

# METROFINANCIERA MORTGAGE WAREHOUSE FACILITY

## PROJECT ABSTRACT

Project number:	ME-L1011
Project name:	Metrofinanciera Mortgage Warehouse and MBS Guarantee Facilities
Country:	Mexico
Borrower:	Metrofinanciera S.A. de C.V., Sociedad Financiera de Objeto Limitado, a specialized mortgage lending institution incorporated under the laws of Mexico.
Total Project Amount:	US\$800 million MBS program
IDB Participation:	Up to US\$75 million Loan and up to US\$75 in Partial Credit Guarantees.
Department:	Private Sector Department
Status:	Due Diligence
Date:	July 25, 2006

## I. PROJECT DESCRIPTION

- 1.1 The project involves the establishment of a revolving US\$75 million collateralized credit facility to be used by Metrofinanciera to finance the origination and accumulation of residential mortgages for securitization in the form of mortgage-backed securities (“MBS”) in the Mexican capital market. The mortgages will satisfy IDB-specified criteria and will be held in a trust separate from the borrower. The IDB will also provide an MBS Guarantee Facility to provide partial credit guarantees for individual MBS issuances to be made by special purpose vehicles established by Metrofinanciera.
- 1.2 The borrower, Metrofinanciera S.A. de C.V. (“MF”), is the fourth largest specialized mortgage lending institution (“*Sofol*”) in Mexico, measured in terms of total portfolio. The main activities of MF are to extend mortgage loans to low-income individuals under the financing programs of the Sociedad Hipotecaria Federal (“SHF”) and to provide construction financing to housing developers. MF, a privately owned company, was established in 1996 and has grown at a rapid pace, driven by the high demand for low-income housing in Mexico. MF is headquartered in Monterrey, N.L. and operates through a network of 45 offices in 31 Mexican states.
- 1.3 By providing funding for MF to accumulate mortgage pools prior to securitization, the IDB will help MF sustain a regular program of MBS issuance. It will also help MF reduce its dependence on the SHF for long-term mortgage funding, which is critical since the SHF will no longer provide funding after 2009. It is expected that the IDB loan and guarantees will support at least MBS issuances with a value of at least US\$800 million.

## **II. PROJECT BENEFITS**

- 2.1 The principal benefits of the project are to:
- (1) Support middle size mortgage bank to transition source of long-term funding for mortgages from public sector to capital markets;
  - (2) Encourage private players to enter market to provide similar pre-securitization warehouse facilities in Mexico;
  - (3) Promote further development and standardization of secondary mortgage market in Mexico, helping to establish MBS as recognized asset class among institutional investors;
  - (4) Generate greater competition in primary mortgage market by enhancing liquidity for mortgage originators; and
  - (5) Stimulate higher levels of low-income housing construction with greater mortgage availability to help reduce Mexico's housing gap.

## **III. IDB PARTICIPATION**

- 3.1 Insofar as it promotes more competitive and more efficient primary and secondary housing finance markets, this transaction is consistent with the IDB's strategy to lower barriers which limit the competitiveness and efficient development of the private sector in Mexico.

## **IV. ENVIRONMENTAL AND SOCIAL STRATEGY<sup>1</sup>**

### **A. Project Status and Compliance**

- 4.1 MF conducts a generic assessment of environmental and social aspects during the credit review process (e.g. confirmation that potential developments are not located at or near environmental sensible areas, areas susceptible to natural hazards, areas with soil contamination, development in compliance with land use regulations, etc). However, this assessment is not comprehensive and systematized, and is not formally structured as a specific procedure. As part of IDB's financial assistance to MF, the Bank will assist the project Company to develop an environmental procedure commensurate to the potential environmental and social impacts and risk associated to MF's business.

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<sup>1</sup> This Environmental and Social Strategy (ESS) is being made available to the public in accordance with the Bank's policy on information disclosure. The ESS has been prepared based primarily upon information provided by the Project sponsors and does not represent either the Bank's approval of the Project or verification of the ESS completeness or accuracy. The Bank, as part of its due-diligence on the feasibility of the Project, will assess the environmental and social aspects. This assessment will be presented in the Project Environmental and Social Management Report that will be prepared by the Bank, and will be made available to public prior to consideration of the Project by the Bank's Board of Executive Directors.

