



Weekly Report

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Exchange Controls, fiscal management, and inflation: Understanding how the 21st Century Socialist model is sustained

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This year makes it 10 years since the current exchange control system has been in place, and in response to this anniversary, there are a number of analysis being released explaining the impact this control has had on the performance of the Venezuelan economy. Also making the news are Venezuela's incredibly high fiscal deficit and the pressures that led inflation to increase significantly during the last few months of 2012. This Weekly Report will discuss and relate these three aspects.

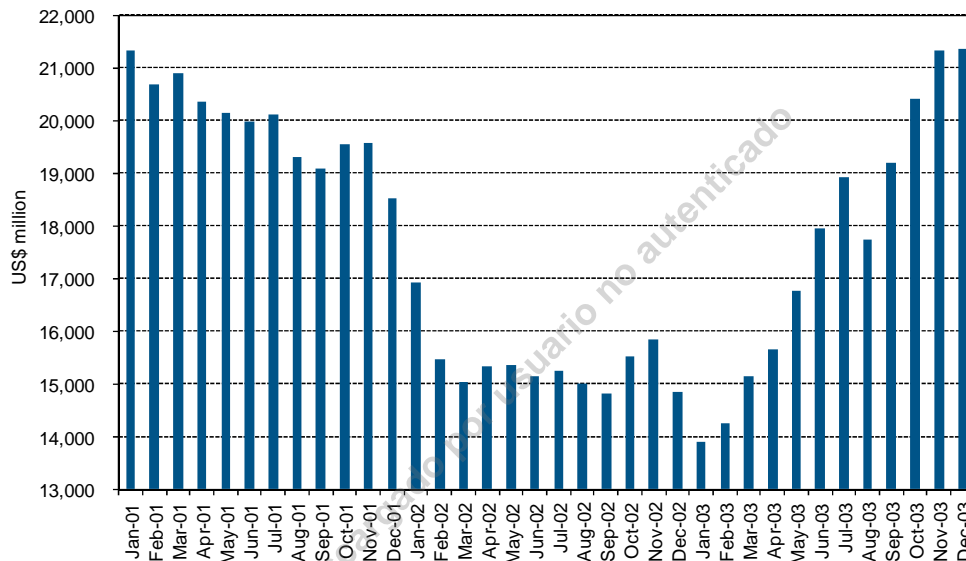
Why is the exchange control still being implemented?

In 2003, after the negative effects suffered by the economy due to the oil strike, which significantly compromised the country's main source of foreign currency, which in turn compromised Venezuela's foreign obligations, it was clear that the only valid solution to deal with the problems at hand was to implement a foreign exchange control. This measure was designed to be implemented temporarily, allowing enough time for the economy to reestablish its macroeconomic balance. In the



end, things turned out differently and it's been 10 years now and the control is still in place.

International Reserves 2001-2003



Sources: BCV and Ecoanalítica

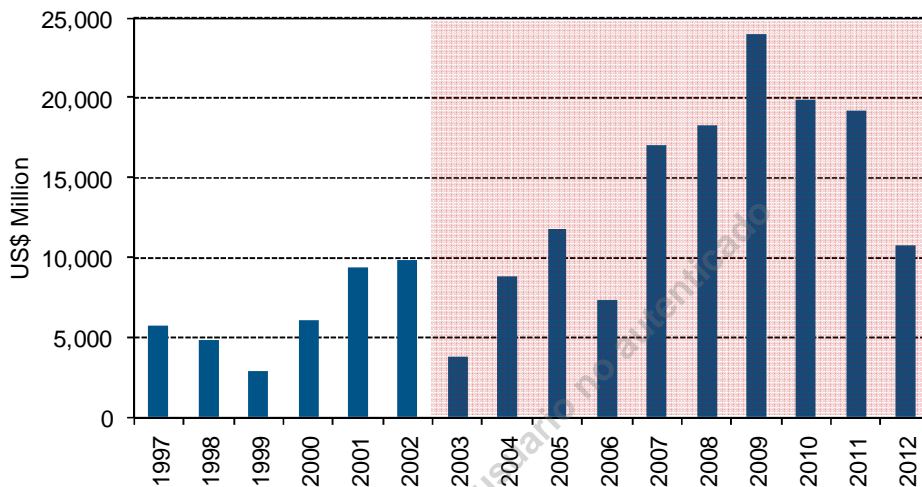
The chavismo movement, after the general strike, and then the attempted coup in 2002, was never the same. From their position in power, they became infected with a type of paranoia, where the private sector ceased to be a relevant player with respect to the economic development of the country, and became a political opponent, which in their minds, needed to be neutralized and dominated. So, in a country where the State controls more than 95% of all the foreign currency in the country, a foreign exchange control is the perfect tool to achieve such an objective.

Paradoxically, despite the fact that the exchange control limits the range and the capability for the Venezuelan private sector to engage in economic action, negatively affecting its competitiveness, it became a gold mine for moving capital out of the country. Between 2003 and 2012, private sector out-going capital from Venezuela totals around US\$ 140.69 billion. According to Barclays, this figure is on the conservative side, saying that the total amount surpasses US\$ 150 billion mark. This is a scandalous figure, especially if you take into account that between 2002 and 2007, private sector out-going capital only reached 109.01 billion.





Private Capital Outflow



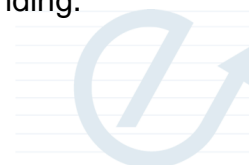
Sources: BCV and Ecoanalítica

Another reason is that...

With this mechanism in place, the chavista Administration is God and the Devil, all at the same time. On the one hand it is able to fence in the private sector with all the bureaucracy and restrictions involved for applying for the significantly subsidized foreign currency at the preferential official rate; and on the other hand it offers a mechanism by which the private sector can get significant amounts of resources out of the country. It has even led to the internationalization of the Venezuelan businessman throughout Latin America, especially in Colombia, Panama and Costa Rica.

