How local conditions affect global banking: the case of BBVA and Santander*

● Joaquim Cuevas
Universitat de València
● Pablo Martín-Aceña
Universidad de Alcalá
● Maria A. Pons
Universitat de València

Introduction

Since the 1990s, Banco Bilbao Vizcaya Argentaria (BBVA) and Banco Santander have undergone a remarkable transformation: they have gone from being two of Spain's largest banks to two of the world's biggest. The aim of this paper is to explain why Latin America has been the main region for the international expansion of the two banks. Although we focus on the period of major internationalisation occurring from 1990 onwards, the main contribution of this paper is to offer a long-term perspective to study the previous history of internationalisation, the roots of this expansion, and the main changes occurring in the 1990s that encouraged the internationalisation process of both banks. This paper argues that the timing of changes in the Spanish and Latin American financial sectors that took place, just when other transnational banks were focusing their attention on other regions, created the optimal conditions for the natural but also unexpected (in term of size and scope) expansion of BBVA and Banco Santander in the region.

* This paper received financial support from the Spanish Ministry of Economy and Competitiveness ECO2015-66782-P and the Generalitat Valenciana AICO/2018/130. Previous versions of this paper were presented at the XVIII World Economic History Congress 2018 (Boston), the Business History Conference 2019 (Cartagena de Indias) and FARECES Seminar "Los orígenes de la globalización bancaria en España y sus posiciones actuales". The authors are particularly indebted to all the participants for their comments and suggestions.

Fecha de recepción: marzo 2020
Versión definitiva: octubre 2020

Revista de Historia Industrial
N.º 81. Año XXX. 2021

In the analysis of multinational banking expansion there are different types of factors governing the scope of the internationalisation process, the choice of location, the type of activities of the bank in the host countries and the strategy used in the internationalisation process. On the one hand, there are some bank-specific characteristics (or internal factors) linked to its size, such as ownership structure, organisational and managerial capabilities, corporate policy, human capital endowment, technological development, and business culture. On the other, internationalisation depends on the economic, political and institutional environment (external factors) of the host country, and also on conditions in the home country: in particular, the level of economic development, and regulations in the financial sector.

In this paper, the focus is placed in the role played by the forces behind the Spanish banking internationalisation process. Taking a long-term perspective, the paper considers the different hypotheses that may have affected the pattern and timing of Spanish banks' entry into the Latin American region. For instance, the role of emigrant remittances and the economic links through trade and FDI, both taken as proxies for the "follow the client" approach. Other factors are the local opportunities existing in the Latin American region, and changes in host country regulations. The paper also discusses how the banking and debt crisis in some Latin American countries during the 1980s and 1990s affected domestic banks and multinational banks and how this situation was exploited by the Spanish banks. Domestic factors such as changes in Spanish regulations and the evolution of competition in the financial sector are also considered.

The structure of the paper is as follows. Section 2 presents the main factors identified in the literature as drivers of bank internationalisation. Section 3 explains why the Latin American region is the natural choice for the Spanish banking sector's expansion, while Sections 4 and 5 discuss the different historical phases and features of BBVA's and Santander's expansion. Although the Latin American geographical area seems to be the natural choice for Spanish banks' internationalisation, the main forces behind the expansion are explored. Section 6 briefly discusses the strategy of Spanish banks as compared to other transnational banks, and the conclusions are presented in Section 7.

Why do banks internationalise?

When examining banking internationalisation, it should be noted that financial products have different characteristics from manufactured products. For example, financial services and products are information intensive. In order to evaluate their operations, banks need to collect abundant data about their clients/customers and the conditions of the local markets. A national bank that decides to expand into foreign countries faces costs related to its cultural, political, fiscal and economic setting. It means that it has less knowledge about the host market than the local competitors do. Inversely, expanding abroad has a number of advantages that have been often cited in the literature. The first is that it enables banks to grow beyond the limits of the home market, and achieve economies of scale and scope (Tschoegl, 2004). As Grubel (1977) suggests, banks not only try to serve their corporate clients/customers that move abroad in search of new business (the "follow the client" motive),[1] but also to go beyond their national boundaries to capture new clients in countries with underdeveloped financial systems and a low level of financial intermediation (an offensive expansion). Furthermore, opportunities to grow in relatively uncompetitive markets are larger than those that can be obtained in well-developed financial markets (Calzoni and Loranth, 2011). Banks seek out new markets that are more profitable or offer higher margins (Aliber, 1976). Moreover, there is a two-way relationship between size and internationalisation: banks expand into other countries in order to grow; and large banks are much more international than small ones (Focarelli and Pozzolo, 2005). The second advantage is risk diversification. Banks attempt to diversify their portfolio, and use foreign markets to compensate for the fluctuations in their home markets. Thirdly, internationalisation allows banks to exploit the resources and capabilities that they have developed in their local markets in new emerging markets, at a relatively low cost (Mulder and Westerhuis, 2015). Moving abroad helps banks to respond to the challenge of domestic rivals, and in this case, internationalisation strategies depend upon the behaviour of competitors (Grubel, 1977). Lastly, a common language and cultural similarities between the home and the host countries reduces information costs and facilitates business interactions (Cull and Martínez Peria, 2010).[2]

As mentioned, the motives for banking internationalisation include external conditions as well as internal conditions. Saturation of domestic demand, local regulatory restrictions or, alternatively, financial deregulation processes that increase competition push banks to internationalise. Otherwise, there are certain elements that act as pull factors, such as capital account liberalisation, financial deregulation, falling communication costs, financial innovation, and

1. As Cull and Martínez Peria (2010) indicate, the "follow the client" approach is the desire of the bank to continue serving its clients in their overseas operations.

2. Cultural ties such as language and psychosocial or cultural proximity are determining factors in good business understanding. A common language reduces transaction costs, but also facilitates the organisational cost of a firm in the internationalisation process due to the reduction in the cost of information or technological transfer and facilitating employee's mobility. It also reduces the psychological distance with which entrepreneurs face their exit to foreign markets, particularly in the initial stages (Jiménez and Narvona, 2010).

trade and financial integration (Berger et al., 2001).[3] Previous experience in foreign markets may also serve to accumulate knowledge and capabilities for future expansions abroad.

Empirical research about the main drivers of banking internationalisation finds that the size of the home country and its level of economic and financial development are two key determinants of banking internationalisation: countries which have a more saturated home market and which have made the most progress in financial development have a higher level of banking internationalisation (Lane and Milesi-Ferretti, 2008; Mulder and Westerhuis, 2015). Other non-economic aspects, such as linguistic and cultural similarities, are also correlated with the internationalisation pattern of banks (Buch, 2003; Focarelli and Pozzolo, 2005). The internationalisation process is also influenced by certain characteristics or internal factors related to the size, efficiency and performance of the banks that expand abroad (Clark et al., 2003).[4]

Most of the research on the factors that encourage banks' entry into foreign markets is based on cross-country evidence and shows that economic, political and regulatory conditions are crucial to an understanding of the pattern and timing of banking internationalisation.[5] However, although the advantages of cross-country analysis are evident, it is also important to consider some specific case studies to contrast whether the general conclusions stemming from cross-country analyses hold true for a specific case study.

The internationalisation of Spanish banks: Latin America as the "natural" choice for foreign expansion

In order to study the timing and drivers of Spanish banking expansion, we differentiate between the pre- and post-1986 periods. This chronology is similar to that of foreign direct investment (FDI). Following Durán (1997, 2005), Spanish FDI began after the 1959 Stabilisation Plan, but increased thereafter during the sixties and seventies. Although limited in volume, it already had two main features that were later repeated. First, the predominance of Latin America as the main investment destination, followed by Europe

3. For the most recent globalisation period, Lane and Milesi-Ferretti (2008) highlight the creation of monetary unions such as the euro area as a factor driving international banking expansion.

4. Several studies have found a positive correlation between bank size (as a proxy of resources available to expand abroad) and internationalisation (Tschoegl, 1983; Grosse and Goldberg, 1991, and Focarelli and Pozzolo, 2005). Fuentelsaz et al. (2002), however, pointed out that large organisations may also be more rigid or inflexible and suffer from bureaucratic inertia that complicate banking expansion.

5. Barth et al. (2001) ; Clarke et al. (2003); Cerutti, Dell'Ariccia and Martínez-Peria (2007).

(Durán 2005). Second the significant weight of investment in banking in overall FDI.

