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FEATURED Q&A

Will Rising Inflation Hold Back Profits at Argentine Banks?



Inflation could weigh on Argentine banks' performance this year. The headquarters of the country's largest bank, Banco de la Nación Argentina, is pictured. // File Photo: Barcex via Creative Commons.

Q Earnings in Argentina's banking sector will take a hit this year amid increasing inflation, Fabián Kon, the chief executive officer of Banco Galicia, said recently. The country's rising level of inflation adds to other economic problems facing Argentina, which is in its third year of recession. How will Argentina's banking sector fare this year, and what are the main factors weighing on banks' performance? How are President Alberto Fernández's policies affecting the banking sector? How quickly will Argentina's banking sector rebound now that Covid-19 vaccines are being rolled out?

A Marcelo De Gruttola, vice president and senior analyst in the Financial Institutions Group at Moody's Investors Service: "The performance of Argentine banks was resilient through 2020, supported by adequate profitability, which in turn led to an increase in capital buffers, rising local currency funding and ample liquidity buffers. Challenges for 2021 remain significant as operating conditions continue to be affected by persistent macroeconomic imbalances, and asset quality metrics do not yet reflect the full deterioration stemming from the pandemic. Also, margins, which have so far remained supportive of overall profitability, have already started to decline. We expect minimum deposit rates and caps on lending rates implemented by the central bank in 2020 to drive further margin pressure in 2021. The recent surge in deposits, mainly in low-cost demand deposits, have prevented a larger drop in margins, although banks are still exposed to margin compression as depositors may decide to move their funds to higher-yielding term deposits. Despite the drop in margins, banks continued to report

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BANKING

JPMorgan Chase to Close Mexico Private Banking Unit

JPMorgan Chase is reportedly closing its private-banking unit in Mexico. The lender signed an agreement to refer local business in Mexico to BBVA.

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REMITTANCES

Remittances to Mexico Rise More Than 25% in January

Mexico received \$3.3 billion in remittances in January, a 25.8 percent increase year-on-year.

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BANKING

Colombian Banks Asked to Hold Profits

Colombia's top banking regulator has asked lenders to retain nearly 68 percent of their profits in order to increase assets ahead of an expected deterioration in loan portfolios. Jorge Castaño said it "will not be an easy year in terms of easing of risk."

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Castaño // File Photo: Colombian Government.

REMITTANCES NEWS

Mexico's Remittances Rise 25 Percent in Jan.

Mexico received approximately \$3.3 billion in remittances in January, a 25.8 percent increase as compared to the same month last year, beating analysts expectations, the Bank of Mexico announced March 1, EFE reported. In the first month of this year, the average amount of a money transfer to Mexico was \$343, higher than \$322 from January 2020, the central bank said. The number of transfers also increased, to 9.61 million, as compared to 8.13 million in January of last year. The majority of transfers were done electronically, the Bank of Mexico said. Last year, amid the Covid-19 pandemic, Mexico received \$40.6 billion in remittances, a record amount, and an increase of 11.4 percent as compared to 2019. "Generous wage/income support fiscal transfers in the U.S., a very competitive MXN/USD level and a deep contraction of activity and employment in Mexico have acted as both push and pull drivers of dollar remittances from the U.S. to Mexico," Alberto Ramos, managing director and head of Latin America economic research at Goldman Sachs in New York, said in a note. "The expectation of continued fiscal stimulus and robust growth profile in the U.S. should keep remittances flow strong in 2021." Mexico's record level of remittances have more than offset the country's loss of income from international travel and tourism and led the country to have a current account surplus of 2.4 percent of gross domestic product last year, "the strongest current account outturn in more than 30 years," Ramos added. Mexico's income from remittances far outpaced the \$14.6 billion that the country received from exports of crude oil, Ramos added. "At a time when the Mexican economy is one of the world's hardest hit by Covid-19, the additional income from family members in the United States is crucial to sustaining living standards," Alma Caballero, director at McLarty Associates, told the Financial Services Advisor in a [Q&A](#) published Dec. 16. "Many of the essential industries in the United States, including the entire food industry, profession-

al maintenance contractors and agriculture, among others, are powered by migrants who have continued to work amid the pandemic," Caballero added.

