

## The reserves requirement: the new regulator

In just four months, the Venezuelan Government has ordered an increase in the banking requirements that financial institutions in Venezuela are required to maintain in the Central Bank of Venezuela (called the “reserve requirements”). First and foremost, this type of adjustment has to do with the Central Bank’s intention to curb the flow of bolivars exacerbated by hyperinflation and by its apparent shortage of options for dealing with it in a context of declining foreign currency revenues.

However, if we look at this in a more historical context, the reserves requirement has affected the credit activity of banks in Venezuela; and those credits have served as a counterweight for the revenues available to households and companies for buying goods and services, including foreign currency. So, it seems that the effects of this measure are not limited to the sphere of banking alone.

Since foreign exchange controls were introduced in 2002 and up to the present with the new hyperinflationary situation we are facing, credit has been a fundamental element in the budgets of households and companies. Even with the differences compared to the role of the banks in more developed economies, where credit activity plays a predominant role in the real economy, Venezuela has relied on credit for commercial activity and consumption. Bearing that in mind, it is not harebrained to think that, besides the monetary effects typical of a policy geared to restricting liquidity, intensive use of the reserves requirement as a means of monetary control could generate more misfortunes for the already hard-hit local economy.

### What is the reserves requirement?

Basically, the reserves requirement consists of the deposits or reserves that financial entities have in the central bank. It is a measure available to the monetary authorities for regulating the circulation of money in an economy. These funds come, in turn, from the money that households and companies deposit in the banks. So, since the banks make use of said deposits in order to lend, an increase in the reserves requirements inevitably results in the banks lending less.

While it is usual in barely developed markets for the reserves requirement to be used only in the sphere of monetary policy, its impact on credit activity has encouraged its use in other spheres of regulation.

An example worthy of note is how, following the overexpansion of credit prior to the 2008 *subprime* crisis, use of the reserve requirement has mutated and become popular in some economies as a macro-prudential tool or, put more simply, as a means for preventing the aggressive expansion of banks' balance sheets. This seeks to minimize the banks' losses when, in the middle of recessive cycles, lending results in problems of solvency. On occasions, small and open economies turn up to reserve requirements to halt monetary excesses, without modifying interest rates that may impact broad capital flows and local goods' competitiveness compared to foreign goods<sup>1</sup>

In Venezuela's case, the financial institutions are currently subject to five types of reserves requirement<sup>2</sup>: a base or ordinary reserve from 31% of the banks' liabilities subject to this requirement; the marginal reserve, calculated as 60% of the variations in said liabilities compared to a benchmark value; and a special reserve, from 100% in the change of the deposits maintained voluntarily by the banks (classified as surplus reserves).

Then there are two additional reserves used as punishments for failing to comply with the previous requirements or for errors in supplying information, which consists of the shortfall amount valued at the interest set for the Central Bank's mop-up operations (with some caveats), and 1% of the bank's assets on a given date, in each case. The Central Bank's last resolution of 2018 includes yet another, sixth, type of reserve consisting of a "fixed" reserve of 50,0% on the amount maintained as the special reserve in December.

<sup>1</sup> A useful summary about the nature and design of reserve requirements in various countries is found in Federico, P; Vegh, C y Vuletin, G (2014): Reserve requirement policy over the business cycle. NBER working paper 20612; además de Brei, M & Moreno, M (2018): Reserve requirements and capital flows in Latin America, BIS working paper 741.

<sup>2</sup> Considering special requirement abolished on January 22th of 2019. Likewise, it includes a special reserve of 12% of total liabilities (and their variations respective with a base amount), applied only to microfinancing banks that register a credit portfolio over 70% of their weekly deposits.

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**Summary of the reserves requirements modifications**

Application date	Measure	Operative definition	Total reserve requirement
21-Jan-19	Elimination of the especial reserve requirement	-	TRR = ORR <sub>t</sub> + MRR <sub>t</sub> + Sanctions
14-Jan-19	Marginal reserve requirement increase 3	$MRR_{4t} = 0,6 * (D_t - D_{28 \text{ sep } 2018})$	TRR = ORR <sub>t</sub> + MRR <sub>t</sub> + ERR <sub>3t</sub> + Sanctions
	Especial reserve requirement 3	$ERR_{3t} = (ER_t - RE_{31 \text{ aug } 2018}) + (0,5 * ERR_{28 \text{ diciembre } 2018})$	TRR = ORR <sub>t</sub> + MRR <sub>3t</sub> + ERR <sub>3t</sub> + Sanctions
4-Dec-18	Especial reserve requirement 2	$ERR_{2t} = \{ER_t - 0,8 * (ER_{31 \text{ aug } 2018})\}$	TRR = ORR <sub>t</sub> + MRR <sub>3t</sub> + ERR <sub>2t</sub> + Sanctions
30-Nov-18	Marginal reserve requirement increase 2	$MRR_{3t} = 0,5 * (D_t - D_{28 \text{ sep } 2018})$	TRR = ORR <sub>t</sub> + MRR <sub>3t</sub> + ERR <sub>t</sub> + Sanctions
22-Oct-18	Marginal reserve requirement increase 1	$MRR_{2t} = 0,4 * (D_t - D_{28 \text{ sep } 2018})$	TRR = ORR <sub>t</sub> + MRR <sub>2t</sub> + ERR <sub>t</sub> + Sanctions
	Ordinary reserve requirement increase	$ORR_{2t} = 0,31 * D_t$	TRR = ORR <sub>t</sub> + MRR <sub>t</sub> + ERR <sub>t</sub> + Sanctions
3-Sep-18	Especial reserve requirement (ERR) 1	$EE_t = RE_t - RE_{31 \text{ aug } 2018}$	TRR = ORR <sub>t</sub> + MRR <sub>t</sub> + ERR <sub>t</sub> + Sanctions
31-Dec-17	Marginal reserve requirement (MRR)	$MRR_t = 0,31 * (D_t - D_{28 \text{ sep } 2018})$	TRR = ORR <sub>t</sub> + MRR <sub>t</sub> + Sanciones (*)
	Ordinary reserve requirement (ORR)	$ORR_t = 0,215 * D_t$	

TRR: Total reserve requirement, D: Total Obligations and net investments, ER: Excedentary reserve (Total reserves - Total reserve requirement)

By the politics desing, the reserve requirement of every week corresponds to the average of the total obligations and net investments reported to weeks before.

(\*) In this case, the sanctions involves the especial requirements and the penalty requirements

Sources: Ecoanalítica, Venezuela's Central Bank resolutions

Setting aside the latest changes in the reserve regime, the adjustments to the regulation mechanism revealed several peculiarities. Up until last week, we were not only talking about larger percentages of liabilities subject to reserve, but also the Central Bank's access to a larger portion of the voluntary reserves. That is the case of the special reserve, where the funds should made up from the average daily variations in those reserves.

**Reserve requirement ratio (2000 - 2014) <sup>1/</sup>**

	Demand deposits	Saving deposits	Term deposits
Argentina	18.7	18.7	12.4
Brazil	45	18.6	15.3
Chile	9	3.6	3.6
Colombia	12.4	12.4	12.4
Mexico	6.4	6.4	6.4
Peru	11.2	11.2	11.2
Uruguay	18	9	4

<sup>1/</sup> Average per country, for depositors in local currency.

Sources: Brei &amp; Moreno (2018) and Ecoanalítica

These characteristics seem to be very different from what happens internationally, where the reserves requirement is traditionally tied to a bank's liabilities and not directly to its assets (the reserves). Given that the demand for these surplus reserves usually responds to incentives unrelated to regulation, this design speaks to us of a more interventionist

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policy with regard to the availabilities of funds for the banking business, with potential credit cuts to the public being their most extreme expression.

### **Credit and reserves requirement: What has happened in Venezuela?**

The reserves requirement reduces first of all the funds available to the banks for expanding their balance sheet, including increasing credit, at least in theory. So, since it represents the deposits that commercial banks must maintain indefinitely as a reserve with the central bank, an increase in said reserve means a reduced supply of loans and, consequently, steadily shrinking creation of secondary money.

