ecoanalítica

Economic Outlook
Report
16 – August 2022

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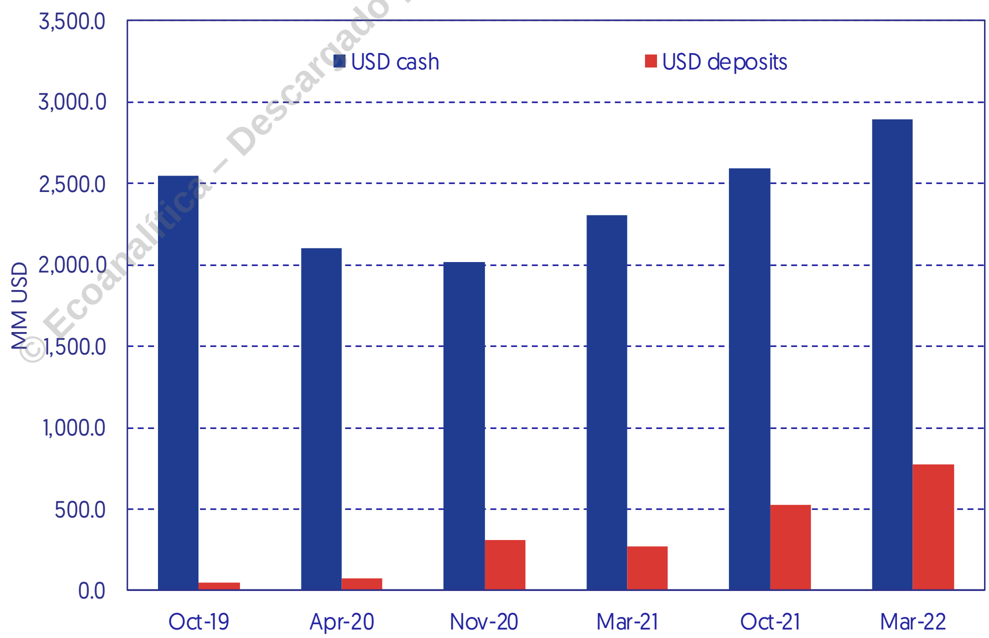
Content

General aspects **of the Venezuelan foreign exchange market**

The purpose of this report is to briefly review the recent characteristics of the Venezuelan foreign exchange market. Starting with the current panorama of the foreign exchange market, passing through a brief review of the historical conditions under which it has operated and, finally, closing with a key aspect of the sanctioned Venezuela: the ways in which companies can transfer their funds from the national territory to foreign countries.

Since the repeal of the Foreign Exchange Illicit Act in August 2018 and the normalization of the use of foreign currency for daily transactions during the blackout of April 2019, the circulation of foreign currency in Venezuela has shown a clear upward trend and since 2019 has been above USD 2 billion. From **Ecoanalítica**, we track such progress through our dollarization studies, which total six since October 2019. For them, we have sampled the main cities of the country. The most recent quantification was made in March of this year, when such circulation stood at approximately USD 2.9 billion, the highest value we have observed in our compilations.

Cash and USD Deposits

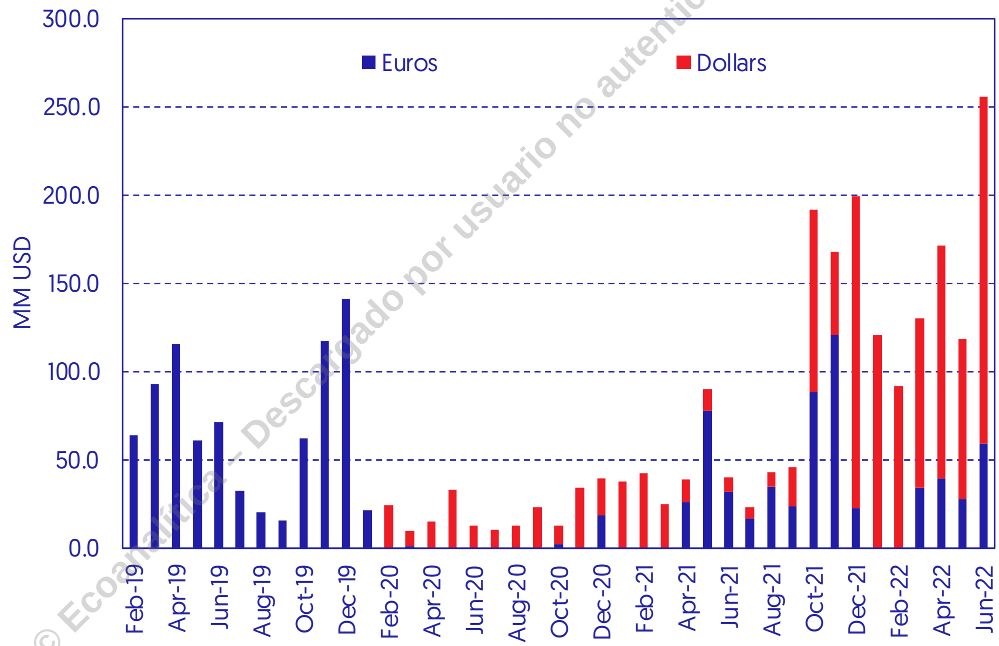


Sources: SUDEBAN and Ecoanalítica.

At the same time, the value of foreign currency deposits held in local banks also expanded in the same reference period. In June, these reached a value of approximately USD 800 million, 6.8% higher than estimated in March (last estimate of foreign currency cash circulation) and 122.8% higher on a year-on-year basis. Moreover, the ratio of cash currency circulation to total deposits has been declining, from 8.5 in March 2021 to 3.7 a year later. Even so, although the dollar continues to gain importance within the local banking system, the system is still far from being able to offer a wider range of products or even grant loans in this currency.

On the other hand, foreign currency sales in cash (in euros and dollars) by the Central Bank (BCV) to Venezuelan banks accumulated in the first half of 2022 USD 887.8 million, 224.8% above the value seen for the same period of 2021. This year, the issuing entity has increased its interventions within the official exchange system in an attempt to contain the escalation of prices through the stability of the exchange rate. As a result, June saw the highest cash injection in our sample (since January 2019). We also estimate that the volume traded within the private foreign exchange desks in recent months has been approximately USD 160 million, an amount much lower than the interventions made by the official entity.

Sale of foreign currency in cash to the financial system



Sources: BCV and Ecoanalítica.

Ever-present green filter

The most recent scenario of the boom of transactional dollarization in the country was closely linked to the hyperinflationary process that accumulated 39 months[1] and caused the value of the local currency to decrease exponentially, facilitating the transition to a predominance of the use of the dollar even in the most daily local operations. However, this use of the dollar is nothing new and has always been present; therefore, we are also used to seeing the effect that the measures implemented by local regulators may have on it.

