

# ***Economic Performance and Political Evolution in Venezuela***

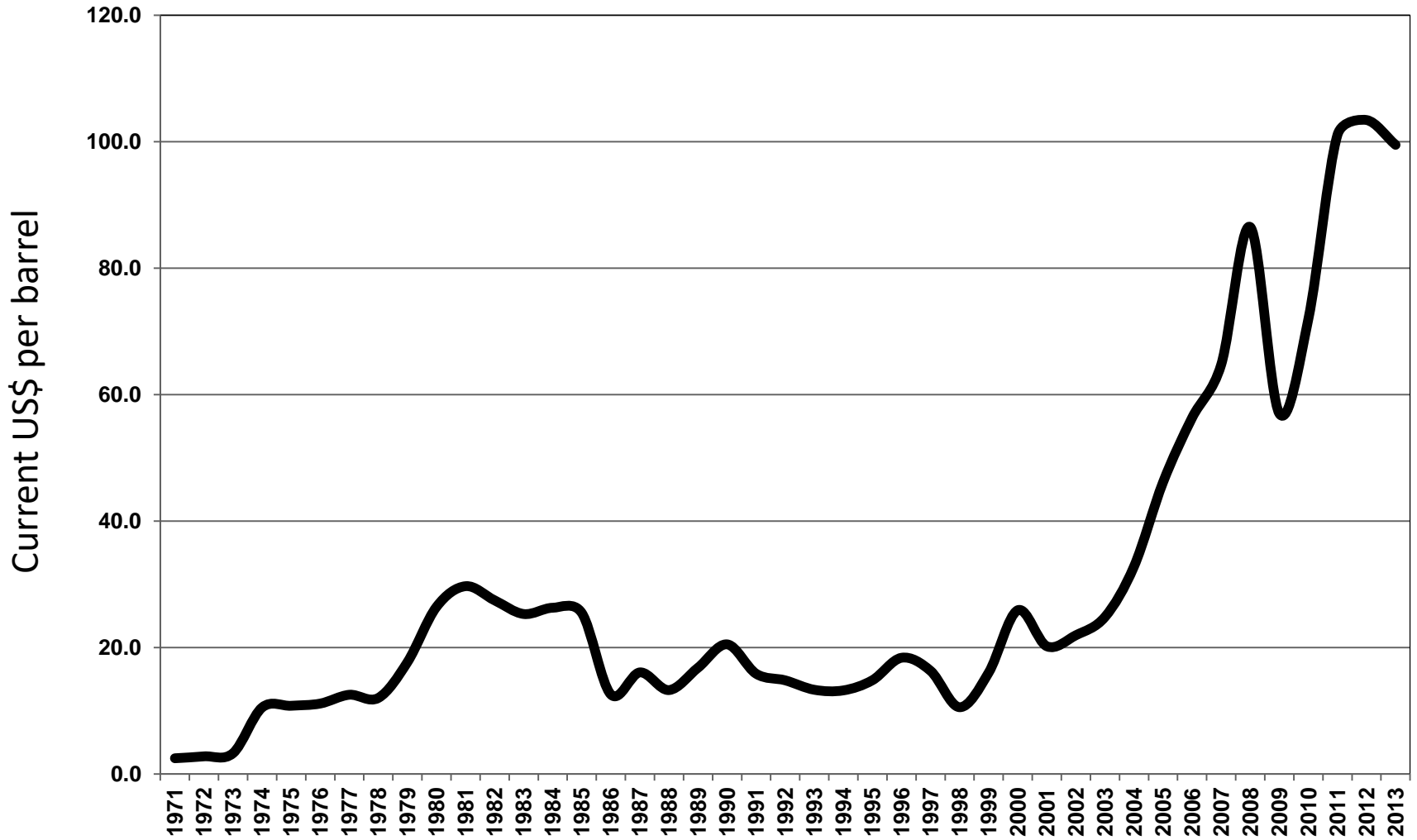
***Pedro A. Palma***

***Pensando Venezuela: A Transformation in Retrospect***

**Stanford University**

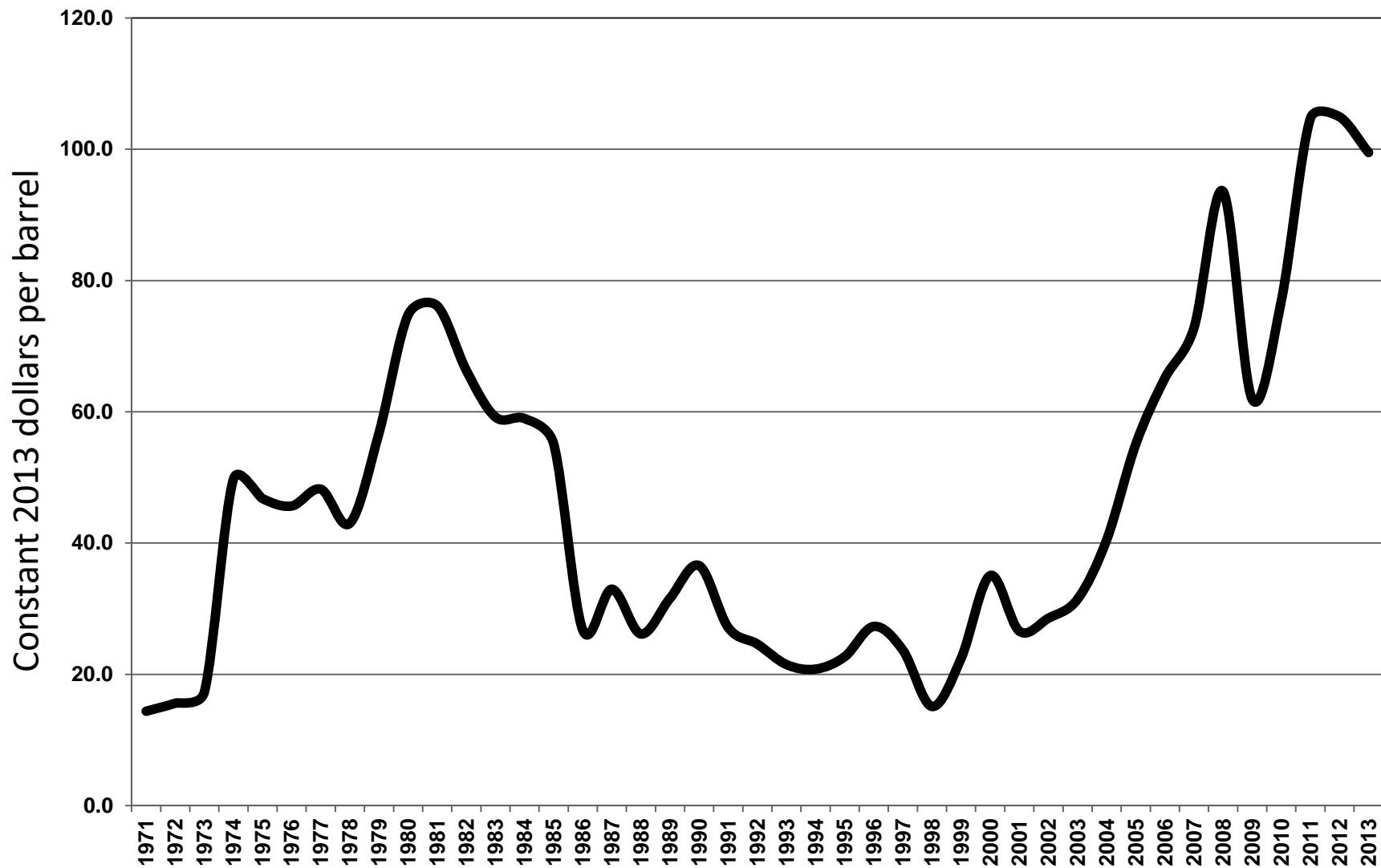
**Palo Alto: February 22, 2014**

# Nominal Venezuelan Oil Export Prices



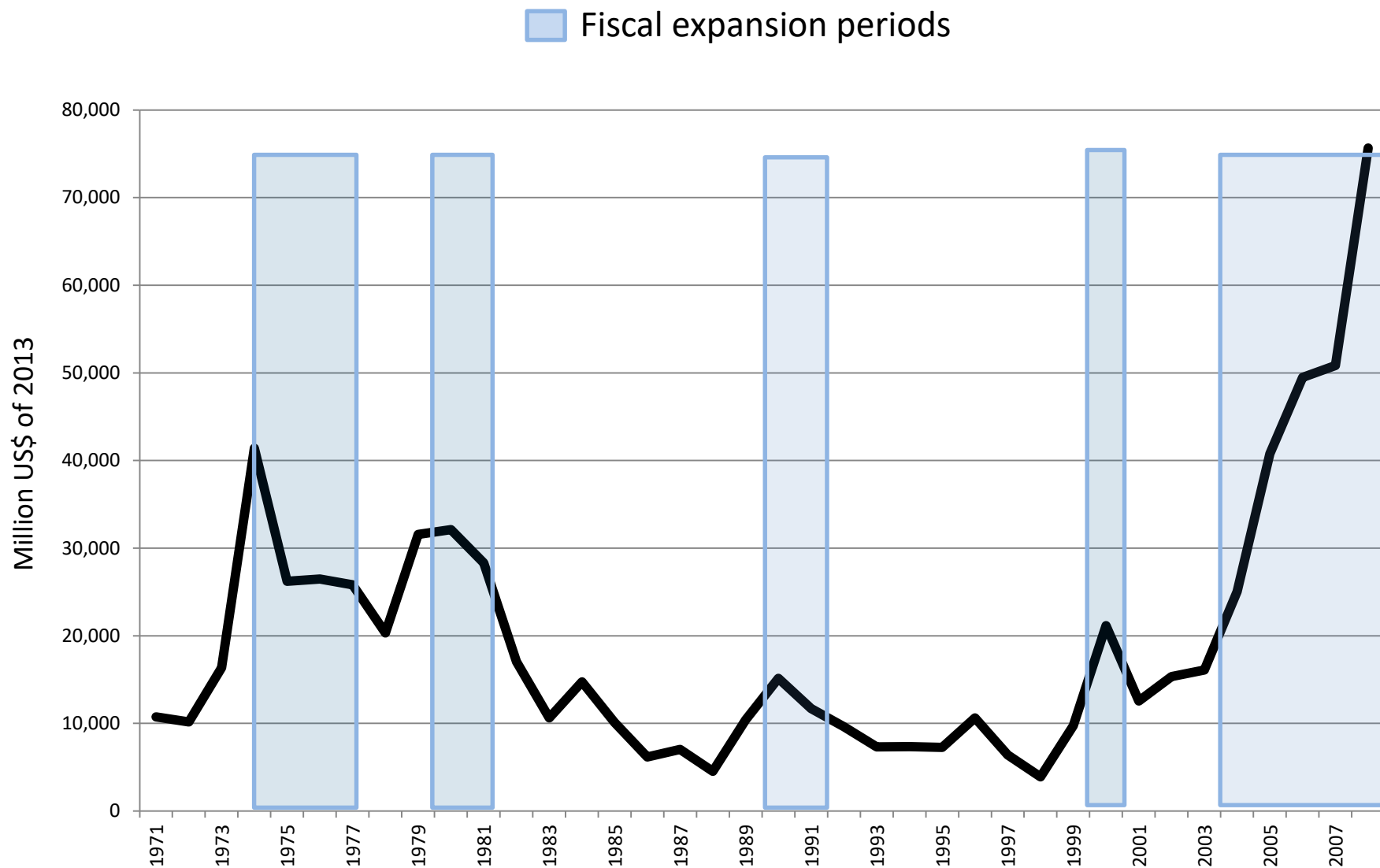
Source: MEP

