



Weekly Report

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***Exchange Control:
Main mechanism used by the
State to control the economy***

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Exchange controls have been in place in Venezuela since 2003. Back then, this not very orthodox but often used mechanism in the history of the Venezuelan economy, was implemented under conditions that one could say justified such a mechanism being introduced, albeit for a short time only.

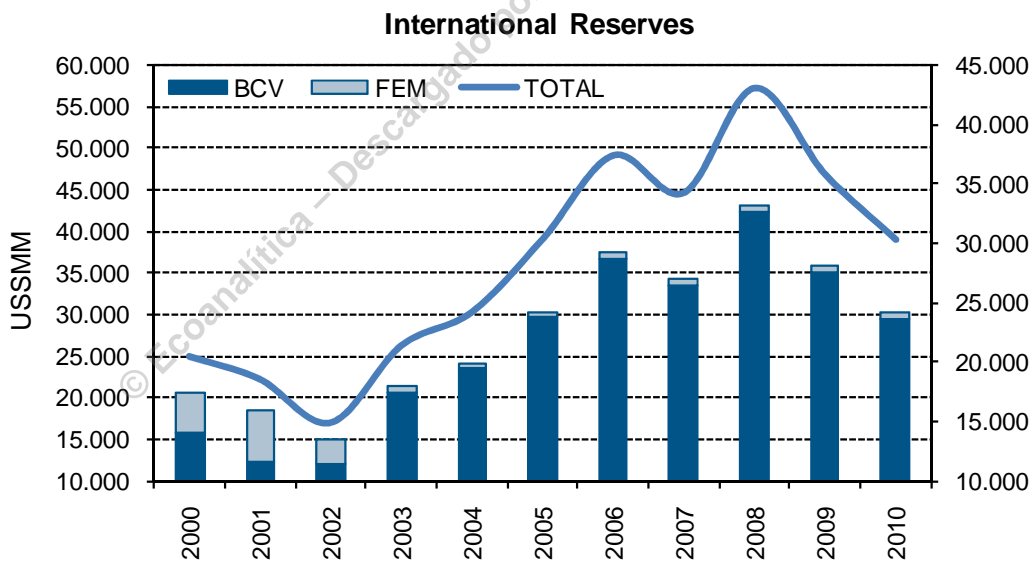
In other words, the significant amount of international reserves that were used during the Oil Strike (Dec/2001-Jan/2002) served to justify the use of such a controversial mechanism as an exchange control, but only for as long as it takes to solve the crisis which led to its implementation. And, if not for the Administration's political objective of introducing a socialist regimen (21st Century Socialism), this exchange control that is still in place would be totally uncalled for and a clear mistake. In other words, from the point of view of a capitalist economy, the Venezuelan exchange control is a complete mistake and damaging to the economy; but from the political point of view of an Administration implementing a socialist project, an exchange control is an excellent policy that will allow it to achieve one of its main



objectives: the continual increase in the power of the public sector and its control over the country's economy. This Report will look at how this control mechanism helps the Administration achieve its goals.

It was economically justified in 2003

Exchange controls, be they all encompassing, such as the CADIVI system, or partial controls, such as imports tariffs, export subsidies, product import quotas, or foreign investment quotas, as seen in other countries around the world; all these measures, to those who defend the ideals of a free market, are the worst ways to solve Balance of Payment problems, no matter how serious the situation may be. This is because the distortions that exchange controls create and the incentives to pervert the system are such that generally, the exchange control solution becomes a much larger and more serious problem than the original problem which led to its implementation. This is quite evident now, for those of us who live in Venezuela.



Sources: BCV and Ecoanalítica

* Petroleum strike in Venezuela

All control mechanisms imply a loss of freedom

Despite this fact, exchange controls exist in a number of countries around the world, used as an emergency measure to avoid Balance of Payments crises. This was the argument used to implement CADIVI back in 2003, and at the time this decision could be justified, though no economic argument can be made to justify the length of time this control mechanism has remained in place.





Since 2004, the exchange control is in place for purely political reasons

Once the crisis brought on by the Oil Strike was under control and international reserve levels were back to normal, the exchange control mechanism should have been dismantled. Back then, not only did international reserve levels return to normal, but oil prices were increasing steadily as the oil boom was beginning, and prices continued to increase, with the exception of an 8 month period when they dropped due to the worldwide financial crisis in during the second semester 2008. Currently, oil prices are on an increasing trend.

But, the Venezuelan exchange control mechanism is still in place because it is one of the Administration's best tools that help it implement its 21st socialist economic model; in other words, an economic model in which the public sector has almost complete control over the so-called "priority sectors" of the economy, a definition which is continually being modified to include more and more sector of the economy.

Another tool of the socialist plan

Through exchange controls, the Administration has the power to control, limit, and command the private sector, since it is the one that has the power to arbitrarily decide which companies receive foreign currency or not, how much they receive, and at what rate foreign currency will be purchased. This means that the Administration can restrict or promote the economic growth of the sectors it chooses.

As we have mentioned in the past, the plan is clearly laid out in the First Socialist Plan 2007-2013. It states that "the State will totally control all production activities of strategic value for the development of the country..." and social production companies and state-run companies will clearly be more predominant than private sector companies.