FINTECH NEWS

Goldman Sachs Boosts Credit Line to Mexico's Konfío

Goldman Sachs has agreed to increase its credit line to Mexican financial technology start-up Konfío to \$160 million, the start-up said Feb. 25 in a statement. "Konfío is changing the way Mexican companies gain access to credit, bringing to the market an agile and innovative process based on powerful proprietary technology," Goldman Sachs spokeswoman Maeve DuVally said in a statement. The credit line was increased from a previous commitment of \$100 million, Bloomberg News reported. The expanded credit line will allow the fintech to increase the number of loans it provides to small- and medium-sized companies. Konfío was founded in 2013 and has granted nearly 50,000 loans since then. Approximately 7,000 of those loans remain active. The Covid-19 pandemic forced Konfío to lower its new financing in order to provide debt relief to customers it already had, Bloomberg News reported. That led it to secure a 1.3 billion peso (\$64 million) loan from the Inter-American Investment Corp. in order restart new lending. Konfío also has funding from Japan's SoftBank Group, which plans to invest approximately \$1 billion this year from its Latin American private equity fund. SoftBank will make approximately 70 percent of those investments in Brazil, though it also sees opportunities in Mexico, Colombia and Argentina, the Latin America fund's manager, Paulo Passoni, told Bloomberg News earlier in February. Konfío's clients can have loan proceeds within 24 hours of filling out an application without posting collateral, the news service reported. The fintech focuses on small- and medium-sized enterprises that it says are underserved by traditional banks.

NEWS BRIEFS

Brazil Plans Tax Hike on Financial Institutions

Brazil's government is planning to increase taxes on some financial institutions and the chemical industry while also ending a federal tax on diesel and cooking gas, Bloomberg News reported March 2. Banks will see the country's "CSSL" tax rising to 25 percent from 20 percent, while credit cooperatives and insurance companies will see it rising to 20 percent from 15 percent.

Ecuadoreans Charged in U.S. With Defrauding Police Pension Fund

Two Ecuadorean citizens have been charged in the United States in connection with an alleged bribery and money laundering scheme connected to Ecuador's public police pension fund, the U.S. Justice Department said March 2. John Luzuriaga Aguinaga and Jorge Chérrez Miño were charged in the Southern District of Florida with conspiracy to commit money laundering. Chérrez, an investment advisor, is accused of paying more than \$2.6 million in bribes to officials of the pension fund, known as ISSPOL, in order to obtain and retain investment business. Among those officials was Luzuriaga, who allegedly received \$1.4 million. Chérrez allegedly received payments in an account in the United States.

Mexican Fintech Stori Raises \$32.5 Million in Funding Round

Mexican consumer fintech Stori has raised \$32.5 million in Series B funding, led by Silicon Valley-based Lightspeed Venture Partners, Stori announced Feb. 25 in a statement. Other participants included Vision Plus Capital, BAI Capital and Source Code Capital. The funding will go toward supporting the company's "rapid growth" and brings the company's total funding to \$50 million.

Traditional financial institutions in Mexico decreased their loans to small- and medium-sized enterprises by 9.4 percent in real terms last year, Konffo said.

BANKING NEWS

JPMorgan Chase to Close Mexico Private Banking Unit: Report

JPMorgan Chase is closing its private-banking unit in Mexico, Bloomberg News reported Feb. 24, citing unnamed sources with knowledge of the matter. The largest lender in the United States, JPMorgan signed an agreement to refer local business in Mexico to BBVA's unit in the country, one of the people said. However, the New York-based financial services company will continue to serve clients in Mexico from an international platform. The news follows a similar action in Brazil, Latin America's largest

The news follows a similar move in Brazil, where JPMorgan has wound down its private-banking business.

economy, where JPMorgan wound down its private-banking business and referred Brazilian wealth clients to the country's Banco Bradesco, the news service reported. JPMorgan posted record profit in Brazil last year, new country chief Daniel Darahem said last month. Total assets in the Brazil unit were up 118.8 billion reais (\$22 billion) as of September, according to central bank figures, Bloomberg News reported. The lender will reportedly maintain other businesses in Mexico. A company spokesman declined to comment to Bloomberg News about JPMorgan's reported exit from Mexico. Wealthy clients in Latin America have been moving their money to international

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positive inflation-adjusted earnings through 2020. In turn, we expect the abundant funding and liquidity buffers banks built last year to support loan growth this year, provided that the incipient economic recovery holds. Although banks have already increased loan-loss provisions since the domestic recession started in 2018, credit costs might also add additional profitability pressures if asset quality stress proves larger than expected. Nonperforming loan metrics have remained low in 2020, although loan tenor extensions and regulatory waivers for nonperforming loan recognition still cloud the view on the underlying deterioration in credit quality, which will likely materialize in the coming quarters."

