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FEATURED Q&A

Has Mexico Found a Good Solution to Banks' 'De-Risking?'



The new program of Banco de México (pictured above) will allow businesses to send dollars to each other through a new electronic clearinghouse. // File Photo: Alfonso21 via Creative Commons.

Q Mexico's central bank will soon unveil a program designed to facilitate the transfer of dollar-denominated assets between Mexican businesses, as international banks are beginning to 'de-risk' from Mexico. Does the program offer a good solution to the negative consequences of de-risking? How successful will a dollar transfer program such as this one be in cracking down on money-laundering in Mexico?

A Jan Smith, member of the Financial Services Advisor board and partner at KoreFusion in Mexico City: "Since 2012, international banks trading with Mexico have been fined \$2 billion for failing to comply with anti-money laundering regulations.

This is less than one percent of the dollars that originate and end in Mexico and pass through U.S. banks. Coldly speaking, a one percent fine should be an acceptable level of risk (credit defaults are much higher). Let's assume the lack of criminal convictions and absence of revoked banking licenses that have accompanied these fines implies there really was no criminal intent in failing to comply. Ergo, the fault lies in a lack of adequate controls, and that is where efforts to improve should focus. Instead, U.S. banks are severing ties with Latin American banks because the regulatory burden is too heavy. Risk management becomes risk avoidance, and with no risk there is never any reward. Quite the opposite. The result? Thousands of bona fide and legitimate business are without a bank, and tens of thousands of individuals are at risk of not receiving remittances. 'De-risking' actually increases the risk of money laundering by pushing entire segments of the economy out of the formal financial

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Citi Facing \$1.1 Bn in Claims Over Loan Scheme

A group of investors and creditors of bankrupt Mexican oil services company Oceanografía have sued Citi in connection with the loan fraud scheme that came to light in 2014.

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Mexico's Remittances Grow 18.8% in January

Remittances to Mexico surpassed \$932 million in January, surprising market analysts who had been disappointed by a flat December.

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BANKING

Scotiabank Sets Aside Higher Loan Provisions

Scotiabank, led by CEO Brian Porter, said the bank had set aside 16 percent more funds to cover bad loans in the oil and gas sector. Porter also said in a television interview that the bank has no plans to expand its business in Brazil or re-enter Argentina.

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Porter // File Photo: Bank of Nova Scotia.

BANKING NEWS

Scotiabank Sets Aside Higher Provisions for Bad Oil Sector Loans

Bank of Nova Scotia, also known as Scotiabank, said March 1 it had set aside more funds to cover bad loans in the oil and gas sector, warning of more bad loans to come as the price slump continues to cripple the oil and gas sector, Reuters reported. The bank's funds set aside for credit losses rose 16 percent in the quarter that ended Jan. 31, to \$399.94 million.

“We’ve got a small business in Brazil, and we’re fine with that, thank you.”

— Brian Porter

“We expect there to be additional provisions for some of our loans in the energy sector,” Chief Executive Brian Porter told analysts. During the quarter, Scotiabank had downgraded 10 percent of its energy portfolio, mostly in the exploration and production sector, with nine names on the “watchlist” of potentially higher-risk loans, according to Scotiabank Chief Risk Officer Stephen Hart. Oil prices reached a 12-year low in January, putting pressure on Canadian banks’ clients and causing some to default on their loans. Scotiabank has the biggest direct exposure to the oil and gas industry of all Canadian banks. Also on March 1, Porter said in a television interview that the bank has no plans to re-enter Argentina or expand its business in Brazil. “We’ve got a small business in Brazil, and we’re fine with that, thank you,” Porter said on Bloomberg TV Canada. “And Argentina, we have no desire to go back.” Scotiabank left Argentina in 2002 after the country’s massive debt default, and has a Brazil business that focuses on investment banking and corporate lending.

