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***VENEZUELA IS
INCREASINGLY LESS
COMPETITIVE... BUT
THE SWAP MARKET HAS
BEGUN TO LEVEL OUT***

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**What does RER
say?**

Real exchange rate (RER) is a measure that allows us to verify how prices behave within the economy in comparison with foreign prices and gives a hint of how competitive our exports are. In the case of Venezuela, the policy of exchange rate control has resulted in a substantial overvaluation of the Venezuelan currency, which has impacted our competitiveness, in particular with the US, Brazil and Colombia.

When we say that RER is appreciated, we mean that domestic inflation grows more than the exchange rate so that domestic currency buys more goods and services abroad than in the domestic economy. This brings about a loss of competitiveness of the country's exports and encourages imports. However, when RER is depreciated, the external price level, measured based on the exchange rate, is higher than domestic inflation. Therefore, goods produced in the local economy are cheaper than those produced abroad thus rendering our exports more competitive.

The degree of overvaluation or undervaluation of our currency can be measured through an RER index. Since we want to know how competitive we are concerning the production of tradable goods, the logical step consists of relating our currency with the legal tender in the

countries that are our most important trade partners. In consequence, we at **Ecoanalítica** have updated our RER index with respect to US dollar, the Colombian peso and the Brazilian real, using as the base year an average between 1990 and 1993.

How to read this indicator?

An RER over 100 means that the currency is undervalued and, therefore, the purchasing power is higher within the country than abroad. And, if RER is below 100, we can say that local currency is weak; meaning that purchasing power abroad is higher than at the local level.

Overvaluation with respect to the US is indisputable

The RER that results from relating inflation in our economy to that in the US is below 100 for most of the periods studied; that is, that the bolivar's purchasing power, either old or strong bolivars, is lower in Venezuela than abroad. Therefore, economic agents are strongly encouraged to import all good and inputs they require. The 40% increase registered by imports in 2007 shows this clearly.

When domestic inflation largely surpasses devaluation, our companies' production costs increase at a faster pace than those of our international competitors, whose exports gain competitiveness in comparison to ours.

Exchange control proves once again to be unsustainable

The exchange rate control, which has been in force over the last five years, has increased bolivar's appreciation, which is reflected in the decrease in RER index. In fact, our estimates show that, only considering the US economy, exchange rate that would compensate for overvaluation levels for the month of May is 4.33 VEF/US\$. This implies that there is a wide gap between the official exchange rate and its implicit value; this translates into a 50.3% difference.

Another interesting point that is worth highlighting is related to the significant decrease in the swap market and the implicit exchange rate of the last placement of international bonds, which was far below VEF 4.30:US\$. In other words, the bond placement resulted in a very cheap dollar, only if we consider the US economy.

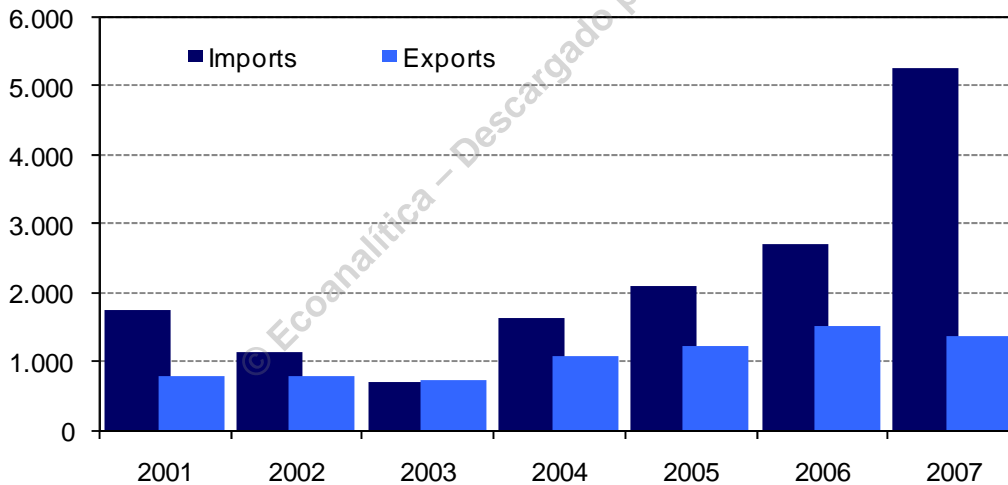
However, as we have pointed out before, although the economy's behavior shows us that the exchange control should be lifted in the short term, the Government has little incentive to do that, because it can use the exchange control as a tool for political deterrence.