A Cynthia Cohen Freue, senior director and sector lead for financial institutions ratings at S&P Global Ratings: "Argentina experienced one of the sharpest GDP contractions among its peers in Latin America in 2020, and we expect only a mild recovery in 2021. This said, the Argentine banking system has remained relatively resilient, thanks to conservative policies and regulations, which have resulted in a low credit penetration, among the lowest in the world, with credit-to-GDP estimated at about 12 percent. This has helped banks to maintain relatively manageable asset quality metrics despite the deterioration, with nonperforming loans to total loans at about 4.2 percent as of December (2.2 percent for private banks). Profitability weakened last year due to higher provisions and lower margins but remained relatively healthy with a return-on-equity for the banking system at around 15 percent. However, we expect profitability to weaken due to the inflation adjustment and continuing need to raise provisions due to the challenging economic environment. Banks are exposed to extraordinary government measures, such as additional initiatives on direct lending, but so far, they have been able to fulfill the requirements on direct

lending while remaining profitable. Another recent measure is the creation of a new tax on credit cards transactions by the city of Buenos Aires, which could discourage the use of credit cards, affecting banks' profits. We expect lending growth to be relatively conservative, as banks usually expect economic growth to come before they take on the risk of boosting lending. Therefore, we expect credit growth to be slightly above inflation, and we expect a continue decrease in dollar-denominated loans and deposits."

A Pablo Bréard, founder and owner of Latin Context in Toronto: "Argentina's economy remains in systemic stagflation. The government and its ill-equipped economic team (including the central bank) perpetuated Argentina's economic isolation and mishandled the global pandemic, without an effective vaccination strategy in sight. In light of a severe macroeconomic crisis, systemic risk within the domestic banking sector is escalating. Key factors shaping the systemic health of the banking sector (eloquently reflected in current market valuations) include the following. 1.) (Hyper)inflation: Consumer price inflation accumulated 440 percent over the past 5 years (1,030 percent in the last decade). Persistently vivid price pressures (inflation this year is estimated at 50 percent) add further fuel to the hyperinflationary fire. If not contained, the super-high inflation environment undermines the viability of the Argentine peso as the national currency. 2.) Capital and price controls: The existing monetary arrangement is unsustainable. The 'exchange rate targeting' regime led to major relative price distortions and eroded the credibility of the peso worldwide. Regrettably, a much-needed abandonment of disruptive price controls and 'systemic subsidies' will not materialize any time soon. 3.) Critical elections: Legislative elections will take place on Oct. 24. Deeper control of Congress by the central government might further damage the quality of the judiciary

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financial capitals in recent years, bankers said, driven among other reasons by the policies of Mexican President Andrés Manuel López Obrador's government.

Colombian Banks Asked to Hold Profits to Boost Assets

Colombia's banking regulator has asked lenders to retain close to 68 percent of the profits they made last year in a bid to increase assets ahead of expected further deterioration in their loan portfolios this year, the regulator said Feb. 26, Reuters reported. The country's bank earnings plunged by 55.3 percent last year to 6.1 trillion pesos (\$1.7 billion) due to adjustments needed to manage debt that was overdue by more than 30 days, according to the report. Overdue debt was approximately 5.4 percent, or about 26.5 trillion pesos, of all debt on banks' balance sheets last year, a trend that is expected to spill over to this year as well. "It will not be an easy year in terms of easing of risk," said Jorge Castaño, the head of the Superintendency of Finance, América Economía reported. "The portfolio will continue to deteriorate and it's natural that will occur in proportion with a lag between the behavior of the economy and the behavior of attention to [debt] obligations," he added. For this reason, and because of uncertainty, "it is prudent at this time not to distribute these dividends, to leave that money within the entity so it can support unexpected loss," Castaño said.

Credit Card Use Drops in Argentina

Fewer Argentines used credit cards to finance household spending in February, breaking an eight-month upward trend, Clarín reported March 7. Consumer credit contracted 2.8 percent last month as compared to January. Personal loans also fell, declining 0.9 percent in February. Meanwhile, credit to private-sector companies contracted 2.3 percent that same month, according to the report.

