

Banks

Monthly Report on Banking and the Financial System

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Banking and the Financial System

At the end of 2016, growth in lending to the private sector was losing dynamism

In December 2016, [the balance of outstanding credit](#) granted by commercial banks to the private sector grew at a nominal annual rate of 15.3% (11.5% in real terms), less than the rate observed in November 2016 (17.1%). This development is mainly due to the slowing pace in nominal growth of lending to businesses (from 22.0% in November to 18.3% in December) and consumer credit (from 12.9% in November to 12.3% in December), while growth in housing loans remained practically unchanged (10.8% in November and 10.7% in December). In the case of lending to businesses, the slackening pace could be related to the reduced valuation effect of exchange rates on borrowings contracted in foreign currency, since during December the peso depreciated less than in November. In the case of consumer credit, the lower growth rate relative to the previous month might be associated both with households' advance purchases in November in order to take advantage of *Buen Fin* (loosely speaking the Mexican equivalent of Black Friday) promotions, and with greater caution on the part of consumers faced by a more uncertain economic environment.

Bank deposits lost momentum because of slower growth in both their components (sight and term)

In December 2016 the nominal annual growth rate in traditional bank deposits (sight + term) was 13.2%, 1.6 pp below that seen in the previous month and 0.1 pp below that recorded in the same month of the previous year. This loss of dynamism was the result of reduced growth in both its components. Sight deposits (63.7% of total traditional bank deposits) grew at a nominal annual rate of 14.4%, 1.4 pp less than the 15.8% posted in the previous month. Term deposits (36.3% of total traditional bank deposits) grew at a nominal annual rate of 11.2%, 2.0 pp less than the 13.2% seen in the previous months. It is possible that the reduced growth in the sight segment has to do with the increase in public spending during the period. According to SHCP (Secretariat of Finance and Public Credit) figures total public spending grew at a nominal annual rate of 9.2% in December, 3.3 pp more than in November. As for term deposits, the flagging pace of growth is probably the result of the slowdown in economic activity observed in the period, as suggested by the Global Economic Activity Indicator (IGAE in the Spanish abbreviation) which reported annual growth of 2.1% in December, 1.6 pp below that posted in the previous month.

Businesses are finding the environment less favourable in terms of accessibility to banking finance and its cost

Mexico's central bank (Banco de México) published a communiqué on the [Development of Business Financing](#) during the last quarter of 2016. The report presents the main results of the Quarterly Credit Market Assessment Survey conducted with a sample of businesses with nationwide coverage.

The results indicate that the sources of financing most used by businesses are suppliers and commercial banks. For 4Q16, 38.5% of respondents said they had borrowed from commercial banks, a lower percentage than in 3Q16 (38.9%) and 4Q15 (41.4%). In 4Q16, 76.8% of businesses used supplier credit and 20.7% obtained financing from other companies in their group or from the parent company. In both cases, the percentages were the highest recorded since 2Q15.

The percentage of businesses using new loans in 4Q16 was 25.9%, slightly less than the 26.3% recorded in 3Q16, but more than at the end of 2015 (25.1%). Among these businesses, the indicators of conditions of access to the bank credit market report more accessible conditions as regards the amounts offered, but less favourable in conditions for refinancing, terms (periods) offered, collateral required, approval times and other requirements of the banks. As regards to the cost of bank borrowing, the perception is of higher interest rates, commissions and other expenses.

International Monetary Fund (IMF) publishes a study on financial depth in Mexico

The IMF published a working document entitled "[Financial Deepening in Mexico](#)". The study documents the low penetration rate of credit in the country, controlling for a series of macroeconomic variables and some that reflect characteristics of the institutional environment. With information on bank financing to the private sector up to 2015, the authors estimate the size of the credit gap as at least 40% of GDP; however, they point out that informal credit might be playing an important role given the share of the informal sector in the economy. Empirical evidence points to structural aspects being behind the low level of financial intermediation observed, as is suggested by the fact that growth in lending these past few years has been driven by supply and by the lag between credit cycles and economic cycles. The authors cite as possible causes of the low level of intermediation the history of banking crises, a low level of financial education, an informal sector of considerable size and an inefficient legal system as regards execution of collateral. The financial reform of 2014 sought to address some of these obstacles, but it has still not been fully implemented. The study warns that, while a higher penetration rate is desirable, if lending increases too fast it could make economic growth more volatile and lead to financial instability.

