



Non-Bank Financial Intermediaries and Financial Stability: lessons for Emerging and Developing Economies

MEBARKI Imene Nour El Houda ^{1*},

¹ University of Oran 2, Laboratory of: New trends and challenges in development policies in Algeria (Algeria), mebarki.imene@univ-oran2.dz

Received: 01/11/2025

Accepted: 08/12/2025

Published: 28/12/2025

Abstract:

This study aims to emphasize both the importance of non-bank financial intermediaries in the operation of the global financial system and the necessity to evaluate and mitigate the vulnerabilities of this sector in a fragmented environment (customs tariffs, capital flight, and systemic risk).

While contemporary risks and challenges to financial stability differ significantly from historical ones, certain risks lack historical precedent, and their interactions remain uncertain.

Our research attempt to assess the implications of certain risks and challenges on the operation of financial markets, especially in emerging and developing economies. Furthermore, it indicates that regulatory bodies and economic actors are unable to predict which risks will manifest or the timing of their occurrence; however, they may enhance their vigilance for any eventualities to ensure global financial stability.

Keywords: Financial markets, Non-bank financial intermediaries, Challenges, Risks, Liquidity.

JEL Classification Codes : G15, G23, G32

1-Introduction:

At the end of 2022, the Financial Stability Board (FSB) had raised concerns about high levels of debt and the interconnectedness between banks and non-bank financial intermediaries (NBFIs), as inflation was high and growth prospects were deteriorating. In such a context, financial stability could not be taken for granted. Since then, although inflation has somewhat eased, there is still some uncertainty about its persistence. As investors prepare for a soft landing, hoping to avoid serious challenges in refinancing their maturing debts, delays in disinflation and negative surprises in the future trajectory of monetary policy have led to caution and a sudden reconsideration of investor's objectives. To this, geopolitical tensions and uncertainty in the economic environment are added.

However, whatever the state of this economic environment, unpredictable or not, the world is far from being worried: surprises can happen. On the other hand, what is more likely is that shocks in the markets could spread. Thus, market volatility could produce vulnerabilities (Sydow, et al., 2021) among some heavily indebted non-bank investors facing liquidity imbalances.

Since the global financial crisis of 2008, banking turmoil has been a recurring source of financial stress on the international financial system. The bank failures largely had distinct causes but produced a broader crisis of confidence in the resilience of banks, banking systems, and financial markets in several countries.

In general, the FSB's review of the lessons learned from bank failures confirmed the robustness of the international framework for resolving these issues. On the other hand, one of the areas of implementation of this framework that deserves special attention is that of NBFIs. Indeed, these NBFIs are of increasing importance in financing the real economy; including capital flows to Emerging Markets and Developing Economies (EMDEs); which underscores the need to effectively assess and address the vulnerabilities of this sector. Relying on the fact that these countries are the most exposed to the global dynamics of financial markets, because of their dependence on international financing, the volatility of international capital flows, and their vulnerability to contagion effects during periods of global financial stress, our work primarily aims to analyze the risks associated with IFNB and their impact on financial stability, particularly EMDEs. It particularly aims to:

- i. Evaluate the vulnerabilities of NBFI and their role in international capital flows to these countries, which allows for a better understanding of the interactions between tariff policies, NBFI, and financial fragilities.

- ii. Anticipate the challenges for global financial stability and emerging markets, particularly in the face of external shocks or financial contagion, and propose strategies for enhancing the resilience of these countries' financial systems against global risks. In this sense, it highlights the vulnerabilities of these countries in the face of global financial dynamics and suggest mechanisms to improve their financial stability. By better understanding the risks associated with NBFI and capital flows, policymakers in these countries will be better able to anticipate crises and strengthen their financial systems against external shocks.

Ultimately, the objective of our work is not limited to technical analysis. It aims to make a proactive contribution to global financial stability, focusing on a fragile but strategic link in the global financial system: NBFIs.

To shed light on this debate, our work will first examine the global economic context of

EMDEs. In a second step, we will examine NBFIs and capital flows, with a particular focus on the NBFIs ecosystem in Algeria. Then, we will analyze the interactions between tariff policies, non-bank financial intermediation, and financial vulnerabilities. Finally, we will present the cyclical perspectives and emerging challenges for global financial stability, as well as for financial markets in general and in EMDEs.

