.

Country focus

South Africa
Kenya
Mauritius
Cambodia
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Ecuador

Soth Africa: Non-bank financial institutions, a key factor in macro-financial

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The South African financial system is developed, deep, and increasingly well-regulated. It plays a central role in economic growth, the reduction of inequalities, the financing of the energy transition, and macroeconomic stability in the country, notably due to the predominant share of public debt held by domestic financial players. However, it presents certain vulnerabilities that pose significant risks in the event of a shock. This is due in particular to the significant concentration and strong interconnection of financial players: commercial banks and non-bank institutions. The weight of pension funds, insurance companies and other investment funds gives them a central role in domestic capital markets, which is a source of risk in the event of financial and sovereign stress.

Non-bank financial institutions (NBFIs) carry a particularly significant macroeconomic weight in South Africa, with assets accounting for 200% of GDP, or two-thirds of the total financial system, in comparison to emerging economies[7] (averaging about 100% of GDP in 2023 according to the Financial Stability Board, FSB) where the size of the non-bank sector rarely exceeds that of banks. Pension funds alone account for nearly 110% of GDP in assets, including the GEPF (Government Employees Pension Fund), which makes up for 40% of the total and is the largest fund in Africa.

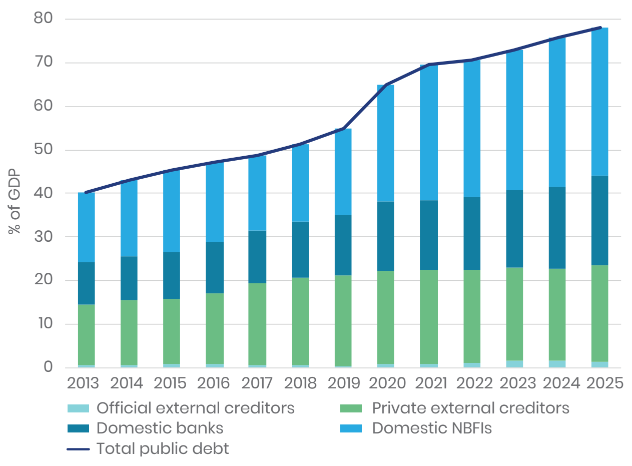
The portfolios of pension funds, insurance companies and mutual funds are deeply rooted in the domestic economy, allowing them to absorb national savings and finance the real economy (government bonds, infrastructure, energy transition and capital market development, for example). They also play an important role in financial inclusion: nearly half of the formal working population contributes to a pension fund and insurance allows households to mitigate economic and climate risks.

Banking assets amount to 100% of GDP, with 90% controlled by the country's five largest private banks, making South Africa's banking sector one of the most concentrated among emerging markets. Despite its strong performance, it shows structural weaknesses in addition to its high concentration: sensitivity to liquidity shocks, dependence on money markets and non-resident capital flows, operational cyber and infrastructure vulnerabilities (linked to the rapid digitalization of financial services and the connection with fintechs and payment infrastructure), and a growing exposure to sovereign risk.

NBFIs are at the heart of the sovereign-financial nexus

Nearly 70% of South Africa's public debt, which stood at 78% of GDP in 2025, is held by the domestic financial sector. Non-bank players hold a significantly larger share of public debt (43%) than banks (26%), which increases both resilience (local financing, lower foreign currency exposure) and the mutual dependence between the State and institutional investors. This is identified as a systemic risk by the IMF and the South African Reserve Bank (SARB).

Graph 13 - Structure of South African public debt by type of creditor



Source: IMF (WEO), AFD calculations.

[7] Argentina, Brazil, Chile, China, India, Indonesia, Mexico, Russia, Saudi Arabia, Türkiye.

The strengthening of the sovereign-NBFI-bank nexus increases the system's sensitivity to a financial or confidence shock regarding sovereign debt. A shock affecting NBFI portfolios could lead to a sudden surge in liquidity demand, a withdrawal of short-term financing, interbank and bond market stress, and could potentially trigger pro-cyclical adjustments.

Furthermore, South Africa's private sector external debt is relatively limited (15.5% of GDP), due to the depth of the domestic market which meets most of the financing needs of both banks and companies. Recent reforms aimed at improving international judicial cooperation, the supervision of non-financial risks, and increasing investigations, prosecutions and confiscation procedures related to money laundering and terrorism financing, led to South Africa's removal from the FATF Gray List in October 2025. The improvements in regulations in both the banking and non-banking sectors are expected to enhance the financial system's attractiveness for foreign investors, who currently hold 25% of domestic public debt and 30% of South African equities, according to the SARB.

The significant interconnectedness of the financial system heightens the transmission of shocks

One of the most structural and sensitive characteristics of the South African financial system is its level of internal interconnectedness, which is among the highest in the world according to the FSB, both within the banking sector, between banks and NBFIs, and through capital markets. This dense network serves as both a buffer (capacity to mobilize liquidity, market depth) and a potential amplifier of vulnerabilities, particularly during periods of stress.

Beyond interconnections through public debt (cross-holdings of sovereign bonds), banks and NBFIs are linked through funding markets, liquidity transformation, and dependence on the same foreign investors. South African banks have significant exposure to these same NBFIs, amounting to over 11% of their total assets net of provisions according to the FSB. These same banks substantially finance themselves – 35% of their total assets according to the FSB – by issuing bonds held by pension funds, insurance companies and other financial institutions. In addition, mutual funds play a central role by providing daily liquidity in the money market.

Furthermore, South African markets, considered reference assets in Africa, are characterized by a certain homogeneity in investor behavior (similar allocation strategies, identical regulatory constraints, exposure to the same macroeconomic risks), and are highly exposed to global capital flows (external debt exceeding 45% of GDP in 2025 and external financing requirements are expected to remain at around 16% of GDP until 2028 according to the IMF). NBFIs and banks thus hold similar assets that are sensitive to global volatility.

In addition, the domestic interconnectedness of financial players is increased by the concentration of non-bank players, particularly in the insurance sector, which dominates with a total of 64% of GDP in terms of assets, controlled by a handful of insurance companies investing primarily over the long term. As the sector is increasingly exposed to physical climate risks, the sharp rise in extreme events (floods, droughts and fires, for example) poses a significant macro-financial threat. Indeed, the losses of insurance companies are transmitted to the financial system through asset sales and a reduction in insurance supply, which increases the cost of capital and the vulnerability of companies and households.

The South African non-banking financial sector is thus both a structural stabilizer, through the depth it brings to the domestic market, by increasing the capacity for shock absorption and financing for the energy transition, and through its central role in social protection and inclusion. But it is also a vector of vulnerabilities through its high exposure to sovereign debt, for both the financial system and the sustainability of public finances. The stability of the financial system will depend on its sound regulation and the continuation of structural reforms: strengthening the prudential framework, integrating climate risks and improving the governance of a sector that remains fragmented.

Kenya: Assessing the systemic

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The increasing financing of Kenya's public debt by domestic banks has increased their sovereign exposure and led to a crowding-out effect on private sector financing. While these two characteristics are well-known, others are less so, notably that i) the sovereign exposure of the main non-bank financial players is also very high, and that ii) there is also a significant concentration of assets outside of government securities. Promoting more competition within the financial system and the diversification of portfolios, while maintaining sound regulation and supervision, remains a challenge in terms of reducing systemic risk and financing the real economy. In terms of demand for financing, companies continue to be cautious pending an improvement in the macroeconomic framework.

Since 2010, the public debt-to-GDP ratio has increased from 35% to 68%. The domestic share has risen from 42% to 54%, and the Kenyan government has the target of reaching 75%. Several factors have increased the interest of domestic banks in sovereign securities: firstly, the cap on private sector lending rates, in effect between 2016 and 2019, and, secondly, the tightening of financial conditions since the Covid-19 crisis, compounded by the inflationary shock following the war in Ukraine, coupled with an increased credit risk. Banks thus hold approximately 45% of government debt securities, which accounted for up to 32% of their assets in 2021 and 29% in 2024. What are the consequences of this concentration?

Growing exposure to sovereign securities

Government local-currency securities are predominantly held by the domestic financial sector. It has held 75.6% on average since 2012, with 87.4% in 2021. Banks, the main players in the financial sector with an average of 64% of assets since 2019, hold the largest share (approximately 45%), followed by pension funds (29%), insurance companies (7%), State-owned enterprises (6%) and other actors (households, non-financial private companies and other financial players such as SACCOs – Savings and Credit Cooperative Organizations). Domestic debt thus represents a significant share of financial sector assets, which rose from 25% in 2012 to 38% in 2024 (see Graph 14).

