
Narrative vs data: the SVB crisis and the resilience of Latin American banks

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Theme

Latin American banks have shown a remarkable resilience in light of the recent financial turmoil triggered by the failure of the Silicon Valley Bank (SVB).

Summary

The financial turmoil unleashed in the US following [the collapse of the Silicon Valley Bank \(SVB\)](#) offers a unique perspective to understand the resilience developed by Latin American banks.

While it is a well-known fact that [Latin American banks have high levels of capitalisation](#), more than double the Basel III requirements, what this analysis highlights is less so: that Latin American banks operate with relatively low levels of duration risk and therefore were prepared to weather much better than their US and European peers the rise in interest rates that began in early 2022 that led to a significant drop in the value of fixed-income securities.

More importantly, the low duration risk on Latin American banks' balance sheets is a strategy that they chose deliberately, but was not determined by the fact that the average maturity of government debt issued by Latin American countries is lower than that of advanced economies.

Analysis

The [recently published report by the Elcano Royal Institute](#) *Why Latin America Matters* aims to analyse and contrast, rigorously and on the basis of data, the installed narratives about Latin America that operate as axiomatic truths in the economic, political and geostrategic spheres, and to contribute to shifting the debate from preconceptions to factual evidence.

The financial turmoil unleashed in the US in March 2023 as a result of the collapse of Silicon Valley Bank (SVB) offers a unique opportunity to contrast the performance of Latin American banks with what would have been expected according to the established narrative, and to understand the reasons for the resilience they have developed.

According to this narrative, a financial crisis like the SVB and its global aftershocks, even more so [in a context of rising interest rates and a strong US dollar](#), should have had a more severe adverse impact on Latin American banks than on those of their counterparts in central countries like the US and the EU, whose central banks issue reserve currency and can act quickly and effectively as lenders of last resort.

But as we shall see below, that is not what ultimately happened. And for very good reasons: the data killed the narrative.

The SVB crisis and duration risk

March 2023 recorded the second-largest bank failure in US history when the SVB collapsed. Normally, bank failures tend to be associated with the materialisation of credit or liquidity risks. But there are other financial risks that can lead to the non-viability of an institution, as in the case of the SVB, victim of the materialisation of the so-called duration risk.

The relationship between interest rates and bond prices is inverse: when interest rates rise, bond prices fall and vice versa. Duration is a measure of the sensitivity of a fixed-income security to interest-rates changes. In the case of a bond, the longer the duration, the greater the change in its price in response to changes in interest rates. For instance, if interest rates rise by 1 percentage point, the price of a 10-year bond will fall by 10% and that of a 1-year bond by 1%, as shown in Figure 1.

Figure 1. Change in bond prices with an initial nominal value of €1,000 against an interest rate increase of 1%

Duration	% change in price	Nominal value
1 year	-1%	990 euros
5 years	-5%	950 euros
10 years	-10%	900 euros

Source: the authors.

SVB had a well-hedged credit risk, as much of its assets were invested in US Treasuries and Mortgage-Backed Securities (MBS) backed by US government agencies. However, the sharp deposit withdrawals suffered by the SVB, coupled with the 475 basis point increase in policy rates mandated by the Fed between March 2022 and April 2023, precipitated the bank's downfall. In particular, [the mark-to-market valuation of the fixed income securities in the SVB's assets](#) (assuming it had not been necessary to sell the assets at deep discounts) would have resulted in the bank losing all its capital.¹

