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The actual design of the financial system in Mexico is the outcome of a series of financial reforms adopted after the 1994 crisis. After the so called “Tequila Crisis”, financial authorities adopted a series of measures to develop a sound and solvent financial system.

By the end of 2000, the banking sector offered low diversification of financial services and products. In addition, these were rigid and costly and therefore, hindered the population’s access for them.
The period between 2001 - 2006 was characterized by a stable macroeconomic environment, mainly attributable to adequate fiscal and monetary policies. This situation allowed the strengthening of the regulatory and supervisory framework to foster financing to the private sector.

Capital adequacy continued evolving favorably during this period. By the end of 2006, the banking sector Total capital ratio averaged 16.1%.

The entrance of new competitors to the banking system promoted competition in the sector.

The adoption of adequate credit underwriting rules contributed to effective risk management practices at banking institutions. The result was an increased in the quality of the credit portfolio.

Since 2000, policy attention turned toward issues of competition and access, while maintaining solvency levels.
The reforms implemented during 2000 – 2006 represented significant strides in strengthening the institutional framework for financial oversight and allowed the resilience of the financial system in spite of the shocks of the crisis.

As of October 2010, the capital ratio of the commercial banking sector more than doubled the international standard of 8.0 percent, and the tier 1 ratio was 14 percent.

Non-performing loans are covered by more than 200% and the level of non-performing loans has decreased over the past years.
During the crisis, the financial system was exposed to volatility effects in the foreign exchange, stock market and interest rates. To avoid a contagion to the financial system, the authorities addressed a series of policy measures to contain spillover effects.

Partly due to the enhanced regulatory framework and partly due to the strength of the financial system coming into the crisis, Mexico weathered the recent financial crisis relatively well.
The financial system did experience a material worsening in asset quality and some pressures on bank funding and market liquidity, however these pressures were overall manageable with comparatively modest public support.

Deterioration in the assets quality of the consumer loans portfolio began before the crisis and was attributable to the efforts carried out by banks to deepen credit to the population.

The regulatory and supervisory framework allowed the banking system to remain sound and solvent in spite of the spillover effects of the global crisis.
It was identified the need to count with inter-agency coordination arrangements to monitor and assess system-wide risks and strengthen macro prudential regulation.

On July 28, the President of Mexico signed the decree for the establishment of the Financial System Stability Council. The Council is led by the Minister of Finance and includes the heads of the Bank of Mexico, the CNBV, the CNSF, the CONSAR, and the IPAB.
Within the international financial regulatory agenda there are other major reforms in progress. These are aimed to enhance the financial regulation and supervision of the financial infrastructure.

- Expanded perimeter of regulation
  - OTC Derivatives
  - Credit rating Agencies
  - Hedge Funds
  - Definition of the regulation for other financial intermediaries

- International cooperation
  - Cross-border crisis management
  - Information Exchange
  - Supervisory Colleges
  - Anti Money Laundering Mechanisms
  - Financial System Vulnerability Assessments
  - Expanded membership of international standard setting bodies
  - Macro-prudential supervisory and regulatory framework
  - Enhanced definition of the regulatory capital
  - Liquidity Standards
  - Leverage Standards
  - Allowances for credit risks
  - International Accounting Standards

Measures addressed to promote financial competition and product innovation

International standards for prudential regulation
As in other countries, the crisis experience underscored the need for a more systemic perspective. It also led to a broad rethinking of some of the key ingredients of financial regulation and resulted in new approaches to address the challenges brought to light by the crisis.

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| Prudential regulation oversight of capital, liquidity and leverage | **Capital:**  
  – Overall, the proposals for strengthening the global capital framework will not have a significant impact in the region since major Latin American banks count with a solid base of capital.  
  – Some of the components of the regulatory framework are already considered in Mexico.  
  – The banking system has a sound capital base. As of October 2010, Total Capital Ratio of the banking system averaged 17.4%.  

  **Liquidity:**  
  – There are some areas of concern for the establishment of liquidity standards.  
  – There is a need to adopt a framework for liquidity risk management, however, is essential to deeper assess the impact of this specific rule and the proposed parameters.  
  – The requirement to comply with a longer term liquidity ratio (stable deposit structure) may lead to market distortions, as some banking business models are funded by wholesale deposits or holding resources. |
From the view of the Mexican financial system, the most important concern refers to the treatment of SIFIs and G-SIFIs.

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| Systemically important financial institutions (SIFIs) | *Systemically important financial institutions (SIFIs)*
| • There is a practical difficulty involved on measuring the systemic importance of a banking institution as there exist a number of elements correlated to their potential risks of failing and that would hinder an agreement for measuring the systemic importance of a banking institution, as such is the case of a bank’s degree of interconnectedness. | |
| • In spite of some established parameters, there is not a clear consensus of the definition of a what involves to be systemic. | |
| • The impact to impose a surcharge capital for Global SIFIs is particularly relevant for the Latin-American region where major international players have a dominant presence. | |
| • The capital raised would be available for the holding firm in case it is needed. On the contrary, the holding would not have a legal obligation to support its subsidiary when insolvent. Therefore, the proposal to impose higher loss absorbency capacity will promote market distortions as regulatory costs would be distributed among subsidiaries, notwithstanding, the capital would not be available for them. | |
| • The effect for this proposal would result on a disequilibrium between national and foreign capital owned banks, as a result of the increased cost of capital for foreign banks. Were this measure approved, there will be an uneven playing field in local markets with foreign institutions reducing their activity. | |
There are other measures that require further cooperation from the national authorities and

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<td>Cross-border resolution regimes and bankruptcy laws</td>
<td>• The implementation of a cross-border resolution regime may result complex and unfeasible due to the following:</td>
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<td>– Current resolution regimes are local in scope.</td>
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<td>– Such regimes are designed accordingly to the characteristics of the legal systems of each country.</td>
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<td>Regulatory and supervisory cooperation (supervisory colleges and information sharing)</td>
<td>• The effectiveness in the cooperation agreements would also depend on the following aspects:</td>
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<td>– Established colleges should consider information exchange mechanisms with non-members supervisors.</td>
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<td>– Global mechanisms for banking supervisors should be flexible and allow for an effective flow of information, given that the existent agreements are rigid and bilaterally based.</td>
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<td>– Information mechanisms should also comprise expedite and formal communication on fraudulent and harmful practices in the financial systems (i.e. Maddof, Stanford).</td>
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Conclusions

Trends today lead to increased regulation and supervision of the global banking and financial system.

The main challenge rests on to assessment of an adequate balance between the new regulation and the development of the banking and financial system to avoid negative effects, distortions and asymmetries.

The adequate implementation of the new *design of the regulatory and supervisory framework* requires of a full assessment and impact studies to determine the outcome.

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