



Weekly Report

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The BCV in the eye of the hurricane: not as bad as expected, the economy only shrank by 1.9% in the second quarter 2010 on a y/y basis

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Two weeks ago, the Central Bank of Venezuela (BCV) published growth and balance-of-payments figures for the second quarter 2010. In this weekly report, we will explain the behavior of economic growth figures, which surprised most analysts, because the economy shrank less than was expected. Additionally, we will present a preview of the prospects that will be published next week in our third Outlook Report.

The market was surprised and prospects were adjusted

With respect to economic growth figures (GDP performance), there is no denying that almost all of them were surprising: we at **Ecoanalítica** expected a y/y contraction of 5.7%, whereas Consensus put this value at -5.6%. The result published by the BCV of only -1.9% (y/y) led us to revise our short and medium-term prospects. According to the latest Bloomberg survey available, the median of market prospects expects that Venezuelan GDP will show a -3.8% (y/y) variation in the third quarter and -0.8% (y/y) in the fourth quarter of this year. We at **Ecoanalítica** are forecasting -1.6% and -1.2%, respectively.



Statistically, the results expected by Consensus (market) would imply a significant deterioration of the economy in the third quarter with respect to the previous one, and a sudden improvement in the last quarter of the year. In our opinion, this doesn't make much sense, due to the fact that the parliamentary elections will be held on September 26 (during the third quarter) and this will spark an increase in public spending.

In fact, figures released by the national Treasury show a significant increase in public spending as of the month of June. Furthermore, between January and June, supplementary appropriations have steadily increased with the approval of VEB 19.71 billion, for an average of VEB 2.29 billion each month; in July-August, supplementary appropriations reached VEB 12.54 billion, or VEB 6.27 billion per month.

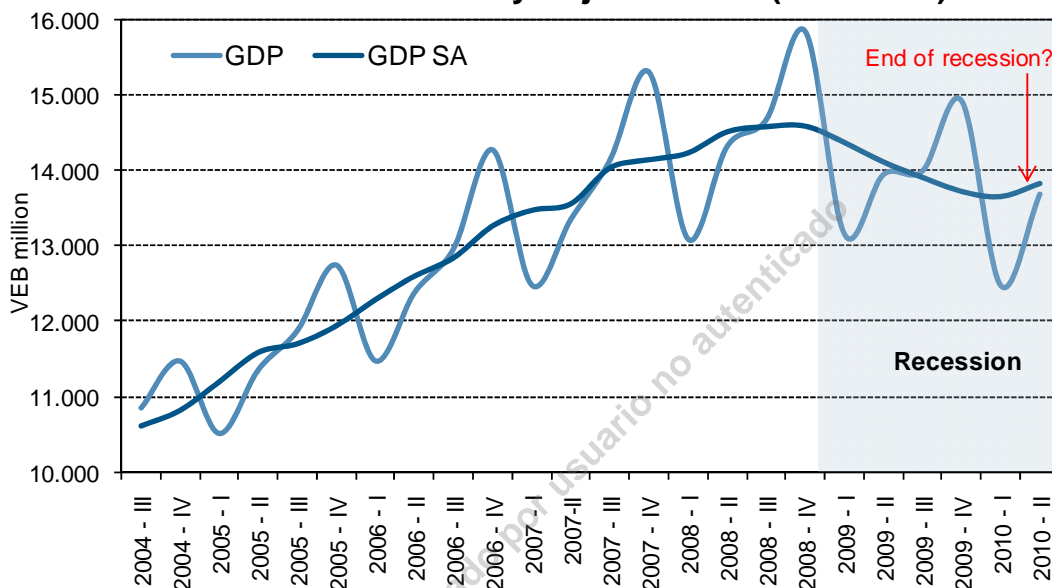
**Less
shrinkage
which implies
growth...**

What is also surprising about the fact that the economy only shrank by 1.9% during the second quarter 2010 compared to the same period in 2009 is that this growth rate also implies an annual quarter-to-quarter seasonally adjusted growth rate of 5.2%. In other words, production increase in the second quarter 2010 with respect to the first quarter of this year and if the economy continues to grow at this pace for four quarters in a row, the annual growth rate would be at 5.0%, which is a figure that everybody is longing to see again, but this is not a very realistic outlook, even with respect to the mid-term market.





GDP Vs. Seasonally Adjusted GDP (VEB 1997)



Sources: BCV and Ecoanalítica
Seasonal adjustment made by X12 method

But this doesn't imply that we have gotten over the hump

Last week, Nelson Merentes, president of BCV, said that the worst part of the country's economic crisis had been overcome and that the Venezuelan economy will start to grow again during the first quarter 2011, at a pace of at least 2% (y/y). While Merentes' opinion is not totally off the mark, we at **Ecoanalítica** are not as optimistic and our forecast is that y/y growth will be close to 0% in the first quarter 2011.

