



Weekly Report

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*With respect to Mercosur:
Just how competitive are we?*

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As the country waits for our membership into the Common Market of the South (MERCOSUR), we ask ourselves how beneficial is the trade agreement, how it will our country. At **Ecoanalítica**, when we look at any trade agreement being contemplated by our Venezuelan government, the first question asked is how beneficial this agreement will be to our economy, what are its advantages, how will it benefit our citizens. Then there is the question of how Venezuela's exchange controls and price controls, which seriously affect our economy, will fit in to the structure of this agreement. This report will offer our take on these issues.

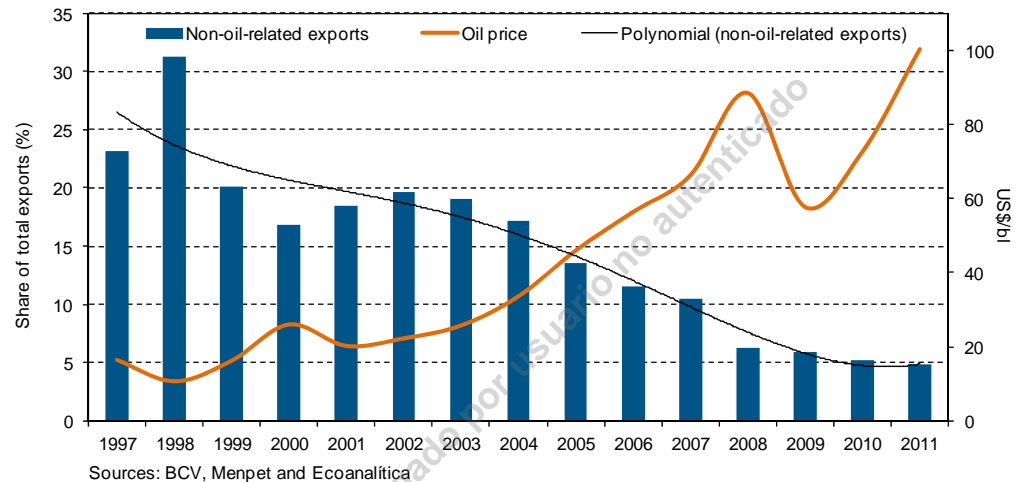
Have there been any signs of diversification with respect to production?

In 1998, 30% of all Venezuelan exports were Non-oil exports. Today, that figure has dropped to 5%. According to Central Bank of Venezuela (BCV) figures, the highest value registered by Non-oil exports was of US\$7.61 billion in 2007, which equaled 3.2% of the GDP for that year. The lowest figure registered was US\$3.40 billion (1.0% of the GDP of 2009). There is no doubt that being dependent on a single good has its consequences, such as being in the middle of a period of high oil prices and seeing how



the Non-oil sector becomes more and more marginal. In other words, we are almost exclusively competitive oil.

Non-oil-related exports / Total Exports



The Dutch disease: exacerbated

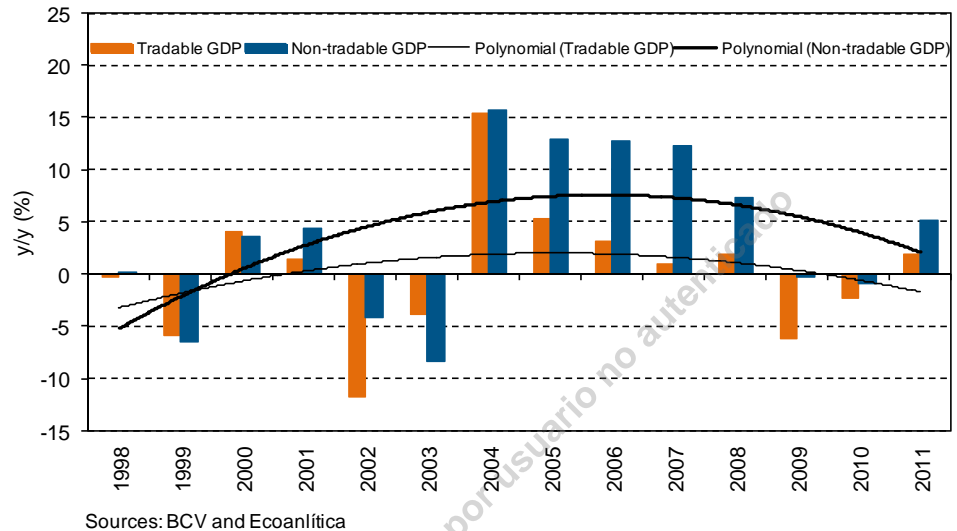
When oil prices go up, the amount of incoming foreign currency from oil export sales increases, thereby increasing the government's fiscal revenues, and consequently, also increasing the demand for tradable goods (exportable) and non-tradable goods (not susceptible to be commercialized in foreign markets, such as services), and this all tends to have an impact on relative prices.

In the case of tradable goods, the increase in demand can be satisfied with a sufficient supply of goods produced in international markets. The abundance of US-dollars resulting from oil export sales, allows the Administration to finance an increase in imports. With respect to non-tradable goods, which aren't susceptible to being exported, it reflects an increase in price due to the rise in domestic demand compared to the supply. Therefore, the flow of resources from one sector to another that results from changes in relative prices incentivizes its production. This is the reason why during an oil bonanza, it's the non-tradable sectors that reflect the highest levels of growth.





Tradable GDP vs. non-tradable GDP



Now, it's clear that during the last 14 years the Dutch disease, which has existed in our economy virtually since oil began to be exploited, has exacerbated.