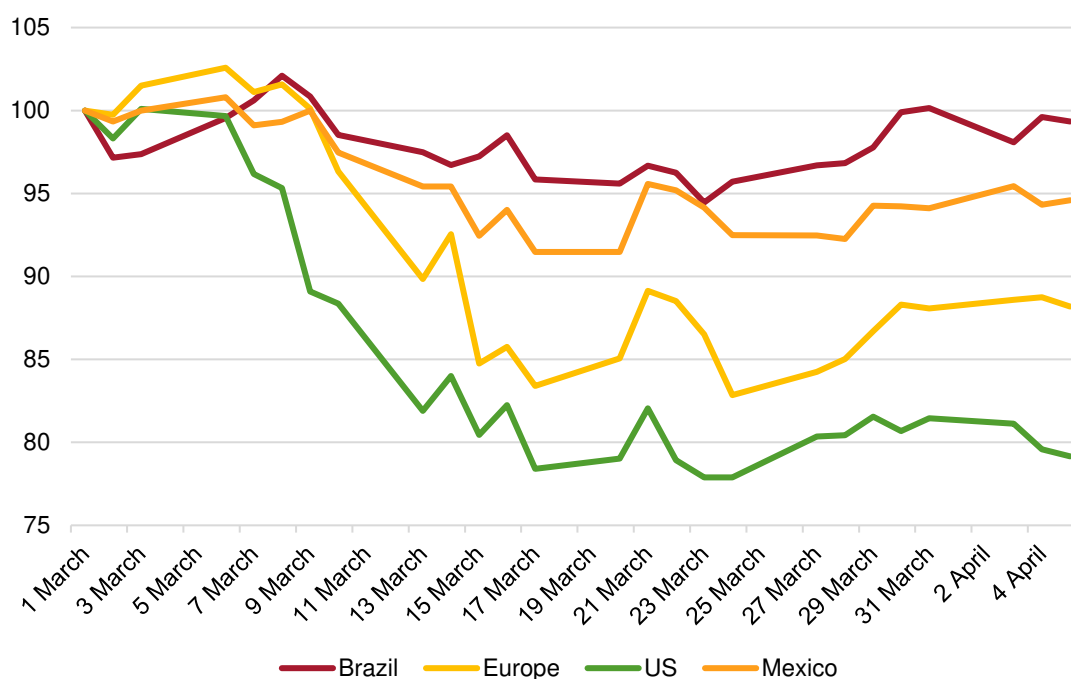
¹ It is worth noting that the assets were nevertheless sufficient to pay its creditors almost in full, including uninsured deposits.

The SVB crisis and Latin American banks

Financial stress spread to other US regional banks and eventually to US and European global banks as well. In the latter case, the crisis of Credit Suisse, which prompted its acquisition by UBS with the support of the Swiss government and Central Bank, was the most emblematic event of the international fallout from the SVB crisis.

Of course, these blows resulted in a strong and widespread stock market punishment of the global banking sector. As shown in Figure 2, bank stock prices were penalised in both the US and Europe, although to a greater extent in the US, which was the epicentre of the financial turmoil. At the peak of the crisis, the prices of the key banking stock market indexes fell by more than 20%.

Figure 2. Share prices of main banks, between 1 March and 5 April 2023 (1 March = 100)



Source: the authors, based on data from Investing.com.

However, in stark contrast to what would have been expected according to the established narrative, there is one element that stands out: the fall in share prices was much smaller for Brazilian and Mexican institutions. Moreover, the share price of Brazilian banks recovered very quickly to pre-crisis levels.²

The heart of the matter: the management of duration risk by Latin American banks

The crisis triggered by the collapse of the SVB is, as explained above, a duration risk crisis. To fully understand the resilience of Latin American banks it is therefore useful to

² For the EU, the Stoxx 600 Banks index has been used; for the US, the Dow Jones US Banks index; and for Brazil and Mexico, an index weighted by the capitalisations of the three listed banks with the largest volume of assets, respectively (Itaú, Banco do Brazil and Bradesco in Brazil's case and BBVA, Santander and Banorte in Mexico's).

focus on examining the duration risk of the bank balance sheets of the various countries under study.

To assess duration risk, and for reasons of data availability, this paper analyses the maturity structure of government debt holdings on the banks' balance sheets.

Using data from the European Banking Authority on sovereign debt holdings in the assets of banks in the US, Latin America and the four major economies of the Eurozone, it can be seen that Latin American banks hold government debt with an average maturity well below that of US and Eurozone banks (see Figure 3).³

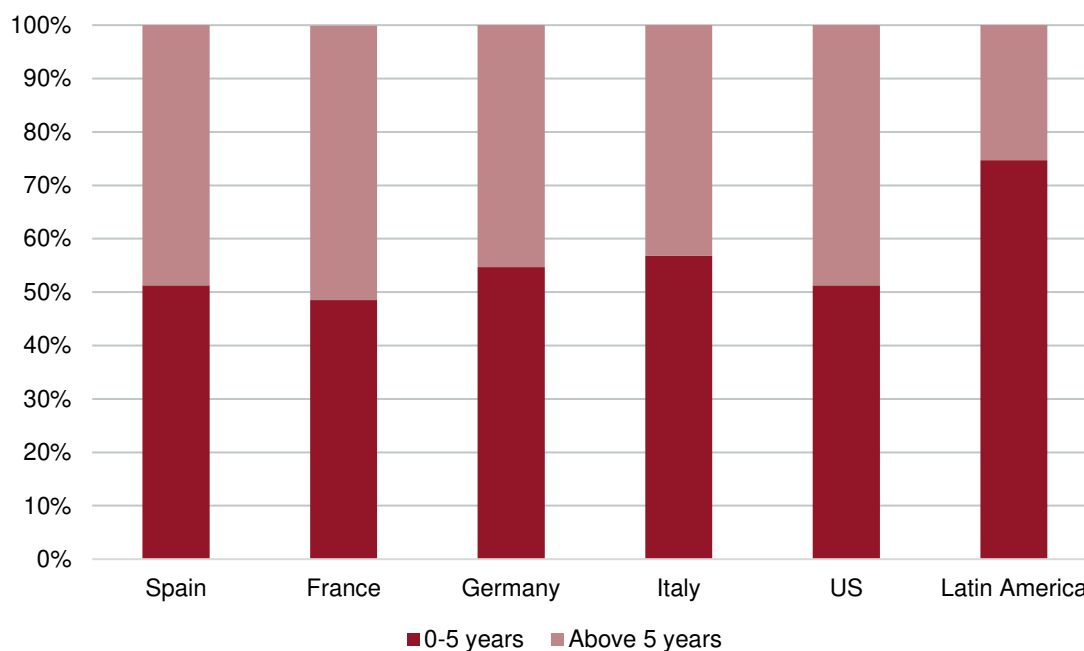
Figure 3. Share of banks' public debt holdings classified by maturity