The Venezuelan exchange rate system is atypical. For decades, the official exchange rate operated under a fixed exchange rate scheme with delayed devaluations,

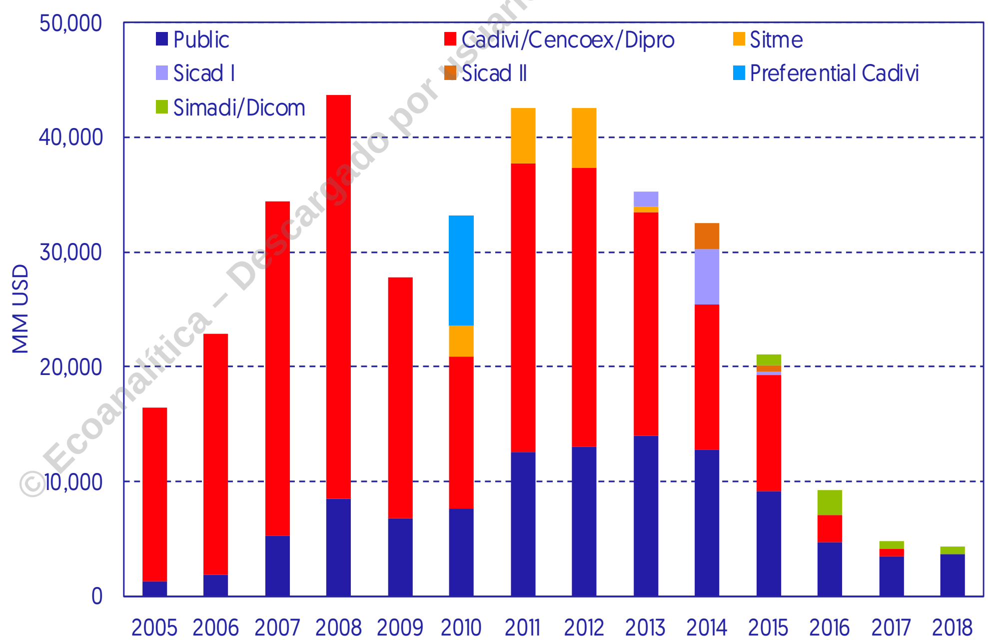
[1] Under **Ecoanalítica'**s data collection and Cagan's definition of months with inflation greater than or equal to 50.0%.

although for some periods it coexisted with other schemes. However, the main characteristic that makes our system atypical is the imbalance between the monetary policy of the Central Bank of Venezuela (BCV) and the officially declared exchange rate objectives. The lack of a clear intervention policy resulted in different exchange rate systems which, at different times, became unsustainable given the fiscal, monetary or social situation that arose together with extraordinary oil revenues that allowed the financing of the undervalued official exchange rate.

A historical review shows that controls on the circulation of capital began in 1983, after the first major contraction of international reserves, in order to limit more severe imbalances in the balance of payments, led to the rejection of their free mobility. Auction mechanisms and the fixing of several simultaneous exchange rates have also been part of the country's exchange rate idiosyncrasy, as well as (albeit briefly) mechanisms of free fluctuation with punctual interventions.

However, all of them have resulted, in one way or another, in a failed attempt to maintain the rate at a stable value or became mechanisms that encouraged arbitrage operations between the different rates. Constantly, the sustainability of maintaining a given exchange rate and the need of agents to hedge against the incessant imbalances in the Venezuelan scenario have gone in opposite directions, which has strengthened the Venezuelan parallel foreign exchange market.

Foreign currency settlements by scheme



Sources: BCV and Ecoanalítica.

Since 2003, in an attempt to contain the influence of the parallel market and capital outflows, new foreign currency settlement systems were established. The Foreign Exchange Administration Commission (CADIVI) began to have the power to coordinate, administer, control and establish the requirements, procedures and restrictions for the purchase and sale of foreign currency in the country. Under this scheme, the Central Bank of Venezuela (BCV) centralized the country's foreign exchange market, while banks and other financial institutions were the foreign exchange operators (previously authorized by the BCV). Thus, the BCV, together with the Executive, approved the amount of foreign currency to be administered.

As of 2010, with the SITME, the BCV controlled and intermediated daily operations in the swap market; it was in charge of establishing the price band in which the securities would move and acted as the guarantor regulator of the current regulation. At the same time, the BCV had the power to supervise the negotiations, request the information it considered necessary and even suspend entities from the negotiations until further notice. With the banks acting as exchange operators, the bidders expressed to the BCV their desire to sell securities, and the country's financial institutions processed this process so that the bond plaintiffs would buy them. In turn, the buyers sold the securities acquired in the international market in exchange for foreign currency.

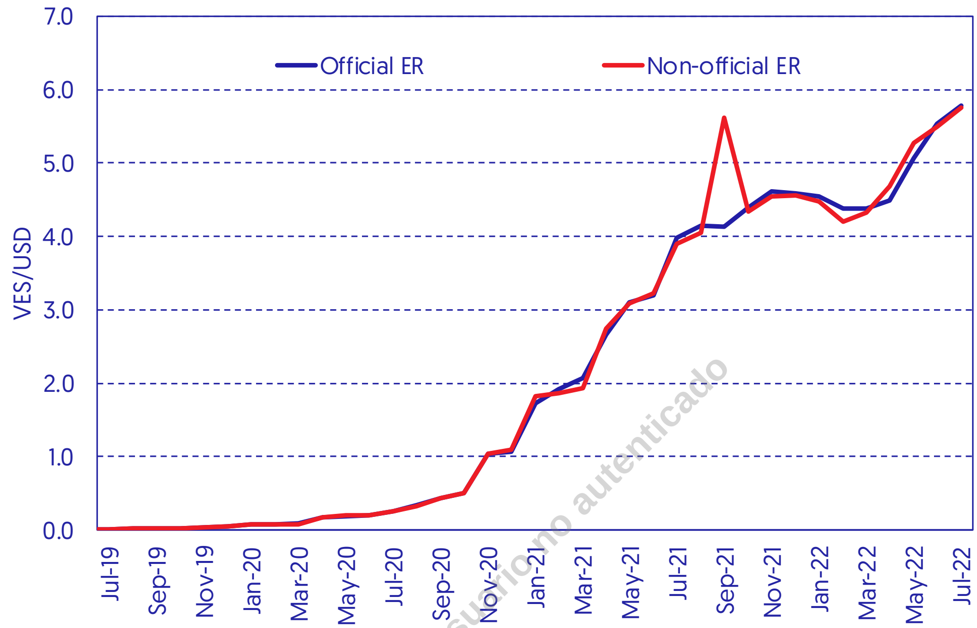
Later on, with the implementation of SICAD and Dicom (all 4 versions), the use of auctions as a mechanism for the allocation of foreign currency began, again with the BCV as the main operator. In the established systems, different official rates were maintained, which again provided the possibility of arbitrage observed in the past until the Dipro system was eliminated and a single official rate remained in the current system of exchange bureaus.