When the expansion began after 1986, Banco Santander and BBVA underwent significant changes. Both are the result of previous mergers. In 1988, Banco Bilbao and Banco Vizcaya merged to create BBV. In 1999, BBV merged with Argentaria, a state-owned conglomerate,[6] to form BBVA. Banco Central and Banco Hispano merged in 1991 to create BCH. Three years later, in 1994, Banesto, which had been subject to an intervention by the Bank of Spain after experiencing difficulties, was sold to Banco Santander. In 1999, Banco Santander merged with BCH to create Banco Santander Central Hispano (BSCH), which changed its name in 2007 to Banco Santander.

In our empirical analysis of the factors that have encouraged the international expansion of Santander and BBVA, the focus is on: a) the economic integration between the home (Spain) and the host countries as a proxy for the "follow the client" approach. In particular, we analyse the influence of emigrant remittances, trade and Spanish FDI; b) the bank characteristics that affect their expansion decisions, in particular, size and profitability; c) the changes in regulations in the home country and their consequences for banking structure and competition; d) the economic and financial changes in the host countries (including banking and debt crises and their consequences); e) the profit opportunities in the host countries; f) the host country regulations, and g) other factors that could affect the pattern of expansion, such as a common language or cultural similarities. As we show in the next section, Spanish banking internationalisation was a dynamic process motivated by multiple domestic and external factors (economic, political and regulatory) that made Latin America the main region for Spanish banks' expansion. Moreover, the impact of the debt crisis on domestic banks but also on other competitors (US, British and German banks) left Spanish banks with enough space to move into the region.

Before 1986: the initial phase

In the pre-1986 period Spanish banks had a limited presence abroad. They extended their overseas activities through representative offices, but these offices did not deal directly with local clients; the volume of investment was low, they took small risks, and the profits linked to their foreign operations did not mean a substantial share of their total profits.

6. Argentaria was the bank created in 1991 from the merger of all stated-owned banks, with the exception of the Bank of Spain: namely, Banco Hipotecario de España, Banco Exterior de España, Banco de Crédito Industrial, Banco de Crédito Agrícola, Banco de Credito Local and Caja Postal (Martín-Aceña, Blasco and Cuevas, 2016).

Why did Spanish banks not adopt a more vigorous international strategy during this period? There are a number of potential explanations. Firstly, internal conditions did not favour overseas expansion. After the Civil War, the banking sector had barriers to entry, was strictly regulated, and competition was restricted. Banks enjoyed high rates of profitability and therefore had little incentive to look for new markets (Pons, 2002; Pueyo, 2003).[7] Hence, until the 1980s, the domestic, regulated environment discouraged foreign banking expansion.

Secondly, the small size of Spanish firms prevented early international expansion (see Table 1).[8] Only when banks reached sufficient size did they have enough financial resources to operate abroad. However, the most internation-

TABLE 1 ▪ *Spanish banks and European and American banks: a comparison, in million USD*

	1953	1960	1975
Spanish banks			
Banco Hispano Americano	0.492	1,110	13,006
Español de Crédito	0.362	1,550	13,869
Vizcaya	0.159	0.589	8,339
Bilbao	0.207	0.595	12,179
Central	0.175	0.835	14,149
Santander	0.047	0.415	6,654
European and American banks	**1953**	**1960**	**1974/1975**
Credit Lyonnais	1,243	2,616	32,972
Societe Generale	1,069	2,285	27,211
Deutsche Bank	2,295	2,690	20, 210
Commerzbank	0.381	1,640	17,682
Bank of America	7,022	11,200	64,272
Citibank	6,026	8,160	60,994
Chase	5,574	8,420	41,713
Barclays	4,142/6,064	5,182/7,463	33,108
Lloyds	3,745	5,033	20,882
Midland Bank	4,264	5,103	23,179
Westminster Bank	2,641	3,809	31,680

Source: For Spain, *Anuario Estadístico de la Asociación Bancaria Privada*; for the major European and American banks in 1953 and 1960, Cassis (2002); for European and American banks in 1974/75, Paxton (1976).

7. The average rate of profitability of Spanish banks in nominal terms between 1960 and 1975 was around 20 per cent, nearly 12 per cent in real terms (Pueyo, 2003).

8. See Canals (1991), and Cardone-Riportella and Cazorla-Papis (2001). For instance, in 1985, the largest bank in Spain (Banco Central) ranked 100th in the world and was about one-fourth the size of Deutsche Bank (Guillén and Tshoegl, 2008).

alised institution, Banco Santander, was small in comparison to other larger (and less internationalised) banks such as Banco Hispano Americano, Español de Crédito, Banco Bilbao and Banco Central.

External conditions did not stimulate Spanish banking investment overseas either. Until the 1980s, most of the potential host countries (such as those in Latin America) had high barriers to entry that deterred foreign investment (Table 2). Although in the last decades of the nineteenth century and the first decades of the twentieth century, foreign banks had a strong presence in the region, particularly in Brazil and Mexico, the situation changed after the Great Depression. In Mexico, for example, following the revolution, and also as a consequence of the First World War and the monetary instability of the 1920s, there was an increase in risk and a decline in banking profitability that led foreign stockholders to lose interest in the country's business. Moreover, the situation deteriorated after the 1931 Banking Law, which subjected foreign commercial banks to severe legal constraints (Marichal and Trainer, 2001). In fact, from 1931 to 1981, there were virtually no foreign banks in Mexico, with the exception of Citibank, the only survivor of the foreign banks installed during the Porfiriato (Del Angel, 2007). This situation was also typical in many other Latin American countries, which, from the 1940s until the 1980s, had very interventionist banking regulations. This high level of interventionism can be framed as part of the ISI strategy of growth adopted in the region. In this period, and especially from 1950 to 1980, the state assumed a new economic role in intervening, protecting and promoting commercial banks, setting interest rates and controlling their operations so that financial institutions channelled funds to priority sectors selected by the government (Bértola and O'Campo, 2010).

Moreover, until the 1990s, and as part of the ISI strategy, the state-owned banks in Latin America held more than 50 per cent of total banking assets (Tovar, 2007).[9] In Brazil, the banking system was nationalised during the 1920s, after which time the activity of foreign banks was limited (Cortés and Marcontes, 2016). Other countries nationalised banks as well during the 1940s, such as Argentina in 1946 or Costa Rica in 1948. Later in the 1980s, there was a new wave of nationalisations, such as those in El Salvador (1980-1990), and Mexico (1982-1990) (Del Angel and Martinelli, 2013). Given this extremely restrictive government regulation and the strong presence of state-owned banks,[10] the incentives for foreign institutions to enter the region were

9. However, there were substantial differences among countries. For example, whereas in Brazil the share of state-owned banks in 1994 was 48 per cent, in Chile it was only 14 per cent (Goldstein and Turner, 1996).

10. There was also an attempt to nationalise the banking sector in Peru (1987) but it was declared unconstitutional (Machuca, 2017). In other countries there were short periods of nationalisation, such as that in Chile between 1970-73, and 1981-82, and in Venezuela in 1995 as

TABLE 2 ▪ *Banking regulation in LatAm countries*

	1930s	1960s	1980s
Mexico	Very restrictive (1931 Banking Law, severe constraints on foreign banks)	Very restrictive	Very restrictive Banking nationalisation 1982
Brazil	Very restrictive (1920s reforms that nationalised the banking system)	Very restrictive	Restrictive (1988 Banking Law eliminated entry barriers)
Argentina	Very restrictive (1946 Decree, nationalisation of bank deposits)	Restrictive (timid liberalisation reform in 1957) Less restrictive (1969 Banking Law that attracted foreign capital to the banking sector) Very restrictive (1973 Law, nationalisation of bank deposits) Restrictive (1977 reform that promoted liberalisation)	Restrictive
Chile	Restrictive. Kemmerer mission in 1925, creation of the Banco Central (central bank) with members of foreign banks on its board of directors	1970-1973: banking nationalisation 1975-1976: first banking privatisation	1981-1982, nationalisation of banks in difficulties 1985: second wave of privatisation 1986 Banking Law (prudential regulation)
Colombia	Kemmerer mission in 1923, creation of the Banco de la Republica (central bank)	Very restrictive (strong state intervention in the credit market and interest rate controls)	Restrictive (1985 Financial Institutions Guarantee Fund to reorganise the banking sector)

Sources: For Mexico, Marichal and Triner (2001); for Brazil, Cortés and Marcondes (2016); for Argentina, Rapaport (2010) and Jones (1995); for Chile, Drake (1984) and Gozzi and Tappatá (2010); for Colombia, Forero-Laverde (2017), Kalmanovitz (2010), Ocampo (2015), and Gozzi and Tappatá (2010).

weak. Hence, the financial repression that characterized many Latin American nations prevented not only the establishment of international banks but also the development of competitive financial markets. Zegarra (2014) argues

a consequence of the banking crisis, but Venezuelan banks were re-privatised in 1996 and 1997 (De Krivoy, 2003).

that the low level of development of the Latin America financial system and the minimal presence of foreign banks in this region was also due to the low demand for banking services (Table 3). This feature also explains why those foreign banks that operated in countries such as Brazil operated in the wholesale market (Paula, 2010). The economic and political instability of this region throughout most of the period may also have been a limiting factor for Spanish banks, in particular the economic difficulties of the 1970s and the "lost decade" of the 1980s (Batiz-Lazo et al., 2008). There were systemic banking crises in Argentina, Chile, Colombia and Uruguay, as well as in Ecuador, Bolivia and Mexico (Morris et al., 1990). However, it is also true that, as we will examine in the next section, the difficulties of both domestic and multinational banks during the Latin America debt crisis were successfully exploited by Spanish banks in the second half of the 1980s and in the 1990s.

