Monthly Report on Banking and the Financial System

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Banking and the Financial System

Uptick in growth of lending to all three segments of the private sector

In May 2016 performing loans granted by commercial banks to the private sector grew at a nominal annual rate of 13.8% (10.9% real), representing an increase of 0.5 percentage points (pp) relative to the rate seen in April 2016 and above that seen in May 2015 (10.2%). This result was due to a faster pace of growth in the three lending segments, mainly in lending to businesses, which once again seems to be related to short-term economic factors, in particular the renewed bout of currency depreciation seen between April and May.

Bank deposits continue to perform well, driven by sight deposits

In May 2016 the nominal annual growth rate in traditional bank deposits (sight + term) was 12.9%, 1.1 pp more than that seen in the previous month. This greater dynamism was due to the improved performance of sight deposits, which increased their contribution to the growth rate in traditional deposits by 1.9 pp in May, from the 7.7 pp seen in April. The contribution of term deposits fell by 0.8 pp from the 4.0 pp seen in the previous month. The increased growth in sight deposits was led by the business segment, probably as a result of businesses redistributing their balances between short and long term, since the improved growth in this segment's sight balances was accompanied by a reduction in the rate of increase in its term balances, in a context of slowing economic growth in which businesses may be holding off on their investment plans.

INEGI (National Institute for Statistics and Geography) publishes results of the first National Survey on Productivity and Competitiveness of Micro, Small and Medium Enterprises 2015 (ENAPROCE in the Spanish acronym)

The ENAPROCE contains information on the economic and operational characteristics of micro-enterprises and SMEs, their management and entrepreneurial capabilities, the business environment in which they operate, the sources of financing and government support they use, the value chains of which they form part and their capabilities as regards the use of ICT. The ENAPROCE covered just over four million micro-enterprises and SMEs, of which 97.6% were micro, 2.0% small and 0.4% medium-sized.

One finding that stands out among those concerning sources of financing used by micro-enterprises and SMEs is that only 10.6% of micro enterprises have financing, compared with 27.8% for small and 39.8% for medium-sized enterprises. Another interesting result is that for those that do have financing, their main source is the formal financial system (53.2% for micro, 68.9% for small and 79.3% for medium-sized enterprises). On the other hand the survey reveals that 66.8% of all these businesses would not accept a bank loan. Most of them would not accept it because they consider it expensive (60.1% for micro, 52.6% for small and 46.5% for medium). Moreover, the main reason for loans being refused to micro and small enterprises was the lack of collateral or guarantee (25.2% for micro and 22.7% for small enterprises); whereas with medium-sized enterprises the main reason for being turned down (23.6%) was over-indebtedness.

The ENAPROCE is a useful source of information which will provide a more detailed insight into some of the characteristics determining the use of financing among micro-enterprises and SMEs. This could help financial institutions to offer products in line with the needs of these businesses and increase their access to formal sources of financing.

FUNDEF (Foundation for Financial Studies) publishes paper on financing of major companies

FUNDEF's paper, "Some factors explaining why lending in Mexico is low", analyses the corporate credit market for foreign and domestic companies in both the private and public sectors. Using a list of 500 companies which the authors consider representative of large companies in Mexico and information from the Credit Bureau and the Mexican Stock Exchange, it reviews the patterns of bank and capital markets financing.

In the case of bank financing, we see that Mexican companies' leveraging is more than double that of foreign companies, and that among Mexican companies the category with the highest levels of debt is that of public sector companies. In the case of the capital markets, the data show that foreign companies make little use of the Mexican securities market and that those that do make use of it are mainly in the automotive sector. Public sector companies show a clear preference for stock market financing, since this type of financing is more than twice that obtained through financial intermediaries.

Based on the information analysed, the study detects two factors that contribute to an understanding of why lending in Mexico is low compared with other countries with similar levels of development. In the first place although foreign companies account for a large part of the national economy, their demand for credit is low compared with their potential for generating revenue. This is because for them, domestic financing is a residual decision, since their basic needs are met by their parent companies. Secondly, the information shows that among public sector companies those in the energy sector stand out: PEMEX and CFE. In other countries, the financing of the activities carried out by these types of companies is classified as lending to the private sector, so when comparing the ratio of credit to GDP with that of similar economies, this difference should be borne in mind.

