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FEATURED Q&A

How Hard Will the Pandemic Hit Latin America's Banks?

Businesses big and small have been shuttered amid the Covid-19 pandemic. // File Photo: Peruvian Government.

Q **Due to low global interest rates over the past several years, companies around the world have taken on ever-growing levels of debt. Now, as the coronavirus pandemic has pummeled commerce and economic activity, numerous countries are facing deep recessions. To what extent are banks in Latin America and the Caribbean at risk from potential corporate debt defaults? How prepared are the region's banks now as compared to during the global financial crisis more than a decade ago? What should governments in the region be doing in order to fortify their banking systems at a time that corporate customers may see increased struggles in servicing their loans?**

A **Jorge O. Mariscal, adjunct professor at the School of International and Public Affairs at Columbia University:** "In general, the banking systems in the large countries of Latin America are well capitalized and, I would argue, able to survive a garden-variety economic recession. But this will not be, by any stretch of the imagination, a garden-variety recession. The economic ramifications of Covid-19 undermine nearly all angles of economic activity, and they do it at punishing speed: availability of importer inputs due to supply chain disruptions, drop in exports as external demand falls, decline in commodity prices, freezing tourism, lower remittances, risk aversion in the global capital markets and a strong dollar, and a retrenchment in domestic consumption due to contagion containment efforts. So while much Latin American corporate debt has been issued in bonds and floated in the international markets, banks will have to face local loans

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Deals Plunge in Q1, Banks Bracing for Difficult Q2

Banks are bracing for a bleak second quarter as share offerings as well as mergers and acquisitions have dried up.

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López Obrador Urges Mexicans to Keep Sending Remittances

President Andrés Manuel López Obrador urged Mexicans living in the United States to continue sending money to their families back home despite the pandemic.

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PENSIONS

Peru's Congress Approves Measure for Pension Fund Withdrawals

Peru's Congress has approved and sent to President Martín Vizcarra legislation to allow workers to withdraw as much as 25 percent of their pension savings in order to mitigate hardships caused by the coronavirus pandemic.

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Vizcarra // File Photo: Peruvian Government.

BANKING NEWS

Latin American Banks Prepare for Bad Second Quarter

Banks in Latin America and the Caribbean are bracing for a bleak second quarter as share offerings have dried up as have mergers and acquisitions amid the coronavirus pandemic, Reuters reported April 3. In the first quarter, the volume of deals plunged 41 percent as compared to the same quarter last year, to $9.3 billion, the wire service reported. In Brazil, Latin America's largest economy, deal volume increased 17 percent in the first quarter to $6.7 billion, but officials there were comparatively late in ordering people to stay home in late March in order to slow the virus' spread. No large deal has been canceled so far in Latin America. The quarter's largest deal, Brazilian pharmaceutical company Hypera's acquisition of Takeda Pharmaceutical's operations in the region for $825 million is expected to close after recently receiving financing. Additionally, the $4.2 billion deal in which Brazilian aircraft manufacturer Embraer would cede approximately 80 percent of its commercial arm to U.S.-based Boeing is expected to proceed, Reuters reported, citing bankers working on the deal. However, bankers do not expect new deals to be announced during the pandemic because of the uncertainty surrounding when economic activity will begin returning to normal. "We are still working on deals, but new announcements will depend on a clearer perspective of when the world can expect to control the pandemic," Alessandro Farkuh, the head of investment banking at Bradesco BBI, told the wire service. Setting prices for deals has also reportedly been challenging. "There will likely be a valuation revision for ongoing deals. We know that the equities market is not a good proxy now, but how to calculate future cash flows?," said Daniel Damiani, a partner at JK Capital, a mergers and acquisitions boutique firm in São Paulo.

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>
> **— Alessandro Farkuh**

Crisis Will Forever Change How People Live: Scotiabank CEO

The Covid-19 pandemic will permanently change the way people live and work, Bank of Nova Scotia CEO Brian Porter said April 7 at the company's annual shareholder meeting, the Financial Post reported. "While the magnitude of the coronavirus pandemic is unlike anything we have faced in recent memory, it is certainly not the first crisis we have navigated," Porter said at the meeting, which was held online because of the pandemic. "There will undoubtedly be learnings from the crisis for us, at the bank, and for society more broadly. There will be permanent changes to the way people live, interact and work. New habits will be formed and behaviors ingrained." Porter said the banking system will survive the crisis, as will Scotiabank, which has spent more than 15 billion Canadian dollars ($10.7 billion) on technology over the past five years. The Toronto-based lender has operations in several countries in Latin America and the Caribbean.

