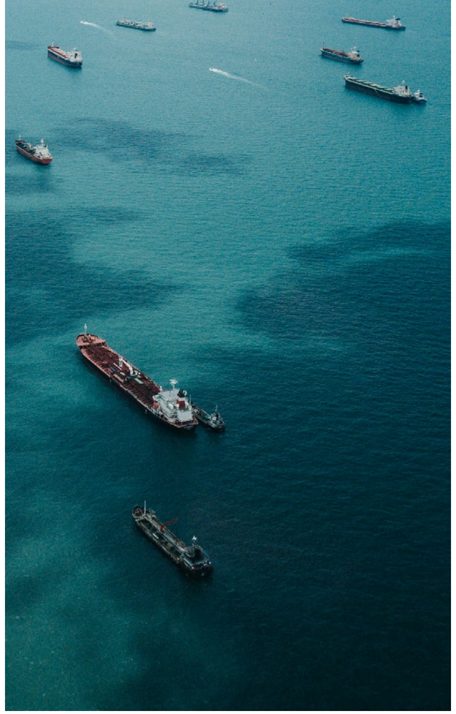
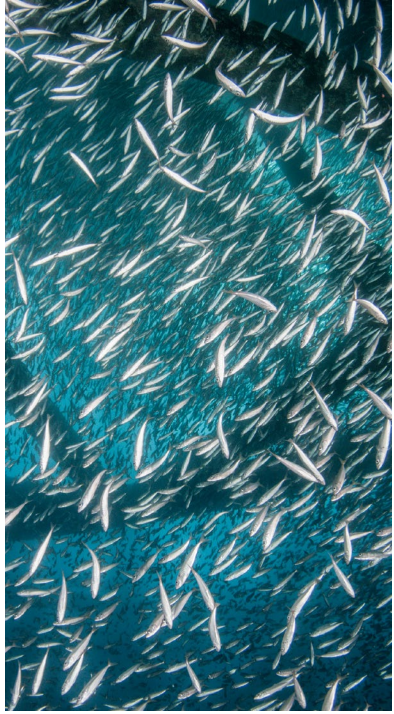


Global Banks Midyear Outlook 2024

Searching For Calmer Waters

July 17, 2024

S&P Global Ratings

This report does not constitute a rating action

Contents

Key Takeaways

- Our outlook for global banks remains steady. As of June 30, 2024, about 75% of bank rating outlooks were stable. This resilience is largely due to solid capitalization, improved profitability, and still sound asset quality.
- That said, the slow economic growth expected in the second half of the year--while rates remain elevated--presents headwinds for business volumes, asset quality, and financing conditions.
- In addition, elections (more than 70 in about 40 countries in 2024), and the Russia-Ukraine and Israel-Hamas wars bring spillover risks, including market volatility. Positively, most banks' earnings continue to benefit from high interest rates and limited credit losses.
- Commercial real estate (CRE) markets are suffering a significant downturn in some jurisdictions, especially in the U.S., China, and a few European countries. Related credit losses are increasing but should be manageable for most.
- We anticipate credit divergence to continue. Pressure will remain more pronounced for nonbank financial institutions and entities with weak funding profiles or those that are more exposed to geopolitical, political, or CRE risks.

Key Risks

Deviation from our economic base case

The risks around our baseline include a sharp reduction in labor demand and spillovers from a strong U.S. dollar, as well as geopolitics, that could lead to a hard landing.

Greater property sector deterioration

Acceleration of weakness in CRE markets, ultimately hurting banks' asset quality more than expected. These risks remain greatest within the U.S. office sector.

High corporate and government-sector leverage

This could exacerbate corporate insolvencies and trigger lower government support for the real economy.

Digitalization, Generative AI, climate change, and cyber to challenge business models and risk management

Nontraditional risks increasingly add to the usual credit, market, funding, and operational risks.

BICRA Developments In 2024

January

Macao
Assigned BICRA Group '5', ER and IR scores of '5'

February

March

Kazakhstan
ER score to '7' from '8', and IR trend to positive from stable

Portugal
ER score to '5' from '6', IR trend to positive from stable

April

Armenia
ER score to '7' from '8', and ER trend to stable from positive

Australia
BICRA to Group '2' from Group '3', IR score to '2' from '3', and IR trend to stable from positive

Iceland
BICRA to Group '4' from Group '5', ER score to '4' from '5', and ER trend to stable from positive

April

Kenya
Assigned BICRA Group '9', ER and IR scores of '9'

Spain
IR trend to positive from stable

May

Israel
BICRA to Group '4' from Group '3', and ER score to '4' from '3'

Czech Republic
ER trend to stable from negative

Macao
ER score to '6' from '5'

May

Bosnia and Herzegovina
Assigned BICRA Group '8', ER score of '8' and IR score of '7'

Turkiye
ER trend to positive from stable

Costa Rica
ER trend to positive from stable

June

Italy
IR trend to positive from stable

Iraq
Assigned BICRA Group '10', ER and IR scores of '10'

Panama
ER score to '6' from '5', and ER trend to stable from negative

Cyprus
ER score to '6' from '7', ER and IR trends to stable and positive from stable

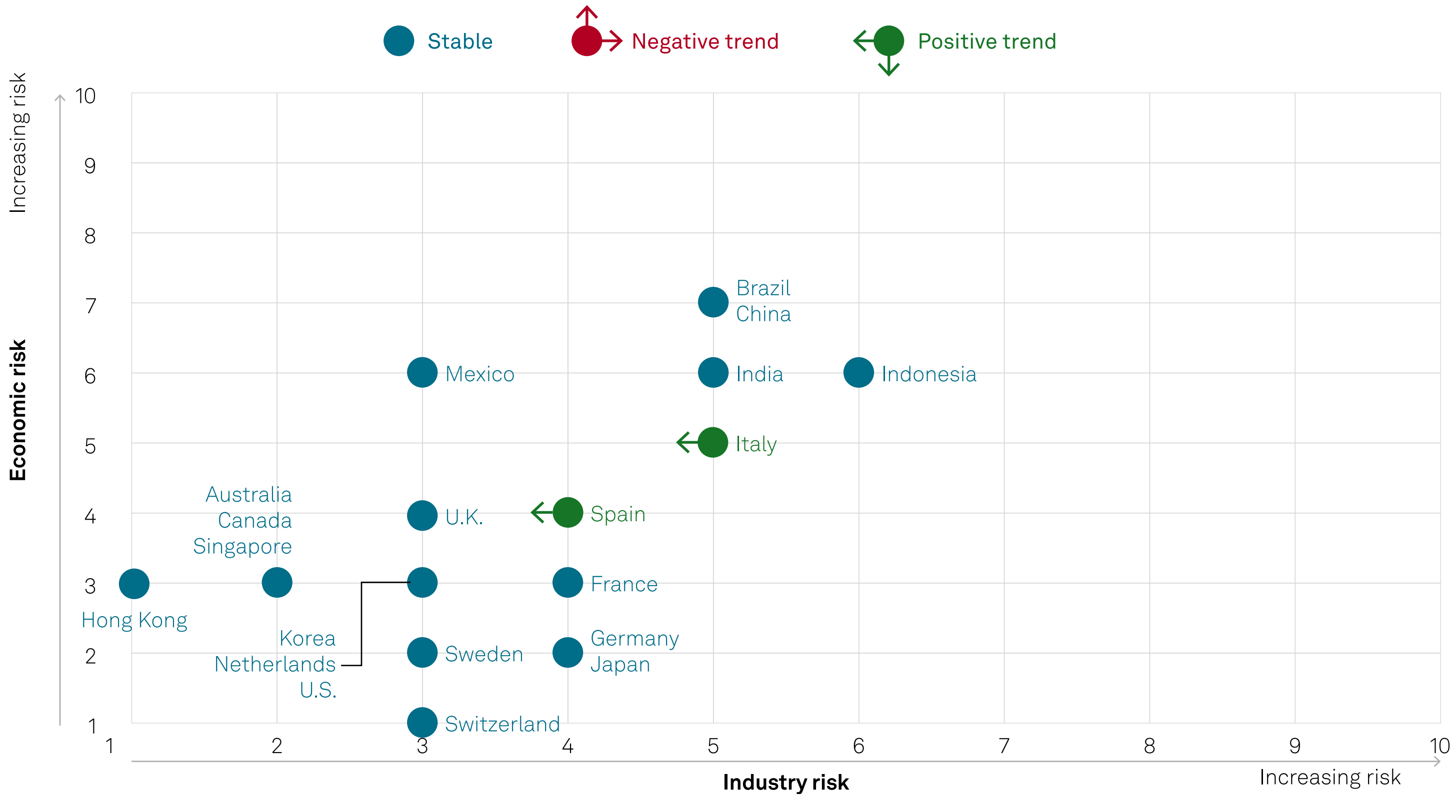
Saudi Arabia
IR score to '4' from '3'

Data as of June 30, 2024. Chart includes changes in BICRA group, industry and economic risk trends and scores. BICRA--Banking Industry Country Risk Assessment. ER--Economic risk. IR--Industry risk. Source: S&P Global Ratings.

BICRA | Stable Trends Dominate

BICRA scores and economic and industry risk trends

Top 20 banking markets



Data as of June 30, 2024. 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). Source: S&P Global Ratings.

BICRA-related changes in the top 20 banking markets: 1H-2024

- **Australia:** BICRA Group 2 from 3 (April)
- **Spain:** Industry risk trend to positive from stable (April)
- **Italy:** Industry risk trend to positive from stable (June)

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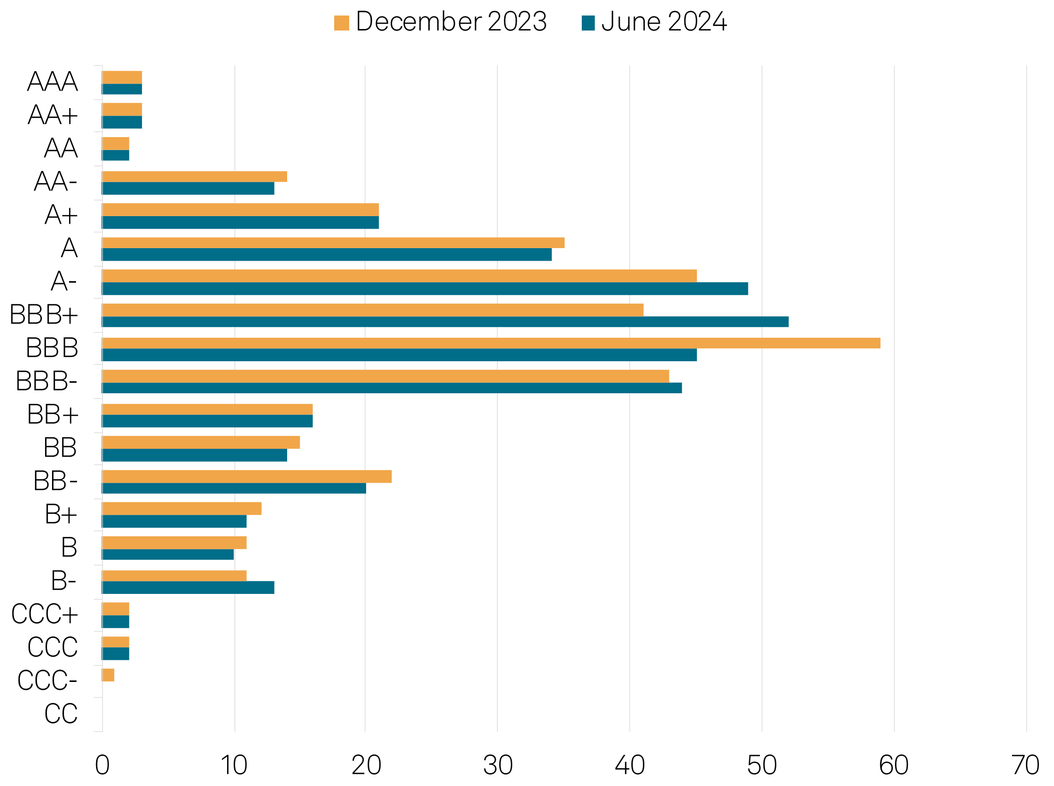
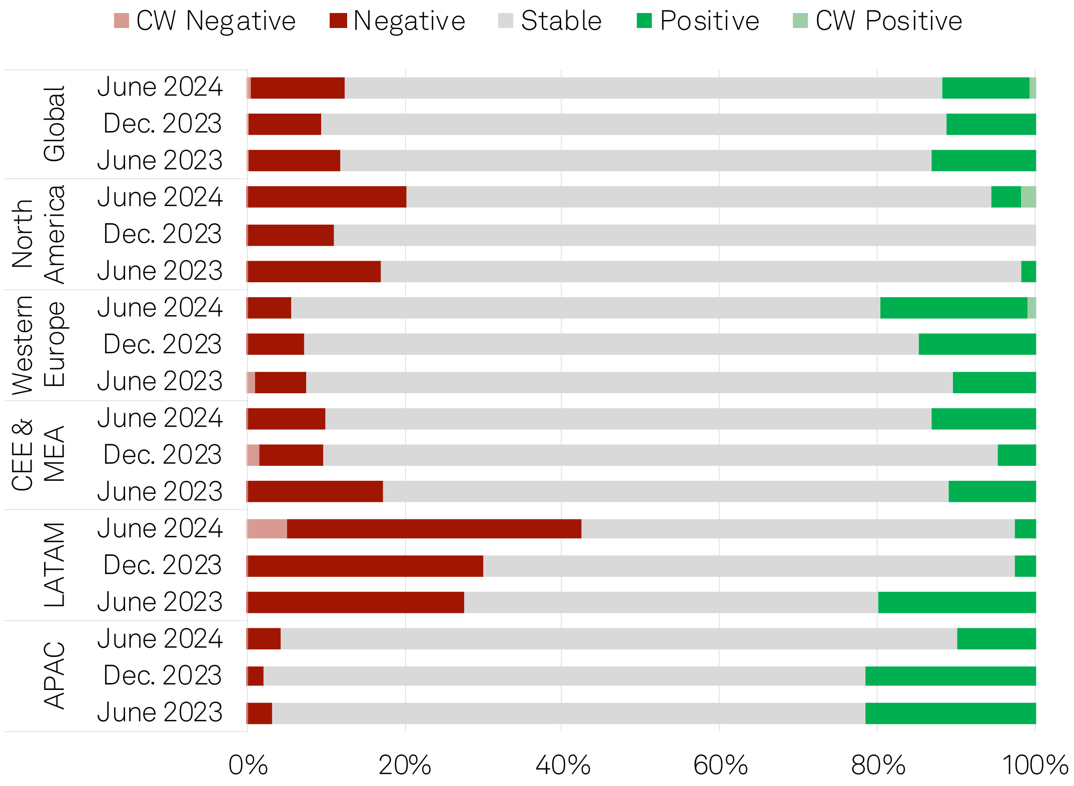
Banks | Generally Stable Outlook

We expect bank ratings to be resilient
Evolution of ratings distribution for rated banks



Operating company issuer credit ratings. Source: S&P Global Ratings.

Bank outlooks are broadly stable
Evolution of outlooks for rated banks by region



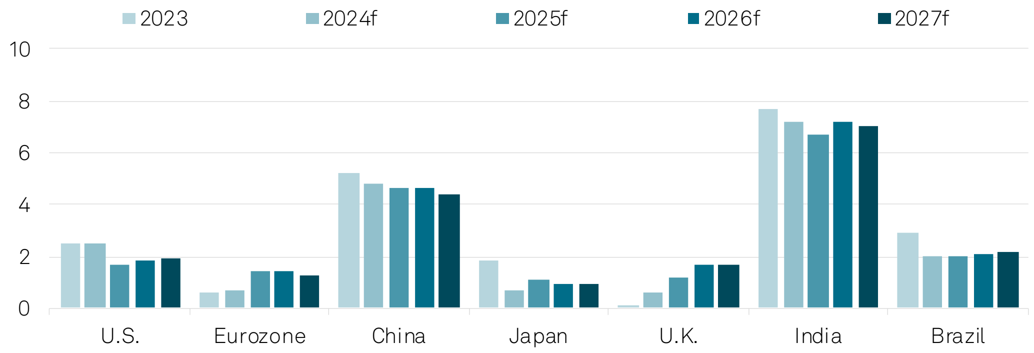
APAC--Asia-Pacific. CEE--Central and Eastern Europe. LATAM--Latin America. MEA--Middle East and Africa. CW--CreditWatch. Source: S&P Global Ratings.

