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FEATURED Q&A

How Would Rising Rates Affect the Region's Banks?



Latin American central banks are facing pressure to raise interest rates. The Chilean central bank's monetary policy committee is pictured in 2018. // File Photo: Central Bank of Chile.

Q Central banks in Latin America are facing increasing pressure to raise interest rates as inflation heats up in the region. Annual inflation is running above policymakers' targets in locations including Brazil, Mexico and Chile as economic activity rebounds from the downturns wrought by the Covid-19 pandemic. How would rising interest rates in Latin American countries affect commercial banks in the region? How would higher interest rates change lenders' loan portfolios, and which sectors would be most influenced by higher rates? In which countries of the region are commercial banks most sensitive to rising interest rates, and what will that mean for bank customers in those countries?

A Theresa Paiz Fredel, senior director for Latin America Financial Institutions at Fitch Ratings in New York: "As inflation pressures materialize in some Latin American countries due to higher commodity prices, faster-than-expected economic recoveries and base effects, pressure to tighten monetary policy has begun, with Brazil, Mexico and more recently Chile already hiking policy rates. Higher interest rates in Latin America generally have a positive impact on net interest margins as commercial banks across the region remain predominantly deposit-funded, of which a material portion of these deposits are nonremunerated or low cost. The net effect on bank credit metrics will depend on the extent that higher rates contribute to deterioration of asset quality. If gradual rate increases occur along with economic and wage growth, then this could underpin higher credit growth and offset risks to borrowers' repayment capacity, thus sustaining

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Brazil's Conductor Reportedly Hires Banks for U.S. IPO

Brazilian payments company Conductor is reportedly hiring banks for an initial public offering in the United States. The IPO could happen as early as this year.

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A.M. Best Keeps Negative Outlook for Mexico's Insurance Sector

The ratings agency said several "aggravating factors" are affecting fundamentals in Mexico's insurance industry.

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REMITTANCES

Brazil's Nubank Starts Money Transfer Service

Brazilian digital bank Nubank has started a remittance service through a partnership with Remessa Online. Nubank co-founder Cristina Junqueira said the partnership was the best way to quickly offer the transfer service to customers.

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Junqueira // File Photo: LinkedIn Page of Cristina Junqueira.

FINANCIAL TECHNOLOGY NEWS

Conductor Hires Banks for U.S. Public Offering: Report

Brazil-based payments company Conductor is hiring banks in preparation for an initial public offering in the United States, Reuters reported July 27. The company, which has backing from venture capital firm Riverwood Capital and payments processor Visa, could happen as early as this year, the wire service reported, citing three unnamed sources with knowledge of the matter. Conductor provides technology for financial services providers, and it allows banks, retailers and financial start-ups to offer services such as payment wallets and credit cards to their clients, Reuters reported. Conductor declined to comment on its IPO plans to the wire service. The investment banking units of Goldman Sachs, JPMorgan, Bank of America and Credit Suisse, which Reuters reported will manage the offering, also declined to comment. The sources did not say how much money Conductor was seeking to raise in the offering, what its valuation would be or which U.S. exchange it would select for listing its shares. Conductor processes some 1.5 billion transactions worth about \$20 billion annually in Latin America, according to the company's website, which adds that it has 30 million active accounts. In total, it has 85 million registered accounts and has had a 46 percent compound annual growth rate since 2012, according to the company's website. Conductor describes itself as "the leading card issuing and banking-as-a-service software platform in Latin America." Conductor will mainly be offering new stock in the IPO as it seeks to raise money in order to pay for its expansion into other countries, engage in mergers and acquisitions and launch new products, one of the sources told Reuters. In June, Conductor announced that it had begun operations in Mexico, according to IBS Intelligence. "Our goal is to be a player that acts to accelerate the leadership of the financial markets ecosystem where we are present, providing

all the necessary support for them to evolve to their full potential," Anderson Olivares, the company's country manager for Mexico, said in a statement. In terms of size and potential, the Mexican market is very similar to the Brazilian market and we believe it will be very relevant for Conductor's growth." Last year, Conductor raised approximately \$170 million in two tranches from investors including Viking Global Investors, Sunley House and Singapore-based Temasek Holdings, Reuters reported. Last October, Conductor's chief executive officer, Antonio Soares, said the company is expecting rapid growth as it seeks to provide services to people who lack a bank account.

