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Searching for Stability: Mexico's 1995 Banking System Reforms

Christopher R. Rowley*

I. Introduction.

In the last two decades, Mexico's banking system has undergone tremendous structural changes. Initially, in the 1970s and early 1980s, the system transformed from a system of large, independent banks to a system experiencing increased governmental control, culminating in the nationalization of Mexican banks in 1982. Later, in the early 1990s, the system changed from a nationalized but noncompetitive system to a privatized but internationally isolated system. Finally, in 1994 and 1995, the system became substantially open to foreign competition. These changes at times have severely strained the soundness and stability of Mexico's banking system.

The financial crisis triggered by Mexico's poorly-maintained fiscal, monetary, and exchange rate policies in late 1994 forced Mexico to address the chronic weaknesses that had developed in its banking system during the course of the various structural changes. In early 1995, Mexico began implementing policies designed to reverse its deeply-rooted systemic problems: inadequate capitalization; poor asset quality; chronic inefficiency due to lack of competition; and insufficient prudential regulation and supervision.

Although such changes always take time, Mexico's efforts finally appear somewhat successful. Mexico's financial system appears to be regaining credibility in the international financial community and Mexico may finally be on the road to a more mature and developed financial system.

This article focuses on Mexico's efforts to regain stability in its banking system following the financial crisis in late 1994. Part II of this article begins with a brief perspective on the historic development of the Mexican banking system, which is necessary to understand the roots of the system's systemic problems. Part III surveys the provisions of NAFTA regarding financial services and the agreement's impact on the Mexican banking system. NAFTA marked the beginning of foreign competition into Mexico and a general optimism toward Mexico's economic future. Part IV discusses the roots of the 1994 financial crisis, and Part V explains how the financial crisis further weakened the banking system. Finally, Part VI explores in depth the legal reforms and stabilization programs implemented by Mexico immediately following the 1994 financial crisis. These measures include the lifting of limits on foreign participation in the Mexican banking system, special programs to improve bank capitalization and asset quality, and enhancement of the prudential regulation and supervision of the Mexican banking system by Mexican authorities. The approval, by the United States Federal Reserve Board of the Mexican financial group Grupo Financiero Banamex Accival, to operate in the United States demonstrates at least the partial success of Mexico's stabilization efforts.

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II. Historical Perspective on Mexican Banking System.

Mexico's movement to a more open and efficient banking system has followed an arduous path. A brief overview of the historical forces which have shaped the Mexican banking system allows one to appreciate the significant advances made by Mexico in recent years.

Mexico's banking system originally developed from large, family-owned businesses in the late 1800s. Despite increasing government control over the Mexican economy, which was intended to ease the country's developing foreign debt problem, these powerful business and family interests controlled the banking system into the 1970s. This system of control was a problem caused by "[e]xcessive government spending, unrestrained lending by international financial institutions, softened demand for petroleum, worldwide recession, and substantial appreciation of the U.S. dollar" all of which "increased Mexico's largely dollar denominated foreign debt to an unbearable level." By 1982, when Mexico faced its first year of real economic decline since 1932, the Mexican Government perceived the control of Mexican banks by Mexico's largest businesses to be an obstacle to necessary government control over the Mexican economy. Unable to pay its foreign debt and deep in economic crisis, Mexico, under the leadership of President López-Portillo, nationalized its banks in September 1982.

A. NATIONALIZATION.

Mexico legitimated the nationalization of its banks by amending its constitution to decree financial services to be public services which only the Mexican Government could provide. Mexico expected the nationalization to prevent the flight of foreign capital, thus preserving the access to capital essential for economic growth. The opposite result occurred, however, as foreign capital continued to disappear and the government, burdened by debt, became the primary domestic borrower, which had the effect of crowding

2. See id. at 385 (citing Ewell E. Murphy, Jr., Expropriation and Aftermath: The Prospects for Foreign Enterprise in the Mexico of Miguel de la Madrid, 18 Tex. Int'l L.J. 431, 440 (1983); White, supra note 1, at 71-89).
5. See Nalda, supra note 1, at 384 (citing Murphy, supra note 2, at 441; White, supra note 1, at 71 89).
6. See Gruben & Welch, supra note 4, at 64; Nalda supra note 1, at 385 (citing Decreto que Establish la Nacionalizacion de la Banca Privada, D.O., Sept. 1, 1982 (Mex.)).
7. See Gruben & Welch, supra note 4, at 64; Nalda, supra note 1, at 385.
8. See Gruben & Welch, supra note 4, at 64; Nalda, supra note 1, at 386.
out private domestic borrowers.9 Mexico's banking industry faced serious problems, not
the least of which was "regulatory laxity."10

B. PRIVATIZATION.

Full scale nationalization of Mexico's financial sector endured only a short time. In
1982, newly elected President Miguel de la Madrid began, almost immediately, the partial
privatization of Mexican banks. In December 1984, Miguel de la Madrid authorized the
sale of stock that represented thirty-four percent ownership of Mexican bank assets.11 The
stock, denominated "Series B" shares, was available to the Mexican government, govern-
ment entities, Mexican bank workers, and Mexican bank customers;12 the Mexican gov-
ernment itself retained stock denominated "Series A" shares, representing sixty-six percent
ownership of Mexican bank assets.13 Mexican law prohibited foreign investors from
acquiring Series B shares.14 Miguel de la Madrid continued this partial privatization in
1984 when he began the sale of non-bank financial institutions, as well as bank property
not associated with traditional deposit and lending functions.15 This sale marked a tempo-
rary movement away from the universal banking system that had developed in Mexico
prior to the 1982 nationalization.16

In December 1988, Carlos Salinas de Gortari succeeded Miguel de la Madrid as
President. Salinas brought with him a plan for comprehensive economic reforms designed
to make the Mexican economy "more open, efficient and competitive."17 Among the prior-
ity reforms of Salinas were the privatization and promotion of foreign investment in the
Mexican banking industry.18 In accordance with the Salinas' plan, Mexico amended its
constitution in 1990 to allow the full privatization of its banking industry.19

