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

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Abstract

This paper explores why Spanish banks internationalise 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 the 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.

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1. Introduction

Since the 1990s, *BBVA* and *Banco Santander* have undergone a huge 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 these two banks. Although we focus on the period of major internationalisation occurring from 1990 onwards, we adopt 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 the changes in the Spanish and Latin American financial sectors, occurring 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 Latin American region.

Although there are many cross-country studies focusing on different aspects of banking internationalisation, specific case studies could be very helpful in providing greater insights into the general results obtained by those cross-country analyses (Mulder and Westerhuis 2015). Case studies allow the researcher to examine in more detail the factors that encourage foreign banks' entry into new markets: the "follow the customer" hypothesis, regulatory changes, local market opportunities or links between foreign bank entry and other foreign direct investments, among other factors. Taking a long-run perspective, this paper discusses different hypotheses about the factors that affected the pattern and timing of Spanish banks' entry into the Latin American region. In particular, the paper focus on the role of remittance collection and economic integration as proxies for the "follow the client" approach, the local opportunities in the Latin American region and the changes in host country regulation. Some bank characteristics that affect foreign expansion decisions, such as size and profitability along with changes in Spanish regulation, are also considered. Finally, the paper discusses why other multinational banks did not compete (or competed to a lesser extent) for the Latin American market at this point in time, a situation that was exploited by the Spanish banks.

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 America 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 banking expansions. Although the Latin America region was definitely the natural choice for Spanish banks' internationalisation, we detail the factors that accelerated and give an unexpected boost to this expansion. Section 6 discusses the strategy of Spanish banks as compared to other transnational banks in the Latin American region. The conclusions are presented in Section 7.

2. Why banks internationalise

As Mulder and Westerhuis (2015) point out, banks have had an international presence ever since the Middle Ages. In the nineteenth century, there was a process of banking globalisation led by some of the big merchant houses such as Barings, JP Morgan and Rothschild, during which time these banks increased their foreign presence, mainly in the colonies. However, foreign banking investments declined in the interwar period and the process of banking internationalisation only re-emerged in the 1970s, before accelerating in the 1990s (Focarelli and Pozzolo 2005).

When analysing the banking internationalisation process, 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 local markets. Banks do not incur physical transportation costs in offering their products and services, but they do need to invest in some fixed costs, for example in offices (Buch and Lipponer 2006). A bank that decides to expand into other countries has to face certain costs related to the cultural, political, fiscal and economic differences, which mean that it has less knowledge about the host market than local competitors do, and coordinating its activity becomes more complex. However, this international expansion also has some benefits. There are a number of key advantages of banking internationalisation 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) but also go abroad to capture new clients in countries with underdeveloped financial systems and a low level of financial intermediation (an offensive expansion). 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, because they have a larger and more international customer base, involved in activities that are typically international (Focarelli and Pozzolo 2005). The second advantage is risk diversification. Banks attempt to diversify their portfolio internationally 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, and employ them in new emerging markets, at a relatively low cost (Mulder and Westerhuis 2015). Lastly, moving abroad helps banks to respond to the challenge of domestic rivals (a defensive expansion); in this case, the internationalisation strategy depends on the behaviour of competitors (Grubel 1977).

There are certain elements that have acted as push factors in banking globalisation processes, such as capital account liberalisation, financial deregulation, falling communication costs, financial innovation, and trade and financial integration[1]. Cull and Martinez Peria (2010) differentiated between four types of factors that act as drivers of foreign bank entry: 1) the "follow the client " approach or the desire of the bank to continue serving its clients in their overseas operations , b) profit opportunities in the host country, 3) the absence of barriers to foreign bank entry in the host country and 4) other factors that reduce the information cost of doing business abroad, such as a common language or cultural similarities between the home and the host countries. Moreover, the internationalisation process is also influenced by certain characteristics related to the size, efficiency and performance of the banks that expand abroad (Clark et al. 2003). As mentioned above, big banks are more likely to have multinational operations and customers that operate abroad and, therefore, they are more likely to follow their clients abroad. Moreover, banks need a minimum size in order to start their international forays and compete in global markets. Several studies, such as Tschoegl (1983), Grosse and Goldberg (1991) and Focarelli and Pozzolo (2000), have found a positive correlation between bank size and internationalisation. Efficiency and bank performance could also affect banking expansions abroad although the empirical evidence is not conclusive as to whether domestic banks are more efficient than foreign banks, or vice versa (Clarke et al. 2003). Whereas Dermiguc-Kunt and Huizinga (2000) and Claessens et al. (2000) show that foreign banks had lower profitability rates than local banks in developed countries, Kiraly et al. (2000) report that large foreign banks rank are among the most efficient banks, and Focarelli and Pozzollo (2000) find that profitability (measured as the bank's return on assets) is correlated with the international expansion. Moreover, 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

[1] In particular, for the most recent globalisation period, Lane and Milessi Ferretti (2008) highlight the creation of monetary unions such as the euro area as a factor driving international banking expansion.

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 Milessi–Ferretti 2008, Mulder and Westerhuis 2015).