The risks associated with this exposure are compounded by the low level of liquidity in the domestic secondary market: the haircuts applied to sovereign securities used as collateral in the interbank market are very high, and remain so despite the launch of DhowCSD, a centralized platform for government securities intended to improve the transfer of securities between lenders and borrowers. The market also remains highly segmented, with interbank trading driven more by interpersonal relations than an approach based on liquidity risk management and asset valuation.

Concentration also extends to other assets

Concentration within the financial sector also extends to other assets. For banks, a stress test conducted by the Central Bank of Kenya (CBK) in May 2025 revealed that the most critical shock remains a default by each bank’s top three borrowers. In this case, there would be a capital shortfall of KSh 220.7 billion to meet regulatory requirements across the banking sector, with 84% of this amount borne by the major banks (Tier I). Bank lending is concentrated in the transport, energy, real estate and manufacturing sectors, which are also exposed to climate and geopolitical risks, as well as sovereign default risk, as some of them are parastatals.

Pension funds also concentrate their investments in three asset classes besides government securities, out of the 15 classes authorized by the regulator. They include guaranteed funds (19%), which are often themselves backed by sovereign securities, real estate investments (11%, a sector highly exposed to non-performing loans), and companies listed on the stock market (9%), with the capital market itself being highly concentrated.

Apart from sovereign bonds, which are highly profitable, insurance companies invest in their subsidiaries (9%), real estate (8%), and term deposits (7%).

A very real credit risk

Beyond the systemic risk that such a concentration can pose to the financial sector, and thus the entire economy, banks' appetite for sovereign securities has had a documented crowding-out effect on private sector credit. The penetration rate for bank lending stood at 32% of GDP in Kenya in 2024, against 27% in Sub-Saharan Africa, 39% in East and Southern Africa, and an average of 46% for lower-middle-income countries (World Bank).

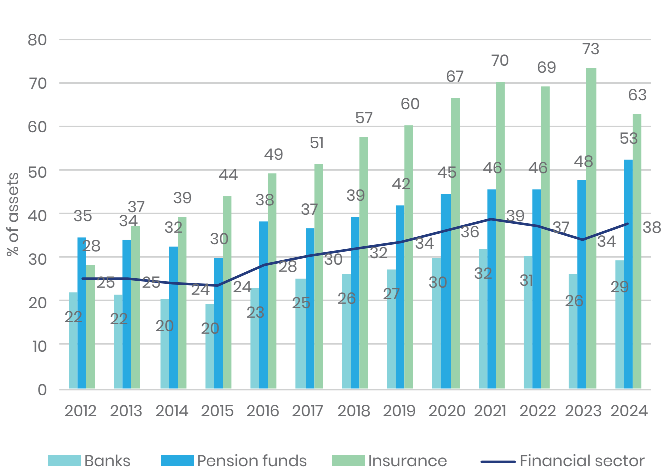
Non-bank credit providers remain minor players in financing the real economy. SACCOs allocate loans amounting to 6.4% of GDP, and loans from digital credit providers (such as Inventure's Tala, with 10 million users, and Safaricom's M-Shwari, with 32 million users) do not exceed 2% of GDP, although they doubled within a year and there were ten digital borrowers for every non-digital borrower in 2023.[8][9]; There has been a huge increase in small personal loans since the pandemic. The annual average stands at 65.6 million, a 63% increase compared to 2019/20, against +7% for business loans, which account for half of the total value of loans. Cash flow requirements take precedence over investment behavior: the number of household savers fell for the first time in 2024 and credit is increasingly used to cover daily needs or emergencies (75%, against 60% in 2016) rather than for investment (42%, against 56% in 2016).

Kenyans also rely on informal sources of credit provided by traders, peer groups ("chamas"), and purchases using digital credit, for example, with Fuliza, a revolving credit system connected to M-Pesa, which has 33 million users. These multiple offers highlight the fragile financial situation of households, for which the poverty rate has still not returned to pre-pandemic levels. They also point to a high credit risk for the banking sector: the loan default rate stood at 16.6% in 2024, against 10.7% in 2021 and the non-performing loan ratio reached 13.7% in 2024, against 9.7% in 2019.

However, the new financial players carry new risks: low inclusivity, prohibitive interest rates and a lack of regulation, along with operational risks such as cyberattacks, which concern all players in the financial sector (43% of banks report being victims in 2024). In an effort to address all or some of these problems, the government has enacted a law to regulate digital credit providers, for which the number of licenses granted increased from 52 in mid-2024 to 85 in mid-2025 and, finally, 153 by year-end 2025, out of 550 applications. It has also created a "Hustler Fund", a government fund providing instant digital loans which is proving very successful (20 million loans), but also has a high default rate.

Thus, while the crowding-out effect is indeed present, credit supply and demand also reflect an unfavorable macroeconomic situation, and a very real credit risk associated with the difficulty of investing profitably: uncertain economic prospects, tax burden on the far too few formal sector players, low productivity, inefficient infrastructure and sometimes ill-suited economic policies (interest rate caps, overvaluation of the shilling).

Graph 14 - Exposure of Kenyan financial players to sovereign securities



Source: Central Bank of Kenya (CBK).

[8] See 2024 FinAccess, Household Survey and Kenya's credit, market landscape.

[9] Unsecured and non-collateralized loans distributed through a mobile or digital channel.

Mauritius: Offshore financial sector, pillar of a changing economy

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While Mauritius is on a growth path that should enable it to join the Seychelles in the very small club of high-income African countries by the end of the decade, the economic situation is unfavorable and the new administration, which came to power in late 2024, is forced to urgently and substantially consolidate public finances. The sluggish global economy, amidst the tariff war imposed by the U.S., is affecting the growth of this small island State, which is sensitive to international headwinds. The new government is aware of these vulnerabilities and intends to leverage Mauritius' historical capacity for reinvention, which has enabled it to become a modern and developed country. The objective is to reduce dependence on imports by redirecting its economic model toward more investment and productivity gains. To finance its new direction, it should be able to count on the participation of its important banking and non-banking financial sector.

At the general elections of November 2024, the pendulum swing proved fatal to the Alliance Lepep, which virtually vanished from the political landscape. By penalizing the team in power for the last 10 years, voters, who turned out in massive numbers (79% participation, a 20-year record), expressed their need for change following the end of a term marked by cost-of-living pressures, political scandals, and cases of corruption that have eroded the country's strong governance indicators. The new administration is faced with a structural slowdown in economic growth, which is increasingly reliant on consumption, and has inherited a degraded public finance situation.

Restoring fiscal discipline

Increases in social benefits (retirement pensions), the wage bill (wage hikes, exceptional 14th month bonus) and subsidies... In the context of the 2024 elections, public spending veered off track, rising by 28% between the two 2023/24 and 2024/25 fiscal years, resulting in a public deficit (7.2% of GDP) not seen outside of the Covid period. Consequently, the public debt-to-GDP ratio has begun to rise again, reaching 88.4% in June 2025, according to the Ministry of Finance.

To redress the situation, which could cause the country to lose its Investment Grade sovereign credit rating,[10] the Ramgoolam government has decided to implement shock treatment for public finances. The consolidation involves a reform of the revenue framework, notably by targeting the numerous tax exemptions inherent to the Mauritian liberal economic model. This includes broadening the base for income tax, corporate tax and VAT, increasing excise duties on alcohol, cigarettes and vehicles, and taxes on high earners and highly profitable companies. The objective is to increase total revenue by 3.7 pp of GDP to reach an unprecedented level of 29% of GDP. Spending is also targeted (-1 pp of GDP compared to the previous fiscal year), with a flagship measure: a gradual increase in the eligibility age for the basic retirement pension.

Overall, the government's highly ambitious plan is to halve the public deficit within a year and bring down the debt ratio to below the official 80% ceiling by the end of the 2027/28 fiscal year. To achieve this, it will require robust economic growth. However, growth is tending to slow.

Toward a deep structural reform to boost potential growth

Following the historic recession in 2020 (-14.5%), caused by the unprecedented impact of the health crisis on this small island economy, it took two years for economic activity to return to pre-pandemic levels. For 2023 and 2024, the highly positive estimates published by the previous government (7% and 6.1%) were revised downward to around 5% for both years. However, growth has remained robust, driven by major

[10] In January 2025, Moody's, which rates the country at Baa3, downgraded the outlook from stable to negative.

infrastructure projects and the strong performance of international tourist arrivals (+7% in 2024 compared to 2023 and +9% in tourism receipts) and financial services.

