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THEDIALOGUE

FEATURED Q&A

Would More Developed Capital Markets Aid Brazil?

Government influence in credit markets has led to the crowding out of corporate financing from debt and stock markets, according to Brazil's Securities and Exchange Commission, led by Executive Chairman Leonardo P. Gomes Pereira. // File Photo: Brazilian Chamber of Deputies.

Q Brazil's securities industry regulator said in June that capital markets activity in Brazil will fail to grow significantly as long as state lenders keep the country's companies hooked on cheap credit, Reuters reported. CVM, as the regulator is known, says that years of what it sees as active state meddling in credit markets have led to the crowding-out of corporate financing from debt and stock markets. Have state lenders been a hindrance to growing Brazil's capital markets? How can Brazil encourage more robust flows of international and domestic capital? What benefits would more sophisticated capital markets bring to Brazil's economy, and what are the downsides of having less state involvement in the financial markets?

A Roberto Teixeira da Costa, board member of SulAmérica in São Paulo: "State banks' credit, particularly from BNDES, has always been regarded as one of the factors that affected users of capital markets as an instrument for corporations to raise medium and long-term capital. But several other factors have hindered market development. Certainly, the most relevant has been Brazilian financial markets' high interest rates, which monetary authorities fix every month. The so-called CDI, an interbank reference rate, has often rewarded investors with a very high level of interest rates (to fight inflation). That rate, well above inflation, was a strong disincentive for other securities instruments to compete with government paper. Between 2006 and 2016, the return on government securities was three times higher than an investment in the Bovespa index. Thus, it is an unfair competition

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TODAY'S NEWS

BUSINESS

CEO of Argentina's YPF Resigns

Ricardo Darré, who joined the company just over a year ago, cited personal reasons for stepping down. Local media have reported for months that Argentine officials have been unsatisfied with the company's performance.

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ECONOMIC

Mexico Records $1.52 Billion Trade Deficit in July

The trade deficit in July contrasted with a trade surplus that the country recorded in June.

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POLITICAL

U.S. Urges Guatemala's Morales to Keep Prosecutor

The U.S. State Department urged Guatemalan President Jimmy Morales to back down on expelling the U.N.-backed anticorruption prosecutor who is leading a probe into Morales' alleged violation of campaign finance laws.

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Morales // File Photo: Guatemalan Government.

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POLITICAL NEWS

U.S. Urges President of Guatemala to Back Down on Expulsion

The U.S. State Department on Monday urged Guatemalan President Jimmy Morales to allow the United Nations-backed prosecutor leading a probe of corruption in Guatemala, and specifically of Morales and other top politicians for possible breaches of campaign finance laws, to continue operating in the country, The Wall Street Journal reported. Morales on Sunday had named Iván Velásquez, the Colombian prosecutor heading the International Commission against Impunity in Guatemala, or CICIG, persona non grata, and asked him to leave the country. Hours after the declaration, the Guatemalan constitutional court granted a temporary injunction, preventing Morales from being able to expel Velásquez from the country. The court is expected to determine whether the stay will be permanent in the coming days. U.S. Ambassador to the United Nations Nikki Haley said that the United States expects Guatemala to continue to allow CICIG to "do its critical work without interference." She praised Velásquez for his work as a crucial "voice calling out corruption and upholding the rule of law." U.S. Rep. Ed Royce (R-Calif.), the chair of the House Foreign Affairs Committee, also called on Morales to "change course" and allow Velásquez to stay in the country. He added that the U.S. Congress "will continue to stand with the Guatemalan people, and especially those in poverty, who are hurt most by corruption," Royce said in a statement.

Colombia Claims Venezuelan Military Incursion

Colombia's government has sent Venezuela a letter of protest, saying Venezuelan security forces crossed the border into Colombia's La Guajira province over the weekend, Reuters reported Monday, citing two unnamed government sources. The sources said Colombia's foreign ministry delivered the protest letter to the Venezuelan embassy in Bogotá. Venezuelan President Nicolás Maduro denied on Sunday

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for private securities, and particularly for stocks. Right now, with inflation falling to an annual rate of 4 percent, interest rates will converge to a level below 10 percent annually. It will make competition fairer, but not yet as in other developed markets. Other factors have also influenced capital market development. Among them, inflation has created a preference for short-term instruments, investors historically have channeled their resources to fixed-income securities and savings accounts, and institutional investments do not play the same role as in other countries. Finally, leading corporations such as OGX, Petrobras and JBS, targeted by the 'Lava Jato' investigation, have created a negative image of such companies for the individual investor. Right now, the state is no longer in the process of supplying funds to corporations with negative real rates, due to the fact that interest rates are coming down, and basic reforms are being discussed in Congress. CVM is also aggressively proceeding with administrative inquiries. These developments are relevant for market growth, a fundamental instrument of our economy."

