



## **CHAPTER 2**

# **Capital Flows to Emerging Markets: The Role of Global Non-Bank Investors**

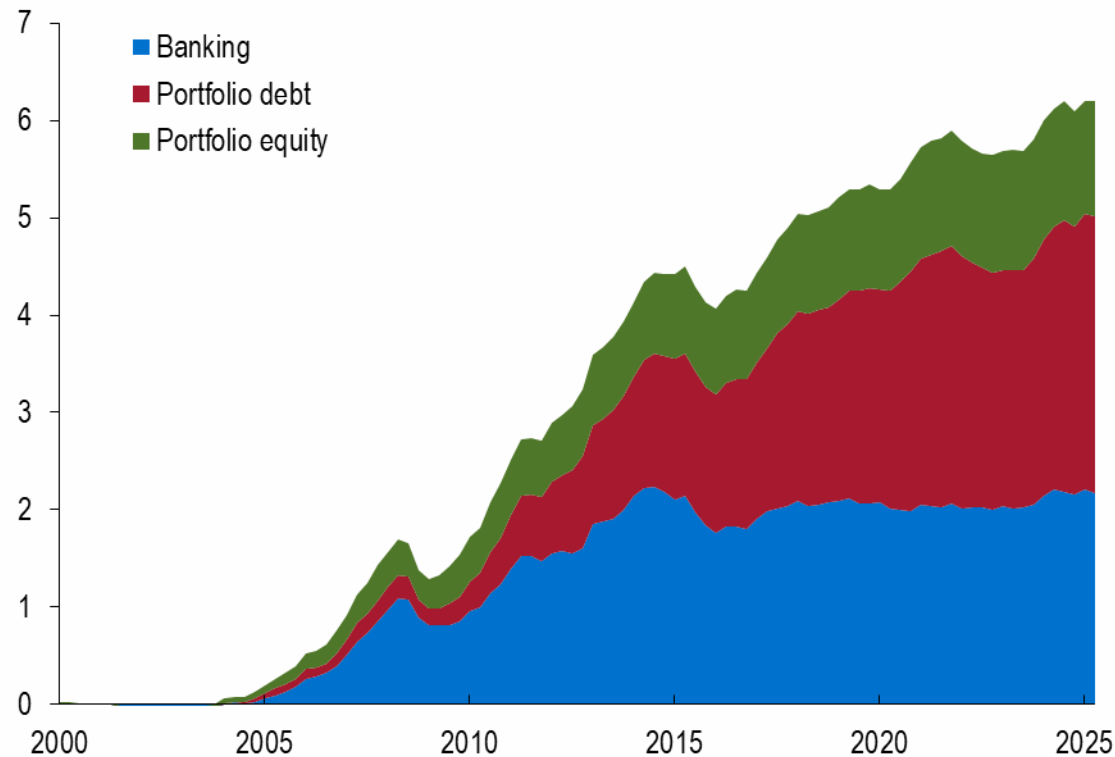
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# **GLOBAL FINANCIAL STABILITY REPORT**