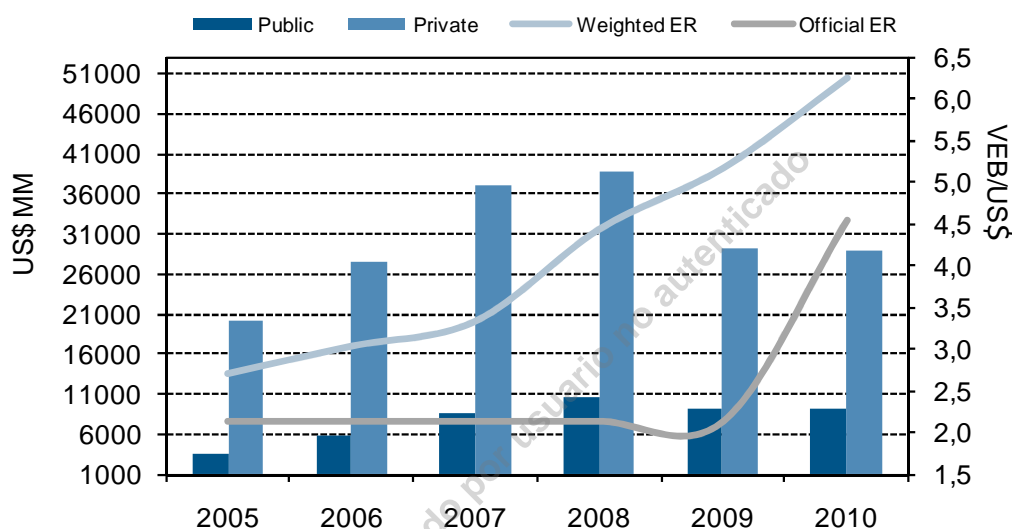
This doesn't sound as bad as "expropriations" but it leads to the same end

In order to achieve total control over production activities of strategic value the Administration doesn't have to expropriate everything, the exchange control mechanism is a powerful tool that can achieve the same end-result indirectly and without generating a lot of political fallout. The Administration doesn't only control which companies will get foreign currency, how much, and at what cost, but the public sector is also able to compete with the private sector with clear advantages in terms of access to foreign currency and exchange rates.





Imports Public Vs private and Official Exchange Rate Vs Weighted Exchange Rate



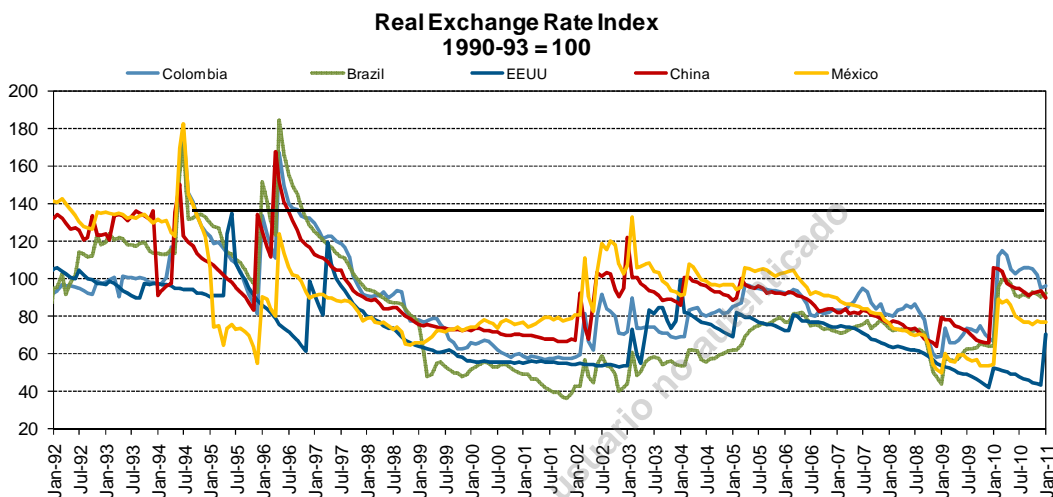
Sources: BCV and Ecoanalítica

While the rest of Latin America is worried about their currency appreciating, in Venezuela we're worried about another devaluation

With countries begin to recover from the worldwide finance crisis, in 2010, most Latin American economies (Brazil and Colombia) were worried about their country's currency appreciating and took measures accordingly, strengthening their currencies against the US-dollar. This move makes their economies less competitive by making their products more expensive for the rest of the world and making imports that compete with domestically produced goods cheaper.

But in Venezuela, where everything seems to work the other way around, we are worried about if there will be another devaluation of the currency, which makes our imports even more expensive. With respect to the appreciation of the currency, it's practically an irrelevant issue in Venezuela since the private sector that exports (most affected by appreciation) is only 5%.

It's the same case with domestic producers that compete with imports, the exchange rate has been so severely appreciated over such a long period that the number of domestic products that compete with imports is virtually non-existent. It's impossible to compete with imported products that receive 20.7% subsidy thanks to the overvaluation created by the exchange control mechanism (local currency overvaluation % compared to the real exchange rate).



Inflation

As the previous graph shows, with every devaluation there is an improvement in competitiveness, and sometimes, a very significant improvement, as was the case with the most recent devaluation and the elimination of the VEB2.6/US\$ “preferential” exchange rate. But this improvement is only temporary, because the devaluation also leads to domestic price increases at accelerated levels, much more than international level price increases, and what was gained in competitiveness deteriorates quickly.

A problem of cause and effect

It's important to point out that the devaluations don't cause inflation in Venezuela, rather the other way around, inflation in Venezuela makes it necessary to devalue the currency periodically, because a fixed rate would imply that a continual appreciation of the exchange rate which in turn makes it impossible to maintain a fixed rate.

A control that limits freedom

The exchange control in Venezuela restricts the freedom of the people, only allowing them to buy limited quantities of foreign goods and services, not allowing them to have a balanced portfolio of foreign and domestic assets if they so desire, or even to sell their goods in order to purchase foreign currency legally.