TABLE 3 ▪ *Financial system deposits to GDP (%)*

	1960	1970	1980	1985
Argentina	13.2	18.2	23.6	13.5
Bolivia	1.6	5.7	9.4	1.7
Brazil	15.2	15.0	15.5	17.3
Chile	5.2	9.5	18.9	23.7
Colombia	13.8	14.4	19.3	25.0
Costa Rica	12.5	13.3	29.6	30.8
Dominican R.	11.2	12.2	18.9	17.5
Ecuador	8.4	13.1	12.7	10.9
Mexico	17.8	25.0	23.2	14.1
Peru	16.0	15.2	12.5	15.1
Spain	49.0	59.4	63.7	54.2

Source: Demirgüç-Kunt, Čihák, Feyen, Beck and Levine (2018).

Despite the above-mentioned obstacles, prior to 1986 Banco Santander had a significant presence in Latin America. The founding of Banco Santander in 1857 involved local merchants and businessmen that had trade connections with America. However, the bank had modest beginnings and a conservative policy approach, concentrating its activity in Spain rather than overseas (Martín-Aceña, 2010). It was not until the 1940s that turned its attention to Latin America. Table 4 shows that the bank increased its activity in the area during the 1970s,[11] and then was forced during the 1980s to restruc-

11. Dominican Republic in 1976, Costa Rica in 1977, Guatemala in 1977, Puerto Rico in 1977, Ecuador in 1979 and Uruguay and Chile in 1979.

ture its presence.[12] In the pre-1986 period, the bank concentrated its activity in Puerto Rico, Chile and Panama. In contrast with Santander, BBVA hardly had a significant presence in Latin America.[13]

TABLE 4 ▪ *Spanish banking expansion in LatAm, 1900-1986*

Banco Hispano Americano(1)	Banco Santander	Banco Bilbao and Banco Vizcaya
1902 Cuba (B)		
1903 Argentina (A), Banco de Comercio		
1905 Argentina (A), Banco de la Provincia de Buenos Aires		
1910 Argentina (A), Banco Hipotecario		
	1947 Cuba (A, RO), Trust Company	
	1951 Mexico (A) Banco Internacional de Mexico	
	1956 Mexico (RO)	
	1957 Brazil (A, RO), Banco Intercontinental de Brasil Venezuela (RO)	
1962 Venezuela (RO) Mexico DF (RO)		
	1963 Argentina (A), Banco Hogar Argentino	
1966 Buenos Aires (RO) Rio de Janeiro (RO) Bogotá (RO) San José (RO)		
	1967 Argentina (A), Banco Mercantil de Rosario y Santa Fe and Banco Comercial e Industrial de Cordoba Panamá, Banco Santander y Panamá	

(Continued on next page)

12. In the early 1980s, Santander reconsidered its investments in LatAm and it sold its affiliates in the Dominican Republic (1985), Ecuador and Guatemala (1986), El Salvador and Panama (1987). By contrast, it maintained its presence in Chile and Uruguay and consolidated in Argentina (Guillen and Tschoegl, 1999, 2000 and 2007).

13. With respect to Banco Hispano Americano (which later merged with Banco Santander), although its deed of constitution (1900) indicated that the aim of the bank was to finance Latin American trade, and it opened some branches and made some agreements with local banks in Cuba and Argentina at the beginning of the twentieth century, the bank stopped its international expansion after 1923. It was not until the 1960s that the bank opened some offices in Venezuela, Mexico, Argentina, Brazil, Colombia, Costa Rica and Peru (see Tortella and García Ruiz, 1993, and Table 1).

Banco Hispano Americano(1)	Banco Santander	Banco Bilbao and Banco Vizcaya
1969 Peru (RO)	**1969** Argentina (RO)	
	1976 Dominican Republic (A), Banco Condal Dominicano	
	1977 Puerto Rico (A), First National Bank of Puerto Rico Costa Rica, Banco Santander Costa Rica Guatemala (A), Banco Inmobiliario Guatemala	
	1978 Puerto Rico (A), Banco de Crédito y Ahorro Ponceño	
	1979 Chile, Banco Santander Chile Ecuador (A), Sociedad General de Crédito, Ecuador Uruguay, Casa Bancaria Santander	**1979** Puerto Rico (A), Banco Comercial de Mayagüez[2]
	1982 Chile (A), Banco Español Chile Uruguay (A), Banco del Litoral Asociados	**1982** Puerto Rico (A), Banco Occidental
		1983 Panamá (B)

B: branch, A: banking agreement with a local bank or acquisition of a local bank, RO: representative office. (1) In 1991, Banco Hispano Americano and Banco Central merged to create BCH and in 1999 Banco Santander merged with BCH to create BSCH, which changed to Banco Santander in 2008, (2) Banco Occidental acquired Banco Comercial de Mayagüez in 1979 and in 1982 Banco Vizcaya acquired Banco Occidental.

Sources: Banco Hispano Americano: Tortella and García Ruiz (1993); Santander: Martín-Aceña (2008), Martín-Aceña (2010); Banco Bilbao and Banco Vizcaya: Arroyo, Larrinaga, and Mates (2012).

An open question is whether the main drive of banks' internationalisation in this period was to provide services to their clients overseas. To analyse the "follow the client" motive, we consider the importance of emigration, trade conditions and FDI. Remittances sent home by Spanish emigrants were significant since 1900, especially to Argentina, Brazil, Cuba and Uruguay. The flow of emigration dried up during the First World War, though later resumed at a high pace (Sánchez Alonso, 1995). After the Civil War, migration for political reasons (the migrants known as *exiliados*) reached a significant number and chose mainly Mexico, the Dominican Republic and Chile (Abellán, 1983).[14] There was also a new wave of emigration to Latin America from 1946 to 1958, this time motivated by economic conditions, with Argentina (35.1 per cent of total migrants) and Venezuela (32 per cent) being the most attractive destinations, followed by Brazil (10.9 per cent). The

14. Mexico was the country that received the most *exiliados*, with more than 21,000 migrants between 1938-1948. Other traditional emigration destinations such as Argentina, Cuba, Brazil and Uruguay were reluctant to accept Spanish refugees, although Argentina also took in a substantial number (Sallé, 2009).

total number of migrants in this period was estimated at more than 560,000 (Sallé, 2009).

As a consequence of these flows of migrants, remittances from Latin America may have been a major factor for the establishment of Spanish banks in the region, although unfortunately quantification of their operations is plagued with difficulties (Sierra, 2007). However, we have some, in particular for Banco Santander (Martín-Aceña, 2007). Emilio Botín, the president, made his first visit to the Americas in the 1940s, where he realised that servicing the Spanish expatriate communities could be a promising business niche (Acta Banco Santander 7/09/1955).

Emigrants were also important clients for Banco Hispano Americano, channelling almost 500 million pesetas per year before 1913 (Tortella and García Ruiz, 1993). The bank's main presence was in Argentina, the primary destination of Spanish migrants before the First World War. The Banco Santander had agency presence in all the countries with high immigration rates, except in the River Plate capital.

