Banks

# Monthly Report on Banking and the Financial System

Javier Amador / Fernando Balbuena / Alfonso Gurza / Iván Martínez / Nestor Matus / F. Javier Morales / Carlos Serrano / Mariana A. Torán / Sirenia Vázquez / Samuel Vázquez

## 1.1. Banking and the Financial System

### Lending to the private sector kept up its double-digit growth in April

In April 2018 the outstanding balance of credit granted by commercial banks to the private sector grew at a nominal annual rate of 10.7% (5.9% in real terms). This nominal rate was 0.4 pp less than that seen in the previous month (11.1%) and 5.2 pp less than that posted in April 2017 (15.9%). April's lower nominal growth rate in lending to the private sector compared with the previous month was due to the flagging momentum in consumer lending (7.9% in April as against 8.2% in March) and lending to businesses (14.2% compared with 14.5%), which the slightly-increased growth in housing loans (8.2% compared with 7.9%) was not enough to offset. On a year-on-year basis however, all components of lending to the private sector showed reduced dynamism in April, with growth in consumer lending down by 3.1 pp (7.9% as against 11.0%), in lending to businesses down by 4.5 pp (14.2% as against 18.7%) and in housing loans down by 2.4 pp (8.2% as against 10.6%). These figures show that in April 2018 the slowing in the growth rate of the outstanding balance of consumer credit was moderate relative to the previous month, but that compared with the same month of last year it was greater. The lower growth rate in lending to the private sector seen from October 2017 to April 2018 is largely due to the reduced dynamism of economic activity, as can be seen from the Global Index of Economic Activity (IGAE). For example, in the first nine months of 2017 the average rate of growth of the IGAE was 2.0%, whereas from October 2017 to March 2018 it was just 1.3%. This means that the slower growth rate of the sources that generate income was also reflected in a slower growth rate of all categories of lending to the private sector.

### The commercial banks' deposit gathering continues to be driven by sight deposits

In April 2018 traditional bank deposits (sight + term) posted nominal annual growth of 9.0% (4.2% in real terms).Growth in April was 1.6 pp less than in March (10.6%) and also 4.5 pp less than the rate seen in April 2017 (13.5%). Also, annual nominal growth rates for sight and term deposits were 7.6% and 11.2%, respectively. This growth, combined with the relative importance of each of these two types of deposits, meant that the contribution to the annual growth of 8.9 pp in traditional banking deposits was 4.7 pp for sight and 4.2 pp for term deposits. From January to April 2018 the growth in sight deposits slowed relative to the same period of 2017, from 14.3% in 2017 to 7.7% in 2018 in nominal annual average terms. Meanwhile, growth in term deposits showed greater average dynamism from January to April 2018 (13.2%) compared with the same period of 2017 (10.9%). The relatively poor performance of sight deposits so far this year might be reflecting the slower growth in the Global Index of Economic Activity (IGAE), which affected some of its components. The greater growth in term deposits in the first four months of 2018 may possibly be explained by the increase in bank interest rates.

## Balance of risks of the Financial System Stability Council (CESF)

On 14 June, the CESF updated the balance of risks for the financial system. According to its communiqué, the main risks in the external environment continue to be considered as:1) an accelerated process of normalisation of monetary policy by the US Federal Reserve and 2) escalation of protectionist trade measures, as well as the future of bilateral relations between Mexico and the US. On the domestic front, the volatility seen in the currency market was attributed to the uncertainty associated with the electoral process of July 1st

For the first time in its quarterly communiqués the CESF (Financial System Stability Council) included a comment on the risk of cyber-attacks on financial institutions and infrastructures, following the attacks reported in April and May 2018 on the working accounts of certain financial institutions linked to the Electronic Interbank Payments System (SPEI by its Spanish acronym). In this regard, the CESF stressed that to maintain financial stability, institutions must continue to invest in information security and comply with the measures determined by the financial authorities.

With this in mind, in May the financial authorities and the trade union associations of the financial institutions signed the "Bases of coordination in the area of security of information". These bases indicate that each financial entity is obliged to create an in-house group for detecting and responding to sensitive IT security incidents and must immediately report any such incidents to the competent authorities. The CESF also followed up on the actions being taken to strengthen regulation and supervision of cyber security, so as to be able to incorporate international best practices and recommendations. The members of the CESF agreed to push for the strengthening of IT security and to identify the supervision of regulations, with a view to safeguarding financial stability.