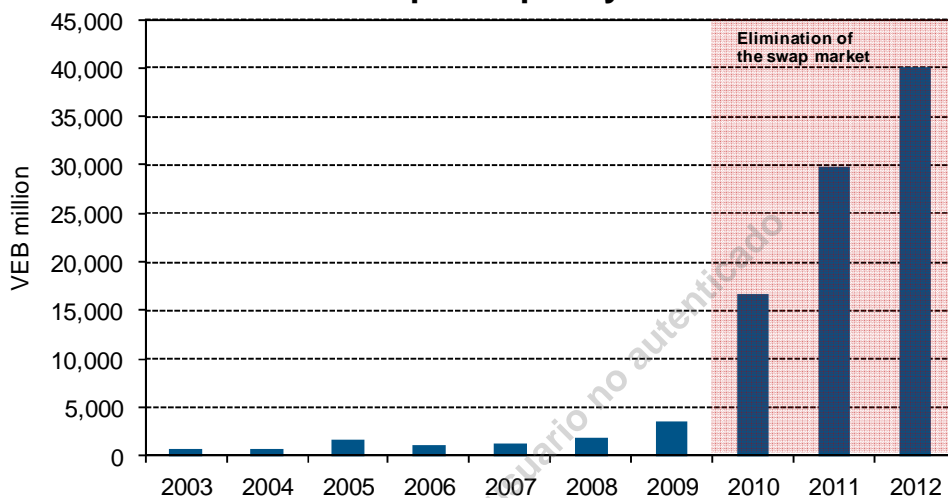
At **Ecoanalítica**, we feel that there is one more advantage that maintaining an exchange control affords the government and this is that it allows the Administration to maintain disorganized fiscal policies. It makes it easier for the Administration to finance the fiscal deficit that in other conditions (no exchange control mechanism in place), it would force the Administration to implement severe adjustments with respect to public finances.

In economic literature, this is known as financial repression. When there is an exchange control mechanism in place, surplus in the local currency, in this case the bolivar, increase significantly, since there is no freedom to legally acquire foreign currency. This surplus allows the Administration to issue debt, and thereby, finance a sustained increase in public spending.





Surplus liquidity



Sources: BCV and Ecoanalítica

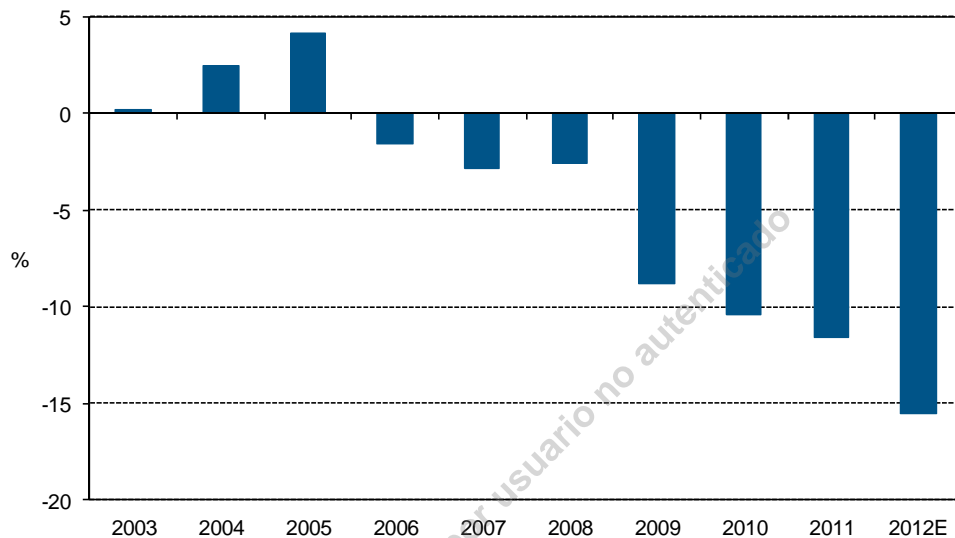
Since 2010, the situation became even more advantageous for the government since the swap-market that had been allowed to exist up to that moment was declared illegal. In 2009, swap-market foreign currency transactions reached US\$30.37 billion; by 2010, this now illegal trading was cut to US\$6.90 billion. This led to surplus bolivars increasing significantly leading to the Administration being more aggressive in the placement of domestic debt.

In 2003, the consolidated public sector registered a surplus of 0.2 percentage points of GDP in its fiscal balance, equivalent to US\$167 million. In contrast, at 2012 the consolidated public sector fiscal registered a deficit of 15.5 points of GDP, equivalent to US\$61.15 billion. 83.9% of this deficit was financed with domestic debt (in bolivars).





Fiscal Superávit/Déficit Restricted Public Sector



Sources: MPF and Ecoanalítica

Cheap debt

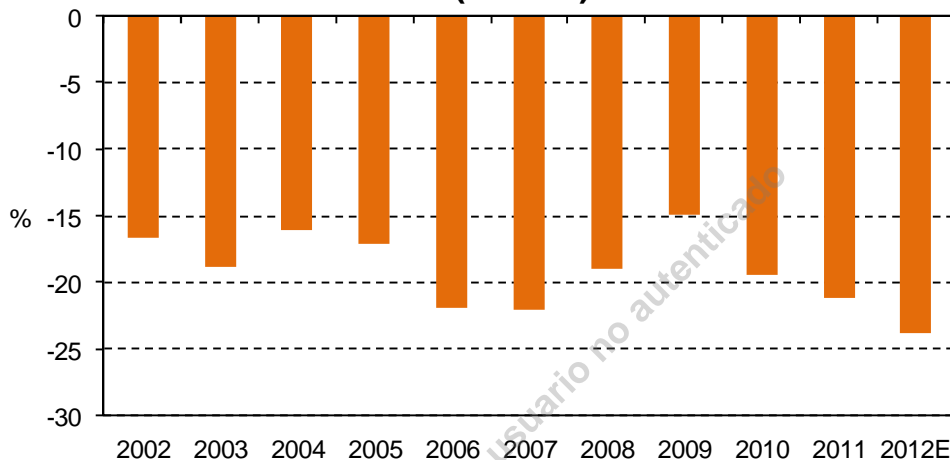
The evolution of the domestic debt allows us to visualize that in 2003, the domestic debt reached US\$15.03 billion and corresponded to 37.8% of the Central Government's consolidated debt. It reached a low point in 2008 when it settled at US\$14.19 billion or 32.2% of the total government debt. In 2012, the domestic debt represents 49.6% of the government's total debt or an amount equivalent to US\$42.92 billion.

