Mexican Finance and Leasing Companies' Liquidity Risks Rise Amid Coronavirus

Constrained Funding Access and Reduced Cash Flows Increase Downside Risks

Fitch Ratings expects Mexican finance and leasing companies' credit volumes and collections to be adversely impacted amid the coronavirus, reducing their cash flows and increasing liquidity and funding risks. Although deferment or restructure plans are already being applied, an extension of these measures could further pressure liquidity and consequently ratings. To manage refinancing and liquidity risks, most Fitch-rated entities are utilizing available funding facilities and/or negotiating new funding lines or extensions with commercial and development banks.

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Fitch Ratings believes that Mexican finance and leasing companies (fincos) face increased funding and liquidity risks due to the coronavirus, as most of these entities are typically wholesale funded and are exposed to disruptions in debt markets. At the same time, the economic slowdown and measures to contain the pandemic are starting to impact credit volumes and collections, reducing fincos' cash flows.

Most of the entities examined in this report are already applying some form of ad-hoc deferment and restructuring plans to borrowers or are adhering to the regulator's programs (in the case of regulated entities), in an effort to avoid a significant rise of impairments and cope with clients' reduced payment capacities. Fitch believes these temporary relief measures make it difficult to gauge the crisis' effects on lenders' asset quality. The impact on asset quality could be further delayed in the event of an extension of these measures, depending on the magnitude and length of the crisis. To manage refinancing and liquidity risks, most Fitch-rated fincos are utilizing available funding facilities and/or negotiating new funding lines or extensions with commercial and development banks.

Fitch notes that development institutions often serve as a primary funding source among Mexican non-bank financial institutions (NBFIs) and especially non-regulated ones, which represent the vast majority. Additionally, development institutions often guarantee loans or market debt issuances for NBFIs. Although development entities were relevant players during prior crises, Fitch believes they have taken longer to react in the current crisis. Even though they have been mirroring deferral actions applied by their debtors to reduce mismatches, most Fitch-rated issuers are still negotiating with the development banks for either an increase in their credit facilities or additional aid. However, despite a decline in the reference rate to historical lows, funding costs have increased for some Mexican fincos, which could pose additional pressures.

Over the past two months, access to international and local debt markets has been delayed or market conditions have not been favorable for entities that have active issuances programs. A similar situation has occurred in the local market for long-term issuances. However, mainly short-term issuances have been partially rolled over at relatively higher costs.

Of the entities included in this report, only four (8.7%) are issuing debt in global markets, 15 (32.6%) are issuing debt in the local markets, and 28 (60.9%) are funded mainly through commercial and development banks.

For the purpose of this report, Fitch has classified rated Mexican fincos into five groups, depending on their business model, as follows: agribusiness, small and medium-size enterprises (SMEs), consumer and microfinance, payroll lending and auto finance. Each entity and group has different risk appetites, which consequently results in varying liquidity and refinancing risks. As a result, Fitch presents a base case (current liquidity gaps) and performs stress tests on each group's liquidity gaps to identify potential pressures on their liquidity profiles.

Stress Test Assumptions on Gross Loans

(%)	Haircut 1	Haircut 2
SME Lenders	20	30
Consumer and Microfinance Lenders	30	40
Agribusiness Lenders	20	30
Payroll Lenders	20	30
Auto Finance Lenders	20	30

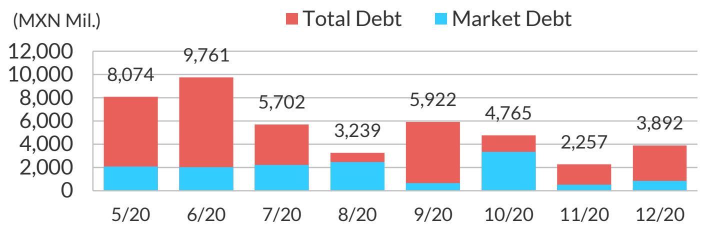
Source: Fitch Ratings.

SME Lenders

In Fitch's view, fincos that target SMEs will face reduced operating cash flows due to higher sensitivity to reduced business activity and social distancing measures combined with the low fiscal stimulus from the Mexican government.