# Venezuelan Oil Export Prices in constant dollars



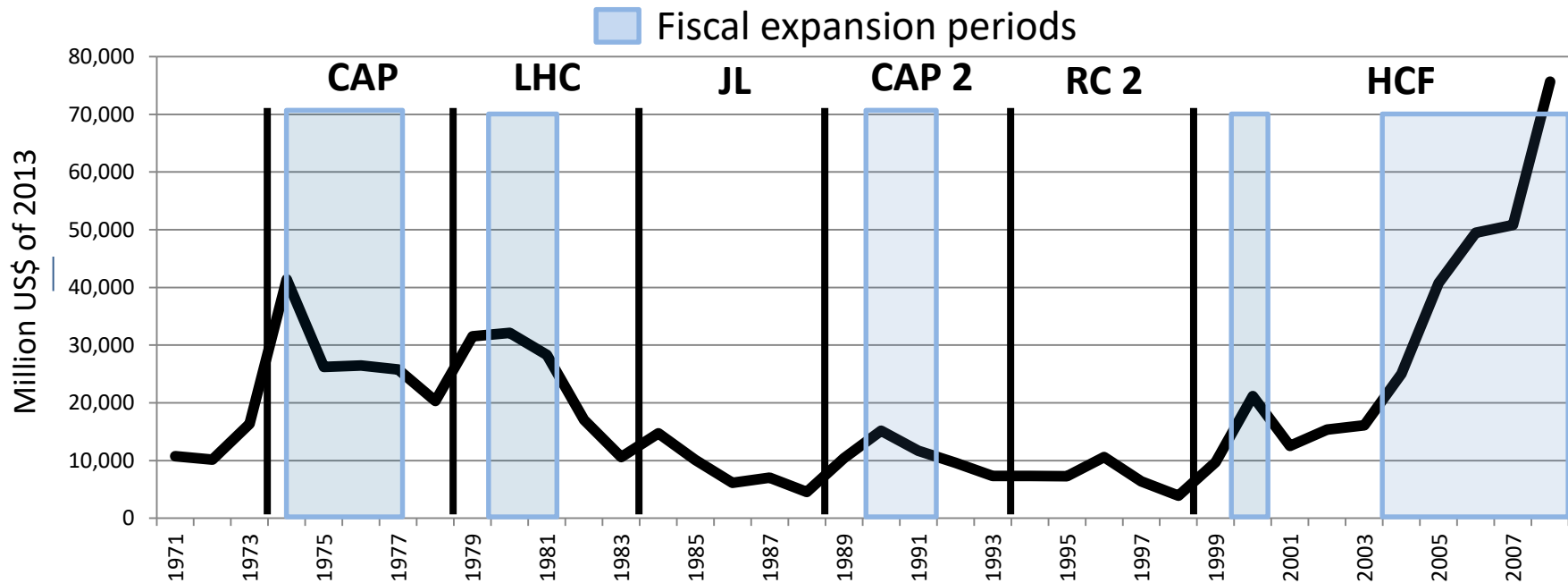
Sources: MEP, US DoL,

# Real Oil Rent and Procyclical Fiscal Policy



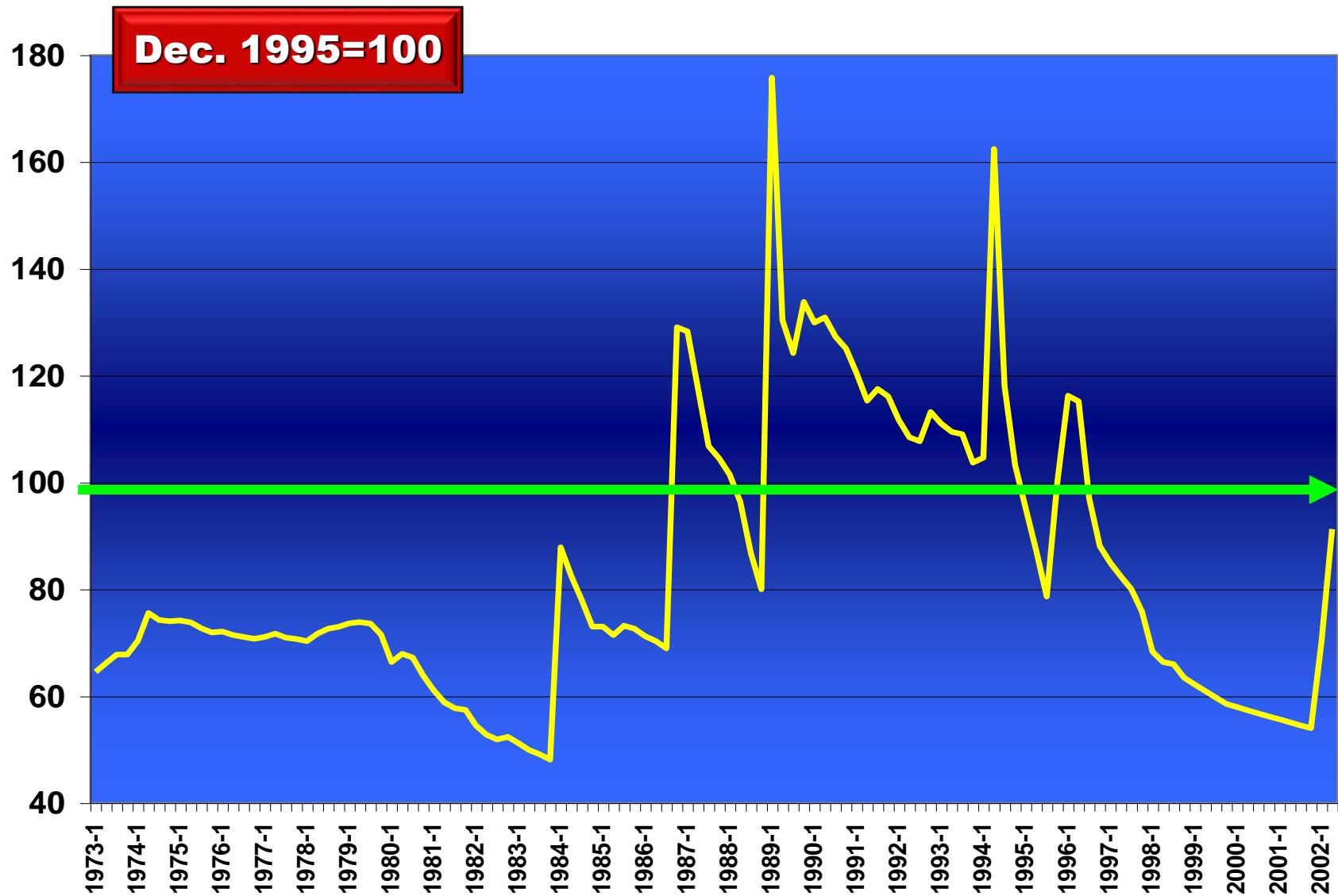
Sources: Baptista, A. (2011), Zambrano Sequín L. (2010), Palma, P. A. (2011)

# Real Oil Rent contractions at the end of five administrations



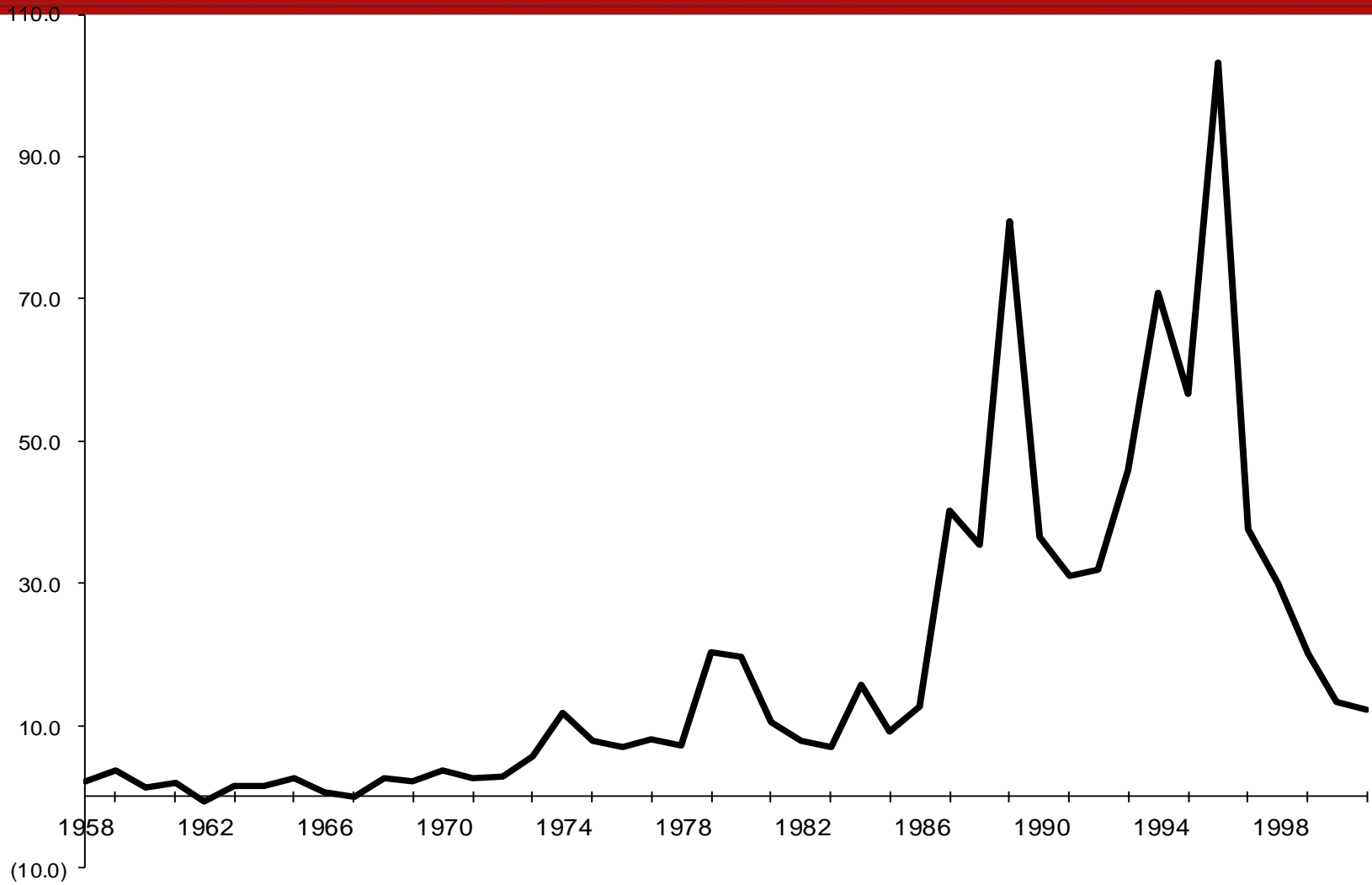
- The five administrations before Chavez finished their constitutional terms in crisis due to real oil rent contractions
- However, none of these governments implemented the necessary adjustments to cope with the crises, thereby making the situation worse
- Their failure to act forced the following administrations to implement the necessary adjustments in order to correct the problems left by the previous administrations

