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FEATURED Q&A

Would New Limits on Swipe Fees Help Brazil's Consumers?

Credit cards in Brazil have an approximate activity rate of 56 percent versus 32 percent for debit cards, Richard Child writes below. // File Photo: pxhere.com via Creative Commons license.

Q Brazil's central bank is reportedly considering a plan to cap the fees that retailers must pay when customers swipe debit cards. Lower swipe fees, which in Brazil typically range from 1 percent to 3 percent of the transaction value, could dent the revenue of card processing firms, but they also might increase card usage. Should Brazil's central bank rein in the swipe fees? What effect would such a move have on card processing firms, banks and consumers? Would it have the intended effect of reducing instances of money laundering and violence against clients carrying cash through decreasing the use of cash and increasing the use of debit cards?

A Jan Smith, member of the Financial Services Advisor board and partner at KoreFusion in Mexico City: "This is not the first time Brazilian regulators have wanted to lower the ceiling on merchant discount rates. Regulators will likely not mandate changes, but instead 'strongly recommend' ceilings and then establish deadlines by when acquirers and banks should 'voluntarily' lower fees. Politically, this placates merchants and consumers, although precedent shows merchants will benefit little, and no savings will be passed on to consumers. Regulators believe investments in card and point-of-sale infrastructure are mature, and that a lowering of fees is justified. Brazil has sufficient debit cards in circulation so that lowering fees will be compensated by an increase in volume, stemming from greater merchant acceptance and debit card use. However, there is another set of factors at play whose consequences—intended or not by a shift in debit card fees—are transformative. This is the beginning of a new payments

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Soros, Cohen Boost Stakes in Argentine App

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Western Union Posts Gain in Latin America Revenue

Transactions that originated in Latin America and the Caribbean led the company's revenue growth, rising 21 percent.

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Rabobank to Pay U.S. Fine Over Money Laundering

Netherlands-based Rabobank, led by managing board chairman Wiebe Draijer, has agreed to pay the U.S. government $369 million after the California unit of the bank pleaded guilty to allowing Mexican drug gangs to exploit flaws in its anti-money laundering system and then attempting to cover it up.

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Draijer // File Photo: Rabobank.

BANKING NEWS

Soros, Cohen Boost Stakes in Argentine Mobile Banking App

Investment groups owned by U.S. investors George Soros and Steve Cohen have both increased their stakes in Argentine tech start-up Ualá, a mobile banking app, Bloomberg News reported Feb. 7. The app, which launched in October, raised $10 million in a funding round of Series A stock led by Soros, which closed last week, according to Soros Fund Management. Cohen's Point72 Ventures, as well as U.S. global investment bank Jefferies Group, participated in the funding round. Less than half of all Argentines have a bank account, and Ualá aims to close the gap by offering a low-cost alternative that allows customers to bank via their smartphones without fees to open, close or maintain the accounts. Each account also provides a prepaid Mastercard. Demand for the product has exceeded Ualá's expectations since its launch in October. Approximately 50,000 cards have been issued in the app's first three months. The founder of the company, Pierpaolo Barbieri, had said he only expected 10,000 users during that period. Forty percent of Argentines have smartphones, and that percentage is expected to reach 70 percent by 2020, according to the trade group GSM Association. Ualá was the fifth-most downloaded financial app in Argentina as of Feb. 4, according to research group App Annie.

Rabobank to Pay U.S. After Guilty Plea on Laundering Charge

Netherlands-based bank Rabobank has agreed to pay the U.S. government $369 million after the California unit of the bank pleaded guilty to allowing Mexican drug gangs to exploit flaws in the bank's anti-money laundering system and then attempting to cover it up, the U.S. Department of Justice said Feb. 8, the Financial Times reported. The Department of Justice said the California subsidiary pleaded guilty to charges of impairing, impeding and obstructing regulators by trying to cover up weak spots in its anti-money laundering compliance program. The U.S. government said Rabobank allowed "hundreds of millions of dollars" in cash to be deposited into its rural bank branches in Imperial County, Calif., which were then transferred via wire, checks and withdrawals. "When Rabobank learned that substantial numbers of its customers' transactions were indicative of international narcotics trafficking, organized crime and money laundering activities, it chose to look the other way," said acting assistant attorney general John Cronan. One such signal was a pattern of cash withdrawals of $9,500—slightly less than $10,000, the amount at which the withdrawal would have needed to be reported—several times in the same day. "Worse still, Rabobank took steps to obstruct an examination by its regulator into those same deficiencies," Cronan said. Rabobank's Calexico branch, which is located about two blocks from the U.S.-Mexico border, was the bank's best-performing branch in the Imperial Valley region, due to its high volume of cash deposits and withdrawals, while the bank did not conduct basic checks on the source of the funds. Wiebe Draijer, Rabobank's board chairman, called the violations "serious, regrettable and unacceptable."

