

The Venezuelan economy: Current Situation and Outlook

Pedro A. Palma



Amnesty International
London: March 2013
(Reviewed version: May 2013)



Acompaña las buenas decisiones...

Economic Imbalances

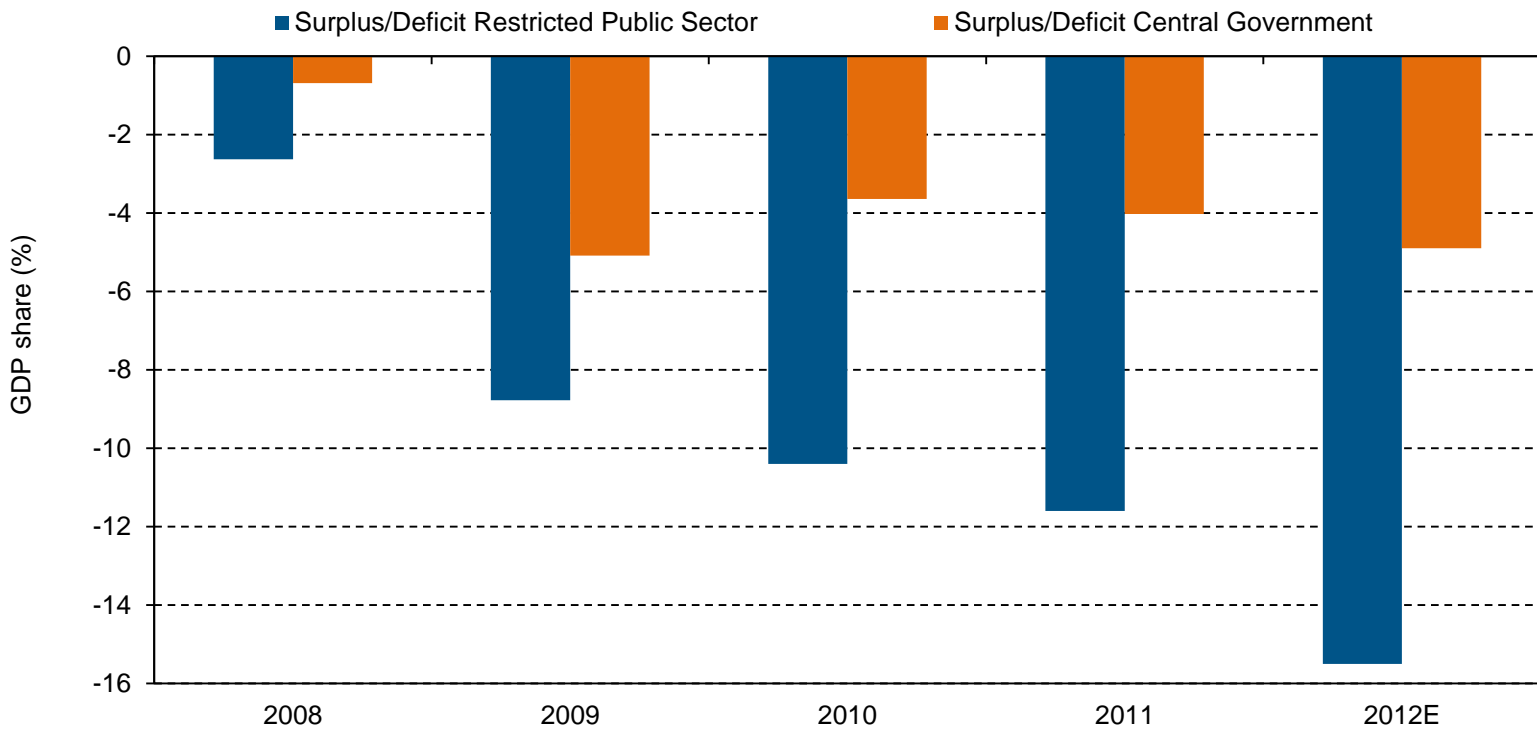
- Public finance imbalances
- Foreign exchange imbalance
- Monetary and financial imbalances
- Production and distribution (shortages) imbalances
- Imbalances between real supply and demand (high dependency on imports)
- Oil imbalances despite high international oil prices
- Political uncertainty

There will be a negative effect on the economy this year



Public finance imbalances

Restricted Public Sector's vs. Central Government's Fiscal Balance



Sources: MPF and Ecoanalítica



Acompaña las buenas decisiones...