Another possible determinant of financial expansion is trade integration. As Lane and Milesi-Ferretti (2008) indicate, trade openness and financial integration go hand in hand. Until the 1960s, Spain was a closed economy and the low level of commercial integration did not stimulate foreign banking activity. Although Spanish banking investments abroad were concentrated in Latin America from 1900 to 1984, the region's share of total Spanish trade fell in comparison to other regions (Table 5). As mentioned, Spanish banks, such as Banco Hispano Americano and Banco Santander, were linked to Latin America providing finance to *indianos*, the name given to those Spaniards who made their fortune across the Atlantic (Tortella and García Ruiz, 1993). As can be seen in Table 5, the area's share of total trade remained fairly steady

TABLE 5 ▪ *Trade with Spain by regions (exports and imports), 1900-1984 (% of total Spanish trade)*

Exports	1900/04	1931/35	1951/55	1980/84
Europe*	77.00	66.54	50.13	48.86
US	2.50	8.11	12.13	7.20
LatAm	11.50	8.96	10.90	5.23
Imports	**1900/04**	**1931/35**	**1951/55**	**1980/84**
Europe*	56.80	39.89	40.20	31.39
US	11.80	16.67	17.06	12.59
LatAm	3.70	6.86	7.32	11.24

Note: (*) Europe includes Belgium, Holland, Luxembourg, France, Italy, the United Kingdom, Germany and Portugal. *Source:* Tena (2005).

over the pre-war period, but then fell in the second half of the twentieth century. Thus, we cannot claim a clear correlation between trade and the presence of Spanish banks in the Latin America.

Although from a macroeconomic perspective there is no available evidence on the influence of trade on banking expansion in Latin America, a few institutions engaged significantly in the region. For example, Marichal (2017) points out that financing commerce was a special business area for Banco Hispano Americano*,* which became a key financial link between Spain, Cuba, Mexico and Argentina, though there is little evidence of how Spanish banks helped Spanish exporters in their trade with the region.

As mentioned, FDI can also drive banks' location, that is, accompanying other multinational firms in their expansion abroad. However, in this period Spanish firms had a scarce presence in foreign countries. As Chislett (2003) has shown, during the 1960s the Spanish FDI only represented 0.1 per cent of total international FDI, and it was also below the 0.1 per cent of the GDP (Guillén, 2004).[15] Then, the main destinations of Spanish firms were some European (CEE) countries, together with Mexico, Argentina, Chile and, to a lesser extent, Brazil. The percentage increased to 0.3 per cent of total FDI in the 1970s. The rise was due to firms increasing their presence in the Caribbean (Puerto Rico), Central America (Panama), and South America. All in all, the three regions represented a 47.1 per cent of total Spanish FDI in 1963-1978 (Vidal, 2008). The expansion, however, was not led by the banks such as Banco Bilbao and Banco Vizcaya with a substantial industrial portfolio.[16]

After 1986: the great expansion

The FDI boom of Spanish companies occurred after Spain's entry into the then European Economic Community, and more especially during the so-called golden decade, 1990-2000 (Durán, 2005; Casilda, 2002; Serrano, 2013), with Latin America the main destination of these investments (Chislett, 2003; Casilda, 2002; Cuenca, 2001). The improvement of the Spanish economic situation since the mid-1980s, along with the institutional transformations in Latin America, led to a substantial increase in investments by Spanish firms

15. As Guillem (2004) indicates, the Spanish government did not facilitate the FDI of Spanish firms in this period. The rigid exchange rate controls and lack of effective aids to facilitate the creation of distributive channels in foreign markets are, among other factors, behind this low FDI rate.

16. At the end of the 1960s, Santander was not so interlocked with industrial firms as other Spanish banks. In fact, Santander's board members were involved in 179 interlocking boards of industrial firms in contrast to 478 for Banco Bilbao, 463 for Banco Vizcaya and 390 for Banco Central (Guillem and Tschoegel, 2008).

in the region. The economic openness of the countries of the subcontinent, combined with programmes of privatisation and the deregulation of public services, attracted Spanish FDI. Chronologically, there were two breaking points: 1988 and 1997, and by 1998-1999 the outflows exceeded the inflows. FDI growth was also accompanied by sectoral changes: from the predominance of banking and insurance to an equivalent role for transport, communications, energy and oil.

Spanish firms' expansion took advantage of the liberalization of services in which private investment had previously been absent or marginal. The first large investments were made by Telefónica in Argentina, Chile, Brazil, Perú, Puerto Rico and Venezuela (telecommunications services with high potential for growth). In energy (electricity generation, transmission and distribution), the lead was taken by Endesa, Iberdrola and Unión Fenosa. Spanish banks also took advantage of the opportunities following the deregulation of local markets by purchasing local firms, although they made large investments in technology as well. Spain's FDI in the region grew to a peak in 1998-2001. A large part of these investments was in the financial sector: between 1997 and 2002 BBVA paid $7.8 billion for 34 acquisitions, and Santander paid $12.3 billion for the purchase of 27 local banks (Batiz-Lazo et al., 2008). If we extend the timeline to the decade of greatest disbursements (1993-2003), the investment of Spanish banks rose to 52 billion euros, to which we should add 2.3 billion euros in insurance and pension funds, and another 1.5 billion in other intermediation activities. Some 40% of these amounts went to Latin America (Rodríguez, 2004).

From the mid-1980s, the Spanish banking sector experienced profound changes. These transformations boosted its internationalisation process: the total assets of Banco Santander in Latin America increased from 2.7 billion dollars in 1985 to 50.3 in 1999 and to 141.9 billion in 2007. In the case of BBVA, assets more than doubled from 0.43 billion in 1999 to 100.2 billion in 2007. Both began their international expansion in this period, after having consolidated their positions in Spain and completed a process of mergers that allowed them to achieve the size they needed to expand abroad. Both also adopted a strategy of entry via acquisition rather than via greenfield operations. The main difference between the two was that Banco Santander took majority stakes in the banks in question, with the objective of ensuring full managerial control,[17] whereas BBVA started with minority stakes, which it gradually increased over time (Guillén and Tschoegl, 1999). Banco Santander and BBVA have specialised in retail banking, in contrast to other foreign

17. As Guillén and Tschoegl (1999) remark, Banco Santander expanded via acquisitions and imposed their brand image, whereas Banco Central Hispano adopted a strategy based on ventures with local partners, but without promoting its own brand.

banks such as Citibank, which focus on a minority of the population: high-net-worth households and investors (Citi Report, 2017).

In the second half of the 1990s, Banco Santander, led by its affiliate Santander Investment, accelerated its expansion in Latin America. Its investments jumped from 9 per cent of total assets in 1990 to 24 per cent in 1998, representing 30.6 per cent of total profits. BBVA also achieved a major business expansion in the region in the 1990s. As will be seen in the next section, the Latin American debt and banking crises and the restructuring of the financial sectors jointly with the privatisation processes favoured Spanish banks entry. Moreover, as Paula (2010) mentions, their preference for Latin America can be explained by the instability of the Asian markets due to the 1990s Southeast Asia crisis and the impermeability of the Indian and Chinese financial markets.

The geographical pattern of Santander and BBVA locations in Latin America in the post-1986 period is shown in Table 6. Banco Santander redirected its strategy from 1986, concentrating its activity in Argentina, Brazil, Chile and Mexico, whereas BBVA's activity concentrated in Mexico, although it has also a presence in Argentina and Brazil. It is interesting to observe how Santander and BBVA show different patterns of geographical distribution, although they do compete in some countries.

The entry of Banco Santander in Brazil was related to the debt and banking crisis and government intervention to restore the financial sector that facilitated the entry of foreign banks (Paula 2010).[18] As seen in Table 6, Banco Santander purchased Banco Geral do Comercio (1997) and Banco Noroeste (1998), and later in 2000 the giant Banespa (when it was privatised). This last acquisition allowed Banco Santander do Brasil to become the third largest private bank in the country (Paula 2010). Despite the early entry of Banco Santander in the Mexican market in the early 1950s, for many years after Mexican law impeded any further investments (Table 2). The Mexican debt default and the financial sector collapse led to the nationalization of the banking sector. The re-privatisation process began in 1990 and the opening to foreign banks in 1994. In those years Santander acquired InverMexico (1997), establishing the Grupo Financiero Santander Mexicano. In 2001, thanks to the acquisition of Serfin in 1999, it created the Grupo Financiero Santander Serfin, later on Santander Mexicano, which became the third largest bank in Mexico after Bancomer and Banamex.

BBVA's biggest investment in Latin America since the 1990s has been in Mexico. The entry began in 1991, through a minority takeover in Probursa, which five years later (with tequila crisis) reached 70%. The acquisition of

18. As Carvalho (2000) explains, the banking crisis of 1995 devalued the existing banks and favoured the entry of foreign banks into the country.