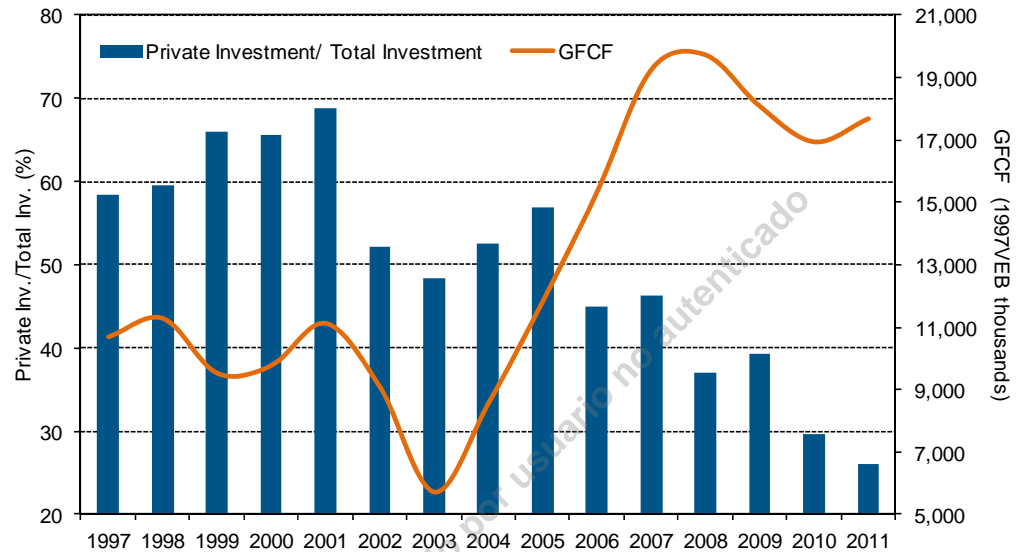
It's not only the exchange issue

Many people may think that this is due to how economic policies have been managed by the Administration. And, there is no doubt that implementing the foreign exchange control, controlling capitals (both which have been in effect for almost 10 years now), and controlling prices for a number of goods has led to a significant overvaluation the local currency (bolívar, VEF), which in turn has affected our competitiveness, especially when compared to our main trading partners. However, despite these factors that we have just illustrated, at **Ecoanalítica**, we believe that the main factor which affects our competitiveness is the economic model that has been implemented since 2004, where the State has slowly but steadily begun to become more directly involved in the economy, and at the same time squeezing, submitting and shrinking the private sector.

Following this maxim, private investment becomes less and less important in the total amount of resources invested in the country, coupled with the fact that public sector investment has not been enough. Such is the case that at **Ecoanalítica**, we will go so far as to say that if changes to the current economic model aren't implemented, we will be destined to be less and less competitive with respect to our main trading partners, including Mercosur.



Private Investment / Total Investment



Sources: BCV and Ecoanalítica

But the exchange issue is critical

In this report we have included an update to our real exchange rate model (TCR) which allows us to analyze the evolution of costs and domestic prices, taking into account the impact on foreign prices which are measured through the exchange rate. This makes the TCR a type of competitive measuring meter for Venezuela.

How to read the TCR model?

Even though we have explained this before, we feel that it is important go over the main factors involved in accurately interpreting the TCR model.

In order to determine if the appreciation/devaluation of the local currency (bolivar) led to an overvaluation/undervaluation of the exchange rate it's important to know and determine what the Real Balanced Exchange Rate (TCRe) is. We have set this value at 100 taking as the base the average of the period 1990-1993. If the TCRe indicator is over 100, then there is an undervaluation in real terms of the local currency, if on the other hand, the indicator is below 100, then there is an overvaluation in real terms of the local currency.

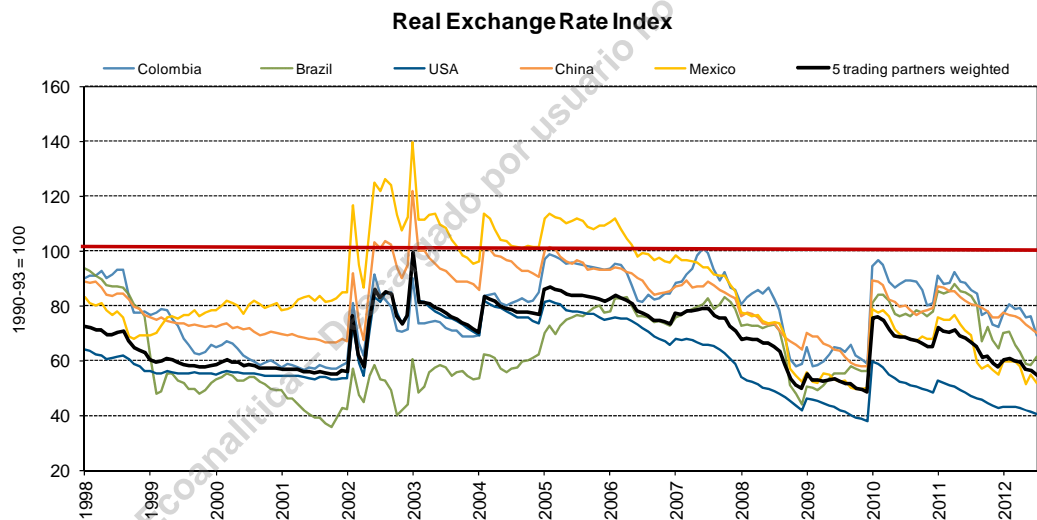
So, if we state that the TCR has appreciated, we are referring to the fact that domestic prices, measured by inflation, are increasing at a pace greater than the exchange rate. This means that the domestic currency is able to buy more goods and services on the foreign market than in its own domestic market; ergo, it's cheaper to import from abroad than to buy



locally. This makes local (Venezuelan) exports be less competitive, and creates an incentive to import. Now, if instead, the TCR has depreciated, then domestically produced goods and services will be cheaper than those offered in foreign markets. This makes our local exports more competitive.

By how much is the exchange rate overvalued?

The following graph shows that Venezuela's TCR has always had a tendency to be overvalued, in other words, we have a "cheap" exchange rate (appreciated), significantly below its balanced value, which increases its purchase power abroad (thus favoring imports), a tendency that has been reinforced over the last few years.



Sources: Central Banks of every country, Bloomberg and Ecoanalítica

By calculating a weighted average compared to our five main trading partners we can calculate an implicit exchange rate that will compensate for the overvaluing. For the month of July, the implicit exchange rate is at VEB/US\$ 8.7, in other words, 102% higher than the official exchange rate, which is the same as being overvalued by 45.3%¹.

