LATIN AMERICA ADVISOR

FINANCIAL SERVICES ADVISOR

A PUBLICATION OF THE DIALOGUE

www.thedialogue.org

November 15-28, 2018

FEATURED Q&A

What Will AMLO's Government Mean for Mexican Banks?

Mexican President-elect Andrés Manuel López Obrador said recently that he would not back a proposed measure to limit bank fees and commissions. // File Photo: López Obrador.

Q **Mexican President-elect Andrés Manuel López Obrador on Nov. 9 said he would not support a bill proposed by his party in Congress to limit commissions and fees banks can charge customers. News of the legislation spooked investors, hitting banking sector stocks particularly hard amid new concerns that the left-leaning politician would implement anti-business policies. Will López Obrador stick to his word not to change policies that would limit bank fees and commissions for the first three years of his administration? What lies in store for banks and the financial services sector in the second half of his term? Why are banking fees more controversial and politicized in Mexico as compared to other countries in the region?**

A **Vicente Gómez, associate analyst at Moody's Investors Service:** "A decision by President-elect Andrés Manuel López Obrador to abide by his commitment to maintain the current regulatory framework for the financial system for at least three years would be positive for Mexico. The proposal by the Senate leader of the Morena party asserts that bank fees are excessively high in Mexico. Limits to fees would be credit-negative for Mexican banks; fees represent about 17 percent of pre-provision, pre-tax earnings (core earnings), a level that is in line with that of most other major systems in the region. The proposal seeks to increase intermediation by making banking services less expensive and therefore more accessible to consumers. Nevertheless, banks' profitability has been high, mainly due to high interest rates that benefit margins and adequate asset quality. Bank intermediation in Mexico is indeed low as bank loans equal 21 percent of GDP, less

Continued on page 3

TOP NEWS

BANKING

Société Générale Fined $1.3 Billion in Sanctions Case

The French bank has agreed to pay the fine to settle allegations that it had processed and concealed billions of dollars in transactions related to Cuba and other countries under U.S. sanctions.

Page 2

INSURANCE

Pan-American Life Names New Vice President

Pan-American Life Insurance Group, which operates in several Latin American and Caribbean countries, named Mark Northrup as its new vice president for application development and infrastructure.

Page 2

BANKING

Scotiabank to Exit Nine Caribbean Markets

Bank of Nova Scotia, led by CEO Brian Porter, announced that it will exit nine Caribbean nations. The bank has operated in the Caribbean since 1889.

Page 2

Porter // File Photo: Bank of Nova Scotia.

BANKING NEWS

Canada's Scotiabank Plans to Exit Nine Caribbean Countries

Bank of Nova Scotia on Nov. 27 released its fourth-quarter earnings and announced it planned to sell its banking units in nine Caribbean countries as part of a shake-up. Scotiabank, which has operated in the Caribbean since 1889, said it would sell its subsidiaries in Anguilla, Antigua, Dominica, Grenada, Guyana, St. Kitts & Nevis, St. Lucia, St. Maarten and St. Vincent & the Grenadines to Republic Financial Holdings, a bank based in Trinidad & Tobago, for $123 million, Republic said in a statement, Loop News reported. Scotiabank said the transactions are not material to the bank, but once the deal closes, it would boost its score tier 1 capital ratio by 10 basis points, Reuters reported. The agreements are subject to regulatory approval. Additionally, the Canadian bank said it was planning the sale of its insurance operations in Jamaica and Trinidad & Tobago, adding it would partner with Barbados' Sagicor Financial Corporation to sell insurance products in those countries. Scotiabank reported adjusted earnings per share of 1.77 Canadian dollars, or $1.33, in the fourth quarter, slightly below analysts' forecast of 1.79 Canadian dollars per share, Reuters reported, citing IBES data from Refinitiv. Excluding one-time costs, Scotiabank's net income rose 13 percent year-on-year to 2.35 billion Canadian dollars ($1.77 billion). The bank's international earnings saw a quarterly net income increase of approximately 21 percent to $804 million, driven by the bank's businesses in the Pacific Alliance countries (Mexico, Peru, Chile and Colombia). For its full financial year, Scotiabank registered earnings of 8.72 billion Canadian dollars, up from a profit of 8.24 billion Canadian dollars last year.

Scotiabank is selling the Caribbean units to Republic Financial Holdings.

