Monthly Report on Banking and the Financial System

Javier Amador / Fernando Balbuena / Alfonso Gurza / Iván Martínez / Saidé A. Salazar / Carlos Serrano / Mariana A. Torán / Sirenia Vázquez / Samuel Vázquez

13 July 2017

Banking and the Financial System

Business loans are underpinning the buoyancy of private sector credit

In April 2017, the balance for performing loans granted by commercial banks to the private sector grew at a nominal annual rate of 16% (9.6% in real terms), 0.9% more than the previous month (15.1%) and above the growth rate reading for April 2016 (13.8%). For the second month running, growth was due to the persistence of business loan expansion, which moved from a nominal annual growth rate (AGR) of 17.4% in March to 19.2% in April, while consumer credit held at a growth rate of 11.1% and housing credit dampened from 11% to 10.6%. The increase in business loans could be a reflection of more optimistic business expectations than in previous months and a higher business preference for assuming bank borrowing rather than non-banking debt. Within consumer credit, there are mixed performances among segments, in line with distinct trends exhibited by certain domestic demand indicators. Whereas retail sales were up in April, real wages and household purchasing power are still being eroded by higher inflation. This might also be influencing a slower pace of housing credit growth.

Banking deposits increased in both the demand and term segments

In April 2017 the nominal AGR for traditional banking deposits (demand + term) was 13.7%, 2.3 percentage points (pp) above the figure observed for the previous month and 1.9pp more than the same month a year earlier. Traditional bank deposits performed better at the beginning of the second quarter of the year as a result of a more spirited showing by both demand and term deposits. Demand deposits nominal AGR was 14.6%, which was 2.3pp more than in the previous month, while new term deposits recorded an annual percentage variation of 12.1%, up 2.5pp on the figure for March. A healthier performance by demand deposits segment is likely to be attributable to a lower level of activity by non-bank financial intermediaries, probably owing to weaker economic activity that emerged for the period, as is suggested by the Global Economic Activity Index, which in April showed an annual percentage variation of -0.7%, 5pp down on the previous month. On the other hand, a stronger term deposits growth might be linked to a slacker pace in investment by the corporate segment and the effect of higher interest rates. In April, the Gross Fixed Investment Indicator offered an AGR reading of -8.6%, i.e. 12.5pp below the figure recorded the previous month. On the other hand, the Industrial Activity Indicator produced an annual percentage change of -4.4%, which was 7.6pp below March data.

Mortgage rates are firmly on the rise

After three years of marking a downward trend, interest rates in the mortgage market hit rock bottom in the second half of 2016. Even so, the transmission from Banxico's monetary policy has been limited given that, while the reference rate was hiked by over 2.5% in 2016, mortgage rates only rose by around 0.32%.

Mortgage loan rates climbed from 9.27% in February last year (the month in which the first reference rate hike was announced) to 9.6% in December, while at the close of March 2017 they stood at 10.2%. Nonetheless, the 0.6% rise in the first quarter is likely to be explained by movements in long-term rates, given their high correlation with the mortgage market. This is because almost all commercial banking loans are granted at fixed rates and over terms averaging 18.5 years.

The ten-year bond (M10) has proved to be the most suitable benchmark for monitoring mortgage rates. Therefore, the stability of this particular instrument likely explains the relative lack of variation in banking mortgages rates last year. However, in the last quarter of 2016 the M10 rate ticked up from 6.05% in September to 7.42% in December, which passed through to the mortgage market in the first quarter of this year. It is worth noting here, that the M10 stabilized at 7.01% by March close.

For all these reasons we foresee mortgage rates potentially ending up with a further 30 basis points (bp) increase in December 2017 to reach 10.5%, in line with M10, which could close with an annualised yield of 7.3%.