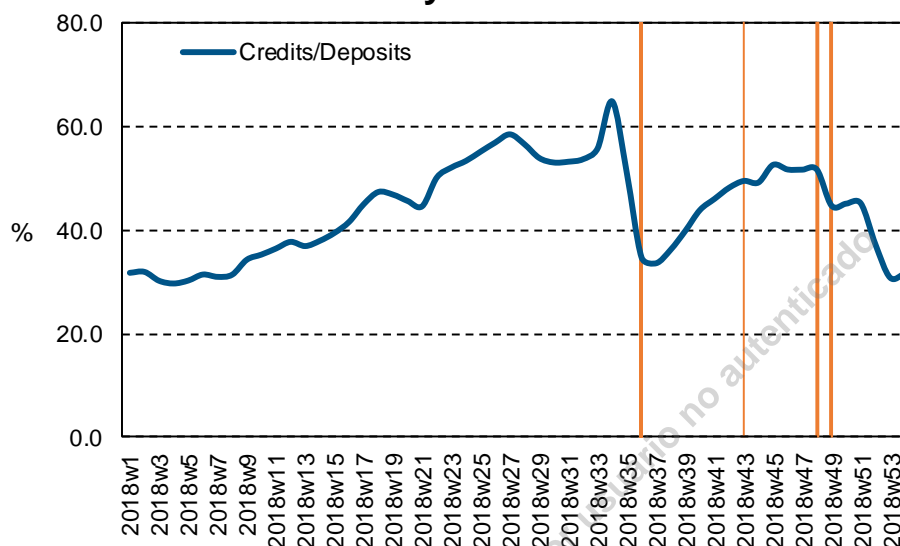
On the other hand, the reserves make it more expensive for the general public and companies to capture the banks' resources. Imagine a bank that has to hand over two out of every three bolivars of its deposits to the central bank. Under this scheme it would only lend one third of what it obtains. In countries with low or nonvolatile inflation, paying interest on three units when in effect only one unit is lent can reduce what the banks receive in net terms (remember that the banks usually charge a higher rate of interest on their loans than the rate they pay on their deposits). In hyperinflation, the drop-in net returns are even more acute. With those profit levels, it would not be attractive for the banks to accept more deposits, which means they would have less lendable funds available.

Bearing in mind the current context in Venezuela, the recent reserve measures taken by the government would seem to seek to reduce the monetary surpluses that are putting pressure on local prices, even though this is at the expense of less credit. The increased reserve requirement established at the beginning of the so-called "Economic Recovery Plan" seem to have had an effect on local credit activity. The banks went from weekly giving up just over three bolivars for every ten received in deposits, after having lent up to more than six bolivars for every ten following the establishment of the new special reserve in August.

After a slight recovery in credit activity, the new marginal reserve measures put forth between August and November also meant another drop in the intermediation (credits over deposits) ratio in the last months of the year. So, it seems that the government realized that the effects of the first reserves were short-lived (usual in a hyperinflationary environment) and implemented this new reserve measure.

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### Weekly intermediation

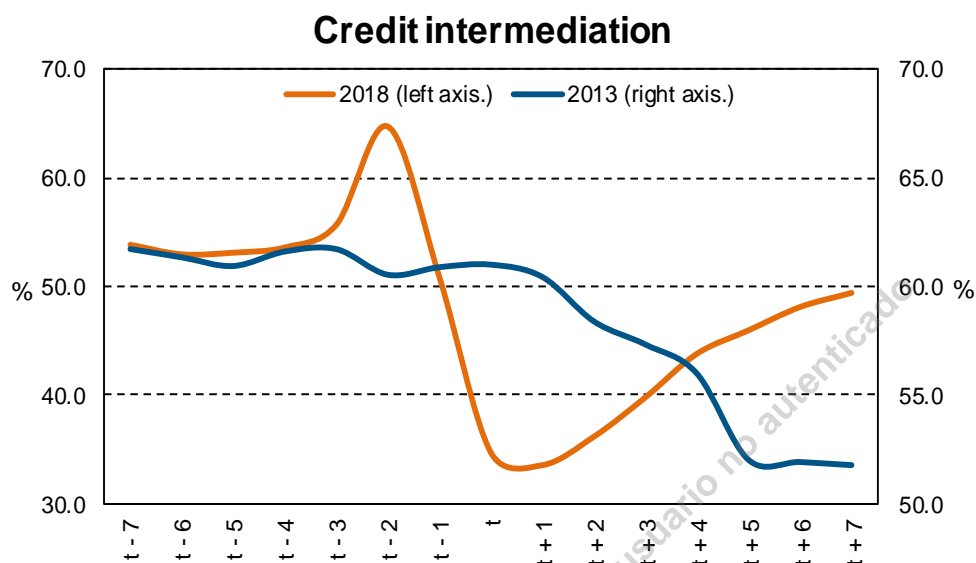


Sources: BCV and Ecoanalítica

Could it be that this response on the credit front was triggered exclusively by the increase in the reserve requirement or the introduction of new reserves? Given that possibility, it is worth evaluating the weekly credit dynamic following the changes in the reserves requirement during other periods not affected by hyperinflation<sup>3</sup>. If we take what happened in 2013, when both marginal and ordinal reserves coefficients were elevated by 8 percentage points, credit showed a similar dynamic, although less extreme. This suggests that through 2018 reserve requirement seemed to restrict intermediation, at least in part, regardless of the remaining measures (indexation to the Petro and the increase in the minimum wage, among others), even if briefly.

<sup>3</sup> Like the event analysis, a timeframe "t" was fixed as the period where a change in reserve requirement came into effect, evaluating the variable's behavior in a window of seven period before (t-1, t-2,...) and after (t+1, t+2,...) of said measure.

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Sources: BCV and Ecoanalítica

### Less loans, lower exchange rate?

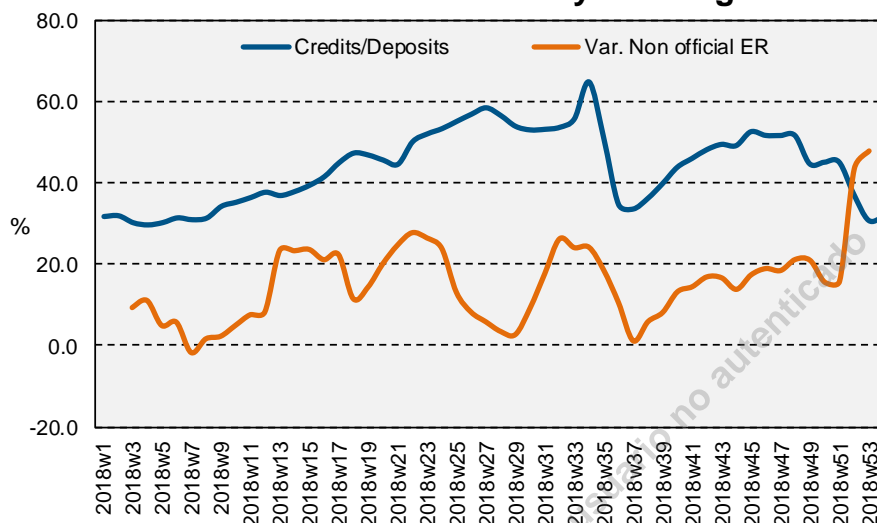
The first changes in the reserves requirement in 2018 were accompanied by an adjustment in the foreign currency market. After a devaluation of the official exchange rate following indexation to the value of the Petro, the exchange rate was adjusted to the new official rate and then showed slower adjustments as credit activity was adjusted to the changes in the reserve requirements. An explanation for these results is that the increase in reserves requirement managed to discourage the banks from supplying funds, which meant that households and companies had fewer resources available for acquiring goods and services, including coverage in foreign currency.

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### Intermediation and weekly exchange rate



Sources: BCV & Ecoanalítica

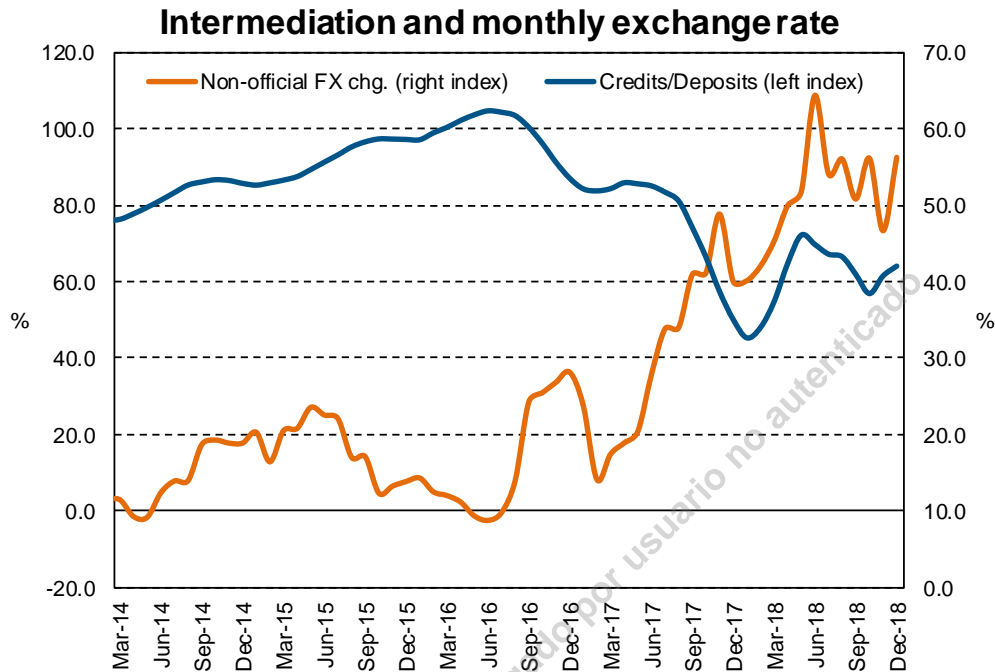
A brief linear estimate<sup>4</sup> reveals that, in effect, the foreign exchange events in 2018 were partially explained by credit activity. Our findings show that, on average, for every additional percent in deposits allocated to loans each week, the unofficial exchange rate tended to go up by approximately 2,9%. Nevertheless, we are talking about a situation that only existed in 2018 (especially during the second semester), which means that it is worth taking a look at this ratio from a more historic standpoint.

