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FEATURED Q&A

What Is the Outlook for Mexico's Banking Sector?

Q Citigroup's chief executive officer, Michael Corbat announced last month that the New York-based financial services company will invest $1.5 billion in its Mexican unit, Banamex, over the next four years and also increase loans to small- and medium-sized businesses as well as to the energy sector by a combined $14 billion. Over the next few years, what is the growth potential for foreign and domestic banks operating in Mexico? Which segments of banks' businesses in Mexico will experience the most growth? How will President Enrique Peña Nieto's financial sector reforms affect the sector?

A Alejandro Garcia, senior director for Latin America Financial Institutions at Fitch Ratings: "Fitch expects that lending growth in Mexico will speed up in 2015 and thereafter, driven by sound investment prospects in the infrastructure and energy sectors, and also aided by the expected economic recovery. Fitch believes that loan growth could resume to roughly 15 percent annually, after recording one-digit annual growth rates in 2012 and 2013. Fitch expects that investment projects will benefit both global and local banks. However, the positive effects could be larger for foreign participants, given their better capacity to provide funding alternatives for infrastructure and energy projects, which will likely require specialization, sizable amounts and long tenors. However, local banks should also benefit broadly from the spillover effect of such investments and the potentially improved economic environment. In Fitch's opinion, corporate and commercial lending will resume quicker and at a faster pace due to strong investment prospects, benefiting banks with strong franchises on these segments. However, the improved economic environment and the planned investments should also benefit smaller businesses and the retail sector, although this is more likely to occur gradually. Fitch believes that the ben-

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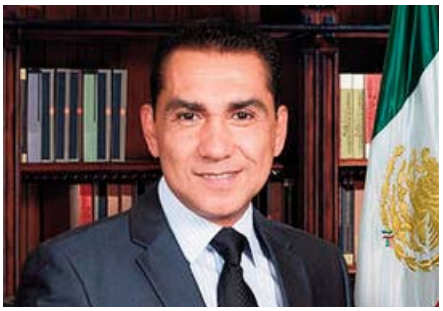

Mexican Mayor, Wife Sought in Students' Disappearance

Iguala Mayor José Luis Abarca and his wife, María de los Ángeles Pineda, are the "probable masterminds" behind the disappearance of 43 students last month in the town, Mexico's attorney general said Wednesday. See story on page 2.

File Photo: Mexican Government.

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NEWS BRIEFS

Colombia to Remove Panama From Tax Haven List

Colombia's government said Wednesday that it will remove Panama from its list of tax havens after the two countries reached an agreement for Panama to help fight tax evasion, according to Colombia Reports. The neighboring countries said they would sign an agreement to cooperate on exchanging tax information.

Toyota Still Miles Away From Building a Factory in Mexico

Toyota Motor Corp. is considering whether to build a factory in Mexico, but top management is not close to approving the move, Steve St. Angelo, the head of Toyota's Latin America unit, told reporters on Tuesday, Bloomberg News reported. "There is a team studying it, but I'll be honest with you, it's still far from being an approved project," the executive said. Toyota is the only major carmaker to not have a high-volume assembly plant in Mexico, where low labor costs and free-trade agreements have attracted other carmakers.

Chile Eyes Streamlined Permit Process for Mines

Chile's mining minister, Aurora Williams, said this week that the ministry is looking to streamline the mine permit process, Reuters reported. "The ongoing revision is going to highlight some aspects that need to be improved," Williams said, adding that the process should be complete early next year. Mining is a key driver of Chile's economic growth, but many projects have been halted or delayed due to red tape or community opposition, and President Michelle Bachelet recently called for a 60-day review of Chile's permitting processes.

