

Mexico Real Estate Flash

The construction guarantee program: Is this what is needed?

The government has announced a housing construction support plan through a guarantees program geared towards promoting bank financing for this activity. Although the intentions are good, further details are needed to put it in perspective and assess the impact it might have on financing. It would also be advisable for the program to go hand in hand with policies for fostering individual mortgage lending which have to be implemented to comply with the National Housing Policy (PNV).

Yesterday, the federal government announced a guarantees program to support home construction, which will be channeled through the SHF (Federal Mortgage Society). The goal of this program, which has a budget of 15 billion pesos, is to create incentives for the banking sector and other financial intermediaries to grant credits for construction, by means of a first loss guarantees program, up to 50% of the lending portfolio granted in 2012. Obviously, with this program the government seeks to rekindle financing for construction which has been registered in recent years. More details are required concerning the working of the program, although on a preliminary basis the following remarks can be made:

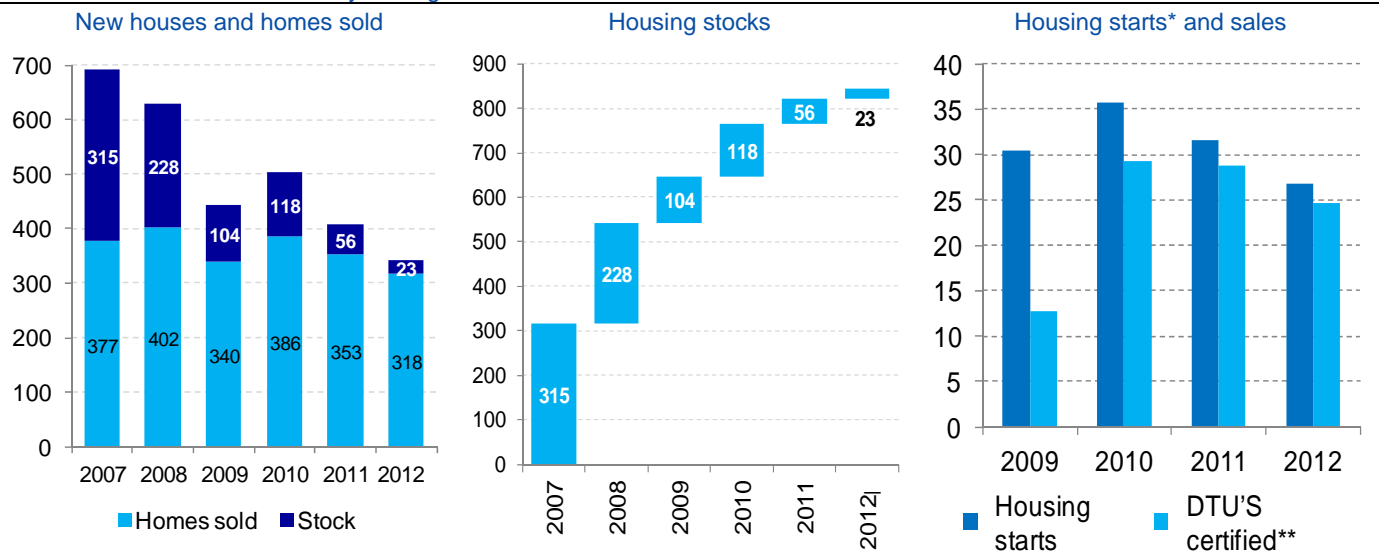
- There has recently been a downward trend in home construction, due to several factors. First, lower activity by public housing institutions (mortgage loans placed by Infonavit and Fovissste went from 584 thousand to 490 thousand between 2008 and 2012). Second, more diversification in the loans offered by Infonavit (in 2012, refurbishment loans accounted for 26% of the total placed by the institution). And also a higher proportion of second-hand homes (rising from 17% to 35% in the case of Infonavit, between 2007 and 2012). Lastly, accumulated housing stocks, both due to excess home construction in previous years and the impact of the crisis in 2009 (accumulated stocks in the region of 840 thousand homes between 2007 and 2012). None of these factors is associated with the lack of financing for construction.
- How effective will the program be? This will depend on its capacity to sufficiently improve the profile of new home construction projects, so that they can be adjusted to required demand. The question is: Does guaranteeing the credit granted in 2012 make the projects for 2013 more appealing? The financial viability of the projects largely depends on their foundations in terms of studies of demand, costs structure and return. The latter two factors ultimately hinge on construction companies' own experience and capacity. Another way of looking at the problem is to ask whether the guarantees program could actually make the credit granting process more lax, and encourage financial institutions to take excessive risks in projects which do not necessarily comply with the general objective of the National Housing Policy, where decent and proper housing goes hand in hand with urban development.
- Details are not yet known regarding rules on how resources are applied. For example, if they apply to any project, or only for those in urban areas, if they can be horizontal housing projects or only vertical ones, or if the type of home must have minimum attributes in terms of habitable space, finishes and facilities. Details to be defined must also take into account incentives offered in order

for the financing of new projects to be in keeping with the goal of adapting to a sustainable urban development model, and preventing territorial reserves being used as the central basis for new projects. The government has sought these goals in the National Housing Policy and it would be advisable for it to give priority to projects with these characteristics.

- The fall in construction activity is largely due to demand factors, which means that the announced program may not be effective at resolving the structural problem. Financing has fallen because there has been a slump in demand due to the type of home built by the largest developers, homes which are not entirely in line with the population's actual needs. In this regard, this program would be effective if it went hand in hand with announcements which could clarify Infonavit's and Fovissste's policies for granting individual loans in the years to come. In fact, were such announcements made then the granting of the guarantees presented yesterday might prove to be unnecessary, as it would create an incentive for projects to focus on specific demand requirements.
- The question also has to be asked if in fact incentives for construction are required when housing stocks in Mexico continue to grow; or if it would be better to stimulate demand, either by making existing stocks more attractive through the urban infrastructure and services provided, or with new construction projects focused on the population's specific needs.
- Lastly, it would be appropriate to bring this program in line with the policies established in the National Housing Policy in such a way that the guarantees are used to promote the construction of homes in keeping with the urban development plans included in the aforesaid plan.

Housing stock formation

Thousands of homes and monthly average



Source: BBVA Research with Single Housing Register data

* Total homes registered in the Single Housing Register from the start of process until sale

** Approximate measure of sales: assumes that the construction company finishes the home when a buyer is available.

In short, the construction financing guarantees program announced yesterday shows that the government is interested in supporting the sector. In our opinion, however, it would be advisable for the program to be brought in line with the urban development plans set out in the National Housing Policy and for it to go hand in hand with clear medium term policies concerning the granting of mortgages by Infonavit and Fovissste.

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