



Weekly Report

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What's going to happen with inflation? Price distortions stemming from the so-called "exchange unification"

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With the so-called "exchange unification" firmly in place, there is no doubt that now all the pressure falls on prices. The Administration is well aware of this and that's why they have begun their crusade against price gouging. Will this latest devaluation trigger a steady increase in prices during the coming months? We'll try to give an answer this question in this week's Report.

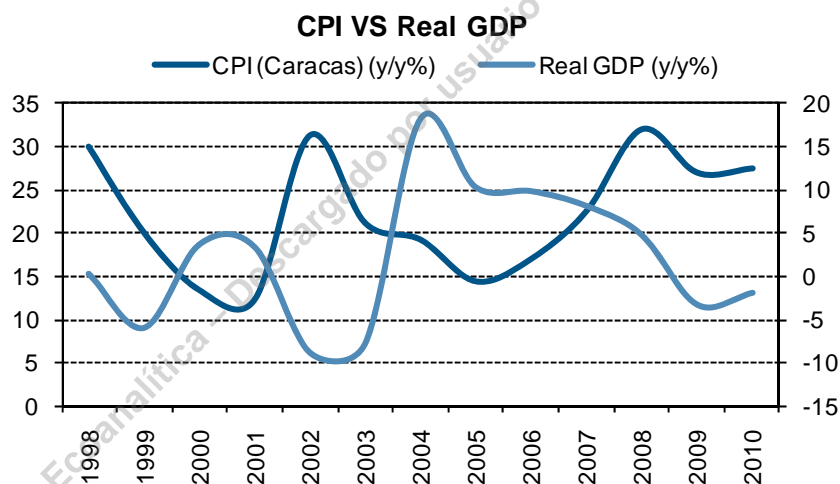
Socialist ideology producing ironic results: first in inflation and last in economic growth

As we mentioned in our last Outlook Report: Venezuela: Caught Between "The Road to Victory" and "A Lost Cause," Venezuelan inflation for 2010 closed at around 27%, nowhere near the goal set by the Administration at the beginning of 2010 (between 20% and 23%), but close to their readjusted inflation goal set in November 2010 at 26%. With this result, Venezuela becomes the country with the highest inflation rate in the world, this despite the fact that there is a price control mechanism in place, and strict price regulations being enforced. Along with this inflation rate, we have to add the country's less than stellar economic performance during the past



two years, leaving no doubt as to the complete failure of the Administration's economic policies.

And the road to a vigorous and self-sustaining process of economic growth along with an efficient control of our chronic inflation problem seems to be further away than ever, given that in order to begin going down such a path would require the Administration to completely revise the paradigms of the current economic policies. And it's very difficult to believe that this will be able to happen since there is no constructive dialogue or trust between the main players of the economy: the Administration, the private sector, and the workers.



Sources: BCV and Ecoanalítica

No sense: “a devaluation without price adjustments.”

Regarding the issue of the exchange rate, it's important to point out that in the 2011 National Budget project presented by the Administration before the National Assembly, and thereafter, sanctioned by the National Assembly in November 2010, it was established that the exchange rate would not suffer any adjustments and that the official exchange rates being used at the time would remain so during 2011. But this didn't happen, and for the second consecutive year, in January, the exchange rate was adjusted. In the words of the Minister of Planning, Jorge Giordani, the exchange rate was “unified” to the official exchange rate of VEB 4.30/US\$ “in order to simplify managing exchange operations,” hopefully this will help streamline CADIVI operations.

This latest devaluation, without any accompanying fiscal and/or monetary policies to compliment it and shape it into some sort of an attempt to



improve the economy, seems to be just a desperate measure by the Administration to generate more fiscal revenues in order to finance public spending during 2011, and possible 2012. This devaluation was much like other devaluations in the past, its only purpose being to help with fiscal matters, and this is why there is an inflationary price to pay that goes along with it; as has been the case in the Venezuelan economy since 1983.

Government spokespersons have made it very clear and the warning has gone out that there will be a crackdown on price gouging. And just to make sure everyone understood, the INDEPABIS promptly went out and closed 167 business for “unduly taking advantage” of the exchange unification. This suggests that any price adjustment after the devaluation will be defined as being price gouging, a fact that totally disregards an economic reality that these items being sold post-devaluation have to be replaced. In order to generate enough revenue to replace them, prices have to be adjusted, or else a business will run the risk of de-capitalizing.

Not sustainable

So, if one considers that the weighted devaluation was at 38% (29% for the private sector), and if we take into account the cost structure of essential goods, the current price control of goods and products, this absolute control of what's been called “price gouging” is not sustainable in the long term. Given the dynamics of production and commercialization that exist in the economy, the retail sale price of a product must be in accordance to the cost of replacing the product. If prices are not allowed to adjust for the devaluation, inventories will shrink, since businesses will not invest in inventories when they are not sure they will be able to earn enough to cover said investment.

And, if you take into account the current restrictions imposed by the INDEPABIS on companies aimed at limiting their stock of strategic goods, a control that began with the passing of the Law for the Defense of People in the Access of Goods and Services, companies now focus on keeping short term inventories, rather than risk being charged with hoarding by the government.

What sectors are vulnerable with this new exchange adjustment?

The official exchange rate of VEB2.60/US\$ was reserved for the import of selected food items, medicines, machinery and equipment, books, science and technology; as well as remittances, funds for students abroad, pensions, special cases, and embassies and consulates. This gives us an idea of the sectors that will be most affected by the increase to the new unified exchange rate of VEB 4.3/US\$).



As of January 1, these products will reflect an increase of 65% in their cost structure. That increase in import costs will have to be passed on to the final product price one way or another. However, if this will be allowed, or exactly how much will be able to be transferred, will depend on the Administration and its regulations.

Facing this new situation, and not all satisfied with the efforts of the INDEPABIS, the Administration is about to create a new office called the Superintendent's Office of Costs and Prices which will control the profit margins of the five sectors that most impact the Consumer Price Index (CPI): foods and alcoholic beverages, health, rent and house prices, restaurants and hotels.

Among the strategic plans of this new office will be to increase even more the role of the State in the setting of cost structures and the prices in the private sector in order to try to control inflation and stop price gouging.

In the end, none of these measures will be enough to generate a substantial difference in the production process, especially if you consider that it is being perceived as an isolated part of a whole set of other fundamental measures required to revitalize the private investment process.

Is this devaluation really a measure that takes social inclusion into account?

If one takes a very serious look at the composition of the price increase figures the outlook is very worrying. Most worrying, with respect to the affects of the devaluation, are food items. Its' not only the sector that most affects the CPI representing 32.2%, but it's also the sector that has increased in price more compared to last year at 33.8%, and especially agriculture products which increased by 55% compared to last year.

The health sector is also one of the six sectors which most impact the CPI representing 4.3% of the index. So, if we consider just these two sectors, we'll notice that they not only have a very particular connotation but also a very relevant one, especially when one considers one of the most important parts of the population. If we consider how prices are measured by social strata, with strata I, the poorest segment of the population, with the lowest amount of income, families in this group use approximately 45% of their salary to buy food.





