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Featured Q&A with our Board of Advisors

Q Citigroup announced July 19 it will acquire up to 50 percent of Chile's Quinenco, the company that control's Banco de Chile, the country's second-largest bank. In light of the news, what is the outlook for Banco de Chile? What about the country's banking sector in general? Do you see more acquisitions in Chile on the horizon?

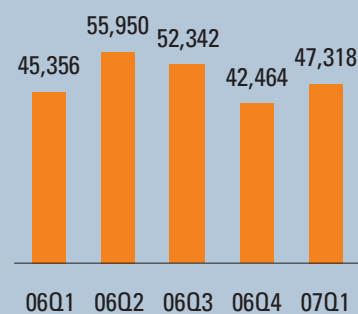
A **Guest Comment: Jeanne del Casino:** "We believe this transaction has the potential to dramatically shift the balance of competition among banks in Chile, particularly for the largest players, in terms of pricing power, operating efficiency, and product offerings given the management and financial resources available within Citigroup. Nevertheless, it may put even greater pressure on medium-sized or small banks which would spur further consolidation. That said, this transaction, and others like it, should have a positive effect on the Chilean banking system in light of the financial and qualitative benefits it implies. The Citi-BCH partnership is also representative of the increased interest and commitment we are seeing from major international banks in Latin America as a whole. The Citi-BCH transaction raises the question of whether other potential suitors might pursue larger investments in Chile and elsewhere. Scotiabank has already made a significant new investment in the Andean region by acquiring Banco Wiese in Peru and is at the same time

empowering its Chilean operation to diversify and increase market share. The already dominant Santander could acquire ABN Amro's operations in Brazil, should its European consortium be successful in acquiring the parent. HSBC and BBVA are also potential acquirers. Other deals may ensue because of the combination of margin pressure and the need for more capital to fund the dynamic loan growth in Chile during the past four years. Important new investments in technology are also driving consolidation, as is the case for the industry globally. The Citi-BCH transaction is likely to put significant pressure on banks such as Bci, the country's fourth-largest bank, whose capital base is much smaller,

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FEATURED CHART

**Banco de Chile
Quarterly Net Income**
(2006-present, in Ch\$ millions)



Source: Banco de Chile

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NEWS BRIEFS

**Banco Patagonia IPO
Raises \$260 Million**

Argentina's **Banco Patagonia** generated about \$260 million from its IPO on three stock exchanges starting on July 19, Dow Jones reported. The bank sold a total of 200 million shares, about 30 percent of its share capital.

**Bancolombia Raises \$480 Million
Through Share Offering**

Bancolombia, Colombia's biggest bank, said July 25 it raised \$480 million in an offering of preferred shares on local and international markets. In a press release, Bancolombia said it sold 21,307,238 shares in Colombia at a price of 15,205 pesos (\$US 7.80) per share and 8,411,470 American Depositary Shares at \$33.25 per share in the operation concluded on July 24. **UBS Securities LLC** served as the global coordinator for the offering.

**Profit Drops 23 Pct at Puerto
Rico's Popular on Loan Losses**

Second-quarter profit fell 23 percent at **Popular Inc.**, parent of Puerto Rico's largest bank, **Banco Popular**, the company reported on July 18 amid soaring loan losses, according to Reuters. The San Juan-based company set aside \$115.2 million for loan losses in the quarter, up 72 percent from the year-earlier period, as bad loans it doesn't expect to be paid soared 78 percent to \$92.1 million. Net income in the quarter fell to \$75 million from \$97.4 million in the same period a year ago. In other Puerto Rico news, the struggling **Doral Financial Corp.** reported July 19 it closed the sale of 90 percent of its shares to a group led by **Bear Stearns Merchant Banking**, according to Reuters.

