

FINANCIAL DEVELOPMENT IN LATAM. THE ROAD AHEAD

Comments to the world bank report

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Comments & Overview



- ❑ Thorough, meaningful, extremely rich analysis of the state and challenges of financial development in Latin America
- ❑ Influenced by crisis environment and flaws in financial deepening in advanced economies
- ❑ Propositive and bold. Policy compendium
- ❑ One general comment and some remarkable findings
- ❑ 3 specific topics:
 - International corporate issuance
 - Role of cross border banking and financial stability
 - Macroprudential policies

A general comment. Is the pendulum swinging too much?



FD basis	Afterthoughts
Macro stability	Too much of a good thing
Financial liberalization	Discipline dilution, excesses
Basel standards	Too narrow
Financial access	Excesses lead to problems
Bright side	Dark side

A bigger role for policies

- Shaping incentives
 - Mitigating excesses
 - Filling gaps
 - Encouraging development
- Is this compatible with weak institutions?*
- Are AE lessons applicable to LAC?.*



Some remarkable findings (in addition to many others)



❑ LAC is underbanked, but not comparatively “underserved”

- Relevance of non-banking credit
- Substantial recent improvements in financial inclusion
- A wide banking gap remains. Multiple interacting explanations:
 - a turbulent macroeconomic and financial past, banking sector size,...
 - also, lagging productivity, lack of profitable projects >>> demand side

❑ Credit is biased toward ST/consumption v. LT/production-housing

- Remarkable: housing booms with no credit?
- Given productivity underperformance, a clear role for policy?

❑ The tested instrumental role of public banks

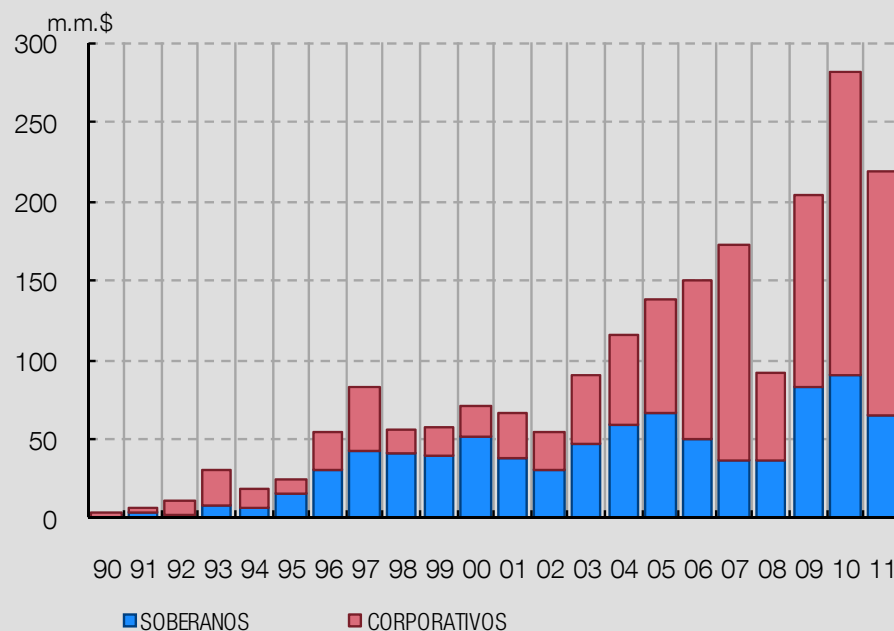
- Admittedly, beneficial aspects in the response to the crisis
- Trade off: normal times inefficiency, extraordinary times flexibility?