The laws implementing Mexican bank privatization permitted foreign minority par-
ticipation in Mexican banks.20 The new bank ownership regime created three types of
stock in Mexican banks which could be exchanged for existing shares: Series A shares,
Series B shares, and Series C shares. Series A shares represented fifty-one percent owner-
ship in a Mexican bank, and could be held only by Mexican nationals and financial hold-
ing companies. Series B shares could represent a maximum of forty-nine percent owner-
sip and could be held only by Mexican nationals, Mexican financial holding companies,
and Mexican private corporations. Series C shares could represent a maximum of thirty

9. See Gruben & Welch, supra note 4, at 64-65.
10. See id. at 64.
11. See Nalda, supra note 1, at 387 (citing Ley Reglamentaria del Servicio Publico de Banca y Credito,
D.O., Dec. 31, 1982 (Mex.).
12. See id. at 387, n.63.
13. See id.
14. See id. at 387.
15. See Gruben & Welch, supra note 4, at 65.
16. See id. at 65-66.
17. GAO, Mexico's Financial Crisis: Origins, Awareness, Assistance, and Initial Efforts to Recover,
Doc. No. GGD-96-56, at 31 (Feb. 1996) [hereinafter Mexico's Financial Crisis].
18. See Nalda, supra note 1, at 390.
19. See Gruben & Welch, supra note 4, at 65.
20. See Nalda, supra note 1, at 390 (citing Decreto, D.O., Dec. 27, 1989 (Mex.).
percent ownership and could be held by foreign investors. Mexican law also limited foreign participation on the board of directors of a Mexican corporation, thus undesirably (from a foreign investor’s perspective) restricting a foreign investor’s participation in a Mexican bank’s management decisions.

The sale of Mexico’s eighteen nationalized banks to private owners was extraordinarily successful. This sale raised $12.4 billion by its completion in July 1992. The proceeds were used by the government to reduce the debt remaining from the economic crises of the 1980s. The salient feature of Mexico’s newly privatized banking industry, however, was a lack of competition. Market power was heavily concentrated in only twenty Mexican banks, three of which held three-fifths of all Mexican bank assets. Market penetration was very low. Mexico had only one branch bank per every 18,000 people while the United States had one branch bank per every 4,000 people. Although Mexican bank profits were quite high, due to loan interest rates that were significantly higher than the cost of funds, the efficiency of Mexican banks was chronically low.

The prospect of increased competition, however, lit the horizon. In 1993, Mexico further opened its banking industry by permitting the charter of new domestic banks. This action spawned seventeen new banks by 1994. More market entrants followed in 1994 after the opening of the Mexican banking system to foreign banks, as required by the North American Free Trade Agreement (NAFTA or the “agreement”).

III. NAFTA Liberalization of Financial Services.

NAFTA, negotiated between Canada, Mexico, and the United States, took effect on January 1, 1994. The primary practical achievement of NAFTA in the area of financial services was to secure an agreement from Mexico to gradually open its financial services market to foreign participation; a market which had been closed to significant foreign participation for over fifty years.
A. GENERAL OVERVIEW OF FINANCIAL SERVICES PROVISIONS.

Summarizing the most important provisions of the complicated agreement, NAFTA requires the three countries to adhere to the national treatment and most-favored-nation treatment principles when imposing laws or regulations on foreign financial service firms. The agreement also, in a broad sense, requires the countries to ensure market access and transparency of regulation, and permit certain trade in cross-border financial services. The agreement is subject to various reservations (provisions by a member country preserving existing laws or regulations not conforming with NAFTA requirements) and exclusions (provisions allowing for future actions inconsistent with NAFTA requirements) by each of the NAFTA countries. The most important exclusion permitted to each NAFTA country is the prudential "carve-out." This concept is an arrangement permitting future actions inconsistent with NAFTA requirements that are implemented for safety and soundness (or prudential) regulation, for regulation of monetary and credit policy, or for regulation of exchange rate policies.

B. TREATMENT OF MEXICAN FINANCIAL SERVICES.

Under NAFTA, foreign investors may establish a subsidiary (as opposed to a direct branch) in Mexico by acquiring an existing, chartered Mexican financial institution or by applying to establish their own chartered Mexican financial institution. Once a foreign investor establishes such a subsidiary, the investor may form a Mexican group holding company that is capable of establishing or acquiring other Mexican companies engaged in providing financial services. Through its group holding company, a foreign investor may expand its business to provide any financial service that a domestic Mexican investor could provide under Mexican law. Such financial services include

31. North American Free Trade Agreement, drafted Dec. 17, 1992, revised Sept. 6, 1992, Can.-Mex.-U.S., 32 I.L.M. 605 (entered into force Jan. 1, 1994) [hereinafter NAFTA]; see generally Bachman, supra note 30 (a comprehensive discussion of the NAFTA financial services provisions). NAFTA applies to a variety of financial entities which are precisely defined in the Agreement, including "financial institution[s]," "financial service provider[s]," and "investor[s]." See NAFTA, art. 1416, 32 I.L.M. at 661. Banking institutions, which are the primary focus of this article, fall under the NAFTA definition of "financial institution" - an entity "authorized to do business and regulated or supervised as a financial institution under the laws of the party in whose territory it is located." Id. A "financial service provider," on the other hand, is an entity "engaged in the business of providing a financial service" whether or not the financial service is regulated or supervised. Id.; Bachman, supra note 30, at 293. An "investor" is any person or entity (public or private) "that seeks to make, makes, or has made an investment"—an "investment" being essentially "any interest in an enterprise that entitles the owner to share in income or profits of the enterprise." NAFTA, arts. 1139 32 I.L.M. 647, 1416 32 I.L.M. 661. The terms in this article are used generally, and the provisions of the Agreement should be consulted when determining their applicability.

