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WHAT DOES 21ST CENTURY SOCIALISM HAVE IN STORE FOR US?

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THE CLIENT

21st century socialism is a euphemism used by the government for its economic plan. The plan can be summarized as more regulation for private enterprise, especially profits, entry of new actors, and strengthening of state capitalism. However, the announced constitutional reform could be a new inhibiting factor for private investment in 2007.

Not even the president knows for certain what 21st century socialism is

Since President Chavez began to talk about 21st century socialism in early 2005, many theories and explanations have emerged to try to pin down what this concept really means. There are versions for all tastes ranging from the most recalcitrant leftist radicalism to those who say the new concept is just another name for the Third Way that Tony Blair has been introducing in the United Kingdom.

Some time ago, in one of the few meetings that President Chavez has held with FEDECAMARAS, he was asked what this 21st century socialism was. Chavez replied: "I don't know yet, we're building it."

Weekly Report

On the day of his reelection the president said that his version of socialism would be native, Christian, indigenous and Bolivarian. Government party (MVR) deputy Carlos Escarrá said that it would not imitate or copy models. "We are challenged to invent something. What? To tell the truth, I don't know. It's going to come out of the debates."

Now, after the presidential election, the debate has revived

After President Chavez' significant victory in the election obtaining 63% of the votes, the government announced that it would make some significant changes to the Constitution next year. Before the election, on October 31, Chavez said he would appoint a presidential commission for constitutional reform. So far, the commission only has one known member: Carlos Escarrá but Chavez is expected to appoint the other members soon.

For its part, the opposition also announced its decision to enter the debate by setting up its own commission to study all aspects of constitutional reform. It is worth noting that both sides (government and opposition) will present essentially diametrically opposed proposals.

On the government side, it seems that "21st century socialism" will entail:

1. Bringing people power into the Constitution. The first steps have already been taken with so-called "street parliamentarianism" and new organizations such as community councils.
2. Respect for private property, but other variants will be introduced, such as social, collective, and public property. A new correlation will be attempted between the factors of production, with the human factor rather than capital prevailing.
3. Changing the concept of free competition for a fair and equitable economy.
4. Moving from a decentralized state to a centralized but deconcentrated state.
5. Analyzing the media concessions.
6. Evaluating creation of a constitutional court.
7. Significant changes in the presidential system: indefinite reelection, changes in recall referendums, etc.

8. Creating a new electoral branch of government consisting of "true representatives of society."

The scope of the reform is still far from clear

Government spokesmen have said that the recommendations of the Presidential Commission will be submitted to the National Assembly. Assembly President Cilia Flores said the document also would be submitted to social parliamentarianism in the street, and then go to a referendum for approval. However, the proposals so far are very general, so it is difficult to define the scope of the reform, combined with the fact that there are very diverse currents inside the government, each with its own specific idea on what the reform should be.

The opposition also presented its reform ideas

Former presidential candidate Manual Rosales said that the main points to be included in a constitutional reform should be:

1. Four-year presidential period with a single reelection and run-off.
2. Review of redistribution of oil revenue.
3. Guarantees for private property.
4. Strengthen decentralization, establishing the state government public finance system
5. Introduction of a social security system.
6. Implement the Federal Council of Government
7. Reestablish proportional representation of minorities in legislative bodies.

21st century socialism is no more than regulating profits.

So far, Rodrigo Cabezas, chairman of the National Assembly Finance Committee, is the person who has best delineated the scope of 21st century socialism for the private sector. According to *El Nacional* newspaper, Cabezas said that the Constitution should include new alternative forms of association, which means joint ventures, state companies, cooperatives, self-management, and social production enterprises which are not included in the present text.

Cabezas categorically stated that the strategic aspects of the reform do not include suppression of private property; that right is not denied by 21st century socialism."

However, the Bolivarian government wants the private sector to contribute to the State through regulation of profits. Cabezas goes

further and says that "profits will be regulated by tax mechanisms ..." He believes that it will probably not be necessary to include more taxes in the Constitution but in the legislation that develops the new constitutional provisions.

More worker participation in decision-making

The government proposal includes a section on worker participation in decision-making in private companies. This does not mean that workers take over companies but that they can give their opinion on important issues, such as production increases.

And more regulation of monopolies

The reform of the Constitution could also include a provision so that "society can combat monopolies and oligopolies which are contrary to the public interest." The National Assembly is currently discussing an Anti-Trust bill along these lines. However, the negative aspects of the bill are that the State is left out of its scope, it lacks clear mechanisms to promote free competition, and its sanctions regime is, in our opinion, disproportionate.