Specifics #1. International corporate bond expansion

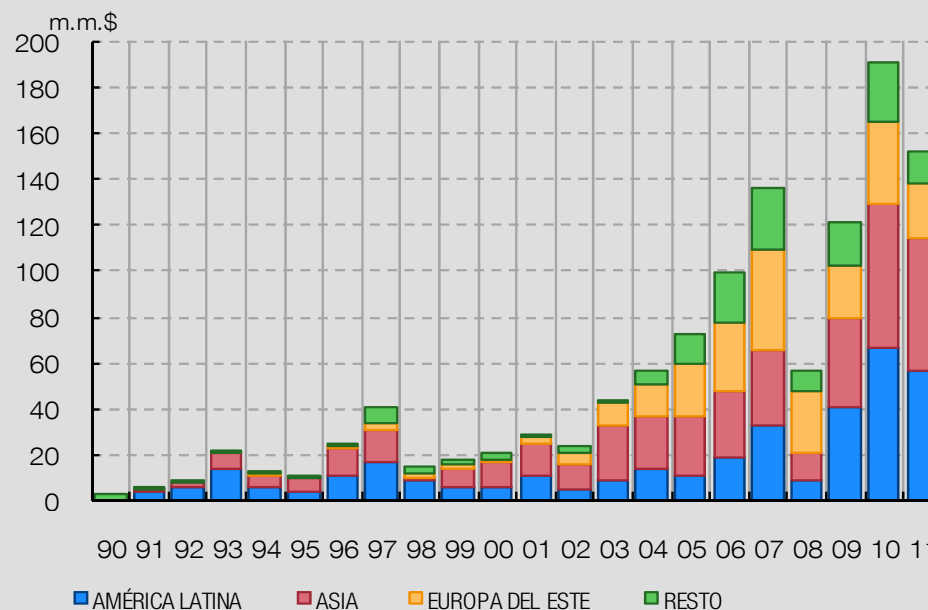


- Corporates explain over 70% of emerging market bond issuance post crisis
- Remarkable boom in Latin America

4. EMISIONES SOBERANAS Y CORPORATIVAS



6. EMISIONES CORPORATIVAS POR REGIÓN



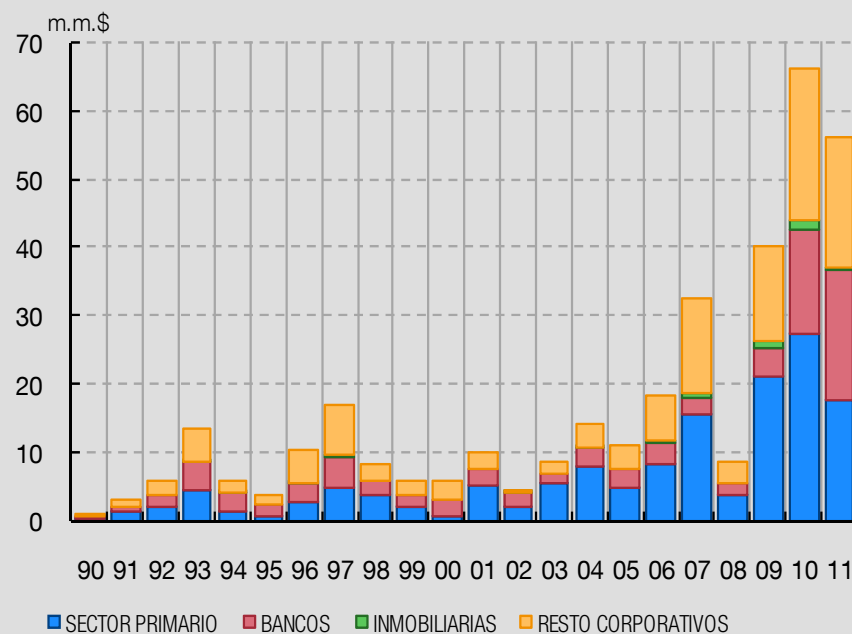
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Specifics #1. International corporate bond expansion



