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FEATURED Q&A

How Have Natural Disasters Affected Insurance Offerings?



Natural disasters over the past year have prompted insurance providers to examine their businesses in Latin America and the Caribbean. A collapsed hotel following Mexico's Sept. 7 earthquake is pictured above. // Photo: State of Oaxaca.

Q Over the past year, natural disasters, including powerful earthquakes in Mexico and strong hurricanes in the Caribbean, have led some global insurers to re-examine their businesses in the region in efforts to mitigate risk. How have the natural disasters in the past year affected insurance and reinsurance companies operating in the region, and what steps are they taking to reduce risk? How will consumers of insurance products be affected this year, including in terms of premium pricing? To what extent are innovations such as catastrophe bonds, or 'cat bonds,' helping insurers to hedge their risks in Latin America and the Caribbean?

A Eduardo Borensztein, principal at Borensztein Consulting:
"There is a natural tendency to consider insurance after a casualty happens. In fact, insurance premiums have often increased after large natural disasters, at least in part owing to stronger demand. Will the disaster occurrences of 2017 result in higher coverage by Latin American and Caribbean countries? As sound as the case for natural disaster insurance may be, there are obstacles that will still stand in the way. First, the tradeoff that catastrophe insurance presents for the policymaker is not a favorable one: insurance is viewed as expensive, and if a disaster doesn't happen, there may be a political fallout. Moreover, a parametric insurance contract may not be triggered by a relatively small disaster, creating an even more uncomfortable position for the policymaker. Second, the design of an adequate parametric contract is complex and often requires expensive geophysical modeling. Finally, special expertise and bargaining skills are required to keep insurance

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TOP NEWS

BANKING

Mexican Unit Helps Drive Profits at BBVA

Spain's Banco Bilbao Vizcaya Argentaria, or BBVA, reported a 20 percent increase in underlying profits for 2017, which it said was boosted by the bank's performance in Mexico.

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ELECTRONIC PAYMENTS

PayPal, Pay-me Partner in Peru

PayPal has reached a deal to partner with Pay-me that will allow the Peruvian payment platform's customers to buy items from online merchants that accept PayPal.

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BANKING

Brazil's Bradesco Taps Lazari as Chief Executive

Brazil's second-largest private bank, Banco Bradesco, tapped Octavio de Lazari as its new CEO. Lazari has been with the bank since 1978 and currently heads its insurance unit. Lazari will replace current CEO Luiz Carlos Trabuco Cappi next month.

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Lazari // File Photo: Bradesco Seguros.

BANKING NEWS

Brazil's Banco Bradesco Taps Lazari as CEO

Brazil's second-largest private bank, Banco Bradesco, named the head of its insurance unit as its new CEO, the Financial Times reported Feb. 5. Next month, Octavio de Lazari, who has been with the bank since 1978, will replace Luiz Carlos Trabuco Cappi as the head of the lender. Cappi has served as CEO since 2009 and will continue to serve as chairman of the board. After Bradesco announced Lazari's appointment, the new chief executive said the bank had already seen improved demand for credit in the first month of this year, adding that credit growth will help keep profitability up at the lender, as Brazilian basic interest rates reach their lowest level ever, Reuters reported. Lazari's appointment came amid a broader management shakeup at Bradesco, with younger executives joining the bank's board and upper management. Three Bradesco executive vice presidents who had been in the running for the post were instead named to the bank's board on Monday: investor relations director Alexandre Gluher, retail head Josué Pancini and IT executive Mauricio Minas. Executive Vice President Domingos Figueiredo de Abreu, who oversees loans approval, was also named to the board.

Mexico Unit Helps Drive Profits of Spain's BBVA

Multinational Spanish banking group Banco Bilbao Vizcaya Argentaria, or BBVA, reported a 20 percent increase in its underlying profits last year, boosted especially by its performance in Mexico, the Financial Times reported Feb. 1. BBVA said its Mexico results were ahead of analysts' expectations, with net profits up 6 percent in the fourth quarter and up 13 percent over the full year to \$2.7 billion. Performance in

its European markets remained sluggish, and a low interest rate environment led net profits at BBVA's Spanish unit to increase by only 5.5 percent over the past year, with operating income down 1.3 percent. Overall in the fourth quarter, BBVA reported a 90 percent decrease in net profit to \$87 million. The fall was due in large

BBVA said its Mexico results were ahead of analysts' expectations, with net profits up 6 percent in the fourth quarter.

part to a one-off charge of \$1.4 billion, because of the decline of the stock price of Spanish telecommunications group Telefónica, in which BBVA owns a 6 percent share. Net profit for the year, excluding the Telefónica charge, was \$5.7 billion, up 19.7 percent year-over-year. For the full year, revenues increased by 2.5 percent to a record \$31.5 billion, Reuters reported. BBVA Executive Chairman Francisco González said in a written statement that performance this year would be even better, thanks to the bank's digital transformation efforts.