Structure weights (%) NCPI

	Base Dec2007=100
Food and non-alcoholic beverages	32.2
Alcoholic drinks and snuff	3.0
Clothing and footwear	7.2
Rental housing	9.8
Service housing except phone	2.3
Equipment from home	5.6
Health	4.3
Transport	10.8
Communications	3.8
Recreation and culture	3.6
Education Services	2.7
Restaurants and hotels	8.8
Miscellaneous goods and services	5.8

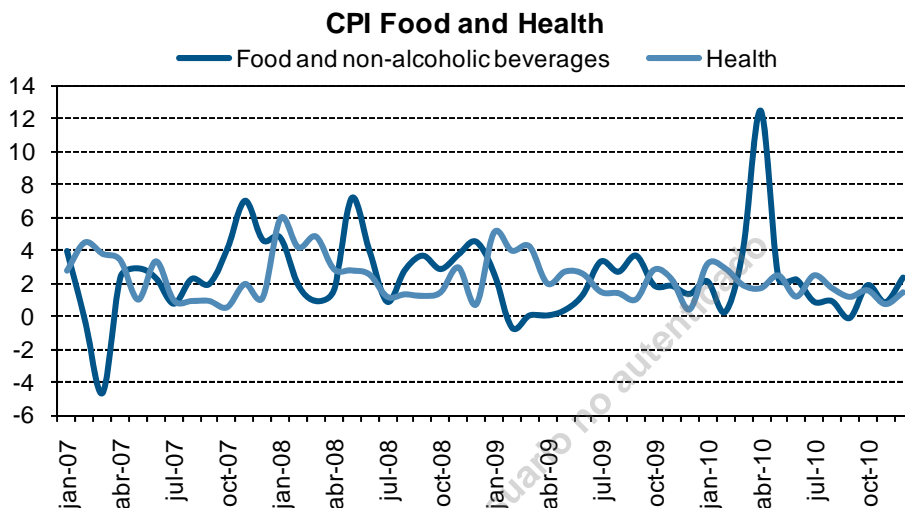
Sources: BCV and Ecoanalítica

A devaluation with regressive effects

With at least 70% of food items consumed by Venezuelans being imported, the impact of the devaluation will further erode the purchasing power of Venezuelans.

And this is why one can expect to see higher inflation rates in the lower income social strata than in some of the groups which have higher income. This seriously questions the sustainable efficacy of the social inclusion policies, food security and independence, the State intervening in the production chain and the distribution of food items, and the Administration's crusade to recover farmlands. In other words, we are facing a regressive devaluation in terms of the distribution of profits.





Sources: BCV and Ecoanalítica

Inflation in 2011, a serious problem

At *Ecoanalítica*, we believe that the Venezuelan economy will in fact register a slight recovery in 2011, but it won't post substantial economic growth rates in the medium term. As long as the Administration isn't willing to work together with the private sector, Venezuela's economic growth rates will be well below potential levels and the results for the general population will be disappointing to say the least. If the Administration's plan is to have the State be the star player with respect to the economy, then our growth rates won't be improving any time soon.

According to our estimates released before the devaluation, we had put inflation at 28% by the close of 2011. However, now, after the devaluation, and the adjustments that will have to be made by those sectors affected by the exchange unification, inflation will shoot upwards again reaching 30%. On top of this, shortages of some products will be more prevalent, if the Administration doesn't act and adjust prices, more so if you consider that the gap between controlled prices and market prices is on average around 72.9%.

More fuel on the fire

The devaluation will have an additional effect on inflation that we are calculating at 2 percentage points, but one needs to add on another factor that will increase pressure: the increase in food commodities which will also push points up a notch or two* and also make public subsidies more expensive. That's why public sector imports in 2001, according to our

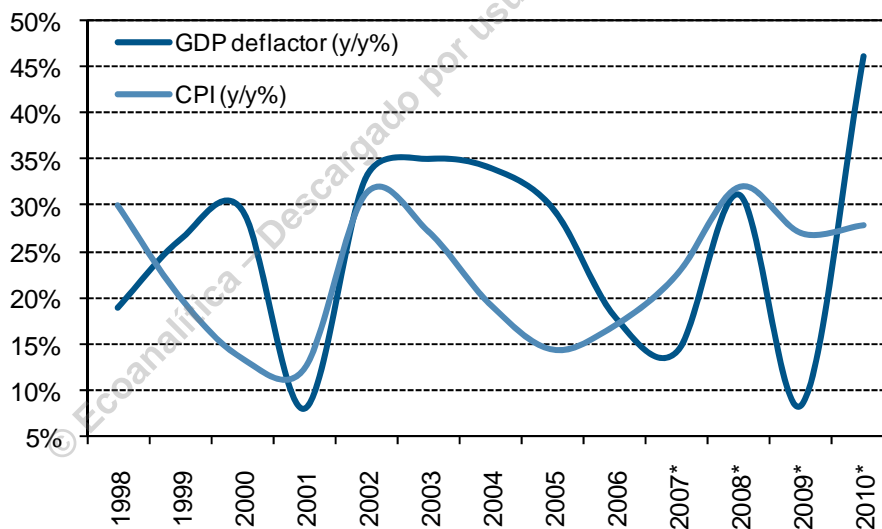
* We'll discuss this issue specifically in a Weekly Report



calculations, represented 35% of total imports, and of this amount around 71.7% was for food items.

What the price indexes don't show

The CPI is a weighted price index of 351 items in the Caracas Metropolitan Area, and it makes up a representative sample of what a typical Venezuelan consumes (we didn't use the National CPI in this exercise because it didn't start being used until December 2007), however, as price distortions begin to accumulate year after year during the tenure of the current Administration, price indexes begin to represent items less accurately with respect to the dynamics of prices ruling the economy. An example of this can be seen by the difference between the CPI growth rates and the GDP deflator.



Sources: BCV and Ecoanalítica
*Preliminary figures

One has to be careful when making this type of comparison because obviously you are talking about very different types of prices. While one is made up of a basket of 351 items to be consumed, the other is dealing with everything that is being produced within the economy (all countable goods and services in the GDP).

Even so, since the CPI is representative sample of how prices are behaving in the economy, such big difference should exist as those registered in 2009 and 2010, when the deflator increased by 8.4% and 46%, while the CPI increased by 26.9% and 27.8%, respectively. It's important to point out that



the GDP figures at current prices released by the Central Bank of Venezuela (BCV) are provisional figures and have been so since 2007.

And what do the official estimates indicate?

Inflation in 2010 at 27.2%; is far from where we would like it to be, but at the same time it generates a sense of hope among the monetary and financial government authorities. They firmly believe that they will be able to keep inflation down to between 23% and 25% in 2011, and that they will be able to whittle it down to single digits by 2012 or 2013. This seems quite ambitious considering that since 1985, no Administration has been able to get inflation down to single digits, unlike other regions that have achieved this objective.

Force of habit

Inflation during 2011 will continue with its tendency to increase, and Venezuela will continue to be an economy with very high and persistent inflation. We are not predicting that inflation will go beyond 35%, which leads us to this thought. In Venezuela, all the economic agents, especially the private sector have gotten used to doing business in a environment of high inflation (especially if we compare ourselves to our Latin American neighbors). But from now on, inflation will begin to weigh a bit more heavily because the country's economic growth rate will pretty much be at bare minimum. In the medium term, the big challenge facing the private sector will be to face inflation rates at around 30%, an economy that is growing well below its potential, and even almost at zero percent. Not an easy thing to do.