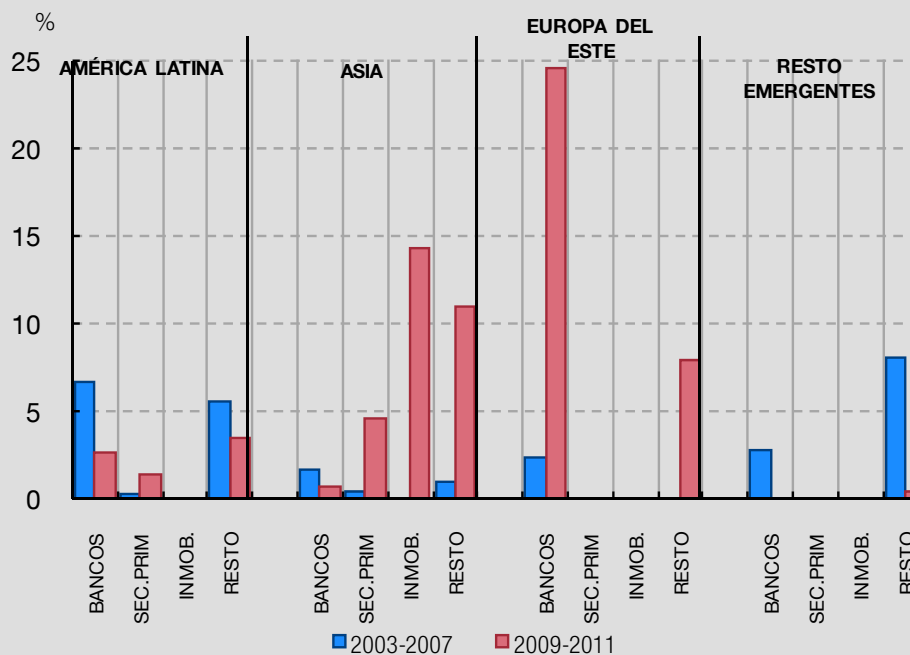
- Commodity-related + banks dominate issuance
- International issues in local currency on the rise, but still a long way to go
- Large increase in first-time issuers with lower ratings

2. EMISIONES CORPORATIVAS POR TIPO DE EMPRESA: AMÉRICA LATINA



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6. EMISIONES CORPORATIVAS: PORCENTAJE DE EMISIONES EN MONEDA LOCAL



Specifics #1. International corporate bond expansion



☐ Bright side:

- Broadens credit access
- Fulfills financing gap corporate sector

☐ Dark side?:

- Issuer credit risk:
 - sovereign vs corporate
 - sectoral and foreign currency-induced credit risk
- Exchange rate risk
- New issuers

☐ Is there increasing evidence of substitution for cross-border credit?

