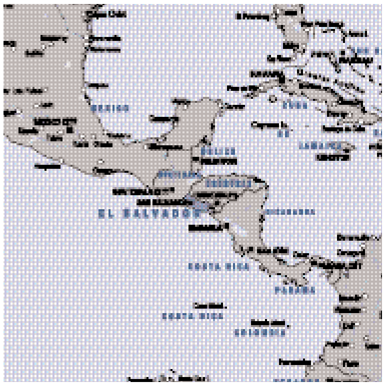
El Salvador



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The financial system of El Salvador

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The financial system of El Salvador includes commercial banks, certain state-owned banks specializing in incentive credit, insurance companies, broker/dealers, bonded warehouses, pension fund managers, financial leasing companies, factoring companies and the Salvadoran Stock Exchange.

In the early 1980s the government nationalized all commercial banks and savings and loan associations. By 1989 the system was essentially insolvent, and a new statute governing the operations of the Central Bank was enacted, along with laws that regulated financial institutions and provided for the conversion of existing unregulated credit institutions into fully regulated members of the new financial system after a three-year transition period. The Central Bank has, ever since, imposed on financial institutions capital adequacy requirements and other standards corresponding to the Basle accords.

Among the most important laws that regulate the financial system are the Law for the Superintendence of the Financial System, the Banking Law, the Monetary Integration Law, the Law for the Securities Market, the Organic Law for the Superintendence of Securities, the Law for Credit Institutions and Auxiliary Organizations, the Law for the Superintendence of Pensions, the Financial Lease Law and the Commercial Code.

Commercial banks

In 1999, the Legislative Assembly passed a new Banking Law that greatly improved transparency, reporting requirements and compliance with Basle standards. It also created a Deposit Insurance Agency, limited transactions of shareholders and officers with the banks and limited certain transactions to the banks so as to increase their responsibility. It regulates the organization and functioning of banks, their operations and services to the public, the restructuring processes in case of insolvency, the supervision of related companies and general measures that apply specifically to entities of this nature.

As of May 2004 there were 14 banks authorized to receive funds from the public. Nine of them were local and privately owned, two were state owned, two were foreign banks operating as branches and one was a savings and loan company in the process of becoming a bank.

Commercial banks and savings and loan companies are under the supervision of the Superintendence of the Financial System (the Superintendence) and are subject to periodic reporting requirements and mandatory audits. The minimum capital requirement to establish a bank has been doubled to $11.4 million, with an obligation to maintain 25% of its capital as reserve. Only in special circumstances and with the previous approval from the Superintendence will a bank be allowed to lower its capital, provided this does not drop below $11.4 million. By law, the capital adequacy requirement of 11.5% will increase to 12% in 2005. In addition, commercial banks are required to maintain a certain percentage of their deposits as a reserve deposited at the Central Bank in the form of cash or securities issued by the Central Bank.

The law prohibits banks from extending loans in excess of 25% of its capital to any single person or entity, with the exception of the Salvadoran government or the Central Bank. The law also limits loans for foreign investment to a maximum of 10% of the bank's capital, and limits the amount of loans to management and shareholders to 5% of the bank's capital. Mergers and acquisitions are allowed under the supervision of the Superintendence. Anyone who intends to own more than 1% of the capital of a bank must be previously authorized by the Superintendence. Foreign ownership is also permitted but with limitations in the capital composition.

Capital markets

El Salvador's capital markets have grown in recent years as the financial system has modernized. However, retail trading of debt and equity securities of private Salvadoran issuers is relatively new and has remained limited so far. Most of the trading in El Salvador's capital markets involves the purchase and sale of government and bank securities. There is one stock exchange, the Salvadoran Stock Exchange, which opened in 1992, but functioned without a specialized securities law until 1994.

