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Featured Q&A with our Board of Advisors

Q Many observers say that establishing strong credit reporting agencies in Latin American countries could help expand access to credit. Do you agree? What are the biggest obstacles to creating or improving credit bureaus in the region and establishing a reliable system for verifying credit histories?

A **Board Comment: Jan Smith and Tricia Juhn:** "Building credit bureaus is only one of several aspects to expanding access to credit for Latin America. Credit bureaus will require transparency, reliability, flexibility, and openness. Systems should be transparent, so consumers understand how credit scores are derived and have the ability to dispute scores if need be. Reliability requires metrics that accurately reflect the real financial capacity of the bearer. To this end, credit bureaus must incorporate all lenders' files so as to not allow borrowers to over leverage themselves as occurred in the micro-finance meltdown of Bolivia. It should be flexible, in the sense that it should incorporate positive credit scores and allow entry of new players. Latin American credit bureaus are comparatively young and face a variety of challenges. Consumer credit archives across the region are thin on income statements and this is negatively reinforced by the large percentage of the population working and hiring off the books. Debt recovery legislation often continues to

favor borrowers, leaving creditors exposed and unwilling to invest in credit bureaus if little positive benefit is foreseeable. Most importantly, as Mexico exemplifies, many credit bureaus remain closed to new participants and legislation does not easily favor the creation of new bureaus nor the sharing of records between them."

A **Guest Comment: José Landa:** "In emerging economies, in general, and in Latin American countries, in particular, the use of credit is growing at a fast speed not only for consumers but also for enterprises.

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FEATURED PHOTO



Argentine President Nestor Kirchner and Venezuelan President Hugo Chavez on February 21 signed a memorandum of understanding to create a new development bank, Banco del Sur. See story on page 2.

Source: ABN

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INDUSTRY BRIEFS

Peru Ups Pension Funds' Foreign Investment Limit

Peru's central bank on February 8 said that it will raise the foreign investment cap for the country's pension funds, or AFPs, to 13.5 percent from the current 12 percent limit, Dow Jones News reported. Amid pressure from the mostly foreign-owned AFPs in the country, late last year the Central Reserve Bank increased the operating cap from 10 percent. The nominal cap, now at 20 percent, is set by congress.

Venezuela Expands Development Bank Presence in Latin America

Venezuela's state development bank, **Bandes**, is looking to expand its presence in Latin America this year, and President Hugo Chavez will also establish a new Latin American development bank, **Banco del Sur**, with his Argentine counterpart, President Nestor Kirchner. On February 21, Chavez and Kirchner met in Argentina—where the two leaders signed a number of accords aimed at fostering closer commercial and financial ties between the two South American countries—and signed a memorandum of understanding to create Banco del Sur, which aims to rival institutions like the World Bank and Inter-American Development Bank. "The Banco del Sur has to be [a bank] that has characteristics and philosophies different from some international banks that also were started to promote investments, but that turned into real punishments for the peoples [of the region]," Kirchner was quoted as saying by EFE. Chavez and Ecuadorean President Rafael Correa on February 8 signed several agreements aimed at increasing cooperation between the countries, including opening a **Bandes** office in Quito.

Banking News**Unibanco Net Income Up 20 Percent in 2006**

Unibanco, Brazil's third-largest non-government owned bank, announced February 14 that its 2006 net income was up 20 percent compared to the year before. The bank's net income, before the extraordinary event of goodwill amortization, was 2.21 billion reais (\$US 1.06 billion), up 20.2 percent when compared to 2005, the company said in a press release. In the fourth quarter of 2006, Unibanco's net

and **HSBC**, which regulators criticize for charging excessive fees and interest rates. The company said it plans to open 125 new retail stores this year and would increase investment in store expansions by 19 percent to 10.8 billion pesos (\$US 985 million), although that figure could be less due to new cost-cutting initiatives, such as energy-saving, and water and garbage recycling. Walmex Chairman and Chief Executive Eduardo Solorzano said that 58 of the 125 new stories will be **Bodega Aurrera** mega stores, Walmex's most suc-

“We will start very gradually, we won't open [bank branches] in 100 or 200 stores all at once.”

— *Julio Bosco, head of Walmex's banking operations*

income reached 576 million reais, boosted by an increase in its credit card loans portfolio, which grew 17.1 percent, as well as SME (small and medium sized enterprises) credit transactions, which were up 7.0 percent. In 2006, operating income increased 20.5 percent from 2005, reaching 3.52 billion. "Higher revenue generation and the expense rationalization resulted in an improvement of Unibanco's operational efficiency," the company said.

