SoBankable™

A CASE FOR INVESTING IN MEXICO

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In 2023, SoBankable launched its residential mortgage program for financing Canadian and American borrowers wishing to own real estate in Mexico. It did this for two reasons: 1) non-resident foreign nationals are typically prime borrowers, yet they cannot obtain mortgage financing from local Mexican banks; and 2) Mexico is currently one of the best foreign markets for Canadian and American non-residents to invest in. For those reasons, SoBankable has committed to providing foreign individuals access to the mortgage financing they deserve.

Real Estate Appreciation

For any investor, the best market to work in is one poised to enjoy future real estate appreciation. Though numerous factors drive the value of residential real estate, none are as pervasive as local employment, domestic population growth, and access to mortgage financing. Though purchases of residential real estate in key destinations by foreign individuals can potentially lead to an overall increase in local real estate values, it cannot, by itself, sustain real estate appreciation in the long term. Domestic demand for homes is required for real estate to increase in value over a period of years. Investing in a market with true domestic demand gives one confidence that the real estate they invest in will be of the same or greater value in the future.

Regarding employment, Mexico's economy is forecast to grow to be the fifth largest globally by 2050, primarily due to growth in its manufacturing and energy sectors. This growth is expected to add to the rising income levels and purchasing power of Mexico's middle-class consumers,[1.] and if it continues, could ultimately lead to an overall increase in real estate values.

Since the NAFTA agreement was signed in 1994, the income levels and living standards for the Mexican middle class have been rising. In 2016, the middle class accounted for 45% of the country's total households, at 33 million. However, that is still less than the 61% average across the 37 nations in the Organization for Economic Development and Cooperation (OECD). Notwithstanding, Mexico's middle-class is expected to continue to grow, with 3.8 million more households projected to move up to the middle range by 2030.[1.]

Further to this, in December 2022, as highlighted in Mexico News Daily (MND), The Economist magazine ranked Mexico sixth out of 34 countries on its list of "2022's Unlikely Winners." [2.] Those 34 countries were ranked and each assigned an overall score according to five economic and financial indicators:

1) gross domestic product (GDP) growth;
2) inflation;
3) inflation breadth (the share of inflation basket items whose price has risen more than 2% in a year);
4) stock market performance; and
5) government debt.

Ranking sixth out of 34, Mexico just beat out Canada, which ranked seventh, but significantly outperformed the United States, which ranked 20th (See Table 1. *Unexpected Performers 2022)*.[2.]

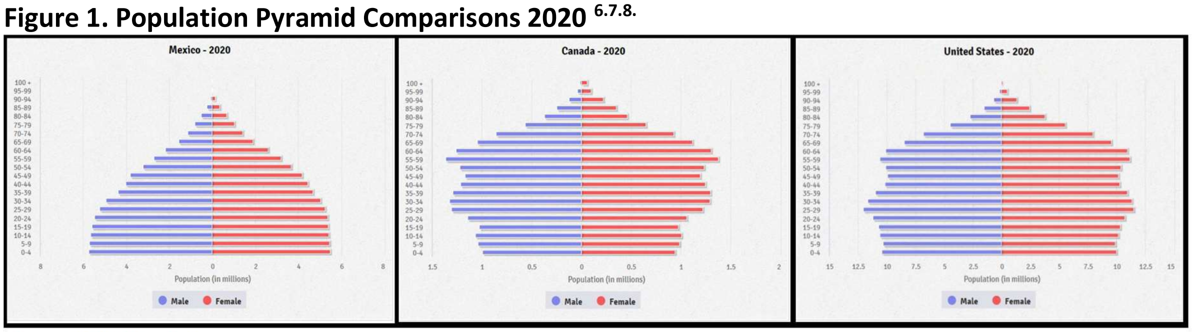
Table 1. Unexpected Performers 2022 [2.]