Chilean Banks Boosting Provisions by \$150 Mn: Fitch

Chilean banks’ loan-loss provisions have increased by \$150 million due to new requirements implemented in January by the country’s central bank, Fitch Ratings said March 3. “Although the new requirements were generally met with existing loan reserves, the new provisioning model will strengthen Chilean banks’ loan reserve buffers for mortgages in the medium term, which is important following five years of strong mortgage growth,” the ratings agency said in a statement. The central bank’s new model for provisions is based on the number of days a loan is past due, loss given default and for the first time now uses the loan-to-value ratio, according to Fitch. That new requirement is the main reason that banks’ provisions increased. On average, Chile’s level of mortgages grew 13.2 percent annually between 2010 and 2015. Most of the country’s banks accounted for the regulatory change last year, but some waited until their January financial statements in order to account for the



López Saffie // File Photo: Banco del Estado de Chile.

higher provisions, the ratings agency said. It added that Banco del Estado de Chile had the largest requirements, but it had voluntary reserves valued at about \$370 million in order to meet the more stringent requirements. Banco del Estado de Chile, led by CEO Jessica López Saffie, started building its voluntary reserves in 2009, a move Fitch said was “prudent since its mortgage portfolio accounts for approximately one-third of gross loans and has a high concentration of low-income borrowers.” Other major banks in the South American country

NEWS BRIEFS

Citigroup Facing \$1.1 Billion in Claims Over Loan Scheme

A group of investors and creditors of bankrupt Mexican oil services company Oceanografía have sued Citigroup in connection with a scheme by which the bank’s Mexican subsidiary, Banamex, made short-term loans to Oceanografía based on Oceanografía’s fraudulent invoices, Bloomberg News reported Feb. 27. The scheme, which came to light in 2014, led Citi to cut its profit by \$235 million. The investors argue they incurred \$1.1 billion in losses.

Grupo Sura Pays \$538 Mn for Stake in Pension Unit

Colombia’s Grupo Sura, one of Latin America’s biggest financial groups, now owns 78.7 percent of Sura Asset Management after paying \$538 million for General Atlantic’s minority stake in its pension fund administration wing of the company, the Financial Times reported March 4. Grupo Sura has recently been expanding its acquisitions, buying the Latin American unit of British insurer RSA for \$614 million and expanding into Mexico, Chile, Argentina, Brazil and Uruguay.

Scotia Group Jamaica Names Hall New Chairman

Scotia Group Jamaica Limited, a subsidiary of the Bank of Nova Scotia, announced the appointment of Jeffrey Hall as the new chairman, effective March 4, the Jamaica Observer reported. He succeeds Sylvia Chrominska, who served five years on the board and two years as chair. Hall is the CEO of the Jamaica Producers Group and has been a member of the Scotia Group Board since November 2007. He is also the chairman of the bank’s Human Resources & Pension Committee and a member of the Audit and Conduct Review Committee of Scotia Group Jamaica.

financed the higher requirements with existing additional reserves, said Fitch. Mid-sized and niche banks are seeing less of an impact from the regulatory change, the ratings agency said. Fitch added that it believes banks in Chile are well-positioned to resist a third consecutive year of economic slowdown. Non-performing loans are likely to increase, however, as Chile's economic slowdown continues.

REMITTANCES NEWS

Mexico's Remittances Grow 18.8 Percent in January

The amount of money Mexican workers sent home from abroad grew 18.8 percent in January as compared to the same month last year, El Universal reported March 1. According to new central bank data, remittances surpassed \$932 million in January, surprising market analysts who were disappointed by relatively flat growth in money transfers in December. Measured in local currency, remittances grew "a very high" 45.5 percent in January as compared to the year before, Goldman Sachs analyst



Ramos // File Photo: Goldman Sachs.

Alberto Ramos said in a research note March 1. The Mexican peso has fallen in value over the past year by some 30 percent, from about 15 pesos per dollar a year ago to nearly 19 pesos. Combined with low inflation, the lower value of the peso is giving recipients a strong boost in real purchasing power, a positive development for private consumption trends among low-income families that make up the overwhelming majority of recipients, according

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sector altogether. 'De-risking' cannot be the default preference of U.S. banks. American regulators are passing the buck south. Mexican authorities are obliged to create a clearing house within the U.S. banking system, and Mexican banks face doubling compliance costs. Mexico's response is effective, but desperate, and begs the question: What would be the response be if instead of Mexico, it was a 'de-risking' of all the international banks that were fined?"