21st century socialism = more state capitalism

According to Cabezas, the State will be responsible for setting up new forms of property, and granting financial and managerial support. The State could also take control of companies in key sectors; however, this point has many facets and has not been discussed in depth, and there is no clear tendency even in the government.

2007 another year of uncertainty

Although **Ecoanalítica** is convinced that the government is not going to abolish private property or anything like it, the mere fact that next year the country will be immersed in a constitutional reform process will generate noise in the private sector and will be a fundamental factor inhibiting private investment. As happened this year, lack of investment by the private sector will be compensated by public investments through a clearly expansionary fiscal policy along with growth of imports.

The industrial sector has said that government priority in 2007 must be to generate the confidence needed to reactivate investments and bring in new capital to set up industries in the country.

Lastly, **Ecoanalítica** echoes the words of CONINDUSTRIA President Eduardo G. Sigala: "Socialism as a word does not disturb me as long as there is space for private activity as there has been in many

economies of this type. For us the important issue is that there are guarantees for private property."

Economic Tips

More growth for 2007. According to Finance Minister Nelson Merentes, in 2007 the economy will outperform the growth achieved in Venezuela this year, which is over 10%. Even so, the budget is based on 5% growth.

Surpluses to be in Constitution. According to Carlos Escarrá, who heads the commission for constitutional reform, the use of surplus revenue will be included in the fiscal regime. The changes could establish that additional oil revenue and surplus international reserves have to be deposited in a special scheme to be used for investment. The reform is also likely to clearly define the concept of surplus reserves.

FEM to stay. Escarrá said that although FONDEN would be included in the text, the provision that obliges setting up the Macroeconomic Stabilization Fund (FEM) will be retained. Until now, the government has used legislative sleight of hand to avoid making contributions to FEM during the current oil bonanza.

Budgeted expenditure goes on rising. The National Assembly Finance Committee authorized three additional credits totaling VEB1.7 trillion. Of the funds approved, 50% will go to pay labor liabilities and pending end-of-year bonuses. The rest will cover other expenditure. With this latest addition, approved expenditure could top VEB125 trillion (US\$58.14 billion).

Surpluses for 2007. Next year the government will have surplus funds available of around VEB10 trillion (US\$4.65 billion), according to Ministry of Finance calculations. These are funds not used in 2006, and include oil and tax revenue. Official sources indicate that this is a minimum surplus scenario since higher revenue cannot be ruled out.

Government places more debt. The Finance Ministry placed US\$225 million on the local market in TICC bonds (payable in bolivars but with dollar-indexed principal and interest) due in 2017. The TICC were auctioned at an average weighted price of 120.068% with a 3,766-day term and a nominal rate of 6.25%, according to information from the Central Bank. A similar amount was placed last week.

More anachronistic protectionism. The government placed restrictions on imported goods which it considers "luxury" or non-priority. On average, the government imposed a 15% tariff surcharge. The items affected include jewelry, some alcoholic drinks, cigars, sailboats, clothes, shavers, furniture, candles, and toilet paper. The measure will have limited impact on the CPI because the products are not part of the average basket of goods for a typical family.

Other priority goods. In another resolution, the government issued a list of goods and their parts used in industrial and agricultural processes, raw materials and inputs not produced in the country, which will receive CADIVI authorization for purchase of dollars without need to apply for a national production certificate from the Ministry of Light Industry and Commerce (MILCO). The list of priority goods consists of products and inputs mainly for the pharmaceutical, textile, industrial and agricultural sectors.

CADIVI authorizations up. CADIVI increased foreign currency approvals by 30.6% between January and November 2006 compared with the same period last year. Daily approvals this year averaged US\$105 million, compared with US\$90 million in 2005. Between January and July daily authorizations were about US\$94 million, but from August to November they speeded up to above US\$110 million. The highest daily level was US\$133 million in November.

Oil Tips

Oil basket rises. The Venezuelan crude basket gained ground for the second week in a row, up US\$1.68 per barrel to US\$53.07. Year to date, the basket has averaged US\$56.68 per barrel.

Stable forecast for oil prices. The Energy Information Administration (EIA) projects in its *Annual Energy Outlook 2007* that from now until 2015 crude prices will decline slightly bringing relief to the market but it will only be a respite. From then on prices will resume their upward trend begun in 2002 to reach a nominal average of US\$95 in 2030, equivalent to US\$59 at 2005 prices. Until 2015, the downward trend will respond to expanded investment in exploration and production, in contrast from 2016 to 2030 rapid growth of crude demand will increase extraction costs and consequently final prices.