Financial Services News**ING in Talks to Buy Santander's
LatAm Pensions Business**

Netherlands-based financial services giant **ING Groep** is in talks to buy **Santander Central Hispano's** pension operations in Latin America, Bloomberg News reported on July 26. Santander CEO Alfredo Saenz said his bank is in "advanced talks" to sell its pension funds business in Latin America, and that ING is a candidate. An ING spokeswoman, Pilar Teixeira, confirmed the report. Santander has also reached an agreement with Argentina's **Banco de la Provincia de Buenos Aires** to sell pension fund manager **AFJP Origenes** to ING for 300 million euros (\$US 413 million), AFX reported on July 25, citing a report in Argentine daily *Clarín*.

**Citigroup to Combine Operations
with Banco de Chile**

US financial services giant **Citigroup** will combine its operations in Chile with the country's second-largest bank, **Banco de Chile**, through a strategic partnership with Banco de Chile's parent company, **Quinenco**, Citigroup announced on July 19. Under the deal, Citigroup will initially acquire an approximately 32.96 percent stake in **LQIF**, a wholly-owned subsidiary of Quinenco that currently holds 52.2 percent of the voting rights and a 30.5 percent economic interest in Banco de Chile, Citigroup said in a press release. Citigroup said it has the option to acquire up to 50 percent of LQIF within three years, at which time LQIF's economic interest in Banco de Chile would be approximately 37.8 percent. Upon completion of the transaction's first phase, expected early in the first quarter of 2008, Citigroup's

Chilean unit, **Citi Chile**, which is valued at \$701 million, will be combined with Banco de Chile. Citi will also contribute an additional \$192 million worth of assets in cash or other businesses, Citigroup said. The deal will result in an institution with a 20 percent market share of the Chilean banking industry, according to Citigroup. As part of the overall transaction, Citigroup will also acquire the US businesses of Banco de Chile for a consideration of \$130 million, it said. Citigroup has the option to acquire an additional 17.04 percent stake in LQIF for approximately \$900 million. The new partnership calls for active participation by Citi in manage-

“ This transaction also underscores Citi's long-term commitment to a key growth market in Latin America. ”

— *Manuel Medina Mora*

ment of Banco de Chile, including board representation at both LQIF and Banco de Chile. "As we did successfully with Banamex in Mexico, we will blend Citi's global products and capabilities with Banco de Chile's leading brand, local expertise, and distribution platform," Manuel Medina Mora, chairman and CEO for **Citi Latin America and Mexico** was quoted as saying in the press release. "This transaction also underscores Citi's long-term commitment to a key growth market in Latin America," he said. [Editor's note: see related [Q&A](#) on page 1.]

**Brazil's Redecard Raises
\$2.15 Billion in IPO**

Brazilian credit card company **Redecard** said it raised 4.07 billion reais (\$US 2.15 billion) in a July 12 initial public offering. In an announcement posted on its Web site, Redecard said it sold 150,827,527 shares at a price of 27 reais per share on the **Sao Paulo Stock Exchange's** Novo Mercado, a special listing for companies

BANK FACTS**Banco de Chile**

- * Second-largest bank in Chile
- * Clients: More than 1 million
- * Total Assets: \$23.9 billion
- * Loans: \$17.9 billion
- * Deposits: \$15.0 billion

Source: Citigroup
Data: 2006

that adhere to stricter corporate governance standards and international accounting principles. Brazilian banks **Itau** and **Unibanco**, and the US' **Citibank**, which jointly control the company, announced in May they would sell part of their stakes in Redecard through the IPO. Citigroup said in a press release that as a result of the sale, from which it expects to record a \$400 million gain in the third

Redecard was the 33rd Brazilian company to go public this year and the 72nd to list on the Novo Mercado.

quarter, its stake in the credit card company fell from 31.9 percent to 25 percent. Redecard was the 33rd Brazilian company to go public this year and the 72nd to list on the Novo Mercado. *Financial Services Advisor* board member Jan Smith, managing director of Miami, FL-based analysis and consulting firm **InfoAmericas**, said in May that Redecard's decision to go public made sense amid positive economic developments in Brazil and expectations for continued growth in the country's credit card market. Redecard will likely focus its growth strategy on expanding use of cards to lower-income consumers and on building loyalty and use among existing cardholders, and will work to improve systems for profiling customer risk and use patterns, Smith told the *FSA*. [Editor's note: see the May 29, 2007 [issue](#) of the *FSA*.]