Without anticipated indicators it is more difficult to forecast

Most world economies use a series of indicators that are published every month, and which helped them have a better idea about the economic performance of their country and helps them estimate more precisely quarterly growth rates. In Venezuela, however, this is no longer possible, first, because the BCV monthly indicators of economic activity are published quarterly, along with the GDP and balance-of-payments quarterly results, and thus they are of little use in terms of monthly estimates, and second, because other indicators that are traditionally used to estimate economic growth, such as electric power consumption and car sales, have become less and less relevant.

The electric power crisis has restricted the supply of power so significantly that the y/y variation of electric power consumption, which used to be a fairly reliable measuring stick in terms of estimating economic growth, now



is completely irrelevant. The same thing can be said of the figures reflecting car sales. The automobile industry has been suffering significant restrictions in terms of the supply of assembly materials and spare parts due to the limited supply of foreign currency being liquidated to the sector by CADIVI, not to mention the rash of labor conflicts the current environment has plagued the industry with. The automobile industry (production) currently accounts for less than 0.6% of GDP and therefore, it can't be considered an indicator which accurately reflects macroeconomic conditions.

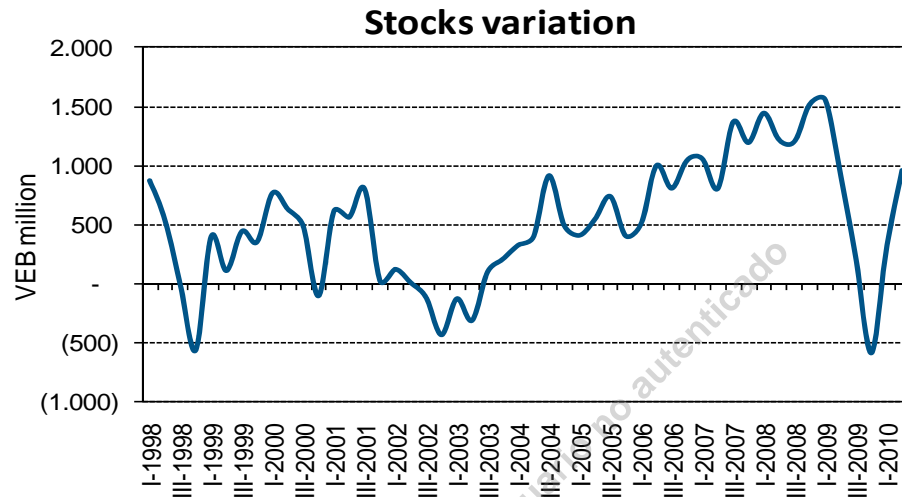
Another important indicator is the behavior of loan portfolio, which is published monthly. However, it also shows significant distortions, since almost half of it is committed to "mandatory loans" (quotas). Finally, data supplied by the different sectors through associations and chambers are not fully public and their publications don't follow a periodical pattern.

Stocks play a relevant role

GDP performance figures reveal a relevant indicator: stock variation, which is essentially a residual measure. Surprisingly, the chart corresponding to *quarterly stock variations* reported by BCV shows that the drop in stocks recorded at the close of the fourth quarter 2009 was even more significant than any drop recorded during any of the quarters during the General Oil Strike. The difference is due to the fact that during the Oil Strike, stocks fell for four quarters in a row, for a total decline of VEB¹ 983 million (at 1997 constant prices), whereas the drop in the fourth quarter 2009 was VEB 585 million.

¹ According to ISO code classification, VEB will be used to refer to amounts in strong bolivars (Bs.F.) instead of VEF that we had been using in our reports.





Sources: BCV and Ecoanalítica

During the first half of the year, stocks bounced back again and recover the same level they had before the current recession. Stocks' variation had a positive effect on GDP growth, accounting for 5% of domestic aggregate demand, two percentage points more than the average over the last ten years.

Are stocks the key?