Brazilian Unit Fuels Santander's Profits in Fourth Quarter

The Brazilian unit of Spanish bank Banco Santander posted an 18.3 percent recurring return on equity, beating analysts' projections for its fourth-quarter performance, Reuters reported Jan. 29. Recurring net income, excluding one-time items, grew 38 percent year-over-year to 2.75 billion reais, or \$865 million, higher than analysts' average estimate of 2.6 billion reais. Banco Santander Brasil's loan book grew by 3.6 percent to 272.56 billion reais during the fourth quarter, and grew 6 percent year-over-year in the fourth quarter, due to approximately 20 percent growth in credit to individuals. The bank's stronger-than-expected perfor-

NEWS BRIEFS

Brazilian Federal Court Orders Arrest of Ex-BNY Mellon Executive

A Brazilian federal court on Feb. 1 ordered the arrest of José Carlos Xavier de Oliveira, a former chief executive officer of the Brazilian unit of Bank of New York Mellon, Reuters reported, citing a source with knowledge of the matter. The court and BNY Mellon declined to comment to the wire service. On Feb. 1, authorities executed 100 search warrants related to graft allegations involving a postal worker pension fund, part of which was managed by BNY Mellon's Brazilian unit.

Scotiabank to Buy Citi's Consumer, SME Operations in Colombia

Bank of Nova Scotia has reached an agreement with Citibank to purchase its consumer and small and medium enterprise operations in Colombia in an effort to expand its operations in Latin America, The Canadian Press reported Feb. 1. Scotiabank did not disclose the details of the deal, but said the transaction was not financially material. Citi's operations in Colombia include 47 branches and 424 ATMs, and the addition of Citi's local credit card division will add 500,000 new customers to the operations of Scotiabank's subsidiary, Banco Colpatría. Scotiabank in 2012 bought a stake of 51 percent in Colpatría, which it says is the fifth-largest banking group in Colombia.

Samsung Pay Gets Bank Support to Allow Launch

Samsung has announced that its mobile payment platform, Samsung Pay, has received the support of several banks operating in Mexico, allowing it to launch in the country, Mobile ID World reported Jan. 30. The platform now has the support of banks including Banorte, Citibanamex and HSBC, as well as American Express, Visa and Mastercard.

mance came amid signs of recovery in Brazil's economy. Santander is one of the world's most diversified banks, with its Brazil unit being one of its largest, as well as retail operations in Britain, Spain, the United States, Mexico and Poland, among others, the Financial Times reported. The bank says its diversity lowers its risk profile, as weak performance in one market



Botín // File Photo: Banco Santander.

is usually offset by a strong performance elsewhere. Last year, however, Santander saw revenue growth in eight of its 10 core markets, with Brazil seeing the strongest rise in profits. Net profits were up 42 percent in Brazil. Overall, Banco Santander reported a 9 percent rise in underlying net profit, to 1.9 billion euros (\$2.37 billion), for the fourth quarter. The Spanish bank's underlying profit for 2017 rose 14 percent, to 7.5 billion euros. The bank's executive chairwoman, Ana Botín, said it was a "very strong year."

ELECTRONIC PAYMENTS NEWS

PayPal Partners With Pay-me in Peru

PayPal has reached a deal with Pay-me, which will allow registered users of the Peruvian online payment platform to associate their accounts with PayPal, local daily newspaper La República reported Feb. 2. Under the deal, Pay-me users will be able to use their bank accounts at Interbank, BBVA, Scotiabank or Banco de Crédito del Perú to buy items online in the more than 200 countries worldwide where PayPal payments are accepted. There are about three million consumers in Peru, or about 10 percent of the country's population,

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costs down. Cat bonds work best for large, nearly undiversifiable risks like California earthquakes. Latin American and Caribbean countries, by contrast, present risks that can help diversify those large exposures of the insurance industry, and this could be a valuable bargaining chip in a well-managed negotiation with reinsurance companies. Overall, the current situation may present an opportunity for multilateral institutions such as international development banks to provide technical support on all these issues and create a more favorable environment for policymakers to go forward."