Country	Rank	**GDP** Q4 '21 - Q3 '22 % Change	**Consumer Prices** Dec 2021 to Oct 2022 % Change	**Inflation Breadth** Oct 2022, %	**Share Prices** Dec '21 to Nov '22 % Change	**Public net debt as % of GDP** 2021 - 2022
Mexico	6	3.3	6.8	82.4	-0.9	-0.7
Canada	7	2.2	6.8	85.7	-4.9	-1.1
United States	20	0.2	6.9	94.4	-9.7	-4.9

Mexico's impressive performance was primarily due to its 3.9% GDP growth in 2022.[3.] Although inflation was high (6.8% consumer price growth and 82.4% breadth), it still compared favorably to many other countries covered in the study.[2.] As at December 2023 BBVA Research forecasted Mexico's 2023 GDP growth to be 3.4% and its 2024 GDP growth to be 2.6%.[4.] Though Mexico's growth rate is expected to slow in 2024 its growth rate is still notably higher than the International Monetary Fund's 2024 Canada GDP growth forecast of 1.3% and its 2024 United States GDP growth forecast of 2.1%.[5.]

Regarding population growth, unlike Mexico, both Canada and the United States are facing serious population decline (see Figure 1. *Population Pyramid Comparisons 2020*).[6.7.8.] Without an increase in international migration, both Canada and the United States will see a significant loss in internal economic activity as fewer consumers will be available to purchase homes, cars and other consumables. For Mexico, it is ideally suited to see its economy grow over the next 50 years as it works through a demographically ideal population structure where the young far outnumber the old. Mexico's current population pyramid is similar to Canada and the United States back in the 1950s.[9.10.]

Figure 1. Population Pyramid Comparisons 2020 [6.7.8.]



Source: CIA World Factbook

Between 2000 and 2021, the share of Mexicans aged 25-34 with post-secondary education increased from 17% to 27%. By 2020, 71% of Mexican children aged 3-5 were enrolled in early childhood education programs, with the share of women attaining upper secondary graduate status growing to 54%, while the men made up 50% of all vocational upper secondary graduates.[11.] Mexico currently has a literacy rate of 94.5% versus Canada and the United States with literacy rates of 99%.[12.]

Regarding mortgage availability, the presence of affordable mortgage financing is essential to encourage the appreciation of real estate. Though Mexican banks provide mortgage financing to permanent residents, Mexico has never enjoyed the inexpensive mortgage financing that is more common in Canada and the United States. This lack of low-cost financing has been a drag on real estate appreciation in Mexico, especially where consumers have been forced to pay cash for their homes. Unlike Canada and the United States, Mexico has no government-sponsored mortgage insurance programs like CMHC (Canada) and FHA (United States). Mexico also lacks a developed secondary mortgage market where banks can sell off their funded loans to long-term institutional investors. This lack of liquidity, coupled with a historically volatile Mexican peso (MXN), leads Mexican banks to charge Mexican borrowers high mortgage interest rates. In addition, Mexican banks require a borrower to purchase several financial products at the same time they take their mortgage. When all the required product purchases are considered, resident borrowers currently face annual percentage rates of between 9.5% (Scotiabank) and 14.1% (BBVA).[13.]

Why Would I Purchase Real estate in Mexico?

Why would anyone purchase real estate in Mexico? The answer is simple, in Mexico, waterfront destination resort properties are considerably less expensive than similar properties in Canada and the United States. For example, in United States dollars (USD), the average 3-bedroom, 2+ bathroom ocean view condominium in Newport Beach, California is $3.4M USD.[15.] A similar property in Puerto Vallarta, Jalisco, is likely around $1.2M USD.[16.]

Not only is real estate more affordable in Mexico than in the United States, but so is the cost of living. Continuing our Newport Beach vs. Puerto Vallarta comparison, we find that in Newport Beach:

1) rent for a one-bedroom apartment outside the City Centre is 322.9% higher;
2) restaurant prices are 161.2% higher;
3) grocery prices are 26.7% higher;
4) preschool (or kindergarten), full day, private, monthly for one child is 370.5% higher;
5) basic utilities (i.e. electricity, heating, cooking, water, garbage) are 53.9% higher;
6) Coke/Pepsi (0.33 liter bottle) is 209.5% higher.[17.]

Regarding property taxes, in Mexico annual property taxes (predial) are very low. Annual property taxes are commonly between $100 and $700.[18.] In Newport Beach annual property taxes would be 1.05283% of the value of the property or $35,796 USD for our $3.4M USD comparable property.[19.] In Puerto Vallarta our comparable property's annual property taxes would be approximately $1,200 USD or 0.001% of our $1.2M USD comparable property.[18.]

