

# Global Banks Midyear 2019 Outlook:

**Low For Longer And Digital Prompt  
Further Rethink**

Emmanuel Volland  
Cynthia Cohen Freue  
Natalia Yalovskaya  
Gavin Gunning

Brendan Browne  
Elena Iparraguirre  
Mohamed Damak  
Osman Sattar

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**S&P Global**  
Ratings

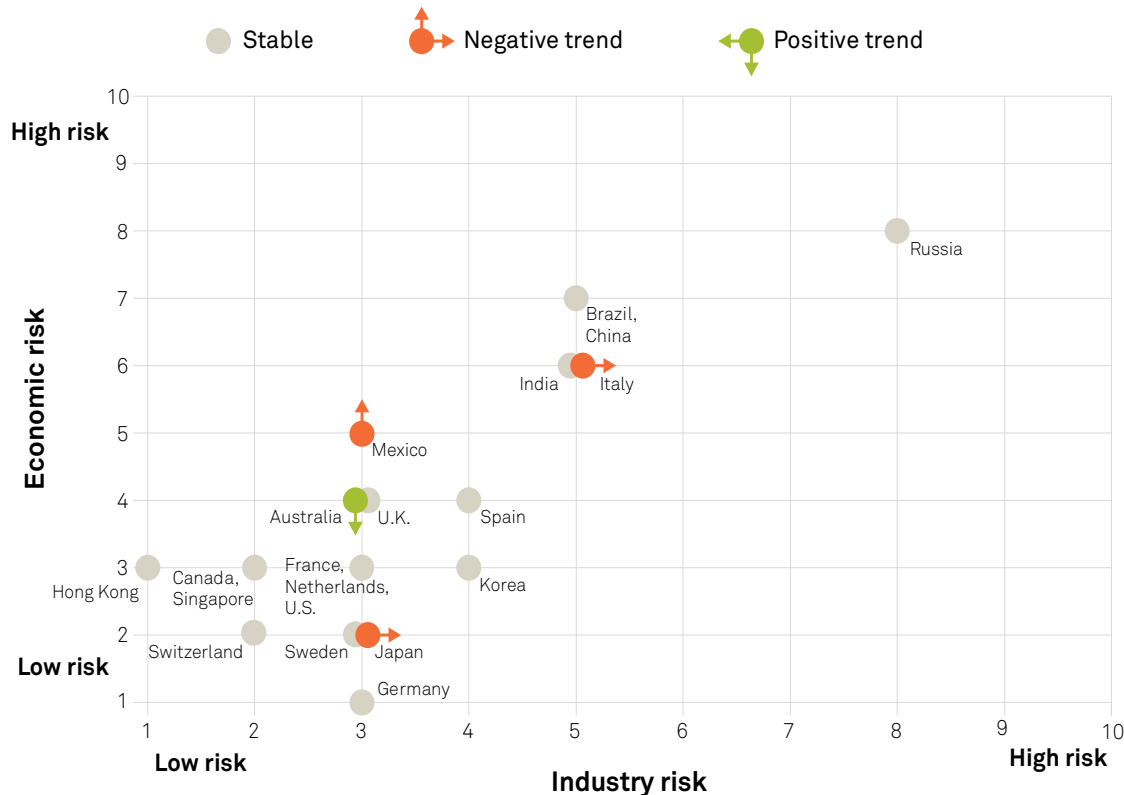
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# Key Takeaways

- Credit conditions remain supportive for banks even if trade and geopolitical tensions are undermining confidence and economic momentum.
- The Fed's and ECB's responses to counter the slowdown are positive for banks' funding conditions but continue to call into question their business models given that interest margins will remain low for longer. The pressure on profitability is higher in Europe and Japan.
- The vast majority of outlooks on banks is stable globally. The bias has become less positive in Europe.
- Credit losses have likely bottomed out in many countries, while capitalization is unlikely to improve further.
- The steady push to make systemic banks resolvable continues, through a variety of approaches across the world.
- Technology is disrupting retail banking across the globe. Banks' ability to respond will depend on their digital readiness.

# BICRA And Trends For Top 20 Global Markets



A BICRA (Banking Industry Country Risk Assessment) is scored on a scale from 1 to 10, ranging from the lowest-risk banking systems (group 1) to the highest-risk (group 10). Data as of July 10, 2019.

## BICRA changes in 2019

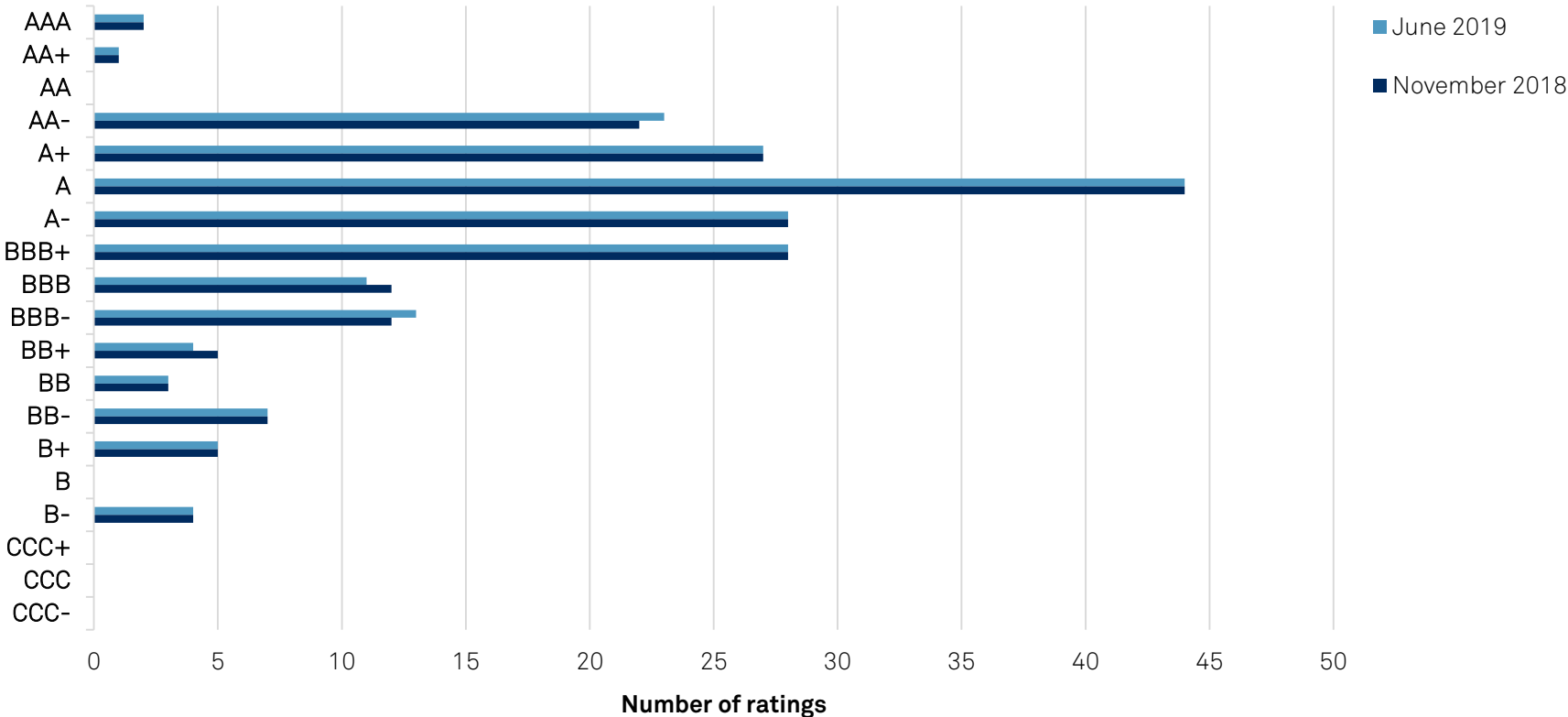
- Indonesia **raised** to 6 from 7
- Philippines **raised** to 5 from 6
- Israel **raised** to 3 from 4
- Poland **raised** to 4 from 5
- Slovenia **raised** to 4 from 5
- Panama **raised** to 5 from 6
- Uzbekistan **raised** to 8 from 9

## Trend changes in 2019

- Economic risk to **stable** from **positive** on the Netherlands
- Economic and Industry risks to **stable** from **negative** on Brazil
- Economic risk to **negative** from **stable** on Mexico
- Economic risk to **negative** from **stable** on Tunisia
- Economic risk to **stable** from **positive** on Croatia

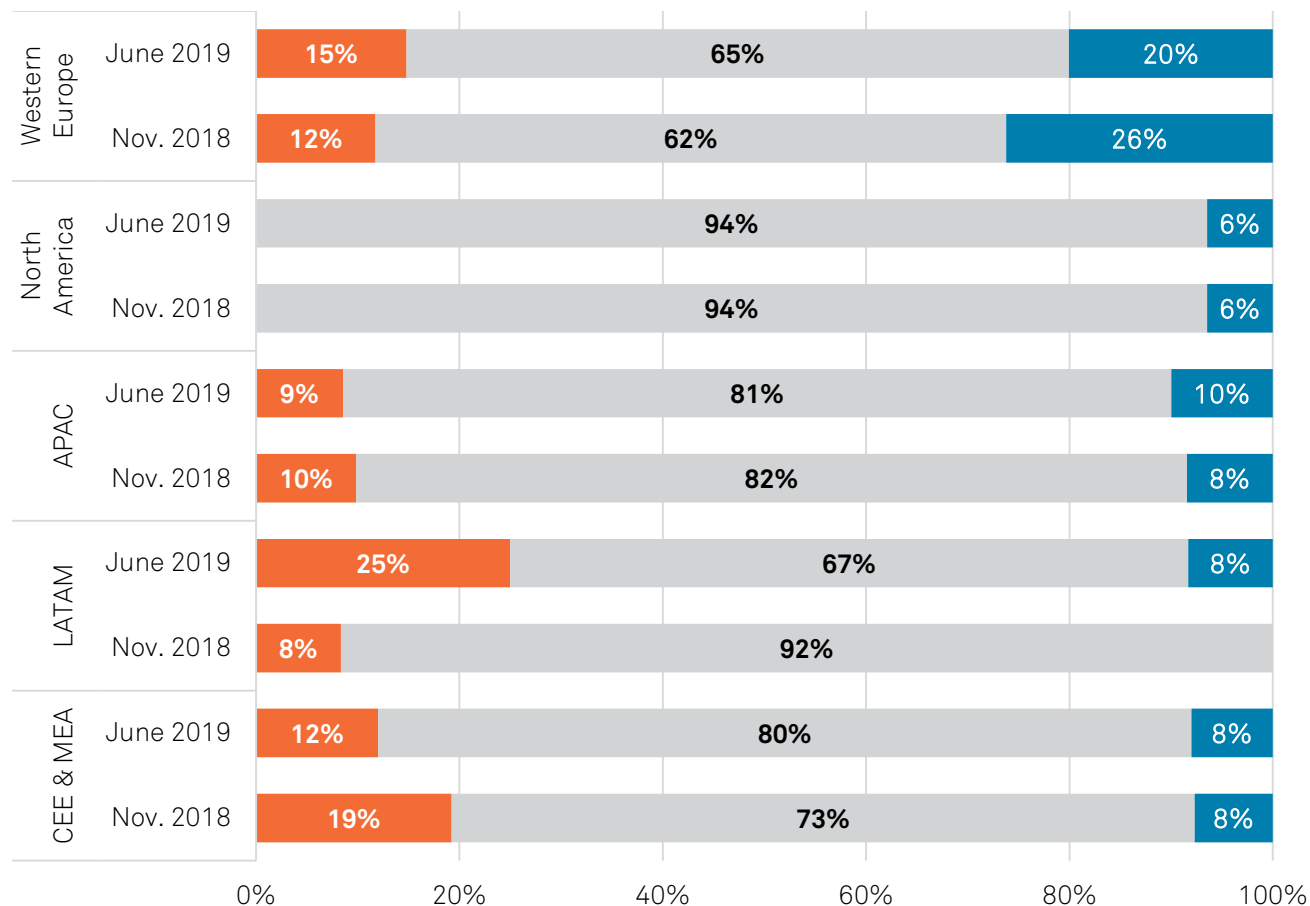
# Broadly Stable Ratings So Far In 2019

## Top 200 Bank Ratings



Operating company issuer credit ratings. Data as of June 30, 2019. Source: S&P Global Ratings.

# Outlooks Of Largest Banks By Region



■ Negative  
■ Stable  
■ Positive

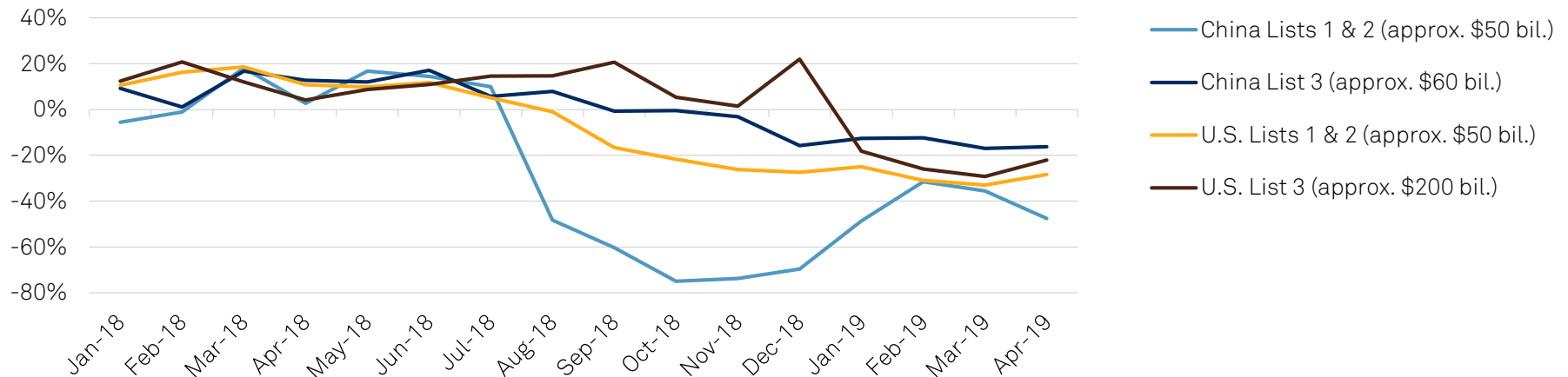
**The positive outlook bias in Western Europe is reducing. The gap with other regions mainly reflects the ongoing build-up of ALAC and positive restructurings.**

Data as of June 30, 2019. Based on the top 200 rated banks. Source: S&P Global Ratings.

