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FEATURED Q&A

Will Argentina's Economic Troubles Bedevil Banks?



Argentina's central bank, led by Guido Sandleris, last month increased banks' reserve requirements. // File Photo: @gsandleris via Twitter.

Q Argentina's central bank on Sept. 29 raised banks' reserve requirements in an effort to rein in inflation following a revised lending agreement with the International Monetary Fund. How will the move affect Argentina's banks? How will banks in Argentina fare as the country grapples with a recession, currency pressures and inflation that is expected to exceed 40 percent this year? What should Argentine banks do to bolster their businesses amid the country's economic woes?

A Santiago Gallo, director for Latin American financial institutions at Fitch Ratings: "Fitch expects the recession in Argentina to have a negative impact on the banking system's performance as slower loan growth, high inflation, soaring interest rates and recent strong peso depreciation will affect profitability and asset quality. This will likely have a marked impact on the banking system's previously aggressive growth plans for at least 2018 and 2019. However, higher liquidity requirements by the central bank and slower loan growth will be compensated, at least partly, by a likely wider net interest margin, as most banks will benefit from the significant rise in interest rates since more than half of total deposits are non-interest-bearing sight deposits. While loan growth potential remains high in Argentina, given low levels of credit penetration, growth will be much lower than previously anticipated, and the tough economic situation will likely lead to some asset quality deterioration, although the system's impaired loans remain at low levels and loan loss reserve coverage is adequate. In addition, capitalization of most Argentine banks is adequate, with a Fitch Core Capital ratio

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TOP NEWS

BANKING

Mexico's Banorte Reports 26% Rise in Q3 Profit

The Mexican bank reported \$417 million in net profit for the third quarter. The report was the first that included results from Banorte's recent acquisition, Grupo Financiero Interacciones.

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CREDIT CARDS

Visa Announces Investment in Brazil's Conductor

The card processor is making a minority investment in the Brazilian digital payments server. The platform allows companies to issue payment cards and digitize payments.

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BANKING

Sale of Chile Unit Boosts Earnings at Spain's BBVA

The sale of BBVA Chile boosted the bank's profit in the third quarter. CEO Carlos Torres Vila said the bank also saw a "challenging" situation in Argentina, but added that its geographic diversification aided results.

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Torres Vila // File Photo: BBVA.

FINANCIAL SERVICES NEWS

Sale of Chile Business Unit Boosts Earnings at Spain's BBVA

The sale of a business unit in Chile boosted Spanish lender BBVA's earnings in the third quarter, with the bank reporting a 46 percent increase in net profit, the Financial Times reported Oct. 30. The sale helped to offset a loss that BBVA took related to its business in Argentina. BBVA reported 1.67 billion euros (\$1.9 billion) in net profit for the third quarter, an amount that was in line with analysts' expectations. For the first nine months of the year, BBVA's profit was 4.32 billion euros, 25.3 percent higher than the same period a year ago, the bank said. BBVA recorded a 633 million euro capital gain due to its sale of BBVA Chile and a charge of 190 million euros to adjust to Argentina's inflation. BBVA's chief executive officer, Carlos Torres Vila, said that while the bank experienced a "challenging" situation in Argentina as well as in Turkey, the "results we are presenting today reveal the strength of our business model and geographic diversification." In Turkey, BBVA said the "macroeconomic environment prompted an increase in impairment losses on financial assets and cost of risk." BBVA's latest earnings report was a "decent set of results," said analysts at Jefferies, who added that the bank saw a stronger-than-expected performance in Mexico, which helped to make up for weaknesses in other parts of the business.

Julius Baer Closing Units in Panama, Peru: Report

Julius Baer Group is closing its operations in Panama and Peru as part of a strategic review of its Latin America branches, Bloomberg News reported Oct. 23, citing a spokeswoman for the private bank. Beatriz Sánchez, head of the Swiss bank's Latin America business, has been reviewing the Panamanian unit as

part of an overall regional evaluation. Julius Baer manages roughly 40 billion Swiss francs, or \$40 billion, in assets in Latin America. The Panamanian business came under scrutiny after a former employee, Mathias Krull, was arrested in connection with a billion-dollar money laundering scheme involving Venezuelan state oil company PDVSA. In August, Krull pleaded guilty to participating in a plan to launder \$1.2 billion from PDVSA, a scheme that prosecutors have said involved banks, real estate firms and money managers and brokerages. Krull is currently awaiting his sentence. Julius Baer has said it is undergoing an internal probe, though the bank has not been charged.