2. Global economic context of EMDEs and financial vulnerabilities:

EMDEs are facing increasing economic and financial challenges, marked by a total debt reaching \$8.63 trillion in 2022 (World Bank Report, 2024). According to the same report, low-income countries particularly experienced a 12% increase in their external debt that same year, with debt servicing absorbing 16.3% of their income. At the same time, capital flows to these countries collapsed by 54% in 2022 as a result of global monetary contraction. This situation was accompanied by high inflation, rising on average from 4.7% in 2021 to 9.9% in 2022, while economic growth decelerated to 3.7% in 2023, compared to 6.7% in 2021 (Bellefontaine, et al., 2023). Moreover, the growing importance of NBFIs increases systemic risks, their assets now represent 49.1% of the total global financial assets (FSB, 2024), and they finance up to 30% of the total credit in some EMs, such as India or Brazil. These dynamics highlight the vulnerability of developing countries to external shocks and the need to strengthen their financial resilience.

As for the Algerian economy, it presents contrasting indicators in 2023, with public debt maintained at 47.3% of GDP (Ministère des Finances, 2025), while foreign exchange reserves increased from \$62.7 billion in 2019 to \$68.9 billion in 2023. In the same timeframe, external debt service constituted 7.2% of exports, revealing vulnerability to external shocks (Bank of Algeria, 2023). However, inflation accelerated to 9.3% in 2023 compared to 7.2% in 2021 (World Bank, 2025), while economic growth, driven to 3.2% by hydrocarbons, shows the continued dependence on the oil sector. As for the financial system, it remains dominated by public banks that hold 80% of the assets, with the NBFIs sector (leasing, insurance) still modest, accounting for less than 10% of total financing. Faced with these challenges, the authorities, in collaboration with the Financial Stability Board (FSB) and the IMF, have initiated reforms thru the 2024 finance law, strengthening the fight against tax evasion and banking supervision, while gradually aligning the regulatory framework with international standards (Basel III).

As for the risks and challenges for Algeria and the EMDEs, we distinguish their dependence on commodity price fluctuations and restricted access to international financial markets. In this context, DEs issued less sovereign debt in 2023 due to rising interest rates (average cost of 7.5% compared to 4.5% in 2020) (World Bank Report, 2024). As for Algeria, for now, it avoids massive external debt, but it could be affected by a refinancing crisis of public enterprises. It is conceivable that a crisis in NBFIs in developed countries could reduce foreign direct investments in Algeria (in 2023, they reached 1.216 billion dollars (Bank of Algeria, 2023), which threatens its financial stability and increases the risk of contagion. To avoid this situation, monetary authorities can act on factors that limit the vulnerability of the national economy to external shocks (inflation, debt, monetary tightening) and reduce its dependence on NBFIs and volatile capital flows. In parallel, a policy of structural reforms, in several areas, must be implemented, specifically the diversification of the national economy (less dependence on oil), financial regulation, and improved supervision of NBFIs to avoid liquidity crises and attract stable investments (business climate reforms). All these actions help regulate the country's financial system, prepare for global risks, and strengthen the supervision of the non-bank financial sector.

3. NBFIs and capital flows:

NBFIs, referred to as "Shadow banking" or "shadow finance" until 2018, refer to a set of financing and capital collection mechanisms conducted by entities outside the conventional banking system, although their activities may resemble those of traditional banks (Banque de France, 2024). In this way, NBFIs can be considered as an alternative and a complement to conventional banking channels, so contributing to the financing of innovation and the stimulation of growth. According to the report (FSB, 2024), as of the end of 2023, these actors represented 49.1% of global financial assets (Table below). This percentage represents a significant share of transactions and investments in financial markets, therefore enhancing liquidity and portfolio diversification. Although their impact can also be negative in terms of systemic risks and amplification of financial market volatility during disturbances. This is one of the reasons why regulators and supervisory authorities closely monitor the evolution of these actors to limit potential systemic risks and ensure financial stability.

Unlike banks, NBFIs lack the power to create money. They only have a financial intermediary role, which consists of obtaining savings resources in order to grant loans to agents who need financing. In this context, these actors play an essential role in the mobilization and allocation of capital on a global scale through techniques that allow for investing an amount greater than the capital held. All these factors aggravate the condition of the financial market during crises. Consequently, their actions may enhance liquidity but also the volatility of these markets.

Table 01: Composition of the global financial system (excluding Russia)

	Total global financial assets	Central banks	Banks ³	PFI ⁵	NBFI sector
Size at end-2023 (USD trillion)	486.4	37.5	188.7	21.4	238.8
Share of total global financial assets (%)	100.0	7.7	38.8	4.4	49.1
Growth in 2023 (year-over-year, %)	5.2	-3.4	3.3	3.5	8.5
Growth 2017–22 (annualised growth, %)	5.3	7.8	6.2	5.2	4.2

Source: Financial stability Board, 2024: Global Monitoring Report on Non-Bank Financial Intermediation

The reasons why agents resort to NBFIs are related to the existence of certain links between the activities of these actors and the financial markets, specifically:

- NBFIs play a crucial role in financing businesses and projects by raising capital in primary financial markets and allocating it thru various assets in secondary markets.
- The transactions carried out by NBFIs in financial markets can operate as significant indicators for other market participants, thereby influencing the transmission of information on asset prices and investment decisions.
- NBFIs often participate in arbitrage activities and contribute to market efficiency by helping to align asset prices.
- The activities of NBFIs can have a significant impact on the liquidity and volatility of

financial markets, particularly during periods of financial stress or market disruptions.

