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Singapore banks under pressure but still resilient

by Justin Hsiao

RMI-CRI data currently indicates increasing credit concerns in the local lenders. As shown in the left panel of Figure 1, RMI-CRI aggregate 1-year Probability of Default (PD) for Singapore banks, a simple median for the PDs for the three public-listed banks in Singapore, has started rising since 2015, from around 3bps to 30bps, highlighting the growing burdens on banks' asset quality and profitability. However, the Singaporean lenders, in their latest financial reports, have demonstrated that they can withstand the headwinds in the economy as they are well-capitalized and capable to manage risks amid recent volatility in the capital market.

The market continues to push down the price of Singapore bank stocks amid sluggish global economy growth, especially in China, and low oil prices. The banks' share prices slumped around 30% compared to their peak in 2015. The banks' exposure to China is significant, consisting of about 35% of the loans of DBS, 28% for OCBC and 12% for UOB. Meanwhile, Singapore banks' exposure to oil and gas companies accounts for 6 to 10% of their total loans, according to S&P's estimate.

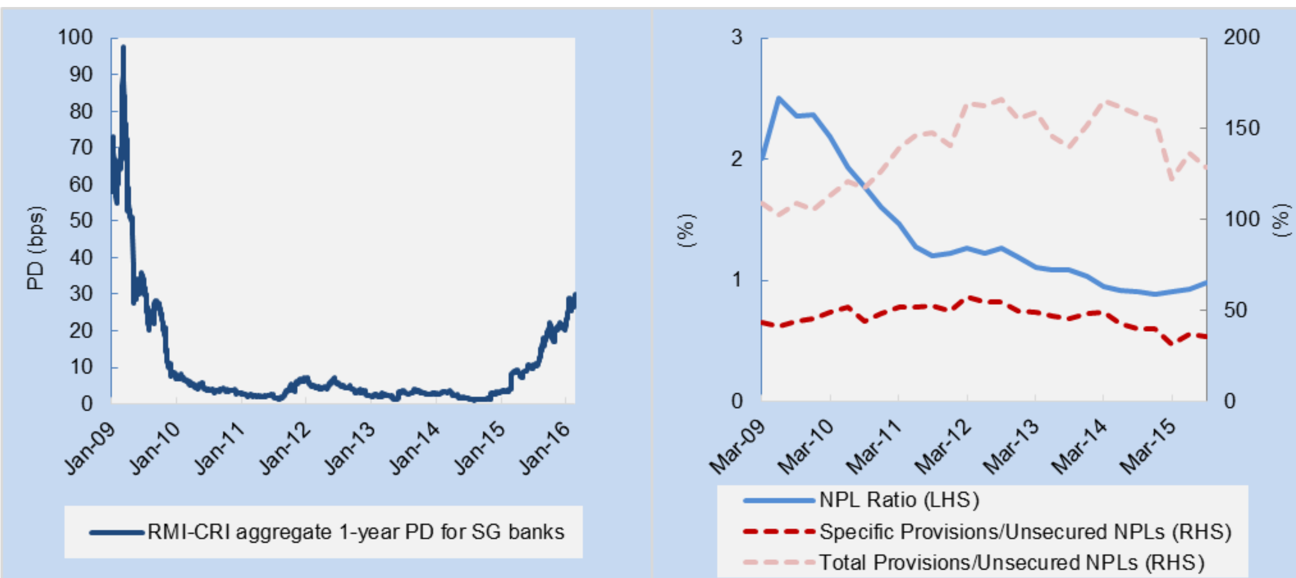

Figure 1. RMI-CRI aggregate 1-year PD (left panel); and NPL ratio and provisions (right panel) for Singapore banks.
Source: RMI-CRI, Monetary Authority of Singapore (MAS)

The right panel of Figure 1 shows that the non-performing loan (NPL) ratio for local lenders edged up to 1% in Q3 2015, as the total NPL amount increased from SGD 6.5bn in Jun 2015 to SGD 6.9bn in Sep 2015. Meanwhile, the provisioning coverage ratio has come down as increased defaults have eaten into these buffers. Given the prolonged down-cycle in the oil and gas market, the provisions would probably increase in the next following quarters, weighing on the firms' profitability.