A **Eli Sanchez, senior financial analyst at A.M. Best:** "Mexico insurers have not been materially affected by the earthquakes and hurricanes of 2017. This has been mainly attributed to sound risk management practices, which included prudent reinsurance protection. However, from the regulatory and legislative perspective, there is an initiative to review the General Civil Law and the catastrophe aspects of the insurance law in order to increase coverage for these events. Approximately 27 percent of Mexican households have insurance for catastrophic events, which is mainly due to mortgage requirements; the majority of households are uninsured. In Puerto Rico, domestic property/casualty insurers were able to navigate the 2017 catastrophe season. Yet challenges still remain there and include: increased reinsurance pricing; macroeconomic and fiscal issues; an evolving view of risk and risk appetite due to catastrophe model changes; a highly competitive and concentrated marketplace; and continued population and infrastructure pressures. For the Latin America region, reinsurance programs that renewed in January experienced higher costs and more stringent terms. Such costs are expected to reflect in higher premium rates for the commercial segments; however, for personal lines, the

timing and the impact of such increases may vary. In Latin America, the use of catastrophe bonds is limited to government sponsors at present. Mexico has had a positive experience with such instruments,

“**Approximately 27 percent of Mexican households have insurance for catastrophic events, which is mainly due to mortgage requirements.**”

— Eli Sanchez

and recently the Pacific Alliance trade bloc (Chile, Colombia, Mexico and Peru) launched a \$1 billion catastrophe bond in conjunction with the World Bank. However, we have not seen individual insurers interested in opting for such instruments. In the Caribbean, there are limited reinsurers issuing such instruments."

A **Eduardo Cavallo, lead research economist at the Inter-American Development Bank:** "A key feature of cat bonds is they allow insurers to pool a variety of uncorrelated risks together, potentially allowing them to provide cost-effective insurance solutions to cover certain layers of catastrophic risk. From the point of view of the insured party, cat bonds provide a key advantage, because payouts are based on the severity of the event, rather than on estimates of damages. Therefore, payments can be made quickly and with little contention, allowing, for example, insured governments to provide emergency relief before foreign aid arrives. The potential of cat bonds has not yet been fully realized in part because they remain expensive. For example, according to estimates done with colleagues at the In-

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that regularly buy goods online, according to an Ipsos survey released last year. The companies hope the deal will strengthen and promote e-commerce in Peru, La República reported.

ECONOMIC NEWS

Venezuelan Central Bank Devalues Currency in Auction

The value of Venezuela's bolívar fell by more than 80 percent Feb. 5 as the country's central bank restarted currency auctions in order to ease hyperinflation and infuse the bank with more dollars, Bloomberg News reported. One U.S. dollar purchased 25,000 bolívares at the auction, a significant decrease in the value from six months ago, when the central bank sold 3,345 bolívares for one dollar. The rate that the central bank announced Feb. 5 is still stronger than bolívar's value of the on the black market, where individuals and businesses can get 225,000 bolívares for one dollar according to dolar.today.com. The currency sale is an attempt by the administration of President Nicolás Maduro to increase access to dollars in order to somewhat improve conditions amid an economic crisis that has been dogging Venezuela for years. The weakened exchange rate, or Dicom rate, is now the official rate for all official transactions, and allows the government to stretch its dollars further when paying for imports, and makes businesses' overseas purchases cheaper than before. The rate is also the rate used by foreign credit cards in Venezuela.

NAFTA Important for Mexico's Economy: AMLO Advisor

The economist that Mexican presidential frontrunner Andrés Manuel López Obrador has tapped to run renegotiations of the North American Free Trade Agreement if López Obrador

ADVISOR Q&A

Which Candidate Has the Edge Ahead of Costa Rica's Presidential Runoff?

Q Right-wing evangelical singer and lawmaker Fabricio Alvarado Muñoz of the National Restoration Party was the top vote-getter in the first round of Costa Rica's presidential election on Feb. 4 and will face center-left former labor minister Carlos Alvarado Quesada of the Citizens' Action Party in the April 1 runoff. Alvarado Muñoz in recent weeks was polling in the single digits, but then surged ahead after vowing to oppose a ruling by the Inter-American Court of Human Rights requiring Costa Rica and other member countries to recognize same-sex marriage. Alvarado Quesada, who is not related, supports same-sex marriage. Will that issue continue to dominate the election ahead of the second round? Who has the edge to become the country's president? What has the election revealed about Costa Ricans' priorities and concerns?