# Credit Conditions: U.S. And Canada

- The U.S. economy is cooling. We now forecast GDP growth at 1.8% in 2020. The expansion is about to reach record length (10 years), and we see little probability of recession in the next 12 months.
- The Fed's dovish policy bias is supporting liquidity and extending the mature credit cycle. We expect the central bank to cut the federal funds rate by 25 basis points, possibly as soon as September.
- The lending backdrop is weakening, potentially indicating an initial –but slight– turn in the cycle. Trade tensions and tit-for-tat tariffs between the U.S. and China remain the key threat.
- The build-up in nonfinancial corporate debt and leveraged lending are other sources of potential instability.

## U.S. And China's Imports Of Tariffed Products

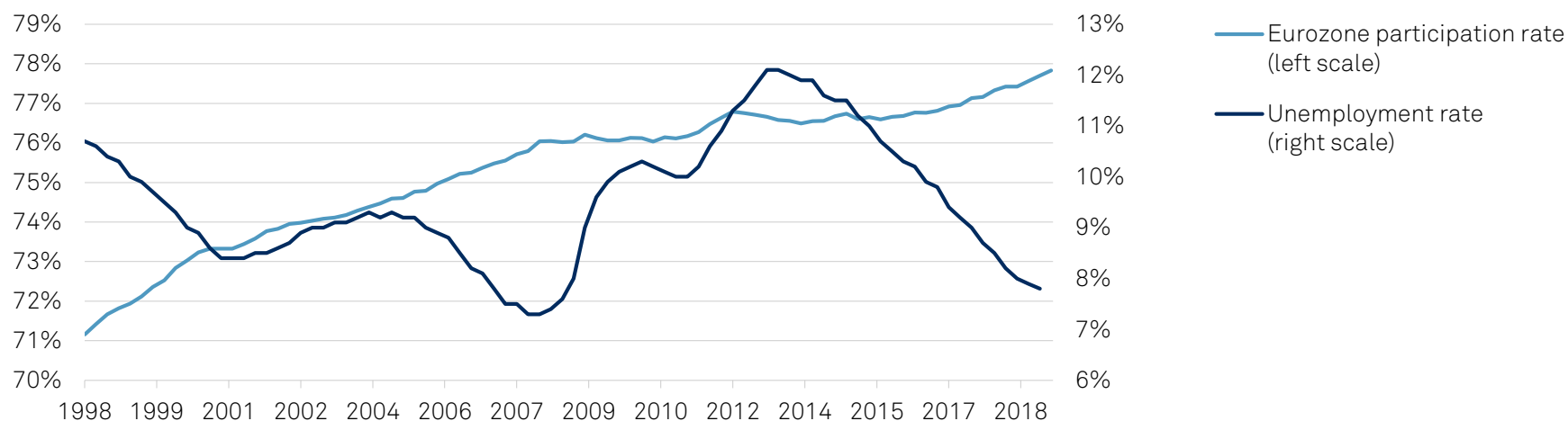


Source: Panjiva.

# Credit Conditions: Europe

- Trade and political tensions are weighing on economic fundamentals. We expect the eurozone to expand by only 1.1% this year and 1.3% in 2020, despite a vibrant labor market and high capacity utilization.
- Financial markets have welcomed the ECB's proactive policy response to counter the risk of an accelerating slowdown. The subdued outlook will prevent the ECB from raising rates until second-quarter 2021, which presents business challenges for banks.
- The political landscape is more divisive and unpredictable after the European elections, raising the risk of unintended consequences with Brexit, trade, and fiscal imbalances in Italy being the main risks.

## The Eurozone Labor Market Is Creating Jobs



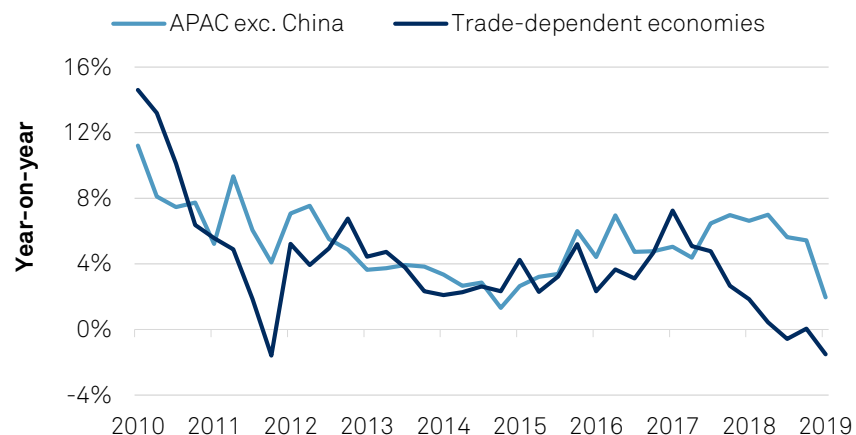
Sources: Eurostat, Oxford Economics, S&P Global Ratings.



# Credit Conditions: **Asia-Pacific**

- Uncertainty has returned. The year started optimistically on the back of the Fed's more dovish policy and China's loosening of lending, but escalating trade strife has shaken confidence.
- The economic slowdown in key economies will be moderate, according to our base case.
- Investment growth across trade-dependent economies, including Korea, Malaysia, and Singapore, has fallen to a seven-year low. For China, investment in technology-related manufacturing is expanding at its lowest level since at least 2004.
- The greatest near-term risk is the strategic conflict between the U.S. and China. Other top risks include corporate refinancing, market liquidity, property repricing, and China's debt leverage.

## Asia-Pacific Real Investment Growth Has Slowed



Sources: CEIC, S&P Global Ratings.

## China Credit Spreads

Yield gap between five-year Chinese government bonds and medium-term notes rated 'AA-' (domestic ratings).



Sources: CEIC, S&P Global Ratings.

# Credit Conditions: Latin America

- Optimism is fading despite the Fed’s more dovish tone and the possibility of lower interest rates in the U.S. later this year.
- Political challenges have surfaced in the largest countries, and new administrations are facing waning domestic investor confidence as policy uncertainty prevails.
- Clouding the economic outlook are the lack of critical reforms in Brazil; the cancellation of major projects, the shift in energy policy, and the lack of long-term direction in Mexico; and the economic slump and upcoming presidential election in Argentina.
- Financing conditions should remain supportive despite increased volatility and lower economic growth expectations.

## S&P Global Ratings’ Forecasts For Latin American GDP Growth

	Base Scenario					
	2017	2018	2019	2020	2021	2022
<b>Argentina</b>	2.7	-2.5	-1.6	2.2	2.5	3.0
<b>Brazil</b>	1.1	1.1	1.0	2.2	2.5	2.5
<b>Chile</b>	1.5	4.0	2.6	2.9	3.0	3.0
<b>Colombia</b>	1.4	2.6	2.9	3.0	3.0	3.0
<b>Mexico</b>	2.4	2.0	1.3	1.8	2.2	2.2
<b>Panama</b>	5.3	3.7	4.5	4.5	4.8	5.0
<b>Peru</b>	2.5	4.0	3.4	3.7	3.9	4.0
<b>Uruguay</b>	2.6	1.6	0.9	1.9	2.8	3.0
<b>Venezuela</b>	-15.7	-20.0	-20.0	-5.0	0.0	3.5
<b>LATAM</b>	0.7	0.1	-0.1	1.9	2.4	2.7
<b>LATAM ex. Venezuela</b>	1.8	1.4	1.2	2.3	2.6	2.6

Note that Latin American GDP aggregate forecasts are based on three-year average (2014-2016) PPP GDP weights. GDP numbers are based on seasonally adjusted series when available. Source: S&P Global Ratings’ economists.

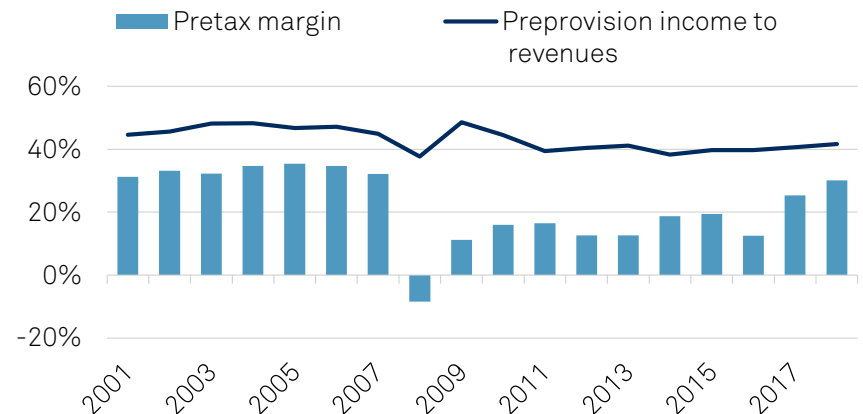
# Impact Of A No-Deal Brexit

- Our base case remains that the U.K. will not leave the EU without a deal, but the risk of disruptive, no-deal outcome is growing.
- The resignation of Theresa May could lead to a harder stance on Brexit. Yet, her successor will face the same challenges because the EU is unlikely to renegotiate the terms of the Withdrawal Agreement. The U.K. Parliament is unlikely to approve it and will likely continue its opposition to a no deal.
- Major U.K. banks' balance sheets are robust and their earnings are modestly improving. Together with contingency planning and explicit supportive measures and statements by the Bank of England about access to liquidity, these features provide a substantial cushion.
- The adverse case in a no-deal Brexit is that the U.K. would enter into a recession. The associated effects on unemployment, insolvencies and defaults, and collateral values, would affect U.K. banks. In such a scenario, outlook revisions are more likely than downgrades in the near term.
- We expect banks in other open European economies to be able to accommodate the effects of a no-deal Brexit.

## Key Figures From The No-Deal Scenario



## Major U.K. Banks' Profit Margins Are Recovering, Providing A Cushion Against Brexit Turbulence

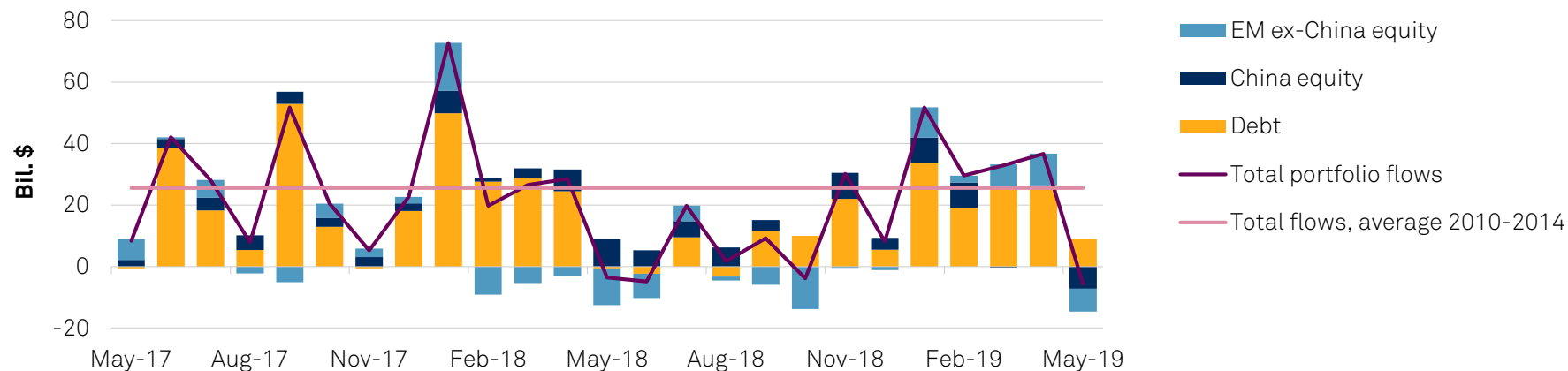


Based on aggregated data for Barclays, HSBC, Lloyds, Nationwide, RBS, and Santander U.K. Source: S&P Global Ratings.

# Overview Of Emerging Markets

- Volatility could resurface and sour financial conditions for banks in emerging markets, as trade and GDP slow and political risks mount. However, Fed and ECB policy should be positive for capital flows in the near term.
- Geopolitical risks are elevated and economic sanctions continue hurting a number of banking sectors and limiting their access to external capital markets (for example, Russia and Turkey).
- Tensions between the U.S. and Iran could result in higher oil prices. On the contrary, the trade war between the U.S. and China might weaken commodity prices, affecting certain emerging markets (for example, GCC, Russia, and Nigeria).
- Dependence on external debt is a high risk for banks in Turkey and Qatar.
- High leverage in China remains a concern. While the government's intent is to deleverage the country over time, it loosened the credit purse strings in early 2019 to avoid an economic slowdown.

## Net Non-Resident Portfolio Flows To Emerging Markets



Sources: IIF, S&P Global Ratings' calculations.

# Regulation And Resolution

- The 2017 finalization of Basel III represents the high point in the multiyear overhaul of prudential regulation. Indeed, we see policymakers taking measures to ease the burden on smaller, simpler institutions. However, full implementation will not finish until 2028, and we expect areas of uneven implementation of global standards.
- We see a steady push in efforts to make systemic banks resolvable--not just in the U.S. and Europe, but now also in Canada, Hong Kong, and beyond. This is a long-term project, and we expect highly variable approaches to resolution across various jurisdictions.

## In Europe

- The EU's latest banking package substantially completes the enactment of the Basel III standards, and simplifies liquidity and funding rules for smaller banks.
- While many of the new rules will be phased in over the coming couple of years, the implementation of key aspects such as the fundamental review of the trading book and risk-weighted output floors remains still several years away. This gives the banks more time to plan and mitigate the effects, but also leads to uncertainty about their end-state requirements.
- Regulatory expectations for banks' anti-financial crime control frameworks continue to increase, but authorities now recognize the need to address inconsistent implementation of standards and fragmentation of supervision.

## In the U.S.

- The regulatory reform legislation passed in May 2018 has lessened regulation to a degree on regional and community banks, including by removing a number of regional banks from the recent Fed-run stress testing.
- The Fed still has an outstanding proposal to tailor regulation based on banks' risk profiles, which would also ease some regulation on non-GSIB banks. It also intends to simplify its capital rules for large banks, most notably with the introduction of a stress capital buffer. It remains unclear when it will finalize either of those proposals.

# Regulation And Resolution

## Stark differences in the implementation of bank resolution frameworks

- The EU and U.S. have transitioned to effective bail-in regimes. However, with some exceptions, European jurisdictions remain behind the U.S. in implementation. Many banks will not finish building their bail-in buffers until 2024.
- Other G-20 jurisdictions are making legislative progress that will enhance their regulatory toolkits, but we see their policymakers as cautious about eliminating the possibility of extraordinary government support. For example, we think the authorities in Canada and Hong Kong are trying to create genuine optionality about whether to bail-in, bail-out, or both.
- The Australian Prudential Regulation Authority (APRA) announced on July 9<sup>th</sup> that it is proceeding with its resolution framework plan. In our view, it does not introduce any policy or process impediments to the government bailing out a systemically important bank. We therefore continue to assess the government as highly supportive.
- Japan and Singapore have enhanced their regulatory tools, but they remain reluctant to bail-in, in our view.