Mexican Cities, States Can Expect Lower Borrowing Costs: Interacciones CEO

The acquisition of Mexico's Grupo Financiero Interacciones by rival Banorte will lead to lower borrowing costs in the state and municipal government debt sector, Interacciones chief executive Carlos Rojo told Reuters on Feb. 14. Proponents of the deal, which is expected to close before the end of the second quarter, say the tie-up will create the country's second-biggest bank, providing efficiency of scale and more financing capacity. "This will allow us

NEWS BRIEFS

Western Union Posts Gain in Latin America Revenue

Colorado-based Western Union on Feb. 13 said its revenue in the fourth quarter of 2017 rose 5 percent as compared to the same period in the prior year, to $1.4 billion. The money transfer company's digital channel, westernunion.com, delivered a 22 percent revenue increase and represented 10 percent of Western Union's total consumer-to-consumer business in the quarter. Geographically, transactions that originated in Latin America and the Caribbean led the company's revenue growth rate, rising 21 percent.

Brazilian Banks Face Profitability Challenge

Brazilian banks will face profitability challenges as the country's central bank is likely to keep interest rates in the single-digit range through 2018, Moody's said in a report released Feb. 8. The benchmark Selic was more than halved from 14.25 percent in October 2016 to the current level of 6.75 percent, a historically low trend that will strain earnings at the country's largest listed banks. "With single-digit rates to stay for the foreseeable future...tighter margins and weak loan growth will pressure profitability," analyst Farooq Khan wrote.

MetLife Reports Flat Earnings in Latin America

New York-based insurer MetLife on Feb. 14 reported that its earnings from Latin America operations during the fourth quarter of 2017 rose to $125 million, up 2 percent year-over-year. However, on a constant currency basis, earnings remained unchanged. Results from the region improved, owing to volume growth, but were partially offset by higher expenses and taxes. Operating premiums, fees and other revenues increased 8 percent, or 5 percent on a constant currency basis. MetLife's quarterly earnings in other parts of the world, especially in Asia, declined sharply by comparison.

to be much more aggressive," said Rojo. The interest rate that states and municipalities pay on loans averaged 8.7 percent through September, government data shows. In related news, Rojo told Chinese news agency Xinhua on Feb. 12 that he is looking to partner with Chinese companies to financially back infrastructure, energy and transport projects in Mexico. "We have been looking for both Chinese banks that could be interested in funding many of these infrastructure projects, and Chinese construction companies that are coming to the country," said Rojo. Banorte agreed to acquire Interacciones, the bank controlled by Mexican billionaire Carlos Hank Rhon, last October for about $1.4 billion, Bloomberg News reported.

INSURANCE NEWS

Protectionism a Risk to Latin America's Insurance Growth: Lloyd's Chairman

The threat of a rise in protectionist policies could prevent Latin America from becoming one of the biggest insurance markets in the world, Bruce Carnegie-Brown, the chairman of Lloyd's of London, said in a speech to an industry group in Miami on Feb. 14. "Insurance works best when risk and capital can flow freely across borders. Protectionist trade barriers reduce capacity, competition and customer choice and at the same time drive up reinsurance costs over the long term," Carnegie-Brown said. International insurance companies have been betting that a combination of low insurance penetration, demographic dynamics and faster rates of economic growth than developed nations would create strong demand for insurance in Latin America over the coming years. However, rising trends toward protectionism "could stop this future in its tracks," he said. Free-market advocates fear protectionism in the United States under the administration of Donald Trump may could retaliatory measures in Latin America, especial-

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era: the use of real-time payments—in Brazil known as TED—for small-denomination merchant and P2P payments (think Venmo). To make this a reality, banks and regulators are exploring ways to make TED agile and economical. The new solution is likely a few years out, but discussions are already well advanced. In other countries, pricing is a fixed fee worth mere cents. This threatens the use of debit cards in particular, because they are the card instruments most used for small- denomination payments. Introducing this new payment solution, without first lowering debit card fees, risks painful disruption by creating too wide a pricing gap between the respective business models."

