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## FEATURED Q&A

# Will Bitcoin Be a Boom or Bust for El Salvador's Economy?



Salvadoran President Nayib Bukele has embraced Bitcoin, a move that the International Monetary Fund has said could bring "significant risks." // File Photo: Salvadoran Government.

**Q** The International Monetary Fund has been openly critical of Salvadoran President Nayib Bukele's decision to adopt Bitcoin as legal tender in the Central American country, and negotiations for a \$1.3 billion aid package from the institution remain stalled. The negotiations were initially halted following Bukele's dismissal of the Constitutional Chamber and attorney general, a move that human rights groups and rattled investors called a "technical coup." Is Bukele gambling with El Salvador's economic health by not complying with the IMF's conditions? What is the outlook for the IMF's talks with El Salvador? How likely is it that Bukele's administration can pay down the national debt using Bitcoin, and is Bitcoin a viable tool to sustain and grow a country's economy in the long term?

**A** Douglas Farah, president of IBI Consultants and senior visiting fellow at the National Defense University's Center for Strategic Research: "The primary issue with Bitcoin in El Salvador is not the cryptocurrency per se, but rather the opaqueness surrounding the purchase of the currency, how it is spent and what the actual purpose is. The move to Bitcoin as a currency is deeply unpopular, and the dislike is compounded by the significant fraud and technical glitches in the state-run Bitcoin delivery system for most transactions, known as the Chivo Wallet. The privately owned wallet run by loyalists of El Salvador's president, Nayib Bukele, effectively ties crypto transactions to government control—the antithesis of the Bitcoin ethos. In addition, four senior Bukele officials have also been labeled by the U.S. State Department as corrupt actors. One of them, Carolina Recinos, is

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## TODAY'S NEWS

### ECONOMIC

## Mexico Seeks Panel to Resolve Dispute Over Auto Rules

The Mexican government has requested a panel under the U.S.-Mexico-Canada Agreement in an effort to resolve a dispute with the United States over auto industry rules of origin.

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## Brazil's XP to Buy Up to 100% of Banco Modal

XP's agreement to buy as much as 100 percent of Banco Modal values it at \$528.5 million.

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### POLITICAL

## U.S. Imposes Visa Restrictions on Cuban Officials

The United States imposed visa restrictions on eight unnamed Cuban officials in response to Cuba's imprisonment of protesters who participated in demonstrations last July. Cuban Foreign Minister Bruno Rodríguez blasted the move.

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Rodríguez // File Photo: Cuban Government.

## POLITICAL NEWS

## U.S. Imposes Visa Restrictions on Eight Cuban Officials

The U.S. State Department on Thursday imposed visa restrictions on eight Cuban officials in connection with Cuba's detention and imprisonment of protesters who took to the streets in massive demonstrations last July. "These eight individuals include Cuban officials connected to the detention, sentencing and imprisonment of peaceful July 11 protesters," the State Department said in a statement, which did not name the Cuban officials targeted in the action. "The United States took steps to enforce visa restrictions in response to Cuban government attempts to deny Cubans their freedom and rights through continued intimidation tactics, unjust imprisonment and severe sentences," it added. Some 600 protesters remain jailed in Cuba following the protests, "some with worsening health conditions and no access to proper food, medicine or calls to their loved ones," the State Department said. In a tweet, Cuban Foreign Minister Bruno Rodríguez criticized the action. "The U.S. government persists in the bad habit of trying to impose its will on other governments by means of unilateral coercive measures. The announcement made today by the Secretary of State in no way alters #Cuba's determination to defend its sovereign rights," said Rodríguez. The new visa restrictions add to sanctions that the State Department slapped on nine Cuban officials on Nov. 30 following the Cuban government's move to quash protests that had been planned for Nov. 15. The protests last July were believed to be the largest in Cuba since 1994. "Everett Briggs, a former U.S. ambassador and National Security Council advisor told the Advisor in a Q&A published July 20 that technology played a big role in the protests. "The regime has tried to silence Internet and cell phone links, but in the modern world of electronic wizardry, and perhaps with an assist from abroad, Cubans will find ways to stay in touch and informed. And maybe, to act," he said.

## ECONOMIC NEWS

## Mexico Seeks Panel to Resolve Dispute Over Auto Rules

The Mexican government has requested a panel under the U.S.-Mexico-Canada Agreement, or the USMCA, in an effort to resolve a dispute about the interpretation of auto industry rules of origin with the United States, The Wall Street Journal reported, citing Mexico's Economy Ministry. Mexico claims that the United States is incorrectly interpreting stricter regional content rules under the USMCA, which replaced the previous NAFTA agreement in 2020, the

**Mexico considers that a panel's decision would provide certainty to the automotive industry in benefit of competitiveness in the region."**

