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Mexico's Proposed Fintech Law Is Credit Positive for Banks

From Credit Outlook

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Last Tuesday, Mexico's Ministry of Finance and Public Credit (SHCP) issued a request for comment on a proposed financial technology (fintech) law that would regulate crowdfunding and tech-enabled payment platforms. The proposal is credit positive for Mexican banks because it establishes a clear set of norms, including minimum requirements for liquidity, solvency and provisions related to investor protection and anti-money laundering, that will make it easier for them to invest in fintech companies and remain at the forefront of financial innovation.

Within the next three years, collaborating fintechs should help banks to reduce their operating costs through the adoption of innovative tech-enabled payment platforms, smartphone applications and tools created by the fintech companies. Beyond those three years, it will widen banks' customer universe as crowdfunders will be mandated to report the credit information of their clients.

The banks that stand to gain the most are those that have made recent inroads into fintech, including Banco Bilbao Vizcaya Argentaria, S.A. (BBVA, A3/Baa1 stable, baa2[1]), parent of Mexico's largest bank, BBVA Bancomer, S.A. (A3/A3 stable, baa2). BBVA acquired Open Pay (unrated), a payment platform that facilitates e-commerce for large and small businesses. Other beneficiaries include Banco Ve por Más, S.A. (unrated), which recently acquired digital bank Bankaool, S.A. (unrated), and small financial institutions such as Caja Bienestar (unrated), which formed a strategic alliance with crowdfunder Micochinito (unrated).

Other Mexican banks have partnered with small fintech startups by providing special financing lines for entrepreneurs, mentoring and participating in business incubator events. These include innovation centers such as Fiinlab from Gentera, S.A.B. de C.V. (unrated), the holding company of microfinance bank Compartamos Banco, S.A.; Nexo BanRegio from Banco Regional de Monterrey, S.A. (unrated); and BBVA's Latin American fintech contest Open Talent.

Financial innovation is especially important in Mexico, where intermediation, measured as loans to GDP, remains one of the lowest among large Latin American economies at 34%, which is below Chile's 92%, Brazil and Colombia's 48% and Peru's 42%, but above Argentina's 16%. Through scalable and flexible business, crowdfunders provide financing alternatives to not just the millennial generation, but also to under-banked sectors, such as lower-income individuals, startups and small and midsize enterprises (SMEs). By providing information on the credit profiles of these customer segments, the proposed law will address what has been a major deterrent to the provision of credit by banks in Mexico, which has a high level of economic informality and a lack of information and transparency.

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[1] The bank ratings shown in this report are the bank's deposit rating, senior unsecured debt rating and baseline credit assessment.

We do not expect banks to heavily target these higher-risk market segments, and believe that fintechs will complement banks rather than compete with them because even many SMEs with good credit quality currently do not have access to traditional credit because of a lack of information and transparency.

Moreover, we continue to expect that Mexico's traditional lenders will continue to dominate lending and payment services through digital channels such as smartphones or the internet. Several banks are making multi-billion dollar investments aimed at enhancing their e-banking platforms and creating smart branches to offer greater convenience and more products and services to customers while improving operating efficiency. Because of their brick and mortar branch networks, Mexican banks' operating costs as a percentage of total assets are among the highest in Latin America at 3.7%, versus an average of 2.5% in Brazil, Chile, Colombia and Peru.

The law also recognizes virtual currencies, such as bitcoin, but only as a means of exchange. However, neither fintechs nor banks will be permitted to lend or offer investment denominated in these currencies, which should reduce systemic risks and opportunities for speculation.

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