The situation with Colombia isn't so serious

Repeating the same exercise with the Colombian peso, we observed that the RER index is also below 100, although in a lesser degree than with respect to the US dollar. This shows that the official exchange rate is overvalued by 15.8%. This results in an implicit exchange rate with Colombia of VEF 2.55 per dollar. This value, although it's only slightly higher than the official exchange rate, shows us that Venezuelan exports have become less competitive vis-à-vis its second trade partner, although never at the same levels as those reached with the US economy.

Moreover, perhaps due to this fall in competitiveness, our exports toward Colombia have systematically reduced over the last years, whereas our imports from that country have multiplied. This has resulted in an increasingly negative trade balance between Colombia and Venezuela.

Venezuela/Colombia foreign trade
US\$ Millions

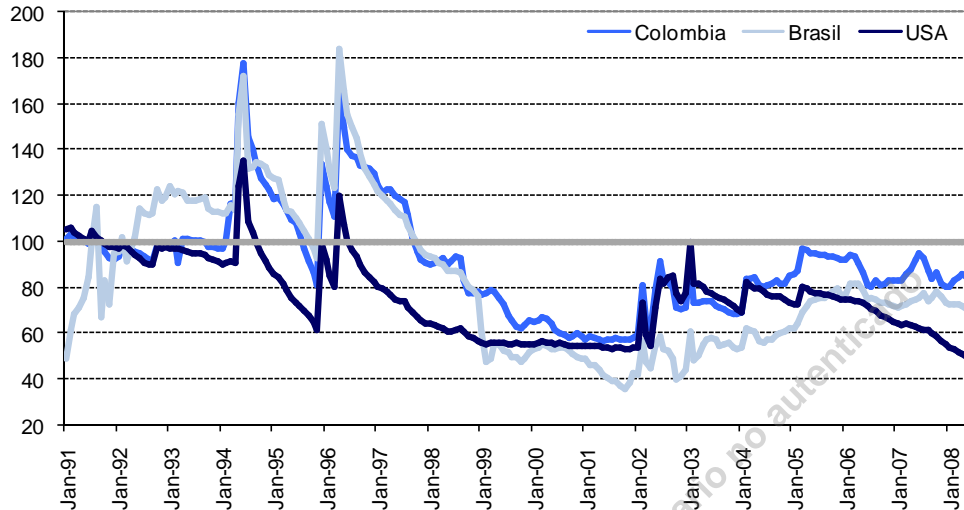


Source: ALADI and Ecoanalítica

With Brazil it's different, but not too much...

RER index with Brazil, in turn, reflects that the implicit exchange rate forecasted for the month of May is equivalent to 3.03 VEF/US\$. This means a 29.2% overvaluation with respect to the current official exchange rate. In other words, in this case we have an "cheap" exchange rate, so that production costs in the Brazilian industry, measured in dollars, are lower than those in Venezuela, which favors exports of that country.

**Real Exchange Rate Index
1990-93=100**



However, we have to highlight that our non-oil exports are really low because they account for 10% of total exports, on average. Furthermore, the situation with Brazil is analogous to that with Colombia: restrictions in the domestic productive sector, related to administrative obstacles or the lack of legal security, determine a clear deterioration of our trade balance with that country. This becomes a vicious circle because the limited domestic supply of goods makes it necessary to cover consumers' needs with an increasingly larger volume of imports.

**Venezuela/Brasil foreign trade
US\$ Millions**



The swap market has begun to level out

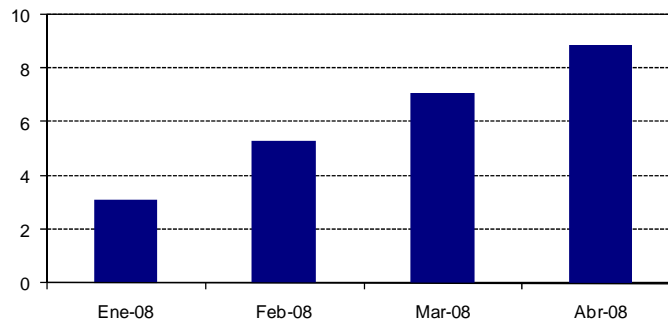
Up until now we have analyzed each case separately. However, the proper procedure is to determine, based on this simple RER model, which is the exchange rate that we should have today, considering our three major trade partners. The implicit exchange rate would be, therefore, VEF 3.71 per dollar, i.e. 72.5% higher than the official exchange rate. It's important to stress that the current swap rate has been moving around lower levels to this value.