A **Richard Child, member of the Financial Services Advisor board and CEO of Mattrix Group:** "Over the past five years or so, we have seen a decline in the number of credit cards and a slight increase in the issuance of debit cards. However, spending with credit cards continues to outpace that of debit cards, as the average per-transaction amount per credit card is higher than debit cards. Having said that, debit card transactions have a significant advantage over credit cards in that debit transactions are settled with the merchant the day after the transaction is made, versus credit cards, where payment to the merchant is made 30 days after the transaction date. The proposed changes in swipe fees will probably have a short-term effect on usage, with a probable run toward using debit cards over credit cards, but I do not think that will be long lived, as the acquiring banks will readily adapt and modify their pricing to balance out the market. Processors will most likely do the same. As for money laundering, I doubt that will be affected by the new fees, as I don't see a dramatic shift to debit card usage by customers, or merchants openly showing their preference for debit over credit cards. Another factor to take into consideration is that credit cards have an approximate activity rate of 56 percent versus 32 percent for debit cards, according to Brazilian central bank figures. In a perfect world, a drop in debit card fees would lead to a substantial increase in the use of debit cards, but I think customers will continue to use their debit cards for small-ticket items and their credit cards for larger expenses."

A **Natan Rodeguero, regional head for Latin America at M-Brain in São Paulo:** "Even before 2010—when the card processing industry was opened to competition in Brazil after years of a duopoly—Brazilian retailers have complained about the fees they need to pay when customers swipe their debit cards. This long battle, though, has not produced many results, as the fees are still in place, ranging from 1 percent to 3 percent of the value of the transaction, on top of the value to rent (or buy) the 'card machine.' Retailers argue that the same fees are around 0.6 percent in the United States, severely overlooking the fact that 85 percent of transactions in the United States—a huge volume that allows for smaller percentage fees—are made through cards, versus 29 percent in Brazil. Also, retailers request that the fees become fixed, per transaction, not dependent on the value purchased. Having the central bank cap such fees may do little to reduce the total cost for consumers, as retailers will most certainly maintain product prices in order to improve their margins. Similarly, it is utopic to think consumers will favor cards in order to make them less prone to suffer violence by carrying cash. Likewise, money laundering will not stop because a cheaper (electronic) payment method is in place—dirty money will most certainly continue to circulate off the books. Indeed, card processing firms may suffer the most impact, as the increase in card usage may not be compatible with the reduction in transaction fees."

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ly in a year with presidential elections in key countries scheduled. "Rising U.S. protectionism may end up providing support to sectoral views that oppose the integration of Latin America into world markets, a process that has contributed to economic growth as well as to poverty and inequality reduction," the Latin American Committee on Macroeconomic and Financial Issues, a group of regional economists, said in a report last April. According to estimates cited by Lloyd's, Mexico's economy could be larger than the United Kingdom's within 15 years, assuming current economic policy remains in place. Meanwhile non-life insurance penetration in Latin America is just 1.8 percent, according to Lloyd's. In related news, Lloyd's suffered the most losses among major property/casualty insurers due to last year's three devastating hurricanes that hit the Americas, taking a $4.8 billion hit due to the third-quarter storms, A.M Best said last month. Swiss Re, Munich Re and Berkshire Hathaway also suffered more than $3 billion each in losses due to hurricanes Harvey, Irma and Maria.

POLITICAL NEWS

Peruvian Court Orders Fujimori to Stand Trial

A Peruvian court on Feb. 19 ordered former President Alberto Fujimori to stand trial in a case involving the killings of six farmers in 1992, during his presidency, Agence France-Presse reported. Fujimori had been serving a 25-year prison sentence when current President Pedro Pablo Kuczynski pardoned him in December, citing his poor health. However, the National Criminal Court ruled that the pardon did not apply to the murders of the farmers. Prosecutors had asked the court to try Fujimori and 23 others in connection with the death-squad killings of the farmers, and the court ruled that Fujimori did not have immunity from prosecution. The jail sentence Fujimori had been serving until December followed his conviction for crimes including commanding death squads that killed civilians who were sympathetic to the left-wing guerrillas that Fujimori's government was fighting. Kuczynski's pardon of Fujimori was widely criticized and led to street protests. Many saw the pardon as payback after Fujimori's son Kenji Fujimori, a member of Congress, helped Kuczynski survive an impeachment attempt over corruption allegations Alberto Fujimori has said he is innocent and will appeal the court's ruling, BBC News reported. The former president's daughter, Keiko Fujimori, who unsuccessfully ran for

THE DIALOGUE CONTINUES

Have Natural Disasters Dealt a Blow to Latin America's Insurance Sector?