With regard to rental income, in Newport Beach the average annual gross Airbnb rental revenue for a 3-bedroom, 2⁺-bathroom condominium is estimated to be $86,368 USD (assumes 60% occupancy).[20.] For Puerto Vallarta the average gross annual Airbnb revenue is estimated to be $88,693 USD (assumes 60% occupancy).[21.] The problem is in Newport Beach the operating costs, including property taxes but before any finance costs, is virtually a breakeven proposition. The Puerto Vallarta comparable performs much better given its market value is 2.83 times less than that of the Newport Beach comparable while the Newport Beach operating costs and property taxes are 6.8 times higher than the Puerto Vallarta equivalent. There is no comparison. In Mexico, one can purchase a lot more house for a lot less money, and if it is a revenue property, in Puerto Vallarta one can achieve a cap rate that is nearly seven times that earned on a comparable property in Newport Beach (see Table 2. *Cap Rate Calculator*).[17.18.19.20.21.]

Table 2. Cap Rate Calculator [17.18.19.20.21.]

NewPort Beach		Puerto Vallarta	
Condo 3-BDRM, 3-Bath		Condo 3-BDRM, 3-Bath	
Market Value	3,400,000	Market Value	1,200,000
Occupancy	60%	Occupancy	60%
Rent	86,368	Rent	88,693
OP Expense	16,020	OP Expense	6,360
Property Tax	35,796	Property Tax	1,200
NOI	34,552	NOI	81,133
Cap Rate	1.0%	Cap Rate	6.8%

Fideicomiso (Bank Trust)

Mexico's Constitution of 1917 proclaimed that all land in Mexico would be "ejido" (communal), or owned by Mexican nationals only. Ejido land was given to every village and could not be sold. In 1973, a constitutional amendment known as the Foreign Investment Law allowed foreigners to purchase real estate anywhere in Mexico except the restricted zone. The restricted zone refers to a specific area of land along the country's coastline and its borders that is subject to foreign ownership restrictions. The restricted zone generally extends up to 50 kilometres (31 miles) from the coastline and 100 kilometres (62 miles) from the borders. Within the restricted zone, foreign individuals can only own real estate through a Fideicomiso (a.k.a. Bank Trust). A Bank Trust allows an individual to invest in Mexican real estate and own it as a beneficiary. The trustee of the Bank Trust is a Mexican bank, which holds legal title to the real estate. The Fideicomiso is a 50-year renewable trust that gives the beneficiary the right to own, occupy, finance, remodel, sell, give away or leave their real estate to their heirs.[22.]

Using a Fideicomiso provides many benefits to both the borrower, which include:

1. Protection of the beneficiary's property rights by the trustee bank;
2. Facilitation of real estate transactions within the restricted zone by allowing foreign individuals to purchase and sell real estate in Mexico;
3. Simplification of inheritance by ensuring a seamless transfer of ownership to the owner's heirs free of capital gains tax;
4. Avoiding future capital gains tax conflicts by crystallizing property values at the time of acquisition; and
5. Reducing the legal risks associated with real estate ownership in Mexico.[23.]

There is no limit on the number of properties a Bank Trust can hold over its lifetime, but the savings derived from holding multiple properties in one trust may be limited. Each time a property is added the beneficiary still has to go through the process and cost of both obtaining a registration number with external affairs and registering the property through a Notary. The savings can come from a reduction in the Bank Trust maintenance fees charged by the trustee bank for each new property.

A Bank Trust is transferable but while it is possible it is generally recommended that a purchaser establish a new trust when purchasing a property. An existing Bank Trust could have undisclosed liabilities and/or legal structural deficiencies, which could adversely affect a buyer in the future. Creating a new trust not only mitigates that risk, but it allows the purchaser to have a trust that is tailored to their individual needs ensuring that the trust meets all current legal and regulatory requirements.

As the benefits of a Fideicomiso are advantageous to the borrower, SoBankable currently does not lend to anyone owning Mexican real estate outside a Fideicomiso.

Is it Safe to live in Mexico?

One concern travelers and foreign individuals have in Mexico is the drug-related violence. Drug cartels and criminal organizations exist in Mexico, and drug-related deaths are unfortunately common. Notwithstanding, overall Mexico is very safe to live in as long as one takes a common-sense approach to their safety.[24.]

Based on available statistics, Mexico seems to be safer than the United States. Overall the United States has higher rates of crime than Mexico, due in part to America's larger population (United States 334.2M vs. Mexico 132.3M). America also has higher rates of gun violence, sexual assault, and drug abuse (see Table 3. *Crime Rate Mexico vs. United States*).[25.]