REMITTANCES NEWS

López Obrador Urges Mexicans to Keep Sending Remittances

Mexican President Andrés Manuel López Obrador on April 6 urged Mexicans living in the United States to keep sending remittances back home despite the economic uncertainty

NEWS BRIEFS

Spain's Santander to Roll Out Int'l Payments System in Mexico This Year

Spanish bank Santander is planning to roll out its international payments system, One Pay FX, in Mexico this year, according to a securities filing, Cointelegraph reported March 30. One Pay FX is based on blockchain system Ripple, but it does not require digital currency to function. Santander describes the platform as a "multi-corridor international blockchain solution … for individuals and small-to-medium enterprises," according to the report. One Pay FX first launched in Santander banks in Spain, Brazil, Poland and the United Kingdom in 2018.

Brazilian Crypto Exchange XDEX Announces Closure

Brazilian crypto exchange XDEX on March 31 announced its closure, saying "market projection, competition and few regulatory advances reduced the opportunities found at the beginning of the project and were the basis for" the decision, Cointelegraph reported. XP Investimentos, one of Latin America's largest brokers, owned XDEX. The announcement marks the fourth company focused on Bitcoin trading that has announced it is closing operations in Brazil. [Editor's note: See related Q&A in the March 12-25 issue of the Financial Services Advisor.]

Republic Financial Holdings Contributing $2 Mn to Fight Covid-19

Trinidad and Tobago-based Republic Financial Holdings announced April 1 that it will contribute a total of $2 million across all the countries where it operates, including several Caribbean nations, such as Grenada, St. Lucia, the Cayman Islands and St. Kitts & Nevis. The funding will be used for the purchase of ventilators, personal protective equipment, testing kits, food and other supplies, the company said.

caused by the coronavirus pandemic, Milenio reported. “We thank the migrants very much because they continue sending help to their families,” López Obrador said at his daily morning news conference. “We tell our countrymen not to stop helping their relatives in Mexico, as they are also going through a difficult time. They shouldn’t stop thinking—as they always have—about their loved ones.” Dollars sent to Mexico have had benefited Mexico even more over the last few weeks due to the peso’s decline against the dollar, he said. “Remittances help in general because as more money circulates, there is more capacity to buy in stores, in businesses, in towns. This is a great help,” said López Obrador. In February, Mexico’s level of remittances grew 10.5 percent as compared to the same month last year, to $2.69 billion, the central bank said April 1. In a research note, Alberto Ramos, the managing director and head of Latin America economic research at Goldman Sachs, said remittances to Mexico would likely take a hit amid an economic downturn in the United States. “Solid workers’ remittances flows have been adding support to the current account and to private consumption, particularly for low-income families, who have a high propensity to consume and are the overwhelming recipients of such transfers,” said Ramos. “The expected sharp recession in the U.S. and spike in unemployment are likely to negatively impact the flow of remittances to Mexico.”

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defaulting as revenues vanish, as well as devalued defaulted bonds they may hold on their balance sheets. Banks will also see a rapid increase in nonperforming mortgages, consumer loans and credit cards. The response domestically should be to sacrifice short-term fiscal objectives and target support to minimize unemployment and loss of income, and to muffle the blow to those most in need. On the monetary front, central banks must inject liquidity and open lines of funding to the banking sector. But this is not likely to be enough, so the U.S. Federal Reserve and the IMF would have to extend support, not just to the ‘well-behaved’ countries, but also to emerging economies. Conditionality should not be based on fiscal or inflationary targets, but on whether governments adhere to scientists’ recommendations on how best to arrest the pandemic.”