# Emerging markets are increasingly relying on nonbank sources of financing

## Portfolio flows to EMs have surged since the global financial crisis, led by debt ...

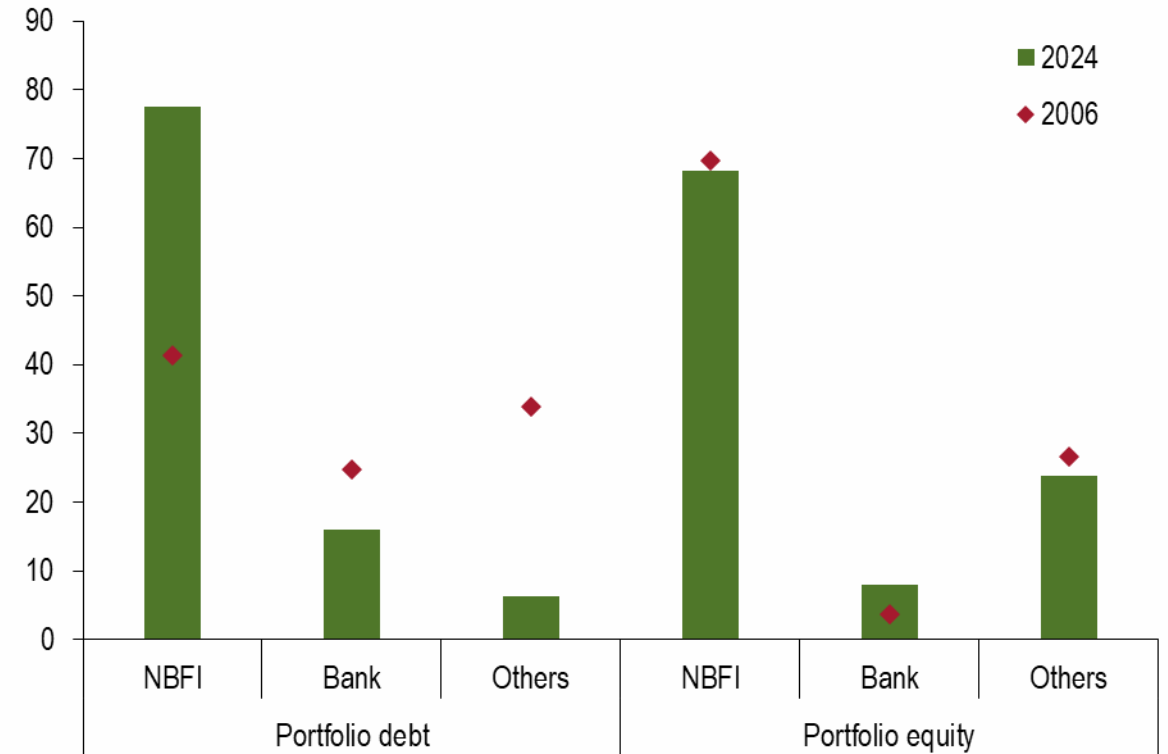
Cumulative nonresident portfolio and banking flows to EMs (trillion of US dollars)



Sources: Bank for International Settlements; IMF, Balance of Payments Statistics; IMF, Portfolio Investment Positions by Counterpart Economy database; and IMF staff calculations.

## ... and largely intermediated by global non-bank financial investors

Share of nonresident NBFI sector in portfolio debt and equity investment in EMs (percent)



Sources: IMF, Portfolio Investment Positions by Counterpart Economy database; and IMF staff calculations.

# Non-bank flows bring substantial benefits but can also create challenges

## ➤ Nonbank flows enhance access to capital and support market development but...

### Nonbank financial investors are highly sensitive to global risk conditions ...

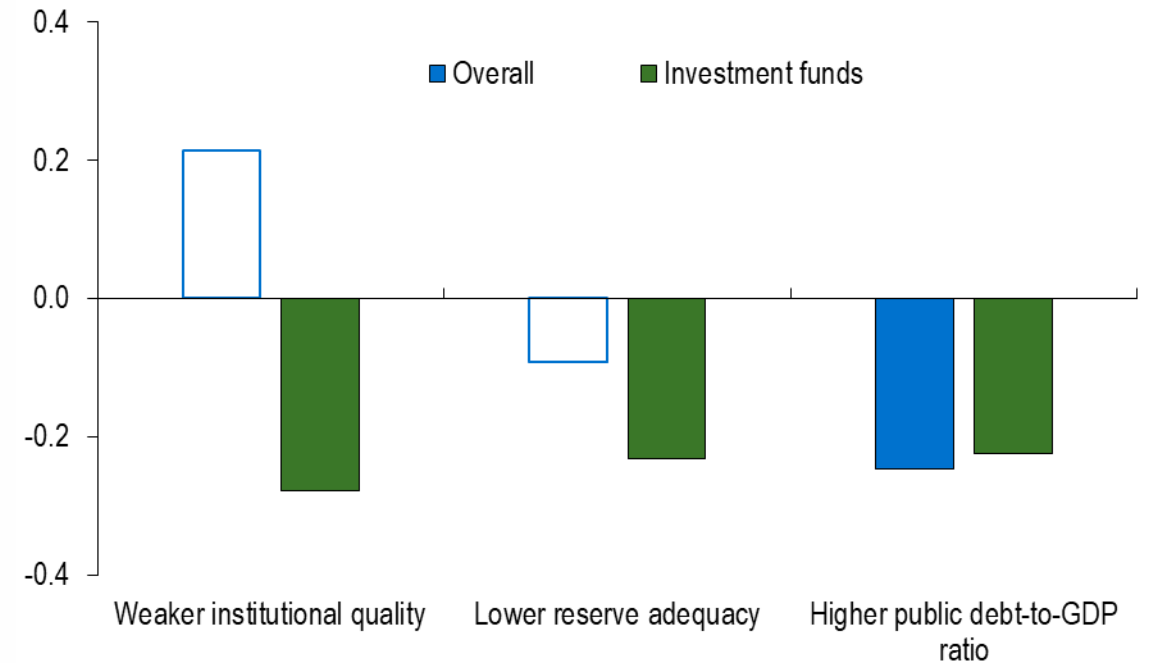
Portfolio liability flows to EMs relative to GDP following an increase in the VIX (standard deviations)