# Tech Is Disrupting The Bank Landscape



**Technology** may alter the global retail-banking sector over the next few years.



We believe **customer preference** will be the main catalyst for change. Banks' ability to respond will depend on their digital readiness.



**Regulation** and governments' willingness to lay the groundwork for banking innovation can promote more rapid change.



**Authorities** would also need to act swiftly to protect banking systems from disruption that may reduce the quality of banking services or result in weaker, more vulnerable banking systems.

# North American Banks

## Key Expectations

- Earnings growth is likely to be limited this year--down sharply from the rapid pace of 2018 that benefited from reduced tax rates and higher interest rates.
- Net interest income should rise moderately on the back of limited loan growth. But with the ending of the Fed's monetary tightening, fewer banks are likely to report higher margins and more could start showing declines.
- Banks will continue to contain costs by consolidating branches, containing head count, and growing digitization.
- The 2020 implementation of new accounting standards for loan loss provisions will likely cause reserves to rise notably, particularly for banks with large consumer loan exposures.
- For Canadian banks, we expect operating performance to gradually strengthen.

## Key Assumptions

- GDP growth slowing to 2.5% and 1.2% in the U.S. and Canada in 2019, with the Fed cutting rates perhaps as soon as September.
- Credit losses have likely bottomed out and may gradually increase.
- The U.S.-Mexico-Canada free trade agreement will remain on a slow path toward ratification.

## Key Risks

- Corporate credit quality, particularly in leveraged lending, could deteriorate after several years of growth.
- Credit quality may also worsen in the auto, student, credit card, and commercial real estate lending.
- In Canada, a sufficiently negative employment shock could trigger a substantial decline in home prices, given elevated prices. This could be accompanied by noticeably higher losses on consumer loans.



# The Outlook For U.S. Banks Is Slightly Positive

Worsening

Neutral

Improving

## Revenues

Net interest income growth is likely to decelerate on modest loan growth along with flattish margins. The benefits of rising interest rates will diminish as benchmark rates pause. Fee income will depend on capital markets activity, market valuations, and mortgage volumes.

## Expenses

Expenses will likely keep growing at a limited pace. Banks will continue to contain costs by consolidating branches, containing head count, and growing digitization. However, investments in technology will be somewhat of an offset.

## Profitability

We expect profitability to improve modestly in 2019. However, the gains will be far lower than in 2018 that benefited from rising interest rates and reduction in corporate tax rates.

## Credit Quality

The end of the Fed's tightening policy cycle could potentially prolong a highly benign period. We expect nonperforming assets and net charge-offs to rise gradually in 2019. Specific areas of potential risk include leveraged loans, autos, credit cards, and pockets of commercial real estate.

## Capital

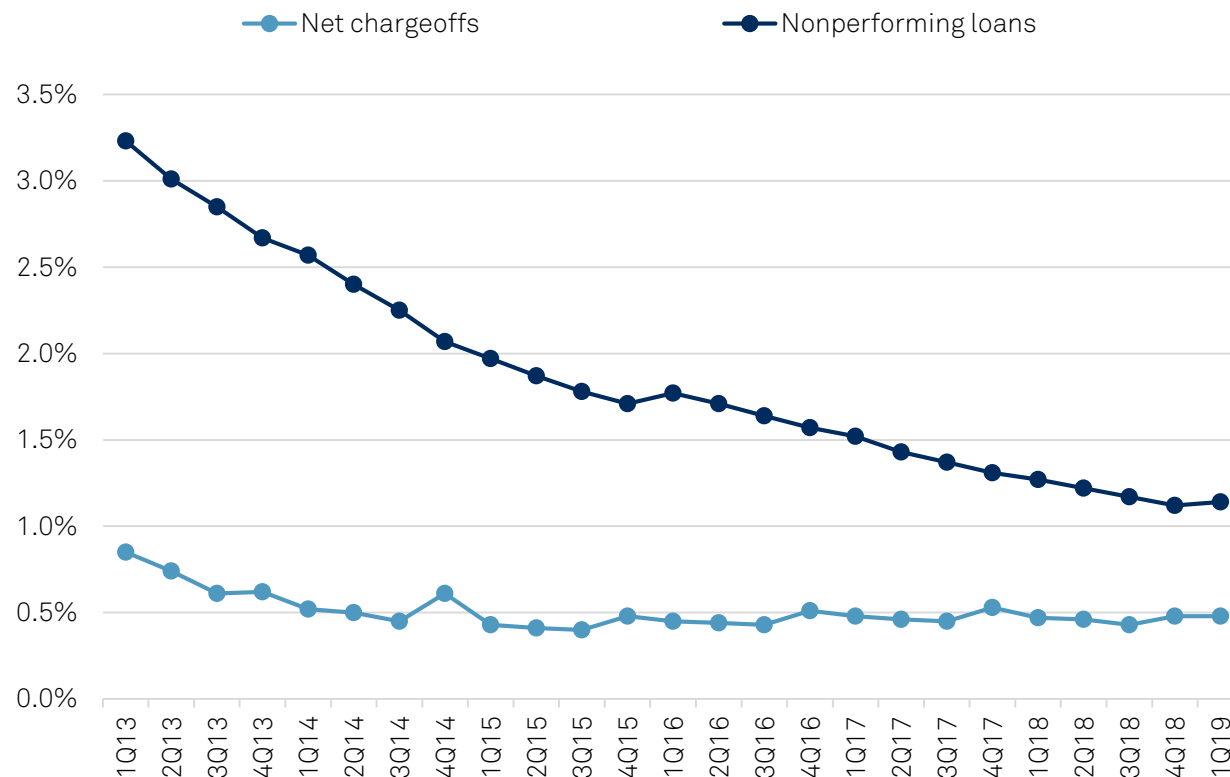
Capital ratios have likely peaked, particularly for regional banks. The capital levels of the GSIBs will depend on final terms of the Fed's proposed stress capital buffer, although their improved performance in the 2019 Comprehensive Capital Analysis and Review may give them more room for reduction.

## Funding & Liquidity

The rise in interest rates since 2015 had been increasingly impacting banks' deposit costs, funding, and liquidity. Deposit costs could still climb somewhat higher. However, the end of the Fed's tightening cycle and the potential for rate cuts may alleviate that pressure.

# Asset Quality Is Excellent For U.S. Banks

## NPAs and NCOs: All FDIC

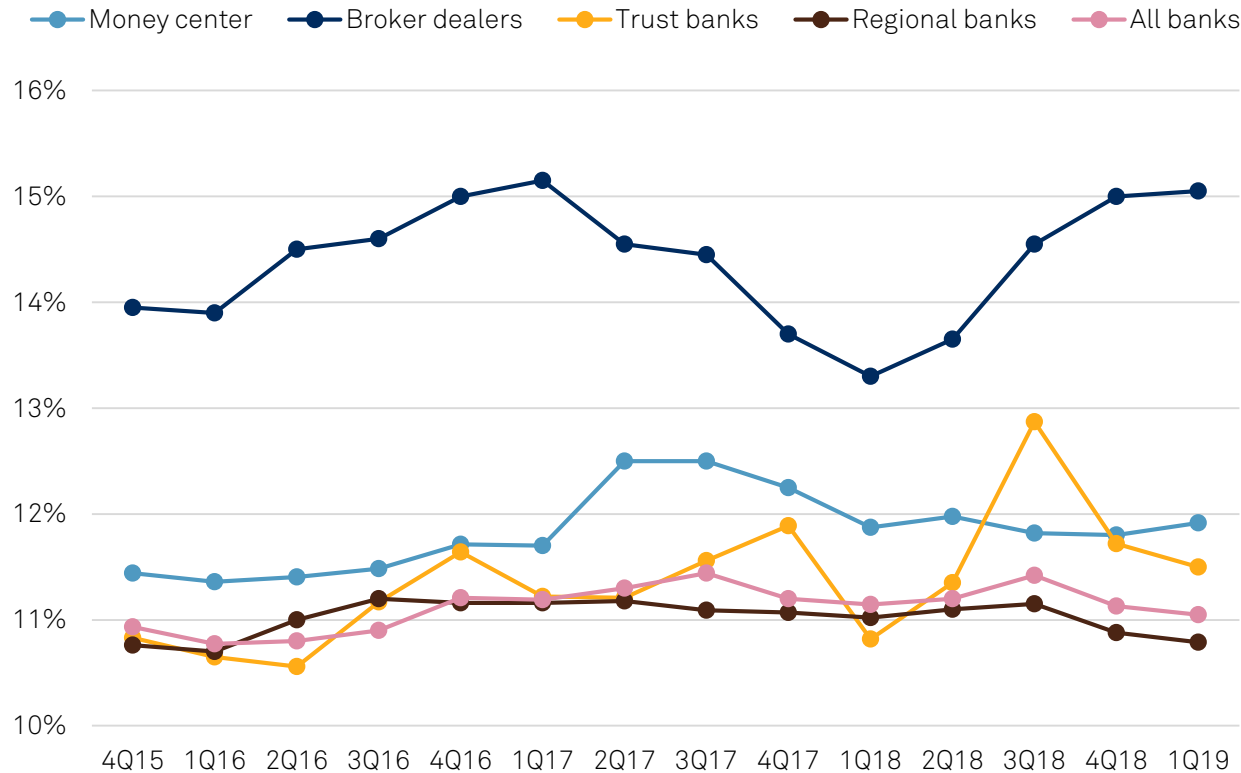


**Asset classes most susceptible to deterioration include auto, credit card, commercial real estate, and leveraged loans.**

Note: Adjusted nonperforming assets include nonaccrual loans, loans 90 days past-due, restructured loans, and OREO (other real estate owned). All FDIC (Federal Deposit Insurance Corporation) results estimated by aggregating call report data. NCO--Net charge-offs. NPAs--Nonperforming assets. Sources: S&P Global Ratings, S&P Global Market Intelligence, regulatory filings.

# Capital Levels Are Likely To Decline

## Median Common Equity Tier 1 Ratio



Sources: S&P Global Ratings, bank regulatory filings, S&P Global Market Intelligence.

**We expect regional banks to reduce their capital gradually following the tailoring of Fed rules. Capital levels of GSIBs will rely significantly on the Fed's proposal to revise regulatory requirements for large banks (stress capital buffer).**

# European Banks

## Key Expectations

- The cycle of rating upgrades is probably over, and we should see a more nuanced picture ahead.
- Economic softening and “low for longer” interest rates will again force banks to address subdued profitability, opening the door to further cost cuts and changes to business models.
- Capital and asset quality should remain solid.
- Progress in the build-up of bail-in buffers by systemic banks. Authorities will continue to enhance bank resolvability.
- Large-scale M&A is unlikely at this stage.

## Key Assumptions

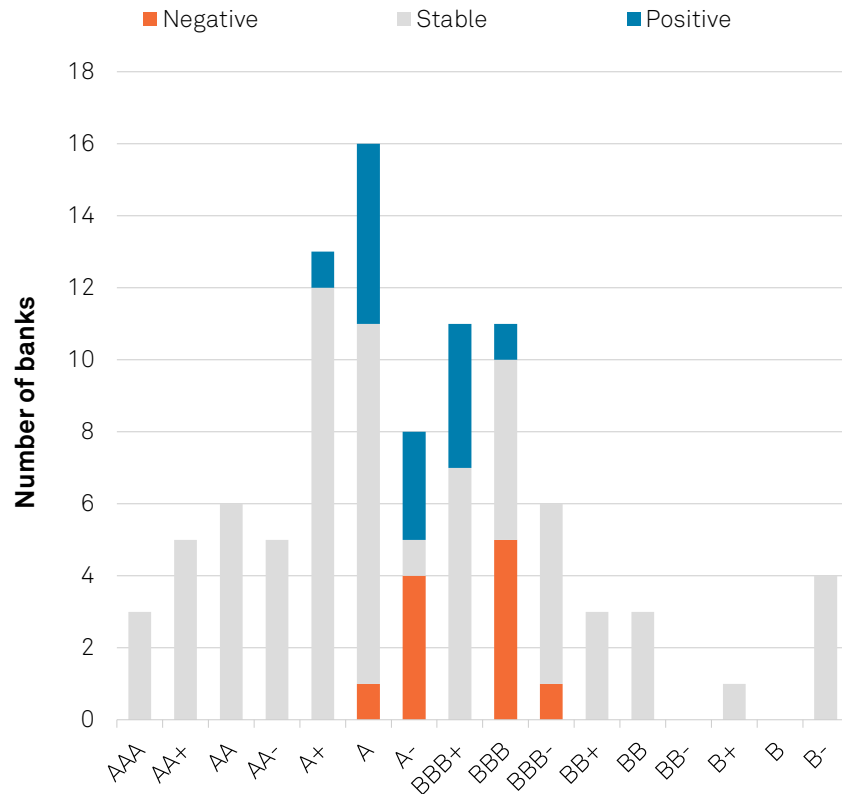
- Brexit will not be disruptive.
- Economic growth will be modest in 2019 and improve slightly in 2020.
- Accommodative monetary policy will ensure credit supply and affordable credit conditions.

## Key Risks

- A disruptive Brexit that leads to a severe economic downturn in the U.K.
- Prolonged uncertainty about fiscal imbalances in Italy that constrain economic growth, limit further progress in banks’ recovery, and raise doubts about old restructurings.
- A more adverse economic outlook for the region, most likely triggered by a further weakening of global trade, would prolong the region’s extremely accommodative monetary policy. This could lead to higher risk-taking and imbalances.