TABLE 6 ▪ *Spanish banking expansion in LatAm: mergers and acquisitions, 1985-2015*

Banco Santander	BBVA
1991 Chile, Banco Santiago (A)	
1995 Peru, Banco Interandino (A) Banco Mercantil (A)	**1995** Mexico, Probursa (A) Peru, Banco Continental (A) Uruguay, Banco Francés
1996 Peru, Banco Santander Perú (Banco Interandino + Banco Mercantil) (M) Argentina, Banco Tornquist (A) Mexico, Banco Santander Mexicano Paraguay, Banco de Asunción Puerto Rico, BCH Internacional (A) Uruguay, Eurobanco (A)	**1996** Argentina, Banco Francés (A) Corp Banco Argentina (A) Colombia, Banco Ganadero (A)
1997 Venezuela, Banco Venezuela (A) Mexico, Banco Mexicano (A) Colombia, Banco Comercial Antioqueño (Banco Santander Colombia) (A) Invercrédito (A) Argentina, Banco Rio de la Plata (A) Riobank Internacional (A) Riobank Internacional Saife (A) Brazil, Banco Geral do Comercio (A) Uruguay, Banco Santander Uruguay	**1997** Venezuela, Banco Provincial Argentina, Banco de Crédito Argentino
1998 Brazil, Banco Noroeste (A) Argentina, Banco de Galicia y Buenos Aires (A)	**1998** Brazil, Banco Excel Economico (A) Chile, Banco Hipotecario (A)
1999 Bolivia, Banco Santa Cruz Mexico, Bital	
2000 Mexico, Grupo Financiero Serfin (A) Brazil, Banco Bozano Simonsen (A) Banco Meridional (A) Banco do Estado de Sao Paolo (A) Venezuela, Banco Caracas (A) Colombia, Holding increased in Banco Santander Colombia Argentina, Banco Rio + Banco Tonquist (M)	**2000** Mexico, Bancomer (A)
2002 Chile, Holding increased in Banco Santiago Banco Santander Chile + Banco Santiago (M)	
	2004 Mexico, Hipotecaria Nacional (A)
	2005 Colombia, Granahorar (A)
2006 Argentina, Banco Galicia (A)	
	2007 Chile, Forum

Sources: Martín-Aceña (2007 and 2008); Calderón and Casilda (2000). Annual reports of Banco Santander and BBVA.

small banks during those years (Banco de Oriente and Banca Cremi) led to a rapprochement with the Bancomer financial group, which was re-privatised (Del Angel, 2007). In 2000, BBVA acquired Bancomer; the following year Citibank merged with Banamex, and in 2002 HSBC acquired Bital. In 2000, BBV Probusa (which was the main shareholder of BBV-Mexico) merged with the

Bancomer financial group (the operation was completed in 2009 with the acquisition of 99.97% of the paid-up capital). Bancomer became the leader in the Mexican banking sector, with 20% of the country's banking market (Cuevas, Martín-Aceña and Pons, 2018).

The 1995 banking crisis in Argentina also favoured the expansion of Banco Santander and BBVA. The crisis was accompanied by massive capital outflows and forced the government to take drastic measures, such as the freeze of deposits. The sector was restructured and as a result the two large domestic banks, Banco Rio (1997) and Banco de Crédito Argentino (1996) were acquired by Banco Santander and BBVA, respectively (Table 6).

Several factors facilitated the international expansion of Spain's largest banks. First, the de-regulation of the late 1980s, which increased domestic competition. Liberalisation started in the 1970s with the elimination of interest rate controls, permission to open branches, and the abolition of compulsory investment coefficients. The deregulation process accelerated with adherence to the European Economic Community in 1986, and later with membership to the euro area, which forced Spain to adapt to European regulations. In 1989, there was a complete liberalisation of interest rates and commissions, the stock market was reformed and updated, and new measures were passed to regulate pension funds. The entry of foreign banks was liberalised. Competition increased not only among banks but also between banks and saving banks, which were allowed to expand geographically (Caminal et al., 1990; Salas and Saurina, 2003). The level of financial intermediation rose sharply and the sector began to be saturated (Table 7); the time came to look for new markets.

TABLE 7 ▪ *Banking penetration in Spain and some LatAm countries, 2000*

	Population aged 18 and over with current account (%)	Clients per branch ('000)
Spain	95	1
Argentina	35	8
Brazil	48	19
Chile	50	8
Mexico	35	13
Peru	37	27

Source: PwC Annual Report (2011).

The increase in competition triggered a reaction by Spanish banks, which were forced to adopt a more market-oriented business strategy to increase their profits. The first banking reaction was to obtain bank size through mergers. Secondly, as the adoption of the euro eliminated some traditional sources of revenues, such as currency trading or currency exchange commissions, banks began to offer new products other than deposits (investments, pension funds, etc.). They also moved to find alternative sources of revenue, such as commissions for financial services, or the reallocation of loan activities to more profitable sectors (Saurina, 2012), as well as restructuring their branch networks (Casilda, 2016). Lastly, they invested in R&D to increase efficiency by introducing new services and devices (cash machines, phone banking, and so on)[19] and improve the management of data, information and marketing procedures. For example, Banco Santander led the way in these new strategies by offering the Super Account, which was launched in 1989 with a massive advertising campaign, and which paid 11 per cent interest — more than double the interest rate paid by other banks at that time. In 1993, Santander offered the "*Superlibreta*" and the "*Superhipoteca*", and in 1990 BBV launched the so-called "*Libreton*".

TABLE 8 ▪ *LatAm: share of foreign banks in selected countries, 1998*

	Total Assets (billion $)	% foreign ownership of assets: Share of equity	% foreign ownership of assets: Effective control	BBVA and Santander (% of total foreign banks)(*)
Argentina	160.3	43.2	51.5	39
Brazil	627.3	19.2	21.4	6
Chile	108.5	39.4	35.9	46
Colombia	30.9	21.5	28.8	59
Mexico	117.1	19.0	16.0	33
Peru	22.0	39.8	58.5	38
Venezuela	22.4	32.4	40.2	34

(*) Total assets of all banks with Spanish ownership as a percentage of total assets of all banks in the country with foreign ownership.

Source: Calderon and Casilda (2000).

Several additional factors explain why Latin America has been the main focus of Spanish banking investments, especially after 1986. Firstly, Spain and Latin America have a common history that harks back to the colonial period, and due to emigration and commerce. There are as well cultural ties and most importantly a common language. Casilda (2002) provides evidence on the importance of having a common language through an ESADE survey

19. Both banks experienced an intense process of technological change and innovation in a framework of strong competition that facilitated international expansion (Batiz-Lazo and Maixé-Altés, 2011; Maixé-Altés, 2010).

TABLE 9 ▪ *LatAm: share of Spanish banks, 2015, billion € and %*

	Santander			BBVA		
	Deposits clients	Credits clients	Assets	Deposits clients	Credits clients	Assets
LatAm	122.4	133.1	267.8	95.8	95.1	171.2
% over total group	17.9%	16.8%	19.9	23.7	22.9	23.7

Source: Annual Reports Santander and BBVA (2016).

in 2000. According to this survey, almost 97% of those interviewed (entrepreneurs and business managers) confirmed that language was Spain's main competitive advantage, followed by cultural affinity. Jimenez and Narvona (2010) used a gravity model to estimate the importance of a common language on Spanish FDI and also offered micro evidence for the period (1999-2005) about how the common language increased the bilateral FDI between Spain and Mexico by 250 per cent. In the same line, Santana et al. (2012) claim that cultural proximity positively affected banking FDI in Latin America, especially in the initial phase of internationalisation. Similar habits and a shared language allow Spanish banks to sell identical or very similar products, to use the same marketing approaches, to transfer know-how, and to facilitate the mobility of employees (Cardone-Riportella and Cazorla-Papis, 2001; Casilda 2016). Santander and BBV transferred their most successful products to Latin America adapted to the peculiarities of each country: Santander launched its products in Chile in 1994 and Mexico in 1997 and BBV introduced the "*Libreton*" in Venezuela (el "*Libretazo*"), Perú ("*Superdepósito*") and Argentina in 1997 (Toral, 2011). After each acquisition Santander restructured their local banks, introducing Santander's peculiar management system, which consisted of a change in risk management procedures, a review of the balance sheet and the injection of new capital to improve the solvency of these institutions (Martín-Aceña, 2010). Finally, in the post-1986 period and especially at the turn of the century, market conditions made Latin American countries a favourable location for Spanish banking expansion.

