



RESERVE BANK OF AUSTRALIA

Financial Stability Review

March 2026

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Financial Stability Review

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Financial Stability Assessment

This Financial Stability Review was finalised on Wednesday 18 March 2026. At the time of writing, the conflict in the Middle East was evolving rapidly, with considerable uncertainty over its ultimate duration, scale and broader spillover effects. Council of Financial Regulator (CFR) agencies are closely monitoring the situation and engaging with industry as appropriate.

Following a lengthy period where risk premia in global financial markets were unusually low, the escalation of conflict in the Middle East has sparked a substantial increase in volatility. Given leverage and concentration risk in key global asset markets had increased materially in recent years, amid a period of low risk premia, this increases the potential for a disorderly repricing of assets in response to further adverse developments. The risk of significant operational, cyber and security incidents, which have risen over recent years, is also heightened at present. The Australian financial system has established a good degree of resilience to navigate through a high-risk international environment, though any of these events, if severe enough, could pose financial stability challenges in Australia.

In this environment, the CFR agencies, including the RBA, continue to engage closely with industry to ensure that:

- Australian financial institutions continue to build resilience and readiness to respond to extreme-but-plausible liquidity, operational and geopolitical risks that could interact
- lending standards remain prudent amid an upswing in credit growth, with regulatory settings continuing to limit the build-up of systemic risk and thus foster confidence in the financial system.

Global financial stability risks are elevated in a rapidly evolving international environment.

Escalation of conflict in the Middle East has sparked a sharp increase in volatility in global financial markets, following a period of benign market conditions. Volatility has been particularly pronounced in energy and other commodity markets, and this has spilled over to other asset classes. Just prior to the escalation of the conflict, some firms had experienced sharp equity price declines as investors reassessed the prospects for AI to affect business models. Conditions for private credit markets had also become more challenging.

Yet risk premia in global equity and credit markets have remained fairly low by historical standards. Additionally, even after an increase in government bond yields in several advanced economies, measures of sovereign bond term premia were well within historical ranges and markets remained functional. Resilience in the global financial system prior to the escalation of the conflict had been supported by systemically important banks remaining profitable and well capitalised, and growth in the global economy over the past year exceeding most analyst expectations, with trade flows adjusting relatively quickly to changes in tariffs. Corporate and household balance sheets in advanced economies have remained strong, although pockets of stress persist among non-prime borrowers.

Global financial stability risks remain elevated due to heightened geopolitical tensions and several sources of uncertainty. The global economic and financial outlook could deteriorate abruptly for any number of reasons, such as:

- **Potential for elevated geopolitical tensions to spillover into a severe international shock.** The geopolitical environment remains highly fluid. The conflict in the Middle East could trigger a larger shock that destabilises the global economy, particularly if supply disruptions to oil and other commodity markets are prolonged. Tensions among major global powers also have the potential to escalate, hostile cyber and other actions are intensifying, and strains in the international rules-based order are increasing alongside the risk of global geoeconomic fragmentation.
- **Potential for a sharp revision of the outlook for AI-related investments.** Should expectations around the productivity benefits of the surge in AI-related investment be reduced, it could lead to a significant downgrade in profitability forecasts and asset valuations. Negative consequences for asset quality in the financial system and investment plans in the real economy could result.
- **Potential for confidence in institutional arrangements to be undermined or regulatory divergence.** A sustained pattern of unconventional policy actions and a push for regulators to rebalance regulatory frameworks in favour of growth (relative to stability) could also undermine established institutional arrangements in some jurisdictions or lead to material regulatory divergence globally. This could affect policy credibility, give rise to a new wave of regulatory arbitrage and present additional challenges for multilateral cooperation.
- **Potential for a disruptive crystallisation of macro-financial vulnerabilities in China.** Chinese authorities have identified strong supply growth in the industrial sector and weak domestic demand continue to characterise the Chinese growth model, which, combined with low inflation relative to trading partners, has led to a real exchange rate depreciation. This has contributed to strong exports and a rising current account surplus, which has amplified tensions with some trade partners. Longstanding vulnerabilities in parts of the Chinese financial system – including banks, non-banks and local governments – have been exacerbated by the ongoing weakness in the Chinese real estate sector. Debt in the corporate sector continues to rise sharply as a share of GDP. Consolidated public debt in China is also expected to rise further, particularly given the need to support highly indebted local governments. A disruptive crystallisation of these vulnerabilities could sharply increase risk aversion in global financial markets and result in reduced Chinese demand for Australian goods and services.

This environment increases the prospect for international developments to interact with existing vulnerabilities and affect financial stability in Australia.

A disruptive adjustment in international financial markets could pose financial stability challenges in Australia. Two global vulnerabilities stand out in this regard:

- **Vulnerabilities arising from a large and growing stock of sovereign debt in key advanced economies, which could be subjected to a disorderly repricing if debt sustainability concerns were to escalate.** A sharp sell-off could be amplified by the growing role in these markets of leveraged, price-sensitive non-bank financial institutions (NBFIs). Projected fiscal deficits in a range of advanced economies are expected to add further to the supply of sovereign debt in the years ahead, at a time where price-sensitive NBFIs are becoming a key source of marginal demand. The historical experience suggests a sharp repricing or period of disorderly functioning in key international sovereign debt markets could spill over to Australian bond markets, presenting challenges to financial stability (discussed in more detail below).

- **Vulnerabilities arising from low risk premia and concentrated exposures in key international equity and credit markets, with the potential for disorderly price adjustments amplified by leverage and liquidity mismatches in global NBFIs.** Global equity and bond markets remain vulnerable to sharp corrections. Ongoing significant increases in exposure to the AI investment cycle across the financial system could also become a source of instability if the optimistic outlook for that sector is substantially revised. More generally, a further escalation in geopolitical tensions, or adverse policy or macro-financial developments, could trigger a sustained increase in risk aversion across global financial markets.

A disruptive adjustment in international markets could spill over to Australia by sharply increasing domestic financing costs, restricting Australian firms' and financial institutions' access to funding and liquidity in global markets, and leading to substantial losses in the value of financial assets, including those held by households. If severe enough, it could also limit credit availability in Australia and have consequences for the real economy. Australian companies, banks and superannuation funds have taken steps to mitigate their exposure to shocks in global financial markets in recent years, including by building significant liquidity buffers, and any depreciation of the exchange rate could also play a shock-absorbing role for the Australian economy. However, a more shock-prone international environment means it is important that Australian borrowers and lenders maintain resilience.

Growing operational complexity and interconnectedness across the financial system is increasing non-financial vulnerabilities. These heighten the potential for operational incidents to have systemic financial consequences, including if they interact with other stress events. For example, an outage at a major financial institution or a service provider used by many financial institutions could disrupt funding markets or stop households and businesses from accessing their money. Operational resilience in the payments system and across financial market infrastructures is particularly critical to ensuring the steady flow of funds throughout the economy. Complexity and interconnectedness can also increase as new technology is introduced to the financial system and has to interact with existing technological infrastructure. When episodes of financial and operational stress occur simultaneously, it also complicates the nature of crisis response and the scope of coordination required across regulators, government and industries.

The Australian financial system has a good degree of resilience, though the risk of a more material adverse shock has increased over recent weeks.

If a significant economic downturn occurs, Australian banks are well positioned to absorb significant loan losses while continuing to support the economy through lending to households and businesses. Banks are well capitalised and have maintained prudent lending standards and provisioning. Non-bank lenders and private credit firms have increased the availability of credit for both housing and business borrowers, which could result in higher loan losses in the years ahead, but their relatively small size means the systemic impact of stress in this sector would be limited. Some borrowers continue to experience severe financial stress, but overall loan losses have remained low by historical standards, reflecting strong collateralisation of loans and the relatively small increase in non-performing loans over recent years. Banks' liquid assets provide a buffer against unanticipated liquidity shocks, but it is important that these can be converted quickly into cash when necessary.

As a large and growing part of the overall financial system, it is important that the superannuation sector continues to strengthen its approach to risk management.

The value of assets managed by the superannuation sector now represents around 160 per cent of GDP, one-third of Australian financial system assets, and is expected to continue growing solidly until at least 2050. This growth, coupled with an increasing share of Australians drawing retirement income streams from the system, means that further strengthening of superannuation funds' governance, liquidity and operational risk management practices will remain a key focus for regulators.

The general insurance sector is not currently a source of financial stability concern, but insurance affordability and availability may become increasingly challenging over time.

The general insurance sector has remained well capitalised and profitable. Home insurance premiums remain at historically high levels and further increases could increase underinsurance, lowering the credit quality of housing loans over time. The forthcoming Climate Vulnerability Assessment by the Australian Prudential Regulation Authority's (APRA) will help quantify how general insurance affordability may be affected by climate change.

The strong financial positions of most Australian households and businesses means that they are unlikely to be a source of instability, though financing pressures will increase for some if inflation is higher for longer than currently forecast.

Borrowers are generally well placed to weather cost pressures stemming from the conflict in the Middle East and higher interest payments, though the most vulnerable borrowers will face growing challenges. Loan arrears have remained at low levels, supported by strength in the labour and housing markets. Company insolvencies have stabilised at around longer run averages at an economy-wide level, although the share of companies entering insolvency remains elevated in the hospitality and construction sectors – where the operating environment has been more challenging, particularly for smaller firms. Fundamentals continued to improve across most commercial real estate (CRE) markets and there continues to be little evidence of financial stress among owners of Australian CRE.

In this environment, financial institutions need to maintain focus on their resilience.

It is important that lending standards remain prudent, and that regulation continues to limit the build-up of systemic risk and foster confidence in the financial system, given the backdrop of strong credit growth.

While overall lending standards have remained sound, there is early evidence that some forms of riskier lending have picked up. Household indebtedness has been a key vulnerability domestically for many years, and high debt-to-income (DTI) lending to investors has increased of late, though remains below APRA's recently implemented limit on high DTI lending. High loan-to-valuation ratio lending to first home buyers has also increased alongside the expansion of the Australian Government 5% Deposit Scheme in October 2025. Heightened competition for business loans over recent years as bank and non-bank lenders seek to expand their business lending has supported credit availability for some businesses and reduced refinancing risks. Relatedly, there has been a slight easing in CRE lending standards over the past year and incremental increases in risk appetite to lend to other businesses more recently. However, there has been little evidence of a broader decline in business lending standards to date.

The RBA and other CFR agencies continue to monitor lending conditions closely and are working together to deliver better regulation of the financial sector without compromising financial stability, consumer protection and market integrity. In addition, the International Monetary Fund will be conducting an assessment during 2026 of the resilience of the financial sector, the quality of the regulatory and supervisory framework, and the capacity to manage and resolve financial crises as part of its Financial Sector Assessment Program.

Enhancing resilience to operational and geopolitical risk is a regulatory priority around the world, including in Australia. Recent operational incidents in Australia and abroad have highlighted the prospect for serious spillover effects to occur across a financial system that has become more complex and interconnected over time. These vulnerabilities are increasingly targeted by sophisticated malicious actors, including state-sponsored attackers, who can seek to co-opt or collaborate with insiders that have greater access to systems. In Australia, CFR agencies are actively working with industry to strengthen the operational and cyber resilience of individual financial institutions, and the system as a whole. The RBA is also strengthening its operating model to support the critical payments settlements system more effectively, including by enhancing its cybersecurity controls and modernising core technology infrastructure. To support the Payments System Board's strategic objective to strengthen the resilience of the payments system, the RBA is actively pursuing a program of work aimed at identifying system-wide vulnerabilities in Australia's payments system. Over the course of 2025, CFR agencies have also worked with large financial institutions on scenario analysis to ensure there is a clear understanding of the potential impact of adverse geopolitical events, and on the development of robust payment system contingency capabilities. As part of this work, CFR agencies are strengthening their engagement with relevant government agencies and industry to support better information sharing and response coordination for extreme-but-plausible events.



Chapter 1

The Global Macro-financial Environment

Summary

Global financial stability risks are elevated in a rapidly evolving international environment.

Volatility has increased sharply in global financial markets following the escalation of conflict in the Middle East, after a period of benign market conditions. Volatility has been particularly pronounced in energy and other commodity markets, and this has spilled over to other asset classes. Just prior to the escalation of the conflict, some firms had experienced sharp equity price declines as investors reassessed the prospects for AI to affect business models. Conditions for private credit markets had also become more challenging.

Yet risk premia in global equity and credit markets have remained fairly low by historical standards. Additionally, even after an increase in government bond yields in several advanced economies, measures of sovereign bond term premia were well within historical ranges and markets remained functional. Resilience in the global financial system prior to the escalation of the conflict had been supported by systemically important banks remaining profitable and well capitalised, and growth in the global economy over the past year exceeding most analyst expectations, with trade flows adjusting relatively quickly to changes in tariffs. Corporate and household balance sheets in advanced economies have remained strong, although they face the risk of sustained higher energy costs and pockets of stress persist among non-prime borrowers.

The global economic and financial outlook could deteriorate abruptly for any number of reasons. Escalation of conflict in the Middle East and persistent geopolitical tensions elsewhere continue to add to already heightened levels of uncertainty for the financial system. Supply disruptions to oil and other commodity markets, unilateral trade policy actions and the large footprint of AI-related investment present risks for both economic activity and asset valuations. Concerns have also grown around international policy uncertainty and the resilience of established institutional arrangements in some jurisdictions, alongside broader fiscal sustainability challenges. Longstanding macro-financial vulnerabilities in the Chinese economy also persist. The global financial sector remains exposed to disruption from cyber-attacks and operational incidents and, over the medium-term, the physical and transition risks from climate change.

Against this backdrop, global stress events have the potential to interact with – and amplify – existing vulnerabilities, and affect financial stability in Australia:

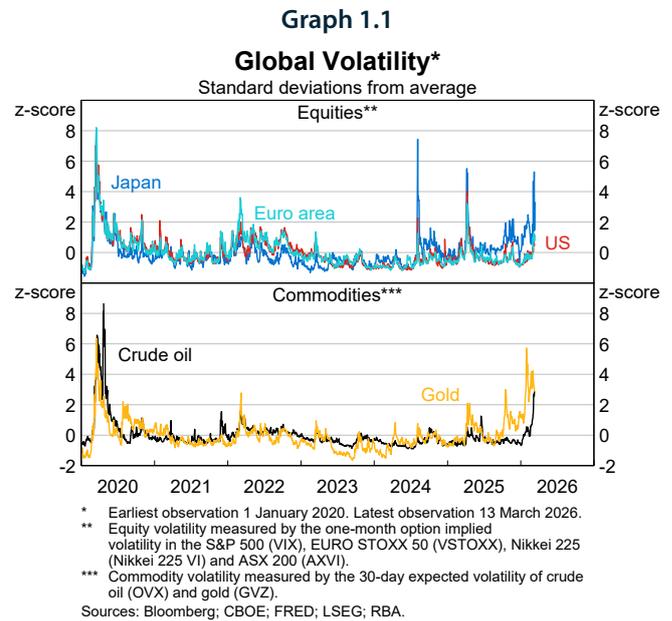
- **A disruptive adjustment in international financial markets could pose financial stability challenges in Australia.** A large and growing stock of sovereign debt in key advanced economies could be subjected to a disorderly repricing if debt sustainability concerns were to escalate. A sharp sell-off could be amplified by the growing role in these markets of leveraged, price-sensitive non-bank financial institutions (NBFIs). In addition, low risk premia and concentrated exposures in key international equity and credit markets increase the potential for disorderly price adjustments, which could be amplified by leverage and liquidity mismatches in global NBFIs.
- **Growing operational complexity and interconnectedness across the financial system is increasing non-financial vulnerabilities.** Alongside elevated geopolitical tensions, which increase the potential for state-sponsored cyber-attacks, these vulnerabilities heighten the potential for operational incidents to have systemic financial consequences, including if they interact with other stress events.

1.1 Key developments

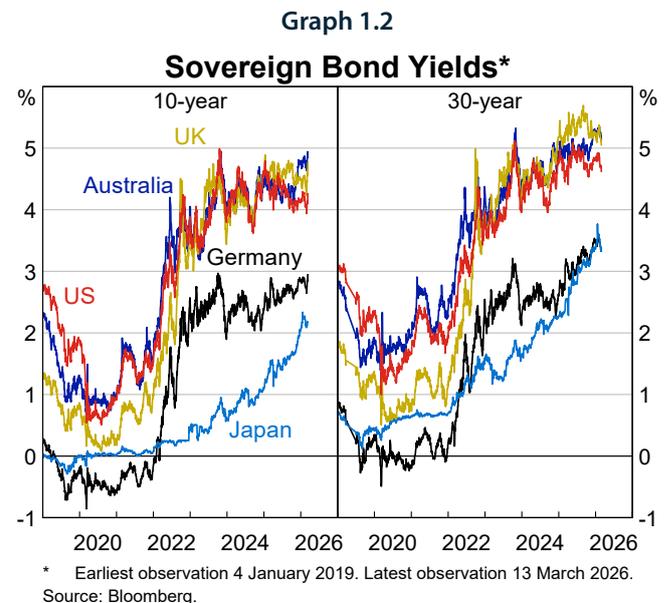
Global financial markets have been volatile following the escalation of conflict in the Middle East, but risk premia have remained low.

Volatility in global equity markets has increased following the recent escalation of conflict in the Middle East, as well as shifting expectations around the medium-term impact of AI (Graph 1.1). Major global equity markets declined in early March, particularly markets most exposed to energy supply disruptions. However, markets remained functional and while equity and credit risk premia increased, they remain at low levels. In the second half of 2025 and into 2026, equity and credit markets had generally been buoyant, with growth in equity prices across many advanced economies underpinned by improved expectations for global growth in 2026.¹ Market valuations were supported by better-than-expected results across most sectors, as well as upward revisions to expected earnings growth in 2026 and 2027. Expectations for generalised growth in AI-exposed companies had also been a key driver of equity market performance over recent years, particularly in the United States and East Asia. However, investors appear to be reassessing this outlook, with a sharp repricing in some technology companies and a widening in some credit risk measures, particularly for some software firms, since late 2025. These adjustments reflect concerns about potential industry disruption from AI-based competition, as well as the level of borrowing required to fund future AI-related infrastructure investment on a large scale.

The escalation of conflict in the Middle East has also led to very high volatility in commodity markets and increases in some government bond yields. In early March, severe disruption to trading routes, particularly the Strait of Hormuz, and damage to infrastructure triggered considerable volatility in global oil, natural gas and fertiliser markets, with most commodities experiencing sharp price increases. Gold and other metal prices had also experienced significant volatility since early 2026, in response to the growing uncertainty in the international environment (Graph 1.1). The escalation of conflict in the Middle East resulted in higher yields and volatility measures across government bond markets,



as investors reassessed the implications for monetary policy and the fiscal outlook. More generally, government bond yields remain above their decade averages, partly reflecting ongoing concerns that issuance will remain significant in coming years (Graph 1.2).

