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FEATURED Q&A

How Important Is Latin America for Multinational Banks?

Spain's Banco Santander said this month that earnings from its Latin American units offset weakness at its operations in Europe. // File Photo: Santander Brasil.

Q **Banco Santander on July 23 reported an 18 percent drop in second-quarter earnings, year-on-year, but reported strength in its Latin American units, which it said offset weakness in Europe. Brazil has become the Spanish lender's main profit driver, contributing a 19 percent rise in earnings. To what extent are Latin American and Caribbean units contributing a growing share of the profit for multinational banks, and why? Which countries are especially fruitful for international lenders, and what consumer trends or other factors are driving profitability? Will such trends continue into the medium and long term?**

A **Alejandro Garcia, managing director and regional group head for Latin American financial institutions at Fitch Ratings:** "Latin America represents a key strategic objective for some major global financial conglomerates. As is usual with emerging markets, Latin American countries pose near-term economic and political uncertainties. However, the medium-term prospects are benign and point to a good-looking reward against those short-term challenges, driven by a number of factors, including the relatively low level of financial intermediation, favorable demographics and gradually improving financial conditions for businesses and households. In addition, spreads, margins and overall earnings are typically higher in emerging markets than in more mature economies when measured across longer periods and throughout the economic cycle. Therefore, the combination of good business opportunities, relatively high expected returns and the byproduct of geographic diversification is typically attractive for multinational banks. Conse-

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Goldman Sachs Sees Improving Credit Conditions in Brazil

Credit conditions are likely to improve in the coming months in Brazil amid moderating risk, Goldman Sachs said in a note. Credit demand should pick up as the labor market improves, the investment bank said.

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Newline Group Establishing Mexico City Office

The London-based specialty insurance group said it will establish a presence in Mexico City through a Lloyd's representative office.

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Nubank Raises $400 Million in Investment Round

Nubank, led by Chief Executive Officer David Vélez, announced that it had raised the funding in its Series F investment round. U.S.-based growth equity firm TCV led the round.

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Vélez // File Photo: Nubank.

BANKING NEWS

Goldman Sachs Sees Improving Credit Conditions in Brazil

Credit conditions are likely to improve gradually in the coming months in Brazil amid moderating risk, Goldman Sachs said July 26 in a note. As Brazil's economy is forecast to recover, credit demand should pick up as the labor market also improves, the New York-based multinational investment bank added. However, overall political risk and macro policy risk are "a source of uncertainty which could eventually undercut the bank credit cyclical recovery," wrote Alberto Ramos, Goldman Sachs' managing director and head of Latin America economic research. Lending rates on non-earmarked credit declined in June by 20 basis points, despite a 30 basis-point increase in lending rates to individuals, Ramos said in the note, adding that corporate credit lending rates declined 80 basis points to 18.7 percent. Nonperforming loans fell 10 basis points to 3.8 percent in June, with the nonperforming rate on corporate credit at a cyclical low of 2.6 percent and to individuals at 4.8 percent, the note said. In addition, lending to individuals sped up to 6.5 percent year-on-year in real terms in June, as compared to 5.1 percent in May and 1.7 percent in June 2018, Goldman Sachs added. [Editor's note: See Q&A on Brazil's economy in the July 24 issue of the daily Latin America Advisor.]

Santander Posts Fall in Q2 Profit, But Latin America Shines

Strong second-quarter profit growth in Latin America helped offset Spanish lender Santander's lackluster performance in Europe, Bloomberg News reported July 23, as the bank reported an 18 percent fall in quarterly net profit. Santander registered a net profit of 1.39 billion euros ($1.56 billion) for the second quarter, higher than the 1.29 billion euros analysts expected, according to a Reuters poll. The euro zone's largest bank in terms of market capitalization, Santander was hit by one-off restructuring costs from its acquisition of Banco Popular in Spain and a weak performance in Britain, where profit fell 41 percent. However, solid performances in Brazil and Mexico in the second quarter helped the lender cope with dire results in Europe. The bank's operations in North and South America account for a rising share of underlying earnings, with Brazil being the bank's main profit driver with a jump of 19 percent. Santander Chairman Ana Botín said the results would have been even better if Brazil's real had not fallen against the euro. "The evolution of countries in Latin America continues to be a vital support," Nuria Álvarez, an analyst at Renta 4 Banco in Madrid, told Bloomberg News. On July 23, Santander shareholders voted to approve a 2.6 billion-euro capital increase to fund the acquisition of a 25-percent stake that they do not control in the lender's Mexico unit, Reuters reported.

