

1995 FINANCIAL SYSTEM REFORMS

Given the number of amendments to its provisions and in order to make it easier for commercial banks to consult and understand the standards applicable to its borrowing, lending and services transactions, on September 20, 1995, Banco de México issued Circular 2019/95, which is a compilation of the regime in effect up until that date. Some of the most important provisions included in the Circular as well as the main provisions issued in 1995 are discussed below.

Banco de México transactions aimed at easing pressures from Federal Treasury Bonds (TESOBONOS) in the foreign exchange market

Banco de México offered banks the possibility of settling in advance loans granted by the Bank in auctions by using Federal Treasury Bonds (TESOBONOS) as payment. Subsequently loans granted by the Central Bank to banks other than those that paid using TESOBONOS were allowed to be settled early as well as deposits created by Banco de México owed by them. In order to help banks wishing to settle loans and/or deposits the Central Bank sold them a short-term foreign currency hedge.

At the end of January it was established that banks could sell TESOBONOS to Banco de México and use the proceeds from the sale to create interest-bearing fixed-term deposits with the Bank, providing that loans and/or deposits funded by Banco de México had already been settled; in order to keep banks' foreign currency positions balanced, the Central Bank entered into foreign exchange hedge sell transactions with any banks that requested them.

On March 17, 1995, Banco de México, on behalf of the Federal Government, offered to pay at their maturity and to those banks requesting it, their own or third party positions of TESOBONOS -besides their equivalent in local currency- in US dollars, as long as said government securities were deposited in their own or third party custody accounts by the close of the working day prior to their maturity date at the latest.

Likewise brokerage firms were given the opportunity to settle repos on TESOBONOS entered into with Banco de México ahead of time in order to use some of the proceeds from the settlement to meet loans granted by the country's banks funded by Banco de México.

In January 1995, Banco de México allowed brokerage firms to settle repos on TESOBONOS entered into with the Bank early in order to pay deposits that Banco de México had funded for and were owed by the country's banks. On January 27th, 1995, Banco de México allowed brokerage firms to settle repos on TESOBONOS entered into with the Bank early so they could create bank deposits in favor of the country's banks.

All of these provisions permitted banks and brokerage firms to reduce their transactions with the Banco de México, and consequently the pressures caused by TESOBONOS in the foreign exchange market.

Foreign currency liability admission

In order to give commercial banks more investment options with respect to their foreign currency liability investment regime, as of January they were allowed to invest up to three percent of their "investable liability" in commercial notes issued by Banco Latinoamericano de Exportaciones, S.A. (BLADEX) denominated in US dollars with a maturity not exceeding 90 days and in demand deposits or 7-day fixed term deposits denominated and payable in US dollars and of this Bank.

In March 1995, a new option besides the existing one was established for commercial banks to determine the maximum amount of "investable assets" in foreign currency. This amount is calculated by multiplying the bank's net capital by 1.6 the second month immediately following the month in question, including liabilities corresponding to the temporary capacity of foreign currency liability admission.

Likewise, on the same date it was decided that the "investable liability" acquired by banks in favor of foreign banks that control at least 51% of the bank's capital stock, or at least 51% of the capital stock of a controlling company affiliate, which in turns controls at least 51% of the capital stock of the bank in question, will not be included in the calculation of the limit on the foreign currency-denominated "investable assets" of commercial banks.

Dollar Futures and Dollar Options Markets

Given that futures markets are an efficient mechanism for managing and distributing risks and for calculating prices and exchange rates and contribute to their stability besides permitting the development of risk hedge mechanisms, in March and April 1995, dollar futures and options markets were established.

Banks interested in participating as intermediaries in these markets had to request authorization from Banco de México that would be granted on a discretionary basis once they had obtained a report issued by a Central Bank approved consulting company stating they had the technical capacity to undertake such transactions. As of August 29, 1995, banks wishing to act as intermediaries must also comply with 31 administration, operation and internal control requirements.

Commercial banks were allowed to enter into local currency liability transactions with foreign banks, foreign brokerage firms and persons acting on their behalf as long as the local currency corresponds to entering into

futures contract on Mexico pesos traded in foreign markets recognized by Banco de México (Chicago Mercantile Exchange). They were also allowed to undertake future transactions on local currency only when they took place in futures markets recognized by Banco de México or complied with Banco de México stipulations in its general provisions.

As the Chicago Mercantile Exchange asked banks to guarantee compliance with payment obligations entered into with the institution, Banco de México authorized the country's banks to guarantee such transactions by creating securities portfolio pledges.

In August 1995 and following diverse requests from some banks to participate in dollar futures transactions and in order to have another instrument for hedging banks' exchange rate risk, the Central Bank established a transitory regime from August 29 to December 31, 1995 under which banks obtained general authorization to participate in the dollar futures market with other intermediary banks and/ or which banks meeting such requisites.

As of January 1996 and until June 30 of that year, only banks that in the opinion of Banco de México met its 16 administration, operation and internal control requirements could continue to participate.

As of July 1st, 1996 it was decided that only banks that had been authorized to act as intermediaries could enter into such transactions. Finally it was stipulated that as of July 1st, 1996, the only authorizations granted to banks would be for specific transactions.

Short-term Foreign Currency Hedges Market

As the risk implicit in short-term foreign currency hedge transactions are similar to those of dollar future market transactions, Banco de México deemed it appropriate for banks acting as intermediaries or participants in the hedges market to meet the same requisites as those requested of banks acting with such characteristics in said market.

A transitory regime was established for banks and brokerage firms that prior to August 29th, 1995 had obtained authorization to act as intermediaries in that market until December 31st, 1995; to renew their authorization expiring on June 30th, 1996, they had to comply with Banco de México's 16 administration, operation and internal control requirements.

Interbank Equilibrium Interest Rate (TIIE)

In order to have an interbank interest rate that more accurately reflects market conditions than the Average Interbank Interest rate (TIIP), in March 1995, Banco de México issued provisions for calculating the Interbank Equilibrium Interest Rate (TIIE).

