



Financiera Rural

FINANCING RURAL INNOVATION

**Enrique De la Madrid Cordero
General Director**

March 22, 2007, Cáceres, Extremadura (Spain)



I. Overview of the Rural Sector in Mexico

II. Rural Financing and the Role of Financiera Rural

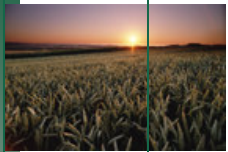
III. Key Products and Programs

IV. Challenges Ahead

OVERVIEW

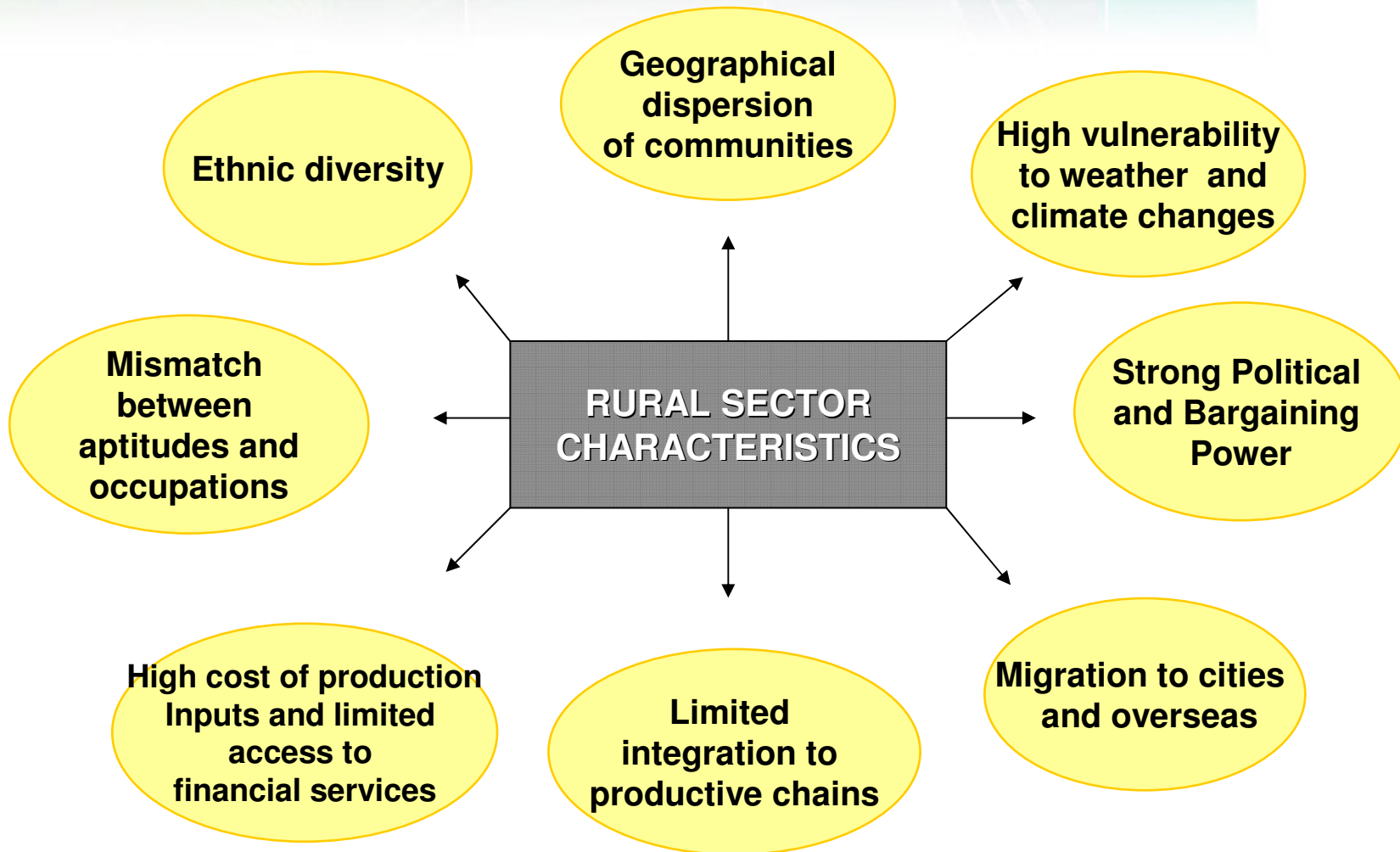
Mexico's Rural Sector

- In 2005, 24 percent of Mexico's population lived in rural areas.
- Agriculture, forestry, fishing and agribusiness sectors contributed to 3.5% of Mexico's GDP in 2005.
- Population in rural areas is aging faster than the urban population, due mainly to migration of labor force to cities and overseas:
- Poverty in the rural sector is large:
 - 57% of the population is poor (vs 41% in urban areas)
 - 28% of the population is extremely poor (versus 11% in urban areas), with large variations between the rural north and rural south.
- The average number of years of formal education of the rural population is 4.8 years, versus 9.7 years of urban population.