However, the restrictive policy mix and the international context are affecting the prospects for growth, notably U.S. decisions on tariff hikes (15% for Mauritius after an initial rate of 40%) and the delays in the extension of the AGOA (African Growth and Opportunity Act). The Central Bank is thus maintaining its key interest rate at 4.5% to anchor medium-term inflation expectations. This is all expected to limit growth to 3.2% in 2025, despite a tourism year that promises to be exceptional. In 2026, economic activity is expected to continue at this pace (3.4%).

The new government has taken stock of the downward trend in growth, as a result of high exposure to the international situation (import prices and tourism, for example) and an aging population. It wishes to redirect the model focused on the consumption of imported goods toward investment and the diversification of exports. The objective is to return to a more inclusive economic growth rate of 5% in the medium term by building on the fundamentals: high-quality infrastructure, labor market flexibility and an investment-friendly business environment. To achieve its objective, the country can rely on the offshore sector, which is a pillar of its financial system, alongside banks.

Offshore financial sector: a structural pillar of the economy

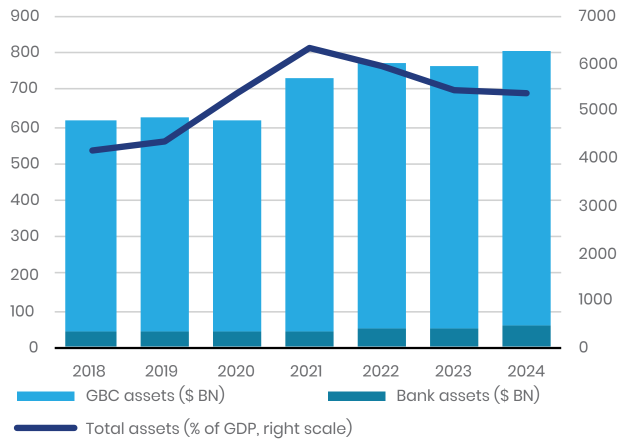
The distinctive feature of the Mauritian financial center is the massive presence of special-status companies (Global Business Companies and Authorized Companies) with international operations. They are incentivized to establish themselves due to the favorable tax rate and the double taxation agreements signed between Mauritius and more than 40 countries. In 2024, total assets in the offshore sector reached a record level of $751 billion (with 75% in equity and 11% in loans), accounting for 90% of financial sector assets and approximately 50 times the GDP of Mauritius.

Alongside local insurance companies, pension funds and leasing companies (accounting for approximately 11% of financial assets), a significant portion of offshore companies are non-bank financial institutions which play an international intermediation role in capital raising and asset management. A familiar feature of the Mauritian economic landscape for over 30 years, they directly or indirectly account for 8.3% of Mauritian GDP according to the latest data from the Bank of Mauritius, through exports of financial services, the tax revenue they generate, the skilled employment they offer, and the domestic services required to support their operations.

The external flows associated with them are a major component of the current account: service exports (consulting, management) and primary income inflows (profits repatriated from subsidiaries, dividends). As Mauritian residents, they receive financial transfers from their parent companies, recorded as foreign direct investment (FDI), which are reinvested abroad as FDI, portfolio investments and other investments. The levels of these substantial flows are volatile and unpredictable, especially during periods of international instability.

The ongoing strengthening of the regulatory framework and prudential tools is essential to prevent macro-financial risks in the offshore sector. Maintaining high foreign exchange reserves also serves as a strong buffer given the sector's volatility. They reached nearly $10 billion in September 2025, equivalent to 13 months of imports of goods and services.

Graph 15 - Assets related to Global Business Companies are disproportionate to the size of Mauritian GDP



Source: IMF, Financial Services Commission.

Cambodia: Between external shocks and a fragile financial system

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Cambodia's economic growth, which had regained strong momentum after the health crisis, is now showing signs of a slowdown. Trade tensions with the U.S. are significantly weakening the economy. Indeed, more than a third of Cambodian exports rely on the U.S. market, and the conflict with Thailand could dampen the recovery of the tourism sector. In this context, growth forecasts for 2025 have been revised downward to around 4.8%. However, the banking sector remains the main vulnerability. Private debt has reached very high levels, non-performing loans are rising, and the real estate market – long supported by Chinese financing – is now showing a marked slowdown. Furthermore, the relatively developed non-bank financial sector has similar weaknesses, which heightens systemic risks.

Predominantly an agricultural country in the early 1990s, Cambodia has progressively embarked on an industrialization process, while significantly liberalizing its economy. This openness is reflected in a trade openness ratio) which reached 143% in 2024, a twofold increase in 30 years. Industry (45% of GDP, including 28% of GDP for the manufacturing sector) first developed around the garment industry (11% of GDP), supported by low labor costs and preferential access to major markets, notably the U.S. and the European Union. More recently, construction (11% of GDP) and the electronics industry have driven growth in the secondary sector, while the development of the banking sector and strength of the tourism sector (10% of GDP) have bolstered the performance of the tertiary sector (39% of GDP). Since 2010, Cambodia has benefited from sustained growth, averaging over 7%, but the Covid-19 crisis highlighted the country's dependence on external demand.

Stability now undermined

The post-Covid recovery had regained strong momentum (6% in 2024), driven by international demand, a robust manufacturing sector, and a marked rebound in the garment industry. However, domestic demand remains weak, hampered by persistent difficulties in real estate and construction, which are themselves affected by the Chinese economic slowdown. Furthermore, foreign trade now faces an increased risk of geo-commercial fragmentation, while renewed tensions with Thailand pose a direct threat to the tourism recovery. In this context, the IMF has revised its forecasts downward: growth is expected to slow to 4.8% in 2025 and 4% in 2026.

Highly integrated into global value chains, Cambodia benefits from numerous trade agreements. However, it now needs to anticipate the loss of its least developed country status, expected between 2027 and 2030, which will lead to the end of preferential treatment for its exports.

Furthermore, the new U.S. trade policy poses an additional threat. The agreement of 26 October 2025 set a reduction in tariffs (19%, against 49% initially), but they remain high (3.6% before the reform), whereas the U.S. accounts for 37% of exports. While exports surged in the first half of 2025 (+21% compared to H1 2024) in anticipation of the new tariffs taking effect on 1 August 2025, the negative effects will be visible starting in 2026. They will vary depending on the weight of the sectors (share of the country's total exports) and their exposure (share of the U.S. market in their exports). The garment, plastics, rubber, leather and electrical appliance sectors will be particularly hard hit. Cambodia could also be affected by U.S. sanctions targeting countries that authorize the re-export of products from Chinese factories established in their territory.

The border dispute with Thailand, which had been simmering for several years, escalated in February 2025, resulting in 43 deaths in July. This had an immediate impact on tourism: -10% in the first half of 2025 compared to H1 2024, followed by a 30% decline during the summer. Despite a ceasefire signed on

26 October, clashes persisted, prompting Thailand to suspend the agreement on 10 November, with fighting resuming on 7 December before a new ceasefire agreement was reached on December 27, 2025.

Growing concerns over bank finance

The banking sector remains vulnerable due to the limited supervisory capacity of the National Bank of Cambodia (incomplete implementation of Basel III) and very rapid credit growth over the last two decades, primarily driven by corporate lending. Private debt is high, with a credit-to-GDP ratio of 125% in 2024, excluding shadow banking, and financial risks are increasing: deteriorating asset quality, declining profitability and a credit slowdown (3%). The real estate and construction sectors, accounting for 22% of loans in 2024, continue to face a bleak outlook for 2025–2026. The non-performing loan (NPL) ratio exceeded 8% in mid-2025, and provisioning remains insufficient (net NPLs at 17.2% of equity in April 2025).

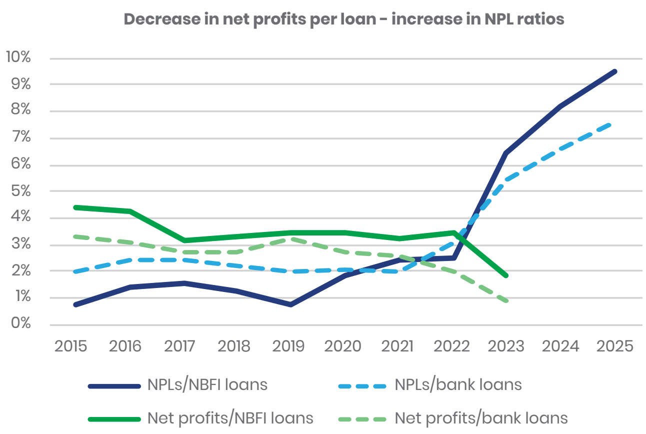
In August 2024, the National Bank of Cambodia authorized banks to restructure their loans twice without reclassification or additional provisioning. This restructuring reached $4.4 billion in 2025 (10% of total loans). This regulatory forbearance provided temporary relief, but its expiry in December 2025 is expected to lead to a further increase in NPLs.