With respect to Brazil, the most important member of Mercosur, the implicit exchange rate for the month of July is at VEB/US\$ 7.3, in other words, 69.8% higher than the official exchange rate that is equal to a real overvaluation of 38.7%. With respect to Colombia, the most important member of the Andean Union (CAN), the implicit exchange rate for the

¹ It's important to point out that the current level at which the non-official exchange rate is trading is even higher than this.



month of July is at VEB/US\$ 6.4, in other words, 49.9% higher than the official exchange rate that is equal to a real overvaluation of 30.7%

The government has a golden opportunity

Having finally been accepted to enter Mercosur, Venezuela has generated a lot of speculation and talk in public circles, especially considering the state of Venezuela's production apparatus. At *Ecoanalítica*, putting aside the issue of whether Venezuela should in fact join Mercosur or go back to the CAN, we believe that this is just one more significant reason to devaluate the bolívar (along with the need to make a fiscal adjustment and adjusting for oil prices that are not increasing as much as expected for 2013). No matter who wins the presidential election in October, this devaluation which is almost certainly coming. If handled properly and with a clearly defined structure, besides making our products more competitive abroad, it will also generate incentives to increase domestic production and help lower inflation in the medium and long term.

At *Ecoanalítica*, we believe that the devaluation after the presidential election is virtually unavoidable. Its impact will be different depending on who is administering it.

Chavism has to rethink its model to be able to compete

Given the current political uncertainty, analyzing the upcoming devaluation in a scenario where the chavistas win the presidential election is a very complex task to carry out. There is the possibility that the chavista party will have another candidate, or another President of Venezuela if Chávez wins, but then is forced to resign for health reasons. In this scenario, one wonders if the exchange policies of the current Administration will continue or not?

We are not talking about dismantling the exchange control system, since it is clear that this is a key piece of the chavista economic model (which even used as a political weapon); but changes in the existing exchange control system could be introduced one way or another. Some groups within the chavista movement have presented the option of reestablishing the swap market and calling it an improvement over the SITME. Another key variable is whether Minister Giordani will remain at the head of the Ministry of Planning and Finance.

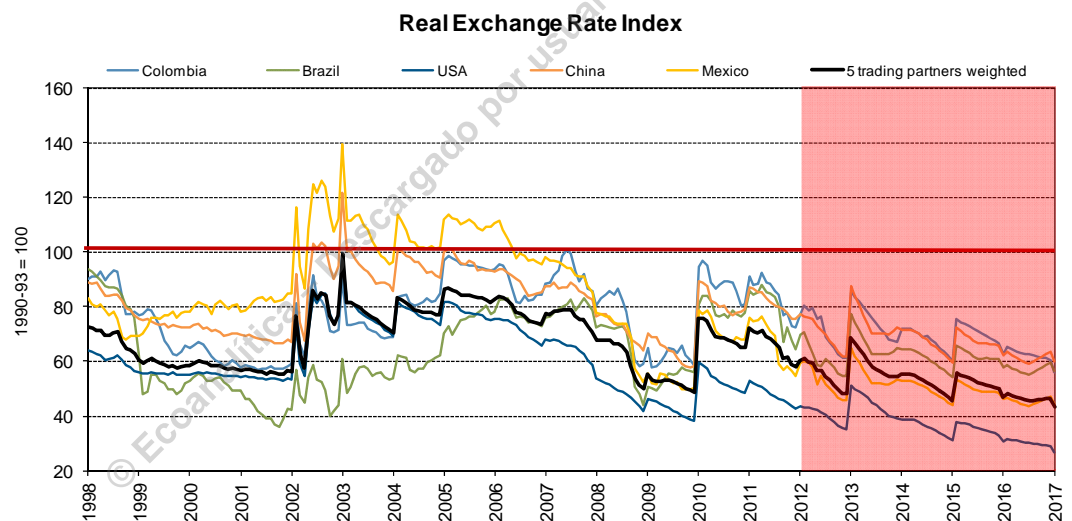
In summary, with another candidate different than Chávez, it is not clear what the future of the exchange control will be, and by the same token, CADIVI, which is at the heart of the current exchange system.





In this scenario, and with the current structure continuing as it is, we assume at **Ecoanalítica** that the CADIVI exchange rate will be adjusted from VEB 4.3/US\$ to VEB 6.3/US\$; this would imply a devaluation of 46.5%. The SITME rate will be adjusted from VEB 5.3/US\$ to VEB 7.5/US\$, an increase of 41.5%. But, the important indicator to watch is the adjustment made to the weighted exchange rate that would go from VEB 4.5/US\$ to VEB 6.5/US\$, which would equal a devaluation of 44.2% and a lowering of the real overvaluation to 33.5% during the 1Q2013.

As seen in the next graphic, this would be a short term solution, in order to make adjustments for fiscal accounts, but would continue to negatively affect our competitiveness in the medium term.



Capriles' recipe to be competitive again

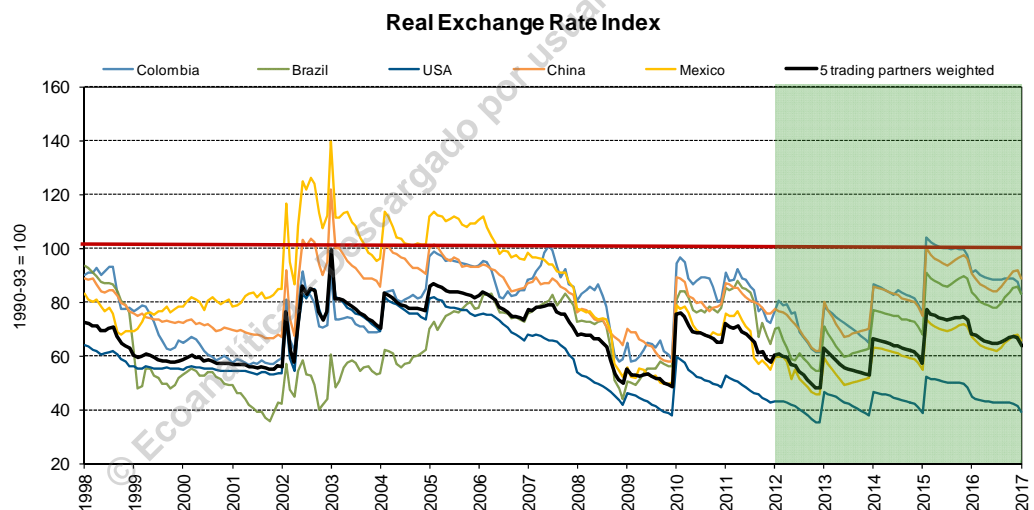
With respect to the Opposition candidate, recently, the coordinator for Henrique Capriles Radonski (HCR) campaign for the presidency, Ricardo Villasmil, pointed out that the first step with respect to dismantling the exchange control system would be to legalize the parallel exchange system. Villasmil continued to say that if the opposition candidate were to win the presidency, that the exchange control system, which has been in place since 2003, would be dismantled and that price controls would be slowly phased out, expropriations would be stopped, and protection mechanisms for the most vulnerable sectors would be implemented.