Economic Tips

US\$18.86 billion less than in 2008. The Currency Administration Commission's (Cadivi) currency liquidation in 2010 was not very different from that of 2009, with a slight variation by 1%, an increase by US\$28,961.90 in 2010 compared to 2009. However, compared to 2008 numbers, there was a 39.3% contraction since that year, the currency distribution reached US\$48.03 billion or US\$18.86 more than the amount released last year. This considerable contraction matches the national Administration's wish to apply a policy of "necessary imports," just like minister of Planning and Finance, Jorge Giordani, has mentioned in several opportunities.

Amount disbursed by Cadivi (US\$MM)			
	2009	2010	Var(%)
Imports	14,924.5	19,857.6	33.1%
Students	266.0	392.8	47.7%
Special cases	79.0	135.6	71.6%
Airlines	893.7	1,299.7	45.4%
Ext Private Debt	39.8	16.8	-57.8%
Consulates and Embassies	83.7	63.7	-23.9%
Insurance and Reinsurance	149.0	84.3	-43.4%
Foreign Investment	533.4	38.8	-92.7%
ALADI Convention	6,070.3	4,299.1	-29.2%
Retirees and Pensioners	52.1	70.0	34.4%
Remittances to family	547.0	760.8	39.1%
Credit Cards	3,344.5	1,452.7	-56.6%
Cash for travel	315.2	300.6	-8.5%
Services	9.5	1.3	-86.3%
Telecommunications	41.1	102.9	150%
Total	27,348.8	28,876.7	5.6%

Sources: CADIVI and Ecoanalítica

What does this contraction tell us? Despite the recovery of Venezuela's main source of foreign currency, there was no increase in Cadivi's distribution. The slight 0.6% increase in 2010 compared to 2009 reflects the shifting of private companies into state hands, a process that results in an increase in public sector imports that are not registered by Cadivi. Along with that is Pdvsa's evident decrease in production, which



means the rise of oil prices does not represent a significant increase of available currency.

List of goods that will be liquidated at 2.60 VEB/US\$ already available. The list of currency liquidation authorizations for imported goods (received before December 31 of 2010) to be liquidated at 2.60 VEB/US\$ was published by the Central Bank of Venezuela (BCV) and certified by Cadivi. This decision was established in Exchange Agreement number 15 signed by Ministry of Planning and Finance and BCV authorities on January 10 of 2011 and published in Official Gazette No. 39,349.

Government spent VEB 233.16 billion in 2010. According to numbers released by the National Treasury Office (ONT), the central government spending reached VEB 233.16 billion in 2010, a 20.9% nominal increase compared to 2009 when the government spending was VEB 192.85 billion. Subtracting the effect of inflation, there was a 5.0% decrease in real terms.

On the income side. As to the government's current income (VEB 198.57 billion), they covered 85.2% of 2010's executed spending. In nominal terms, financing expanded by 29.5% off current income, comparing to 2009's results, as a consequence of the oil tax revenues generated by the devaluation of January 2010.

That leads us to a financial deficit. The unbalance between the Government's current income and total spending results in a deficit of VEB 34.59 billion, approximately 3.9% of Venezuela's GDP, a 1.8% contraction compared to 2009 when the deficit reached VEB 3*9.57 billion (5.7% of the GDP).

CHART – CG INCOME AND OUTCOME ADMINISTRATION 2009 vs. 2010

16% of 2010's budget was funded by debt bonds. In 2010, the issuing of Sovereign Bonds and Treasury Bills funded 16% or VEB 31.30 billion of the National Budget, according to information provided by the Ministry of Planning and Finance. This shows that the Government's policy of issuing public debt certificates to finance part of the national budget is still one of the most active fiscal measures in the Chavez Administration. However, this indebtedness policy is also used as an alternative to feed the "parallel budget" and keep it from collapsing.

Venezuela among the 5 countries that reported increasing unemployment rates. According to the 2010 labor outlook report prepared by the International Labor Organization (ILO), only five countries in Latin America and the Caribbean reported increasing unemployment figures. These five countries are Honduras, Venezuela, Barbados, Jamaica and Trinidad & Tobago. In light of this, report author, said: *"the countries showing increases in unemployment rates have still not been able to recover*



from the deceleration of the world's economy and that's reflected in their own economic growth."

Index of economic freedom. In a study prepared by the Heritage Foundation and The Wall Street Journal, Venezuela is included among the group of countries with the most "repressed" economies in the world. Out of a total of 179 nations, Venezuela ranks 175th, a step down from 2010's ranking, beating only Eritrea, Cuba, Zimbabwe and North Korea. In contrast, the nations with the most economic freedom are: Hong Kong and Singapore, Australia, New Zealand, Switzerland and Canada. The 2011 Index of Economic Freedom is based on 10 measures that assess openness, rule of law and competitiveness, and rates countries based on their economic freedom.

Interest rate. The lending rate for the third week in January was at 18.1%, down by 1,4% compared to the previous week. Time deposits and savings rates were steady at 15.5% and 12.6%, respectively.

International reserves. International reserves increased 0.4% going from US\$29,54 billion during the second week in January to US\$29,66 billion during the third week of January. Compared to the same period last year, international reserves have dropped by 8.7%.

Monetary liquidity. Monetary liquidity for the second week in January was down 0.2%, compared to the previous week settling at VEF 295.1 billion. The M2 has increased 25.4% year-on-year.

Sitme figures. To date, US\$5,6 billion have been negotiated through the Integrated System for Foreign Currency Transactions (Sitme), averaging US\$34.7 million a day, with an implicit exchange rate of VEF 5.3/US\$. Last week the traded amount reached US\$117 million, US\$14 million less than last week when braided US\$132 million.

Oil Tips

Pdvsa's tax contribution decreased by 10.5% in real terms. According to numbers provided by the public finance office, in 2010 Pdvsa submitted a total of VEB 60.8 billion to the tax administration for royalties, dividends and other taxes, that is 14% more in nominal terms than 2009's contribution (VEB 53.2 billion), although crude oil



prices increased by 27.5%. Additionally, considering last year's inflation, Pdvsa's tax contribution decreased by 10.5% in real terms.

Less Income Tax despite higher oil prices. Reviewing Pdvsa's tax contribution we can observe it paid 28% less in income tax in nominal terms, going from VEB 12.9 billion in 2009 to VEB 8.7 billion in 2010. The reason for this, despite the increase of crude oil prices, is the increase of Pdvsa's obligations and operation costs. Price increases do have a direct relation with Pdvsa's contribution due to oil revenues royalties, which grew from VEB 31.8 billion in 2009 to VEB 42.05 billion in 2010, (32.3%).

Oil agreement between Venezuela and Turkey. A Turkish delegation will visit Venezuela on February 11 to reach an agreement discussed last week between the Turkish Minister of Energy and Natural Resources, Taner Yildiz, and his Venezuelan Homologue, Rafael Ramirez. With this agreement, Turkey hopes to be allowed the exploitation of two oil extraction fields in the Orinoco oil belt and the possibility to establish a joint refinery in Turkey to allow them to import crude oil at prices below international market standards in approximately one and a half years.