> **"The evolution of countries in Latin America continues to be a vital support."**
> **— Nuria Álvarez**

FINANCIAL TECHNOLOGY NEWS

Brazil's Nubank Raises $400 Million in Investment Round

Brazilian financial technology company Nu Pagamentos, commonly known as Nubank, announced July 26 that it has raised $400 million in its Series F investment round. U.S.-based growth equity firm TCV led the round, marking what Nubank said was the firm's "first significant investment in Latin America." Existing investors Tencent, DST Global, Sequoia

NEWS BRIEFS

Banco do Brasil to Offer Buyouts to Workers Amid Effort to Reduce Costs

Banco do Brasil said July 29 that it plans to offer buyouts to some of its workers amid a push to reduce costs, Reuters reported. The state-controlled bank said in a security filing that it had a plan to "optimize" its workforce and trim "excess" at its bank units in an effort to lower costs. The lender did not say how many of its workers would be offered buyouts but said it would disclose the financial impact of the move by the end of August. Bank officials are planning to convert some of their 333 locations to simpler operations with potentially lower costs. Brazilian banks are increasing efforts to lower expenses amid higher levels of competition from digital fintech companies such as Nubank.

Newline Group Establishing Mexico City Office Through Lloyd's

London-based specialty insurance firm Newline Group is establishing a presence in Mexico City through a Lloyd's representative office in the city, Newline said July 30. Newline said its Latin America division will be able to start underwriting liability and financial lines coverage right away.

FacePhi to Provide Facial Recognition to Banco de Crédito del Perú

FacePhi, a provider of facial recognition technology, announced July 26 that it has secured a contract with Banco de Crédito del Perú. The contract is the first in Peru for the technology firm, which specializes in biometrics in the fintech field. BCP's customers will be able to use the company's SelphID technology on mobile phones with iOS and Android operating systems as well as on the bank's website.

Capital, Dragoneer, Ribbit Capital and Thrive Capital also participated in the round, Nubank said. With the latest investment, Nubank has raised $820 million in seven rounds of investment. The latest investment values the company at more than $10 billion, The Wall Street Journal reported. Nubank previously engaged in talks about a potential investment from SoftBank Group, but the talks broke down, the newspaper reported, citing people familiar with the matter. The funding makes Nubank

The latest investment reportedly values the company at more than $10 billion.

Latin America's most highly valued private technology company, The Wall Street Journal reported, citing PitchBook Data. Nubank said in a statement that it has opened offices in Mexico and Argentina and is preparing to begin operations in those countries. The company is Brazil's sixth-largest financial institution by number of clients, and it began its international expansion in May. It has expanded its product portfolio beyond its app-controlled credit card and rewards products and now offers personal loans and digital savings accounts for individual consumers, as well as microentrepreneurs and small- and medium-sized businesses. "Even though the technological change has been transformational for most industries across the globe, most banked consumers continue to pay absurd interest rates and fees to receive very poor financial services in return," Nubank's founder and chief executive officer, David Vélez, said in a statement, adding that two billion people in the world still lack basic financial services. "With this new investment by TCV and our existing investors, we expect to contribute to meaningfully change this situation by accelerating our growth in Brazil and supporting the launch of our new Latin American markets." About 10 million people use Nubank's digital credit card, consumer banking and lending services, The Wall Street Journal reported, citing a person familiar with

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quently, we expect that these entities will maintain, or even increase, their interests in the region over time. Some countries in Latin America are relatively more attractive than others, especially those that have conditions such as large and diversified economies, sound and stable macroeconomic policies, strong and evolving banking regulations, good degree of competition and openness, and/or attractive profitability metrics. Based on these, the key target markets in Latin America for multinational banks over the medium term are Brazil, Mexico, Chile, Colombia, Argentina and Peru, but smaller economies are increasingly under the radar of these conglomerates."