Finally, home country regulations can also determine which banks internationalise. Local regulatory restrictions or, alternatively, financial deregulation processes that increase competition, could incentivise the bank to increase its presence in other countries. Other noneconomic aspects, such as linguistic and cultural similarities, are also correlated with the internationalisation pattern of banks, because such factors lower the information costs of doing business in a new market (Buch 2003, Focarelli and Pozzolo 2005).

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 (Barth et al. 2001 Clarke et al. 2003, Cerutti, Dell'Ariccia and Martínez-Peria 2007). However, although the advantages of cross-country analysis are evident, it is also important to consider some specific case studies to obtain evidence about how local conditions in the host countries could act as incentives for attracting foreign banking investments and to contrast whether the general conclusions stemming from cross-country analyses hold true for a specific case study.

3. The internationalisation of Spanish banks: LatAm as the "natural" choice for their international expansion

To analyse the main factors behind the international expansion of Spanish banks, it is necessary to draw a general picture of the main phases of Spanish bank internationalisation and thereby explore the changing drivers that have operated in each of these phases. In his study of the *Santander* expansion, Martín-Aceña (2010) made a distinction between the pre-1980 period and the period from 1980 onwards. In their paper about the *BBVA* and *Santander* international expansion, López-Morell and Bernabé Pérez (2018) differentiated between the pre-1980 period, the 1990s and the twenty-first century. Sierra (2007) identified two separate periods: a) from 1900 to 1992 and b) from 1993 to 2007. For the most recent banking globalisation period, Parada et al. (2009) distinguished between the late 1980s, the 1990s and from 1999 onwards. Each of these phases shows different characteristics and, as we explain in the following pages, the drivers that have influenced Spanish banking globalisation have historically changed alongside the shifts in international and external conditions. In order to study the timing and drivers of Spanish banking expansion, we differentiate between the pre- and post-1986 periods.

Banco Santander and *BBVA* changed somewhat over the two periods under analysis; indeed, the current *BBVA* and *Santander* are the result of previous mergers. In 1988, *Banco Bilbao* and *Banco Vizcaya* merged to create *BBV*. In 1991, *BBV* merged with *Argentaria*, a state-owned bank[2], to form *BBVA*. That same year, *Banco Central* and *Banco Hispano* merged to create *BCH*, and in 1994, *Banesto*, a bank that 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*, we concentrate on a number of aspects that the theoretical and empirical literature have identified as the main determinants of banking internationalisation: a) the economic integration between the home (Spain) and the host countries as a proxy for the "follow the client" approach, b) the profit opportunities in the host countries, 3) the host country regulations, 4) other factors that could affect the pattern of expansion such as a common language or cultural similarities between the home and the host countries, 5) the bank

[2] *Argentaria* was the bank created 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 a la Construcción*, *Banco de Credito Local de España* and *Caja Postal*.

characteristics that affect their foreign expansion decisions, in particular, size and profitability, and 6) the changes in regulation in the home country. 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 LatAm the main region for Spanish banks' expansion. We maintain that the approaches of other competitors (the US, British, French, German or Japanese banks) left Spanish banks with greater room for manoeuvre in their globalisation process during the 1980s and 1990s.

4. Before 1986: the initial phase

In the pre-1986 period, particularly the period up until 1970, Spanish banks had a limited presence abroad. They extended their overseas activities through representative offices, but these offices did not deal with local clients, the volume of investment abroad was low, banks took small risks, and the profits linked to these foreign operations did not represent a substantial share of their total profits.

An important question is why Spanish banks did not adopt a more vigorous international strategy during this period. There are a number of potential explanations. Firstly, internal conditions in Spain did not favour overseas expansion. Throughout most of these years (especially after the Spanish Civil War), the Spanish banking sector had high barriers to entry, was strictly regulated and had a relatively low level of competition. In this context, banks achieved high rates of profitability and interest margins and thus were not incentivised to look for new markets[3] (Pons 2002, Pueyo 2003). Therefore, until the 1980s, the very protective domestic regulation, which ensured high profits, discouraged foreign banking expansion.

Secondly, the size of Spanish banking firms was not favourable. As Canals (1991) and

[3] 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)

Cardone-Riportella and Cazorla-Papis (2001) mention, the small size of Spanish firms prevented them from expanding internationally any earlier[4] (see Table 1). Only when Spanish banks had reached a sufficient size did they have enough financial resources to operate in international markets.

Table 1. Spanish banks and European and American banks: a comparison, in million US $

	1953	1960	1975
Spanish banks ($ m.)			
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 ($ m.)	**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 bank	4,142/6,064	5,182/7,463	33,108
Lloyds bank	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*)*. Own elaboration.

