

FINANCIAL SERVICES ADVISOR

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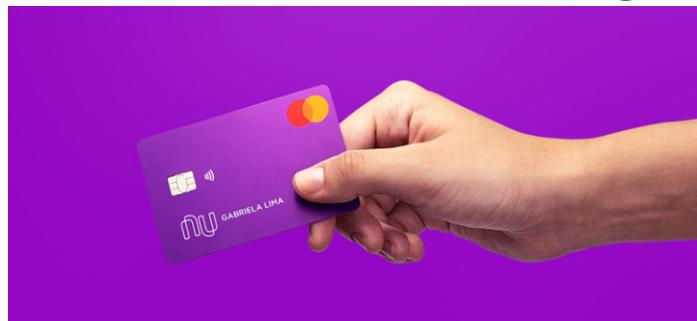
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FEATURED Q&A

How Are Fintechs Changing Latin American Banking?



A recent investment round has given Brazilian financial technology company Nubank, a sample card of whose is shown, a value of more than \$10 billion. // File Photo: Nubank.

Q **Brazilian financial technology company Nubank announced July 26 that it had raised \$400 million in its latest investment round, giving the firm a value of more than \$10 billion. The company, founded in 2013, has become Brazil's sixth-largest financial institution by number of clients and started an international expansion in May. How are fintechs such as Nubank changing the financial services landscape in Latin America and the Caribbean? What are the traits of the most successful fintech companies in the region? How are brick-and-mortar banks and other traditional financial services companies responding to the growth of fintechs in the region, and how is the trend affecting their businesses?**

A **Wally Swain, principal consultant for Latin America at Ovum:** "There can be no doubt that fintech is gaining mindshare in the region, at least with investors and policymakers. Statistics on the number of fintech start-ups and the amount of capital they attract are astounding. The fundamental reality of start-ups—especially Internet-based start-ups where barriers to entry tend to be fairly low—is that few will be considered successful, and even fewer will become stand-alone businesses, such as Nubank. There is only one Airbnb, three ride-sharing platforms (Uber, Lyft, Didi), and a few commerce platforms (Amazon, eBay, Alibaba, MercadoLibre) in Latin America. Banking regulation will mean this 'law of nature' will play out locally, not globally (so one or perhaps two Nubanks per market), but that will be the only difference. Many or perhaps most of the successful fintechs will be absorbed into existing businesses, probably traditional banks. The banks

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TOP NEWS

FINANCIAL SERVICES

AFP Habitat Buys Colombia-Based Colfondos

Chile-based pension fund manager AFP Habitat has agreed to acquire Colfondos following a deal with Canada's Scotiabank and Mercantil Colpatria.

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INSURANCE

China Boosting Presence in Latin America Insurance Markets: A.M. Best

China is gaining strength in the region's insurance sector, said a senior director at A.M. Best.

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FINANCIAL SERVICES

Banco Macro Reports 4 Percent Profit Slide in Q2

Argentina's Banco Macro, led by CEO Jorge Brito, reported net income for the second quarter that totaled 7 billion pesos (\$153 million), a 4 percent decline from the previous quarter. However, recurring net income rose 37 percent as compared to the first quarter.

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Brito // File Photo: Superagente86 via Creative Commons.

FINANCIAL SERVICES NEWS

Banco Macro Reports 4 Percent Profit Slide in Second Quarter

Argentine bank Banco Macro's second quarter net income totaled 7 billion pesos, or roughly \$153 million, down 4 percent from the previous quarter, the lender said in a statement on Aug. 7. Recurring net income amounted to 7.8 billion pesos, increasing 2.1 billion pesos, or 37 percent, from the January-March period. The bank's financing to the private sector grew 705 million pesos quarter over quarter and 23.8 billion pesos year-on-year, totaling 174.7 billion pesos. Commercial loans, especially overdrafts, drove this growth, the statement said. In the second quarter, Banco Macro's total deposits also rose 4 percent to 284.3 billion pesos, or 84 percent of the bank's total liabilities. Private sector deposits grew 7 percent, about 16.2 billion pesos. The lender's accumulated annualized return on average assets was 7.7 percent, while its accumulated annualized return on average equity was 47 percent, according to the statement. Banco Macro is Argentina's second-largest bank, and the sixth-largest lender in the country in terms of deposits and lending. JPMorgan Chase recently increased its price target for Banco Macro, from \$57 to \$61, according to a research report sent to investors, Mayfield Recorder reported. The New York-based investment bank currently has a neutral rating on Banco Macro's stock.