The vulnerability of this policy can be seen through the non-oil fiscal balance, an indicator that measures the difference between non-oil revenue and total spending. In 2003, it was equal to 18.9 points of GDP. In 2012, it's equal to 23.7 points of GDP. In other words, this figure represents the part of spending that has to be financed with oil and issuing debt.





Non-oil Deficit of Restricted Public Sector (%GDP)



Sources: BCV and Ecoanalítica

And inflation?

Within a scenario of financial repression, out of control increasing public spending, and exchange distortions, it's clear that the inflation rate will reflect these problems.

Since 2003 to date, Venezuela's average yearly inflation rate has been 23.4%. For a number of years now, government spokespersons have heralding that the lowering inflation to a single digit is possible. In our opinion, with this economic model that the Administration is implementing, we do not believe that it is possible.

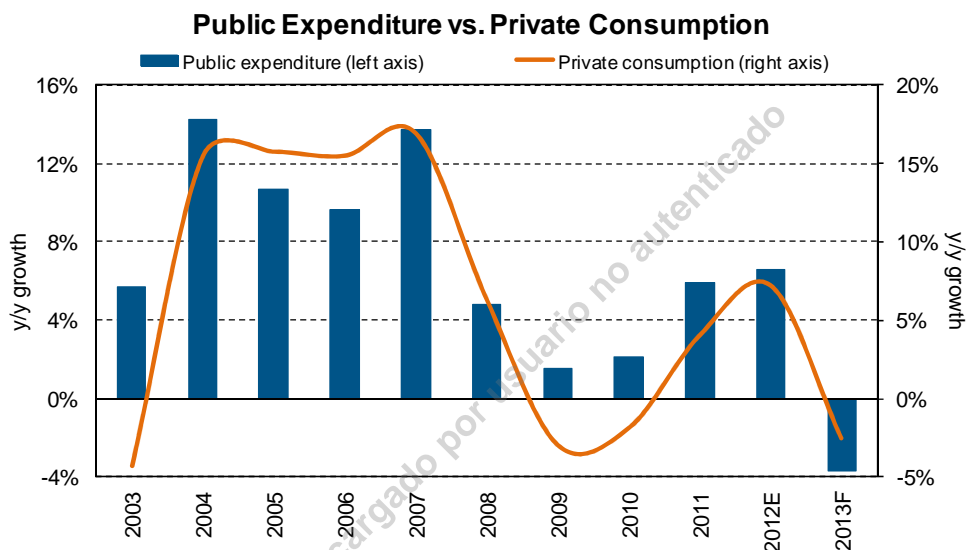
The reason is evident: the exchange control controls foreign exchange and also functions as a mechanism for prices subsidies (especially for priority goods). Exchange distortions (the gap between the official exchange rate and parallel market exchange rates), price controls, institutional weakness, and fiscal management producing deficits, among other things, all work as elements which obstruct the lowering of the inflation rate to levels on par with other Latin American countries.

High inflation is part of the model

Is permanently lowering the inflation level a priority for the chavista Administration's public policies? The answer to this question is no. The chavista Administration has constructed a model policies based on oil revenues, with clear populist and rentist elements. Through stimulus from public spending and transfers from the public sector, generalized subsidies have been able to fuel private consumption to levels that the people find acceptable, thereby maintaining the Administration's support among the



people. At **Ecoanalítica**, we have measured the correlation between public spending and the president's popularity figures, and between 2000 and 2012 they average 60%.



Sources: ONT, BCV and Ecoanalítica

This is the perfect equation for the chavista Administration, an exchange control that provides cheap financing for balancing fiscal budgets, allows for increasing public spending to keep grass roots followers happy (through gifts, subsidies, and benefits), generates increasing inflation which can be controlled to a point by expensive subsidies, the two most popular being the exchange subsidy and the energy subsidy. In other words, the Administration is not losing any sleep over persistent high inflation, as long as they can continue to provide their followers with what they need to continue to support the movement.

2013: Will the model change?

This year, the chavista movement is facing some serious problems. Chávez' absence has pushed the economy on the back burner. An exchange adjustment that urgently needs to be implemented, has been postponed. Shortages are on the rise as is inflation, and fiscal spending is slowing down.

The chavista dilemma

If the chavistas decide to gear up for another presidential election in the short term, they will need to reactivate public spending. This means increase public spending in real terms, without implementing a devaluation or any other timid half-measures. The answer would then be to increase domestic debt being issued (including financing from the BCV to Pdvsa



and non-finance public companies), increase taxing mechanisms, and repressing and controlling prices for the private sector. The key for the Administration will be to show that it's the private sector's fault and that it is responsible for the shortages.

A strategy with limited range

In summary, the strategy for chavista Administration in 2013 will be focuses on:

1. Expanding public spending (backed by issuing domestic debt and financing from the BCV).
2. With respect to foreign debt, the China agreements are a priority, looking to reactivate a Big Volume Fund for around US\$ 15.0 billion.
3. Preferential foreign exchange rates for priority sectors: food and medicines, which would compromise 45% of the total amount liquidated by Cadivi for imports, in other words, around US\$6.30 billion.
4. Increased public sector imports in order to strengthen public food distribution networks (Mercal and Pdval) and other goods and services (My Well Equipped Home program, computers, cell phones, automobiles, among other things).
5. Increase Sundecop's range of action, increase monitoring on items such as spare parts, construction materials, medical services, just to name a few, as a measure to control inflation.