External conditions (or local conditions from the perspective of the host countries) did not stimulate Spanish banking investment overseas. Until the 1980s, most of the potential host countries (such as those in LatAm) had high barriers to entry that deterred foreign investment, and there were major interventions in their financial systems (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 certain LatAm countries such as Brazil and Mexico, the situation

[4] 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).

changed over the course of the twentieth century, especially after the Great Depression. In Mexico, for example, following the Mexican revolution, and also as a consequence of the changes in the financial context linked to the First World War and the monetary instability during the 1920s, there was an increase in risk and a decline in banking profitability that made foreign stockholders lose interest in the Mexican 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. This situation was typical in most LatAm countries, which, from the 1940s until the 1980s, had very interventionist banking regulations. This was the case not only in Mexico but also in Argentina and Brazil, among others. In Argentina, for example, the state interventionism in the banking sector that began in the 1940s reduced foreign banking activity[5].

Moreover, until the 1990s, the state-owned banks in LatAm held more than 50 per cent of total banking assets[6] (Tovar 2007). In Brazil, the banking system was nationalised during the 1920s, after which time the activity of foreign banks was extremely limited (Cortes and Marcontes 2016). Other countries nationalised banks during the 1940 such as the above-mentioned Argentinian case in 1946 or Costa Rica, which nationalised the banking sector in 1948. In the 1980s, there was a new wave of nationalisations, such as that in El Salvador (1980-1990) or Mexico (1982-1990) (Del Angel and Martinelli 2013). In this context, with very restrictive regulation and a strong presence of state-owned banks[7], the incentives for foreign banks to enter the region were weak. Most LatAm financial systems in the second half of the twentieth century can be characterized as repressed by severe institutional arrangements that

[5] In Argentina, private banks were nationalised in 1946, during Perón's first presidential term; later they were de-nationalised during the "*Revolución Libertadora*" before being re-nationalised in 1973 (Rapaport, 2010).
[6] 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).
[7] 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, or in Venezuela in 1995 as a consequence of the banking crisis, but Venezuelan banks were re-privatised in 1996 and 1997 (De Krivoy 2003).

forced public and private agents to access foreign debt markets in order to meet their financing needs. Hence, financial repression acted as a restrictive factor for financial sector development.

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 Trainer (2001); for Brazil, Cortes and Marcondes (2016); for Argentina, Rapoport (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).

Zegarra (2014) affirms that the low level of development of the LatAm financial system and the minimal presence of foreign banks in this region was also linked to the low demand for banking services and the underdevelopment of the financial system (Table 3). 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 LatAm countries in the 1970s and the "lost decade" of the 1980s (Batiz-Lazo et al. 2007). In fact, during the 1980s, there were systemic banking crises in Argentina, Chile, Colombia and Uruguay, and there was also banking distress in Ecuador, Bolivia and Mexico (Morris et al., 1990).

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 LatAm[8]. 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 (Martin Aceña 2010). It was not until the 1940s that *Banco Santander* once again turned its attention to LatAm. As Table 4 indicates, *Banco Santander* substantially increased its activity in LatAm during the 1970s (Dominican Republic in 1976, Costa Rica in 1977, Guatemala in 1977, Puerto Rico in 1977, Ecuador in 1979 and Uruguay and Chile in 1979) although the economic difficulties prevalent in the region during the 1980s forced the bank to restructure its presence. In the pre-1986 period, the bank primarily concentrated its

[8] Although *Banco Hispano Americano* (which later merged with *Banco Santander*) indicated in its deed of constitution (1900) that the aim of the bank was to finance Latin American trade, and 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 (Tortella and García Ruiz, 1993 and Table 1)

activity in Puerto Rico, followed by Chile and Panama. However, the banks that later formed *BBVA* did not have a significant presence in LatAm, with the exception of Panama (1982).

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 Panama*	
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, 2010), *Banco Bilbao* and *Banco Vizcaya:* Arroyo et al. (2012).

There were two main drivers of banks' internationalisation in this period: to provide a service to their clients overseas and to use the experience accumulated in the domestic and first experiences in the international markets in the later expansion stages. To analyse the follow-the-client motive, we consider the importance of emigration and trade conditions. In the pre-1986 period, one of the key drivers of Spanish banking internationalisation was the remittances sent home by Spanish emigrants (Sierra 2007). At the beginning of the twentieth century, Spanish emigration to South America grew at a rate of around 10 per cent annually between 1900 and 1913, with Argentina, Brazil, Cuba and Uruguay being the main destinations (Sánchez Alonso 1995). The total number of migrants from 1882 to 1930 was 3,471,755, although a very high proportion later returned home (2,114,496 migrants) (Sallé 2009). The flow of emigration dried up during the First World War, and especially the Spanish Civil War. However, during the Civil War and the years immediately after, there was significant migration for political reasons (the migrants known as "*exiliados*"), and LatAm was again the main destination, particularly Mexico, the Dominican Republic and Chile (Abellán 1983)[9]. There was also a new wave of emigration to LatAm 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 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 LatAm were significant and one of the main factors attracting some Spanish banks to the region; in particular, for *Banco Santander* (Martín Aceña 2007). Emilio Botín made his first visit to the Americas in the 1940s, where he realised that the Spanish expatriate communities and, in particular, remittances, represented a promising business niche (*Acta Banco Santander* 7/09/1955).

[9] 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).

