

# Monthly Report on Banking and the Financial System

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## Banking and the Financial System

### Credit to the private sector is maintaining a good rate of growth because of consumption and companies

In June 2016 the balance of [performing loans granted by commercial banks](#) to the private sector grew at a nominal annual rate of 15.5% (12.7% real), representing an increase of 1.8 percentage points (pp) relative to the rate seen in May 2016. This result was due to a higher rate of growth in consumer and company credit, which in turn is related to incipient recoveries in domestic consumption, in household income and in some economic sectors such as construction and services.

### Bank deposits record better performance led by the term segment

In June 2016 the nominal annual growth rate in traditional bank deposits (sight + term) was 14.5%, 1.6 pp more than that seen in the previous month and 1.0 pp above that recorded in the same month of the previous year. Sight deposits increased their contribution to the growth rate of traditional deposits by 0.6 pp, from the 9.6 pp seen in May. The boost in sight deposits was led by deposits from Non-Bank Financial Intermediaries (NBFIs). Meanwhile, the contribution of term deposits fell by 1.1 pp from the 3.2 pp seen in the previous month. In this case, greater dynamism was seen in the companies segment.

Perhaps the better performance of term deposits in the companies segment (the main engine of growth in traditional deposits in the period) was motivated by a restructuring of the financial savings of these agents (between their short- and long-term deposits), in an environment which has seen a moderation in economic activity and a slower pace of investment.

### The most recent inflation report from the Bank of Mexico notes that savings and external financing have slowed, in favour of more dynamic domestic sources

In its [quarterly inflation report April-June 2016](#) (2Q16), the Bank of Mexico said that during 2Q16 the sources of the economy's financial resources moderated their growth rate compared with that seen in the first quarter. This was the result of a slowdown in external sources, motivated by the volatile environment that persisted in international financial markets. The item that was most affected was the balance of financial savings of non-residents, which contracted 8.4% compared to 2Q15, due to the lower demand for CETES by foreigners. In contrast, the balance of domestic financial savings expanded, increasing its growth rate from 4.4% in 1Q16 to 4.9% during 2Q16.

Regarding the use of financial resources, Banxico stresses that a decrease was seen in financing the public sector compared to the previous quarter, while lending to the private sector continued to expand, albeit at more moderate rates than during 1Q16 (6.8% vs 6.0%). Such moderation was the result of a slowdown in external financing. By debtor sector, it stresses that the domestic financing of companies ended the quarter with a real rate of annual growth of 9.1%, due to an expansion of bank credit, while the domestic debt market showed less activity. Delinquency rates in this segment also remained at relatively low levels, although the credit portfolio of development banks showed some signs of deterioration. Credit to households also continued its dynamism, growing 8.0% in 2Q16 vs 6.7% in 1Q16. The growth of the housing portfolio reflected increased lending both to commercial banks and from Infonavit. In the first case, historically low interest rates and low and stable delinquency rates are still being seen, while some deterioration was recorded in the Infonavit portfolio. Meanwhile, consumer credit granted by commercial banks grew in all

segments, with no significant changes in interest rates or delinquencies, excluding payroll credit, which showed some increase, although still at relatively low levels.

### **Mexico Bank indicators show the recovery of the credit card portfolio, although with less dynamism than other segments of consumer credit**

Bank of Mexico published the [Basic Indicators of Credit Cards](#), with information at the end of December 2015. Credit granted through this segment represented 41% of the total portfolio of consumer credit. In December 2015, this credit recorded a real increase of 2.7% over the same month in 2014, situating itself as the least dynamic segment within consumer credit, although showing a recovery with respect to the performance seen in 2014.

In December 2015, there were a total 16.7 million active cards, which were up to date with their payments, with a balance amounting to 274.7 thousand million pesos. The cardholders paying the total amount represented 47.3% of the number of cards and 24.5% of the balance, the highest numbers since card holder repayment behaviour has been recorded (Jun-09). Meanwhile, the weighted average effective interest rate per balance (TEPP) of the total portfolio in December 2015 was 23% (90 basis points less than in December 2014). It highlights the increased use of promotions of months without interest, as of December 2015, where 46.3% of cards were used to make purchases under this scheme.

### **More dynamic Personal Credit portfolio, with better financing conditions**

Bank of Mexico published the [Basic Indicators of Personal Loans](#), with information at the end of February 2016. In accordance with that report, between February 2014 and February 2016, the balance of these loans rose at an average annual real rate of 5.4%. At the end of February 2016, personal loans represented 19.8% of the total portfolio of consumer credit granted by regulated entities. This type of financing totalled 11.2 million loans, with a total balance of 183.6 thousand million pesos.