a. Financial and economic conditions in Latin America

The 1980s were very difficult years for the subcontinent (the "lost decade"), with a dramatic fall in per capita GDP and 18 countries suffering financial crises (O'Campo, 2014). These problems affected international banks but also some of the leading domestic banks. As an ECLAC report explained, the debt crisis affected a large part of the US banking system and American banks' risk aversion discouraged them from investing in this region. In 1986 the exposure of the top nine US banks in Argentina, Brazil, and Venezuela accounted for 41 billion dollars, or 45 per cent of total US bank exposure (Sachs and Huizinga, 1987). Those nine banks accounted for a remarkable 65 per cent of total exposure of US banks in the region. Moreover, sovereign loans accounted for about two-thirds of US bank lending to less developed countries. For example, FleetBoston (Bank Boston Corporation from 1997) was heavily involved and hit by the crisis during the 1980s and 1990s and that affected its international strategy (*The Times*, 1987). The debt crisis also forced other US banks such as Citicorp and Chase to stop overseas lending and to restructure existing loans and their investment portfolio.[20] However, as Alvarez (2015, 2018) explains, although the exposure of international banks to Latin American debt is well known, the exposure of domestic banks received much less notice. In Mexico, for example, domestic banks such as Ba-

TABLE 10 ▪ *Growth rates of per capita GDP in LatAm and the Caribbean region (%)*

Country	1980-1990	1990-2000
Argentina	-3.87	4.22
Bolivia	-2.22	1.08
Brazil	-0.26	1.46
Chile	1.28	4.79
Colombia	1.35	0.87
Costa Rica	-0.94	1.75
Ecuador	-1.17	-0.85
El Salvador	-1.66	2.30
Guatemala	-1.21	0.84
Jamaica	1.72	-1.05
Mexico	-0.43	1.78
Nicaragua	-3.00	-2.42
Panama	-0.69	1.96
Paraguay	1.01	-0.58
Peru	-3.13	2.47
Uruguay	-1.00	2.81
Venezuela	-1.36	-0.80
Average LatAm	-0.74	0.98
World	0.98	1.32

Source: Heston, Summers and Aten (2002): *Penn World Tables*.

20. Citicorp and Chase were rated Aaa in 1982, dropped to Aa1 in 1982 and, as a consequence of the debt crisis, by 1987 their ratings had deteriorated to A1 and Baa1, respectively (FDIC, 1997).

namex, Bancomer, Banca Serfin and Multibanco Comermex were involved in international lending, had considerable amounts of Mexican external debt and were then as exposed as many other international institutions. When the debt crises erupted, foreign institutions retreated, while domestic banks could not unmake their risky portfolio and remained, and their financial positions deteriorated sharply. Spanish banks took advantage of these developments and entered with force into the region.

At the turn of the twenty-first century, economic conditions in many Latin American countries changed somehow. Growth returned and was accompanied by macroeconomic stability. There were, however, some exceptions. Severe problems in Argentina (the *corralito* in 2001), in Venezuela (when in 2008 President Chávez announced the nationalisation of Banco de Venezuela, the Venezuelan bank owned by Grupo Santander), and in Brazil and Uruguay surfaced. The Emerging Market Bond Spread (EMBI),[21] published by JP Morgan from 1997, can be used as an indicator of country risk and shows that from 1997 to 2010 Brazil, Chile, Colombia and Mexico exhibited low EMBI rates. On the contrary, Argentina, Ecuador and Venezuela enjoyed high EMBI rates (World Bank databank, EMBI TS, several years, and Table 11). Spanish banks tried to maintain their position and to reduce risk. Santander created a special 1.3-billion-dollar fund to convert the entire book value of its Argentine banks. Economic as well as political instability drove Santander to adopt measures such as the sale of Banco Santa Cruz in Bolivia when in 2005 Evo Morales won the election (Parada et al., 2009). In Venezuela in 2009, Santander sold the bank to the Venezuelan government for

TABLE 11 ▪ *Emerging Markets Bond Spread (EMBI) in Latin America, 1997-2010*

	LatAm Average	Argentina	Brazil	Chile	Colombia	Ecuador	Mexico	Venezuela
1997	467	456	520	n.d	286	400	400	436
2000	664.5	667.7	726.7	197.3	668.0	2,863.0	366.5	879.7
2005	363.9	2,586.6	394.3	64.8	322.7	706.6	167.3	409.3
2010	359.5	681.3	201.8	129.2	189.2	925	186.6	1,080.4

Source: World Bank Databank EMBI TS, several years.

21. J.P. Morgan's initial EMBI is an index constructed for dollar-denominated sovereign bonds issued by a sample of emerging countries. It is based on the spread or interest differential between dollar-denominated bonds issued by developing countries and US Treasury bonds (the latter being considered to be risk-free). The EMBI has recently lost some relevance as an indicator of country risk because the dollar-denominated bonds only represent a relatively small portion (less than 30 per cent) of outstanding sovereign debt and JP Morgan offers other indexes.

1.05 billion. In the case of BBVA, despite the continuous threats of expropriation and the financial sector's risk exposure, it declared that it had no intention of leaving the country.[22]

Expectations improved as well. Populations grew, private consumption rose thanks to an expanding middle class (Calderon and Casilda, 2000), and Spanish banks focused on the mass market (lower- and middle-income segments), in contrast to other foreign banks such as Citibank, which concentrated on the upper-income market.

Moreover, the region had an underdeveloped financial system (Table 12) with considerable potential for the expansion of bank branches and introduction of financial products. At that time, the banking penetration rate was 95 per cent in Spain and 35 per cent on average for Latin America (see Table 8). Domestic competition was low in comparison with the European market (Guillén and Tschoegl, 2007). There were profitable business niches, such as the mortgage market and pension fund management (PwC, 2011). Between 1981 and 2008, 11 countries introduced private pension schemes: Chile (1981), Peru (1993), Argentina and Colombia (1994),[23] Uruguay (1996), Bolivia and

TABLE 12 ▪ *Financial system size: Total deposits to GDP (%)*

	1995	2000	2005	2010	2015
Argentina	14.97	24.96	19.50	16.23	17.85
Bolivia	31.96	45.92	35.98	42.51	59.65
Brazil	24.69	39.84	46.65	47.31	55.35
Chile	29.13	47.04	44.31	37.34	51.83
Colombia	22.45	22.70	15.13	18.34	24.28
Costa Rica	22.04	12.95	20.21	23.86	25.52
Dominican R.	16.86	22.53	16.42	18.70	20.82
Ecuador	18.27	15.98	19.26	24.52	29.82
Mexico	20.80	20.99	20.19	24.69	28.76
Peru	16.45	27.26	22.05	28.84	36.62
Spain	60.81	74.10	76.16	97.21	95.60

Source: Financial system deposits to GDP from Demirgüç-Kunt et al. (2018): *Financial Development and Structure Dataset*.

22. The last such declarations were made by Francisco Gonzalez, executive chairman of BBVA, in February 2018, in *El Nacional*.

23. In Colombia, for example, Law 45 in 1990 and Law 100 in 1993 created a private healthcare and pension system that increased the number of institutional investors (Forero-Laverde, 2017).

Mexico (1997), El Salvador (1998), Costa Rica (2001), Dominican Republic (2003), and Panama (2008) (Minda 2007).[24]

Finally, Latin America represented a complementary area for Spanish banks: whereas the Spanish economic cycle is highly correlated with that of the Euro zone, it was negatively correlated with that of the Latin American area. A clear example of this complementarity is the positive evolution of Spanish banks' profits in the region after the 2008 crisis. Therefore, Spanish banks were attracted not only by the potential growth and opportunities the region offered, but also because it had a complementary cycle with respect to Spain (Casilda, 2002).

b. Capital controls and deregulation

Latin American governments, which had restricted the entry of foreign capital in previous decades, changed their policy. Foreign banks were considered an important instrument to correct the shortage of financing and also to promote the modernisation of their financial systems. In some countries, the debt crises also altered foreign banking entry conditions. In Brazil legislation was passed in 1988 that eliminated barriers to entry into the national financial system (Nyasha and Odhiambo, 2013), and according to Bodin de Moraes (1989), this foreign openness was part of the hidden negotiation of the Brazilian central bank and the World Bank to avoid a default. Foreign bank liberalisation also took place in Colombia in 1990, where 45 restrictions on foreign investment in the financial sector were eliminated and the system for mergers, acquisitions and liquidation of financial intermediaries was simplified as part of an ambitious programme of modernisation (Forero-Laverde, 2017).

Furthermore, the so-called Washington Consensus favoured the adoption of policies aimed at deregulating and liberalising ample sectors of the economy. Between 1985 and 1995 there was a "first generation" wave of reforms resulting in the liberalisation of interest rates and the elimination of barriers to entry in Bolivia, Costa Rica (1985), Ecuador (1986), Mexico (1988), Argentina, Brazil, Venezuela (1989), and Peru (1991) (Moguillansky and Studart, 2004).[25] Only Chile and Uruguay had started their liberalisation process-

24. After 2008, Chile and Argentina introduced a re-reform to restructure their pensions system; for example, Argentina integrated again the valuable private system into the public system (Mesa-Lago, 2010). Before 2008 BBVA was the biggest fund manager in Latin America and in some countries it had a nearly 70 per cent market share of the pension fund business. However, in 2012-13 it sold part of its fund business in Chile, Colombia, Peru and Mexico (Financial Times, December 2012; Reuters, April 2013).

