LATIN AMERICA ADVISOR

A DAILY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

Monday, September 19, 2016

BOARD OF ADVISORS

Diego Arria
Director, Columbus Group

Devry Boughner Vorwerk
Senior Policy Advisor
Akin Gump Strauss Hauer & Feld, LLP

Joyce Chang
Global Head of Research,
JPMorgan Chase & Co.

W. Bowman Cutter
Former Partner,
E.M. Warburg Pincus

Dirk Donath
Senior Partner,
Catterton Aimara

Marlene Fernández
Corporate Vice President for
Government Relations,
Arcos Dorados

Peter Hakim
President Emeritus,
Inter-American Dialogue

Donna Hrinak
President, Boeing Latin America

Jon Huenemann
Vice President, U.S. & Int'l Affairs,
Philip Morris International

James R. Jones
Chairman, ManattJones
Global Strategies

Craig A. Kelly
Director, Americas International
Gov't Relations, Exxon Mobil

John Maisto
Director, U.S. Education
Finance Group

Nicolás Mariscal
Chairman,
Grupo Marhnos

Thomas F. McLarty III
Chairman,
McLarty Associates

Carlos Paz-Soldan
Partner,
DTB Associates, LLP

Beatrice Rangel
Director,
AMLA Consulting LLC

José Antonio Ríos
Chief Executive Officer,
Vadium Technology Inc.

Gustavo Roosen
Chairman of the Board,
Envases Venezolanos

Andrés Rozental
President, Rozental &
Asociados and Senior
Policy Advisor, Chatham House

Shelly Shetty
Head, Latin America
Sovereign Ratings, Fitch Inc.

Roberto Sifon-Arevalo
Managing Director, Americas
Sovereign & Public Finance Ratings,
Standard & Poor's

THEDIALOGUE

FEATURED Q&A

Will Slower Growth Start Taking Its Toll on Mexico's Banks?

Philip Finch, a banking sector analyst at UBS, expects earnings-per-share for Mexican banks to jump 14 percent this year—well above the 1 percent growth projected for emerging-market peers, Bloomberg News reported last week. // File Photo: Bloomberg.

Q Mexico's economy shrank in this year's second quarter, the first quarterly contraction since 2013, the national statistics agency announced Aug. 22. At the same time, the government reduced its growth forecast for the year. How are Mexico's broader economic conditions affecting lending and the country's banks? How strong are Mexican banks' balance sheets, and do they have strong enough provisions to counter loan defaults? Have President Enrique Peña Nieto's policies been good or bad for the banking sector?

A Sergio Luna Martínez, director of research at Banamex: "GDP growth projections by the government and Banxico were downgraded as part of a quarterly review process and essentially caught up to standing projections by private analysts; we have, for example, been calling for a 2.1 percent GDP growth rate since April, and this is now the middle of Banxico's forecast range. Although overall GDP growth in this year's second quarter was weak at a seasonally adjusted annual rate of -0.7 percent quarter-over quarter, the segment relevant to the banking sector is the internal market, and this has been performing comparatively better: if we use the tertiary sector as a proxy for the internal market, the seasonally adjusted annual growth rate in this year's second quarter stood at 0.6 percent quarter-over-quarter, virtually the opposite of the headline figure. This is more consistent with the most recent numbers for bank lending; in July bank lending to the private sector rose 13.9 percent year-over-year in real terms, and nonperforming loans remained stable at 2.9 percent of the total. Overall,

Continued on page 2

TODAY'S NEWS

POLITICAL

Venezuela Finds Support at NAM Summit as Critics Lash Out

The 17th Summit of the Non-Aligned Movement closed Sunday in Venezuela with fiery rhetoric to rally against imperialism at the hands of the United States government, as well as criticism that fewer heads of state attended the meeting than ever.

Page 2

ECONOMIC

Brazil Currency Rally May Have Stalled: Analysts

Brazil's impressive currency rally this year, which has seen the real rise 23 percent against the U.S. dollar, may be leveling out.

Page 3

POLITICAL

Jamaica's PNP Keeps Simpson Miller as Head

Former Jamaican Prime Minister Portia Simpson Miller has defeated challenger Karl Blythe to continue as president of the People's National Party.

Page 2

Simpson Miller // Photo: Via Twitter @PSimpsonMiller.