A **Tiago de Lima Binsfeld, equity research analyst at Itaú BBA:** "Multinational banks' net income from Latin American and Caribbean units have grown at a higher pace than units in other regions. In the case of Santander, 43 percent of consolidated net income stemmed from Latin American countries in 2018 (up from 38 percent in 2015). For BBVA, this share was 41 percent in 2018 (up from 40 percent in 2015). At Santander, the main driver behind the solid earnings expansion was the results from the bank's operations in Brazil, where it had gained market share in recent years. We compiled the aggregate earnings of the banks with operations in Brazil, Chile, Colombia, Peru, Mexico and Argentina from 2015 to 2018. Net income of this sample totaled $49 billion in 2018, with multinational banks representing 24 percent of this amount (up from 20 percent in 2015). Within these five countries, Mexico, Peru and Chile had a larger participation of foreign financial institutions in 2018, measured as a percentage of net income. In Colombia and Brazil, domestically controlled banks are more relevant. Brazil is the largest addressable market in Latin America, with a population of 210 million people, 30 percent of which do not have financial accounts. Latin American economies are more unbanked as compared to developed markets, particularly in younger populations, thus there is stronger earnings growth potential given the potential addressable market. The main driver for profitability in Brazil's banking system is the level of interest income. Because of the high interest rates in Brazil, interest expenses have been relatively high. More recently, this funding cost has been trending down as the benchmark Selic interest rate dropped to 6.5 percent and could decline further. As a result, return on equity in the Brazilian banking system averaged 15 percent as of 2018 and reached 20 percent for the largest private banks in the country."

A **Mark Manger, associate professor of political economy at the Munk School of Global Affairs & Public Policy at the University of Toronto:** "For the two major Spanish banks—BBVA and Santander—the expansion into Latin America turned them from large domestic banks into competitive international players. Both grew in Spain by acquiring numerous smaller domestic rivals but ran into natural limitations in the saturated home market. For a variety of strategic reasons, BBVA expanded into Mexico but left Brazil, while Santander did the opposite. Although the Brazilian economic recovery and the current bout of optimism regarding President Bolsonaro's reforms has boosted Santander's earnings, it is important to remember that as recently as 2015, BBVA was praised for having exited Brazil and for focusing on the Mexican market instead. Political risk is never far away in Latin America. Nonetheless the region still holds much promise for international banks: The economies are relatively 'underbanked,' driven by consumption, and acceptance of credit cards is as common as in much of Europe, though of course still less than in North America. We can expect the growth of consumer credit to continue despite often exorbitant interest rates of more than 40 percent per annum.

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the matter. The company has a partnership with Mastercard and launched its digital credit card and mobile app in 2014. Nubank advertises the credit card and app as free to consumers and generates revenues from outstanding credit card balances and merchant fees, the newspaper reported.

POLITICAL NEWS

Guatemalan Official Seeks Reversal of 'Third Country' Deal

Guatemalan human rights prosecutor Jordán Rodas on July 29 asked the country's Constitutional Court to nullify a deal that President

Rodas // File Photo: Guatemalan Government.

Jimmy Morales' government reached with the administration of U.S. President Donald Trump requiring Central Americans transiting Guatemala to request asylum there instead of the United States, the Associated Press reported. In the appeal, Rodas argues that the deal was reached under threats from Trump, who recently said his administration would possibly levy tariffs or "remittance fees" if Guatemala did not agree to its proposal. "We presented an appeal for what was signed to be declared null and not take effect," Rodas said, the AP reported. "Article 52 of the Vienna Convention signals that any treaty or agreement … that has been obtained under threats is null." Rodas also requested the removal and investigation of Foreign Minister Enrique Degenhart, who he argues had no authority to sign the deal at the White House on July 26. Guatemala's Constitutional Court had previously granted three injunctions ordering Morales' government not to enter into a deal without approval from Guatemala's Congress, which it ignored. Under the agreement, Salvadorans and Hondurans that transit Guatemala will not be allowed to apply for asylum in the United States unless they did so in Guatemala first, and migrants could be sent back from the United States to Guatemala, regardless of their country of origin. Critics have blasted the agreement, saying Guatemala is not a safe destination for migrants who are mostly fleeing from poverty and violence in their home countries, The New York Times reported.

ADVISOR Q&A

What Is Holding Back Mexico's Economy?