There is no such thing as a free lunch

The private sector will continue to operate in an environment short of foreign currency and greater control and pressure from the State. There will be noticeable differences, depending on the sector that you are in. Key sectors such as: food and medicine will suffer less if there are cut backs on foreign currency, compared to the amount of cut backs other sectors will suffer, and the margin to maneuver to increase prices will be very limited.

The key will be production volume optimizing production lines. The less regulated sectors could have a greater margin to maneuver in terms of increasing prices but with significant restrictions when it comes time to gaining access to preferential rate foreign currency; either way, the situation will be difficult and there is no escaping it.





Economic Tips

“Progressive” adjustments. Rodrigo Cabezas, President of the Latin American Parliament, said that there will be economic adjustments this year, which will be gradually announced by the Government’s economic cabinet. Regarding the devaluation, Cabezas said that it should be used to give more competitiveness to the economy internationally, through industrialization by imports.

More currency to import food. US\$7.24 billion were assigned in 2012 to cover regular imports in the food and beverage sector, through the Aladi and Sucre agreements, said Cadivi through a press release. This represents a 14.9% increase compared to 2011, when the assignment for food imports was US\$6.30 billion.

Cadivi drives the Sucre. In 2012, Cadivi increased assignments towards the Sucre as an import mechanism, reducing the assignment of currency for purchases through ordinary pathways, and the Aladi agreement. In 2012, operations with Sucre amounted to 2.75 billion dollars, a 478% increase compared to 2011. The Sucre is a compensation mechanism used by Alba member states, and allows Venezuelan companies to pay in bolivars for imports from Cuba, Nicaragua, Bolivia and Ecuador.

Chinese dollars. According to a study by the School of Economics of the Universidad Nacional Autónoma de México (UNAM) on Chinese loans to Latin America, Venezuela negotiated credits with the Asian nation for US\$ 46.50 billion in the last 4 years, equivalent to 55% of the total financing authorized to the region’s countries (US\$85.80 billion).

Talking about ineffective measures. In its last report, Barclays Capital estimates that in the 10 years of exchange controls, the capital flight has been US\$150.0 billion. Paradoxically, the Government facilitated it by allowing and even promoting the issue of bonds through Pdvsa and the Ministry of Finance, in dollars and payable in bolivars, which were easily purchased by nationals and negotiated in international markets.

And expensive... since the Government administers the cheap dollars, it has had to assume the impact of placing the currency in the national market at a price well below its real cost. Barclays Capital estimates that the sale of dollars at the official exchange rate has cost the Government the equivalent to 6.8% of GDP per year on average, which in 2012 increased to 10% of GDP. The cost estimated by Barclays is lower than the average estimated in public accounts, 5.6% of GDP.



Negative outlook. Moody's gave a negative forecast for Venezuelan bonds, stating that "*Venezuela faces the risk of a transition, due to the weakness of its institutions, and the concentration of power in President Chávez*", and also significant policy adjustments "*to help reduce imbalances and macroeconomic distortions*".

Spending increased 6.7% in 2012. Ministry of Finance figures reveal that in 2012 Central Government spending reached VEB 414.0 billion, a 6.7% increase in real terms compared to the VEB 326.0 billion spent in 2011. This greater spending allowed the construction, government services, and trade sectors to be particularly dynamic last year.

Without elections there will be no paradise. With the electoral campaign over, the Government seems to have reduced public spending, as reflected by figures of the Ministry of Finance showing that between October of last year and January of this year, the amount disbursed (in real terms) dropped 15% (a/a), when they were growing an average of 17.2% during the first nine months of 2012. **Ecoanalítica** considers that the early increase in spending in 2012 allowed the Government to create a favorable economic environment for the elections.

Tax collection in December. According to figures released by the National Integrated Service for Tax Administration (Seniat), VEB 20.80 billion were collected in taxes for the month of December. Of this amount, VEB 4.04 billion (19.4%) are Income Tax, while VEB 10.42 billion (50.1%) were collected as VAT.

In real terms, December tax collection was up by 7.9% compared to the same period last year. The VAT increased by 10.5% in real terms compared to the same period last year, while the Income Tax increased 12.8% respectively. Customs revenue went up by 14.2% in real terms compared to the same period last year.

Tax collection for 2012. According to the figures released by the National Integrated Service for Tax Administration (Seniat), VEB 192.34 billion were collected in taxes for 2012. Of this amount, VEB 47.86 billion (24.9%) came from Income Tax, and VEB 88.92 billion (46.2%) from the VAT.

In real terms, 2012 tax collection was up by 7.7% compared to the same period last year. Both, the Income Tax and the VAT increased in real terms compared to the same period last year, by 7.5% and 12.5%, respectively. Customs revenue went up just by 0.1% in real terms compared to the same period last year.





Concepts (VEB Million)	Dec-11	Dec-12	Var (%)	Real Var	2011	2012	Nominal Var	Real Var
Total Income	16,063	20,801	29.5%	7.9%	147,442	192,339	30.5%	7.7%
Income Tax	2,985	4,044	35.5%	12.8%	36,770	47,859	30.2%	7.5%
VAT (Internal)	7,853	10,418	32.7%	10.5%	65,234	88,916	36.3%	12.5%
Customs revenue*	3,345	3,819	14.2%	-4.9%	34,131	41,371	21.2%	0.1%
Other Internal Revenue	1,839	2,055	11.7%	-6.9%	9,177	11,697	27.5%	5.3%
Spirits	998	1,263	26.5%	5.4%	2,762	3,542	28.2%	5.9%
Cigarettes	481	740	53.9%	28.2%	6,011	7,706	28.2%	5.8%
Inheritance	27	43	61.2%	34.2%	273	346	26.6%	4.5%
Random games or bets	6	9	55.9%	29.8%	129	104	-20.0%	-33.9%
Others	368	464	26.0%	5.0%	2,130	2,497	17.2%	-3.2%

Sources: Seniat and Ecoanalitica

* Includes VAT on imports

More income required. Jesús Faría, National Assembly (NA) representative, said that *"the injection of oil resources to society"* has been a key factor in the greater economic growth, but acknowledged that it is necessary to activate other sectors to have higher incomes. Faría highlighted tax reforms as an alternative to increase non-oil income, because we are *"reaching the financing limits that oil resources provide"*.