Year 2022: two rates, penalties and the need to communicate with the outside world

The current scenario of the Venezuelan foreign exchange market presents two rates defined as official and unofficial. In the case of the unofficial market, distinctions are observed between the retail market and the corporate market, where the main differences are in the amounts handled, its participants and transaction costs (and the consequent premium in the rate of the latter over the former).

The repeal of the Foreign Exchange Law could have created a multi-currency environment different from the current one, without the transactional and capital transfer frictions caused by the financial sanctions on the country. However, certain characteristics of the past remain. Although the monetary authority maintains its interventions in the official market, their sustainability and scope are limited. The largest injections in the exchange system observed this year are closely linked to a new extraordinary increase in international crude oil prices and, even with this, it has not been a guarantee to keep the value of the currency stable in a sustained manner. The current system stands out for its total opacity regarding the amounts traded, but the increase in the rate seems to show that it is an official foreign exchange market that does not allow the needs of the agents to be emptied. In addition, there is still a need to transfer foreign currency abroad, either to repay parent companies or investors abroad, or as a form of protection against the uncertainty of the Venezuelan environment.

Parallel and official exchange rates



Sources: LocalBitcoins, BCV and Ecoanalítica.

Likewise, the aforementioned increase in the supply of foreign currency could also be attributed to greater difficulties in transferring dollars abroad, due to geopolitical tensions between Venezuela and its main financial partners, particularly Russia. In this sense, international financial institutions have shown less willingness to handle funds coming from the Venezuelan financial system to avoid punitive measures from their local authorities. In view of this, the Venezuelan private sector has developed different mechanisms to transfer its foreign currency abroad. Among these are:

1. Exchange bureaus: Private banks perform the bolivar to dollar exchange operation, transferring the funds to the correspondent of the financial institution (mainly in the United States), provided that the account is in the name of the company requesting the operation. However, this mechanism is limited to a group of large companies (usually multinationals), due to the risk associated with extracting foreign currency from Venezuela.

2. Parallel market of foreign exchange desks (corporate): Carried out by Brokers, where an exchange transaction is made from bolivars to dollars to branches abroad, assuming a commission cost reflected in the corporate exchange rate premium. Such premium reflects the risk of performing the transaction, which remains between 10% and 15% above the parallel exchange rate.

3. Cryptocurrencies: Also operated by brokers, who use cryptocurrency platforms to avoid the obstacles observed in more traditional mechanisms. First, bolivars are exchanged into a digital currency (usually Bitcoin), which are then traded for dollars that are deposited in foreign accounts. Additionally, some firms have internalized this mechanism, eliminating intermediaries.

4. Cash: Operation executed by brokers, and (sometimes) banks, for companies whose cash flow is mainly composed of foreign currency transactions in cash and which have to make payments to suppliers abroad. In this case, commissions are charged to "bank" such cash, between 4% and 6%, transferring it to electronic accounts abroad.

5. Link of points: Agreements between companies that have cash or bolivars in the local market and companies (usually exporters in the primary sector) that keep most of their liquidity in foreign accounts and need to repatriate such money to make payments to their domestic suppliers. In this case, no commission is charged between the two firms, and the former transfers the funds to the latter through local mechanisms, in exchange for a transfer in foreign currency to their foreign accounts, thus eliminating the need for intermediaries (brokers).

6. Exchange to pesos in the Colombian market: Through exchange operations at the border, companies with access (subsidiaries) and accounts in the Colombian market, buy pesos with their bolivars, depositing such pesos in their accounts in Colombia, where it is easier to exchange them to dollars and transfer the capital to accounts abroad.

Despite the changes in the Venezuelan foreign exchange market in recent years, the country's new relationship with foreign exchange still retains elements of the past. The domestic exchange rate environment continues to be part of the national economic fabric and, therefore, is conditioned by the rest of the dimensions of the domestic market. This is why the domestic economic fragility and the uncertainty that frequently surrounds the official stance on price stability will continue to be reflected in the volatility still shown by the Venezuelan exchange market, where the official rate can go from increasing "only" 8.3% in a period of seven months to 28.9% in "only" three months.

Jhoan F. Castellano
Diego Santana Fombona

Weekly **Indicators**

	3rd Week August	*Weekly chg. (%)*	*Depre/Apre (pp)*[1]
FX Boards (VES/USD)[2]	6,0	1,3	1,3
	1st Week August	Weekly chg. (pp)	Annual chg. (pp)
Lending Interest Rate (%)	58,4	1,6	3,9
	3rd Week August	Weekly chg. (pp)	Annual chg. (pp)
Overnight Interest Rate (%)	5,6	-136,7	-124,5
	2nd Week August	Weekly chg. (%)	Annual chg. (%)
International Reserves (USD Bn)	10,3	0,34	66,3
	1st Week August	Weekly chg. (%)	Annual chg. (%)
Monetary Liquidity (MM VES)**	8.609,6	-4,2	282,0

Price of International Oil Baskets (USD/bl)

	2nd Week August	Weekly chg. (%)	Annual chg. (%)
WTI	94,7	0,7	40,0
Brent	104,6	2,0	48,2

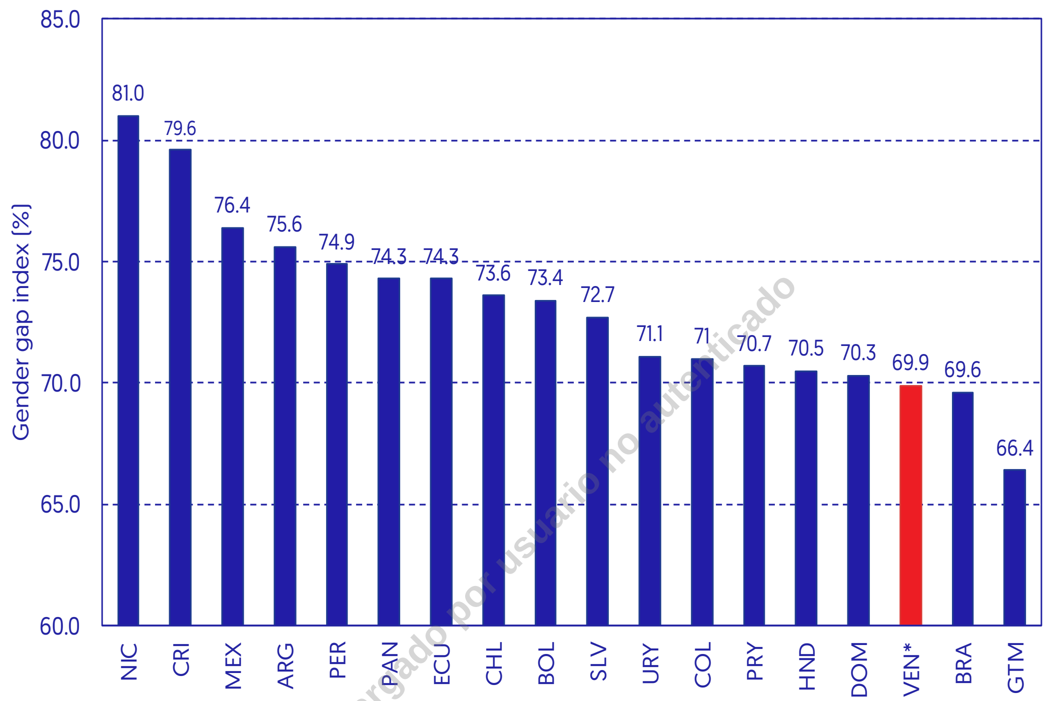
Price of the Venezuelan oil basket (USD/bl)