COPYRIGHT © 2016, INTER-AMERICAN DIALOGUE

POLITICAL NEWS

Under Fire, Maduro Seeks Support at NAM Summit

The 17th Summit of the Non-Aligned Movement closed Sunday in Venezuela with fiery rhetoric to rally against imperialism at the hands of the United States government, as well as observations that fewer heads of state attended the meeting than ever, which critics say cost millions of dollars for Venezuela to host while its citizens lack basic food and medical supplies, the Associated Press reported. While Venezuelan President Nicolas Maduro said Sunday that the summit "has been a total success, a victory of Bolivarian diplomacy," TeleSUR reported, other media reports noted that only 12 heads of state had arrived for the two days of meetings taking place on the Caribbean island of Margarita, including the leaders of Cuba, Iran and Zimbabwe. More than 30 world leaders attended the last summit of the Cold War-era group, founded as an alternative for states to align with either the Soviet Union or United States, which was held in Iran in 2012. India's Prime Minister, Narendra Modi, became the first Indian Prime Minister to not attend the NAM summit since 1979. Venezuelan opposition leader Henrique Capriles lashed out at Maduro's effort to portray himself as having international support for his administration's policies. "Millions of dollars of Venezuelans' money spent for the government's ego," Capriles said, UPI reported. "Many of the countries didn't come to the show," he added. As the meeting got underway, Cuban President Raul Castro warned that Venezuela was being targeted by a U.S. economic war aimed at toppling Maduro."Venezuela is facing an onslaught ... that is against all of Latin America and the Caribbean, that is trying to re-impose and recolonize the politics, economy, culture and life of our countries," Castro said. Meanwhile, Venezuela's Oil Minister, Eulogio Del Pino, said Saturday that efforts to build consensus around a higher global price for oil, practically Venezuela's only source of revenue, have begun taking hold, with Maduro telling reporters "we're close to a deal" after meeting with Iran's leader, Hassan Rouhani, on Sunday. The Organization of the Petroleum Exporting Countries, or OPEC, will likely revive talks on freezing oil production levels when it

FEATURED Q&A / Continued from page 1

the financial reform has been positive for the banking sector as it has sought to increase bank lending as a proportion of GDP through the right set of incentives: more intense competition as well as a legal framework that facilitates the management of credit risk are two good examples."

Busy Juárez, associate analyst in the Financial Institutions Group at Moody's Investors Service: "Mexico's banking system remains strong. That said, the combination of low oil prices and other external headwinds has undermined expectations for improved economic performance and shifted the balance of risks and opportunities for banks to the downside. We expect Mexico's economy to grow by 2.5 percent through the end of this year and in 2017, relatively unchanged from 2015. However, while economic growth remains tepid, loan growth is still climbing rapidly at around 12 percent, with new lending that aims primarily at risky consumers as well as small and midsized enterprise segments. Consequently, asset quality is likely to deteriorate, but loan delinquency metrics will continue to be largely controlled by banks' aggressive write-off practices. Therefore, we expect the system's non-performing loan ratio will rise only slightly by the end of 2017. Banks' oil exposures remain a key risk. These include exposure to state oil company Pemex (Baa3 negative), one of the largest corporate borrowers in the banking system, which continues to grapple with liquidity strains and high financial leverage. Banks' exposures to the sector account for about 6 percent of all outstanding loans in the system, and for

Continued on page 4

NEWS BRIEFS

Kerry to Attend Colombia Peace Signing, Appeals for More International Aid

U.S. Secretary of State John Kerry said Sunday he will attend the signing of Colombia's negotiated peace deal with the Revolutionary Armed Forces of Colombia, or FARC, guerrillas on Sept. 26, the Associated Press reported. Kerry also said the United Sates will provide an additional $36 million in aid for landmine removal and asked other countries "to come forward as well." A national referendum to accept or reject the peace accord is scheduled for October 2.

Jamaica's Simpson Miller Retains Leadership of Opposition Party

Former Jamaican Prime Minister Portia Simpson Miller, who lost control of the government earlier this year in a surprise election result, on Saturday defeated challenger Karl Blythe to continue as president of the 78-year-old People's National Party, the Jamaica Gleaner reported. Simpson Miller emerged with 2,471 votes in her party's congress, while Blythe managed only 198 votes. On Sunday, Simpson Miller called for new campaign finance legislation before holding local elections scheduled for December. Parties in Jamaica have come under criticism in recent races for how campaign funds are allocated and spent.

Anglo American Strikes Deal With Chilean Miners

Anglo American announced last Friday it had reached a deal with miners at the Los Bronces copper mine in Chile, ending a week-long strike, Reuters reported. Mining activities halted on Sept. 9 at the company's premier mine after labor negotiations broke down between the two sides. The company said Friday it had already begun the process of restarting work at the Los Bronces, to which 1,700 striking workers agreed to return.