➤ NBFIs frequently lead in financial innovation by developing new products and investment strategies that influence the dynamics of financial markets.

➤ NBFIs are often interconnected with other actors in the financial system, which can create risks of contagion and rapid propagation of shocks throughout the whole financial system.

On the other hand, NBFIs play an essential role in facilitating transactions in the financial market. Some of these entities, such as securities brokers, private equity funds, asset management companies, and insurance companies, provide a range of specialized financial services that often complement those offered by traditional banks. For example, securities brokers facilitate the buying and selling of equities on global stock markets, while private equity funds invest in companies around the world to generate returns for their investors.

This interconnection between international financial markets and NBFI creates a dynamic but also vulnerable financial ecosystem. Economic shocks in one region can quickly spread across the world, impacting financial markets and non-bank institutions. Moreover, this interconnection can amplify systemic risks, as was the case during the 2008 global financial crisis, when losses incurred by NBFI had devastating repercussions on the entire global financial system.

Ultimately, the link between international financial markets and NBFI is a crucial feature of the contemporary global economy. Although it offers numerous opportunities, it also poses challenges in terms of risk management and regulation to ensure the stability and resilience of the global financial system.

Thus, enhancing the resilience of NBFIs should guarantee a more stable supply of financing to the economy and reduce the need for singular interventions by central banks. To this end, they must contain liquidity imbalances. This means they must identify in advance the sources of high liquidity demand in case of stress, such as the unilateral sale of assets by investment funds or unexpected margin calls. In addition, there is also the monitoring of excessive leverage accumulation, which can amplify negative dynamics.

Consequently, NBFI are now major players in the financial sector and global financial stability could depend on their resilience as monetary policy tightens to combat high inflation. It is therefore particularly important to properly understand and protect this vast segment of the financial sector, which includes a wide range of institutions other than banks.

Since the global financial crisis of 2008, the growth of the NBFI sector has accelerated, and it now accounts for nearly 50% of global financial assets. On the other hand, NBFIs also play a major role in bank financing. According to the ECB report (2023), in the last quarter of 2022, nearly half of the banks' funding came from NBFIs. At the same time, the share of funding for Eurozone banks has fluctuated between 41% and 54% since 2015, with French, German, and Dutch banks as the main beneficiaries. The smooth functioning of non-banking sector operations is therefore essential for financial stability. At the European level, banks' dependence on funding from NBFI (14% of European banks' funding) constitutes a risk enhancing factor because these banks play a central role in the allocation of credit within the economy (ECB, Financial Stability Review, 2023).

Although small compared to deposits from individuals and businesses, financing through deposits from NBFI can be particularly vulnerable to changes in market conditions. About half of all these deposits are held by banks for non-operational purposes, these deposits are not related to clearing or cash management and can be withdrawn freely. They often reflect the liquidity reserves of NBFIs and would generally be the first line of defense to meet buyback and other liquidity needs.

Similarly, they would constitute the main vector for transmitting liquidity shocks from this sector to the banking sector (ECB, Financial Stability Review, 2023). In the event of a liquidity shock affecting NBFIs, massive withdrawals or the hasty sale of assets can lead to capital flight from emerging markets. Which leads to:

- A sharp increase in interest rates;
- A depreciation of local currencies;
- Macroeconomic instability in the concerned countries.

However, the vulnerabilities of NBFIs seem to have increased in recent years following a series of multiple events: the global financial crisis of 2008, the COVID-19 pandemic, a more tense geopolitical environment than ever before, and new customs tariffs. In addition, disruptions affecting NBFIs tend to manifest in a context of high debt levels, for example thru companies resorting to borrowing to finance their investments or increase their returns, or thru the use of financial instruments, such as derivatives. Tensions are also caused by liquidity asymmetries, when an institution is unable to generate sufficient liquidity, either thru assets liquidation, such as bonds or stocks, or thru the use of credit lines to meet redemption requests from investors. Moreover, high levels of interconnection between NBFIs and traditional banks can be a decisive factor in amplifying financial tensions (Sydow, et al., 2021). Consequently, any disturbance in the NBFIs sector can therefore reduce or make more expensive access to international financing for EMDEs.

