



## ICR Review

Operations Evaluation Department

Report Number: ICRR10220

### **1. Project Data :**

<b>OEDID:</b>	L3911
<b>Project ID:</b>	P040497
<b>Project Name:</b>	Financial Sector Restructuring Loan (FSRL)
<b>Country:</b>	Mexico
<b>Sector:</b>	Other Finance
<b>L/C Number:</b>	L3911
<b>Partners involved :</b>	Inter-American Development Bank
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<b>Reviewed by :</b>	Roger Robinson
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<b>Date Posted :</b>	08/26/1998

### **2. Project Objectives, Financing, Costs and Components :**

The FSRL of 1995 was part of an international effort, referred to as "The Mexican Rescue Package," designed to bolster confidence in the Mexican financial system . The Bank loan of US\$ 1000 million, was part of a multilateral financial package including assistance from the IDB, IMF and the US Government . The overriding objective of the operation was to restore the solvency of and confidence in the banking system . Specifically, the FSRL supported actions to (a) improve discipline and manage systemic risks in the provision of liquidity by the central bank and in lending by development banks, (b) determine the health of the banking system, (c) restructure troubled banks, (d) reform accounting standards, prudential regulation, and supervision, (e) facilitate corporate work-outs and debt restructuring, (f) remove obstacles to secured lending and (g) formulate regulations for brokerage houses and a revised scheme of deposit protection . The loan was disbursed in two equal tranches : the first on effectiveness and the second, nine months later, on the completion of audits of problem banks, examination of all major banks, implementation of accounting standards, and completion of studies for improvements in the legal /regulatory framework. The Financial Sector Technical Assistance Loan, approved in early 1995 was restructured to provide technical support in areas of immediate need.

### **3. Achievement of Relevant Objectives :**

The FSRL has helped improve accounting standards, prudential regulations and supervision . It also helped the National Banking Commission establish procedures to improve the internal controls of banks . Accounting and regulation of financial groups has improved . When fully implemented, the accounting standards, prudential regulation and supervision should improve the performance of the banking system .

### **4. Significant Achievements :**

Actions taken by the government succeeded in restoring a degree of stability and confidence in the banking system and averted a deep financial crisis with international ramifications . Surviving banks are less vulnerable than they were in 1995.

### **5. Significant Shortcomings :**

Project objectives were overly ambitious and their achievement was incomplete . Restoration of the soundness of the banking system was slower than expected because the problems of the banks had been underestimated . According to the ICR, the issues of adequacy of bank capital, restructuring of banks, accounting standards and quality of information, and prudential regulation and supervision, have not yet been fully resolved . A comprehensive strategy still has to be developed for dealing with the US\$ 42 billion in assets in government hands created by interventions and assistance to banks . The banking system remains heavily burdened by non -performing and low earning assets and reserves for loan losses are still inadequate . Capital adequacy remains a concern, but accounting under the old rules makes estimating capital deficiency speculative .

<b>6. Ratings:</b>	<b>ICR</b>	<b>OED Review</b>	<b>Reason for Disagreement /Comments</b>
<b>Outcome:</b>	Unsatisfactory	Unsatisfactory	

<b>Institutional Dev .:</b>	Partial	Modest	
<b>Sustainability :</b>	Uncertain	Uncertain	
<b>Bank Performance :</b>	Satisfactory	Satisfactory	
<b>Borrower Perf.:</b>	Satisfactory	Satisfactory	
<b>Quality of ICR :</b>		Unsatisfactory	

**7. Lessons of Broad Applicability :**

Emergency or relief programs are not good vehicles for pursuing institutional or legislative reforms . This is especially true when, as in this case, the Banks financial contribution is a relatively small part of a large package . Unless there is a single reform package on which all partners have agreed, concerns of major partners will dominate . The pressure for disbursement in emergency situations also weakens the Bank's leverage in enforcing policy conditions. The nine-month period foreseen between effectiveness and disbursement of the final tranche was not a reasonable time span for accomplishment of the project's reform agenda . Country counterparts also tend to pay more attention to short term concerns (in this case keeping the banking system from collapsing ).

**8. Audit Recommended? ● Yes ○ No**

**Why?** It would be useful to assess the current state of Mexico's financial system .

**9. Comments on Quality of ICR :**

The ICR is unsatisfactory. While the coverage is detailed, the ICR contains none of the standard tables required for an ICR. The ICR does not explicitly review the accomplishment of tranche release conditions and it would have been useful to have included a copy of the second tranche release memorandum .