Q Mexico's industrial output declined 2.1 percent in May as compared to April, the country's National Statistics Institute said July 12. The sharpest drop in industrial output in a decade, the statistic was among recent data that suggest the country's economy slipped into a recession in the second quarter, following a 0.2 percent contraction in the first three months of the year. What factors are most weighing on Mexico's economy? What does Mexico need in order to return the country to growth? How well is President Andrés Manuel López Obrador managing the economy, and how would a recession affect his agenda?

A Charles Seville, senior director for Americas sovereigns at Fitch Ratings: "Mexico's overall output has stalled, as shown by the economic activity indicator for May. As ever, the data present a mixed picture. Households are continuing to spend, and manufacturing and exports (7 percent higher year-on-year in May) are holding up. U.S. growth remains supportive. Investment is the main weak spot. Part of this may relate to global trade uncertainty, but domestic policy considerations are also weighing on sentiment. Business confidence is still in positive territory but has weakened. Microeconomic policy interventions by the government have increased uncertainty in some areas. Actions to tackle some of the weaknesses in Mexico's business environment and reduce corruption will take time to pay off. Moreover, monetary and fiscal policy are also tight. Real interest rates are among the highest in the region, yet core inflation is still higher than the central bank would like. Lower government spending is subtracting from activity. We expect this effect—typical of the first year of a presidential term—to fade. Public investment has been cut over successive years, but higher investment, not to mention some proposed programs, will be difficult to accommodate within the current fiscal framework. Pemex will receive more resources to carry out a revised business plan. The company announced that it had stabilized crude production in the second quarter, although we think it's too early to celebrate. A still relatively new administration faces a classic trade-off between maintaining the confidence of investors in the policy framework and supporting the economy. So far, it has chosen the former. Meeting the fiscal target of a 1 percent of GDP non-financial public sector primary surplus is within reach in 2019, but meeting a higher target in 2020 may prove challenging. We expect Banco de México will cautiously start cutting rates this year, helped by a more dovish global rates picture."

EDITOR'S NOTE: More commentary on this topic appears in the July 29 issue of the Latin America Advisor.

NEWS BRIEFS

Paraguay's Foreign Minister Resigns Over Energy Deal With Brazil

Paraguayan Foreign Minister Luis Castiglioni and three other officials resigned on July 29 amid a public outcry over the signing of an energy deal with Brazil, Reuters reported. Lawmakers and officials say the energy agreement, related to the Itaipu hydroelectric plant at the two countries' border, would be detrimental to Paraguay and cost the country some $200 million. The agreement was reached in May but was just recently made public. The Paraguayan government said it would ask Brazil to suspend the deal.

Mexico's López Obrador Wants Lower Interest Rates to Boost Growth

Mexico should cut interest rates to boost economic growth, President Andrés Manuel López Obrador told Bloomberg News in an interview on July 29, adding that he respects the central bank's autonomy. "The Bank of Mexico is watching over inflation. That's not bad," he said, "But it's important to lower rates to kickstart the economy." Mexico's central bank has kept its benchmark rate at a decade-high of 8.25 percent, even as inflation slowed to less than 4 percent.

Ecuador's Moreno Signs Decree Requiring Venezuelans to Have Visas

Ecuadorean President Lenín Moreno on July 26 signed a decree requiring visas for Venezuelan citizens wishing to enter the country, who previously could cross the border with just a passport or other form of identification, Reuters reported. The measure is part of a wider security plan for migrants, which outlines tighter regulations and a non-obligatory census of Venezuelans in Ecuador to help them access education, health and welfare benefits.