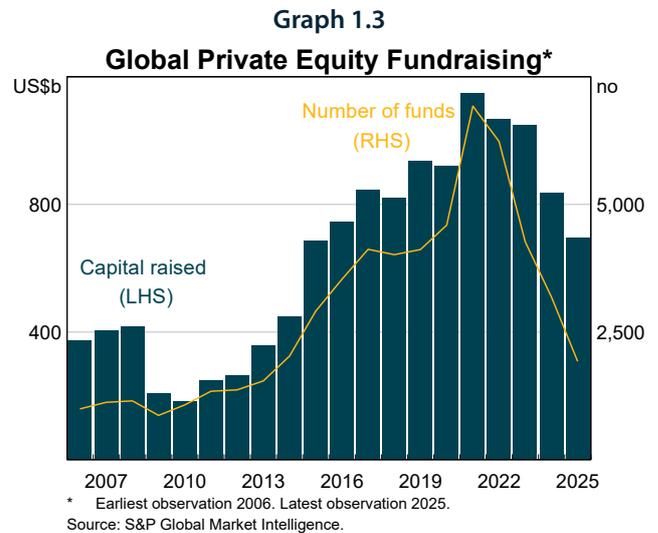


Global private markets have continued to grow, though conditions remain challenging.

High-profile defaults in the United States and the United Kingdom have highlighted how vulnerabilities in segments of private credit markets could spill over to the broader financial system.

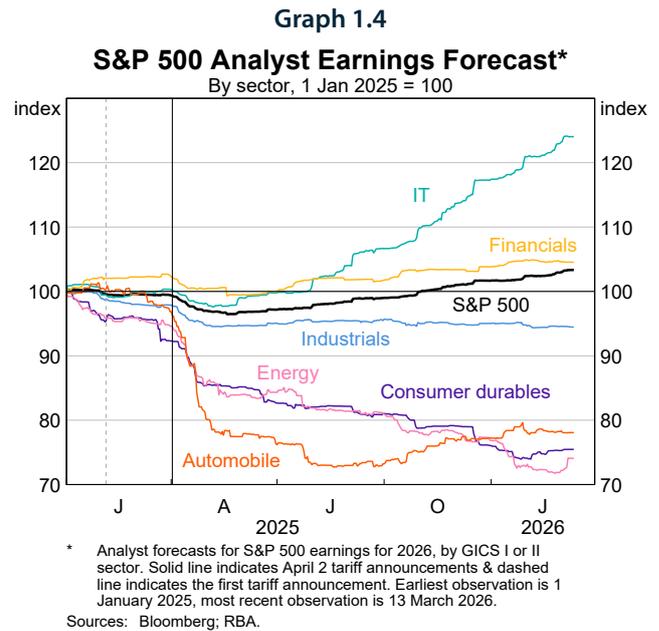
The defaults of First Brands Group (a global automotive parts supplier) and Tricolor (a subprime auto lender and dealer) in September 2025 highlighted opaque linkages and common exposures between non-bank credit providers and the broader financial system. These defaults were largely perceived as idiosyncratic by investors, including allegations of fraud and poor due diligence. However, banks reported total writedowns of over US\$1 billion from their direct lending to these firms, as well as their exposures through credit funds and warehouse lending facilities. More recently, and in comparable circumstances, some global banks and private credit providers reported material exposures to UK-based mortgage lender Market Financial Solutions. Concerns have also grown among investors around private credit and private equity exposures to the software industry, where valuations have come under pressure in the face of potential disruption from AI-based competition. Some private credit funds have reportedly experienced an increase in redemption requests in response to recent developments, leading them to introduce restrictions on investor redemptions. Better understanding and responding to challenges in private markets is a growing focus of regulators globally.² In December 2025, the Bank of England launched a system-wide exploratory scenario exercise to enhance its understanding of broader risks and dynamics in private markets, with results expected to be published in early 2027.³

Following significant growth over the last decade, global private equity funds have encountered challenges in exiting their investments. Assets under management by private equity funds reached US\$10.9 trillion as of September 2025, although fundraising has slowed considerably over the past two years (Graph 1.3). The private equity industry has also faced persistent challenges with selling ('exiting') portfolio investments, with the average asset holding period at exit for buyout funds having increased to seven years in 2025, compared with five years in 2010.⁴ This has intensified liquidity pressures for fund investors, as delays in the return of capital prevent them from redeploying funds or rebalancing their portfolios. To alleviate some of these liquidity pressures and return capital to investors, a greater share of fund managers are turning to alternative divestment solutions. For example, some fund managers are selling partial stakes in their investments (as opposed to making full exits), or setting up new continuation vehicles that buy assets from their existing funds, including through the use of some leverage.



Corporate and household balance sheets in advanced economies have remained strong, but pockets of stress persist among the most vulnerable borrowers.

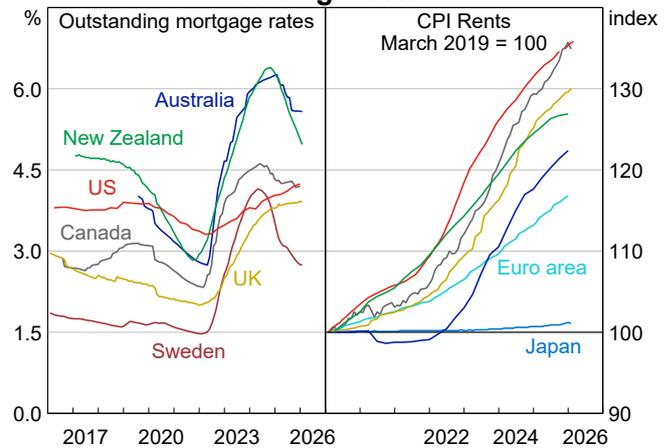
Corporate balance sheets have largely remained healthy for listed companies across advanced economies, but sustained elevated energy prices would increase cost pressures. Gross profit margins have continued to rise while median cash buffers remain around or above pre-pandemic averages. Impacts from tariffs have been limited to date, with better-than-expected earnings results in Europe and the United States across most sectors. Looking forward though, a sustained period of elevated energy prices would affect demand growth, as well as reduce the profitability of some firms due to higher input costs. In addition, higher earnings expectations for technology firms have masked weaker forecasts for more tariff-exposed sectors such as automobile manufacturing, consumer durables and energy, particularly in the United States (Graph 1.4). Leverage for the median listed company increased over the year in most advanced economies, although interest coverage ratios also increased, indicating that debt servicing capacity has not deteriorated alongside the additional borrowing. Default rates on speculative-grade debt remain elevated in Europe and the United States, though ratings agencies expected them to ease over 2026. Corporate defaults continue to be dominated by out-of-court debt restructurings ('distressed exchanges'), for which there is an increased risk of firms re-entering default if underlying issues are not resolved.



Financing conditions for corporates have remained accommodative and debt issuance has been strong, but there are considerable funding needs in coming years. Corporate bond spreads for all but the riskiest asset class remained close to historical lows. Corporate debt issuance was strong in the second half of 2025, with notable issuance from AI-exposed firms, particularly hyperscalers, to finance large-scale infrastructure investments.⁵ Many firms, including speculative-grade issuers, have also been taking advantage of accommodative funding conditions to refinance debt and push back upcoming maturities. In the six months to October 2025, European and US speculative-grade issuers reduced their maturities over the next three years by almost 15 per cent. Nevertheless, as of October 2025, over US\$1.5 trillion in outstanding speculative-grade debt (including bonds, loans and revolving credit) remained due to mature in the United States and Europe by the end of 2028. Refinancing plans for more vulnerable firms could be affected if global financial conditions were to tighten materially over the period ahead in response to heightened international uncertainty.

Households have largely remained resilient, but the prospect of further cash flow support from lower interest rates has diminished, while the risk of sustained higher energy costs has increased. Over the last two years, gains in housing and equity markets supported aggregate household balance sheets, while easing policy rates alleviated debt servicing pressures in many advanced economies. However, improvements in household cash flows observed over recent years may not be sustained as many central banks have recently signalled a likely end to policy easing, and interest rate expectations have shifted upwards. In addition, pockets of stress persist among some renter and highly indebted households following an extended period of elevated interest rates and cost-of-living pressures – with the potential for higher energy costs to further affect household budgets in the period ahead (Graph 1.5). While aggregate consumer credit delinquencies have somewhat stabilised, arrears remain elevated among the most vulnerable households, providing evidence of stress in some markets. For example, non-prime auto loan delinquencies in the United States are at historically high levels.⁶ Although further policy rate cuts are still expected in the United States, households would only see marginal resulting improvements in their cash flows due to the high share of fixed-rate mortgages. Continued global uncertainty and elevated asset valuations pose additional risks to the balance sheets of some households that have increased exposure to the stock market in recent years. For instance, US margin lending has increased notably over the past year.

**Graph 1.5
Housing Costs***



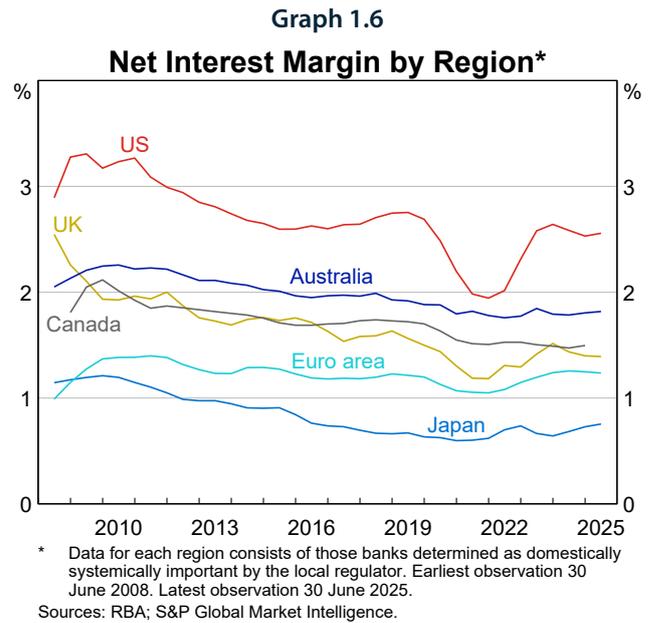
* Earliest outstanding mortgage rate observation July 2019 for Australia, January 2017 for New Zealand, July 2016 for Canada, March 2016 for the US and January 2016 for all other jurisdictions. Latest outstanding mortgage rate observation December 2025 for Australia and the US and January 2026 for all other jurisdictions. Earliest CPI rents observation March 2019 for Australia and New Zealand, and January 2019 for all other jurisdictions. Latest CPI rents observation January 2026 for Canada, Japan, the UK and the US and December 2025 for all other jurisdictions.

Sources: ABS; Eurostat; LSEG; RBA; Statistics Sweden.

Large banks in advanced economies have remained highly resilient overall, prompting some regulators to review elements of their regulatory frameworks to alter the balance between resilience and growth.

Banks' balance sheets and profitability remained strong, though risks remain elevated in certain segments. Common Equity Tier 1 ratios for large banks were generally robust and recent stress tests indicated that large banks would remain above minimum capital requirements even under adverse economic scenarios. Profitability indicators have been resilient to date, and net interest margins (NIM) remained healthy despite declines in policy rates (Graph 1.6). Notwithstanding increased expenses to support investment in personnel and IT modernisation, cost ratios have remained stable. Asset quality also remained generally strong with non-performing loan ratios around multi-year lows across most advanced economies. However, authorities remain alert to potential areas of risk. They have become increasingly concerned about potential risks from bank exposures to NBFIs building over the past decade, as highlighted by losses from recent non-bank defaults in the United Kingdom and the United States. In addition, bank exposures to tariff-sensitive corporates, small and medium-sized enterprises, commercial real estate and subprime household borrowers continue to carry elevated risks and could affect asset quality if macro-financial conditions were to deteriorate sharply. While advanced economy banking systems have remained resilient, vulnerabilities in the Chinese banking sector persist alongside an ongoing and significant downturn in the residential property sector (see Box: Vulnerabilities in the Chinese financial system).

Some jurisdictions are reviewing elements of their banking regulation and supervision, aiming to recalibrate the balance between resilience and growth. There is broad agreement among advanced economies that financial stability is vital to supporting sustained economic growth. At the same time, several jurisdictions have recently expressed concerns that current regulatory complexity and high compliance costs may be constraining competition in the banking sector and encouraging migration of lending and



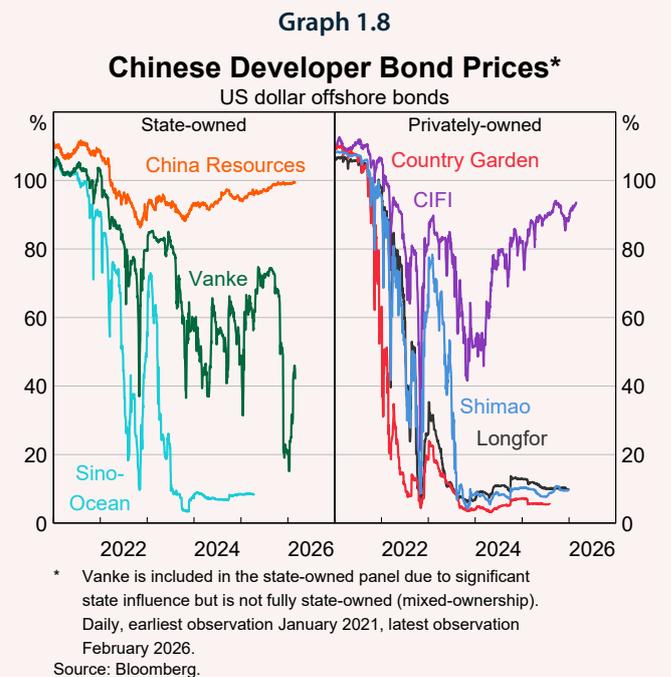
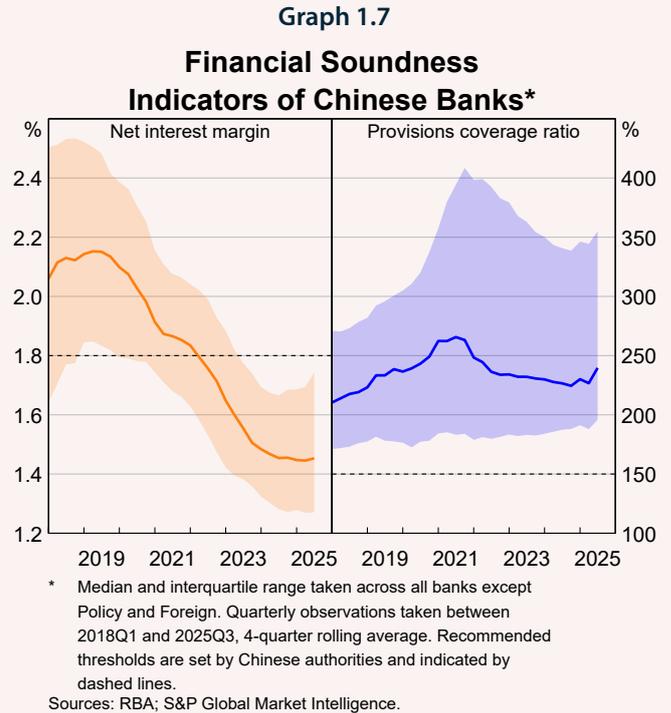
investment activity to less-regulated segments. Authorities in the euro zone, New Zealand, the United Kingdom and the United States are considering avenues to modernise financial regulation, streamline supervisory frameworks and better tailor rules to institutions' risk profiles. Central banks in these jurisdictions have emphasised that such efforts are intended to reduce complexity, while maintaining core standards. In Australia, the Council of Financial Regulators (CFR) agencies are working together to deliver better regulation of the financial sector, aiming to improve efficiency through regulatory reform without compromising financial stability, consumer protection and market integrity.⁷ If material regulatory divergence were to emerge across major economies in the current environment, this could increase the risk of regulatory arbitrage and, if significant, weaken the global banking system's resilience to future shocks. Against this backdrop, international bodies, including the Financial Stability Board (FSB), are monitoring these initiatives and adjusting their workplans to support alignment across jurisdictions.⁸

Box: Vulnerabilities in the Chinese financial system

Chinese authorities continue to respond to longstanding structural weaknesses in the Chinese financial system. Many banks, including the five major globally systemically important banks in China, continue to report NIMs below the 1.8 per cent threshold recommended by authorities, although the previous sustained decline in NIMs has stabilised. Bank capital ratios remain adequate in aggregate, and asset quality appears to be improving, although future potential loan losses could be a factor in higher provisioning (Graph 1.7).

Chinese authorities have provided support through targeted interventions, including recapitalising the largest state-owned banks and promoting consolidation in the banking sector – with the closure of a significant number of institutions during 2025, particularly in rural areas. In addition, while business and government debt continue to rise sharply as shares of GDP, the ongoing local government debt swap program has reduced off-balance sheet debt held by local government financing vehicles. This has eased debt interest costs for local governments, particularly in high-risk provinces. Central authorities are reportedly considering reforms that would increase their share of overall fiscal expenditures and expand revenue sources for local governments, which could improve the sustainability of local government debt servicing and the provision of public services. However, progress remains limited to date, particularly given ongoing weakness in the property sector.⁹

The downturn in the property sector has continued over the past six months. Housing prices continued to decline, returning to the rates of decline seen in 2024. The banking sector’s exposure to the property market remains substantial, including to property developers, a number of which remain under severe financial stress. Bond prices of Vanke, a major developer, fell sharply on renewed solvency concerns. Following extended debt restructuring negotiations, Vanke’s major state-owned shareholder eventually agreed to provide support (Graph 1.8). Authorities have maintained a supportive-but-not-stimulative stance towards the property sector as the downturn continues, preferring market-based solutions as they seek to balance moral hazard concerns with disorderly corrections.



Instability in the Chinese financial system is unlikely to have a direct impact on financial stability in Australia as the financial links between China and Australia are limited. However, a shock to the Chinese financial system could affect the rest of the world and Australia indirectly, via increased risk aversion in global financial markets. Other channels of transmission of financial stress in China to Australia would likely be lower global commodity prices, reduced Chinese demand for Australian goods and services and a sharp slowing in global economic activity. If this were to eventuate, the Australian dollar exchange rate would be expected to act as an automatic stabiliser and help to offset some of the negative impact on the Australian economy.

1.2 Key vulnerabilities that could affect financial stability in Australia

Risks to the global financial system remain elevated due to heightened geopolitical tensions and policy uncertainty.

The geopolitical environment remains highly fluid. The escalation of conflict in the Middle East could trigger a larger shock that destabilises the global economy, particularly if supply disruptions to oil and other commodity markets are prolonged. Tensions among major global powers also have the potential to escalate, hostile cyber and other actions are intensifying, and strains in the international rules-based order are increasing alongside the risk of global geoeconomic fragmentation. A sustained pattern of unconventional policy actions and a push for regulators to rebalance regulatory frameworks in favour of growth (relative to stability) could also undermine established institutional arrangements in some jurisdictions or lead to material regulatory divergence globally. This could affect policy credibility, give rise to a new wave of regulatory arbitrage and present additional challenges for multilateral cooperation.

While the global economic outlook has been resilient to date in the face of considerable headwinds, macro-financial risks have increased.

