INTER-AMERICAN DIALOGUE'S
LATIN AMERICA ADVISOR ▸ FINANCIAL SERVICES

FEATURED Q&A

Are Past-Due Loans Putting Colombian Banks on Shaky Ground?

Q Colombia's government will force some of the country's banks to boost their provisions for bad debt because of concerns about an increasing amount of past-due loans, Finance Minister Juan Carlos Echeverry said May 18, MarketWatch reported. The number of past-due loans has grown 26 percent so far this year, said Echeverry. What is causing the increase? Is Colombia's financial services industry on firm ground? Is the government imposing adequate regulations and safeguards on the industry, or is it unnecessarily holding banks back?

A Marcela Blanco, associate attorney at Diaz, Reus & Targ LLP in Bogotá: "It should come as no surprise that banks are now seeing higher rates of delinquency among their loan portfolios. The ratio of consumer-to-corporate loans is now higher than in prior years. The product of aggressive credit expansion programs at the consumer and retail level, the increase in buying power of ordinary citizens is resulting in a higher rate of default among ordinary consumers. Last year, consumer loans increased by 25 percent, mortgage loans by 18 percent and banks issued more than one million new credit cards. Car sales reached record highs by offering low monthly payments. Sales staff at department stores pursued shoppers with discounts if only they would use store credit cards. And banks cold-called clients offering preapproved loans. During the last several months, Colombia's growing middle class has taken on too much bank debt to buy new cars, real estate and home appliances. This is not to say, however, that Colombia is in the midst of a consumer credit free-for-all. The reserve requirement imposed by Colombian authorities for consumer lending is meant to restrict liquidity and control inflation without raising interest rates. This measure will not restrict banks' ability to lend. Rather, it will

Continued on page 3

Bancolombia Eyes Possible Acquisitions in Latin America

Bancolombia, Colombia's largest lender, is looking for acquisitions in Latin America and may tap capital markets if it needs financing, CEO Carlos Raúl Yepes said May 29. He added that the bank is open to acquisitions across the region. See story on page 2.

File Photo: Colombian Government.

Inside This Issue

FINANCIAL SERVICES BRIEFS

Chilean Banking Sector Sees 14.53 Percent Drop in Profits

The profits of Chile's banking sector fell 14.53 percent in the first four months of 2012 compared to the same period a year prior, Reuters reported May 31. Profits in April fell 20.88 percent in comparison to March as a result of higher credit risk provisions, said the report, which cited the banking regulator. Profits for the January-April period totaled $1.14 billion.

Western Union Launches New Remittance Card in El Salvador

Money transfer giant **Western Union** and **AirPak**, its agent in Central America, announced June 4 that they are launching a new remittance card in El Salvador. Receivers of money transfers will be able to place all or part of the remittance onto the new **MasterCard**-branded card and then use it wherever MasterCard is accepted, including for shopping online and at ATMs, said Western Union. Only 47 percent of adults in El Salvador have bank accounts, according to a 2010 Word Bank report. The Central American country received $3.6 billion in remittances in 2010, according to the World Bank.

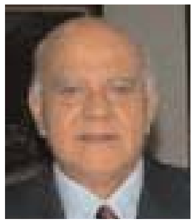
Haiti Launches Mobile Phone Cash Transfer Program

Haiti launched a conditional cash transfer program on Sunday that provides as much as $20 a month to mothers who keep their children in school, the Associated Press reported. Venezuela's "Ti Manman Cheri," which translates to "Dear Little Mother" in Creole is targeting 100,000 families in the poorest areas of Port-au-Prince. Venezuela's Petrocaribe provided the initial $15 million for the program, which transfers funds via mobile phones.

Financial Services News

Brazil's Government Seizes Banco Cruzeiro do Sul

Brazil on June 4 seized medium-sized bank **Banco Cruzeiro do Sul**, saying the bank had violated unspecified regulations, Dow Jones reported. Authorities also found inconsistencies in the bank's assets, according to the central bank. Cruzeiro do Sul, which has 12 billion reais ($5.88 billion) in assets was placed under the control of Brazil's state banking insurance deposit fund for 180 days, according to the central bank. The Credit Guarantee Fund, known as FGC, announced that some of the bank's senior managers and board members would be removed from their positions. The bank will continue operating normally, the FGC added. Cruzeiro do Sul had sought to leave the FGC on May 31, saying it had a 1.3-billion real capital shortfall, according to Antonio Carlos Bueno, the executive director of the FGC. Cruzeiro do Sul will undergo an audit over the next 90 days, Bueno told reporters on Monday. "In truth, we don't yet know the exact size of the problem," said Bueno, adding that the audit might lead to a sale of the bank. Investment bank **BTG Pactual** had been discussing a possible purchase of the bank, but the talks broke down over uncertainty about Cruzeiro do Sul's problems, Bueno added. A Cruzeiro do Sul spokesman referred questions from Dow Jones to the FGC.