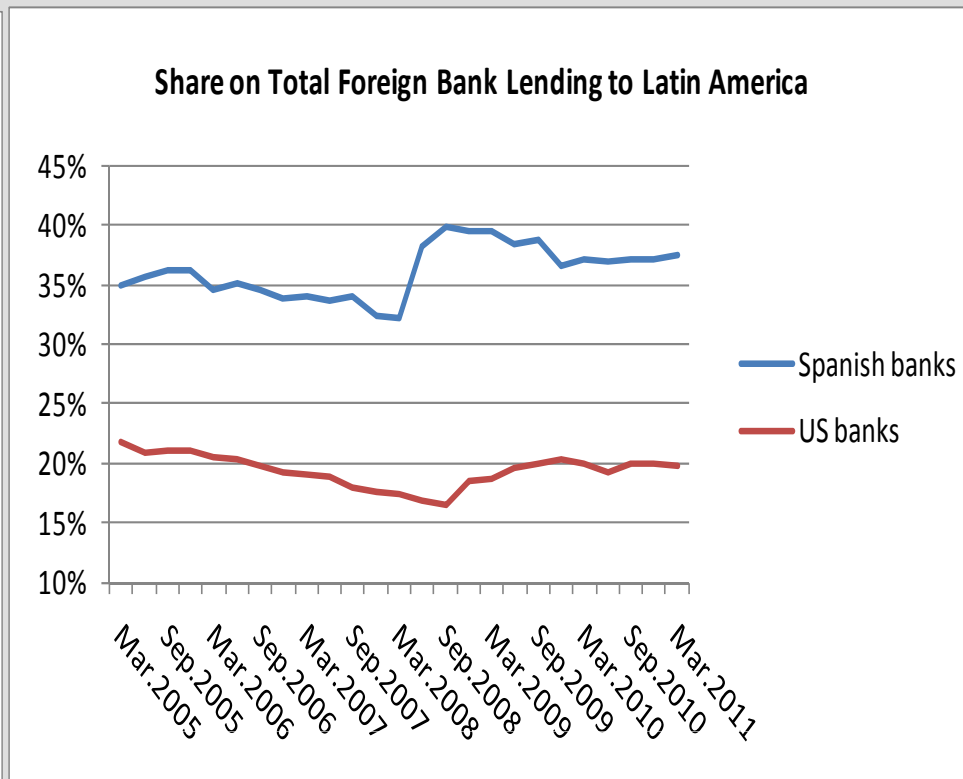
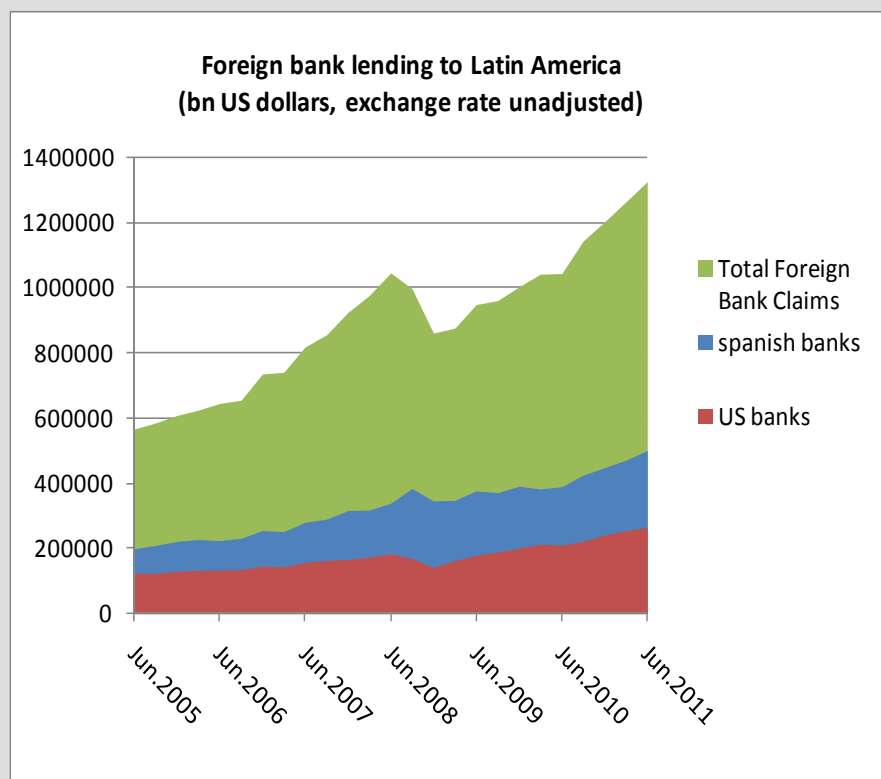
☐ If all risks moved in the direction of easier credit standards, should we worry?

☐ How can this be reconciled with preference for local markets development?

Specifics #2. Cross border business model and supervision. An Spanish perspective

Subsidiary model limits contagion risks

Business model based on retail banking, funding primarily deposits has been more resilient, there and here.