A look at the history of the relationship between credit and the exchange rate tells us little. Not necessarily in all the episodes in which the reserve policy was changed did the exchange rate adjust itself as a consequence. As a matter of fact, 2017 saw falls in intermediation alongside higher depreciation pressure. Even so, this invalidates the relationship between pressures in the credit market and the rate at which foreign currencies are traded. It speaks to us rather of a new reality where, with a currency that enjoys less credibility by the day and money that has ever more explosive effects on prices, any circumstantial event that affects monetary conditions directly (including bigger or smaller reserves) has a greater influence on the exchange rate dynamic.

<sup>4</sup>Based on a linear regression model, in which the weekly unofficial exchange rate through 2018 is explained by local inflation, intermediation ratio, amounts assigned by DICOM foreign currency auctions, monetary liquidity (M2), with controls for linear trends and exchange rate overreaction to August's economic measures. Likewise, we controlled for potential endogeneity of prices to exchange rate, using second lags as instruments. Results did not change under a dynamic specification.

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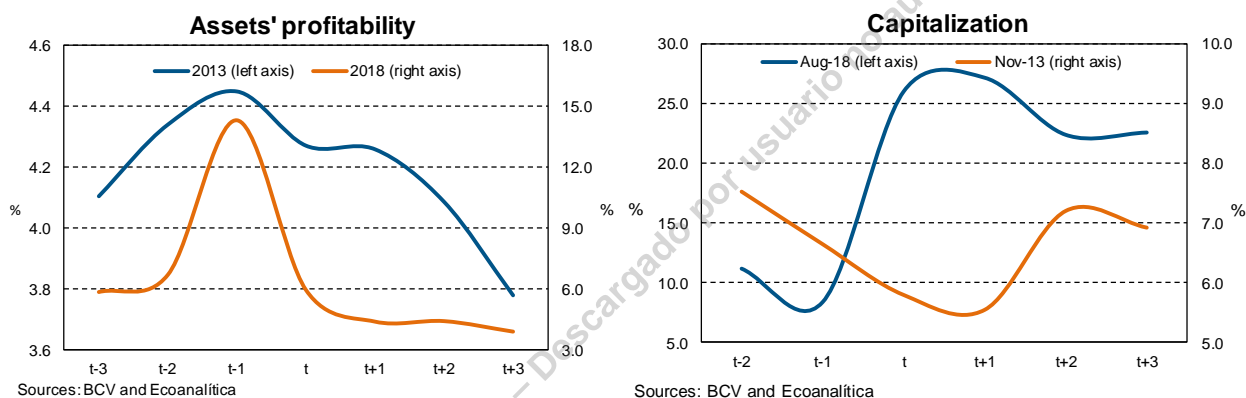
Sources: BCV, Dólar Bitcoin and Ecoanalítica

This notion of transiency in reserve requirement effects is crucial for the measurement of its potential impacts, especially if we consider that, amidst hyperinflation, such requirement constitutes a tool with short reach to steadily mitigate the bolivar's very low credibility as a value reserve, or the impacts from regulatory and policy misses. As an example, a button: while intermediation levels for January's second week fell to 31,4% of deposits, the unofficial exchange rate was 1,5 times its previous week value, in the midst of political tensions and regulatory uncertainty. As such, we speak of changes in credit (forced by reserve requirements) apparently innocuous for the currency market.

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## The banks: prey or predators?

By discouraging the banks from capturing more deposits, a reserve can affect credit activity as a generator of revenues. Fewer loans mean reduced profitability and, consequently, a deterioration in the banks' net worth in the medium term. With a scheme of controlled interest rates, hyperinflation not only makes the drop in revenues sharper, it also exposes the banks to non-payments that could have been met with precisely those funds. If we add the effects on net worth and revenues, the capacity of the banks for honoring their debts with third parties –or what is usually referred to as bank stability- is affected.



If we take these this scale of things in the context of the changes in the reserve requirements between 2013 and 2018, we find that, in 2013, the banking system managed to keep its capitalization levels (presumably by disincentivizing deposit accumulation). Following the first reserve requirement adjustment of 2018, bank's capitalization was reduced two months hence, in the middle of an intermediation downward thrust that, as we inferred previously, came linked to such changes in reserve requirements.

Although in 2013 there was a reduction the month following the establishment of more rigid reserve requirements, in terms of magnitude such fall didn't surpassed the capital spoilage in hyperinflation. Banks' profits also seems to be reduced in the face of 2018 reserve changes in larger magnitudes than compared to 2013's requirements, particularly after three months of setting such measures.

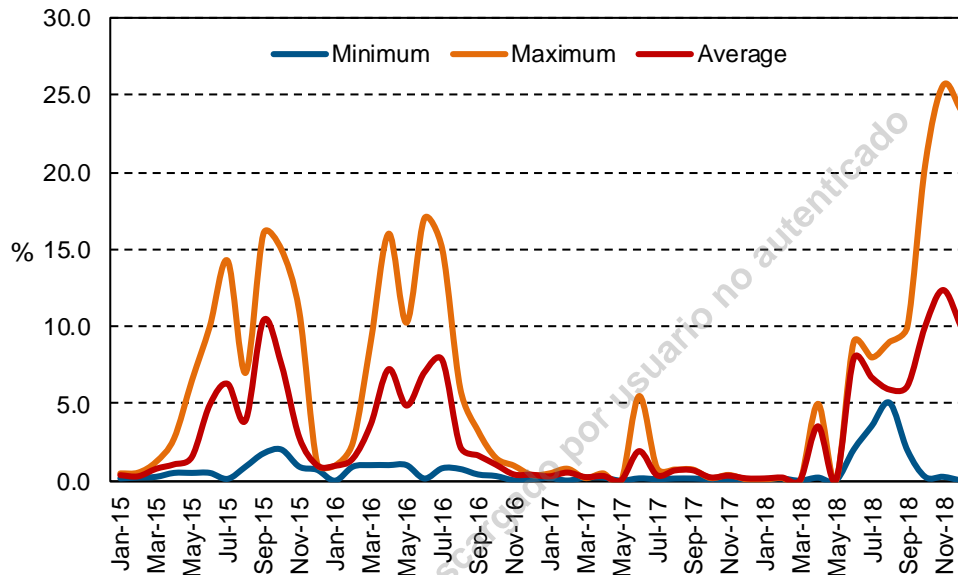
On the other hand, we find more hectic interbank activity as the new reserve conditions were implemented. It should be remembered that, whereas the marginal and ordinary reserves are set and paid weekly, the new special reserve was calculated and accumulated daily. This resulted not only in a greater volume traded between banks compared to other months, but also in making the loans obtained in those funds more

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expensive. The overnight rate hit new historic highs as a result of the increased demand for funds.

### Overnight rates



Sources: BCV and Ecoanalítica

Specifically, the banks resorted more to obtaining resources (reserves) from other banks at the end of each week, when they had to make up the reserve requirement. It was precisely during these periods when the agreed yields rose more sharply. With lending rates of no more than 28 percentage points, the increase in interbank yields posed new difficulties for getting together funds to overlap the drop in the banks' availabilities following implementation of the new reserves.

Added to the drop in credit, the foregoing suggests how banking could be seriously affected, not only in terms of what is tacitly revealed on their balance sheets, but also in terms of their capacity to take on more borrowing and, thereby, contribute to improving the performance of the local economy.

This could be no small thing for the local market. Even when exchange controls restrict the banking business, we are talking of a sector that is as small as the economy itself. So, a reduced banking balance sheet in historical terms does not restrict the potential role of credit in the real economy under present conditions.