S&P Global Ratings

What We Are Watching In 2H-2024

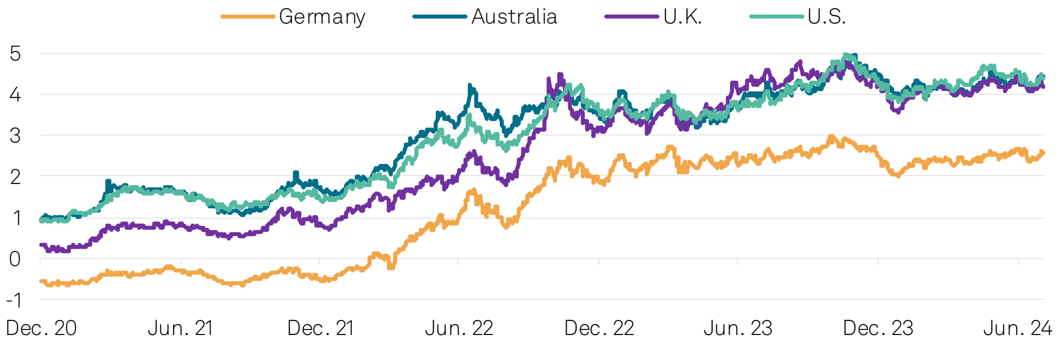
1. How economic conditions will impact banks

GDP growth forecast by country (%)



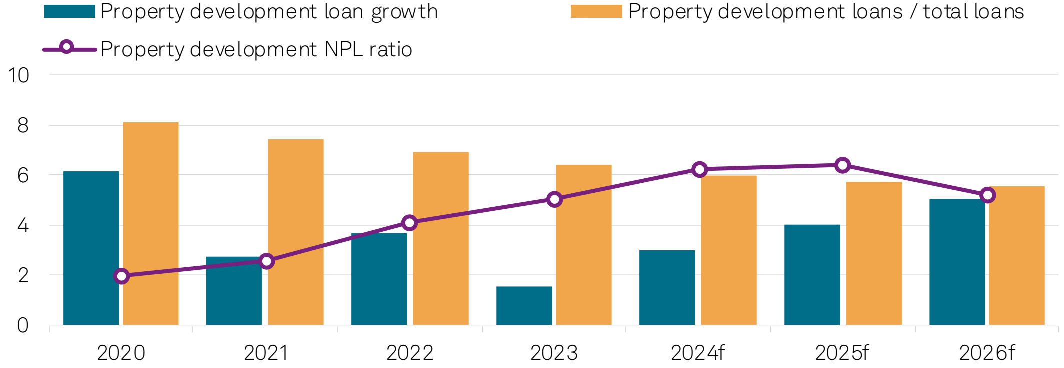
2. How long borrowing costs will remain high

10-year government bond yields (%)



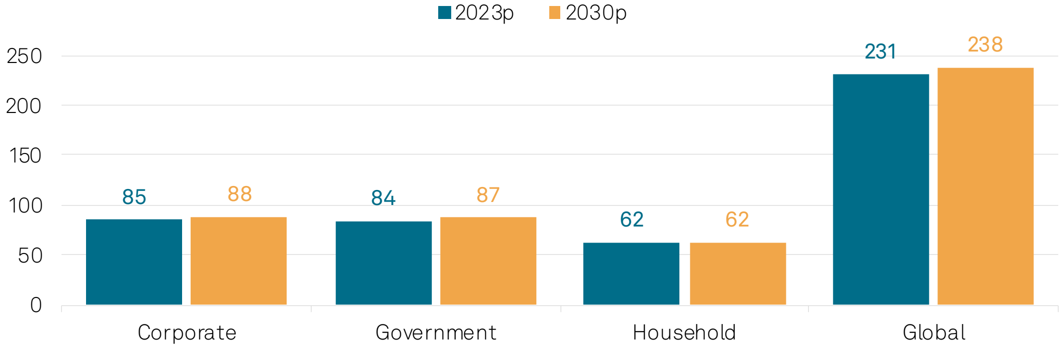
3. How much will property sector affect banks' asset quality

Property development NPLs to peak higher, later for Chinese banks (%)



4. The impact of high debt leverage on bank borrowers

Global debt-to-GDP, 2023 and baseline 2030 (%)



1. For India, fiscal year beginning April 1 in the reference calendar year. f--Forecast. Source: S&P Global Ratings. 2. Sources: S&P Global Market Intelligence. S&P Global Ratings. 3. NPL--Nonperforming loans. Source: S&P Global Ratings. 4. Data compiled Dec. 1, 2023. p--Projected. Source: S&P Global Ratings.

Higher-For-Longer Interest Rates Still Weigh On Economies

- Most economies have seen solid growth in 2024 so far but this may prove a high point. The macro picture indicates a period of subpar growth, and higher-for-longer rates with a slow adjustment back to steady states; this is conditional on strong labor markets.
- Inflation has started to reduce in most markets, but core measures are sticky and remain above central bank targets.
- The main risk is that demand and inflation pressures remain higher and stickier than expected, prompting high policy rates, tight financing conditions, and an eventual hard landing. A worsening geopolitical landscape, a severe economic downturn, a longer-than-expected period of high rates, and growing threats to global trade could derail our base case.

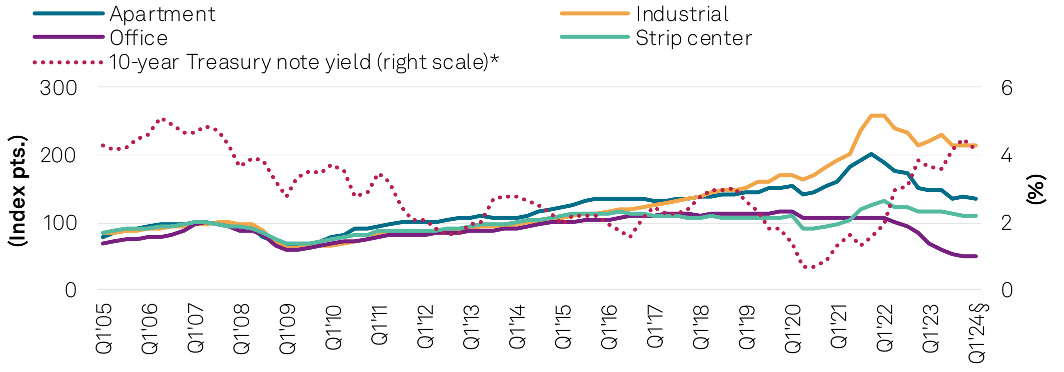
Policy interest rates and S&P Global Ratings' forecasts (%)

	U.S. (Fed)	Eurozone (ECB)		U.K. (BoE)	Switzerland (SNB)
Policy Rates	**Federal funds rate**	**Deposit rate**	**Refi rate**	**Bank rate**	**Policy rate**
2023	5.02	4.00	4.50	5.25	1.75
2024f	5.31	3.25	3.40	4.50	1.00
2025f	4.60	2.50	2.65	3.25	1.00
2026f	3.27	2.50	2.65	3.00	1.00
2027f	2.90	2.50	2.65	3.00	1.00

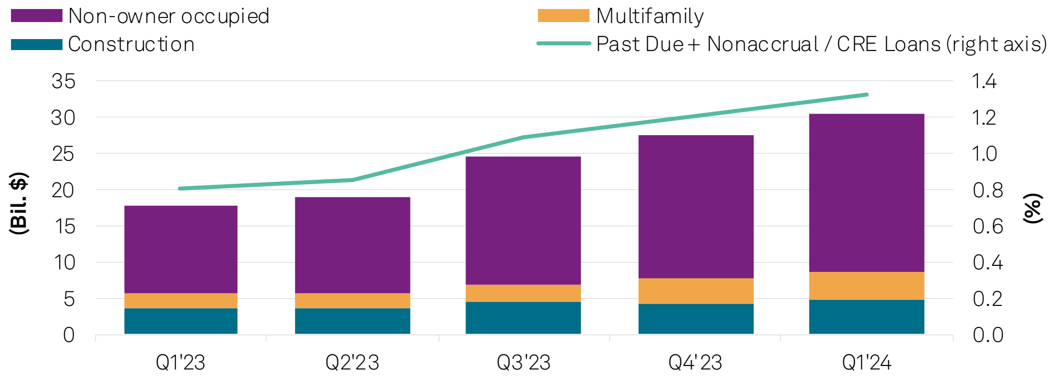
BoE--Bank of England. ECB--European Central Bank. f--S&P Global Ratings forecast. SNB--Swiss National Bank. Percentages are annual averages. Source: S&P Global Ratings Research.

CRE | Still Rising Credit Risk, But Exposures Are Manageable For Most

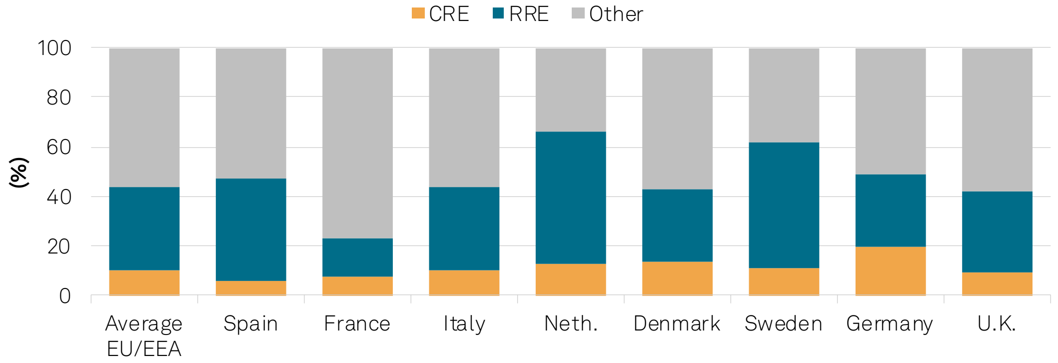
1. U.S. CRE valuations pressured...



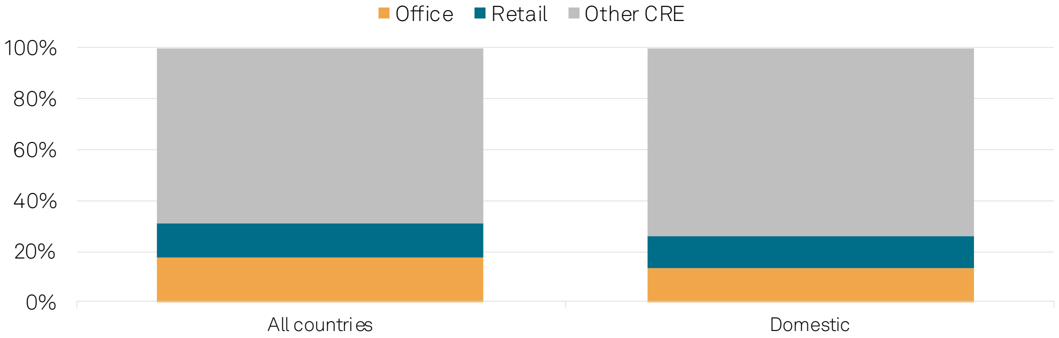
2. ...yet asset quality so far is manageable for U.S. banks.



3. In Europe, CRE amounts to around 10% of bank lending...



4. ...of which office exposures comprise less than 20%



1: Green Street Commercial Property Price Index. The index incorporate the valuations of class 'B' and 'B+' commercial properties. *Reflects the average of daily treasury yields published each quarter. §Data for Q1 2024 ends at March 21, 2024. 2: CRE--Commercial real estate. Bars represent past due loans (defined as any loan at least 30 days past due), and nonaccrual loans. Sources: Regulatory filings, S&P Global Ratings. 3: Data is as end-December 2023. 4: Share of CRE exposures of sample of 32 banks supervised by the ECB, H1 2022. CRE--commercial real estate. RRE--Residential real estate. Sources: Green Street, St. Louis Federal Reserve, U.S. regulatory filings, European Central Bank, S&P Global Ratings.

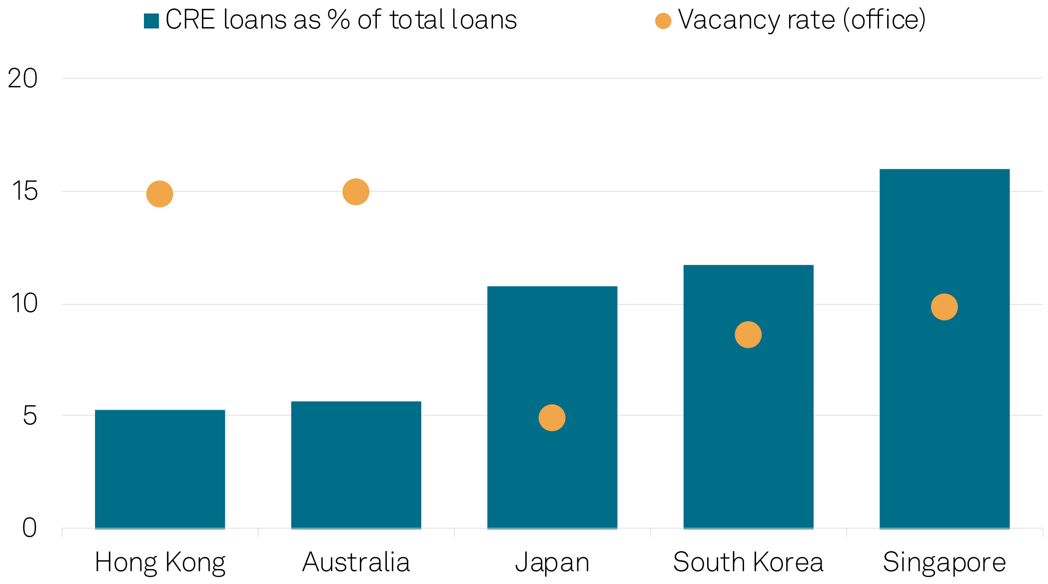
S&P Global Ratings

CRE | Still Rising Credit Risk, But Exposures Are Manageable For Most

- We estimate that major banks in advanced Asia-Pacific economies can comfortably absorb a hypothetical additional 200 basis points in credit losses on CRE exposures.
- This is in addition to our current base case credit losses across their entire loan portfolios (including CRE).

Banks have manageable CRE exposures...

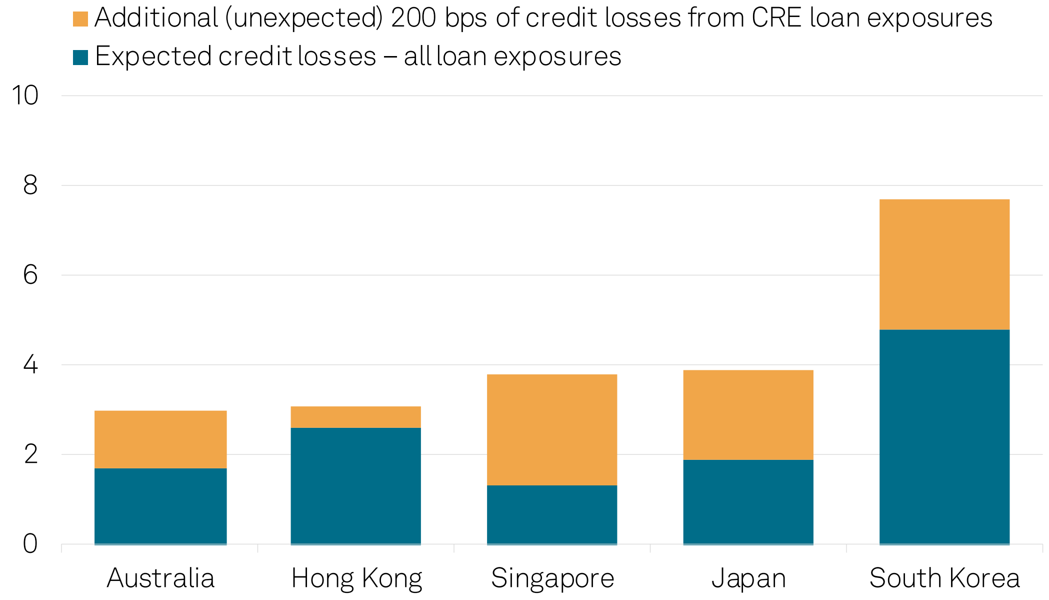
(%)



Data is for 2023 actuals. Commercial property includes income-producing commercial real estate and excludes construction. The chart includes systemically-important banks for each country as a proxy for system data. CRE--Commercial real estate. Source: S&P Global Ratings.