Microfinance: a pillar, under pressure

The Cambodian non-bank financial sector primarily consists of microfinance, which has undergone a significant transformation over the last decade. Indeed, it has become a crucial pillar of the national financial system, with about 50 institutions accounting for 10% of total private sector credit in 2023. In 2024, the dynamics of microfinance were paradoxical: while the number of borrowers declined (1.48 million), there was a slight increase in total outstanding loans ($5.16 billion). This decrease suggests difficulties in attracting new clients or maintaining the existing client base in a time of economic uncertainty. However, it also shows that active clients are borrowing larger amounts.

These developments are coupled with a deterioration in the quality of loan portfolios. The NPL ratio rose from 5.7% in 2023 to 8.2% in 2024 and is expected to reach 9.5% in 2025. This deterioration is due to the global economic slowdown and the increasing vulnerability of households and microenterprises. The National Bank of Cambodia's August 2024 circular encourages loan restructuring to support the most vulnerable borrowers.

Graph 16 - Decrease in net profit per loan, increase in NPL ratios



Source: National Bank of Cambodia.

Cambodian microfinance is largely based on small loans, with 71% of borrowers contracting amounts of $3,000 or less. However, these loans only account for 24% of the total outstanding amount. The sectoral distribution of loans shifted between 2009 and 2024. Agricultural financing, once dominant, fell from 42% to 21%, raising concerns over the resilience of a sector already vulnerable to climate change and market fluctuations. Trade sectors declined to 20%, while services rose to 12% and construction to 7%, reflecting growing demand for urban and infrastructure-related activities. However, the most significant change concerns loans to households, which now account for 33% of the portfolio, indicating an increase in non-productive loans for personal debt to cover needs such as education, healthcare and daily expenses.

At the same time, there has been a marked increase in savings in the sector. The number of depositors has almost doubled since 2020, reaching 2.1 million in 2024, and the volume of deposits has increased from $1.8 billion to $2.5 billion. This trend demonstrates the public's increased confidence in microfinance institutions.

India: Financial sector reshaped by the rise of new players

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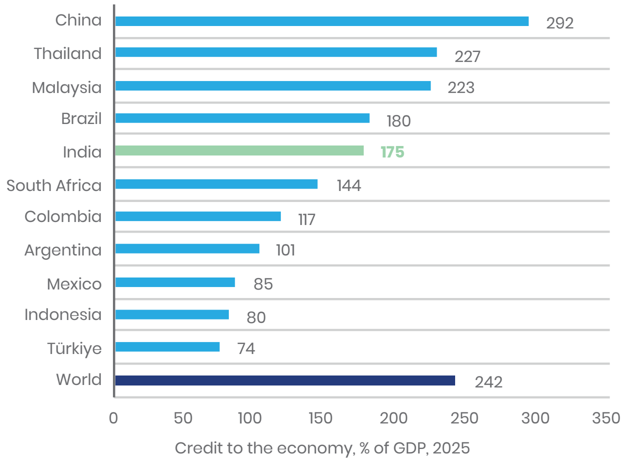
India became the world's fourth largest economy in 2025 (ahead of Japan), while remaining a lower-middle-income country (LMIC). In view of its level of development, it benefits from a relatively deep and inclusive financial sector. While the financial system has been historically dominated by public banks, it has undergone significant transformations over the last 30 years, becoming more diversified and complex. In addition to private banks, which capitalized on the waves of liberalization of the 1990s, then the difficulties of public banks to expand, a multitude of non-bank players have emerged, ensuring a certain dynamism within the financial sector.

Despite ongoing development challenges, India has a relatively deep and inclusive financial sector. Indeed, as the poorest of the major emerging countries, it ranks in the upper average of this group of countries in terms of assets held by the financial sector and credit provided to the economy. Similarly, India's financial inclusion indicators are generally satisfactory, despite significant disparities between states, with 89% of the population holding an account with a financial institution (including mobile money) in 2024, against 54% ten years earlier according to the World Bank. This relatively high level of development is partly due to the diversity of players within the financial system, primarily banks, but also a myriad of non-bank entities.

Graph 17 - India's financial sector is relatively deep



Source: Bank for International Settlements.

Historically dominant, public banks are facing increasing competition from private banks…

While the Indian economy is moving toward liberalization and international openness, the State continues to play a structural role, shown by the dominance of public banks in the financial sector. However, the market share of the country's 12 State-owned banks has gradually been declining over the last 30 years. Indeed, while they accounted for over 90% of banking assets in the 1990s and still 75% in 2010, they now only hold just over half (55%), against 38% for Indian private banks and 6% for foreign banks (excluding local, regional and cooperative banks).

This relative decline of public banks has occurred in several phases. They first faced competition from new players as of 1991–1992, following the liberalization of the banking sector, which enabled the development of private entities. These entities had previously been marginal, but experienced a rapid expansion in the 2000s. Public banks subsequently went through a highly turbulent period in the 2010s, which indirectly fostered the growth of private entities. Indeed, after having massively and laxly financed the development of the economy in the 2000s (with loan growth around 20% per year), the financial situation of the Indian banking sector deteriorated, primarily for public banks, in particular due to the slowdown in economic growth and deterioration of external conditions. The non-performing loan (NPL) ratio for public banks peaked at 16% in 2017, while their profitability remained negative for five consecutive years (from 2015 to 2020). While the quality of the assets of private banks also deteriorated during this period, their NPL ratio was below 6%. In response, the Reserve Bank of India (RBI) implemented stringent consolidation measures as of 2015. A comprehensive asset quality review was conducted, the definition of non-performing loans was broadened, and regulatory requirements were raised, in particular with the application of Basel III regulations. At the same time, a wave of recapitalizations took place, and ten public banks were merged into four entities to strengthen the levels of capitalization. Credit restrictions were imposed, a debt restructuring framework was established, and a bad bank was set up to acquire $25 billion in non-performing loans. This consolidation led to a spectacular recovery in the balance sheets of public banks, with the NPL ratio falling to 3% in 2025. At the same time, however, these measures weighed heavily on their dynamism. Public bank assets thus only accounted for 52% of GDP in 2024, against 68% in 2015. Over the same period, the assets of Indian private banks continued to increase, rising from 19% to 36% of GDP.

…but also from a myriad of non-bank financial players

Beyond banks, the last 30 years have also been marked by the rapid development of non-bank financial players: insurance companies, investment funds, pension funds and non-banking financial companies (NBFCs). The latter category is highly developed in India and is composed of around 10,000 very heterogeneous entities: some are public, a minority can collect deposits and many of them conduct financial intermediation activities without a banking license (shadow banking). The aggregate weight of these various non-bank financial players has thus grown significantly, with total assets increasing from 37% of GDP in 2010 to over 80% today.

This development of non-bank financial players was also fostered by the waves of liberalization in the 1990s and 2000s (opening up to competition, growth of capital markets and development of modern payment infrastructure, for example). It has profoundly transformed the structure of the Indian financial system. Indeed, these players have contributed to innovation in the sector (digitalization, leasing, asset-based lending and microcredit, for example), and improved its resilience by strengthening the interdependence between players. As their activities are largely complementary to the activities of traditional banks, they have also helped structure capital markets, diversify sources of financing for the economy, and improve financial inclusion by targeting previously underserved segments (infrastructure, real estate, industrial SMEs, microfinance and consumer credit, for example). The IMF estimates that nearly half of private sector credit now comes from non-bank players. For the Indian State, these developments have also expanded the potential investor base for public debt, the level of which is structurally high (81% of GDP at the end of 2025).

However, the emergence of non-bank financial players has introduced new risks and an increased need for regulation. In this respect, the case of NBFCs is emblematic. In addition to providing functions complementary to the traditional banking sector, they largely capitalized on the sluggishness and caution of public banks during the 2010s to position themselves as an alternative source of financing. Historically subject to less supervision, mostly non-deposit-taking, reliant on banks and capital markets for their refinancing, and often highly specialized by sector, NBFCs have specific vulnerabilities. In 2018-2019, the defaults of two major players – Infrastructure Leasing & Financial Services (IL&FS) then Dewan Housing Finance Limited (DHFL) – triggered a crisis of confidence and a sudden liquidity crunch, leading to a contagion effect and significant turbulence for the sector (with NBFC non-performing loan ratios peaking at approximately 7% between 2018 and 2020). In response, the RBI implemented a major tightening of its prudential regulations, particularly regarding liquidity management and supervision, which has since led to a marked recovery in balance sheets (with the NPL ratio falling to 3% in early 2025).