Laub Resigns as Chief Executive of Credicorp Capital

Peruvian financial holding company Credicorp Capital's chief executive, Christian Laub, resigned from his post after more than six years with the firm, El Comercio reported Oct. 19. The move came as Credicorp seeks to expand its wealth management brand across other countries in Latin America. "Credicorp has strengthened its regional model and is now in a new stage of consolidation and integration with its Peru wealth management business, which



Laub // File Photo: Credicorp Capital.

brings along structural changes that will allow us to continue bolstering the service offering for all the clients in Chile, Colombia and Peru," the financial company said in a statement after announcing Laub's resignation in a regulatory filing, CityWire reported. Eduardo Montero, who currently serves as Credicorp's wealth management head, will replace Laub when the

NEWS BRIEFS

Mexico's AMLO Vows Safe Environment for Banks

Mexican President-elect Andrés Manuel López Obrador on Oct. 22 told Banco Santander's executive chair, Ana Botín, that his government will create a safe environment for banks because "we need the investment," Reuters reported. Santander committed to an investment of 15 billion pesos (\$773 million) in Mexico between 2017 and 2019. The same day, Botín said the Spanish bank plans to continue investing in Mexico. López Obrador will take office on Dec. 1.

Ecuador's Moreno Orders Probe Into Bank Charges

Ecuadorian President Lenín Moreno has ordered the country's banking oversight agencies to initiate a probe into banks and financial services companies that clients claim have unduly charged them, El Comercio reported Oct. 17. Customers of Ecuadorian banks have been using social media to complain about charges to their bank accounts and credit cards made without their authorization. "We will not tolerate any damage to the pockets of Ecuadorians by companies that may be behaving unscrupulously," Moreno said at an event in Quito, El Comercio reported.

Mexico's Banorte Reports 26% Increase in Profit for Third Quarter

Mexico's Banorte reported a net profit of 7.82 billion pesos, or \$417 million, in the third quarter, a 26 percent increase from the same period a year ago, Reuters reported Oct. 19. Moreover, the Mexican bank said consumer credit and demand for autos and housing boosted its loan portfolio by 25 percent, in comparison to the third quarter last year, to 751.7 billion pesos. It was the first report that included the results of Grupo Financiero Interacciones, which Banorte acquired earlier this year.

changes take effect on Jan. 1. The firm had undergone structural changes last year, merging the wealth units of Credicorp and of its sister bank Banco de Crédito del Peru, or BCP, into a single division to bring BCP's advisory business to Colombia and Chile, the wire service reported. Montero, who previously led BCP's \$11 billion advisory wing, was named head of the combined unit last July. Mariano Baca, who currently manages BCP's corporate banking unit, will take Montero's place, according to a spokesperson for Credicorp, CityWire reported.

CREDIT CARD NEWS

Visa Announces Investment in Brazil's Conductor

Visa on Oct. 23 announced it is making a minority investment in Brazilian digital payments server Conductor, a move designed to help it accelerate the growth of payment innovation in the South American country, Visa said in a statement. Conductor, a platform that allows retailers, banks and other companies to issue cards and digitize payments, has roughly 100 customers and 135,000 commercial establishments across Brazil, Valor Econômico reported. It started out as a card-processing business 20 years ago, but the company has grown fourfold since private equity fund Riverwood Capital invested in it in 2014. Conductor and Visa plan to develop solutions for payments via mobile wallets, improving access to Visa applications and expanding digital payment services in small- and medium-sized businesses, among others. "Through our investment in Conductor, we are reinforcing our commitment to significantly invest in attractive fintechs and key digital enablers from Latin America and the Caribbean," Ruben Salazar, senior vice president of products and innovation at Visa Latin America & Caribbean, said in the statement. Fernando Teles, Brazil's country manager at Visa, earlier this month said he was aiming to boost the company's market share in the South American country. In 2010, Visa handled approximately

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consistently above 12 percent for most large banks. In Fitch's view, while pressures on loan quality and profitability remain as key risks, cyclical deterioration is unlikely to affect the banks' ratings. However, as most of the largest banks' ratings are constrained by the sovereign ratings, bank rating actions will mirror those of the sovereign."