Growth in the global economy over the past year or so exceeded most analyst expectations, with trade flows adjusting relatively quickly to changes in tariffs. However, uncertainty remains high, particularly surrounding disruptions to oil supply and global trade. Fiscal sustainability in some advanced economies also remains a concern. Further, should expectations around the productivity benefits of the surge in AI-related investment be reduced, it could lead to a significant downgrade in profitability forecasts and asset valuations. A disruptive crystallisation of macro-financial vulnerabilities in China, and related spillovers to the global economy, could also sharply increase risk aversion in global financial markets.

Stress events have become more likely in this environment, and have the potential to interact with existing vulnerabilities to generate disruptive international shocks.

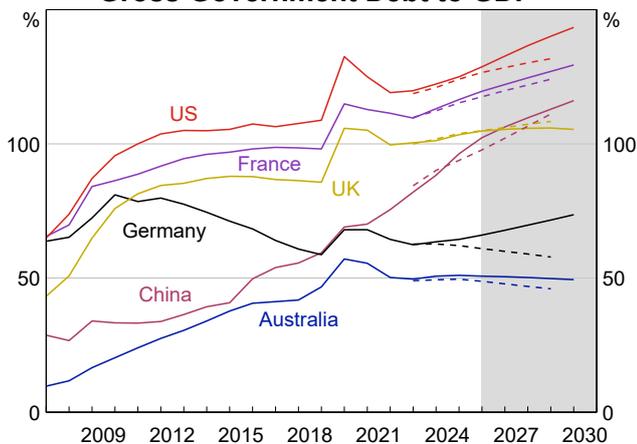
The following global vulnerabilities stand out as having the potential to significantly affect financial stability in Australia in such a scenario.

A large and growing stock of sovereign debt in key advanced economies could be subjected to a disorderly repricing if debt sustainability concerns were to escalate.

Persistent strong growth in the supply of sovereign debt is expected in the years ahead. Projected fiscal deficits are expected to increase further the supply of government debt and raise debt-to-GDP ratios in most major advanced economies by the end of the decade (Graph 1.9). Defence spending commitments, growing expenditures driven by global population ageing and the costs of severe weather events and climate transition investments are among the structural factors expected to contribute to this increase. Further, the composition of government debt portfolios continues to shift to shorter maturities, particularly in the United States, increasing sovereign issuers' exposure to rollover risks, which could increase debt-servicing costs. In some major emerging economies like China, consolidated public debt is also expected to rise further, as structural fiscal pressures mirror those seen in advanced economies. In particular, the need to support highly indebted local governments is likely to drive continued expansion of sovereign and quasi-sovereign debt issuance, amid a structural rebalancing of the Chinese economy.

Graph 1.9

Gross Government Debt to GDP*



* Earliest observation 2007. Latest observation 2030. Shaded region indicates IMF forecasts as at October 2025. Dashed lines indicate IMF forecasts as at October 2024.

Source: IMF.

At the same time, leveraged, price-sensitive NBFIs are expected to absorb a larger share of new sovereign bond issuance.¹⁰

The relative footprint of traditional buyers of longer maturity government debt, including defined-benefit pension funds and insurers, has declined in recent years, while central banks have unwound much of their pandemic-era government bond purchases. A range of price-sensitive investors with greater appetite for short maturity debt have taken a more prominent role as marginal buyers. These include leveraged hedge funds investing in relative value trades (e.g. the Treasury basis trade), as well as bond funds, money-market funds and fast-growing US-dollar stablecoins susceptible to potential redemption risk.¹¹ These business models could face liquidity or deleveraging pressures during periods of heightened volatility, amplifying market stress with the potential to spill over into closely linked markets such as the repo market.¹²

Were debt sustainability concerns to escalate, global sovereign bond markets could be subjected to a disorderly repricing, which could spill over to the Australian financial system.

Term premia on government debt have increased over recent years, partly in response to high debt levels and deteriorating fiscal outlooks; however, they remain broadly at or below longer term averages. Further geopolitical shocks, increased economic policy uncertainty or concerns about fiscal slippage could trigger a material shift in investor sentiment and sharp increases in term premia and government bond yields. The escalation of conflict in the Middle East and events following the announcement of the snap election in Japan

demonstrate how quickly sovereign yields can respond to geopolitical or policy uncertainty, particularly in advanced economies with high debt ratios.¹³ Given the role that sovereign bonds play in global funding markets and the management of market participants' credit and liquidity risks, any material disruption could spread to critical parts of the international financial system.

Longer term fiscal sustainability concerns raise broader potential challenges for the global financial system.

Households, corporates and financial institutions could see tighter financial conditions if sovereign borrowing costs increased materially, and policymakers would face increased challenges in managing public debt levels, including trade-offs between growth in spending programs, debt servicing and inflation. This could also reduce the fiscal space available in some jurisdictions to respond to a material economic downturn or other future shocks.

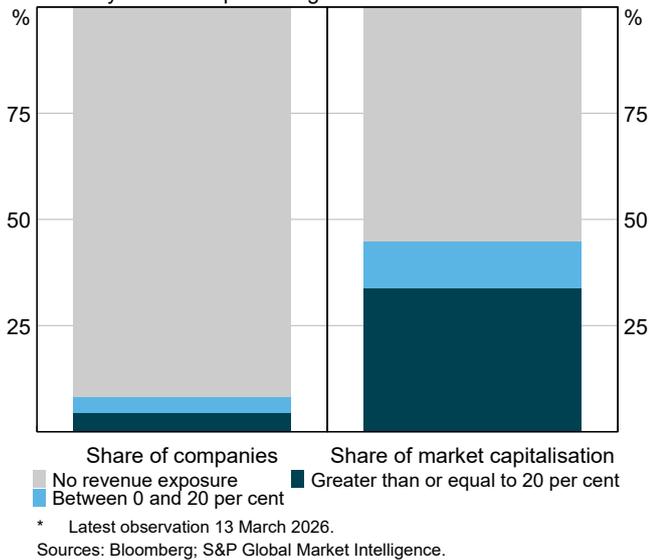
Low risk premia and concentrated exposures in key international equity and credit markets increase the potential for disorderly price adjustments, which could be amplified by leverage and liquidity mismatches in global NBFIs.

Global equity and corporate bond markets remain vulnerable to sharp corrections. Equity market valuations and sectoral concentration measures remain elevated, with companies that earn revenue related to AI estimated to account for over 40 per cent of S&P 500 market capitalisation (Graph 1.10). While global markets have been volatile in response to the escalation of conflict in the Middle East, risk premia remain close to historical lows. The likelihood of sudden shifts in global risk sentiment remains elevated. While bouts of market volatility over the last few years have typically been contained and short-lived, near-term market developments will likely depend on the length of and spillovers from the conflict. A further escalation in geopolitical tensions, or adverse policy or macro-financial developments, could lead to a sustained increase in risk aversion across global financial markets, triggering disorderly asset price corrections and impairing market functioning as seen in past episodes of severe volatility.

Graph 1.10

S&P 500 Exposure to AI*

By estimated percentage of revenue related to AI

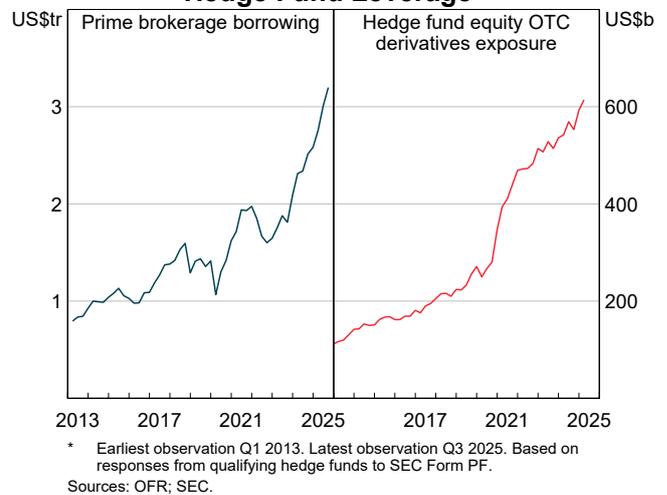


Ongoing significant increases in exposure to the AI investment cycle across the financial system could become a source of instability, particularly if leverage increases. Revenue streams for the AI sector can be opaque and highly interconnected, as firms have become increasingly engaged in interrelated financing activities where AI-exposed companies extend credit and take equity stakes in one another. These practices can reduce the transparency and reliability of cash flows, inflate revenue expectations and introduce balance sheet fragility, leaving shareholders and lenders exposed to potential volatility and losses if expected earnings fail to materialise. While the use of leverage has been relatively contained to date, the growing role of debt financing for AI investment is creating deeper links between the AI sector and credit providers, including banks, bond-market investors and private credit, raising the potential for any losses to spread across the financial system. Borrowing is expected to increase rapidly in the years ahead to fund ongoing large-scale infrastructure investment. Much of the planned investment is expected to be funded from internal cash flows, but market analysts estimate that a significant share will likely be financed externally, including through debt.¹⁴

Episodes of market stress could then be amplified and transmitted, including to households, by persistent vulnerabilities in the operating models of some types of global NBFIs. Use of leverage by hedge funds and other investment vehicles, including margin lending from prime brokers and exposure to

equity derivatives, is at historical highs (Graph 1.11). Alongside liquidity mismatches at bond and equity open-ended funds, such leveraged strategies can exacerbate episodes of heightened market volatility through forced deleveraging, asset fire sales and liquidity strains.¹⁵ Against this backdrop, international bodies have highlighted risks from households' growing exposure to equity markets, often through retirement savings in pension funds or passive investments (e.g. through index funds, ETFs), but also increasingly through active retail trading.¹⁶

Graph 1.11

Hedge Fund Leverage*

A severe global market stress, whatever its source, could sharply tighten financial conditions in Australia with potential consequences for financial stability. A disruptive adjustment in international markets could sharply increase domestic financing costs, restrict Australian firms' and financial institutions' access to funding and liquidity in global markets, and lead to substantial losses in the value of financial assets, including those held by households. If severe enough, it could also limit credit availability in Australia and have consequences for the real economy. Australian companies, banks and superannuation funds have taken steps to mitigate their exposure to shocks in global financial markets in recent years, including through hedging and by building significant liquidity buffers, and any depreciation of the exchange rate could also play a shock-absorbing role for the Australian economy.¹⁷

Growing operational complexity and interconnectedness across the financial system is increasing non-financial vulnerabilities.

Today's fast-paced technological environment presents financial institutions, their customers and regulators with a range of opportunities and challenges. On the one hand, the introduction of new technologies, business models, products and services can increase efficiency in the financial sector, improve customer service and enhance risk management practices. Regulators can also benefit from developments in supervisory technology improving data availability, analysis and monitoring. On the other hand, extensive digitalisation has led financial institutions to build networks of dependencies linking the core of the global financial system, including banks and financial market infrastructure, to critical service providers often located offshore and outside the financial regulatory perimeter.¹⁸ The complexity, opacity and concentration of these linkages, as well as unexplored risks from innovations such as AI agents and quantum computing, expose firms to operational and financial disruptions originating outside the financial sector. In an environment of heightened geopolitical risk, such vulnerabilities are also targeted by malicious actors through sophisticated cyber-attacks, including through the potential co-opting of insiders with system access.

Recent operational incidents underscore the risk of operational disruptions leading to broader financial system challenges. The outage at CME Group in November 2025 resulted in a loss of operation for its derivatives markets, when a cooling issue at a third-party data centre caused servers to shut down. It was an example of how an external technical issue can impair core market functions that the financial system more broadly depends on, such as price discovery, hedging and liquidity management, at short notice and on a large scale. Such incidents have the potential to affect financial system stability if they are sustained, or materialise alongside other shocks or during periods of market stress. While less likely to be systemic, other small-scale incidents could still affect public confidence in the financial system or generate losses, for example, by impacting service availability for retail customers accessing payments, brokerage services or other banking applications. An extended period where banks' customers could not access their funds would, of course, be more serious.

Enhancing operational resilience is a regulatory priority around the world, including in Australia.¹⁹ Over the course of 2025, new regulation aimed at strengthening operational resilience has come into force across various jurisdictions, including the United Kingdom's *Critical Third Party* regime and the European Union's *Digital Operational Resilience Act*. Among other things, these frameworks seek to bring critical service providers within the regulatory perimeter, as part of broader efforts to strengthen operational risk management in the financial sector. In Australia, CFR agencies are actively working with industry to strengthen the operational and cyber resilience of individual financial institutions, as well as the system as a whole.²⁰

Endnotes

- 1 Resilient trade flows and strong growth in AI-related investment, as well as the effects of earlier monetary policy easing and fiscal policy support on domestic demand, had driven upward revisions to the outlook for several advanced economies. For further details, see RBA (2026), 'Chapter 3: Outlook', *Statement on Monetary Policy*, February.
- 2 See FSB (2025), 'FSB Chair's Letter to G20 Leaders', 20 November.
- 3 Bank of England (2025), 'Private Markets System-wide Exploratory Scenario', 4 December.
- 4 Bain and Company (2026), 'Global Private Equity Report 2026', Report, February.
- 5 A hyperscaler is a cloud service provider that offers scalable computing, storage and networking services via distributed data centre infrastructure, often used to support large scale applications such as AI.
- 6 Federal Reserve (2025), 'A Note on Recent Dynamics of Consumer Delinquency Rates', 24 November.
- 7 For details, see CFR (2025), 'Better Regulation Roadmap'.
- 8 FSB (2025), 'FSB Plenary Sets Out 2026 Work Plan', 19 November.
- 9 For further details regarding the local government debt-swap program, see Baird A, S Nightingale and G Taylor (2025), 'Behind The Great Wall: China's Post-pandemic Policy Priorities', *RBA Bulletin*, January.
- 10 See RBA (2025), 'Box: Demand and Supply Trends in Sovereign Bond Markets', *Financial Stability Review*, October.
- 11 Research by the US Federal Reserve indicates that hedge funds domiciled in the Cayman Islands are increasingly the marginal foreign buyer of US Treasuries, with the Cayman Islands now the largest foreign holder of US Treasuries. For further details, see Federal Reserve (2025), 'The Cross-Border Trail of the Treasury Basis Trade', 15 October.
- 12 FSB (2026), 'Vulnerabilities in Government Bond-backed Repo Markets', 4 February.
- 13 Following the announcement of a snap election earlier in the year, yields on long-end Japanese government bonds had risen sharply, driven by higher policy rate and inflation expectations due to the potential for further fiscal stimulus.
- 14 Bank of England (2025), 'Box C: Financial Stability Risks from the Impact of AI Development on Financial Markets', *Financial Stability Report*, December; BIS (2026), 'Financing the AI Boom: from Cash Flows to Debt', *BIS Bulletin*, 7 January.
- 15 RBA (2023), 'Leverage, Liquidity and Non-bank Financial Institutions: Key Lessons from Recent Market Events', *RBA Bulletin*, June
- 16 Equity holdings have grown to make up just under one-third of US household assets, but most of the contribution to this increase has come from the wealthiest 10 per cent of households. See IMF (2025), 'Chapter 1: Enhancing Resilience amid Global Trade Uncertainty', *Global Financial Stability Report*, 22 April. The European Central Bank (ECB) noted that households hold a considerable share of EU-domiciled equities. For details, see ECB (2025), 'Box 2: The Role of Household Investors in Market Downturns', *Financial Stability Review*, November.
- 17 The transmission of such shocks through to the domestic financial system can take place through several channels. For details, see RBA (2025), '4.1 Focus Topic: How Overseas Shocks Can Affect Financial Stability in Australia', *Financial Stability Review*, October.
- 18 For further details, see RBA (2025), '4.2 Focus Topic: Looking at Digitalisation through a Financial Stability Lens', *Financial Stability Review*, April.
- 19 See Bank of England (2025), *Financial Stability Report*, December; Federal Reserve (2025), *Financial Stability Report*, November; FSB (2025), 'Monitoring Adoption of Artificial Intelligence and Related Vulnerabilities in the Financial Sector', Report, 10 October.
- 20 CFR (2025), 'CFR Initiatives on Systemic Risks and Vulnerabilities', December.

Chapter 2



Resilience of Australian Households and Businesses

Summary

Households and businesses are generally well placed to weather higher interest payments and cost pressures. While the risk of a more material adverse global shock has increased over recent weeks, the strong financial position of most borrowers means that the household and business sectors are unlikely to be a source of systemic instability. Nevertheless, with domestic credit growth accelerating over the past year and global stability risks elevated, it is important that lending standards remain prudent so that household and business resilience is not undermined.

- **The financial position of most households and businesses is strong and cash flow pressures have eased relative to mid-2024 as inflation, and then interest rates, declined.** While some households continue to experience budget pressures, the share of mortgagors in severe financial stress – where mortgage payments and spending on essentials exceed their income – has declined since mid-2024 and is small. Loan arrears have remained at low levels, supported by strength in the labour and housing markets. Company insolvencies have stabilised at around longer run averages at an economy-wide level, although the share of companies entering insolvency remains elevated in the hospitality and construction sectors where the operating environment has been more challenging, particularly for smaller firms. Broader spillovers to the financial system from insolvencies have been contained due to these firms' limited bank debt and small size. Fundamentals continue to improve across most commercial real estate (CRE) markets and there is little evidence of financial stress among owners of Australian CRE.
- **Cash flow pressures on household and business borrowers are expected to increase in the near term, but most appear well placed to manage these.** The Monetary Policy Board increased the cash rate at its February and March meetings. This, alongside the forecasts presented in the February *Statement on Monetary Policy* (based on the market-implied cash rate path at that time), suggest that most households and businesses would see some deterioration in their cash flow positions over the next year or so as financial conditions tighten, inflation remains elevated and the unemployment rate edges higher. The escalation of conflict in the Middle East has also added further cost pressures. While this environment will be challenging for some households and businesses, the strong financial position of most borrowers is likely to limit the risk of widespread financial stress in response to higher inflation and interest rates, or if a significant economic downturn were to occur.

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- **The RBA, together with the other Council of Financial Regulators (CFR) agencies, will continue to closely monitor potential vulnerabilities in the household and business sectors that could emerge over time.** It is important that lending standards remain prudent and riskier forms of lending remain contained in the period ahead given the backdrop of high household indebtedness, recent strong credit growth and reports of strong competition among lenders. While overall lending standards remain sound, there is early evidence that some forms of riskier lending to certain household segments have ticked up recently alongside very strong investor housing credit growth. High debt-to-income (DTI) lending to investors has increased, though remains well below new limits activated by the Australian Prudential Regulation Authority (APRA) on high DTI lending. These limits support prudent lending standards by guarding against a material build-up of vulnerabilities from a more substantial increase in high DTI lending. High loan-to-valuation ratio (LVR) lending to first home buyers has also increased alongside the expansion of the Australian Government 5% Deposit Scheme in October last year. For businesses, financial conditions over the past year or so have eased alongside more vigorous lending competition among banks and non-banks, but there is little evidence that this lending poses a risk to financial stability.