INSURANCE NEWS

A.M. Best Maintains Negative Outlook for Mexico Insurance

Insurance industry-focused ratings agency A.M. Best said July 15 that it is maintaining its negative outlook on Mexico's insurance sector. The ratings agency, based in Oldwick, N.J., said that several "aggravating factors" from the Covid-19 pandemic are affecting macro and microeconomic fundamentals in

Mexico's insurance sector contracted 2.6 percent in real terms last year, according to A.M. Best.

Mexico. "In 2020, Mexico's insurers were able to generate minimal business, reflecting the limited economic response to the pandemic on a local level, as well as the global slowdown that affected its main underlying industries," A.M. Best said in a report. "Additionally, claims were muted by restrictions in mobility of the population." The agency added that it expects premiums to recover slowly this year "amid limited expansionary policies and slow

NEWS BRIEFS

Itaú Corpbanca Shareholders Approve Capital Increase

Shareholders of Chile's Itaú Corpbanca on July 13 approved a \$1.1 billion capital increase, the bank said in a filing with regulators, Reuters reported. The capital increase is part of the bank's efforts to boost growth and also adhere to Basel III capital requirements, the lender said. Itaú Corpbanca said in a filing with financial regulators that the new funding would assure "capitalization ratios in line with the main banks in the country." CEO Gabriel Moura said the capital increase is "an important step" in the bank's evolution. Itaú Corpbanca operates in Chile, Colombia and Panama.

Deutsche Bank Unit Hires Seven Bankers in Americas

The international private bank unit of Deutsche Bank has hired seven bankers in the Americas as it seeks to bolster its business in the region, Reuters reported July 16. The new bankers at Deutsche Bank are joining from positions at Citigroup, Bank of America and Goldman Sachs Wealth Management. They will be part of Deutsche Bank's New York, San Francisco and Latin America teams, said the Germany-based lender. The international private bank unit provides advisory and wealth management services to high-net-worth individuals.

Argentine Investment Fund Becomes Major Buyer of Company Debt

Argentina's largest pension fund, which is part of the Anses state pension manager, is becoming the country's largest buyer of long-term company debt, Bloomberg News reported July 23. Anses' fund manager unit has purchased as much as 80 percent of recent dollar-linked debt by YPF, Pan American Energy and a unit of Albanesi, the news service reported, citing unnamed people with knowledge of the matter.

vaccination efforts.” Resumed claims could put pressure on companies’ net results, A.M. Best added. Mexico’s \$29.8 billion insurance sector contracted 2.6 percent in real terms last year, the agency said, adding that it shrank 2.1 percent in real terms in the first quarter of this year. Auto and surety were the most affected property and casualty segments. Overall, property and casualty, excluding automobile insurance, contracted 2.2 percent in real terms in the first quarter of 2021. A.M. Best added that the underlying industries for insurance consumption, including auto and tourism, are beginning to gain momentum in Mexico this year. However, it added that this momentum has not been reflected in the growth of premiums. Last year, the life insurance segments, including accident and health insurance, “remained afloat given a greater awareness of insurance protection due to the pandemic, with major medical expenses driving the growth of the market,” the ratings agency said. Mexico’s insurance sector faces downside risks this year, including a challenging security environment as well as the Mexican government’s “contingent liability exposure” to state-owned oil company Pemex. A.M. Best added, however, that faster-than-expected economic growth in the United States has improved the outlook for remittances, exports and foreign investment in Mexico in the coming year.

