S&P Global
Ratings

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Mr. Jorge Alejandro Chávez Presa
Instituto del Fondo Nacional de la Vivienda para los Trabajadores (Infonavit)
Barranca del Muerto Núm. 280, Ofna 109,
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Dear Mr. Chávez:

Thank you for requesting that S&P Global Ratings provide you with feedback through its Rating Evaluation Service (RES) on the 'BBB+/Stable/A-2' indicative ratings impact for Instituto del Fondo Nacional de la Vivienda para los Trabajadores (Infonavit) given the scenarios pertaining to a potential reduction of its capitalization metrics. S&P Global Ratings has reviewed the specific scenarios you have provided and the following is a summary analysis reflecting our RES committee response.

Existing Ratings
Global Scale Rating: BBB+/Stable/A-2
National Scale Ratings: mxAAA/Stable/mxA-1+
Stand-alone credit profile (SACP): bbb

Scenarios Presented

It is certain that Infonavit must grant the highest possible yield to its workers' saving accounts; however, the regulatory capital ratio (ICAP) and our risk-adjusted capital (RAC) ratio are two variables that affect this return rate's performance--the higher the capitalization level, the lower the yield to the workers' saving accounts. Infonavit's financial target for 2018-2022 is a regulatory capital ratio of 13% and a strong RAC ratio, according to our methodology. In this regard, the management has requested a RES to determine if the entity's capitalization objectives are acceptable or if they can increase workers' returns without affecting our strong capital and earnings assessment.

- **Scenario 1** – Infonavit will reduce its current capital base to MXN154.474 billion in 2018 from MXN198.746 billion reported in 2017. This reduction is aimed at increasing the housing fund return rate. This improvement in workers' saving accounts return rates will lower the regulatory capital ratio to 10%, as well as lowering net interest margins and internal capital generation, and consequently decreasing our projected RAC ratio over the next two years.

- **Scenario 2** – Infonavit will reduce its current capital base to MXN170.659 billion in 2018 from MXN198.746 billion reported in 2017, aiming to increase the housing fund return rate. This improvement in workers' saving accounts return rates will lower the regulatory capital ratio to 11%, as well as lowering net interest margins and internal capital generation, and consequently decreasing our projected RAC ratio over the next two years.

- **Scenario 3** – Infonavit will reduce its current capital base to MXN186.844 billion in 2018 from MXN198.746 billion reported in 2017, aiming to increase the housing fund return rate. This improvement in workers' saving accounts return rates will lower the regulatory capital ratio to 12%, as well as lowering net interest margins and internal capital generation, and consequently decreasing our projected RAC ratio over the next two years.

Summary of Indicative Rating Conclusions*

	Current Ratings	Scenario 1	Scenario 2	Scenario 3
Issuer credit rating (ICR)	BBB+	BBB+	BBB+	BBB+
Short-term ICR	A-2	A-2	A-2	A-2
Outlook	Stable	Stable	Stable	Stable
National scale ICR	mxAAA	mxAAA	mxAAA	mxAAA
Short-term national scale	mxA-1+	mxA-1+	mxA-1+	mxA-1+
National scale outlook	Stable	Stable	Stable	Stable
SACP	bbb	bbb-	bbb	bbb

*Assumes that the hypothetical scenario submitted to S&P Global Ratings by you is implemented in accordance with information and representations you have provided.

Indicative Ratings Score Snapshot

	Current Ratings	Scenario 1	Scenario 2	Scenario 3
ECONOMIC RISK	**5**	5	5	5
INDUSTRY RISK	**3**	3	3	3
ANCHOR	***bbb***	bbb	bbb	bbb
BANK SPECIFIC FACTORS				
Business position	**Adequate (0)**	Adequate (0)	Adequate (0)	Adequate (0)
Capital and earnings	**Strong(+1)**	Adequate (0)	Strong(+1)	Strong(+1)
Risk position	**Moderate (-1)**	Moderate (-1)	Moderate (-1)	Moderate (-1)
Funding and liquidity	**Adequate & Strong(0)**	Adequate & Strong(0)	Adequate & Strong(0)	Adequate & Strong(0)
GROUP OR GOVERNMENT	**N/A**	N/A	N/A	N/A