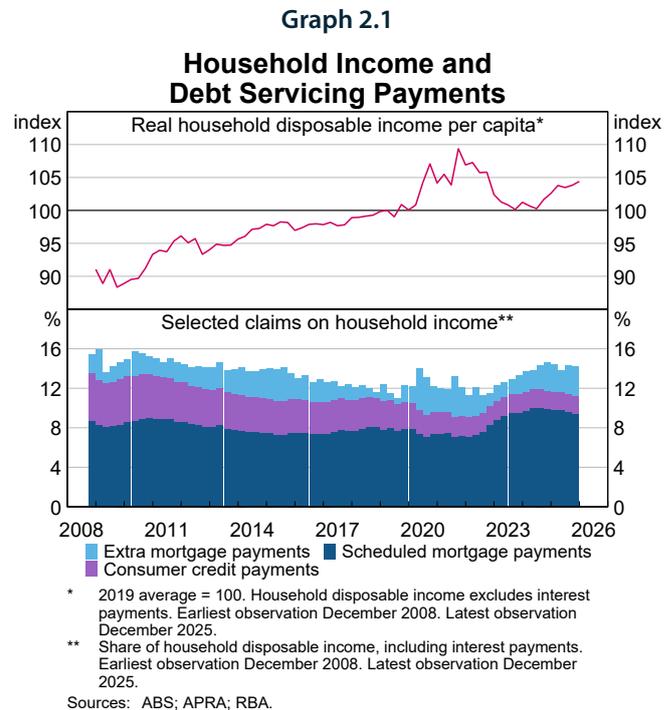
2.1 Households

The financial position of most Australian households is strong and budget pressures have eased relative to mid-2024.

Household cash flows have improved since mid-2024, reflecting the decline in inflation and interest rates and the Stage 3 tax cuts. Real

disposable income per capita – that is, income after tax and interest payments and adjusted for inflation – continued increasing steadily in 2025, after a notable pick-up over the second half of 2024 (Graph 2.1).¹

Scheduled mortgage payments declined over 2025 as cash rate reductions were passed through to lending rates, though remain higher as a share of household disposable income than before the pandemic. At the same time, households with mortgages have (in aggregate) continued to make extra payments into offset and redraw accounts, adding to their savings buffers. That said, experiences vary significantly across different household types with some having experienced materially more financial pressure. For example, lower income households, many of whom are renters, are more likely to experience financial stress as their essential expenses are a larger share of their disposable income and they tend to have lower savings buffers than other households.² Despite these differential experiences, personal loan arrears rates have remained around pre-pandemic levels and enquiries to services such as the National Debt Helpline have been broadly stable over the past year.

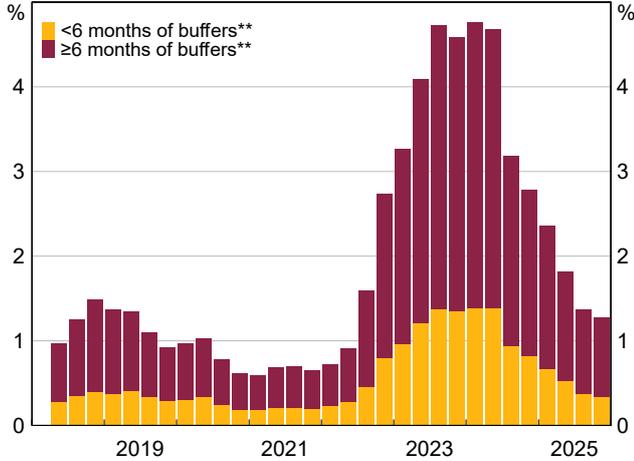


The vast majority of borrowers continue to have sufficient income to cover their scheduled mortgage repayments and essential expenses. The 50 basis point increase in the cash rate since the start of the year and increases in oil and gas prices over recent weeks stemming from the escalation of conflict in the Middle East are not estimated to have changed this picture materially. A little over 1 per cent of variable-rate owner-occupier borrowers were estimated to be experiencing a cash flow shortfall as at the end of 2025 (Graph 2.2).³ As lower inflation and interest rates have boosted real disposable incomes, the number of borrowers with a cash flow shortfall has declined notably since mid-2024.⁴ The share of borrowers at greatest risk of falling behind on their loan – those experiencing a cash flow shortfall that also have low prepayment buffers (lighter bars on Graph 2.2) – is around 0.3 per cent. Consistent with this, the share of loans in formal hardship arrangements has declined over the past year to be around pre-pandemic levels. The share of households that are persistently drawing down on their prepayment buffers has also declined over the past few years, though remains a bit above pre-pandemic levels.

Graph 2.2

Borrowers with Cash Flow Shortfall*

Estimated share of variable-rate owner-occupier borrowers



* Estimates of borrowers with minimum scheduled mortgage payments and essential expenses (HEM) exceeding their income. Excludes borrowers in arrears. Earliest observation June 2018. Latest observation December 2025.

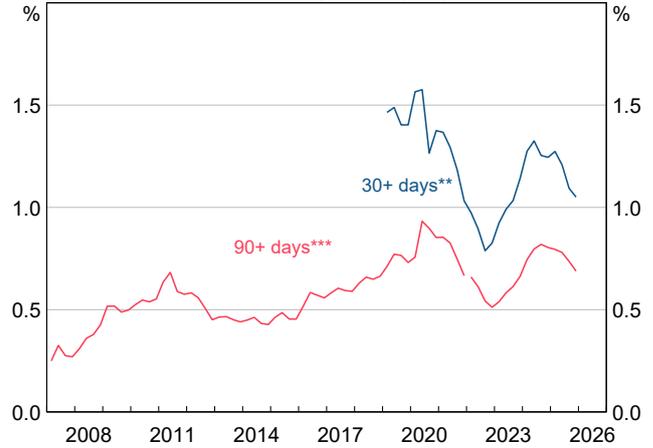
** Buffers expressed relative to borrower's cash flow shortfall.

Sources: ABS; Melbourne Institute; RBA; Securitisation System.

Graph 2.3

Housing Loans in Arrears*

Share of banks' housing credit by days past due



* Earliest observation March 2007. Latest observation December 2025.

** Series only available from March 2019.

*** Well-secured loans prior to March 2022; both well-secured and not well-secured loans thereafter.

Sources: APRA; RBA.

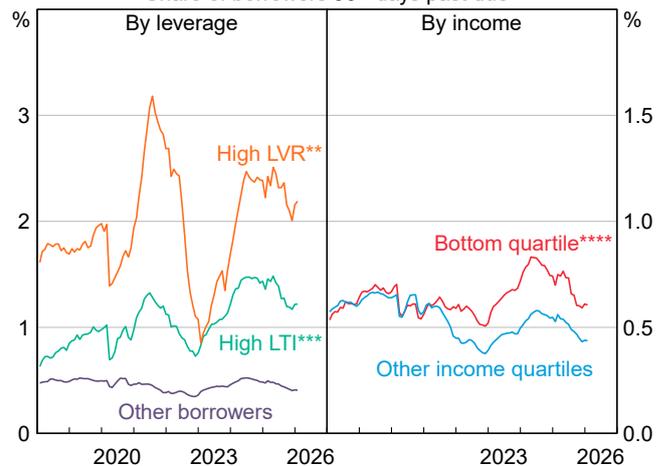
Housing loan arrears are low and have continued to decline.

The share of housing loans more than three months in arrears has declined over the past year, returning to around pre-pandemic levels (Graph 2.3).⁵ Arrears rates among highly leveraged and lower income borrowers have also declined over the past year; arrears rates among these borrowers tend to be higher than for others because they are more vulnerable than other borrowers to unexpected changes in interest rates, income or expenses (Graph 2.4). Low unemployment – and, in turn, the ability of workers to retain or find more work (including extra hours) and obtain wage increases – has supported households' ability to service their debts. While the unemployment rate has risen a bit over recent years, it remains low in the context of the past few decades. Conditions in the housing market have also been supportive; housing prices have increased by 18 per cent over the past four years, despite interest rates having increased by around 4 percentage points over that period. This has helped limit the share of borrowers with negative equity, giving more borrowers the option of making the decision – though difficult and disruptive – to sell their property to fully pay off their loan if they experience acute financial stress, rather than falling behind on their payments.

Graph 2.4

Arrears Rates by Risk Factor*

Share of borrowers 90+ days past due



* Variable-rate owner-occupier loans. Arrears rates in 2020 are affected by large changes in the composition of loans in the dataset due to the introduction of the Term Funding Facility. Earliest observation January 2016. Latest observation January 2026.

** LVR > 80 per cent based on current loan balance and estimated property value.

*** LTI > 4 based on current loan balance and estimated income.

**** Borrowers in the bottom quartile for gross household income (<\$118,000 for January 2026).

Sources: ABS; Cotality; RBA; Securitisation System.

Most households with mortgages appear well placed to weather a wide range of adverse economic outcomes.

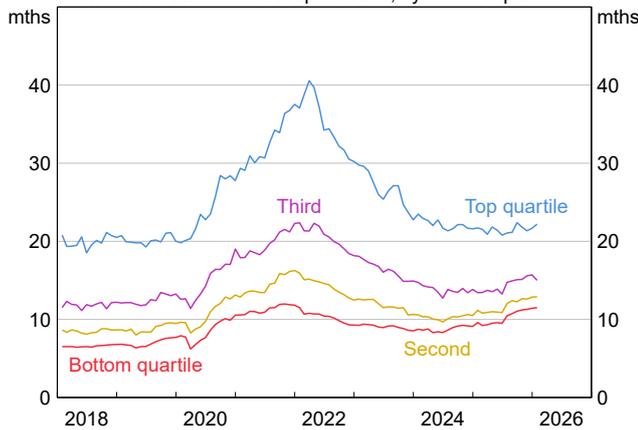
Most borrowers have large liquidity and equity buffers that can help them withstand shocks.

The median mortgage prepayment buffer (relative to a borrower’s minimum scheduled payments) is larger than prior to the pandemic for all income quartiles (Graph 2.5). Additionally, mortgagors’ equity positions are strong, with less than 1 per cent of households currently in negative equity – a meaningfully lower share than before the pandemic (Graph 2.6).⁶

Graph 2.5

Median Mortgage Prepayments*

Variable-rate owner-occupier loans, by income quartile

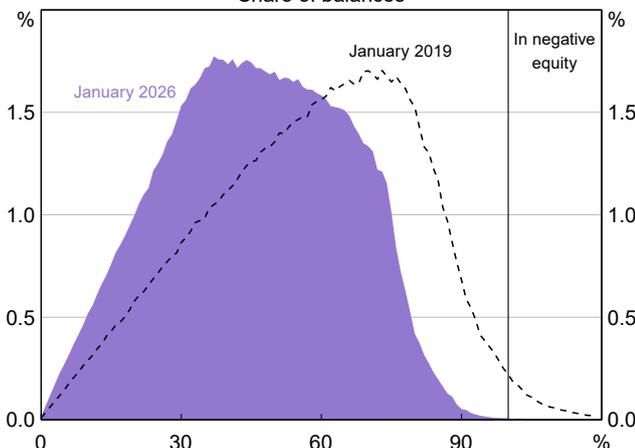


* Number of months that prepayments (offset and redraw balances) can cover minimum scheduled mortgage payments. Income quartiles based on the distribution of variable-rate owner-occupier borrower incomes. Income quartile upper bounds for January 2026 are \$118,000 for the bottom quartile, \$173,000 for the second quartile and \$248,000 for the third quartile. Earliest observation January 2018. Latest observation January 2026.
Sources: ABS; RBA; Securitisation System.

Graph 2.6

Outstanding LVR Distribution*

Share of balances



* Loan balances adjusted for redraw and offset account balances; property prices grown forwards using SA3 price indices.
Sources: ABS; Cotality; RBA; Securitisation System.

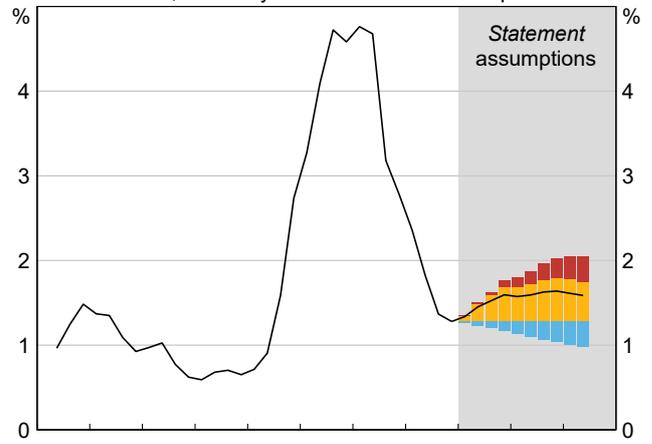
Pressure on existing mortgagors is expected to increase a bit based on projections in the February Statement, although these forecasts were produced before the escalation of conflict in the Middle East.

According to the RBA’s central forecasts in February (which were based on an increasing cash rate path in line with market expectations at the time), nominal wages growth is expected to support cash flows for many borrowers over the forecast period. However, this is expected to be partly offset by an increase in the unemployment rate and mortgage interest expenses. While the future path for interest rates (and the projections more generally) are uncertain, overall this outlook would imply a slight increase in the share of households facing acute budget pressures (Graph 2.7). However, any increase in the share of borrowers estimated to be experiencing a cash flow shortfall is unlikely to translate directly into increases in mortgage defaults given that very few of these borrowers would be at risk of depleting their liquid savings buffers over the forecast period.

Graph 2.7

Borrowers with Cash Flow Shortfall*

Estimated share of variable-rate owner-occupier borrowers, February 2026 Statement assumptions**



■ Real wages growth (after tax)*** ■ Cash rate**** ■ Unemployment

* Estimates of borrowers with mortgage payments and essential expenses (HEM) exceeding their income. Earliest observation June 2018. Projection to June 2028, based on borrowers not in arrears as at December 2025.

** The sum of the bars does not exactly equal the estimate (line) due to small interaction effects between the individual factors. Bars representing interaction effects are omitted from this graph.

*** Factor represents the growth of trimmed mean inflation and WPI.

**** Cash rate implied by market pricing as at February 2026 Statement.

Sources: ABS; Melbourne Institute; RBA; Securitisation System.

The vast majority of borrowers would remain able to service their debts under a range of adverse scenarios. Previous modelling suggests that large and increasing liquidity and equity buffers would enable most households to navigate a ‘trade war’ scenario,⁷ a significant deterioration in the labour market,⁸ or a period of higher-than-expected inflation and interest rates.⁹ Even when faced with a severe 40 per cent decline in housing prices, around 80 per cent of mortgagors are estimated to have positive equity. These borrowers would likely have enough equity to make the difficult and disruptive decision to sell their home and repay their loan in full if needed.

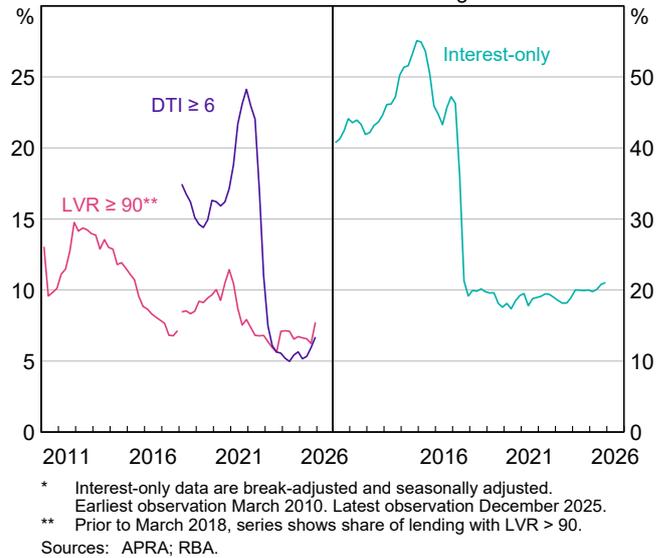
The RBA, together with the other CFR agencies, will continue to closely monitor potential housing-related vulnerabilities that could emerge over time.

Housing-related vulnerabilities currently remain contained, though credit growth has accelerated.

Lending standards have remained sound and riskier forms of lending – such as high DTI, high LVR and interest-only lending – are currently contained (Graph 2.8). It is important that lending standards remain prudent in the period ahead given the backdrop of high household indebtedness, recent strong growth in housing prices and credit, and reports from liaison with banks of heightened levels of competition for new lending. While growth in credit and housing prices is to be expected with the reduction in interest rates in 2025, this growth has been stronger than in most previous easing phases.¹⁰ It would be concerning if there was a material increase in risky lending because of loosening lending standards and/or in response to expectations of sustained strong housing price growth into the future; this could increase the risk, severity and macroeconomic implications of future shocks.

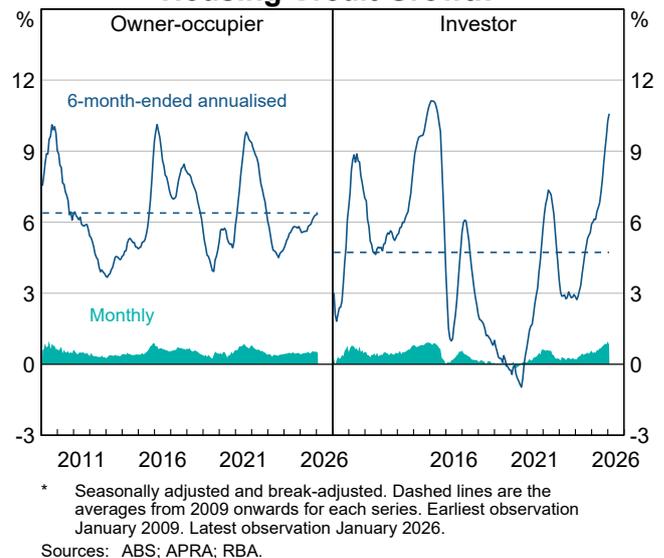
Heightened investor activity could lead to a build-up in financial vulnerabilities if it significantly amplified the housing credit and price cycle. Investor credit growth has been the primary driver of recent strength in housing credit (Graph 2.9). While investor activity tends to drive housing price dynamics to a greater extent than owner-occupier activity, heightened investor activity alone does not necessarily indicate that vulnerabilities

Graph 2.8
Housing Loan Characteristics*
Share of banks' new lending



are building; historically, investors have tended to be less likely to default than other types of borrowers in Australia.¹¹ However, it would be concerning if investor activity was to contribute to rapid and unsustainable increases in housing prices, leverage and/or an easing in lending standards as other borrowers attempted to enter a rising market. This would increase the economy's sensitivity to macroeconomic shocks.¹² However, as already noted, lending standards have remained prudent to date.

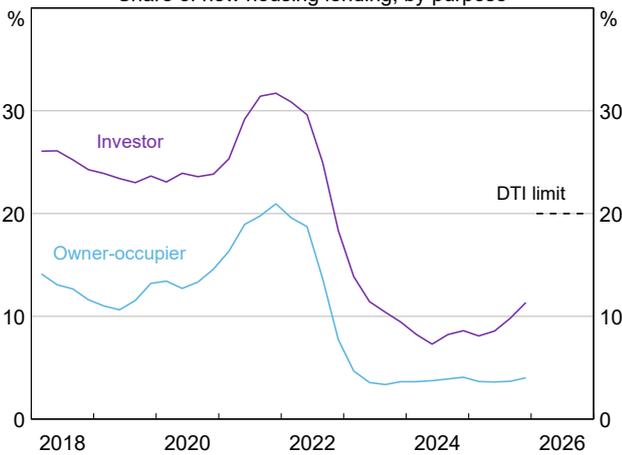
Graph 2.9
Housing Credit Growth*



The share of housing loans to investors with high DTI ratios has increased from low levels but remained well below APRA’s new limits on high DTI housing lending, prior to the limits taking effect in February 2026 (Graph 2.10). APRA’s new DTI limits support prudent lending standards by guarding against a material build-up of vulnerabilities from a more substantial increase in high DTI lending (see Box: What are APRA’s new DTI limits and how do they work?). The limits are assessed at the institution level with banks required to manage their share of lending at high DTI ratios for both owner-occupier and investor loans. All things equal, borrowers are able to take out and service larger loans relative to their incomes when interest rates are lower. As such, the current market expectation for the path of interest rates, while uncertain, suggests most banks are likely to remain below the new DTI limits in the near term.