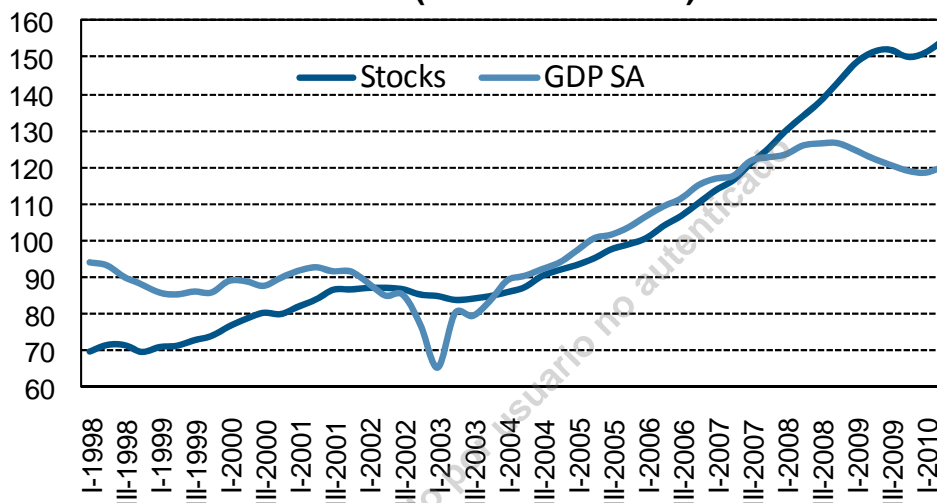
Since BCV doesn't publish the total stock volume but only their variation, that is, stock flow, we at **Ecoanalítica** developed a stock index that was shown on a graph along with a GDP index (seasonally adjusted to eliminate cyclic distortion), so as to have a better idea about the variation of stocks over the upcoming quarters.





Stocks Vs. GDP

Index (1998-2010 = 100)



Sources: BCV and Ecoanalítica

According to the chart, over the last decade, economy stocks grew more or less parallel to their production, although following a more stable pattern that exhibits drops only during the Oil Strike and in current recession. It is worth highlighting that with the recovery stocks recorded in the first half of the year, they reached a record high, and since our prospects as to medium-term growth are not very optimistic, it is likely that stock levels will remain constant, at best, or drop slightly, meaning that stocks won't be pushing growth.

In the midterm, economic performance will leave a lot to be desired

Even though the results for the second quarter have led us to revise our growth prospects for this year, adjusting growth from dropping 4.7% to only dropping 2.4% compared to 2009, our projections for the upcoming years continue to be pessimistic. Despite the fact that growth will certainly continue its increasing trend in 2011, it will be far below its potential, similar to the population growth rate (1.7% over the last ten years). The unfavorable macroeconomic environment, juridical lack of security and the Exchange policy will prevent the economy from reaching high growth rates like the ones that are typically seen in an economy that is coming out from a recession. Along with high inflation, this prevents economic growth from translating into increased wellbeing for the population.

Basically, with expected oil price levels, the Venezuelan economy is entering an initial recession stage and, after a slight recovery (rebound),



which, notwithstanding, shows poor growth rates, private sector will lose weight while the public sector gains influence as well as the new property modalities stimulated by the State, which still exhibit a very poor performance as to their potential to generate sustained growth. Therefore, everything indicates that the country has entered a new cycle, a period of limited expectations and meager growth, which, among other things, will not allow for creating enough new jobs.

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Economic Tips

Chávez boasts about GDP recovery. President Hugo Chávez dismissed the fifth consecutive drop in Gross Domestic Product (GDP) that shrank 1.9% in the second half of 2010, and assured that “recovery is remarkable” if it is compared to the first quarter (-5.8%). *“The Central Bank admits that we have started to recover in the second quarter,”* Chávez added. However, the President admitted that the Venezuelan economy is “in recession” due to the *“global crisis, the drop in oil exports and the electrical crisis”* the country went through.

And employment will recover. The president of the National Statistics Institute, Elías Eljuri, stated that unemployment rate is currently at 8.7%, as a result of the 1.9% decline of the economy in the second quarter 2010. Eljuri assured that unemployment rate for the upcoming months will fall and that it would close 2010 at 7%. *“Formal employment expanded from 49% to 56% and informal employment has dropped from 51% to 44%, with an improvement in job quality.”* He added that with higher investment levels, employment will grow: *“policies over the next months have to bring about an increase in employment and economic activity.”*

Imports: private fall, public grow. In 1S2010, private sector imports amounted to US\$11.1 billion, which implies a 33% decrease from 2009, the lowest level since 2006. It's worth highlighting that the all components of the importer private sector show a decrease. Furthermore, State's purchases abroad over the same period reached US\$6.27 billion, which translates into a 34.4% jump with respect to the same period in 2009 and in the highest figure since 1997.

Per economic destination. In the case of the private sector, imported products earmarked for final consumption lost 37%, production input purchase declined fell 30.6% and machinery and equipment purchases contracted 33.7%. The State doubles imports earmarked for final consumption, maintains input imports unchanged with a tiny increase of 0.7% and rises purchase of machinery and equipment by 18.7%, basically, through the acquisition of thermal power generation plants.

Non-oil exports continue to shrink. According to Balance-of-Payments figures, non-oil exports reduced 7.4%, comparing the second quarter 2010 to the same period in 2009.





Capital flight reaches US\$8.687 billion in the first semester. According to figures expected for the Balance of Payments, published by the Central Bank, capital outflow during the first six months of the year recorded US\$8.687 billion, i.e. 10% over the same period the previous year.