Loans granted between March 2015 and February 2016 accounted for 82.8% of the portfolio to February 2016 (indicating that many of these loans are for terms of less than one year), and their rate of average interest was 35.8%. This rate was 116 basis points lower than in the previous year. The average amount of a personal loan granted last year was 17.3 thousand pesos; this figure rose 7.5% in real terms between 2015 and 2016. As for the term of the loans, 43.2% of loans were granted last year for terms ranging between 12 and 18 months.

### **Bank of Mexico updates auto loan indicators**

Based on the [Basic Indicators of Automotive Credit](#) published by the Bank of Mexico at the end April 2016, the balance of this type of credit grew 14.2% over the same month last year, maintaining a stake of 10.9% in the total portfolio of consumer credit. Meanwhile, the delinquency rate was 1.4%, remaining the lowest among consumer loans. In April 2016, there were a total of 618,686 credits in force with a balance of 72,458 million pesos. Of these loans, 41% were awarded during last year (54.7% of the balance). The average amount of outstanding loans was 174,200 pesos, at an average term of 50 months, and a weighted average interest rate of 11.7%.

## **Financial markets**

### **Signs of a more accommodative stance lasting longer in developed countries favour financial markets during July**

During August, the markets' attention focused on oil prices and expectations about US monetary normalization in a context of low aversion to risk. The announcement of an extraordinary OPEC meeting during the second half of September, to again address the issue of a freeze on oil production, influenced price rises of around 17% during the first half of August. This led to Brent crude oil trading back above the \$50 per barrel mark. However, new inventory data, which was higher than expected in the United States,

reduced the price to \$47 per barrel at the end of the month. Influenced by the sharp price rise in the oil market during the first half of the month and by the absence of risk aversion, the Mexican peso rose 3.8%, the second highest rise among emerging currencies in that period, whereby the dollar traded up to 18.06 pesos per dollar. However, days later, some members of the FOMC stated that the market again assigned a very low probability to increases in the federal funds rate, which was reinforced by the speech of the president of the Federal Reserve in which she stressed that the possibility of an increase in the federal funds rate had strengthened in recent months. As a result, the odds of a rise of 25 basis points for the meetings in September and December in the futures market went from 15% to 44% and 38% to 45%, respectively. This pushed up the exchange rate, which closed the month at 18.78 pesos per dollar.

In equity markets, gains continued for emerging economies, while these were moderated for developed markets. The MSCI EM advanced an additional 2.3% in August, while the CPI had profits of 1.9%, which meant it reached a new historic maximum. Meanwhile the benchmark of global stocks fell 0.13% similar to that seen in the S&P500 that fell 0.12%, which did not prevent it also reaching a new record high by mid-month.

In the bond market, during the first eight months of the year the performance of Mbono 10-year averaged 6.01%, slightly higher than the observed average level in 2015 (5.94%), but marginally lower than that observed in the 4Q15 (6.10 %). In this average of 2016, what is highlighted is the downward trend despite persistent pressure on the peso and a more adverse context as far as the appetite of foreigners for Mexican bonds. Thus, while the rate of Mbono 10-year averaged 6.12% in 1Q16, during 2Q16, it decreased to 5.99% and recorded a further decline to 5.90% in the first two months of 3Q16. This downward trend occurred despite the increase of 100 basis points (bp) in the reference rate. While it is normal to expect a flattening of the yield curve from very accommodative levels when the policy rate increases, the flattening observed has not only obeyed the increase at the short end of the curve, but is also the result of the decreased interest rates at 10 years. At the end of January this year, i.e., before Banxico made its first 50 bp hike in the lending rate, the slope between the yield at 10 years and 1 year was 259 bp. At the end of August, and having observed the two increases in the policy rate made during 2016 (for a cumulative 100bp), the slope had decreased 128 bp. This reduction is explained mainly by the increase of 112 bp in the interest rate to 1 year, but also responds to the decrease of 19 bp in the rate to 10 years.

We believe that the positive trend in long-term rates in Mexico has been influenced primarily by two factors. First, the downward trend of long-term interest rates in the U.S., the 10-year Treasury Note (NT 10a) started the year at 2.2% and in two months of 3Q16 has averaged 1.53%, ranging between 1.4% and 1.6%, depending on the market expectations regarding Federal Reserve monetary policy. A second reason is the decline in bond issues in domestic currency that results in a slowdown in the rate of increase in the supply of bonds in the market, which puts upward pressure on prices thereof, i.e. downward pressure on interest rates. Anticipating that these two factors will present during the rest of the year, it is expected that long-term interest rates in Mexico remain low for the remainder of 2016. By 2017, significant increases will hardly be expected in long-term rates in the U.S., also the process of fiscal consolidation in which the federal government is already immersed will continue to limit the supply of long-term bonds. Thus, we are revising down our forecast for the 10-year Mbono interest rate from 6.3% to 5.85% for the end of 2016, and we now expect an increase of only 30 basis points in 2017.

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