It re-distributed wealth in a regressive manner

Exchange controls have a very perverse effect in the re-distribution of the country's oil wealth. Those that know how to work the system and take advantage of the exchange distortions and increase their wealth; unfortunately, it's not the lower income bracket citizens that know how to take advantage of this. The poor don't usually have credit cards and/or bank



Political objectives take priority over social objectives

accounts (domestically and/or abroad) that will allow them to play the system, take advantage of CADIVI (or SITME), make Internet purchases. And even fewer people among the total population have bank accounts abroad that will let them take advantage of the foreign currency available through the SITME in order to invest in PDVSA or Republic bonds. In conclusion, despite the fact that the Administration is from the Left and heralds the importance of the re-distribution of the country's wealth in an equal manner for all; that opportunities must be created for the poor (which we don't deny they have done), the Administration's political objective is to dominate the economy and this seems to be more important than their social equality objective.

It doesn't cost anything to dream

This issue could be taken up using valid quantitative measure, such as the Gini Coefficient Index, which does point to wealth being re-distributed more equally during the Chávez Administration, but, imagine what the re-distribution of wealth would have been like if the country would have taken advantage of the oil boom with solid market economy policies? We can only guess at the answer. But it is very likely that economic growth would have been greater which would imply greater social wellbeing on all levels, and a more equal distribution of wealth. Even in the worst case scenario, the poor would have received more wealth, albeit not in an equal manner.





Economic Tips

Inflation in imported goods takes off. The devaluation of the currency is beginning to be felt in the wholesale price of imported products, which in January rose by 4.1%, the highest for the first month of the year since 2003. The reason behind the price increase of imported goods is mainly the devaluation announced in the beginning of the year, which raised the exchange rate for the purchase of basic goods from VEB/US\$2.6 to VEB/US\$4.30.

Operational reserves of BCV are at US\$ 9.2 billion. The balance of the Central Bank of Venezuela at the close of 2010 shows that the liquid portion of international reserves, or the Dollars in bank accounts or instruments that are immediately available to cover imports and debt payments, are US\$ 9.2 billion.

The cost of the food basket is already double the minimum wage. According to the Center for Documentation and Analysis for Workers (Centro de Documentación y Análisis para los Trabajadores - Cenda), in January, the food basket for a five member family costs VEB 2,535.5, while the minimum wage is VEB 1,223.9. This value for the food basket in January also showed an inter-monthly increase of 1.7% with respect to December.

The adjustment of the tax unit will be less than 2.7%. The President of the Finance Commission of the National Assembly, Ricardo Sanguino, said that the adjustment of the tax unit, which is presently at 65 Bolívares, will not match the inflation of 2010, or 27.2%. The National Integrated Service of Tax Administration (Servicio Nacional Integrado de Administración Tributaria - Seniat), presented the report with the tax unit increase to the Parliament, which will be reviewed in the next 15 days. The member of the Assembly only said that it won't be pegged to inflation.

Pdvsa's exchange losses affected its income tax contribution. The financial administration of Petróleos de Venezuela during 2010 affected the contributions of the oil industry to the national treasury. Pdvsa's financial report reveals that during the nine month period between January and September, 2010, the advanced payment of income tax dropped US\$3.2 billion "as a result of the increase in the exchange rate in force" for the operations of the industry with the Central Bank of Venezuela, which Pdvsa tallied as losses in its accounting books.

High demand for petrobonds evidences a shortage of foreign currency. In March of last year, the Ministry of Finance eliminated the exchange mechanism that allowed



the free purchase of Dollars through stock brokers and since then, the market is facing a strong drought of foreign currency. Pdvsa didn't meet the expectations, and only assigned US\$3,000 to companies and individuals.

Government uses BCV resources to finance expenses. If there ever was an institution that defended its autonomy and its role as guarantor, it was the Central Bank of Venezuela. However, the reform of its guiding legal instrument and the changes in its Board of Directors were enough for the Administration to legalize the transfer of international reserves and short term loans. Article 113 of the legal instrument established that the Central Bank will have to make the transfers within 15 days of the end of the semester.

Central Bank releases Financial Statements at the end of 2010. Through *Gazette N° 39.614*, dated 11, February 2011, the Central Bank of Venezuela published its comparative general balance, comparative results, and changes in capital accounts, accompanied with its corresponding notes.

Government uses the resources of BCV to finance expenditures. Transfers of international reserves to the National Development Fund amount to 38.8 billion Dollars from 2005 to the present. These reserves come from the oil sales of Petróleos de Venezuela, which the entity pays in Bolívares, and when they are deposited, they guarantee those Bolívares. When these reserves are removed, without the Treasury paying the BCV its equivalent in Bolívares, the equity of the entity is affected.

...the greatest inconvenience that BCV authorities face is that by allowing the transfer of reserves, it cannot design an anti-inflationary monetary policy. To provide resources to the Government, for it to spend it through Fonden is to have more money circulating, which incentivizes the demand of goods and services, and pushes prices higher.

Vices denounced in assignment of Pdvsa's bonds to companies. For the issue of this bond, the state-owned oil company invited "mainly companies in the food, health, machinery, equipment, and oil sectors". However, according to Juan Socías, President of Grupo Soluciones, companies with only one import in these areas made their application, as if they belonged to a "priority sector".

Government tries to reduce gasoline consumption. The government is preparing a campaign to promote the rational use of gasoline in the country, not only to avoid waste, but to stimulate consumers to use the right octane number for their vehicles, as was gathered extra officially. Rafael Ramírez, Minister of Oil and Energy and President of Pdvsa, said on Sunday in the program "Aló Presidente" that the State is losing US\$1.5 billion per year through subsidies to fuel, making it the cheapest in the world.



Interest rate. The lending rate for the second week in February was at 18.2%, up by 0.8 perceptual points compared to the previous week. Time deposits and savings rates were steady at 14.9% and 12.6%, respectively.