REMITTANCES NEWS

Brazil’s Nubank Begins Money Transfer Service

Brazilian digital bank Nubank on July 26 began offering a remittance service that will allow customers to send and receive money from abroad through its application, Reuters reported. Nubank is offering the service through a partnership with Remessa Online. “Offering international transfers through a partnership was the best way we found to make this facility more available to our customers as quickly as possible,” said Nubank’s co-founder, Cristina

FEATURED Q&A / Continued from page 1

stronger profitability. By contrast, a sharp hike in rates due to accelerating inflation could derail the region’s incipient economic recovery, making it tougher for borrowers to repay their loans and increasing credit costs. In an environment of higher rates amid a sustained economic recovery, credit growth is likely to shift toward consumer loans and economic sectors related to consumer goods and services. Conversely, banks are likely to reduce exposure to more debt-intensive industries such as telecoms, manufacturing, shipping and construction, particularly homebuilders, as higher rates weaken their repayment capacity. Among the region’s larger markets, commercial banks in Argentina, Mexico and Panama are likely to be more sensitive to rising interest rates due to tepid economic recoveries, which could weaken borrowers’ repayment capacity and continue to pressure credit costs.”

A **Cynthia Cohen Freue, senior director and sector lead for financial institutions ratings at S&P Global Ratings:** “We believe that Latin American banks can cope with the increasing interest rates as they did in the past. Although they would be able to transfer the rising funding costs to borrowers, this could weigh on households and corporations’ payment capacity and on banks’ asset quality. For Brazilian and Mexican banks, corporate and SME loans are set at a variable interest rate (the repricing should be fairly quick), and credit cards are

Junqueira, the wire service reported. The agreement between Nubank and Remessa Online will guarantee Nubank’s customers a discount on administrative fees. During the first eight weeks of the partnership, the administrative fee will be reduced by 15 percent, Reuters reported. Customers will be able to send money to a recipient in another country through the app via the “Transfer Internationally” function. The customer fills in the amount of the transfer in local currency and the destination country,

also set at variable rates, while consumer and payroll loans are set at a fixed rate, but the maturity is typically short term. Mexican banks provide mortgages at a fixed rate, and their Brazilian peers do so as well, but a small—but increasing—share is disbursed at a variable rate. However, the share of

“Higher interest rates could increase Latin American banks’ margins and returns on investments.”

— Cynthia Cohen Freue

mortgages of total loans in both countries is relatively manageable at about 18 percent. We believe the repricing will take some time, and there could be some temporary pressure on margins, but they should recover in the longer term. We would like to point out that we don’t expect a major pickup in interest rates in Mexico, and although we expect a steeper increase in Brazil, it should remain below high historical levels. Chilean banks, in contrast, generally benefit from higher levels of inflation, because their mortgage portfolios that are denominated in inflation-adjusted measures, Unidad de Fomento (UF), have a longer maturity than funding sources, which are bonds issued in the domestic market denominated in UF with a shorter maturity. In general, we believe that higher interest rates could increase Latin

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and the app will show the converted value. In order to receive an international transfer, Nubank customers will need to be registered with Remessa Online, which will give them an international bank account number. Through the partnership, Remessa Online is expecting its number of customers served to jump from 350,000 to one million over the next year. The company is also expecting revenue growth of 150 percent next year, the same growth that it is expecting for this year.

POLITICAL NEWS

Top Haitian Security Official Arrested in Assassination Probe

Haitian authorities on July 26 arrested a top security official for late Haitian President Jovenel Moïse in connection with the slain president's assassination, the Associated Press reported, citing the man's attorney. Jean Laguel Civil is among more than two dozen people who have been arrested in connection with Moïse's July 7 assassination. Civil's attorney, Reynold Georges, called the arrest politically motivated, the AP reported. It was unclear on July 26 whether Civil had been charged. Civil's arrest happened as more than 1,000 demonstrators rallied around gang leader Jimmy Cherizier, a former police officer who now heads the so-called "G9" federation, a group of nine gangs that police blame for a rise in kidnappings and violence this year. "Everyone needs to wait on my order before we respond to the killing of Jovenel Moïse," Cherizier, who goes by the nickname "Barbecue," told supporters. Haitian officials have vowed to pursue those responsible for Moïse's assassination. "An investigation is underway by the Haitian National Police, Department of Justice and all relevant ministries to ensure that the culprits of this heinous crime are brought to justice," Haitian Ambassador to the U.S. Bocchit Edmond told the daily Latin America Advisor in a [Q&A](#) published July 9.