Bueno
Photo: Brazilian Government.

Bancolombia Eyeing Acquisitions in Latin America: CEO

Bancolombia is looking for acquisitions in Latin America and may seek to tap capital markets if it identifies potential targets and needs financing, the bank's chief executive officer told Reuters on May 29. "Our strategy is not to wait and see what's being sold, it's to go and look for what we want," Carlos Raúl Yepes told the wire service. "We would wait to buy when acquisitions are at the right price." Bancolombia, Colombia's largest lender, is interested in acquiring brokerages, fiduciary funds and banks and is open to possible acquisitions across the region, said Yepes. He added that the bank is not poised at this moment to make any deals. In the first quarter, Bancolombia sold nearly $1 billion in shares and had a record level of bond sales last year. Those moves allow the bank to pursue acquisitions without the need for more financing. However, Yepes said Bancolombia maintains tapping the public markets as an option. On May 28, Bancolombia's board approved the issuance of as much as 3 billion pesos ($1.63 billion) in local bonds. It did not specify how the money raised would be used. "We want to take advantage of the liquidity in the market," Yepes told Reuters. José Fernando Restrepo, head of economic investigations at the Interbolsa brokerage, told the wire service that acquiring assets outside of Colombia could be a good move for Bancolombia. "Buying overseas banks would give it bigger income diversification," he said. "Acquisitions are always on the radar for companies like Bancolombia." After losing its investment-grade rating more than a decade ago, Colombia regained it last year on the heels of its steady financial management, strong economy and advances in security. Colombian banks have received a flood of new middle-class customers who have sought more loans. However, the country's central bank has expressed concerns about growing consumer debt levels. The

"Our strategy is not to wait and see what's being sold, it's to go and look for what we want."

— *Carlos Raúl Yepes*

central bank at its May 28 meeting left its benchmark interest rate unchanged at 5.25 percent for the third consecutive month.

Banco de Guayaquil Considering Acquisitions in Andean Region

Ecuador's second-largest publicly traded bank, **Banco de Guayaquil**, is looking for acquisitions after the sale of its insurance operation swelled the cash it has on hand, Bloomberg News reported Thursday. Switzerland's **Ace Ltd.** bought the insurance unit for $55 million when Banco de Guayaquil was forced to sell it due to changes in government regulations. "We'd like to buy something, but we haven't found any sellers," the bank's vice president of finance, Miguel Macias, told Bloomberg News in an interview. "Last year we opened the doors to look in international markets." The bank is looking for acquisitions in Ecuador, Colombia or Peru, Macias added.

Banks Will Take Over 19% of YPF After Petersen Defaults on Loan

Six banks, led by **Credit Suisse**, will take over 19 percent of Argentina's **YPF** after the **Petersen Group** defaulted on a loan that used the stake in the oil company as collateral, Bloomberg News reported June 1. Petersen, which Argentina's Eskenazi family owns, defaulted on the $1 billion loan after it had been using dividends from YPF to meet its loan obligations. However, the government last year opposed the company's dividend payments and seized control of YPF in April from Spain's **Repsol**.

Peru Unveils Pension Reform Plan in Effort to Lower Fees

Peru's government on May 30 announced a plan to reform the country's private pension fund system in an effort to boost competition and lower the fees that pension funds charge, Dow Jones reported. Four pension funds currently make up the system, which is a significant player in Peru's financial markets. The government aims to ensure that workers for small companies can access the funds, said

Featured Q&A

Continued from page 1

only apply to those financial institutions showing higher levels of delinquencies in consumer loans. Moreover, the Colombian financial system is sound and stable overall. The rise in consumer lending, although noticeable, is nevertheless moderate. More importantly, measures have been put in place just in time to prevent a future repayment crisis."