Update of the housing price index at the close of 2016

In February, the SHF (Federal Mortgage Company) published the housing price index for the fourth quarter of 2016. According to this indicator at the end of last year housing prices were up by 7.41% in real terms. The sub-index for the medium-residential segments rose by 8.36% annualised in the quarter, whereas the sub-index for the social housing segment rose by just 6.36%. This difference of two percentage points, which held steady

throughout 2016, continues to reflect greater demand for more expensive housing. At the same time the social housing market continues to contract, partly due to consumer preferences but also because of reduced amounts of subsidies for new home purchases. Although the Secretariat for Agricultural, Regional and Urban Development (SEDATU in the Spanish acronym), through the National Housing Commission, announced in February that it would bring forward by two months the allocation of subsidies, these will not be enough to reactivate demand in the low-cost segments, since the amount for 2017 represents a reduction of just over 30% relative to 2016.

Financial markets

Better-than-expected US economic data sustain risk appetite; the peso appreciates, underpinned by the measures taken by Banco de México

In a context of uncertainty as to the policies of the Trump administration, the improvement in many of the US economic indicators sustained risk appetite in the financial markets. The lack of details on the pro-growth policies of the new US administration (cut in corporation tax, spending on infrastructure and less regulation) did not interrupt the rise in equity markets observed since last November, given the improvement in employment indicators, manufacturing production and the service sector of the US economy, combined with better-than-expected corporate earnings reports. The S&P500 reached a new all-time high after gaining 3.72% during February, an increase which exceeded that of the global equities benchmark MSCI World by more than one percentage point. This increase in risk appetite also extended to emerging markets, which gained 2.98% (MSCI EM) in February and to European markets, which gained 2.81% (Euro Stoxx 600). In Mexico, the IPyC stock market index ended the month down by 0.31%, largely influenced by the fall of more than 1.0% on the last day of February as a result of the volatility caused by Donald Trump's first speech to the US Congress and of some delays in corporate earnings reports. We would point out that despite the fact that uncertainty about economic policy, particularly in the US, is running high, traditional indicators of volatility in the financial markets such as the VIX are still at all-time lows. Additionally, the apparent compliance with the OPEC production cuts has maintained some stability in the price of oil at around US\$56 per barrel.

In the currency markets, the tone of the US Federal Reserve's discourse largely reversed the dollar's losses. Members of the Federal Reserve's Open Market Committee made it clear in their public statements that they were seriously considering the possibility of increasing the federal funds rate at the meeting of 15 March. As a result, and rather unusually, the implied probability of a 25 bps rate hike at the March meeting in the futures market went from less than 30% to 80% at the end of February. This change of tone strengthened expectations of a faster rate of monetary normalisation, which increased the demand for dollars to such an extent that during the month the US dollar gained 1.48% relative to other developed countries' currencies. In the particular case of the Mexican currency, the announcement of auctions of currency hedges for settlement in pesos by Banco de México led to the peso's appreciating by 2.9% during the month, considerably more than the 0.88% appreciation of the emerging market currencies benchmark, and ending the month with the third biggest gains against the dollar of all emerging market currencies. In fact the central bank's announcement simply reinforced an existing

upward trend based on the perception that in the most likely scenario trading relations between Mexico and the US will not be fundamentally disrupted.

Regulation

Amendments to Circular 3/2012 on participation in clearing houses, addressed to credit institutions, Financiera Rural and Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero (state-owned rural development banks)

On 9 February Banco de México [simplified](#) the requirements for accessing the services of document clearing houses (for cheques and electronic transfers), while seeking to maintain competitive and equitable conditions for these services' fees. Among other aspects, the amendments clarify the right of any credit institution to join a clearing house while not being a shareholder and strengthen the clearing houses' obligation to not discriminate among its members.

Distribution of subsidies through basic accounts

On 14 February Banco de México [published](#) amendments to Circular 22/2010 on basic accounts for the general public, laying down additional conditions for the basic account in order to flexibilize its operation for the distribution of government subsidies and at the same time, to promote the incorporation into the financial system of the subsidies' beneficiaries. The amendments establish more relaxed standards for keeping these accounts open in terms of minimum movements and balances.

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