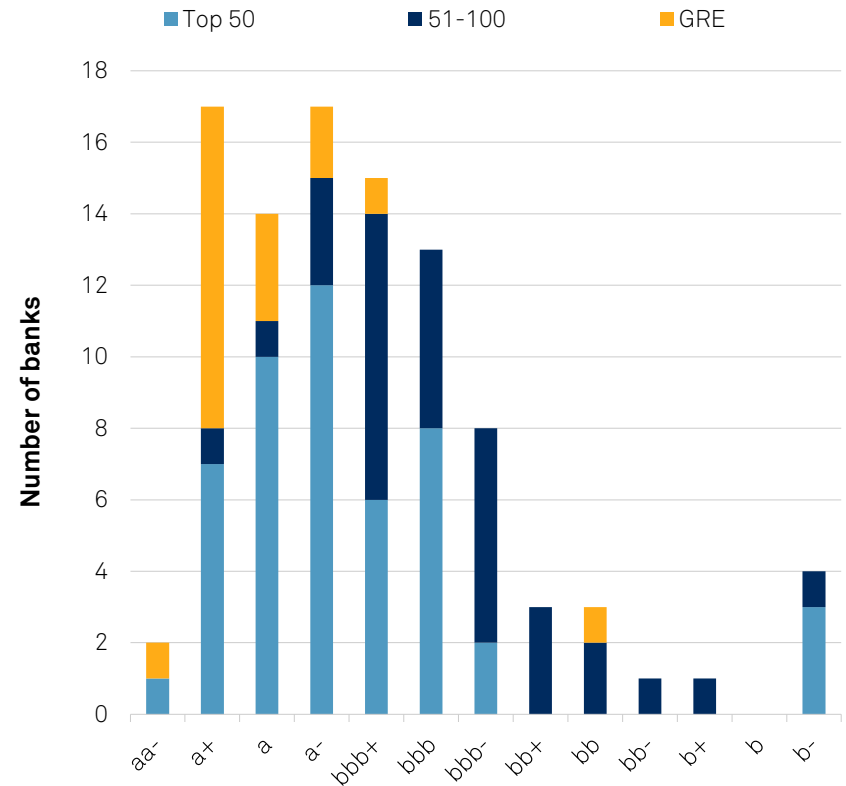
# The Positive Outlook Bias Is Reducing

**Top 100 European Banks: Issuer Credit Ratings and Outlooks**



Data as of June 30, 2019. Source: S&P Global Ratings.

**Top 100 European Banks: Stand-Alone Credit Profiles**

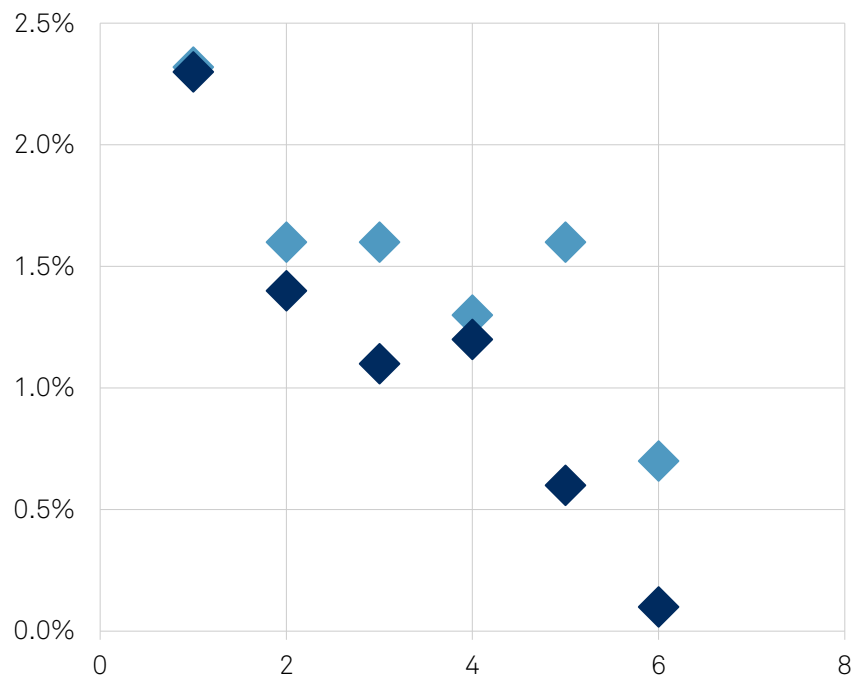


Data as of June 30, 2019. GRE--Government related entities. Source: S&P Global Ratings.

# A Weakened Environment For European Banks

## Economic Growth Is Slowing Down

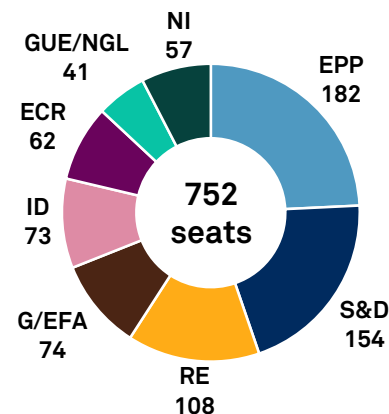
- ◆ 2019 GDP growth (Dec. 2018 forecast)
- ◆ 2019 GDP growth (current forecast)



## Political Risk Is Rising

Eurosceptic and far-right parties did not gain as much representation in the Parliament as polls had suggested. However, the political landscape appears more divisive and unpredictable as the two largest groups no longer hold the majority. In addition, government instability has increased in Austria, Greece, Italy, the U.K., and Spain.

## European Parliament 2019-2024

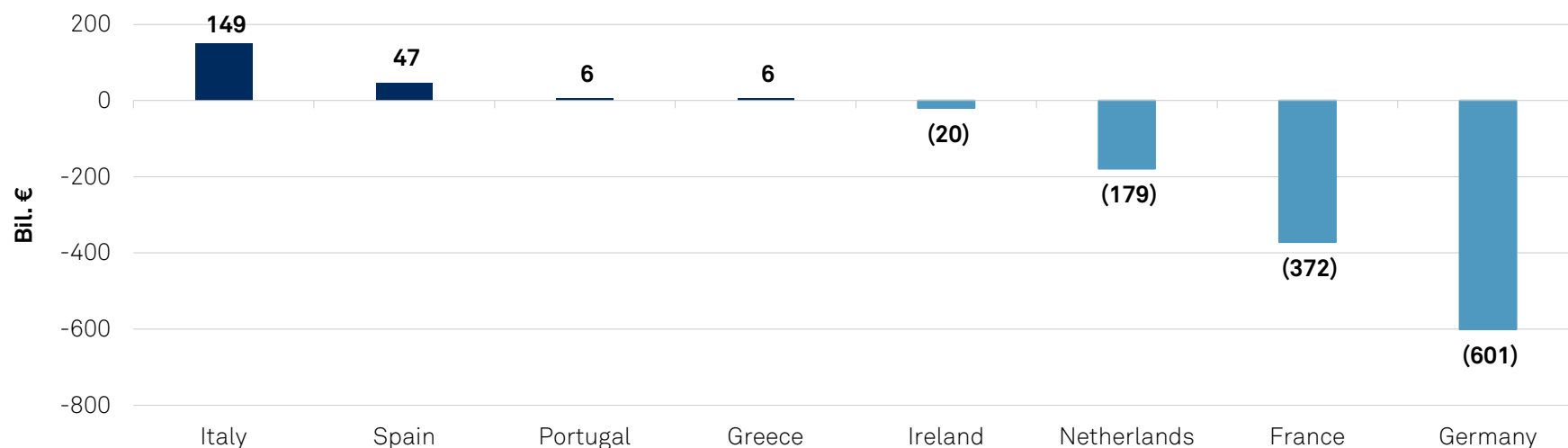


1. Source: S&P Global Ratings. 2. EPP--European People's Party. S&D--Socialists and Democrats. RE--Renew Europe. G/EFA--Greens/European Free Alliance. ID--Identity and Democracy. ECR--European Conservatives and Reformists. GUE/NGL--EU Left and Nordic Green Left. NI--Non-attached members. Source: European Parliament.

# Monetary Policy: Low For Longer

- The ECB will not raise interest rates until at least the second quarter of 2021 in our view. In its latest statement, it left open the possibility of an interest rate cut and the resumption of asset purchases.
- Its third long-term funding program for banks (TLTRO III) has a shorter maturity but still attractive pricing, ensuring that credit conditions will remain favorable for banks.
- We see TLTRO III playing only a differentiating role for second- and third-tier Italian banks, which would otherwise have higher funding costs.

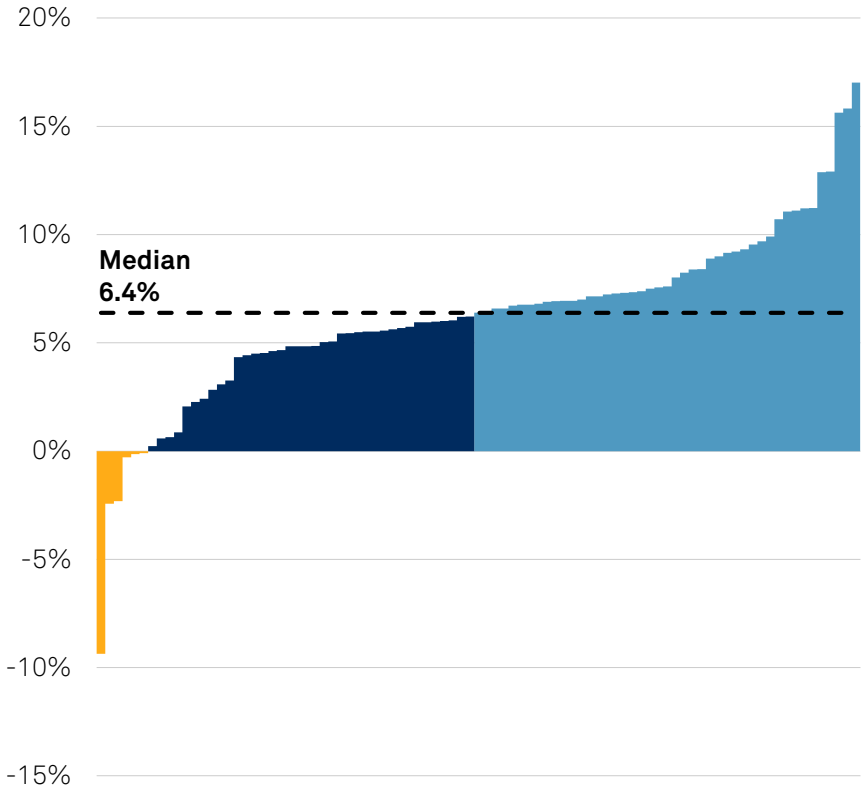
## Banks' Net ECB Borrowing/Lending



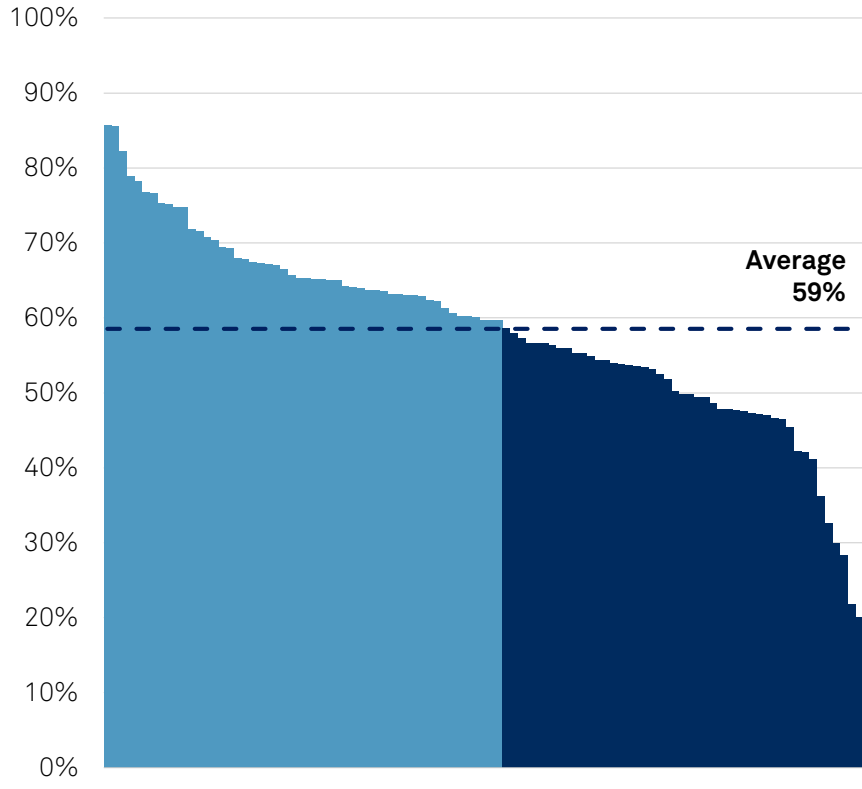
Liquidity deposited at the ECB includes both the deposit facility and current accounts. Data as of April 19, 2019. Source: ECB.

# Pressure Is Mounting To Address Low Profitability

**Projected Return On Equity For The Top 100 European Banks In 2019**



**European Top 100 Banks: S&P Forecast of 2019 Cost to Income**



Data as of June 30, 2019. Source: S&P Global Ratings.



# Asia-Pacific Banks

## Key Expectations

- The majority of outlooks is stable, and this is likely to continue into 2019.
- Aside from India, nonperforming loans should remain relatively low in 2019.
- Earnings and capital should remain generally supportive of ratings at current levels.
- We see little rating upside but some notable downside risks if the credit cycle turns.

## Key Assumptions

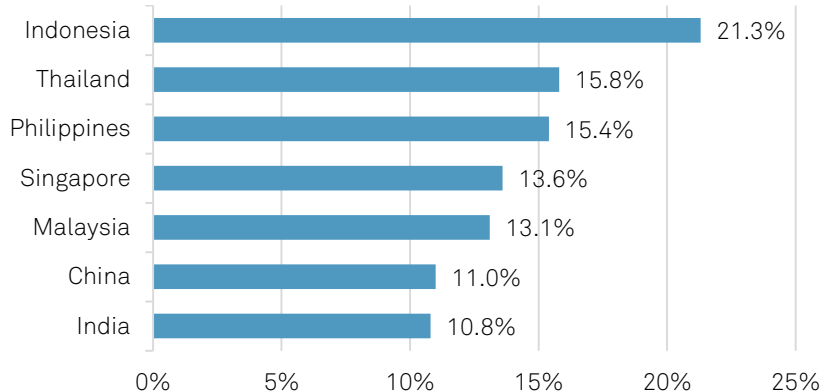
- Macroeconomic conditions should remain relatively stable. The cyclical downturn in Asia-Pacific trade is manageable for the majority of banks.
- Systemically important private-sector banks should continue to benefit from government support in most jurisdictions in the short-to-medium term.

## Key Risks

- Debt and asset prices remain relatively high amid low interest rates. These factors set the stage for a potential deterioration in credit quality, especially if a sharp correction in asset prices and pullback in liquidity were to occur.
- A significant and abrupt credit cycle downturn will likely result in negative ratings momentum. We expect, however, that most banks can weather a moderate and less-abrupt downside scenario.