SUPPORT				
ADDITIONAL FACTORS	N/A	N/A	N/A	N/A
SACP	bbb	bbb-	bbb	bbb
ISSUER CREDIT RATING	BBB+	BBB+	BBB+	BBB+
OUTLOOK	Stable	Stable	Stable	Stable

Supporting Rationale

Upon Infonavit's formal announcement that it has signed a definitive decision to reduce its capitalization metrics, S&P Global Ratings would expect to respond with a publication consistent with our policies and procedures for communicating the rating information derived from this evaluation. This would typically be through a public research update indicating, to the extent possible, the implications for the existing issuer credit ratings and issue-level ratings if applicable. The specificity of our comments regarding the ratings would depend on the availability of definitive information regarding the capital optimization plan. Assuming that Infonavit had made a final decision about the proposed scenarios, and that its plan was consistent with one of the scenarios provided, we would indicate the rating conclusions as detailed below in our external communication. Given that Scenario 1 would likely result in a lower SACP, we would likely affirm the global and national scale ratings and then revise our SACP downwards once Infonavit announces the capitalization optimization plan. However, under Scenario 2 and Scenario 3, the more conservative capital optimization plans, we conclude that no change would likely occur to the ratings (including SACP) or the outlook. If Infonavit pursues one of these plans, we would likely publish a research update to indicate that we had reviewed the implications of the proposed plan and we expected no change to the existing ratings.

Scenarios

Scenario 1

This scenario would likely result in a negative SACP adjustment to 'bbb-' from 'bbb' and no ICR or outlook changes. Upon the implementation of this scenario, our RAC ratio will be in the adequate category. We base this on the negative adjustment of Infonavit's capital base by MXN44.272 billion, translated into the workers' saving accounts return.

Scenario 2

This scenario would likely result in no ratings (including SACP) or outlook changes. Implementation of Scenario 2 would likely result in us maintaining our current 'BBB+/Stable' ICR on Infonavit as well its SACP at 'bbb', because our RAC ratio would be at the strong category. We base our view on the company's sufficient capital base and projected internal capital generation, which should maintain its strong category, after the negative adjustment of the capital base of up to MXN28.087 billion, translated into the workers' saving accounts return.

Scenario 3

This scenario would likely result in no ratings (including SACP) or outlook changes. Implementation of Scenario 3 would likely result in us keeping our current 'BBB+/Stable' ICR on Infonavit as well its SACP at 'bbb', because our RAC ratio would be at the strong category. We base our view on the company's sufficient capital base and projected internal capital generation, which should maintain its strong category, after the negative adjustment of the capital base of up to MXN11.902 billion, translated into workers' saving accounts return.

General Assumptions

Scenario 1:

The RES focused on Infonavit's prospective operating and financial performance using the following key assumptions provided by the company:

- The company will reduce its capital base by MXN44.272 billion compared to the audited figures reported in December 2017, reducing its regulatory capital ratio to 10% (which as of June 2018 was 12.62%).
- Decreasing net income generation over the next three years. We assume that the company will reduce its net income by 26.9% in 2018 versus 2017 (reported figures), further reducing it by 37.1% in 2019 versus 2018, and then reducing it by 24.1% in 2020 versus 2019.
- The main reason for the negative trend in its net income results is the increase in its interest expenses of around 12%, translated into higher workers' savings return rate, of about 300 basis points (bps) additional from the legally minimum return rate requirement (Art. 39).
- Significant growth in the company's new credit loss provisions will also affect income generation. Credit loss provisions will represent more than 4% of Infonavit's total loan portfolio, compared with 2.73% in 2017. This increase reflects our assumption that the company's non-performing assets (NPAs) will be 9.76% in 2018, 10.37% in 2019, and 11.05% in 2020.
- Consequently, our core earnings to adjusted assets will be 1.23% for 2018, 0.70% in 2019, and 0.48% in 2020, compared to the 1.86% reported as of year-end 2017.
- Efficiency levels and operating expenses will remain in line with historical levels.
- Other macroeconomic assumptions:

Variable	2018	2019	2020
GDP	1.80%	1.50%	1.70%
IMSS Jobs	2.85%	0.16%	0.16%
Inflation	6.00%	5.50%	5.00%

Our analytical judgements include:

- We assume that our risk-weighted assets (RWA) will increase by 8.44% in 2018, 5.23% in 2019, and 5.05% in 2020; in line with the projected asset and loan portfolio growth over the next three years.

Scenario 2:

The RES focused on Infonavit's prospective operating and financial performance using the following key assumptions provided by the company:

- Infonavit will reduce its capital base by MXN28.087 billion compared to the audited figures reported in December 2017, reducing its regulatory capital ratio to 11% (which as of June 2018 was 12.62%).
- Decreasing net income generation over the next three years. We assume that the company will reduce its net income by 21.9% in 2018 versus 2017 (reported figures), by 34.2% in 2019 versus 2018, and by 20.7% in 2020 versus 2019.
- The main reason for the negative trend in its net income results is the increase in interest expenses of around 12%, translated into higher workers' savings return rate, of about 300 basis points (bps) additional from the legally minimum return rate requirement (Art. 39).
- The significant growth in the company's new credit loss provisions will also affect income generation. Credit loss provisions will represent more than 4% of Infonavit's total loan portfolio, compared with 2.73% in 2017. This increase reflects our assumption that the company's NPAs will be 9.76% in 2018, 10.37% in 2019, and 11.05% in 2020.
- Consequently, our core earnings to adjusted assets will be 1.31% for 2018, 0.78% in 2019, and 0.56% in 2020, compared to the 1.86% reported as of year-end 2017.
- Other macroeconomic assumptions:

Variable	2018	2019	2020
GDP	1.80%	1.50%	1.70%
IMSS Jobs	2.85%	0.16%	0.16%
Inflation	6.00%	5.50%	5.00%

Our analytical judgements include:

- We assume that our RWA will increase by 8.44% in 2018, 5.23% in 2019, and 5.05% in 2020; in line with our projected asset growth over the next three years.

Scenario 3:

The RES focused on Infonavit's prospective operating and financial performance using the following key assumptions provided by the company:

- Infonavit will reduce its capital base by MXN11.902 billion compared to the audited figures reported in December 2017, reducing its regulatory capital ratio to 12% (which as of June 2018 was 12.62%).
- Decreasing net income generation over the next three years. We assume that the company will reduce its net income by 17% in 2018 versus 2017 (reported figures), by 31.7% in 2019 versus 2018, and by 17.9% in 2020 versus 2019.
- The main reason for the negative trend in its net income results is the increase in its interest expenses of around 12%, translated into higher workers' savings return rate, of

about 300 basis points (bps) additional from the legally minimum return rate requirement (Art. 39).

- The significant growth in the company's new credit loss provisions will also affect income generation. Credit loss provisions will represent more than 4% of Infonavit's total loan portfolio compared to 2.73% in 2017. This increase reflects our assumption that the compnay's NPAs will be 9.76% in 2018, 10.37% in 2019, and 11.05% in 2020.
- Consequently, our core earnings to adjusted assets will be 1.39% for 2018, 0.86% in 2019, and 0.65% in 2020, compared to the 1.86% reported as of year-end 2017.
- Other macroeconomic assumptions:

Variable	2018	2019	2020
GDP	1.80%	1.50%	1.70%
IMSS Jobs	2.85%	0.16%	0.16%
Inflation	6.00%	5.50%	5.00%

Our analytical judgements include:

- We assume that our RWA will increase by 8.44% in 2018, 5.23% in 2019, and 5.05% in 2020; in line with projected asset and loan portfolio growth over the next three years.