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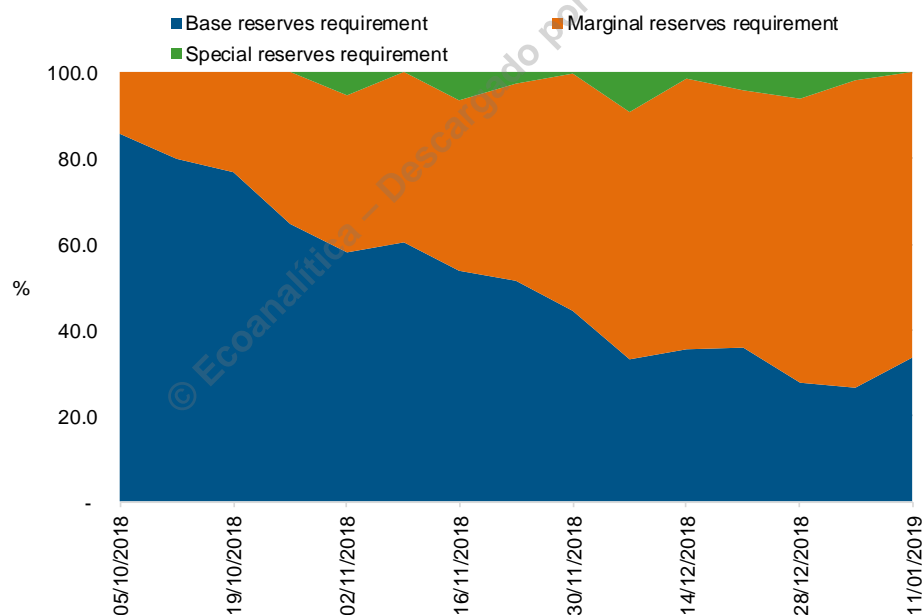
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## Getting rid of the special reserve

This week, the Central Bank of Venezuela sprang yet another “surprise” on the regulatory front when it decided to repeal the special reserve implemented in August last year and return to the traditional scheme of ordinary and marginal reserves.

The elimination of this reserve hides several things. In our weekly report number 35, we offered, among other things, a brief analysis of the then recent reserves requirement measure set by the Central Bank in an attempt, according to the government’s rhetoric, to curb the monetary surpluses behind local hyperinflation. In this report we pointed out that the measure would not be very effective on those terms, if that environment discouraged the build-up of voluntary funds in a context of a sharp increase in prices. Time (and hyperinflation) would prove us right.

### Composition of the weekly reserves requirement



Sources: BCV and Ecoanalítica

Following the elimination of this measure, what seems to be in play is not greater willingness on the part of the government to improve credit but rather the little relevance of the special reserve compared to the other requirements. Since the surplus reserves are only one part of the banks’ deposits in the Central Bank, which, in turn, come from a percentage of the general public’s deposits, the calculation base is much smaller than that of the other reserves, which are calculated based on total deposits (levels or differences). So, as we argued in our previous report, as the increases in prices speed

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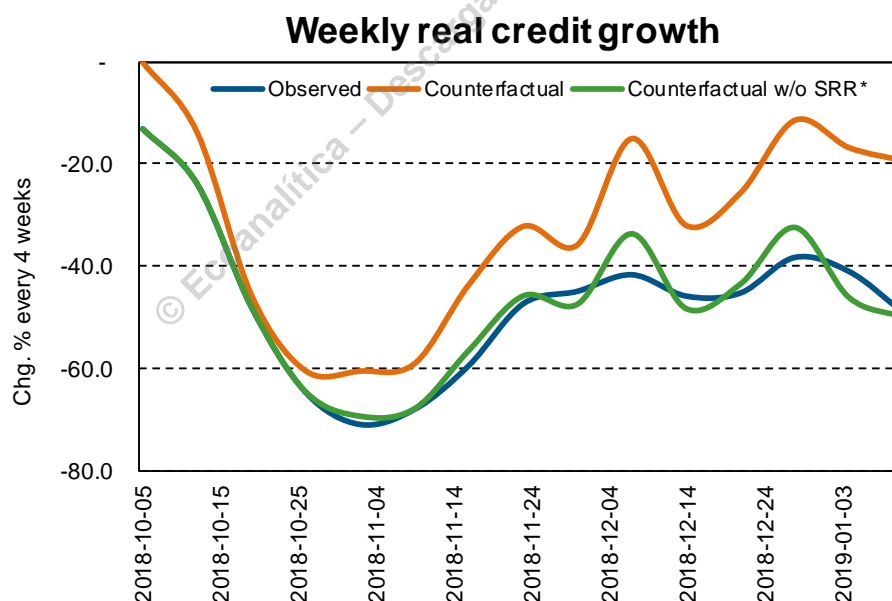
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up, that voluntary part of the reserves will be progressively less and the reserves requirement from this will be less. Therefore, it seems that the government has given way on the fraction of the reserve that is expected to have less impact on the future supply of loans.

### A brief counterfactual exercise

As a way of evaluating the impact of the reserve on credit, we performed a brief exercise that seeks to identify the potential reduction in loans following increases in the reserve requirements. To do this, we reproduced the calculation of the so-called reserve position from the sum of the amounts associated with the ordinary and marginal reserves. We omitted the punitive reserves given their little relevance. We assumed that the liabilities subject to reserve are made up exclusively of deposits by the general public.

Based on this calculation, we determined the level of net deposits available for lending (deducting the reserve) versus the expected level in the absence of the new reserve requirements.



Sources: BCV and Ecoanalítica

\*SRR makes reference to the special reserves requirement.

On the assumption that the banks still intermediate, based on what was observed in 2018, 45% of their deposits, we calculated the real variation in credit in both context. The results tend to reveal that credit fell by around 20 percentage points less in real terms than if the reserve measures had not been taken. By deducting the already repealed special

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reserve, we even find few changes compared to the benchmark case, which reaffirms the less important role of this type of requirement.

### Long live the reserves requirement?

Considering the recent measures taken by the Nicolás Maduro administration, it seems that the reserves requirement will continue to be a mechanism frequently used by the regulating authorities, given the government's short-sightedness that has contributed to the Venezuelan market entering a hyperinflationary scheme. As we have mentioned on several occasions, the Venezuelan Government seems to lack the technical tools (not to mention the will) to mitigate the macroeconomic imbalances we are suffering from.

The outlook is not good, which means that it is likely that it is we, the local agents (the banks with an even poorer performance and households/companies with less credit with which to leverage increased expenditures), who will continue to pay most of the cost of the present crisis. Consequently, it is up to us, as specialist analysts, to explain wherever possible the potential externalities following the mistaken or insufficient government measures (aimed ultimately at solving the economic crisis) that could be taken in the coming months.

**Luis Arturo Bárcenas**

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## WEEKLY INDICATORS

Weekly Economic Indicators			
	4th Week January	Weekly chg. (%)	Depre/Apre (pp) <sup>1</sup>
FX Dicom (VES/USD)	1,572.55	65.6	39.6
	2nd Week January	Weekly chg. (pp)	Annual chg. (pp)
Lending Interest Rate (%)	21.5	0.1	0.1
	3rd Week January	Weekly chg. (pp)	Annual chg. (pp)
Overnight Interest Rate (%)	17.7	2.9	17.7
	3rd Week January	Weekly chg. (%)	Annual chg. (%)
International Reserves (USD Bn)	8.4	-0.9	-12.3
	2nd Week January	Weekly chg. (%)	Annual chg. (%)
Monetary Liquidity (VES)	1,048,437,010	8.7	76,837.7
Price of International Oil Baskets (USD/bl)			
	3rd Week January	Weekly chg. (%)	Annual chg. (%)
WTI	51.7	2.9	-19.3
Brent	60.5	2.1	-13.0
Price of the Venezuelan oil basket (USD/bl)			
	3rd Week January	Weekly chg. (%)	Annual chg. (%)
Weekly Average	54.1	1.9	-11.6
Annual Average	51.7	2.4	-14.1

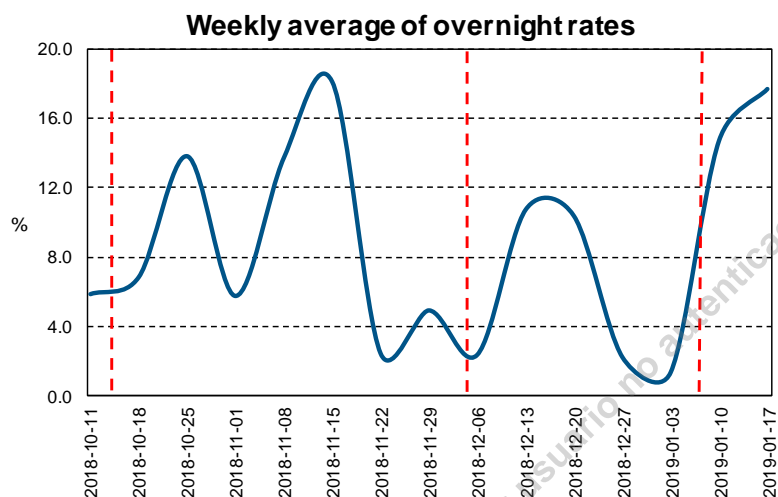
Sources: BCV, MENPET, ONT and Ecoanalítica

\* Annual variation of accumulated expenditure.