COPYRIGHT © 2016, INTER-AMERICAN DIALOGUE

meets non-OPEC nations in Algeria next week, sources told Reuters. Oil prices rose nearly 2 percent in early trading today in reaction to Maduro's comments about a possible output agreement, Ric Spooner, CMC Markets' chief market analyst, told Reuters.

ECONOMIC NEWS

Brazil Currency Rally May Have Stalled: Analysts

Brazil's impressive currency rally this year, which has seen the real rise 23 percent against the U.S. dollar, may be leveling out, Bloomberg News reported Sunday. Brazil's currency has been falling in recent weeks and is now barely hanging on as 2016's top-performing global currency, according to the report. Investors had been betting that the ouster of President Dilma Rousseff would bring new economic policies that would end one of the deepest recessions in the nation's history. But some investors now fear that a fractured Congress and ongoing corruption scandals are restricting President Michel Temer from pushing through reforms and building confidence, according to the report. The real has fallen from more than 4 reais to the dollar in January to less than 3.2 earlier this month. "On the data side nothing has changed, and the new government will just inherit the challenges of the previous one," Arnaud Masset, an analyst at Swissquote Bank, told Bloomberg. "We've had a mammoth rally this year, with a lot of good news priced in already. Now we turn our attention back to fundamentals and policy," said Mike Moran, head of economic research for the Americas at Standard Chartered. Last week, the Temer Administration announced a new plan to sell 14 airports and two port terminals, as well as offer contracts to private firms for projects ranging from building new roads to running mines, BBC News reported. Also, the government is considering a "re-auction" process for some airport concessions already functioning in an effort to stimulate new investments, according to Brazil Focus.

LEGAL BRIEFS

ICSID Sides With Chile in Longstanding Case

The International Center for Settlement of Investment Disputes, or ICSID, last week declared that Chile does not have to pay $10 million to Spanish publisher Víctor Pey Casado, reversing an earlier decision on the matter, Agence France-Presse reported. Pey Casado was the publisher for Chile's Clarín newspaper until 1973, when it was shut down by dictator Augusto Pinochet. Pey Casado brought the case to the ICSID in 1997 and won a preliminary decision in 2008, which has now been reversed. Arbitrators said they hope that the case, which is the longest-running at ICSID, has reached its "final end," according to Latin Lawyer.

Holland & Knight, Skadden Expand in Latin America

International law firm Holland & Knight announced on Sept. 7 it has added Carlos Véjar to its Mexico City office. Before joining the firm, Véjar served as general counsel for international trade for Mexico's Ministry of Economy. In other news, Skadden, Arps, Slate, Meagher & Flom announced it has hired Jennifer Parmesly in its New York office. Parmesly will work with the firm's International Litigation and Arbitration Group and will focus on Latin America, Latinvex reported last week.

Tauil & Chequer Opens New Brasília Office

Brazilian law firm Tauil & Chequer Advogados announced the opening of a new office in Brasília on Sept. 14. The new office will be led by former Brazilian Attorney General Luís Inácio Adams. The firm said Adams will work primarily on cases at Brazil's Superior Court of Justice and Supreme Court.

Ecuador Case With Chevron Goes to Canadian Courts

A court in Ontario, Canada, last week began proceedings in a case between lawyers representing Ecuador in their suit against Houston-based energy company Chevron, CBC News reported. The Ecuadoreans are trying to force Chevron to pay $9.5 billion awarded to local villagers in a local court over environmental damages that activists claim have led to more frequent instances cancer and miscarriages. Courts in the United States have repeatedly found that the monetary award was obtained through bribery and corruption. Because Chevron has virtually no assets in Ecuador, the plaintiffs are trying to enforce the judgment elsewhere in the world.

Iberian Firm Cuatrecasas Focuses on Colombia

Madrid and Lisbon-based law firm Cuatrecasas last week announced it had struck an alliance with Colombia's Posse Herrera Ruiz to offer legal services in both the Colombian and Iberian markets. The two law firms have created a company, Posse Herrera Ruiz + Cuatrecasas, with headquarters in Bogotá, through which they will coordinate services for mutual clients. Both firms will maintain their independence and alliance policies and have ruled out the possibility of merging their firms and brands.

COPYRIGHT © 2016, INTER-AMERICAN DIALOGUE

FEATURED Q&A / Continued from page 2

a very high 30-40 percent of core capital at many banks. Notwithstanding rising credit costs, profitability will remain robust thanks to banks' stable, low-cost funding, which helps mitigate risks stemming from the less favorable operating environment. Capitalization will remain strong as well, despite an anticipated decline over the next two years, as retained profits will be insufficient to fully replenish capital consumed by rapid loan growth."