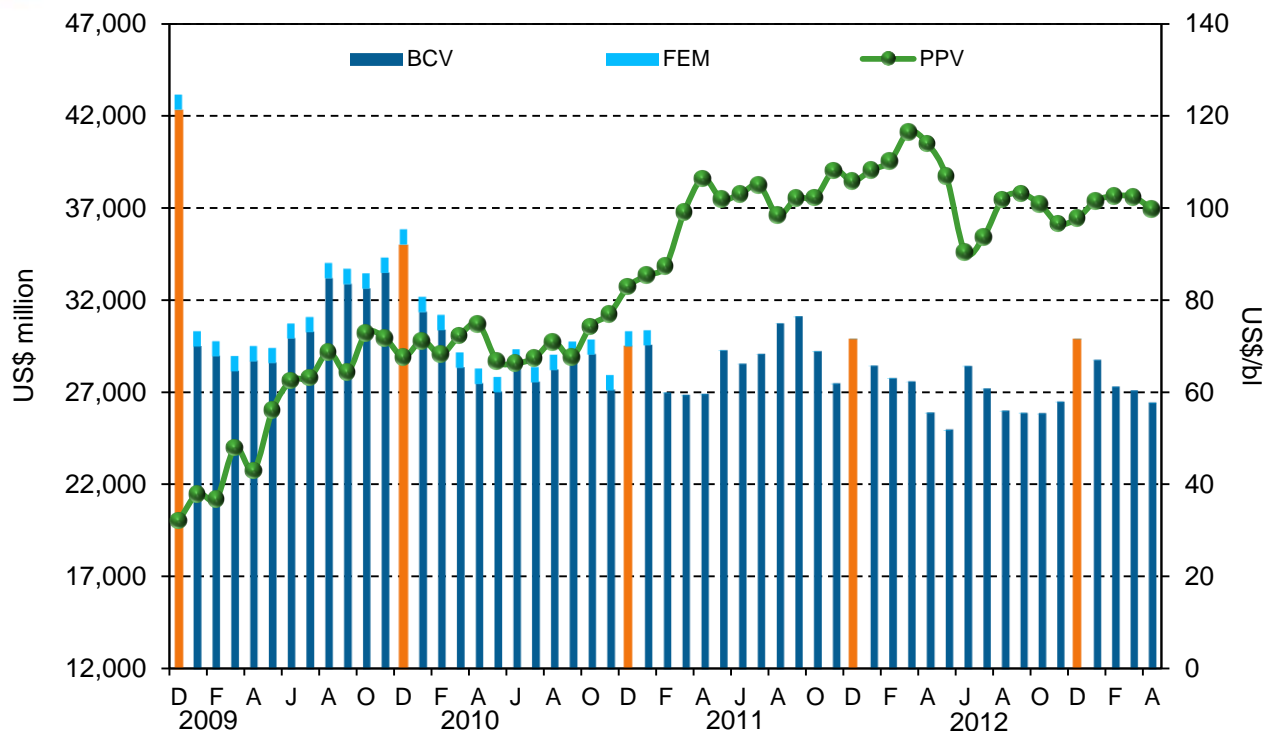
Answers to Public Finance Imbalances

- Spending rationalization
- Possible tax hikes
 - Income tax
 - VAT
- Possible new taxes such as the Bank Debits Tax
- Possible adjustments of public services tariffs and prices of public goods
- Adjustments to the official exchange rate (devaluation)
- Rationalization of domestic and foreign debt

Recessive and inflationary effects

Acompaña las buenas decisiones...