Graph 2.10

High DTI Housing Lending*
Share of new housing lending, by purpose



* High DTI lending defined as DTI ≥ 6. Earliest observation March 2018. Latest observation December 2025.
Sources: APRA; RBA.

The share of high LVR lending has picked up recently, most notably among first home buyers, but still remains low overall. The increase in high LVR lending for first home buyers can be attributed to the Australian Government 5% Deposit Scheme, which allows eligible first home buyers to take out loans with a 5 per cent deposit without paying for lenders mortgage insurance.¹⁷ Information from the RBA’s liaison program suggests participation in the scheme has been strong. There is already some evidence that first home buyers are electing to take out larger loans relative to the value of their properties. Since October 2025, when the expanded scheme came into effect, the share of very high LVR borrowing has increased and borrowing at an LVR of 80 (above which lenders mortgage insurance (LMI) would otherwise be required without the scheme) has decreased (Graph 2.12).¹⁸ Although highly leveraged households are generally more vulnerable to shocks, which can lead to repayment difficulties, first home buyers have historically tended to experience more favourable labour market outcomes than other borrowers.¹⁹ More generally, scheme participants are unlikely to transmit stress to the broader financial system as the Government guarantees up to 15 per cent of the property value in the case of default. The expanded scheme may also have indirect effects if increased demand for housing encourages other borrowers to take on more debt than otherwise.

Graph 2.12

First Home Buyer Borrowing by Loan-to-Value Ratio
Share of banks’ new first home buyer lending



* Dashed line marks the beginning of the expanded 5% deposit scheme. Data from significant financial institutions collected on a ‘best endeavours’ basis. Earliest observation November 2023. Latest observation January 2026.
Sources: APRA; RBA.

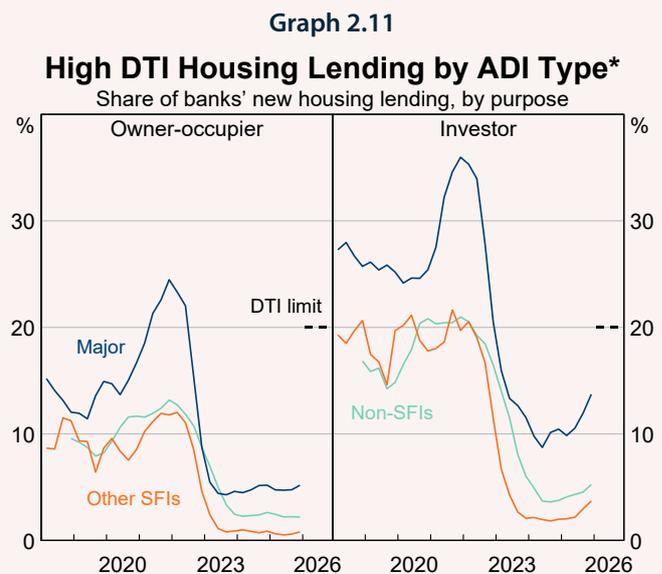
Box: What are APRA's new DTI limits and how do they work?

APRA activated DTI limits on 1 February 2026 as a guardrail to contain the share of lending to highly indebted housing borrowers. The new limits are intended to pre-emptively contain the build-up of housing-related vulnerabilities during periods of heightened risk, without overly constraining credit supply at other times.¹³ The limits allow no more than 20 per cent of authorised deposit-taking institutions' (ADIs) new mortgage lending to have a DTI ratio of six or more. These limits apply to owner-occupier and investor portfolios separately. The limits also include carve-outs to mitigate the direct effects on new housing supply and the smooth functioning of property transactions, and provide for proportionate treatment for smaller institutions.¹⁴

While APRA's new DTI limits are unlikely to be restrictive in the near term at the system level, they would have meaningfully constrained the supply of high DTI credit observed in some previous periods:

- When high DTI lending flows were around their peak in 2021 and 2022, growth in this riskier lending would have been notably restricted by the new DTI limits if they had applied at the time (Graph 2.11).¹⁵
- The new DTI limits would have also restricted high DTI lending to investors in 2018 and 2019, although they would not have meaningfully impacted on high DTI lending to owner-occupiers.¹⁶

APRA's new DTI limits are more likely to bind when rates are lower, on investors (compared with owner-occupiers) and on larger banks. Generally, DTI limits are more likely to bind when interest rates are lower, as a reduction in interest rates enables borrowers to take out loans at higher multiples of their income, all else equal. Vigorous lending competition can amplify this. Investors are able to borrow at higher DTI ratios than owner-occupier borrowers because they tend to have higher assessed borrowing capacities, with typically higher incomes, in part supported by rental incomes and associated tax deductions, including on loan interest expenses. Historically, a greater share of the major banks' new lending has a DTI ratio over six at origination, compared with other banks.



* High DTI defined as DTI \geq 6. Major and other significant financial institution (SFI) shares of high DTI lending are calculated quarterly, while non-SFI shares are calculated on a 4-quarter rolling average. Without accounting for exemptions on certain loan types. Earliest observation March 2018. Latest observation December 2025.

Sources: APRA; RBA.

2.2 Businesses

Cost pressures remain a challenge for some Australian businesses, as evident from higher insolvency rates in some industries, but risks to the financial system from business lending appear low.

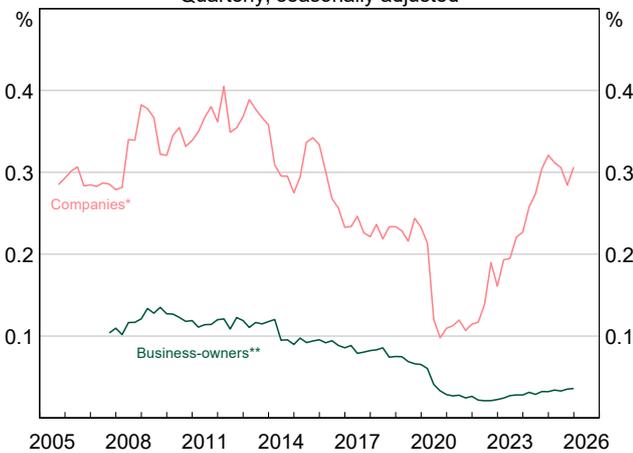
Total company insolvencies as a share of operating companies have stabilised over the past year, at around the longer run average (Graph 2.13).²⁰

Company viability has been supported by easing cash flow pressures for some companies and recovering domestic demand. The increase in total insolvencies over recent years from exceptional lows during the pandemic has reflected a catch-up effect following the removal of temporary support measures and challenging trading conditions.²¹

Company insolvency rates remain elevated in some industries, particularly hospitality and construction (Graph 2.14). This reflects ongoing wage and input cost pressures, as well as thin margins for some construction companies.

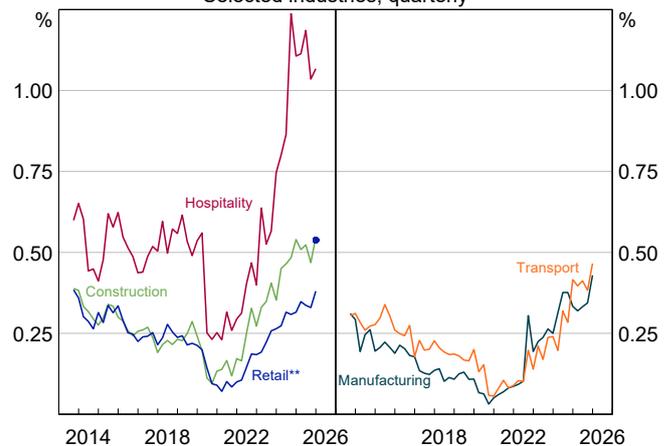
Consistent with this, information from the RBA’s liaison program suggests that the number of businesses seeking guidance from community organisations remains elevated in these industries. Support managing unpaid tax debt remains a common area of assistance in these cases, following recent further steps by the Australian Taxation Office (ATO) to resume enforcement actions on unpaid taxes. Consistent with this, the share of insolvent firms with large debts owing to the ATO has increased notably over the past three years.²² Insolvency rates are somewhat elevated among retail, manufacturing and transport companies, reflecting cash flow constraints, and labour shortages remain a constraint for some transport firms.²³ There is a risk that a sustained energy price shock adds to cost pressures, particularly in more energy-intensive industries such as transport. Personal insolvencies of business owners – many of whom are in the construction and hospitality industries – have also increased over the past few years, although from very low levels (Graph 2.13).²⁴

Graph 2.13
Business Insolvency Rates
Quarterly, seasonally adjusted



* Calculated as a share of operating companies; operating companies prior to September 2012 estimated using BLADE. Earliest observation September 2005. Latest observation December 2025.
** Calculated as a share of total operating businesses. Earliest observation September 2007. Latest observation December 2025.
Sources: ABS (BLADE); AFSA; ASIC; RBA.

Graph 2.14
Company Insolvency Rates*
Selected industries, quarterly



* Seasonally adjusted. Calculated as a share of operating companies in each industry; operating companies in 2025 estimated using 2024 growth rates. Earliest observation September 2013. Latest observation December 2025.

** The sharp increase in the retail insolvency rate in December 2025 largely reflects a large franchisee group that entered insolvency. The rate including all stores in the franchisee group is represented by the blue dot.

Sources: ABS (BLADE); ASIC; RBA.

Financial stability risks from company insolvencies remain contained. Banks’ exposure to insolvent companies remains limited, as most insolvencies to date have involved small companies or companies with little bank debt (Graph 2.15).²⁵ While insolvent companies in the manufacturing industry tend to be a bit larger in terms of debts owed to creditors and number of employees, they account for a much smaller share of total insolvencies. Consistent with this, while banks’ non-performing business loans (business NPLs) have increased over the past three years, they remain well below the highs seen during the global financial crisis (GFC), and have shown some signs of improvement more recently.²⁶ Banks are also well placed to manage potential losses, as more than half of their business NPLs are well secured (see Chapter 3: Resilience of the Australian Financial System). While very disruptive for the affected individuals, the indirect effects of insolvencies on the broader economy and financial stability – for example, through job losses at insolvent companies – have been limited by the small size of these companies and resilient labour market conditions helping most affected employees to quickly secure new employment.²⁷

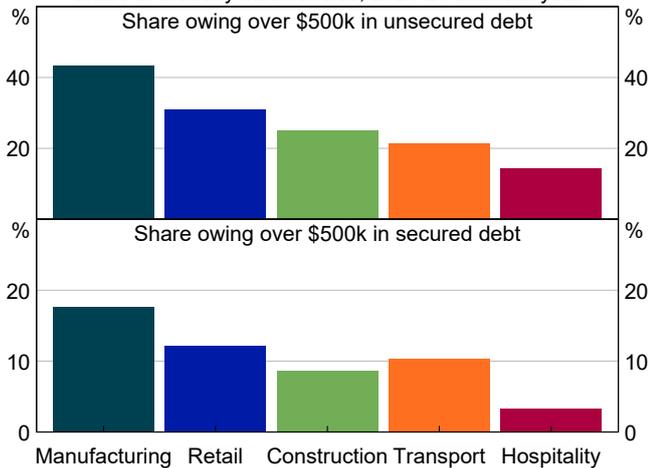
The business sector appears to remain financially resilient overall.

Most businesses’ operations remained profitable in mid-2025. Operating profit margins for small and medium-sized firms (SMEs) (which are calculated before deducting interest, tax, depreciation and amortisation expenses) are available up to the June quarter 2025 and were at that time around the levels recorded over the decade prior to the pandemic for most businesses (Graph 2.16). These data – which predate the latest escalation of the conflict in the Middle East and the associated increase in energy prices – suggest most firms had been able to slightly improve their operating margins, despite strong input cost growth over recent years. Consequently, the share of SMEs making operating losses has decreased over the past few years. While operating profit margins do not include interest expenses or debt management pressure (including unpaid ATO liabilities), which have contributed to insolvency trends, more recent survey measures also suggest that overall business conditions are around long-run averages, although conditions remain weaker in some sectors, such as retail and manufacturing.

Graph 2.15

Insolvent Company Debt*

Share of industry insolvencies, 2024/25 financial year



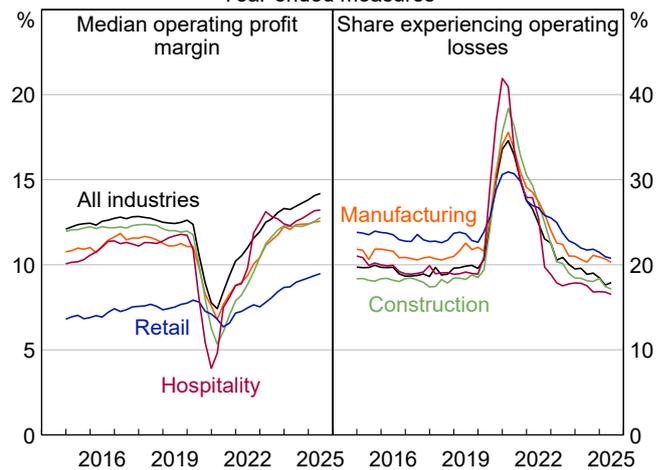
* Share of industry insolvencies at the point of insolvency. Data based on external administrator reports, which represent a subset of total company insolvencies.

Sources: ASIC; RBA.

Graph 2.16

SMEs Operating Profit Margins

Year-ended measures*



* ATO tax data of ~250,000 GST-remitting companies. Operating profits as year-ended operating revenue less operating costs and wages; not including government payments (e.g. JobKeeper); seasonally adjusted. Earliest observation December 2014. Latest observation June 2025.

Sources: ABS (BLADE); RBA.

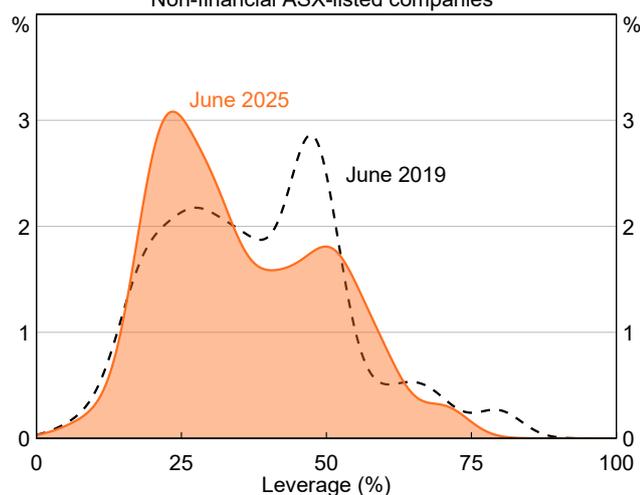
Larger businesses' balance sheets remained a little stronger than historical averages in 2025, which has improved their capacity to absorb shocks. Cash buffers of ASX-listed companies and bank deposits of larger SMEs remained above pre-pandemic levels, supporting their ability to navigate potential cash flow disruptions.²⁸ Aggregate corporate leverage also remains low, with the distribution of leverage across listed companies a bit lower than before the pandemic (Graph 2.17). This supports the ability of most companies to access liquidity from lenders or bond markets if required. Information on small businesses' leverage is limited, as many of them obtain loans by borrowing against the business owner's residential property. Nevertheless, continued housing price growth is likely to have supported their balance sheet position in these cases.

Lenders' ongoing appetite to lend to businesses has been supporting resilience, including for smaller businesses. Heightened competition for business loans over recent years as lenders seek to expand their business lending, including non-bank lenders, has supported credit availability for some businesses and reduced refinancing risks (see Chapter 3: Resilience of the Australian Financial System). Other factors, including automation of loan approval processes and more specialist non-bank and private credit lenders, have also improved small businesses' access to credit.²⁹ While strong business credit growth has not been associated with a broad decline in lending standards to date, the RBA, together with other CFR agencies, is monitoring this closely as it is important that this remains the case (see below).

Graph 2.17

Debt-weighted Leverage Distribution

Non-financial ASX-listed companies*



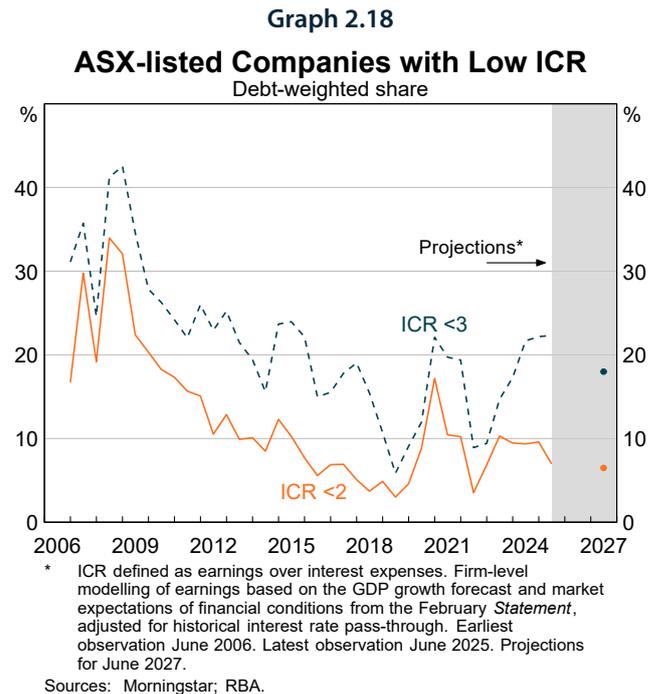
* Leverage defined as the ratio of total debt to total assets. Smoothed distribution, excludes the largest 2.5 per cent of leverage values.

Sources: Morningstar; RBA.

Cash flow pressures are expected to increase for some businesses over the period ahead due to increased costs stemming from the escalation of conflict in the Middle East and higher interest rates, though many businesses remain well placed to manage these.

Larger companies are expected to remain resilient to higher interest rates and cost pressures. Changes in borrowing costs typically take some time to pass through to interest expenses of larger firms because many of them issue fixed-rate debt or hedge their interest rate exposure.³⁰ The debt-weighted share of ASX-listed firms with a low interest coverage ratio (ICR) – historically associated with greater risk of insolvency – is projected to be little changed based on market expectations of increases in interest rates as of the February *Statement* (Graph 2.18).³¹ This reflects the forecast in the *Statement* that recent strength in GDP growth is likely to continue to support earnings in the near term. Moreover, this share is projected to remain low by historical standards and balance sheets generally remain a little stronger than normal suggesting that most larger companies would be resilient to tighter-than-expected financial conditions or weaker-than-expected demand.

