



Year 2, Number 29
August 04, 2006

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***IN SPITE OF A
REACTIVATION IN
EMPLOYMENT, THE
NATIONAL ASSEMBLY
IS MULLING
"CREATIVE" LAWS***

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THE CLIENT

The first half of 2006 has witnessed recuperation in the employment market. High economic growth has begun to create jobs, and the greater demand for personnel is edging real salaries higher. It would seem, however, that the National Assembly (AN) is turning a blind eye, because it is said to be studying a reduction of the working day, while obliging employers (both public and private) to maintain the same salaries.

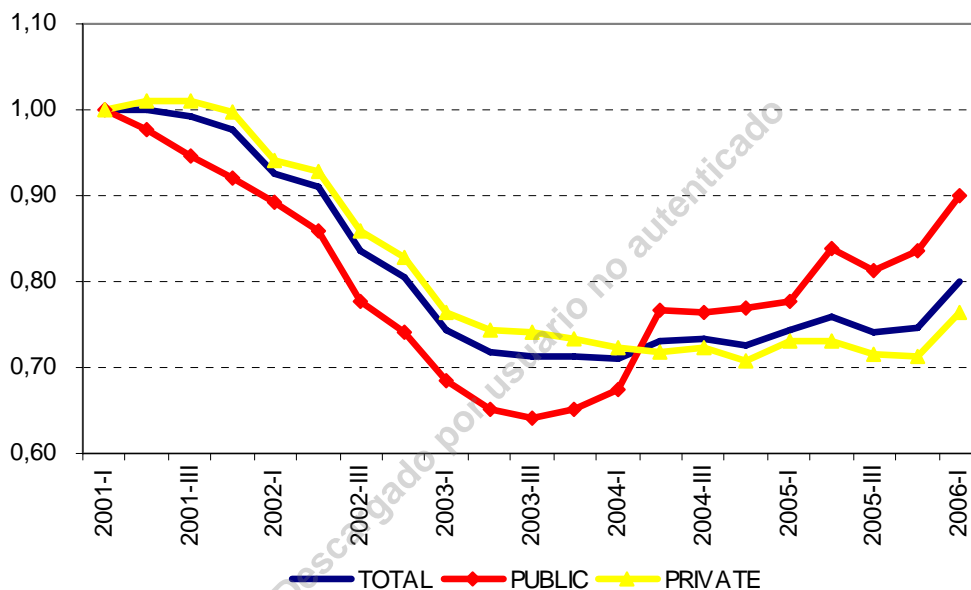
High economic growth has at last begun to generate jobs and rescue the purchasing power of salaries

The working force grew from 10.4 million in June 2005 to 10.9 million in June 2006, figures that represent 488,377 new jobs, or a growth of 4.7%. The most important aspect of this number is that almost 70% comes from the private sector and only a little over 30% from the public sector. These statistics contrast heavily with the 2005 figures, where only 37,908 jobs were created in the public sector and 240,000 jobs were lost in the private sector. This creation of jobs is reflected in

Weekly Report

an increase of almost 10% in real salaries both for the public and private sectors in the first quarter of 2006.

**Real Wages Index
(IQ-2001 = 1,00)**



Sources: BCV and Ecoanalítica

In spite of these positive numbers, the AN wants to reduce working hours

The AN is studying the possibility of reducing the working day from 8 to 4 hours as a way to bring down unemployment, since this would force companies to contract more workers to cover their labor requirements. According to the AN, the voluntary extension of the working day will not be punished, but obligatory extension could hold up the procedure to be followed by companies for obtaining their certificate of labor good-standing, as well as other sanctions. Apart from anything else, the AN has made it clear that workers' salaries will not be affected and that such changes must eventually be introduced into the Labor Law.

An ineffective measure that will scare off investment and encourage “spontaneous” employment, given the current political environment

In Europe the efficiency of job creation through reduction of working hours has been more widely debated than anywhere else. This type of measure seeks to achieve an increase in employment that is proportional to the reduction in working hours. However, in Europe the reduction percentages never go beyond 15%, while the initial proposal of the AN is a reduction of 50%. At *Ecoanalítica* we are of the opinion that the Assembly will approve a reduction in the working day that would take it to 6 or 7 working hours per day, or 30 to 35 hours per week.

Economic theory teaches us that reduction of salaries goes hand-in-hand with workers' productivity. For this reason, all attempts to create employment by reducing working hours, eliminating overtime, or the massive use of part-time contracts, inevitably lead to salary reductions. It has been clearly proven that what most contributes to the creation of employment is the efficient design of public policies that are based on the flexibilization of the job market, the increase of competitiveness among companies and investment in human capital, all of these being fundamental measures for obtaining a sustainable and socially responsible growth.