...Even if CRE losses are 200 bps worse than we expect

Credit losses as a percentage of total adjusted capital (%)



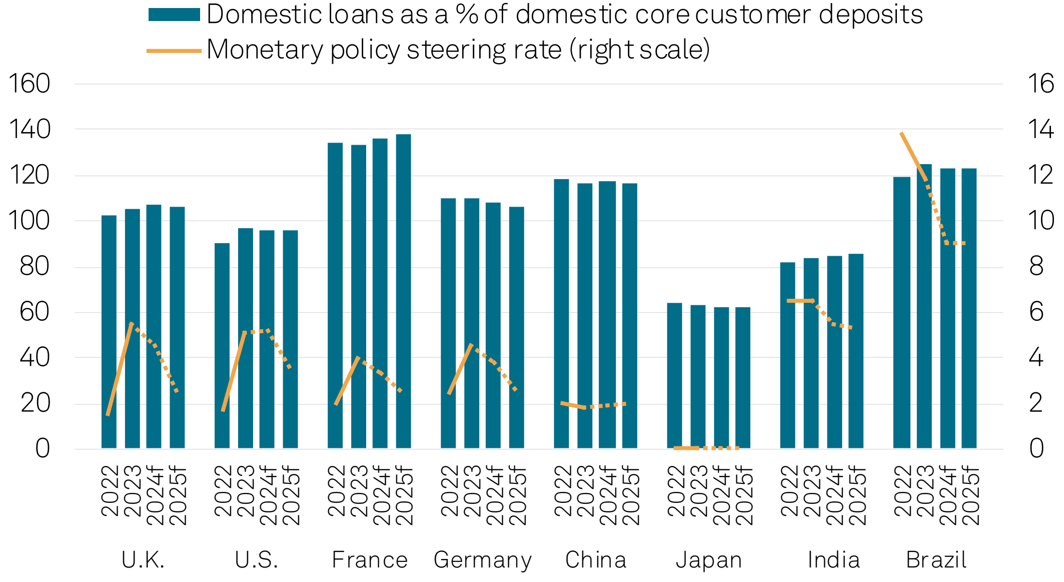
Data is 2024 forecasts. Commercial property includes income-producing commercial real estate and excludes construction. The chart includes systemically-important banks for each country as a proxy for system data. CRE--Commercial real estate. Source: S&P Global Ratings.

Monetary Policy Easing Should Support Funding And Liquidity

- Monetary policy easing should support global banks' funding conditions, although delays in the Federal Reserve's actions could test some banks with weaker funding profiles, especially in the U.S. and emerging markets.
- Liquidity levels appear broadly adequate, but enhancing liquidity risk management remains a priority as banks and regulators draw their lessons from the 2023 banking turmoil. Banks are beefing up contingency funding plans to mitigate risks from rapid digital deposit runs.

Expectations of lower policy rates are supporting funding conditions--all eyes are now on central banks' actions

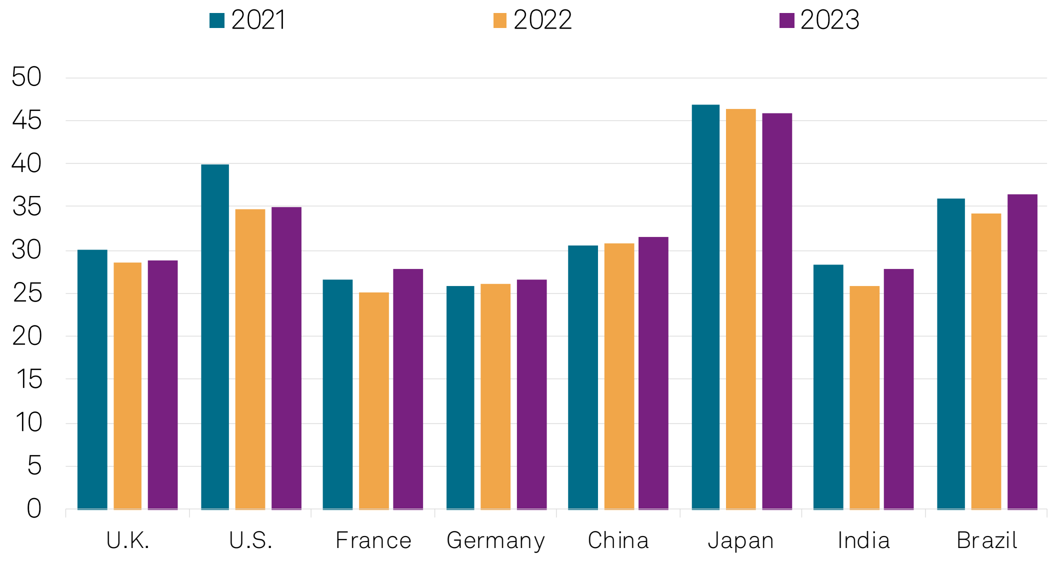
(%)



Monetary policy steering rates are annual averages. Source: S&P Global Ratings.

Adequate liquidity provides some comfort but is not a substitute for sound liquidity risk management

Broad liquid assets to total assets (%)



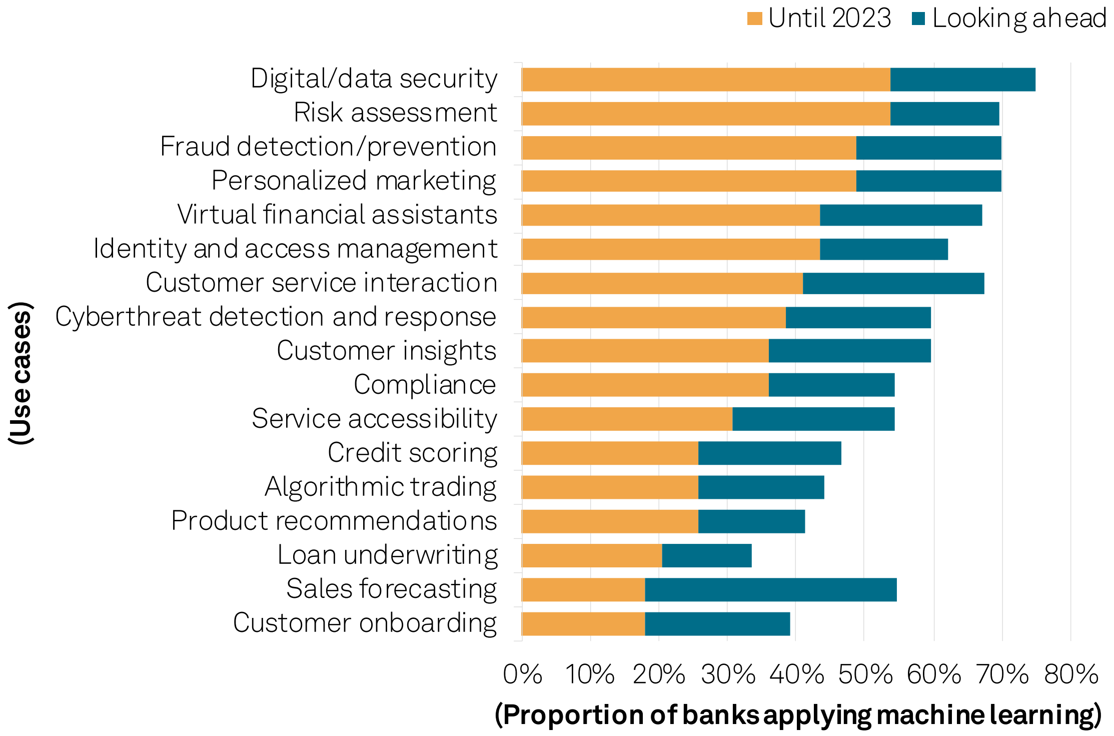
Data as of Dec. 31. Source: S&P Global Ratings.

Generative AI Will Reshape Banks’ Business Models

We expect the impact to be gradual, incremental, and uneven

Read report here

Banks’ AI priorities are changing, from automation to human enhancement



Question: Which of the following best describes your organization’s machine learning use case(s)? Please select all that apply. Source: 451 Research's Voice of the Enterprise: AI & Machine Learning, Use Cases 2024.

Key trends to watch over the next five years

- Internal talent reskilling and customer preferences
- Risk-based and human-centered approach to scaling AI
- Integrated digital operational resilience
- AI regulation enforcement
- AI strategy, development and governance infrastructure

Source: S&P Global Ratings.

S&P Global
Ratings

Cyber Risk | Supply Chain Risks Exacerbated By Skills Shortage

The Rise Of Artificial Intelligence Will Transform The Landscape

Banks' cyber resilience impacted by their suppliers' cyber risk preparedness

Recent cyber incidents underscore the importance of strong third-party oversight in relation to risk management. With increased digitalization, the robustness of a bank's cyber risk management is increasingly determined by the quality of its third-party relationships. For this reason, banks are continuing to refine their partnerships with suppliers to ensure that their cyber risk management is aligned. The regulatory environment is also developing, further strengthening banks' effective oversight of their supply chain partners.

The emergence of AI and quantum computing will bring forth new challenges and possibilities in cyber risk management

The use of Generative-AI-augmented processes increases the vulnerabilities that could be exploited by threat actors. Bank systems could become vulnerable to AI initiated phishing lures, deepfakes, and malware and manipulations of data (data poisoning or backdoor attacks) used to train AI models, which could lead to adverse business outcomes and loss of proprietary data. At the same time, AI offers opportunities for developing better cyber defenses that could strengthen banks' cyber risk management. Quantum computing poses cyber risks by potentially breaking widely-used encryption methods, rendering current data security practices obsolete.

Shortage of skilled personnel can be consequential for smaller banks

Key industry reports indicate that substantial gaps exist between the number of skilled professionals demanded versus the number available in the pool. This ultimately introduces lags and inefficiencies for banks executing their cyber risk management. In the time it takes for the supply of skilled professionals to correct, banks exposed to the complexity created by the combination of old and new technology systems and smaller, less resourced organizations could be exposed to heightened cyber risks, in our view.

Climate Change | Bank Strategies Are Evolving

Exclusion

Customer engagement

New products and services

Divestment

Finance green projects and technologies

Acquire and broaden expertise

- Assessing, managing, and ultimately reducing climate-related risks are key priorities for an increasing number of banks. Awareness and preparedness is gradually improving.
- More climate-related data is available, and methodologies/models are progressing. Regulatory climate stress tests are being developed rapidly across several countries.
- While exclusion and divestment policies have the potential to rapidly reduce banks' climate risk, customer engagement is gaining traction.
- Banks are also increasingly committing to finance green projects and technologies.
- The energy transition offers large business opportunities for banks. The suite of "green" products and services offered is broadening (e.g. green mortgages and electrical vehicle loans).

Emerging Markets | Geopolitics And Interest Rates Will Shape The Credit Story

High interest rates and a potential increase in geopolitical risk could affect the narratives for EMs

Geopolitical tensions could erode credit fundamentals

While we do not expect a full-scale regional war in the Middle East, escalation could derail the macroeconomic story particularly if the Strait of Hormuz is closed. The key transmission channels that we are keeping an eye on are energy prices, supply chain disruptions, financial market volatility, and resumption of inflationary pressures.

Monetary policy normalization in EMs will take longer than previously expected

We now expect the U.S. Federal Reserve's first interest-rate cut in December. This change in path has led us to update our forecasts for the policy-rate and exchange-rate trajectories for many EMs, particularly those that are more vulnerable to the Fed's decisions, such as Latin America.

There are a few bright spots

A few EMs are relatively better placed, particularly India and the Gulf Cooperation Council (GCC) countries where profitability and asset quality indicators remain healthy. A key factor to watch is the potential buildup of external debt in Saudi Arabia and Bahrain.

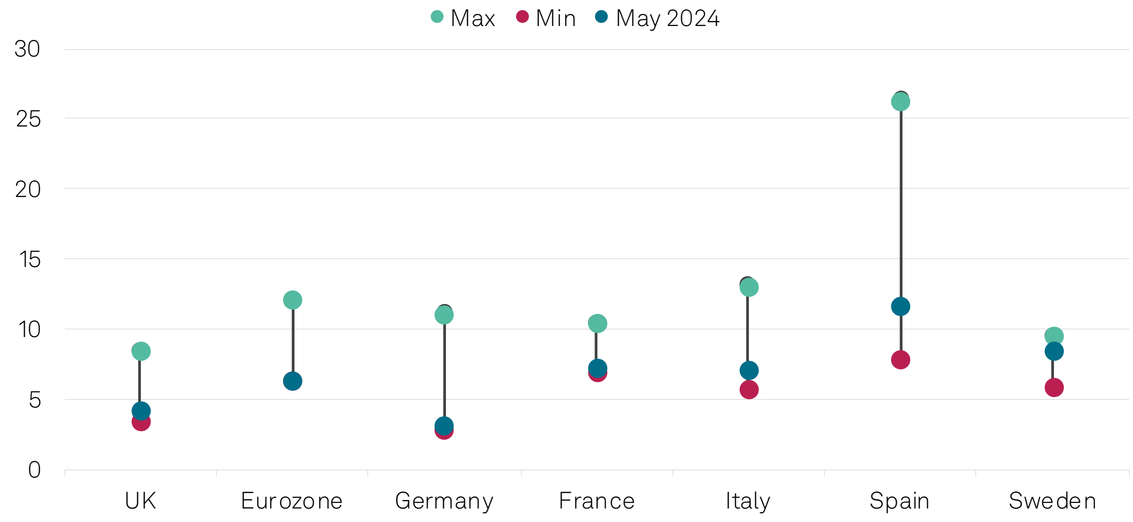
Europe & EMEA Emerging Markets

Credit Conditions: Europe

- Economies are gradually recovering, and activity will strengthen over the rest of the year, but economic growth will only reach its potential in 2025. In 2024, real GDP will rise by just 0.7% in the eurozone and 0.6% in the U.K.
- The labor market is proving extremely resilient but is unlikely to improve much further.
- Financing conditions should remain supportive amid declining interest rates, although heightened political risk poses risks to confidence

Unemployment is close to or at historical lows in most countries

Unemployment rate, last 20 years (% of labor force)



Source: S&P Global Ratings.

Debt issuance has been robust with banks taking advantage of investors seeking to lock in attractive yields

(bil. €)

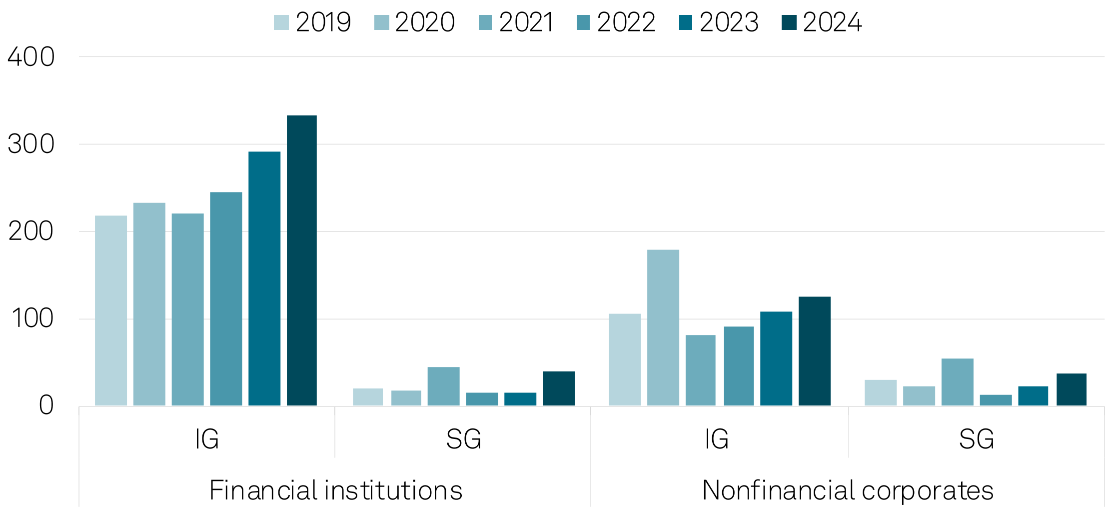


Chart shows data for January-May each year. Includes both financial and nonfinancial corporates with rated debt. IG--Investment-grade issuers. SG--Speculative-grade issuers.
Sources: Refinitiv, S&P Global Ratings Credit Research & Insights.