French Bank Fined $1.3 Billion for Cuba Sanction Violations

French bank Société Générale has agreed to pay $1.34 billion in penalties to settle allegations by U.S. and New York state authorities that the bank had processed and concealed billions of dollars in transactions related to Cuba and other countries under U.S. sanctions, The Wall Street Journal reported Nov. 19. The majority of the transactions and much of the total value involved a dollar credit facility designed to finance oil transactions between a Dutch commodities trading firm and a Cuban company with a state monopoly on the production and refining of Cuban crude, federal prosecutors said. The department that managed the scheme "engaged in a deliberate practice of concealing the Cuban nexus of U.S. dollar payments," prosecutors said. The total penalty amount is the second-largest imposed on a financial institution for violations of U.S. sanctions, according to the report. As part of the deal, prosecutors deferred criminal charges, including conspiracy to violate the Trading with the Enemy Act and the Cuban Asset Control Regulations, the Associated Press reported. The charges would be dropped entirely after three years. The bank said it is fully cooperating with U.S. authorities and has taken steps to strengthen compliance.

Santander Economist Chosen to Lead Brazil Central Bank

Incoming Economy Minister Paulo Guedes has chosen Banco Santander economist Roberto Campos Neto to take over Brazil's central bank under President-elect Jair Bolsonaro, Bloomberg News reported Nov. 15. Campos

NEWS BRIEFS

First Data Launches Smart Payment Devices in Argentina

U.S.-based First Data on Nov. 20 announced that it is launching its Clover Mini and Clover Flex payment devices in Argentina. The portal will allow merchants to monitor the status of transactions, see receipts in an online archive and also make configuration changes remotely.

Pan-American Life Names New Vice President

Pan-American Life Insurance Group, which has operations in several Latin American and Caribbean countries, has named Mark Northrup as its new vice president for application development and infrastructure, the company announced Nov. 26. In the newly created position, Northrup will be responsible for the New Orleans-based insurer's applications development, infrastructure support and operations. Northrup was previously chief information officer at Cleco LLC. Pan-American Life has branches and affiliates in locations including Mexico, Colombia, Guatemala, Costa Rica, Panama and 12 markets in the Caribbean.

Armed Assailants Attack Banks, Police Offices in Brazil's Maranhão State

A group of 50 armed individuals on the night of Nov. 25 attacked the headquarters of the police force and the military police, as well as two banks in Bacabal, in Maranhão State, Globo reported. The gang prompted a shootout against police and military that left three of the attackers dead, Flávio Dino, the state's governor, said in a tweet. G1 Globo reported that a Banco do Brasil branch was "completely destroyed" and added that the bank has not disclosed how much money was stolen. The gunmen also took several people hostage, gradually releasing them that same night. Three people have been arrested.

Neto, 49, will replace Ilan Goldfajn, a market favorite who has lowered interest to record lows since taking the job in 2016. The appointment needs to be approved by Congress. Current

Campos Neto // File Photo: Brazilian President-elect's Transition Office.

Treasury Secretary Mansueto Almeida will be invited to stay on in Bolsonaro's government, Guedes added in a statement, Reuters reported. Market analysts said Campos Neto is an orthodox, pro-market economist who will likely maintain independent monetary policy. [Editor's note: See **Q&A** about Bolsonaro's cabinet selections in the Nov. 27 issue of the daily Latin America Advisor.]

Chilean Regulator Approves BCI's Buy of Walmart Unit

Chile's oversight agency for banking and financial institutions, known as SBIF, has authorized the sale of Walmart Chile's financial business to Banco de Crédito e Inversiones, or BCI, the Walmart subsidiary said Nov. 21, Cooperativa reported. The Santiago-based bank will now operate the retail store's financial unit, known as "Tarjeta Presto," which includes the administration of Lider MasterCard credit cards and personal insurance services, local newspaper Diario Financiero reported. As of October, Walmart Chile had issued roughly 1.4 million credit cards with a credit portfolio equivalent to approximately $587 billion Chilean pesos, roughly $869 million. The deal is part of a long-term cooperation agreement between BCI and Walmart. "This transaction comes within the framework of the bank's strategy of continuous search for growth opportunities at the local and international levels and of our goal to become a reference actor in the credit card industry in Chile," said Eugenio Von Chrismar, BCI's chief executive, Diario Financiero reported. Walmart Chile CEO Horacio Barbeito said the sale aims to "give the best of retail and the finance world" to its customers, who will now be able to access credit through a well-known banking institution, Cooperativa reported. Barbeito added that the transaction will now allow Walmart Chile to focus entirely on its plans for growth in the South American country, where the retailer promised $800 million in investments through 2019. BCI announced last December that it would pay $148 million for the unit.