Warring Factions of Mexico's Gulf Cartel Announce Truce

Three factions of Mexico's Gulf drug cartel announced July 26 that they have entered a truce, the Associated Press reported. The warring factions made the announcement via printed banners that appeared in the border city of Reynosa and other towns in Tamaulipas state, police said. "We hereby inform all the citizens of the state that today, July 19, we agree to a

ADVISOR Q&A

Would a Global Minimum Tax on Corporations Work?

Q Mexico could raise \$1.5 billion in revenue if a global minimum corporate tax rate of 15 percent comes into effect, Deputy Finance Minister Gabriel Yorio said this month without specifying a time frame. His comments came after the Organization of Economic Cooperation and Development, or OECD, announced that 130 countries had agreed on that rate for a global corporate tax. What are the most significant components of the latest agreement on a global corporate tax? Which Latin American and Caribbean countries are likely to be most affected by the suggested taxing system, and what are the proposal's benefits and drawbacks? What does the 15-percent corporate tax mean for companies investing and operating in the region?

A Grace Perez-Navarro, deputy director of the OECD's Center for Tax Policy and Administration: "Earlier this month, 132 countries and jurisdictions, representing more than 90 percent of global GDP, joined the statement establishing a new, historic framework for international tax reform. This framework will address two problems with the current international tax rules, which are more than 100 years old. First, multinational enterprises (MNEs) are only obliged to pay tax in foreign markets where they have a physical presence, which made sense in the past, when business revolved around factories, warehouses and physical goods.

truce of tranquility and we stand in solidarity with the people and with coherent principles and ideologies that generate peace," read one of the banners, according to photographs, Infobae reported. The banners were printed in red, white and green, the colors of the Mexican flag, and some included slogans such as "Long

live peace!" State authorities said four people had been arrested under suspicion of putting up the banners in buildings or overpasses in more than six cities across Tamaulipas, including Padilla, Matamoros and near the U.S. border in Río Bravo, Infobae reported. Three factions of the Gulf cartel that have been en-

EDITOR'S NOTE: More commentary on this topic appears in the July 26 issue of the Latin America Advisor.

NEWS BRIEFS

Venezuela's Maduro Says He's Ready for Talks With Opposition Next Month

Venezuelan President Nicolás Maduro said he expects to begin a dialogue with the opposition in August, expressing hopes that the United States would embrace the talks, Reuters reported July 26. The negotiations are set to begin next month in Mexico, with Norway acting as an intermediary. High-level officials from the United States, the European Union and Canada said last month that they would be willing to review sanctions against Maduro's government if there was significant progress toward free and fair elections in Venezuela.

Mexico Signs Deal With U.S. FAA in Hopes of Recovering Safety Rating

Mexico has inked a deal with the U.S. Federal Aviation Administration, or FAA, with the hopes of recovering its Category 1 air safety rating, Mexico's ministry of communications and transportation said on July 26, Reuters reported. FAA representatives are set to visit Mexico in August to provide technical assistance and an evaluation of the country's efforts to reverse a safety demotion to the lowest level in May. The downgrade bars Mexican airlines from adding new flights to the United States.

Guatemalan Anti-Graft Prosecutor Flees Country Following His Firing

Anti-corruption prosecutor Juan Francisco Sandoval fled Guatemala late on July 23, hours after Attorney General Consuelo Porras fired him and accused him of unspecified "abuses," the Associated Press reported. The former head of the Special Prosecutor's Office Against Impunity, Sandoval said he was removed because of his probing of top officials in the administration of President Alejandro Giamattei, the AP reported.

gaged in a decade-old turf war, the Metros, the Scorpions and the Reds, signed the banners. It was unclear whether a fourth faction known as the Cyclones was part of the peace agreement, the AP reported. The announcement came slightly more than a month after a 15-person massacre in Reynosa allegedly carried out by the Gulf cartel, Infobae reported.