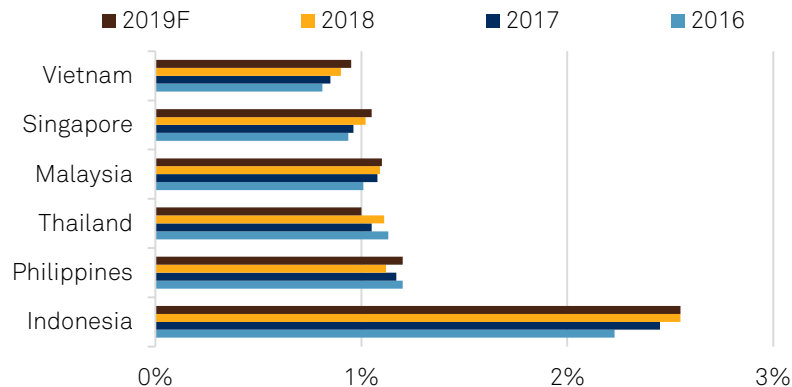
# ASEAN: Well-Positioned Against Headwinds

## 1. Healthy Tier 1 Ratios Provide Good Capital Buffers

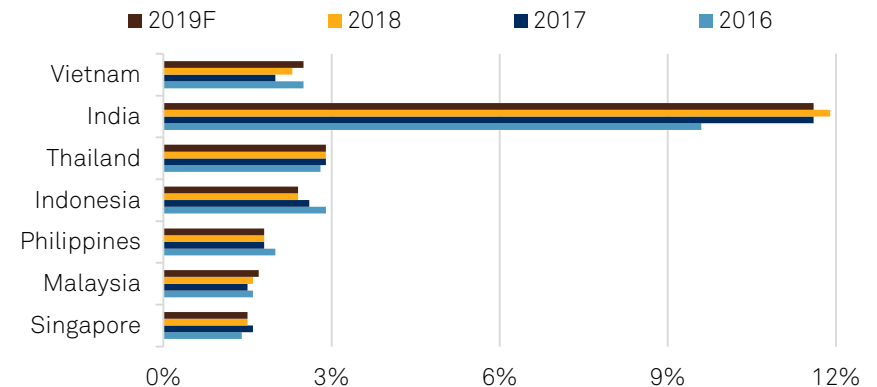


- Banks will continue to experience modest growth due to headwinds from the trade war and geopolitical uncertainties.
- Profitability remains good despite margin pressure, thanks to cost control and lower provisions.
- Asset quality has either stabilized or improved.
- Banks have good capital levels, having accumulated buffers during previous years, and are well-positioned to face external headwinds.

## 2. ROA – Banks Show Reasonable Returns



## 3. Nonperforming Loans – India Is An Outlier



F--Forecast. Source: S&P Global Ratings.

# China: More Pressure On Small Banks

## Chinese Banks Are Playing Catch-Up To Big Tech

Banks lag the country's technology companies when it comes to fintech services, particular for retail payments. The biggest banks have the resources to close the gap, but smaller ones will likely have to rely on and partner with Big Tech.

## Megabanks Will Lead The Micro and Small Enterprise (MSE) Loan Surge

We expect megabanks to lead the pack on financial inclusion MSE lending. Banks have limited room to expand margins on these loans, which are typically higher risk. We are unlikely to see a spike in credit risk because of greater monetary and administrative support.

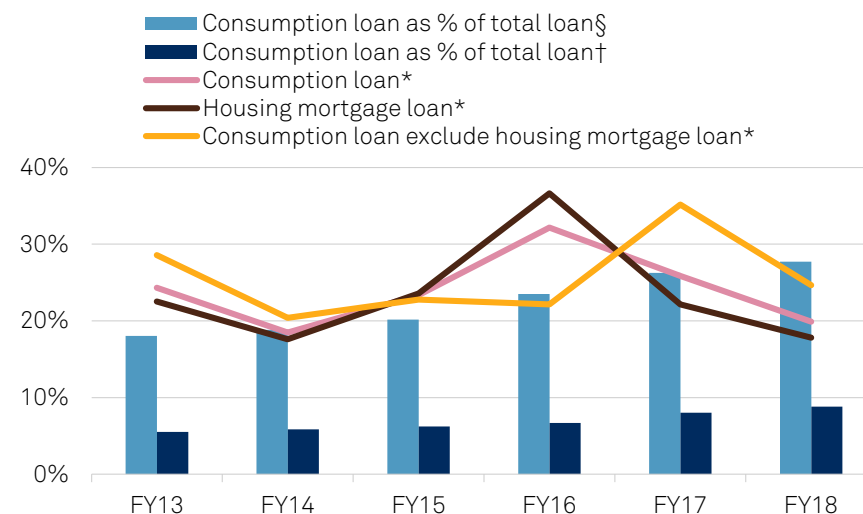
## China's Bailout Of A Troubled Bank Isn't Surprising

We anticipate high regulatory discretion in managing troubled banks, as seen in the case of Baoshang Bank, and financial stability to be of paramount consideration. Regulators are balancing moral hazard and market confidence in their response.

## Risks From High Consumer Lending Growth Continue To Rise

Credit card debt grew six times in six years. Fast growth and intense competition could bring about more risk, considering aggressive lenders, customer inexperience, and under tested risk management. Joint stock commercial banks, along with some regional banks, have a higher proportion of consumer lending.

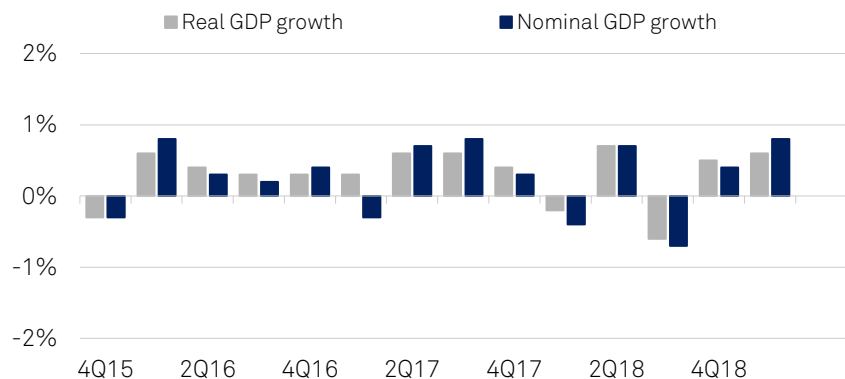
## The Fast Rise Of Consumer Loans



\*Year-on-year. §Residential housing included. †Residential housing excluded.  
Source: PBOC.

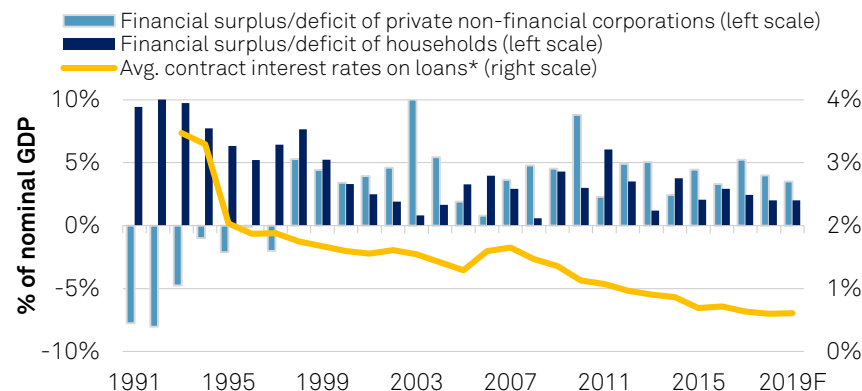
# Japan: Weakening Profitability

## 1. Evolution Of GDP Growth

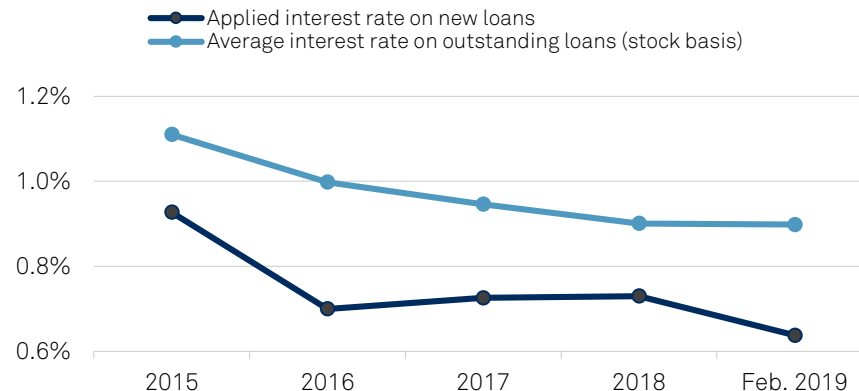


- Japan's negative interest rate policy seems to have bolstered current domestic economic growth.
- However, the policy did not push up lending demand due to a funding surplus in the private sector.
- As loan growth remains very limited, margins are narrowing. Our analysis focuses on whether banks' risk appetite will remain subdued, even as profitability declines.

## 2. Private Sectors Are In A Surplus Position



## 3. Margin Pressure Continues



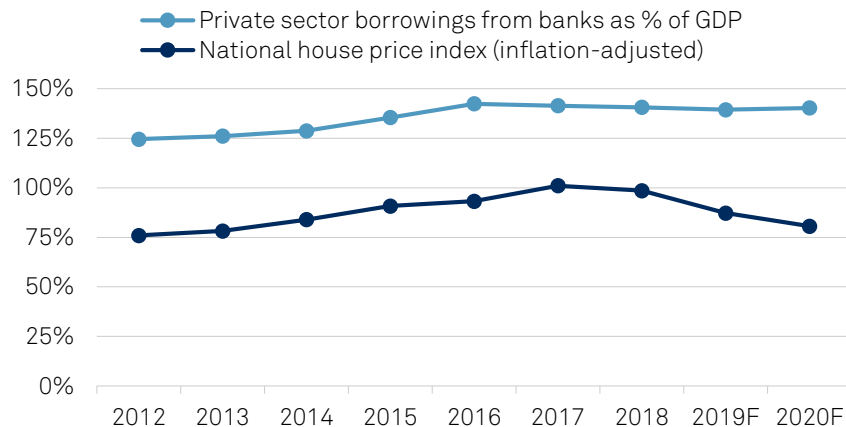
Sources: Government data, S&P Global Ratings analysis. 2. \*Domestic banks. 2018 data is estimated. F--Forecast.

# Australia: Imbalances Ease

## Outlooks On Major Banks Now Stable

Our outlooks on major banks was revised to stable following the announcement of APRA that it is proceeding with its resolution plan. We believe that the government will remain highly supportive of the country's systemically important banks. We expect that the banks would predominantly use tier-2 capital instruments to strengthen their loss absorbing capacity.

## Imbalances in Australia Show Signs of Easing



Note: National house price index: March 2012 = 100. F--Forecast.  
Source: S&P Global Ratings.

## Fintech Flags Turning Point For Australian Banks

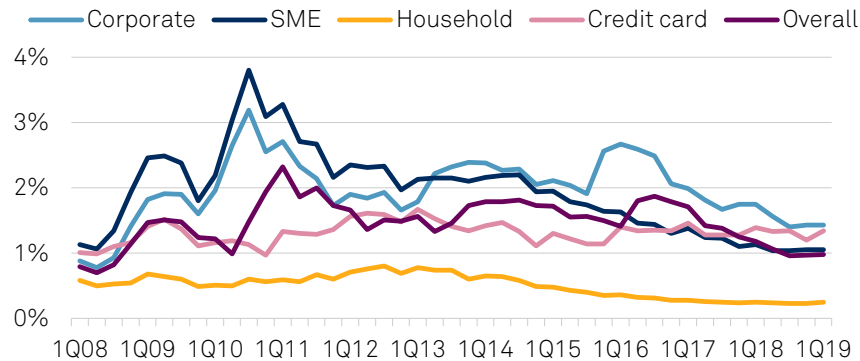
Technological capabilities are becoming increasingly important for banks--influencing cost base, product offerings, and risk management capabilities. It may ultimately weaken banks' competitive dynamics and credit quality.

Open banking and data driven analysis	Digital banking and cloud-based infrastructure	Regulatory technology (regtech)
Increased competition driven by tailored product offerings	Significant cost savings	Addresses shortcomings in monitoring of nonfinancial risks highlighted by the Royal Commission and Austrac findings into CBA
Data management system upgrades to comply with open banking requirements	Accelerating innovation driven by lower product adoption costs	Role in managing nonfinancial risks in a cost-efficient way
Reduced reliance on standardized benchmarks	Improved operational stability in the long run	
	Resurgence in online banking	

Economic imbalances remain elevated. However, low credit growth and small falls in house prices in the past year, along with our expectation that credit losses will remain very low, suggest an orderly unwinding of risks.

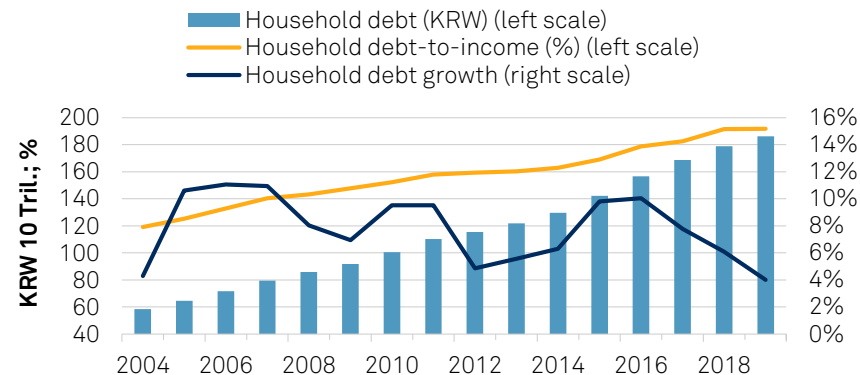
# Korea: Navigating Uncertain Conditions

## 1. Asset Quality Improvement: NPLs By Loan Type



- Adequate capitalization backed by moderate loan growth of about 5% and largely stable profitability, despite the U.S.-China trade conflict and weaker domestic housing demand.
- Potential credit risks mitigated by an overall improvement in asset quality in recent years.
- High household debt (at about 100% of GDP) remains a key risk.
- A resolution regime that includes the bail-in of senior creditors may result in some downgrades of systemically important banks.

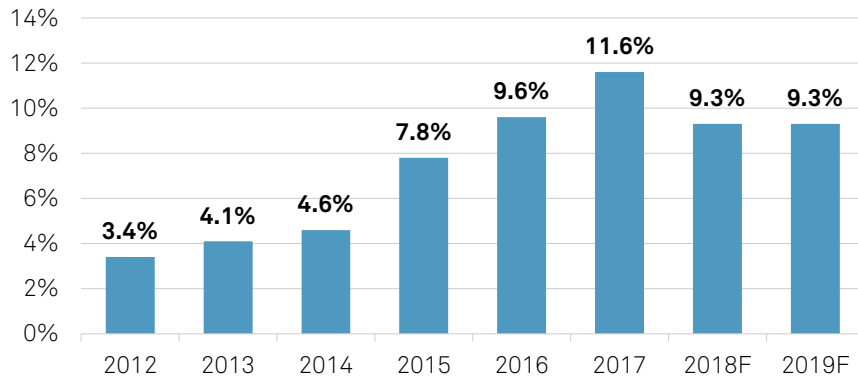
## 2. Household Debt And Debt-To-Income On The Rise



Source: Bank of Korea, S&P Global Ratings. 2. KRW--Korean Won. 2019 data is forecast.