Gustavo Junqueira de Godoy Pereira and Thiago Vallandro Flores, attorneys at Dias Carneiro Advogados in São Paulo: "The fact that BNDES and other Brazilian policy banks (such as Banco do Nordeste do Brasil, Caixa Econômica Federal and Banco do Brasil) have been providing subsidized credit may indeed be viewed as impairing the development of the Brazilian capital market, but also as being a consequence of its current stage of development. On the

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NEWS BRIEFS

Chile's Bachelet Sends Lawmakers Bill to Legalize Same-Sex Marriage

Chilean President Michelle Bachelet on Monday introduced legislation that would legalize gay marriage, the latest move toward reform in what has been known as one of Latin America's most socially conservative countries, the Associated Press reported Monday. Bachelet signed the proposal, which will now be sent to legislators, on Monday at the presidential palace. She said the bill would expand the definition of marriage as well as expand the rights for gay couples, allowing them to adopt children. Chile approved civil unions for same-sex couples in 2015 and decriminalized gay sex in 1999. The bill comes a week after the country's Constitutional Court upheld a measure that allows abortions in some cases.

Mexico Registers Trade Deficit of $1.52 Bn in July

Mexico's trade deficit reached $1.52 billion in July, contrasting from a trade surplus in June but lower than the $1.83 billion deficit during the same period a year before, as a rise in exports helped counterbalance an increase in imports, Mexico's National Statistics Institute said Monday. Exports increased by 8 percent in July year-over-year to $32.16 billion, due to increased shipments of crude oil as well as an increase in exports of manufactured products, agricultural goods and materials. Imports rose by 6.6 percent to $33.69 billion.

Former VP Vargas Announces Bid for Colombian Presidency

Former Colombian Vice President Germán Vargas announced today that he will run for the country's presidency in next year's election, according to Colombia Reports. Vargas said he will run as an independent, rather than with the backing of his Radical Change party.

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that such an incursion took place. La Guajira's governor took to Twitter over the weekend to say that security forces crossed the border into Colombia on Saturday night and stole money and cell phones from area residents. Tensions between the Colombian and Venezuelan governments have flared in recent weeks as the government of Colombian President Juan Manuel Santos joined others in the region in criticizing Maduro's government over its creation of a "constituent assembly," which earlier this month declared itself superior to all other government institutions and gave itself the power to make laws. [Editor's note: See **Q&A** in the Aug. 18 issue of the Advisor on how the international community should respond to Venezuela's crises.]

JOB POSTINGS

EDITOR'S NOTE: We are pleased to share Latin America-related job postings that readers of the Advisor and others have posted recently.

Winston & Strawn: Senior Specialist, Latin America, Marketing and Business Development, New York

Wyndham Hotel Group: President and Managing Director, Latin America and Caribbean, Miami

Coca-Cola: Senior Manager, Latin Affairs, Atlanta

CTDI: General Manager, Latin America, West Chester, Pa.

Pfizer: Director, Latin America, International, Various locations

Netflix: Director of Publicity, Latin America, Los Angeles

IHS Markit: Senior Economist, Latin America, Philadelphia

ECONOMIC NEWS

Brazil's Temer Seeks Chinese Investors in Privatization Drive

Brazilian President Michel Temer left today for China where he is to meet with investors as he seeks to privatize dozens of state firms in an effort to boost the South American country's economy, Agence France-Presse reported. "We hope China may be interested in taking a stake in these concessions and bring capital to Brazil," Temer said in an interview on Chinese state television. "It will be very useful to us." Temer's government is seeking to privatize 58 state firms in all, including São Paulo's Congonhas aircraft terminal, state-run electric utility Eletrobras and the country's mint. Temer, who is accompanied on the trip by cabinet members and business leaders, is scheduled to meet with Chinese President Xi Jinping on Friday. During his visit to China, the Brazilian leader is also expected to participate in a summit of BRICS nations on Sept. 3. Brazil and China are expected to sign bilateral agreements in areas including health, infrastructure, technology and culture during Temer's trip, Alexandre Parola, a spokesman for Brazil's presidency, told AFP. "Brazil is a safe destination for Chinese investment and a big provider of food and supplies to China, our main trade partner," said Parola. Last year, trade between the two countries amounted to more than $58 billion, according to Brazil's foreign trade ministry. Brazil's financial markets have rallied on the privatization plans, with the real gaining against the dollar and the stock market rising.