Sources: Bank for International Settlements; IMF, Balance of Payments Statistics; IMF, World Economic Outlook database; and IMF staff calculations. Notes: Solid bars indicate that the reported effect is statistically significant at 10 percent.

### ... and retrench more strongly from countries with preexisting vulnerabilities

Portfolio debt liability flows to EMs relative to GDP following an increase in the VIX (standard deviations)

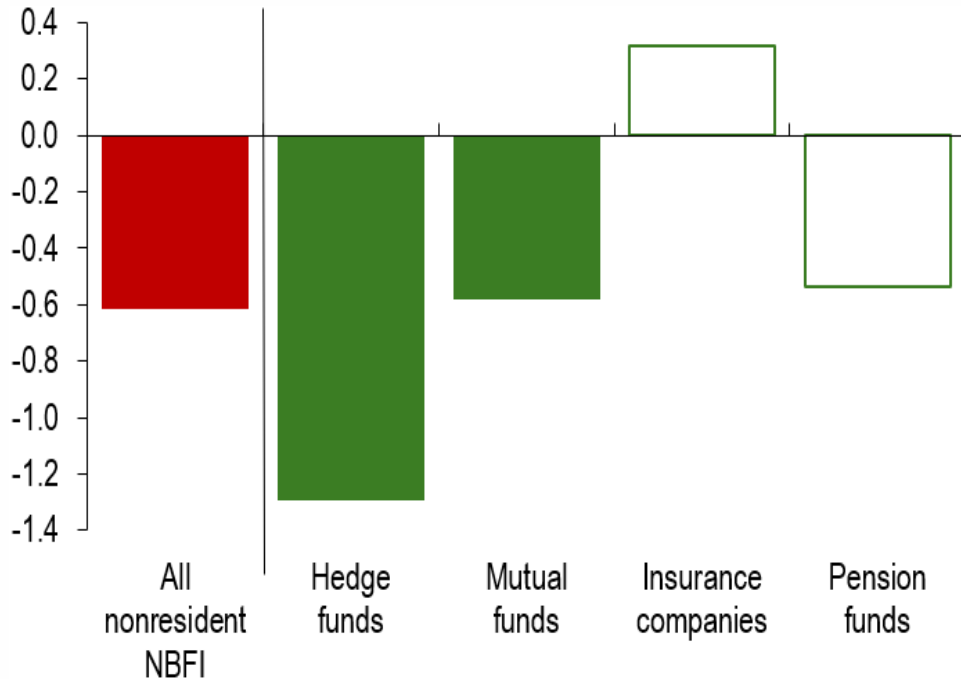


Sources: Emerging Portfolio Fund Research; IMF, Balance of Payments Statistics; IMF, World Economic Outlook database; and IMF staff calculations. Notes: Solid bars indicate that the reported effect is statistically significant at 10 percent.