The CNBV has released an update on its Financial Inclusion Report

The National Banking and Securities Commission (CNBV) has published the eighth update to its National Financial Inclusion Report (Report), featuring figures as of June 2016. As regards infrastructure, the Report includes a total of 241 institutions, comprising commercial banking institutions (47), development banks (6), savings and credit cooperatives (149) and popular finance institutions (44). With respect to access channels on a nationwide level (branches, banking agents, ATMs and point of sale terminals (POSs)) a 17.8% increase was reported between June 2015 and June 2016. Municipal coverage by these channels remained distinct over the reference year: branches had a presence in half of municipalities, ATMs in 62.7%, POS terminals in 72.5% and banking agents in 77.1% of them. The percentage of municipalities having at least one access point moved up from 68.9% in June 2015 to 72.5% in June 2016.

In this update, the report features a review of transactions in the financial system. Notable among the results was that from 2010 to 2016 there has been both accelerated growth in cash transactions and a drop-off in the amount per transaction for bank transfers, which is attributable to the tax reform coming into effect in 2014. The Report also finds that the mean of payment which has shown the largest growth is POS terminals, followed by ATM transactions and transfers. In contrast, the number of cheque transactions dwindled over the same period. On the other hand, the number of debit card contracts has risen at a faster rate than credit cards (CCs), which indicates that the former is taking hold as an effective mechanism towards population's financial inclusion.

With respect to savings products, as of June 2016 deposit contracts totalled 111 million, 9.5% up on the level reported for the corresponding month the previous year. Of these contracts, 81% were made with commercial banking institutions. Despite this increase, differences still persist from state to state and the challenge remains to increase coverage in the southern states of the country.

Regarding credit penetration, it is notable that the number of loans granted by banking institutions and Popular Savings and Credit Institutions (EACPs) shrank slightly between June 2015 and June 2016, which was reflected in a drop in the number of credit contracts per 10,000 adults from 6,110 to 5,936. Most contracts are concentrated among only a few types of credit: Credit cards and personal loans in the banking sector (over 70%) and consumer loans in the case of the EACPs (more than 95%).

Looking at retirement savings, as of June 2016 there were 54.5 million accounts registered, which represented growth of 1.8% relative to June 2015. At the close of the first half of 2016 (1H16), funds invested in Siefores reached 2.7 trillion Mexican pesos (15% of GDP). Between June 2015 and June 2016 voluntary contributions were reported for only 1% of total accounts.

With respect consumer's protection in financial services, the document reports that between 1H15 and 1Q16, the number of actions to protect consumers rose by 9.7%. 85% of total actions filed to CONDUSEF (the National Commission for the Protection and Defence of Financial Users) relate to advisory and consulting assignments, and only the remaining 15% are associated with claims by consumers against a particular financial institution.

Finally, the Report includes sections that analize financial education and financial inclusion issues from a gender perspective.

Banxico has updated its report on housing loan indicators

The central bank updated its Basic Housing Loan Indicators, with data as of September 2016. Although it does not include loans granted by the government housing agencies INFONAVIT and FOVISSSTE, it does include information on loans co-financed by these institutions and commercial banks. At the end of September 2016 the total balance of housing loans accounted for 19.7% of the portfolio granted to the non-financial private sector. At the end of 3Q16 the housing portfolio grew by 7.1% in real terms compared to the like quarter the year before and showed a delinquency rate of 3%, keeping the falling trend that began from 4Q14 onwards. The most significant type of loan within the housing portfolio is the new or second-hand homes (80.3% of the balance granted between October 2015 and September 2016). In the most recent 12 months this segment exhibited a weighted average lending rate of 9.2%, a loan term ofover 19 years and an average loan amount of 1.25 million pesos. Pay off loans increased its importance, reaching 11.3% of the balance granted between October 2015 and September 2016, due to customers switching their mortgages between lenders as the market became more competitive.