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 Thomas Morante, member of the Financial Services Advisor board and partner at Holland and Knight, and Yani Contreras, attorney and consultant on the Financial Services Team of Holland & Knight: "Insurance companies covering property and casualty risks in Latin America and the Caribbean are expected to report losses this year resulting from the natural disasters that affected the region last year. These losses will inevitably trigger an increase in insurance and reinsurance premiums in 2018, but likely will not endanger the operations of these insurers, given the sector's profitability in the past few years. In Mexico, the earthquakes last September caused damages not only in Mexico City, but also in the states of Oaxaca, Chiapas and Morelos, where there is low penetration of property insurance. Insurance companies can handle the losses derived from these earthquakes because they have sufficient technical reserves and a special reserve for earthquake-related losses, and because generally up to 80 percent of this earthquake risk was ceded to international reinsurers. In Mexico, only about 5 percent of properties are insured, but these recent events may change risk management tolerance. The demand in Mexico for property and car insurance against earthquakes and other natural disasters is expected to grow 100 percent or more in 2018. In an immediate response to the tragedy, demand for earthquake coverage grew up to 200 percent last October. However, a decline within two or three years can be expected since policyholders traditionally don't renew long-term contracts and will likely stop paying premiums. Among other insurance coverage developments, the Mexican Institute of Insurance Companies, or AMIS, intends to engage in a lobbying effort to pursue a bill to make property insurance mandatory for condominiums. In spite of these natural events, insurance companies are expected to continue expanding in Mexico's insurance market, which is projected to increase 7 percent this year."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in the Jan. 25-Feb. 7 issue of the Financial Services Advisor.

NEWS BRIEFS

Brazil Shelves Plans to Overhaul Pension System

Brazil's government has shelved plans to overhaul its pension system, a reform that economists have seen as critical to the country's long-term financial health, the Financial Times reported Feb. 20. The first vote on the reforms had been planned for this month in the lower house, but President Michel Temer on Feb. 16 handed control of Rio de Janeiro's security to the military amid a wave of violent crime. The move blocked the reform as the country's Constitution cannot be amended during a military intervention.

Thirteen Killed in Mexican Military Helicopter Crash

Thirteen people, all on the ground, were killed Feb. 16 when a military helicopter crashed in southern Mexico as officials were surveying damage from the 7.2-magnitude earthquake that struck the country earlier in the day, The Wall Street Journal reported. Fifteen others were injured. The helicopter, which was attempting to land in the town of Santiago Jamiltepec, was carrying Mexican Interior Minister Alfonso Navarrete and Oaxaca Governor Alejandro Murat, neither of whom were seriously injured.

Peru, Australia Sign Free-Trade Deal

The governments of Peru and Australia on Feb. 13 signed a new trade deal following nine months of talks, China's state-run Xinhua news agency reported. Negotiations for the Peru-Australia Free-Trade Agreement, or PAFTA, opened last May. The time span of the talks was the shortest for any trade accord that Australia has ever concluded. The deal, which was signed in Canberra, will eliminate tariffs on 99 percent of Australian goods that are exported to Peru within five years. The accord is expected to make Australia one of Peru's largest suppliers of sugar within 18 years.

president in 2016, expressed confidence that her father would be found not guilty. She urged that the court's decision "not be an excuse to jail a man of advanced age and fragile health." She added, "Alberto Fujimori deserves to confront this while free." Prosecutors are seeking a 25-year prison sentence for Alberto Fujimori on the latest charges, AFP reported.