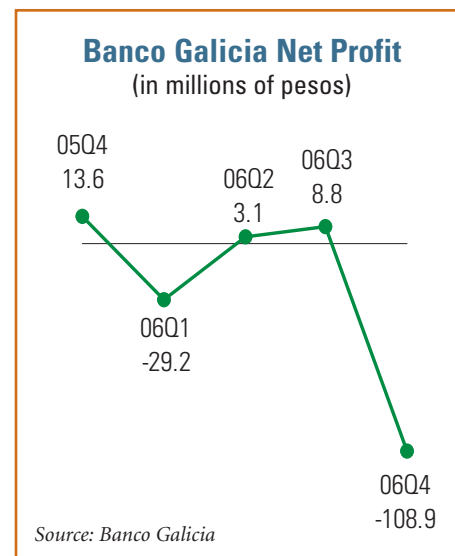
Walmex Plans to Have 60 Bank Branches in 2008

Wal-Mart de Mexico (Walmex), Mexico's biggest retail chain, said Tuesday it expects to have 60 in-store bank branches through 2008, Reuters reported. The company, a unit of US retail giant **Wal-Mart Stores Inc.**, recently received approval from Mexican regulatory authorities to offer banking services. "We will start very gradually, we won't open [bank branches] in 100 or 200 stores all at once," Julio Bosco, the head of Walmex's banking unit, was quoted as saying. The in-store bank branches, operating under the name **Adelante**, will target low-income customers. Walmex will compete against large multinational banks such as **Citigroup**

and successful supermarket format for low-income shoppers. Walmex has 897 outlets and has close to 142,000 employees.

Galicia's Year-End Profits Down on Debt Operation

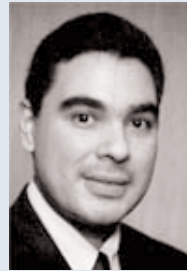
Argentine banking conglomerate **Grupo Galicia** on February 15 reported a 19 million-peso loss for 2006, compared to net profit of 107 million pesos in the previous year, citing a debt compensation operation between its bank, **Banco Galicia**, and the



country's central bank in the fourth quarter, Reuters reported. "The quarterly result is due mainly to the loss stemming from our involvement in Banco Galicia," the group said in a filing with the Buenos Aires stock exchange. For the fourth quarter, the group registered a net loss of 92 million pesos (\$US 30 million) in the fourth quarter, compared with net profit of 27.5 million pesos a year earlier. Banco Galicia's fourth quarter loss registered in at 108.9 million pesos, according to a press release posted on the bank's Web site. For the full year 2006, Banco Galicia registered a loss of 126 million pesos, according to the press release, compared to net profit of 191 million pesos in 2005.

Itau Q4 Net Down on Charges; Finalizes BankBoston Deal in Chile

Brazilian banking giant **Banco Itau Holding Financeira** last week reported consolidated net income of 1.28 billion reais (\$US 612 million) in the fourth quarter of 2006, according to financial information released on the bank's Web site. The figure reflects falling profits of about 10 percent compared to the previous quarter, according to Bloomberg News. In a press release, Itau explained that, by discounting the "non-recurrent effects" of operations like recent acquisitions, the bank's consolidated net income reached 1.62 billion reais in the fourth quarter, an increase of 2.3 percent compared with the recurrent net income of the third quarter. Itau has been expanding its credit card business in Brazil as well as acquisitions abroad. On February 12, the bank received official authorization from Chile's superintendency of banks and financial institutions (SIB) for the acquisition of **BankBoston's** operations in Chile, a deal it had sought since last May when it announced its \$2.2 billion acquisition of BankBoston's Brazilian operations [Editor's note: see related Q&A in the May 2006 issue of the *Latin America Banking Advisor*, the publication replaced by this newsletter in September 2006]. In August, Itau agreed to pay \$631 million for BankBoston's operations in Chile and Uruguay. Brazilian regulators have already approved the deal. Itau said it will initiate its business activities in Chile in the sec-



Editor's note: The Financial Services Advisor is introducing one member of its Board of Advisors in each issue. Subscribers can pose queries to the Board for publication in the Featured Q&A by writing Assistant Editor Elisabeth Burgess at eburgess@thediologue.org.

Manuel Orozco is executive director of the remittances and rural development project at the Inter-American Dialogue, where he conducts policy analysis and advocacy on issues relating to global remittance flows.

A frequent advisor to companies, governments, and international organizations across the Americas, as well as in Africa and Asia, Orozco led a program in 2004 and 2005—funded by the Inter-American Development Bank's Multilateral Investment Fund and the United Nations' International Fund for Agricultural Development—seeking to better leverage remittance transfers.