Payroll loans have become more sluggish in spite of the improved conditions as regards the sum borrowed and the lending rate

Banxico updated its Basic Payroll Loan Indicators with information as of December 2016. By year-end the payroll credit balance represented 24.4% of overall consumer credit, achieving a real growth rate of 10.1% between December 2015 and December 2016, and easing off the pace considerably compared to the year before (17.1% between December 2014 and December 2015). Payroll loan delinquencies in December 2016 stood at 3.4%, lower than the figure for consumer credit in general (4.2%). Of the 4.3 million credit facilities in place at the end of 2016, 60.2% were granted in the past year, equivalent to 71% of the total balance. The average weighted interest rate on new payroll loans was 25.1%, lower than the average weighted rate of 26.1% reported in the previous year (December 2015). The average loan amount granted over the last year was 62,100 pesos (7,800 pesos more than the average for the previous year) while the average term increased to 43 months, one month more than in December 2015.

A recent study offers evidence of how card-holders in Mexico spread their borrowing among credit cards

In an original new study, Ponce, Seira & Zamarripa (2017) examine the behaviour of CC users in Mexico to asses whether they manage to minimise their costs by using the lowest interest rate card. Based on a representative sample of card-holders and using data from 2004 to 2005, they find that relative prices have little impact on the decision to allocate debt and making purchases or payments. Consumers allocate a high proportion of their balance (24%) to the most expensive CC and, as a result, they end up paying 31% more interests. They also use experimental data and find that, when offered a lower interest rate, consumers raise their overall debt but fail to reallocate it from the costliest card to the cheapest. Based on a survey conducted expressly for this study, the authors conclude that such behavioural patterns could be due to the fact that, when consumers make purchases or payments, they do not compare interest rates, which implies that the amount of outstanding debt seems to be a more powerful predictor of the allocation of payments and their balance.

Financial Markets

Central banks take centre stage again. The Mexican peso continues to go from strength to strength and is approaching levels not seen in over a year

Announcements by central banks over June were, to a large extent, decisive in moving financial markets. In Mexico's case, the clear signal of an end to monetary tightening from Banxico wrong-footed the markets and prompted significantly lower policy rate expectations for the years immediately ahead. This in turn caused rates in the middle and at the long end of the curve fell away to such an extent that its slope turned negative. In fact, even though the reference rate was raised by 25 bp to 7% in the month, the yield to maturity of the 10-year bond closed with a drop for the period of almost 60 bp to 6.8%. Meanwhile, the less accommodative tone of announcements from the president of the European Central Bank and the governor of the Bank of England in the final few days of June produced a feeling in markets that the withdrawal of stimuli is not far off, which translated into a rise in long term rates of as much as 10 bp on the month in the case of 10-year Treasury bonds. This, together with the comments by the chair of the Fed that certain stocks appeared "over-priced", contributed to slow down gains on stock markets – the S&P500 ended the month with a rise for the period of 0.5% following a major dive in technology stock prices. This outperformed the global equity market benchmark, the MSCI World, which rose 0.25%. In the case of the emerging markets, the rise was 0.54% (MSCI Emerging Markets), but even so, the Mexican market shone by recording a 2.2% MoM gain.

On the Forex market the Mexican peso marked levels of under 18ppd for the first time since May last year on formalisation of the NAFTA renegotiation process by the United States and the traditional government party's victory in the State of Mexico elections. Nonetheless, towards the end of the month a tumbling oil price (-8%) and fluctuations in global volatility left it standing at 18.12 pesos per dollar. This 3.1% appreciation in June was again notable when held against the average performance for emerging currencies, which barely firmed 0.4%.

Regulation

Adjustments to the Banking Regulation Circular (CUB) of the CNBV

On 26 June the CNBV amended its provisions for Credit Institutions in order to adjust credit rating and provisioning methodologies. First, there is a change on how secured interests (different from mortgages) are treated in estimating loss given default for non-revolving consumer credit, credit card and other revolving loans, and microcredit portfolios. For the purposes of calculating loss given default, price coverage for agricultural loans is recognised, while the requirements for its recognition are established. Finally, the period for complying with loan provisioning derived from the non-revolving consumer credit, home mortgage and microcredit methodologies published on 6 January 2017 has been extended.