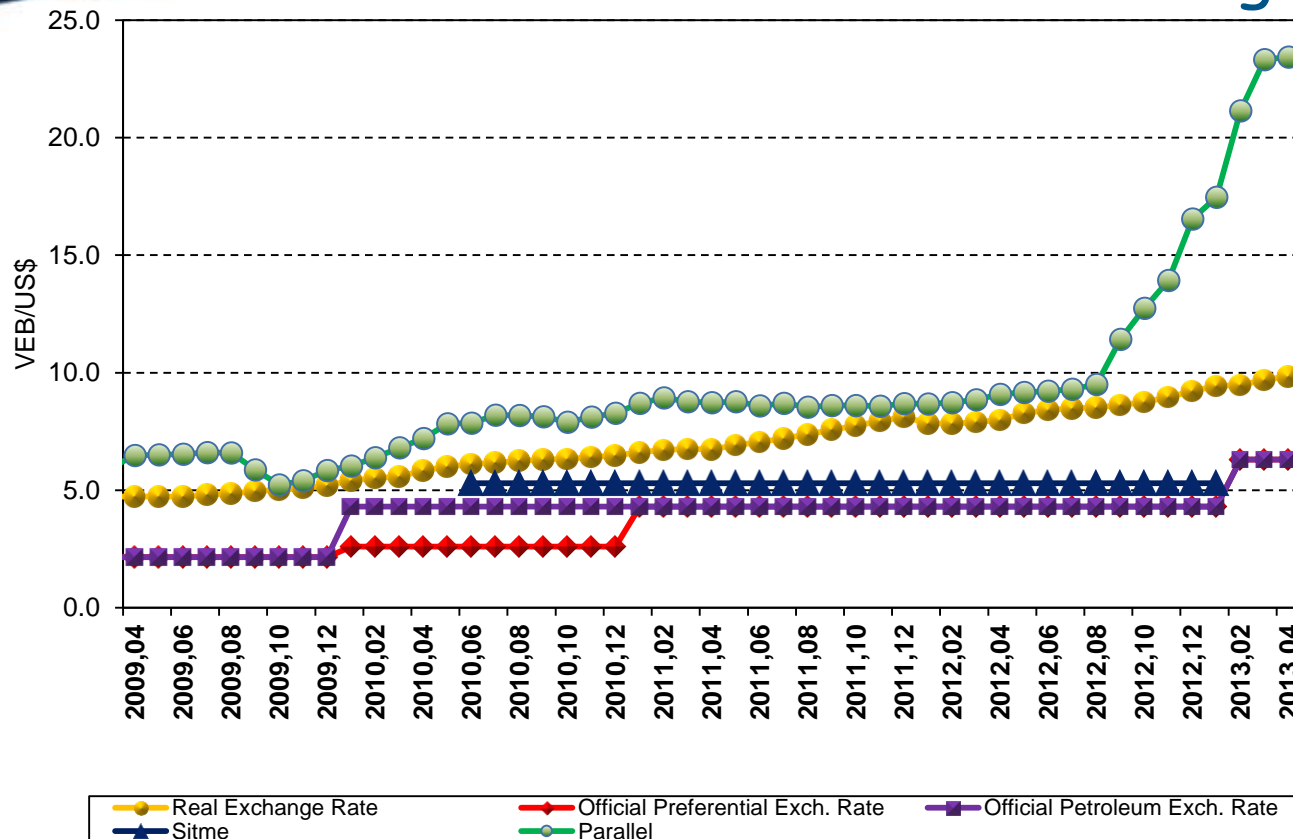
International Reserves and Oil Prices



Sources: BCV, MPPEP and Ecoanalítica

So far this year the average price for the Venezuelan oil basket is \$/b 102.45. During the week of May 13-17 that average oil price was \$/b 100.35. On May 16th the international reserves at BCV were \$ 25,574 MM.

	2009	2010	2011	2012
International Reserves (Million US\$)	35,830	30,332	29,902	29,890
Average Oil Price (US\$/b)	57.0	72.7	101.0	103.4



Sources: BCV and Ecoanalítica

On March 27th the first auction of the Complementary System of Foreign Exchange Administration (Sicad) was held (US\$ 200 MM), with an estimated implicit average exchange rate of VEB 14/US \$



Acompaña las buenas decisiones...

Answers to Foreign Exchange Imbalances

- Adjustments to the official exchange rates (announced on February 6th 2013)
 - Cadivi: from Bs/\$ 4.30 to Bs/\$ 6.30. (increased by 46.5%)
 - Elimination of Sitme and creation of Sicad
 - Bs/\$ 4.30 exchange rate reserved for some imports requested and authorized before Jan. 15, 2013
 - ✓ Authorized after 15 Oct. 2012: foods, health, commerce, communication, electrical appliances, telecom., IT, and media
 - ✓ Authorized after 15 July 2012: automotive, electricity, chemicals, construction, rubber and plastics, graphics, textile, paper, books, school supplies, machinery & equip., metal
- Additional controls on allocation of preferential dollars
 - Creation of the Higher Office for Optimization of the Exchange Control System
- Reduction of the exchange rates gap
 - Possible creation of an exchange mechanism managed by the BCV or the BVP
 - Possible legalization or flexibilization of the parallel market

Devaluation has effects on inflation and public finances

Effects of Devaluation on Public Finances

Nominal 2012 GDP	Bs. 1.64 trillion
External Public Debt at the end of 2012	\$ 105.78 billion
• Nominal GDP in \$ at the Bs/\$ 4.30 exchange rate	\$ 381.5 billion
• Nominal GDP in \$ at the 2012 real average exchange rate (Bs/\$ 8.50)	\$ 193.0 billion
• Public External Debt at the end of 2012 / GDP 2012 (real Exch. Rate)	54.8%
• Public External Debt at the end of 2012 / Export. of goods	108.7%
• Public External Debt at the end of 2012 / Internat. Reserves at year end	354%

Effects on public revenues

- Increase in fiscal revenues due to devaluation: Bs. 85 billion (4.1% of GDP)
- Increase of PDVSA's revenues because of devaluation
 - From sales of \$ to BCV at Bs/\$ 6.30: Bs. 90 billion ($\$ 45 \text{ billion} * 2 (6.30 - 4.30)$)
- Dilution of PDVSA's net debt to BCV in US\$ (at the end of 2012)
 - Bs 165.50 billion / 4.30 = \$ 38.37 billion
 - Bs 165.50 billion / 6.30 = \$ 26.19 billion
 - Dilution: \$ 12.18 billion (equivalent to a contraction of 31.7%)
- Dilution of Central Government domestic debt: \$ 18.83 billion (-31.7%)
(nominal domestic debt of the Central Government at the end of 2012: Bs. 255 billion) 8



Acompaña las buenas decisiones...