Emigrants were also important clients for *Banco Hispano Americano*, channelling almost 500 million *pesetas* per year through migrant remittances before 1913 (Tortella and García Ruiz 1993). The bank's main presence in LatAm was in Argentina, the primary destination of Spanish migrants until 1913. In the case of *Banco Santander,* the bank expanded into Cuba, Mexico, Brazil and Venezuela, while the principal destinations for Spanish migrants were Argentina, Brazil, Cuba, Uruguay, Mexico, Dominican Republic, and Venezuela; that is, with the exception of Argentina, *Banco Santander* had a presence in all the countries with the highest immigration rates.

According to Esteve and Khoudour-Costeras (2009), there is little literature on the effect of remittances on financial development in nineteenth-century Europe. In fact, informal transfers were very common: migrants used to send banknotes by regular mail or entrusted an envelope with cash to family or friends who were travelling back home. As Salle (2009) mentions, until the beginning of the nineteenth century, the Spanish banks played a minor role in the remittance distribution services. Indeed, it was the merchant banks ("*comerciantes banqueros*")—which gradually transformed into banking houses—that specialised in these operations (García López 1992). At the turn of the century, some newly-established banks started to carry out remittance activities, such as the above-mentioned *Banco Hispano Americano* (founded in 1901), *Crédito Ibero Americano* (founded in 1903) and *Banco de Gijón* (founded in 1901). García Lopez (1987) indicates that the Asturian merchant banks and banking houses received substantial amounts of remittances (although he does not offer precise data). At the beginning of the twentieth century, a foreign bank, *Banco Español del Río de la Plata*[10], opened several branches in Spain to take advantage of the remittance business (in Madrid in 1918, and as noted by Maixé et al. (2003), in A Coruña, Pontevedra and Vigo)[11].

[10] A priority service for these banks was the sending of remittances abroad, particularly to locations in Spain to which Spanish residents in Argentina used to transfer money (Iglesias 2012).
[11] For a more detailed analysis about the presence of foreign banks in Spain in this period and their activities, see García Ruiz (2001).

Unfortunately, as discussed above, although we have qualitative evidence on the importance of emigration for banking expansion in LatAm, we cannot quantify Spanish banks' remittance activities.

Another possible determinant of financial expansion is trade integration. As Lane and Milessi- 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.

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*	77.0	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)

Although Spanish banking investments abroad were concentrated in LatAm, from 1900 to 1984 this region's share of total Spanish trade fell in comparison to other regions (Table 5). In their early years, some Spanish banks, such as *Banco Hispano Americano* and *Banco Santander*, were linked to LatAm and Spain's ex-colonies (serving the *indianos* or Spaniards who made their fortune across the Atlantic) (Tortella and García Ruiz 1993) but later on this market became less commercially attractive. As can be seen in Table 5, LatAm's share of total trade remained fairly steady (and even fell in the case of exports) over the pre-war period and into the second half of the twentieth century. Thus, we cannot claim a clear correlation between trade and the presence of Spanish banks in the LatAm region.

Although from a macroeconomic perspective there is no available evidence about the influence of trade on banking expansion in LatAm, certain banks engaged in significant trade with this region. For example, as Marichal (2017) point out, trade with LatAm was a special business area for *Banco Hispano Americano,* a bank which became one of the key financial links between Spain, Cuba, Mexico and Argentina. However, as with remittances, there is little evidence of how Spanish banks helped Spanish exporters in their trade with the LatAm region.

5. After 1986: the great expansion

From the mid-1980s, the Spanish banking sector experienced profound changes. These transformations boosted its internationalisation process: the total assets of *Banco Santander* in the LatAm region increased from 2.7 billion US dollars in 1985 to 50.3 in 1999 and to 141.9 billion US dollars in 2007. In the case of *BBVA*, assets more than doubled from 0.43 billion US dollars in 1999 to 100.2 in 2007. *Santander* and *BBVA* started their international expansion in this period, 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 banks 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[12], 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 banks such as Citibank, which focus on a minority of the population: high-net-worth households and investors (Citi Report, 2017).

The geographical pattern of *Santander* and *BBVA* locations in LatAm in the post-1986 period is shown in Table 6. *Santander's* activity is distributed among different countries (Argentina, Brazil, Chile and Mexico) whereas *BBVA*'s activity is more concentrated in Mexico, although is has also presence in Argentina and Brazil. It is interesting to observe how

[12] 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.

Banco Santander and *BBVA* show different patterns of geographical distribution, although they do compete in some countries.

