FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Contraparte Central de Valores de Mexico's IDRs at 'BBB'; Outlook Negative

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Fitch Ratings - Monterrey - 15 Sep 2020: Fitch Ratings has affirmed Contraparte Central de Valores de Mexico, S.A. de C.V.'s (CCV) Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) at 'BBB' and Short-Term Foreign and Local Currency IDRs at 'F3'. Fitch has also affirmed CCV's Long- and Short-Term National Ratings at 'AAA(mex)' and 'F1+(mex)'. The Rating Outlook for the long-term Foreign and Local Currency IDRs is Negative, while the Rating Outlook for the Long-Term National Ratings is Stable.

KEY RATING DRIVERS

The support driven IDRs of CCV are highly influenced by Fitch's assessment about the ability and propensity of support from its ultimate parent Bolsa Mexicana de Valores (BMV; rated BBB/Negative). Fitch considers that the ability of support is reflected in BMVs IDRs and the agency's view that any required support would be manageable for BMV considering that CCV's operations are relative of small size in respect to BMV's overall operations. As of June 2020, CCV's net income and equity represented 6.3% and 5.8% of BMV's total net income and equity, respectively. Regarding the propensity of support, Fitch considers that

CCV's performs a core role for its ultimate parent given that it is the only central counterparty for Mexican stock market and represents an important business line for BMV. The propensity of support also factors in the huge reputational risk that CCV's default would represent for BMV as potential losses could be relevant despite its relatively small size to BMV.

CCV's Negative Outlook on its IDRs reflects the Rating Outlook of its ultimate parent BMV due to CCV's ratings are support driven and aligned to BMV's ratings. The Negative Outlook reflects Fitch's opinion that although BMV and its subsidiaries have demonstrated strong operational and counterparty resilience in the elapsed months of the current crisis, the ratings of national Financial Market Infrastructures (FMIs) remain sensitive over the medium to long term to investor appetite and sentiment locally and globally, which amid the rising uncertainties in the Mexican operating environment pose additional risks for BMV and its subsidiaries' franchise and company profile when compared to some other globally rated FMIs operating in deeper markets with higher-rated operating environments.

CCV's national scale ratings are relative rankings of creditworthiness within a certain jurisdiction. The Rating Outlook on the National Long-Term ratings is Stable as Fitch does not anticipate negative changes in local relativities.

Notwithstanding that the following aspects do not have direct implications for CCV's ratings, due to they are support driven, Fitch evaluated the overall business of CCV as follows:

In Fitch's view, CCV presents a solid franchise considering its unique role in the Mexican financial market and its long track record of more than 16 years of operation in the Mexican stock market. Its franchise is also benefited from high entry barriers considering the rigorous regulatory and operational requirements. Fitch assessment of CCV's business model is weaker than other global FMIs due to a less deep stock market, less diverse business model and a high clearing agent concentration. Due to the nature of its operations, CCV's business model is concentrated in clearing and settlement services, trade novation and collateral management services in the equities market, which as of June 2020 represented around 93% of its total revenues, excluding the net financial margin. The entity is still working on the diversification of its income sources through the analysis of several alternatives.

Fitch considers CCV maintains a solid Financial Safeguard System (FSS) composed by three guarantee funds, which are frequently tested through detailed stress exercises. As of June 2020, those guarantee funds registered MXN4.1 billion (above the MXN3.9 billion of the same date in 2019), amount that covered around 10.7x the Value at Risk registered as of that date. During 2019, CCV's reinforced its FSS according the international best practices by applying the skin in the game in an earlier step in the FSS and increasing the percentage of that skin in the game. During 2019 and the first half of 2020, there has not been defaults that have detonated CCV's FSS.

The strong capitalization and leverage metrics of CCV are driven by the fact that CCV's operations are completely equity funded. Also, CCV's exhibits a low liquidity risk due to the guarantee funds are mainly invested in highly liquid debt securities (mainly cash, government instruments and repo operations) and in high marketability equity. Fitch considers that CCV presents the opportunity area relative to best global practices as it lacks of a contingent liquidity line; however, CCV is planning to strength its liquidity and it is considering the possible implementation of a contingent liquidity line.

CCV also exhibits a robust profitability level given its constant earnings generation and its efficiency metrics that resulted from the synergies with Asigna and its parent company. As of June 2020, CCV presented a strong fee adjusted EBITDA to total revenues of 59.9%, above the 56.0% registered at the end of 2019 driven by the current market volatility and macroeconomic uncertainty.

Regarding its counterparty exposure, CCV's exhibited high concentrations since its 10 main clearing agents represented around 73% of the operated volume as of July 2020. The agency considers that concentration risks exacerbate under current more volatile conditions and considering the average more modest credit profiles of its clearing agents in respect to some other rated CCVs. In Fitch's opinion, CCV exhibits the opportunity area of concluding the implementation of IOSCO's Principles of Financial Markets Infrastructure (PFMIs) and the full implementation of the Cover One stress test and of the Reverse stress test. Also, the entity does not perform a Cover Two stress test, which is usually seen on CCPs. PFMIs' implementation has taken longer than expected due to additional requirements from local authorities.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Any perception by Fitch of reduced strategic importance of CCV to its parent company may trigger a downgrade of its IDRs, but is not the base case scenario since Fitch considers CCV a core subsidiary of BMV.

--In the case of a downgrade of BMV's IDRs, CCV's IDRs could be driven by its intrinsic credit profile if this remains without changes from the effects of the challenging operating environment.

--Any downgrade to CCV's national scale ratings will reflect a negative change in local relativities.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--There is limited upside potential for CCV's IDRs. The IDRs are already one notch above Mexico's IDRs, which have a Stable Outlook. CCV's IDRs could only be upgraded by a similar rating action on sovereign ratings that drives an upgrade in BMV's IDRs.

--The national scale ratings of CCV are at the highest level on the national scale; therefore, they cannot be upgraded.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579]

SUMMARY OF FINANCIAL ADJUSTMENTS

Pre-paid expenses and other deferred assets were reclassified as intangibles and deducted from total equity due to its lower loss absorption capacity.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

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RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Contraparte Central de Valores de Mexico, S.A. de C.V.	LT IDR	BBB Rating Outlook Negative	Affirmed	BBB Rating Outlook Negative
	ST IDR	F3	Affirmed	F3
	LC LT IDR	BBB Rating Outlook Negative	Affirmed	BBB Rating Outlook Negative
	LC ST IDR	F3	Affirmed	F3

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Metodología de Calificaciones en Escala Nacional - Efectivo desde agosto 2, 2018 hasta junio 8, 2020 (pub. 01 Aug 2018)

Metodología de Calificación de Instituciones Financieras no Bancarias (pub. 18 Sep 2019)

Non-Bank Financial Institutions Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

National Scale Rating Criteria (pub. 08 Jun 2020)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Contraparte Central de Valores de Mexico, S.A. de C.V.	EU Endorsed

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Non-Bank Financial Institutions   Latin America   Mexico