

## CHILE

### BANKING

#### *SUMMARY*

As of year-end 1997, 29 banks and three consumer finance companies were operating in Chile. The Banco Santiago (the result of the merger of two banks in 1997) is Chile's largest bank, accounting for 17 percent of loans and almost 14 percent of deposits. However, Chile's one state-owned bank, the Banco del Estado, continued to hold the largest share of deposits, almost 16 percent of the total. Private banks handle nearly all corporate business within the banking sector. Three "financieras," roughly equivalent to consumer finance companies, concentrate on consumer business and are not permitted to offer checking accounts or handle international business.

Continued vigorous economic growth in recent years has strengthened bank profits. Loans and deposits both doubled in the four years through December 1997, and banking system assets grew in nominal terms by 25 percent in 1997.

A new banking law, passed in November 1997, stipulates objective parameters for allowing new banks to enter the Chilean market. The law also substantially expands the types of activities in which banks may engage: Chilean and foreign banks may establish subsidiaries for securities and insurance brokerage, leasing, and factoring. With the exception of the regulation regarding the maximum conventional interest rate, all of the regulations for effecting the changes embodied in the new law have been promulgated.

The banking sector is regulated by the Superintendency of Banks and Financial Institutions, an agency that reports to the Finance Minister. The Central Bank, in conducting monetary and exchange rate policy, also regulates bank operations.

As of year-end 1997, six U.S. banks had 35 branches in Chile. The six banks with branches accounted for around 4 percent of deposits and slightly less than 5 percent of loans in the banking system. U.S. banks generally focus on corporate rather than retail business.

Foreign banks are allowed to establish either as branches or subsidiaries, although the Bank Superintendency appears to prefer that foreign banks set up branches. Foreign banks operating in Chile are guaranteed nondiscriminatory treatment by a 1960 law and Chile's foreign investment law (Decree Law 600). Foreign banks can engage in the same range of activities permitted domestic banks. Lending limits are based on a foreign branch's local capitalization, rather than the worldwide capital of its parent.

As of year-end 1997, one private Chilean bank, the Banco de Chile, had a branch office in New York, a state agency in Miami, and a representative office in Frankfurt. Banco de Santiago has

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applied to establish a federal branch and a state agency in the United States. Other private Chilean banks had representative offices in Buenos Aires, Sao Paulo, Caracas, Mexico City, and Hong Kong.

### *DESCRIPTION OF THE MARKET*

#### **Structure of the Market**

As of year-end 1997, 29 banks and three finance companies were operating in Chile; total banking system assets were US\$105.2 billion.<sup>1</sup> Domestic Chilean banks have varying patterns of ownership. The one state-owned bank, the Banco del Estado, accounted for 12 percent of loans and 15.6 percent of deposits. Some of the 11 private Chilean banks are controlled by Chilean families with other commercial and industrial interests. Others are owned in part by banks or firms from the United Kingdom, France, Italy, the Netherlands, Canada, and Spain. Shares of most private Chilean banks are traded on Chilean stock exchanges, and four are traded on the New York Stock Exchange. The 17 foreign banks operating in Chile include six U.S. banks (35 branches) and branches or subsidiaries of banks from Spain, Brazil, Argentina, the Netherlands, France, Japan, and Hong Kong.

The Banco del Estado concentrates on providing services to the public sector and savings accounts to small individual savers. It is not seen as a major direct competitor to the commercial banking system. Private banks handle nearly all corporate business within the banking sector. Three "financieras," roughly equivalent to consumer finance companies, concentrate on consumer business and are not allowed to offer checking accounts or handle international business.

Corporate lending is focused on medium-sized businesses. Until early 1994, banks were prohibited from lending more than 5 percent of their assets on an unsecured basis to a single customer, so firms wanting to borrow larger amounts resorted to international sources of finance. A new banking law passed in late-1997 established a variety of specific collateral criteria for lending in excess of this general limit, such as for export and public works projects.

Chile's rapid economic growth throughout this decade has permitted increased financial activity and healthy bank profits – the volume of loans and deposits both doubled in the four years through December 1997, and banking system assets grew in nominal terms by 25 percent in 1997. Loan quality has improved as a result and at the end of 1997, delinquent loans were near the historic low point and stood at 1.0 percent of total loans. However, higher interest rates may increase the amount of non-performing loans.

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<sup>1</sup> Asset figure not adjusted for futures operations, checks in clearance, and adjustment/control accounts.

A new banking law, passed in November 1997, substantially enhanced the prospects for new banking activity in Chile. Since the financial crisis of the early 1980s, Chilean authorities had considered Chile "overbanked" and allowed no new banks, foreign or domestic, to enter the market except through the purchase of existing banks; several foreign banks entered the Chilean market in this manner. In addition to stipulating objective parameters for allowing new banks to enter the Chilean market, the new law also substantially expands the types of activities in which banks may engage. Under this law, Chilean and foreign banks may establish subsidiaries for securities and insurance brokerage, leasing, and factoring. (Branches may also engage in leasing and factoring.) Chilean banks also are now permitted to engage in banking business overseas, through cross-border lending, the establishment of branches and by directly investing in foreign affiliates. Many of the regulations for effecting the changes embodied in the new law were still pending as of mid-1998.

Automatic teller machines are provided by a network of 17 private banks. As U.S. banks concentrate on corporate lending, there are only two U.S. banks that participate in the network. However, foreign banks are afforded the same treatment for offering ATM services as domestic institutions. As of mid-1998, the number of ATM cards in use was estimated at almost 2.8 million and there were almost 1,600 machines operating in the country; in 1997, the number of transactions recorded on the system totaled 101.4 million.