International reserves. International reserves decreased 0.5% going from US\$29.35 billion during the first week in February to US\$29.22 billion during the second week of February. Compared to the same period last year, international reserves have dropped by 6.4%.

Monetary liquidity. Monetary liquidity for the first week in February was up 0.4%, compared to the previous week settling at VEF 292.2 billion. The M2 has increased 26.5% year-on-year.

Sitme figures. To date, US\$5.97 billion have been negotiated through the Integrated System for Foreign Currency Transactions (Sitme), averaging US\$34.5 million a day, with an implicit exchange rate of VEF 5.3/US\$. Last week the traded amount reached US\$171 million, US\$24.6 million more than last week when braided US\$146.4 million.

Oil Tips

First place. As published by the Ministry of Energy and Oil, Venezuela is the country with the greatest oil reserves in the planet, after adding 86.4 billion barrels, and placing proven reserves at 296.5 billion barrels. The composition of reserves is divided into 242.4 billion barrels in Traditional Areas and Off Shore; and 86.16 billion barrels in the Orinoco Oil Belt. The update took into account traditional areas in the Barcelona, Maracaibo, Maturín, Barinas, and Cumana jurisdictions, as well as the condensate off shore, Cardón IV, Campo Perla, in the state of Falcón; and in the Orinoco Oil Belt, the Boyacá 3, Boyacá 4, Boyacá 6, Boyacá 7 and Boyacá 8 blocks, Parque Aguaro Guariquito, Ayacucho 1 and Ayacucho 8, Junín 6, Junín 7, Junín 8, Junín 9, the mixed companies Petroindependencia, Petrocarabobo, Petrocedeño, Petropiar, Sinovensa, and the block operated by Pdvsa, known previously as Bitor.

Income Tax Payments dropped. The national treasury received US\$3.2 billion less from Petr6leos de Venezuela (Pdvsa), from income tax (ISLR) during the first nine months of 2009, compared to the same period in 2009 (*sic*). This drop is caused by the increase in the official exchange rate, which the oil company counted as losses in its balance sheet.



Debts with Pdvsa. At the end of 2010, several public entities have debts with Pdvsa, among them Pequiven, Cadafe, Corpoelec and the Banco de Desarrollo Económico y Social (Bandes) of the Nation, which owe a total of US\$2.2 billion. Pequiven's debt reaches US\$330 million and dates to 2009. Cadafe's debt reaches US\$25 million and is related to the absorption of the National Electric Corporation. Corpoelec's debt is US\$1.3 billion, and corresponds to investments. Finally, Bandes' debt of US\$581 million, is associated to the financing fund signed between the governments of China and Venezuela, paid with shipments of crude and by-products by the state oil company.

Dispatches to the US recover. Throughout this year and the last quarter of 2010, exports to the United States (USA) had dropped. However, in the last four weeks they have been recovering, and exports to North America are on average 1.0 million barrels per day. This number was boosted by the last record of 1.1 million barrels per day during the week of January 31 to February 4. It is the first time since the week of August 9 to 13, 2010 that the shipment record to the US is over a million barrels, which was at that time 1.1 million barrels per day. Since that date, the average was around 960 thousand and 865 thousand barrels per day.

Accidents continue in Pdvsa. At the Tía Juana oil field, in the Simón Bolívar municipality of the State of Zulia, there was a fire caused by a crude oil spill in one of the distribution lines of the complex. The details of the accident are still not known, but it has been controlled.

The figure is unbelievable and so is the excuse. Rafael Ramírez, President of Pdvsa, said that the gasoline subsidy is close to US\$1.5 billion per year, which means a loss for the state oil company. Ramírez said that gasoline subsidies are around 90,0% of the price that it should have to cover costs. These statements were given during the program "Aló Presidente", on Sunday, February 13. President Chávez in turn noted that in 12 years of government, the price of gasoline has never increased, a measure implemented to counteract inflation and protect the people from speculation. He also said that "we must be clear where we are heading to. Our goal is to reduce gasoline consumption and replace it with natural gas for vehicles". What is not credible is the fact that the decision was made to control inflation, if the government doesn't implement other measures with greater and deeper incidence, to reduce inflation in Venezuela, which is above the average in Latin America.

Pdvsa will buy new ships. Pdvsa announced that it obtained financing with Japanese companies to acquire four Aframax ships, with an approximate capacity of 104.000 dead weight tons (draft 15 meters, breadth 45 meters, and length 250 meters). The Japanese companies Itochu and Mitsubishi are involved in the purchase of these



ships. In total, Venezuela would be buying 14 ships, since in September 2010 the purchase of 10 ships of the same type was announced, for US\$700 million, to a shipyard in Russia. The South Korean company Daewoo, will cooperate in the construction of the ships.

Pdvsa acquired Sucegas. The public sector acquired the private liquefied gas company Sucegas, through Pdvsa Gas Comunal. This company was in charge of distributing liquefied petroleum gas in Cagua, Magdaleno, Belén, Turmero and Villa de Cura, to improve domestic gas service in the State of Aragua. With this acquisition, the operations of the company will resume, which were almost paralyzed due to lack of investment. This had deteriorated the facilities and reduced plant production by 50.0%. Pdvsa Gas Comunal assumes the responsibility of strengthening the supply of gas cylinders to more than 33.000 families of the area, by adding new cylinders to the cylinder yard, and trucks to make the proper distribution to the established sales routes.

International oil baskets. At the close of the New York market last Thursday, February 17, the WTI was at US\$86.1/bl, showing a 2.0% decrease compared to the US\$87.8/bl of the previous Thursday. The Brent increased by 0.6% to reach US\$102.9/bl, compared to US\$102.3/bl of the previous Thursday.