Deutsche Bank Announces Plan to Expand Brazilian Presence

Deutsche Bank AG, Germany's biggest bank, plans to expand its workforce in Brazil by 25 percent, CEO Josef Ackermann announced on July 16 following a meeting with Brazilian President Luiz Inacio Lula da Silva, Bloomberg News reported. "Latin America is becoming more important to us," Ackermann said. "We are extremely committed to strengthening our resources in the region. That's why we are here." Deutsche Bank,

Special Q&A

How Extensive is Insider Trading in Brazil?

Q The Brazilian government is reportedly stepping up efforts to crack down on insider trading in the country's stock market.

How extensive a problem is insider trading in Brazil, and what impact is it having on the country's markets and economy? How can Brazilian securities regulators best combat the phenomenon?

A **Board Comment: Roberto Teixeira da Costa:** "Insider trading is a problem for every stock market in the world. I remember very well that during the few months after the creation of our Securities Commission (CVM), which was organized in 1977 by a board that I chaired, one of our deepest concerns was how to control insider trading. One of the first inquiries by the CVM, which we investigated, involved Petrobras after the disclosure of offshore oil discoveries in Campos, in Rio de Janeiro. As the market grows, with daily transactions on the Sao Paulo Stock Exchange exceeding \$2 billion and IPOs projected to be more than \$20 billion in 2007, an increasing preoccupation with insider trading is natural. If corporate governance is being defended as one of the most important pillars of the Novo Mercado (New Market, created by the Sao Paulo Stock Exchange in 2001 and now concentrating particularly on all the new issues), let's not forget that many newcomers to the market are not yet fully conscious of the implication of being a public corporation with listed shares. Thus, some lead time has to be given to analyze the full dimension of this new reality. Abrasca (Brazilian association of publicly held corporations) recently edited a very comprehensive document alerting their associates to the need for full disclosure and avoiding practices that go against best-market development. The CVM, on the other hand, is fully aware of the need to prevent and punish insider trading. Processes are being put in motion, and speedier and final results are being publicized closer to the event that

generated the process. Nevertheless, no regulatory agency can replace market players and the benefit of practicing self-regulation for market growth and maintaining investor confidence."

A **Guest Comment: Thiago Giantomassi:** "Illegal insider trading takes place in any country's capital markets, including Brazil, and punishment essentially depends on the respective securities and exchange commission having a strong system and a highly technical staff to effectively avoid such practices. Brazil is evolving, especially by virtue of the CVM's efforts—despite its reduced staff ... For example, the CVM halted the clearance of some suspicious trades on the stock exchange in a recent transaction involving publicly held companies. However, as a result of the increasing number of companies going public, more Brazilian citizens are investing in securities markets (mainly shares), highlighting the stock market's importance in the Brazilian economy as an investment option for public savings and requiring an active enforcement program by the CVM. At the same time, in such initial public offerings, around 70 percent of the investments are from foreign qualified institutional investors, which will also play an important role in bringing international regulatory standards into Brazil and enhancing Brazilian securities markets. In particular, the CVM will need to establish the inspection, detection, and prosecution of illegal insider trading as one of its main policies. Such a policy will succeed in maintaining fairness and integrity as the main assets of the securities markets."

Roberto Teixeira da Costa is a member of the Financial Services Advisor board, a member of the boards of Banco Itau and SulAmerica in Brazil.