Bank credit cards are managed by a separate network of 13 private banks. At the end of 1997, over 2.2 million credit cards were being used in Chile; the number of cards in use had almost doubled in a period of four years. In the final quarter of 1997, spending using bank credit cards totaled almost US\$450 million. Retail stores make up a significant part of the credit card business, and a department store is actually Chile's largest issuer of credit cards (by number of cards). Debit cards were introduced into the Chilean market in 1995; in 1997, transactions using this type of instrument amounted to US\$11 million.

Banks trade foreign exchange in the official foreign exchange market. Since mid-1992, banks and other local firms have been allowed to trade currency and interest rate futures. The volume of these transactions on the Santiago Stock Exchange is small; the off-exchange trading volume is not known.

### **Regulatory Structure**

The banking sector is regulated by the Superintendency of Banks and Financial Institutions, an agency that reports to the Finance Minister. The Central Bank, in conducting monetary and exchange rate policy, also regulates bank operations. The new banking legislation passed in 1997 implemented Basle capital adequacy standards in Chile. The Superintendency establishes a differentiated maximum lending rate, the "tasa maxima convencional," for various categories of loans made by financial institutions. The Central Bank and the Superintendency both regulate derivatives trading.

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Under the new banking law, 100 percent of sight deposits and long-term savings accounts for both domestic and foreign banks are guaranteed. Ninety percent of the value of bank time deposits are also guaranteed, for both domestic and foreign banks, up to a limit of approximately US\$3,400 per individual depositor.

In April 1998, the Federal Reserve Board of the United States, the U.S. Comptroller of the Currency, and the Chilean Superintendency of Banks and Financial Institutions entered into a cooperation arrangement. The regulatory authorities agreed to exchange information concerning applications filed for establishing banking business in Chile and the United States, as well as material information relevant to banking supervision, subject to each country's disclosure restrictions.

### ***U.S. PRESENCE IN THE MARKET***

Six U.S. banks operate in Chile through 35 branches. Most U.S. banks have concentrated on corporate lending, although a few U.S. banks have significant retail banking businesses. Several have established securities subsidiaries that have no formal connection to their Chilean banking branches.

Chilean branches of U.S. banks in general have not been highly profitable compared to private Chilean banks. U.S. banks generally show more dollar assets than obligations and more peso obligations than assets which, due to the real peso appreciation that has taken place over the past several years, led to losses as most head offices require that local capital be hedged in dollars. These losses of Chilean branches are balanced by corresponding gains of U.S. parent firms, which have balancing surpluses of dollar obligations and peso assets. This phenomenon appeared to reverse in early 1998 as U.S. banks substantially outperformed Chilean banks due largely to a lack of market liquidity and subsequent dollar appreciation.

### ***TREATMENT OF U.S. FINANCIAL INSTITUTIONS***

Foreign banks are allowed to establish either as branches or subsidiaries, but the Bank Superintendency appears to prefer branches because the legal liability of a foreign branch extends to the parent institution. All U.S. banks in Chile are considered branches by their home offices and Chilean law. However, they have the subsidiary-like characteristic of being subject to lending limits based on local capital.

Foreign banks are permitted the same range of activities as domestic banks, including issuance of credit cards and the offering of ATM services, and may fund themselves through deposits as do domestic banks. Foreign banks also can establish securities subsidiaries that have no formal connection to their Chilean banking operations to carry out these activities.

Foreign banks can trade foreign exchange through the official exchange market. However, Chile retains some controls on international movement of capital. One measure discouraging inward flows, particularly of short-term capital, is a reserve requirement on all credit inflows except direct supplier credits. Under this measure, firms are required to deposit an established percentage of the inflow in a non-interest-bearing reserve account for one year, or pay the Central Bank a tax equivalent to the interest that would be foregone. (However, the percentage rate was lowered from 10 percent to zero in September 1998.) These capital restrictions apply to domestic and foreign firms equally under the law, but their removal probably would benefit foreign, including U.S., banks disproportionately because foreign banks' international networks are stronger than those of Chilean banks. Foreign banks can fund themselves through deposits.

Chilean regulatory practices are generally transparent. U.S. bankers contacted for this report did not express any complaints about regulatory transparency.

Chilean Banking System (Shares of Deposits and Loans by Type of Institution)				
Type of Institution	Number of Firms	Number of Branches	Percent of Deposits	Percent of Assets
Domestic Private Banks	11	742	62.1	54.8
Banco del Estado	1	204	15.6	10.9
Foreign Banks*	17	220	18.3	32.5
<i>of which: U.S. Banks</i>	6	35	4.2	16.2
Consumer Finance	3	159	4.0	1.8
TOTAL	32	1325	100.0	100.0

\*At least 51 percent foreign ownership. Figures are as of December 1997.

Source: Superintendency of Banks and Financial Institutions.

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### U.S. Commercial Banks' Share of the Chilean Market as of December 31, 1997

Bank	Percent of Deposits	Percent of Assets
Citibank	2.6	3.8
Bank Boston	0.7	5.0
Republic National Bank	0.5	0.6
Chase Manhattan	0.3	3.5
American Express	0.2	0.8
Bank of America	0.0	2.4
TOTAL	4.3	16.1

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Source: Superintendency of Banks and Financial Institutions