Effects of Devaluation

Positive effects for

- Exporters
- Public entities receiving revenues in \$
- Private debtors in bolivars who have \$
- PDVSA
 - Receives more bolivars for each dollar it sells
 - Its local debt is diluted
- Government (increased tax collection)

Negative effects for

- Importers (exchange tax)
- Debtors in foreign currency
- Consumers (higher inflation, loss of purchasing power of their revenues and more expensive preferential dollars)
- Multinational corporations with retained dividends in Bs
- Former Sitme beneficiaries (individuals and firms)



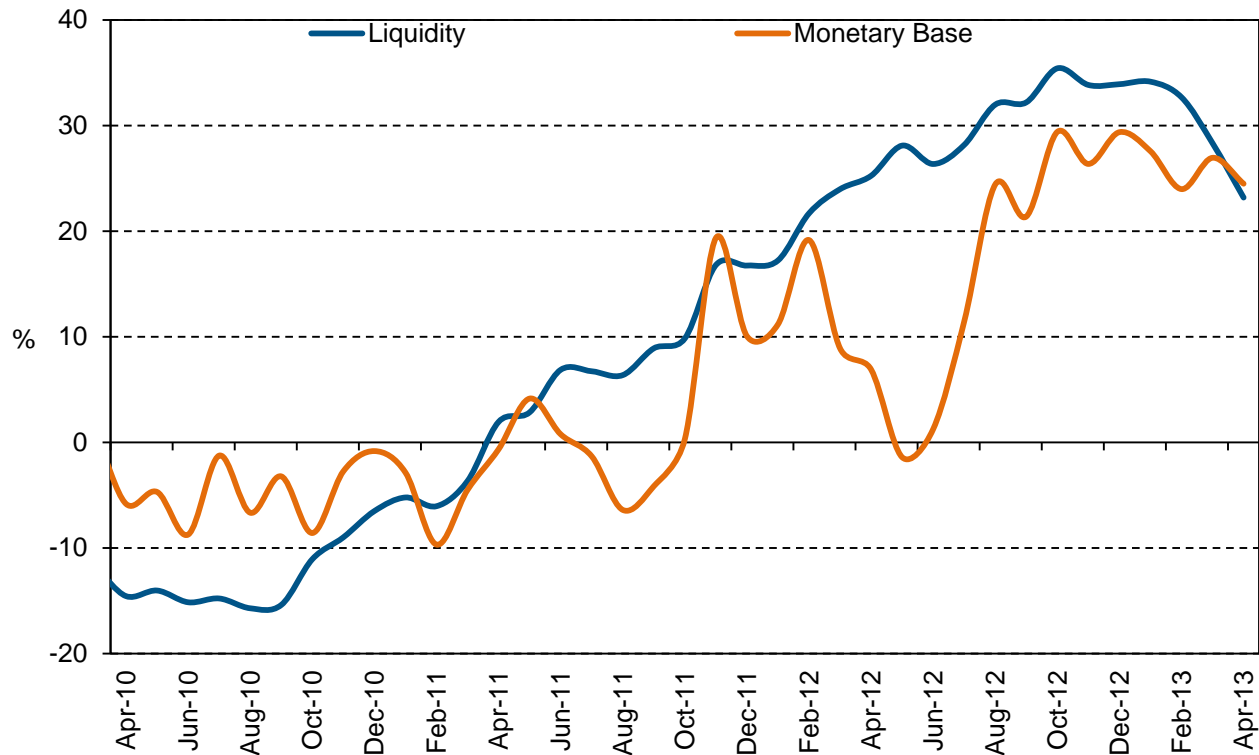
Acompaña las buenas decisiones...

Monetary and Financial Imbalances

- High increase of money supply
 - Nominal liquidity growth in 2012: 60.9%
 - Real liquidity growth in 2012: 33.9%
 - Nominal liquidity growth between April 2012 & April 2013: 63.7%
- High level of banking excess reserves: Bs 65.6 billion as of May 17th 2013
- High BCV's financing to public entities
 - PDVSA's net debt to BCV at the end of April 2013: Bs 170.8 billion
 - Net debt of other non-financial public sector firms to BCV at the end of April 2013: 18.6 billion
 - BCV's net loans to public sector firms at of end of April 2013 were equivalent to 75.9 % of the monetary base and 24.6% of liquidity (M2)