32. See Bachman, supra note 30, at 292.
34. See id. art. 1410 32 I.L.M. at 659.
35. See id. annex VII(B)-Mex. 32 I.L.M. at 769; see generally Bachman, supra note 30, at 305 (discussing establishment of financial institution subsidiaries in Mexico).
37. See id.
banking, securities, insurance, factoring, leasing, bonding, and warehousing.\textsuperscript{38}

Mexico's reservations require that foreign investors requesting entrance to the Mexican market to have previously provided similar financial services in the foreign investor's home country.\textsuperscript{39} Mexico also reserved the right to prohibit foreign investors from owning more than one Mexican financial institution of each type, as well as the right to require a foreign investor to wholly-own any financial institutions which it establishes or acquires in Mexico (other than an insurance company).\textsuperscript{40}

C. GRADUAL FOREIGN ACCESS TO MEXICO: FOREIGN PARTICIPATION LIMITS.

Although NAFTA achieved significantly greater access to the Mexican financial services market, Mexico, in an attempt to protect its newly privatized banking industry from intense international competition, drafted its reservations to the Agreement to ensure that increased foreign access would occur gradually. Most importantly, Mexico's reservations provide that access to the Mexican market will be phased in over a six year period between January 1, 1994 and January 1, 2000 for banking, securities, and insurance services.\textsuperscript{41} The agreement achieves this gradual access with capital and asset limits imposed on foreign financial firms. For both individual foreign firms and for the aggregate of all foreign firms within certain categories of financial institutions (i.e., banking, securities, or insurance), the Mexican reservation limits the amount of capital or assets that a foreign firm may hold as a percentage of the total capital of all financial institutions of that category in Mexico.\textsuperscript{42}

The aggregate capital limit for banks owned by foreign investors began at eight percent in 1994, with the limit increasing to fifteen percent in 1999.\textsuperscript{43} The individual institution capital limit is 1.5 percent throughout the period.\textsuperscript{44} Additionally, a foreign investor may not acquire a Mexican bank if the capital of the acquired bank and any other Mexican banks owned by the acquiror would exceed four percent of the aggregate capital of all Mexican banks.\textsuperscript{45} There is also a provision that permits Mexico to extend or freeze the aggregate capital limit for all foreign owned banks, in certain circumstances, for up to three years until the year 2004.\textsuperscript{46} If at any time, the aggregate capital of all foreign owned banks in Mexico exceeds twenty-five percent of the aggregate capital of all banks in Mexico, Mexico may require consultations with the United States and Canada to discuss the need for appropriate action.\textsuperscript{47}

The limits apply in a similar fashion to securities and insurance firms owned by foreign investors. The aggregate capital limit for securities firms owned by foreign investors

\textsuperscript{38} See id. annex VII(5)-Mex., 32 I.L.M. at 770.

\textsuperscript{39} See id. annex VII(B)(14)-(a)-Mex., 32 I.L.M. at 770.

\textsuperscript{40} See id. annex VII(B)(14)-(b)-Mex., (B)(12)-Mex., 32 I.L.M. at 770.

\textsuperscript{41} See id. annex VII(B)-Mex., 32 I.L.M. at 770.

\textsuperscript{42} See id. annex VII(B)(2), (5), (6)-Mex., 32 I.L.M. at 770; see generally Bachman, supra note 30, at 307.

\textsuperscript{43} See id. annex VII(B)(5)-Mex., 32 I.L.M. at 770.

\textsuperscript{44} See id. annex VII(B)(2)-Mex., 32 I.L.M. at 770.

\textsuperscript{45} See id. annex VII(B)(13)-Mex., 32 I.L.M. at 770.

\textsuperscript{46} See id.

\textsuperscript{47} See id. annex 1413.6(B) 32 I.L.M. at 662, VII(B)(9) 32 I.L.M. at 770, (C)(Definitions)-Mex., 32 I.L.M. at 772.
began at ten percent, and will increase to twenty percent by 1999. The individual institution capital limit for securities firms is four percent. The aggregate capital limit for insurance firms owned by foreign investors began at six percent and will increase to twelve percent by 1999. The individual institution capital limit for insurance companies is 1.5 percent.

D. ENTRY OF FOREIGN FINANCIAL FIRMS INTO MEXICO.

Shortly after the effective date of NAFTA, large numbers of foreign banks applied for permission to enter the Mexican financial services market. By August 1994, Mexico had received applications from 102 foreign financial services providers; it formally approved fifty-four financial services providers to begin operations in Mexico on October 17, 1994. Although Mexico was one of the most underbanked economies in the world and "desperately in need of more financial services," the individual and aggregate capital limits imposed by NAFTA limited what might have been greater direct foreign investment by preventing most foreign banks from pursuing retail banking in Mexico, potentially a very profitable business. Instead, the firms generally intended to focus on more sophisticated financial services where they held clear competitive advantages.

IV. Mexico's 1994 Financial Crisis.

In December 1994, eleven months after the implementation of NAFTA, Mexico plunged into a severe financial crisis caused by complex financial, economic, and political forces. The financial crisis forced Mexico to implement unanticipated measures in an attempt to stabilize the country's banking system.

Although the roots of the financial crisis are complicated, they are worth exploring briefly. In early 1994, buoyed by general approval of NAFTA, foreign investor's perceived

49. See id. annex VII(B)(2)-Mex., 32 I.L.M. at 770.
50. See id. annex VII(B)(6)-Mex., 32 I.L.M. at 770.
51. See id. annex VII(B)(2)-Mex., 32 I.L.M. at 770.
52. See More than 100 Financial Companies Have Applied to do Business in Mexico, BANKING DAILY (BNA) (Aug. 10, 1994) [hereinafter Business in Mexico]; Fifty-Four Foreign Financial Firm Applications Are Approved by Mexico, BANKING DAILY (BNA) (Oct. 20, 1994) [hereinafter Firm Applications].
53. See Business in Mexico, supra note 52.
55. See Mexico Fires the Starting Gun, supra note 54.
the Mexican economy as "fundamentally strong." Accordingly, Mexico experienced a heavy inflow of foreign investment. This inflow of foreign investment, however, substantially consisted of equity and debt portfolio investments that tended to be liquid and relatively short term, all of which were investments capable of being very quickly withdrawn.

This substantial foreign investment allowed Mexico to support a very large deficit in its current accounts. This action was permitted, because Mexico maintained plentiful foreign currency reserves, it experienced rapid growth in exports, and there appeared to be little risk of Mexico not being able to attract and retain foreign investment in the near future. Normally, a country must act to reduce a current account deficit by adjusting its monetary policy, fiscal policy, or its exchange rate system. Mexico could have taken several measures to reduce such a current account deficit, including: (1) attracting more foreign capital; (2) allowing its currency to depreciate, thus making imports more expensive and exports cheaper; (3) tightening monetary and/or fiscal policy to reduce the demand for all goods, including imports; and (4) using foreign exchange reserves to cover the deficit.