RESEARCH ALERT

Remittances to Latin America Grow 6% in 2020 Despite Pandemic: Report

By Diana Roy

Family remittances to Latin America and the Caribbean grew 6 percent in 2020, according to a [report](#) published in February by the Center for Migration and Economic Stabilization at Creative Associates International. More than 30 million households in the region received remittances worth more than \$114 billion despite a 3.7 percent decline in global income last year as a result of the Covid-19 pandemic and subsequent economic recessions.

The positive growth represents a countercyclical trend in the region, with remittance flows from the United States growing even during a recessionary period that saw global trade fall by 10 percent and tourism by more than 50 percent, wrote the authors of the report, Manuel Orozco and Jessica Spanswick.

The increase in flows was most prominent in Jamaica, the Dominican Republic and Haiti, which saw 30 percent, 16 percent and 14 percent growth, respectively. There were also significant increases in the amount of money migrants sent to Central American countries, the report said.

However, remittances to some Latin American countries shrank last year. Venezuela experienced the largest decline—a 20 percent plunge in money transfers—while in Bolivia, remittance flows fell by 19 percent, the second-sharpest drop in Latin America. Remittance growth in Paraguay and Peru also declined, by 14.4 percent and 14 percent, respectively.

Despite the overall regional increase in remittances, GDP growth in each country included in the analysis was down, with Venezuela experiencing a 30 percent decline alongside a 58 percent decrease in trade growth.

Where migrants are located may play a role in the remittances they send home, with those living in the United States possibly at an economic advantage than those in less developed countries, the report said. For example, Guatemala, which received 90 percent of its money transfers from the United States, saw a 7 percent year-over-year increase in remittance flows.

Another factor that could help explain the general upward trend in remittances in the region is the amount of time a migrant community has lived abroad, the report added. The longer a migrant has lived in the United States, the more time they have to plant roots, earn money and increase their savings, with potential impact on the amounts and frequency with which they send money to their home country.

Technology has also played a role in the general increase in remittance flows, as there was a notable shift to the use of online money transfers. Mexico observed a 10 percent growth in digital remittances transfers. Meanwhile, the market share of digital or online remittance companies increased from 21 percent to 36 percent in terms of originating transactions during this period.

NEWS BRIEFS

Annual Inflation in Mexico Rises at Fastest Rate in Four Months

Annual inflation in Mexico accelerated to its highest rate in four months in February but continued to be within the central bank's target range, according to data from national statistics agency INEGI March 9. Consumer prices were up by 3.76 percent in the year through February, slightly above analysts' expectations of 3.72 percent, according to a Reuters poll. Energy prices rose sharply, up 3.47 percent, with gasoline rising 5.08 percent.

OECD Sees Recovery in Latin America, Africa Behind Rest of the World

The OECD on March 9 released new forecasts predicting global GDP growth will reach 5.6 percent this year, an upward revision of more than one percentage point since its projection in December, and 4 percent in 2022. However, the recovery is likely to be more moderate in the emerging market economies of Latin America and Africa due to "a resurgence of the virus, slow vaccine deployment and limited scope for additional policy support." Meanwhile, expected stimulus spending in the United States could boost growth by 0.5-1 percentage points in major U.S. trading partners such as Canada and Mexico, the OECD said.

Venezuela Begins to Ration Diesel Fuel

Venezuelan state oil company PDVSA has begun rationing diesel fuel to truckers due to low domestic refining output, Reuters reported March 7. With some of the largest oil reserves in the world, Venezuela has long offered diesel fuel to truckers at no cost and continues to do so. The shortages could have implications for electricity production in the months ahead, as parts of the nation's grid are dependent on thermal generation.

POLITICAL NEWS

Court Ruling in Brazil Could Pave Way for a Lula Run Next Year

A Supreme Court judge in Brazil on March 8 annulled the corruption convictions that have barred former leftist President Luiz Inácio Lula da Silva from running for office, Folha de S.Paulo reported. Justice Luiz Edson Fachin cited procedural grounds in removing the convictions, arguing the cases were tried in the wrong jurisdiction, meaning the ruling may not affect numerous other convictions of elites also swept up in the sprawling "Car Wash" investigations centered on corruption at state-run oil company Petrobras, the Associated Press reported. Lula was released from prison in November 2019 after 580 days behind bars, but he has been unable to seek political office due to the convictions, The Guardian reported. The annulment surprised observers and led to speculation that Lula will run for president in next year's election against far-right President Jair Bolsonaro. Supporters of Lula celebrated the news, shouting from their windows, "Out with Bolsonaro!" according to a Foreign Policy report. Bolsonaro sought to play down the news. "I think the Brazilian people don't even want a candidate like that in 2022," he said. Lula had led in the polls in the 2018 election campaign before his first corruption conviction prevented his candidacy. Bolsonaro's approval rating slumped to 33 percent in February, from 41 percent in October, according to a poll released Feb. 22 by transport association CNT, Reuters reported.

