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Will Interest Rates Go Up Soon For Singapore Property Mortgages?

Many people are concerned the current low rate of interest environment in Singapore could end by the end of the current year, driving up the price of mortgages and putting force on the real estate market. In this article we take a look at how IRs in Singapore are determined, and where they are probably going to head for the remainder of the year and beyond.

How are rates determined?

In a 1999 paper titled "Interbank Interest Rate Backbone in Singapore and its Linkages to Deposit and Prime Rates", staff of the Monetary Authority of Singapore (MAS), the central bank, found that "only changes in US rates or market expectancies of future movements in the exchange rate have a significant impact on the domestic interbank rate."

But other analysts have discovered that the SIBOR has often been definitely correlated to the movement of the bank loan to deposit proportion, even after controlling for the impact of US IRs. This indicates that if bank loans grow quicker than deposits, SIBOR tends to head upwards.

So to sum up, exactly how rates in Singapore are determined is a debatable topic and there isn't any straightforward formula! But we all know there are three heavy factors which will influence it: 1) US rates 2) Market expectancies of the Singapore Dollar exchange rate (will it appreciate or depreciate?) and 3) Demand and supply for loans and deposits in Singapore.

So where are interest rates heading?

Hong Kong mortgage rates have already risen by as much as 1% over the last three months, driven by tight liquidity in the banking system as the expansion of loans have outpaced the expansion of deposits. Will rates in Singapore also head upwards because of the demand-supply dynamics in the local banking system, whether or not US IRs stay low for the moment?

In a corresponding situation to HK, loans have been growing faster than deposits, with loan expansion till April of 21.9% versus deposit growth of 12.7%. If the distance between the expansion of loans and deposits continues, this can increase the negotiating power of local banks and increase the probability of a higher SIBOR and also interest rate spread above SIBOR for mortgages.

But Hong Kong has its own precise dynamics "there's been a growing shift into Renminbi from Hong Kong Greenback deposits, that has been absent in Singapore as the MAS has let the Singapore Dollar appreciate against the US dollar, while the Hong Kong Greenback is attached to it. Actually the Singapore Dollar has even appreciated against the Renminbi over the past 2 years! But if the MAS comes to a decision to slow the appreciation of the Singapore Buck, we could begin to see higher rates.

Also, the Singapore government's contemporary moves to moisten conjecture in the property sector could lead to both lesser transactions and thus mortgage volume, and also a lower mortgage per exchange (as the Loan To Valuation limit has been lowered for investment properties). This indicates that loan expansion might start to weaken, while deposit expansion remains healthy in spite of the low rates as folk like to park their cash in a "strong" currency.

As for where US rates are headed, it is anybody's guess. But Singapore's Asian neighbors China and India have recently been raising rates to attempt to handle rising inflation. If inflation starts becoming a controversy in the USA, and policymakers have faith in the strength of the economy, then interest rate walks could come sooner than predicted.

While we don't expect a massive spike in interest rates shortly, they definitely can't go much lower, and borrowers should be prepared for scenarios where they start moving higher. For house purchasers, this means that you should not presume that rates will always remain this low, and to plan your finances so that you will still be in a position to meet your mortgage payments even though IRs rise.

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