As the majority of these fincos are non-regulated and not able to receive deposits or quasi-deposits, development institutions are usually a relevant source of funding and are expected to play a significant role in containing the deterioration of the fincos' liquidity profiles. However, these development entities have been relatively slow in approving additional credit lines for liquidity purposes. The largest fincos have had access to international and/or local debt markets over the past few years. Nevertheless, these funding sources are sensitive to market sentiment.

Short-Term Debt Maturities — SME Lenders



Note: Market debt includes the public issues of entities in the local and global financial markets. Total debt encompasses all of the entities' obligations, including market debt.
Source: Fitch Ratings.

About MXN14,000 million of the local and global debt issued by the largest SME lenders matures during 2020 (32% of their total debt), increasing near-term refinancing risk. These entities have been working to increase their on balance-sheet liquid assets and are seeking additional credit lines to cover these maturities.

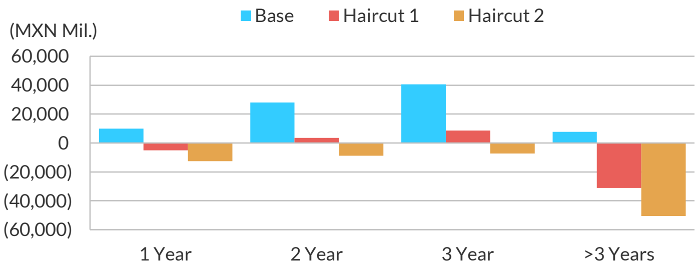
As of March 2020, around half of these fincos were acquiring additional credit lines mainly from commercial banks and, to a lesser extent, from development banks, other NBFIs and international investment funds. Some of these entities have adhered to the deferral programs of their funding providers (commercial and development banks) to match the deferral actions taken with some clients in their loan portfolio. Those entities presented positive cumulative liquidity gaps as of March 2020, so they seek to benefit from those deferral programs to match their clients' conditions with those of the funding sources that fund those credits.

As of March 2020, more than half of these entities had liquid assets and available credit lines that exceeded all of their short-term liabilities. The remaining entities covered almost all short-term liabilities or belong to a financial group, which could provide support if needed. Fitch will closely monitor the implemented actions of these companies and the effectiveness on their liquidity profiles.

Stress Test Results

The SME lenders stress test results show high sensitivity to reduced cash inflows, which could come from portfolio deterioration. Fitch applied haircuts of 20% and 30% on gross loan collections, which result in negative liquidity gaps from year 1. Fitch believes the availability of liquid resources and credit facilities to most of these entities, which cover slightly more than 1x their 2020 maturities, partially mitigates short-term liquidity risks.

Liquidity Gap Scenarios
(SME Lenders)



Source: Fitch Ratings.

Consumer and Microfinance Lenders

Fincos oriented toward unsecured consumer and microfinance lending exhibit higher risk appetites given their focus on the lower income population segment and the unsecured nature of the loan portfolio. This results in increased liquidity risks in the current environment, given the expected reduction in collections due to already increased unemployment and reduced commercial micro activity in the formal and informal sectors.

Deferral programs in these niches are not widespread given the short-term nature of the loans (16 weeks for microfinance loans) and the clients' less financially sophisticated nature. This low-income segment lending niche is characterized by high chargeoffs due to uncollected payments, which usually have low recoveries. Structural asset quality effects from the pandemic will be clearer once social distancing measures ease and employment, and informal and commercial activities stabilize.

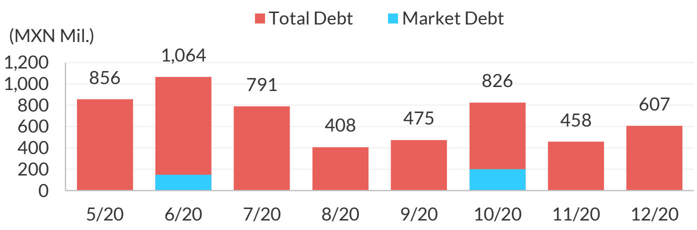
Although remittances could be affected by economic activity in the U.S., Mexican peso depreciation and Mexican government initiatives directed to micro businesses, these could potentially partially offset asset quality pressures.

As of March 2020, consumer and microfinance lenders still exhibited positive liquidity gaps for all periods. The business model benefits from the short-term nature of its loan portfolio compared to the medium- to long-term horizon of its liabilities.