Chile's AFP Habitat Buys Colombia-Based Colfondos

AFP Habitat, Chile's largest pension fund manager, has agreed to acquire Colombia's Colfondos after reaching a deal with Scotiabank and Mercantil Colpatria, the Canadian bank said in a statement on Aug. 9, Reuters reported. Scotiabank, which owned 51 percent of Colfondos, said the sale would allow it to

focus on its banking operations in the Andean country. Colpatria owned the remaining 49 percent of Colfondos, Colombia's third-largest pension fund manager. AFP Habitat manages \$60 billion worth of private pension funds, mostly in Chile and Peru. The acquisition of Colfondos would mark AFP Habitat's first entry into the Colombian pension market, Citywire reported. The sale process could take between four to six months, according to Colfondos'

The deal reportedly has a value of more than \$170 million.

chief investment officer, Andrés Lozano Umaña, who told Citywire Americas that Colfondos' investment strategy would not change following the sale and that there were currently no plans to make any personnel changes. AFP Habitat's main shareholders are Inversiones La Construcción and Prudential Financial, both of which indirectly own 40.3 percent of its shares, according to the report. The deal reportedly has a value of more than \$170 million, according to La República. Regulatory approval is still pending, and it is expected by the end of this year or early next year, the newspaper reported.

FINANCIAL TECHNOLOGY NEWS

Six of 10 Brazilians Use Digital Payment Methods: Study

Six out of 10 Brazilians use digital services including applications such as PayPal, PagSeguro and Google Pay as a method for payment of bills, purchases and transactions, The Rio Times reported Aug. 2, citing a recently published IDC survey. Sixty-one percent of the survey's respondents in Brazil—which were more than 1,000 people in total across the country's middle and upper classes—reported using digital wallets, according to the study. In

NEWS BRIEFS

Canadian Billionaire Buying 15% Stake in Argentine Digital Bank

Canadian billionaire David Thompson is buying a 15 percent stake in Argentine digital bank Brubank, Bloomberg News reported Aug. 2. The bank has no physical branches, but it does have 40,000 customers after seven months in operation. The deal is subject to approval by Argentina's central bank.

Former Banamex CEO Medina Mora Dies at 69

Influential Mexican banker Manuel Medina Mora, who was an executive at Citigroup for many years and served as chief executive officer of the bank's operation in the country, then known as Banamex, died Aug. 7 at 69 after a battle with multiple sclerosis, Reuters reported, citing Citi's Citibananamex unit. He was diagnosed with the disease just months after he retired, El Financiero reported. Medina Mora was credited with turning around the lender and making it Citi's most important foreign operation, Reuters reported. However, his legacy was tarnished by loan fraud scandals at the unit.

Mexican Banks Report Problems With Card Payment Processing

Several of Mexico's largest banks, including Banorte, HSBC and Santander, on Aug. 10 reported experiencing problems processing debit and credit card payments, and stores in Mexico City were only accepting cash payments, Puerto Vallarta Daily News reported. The PROSA system, a leading electronic banking system, was reportedly presenting problems in Latin America, including with ATM transactions, point of sale terminals, recurring charges and Payware, among others. PROSA said the evening of Aug. 10 that the issues had been repaired.

Mexico, that number was 62 percent, while in Colombia it was 52 percent.

WEX Appoints New Latin America Managing Director

Financial technology service provider WEX announced Aug. 1 that it appointed Marcelo Geraldi Velloso as the new managing director of Latin America at its São Paulo office, the company said. Velloso has previously held executive leadership roles in several Latin American countries. Before joining WEX, he served as chief operating officer of Madeira-Madeira in Curitiba, in Brazil, as vice president of Atento in both Brazil and Mexico and as executive director of retail bank and wealth management at HSBC México. As WEX's Latin America managing director, Velloso will be responsible for continuing to expand the company's payment offerings in the Latin America market, the statement said.

INSURANCE NEWS

China Becoming Stronger Player in Insurance: A.M. Best

China is gaining strength in Latin America's insurance sector, Carlos De la Torre, senior director at credit ratings agency A.M. Best told the Financial Services Advisor in an email. "China is certainly becoming a stronger player with a far more established presence in Latin America when compared with a few years ago," said De la Torre in response to questions about reports that People's Insurance Company of China (PICC) is seeking permission from Argentina's insurance watchdog to begin operating in the South American country as early as September. "PICC's recent meetings with regulators, brokers and ceding companies show that it's prepared to solidify a presence in Argentina, and we anticipate, expand through

FEATURED Q & A / Continued from page 1

have significant influence over regulators in most Latin American countries (if not everywhere) and can shape regulation to retain their advantages in the marketplace. Regulators' understandable concerns about money laundering in the region and about cybersecurity and privacy are but three items of the list of issues that arise once fintech evolves from small-scale experiments to something that might seriously threaten traditional banks' market shares. It would be easier for the developer (and for regulators) if the banks find a way to absorb the innovation into their existing, regulated activities."