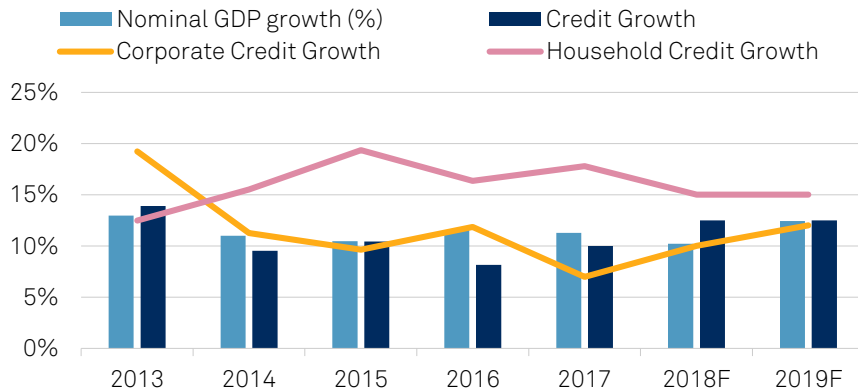
# India: Slow Recovery

## 1. NPL Recognition Largely Done

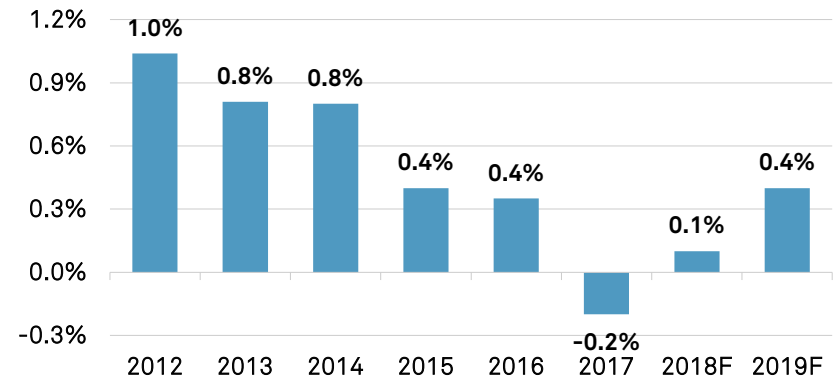


- Developers, finance companies, and promoters with pledged shares are stressed and could delay recovery.
- Some public banks will continue to report losses in 2019. Capital support from the government is vital to ensure the cleanup of their balance sheets.
- Profitability of finance companies is under pressure as the cycle of easy liquidity and low cost of funds has reversed.

## 2. Loan Growth To Pick Up



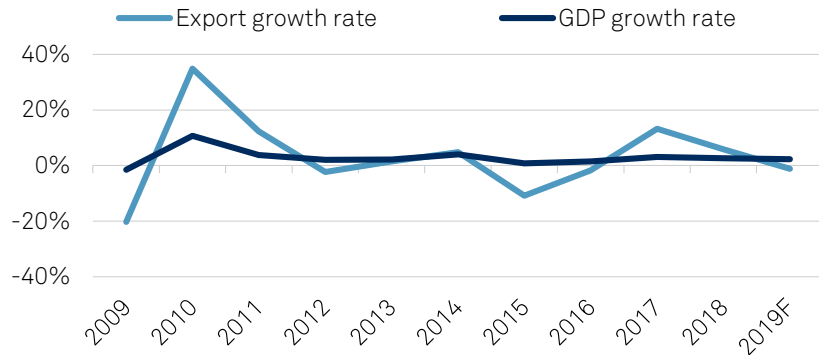
## 3. Positive Earnings To Resume In 2019 - ROA



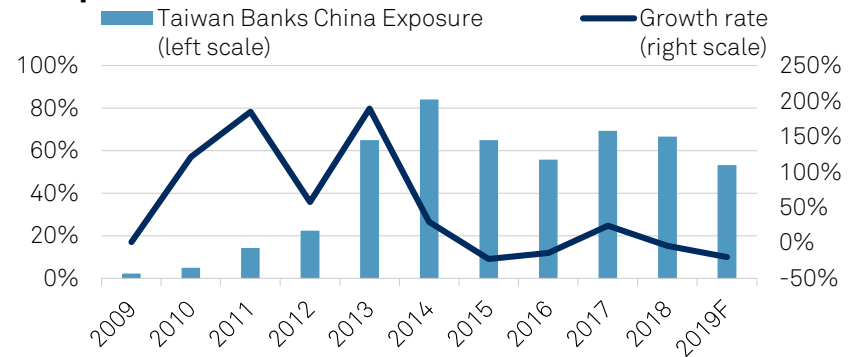
F--Forecast. Sources: Reserve Bank of India, Bank reports, S&P Global Ratings.

# Taiwan: Trade Tension Uncertainty

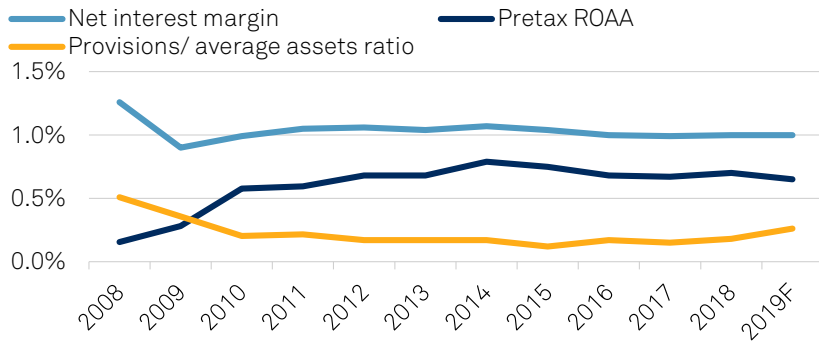
## 1. Worsening U.S.- China Trade Rhetoric Casts A Shadow Over Taiwan's Export-Oriented Economy



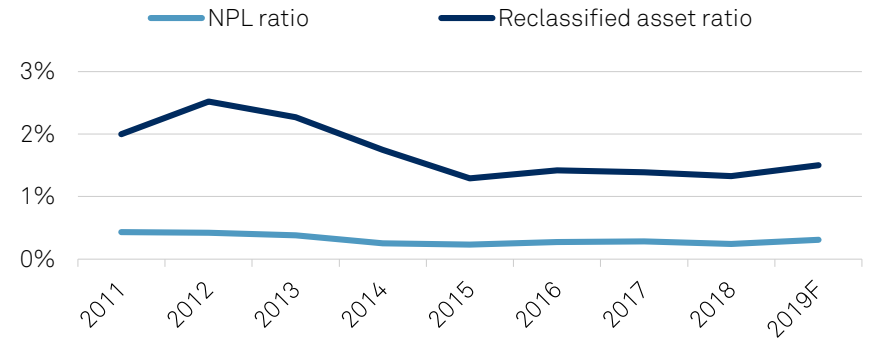
## 2. Banks Will Remain Cautious About Credit Exposure To China In 2019



## 3. Profitability Constrained By Low Interest Rates, Competition, And Potential Rise In Credit Costs



## 4. Weaker Economic Prospects Pressure Asset Quality



F--Forecast. 1. Sources: National Statistics R.O.C., S&P Global Ratings. 2. Note: Total exposure includes loans, investments and interbank activities. Source: Taiwan Central Bank. 3. ROAA--Return on average assets. LLP--Loan loss provision. Sources: Taiwan's Financial Supervisory Commission (TFSC), Taiwan Ratings Corp. 4. Note: Nonperforming loans (NPL) ratio based on regulatory definition. Reclassified asset ratio based on the regulatory definition of type II-V assets. Source: TFSC.



# Hong Kong: Well-Placed Against Headwinds

## Despite Risks, Banks To Maintain Their Credit Profiles

- The impact of trade tensions is limited to a slowdown in revenue, mainly from trade finance activities.
- Risks from a sharp rise in interest rates have subsided for now. Credit risks from mainland to be reasonably contained.
- Property prices continue to rise after a 10% drop at its peak in August 2018. The banking sector has withstood property market cycles with good resilience. A correction in prices will likely have a limited effect on the quality of property-related loans.

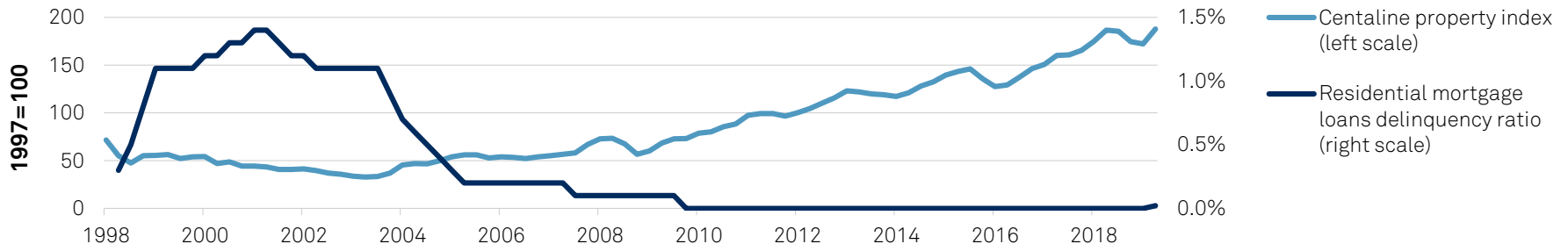
## Government Support Is Still Anticipated

- Banks (Resolution) loss-absorbing capacity (LAC) requirements took effect on Dec. 14, 2018.
- Hong Kong and Canada are the two countries with effective resolution regimes, with systemic banks likely to benefit from government support.

## Virtual Bank Licenses Will Rejuvenate The Sector

- Eight banks were granted virtual bank licenses. They could become a new growth engine as they compete fiercely with traditional banks.
- A low-cost model should allow wider access to previously underserved customers.

## Hong Kong Delinquencies Remained Low Even After The 1997 Housing Crash



Sources: Bloomberg, Centa-City Index, Hong Kong Monetary Authority, S&P Global Ratings.

# Latin American Banks

## Key Expectations

- Credit growth to be modest as political uncertainties and muted economic performance have softened business confidence in several countries.
- Asset quality is to stabilize in Brazil, Peru, Chile, and Colombia.

## Key Assumptions

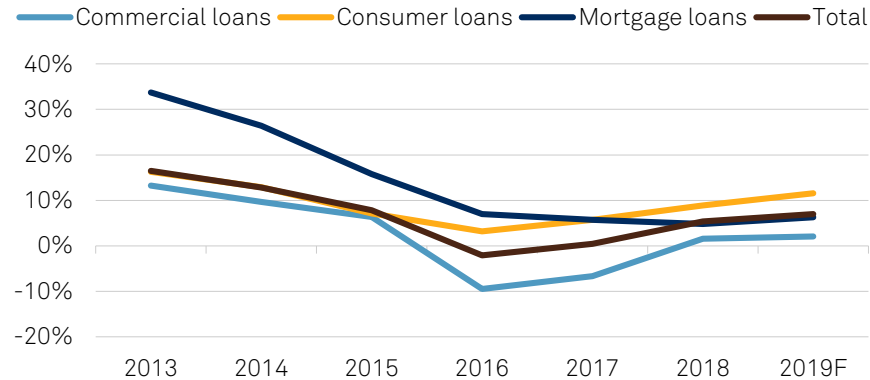
- Low dependence on external funding, high liquidity, and customer deposit funding will help banks withstand potential volatility.
- Credit losses will stabilize or improve, except for Argentinian and Mexican banks.

## Key Risks

- Changes in economic policies in Mexico, difficulties in passing reforms in Brazil, the presidential election in Argentina, and political turbulence and corruption investigations in Peru pose risks to banks.
- Weak investor confidence and economic growth in Mexico could weaken asset quality and credit supply.
- Cybersecurity is a rising threat, as seen in recent attacks on institutions in Mexico and Chile.
- High inflation and interest rates in Argentina, coupled with softening economic conditions, could hinder household debt payment capacity at a greater pace than we expect.

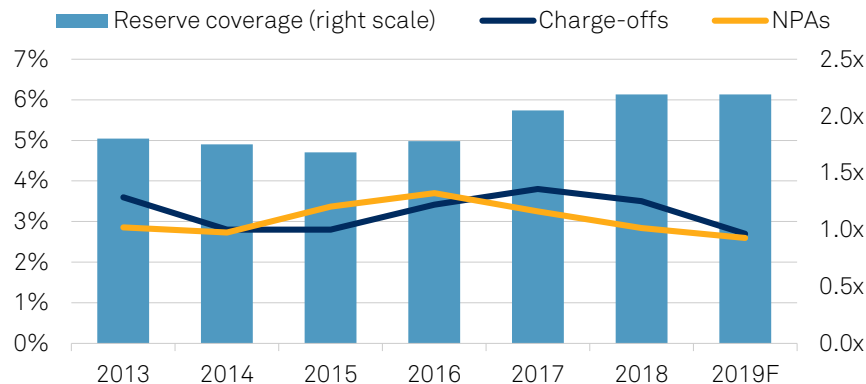
# Brazil: Disappointing Economy

## 1. Credit Growth

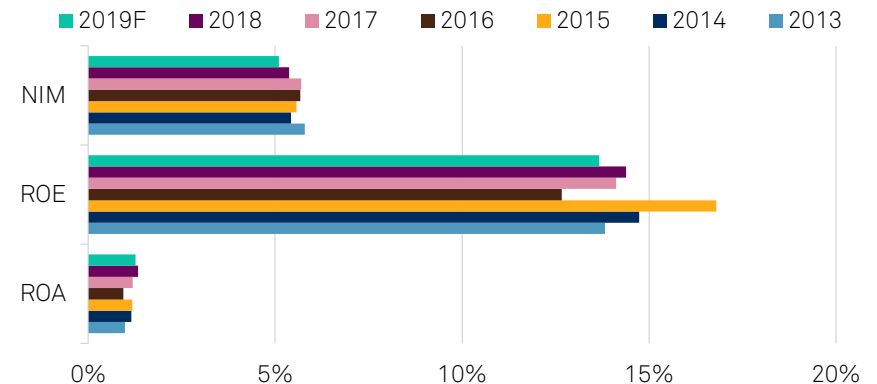


- Political uncertainties and weaker-than-expected economic performance in the first quarter have softened business confidence.
- Credit growth will moderate in 2019 to 6%-8%, with the corporate sector continuing to deleverage.
- Nonperforming loans have narrowed from a peak of 3.5% in 2017 to 3.0% in March 2019. We expect them to decrease to 2.6% in 2019-2020.
- High interest margins and provisioning coverage will help banks continue posting solid results.