Higher interest expenses and input costs are expected to increase cash flow pressures for some smaller businesses. Pass-through from a higher cash rate is likely to be quicker for small businesses than larger corporates. This is in part because many smaller businesses take out variable-rate business loans secured with a residential property mortgage. Stress relating to higher energy input costs is more likely to be concentrated in firms with very high energy intensities; in general, smaller firms are more likely to fall into this category, as are firms in the transport, mining, agriculture and utilities industries. However, if conditions were to evolve according to the central outlook from the February *Statement*, with stronger growth in private demand in the near term than previously expected and slower growth in unit labour costs, these may offset some cash flow pressures in the period ahead. The incidence of financial stress is expected to remain



higher for smaller businesses, particularly in the construction, hospitality and retail industries, because some of these businesses accumulated sizeable debts in recent years, such as unpaid GST collected on sales. Information from liaison suggests lenders expect some businesses will continue to experience cash flow pressure but are not expecting a significant increase in business NPLs.

Risks remain elevated given the escalation of conflict in the Middle East, heightened geopolitical tensions and international macro-financial uncertainties; an adverse shock could negatively affect some businesses, particularly in more export-intensive industries such as manufacturing and wholesaling.³² As a small open economy, large shocks to global demand or international trade, including shipping costs, would create stress among a range of Australian businesses. Mining, wholesale and manufacturing are the most export-exposed sectors in Australia, though the features of export-exposed firms in these sectors somewhat mitigate financial stability risks that could otherwise arise from overseas shocks.³³

Business credit growth remains strong and the RBA, in conjunction with other CFR agencies, continues to closely monitor for signs of a build-up in vulnerabilities.

While supply and demand for lending remain strong, overall lending standards remain sound.

Business credit has continued to grow strongly, with growth in recent years above its post-GFC average, though that was a period of relatively subdued business credit growth (Graph 2.19).³⁴ While data limitations make comparison of business lending standards over time challenging, liaison with lenders indicates there have been further incremental increases in their risk appetite to expand business lending over the past year, including to smaller business customers. Some adjustments to lending include a greater reliance on automated credit assessment processes, resulting in reduced documentation requirements. This has facilitated an increased supply of credit to some smaller businesses and self-employed borrowers. There has also been a slight easing in CRE lending standards over the past year (discussed below). Overall, however, there has been little evidence to date that the strong competition for business lending has led to a material decline in lending standards.

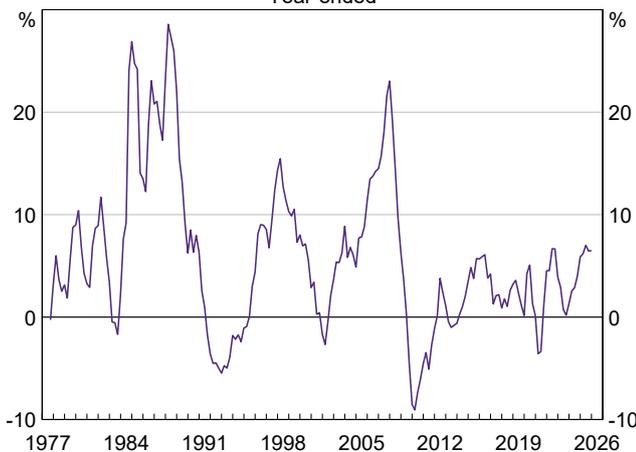
Leverage in the business sector remains relatively low and is not expected to pick up notably.

Historically, business leverage in Australia has tended to be more sensitive to the outlook for demand than financial conditions and the monetary policy cycle. Looking ahead, the recent increase in growth is expected to moderate further out based on projections in the February *Statement*. The recent pick-up in demand may support some businesses' appetite for increasing their leverage but does not appear strong enough to warrant expectations of a notable pick-up in leverage. The larger-than-normal cash buffers held by many large companies could provide a cheaper alternative to fund expansion in the near term than taking on external finance such as debt, though some firms may opt to retain cash due to uncertainty about their cash flow outlook.³⁵

CFR agencies are monitoring for any material erosion in lending standards that would lead to a build-up of vulnerabilities in the sector and undermine future resilience.

CFR agencies' monitoring of developments extends beyond regulated entities like banks to include business credit supplied by non-bank financial institutions (NBFIs). Information on some non-bank lenders, and in particular private credit firms, is more limited. If losses on private credit deals picked up, these would be passed through to their investors and potentially cause stress for those with large exposures. However, systemic impacts would likely be limited by the sector's small size (see Chapter 3: Resilience of the Australian Financial System).

Graph 2.19
Real Business Credit Growth*
Year-ended



* Earliest observation December 1977. Latest observation December 2025.

Sources: APRA; RBA.

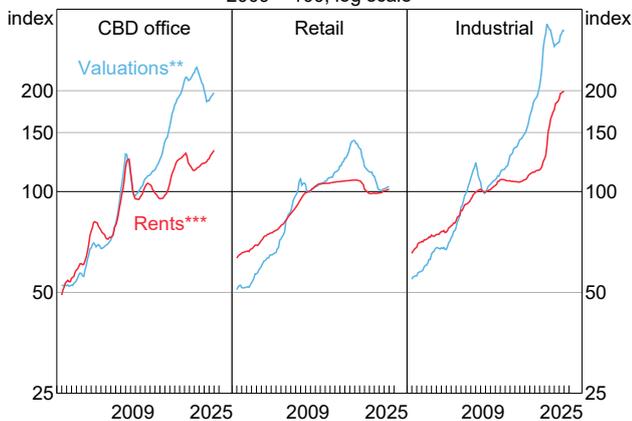
2.3 Commercial real estate

Fundamentals have continued to improve across most Australian CRE markets and there has been little evidence of financial stress among owners of CRE.

Fundamentals improved and valuations increased across most CRE markets over 2025 (Graph 2.20).

Demand for prime office space is supporting increased valuations and rents in the office sector. While some markets remain weaker – including lower grade office properties and those located in areas with high vacancies, such as parts of Melbourne – conditions in these markets have been stable. Valuations and rents are gradually rising in the retail sector, consistent with declining vacancy rates. In the industrial sector, higher valuations and rents have been primarily driven by the ongoing demand for warehousing and distribution centres.³⁶

**Graph 2.20
Commercial Property***
2009 = 100, log scale

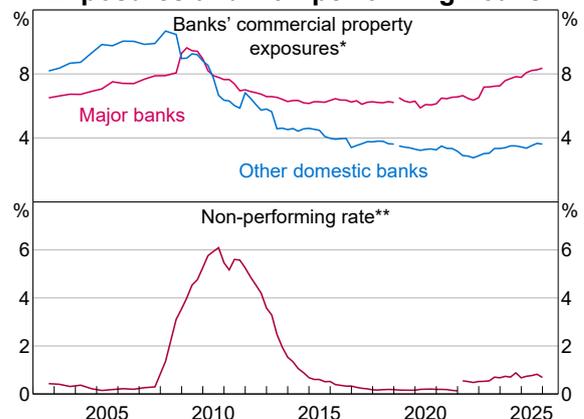


* CBD office and industrial are prime property; retail is regional (large) centres. Earliest observation December 1994. Latest observation December 2025.
 ** JLL Capital Value Indicator.
 *** CBD office is effective rents; industrial and retail are face rents.
 Sources: ABS; JLL Research; RBA.

There has continued to be little evidence of financial stress among owners of Australian CRE. Specifically:

- **ASX-listed A-REITs maintain solid financial positions.** Earnings have improved a little over the past couple of years and leverage remains stable, reflecting improved asset valuations. ICRs have improved a little over 2025, reflecting the pass-through of lower borrowing costs to interest expenses.
- **The share of banks' CRE loans classified as non-performing remains low by historical standards** (Graph 2.21). Liaison with banks suggests that CRE loan quality is expected to remain strong.
- **Liaison with non-bank lenders suggests that their loan performance also remains sound.** That said, visibility is limited, particularly among lenders with significant exposures to lower quality assets or riskier borrowers.

**Graph 2.21
Banks' Commercial Property Exposures and Non-performing Loans**

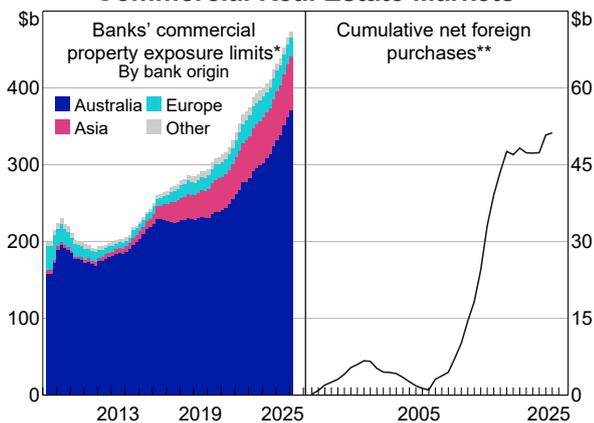


* Share of assets. Excludes overseas exposures and foreign banks. Series break in March 2019. Earliest observation September 2002. Latest observation December 2025.
 ** Share of commercial property exposures. Excludes overseas exposures. Prior to 2022, data reported as impairment rates. Earliest observation September 2002. Latest observation December 2025.
 Sources: APRA; RBA.

Australian CRE has been a relatively attractive asset class for investors. Domestic transaction volumes were strong in the industrial and retail sectors last year, which have contributed to improvements in valuations. Foreign banks continued to lend to owners of Australian CRE, and foreign investors have maintained their exposure with net foreign purchases increasing further in 2025 (Graph 2.22). Liaison with lenders exposed to CRE cite a number of factors for Australian CRE's attractiveness to overseas investors, including a stable economy, higher yields than some other markets (such as Europe) and a desire for geographical diversification. This has the potential to continue to support Australian valuations through inflows of foreign capital, except if these factors were to change.

Graph 2.22

Foreign Activity in Australian Commercial Real Estate Markets



* Total limits on facilities committed by banks. Earliest observation March 2008. Latest observation December 2025.

** Includes office, retail and industrial properties. Transactions greater than \$5 million. Earliest observation December 1988. Latest observation December 2025.

Sources: APRA; JLL Research; RBA.

Banks' exposures to CRE have continued to increase, but risks to the financial system remain contained.

After declining for more than a decade after the GFC, CRE loans have increased as a share of Australian banks' assets in recent years, driven by growth in lending by the major banks (Graph 2.21). However, liaison suggests a significant share of this has been increased lending to existing customers deemed by the banks to be lower risk, which has limited potential build-up of vulnerabilities. Consistent with this, the share of banks' CRE NPLs remains low and liaison contacts expect this to remain the case. Systemic risks from non-bank lenders also appear limited by the sector's small size (see Chapter 3: Resilience of the Australian Financial System).

Ongoing strong competition in CRE lending has contributed to some easing in lending standards and could undermine future resilience if it leads to a further and more material deterioration.

Competition in CRE lending remains strong from both bank and non-bank lenders, which has led to some easing in lending terms over recent years.

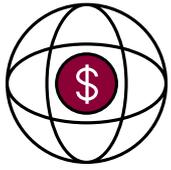
For instance, some lenders have loosened loan covenants, or lowered presale requirements for residential developments, although other terms generally remain unchanged.³⁷ Liaison with lenders has indicated they are instead more discerning on project fundamentals (including location) and by engaging with trusted builders and developers. However, information is more limited on lending by non-bank lenders, and private credit firms in particular, which are active in the sector. A further and more material easing in CRE lending standards would increase the risk that credit is extended to riskier borrowers, undermining the resilience of the sector.

Endnotes

- 1 For a discussion on the drivers of real disposable income growth over the past five years, see RBA (2025), 'Box B: Consumption and Income Since the Pandemic', *Statement on Monetary Policy*, February. Real household disposable income per capita is the preferred measure as it provides a broader view of resources available for consumption than wages. It captures all labour income, impact of tax changes, and exposure to interest components.
- 2 Data from the Household, Income and Labour Dynamics in Australia (HILDA) Survey show that in 2024, when real disposable income per capita was at its lowest post-pandemic level, the share of renters experiencing at least one incident of financial stress was around two times that of owner-occupiers.
- 3 The share of borrowers in cash flow shortfall is based on estimates for income and essential expenses. The Securitisation System records income when the loan is originated. To estimate current income, origination income is grown forward using the Wage Price Index. To estimate essential expenses, we use the Melbourne Institute's Household Expenditure Measure according to Greater Capital City Statistical Areas (GCCSAs), which allows essential expenses to vary across different geographic areas.
- 4 Cash flow shortfalls are estimated using minimum scheduled mortgage repayments based on outstanding interest rates. As many lenders do not automatically adjust repayments when rates fall, excess payments typically accumulate in offset or redraw accounts. It is assumed that borrowers in financial stress would reduce repayments to the minimum amount by contacting their lender.
- 5 While the share of housing NPLs has trended up over the longer term, it remains low and has not been accompanied by a corresponding increase in overall loan losses. See Chapter 3: Resilience of the Australian Financial System.
- 6 This estimate is based on the share of mortgagors or loans in negative equity, net of offset and redraw account balances. Banks typically report the share of loan balances in negative equity; estimates of negative equity on this basis are larger than the share of loans by number.
- 7 See RBA (2025), *Financial Stability Review*, October.
- 8 See RBA (2024), *Financial Stability Review*, September; RBA (2025), *Financial Stability Review*, October.
- 9 See RBA (2024), *Financial Stability Review*, March.
- 10 This does not necessarily mean that monetary policy transmission is stronger than usual in the current episode. Recent housing price strength is also likely to reflect the stronger starting position of the labour market compared with past episodes of easing monetary policy. Recent housing market activity may also have been supported by the expansion of the Australian Government 5% Deposit Scheme, although the size of this effect is uncertain. See RBA (2026), *Statement on Monetary Policy*, February.
- 11 However, investor loans may prove to be at greater risk of default in a severe downturn. In the United States, United Kingdom and Ireland, for example, investor loans became much riskier during crises. See Cassidy M and N Hallissey (2016), 'The Introduction of Macroprudential Measures for the Irish Mortgage Market', *The Economic and Social Review*, 47(2), pp 271–297; Zemaityte G, E Hughes and K Blood (2023), 'The Buy-to-let Sector and Financial Stability', Bank of England *Quarterly Bulletin*; Albanesi S (2022), 'A New Narrative of Investors, Subprime Lending, and the 2008 Crisis', in M Schularick (ed), *Leveraged: The New Economics of Debt and Financial Fragility*, Chicago University Press, pp 79–136.
- 12 This would reflect a combination of two mechanisms: (i) more highly indebted borrowers drawn into the market during the upswing in leverage are more likely to pull back on consumption in response to an adverse shock; and/or (ii) because amplifying the housing price cycle increases the risk that prices overshoot their fundamentals and then correct, weighing on consumption through the wealth effect. For a discussion of debt overhang effects in Australia, see Price F, B Beckers and G La Cava (2019) 'The Effect of Mortgage Debt on Consumer Spending: Evidence from Household-level Data', RBA Research Discussion Paper No 2019-06. Beyond consumption effects, highly indebted borrowers are also more likely to default.
- 13 See APRA (2025), 'Activating Debt-to-income Limits as a Macroprudential Policy Tool', November.
- 14 Bridging loans for owner-occupiers and loans for the purchase or construction of new dwellings for both owner-occupiers and investors are exempt from the DTI limits, though ADIs' high DTI investor lending share is unlikely to be materially impacted by these carve-outs. For significant financial institutions (SFIs) – banks with assets greater than \$20 billion or determined as such by APRA – compliance with the DTI limit will be assessed on a quarterly basis. For non-SFIs, compliance will be assessed on a four-quarter rolling window. See APRA, n 13.
- 15 With a 20 per cent high DTI lending limit, aggregated high DTI lending flows would have been around \$40 billion lower in the 2021/22 financial year, representing 2.1 per cent of total outstanding housing credit. Though banks would likely have implemented management buffers meaning the actual impact may have been higher. On the other hand, these estimates do not consider exemptions for bridging loans or the construction of new dwellings, or that some banks had capacity to absorb some of these excess flows and may have elected to do so, or more general adjustments by borrowers and banks. There may also have been spillovers of high DTI lending to non-ADI lenders.
- 16 If APRA's limit was in place in the 2018/19 financial year, it would have required lenders to reduce their high DTI lending by around \$10 billion, or 0.5 per cent of outstanding credit at the time.
- 17 Australian Government (n.d.), 'Australian Government 5% Deposit Scheme'.

- 18 First home buyers appear to be more deposit constrained than other borrowers, with a larger share historically taking out loans at 80 per cent LVR than other owner-occupiers or investors. This clustering at an LVR of 80 suggests that some first home buyers, when provided the choice, will opt to take out larger loans if they can avoid LMI (which generally adds around 1 to 5 per cent to the loan amount). Loan level data suggest that most first home buyers who took out LVR 80 loans over the past few years have ample room to increase their loan size without coming up against serviceability constraints.
- 19 Data from the HILDA Survey show that first home buyers experienced faster income growth than other owner-occupiers on average for a couple years before and after taking out their loan and were persistently less likely than other owner-occupiers of the same loan age to report job insecurity. See Alfonzetti M (2022), 'Are First Home Buyer Loans More Risky?', RBA *Bulletin*, March. Though it may be the case that the characteristics of previous first home buyers do not generalise to current borrowers participating in the scheme, given they face different constraints to enter the housing market.
- 20 The longer run average refers to the average total company insolvency rate calculated using data from 2005–2019. In cumulative terms, total company insolvencies have risen back to around their pre-pandemic trend. However, the pre-pandemic trend is a conservative benchmark because it does not account for strong growth in the number of operating companies over the past five years. Higher growth in the number of companies means that for a given insolvency rate, the absolute number of insolvencies will remain elevated above historical averages (even after detrending).
- 21 The catch-up effect over recent years reflects the removal of significant support measures introduced during the pandemic, including the ATO resuming enforcement actions on unpaid taxes. For more details, see RBA (2025), '4.3 Focus Topic: The Recent Increase in Company Insolvencies and its Implications for Financial Stability', *Financial Stability Review*, April.
- 22 The share of insolvent companies owing more than \$1 million in unpaid taxes has increased from around 5 per cent in June 2021 to 9 per cent in June 2025. Insolvent companies in manufacturing and construction industries tend to owe slightly larger unpaid taxes. For more details on the resumption of ATO enforcement actions, see RBA, n 21. Further, interest charged by the ATO for late payments are no longer tax deductible (as of July 2025). This change increases the cost associated with unpaid tax debt.
- 23 The pharmacy stores of the large franchisee group entering insolvency in December will continue to operate as the sale of the group is arranged.
- 24 Business owners includes both owners of companies and individuals acting as sole proprietors or in partnerships.
- 25 Around 75 per cent of companies that entered insolvency over the 2024/25 financial year had less than 20 full-time employees, and around 70 per cent had no debt owing to secured creditors (the type of debt most likely to be owed to banks).
- 26 Loans are typically classified as non-performing if payments are more than 90 days past due or if banks no longer expect to realise the full economic benefit of a loan, which generally includes when a business borrower enters insolvency. For more details, see RBA (2025), 'Box: The Recent Increase in Banks' Non-performing Business Loans', *Financial Stability Review*, October.
- 27 For more details, see RBA, n 21.
- 28 Latest available data include listed company buffers as at June 2025 and business cash deposits as at January 2026.
- 29 See Harvey N, S Lai and J Spiller J (2025), 'Small Business Economic and Financial Conditions', RBA *Bulletin*, October.
- 30 Indeed, latest available data show that average interest rates on outstanding listed company debt had still been increasing to June 2025 despite decreases to the cash rate over 2025.
- 31 An ICR of two is used as a threshold indicative of weaker debt servicing capacity and historically associated with an increased risk of insolvency; the dashed ICR <3 line in Graph 2.18 is shown as an additional sensitivity analysis.
- 32 See RBA (2025), '4.1 Focus Topic: How Overseas Shocks Can Affect Financial Stability in Australia', *Financial Stability Review*, October.
- 33 Australia's mining exports are produced by large firms that are relatively low-cost producers, which gives them a comparative advantage over overseas producers in the face of a negative shock to global demand. The mining sector accounts for less than 3 per cent of business credit, which should limit the transmission of financial stress to their domestic lenders. Around half of Australia's export-intensive firms are within the wholesale and manufacturing sectors, but account for just over 10 per cent of businesses within these industries on a revenue-weighted basis. While banks have sizeable exposures to the wholesale and manufacturing industries, only a proportion of these are to export-intensive firms and many of these loans are likely to be secured. Further, exporters tend to have somewhat stronger balance sheets than other firms, which can support their resilience to trade shocks. For more details, see RBA, n 32.
- 34 Growth has remained substantially lower than before previous large deteriorations in loan performance, such as the GFC and the 1990s recession; this is particularly the case in a real sense and relative to GDP, see RBA, n 10. See Jennison S, J Spiller and P Wallis (2026), 'Recent Changes in Credit Markets and Their Implications for Monetary Policy', RBA *Bulletin*, February.
- 35 See La Cava G and C Windsor (2016), 'Why Do Companies Hold Cash?', RBA Research Discussion Paper No 2016-03.
- 36 Industrial sector CRE data exclude data centres, which are classified separately but data are more limited. Investments in developing data centres in Australia have picked up strongly recently, supported by growing demand from global technology firms; liaison contacts expect this trend to continue in the years ahead.