Fabian Saide, member of the Financial Services Advisor board and founder, CEO and president of Paykii: "We have heard about Peter Thiel's bible for entrepreneurs 'Zero to One,' but have you heard David Vélez's Nubank story? His is from zero to a \$10 billion valuation with more than 10 million customers within six years of inception. This is the story of a true disruptor who has challenged the oligopolistic banking industry in Brazil, against all odds. He has opened the opportunity for investors to focus on fintech and other start-ups to challenge the status quo. Nubank's strategy is customer-centric, with lower-cost products. Traditional banks can't replicate the fintech cost base. Nubank has started a revolution in Brazil, where more than 10 million customers enjoy much better services and rates today. This 'neobank' has just started, targeting Mexico and Argentina as new channels for growth.

the rest of Latin America once it grows more familiar with the region." China already has a presence in Latin America's reinsurance markets through reinsurance coverages of some property/casualty programs through Lloyd's, said De la Torre. Additionally, a joint venture between China Re and U.S.-based insurance company Mapfre will "potentially open the door to a presence" in at least 16 countries in Latin America where Mapfre operates, he added.

The digital era has arrived, and this is a late wake-up call for traditional banks. They need to go from bricks to clicks, develop a new digital identity to overcome years of 'my way'



Nubank has started a revolution in Brazil, where more than 10 million customers enjoy much better services and rates today."

— Fabian Saide

business models and evolve their generic products, which are the bulk of banks' portfolios, into very specific, customer-centric and low-based prices. As J.P. Morgan CEO Jamie Dimon warned shareholders and the banking industry in 2015, 'Silicon Valley is coming.'



Kai Schmitz, leader of FinTech Investment for Latin America at the IFC Global FinTech Investment Group: "Nubank is the third Brazilian fintech changing the financial services landscape. It follows PagSeguro and Stone, two merchant acquirers that set out to compete with market leader Cielo, at the time the most profitable listed company in Latin America and owned by two of the largest banks in Brazil. Comparing the share price of these entities provides an idea of the impact fintech can have. It also shows

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Chinese investment in various projects in Latin America is also a factor in the presence of Chinese insurance companies in the region, De la Torre said. "Given China's considerable investment and projects in the region, having one or more Chinese reinsurers willing to cover projects and companies that they are already familiar with would generate more competition for the current providers, thus, ideally offering more options to the final consumer," he said.

Chubb Names Latin America Regional VP

U.S. insurance company Chubb has named Marcos Gunn as regional vice president for Latin America, as well as senior vice president of Chubb Group, Insurance Business Magazine reported Aug. 2. In his new role, Gunn will oversee general management and business results for all operations in the Latin America region, including in Argentina, Brazil and Chile, among others, the company said in a statement. Gunn is currently the president for the company's Northern Latin America division, which handles affairs relating to Mexico, Central America and the Caribbean, and chief operating officer of the Latin America region. He will retain these roles until a successor is announced.

POLITICAL NEWS

Venezuela Pro-Gov't Assembly Eyes Early Legislative Elections

Venezuela's pro-government Constituent Assembly on Aug. 12 said it would create a commission to consider moving up the date of legislative elections planned for next year, a move that could give President Nicolás Maduro's government an opportunity to regain control of the country's opposition-led National Assembly, Reuters reported. The move came a day after opposition leader Juan Guaidó, whom dozens of countries recognize as Venezuela's legitimate president, warned that the Constituent Assembly would seek to disband the elected National Assembly and move up elections following Maduro's call for a "new offensive." Maduro's government created the powerful Constituent Assembly in 2017 and filled it with loyalists. On Aug. 12, the Constituent Assembly's leader, Diosdado Cabello, dismissed Guaidó's comments, saying there was no need to dissolve the National Assembly, saying it "didn't work" and "had eliminated

THE DIALOGUE CONTINUES

How Important Is Latin America for Multinational Banks?