US\$2.4 billion were paid to the China-Venezuela Fund. During the first six months of the year, Pdvsa exported fuel oil to China equivalent to US\$2.4 billion, as repayment for the China-Venezuela Fund that both countries created in 2007. In 2009, Pdvsa paid the equivalent to US\$4.2 billion. The Fund will be renewed in October, when China's Development Bank will contribute US\$4.0 billion and Venezuela US\$2.0 billion to the Fund.

Supplementary appropriations for VEB 33.0 billion. In 2010, the National Assembly has authorized supplementary appropriations for VEB 33.0 billion to cover extra-budgetary expenditure. Consequently, 2009 fiscal budget goes up to VEB 192.0 billion, from VEB 159.4 billion included in the initial budget.

42% of public works were completed over the first seven months of the year. Of the VEB 7.2 billion approved for public works and housing in 2010, VEB 4.5 billion were executed during the first seven months of the year, or 42% of the total; ministries with higher budgets, in turn, had executed more than 50%:

Coexistence continues. The BCV announced that "old" bolivar bills and coins will co-exist with "strong bolivar" bills and coins. The Bank asked businesses and citizens to try to preserve current bills and coins, use cash in their transactions and pay and demand exact change.

Sitme figures. To date, US\$1,561.7 million have been negotiated through the new Integrated System for Foreign Currency Transactions (Sitme), averaging US\$26,9 million a day, with an implicit exchange rate of VEB 5.3/US\$. Last week the traded amount reached US\$139.6 million, US\$4.2 million more than last week when braided US\$135.4 million.

Interest rate. The lending rate for the third week in August was at 17.3%, down by 215 base points compared to the previous week. Time deposits and savings rates were at 14.5% and 12.6%, respectively. This reflects a 1 base point increase for time deposits while savings remains steady.





International reserves. International reserves dropped by 0.3% going from US\$28,476 million during the third week in August to US\$28,376 million during the fourth week in August. Compared to the same period last year, international reserves dropped by 9.0%.

Monetary liquidity. Monetary liquidity for the third week in August was down by 1.3% compared to the previous week settling at VEB 258.39 billion, and up by 9.6% year to date in nominal terms and down by 17.7% compared to the same period last year.

Oil Tips

Exports to US decreased. Venezuelan oil exports to the United States decreased by 12.7% during the first half of 2010, reporting a daily average of 977,100 barrels, against 1.12 million barrels per day exported during the same period of 2009, so was published by the US Energy Information Agency (EIA). EIA numbers also indicate Venezuela sold an average of 897,000 barrels per day during June, which represents a 27% y/y decrease.

And the demand falls. The EIA also indicated US's oil demand, the world's largest oil consumer, was slightly lower than the one expected by analysts. However, it is still at its highest level since October of 2008. The agency reduced its June oil demand numbers by 0.3%, although the consumption record was 2.5% higher in y/y terms, reaching its highest level in one year.

Proven natural gas reserves increase. Venezuela is now ninth in the list of countries with the largest proven natural gas reserves and the first in Latin America, after its reserves increased reporting 185.24 normal trillion cubic feet (tcf), so was published in Official Gazette N° 39,486 of August 27. This increase was originated by a discovery in block Cardon IV of the Rafael Urdaneta Project in the Gulf of Venezuela.

Nationalized drills are operative. The Minister of the People's Power for Energy and Oil and president of Petroleos de Venezuela (Pdvsa), Rafael Ramirez, activated two new nationalized drills in the Monagas State, along with the absorption of 87 workers who were previously subcontracted by drill operating companies. During 2009, Pdvsa incorporated 10,500 workers from nationalized companies. He also indicated the activation of three more drills was already scheduled, and the activation of the Bicentenario base of drilling operations, with only nationalized drills.



Santa Ines Refinery for 2012. According to statements issued by Pdvsa's vice president of Refining, Trade and Supply, Asdrubal Chavez, and the governor of Barinas, Adan Chavez, the first stage of the Santa Ines refining complex should be completed by 2012, with an initial refining capacity of 60 thousand barrels per day, which will eventually reach 100 thousand barrels per day, to satisfy the energy demand of the states of Apure, Barinas, Merida, Portuguesa and Táchira, calculated at 74.4 barrels per day. The refinery will generate approximately 2,500 direct jobs.

Serious concerns about Pdvsa's financial statements. The Venezuelan Federation of Public Accountant Associations' expanded directory held a three-day meeting in Caracas in which they agreed to review Pdvsa's 2009 annual management report and present a document regarding the company's financial results, since they indicated the company meets the generally accepted accounting principles. However, it is a great concern for them how the company's liabilities have increased, especially their accounts receivable, since, as they indicate, this seems to be happening due to cash flow problems. In their press release they also talked about the need to increase said financial statements' transparency.