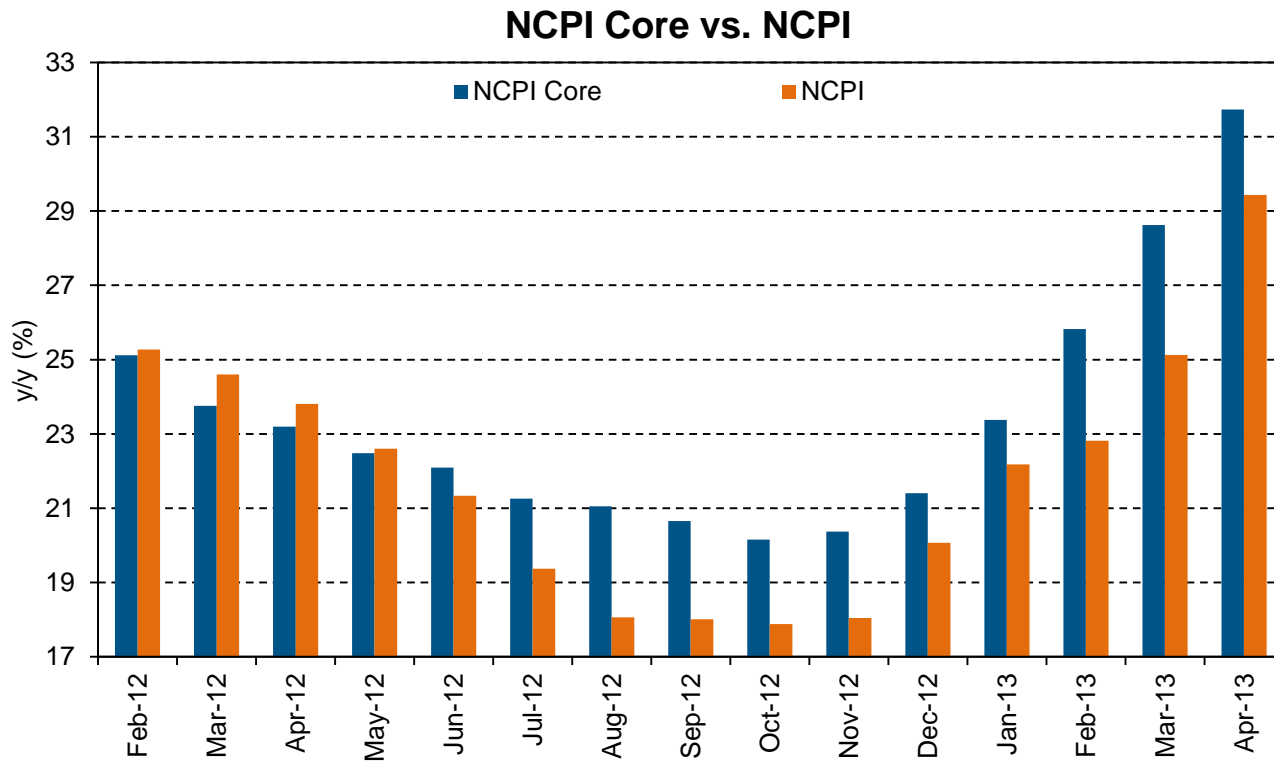
Monetary and Financial Imbalance

Monetary Base and Liquidity (M2) Real Growth (y/y%)