Specifics #2. Cross border business model and supervision. A Spanish perspective

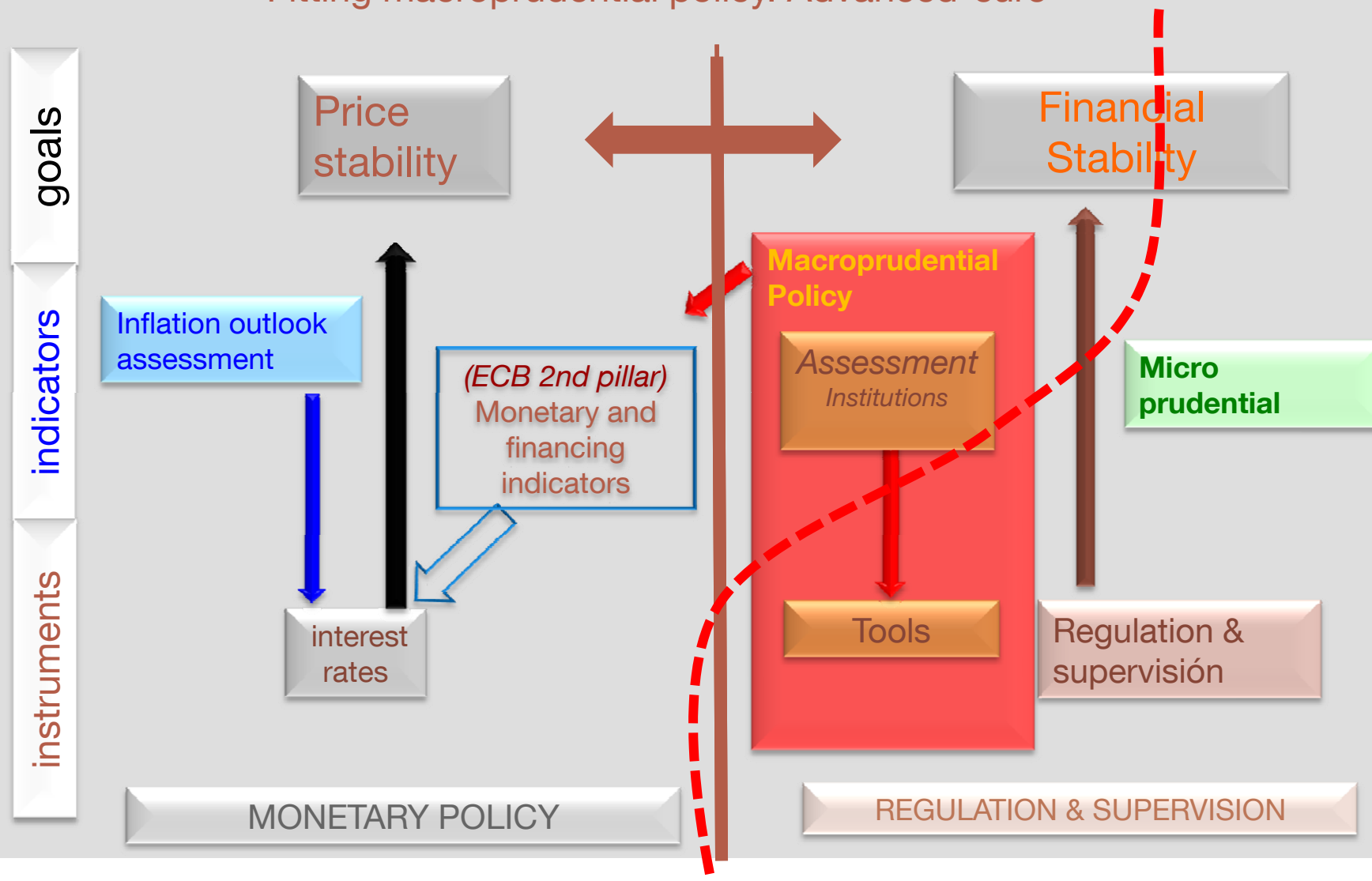


- ❑ **Effective cross border supervision is challenging...but a lot has been accomplished**
 - Universal colleges of supervisors
 - Positive and constructive relationships between host and home country
 - Crisis management groups

- ❑ **Structure, business model and cross border supervision reinforce each other. Implications for financial stability**
 - Symmetry
 - Perimeter of supervision