At **Ecoanalítica**, we believe that in this scenario, in 2013, CADIVI will remain for the priority sectors (food and medicines), and in accordance,



we expect that the CADIVI exchange rate will go from VEB 4.3/US\$ to VEB 5.7/US\$. This would imply a devaluation of 32.6%. The SITME rate would be adjusted from VEB 5.3/US\$ to VEB 9.4/US\$, an increase of 77.4%. The important indicator, the adjustment to the weighted exchange rate, would go from VEB 4.5/US\$ to VEB 6.0/US\$, which would equal a devaluation of 32.1% and a lowering of the real overvaluation of 20.0% in the medium term.

In our opinion, this schema will remain until the distortions in relative prices are eliminated to then go to another one, similar to that of our main trading partners, which would create a better climate for investment and could make our products more competitive up against our main trading partner.



Sources: Central Banks of each country, Bloomberg and Ecoanalítica

Epilogue: What opportunities are there in Venezuela?

How are we to survive what's coming? At **Ecoanalítica**, we have carried a number of studies analyzing the different business models of the non-oil export sector. Our studies show that the export companies that have survived have been forced to design strategies and be creative and skillful, looking for different ways to ensure success. These companies made a serious commitment facing the internationalization. Leaving the opportunistic vision of international markets, which generate two very valuable benefits: (i) escape from Venezuelan volatility, and (ii) diversify operative risks.

This demands that you develop your own capabilities, those of a multinational company. It's clear that companies that carry out this model



do so more out of reacting to high regulative risks than for the competitive advantages this business model can provide.

Advise to non-oil export sector

In summary, initiatives identified to improve export business in the current situation we are going through are:

- Escape the market: move supply to another source
- Improve costs: such as: unifying packaging
- With respect to commercialization: many have sought to reposition themselves creating products such as *SuperPremium*
- Designing mechanisms and/or strategies for coverage, such as:
 - ✓ Create companies to hold earnings abroad.
 - ✓ Finish the product outside of Venezuela to offset inflation costs.
 - ✓ Capital Non-Repatriation schemas (Exchange between exports and imports).

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Economic Tips

Authorizations in dollars increase 7.2% in 1S2012. In the first half of this year the Foreign Exchange Administration Commission (Cadivi) authorized a total of US\$15.11 billion, an increase of 3.6% over the same period in 2011, when it approved US\$ 14.58 billion.

Dollar`s supply for imports increases 2.9%. In 1S2012, the Central Bank effectively settled for ordinary imports US\$8.34 billion, a figure that translates into a decrease of 2.5% over the same period in 2011. But by adding imports via Aladi Convention and Sucre, the amount paid reach US\$10.92 billion, an increase of 2.9% over the same period in 2010 when it settled US\$10.61 billion.

BCV's disbursed amount (US\$ Million)			
Rubro	1S2012	1S2011	Var (%)
Imports	10,918	10,610	2.9%
Students	232	225	3.2%
Special Cases	238	123	94.1%
Airlines	635	583	8.9%
Ext .Private Debt	3	4	-26.1%
Consulates and Embassies	43	30	45.4%
Insurance and Reinsurance	52	31	66.5%
Foreign Investment	13	6	110.5%
ALADI Convention	149	322	-53.7%
Retirees and Pensioners	43	29	48.2%
Remittances	385	374	2.8%
Credit Cards	1,317	846	55.8%
Cash for travel	210	154	36.7%
Services	1	4	-81.1%
Sucre	19	7	180.3%
Telecommunications	125	73	71.4%
Total	14,383	13,420	7.2%

Sources: CADIVI and Ecoanalítica

*Includes regular imports and imports through ALADI and Sucre

**Excludes imports

Tax collection for June. According to the figures released by the National Integrated Service for Tax Administration (Seniat), VEB 16.20 billion were collected in taxes for the month of June. Of this amount, VEB 4.10 billion (25.0%) came from Income Tax, and VEB 9.60 billion (58.8%) from the VAT. The agency raised VEB 88.23 billion during the first semester, of which VEB 24.59 billion came from Income Tax (27.9% of the total), and VEB 39.36 billion from Value Added Tax (VAT) (44.6% of the total).



In real terms, June tax collection was up by 6.8% compared to the same period last year. Both, the Customs revenue and the VAT increased in real terms compared to the same period last year, by % and 30.9%, respectively. Revenue coming in due to Income Tax went up by 35.6% in real terms compared to the same period last year. Total revenue in the first half of this year grew by 4.7%. In turn, VAT and Other income from customs increased in real terms, 10.1% and 43.3%/y respectively. Meanwhile, income tax revenues increased 2.9% in real terms over the same period of 2011.

Concepts (VEB Million)	1S 2011	1S 2012	Nominal Var	Real Var
Total Income	67,446	88,230	30.8%	4.7%
Income Tax	67,446	24,585	-63.5%	-70.8%
VAT (Internal)	28,629	39,365	37.5%	10.1%
Customs revenue*	15,127	18,845	24.6%	-0.3%
Other Internal Revenue	3,886	6,958	79.0%	43.3%
Spirits	664	526	-20.9%	-36.6%
Cigarettes	3,023	4,542	50.3%	20.3%
Inheritance	108	150	38.7%	11.0%
Random games or bets	87	42	-52.0%	-61.6%
Others	683	851	24.5%	-0.3%

Sources: Seniat and Ecoanalítica.

* Includes VAT on imports.

Unemployment rate at 7.4%. According to numbers released by the National Statistics Institute (INE), unemployment rate decreased 0.4 percentage points in June, as compared to the same period in 2011, when unemployment rate closed at 7.4%; this means that in the six month of the year, 1.001.703 people didn't have a job. Men unemployment was at 6.9%, meaning a 1.2 percentage points decrease throughout the year, women unemployment was at 8.1%, meaning a 1.4 percentage points decrease throughout the year.

Inactivity rate decreases. According to inactivity rate figures published by INE, it shows that the rate decreased 0.2 percentage points compared to June 2011, to settle at 35.6%. Within this, men inactivity experience an increase of 0.3 percentage points, from 2.255.976 of inactive men in June 2011 to 2,330,208 in the same month in 2012, settle at 22.3%. Women inactivity, in turn, decreased 0.6 percentage points reaching 48.8%.