25. The privatizations and deregulations of those years involved a major investment effort that exceeded domestic capitalization capacity. According to Casilda (2002), this effort exceeded 10 per cent of GDP for three countries in the region, while for another six it reached 5 per cent, with marked differences by country. In addition, 57% of privatizations in the 1990s

es earlier (in 1974); however, in the case of Chile, the government intervened in the banking system between 1982 and 1984, with the system being re-liberalised from 1985 (Barth et al., 2018; Moguillansky and Studart, 2004, and Paez, 2004).

The reforms included the privatisation of state-owned banks (Chile, 1985-89; Mexico, 1991-92; Argentina, 1994; Brazil, 1998-1999). Privatisations were part of the financial reforms prompted by the IMF and the World Bank, and in response to domestic financial crises and instability (Guillén ,2006). Case studies provide interesting insights into how banking privatisation facilitated the entry of foreign banks in those years and the differences. In Brazil, banking privatisation was less intense than in other countries in the region. The two largest banks, Banco do Brasil and Caiza Economica Federal, were still public in 1995 and as late as 2015, respectively (Cortés and Marcondes, 2016). The presence of Banco Santander in Brazil began with the privatisation process. In 2000, it acquired 33 per cent of a state-owned bank, Banco do Estado de Sao Paulo*,* and in the following years Brazil became the Spanish bank's main foreign market. In 1995, BBVA bought Banco Continental de Perú, which had been privatised by the Peruvian government three years earlier. Similarly, it was after the process of privatisation that BBVA acquired the largest Mexican banks (BBVA, 2008).

The deregulation process coincided with the withdrawal of US banks from the Latin American market, partly due to the impact of prudential limits on bank exposure to specific risk in some countries, such as Brazil, Argentina, and Mexico. In the second half of the 1990s, there was a wave of "second generation reforms" that were introduced to strengthen mechanisms of control and supervision but also to facilitate new areas of banking activities and operations. These regulatory changes encouraged the entry of foreign banks into Latin America (Correa, 2004).

Finally, although the situation differs substantially between countries, the banking deregulation process in the 1980s coincided with a rule of law movement that increased legal certainty. Although legal reforms failed on many fronts and overall progress was modest at best, a governance index (which includes rule of law, the expropriation risk, and the repudiation of contracts by government, among other variables) shows a decline in values from 1985 to the late 1980s, but a recovery from 1990 to 1995 in countries such as Argentina, Chile, Ecuador and Peru (Loayza and Palacios, 1997). The waves of populism in countries such as Argentina, Ecuador and Venezuela, from the end of the twentieth century, are creating significant risk to the rule of law and this has affected recent strategies of Spanish banks in these countries (see footnote 23).

took place in the services sector. Thus, foreign investment in privatisation accounted for 36% of FDI in the 1990s.

c. Price and returns

The pattern of internationalisation was also influenced by a price factor, because the valuations of European banks were much higher than those of Latin America. Buying Latin American banks was a cheaper way to increase the size of the parent bank than buying European banks (Guillén and Tschoegl, 2000).

Additionally, the institutions' regions offered increasing returns. The net interest margins were considerably higher than in Spain. From 1990 to 1994 they were above 5 per cent: 5.1 per cent in Mexico, and 9.2 per cent in Argentina; but only 3 per cent in Spain.[26] The estimates by Paula (2010) for the period 1995-2005 show that whereas intermediation margins in developed countries was around 2.9 per cent, in Latin America it was 8.5 per cent. According to the BBVA research department, the cost of a 1 per cent share of deposits in Spain in 1999 was 2.263 billion dollars, not very far off the equivalent cost in Germany of 2.28 billion dollars, whereas in Argentina it was 1.96 billion dollars, in Chile 1.72 billion dollars, and in Mexico 2.05 billion. The spreads in Latin American countries remain high, with Brazil and Peru being the two countries with the largest interest rate spreads. In 2014, Brazil had the highest spreads at over 15 per cent, with a ROE of around 20 per cent for the largest banks (IMF, 2016). In Spain in the same year, banks had a ROE of around 6.6 per cent (Bank of Spain, 2017).

d. Non-financial Spanish foreign investments

Banking investment in Latin America was a substantial part of the Spanish FDI in this period, along with investments in energy and communications. The coincidence in time of Spanish multinationals' expansion and banking internationalisation was not only a "follow the client" motive, but also part of an overall strategy. The banking mergers that took place in Spain between 1988 and 1996, and the privatisation of Spanish public companies led to the formation of large conglomerates in which banks had significant investments (Serrano, 2013).

Spanish companies with interests in Latin America achieved financial support from Santander and BBVA. In 1995, BBVA had a portfolio of industrial companies that included 11% of Iberdrola, 7% of Repsol, and 5% of Telefónica, and a significant presence in Endesa, that is, some of the most active Spanish companies in Latin America (Durán, 1997). Furthermore, the presence of

26. The countries with the highest interest margins between 1990 and 1994 were Argentina (9.2), Colombia (8.3), and Venezuela (8.1), followed by Brazil (6.8), Chile (6.1), and Mexico (5.1) (Goldstein and Turner, 1996).

common directors in the boards of these firms favoured the convergence of interests. A clear example is provided by the Chairman of BBV, Emilio Ybarra, who from July 1996 was also Deputy Chairman of Repsol. Santander also had stakes in Telefónica, although its industrial portfolio was more diversified and smaller than that of BBVA. In short, this convergence of interests allowed for operations such as that carried out by BBV in July 1995, when it announced the acquisition of 1.5% of the capital of Telefónica de Perú, a subsidiary of Telefónica de España, which held, through a controlling holding company, 31% of the Peruvian company. This participation was facilitated by the placement of Telefónica Perú shares in foreign markets in the first week of July 1996, an operation brokered by a company of the bank, BBV Interactivos. Such an operation was in line with the bank's strategy of accompanying the direct participation and international investments made by its investees Telefónica and Repsol, especially in those markets where BBV operated as a bank. Subsequently, BBVA acquired 8% of Repsol de Perú's, in a similar cross border operation (Durán, 1997). In the case of Santander, FDI seems to be less determinant. It has a lower industrial portfolio than BBVA, although it had a high participation in CEPSA, which operates in oil exploration and production in Brazil, Colombia and Peru (and from 2018 in Mexico), and in petrochemical in Brazil (Guillén and Tschogel, 2008).

e. Recent events

Entry into Latin American countries provided a stepping-stone for expansion into other countries. Firstly, it allowed Spanish banks to increase their size in order to compete in the international arena. Secondly, it offered a geographical advantage in that it facilitated the later expansion in the US market, particularly in Hispanic-majority areas (where many people, moreover, knew the Spanish banks from their countries of origin). After the Great Recession there has been a reduction in the global flows of capital. The number of foreign banks around the world dropped from 1,445 in 2009 to 1,368 in 2013, with a reduction in all countries regardless of the level of income (BBVA, 2016). In fact, the presence of foreign banks in some regions has still not returned to pre-crisis levels. There has also been a reduction in international loans (Álvarez et al., 2016; Claessens and Van Horen, 2014). In comparative terms, foreign investment in Latin America has better withstood the impact of the crisis. The decline in banks' international activity can be traced back to the new regulations introduced after the 2008 crisis (Ichiue et al., 2006). These new regulations have mainly affected capital requirements, which can explain the restructuring of the international position of Spanish banks, mainly BBVA, in geographic areas where profitability was not high enough to ensure the required capital ratios. The general trend observed has been a reorganisation process, with banks identifying countries that offer the most profitable opportunities and exiting the less attractive countries (in the sense of low profitability or political issues, as in the cases of Argentina and Venezuela).

The 2008 crisis, therefore, forced banks to become more selective in terms of international expansion and portfolio decisions. As Claessens and Van Horen (2014) point out, banks in advanced economies (including BBVA and Santander) are less likely to engage in particularly active foreign expansion in the future, whereas banks from emerging economies are more likely to play an increasingly important role as foreign investors. The forthcoming challenges for the banking industry in terms of stricter regulation, technological change, and increasing competition will require a change in the banks' approaches. The future evolution of the Latin American market will be a crucial issue as BBVA and Santander redefine their strategies.

All of the factors mentioned so far that fostered the Spanish banking expansion in Latin America occurred at the same time that other transnational banks were focusing their attention on other regions. Given the importance of this aspect to the expansion strategy of Spanish banking, we discuss it in detail in section 6.