The Law for the Securities Market regulates the public offering of securities and its transactions, markets and intermediaries. The Superintendence of Securities has the overview control of the entities involved, such as the stock exchange and the brokerage firms. A public registry keeps records of the entities mentioned, the public issuers and their issuances. The exchange lists 58 companies and 13 public entities; last year approximately $7.8 billion of securities were traded.

In 2002, the Law for the Securities Market was amended to allow the more efficient negotiation of securities from other central American nations, to facilitate capital movements in the region and to improve access to the international markets. Foreign securities can be registered and negotiated in the stock exchange provided they comply with appropriate registration requirements, such as where the securities are already registered in the stock exchange of their home country – especially if the home country's securities market is better developed than the Salvadoran one.

Currency control regulations

Until 2001, the single monetary unit of El Salvador was the colon. With the enactment of the Monetary Integration Law in 2001, a fixed exchange rate was established between the US dollar and the colon at a rate of C8.75:$1. Moreover, the US dollar was adopted as a valid currency, and since then, both currencies are used by the public – for example, wages and payments can be paid either in colones or US dollars. The law requires that all financial operations, including the issuance of securities and accounting records must be expressed in US dollars. Devaluation and conversion risks disappeared, acting as an incentive for foreign investment. As of March 2004, approximately 93.2% of all currency in circulation in El Salvador was US dollars.

Mergers and acquisitions

These transactions are almost solely regulated by the Commercial Code, except when the merger involves a bank, in which case the Banking Law and other special laws regulate the transaction.

The resolution to merge must be taken at a general shareholders' meeting and must be published in the official gazette. Ninety days after the publication, new articles of incorporation must be signed, or the proper modifications in the articles of the absorbing entity must be executed in writing before a notary public for them to be valid. The transaction must then be registered in the Registry of Commerce.

Corporate and commercial

Recommended firms
FA Arias & Muñoz
Delgado & Cevallos
Guandique Segovia Quintanilla
Rusconi Valdez & Asociados
Espino Nieto Umaña & Asociados

FA Arias & Muñoz

FA Arias quite simply does more work in El Salvador than any other firm, working on the largest transactions and often coordinating deals across central America from its San Salvador office. The biggest recent takeover, for example, was the acquisition of Bell South in central America by Telefónica of Spain. FA Arias acted as local counsel on the deal in Guatemala, Nicaragua, Panama and El Salvador, directing the operation from its office in El Salvador. Other mergers and acquisitions work handled over the past year includes acting on the sale of several of wheat producer Famossa's subsidiaries, advising beverage business Industrias La Constancia on the merger of several local entities and acting for Aureos Central America Fund on the acquisition of a 15% stake in Avance Ingenieros. Francisco Armando Arias is the head of the corporate department and led the team on the first two of these deals.

The firm is also strong in banking and finance work. Recent examples are advice to DEG on granting a subordinated loan to Banco Salvadoreño, advising the lenders on a syndicated loan to Digicel and acting for the World Bank on granting a loan to construction company Metrocentro.

Founded in 1942 as Bufete FA Arias, the firm assumed its current form in 1998 when it merged with a Costa Rican firm led by José Antonio Muñoz and Pedro Muñoz. Arias now comprises five partners and 13 associates, and is the El Salvador representative in the Globalaw network of independent law firms worldwide.

Key contact partners
Francisco Armando Arias
Zygmunt Brett
Lilian Zelaya

Leading lawyers
Francisco Armando Arias
Zygmunt Brett

Delgado & Cevallos

A relative newcomer to the El Salvador legal market, Delgado & Cevallos has garnered a strong reputation for finance work in recent years, led by highly recommended partners Omar Ivan Martinez and Aquiles Antonio Delgado.

This work has included working on a commercial paper programme for Banco Cuscatlán, with the bank issuing notes to be held by Wachovia Bank and sold into the US paper market; advising Banco Cuscatlán again on an issue of notes backed by remittance flows from several US banks; and acting for Banco Agricola, the second largest bank in El Salvador, on an asset-backed securitization. In capital markets the firm also acted for Union de Bancos Cuscatlán Internacional on its listing on the Madrid stock exchange, the first central American financial group to do so. Delgado was also recently appointed as legal counsel to the financial and banking industry in El Salvador for the negotiations over the Central American Free Trade Agreement with the United States.