The funding and legal structure of the regulated entities in this group (mainly Sofipos) allows them to take deposits. Therefore, much of their refinancing risk is related to the stability of their deposit structure, which in most cases has been proven through several years. Fitch considers that, in the case of non-regulated entities, refinancing risk will depend on the degree of participation by development banks and international funds, which represent a meaningful proportion of most entities' funding structures. In this group of fincos, only CAME and Crediclub have local debt issuances with maturities during 2020 but Crediclub already paid it off in full and CAME has sufficient liquid sources to cover this maturity, without the necessity to refinance through local markets.

In this group, only Findep has outstanding debt in the global markets; however, refinancing risk is not imminent because of the bullet maturity of its USD250 million bond in 2024.

Short-Term Debt Maturities — Consumer and Microfinance



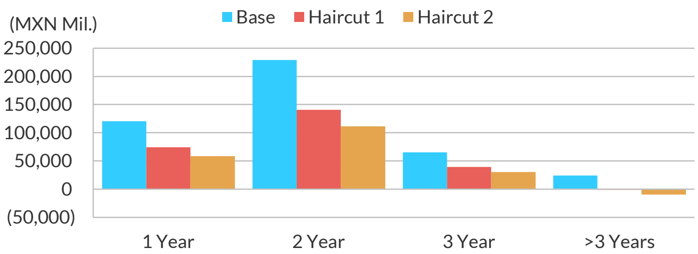
Note: Market debt includes the public issues of entities in the local and global financial markets. Total debt encompasses all of the entities' obligations, including market debt.
Source: Fitch Ratings.

Stress Test Results

Fitch performed two stress scenarios that consider haircuts of 30% and 40% on gross loans (due to their high sensitivity to the operational environment given the unsecured nature of their operations). Liquidity gaps are resilient over the coming three years, but the majority of the entities presented negative liquidity gaps over the longer term due to the very short-term nature of their portfolios

Liquidity Gap Scenarios

(Consumer and Microfinance Lenders)



Source: Fitch Ratings.

Agribusiness Lenders

Half of the entities in the Agribusiness group are credit unions, whose funding structures incorporate quasi deposits from associates, which are typically of a short tenor. Under Fitch's base and stress analysis, this results in mostly negative short-term liquidity gaps as of March 2020. Nevertheless, this is partially mitigated by the niche focus in specific guilds or communities with a long track record in the market (over 40 years on average in this sector), which has traditionally resulted in deposit stability. Additionally, Fitch considers that all entities in this group exhibited reasonable liquid resources and credit lines coverage for wholesale current liabilities since liquid assets (cash and short term investments) and available credit lines, which together add up to about USD350 million, covered almost 3x the total amount of their non-quasi-deposit short-term liabilities as of March 2020.

Most of the fincos in this group are not acquiring any additional credit lines, as credit unions are relying heavily on the stability of their main depositors. Fitch believes that, although deposit stability has been proven over several years, this specific crisis has no precedent and there might be some sensitivity to market sentiment due to increasing uncertainties or liquidity needs from local lockdowns that have extended periods.

Given their agriculture-oriented business model, most of these companies are more exposed to the cyclical conditions of agriculture, which could be further challenged by lower economic activity and demand under the current pandemic.

Development institutions, such as Fideicomisos Instituidos en Relacion con la Agricultura (FIRA), have usually been relevant in the funding structure of agricultural financing. As of March 2020, around 35% of total funding came from the development bank. FIRA usually also provides partial guarantees on client loans and the agency expects its effectiveness to be tested under the current environment.

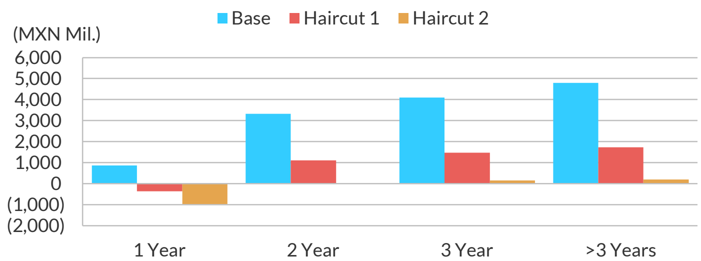
Agribusiness lenders are not issuing senior unsecured public debt in the capital markets. Only a Sofom included in this group (SEFIA) has an outstanding securitization as a funding source that will mature in June 2020.