However, it isn't completely clear that swap rate will remain at these levels over the next months. If the Government continues with its policy of restricting foreign exchange for imports, along with a strong fiscal expansion in the second half of the year, the parallel market is going to be under a substantial pressure that will be reflected in its price, despite of the fact that the Government has announced more issues. Therefore, we advise our clients to take into account these considerations when designing their coverage strategies. The popular saying says *"better the devil you know than the devil you don't."*

Economic Tips

1.7% in April. The National Consumer Price Index (NCPI) registered a 1.7% variation in April, similar to that reported the previous month, according to BCV. The Central Bank explained in a statement, that with April's results, the cumulative variation for the four first months of 2008 amounted to 8.9%. The highest month-to-month variations occurred in transportation (2.8%), restaurants and hotels (2.1%), health (2.0%), and food and non-alcoholic beverages (1.8%). Price behavior in April was the result of uniform growth both in the price-controlled items (from 1.8% to 1.7%) as well as in the non-controlled ones (from 1.7% to 1.6%) he added.

National Consumer Prices Index
(Accumulated %)



More structured notes still to be offered. Of the US\$6.20 billion of FONDEN's funds, which were invested in structured notes, there are around US\$500 million left, according to our estimates, which could be offered to the public. The rest has matured or has been sold before.

Savings mechanism for workers. The Minister of Planning and Development, Haiman El Troudi, is studying at the request of the president, different savings mechanisms for workers. The most attractive of all possibilities is a likely debt issue for workers to invest in State bond, besides a reform of the law that currently rules savings banks.

New foreign exchange budget for 2009. The Minister of Planning and Development, Haiman El Troudi, announced that the Executive is working on a foreign exchange budget for next year. He added that it consists of determining the number of products that the economy requires apart from food, and based on this a budget will be prepared to determine the amount of foreign exchange necessary to import the goods that the country needs, such as consumption and capital goods and finished products. This system, in fact, has been operating somehow over the last few months.

Unions remind employers wage and salary increase. Unions that gather the workers of regional governments and mayor's offices will send an official letter to regional governors in which they ask the 30% wage and salary increase authorized for the central administration personnel to be granted to them.

Wage and salary increase will push inflation up. José Manuel González, chairman of Fedecámaras, said that the impact of inflation will overwhelm that of the wage and salary increase. He added that the increase percentage decreed is an explicit acknowledgement by the Executive of their incompetence to control inflation in the country.

The wage and salary increase isn't included in the budget. Wage and salary increase will imply a VEF 5.5 billion increase for the Administration and a total VEF 31.0 billion increase for the fiscal year, more than the VEF 25.4 billion budgeted. This increase in Government's spending will have a substantial impact on liquidity, contrary to the policies that have been implemented by the Executive.

Regions will receive less money. Based on the reforms of legal frameworks, revenue sharing will decrease and now, with the tax on oil windfall profits and the

cutback on income tax contribution, regions will receive fewer resources, with this drop being estimated at US\$ 1.1 billion for the year.

Higher interest rates. As a policy to encourage savings, the Executive ordered the BCV to increase interest rates. Savers will now receive 15% for deposits and 17% for time deposits, whereas people with credit card debts will be subject to a 33% rate.

Other rates were also adjusted. The Central Bank also adjusted rates for absorption operations: 13% (28 days) and 14% (56 days). For injection operations, rates were set at 22% (7 days), 23% (14 days) and 24% (28 days).

International reserves. International reserves were at US\$ 31.02 billion on the first week of May, up 1.23% from the last week of April.

Interest rates. Interest rates of the six major banks in the country were at 22.64% on the fourth week of April. Time deposits gained 0.22% to 14.22%.

Liquidity. Liquidity closed at VEF 152.05 billion for the third week of April, up 2.62% from the prior week.

OIL TIPS

Deceleration of Venezuelan oil basket prices. According to the Ministry of Energy and Petroleum, the barrel of Venezuelan oil crude and by-product lost US\$1.83 last week, averaging US\$103.25.