Informality rate increases. According to INE's figures, at end-June, 5,400,667 people were employed at the informal sector (40.8% of working population), which results in an increase of 0.3 percentage points compared to June 2011, when the



sector employed to 5,176,970 people. Formal sector, which employs 57.3% of working population, increased 0.3% with respect to the same period in 2011.

Food basket decreased by 1.1% in June. According to figures released by the National Statistics Institute (INE), the food basket value was VEB 1,832 in June, up 1.1% from May and up 20.6% from June 2011, this means that the reference food basket increased VEB 313.3 in one year.

Where the money? Products that have greater participation in the basket are primarily fruits and vegetables with a share of 28.6% equivalent to VEB 523 (US\$121.6) followed by cereals and their derivatives represent 15.1% equivalent to VEB277 (US\$64.3).

Minimum wage only covers 97.2%. This means that minimum wage is not enough to buy basic foodstuffs, because a worker earning the minimum wage (VEB 1,780) can buy 97.2% of the basket estimated by INE.

The government wants more money. Despite high oil prices, funds available aren't enough to cover the increased current spending and, for the second year in a row, Chávez' administration is requesting VEB30.0 billion worth in additional borrowing that will be earmarked to pay pensions and labor obligations.

Further transfers for missions in the second half of the year. At *Ecoanalítica* we believe that the State has grown to such an extent that it requires more funds to meet new requirements related to housing projects; however, we also expect an increase in transfers (wages, missions, among others) for the second half of the year.

Higher liquidity could drive inflation up. In the first half of 2012, the significant increase in public spending hadn't translated into higher liquidity, because the administration had transferred bolivars to the Treasury by selling bonds to banks, thus preventing cash from reaching the public.

However, the administration began to use these funds in June and liquidity gained 7% (the highest increase for the year-to-date). The higher amount of money behind the same products could bring about inflationary pressures, unless the administration is able to increase supply through higher disbursements by Cadivi, or reduce liquidity through issues.

Controls help reduce inflation. According to Elías Eljuri, president of the National Statistics Institute (INE), controls over product prices and costs haven't impacted the supply of goods, because the administration has intensified its efforts to maintain



supply and this has been significant to continue abating inflation, which recorded a month-to-month variation of 1.4% in June.

Domestic debt service is projected at US\$ 18.5 billion for the next year and a half. The strong increase in borrowing has had its impact on funds earmarked for public debt payment; according to date released by the Ministry of Planning and Finance, debt service to be paid by the central government over the next year and a half is projected at US\$27.9 billion. The highest weight comes from domestic obligations; at the end of the first quarter of 2012, the Ministry of Finance applied US\$ 3.3 billion for domestic debt payments and debt service for the rest of 2012 through end-2013 is expected at US\$18.5 billion.

Three supplementary appropriations for VEB 1.5 billion approved. The Finance Committee of the National Assembly (AN) approved three supplementary appropriations for VEB1.5 billion, including VEB1.0 billion for programs developed by Inder and CVAL of the Ministry of Agriculture and Lands and VEB 422 million for Corpivensa and Bauxilum (Ministry of Industries). The funds will be used to pay labor obligations and wages of the current month.

Interest rates. The lending rate for the second week of July was at 17.1%, increasing by 2.9 percentage points compared to the previous week. The time deposit rate remained since July 2011 in 14.5%, while the passive rate has not experienced any significant variation since November 2011, placing well at 12.5%.

International reserves. International reserves decreased 2.1%, going from US\$28,245 million during the first week of July to US\$27.658 million during the second week of July. Compared to the same period last year, international reserves have decreased by 8.3%.

Monetary liquidity. Monetary liquidity decreased 0.4% in the first week of July compared to the previous week, settling at VEB 518.234 million. The M2 has increased 52.4% in relation with the same period last year.

Sitme figures. So far this year, US\$5.64 billion have been negotiated through the System for Foreign Currency Transactions (Sitme), averaging US\$43.1 million a day, with an implicit exchange rate of 5.3 VEB/US\$; this represents an increase of US\$1.34 billion (31.1%) over the same period of 2011, when US\$4.12 billion were negotiated. Lastly, during the second week of July the amount traded reached US\$129.9 million, US\$96.9 million more than last week when US\$226.9 million were traded, with a daily average of US\$45.4 million.





Oil Tips

Preliminary agreement on labor contract. Wills Rangel, president of the oil and gas worker union FUTPV, announced that a preliminary agreement on the collective contract was reached after accepting the proposal presented by PDVSA's negotiators of increasing base wage only by 50%. *"We have to accept a proposal that is viable for the company,"* Rangel said. The draft contract presented by FUTPV called for an 82% increase to compensate for inflation over the last two years, which has been over 56%.

What is still to negotiate? Although a wage increase was agreed, clauses concerning longevity payments, retirement plan, work schedule, union activities and the one considered medullar and essential for the contract, the clause referred to different payments and deadlines on which PDVSA commits to make the respective payments.

OPEC: Venezuelan production unchanged. According to OPEC July's report, Venezuelan crude oil output remained practically unchanged, gaining just 1 kb/d in May-June to 2.36 mb/d, down 40,000 b/d (kb/d) or 1.6% from June 2011. The report also shows that OPEC's output averaged 31.36 mb/d in May, down 106 kb/d from 31.46 mb/d of May 2011.

According to Petro-Logistics, exports increased. According to the last report by Petro-Logistics, a firm that monitors Venezuela's oil production, exports increased 8.4% on a month-to-month basis, going from 1.91 mb/d in May up to 2.07 mb/d in June, for a substantial increase of 164 kb/d. The report also says that in June, Venezuela sold more oil to India (314 kb/d) than to China (233 kb/d).

Global oil demand for 2013. The last report released by the International Energy Agency (IEA) shows that global oil demand will reach up to 90.9 mb/d in 2013, that is, only 1.0 mb/d over 2012 estimate. The agency points out that this increase is essentially equal to that estimated for 2012 (0.8 mb/d), far below the pre-crisis period. Given projections pointing at global stagnation, demand from emerging countries is expected to exceed that of developed countries.

OPEC supply anticipates sanctions. According to the IEA report, OPEC supply was close to recent peaks, reaching up to 31.8 mb/d in June, before U.S. sanctions and EU's embargo against Iran enter into force. IEA expects that OPEC's supply reaches 31.2 mb/d in 3Q2012, and to 30.5 mb/d in 4Q2012-4Q2013.