	5th Week July (2020)	Weekly chg. (%)	Annual chg. (%)
Weekly Average	22,4	0,0	-61,9
Annual Average	28,8	-0,7	-51,7

Sources: BCV, MENPET, ONT and Ecoanalítica.
****Annual variation of accumulated expenditure.***
*****Reconverted amounts.***
[1]Depreciation (+)/Apreciation (-)
[2]FX Borads' average exchange rate.

Graphic of the week
Gender equality: A long road...

Global Gender Gap Index for Latin America



Note: This index measures scores on a scale from 0 to 1, where 1 means that there is greater gender parity.
****For Venezuela we use the latest available data in 2021, as it was included in the Global Gender Gap Index until that year.***
Sources: World Economic Forum and Ecoanalítica.

The Global Gender Gap Index assesses the world's progress toward gender parity in four key dimensions: economic participation and opportunity, educational attainment, health and survival, and political empowerment. It is the oldest index tracking progress toward closing gender gaps, created in 2006.

This index shows scores on a scale of 0 to 1, where 1 represents complete gender parity, where scores can be interpreted as the distance traveled toward parity, i.e., the percentage of the gender gap that has been closed. Cross-country comparisons are intended to leverage the identification of the most effective policies to close gender gaps. By 2022, the global gender gap has closed to 68.1%, a slight four-year improvement compared to the 2021 estimate. At the current rate of progress, it will take 132 years to reach full parity.

Latin America and the Caribbean ranks third in the overall index, after North America and Europe. The region has overcome 72.6% of the gap, an increase of almost 0.4 percentage points (pp) since the previous edition. Among the 18 countries shown from Latin America, and compared to the 2021 index, it can be seen that Peru and Chile have improved their gender parity scores the most, while Brazil, Mexico and Argentina showed slight stagnation and El Salvador, Honduras and Colombia regressed.

In the overall regional ranking, Nicaragua (81%), Costa Rica (79.6%) and Mexico (76.4%) occupy the top three places in Latin America, while Venezuela (69.9% in 2021), Brazil (69.6%) and Guatemala (66.4%) occupy the lowest positions.

Despite the progress made to achieve gender equality in recent years, it has not yet been achieved and there is still a long way to go to reduce the different gender gaps that exist in society, some of which, as a consequence of the crisis caused by the HIV/AIDS pandemic, have increased.

Tips
Economic, oil, sectorial and political

ECONOMIC TIPS

COVID-19 in Venezuela. According to government figures as of August 16, 2022, the country accumulated 540,681 registered cases of coronavirus and 5,779 deaths. In turn, according to OurWorldInData, it is estimated that 78.57% of the population has received at least one dose of some vaccine as of March 25, 2022.

Pragmatism and growth (I). According to Bank of America (BOFA), the Venezuelan economy will grow above 10% in 2022. Sebastián Rondeau, economist of the entity, expressed that the increase in oil prices and some signs of pragmatism in the national Executive have been key to alleviate the Venezuelan economy.

Pragmatism and growth (II). Rondeau emphasized that there are signs that the Venezuelan government has matured in economic matters; for example, it has allowed a certain degree of openness to private investments. In addition, Rondeau added that dollarization has been a good ally and has contributed to reduce inflation levels compared to previous years.

Productive credit. The Superintendency of Banking Sector Institutions (Sudeban) established that financial entities must allocate a minimum monthly percentage of 25% of their gross loan portfolio to the financing foreseen in the Single National Productive Portfolio, in contrast to the range between 10% and 25% that was in force until August 11.

Interventions continue. The BCV made a new foreign exchange intervention on August 8 for an amount of USD 90 million. With this operation, the BCV has injected USD 2,905 million to the financial system so far this year, exceeding in 46.5% the total amount for 2021. The sale price of this operation was VES 5.96/EUR, equivalent to VES 5.87/USD, being the fifth consecutive week with an increase in the quotation.

Average wages (I). Omar Zambrano, chief economist of Anova Policy Research, indicated that the average salary in the commerce and services sector for young employees is between USD 120 and USD 130 per month, according to his figures for the metropolitan area of Caracas. Regarding professional employees, the average salary is close to USD 200, while in the management area the figure rises to USD 300 or USD 350.

Average wages (II). Likewise, Zambrano indicated that these figures are not replicated in other sectors such as industry, agribusiness, manufacturing, financial and banking services, which is a sign that they have not yet recovered. Regarding the public sector, he pointed out that it is lagging behind, since the salary table oscillates around USD 20 per month.

Money tables. For the third week of August, the average money desk rate was VES 6.0/USD, representing a 1.3% depreciation from the previous week.

OIL TIPS

Production falls... OPEC's monthly report published that Venezuelan oil production in July was 629 kb/d, as reported by primary sources. This figure represents a 13.5% drop with respect to June's production level.

...according to both sources. According to secondary sources, Venezuelan crude oil production stood at 661 kb/d in July, which was 6.9% below the 710 kb/d produced the previous month. It is noteworthy that what was reported by direct communication is lower than what was recorded by secondary sources for the first time in several months.

Far below... OPEC members subject to quotas increased their crude oil production by 500 kb/d in July as part of the final phase of removing their supply cuts due to the COVID-19 pandemic; however, according to Argus estimates, it is still below their target for the month.

...and far from returning its cuts (I). The group's production of 38.70 mb/d remained 2.75 mb/d below its monthly target. Declining spare capacity, underinvestment and sabotage have dented the coalition's ability to return the 9.7 mb/d it withdrew from the market in May 2020.

...and far from returning its cuts (II). Among OPEC members, Saudi Arabia achieved the largest monthly increase in production in July. Exports rose by more than 550 kb/d per month and reached about 7.37 mb/d in July, and there was a seasonal increase in domestic crude oil burning for air conditioning.

Lower prices, although still high. The price of Merey, Venezuela's benchmark crude, fell 8.2% month-on-month in July to USD 84.72/bl. Even so, to date this crude has averaged a price of USD 81.86/bl in the first 7 months of the year, which represents an increase of 73.0% with respect to the same period of 2021.

