

CASE STUDY

# Accessing Local Currency Financing and Risk Management Tools at the Sub-national Level in Mexico

## OVERVIEW

Mexico's federal mortgage corporation needed to reduce the rollover risk and asset-liability mismatch on its balance sheet. IBRD provided a 30-year US\$1 billion loan (roughly 13% of Sociedad Hipotecaria Federal's (SHF) total balance sheet). A customized package of financing and risk management tools allowed SHF to extend the maturity of its debt portfolio and mitigate exposure to foreign currency and interest rate risks.



## Background

Mexico's federal mortgage corporation, Sociedad Hipotecaria Federal (SHF), grants loans and guarantees to mortgage intermediaries in Mexico. SHF also plays a crucial role as market maker by providing liquidity to the market, buying and selling mortgage securities.

In order to continue supporting the development of the domestic housing finance market, SHF needed to strengthen its balance sheet. At the same time, it was important for SHF to reduce its vulnerability to the rollover risk and mismatch of financial terms that resulted from using short-term borrowings to fund longer term lending operations.

## Financing Objectives

SHF needed access to flexible, long-term financing

in local currency to extend the maturity structure of its portfolio and avoid the foreign currency exposure usually related to external financing. It also needed tools to manage interest rate risk over time as on-lending to financial intermediaries materialized.

## IBRD Financial Solution

An IBRD Flexible Loan for US\$1 billion (roughly 13% of SHF's total balance sheet) with a 30-year maturity, including a 5-year grace period, allowed SHF to extend the maturity of its debt portfolio to attain a more stable risk profile. The IBRD loan has risk management tools, which SHF accessed to mitigate its exposure to foreign exchange and interest rate volatility.

IBRD Customized the loan per SHF's request with a mix of fixed and floating interest rates in Mexican pesos. SHF has the option to change the mix of fixed

to variable interest rates in the future for the full or partial maturity of the loan, in order to match the interest rate risk on its balance sheet (see Figure 1).

## Outcome

The World Bank Treasury customized a package of financing and risk management tools for SHF that allowed it to strengthen its balance sheet and attain a more stable risk profile in terms of maturity, interest rate basis, and currency mix. IBRD acted as a market intermediary, accessing long-term cross-country and interest rate swaps in the market at more favorable rates than SHF would have been able to obtain had it accessed the market directly.

## Terms & Conditions

<b>Amount</b>	US\$1 billion
<b>Maturity</b>	30-yr final maturity; 5-yr grace period
<b>USD Interest Rate</b>	Floating rate (6-month LIBOR <sup>1</sup> + fixed spread)
<b>Currency Conversion</b>	MXN
<b>MXN Interest Rate</b>	Floating rate (28-day TIIE <sup>2</sup> + spread) and fixed rate
<b>Risk Management</b>	Currency and interest rate hedging

1. LIBOR (London Interbank Offered Rate) is a floating reference rate based on the interest rates at which banks borrow unsecured funds from other banks in the London wholesale money market.
2. TIIE (Tasa de Interés Interbancaria de Equilibrio) is a benchmark Mexican peso floating rate index.

Figure 1: Illustration of Currency and Interest Rate Risk Management Transactions



3. SHF executed partial maturity fixings of a portion of the Mexican peso floating rate financing for periods of 12 and 15 years.

## For information:

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