A Joy K. Gallup and Michael L. Fitzgerald, partners in the Corporate Department of Paul Hastings, LLP: "The decline of correspondent banking relationships between U.S. and other foreign banks and their Mexican counterparts due to concerns about money laundering regulations has made dollar transfers increasingly difficult, and even Mexican-based wired transfer services such as Monex have had to curtail their cross-border wire transfer operations due to increasing scrutiny and the fear of regulatory penalties. This is a significant problem for Mexico, considering the estimated \$531 billion in trade that it has with the United States. Having Mexican central bank oversight over a clearinghouse for business-to-business dollar transfers may help to overcome some of the regulatory concerns and enable smoother operations; however, the proposal from Banco de México requires participating Mexican banks to step up their own internal scrutiny of their customers and also contemplates a U.S. bank as a middleman in the transfer process. Both of these requirements seem problematic for the smooth implementation and effectiveness of the program. The potential for money-laundering arising from the realities of Mexico's geographic location in the chain of illicit operations from South America to the United States puts its dollar transfer activity in the unfortunate position of being extremely difficult to control. Further, assuming a U.S. bank is willing to step into the process, it would likely be subject to

the same intense scrutiny and penalties that caused the 'de-risking' in the first place. Despite Mexico's highly sophisticated banking system and evolving economy, these issues continue to present challenges for which there is no easy solution."

A Adalberto Palma Gomez, senior partner at Aperture S.C. in Mexico City: "The objective of correspondent banking relationships is to access financial services around the world and provide to third parties cross-border payment services to support international trade and financial transactions. In this scenario, central banks should contribute to an efficient international payment system. The announced system, known as SPID,

“At best, it is a small step toward fixing a huge problem with grave implications for swift international trade operations.”

— Adalberto Palma Gomez

seems not to be developed as a solution for 'de-risking.' At best, it is a small step toward fixing a huge problem with grave implications for swift international trade operations. The central bank should start working in a profound and holistic solution to the de-risking problem. An efficient financial industry needs to reduce its transaction costs and offer certainty on the requirements needed for establishing, maintaining and improving correspondent banking relationships with foreign financial institutions. A possibility exists for local and international authorities to develop an agreed-upon regulatory standard (a 'NAFTA standard') for correspondent banking relations. Establishing basic principles like: 'know your customer's

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to Ramos. Total remittances sent home in 2015 exceeded \$24 billion, the central bank said. According to a survey released Tuesday by American Express and CFO Research, Mexico ranks second in the world among countries surveyed for economic optimism. Seventy-nine percent of Mexicans surveyed said they expect economic expansion in their country this year, behind only India, with 86 percent.

POLITICAL NEWS

Opposition Coalition Launches Drive to Oust Maduro

Venezuela's Democratic Unity Roundtable, or MUD, coalition on March 8 announced a multi-pronged effort to force President Nicolás Maduro from office halfway through his six-year term. The attempt will include street protests as well as a recall referendum or a constitution-



Members of the MUD coalition on March 8 announced the effort to oust Maduro. // Photo: MUD Coalition.

al amendment to cut his term short, coalition leaders said in a news conference, Reuters reported. "Change is coming and no one can stop it," said the coalition's head, Jesús Torrealba. The group also said that the more than two dozen political parties that make it up unanimously decided to employ "all mechanisms for chance" in order to achieve a "national unity government." However, despite the display of unity, the MUD coalition has opposing factions, with former presidential candidate Henrique Capriles leading a moderate wing and imprisoned opposition leader Leopoldo López leading a more radical wing, analysts told Reuters. "The MUD's strategy reflects its internal divisions.

ADVISOR Q&A

What Does the Case Against Lula Mean for Rousseff's Government?

Q **Brazilian federal police on March 4 briefly detained former President Luiz Inácio Lula da Silva for questioning and searched his properties as well as his institute in an operation that involved some 200 agents. Lula, who has been implicated in connection with the massive corruption scandal at state-run oil company Petrobras, has repeatedly denied wrongdoing. His wife and sons are also being investigated. What does the police raid mean for Lula's power and prestige in Brazil and abroad? How big a blow is Lula's detention to the government of his protégé, President Dilma Rousseff? Does Rousseff need to distance herself from her mentor for the sake of her political survival? How will the Supreme Court's recent decision to put House Speaker Eduardo Cunha, a Rousseff foe, on trial for corruption charges related to the Petrobras case affect the impeachment case against Rousseff?**

