BBVA Research

Banks

Monthly Report on Banking and the Financial System

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1.1. Banking and the Financial System

Private sector credit keeps the growth rate in double figures at the start of the year

In January 2019, the annual nominal growth rate of the balance of private sector credit granted by commercial banks was 10.1% (5.5% in real terms). This growth was a little more than that of the previous month (10.0%) and less than that of the same month of 2018 (11.8%). The average annual nominal growth rate for the twelve-month period from February 2018 to January 2019 was 11.4%. This average growth rate is higher than that recorded in January 2019. On the other hand, the annual nominal growth rates of the main categories of bank credit were as follows: corporate, 11.6% (6.9% in real terms); housing, 9.9% (5.3% in real terms); consumer 6.3% (1.8% in real terms). As a result of this performance, the contribution made by bank credit components to the total growth of 10.1 percentage points (pp) in January 2019 was as follows: business credit, 6.5 pp; housing, 1.8 pp; consumer, 1.5 pp.

These contribution figures indicate that business credit in January 2019 continues to be the main driver of private sector credit growth, due to bank credit in the country having replaced internal and external non-banking financing. On the other hand, the slowdown of consumer credit could reflect a lower rate of formal job creation, whereas the better performance of housing credit could be mainly associated with a relative improvement in workers' real salaries.

More moderate performance of traditional bank deposits

In January 2019, the annual nominal growth rate of traditional commercial bank deposits (sight + time) was 7.8% (3.3% in real terms), similar to that of the previous month (7.9%) and lower than that recorded in January 2018 (9.0%). This result reflected a slight recovery in the growth of sight deposits that failed to offset the decline in time deposits. In the case of sight deposits, the annual nominal growth rate was 5.3% (0.9% in real terms), 1.5 pp higher than that of the previous month. This recovery could be due to the effect of lower opportunity costs of maintaining sight deposits. On the other hand, time deposits experienced an annual nominal growth rate of 11.7% (7.0% in real terms), below the annual nominal rate of 14.3% recorded in January 2018.

The reallocation of funds toward more liquid instruments would explain this moderation in the growth rate of longer term savings. As a result of this performance, sight deposits accounted for 3.2 pp of the 7.8% growth in traditional bank deposits, while time deposits contributed 4.6 pp. Therefore, despite the slowdown and lower share of traditional deposits, time deposits continue to be the most important driver in the growth of traditional bank deposits.

The CESF reviews its balance of risks, highlighting the increase of foreign risk

In March, the CESF (Consejo de Estabilidad del Sistema Financiero — Mexican financial system stability council) updated its balance of risks and published the main conclusions of its 2019 Annual Report. Based on its analysis, global economic activity has been experiencing a slowdown since the end of 2018, evidenced by the reduced dynamism of most of the main advanced economies and certain emerging economies. This deterioration has resulted in lower economic growth forecasts for 2019 and 2020.

The CESF believes that the main external risks that might affect Mexico's financial system are: 1) Uncertainty caused by the escalation of trade tensions between China and the USA; 2) the possibility of the UK's disorderly exit from the EU; 3) the possible aggravation of geopolitical tension; 4) a faster-than-expected slowdown of the global economy; 5) more stringent financial terms; 6) a reduction in global risk appetite leading to a reversal in capital flows in emerging economies and the spread of this trend to economies with weaker macroeconomic fundamentals.

On the other hand, the decision of three rating agencies to change Mexico's credit outlook from stable to negative is just one of the internal risks identified by the CESF for the Mexican financial system. In their decisions, the agencies noted that the change was partly due to the uncertainty associated with certain public policies and to risks relating to the new energy sector strategy, as well as the challenges posed by Pemex's financial situation. According to the CESF, there is a need to maintain a solid macroeconomic framework that encourages price stability, fiscal discipline and financial stability.

The CESF has also continued to implement cybersecurity measures, underlining the importance of working alongside the authorities and regulated organizations in order to further strengthen the IT security of the financial system.

As for the banking system in Mexico, the CESF considers that the banks have sufficient capital and reasonable liquidity levels to handle stress situations and that the prudential regulations for Mexican banks have ensured that the volatility of the financial markets does not constitute a direct risk for their solvency or liquidity. However, the authorities are advised to track the behavior of certain specific vulnerabilities that are principally associated with the concentration of financing sources in some institutions.

The CNBV announces a new publication on financial inclusion

In March, the CNBV (Comisión Nacional Bancaria y de Valores — National Banking and Securities Committee) presented the first edition of the "Financial Inclusion Bulletin," to be published every quarter. The goal of this quarterly publication is to review the main studies on financial inclusion prepared by international organizations, public and private national institutions, and academics and researchers. It also aims to track and review financial infrastructure and the access to and use of financial products in the country.

Its first edition includes reviews of the most significant results of the latest National Financial Inclusion Survey, the ninth National Financial Inclusion Report and the Global Microscope 2018. With regard to the performance of financial product access and use indicators, the Bulletin highlights the increase in points of service per 10,000 adults from 11.2 to 12.6 for the period from December 2015 to June 2018. The percentage of municipalities with at least one point of service increased from 72.0% to 75.7% and the share of the adult population living in a municipality with at least one point of service rose from 97.25% to 98.1%. In terms of indicators of use, the bulletin points out that deposits increased from 12,161 (contracts per 10,000 adults) to 12,186, whereas credit products increased from 5810 (contracts per 10,000 adults) to 5,951.

