

Additional measures to promote an orderly behavior in the financial markets strengthen credit granting channels and provide liquidity for the sound development of the financial system in Mexico

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The pandemic caused by COVID-19 has led, among other measures, to significant reductions of interest rates and adoption of extraordinary measures by central banks around the world to promote the proper functioning of their financial systems.

In this context, on April 20, 2020, the Board of Governors of the Mexican Central Bank (Banco of México) approved additional measures to promote orderly behavior in the financial markets, strengthen credit granting channels and provide liquidity for the healthy development of the financial system.

The referred measures are the following:

1. **Increase of liquidity during business hours to enable the optimal functioning of financial markets and payment systems.**

In order to promote an orderly behavior of the money market in our country, the Mexican Central Bank has maintained a daily excess of liquidity during the business hours of the financial markets. The Mexican Central Bank will **increase liquidity during business hours if necessary**. Information regarding the daily liquidity amount will be disclosed to the credit institutions through the systems managed by the Central Institute (Instituto Central).

2. **Expansion of securities eligible for the Ordinary Additional Liquidity Facility (Facilidad de Liquidez Adicional Ordinaria or “FLAO”), foreign exchange hedging transactions and credit transactions in dollars.**

In order to provide liquidity to stock market instruments that, due to uncertainty and volatility conditions, have seen their operability and liquidity decrease in the secondary market, and thus avoid a segmentation of the debt market, the Mexican Central Bank has decided to **expand the range of eligible debt instruments in the FLAO repurchases, and the guarantees for foreign exchange hedging transactions that are settled in pesos, as well as credit auctions in dollars**. Eligible securities in national currency must have credit ratings equal to or greater than those equivalent to “A” on a national scale, or equivalent to “BB+” on a global scale for securities

denominated in foreign currency, granted by at least two rating agencies in each case. The Mexican Central Bank expressed that further details for these measures will be disclosed through amendments to Circular 8/2009¹, Circular 3/2017² and Circular 10/2015³.

3. Expansion of counterparties eligible for the FLAO

The Mexican Central Bank has decided to expand access to the FLAO to development bank institutions, with the aim that these institutions can obtain liquidity, through guaranteed loans or repurchases, at the same cost of 1.1 times the target for the overnight interbank interest rate of the Mexican Central Bank. In doing so, the Mexican Central Bank provides an additional liquidity alternative to development banks and helps them to channel resources to productive projects for the benefit of the country. The Mexican Central Bank expressed that further details will be set forth through amendments to Circular 10/2015.

In relation to items 2 and 3 above, on May 13, the amendments to Circular 10/2015 were published in the Official Gazette (Diario Oficial de la Federación or “DOF”), through the Circular 15/2020, in order to facilitate credit institutions, the implementation of the necessary measures to access the financing granted by the Mexican Central Bank to cover ordinary liquidity needs.

The following are the most relevant amendments:

- It is clarified that such Circular is also applicable to development bank institutions and not only to multiple bank institutions. Only those institutions that face temporary liquidity needs to meet their payment obligations in the required terms or carry out their operations and who meet the requirements established for each type of financing set forth in the Circular, may request temporary financing.
- Foreign subsidiaries that grant credit ratings to the securities subject to repurchase are included within the concept of securities credit rating institutions.
- The concepts of “Global Scale Credit Quality Criteria” and “National Scale Credit Quality Criteria” (“Criterio de Calidad Crediticia Escala Global” and “Criterio de Calidad Crediticia Escala Nacional”, accordingly) are added, applicable to the securities offered for repurchase.
- Debt securities denominated in national currency or in UDIS, deposited in Indeval, that comply with the Credit Quality Criteria on National Scale and which have been issued by:
 - State-owned companies of the Federal Government;
 - State Productive Companies;
 - Multiple bank institutions, other than the one reported and that are not part of the same financial group, business group or consortium to which the latter belongs;
 - Federal entities and Municipalities;
 - International financial organisms and multilateral entities;
 - Non-financial legal entities resident in Mexico that are not part of the same financial group, business group or consortium to which the reported belongs;
 - Certain trust fiduciary institutions that issue such debt securities in the form of trust certificates

The amendment sets forth which provisions will be in force only between the entry into force of the referred Circular and September 30 of this year.

¹ Rules applicable to credit auctions in US dollars.

² Rules applicable to foreign exchange hedging auctions.

³ Rules applicable to the exercise of financing granted by the Mexican Central Bank to cover ordinary additional liquidity needs.

4. **Window for the repurchase of government securities with term.**

With the purpose of providing liquidity to financial institutions holding government debt, the Mexican Central Bank has decided to open a window for the acquisition of government securities under repurchase for terms longer than those regularly used in open market transactions. This will allow these institutions to obtain liquidity without the need to dispose of their securities under conditions of high volatility in the financial markets. The cost of the repurchase will be the equivalent to 1.02 times the average of the overnight interbank interest rate of the Mexican Central Bank during the term of the transaction. With this window, the Mexican Central Bank enables an orderly brokerage of government securities (Cetes, Bonos M, Udibonos, Bondes D and BPAs), which would benefit those financial institutions with liquidity needs. The amount of the program will be up to 100 billion pesos and may be adjusted based on the prevailing conditions in the financial market.