A **Cynthia Cohen Freue, senior director and sector lead for financial institutions ratings at S&P Global Ratings:** “As the coronavirus pandemic escalates and growth stalls against a backdrop of volatile markets and rising credit stress, we now forecast a global recession this year. Even though Covid-19 reached Latin America later than other regions of the world, we expect Latin American banks to suffer through lower access to the international capital markets and see a deterioration in asset quality and operating performance. The pressure on banks’ asset quality will surge while loan growth will slow as the coronavirus outbreak hits trade and corporate demand for credit and consumer banking. As this public health crisis disrupts production and the plunge in consumption interrupts the payment chain, some companies and individual borrowers will have difficulty with debt repayment, but the regulatory measures, including forbearance on loan recognition and lower reserve requirements and interest rates and government subsidies to the more vulnerable sectors, will mitigate this risk to some extent. However, the extension of the quarantine will determine the degree of detriment to asset quality. We expect small- and medium-sized enterprises (SMEs) and self-employed workers, who have limited financial flexibility to cope with a sudden stop in cash flows, to suffer the most in Latin America. However, we believe that Latin America’s major banks can cope with a temporary disruption in capital markets because retail deposits provide the bulk of their funding, and because of the absence of significant debt maturities in 2020, thanks to banks’ conservative liability management while investors’ appetite for emerging markets was strong. In comparison to 2008, prior to the global financial crisis, credit penetration has increased, more so within the countries that have experienced stronger economic growth and increased the GDP per capita, which is a mitigating factor. In addition, banking regulators have introduced the Basel III requirements in the larger economies of the region, which

> **“The pressure on banks’ asset quality will surge while loan growth will slow...”**
> — Cynthia Cohen Freue

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PENSIONS NEWS

Peru’s Congress OKs Measure to Allow 25% Pension Withdrawals

Peru’s Congress has approved a bill to allow workers to withdraw as much as 25 percent of their pension savings to mitigate the economic effects of the coronavirus pandemic, shrugging off warnings that the measure will spook investors and drive up borrowing costs, Bloomberg News reported April 3. Lawmakers voted 107-4 in favor of the bill, which allows Peruvians who contribute or have contributed to the pension system to withdraw 100 percent of their savings if their pension funds are less than 4,300 soles (around $1,240) or as much as 12,900 soles if they have more, La República reported. According to Congress, which was recently elected to replace the one President Martín Vizcarra dissolved last year, pension administrators would have to transfer approximately 21,500 million soles if every person decides to withdraw from their fund, Reuters reported. The proposal has shaken up the $44 billion private pension industry in the Andean nation, with the potential sale of as much as $8.7 billion in stocks and bonds by Peru’s four private pension funds alarming foreign investors who own more than half of the country's local currency debt, Bloomberg News reported. Vizcarra can veto, propose amendments or sign the legislation into law. Congress can vote again for its promulgation.

POLITICAL NEWS

Morgues at Capacity in Guayaquil, Bodies Lie in Streets

Guayaquil has emerged as among the Latin American cities hardest hit by the coronavirus pandemic, with morgues in Ecuador's most populous city overwhelmed and bodies in some cases left lying on sidewalks and in the streets, UPI reported April 2. Other corpses have been left unclaimed in hospitals and clinics as fatalities have happened faster than crews can bury the dead. "They're leaving them in the villages, they fall in front of hospitals," Mayor Cynthia Viteri said in a recent video message. "No one wants to recover them." Viteri herself is quarantined after she tested positive for Covid-19. As of April 7, Ecuador had 3,747 confirmed cases of the disease and 191 deaths related to it. In the region, only Brazil and Chile have more confirmed cases. Authorities in Guayaquil say they have collected at least 400 corpses in recent days, UPI reported. Images on social media show people coughing outside of overcrowded hospitals in Guayaquil and some slumped over on the streets, the Miami Herald reported. "What's happened with our health care system?" Viteri said in a posting on Facebook. "Families are wandering the city, knocking on doors hoping a hospital will take them in, but there are no more beds." The city has raided a $10 million fund that was intended to celebrate Guayaquil's bicentennial in order to buy 50,000 additional testing kits, 40 portable ventilators and 20 ventilators for intensive care units, the newspaper reported. Additionally, it has brought in four refrigerated trucks to store bodies. Leaders elsewhere have taken notice of the dire situation in Guayaquil and are using it as a warning. "They said the pandemic wouldn't hit Latin America so hard because we're used to illnesses, because it's hot, because the population is young, etc, etc," Salvadoran President Nayib Bukele wrote in a posting on Twitter. "Look at what's happening in Ecuador. If you don't see yourself reflected in the mirror of Italy, Spain or New York, look at yourself in that one." Bukele has taken among the most aggressive measures in the region in an effort to contain the virus. He closed the country's borders and its international airport on March

THE DIALOGUE CONTINUES

What Does Market Volatility Say About Cryptocurrencies?

