Financial Disclosure in Mexico: Evidence from an Audit Study

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Many financial decisions are made infrequently and may involve unfamiliar concepts, especially for individuals with limited financial capabilities. Therefore, financial consumers are prone to mistakes either in choosing among products or in using them inappropriately.

These mistakes would be less of a concern if market forces led to a set of relatively cheap financial products. But this is rarely the case. In Mexico the total annual cost of a 10,000 pesos loan (748 USD) ranges from 10.7% to 326.5%; the total annual yield for savings products with an initial deposit of 5,000 pesos ranges from -63.6% to 6.2% for an investment account and from -100% to 5.1% for a checking account. This large price dispersion is the result of a market failure created by the information asymmetry between less informed customers and better informed financial institutions and the misalignment of their incentives.

Many governments around the world have tried to reduce the information asymmetry by introducing legislation to improve disclosure and transparency, and in some cases have mandated that low-cost savings products be offered in the marketplace or have imposed usury laws capping the interest rate that can be charged. An early example of mandated financial disclosure is the Truth in Lending Act of 1968 which required that consumers in the US be presented with key financial terms for credit products, and standardized the calculation of certain key product terms and disclosure formats. Mexico enacted a similar law in 2009 and in addition, the Banco de Mexico requires that all deposit-taking institutions offer a “basic account” without account opening, deposits, withdrawals, balance enquiry fees, or debit card fees.

But as the financial crisis of 2008 painfully reminds us, these efforts may not have been successful partly because financial institutions shroud prices and adjust their behavior to undermine transparency initiatives and prevent the marketing of mandated products.

This discussion highlights two questions that are the focus of our investigation. First, what is the quality of information provided by financial institutions to low-income customers when choosing among credit and savings products? Second, do financial institutions offer the products that best meet the customer needs, in particular as it relates to cost and intended usage?

Audit Study

To answer these questions, we implemented an audit study in peri-urban areas near Mexico City. Auditors visited the branches of financial institutions seeking to acquire a loan or a savings product. Since the goal was to capture all the information given to the auditor until the product was contracted (or the auditor was rejected in the case of credit), several follow-up visits were required. The scripts used by auditors differed along four dimensions.

- First, we introduced variation specific to the product sought. Savings auditors expressed a preference for either a checking account (for day-to-day financial needs) or an investment account where funds would be deposited for one year. Credit auditors requested a loan amount of either 20 or 70 percent of their household’s annual income, thus creating
exogenous variation in the level of household indebtedness.

- Second, we varied the financial sophistication of the auditor made salient by the language used and the level of engagement during the visits.
- Third, we varied the level of competition among sophisticated auditors by stating that a competing institution had offered them better terms.
- Finally, we created variation in the dress code used during the visit.

Each auditor was given a randomized list of branches to visit and was randomly assigned to a script.

**Results**

We found that the staff provided enough information to allow auditors to apply for the loan or to open the savings account, but that very little voluntary information about avoidable fees and commissions was provided to unsophisticated auditors. In contrast, experienced auditors, who were instructed to ask specific questions about the product if the staff did not disclose this information voluntarily, ended up being better informed, both because they asked more and because the staff provided more information voluntarily.

Hence, the first key finding is that staff adjusts the information provided to the perceived knowledge of the customer, resulting in too little voluntary provision of basic product information to inexperienced customers.

Related, while savings auditors were offered products that matched their preference for maturity, they were rarely offered the cheapest product. The mandated basic account was only offered in 2 of the 54 visits in which the auditor expressed a preference for a checking account. By contrast, when faced with credit auditors requesting large amounts, financial institutions demonstrated ability to assess the capacity to pay of borrowers by both being more likely to reject their loan application and by reducing the amount granted if the application was finally approved.

Thus, firms seem to behave rationally by following their own self-interest.

**Policy Implications**

In Mexico financial disclosure policy can be improved, for example by providing basic guidance to consumers on the key questions to ask when looking for a credit or savings product. In addition, information could be provided more transparently as tested in a follow-up to this study (Giné, Martinez and Mazer, In process).

Of course, not all terms and conditions should be disclosed because too much information may also be ineffective, but aggregate terms such as the total cost of credit (CAT) and total yield (GAT) should be adequately disclosed as required by law to enhance comparability across similar products.

This study covers standard consumer credit and savings products that may be expensive to offer, especially to low-income populations. A promising avenue is the take-up of low-cost mobile or online savings accounts, or access to financial products as a byproduct of government-to-person payment programs, as is the case with the “Oportunidades” social protection program in Mexico.


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