<sup>1</sup> Depreciation (+)/Appreciation (-)

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## GRAPH OF THE WEEK: “A BANKING SECTOR IN DIFFICULTIES”



Sources: BVC and Ecoanalítica

\*The lines show the announcements of the increase of the reserves requirement.

On January 8, the government raised the marginal legal reserve yet again to 60%. This requirement is basically the percentage of total deposits that must be maintained with the Central Bank of Venezuela. Along with the devaluations of the DICOM exchange rate and hikes in the minimum wage, raising the ordinary and marginal legal reserves has been one of the strategies used by the government to “deal with” the present economic crisis.

In order to understand the effects that these increases have on the economy, it is necessary to analyze their impacts on the banks and the overnight rates. These rates are negotiated on interbank operations, to which financial institutions usually resort for loans to temporarily cover their shortfall in liquidity. So, higher rates are associated with environments where the banks are experiencing major shortfalls in availability. In this context, an increase in the legal reserve restricts the banks’ liquidity, resulting in them resorting to the interbank market with increasingly higher rates.

The week following the three announcements of increases in the legal reserve, the overnight rates went up by 9.54 percentage points on average compared to the week of the announcement, an average increase of 470.4%. This indicates that the banks anticipated the future lack of availability and demanded funds at higher rates, an increase that got worse once each legal reserve went into force. Whatever the intention may be, raising the legal reserve seems not only to be ineffective, but also to generate additional distortions in the banking system and in credit activity heavily restricted by hyperinflation.

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## ECONOMIC TIPS

**One step forward, one step back.** The Central Bank of Venezuela's board of directors announced that it was repealing implementation of the legal reserve on surplus bank reserves starting January 22 this year, after evaluating the performance of the money market.

**Special legal reserve, part I.** Guidelines for implementing this legal reserve were set forth in *Gaceta Oficial* Number 41,560 dated January 9, 2019. According to the *Gaceta*, the banks have to keep *"an amount equal to 100% of the increase in surplus bank reserves as at the close of business on August 31, 2018, once the ordinary reserve fund has been deducted."*

**Special legal reserve, part II.** The *Gaceta* also established that this 100% applied after deducting *"50% of the special reserve amount constituted at the close of business on December 28, 2018."*

**Our international reserves.** The international reserves came to USD 8.43 billion on January 18, down 0.9% from the previous week, when they were at USD 8.51 billion (January 11). Year-on-year, the reserves have dropped by 10.7%.

**DICOM Auction No...** The exchange rate resulting from the last DICOM Auction, held on January 18, was VES 1,123.46/USD, which gives a devaluation of 10.8% compared to the previous auction on January 16. The devaluation so far this year, after only three weeks, is 37.3%.

**Disbursements are getting less.** It is worth noting that the amount disbursed fell significantly compared to the previous auction, from around USD 1.4 million to USD 306,979.8. This amount is also below the average disbursed over the past four weeks.

**Companies and private individuals.** Companies took the lead at this auction, receiving USD 225,843.2, 73.6% of the total amount auctioned. Private individuals, on the other hand, only got USD 81,136.6, or 26.4% of the total.

**On the increase.** The monetary base came to VES 603.84 billion in the week of January 11, 2019. This gives a weekly increase of 18.7% and a cumulative increase for the year to date of 38.7%.

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## OIL TIPS

**1.51 mb/d vs. 1.15 mb/d.** Even though reports of Venezuelan oil production from secondary and primary sources have always been different, in December, that difference was much greater. Primary sources gave a production of 1.51 million barrels a day (mb/d), whereas secondary sources put it at 1.148 mb/d.

**A difference of 362 kb/d.** The difference between the two figures casts doubt on the integrity and validity of the information provided by the Venezuelan Government, according to ArgusMedia. That same news portal states that Venezuela was able to halt the drop in its production thanks to the repairs carried out at the Jose facility.

**Behind the numbers.** Official figures also reveal that PetroMonagas, a company managed jointly by PDVSA and Rosneft, and Sinovensa, a company managed jointly by PDVSA and CNPC (China's state-owned oil company), added 30 kb/d to Venezuela's production in December. Production from PetroPiar remained stable. Based on these assumptions, ArgusMedia estimates that production in January will be 1.2 mb/d.

**What's the reason for the difference?** According to ArgusMedia's analysis, the official figures are inflated by factors such as the water cut, which creates a systematic difference between the operating figures reported by PDVSA's field managers and those measured by the Ministry of Oil. Field managers tend to exaggerate the numbers in order to make performance targets.

**Fuel theft.** Other factors affecting production are the lack of oil services and the thefts of petroleum and also of equipment from the plants that process the crude. ArgusMedia also explains that the production that goes directly to the domestic market can be easily altered and is much more difficult to detect.

**Winter is coming.** The United States Government is planning to impose new sanctions on Venezuela following the swearing-in of Nicolás Maduro as president on January 10, which they consider illegitimate, according to Reuters. The proposed sanctions include banning the exporting of refined products to Venezuela from the United States or restricting oil imports.

**Who will this affect?** US oil company executives met with White House officials to discuss the proposal. If imports of Venezuelan crude are reduced, US refineries would have few alternative sources of supply. Other crudes have been more difficult to obtain due to production cuts and reductions by Canada, Mexico and Venezuela itself.

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**Options on the table.** As for Barclays, it stated that sanctions could go from a ban on selling US diluents (used to blend crudes for export) to Venezuela to recognizing an alternative government to the Maduro administration, which would allow the international community to freeze Venezuela's assets and revenues.

**Other things in play.** S&P Global Platts reported that Venezuelan sources had said that the new US sanctions could have an impact on the renewal of the contract between PDVSA and Valero Energy, which expired on December 31 and is currently being discussed. According to a contract with ConocoPhillips, a contract with Valero should be established as part of the agreement on PDVSA's obligations with ConocoPhillips.

**Some have already withdrawn.** However, oil companies have not waited for the sanctions in order to stop buying Venezuelan crude. Royal Dutch Shell Plc and Phillips 66 stopped importing Venezuelan crude last year when the United States applied fiscal sanctions on PDVSA. This meant that Mexico became the biggest supplier of crude in the US Gulf, according to data from the Energy Information Agency (EIA).

**Explosion in Mexico.** Last weekend, a pipeline of Mexico's state-owned oil company, Pemex, exploded killing 21 and injuring many more. It is presumed that an attempt to steal crude caused the explosion. This situation has cast doubt on President Andrés Manuel López Obrador's ability to manage things, given that he had said that he would give priority to stopping the theft of crude.

## BUSINESS SECTOR TIPS

**Farming faces technical stoppage.** The first vice president of the Confederation of Agricultural and Livestock Producers Associations (Fedeagro), Celso Fantiel, warned of the serious situation farming finds itself in at the start of the year. He explained that only 10,000 hectares of rice had been planted this crop cycle, when no less than 70,000 hectares should have been planted.

**They'll only sell to Venezuela for cash.** Referring to the situation farming is facing as regards imports, he asked: "*How are we going to have that amount of fertilizers, agro-chemicals and seeds by the first half of January? It would be a truly titanic task to know whether they already have the cash... if they can pay the suppliers... because Venezuela no longer has any credit.*"

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**Problems with planting.** Apart from the numerous economic hurdles agriculture faced in 2018, Fantiel said they also had to cope with environmental problems that, because they were not dealt with correctly, cost farmers nearly 25,000 hectares of beans.

**We can't work like this.** The president of the Federation of Commerce and Production Chambers and Associations of Venezuela (Fedecámaras), Carlos Larrazábal, announced that a team from the International Labor Organisation (ILO) is to arrive in Venezuela on February 9 in response to reports of violations of workers' rights.

**The demise of companies.** Juan Pablo Olalquiaga, the president of the Venezuelan Confederation of Industrialists (Conindustria), warned of the possibility that 40% of the country's industries might not survive 2019. According to Olalquiaga, this would be due to the fact that *"the possibilities of operating in Venezuela are simply not there."*

**Industry's last hope.** Referring to industry's expectations for this year, Olalquiaga explained that Venezuela's industry is living in the hopes of a political change, since this is the only thing that *"has kept alive the hope of being able to keep our doors open."*

**A new industry.** The president of Conindustria presented the plan *"Towards an industrialized Venezuela."* He estimates that investment of USD 20 billion will be needed to get manufacturing back on its feet, among other things, not only in terms of its share of GDP but also as a contribution to the trade balance to reduce the country's reliance on oil.