Due to the close financial relationships that unite the IFBN sector and other sectors, any shock impacting this sector could be transmitted to other sectors. To this end, crisis exercises have highlighted the role of NBFIs in contagion effects (HCSF, 2020). It is therefore crucial to monitor and manage the risks associated with NBFIs to ensure global financial stability. The accomplishment of this task requires appropriate regulation and supervision, as well as clear communication among the several parties. The urgency of these actions is all the more crucial given the increase in the size of this sector, its complexity, and its strong interconnections, which are sources of increased systemic risk.

3.1 NBFIs and financial market stability

Overall, the influence of NBFIs on financial markets is exerted in various ways, specifically:

- As leverage and increased volatility, some of these actors may use high leverage to increase their potential returns. However, this can also increase market volatility, as they may be forced to quickly liquidate positions in the event of unfavorable market movements.

- The investment decisions of large investment funds and private equity firms can amplify market trends. For example, if an investment fund decides to massively sell shares in a particular sector, it can lead to a drop in prices in that sector, affecting the entire market.

- The interconnections between different financial intermediaries and banking institutions can lead to systemic risks by rapidly spreading risks in the event of failure or crisis in the non-banking financial sector. This can potentially destabilize the entire financial system.

- If investors in investment funds or private equity funds decide to make massive withdrawals, they can affect market liquidity, particularly for less liquid assets such as corporate bonds or real estate assets.

- Indeed, NBFIs are often at the forefront of innovation in new financial products, developing new products and investment strategies. This can change market dynamics and create new opportunities, but it can also introduce new risks.

Furthermore, the importance of NBFIs can be illustrated; in addition to the growth of their share in international financial markets; by their increasing importance in the global financial landscape. This concerns their representation in certain regions of the world. As an example, we can mention, more particularly:

➤ North America

- Investment funds are particularly predominant, with assets under management often exceeding trillions of dollars.
- Insurance companies also hold a significant share of financial assets, supporting capital markets.

➤ Europe

- Investment funds and asset management companies are major players in European markets, with financial hubs such as London, Paris, and Frankfurt.
- Insurance companies also play a significant role, particularly in the management of pension funds.

➤ Asia-Pacific

- The growth of NBFIs is rapid, with a notable increase in investment funds, insurance companies, and asset management firms.
- Emerging financial centers like Hong Kong and Singapore that have become major hubs for these players.

➤ Middle East and Africa

- Sovereign wealth funds are important NBFIs in this region, often investing in diverse global assets.
- Insurance companies and investment funds are also present, although to a lesser extent than in other regions.

In order to reduce the vulnerabilities of international financial markets in the future, several challenges in various directions must be addressed:

➤ The strengthening of regulation and supervision, which allows regulatory authorities to establish robust and effective regulations to monitor the activities of international financial markets and NBFI. This includes the implementation of transparency standards, systemic risk monitoring, and compliance controls to prevent abusive behavior and reduce the likelihood of financial crises.

➤ Given the cross-border nature of financial markets, close coordination between regulators and supervisory authorities on a global scale is essential. This would facilitate the exchange of information, improve risk detection, and take coordinated preventive measures to moderate potential crises.

➤ With the rapid evolution of technology and the emergence of new and complex financial products, it is crucial to closely monitor financial innovations and understand their implications on market stability. This requires adaptive and proactive regulation to oversee new forms of financing, such as cryptocurrencies and decentralized finance.

➤ Regulatory authorities must try hard to reduce systemic risks by identifying and mitigating interconnections and interdependencies among market participants. This could involve implementing capital controls, risk exposure limits, and stress tests to assess the resilience of the financial system in stress scenarios.

➤ Financial market actors, including investors, financial institutions, and regulators, must adopt and promote a more prudent and responsible risk culture. This involves rigorous risk assessment, judicious decision-making, and proactive risk management to prevent excessively speculative behaviors and the excessive accumulation of risks.

By addressing these challenges proactively and collaboratively, international financial markets can become more resilient and less vulnerable to economic and financial shocks, thereby contributing to global financial stability.