S&P Global Ratings

Credit Conditions: Europe

Downside risks...

- **Market turbulence** caused by adverse geopolitical events or unexpected monetary policy decisions, leading to higher funding costs.
- **A protracted, painful recession**, leading to higher corporate insolvencies and unemployment.
- **Banks' failure to deliver** commercially and operationally resilient business models.

..and what they mean for the sector

- **Tighter financing conditions would stress financial institutions with weaker funding structures**, especially non-bank financial institutions with high refinancing needs, and expose banks to higher counterparty credit risks.
- A recession could undermine the financial health of corporates and households, particularly the more vulnerable ones, **weakening banks' asset quality** and clouding business prospects.
- Failure to tackle inefficiencies, properly digitalize the business and sustain resilience to cyber attacks could **test the long-term viability of some institutions**.

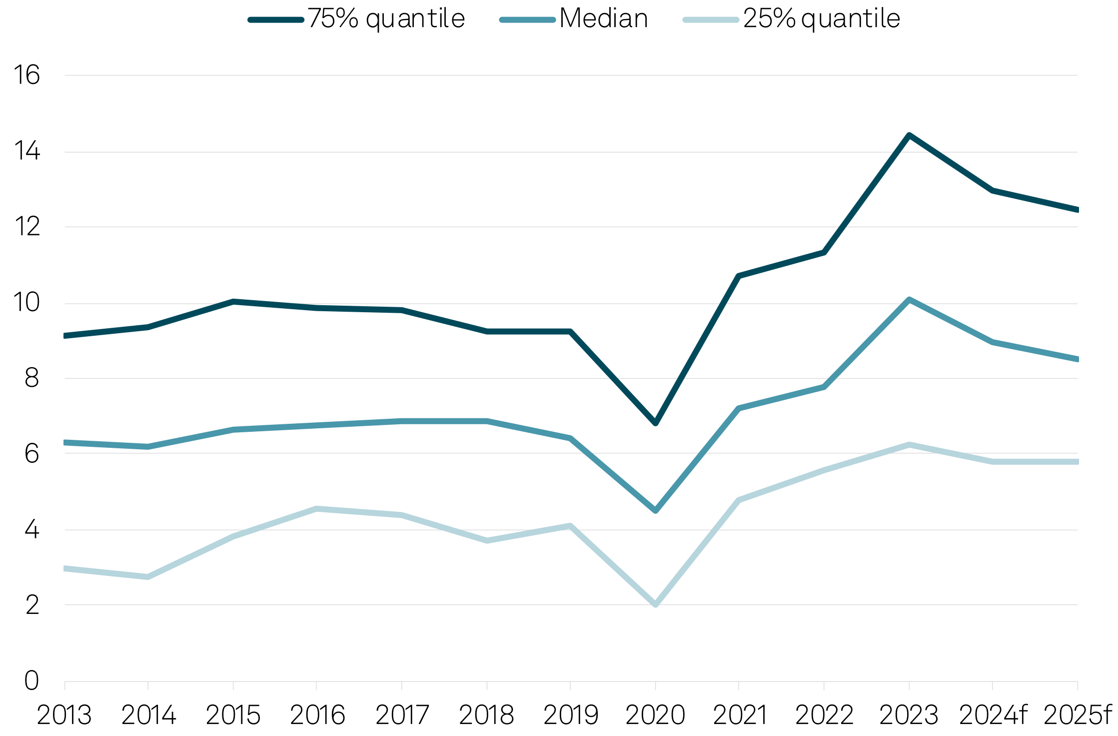
What we expect for next 12 months

- **European banks will remain solid** amid sluggish economic growth, gradually easing monetary policy, and heightened geopolitical risks.
- **Bank lending will remain subdued** as high uncertainty and interest rates weigh on credit demand. Credit costs will normalize, with the biggest impact felt by those banks most exposed to commercial real estate, small and midsize enterprises, and unsecured retail loans.
- **Net interest margins (and thus earnings) will hold up well** as banks are positioning their balance sheets to offset a gradual decrease in rates.
- **Attractive shareholder remuneration will continue** on the back of banks' solid capitalization, while sound liquidity will also be preserved.

Profitability Should Remain Comfortable

Tighter cost management and greater focus on fees will help compensate for pressure on revenue

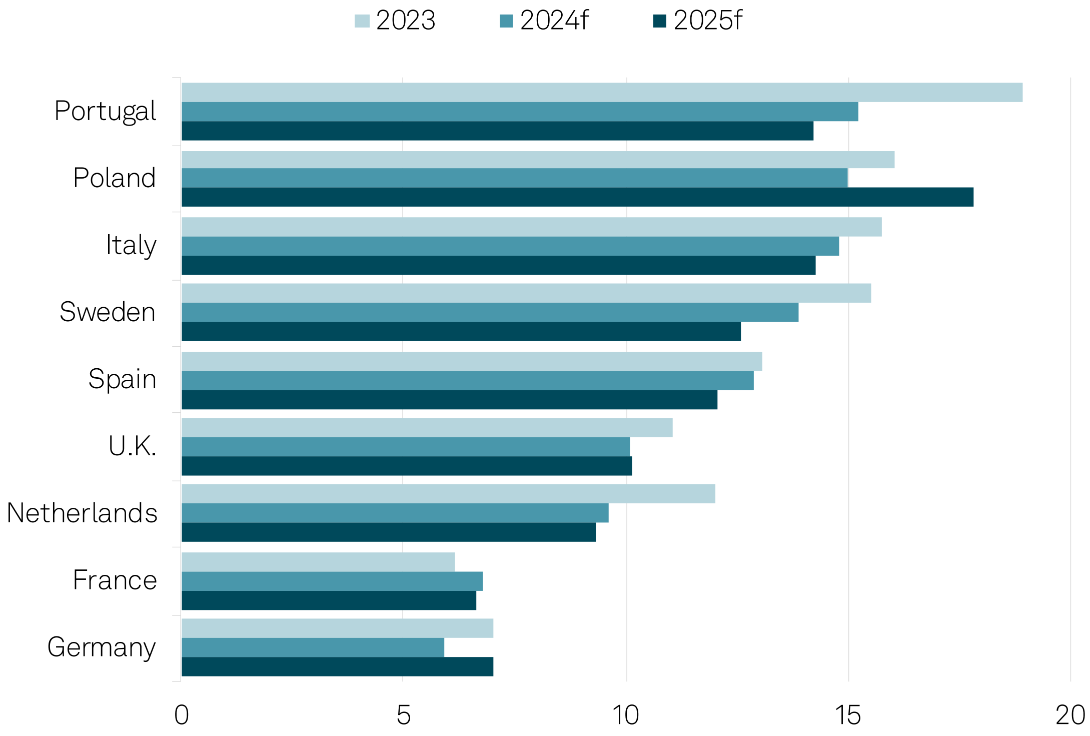
Evolution of return on average common equity (%)



Sample includes rated European banks with a stand-alone credit profile. f--Forecast. Source: S&P Global Ratings.

But performance will vary by country

Weighted average RoE for rated European banks (%)



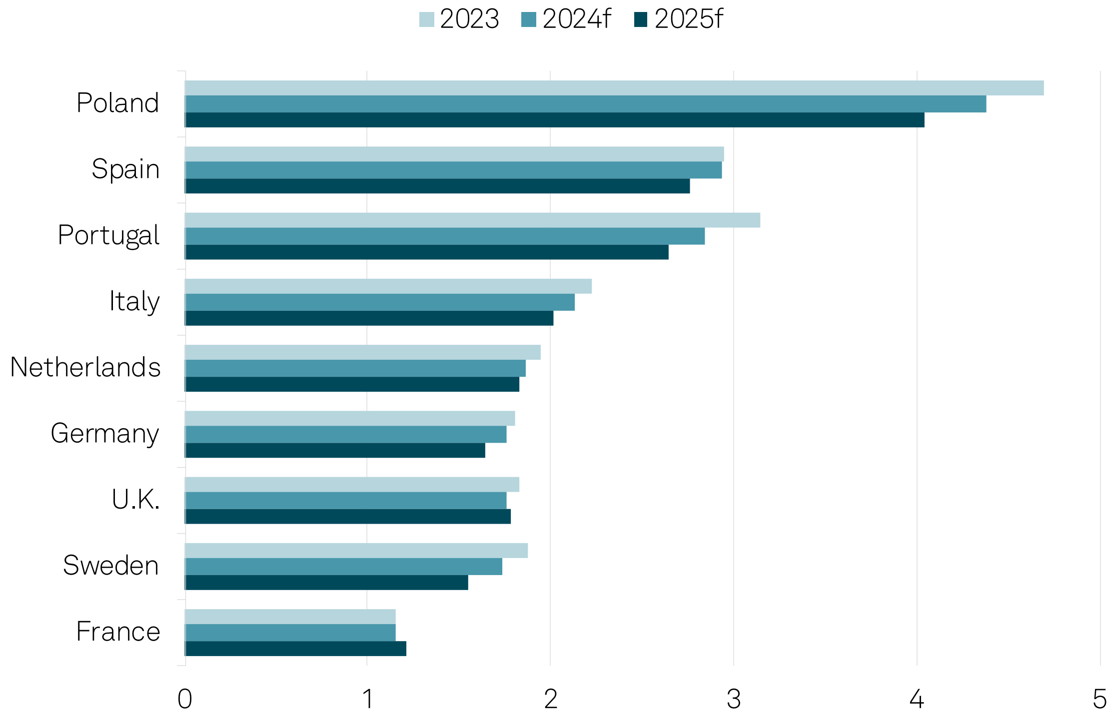
Values are weighted by total assets. Sample includes 75 banks. f--Forecast. RoE--Return on equity.
Source: S&P Global Ratings.

S&P Global Ratings

Banks Are Positioning Balance Sheets To Offset Declining Interest Rates

Margins will fall only moderately over 2024-2025

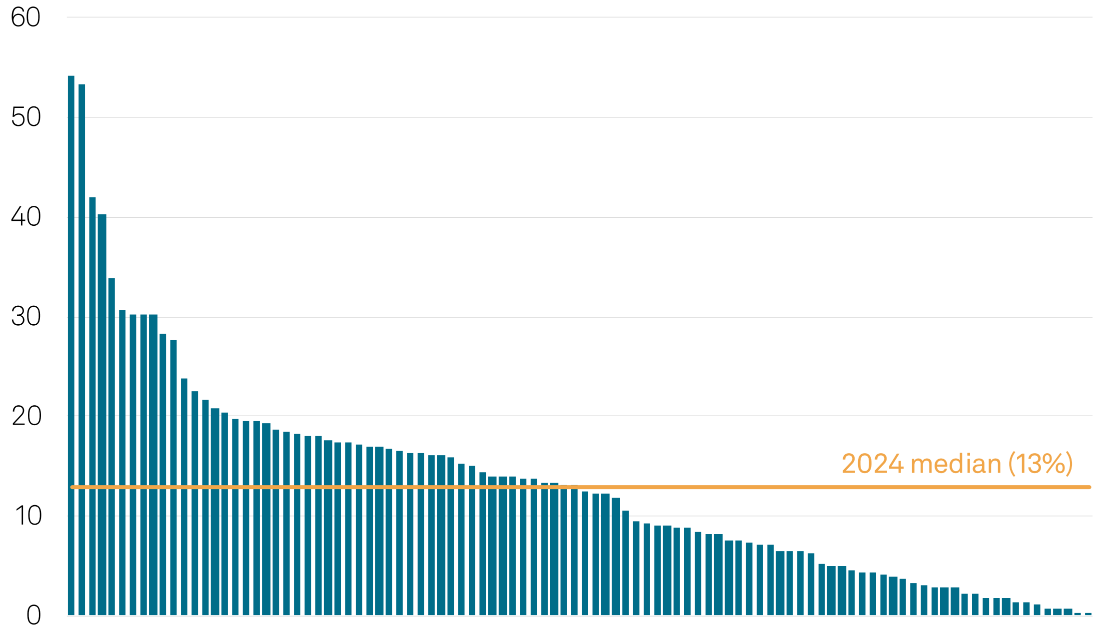
Weighted average net interest margin for rated European banks (%)



Values are weighted by total assets. Sample includes 72 rated banks. Source: S&P Global Ratings.

Ample capacity to absorb a more normalized cost of risk

2024 credit losses as proportion of pre-provision earnings, top 100 rated European banks (%)



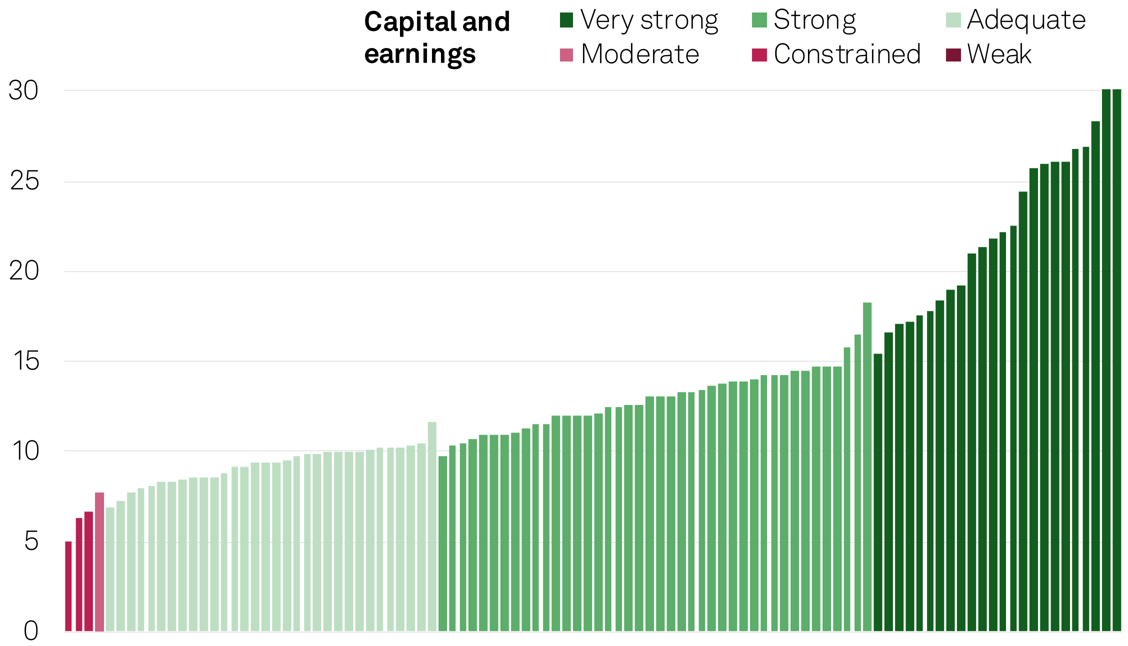
Values are weighted by total assets. Sample includes 75 banks. f--Forecast. Source: S&P Global Ratings.

Capitalization Will Remain Resilient

Muted credit growth and increased use of risk-transfer techniques will support capitalization, despite ongoing shareholder distributions

Most banks have ample capital headroom

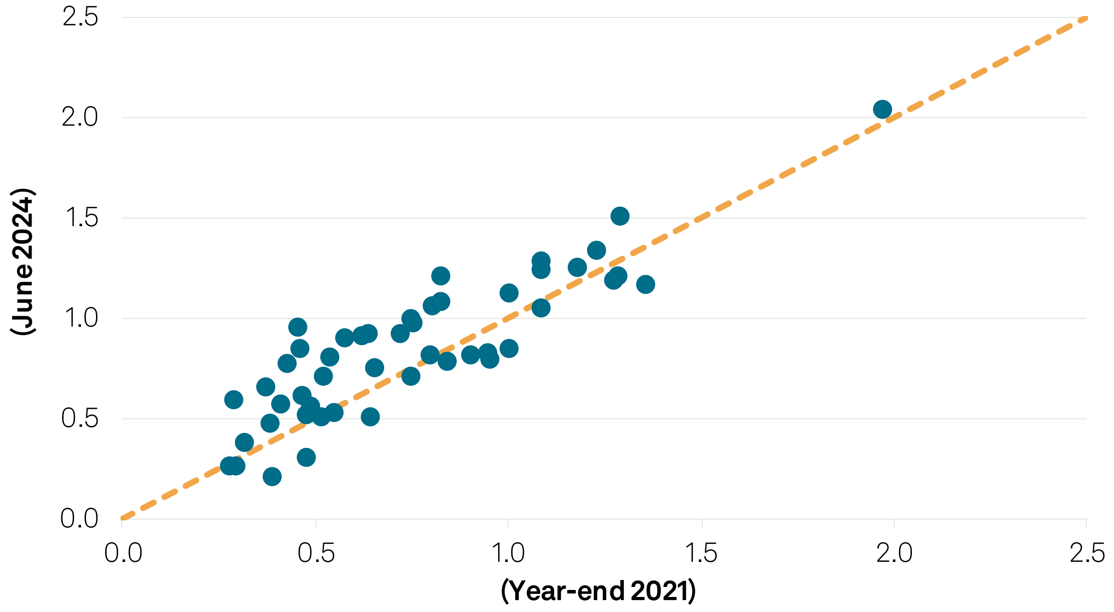
2024 RAC forecasts, top 100 rated European banks (%)



RAC ratios capped at 20%. Source: S&P Global Ratings.