Infonavit Rating Assessment Impact

Business position – Adequate/Adequate

We continue to assess Infonavit's business position as adequate in the three scenarios provided. We believe that the company's strategy to increase the housing fund return wouldn't affect our overall business position assessment. We base this belief on Infonavit's overall business profile, which continues to reflect its solid business stability. With a total on-balance loan portfolio of $67.23 billion as of June 30, 2018 (period-end exchange rate of 19.9085), we expect Infonavit to remain the country's largest mortgage originator, with a market share of nearly 57% of the mortgage sector. We also expect Infonavit to continue to reflect adequate business stability in its consistent revenue generation, which will provide sufficient space to improve saving accounts' return.

Capital and earnings

Scenario 1 (Regulatory ratio – 10%)

Assessment revised to adequate from strong

With the implementation of Scenario 1, we would revise Infonavit´s capital and earnings assessment to adequate from strong, reflecting a projected RAC ratio of 9.35%, on average, for the next three years.

The factors affecting our capital and earnings assessment score are:

- Higher interest expenses translated into higher housing fund returns.
- Higher loan loss provisions that will increase by 46.0% in 2018, 22.0% in 2019, and 8.4% in 2020.
- The capital base will be reduced by 22% versus 2017 figures.
- The bank will report net income and internal capital generation as follows:

TAC Calculation	2018	2019	2020
Common shareholders' equity (Reported) (Past Year)	154,474	171,363	181,983
- Dividends (not yet distributed) OR Buybacks (Past Year)			
+ Net Income (Current Year)	16,889	10,620	8,065
Common shareholders' equity (Reported) (Current Year)	**171,363**	**181,983**	**190,048**

- We assume our RWA will grow 8.44% in 2018, and 5.14% on average for the next two years, reflecting moderate loan growth.

Scenario 2 (Regulatory ratio - 11%)

Assessment unchanged at the strong category

With the implementation of Scenario 2, we would keep Infonavit's capital and earnings assessment at strong, reflecting a projected RAC ratio of 10.30%, on average, over the next three years.

The factors affecting our projected RAC ratio are:

- Higher interest expenses translated into higher housing fund returns.
- Higher loan loss provisions that will increase by 46.0% in 2018, 22.0% in 2019, and 8.4% in 2020.
- The capital base will be reduced by 14% versus 2017 figures.
- The bank will report net income and internal capital generation as follows:

TAC Calculation	2018	2019	2020
Common shareholders' equity (Reported) (Past Year)	170,659	188,694	200,559
- Dividends (not yet distributed) OR Buybacks (Past Year)			
+ Net Income (Current Year)	18,035	11,865	9,414
Common shareholders' equity (Reported) (Current Year)	**188,694**	**200,559**	**209,973**

- We assume our RWA will grow 8.44% in 2018, and 5.14%, on average, for the next two years, as a result of the reduced internal capital generation and moderate loan growth.

Scenario 3 (Regulatory - 12%)

Assessment unchanged at the strong category

With the implementation of Scenario 3, we would keep Infonavit's capital and earnings assessment at strong, reflecting a projected RAC ratio of 11.30%, on average, over the next three years.

The factors affecting our projected RAC ratio are:

- Higher interest expenses translated into higher housing fund returns.
- Higher loan loss provisions that will increase by 46.0% in 2018, 22.0% in 2019, and 8.4% in 2020.
- The capital base will be reduced by 5.99% versus 2017 figures.
- The bank will report net income and internal capital generation as follows:

TAC Calculation	2018	2019	2020
Common shareholders' equity (Reported) (Past Year)	186,844	206,025	219,135
- Dividends (not yet distributed) OR Buybacks (Past Year)			
+ Net Income (Current Year)	19,181	13,110	10,764
Common shareholders' equity (Reported) (Current Year)	**206,025**	**219,135**	**229,899**

- We assume our RWA will grow 8.44% in 2018, and 5.14% on average for the next two years, as a result of the reduced internal capital generation and moderate internal growth.