International indicators also lost ground. West Texas Intermediate and Brent lost US\$1.54 and US\$1.35 per barrel, closing the week with averages of US\$115.8 and US\$113.7 per barrel, respectively. OPEC basket lost US\$0.67 last week to close at US\$109/bbl.

However, averages set record levels. April's monthly average closed at US\$100.14. Cumulative price for the year so far is US\$92.19, up around US\$ 28 from the last year's average and up 163% from the price estimated for this year's budget.

MENPET will regulate the new tax. Rafael Ramírez, minister of energy and Petroleum, announced that the new oil windfall profits tax, unlike other taxes, will be collected by MENPET with the proceeds being earmarked for FONDEN. According to the law that will govern the tax, “contribution” payments have to be made on a monthly basis and in foreign currency.

There’re still doubts. The regulation issued by MENPET doesn’t expressly mention what will be the source employed to determine the Brent price, which is the marker used to compute the tax, or how it will be collected every month.

What about mixed companies? Article 1 of the law provides for that the contribution “shall be paid by those who export or transport liquid hydrocarbons abroad.” However, mixed companies don’t export the extracted barrels directly. Notwithstanding, Ramírez pointed out that all mixed companies must pay the new tax, because oil purchase-sales contracts signed by PDVSA are based on a net-back system, according to which all partners to such companies are benefited from the export price.

PDVSA included financial deficit in the budget. According to the April 30th Official Gazette, published by the National Budget Office, 2008 PDVSA’s budget increased by 25.3% in comparison with last year, to VEF 121.7 billion. This balance, under the premise used for the national budget of a price of US\$35 for the Venezuelan basket, reflects a financial deficit of VEF 26.53 billion, which results from a similar deficit in the capital account and represents a 117% increase with respect to the deficit estimated for 2007.

PDVSA’s cumulative amortization and depreciation increase. A 31% increase in cumulative amortization and depreciation is observed in the capital account, from VEF 1.73 billion to VEF.4.04 billion, in comparison with 2007, and a 56% increase in capital expenditures, from VEF 21.65 billion to VEF.33.69 billion, with respect to last year. It’s worth mentioning that these figures would likely change if the annual average oil price that will register the Venezuelan basket this year is taken as a reference, which will not fall below US\$80 this year.

Payroll increase. PDVSA has plans to increase its full time personnel by 26%, from 56,748 to 71,652 employees this year. However, minor payroll is expected to fall from 17,300 to 16,959 people with the number of workers in the daily payroll increasing only by 267 people, to 15,715 workers. Therefore, the increase expected for the total payroll can be attributed to the substantial growth of the managers’ and top executives’ payroll, which will increase from 23,523 up to 37,852 and from 477 up to 1,126 people, respectively.

Operational premises. PDVSA's budget foresees an increase of 386,000 b/d for 2008, to an average production of 3.63 million b/d and an export volume of 2.9 million b/d, i.e. 299,000 b/d more than in 2007. For fuel sales on the domestic market, the same number of daily barrels as the one used as a reference for 2007 budget (550,000 b/d) is expected. Finally, 458,000 b/d of natural gas are expected to be placed on the domestic market this year.

Barrels' destination diversified. According to the Minister of Energy and Petroleum and President of PDVSA, Rafael Ramírez, it is planned to change the destination of the crude oil improved in the Oil Belt, most of which is currently being shipped to the US. The diversification will be carried out without disrespecting current agreements.

BUSINESS SECTOR TIPS

Wage and salary increase for doctors too. The president of the Frente Nacional de Médicos Bolivarianos, Fernando Bianco, stated that the project of the National Public Health System contemplates in its proposal a substantial salary increase for workers of this sector and an improvement in the country's health infrastructure.

Food industry growth is slowing down. Eduardo Gómez Sigala, president of Conindustria, announced that this productive activity grew 6.5% in January 2007, whereas growth in January 2008 was 2.5%. The decrease is due mainly to the foreign currency restrictions, the implementation of the Tax on Financial Transactions, and the high labor conflicts in the industrial sector.

Food imports grow. CADIVI increased its foreign currency disbursement for food imports by 208%, as a measure to counteract 2006-2007 food shortages. However, import volumes didn't increase at the same proportion. The decrease in international supply, the rise in freight prices due to the distortion caused by transportation demand from Asia, weather conditions and speculation have pressured a rise in the main international prices.