Refining and inventories. The IEA pointed out that the increase in refining capacity for 2012 and 2013 will be 1.0 and 1.3 mb/d, respectively, remaining above demand growth. Industry's oil reserves gained 15.4 million barrels in May, for a five-year average of 25.1 mb. However, preliminary data shows a drop of 7.2 mb in inventories in June according to OECD.

More gasoline from the "Empire". According to data from the US Department of Energy (DOE), Venezuela imported 1 mb of gasoline in December 2011, a figure that is similar only to gasoline imports from the US after the oil strike, when 1.01 mb, about 11.3% of Venezuela's domestic consumption, were bought.

Declining refining volumes. The US hadn't exported gasoline to Venezuela at least since March 2005, but in past December, it sold 1 mb of gasoline to the country. This could be associated with the deterioration of the crude oil refining circuit in Venezuela, increased pressures on the domestic market and the necessity of complying with markets. In 2012, gasoline purchases dropped to their average levels (592,000 barrels in January, 310,000 barrel in February and 512,000 barrels in April).

Product imports also recovered. According to DOE, 1.62 mb of refined products was exported from the US to Venezuela in April. Product sale from the US increased throughout 2011, to more than one million barrels per month; in December, sales amounted to 2.2 mb.

How much do gasoline imports cost? Since December 2011 through April 2012, Venezuela imported an average of 15.8 kb/d finished gasoline; considering an average price of US\$122/bl. of gasoline for that same period on the US markets, Venezuela spent about US\$1.9 million/day to buy gasoline. In total, about US\$288 million were spent in gasoline over the five-month period.

"It's not rationing, but sale control, because gasoline is virtually free of charge." Despite these words, referred to the placement of fuel chips on motor vehicles in Zulia State, president Chávez explained that the measure is intended to prevent smuggling and "*reduce fuel consumption*" so as to increase exports and get more foreign currency. The Ministry of Petroleum and Mining has estimated that gasoline demand in places where chips are to be installed will decrease by 35%-40%. It sounds like rationing.

Trying to refine heavy oil. During a visit to Guaraguao Refinery in Anzoátegui State, president Chávez informed that in 2015, once the deep conversion project is completed, the refinery will increase its daily production capacity by 30 thousand barrels to refine 210 kb/d of heavy crude from the Orinoco Oil Belt.



Shady business. Although PDVSA bought boats for barge activities so as to put an end to shady businesses (machinery rents amount to roughly US\$8-US\$14 million daily), 60% of those equipment are damaged and top management hasn't decided to repair them. Union leaders have charged that directors own equipment than they rent to PDVSA or charge their commissions for the expensive rent, that is, there is a monopoly between management and companies renting equipment.

Ancap is trying to pay to PDVSA. Uruguay's state-owned oil company is negotiating with PDVSA the setting-up of a trust fund as a way of payment to repay the US\$800 million debt that Ancap owes Petróleos de Venezuela. Ancap vice-president, Germán Riet, stated that the agreement is moving forward positively and the definite announcement of the agreement is expected to be made in September.

What are we going to do with coke? This is the question the administration is asking when faced with coke mountains. "We don't want to be coke exporters for others to take it," the Minister for Science and Technology, Jorge Arreaza, pointed out, adding that the volume of coke accumulated is estimated at 20,000 tons/day; therefore, its processing has to be analyzed to develop new environmentally sound alternatives.

International baskets. At the time of foreclosure in New York, WTI was traded on July 13 at US\$85.25/bl, which shows an increase of 1.2% compared to US\$86.25/bl recorded the previous week. Meanwhile, Brent rose by 0.3% to reach US\$ 99.6/bl compared to the previous week, when it reached US\$99.3/bl.

Local basket price. The Venezuelan oil basket price fell last week to close at US\$92.8/bl on July 13, resulting in a decrease of 0.1% compared to US\$92.9/bl recorded the previous week. Meanwhile, the average of the Venezuelan oil basket stands at US\$ 106.7/bl.

Business Sector Tips

How is trade with the US doing? According to figures released by the Venamcham (Venezuelan-American chamber of Trade and Industry), during the first five months of the year, imports from the US gained 42%, whereas exports from Venezuela



dropped 8%. Oil imports surged in 2011-2012, with a 45% jump, whereas non-oil exports fell by 48%.

Cadivi isn't even allotting foreign currency for medicines. Cifar (pharmaceutical industry chamber) states that Cadivi has only authorized 15% of the amount requested. Representatives of the pharmaceutical industry point out that foreign currency allocation is substantially lower than last year and that approval periods have doubled lasting about 90 days today (vs. 45 days in 2011). The most impacted are local producers, which have difficulties to keep up with their production schedules.

Fears for shortages. Since backlog in foreign currency allocations has doubled over the past three months, businesses trading with price-controlled products gathered with Karin Granadillo, superintendent of costs and prices. Although the distribution report doesn't show any shortage of these products, businesses warned Sundecop that if delays in foreign currency allocations continue, processing and supply chain could be interrupted.

Cheaper imports. Venezuela's accession to Mercosur will render imports cheaper and will allow us to consume products from "*sister nations*," according to Ricardo Menéndez, vice-president of the Productive Economic area. Menéndez said that "*with Mercosur, we are going to have the possibility of accessing foodstuffs and products at different prices*" and Venezuela's integration into the regional bloc will result in an "evident reduction of prices" in a large number of products that the national government is already purchasing from Mercosur member countries.

Time deposits in free fall. According to the Superintendent's Office of Banks (Sudeban), from June 2011 through June 2012, time deposits dropped 64.6%, accounting for 0.7% of deposits. The administration obliges banks to grant 47% of their credits at low interest rates, therefore, to maintain their profits up, banks have opted for minimizing these deposits. Edgar Hernández Behens, superintendent of banks, sent a letter to banks urging them "*not to discriminate, restrict, dissuade or prohibit clients from opening saving accounts and time deposits.*"

Unbeatable profits. Sudeban stated that profits accrued by banks in the first six months of 2012 amount to VEB 12.83 billion (US\$2.98 billion), up 132.4% from the same period in 2011. Other indicators are equally positive: profitability with respect to equity went from 30% in the first half of 2011 up to 49.5% and credit portfolio closed the six-month period with an increase of 56.3%, with VEB 324,400.

