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FEATURED Q&A

How Is Mexico's Economic Climate Affecting Banks?



BBVA Bancomer is Mexico's largest bank by assets. A branch in Zamora, in Michoacán state is pictured above. // File Photo: Macy via Creative Commons.

Q Mexico's economy shrank in this year's second quarter, the first quarterly contraction since 2013, the national statistics agency announced Aug. 22. At the same time, the government reduced its growth forecast for the year. How are Mexico's broader economic conditions affecting lending and the country's banks? How strong are Mexican banks' balance sheets, and do they have strong enough provisions to counter loan defaults? Have President Enrique Peña Nieto's policies been good or bad for the banking sector?

A Busy Juarez, associate analyst in the Financial Institutions Group at Moody's Investors Service: "Mexico's banking system remains strong. That said, the combination of low oil prices and other external headwinds has undermined expectations for improved economic performance and shifted the balance of risks and opportunities for banks to the downside. We expect Mexico's economy to grow by 2.5 percent through the end of this year and in 2017, relatively unchanged from 2015. However, while economic growth remains tepid, loan growth is still climbing rapidly at around 12 percent, with new lending that aims primarily at risky consumers as well as small and mid-sized enterprise segments. Consequently, asset quality is likely to deteriorate, but loan delinquency metrics will continue to be largely controlled by banks' aggressive write-off practices. Therefore, we expect the system's non-performing loan ratio will rise only slightly by the end of 2017. Banks' oil exposures remain a key risk. These include exposure to state oil company Pemex (Baa3 negative), one of the largest corporate borrowers in the banking system, which continues to grapple with liquidity

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Brazilian Police Launch Probe of Pension Funds

Authorities said they had launched an investigation into alleged fraud amounting to some \$2.5 billion and involving four of the country's largest pension funds.

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Popular Inc. Enabling Credit Cards for Use in Cuba

The financial institution said its MasterCard-branded cards can now be used at any of Cuba's more than 11,000 authorized merchant terminals and automated teller machines.

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FINANCIAL SERVICES

Scotiabank Reports 6.1% Rise in Quarterly Profit

The lender's global banking and markets unit saw a 12 percent jump in profit for the quarter, due in part to CEO Brian Porter's focus on retail lending in Mexico, Chile, Colombia and Peru.

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Porter // File Photo: Scotiabank

FINANCIAL SERVICES NEWS

Brazilian Police Launch Probe of Pension Funds

Brazilian police on Sept. 5 said they had initiated an investigation into alleged fraud amounting to some \$2.5 billion at four of the country's largest pension funds, all of which are linked to state-run companies, The Wall Street Journal reported. Judge Vallisney de Souza Oliveira ordered the freezing of assets totaling the value of that sum, which belongs



Oliveira // File Photo: vallisneyoliveira.com.

to a total of 103 people and companies that are under investigation. The assets include 90 properties, 139 cars, a plane, bank accounts and shares. The Federal Police said its officers and other agencies are investigating into fraud at Previ, the employee pension fund for Banco do Brasil; Funcef, the employee pension fund for state-controlled Caixa Econômica Federal; Petros, the employee pension fund of Petrobras; and Postalís, the employee pension fund for the country's postal service. The Wall Street Journal was unable to immediately reach the pension funds' lawyers for comment, and press officials at the four funds did not respond to the newspaper's requests for comment. The investigation involves allegations that the pension funds had purchased shares in independent investment vehicles that had paid too much for company stocks or bonds, according to court documents released by prosecutors. The valuations upon which the investment vehicles had based the purchases of stocks or bonds were "unreal and technically irregular," according to the documents, and were based

on information provided by, in at least some of the cases, the companies seeking investment.