3.2 Risk management in the NBFi sector

The injection of liquidity by central banks, over decades, to maintain price stability has made the fight against inflation more complex. However, as the COVID-19 health crisis period came to an end, inflation reached high levels, and central banks faced difficult trade-offs between promoting financial stability and ensuring price stability, which threatened the health of the financial system. In such situations, policymakers must have appropriate tools to deal with disturbances in the NBFi sector, which could have negative consequences for financial stability. Rigorous monitoring, regulation, and supervision are essential prerequisites for mitigating these disruptions. In this context, a strengthening of risk management in the private sector must be supported by adequate prudential standards, such as capital and liquidity requirements, as well as more rigorous controls executed with more resources. By limiting the conditions and motivations that promote excessive risk-taking, NBFIs could make more prudent operational decisions. Moreover, central bank intervention to provide liquidity during period of systemic stress should become less necessary and less frequent. If, however, central bank intervention is necessary, it can be carried out in three ways, namely:

- Intervention in the NBFi sector must be discreet and limited to segments that threaten financial stability.
- Intervention must discreetly target systemically important non-bank institutions facing difficulties, with loans being fully secured by collateral, at a higher interest rate, and subject to increased monitoring. A precise schedule should be established to restore the liquidity level of the NBFi and return to market financing.
- The conditions for access to permanent lending facilities should be very strict in order to avoid moral hazard. Such access can only be granted if appropriate regulations and restrictions are established for the different types of NBFIs.

3.3. The Algerian IFNB ecosystem

The desire to modernize the Algerian financial system has resulted in the promulgation of Law No. 23-09 of June 21, 2023, on monetary and banking law. It should be noted, however, that this law is adopted in a context of significant reform of the Algerian financial landscape and aims, in particular, to update the legal framework, institutions, and strategic rules to improve competition among IFNBs, introducing two major innovations:

Creation of new NBFIs

The law introduces a new legal framework for NFIs, such as:

- ✓ Digital banks, which are companies operating exclusively in a digital format and are licensed accordingly.
- ✓ Payment service providers (PSP), joint-stock companies dedicated to payment outside the traditional banking circuit.
- ✓ Independent brokerage intermediaries.
- ✓ Licensed currency exchange offices.

These new actors are subject to approval by the Monetary and Credit Council (MCC). The MCC also assumes the function of integrating the risk center, which is also expanded to include

operators such as microcredit organizations previously outside the supervision of the Bank of Algeria (articles 89-104 and 105-109).

Creation of the Financial Stability Committee (FSC)

The establishment of a FSC, responsible for the macro-prudential supervision of the Algerian financial sector, crisis management, and the preparation of an annual report addressed to the presidency of the republic (articles 161-164). This committee is designed to collaborate with local and international bodies in order to strengthen the resilience of the national financial system. This monitoring mission is thus carried out within an internationally harmonized framework. It should be noted that the detailed modalities of this coordination have not yet been fully published. Indeed, its actions now strengthen the resilience of the national financial system by following international standards of financial governance.

On the other hand, Law No. 23-09 has brought other notable innovations to the banking and financial system in Algeria. To this end, the governance of the Bank of Algeria is strengthened thru the establishment of a mandate for the governor and vice-governors, which translates into greater institutional independence. This law assigned the Bank of Algeria the responsibility of implementing monetary policy instruments adapted particularly to Islamic and green finance, the possible launch of the Digital Algerian Dinar, the legal framework for the dematerialization of exchanges between banks, financial institutions, and PSPs, and the harmonization of certain provisions with the finance law. More generally, thru its presence in the supervisory authorities of the banking and financial system, it participates in the monitoring of the Algerian financial system.

In this regard, Law No. 23-09 constitutes the legal foundation for a modernized framework to integrate NBFIs into regulation, while establishing a FSC responsible for anticipating and managing systemic risks. These measures aim to align the Algerian financial system with the best international standards and strengthen its resilience.

4. Tariff policies, NBFIs, and financial vulnerabilities

The repercussions of policies related to the new customs tariffs recently implemented by the United States are being felt across all financial markets. These effects manifest in the short term by influencing volatility and risk perception, and in the medium to long term thru sectoral restructurings and adjustments in investment strategies (Rodrik, 2018). To understand the current dynamics related to these new tariffs, particularly when they are imposed between major economies and their consequences on financial markets as well as on all stakeholders, including non-bank financial intermediaries, it is necessary to analyze their potential effects at several levels: increased macroeconomic risks, increased volatility in financial markets, and specific risks for listed companies.

4.1 Increased macroeconomic risks

4.1.1 Global economic slowdown

Tariff increases hinder international trade, which means less exchange and a slowdown in global economic growth. The anticipation of these risks by the markets translates into a drop in stock indices and an increase in volatility. Thus, custom duties radically change the rules of the free trade game, making it difficult to predict companies' ability to react to the changing rules and shortening the horizon of their forecasts (Bown, 2022). Thus, the risk of investing in the type of action concerned increases, which translates into a recessionary risk that ultimately leads to a currency war and tensions on stock indices, causing a struggle between financial markets and central banks, which will be pushed to reduce their balance sheets as observed after the 2007

financial crisis. If these tensions persist over time, we will likely witness a transformation of the global economic model.