Shipments are stopped. State-owned Petróleos de Venezuela S.A. (PDVSA) resumed last June the export of oil to Europe after a two-year pause caused by U.S. trade sanctions. However, this week, PDVSA suspended oil shipments to Europe due to the fact that the agreement has not granted the national company the cash and fuel it needs. For this reason, PDVSA asked Italian oil company Eni and Spanish oil company Repsol to supply it with fuel in exchange for future shipments.

Gas prices on the rise. Trading Hub Europe (THE), area coordinator of the gas market in Germany, reported that as of October 1 the price of gas for industry and households in the country will increase by 2.419 euros per kilowatt/hour. This price increase is caused by the supplement that the German government authorized the companies in the sector to charge to pass on to end customers part of the extraordinary costs that they must assume due to the reduction in gas supplies from Russia.

Record profit. Saudi Aramco reported a record net profit of $48.4 billion in the second quarter of this year generated by higher crude oil prices as a result of the war in Ukraine and strong post-pandemic demand. In this way, the company achieves its second consecutive quarterly record after announcing a profit of $39.5 billion in the first quarter of 2022. With these increases, the company's net profit increased by 90% compared to the same quarter last year and grew by 22.7% compared to the previous three months.

SECTORIAL TIPS

Pharmaceutical sector on the rise. According to data from the Chamber of the Pharmaceutical Industry (Cifar), the country's pharmaceutical sector grew 12.7% in the first semester of this year. Taking this into consideration, the president of Cifar, Tito López, informed that the industry is estimated to grow 19% by the end of this year with a distribution of 190 million medicines, which would be close to the numbers envisioned for the first semester of 2021, when there was a growth of 19.2% and a distribution of 159 million.

Less gasoline. According to the general secretary of the Federation of Oil and Gas Workers, Iván Freites, the production of gasoline in the country was reduced from 140,000 to 110,000 barrels per day due to the fact that the shipment of crude and condensates received by the country from Iran has been exhausted. He explained that the population only receives 10% of this gasoline because "from these 110,000 barrels per day, 50% of the quota sent by the Government to Cuba and 40% controlled by the military and high government officials must be deducted".

Reduction of the banking sector. According to Luis Oliveros, economist and financial advisor, Venezuelan banking reduced its personnel from 3,664 to 3,298 workers and the number of its agencies from 181 to 170 throughout the country, between December 2021 and June 2022. Oliveros added that the number of financial institutions was reduced to 26 after Citibank ceased operations and Banco Occidental de Descuento (BOD) sold its shares to Banco Nacional de Crédito (BNC). Finally, he commented that, as of May 2022, public banks occupied 65.02%, private banks covered 34.56% and microfinance banks represented the remaining 0.45% of the total market.

No financing to primary producers (I). José Luis Pérez, president of the Venezuelan Federation of Rice Producing Organizations (Fevearroz), explained that 42,500 hectares of the planting cycle that began in April 2022 are expected to be planted. He also informed that the rice planting stage of this cycle is culminating, with 90% of the planting intentions already completed. However, he said that, despite achieving these planting figures, only 30% of what was traditionally done would be sown.

No financing to primary producers (II). Finally, Pérez added that there is no direct bank financing for primary producers and that the little that exists is for companies. He stated that, not having their own resources, the producer is absolutely limited to execute what is offered by the industry or the association, an aspect that goes against the integral development that producers should seek to improve yields.

Venezuela and Colombia united. The president of the Venezuelan Confederation of Industrialists (Conindustria), Luigi Pisella, informed that this week he will start a tour together with the recently appointed Minister of Industries and Commerce of Colombia, Germán Umaña, in Cúcuta and Bucaramanga, with the purpose of talking about the formality of the exchange between the two countries and to establish agreements on what exportable offer can be provided from Venezuela.

Different sectorial perspectives. Olim Valera, president of the Chamber of Commerce of the state of Lara, explained that informality in the hardware and construction materials sector is approximately 60%, due to the high municipal taxes and the complex permits required by the national entities. He also commented that the automotive sector of the entity has registered a 25%

growth in inter-annual terms, which generates around 3,000 jobs. Finally, in the health sector, retail sales are down approximately 18% compared to 2021.

POLITICAL TIPS

Humanitarian plan (I). The United Nations (UN) launched a new humanitarian aid plan for Venezuela. It seeks to assist 5.2 million people with urgent needs and requires US$ 795 million.

Humanitarian Plan (II). The so-called "Humanitarian Response Plan 2022-2023" is a biannual roadmap that requires money this year to attend the most vulnerable populations in the country, mostly located in the states of Miranda, Sucre, Falcón, Bolívar, Delta Amacuro, Apure, Amazonas and Zulia.

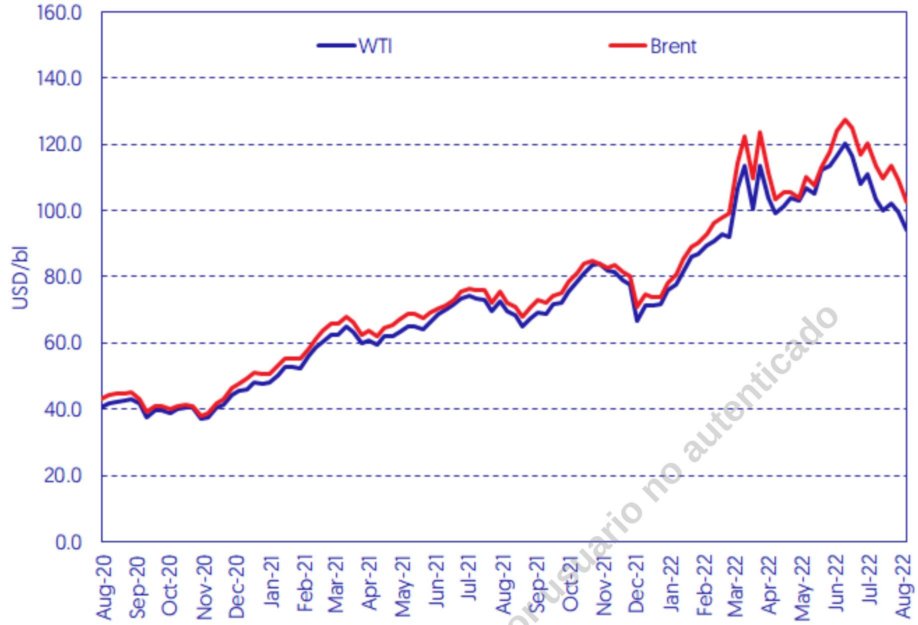
Persian market (I). Soldiers of the National Armed Forces started military maneuvers in Barquisimeto with Russia, China, Iran, Belarus, Uzbekistan, Vietnam and Myanmar, among others. The purpose of the military exercise was to exhibit their techniques and capabilities in the use of armored vehicles, AK-47 assault rifles, ammunition, long distance shooting with snipers and remote-controlled drones.