FEATURED Q&A / Continued from page 1

than half the Latin American average. However, the measure does not tackle the most important impediment to increased lending in Mexico. Efforts to address the high level of borrowers' informality and the weak legal framework that hinders repossession and recoveries could have a more favorable effect on credit intermediation. Nevertheless, this proposal could signal further intentions to undermine free-market conditions in the financial system, similar to those taken by other Latin American governments. Across the region, banks have been subject to interest-rate caps (Argentina, Bolivia, Chile and Colombia); mandated lending to specific industries (Argentina, Bolivia and Brazil); and the excessive leveraging of state-owned banks' balance sheets in support of specific policies (Brazil). These measures have, to varying degrees, weakened banks' asset quality and profitability and pressured capitalization, while generating distortions in the financial system with regard to interest rates and risk allocation."

A **Michelle DiGruttolo, senior managing director at Ankura:** "López Obrador is a canny and pragmatic politician who has thrived in a deeply fractured political environment through deliberate messaging. His base now contains a heady mix of social liberals and fiscal conservatives, making any policy choices sure to alienate one wing or the other and forcing him to deftly balance conflicting priorities and carefully craft his messages. A pro-business leftist, AMLO needs the support of the business community to fund his social welfare program and the support of his party to accomplish his policy agenda. Canceling projects like the Texcoco airport secure party loyalty, addressing corruption in infrastructure projects and reallocating resources to social safety nets.

> **"Reducing fees would increase access to credit for Mexico's poorest and rein in the profits of foreign-owned banks."**
> **— Michelle DiGruttolo**

Opposing limits to banking fees inspires business backing and demonstrates his commitment to growth. Banking fees are a particularly sensitive issue in Mexico, given the high concentration of foreign capital in the sector and the fact that banking fees are disproportionately higher there than in the rest of the region. Fees make it unaffordable for much of the population to have a bank account. Reducing fees would increase access to credit for Mexico's poorest and rein in the profits of foreign-owned banks. Clearly, AMLO will not be able to keep all the promises he has made, but no president does. Rather, over his first term, he will likely keep the promises he feels will best help him combat corruption, widen social safety nets and maintain economic growth. He will try to balance competing priorities in a way that appeals to both flanks of his base, negotiating compromises and redefining promises along the way."

Continued on page 6

POLITICAL NEWS

Honduran Leader's Brother 'Large-Scale' Trafficker: Officials

U.S. prosecutors on Nov. 26 described Juan Antonio "Tony" Hernández, 40, the younger brother of Honduran President Juan Orlando Hernández, as a "large-scale drug trafficker" who was so established in moving narcotics that he had his own cocaine brand and had his initials stamped on packets of the drugs, The New York Times reported. The younger Hernández spent a dozen years transporting cocaine through Central America and to the United States, prosecutors alleged. He was also deeply involved in a wide range of activities related to drug trafficking, which included arranging security for drug shipments, pocketing bribes from traffickers and assuring government contracts for companies that helped to launder drug money, Geoffrey S. Berman, the U.S. attorney in Manhattan, alleged. Hernández was charged with conspiring to import cocaine into the United States, as well as related weapons crimes and making false statements to federal agents, Berman added, WNBC-TV reported. Hernández, a former Honduran congressman, was arrested Nov. 23 in Miami. Between 2004 and 2016, several drug trafficking rings in Honduras worked with prominent public and private individuals, including politicians and law enforcement officers, in order to receive cocaine shipped from locations including Colombia and then transport them to the United States, prosecutors alleged Nov. 26. The drug traffickers also bribed public officials, including members of Honduras' Congress, to aid in the effort, prosecutors added. Juan Antonio Hernández was linked to a drug trafficking ring called Los Cachiros when the ring's former leader, Devis Leonel Rivera Maradiaga, struck a plea deal with U.S. prosecutors, testifying that he had paid the president's brother a bribe, The New York Times reported. The younger Hernández has denied previous allegations of involvement with the criminal group, Reuters reported. Rivera has been cooperating with the U.S. Drug Enforcement Administration since 2013, and those convicted in connection with his testimony include Fabio Lobo, the son of former Honduran President Porfirio Lobo, The New York Times reported. In a statement

Hernández was so established that he had his own cocaine brand, prosecutors alleged.