# The Venezuelan "Dutch Disease" Real Effective Exchange Rate Index



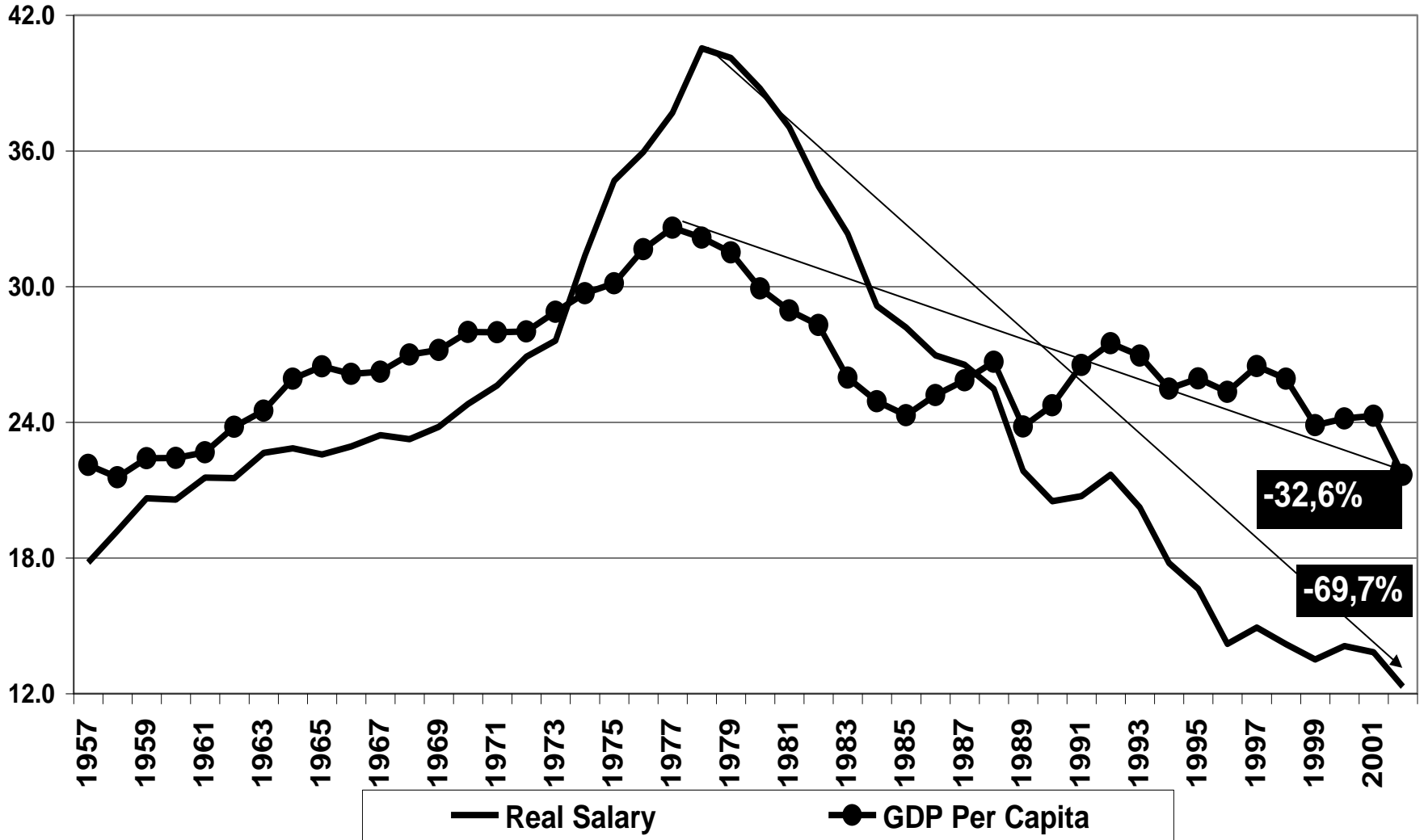
Sources: José Barcia and Metroeconómica

# Inflation



Source: Central Bank of Venezuela

## GDP Per Capita and Average Real Salary (Thousand 1984 bolivars)



Sources: Central Bank of Venezuela, Central Office of Statistics and Information and Metroeconómica



# Economic Decline and the Quest for Change

## Poor record of economic performance until 1998

- High volatile oil rent dependency and procyclical fiscal policies made the economy very unstable (from crisis to bonanza to crisis again)
- Political clientelism
- High corruption
- Persistent presence of the Dutch Disease
- A devastating banking crisis in 1994
- Massive capital flight and exchange controls
- High inflation
- Fall of real income per capita
- Persistent contraction of real GDP per capita
- Deteriorated labor conditions

*At the end of the 20<sup>th</sup> century Venezuelans were looking for a change*

# The first 5 conflicting years of the Bolivarian Revolution

## Basic economic indicators

	1999	2000	2001	2002	2003	1999-2003
Real GDP Growth (% Var.)						Average
Total	-6.0	3.7	3.4	-8.9	-7.8	-3.3
Oil	-3.8	2.3	-0.9	-14.2	-1.9	-3.9
Non-Oil	-6.9	4.2	4.0	-6.0	-7.4	-2.6
Total Per Capita	-7.8	1.8	1.5	-10.5	-9.4	-5.0
Inflation (Dec. to Dec.)	20.0%	13.4%	12.3%	31.2%	27.1%	154.8%
Real Remuneration Index	772.0	803.1	858.7	764.2	629.9	-17.2%
% Var.	-1.5%	4.0%	6.9%	-11.0%	-17.6%	
Average oil price	16.04	25.91	20.21	21.95	24.84	
Exchange Rate (year end) (Bs/US\$)*	648.25	699.75	763.00	1,401.25	2,745.82	386.40%
Balance of Payments:						
Exports of Goods (MM\$)	20,963	33,529	26,667	26,781	27,230	
Imports of Goods (MM\$)	14,492	16,865	19,211	13,360	10,483	
Trade Balance (MM\$)	6,471	16,664	7,456	13,421	16,747	
Current Account Balance (MM\$)	2,112	11,853	1,983	7,599	11,796	
Net Direct Foreing Investment (MM\$)	2,890	4,701	3,683	782	2,040	
Private Capital Outflow (MM\$)**	-3,087	-4,655	-8,019	-8,450	-3,386	-27,597
International Reserves, (year end) (MM\$)	15,379	20,471	18,523	14,860	21,366	

\* The 2003 figure corresponds to the free market rate

\*\* Equal to: Net private "Other Investment" plus 50% of "Errors and Omissions"