Sources: BCV and Ecoanalítica

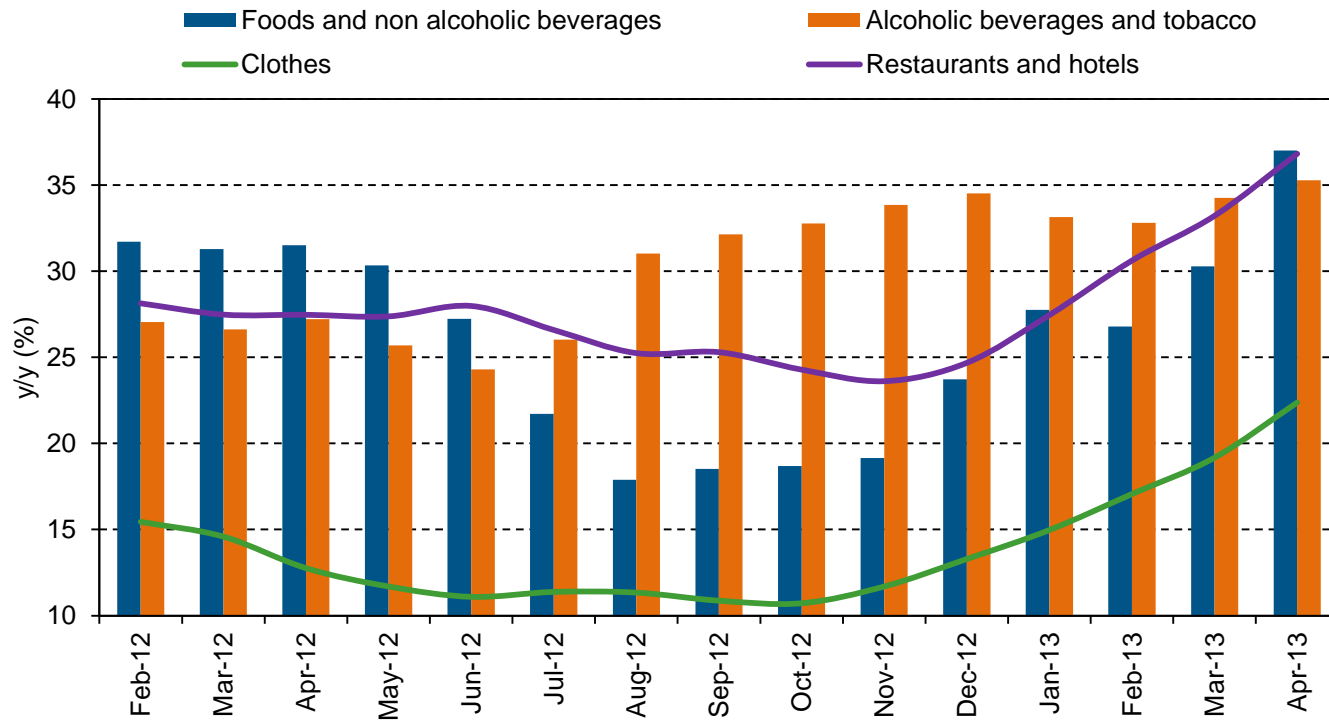
NCPI Core vs. NCPI



Sources: BCV and Ecoanalítica

Inflation by Item

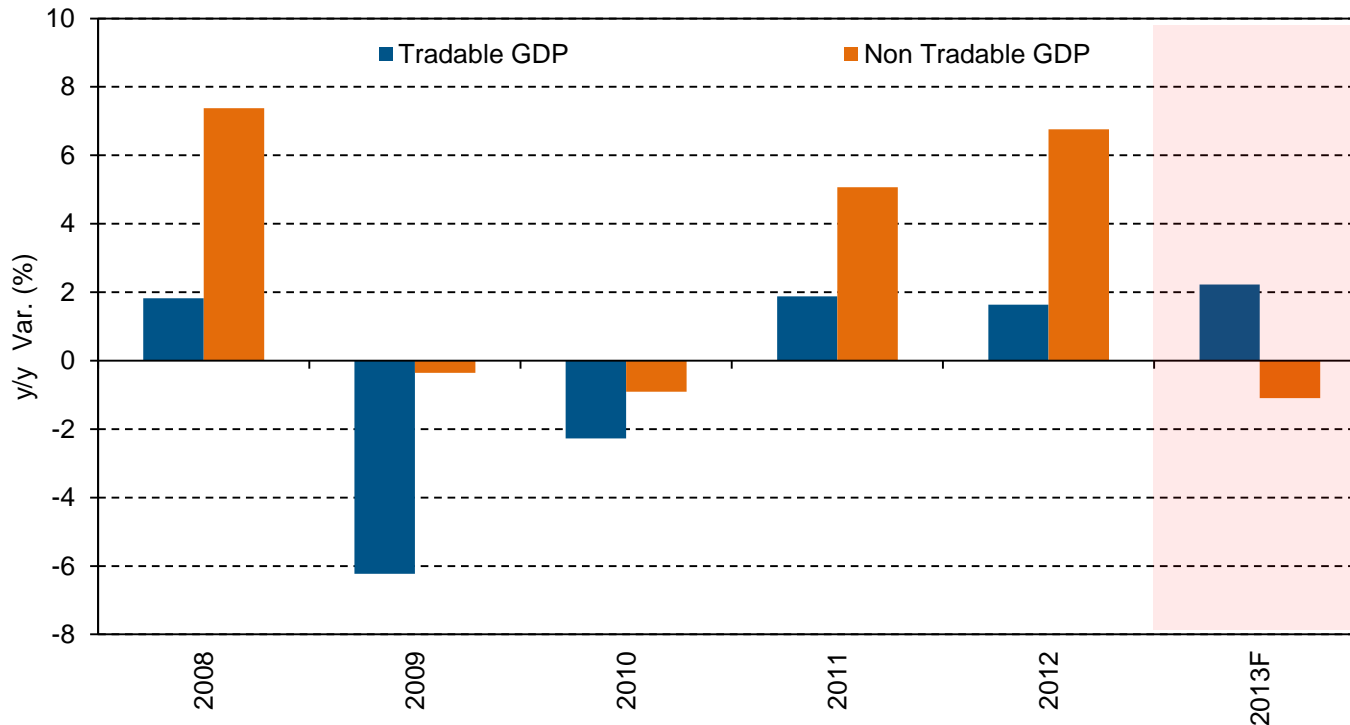
Inflation by Item



Sources: BCV and Ecoanalítica

Production and distribution imbalances

Tradable vs. Non-Tradable GDP Growth



Sources: BCV and Ecoanalítica



Acompaña las buenas decisiones...

Production and Distribution Imbalances

- Production of tradable goods has been severely affected
 - Loss of competitiveness due to a highly overvalued currency
 - Disproportionate price controls that have forced multiple produces to produce at losses
 - Production and distribution controls
 - Cumbersome requirements to obtain foreign currency
 - ✓ Non-domestic production certificate
 - ✓ Labor debt compliance certificate
 - Delays to obtain preferential dollars for imports
 - Increasing difficulties to obtain financing from foreign suppliers
 - Government harassment
 - ✓ Expropriation threats
 - ✓ Seizure of raw materials or products due to alleged hoarding
- Deterioration of production capacity due to expropriations of companies