Persian market (II). The Spanish newspaper ABC indicated that this type of event is propitious for the organization of an arms market, which turns Venezuela into the "Persian market" for remote-controlled weapons. It is presumed that various groups of buyers, including criminal organizations, drug traffickers and adventurers, come to acquire the latest sophisticated weapons.

Firing and appointing. After weeks of protests in the education sector, President Nicolás Maduro fired the director of the National Budget Office (Onapre), Marco Polo Cosenza, and appointed in his place Jennifer Quintero de Barrios, and appointed Christian Moisés Hernández as head of the National Treasury.

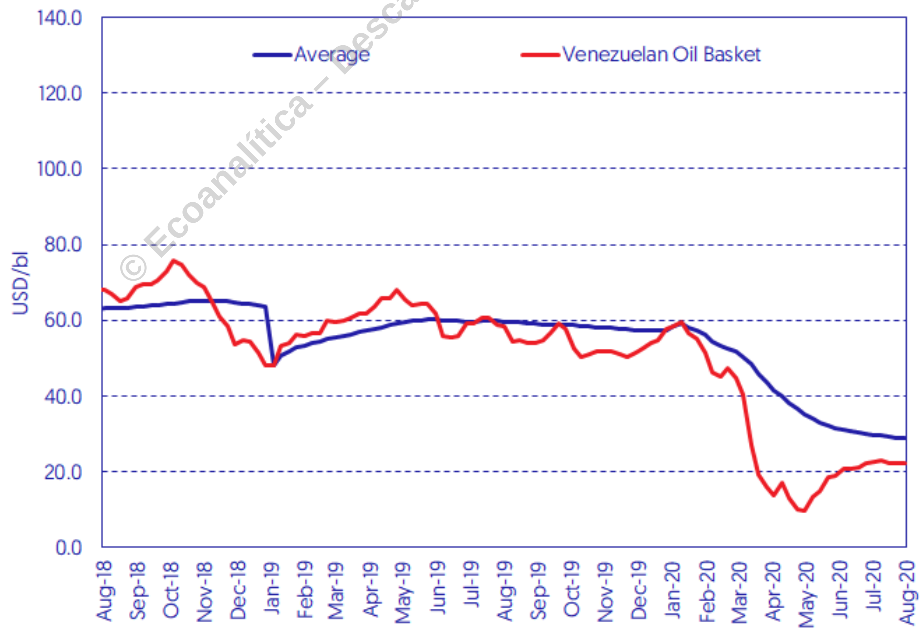
Credible versions are circulating. The former Undersecretary for Terrorist Financing of the U.S. Treasury Department, Marshall S. Billingslea, warned that Joe Biden's Administration could take measures to favor Alex Saab. Billingslea indicated that Washington could recognize Saab's alleged diplomatic role and thus "sabotage the judicial case against him".

Oil prices (WTI and Brent)



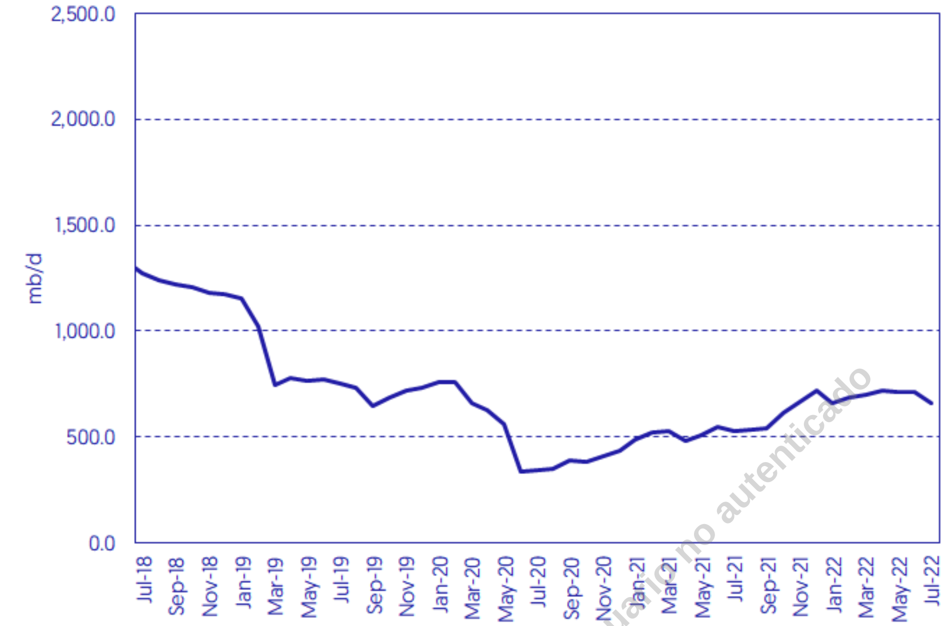
Sources: Menpet and Ecoanalitica.

Oil prices (Venezuelan basket)



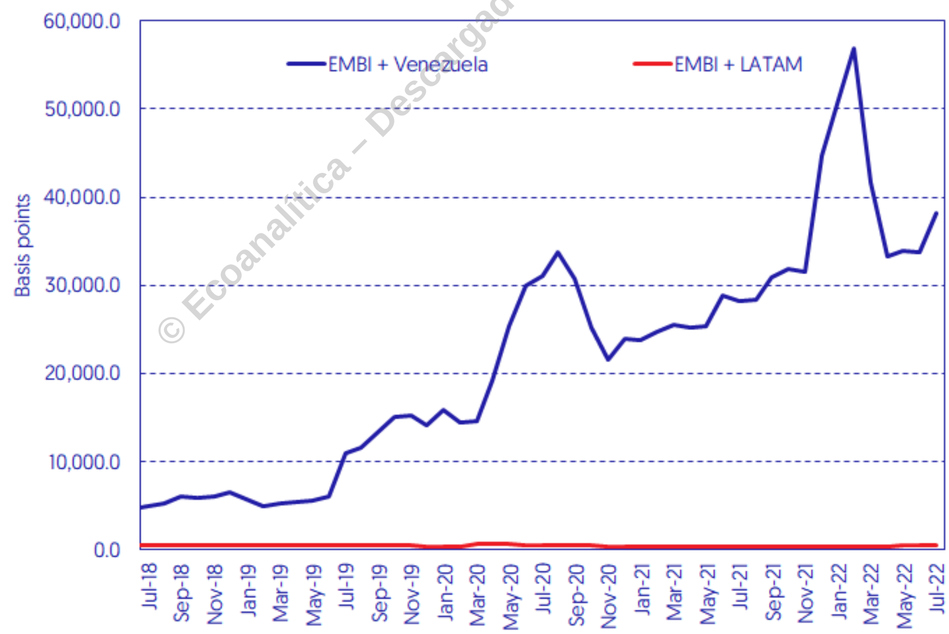
Sources: Menpet and Ecoanalitica.