Freight increased. Transportation firms working in the central part of the country agreed to increase freight for transportation of foodstuffs and bulk products by 20%.



Jonathan Durvelle, vice-president of Catracentro (transportation association of the central region) explained that since October (last increase), they have had to assume variation in the price of trucks and spare parts, in addition to daily delays at Puerto Cabello port, where a loaded truck can remain up to six hours retained.

Pasteurized milk production fell 70%. Although the liter of fresh milk at corral gate is set at VEB 3.6, the industry pays up to VEB 4.5 per liter, with the result being a drop in profitability of pasteurized milk, the price of which has been set by the administration at VEB 5.9. Roger Figueroa, president of Cavilac, explained that many businesses have ceased to produce milk, whereas the few that are still active on the market are registering losses, with milk production dropping by about 70% this year.

More price backlogs. Venmaíz (association of precooked corn flour producers) explained that companies will have to assume a 47% increase in corn price starting from August, which will translate into an increase in production costs of precooked corn flour (in addition to the 20% increase in raw material freights). This signifies higher losses for the industry. Venmaíz is demanding an adjustment of VEB 4.1 to VEB 6.8, which would help to cover production costs.

And rice too. Corn producers, in turn, are demanding that the price of one kg of rice, currently at VEB 5.6, be increased by 35%, because starting from August, they will have to assume a 23.7% increase in raw material prices.

Sundecop will make its own calculations. William Contreras, Superintendent of costs and prices, said that since irregularities have been detected in the study of cost structures of companies working with prioritized products, Sundecop is considering its own means to calculate production costs of prioritized products.

More products from Colombia. According to figures released by the National Administrative Department of Statistics (DANE), in January-May, Colombia exported to Venezuela US\$976 million worth in merchandises, whereas for the same period in 2011 the figure was US\$605 million, down 61.2%. These numbers show that imports are retaking the levels they had in late-2009, when diplomatic relations were broken and trade virtually disappeared.

Less from here to there. In return, Colombian imports from Venezuela show that up until April, Venezuela exported US\$224 million worth in products, whereas, the figure amounted to US\$245 million, down 8.5%, in the same period in 2011. At least since 2004, the trade balance has favored Colombia and in the first fourth-month period the balance in favor of Colombia was at US\$516 million.





Nicaragua strives to continue to sell. Since contracts for beef and milk exports expire at the end of July and given the current national political situation, Nicaraguan producers are afraid that trade relations might be negatively affected. Ariel Bucardo, Nicaraguan Minister of Agriculture and Livestock and Forest Affairs, said that Nicaragua maintains its commitment to export milk and beef up until late-2012, under the same terms, regardless that agreements expire this month. Bucardo urged the local government to sign new agreements.

The Stock Exchange is a good option for small savers. In a scenario where banks have ceased to receive time deposits, the Public Stock Exchange is an option for small investors to make profits from their moneys, Félix Franco, president of the Public Stock Exchange, said. To invest in bonds of the Republic, which accrue interests between 16-17%, a minimum of VEB 5,000 is required, but the Public Stock Exchange has devised a mechanism that allows groups of small investors to obtain benefits on the capital market with an investment of VEB 1,000,

Alberto Lovera Plant is ready. The administration opened the Alberto Lovera thermal power generation plant in Anzoátegui State on Friday, July 13. The plant will produce 300 MW that will be added to the national power grid. The construction of the plant was originally planned in 2005 and according to the authorities, it will guarantee power supply to about one million people in Anzoátegui.

World Economy Tips

Lower global growth expectations. In its review of global economy, the IMF lowered its growth forecast for 2013, from 4.1% to 3.9%. The IMF warned that the European debt crisis might further damage world growth unless EU leaders take firm steps to combat it. Growth forecast of the group of emerging countries (including China, Brazil and India) was adjusted from 5.9% to 5.6%, whereas growth for developed economies was revised downward from 1.9% to 1.4%. Finally, for Spain, the IMF expects recession to last throughout 2013.

Lower growth for emerging economies. The consequences of the European crisis have been felt all over the world with emerging economies being hit the hardest. According to Olivier Blanchard, chief economist at the IMF, now that growth rates in emerging countries have decreased, *“there are two reasons for concern: first, if this is the beginning of the end, will growth rates will be very low? The answer is no. The*



other concern is that growth rates will not be as high as those of the '2000s, so we expect high growth, but not as high as before." Forecasts, however, haven't been as dismal when compared with US or EU growth forecasts.

US: drop in retail sales; another sign of weak recovery. According to the US Department of Commerce, retail sales dropped 0.5% in May-June. The decline is perceived as a new sign of a weak economic recovery, because consumption is an important engine of US economy. Another sign of poor recovery has to do with the economic growth shown until June, which is too low to reduce unemployment, which in June remained at 8.2%.

Surprising hike in producer price index. Producer price index for end products in the US gained 0.1% in June, when a 0.4% drop was expected, after May's 1% contraction. Despite this unexpected increase, PPI variation is just 0.8% on a year-to-year basis, the lowest since October 2009. The increase was driven by a 0.5% hike in food prices, whereas energy prices fell 0.9%.

More austerity, more unemployment. Euro zone could lose a further 4 million jobs, as assured by representatives of the International Labor Organization (ILO). According to ILO, if the European Union doesn't take a road other than the austerity measures, the total number of jobless people in the EU could rise up to 22 million. ILO pointed out that an agreed policy is required not to fall in the "austerity measure trap" and speed up job creation.

A last attempt to prevent Venezuela from joining Mercosur. Paraguay presented a document to the Permanent Review Tribunal of Mercosur requesting Paraguay's suspension from the bloc and Venezuela's accession, which has been at a stalemate given the refusal of the Paraguayan Congress, to be annulled. The Paraguayan State alleges that as per the Treaty of Asunción, accession requests should be approved by a unanimous decision by Party States, and since it is still a member of Mercosur, the bloc cannot accept another member without Paraguay's approval.

South Korea: unexpected cut in rates. The Central Bank of South Korea cut interest rates in an attempt to protect the country from the effects of the euro zone crisis and the weakening of Chinese economy. The weak economic recovery of the US and the lower growth forecasts were also reasons taken into account by the Bank to take official interest rates to 3%. It's worth noting that the European and China Central Banks cut back their rates, in an attempt to revive consumption and give a boost to investment.