A Felipe Carvallo Mendoza, assistant vice president and analyst at the Financial Institutions Group of Moody's de México: "We continue to see conservative lending practices among Colombian banks, especially related to the composition of loan portfolios (63 percent of which are commercial loans), past-due loan levels at 1.67 percent and ample reserve coverage (2.8 times past due loans), as of the end of March. There indeed has been deterioration in asset quality, but to very manageable levels and it has been equivalently spread among the different products. Past-due loans increased to about 4 trillion pesos as of year-end 2012, up from the 3.7 trillion pesos we had seen through most of the first half of 2011. Growth in past-due loans (7 percent for the 12-month period that ended in March) has been accompanied by strong 20 percent growth in gross loans overall for the same period. We are comfortable with this because these increases occur in an operating environment supportive of healthy loan growth, including strong GDP, low inflation and record low unemployment. We still do not have precise measurements on how the new reserves will work, but one of the main features of the Colombian banking system is the ample reserve coverage they maintain. Our understanding is that the new reserves will be based on deterioration in asset quality, not on a blanket rule, and as such it is more likely to affect entities that have seen strong deterioration relative to their portfolios. That said, we are still waiting for March data on write offs, which could shed some light on another way of analyzing asset quality."

A Enrique Gómez-Pinzón, partner at Holland & Knight in Washington: "The 26 percent increase in past-due loans might have originated in the manner in which some banks have recently been granting consumer loans. Banks had excess liquidity and the textbook example of what should be avoided happened: banks were granting consumer loans to individuals that did not really qualify to fulfill their financial obligations and were not accustomed to receiving and using consumer loans. Therefore, borrowers started to default. In spite of this, I believe the Colombian financial services industry is on firm ground, growing steadily and still really attractive for foreign investors. It is important to remember that the Colombian financial system had profits of more than $5.5 billion as recently reported. The government is trying to stir the financial system to avoid unnecessary exposure by forcing banks to increase their loan-loss reserves where appropriate. Conservative and strong regulations are precisely one of the factors that make the Colombian financial system attractive for foreign investment. Just ask the Chileans, the Peruvians, the Ecuadoreans, the British, the Spanish, the Americans and now the Brazilians."

"I believe the Colombian financial services industry is on firm ground, growing steadily and still really attractive for foreign investors."

— Enrique Gómez-Pinzón

Continued on page 6

Finance Minister Luis Miguel Castilla. "We think that we can reduce commissions by 30 percent to 40 percent by reducing barriers to entry and with improved efficiencies," Castilla told reporters. "We can increase coverage to 50 percent from 36 percent of the economically active population." Approval of any pension reforms would be up to Peru's Congress, which already is studying more than a dozen plans to modify the system. Most workers in Peru's formal labor sector are required to contribute to the funds, leading some advocates of reform to argue that they should be able to select between the private system, a government-run system or mutual funds.

Castilla

File Photo: Peruvian Government.

Political News

Leftist Leaders Demand OAS Reforms as Annual Meeting Ends

At the closing of the Organization of American States' annual General Assembly meeting in Bolivia on June 5, leftist Latin American leaders demanded that the organization take on reforms or risk becoming irrelevant, *The Miami Herald* reported. At the center of the criticism were the OAS' Inter-American Human Rights Commission and Inter-American Human Rights Court. Bolivia, Ecuador, Nicaragua and Venezuela have criticized the human rights arms of the OAS, saying they and the OAS itself are under the influence of the United States. The reforms discussed at the meeting would strip the commission and court of some of their independence and would also allow governments to delay the commission's country reports, softening their impact. In an interview with Venezuelan television station Telesur, Ecuadorean President Rafael Correa, the only head of state besides the meeting's host, Bolivian President Evo Morales, to attend the meeting said OAS reforms are urgently needed. "There's no more time to lose," said Correa. "If it's necessary to abandon the OAS and create our own system, then we have to do it." Human rights organizations have expressed alarm about the proposed reforms of the OAS' human rights bodies. José Miguel Vivanco, director of Human Rights Watch, said the commission has helped protect freedom of speech and other rights. "Well, if this organization has been so successful, why then has a campaign against it been launched?" Vivanco wrote in a letter before the meeting. "Very simple: Because it has touched the interests of important governments that possess clear autocratic tendencies or are sufficiently powerful as to believe that they are entitled to not render accounts to a supervisory regional body." In addition to the OAS' staunchest opponents, influential countries in the region have also criticized the commission. For one, Brazil has criticized the commission's opposition to the Belo Monte dam project. The United States is among the main support-

> "If it's necessary to abandon the OAS and create our own system, then we have to do it."
>
> *— Rafael Correa*

Advisor Q&A

Will Brazil Return to Boom-and-Bust Economic Cycles?