PDVAL reaches out. Alberto Madail, vice-president of PDVAL, pointed out that the country's entities were grouped in seven regions in order to streamline countrywide food distribution. According to Madail, up until now, PDVAL along with Community Councils have opened 591 "Pdvalitos" and the commercialization network has 100 Pdvaes and 2 Hiper Pdvaes. Although this network was aimed at the middle class,

PDVAL is covering sectors of Class D and E, selling oil, sugar, rice, powdered milk, and beef, among other products.

Goals. PDVAL network has plans to sell around 150,000 tons of food a month by the end of 2008. These plus around 160,000 tons that Mercal expects to sell would allow Government's networks to cover approximately 30% of the monthly national consumption.

Mercal has executed 50% of subsidies for 2008. Félix Osorio, Minister of Food, announced that the Mercal network, which assumes more than 35% of the costs of 14 staples, has executed almost 50% of its budget for the year-to-date. Subsidies planned for this year amount to VEF 2.40 billion, of which VEF 1.20 billion have been executed.

Poultry sector is waiting for official foreign currency. After paying US\$14 million due to the delays of corn shipments in Puerto Cabello in August and September last year, the poultry sector is expecting the Government to recognize that amount at the official exchange rate and for it to be reimbursed.

Poultry commercialization chain increases its prices. After the adjustment of the final prices of poultry and its products, the Executive authorized a price increase in the commercialization chain. As a consequence, supply has normalized.

Against shortages. Richard Canán, Vice-Minister of Agricultural Economy and president of the Banco Agrícola de Venezuela, pointed out that the 2008-2009 Agricultural Development Plan includes sowing 2,300,000 hectares in order to produce 21 million tons of food, prioritizing items such as corn, rice and sugarcane.

Workers in CADAPE Bolivar are on strike. Workers of CADAPE Bolívar announced that work activities will be stopped starting today to demand for working apparel, implements, trucks, tools and protest against the lack of attention by the authorities who don't seem to understand the state of complete obsolescence in which CADAPE is found.

Optimistic insurance sector. The Chairman of the Cámara de Aseguradores de Venezuela (Association of Insurance Companies), Pedro Luis Garmendia, announced that, based on economic perspectives for this year, net premiums of the insurance market are expected to grow 40% by the end of the fiscal year. However, they expect accident rates for this year to be higher than the one of 2007, mainly due to the increase in spare part prices in the case of car insurance, as well as to

the price increases registered in the health sector, which had an impact on the number of cases reported for hospitalization, surgery and maternity policies.

CANTV will develop three pillars. According to the minister of telecommunications and president of CANTV, Socorro Hernández, the telephone company will work based on three fundamental pillars: the company's medullar activity, strengthening the social economy sector, and continue to work with private businesses.

The National Assembly authorizes nationalization of SIDOR. The decree that was discussed at the National Assembly last week provides for as follows: "The work Centro de Producción Siderúrgico del Orinoco (Orinoco Steel Production Center) is declared of common public and social interest. This work is bound to strengthen the strategic national sector of the transformation industry of iron ore into steel and its various products... its distribution and commercialization as well as the protection and generation of job creation sources."

SIDOR collective bargaining finally comes to an end. After a 16-month-long discussion, in the small hours of last Sunday, the collective bargaining discussions that cover 4,000 steel workers from this year until 2010 came to an end. According to José Meléndez, finance secretary of the union, the agreements reached on the collective contract will cost US\$300 million.

Higher housing costs. The reduced supply of houses, both old and new, has directly impacted prices. From August 2007 to February 2008, prices have increased 20.3% on average. In some areas, the rise surpassed 40%. Based on prices, the most expensive areas in Caracas are Los Palos Grandes, El Marqués, El Paraíso, La California Norte, Palo Verde, Chacao, and El Cafetal.

Hardware stores are also in trouble. The delays in the authorization of foreign currency by CADIVI for hardware stores are bringing about shortages of hardware and construction products, which could lead to lack of supplies in the medium term and to the strangulation of businesses in this sector.

Minister "ashamed". Rafael Ramírez, minister of energy and petroleum, admitted he was "ashamed" of the blackout of last Tuesday and assured that the Government is working to overcome the lack of investment in the power generation sector. The project contemplates investments of US\$3.75 billion, the commissioning of 17 plants, new or expanded, and the execution of transmission projects.