OVERVIEW

Mexico's Rural Sector



Agriculture Land in Mexico

Ejidos or social land represent more than 50% of the Mexican territory;

Some Ejido characteristics are:

- Average age of ejido's owners is 51.4 years;
- Ejidatarios use their crop land mainly for the production of maize (61.2%), beans (17.4%) or both (10.4%).
- The average ejido is 9.5 hectares;
- Most ejidatarios and private owners own less than 5 hectares;

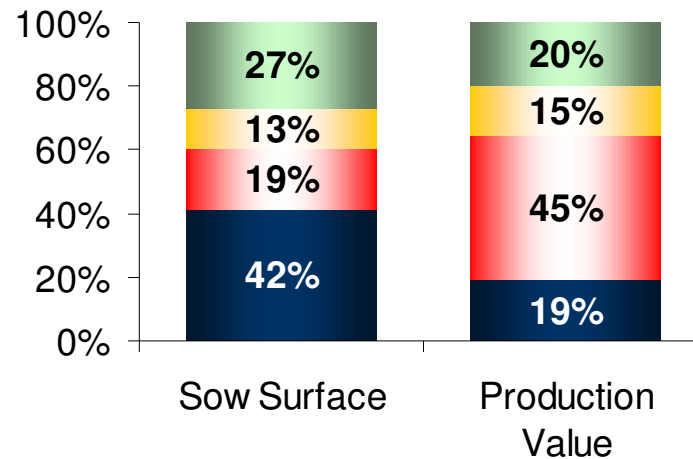


Agriculture Land in Mexico

- The participation of cereals (mainly maize) on the sow surface between 2001 and 2005 averaged 42%, but the participation in the production value averaged only 19% for the same period.
- On the other hand, fruits and vegetables with only 19% of the sow surface, have an average participation in production value of 45% for that period.



Participation on Total Production Value and Sow Surface



■ Cereales ■ Fruits and Vegetables
■ Industrial and oil seeds ■ Others



II. Rural Financing and the Role of Financiera Rural

RURAL FINANCING

Key Issues

- In the past years, private commercial banks have reduced their loan portfolio in the rural sector due to:
 - Limited number of branches in rural areas
 - high default rates in the past
 - difficulties to recover credit
 - small size of loans
- Informal lenders provide credit to rural producers. However, this type of credit is expensive and short term.
- Due to existing risks, development banks and agencies have an important role to play in the rural sector by mitigating risks and establishing incentives for private financial institutions to serve this segment of the market.

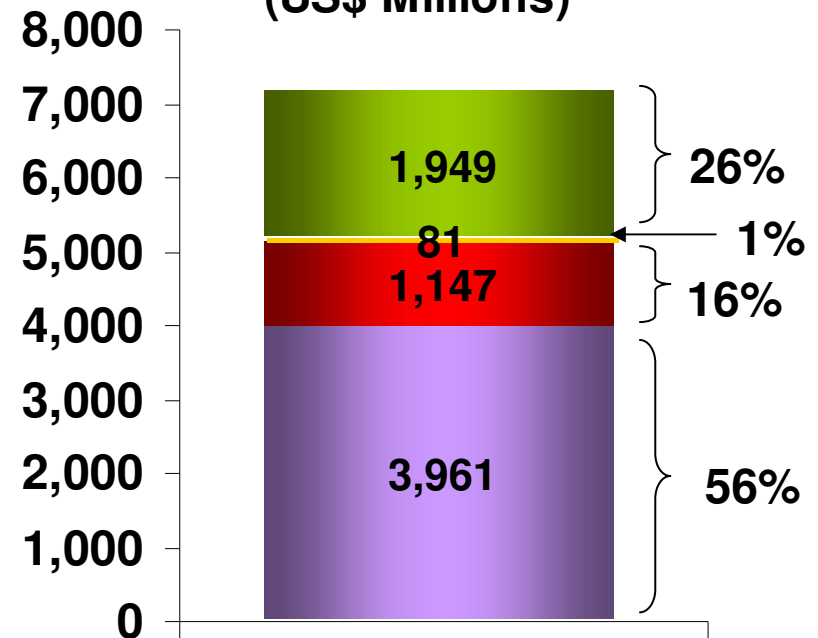
OVERVIEW

The Mexican Rural Financial Gap

- \$7,137 million dollars of credit were granted to the rural sector by public institutions and commercial banks.
- This resources represent only 25% of Agriculture, Livestock, Silviculture and Fishing GDP.