Indonesia: A sound but underdeveloped financial system

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To achieve its objective of becoming a high-income country by 2045, Indonesia would need an economic growth rate of at least 8% per year – a rate higher than the 5% average seen over the last 20 years. The Indonesian financial sector is one of the drivers supporting growth in economic activity, but it remains relatively small, dominated by banks, and still has a limited role in private sector financing. The assets of non-bank financial institutions are relatively small compared to other G20 emerging economies.

Indonesia was classified as an upper-middle-income country (UMIC) in 2022, after a brief first period in 2019 (followed by a return to LMIC status in 2020 and 2021). The standard of living of Indonesians has more than doubled since 2000, and the Human Development Index has improved significantly over the last three decades (from 0.52 in 1990 to 0.73 in 2023), reaching a high level. In addition, there has been a marked decline in the national poverty rate, from 16% in 2005 to 8.5% in 2025. Income inequality has also shown a downward trend over the last decade (Gini coefficient of 0.34 in 2024, against a peak of 0.41 in 2013), but remains higher than in certain neighboring countries (India, Thailand, Vietnam). However, alongside this social progress, there has been an erosion of the middle class, which now only accounts for 17% of the population (against 21% in 2019), whereas it is one of the main growth drivers through its resilient consumption.

In pursuit of higher growth

Real GDP growth has been sustained for two decades (+5% per year on average between 2005 and 2024), driven by the dynamism of private consumption. Indonesia has historically experienced less volatility in its economic activity than its neighbors, as it is less dependent on the international economic climate. This trend is shifting, as Indonesia has become more dependent on the Chinese economy (with 24% of its exports destined for China, against 15% in 2020).

The country has established a target and a roadmap to become a resilient, prosperous, inclusive and sustainable high-income country by 2045 – the centennial of its independence. To reach this target, the authorities are aiming for GDP growth of at least 8% per year, a significantly faster pace than its average growth between 2005 and 2024.

While at the beginning of 2025, GDP growth was expected to be below 5% (IMF forecast of 4.7% in April 2025), the authorities have taken several steps to support the growth rate: fiscal stimulus, five cuts in policy rate in 2025 totaling 125 basis points to reach 4.75% in October, its lowest level since 2022, and $12 billion in liquidity injections into the banking system for productive financing. The IMF has revised its forecast to 5% for 2025 and 5.1% for 2026. Bank Indonesia estimates growth to stand at between 4.7% and 5.5% in 2025, before accelerating in 2026.

The country has a sound macroeconomic framework and buffers against shocks, enabling it to undertake the structural reforms needed to increase its per capita income. Indeed, foreign exchange reserves are at an adequate level (covering close to 6 months of imports), inflation is well anchored within the central bank's target range (2.5% ±1%), and the public finance situation is comfortable, with fiscal space available to increase public revenue (currently at least 6 percentage points of GDP below its potential)[11] and finance productive investments.

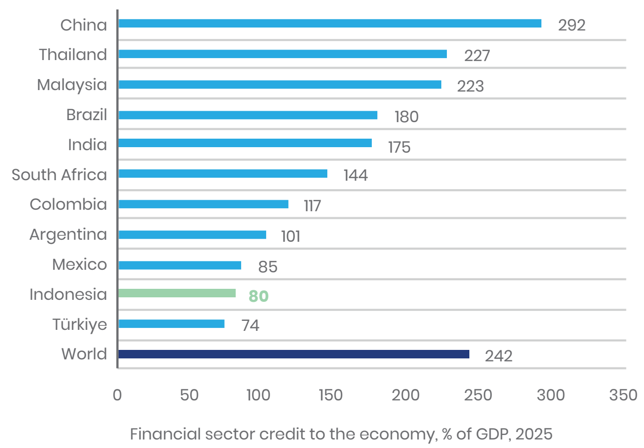
[11] World Bank (2024), Indonesia Economic Prospects, December 2024: Funding Indonesia's Vision 2045.

A financial sector with limited private sector financing

While it could play a leading role in financing the economy, and the private sector in particular, the Indonesian financial sector remains relatively small. It is dominated by well-capitalized banks, several of which are State-owned. The four largest public banks thus account for 40% of credit. The conservative risk management of banks fits in with a regulatory framework compliant with international standards (Basel III). The high level of the solvency ratio (CAR at 24.3% in the second quarter of 2025) allows the banking sector to absorb shocks, although some smaller banks are fragile. Asset quality is good (non-performing loan ratio of 2%), and the Omnibus Law on Financial Services, which came into effect in January 2023, has reorganized banking supervision by clearly defining the respective mandates of the regulator (OJK) and the Central Bank (Bank Indonesia – BI).

Private sector financing by Indonesian banks remains moderate in proportion to GDP. It stood at 36% in 2024, compared to an average of 65% in G20 emerging economies, excluding China. Similarly, the financial sector (both banking and non-banking) lacks depth, with total credit to the economy accounting for 80% of GDP, whereas it is significantly higher in most other emerging economies (see Graph 18).

Graph 18 - Indonesia's financial sector (both banking and non-banking) lacks depth



Source: Bank for International Settlements.

Non-bank financial institutions, which include insurance companies, pension and guarantee funds, microfinance institutions, fintechs and other financial entities, have not experienced the same growth rates as in other emerging economies. According to OJK data, at the end of September 2025, total assets in the insurance and pension fund industries only accounted for 11.8% of GDP and had shown weak growth in recent years. At the same time, while credit allocated through digital finance remains limited (outstanding financing at 0.4% of GDP), it appears to be increasing more rapidly (+22% year-on-year in September 2025).

There has been a significant improvement in financial inclusion, with the bank account usage rate increasing from 76% of the population in 2019 to 91% in 2025.

Through monetary easing and macro-prudential measures, authorities seek to support private sector financing and to boost credit growth which is slowing down since 2024. In 2024, credit to private sector only increased by 7.7%. In 2025 it rose by 8.1%, a rate close to the lower bound of BI's target set between 8% and 11%. The cuts in the key interest rate in 2025 led to a downward trend in the money market reference rate (IndONIA), which fell by 200 bp in 2025, reaching 3.74% in January 2026. This could contribute to stronger credit growth in 2026. In addition, to increase financing for sectors aligned with national priorities, in 2024, the Central Bank decided to ease reserve requirements for loans to certain sectors, including housing, agriculture, small and medium enterprises and the environment.

Türkiye: Banking system the backbone of the economy

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To further redress the macro-financial imbalances generated by the expansionary policy (low interest rates and credit boom), it is essential to sustain the "normalization" of the economic policy introduced in 2023. This expansionary policy led to economic overheating, inflation, external deficits, loss of investor confidence (especially at the local level), financial dollarization, a plunge in the lira, and impoverishment. Walking a tightrope, the Turkish economy has managed to avoid a balance of payments crisis similar to in 2000–2001, a trauma deeply embedded in the collective memory, through rapid (often temporary) monetary policy readjustments, healthier public finances, and a fundamentally sound and agile banking system.

The opening and liberalization of the economy in the 1980s had made the Turkish financial system more vulnerable to external shocks. The 1994 crisis was an early warning of the major systemic crisis of 2000–2001, highlighting the weaknesses of the banking system, as it is highly dependent on short-term external financing, within a failing regulatory and supervisory framework. The sector has since been thoroughly restructured and strengthened, while remaining a pillar of economic policy.

Transmission mechanism of Erdoğanomics

The expansion of bank credit since 2010 has been a powerful driver of domestic demand and economic growth, fueling the current account deficit and a spiral of exchange rate depreciation and inflation. The accommodative bias of monetary policy, its unpredictability, and political interference became more acute following the attempted coup of July 2016 and the exchange rate crisis of the summer of 2018, a consequence of economic overheating and U.S. sanctions during the first Trump term. Bilateral relations have since eased considerably, even in the midst of the current "universal" trade war, as shown by Recep Tayyip Erdoğan's visit to the White House at the end of September 2025.

In the early 2010s, the excess foreign exchange liquidity of banks, driven by the limited confidence of savers in the lira (TRY), led to the creation of a Reserve Options Mechanism, allowing banks to hold a portion of their reserve requirements in foreign currency or gold (2011). The aim of this system was to buffer liquidity shocks while boosting gross foreign exchange reserves on the balance sheet of the Central Bank (CBRT), yet it proved to be counterproductive. By encouraging foreign currency indebtedness among banks, it complicated financial intermediation and transformation, and weakened the effectiveness of monetary policy, before finally being repealed in June 2023.