A **Cynthia Cohen Freue, director and sector lead for financial institutions ratings at S&P Global in Buenos Aires:** "The

central bank of Argentina is fighting inflation by reducing the pesos in circulation, keeping the monetary base constant, increasing reserve requirements and increasing interest rates. These measures have varying effects on banks' profitability: on the one hand, the increase in reserve requirements has a negative impact on banks' interest margins because part of them are not remunerated. But on the other hand, the increase in interest rates on central bank notes has a positive effect on their profitability. In addition, these measures, combined with the reduction of government expenditures with the intent to reduce the fiscal deficit, have recessionary effects on the economy. This, together with the still very high inflation expected for the year, will definitely affect banks' asset quality metrics, which are already showing signs of rapid deterioration. This will also have a negative effect on banks' profitability, as they will need to raise provisions. That said, we believe Argentine banks have had conservative strategies since the 2002 crisis, which will help them cope with the difficult economic conditions and volatile exchange rate, including focusing on higher income segments and corporates (resulting in a low penetration) and only lending in dollars to exporters or dollar generators. Moreover, healthy profitability levels will help them manage the increasing provisioning requirements. Banks most likely will implement conservative underwriting practices, limiting

their exposure to the most vulnerable segments such as small and middle enterprises, while offering credit to the higher income segment and large corporates; and limiting

“**Argentine banks have had conservative strategies since the 2002 crisis...**”

— Cynthia Cohen Freue

the focus on UVA-denominated loans. As a result, we expect to see a reduction in the share of loans on banks assets while an increase in securities.”

A **Valeria Azconegui, vice president and senior analyst at Moody's Investors Service:** "The most significant risks that Argentina's economy faces are related to rising inflation, extraordinarily high interest rates and the ensuing decline in economic activity, which we foresee will continue reducing banks' lending growth over the next year as the recession deepens and the monetary policy becomes much more restrictive. To contain the peso's rapid depreciation, the central bank has raised interest rates by nearly 40 percentage points to 71 percent annually (103 percent effective rate), as of Oct. 3, from an already very high 27.25 percent in April. This has led to a doubling of interest payments on variable-rate and new short-term loans, which together represent a significant part of the banks' loan book. In addition to raising interest rates, the central bank has also significantly increased average deposit reserve requirements to 41 percent in mid-September from 28 percent in late July, to absorb excess liquidity. Despite the remarkable rise in interest rates and reserve requirements, annual inflation surged

Continued on page 6

half of all card transactions in Brazil, but by last year had only 36 percent of the market share, according to central bank data.

ECONOMIC NEWS

López Obrador Vows to Halt Mexico City Airport Project

Mexican President-elect Andrés Manuel López Obrador on Oct. 29 said he will halt the construction of a new airport that has been planned for Mexico City, El Universal reported. The announcement followed Mexicans' rejection of the project in a referendum. "The decision that citizens made about the new airport is rational, democratic and efficient," López Obrador told reporters. "The decision is to obey the mandate of the citizens." López Obrador, who takes office Dec. 1, has long criticized the \$13 billion project, which he has blasted as being marred by corruption, Agence France-Presse reported. Business leaders have said a new facility is needed in order to ease traffic at the capital's current airport. Instead of continuing with the new airport's construction, López Obrador said the current airport could be upgraded and that two runways could be built at the nearby Santa Lucía airbase.

Chile's Piñera Releases Pension Reform Plan

Chilean President Sebastián Piñera on Oct. 28 released his long-anticipated plan to reform the country's once-lauded pension system, Reuters reported. In a bid to boost payouts for increasingly agitated retirees who had come to expect larger withdrawals upon retirement, Piñera said in a televised address that he would ask employers to pay for an additional 4 percent contribution to each of their workers' pension accounts. The government also would boost its contribution to a collective fund to 1.12 percent

ADVISOR Q&A

Will Bolsonaro Bring Big Changes to Brazil?

Q Far-right candidate Jair Bolsonaro won the Oct. 28 presidential election in Brazil, defeating Fernando Haddad of the leftist Workers' Party in a runoff with just over 55 percent of the vote, as compared to just less than 45 percent for Haddad. Bolsonaro takes office Jan. 1. What factors led to his victory? What are the top items on the agenda for his presidency, and can voters expect the kind of sweeping change the candidate has promised? To what extent will Bolsonaro's history of controversial statements, including about torture, women, blacks and gays, translate to policy? What will Bolsonaro's presidency mean for investment in Brazil, as well as the country's economy and businesses?