**They're stealing cattle!** According to the president of the National Cattlemen's Federation of Venezuela (Fedenaga), one of the reasons for the increase in the price of beef is the constant confiscation of cattle by the state governments. In some cases, they are confiscating more than 30% of the cattle that enter the slaughterhouse.

**New shipping lines.** The US Company Shiplilly announced that it is to expand its operations to La Guaira and Puerto Cabello, linking up with numerous destinations around the world via the company's facilities in the Panama Canal.

**We're going to plant sugarcane.** Governor of Aragua Rodolfo Marco Torres announced that El Palmar sugar mill increased the area planted with sugarcane from 3,200 hectares to 3,800 hectares, from which they hope to produce 205,000 tons of sugar. It is expected that the area planted with sugarcane will be increased to 7,000 hectares by 2022.

**Mining apprentices.** According to Wuilkelma Ángel, the president of the National Training and Socialist Education Institute (INCES), the institute is focusing on expanding its training program to the mining sector *"from mining the mineral to processing it."*

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## WORLD ECONOMY TIPS

**The big forum at Davos.** Company chief executive officers and world leaders are to meet this week at Davos, Switzerland, for the World Economic Forum. The leaders of world powers such as the United States, France and England will not attend, opening the way for countries such as Brazil and China to transmit their message.

**A first step.** President Trump made his first offer for ending the shutdown that has lasted for more than four weeks. Although he did not back down regarding his demand for USD 5.7 billion for his wall, he did offer three years' protection for the dreamers (undocumented immigrants who entered the United States as children). The Democrats rejected the offer.

**Spies on your phone.** The US authorities plan to take the Chinese giant Huawei to trial for allegedly stealing trade secrets from US companies and using its products for spying. This could prove to be a setback for the meetings between Chinese and US officials that seek to put an end to the trade war.

**A three-decade low.** The Chinese economy has posted the lowest annual growth in the past 28 years. This situation, due mainly to fluctuating demand and US tariffs, is generating pressure on Peking for it to offer more incentives and to solve its trade dispute with the United States.

**Everything has repercussions.** This growing weakness of the Chinese economy, which has generated nearly one third of world growth in recent years, is causing concern regarding the world economy and proving detrimental to companies such as Apple and the big motor vehicle manufacturers.

**Plan B.** After her plan for Brexit met with a huge rejection, Theresa May now has to come up with another plan by March. Her main options include making sure of a bilateral agreement with Ireland that does not take the European Union into account.

**Disappointing outlook.** The International Monetary Fund (IMF) revised its growth forecast for Latin America for the third time in a row due to the continuing weakness of the emerging economies as a result of a reduced flow of capital from countries such as China. According to the IMF, the Latin American economy will grow by 2% this year.

**Banded.** The Central Bank of Argentina purchased USD 190 million on the foreign exchange market, maintaining a strict monetary policy that seeks to contain the peso

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between the established bands. To avoid exaggerated interventions, the Central Bank has undertaken to not buy more than USD 50 million a day in a bid to stabilize the exchange rate.

**Mexico suffers the consequences.** The Mexican peso depreciated as a result of an upturn in the dollar and the slowing down of the Chinese economy. The peso fell to MXN 19,174/USD, for a drop of 0.51%.

**Good news in Colombia.** Estimates by the Colombian Government indicate that Colombia's exports will go up by approximately 10% (USD 47 billion), thanks to better raw materials prices, the depreciation of the peso, and bigger sales of manufactured goods.

## POLITICAL TIPS

**The National Assembly “null and void.”** This Monday, January 21, Juan José Mendoza, the chairman of the Supreme Tribunal of Justice's Constitutional Chamber, declared all the National Assembly's boards of officers since the National Assembly was declared to be in contempt to be null and void. This decision covers the boards of officers appointed in 2017 (Julio Borges), 2018 (Omar Barboza), and 2019 (Juan Guaidó).

**Liability of the officers.** The representative of the Supreme Tribunal of Justice stated that the National Assembly is in contempt and that, therefore, its decisions are considered null and void. What is more, those who take those decisions could be held criminally, administratively, and civilly liable and would be investigated by the Public Prosecutor's Office.

**Does that mean no amnesty for the military?** The implications of this ruling include rendering the decisions taken by the National Assembly on January 15 invalid, among them the agreement that would grant amnesty to civilians and members of the military who restore the constitutional order, the agreement approving the entry of humanitarian aid, and the agreement for guaranteeing the protection of the Republic's assets.

**“You are the usurpers, not us.”** Resorting to a narrow interpretation of the Constitution, the chairman of the Constitutional Chamber stated that the National Assembly pretended to refuse to acknowledge the Judiciary, the Electoral Branch, and the Executive Branch, which would mean a usurpation of the functions of those branches of government and, therefore, violate Article 138 of the Constitution.

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**But there is amnesty with Guaidó.** Juan Guaidó, the president of the National Assembly, called the ruling handed down by the Constitutional Chamber of the Supreme Tribunal of Justice on January 21 “*a political absurdity*” and repeated the guarantees previously offered to civilians and members of the military. He also announced that the “*transition statute*” would be discussed at the session on January 22.

**Cotiza, a delicate situation (I).** On January 21, Cotiza, a low-income district of Caracas, awoke to gunshots allegedly caused by the uprising of a contingent of the Bolivarian National Guard. Later, these actions led to the start of a demonstration against the Nicolás Maduro administration by local inhabitants.

**Cotiza, a delicate situation (II).** Referring to the incident in Cotiza, the president of the Constituent National Assembly, Diosdado Cabello, claimed that the National Guardsmen who took part in the uprising had already been taken into custody, describing the situation as “*an attack on the Fatherland and its institutions.*”

**International support.** Ambassadors of the European Union met on Saturday, January 19, with the National Assembly’s board of officers to reaffirm their support and make their position known through the community’s foreign affairs spokesperson Maja Kocijancic, who called for “*new elections that are free and fair*” and also for “*the National Assembly to be respected, all political prisoners to be released, and the rule of law, human rights and fundamental freedoms to be observed.*”

**Asking to negotiate with Trump.** During an interview with the US news television channel Fox, the head of the Venezuelan Government Nicolás Maduro sent a message to his US counterpart with the intention of paving the way for dialog. He made this call arguing that they are both “*people with whom one can talk and negotiate.*”

**A new dialog.** Federica Mogherini, the High Representative of the European Union for Foreign Affairs and Security Policy, confirmed that a contact group made up of countries of the region could start working in February with the intention of “*contributing by providing a space for the political process which, at the moment, is lacking.*”

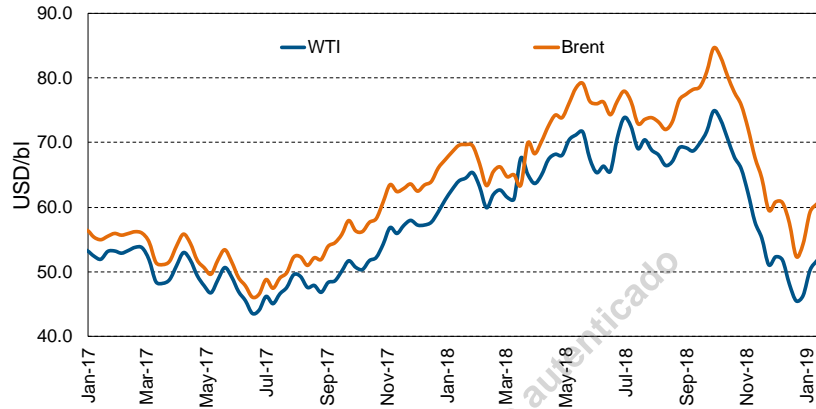
**Ladies and gentlemen, we have to talk.** The United States and six more countries, among them Brazil and Colombia, made a request for an extraordinary meeting of the Permanent Council of the Organization of American States (OEA) with the intention of addressing recent events in Venezuela. The meeting has been scheduled for Thursday, January 24.