# Sensitivity to global risk varies across types of non-bank financial investors

## Hedge funds and mutual funds are most sensitive to global risk ...

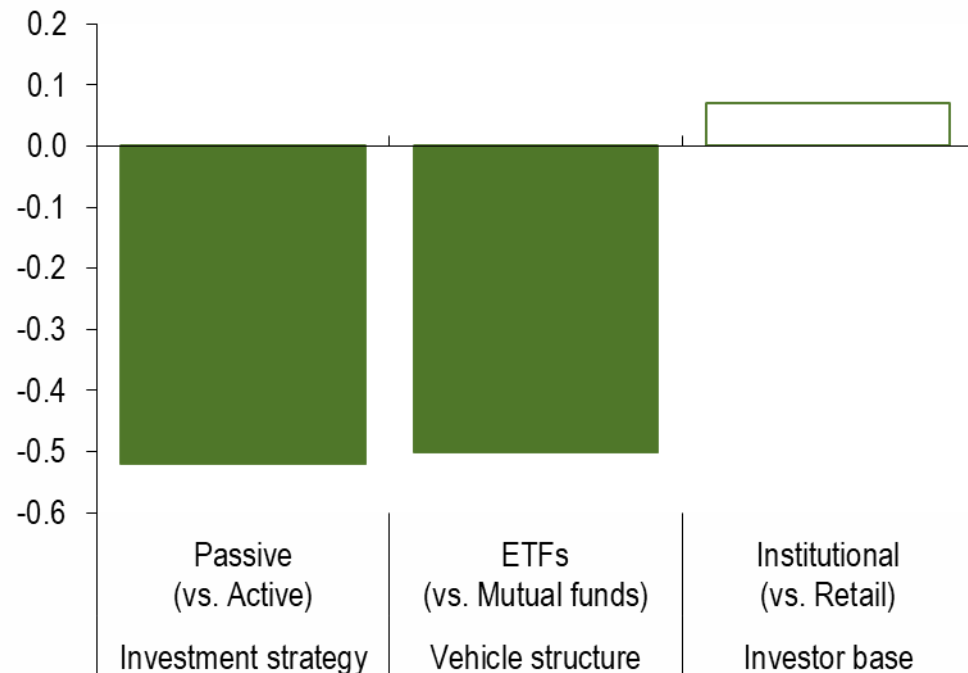
Change in nonresident investments after an increase in the VIX (percentage points, relative to initial holdings)



Sources: Chicago Board Options Exchange; FactSet; Lipper; and IMF staff calculations. Notes: The reported effects are valuation-adjusted, expressed relative to initial holdings, and benchmarked against residents. Solid bars indicate that the estimated effect is statistically significant at 10 percent.

## ... and among mutual funds, passive funds and ETFs are especially sensitive

Change in nonresident investments after an increase in the VIX (percentage points, relative to initial holdings)