Following the attempted coup in 2016, the surge of "patriotic liraization" reduced the euro-dollarization rate of deposits to below 40%, before it climbed back to a peak of 70% in December 2021. Meanwhile, in response to the slowdown in economic activity, state-owned banks took on an increasingly important role as the main driver of the expansionary economic policy through private sector credit (peaking at 71% of GDP in 2022), backed by a State guarantee fund. Private commercial banks (Turkish or foreign-owned) maintained a prudent management of their credit portfolios. The three major state-owned banks (Ziraat 1st, Vakif 2nd and Halk 4th) now account for 41% of the banking system's assets (30% in 2014), 42% of credit allocated, and 47% of deposits. But they have benefited from significant State recapitalizations to maintain their solvency. Furthermore, the regulatory easing, moratoriums and foreign currency deleveraging of non-financial corporations have helped prevent massive bankruptcies.

Following a brief period of monetary tightening (end of 2020-mid-2021), the financial engineering and regulatory straitjacket, deployed as of December 2021, aimed to address the depletion of foreign exchange reserves and soaring inflation resulting from the monetary easing driven by the executive. More palliative than curative, and coercive for banks and companies, the arsenal of measures aimed to "reliraize" the economy and attract foreign currency liquidity through various instruments: mechanism for bank deposits in lira hedged against the foreign currency risk (KKM) guaranteed by the CBRT, prohibition on banks from lending in lira to companies holding "excessive"' foreign currency, forced conversion and increased fees on foreign currency deposits, and extension of foreign exchange swaps between the CBRT and public banks to support foreign exchange reserves. Furthermore, the mandatory collateral in government securities on loans allocated by commercial banks, at interest rates higher than 1.8 times the key interest rate, resulted in captive demand for T-bills (up to 19% of total bank assets in 2022) and a sharp drop in the bond yield curve.

Saver confidence maintained

Since June 2023, following the re-election of Recep Tayyip Erdoğan, political turmoil, such as the arrest of opposition leaders, including the Mayor of Istanbul in March 2025, has again weakened the lira, but has served as a positive test for monetary governance. The fact that there have been no deposit runs in recent years demonstrates saver confidence in the banking system. The end of KKM deposits came into effect in August 2025, the regulatory requirement for 60% of deposits to be in lira has been met since May 2024, and deposits are rapidly increasing. However, the IMF highlights the need to improve the capacity for the resolution, assessment, planning and funding of the Savings Deposit Insurance Fund (SDIF). Furthermore, restoring the operational autonomy of the financial regulator (BDDK) and realigning regulatory and accounting practices with international Basel standards remain challenges.

While slow disinflation (30,6% in 2025) allows for very gradual monetary easing, credit remains regulated (monthly ceiling on growth in commercial loans), and regulation restricts access to external financing. Intermediation margins are squeezed, but bank balance sheet ratios remain satisfactory in terms of solvency (CAR at 18.2% in August 2025), profitability (ROA at 1.5%), and loan portfolio quality (NPL ratio at 2.2% in August 2025, just as the OCER). Banks are taking advantage of the easing of sovereign spreads, which are at a ten-year low (230 bp in USD and 140 bp in EUR), to (re)finance internationally on relatively favorable terms.

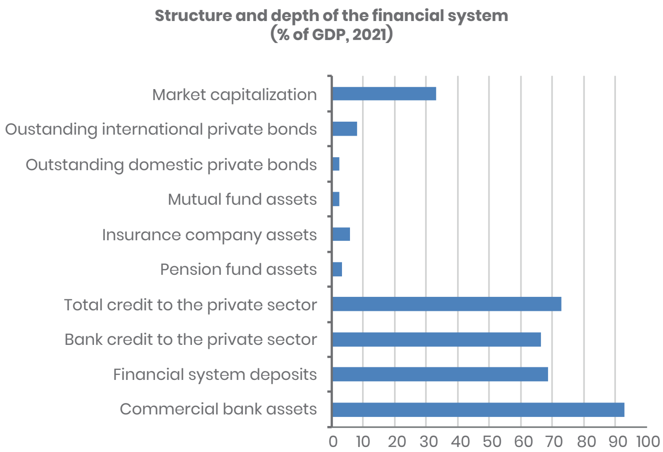
NBFIs still minor players

In a financial system largely dominated by the banking sector, the financing role of non-bank financial institutions (private credit, factoring, leasing) remains limited and these entities are often subsidiaries of major banks.

The shortage of long-term savings (notably for retirement), despite a national savings rate estimated at 30% of GDP by the IMF, and the narrow base of institutional investors (pension funds, insurance companies, foreign investors), combined with a complex tax system, hinder the development of capital markets. However, asset management is progressing (beyond the acquisition of the non-performing loans of banks since 2008), and the development of mutual funds is highlighted by the CBRT (Financial Stability Report, May 2025). They accounted for 10% of the financial system in 2024, against 2.6% in 2021, while their flexible, short-term investment profile is a potential source of volatility and instability. Investment in crypto-assets is strictly regulated, and the use of cryptocurrencies for payments is prohibited.

The continued improvement of the country's macro-financial conditions will be crucial in terms of shoring up investor confidence and market rules for asset pricing (including rates, exchange rates, stocks, gold and real estate) in order to deepen domestic markets and reduce the risk of financial and real estate bubbles.

Graph 19 - A financial system largely dominated by banks



Source: World Bank.

Argentina: Confidence needs to be restored to develop the financial sector

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Since the Milei administration took office, macroeconomic stabilization has been well underway, with achievements in terms of fiscal balance, inflation control, and economic recovery. However, there are still major factors of instability. The results of the mid-term elections of October 2025 have supported the continuation of the ongoing reforms, and the new composition of Congress is expected to strengthen the country's governability. In this context, the financial sector, held back for a long time, should experience a growth path which will require special attention to developments in the quality of credit portfolios and provisioning practices, especially in the non-banking sector. It will take time to deepen the financial sector due to the lack of confidence among economic operators, the legacy of many years of poor economic performance.

Two years have passed since the Milei administration took office and embarked on its radical reform policy. Macroeconomic stabilization is well underway, and the country returned to a path of growth in 2025 after three years of recession. However, the economic balance remains particularly fragile, as shown by the extreme volatility during the recent electoral cycle, which required a massive and rare intervention by the U.S. to avoid another peso crisis.

Economic policy bolstered by mid-term elections

Since December 2023, the Milei administration has implemented a series of drastic macroeconomic adjustment measures. It first carried out a sharp devaluation of the peso (-54%) and has maintained strict fiscal austerity by cutting public spending (-30% in real terms in 2024 compared to 2023). The objective was to secure a primary surplus, at the minimum covering debt interest payments. This strategy has made it possible to end the monetary financing of the fiscal deficit by the Central Bank (BCRA), the main source of the country's inflationary spiral. Despite pressure, particularly in the run-up to the mid-term elections, the authorities have scrupulously applied their fiscal agenda month after month.

While the initial devaluation of the peso pushed inflation up to nearly 300% (year-on-year) in April 2024, it subsequently started to rapidly decline: 120% at the end of 2024, less than 50% in April 2025 and 30% at the end of 2025. In addition, the monetary stabilization and fiscal balance helped bring public debt down from 154% of GDP in 2023 to 79% in 2025.

In terms of economic activity, following a sharp contraction of GDP in the first half of 2024 due to rampant inflation and the immediate effects of budget cuts, the recovery was strong starting in the second half of 2024, limiting the economic recession to -1.3% in 2024. The strong momentum at the beginning of 2025 subsequently slowed in the run-up to the elections. Ultimately, 2025 is expected to have ended with growth exceeding 4%. However, not all sectors are on an equal footing. The momentum is driven by export sectors (oil, gas, mining, agriculture), while sectors more oriented toward domestic demand (construction, manufacturing and retail industries) are struggling.

The recovery in economic activity, combined with policies on social welfare benefits targeting the poor, brought the poverty rate back to the pre-pandemic level in the first half of 2025 (32%), erasing the sharp increase seen in the first half of 2024. The overall decline in inequality masks sharp disparities between informal sector workers, whose real income has increased, as opposed to workers in the formal private sector, and even more so in the public sector. Furthermore, as a result of the cuts in civil service staff and business failures in the formal private sector, there has also been a shift of workers toward the informal sector. At this stage, the decline in poverty (31% of the population lives below the poverty line) is nonetheless accompanied by a form of impoverishment of the population.