Spanish banks versus transnational banks in Latin America

Most of the changes outlined above stimulated Spanish banks' entry into the Latin American market. However, they were not strong enough to pull other transnational banks into the region. As Galindo, Izquierdo and Rojas-Suárez (2015) suggest, an important aspect is how different types of foreign banks follow different strategies when expanding abroad. In an empirical analysis for the period 1996-2007, the authors differentiate between US banks, banks of Spanish origin, and other foreign banks; they report differing behaviour depending on the country of origin. We can use this narrative to explore the main drivers of different overseas expansion strategies during the 1980s and 1990s.

In 2001, in addition to BBVA and Santander, the foreign banks with the largest presence in the region in terms of lending were Citigroup, FleetBoston, HSBC, ABN Ambro, and Scotiabank. With the exception of Citibank, which accounted for a larger share of lending in the region than Santander and BBVA, the rest of the foreign banks had much smaller participation (ECLAC, 2002). The debt crisis reduced the US banks interest in expanding in Latin America, and forced them to undergo restructuring processes.[27] By

27. The debt crisis affected a large part of the US banking system and American banks' risk aversion discouraged them from investing in this region. In 1986, the exposure of the top

contrast, promising opportunities and good results in the US market encouraged these banks to increase their domestic investments, and even in some cases attracted the attention of European banks, such as Deutsche Bank. Only after seeing the success of the Spanish banks in the Latin American region did Citigroup begin to adopt a more aggressive policy. Citigroup decided to reorient its activity towards commercial banking with the acquisition in 2001 of Banamex, which allowed it to increase its number of banking accounts in just one year from 9 to 23 million (Ballescá, 2007).

By contrast, European banks had been less involved in the Latin American region during the 1980s, and consequently did not have the bad experience that US banks did. Banks from the Netherlands, Germany, France, Switzerland and, finally, Spain intensified their internationalisation from the 1980s through to 2000 (Slager, 2005). They took advantage of the opportunities offered by the European Union and thus focused their investments in Europe. German banks, for example, which had a considerable presence in Latin America in the 1980s and 1990s, expanded throughout Western and Eastern Europe, and in the US. Dutch banks also focused on Central and Eastern Europe (ECLAC, 2002). With respect to the British banks, Midland Bank, for example, which had been very active in Latin America, increased its presence in European countries (Germany, France, and Italy) and in the US. However, the acquisition of a US bank with bad real estate loans and a substantial share of Latin American debt put the bank in a very difficult situation, which forced it to end its international forays (Holmes and Green, 1986). Also Lloyds[28] decided in the mid-1980s to refocus its activities on the domestic market (Altamura, 2017), and Barclays scaled down its international operations in the 1990s (Rogers, 1999). Japanese banks moved to the UK and the US in the 1980s, and their international expansion headed towards Asia in the 1990s. However, the Japanese banking crisis that triggered a credit crunch in 1998, along with the 1997 Asian financial crisis, forced Japanese banks to scale back their foreign activity. Other banks, such as HSBC,[29] expanded in Latin America in 1997 by buying banks in Argentina, Brazil, Mexico, and Peru (Kiforenko, 2016). Scotiabank also entered the region in the 1990s in Mexico, Chile, Peru, and Colombia (Connor, 2017). In short, Spanish banks' urgent need to grow was facilitated by the general weakness of most of the Latin American domestic banks, and the retreat of Euro-

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nine US banks in Argentina, Brazil, and Venezuela accounted for 41 billion dollars, or 45 per cent of total US bank exposure (Sachs and Huizinga, 1987). These nine banks accounted for a remarkable 65 per cent of total exposure of US banks in LatAm; moreover, sovereign loans (those to public sector borrowers in the host countries) accounted for about two-thirds of US bank lending to less-developed countries.

28. Lloyds was one of the leading providers of credit to Brazil and Mexico (Jones, 1995).

29. In 1992, HSBC closed a deal with Midland Bank and in the late 1990s expanded in LatAm, Turkey, France, Switzerland and the US (HSBC Annual Reports).

pean and US financial institutions. This also happened at a time when the largest international banks were redirecting their attention to the Pacific, and other potential markets. This cleared the way for Santander and BBVA to expand in the region.

Conclusions and final remarks

Although the internationalisation processes of BBVA and Santander intensified from the 1990s onwards, they come, due to mergers and acquisitions, on the back of a previous history of internationalisation. Santander and BBVA started their international expansion after: a) consolidating their positions in Spain, and b) a process of mergers that allowed them to achieve the size needed to expand abroad. In both cases, Latin America was the first area of expansion, and the region was crucial for their internationalisation. Santander moved abroad before BBVA. In the pre-1986 period, Santander's entry was aimed at providing its clients with the necessary services to carry out their operations abroad; later it looked for new growth opportunities by acquiring local banks. Although we lack good quantitative evidence, different qualitative sources point to the importance of emigrant remittances and, in some specific cases, financing trade between the Peninsula and the different countries' regions.

Spanish banks' penetration in Latin America was, however, limited. First, because the regulated domestic financial market and the absence of competition sufficed to ensure handsome benefits. Second, most of the banks were small in comparison to international institutions. Third, external conditions prevented overseas investment, since Latin American countries put barriers to entry and other regulatory constraints. ISI growth strategy and nationalism did no favours either to foreign undertakings. Finally, the low demand for banking services in the Latin American region also acted as a limiting factor for Spanish banks.

In the post-1986 period, Santander Group and BBVA increased their presence in Latin America. In 1999, Banco Santander had more foreign assets as a percentage of total assets (29.92 per cent) than BBVA (21.03 per cent). However, between 1999 and 2006, BBVA registered an increase in this percentage from 21.03 to 26.14 per cent, whereas Santander rose from 29.92 to 62.36 per cent.

Both banks adopted a strategy of entry via acquisition rather than via greenfield operations. And both specialised in retail banking, in contrast to other foreign banks such as Citibank, which focussed on a minority of the population: high-net-worth households and investors (Citi Report, 2017). In 2017, this region accounted for 53 per cent and 56 per cent of the two Spanish entities' profits, respectively. Santander's activity is distributed among different countries (Argentina, Brazil, Chile, and Mexico), while BBVA's activity is more concentrated in Mexico. Both banks have nearly 30 per cent of their total assets in Latin America.

There are several factors that explain the Spanish banking sector's international expansion in the post-1986 period. First, deregulation and increasing competition in the domestic market. Second, the increase in bank size: by merging operations, Spanish banks gained financial muscle that allowed them to move abroad. Also, financial conditions in the host countries changed so as to provide news grounds for internationalisation. The weaknesses of the domestic market, the debt crisis, the elimination of barriers to entry, deregulation, and privatization, were the most significant aspects. Low purchasing prices and high interest margins were also contributing factors for expansion, particularly in Latin America. Finally, the fact that transnational banks focused their attention on regions other than Latin America meant that with an absence of competition Spanish banks had plenty of space to open branches and acquire domestic institutions.

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How local conditions affect global banking: the case of BBVA and Santander

ABSTRACT

This paper explores why Spanish banks internationalize and why Latin America has been the main region for the international expansion of BBVA and Santander. It shows that prior to 1986 Spanish banks had a limited presence abroad, and analyses the main drivers of this initial expansion (remittances and trade connections). However, from 1986 on, there was a confluence of domestic and external factors (economic and regulatory changes in Latin America) that encouraged the international forays of BBVA and Santander. The fact that changes in the Spanish and Latin American financial sectors occurred just when other transnational banks were turning their attention to other regions created the optimal conditions for the expansion of Spanish banks in Latin America.

KEYWORDS: banking globalisation, financial markets in Latin America, Spanish banks.

JEL CODES: G15, G21, N26

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Cómo las condiciones locales afectan a la banca global: el caso de BBVA y Santander

RESUMEN

Este artículo explora por qué los bancos españoles se internacionalizan y por qué América Latina ha sido la región principal para la expansión internacional de BBVA y Santander. Se muestra que antes de 1986 la banca española tenía una presencia limitada en el exterior y se analizan los principales impulsores de esta expansión inicial (remesas y conexiones comerciales). Sin embargo, a partir de 1986 se produjo una confluencia de factores internos (liberalización bancaria española, creciente competencia y aumento de la IED española) y externos (cambios económicos y regulatorios en América Latina) que incentivaron las incursiones internacionales de BBVA y Santander.

PALABRAS CLAVE: globalización bancaria, mercados financieros en América Latina, bancos españoles.

CÓDIGOS JEL: G15, G21, N26.