Thiago Giantomassi is an Associate at Demarest e Almeida Advogados in Brazil.

which currently employs 250 people in Brazil, has about 8.98 billion reais in total assets in the South American country, according to Brazil's Central Bank, Bloomberg News reported. In June, a Deutsche Bank subsidiary paid 950 million reais for a real estate unit of **Unibanco**, Brazil's sixth-largest bank. Deutsche Bank's expansion in Brazil comes as record-low interest rates and rising corporate earnings have prompted the benchmark **Bovespa** stock index to climb 189 percent in dollar terms over the last two years. Every month since February 2004, bank lending in Brazil has increased. Last month, the central bank cut its benchmark interest rate for the 16th time in less than two years to 12 percent, helping to boost bank lending by 20 percent over a year period, Bloomberg News reported. Other foreign investment firms have already begun to expand in Brazil. Last year, **UBS AG**, Switzerland's largest bank, purchased **Banco Pactual SA** for \$2.6 billion, and this past March, **Goldman Sachs** announced plans to double its staff in Brazil.

Mexico to Require Fee-free Banking

Mexico's central bank will require lenders to offer free accounts to low- and middle-income consumers in an effort to reduce the high service fees it says prevent many Mexicans from participating in the financial system, Banco de Mexico officials announced on July 13, according to Bloomberg News. Commercial banks will have six months from July 16 to offer accounts that do not charge fees for ATM

O'Dogherty expressed hope that the new requirements will make it easier for Mexicans to open their first bank accounts and make lenders more efficient.

withdrawals, balance inquiries, debit cards, and maintenance. "Many people don't open an account because they're afraid of the fees," Pascual O'Dogherty, head of financial system research at the

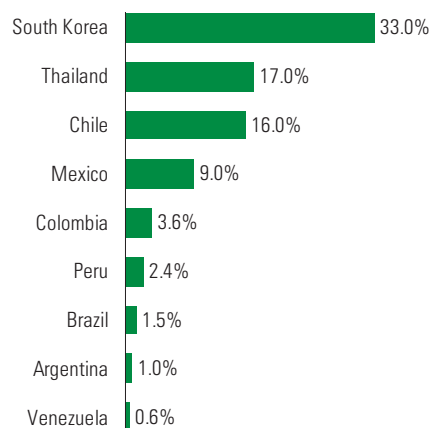
In Focus

Ample Room for Growth in LatAm's Mortgage Markets—Report

There is ample room in Latin America for banks to grow their mortgage markets, according to a report published this month by the *McKinsey Quarterly*.

"Comparisons with emerging economies elsewhere illustrate the growth potential of banking in Latin America," wrote the report's author, Luis Andrade, a director in consulting firm McKinsey & Company's Bogota office.

Mortgage Penetration* (as a % of GDP)



Source: The McKinsey Quarterly
* December 2005 data

The report notes Latin America's growing middle class purchasing power, GDP growth rates in the 4 to 5 percent range, falling interest rates, and lengthening debt maturities.

"On the asset side, the growth opportunity in mortgages stands out," he wrote. "Except for Chile, which has enjoyed monetary stability for more than a decade, none of the major economies has experienced the conditions needed to develop this important market," Andrade observed, noting low numbers for mortgage penetration in Latin America compared to other emerging markets.

"These numbers would actually be lower if governments didn't use subsidies and forced-lending mechanisms," he explained.

central bank said in an interview, according to Bloomberg News. O'Dogherty expressed hope that the new requirements will make it easier for Mexicans to open their first bank accounts and make lenders more efficient. The new rules apply to any payroll account or those accounts where an individual deposits more than 165 times the daily minimum wage per month, about 8,000 pesos (\$US 743) per month. O'Dogherty said these parameters cover most of the Mexican population. Since winning a second term in 2003, Central Bank Governor Guillermo Ortiz has made competition in the banking sector a priority. He has required banks to cut credit and debit card fees by \$200 million annually and to disclose all levies built into loans. Still, six banks control almost 90 percent of banking assets in Mexico. According to a 2004 survey by the govern-

ment's statistics agency, the latest information available, just one-fifth of Mexico's 25.8 million households use financial services, Bloomberg News reported.

