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Rising US rates to boost Singapore bank earnings towards pre-Covid levels

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WITH Singapore having one of the largest pass-throughs of higher US interest rates into local lending yields in the Asia-Pacific region, Fitch Ratings believes the recovering operating profit and risk-weighted asset (RWA) ratios of the country's banks are geared for a recovery towards their pre-Covid levels.

In a research report on Tuesday (Jul 5), the research house raised all 3 Singapore banks' earnings and profitability scores to "A+" from "A" to reflect diversified business models and resilient asset quality. While DBS and OCBC have each been issued a long-term issuer default rating of "AA-/Stable", UOB is rated "AA-/Negative" considering how it has the least headroom in its capitalisation and leverage score, compared to its peers.

Fitch nonetheless sees adequate headroom within the scores of all 3 banks to "withstand some moderate impairment", with asset-quality risks to remain contained despite higher inflation and rising interest rates.

The business profiles of Singapore's banks are also underpinned by diversified business models with strong earnings stability throughout cycles, noted the research house.

In particular, Fitch highlighted that the volatilities of their operating profit and RWA ratios are the lowest compared with other highly rated banks rated by Fitch globally - despite their significant exposures to emerging markets at some 17 to 29 per cent of total loans.

"Singapore banks' diversified business models enabled them to lean on non-interest revenue to offset lower interest rates, which helped to keep their operating income relatively steady between 2019-2021. Resilient asset quality also meant lower earnings volatility from swings in impairment charges," noted analysts of Fitch.

"We see potential for a sustained improvement in core profitability across the banks. Earnings should also benefit from cyclically higher interest rates," they added.

The banks' cost-to-income ratios are further expected to improve on higher operating income.

Although Fitch's analysts see some upside in UOB and DBS's profitability upon completion of their respective acquisitions of Citigroup's consumer businesses, they maintain that any improvement will only be reflected after factoring in one-off integration costs to be incurred over the next few years.

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