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 **Cynthia Cohen Freue, director and sector lead for financial institutions ratings at S&P Global in Buenos Aires:** "International banks operating in Latin America that have the highest share of loans and contribution to revenues are BBVA, Santander and Scotiabank. This is after other lenders, such as HSBC and Citibank, reduced their exposure to the region. Bank operations in Latin America have widened their geographical diversification, which has proved positive and helped the groups withstand a difficult economic cycle in their home markets, such as Spain, during the financial crisis. International banks' profitability in Latin America has remained sound and resilient, even during economic downturns in Brazil and Argentina, while operations in developed

itself on its own," Reuters reported. The new commission would study when to schedule legislative elections "in accordance with the law, the Constitution and the political situation," said Cabello. He also issued a warning to opposition lawmakers, saying, "Don't go on vacation because we are going to make life

markets have posted thinner profitability metrics. BBVA generated about 50 percent of its net income in Latin America in 2018, while Santander posted 36 percent. However, their exposures are much lower (BBVA about 23 percent and Santander 20 percent). Mexico is contributing the most to BBVA (40 percent of net income in 2018), while Brazil contributed 26 percent for Santander, based on the relative exposure they have in those countries. On a comparative basis in the largest economies of Latin America, excluding Argentina, figures for which are not yet adjusted to inflation, Peru is the most profitable banking system (2 percent return on average assets) followed by Colombia (1.8 percent), Mexico (1.7 percent) and Brazil (1.4 percent), compared with Spain's 0.5 percent. The main drivers of stronger profitability have been healthy net interest margins, thanks to the banks' pricing power and resilient business model even during Brazil's downturn. We expect international banks operating in Latin America to continue showing stronger profitability metrics over the next two years due to their conservative lending standards, healthy provisioning coverage and sound margins."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in the July 18-31 issue of the Financial Services Advisor.

impossible for you over the next month." Venezuela's congressional elections are scheduled to be held every five years, with the next vote due in December 2020. In 2015, the opposition trounced Maduro's party to take control of the National Assembly. Maduro responded by refusing to recognize its actions, and the coun-

NEWS BRIEFS

Brazilian Prosecutors Seek to Block Bolsonaro From Naming Son Envoy

Brazilian prosecutors on Aug. 12 asked a court in Brasília to bar the appointment of President Jair Bolsonaro's son as ambassador to the United States amid concerns over nepotism, the Financial Times reported. The president last month nominated his son Eduardo, who currently represents Rio de Janeiro in the Chamber of Deputies, to take the top diplomatic post in Washington, sparking controversy. Prosecutors argue the position requires at least three years' experience serving Brazil abroad. The Senate would still need to approve Eduardo Bolsonaro's nomination.

Mexico Won't Cancel or Grant Any Mining Concessions: President

Mexico's government will not cancel any current mining concessions, but it also will not grant any new ones, President Andrés Manuel López Obrador said Aug. 12, Reuters reported. "We're going to keep the current concessions and not hand out new concessions because they aren't needed," he said. Mexico is the world's top silver producer and one of the largest producers of copper and gold. The mining sector makes up around 4 percent of Mexico's gross domestic product.

Former Panamanian President Martinelli Cleared of Espionage

Former Panamanian President Ricardo Martinelli was acquitted Aug. 9 of political espionage after being accused of spying on 150 politicians, journalists and union leaders, The New York Times reported. The court ordered Martinelli's release from prison, saying prosecutors had "failed to prove" their case. Martinelli had been living in the United States when he was extradited to Panama in 2018.

try's Supreme Court, which Maduro stacked with supporters, has overruled all of the elected legislature's decisions. Also on Aug. 12, the Constituent Assembly, which functions with no checks on its power, stripped the legislative immunity of four opposition lawmakers amid allegations of treason, the Associated Press reported. Cabello oversaw the unanimous vote that brought to 18 the number of politicians Maduro's government has threatened to prosecute this year. The four lawmakers are José Guerra, Rafael Guzmán, Tomás Guanipa and Juan Pablo García Canales, the AP reported. In a video posted online, Guerra called the charges "absurd." He added, "You're the ones who are traitors, who have left this country in misery and ruin." The National Assembly's vice president, Édgar Zambrano, remains jailed after he was accused of taking part in a failed military uprising against Mauro's government on April 30. Authorities towed away his car while he was still in it. Other legislators who fear prosecution have fled the country or sought refuge in foreign embassies in Caracas.