Scotiabank Reports 6.1 Percent Rise in Quarterly Profit

Bank of Nova Scotia, or Scotiabank, on Aug. 30 reported 1.96 billion Canadian dollars (\$1.5 billion) in net income, a 6.1 percent rise year-over-year for the quarter ending July 31, Bloomberg News reported. The Toronto-based lender's global banking and markets unit saw a 12 percent jump in profit for the quarter year-over-year, due in part to CEO Brian Porter's focus on retail lending in Mexico, Chile, Colombia and Peru, where the bank hoped to take advantage of the countries' relative economic stability and promising growth prospects, the news service reported. "We are very pleased with continued strong quarterly results in international banking

“We are very pleased with continued strong quarterly results in international banking....”
— Brian Porter

and remain positive about the medium and longer term potential for these markets,” Porter said in a statement. The lender posted strong gains across all of its businesses, though capital markets and international banking saw the biggest quarterly increases. Profit beat analysts' estimates, and the bank boosted its dividend 2.8 percent. Shares of Scotiabank rose by approximately 1.8 percent after the bank posted its fiscal third-quarter profit. Net income from international banking, boosted by increased contributions from fixed income, corporate banking, investment banking and precious metals, rose 10 percent to \$450 million. Scotiabank, which has the most oil-and-gas loans of Canada's five largest banks, said im-

NEWS BRIEFS

Brazil Bank Employees Begin Strike in 15 States

Bank employees in at least 15 of Brazil's states, plus the capital, began a strike Sept. 6, following a stall in negotiations between bank workers and Fenaban, the National Federation of Banks, the Rio Times reported. The bank workers' union had been seeking a pay raise of nearly 15 percent, while Fenaban offered 6.5 percent. "Striking is the last weapon to force the banks to meet the just demands of the employees, as decided by the general meetings held throughout the country," the Contec national confederation of financial workers said in a statement.

Mexico's Bankaool Opens 65,000 Accounts in First 10 Months

Mexico-based online bank Bankaool said Sept. 6 that it had opened 65,000 accounts in its first 10 months of operation. Most of the accounts opened during that time have been opened online, and most of those accounts have been opened using mobile devices, the bank said. Most of the bank's accounts have been established in the evening hours when traditional banks are closed, Bankaool's digital banking manager, Juan Carlos Espinosa, said in a statement.

Probitas Syndicate 1492 Hires Lloyd's Mexico Head

Insurance underwriting syndicate Probitas 1492 has hired Gabriel Anguiano, the current country manager for Mexico at Lloyd's, as its new head of strategy and business development, Probitas announced Sept. 5. Anguiano "will have responsibility for driving business growth across Latin America in line with one of the core strategies of the syndicate," Probitas said in a statement. Anguiano is to join Probitas later this year.

paired energy loans rose to approximately \$280 million from \$268 million the previous quarter, and \$73 million a year earlier.

Deutsche Bank to Sell Argentine Subsidiary

Deutsche Bank announced Aug. 26 that it plans to sell its subsidiary in Argentina to Banco Comafi as it scales back its operations in South America. Deutsche Bank, which did not disclose the terms of the deal, said it will continue serving clients in Argentina from other offices. "The sale of our subsidiary in Argentina is another mark of the progress we



von Rohr // File Photo: Deutsche Bank.

have been making towards our Strategy 2020 goal of becoming simpler and more efficient," Karl von Rohr, the Frankfurt-based bank's chief administrative officer, said in a statement. "I am pleased with the progress of the program to date. We are also well on track in executing our footprint rationalization plans in the other countries that were announced in October of last year." Last October, the German bank said it planned to cut some 26,000 jobs in offices worldwide by 2018 in an effort to boost returns, Bloomberg news reported. In addition to exiting Argentina, Deutsche Bank is also closing its operations in Mexico and eliminated about half its employees in Brazil. The lender is planning to move some Brazil-based trading operations to other locations. Deutsche Bank also has plans to shutter its operations in Chile, Peru and Uruguay. The five Latin American nations where the bank is closing down its operations had 269 employees in total, according to the bank's 2014 financial statements, Bloomberg News reported. Banco Comafi is Argentina's

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strains and high financial leverage. Banks' exposures to the sector account for about 6 percent of all outstanding loans in the system, and for a very high 30-40 percent of core capital at many banks. Notwithstanding rising credit costs, profitability will remain robust thanks to banks' stable, low-cost funding, which helps mitigate risks stemming from the less favorable operating environment. Capitalization will remain strong as well, despite an anticipated decline over the next two years as retained profits will be insufficient to fully replenish capital consumed by rapid loan growth."