A Pablo Duncan-Lynch, founding partner and country director for Costa Rica at CLC Comunicación, an affiliate of Llorente & Cuenca: "Even though Costa Rica's economy faces important challenges related to the growing budget deficit and stagnant unemployment, the cultural issues that arose after the same-sex marriage ruling will still play an important role in the second round, polarizing the election. Because the two parties with the most votes each received less than 30 percent of the vote, agreements and coalitions before the second round

might be the deal breaker. Both candidates have their weaknesses on economic affairs. In the case of Fabricio Alvarado, there are doubts about his eventual economic team, while Carlos Alvarado has been criticized for wanting to keep part of the current economic cabinet. Given this situation, the candidate who becomes more open to the economic programs of other parties will have a better chance over the other. As the ruling party candidate, Carlos Alvarado is vulnerable to any unpopular government action or scandal over the next two months. The campaign before the second round will be long and wearing. In order to form political coalitions and win elections, the government's candidate must relax his positions on controversial issues such as the establishment of sex-education guides with a gender focus in primary schools. Sixty percent of Costa Ricans reject such progressive topics, according to recent surveys. The opposition candidate will probably continue with his conservative agenda, because the strategy has paid off. Both candidates will surely offer multi-party cabinets to their main political adversaries, especially the Christian Social Unity Party and the National Liberation Party. Success in these alliances will be crucial to determining the election."

EDITOR'S NOTE: More commentary on this topic appears in the Feb. 6 issue of the *Latin America Advisor*.

dor is elected in July said that the agreement is an important part of Mexico's economy, adding that she does not plan to scrap the progress that Mexico, the United States and Canada have made in talks to modernize it, Bloomberg News reported Feb. 1. Graciela Márquez, who

López Obrador has said would be his economy minister, said NAFTA has helped with job growth in Mexico. She said López Obrador and his party "support the continuation of NAFTA," adding that it is "very important to the well-being of Mexicans." However, the

NEWS BRIEFS

Guatemalan Authorities Arrest 28 in Crime Ring Investigation

Guatemalan authorities have arrested 28 people, including nine police officers, in a bust of an organized crime and drug trafficking network, the Associated Press reported Feb. 5. Prosecutor Gerson Alegría said the network had been under investigation since last year. The ring would allegedly contact drug vendors and say they wanted to do business, and then would steal vendors' merchandise with support from the police belonging to the ring. The group also conducted illegal raids of homes in order to steal possessions.

Colombia Opens Shelter for Fleeing Venezuelans

The Colombian government on Feb. 3 opened its first shelter for Venezuelans fleeing the country's economic and political crises, The Wall Street Journal reported. The shelter is located near the border city of Cúcuta, and is expected to provide shelter for up to 48 hours for 120 people per day. Priority will be given to pregnant women, the elderly and minors who entered Colombia legally. The Red Cross will administer the shelter. Some 35,000 Venezuelans cross into Colombia every day.

Mexico's Antitrust Agency Investigating Monopoly Practices in E-Commerce

Mexico's antitrust agency, the Federal Commission for Economic Competition, or Cofece, on Feb. 1 said it is investigating "probable" monopoly practices in Mexico's e-commerce market, Reuters reported. Cofece said in a statement that it is investigating possible practices such as price discrimination by major companies in order to inhibit growth by smaller retailers. The agency did not name any specific retailers that it is investigating.

agreement is not perfect, and López Obrador wants to develop the domestic market and reduce inequality without implementing protectionist policies, Márquez added. She said she is ready to negotiate with U.S. President Donald Trump's administration if negotiations have not been completed by the time Mexican President Enrique Peña Nieto leaves office in December. The comments from Márquez are a departure from some of the messaging from López Obrador's campaign, especially during the two previous occasions he ran for Mexico's highest office.