Table 3. Crime Rate Mexico vs. United States [25.]

Crime	Comparison
Murders with Fire Arms per million	United States 33% more than Mexico
Rape	United States 2 times more than Mexico
Total Crimes per 1000 people	United States 3 times more than Mexico
Violent Crime Intentional Homicide Rate	Mexico 3 times more than United States
Murder per 1 million people	Mexico 5 times more than United States
Burglaries	United States 35 times more than Mexico
Robberies	Mexico 3 times more than United States
Car Thefts per 1000	United States 3 times more than Mexico
Drug Abuse - Cannabis	United States 11 times more than Mexico
Drug Abuse - Opiates	United States 6 times more than Mexico

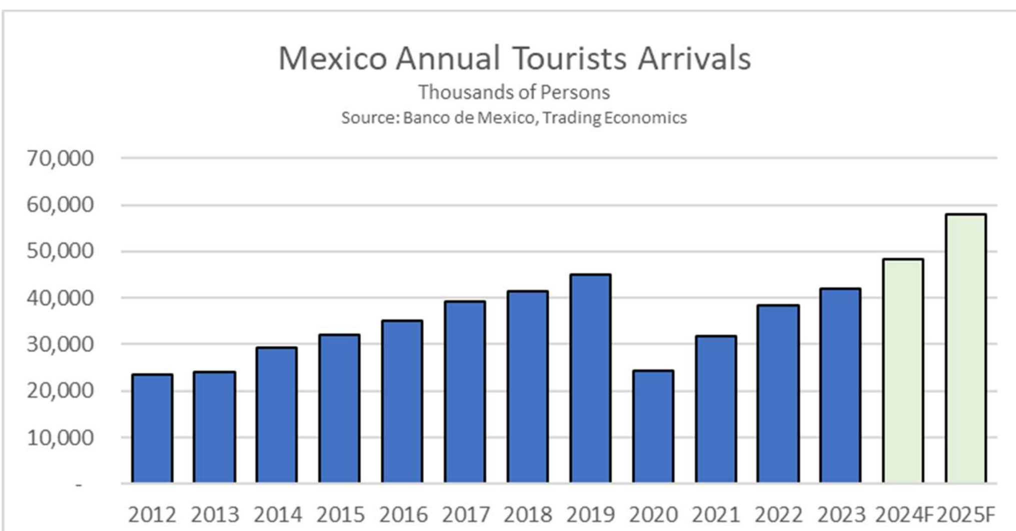
For many, Mexico is perceived as a third world country with excessive crime and lawlessness. That is a misguided assessment given that in 2023 there were 656 (1.80/day) mass shootings reported in the United States.[26.] In reality, a substantial amount of Mexico does not suffer any ill effects of the cartels. Much of the violence occurs in United States border cities, such as Tijuana, Ciudad Juarez, Nuevo Laredo, Matamoros, Nogales, Piedras Negras, and Reynosaor or in remote areas not commonly visited by foreign individuals.[27.] SoBankable currently lends in six of Mexico's thirty-one states: Baja California Sur, Jalisco, Nayarit, Oaxaca, Quintana Roo, and Yucatan. According to Global Guardian's 2023 Risk Assessment Map, cartels are only active in two of those six states, Oaxaca and Quintana Roo.[28.] Within Quintana Roo three municipalities, Cancun (11th), Cozumel (10th), and Playa del Carmen (22nd), are ranked in the top 30 safest cities in Mexico.[29.] Within Oaxaca one municipality, Huatulco is ranked 6th.[29.] Further to this, in August 2019 *CEOWorld Magazine* declared Merida the safest city in

Mexico and the second safest city on the Americas Continent (i.e. North and South America combined) [30.], a sentiment echoed in *mx 30 Safest Cities in Mexico for Travelers & Expats in 2024*.[29.] According to the Yucatan Times in a similar 2019 article, a number of news sources including *Forbes* news magazine and the *New York Times* maintained that Merida was as safe as Europe.[31.] In 2021, *CEOWorld Magazine* named San Miguel de Allende first and Merida third best small cities in the world.[32.] In 2022, *Conde Nast Traveller* magazine's Reader's Choice Awards named San Miguel de Allende as the number one best city in the world.[33]

Between January 2016 and November 2021, 25 Canadians were murdered in Mexico while 22 Canadians were murdered in the United States.[34.] Though the United States is essentially no safer for Canadians than Mexico, Mexico is still viewed by many as a higher risk destination than the United States. In truth cartels are typically eager to avoid confrontations with tourists as such confrontations draw the attention of government security forces. The reason cartels are found in any resort areas at all is because tourists are big buyers of drugs (particularly cocaine) and where there is demand for drugs there are drug dealers.[35.]