Exchange. With the agreement, Venezuela will be able to obtain electric investments from Turkey for approximately US\$2 billion, and infrastructure and real estate investments still to be defined. It is estimated that Turkey has a capacity to build 470,000 homes per year.

Two Orinoco oil belt projects to be put on hold due to maintenance. A 35-day stop is scheduled between June and August to perform maintenance labors on the facilities of the extraction and mixing project integrated by China Petroleum Corporation (CNPC) in the Orinoco oil belt (FPO), and for the same reasons, Petroanzoategui's heavy crude oil upgrader, which processes 130 kb/d, will be put on hold for 40 days between August and September.

Pdvsa Gas Comunal buys Tauro Gas Distributor. Pdvsa keeps expanding its liquefied oil gas (LOG in cylinders) distribution network, as it purchased the company Tauro Gas, which was in charge of distributing gas cylinders in the municipalities of Libertador, Baruta, El Hatillo, Los Salias and Sucre, in the Caracas metropolitan area.

Opec urged to increase production. Yesterday, the Center for Global Energy Studies (CGES) urged the Organization of Petroleum Exporting Countries (Opec) to increase its production in order to balance the market and moderate the price of a crude oil barrel, closing in on the US\$100 barrier for a few weeks now. The organization condemned the crude oil exporting cartel's resistance to understand that these are the market's circumstances, with an *"unexpected increase of demand,"*



acknowledging that Opec doesn't have the faculty to stabilize prices at a specific level, but that it's there to promote the interests of its member countries.

Gasoline prices increase while oil prices decrease. Last week, the price of a gallon of regular gasoline went up to US\$3.1. These are the strongest prices since October 2008 and are almost double the prices of December 2008 when gasoline reached a price of US\$1.6/gallon. On the other hand, crude oil prices decreased last week to US\$89.8 per barrel, while early this week the price reached US\$86.7/bl, the lowest since November. The economic analysis consulting agency Haver Analytics expects gasoline prices in the US to reach US\$3.4/gallon this quarter, even though the seasonally adjusted demand increase has been lower than expected.

International oil baskets. At the close of the New York market last Thursday, January 27, the WTI was at US\$85.6/bl, showing a 1.8% decrease compared to the US\$88.2/bl of the previous Thursday. The Brent increased by 1.0% to reach US\$97.3/bl, compared to US\$96.3/bl of the previous Thursday.

Local oil basket price. The Venezuelan oil basket price increased last week, to close at US\$86.8/bl on Friday, January 21, up by US\$1.03 or 1.0% from the US\$85.87/bl registered the previous week. Meanwhile, the basket's annual average is at US\$85.9/bl.

Business Sector Tips

Administration contemplates taking measures in the agriculture-food industry. A complicated scenario in the field of production could push the administration to take some measures to take care of both the consequences of the heavy rains on agricultural lands, and the effects of the devaluation of the preferential exchange rate for food and other products and basic supplies.

There is enough flour and oil for two months. The president of the National Federation of Flour Industry Workers (Fetraharina), Juan Crespo, said within approximately two months people would begin to notice the shortage of oil and wheat flour and, in consequence, pasta and bread. The situation has a local motivation: imports at VEF/\$ 4.3, as they generate a price adjustment in wheat flour and its byproducts, as well as the basic supplies to manufacture oil.





Water processing lines reactivated at the Coca Cola Femsa plant in Carabobo.

The secretary of Acts and Correspondence of Coca Cola Femsa workers' union, Regino Romero, said the restart of operations is based on the plant's need to operate with the minimum necessary services established in the Organic Labor Law to carry out a labor strike.

Purchasing power decreases and consumption credit falls. A report on the financial system as of the end of 2010 evidences that families consume less and therefore, credit card financing and vehicle loans decrease.

Administration denies decrease in rice and corn production. The National Administration denied there being a decrease in rice and corn production as a consequence of import policies. According to Elias Jaua, vice president of Venezuela, this problem came as a consequence of the weather conditions.

Western transmission network presents structural weakness. Despite the low early year demand, Cadafe Occidente is importing energy from the lower Caroni River. This exchange process "violates transmission limits not only during rush hours, as it occurs in some Central states, but all throughout the day." During 2010 there were two interruptions in the country's western region (April 24 and August 6), due to malfunctions in the transmission network, affecting Andean and Plane states and the Maracaibo Lake's South coast area. On January 17, 2011, there was a similar event; this time the electric demand was 15,188 Mw.

Electric Objective: Armoring Caracas. In order to make Caracas independent from the energy supplied from the Caroni River, the National Government hopes to incorporate a total of 2,913 Mw to the National Electric System (SEN), through the execution of different projects being carried out in the Miranda and Vargas states.

Giordani: Home construction will boost the economy. According to recent statements by Minister of Finance, Jorge Giordani, the nation's economy will grow by 2% this year. However, he did not rule out the possibility of a better performance if the government is able to execute the home construction plan. Minister Giordani said that the national government's optimism about the economy was well based. *"This economy will continue to grow and that's not just optimism. We have our feet on the ground and our eyes on the universe."*

TSJ measure has 20,000 tenancy trials in suspense. The president of the Venezuelan Real Estate Chamber (CIV), Aquiles Martini, said that the Supreme Court of Justice's (TSJ) measure to suspend all legal actions on properties generates uncertainty. Due to that decision, 20,000 tenancy trials are now in suspense.



Caution in the automotive industry. The negative result of the last three years and the recent devaluation suggest that the automotive business will remain contracted this year. After the devaluation announced by the National Government last December 30, the sector's alarms went off, since this makes this sector's situation even harder. However, the industry expects to maintain the same production levels and sales reported in 2010.

Labor claims continue in Guayana industries. Workers deny companies increased production, according to recent statements issued by the secretary general of the CVG Bauxilum Workers' Union, José Mocomia, about the operative situation of iron, aluminum and steel companies: "you can't lie to the nation and say Guayana's companies are 100% productive."

90.9% of industries have short term inventories. The latest Qualitative Industrial Survey carried out by the National Institute of Statistics (INE) corresponding to the third quarter of 2010 indicated that 90.9% of manufacturing companies had enough product inventories for only three months of sales.

Cadivi and Sitme cover only an average of 30% of the required foreign currency. According to a recent measure made by Venancham amongst the sector's members, out of the total foreign currency required to operate in Venezuela, an average of only 30% can be covered through SITME and CADIVI.

Mining activity contracted by 60% since 2009. The national mining sector is no stranger to the contractive behavior reported by other segments of the productive activity. According to numbers issued by the Central Bank of Venezuela, over the last two years, the mining industry has contracted by approximately 60%. The president of the Venezuelan Mining Chamber (Camiven), Luis Rojas Machado, says there are many factors influencing this performance, with the most important being "a lack of a mining policy, information and dialogue."

Sales volume down by 17% in December of 2010. As of December of 2010, the Mass Consumption Products' Committee reported a sales volume contraction by 17%, registering a cumulative y/y average of -15%. Last month, sales value grew by approximately 25%, 24% more than the average at the end of 2010.

