Mexico Development Bank Lending Rises Following Financial Reforms

By Michael Perez

There are indications that Mexico's financial reforms are working. The loan portfolios of the nation's six development banks increased 28 percent in the 18 months following the reforms' initiation in January 2014.

Mexico's development banks are publicly owned institutions serving economic sectors not generally reached by commercial banks (*Table 1*). The big banks' relatively high collateral requirements and stringent screening mechanisms exclude many potential customers.

Extending more credit signals an important strategic shift. The development banks have traditionally maintained a low-risk appetite, with restrictions on short- and medium-term loan issuance. The new regulations direct the development banks to more actively expand credit by mandating that they more aggressively serve their target markets. Examples include increased lending to small- and medium-sized enterprises and low-income households.

Development banks also now have options to help struggling firms. They can make multiple loans to the same borrower without finance ministry permission and may assume more risk and incur losses so long as their equity and reserves are not depleted. Lending can be based on pledged collateral, and the development banks' increasing asset base allows them to offer more backstops for commercial bank loans to small and medium enterprises.

Total assets for the six development banks reached U.S. $88 billion in August 2015, equal to one-fifth the size of commercial banks. That figure reflects a 16 percent increase in assets since the reforms were signed. The growth, however, has not been uniform across each loan type or development bank (*Chart 1*). Payroll loans financed by Bansefi and Banjercito have driven consumer lending growth. Bancomext and Nafin increased their business loan portfolios, with commercial loans making up the bulk of development bank lending.

Table 1 Mexico's Development Banks Target Specific Markets

Bank name	Specialization
Nacional Financiera (Nafin)	Small-, medium-sized businesses
Banco Nacional de Obras y Servicos Públicos (Banobras)	Public infrastructure, municipal projects
Banco Nacional de Comercio Exterior (Bancomext)	Export and import financing
Banco Nacional del Ejército (Banjercito)	Armed forces
Banco del Ahorro y Servicios Financieros (Bansefi)	Lower-income households, the unbanked
Sociedad Hipotecaria Federal (SHF)	Housing, housing development

SOURCE: Comisión Nacional Bancaria y de Valores (National Banking and Securities Commission).

Stagnant homebuilding has limited SHF's mortgage lending activity. A government initiative, backed by a $25 billion appropriation, seeks to stimulate home construction and could improve the outlook.

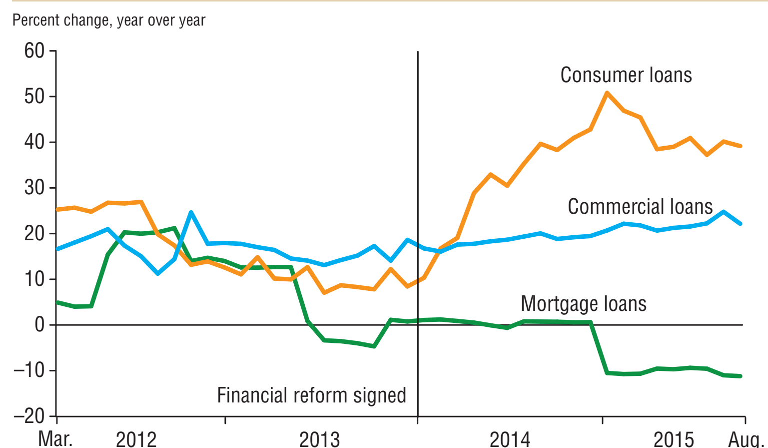
Greater credit accessibility is a key objective of the reforms.[1] Mexico's ratio of credit to gross domestic product stood at 31 percent as of year-end 2014, well below Latin American counterparts Brazil (69 percent) and Chile (109 percent). Furthermore, small- and medium-sized enterprises receive only 4 percent of business loans while providing the great majority of jobs in Mexico. The reforms mitigate these issues by expanding banking competition and improving loan guarantees.

While it is too soon to pronounce the financial reform effort complete, it has reshaped lending strategies of Mexico's development banks. A focus on providing individuals and businesses access to essential financial resources will bring banking to more households and firms. Similarly, increased development bank participation will provide more formal finance to small businesses, better helping them serve as engines of growth.

Note

[1] More information on the financial reforms can be found at: www.dallasfed.org/assets/documents/research/swe/2014/swe1403d.pdf.

Chart 1 Development Bank Loan Portfolio Grows After Reforms



SOURCE: Comisión Nacional Bancaria y de Valores (National Banking and Securities Commission).