Deeming it useful for the general public and especially for people that undertake financial system transactions, to be kept aware of the TIIP, Banco de México decided to continue to publish the rate along with the TIIE in the Official Federal Gazette on the bank working day following the day it is calculated. As the TIIP will eventually cease to be used in bank transactions, it will only be published until December 31st, 2001, unless Banco de México decides it is appropriate to continue publishing it after that date.

With respect to nominal interest rate future markets as of March 24th, 1995 TIIE will be used instead of TIIP.

National Consumer Price Index

In order to make price indexes more representative of the general price trend, on March 24th, 1994, Banco de México published the presentation base 1994=100 in the Official Federal Gazette in substitution of 1978=100. These new index weightings correspond to household expenditure in 1993 prices and substitute those of 1980. The sample of cities increased to 46 from 35 located in all states; the basket of basic products increased from 302 to 313 and the number of prices collected every two weeks from 70,000 to 85,000. Up until the second half of February 1995, the National Consumer Price Index was published in the Official Federal Gazette with the 1978=100 base.

In order to be congruent with these changes Banco de México decided that the base used in NCPI futures market would be 1994=100.

Investment Units

In order to provide an instrument that contributes to mitigating the problems inflation causes savers and borrowers as a result of loan transactions, on April 1st, 1995, the Official Federal Gazette published the Decree establishing obligations that can be denominated in investment units (UDIS).

The investment unit is a unit of constant, real value that anything related to credit can be denominated in with the exception of checks and mercantile and other commercial actions in general. Banco de México periodically publishes the peso value of the unit of account in the Official Federal Gazette. Banks can denominate the following debt transactions in investment units: deposits withdrawable on demand; deposits withdrawable on preset days; fixed-term deposits; loans documented in promissory notes paying a return that can be settled at maturity; bank bonds; subordinated debentures; bankers' acceptances; commercial paper with a bank guarantee; local currency debt derived from interbank transactions and assets. The term of debt transactions may not be less than 3 months.

In order for banks to re-state local currency-denominated debt transactions entered into prior to April 4, 1995, in investment units, they were exempted from section XV of article 106 of the Law on Credit Institutions regarding the early payment in full or in part of obligations derived from the debt transactions mentioned in the previous paragraph as long as they had agreed with clients that with the proceeds from the payment would be used to enter into a new debt transaction denominated in UDIS for a period equal to or greater than the one on which an early payment had been made.

Banco de México publishes the local currency value of the UDIS each day in the Official Federal Gazette as follows: a) on the 10th of each month at the latest it publishes the value corresponding to the 11th and 25th of each month, and b) on the 25th of each month it publishes the value corresponding to the 26th of the month through the 10th of the following month.

It was determined that the legal instruments used by banks to document their

UDIS-denominated borrowing and lending transactions should include the payment of a single rate of interest with no other options.

In order for banks to balance their UDIS transactions a procedure was established for calculating the Net Position of certain UDIS-denominated assets and liabilities.

In order to have a reference rate for transactions denominated in investment units, in May 1995, Banco de México modified the procedure for calculating the Interbank Equilibrium Interest Rate (TIIE) to include transactions denominated in Investment Units (TIIE-UDIS); however, as quotations received from banks for calculating the TIIE-UDIS for the first time were very varied, Banco de México deemed it appropriate to wait until the UDIS-denominated bank transactions market was more developed before calculating this rate.

Single Account

The regime related to the single account underwent diverse modifications throughout 1995 and so in the middle of September a compilation of this regime could no longer be postponed and occurred through Circular 2019/95, with diverse Circulars-Telefax ceasing to have effect. The same regime was applied to development banks with the exception of guarantees.

The daily balances of bank in question are added at the end of a calculation period, which consists of 28 calendar days. The result is known as accumulated daily accounts.

At the end of the calculation period, banks must have accumulated daily balances greater than or equal to zero; if not Banco de México charges to their accounts an amount equal to the result obtained from applying to their negative balance the rate resulting from multiplying the arithmetic average of the annual CETES yield of the four auctions prior to the date on which the balance of the accumulated daily balances is calculated by two and the result is then divided by 360.

Commercial banks may only overdraw on this account by up to the value of bank and government securities previously given to Banco de México in guarantee. Banco de México informs them by no later than the 20th of each month of the minimum amount of guarantees they must maintain at all times during the next calendar year.

Development banks may only overdraw by up to an amount not exceeding 25% of the net capital registered in the second calendar month immediately prior to the one in which such overdrafts take place. However, because of the problems they could cause the financial system, Banco de México accepts certain additional overdraft amounts to those mentioned in the previous two paragraphs. The transactions mentioned are always settled; however, banks must pay interest on each minute their single account is overdrawn in relation to these concepts.

Foreign Exchange Risk Positions

A new regime was established for determining the foreign currency risk

position of banks and brokerage firms previously known as foreign exchange market position. The aforementioned foreign risk position is the difference between the sum of bank and brokerage firm assets subject to foreign exchange risk that increases their value in local currency and liabilities that decrease it in the event of peso depreciation against foreign currencies (long position), and the sum of bank and brokerage firm assets subject to foreign exchange risk which decreases their value in local currency and liabilities which increase it as a result of peso depreciation against other currencies (short position).

Foreign currency purchases and sales pending settlement resulting from dollar future and options transactions were included in the assets and liabilities for consideration in the calculation of banks' foreign exchange position as per their regime.

Special Personal Savings Accounts

Interest paid on personal savings accounts was brought into line with other demand deposits.

Settlement of the Results of Clearing House Documents.

As of January 4, 1996, in order to: a) make the payment system more secure; b) promote the use of alternative payment media to the cheque for transaction settlement, and c) make the credit risks incurred by banks and the Central Bank when clearing documents explicit, Banco de México settles cheque clearing results on the bank working day following their submission to the clearing house with no retroactive effects. The Bank also fostered the commercial banks' obligation to debit and credit clearing house checks to their clients' accounts at the start of the bank working day following the one on which such checks were deposited in the account. This procedure only applies to checks drawn within the same city.