Equity valuations have improved, but remain below book value for many banks

Price to book ratio of top 100 rated European banks (%)



Sources: S&P Capital IQ, S&P Global Ratings.

Key Risks For Banks In Emerging Market (EM) EMEA

We foresee three main risks for EM-EMEA banks in 2024-2025

Higher-for-much-longer rates

- Higher-for-much-longer interest rates will likely pressure some of the weakest borrowers in EM-EMEA, with potential negative impacts on asset quality indicators.

External debt dependence or buildup

- We expect external debt to continue building for Bahrain and Saudi Arabia, while in Qatar it should stabilize in the absence of major government investments.
- Refinancing risk is stabilizing for Turkiye (with higher rollover of debt, thanks to a continued policy shift) and Egypt (strong external support), but uncertainty remains high for Tunisia.

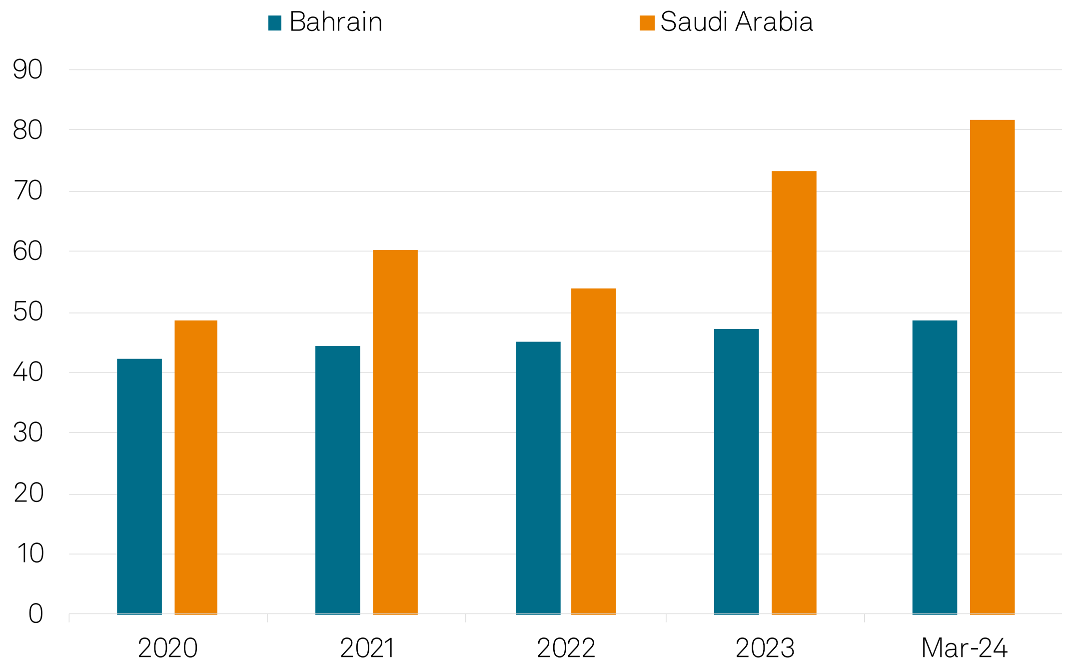
Geopolitical risk and local policy choices

- The Israel-Hamas war, Russia-Ukraine conflict, and potential skirmishes between Iran and countries in the region are among the key factors that will shape the credit story for EM-EMEA in 2024 and 2025.
- Implementation of a resolution regime in South Africa, continued liquidity support in Saudi Arabia, an upcoming election in Tunisia, and reform implementation in Tunisia, Egypt, and Turkiye are also key drivers for EM-EMEA.

GCC | External Debt Buildup Is A Factor To Watch

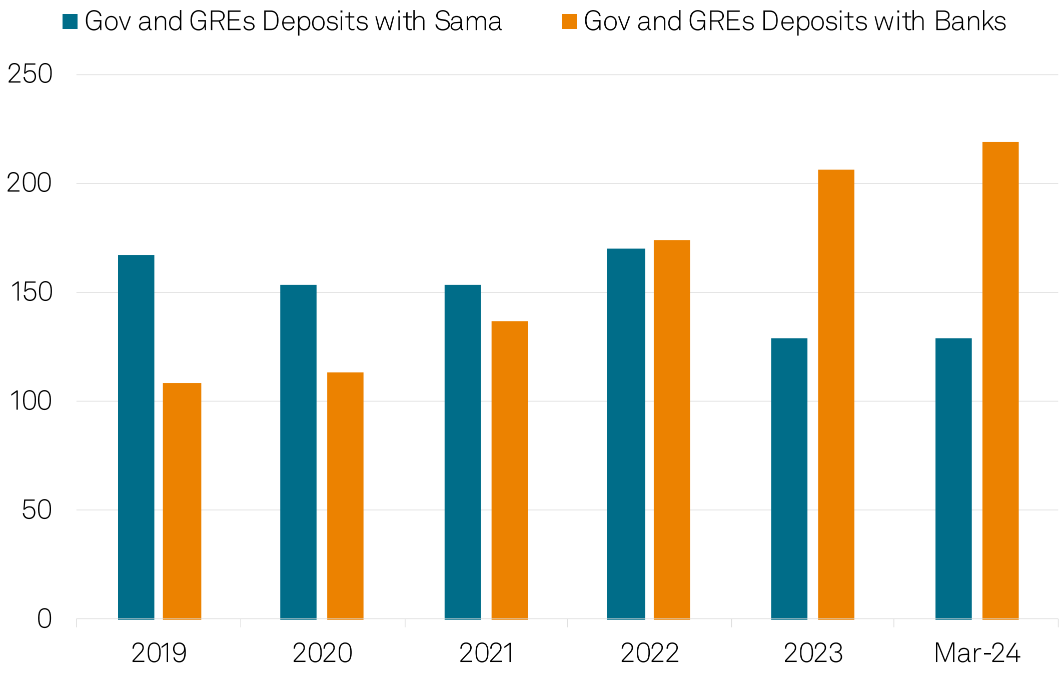
External debt is building up in Saudi Arabia and Bahrain, helped by relatively supportive market conditions for the former and continued regional support for the latter

External debt is building up in some countries (bil. US$)



Gross external debt in U.S.$ billion. Sources: Central Bank of Bahrain and Saudi Arabia, S&P Global Ratings.

Government support for Saudi banks continues (bil. US$)

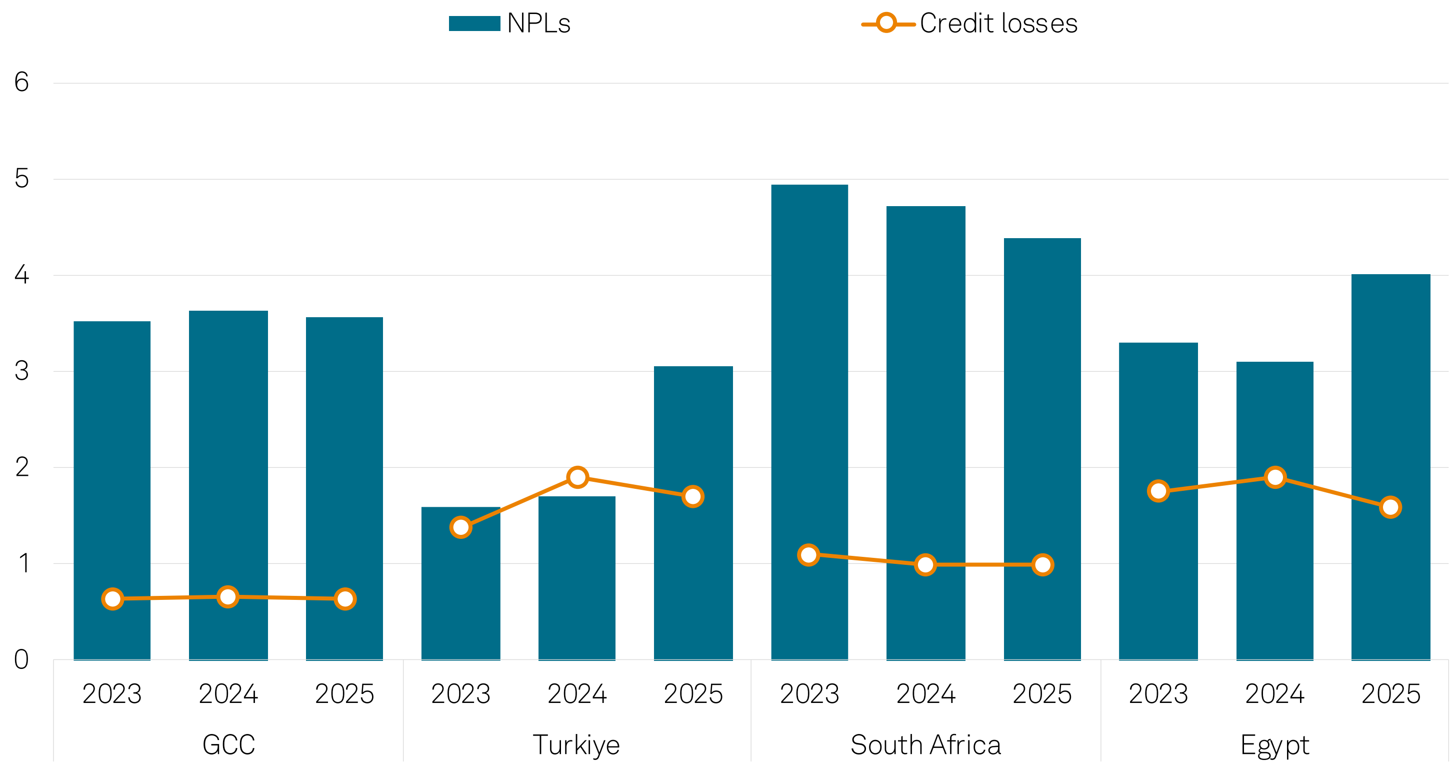


Gov--Government. GRE--Government-related entities. Sources: Central Bank of Saudi Arabia, S&P Global Ratings.

Higher-For-Longer Rates Will Bite The Weakest Borrowers

Some countries will suffer more than others

Asset quality indicators for selected EM-EMEA countries (%)



GCC--Gulf Cooperation Council. NPLs--Nonperforming loans. Source: S&P Global Ratings.

- **GCC:** Higher-for-longer rates will pressure the weakest borrowers in the GCC, but banks' strong existing cushion of provisions will keep credit losses in check.
- **Egypt:** Credit losses will likely remain high over the next couple of years because of the protracted poor economic performance, high inflation, tight monetary policy, and depreciating Egyptian pound.
- **Turkiye:** Unwinding economic imbalances, lower credit demand, and a slowing economy will result in elevated, but manageable credit losses for banks.
- **South Africa:** Structural economic issues, tight lending conditions, and pressured household disposable income in 2024 will keep credit losses above historical levels.

Egypt and Turkiye | High Imbalances But Improving Situation

Strong support from the GCC for Egypt and ongoing reforms in Turkiye are helping to unwind imbalances

High exposure to government creditworthiness and pound depreciation

- Egyptian banks' exposure to the sovereign stood at 64% of their assets on Feb. 29, 2024, or 9.5x the system's equity.
- The depreciation of the Egyptian pound is likely to consume 300-400 basis points (bps) of banks' total capital ratios since about 21% of assets were in foreign currency as of December 2023.
- We do not expect a major improvement in the banking system's net external debt position as most of the foreign currency inflows to the country are likely to be directed to the central bank reserve.

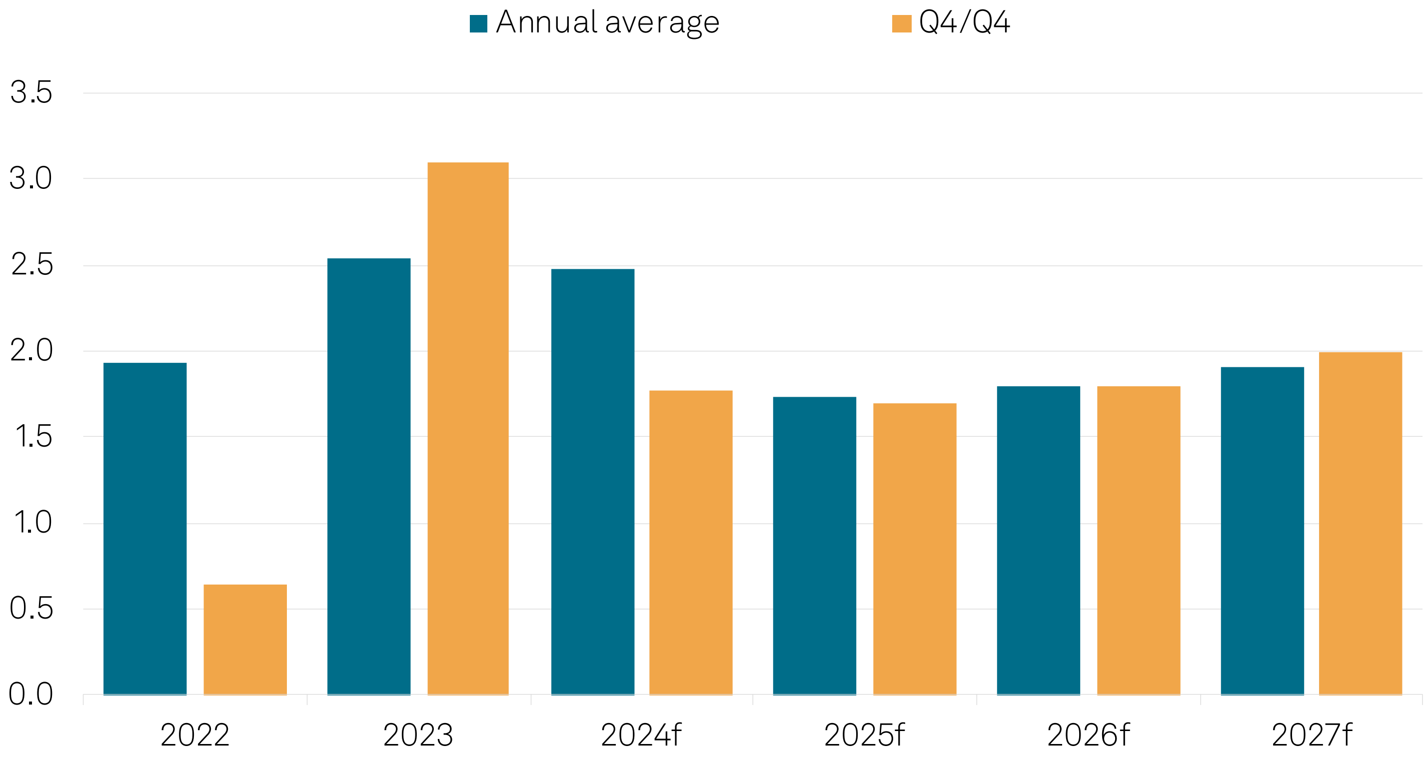
Unwinding imbalances

- A prolonged period of monetary tightening, combined with better coordination between monetary, fiscal, and income policies, is likely to help gradually rebalance the economy.
- We expect the Turkish lira (TRY) will depreciate further, to TRY42 to $1, by end-2025 and real estate prices will moderately contract in real terms. This would erode Turkish borrowers' disposable income and increase banks' impairment charges (net of provisions reversal) to about 170-190 bps in 2024-2025, from an estimated 138 bps in 2023.
- Refinancing risks for Turkish banks have somewhat stabilized but their overall funding profiles remain fragile. The rollover rate increased to over 100% in the past few months and costs are down. Assuming the authorities maintain their current efforts, we expect Turkish banks to be able to refinance most of their $103.2 billion of short-term debt (as of March 2024).