Economic News

Ecuador's Correa Appoints New, Moderate Economy Minister

Ecuadorean President Rafael Correa on July 25 replaced his hardline economy minister, naming a more market-friendly moderate to the post. Correa appointed 42 year-old Fausto Ortiz, who served for 15 months as vice minister of the economy during the previous administration of ex-President Alfredo Palacio, to head up the ministry. Ortiz immediately adopted a

softer line than his predecessor, Ricardo Patino, who had upset investors with talk of restructuring the country's foreign debt. Ortiz said Ecuador would not do anything that might jeopardize foreign financing, and that spurring economic growth was his priority, not debt restructuring, Reuters reported. Correa and Patino said the cabinet moves did not signal a change in economic policy. "Fausto Ortiz will not only continue with our sovereign agenda, but his contribution will also be evidence that we are not a cult but rather a team of thousands of women and men willing to give our lives for our new country," Correa was quoted as saying.

Head of Argentina's Indec Replaced After Just Three Months in Office

The head of Argentina's National Statistics Institute, or Indec, has resigned after three months in office amid protests by Indec employees and criticism by outsiders that government inflation data had lost credibility, Bloomberg News reported on July 25. The economy ministry said it appointed Deputy Director Ana Maria Edwin as the new head of Indec, replacing Alejandro Barrios, who took control of the Institute on April after then-Director Lelio Marmora resigned a month earlier. "Barrios wasn't managing the personnel at Indec well nor publishing the statistics data on time," Economy Ministry spokesman Eduardo De Simone was quoted as saying. "Edwin has the capacity to manage Indec better." In February, Kirchner replaced Indec's career official in charge of measuring inflation with a political appointee, prompting employee protests and leading investors to question the reliability of inflation data reported by a government facing politically damaging rises in consumer prices.

Political News

Lula Fires Defense Minister Amid Continuing Aviation Crisis

Brazilian President Luiz Inacio Lula da Silva fired his defense minister on July 25, just over a week after a TAM airlines jet carrying 187 passengers crashed at Sao

Paulo's Congonhas airport, killing all on board and 12 people on the ground. The country's civil aviation system, run by the military, has been subjected to increasing criticism since last week's crash, the worst in Brazil's history and the second major crash in 10 months. The outgoing defense minister, Walder Pires, a close friend and political ally of the president, was replaced by former Supreme Court President Nelson Jobim, the Associated Press reported. "It's no secret ... that we have an aviation crisis," Silva was quoted as saying at Jobim's swearing-in ceremony. "Every time the airplane door closes, I deliver myself to God," he added. Jobim will have to make good on Lula's promises, made in a televised speech on July 20, to investigate the causes of the crash, build a third airport in Sao Paulo, and deal with strife among air traffic controllers. Controllers have staged a number of work slowdowns to protest poor work and safety conditions since last September, when 154 people died in a Gol airlines flight that crashed over the Amazon. In the last week, a radar failure, rainy weather, and the closure of the Congonhas runway where the TAM flight crashed have all sent the country's air travel system into chaos.

Uribe Says Colombian Institutions Now Free of Paramilitaries

Colombian President Alvaro Uribe said July 20 that his country's institutions are now free of infiltration and corruption by right-wing paramilitaries, the Associated Press reported. "Today paramilitarism no longer exists because combat against leftist rebels is now, in practice, the exclusive work of our democratic institutions," Uribe was quoted as saying during a speech to Congress marking Colombia's independence day. Uribe also said collusion with the paramilitaries, who are blamed for some of the worst human rights abuses during the country's decades-long civil war, "was never institutional," contradicting testimony by former paramilitaries, soldiers, and victims of the civil war who say the paramilitaries often worked closely with government security forces, according to the AP. [Editor's note: see related Q&A in the July 25, 2007 [issue](#) of the daily *Latin America Advisor*.]

POLITICAL & ECONOMIC BRIEFS

Argentine Peso Falls to Four-Year Low Against the Dollar

The Argentine peso lost two centavos against the dollar on July 25, bringing the currency to its weakest point since early 2003, while the Central Bank sold dollars in the spot and futures markets to curb further losses, Dow Jones reported. The peso ended the day at 3.18 pesos per dollar in the interbank market, six centavos less than the close on Friday, July 20, a relatively steep loss compared to other emerging market currencies, which have also slumped lately.