The firm has a good mergers and acquisitions practice, despite being better known for its finance work. Recent examples include acting for UBC International Corporation on its acquisition of Lloyds TSB's branches in Guatemala, Honduras and Panama, and advising Banco Cuscatlán on its merger with Panaholding Group, owner of Banco Panamericano.

Key contact partner
Ricardo Cevallos

Leading lawyers
Aquiles Antonio Delgado
Omar Ivan Martinez

Guandique Segovia Quintanilla

Guandique Segovia Quintanilla was set up in 1972 and today consists of three partners, 10 associates and one external consultant working from San Salvador. Competitors recommend partner Luis Nelson Segovia as a talented finance lawyer and Patricia Portillo as a rising star.

One of the firm's most important deals in recent years was working on Banco Cuscatlán's $100 million bond issue through Citibank. It was central America's first futures transaction to achieve a AAA rating from Standard & Poor's. Guandique represented Citibank alongside US firm Sidley Austin Brown & Wood.

The firm has a strong capital markets practice in general, other examples of work being advising the arrangers on three bond issues in 2002 and 2003: a $300 million issue in July 2002, a $451.5 million issue in October 2002 and one for $348.5 million in March 2003. The firm advised arrangers Credit Suisse First Boston and Salomon Smith Barney, led by partner Luis Nelson Segovia. Espino Nieto Umaña & Asociados advised the government.

Key contact partners
Luis Guandique Mejía
Carlos Quintanilla Schmidt
Luis Nelson Segovia

Leading lawyer
Luis Nelson Segovia

Rusconi Valdez & Asociados

Although some of Rusconi Valdez & Asociados' competitors say "the firm has not been very visible lately on deals," it did advise on a $240 million financing for a local utility company, an exchange of $500 million-worth of notes for an international telecoms corporation, and the first credit facility for a private mobile telephone operator in El Salvador – a $30 million deal arranged by the Inter-American Finance Corporation.

And other work includes coordinating an M&A deal across El Salvador, Panama and the Dominican Republic for the acquisition of a local data company, and two project financings – one for Citibank valued at $23 million and one for $60 million as a joint venture in El Salvador by two multinational electricity generating companies.

The firm was established in 1993 by the merger of two independent firms, headed by Piero Rusconi and Benjamin Valdez. It then merged with law firm Jaime Medina Minero & Asociados, a specialist firm for international advice, in 2001 and in the same year formed an alliance with Deloitte Touche Tohmatsu, becoming the central American partner for all of Deloitte & Touche's tax and legal services. Although the firm is young, Rusconi, Valdez and new partner Luis Medina each has over 30 years' experience working on corporate and commercial deals in El Salvador.

Key contact partner
Luis Medina

Espino Nieto Umaña & Asociados

Espino Nieto Umaña & Asociados is a market leader for intellectual property work, and has talented lawyers working in its tax and labour law departments, but is not traditionally known as having a market-leading corporate finance practice.

It has, however, advised the Republic of El Salvador on three bond issues: a $300 million issue, one for $451.5 million issue and one for $348.5 million. Guandique Segovia Quintanilla advised arrangers Credit Suisse First Boston and Salomon Smith Barney. Espino also advised telecoms company Digicel on its $80 million investment in the mobile phone market, to become the largest in El Salvador behind Millicom, France Télécom and Telefónica. It advised Duke Energy Corporation on the $75 million expansion of its thermal energy generation plant, and advised Pepsi-Cola on restarting operations with a new regional bottler after it ended its previous 40-year relationship.

The firm was founded in 1960 by Alfredo Espino Nieto, employs 12 lawyers, and is a member of both Club de Abogados and the State Capital Law Firm Group.

Key contact partner
Luis Miguel Espino