Paraguayans Call for President's Ouster in Third Day of Protests

Paraguay saw its third day of civil unrest March 7 as protesters again took to the streets in outrage over alleged corruption and mismanagement in the government of Mario Abdo Benítez,

ABC Color reported. In the capital Asunción, marchers draped in the national flag carried signs expressing anger over a health system that has reached a saturation point due to the Covid-19 pandemic, as well as allegations that government-purchased health supplies and medicines had been illegally obtained by private merchants who were reselling them at a profit. The crowds were also calling for the resignation of Benítez's vice president.

Biden Administration Offers Venezuelans Protected Status

The administration of U.S. President Joe Biden announced March 8 it would allow Venezuelans who can demonstrate continuous residence in the United States to apply for temporary legal status, The Hill reported. "The living conditions in Venezuela reveal a country in turmoil, unable to protect its own citizens," Department of Homeland Security Secretary Alejandro Mayorkas said in a statement. More than 300,000 Venezuelans currently living in the United States would be able to apply for Temporary Protected Status, or TPS, letting them stay in the country for 18 months, CBS News reported. Many of them have fled a humanitarian crisis at home under socialist President Nicolás Maduro, whose authoritarian government has been hit with numerous economic sanctions from Washington. "To keep deporting Venezuelans back to Maduro's tragedy would be to tell them they are a burden on our communities, a menace to our national security, and an unwelcome guest in our country. Reality and our national interest are precisely the opposite," said Sen. Robert Menendez (D-N.J.), who led previous legislative efforts to secure TPS for Venezuelans. While the administration of former Republican President Donald Trump declined to provide TPS to Venezuelans, some in his party supported Mayorkas' action. "It is critical that we continue working with our democratic allies to secure a Venezuela free from tyranny and ensure this temporary status in the U.S. does not become a permanent one," said Sen. Marco Rubio (R-Fla.), according to the report.

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and impair the rule of law. Moreover, bank earnings will suffer from the absence of structural reforms needed to boost economic and employment growth in the foreseeable future. 4.) Explosive public debt: Depleting central bank foreign exchange reserves, Paris Club debt amortization and electoral-related delays in renegotiating a \$49 billion credit facility with the IMF are all relevant factors heightening systemic risk in Argentina's banking sector. It remains unclear what position the U.S. Treasury, the dominant force inside the IMF, will adopt toward Argentina's political regime."

A **Santiago Gallo, director for Latin American banks and nonbank financial institutions at Fitch Ratings:** "Fitch expects the prolonged recession, together with the effects of the pandemic, to underpin a sustained deterioration in the banking system's performance. Profitability will remain under pressure due to slow loan growth, higher credit costs, narrowing margins, likely lower gains from central bank securities, persistently high inflation and peso depreciation. Asset quality has been under significant pressure. Although nonperforming loans decreased to 4.2 percent as of December from their peak of 6.1 percent in February 2020, this

was due to regulatory forbearance. Fitch expects the deteriorating trend to resume in 2021 as loan forbearance measures expire. Fitch expects loan growth to remain low in 2021 with any improvement greatly dependent on the extent of the economic recovery, inflation and the policy framework to be implemented by the government. Fitch estimates a modest recovery of the Argentine economy of 4.7 percent in 2021. The vaccination process could help but, so far, it has been slow. Interventionist regulations by Argentina's central bank, such as capping interest rates on loans and placing floors for deposit rates amid very low credit growth, have increased Argentine banks' exposure to the public sector as nearly the only type of credit currently growing is the one under the credit facility for small- and medium-sized enterprises established by the central bank, which carries an interest rate that is below the floor for deposits rate. On the positive side, given loan book contractions in the recent past, banks have ample liquidity and good capitalization, with a Core Equity Tier 1 ratio of 21.4 percent as of December."

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

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Advisor Video

The Economist's Michael Reid on Latin America's Social Contract

The Latin America Advisor talked with Michael Reid, "Bello" columnist and senior editor for Latin America and Spain at The Economist, about the region's social contract in the context of upcoming elections in South America.



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