Sources: Central Bank of Venezuela, INE, MEP, Ecoanalitica

# Poor balance of the first 5 years of Chavez

- Escalating political and social unrest
- The general strike between December 2002 and February 2003 had devastating economic effects
- GDP per capita cumulative contraction in the period 1999-2003: -22.8%
- In 2003 unemployment rate was 18%, and 52.6% of the labor force was underemployed
- In 2003 54% of households were under the poverty line and 25.1% were under the extreme poverty line
- Massive capital flight forced the government to implement an exchange control in February 2003
- Severe price controls started in year 2003
- After the oil industry strike of December 2002-February 2003 more than 18,000 of Pdvsa's managers and skilled workers were fired, leading to very negative long term consequences
- The imminent adverse results of the presidential revocatory referendum of 2003 made the government to start implementing different social programs (the "missions")

# The Oil Bonanza of the Bolivarian Revolution

## Basic economic indicators

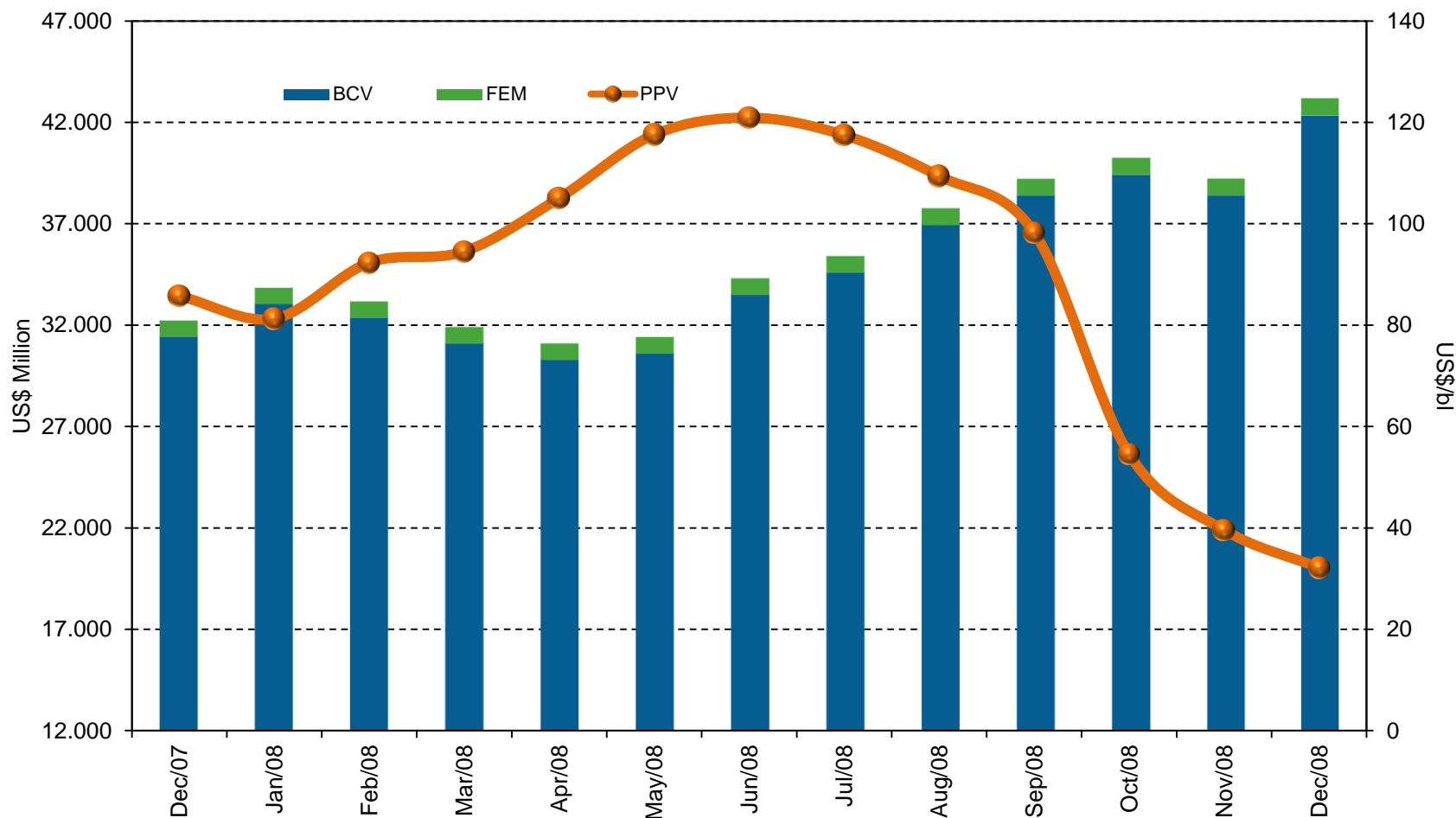
	2004	2005	2006	2007	2008	2004-2008
Real GDP Growth (% Var.)						Average
Total	18.3	10.3	9.9	8.8	5.3	10.4
Oil	13.7	-1.5	-2.0	-3.3	2.9	1.8
Non-Oil	16.1	12.2	10.9	9.7	5.7	10.8
Total Per Capita	16.2	8.4	8.0	7.0	3.6	8.6
Inflation (Dec. to Dec.)	19.2%	14.4%	17.0%	22.5%	31.9%	157.8%
Real Remuneration Index	630.6	647.9	680.9	691.4	658.2	4.5%
% Var.	0.1%	2.7%	5.1%	1.5%	-4.8%	
Average oil price	32.82	46.15	56.35	64.74	86.49	
Exchange Rate (year end) (BsF/US\$)*	2.70	2.70	3.40	5.70	5.70	111.10%
Balance of Payments:						
Exports of Goods (MM\$)	39,668	55,716	65,578	69,980	95,021	
Imports of Goods (MM\$)	17,021	24,008	33,583	47,252	51,490	
Trade Balance (MM\$)	22,647	31,708	31,995	22,728	43,531	
Current Account Balance (MM\$)	15,519	25,447	26,482	15,981	32,146	
Net Direct Foreign Investment (MM\$)	1,483	2,589	-508	1,505	1,741	
Private Capital Outflow (MM\$)**	-7,546	-9,942	-7,259	-17,544	-20,103	-62,394
International Reserves, (year end) (MM\$)	24,208	30,368	37,440	34,286	43,127	

\* These figures correspond to the free market rate

\*\* Equal to: Net private "Other Investment" plus 50% of "Errors and Omissions"

Sources: Central Bank of Venezuela, INE, MEP, Ecoanalítica, Venezuela FX, Metroeconómica