Venezuela will grow 1.8%. The WB expects the Venezuelan economy to grow only 1.8% this year, which would mean a strong slowdown compared to the 5.5% recorded in 2012, and a rate that is far from the Government's target of around 6%. The entity expects countries like Bolivia, Ecuador and Venezuela, classified as "energy exporters", to have a slowdown in their growth, in an environment with lower public spending.

There is food security in Venezuela. According to FAO Ambassador Marcelo Resende de Souza, of the 800 million people who are hungry in the world, 49 million are Latin American, *"but none are in Venezuela, because there is food security"*. FAO also revealed in its last report for 2012 that Venezuela is fulfilling the millennium goal of eradicating hunger, and is complying with the main principles of food security.

Unemployment rate at 7.8%. According to numbers released by the National Statistics Institute (INE), unemployment rate decreased 0.4 percentage points (pp) in 2012, as compared to 2011, when unemployment rate closed at 8.2%; this means that in 2012, 1,055,164 people didn't have a job. Men unemployment was 7.2% and women unemployment at 8.8%.

Inactivity rate increases. According to inactivity rate figures published by INE, shows that increased 0.4 percentage points compared to 2011, to settle at 36.0%. The increase in inactivity was associated to the larger number of people in other situations (retired, pensioner, and rentists) which increased 7.1% on average for the year (101,010 people more in absolute terms).



Informality rate at 41.7%. According to INE's figures, at 2012, an average of 5.183.382 people were employed at the informal sector (41.7% of working population), which means a decrease of 1.5 pp compared to 2011. Formal sector, which employs 58.3% of working population, increased 4.3% with respect to the same period in 2011.

Interest rates. The lending rate for the second week of January was at 15.1%, up by 3.8 percentage points compared to the previous week. The time deposit rate was at 14.5%, without variations compared to the previous week, while the passive rate has not experienced any significant variation since November 2011, placing well at 12.5%.

International reserves. International reserves increased 2.0%, going from US\$28.03 billion during the second week of January to US\$28.57 billion during the third week of January. Compared to the same period last year, international reserves have decreased by 3.7%.

Monetary liquidity. Monetary liquidity (M2) went down by 0.1% in the second week of January compared to the previous week, settling at VEB 709.60 billion. The M2 has increased 61.3% in relation with the same period last year.

Sitme figures. So far this year, US\$253 million have been negotiated through the System for Foreign Currency Transactions (Sitme), averaging US\$15.8 million a day, with an implicit exchange rate of 5.3 VEB/US\$; this represents a decrease of US\$283 million (52.7%) over the same period of 2012, when US\$535 million were negotiated. Lastly, during the third week of January the amount traded reached US\$78.6 million, US\$2.1 million less than the previous week when US\$80.7 million were traded, with a daily average of US\$15.7 million.

Oil Tips

Pdvsa's debt increases 14.7% in 2012. In 2012, Pdvsa increased its obligations through bonds and loans, making its financial debt increase 12.7%. The industry's debt management report states that at the end of 2012 the balance was US\$40.02 billion, while in 2011 it was US\$34.89 billion. The state-owned company assumed responsibilities throughout the fiscal year forcing it to make more commitments and thus look for ways to negotiate more funds.



We are not importing gasoline. Rafael Ramírez, Minister of Oil and Mining, once again denied that Venezuela is importing gasoline, but the US Department of Energy (DOE) states otherwise. *"They are trying to say that the gasoline Venezuelans use is imported. This not only is impossible, it is false. We have our own refining park in perfect conditions. We import elements for gasoline, like MTBE (methyl-ter-butyl-ether) which is added to gasoline to make it ecological"*, said Ramírez.

But the IEA said otherwise. To the production drop in Amuay, due to last year's fire, a new gas leak in Cardón is added, for an additional deficit of 50,000 barrels of gasoline. These problems mean that Amuay is producing only 30% of gasoline, and Cardón 35%, so there is a large deficit. Despite what Pdvsa says, the International Energy Agency (IEA) said that *"Venezuela imports gasoline components since 2005, but since the explosion in Amuay last August, it is importing finished gasoline"*.

Amuay still paralyzed. The Amuay refinery is not fully operational, and the possibility that it will be so during the first quarter of this year doesn't seem viable, according to IEA technicians. According to the IEA, the production of Venezuela's refineries during the last quarter of last year was 720 kb/d, 35.8% less than during the same period of 2011. In absolute terms, this means a reduction of 402 kb/d, and the AIE considers unlikely that production will recover before the end of March 2013.

Difficult to believe. Venezuela's official refining data surprisingly indicated that last September it increased 100 kb/d, and was 900 kb/d, which appears incompatible with the interruptions at the Amuay and El Palito refineries, and with the increase in fuel imports. IEA's figures reveal that the Pdvsa's purchases in the United States was close to 200 kb/d at the end of 2012, compared to previous years when imports were less than 50 kb/d.

Cardón could fall. The reports of international organizations don't take into account the situation at the Cardón refinery, which together with Amuay, is part of the Paraguaná Refining Complex (Complejo de Refinación de Paraguaná -CRP). Iván Freites, President of the worker's trade union of CRP informed that Cardón's lubricant complex didn't receive maintenance for eight years, which has extended its major shutdown for more than one year.

Official figures. According to a report of Pdvsa published by Reuters, the Amuay refinery is processing 345 kb/d of its 645 kb/d capacity, while Cardón processes 206 kb/d of its 310 kb/d capacity. Thus, CRP is processing around 551 kb/d, of a total capacity of 955 kb/d, meaning that the main crude refining center of Venezuela is operating at only 57.7% of its capacity.