The most critical point in macro-financial stabilization concerns monetary policy and the management of external reserves. Chronic instability since the 2001–2002 crisis has been self-perpetuating due to a lack of confidence in the peso, strong demand for the dollar outside the financial system, and a high level of Argentine private savings held abroad. Combined with a trade balance highly dependent on changes in commodity prices, this has resulted in a clearly insufficient level of foreign exchange reserves, at 25% of the adequate level at the end of 2024 according to the IMF.

In April 2025, Argentina concluded a new financial program with the IMF ($20 billion), combined with a change in the exchange rate regime (flexibilization) and a gradual easing of capital controls. The implementation of the program was considered satisfactory, but required an exemption regarding the rate of accumulation of external reserves (July 2025 Review).

In a context of insufficient reserves, the tensions between the government and Congress, a corruption scandal, and the defeat in the Greater Buenos Aires provincial elections exacerbated financial volatility ahead of the mid-term elections. Increased demand for the dollar caused the peso exchange rate to spiral beyond the fluctuation band and brought the sovereign spread up to 1,500 bp. Various devices were used to stimulate the supply of dollars and, ultimately, it was the intervention of the Trump administration (purchase of pesos for over $2 billion, announcement of a $20 billion USD/ARS swap line) that stabilized the situation.

The result of the mid-term elections, which was very favorable to the Milei administration, has reinforced this stabilization and offers a window of opportunity to initiate certain key reforms concerning labor, taxation, and pensions. A challenge will also be to have a more proactive policy for the accumulation of external reserves, with potential implications for the exchange rate.

The need to develop a crippled financial sector

The low level of development of the Argentine financial sector, relative to the level of per capita wealth, is the result of multiple historical factors that have generated deep-seated mistrust among savers, including the 2001 debt crisis, a new financial crisis in 2008, financial repression to prioritize government financing, and taxes on financial transactions.

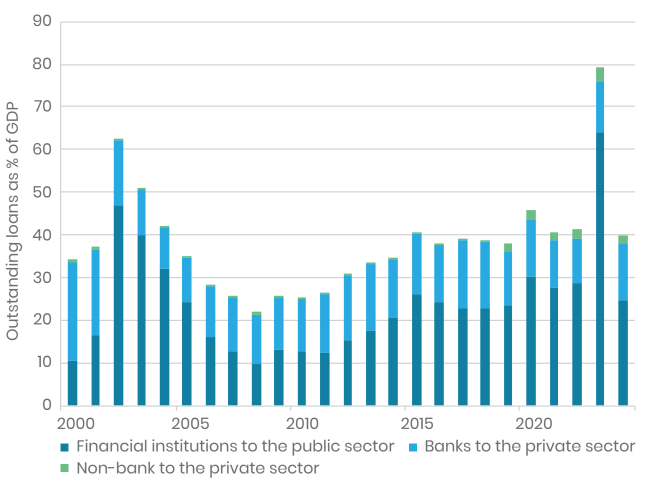
In 2023, the financial intermediation sector accounted for only 1.6% of GDP and employed fewer than 150,000 people (2% of the working population). At around 15% of GDP, credit to the private sector, from both banking and non-banking, is four times lower than the average of peer countries in Latin America.

The banking sector is both highly concentrated (six banks account for two-thirds of assets) and fragmented (with nearly 80 banks). Sources and uses remain very short-term and, until recently, public sector financing greatly limited private sector lending. After five years of decline (2020-2024), credit finally restarted in real terms at the end of 2024, and the sector anticipates continued growth (+30% in real terms for 2026).

The banking sector coexists with 13 non-bank financial institutions (financial corporations), two-thirds of which are foreign-owned. Their outstanding loans ($2.5 billion in September 2025) account for less than 3% of banking sector loans. The activity of these institutions is growing faster than the traditional banking sector, but they face poorer credit quality (4%, against 2% in March 2025), and a less well-provisioned portfolio (100%, against 150%). Given their limited weight, they do not pose a systemic risk.

The BCRA also conducts oversight on non-financial credit providers (NFCPs), financial trusts funds, and peer-to-peer (P2P) lending platforms. This segment comprised over 500 institutions in March 2025, including nearly 70 particularly active fintechs. The financing portfolio of these institutions was equivalent to nearly $7 billion (at the parallel exchange rate) in January 2025, an amount significantly higher than that of non-bank financial institutions. This segment is showing strong momentum in a context where 40% of national employment is informal. The levels of irregularity need to be monitored, as they remain higher than those of the financial system (8.6% in January 2025 for non-financial credit providers).

Graph 20 - Public sector financing significantly constrains private sector access to credit



Source: World Bank, AFD calculations.

Ecuador: Can credit cooperatives support economic recovery?

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Ecuador's macroeconomic situation has shown signs of stabilization since the end of 2024. Following the 2% recession recorded in 2024, economic growth reached 3.8% in the first half of 2025, alongside relatively robust investment. The traditional banking sector is constrained by the specificities of dollarization and the regulatory environment, which limits its capacity to finance the private sector. Conversely, credit cooperatives have developed rapidly over the last 15 years. They show a real complementarity with the banking sector, particularly in supporting the productive base of small businesses that can serve as growth drivers. However, credit cooperatives have vulnerabilities that require measures to safeguard the stability of the sector and its financing capacity.

Over the last ten years, the Ecuadorian economic model has experienced numerous shocks and crises: fall in oil prices in 2015–2016, recurrent periods of political uncertainty between 2017 and 2024, a sovereign default in 2020, a rise in insecurity and organized crime throughout the period and a succession of exogenous shocks (earthquake in 2016, pandemic in 2020, extreme climate events). Following the last recession, which saw GDP contract by 2% in 2024, economic growth stood at 3.8% year-on-year (yoy) in the first half of 2025 and is expected to reach 3.5% over the year. The domestic financial sector is key to supporting economic recovery by sustaining consumption, but also and especially investment, with a view to diversifying the productive model.

An encouraging economic recovery, but uncertain growth drivers

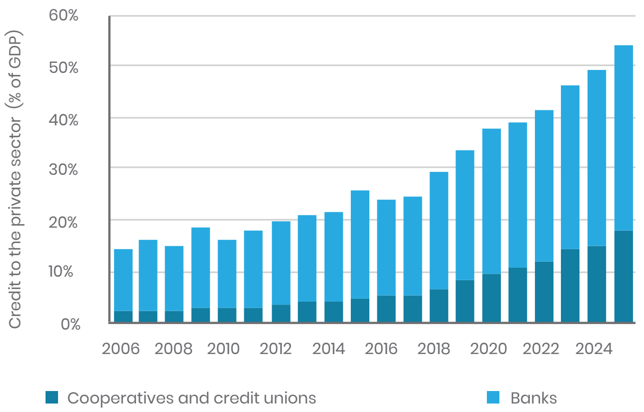
The economic rebound since the beginning of 2025 is based on several factors: political stabilization following the general elections, fiscal discipline (deficit contained at 1.2% of GDP), renewed support from donors ($5 billion in expected budget disbursements over the year), strong performance of non-oil exports (+13%) and a significant increase in remittances from expatriate workers ($6 billion in 2025, or 4.6% of GDP). A sign of this more favorable environment, investment rebounded during the first six months of 2025 (+7% yoy), reflecting the restored confidence of economic agents and dynamism in certain sectors (agriculture, manufacturing of agri-food goods for export, services). At the same time, donor financing, exports of goods, and migrant remittances are increasing domestic liquidity, which translated into an acceleration in the growth of bank deposits since the end of 2024.

While the conditions look favorable in terms of supporting economic activity in the coming quarters, there are persistent difficulties. In addition to uncertainty over the ability of the public sector to fully refinance its debt in 2026 and a business environment that remains deteriorated, the traditional banking sector faces constraints in supporting private sector financing. Indeed, it is subject to the constraints of the Ecuadorian economic and regulatory environment: dollarization leads to high liquidity requirements and tighter risk risk management (which accounts for the robustness of the sector), resulting in great caution among banks. Furthermore, banking regulations (rate caps by segment, activity sector and type of client, financial repression on government securities) create market distortions that especially exclude more informal and smaller clients, yet they are potential drivers of inclusive and diversified growth. Finally, the persistent uncertainty inherited from ten years of shocks also results in a timid recovery in lending activity. Despite the increase in deposits since the beginning of 2025, the volume of private sector loans allocated by banks increased by only 10% yoy in October (compared to 17% for deposits). While this decoupling strengthens the liquidity position of banks, it limits the potential growth of the economy.