This Circular-Telefax modified the value dates on which Banco de México executes the fund transfer orders resulting from the clearing process. Clearing settlement was previously undertaken with retroactive effect on the previous working day so banks could consider checks drawn on other banks as firm deposits with no funding cost, which meant they ran the risk of there not being funds to collect the checks, and the decision not being made in accordance with strict controls for granting such funding.

Furthermore, it was established that instructions for fund transfer orders related to interbank transactions should be made through SIAC-BANXICO from 9:00 to 17:30 hours with a same value date or next bank working day value at the bank's request. It was also established that between 18:30 and 19:30 hours Banco de México would execute local currency-denominated fund transfers with a same day value date between banks' single accounts as long as said transfers were originated by credit transactions banks had entered into exclusively and directly.

Fund transfers resulting from clearing are executed by Banco de México with the same value date when Banco de México receives the order through SIAC-BANXICO from 7:30 to 9:00 hours. If the order is received between 9:00 and 19:30 hours, it is executed with a next bank working day value date.

Provisions related to the single account overdraft regime were also modified to establish that overdrafts registered at 19:30 hours each working day will incur interest per minute between 17:30 hours of the working day in question and 9:00 hours on the next working day. As a result of the new settlement procedure for documents with a "next working day" value date, diverse necessary adjustments were made.

Interest Rates on Lending Transactions

In November and December 1995, substantial changes were made to provisions related to interest rates on lending transactions in order to give the general public elements that facilitate knowledge and comparison of the effective cost of funding offered by commercial banks.

In order to achieve this Banco de México instructed commercial banks to document a single interest rate, which would be either fixed or variable in accordance with fluctuations in a single reference rate, in their loan contracts. Consequently, commercial banks cannot make the interest rate applicable to their credit transactions the highest of several reference rates.

TIIE is the only reference rate commercial banks can use for local currency-denominated loans; the primary CETES rate, the CPP that Banco de México publishes in the Official Federal Gazette or the rate that Nafin publishes in the Gazette can only be used for loans subject to a discount with Nacional Financiera, S.N.C., or granted with the funds of that development bank. In the case of loans denominated in UDIS, the CPP-UDIS published by Banco de México in the Official Federal Gazette and US dollar denominated loans, the LIBOR rate or the rate agreed on for instruments that document loans from foreign or international financial entities can only be used for loans granted using the funds of such entities.

In the event that banks agree to an interest rate based on a reference rate, they must also agree that said reference rate be the last one published during the period agreed on for determining the interest rate, or the one resulting from the arithmetic average of such rates published during the reference period.

The only way in which banks can agree to one or more substitute reference rates is if the originally agreed upon reference rate no longer exists. In order to give banks time to prepare the documents required to comply with the regime and make the corresponding adjustments to their systems, Banco de México stipulated that the regime would come into effect on January 2nd, 1996.

Interactive Securities System (SIDV)

At the end of 1995 a scheme for payment against government and bank securities was implemented. S.D. Indeval, S.A. de C.V. (Indeval) will play a vital role in this scheme and so all bank and government securities placed in the market through a public offering and securities market intermediation must at all times be deposited with this securities deposit institution; in the case of government securities, however, Indeval maintains a centralized deposit with Banco de México.

All proprietary or third party transactions undertaken by banks and brokerage firms involving bank and government securities must take place through transfers made by Indeval in accordance with its internal regulations. These transfers will be evidenced by the debits and credits that Indeval delivers to such financial intermediaries.

In order to operate this payment against delivery mechanism, a procedure was established under which on a daily basis Banco de México will determine the maximum negative balance of each bank's single account in relation to the settlement of their bank and government securities transactions in Indeval.

Commercial banks and Nacional Financiera, S.N.C. may request authorization from the Central Bank to grant credit lines they are willing to grant during the next working day to one or more brokerage firms so they settle it against the control account maintained with Indeval. Banco de México will inform them whether their maximum capacity will be increased in order to grant the requested loan. This loan will be granted through repo transactions in which the bank will act as a buyer, and the brokerage house as seller; the repo term will be a working day and the price will be the guarantee value of the bank and government securities the repo.

Banks were allowed to act as buyers to acquire bank securities issued by them as long as such acquisitions were made in accordance with repo transactions entered into under the terms of the previous paragraph.

The maximum capacity that Banco de México grants to banks can be increased up to the amount required to settle the government securities assigned to banks in the primary market.

Commercial banks must guarantee punctual payment of the single account negative balance in relation to the settlement of bank and government securities in Indeval by granting an irrevocable mandate to the institution so that in the event of the guarantees not having been created by 17:50 hours on the day the single account's negative balance is incurred, Indeval creates a guarantee in favor of Banco de México.

Meanwhile Government Securities Placement Rules established that delivery of the assigned securities would take place through Indeval with Banco de México depositing the assigned securities in Indeval's bidder accounts.

The previously established payment procedure was modified such that brokerage firms and banks must pay for the securities in accordance with Indeval's Internal Regulations and other persons must pay for such securities through a bank or brokerage house.

Guarantees granted to Banco de México

The range of securities commercial banks can use to guarantee obligations drawn on them in favor of Banco de México was broadened to include Federal Treasury Certificates issued under investment unit loan restructuring programs (SPECIAL CETES).

Furthermore, in December 1995, it was established that commercial banks may guarantee negotiable instruments deposited with Indeval drawn on them

or development banks announced by Banco de México through the Guarantees Administration System (SAGA) of SIAC-BANXICO, and negotiable instruments issued by FOBAPROA backed by the Federal Government as solidary debtor.

In order to create such guarantees a contract was signed with commercial banks to establish the procedure for creating, replacing and cancelling such guarantees. Negotiable instruments or securities pledged as guarantees are valued in accordance with a Banco de México procedure. There is also a guarantees composition index which varies if the guaranteed obligation is derived from single account overdrafts or loans Banco de México grants through auctions.

Commercial banks must provide guarantees for the overdrafts incurred in their single accounts and loans assigned through auctions. Development banks must only guarantee loans assigned to them through auctions.

Extended Use Electronic Payments System (SPEUA)

In March 1995, the Extended Use Electronic Payment System (SPEUA) was established. This system permits large value payments with a same day value date between the accountholders of different banks.