In 1994, due partly to this current account deficit, Mexico permitted a "growing inconsistency" between its monetary and fiscal policy and its exchange rate system. This inconsistency would have required Mexico to either raise interest rates or devalue the peso (for which Mexico maintained an exchange rate pegged to the U.S. dollar). Due to its upcoming presidential election, Mexico hesitated to take either of these actions.

Throughout the year, several internal events further complicated Mexico's financial situation, and caused the rapid withdrawal of large amounts of liquid foreign investment from Mexico. First, in March 1994 the assassination of PRI presidential candidate Luis Donaldo Colosio rattled the confidence of foreign investors and triggered a tremendous outflow of foreign capital. Then, in November and December 1994, renewed fighting in the Mexican State of Chiapas and the developing scandal regarding another assassination, that of PRI Secretary General Francisco Ruiz Massieu, triggered a second outflow of foreign capital. Mexico's foreign currency reserves, which are essential to both maintain the peso's dollar-pegged exchange rate and cover the country's current account deficit, quickly began to fall. Mexico took several actions to lessen the outflow of foreign capital, including depreciating the peso, securing a short-term credit agreement with the United States and Canada, and increasing interest rates on short-term, peso-denominated, government debt, called "cetes."
As 1994 progressed, however, investors became increasingly concerned about the possibility of a large currency devaluation necessary to stabilize Mexico’s financial situation. In order to alleviate these concerns, Mexico opted to increase its issuance of short-term, dollar-denominated debt called “tesobonos,” rather than take action which might have dampened Mexico’s economy, such as increasing interest rates, reducing government expenditures, or devaluing the peso. Tesobonos guaranteed an investor’s repayment in pesos sufficient to cover the dollar value of his investment, thus protecting the investor in the event of a devaluation. The issuance of these tesobonos, with short maturities and purchased primarily by portfolio investors willing to switch to other, less risky investments if they perceived a possible default or potential for higher returns, left Mexico’s foreign currency reserves vulnerable in the event of an outflow of foreign capital.

Mexico’s financial situation failed to improve, and it became apparent that Mexico’s financial stability required an adjustment in monetary, fiscal and exchange rate policies. Mexico continued to lose investor confidence and foreign currency reserves when it failed to adopt appropriate monetary, fiscal and exchange rate policies following the renewed fighting in Chiapas and the developing Ruiz Massieu scandal. Circumstances forced Mexico to completely devalue its currency on December 22, 1994. The devaluation resulted in outflows of foreign capital, high inflation, and ultimately, a severe downturn in the Mexican economy.

V. Weakening of the Mexican Banking System.

Mexico’s financial crisis exacerbated weaknesses in Mexico’s banking sector. Mexico’s banks experienced weakness following their privatization under the Salinas administration. First, buyers purchased privatized banks at very high prices, requiring strong future performance for them to remain financially sound. Second, the government, ineffective at evaluating the creditworthiness of borrowers, passed on to buyers serious loan portfolio problems and an ever increasing loan default rate. A perceived strong economy and the tremendous inflow of foreign capital following NAFTA temporarily disguised these problems, as “[t]he problem during a strong economic upturn ... is that the abundance of liquidity masks risky borrowers who would be recognized for what they are in less risky times.”

69. See Mexico’s Financial Crisis, supra note 17, at 10.
70. See id.
71. See id.
72. See Arner, supra note 56, at 54-56; see Mexico’s Financial Crisis, supra note 17, at 10.
73. See Mexico’s Financial Crisis, supra note 17, at 11.
74. See Arner, supra note 56, at 57, Table 18; See Mexico’s Financial Crisis, supra note 17, at 11-12.
75. See Mexico’s Financial Crisis, supra note 17, at 12.
76. See Gruben & McComb, supra note 56, at 27.
77. See Mexico’s Financial Crisis, supra note 17, at 143; Gruben & McComb, supra note 56, at 26.
78. See Mexico’s Financial Crisis, supra note 17, at 143; Gruben & McComb, supra note 56, at 26.
In addition to ineffective evaluation of borrower creditworthiness, there were other regulatory problems in Mexico's banking system. Regulation of Mexico's developing universal banking system was among those problems. The regulation dealt poorly with self-lending among financial groups, making it difficult for regulators to prevent questionable internal lending. Mexico's accounting standards did not provide for consolidated reporting, which might have helped regulators assess possible self-lending. Additionally, Mexico's banks experienced inadequate capitalization levels prior to and following privatization.

With the devaluation of the peso, the outflow of foreign capital, and the ensuing economic downturn, Mexico's banking system faced tremendous stress. First, with the outflow of U.S. dollars, Mexican banks had insufficient dollar liquidity necessary to meet their dollar obligations that created an "immediate dollar liquidity problem." Second, Mexican banks maintained significant dollar-denominated debt, and as the peso continued to decline in value against the dollar, the capitalization levels of Mexican banks also declined. Finally, as Mexico's interest rates rose, so did the already high rate of non-performing loans held by Mexican banks.

VI. Mexico's 1995 Banking Law Reforms and Programs.

To prevent financial collapse, Mexico had to immediately increase the capitalization and improve the asset quality of its banking system. Mexico quickly acted to implement programs, policies, and laws designed to achieve banking system stability. Measures implemented by Mexico included an overhaul of the laws governing foreign participation in its banking system, special government programs to improve bank capitalization and asset quality, and measures to improve the prudential regulation and supervision of its banks.

A. FOREIGN PARTICIPATION.

A large part of Mexico's strategy to infuse new foreign capital into its banking system involved amending its banking laws to permit and encourage increased foreign investment in Mexican banks. Mexico unilaterally amended its Credit Institutions Law (Ley de Instituciones de Credito), its Securities Market Law (Ley del Mercado de Valores), and its Law to Regulate Financial Groups (Ley para Regular las Agrupaciones Financieras) on February 16, 1995 (collectively, the "1995 amendments"), and committed itself to opening its economy. The legislation effectively nullified the foreign capital limitations estab-

80. See id. at 26.
81. See id.
82. See id. at 25-26.
83. Mexico's Financial Crisis, supra note 17, at 143.
84. See id.
85. See id.
87. See Mexican Banking Laws Allow More Foreign Participation, Banking Daily (BNA) (Feb. 1, 1995).
lished in NAFTA and represented a "dramatic change" in Mexico's previous position, since access to Mexico's financial services market had been "one of the most controversial issues in the NAFTA negotiations."  