Local oil basket price. The Venezuelan oil basket price decreased last week, to close at US\$85.6/bl on Friday, February 11, up by 2.2% from the US\$87.6/bl registered the previous week. Meanwhile, the basket's annual average is at US\$85.8/bl.

Business Sector Tips

Trade balance with the US closed in 2010 at US\$22.1 billion. Trade exchanges between Venezuela and the United States ended last year at US\$ 22.1 billion, an increase of 18% with respect to 2009, according to a press release sent by the Venezuelan-American Chamber of Commerce and Industry (Cámara Venezolano Americana de Comercio e Industria - Venamcham).

Investments in telecommunications increased 8.7% in 2010. The National Telecommunications Commission informed that last year, the companies in the telecommunications sector invested 8.7% more than in 2009. According to a report from the entity, in 2010 investments in the area totaled VEB 3.68 billion, while in 2009 they were VEB 3.23 billion.



Conatel sets reference prices for interconnection charges for mobile telephone services. Through Official Gazette No 39.615, of February 14, 2011, the National Telecommunications Council set the reference price or value to determine interconnection charges for mobile telephone services. They were set at: VEB/Second 0.0031485 (from 2010 to June 2011) and at BsF/Second 0.0027 (starting on July de 2011) for interconnection charges, mobile phones. While interconnection charges, mobile phones, for calls originated in public terminals were established at VEB/Second 0.0023 (from 2010 to June 2011) and VEB/Second 0.0021 starting on July 2011).

Income of telecommunications companies increased 21% in one year. As stated in the last report of Conatel, the companies operating in the telecommunications sector had a 21% increase in income in 2010 compared to 2009, at VEB 33.81 billion. Between October and December, the income was Bs.F. 9.47 billion, 56% of which corresponds to mobile telephony. The institution also reported an increase in service penetration of 3.15% in fixed telephony; 0.87% in mobile telephony; 16.1% in Internet; and 15.2% in paid TV.

Cellular telephony can still grow. The difficulties to obtain foreign currency to import terminals affected the performance of mobile telephony between October and December 2010. According to the National Telecommunications Commission, the number of active users of this service decreased 0.87% during that period, compared to the same period the year before. Mobile telephony in Venezuela has a penetration of 96.70%, according to the report, which means that 97 out of 100 people have a cell phoner.

34% of broad band subscribers use mobile Internet services. More and more Venezuelans are using mobile internet services. The entry of cell pone companies in this business (offering USB modems that allow wireless internet connection) could explain the surge of this service in the country. Conatel informed that of the group of people subscribed to broad band, 65.8% uses the fixed service, while 34% connects through a mobile platform.

Used industrial capacity was 70.2% in 2010. Elías Eljuri, president of the National Institute of Statistics (Instituto Nacional de Estadística - INE) said in a press release that the used capacity of the industries was 70.2% at the end of the fourth quarter of last year. The data recorded during the quarter with the highest production, before the Christmas season, represents an increase of 0.39 points compared to 69.81% during July and September of the same year.





The Administration freezes the price of all medications. Through a letter sent on January 13 to the different chambers in the pharmaceutical sector, the authorities notified about the decision to prohibit any adjustment in the price of all medications, after the devaluation of the currency.

In 12 years, the government built 284.000 houses. Hugo Chávez, President of the Republic, re-launched in his customary Sunday program a “misión” related to housing, saying that within seven years, they will build 2 million housing units. However, in 12 years, he already launched two “misiones” and the result was 284.000 units.

Occupation announcements are seen with concern by the real estate sector. The real estate sector is reviewing the measures under analysis by District Attorney Luisa Ortega Díaz, to occupy goods in the hands of construction companies accused of fraud. However, real estate entities state that the Attorney General’s Office is making decisions before there is even a sentence. The intention of the District Attorney’s Office is to enforce the Law against Organized Crime, and order the temporary occupation of the assets of construction companies.

The goods of the construction companies to be taken are being evaluated. 42 people have been detained for being allegedly linked to real estate fraud, as indicated by Luisa Ortega Díaz, Attorney General of the Republic. Now, the goods to be occupied, property of these companies are under scrutiny.

Only 11% houses to be built through international agreements were finished. The government signed international agreements between 2005 and 2007 to build houses in eight states. Six years later, the units are not finished. The companies in charge of the projects have only finished 11% of the programmed housing solutions.

Purchase-sale transactions of apartments in the metropolitan area of Caracas dropped 48%, while the price of housing units increased 28%. According to statements by Martín Fernández, director of the company “TIR Inmobiliarios”, since 2008 the number of operations has decreased, and since 2010 the greatest drop was in the primary market, or around 25% of the sector’s operations.

The expropriation law was replaced by another one. For the construction and real estate sectors, the Emergency Law for Urban Land and Housing, in force since January 29, is replacing the expropriation Law. The Legal consultant for the Real Estate Chamber of Venezuela, Irma Lovera, said that the government has not reformed the Expropriation Law, because it gets around it through other legal means. Also, the new legal framework of the housing sector violates municipal orders regarding the use of idle urban land.





The construction of 150,000 housing units is considered unviable. The official goal to build 150,000 housing solutions in 2011 is “unviable” without the participation of all actors, according to Aquiles Martini, President of the Real Estate Chamber of Venezuela. He said that if there is no clear dialog between the banking sector, the government, lawmakers, real estate promoters, and urbanists to develop a viable plan that is really feasible, it won't be possible to build 150,000 housing solutions.

Public sector depends on salary adjustments by decree. The greatest increases in the public sector in 2010 were for workers with low salaries, those that depend the most of minimum wage adjustments, which is approved by decree, by the Administration every year.

A drop in production increases the price of food. Many plans have been designed to stimulate the agricultural sector, but few have been really effective. In the past few years, agriculture has lost impetus, and has decayed, falling in a deep recession as a result of several factors, among them the controls and policies applied to this sector.