Mexico's 12-Month Inflation Rises Above Central Bank's Upper Limit

Inflation in Mexico edged into the central bank's danger zone, as consumer prices in Mexico increased 0.25 percent in the first half of July, Reuters reported. Banco de Mexico said the 12-month inflation rate hit 4.08 percent, above an upper limit of 4 percent, prompting expectations for an interest rate hike this year. Prices for food such as dairy and tomatoes led the increases during the period, according to Reuters.

Rebel Group Says Pipeline Attacks Were in Self-Defense

The EPR, the Mexican guerrilla group that claimed responsibility for July 5 and 10 bomb attacks on natural gas pipelines owned by state-owned oil monopoly Pemex, released a new statement on July 19 saying the attacks were "in self defense," Bloomberg News reported. The EPR said it must act against the current administration because of its repression of popular movements and demanded the release of two of its members allegedly held by the government.

Featured Q&A*Continued from page 1*

but has an established and diverse retail franchise that makes it attractive to domestic and international institutions alike. Other smaller, but still sizable, institutions such as CorpBanca, Banco del Desarrollo, and Banco Security, are also attractive targets because of their niche and product expertise and client penetration."

A **Guest Comment: Tricia Juhn:** "In the next three to five years, we anticipate that the lion's share of Latin retail banking will be divided among two or three global giants—say Citi, Santander, and a third player to be named later. Citi's acquisition of Quinenco is a logical addition to its global portfolio. On the Citi

“The process is inexorable: bulge brackets need to show returns to their investors, and they go where the growth is.”

— *Tricia Juhn*

side, the buy is driven by the success of acquisitions in Mexico and Central America. On the Chilean side, the deal gives Citi a 20 percent share of the market, roughly on par with rival Santander. This deal is the continuation of consolidation in the Latin financial services sector, as local banks get bought out by global giants. (Citi and HSBC have effectively divided Central America between them. Some 80 percent of deposits in Mexico are owned by five banks, led by Citi's Banamex and Bancomer-BBVA.) We are seeing Scotiabank make prudent but decisive moves throughout Latin America as well as the Caribbean; and there are the Spanish giants, Santander and BBVA, to contend with. The process is inexorable: bulge brackets need to show returns to their investors, and they go where the growth is. It makes sense that they would go where macro condi-

tions have stabilized enough to execute. Moreover, once one bulge bracket goes into a new market, the others will follow to compete for share. Expect continuing consolidation within Latin America, with a cautious expansion into the Caribbean in the medium term."

A **Guest Comment: Natalia Aránguiz:** "Throughout 2006, loans in the Chilean banking system grew at a rate of 20 percent. However, that trend has tended to slow this year. Moreover, future inflation pressures foretell interest rate hikes in monetary policy that could decrease the demand for credit. On the other hand, the general tendency in the sector is a focus on low-penetration segments by way of [banks'] consumer divisions. This primarily occurs because much higher interest rates can be applied to these loans than to those for large companies. Although Chile's banking sector is composed of 26 entities, 80 percent of the market is in the hands of just six banks. Thus, in aiming to improve efficiency, generate economies of scale, and compete on a more level field with the country's large banks, it is natural to imagine new alliances in this sector. In this context, the strategic alliance between Banco de Chile and Citibank offers Banco de Chile better tools to compete in the most attractive market segment: individual consumers. Additionally, in the corporate segment, the combined bank is positioned as the largest in the country. Finally, Citibank's international experience makes the prospects for this new alliance very attractive."

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The Inter-American Dialogue's Financial Services Advisor

is published biweekly.
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The Inter-American Dialogue's **Financial Services Advisor** is published biweekly from 1211 Connecticut Avenue, Suite 510 Washington, DC 20036
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