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)	**1995** Mexico, *Probursa* (A)
Banco Mercantil (A)	Peru, *Banco Continental* (A)
1996 Peru, *Banco Santander Perú*	Uruguay, *Banco Francés*
(*Banco Interandino* + *Banco Mercantil*) (M)	**1996** Argentina, *Banco Francés* (A)
Argentina, *Banco Tornquist* (A)	*Corp Banco Argentina* (A)
Mexico, *Banco Santander Mexicano*	Colombia, *Banco Ganadero* (A)
Paraguay, *Banco de Asunción*	
Puerto Rico, *BCH Internacional* (A)	
Uruguay, *Eurobanco* (A)	
1997 Venezuela, *Banco Venezuela* (A)	**1997**, Venezuela, *Banco Provincial*
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*	
1998 Brazil, *Banco Noroeste* (A)	**1998** Brazil, *Banco Excel Economico* (A)
Argentina, *Banco de Galicia y Buenos Aires* (A)	Chile, *Banco Hipotecario* (A)
1999 Bolivia, *Banco Santa Cruz*	
Mexico, *Bital*	
2000 Mexico, *Grupo Financiero Serfin* (A)	**2000** Mexico, *Bancomer* (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)	
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, 2008, 2010), Calderón and Casilda (2000), and Annual reports of *Santander* and *BBVA*

Several factors facilitated this international expansion. The Spanish banking system underwent a process of domestic de-regulation in the late 1980s. As mentioned above, there was limited competition among Spanish banks until the 1970s. Interest rates were regulated and banks used other mechanisms to compete, such as free commissions or opening more branches. Moreover, during the Franco period, regulation limited the entry of foreign banks. Banking liberalisation started in the 1970s with the elimination of interest rate controls, branch liberalisation, and the abolition of the compulsory investment coefficients. As a result, competition intensified. This process was first accelerated by Spain joining the European Economic Community (EEC) in 1986 and later by its membership of the euro area, as this meant that Spain had to adapt to European regulations. In 1989, there was a complete liberalisation of interest rates and commissions, a number of stock market reforms were introduced, and new measures were passed to regulate pension funds. The entry of foreign banks was liberalised, although these banks faced serious difficulties in expanding because of the large number of branches of Spanish banks. Moreover, competition increased not only among banks in general but specifically between banks and saving banks (Caminal et al.1990; Salas and Saurina 2003). The problem was that this increased competition took place in a saturated banking market (see Table 7) highlighting an evident need 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 (2011)

The abovementioned increase in competition had a clear effect on the net interest margins, which decreased by 40 per cent between 1997 and 2006: clearly a greater fall than the 24 per cent reduction in the same period in the euro zone countries or 27 per cent drop in the EU-15. One reason why the reduction in net interest margins was so large in Spain is because they were initially higher in Spain than in other countries; even after the fall, in 2006 the margin in Spain was the 5th highest in the EU-15 after Austria, Portugal, Italy and Greece (Fernández de Guevara and Maudos 2007)[13].

This increase in competition triggered a necessary reaction from Spanish banks, which were forced to adopt a more market-oriented business strategy to increase their profits. The first banking reaction was to increase bank size through mergers[14]. Secondly, as the adoption of the euro eliminated some traditional sources of revenues, such as currency trading or currency exchange commissions, banks were forced to offer new products other than deposits. These included investments, pension funds or, later on, highly complex financial products, such as derivatives, which increased the cost of funds and had a negative impact on profitability. They also tried to find other sources of revenue, such as commission for services rendered, or 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 (cash machines, phone banking…) and also to manage data, information, risk and marketing.[15].

The main reaction of Spanish banks to this increasing competition was international expansion. The merger processes facilitated the banking sector's international expansion. For example, the acquisition of *Banesto* by *Banco Santander* in 1994 put the resulting bank in a good position to expand overseas. Although Spain is in Europe and the other European countries are its main trading partners—even more so after Spain joined the EEC and later the

[13] The average net interest margin from 1990 to 1994 was 3.1 per cent in Spain whereas it was 9.2 per cent in Argentina, 8.3 per cent in Colombia, 8.1 per cent in Venezuela and 6.8 per cent in Brazil (Guillén and Tschoegl 1999).

[14] The result was the creation of big banks such as *BBVA* in 1991 or *Banco Santander Central Hispano* (*BSCH*) in 1999.

[15] *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. As Parada et al. (2009) explain, *Banco Santander* also developed a system for better monitoring credit risk that allowed prompt identification of bad debts, and the bank made an extraordinary effort to strengthen its retail businesses, for example, by encouraging clients to directly deposit their wages in their account and by identifying its clients' needs though information about their spending and income patterns.

European Union (EU)—the main receiving region for Spanish banks' investment abroad was LatAm (Tables 8 and 9). In some countries, such as Colombia and Chile, *Banco Santander* and *BBVA* have a large presence.

Table 8. LatAm: share of foreign banks in selected countries, 1998

	Total Assets (billion $)	% foreign ownership of assets		*BBVA* and *Santander* (% of total foreign banks)(*)
		Share of equity	Effective control	
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)

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

Several factors explain why LatAm has been the main focus of Spanish banking investments, especially after 1986. Firstly, as mentioned above, the prior emigration of Spaniards to LatAm was a determinant of Spanish banking interest in this region. Moreover, Spain and LatAm have a common history with a former colonial period and historical trade relationships. Secondly, there are additional cultural factors that imply some affinities in patterns and habits, as well as a common language. These 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). Thirdly, in the post-1986 period and especially at the turn of the century, certain market conditions made LatAm countries a favourable location for Spanish banking expansion.