In addition to his work at the Dialogue, Orozco is senior researcher and professor at the Institute for the Study of International Migration at Georgetown University. Until 2005, he was chair of Central America and the Caribbean at the US Foreign Service Institute. He has taught political science at the University of Akron, Ohio and has been a researcher for the Tomas Rivera Policy Institute.

Orozco holds a PhD in political science and a masters degree in public administration and Latin American studies from the University of Texas at Austin, and a BA in international relations from the National University of Costa Rica.

His recent publications include "Global Remittances and the Law—A Review of Regional Trends and Regulatory Issues" in *International Migration Law: Developing Paradigms and Key Challenges*, published by Cambridge University Press in January 2007; "International Flows of Remittances: Cost, competition and financial access in Latin America and the Caribbean—toward an industry scorecard," published by the Inter-American Development Bank in 2006; *Remittances: Global Opportunities for International Person-to-Person Money Transfers*, published by VRL Publishing Ltd. in 2005; and "Markets and Financial Democracy: The Case for Remittance Transfers," which appeared in the *Journal of Payment Systems Law* in March/April 2005.

ond half of February, according to the press release.

Remittances News

Mexico's Farmacias Guadalajara in Western Union Money Transfer Deal

Colorado-based money transfer company **Western Union** and Citibank's **Banamex** unit on February 21 announced that 450 **Farmacias Guadalajara** locations

throughout Mexico have begun offering Western Union consumer money-transfer services. Founded in 1942, the 24-hour Farmacias Guadalajara drug store chain has 500 locations in 113 cities in 18 states in Mexico. Banamex already offers Western Union services at more than 4,500 locations throughout Mexico through its own branches and other partners. Banamex has served as an Agent for Western Union and its Orlandi Valuta in Mexico since 2001. In late 2006, Banamex extended its service offerings to include

Vigo, a Miami-based money transfer company. [Editor's note: see coverage of Western Union's most recent financial performance in the February 6, 2007 edition of the *Financial Services Advisor*.]

Political News

Colombian Foreign Minister Resigns Amid Paramilitary Scandal

Colombian Foreign Minister Maria Consuelo Araujo resigned on February 19, just days after her brother, Senator Alvaro Araujo, was arrested on charges of colluding with outlawed right-wing paramilitary groups. "I am leaving because I am tied to no office," Araujo wrote in her resignation letter to President Alvaro Uribe, according to Colombian state news service SNE. "But on the other hand I see clearly that the judicial process must be free of any interference." Araujo, who took office just six months ago, was the first high-ranking official in the Uribe government to resign since allegations surfaced in November of ties between pro-Uribe lawmakers in Colombia's Congress and illegal paramilitary groups. A week before the foreign minister's resignation, Sen. Araujo and four other pro-Uribe lawmakers were arrested on charges of colluding with paramilitary leaders. Three other pro-Uribe lawmakers were previously jailed on similar charges. Colombia's paramilitary groups are accused of killing thousands in a decades-old war against leftist rebels, protecting drug traffickers, and other crimes. The recent scandal involving pro-



Maria Consuelo Araujo

Photo: SNE

Uribe lawmakers threatens to undermine US support and financing for the Colombian leader's pro-security program, with some members of the Democrat-controlled US Congress saying the US should reconsider the \$700 million in mostly military aid that Colombia gets each year. Uribe, who says he welcomes the investigation to purge his government of paramilitary influence, appointed former

Interior Minister Fernando Araujo, who escaped from rebels on New Year's Eve after six years in captivity, to serve as the new foreign minister. He is not related to his predecessor. [Editor's note: look for a related Q&A in the February 23, 2007 issue of the daily *Latin America Advisor*.]

Correa: Constitutional Assembly Would be Able to Dissolve Congress

If its creation is approved by a popular referendum, an assembly to rewrite Ecuador's Constitution will have the power to dismiss all elected officials, including members of Congress, President Rafael Correa said on February 14, according to the Associated Press. "It is absurd to say that the assembly cannot dissolve established institutions. I will be the first to present my resignation before that assembly, recognizing that they can send home the national Congress, the Supreme Court or president of the republic," Correa was quoted as saying. On February 13, Congress approved Correa's proposal for a referendum, to be held on April 15, but stipulated that the assembly would not have the authority to dissolve Congress. Earlier this month, Correa's government denied any plans to dissolve the legislative body, which the president has called a "sewer of corruption," according to the AP. Correa took office last month vowing to reform Ecuador's political system to curb the influence of traditional parties. Critics say the president is seeking to use the assembly to accumulate greater power in step with his ally, Venezuelan President Hugo Chavez. According to a **Cedatos-Gallup** poll published last month, three-fourths of Ecuadoreans support Correa's proposal to rewrite the Constitution. [Editor's note: see related Q&A in the February 22, 2007 issue of the daily *Latin America Advisor*.]