Government to create chain of low-priced butcher shops. The National Administration is preparing an expansion plan for the Nutrition Mission which will contemplate, among other aspects, injecting more resources to the purchase of supplies and creating new product distribution networks. Among the new distribution networks will be a chain of butcher shops. However, this proposal has already been applied twice by State organizations and has had no significant effects on the market.



More spending. Chavez said that, according to FAO, food prices blew up “because of the weather conditions and the demand of large countries.” He also announced there would be an additional budget for over VEB 2 billion to acquire food products.

President Chavez will be entitled to order banks’ audits. The reform to the Law of Banks gives more power to President Hugo Chavez, who, according to article 8, will be entitled, in a Ministers’ Council, to “agree upon the auditing, liquidation or any other measure deemed necessary, over banking institutions, as well as over their related or associated companies.”

Sivensa sales reported a 34% fall. Sivensa’s sales for the fiscal year ended on September 30 reached VEB 1460 million, 34% less than in the previous year, and all of them correspond to the sales of Sidetur’s affiliate. The company’s results reflected the impacts of the electric crisis and the 6% fall in the construction sector’s economic activity.

Expropriation of urban lands ordered. Decree No. 8,011, published in the Official Gazette No. 39,600 dated January 24, 2011, orders the expropriation (forced acquisition) of lands located in the parishes of Altigracia, El Paraiso, La Vega, El Recreo and San Bernardino, Caracas, Libertador Municipality, to be used to build “Suitable Homes for The People”.

Government to hand-in expropriated homes in 2 years. In November of 2010, the Venezuelan Government expropriated and occupied housing developments nationwide because construction companies were delayed in the culmination of the housing units and charged the consumer price index adjustment in the pre-sale agreements, but according to the Minister of Commerce, Richard Canan, said homes will be handed-in within 2 years.

International airline sales down by 20% in 2010. The president of the Venezuelan Association of Airlines (ALAV), Humberto Figuera, said in a press conference that international airlines sales measured in US\$ had decreased by 20% in 2010 compared to 2009. The executive indicated this behavior was related to the currency devaluation that took place early in 2010, when the exchange rate went from 2.15 to 4.30 VEB/US\$.

Russian participation in plantain plantations under negotiation. Information from Moscow released by the newspaper Kommersant indicates “the Russian banking tycoon Vladimir Kejman and the Venezuelan Food Corporation (CVA) are planning to embark on a joint venture to handle more than half of Venezuela’s plantain plantations.”



World Economy Tips

Euro zone manufacture grows but Germany and France decelerate. Markit Economics, the firm that prepares the monthly flash survey of purchasing managers in approximately 30 countries, published the overall estimations of euro zone purchasing manager surveys as well as for Germany and France. The survey covers the manufacture and services industries as well as a combination of both. Readings over 50 indicate expansion and those under 50 indicate contraction. January results show increases in the combined index for Germany and France. As for the euro zone, the index went from 55.0 to 56.3. However, reviewing both indexes separately, both Germany and France have reported decreases in manufacture, with the first going from 60.9 to 60.2 and the latter going from 56.3 to 54.3. Despite these slight decreases, both countries are still over 50, and Germany is getting closer to its pre-recession levels.

IMF about the Situation in Europe. According to the IMF, the effective volume of Europe's financial rescue fund should be raised, and its banks need to undergo rigorous tests of tension to restore the markets' trust. The problems in Greece, and now in Ireland, have revived questions about the sustainability of the sovereign debt and the health of the banking system in a wider section of the euro zone, and possible beyond it, said the IMF. For those reasons, the Fund recommended an increase in the effective size of the European Financial Stability Facility (EFSF), and said it should have a more flexible ruling to ensure access to financing. The Fund talked said the European Central Bank needed to continue to grant the stimulus to banks that needed it.

US: Loans defaults decreased but remain at alarming levels. The American Bankers Association said last week that the defaults of all kinds of loans have reported decreases. Credit card defaults are down by 3.6%, after having reached more than 5.0%, which reflects a reduction in consumption. As to other consumption loans, the numbers are much lower than the peaks reported in the 90s, while mortgage loan defaults showed a more modest reduction. However, these decreases vary from line to line, so many analysts think they are not enough and defaults are still high compared to pre-crisis levels.

High number of defaults has had the strongest impact on loan disposition. Up until the third the third quarter of last year, the loan portfolios of US banks and savings institutions decreased at y/y a rate of 0.4%, much less than the previous year's 10.6%. However, this situation is alarming and sends mixed signals: for construction and



development loans, the rate of decrease reached 27.0% y/y, while mortgage loans dropped at a steady pace of 3.7% y/y. Individual loans took a positive turn early in the year, growing by up to 25% in 3Q2010. Commercial and industrial loans stopped falling intermittently but reported a 7.8% y/y decrease. The same happened with residential mortgages which decreased by 2.5% y/y.

IMF: Global Economy to grow by 4.4% in 2011. In an update to its annual report "World Economic Outlook," the International Monetary Fund said the global economy would grow by 4.4% this year, slightly higher than the 4.2% announced in October. For 2012, the IMF projects a 4.5% growth. For the Fund, the fiscal cutbacks of late 2010 will probably boost the US growth by 0.5% this year, while a stimulus package in Japan will help maintain a moderate global recovery. *"Overall, the signs of private consumption -which fell significantly during the crisis- are beginning to strengthen in advanced economies,"* said the institution. The IMF indicated the US economy would probably report a 3.0% expansion this year, representing a significantly positive review from the 2.3% announced in October. For the euro zone, the IMF maintained its projection of 1.5% and estimated the European economy would improve by 1.7% next year.

Panama: Latin American Star. Panama's economic activity expanded by 9.5% in November of 2010 compared to the same month of 2009, said last Tuesday the government of this Central-American country. According to the information, the transportation and telecommunications sector greatly contributed to this expansion, due to the transit of vessels through the Panama Canal and the railroad activity. The commercial activity in the great Caribbean free trade zone of Panama also contributed to this growth. Panama's economy, mainly sustained by the services sector, is one of the best performing economies in the region and the government expects a growth close to 7% in 2010.

Political Tips

Human Rights situation is "precarious." Human Rights Watch director for the Americas, Jose Miguel Vivanco, held a press conference in Washington to present the results of the organization's annual report regarding Latin America. In this report, HRW states the human rights situation in Venezuela is "precarious" and that the Government "has control" over the judicial power and "systematically undermines" freedom of speech. Vivanco indicated there have been human rights "setbacks" over the past few months, especially in December when the National Assembly, among



other things, authorized an empowering law for President Hugo Chavez to legislate by presidential order for 18 months.

Afiuni case in sight. HRW also condemned that the Venezuelan Government has some control over the judicial power, and warned that *“judges appointed against Government interests could suffer from retaliation.”* Vivanco quoted the case of Judge Maria Lourdes Afiuni, indicating the “inhumane” conditions in which a person suffering from cancer lives in prison. According to Vivanco, the judge acted *“by the rules of the Venezuelan game”* and *“public prosecutors said there was no evidence of corruption,”* adding that, unless the necessary measures were taken in the Afiuni case, for whom President Chavez publicly requested the worst punishment, a precedent of “severity” will be set in Venezuela.