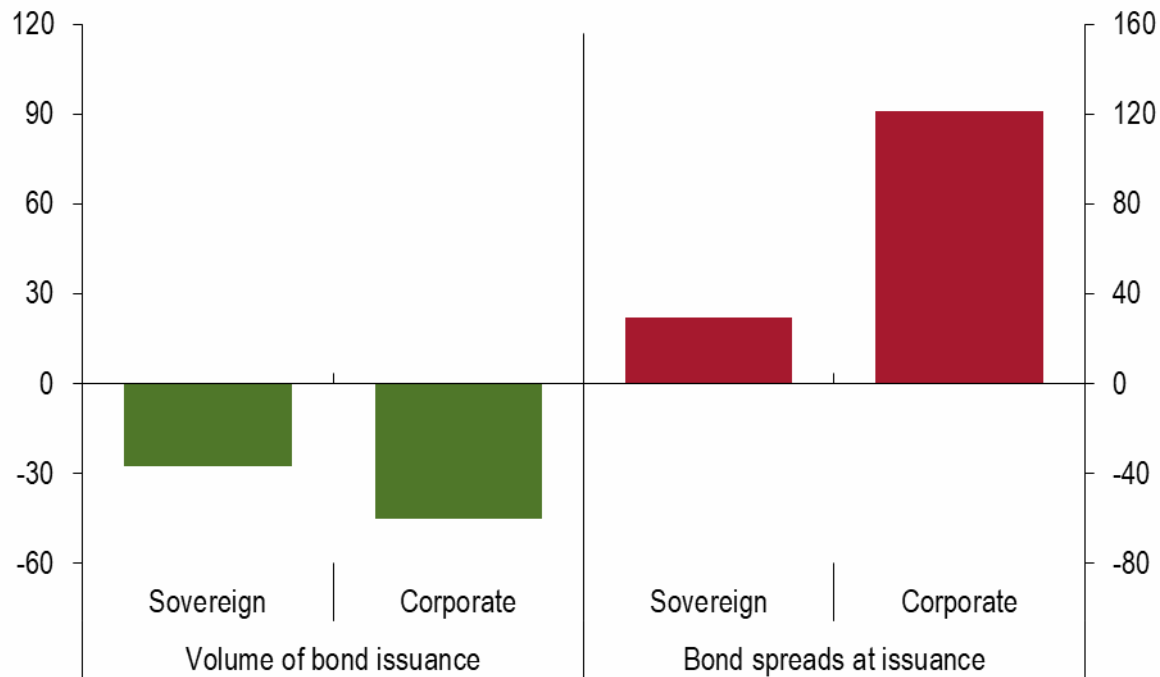


Sources: Chicago Board Options Exchange; FactSet; Lipper; and IMF staff calculations. Notes: The reported effects are valuation-adjusted, expressed relative to initial holdings, and benchmarked against residents. Solid bars indicate that the estimated effect is statistically significant at 10 percent.

# Exposure to risk-sensitive investors could lead to greater macro-financial stress

## Stress episodes trigger weaker bond issuance, higher spreads ...

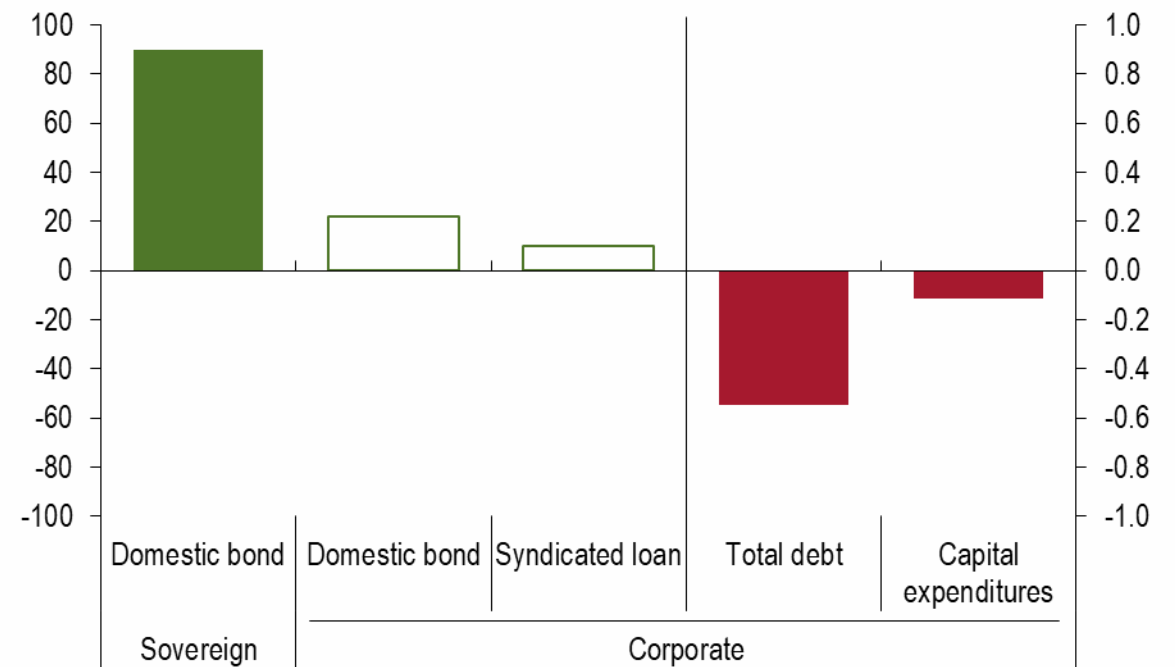
Bond issuance volume and spreads for issuers with higher reliance on flighty investors  
(percentage points, left scale; basis points, right scale)



Sources: Dealogic; FactSet; Federal Reserve Economic Database (FRED); London Stock Exchange Group; WorldScope; and IMF staff calculations. Notes: Solid bars indicate that the reported effect is statistically significant at 10 percent.