THE DIALOGUE CONTINUES

Is Bank De-Risking Choking Caribbean Growth Prospects?

Q During the U.N. General Assembly meeting in October, three Caribbean leaders, including two prime ministers, said bank "de-risking" and the loss of correspondent banking relationships have severely harmed their economies. Among them, Timothy Harris of St. Kitts and Nevis said the trend is hindering the island nation's development trajectory. How big a problem is bank de-risking for Caribbean economies and their banking sectors? Has compliance with international financial regulations, many of which originate in the United States and Europe, become too onerous for Caribbean banks to cope with? What would it take to reverse the de-risking trend?

A Rogelio Cardozo, managing director of Italbank International: "De-risking poses significant challenges to developing economies. As an international financial institution based in Puerto Rico, Italbank has witnessed this trend first hand as well as its substantial impact on small- to medium-sized enterprises (SMEs) and on regional trade. The implications are serious as correspondent banking allows SMEs and individuals to safely move money across borders and around the world. The lack of correspondent banking services has had a disturbing effect on economies in terms of trade and remittances. In the Caribbean, 12 countries have had the correspondent banking relationship (CBR) of at least one of their local banks terminated. As a result, trade and often the flow of goods are restricted, impeding economic growth. From our regional experience, we can attest that all banks are facing burdensome challenges in serving clients. Much of the stress is on local banks and their economies. Regional and/or global banks have more options. There are also higher standards to cater to local SMEs and international trade needs. As Georges Hatcherian indicated in his commentary in the most recent issue of the Financial Services Advisor, global banks have cut CBR relationships due to limited economic benefits. Therefore, smaller niche U.S. financial institutions with knowledge of Caribbean markets are needed to better balance risk. A greater proximity approach that spreads risk as banks partner with local financial institutions and fintechs opens new income avenues. Local economies can be positively affected at both ends of the trade relationship. For all of this to happen, forward-thinking regulators are needed to promote frameworks that allow smaller institutions to enter into these relationships."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in the Nov. 1-14 issue of the Financial Services Advisor.

NEWS BRIEFS

Incoming Mexican Finance Minister to Seek Larger Budget Surplus

Carlos Urzúa, Mexico's incoming finance minister, said Nov. 26 that he will seek a larger government budget surplus next year as part of the government's efforts to boost investor confidence, Reuters reported. Andrés Manuel López Obrador takes office as the country's president on Dec. 1, and Urzúa has said the new administration is aiming for a budget surplus of about 1 percent next year, as compared to a projected surplus of 0.7 percent this year.

Peru Near Settlement in Odebrecht Case: Prosecutor

Brazil's Odebrecht and Peruvian prosecutors are close to agreeing on a settlement in relation to the probe into bribes the construction company paid in exchange for public work contracts in Peru, Rafael Vela, one of the prosecutors, told Reuters on Nov. 26. He did not provide any further details about the deal. Odebrecht has confessed to paying around $30 million in bribes in Peru, where the four most recent former presidents are under investigation for alleged links to the massive corruption scheme.

Costa Rica's High Court Backs Tax Reform Plan

Costa Rica's Supreme Court on Nov. 23 ruled in favor of a tax reform that would increase taxes and cut government worker benefits to address the country's mounting debt, Reuters reported. The bill, which President Carlos Alvarado endorses and which lawmakers approved in October, will now go back to the Legislative Assembly for a second vote. Opposition lawmakers had argued the government illegally fast-tracked the bill through the assembly. Thousands of public workers have been on strike to protest the reforms since September. on Nov. 23, the office of Honduras' president confirmed the arrest of the president's brother and said no one was above the law. Attorney information for Juan Antonio Hernández was not immediately available, WNBC-TV reported. If convicted, he faces a life sentence in prison on the drug and weapons charges and five years in prison on the charge of making false statements to federal agents.

Panamanian Judge Orders Martinelli to Stand Trial

A Panamanian judge on Nov. 26 ordered former President Ricardo Martinelli to stand trial on political espionage charges, the Associated Press reported. Martinelli, who was the Central American country's president from 2009-2014, is accused of ordering the interception communications of at least 150 people and also spending millions of dollars on equipment to be used for spying, the wire service reported. Martinelli is also accused of embezzling government money because the spy equipment purchases are alleged to have been for "personal benefit." Martinelli has denied wrongdoing. If convicted, he faces up to 21 years in prison.