Economic Tips

Inflation rears its ugly head. CPI increased 2.4% in July, the biggest variation so far this year, higher than June (1.9%), and that of the same month last year (0.9%). So far this year inflation has been 8.1%, while the figure for the last 12 months is 13.5% - way above the official goal of 10%.

Agricultural products again. According to the Central Bank (BCV), the CPI performance for July was influenced by a lower seasonal production of determined agricultural items, by the begin of the vacation period and by the increase in school registry fees that occur around this time. It is surprising that the scant offer of agricultural products is the recurring cause of inflation increases over the last 3 months.

Greater price increases in non-controlled items. According to the BCV, prices of non-controlled goods and services rose 2.8%, while controlled items rose 1.9%, almost double the percentage reported for the previous month (1.0%).

Inflation, the Achilles heel. In spite of the different distortions and subsidies applied by the Government to keep inflation at bay, it continues to be affected by monetary aggregates, the most important driver of which is the increase in public expenditure. *Ecoanalítica* believes it is impossible for inflation to close out the year at a single digit.

Venezuela, the fastest growing country. The Economic Commission for Latin American, **CEPAL** reports that the Latin American economy will grow by 5% this year, and that the countries showing most growth will be Venezuela and the Dominican Republic, both with an 8% growth. The country that will show least growth will be Haiti with 2.5%. In light of the high oil prices, *Ecoanalítica* believes that the CEPAL's forecasts in respect of Venezuela will come up short.

The high levels of growth are thanks to an expansive fiscal policy. At the close of the first half of the year, budgetary execution stood at 50%, that is, VEB 53 trillion (out of the total annual budget of VEB 103 trillion). This means that the public expenditure of the Central Government could run to VEB 130 trillion for the complete year.

Unproductive expenditure. 50% of total expenditures have been to attend public sector salaries. The remaining 50% are for transfer to the different regions, for government agency expenses and investment in infrastructure and education, among other areas.

Income on track. According to Finance Ministry (MF) figures, the Government received oil and non-oil income of VEB 51.4 trillion, of which VEB 23 trillion came from oil. According to the same MF figures, the Government had run up a deficit of VEB 1.6 trillion by the close of the first half of 2006.

More countries to be included in debt issuing plans for 2007. Venezuela may include other countries in its designing of financial options along the line of the so-called "Southern Bonds" with Argentina. However, this proposal may not come about until halfway through next year, since financial conditions have to be discussed, as well as the financing requirements of the different countries.

Capital gains tax looms. The elimination of the succession tax and the tax on matches will be compensated with the creation of an individual capital gains tax. This levy will be paid by all individuals whose assets are valued at more than 15,000 Tax Units (VEB 505 million) and will be taxed at a flat rate of probably between 0.5% and 1%, to be declared annually and discounted from the income tax (ISLR) filing. If approved in 2007, it would enter into force in 2008, and will be levied on personal property and airplanes, boats, vehicles, jewellery, artwork, deposits abroad, shares and equity participation in companies and other assets. A person's main dwelling, participation in cooperatives

and civil associations, assets belonging to members of diplomatic and consular missions, savings accounts or funds and social benefits and household goods and domestic appliances will be exempt from the tax, as well as public national debt bonds.

Oil Tips

Prices down for the week. The Venezuelan basket fell US\$ 1.46 to finish the week at US\$ 63.37 per barrel, according to data supplied by the Ministry of Energy and Petroleum (MENEP). The July average was US\$ 64.14 per barrel and so far this year the basket has averaged US\$ 58.01 per barrel.

PDVSA moves away from the market. Moody's, the investment rating agency, announced that it will no longer issue ratings for PDVSA because the company does not supply "adequate" information on its operations. This affects the B1 rating for local currency issues and the B1 rating for foreign currency issues. An important fact emphasized by Moody's is that "as far as can be seen, PDVSA does not intend to timely provide verified financial information."

Moody's decision does not affect Citgo or Orinoco Oil Belt. The decision does not affect Citgo or other projects in which the Venezuelan oil company participates, since all such entities continue to provide information on their accounts and operations. It may well be that other rating agencies (Standard and Poor's, Fitch) take a decision similar to Moody's.

Russia moves into the gas business. The Russian firm GAZPROM has executed a contract with PDVSA to develop gas projects in our country. GAZPROM is to prepare a plan evaluating Venezuelan gas reserves and demand, in order to precisely program natural gas extraction, transport, storage and treatment.