Curacao's Isla refinery reactivated. Several minor units of the Isla refinery located in Curacao were reactivated after having spent several months inoperative; however, the refinery's key catalytic cracker will not resume operations for another few weeks. The refinery has a refining capacity of 335 thousand barrels per day.

New liquefied gas presentations. With the purpose of fighting speculation and stockpiling, Pdvsa Gas Comunal is carrying out different plans to sell liquefied oil gas canisters, in presentations of 10, 18 and 43 kilograms, at regulated prices. These plans were already activated in the states of Aragua, Anzoátegui, Apure, Barinas, Bolivar, Carabobo, Cojedes, Falcon, Guárico, Merida, Monagas, Nueva Esparta, Portuguesa, Vargas and Zulia, and consumers can purchase a 10 kg canister for 3.7 bolivars, an 18 kg canister for 6.7 bolivars and a 43 kg canister for only 16 bolivars.

Belarus signs an agreement with Venezuela. The president of Belarus, Alexandr Lukashenko, said his country would import approximately 10 million tons of Venezuelan oil from 2012, thus reducing its oil dependency with Russia. Lukashenko's statements took place during a visit to the Mozir refinery, which will process Venezuelan crude oil to be exported to other European countries. Earlier this year, the Venezuelan President, Hugo Chavez had said Venezuela would start selling 80 thousand barrels per day to Belarus.

Only four OPEC countries contracted. According to the International Monetary Fund (IMF), only four OPEC member countries suffered economic contractions during 2009; Kuwait contracted by 2.7%, United Arab Emirates contracted by 0.7%, Angola by 0.4%



and Venezuela by 3.3%. In the same report, the IMF predicts that all OPEC countries will report growth in their economies boosted by the recovery of oil prices and the substantial increase in China's demand, except for Venezuela, which is expected to contract by 2.6% in 2010 and report a slight 0.4% growth in 2011. The price of an oil barrel now seems to be a necessary condition, but not enough to guarantee economic growth.

International oil baskets. At the close of the New York market last Thursday, September 2, the WTI was at US\$74.96/bl, showing a 2.2% increase compared to the US\$73.4/bl of the previous Thursday. The Brent increased by 3.3% to reach US\$77.3/bl, compared to US\$75.1/bl of Thursday, August 26.

Local oil basket price. The Venezuelan oil basket price increased last week, to close at US\$72.8/bl on Friday August 27, up by US\$5.3 from the US\$67.6/bl registered the previous week. Meanwhile, the basket's annual average kept constant in US\$69.9/bl.

Business Sector Tips

Cadivi: US\$853 million for the aeronautical industry. The Venezuelan Currency Administration Commission (Cadivi) reported that from January 1 to August 23 of 2010, US\$853.5 million were authorized for the aeronautical sector. IN a press release, Cadivi indicated the amount authorized during 2010 represented 64% more than the US\$517.5 million authorized by the Commission to be liquidated for the aeronautical sector during the same period of 2009. In a meeting between the exchange authority and aeronautical and tourism sector companies, those present stated the authorization and liquidation of currency for airlines had improved considerably during this year for a sector that promotes tourism in Venezuela.

Debt in subscription TV. Since 2008, subscription TV companies accumulate a debt calculated between US\$200 million and US\$250 million. Mario Seijas, president of the Chamber of Subscription Television (Cavetesu) explained *"there are accumulated debts in hardware and intangible assets such as programming, owed to 5 or eight suppliers that demand payment in US\$; we're trying to figure out how to satisfy their demands."*

Pay your debts. The president of the Colombian Industrials' National Association (ANDI) said, regarding the reinstatement of commercial relations between Colombia and Venezuela, that a new kind of renewed institutionalism was needed in this bilateral relation, highlighting the fact that Venezuela's payment capacity would determine



whether or not the trust in the Colombian-Venezuelan trade can be reinstated. Colombian companies await the payment of approximately US\$800 million in exports made to Venezuela since 2008 which haven't been honored by national entrepreneurs due to the difficulties to obtain foreign currency imposed by Cadivi.

Who's first? After the agreements made in the public and private sectors of both nations, Colombian airline and pharmaceutical sectors will receive the first payments, for approximately US\$200 million. The rest, nearly US\$600 million, will be honored as long as Venezuelan authorities are able to "confirm" the existence of such debts by Venezuelan importers (some from 2008) with Colombian companies. The rounds of payments to Colombian companies are expected to begin by mid-September, to then find the way to reactivate commerce.

Imports from Colombia will retake their pace. Vice President Elías Jaua informed that imports from Colombia to Venezuela will be progressively reactivated. A new commission will be created to evaluate import procedures and streamline permit granting.

Even steel is imported from Colombia. Traditionally Colombia was an importer of Venezuelan steel; however, in the first half of 2010, the iron and steel industry Paz del Río sold 5,000 t of the product, the first time that Colombia exports steel to Venezuela, even though the exported volumes are not significant, according to the firm's vice president, Gilson Mo-raes.