The aim of SPEUA was to replace large value checks and thereby reduce the credit risk run by Banco de México, banks and the general public as well as lessen systemic risks.

Given diverse modifications to the system a second Circular was issued at the end of November 1995 which compiled the SPEUA modifications in a single document, and lowered the minimum amount of orders that can be processed through this payment system.

SPEUA operates through payment orders a bank sends to another bank to pay a certain sum in local currency to the beneficiary indicated in the order. Anyone wishing to request a payment order must be an accountholder of the bank, have enough funds in their account and request a transfer for at least \$150,000.00. The payment order beneficiary must be the participating bank or an accountholder with a demand deposit with or without a checkbook.

In order to prevent banks from running excessive risks, each day when SPEUA opens, the participating bank must establish a local currency risk exposure applicable to that day vis a vis all other participants'.

Both the risk exposure limit determined by each participating bank in relation to the other banks and the sum of all of the risk exposure limits have maximum limits. Even so each day Banco de México calculates the Maximum Debt Limit corresponding to each participating bank, which is the lower amount of the sum of all risk exposure limits that other participants' have established or the amount that Banco de México in particular establishes based on the bank's liquidity and financial health.

Banco de México automatically performs and continues the clearing calculations of reciprocal obligations drawn on one bank with respect to another derived from the payment orders that both participants' send each other through SPEUA in order to obtain the bilateral net balance. Based on this Banco de México determines the net amount payable or receivable for

each participating bank by deducting: a) the sum of the bilateral net balances drawn on a participating bank from; b) the sum of the bilateral net balances it holds in its favor. The result is the multilateral net balance of that participating bank.

At the end of the day, the debtor participating bank must pay the multilateral net balance drawn on it. For this purpose Banco de México makes the corresponding settlement through SIAC-BANXICO in the form of debits and credits to participants' single accounts.

Credit Support Programs

During 1995 multiple Credit Support Programs were agreed by the Federal Government and banks and other financial intermediaries in order to lessen the growing problem of their past due loans which enabled them to restructure loans granted in local currency and US dollars in UDIS, lower the interest rate charged on such loans, extend the loan maturity and sometimes defer payment of the principal for reasonable periods of time.

Each of these Programs was the result of an agreement between the Federal Government through the Ministry of Finance and Public Credit and commercial banks represented by the Mexican Bankers' Association, Asociación de Banqueros de México, A.C. and sometimes several or all of the development banks. The Ministry subsequently established terms and conditions for the basic credit line granted to participants to make implementation possible as well as the general operating rules they must observe. Banco de México informs banks of these operating rules through Circulars-Telefax and as Federal Government agent is responsible for managing the respective credit lines. The National Banking and Securities Commission informs banks of the accounting rules they must follow.

Each Program establishes the type of loan that can be restructured according to the sector support was granted to as well as the loan amounts, age and characteristics of eligible loans and other requirements to be eligible under the Program.

Banks must select loans that could be eligible under the Programs and negotiate their restructuring with the respective clients in accordance with the maturity options and real interest rate plus a certain number of maximum points indicated in the agreement.

Banks transfer the restructured loan portfolio (the Portfolio) to trusts created especially for that purpose in exchange for the simultaneous payment of its value minus the corresponding loan loss provisions percentage under the Program.

To pay for the Portfolio the trust exercises the Federal Government's basic credit line. With the proceeds from the payment of the Portfolio banks simultaneously acquire long-term SPECIAL CETES.

The following Programs were issued in 1995

Programs: Credit Support Programs for the National Production Apparatus.

Restructuring of US dollar denominated loans under the Credit Support Program for

the National Production Apparatus.

Credit Support Program for States and Municipalities.

Mortgage debtors Support Program.

FOVI Type Entry Level Housing Program.

Support Program for Housing under Construction.

Support Program for Credit Card debtors.

Support Program for Debtors of Loans taken out to acquire Consumer Durable and Personal Goods.

Support Program for the National Production Apparatus through the Restructuring of Rediscount Operations between Commercial Banks and Development Banks.

Support Program for the National Production Apparatus through the Restructuring of Tier 1 loans.

Bank Debtors Support Agreement.

This latter Program known by the acronym "ADE", is an agreement that complements extant UDIS restructuring programs. Its main objective is to grant priority financial support to medium-sized and small debtors of: 1) credit cards; 2) loans for the acquisition of durable and personal goods; 3) mortgage loans; 4) business loans, and 5) agriculture and cattle breeding loans.

The term of the original application of this agreement is 12 months with the exception of loans to the agriculture and cattle breeding sector in which case it is 18 months. If it deems appropriate the Ministry of Finance and Public Credit can extend these terms. As a general rule these terms took effect on September 1st, 1995.

In order to be eligible for the benefits of ADE you must be up-to-date with your loan payment or have signed a letter of intent before January 31st, 1996 expressing the debtor's wish to bring the payments up to date as well as to restructure the debt in UDIS.

Securities Lending

Given that securities lending boosts the liquidity of the market for them and the number of defaults occurring in securities deposit institutions are reduced, in the middle of March Banco de México allowed banks, brokerage firms and equity and debt mutual funds to undertake securities lending transactions.

Securities lending consists of the transfer of securities ownership from the owner, known as the lender, to the borrower, who in turns commits to returning at the end of the established period, more securities of the same issuer either in their nominal value, kind, class, series or maturity date to the

lender in return for the loan, and to reimburse the proceeds from the economic rights the securities may have generated during the term of the contract.

Banks and brokerage firms were allowed to enter into securities lending transactions. Securities acquired by banks should not be subscribed by the same institution.

Securities that can be used in such transactions are government securities, bank instruments and stock, except when securities lending is entered into by banks, which may not use stock for securities lending purposes.

The parties may freely decide the lending term, which may not exceed 360 days and may be extended as long as each extension does not exceed the aforementioned period.

Securities that are lent must be guaranteed by the borrower unless it is a bank. The guarantee can be in cash, securities, or an irrevocable letter of credit issued by a bank. The guarantee administrator is called guarantee custodian and can be a brokerage firm, bank or the securities deposit institution the parties choose as long as it is not a borrower in the transaction. Once the borrower returns the securities to the lender the guarantees are released.