Sectoral Tips

CANTV presents numbers. CANTV income for Q206 increased 34%, while expenses rose 40%, mainly due to strong competition in the cellular phone market. Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) for the same period increased 12.5%. An outstanding fact is that free accumulated cash flow rose 53.5% for the year.

Movilnet in the lead. CANTV continues its penchant towards boosting its cell phones business and the second quarter numbers show that its Movilnet affiliate contributed 46% to overall income, followed by fixed-line services at 41%, with the remainder belonging to Internet (13%). Cellular telephone business grew 69% year-on-year, followed by Internet, 35%, and fixed-line services which only grew 9%.

Debt continues to fall. CANTV has been steadily drawing down its debt, so much so that at the close of June, company debt stood at US\$ 34.9 million, i.e., a 73% reduction on the June 2005 figure.

Earnings too. CANTV's earnings fell 16% for Q206 on an interannual basis, explained by less tax benefits, drop in performance and absence of exchange earnings. Generally speaking, we believe that the CANTV results are positive and that during the second half the numbers will improve, given the growth dynamic of the telecommunications sector.

Telefónica does well. Movistar Venezuela has announced that its number of lines grew by 1.1 million in the year's second quarter, to reach a total of 7.8 million clients. This represents an 89% increase over the second quarter of 2005. In addition, the strong growth of its client base, together with more traffic and the continuing improvement of data registry, all contributed to a growth of 51% in local currency services income over the first half of 2005 and 49% over total income. EBITDA increased by 33.5% year-on-year. Besides this, Movistar earned US\$ 630 million in the country during Q206, 33% more than a year ago.

Market penetration growing. According to MOVISTAR, the cell phone market penetration reached 58% at the close of the first half, an increase of 19 percentage points with respect to the first semester of 2005.

CEMEX results. CEMEX net sales for Q206 were 14% up on Q205, but net profit was down 22%. Apart from Venezuela, these operations include Panama and the Dominican Republic. In Venezuela, the volume of cement sold in the domestic market increased 32% and concrete 19%, compared with 2005. On the other hand, exports declined by 43% against last year. Cemex República Dominicana, a subsidiary of Cemex Venezuela, increased its volumes of cement dispatches in 33% and concrete in 71%, thanks to the reactivation of construction in the tourism and residential areas. On its part, Cemex Panamá managed an increase in cement volumes dispatched of 15%, while concrete grew by 82%, due to the acquisition of new concrete plants.

SIVENSA also reports sales. A growth of 7% in Q206 sales, year-on-year, was reported, with special mention made of an increase of 19% in local sales. The company

reported losses of US\$ 18.2 million against profits of US\$ 75.1 million in the second quarter of 2005.

Increase of mortgage financing sought. The Bank Superintendency, through its Superintendent Trino Díaz, noted that it is studying ways to increase the levels of banks' sources for mortgage financing. The current obligatory portfolio is established as 10% of a bank's total portfolio, 7% of which goes in credits to builders and the remaining 3% for individual housing loans. Among the options available, two in particular are under study, one of which is to maintain the current portfolio at 10%, but divided 5% and 5%; and the second option is to increase the obligatory portfolio to 12%, of which 7% would be maintained for builders, and personal credits would be upped to 5%.

Unification of the State electricity sector. The Energy Sub commission of the National Assembly is proposing a reform of the Organic Law of Electricity Services to incorporate an entity or institute that will unite the two State electricity companies (CADAFE and EDELCA). It should be mentioned that the management and the workers of both companies are against the measure.

Petrochemical sector in crisis ... The Venezuelan Association of Chemical and Petrochemical Industries, which represents 110 companies and contributes 12% to the country's manufacturing GDP, has declared that the sector is experiencing an "uncertain economic climate that is impossible to quantify." The greatest difficulty is that activity in the internal market is in decline, mainly due to the increase of imports.

... but the metallurgical sector is growing. The metallurgical and metal mechanical sector has reported an increase in its used capacity from 8% to 10% in the first half of the year. According to sector spokespersons, the main drivers of this expansion are the investments leveraged by the plans of the Executive, especially in the oil, railroad and housing areas. Total employment in this sector has also grown by between 55,000 and 60,000 jobs.

3rd postponement. The Venezuelan Airlines Association and representatives of the airlines that had decided to lower the amount paid in commissions to the travel agencies for acting as intermediaries, have decided to extend for a further 15-day period the reduction of sales-based commissions to 3%, originally established for July 31. The purpose of this program is to analyze the impact of the measure on the sector, and to draw up possible actions to counteract such effects.

Only 1/4 of the goal has been met. As of the close of the first six-month period, the Government had constructed only 35,000 homes, just 24% of the year's target of 150,000 housing solutions.