Generalized deterioration. Certainly, HRW believes the Chavez Administration has reinforced the State’s ability to limit freedom of speech and has created powerful incentives for government critics to censure themselves, such as the modifications to the Penal Code expanding the reach of “contempt” laws and penalize expressions considered to be offensive for high rank officials.

Venezuelan press tones down Government critiques. An article in the Spanish newspaper *El País* indicates that several mass media companies have incurred in financial losses due to the massive retreat of publicity spaces of public or nationalized companies. The article analyzes what happened with RCTV, the Globovision case, Guillermo Zuloaga and Alberto Ravell, the financial situation of the newspaper El Universal after the nationalization of the chain of supermarkets Exito, the losses reported by the newspaper El Nacional and the moderation of Venevision’s anti-government orientation concluding that *“the confrontation developed in Venezuela during the Chavez Administration is so virulent in the press that anti-government media channels acknowledged having toned down their critiques to avoid being economically strangled by the Government.”*

MUD proposes plan for housing crisis. Representative Andres Velasquez said it without beating around the bush: *“President Chavez will fail his promise of building 150,000 homes this year.”* The accusation, formulated during a press conference in representation of the Democratic Unity Table (MUD), is based on the fact that, in order for Chavez to be able to live up to his promise, the Government would have to build 12,500 homes per month, and with January over, not a single home was built, besides the fact that Chavez’s policy to order on national broadcasting people in need to go out and invade abandoned warehouses and buildings what does provoke are “disasters,” said the representative. Velasquez spoke yesterday in representation of the Labor, Production and Property Commission, and proposed a twenty-step plan to “have a home in peace” to be developed by the National Assembly.



Indicted for invasions. The Public Ministry indicted 11 people for their alleged implication in several property invasions in the Chacao municipality, Miranda State, last Saturday January 22. At the hearing carried out before the 2nd Court of Control of the Metropolitan Area of Caracas (AMC), the 17th District Attorney of the aforementioned jurisdiction, Carmen Elena Padron, indicted Nelson Coro Blanco and Angel Antonio Rangel Yanez for allegedly committing the crime of usurpation, provided and penalized in the Civil Code. Said citizens were arrested by Chacao Police Department officers.

Opposition mayors condemn last weekend's invasions. The Mayors of Sucre, El Hatillo and Baruta condemned the invasions occurred in Chacao and regretted the Government's attempt to solve the housing problem by generating other problems. The first authority of Sucre, Carlos Ocariz, assured he understood these people's need of a home, but said that taking others' properties by force would not only be a great injustice, but would also generate a terrible sense of distrust in the country. Ocariz indicated that three pieces of land in Sucre (Mariche and Petare) had been offered for the National Government to build houses for those affected by rains in this municipality, and that the government had not replied yet: *"If the real intention is to solve the problem, why haven't they reached out to us?"*

PSUV: "turned away from reality". President Chavez announced a number of self-critiques to the United Socialist Party of Venezuela (PSUV) in a meeting in the Vargas state, including the fact that the party is turned away from the people's reality, it can't continue to be only an electoral machinery, and its members should embrace socialism and leave capitalism behind. He also condemned his governors and mayors and urged them to step away from the party unless they could work together as PSUV militants and assume their responsibilities.

Russian tanks arrive to Venezuela. Despite opposition criticism, Hugo Chavez announced the arrival of a lot of Russian armed tanks. He also reminded having bought training planes and radars from China and rifles, helicopters, planes and tanks from Russia. *"With this equipment we have upgraded Venezuela's arms stock,"* Chavez said, and added *"the Venezuelan high class attacks my arming policy because, following Washington's orders (...) they would like to eliminate our Armed Force and thus facilitate the US ultra-right wing plans to stop the Bolivarian revolution."*





Legislative Tips

Human rights to be discussed at Parlantino. During the current period, representatives of the Democratic Unity Table (MUD) in the Latin America Parliament (Parlatino), proposed the discussion of “the strict compliance with the sentences and other decisions made by international organizations in charge of promoting and guaranteeing human rights,” to be addressed as part of the 11 points to be developed. The plan is to propose a dialogue process including the Inter American Court of Human Rights, the Commission, regional civil society organizations and all regional parliaments. MUD also plans to present an agenda to fight arms build-up, organized crime and corruption in all member countries.

Latin American Parliament Commissions. With the Latin American Parliament Commissions defined, it is now known that pro-Chavez representatives will participate in eight of them, Political, Municipal and Integration Affairs (Roy Daza); Economic Affairs, Social Debt and Regional Development (Rodrigo Cabeza); Citizen Safety, Fight and Prevention against Drug Trafficking, Terrorism and Organized Crime (Walter Gavidia); Human Rights, Justice and Prison Policies (Roy Daza); Labor Affairs, Social Contingency and Legal Affairs (Roy Chaderton); Environment and Tourism (Ana Elisa Osorio); and Indigenous People (Dalia Yanez). MUD representatives will coordinate the commissions of Equal Opportunities for Both Genders, Children and Youth (Delsa Solórzano); Education, Culture, Science, Technology and Communication (José Ramón Sanchez); health (Francisco Garcia); Public Services and Defense of Users and Consumers (Henry Ramos Allup) and Agriculture, Stockbreeding and Fishing (Timoteo Zambrano).

Law of Emergency for Urban Lands and Housing proclaimed. During the act of definition of the United Socialist Party of Venezuela’s (PSUV) strategic lines for 2011 and 2012, President Chavez proclaimed the Law of Emergency for Urban Lands and Housing, which entitles the government to declare idle urban lands as public utility. He reiterated, “wherever there’s a facility, a warehouse, beer and junk stockrooms, junkyards, we will take action and use them to build homes for the people.” This Law of Lands was presented before the National Assembly (NA) in December of 2010, as a response to the emergency generated by the heavy precipitations. The draft approved in first discussion gave fiscal incentives to private companies for building homes. However, it increased the faculties of official entities to carry out occupations and control real estate prices.





Now, it is unknown whether it will be shorter. During his speech at the January 23 march, President Chavez said he was no longer sure he'd use his Empowering Law only until May. "They (the opposition) are not interested in making it shorter, that was my way of contributing with the dialogue, but since they're not interested then, why would I? There's no need to make it shorter. We'll see as we go," without specifying until when he was willing to use it.

Debt of agricultural producers pardoned. Within the framework of his Empowering Law, President Hugo Chavez pardoned the debts of national agricultural producers who lost their crops during the rains of late 2010. The debt was pardoned with both private and public banks.

National Assembly as a space for the people. The president of the National Assembly, Fernando Soto Rojas, said the entity needed to become a space to listen to the people's opinions and proposals, not only for elected representatives. He said this change was necessary to build socialism.

Banking system with more regulations. Official Gazette No. 39,597 of January 19, 2011 includes the new regulations imposed by the Superintendence of Banks to increase security and regulate electronic banking operations. The regulations specify that banks and financial institutions must inform their clients of the services offered and the responsibilities of using them, either in writing, through printed media or electronic media. They are also obligated to inform their clients about the procedures to affiliate, cancel, suspend and reactivate the electronic service, daily transaction limits, and commissions and fees to use the banking system. According to the Official Gazette, a category-2 authentication factor (one that includes the use of a password set by the client) is necessary to affiliate and disaffiliate electronic services; additionally, category 3, 4 and 5 authentication factors must also be established, providing the use of single-use dynamic passwords, certified electronic signatures duly issued by the client and user information derived from his biometric features, respectively. The banking system also needs to establish the top daily amounts for online transactions.