5.1. Potential growth of the region and economic cycle

After the lost decade of the 1980s, the LatAm region experienced a relative improvement in terms of growth (see Table 10). Although the growth rates were not sustained and there were differences among countries, they came in marked contrast to the situation in the previous period (Minda, 2007). *Banco Santander* redefined its strategy from 1986 on by selling four entities in Costa Rica, Guatemala, Ecuador and Panama, and concentrating its activity in Argentina, Uruguay, Chile and Puerto Rico. In the second half of the 1990s, in a better macroeconomic climate than in the previous decade, *Banco Santander*, led by Santander Investment, accelerated its expansion in LatAm. Its investments in this region rose from 9 per cent of total assets in 1990 to 24 per cent in 1998, representing 30.6 per cent of total profits. From 1994 to 1998, *Banco Santander* invested 5 billion euros into the LatAm region. *BBVA* also achieved a major business expansion in LatAm in the 1990s, with Mexico being the country that received the biggest investments from *BBVA* in this decade.

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 et al. (2002), Penn World Tables.

At the turn of the twenty-first century, economic conditions in LatAm were more favourable, with more positive expectations[16]. Growth was accompanied by greater macroeconomic stability. Expectations were also positive about the expanding middle class. LatAm witnessed significant population growth, with a very young population, unlike developed countries with their aging populations (Calderón and Casilda 1999). As mentioned, 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 a very underdeveloped financial system (Table 11) with considerable potential for the expansion of bank branches and introduction of financial products. The percentage of the population with a savings account, credit card, or personal loan was very low. At that time, the banking penetration rate was 95 per cent in Spain and 35 per cent on average for LatAm (see Table 8). This also implied a relatively low level of competition in the LatAm banking sector (Guillén and Tschoegl 2007). Moreover, there were some profitable business niches such as the mortgage market and pension fund management (PwC 2011). Between 1981 and 2008, 11 countries introduced pension systems that partially or totally replaced the previous pension systems with private pension schemes (individual pension accounts managed by pension fund administrators): Chile (1981), Peru (1993), Argentina and Colombia (1994)[17], Uruguay (1996), Bolivia and Mexico (1997), El Salvador

[16] There were some exceptions. For example, at the beginning of the twenty-first century there were several problems in Argentina (with the *corralito* in 2001), Venezuela (when in 2008 President Chávez announced the nationalisation of *Banco de Venezuela*, the Venezuelan bank owned by *Grupo Santander*), Brazil and Uruguay. *Banco Santander* tried to maintain its position and to reduce risk; for example, it created a special 1.3 billion dollars fund to convert the entire book value of its Argentine banks. Economic as well as political instability drove *Banco 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 1.05 billion dollars. In the case of *BBVA*, despite its difficulties, the continuous threats of expropriation and the financial sector's risk exposure, the bank has declared it has no intention of leaving Venezuela (the last such declarations were made by Francisco Gonzalez, executive chairman of *BBVA,* in February 2018, in *El Nacional*)

[17] 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 and boosted the demand for liquid assets (Forero-Laverde 2017).

(1998), Costa Rica (2001), Dominican Republic (2003) and Panama (2008) (Mesa-Lago 2010)[18]. Data for the 2000s show that before the 2008 crisis *BBVA* was the biggest pension fund manager in LatAm; indeed, in some countries it had nearly 70 per cent market share of the pension fund business (Minda 2007)[19]. In 2012/13, however, *BBVA* sold part of its pension fund businesses in Chile, Colombia, Peru and Mexico, for a total of 4 billion euros, to strengthen its capital base (Financial Times, December 2012 and Reuters, April 2013).

Table 11. 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).

Finally, in terms of diversification, the LatiAm region represented a complementary area for the Spanish banks: whereas the Spanish economic cycle is highly correlated with that of the euro zone, it was negatively correlated with LatAm. A clear example of this complementarity is the positive evolution of Spanish banks' profits in LatAm after the 2008 crisis, a crisis which negatively impacted the Spanish market. 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.

[18] After 2008, Chile and Argentina introduced a re-reform to restructure their pensions system; for example, Argentina integrated again the precious private system into the public system.
[19] In fact, in 2010 *BBVA* had a 69.3 per cent market share in the Ecuadorian pension fund system, 52.8 per cent in Bolivia and 30.3 per cent in Chile (Hernansanz and Sebastian 2000).

5.2. Capital controls

LatAm governments, which had restricted the entry of foreign capital in previous decades, changed their position and considered the entry of foreign banks as an important instrument to tackle the shortage of financing and also to promote the modernisation and development of their financial systems. For example, Brazil passed a Banking Law in 1988 that eliminated barriers to entry into the national financial system for foreign banks (Nyasha and Odhiambo 2013). Similarly, in Colombia in 1990, Law 45 eliminated restrictions on foreign investment in the financial sector and simplified the system for mergers, acquisitions and liquidation of financial intermediaries (Forero-Laverde 2017).