Q: Brazilian President Dilma Rousseff on May 21 unveiled a new stimulus package, including tax cuts worth about $1 billion to spur the auto sector and other industry in the country. After growing 7.5 percent in 2010, Latin America's largest economy grew only 2.7 last year and it is unlikely to meet its earlier 4.5 percent growth projection for this year. Is Brazil experiencing a minor bump in its road to sustained economic progress, or will it return to the boom-and-bust cycles of the past? Will the government's stimulus efforts yield positive results?

A: Carlos Eduardo Lins da Silva, director of Educare in São Paulo: "Brazil dealt extremely well with the 2008 financial crisis and was one of the few countries that suffered relatively small consequences from that first wave of the turmoil. The measures taken then were mostly aimed at increasing domestic consumption through tax cuts on the sale of some specific products, including automobiles and domestic appliances, and the decline of interest rates. However, the global crisis has been proving itself more resilient than initially thought. Problems in Europe, the United States and—most importantly for Brazil—China linger and hurt the Brazilian economy in several aspects. President Rousseff's initial reaction to these new challenges followed the same recipes used by her predecessor. Once more, she has tried to spur the sales of some industrial goods (again, including vehicles) and pushing banks and financing institutions to lower interest rates and make credit easier for consumers. Some analysts believe this formula has exhausted its efficacy and will not be enough to produce impressive results. What is necessary now is a significant increase in investments, which neither the government nor the private sector seems able to deliver in the short or medium range. The country still suffers due to its chronic infrastructure deficits and does not show strong signals of being able to solve them in the next couple of years. The expectation for GDP growth in 2012 is now around 2.5 percent or even less, indicating that Brazil may have returned to its traditional 'chicken flight' model after its extraordinary performance in 2010."

Editor's note: More commentary on this topic appears in the June 4 issue of the Dialogue's daily Advisor.

ers of maintaining the status quo. Its ambassador to the OAS, Carmen Lomellin, expressed support for maintaining the commission's independence and continuing its work on the hemisphere's pressing problems. "In recent months, our discussions have sometimes seemed as if we are seeking to weaken the fabric that binds us together in the inter-American system, rather than focusing on how the countries of the Americas can work together to address the issues that most concern our citizens," said Lomellin. Despite some countries' talk about abandoning the OAS, as the meeting closed June 5, most delegates were discussing ways to reform the body. They also selected Guatemala as the site of next year's annual meeting. Bolivia, Ecuador, Nicaragua and Venezuela also announced they were withdrawing from a regional defense treaty that considers an attack against one to be an attack against all the signatories. The Inter-American Treaty of Reciprocal Assistance was originally spearheaded by the United States and is no longer relevant, said Ecuadorean Foreign Minister Ricardo Patiño. The assembly also approved The Social Charter of the Americas, which states governments should "promote inclusion and to prevent, combat, and eliminate all forms of intolerance and discrimination, especially gender, ethnic, and race discrimination in order to safeguard equal rights and opportunities and strengthen democratic values." Most of the countries attending the meeting also voiced support for Argentina's claim to the Falkland Islands.

Lomellin

File Photo: U.S. State Department.

Brazil's Lula Willing to Run Again for President in 2014

Former Brazilian President Luiz Inácio Lula da Silva said May 31 in a television interview that he would be willing to run again for president in 2014 in order to prevent the Brazilian Social Democracy Party, or PSDB, from returning to power, Reuters reported. "The only situation under which I'd be a candidate again is if [current President Dilma Rousseff] doesn't want the job," Lula said on the television program "O Ratinho," or "The Rat," on Brazil's SBT network. "I will not permit a member of the PSDB to become president of Brazil again." Lula served two terms as president, from 2003-2011. The country's Constitution allows former presidents to run again if they sit out at least one presidential term. Lula, like Rousseff, is a member of Brazil's Workers Party, or PT. Before his election in 2002, Lula was defeated twice by Fernando Henrique Cardoso, a member of the PSDB.

Economic News

Morales Discusses Nationalizing All Natural Resource Industries

Bolivian President Evo Morales indicated on June 3 that his government may seek to nationalize all of the country's natural-resource industries, Agence France-Presse reported. "Another policy ought to be how we recover, or nationalize, all natural resources, so they are in the people's hands under state administration," Morales said in a speech. "Utilities …never should be private businesses." Since his government seized the telecommunications industry, coverage was extended to rural areas that never had telephone service, Morales said. Last month, Morales nationalized Bolivia's electrical grid, which had been controlled by Spain's **Red Eléctrica**. Bolivia is also believed to hold more than half of the world's reserves of lithium, most of which are in the Uyuni salt flats. The soft metal is used to make batteries for laptop computers and electric cars. France, Japan and South Korea have expressed interest in helping to develop Bolivia's minerals, but Morales' government turned them away in 2010.