Nationality of the bank	0-3 months	3 months -1 year	1-2 years	2-3 years	3-5 years	5-10 years	10 years and longer
Spain	1,86	19,64	6,48	9,77	13,50	33,87	14,88
France	19,38	11,69	5,24	4,22	8,06	18,71	32,70
Germany	11,94	11,22	9,39	7,79	14,38	19,93	25,36
Italy	5,93	10,49	12,29	12,98	15,18	25,39	17,74
US	9,84	10,44	6,44	10,20	14,37	20,12	28,58
Latin America	21,12	10,29	11,02	12,86	19,45	10,74	14,52

Source: the authors, based on data from the European Banking Authority, <https://www.eba.europa.eu/risk-analysis-and-data>.

Indeed, as shown in Figure 4, almost 75% of Latin American banks' government bond holdings have a maturity of less than five years as opposed to that of US and Eurozone banks, where around 50% of government bond holdings have a maturity of more than five years. This means that other things being equal (eg, rising interest rates on relevant fixed-income securities on bank balance sheets and capitalisation levels), the duration risk that Latin American banks were 'carrying' on their balance sheets when the rising interest-rate cycle that triggered the SVB crisis began, was substantially lower than that of their US and European peers.

³ The European Banking Authority provides data disaggregated by country for the euro zone.

Figure 4. Share of public debt on banks' balance sheets with maturities below five years

Source: the authors, based on data from the European Banking Authority, <https://www.eba.europa.eu/risk-analysis-and-data>.

Latin American banks have traditionally had to operate in a context of high macroeconomic volatility and have experienced, especially in the 1980s and 90s, recurrent financial crises.

In particular, the periods of high inflation in the 1980s and 1990s, and the often-failed attempts to stabilise it, had as a corollary a sharp fluctuation in interest rates that led Latin American banks to manage duration risk particularly carefully.

This has been done in different ways. [As the credit rating agency Standard and Poor's recognises](#), Latin American banks are particularly accustomed to inflation, leading them to implement significant hedging operations and to hold floating-rate or inflation-linked bonds on their balance sheets. But certainly, another way to manage duration risk is precisely by holding bonds with a low residual maturity.

It could be argued that Latin American banks have chosen this strategy because the average maturity of government bonds issued in their countries is lower than in advanced economies. However, this does not seem to be a reason that can explain this behaviour for Latin American banks. While it is true that the average maturity of Brazil's public debt is less than four years, this is not the case for other countries such as Mexico and Colombia or Peru, as shown in Figure 5.

Figure 5. Average maturity of outstanding public debt

Country	Average maturity (years)
Brazil	3.70
Mexico	7.30
Colombia	9.80
Chile	6.30
Peru	13.30

Source: the authors, based on data from the Bank of Spain, <https://www.bde.es/wbe/en/estadisticas/>.

Carrying low duration risk on their balance sheets is thus a strategy for which Latin American banks have opted. It is a strategy that has shielded them from significant losses in the value of fixed-income securities in their assets as a result of the rise in interest rates that began in early 2022.⁴

The SVB crisis, Latin American banks and Spanish banks

Since the second half of the 1990s the main Spanish banks have been expanding their activities in various Latin American countries. As a result, Spanish banks now have a very significant presence in the region. In fact, for Banco Santander and BBVA, their presence in the Latin American region has already reached a clearly strategic value.

This is so to such an extent that the Santander and BBVA groups are now major players in the banking systems of the two main Latin American economies, precisely those on which this analysis is focused: Mexico and Brazil. In Mexico's case, the two entities account for more than 30% of the country's loans and deposits, with BBVA in first place and Santander in third. In Brazil, Santander is the largest foreign-owned private bank by volume of operations, with a market share of around 10%. In addition, in countries such as Chile, Colombia, Peru, Argentina and Uruguay, Santander has a combined market share of more than 10%.