Brent production will increase. Oil production in the North Sea could increase 17.7% in February due to the strong recovery in the supply of the main British reservoir, the Buzzard de Nexen field, after a prolonged maintenance in 2012. Production will be 2.06 million barrels per day (mb/d) in February, based on the last shipping reviews, compared to 1.75 mb/d in January, which could weaken one of the pillars supporting the price of the Brent.

Losing a client. Oil production in the United States increased more in 2012 than in any other year since the beginnings of the industry in that country in 1859, and is expected to increase this year. The boom is the result of a recent combination of technologies, and the authorities expect production to increase around 900,000 barrels per day in 2013. In the meantime, Venezuela has the largest reserves in the world, apparently enough for 200 years, but we are stuck at a production of less than 3 million barrels.

International baskets. Last Friday, January 18th in New York, WTI closed at US\$94.1/bl, which shows an increase of 0.2% compared to US\$93.3/bl recorded the previous week. Meanwhile, Brent steady stable decreased by 0.9% to reach US\$ 110.7/bl compared to the previous week when it reached US\$111.7/bl.

Local basket price. On Friday, January 18th the Venezuelan oil basket price closed at US\$101.3/bl steady stable in comparison to the price recorded the previous week. Meanwhile, the average of the Venezuelan oil basket stands at US\$ 101.2/bl.

Business Sector Tips

The BCV said it. In a report describing the situation of stores in Caracas, the BCV classifies six products with critical shortage, with an index higher than 40% for December, 2012. First was sunflower seed oil, with a shortage of 86.1% in stores, followed by wheat flour, with a shortage index of 76.8%, as well as sugar, corn flour, and corn and vegetable oils.

Maduro promised the earth and the moon. Together with the National Surveillance Plan launched by the Administration two weeks ago, the Vice-president of the Republic says that a project is underway to reinforce the fleet of trucks and overweight transport to guarantee the transfer of food in the country, both produced domestically and imported. He said that next week, the ministers in charge of this



area will meet with representatives of the corresponding companies to create a plan and establish the investment required.

Public industries must be investigated. The country's industrial associations requested the government to carry out the same reviews it does for the private food marketing chain in its own companies. Carlos Larrazábal, President of Conindustria, said that the responsibility of supplying the market is not only private, because the public sector has become an increasingly important actor in the agro-food industry. Larrazábal said that *"the public sector has a share of more than 50% in the production of coffee, sugar, and pre-cooked corn flour, sectors where more companies have been expropriated"*.

"Shortages never". According to José Agustín Campos, President of the National Confederation of Farmers and Cattle owners (Confederación Nacional de Agricultores y Ganaderos -Confagan), the national production of food increased 84.6% in the last 14 years, going from 13 million tons of food in 1998, to 24 million tons in 2012. *"In the last years, the Venezuelan population has not had shortages, because that occurs when there is a lack of raw materials to elaborate products or foods from the food basket; there have been specific faults, but never a shortage,* said Campos.

Existing controls "make it impossible" to hoard or speculate with regulated foods. This according to Pablo Baraybar, President of the Venezuelan Chamber of the Food Industry (Cámara Venezolana de la Industria de Alimentos - Cavidea), denying accusations of hoarding against the sector. Baraybar proposed the creation of a technical group formed by public and private food industries, and those responsible for supplies, to monitor the issue permanently, and develop specific policies that strengthen food security.

Fears to supply inventories. Carlos Larrazabal, President of Conindustria, warned that the solution for shortages isn't to prosecute the private sector. Larrazabal said that there is fear among store owners to supply their inventories, because of fears of being considered hoarding. The implementation of the Labor Law, which extended the vacation period in December, the elections, the delays in currency liquidations and in the ports, affected the supply chains and inventories in the commercial sector.

Production isn't enough. In Venezuela, 1.2 million tons of sugar are consumed per year, between domestic and industrial demands, and the sugar production for 2011-2012 was only 501,000 tons (41.7% of consumption). This isn't enough to cover the demand, and the deficit is 58.3%, or 699,000 tons.





Awaiting the sugar plan. For the Government, the 501,000 tons of sugar refined in 2011-2012 went beyond the 486,000 ton target, and represent a 4.3% increase compared to 2010-2011. However, sugar cane growers and the Government agree that the implementation of the sugar production plan must be accelerated, to achieve the historical figure of 2005-2006 of 9.1 million tons of sugar cane collected. For now, sugar cane growers are waiting for financing to renew their crops and add more planting hectares.

Auto-part production increased 15%. Omar Bautista, President of the Chamber of Venezuelan Manufacturers of Car Part Products, informed that the production of car parts for the replacement market increased around 15% last year, compared to 2011 in line with the increases in car assembly, which was 1.6%. He expects car part manufacturers to continue at the same pace in 2013. However, it will depend on the amount and the frequency of the dollars assigned to import raw materials.

Car dealers in the limelight. Claims against car dealers that make irregular car sales led a group of representatives propose a law to regulate the price of new cars, and cars with up to two years of use. *"New cars provided by assembles are not offered as new in the dealerships, rather they give them to other people, who send them as used vehicles with a price of 300 and 400 above its value"*, explained José Morales, Vice-president of the Domestic Policy Commission of the National Assembly.

One law won't reduce the price of cars. The automotive sector insists on one argument: price distortions are the result of insufficient supplies. *"The law won't solve the problem"*, said a car dealer entrepreneur. He reminded that the price distortion in the market coincides with the lengthy decline in production and global supplies, which according to Cavenez fell 73.5% between 2007 and 2012.

Distortions in the real estate market. Aquiles Martini, President of the Real Estate Chamber, said that the sale price of a rented property is between 60% and 70% below the real market cost, since the regulation of the construction value entered into force in November of last year, to set the rental and the sales price, and also said that the supply of housing solutions in the secondary market is almost at a standstill.