## Value of cars bought on credit shifted towards higher prices

Banco de México (Banxico) updated its report on automotive lending indicators with information to October 2017. At the end of that month, automotive lending granted by banks (12.1% of total consumer lending) was growing at 12.3% in real annual terms. Although between October 2016 and October 2017 car loans were the most dynamic form of consumer credit, the real growth rate was less than the figure of 13.8% reported in October 2016.The NPL rate for its part reached 1.6% in October 2017 and the adjusted NPL rate was 3.7%, both indicators showing increases relative to those observed the previous year (1.5% and 3.4% respectively in October 2016).

The report highlights the fact that between October 2011 and October 2017 the auto price index increased by 20.6%, and the distribution of the value of vehicles acquired on credit shifted towards higher prices, the majority being concentrated in a range of 125,000 to 350,000 pesos. As regards loans granted in the past year (between November 2016 and October 2017), the comparable portfolio[1] was 667,600 loans, with a balance of 117,900 million pesos and a weighted average interest rate of 12.6% (1.3% more than in the previous year). The average term of the loans granted during the past year was 52 months (one month more than in the previous year).

1: The report analyses the comparable portfolio of the automotive sector, which consists of loans to the public with uniform features (loans in force in October 2017, up to date with payments, for the purchase of vehicles for private use, in domestic currency), comparing them as regards the following elements: interest rate, amount, value of the car and term.

### The value of production of construction companies fell by 2.6% in the first four months of 2018

In April 2018 the output value generated by construction companies in real annualised terms fell by 2.6% relative to 2017. Building, which represented 48% of the total in that period, held steady, without advancing.

However, within the building sub-sector, the value of production for housing construction increased by 2.2%, which probably reflects the consolidation of the projects started during the second half of 2017. This is in line with the recovery in consumer confidence during the second half of last year and the continuing stability and attractiveness of mortgage interest rates.

The value of building of industrial premises and shopping centres for its part remains in negative territory, and in April it fell by 1.7% in real terms relative to the previous year based on annualised figures. Apart from this, the construction value of schools, clinics and hospitals accelerated during the first half of the year, in line with the seasonal behaviour of the budgetary closure for the end of the six-year period. However, these works account for less than 10% of all building, so they do not constitute significant accelerator in the industry.

## 1.2. Financial Markets

### Reduced concerns about global trade tensions give respite to domestic assets in the second half of June

The escalation of trade tensions, mainly between China and the US, were the main factor behind the movements in the financial markets. During the first two weeks of June, the US announcement of tariffs to be imposed on several products from China, and China's retaliation in kind led to a bout of risk aversion which strengthened the dollar. However, in the last few days of June, the markets weighed the limited effects that these measures might have on growth, at least for the time being. This, the expectation that the level of tension will not increase further, and the better-than-expected figures for the US economy all combined to bring about a reduction in risk aversion.

In June the Mexican peso depreciated by 0.92%, the dollar ending the month above 19.91 pesos, after peaking at 20.9 in mid-month. We should point out that the appreciation during the second half of the month was also influenced by the incorporation into prices of an electoral scenario with a clear winner as indicated by the polls. The peso's depreciation during the month was less than the 2.95% fall in the EM currency benchmark, and less than the 0.43% that developed countries' currencies lost against the dollar.

In the fixed income market, the yield to maturity on the ten-year Mbono bonds decreased by 16 basis points (bps) during June to 7.62% at month-end, after peaking at 8.0% on 15 June. This reduction was influenced by the fall of nearly 20 bps in the CDS spread in the second half of the month, after it had surpassed 150 bps. Yield to maturity on Treasuries at the same term increased by 1 bp, reflecting the predominant role of the reduction in risk aversion in the second half of the month. In equity markets, the 6.6% rise in Mexico's IPyC stock exchange stood out in a context of generalised losses. In fact, globally equity markets lost 0.53% and emerging markets lost 3.88%.

In short, the vicissitudes of financial markets' perception of the escalation of global tensions, combined with expectations of an orderly electoral process without surprises allowed races of domestic assets to recover.

## 1.3. Regulation

### Adjustments to the calendar for the capital stress tests

On 26 June the CNBV (National Banking and Securities Commission) amended the "Single Banking Circular", making the procedure for submitting information and results of stress tests under supervisors' and own scenarios more flexible. Previously it had been established that the CNBV would send institutions the calendar for submitting this information and results in June each year; now the Commission will publish the calendar on its website in January, also establishing the date from which projections must be made. For 2018 it establishes that institutions will use the supervisor scenarios officially sent to them by the CNBV in September of the same year and submit results within the deadlines established in that communication.