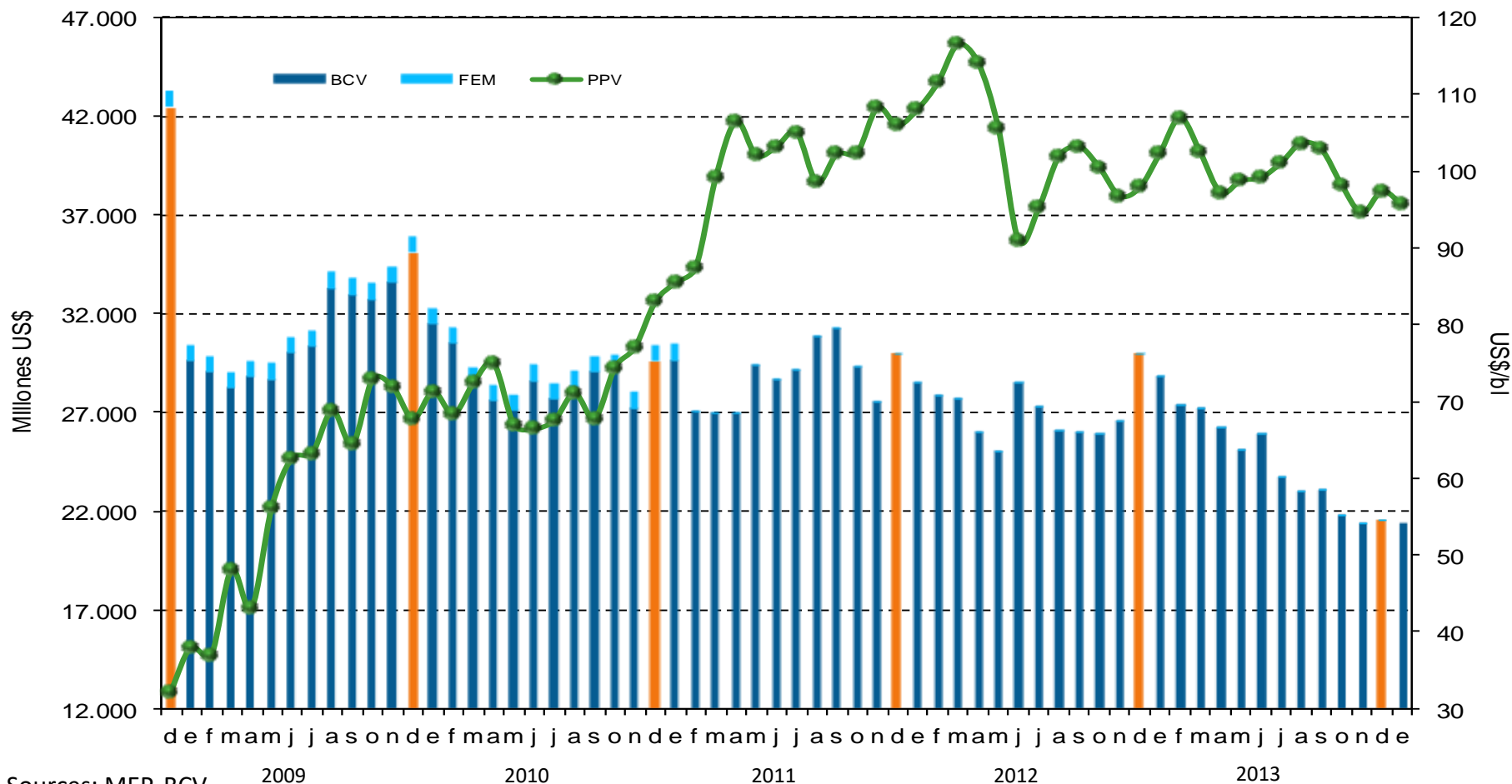
# International Reserves and Oil Prices in 2008



Sources: MEP, BCV

	2007	2008
<b>International Reserves ( Dec 31st)</b>	<b>34,286</b>	<b>43,127</b>
<b>Oil Average Price</b>	<b>64.74</b>	<b>86.49</b>

# International Reserves and Oil Export Prices



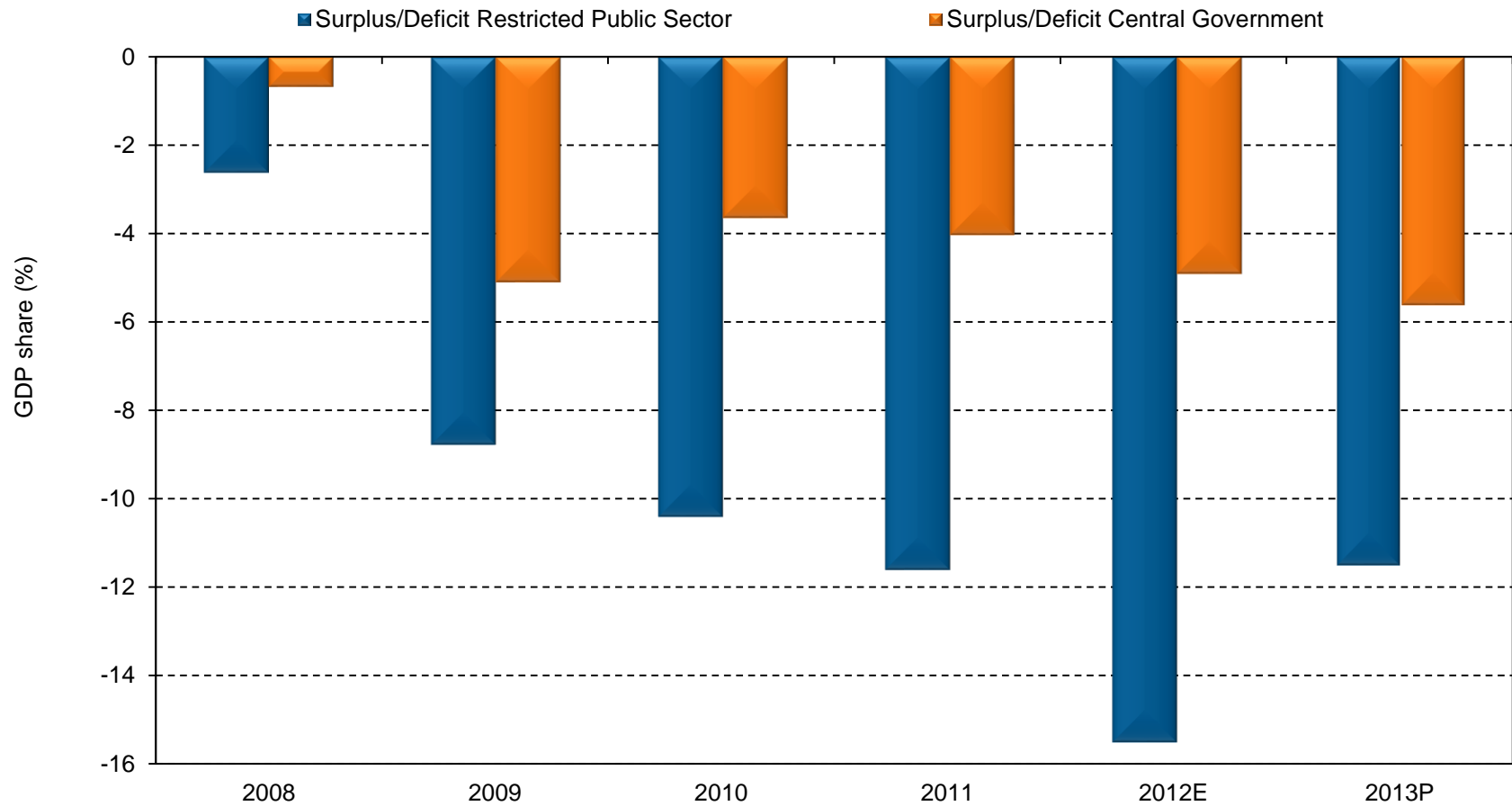
Sources: MEP, BCV

So far this year the average oil export price of the Venezuelan basket is US\$/b 96.30. The international reserves at the end of January 2014 were US\$ 21,328 million. On February 20<sup>th</sup> the international reserves were US\$ 20,405 million.