A Tapen Sinha, professor of risk management at the Instituto Tecnológico Autónomo de México and professor at the University of Nottingham Business School: "Large financial groups dominate Mexico's financial sector: They are BBVA Bancomer, Santander, Banamex and Banorte. A recent report from the CNBV shows that these banks' assets grew more than 10 percent from July 2015 to June 2016 with an annualized increase of 3 percent in the last quarter. The return on assets in June 2016 was 1.37 percent. This is lower than 1.55 percent in June 2015, but not by much. Similarly, the return on equity was 12.53 percent in June 2016. If we ignore

19th largest bank by assets, with approximately \$1.1 billion, and has equity totaling \$103 million, according to Argentina's central bank.

CREDIT CARD NEWS

Popular Inc. to Enable Credit Cards for Use in Cuba

Puerto Rico-based Popular Inc. announced Aug. 23 that it has become the second U.S. financial institution and the first in Puerto Rico

a spike in 2013, this has been the pattern of the return on equity since 2009. The use of credit cards doubled between 2010 and 2015. Yet, the default rate on those loans has barely budged—it went from 2.5 percent to 3.1 percent. Compared with other Latin

“The use of credit cards doubled between 2010 and 2015.”

— Tapen Sinha

American countries, Mexico lags in banking services. At this point, there is no indication that the short blip in fall of GDP in the last quarter is any indication of a further decline. The future growth rate has been pared down, but no one is predicting a further contraction of the economy. During Peña Nieto's government, there has been large growth of government debt, but it has mainly been a result of state level mismanagement and subsequent rescue by the federal government that added to the debt—not so much by fiscal irresponsibility by the federal government."

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to enable its credit cards for use in Cuba. The MasterCard-branded cards of its two banking subsidiaries, Banco Popular de Puerto Rico and Popular Community Bank, can now be used at any of Cuba's more than 11,000 authorized merchant terminals and automated teller machines, the company said in a statement. Before visiting Cuba, cardholders will be required to complete a document acknowledging that the card may only be used in connection with one of the 12 categories, such as religious and academic activities, that U.S. regulations have established as a condition for its citizens to travel to the island. Florida-based Stonegate Bank, which since last November has offered its customers debit cards that work in Cuba,

began offering MasterCards that can be used in the Caribbean nation in June. [Editor's note: See related [Q&A](#) in the April 22 issue of the Advisor.]

POLITICAL NEWS

Nicaraguan Gov't Grants Asylum to El Salvador's Funes

Nicaragua's government on Sept. 6 granted asylum to former Salvadoran President Mauricio Funes, Reuters reported. Funes faces questions over the source of more than \$700,000 in his personal bank accounts, which he is accused of obtaining illegally. El Salvador's Supreme Court froze Funes' accounts in February as it announced a civic trial investigating the origin of the money. Funes is also under investigation for his travel and alleged connection to criminal gangs during his time in office, though he denies any wrongdoing. The Nicaraguan government announced it had granted asylum to the former Salvadoran leader as well as his wife and three children, whom it claims were persecuted for political reasons. "Asylum only seeks to guarantee protection from persecution," Funes said in a tweet, The New York Times reported. "I have not given up on facing the judicial process or proving my innocence." Funes maintains that the charges and evidence amount to a political conspiracy, Reuters reported. Last month, Salvadoran authorities found arms and ammunition on Funes' property, though no charges were filed. Funes has spent the last three months in Nicaragua, and previously said in a tweet that he was in the country for work reasons.

Colombia Peace Deal to Be Signed Sept. 26

The peace accord between Colombia's government and the Revolutionary Armed Forces of Colombia, or FARC, rebels will be signed on Sept. 26, President Juan Manuel

ADVISOR Q&A

What Does Dilma's Impeachment Mean for Brazil?

Q Brazil's Senate on Aug. 31 permanently removed President Dilma Rousseff from office, formally ending her presidency and more than 13 years of presidential rule by the Workers' Party. What does Rousseff's impeachment say about the strength of Brazil's democracy? What is the future of the Workers' Party? How good a job has Michel Temer done since May as interim president, and how well will he be able to navigate the country's politics and deal with its problems, including an unusually deep recession that has pushed per capita GDP down by nearly 10 percent?