The relevant regulation is included in Circular 17/2020 (Rules applicable to government securities repurchase transactions with the Mexican Central Bank to cover liquidity needs), published in the DOF on May 19, which will be in force until September 30 of this year. The foregoing, unless that at this date reports remain in force, in which case they will remain in force until their liquidation, subject to the provisions of the Circular and the applicable contracts

5. **Window for the temporary exchange of collateral.**

In order to promote an orderly behavior of the debt market, the Mexican Central Bank has decided to implement a facility for the exchange of debt instruments to provide liquidity to stock instruments that, due to the uncertainty and volatility conditions, have seen their operability and liquidity decrease in the secondary market. Eligible securities in national currency for this transaction must meet the same credit quality criteria as in FLAO. Under this facility, eligible institutions may deliver as a guarantee, debt instruments to the Mexican Central Bank⁴ in exchange for government securities, subject to the obligation to return such government securities at the end of the corresponding period. The amount of the program will be up to 100 billion pesos and may be adjusted based on the prevailing conditions in the financial markets.

The details of this facility were disclosed through the issuance of Circular 16/2020 (Rules applicable to securities lending operations with the Mexican Central Bank to improve liquidity), published in the DOF on May 19, whose validity will expire on September 30 of this year.

6. **Facility for the Repurchase of Corporate Securities (Facilidad de Reporto de Títulos Corporativos or “FRTC”).**

The Mexican Central Bank has decided to implement a facility to repurchase corporate securities from credit institutions, with the aim of providing liquidity to short-term corporate bonds and long-term corporate debt, whose operability and liquidity in the secondary market have decreased due to conditions of uncertainty and volatility. The securities eligible for the repurchase transactions will be those issued by non-financial institutions in the private sector with residence in Mexico, and which meet the same criteria as in FLAO. The cost of the repurchase will be equivalent to 1.10 times the average of the overnight interbank interest rate of the Mexican Central Bank during the term of the transaction. The amount of the program will be up to 100 billion pesos and may be adjusted based on the prevailing conditions in the financial markets.

In relation to the above, Circular 19/2020 was published in the DOF, dated May 19.

7. **Provision of resources to banking institutions to channel credit to micro, small and medium-sized companies and to individuals affected by the pandemic.**

With the aim of promoting greater credit to micro, small and medium-sized companies, as well as to individuals affected by the pandemic, the Mexican Central Bank has decided to provide resources to multiple and development banking institutions so that these institutions, in turn, channel such resources to the aforementioned companies and individuals. The Mexican Central Bank will release resources associated with the Deposit of

⁴ The guarantee may be established with respect to the same securities that may be object of repurchase agreement, previously mentioned in this document regarding the description of Circular 15/2020.

Monetary Regulation (Depósito de Regulación Monetaria) or, if necessary, will provide financing for a term of between 18 and 24 months, with a cost equal to the target for the overnight interbank interest rate, to multiple and development banking institutions that finance the aforementioned companies and individuals with additional resources. Financing will be guaranteed with securities that must meet the same eligibility criteria as in FLAO. To ensure that the origination and management of the portfolio complies with the provisions, the registration and monitoring of credits associated with this facility will be done by a development bank or development institution (institución de fomento), in the same terms of other programs carried out by such institutions, or directly by the Mexican Central Bank. These resources may be combined with the guarantee programs implemented by development banks and development institutions. The amount of the program will be up to 250 billion pesos and may be adjusted based on the prevailing conditions in the financial markets. Further details will be announced through the issuance of a circular that will regulate these transactions.

8. Financing facility for multiple banking institutions, guaranteed with loans to companies, for the financing of micro, small and medium-sized companies.

The Mexican Central Bank has decided to temporarily provide a financing facility guaranteed with loans to companies that issue stock debt, so that such financing is channeled to micro, small and medium-sized companies in Mexico. The Mexican Central Bank will provide financing with a term of between 18 and 24 months, with a cost equal to the target for the overnight interbank interest rate, guaranteed with loans from companies whose credit rating is equal to or greater than "A" on a local scale by at least two rating agencies. As in the previous case, the registration and monitoring of the new credits associated with this facility will be done through a development bank or development institutions, in the same terms as other programs carried out by such institutions, or directly by the Mexican Central Bank. The amount of the program will be up to 100 billion pesos and may be adjusted based on the prevailing conditions in the financial markets. Further details will be announced through the issuance of a circular that will regulate these transactions.

9. Swap (permuta) of government securities.

With the aim of promoting the proper functioning of the government debt market, the Mexican Central Bank will carry out government securities swap transactions, through which it will receive long-term securities (from 10 years) and deliver other securities with terms to maturity of up to 3 years. The characteristics and terms of the swap will be set forth in each auction call. The amount of the program will be up to 100 billion pesos and may be adjusted based on the prevailing conditions in the financial markets. The amounts and characteristics of the auctions will be disclosed in the corresponding amendments to Circular 8/2014, as well as in the respective auction calls.

10. Exchange rate hedges payable in United States dollars with counterparties not domiciled in the country to be able to operate during the hours in which the national markets are closed.

Considering the characteristics of the Mexican peso as a global currency, which has ample liquidity and operates 24 hours a day, the Mexican Central Bank, by instruction of the Exchange Commission (Comisión de Cambios), and under the same terms of the Exchange Coverage Program (Programa de Coberturas Cambiarias) currently in force, will include in its tools for intervention in the foreign exchange market, the possibility of arranging and executing exchange hedging transactions that can be settled for differences in United States dollars. The foregoing in order to be able to operate in the hours in which the national markets are closed. Thus, these transactions may be arranged and executed with institutions not domiciled in the country at any time. The purpose of this complementary tool will be to seek orderly operating conditions in the peso-dollar exchange market, particularly during the Asian and European sessions, when so determined by the Foreign Exchange Commission.

The first nine measures described above are in force until September 30, 2020, while the validity of the tenth measure will be determined by the Foreign Exchange Commission.

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