Risk position

After evaluating the scenarios provided by the issuer, we believe we would keep Infonavit's risk position at moderate. For the three scenarios provided, the company assumed stressful economic conditions that would affect overall asset quality metrics. We expect NPA levels of 10.24% in 2018, 9.64% in 2019, and 9.05% in 2020. Infonavit's NPA ratio was 9.50% as of the first quarter of 2018, compared with 9.41% at the end of 2017 and 8.92% in 2016. Although most of the company's origination focuses on low-income individuals, Infonavit's improving origination and collection policies have resulted in more stable asset quality metrics, and we expect this to continue. Finally, we believe Infonavit's loan collection capacity will continue to differentiate it from other non-bank financial institutions (NBFIs) in Mexico, along with its highly diversified loan portfolio by clients. Thus, we don't believe that the variables presented in the three scenarios would significantly affect Infonavit's risk possession assessment.

Funding and liquidity

We believe that Infonavit´s stable funding ratio (SFR) will remain relatively stable despite the strategy to increase housing fund return. Infonavit's funding structure will continues to be one of its main credit strengths. The funding structure mainly consists of the mandatory contributions from private-sector employees (slightly above 19 million), with an average duration that exceeds Infonavit's mortgage loan portfolio.

Infonavit also has the ability to initiate legal action against employers that fail to transfer the worker contributions on a timely basis. This mechanism resulted in a highly stable funding base of $55 billion at the end of the second quarter of 2018. Under the three scenarios provided, we believe Infonavit's liquidity levels are solid, thanks to the long-term nature of its liabilities and its sufficient liquidity sources to meet its obligations.

Government-related entity assessment

According to our criteria for rating government-related entities (GREs), we base our assessment of the extremely high likelihood of extraordinary government support to Infonavit on the following factors:

- Its critical role as the largest mortgage lender institution in the country and its focus on promoting and implementing the government's housing policy. We expect Infonavit to continue originating around 370,000 mortgages annually for the next few years, while maintaining around a 57% market share in this sector.
- Its very strong link with the Mexican government. Historically, the government has been represented on Infonavit's general assembly, board of directors, and surveillance committee, and so has been directly involved in developing the entity's financial plan and business strategy, and appointing top management. We believe that Infonavit's hypothetical default would hurt the country's housing industry and market access for other GREs.

Criteria

- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables, Aug. 14, 2017
- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Financial Institutions - General: Nonbank Financial Institutions Rating Methodology, Dec. 9, 2014
- General Criteria: National And Regional Scale Credit Ratings, Sept. 22, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

We have included the data used by the RES committee in reaching its conclusions.

This evaluation is both preliminary and confidential. It is preliminary in that it is based on hypothetical information presented to us by you. You understand that S&P Global Ratings will not review, modify or surveil this evaluation. Subsequent information or changes to the information previously provided could result in final conclusions that differ from the preliminary *proposed conclusions. Please note the conclusions provided herein are based on assumptions you and your team have provided to us. To the extent that these assumptions, our criteria or other factors change, the rating implications could also change. You understand and agree that we are not financial advisors to you and that in performing the RES, S&P Global Ratings is providing indicative rating opinions on the scenarios presented; it is not endorsing or advocating any particular course of action. Nothing in this report is intended to create, or should be construed as creating, a fiduciary relationship between you and us and recipients of the indicative rating opinions. We have not consented to and will not consent to being named an "expert" under applicable securities laws. Neither S&P Global Ratings' RES or any indicative rating set out herein is a credit rating, nor is it a recommendation to buy, hold or sell any financial obligation of an issuer. This letter is subject to the Terms and Conditions attached to the Engagement Letter applicable to the RES (the "applicable T&Cs").*

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Should you have questions, please do not hesitate to contact me.

Sincerely,

S&P Global Ratings, acting through
S&P Global Ratings, S.A. de C.V.

Claudia Sánchez

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