	2009	2010	2011	2012	2013
<b>International Reserves (Millions of US\$)</b>	<b>35.830</b>	<b>30.332</b>	<b>29.902</b>	<b>29.890</b>	<b>21.481</b>
<b>Average Oil Export Price (US\$/b)</b>	<b>57,0</b>	<b>72,7</b>	<b>101,0</b>	<b>103,42</b>	<b>99,49</b>

# Public finance imbalances

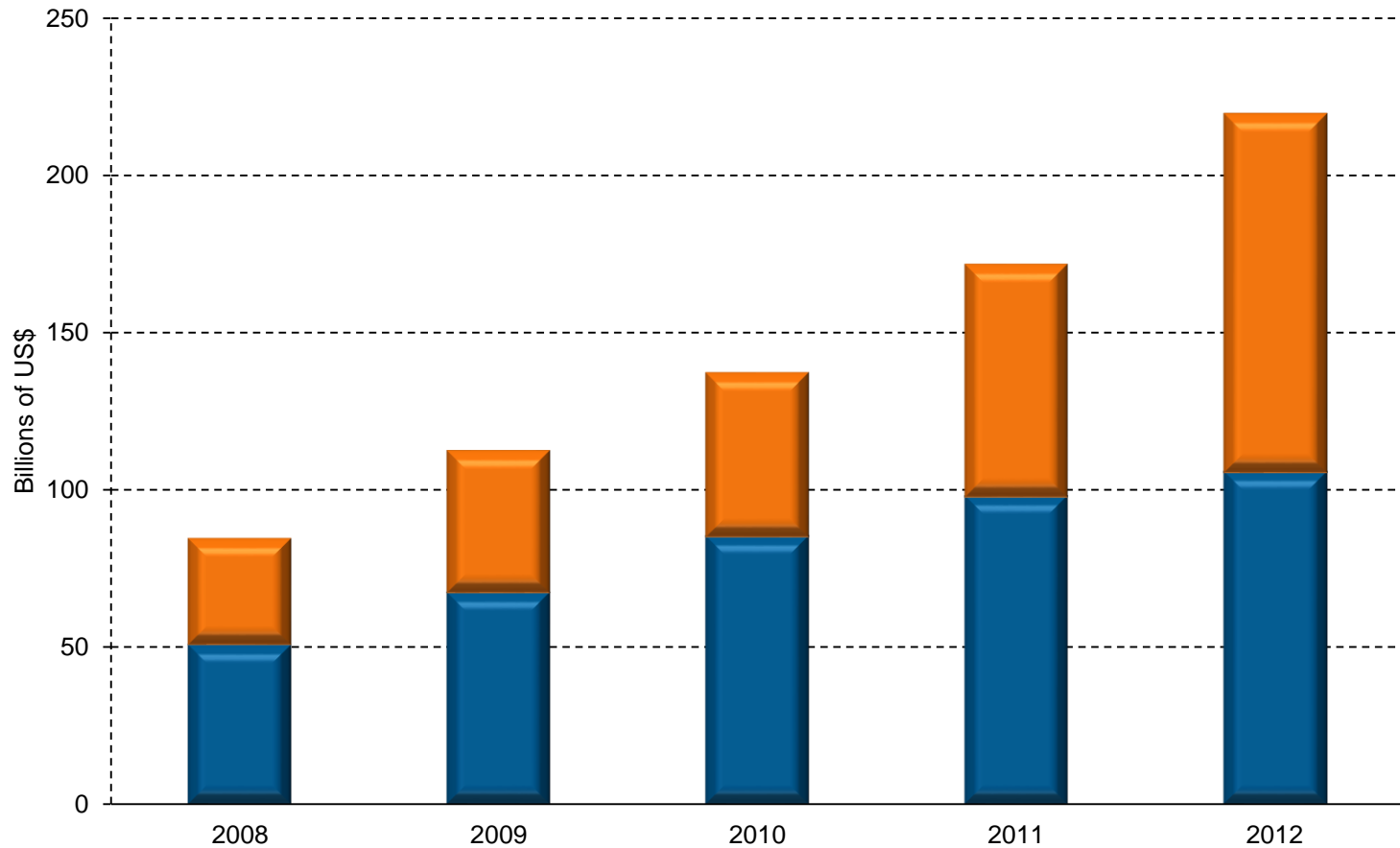
## Restricted Public Sector's vs. Central Government's Fiscal Balance



Sources: MPF and Ecoanalítica

# Public Sector Debt

Foreign (blue) and Domestic (yellow) Public Sector Debt



Sources: Pdvsa y Ecoanalítica

Note: The domestic debt only includes the debt of the central government and of Pdvsa



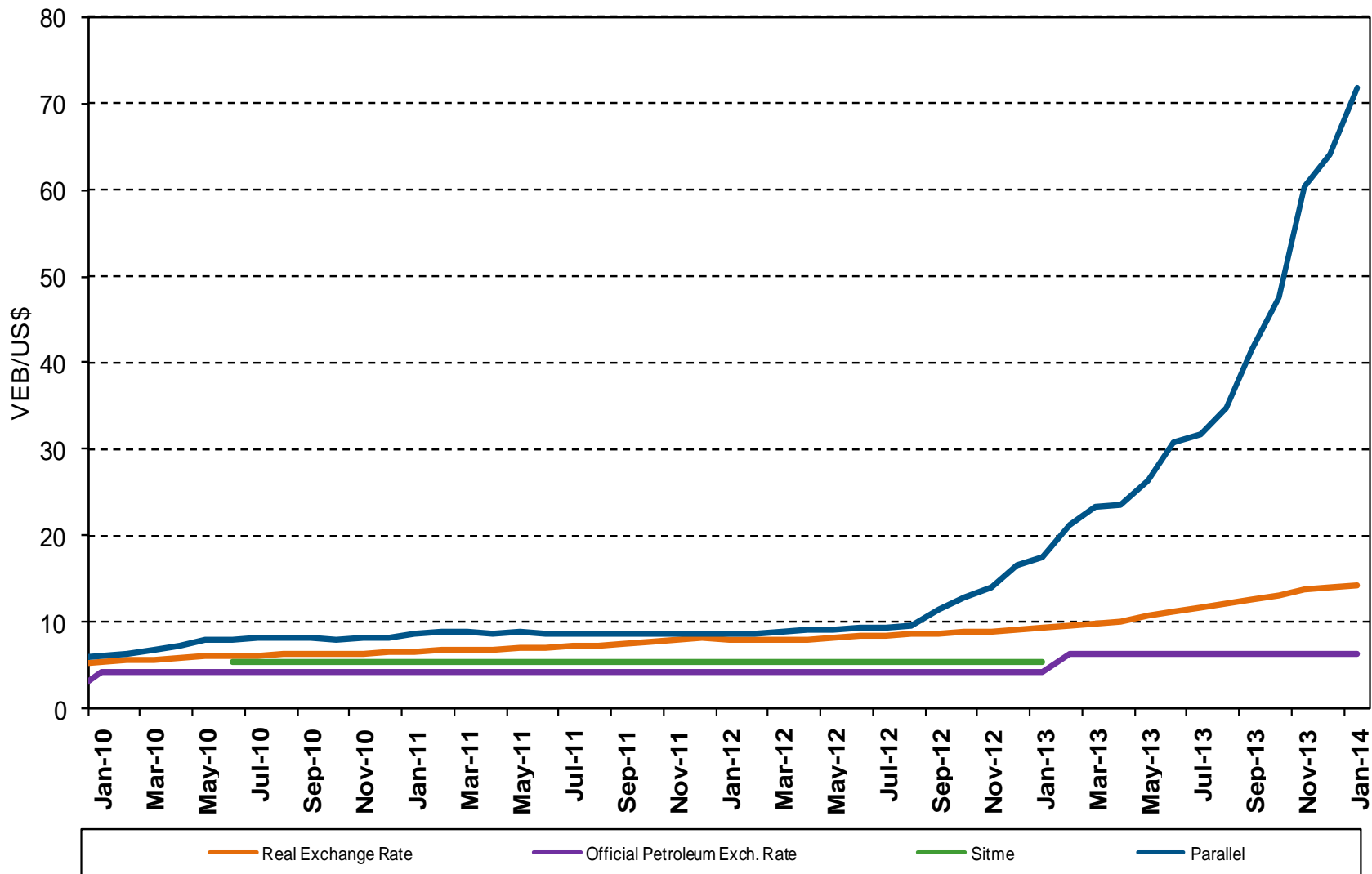
# Oil Imbalance despite high international oil prices