Stress Test Results

For the liquidity gap analysis of this group, Fitch performed two stress scenarios. The first stress scenario included a 20% haircut on gross loans and, the second, a 30% haircut. The entities of this group had positive liquidity gaps as of March 2020; however, they show negative gaps under scenarios 1 and 2 for the first year. Nevertheless, entities in this group presented reasonable liquidity and credit lines coverage as of March 2020, which leads Fitch to consider that liquidity and refinancing risks are mitigated for this group in the medium and long term.

Liquidity Gap Scenarios

(Agribusiness Lenders)



Source: Fitch Ratings.

Payroll Lenders

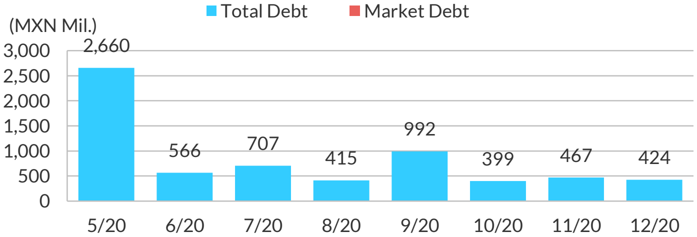
Payroll lending companies also face refinancing and funding challenges given their wholesale funding bases. This segment considers funding and liquidity information of three Mexican payroll lenders. Recently, there was an agreement among the Mexican Social Security Institute (IMSS), the Comision Nacional para la Proteccion y Defensa de los Usuarios de Servicios Financieros (Condusef) and several regulated and non-regulated financial entities in this sector to defer automatic withholdings to service payroll loans granted to pensioners, retirees, and active workers affiliated with the Mexican Institute of Social Security (IMSS) for three months (May, June, and July). Although this measure will result in reduced cash flows for the companies during this period, the agency believes these are manageable due to their appropriate cash positions as well as sufficient available credit facilities and that this will not necessarily result in permanent asset quality deterioration.

Fitch has highlighted repeatedly that payroll lenders are exposed to higher risk due to the operational and political risks that arise from business models concentrated in government employees or retirees. Although it is not part of the signed agreement, Fitch believes an unexpected additional extension of the deferral will likely have an impact on the ratings.

Payroll lenders are all issuing secured or unsecured debt in the local or global markets; however, there are no public debt maturities during 2020 for the entities of this group.

In Fitch's view, the entities of this group exhibit good liquidity resources and credit line coverage. As of March 2020, liquid assets (cash and short term investments) and available credit lines, which together add up to about MXN16,500 million, covered more than 1x the total amount of their short-term liabilities.

Short-Term Debt Maturities — Payroll Lenders

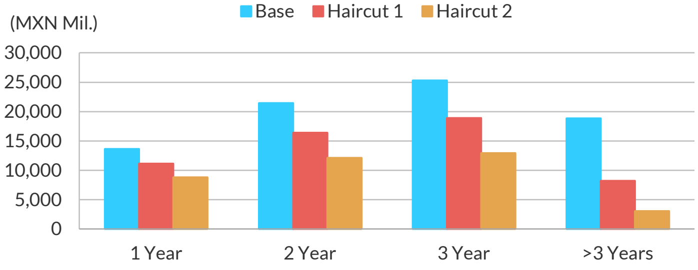


Note: Market debt includes the public issues of entities in the local and global financial markets. Total debt encompasses all of the entities' obligations, including market debt.
Source: Fitch Ratings.

Stress Test Results

In comparison with other fincos discussed in this report, payroll companies exhibit the most resilient liquidity gaps. The stress tests applied in this group included haircuts of 20% and 30% on gross loans, which resulted in positive liquidity gaps under both scenarios and across all buckets. Fitch believes these entities are better positioned to cope with the liquidity pressures from the current crisis than other NBFIs.

Liquidity Gap Scenarios
(Payroll Lenders)



Source: Fitch Ratings.

Auto Finance Lenders

Most of the entities in this group are captive finance companies whose ratings are fully driven by support, either due to explicit guarantees from their parent companies or their core role in the parent's strategy in the Mexican market. The lone exception is Sicrea, which is focused in providing auto loans mostly to organized groups of low income and informal workers.