Located at an important geopolitical position in Asia, Singapore banks have abundant access to cross-border funding. Even though Singapore's banking system is self-sufficient, the cross-border interbank funding still accounts for about 34% of the whole funding source. According to MAS data, the cross-border interbank funding in Q3 2015 was SGD 729bn, 27.4% higher than the level in 2009. Banks that derive their funds from one currency but lend in another unhedged currency could face significant exchange rate risks. For example, the USD and emerging market currency pairs would have posed such risk to banks for the most part of 2015.

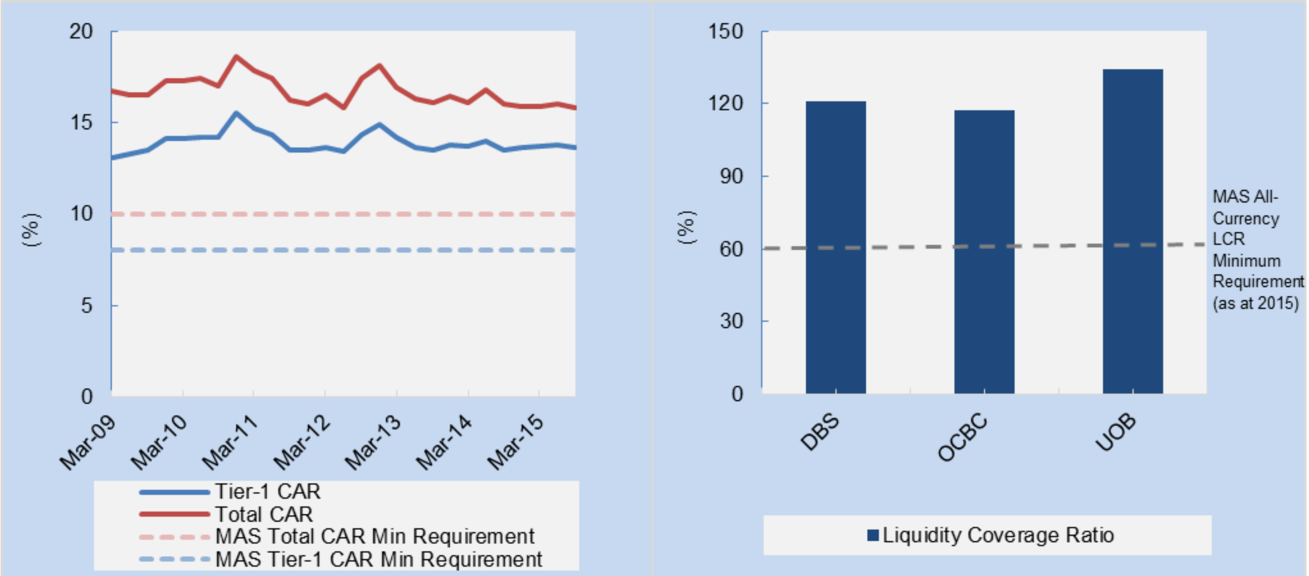

Figure 2. Tier-1 Capital Adequacy Ratio (CAR), total CAR (left panel) and Liquidity Coverage Ratio (LCR) (right panel) and MAS requirements for Singapore banks as of Q3 2015. *Source: MAS*

Despite obstacles, overall local banks' capital and liquidity still remain healthy even under slower economic growth. According to the latest financial stability review issued by MAS (see Figure 2), the local banks' total and tier-1 capital adequacy ratio (CAR), a measure of a bank's capital to its risk, were stable and above regulatory requirements, signify a robust capital buffer. At the same time, the liquidity coverage ratio (LCR) for all domestic Singapore banks are all above MAS's requirement, indicating the financial firms' ability to use their liquid assets to meet short-term obligations.

In addition, the net interest margin of Singarore's big-3 banks climbed to a four-year high of 1.79%, generating net profit YoY growth in Q4 2015. On Feb 22, DBS, the largest bank in the nation, posted a 20% increase in its Q4 2015 net profit reaching SGD 4.45bn, which beat market consensus. One week earlier, OCBC also posted a record net profit of SGD 3.9bn in Q4 2015, up by 20% YoY. It is noteworthy that although UOB saw net profit in Q4, the YoY growth was merely 0.3% due to the drag of loan provisions, highlighting the ongoing concerns over asset quality. Therefore, if Singapore banks can control their asset quality well, they still have good potential to thrive in the adversity of challenging 2016.