A Carlos Eduardo Lins da Silva, global fellow at the Woodrow Wilson International Center for Scholars: "Dilma is the second Brazilian president to be impeached in 24 years—not a good record for a healthy political system. But it shows that the country is able to solve its most complex problems peacefully and under the rule of law. The lessons of these two cases should lead to a review of Brazil's political system, perhaps in the direction of a parliamentary model. The Brazilian Congress has representatives of more than 30 parties. No party has more than 15 percent of the seats. The president

is always forced to form huge alliances in order to govern. These are characteristics of parliamentary regimes. In presidentialism, ousting a head of government is always traumatic. In parliamentarism, it is part of the regular game. The future of the Workers' Party largely depends on the fate of Lula, its only real leader in its 37-year history. Even if Lula is able to escape a harsh sentence, the party will have to fight hard to overcome its present unpopularity and recover the values that bought it to power 13 years ago. Temer's critical challenge will be to convince Congress to pass at least three structural reforms (fiscal, pension and labor) in order to address the fiscal crisis, a critical step in turning the economy around and recapturing consumer and business confidence. All three require constitutional amendments, passage of which entails two votes in each house of Congress by a three-fifths majority, an extremely difficult political challenge in a multiparty, divided legislature. It is no small task."

EDITOR'S NOTE: More commentary on this topic appears in the Sept. 1 issue of the Latin America Advisor.

Santos announced, BBC News reported Sept. 3. Santos called it "perhaps the most important announcement" of his life. Santos said the final peace deal, which negotiators from the two sides agreed upon last month in Havana, will be signed in Cartagena. There had been speculation that the peace deal would be signed at the United Nations in New York. Before the accord can take effect, however, Colombians must ratify it in a referendum scheduled for Oct. 2. In order for it to be approved, more Co-

lombians must vote "yes" than "no," and votes to approve the deal must total at least 4.4 million, 13 percent of Colombia's electorate, AFP reported. The ballot question will ask voters, "Do you support the final accord to end the conflict and build a stable and lasting peace?" The FARC is expected to hold a separate vote on approving the peace deal, BBC News reported. The deal between the government and the rebels includes an agreement by the rebels to disarm within 180 days of the final peace deal.

NEWS BRIEFS

At Least Two Dead as Hurricane Newton Pummels Baja California

Two people died and three more are missing after their fishing boat capsized in the Gulf of California on Sept. 6 as Hurricane Newton slammed into Mexico's Baja California peninsula, Reuters reported. Officials said the five people had ignored warnings against going out to sea, BBC News reported. The hurricane had also felled trees and damaged power lines after making landfall near the popular resort of Cabo San Lucas.

No Confirmed Cases of Zika Among Olympic Athletes, Spectators: WHO

The World Health Organization announced there were no confirmed cases of Zika among travelers and athletes at the Rio Olympic Games, BBC News reported Sept. 2. Before the Games, the WHO had said the Olympics would not contribute in any significant way to the spread of the Zika virus. At a news conference, the head of the WHO's health emergency program, Peter Salama, said of the Paralympics set to start Wednesday that, "We are optimistic that the same risk assessment will hold and there will be little additional risks."

First Commercial U.S.-to-Cuba Flight in Five Decades Touches Down

A commercial flight from the United States to Cuba touched down Aug. 31 with 150 people on board, marking the first instance of commercial air travel between the two countries in more than 50 years, ABC News reported. The Jet Blue plane flew from Ft. Lauderdale, Fla. to Santa Clara, Cuba, and the flight lasted approximately 45 minutes. Members of the media, airline executives and other VIPs made up the majority of the passengers on board.

It also would establish temporary transition zones and camps for the FARC as well as a provision that civilians will be barred from entering FARC camps. In addition, the deal provides that U.N. monitors will receive all of the FARC's weapons. [Editor's note: See related [Q&A](#) in the Aug. 25 issue of the Latin America Advisor.]