North America

Credit Conditions: North America

Real U.S. GDP growth (%)



f--Forecast. Sources: The U.S. Bureau of Economic Analysis, S&P Global Ratings' forecasts.

- S&P Global Ratings expects the U.S. economy to expand 2.5% in 2024 and 1.7% in 2025.
- Businesses continue to face higher costs of capital, which will limit capital expenditure and hiring, and the unemployment rate will likely rise in the next two years--to 4.4% from 4.0% currently.
- We expect the Fed, in response to a slowdown in inflation, to start reducing its policy rate in December.
- In Canada, we expect real GDP growth of 1.1% in 2024, 1.7% in 2025, and 2.1% in 2026.

Credit Conditions: North America

Banks are operating cautiously amid higher-for-longer interest rates

Downside risks...

- **A slowdown in economic growth and stubborn inflation.** S&P Global economists expect a resilient U.S. economy to slow and transition to slightly below-potential growth in the next couple of years. They also expect inflation to continue to abate. However, a greater-than-expected slowdown coupled with continued inflation would negatively affect banks.
- **Funding and liquidity pressures.** Recent deposit growth has supported banks' funding and liquidity. Still, many banks have limited on-balance-sheet liquidity and material unrealized losses on securities.
- **Real estate stress.** Deterioration in commercial real estate (CRE), particularly the office sector, has affected asset quality. This will remain a key challenge for many banks over the next year.

..and what they mean for the sector

- **Asset quality should worsen further but remain manageable.** Provisions and charge-offs will likely rise further, especially on CRE. Still, we believe most banks' preprovision earnings place them well to absorb credit losses.
- **Net interest income (NII) will fall this year.** Funding costs have inched higher in the first half of 2024, weighing on NII. We expect stabilization in the second half of the year, though NII will be down for the year.
- **Unrealized losses could remain elevated.** The rise in rates caused unrealized losses on securities and loans to rise. While those unrealized losses have fallen from their peak, they will remain elevated for many banks over the next year unless long-term rate drop materially.

What we expect for next 12 months

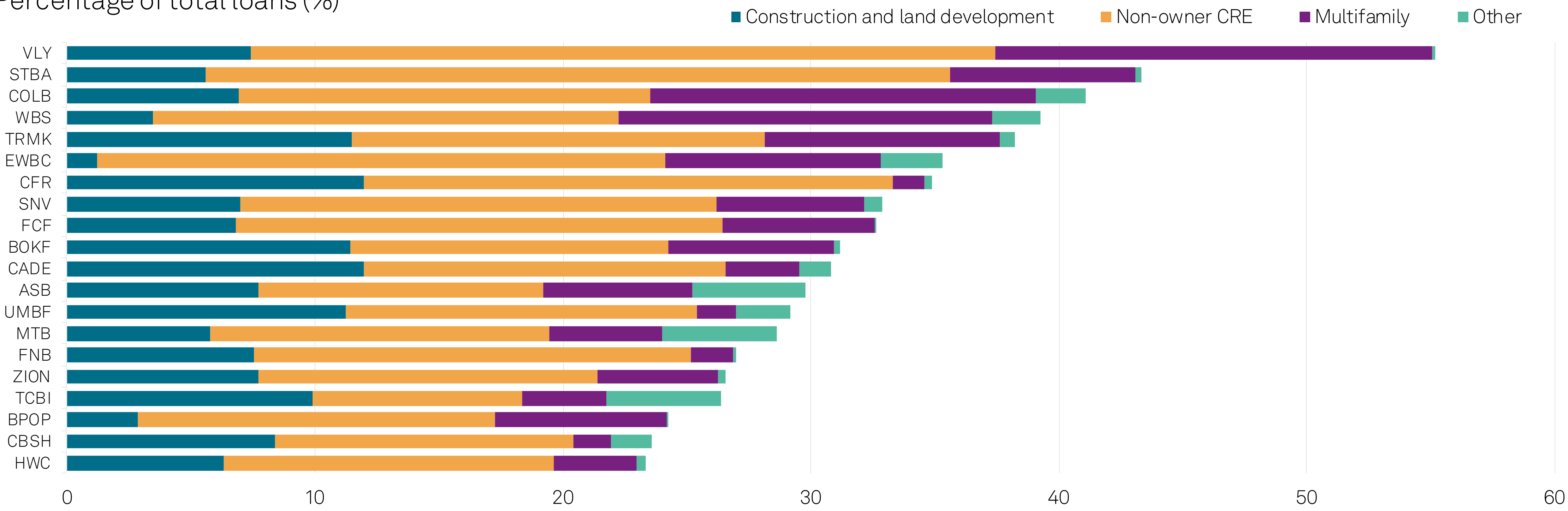
- **Profitability will drop but remain reasonably strong.** Lower NII is likely to pressure profitability in 2024. Still, we expect banks to generate a return on common equity of 10%-11%.
- **Banks will continue to improve liquidity and grow loans slowly.** Banks have added significant contingent liquidity in the last year, and we expect them to add more on-balance-sheet liquidity as deposits rise. They are managing their balance sheets prudently in part by growing loans slowly.
- **The sector will see proposed changes to regulation and supervision.** Regulators said they will alter the Basel III endgame proposal they made last year pertaining to capital requirements for large banks. They also may finalize a resolution proposal for large banks and make proposals on liquidity and other topics.

CRE Delinquencies Are A Growing Risk For Banks With Large Exposures

- Office loans could struggle in the long-term owing to secular changes in work arrangements; select multifamily could also be pressured.
- Banks' broadly diversified loan portfolios and conservative underwriting should mitigate losses.

Top CRE loan exposure of rated banks

Percentage of total loans (%)



Data as of March 31, 2024. CRE--Commercial real estate. CET1--Common equity Tier 1. CRE--Commercial real estate. Sources: FDIC data, S&P Global Ratings.

U.S. Forecast | Earnings Dip But Banks Still Generate Double-Digit ROE

Worsening		Neutral		Improving

Revenues	Net interest income (NII), which fell in the first quarter, will likely be moderately down for the full year, with funding costs rising further through the middle of the year. Fee income rose for most banks in the first quarter, partly on better investment banking results, but higher-for-longer interest rates may limit improvement for the full year.
Expenses	Overall expenses should drop for the full year due to one-time charges in 2023. However, inflation, investments in technology, and perhaps some increase in business activity will push core expenses somewhat higher, notwithstanding banks' continued focus on cost controls.
Profitability	Profitability will weaken somewhat on lower NII and higher provisions. We expect an industry return on common equity of 10%-11%, down from greater than 11% in 2023.
Credit quality	We expect delinquencies and charge-offs, particularly in certain asset classes, to continue rising amid high rates, declining consumer savings, and stress in areas like CRE.
Capital	Some banks may increase capital ratios further by limiting payouts to support market confidence and in anticipation of potentially stricter capital rules. However, increases in capital made last year and uncertainty about stringency of Basel III endgame implementation may make significant further increases in capital unlikely.
Liquidity **Funding**	While deposits rose in Q4'23 and Q1'24, growth should be fairly limited amid high rates. Funding costs may also increase further partly due to continued shifts in deposit mixes. Banks are likely to maintain good contingent liquidity, although many have relatively low cash balances and still material unrealized losses on their securities.

Note: Forecast for next 12 months. ROE--Return on equity. Source: S&P Global Ratings.

Canada Forecast | Provisions And Elevated Expenses Strain Profitability

Worsening — Neutral — Improving

Revenues	NII growth may moderate as rates have begun to decline and loan growth is moderating. Fee income is likely to remain robust given strong equity and capital markets activities.
Expenses	Banks are managing expenses by reducing discretionary costs, delaying certain investments in technology, and reducing headcount, which could help moderate expense growth in 2024, though we expect expenses to remain elevated.
Profitability	Profitability will remain strained as provisions for loan losses are rising from very low levels and high expenses are pressuring operating performance. We expect an industry return on common equity of 9%-12% in 2024.
Credit quality	Delinquencies are rising. We expect asset quality to normalize from very strong levels and banks to continue to build allowances. We expect net charge-offs to rise but to remain manageable.
Capital	The Office of the Superintendent of Financial Institutions in June 2024 kept the domestic stability buffer unchanged at 3.5%. The Basel III reform has been fully implemented in Canada and had minimal negative impacts on domestic systemically important banks' CET1 ratios. We expect banks to maintain risk-adjusted capital (RAC) ratios at an adequate 7%-10%.
Funding and liquidity	Funding remains well diversified even though the deposit mix changed because of high interest rates, driving growth in higher-yielding savings products such as guaranteed investment certificates. We expect growth in demand deposits will resume as rates have begun to decline. Banks continue to have solid access to global funding markets. We expect liquidity metrics to remain relatively unchanged.

Note: Forecast for next 12 months. CET1--Common equity Tier 1 ratio. Source: S&P Global Ratings.

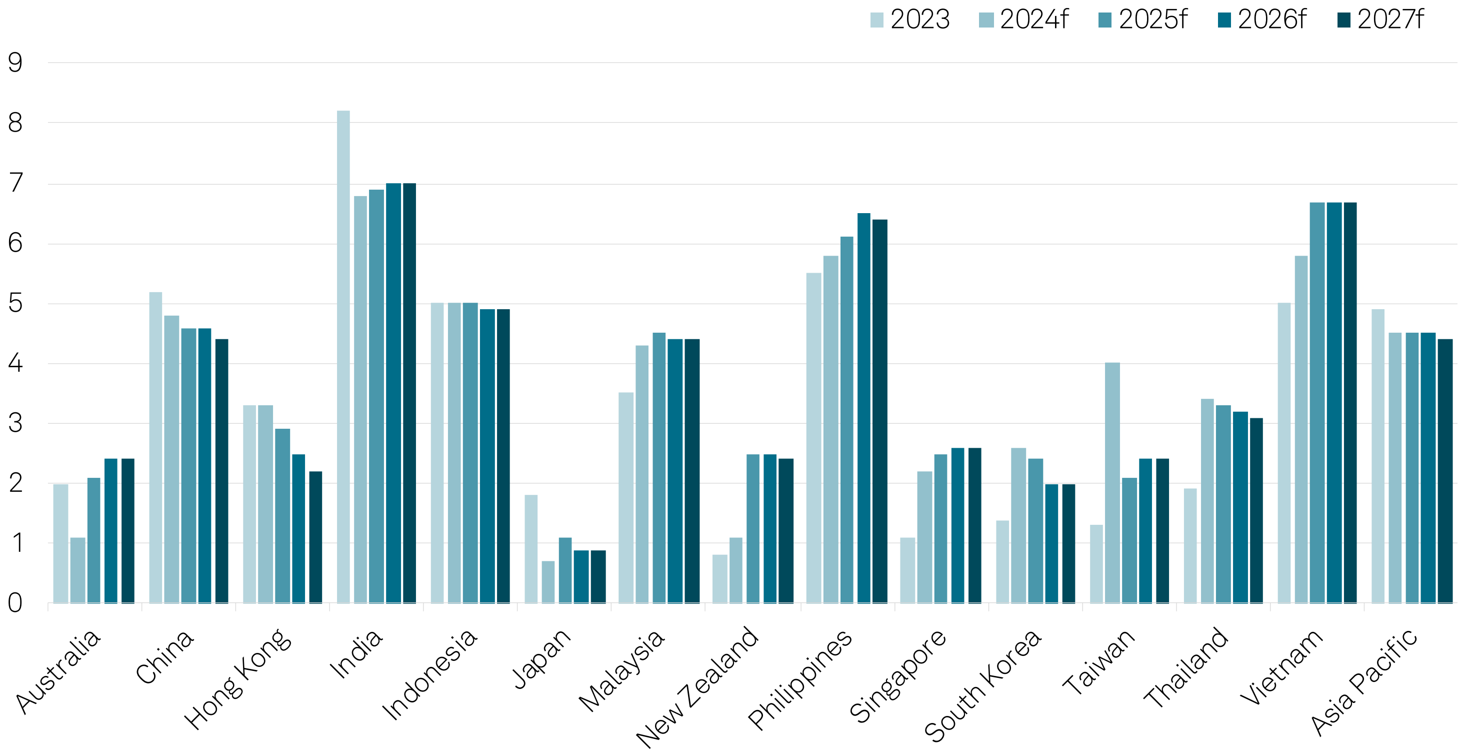
Asia-Pacific

Credit Conditions: Asia-Pacific

- **China vs West.** The trade conflict between China and the West is unfolding. Intensifying tariffs could drag China's industrial production-led economic recovery, and potential retaliatory tariffs by China would widen the global impact. The region's growth should stay at 4.5% over 2024-2026.
- **Confidence dragging in China.** Property sales and home prices are declining despite bolder stimulus, underlining very weak Chinese confidence.
- **Walking a tight rope.** A strong U.S. dollar is depressing Asian currencies. For importers and households, this can translate into costlier offshore debt borrowings and imported inflation. The region's central banks are maintaining high interest rates. Onshore financing channels generally remain cheap and available, so far.
- **Gathering clouds.** Asia-Pacific's credit conditions look stable. Surprise election outcomes globally could cause shifts in political orientations and dilute policy predictability, causing volatility.

Exporters And EMs Are Outperforming

Real GDP growth, year over year (%)



Note: For India, 2023 = FY 2023 / 24, 2024 = FY 2024 / 25, 2025 = FY 2025 / 26, 2026 = FY 2026 / 27, 2027 = FY 2027 / 28. The fiscal year ends March 31.
Source: S&P Global Ratings Economics.

Credit Conditions: Asia-Pacific

Higher interest rates will pressure asset quality

Downside risks

- **Property downside risks intensify.** Banks' net interest margins benefit from higher interest rates, but higher-for-longer rates or weaker-than-expected economic growth outside our base case will eventually hurt banks' asset quality. This is especially true for property markets in the region that are under strain, most notably China's.
- **Structural risks**. Climate change, cyber risks, and digitalization trends will affect the competitive banking landscape. While these risks typically are a slower burn for banks, they increasingly will test banks' business models and financial flexibility.

...and what they mean for the sector

- **Credit losses will increase.** We anticipate that Asia-Pacific banks' credit losses will increase in 2024 to more than US$400 billion. If economic hurdles worsen outside our base case, asset quality will weaken further, testing rating outlooks. Profitability and capitalization buffers are adequate for most banks at current rating levels.
- **Greater credit differentiation**. Potentially more vulnerable are institutions with high direct exposures to weak counterparties or sectors; and those that are inherently weaker and non-systemically important.
- **Governments throw a lifeline.** In the unlikely event it were required, we believe extraordinary government support for systemically important private sector commercial banks across most Asia-Pacific banking jurisdictions will buffer banks' credit-quality.

What we expect for next 12 months

- **Ratings outlook is stable.** Asia-Pacific banks are managing property-sector risks and other key risks satisfactorily at current rating levels. We have stable outlooks on about 95% of the Asia-Pacific banks we rate.
- **Ratings upside is limited during 2024.** Given higher-for-longer interest rates, weaker economic growth, and property market sensitivities prospects for upward ratings momentum is constrained.
- **Risks remain on the downside.** The emergence of a meaningful downside scenario outside our base case will cause higher than expected credit losses and may tilt rating outlooks toward the negative.

What Are We Monitoring: China

Prospective conditions remain somber

- We forecast China real GDP growth to be 4.8% in 2024, and 4.6% next year.
- Momentum has slowed after relatively brisk 5.3% year-on-year GDP growth in the first quarter of 2024. This has happened amid the relentless property downturn, with housing sales and starts still down around 20% in May on a year ago, and weak domestic confidence and spending.

Property NPLs will continue to increase

- China's property downcycle is poised to continue. During the first five months of 2024, nationwide property sales were down 27.9% from the previous year, according to the National Bureau of Statistics.
- We project NPL ratios for property development will rise to 6.4% in 2025, before recovering to 5.2% in 2026.