Alcasa lost US\$1.8 billion due to labor conflict. At CVG Alcasa there has been no truce and after 17 days with minimum operations, the Board of Directors of the aluminum company has started evaluating the consequences. According to statements of the president of CVG Alcasa, Elio Sayago, the stop in operations has delayed the rolling of 600 tons of primary aluminum, which translates into US\$1.8 billion lost.

Production decreases worries industrials in Guayana. Since 2009, the alarms of the industrial sector of Guayana have been turned on. With the loss in production at the basic industries, which has worsened in the last two years, the small and medium industries that provide services and products have experienced a reduction in contracts, as well as insolvency due to financial limitations.

Socialist workers demand the approval of the Organic Labor Law (LOT). Socialist workers demonstrated last Friday to present to the President of the National Assembly (AN), Fernando Soto Rojas, a document with urgent requests from the working class.

Intervention of four mercantile societies is ordered. The banking superintendence ordered the intervention of four mercantile societies through resolutions published in *Official Gazette N° 39.614*. The companies are: “Inversiones Algora 54, C.A”; “Inversiones MM 5.000, S.A”; “Elsa Parette de Venezuela”, C.A. and “Celtek Comunicaciones de Venezuela, C.A”. and had links to other companies that



had already been intervened. Sudeban also ordered the liquidation of “Inversiones 171777 C.A.” and of the company “Inversiones Maragal, C.A.”.

Sudeban liquidates the investment company “Dolomita C.A.” The superintendence of institutions in the banking sector (Sudeban) ordered through *Official Gazette N° 39.615* of February 14, 2011 the liquidation of the investment company “Dolomita C.A”, a company related to the Financial Group “Cavendes”. According to the resolution, the liquidating entity is the Social Protection Fund for Bank Deposits (Fondo de Protección Social de los Depósitos Bancarios - Fogade).

..Sudeban also ordered the intervention of (1) Editorial EDC C.A., (2) Inversiones Sisalud C.A., (3) Consorcio Inversionista Bancanarias C.A. and (4) Oficina Técnica Rocil C.A.

Six million VEB lost due to protests at Venalum. During the five-day strike, CVG Venalum has not been able to dispatch aluminum to national clients, since the trade union leaders ordered the closing of the main gates, and operations are at a critical level because there is not enough staff to perform maintenance and regular processes. Every day, the production loss is 275 metric tons of primary aluminum.

The thermoelectric Planta Centro is operating with only one of its five units. The operational problems of the thermoelectric plant continue; only one unit of the plant, which is a key element to generate electricity for the central region of the country, is operational, a situation that has lasted four weeks. It isn't known how long the repairs will take.

Unit 16 at Guri is out of service. Unit 16 of the hydroelectric plant at Guri, the main source of electric power of the country, is temporarily out of service since this weekend, adding to the five units that are presently unavailable. The cause is that one of the seals (gaskets) is broken. Because of this failure, the service is not providing 630 megawatts (Mw) to the National Interconnected System (Sistema Interconectado Nacional - SIN), so it will be necessary “to ration around 1,100 Mw in the country”.

Coca-Cola Femsa Plant in Valencia resumes operations normally. After reaching an agreement, the parties involved signed a collective bargaining agreement, which was taken into consideration by the company. According to Rodrigo Anzola, Legal and Corporate Affairs Director of the bottling company, it is “*a very important step to reaffirm the commitment of Coca-Cola Femsa with its workers in the country, and achieve the goal of constantly improving the conditions of wage earners*”.



The first vital areas to build housing solutions in the country were decreed. On February 15, the first Vital Areas for Housing and Residence (Áreas Vitales de Vivienda y de Residencia - Avivir) were decreed through Official Gazette N° 39.615, destined to build housing complexes in the country. This decree follows the mandate of the President of the Republic, Hugo Chávez and is contemplated in the Organic Emergency Law for Land and Housing, which has the purpose of creating incentives and special conditions for the selected areas, to solve the housing crisis caused by the rains.

Shortages in the construction sector worsen. The situation of the main construction materials in the country is getting worse since last year, and is now critical, since there is a marked shortage and the prices have increased dramatically, as stated by Octavio Campos, President of the Construction Trade Union (Fetraconstrucción).

World Economy Tips

US citizens more confident. The improving labor market along with the low prices, seem to be boosting consumers' spirit. Mid-February readings of the University of Michigan's Consumer Confidence Index reached 75.1, recovering from the non-adjusted decline reported in January, 74.2. The number was close to its peak level reported in June. The latest reading almost matched consensus expectations of 75.0. Over the last ten years there has been a 60% correlation between the confidence level and the three-month growth in real consumption spending, so consumption could improve even more than expected.

European Industrial Production recovering. The largest economies of the euro zone (Germany, France, Italy and Spain) and the United Kingdom showed positive results in industrial production last December. Even though growth rates show a deceleration over the last semester, quarterly growth rates are back where they were a year ago, except for Germany which is still the strongest of the largest European economies showing q/q increases by 8.5%.

Meanwhile, still behind in terms of growth. The European monetary Union (EMU) reported a q/q seasonally adjusted annual growth rate (SAAR) of 1.2% in the fourth quarter of 2010. The countries with the best growth rates were Holland (2.3%), Germany (1.5%) and France (1.4%), while other countries, such as Greece, still



display negative rates (-5.6%) although with some deceleration compared to the third quarter (-6.6%). Italy reported a slight growth (0.2%). These results indicate a y/y growth by 2.0% for the EMU, led by Germany (4.0%), Holland (2.1%) and France (1.5%). Comparing these results with countries such as the United Kingdom (1.6%), the United States (2.8%) and Japan (2.6%), we can see how Europe continues to fight for getting its economy to take off, a task that seems to get harder and harder, especially within a context of high commodity prices, affected members (Greece, Spain, Portugal) and a global economy increasingly depending on the emerging markets.