4.1.2 Imported inflation

Additional duties directly impact the final consumer price, which can lead to an adjustment in demand and influence the performance of exporting companies or those integrated into global supply chains. Thus, customs tariffs make certain imported products more expensive. This can cause inflation in countries dependent on imports. In the past, in some sectors, imported inflation of around 1 to 2% has been mentioned (Evenett, Fritz, & J, 2021), which can prompt central banks to adjust their interest rates, necessarily impacting bonds and currencies. These adjustments then have repercussions on the valuation of bonds and on exchange rates. Thus, all these reactions lead to additional and significant losses in the purchasing power of businesses and households.

4.2 Increased volatility in financial markets

The uncertainties related to trade policies increase volatility and abrupt market reactions in response to the announcement of new tariffs. In this context of uncertainty, demand for safe-haven assets (gold and the currencies of the most stable countries) increases in order to minimize losses from stocks. For example, during periods of turbulence, there is a noticeable influx of capital toward assets considered safe, which has sometimes been accompanied by a 2 to 3% increase in the prices of these assets within a few days, in response to tariff announcements (Fabrizio & Lagrange, 2023).

The losses related to the incertitude of trade policies are caused by the need for investment funds to cope with this volatility and the abruptness of market reactions, especially since these investment funds, unlike banks, do not have access to central bank financing (Evenett, Fritz, & J, 2021).

In this context, NBFIs, often very active in managing alternative portfolios or in trading strategies, find themselves facing liquidity risks and volatility that can complicate the valuation of their assets, forcing them to regularly review their hedging strategies and further diversify their investments across multiple regions or industries to minimize systemic risk (IMF, 2022). Thus, the increase in commercial uncertainty forces these actors to review their stress test scenarios and forecasts, which can influence their investment and portfolio management decisions. As a result, they are encouraged to improve their resilience to external shocks, while also facing increasingly stringent regulations aimed at limiting systemic risk.

4.3 Specific risks for listed companies

Exporting companies or those dependent on global supply chains are experiencing cost increases. This impacts their profit margins and forces them to revise their forecasts, while their stock prices fall (OECD, 2021). In this context, sectors sensitive to international trade (technology, automotive, heavy industry) are more vulnerable in terms of sectoral reallocation and are led to revise their profits downward. At the same time, other sectors (domestic services, local consumption) may be more resilient. Which leads to a redefinition of the competitive environment and pushes investors to adapt their strategy, turning toward sectors estimated less vulnerable to tariff tensions and to a reallocation of investors' portfolios (Handley & Limão, 2017).

According to some analyzes, for companies with strong international supply chains, cost increases resulted in lower competitiveness, potentially could diminish their profit margins and, consequently, a drop in their stock market valuation that could amount to several percentages over

the current year.

In a context marked by persistent trade uncertainty, investors and asset managers face several major challenges. They must adapt their asset allocation strategies to better navigate a volatile economic environment. From this perspective, geographical and sectoral diversification becomes increasingly important, allowing for the limitation of exposure to sectoral shocks (Fabrizio & Lagrange, 2023). Moreover, the search for effective hedging mechanisms against political and monetary risks becomes essential to protect portfolios from unexpected events that could negatively affect financial markets.

In this context, monetary and fiscal policies play an increasingly central role, with central banks frequently being called upon to mitigate the negative effects of tariff wars, notably through interest rate cuts or liquidity injections (Evenett, Fritz, & J, 2021). However, these interventions can alter the perception of risk in the markets, leading to an increasing dependence on accommodative monetary policies.

Historically, tariff increases have coincided with periods of high market volatility. For example, recently, several stock indices like the S&P 500 have experienced daily fluctuations that can exceed 6% during key announcements, and some stocks in directly impacted sectors (technology, automotive, industry) have seen their prices drop by around 10 to 15% on days marked by heightened uncertainty. Generally speaking, tariff policies create an uncertain and unstable environment that affects trade flows, prices, financial markets, and investment decisions, which indirectly but strongly impacts EMDEs due to their vulnerability to external shocks and their high dependence on international trade and investments. Especially since these countries, more exposed and less resilient, are particularly vulnerable to these global shocks, which affect their macroeconomic stability, financial attractiveness, and growth trajectory.

This analysis, even though brief, illustrates how tariff policies can quickly influence both corporate performance and the overall dynamics of financial markets and helps to understand the magnitude of the economic and financial repercussions of trade tensions related to these tariff policies. On the other hand, it provides some elements of the complexity of the interactions between trade policies and financial markets, where each tariff measure has the potential to quickly alter the perception of risk and investor confidence on a global scale.