Trade balance with Iran grows. The national Government has signed 57 commercial exchange agreements with Iran in the past five years, some of which have allowed the installation of plants in various sectors such as agricultural industry, automotive, textile, electronic, construction, oil. Therefore, Venezuela's trade balance with Iran has gone from US\$1 million in 2004 to US\$79 million in 2010.

Commercial exchange with the EU down. According to information released by the Institute of National Statistics, commercial exchange between Venezuela and the European Union dropped by 18% during the first five months of 2010, reaching US\$1.9 billion, compared to the US\$2.3 billion of the same period of 2009.

Guri: Just two meters. The Guri hydroelectric dam is about to reach its optimum level of 271 meters above sea level, after placing on Friday over 269.72 meters. People's Power Minister for Environment, Alejandro Hitcher reported last Friday that the main source of generation in the country "lacks 01.28 meters to reach their optimum level". Hitcher also noted that, until July, the Government had installed 1265 more than megawatts. The Guri Dam is the supplier of more than 70% of energy consumed in Venezuelan and the volume is rising at an average 15 to 20 centimeters a day, so it is possible that by the next week to reach its normal height of 271 meters.



Is the electric emergency over? Even though the electric emergency is officially “over,” electric failures and general power shutdowns (especially outside the capital city) are still a reality, negatively affecting the national industry. According to the Situation Survey of the second quarter of 2010 carried out by Conindustria, 76% of companies in the manufacturing sector consider the electric rationing is one of the factors hampering production. According to the president of Conindustria, what aggravates this situation is the fact that power cutbacks are untimely, which keeps companies from planning the shutdown of production lines in order to avoid machinery damages and delays in productive goals.

Recession affects sales volume. In a scenario in which price increases exceed average families’ purchasing power thus reducing consumption, Central Bank statistics reported that during the first semester of 2010, sales volume, both retail and wholesale, experienced an 8.9% contraction. Only retail sales contracted by 12.4% during the first semester, while wholesale sales reported a slight growth by 1.1%. Analyzing the behavior of retail sales, foods, drinks and tobacco in specialized establishments decreased by 29.6%; textile products decreased by 19.6%, pharmaceutical products, medicines and personal care products decreased by 30.4% and vehicles by 36.9%.

Fedeagro: Price adjustment now! Fedeagro summoned an extraordinary assembly to evaluate the agricultural crisis. Pedro Rivas, president of Fedeagro, said “*the economic pressure agricultural producers have been subject to has caused them to lose productive capacity,*” a situation originated from a collapse of national production. Rivas said the sector’s costs had increased by nearly 80% in the past three years, and this increase had not been acknowledge in the price adjustments granted to the sector. Industry representatives claim the sector need a price adjustment as soon as possible, in order to guarantee not only their reinvestment in production for the upcoming cycles, but to pay the debts they have contracted.

Another 30 food companies. The National Administration announced in the *Official Gazette N° 39,494* on Tuesday August 24, the reorganization of the tens of food production companies owned by the State by ordering the ascription of 30 new companies to Corporación Venezolana de Alimentos (Venezuelan Food Corporation, CVAL), in order to centralize their management and operation and “*efficiently continue with the new model of production social relations and the effective articulation of the agricultural industry.*” Among the companies ascribed are the ALBA mixed companies in the fields of rice, pulses, pork cattle, poultry, fish, dairy.

Movistar suspends Roaming service. Due to debts ranging from 3 to 6 months in service payments to foreign operators for the processes related to the acquisition of foreign currency through Cadivi, Movistar de Venezuela was forced to suspend International Roaming services in 13 countries. Augusto Moronta, vice president of



Marketing of the Venezuelan branch of Telefonica, ruled out for now the possibility for this currency authorization delay situation to affect other value added services. However, the acquisition of new telephone devices has been affected by this situation. He also warned that, should this situation continue, other companies might be joining them in the measure of suspending roaming services.

Meanwhile, the Government... National authorities decided to review the paperwork that telecommunication companies are currently required to submit in order to obtain foreign currency, in order to take care of the current debt situation and avoid similar circumstances in the future, said the telephone company in a press release.

Funds for cement companies. President Hugo Chavez authorized US\$117 million for the total payment of Fabrica Nacional de Cementos' shares of stock, a company that was nationalized on June 18 of 2008. This payment, to be made in four installments, corresponds to the transfer of shares by the French company Lafarge to the Venezuelan state, to be acquired by Corporacion Socialista del Cemento with resources from the National Development Fund (Fonden).