Maduro Vows to Attend Summit Though Disinvited

Venezuelan President Nicolás Maduro on Feb. 15 said he will attend the Summit of the Americas in April, even though Peru, the gathering's host, withdrew his invitation, Agence France-Presse reported. "Are they afraid of me? They don't want to see me in Lima? They're going to see me, come rain, thunder or lightning!" Maduro defiantly said at a press conference in Caracas. Maduro vowed to get to Peru for the summit "by air, land or sea." Peru's prime minister, Mercedes Araoz, said Maduro was mistaken. "A head of state cannot come to a country without an invitation, so he cannot get to step on Peruvian soil without an invitation," Araoz told reporters. She described the Venezuelan president's attitude as "aggressive" and added, "neither the Peruvian soil, not the Peruvian sea, nor the Peruvian air can be invaded by a foreign force." On Feb. 14, Peru's government announced that Maduro would "no longer be welcome" at the April 13-14 summit. The government announced the decision after Venezuela said that it would proceed with a snap presidential election on April 22 despite not having reached an agreement with the opposition on how to conduct the balloting freely and fairly. Peru's decision to withdraw Maduro's invitation followed a meeting of the 14-nation Lima Group, which was formed to seek a peaceful exit to Venezuela's political and economic crises. The Lima Group urged Venezuela to reconsider holding the April 22 vote, saying conditions for a free and fair election did not exist. Maduro also lashed out at the bloc. "In Venezuela, Venezuelans are in charge, not the Lima Group," he said. "Not [Peruvian President] Pedro Pablo Kuczynski, not [Colombian President] Juan Manuel Santos." Several Peruvian political parties have called a demonstration for April 12, on the eve of the summit, against Maduro's government, MercoPress reported. In addition, Mexican Foreign Minister Luis Videgaray plans to travel next month to Jamaica, Grenada and Saint Lucia as part of an effort to erode Maduro's influence in the Caribbean, Reuters reported, citing a Mexican official. Also, Cuban diplomats are planning to visit Mexico next month to discuss the regional impact of Venezuela's crises. The Cuban Embassy in Mexico City said the trip was not yet confirmed, but added that the two countries have held bilateral meetings. There was no sign that Havana was planning to turn against Venezuela, a steadfast ally.

Guatemala's Colom, Cabinet Members Accused of Graft

Guatemalan officials on Feb. 13 arrested former President Álvaro Colom and former Finance Minister Juan Alberto Fuentes Knight, who is now the chairman of international development confederation Oxfam International, as well as nine other former members of Colom's cabinet, on corruption charges, The New York Times reported. Prosecutors said $35 million in government funds had been transferred to a consortium of private bus companies known as Transurbano in a deal approved by Colom, Fuentes Knight and other ministers, without proper legal oversight. Nearly a third of the money was spent on equipment that was never used, and it is unclear where the rest of the funds went. Colom is the fourth former president of Guatemala to face charges of corruption due to investigations headed by the United Nations-backed International Commission against Impunity in Guatemala, or CICIG. In related news, the leader of the Organization of American States' anti-corruption mission in Honduras resigned Feb. 15, saying he was not receiving enough support from the OAS and from the Honduran government, the Associated Press reported.

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A **Lindsay Lehr, senior director at Americas Market Intelligence:** "A cap on debit card fees for merchants in Brazil will most certainly not have a direct effect on consumers' habit of carrying high volumes of cash. There may be a residual outcome in the long term, a result of more merchants accepting debit cards, but a cap on debit card fees will most likely not have any effect on consumers in the short term. When debit card fees are capped, merchants win, and card processors and issuers lose. This may incentivize more merchants to accept debit cards, which affects consumers indirectly; it will also put pressure on both issuers and processors to trim the fat and cut costs. It may benefit digital-only banks with much lower overhead costs than traditional debit card issuers. Since the greatest barrier to overall card acceptance in emerging markets, including Brazil, is high fees, reducing debit swipe fees for merchants will help promote financial inclusion among longtail merchants and contribute toward the penetration of electronic payments throughout the economy. This should be considered a medium-term outcome, however."

> **"In many cases, regulations on swipe fees result in the consumer being the victim."**
>
> **— Jordan McKee**

A **Jordan McKee, principal analyst for payments at 451 Research:** "Capping swipe fees can have unintended consequences. The card payments ecosystem is unlikely to sit idly by while a major revenue stream is throttled. As we saw in the United States when the Durbin Amendment (as part of the Dodd-Frank Act) capped debit card transaction fees, banks simply looked elsewhere to make up the lost revenue. This resulted in more service fees for bank customers, the widespread elimination of free checking accounts and major cutbacks on debit card rewards programs. In many cases, regulations on swipe fees result in the consumer being the victim."

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

Advisor Video

Piñera's Second Term

An Inter-American Dialogue discussion with Robert Funk of the University of Chile, Gabrielle Trebat with McLarty Associates and Sergio Urzua of the University of Maryland

View a webcast of the Feb. 15 discussion.

PLAY

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