Giammattei Elected President in Guatemala Runoff

Conservative candidate Alejandro Giammattei won the second round of Guatemala's presidential election on Aug. 11, defeating former First Lady Sandra Torres, Prensa Libre reported. With 99.73 percent of the ballots counted, Giammattei received 57.95 percent of the votes, and Torres garnered 42.05 percent, according to the country's Supreme Electoral Tribunal, or TSE. The turnout was 42.71 percent, the lowest voter participation rate in a presidential election since 1999, The Wall Street Journal reported. Giammattei's victory came in his fourth run for the Central American country's presidency. "With a lump in my throat 12 years later, I come to tell you, for me, this humble servant, this humble citizen of Guatemala, it will be an immense honor to be the president of the country," Giammattei said in declaring victory, daily newspaper Prensa Libre reported. Giammattei, of the Vamos party,

thanked his supporters, saying voters backed his candidacy "so that Guatemala could win the possibility of moving forward." Just before being declared the winner, Giammattei told Reuters that he hoped to change a controversial migration deal that current President Jimmy Morales' government made with the United States.

ECONOMIC NEWS

Argentine Stocks, Peso Plunge After Peronists' Win

Argentine stocks plunged on Aug. 12 following President Mauricio Macri's crushing defeat in the country's primary election the day before, The Wall Street Journal reported. The Merval index in Buenos Aires closed 38 percent lower on Aug. 12, its steepest fall in decades, as investors worry over the possible return of a populist Peronist government, which advocates for greater state intervention in the economy and opposes a landmark trade deal with the European Union. The Argentine market's fall was the second-largest one-day rout on any of the 94 stock exchanges that Bloomberg has tracked since 1950. The Argentine peso also plummeted by more than 30 percent against the U.S. dollar before recovering some ground after the country's central bank took action on Aug. 12, auctioning off \$50 million to try to support the peso, The Wall Street Journal reported. The bank's benchmark interest rate was up to 74.8 percent, from 63.7 percent on Aug. 9. Stocks had jumped 7.7 percent that day on expectations that Macri would come in a close second to his opponent, Peronist candidate Alberto Fernández, whose running mate is former President Cristina Fernández de Kirchner. Macri lost the nationwide vote, which had no practical effects but served as a sort of national poll ahead of the October presidential election, by more than 15 percentage points. The wider-than-expected loss has largely reduced the chances of Macri being re-elected, analysts say, The Wall Street Journal reported.

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that once a market reaches a tipping point, it is hard to reverse. The success of these acquirers also demonstrates how technology enables fintech to generate value out of segments of the market not profitable for banks. Nubank comes from the other side, the credit card market, but it may have a similar impact. It still has a simple business model, mostly issuing cards, but is growing into a full digital bank and expanding across the region. Unlike Stone and PagSeguro, it is acquiring customers that are at the heart of banks' interests: young, higher-income, urban consumers. Other fintech companies in the region have also gained strength and evened the scale with big funding rounds. Creditas, Konfio and others have proven that they can compete with banks or enter segments of the market where banks are not present and attract sufficient capital to take on the competition. The trend for many fintech companies has become to emulate banks without actually being licensed as such. Most digital banks start without a banking license and instead offer their services with lighter regulation or in partnership with a bank. This BaaS model is an opportunity for banks to participate in fintech and gain share in markets they would not otherwise be able to succeed in. Banks sometimes assume that fintech companies would suffer from the same inefficiencies they deal with if the fintech companies become licensed as full banks. This may be wishful thinking. The lighter and more agile systems and higher levels of automation in fintech companies are more likely to maintain their competitive advantage. The development on both sides point to a future market where digital banks dominate and are either regulated former fintech companies or banks that have managed the digital conversion. The discussion about the (arguably high) valuations is useful for investors but should not be mistaken by banks to imply that the threat may be temporary. The world

is turning digital, and financial services are no different."

Lindsay Lehr, senior director at Americas Market Intelligence:
"Fintechs succeed when they fulfill an acute need. Nubank has been so successful because the need it is fulfilling—a free, easy-to-access credit card designed for young middle-class people—has been both chronic and critical. A credit card provides two key things: access to financing and e-commerce, as well as in-app purchases and digital subscriptions, the former of which has always been in high

Fintechs succeed when they fulfill an acute need."
— Lindsay Lehr

demand in Brazil, and the latter of which is increasing in demand. In response, banks in Brazil are following suit, sort of. Many large retail banks have launched a digital-only version (Next from Bradesco and SuperDigital from Santander) and offer a simpler, lower-cost version of their services. But credit card issuance by these incumbents, even within their digital subsidiaries, does not extend issuance to as broad a population and are still more expensive than digital natives, such as Nubank. Nubank and others were born to serve a particular population entrenched in the digital age, and they have the technology, agility and internal culture to do so. Traditional financial services providers who at their core cater to a different clientele will struggle to compete in that particular niche."

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

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