Colombia: A Developing Story

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Colombia, since declaring independence in 1810, has suffered periods of political violence which continue to this day. This is why, in last month's column (The Long Journey – Issue 195), I wrote that the country only had a developing, rather than a developed, democracy. Independence did not come easily and Simón Bolívar was only able to make the 1810 declaration a reality after his defeat of the Spanish at the battle of Boyacá in 1819.

Colombia, at that time, was known as Nueva Granada and it joined with Venezuela and Ecuador to create a federation called "Gran Colombia". It was Bolívar's dream to create a unified state that would rival the United States of America, which at that time was an emerging power. However, economic strains and political rivalry among caudillos (regional leaders) meant that by 1830 the federation, like Bolívar's dream, had collapsed and all 3 countries became independent nations. This was not smooth sailing for Colombia; domestic politics in the nineteenth century saw outbreaks of fighting between the anti-clerical Liberals and the pro-Church Conservatives. In the "war of 1,000 days" between 1899 and 1903, approximately 100,000 people were killed.

Things deteriorated further from then on. In 1948, the Liberals and the Conservatives became more extreme, with the Conservatives leaning towards fascism and the Liberals moving towards left-wing populism. Following the assassination that same year of the leftist leader, Jorge Eliécer Gaitán, the country entered the period known as "The Violence" which did not end until the 1960s by which time it is thought that between 200,000 and 300,000 lives had been lost. This unrest was the breeding ground for the Marxist rebellion and the environment in which drug trafficking came to the fore, personified by the Medellín and Cali cartels. Despite power-sharing deals between Liberals and Conservatives at the start of the 1960s, festering anger in some quarters contributed to the development of guerrilla groups.

In spite of all this, the economy has been one of the region's healthiest in the last few decades. Originally, Colombia's economy was based on coffee, until the country slowly industrialised with a concentration on textiles. Its finance ministers practised prudence, avoiding heavy indebtedness, and it is noteworthy that, during the regional crisis of the 1980s, Colombia did not have to reschedule its debt. Although policy missteps were partly to blame for a recession in 1998-99, the economy rebounded with strong support from Colombia's current president, Álvaro Uribe, whose government, since 2000, has applied orthodox, but market-friendly, policies. Public finances, however, are still weak and tax reform is needed. Unfortunately, the global economic downturn will exacerbate Colombia's fiscal and current-account deficits and Gross Domestic Product growth in 2009 is likely to drop below 2%. All of the country's leading markets for exports are, of course, also victims of the global downturn.

As if the financial challenges this year were not enough to handle, the country has recently experienced its "Madoff moment" following the exposure of some domestic pyramid schemes through which it is believed that up to two million people deposited over USD900 million. I should add that although Bernard Madoff is at the centre of a swindle in the US (referred to in last month's column – Issue 195), some of his investors were from Latin America. But it is David Murcia, head of the Colombian company, DMG Grupo Holding, who is at the centre of the most prominent pyramid scheme at this time and who, along with other officers of the company, has been arrested. The ensuing civil unrest forced the government to declare a state of "social emergency" allowing the president to rule by decree.

This time the violence in the streets was about pesos and not politics. Irate investors of another exposed scheme, Proyecciones DRFE (the Spanish initials for "Fast Easy Money in Cash"), went on the rampage and in 13 cities many offices were looted and shop fronts were torched. It is estimated that hundreds of thousands of Colombians had invested in this classic pyramid scheme which has left many of them penniless; as the recriminations flew, Colombia's chief financial regulator resigned. Although the investigation still continues, it is thought that up to USD200 million in deposits was received.

Besides Bernard Madoff, Latin Americans have suffered losses at the hands of another foreigner, Sir Allen Stanford, an American financier, who stands accused of perpetrating an international USD8 billion fraud. Wealthy people in Latin America invested heavily in the Texan's offshore investment schemes, and it is possible that in Venezuela alone, where the suspicions were first exposed, investors may have placed over USD2 billion in firms connected with the Stanford Group. As with the Madoff case, it wasn't the US Securities and Exchange Commission that caught up with Sir Allen. Alex Dalmady, a Venezuelan financial analyst, sparked the Stanford investigation after publishing a critique of Stanford International Bank in Veneconomía, a Venezuelan magazine. A friend had asked for his opinion before investing and what the SEC failed to see, Mr Dalmady apparently saw in less than an hour using the internet.

Stanford International Bank in Antigua, the jewel in Sir Allen's crown, had as its auditors, C.A.S. Hewlett & Co., a small Antiguan firm headed by Charlesworth Hewlett (now deceased). Several years ago Mr Hewlett had maintained a one-room office in Enfield, England next door to Zig Zag's hair and beauty salon. Sceptics might say that only offshore would one find such an auditing firm acceptable to regulators. What about the Jewish T-Bill (Mr Madoff's nickname), and his fund? Who audited the firm which has allegedly committed a fraud that is perhaps at least six times larger than the one Sir Allen is alleged to have committed? Mr Madoff's auditors (Friehling & Horowitz, CPAs, P.C.) comprised three people, including a secretary (Paul Stibbard discussed this in the March issue of Offshore Investment (Comment – Issue 194)). It is worth noting that USD50 billion in 2008 might have covered the US expenditure on the Iraq war for 4 months; or to put it another way, the US Federal Bureau of Investigations estimates that there were just under 10 million crimes against property in the US in 2007. The total losses applicable to property crimes amounted to USD17.6 billion, which comes to less than 50% of what Mr. Madoff has apparently cost his victims. There was nothing offshore about this – except for some of the victims.

One needs to remember that a generalisation points to a disposition and not a definite, so assumptions which form the basis of a judgement can certainly lead to distorted conclusions. Cynics of offshore business take note. I discovered that my US focus on the regulatory weakness in Delaware, for instance, (Man, Angels and Brazil – Issue 193) was a revelation to many professionals and in her March article (Challenges and Changes – Issue 194), Karen Wasson also referred, inter alia, to Delaware and double standards. The Luxembourg prime minister, like the Brazilian president, wants Delaware (not to mention Nevada and Wyoming) to be regarded as a tax haven.

I read recently that a US adviser warned Americans living abroad to beware weak regulatory regimes and the prevalence of dishonest practitioners outside the US. Around this time I also read of a virtuoso violinist, disguised as a busker, who played in a subway station but none of the passers-by stopped to listen. Their ears did not expect to hear such music in those surroundings, and particularly not from someone dressed as he was. In other words, expectations and assumptions, rather than facts, took precedence. I first wrote on this subject in September, 1996, (Toothless and Dangerous – Issue 69) when I reminded readers that a trustee's skill, not necessarily his location, was the key issue.

So let me say thank you to Mr Madoff because he has reminded us all that we should keep our perceptions in check. The late Somerset Maugham, writer, spy and socialite, would never have fallen for Messrs. Maddof's and Murcia's wiles, because, as he put it: "The nature of men and women – their essential nature – is so vile and despicable that if you were to portray a person as he really is, no one would believe you". It is a view shared, I'm sure, in 2009 by many duped and disillusioned investors the world over – and one that has, since 1810, been understood by the victims of violence in Colombia.

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