Oil production (secondary sources)



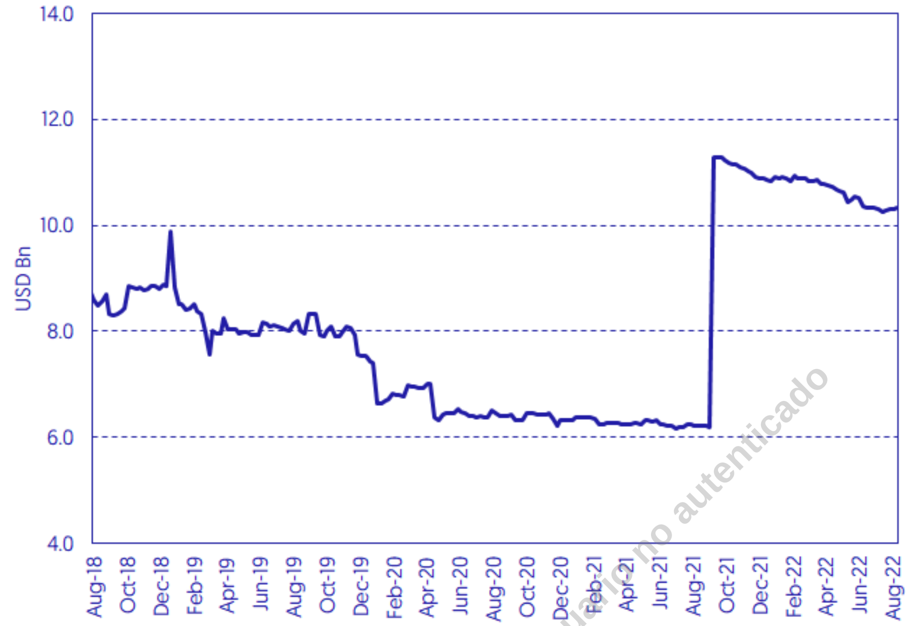
Sources: OPEC and Ecoanalitica.

EMBI



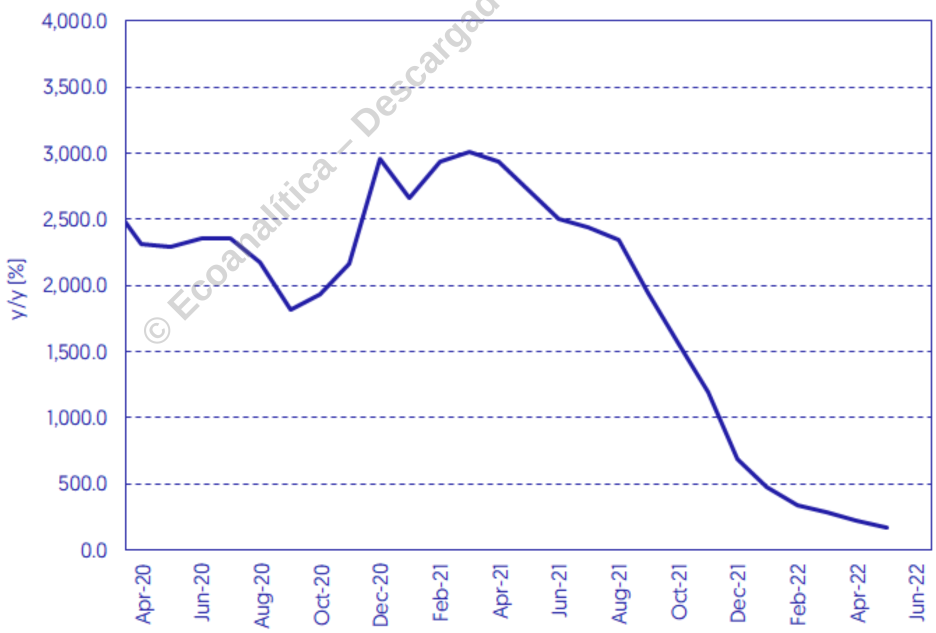
Sources: BCRP and Ecoanalitica.

International reserves (BCV)



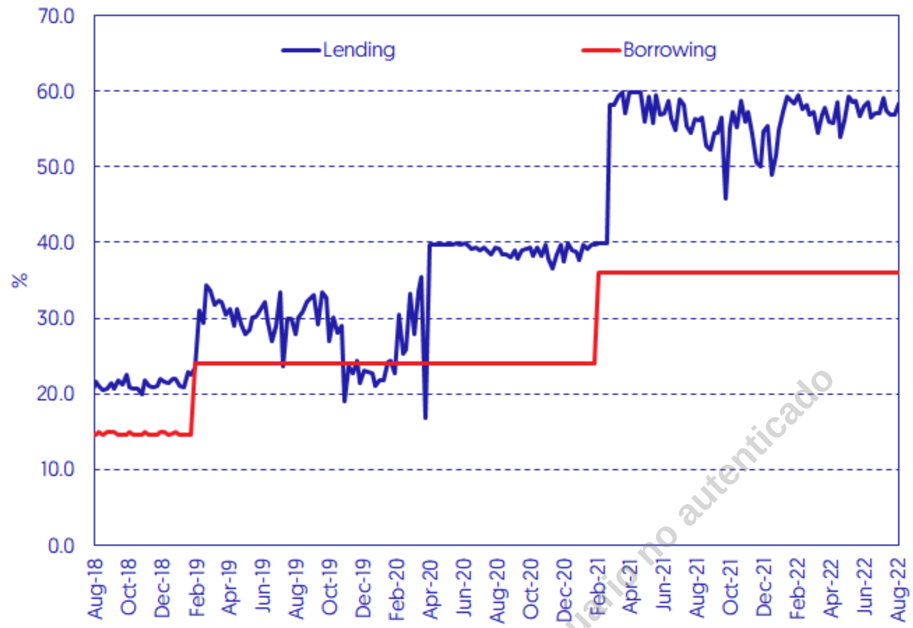
Sources: BCV and Ecoanalitica.