— Mexican Economy Ministry

Associated Press reported. "Mexico considers that a panel's decision would provide certainty to the automotive industry in benefit of competitiveness in the region," the Economy Ministry said, The Wall Street Journal reported. While Mexican President Andrés Manuel López Obrador requested formal consultations with the United States under the USMCA and auto content rules in 2021, the countries were unable to resolve differences between the neighboring countries. In a Q&A published in the Advisor on Sept. 7, Kellie Meiman Hock, managing partner at McLarty Associates, said the countries should be "laser-focused on clear and predictable implementation" of the trade accord. "While the disconnect over the formula to calculate auto rules of origin at play in this dispute is one factor, we cannot forget that we are into year two of this agreement and still do not have the uniform regulations," said Meiman Hock. "This undercuts the main benefit of a

## NEWS BRIEFS

## Mexico to Require Visas of Venezuelan Migrants

Mexico will be requiring visas from Venezuelans seeking to enter the country beginning Jan. 21, the country's Interior Department said in new migratory rules published on Thursday, the Associated Press reported. The department cited a recent tenfold increase in Venezuelans arriving in the country who are trying to proceed to the United States "in an irregular manner," the AP reported.

## Peru's Central Bank Hikes Interest Rates for Sixth Consecutive Month

Peru's central bank on Thursday increased its benchmark interest rate for the sixth consecutive month amid escalating inflation and the country's economic rebound, Bloomberg News reported. Policymakers hiked the key rate a half percentage point, to 3 percent. The move was in line with the expectations of five of seven economists in a Bloomberg survey. Two of the economists expected a hike of 75 basis points. Peru's annual rate of inflation accelerated to 6.4 percent, a 13-year high, in December. The country's economy likely grew 12.6 percent last year, according to analysts in a Bloomberg survey.

## Brazil Extends Coal Use, Subsidies Under 'Just Energy Transition' Law

Brazil has extended its coal use and subsidies until 2040 under a so-called "just energy transition" law that was published on Thursday, Reuters reported. The "just transition" process has the objective of ensuring the widespread benefits of a green economy shift. However, policy experts argue that the law goes against the climate and consumers, as it benefits coal producers by extending the lives and activities of coal-based power plants in Santa Catarina state for 18 years, Reuters reported.

free trade agreement—certainty for investors and workers,” she added.

## BUSINESS NEWS

# Brazilian Brokerage XP to Buy as Much as 100% of Banco Modal

Brazilian brokerage XP announced today that it has signed a binding agreement to buy as much as 100 percent of investment platform Banco Modal. In a statement, XP said it will pay for the transaction with up to 19.5 million newly issued XP Class A shares or Brazilian Depository Receipts. The deal implies a 35 percent premium over the average price of Banco Modal's shares. The deal values Banco Modal at \$528.5 million, Reuters reported. As a result of the transaction, the companies together will have 3.8 million clients and a net revenue of 11.8 billion reais (\$2.07 billion), XP said in its statement. “Given the immaterial overlap between XP and Modal's clients, we expect that interesting revenue synergies and client experience enhancements will be captured,” XP's chief financial officer, Bruno Constantino, said in the statement. “Furthermore, with increased scale and pricing power, we will strengthen our purpose of better serving our clients with great products at lower prices, as we recently did with online brokerage fees,” he added. XP's chief executive officer, Thiago Maffra said the tie-up would help the combined company compete against Brazil's traditional banks. “Brazil has one of the most concentrated financial sectors globally, and together we'll be able to be even more competitive against the traditional banks,” said Maffra. “Our priority is to constantly improve the value proposition for Brazilian consumers,” he added. Following the transaction, Banco Modal will remain “independent and segregated,” XP said, adding that “current partners and executives will be aligned to our long-term objectives and continue to manage Banco Modal as an open and independent financial ecosystem.”

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part of Chivo Wallet's corporate leadership. This means any U.S. platform supporting Chivo Wallet is at risk of being sanctioned, making corruption and transparency core issues for Bitcoin. Because of the overall lack of transparency in the Bukele administration's public finances, concerns about corruption and the massive debt accrued with little public discussion or debate, it is unlikely the IMF will approve a loan. The Bukele administration is out of money, its Bitcoin investments have lost value and yet it has done nothing to meet the transparency and rule of law conditions that would make a loan tenable. In addition, Bukele has publicly and repeatedly attacked the United States, souring relations. Until Bukele takes steps to reverse these trends, there's no foreign aid money on the horizon, and his Bitcoin investments are unlikely to provide any solutions.”

**A Julia Yansura, program manager for Latin America at Global Financial Integrity:** “President Bukele was elected promising big changes, and he has delivered on this promise while garnering popular support in El Salvador. That said, international observers—and lenders—are right to be concerned about the country's trajectory. Adopting Bitcoin as legal tender presents some benefits but also serious risks for the economy, and it's not clear that these risks are being adequately managed—or even so much as discussed. Some issues, such as volatility, have to do with Bitcoin itself. Others, such as the lack of transparency surrounding the Chivo Wallet, have to do with the way it was implemented in El Salvador. Moreover, the hasty rollout raises questions regarding consumer financial protection, as well as sufficient AML/CFT controls to combat illicit financial flows. To be clear, the existing financial architecture in El Salvador has had problems with financial stability and integrity as well. These challenges are not unique to Bitcoin. However, the adoption of Bitcoin as legal tender raises these longstanding

challenges for a new asset class, presenting risks that must be understood, assessed and mitigated with great care. This is especially true for AML/CFT policy. My greatest concern for El Salvador's Bitcoin adoption is the lack of an open conversation regarding AML risks against a political backdrop where any criticism or concern is treated as heresy. In this context, the stalemate with the IMF is only the tip of the iceberg for underlying economic risks. The Bukele administration would do well to take action, not only for the IMF, but to ensure the financial integrity of the country's economy.”

