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FEATURED Q&A

How Have Natural Disasters Affected Insurance Providers?



Recent natural disasters have prompted insurance providers to examine their businesses in Latin America and the Caribbean. Damaged buildings in the town of Juchitán in Oaxaca state, following Mexico's Sept. 7 earthquake are pictured above. // Photo: Mexican Government.

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, 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

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TODAY'S NEWS

POLITICAL

Brazil's Congress Approves Military Policing in Rio

Lawmakers signed off on a decree from President Michel Temer that puts the military in charge of security in Rio de Janeiro amid rising crime in the city.

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BUSINESS

PREPA Gets Approval for \$300 Mn Loan

A U.S. federal judge approved a loan for the beleaguered commonwealth-owned Puerto Rico Electric Power Authority in order to help it pay expenses.

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ECONOMIC

Venezuela Says New Digital Currency Raises \$735 Million

The first day of the pre-sale of Venezuela's new digital currency, the petro, raised \$735 million, the government said. President Nicolás Maduro said the petro would be a "big solution" for the country's economic problems.

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Maduro // File Photo: Venezuelan Government.

POLITICAL NEWS

Brazil's Congress Approves Policing by Military in Rio

Brazil's Congress late Tuesday approved a presidential decree to place the military in charge of the security forces in Rio de Janeiro, which has been facing rising levels of crime, the Associated Press reported. The Senate approved the measure shortly before midnight, following similar action by the lower house earlier in the day. President Michel Temer issued the decree last week, and the military took over Rio's police force on Friday, but the action still needed congressional approval. In opening the debate, the lower chamber's president, Rodrigo Maia asked lawmakers to support the measure, the Rio Times reported. "We are living a war on crime, and the Constitution is our weapon," said Maia. However, lawmaker Chico Alencar, a member of the PSOL party and a deputy for Rio, sought to postpone the vote, arguing that there was not enough information about the financial resources available for the operation. The measure was approved following seven hours of debate. On Monday night, the armed forces fanned out in Rio in their first major

operation since Temer issued the decree. Soldiers were positioned on major roads that connect the city with the rest of the country as part of an effort to keep illegal weapons, drugs and stolen goods from entering Rio de Janeiro, the AP reported, citing Col. Roberto Itamar, a military spokesman. Some 3,000 members of the military were involved in the operation. Armored vehicles also rolled through at least one neighborhood in Rio, while boats were seen patrolling the waters. Soldiers and police officers searched people entering and leaving the city on Tuesday morning. By Tuesday night, authorities had detained 11 people and had seized six guns, six grenades and a large quantity of drugs, according to Rio's state security department.

ECONOMIC NEWS

Venezuela Says Digital Currency Sale Raises \$735 Mn

Venezuela's government announced Tuesday that the pre-sale of its new "petro" digital currency raised \$735 million on its first day, the Financial Times reported. The petro is backed

NEWS BRIEFS

At Least 25 Killed as Bus Plunges From Highway in Peru

Peruvian authorities said at least 25 people were killed and 20 others wounded when a bus drove off a cliff early this morning near the Ocoña bridge at kilometer 780 of the Panamericana highway in Arequipa, state news agency Andina reported. Jacqueline Choque, head of Arequipa's civil defense unit, said that the vehicle belongs to the Rey Latino bus company and departed from Chala in the province of Caravelí last night bound for the city of Arequipa. But at about 1:30 a.m. local time, the bus overturned and plunged approximately 80 meters.

Principal Financial Completes Acquisition of Mexico's MetLife Afore

Iowa-based Principal Financial Group on Tuesday announced it has completed its acquisition of MetLife Afore, a pension fund management business in Mexico. The deal makes Principal Afore the fifth-largest pension manager in Mexico, with a more than 7 percent market share, the company said. MetLife Afore clients will become part of Principal Afore within the next 90 days.

Southern Copper Wins Tender for Peru's Michiquillay Copper Mine

Peru's government announced Tuesday that Southern Copper, the mining firm held by Grupo Mexico, had won the tender to develop Peru's massive Michiquillay copper mine, Reuters reported. The auction, which reportedly had as many as 10 companies pre-register, in the end attracted just two bidders. Southern won with a proposal to transfer \$400 million to the government and pay 3 percent royalties, beating out Lima-based Compañía Minera Milpo, which had offered \$250 million in transfers and 1.875 percent royalties.