Especial Law of Suitable Shelters in effect. Through the Empowering Law, President Chavez proclaimed the Especial Law of Suitable Shelters, made official in OG No. 38,599 on Friday, January 21, 2011. The idea of this law is to turn shelters into protection centers that are adapted to the needs of the people affected by an emergency or a natural disaster. One of the main objectives is to transform the available shelters into spaces suitable for life and coexistence in community, in places where people's rights are protected. This law classifies shelters in five types and three levels, and refuges are to be labeled depending on the type of building and services available.



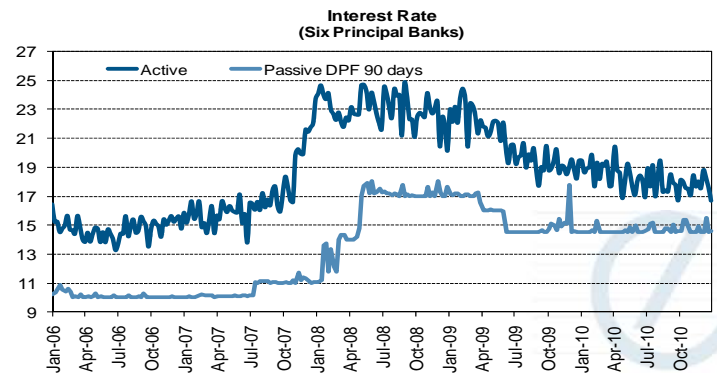
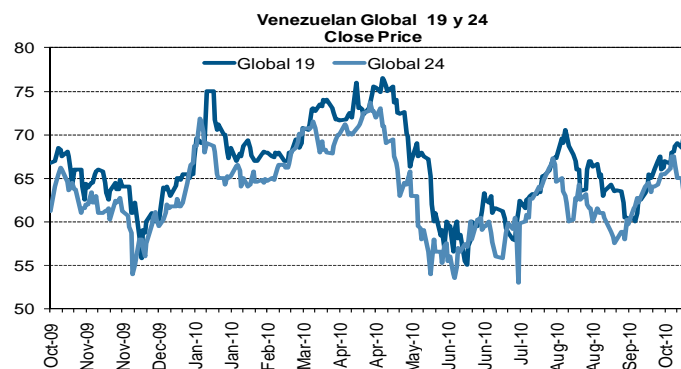
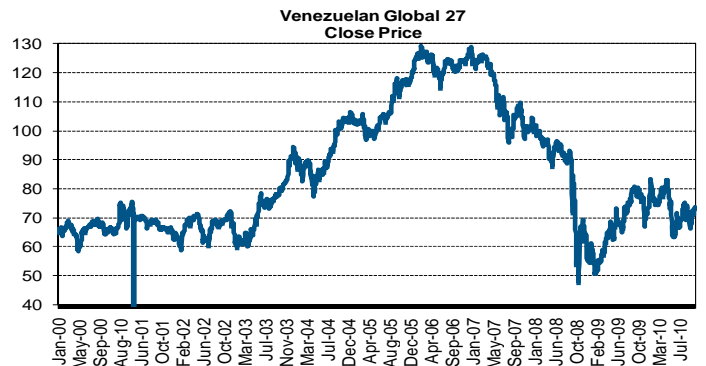
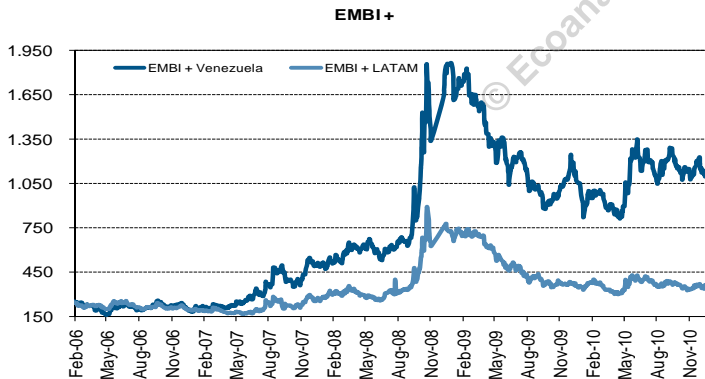
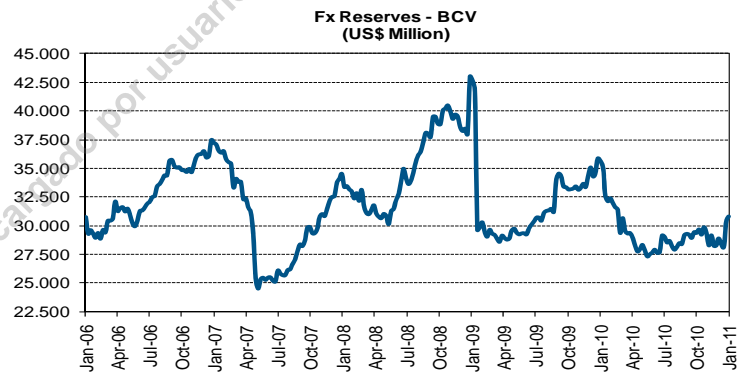
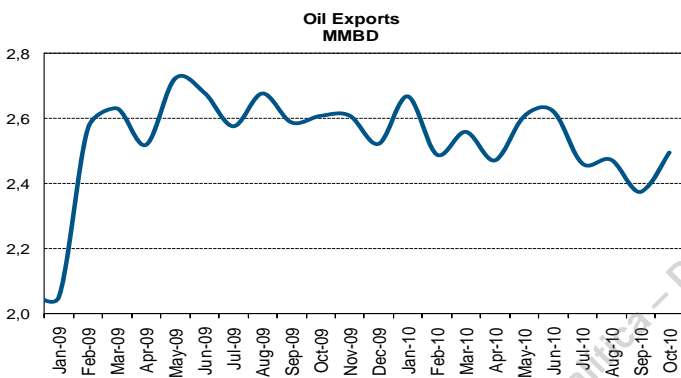
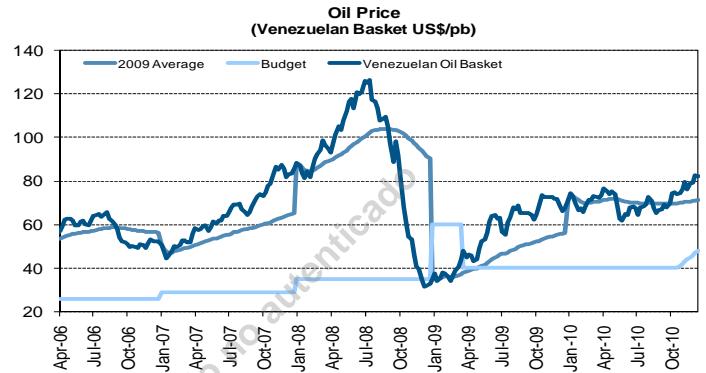
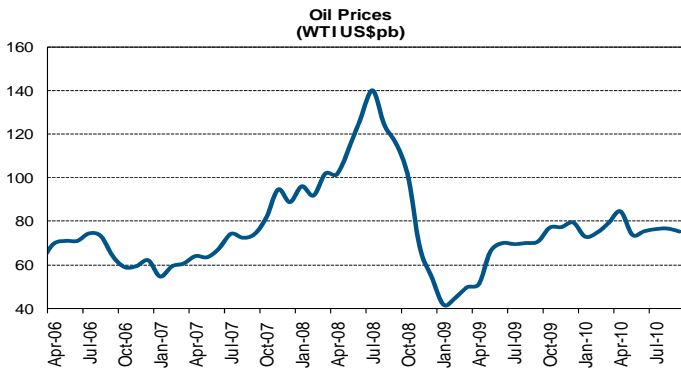
Regulation and directors ready. Official Gazette No. 39,600, published on January 24, 2011, establishes the regulation for the operations of the new Bicentennial Public Securities Exchange (BPVB). Alessandra Navarro Garcia was appointed as President of the BPVB and Anelkys de Castro Flores and William Lopez were named its main directors. The BPVB is attached to the Ministry of Planning and Finance and is located at Torre Europa in Campo Alegre.