Italy is being financed at lower rates. Italy placed US\$ 9.15 billion last week on one-year debt bond markets, at an interest lower than that of one month ago. 12-



month papers reached a profitability rate of 2.69%, after 3.97% in June 13 auction. Furthermore, at the end of the week, 10-year bonds were sold below 6%, after having briefly increased over that level. The Italian Government successfully auctioned several billion dollars in 3-year bonds at 5%, in spite of the fact that Moody's lowered the country's risk rating.

Political Tips

“Commitment to Democracy.” Last week, the National Electoral Council (CNE) proposed the signing of an agreement to abide by electoral rules vis-à-vis the upcoming October presidential election. While stances on the pact proposed by the CNE have been contrary (Chávez is fully in agreement, whereas Capriles isn't and has described the pact as *“majunche”* (poor)), presidential candidates, as well as representatives from political parties, are expected to express their adherence to the Pact.

CNE scolds parties and media. Tibisay Lucena, president of the National Electoral Council (CNE) warned the campaign commands of the different presidential candidates that children cannot be used in election ads. Lucena also recalled that media cannot develop their own campaigns; “all campaigns that aren't identified with the tax identification number and by a command will be considered independent campaign by mass media,” and in this case, media could be admonished.

Church and government resume dialogue. Five years after having broken relations, last week top government officials, including Vice-President Elías Jaua, gathered with the Bishops of the Venezuelan Episcopal Conference (CEV). Jaua assured that president Chávez is willing to “reestablish a climate of institutional, political and personal respect” with the CEV, and that assurances that these relations will be resumed will depend on everyone playing their corresponding role in society and on relations being based on mutual respect.

The administration withdraws institutional campaign “Corazón Venezolano.” The institutional campaign “Corazón Venezolano” (Venezuelan Heart), which replaced that of “Bicentenario” a few months ago, will be withdraw, Andrés Izarra, Minister of Communication and Information, informed. Izarra pointed out that President Chávez, following the call by the CNE “has ordered to withdraw the campaign during the election period.” The campaign had visual elements that were



similar to Chávez reelection campaign, which has the slogan of “Heart of my Homeland.”

“Gato” Briceño joins Capriles’ “Road.” A few months ago, José Gregorio Briceño, governor of Monagas State, clashed with his former party because of his opposition to how the administration was dealing with an oil spill in Monagas. Now, expelled from the pro-government party PSUV, Briceño attended his first public meeting with opposition leaders. The brief encounter was attended by presidential candidate Henrique Capriles Radonski and several governors that support the Democratic Unity Panel. At the meeting, Briceño was invited to join the political project with which the opposition aspires to win next October elections.

Undecided will be the ones who decide. Luís Vicente León, president of Datanálisis, stated in a TV interview that “undecided voters will be the ones to define the winner” and that we’d better wait for the campaign to be fully developed in August-September, because the results in those months will “truly show what is the trend that will favor one of the political options.” Finally, León stated that candidates have to “convince groups to win the presidential elections without falling into partisanship,” because “undecided have always defined election” all over the world.

Opposition: “Caracas delivered”. The demonstration called “Walk for the Future” held by the Venezuelan opposition, took place in Caracas last Sunday. Armando Briquet, chief of campaign of Comando Venezuela stated that “*Caracas delivered and it was shown yesterday.*” An optimistic Briquet pointed out that “*The human wave (...) demonstrates that Venezuela is full with hope and that Capriles is the future for Venezuelans.*” Furthermore, Briquet underscored that in next October 7 elections, the people will chose “between a candidate that doesn’t have anything new (...) and a candidate that has proven to do things well.”

Chávez says that the best governors are on his side. During a visit in Barcelona (Anzoátegui State), president/candidate Hugo Chávez stated that the most responsible State is the one that “shares responsibility” with the people and regional authorities of the location where public services are located. President Chávez also pointed out that the opposition is “hypocrite” because it offers to solve problems with public services and that he is certain that “his governors” performance has been better than that of any opposition governor, because these latter use their posts “*to make businesses; they don’t care about the people; they are liars and hypocrites.*”

Ten minutes a day for “institutional” information. Several “institutional” ads were sent to Globovisión for the channel to broadcast them during the 70 minutes per week reserved for this purpose. Globovisión representatives charged before Conatel that the Ministry of Communication and Information (Minci) not only has limited to



determine hours and duration of the “institutional” ads, but it also has impose a specific broadcasting order, which “is an excessive exercise” of powers granted by law.

“How many deaths more?...” Deputies Ricardo Sánchez and Juan Carlos Caldera claimed that it’s unacceptable for PSUV party to announce that a new parliamentary committee has been appointed instead of putting the draft document up for discussion at the plenary session. *“How many deaths more are necessary for the government and PSUV to approve the law?”* Sánchez asked. Deputy Sánchez described the unilateral appointment of MUD deputies for the new committee as a political veto.

Legislative Tips

Additional indebtedness special law 2012. The instrument consists of 6 items, it authorizes the National Executive in the current fiscal year to approve public funds above the ceiling specified in the Special Law of Indebtedness for Fiscal Year 2012. It will also go to the partial payment of liabilities arising from social benefits to public sector workers.

Opposition will participate in new commission Disarmament Act. The point was taken on Monday by the coordination of La Unidad. Three of the four leaders supported the view of joining the single instance and Juan Carlos Caldera rejected it on behalf of Primero Justicia. Gomez Sigala said yesterday that *“beyond the individual items, we decided to participate in the commission for the contents and scope of the legal instrument.”*

AN approves additional funds for states and municipalities. The parliament in the session of July 18, 2012 approved 1.3 extra billion for the constitutional concept. Ricardo Sanchez said that *“these additional resources are a right and a conquest of our people, not a gift of centralism from which today all states and municipalities are victims.”*

AN workers protested at the Ministry of Labour. AN workers marched on July 18, 2012 to the Ministry of Labour to demand their discussion of collective bargaining, demanding *“immediate admission of the draft convention already introduced to the ministry”*. The protest led to a rapid response from the Ministry and pledged to press the accelerator in this matter.



Third time lucky? The Draft Law on Disarmament has been bouncing from committee to committee. The first document was prepared by the mixed committee of the National Assembly (AN), led by deputy Freddy Bernal; then, the presidential committee for disarmament surprised everybody with another proposal. Notwithstanding, just 30 days before its approval, the AN appointed a new committee on Tuesday, July 10, which excludes Bernal, to “unify” the different documents.

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ECONOMIC OVERVIEW