BUSINESS NEWS

CEO of Argentina's YPF Resigns

The CEO of Argentine state-owned energy company YPF, Ricardo Darré, resigned from his post, citing personal reasons, the company said in a statement Monday, The Wall Street Journal reported. The president of YPF, Miguel Gutiérrez, will remain in his position, as will the other top executives at the company. Darré joined YPF as CEO just over a year ago. The company said it had created a six-person executive committee, which aims to make strategic decisions and focus the company's efforts on operations management and business opportunities. "With this reorganization, the management team's mission will be to transform YPF into an integrated energy company that offers innovative and sustainable solutions for the country's energy development," YPF said. Members of the committee include Daniel González, who has been in charge of the company's finances, and Pablo Bizzotto, who is known for his work building the Vaca Muerta shale oil and gas field. Local media in Argentina had been reporting for months that government officials had not been satisfied with YPF's performance since President Mauricio Macri took office in December 2015. Since early 2016, the company had taken on a lower profile than under its previous president, Miguel Galuccio, who had aggressively sought top investors and arranged for joint ventures with major oil companies such as Chevron.

Darré // File Photo: Telam.

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one hand, less expensive loans encourage companies to reach out to Brazilian policy banks when funding is needed. On the other hand, the requirements and regulations applicable to Brazilian capital markets may be a deterrent for companies, particularly less sophisticated companies, which may find requirements and regulations complex and burdensome, including from a cost standpoint. Whether availability of cheap financing from BNDES, in particular, is a cause or a consequence (or even both) of the current stage of Brazilian capital markets can be debated. Separately, as the basic Brazilian interest rate remains high, investors may not see the capital markets as the most interesting type of investment. That said, Brazil could de-regularize and simplify the regulations in order to make it a more appealing market to companies and, from a macroeconomic perspective, lower the basic interest rate. Having more-developed capital markets would bring more transparency to companies' businesses and enhance scrutiny by third parties, which would require (and lead to) better management and ultimately an increase in the companies' competitiveness. As a downside, some could claim that the government would have less power to control the economy and prices (which is not necessarily beneficial). Finally, it is important to note that capital markets transactions might commence to play a more important role, taking into consideration the current economic/financial crisis that Brazil is facing and recent changes to BNDES' upper management, which could lead to changes in its lending policies."

Alexandre Albuquerque, vice president and senior analyst at Moody's América Latina in São Paulo: "The rapid expansion of subsidized loans by government-owned banks, especially by development bank BNDES, has crowded out private lenders and created significant distortions in Brazil's credit and capital markets. After repaying 123 billion reais of the loans it received from the national treasury between 2008 and 2014, BNDES still owes roughly 440 billion reais to the government. Those resources allowed BNDES to flood the market with below-market financing to large and small companies, particularly in the infrastructure and heavy-industry sectors. The ample volume of subsidized loans supplied by BNDES discouraged companies from seeking financing from debt and stock markets. Even companies that had access to private market financing would still turn to BNDES because of its favorable loan terms. We expect slower growth at BNDES will ease the crowding-out that happened in recent years, diminishing distortions in the corporate finance market and in monetary conditions. This will allow other banks to step in and capture greater market share. With BNDES playing a less active role, private banks will be able to boost their fee income by helping companies sell debt, and eventually take advantage of the country's more developed capital markets to raise funding and increase their participation in financing projects and investments. The government has also taken steps to reduce subsidized lending by creating a new long-term rate, the TLP. Once the new rate becomes effective in January of next year, BNDES will apply the TLP to originated subsidized loans for eligible projects, which, according to the bank's current lending policies, include funding infrastructure projects, innovation and investments in health care and education. Initially, the TLP will equal the TJLP, a rate the central bank sets every three months, which is currently 7 percent. However, in the next five years, the TLP will converge gradually toward the rate of the inflation-linked treasury note NTN-B, which is ultimately determined by the market. Once the TLP is fully matched to the market rate, commercial banks will be in a better position to compete with BNDES in the supply of long-term financing."

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

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