5. Conjunctural perspectives and new challenges to global financial stability

The emerging challenges that policymakers and financial system actors will face can be divided into two categories: those related to the nature of risks and those related to the vulnerability of the financial system and mechanisms for amplifying systemic risks.

5.1 The nature of risks

The nature of the risks that financial markets are likely to face in the coming years presents a different complexity from that of recent years. Some of these risks could come from the financial system itself, such as the risk of rapid deposit withdrawals in the digital age. Concerns about profitability and poor risk management have long been the cause of deposit withdrawals. For example, Silicon Valley Bank recently lost 30% of its deposit base in a few hours, with another 50% drop expected the next day. In the current system, any bank would struggle to survive such a situation. It was well beyond the provisions required under Basel III and more severe than the fastest withdrawals known during the global financial crisis (GFC). The explanation lies in the interaction between new technologies and a set of balance sheet vulnerabilities different from those that prevailed during the GFC. The herding effects associated to social media present a new

challenge for financial regulators. Although the role of new technologies here should be seen more as an amplification mechanism than as a root cause of vulnerability.

Other risks may come from outside the system (geopolitics, operational risks, excessive customs tariffs, and climate change) for which there is no historical precedent to guide policymakers and financial market players. Recent geopolitical events and the implementation of new tariffs by the USA have prevented economic decision-makers and industry players from focusing on the aspects and modalities that would allow the global economy to emerge from the post-health crisis situation, resulting in geoeconomic fragmentation. Thus, this fragmentation will make the global economy more susceptible to supply shocks. In 2023, the IMF estimated that it could lead to global production losses of up to 7%, or even 12% for some countries. Moreover, a more tense geopolitical environment could also have repercussions on financial stability, particularly regarding cross-border capital allocation, international payment systems, major financial institutions, global financing and commodity markets. Thus, a weakness in international cooperation risks compromising the functioning of the global financial safety net. More generally, the political implications and compromises associated with increased geopolitical risk are challenging and complex. It is important to note the importance of strengthening financial and operational resilience across different dimensions, both at the national and international levels. More precisely, at the international level, mechanisms must be implemented to prevent the global financial safety net from fragmenting into smaller liquidity pools based on geopolitical blocs.

As for climate-related financial risks, they are not just a long-term financial risk or an extreme event, but a current risk. Thus, it is crucial to limit global warming and to do so before it is too late. The effects related to this phenomenon are destabilizing for the financial system, such as rising risk premiums for assets exposed to climate risks and/or insurance problems in covering losses caused by natural disasters.

As for the vulnerabilities of the financial system and mechanisms for amplifying systemic risks, it should be noted that in normal times, some systemic risks do not have systemic importance: massive rapid withdrawals of deposits are undoubtedly a particular case of a broader vulnerability. This means that the risk of contagion takes on a new difficult dimension to manage. Thus, two amplification mechanisms have been strengthened:

- The speed of monetary and information flows can amplify the effects of mimicry.
- The procyclicality in certain parts of the international asset management industry that have experienced strong growth.

Under normal conditions, less friction in monetary and information flows should lead to better economic outcomes. But in times of increased stress the issue is more complex. Continuous access to banking and payment services and globally connected trading platforms increases the possibility that a shock produced somewhere in the financial system will turn into a broader crisis.

In response to the rapid spread of information and misinformation, including that amplified by the media and social media, withdrawals from institutions and markets can now occur at unprecedented speed.

Overall, the recent shock of the Covid-19 pandemic has highlighted significant vulnerability in NBFIs. This shock led to a widespread liquidity shock in bond markets and massive redemption requests from specific investment funds. This suggests that banks could face significant refinancing risk to offset large and abrupt capital outflows to very quickly replace funding obtained from these

funds. This situation creates counterparty and liquidity risks for banks.

Thus, any disruption in the NBFI sector is likely to disproportionately affect large banks, as asset exposures, funding links, and derivative exposures are concentrated in this group. Thus, any disruption in the NBFI sector can have a significant impact on these banks due to their close ties with this sector. In the euro area, the concentration of banks' exposure to NBFI on the lending side is much higher than the concentration of banking assets. In 2023, the top five banks account for about 50% of the total exposure to loans and securities, and the top 13 banks for more than 80% (ECB, Financial Stability Review, 2023). This group of banks includes the eight major banks of the Global Systemically Important Banks in Europe (G-SIBs) of the euro area, as well as several other major banks worldwide.

5.2 The challenges ahead for financial markets

Across the world, financial markets are strongly linked and affected by the same risks. To this end, they must, with a few exceptions, face the same challenges. These challenges particularly concern the following areas:

- Increased regulation and oversight: regulators are seeking to strengthen financial market regulations to better prevent systemic risks and protect investors. This may include measures such as stricter capital requirements, increased monitoring of high-frequency trading activities, and better transaction transparency.