Political Tips

Chávez yes, Rosales probably no. The Constitutional Chamber of the Supreme Tribunal (TSJ) declared that President Hugo Chávez is not obliged to remove himself from his post in order to dedicate himself to his re-election campaign. However, the same sentence dictated that those holding a high level public position, such as the case of Governor Manuel Rosales, must resign their posts if they aspire to a different position. The measure caused surprise, and the people at the National Election Commission (CNE) are still not clear as to scope of the sentence and as to whether Rosales will have to definitively resign as Governor if he enrolls as a presidential candidate.

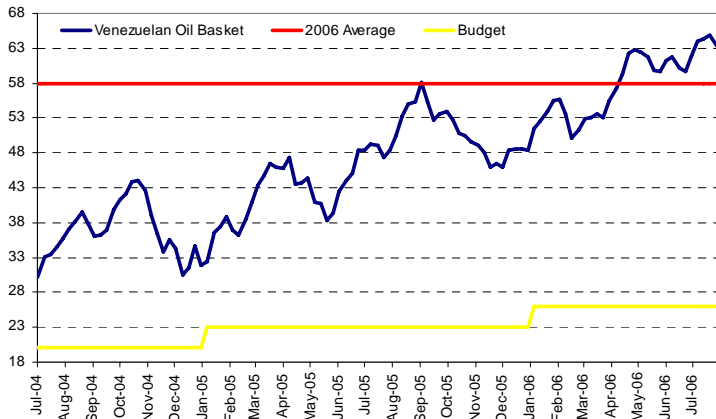
Publicity and propaganda regulations passed. The CNE has approved the publicity and propaganda regulations that are to govern the upcoming elections, emphasizing that no restrictions will be imposed on the Head of State during his re-election campaign. In other words, "Alo Presidente" will not be suspended and the blanket broadcasts by the President will not be regulated.

There will be no primaries. The three main opposition candidates (Julio Borges, Manuel Rosales and Teodoro Petkoff) have made clear in a joint communiqué that they are committed to a single candidacy, irrespective of the selection method. On the other hand, it is unlikely that primaries will be held, and in our opinion this would be favorable for the opposition sector, in light of the logistical and organizational problems being faced by SUMATE in organizing the run-offs. The most important thing for the opposition is that there be one sole candidate.

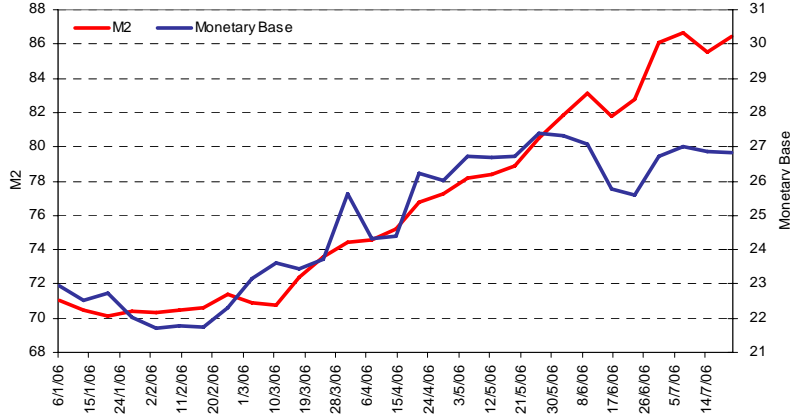
More candidates join the fray. Last week the comedian Benjamín Rausseo launched his presidential candidacy. Rausseo has no political experience and we at **Ecoanalítica** are skeptical about this candidate's achieving support among the lesser-privileged members of society. Another potential candidate is the ex-President of FOGADE Jesús Caldera Infante who left the Government under the cloud of accusations of corruption.

ECONOMIC OVERVIEW

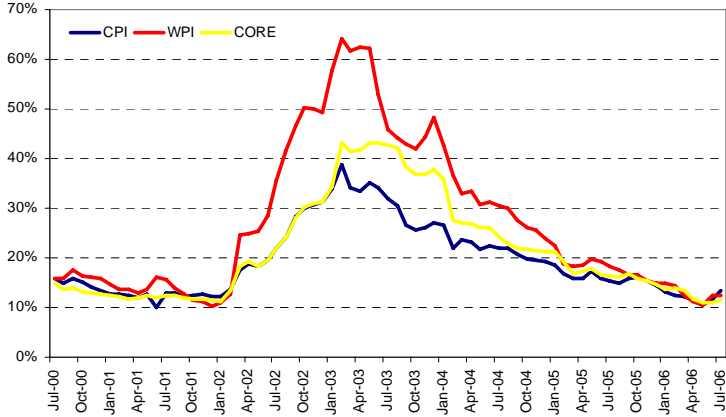
Oil Price
(Venezuelan Basket US\$/pb)