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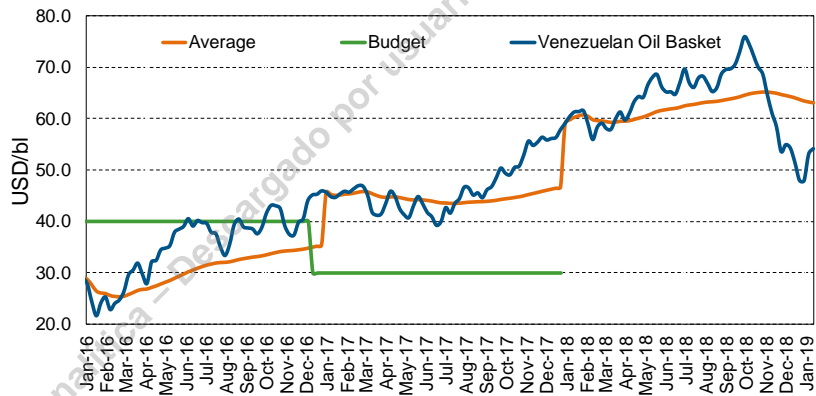
**ECONOMIC INDICATORS**

**Oil Prices  
(WTI and Brent)**



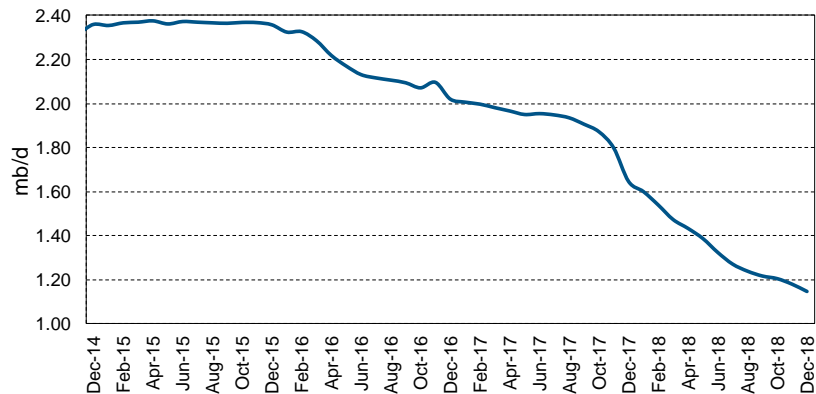
Sources: Menpet and Ecoanalítica

**Oil Price  
(Venezuelan Basket)**



Sources: Menpet and Ecoanalítica

**Oil Production  
(Secondary sources)**

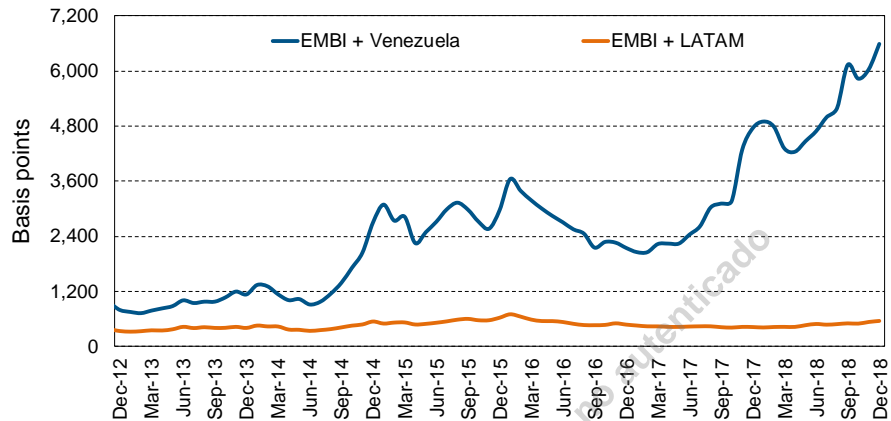


Sources: OPEC and Ecoanalítica

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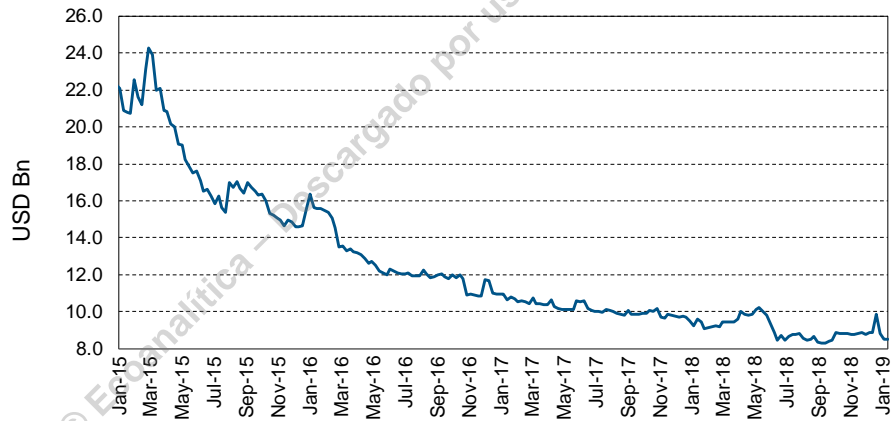
**ECONOMIC INDICATORS**

**EMBI**



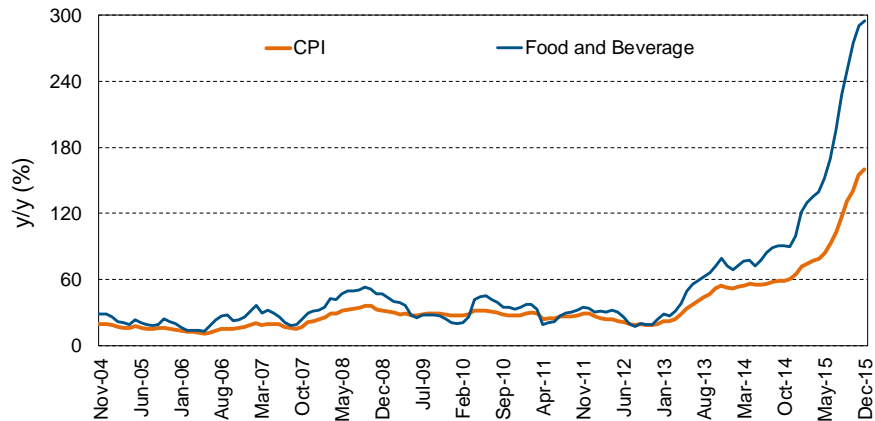
Sources: BCRP and Ecoanalítica

**FX Reserves (BCV)**



Sources: BCV and Ecoanalítica

**Inflation (BCV)**

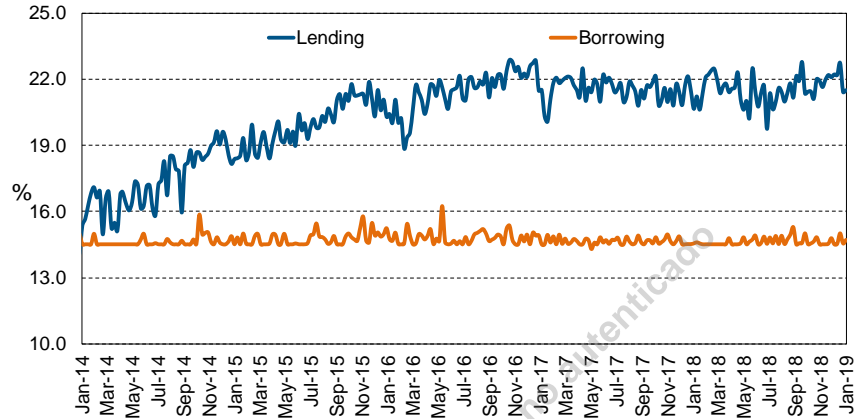


Sources: BCV and Ecoanalítica

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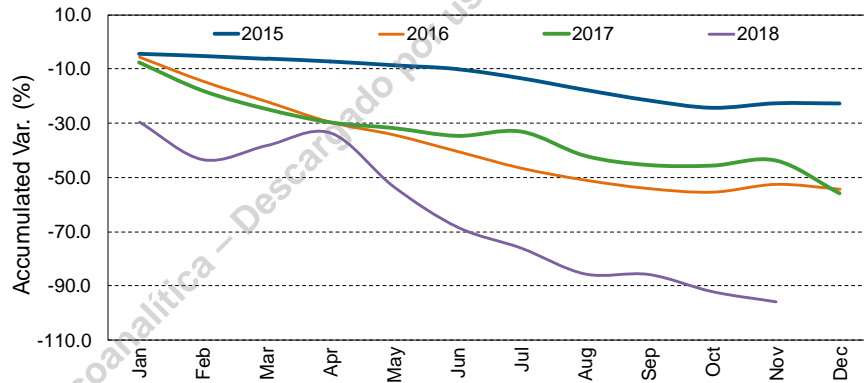
**ECONOMIC INDICATORS**