5.3. Regulation

As a consequence of the package of measures linked to the Washington Consensus, a process of deregulation and liberalisation took place in the LatAm countries. As Moguillansky and Studart (2004) remark, between 1985 and 1995 there was a "first generation" wave of reforms resulting in the liberalisation of interest rates and fewer barriers to entry, among other measures, in countries such as Bolivia and Costa Rica (1985), Ecuador (1986), Mexico (1988), Argentina, Brazil, Venezuela (1989) and Peru (1991). Only Chile and Uruguay had started their liberalisation processes 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-liberalized from 1985 (Barth, Caprio and Levine 2013, Moguillansky et al. 2004, Paez 2004)

These reforms also included the privatisation of the state-owned banks (Chile 1985-89, Mexico 1991-92, Argentina 1994, Brazil 1998-1999). In this sense, case studies can provide interesting insights into how banking privatisation facilitated the entry of foreign banks in those years and the differences in terms of banking privatisation among LatAm countries. For example, Brazil's privatisation process was less intense than other countries in the region; indeed, the two largest banks in terms of assets, *Banco do Brasil* and *Caiza Economica Federal*, were still public in 1995 and as late as 2015, respectively (Cortés and Marcondes 2016). However, it is clear that the growing presence of *Banco Santander* in Brazil started with the privatisation process. In 2000, *Banco Santander* 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 the same vein, in 1995 *BBVA* bought *Banco Continental de Perú*, a bank that had been privatised by the Peruvian government three years earlier. Similarly, it was after the process of privatisation that foreign banks such as *BBVA* acquired the largest Mexican banks (*BBVA* 2008).

This de-regulatory process also coincided, however, with the withdrawal of the US banks from the LatAm market, partly due to the impact of prudential limits on bank exposure to specific risk in some countries such as Brazil, Argentina and Mexico. Later on, there was a wave of "second generation reforms" that were introduced in the second half of the 1990s as a consequence of the problems of instability that emerged in those years. These reforms were mainly introduced to strengthen the mechanisms of control and supervision and to facilitate new areas of banking activities and operations. These regulatory changes encouraged the entry of foreign banks in LatAm (Correa 2004).

Finally, although the situation differs substantially among countries, the banking de-regulatory 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).

5.4. Price and returns

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

Additionally, the LatAm region offered increasing returns. The net interest margins were considerably higher than in Spain. For example, from 1990 to 1994 they were above 5 per cent in LatAm (5.1 per cent in Mexico and 9.2 per cent in Argentina) and only 3 per cent in Spain (Goldstein and Turner 1996)[20]. 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 2.28 billion dollars), whereas in Argentina it was 1.96 billion dollars 1.72 billion dollars in Chile and 2.05 billion in Mexico. The spreads in LatAm countries remain high, with Brazil and Peru being the two countries with the largest interest rate spreads. For example, in 2014 Brazil had the highest spreads at over 15 per cent, with an ROE of around 20 per cent for the largest banks (IMF 2016) whereas in Spain in the same year, banks had an ROE of around 6.6 per cent (Bank of Spain 2017).

5.5. Other Spanish foreign investments

The LatAm region was not only the main destination for banking investments but also a key target of other sectors. The first big Spanish investment in LatAm was by *Telefonica*, followed by *Iberia* (via privatisations), while other firms such as *Endesa*, *Iberdrola* and *Repsol* also expanded in this region. The massive entry of multinationals into LatAm during the 1990s acted as an incentive to the banks that followed them to provide financial services (Minda 2007).

[20] 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).

5.7. Other factors: some recent events

The entry into LatAm 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). However, after the Great Recession, there was 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 LatiAm has better withstood the impact of the crisis. As Ichiue et al. (2016) affirm, the decline in banks' international activity can be traced back to the new regulations introduced after the 2008 crisis. These new regulations have mainly affected capital requirements, which can explain the restructuration 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 and economic risks). *Banco Santander* made some divestments in 2009 in Chile (with the sale of *Credit Portfolio*) and Venezuela (with the sale of *Banco de Venezuela*), and in 2012 in Colombia (with the sale of *Banco Corpbanca Colombia*). That said, other banking institutions made similar decisions: for example, Citigroup (2009), *Credit Agricole* (2012) and JP Morgan (2011) in Argentina; Royal Bank of Scotland in Chile (2010) and Colombia (2010); HSBC in Costa Rica (2012), Honduras (2012) and Panama (2013), among others (IMP Report 2016).

The 2008 crisis has, therefore, forced banks to become more selective in terms of international expansion and portfolio decisions. As Claessens and van Horen (2012) 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 banks' strategies. The future evolution of the LatAm market will be a crucial issue as *BBVA* and *Santander* redefine their strategies.

All of the abovementioned factors that fostered Spanish banking expansion in LatAm occurred at the same time as other transnational banks were focusing their attention on other regions. Given the importance of this aspect to the Spanish banking expansion strategy, we discuss it in detail in Section 6.