In Fitch's opinion, most of the companies in this segment exhibited good liquid asset coverage as of March 2020 since their liquid assets and available credit facilities covered around 1x their short-term liabilities.

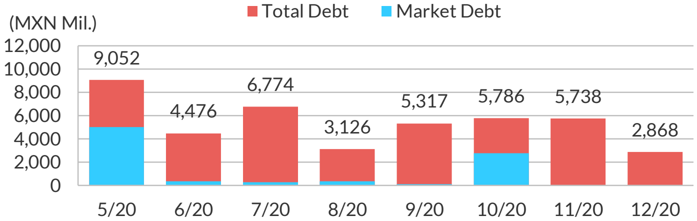
Captive fincos benefit from explicit guarantees on their debt programs or contingent credit lines provided by their parent companies, which widely mitigate refinancing and liquidity risks.

While these companies are recurrent issuers in the secured and unsecured local debt market, some entities have only been able to refinance their commercial paper for smaller amounts than in the past, in spite of their relatively high national-scale ratings, given current market conditions. The lower amounts issued in the local markets by the companies in this segment reflect the market sentiment challenges for this funding source.

According to the Mexican Association of Automotive Dealers (AMDA), sales in the automotive sector have been decreasing steadily since 2018. The AMDA reported that, during the first five months of 2020, automobile sales dropped around 30% relative to the same period in 2019 and car financing declined 18.1% year over year as of April 2020, which will impact profitability prospects for the segment. Deferral programs are being applied among these entities, most of them according the local regulator's guidelines since most are regulated Sofomes. The non-regulated ones are applying ad-hoc deferral programs. These programs will underestimate the effects on asset quality metrics but will very likely trigger a decrease in cash inflows in the sector.

However, Fitch believes the captive finance segment is better positioned to face the liquidity and refinancing risk that could arise from the coronavirus crisis given the availability of support, if needed, from their international corporate parents. In addition, this group increased significantly its cash and investments positions as of March 2020 and maintains a significant amount of available credit facilities.

Short-Term Debt Maturities — Auto Finance Lenders



Note: Market debt includes the public issues of entities in the local and global financial markets. Total debt encompasses all of the entities' obligations, including market debt.
Source: Fitch Ratings.

In the case of Sicrea, its funding structure includes monthly contributions by its groups of creditors, securitizations and available credit lines provided by commercial banks and a related party. The entity has historically relied heavily on securitizations (as of March 2020 they represented 100% of its interest bearing liabilities), which are exposed to market sentiment. The existing securitization had a partial amortization in April 2020 and re-starts its period of amortization in September 2020. The entity will seek for a new securitization issuance, but refinancing risks could arise due to market conditions. Fitch believes liquidity risk is partially mitigated because the entity had liquid assets and available credit lines that covered around 0.8x its short-term liabilities (interest bearing, insurance near term payments and automobiles to be delivered to the groups) as of May 2020.

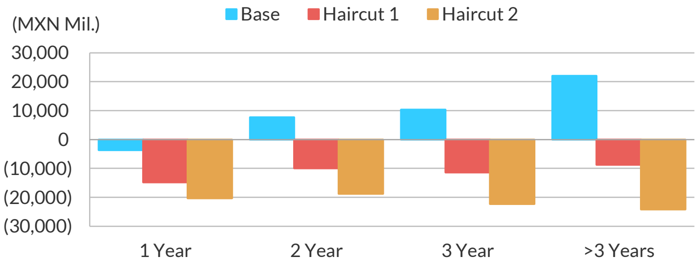
Stress Test Results

The stress scenarios at these companies included 20% and 30% haircuts on gross loans. Although this segment's liquid assets and credit facilities coverage is good, stressed liquidity scenarios showed negative gaps in all buckets. However, the latter is fully mitigated by the support from these entities' parent companies. Fitch expects each captive's parent to provide financial support in the event its respective subsidiary is unable to refinance its short-term debt maturities.

In the case of Sicrea, liquidity gaps are positive under both stress scenarios for all buckets, even in the shortest ones.