Christmas season in danger. The economic recession, the public spending reduction plan, the restriction of foreign currency through Sitme and the elimination of the parallel currency market, have brought serious consequences to the importing sector. Additionally, the last issuing of the International sovereign bond 2022, initially thought as a legal way to obtain foreign currency, left out a representative group of companies. Importers have expressed their concern for the shortage of supplies to produce basic and highly demanded goods, especially during the last quarter of the year. The most affected ones are importers of home appliances, telecommunication devices, liquor, auto-parts, vehicles, personal care, textile, footwear and other mass consumption goods.

Expensive rice for cheap oil. According to information reflected by international news agencies, Guyana is going to export to Venezuela 64.000 metric tons of rice, each of which will be canceled at \$700, according to the leader of the Association of Rice Producers of that country, as part of payment for the oil shipments sent from Venezuela. For every kilo of imported rice will be canceled VEB 1.8. Taking into account the official exchange rate of VEB/US\$ 2.6, that price is more than 50.0% more than the price paid to domestic producers, who receive a maximum of VEB 1.2 by one kilo of rice harvested. Even, the amount paid for each kilo of rice from Guyana exceeds 7.0% the equilibrium price set by domestic producers of VEB 1.7.





World Crisis Tips

Bernanke admits weakness, but claims they are prepared. The president of the Federal Reserve, Ben Bernanke, acknowledged once again the economy's recovery is getting complicated, warning of a possible economic cool down. However, he said the Federal Reserve was prepared and capable to face this situation and take the necessary stimulus measures to avoid a relapse. This statement was positively received by the stock markets, with the Dow Jones and Standard & Poors reporting a 1.7% growth after the announcement.

Review only made things worse. Haver Analytics said the news about the US GDP variation review down indicating a 1.6% growth as opposed to the previously published 2.4% were disappointing. However, it is worth mentioning that this review was higher than consensus expectations (1.4%), and it represents the fourth consecutive month of growth, since the end of the recession. The decrease is mainly due to the growth of inventory accumulation by 0.6% and a deterioration of the trade balance deficit by 3.4%.

Domestic demand did improve. As to the United States domestic demand for the second quarter of 2010, a 4.3% growth was reported, better than the previously published number, mainly due to a 1.7% y/y increase in private consumption. The numbers also show the gross fixed capital formation increased by 5.3%, compared to the same period of 2009. Government consumption was revised at 4.3%, down from the previous 4.4%.

Consumption exceeds expectations. Private consumption numbers exceeded expectations for July, after the contraction reported in June (-0.0%), increasing by 0.4% when projections indicated the growth would be by 0.3%. This variation is mainly due to an increase in home service expenses (7.1%); "others" (4.3%); transportation (3.3%); and health (2.7%).

And consumer confidence increases. According to the news agency Bloomberg, the *Conference Board's* Consumer Confidence Index increased by 4.9% during August, going from 51 points to 53.5 points. This increase exceeded the expectations of economists interviewed by the news agency, most of whom estimated the index to



reach 50.7 in August. This result helps reduce the existing pressure regarding the concerns in terms of consumer spending.

Delayed payments improve a little, but stay high. The number of mortgage loans with delayed payments still reports very high levels, even though it had a slight improvement compared to the previous quarter. During the second quarter of 2010, the level of mortgage loans with delayed payments reached 9.9%, compared to 10.1% in the first quarter, when pre-crisis levels were near 5.8%. The rate reported in the second quarter translates to 44,508,533 mortgage loans with delayed payments. Meanwhile, the number of foreclosures has decreased when compared to the highest levels of 2009. However, the yearly foreclosure rate is 4.7%, four times more than in 2006.

Economic activity loses momentum. The rate at which the US economic activity had been expanding lost some momentum during August, according to *The Institute for Supply Management-Chicago's* Business Barometer, going from 62.3 points in July to 56.7 points in August. The main reason for this loss of momentum is the restriction of the manufacturing activity.

Concerns about the European economy lighten up. The Economic Sentiment Indicator (ESI) published by *The European Commission* for all 27 countries in the European Union reached 102.7 points in August, up from the 102.0 reported in July. In the indicator for 16 countries, the number reached 101.8 points, 0.8 more than in the previous month. These results are higher than the index's historic levels. The index is based on the opinion of approximately 130 thousand executives and 40 thousand consumers during the first two weeks of each month. The countries that showed a continuous improvement in their economic sentiment were Germany, the United Kingdom and France.

Japan's inflation is always a problem. Japan's June inflation reported a 0.3% decrease to reach a downwards variation by 1.6% in the last three months. With this result in June, the accumulated number for the last six months reached -0.6% and -0.9% for the last twelve months. Despite all the crisis distortions, during which it even came to accumulate positive inflations, Japan has not been able to overcome its deflation problem.