The purchase and use of drugs in Mexico is illegal. Those foreign individuals who respect Mexican law by not consuming illicit substances will likely never come in contact with cartel members. Those who insist on seeking out such drugs run a greater risk of encountering potentially dangerous elements. That being the case, the issues associated with foreign individuals' perspective on Mexico's drug issues can be bifurcated into two classes: 1) those that avoid the risk entirely and see Mexico as a low risk place to live; and 2) those that effectively seek it out and may ultimately see living in Mexico as a high-risk proposition. Snowbirds, remote workers, and short-term tourists all have to reconcile themselves to the fact that they are guests in a foreign country and as such, they have to respect the rules and laws and potential risks associated with being in that country.

Graph 1. International Tourist Arrivals in Mexico 2012 – 2025 [36.37.]



Notwithstanding Mexico's public relations issues with cartels, it is seeing an increase in foreign individuals visiting its country. Annual tourists visiting Mexico climbed into the 45 million persons range pre-pandemic. Though Mexico never suffered the COVID lockdowns that Canada and the United States did, they still saw a sharp decline in visitors primarily due to a reduction in flight availability. Current forecasts have Mexico's annual tourist population surpassing pre-pandemic levels in 2024 with notable growth continuing through 2025 (see *Graph 1. International Tourist Arrivals in Mexico 2012 – 2025*).[36.37.] The demonstrable increase in foreign travel to, and real estate acquisitions in, Mexico are a strong indication that many foreign individuals not only see Mexico as a safe place to vacation, but as a safe place to make long term real estate investments. This positive sentiment is supported by InterNations annual survey of United States citizens living abroad (U.S. Expats) where those U.S. Expats rated 53 countries U.S. Expats prefer to live in. In their 2023 survey, Mexico, for the tenth consecutive year, was rated #1 overall, ahead of Canada, which rated #27. The top drivers for U.S. Expats in Mexico were its resident's friendliness and the affordability of lifestyle.[38.]

InterNations also released its *Expat City Ranking 2023*, which ranks the top 49 cities U.S. Expats live in, of which Mexico City ranked #7 after Malaga (#1), Alicante (#2), Valencia (#3), Ras Al Khaimah (#4), Abu Dhabi (#5) and Madrid (#6). Rounding out the world's top 10 cities for U.S. Expats to live in were Kula Lumpur (#8), Bangkok (#9) and Muscat (#10). Interestingly the only Canadian cities to make the list were Toronto (#35) and Vancouver (#47). [39.]

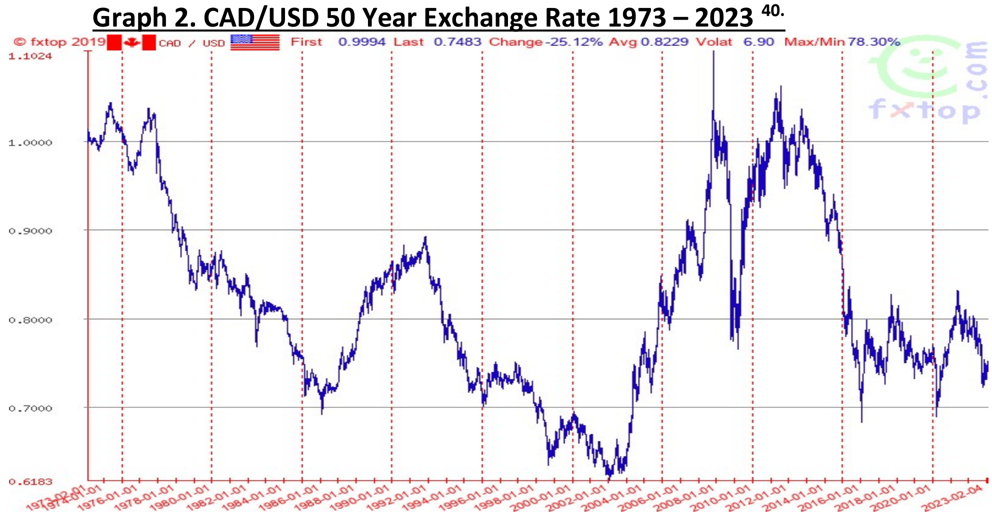
The Benefit of Borrowing in Canadian Dollars

SoBankable lends to Canadian and American borrowers in Canadian dollars (CAD). Intuitively, the benefit of a Canadian financing the purchase of real estate in Mexico using CAD is obvious - there is no exchange rate risk for the Canadian borrower, but the benefits don't end there.