Q In mid-March, the value of cryptocurrencies plunged as financial markets around the world were roiled amid the coronavirus pandemic. While several asset classes saw severe declines, cryptocurrencies were hit especially hard, with Bitcoin plunging by some 50 percent since mid-February. What does the recent volatility in digital currencies reveal about them, and how will it affect their use in Latin American countries such as Argentina where they have been growing in popularity? How is policy on digital currencies developing in the region? How is the use of digital currencies affecting banks and other traditional financial services providers in Latin America and the Caribbean?

A Juan Llanos, global compliance advisor for multiple start-ups: "I think the recent volatility, especially the spectacular drop during what I call Dark March, was due to a number of relatively new, large, institutional market entrants suddenly panic selling as a result of the coronavirus pandemic. In any case, volatility in any new market including digital currencies such as Bitcoin is an expected growing pain. What this volatility reveals is precisely that: the market is small and inefficient, and therefore very sensitive to the actions of a few powerful speculative players, who in turn influence those who are tiptoeing into the market without much conviction. Volatility does not help with adoption, but countries such as Argentina and Venezuela, where the alternatives seem even riskier than these volatile digital assets, are more inelastic to price swings. I do not see any novelty or progress on digital currency policy in the region. Yes, there is a growing interest in digital money and innovation in financial technology, but countries are still wary of alternative digital currencies that are decentralized, resistant to censorship and relatively immune to traditional policy actions. The current crisis may change all this. In principle, given how early we are in the evolution of this industry, the use of digital currencies is not having much effect on banks and other traditional financial services providers in Latin America and the Caribbean. Traditional financial services continue to be the dominant players in the region, especially because they play the de facto role of market gatekeepers. Today, all digital currency service providers require bank accounts to be able to execute the basic use case of currency conversion, and obviously simply to operate as going concerns. At this point, the presence of alternative virtual currency-based services is only a market opportunity for traditional players. In time, however, as in the tale of the frog and the slowly boiling water, they may or may not start perceiving them as an existential threat."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in the March 12-25 issue of the Advisor.

NEWS BRIEFS

Eleven Killed in Colombia Coal Mine Explosion

An accidental explosion at a coal mine in Colombia's central Cundinamarca department killed 11 people and injured four, Mining.com reported April 5. The department's government and the local fire department did not provide details on the causes of the explosion, which occurred at the Veracruz coal mine in the Cucunabá municipality. The National Mining Agency announced a halt to all underground coal mining operations in the municipality following the incident.

Guatemala Asks U.S. to Limit Number of People on Deportation Flights

The government of Guatemalan President Alejandro Giammattei has asked the United States to limit the number of people it puts on planes for deportation to Central American countries to 25, BBC News reported April 6. The figure is down from a range of 60 to 90 people. Two people recently had to be taken to a hospital after they tested positive for coronavirus upon getting off a deportation flight. Guatemala has 74 confirmed cases, while the United States on Monday said it has surpassed 10,000 deaths from the virus.

Chilean Consul to Rosario in Argentina Dies After Contracting Covid-19

Chile's consul in the Argentine grains hub city of Rosario, Fernando Labra, has died after contracting Covid-19, Chile's foreign ministry announced April 1, Reuters reported. Labra, who was in his 60s and had nearly four decades of experience as a diplomat, developed symptoms after returning from a trip to Chile. Argentine Foreign Minister Felipe Solá expressed his "heartfelt condolences" to his Chilean counterpart over Labra's death, according to the statement.

14, before the country had even confirmed its first case of Covid-19. "The world IS NOT doing enough to stop the virus. Its advance is ruthless, and it has already brought the world's most powerful countries to their knees," Bukele tweeted. "We're also not doing enough. The worst part is that there are people complaining that we're being too strict. They don't understand anything." As of April 7, El Salvador had 78 confirmed cases of the disease and four related deaths.