37 In February 2025, APRA clarified that its 2017 letter on commercial property lending standards did not constitute minimum presale requirements. This guidance had previously been misinterpreted by some lenders as a requirement for qualifying presales equivalent to at least 100 per cent of committed debt. Some lenders interpreted this clarification as guidance supporting an easing in standards, though liaison contacts generally note lower presale requirements in the industry have been mainly driven by heightened competition and an optimistic outlook on the property market. See APRA (2025), 'APRA Clarifies Its March 2017 Letter Regarding Commercial Property Lending', February; APRA (2017), 'Letter to ADIs: Commercial Property Lending', March.



Chapter 3

Resilience of the Australian Financial System

Summary

The Australian financial system remains well positioned to continue providing services to Australian households and businesses in a range of scenarios, including a pick-up in inflation and/or a weakening of economic growth. There is a good degree of financial resilience in the system but it is important that lending standards remain strong so this resilience is maintained. At the same time, the global risk environment has deteriorated and remains challenging, with the potential for both financial and non-financial shocks to affect Australia. Enhancing operational resilience and crisis preparedness therefore remains a priority given the complexity of the operating environment.

- **Banks are well capitalised and have maintained prudent lending standards and provisioning.** Their financial positions are further supported by strong collateral values and holdings of liquid assets that exceed regulatory requirements, although regulators continue to discuss the suitability of liquidity risk frameworks. Strong credit growth has been accompanied by increased competition for lending both among banks and with other lenders. To date, this does not appear to have driven a material loosening in banks' lending standards or substantially reduced their profitability.
- **Credit extended by non-banks has been growing at a faster pace than for banks, though financial stability risks from non-bank lenders are limited by their relatively small size.** The sector plays an important role in the provision of finance in areas where banks tend not to compete. Lending by both traditional non-bank lenders and private credit has continued to grow strongly. While this could lead to higher loan losses in the future, the available evidence suggests that to date the strong pace of lending over the past year or so has not been associated with a material erosion of lending standards at the aggregate level.
- **The superannuation sector is a key, growing component of the financial system where building resilience remains a focus.** Ongoing strengthening of preparedness for liquidity and operational risk remain important to limit the potential role of the sector in amplifying shocks. The results of the first system risk stress test by the Australian Prudential Regulation Authority (APRA) demonstrate the importance of superannuation in a broad systemic stress event and inform ongoing work to strengthen resilience, including where multiple sources of risk materialise concurrently.
- **Strengthening the resilience of financial market infrastructures (FMIs) is a priority for financial stability.** Australian authorities continue to work with industry to strengthen the operational resilience of the Australian financial system as a whole. In addition, regulators remain focused on strengthening governance, capabilities and risk management at clearing and settlement facilities.

-
- **General insurance firms remain profitable and well capitalised.** The insurance sector is relatively small in terms of its share of financial assets in Australia, but it does play an important role in supporting the economic and financial resilience of domestic households and businesses. Home insurance affordability remains challenging and this could contribute to increasing underinsurance over time with the potential to undermine future resilience.

3.1 Banks

Banks' credit quality and collateralisation remains strong.

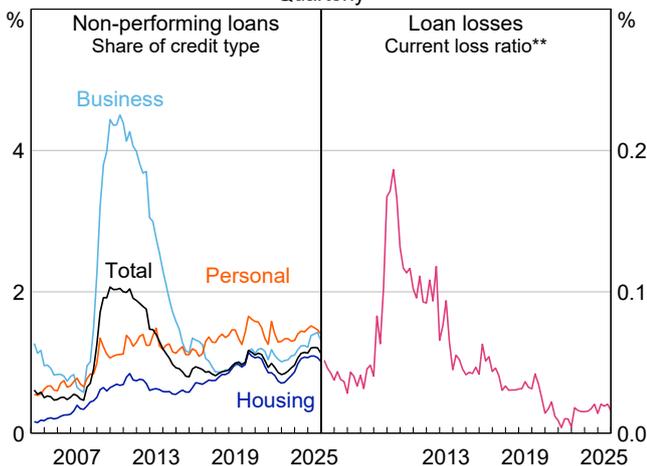
Credit quality stabilised in 2025, following a mild deterioration over the previous two years. The share of non-performing loans (NPLs) in total credit increased modestly but steadily from the low in 2022 to mid-2025 and has since stabilised well below the highs seen in the global financial crisis (GFC) (Graph 3.1). This stabilisation has largely been driven by housing loans, as earlier budget pressures from inflation and higher interest rates eased for some borrowers and unemployment remained low (see Chapter 2: Resilience of Australian Households and Businesses). The share of personal NPLs has also stabilised, although personal loans account for less than 3 per cent of total credit, a much lower share than prior to the GFC. Business NPLs increased slightly over 2025 and remain well below the highs seen during the GFC. The increase partly reflected lending to sole proprietors and partnerships, many of which are in the hospitality and construction sectors.¹

assess business cash flows as well as increased competition both among banks and from non-bank lenders and private credit. In some cases, banks have increased partially secured and unsecured lending, with measures of business and commercial real estate lending standards easing slightly. In liaison discussions with the RBA, lenders that have reported easing their own standards consider the easing to be incremental and prudent.

Loan losses have remained low by historical standards reflecting strong collateralisation and the relatively small increase in non-performing loans.²

Over 90 per cent of housing NPLs and over 50 per cent of business NPLs were considered well secured in December 2025 (Graph 3.2).³ This means that in most cases, even where a borrower is at risk of defaulting, the associated collateral can be sold to repay the loan in full. While this is highly disruptive and difficult where it involves the sale of a family home, it does limit the transmission of financial stress through the system. In addition, the increase in NPLs since 2022 has also been low compared with historical periods of more substantial losses, such as the early 1990s recession and the GFC.

Graph 3.1
Banks' Loan Performance*
Quarterly

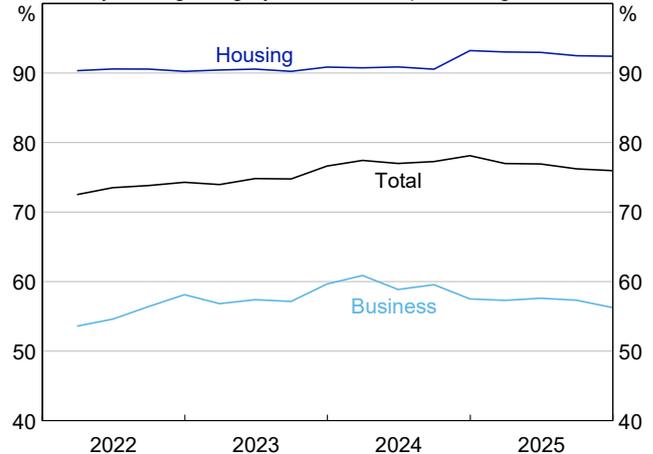


* Earliest observation 31 March 2004. Latest observation 31 December 2025.
** Write-offs made against provisions and directly to profit and loss over the quarter as a share of credit outstanding at the start of the quarter.
Sources: APRA; RBA; Rodgers (2015).

There has been strong growth and competition in business lending over recent years, but overall lending standards appear to remain prudent. Greater supply of credit to businesses has reflected the improvement in the ability of banks and other lenders to

Graph 3.2

Well-secured Non-performing Loans*



* Data on loan security only available from March 2022 onwards. Loans are considered 'well-secured' if the bank is confident that the value of the collateral securing the loan is enough to cover all amounts owed. Earliest observation 31 March 2022. Latest observation 31 December 2025.
Sources: APRA; RBA.

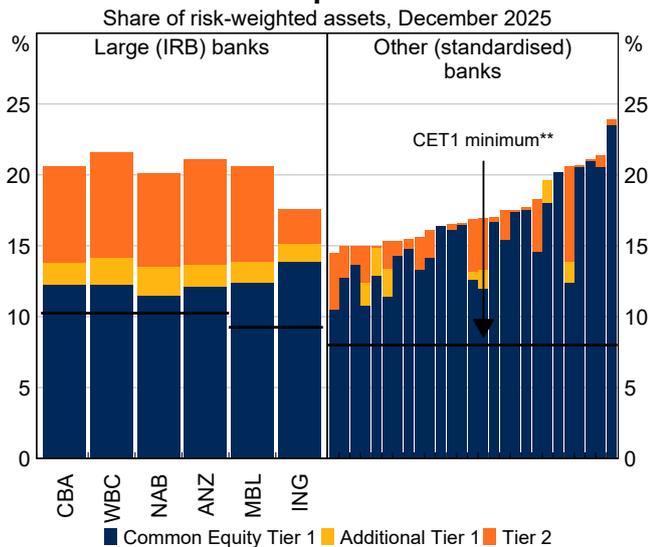
Australian banks remain well placed to support the economy even if a sharp economic downturn were to occur.

The high quantity and quality of capital in the banking system means it could absorb large losses while continuing to extend credit. The banking system’s ratio of Common Equity Tier 1 (CET1) capital – the highest quality of regulatory capital – to risk-weighted assets remained high and well above regulatory requirements at 12.3 per cent in December 2025 (Graph 3.3). Banks’ solid provisioning (at around pre-pandemic levels) and profitability add to their ability to absorb increases in loan losses. Australian banks are unlikely to face substantial direct losses arising out of exposures to the Middle East as they have very limited direct exposure to the region. Ongoing profitability could come under greater pressure if markets were to remain volatile and funding conditions tightened substantially as well as if elevated energy prices contributed to a meaningful deterioration in asset quality, but these developments would occur in the context of a banking system with a strong capital position.

Prospective regulatory refinements are consistent with maintaining the resilience of the banking system. APRA has proposed a simplified pathway for banks’ accreditation for the internal ratings-based (IRB) approach to calculating risk-weighted assets.⁴ This pathway aims to make IRB accreditation more accessible for medium-sized banks and was one of the commitments made in the Council of Financial Regulators (CFR) Review into Small and Medium-sized Banks.⁵ APRA is currently undertaking consultation on the proposed changes and expects to finalise the amendments in the first half of 2026. The phase out of Additional Tier 1 (AT1) capital instruments has also been finalised. The new framework applies from 1 January 2027 and AT1 instruments issued by banks are expected to be phased out by 2032.⁶ The new framework involves a slight reduction in the minimum leverage ratio from 3.5 per cent to 3.25 per cent to avoid an effective tightening of regulation that would have occurred due to the phase out of AT1 instruments. APRA does not expect this change to increase leverage in the banking system.

Graph 3.3

Banks’ Capital Ratios*



* Excludes foreign bank branches and banks with capital ratios exceeding 30 per cent.

** APRA may set higher requirements for institutions on a case-by-case basis.

Sources: APRA; RBA.

Banks hold large reserves of liquid assets and it is important they can be quickly converted into cash in a liquidity stress event.

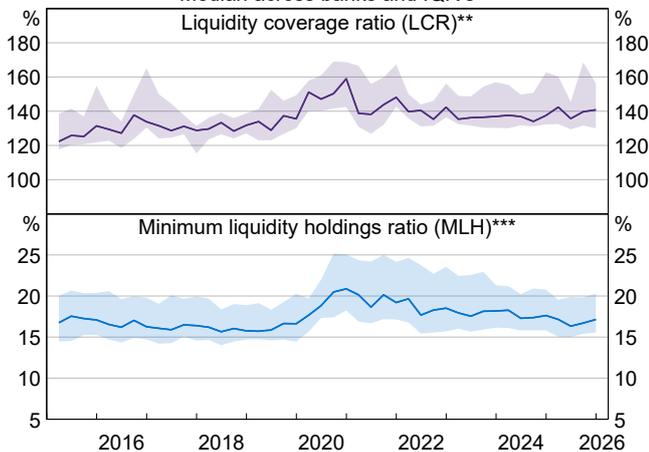
Banks retain large liquid asset holdings to cover a wide range of liquidity stresses. Banks' liquidity ratios measure holdings of specific highly liquid assets as a share of either total liabilities or potential outflows under a severe stress scenario. These ratios remain well above regulatory requirements, although regulators continue to discuss the suitability of liquidity risk frameworks in light of the rapid nature of deposit runs in the digital era (Graph 3.4).⁷ In addition, smaller and less complex banks, which are subject to the minimum liquidity holdings ratio requirement (MLH banks), have reduced the concentration of bank debt in their liquid assets, consistent with APRA's communication in July 2024 that MLH banks should further diversify their liquid asset portfolios. APRA still intends to consider liquid asset eligibility as part of an upcoming broader review of liquidity risk.

It is important that banks are ready to quickly convert assets that they hold for liquidity purposes into cash when necessary. Banks commonly seek to increase their holdings of Exchange Settlement (ES) balances substantially in times of liquidity stress. ES balances are cash balances held at the RBA that can be used to settle payments across the banking system. Under the RBA's 'ample reserves with full allotment' system, banks (and other eligible counterparties) can borrow as large a quantum of ES balances as they wish at weekly open market operations (OMO), secured by eligible collateral. This arrangement allows counterparties to increase their ES balances during a period of liquidity stress, supporting their resilience, and can forestall the need to engage in asset fire sales during periods where market functioning may be impaired. Other private market repo transactions can also be available to banks when seeking to monetise liquid assets. If eligible counterparties cannot find liquidity on suitable terms in private markets or via RBA OMO, they are expected and encouraged to use the RBA's overnight standing facility. The RBA and APRA consider the use of the overnight standing facility by banks to be consistent with routine liquidity management activities.⁸

Graph 3.4

Bank Liquidity Measures*

Median across banks and IQR's



* The LCR applies to the 13 largest and most complex banks in Australia. All other banks are subject to the MLH regime. Line refers to the median, ranges refer to the 25th and 75th percentiles. Earliest observation March 2015. Latest observation December 2025.

** LCR = High quality liquid assets / net cash outflows.

*** MLH = Liquid assets / liabilities.

Sources: APRA; RBA.

As Australian financial institutions face an increasingly complex risk environment, particularly from offshore, strengthening resilience is important.

The CFR is working to strengthen the system's resilience to geopolitical risk. In December 2024, the CFR agreed a multi-year inter-agency work program designed to ensure that the Australian financial system is prepared for a range of geopolitical scenarios. Over the course of 2025, CFR agencies engaged with large financial institutions on scenario analysis to ensure there is a clear understanding of the potential impact of adverse geopolitical events, and on the development of robust payment system contingency capabilities. CFR agencies have also strengthened engagement with relevant government agencies to support information sharing and response coordination. In addition, CFR agencies are integrating geopolitical considerations into routine supervisory activities, to ensure that regulated entities strengthen risk management and contingency planning.⁹

The increasing complexity of the risk environment warrants continuous improvement in managing operational risk alongside other risks. APRA's prudential standard on operational risk management, CPS 230, which commenced in July 2025, is assisting APRA-regulated entities to build resilience to operational risks and related disruptions. A key component is the requirement on entities to manage risks arising from the use of material service providers. Banks, superannuation funds and insurers rely on many third-party service providers throughout the technology supply chain. Some of the largest regulated entities have around 150 service providers supporting critical operations, with many providers used by multiple entities, if not the whole industry. Many of these are located overseas and outside of the Australian regulatory perimeter.¹⁰ APRA now requires entities to report their dependencies on service providers, which will enable a better understanding of where reliance on particular service providers is concentrated, to support better management of systemic risks. International and domestic experience, such as the cyber-attacks on Australian superannuation funds in April 2025 that coincided with tariff-related market volatility, also demonstrate the value of strengthening preparedness to deal with simultaneous operational and financial stress events.

3.2 Non-bank financial institutions (NBFIs)

Non-bank lenders have increased the availability of credit for both housing and business borrowers but risks to financial stability remain contained.

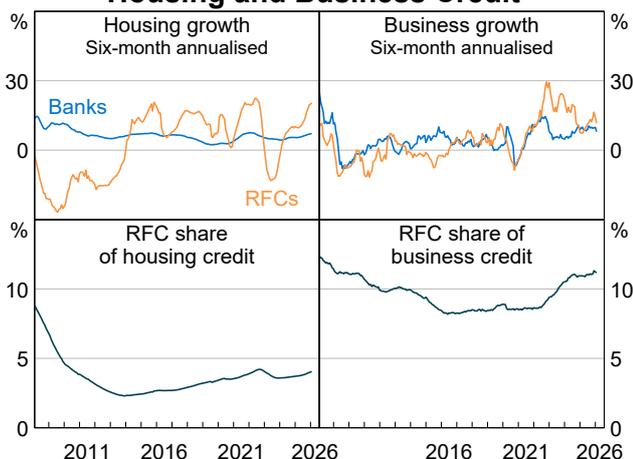
Non-bank lenders continue to grow as a source of finance in the Australian economy but their share of total credit remains relatively small. Growth in both business and housing lending by non-bank lenders – lenders that are restricted from offering deposits – has remained strong (Graph 3.5). This growth has been supported by favourable funding conditions for non-bank lenders in capital markets up to early 2026. Funding conditions tightened in March 2026 as financial market volatility picked up in response to the escalation of conflict in the Middle East. Despite the strong growth in their lending, non-bank lenders still only account for 6 per cent of financial system assets, limiting their systemic importance. Private credit has continued to grow strongly. Nevertheless, available estimates suggest private credit remains a small part of the overall financial system, accounting for less than 2 per cent of assets in the financial system.¹¹

Liaison suggests there has been some easing in lending standards by non-bank lenders, but to date this appears to have been modest. The most notable, though still modest, easing is reported to have been for property developers, including less stringent presales requirements and some reduced collateral requirements (see Chapter 2: Resilience of Australian Households and Businesses). However, this has not led to a substantial deterioration in asset performance to date. The available data suggest the share of non-bank housing lending in arrears remains a little below 1 per cent, which is only slightly above the share at banks. While there is limited visibility of business loan performance for non-bank lenders, liaison suggests arrears rates have increased slightly but remain contained.