## 2. Asset Quality Metrics



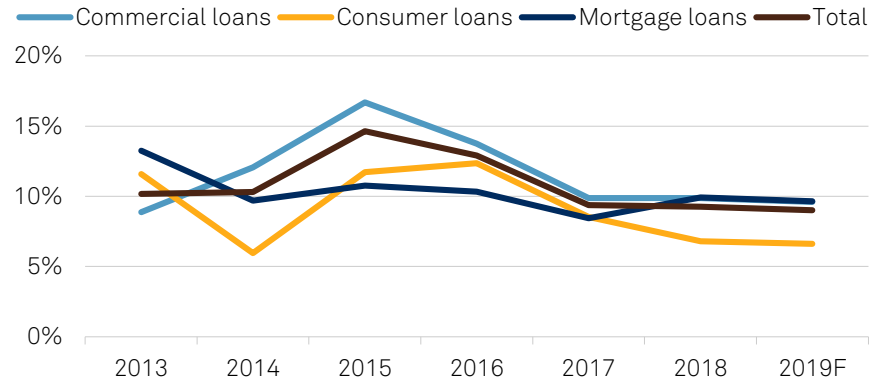
## 3. Profitability



F--Forecast. NPAs--Nonperforming assets. NIM--Net interest margin. ROE--Return on equity. ROA--Return on assets.  
Source: S&P Global Ratings.

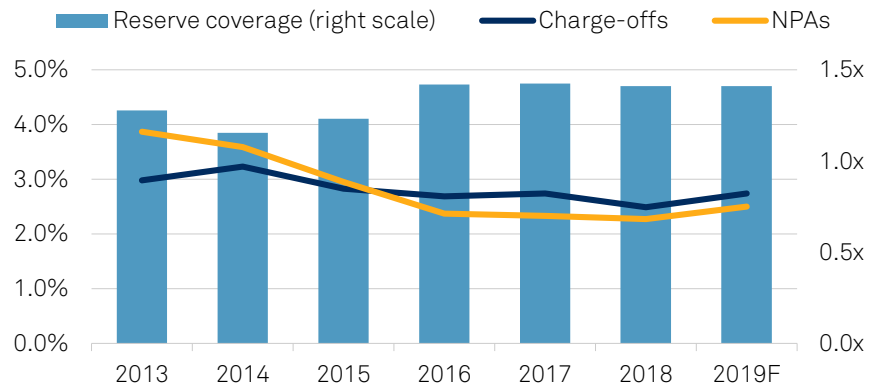
# Mexico: Uncertainties About Government Policies

## 1. Credit Growth

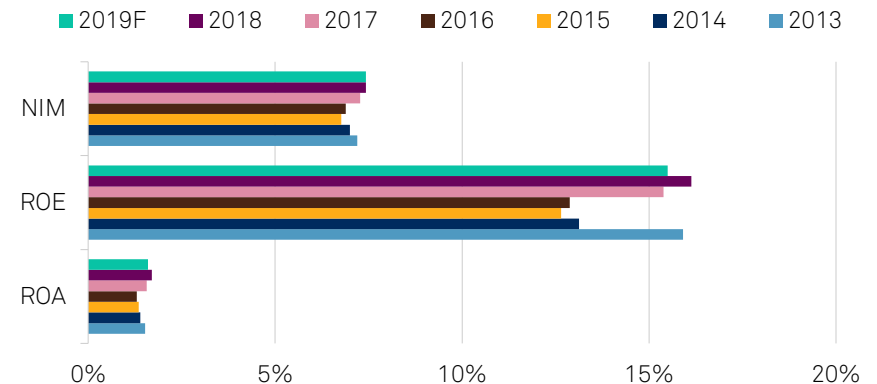


- We're seeing weaker economic growth due to declining investor confidence and uncertainty about the government's energy policy.
- NPAs (which are fully covered by reserves) and charge-offs are to only slightly deteriorate in the next two years due to cautious lending standards.
- Banks are mainly funded through customer deposits.
- Net interest margins are to remain among the highest in the region at more than 7%. Profitability is also supported by healthy asset quality.
- The banking system remains well-capitalized.

## 2. Asset Quality Metrics



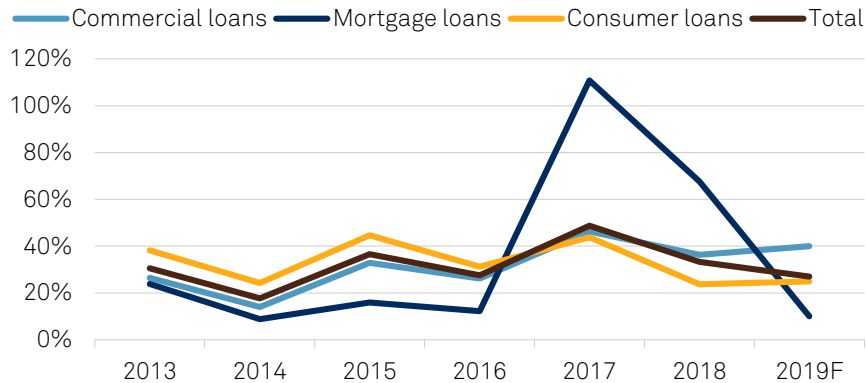
## 3. Profitability



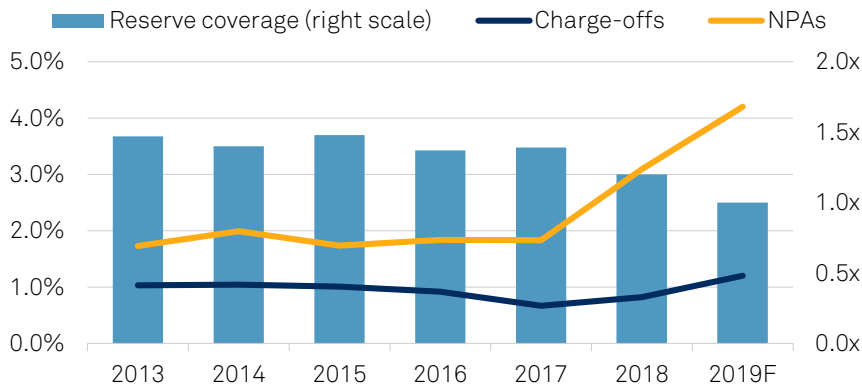
F--Forecast. NPAs--Nonperforming assets. NIM--Net interest margin. ROE--Return on equity. ROA--Return on assets.  
Source: S&P Global Ratings.

# Argentina: Well Positioned Against Struggles

## 1. Credit Growth

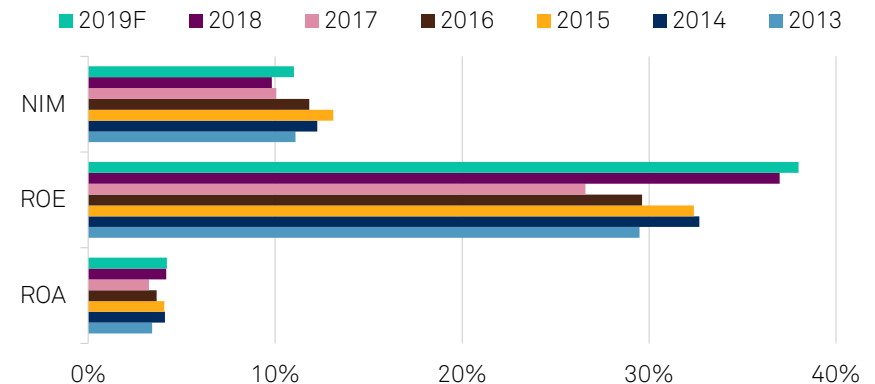


## 2. Asset Quality Metrics



- The plan to reduce the fiscal deficit under the IMF program has taken a hit on the economy, exacerbated by the upcoming presidential election. Loan portfolios are decreasing in real terms due to tightening underwriting.
- We see a manageable deterioration of asset quality in the corporate and consumer segments. Low banking penetration (credits to GDP is below 15%), limited exposure to cyclical segments, healthy margins, and limited FX open positions are helping banks overcome the difficult situation.
- Funding stability is supported by high level of liquidity.

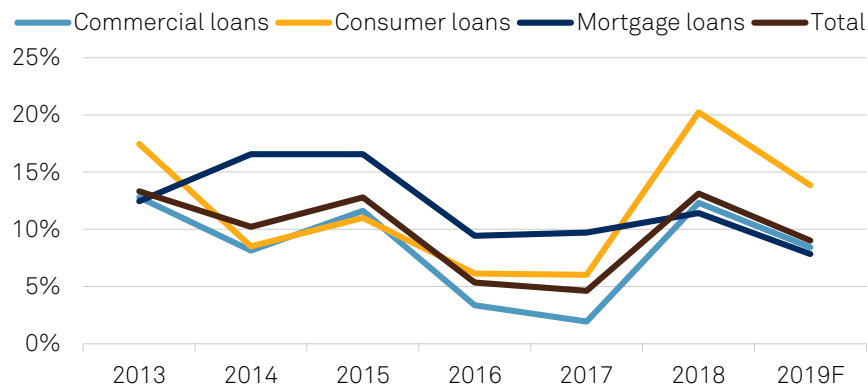
## 3. Profitability



F--Forecast. NPAs--Nonperforming assets. NIM--Net interest margin. ROE--Return on equity. ROA--Return on assets.  
Source: S&P Global Ratings.

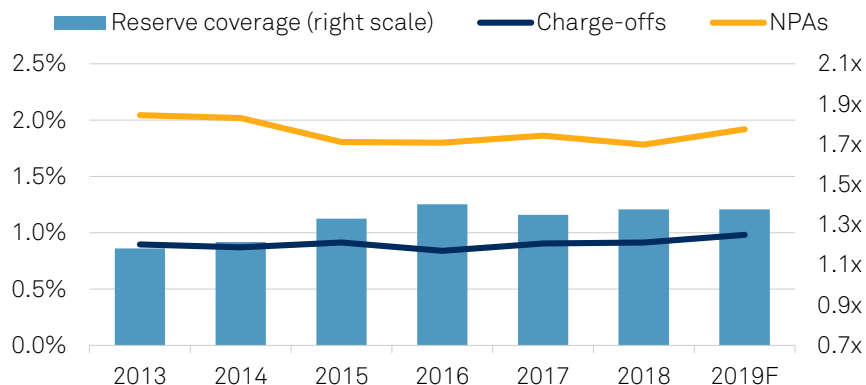
# Chile: Stability In A Healthy Environment

## 1. Credit Growth

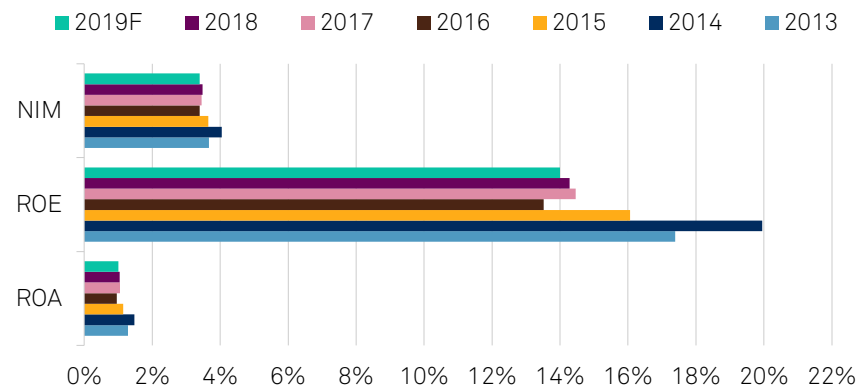


- Economic growth and business confidence remain supportive for the banking sector.
- We expect loan growth to be about 9% in 2019.
- Rather stable economic conditions should help the system maintain healthy asset quality metrics, with NPAs at about 2%.
- We expect profitability to slightly weaken due to lower margins, with ROE of about 14% in 2019.

## 2. Asset Quality Metrics



## 3. Profitability

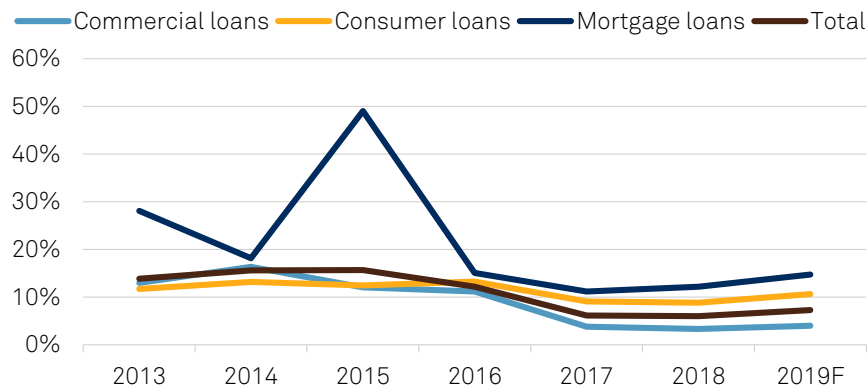


F--Forecast. NPAs--Nonperforming assets. NIM--Net interest margin. ROE--Return on equity. ROA--Return on assets.

Source: S&P Global Ratings.