Alternative sources will increase. The EIA forecasts an increase in consumption of biofuels, such as ethanol and biodiesel, as well as production of liquid coal. However these new energy sources will not have much weight at the end of the day because by

Weekly Report

2030, oil, coal and natural gas are expected to meet 86% of primary demand for energy in the United States.

Sectoral Tips

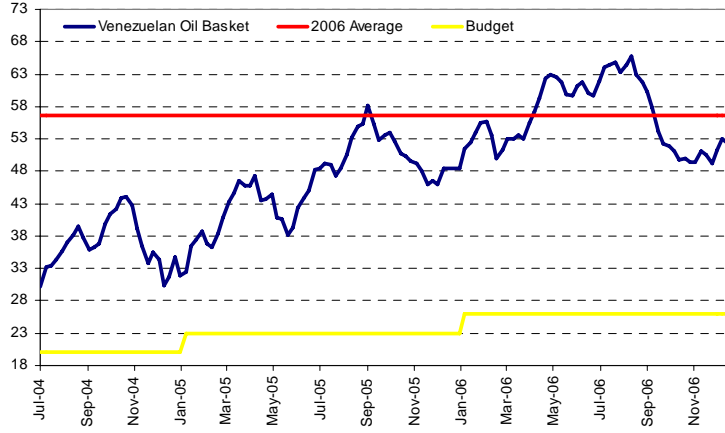
More aid for Argentina. The national government expanded the initial offer made to SANCOR from US\$80 to US\$135 million. Under the loan agreement signed yesterday by representatives of both governments (Venezuela and Argentina), BANDES allocates US\$80 million for debt restructuring and US\$55 million for working capital. SANCOR will pay back the debt with exports of powdered milk to Venezuela for 15 years, calculated at 20,000 tons a year, plus technology transfer and staff training package.

Strong growth forecast for financial sector. The banking and insurance sectors grew 30% in this period, according to Trino Alcides Díaz, the head of the Superintendency of Banks and other Financial Institutions (SUDEBAN). Díaz says that these were the fastest growing sectors, outstripping construction, mortgages and tourism. Profits obtained in the last half of 2006 were 23.23% higher than in the preceding half year, and for the third quarter of 2006, profits grew 21.94% from the same period of 2005.

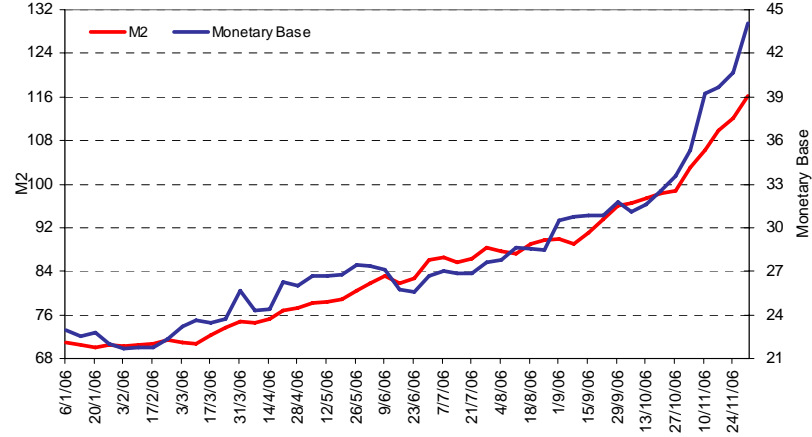
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ECONOMIC OVERVIEW

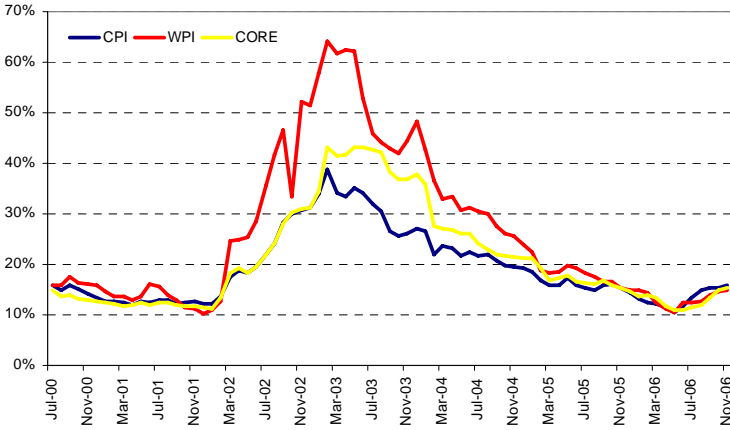
Oil Price
(Venezuelan Basket US\$/pb)