Nationalization affected EDC. According to the 2007 Annual Report released by Electricidad de Caracas, the company faced obstacles concerning administrative

procedures and human resources, besides failures in the transmission, distribution and power generation procedures that HAN SIDO ARRASTRADOS the AES Corporation administration. The report also warns of the serious need of skilled personnel in the company.

Funds to purchase CEMEX. The commission appointed by the National Executive to negotiate with cement companies is already appraising the assets. Once this procedure is completed, the financing scheme for the purchase of the stockholding will be agreed upon. According to the resulting amount, the Government would resort to FONDEN, the Miranda Fund (mechanism that covers supplementary appropriations) and a contribution from PDVSA.

Splitting up CEMEX. Cemex Venezuela ordinary Shareholders' Meeting was held last Friday May 2nd. The items approved include dividends and the distribution of the total retained earnings, which accounts for approximately to US\$306 million, that is, VEF 0.46/sh., with this last dividend being the largest paid in the history of the company in Venezuela. Considering the share price at the Caracas Stock Exchange, which is on the order of VEF 1.10 per share, we would be talking about more than 40% profits.

Political Tips

Next May 9th Chávez will announce how PSUV candidates will be elected. The president called upon a PSUV general assembly for next May 9th to present the party with the methodology on which the selection of the candidates for governors, mayors and legislative councils will be based. He added that the definite candidates will be ready before the month's end.

CNE must specify mechanisms for the activation of Constituent Assemblies. A ruling of the TSJ Electoral Chamber ordered CNE to specify the mechanisms that have to be developed and completed to call upon a National Constituent Assembly. Franco Casello, member of Movimiento 348, pointed out that after the petition they brought before the Electoral Chamber, this judicial entity decided that the CNE must fill the legal loophole concerning Article 348 of the National Constitution, which provides for calling upon a Constituent Assembly at the people's initiative, but which application methodology is unknown.

More Cuban doctors in Venezuela. In March and April 2008 a new group of Cuban doctors arrived in Venezuela, this time to launch the new José Gregorio Hernández Mission. This initiative is expected to gather information about disabled people in the country, in a first stage, and determine causes and design prevention and care plans for this population, in a second stage.

Elections at the UCV. The first election round for the 2008-2012 term of the 4 UCV top authorities: Rector, Academic Vice-Rector, Administrative Vice-Rector and Secretary, will be held next May 9th, with a second round scheduled for May 12th. Like is usual every 12 years, ten deans and the professorial representatives to the university co-government will also be elected.

University admission procedure. Since after the elimination of the Academic Efficiency Test, there isn't any instrument left to measure applicants' abilities, except for the internal admission tests, it was necessary to look for a more suitable admission modality. Therefore, it was agreed that the National University Council (CNU) would grant university places based on the average of high school grades.

Constitutional reform is being implemented through other ways. According to the constitutionalist lawyer Gerardo Fernández, the Government is trying to surreptitiously imposed the constitutional reform that was rejected on last December 2nd, resorting to laws, plans, decrees, decree-laws, ministerial resolutions and de-facto mechanisms.

Other Tips

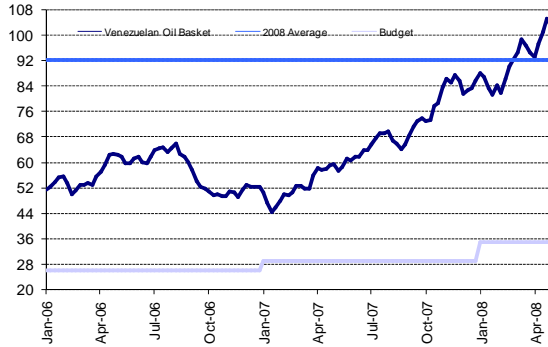
NA approved Law on Recreation in the first discussion. This legal instrument was presented by the president of the NA Commission on Education, María de Queipo. According to the spirit of the draft, the law is aimed at regulating the protection, promotion, organization, planning, coordination and implementation of public policies on recreation.

Six Latin Americans between the world's 100 most influencing people. Presidents Evo Morales and Michelle Bachelet, athletes Lorena Ochoa and Kaká, the mogul Carlos Slim and the Cuban blogger Yoani Sánchez are the six Latin Americans that managed to make this year's list of the world's 100 most influencing people of Time Magazine.