1. **Foreign Bank Subsidiaries.**

Mexican law, immediately following NAFTA, allowed foreign investment in Mexican banks by two methods: (1) as a subsidiary of a foreign financial institution, and (2) by a minority investment in a Mexican majority-owned bank. For foreign subsidiaries, the individual capital limits, established in NAFTA and adopted as Mexican law, limited the foreign bank subsidiary to 1.5 percent of the total capital of Mexican banks. The aggregate capital limits limited all foreign bank subsidiaries to between eight and fifteen percent of the total capital of Mexican banks. Mexican law also required these foreign subsidiaries to be ninety-nine percent owned by the foreign financial institution.

The 1995 amendments significantly altered these requirements. First, the amendments increased the individual capital limit for subsidiaries to six percent, well above the 1.5 percent limit under NAFTA. This action effectively allowed all but three of Mexico's largest banks (Banco Nacional de Mexico, Bancomer, and Banca Serfin) to be acquired as subsidiaries. Second, the amendments increased the aggregate capital limit to twenty-five percent, well above the maximum limit under NAFTA of fifteen percent. Finally, the amendments abandon the requirement that a foreign financial institution own at least ninety-nine percent of its Mexican subsidiary. Instead, the foreign financial institution's ownership of its Mexican subsidiary can be as low as fifty-one percent—allowing the subsidiary to invite participation of Mexican or other foreign investors at a level of up to forty-nine percent ownership.

The foreign financial institution's ownership of a subsidiary is represented by "Series F" shares, while the remaining ownership (up to forty-nine percent) is represented by "Series B" shares. Individual investors are limited to maximum ownership

88. See id.
89. Id.
90. See Rogers & Zubikarai, supra note 86, at 7.
91. See NAFTA discussion, supra note 31, § III.C.
92. See id.
93. See Rogers & Zubikarai, supra note 86, at 7.
94. See Ley de Instituciones de Credito, supra note 86, art. 17; see also Rogers & Zubikarai, supra note 86, at 7; see William Acworth, Mexican Congress Affirms Open Door Policy, THOMSON'S INT'L BANKING REG., Vol. 7, No. 5, Feb. 6, 1995, at 3.
95. See 1995 Amendments, Articulos Transitorios, Second, supra note 86; see also Rogers & Zubikarai, supra note 86, at 7.
96. See Rogers & Zubikarai, supra note 86, at 7.
97. See Ley de Instituciones de Credito, supra note 86, art. 45-G; see also Rogers & Zubikarai, supra note 86, at 7, 10.
of five percent of Series B shares, with the possibility that regulators may approve up to twenty percent ownership.99

2. Foreign Minority Ownership of Mexican Banks.

For foreign investors making minority investments in Mexican majority-owned banks, prior Mexican law limited such investments to thirty percent of bank ownership.100 The law limited individuals to five percent of bank ownership, with the possibility of regulator approval for up to ten percent ownership.101 This ownership could be represented by either "Series C" shares or special "Series L" shares that had limited voting rights.102

The 1995 amendments significantly altered these foreign minority investment ownership requirements. The amendments increased the percent ownership that could be acquired as a minority investment to forty-nine percent (from thirty percent).103 These minority investments are not subject to any of the capital limits for subsidiaries, either individual or aggregate.104 As under previous law, however, there are individual ownership limits of five percent.105 However, the 1995 amendments extended to twenty percent (from ten percent) the individual ownership limit that may be obtained with regulator approval.106

The amendments eliminate Series C shares (formerly representing foreign ownership of a bank), so that stock of foreign minority investors is now represented by Series B shares. They also allow foreign "institutional investors" to acquire the Mexican-owned majority shares, Series A shares.107 With this arrangement, it is conceivable for foreign investors to obtain some degree of control over a Mexican bank if institutional investors substantially owned Series A shares of the bank combined with individual foreign investors (each holding less than five percent ownership, or twenty percent with regulator approval) owning forty-nine percent.108

98. See Ley de Instituciones de Credito, supra note 86, art. 17; see also Rogers & Zubikarai, supra note 86, at 7.
99. See Ley de Instituciones de Credito, supra note 86, art. 17; see also Rogers & Zubikarai, supra note 86, at 7.
100. See Ley de Instituciones de Credito, supra note 86, arts. 11-17; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 6.
101. See Ley de Instituciones de Credito, supra note 86, arts. 11-17; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 6.
102. See Ley de Instituciones de Credito, supra note 86, arts. 11-17; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 6.
103. See Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 7-8.
104. See Rogers & Zubikarai, supra note 86, at 9.
105. See Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 8.
106. See Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 8.
107. See Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 8.
108. See Ley de Instituciones de Credito, supra note 86, arts. 11-15; see Ley Para Regular Agrupaciones Financieras, supra note 86, arts. 18-20; see also Rogers & Zubikarai, supra note 86, at 8, 10.
3. Corporate Governance Changes.

The 1995 amendments also make several changes relating to corporate governance. First, previous Mexican law allowed foreign subsidiaries to maintain boards consisting of only five directors. Now, however, foreign subsidiaries that opt to own less than ninety-nine percent of their stock must have eleven directors (or a multiple of eleven, i.e., twenty-two, thirty-three, etc.). Additionally, Mexican law previously required that directors representing Series A or Series B shares be Mexican nationals or immigrants residing in Mexico. However, for Series A shares, the new law eliminates the requirement that directors residing in Mexico must have immigrants status, though it retains the requirement that they reside in Mexico. For Series B shares, directors no longer must reside in Mexico, although the legislation retains the requirement that a majority of the directors of any subsidiary must reside in Mexico.

B. SPECIAL PROGRAMS TO IMPROVE BANK CAPITALIZATION AND ASSET QUALITY.

To further address the capitalization and asset quality problems in the Mexican banking system, created by the 1994 financial crisis, the Mexican central bank (Banco de Mexico) and Mexico's bank regulators implemented several innovative and specialized programs. Banking experts generally credit these programs with having initially stabilized the Mexican banking system.