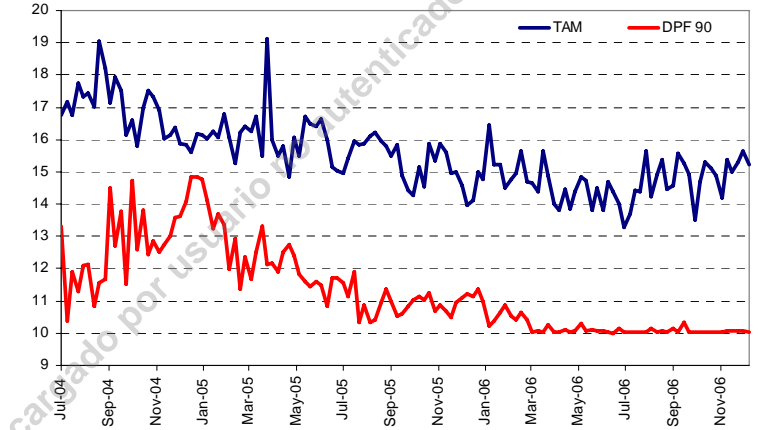
Monetary Base & M2
(VEB Billions)



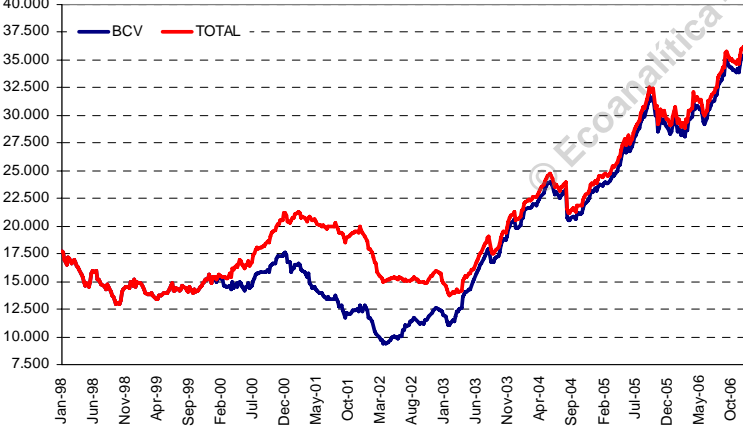
Inflation
(Last 12 Months)



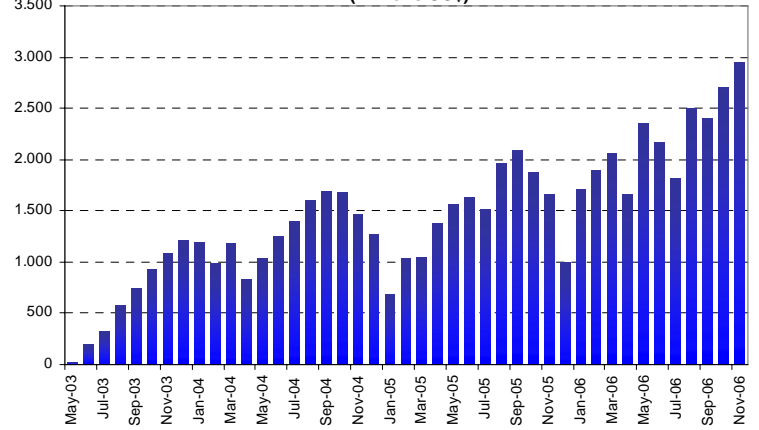
Interest Rate
(Six Principal Banks)



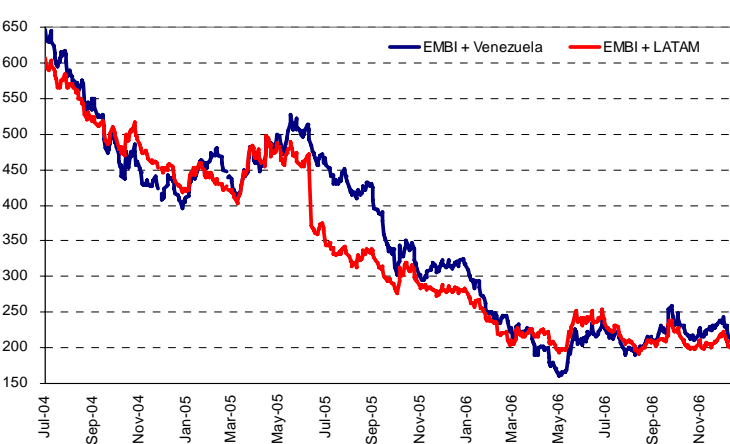
Fx Reserves
(Millions US\$)



Disbursement
(Millions US\$)



EMBI



Central Government
(VEB Billions)