Financial markets

Signs of a more accommodative stance lasting longer in developed countries favoured financial markets in July

Movements in the financial markets in July were mainly influenced by signs of a more accommodative stance on the part of industrialised countries' central banks in response to increased risks to global growth. Following the wave of volatility unleashed by the outcome of the so-called "Brexit" referendum and increased concerns about growth, the European Central Bank, the Bank of England and the Bank of Japan all came out in favour of increasing monetary stimulus measures, and this, combined with the expected slower pace of rate hikes by the US Federal Reserve set investors off again on their quest for returns. As a result, equity markets worldwide posted gains, to such an extent that several indices reached new all-time highs during the month. In particular, the world benchmark for equity markets, MSCI World, gained 4.15%, the STOXX Europe 600 gained 3.64%, and the S&P 500 advanced 3.15%, bringing it to a new all-time record high during the month of 2,175 points. In Mexico, the IPC rose by 1.5% in July, and although this increase was less than the 4.7% seen in emerging markets (MSCI EM), it was enough to take it to a new record high of 47,537 points. As for currencies, demand for dollars picked up again following the release of better-than-expected June employment figures, which moderated the uncertainty about the US cycle, but second quarter GDP growth figures (1.2% QoQ annualised) brought a halt to this demand, to the extent that during the month the DXY index (US dollar against a basket of five major currencies) fell by 0.63%. The Mexican peso for its part depreciated by 2.52% in July, the fourth biggest depreciation among emerging market currencies, ending the month at 18.75 pesos to the dollar. We should point out that this depreciation, in a context of reduced risk aversion (the VIX ended the month at around 12%), was once again influenced by lower oil prices. The price of Brent crude fell by 14.5% in July on higher inventories in the US, ending the month at US$42 per barrel.

In the bond markets, following June's movements which reflected a quest-for-returns strategy, with the prospect of accommodative monetary stances lasting longer, the fall in oil prices (by around 15% since June) seems to be starting to produce a less favourable context for risk assets, which could lead to this strategy marking time for a while. We noted a certain contrast between movements in June and those in July, which seem to be starting to reflect this change. Whereas in June the yield on the 10-year Treasury note fell by 38 bps to end the month at 1.47%, and this drove the quest for returns, favouring, among others, the performance of long-term Mexican bonds and being reflected in a 25 bps fall in the rate of the M10 bond which stood at 5.89% at month-end, in July the movements show a flight to safety in US bonds and a certain braking effect on quest-for-returns strategies. The yield on the 10-year Treasury note ended the month at 1.45% (2 bps down from the end of June), while the interest rate on the M10 bond increased by 4 bps to 5.93%. All the same, even though the recent revaluation of long-term Mexican bonds came to a halt, their positive performance continues to stand out. In this context, Mexico's yield curve has continued its flattening trend. Whereas at the end of June the gap between the ten- and two-year bonds was 91 bps (already incorporating the effect of Banxico's 50 bps rate hike), at the end of July it was down to 60 bps. In the absence of a market downturn these trends can be expected to continue in the near future.

Regulation

Adjustments to deadlines for meeting capital requirements for operational risk

On 29 July the National Banking and Securities Commission (CNBV) amended the provisions regarding operational risk that allow credit institutions to meet the requirements in a staggered manner: 2H 2016, 30%; 1H 2017, 45%; 2H 2017, 80%; and 2018, 100%. It also established that banks must inform the CNBV in writing of their intention to make use of this option, and to state whether they intend to apply the standardised approach or the alternative standardised approach provided in the regulation. In no case will the application of this procedure allow banks to have levels of capital for operational risk below those reported at the end of June 2016.

Adjustments to capital regime

On 1 August the CNBV made some adjustments to the capital regime for banks. On the one hand it reduced the projection period for capital adequacy assessments from 12 to 10 quarters to bring it into line with the horizon at which banks carry out their own scenarios. It also reiterated the phasing in of the requirement for the countercyclical capital buffer, with the obligation to establish 25% of the requirement no later than year-end 2016, 50% by the end of 2017, 75% by the end of 2018 and 100% by 31 December 2019; and indicating lastly that with effect from 1 January 2020 credit institutions will have to comply at all times with their applicable capital buffer.

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