1. Capitalization.

As well as changing its foreign participation limits, Mexico implemented a temporary bank recapitalization program (Programa de Capacitacion Temporal, or PROCAPTE) in February 1995. PROCAPTE is a voluntary recapitalization program for banks whose capitalization levels fall below the capitalization standards of the Basle Accord—eight percent of risk-weighted assets. A bank participating in PROCAPTE issues subordinated con-
vertible debentures which are then purchased by the deposit insurance authority of Mexico's central bank (Fondo Bancario de Proteccion al Ahorro, or FOBOPROA). The bank issues the debentures in an amount sufficient to raise its capitalization to nine percent. Banks participating in PROCAPTE must repay their debt within five years, otherwise FOBOPROA will convert the debt to equity and sell the equity on the private market. There are also provisions allowing FOBOPROA to convert the debt to equity if a bank is poorly managed or is likely to become insolvent.

According to the U.S. General Accounting Office (GAO), six Mexican banks entered the PROPCAPTE program. The banks issued $1 billion in convertible debentures and Mexico's third largest bank, Banca Serfin, left the program in June 1995.

2. Asset Quality.

In early 1995, Mexico took several steps to address the increase in nonperforming loans brought on by the 1994 financial crisis. First, Mexico required banks to maintain higher levels of loan loss reserves as protection against losses from nonperforming loans. New regulations required banks to maintain an amount of loan loss reserves the larger of either sixty percent of all past due loans or four percent of total loan portfolio.

Second, Mexico implemented a loan restructuring program designed to spread over time the impact of current losses from nonperforming loans, increasing the probability that the loans would perform, despite Mexico's high inflation and interest rates. The program allowed banks to restructure certain types of past-due private debt (i.e., commercial loans and mortgages) into quasi-bond instruments which were then purchased by the government. The government then issued special bonds to finance the purchase of the restructured debt from the banks. Finally, the banks repurchased the bonds issued by the government, which were denominated in “Unidades de Inversion” (UDIs)—units indexed to the consumer price index so as to preserve the real value of the principal. The restructuring system also extended the maturity of the loans by allowing loan repayments to be extended and weighted to the end of the loan.

In addition to these programs, Mexico received a $1.7 billion loan from the World Bank to recapitalize FOBOPROA, Mexico's deposit insurance authority, and enable it to purchase assets and effectively resolve failing financial institutions. More importantly to Mexico's ability to maintain high asset quality in the future, the World Bank and other

116. See Mexico's Financial Crisis, supra note 17, at 144; see Gruben & McComb, supra note 56, at 27.
117. See Mexico's Financial Crisis, supra note 17, at 144; see Gruben & McComb, supra note 56, at 27.
118. See Mexico's Financial Crisis, supra note 17, at 144; see Gruben & McComb, supra note 56, at 27.
119. See Gruben & McComb, supra note 56, at 27.
120. See Mexico's Financial Crisis, supra note 17, at 144.
121. See id.
122. See id. at 145.
123. See id.
124. See Gruben & McComb, supra note 56, at 27; Mexico's Financial Crisis, supra note 17, at 145.
125. See Gruben & McComb, supra note 56, at 27.
126. See id.
127. See Mexico's Financial Crisis, supra note 17, at 145; Gruben & McComb, supra note 56, at 27.
128. See Mexico's Financial Crisis, supra note 17, at 145.
129. See id.
international institutions provided Mexico technical assistance on how to improve Mexico's prudential regulation and supervision of its banking system.\textsuperscript{130}

C. PRUDENTIAL REGULATION AND SUPERVISION.


Mexico recognized, following the 1994 financial crisis and the accompanying bank capitalization and asset quality problems, that stabilization of its banking system would require strengthening of the prudential regulation and supervision of its financial sector.\textsuperscript{131} To achieve this goal, Mexico drafted, and in May 1995, enacted legislation merging the National Banking Commission and the National Securities Commission that were previously separate administrative agencies responsible for regulating banking and securities industries.\textsuperscript{132} The new law (\textit{Ley de la Comisión Nacional Bancaria y de Valores}) created the National Banking and Securities Commission (in Spanish, forming the acronym CNBV) to regulate Mexico's financial system.\textsuperscript{133} The primary goal of this merger was to "facilitate the effective supervision of financial groups on a \textit{consolidated basis} by placing the supervisors of Mexico's brokerage houses under the same roof as the supervisors of their bank affiliates."\textsuperscript{134} This approach makes sense given the regulatory problems associated with a universal banking system such as exists in Mexico.

The CNBV's objective is to ensure the stability of Mexico's financial system as indicated by factors such as adequate capitalization, liquidity, reserves and profitability, and by high asset quality and capable management of financial institutions.\textsuperscript{135} The CNBV's \textit{Institutional Program 1997-2000} (Institutional Program) describes in detail the CNBV's agenda for achieving these goals through the use of prudential regulation, supervision, market self-regulation, and corrective actions.\textsuperscript{136}

a. Prudential Regulation.

The Institutional Program recognizes that financial institutions must have "internal control systems"—or prudential regulation—that will limit excessive risk taking during both strong and weak economic periods.\textsuperscript{137} Because of the disjointed development of its financial system, Mexico developed different prudential regulation schemes for its different types of financial institutions.\textsuperscript{138} The Institutional Program strives to develop a uniform system of prudential regulation for Mexico's universal banking system.\textsuperscript{139} This includes

\begin{itemize}
  \item 130. See id.
  \item 132. See id. at 3.
  \item 133. See id.
  \item 134. Karaoglan & Lubrano, supra note 114, at 29 (emphasis added).
  \item 135. See Institutional Program, supra note 131, at 5.
  \item 136. See id. at 5-12.
  \item 137. See id. at 6.
  \item 138. See id.
  \item 139. See id.
\end{itemize}
the development of uniform “norms, procedures and mandatory minimum standards” for
capital adequacy levels, reserves levels, assessment of credit and investment portfolio risk,
accounting principles, and the timely and accurate disclosure of information - in essence,
uniform standards for measuring financial institution performance.\(^{140}\)

For instance, although Mexico’s minimum capital adequacy requirement is eight per-
cent for banks, a level consistent with international standards, Mexico’s capital adequacy
standards previously focused on credit risk, rather than market risks such as interest rate
risk and exchange risk.\(^{141}\) To address this problem, CNBV issued new “Rules for
Capitalization Requirements in Commercial Banking Institutions and Brokerage Houses,”
which now account for those market risks.\(^{142}\) The CNBV plans other changes to Mexico’s
capital adequacy rules as well.