The upshot: shortages and scarcity



Supply and Demand Imbalances

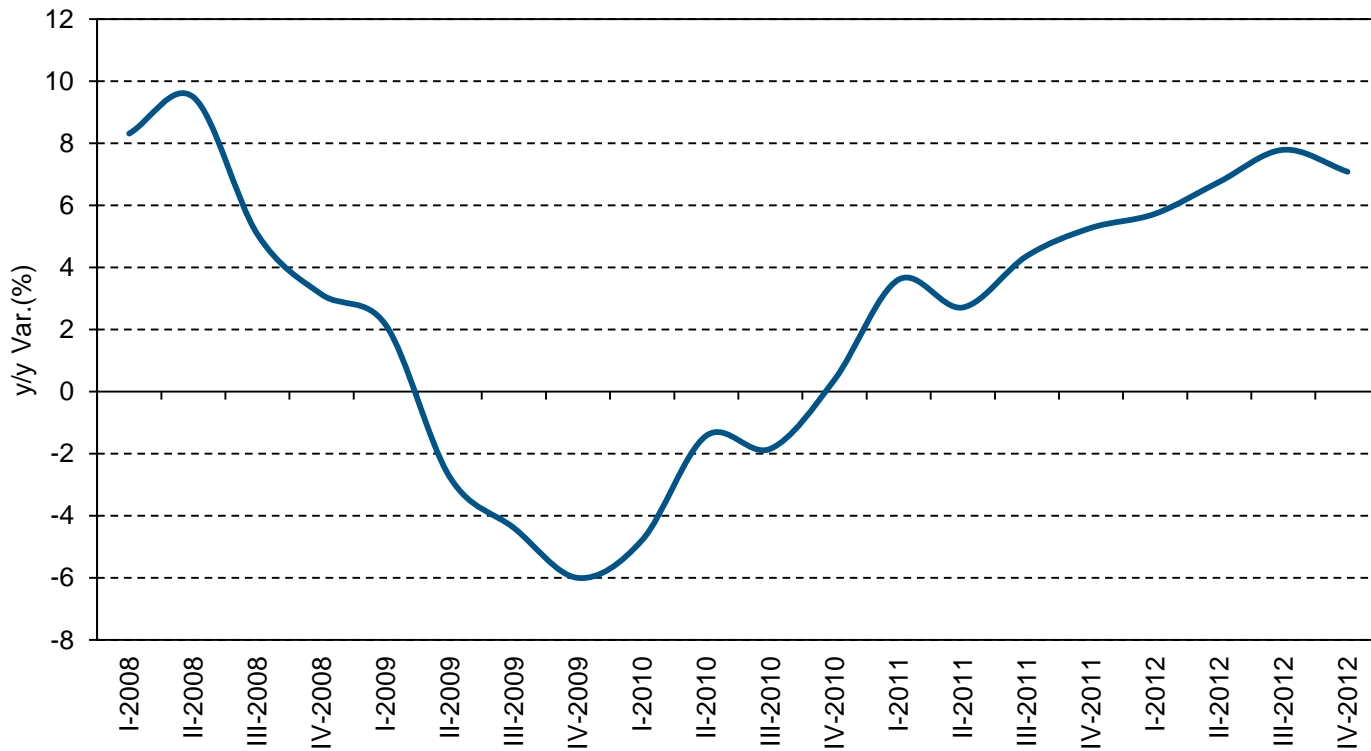
- Solid expansion of private consumption
 - Growth of money supply
 - Higher banks' lending capacity
 - Government's social programs (missions)
- Restriction of domestic production
- Growing dependence on imports

Deregulation and promotion of production activities

- Limitations of controls
- Investment promotion (higher production capacity and efficiency)

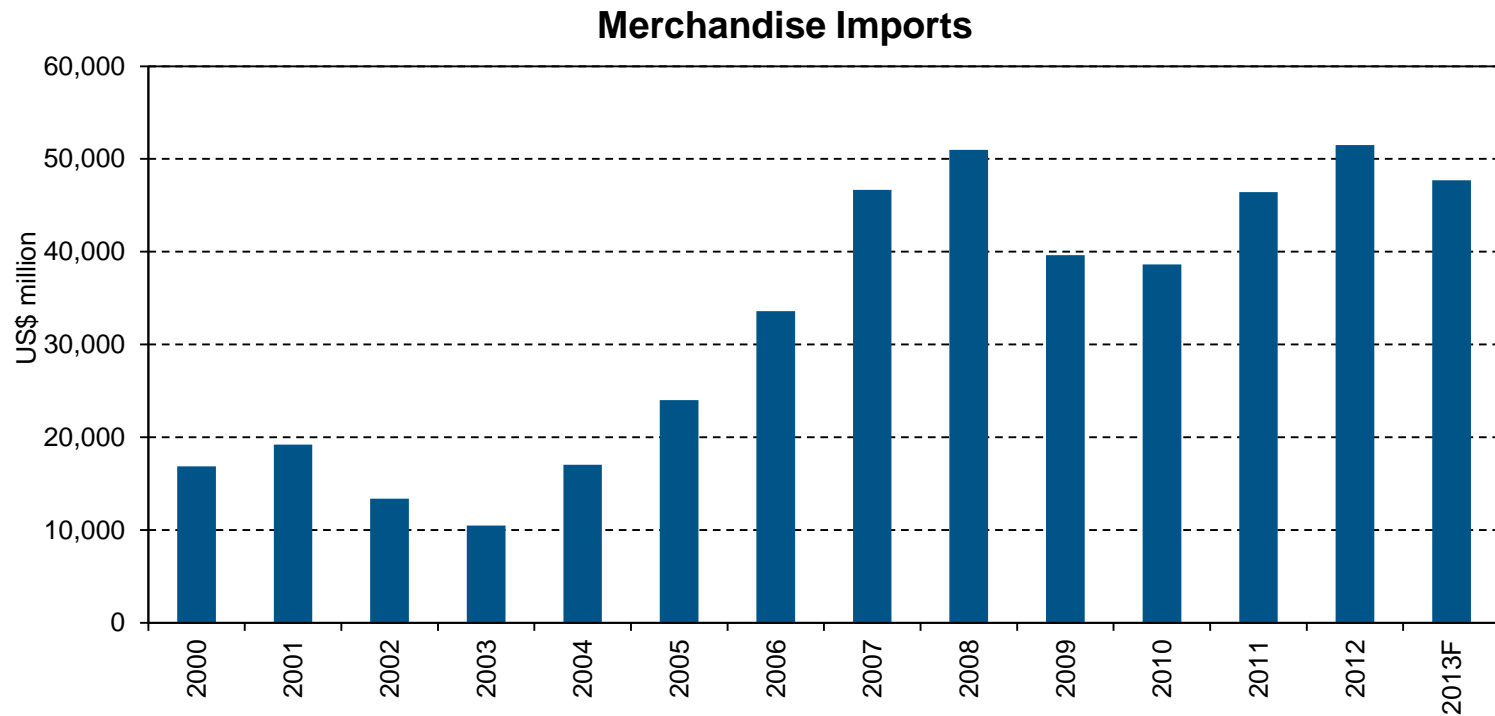
Acompaña las buenas decisiones...