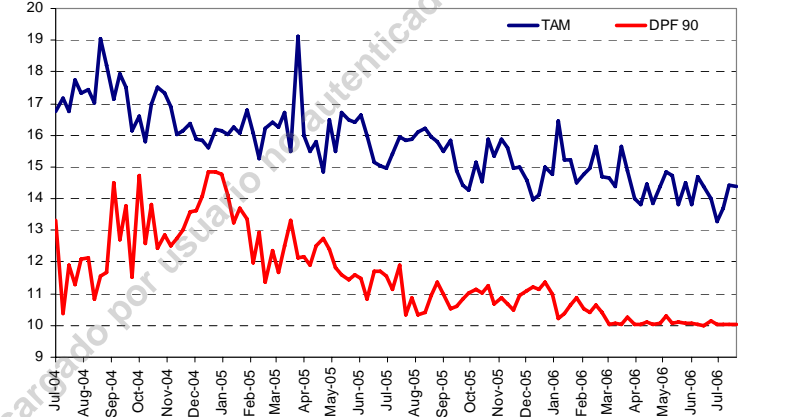
Monetary Base & M2
(VEB Billions)



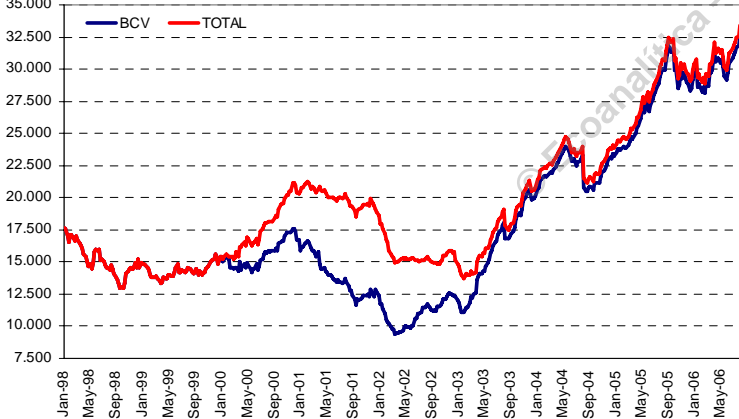
Inflation
(Last 12 Months)



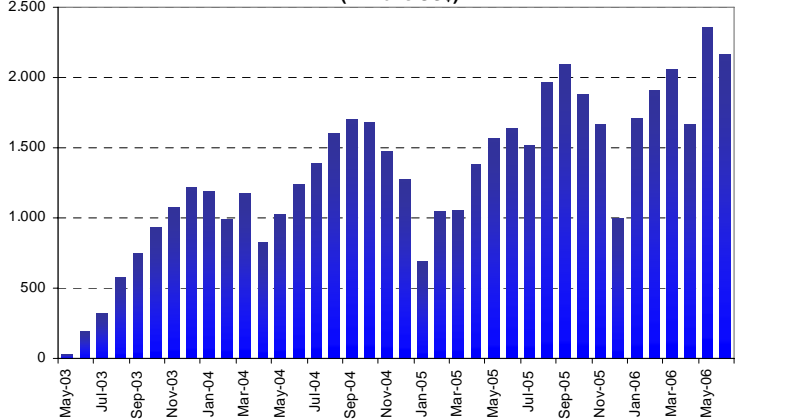
Interest Rate
(Six Principal Banks)



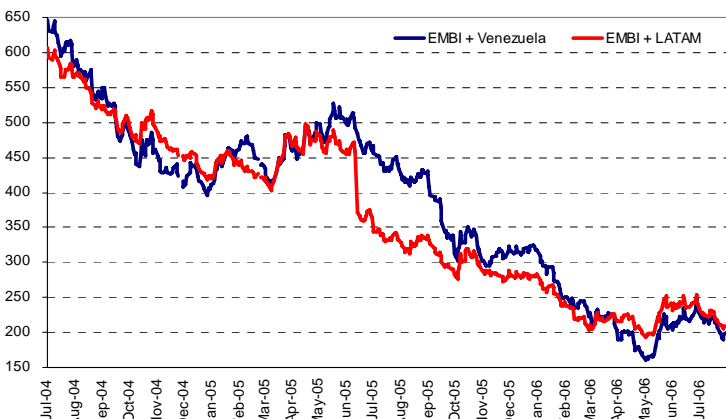
Fx Reserves
(Millions US\$)



Disbursement
(Millions US\$)



EMBI



Central Government
(VEB Billions)