A Peter Hakim, president emeritus of the Inter-American Dialogue: "The election highlighted the bitter rifts in Brazilian society, reflecting regional, racial, religious and income differences. Nearly half of voters favored the Workers' Party (PT), evidence that Lula would have been returned to power if allowed to run. The majority of voters favored Bolsonaro, who wants Lula imprisoned and the PT quashed. Often called the tropical Trump, Bolsonaro and the U.S. president have similarly volatile and aggressive temperaments. They are both tough guys who split the world into 'us' and 'them' and are extremely belligerent toward the 'them' in order to incite and mobilize the 'us.' Order and hierarchy are values they share—along with an indifference to democracy, human rights and international cooperation. But Bolsonaro

of gross domestic product from 0.8 percent, while kicking in additional funds for the middle class, women and those who delay retirement, according to the report. Workers would be able to select from a wider diversity of for- and

confronts more difficult terrain. When Trump took office, the United States was far healthier and more secure than Brazil today. The American economy had grown steadily for eight years, while Brazil has remained mired in an economic slump since 2014. Yes, many Americans are angry and distrustful of government, but President Obama left office with a 53 percent approval rating. The current Brazilian president, like his predecessor, will depart with single-digit approval. Americans may be skeptical of their leaders and institutions, but Brazilians hold theirs in contempt. Problems of public security and corruption affect both countries, but only Brazil's threaten the political order. Moreover, Trump quickly assumed control of the Republican party, with its majorities in the House and Senate, giving him a vital base of power. Bolsonaro starts with the second largest party in Congress, but it includes only 10 percent of legislators. He needs to assemble an ample party coalition to pass essential legislation. In short, Bolsonaro will confront a much more difficult agenda than Trump, with a much weaker power base. The biggest threat to Brazil and its democratic institutions is not Bolsonaro's extremist, hardline views—but rather the fact that he may lack the competence and authority needed to effectively confront the economic and governance crises battering Brazil."

EDITOR'S NOTE: More commentary on this topic appears in the Oct. 30 issue of the Latin America Advisor.

non-profit fund managers, thereby boosting competition in the industry, Piñera added. The plan, which has an overall price tag of \$3.5 billion, will be phased in gradually. Employees can choose to work with one of six private pen-

NEWS BRIEFS

Bolsonaro Intends to Tap Moro for Justice Minister or Supreme Court

Brazilian President-elect Jair Bolsonaro said Oct. 29 that he plans to tap the country's top anti-corruption judge, Sérgio Moro, as his justice minister or for a seat on the country's Supreme Court, Mercopress reported. Moro would be a person "of extreme importance in a government like ours," Bolsonaro, who was elected in the Oct. 28 runoff election, said in a television interview. Moro has overseen the massive Car Wash corruption case.

Venezuela's Socialists Reportedly Seeking Dialogue With Opposition

Venezuela's ruling Socialist Party has reportedly sought to re-establish a dialogue process with the opposition in recent weeks, according to four unnamed sources involved in the effort, Reuters reported Oct. 29. A source from an opposition group told the wire service the government, with President Nicolás Maduro's support, had made the first move to seek dialogue. Venezuela's information ministry did not respond to a request for comment. Three opposition parties recently issued a statement openly opposing any dialogue with the government.

IMF Boosts Argentina Loan Deal to \$56.3 Billion

The International Monetary Fund on Oct. 26 agreed to increase the amount of its standby loan agreement to Argentina to \$56.3 billion while toughening previously agreed upon measures to bring the South American country's fiscal deficit, which stands at an estimated 2.7 percent of GDP, to zero next year, Reuters reported. IMF Director Christine Lagarde applauded a budget proposal recently approved by Argentina's lower house of Congress, saying it would help the government meet its targets.

sion fund administrators currently operating in the country, known as AFPs. In recent years, a wide-ranging social movement demanding the end of the AFP system has resulted in protests. Chile's Congress must approve the changes before they can be implemented. [Editor's note: See related [Q&A](#) in the March 23 issue of the daily Latin America Advisor.]