Inflation (BCV)



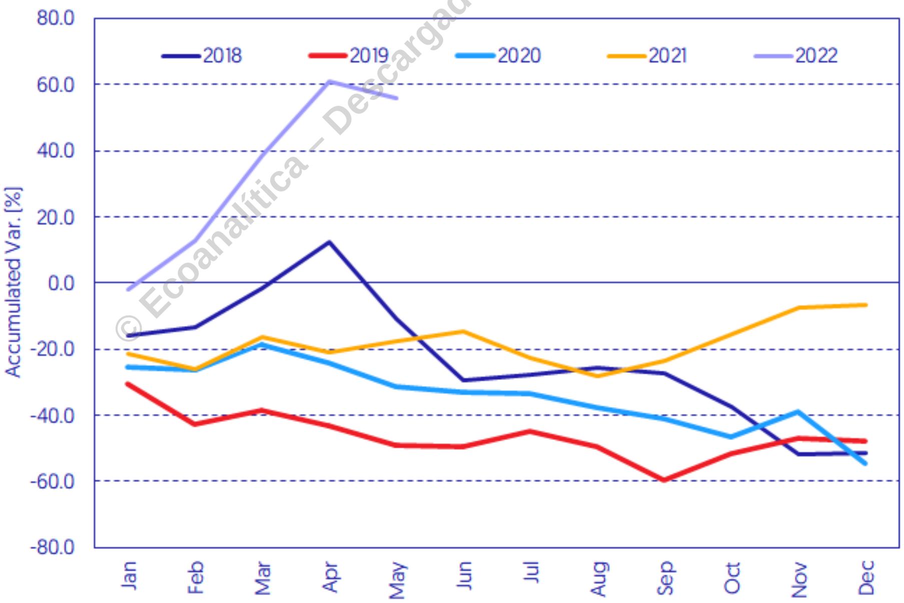
Sources: BCV and Ecoanalitica.

Interest rate (six major banks)



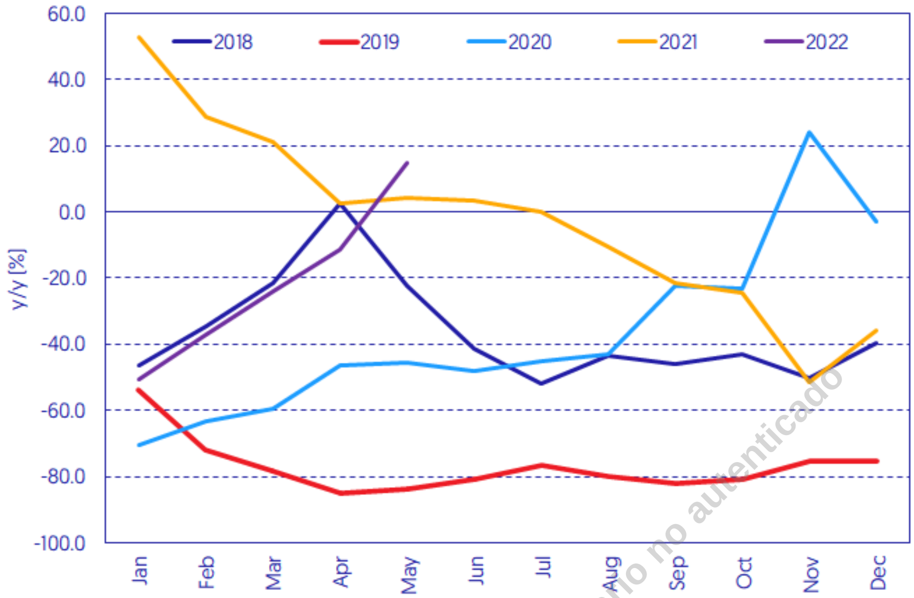
Sources: BCV and Ecoanalitica.

M2 Expansion (real)



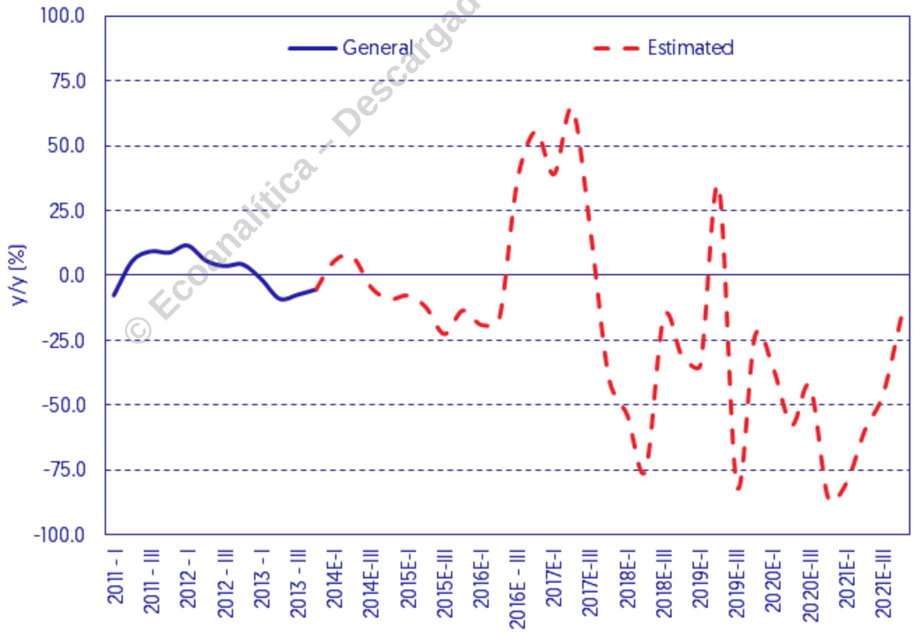
Sources: BCV and Ecoanalitica.

Loan Portfolio (real)



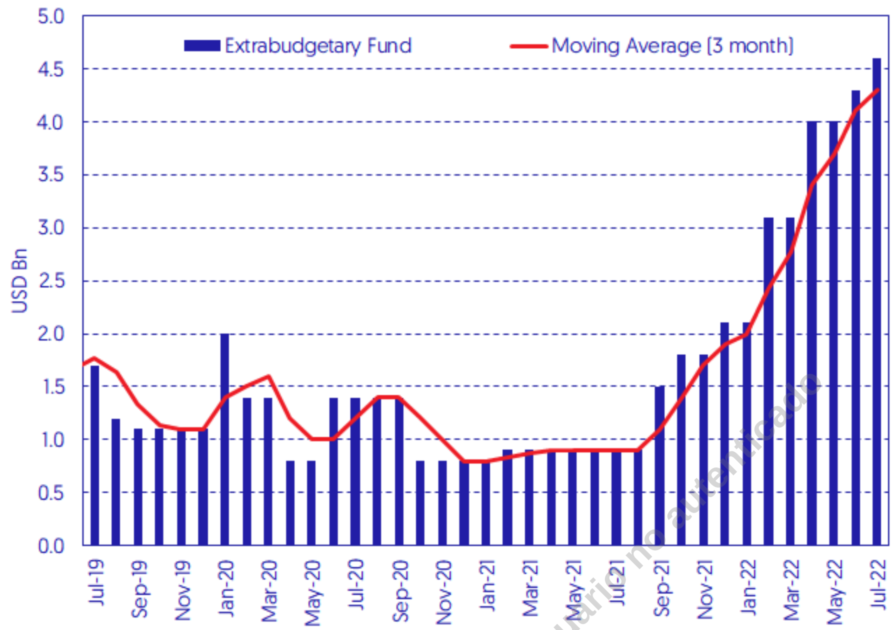
Sources: Sudeban and Ecoanalitica.

Real wage index



Sources: BCV and Ecoanalitica.

State extrabudgetary resources



Source: Ecoanalitica.

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