Bank Credit Card Issuance and Operating Rules

In order to give the general public more guidelines about the benefits and effective cost of the financing they receive from the use of bank credit cards, and include other measures that benefit debtors by increasing transparency and information about the implied financial cost of using them, on December 18th, 1995, Banco de México published the rules that commercial banks must adhere to when issuing and operating credit cards.

The rules instruct banks to agree on one interest rate which can be fixed or change based on fluctuations in the reference rate in new credit contracts. Consequently, banks may not agree that the interest rate applicable in such transactions can be the higher of several reference rates.

Banks and their borrowers will agree on the applicable interest rate; however, only an ordinary interest rate may be agreed on and in the event a past due interest rate; the interest rate must be expressed in accordance with one of the following three options: a) fixed percentage points and/or fractions thereof; b) fixed percentage points and/or fractions added to the reference rate chosen from among the following rates: i) the interbank equilibrium rate (TIIE), ii) the rate of return in the primary CETES auction, iii) the CPP published by Banco de México in the Official Federal Gazette, or c) by establishing the minimum and maximum number of percentage points that may be added to one of the reference rates within which range the applicable interest rate is adjusted either up or down by adding the percentage points or fractions thereof obtained by applying the percentage agreed to with clients to the reference rate to the reference rate used.

Institutions were not allowed to modify the terms and conditions of new credit contracts during their term –which may not be below one year– with the exception of the extension of the credit limit, which can be unilaterally

lowered by the bank or extended by a percentage not exceeding the increase in the National Consumer Price Index that Banco de México publishes in the Official Federal Gazette without requiring the borrower's consent.

It was stipulated that banks must take out insurance to cover risks derived from credit card loss or theft or assume them directly as well as one to cover the payment of existing balances following the borrower's death up to the agreed limit or else forgive them.

Banks may only deliver credit cards the applicant has applied for and they must be delivered to the main holder or to a person at the cardholder's domicile who identifies themselves; they must not be sent by mail unless in the bank's systems the possibility of using delivered cards is contingent on the user requesting it through electronic devices, by telephone or directly at bank branches.

Banks were allowed to continue to use previous credit application forms but when the card is sent to the user a document should be included establishing the new contract conditions resulting from said modifications.

Average percentile cost of Investment Unit denominated transactions

In November 1995, Banco de México published a resolution initiating the monthly estimate of the average percentile cost of deposits which all of the country's commercial banks must make in relation to the interest rate on UDIS-denominated debt with the exception of those derived from subordinated debentures convertible into securities representing banks' capital stock, the granting of guarantees, and interbank transactions.

It was determined that Banco de México would begin to announce the reference rate as of November in the Official Federal Gazette between the 21st and the 25th of each month.

Reforms to financial laws

Reforms to Financial Laws published in the Official Federal Gazette on February 15th, 1995.

The aim of these reforms was to strengthen the structure of banks, improve their organization and how they work so they contribute to the execution of local economy stabilization and growth policies.

Consequently it became essential to strengthen the capital stock of entities comprising our financial system by making it easier for those local and foreign investors with the sufficient funds to access to it. As a result, the President decided to promote the modification of the capital stock ownership structure of the controlling companies of financial groups, commercial banks and brokerage firms by allowing Mexican and foreign corporations to have a bigger share in them with the aim of encouraging strategic ventures and thereby raising the efficiency levels of the financial system.

The table below shows the capital stock structure of commercial banks, brokerage firms and stock market, and the controlling companies of financial groups in 1995.

LAW ON CREDIT INSTITUTIONS

| ART. | REGIME APPLICABLE UNTIL FEBRUARY 15 1995 | REGIME APPLICABLE AFTER FEBRUARY 15 1995 |
|-------------|---|--|
| Art. 11 | - The common capital stock was divided into: "A", "B" and | - The common capital stock is divided into: "A", "B" |

| | | |
|---------|--|---|
| | "C" series. | and "C" series. |
| | -Whose percentages were: "A" 51% | - Whose percentages are: "A" 51% |
| | "A" and/or "B" and/or "C" up to 49% "C" up to 30% | "A" and/or "B" 49% |
| | - The additional capital stock was comprised of series "L" shares with a percentage of up to 30% | - The additional capital stock is comprised of series "L" shares with a percentage of up to 40% |
| Art. 13 | <p>Persons eligible to be series "A" shareholders:</p> <ul style="list-style-type: none"> - Mexican individuals and equity mutual funds for Mexican individuals. - The Federal Government, development banks and the Bank Savers Protection Fund (FOBAPROA). - Controlling companies. | <p>Persons eligible to be series "A" shareholders:</p> <ul style="list-style-type: none"> - Mexican individuals - Mexican corporations majority owned by Mexicans and controlled by them. - The Federal Government and FOBAPROA. - Controlling companies. - Institutional investors. |
| Art. 14 | <p>Persons that could be series "B" shareholders.</p> <ul style="list-style-type: none"> - Previously mentioned persons. - Mexican corporations whose bylaws include the direct and indirect foreign investment exclusion clause. - Insurance and surety institutions as an investment of their technical reserves and for variations in securities, mutual funds, pension or retirement funds and other institutional investors. | <p>Series "B" and "L" shares are freely subscribed.</p> <p>Foreign corporations with positions of authority may not participate in banks' capital stock.</p> |
| Art. 15 | <p>Persons that could be series "C" and "L" series shareholders.</p> <ul style="list-style-type: none"> - The abovementioned persons. - Other Mexican corporations, and | |

| | | |
|-------------|--|--|
| | - Foreign individuals or corporations that do not exercise positions of authority. | |
| Art. 17 VII | <p>No individual or corporation may individually own more than 5% of the stock.</p> <p>- The Ministry of Finance and Public Credit may authorize a holding of up to 10%.</p> <p>Foreign banks that invest in series "C" stock with the prior permission of the Ministry of Finance and Public Credit may acquire a controlling stake representing 20% of the bank's capital stock.</p> | <p>No individual or corporation may individually own more than 5% of series "A" and "B" stock.</p> <p>- The Ministry of Finance and Public Credit may authorize a holding of up to 20%.</p> <p>Foreign banks and subsidiary holding companies that acquire shares of any series under the Ministry of Finance's program are excluded from the above paragraph.</p> |
| Art. 45-G | <p>- The capital stock of subsidiaries was represented by a "Single" share series.</p> <p>- A foreign bank or a controlling subsidiary had to own at least 99% of a subsidiary's capital stock.</p> | <p>- Subsidiaries' capital stock comprises series "F" and "B" shares in the following percentages: "F" 51% "B" and/or "F" 49%.</p> <p>- Series "F" shares can be acquired by a subsidiary controlling company or by foreign banks.</p> <p>- Series "B" shares will be governed by the pertinent articles under the Law.</p> |