A **Peter Hakim, president emeritus of the Inter-American Dialogue:** "The police actions against President Lula were the latest blow to his credibility and influence. Once considered Brazil's greatest political leader ever, Lula left office with 80 percent-plus public approval, but his approval rating has now slipped below 30 percent. Unless put on trial and found guilty, however, Lula cannot yet be written off as politically irrelevant. Despite his tarnished reputation, many Brazilians hold him in high regard. The Workers' Party (PT) he founded 30 years ago has no one else of his stature or authority. Indeed, across the political spectrum, there is a vacuum of leadership. Although hardly the favorite today, Lula could well be a viable candidate for president in 2018. President

Dilma's poll numbers are worse, close to single digits. Her aptitude for politics and governing is limited, and she has failed to mobilize the political support needed to address Brazil's battered economy. Without Lula's support, her capacity to govern will shrink further. She will become even more isolated and ineffective, while problems with

“Across the political spectrum, there is a vacuum of leadership.”

— Peter Hakim

the Brazilian electorate, Congress, and her own party are likely to grow. Impeachment remains a strong possibility and a case can be made for the president's resignation. It is disappointing, however, that Brazil's political leaders have not done much to build a minimal consensus on what next steps might follow her departure in order to confront the country's massive challenges—particularly to put some order and realism into policymaking in the legislative and executive branches and pursue a serious program for restoring economic stability and growth. Brazil is not a deeply polarized nation. Its Congress is erratic and mediocre, but it is not divided into two ideologically clashing blocs. Compromise is possible. It is early to consider Brazilian politics and economics broken and irreparable, just as it was premature to proclaim Brazil a robust success story a half dozen years ago."

EDITOR'S NOTE: More commentary on this topic appears in the March 8 issue of the Latin America Advisor.

NEWS BRIEFS

Mexico Won't Pay for Trump's Wall: Peña Nieto

Mexico will not pay for U.S. presidential candidate Donald Trump's proposed wall along the countries' border, Mexican President Enrique Peña Nieto told the *Excelsior* newspaper in an interview published March 7. In the interview, Peña Nieto also likened Trump's tone to that of dictators Adolf Hitler and Benito Mussolini. "Of course I can't agree with this American politician's position," said Peña Nieto.

Venezuelan Lawmakers Demand Gov't Probe Case of Missing Miners

Opposition members of Venezuela's National Assembly on March 8 demanded that Venezuela's government more closely investigate the disappearance of 28 miners in Bolívar state who were allegedly killed by gang members, the Associated Press reported. Family members of the victims say the miners were abducted and dismembered by a gang over a disputed gold claim. Some family members and those who witnessed the attack accused law enforcement agents of participating, though Defense Minister Vladimir Padrino López denies the claims.

Colombia Fines Uber for Providing Unauthorized Taxi Services

Colombia fined the app-based taxi service Uber on March 7 for providing unauthorized transportation services, the Associated Press reported. The company was fined approximately \$140,000 for failing to comply with local transportation regulations. Uber responded in a statement by saying it's been unfairly pursued by the Colombian government, adding that it would continue operations in the country. Bogotá's taxi driver association welcomed the fine, but said it does not go far enough.

Today's announcement had been postponed twice in the last five days. Lacking consensus, the coalition has opted to pursue three distinct but overlapping strategies," said Nicholas Watson of Teneo Intelligence Consultancy, the wire service reported. The opposition coalition said it would begin protests on March 12 in Caracas. However, Maduro's opponents are expected to try to avoid a repeat of the violent protests of February 2014, which led to the deaths of 43 people. Maduro supporters have condemned the opposition's plans, saying they amount to a U.S.-backed coup effort and would lead to bloodshed. "They want to organize street rallies to generate violence and bring about a coup, supported by U.S. imperialism," former National Assembly head Diosdado Cabello said this week, *The Guardian* reported. [Editor's note: See [Q&A](#) on Venezuela's political situation in the Jan. 12 issue of the Advisor.]

Obama to Announce Further Easing of Restrictions on Cuba

U.S. President Barack Obama's administration will announce further easing of restrictions on Cuba on March 17, ahead of his historic visit to the communist-ruled island later this month, U.S. congressional sources told Reuters on March 8. Details on the measures were not immediately available as they are still being decided upon, but are likely to make it easier for U.S. citizens to travel to Cuba if they apply under one of the 12 approved categories of travel such as educational or cultural visits. The measures will also likely ease trade and banking rules. The White House has invited members of Congress to accompany the president during his visit on March 21 and 22 to Havana, and about 20 members of Congress, mostly Democrats, are expected to go. Critics in the government have argued that the White House's policy shift is giving too much to the Cuban government without receiving much in the way of policy shifts from the Cuban government in return. Obama's trip to Cuba this month will be the first visit by a sitting U.S. president since 1928.