> "Utilities …never should be private businesses."
>
> *— Evo Morales*

POLITICAL & ECONOMIC BRIEFS

Chile, Mexico, Colombia and Peru to Sign Pacific Trade Alliance

Chilean President Sebastián Piñera is hosting a meeting June 6 in Paranal to sign an agreement with his counterparts from Mexico, Peru and Colombia to ratify the regional Pacific Alliance trade bloc, Bloomberg News reported. The alliance will eliminate barriers not included in current bilateral trade agreements. Costa Rica and Panama will attend the meeting as observers and may join the bloc eventually. The countries' decision to sign the accord contrasts with recent moves by countries including Argentina and Brazil to raise import restrictions.

Climate Change Could Cost Region $100 Bn Per Year by 2050: IDB

Latin America and the Caribbean could face damages of $100 billion per year by 2050 if average temperatures rise two degrees centigrade from pre-industrial levels, according to a report released June 5 by the Inter-American Development Bank, Reuters reported. However, the report also estimated that only around 0.2 percent of the region's GDP would be necessary to adapt to climate change.

E.U. Trade Ministers Provisionally Approve FTA With Colombia, Peru

European Union trade ministers on May 31 gave provisional approval to a free-trade agreement with Colombia and Peru, Peru's state news agency Andina reported. The accord still must be approved by the European Parliament to take full effect. The trade agreement, which officials initialed in March 2011, aims to open trade through methods including elimination of tariffs and taking down technical trade barriers.

Featured Q&A

Continued from page 3

A **Beatrice Rangel, director of AMLA Consulting LLC in Miami Beach:** "I believe this to be a wise move. 2012 will prove to be yet another trying year for the world economy as a whole and for emerging markets in particular. Indeed, the potential for a European blowout is high as the euro seems to be unsustainable in the long run unless there is economic policy unity in the euro zone. While Colombia's largest trading partner by far is the United States, its trade with the euro zone remains significant and it is bound to suffer important decreases. Add to this the weight of Spanish banks in Colombia's economy and the recent reduction in the speed of GDP growth to clearly see that these measures are well thought out in terms of preparing the country for what will most likely be an externally induced growth reduction. Under such a scenario, it is always better to meet external shocks with significant reserves than to wade turbulent waters with debt burdens. Recent growth expectations in Colombia had boosted aggregate demand and consumer credit. But as the euro zone crisis engulfs Spain and other trading partners, Colombia's growth is slowing. As a result, past-due loans have become more heavily weighted in banks' portfolios. This calls for action on the part of economic authorities who need to curtail credit and abort inflationary pressures that could result from excess money in the hands of consumers. I believe the decision is in line with Colombia's longstanding record of macroeconomic responsibility."

A **Jorge Lara Urbaneja, international business consultant based in Bogotá:** "Banks in Colombia have had steady growth, reflecting the positive behavior of the country's economy during the last 10 years. For the first time, Colombian financial groups have gone abroad and acquired banking and insurance operations in other Latin American countries. Thus, the increased amount of past-due loans should not be viewed as a systemic problem that should require regulatory measures or new policies. In order to prevent a banking crisis and strengthen the financial sector, in 1998 the government adopted several measures. One of them was the imposition of the 0.2 percent tax on financial transactions, which is today at 0.4 percent and redirected as ordinary tax income. In addition, the government imposed new banking regulations, following Basel standards as then practicable. Therefore, the increase of past-due loans at certain banks is probably the result of aggressive credit promotions. This seems to be the understanding of Colombia's banking superintendent, Gerardo Hernández. He has announced a close review of those institutions where bad debt numbers have recently increased, so as to determine whether such institutions operate under applicable regulatory policies and guidelines or whether they deserve corrective measures. From another angle, the minister of finance should be mindful that imposing bad-loan reserves on banks, beyond real needs, would reduce banks' taxable profits in fiscal year 2012, the last year when Colombian companies will pay income tax at a 33 percent rate. Thereafter, if Congress approves the tax reform as the government has proposed, the income tax rate will drop to 27 percent."

> "The increased amount of past-due loans may not be viewed as a systemic problem that should require regulatory measures or new policies."
>
> *— Jorge Lara Urbaneja*

The Advisor *welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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