The CNBV has also modernized accounting principles applicable to Mexican financial
institutions, which previously differed depending on the type of financial institution and
in some cases differed from international accounting standards.\(^{143}\) Such differences made
it difficult to assess the consolidated position of Mexican financial institutions as well as
for foreign investors to compare Mexican financial institutions with other financial institu-
tions around the world.\(^{144}\) Mexico now uses international accounting standards and
applies them uniformly to its financial institutions.\(^{145}\)

b. Financial Supervision.

In order to implement the CNBV’s prudential regulation policies, the Institutional
Program recognizes that it must have “methodologies and procedures” for financial super-
vision that will allow CNBV “to verify that the institutions carry out their activities in con-
formity with the rules and regulations and with sound financial practices, to objectively
measure their risks, and [to] evaluate the quality of their internal controls.”\(^{146}\) Again,
Mexico’s developing universal banking system created supervision problems in the past,
however, CNBV has now implemented consolidated supervision that allows for improved
monitoring of both individual institutions and financial groups as a whole.\(^{147}\)

The CNBV has developed a comprehensive “consolidated supervision scheme” called
“MACRO,” consisting of on-site inspections and routine off-site monitoring of financial
institutions.\(^{148}\) The program evaluates a financial institution’s management of funds, capi-
tal adequacy, asset quality, profitability, and organization (in Spanish, forming the
acronym MACRO).\(^{149}\)

\(^{140}\) See id.
\(^{141}\) See id.
\(^{142}\) See id.
\(^{143}\) See id. at 8.
\(^{144}\) See id.
\(^{145}\) See id.
\(^{146}\) See id.
\(^{147}\) See id.
\(^{148}\) See id.
\(^{149}\) See id.
Very significantly, regarding on-site inspections, the CNBV has eliminated the practice of permanently placing inspectors within financial institutions in favor of using groups of inspectors officed outside of financial institutions that carry out regular inspections - a change which makes the inspection process more effective.\textsuperscript{150} The on-site inspectors are responsible for ensuring that financial institutions maintain an "efficient internal control system for risk-management" based on the inspector's first-hand observance of an institution's "operations, procedures, internal controls, management and compliance with regulations."\textsuperscript{151} An institution must maintain manuals establishing clear policies that demonstrate a low tolerance for excessive risk taking, as well as procedures ensuring that an institution's employees comply with these policies.\textsuperscript{152}

The primary focus of the CNBV's off-site inspection is the development of its "Financial Analysis System" (in Spanish, forming the acronym SAF).\textsuperscript{153} The SAF is a computer database which receives financial information directly from financial institutions, eliminating the need for physical delivery of the information that financial institutions must provide the CNBV.\textsuperscript{154} Armed with this consistent and uniform financial information, off-site supervisors are able to create individual, comparative or sectoral analyses of a financial institution's performance and develop "early-warning mechanisms that make it possible to detect in a timely manner any risks that may undermine the institution's financial position."\textsuperscript{155} These techniques, the CNBV predicts, will allow the agency "to detect atypical behaviors, whether individual or systemic, and . . . [address them] before they reach critical levels."\textsuperscript{156}

The Institutional Program contemplates a new structure for the system of internal and external audits which "complement" the supervision of financial institutions by the CNBV.\textsuperscript{157} There has been some trouble with external auditors in Mexico. The Institutional Program recommends that external auditors be registered, that CNBV evaluate their performance and opinions, and impose sanctions if required.\textsuperscript{158} The Institutional Program also recommends that internal auditors should report directly to a financial institution's board of directors, rather than the intermediate management of the institution, and that the CNBV supervise internal auditors by examining the scope and regularity of audits, audit procedures, and the content of internal audit reports.\textsuperscript{159}

Finally, the Institutional Program recognizes the importance of strengthening world confidence in Mexico's financial institutions by providing foreign financial authorities with quality financial information, in international terms, so that those authorities may measure Mexican institution's exposure to risk.\textsuperscript{160} Along this line, the Institutional

\begin{enumerate}
  \item See id. at 9.
  \item See id. at 8-9.
  \item See id. at 9.
  \item See id.
  \item See id.
  \item See id.
  \item See id. at 10.
  \item See id.
  \item See id.
  \item See id.
  \item See id.
  \item See id. at 11.
\end{enumerate}
Program promotes “greater cooperation with foreign authorities and multilateral organizations” such as the International Organization of Securities Regulators, the Latin American and Caribbean Association of Banking Supervisors, and the Basle Committee.\textsuperscript{161}


The Institutional Program recognizes the need to ensure that prudential regulation does not “replace the disciplines and sanctions imposed by the market on [financial institutions] which do not follow sound financial practices or take excessive risks.”\textsuperscript{162} The objective of the Institutional Program is to encourage financial institutions to regulate themselves through “codes of ethics and behavior that are consistent with sound financial practices, and the necessary mechanisms for assuring they are complied with.”\textsuperscript{163} It also encourages the development of non-governmental financial data-compiling institutions, such as credit rating agencies, to help “improve the quality and timeliness of the information and, on the other hand, enable markets and those participating in them . . . to assimilate this information quickly without having to pay a high price for it.”\textsuperscript{164}

In order to correct instances of inappropriate behavior by financial institutions, the CNBV has developed an array of corrective measures including corrective and mandatory compliance programs and, in extreme cases, interventions in the administration and management of financial institutions.\textsuperscript{165} In order to achieve greater compliance, the CNBV intends to revise these measures “to assure that sanctions are such that they really dissuade behavior and actions that are counter to sound financial practices.”\textsuperscript{166}

d. Other Objectives of the CNBV.

The Institutional Program highlights several other objectives in addition to those relating to the stability and solvency of Mexico’s financial system as a whole. Those objectives include: protecting the interests of depositors and investors, fostering improved quality of management among financial institutions, fostering the efficient and sound development of the financial system, and strengthening the CNBV’s institutional development.\textsuperscript{167}

In order to enhance the protection of depositors and investors, the Institutional Program recommends implementing measures improving (1) the extensive, clear and timely disclosure of financial data, (2) the regulation of insider information, (3) the effectiveness of deposit insurance programs, (4) the regulation of conflicts of interest, (5) the sophistication of the general public in its use of financial services, and (6) the attention by financial institutions to the needs of consumers.\textsuperscript{168} The CNBV intends to improve the management quality of Mexican financial institutions by implementing stricter procedures

\textsuperscript{161} See id.