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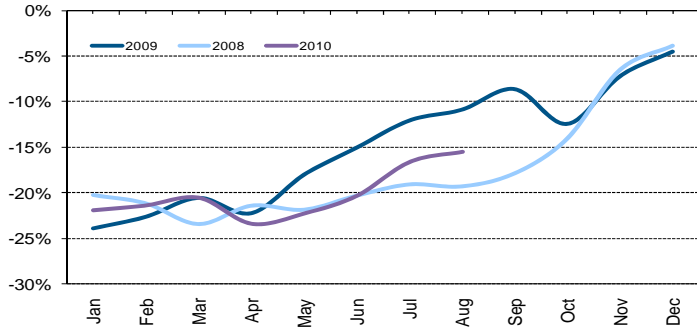


ECONOMIC OVERVIEW

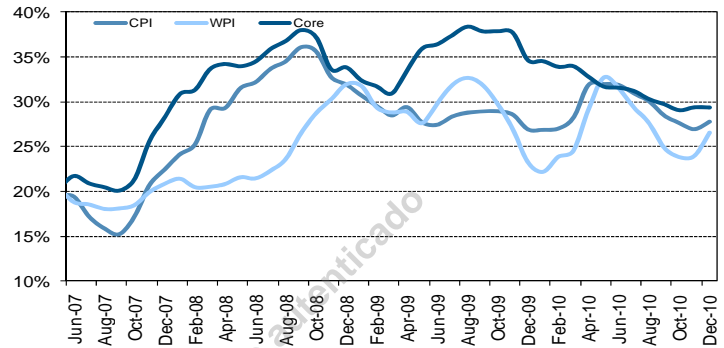




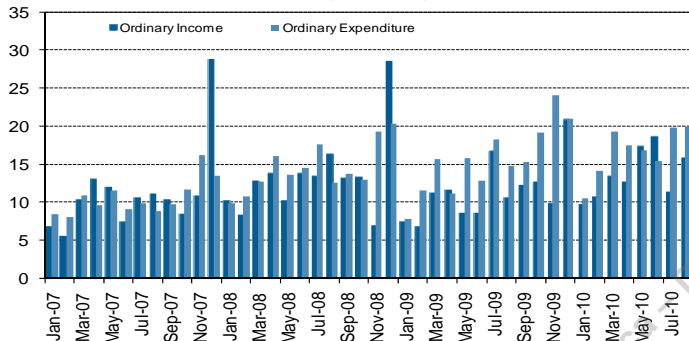
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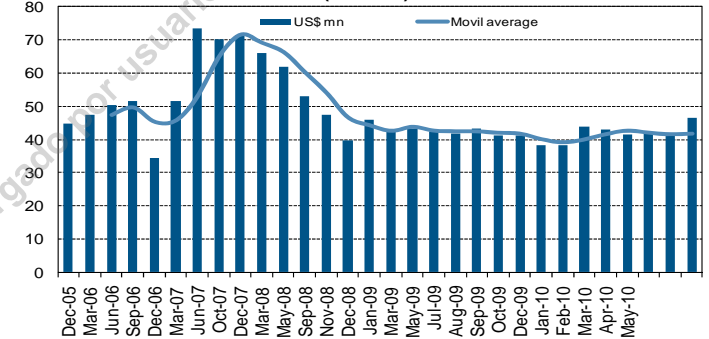
Inflation (Last 12 Months)



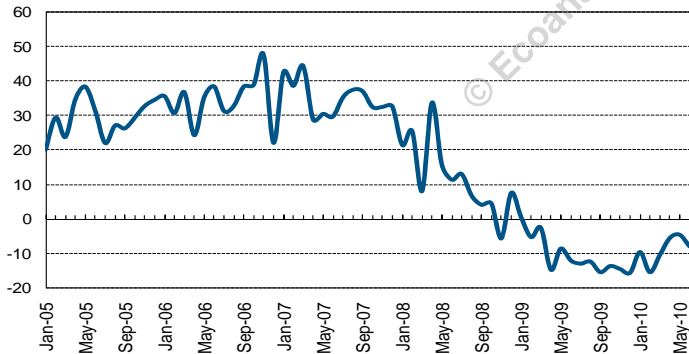
Central Government (VEB Billion)



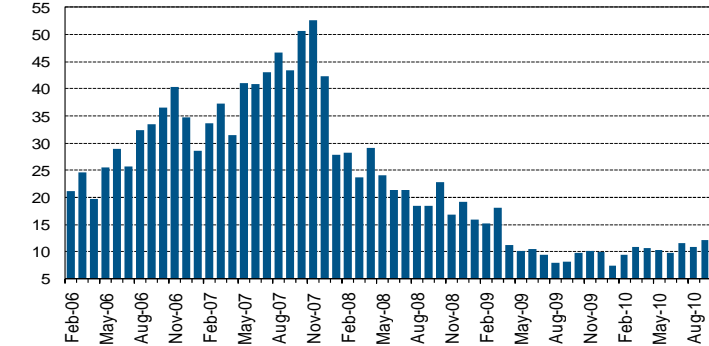
Resources of the State (US \$ MM)



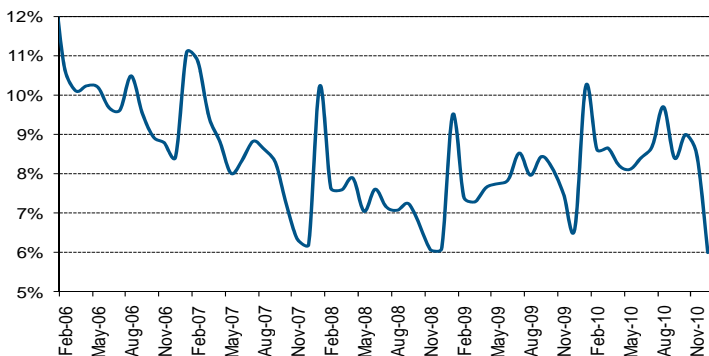
Volume of Sales (% Variation)



Sale of Vehicles (Thousands of Sold Units)



Rate of unemployment



Disbursement (US\$ Million)