POLITICAL NEWS

Ecuadoreans Vote to Limit Presidents to Two Terms

Ecuadoreans went to the polls on Feb. 4 and voted in favor of a measure that sets limits on presidents to serving two terms, essentially blocking former President Rafael Correa from returning to the presidency, The Wall Street Journal reported. Ecuador's National Electoral Council said two out of every three voters approved the measure proposed by President Lenín Moreno, who was elected in 2017 and was widely seen as a placeholder for Correa until he could run again for president in 2021. He served for six years as Correa's vice president, but surprised Ecuador by almost immediately turning against Correa once elected president. He has made efforts to fight corruption, most notably with his former vice president, Jorge Glas, being sentenced to six years in prison on charges of taking bribes from a construction company. Moreno has also worked to improve relations with journalists, indigenous groups and business leaders, groups that were often challenged by Correa during his presidency. Moreno pushed for a total of seven constitutional changes in the referendum, most of which reverse policies from the Correa administration. The reforms received between 63 percent and 74 percent support from Ecuadoreans. "The days of confrontation

are behind us," Moreno said, the Associated Press reported.

U.S., Peru Vow to Continue Anti-Drug Cooperation

The U.S. and Peruvian governments will keep working together to combat drug trafficking, Peruvian Foreign Minister Cayetana Aljovín told reporters Feb. 5 alongside U.S. Secretary of State Rex Tillerson, who is on a five-nation tour of Latin America, Reuters reported. The statement came just days after U.S. President Donald Trump threatened to restrict aid to countries that he said were "pouring drugs" into the United States and said he wanted to "stop the aid" after he was told by a U.S. Customs and Border Protection official that cocaine primarily from Peru and Colombia was being trafficked through Central America and Mexico, the wire service reported. Tillerson, however, was more conciliatory in his remarks. "The U.S. is victimized certainly by the flow of narcotics to the U.S., but the countries in which these narcotics are transited, or where organizations are carrying out their activities to move these drugs, they also suffer as well," said Tillerson. "The U.S. has to acknowledge that we are the market. We are the largest consumer of illicit drugs and so we have to begin to work on that problem." Tillerson said Trump had allocated \$1 billion toward solving the problem. Tillerson said the United States is also engaged in "clear dialogue" with Mexico, which was the first stop on his tour of Latin America. On Feb. 6, Tillerson heads to Colombia, which received some \$10 billion in funding for military and social programs between 2000 and 2015 through Plan Colombia. Tillerson on Feb. 5 declined to confirm if Trump would attend the Summit of the Americas, which is scheduled to be held April 13-14 in Lima, the Associated Press reported. "There's been no final decision made," said Tillerson, adding that Trump's attendance would depend on his schedule, which is not typically known so far in advance. U.S. presidents have attended all seven previous summits.

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ter-American Development Bank and Johns Hopkins University, a typical cat bond may cost up to four times or more what a country is willing to pay to reap the welfare gains of such insurance. This is probably because of the immensely complex challenge of calculating low probability events and related costs. Moreover, no private company is likely to invest in the costly risk analysis and modeling required to find out; their work would simply end up in the public domain. The result is an information-starved environment in which investors shy away and coverage is expensive. The public sector might have a catalytic role to play in developing these markets by subsidizing the research, or sharing the results of publicly funded research with the private sector."

A **William Vlcek, senior lecturer in global political economy at the School of International Relations at the University of St. Andrews in Scotland:** "There has been a growing consideration over the past few years about resilience—personal resilience, societal resilience and national resilience. The difficulty with this strategy, however, is that building resilience requires resources, including a firm foundation upon which to construct a resilient society. Images from the Caribbean barely begin to reveal the catastrophic impact of the 2017 hurricane season for the region. The consequences of

the devastation shown in them are compounded by the varied scope of insurance coverage carried by individuals, businesses and governments. The collective resources of the region for recovery and reconstruction are not sufficient for the task, even with the improvements undertaken in the past decade. We should remember that the introduction of catastrophe bonds as an alternative source of insurance at the same time represents an alternative form of investment. The point is to highlight the operation of a market mechanism behind the establishment of the catastrophe bond, just as the insurance industry functions as a market expecting a profitable return, over the long run. Thus, while insurance serves as a risk-mitigation tool for the purchaser of the insurance policy, risk mitigation for the insurance firm involves offering policies that, over the long term, will be profitable for them. Shifting weather patterns due to climate change influence the risk calculations of the insurance firm and highlight the increased likelihood of weather-related damage. Consequently, going forward, governments and international agencies need to pursue additional, innovative insurance solutions to address climate change-induced natural disaster risk."

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

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