**A Ricardo Valencia, assistant professor of communications at California State University, Fullerton:** “El Salvador's president has a penchant for short-term popularity gains over the ability to tackle mid-term and long-term economic challenges. The Salvadoran economy is precarious, with no alternative to aid from the IMF. The adoption of Bitcoin has not brought in substantial revenues. The government-run Chivo Wallet has become a financial black hole—funded by public money but without public oversight. Salvadorans in the country and abroad have reported losses of tens of thousands of dollars in fraudulent or suspicious transactions. The Chivo Wallet has become the epicenter of dozens of scams in which fraudsters have used the National Registry database to defraud legit users. On top of that, the government has stopped honoring its commitments on things like a public transportation subsidy, bonus pay for health care workers and state university funding. Bukele has sought new resources through the issue of government securities to fund public infrastructure. These new sources of fresh money are jeopardized due to the fact that El Salvador is one of the three riskiest countries in Latin America in terms of international debt repayment. The adoption of Bitcoin looks like a Hail Mary to alleviate Bukele's diplomatic isolation, and it might

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not be enough to be a viable tool to sustain the Salvadoran economy. The most likely scenario is that first, Bukele's government will stop paying local debt, and if the situation continues to deteriorate, he might find it impossible to pay down international loans. Bukele is on a downward spiral that will lead to increased repression of the press, opposition politicians and dissidents, and may very well end in economic calamity."

**Álvaro Trigueros, director of the Economic Studies department at the Salvadoran Foundation for Economic and Social Development (FUSADES):** "El Salvador's main macroeconomic challenge is the tension between a high level of debt and limited access to financing in international markets. Public debt in 2021 reached 86.4 percent of GDP, while the JPMorgan Emerging Market Bond was 14.89 at the end of 2021—the third worst year for Latin America on that bond index. Even if El Salvador's government does a full rollover of \$2.6 million of short-term domestic debt, it faces a 2022 financing gap of \$1.4 billion, plus a bond for \$800 million that expires this month. Finding funding in the traditional market without an IMF agreement is almost impossible. Nayib Bukele's administration is unlikely to reach a financing deal with the IMF, since the strengthening of democratic institutions, civil liberties and the fight against corruption are not a priority for his government. To avoid these conditions, the government seeks to open a non-traditional source of financing, issuing a \$1 billion Bitcoin bond in early 2022 on an unregulated digital asset exchange platform. The result is highly unpredictable, and its destiny is not to close the tax gap, but to buy Bitcoin and finance Bukele's Bitcoin city project, which is not in the 2022 budget. Thus, the government of El Salvador does not yet have a credible route to stop, and course correct, on the public debt."

**A Tim Jacklich, senior cryptocurrency analyst at Americas Market Intelligence:** "By the end of September 2021, 2.2 million Salvadorans had reportedly downloaded the country's Bitcoin-enabled Chivo Wallet. If accurate, this rate of uptake is quite impressive, potentially rivaling the penetration of mainstream bank accounts—only 30 percent of Salvadoran adults had one in 2017. However, Chivo's long-term importance to Salvadoran commercial development remains very much in question. Rather than enthusiasm for Bitcoin, most Salvadorans likely downloaded the Chivo Wallet to access the government's offer of \$30 in Bitcoin as an incentive for opening an account. Some immediately withdrew their \$30 from the Chivo ATMs around the country. For Salvadorans who remain in the Chivo ecosystem, the wallet can indeed provide some powerful benefits, namely access to a digital wallet account (with a balance in U.S. dollars) and the ability to make mobile app-based, real-time transfers. However, it is difficult to distinguish these benefits from those of a non-crypto digital wallet. Though Chivo is capable of transferring on the Bitcoin network, transfers between Chivo users are 'between-us' crypto transactions, meaning that they are settled to Chivo's internal ledger (and not a Blockchain), much like a transfer between PayPal users. Further, though Salvadoran merchants are legally required to accept Bitcoin payments, the price volatility of Bitcoin makes it infeasible to list prices in Bitcoin, meaning that the U.S. dollar remains the dominant unit of account. Any long-term benefits from Bukele's Chivo experiment may ultimately derive not from Bitcoin but rather from the launch of a widely accessible digital U.S. dollar wallet in an underbanked country."

*The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at [gkuleta@thedialogue.org](mailto:gkuleta@thedialogue.org).*

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