Liquidity Gap Scenarios

(Auto Finance Lenders)

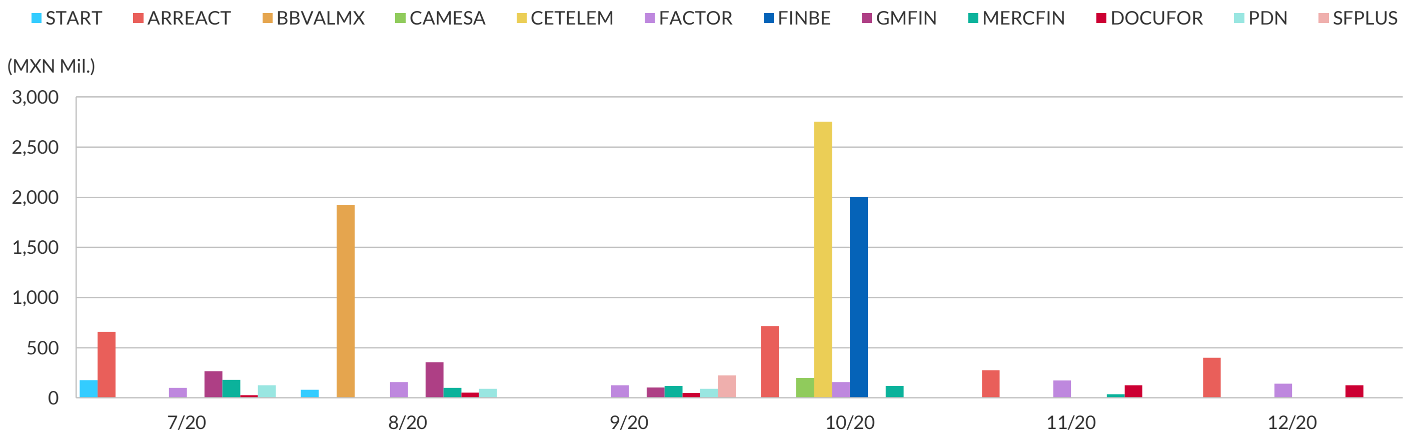


Source: Fitch Ratings.

Annex 1 — Short-Term Senior Unsecured Market Debt Maturities

Short-Term Senior Unsecured Market Debt Maturities — In the Coming Months

(As of March 31, 2020)



Note: CAMESA's senior debt has a partial guarantee.
Source: Fitch Ratings.