SECURITIES MARKET ACT

| ART. | REGIME APPLICABLE UNTIL FEBRUARY 15 1995 | REGIME APPLICABLE AFTER FEBRUARY 15 1995 |
|---|--|--|
| Art. 17 Sect. II, subparagraph b), second paragraph | -The Ministry of Finance authorized foreign investment, including that of foreign banks, in the capital stock of brokerage firms and securities specialists as long as it does not exceed the whole. | -Repealed section. |

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| | -The foreign individual holding was up to 10% and with Ministry of Finance authorization it could be up to 15% of the capital stock. | |
| Art. 17 Bis | - The capital stock of brokerage firms and securities specialists was divided into a common part and an additional part. The common part was divided into "A" and "B" stock. - The percentages were: "A" 70% "A" and/or "B" up to | - The capital stock of brokerage firms and securities specialists is divided into a common part and an additional part. The common part is divided into "A" and "B" stock and the percentages are: "A" 51% "A" and/or "B" 49%. |
| | - The additional capital stock comprised series "L" shares in a percentage of up to 30%. | - The additional capital stock comprises series "L" shares in a percentage of up to 40%. |
| | People that could be series "A" shareholders: - Mexican individuals or corporations. Persons that could own series "B" and "L" shares: - The abovementioned persons. - Foreign individuals or corporations. | Persons that can be series "A" shareholders: - Mexican individuals and corporations majority owned by Mexican capital and controlled by it. - The Securities Market Support Fund (FAMEVAL) Series "B" and "L" shares are freely subscribed (with the exception of the restrictions mentioned in article 17, section II of this Law). |
| Art. 19 | - The acquisition of the 10% controlling stake or more shares representing the capital stock of a brokerage firm or a securities specialist had to be submitted to the C's authorization. - No individual or corporation could own 15% or more of the stock. | - The acquisition of the controlling stake of 10% or more of the series "A" and "B" shares representing the capital stock of a brokerage firm or a securities specialist must be submitted to their authorization. - No individual or corporation may own more than 20% of the stock. |
| Art. 22 | - Brokerage firms may not issue subordinated debentures. | - Brokerage firms are allowed to issue subordinated debentures convertible into company securities. |

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| <p>Art. 28 BIS 7</p> | <ul style="list-style-type: none"> - The capital stock of subsidiaries comprised of a "Single" share series. - A foreign bank or subsidiary controlling company had to own at least 99% of the subsidiary bank's capital stock. | <ul style="list-style-type: none"> -The capital stock of subsidiaries comprises series "F" and "B" shares with the following percentages: "F" 51% "B" and/or "F" 49%. - Series "F" shares can be acquired by a subsidiary controlling company or by foreign banks. - Series "B" shares will be governed by that set forth for these shares in other articles of the law. |
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LAW FOR THE REGULATION OF FINANCIAL GROUPS

| Art. | REGIME APPLICABLE UNTIL FEBRUARY 15 1995 | REGIME APPLICABLE AFTER FEBRUARY 15 1995 |
|-------------|---|---|
| Art. 18 | <ul style="list-style-type: none"> - Common capital stock was divided into series "A", "B" and "C" shares. | <ul style="list-style-type: none"> - Common capital stock is divided into series "A" and "B" shares. |
| | <ul style="list-style-type: none"> -Whose percentages were: "A" 51% | <ul style="list-style-type: none"> - Whose percentages are: "A" 51%. |
| | <ul style="list-style-type: none"> "A" and/or "B" and/or "C" up to 49%, "C" up to 30% | <ul style="list-style-type: none"> "A" and/or "B" 49%. |
| | <ul style="list-style-type: none"> - The additional capital stock was comprised of series "L" shares in a percentage of up to 30%. | <ul style="list-style-type: none"> The additional capital stock is comprised of series "L" shares with a percentage of up to 40%. |
| | <p>Persons that could be series "A" shareholders:</p> <ul style="list-style-type: none"> - Mexican individuals and equity mutual funds for Mexican individuals. - By FOBAPROA and by FAMEVAL. | <p>Persons that can be series "A" shareholders:</p> <ul style="list-style-type: none"> - Mexican individuals. - Mexican corporations majority owned and controlled by Mexican capital. - FOBAPROA AND FAMEVAL. - Institutional Investors. |
| | <p>Persons that could be series "B" shareholders:</p> <ul style="list-style-type: none"> - The persons indicated | <p>Series "B" and "L" shares.</p> <p>Freely subscribed. Foreign corporations with positions of</p> |

| | | |
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| | <p>above.</p> <ul style="list-style-type: none"> - Mexican corporations whose bylaws include the direct and indirect foreign investment exclusion clause. - Institutional investors. | <p>positions of power cannot participate in the capital stock.</p> |
| | <p>Persons that could be series "C" and "L" shareholders:</p> <ul style="list-style-type: none"> - The previously mentioned persons. - Other Mexicans, and - Foreign individuals or corporations with no positions of power. | |
| Art. 20 | <p>No individual or corporation could individually own more than 5%.</p> <p>The Ministry of Finance could authorize a holding of up to 10%.</p> | <p>No individual or corporation can individually own more than 5% of series "A" and "B" shares.</p> <p>The Ministry of Finance could authorize a holding of up to</p> |
| Art. 27-H | <ul style="list-style-type: none"> - The capital stock of subsidiary controlling companies was comprised of a "Single" share series. - A foreign bank had to own at least 99% of the subsidiary institution's capital stock. | <ul style="list-style-type: none"> - The capital stock of subsidiary controlling companies will be comprised of series "F" and "B" shares with the following percentages: "F" 51% "B" or "F" 49%. - Foreign banks may acquire series "F" shares. - Series "B" stock will be governed that set forth in other articles of the law. |

Financial Law reforms published in the Official Federal Gazette on November 17, 1995

Substantial changes were made to these reforms: The strengthening of the protection of the public's interests; the modification of the share ownership structure of some financial intermediaries as well as the adoption of measures to prevent and combat money laundering.