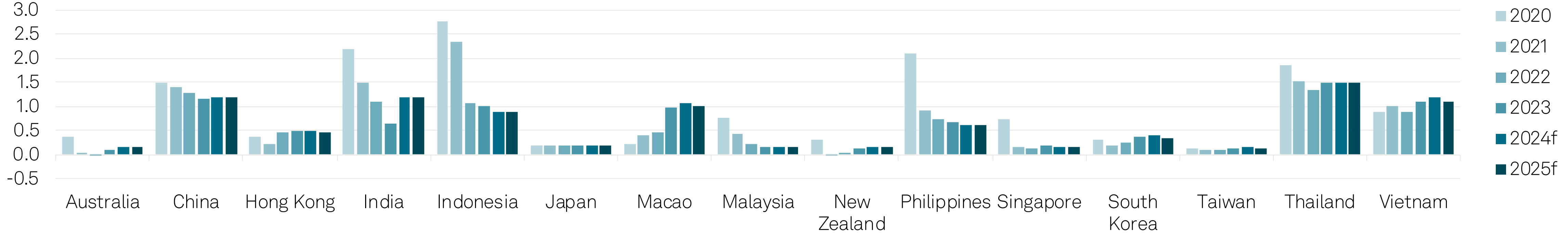
Local-government SOE debt risk

- Default risk is rising for the state-owned enterprises (SOEs). Delayed payments by SOEs could disrupt local credit-driven activities and hurt economic recovery.
- Our base case assumes any loan restructuring would be selective over time and on a case-by-case basis, because moral hazard considerations mean wholesale local government financing vehicle (LGFV) loan restructuring is unlikely.
- Lower interest rates and maturity extensions for such debt would weigh on the capital and earnings of some banks, particularly smaller institutions with LGFV concentration in weak regions.

Asset Quality Is Steady

Credit losses will increase marginally in 2024 and 2025 for most banking systems

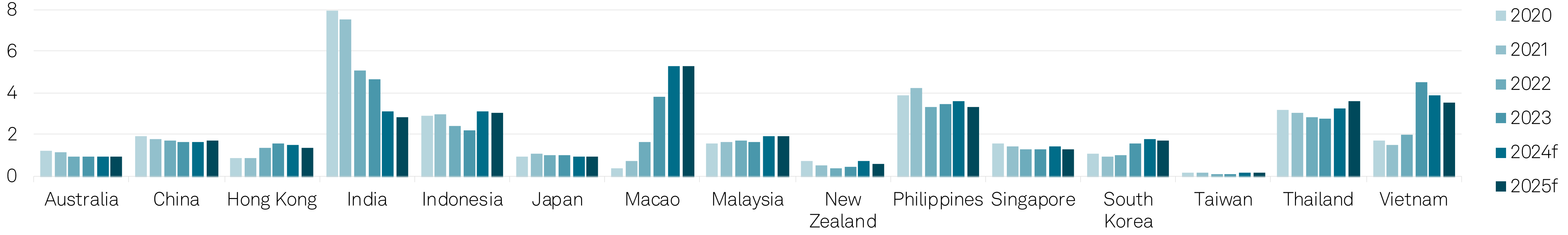
Credit losses as a percentage of gross customer loans (%)



Note: For India and Japan, 2020 refers to fiscal year ended March 31, 2021. f--Forecast. Source: S&P Global Ratings.

Nonperforming assets will remain elevated

Nonperforming assets as a percentage of systemwide loans, year-end (%)

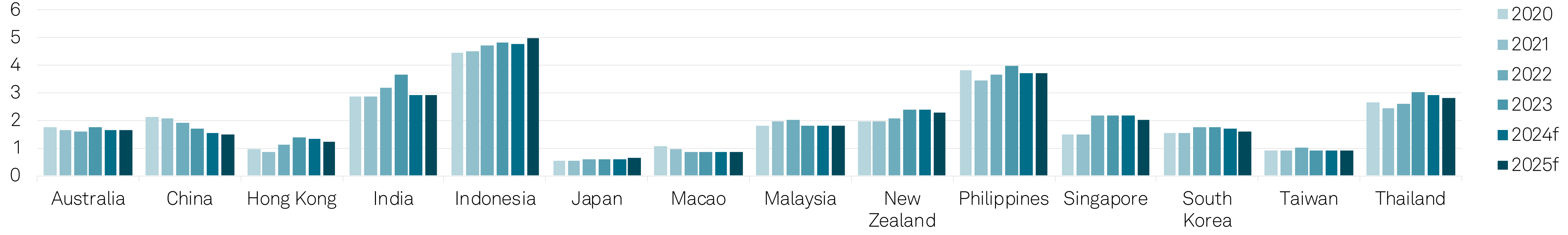


Note: For India and Japan, 2020 refers to fiscal year ended March 31, 2021. f--Forecast. Source: S&P Global Ratings.

Earnings Prospects Remain Sound

NIMs continue to benefit from higher rates

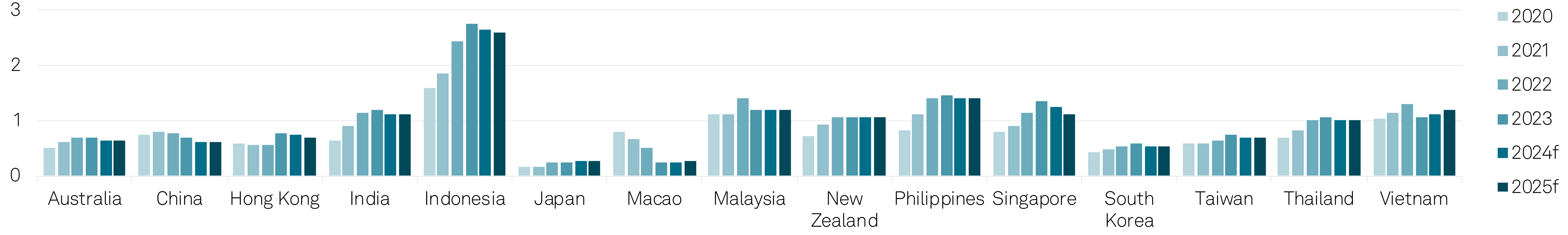
Net interest income to average earning assets (%)



Note: For India and Japan, 2020 refers to fiscal year ended March 31, 2021. f--Forecast. NIM--Net interest margin. Source: S&P Global Ratings.

RoAAs will remain sturdy despite higher credit losses

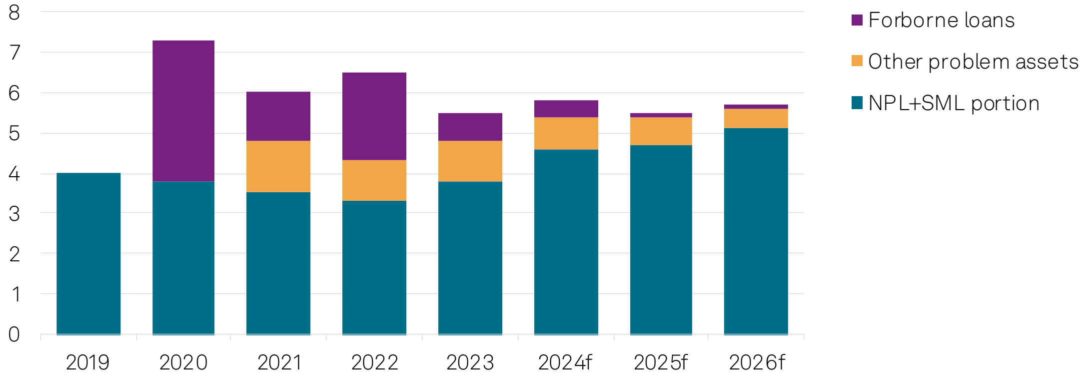
Systemwide return on average assets (%)



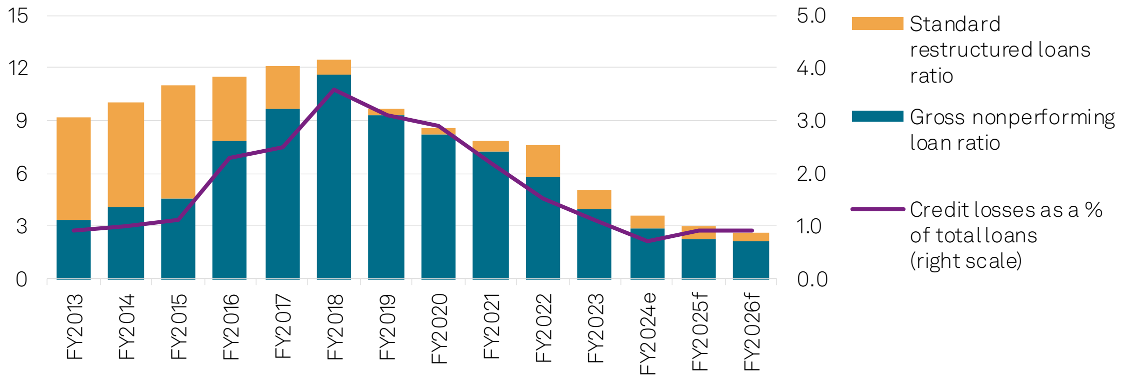
Note: For India and Japan, 2020 refers to fiscal year ended March 31, 2021. 2021 is an estimate for India. f--Forecast. RoAA--Return on average assets. Source: S&P Global Ratings.

Asia-Pacific Banks

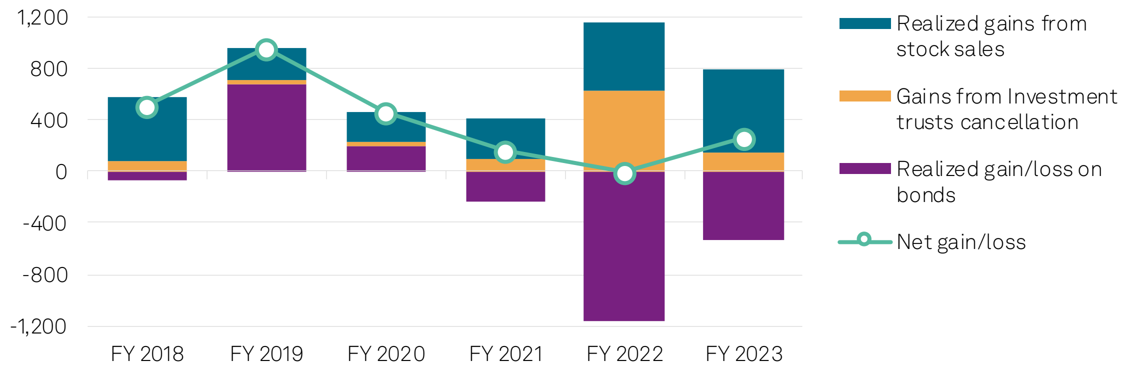
1. China: NPL and SML ratios likely to increase (%)



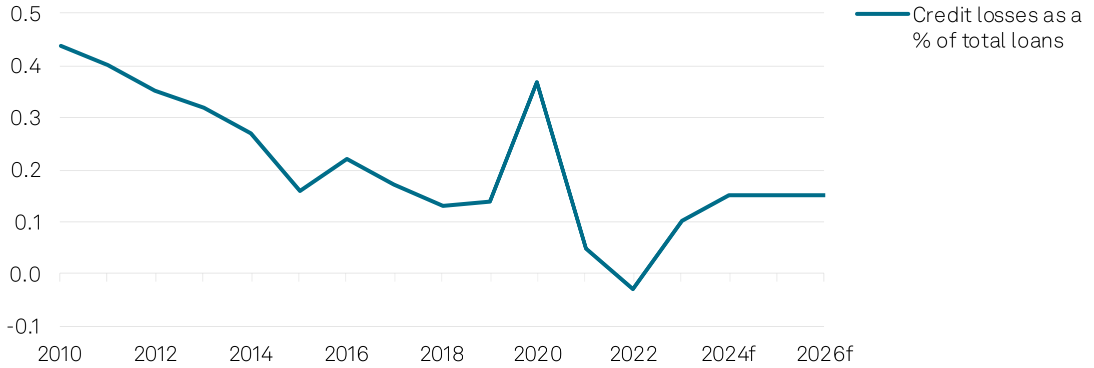
2. India: Banks' asset quality improvement to persist (%)



3. Japan: Gains from stock sales will help absorb losses (bil. ¥)



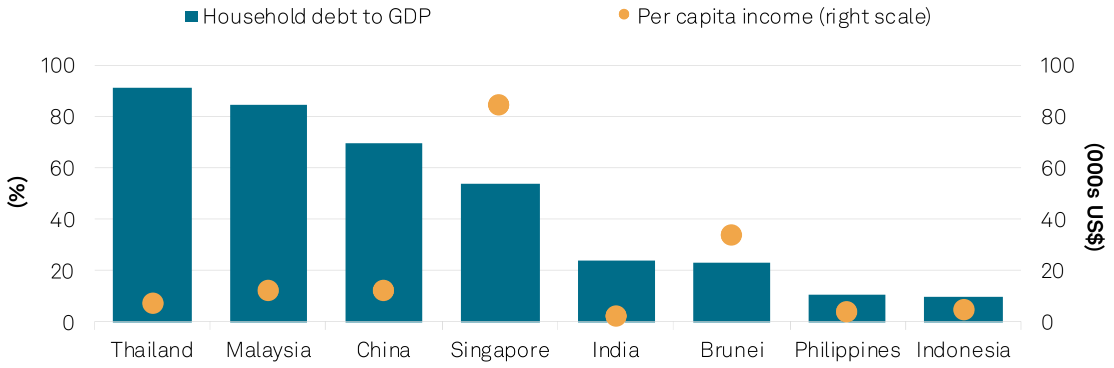
4. Australia: Credit losses should remain low (%)



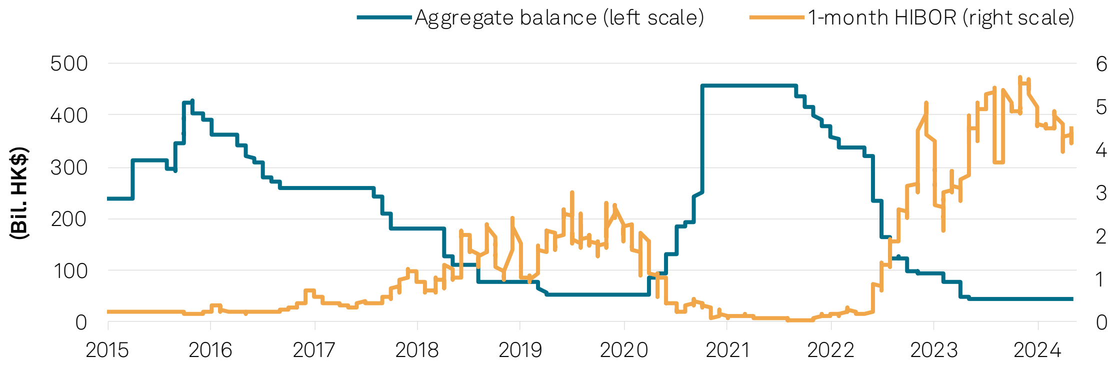
1. NPL--Nonperforming loan. SML--Special mention loan. NPA--Nonperforming assets. 2. Data for fiscal years, all ended March 31. FY--Fiscal year. Sources: Reserve Bank of India. S&P Global Ratings calculation and estimates. 3. Chart for Japan reflects net gains/losses from securities portfolio" of three major banking groups. Source: S&P Global Ratings, based on company disclosures. 4. f--Forecast. Source: S&P Global Ratings.