**Interest Rate  
(Six major banks)**



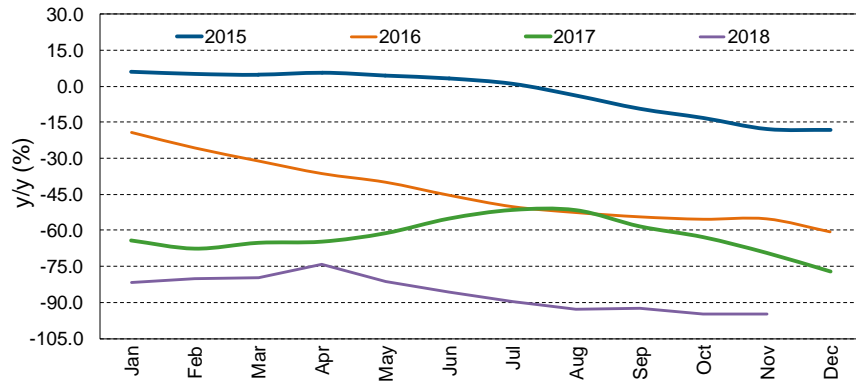
Sources: BCV and Ecoanalítica

**M2 Expansion  
(Real)**



Sources: BCV and Ecoanalítica

**Loan Portfolio  
(Real)**



Sources: SUDEBAN and Ecoanalítica

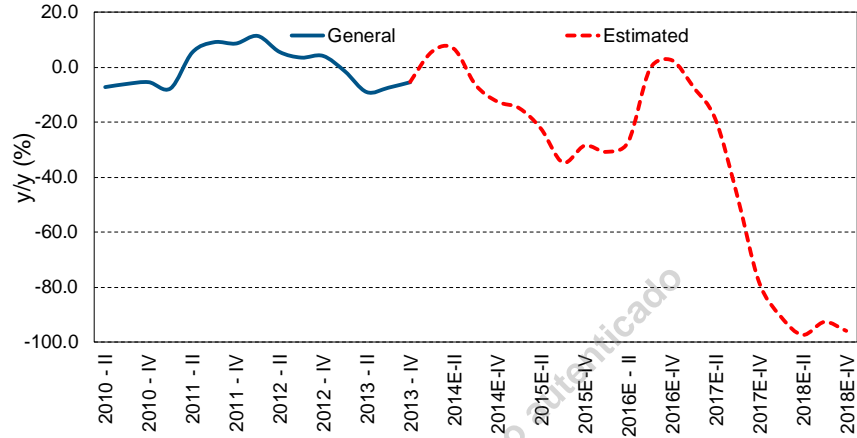
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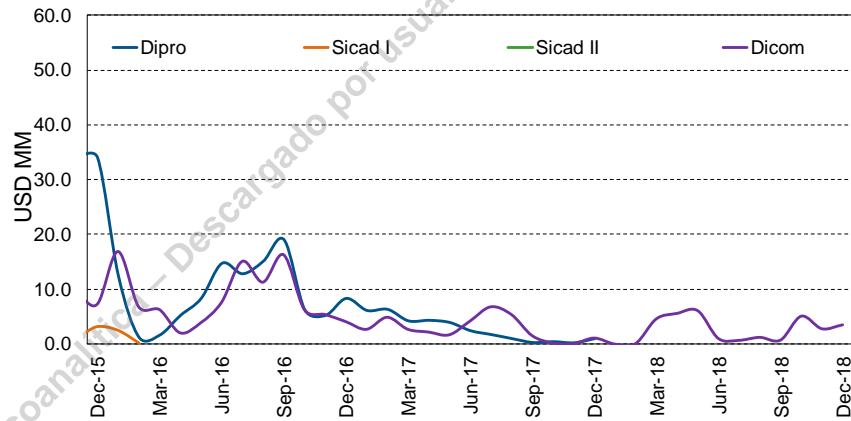
**ECONOMIC INDICATORS**

**Real Wage Index**



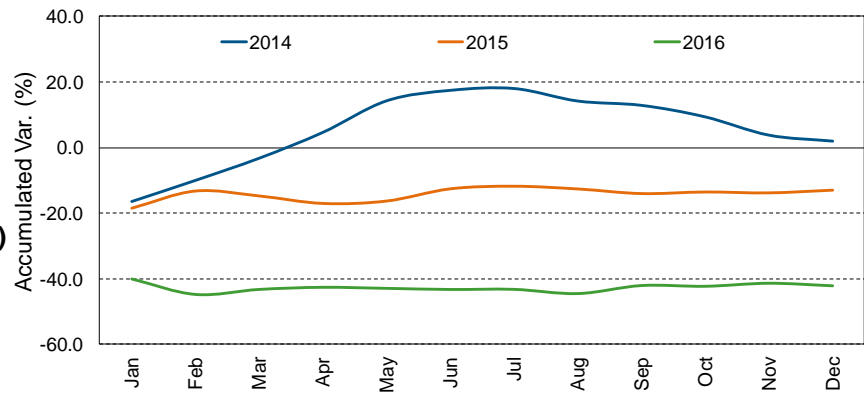
Sources: BCV and Ecoanalítica

**Disbursements to the Private Sector (Daily Average)**



Source: Ecoanalítica

**Primary Spending NTO (Real - Central Government)**



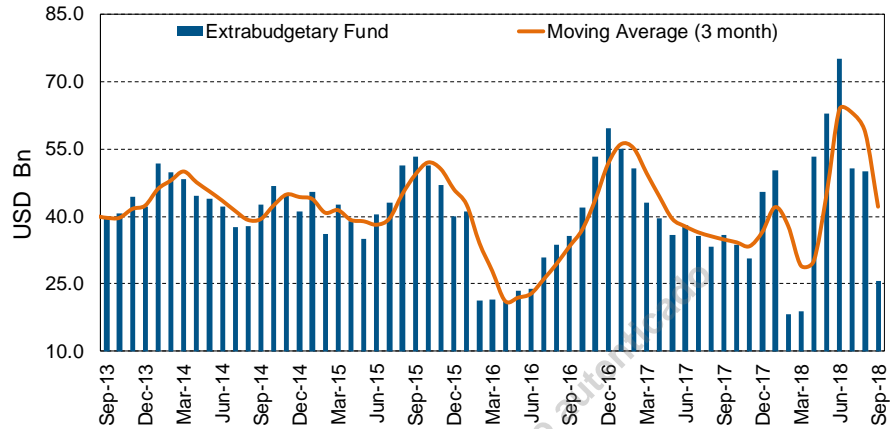
Sources: ONT and Ecoanalítica

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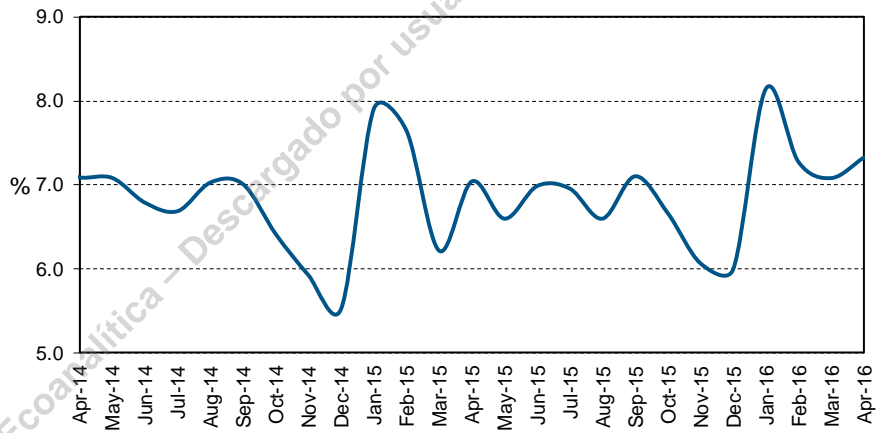
**ECONOMIC INDICATORS**

**State Extrabudgetary Resources**



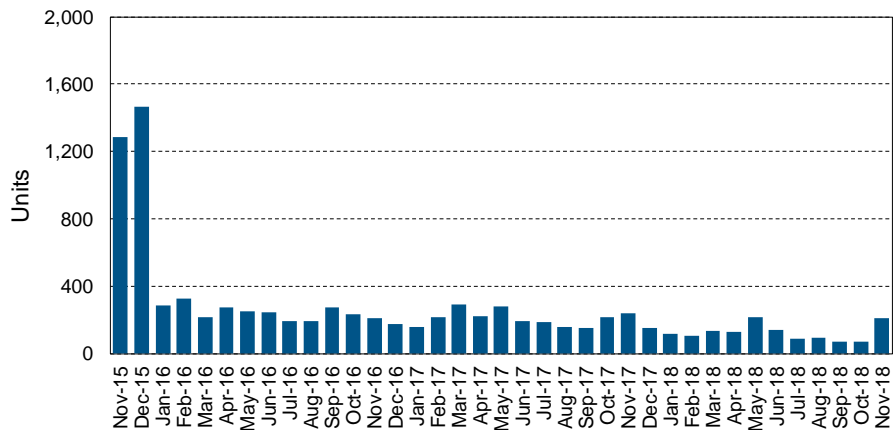
Source: Ecoanalítica

**Unemployment Rate**



Sources: INE and Ecoanalítica

**Vehicle Sales**



Sources: CAVENEZ and Ecoanalítica

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