China's trade balance decelerates. China reported a commercial surplus by US\$6.5 billion in January, a reduction by US\$6.6 billion compared to December of 2010 and by US\$7.7 billion compared to January of the same year. The decrease was a result of a 2.2% contraction of exports, which reached US\$150.7 billion and a 2.3% increase of imports which reported US\$144.3 billion. The increase in Exports to the European Union is perceived to harm the other areas the Asian giant exports; while the increase in imports is mainly perceived in commodities. However, it is necessary to point out that the early-year data look affected not only by seasonal factors, but also by the Chinese New Year (an effect felt before, during and after the event). This year, the Chinese New year started on February 2, and that may have had an impact on January's data.

OECD Leading indicators predict growth. The Organization for Economic Cooperation and Development's leading indicators as of December of 2010 show positive m/m signs. In the case of Japan, the positive result is encouraging after the fall of its GDP reported in 4Q2010. Beyond the metrics of leading indicators, the normal economic data suggests that the transition towards a sustained growth seems to be in motion. Even though the situation in Egypt and the Middle East, the still unresolved debt problems in Europe, the deceleration in China and the increase in the prices of commodities represent certain challenges to continuous expansion, overall, the data are still ahead and pointing towards growth. As of December, we can see that the different measures are being effective and show accelerations above the data reported in November. To summarize, OECD's data are consonant with a long-lasting expansion, but these indicators do not predict a solid direction right now.

Commodity prices: precursors of inflation or real growth? Over the last few months there has been a continuous increase in the prices of commodities overall, not only in the price of gold. It is then valid to wonder whether this will suggest higher prices for finished products (inflation). The answer is yes. Over the last ten years there has been a high correlation (64%) between the y/y variation in industrial commodity prices and the consumer price index of goods, despite the different costs of production, manufacturing, packaging, transportation and retail sale of each good.



However, with the indicator of industrial activity, the prices of commodities have a 78% correlation, so, the higher commodity prices are being supported by the recently gained strength of industrial production. On the other hand, this strength could also support the high prices of finished products, but thus far this correlation has been interrupted.

Political Tips

Chavez: “the biggest consensus possible.” President Hugo Chavez branded as “positive” the appearances of Venezuelan executive cabinet ministers in the National Assembly. He assured that his call to dialogue was *“authentic and we have proven it, we want to play the game of politics, and I said it in the National Assembly.”* He said it was important to “achieve the biggest national consensus possible.”

Capriles: homes owned by people, not the State. During an act to hand out 34 certified documents to acquire homes to residents of the Plaza municipality in Guarenas, the governor of Miranda, Henrique Capriles Radonski, specified that the homes “belonged to the people, not to the State.” “You are the owners, not the State, because otherwise it would be blackmail.” In light of the construction crisis, he demanded the national government to call all sectors in order to find a global solution.

Opposition in a good streak. According to the Venezuelan Institute of Data Analysis (Ivad), 6 out of every 10 citizens have a positive opinion of the opposition’s performance for the nation’s wellbeing and 45.4% are convinced that there’s an alternative national project to Hugo Chavez. Regarding the end of the presidential period, 58% of citizens don’t want Chavez to continue after 2012. 13.5% hope he steps out of office before the presidential election, 17.3% want the president to stay until 2018 and 20% hope he rules “beyond 2018.” As of today, 44.2% think it is possible for Chavez to lose the election in 2012, while 8.3% declines to consider this possibility. According to Ivad, 71.5% of citizens think Chavez’s opposing candidate should be elected in primary elections. Only 7.8% believe in the formula of consensus. 58% of citizens claim they will vote in opposition primary elections.

Who will be the adversary? In the latest Ivad survey, the first option to replace Chavez was Miranda’s governor, Henrique Capriles Radonski (16.5%), with double the preference of Manuel Rosales, Pablo Perez and Leopoldo Lopez. Assessing the presidential expectations in polarized scenarios, the following results were obtained:



Chavez: 46.3% Vs. Leopoldo Lopez: 39.9%; Chavez 46.4% vs. Pablo Perez: 37.4%; Chavez: 45.3% Vs. Capriles Radonski: 41.9%. In these polarized scenarios, the number of undecided went up to 16.3% with the presence of the Governor of Zulia; it went down to 13.9% with Leopoldo Lopez and to 12.9% with the Governor of Miranda.

The high crime rate is the main course. According to the latest survey carried out by the Institute Ibad between January 20 and 30 of 2011, 74% of Venezuelans think the measures adopted by the National Administration to control crime are “little” or “not at all” effective. The crime rate (in spontaneous answer) is still the main issue for 86% of citizens, while 42% think it’s unemployment and 20% believe it’s the lack of housing. Even though the crime rate is the main issue, according to the majority, the appointment of responsibilities is still diverse. In spontaneous answer, 30% of the people think the Government is responsible, 25.4% blame it on the “loss of values,” 12% blame the President and 7.5% the law enforcement agencies.

The nation is in a bad situation and we reject expropriations. When judging the nation’s situation, 52.5% of citizens have a negative perception; of those, 28.2% think it is fair to bad, 15.6% think it is bad and 14.5% think it is “very bad.” 59.5% of Venezuelans think private property is threatened, only 30% agree with the expropriations ordered by the National Administration. Moreover, Chavez’s “communal property” proposal is only approved – the number hasn’t changed significantly since 2007- by only 34.3% of the people.