ECONOMIC NEWS

Ecuador Estimates it Needs $550 Mn for Migration Crisis

The Ecuadorean government said Nov. 23 that it needs $550 million to cope with the influx of Venezuelan migrants, El Tiempo reported. Santiago Chávez, Ecuador's deputy minister of human mobility, said the Andean country hopes to raise the funds with the help of multilateral agencies and nearby countries, Reuters reported. Ecuador estimates some 600,000 Venezuelans have crossed into the country after traveling through Colombia, with most on their way to Peru. Officials from Ecuador, the United States, Canada, Japan, Qatar and the European Union are scheduled to meet on Nov. 30 in Quito to discuss how to deal with Venezuelan outmigration, which the United Nations estimates has reached around three million people since 2015. [Editor's note: See related Q&A in the Nov. 19 issue of the daily Latin America Advisor.]

Air Travel Expected to Double in Latin America by 2037

Latin America's air travel volume is expected to double in the next two decades, according to a market forecast report released Nov. 20 by European manufacturer Airbus. The region's expanding middle class, which could grow from 350 million people to 520 million by 2037, underpins the forecast, as well as "evolving airline business models" that will make travel more accessible, the report said. Passenger traffic in the region has more than doubled since 2002 and is expected to increase from 0.4 trips per capita in 2017 to nearly 0.9 trips per capita in 2037. "We continue to see growth in the region's air transport sector, despite some economic challenges," said Airbus regional president Arturo Barreira in a statement. Earlier this year, U.S.-based Boeing, an Airbus rival, announced it had expanded its commercial service capabilities in Latin America with Brazil's GOL Linhas Aéreas and Mexico's Aeroméxico. Boeing expects that by 2036, the region's aviation support and services market will be valued at $530 billion.

> **"We continue to see growth in the region's air transport sector, despite some economic challenges."**
> — Arturo Barreira

FEATURED Q&A / Continued from page 3

A Alfredo Calvo, director and sector lead of financial institutions ratings at S&P Global Ratings: "Recently, the Mexican supervisor in charge of protecting individual users of financial services highlighted that bank charges in Mexico were high—fee income to bank's revenues are estimated to be above 30 percent, levels significantly higher as compared to Mexican banks' respective international parents. This has made banks' commissions a controversial issue and resulted in the initiative to eliminate certain banking fees and commissions, most of them related to credit cards. Mexican banks' ratio of fee income to operating revenues is neither the highest nor the lowest among global peers. In Mexico, according to our estimates, fees and commissions represent 17 percent of operating revenues as of Sept. 30 and average 18 percent during the past four years. This level is below what we see in Canada, Spain, the United Kingdom, Argentina and Brazil, among other countries. In our opinion, if the Mexican Congress passes the proposal to eliminate certain banking commissions, we expect a limited impact for Mexican banks' profitability and risk-adjusted capitalization. However, our assessments would vary depending on the relative importance of the credit card loan portfolio within each financial institution's business portfolio. If the proposal becomes effective, generally, we expect banks' operating revenues to drop around 7 percent. Banks with at least adequate diversification by business line will be better positioned to face such a scenario and offset the impact.

> **"Mexican banks would have some flexibility to offset the potential impact of this proposal to their capital and earnings."**
> — Alfredo Calvo

In our view, Mexican banks would have some flexibility to offset the potential impact of this proposal to their capital and earnings. For instance, they might use margins (higher interest rates on their lending products and/or lower in their retail funding products) and tighten cost-containment policies. Moreover, the application of conservative growth strategies could also release pressure on capitalization levels."

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

FINANCIAL SERVICES ADVISOR
is published biweekly by the
Inter-American Dialogue, Copyright © 2018

Erik Brand
Publisher
ebrand@thedialogue.org

Gene Kuleta
Editor
gkuleta@thedialogue.org

Anastasia Chacón González
Reporter
achacon@thedialogue.org

Financial Services Advisor is published biweekly, with the exception of major holidays, by the Inter-American Dialogue at
1155 15th Street NW, Suite 800
Washington, DC 20005

www.thedialogue.org

ISSN 2163-7962

Subscription inquiries are welcomed at
freetrial@thedialogue.org