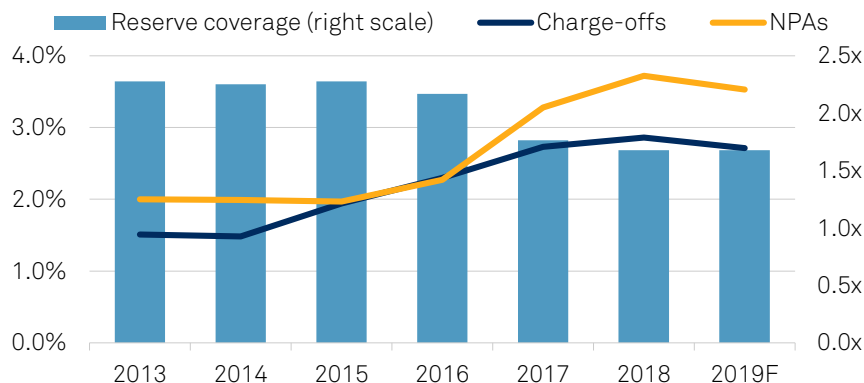
# Colombia: Easing Pressure On Asset Quality

## 1. Credit Growth

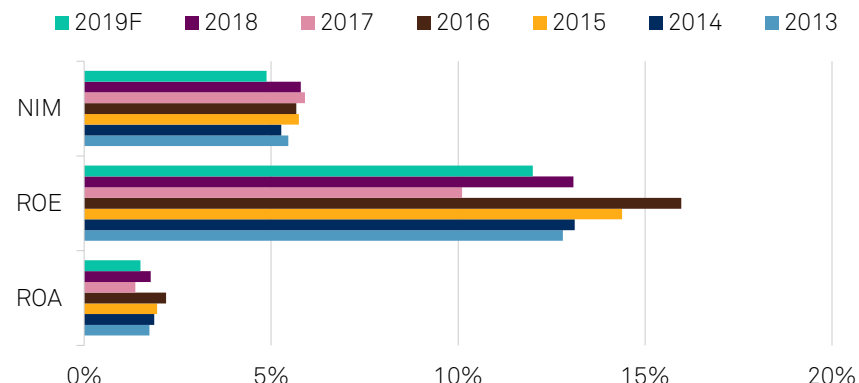


- Consumer and mortgage loans will continue to support credit growth, reflecting improving consumer confidence and private consumption.
- The NPA ratio is to stabilize at about 3.5% in 2019-2020 because of improving conditions and higher credit demand.
- Profitability is to remain sound, mitigating pressure from potential increases in interest rates and provisioning.
- Low retail deposits remain a weakness compared with those of other regional banking sectors.

## 2. Asset Quality Metrics



## 3. Profitability



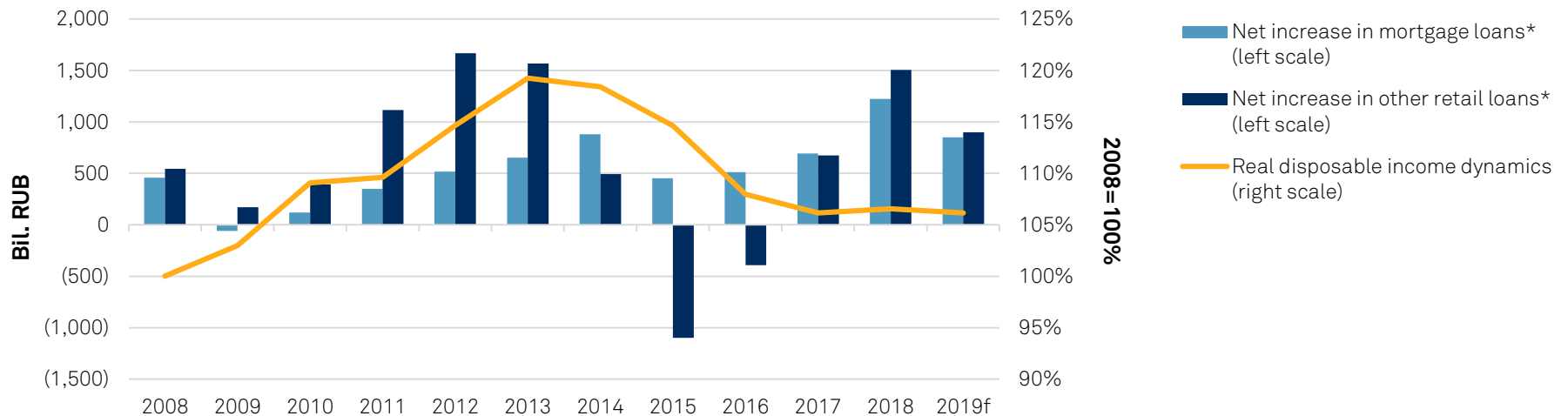
F--Forecast. NPAs--Nonperforming assets. NIM--Net interest margin. ROE--Return on equity. ROA--Return on assets.

Source: S&P Global Ratings.

# Russia: Retail Lending Supports Growth

- Growth in retail lending is driving the pickup in lending since 2017.
- State banks will retain their dominant market position, with increasing competitive pressure on smaller banks.
- Domestic deposits remain the key source of funding. Their stability is dependent on the recovery of macroeconomic fundamentals, and they are vulnerable to additional sanctions.
- Domestic capital markets remain undeveloped, and limited access to external markets continues to restrict banks and their borrowers to access long-term funding.
- Capitalization of the sector remains weaker than many peers', especially when nonperforming and restructured loans are taken into account.

## Growth In Retail Lending And Disposable Income Dynamics In Russia, 2008 - 2019



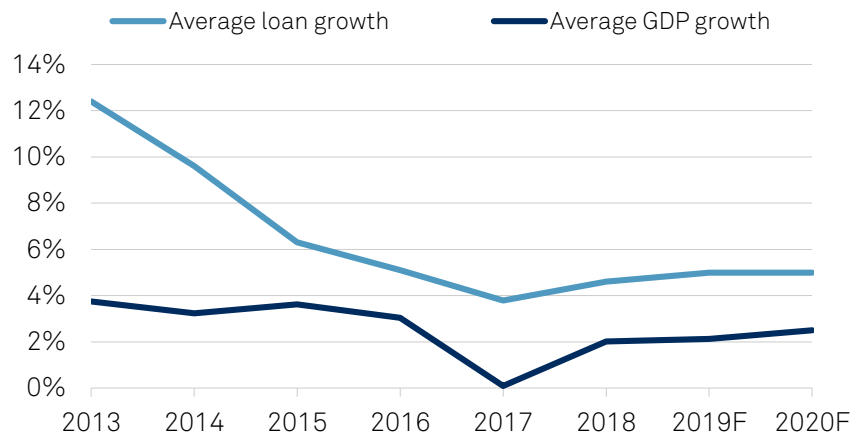
\*Including repayments within the period. RUB--Russian ruble. Sources: CBR, Russian Federal State Statistics Service, S&P Global Ratings.



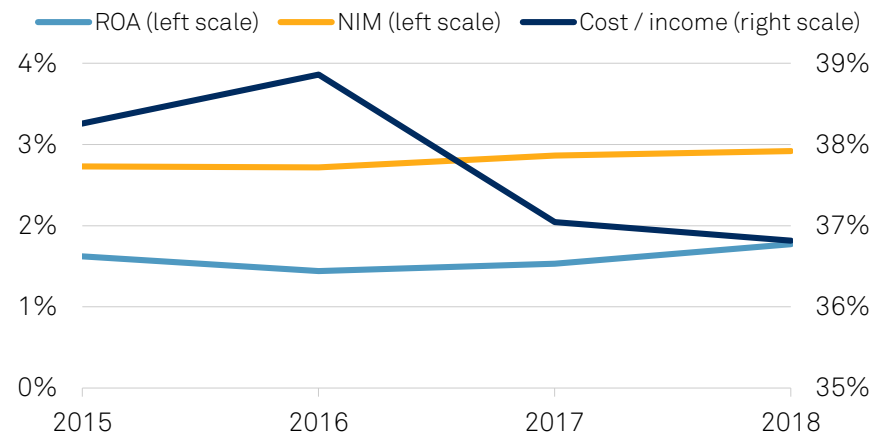
# GCC: Geopolitics And Oil Are Key

- Financial profiles should remain stable for the remainder of 2019 and 2020, absent any unexpected geopolitical shock or significant drop in oil prices.
- Lending growth should stabilize at 4%-6% as public investments support growth.
- Returns on assets and net interest margins are to benefit from stable interest rates and significant noninterest bearing deposits.
- Exposure to Turkey is a source of risk.
- Stage 2 loans in countries like Qatar and Oman reveal some challenges given the stress on both economies. We expect problematic loans (Stage 2 and Stage 3) to remain stable at about 15% of total loans over the next 12-24 months.

## Growth Of Loan Portfolios Versus GDP



## Rated GCC Banks Profitability Indicators

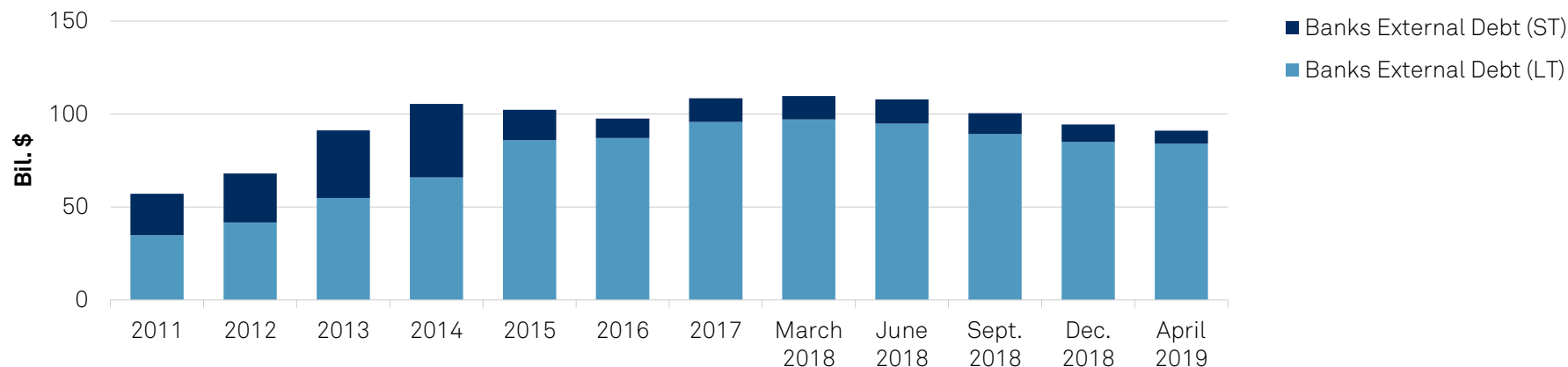


F--Forecast. ROA--Return on assets. NIM--Net interest margin. Sources: S&P Global Ratings, GCC Central Banks.

# Turkey: External Debt Is Key Risk

- Banks' external debt is declining with lower rollover rates, higher cost, and concerns from investors about the country's policy direction.
- Foreign currency liquid assets increased slightly in 2019 (to more than \$100 billion) and provide some leeway for banks to withstand more stress. However, a lower rollover rate might displace the problems to the central bank's balance sheet.
- Risks to banks include weakening asset quality and capitalization. The government announced a TRY28 billion capital injection into state banks and the creation of two funds to take over some nonperforming loans in the construction and energy sectors.
- We expect nonperforming loans to double over 2019 and 2020 to 6%-8%, and problematic loans (which include restructured loans) to climb to about 20%.

## Turkish Banks' Commercial External Debt

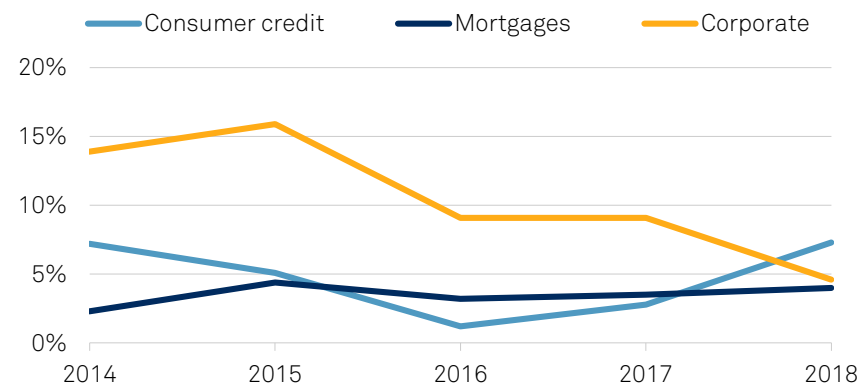


Source: S&P Global Ratings.

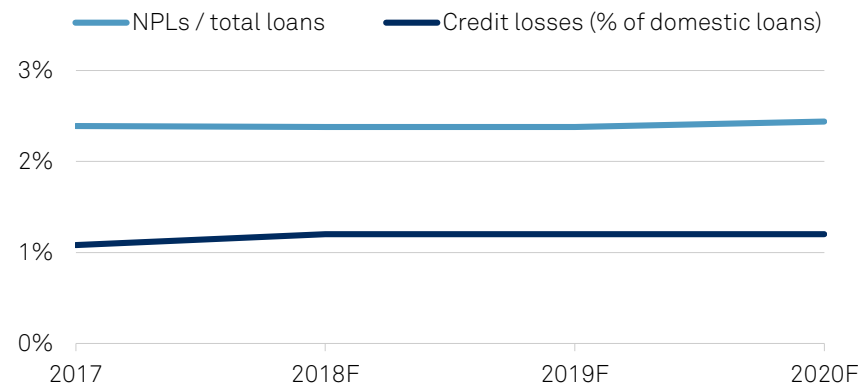
# South Africa: Weak Economic Growth

- Economic growth remains below peers', with real GDP growth to average 1.5%-2.0% over 2019-2020. We expect very modest growth in retail lending as low economic growth, rising unemployment, and political uncertainties hurt consumer confidence.
- The sector is not exposed to external refinancing risk, unlike other emerging-market peers.
- We expect good earnings resilience in 2019-2020. Banks have historically displayed strong returns with recurring fee income and good risk control.
- Domestic households are the main risk because of relatively high leverage and low wealth levels. There is some room for deterioration in corporate book quality, especially for small businesses.
- Commercial real estate continues to exhibit lower credit losses. Credit risk may be building given the rise in office vacancy rates and lower consumer spending. We see signs of stress in the construction and retail industries.
- Provisions are to increase mildly due to the adoption of IFRS 9.

## South African Banks Lending Growth



## Asset Quality Remains Under Control



NPLs--Nonperforming loans. F--Forecast. Source: S&P Global Ratings.

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# Analytical Contacts



## Global FI Sector Lead

### Emmanuel Volland

Paris  
+33 1 4420 6696  
emmanuel.volland  
@spglobal.com



## North America

### Brendan Browne

New York  
+1 212 438 7399  
brendan.browne  
@spglobal.com



## Latin America

### Cynthia Cohen Freue

Buenos Aires  
+54 11 4891 2161  
cynthia.cohenfreue  
@spglobal.com



## Western Europe

### Elena Iparraguirre

Madrid  
+34 91 389 6963  
elena.iparraguirre  
@spglobal.com



## Russia & CIS

### Natalia Yalovskaya

London  
+44 20 7176 3407  
natalia.yalovskaya  
@spglobal.com



## Western Europe

### Osman Sattar

London  
+44 20 7176 7198  
osman.sattar  
@spglobal.com



## Asia Pacific

### Gavin Gunning

Melbourne  
+61 3 9631 2092  
gavin.gunning  
@spglobal.com



## Middle East & Africa

### Mohamed Damak

Dubai  
+971 4372 7153  
mohamed.damak  
@spglobal.com

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