In view of this diverse reforms were proposed to the Law on Credit Institutions and the Securities Market Act aimed at giving the National Securities and

Banking Commission more powers to efficiently protect the interests of bank and credit user services by allowing the revision of diverse contract models to ensure they did not contain confusing stipulations that did not enable clients to know the scope of the obligations agreed on. Likewise, in order to contribute to a more balanced relationship between banks and their clients, the Commission can resolve claims submitted by bank users.

Furthermore, the Ministry of Finance and Public Credit was empowered to inform financial intermediaries, including officers and employees, of the guidelines, measures and mechanisms required to anticipate and control money laundering.

Finally, reforms were also made to the following laws: General Act on Credit Organizations and Related Activities, the General Act on Mutual Insurance Institutions and Companies, and the Federal Act on Surety Companies to modify their stock ownership structure and thus facilitate access for local and foreign investors. Furthermore, in order to encourage a greater number of strategic alliances between such investors, the share ownership percentage in subsidiaries incorporated as limited purpose financial companies, auxiliary credit organizations and insurance and surety institutions owned directly or indirectly by a foreign bank, was lowered to 51% from 99%.

National Banking and Securities Commission Act

Given the global reform and integration processes our economy has experienced in recent years, the consolidation of a single body with separate functions to those attributable to the National Banking and Securities Commission became necessary, and so in April 1995 the National Banking and Securities Commission Act became law.

The National Banking and Securities Commission amalgamated the functions and powers of the two previously mentioned commissions, and included all financial system institutions with the exception of those corresponding to the insurance and surety sector.

The National Banking and Securities Commission preserved the powers of authority that were previously the domain of oversight committees and complemented them with compulsory preventive and corrective programs or agreements for banks aimed at eliminating financial imbalances that could impact their liquidity, solvency or stability.

It was given the power to decree prudential rules aimed at preserving the liquidity, solvency and stability of intermediaries, such as risk diversification, capitalization, and loan-loss provision rules.

The management of the new devolved body of the Ministry of Finance and Public Credit was conferred on a governance board and chairman.

General Rules for Credit Information Companies

On February 15, 1995, the Official Federal Gazette published the General Rules that Credit Information Companies referred to in article 33 of the Law to Regulate Financial Groups must adhere to.

The purpose of these companies is to provide information services about borrowing and lending with transactions as well as other similar ones undertaken by financial entities.

Credit information companies can only provide their services to users with express written authorization from each of the subjects investigated who prove that they are aware of the nature and scope of the information that will be requested. If a credit information company provides information to users that do not have this authorization, it will be considered a violation of bank secrecy laws.

Authorization to organize and operate such companies is discretionary and falls with the Ministry of Finance and Public Credit after hearing the opinion of Banco de México and the National Banking and Securities Commission.

Credit information companies may exchange or provide information with other similar companies; however, they must adopt the security and control measures that are necessary to prevent the incorrect handling of information.

Annex

PAYMENT SYSTEMS REFORM

Introduction

In 1994 the Central Bank embarked upon a comprehensive reform of the country's payment system. The reform aims to ensure timely, secure and irreversible payments, which are crucial to minimizing the risks intrinsic to the financial transactions undertaken by diverse economic agents as well as to fostering the adequate monetary policy implementation. The guiding principles of the reform as well as its main components were presented in Banco de México's 1994 Financial Report.

In 1995 Banco de México worked closely with financial intermediaries, with banks in particular, to continue implementing the reform and thereby reach the proposed objectives while not obstructing the adequate working of financial market

The Reform in 1995

1. Large Value Payments

With respect to the large value electronic payment system, several activities were undertaken in 1995. As announced in November 1994 by the Central Bank authorities, the Extended Use Electronic Payments System (SPEUA) began operating in March 1995.

The objective of this system was to provide the medium for undertaking immediate large value payments by providing an alternative to the use of checks to settle financial transactions and other large amounts.

Using SPEUA instead of checks is an advantage for agents involved in the payment process, as it makes the collection and payment process more efficient, increases control over funds, guarantees that payments are final and considerably lowers the risk of fraud. It also lowers the risk derived from clearing house check settlement.

From March until August 1995, the system worked between financial intermediaries (banks and brokerage firms). As of September, the clients of these institutions also have access to SPEUA.

SPEUA's operation is based on granting loans to banks through what is known as "risk exposure bilateral credit lines". Establishing these credit lines means the credit risk of interbank electronic transfers that occur in the system mostly impacts participants rather than Banco de México. In order to contain the risk assumed by banks in this system, Banco de México imposed limits on the amount of credit that each SPEUA participant can grant its counterparts.

Table 1 shows the evolution of SPEUA in 1995. It shows an exponential increase in the use of this payment medium since it began reaching, in December, total payments amounting to more than 85 billion pesos through approximately 1,500 transactions daily. These numbers include loan transfers from banks' SPEUA accounts to their current accounts in SIAC-BANXICO and vice-versa. As the table shows, the net transfer amount is equal to one third of total payments. At the end of SPEUA's operation, transactions are settled through SIAC-BANXICO. In other words, the operation's net balances, both debit and credit, are settled in banks' current accounts with Banco de México.