POLITICAL NEWS

U.S. Sending 5,200 Troops to Southern Border

The United States is sending 5,200 troops to its southern border with Mexico, including armed soldiers, the Pentagon said, as caravans of roughly 4,000 Central American migrants continue to trek north across Mexico, El Universal reported Oct. 30. The soldiers will be helping Customs and Border Protection "harden the southern border" by toughening security at and near legal entry points, according to Air Force



O'Shaughnessy // File Photo: U.S. Air Force.

General Terrence O'Shaughnessy, the Associated Press reported. Eight-hundred troops are already on the way, he added, with a total of 5,200 arriving by Nov. 2, the Associated Press reported. The number is more than double the 2,000 troops who are deployed in Syria. The soldiers being sent to the U.S.-Mexico border will join the more than 2,000 National Guardsmen that U.S. President Donald Trump had already sent there. The announcement of the deployment comes as Trump and other Republicans have made the mass migration a campaign issue just ahead of the U.S. midterm

congressional elections on Nov. 6. "This is an invasion of our Country and our Military is waiting for you!" Trump tweeted on Oct. 29. In an interview on Fox News the same day, he said the United States would build "tent cities" for asylum seekers and denied his focus on the migrants had anything to do with the elections. [Editor's note: See related [Q&A](#) on the migrant caravan in the Oct. 29 issue of the daily Latin America Advisor.]

U.S. on Path of Confrontation: Cuba's Rodríguez

The United States is on a path of "confrontation" with Cuba and is pressuring countries to reject Cuba's upcoming annual United Nations resolution, calling for an end to the U.S. embargo of the island, Cuban Foreign Minister Bruno Rodríguez told reporters Oct. 24, El Nuevo Día reported. Since Donald Trump became U.S. president last year, relations between the two countries have deteriorated with tighter U.S. travel and trade restrictions. The straining of relations followed former President Barack Obama's moves to thaw diplomatic relations including the opening of embassies in Washington and Havana. During the hour-and-a-half news conference in Havana, Rodríguez decried the Trump administration's tougher stance. "We regret the U.S. government is advancing on a course of confrontation with Cuba," he said, Reuters reported. A White House official recently said the administration was planning to increase economic pressure on Cuba's intelligence agency and military, the wire service reported. In his remarks to reporters, Rodríguez also said the United States is trying to win support for its embargo at the United Nations, where Cuba's government is expected to again call for the embargo's end. Rodríguez said the United States seeks to justify the embargo because of human rights concerns, while it "violates the human rights of the Cuban people." [Editor's note: See [Q&A](#) on Cuban President Miguel Díaz-Canel's recent trip to the United States in the Oct. 12 issue of the daily Latin America Advisor.]

FEATURED Q&A / Continued from page 3

to 34 percent in August from 25 percent in April, and we expect it to surpass 40 percent this year. Rising inflation and interest rates led the economy to shrink 4 percent in the second quarter, quarter-on-quarter adjusted for seasonality. We expect real GDP to contract 2.5 percent this year and 1.5 percent in 2019. In addition, the monetary base had been growing at a rate of 40 percent annually as of September. The central bank commitment to limit growth to zero between now and June 2019 will likely lead to even higher interest rates, higher minimum reserve requirements or both.”

A **Alfredo Félix Blanco, economist at the Universidad Nacional de Córdoba in Argentina:** “Argentina’s recent economic difficulties forced President Macri’s government into a new agreement with the International Monetary Fund. In an effort to restore financial markets’ confidence, Argentina assumed new commitments. Among them, there is a strong fiscal adjustment to achieve a primary balance in 2019 and a primary surplus in 2020. These imply a very deep adjustment of public finances to reduce the federal government’s financing needs. With reference to the financial system, the adopted measures tend to restrict the nominal amount of money of the economy (the monetary base

cannot increase during the next 12 months). Fortunately, the Argentine financial system, although relatively small, is solid and solvent. So it is possible to expect no serious problems for banks, but lending conditions will be more difficult. The main difficulties are for companies that must cope with very

“It is possible to expect no serious problems for banks, but lending conditions will be more difficult.”

— Alfredo Félix Blanco

high real interest rates. The economy has entered a recessive phase, and a short-term change of situation should not be expected. Argentina’s economic situation will be difficult at least for one year, and President Macri needs an improving economy next year ahead of the election. Also, there are many doubts that Argentina will be able to successfully fight its high inflation rate.”

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

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