Rafael Correa

Photo: Ecuadorean government

Calderon Rewards Soldiers For Work in Mexican Drug War with Pay Raises

Mexican President Felipe Calderon on February 19 announced pay raises of

nearly 50 percent for the military to reward soldiers for their participation in the fight against drug trafficking and organized crime. In a speech to commemorate Army Day in Mexico, Calderon said rank-and-file soldiers would see their pay rise from 3,500 pesos (\$US 319) to 5,200 pesos monthly, applied retroactively to January 1, while officers will receive similar pay increases, Calderon said. In addition, the government will implement a program to make housing loans available to members of the army and navy, the president stated. "In the name of the people of Mexico I make a special recognition of [the military's] courageous participation in the fight we are waging against those who threaten the security and peace of citizens, and who are trying to poison the bodies and souls of children and youth," Calderon said. "Our armed forces have been on the front line of the battle, with patriotism." Immediately after taking office in December, Calderon launched a major counterdrug offensive, sending thousands of police and soldiers first into his home state of Michoacan, and then into the border city of Tijuana and to Acapulco, to take on drug gangs, which have been responsible for spiraling violence in recent years. On February 18, the government announced it was sending thousands more police and military to the border states of Nuevo Leon and Tamaulipas. Calderon's use of the military in his counterdrug offensive is the biggest since former President Ernesto Zedillo deployed soldiers in counterdrug operations in the late 1990s. However, the use of the military backfired on Zedillo with the 1997 arrest of the army general Zedillo had put in charge of the operations. [Editor's note: see related Q&A in the January 8, 2007 issue of the daily *Latin America Advisor*.]

Venezuela to Spend \$2.8 Billion on New "Communal Councils"

Venezuela will allocate 6 trillion bolivars (\$US 2.8 billion) to fund newly created "communal councils" as part of President Hugo Chavez's program to bring socialism to the South American nation, Bloomberg News reported on February 15. "We have to subordinate the power of

the state to the power of the people," Chavez was quoted as telling hundreds of council members in Caracas. "We have to do this thinking always as good socialists, not about how to get rich, but how to satisfy community needs." The local councils will use the money, to be funded from state oil revenues and other government sources, to finance housing, water, electricity, and other projects that members determine their community needs, according to Bloomberg News. Each council should also set up its own "productive unit" to produce basic supplies and make their communities more self-sufficient, Chavez said. Each council must spend its full grant each year, with funding to increase to \$4.7 billion next year, he said.

UN Security Council Extends Haiti Mission by Eight Months

The United Nations Security Council on February 15 voted to extend peacekeeping operations in Haiti by another eight months and called for peacekeepers to continue a campaign against armed gangs. In a press release, the Security Council said the unanimously passed resolution extended the mandate of the United Nations Stabilization Mission in Haiti (MINUSTAH) to



David Wimhurst

Photo: UN file photo

October 15. The mission expired on February 15. The resolution, which follows stepped-up action by the nearly 9,000-strong UN force to disarm gangs in the country, particularly in slum areas of Port-au-Prince, calls on MINUSTAH "to accelerate efforts to reorient its disarmament, demobilization and reintegration resources towards a comprehensive community violence reduction program ... in close coordination with the government of Haiti and other relevant actors." MINUSTAH spokesman David Wimhurst told reporters that the operations against armed gangs would continue "until we have really dislodged" the gangs, which he said in Port-au-Prince were holding the rest of the country hostage, and impeding investment and develop-

ment. On February 9, more than 700 UN troops entered the sprawling Port-au-Prince slum of Cite Soleil to try to break up a gang and arrest its leader, who was able to escape. One person was killed and two UN peacekeepers were injured in the operation, which the UN said resulted in the seizure of large amounts of weaponry and ammunition. Despite the call for continued action against gangs, Wimhurst said that UN peacekeeping operations in the impoverished Caribbean nation are just a "band-aid," and that "the cure to what ails Haiti is development."