## **B. Environmental and Social Impacts and Risks**

- 4.2 Based upon the nature of this project (i.e. facility to warehouse and package individual mortgages), there should be limited direct environmental, social, or health and safety impacts or risks, and thus a limited environmental assessment is required. The potential key environmental, social, health and safety, and labor issues and risks include (i) environmental, social and health and safety impacts associated with construction of housing development financed by MF, (ii) MF's environmental credit risks, and (iii) IDB Reputation Risks associated to MF's environmental, social, health and safety, and/or labor practices.
- 4.3 The environmental, social and health and safety impacts associated with housing developments will be related mainly to the magnitude and the location of the development. The key potential project-related environmental, social, and health and safety impacts and risks are those typically associated with new construction, such as: a) social issues associated with acquisition of the site, including any potential displacement of illegal settlements occupying the construction site, and any changes of land use; b) potential impacts from construction on brownfield sites with existing contamination (e.g. release/re-suspension of contaminants with consequent health issues); c) typical temporary impacts from construction related activities such as loss of vegetation, soil erosion; increased air emissions and noise as a result of construction, engine combustion from heavy equipment and machinery, increased generation of solid waste and construction debris, potential contamination or disruption of surface and ground waters; etc.; d) potential impacts on sites of archeological, cultural or historical value, if found; e) potential accidents or other health and safety risks to construction workers from activities associated with the use and handling of heavy equipment; f) other temporary related impacts associated to ancillary activities or facilities (e.g. landfills, quarries, etc) and g) permanent landscape disruption. Once developed, housing complexes could create a significant pressure over public services (e.g. potable water and sewers systems, electricity, access roads, schools, hospitals, etc) and create significant nuisances to nearby populations or sensible habitat if any. Additionally, large housing developments may attract illegal settlement looking for proximities to improved public services and access roads, not only aggravating any environmental and social impact but also increasing the risks for additional environmental and social issues (e.g. land slides, vandalism, crime, etc.).
- 4.4 Environmental Credit Risks refer to potential negative effects on MF ability to repay the IDB because of: (i) risks due to MF credit programs associated with the reduction in mortgage asset values or property guaranties/securities due to environmental or social issues (e.g. environmental liabilities) or increased probability of non-repayment of loan due to environmental and social issues (e.g. law suits, fines, etc); and (ii) risks associated with MF facilities and operations, such as environmental liabilities in their six regional offices and 27 branches offices due to PCB transformers, asbestos, lead paint, etc. or MF employees having occupational health and safety problems due to working

conditions/environment (e.g. inadequate emergency preparedness, lack of fire exits, etc).

- 4.5 Reputation Risks are associated with MF involvement in projects or companies considered unacceptable to the IDB and/or that will face significant public opposition or concerns, such as (i) inappropriate development siting; (ii) MF finance application and analysis process that is not equitable, fair, and unbiased in terms of social factors (e.g. gender, age, ethnicity, or cultural heritage, etc.); and (iii) significantly deficient labor practices by MF, the homebuilders and their subcontractors.

### **C. Strategy for the Environmental and Social Due Diligence**

- 4.6 The Bank, as part of the due diligence process, will analyze the environmental and social aspects of the project. The environmental and social due-diligence will specifically include the components listed below:

- i. An assessment of MF compliance status with the applicable environmental, social, health and safety, and labor regulatory requirements in Mexico.
- ii. An assessment of the sufficiency of current credit appraisal, approval, and monitoring procedures to manage environmental and social liabilities, risks and/or impacts of loan/mortgage operations, including risks associated with MF mortgage portfolio. Current procedure should at a minimum be able to (i) include in the loan/mortgage application and analysis process (i.e., underwriting guidelines and risk review process) consideration of environmental or social aspects, and assess potential environmental financial/credit risks and liabilities that may be associated with the properties, (ii) apply loan/mortgage insurance to cover environmental issues (e.g., soil and ground water contamination, lead based paint, asbestos, polychlorinated biphenyl compounds) and natural hazards (e.g., fire, tornadoes, hurricanes, floods, seismic events), and (iii) count with mortgage credit officers qualified and trained to identify potential environmental, social, health and safety, and labor issues/liabilities.
- iii. An evaluation to assure an appropriate inventory of present environmental and health and safety liabilities in MF facilities and operations, and if they exist, assess the adequacy of the action plan to properly resolve them.
- iv. An evaluation to ensure that MF has adequate health and safety and Contingency Plans and procedures (i.e. emergency response programs, building evacuation drills, etc) including their technical adequacy, adequate level of training, and sufficient resources to ensure adequate implementation.

- v. An evaluation of MF compliance with the Fundamental Principles and Rights at Work and with any other international labor organization conventions and treaties which have been ratified by Mexico, to determine presence of any existing major labor problems associated with MF, and whether they practice fair and unbiased labor practices related to sex, age, ethnicity, cultural heritage, and collective bargaining. MF must have (or develop) written procedures to assure adequate hiring procedures and treatment of employees.
  - vi. An assessment of the adequacy of MF procedures to ensure that loan/mortgage and/or foreclosure procedures, finance application and analysis process is equitable, fair, and unbiased in terms of social factors (e.g. age, gender, cultural heritage, etc).
- 4.7 The team will establish environmental, social, health and safety, and labor requirements in the Loan Proposal for review and approval by the Bank's Committee on Environment and Social Impact (CESI).