Credit News

HSBC has quarterly loss on lending income and bad loan

Feb 22. HSBC Holdings, Europe's largest bank, posted a fourth quarter loss of USD 858mn, which was much worse than the expected profit of USD 1.95bn by market consensus and the profit of USD 1.73bn in the same quarter last year. The heavy loss could be attributed to the falling income from its lending business, the increasing loan impairment charges, and the loss recognition of the fair value on its debt. The Q4 revenue sank by 18% to USD 11.8bn as net interest income fell to USD 8.1bn. The expenses related to losses on hedging also weighed on the revenue. Impairments on bad loans and credit risk provisions increased by 32% to USD 1.64bn, taking full year charges to USD 3.7bn, exceeding the consensus of USD 3bn. (Bloomberg)

OECD cuts global growth forecast

Feb 18. Global gross domestic product will expand 3.0% in 2016, the same pace as in 2015 and 0.3 percentage point less than predicted in November, according to the Organization for Economic Cooperation and Development (OECD). OECD cut its global growth forecasts, saying the economies of Brazil, Germany and the US are slowing and warning that some emerging markets are at risk of exchange-rate volatility. Stock markets around the world have plunged this year amid concern that slowing growth in China and a slump in oil prices will slow global expansion. The MSCI World Index fell to its lowest in more than two years last week as crude oil prices slumped below USD 30 a barrel for the first time in more than a decade. (Bloomberg)

Taiwan cuts 2016 economic outlook as exports seen falling

Feb 17. Taiwan cut its economic growth forecast for 2016 as China's slowdown weighed on its export demand. The economy will expand 1.47% this year, less than an earlier projection of 2.32%, the statistics bureau said on Feb. 15. Gross domestic product contracted 0.52% in the fourth quarter from a year earlier, steeper than the originally reported 0.28% decline. Taiwan's export-led economy has been buffeted by a slowdown on the mainland, and as China becomes an increasingly sophisticated competitor in high-tech manufacturing. The forecast for exports was lowered to minus 2.78% for 2016, from 1.97% growth seen previously. (Bloomberg)

Oil exporting countries hit by downgrades

Feb 17. S&P slashed the credit ratings of a slew of oil exporting countries, including a two-notch drop for Saudi Arabia. The credit rating agency also pushed down Bahrain's credit level citing the slide in oil prices, now into its 20th month, and further lowered the ratings for Brazil, Kazakhstan and Oman. The oil market has recovered its footing recently, but the rating agency said it did not expect the agreement between Saudi Arabia, Russia, Qatar and Venezuela to freeze oil output at January levels to have a material impact on its oil price assumptions. (FT)

China's debt surge has potential to pressure ratings, S&P says

Feb 16. China is facing systemic risks and potential pressure to its ratings as record-low interest rates and a scramble to repay overseas corporate loans fuel a borrowing spree, according to S&P. The yuan's worsening outlook is spurring some Chinese companies to raise funds onshore to pay down foreign-currency debt, which could contribute to higher domestic leverage over the next one to two years. Also, local firms tend to borrow as much as they can during an easing cycle. China's debt-to-GDP ratio climbed to 232% at the end of 2014, a record high since 2004. (Bloomberg)

StanChart accused over USD 100mn African 'dirty debt' (FT)

GM to issue USD 2bn in unsecured debt (WSJ)

Fears recede at Glencore as banks line up to join debt refinancing (The Guardian)

Regulatory Updates

Fed to raise the bar in bank stress tests

Feb 21. US banks are preparing for the Federal Reserve's annual stress tests, which will assess how 33 US banks would withstand a 10% US unemployment rate, moderate deflation and worldwide recession. The stress tests are a series of hypothetical scenarios used to ensure that the lenders have sufficient loss absorbing capital in the event of a financial crisis. In this year's severely adverse scenario, there would be significant market illiquidity, rapid selling of assets by a large financial institution and a sudden increase in credit risk. Banks will submit their capital plans by April 5 and the Fed will announce the results of the stress tests by June. (FT)

European banks gain reprieve as ECB retreats on capital demands

Feb 19. The ECB will cut its capital demands on banks as they found that banks in the euro area have capital in excess of minimum thresholds. European banks have a common equity Tier 1 capital ratio of 13%, well above the 9% level in 2010. The ECB said that the banking sector is in a stronger position to absorb unexpected financial or economic headwinds and the central bank will not impose further capital requirements on banks. Instead, the ECB may place more emphasis on the lenders' liquidity and funding situations in their next supervisory review. (Bloomberg)

Banks to conduct stress test for China yuan: FSC (China Post)

Brokerage platforms begin to clean up act after FCA warning (FT)