Formal Sources of Rural Financing (US\$ Millions)



2006

- FIRA
- Financiera Rural
- Development Banks
- Commercial Banks

Banrural (1975 – 2003)

- Development bank focused on agricultural activities
- Funding through “unlimited” access to loans from the Federal Government
- Highly vulnerable to political pressures to lend
- Inefficient cost structure; operating costs over 100% of operating income

Financiera Rural (2003 →)

- New Development Agency focuses on rural productive projects
 - Legally banned from taking deposits, loans or market funding. It must maintain endowment value over time to sustain operations
 - Operates with credit processes that apply international best practices. It has spread payment culture among clients
 - Efficient cost structure
-
- 29% of Non-Performing Loans (average 1991-2002)
 - 2.88% Average of Non-performing loans (2003 – 2006)



FINANCIERA RURAL

Mission and Vision

MEXICAN GOVERNMENT

Structural Transformation of Rural Credit

Bank Operations

Supports any productive activity in the rural area

- Agriculture
- Livestock
- Forestry
- Fishing
- Tourism
- Commerce

Creation of a Rural Financial System

Development Agency

FR

Supports the creation and consolidation of Rural Financial Institutions

- Financial Resources
- Training and Advisory Services
- Technical Assistance

Implementation of multiple government programs

- Guarantees
- Access to Finance
- Etc.

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Credit Allocation by Sector

- Agriculture represents 55% of FR's lending portfolio, and accounts for almost 80% of the number of loans.
- Clearly, in the medium term, FR needs to diversify to other sectors in the rural areas, such as forestry, fishing, tourism, and increase the participation of livestock in the lending portfolio.



2006 FR Credit Allocation by Sector (US\$ Millions)				
Sector	Num. Of Loans	% of Total	Value	% of Total
Agriculture	46,280	79.0%	680	54.5%
Livestock	7,930	13.5%	173	13.8%
Services	1,029	1.8%	133	10.7%
Comercial	1,937	3.3%	131	10.5%
Other	1,402	2.4%	130	10.4%
TOTAL	58,578	100.0%	\$ 1,247	99.9%



III. Key Products and Programs

FR PRODUCTS & PROGRAMS

Types of Credit

- Inventory Credits (Depository Receipts). (Prendario)
- Mid-term loans (for any purpose). (Simple)
- Working capital. (Avío)
- Long-term, asset-backed loans. (Refaccionario)
- Factoring (Factoraje)

Sector-Specific Programs

- Procampo (government guaranteed)
- Preauthorized credit lines for specific products
- Agroindustry providers
- Microcredit
- Credit Unions
- Other financial intermediaries
- Specific product programs: sugar cane, rice, cotton
- Regional programs

- In 2006, Financiera Rural disbursed \$1,247 million dollars;
- 42% of loans were originated via other financial intermediaries and associations of producers.
- Since it initiated operations, FR has granted nearly 350,000 credits, reaching 15% of total rural financing in Mexico.

CREDIT INNOVATIONS

Example of Innovative Programs

In the past, several second-tier programs implemented by development banks have failed due to the abuse of clients, inadequate regulatory and supervisory framework, and poor risk management.

A new generation of second tier programs aims to develop and consolidate RFIs by putting resources in the hands of rural sector producers, based on the principle of joint responsibility (risk-sharing) and recognizing that organized producers:

- Have a better and broader outreach than Financiera Rural' credit agencies;
- Have formal and informal credit intermediation experience;
- Are able to effectively evaluate and collect credits;
- Could become RFIs.

CREDIT INNOVATIONS

Second Tier Programs

- Through its second tier credit programs Financiera Rural:
 - Allocated during 2006 more than 42% of all its loan amounts,
- Some of the most successful second tier programs are the ones designed for:
 - Credit Unions,
 - Microfinance Institutions,
 - Disbursing Entities, and
 - Cotton, Rice and Sugar Cane producers.





IV. Challenges Ahead

CHALLENGES AHEAD

- Incentivate the entry of more private financial intermediaries into the rural sector
- Improve coordination with other development banks and government agencies at federal and state levels.
- Contribute to the formulation and implementation of a long term government strategy for the development of the rural sector
- Provide strategic information and knowledge to small producers to help them obtain more value-added for their production
- Help small producers face the transition to open and liberalized agriculture markets



CHALLENGES AHEAD

- Serve our client base through better products and services, maintaining the value of FR's endowment over time, through self-sufficient operations
- Increase total financing to rural sector
- Continue to strengthen the rural financial system in order to gradually pull out of the first-tier.
- Diversify client base into non-agricultural activities.
- Find alternative liquidity sources (loan securitization).





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