Economic News

US Lawmakers Propose Relaxation of Rules on Food Sales to Cuba

Four members of the US House of Representatives on February 15 proposed easing rules for selling food to Cuba, saying the time is right for the US to relax its embargo against the island following the decision last year by aging Cuban leader Fidel Castro to temporarily cede power. Under the legislation, sponsored by Reps. Jerry Moran (R-KA), Stephanie Herseth (D-SD), Jo Ann Emerson (R-MO), and Mike Ross (D-Ark), the Cuban government would be allowed to pay US banks directly for food purchases instead of routing the money through foreign banks, and the proposed rules would allow payment before delivery, instead of before ships leave US ports, as the Bush administration currently requires. The bill would also direct the US State Department to issue general licenses to producers' groups to facilitate sales trips to Cuba, allow temporary visas for Cubans to come to the US to buy agricultural goods or inspect them for shipment. Moran said it was "an opportune time to encourage the United States to change its trade policies toward Cuba," citing the decision by Castro in July of last year to transfer power to his younger brother, Raul Castro, in order to undergo intestinal surgery. Officials have been saying that Fidel Castro is recovering. Herseth said the bill would benefit US producers but also help "millions of Cubans [who] are in need of access to a safe and abundant food supply."

POLITICAL & ECONOMIC BRIEFS

DR's Economy Grew 10.7 Percent in 2006

The Dominican Republic's central bank on February 19 said the country's economy grew 10.7 percent in 2006, up from 9.3 percent growth in 2005 and continuing a strong recovery from a recession triggered in part by a 2003 collapse bank, Reuters reported. Growth last year was driven by the telecommunications and construction sectors, which expanded 26.1 percent and 22.9 percent, respectively, the central bank said.

Ecuador Makes \$135 Million Debt Interest Payment on Time

The government of Ecuadorean President Rafael Correa made a \$135 million interest payment due on February 15. Economy ministry officials had earlier said they would not make the payment by yesterday's deadline, instead using a 30-day grace period because of a shortage of cash. Correa, who took office last month, has pledged to restructure the country's \$10 billion debt in order to devote more government resources to social programs, and has said that some of the debt was contracted illegally by past governments.

Nicaragua's Aleman Admits to Spending Government Funds

Former Nicaraguan President Arnoldo Aleman on February 17 admitted that he spent \$1.8 million in government funds while in office, the Associated Press reported. Some of the spending was for jewelry, a honeymoon trip, food, and crafts purchased abroad. Aleman, who prosecutors accuse of stealing \$100 million from government coffers, in 2003 was charged with money laundering and embezzlement during his 1998-2002 presidency.

Featured Q&A*Continued from page 1*

Implementation of economic and financial policies that have created stable environments (inflation, interest, and exchange rates) have facilitated more recipients every day to qualify for a loan from financial sources. The need for the use of credit is there, the ability or potential to qualify not always is. Credit reporting agencies or credit bureaus have contributed to the expansion of credit.

“One of the main challenges of the credit industry has been in how to qualify people in the informal sectors, and those who have never been clients of a financial institution ... The potential these kind of consumers and firms represent for the financial industry is enormous.”

— José Landa

Financial institutions rely on their information to operate and authorize applications. At the same time, they have contributed to a borrower's culture by targeting incentives to those with good payment records. One of the main challenges of the credit industry has been in how to qualify people in the informal sectors, and those who have never been clients of a financial institution. Numerous examples can be found in self-employed activities (taxi drivers), others that are remunerated with a small pay and remaining based in tips or commission (waiters, sales clerks). We also have very low-income people and micro-firms that do not qualify for financial credit, just in the form of deferred payments like electricity or telephone bills, supplier credit, etc. How to incorporate cases like these in reporting agencies is a challenge in itself. However, the potential

these kind of consumers and firms represent for the financial industry is enormous, as it has been demonstrated in countries like India. The reward lies in the challenge.”

A **Guest Comment: Christian Stracke:** "Better credit reporting systems would do a lot to help expand consumers' access to credit in Latin America, but there are still impediments to fully developed reporting systems in a number of countries. The main problem is that many of these systems are effectively starting from scratch, so very few individuals have any credit history to be scored. The prevalence of informal employment, together with the potential for identity fraud, make other credit metrics relatively unreliable. In the absence of credit histories, positive indicators like verifiable income levels, time at one's current employer, and time at one's current address are critical, but economic informality make these indicators difficult to measure. Regulatory safeguards of consumer privacy are also a problem, restricting banks' ability to share debtors' records. Many countries in Latin America have taken important steps to resolve some of these issues, but the basic problems of the informal economy and the lack of credit history will remain a problem for the foreseeable future."

Jan Smith is a member of the Financial Services Advisor board and Managing Partner at InfoAmericas, and **Tricia Juhn** is Director of the Financial Services Practice at InfoAmericas.

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