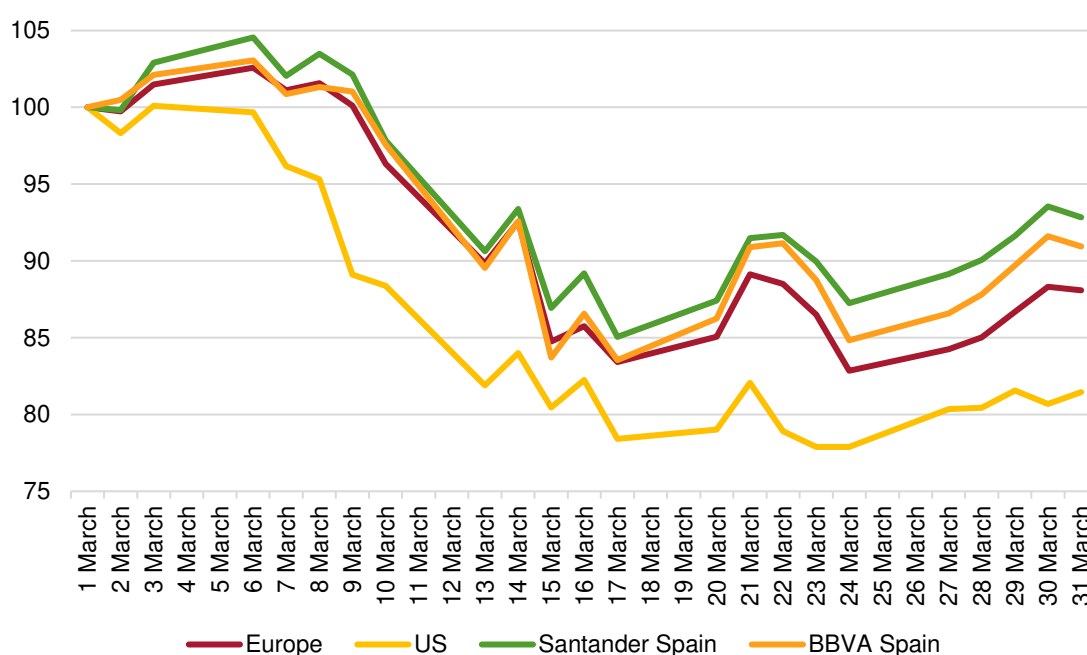
The presence of these entities in Latin America is also relevant from both the perspective of the volume of assets they concentrate in the region and from the point of view of profits.

⁴ Latin American banks hold government securities for liquidity reasons, which explains the demand for fixed-income securities with a relatively low residual maturity in order to protect the value of liquidity against market risk.

This geographic diversification in their activity towards Latin America has allowed Spanish banks, along with other factors, to better weather the impact of recent crises, such as the 2008-09 crisis, the euro zone sovereign debt crisis and COVID-19.

The latest SVB crisis has been no exception. As shown in Figure 6, the share prices of Banco Santander Spain and BBVA Spain outperformed their US and European counterparts during the SVB crisis. Of course, this differential performance is not attributable to a single factor. The Spanish banking sector's high capital and liquidity positions, its focus on the retail segment and the strong supervisory framework have all played in its favour. But everything points to the fact that the international diversification of the main Spanish banks has enabled them to better weather the financial turbulence.

Figure 6. Share prices of main banks (1 March = 100)



Source: the authors, based on data from Investing.com.

Conclusions

The financial turmoil unleashed in the US in the wake of the collapse of the SVB offers a unique perspective to understand the resilience that Latin American banks have developed.

It is a well-known fact that Latin American banks have high levels of capitalisation, more than double the Basel III requirements. What is less well known, and what this analysis highlights, is that Latin American banks operate with relatively low levels of duration risk and are therefore coping much better than their US and European peers with the upward cycle in interest rates that began in early 2022 and that has led to a significant drop in the value of fixed-income securities.

Unlike their counterparts in developed countries, Latin American banks are accustomed to operating in contexts of volatility and recurring crises. As a result, they have adopted a set of practices that make them more resilient to interest rate hikes: the average maturity of Latin American banks' government bond holdings is much shorter than that of their US and Eurozone counterparts. This, coupled with the fact that Latin American banks tend to accumulate floating rate or inflation-linked debt on their balance sheets, has made them much more resilient to duration risk and therefore to rising interest rates.

From a Spanish perspective, this is good news for domestic banks, many of which have focused their international expansion precisely on Latin America. Once again, it seems that the international expansion of Spanish banks has worked in their favour when weathering the financial storm.