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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."



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

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by Venezuela's oil reserves, and a white paper on the currency said 100 million petro coins will be issued. Of that amount, the government plans to sell 38.4 million through a pre-sale, with a \$60 reference price. The pre-sale is scheduled to last until March 19. The government plans to sell an additional 44 million coins in an initial offering, scheduled to start on March 20. In a tweet late Tuesday, President Nicolás Maduro said the currency would be a "big solution" to Venezuela's economic problems. [Editor's note: See [Q&A](#) about the petro in the Jan. 31 issue of the Advisor.]

BUSINESS NEWS

Mexico's Televisa Reports Decline in Profit for Q4

A decline in advertising sales pushed quarterly net profit at Mexican broadcasting giant Grupo Televisa down 12.5 percent from a year ago, Reuters reported Tuesday. Televisa posted net profit of 563 million pesos (\$28.6 million) and net sales of 26.1 billion pesos during the fourth quarter ending in December. A new

A new advertising pricing plan based on television show ratings likely hurt sales.

advertising pricing plan based on television show ratings likely hurt sales, analysts said. Established broadcasters such as Televisa have also been facing increased competition from Internet-based streaming services. The company has announced plans to sell assets in order to focus on content and distribution. Last week, Televisa said that it had agreed to sell its 19 percent stake in Spanish media group Imagina for approximately \$350 million. Imagina markets rights to sporting events including the Spanish soccer league and produces television content and films. The stake is part of the 53.5 percent of Imagina being acquired by Chinese

THE DIALOGUE CONTINUES

Will Venezuela's Proposed Digital Currency Succeed?

Q **The U.S. Treasury in mid-January warned U.S. investors to approach Venezuela's proposed "petro" with caution, saying the proposed oil-backed digital currency may conflict with U.S. sanctions against the Venezuelan government. The week before, Brazil's securities regulator prohibited local investment funds from buying cryptocurrencies, saying they could not be considered financial assets. To what extent will Venezuela succeed in using the new "petro"? Will investors from other countries accept the petro from Venezuela if the United States blacklists it? How will the recent increase in the global price of oil affect the proposed currency ahead of its introduction?**

A **Alexander Guerrero, associate professor of economics at UNIMET in Caracas:** "The petro is just like any ordinary parallel currency, but this one is government-issued. It is not a cryptocurrency either, since it is not mined. It is more like a government bond. It emulates 'legal tender,' or currencies similar to those issued by central banks.

private-equity firm Orient Hontai Capital, The Wall Street Journal reported. Last month, Televisa's longtime top executive, Emilio Azcárraga, stepped down from the CEO position, which was assumed by vice presidents Alfonso de Angoitia and Bernardo Gómez as co-CEOs. Azcárraga remains chairman of the board.

Puerto Rico's Power Utility Gets Approval for \$300 Mn Loan

The Puerto Rico Electric Power Authority has received a judge's approval to get a \$300

million loan in order to help pay expenses at the beleaguered commonwealth-owned electric company, Reuters reported Tuesday. U.S. District Court Judge Laura Taylor Swain approved the loan for the utility, better known as PREPA. The federal board that is overseeing Puerto Rico's debt restructuring had originally sought a \$1.3 billion loan after Hurricane Maria battered the island last September, cutting off power to much of the territory. However, creditors opposed that initial amount over its size and terms, and the two sides argued the issue in court. The judge reduced the loan amount to \$300 million. Puerto Rico has more than \$70 billion in debt, and PREPA has in excess of \$14 billion in liabilities.

“The petro, as parallel currency, will not help to resolve Venezuela's financial collapse...”

— Alexander Guerrero

will not help to resolve Venezuela's financial collapse, which has been caused by a dual crisis, a huge balance of payments deficit and an irreparable fiscal crises, which have provoked today's hyperinflation.”

EDITOR'S NOTE: The comment above is a continuation of the [Q&A](#) published in the Jan. 31 issue of the Advisor.

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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, 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 them."

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

“**The potential of cat bonds has not yet been fully realized in part because they remain expensive.**”

— Eduardo Cavallo

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 Inter-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."

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

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