Asia-Pacific Banks

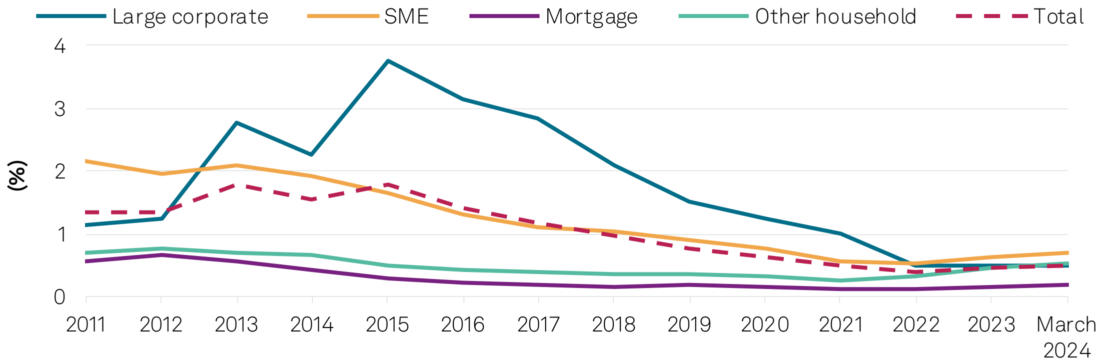
1. SSEA: Household leverage is high in Thailand and Malaysia



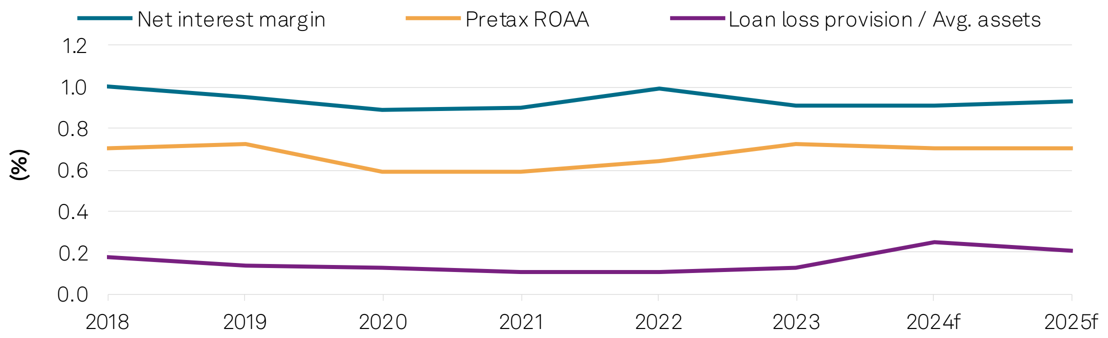
2. Hong Kong: High HIBOR benefits NIMs



3. Korea: Good record of managing asset quality



4. Taiwan: Improved core earnings offsets rising credit costs



1. SSEA--South and Southeast Asia. Source: S&P Global Ratings. 2. HIBOR --Hong Kong Interbank Offered Rate. Source: HKMA. 3. Chart reflects Korean banks' domestic regulatory nonperforming loan ratios by segment. Sources: Financial Supervisory Service, Korea. 4. ROAA--Return on average assets. f--Forecasts. Sources: Financial Supervisory Commission. Taiwan Ratings Corp.

S&P Global Ratings

Latin America

Credit Conditions: Latin America

- Our 2024 real GDP growth forecast for the region remains unchanged at 1.2% (or 2.0% excluding Argentina), although we revised expectations for several countries.
- For Brazil, we revised up our forecast to 2.0% growth this year (compared with 1.8% previously), mainly due to stronger-than-expected growth in the first quarter. In Chile, we now project the economy will expand 2.4% in 2024 (compared with 2.0% previously), also due to stronger-than-expected growth in the first quarter.
- For Mexico, we revised down our forecast to 2.2% growth in 2024 (compared with 2.5% previously), given softer-than-expected growth so far this year as construction and manufacturing activity moderates from strong levels in 2023. The resounding electoral victory by incumbent Morena party's Claudia Sheinbaum has increased investor concerns over the future of several reforms and the path of fiscal policy, as reflected in a surge in volatility in Mexico's exchange rate markets.

GDP growth forecasts (%)

	2019	2020	2021	2022	2023	2024f	2025f	2026f	2027f
Argentina	-2.0	-9.9	11.0	5.0	-1.6	-3.5	3.3	2.2	2.5
Brazil	1.2	-3.6	5.1	3.1	2.9	2.0	2.0	2.1	2.2
Chile	0.7	-6.4	12.0	2.1	0.3	2.4	2.6	2.6	2.7
Colombia	3.2	-7.2	11.0	7.3	0.6	1.1	2.8	3.0	3.1
Mexico	-0.3	-8.8	6.3	3.7	3.2	2.2	1.7	2.1	2.2
Peru	2.2	-11.0	14.0	2.7	-0.5	2.7	3.0	3.1	3.2

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

Credit Conditions: Latin America

Profitability To Moderate From Strong Levels And Remain Solid Relative To International Peers

Downside risks

- Continued strength in the U.S. economy has led to a longer horizon for interest-rate cuts by the Federal Reserve. A delayed start to cut rates will likely affirm Latin American central banks' determination in anchoring inflation expectations--meaning the process of shifting monetary policy to neutral from restrictive will take longer than previously assumed.
- A complex political landscape across Latin America which will likely result in market volatility over the next few quarters as investors strive to understand the new administrations' policies and the balance of powers that will drive the legislative agenda over the coming years.

...and what they mean for the sector

- Asset quality metrics have deteriorated across the region due to the soft economic performance, low credit growth, and pressure on the consumer and small and midsize enterprise (SME) lending segments. We expect asset quality metrics to stabilize by the end of this year and start improving in 2025.
- Provisions will likely remain high, denting profitability. However, operating performance will likely remain solid thanks to banks' higher margins than those of peers. Banks will continue to operate with solid capitalization and sound liquidity.

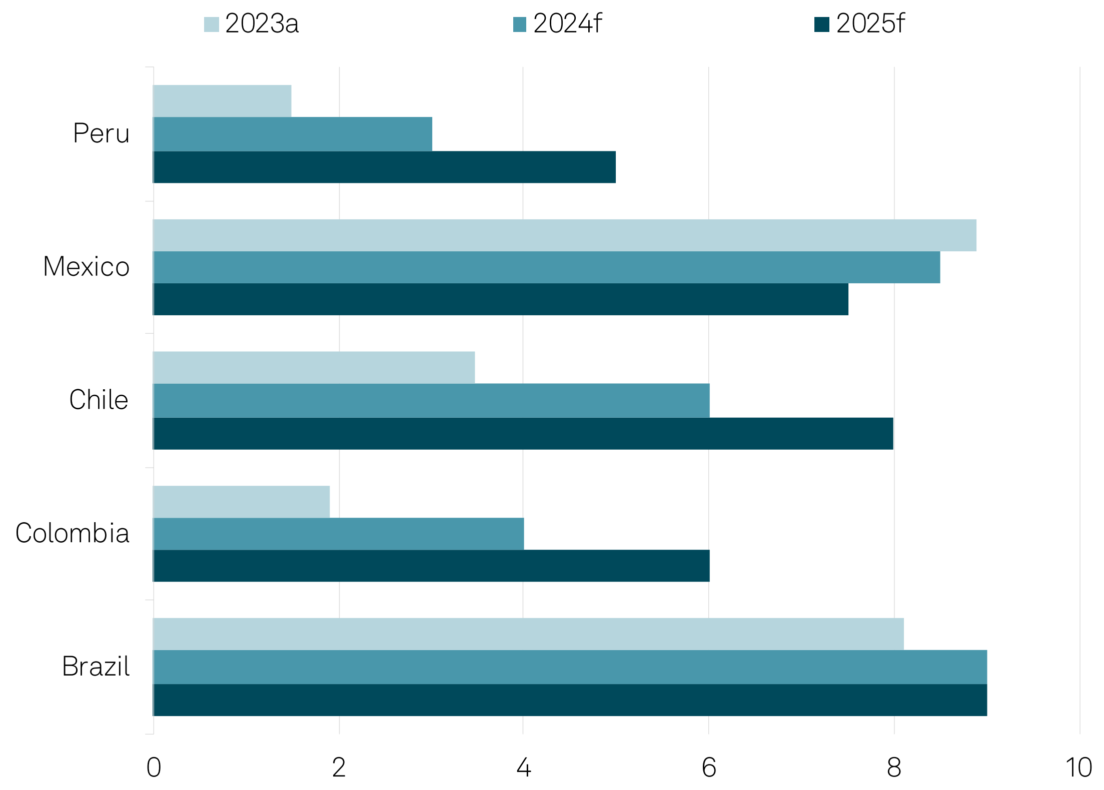
What we expect for next 12 months

- We expect the lending growth pace to remain at single digits. We expect a pick-up in credit demand in the corporate sector once interest rates fall to more affordable levels. But banks will likely continue to pursue conservative underwriting practices, given the tepid pace of asset quality stabilization.
- Banks in Latin America are used to operating in challenging operating conditions, and have solid regulatory capital and liquidity levels, which will help them navigate the tougher environment. Local regulators are typically stringent given the volatile economies, and regulation is implemented across all regulated entities.

Soft Economic Performance Will Limit Credit Demand

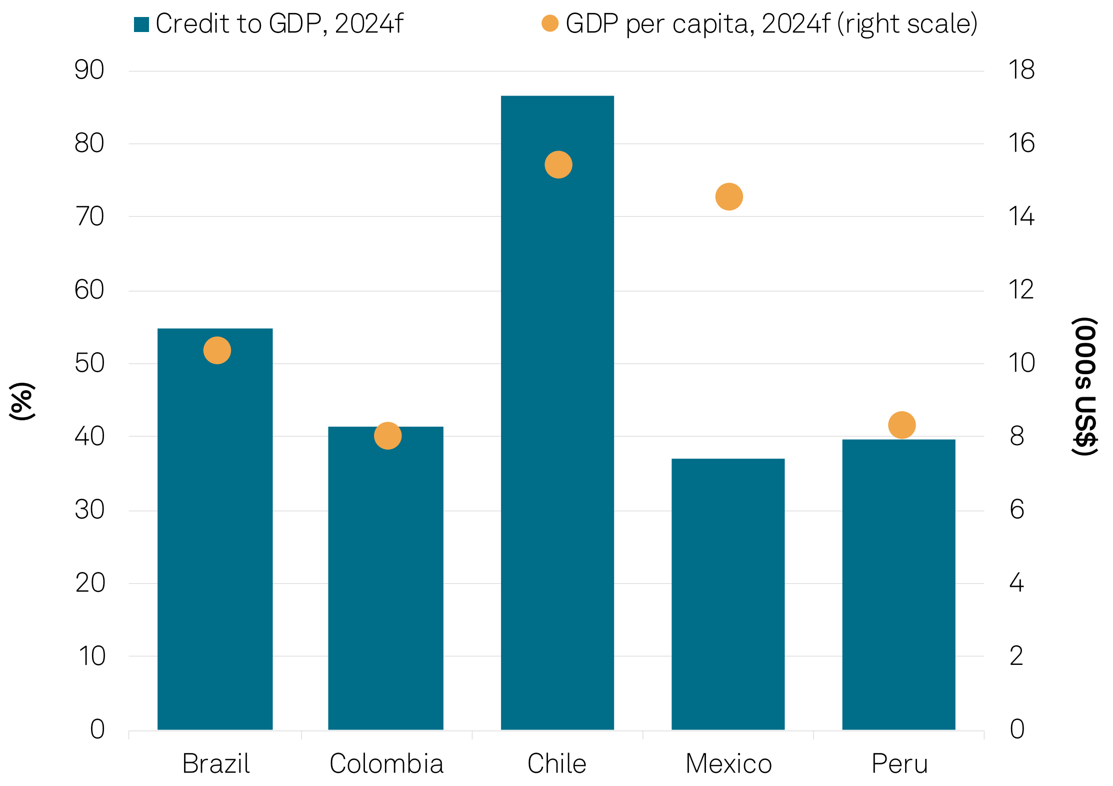
Modest rebound in credit growth in 2024-2025

Credit growth (%)



e--Estimate. f--Forecast. Source: S&P Global Ratings.

Access to credit remains low (except for Chile)

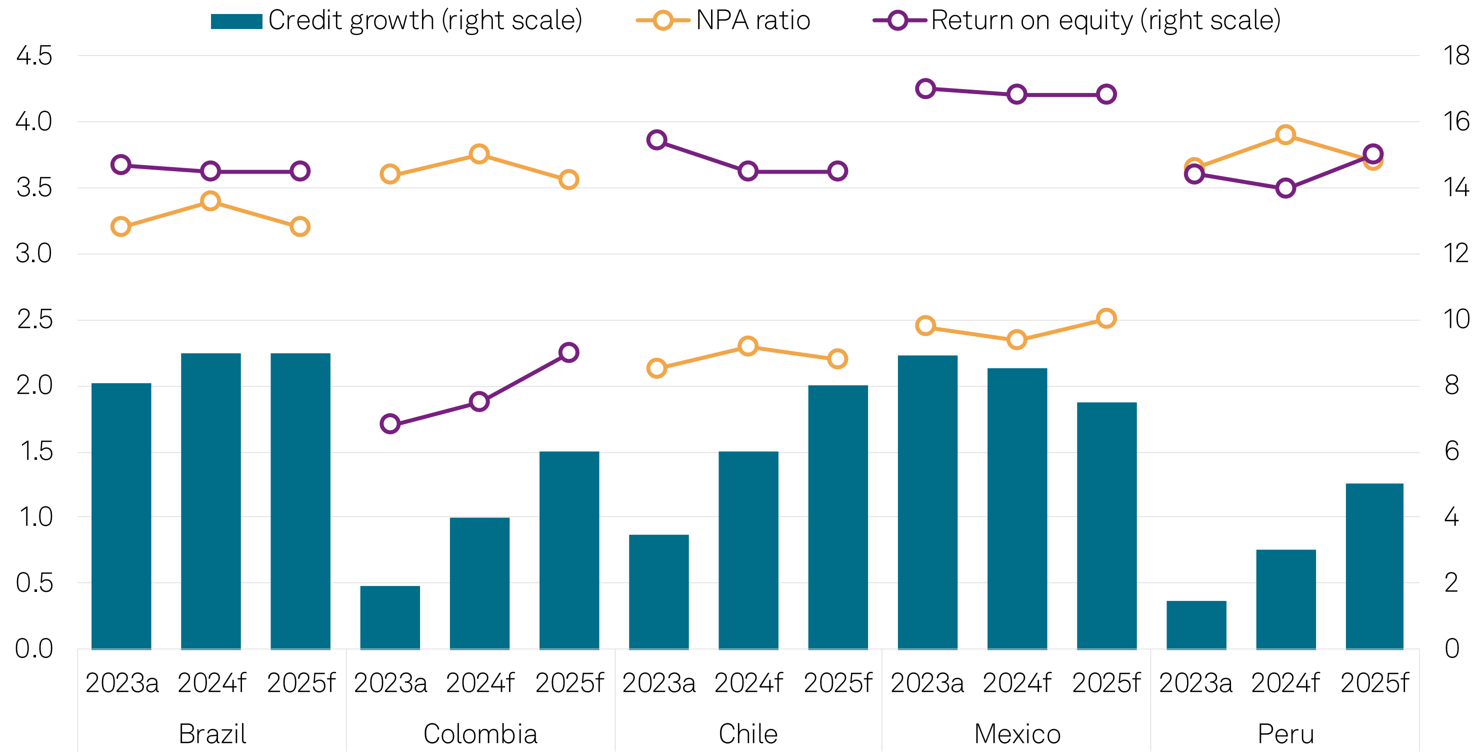


f--Forecast. Source: S&P Global Ratings.

S&P Global
Ratings

Stabilizing Asset Quality Metrics And Profitability

Profitability and asset quality metrics (%)



e—Estimate. f--Forecast. NPA--Nonperforming assets. Source: S&P Global Ratings.

Profitability will remain under pressure in in 2024 but will continue to be sound relative to global peers.

Asset quality will keep deteriorating in 2024 due to the still high interest rates and soft economy. We expect stabilization by the end of the year.

Subdued economic growth and persistently high interest rates will continue pressuring asset quality metrics in 2024.

Interactive Dashboard

How to access the Global Banks Midyear Outlook 2024 Dashboard

The Dashboard includes our in-house sector insights and trends, latest global and regional banking statistics and aggregate data.

Using the link, compare a banking system with its peers according to geographic region or BICRA group.

Click here

Global Banks Midyear Outlook 2024 Dashboard

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- Rising Global Defaults Will Test Private Credit Funds In 2024, May 1, 2024
- G-SIBs Monitor H1 2024 Published, April 25, 2024
- Capital Markets Revenue Could Improve In 2024 On Rebounding Investment Banking, April 25, 2024
- Banking Risk Indicators: April 2024 Update, April 22, 2024
- White Paper Explains Assessment Of How Megatrends May Influence Credit Ratings, April 18, 2024
- China Banks Brace For Tide Of Bad Property Loans, April 15, 2024
- Global Shadow Banks Face Scrutiny As Risks Rise, March 20, 2024

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