- Crude oil production restrictions
- High levels of domestic consumption
- Fuel smuggling
- PDVSA plundering by the government
  - Financing of government's missions (social programs)
  - Massive transfers to Fonden (\$ 59.7 billion in 8 years)
  - Limited cash flow
    - ✓ Shipments to Cuba: 91.1 Mb/d in 2012
    - ✓ Shipments to Petrocaribe, ALBA and others: 175.6 Mb/d
    - ✓ Shipments to China: 451 Mb/d in 2012
- High financing needs (loans from BCV)

# Monetary and Financial Imbalances

- High BCV's financing to public entities
  - PDVSA's net debt to BCV at the end of 2013: Bs 407.8 billion (\$ 64.7 billion)
  - BCV's net loans to public sector firms at the end of 2013 were equivalent to 97% of the monetary base and to 35.6% of the money supply ( $M_2$ )
- High increase of money supply (75.2% Feb. 2013 - Feb. 2014)
- High level of banking excess reserves: Bs 118.1 billion as of February 21<sup>st</sup>, 2014. The average during July 2012 was Bs 26.7 billion
- Significant negative real interest rates

# Exchange Rates



Sources: BCV, and Ecoanalítica

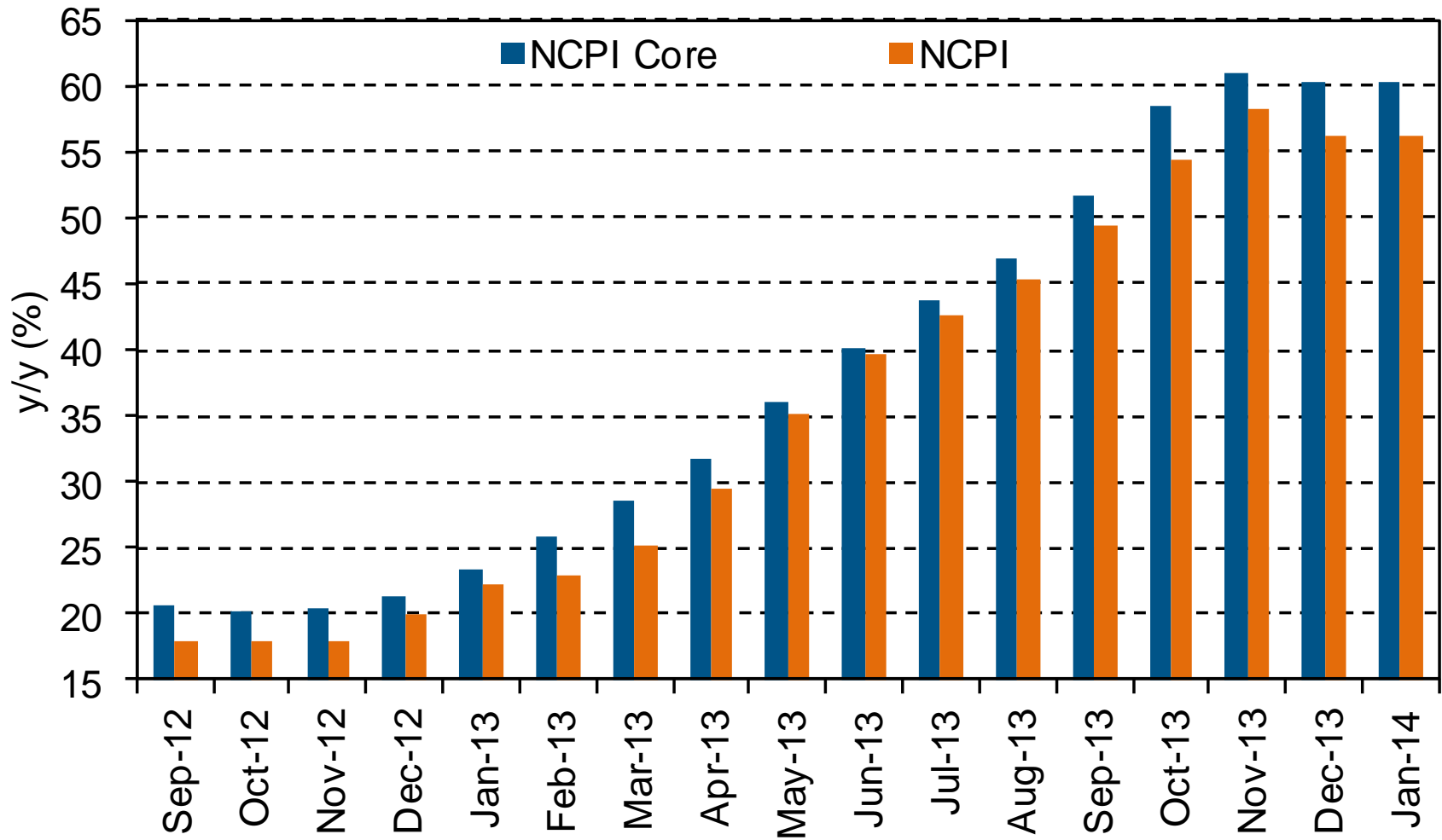
# Production and Distribution Imbalances

- Production of tradable goods has been severely affected
  - Loss of competitiveness due to a highly overvalued currency
  - Disproportionate price controls that have forced multiple producers to produce at a loss
  - 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
    - ✓ Law-decrees as part of the Enabling Law approved on Nov. 11<sup>th</sup>
- Deterioration of production capacity due to expropriations of companies

*The upshot: shortages and scarcity*

# High Inflation

## NCPI Core vs. NCPI



Sources: BCV and Ecoanalítica

# Socialism of the 21<sup>st</sup> Century: A Summary

- Populism (populist spending programs)
- No autonomous democratic institutions (total control by the Executive Branch)
- Controlled economy by an authoritarian centralized government
  - Exchange controls
  - Price controls
  - Production and distribution controls
- Very high economic dependency of the oil rent, more than ever
- Public spending plays a key role as the main economic stimulus
- Very hostile attitude against the private sector (expropriations)
- Rampant corruption
- Massive and high cost support to allied countries (Cuba, ALBA, etc.)

**Results:** High inflation, scarcity, low growth, lower purchasing power, no rule of law, high crime, depleted labor rights.

**However:** The government still has important popular support, particularly in small towns and rural areas

# A final thought

“An ignorant people is a blind instrument of its own destruction. Ambition and intrigue abuse the credulity and experience of men lacking all political, economic, and civic knowledge; they adopt pure illusion as reality; they take license for liberty, treachery for patriotism, and vengeance for justice”

Simon Bolivar

Angostura: February 15<sup>th</sup> 1819

**THANK YOU**