Political News

Mexican Mayor, Wife Accused in Students' Disappearance

The mayor of the Mexican town of Iguala and his wife are the "probable masterminds" behind the disappearance of 43 students who went missing last month in the town after being detained by police, Mexico's attorney general said Wednesday, Reuters reported. According to testimony from local police officers, Mayor José Luis Abarca had told police to intercept the students to prevent them from disrupting an event in which the mayor's wife, María de los Ángeles Pineda, was giving a report to local officials about a social services program that she heads, said Attorney General Jesús Murillo Karam, BBC News reported. The mayor requested a leave of absence after the incident on Sept. 26, and neither he nor his wife have been seen since. They are both considered fugitives. Warrants have been issued for their arrests as well as the arrest of Iguala's police chief, Felipe Flores. The students, from a teachers' training college in the nearby town of Ayotzinapa, had gone to Iguala to demonstrate against what they contended were discriminatory hiring practices and also to collect money for their school. The college has a history of leftist activism, and Abarca had been maddened by a previous protest by students from the college, BBC News reported. Six people were killed in clashes between police and the students around the time of the incident last month, and the 43 students who went missing were last seen being herded into police cars. Authorities so far have arrested 52 people in connection with the matter, including dozens of police officers who are believed to have ties to the local Guerreros Unidos gang, Reuters reported. The gang's reputed leader, Sidronio Casarrubias, was arrested last week. Murillo Karam said Wednesday that Casarrubias had told prosecutors that the mayor and his wife had ordered police to intercept the students. The local police turned the students over to the gang, said Murillo Karam. Casarrubias also accused Pineda of being "the main operator of criminal activities in Iguala," Murillo Karam added. The attorney general also said Casarrubias ordered the students' disappearance after he received word from one of his men that the students were part of a rival gang, BBC News reported. The students were taken to Pueblo Viejo, where several mass graves have been found, Murillo Karam said. Forensic tests determined that the bodies in the mass graves were not those of the students, but those tests "may have been flawed," said Murillo Karam.

Murillo Karam

File Photo: Mexican Government.

Economic News

Brazil's Jobless Rate Declines to Record Low for September

Brazil's unemployment rate fell last month to 4.9 percent from 5 percent in August, marking a record-low unemployment rate for September, the country's national statistics agency announced today, Bloomberg News reported. The decline is good news for President Dilma Rousseff, who is fighting for re-election. She faces off in Sunday's runoff election against Senator Aécio Neves, and polls have shown the two candidates are in a dead heat. Rousseff has urged Brazilians to recognize the role her Workers' Party has played in preserving jobs and has said Neves would reverse that trend. Neves has blamed Rousseff's policies for above-target inflation and an economic recession. Brazil's annual rate of inflation stood at 6.62 percent through mid-October, higher than the 6.5 percent upper limit of the

Brazil's annual rate of inflation stood at 6.62 percent through mid-October.

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central bank's target. The central bank has kept the benchmark Selic interest rate at 11 percent for three consecutive meetings after boosting it by 3.75 percentage points in the 12-month period through April. The economy slipped into a recession in the second quarter as gross domestic product shrank 0.6 percent. The contraction followed a revised decline in GDP of 0.2 percent in the first quarter. Job creation has also slowed. Latin America's largest economy created 730,124 government-registered jobs this year through September, as compared to 1.04 million in the same period last year, Labor Minister Manoel Dias announced last week.

Company News

Britain Offers as Much as $1 Billion in Loans, Guarantees to Codelco

Britain on Wednesday offered Chile's state-owned **Codelco** as much as $1 billion in loans and guarantees in order to support British companies' deals with the world's largest copper producer, Reuters reported. Deals that could be backed by the loans and guarantees include initiatives for new infrastructure, mining equipment and financial investments. "It strikes me that Chile is a natural partner for us in the U.K.," said David Godfrey, the head of the government's U.K. Export Finance department. Godfrey presented a document detailing the potential line of credit to Aurora Williams, the Chilean minister of mines, at an event in London during London Metal Exchange Week. In order to reverse declining production and upgrade its mines, Codelco needs approximately $30 billion, Reuters reported. The company's chairman told the wire service on Monday that Codelco would announce the results of a project review within months.

Godfrey

File Photo: British Chambers of Commerce.

Featured Q&A

Continued from page 1

efits of the financial reform will be material only over the medium term. In the near future, loan growth is mostly driven by the pace of economic growth. Lending could accelerate in the short term if development banks provide larger and more flexible funding alternatives, but longer term prospects depend on increasing per capita GDP and reducing informality."