Yes to Communal Councils and we believe in the decentralization. A proposal that did receive the people’s acceptance was the creation of Communal Councils, entities approved by 66% of Venezuelans. However, 56.2% disagree with having part of the faculties of State and Municipal Governments transferred to the Communal Power, as proposed in the Draft of Transfer of Faculties the Head of State has yet to define whether will be promulgated as an Executive Order Law through his Special Powers Law.

Regarding the Special Powers Law... Regarding Chavez’s special powers to rule by executive order, even though there is a balance between those who think this law was necessary to take care of the emergency generated by the rains and those who disagree with this notion, most Venezuelans (44.6%) are convinced that this attribution was granted to the president in order to take away some power from the new National Assembly.

Block request on Venezuela. Republican Representative Connie Mack, very critical of President Hugo Chavez, once again yesterday asked the US Government to include Caracas in the list of terrorism sponsors and proposed a full block on the country.



Mack also proposed that USA increased the oil supply from Canada, one of its main suppliers along with Saudi Arabia, in order to depend even less on exports from Caracas.

Students' hunger strike continues. All 13 students in hunger strike for the last two weeks demanding *"freedom to political prisoners"* warned they would maintain their protest until *"the last consequences,"* and urged the Secretary of OAS, Jose Miguel Insulza, to be *"more forceful"* against the government of Hugo Chávez. Insulza asked the young students to cease from their protest, but the strikers warned they were *"willing to give their lives for the political prisoners. We'll be here until the end, until the last consequences, we're not afraid to die,"* they said.

Legislative Tips

First fistfight... After the intervention of Representative Alfredo Ramos for the Democratic Unity table (MUD) and before Rep. Oswaldo Vera of Psuv took the floor, there was a struggle between pro-government and opposition congressmen as Representative Alfonso Marquina asked not to cut the audio of Rep. Ramos. During his floor time, Ramos, on behalf of MUD, proposed a general wage and salary raise before May 1, and granting the benefit of food stamps to retired seniors, and the negotiation of several expired collective labor agreements. According to Ismael Garcia, Representative for Podemos, Henry Ventura *"rushed towards Marquina and unfortunately the rumpus started."* The session was momentarily interrupted and was resumed once the board of directors of the National Assembly urged both congressmen to return to their seats.

Journalists in the National Assembly. The president of the National Assembly, Fernando Soto Rojas, said that journalists and media representatives were welcome to move around the Legislative Palace, *"but during a session, we need to work"* and journalists can not participate within the chamber. This came as a response to a consultation regarding the measure that keeps social communicators from walking in the Legislative Palace's patio. *"We have given them a comfortable room where they can take care of people."*

Refuse to participate. Opposition and MUD representatives refused to attend the National Assembly session called for last Tuesday in Ciudad Bolívar to commemorate the Congress of angostura. The reason for their denial was the appointment of



General in Chief, Henry Rangel Silva as main speaker. As stated by Omar Barboza, their denial *“doesn’t mean we’re going to abandon our labor in the National Assembly.”* In a press conference, he regretted the appointment of Rangel Silva as main speaker after his statements given last year assuring the Armed Forces were married to the Venezuelan Government. He said *“there’s a difference between political militaries and the militaries that really respect the constitution and the people,”* he also mentioned that *“unity parties respect the Venezuelan Armed Forces”* but that this attitude represented only a minority group within the Armed Forces.

More pressure on the Salary Law. Over the last few weeks there has been a significant increase in the demands received by the Supreme Court of Justice (TSJ) against the Organic Law of Salaries, Pensions and Retirement Funds of High-rank Public Officers, looking to get it dismissed. This regulation established the maximum salary of the President of the Republic, Ministers, National Assembly Representatives, National Electoral Council rectors, Central Bank directors, Attorney general, Ombudsmen, Comptroller and TSJ Members at twelve minimum wages. Among the claimants are the San Diego Municipal Hall, Carabobo State; the Municipal Council of Atures, Amazonas State; and the Municipal Council of Francisco de Miranda, Anzoategui State. Organizations such as Transparency Venezuela fear that this salary reduction could provoke an increase in corruption.

MUD supports the strike. In representation of the Democratic Unity Table (MUD), Edgar, Representative for Accion Democratica (AD), handed out a document to the young strikers outside the office of the Organization of American States (OAS) stating the opposition supported their requests. This protest is to back the parliamentary immunity of Representatives Biaggio Pilieri and Jose Sanchez, who haven’t been able to get sworn in due to the ordinary judicial processes they are being subjected to.

Emergency Organic Law for Land and Housing applied. Lands of Ciudad Tiuna I and Ciudad Tiuna II (Tiuna Fort, South-East of the Libertador Municipality), Estacion Cua (Urdaneta Municipality, Miranda State), Charallave Norte (Cristobal Rojas Municipality, Miranda State), CODECYT (Urdaneta Municipality, Miranda State), Lomas de Guadalupe (Lander Municipality, Miranda State), El Triplex (Independencia Municipality, Miranda State), Playa Grande (Vargas Municipality, Vargas State), Catia La Mar (Vargas Municipality, Vargas State), Libertador Base (Libertador Municipality, Aragua State), Aragua Base (Girardot Municipality, Aragua State), Socoromi (Bolívar Municipality, Anzoategui State), El Viñedo (Bolívar Municipality, Anzoategui State), Yucatan (Iribarren Municipality, Lara State) and East Coast of the Maracaibo Lake (Lagunillas Municipality, Zulia State) were declared as *“Vital Areas of Residential Housing”* and published in Official Gazette N° 39,615 by Presidential Order in accordance with the Emergency Organic Law for Land and Housing. Also, 62 acres of Barrio Federico Quiroz were evacuated for it being an *“Area of Housing Emergency.”*



ECONOMIC OVERVIEW