Brazilian Health Minister Says He'll Remain in Position

Brazil's health minister, Luiz Henrique Mandetta, said April 6 that he will remain in his position after he and President Jair Bolsonaro overcame their disagreement, Veja reported. Amid the coronavirus pandemic, Mandetta has called for social distancing in order to fight the virus, in contrast to statements from Bolsonaro, who has downplayed the threat of the virus and has equated it to "a little cold." Brazil, Latin America's most populous nation, also has the largest number of confirmed Covid-19 cases in the region, with 12,377 reported infections and 582 deaths that have been caused by it as of April 7. "A doctor does not abandon his patient. We will continue," Mandetta, a pediatric orthopedist by training, told reporters April 6, Reuters reported. Throughout the day, there was speculation that Bolsonaro would fire him. "The government is taking a new position and it will be more focused," he added. Mandetta's stance had visibly irritated Bolsonaro, who had said, "Nobody should forget that I'm the president." Bolsonaro's downplaying of the pandemic has reportedly led to a split in his cabinet, with senior military officers siding with Mandetta on the need for more aggressive measures against the virus. Among them are Bolsonaro's chief of staff, Walter Braga, an active-duty general in Brazil's army, Reuters reported. Mandetta added that Brazil needs to finalize purchases of medical equipment from China. "We are not ready for the escalation of cases in our biggest cities," he told reporters. The health minister added that social interaction among Brazilians will inevitably lead to greater contagion of coronavirus to vulnerable parts of Brazil's society, including in its large cities and slums.

ECONOMIC NEWS

Fitch Downgrades Argentina's Debt After Payment Halt

New York-based Fitch Ratings on April 6 downgraded Argentina's debt after the government announced a plan to temporarily suspend payments on some $10 billion in debt denominated in U.S. dollars but subject to Argentine law, Reuters reported. Fitch downgraded Argentina's long-term foreign currency rating to 'Restricted Default' from 'CC' following the government's decree on April 5 that it will suspend all payments on foreign-currency securities issued in the domestic market for the rest of the year as it grapples with recession and the spread of coronavirus. Officials will continue restructuring talks with holders of $69 billion of bonds covered by foreign law, which the government has kept paying. The move is most likely to hurt investors who put their faith in the country's domestic bonds, while potentially improving the outlook for holders of international notes, Bloomberg News reported. President Alberto Fernández said in an interview published April 5 that the coronavirus pandemic had pushed the government's debt talks to the back burner and that the country would prioritize its response to the health emergency. In an effort to keep the economy breathing during the crisis, the Fernández government so far has extended lines of credit for housing, temporarily eliminated payroll taxes for certain sectors, made partial payments of private sector salaries and increased unemployment insurance and social security benefits, according to analysis circulated April 6 by Goldman Sachs. [Editor's note: See **Q&A** on Argentina's debt talks in the April 2 issue of the Dialogue's daily Latin America Advisor.]

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will help cushion a challenging and uncertain scenario in 2020."

A **Alejandro Garcia Garcia, managing director and regional group head for Latin America Financial Institutions at Fitch Ratings:** "Corporate and commercial loans usually make up a sizable fraction of banks' loan portfolios, particularly in Latin America, given the relatively high number of unbanked people and/or individuals and small businesses in the informal sector. The adverse economic outlook and its impact on income for businesses and households will certainly affect borrowers' capacity to repay, with the consequent impact for banks in the form of rising impairments and credit costs, as well as reduced profitability. While Latin American banks have been tested in previous crises, the reach and magnitude of the current shock is unknown. Banks typically lend hard currency loans primarily to exporting companies, whose debt repayment capacity will also be tested under more severe conditions of reduced aggregate demand globally, not to mention the price and volume shock for commodities, which are also relevant for the region's main countries. The banking systems in Latin America are relatively better prepared to face these adverse conditions as compared to the 2008 global financial crisis: the regulatory bar has continued rising in most countries; internal risk management frameworks have also been further enhanced; and the pace of loan growth in the years preceding this shock

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>
> **— Alejandro Garcia Garcia**

has been fairly limited. It is yet to be seen if these strengths will materially mitigate the effects of an unprecedented shock. It is probably too late for financial authorities to take preventive measures against this crisis, but hopefully there will be lessons learned to eventually strengthen regulation regarding borrower concentrations, and currency and liquidity risk management, among others."

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

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