Borrowing in CAD may hold unexpected benefits for both Canadians and Americans when they earn income in USD. Earning revenue in USD and paying mortgage financing in CAD can generate savings, due to the historically favorable CAD/USD exchange rate.

In the past 50 years (1973 to 2023), the CAD/USD exchange rate has had four distinct periods where CAD was close to or above parity with USD, those being; 1) December 1973 to February 1975 (14 months); 2) February 1976 to December 1976 (10 months); 3) September 2007 to July 2008 (10 months); and 4) April 2010 to February 2013 (34 months) (see Graph 2. *CAD/USD 50 Year Exchange Rate 1973 – 2023*).[40.] With regard to the third and fourth periods, CAD/USD was not above par the entire time, but actually whipsawed above and below parity several times. Overall, in the past 50 years CAD/USD has been below parity over 92% of the time.

Graph 2. CAD/USD 50 Year Exchange Rate 1973 – 2023 [40.]



The added benefit for Canadians and Americans who earn USD either from rental income on their Mexican property or from their employment income in their home country is that the repayment of CAD debt in USD can reduce the net effective cost of their borrowing. For example, if you purchased a property in April of 2013 using 11.9% CAD denominated mortgage financing, for the 10 years between April 2013 and March 2023 the net effective cost of funds after the CAD/USD exchange would have been 9.09%.[41.] Likewise, had you purchased in April 2008 the net effective rate for the 15 years between April 2008 and March 2023 would have been 9.85%.[41.] In both cases a significant savings was achieved simply by taking advantage of the arbitrage created by historically favorable CAD/USD exchange rates. Conversely, had you purchased either in April of 2016 (7 years prior) or April 2018 (5 years prior) the savings would have been negligible at 11.72% and 11.59% respectively.

Based on historical CAD/USD exchange rates the CAD/USD exchange will generally work in favour of the borrower. For the times when the CAD/USD is disadvantageous to a borrower, if the borrower has Canadian income they can pay their mortgage using CAD and hold their rental income in USD until it is again favourable to exchange that USD to CAD.

It Pays to Pay in Pesos

When it comes to purchasing real estate in Mexico, such transactions should always be conducted in MXN and not USD. In Mexico, all real estate transactions are recorded in MXN. Transacting in USD not only adds the unnecessary cost of exchange fees to convert CAD to USD and then USD to MXN, but it can needlessly expose the purchaser to capital gains tax when they sell their property in the future.

With regard to transaction costs, converting CAD to USD to MXN, can add anywhere from 1.5% to 2.5% to the cost of the transaction.[42.] For our $1.2M USD Puerto Vallarta property that unnecessary cost could be between $18,000 to $30,000 CAD to complete two currency exchanges instead of one.

With regard to Mexican capital gains tax, assume the $1.2M USD purchase closes today in USD. Given the exchange rate is 17.23 MXN for 1.0 USD the price of the property in MXN should have been $20.67M MXN, but it was done in USD not MXN. Now assume the property is sold five years later for the same value of $1.2M USD except the USD to MXN exchange rate is 21.00 MXN to 1.0 USD. Though the property has not appreciated in terms of USD it has appreciated in terms of MXN. The property's value has increased from $20.24M MXN to $24.67M MXN or 22%,[43.] and, as a result, the seller is subject to capital gains tax, which could be as high as 35%.[44.]

In short, the best way to acquire real estate in Mexico is to purchase the property in MXN, finance it in CAD and pay the CAD denominated mortgage using USD.

Conclusion

Mexico is not only a desirable place to own real estate but also offers borrowers an opportunity to own beautiful property at a more reasonable price while potentially enjoying significant gains on CAD/USD currency exchange rates. SoBankable provides borrowers with a unique suite of mortgage products and a team of experts knowledgeable in Mexican real estate transactions. Visit our website (www.sobankable.com) to try our Mexico Mortgage Calculator or contact us to learn more (inquiries@sobankable.com).

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