6. Spanish banks versus transnational banks in LatAm

Most of the abovementioned changes in LatAm conditions incentivised Spanish banks' entry into the market, but a key question is why all these factors did not attract other transnational banks in the same way. As Galindo, Izquierdo and Rojas-Suarez (2013) point out, 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 from foreign banks depending on their 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 a far smaller share (ECLAC 2002). In general, during the 1980s, US banks lost interest in expanding in LatAm and consequently reduced their investments in the region. As the ECLAC report (2002) explains, the debt crisis affected a large part of the US banking system and American banks' risk aversion discouraged them from investing in this region. As Sachs and Huizinga (1987) report, 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. 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. For example, FleetBoston (Bank Boston Corporation from 1997) was heavily involved in LatAm and suffered a severe crisis during the 1980s and 1990s 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 loan and investment portfolios in specific markets or products[21]. Moreover, most US banks that operated in LatAm in the twentieth century underwent a restructuring process during the 1980s and 1990s (for example, Citibank, Chase Manhattan, Bank of Boston and Bank of America), which absorbed a large part of their resources. Finally, 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 LatAm region did Citigroup begin to adopt a more aggressive attitude, once again increasing its presence in this area from 2000 on.

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[21] 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 2018).

By contrast, European banks were less involved in the LatAm 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 to 2000 (Slager 2005). Some banks tried to take 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 some LatAm countries during the 1980s and 1990s, expanded in Europe (Italy, the Netherlands, and Austria) and the US, and from the 1990s in Eastern Europe. The Dutch banks also focused on Central and Eastern Europe (ECLAC 2002). With respect to the British banks, Midland Bank, which had been very active in LatAm, increased its overseas presence in European countries (Germany, France and Italy) and the US. However, the acquisition of a US bank with bad real estate loans and a substantial share of LatAm debt put the bank in a very difficult situation, which forced it to end its international forays (Green and Holmes 1986). Also, Lloyds[22] 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). With respect to the Japanese banks, they went 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. Regarding banks from other countries, the HSBC[23] expansion in LatAm started in 1997 when it bought banks in Argentina, Brazil, Mexico and Peru (Kiforenko 2016), while Scotiabank also entered the region in the 1990s in countries such as Mexico, Chile, Peru and Colombia (Connor 2017). To sum up, Spanish banks' urgent need to grow coincided with auspicious conditions in LatAm at a time when other competitors were focusing their attention

[22] Lloyds was one of the leading providers of credit to Brazil and Mexico (Jones 1993).
[23] 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).

on other potential markets. This cleared the way for *Santander* and *BBVA* to expand in the region.

7. Conclusions

Although the internationalisation process of *BBVA* and *Santander* intensified from the 1990s onwards, some of the banks that had been merged to form these two banks had 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 they needed to expand abroad. In both cases, Latin America was the first area they expanded into, and this region has been crucial for their internationalisation. However, *Santander's* process of internationalisation started before that of *BBVA* (or the banks that formed *BBVA*). In the pre-1986 period, *Santander* had a much more notable presence in Latin America than *BBVA*. *Santander*'s initial entry was aimed at providing its clients with the necessary services to carry out their operations abroad ("follow-the-client") but from the 1960s and especially in the 1970s, the bank looked for new growth opportunities and acquired some local banks in Latin America. There is fairly limited quantitative evidence on the activities carried out by the banks in Latin America in the pre-1986 years; in particular, although there is qualitative evidence about the importance of remittances for *Santander,* there are no precise data on this. The situation is similar with trade, in that there is little available information about how banks helped Spanish exporters in their trade with Latin America.

As shown in the paper, in the pre-1986 period, the banks that would later form *BBVA* had a relatively limited presence abroad. There are several reasons why Spanish banks did not adopt a more vigorous internationalisation strategy during this period. Firstly, the lack of competition in the Spanish banking sector, with regulation that ensured profits. Secondly, the small size of the Spanish banks. Thirdly, external conditions did not encourage Spanish investment overseas because most of the Latin American countries had barriers to entry and other regulatory constraints. 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* have reinforced 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) but neither of these two banks reported a ratio above 30 per cent. However, the main difference arose between 1999 and 2006, when *BBVA* registered an increase in this percentage from 21.03 to just 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. The main difference was that whereas *Banco Santander* took majority stakes with the objective of ensuring full managerial control, *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 banks such as Citibank, which focus 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. *Santander's* activity is distributed among different countries (Argentina, Brazil, Chile and Mexico) whereas *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 key factors that facilitated the Spanish banking sector's international expansion in the post-1986 period. Firstly, the increase in domestic competition in a saturated market forced Spanish banks to expand abroad. Secondly, there was an increase in bank size. It was in this period when, thanks to mergers, Spanish banks became big enough to accelerate internationalisation. Finally, certain conditions made Latin American countries a favourable location for Spanish banking expansion: the potential growth of the region, the elimination of barriers to entry for foreign capital, a process of deregulation and liberalisation in the region, the lower purchase prices of the Latin American banks, the higher interest margins, and the mass entry of multinationals into Latin America during the 1990s, which prompted Spanish banks to follow their clients that were investing in Latin America at that time. The fact that other transnational banks (and direct competitors) focused their attention on regions other than Latin America gave Spanish banks plenty of room to manoeuvre in their international forays.

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