No distinctions. Roberto Orta, President of the Association of Real Estate Owners, said that the value of the square meter of rentals that are up for sale depreciated, because the law doesn't differentiate the price according to its location in a city. *"A property in Chacao, Catia, or La Guaira has the same sales price for the tenant, as long as it has the same size, structural characteristics, years of construction, and is in the same region: the plains, the capital, the island or in the central part of the country"*, he said.



Possible shortage of medicines. The procedure to request the certificate of non-national production for pharmaceutical companies, essential to request foreign currency before Cadivi, takes up to 90 days, when in August of last year, it took 10 to 15 days, according to sources in the pharmaceutical sector. At present, there are medication inventories, but if the attainment of non-production certificates isn't sped up, there could be a shortage of some medications.

Waiting for currency. The pharmaceutical industry started the year with a debt of US\$2.0 billion with foreign suppliers of more than 100 companies in the sector. The Government warned that they would grant currency according to the active principles they consider a priority, but companies in the pharmaceutical industry are more concerned about what will happen with the currency that has already been authorized but not liquidated to pay their international commitments. Between 2011 and 2012 the waiting time to obtain currency increased from 50 to 160 days.

Industries use credit improperly. Ricardo Menéndez, Minister of Industry, questioned the use some entrepreneurs make of the credit portfolio given to manufacturing activities. He said that last year, 35% of the money that banks granted through the manufacturing portfolio was used to purchase "*final consumption products*" and said that instead of using the resources to improve production, they are being used to "store" imported products, and announced that next week they will issue a norm regarding the criteria to use the manufacturing portfolio.

"It is cheaper to import than to produce". The effects of exchange rate controls in the Venezuelan economy result in the de-industrialization of the country, said Sary Levy, economist and Dean of Faces at UCV. This is because while the exchange rate in the country is constant, the world is experience low inflation levels, so there are mismatches between domestic and foreign production costs. This generates a drop in the production capacity, makes domestic products more expensive, and makes the country more dependent on imports.

World Economy Tips

Growth in the hand of the larger ones. Countries, particularly the U.S. and Europe, must continue with their fiscal and reform promises, to reduce uncertainty, a factor that has limited investment, contracting, and therefore growth, said Christine Lagarde Managing Director of the International Monetary Fund (IMF). Lagarde also urged the



U.S. to raise its debt limit, to avoid a recession that would have significant consequences in global growth.

The ECB has to contribute with more. Lagarde once again praised the ECB's program to purchase bonds from countries in the Eurozone that are in debt and need rescue, qualifying it as an important financial firewall, but regretted that it isn't operational yet. The IMF Director also said that the ECB must maintain a flexible monetary policy and try to reduce financing costs, to help countries with the largest debt.

From engines to burdens. The slow recovery of developed countries is slowing down the global economy, said the World Bank (WB) in its last global economic outlook report. The WB forecasted that the global GDP will grow 2.4% this year (0.6% below June estimates). The WB also reduced its estimates for developing countries to 5.5% in 2013 (from the 5.9% forecasted in June), while the expansion of advanced economies is estimated at 1.3%.

U.S. in the eye of the hurricane. The WB warned that a prolonged political battle in the United States regarding the limit of the debt could harm the growth of developing countries. If the authorities don't agree on a new limit for the debt, "*a loss of trust in the currency and a general increase in market tensions could make the growth of the U.S. and the global growth drop 2.3% and 1.4%, respectively*", said the entity.

And Latin America? The WB expects growth to be 3.5% this year in Latin America and the Caribbean, thanks to "*a greater foreign and domestic demand*". Also, the WB forecasts a 3.4% growth for Brazil, the region's giant, fostered by monetary and fiscal adaptation policies; and a 3.3% growth for Mexico, affected by a lower growth in the U.S.

U.S.: less inflation than in 2011. According to the Department of Labor Statistics of the U.S. the consumer price index of this country didn't have any variation in December, making the inflation rate for 2012 close at 1.7%, 0.3% below the inflation of 2011. This lower inflation was the result of less variation in the price of food, 1.8% (a/a) in 2011, well below the 4.4% (a/a) registered in 2011.

And also Europe. According to data published by Eurostat, inflation for the 27 countries of the European Union (EU) ended at 2.4% in 2012, around 0.6 percent points below that of 2011. The EU countries with the greatest inflation in 2012 were Hungary (5.7%), Estonia (4.2%), and Poland and Slovakia (3.7%); while those with the lowest inflation were Sweden (0.9%), Greece (1%) and German (2.1%).





Germany defending inflation targets. The German Minister of Economy urged the European Central Bank (ECB) to return to the goal of price stability as soon as possible after the entity adopted extraordinary support measures. The German office said that the ECB has a clear mandate: the final goal of the monetary policy is to guarantee price stability; therefore it is *“essential that it returns to its habitual monetary policy”*.

The giant slows down. The Chinese economy grew 7.8% (a/a) in 2012, 1.5 percent points below 2011, and the lowest growth in the last 13 years, according to estimates of the National Office of Statistics of that country. The weakness of its main destination markets, the U.S. and Europe, and the control applied to its real estate sector, affected the slowdown in China's growth.

Collateral Damage. The Japanese economy fell 3.5% (a/a) during 3Q2012, affected by a 17% (a/a) drop in its exports to China, one of its main trade partners, and with whom it has a territorial dispute since last September, to control an archipelago that China also claims. The resolution of this conflict between the two Asian giants could help Japan return to a path of growth.

Fight against hunger and poverty. The United Nations Food and Agriculture Organization (FAO) called to make responsible investments to fight hunger and poverty in the poorest countries of the planet. According to the entity, 870 million people (one in eight), are hungry and don't have enough access to food, and most live in rural areas of developing countries.

Political Tips

The importance of Unity. In a commemoration of January 23, the date that marked the end of the dictatorial government of Marcos Perez Jimenez, the Bureau of Democratic Unity (MUD) noted the importance of the union of all Venezuelans, and the resolution of political differences that currently divide the country, factors that allowed the nation make their way to the democracy.