1.2. Financial Markets

The economic slowdown and unchanged interest rate expectations are the main factors behind financial market movements

The world economy is currently at a phase of the cycle that combines symptoms of decline with no medium-term changes in interest rates. In light of this scenario, investors are constantly looking for signs to help them quantify the extent of the slowdown and the risk of a possible recession in the near future, which explains the increased sensitivity of the financial indicators to economic activity data in the main developed economies. Monthly data for March show that not all regions are experiencing the slowdown in growth and that, to date, a recession in the USA or a sharp drop in growth in China do not form part of the most likely scenario. Given these data and the absence of inflationary pressures, the central banks of industrialized nations have eased their monetary positions, to such an extent that the average forecast for March of the members of the Federal Open Market Committee (FOMC) indicates that the federal funds rate will not be increasing in 2019. These forecasts had already been included in market prices since the start of the year.

This context of slowdown—which is still some way away from recessive behavior—combined with the expectation that interest rates for the rest of the year will remain unchanged, has boosted profits in the stock markets. In March, the main stock indexes of the USA and Europe showed gains of around 1.7%, higher than the global equities benchmark, which increased somewhat over 1.0%. The behavior of the IPC in Mexico was similar to that observed on a global level (1.07%) and above the level of stock markets in emerging countries (0.68%).

In the fixed income market, prices reflect a more prudent reaction to the environment. The government yield curve in the USA in March showed a downward slope among certain tenors, due a sharper drop in the longer share of the curve that led the yield to maturity of the 10-year bond falling below 2.4% for the first time since the end of 2017. In Mexico, the longer part of the curve continued falling after the upward trend observed at the end of 2018. This resulted in the yield to maturity of the 10-year bond closing the first quarter of the year slightly above 8.0%, for the first time since October 2018. In short, the 10-year node has dropped by almost 125 basis points between the end of November (when it reached its highest point) to the end of March.

On the other hand, the currency market closed in March with monthly gains for the US dollar. Against developed currencies, the US dollar increased by 1.2% — influenced by the uncertainty regarding Brexit and lower-than-expected manufacturing data in the Eurozone, which appears to be the region showing the most weakness at present. Against all of the emerging currencies, US dollar gains reached 1.7% due in part to the significant depreciation of the Turkish lira, as a result of political events. Meanwhile, although the Mexican peso underwent a depreciation of 0.8% in March, this performance was heavily influenced by the general aversion behavior toward emerging currencies in the last third of the month, given that until 20 March—the date of last FED meeting —the peso had risen 2.4%. In fact, the exchange rate reached 18.82 pesos per dollar on that date. In general, the behavior of the peso has been mainly supported by the higher relative risk-adjusted yields of local assets compared to other emerging nations, amid a context of certain pursuit of profitability, in light of expectations that the Fed will not take further action for the remainder of the year.

1.3. Regulation

Amendments to the FTI single circular

On March 25, amendments that extended banks' information security system to financial technology institutions (FTIs) were released. The regulations aim to protect institutions and their customers from cyberattacks that might affect the confidentiality, integrity and availability of information. The regulations focus on information security, the use of electronic means, information security standards in outsourcing and on the disclosure of information relating to projects and their progress to consumers and to the general public. They also establish the content and frequency of delivery of regulatory reports to the CNBV.

Provisions applicable to innovative models (*start-ups*)

On March 11, the SHCP (Secretaría de Hacienda y Crédito Público — Mexican secretariat of finance and public credit) issued provisions that established requirements, additional to those set forth in law, to obtain the temporary authorization to operate under innovative models. The regulations further address the registration of corporations that obtain said authorizations, as well as the reports to be presented regularly to the SHCP.

Bank of Mexico issues provisions regarding the internal use of virtual assets

On March 8, the Bank of Mexico published Circular 5/2019, on the use of virtual assets by banks and FTIs exclusively for internal operations. To this end, it establishes the criteria that must be met in order to obtain the authorization established by law.

The Bank of Mexico regulates foreign currency transactions by crowdfunding institutions

On March 8, the Bank of Mexico published Circular 6/2019 establishing the terms and conditions according to which crowdfunding institutions may perform foreign currency operations, as well as the information to be reported to the Bank of Mexico.

Systems for innovative models (*start-ups*)

On March 8, the Bank of Mexico published its regulations setting forth the procedure for authorizing start-ups with regard to CONSAR (Comisión Nacional del Sistema de Ahorro para el Retiro — Mexican national pension system commission) related activities, as well as with regard to the public registry of companies authorized to operate under innovative models and the regular reports to be presented to CONSAR.

On the other hand, the Bank of Mexico published the provisions for the authorization of corporations interested in implementing innovative models to provide clearing, payment and settlement services. The provisions seek to disclose required information to its participants and their customers, along with guidelines to mitigate operational and cybersecurity risks.