- Cybersecurity: with the increasing digitization of financial transactions, cybersecurity is becoming a major issue. Cyberattacks can compromise the security of investors' data, disrupt market operations, and create systemic risks.

- Increased volatility and economic uncertainty: the rapid fluctuations in exchange rates can create challenges for companies operating internationally, as this can affect their costs and revenues. Moreover, financial markets are increasingly sensitive to geopolitical events, fluctuations in global economic growth, and the monetary policies of central banks in developed economies. Thus, increased volatility can make risk management more complex for investors and significantly impact global financial markets by creating uncertainty and influencing investment decisions.

- Transition to a sustainable economy: the growing awareness of environmental and social issues is leading to an increasing demand for sustainable and responsible investments. Thus, companies that fail to adapt to this new requirement could see their value decrease as regulations become stricter and demand for polluting products declines. Moreover, these companies could be held liable for damages caused by their greenhouse gas emissions, which could lead to costly litigation and significant financial penalties and affect their market valuation and access to capital. Alongside this, financial markets must adapt to this transition toward a greener and more ethical economy. On the other hand, climate change-related risks, such as natural disasters and stricter environmental regulations, can impact global financial markets, particularly in environmentally sensitive industries like energy and insurance. To the extent that natural disasters can damage physical assets, they lead to financial losses for businesses, insurers, and investors. Similarly, policies aimed at reducing carbon emissions and promoting renewable energy can lead to a devaluation of fossil fuel-related assets, such as oil and gas reserves, which can impact financial markets. In general, climate change presents a series of challenges and opportunities for international financial markets, and it is increasingly important for investors and businesses to understand and manage these risks proactively.

- Technological innovation: technological advances such as artificial intelligence,

blockchain, and FinTech's are rapidly transforming financial markets. Traditional players must adapt to these changes to remain competitive and address the challenges related to regulation and security.

In summary, financial markets face a series of complex challenges that require a coordinated response from regulators, businesses, and investors. The ability to meet these challenges will largely determine the stability and resilience of financial markets in the future.

6. Conclusion:

Overall, our work has shown that links with the NBFIs expose banks to liquidity, market, and credit risks. However, liquidity seems to be the main concern at present. In developed countries, the diversification of financial intermediation is associated with the emergence of new types of banking intermediation. Banks are increasingly transforming into service and risk management companies, backed by the capital market and driven by technological and financial innovations.

In general, we are observing a transition toward more diversified financial intermediation, with a rise in market intermediation and a decrease in traditional banking intermediation in many developed and emerging countries. This evolution is influenced by factors such as deregulation, technological innovation, interest rates, the needs of economic actors, and investor preferences. To these elements is added the complexity of the interactions between trade policies and financial markets, where each tariff measure has the potential to quickly alter the perception of risk and investor confidence on a global scale.

Moreover, although we have examined some elements of the cyclical outlook and emerging challenges for global financial stability, we cannot conclude that our results are generalizable to all global financial markets. In this sense, EMDEs face a multitude of risks (economic, climatic, geopolitical, and technological) that can weaken their financial stability, reduce their growth, and further marginalize them in a fragmented world. To deal with it, strengthening their resilience, improving international cooperation, and diversifying their sources of financing will be essential priorities.

The rise of NBFIs in the international financial system requires Algeria to rethink its approach to financial regulation. It is not about prohibiting or restricting these actors, but about integrating them into a coherent, transparent, and resilient framework, in accordance with international best practices. This will not only preserve macroeconomic stability but also channel new financing toward the real economy, with a focus on sustainable, inclusive, and sovereign growth.

The Algerian financial sector, although still marginally exposed to these actors, cannot ignore the rise of non-banking players and their challenges. If they are well regulated, these actors can become a useful financing lever for Small and Medium-sized Enterprises, innovation, startup, and structuring projects. But without appropriate regulation, they could become a factor of instability. In this regard, adopting a specific framework law for NBFIs, including requirements for transparency, risk management, and solvency, allows monetary authorities to provide the economy with an additional and necessary amount of money for continued economic growth and to integrate them into macroprudential stability policies.

Finally, the increasing interconnection of markets, the volatility of capital flows, and the dependence on hydrocarbon revenue make our economy vulnerable to external shocks. Algeria has everything to gain by equipping itself with a modern, preventive, and inclusive framework to

channel these new financial flows in the service of its sovereign economic development. However, in the near future, political decision-makers and financial system stakeholders will face new questions and challenges. These new questions concern: the new risks and opportunities that could emerge and what their impact might be and how they could interact?

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