Nicaraguan Agents Arrest Seventh Presidential Hopeful

Nicaraguan authorities on July 24 placed under house arrest opposition leader Noel Vidaurre, the seventh presidential hopeful to be detained in recent weeks, the Associated Press report-



Ortega // File Photo: Nicaraguan Government.

ed. With Vidaurre's arrest, nearly all potential candidates challenging President Daniel Ortega in the Nov. 7 elections have been detained.

Political commentator Jaime Arellano was also placed under house arrest on July 24 after criticizing a speech by Ortega. Vidaurre, one of the potential contenders of the Citizens for Liberty alliance, is accused of "undermining the sovereignty" of the country under a treason law that the Ortega-controlled National Assembly passed last December, Agence France-Presse reported. Citizens for Liberty recently announced it had picked Óscar Sovalbarro as its candidate. It was not clear if Sovalbarro had accepted the nomination. Ortega's government over the past two months has cracked down against opponents, detaining 28 opposition figures, including seven presidential contenders, journalists and opposition activists. Presidential candidates can register from July 28 to Aug. 2. The speaker of Nicaragua's assembly,

Gustavo Porras, recently confirmed that Ortega will be the candidate of the Sandinista National Liberation Front in the November vote. Ortega was first elected president in 1984 and ruled until 1990 before returning to power in 2007. He has since won two successive re-elections, AFP reported.

ECONOMIC NEWS

Brazil Coffee Crops Hit by Cold Weather, Prices Soar

Unusually cold weather has damaged crops in Brazil's main coffee-growing regions, shaking up prices for this year's crop, Reuters reported July 22. Coffee nurseries were also hit by the freezing temperatures, which could complicate replanting plans and potentially harm prospects for next year's harvest. Coffee futures soared 10 percent on July 22, with prices posting their largest single-session gain since early 2014, sending coffee prices to their highest point in more than six years, MarketWatch reported. Brazil's worst drought in nearly a century had already cut Brazilian coffee production before the cold snap. Coffee exports have also been coping with high shipping rates and

“The market's worst fears have been realized this year.”

— Sal Gilbertie

supply chain bottlenecks this year, according to Bloomberg News. “The market's worst fears have been realized this year,” Sal Gilbertie, president and chief investment officer at Teucrium Trading, told MarketWatch. Brazil accounts for a third of the world's coffee production, according to industry trade association CNA. The sector sustains 265,000 coffee producers, the majority of whom are smallholders. The freeze could also cut into production of other important crops in Brazil.

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American banks' margins and returns on investments. However, they could experience a sharper deterioration of asset quality due to a higher burden from inflation and higher credit costs to individual and commercial borrowers, which in turn could prompt banks to raise provisions, leading to profitability pressures."

A **Maria Paula Costa Bertran Muñoz, associate professor of law and society at the University of São Paulo:** "Higher interest rates create incentives for banks to decrease their exposure to household loans. It is safer, easier and more profitable to redirect capital to public bonds, instead of feeding the local credit markets. So, the first thing to consider is that there will be less money available for household loans. It reflects better credit selection and the avoidance of credit without collateral. Housing is likely to be the most affected market. Since the 2008 crisis in the United States, the literature describes how the housing prices vary according to the interest rates. Professors Atif Mian and Amir Sufi (authors of the book *House of Debt*) state that the lower the interest rates, the higher the prices of homes. In their analysis, the price of the homes is inflated by the

availability of resources to buy them, creating a market-specific inflation that tends to be higher than inflation in general. Brazil has seen real estate prices skyrocket during the pandemic and the months in which the country has had low interest rates. The rise of

“Higher interest rates create incentives for banks to decrease their exposure to household loans.”

– Maria Paula Costa Bertran

interest rates may represent a good outcome for households, as Latin American countries can avoid the deepening of a new housing bubble and count on a more predictable market. In addition to that, households are likely to avoid spending irrationally, limiting the economic crisis that always follows the increase of household debt, according to what Mian and Sufi consider as robust as an empirical evidence."

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

FINANCIAL SERVICES ADVISOR

is published biweekly by the
Inter-American Dialogue ISSN 2163-7962

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

www.thedialogue.org

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Advisor Video

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