\textsuperscript{162} See id.

\textsuperscript{163} See id.

\textsuperscript{164} See id. at 12.

\textsuperscript{165} See id.

\textsuperscript{166} See id.

\textsuperscript{167} See id. at 2-3.

\textsuperscript{168} See id. at 12-15.
for the authorization of individuals to establish financial institutions and created a corpo-
rate governance scheme that more efficiently limits excessive risk taking.\textsuperscript{169} The agency
hopes to promote a sound and efficient financial system by facilitating (1) the develop-
ment of more and improved savings and financial instruments, (2) the expansion of the
availability of financial resources to a wide base of financial institutions, (3) increased
competition among financial institutions, (4) the restructuring of the financial system in
the wake of the system’s reform, and (5) development of an efficient and speedy judicial
system.\textsuperscript{170} Finally, the CNBV’s own institutional development priorities include: (1)
implementation of a comprehensive planning system, (2) development of a highly special-
ized, technically trained career civil service within the CNBV, and (3) development of
modern information infrastructure systems.\textsuperscript{171}

2. Effect of Prudential Regulation and Supervision Improvements.

Although the CNBV program demonstrates that significant concrete measures have
been taken to improve prudential regulation and supervision in the Mexican banking sys-
tem, much of the program represents mere “goals” which may or may not be actually
achieved. Still, the overhaul of Mexico’s system of financial institution regulation and the
accomplishments and objectives of the CNBV present serious efforts by Mexico to regain
world confidence in its financial institutions. These efforts appear to have born some success.

In September 1996, the U.S. Federal Reserve Board (the Board) approved the applica-
tion of a Mexican financial group, Grupo Financiero Banamex Accival (Banacci), to become
a bank holding company, under the U.S. Bank Holding Company Act,\textsuperscript{172} and to engage in
securities activities including brokerage services, private placement, and riskless principal
activities.\textsuperscript{173} In order to approve Banacci’s application to establish a bank holding company,
the Board had to determine that the foreign bank is subject to comprehensive supervision or
regulation on a consolidated basis by its home country supervisor.\textsuperscript{174} Prior to its decision,
the Board received comments protesting the application and asserting that home country
supervision of Banacci was insufficient to justify the Board’s approval.\textsuperscript{175}

Per Federal Reserve Board regulations, a foreign bank is subject to comprehensive
supervision or regulation on a consolidated basis if “its home country supervisor receives
sufficient information on the foreign bank’s worldwide operations, including its relation-
ship to any affiliate, to assess the foreign bank’s overall financial condition and compliance
with law and regulation.”\textsuperscript{176} Factors considered by the Board include the extent to which

\textsuperscript{169} See id. at 16-17.  
\textsuperscript{170} See id. at 16-18.  
\textsuperscript{171} See id. at 18-20.  
\textsuperscript{173} See Federal Reserve Board, Order Approving the Formation of a Bank Holding Company and a
Proposal to Engage in Certain Securities Activities, Grupo Financiero Banamex Accival, S.A. de
C.V., Mexico City, Mexico, et al. (Sept. 9, 1996) [hereinafter Banacci Order].  
\textsuperscript{174} This determination is required by the Bank Holding Company Act, 12 U.S.C. § 1842(c)(3)(B)
\textsuperscript{175} See Banacci Order, supra note 173, at n.5.  
\textsuperscript{176} Id. at 3.
the home country supervisor: (i) ensures that the foreign bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtains information on the condition of the foreign bank and its subsidiaries and offices outside the home country through regular reports of examination, audit reports, or otherwise; (iii) obtains information on the dealings and relationships between the foreign bank and its affiliates, both foreign and domestic; (iv) receives from the foreign bank financial reports that are consolidated on a worldwide basis, or comparable information that permits analysis of the foreign bank’s financial condition on a worldwide, consolidated basis; and (v) evaluates prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. Based on its evaluation of these factors, the Board concluded that Banacci was subject to comprehensive supervision on a consolidated basis by Mexico’s National Banking and Securities Commission, the CNBV, its home country supervisor responsible for enforcing Mexico’s banking and securities laws.

The Board specifically referred to the CNBV’s substantial revision of Mexico’s banking supervisory framework through the “issuance of supervisory and regulatory requirements that seek to ensure the safe and sound operations of Mexican banks.” Recent regulatory measures taken by the CNBV and noted by the Board include:

1. improvement in the quality of required regulatory financial reporting;
2. strengthening the monitoring of bank’s conditions by conducting annual on-site examinations that focus on risk management and management information systems;
3. changes in the asset classification process and related loan loss reserve calculation to provide a better assessment of asset quality;
4. promotion of a closer exchange of information with foreign supervisory authorities.

The Board also noted the “Financial Technical Assistance Program” between Mexico and the World Bank as well as the pending revision of Mexico’s accounting standards to conform with international accounting standards.

Analyzing other issues related to approval, the Board found that Banacci’s capitalization exceeded the minimum standards in the Basle Accord, and that although Banacci suffered asset quality problems following the 1994 financial crisis, Mexico’s loan restructuring program (UDI) and loan purchase/recapitalization programs (PROCAPTE) slowed the deterioration in its asset quality and improved its capitalization.

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177. See 12 C.F.R. 211.24(c)(1) (1993); see also Banacci Order, supra note 173, at 3-4.
178. See Banacci Order, supra note 173, at 5.
179. See id. at 4.
180. See id.
181. See id. at 4-5.
182. See id. at 6.
VII. Conclusion.

Although its financial system is still troubled, the opening of Mexico’s financial markets to foreign competition and the recapitalization and asset quality programs implemented in 1995 appear to have stabilized its banking system. Perhaps equally significant, the creation of the CNBV and the development of a program for enhancing prudential regulation and supervision of Mexico’s banking system demonstrate measures which may ultimately cure problems with inadequate capitalization and nonperforming loans. The U.S. Federal Reserve Board’s approval of the Banacci Order indicates that the international community is regaining confidence in the Mexican banking system. Although Mexico’s financial system remains a long way from developed country standards of soundness and stability, Mexico finally appears to have begun implementing the policies necessary to ultimately achieve those standards.