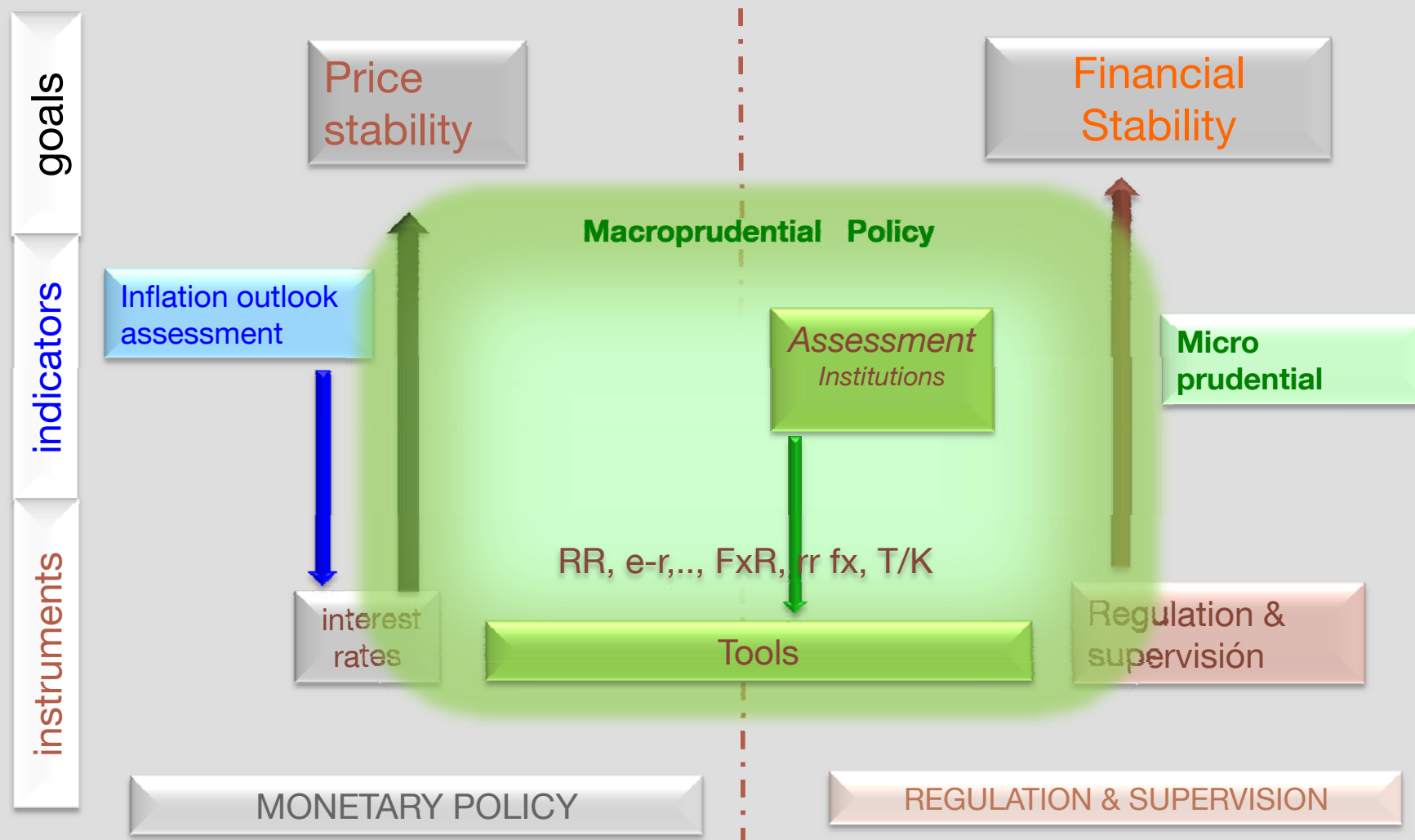
Specifics #3. Macroprudential policies

Fitting macroprudential policy. Advanced-euro



3. Macprudential policies

Fitting Macprudential policy. Emerging market economies



Conclusions



- **The road ahead for financial development in Latin America is looking much brighter than in the past**
 - Notwithstanding this, the global financial crisis and Latin underscores the scope for improvement.
 - Some reassessment is welcome and policy has a key role to play.
 - A great contribution
- **A cautionary note. The pendulum risk**
 - Beware of calls for higher public intervention in a region whose previous development was burdened by excesses in that area.
 - Quality v. quantity of intervention