ECONOMIC NEWS

Colombian Mining Minister Resigns Amid Graft Probe

Colombia's mining and energy minister, Tomás González, resigned March 7 from his post after being charged with corruption, according to Colombia Reports. President Juan Manuel Santos told reporters in Bogotá that González did not resign over the corruption scheme he was allegedly spearheading, but rather over the difficulties associated with maintaining Colombia's energy reserves amid the country's worst energy crisis since the 1990s. Colombia's reserves are under pressure, due to an extreme drought caused by El Niño and technical failures in some of the country's key power generators. On March 7, Santos announced measures designed to save energy, including a requirement that government buildings shut down their power at 6 p.m. Colombia's inspector general's office is investigating whether González participated in influence peddling. One of his family's companies, Connecta, received state contracts adding up to a total of \$2 million to measure public opinion while he was minister. González said he sold his 20 percent stake in the company in October 2010 in order to serve in the government as vice minister, but by March 2013, he left the government and returned to Connecta as an employee. During that time, the company closed at least two contracts with the government amounting to hundreds of thousands of dollars, and before the contracts were even close to finished, González was back in the government, working in Santos' Good Governance foundation. He was named the minister of mining and energy in March 2014. While he was working in the government for a second time, Connecta received assignments valued at approximately \$1 million from the Education Ministry and the Fund for Special Peace Programs. Santos' interior minister, finance minister, health minister, defense minister and housing minister are also under investigation by the inspector general in connection with corruption allegations.

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customer,' exchange of information between institutions, scope and quality for customer due diligence and enhanced due diligence as well as monitoring, internal controls, training, audits and supervision. Meanwhile, the central bank should consider facilitating those products and services (payments to third parties and repatriations of dollars) that have been limited, reduced or canceled by U.S. correspondent banks to Mexican institutions. SPID, although a step in the right direction, is not structured for cracking down on money laundering. It relies on the anti-money laundering policies, procedures and responsibilities of the institutions. Not taking care of formal and supervised payment systems, flows of money could divert to alternative channels where money traceability becomes difficult, with the correspondent risk of money laundering."

A **Eduardo Canales, global energy transactions associate at Akin Gump Strauss Hauer & Feld, LLP:** "The development of rigorous anti-money laundering and compliance regulations in financial hubs around the world to de-risk international transactions has had unintended consequences on the Mexican banking system. Even though these controls were conceived to combat illegal activities, their implementation has slowed down thousands of legal transactions burdened by the heightened standards and causing, for instance, the cancellation of international bank accounts, the severance of banking relationships between international financial institutions and their Mexican counterparts and the denial to process money wires. It is estimated that Mexico had more than \$380 billion in exports and over \$395 billion in imports worldwide during 2015. Mexico's integration into the global eco-

nomie system as well as the interactions of thousands of Mexican businesses with firms around the world have created the need for an efficient domestic financial system that promotes observance of international anti-money laundering and compliance regulations while providing the necessary tools that facilitate transactions into, out of and within Mexico in global currencies. Mexico's central bank is trying to address this market inefficiency and provide the basic tools to support the globalization of the Mexican banking system through the creation of the Sistema de Pagos Interbancarios en Dólares (SPID). This interbank payment system will work as a clearinghouse to facilitate dollar transactions between Mexican businesses while incorporating swift transparency and anti-money laundering standards. The SPID is expected to allow Mexican banks to process dollar transactions more efficiently and at a lower cost. Banxico is expected to supervise the operation of the clearinghouse as well as the SPID's relationship with an American clearing bank. Moreover, the SPID will include international best practices like the use of the Global Legal Entity Identifier System, which assigns unique identifiers to legally distinct entities and allows monitoring of their financial market activities, and heightened reporting and auditing requirements for participating domestic banks. The SPID's success will depend on the costs involved, which will drive the participation by Mexican banks and businesses, and the regulatory and enforcement mechanisms, which may help assimilate heightened rigorous anti-money laundering and compliance controls, ultimately de-risking Mexico."

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

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