Puerto Rico Secretary of Justice Doesn't Want Governor's Job

Puerto Rico Secretary of Justice Wanda Vázquez, who is next in the line of succession to replace Governor Ricardo Rosselló, said July 28 that she does not want to be governor of the U.S. territory. Rosselló is set to step down Aug. 2 after announcing his resignation the previous week following days of massive protests demanding his ouster. "I have no interest in occupying the position of Governor," Vázquez said on Twitter. As secretary of justice, she was next in the constitutional order of succession, given that the territory's secretary of state, Luis G. Rivera, who would normally replace the governor, also resigned, CNN reported. Rivera was a member of a group chat at the heart of the scandal that resulted in Rosselló's resignation. Hundreds of pages of group messages that included misogynistic and homophobic comments as well as jokes about victims of Hurricane Maria were leaked, prompting Puerto Ricans to take to the streets in numbers comparable to past protests demanding that the U.S. Navy leave Vieques island in the early 2000s. Puerto Ricans protested against Vázquez, calling on her to resign. "Her positions and her character as a person is well aligned with what Ricardo Rosselló represents," Mayra Velez Serrano, a professor of political science at the University of Puerto Rico at Río Piedras, told CNN. "It's no surprise that Puerto Ricans don't want her either." [Editor's note: See related **Q&A** in the July 23 issue of the daily Latin America Advisor.]

U.S. Treasury Sanctions Family of Venezuela's Maduro

The U.S. Treasury Department on July 25 accused three stepsons of Venezuelan President Nicolás Maduro of involvement in an alleged scheme to steal hundreds of millions of dollars from the South American country's food subsidy program. In addition to sanctioning the stepsons, the Treasury also imposed sanctions on seven other people, including a prominent Colombian-born businessman, Alex Saab, who the Treasury alleged was the mastermind of the alleged scheme. "Alex Saab engaged with Maduro insiders to run a wide scale corruption network they callously used to exploit Venezuela's starving population," U.S. Treasury Secretary Steven Mnuchin said in a statement. "Treasury is targeting those behind Maduro's sophisticated corruption schemes, as well as the global network of shell companies that profit from the former regime's military-controlled food distribution program." The Treasury accused Maduro's three stepsons, Walter, Yosser and Yoswal, of receiving money that Saab allegedly funneled to them in exchange for Venezuelan government contracts, including ones for the food subsidy program.

ECONOMIC NEWS

Argentina Posts First Rise in Economic Activity in a Year

Argentina's government said July 25 that economic activity rose in May for the first time in more than a year, Reuters reported. The 2.6 percent increase in May from the same month a year ago exceeded estimates of analysts in a Reuters poll. Economic activity in Argentina had fallen 1.3 percent in April versus the same month in 2018, the 12th consecutive monthly decline. Argentina's Treasury Department said the rise was due to strong growth from the farming sector, which it said was up nearly 50 percent versus a year ago, as well as improvements in sectors including transportation, industry, commerce and construction. Bad weather conditions damaged crops last year across much of the country. Looking ahead, better salaries and lower inflation should help boost consumer spending, the statement added. The improving economy is good news for conservative President Mauricio Macri, who is in a tight campaign for re-election.

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The biggest challenge is the large informal employment sector that makes credit risk assessment more difficult. Here, fintech firms are opening up new markets. We can expect international banks to partner with these firms or to develop their own solutions to seize these growth opportunities."

A **Ravika Rameshwar, associate attorney, and Audriana Rodriguez, law clerk, at Diaz Reus & Targ:** "Within the past few decades, Latin America has shifted from playing a minor role in the international banking industry to becoming one of the world's strongest and most profitable regions. Countries such as Brazil, Mexico and Colombia have experienced the largest growth in international lending as a result of the region's success in managing volatility within the financial market, coupled with high capital levels and management of high risk. Another contributing factor to the region's growth stems from the technological advances affecting the banking industry; digital banking has transformed the market, as banks can more readily detect the level of credit risk a consumer poses. While Latin America appears to face optimistic prospects for continued growth in international lending, the region's biggest threat is its political climate. Changes in administrations can greatly affect the profitability of Latin America and ultimately dictate the region's future in international lending."

> **"Countries such as Brazil, Mexico and Colombia have experienced the largest growth in international lending..."**
> **— Ravika Rameshwar & Audriana Rodriguez**

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

JOB POSTINGS

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

MetLife: Director of Governance, Latin America, New York

Accion: Senior Director, Digital Transformation, Latin America

Mastercard: Manager, Managed Services, Mexico City

Zimmer Biomet: Compliance Senior Counsel, Investigations, Latin America

Hillrom: Financial Analyst, Latin America, New York

U.S. Air Force: Professor of National Security Studies (Latin America), Alabama

Inter-American Development Bank: Resource and Planning Specialist, Washington

Inter-American Dialogue: Coordinator, Development and External Relations

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