Credit cooperatives, an essential but fragile vehicle for financing the economy

The constitutional revision in 2008 officially recognized and formalized the role of the Popular and Solidarity Economy (EPS) in the organization of Ecuadorian society, with credit cooperatives and mutualists serving as its financial vehicle. These institutions have thus experienced rapid growth over the last 15 years, making them essential to the financing of the economy. Their loan portfolio (which increased from $2 billion at the end of 2010 to $20 billion in mid-2025) accounted for just under 15% of credit to the private sector in the early 2010s, against nearly 30% in 2025. Their consolidated assets now account for 24% of GDP.

Graph 21 - Growing weight of credit cooperatives in the financing of the economy



Source: ECB, Asobanca, IMF, AFD calculations.

The development of credit cooperatives has made it possible to serve a segment of credit demand where traditional banks were not very active. They have thus positioned themselves in consumer credit (52% of their loan portfolio, against 40% for banks) and microcredit (38% for credit cooperatives, against 7% for banks). This has contributed to increasing financial inclusion, which rose from 37% in the early 2010s to nearly 65% at the end of 2024, and to economic development and poverty reduction. Furthermore, they have remained relatively active during economic crises, in particular when bank lending contracted in 2009, 2016 and 2020.

However, the increasing importance of the nearly 400 existing credit cooperatives calls for attention in several respects. Firstly, because they remain structurally more fragile than traditional banks: they are less profitable (return on equity of 4.3%, against 10.7% for banks in 2025) and have a high non-performing loan ratio (8.2% of gross loans, against 4.3% for banks), along with a lower, albeit comfortable, provisioning ratio (101%, against 188% for banks). Secondly, because credit cooperatives operate under a differentiated supervision and regulation regime, whereas the largest among them have activities and balance sheets akin to those of Tier 1 banks: eight credit cooperatives have assets equivalent to $750 million or more and the largest has a balance sheet of $3.7 billion, making it the 7th largest financial institution in the country. This increases the systemic risk, as shown by the liquidation of CREA ($250 million balance sheet) in the summer of 2025, despite being among the institutions subject to enhanced supervision. Finally, the activity of credit cooperatives has slowed since the beginning of 2024, with a credit growth rate well below the averages observed over the last 15 years. This may be indicative of the operational and financial limits of these institutions, and their exposure to local economic conditions (climate conditions for the agriculture sector and insecurity for trade in particular). The legislative and regulatory reforms implemented by the authorities in 2024-2025 on the harmonization and strengthening of supervision, sector governance, AML/CFT requirements and resolution mechanisms should strengthen the regulatory framework of the sector so that it can continue to support the economic development of Ecuador.

List of acronyms and abbreviations

AGOA	African Growth and Opportunity Act
AI	Artificial intelligence
AML-CFT	Anti-money laundering and combating the financing of terrorism
BIS	Bank for International Settlements
BP	basis point
CAR	Capital Adequacy Ratio
CPEC	China-Pakistan Economic Corridor
EDCs	Emerging and developing countries
EIU	Economist Intelligence Unit
FATF	Financial Action Task Force
FSB	Financial Stability Board
G20	Group of Twenty, an intergovernmental forum comprising 19 of the most developed countries, plus the European Union and the African Union
GDP	Gross domestic product
GEPF	Government Employees Pension Fund
IMF	International Monetary Fund
IRA	Inflation Reduction Act
KSh	Kenyan shilling
LIC	Low-income country
LMIC	Lower-middle-income country
Mb/d	Million barrels per day
NAFTA	North American Free Trade Agreement
NBFIs	Non-bank financial institutions
NPLNC	Non-performing loans net of provisions to capital
NPLs	Non-performing loans
OECD	Organisation for Economic Co-operation and Development
OPEC	Organization of the Petroleum Exporting Countries
Pp	percentage point
ROA	Return on assets
SACCOs	Savings and Credit Co-operatives
UMIC	Upper-middle-income country
UNCTAD	United Nations Conference on Trade and Development
USAID	U.S. Agency for International Development
USD	United States dollar
WEO	World Economic Outlook
yoy	year-on-year

List of figures and tables

ISO-3 code	Country	ISO-3 code	Country	ISO-3 code	Country
AFG	Afghanistan	**GNB**	Guinea-Bissau	**PAK**	Pakistan
AGO	Angola	**GNQ**	Equatorial Guinea	**PAN**	Panama
ALB	Albania	**GRD**	Granada	**PER**	Peru
ARG	Argentina	**GTM**	Guatemala	**PHL**	Philippines
ARM	Armenia	**GUY**	Guyana	**PLW**	Palau
ATG	Antigua and Barbuda	**HND**	Honduras	**PNG**	Papua New Guinea
AZE	Azerbaijan	**HTI**	Haiti	**PRY**	Paraguay
BDI	Burundi	**IDN**	Indonesia	**PSE**	Palestine
BEN	Benin	**IND**	India	**RWA**	Rwanda
BFA	Burkina Faso	**IRN**	Iran	**SDN**	Sudan
BGD	Bangladesh	**IRQ**	Iraq	**SEN**	Senegal
BHS	Bahamas	**JAM**	Jamaica	**SGP**	Singapore
BIH	Bosnia	**JOR**	Jordan	**SLB**	Solomon Islands
BLR	Belarus	**KAZ**	Kazakhstan	**SLE**	Sierra Leone
BLZ	Belize	**KEN**	Kenya	**SLV**	El Salvador
BOL	Bolivia	**KGZ**	Kyrgyzstan	**SOM**	Somalia
BRA	Brazil	**KHM**	Cambodia	**SRB**	Serbia
BRB	Barbados	**KIR**	Kiribati	**SSD**	South Sudan
BTN	Bhutan	**KSV**	Kosovo	**STP**	Sao Tomé and Principe
BWA	Botswana	**LAO**	Laos	**SUR**	Suriname
CAF	Central African Republic	**LBN**	Lebanon	**SWZ**	Eswatini
CHN	Chile	**LBR**	Liberia	**SYC**	Seychelles
CHN	China	**LBY**	Libya	**SYR**	Syria
CIV	Côte d'Ivoire	**LCA**	Saint Lucia	**TCD**	Chad
CMR	Cameroon	**LKA**	Sri Lanka	**TGO**	Togo
COD	Democratic Republic of the Congo	**LSO**	Lesotho	**THA**	Thailand
COG	Congo	**MAR**	Morocco	**TJK**	Tajikistan
COK	Cook Islands	**MDA**	Moldova	**TLS**	Timor-Leste
COL	Colombia	**MDG**	Madagascar	**TON**	Tonga
COM	Comoros	**MDV**	Maldives	**TTO**	Trinidad and Tobago
CPV	Cape Verde	**MEX**	Mexico	**TUN**	Tunisia
CRI	Costa Rica	**MHL**	Marshall Islands	**TUR**	Türkiye
CUW	Cuba	**MKD**	North Macedonia	**TUV**	Tuvalu
DJI	Djibouti	**MLI**	Mali	**TZA**	Tanzania
DMA	Dominica	**MMR**	Myanmar	**UGA**	Uganda
DOM	Dominican Republic	**MNE**	Montenegro	**UKR**	Ukraine
DZA	Algeria	**MNG**	Mongolia	**URY**	Uruguay
ECU	Ecuador	**MOZ**	Mozambique	**UZB**	Uzbekistan
EGY	Egypt	**MRT**	Mauritania	**VCT**	Saint Vincent and the Grenadines
ERI	Eritrea	**MUS**	Mauritius	**VEN**	Venezuela
ETH	Ethiopia	**MWI**	Malawi	**VNM**	Vietnam
FJI	Fiji	**MYS**	Malaysia	**VUT**	Vanuatu
FSM	Micronesia	**NAM**	Namibia	**WSM**	Samoa
GAB	Gabon	**NER**	Niger	**YEM**	Yemen
GEO	Georgia	**NGA**	Nigeria	**ZAF**	South Africa
GHA	Ghana	**NIC**	Nicaragua	**ZMB**	Zambia
GIN	Guinea	**NPL**	Nepal	**ZWE**	Zimbabwe
GMB	Gambia	**NRU**	Nauru		

MacroDev - Semestrial Panorama

Semestrial Panoramas are special issues of the MacroDev series written by analysts from the Agence Française de Développement (AFD, French Development Agency). They present a synthesis of macroeconomic and socioeconomic analyses of emerging and developing countries (EDCs). A thematic section accompanies the country focus and sheds light on the economic and structural issues of developing countries.

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Date completed: 15/01/2026

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