Annex 2 — List of Fincos with Public Ratings

Mexican Fitch Rated Issuers with Public Ratings

	Rating/Outlook/Watch	
Issuer	**(Current)**	**(End-2019)**
Almacenadora Accel, S.A., Organizacion Auxiliar del Credito	BBB+(mex)/Stable	BBB+(mex)/Stable
Almacenadora Banorte, S.A. de C.V., Organizacion Auxiliar del Credito, Grupo Financiero Banorte	AAA(mex)/Stable	AAA(mex)/Stable
Almacenadora Mercader, S.A., Organizacion Auxiliar del Credito	A(mex)/Stable	A(mex)/Stable
Almacenadora Sur, S.A. de C.V., Organizacion Auxiliar del Credito	BBB+(mex)/Negative	BBB+(mex)/Negative
Apoyo Economico Familiar S.A. de C.V., SOFOM, E.N.R.	A(mex)/Rating Watch Negative	A(mex)/Stable
Arrendadora Actinver, S.A. de C.V.	AA-(mex)/Negative	AA-(mex)/Stable
Arrendadora Ve por Mas, S.A. de .C.V., Sociedad Financiera de Objeto Multiple, Entidad Regulada, Grupo Financiero Ve por Mas	A(mex)/Negative	A(mex)/Stable
Arrendadora y Comercializadora Lingo, S.A. de C.V.	BBB-(mex)/Stable	BBB(mex)/Stable
Arrendadora y Factor Banorte, S.A. de C.V., SOFOM, E.R., Grupo Financiero Banorte	AAA(mex)/Stable	AAA(mex)/Stable
BBVA Leasing Mexico, S.A. de C.V.	AAA(mex)/Stable	AAA(mex)/Stable
Consejo de Asistencia al Microemprendedor, S.A. de C.V., Sociedad Financiera Popular	A(mex)/Negative	A(mex)/Negative
Credicam, S.A. de C.V. SOFOM, E.N.R.	BBB+(mex)/Negative	BBB+(mex)/Stable
Crediclub, S.A. de C.V., Sociedad Financiera Popular	A-(mex)/Negative	A-(mex)/Stable
Credito Real, S.A.B. de C.V., Sociedad Financiera de Objeto Multiple, Entidad no Regulada	A+(mex)/Stable	A+(mex)/Stable
De Lage Landen, S.A. de C.V., SOFOM, ENR	AAA(mex)/Rating Watch Negative	AAA(mex)/Stable
Factoring Corporativo, S.A. de C.V. Sociedad Financiera de Objecto Multiple, Entidad Regulada	A-(mex)/Stable	A-(mex)/Stable
Financiera Bajio, S.A. de C.V., SOFOM, E.R.	AA(mex)/Negative	AA+(mex)/Stable
Financiera Bepensa, S.A. de C.V., Sociedad Financiera de Objeto Multiple, Entidad Regulada	AA+(mex)/Stable	AA-(mex)/Stable
Financiera Independencia, S.A.B. de C.V., SOFOM, E.N.R.	A(mex)/Rating Watch Negative	A(mex)/Stable
Ford Credit de Mexico, S.A. de C.V., Sociedad Financiera de Objeto Multiple, Entidad Regulada	AA-(mex)/Negative	AA(mex)/Negative
LC Liquidez Corporativa, S.A.P.I. de C.V. SOFOM E.N.R.	BBB(mex)/Negative	BBB(mex)/Stable
Mercader Financial, S. A., SOFOM, E.R.	A-(mex)/Negative	A-(mex)/Stable
Metrofinanciera, S.A.P.I. de C. V., Sociedad Financiera de Objeto Multiple, Entidad Regulada	B+(mex)/Stable	B-(mex)/Stable
Mexarrend S.A.P.I. de C.V.	BBB+(mex)/Negative	A-(mex)/Stable
Oportunidades para Emprendedores, S.A.P.I. de C.V., SOFOM E.N.R.	BBB-(mex)/Negative	BBB-(mex)/Stable
Portafolio de Negocios, S.A. de C.V., SOFOM ER	A(mex)/Stable	A(mex)/Stable
Santander Consumo, S. A. de C. V. Sociedad Financiera de Objeto Multiple, Entidad Regulada, Grupo Financiero Santander Mexico	AAA(mex)/Stable	AAA(mex)/Stable
Servicios y Financiamiento Agricola, S.A. de C.V., SOFOM ENR	BBB+(mex)/Rating Watch Negative	BBB+(mex)/Stable
Sistema de Credito Automotriz, S.A. de C.V.	A-(mex)/Negative	A-(mex)/Stable
Sofipa Corporation, S.A.P.I. de C.V., SOFOM, E.N.R.	BB+(mex)/Stable	BB+(mex)/Positive
Sofoplus, S.A.P.I. de C.V., Sociedad Financiera de Objeto Multiple, Entidad Regulada	A-(mex)/Negative	A-(mex)/Stable
START Banregio, S.A. de C.V. SOFOM E.R., Banregio Grupo Financiero	AA(mex)/Negative	AA+(mex)/Stable

Mexican Fitch Rated Issuers with Public Ratings

	Rating/Outlook/Watch	
Issuer	**(Current)**	**(End-2019)**
Toyota Financial Services Mexico, S.A. de C.V.	AAA(mex)/Stable	AAA(mex)/Stable
Unagra, S.A. de C.V., Sociedad Financiera Popular	BBB-(mex)/Stable	BBB-(mex)/Stable
Unifin Financiera, S.A.B. de C.V.	A(mex)/Negative	A(mex)/Stable
Union de Credito Agricultores de Cuauhtemoc, S.A. de C.V.	A-(mex)/Stable	A-(mex)/Positive
Union de Credito Allende, S.A. de C.V.	BBB(mex)/Stable	BBB(mex)/Stable
Union de Credito Concreces, S.A. de C.V.	BB+(mex)/Rating Watch Negative	BB+(mex)/Stable
Union de Credito de Gasolineros, S.A. de C.V.	BBB+(mex)/Stable	BBB(mex)/Positive
Union de Credito Mixta de Coahuila, S.A. de C.V.	BBB(mex)/Negative	BBB(mex)/Stable
Union de Credito para la Contaduria Publica, S.A. de C.V.	BBB+(mex)/Negative	BBB+(mex)/Stable
Valmex, Soluciones Financieras S.A. de C.V.	AA-(mex)/Stable	AA-(mex)/Stable

Source: Fitch Ratings.