Private Consumption Growth



Sources: BCV and Ecoanalítica

Imbalance Between Demand and Supply



Sources: BCV and Ecoanalítica



Acompaña las buenas decisiones...

Oil Imbalance despite high international oil prices

- Crude oil production restrictions
- High levels of domestic consumption
- Fuel smuggling
- PDVSA plundering by the government
 - Financing of government's missions
 - Massive transfers to Fonden (\$ 59.7 billion in 8 years)
 - Limited cash flow
 - ✓ Shipments to Cuba
 - ✓ Shipments to Petrocaribe and ALBA
 - ✓ Shipments to China
- High financing needs (loans from BCV)

Oil policy has to be reviewed

- Regularization of PDVSA's commitments to partners and suppliers
- Production increase (medium term)
- Relieving PDVSA from commitments alien to its core activities



Acompaña las buenas decisiones...

Corrective Measures have Consequences

- Inflation
 - Higher indirect taxes (VAT, Bank Debits Tax?)
 - Devaluation (more expensive imports)
 - Necessary price adjustments to avoid shortages
- Economic deceleration
 - Lower people's purchasing power
 - Private consumption deceleration
 - Exchange tax due to devaluation
- Deterioration of labor situation
 - Fewer jobs & high unemployment and underemployment
 - Deterioration of real wages

Conclusion: 2013 will be a complex year for the economy



Acompaña las buenas decisiones...

THANK YOU



Acompaña las buenas decisiones...

ADDITIONAL SLIDES

Exchange Agreement No. 14 of Feb/9/2013

- Official exchange rate goes from Bs/\$ 4.30 to Bs/\$ 6.30
- Applicable to public and private debt service payments (Art. 2), international investments, royalties, patents, brands, licenses, etc. (Art. 3)
- BCV may carry out the purchase and sale of dollar denominated bonds issued on the domestic market.; as may other public entities with previous authorization from the BCV and the Ministry of Finance (art. 4)
- The Bs/\$ 4.30 exchange rate will apply to (Art. 5):
 - Purchase of \$ which ALDs had been received by the BCV up to Feb. 8, 2013
 - Purchase of \$ by exchange operators and allocated to their clients up to Feb. 8, 2013
 - Sale of \$ which ALD was requested from the BCV up to Feb. 8, 2013
 - Sales operations of \$ made by exchange operators up to Feb. 8, 2013 based on Cadivi authorizations
 - Transactions with credit cards made up to Feb. 12, 2013
- The Bs/\$ 4.30 exchange rate will apply to (Art. 6):
 - Sale of \$ which ALD have been presented to the BCV up to Feb. 8, 2013.
 - ALADI operations with AAD issued as of Feb. 8, 2013
- The Bs/\$ 4.30 exchange rate will apply to \$ sale operations with Cadivi AAD up to Feb. 8, 2013 but which ALD has not reached the BCV (Art. 7)
 - Imports of food, health, commerce, communication-media, electrical appliances, electronics, comp. information, and telecom; as long as they have their respective Cadivi AAD as of Oct. 15, 2012
 - Imports of automotive, electric, construction, chemicals, rubber and plastics, paper, carton and wood, health, veterinary, textile, graphics, bookstores, school supplies, machinery and equipment, science and technology items if they have their Cadivi AAD as of July 15, 2012

Exchange Agreement No. 14 of Feb. 9, 2013 (continued)

- The Bs/\$ 4.30 exchange rate will apply to the sale of \$ which applications have been received by Cadivi up to Feb. 8, 2013 and submitted by July, 15, 2012 (Art. 8):
 - National civil aeronautic payment operations
 - Maintenance of machinery and equipment or imported software for the telecom. sector.
- The Bs/\$ 4.30 exchange rate will apply to the sale of \$ corresponding to applications received by Cadivi up to Feb. 8, 2013 (Art. 9) earmarked for:
 - Students studying abroad
 - Recovering health, sports, culture and scientific research
 - Retirement and pensions
 - Family remittances
 - Service rental agreements, patents, brands, licenses, and franchises
 - Passenger and cargo international air transportation
 - Insurance operations
- The Bs/\$ 4.30 exchange rate will apply to Bancoex's loans in \$ approved during the 6 months prior to Feb. 9, 2013 (Art. 10)
- Private exporters may keep up to 40% of the \$ of their exports (Art. 11)