The goals of the MUD. After criticizing the attitude (and aptitude) of the national government, the general secretary of the MUD, Ramon Guillermo Aveledo, mentioned the twelve "national goals" that will transform the country into a "truly democratic and free Venezuela", among which include: the defense of sovereignty,



defense of the decentralization, combating violence, combating electoral opportunism, and promote national dialogue.

No more primaries. In case of confront a new presidential election, the MUD ensured that its candidate will be nominated by consensus and not through a new primary process. Finally, the MUD expressed its commitment to work with all Venezuelans for make Venezuela a better country, for build a "new Venezuela".

Red justice. Luisa Estela Díaz, President of the Supreme Tribunal of Justice (TSJ), said during the Judicial Opening that the highest court of the country is taking the challenge to "*continue building (...) the Bolivarian Socialism of the 21st century in Venezuela to endure the greatest amount of social security, political stability, and happiness for our people*". Díaz also announced that in the next weeks, the TSJ will present its proposals for the II Socialist Plan for the Nation (2013-2019).

Vade retro Fedecamaras. After the Board of Directors of Fedecámaras requested a dialog with Nicolás Maduro, Vice-president of the Republic, the latter answered by criticizing the entrepreneurial association, accusing it of fostering a neoliberal economic package for the price of food. "*Fedecámaras, that isolated and defeated group of leaders, is proposing the liberation of prices. They want Chávez's government to implement a neoliberal package. Fedecámaras, move far away from us*", was Maduro's response.

The Administration must not blame anyone. Representative Julio Borges, National Coordinator of Primero Justicia, targeted the Government as the one to blame for the shortages, a problem that is presently affecting the country. According to Borges "*the only explanation*" for the increase in shortages "*is a failed economic policy of a Government obsessed with owning everything*"; "*if the Government controls almost the whole production or import process, as well as the transport, distribution, and marketing, they cannot blame anyone else*", said the representative

2012: 365 days more of discontent. According to the annual report on protests prepared by the Venezuelan Observatory of Social Conflict (Observatorio Venezolano de Conflictividad Social - OVCS), around 5,483 protests were held in 2012, a 3% increase compared to the previous year. The study states that there was an average of 15 rallies, concentrations, or closing of roads every day. The Observatory also mentioned that the number of protests recorded in 2012 equals the total of the first 4 years of Hugo Chávez's mandate (1999-2002).

What do people want? Of the total protests counted by OVCS, 41.1% were to denounce the violation of labor rights or demand new claims, 34.2% demanded access to dignified housing, and 4% claimed for the right to education. The OVSC



study highlights the 8% increase in the number of labor protests in 2012, same year in which the Government issued the new Organic Labor Law.

Jaua's appointment isn't illegal. According to Luisa Ortega Díaz, Attorney General of the Republic, "*there are no irregularities*" on the decree issued by the National Government last January 15, appointing Elias Jaua as new Foreign Affairs Minister, which appears as signed by President Hugo Chávez, who is in Cuba recovering from a surgery performed in December .

But there could be "false testimony". Former magistrate Perkins Rocha, introduced before the Supreme Tribunal of Justice (TSJ) a claim for false public document against President Hugo Chávez, for decrees 9351 and 9352, appointing Elías Jaua as Foreign Affairs Minister. Rocha alleges "*false testimony*" by the Head of State, since the document "*says that it was awarded and signed in Caracas*", when the fact is that that day he was in Havana, Cuba.

A depressed economy. According to the latest estimate of the economic freedom index prepared by The Heritage Foundation, which measures the ratio of countries that obtain prosperity according to their economic freedom, Venezuela's score was 36.1, in place 174 out of 177 countries. According to this estimate, Venezuela's economy is classified as a "repressed" or "not as free", affected by "*corruption, poor private property protection, the expansion of public spending, a long tradition of poor governance, and a weak rule of law*".

OAS at the service of the revolution? According to retired ambassador Emilio Figueredo, the OAS is "*dominated by Chávez's allies, led in South America by Brazil and Argentina*", guaranteeing a situation of "*blockade*" against decisions that are against the interests of the National Government. Last week, the Permanent Council of the OAS debated the political situation caused by the absence of the president, but most expressed their solidarity with the Venezuelan Government.

Legislatives Tips

Vehicle controls are on the making. Once again the possibility is open for the National Assembly (NA) to elaborate a law controlling the sale of new and used vehicles. The text presented basically preserves the essence of the 2009 proposal, contains 33 articles, and has the purpose of creating a regulatory framework for the



authorities to define the price of new vehicles, prohibit the sale of used cars through internet, and define a tax for individuals selling cars with less than two years of use, among others.

An eye for an eye. These were the threats made by Diosdado Cabello, President of the AN, to his colleagues of the Democratic Alternative of Parliament: *"A representative that doesn't acknowledge the Bolivarian Government, is a representative that won't be acknowledged by the AN"*. The ruling party representative gave these statements referring to comments by opposition sectors that consider that Vice-president Nicolás Maduro is *"usurping State functions"*.

Parlatino Venezuela ratifies members of its commissions. The Latin American Parliament held its first regular plenary meeting of 2013, appointing the members of the permanent commissions of the legislative body. Ana Elisa Osorio, Vice-president of the Venezuelan Parlatino, informed about the unanimous decision to ratify the members and maintain the distribution of 2012. This means leaving the thirteen permanent commissions with three representatives each, like last year.

Parliament of Táchira will investigate Leopoldo López. Nellyver Lugo, representative of the Legislative Council of Táchira, proposed to request The Public Prosecutors Office an investigation against Leopoldo López and María Corina Machado, for *"treason against the State, instigations to commit a crime, which were public and notorious public communications published in regional and national communication media"*. The proposal was approved with 7 votes and 4 abstentions, waiting to consult the AN whether the investigation against María Corina Machado proceeds or not, since she enjoys parliamentary immunity.





ECONOMIC OVERVIEW