A Nicolás Mariscal, chairman of Grupo Marhnos in Mexico City: "Mexico is a country with macroeconomic stability and is very attractive to banks because of its growth potential and its juicy rates of return on equity (ROE), which on average are 14 percent (though depending on the niche could reach levels of 30, 40 or even 70 percent). The average ROE in other regions is 8.2 percent for Europe, 8.8 percent for North America, 16 percent for Asia-Pacific and 17.2 percent for Latin America. And while the seven largest banks in the Mexican banking system account for 88 percent of the profits, the size of the market and the potential for bringing more people into the banking system as well as the opportunity to diversify into various niches also gives other players the opportunity to be winners. Banks in Mexico lend an amount equivalent to 26 percent of the country's GDP, while the amount banks lend in Argentina and Brazil is equal to about 50 percent of their countries' GDP. The financial reform, approved in January, encourages lending with better conditions for consumers and increases competitiveness. Along with the new legal framework, development banks have a more important role to play alongside commercial banks in order to achieve financial inclusion. This is because there are still millions of Mexicans who do not have access to credit or don't have a formal savings account. I believe that there and in financing for small- and medium-sized enterprises is where there is most opportunity."

> "The financial reform, approved in January, encourages lending with better conditions for consumers and increases competitiveness."
>
> — *Nicolás Mariscal*

A Tapen Sinha, professor of risk management at the Instituto Tecnológico Autónomo de México: "The World Bank's Global Findex database shows that less than 30 percent of Mexican households have bank accounts. This contrasts sharply with regional leaders like Brazil or Chile, both of which have nearly double the proportion of households with bank accounts. Countries with much lower per capita income, such as Bolivia or Ecuador, have more households with bank accounts. The two largest banks in Mexico, BBVA Bancomer and Banamex, have 2,000 branches each, whereas HSBC, Banorte and Santander have half of that. In Brazil, Banco Popular do Brasil specifically targets low-income households that prefer cash transactions. In Mexico, there is no such institution. Research from other countries shows that reducing fixed costs of opening and operating bank accounts increases the take up rate substantially in poorly banked parts of a country. In Mexico, instead of reducing those costs, we are observing their rise. The Internet transfer of money costs 20 pesos, yet getting a check certified costs 10 times that. In other words, the rich can do transactions more cheaply than the poor in Mexico. What will the efforts by Banamex do? They will increase the monopoly power the bank already has. I suspect most of their increased interest is not so much to boost lending to small- and medium-sized businesses, but rather to take advantage of the Citibank connection to get oil-related transactions, which will definitely be dominated by large busi-

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Featured Q&A

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nesses, not small ones. Already, 80 percent of Mexican banks have foreign ownership. These actions will certainly not reduce that."

Adalberto Palma Gómez, senior partner at Aperture S.C. in Mexico City: "Several structural economic reforms approved by Mexico's Congress have generated optimistic expectations for the development of projects for which, it is assumed, financial activity will be required. Along with officially announced infrastructure programs, there is a scenario for financing needs in areas such as energy, telecommunications and other large infrastructure projects. By their nature, the execution of such projects must focus primarily on large companies in the productive sector and, on a more limited and selective basis, medium-sized companies. The financing needs of the projects that the government's reforms and infrastructure works require transcend the current capacity of the local banking system. The small group of banks (with foreign capital) that are concentrated in the Mexican market could partially participate in meeting these requirements. However, a substantial portion will have to be satisfied with transnational bank financing. The financial reform enacted by Congress aims to reduce the high levels of concentration that prevail in the sector and also to promote the extension of credit—in particular, credit that is geared toward small- and medium-sized enterprises (SMEs). For such goals to be achieved, the effective development of competitive conditions for the participation of small- and medium-sized financial institutions, which mainly operate with local capital, need to be implemented. These financial institutions face competitive disadvantages that restrict the deployment of their potential (such as the absence of regulations applicable to their business models). There is a real danger that the objectives of 'de-concentration' and increased credit offering to SMEs may be jeopardized in favor of further concentration in the entities identified in the financial reform."

The Advisor *welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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