Tapen Sinha, professor of risk management at the Instituto Tecnológico Autónomo de México and professor at the University of Nottingham Business School: "Large financial groups dominate Mexico's financial sector: They are BBVA Bancomer, Santander, Banamex and Banorte. A recent report from the CNBV shows that these banks' assets grew more than 10 percent from July 2015 to June 2016 with an annualized increase of 3 percent in the last quarter. The return on assets in June 2016 was 1.37 percent. This is lower than 1.55 percent in June 2015, but not by much. Similarly, the return on equity was 12.53 percent in June 2016. If we ignore a spike in 2013, this has been the pattern of the return on equity since 2009. The use of credit cards doubled between 2010 and 2015. Yet, the default rate on those loans has barely budged—it went from 2.5 percent to 3.1 percent. Compared with other Latin American countries, Mexico lags in banking services. At this point, there is no indication that the short blip in fall of GDP in the last quarter is any indication of a further decline. The future growth rate has been pared down, but no one is predicting a further contraction of the economy. During Peña Nieto's government, there has been large growth of government debt, but it has mainly been a result of state-level mismanagement and subsequent rescue by the federal government that added to the debt—not so much by fiscal irresponsibility by the federal government."

Jonathan Heath, independent Mexico-based economist: "Although GDP fell in the second quarter, Mexico's economy is still showing an upward trend. While April registered declines in consumption, investment, exports and government spending, data for May and June shows rebounds in most indicators. This means that April was an outlier, while the economy is still growing, albeit at a slow pace. For example, household consumption fell 2.1 percent in April, but then grew 1.6 and 0.9 percent, respectively, in May and June. While consumption will be down for the quarter, the June level is actually a new high, and the trend is growing. GDP growth for the year may not reach 2 percent, much less than what was forecast not too long ago. Nevertheless, car sales have been growing at a rate of 16 percent or more for more than a year, while retail sales continue to expand. Household consumption is currently Mexico's main engine of growth, fueled in part by commercial bank lending, up by more than 10 percent over last year. Most banks continue to show relatively good results, loan defaults are not really growing and balance sheets show more than enough provisions. Mexico at this time has many worries, but the banking sector is not one of them."

> **"Mexico at this time has many worries, but the banking sector is not one of them."**
>
> **— Jonathan Heath**

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

LATIN AMERICA ADVISOR
is published every business day by the Inter-American Dialogue, Copyright © 2016

Erik Brand
Publisher
ebrand@thedialogue.org

Gene Kuleta
Editor
gkuleta@thedialogue.org

Nicole Wasson
Reporter, Assistant Editor
nwasson@thedialogue.org

Michael Spak
Editorial Intern

THEDIALOGUE

Michael Shifter, President
Genaro Arriagada, Nonresident Senior Fellow
Sergio Bitar, Nonresident Senior Fellow
Joan Caivano, Director, Special Projects
Kevin Casas-Zamora, Director, Peter D. Bell Rule of Law Program
Ramón Espinasa, Nonresident Senior Fellow
Ariel Fiszbein, Director, Education Program
Alejandro Ganimian, Nonresident Fellow
Peter Hakim, President Emeritus
Claudio Loser, Senior Fellow
Nora Lustig, Nonresident Senior Fellow
Margaret Myers, Director, China and Latin America Program
Manuel Orozco, Director, Migration, Remittances & Development
Jeffrey Puryear, Senior Fellow
Tamar Solnik, Director, Finance & Administration
Lisa Viscidi, Director, Energy Program

Latin America Advisor is published every business day, except for major U.S. holidays, by the Inter-American Dialogue at 1211 Connecticut Avenue NW, Suite 510 Washington, DC 20036

www.thedialogue.org

ISSN 2163-7962

Subscription inquiries are welcomed at freetrial@thedialogue.org

The opinions expressed by the members of the Board of Advisors and by guest commentators do not necessarily represent those of the publisher. The analysis is the sole view of each commentator and does not necessarily represent the views of their respective employers or firms. The information in this report has been obtained from reliable sources, but neither its accuracy and completeness, nor the opinions based thereon, are guaranteed. If you have any questions relating to the contents of this publication, contact the editorial offices of the Inter-American Dialogue. Contents of this report may not be reproduced, stored in a retrieval system, or transmitted without prior written permission from the publisher.