2. Modifications to clearing houses' settlement of payment documents

On September 21, Banco de México issued a provision modifying how SIAC-BANXICO settles the results of clearing house documents. The modification consisted of eliminating the one day retroactivity of the application of debits and credits resulting from the clearing of checks in banks' current account with Banco de México. The new rules came into force on January 4th, 1996.

Prior to the coming into effect of the new rules, banks that submitted a check to the clearing house for collection received payment on the same value date as the one the document was submitted on. This permitted "same day" payment transactions using checks.

The situation described gave rise to a very high risk of fraud while at the same time amounts cleared by the clearing houses became larger, creating a substantial risk for Banco de México and the financial system as a whole. The introduction of SPEUA provided an alternative to the use of the check and enabled the rules to be modified, considerably lowering the risks. Initial numbers corresponding to 1996 show that the amount of documents cleared by clearing houses on a daily basis dropped from approximately 60 billion pesos at the beginning of 1995 to 6 billion in the first week of 1996. And they will decrease further to the extent more large value payments are channeled through SPEUA.

Interestingly, while the number of checks submitted to clearing houses decreased, it was comparatively less than the amount cleared. This reflects how it was large value payments that began to take place through SPEUA, while the check continues to be used for relatively smaller interbank payments and transfers.

3. Modifications to the rules regarding the handling of banks' current accounts with Banco de México

On March 3, 1995, Banco de México issued new rules for handling banks' current accounts.

The regulation established that banks could overdraw on their current accounts with the Central Bank for an amount equal to the government and bank securities pledged to Banco de México. Nevertheless, the Central Bank accepts overdrafts in excess of such guarantees when derived from debits related to the settlement of some special kinds of transactions, such as: clearing house document settlement; SPEUA settlement; the withdrawal of notes from Banco de México safes; the collection of loans Banco de México grants through auctions to those banks, as well as any other obligation owed by a bank to Banco de México. Furthermore, as of April a mechanism was introduced enabling the Central Bank to charge a conventional fine on overdrafts in banks' single accounts that are not guaranteed.

It should be mentioned that these limits and the penalization of overdrafts in bank current accounts with Banco de México gives the Central Bank additional tools for effectively handling monetary policy.

4. Small value electronic payments

Just as SPEUA replaces the check for making large value payments, the Interbank Payment System managed by CECOBAN replaces the check in small value payments that can be programmed in advanced. Companies that use this system can make money transfers swiftly and immediately through electronic payments, thereby lowering the risks associated with using the check. In 1995 Banco de México promoted this payment system and got all banks with a large branch network to participate, so this system may soon be used throughout the country. In 1995 the bases were also laid for this system to begin collection operations.

5. Government and bank securities settlement system

One of the main sources of risk in financial markets in terms of both credit and systemic risk is the settlement of securities transactions. Securities transaction risks derive from the current separation between the delivery of securities and their corresponding payment. The participant that delivers securities without having received the countervalue in pesos runs the risk of being without securities and money. The same situation occurs if securities that have not yet been received are paid for.

Several countries have remedied this situation by adopting a settlement scheme in which the delivery of securities and the corresponding payment occur simultaneously. As part of the payments system reform, el Banco de México included the design and set-up of a scheme of this type. Towards the end of 1994, it was decided that such a scheme known as "delivery vs. payment", will work with government and bank securities within the system managed by S.D. Indeval.

In 1995, the legal framework within which the "delivery versus payment"

practice will take place was established. The appropriate computer systems were developed and the corresponding operating procedures were designed.

It should be pointed out that under this system, Banco de México will cease to manage government securities accounts for financial intermediaries and will only do so for Indeval. Indeval will also manage such accounts on behalf of banks and brokerage houses as well as some other securities holders.

From a systems point of view, the "delivery against payment" system is a complicated system in which Banco de México, Indeval, the Mexican Stock Exchange and all banks and brokerage firms in the financial system participate. The operation of the system is based on credit lines that Banco de México grants to banks and credit lines banks grant to brokerage firms. The exercise of such lines is always backed by the proprietary holdings of intermediary securities such that at the of the day when these lines have to be paid, the credit Banco de México has to grant to cover settlement of this system will be automatically guaranteed. This system will begin to function in 1996.

| TABLE 1 | | | | |
|--|--------------|------------------|-------------------|-------------------|
| SPEUA | | | | |
| AVERAGE DAILY PAYMENT ORDERS ISSUED IN 1995 | | | | |
| PAYMENT ORDER AMOUNT | | | | |
| (million pesos) | | | | |
| MONTH | TOTAL | INTERBANK | SPEUA-SIAC | SIAC-SPEUA |
| MARCH | 19,398 | 13,752 | 4,299 | 1,347 |
| APRIL | 55,844 | 26,115 | 26,276 | 3,453 |
| MAY | 59,515 | 31,289 | 26,968 | 1,258 |
| JUNE | 65,876 | 34,947 | 29,027 | 1,902 |
| JULY | 64,765 | 30,878 | 32,417 | 1,470 |
| AUGUST | 64,822 | 28,977 | 34,067 | 1,778 |
| SEPTEMBER | 68,127 | 38,510 | 27,298 | 2,319 |
| OCTOBER | 73,618 | 42,506 | 29,246 | 1,866 |
| NOVEMBER | 82,613 | 47,623 | 30,192 | 4,798 |
| DECEMBER | 85,116 | 50,002 | 30,473 | 4,641 |
| NUMBER OF PAYMENT ORDERS | | | | |
| (in units) | | | | |
| MONTH | TOTAL | INTERBANK | SPEUA-SIAC | SIAC-SPEUA |
| MARCH | 316 | 294 | 17 | 5 |
| APRIL | 588 | 527 | 54 | 7 |
| MAY | 631 | 575 | 52 | 4 |
| JUNE | 636 | 579 | 52 | 5 |
| JULY | 676 | 614 | 57 | 5 |
| AUGUST | 710 | 645 | 60 | 5 |
| SEPTEMBER | 926 | 863 | 55 | 8 |
| OCTOBER | 1,078 | 1,011 | 59 | 8 |
| NOVEMBER | 1,202 | 1,134 | 57 | 11 |
| DECEMBER | 1,543 | 1,473 | 57 | 13 |