Clinton Declines Peña Nieto's Invitation to Mexico

Democratic U.S. presidential candidate Hillary Clinton said Sept. 5 that she declined Mexican President Enrique Peña Nieto's invitation to visit the country before the November presidential election. When asked by David Muir of ABC News whether she would travel to Mexico



Clinton // File Photo: Clinton Campaign.

before Election Day, Clinton responded, "No." She added, "I'm going to continue to focus on what we're doing to create jobs here at home, what we're doing to make sure Americans have the best possible opportunities in the future." Clinton's opponent, Republican presidential nominee Donald Trump, met with Peña Nieto Aug. 31 in Mexico City. After the meeting, Trump told reporters that he and the Mexican president did not discuss who would pay for one of Trump's signature proposals—a wall between the two countries. Hours later, Peña Nieto tweeted that he indeed told Trump right away that Mexico would not pay for such a wall. Trump "did choke" at the meeting, said Clinton. "He didn't know how to even communicate effectively with a head of state. And I think that's a pretty clear outcome from that trip," Clinton said. Later on ABC, Trump said, "I don't choke... She chokes," referring to Clinton.

ECONOMIC NEWS

Argentine Gov't Seeking to Unify Mining Regulations

The Argentine government plans to propose legislation that would unify mining regulations and allow open-pit mines to operate throughout the country, in an attempt to attract more investment to the sector, a government official said, Reuters reported Thursday. Argentina's mining sector has been lagging behind that of its commodity-rich neighbors, including Chile and Peru. Seven of the country's 23 provinces currently prohibit open-pit mining due to environmental concerns. "We have decided to invite the provinces back into the system by way of a federal agreement," Argentine Secretary of Mining Daniel Meilán said in an interview last week. He added that the government would submit a bill to Congress early next year. Though Argentina attracted very little investment in its mining sector under former President Cristina Fernández de Kirchner from 2007 to 2015, analysts say there is some \$400 billion worth of minerals underground in the South American country. Her successor, business-friendly Mauricio Macri, has already eliminated mining sector export taxes since taking office in December. He also lifted Fernández's ban on foreign mining companies sending profits made in Argentina out of the country.

Brazil Posts Sixth Straight Quarterly Contraction

Brazil posted its sixth consecutive quarterly contraction in the second quarter, according to the Brazilian Institute of Geography and Statistics, The Wall Street Journal reported Aug. 31. Brazil is suffering from several economic woes, including high inflation and unemployment rates. The country's GDP shrank 0.6 percent during the second quarter and contracted 3.8 percent year-on-year.

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A **Sergio Luna Martínez, director of research at Banamex:** "GDP growth projections by the government and Banxico were downgraded as part of a quarterly review process and essentially caught up to standing projections by private analysts; we have, for example, been calling for a 2.1 percent GDP growth rate since April, and this is now the middle of Banxico's forecast range. Although overall GDP growth in this year's second quarter was weak at a seasonally adjusted annual rate of -0.7 percent quarter-over-quarter, the segment relevant to the banking sector is the internal market, and this has been performing comparatively better: if we use the tertiary sector as a proxy for the internal market, the seasonally adjusted annual growth rate in this year's second quarter stood at 0.6 percent quarter-over-quarter, virtually the opposite of the headline figure. This is more consistent with the most recent numbers for bank lending: in July bank lending to the private sector rose 13.9 percent year-over-year in real terms, and nonperforming loans remained stable at 2.9 percent of the total. Overall, the financial reform has been positive for the banking sector as it has sought to increase bank lending as a proportion of GDP through the right set of incentives: more intense competition as well as a legal framework that facilitates the management of credit risk are two good examples."

A **Jonathan Heath, independent Mexico-based economist:** "Although GDP fell in the second quarter, Mexico's economy is still showing an upward trend. While April registered declines in consumption, investment, exports and government spending, data for May and June shows rebounds in most indicators. This means that April was an outlier, while the economy is still growing, albeit at a slow pace. For example, household consumption fell 2.1 percent in April, but then grew 1.6 and 0.9 percent, respectively, in May and June. While consumption will be down for the quarter, the June level is actually a new high, and the trend is growing. GDP growth for the year may not reach 2 percent, much less than what was forecast not too long ago. Nevertheless, car sales have been growing at a rate of 16 percent or more for more than a year, while retail sales continue to expand. Household consumption is currently Mexico's main engine of growth, fueled in part by commercial bank lending, up by more than 10 percent over last year. Most banks continue to show relatively good results, loan defaults are not really growing and balance sheets show more than enough provisions. Mexico at this time has many worries, but the banking sector is not one of them."

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org.

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