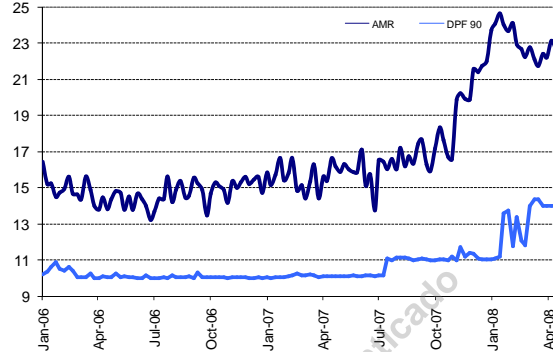
Weekly Report

ECONOMIC OVERVIEW

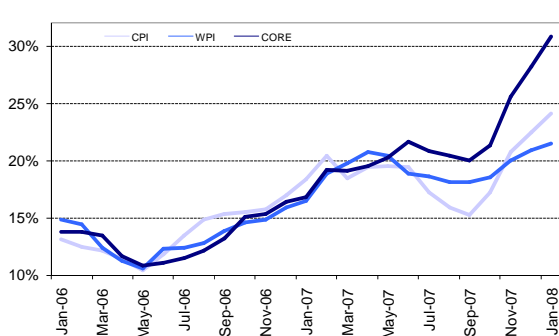
Oil Price
(Venezuelan Basket US\$/pb)



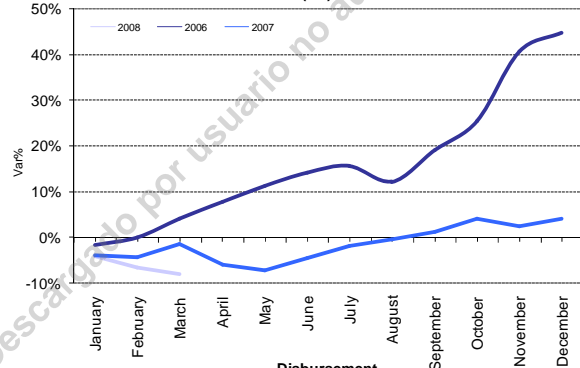
Interest Rate
(Six Principal Banks)



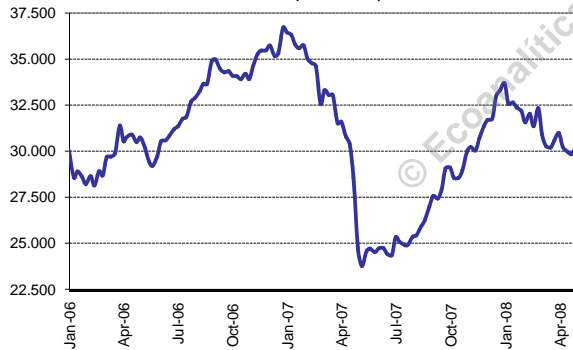
Inflation
(Last 12 Months)



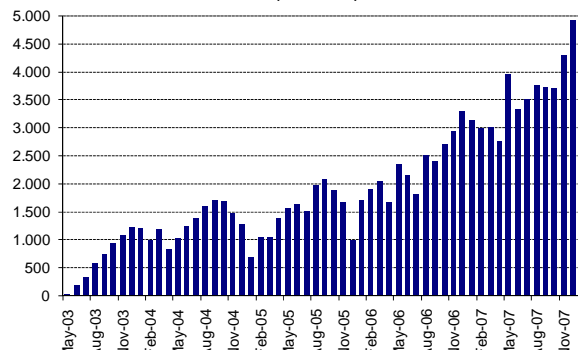
Real Expansion
(M2)



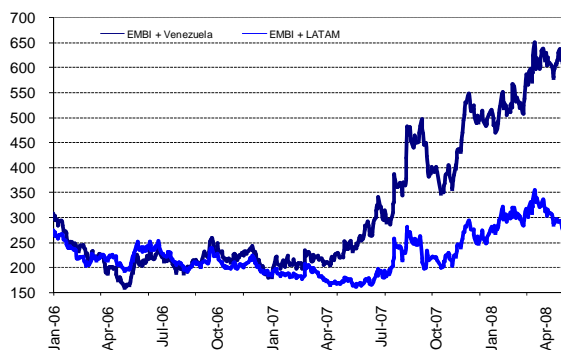
Fx Reserves - BCV
(US\$ Million)



Disbursement
(US\$ Million)



EMBI



Central Government
(VEB Billion)