## ... and weaker investment for EM issuers exposed more to 'flighty' investors

Volume of alternative funding for issuers with higher reliance on flighty investors  
(percentage points, left scale; percent, right scale)



Sources: Dealogic; FactSet; Federal Reserve Economic Database (FRED); London Stock Exchange Group; WorldScope; and IMF staff calculations. Notes: Solid bars indicate that the reported effect is statistically significant at 10 percent.

# POLICY IMPLICATIONS

- **Strengthen resilience to mitigate risks from capital flow volatility by**
  - improving macroeconomic fundamentals and institutional quality
  - pursuing risk management in line with the IMF's Integrated Policy Framework
- **Use systemwide stress tests to gauge resilience**
  - and ensure adequate capital and liquidity buffers at financial institutions
- **Continue deepening domestic bond markets**
  - and broadening the domestic investor base (Oct '25 GFSR)

- **Foster international cooperation**
  - to close regulatory gaps and limit the cross-border propagation of shocks
- **Improve regulatory reporting and international data sharing on**
  - nonbank exposures and vulnerabilities to strengthen surveillance and risk management

# GLOBAL FINANCIAL STABILITY REPORT



## Chapter 2 at a Glance

- Cross-border portfolio flows to emerging markets have risen sharply since the global financial crisis, driven largely by nonbank financial investors, with cumulative inflows approaching \$4 trillion in 2025.
- By supporting market development and expanding financing options, cross-border portfolio flows offer important opportunities but also carry risks, such as heightened sensitivity to shifts in global risk sentiment.
- Sensitivity to global risk varies significantly across the types of investors. Hedge funds and investment funds react more strongly to shifts in global risk than other nonbanks, with passive mutual funds and exchange-traded funds showing the greatest sensitivity within the investment fund sector.
- During periods of global market stress, emerging markets that are more exposed to risk-sensitive investors face tighter financial conditions—including reduced debt issuance and wider spreads—with adverse implications for macrofinancial stability.
- Robust policy frameworks can mitigate the impact of adverse shocks. Nonbank financial investors pull back less from countries with stronger institutions, ample reserve buffers, or lower fiscal risks when global risk increases.
- Cross-border private credit and stablecoin flows into emerging markets are expanding rapidly, creating opportunities but also challenges. Stablecoin flows remain closely tied to crypto market dynamics, although demand is often elevated in countries with weak fundamentals and policy frameworks, raising currency substitution concerns.

## Policy Implications

- To reduce volatility in cross-border portfolio flows, countries—especially those reliant on more risk-sensitive investors—should strengthen macroeconomic fundamentals and institutional quality, build robust fiscal and external buffers, and pursue proactive risk management consistent with the IMF's Integrated Policy Framework.
- International cooperation is essential to close regulatory gaps in nonbank financial intermediation and limit the cross-border propagation and amplification of global financial shocks.
- More comprehensive disclosure and enhanced international data sharing on nonbank exposures and vulnerabilities could strengthen market surveillance and improve risk management practices.
- The rapid expansion of private credit markets and stablecoins in emerging markets warrants continued, proportionate monitoring, particularly where interlinkages with regulated financial institutions are material.

## Introduction

Cross-border capital flows from the nonbank financial intermediation (NBF1) sector are an important source of funding for emerging markets. Since the

global financial crisis, nonresident portfolio flows to emerging markets—particularly investments in debt securities—have grown markedly compared with bank flows, constituting a key source of external financing for these countries (Figure 2.1, panels 1 and 2).<sup>1</sup> The

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<sup>1</sup>According to the IMF *Integrated Balance of Payments and International Investment Position Manual*, seventh edition (BPM7) portfolio investment is defined as cross-border flows and positions involving debt or equity securities, other than those included in direct investment or reserve assets. The flows discussed here refer to net incurrence of liabilities in the financial account under BPM7.