The Australian Securities and Investments Commission (ASIC) finalised its review of public and private markets in November 2025, finding varied strength in practices in the private credit funds management sector. Private markets play an important role in funding growth and innovation in the economy, but limited visibility over activity in these markets restricts the ability of regulators to assess (and respond to) risks that could emerge in a timely way. ASIC has issued a roadmap of work and stakeholder engagement over the next 12–18 months to uplift practices in the private credit sector, improve data and transparency on managed investment funds including on private credit funds, promote strong practices by superannuation trustees, and foster the attractiveness, competitiveness and integrity of Australia’s public markets.¹²

Graph 3.5

Housing and Business Credit*

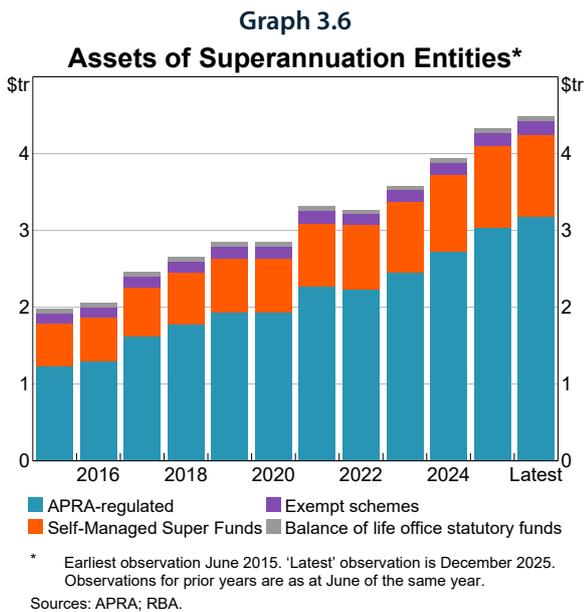


* The Registered Financial Corporations (RFCs) series includes non-bank lenders with more than \$50 million in assets (including lenders consolidated within banking groups), and does not include superannuation funds or insurers. Earliest observation January 2008. Latest observation January 2026.

Sources: APRA; RBA.

The superannuation sector is a key, growing component of the financial system where building resilience remains a focus.

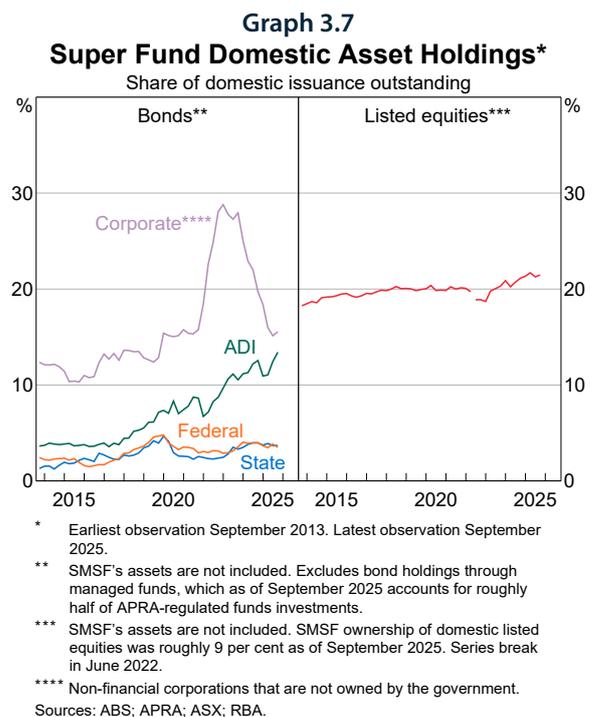
The superannuation sector is large and will continue growing for many years. The value of assets managed by the superannuation sector reached \$4.5 trillion in December 2025, representing around 160 per cent of GDP and one-third of Australian financial system assets (Graph 3.6). Assets under management are expected to continue increasing until at least the 2050s, after which the growing share of assets held by members in retirement could start to drive net outflows from the superannuation system in aggregate.¹³ As superannuation funds continue to grow, they will own an increasing share of Australian financial assets and allocate more of their funds to offshore markets.



Superannuation funds have been a source of financial system stability in the past, but could have the potential to amplify stress under severe scenarios in the years ahead. The long-term investment mandate and growing pool of savings in superannuation generally position the industry to provide a stable source of funding through periods of market-wide stress. Employers' compulsory superannuation contributions (at least 12 per cent of wages since 1 July 2025) ensure steady net fund inflows and fund members are generally restricted from withdrawing funds until retirement or a specific,

qualifying age. Most assets in the system are managed under 'defined contribution' programs, which means members bear the market risk on investments rather than superannuation fund trustees. So unlike in 'defined benefit' programs, which are more common overseas, trustees do not face a mismatch between returns on investment and payments owed to members. This reduces financial stability risks, though means that fund members exiting the system or withdrawing funds, and particularly those in retirement, may be exposed to market volatility. Overall, however, the system supports saving and thus resilience of households, contributes an important source of long-term funding to businesses, and mitigates risks to the government balance sheet from an ageing population. Further, around two-thirds of superannuation assets are managed by APRA-regulated funds, which are restricted from taking on direct borrowing.

At the same time, there is still the potential for a severe stress event to result in superannuation funds seeking to raise liquidity in ways that could inadvertently amplify system-wide stress. This includes by engaging in asset fire sales at the same time as much of the rest of the market if they misjudge their liquidity needs for extreme-but-plausible shocks. APRA-regulated funds hold a significant share of domestic financial assets (Graph 3.7).¹⁴



Managing liquidity risk will become increasingly important as the superannuation sector continues to grow and increasingly provides income streams to a greater number of Australians in retirement.

APRA's recent system risk stress test highlighted the critical roles and interconnections between financial institutions, including superannuation funds.

The exercise has provided insights about issues that will become more important as superannuation in Australia grows and evolves. The test found that the largest banks and superannuation funds were able to maintain or raise liquidity under a specific severe-but-plausible shock to financial markets and the domestic economy, accompanied by an operational disruption. However, it also showed that liquidity stress at individual banks could arise from super funds (alongside other entities) rapidly withdrawing funding. Notably, differing assumptions were made by participants, both within and across industries, when responding to the shock. Phase 2 of the system risk stress test will investigate these issues further, with a final report due to be published in mid-2026. Foreign exchange hedges will also likely require increasing management from superannuation funds as they deploy more capital abroad, and a larger share of this capital is directed toward fixed income assets as more members approach retirement.

Another priority is that industry strengthen operational resilience and preparedness for events where multiple sources of stress occur at the same time.

The simultaneous financial market volatility and cyber-attacks in April 2025 and the insights from the APRA system risk stress test highlight the importance of preparing for complex, interconnected stress events.¹⁵ In addition, superannuation funds' operational systems will be required to manage more frequent contributions when Payday Super is introduced.¹⁶ Operational vulnerabilities arise from ongoing digitalisation and the superannuation sector's reliance on a limited number of service providers for some critical functions, some of which are located offshore beyond the Australian regulatory perimeter. Outsourcing to specialist providers can have important benefits, but associated vulnerabilities need to be managed well. Strengthening operational resilience and governance practices across the superannuation sector is a regulatory priority to preserve the best interests of members, reduce the risk of disruptions and maintain trust in the system.

Strengthening the resilience of FMIs is a priority for financial stability.

While safe and efficient FMIs contribute to maintaining and promoting financial stability and economic growth, they also concentrate risk.

The functioning of Australia's financial system is supported by FMIs such as individual payment systems, central counterparties and securities settlement facilities that facilitate the clearing, settlement and recording of payments and other financial transactions. A prolonged outage at an FMI, or one occurring alongside other system-wide stresses, could damage confidence in the financial system with the potential to disrupt financial markets or amplify existing stresses. For example, if an operational disruption to payments results in a delay to a financial institution receiving funds it was relying on to settle other obligations, it may need to liquidate other investments quickly to be able to meet its obligations. This situation could impact liquidity and potentially lead to fire sale dynamics in asset markets, thereby transmitting stress more broadly in the financial system. In recognition of the important role that FMIs play, international standards have been developed for managing risks and ensuring efficiency and transparency at systemically important FMIs.¹⁷ ASIC and the RBA are responsible for implementing these international standards in Australia.¹⁸

FMIs often rely on complex, and sometimes ageing, technology with a high degree of interdependence among participants and service providers.

FMIs are networks, which by their nature create interdependencies among participants. In addition, FMIs and their participants often outsource critical services to specialist providers to reduce costs and keep up with technological changes. There is also a mix of new and old technological infrastructure supporting the financial system that need to interact with each other, so industry-wide coordination is often required to implement technological enhancements.¹⁹ Concentration in particular FMIs or providers, with sometimes limited substitutability or interoperability of services, exposes payments and other financial transactions to risks from single points of failure. While it was largely resolved within the day and did not have financial stability implications, the RBA operational incident on 27 January illustrates the central role played by the RBA as an operator of interbank settlements.²⁰

Similarly, the prolonged power outage in Spain in 2025 demonstrated how the dependence on electricity and telecommunications could disrupt payments.²¹ Vulnerabilities are growing over time, as geopolitical fragmentation poses risks to the continuity of offshore services, and technological changes have the potential to add further complexity to the infrastructure supporting the financial system.²² Australian authorities are leading a number of initiatives to mitigate these vulnerabilities (see Box: Initiatives to enhance operational resilience in Australia).

ASX, the operator of a number of systemically important FMIs in Australia, remains under heightened regulatory scrutiny. Following a string of operational issues and mounting concerns from regulators, ASIC launched an Inquiry into ASX in July 2025. The Inquiry panel has been tasked with reviewing ASX's governance, capabilities and risk management. It issued the following interim findings in late 2025:

- The resiliency of critical market infrastructure has been compromised to deliver high shareholder returns.
- Governance arrangements fail to provide the necessary focus on critical market infrastructure.
- ASX lacks the aspiration to be a steward of critical market infrastructure.
- Capability and cultural barriers are hindering transformation change at ASX.
- The current regulatory approach has not delivered the desired outcomes.

Based on these findings, ASIC, with support from the RBA, has obtained ASX's commitment to a package of reforms including a \$150 million capital charge, changes to strengthen the independence and governance of clearing and settlement facility boards, a strategic reset of ASX's Accelerate transformation program and a commitment to stronger leadership. The Inquiry panel's final report is due to be delivered to ASIC by 31 March 2026. Regulators are also currently undertaking a review of the regulatory engagement model.

The general insurance sector is not currently a source of financial stability concern, but declining home insurance affordability could undermine resilience in the longer term.

The general insurance sector has remained well capitalised and profitable. The sector's capital ratios were well above APRA's prescribed capital amount in December 2025. Profits have been supported by growth in premiums, strong investment results and a softening reinsurance market, but margins have come under some pressure from extreme weather events.²⁶

Home insurance affordability remains a challenge and could have systemic implications over time. Further decreases in the affordability of insurance could increase underinsurance, lowering the credit quality of existing mortgage loans. APRA's Climate Vulnerability Assessment will help to quantify how general insurance affordability may be impacted by climate change in the medium term, with the results due to be released in mid-2026.²⁷

Box: Initiatives to enhance operational resilience in Australia

Australian authorities continue to take steps to strengthen the operational resilience of the Australian financial system as a whole:

- The RBA is also strengthening its operating model to better support the critical payments settlements system, including by enhancing its cybersecurity controls and modernising core technology infrastructure.²³
- The Payments System Board, which is responsible for exercising the RBA's payment system policy in a way that (among other things) best contributes to controlling risk in the financial system, has identified strengthening the resilience of the payments system as one of its strategic objectives. The RBA has a program of work aimed at identifying system-wide vulnerabilities to Australia's payments system.²⁴
- Under the Industry Resilience Initiative, APRA and the RBA are overseeing work by key financial institutions and infrastructure operators to enhance industry-wide response capabilities to significant payments system disruptions.
- The RBA is collaborating with government agencies and members of the payments industry to address recommendations relating to incident coordination, which were identified from the tabletop cyber-attack simulation exercise hosted by the RBA in 2024.
- The *Security of Critical Infrastructure Act 2018* was recently amended to expand and strengthen government powers to respond to cyber, physical and operational threats impacting critical infrastructure. A further independent review of the Act has recently concluded, with recommendations anticipated to be released in the coming months.
- The CFR's Cyber Operational Resilience Intelligence-led Exercises program, led by the RBA, continues to assist in raising cyber resilience testing capabilities and highlighting cyber resilience strengths and weaknesses across systemically important financial institutions and market infrastructures. The program has now increased its resources to provide a more comprehensive view of the cyber threat landscape to participants and to test a larger number of entities each year.
- The RBA and other CFR agencies also continue to participate in a wide range of crisis response exercises, including whole-of-government scenario exercises designed to strengthen cross-agency, government and industry coordination and enhance industry resilience to large-scale cyber-attacks.

The International Monetary Fund (IMF) will independently assess the cyber resilience of the Australian financial system this year, as part of its Financial Sector Assessment Program.²⁵ This will help to inform the Australian authorities' ongoing work to strengthen the operational resilience of the Australian financial system.

Endnotes

- 1 See RBA (2025), 'Box: The Recent Increase in Banks' Non-performing Business Loans', *Financial Stability Review*, October.
- 2 For information on the calculation of loan losses, see Rogers D (2015), 'Credit Losses at Australian Banks: 1980–2013', RBA Research Discussion Paper No 2015-06.
- 3 A loan is considered well secured if the bank judges that the fair value of any collateral (after accounting for the costs involved in taking possession of and selling the collateral) is sufficient to cover the outstanding loan balance, including any accrued interest and fees.
- 4 The IRB model is one of two methods to calculate credit risk-weighted assets under Basel III; the other is a standardised model. The IRB model is more complex, granular and precise, and can allow for lower risk-weighted assets given improved risk management practices. For more information, see APRA (2025), 'A New Pathway to Internal Ratings-based (IRB) Accreditation for Medium-sized ADIs', Consultation, October.
- 5 CFR (2025), 'Review into Small and Medium-sized Banks', Report, July.
- 6 AT1 instruments are hybrid bonds intended to help absorb bank losses in stress supporting recovery or orderly resolution through reductions in coupon payments or conversion to equity. For more information on the phase out of AT1, see APRA (2025), 'Improving the Effectiveness of Additional Tier 1 Capital Instruments', Consultation, December.
- 7 The Basel Committee on Banking Supervision's report on its post-2023 liquidity work program highlights the need to recalibrate liquidity requirements in light of increased digitalisation and to subject them to regular stress testing. The report also underscores the importance of banks' operational readiness to access central bank liquidity facilities. In response, several central banks in advanced economies are exploring ways to improve the availability of these facilities and reduce the stigma associated with their use. See BIS (2024), 'The 2023 Banking Turmoil and Liquidity Risk: A Progress Report', October.
- 8 APRA and RBA (2025), 'Joint APRA-RBA Statement on Use of the RBA's Overnight Standing Facility', Media Release No 11-2025, 2 April.
- 9 CFR (2025), 'CFR Initiatives on Systemic Risks and Vulnerabilities', December.
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- 13 Deloitte's SPROUT model (2024) and Treasury's MARIA microsimulation (2019) both expect growth to continue into the 2050s.
- 14 See RBA (2025), 'Box: Interconnections Between Australian Banks and Non-bank Financial Institutions', *Financial Stability Review*, October.
- 15 See RBA (2025), 'Box: April Market Volatility', *Financial Stability Review*, October.
- 16 Australian Treasury (2024), 'Payday Super', Factsheet, September.
- 17 BIS Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions (2012), *Principles for Financial Market Infrastructures*, April.
- 18 RBA and ASIC (2013), 'Implementing the CPSS-IOSCO Principles for Financial Market Infrastructures in Australia', February.
- 19 For example, the proposed decommissioning of the Bulk Electronic Clearing System (BECS), Australia's primary system for account-to-account payments. See RBA (2025), 'Decommissioning of the Bulk Electronic Clearing System: RBA Risk Assessment', March.
- 20 RBA (2026), '27 January Payments Settlements Outage', Report, February.
- 21 Cremades, L, Á Esandai, M Pérez (2025), 'Impact of the 28 April 2025 Blackout on Spain's Payment Systems', *Banco de España Financial Stability Review*, Issue 49, Autumn.
- 22 Jones B (2025), 'Resilience, Innovation and the Future of the Payments System', Speech at the AusPayNet Summit 2025, 16 December.
- 23 RBA (2025), 'Corporate Plan 2025/26', August.
- 24 RBA (2025), 'Payments System Board Annual Report', September.
- 25 The Financial Sector Assessment Program is a comprehensive and in-depth assessment of a country's financial sector. In advanced economies, the IMF focuses on assessing the resilience of the financial sector, the quality of the regulatory and supervisory framework, and the capacity to manage and resolve financial crises.
- 26 Insurance Council of Australia (2026), 'Extreme Weather Cost \$3.5 Billion in 2025', Media Release, 23 January.
- 27 APRA (2025), 'APRA Corporate Plan 2025-26', August.

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The results of these studies are based, in part, on data supplied to the ABS under the *Taxation Administration Act 1953*, *A New Tax System (Australian Business Number) Act 1999*, *Australian Border Force Act 2015*, *Social Security (Administration) Act 1999*, *A New Tax System (Family Assistance) (Administration) Act 1999*, *Paid Parental Leave Act 2010* and/or the *Student Assistance Act 1973*. Such data may only be used for the purpose of administering the *Census and Statistics Act 1905* or performance of functions of the ABS as set out in section 6 of the *Australian Bureau of Statistics Act 1975*. No individual information collected under the *Census and Statistics Act 1905* is provided back to custodians for administrative or regulatory purposes. Any discussion of data limitations or weaknesses is in the context of using the data for statistical purposes and is not related to the ability of the data to support the Australian Taxation Office, Australian Business Register, Department of Social Services and/or Department of Home Affairs' core operational requirements.

Legislative requirements to ensure privacy and secrecy of these data have been followed. For access to MADIP and/or BLADE data under Section 16A of the ABS Act 1975 or enabled by section 15 of the *Census and Statistics (Information Release and Access) Determination 2018*, source data are de-identified and so data about specific individuals has not been viewed in conducting this analysis. In accordance with the *Census and Statistics Act 1905*, results have been treated where necessary to ensure that they are not likely to enable identification of a particular person or organisation.