Political Tips

Chavez back in Cuba. The Venezuelan President, Hugo Chavez, held a meeting with the Cuban leader Fidel Castro and his brother Raul last week in Havana during an unannounced visit that lasted several hours, according to the official media. Chavez and Castro addressed various issues of international current events, said the press release, along with several pictures published by the state TV channel and the website Cubadebate. Both leaders particularly addressed *“the high risks of a nuclear war currently threatening humanity,”* practically the only topic Fidel Castro has talked about in his last public interventions and articles called “Reflections.”

The base of the government’s campaign. In different opportunities, President Chavez and other PSUV leaders have stated the need to avoid the opposition’s success since that would bring anarchy, violence, the elimination of social benefits, among other things. Recently, Chavez said: *“We can not allow them to get Venezuela off track and drive it down a cliff because it is our children who come in that train.”*

Opposition kicked off with a march. Screaming *“Yes to life, no to death,”* hundreds of citizens took the streets of Caracas in response to a call made by female representatives of various opposition parties to protest against the high crime rate and demand the National Government to take measures in that regard. The demonstration took place calmly and with no incidents to regret. Different political organizations took advantage of this mobilization to raise funds to finance future electoral activities.

Division in the opposition’s core. The political movement Voluntad Popular (VP) issued a press release stating some critiques to the opposition strategy of MUD for the election of September 26. The most important issues addressed by VP included: message unification, changes to the current campaign slogan, changes in some candidacies, among others.

El Aissami: New York Times is an immoral newspaper. The minister of the People’s Power for Internal Affairs and Justice, Tareck El Aissami rated the American newspaper The New York Times as immoral after it published a note last Monday called: *“Venezuela, deadlier than Iraq.”* Minister El Aissami said this note corresponded to *“an immoral, cynical and hypocritical newspaper that applauded the United States invasion of a country and now intends to teach us about human rights.”*



The note made reference to alleged numbers indicating Venezuela's rate of violent deaths was higher than in the Mid East war.

CNE carried out a production audit on electoral machines. According to the electoral schedule, the production audit process of all voting machines to be used in the upcoming election of September 26 was initiated last Wednesday. The process consists of programming each one of the 36,773 machines to be used in the parliamentary election plus another batch to be available in reserve to solve any contingencies that may arise. CNE and political organization technicians will make sure the software used is the same that was audited last August 13, which works with a code that was shared by all the parties that attended said electoral process.

Supreme Court of Justice authorized extradition of Nelson Mezerhane. The Supreme Court of Justice considers the extradition of Nelson Mezerhane to be necessary to subject him to the jurisdiction of Venezuela's ordinary courts, its neutral judges. The Public Ministry requested the initiation of all legal procedures for the active extradition of Mezerhane before the Forty-Third Court in Control Functions of the Judicial Penal Circuit of the Caracas Metropolitan Area, for the alleged commission of the crimes of unlawful authorization of loans, distraction and/or appropriation of financial resources, fake financial information, withholding information in the institutional statement, association to commit a crime and fraudulent use of public funds.

Do not alter institutions. The Ombudsman's office issued a statement last Thursday about the protests that took place last Wednesday and Thursday near the National Assembly and the ombudsman's office, with the intention of altering the regular operations of these two institutions. The ombudsman's office rejected the accusations of alleged use of both institutions "*as an electoral campaign mechanism*" and reminded the execution of "*political*" activities without the corresponding authorization violates the legal framework.

Institute of National Statistics (INE) released 2009 crime figures. According to the Venezuelan Institute of National Statistics' annual report, the crimes with the highest incidence in 2009 were homicides, theft, personal injuries, cons and robberies. The data compiled indicates a total of 2,364,452 crimes were committed in 2009. 1,428,612 (60.42%) of citizens were violently robbed. Of that total, only 335,452 made formal reports to the authorities. The second most frequent crime was theft, with almost 500,000 victims (20.64% of the total). Nearly 77,000 people presented injuries



(3.24%). Approximately 27,000 people were victims of kidnapping (1.14%) and there were almost 50,000 cases of corruption (2.09%) and over 21,000 homicides (0.89%).

“Ballistic control” to be proposed at the National Assembly. The director of the National Bolivarian Police, Luis Fernandez, will submit a proposal before the National Assembly’s Defense Commission regarding ballistic control to be incorporated to the Law of Disarming approved in first discussion early this year. The public clerk explained this proposal’s purpose was to make a contribution to this new legal instrument by suggesting the codification of projectiles with a serial that allows the identification of whoever shot them. *“Should a gunshot corpse appear, with that code we would be able to determine what officer that projectile was assigned to and we’ll be able to go further in the investigation.”* Officer Fernandez rejected the opposition’s intention to try to solve the crime problem merely by mentioning the need to sanction the Law of Disarming.

Extraordinary session to approve law of disarming. The president of the National Assembly, Cilia Flores, informed of an extraordinary session scheduled for next week, after the AN declared itself in recess two weeks ago, to carry out the second discussion of the law of disarming that proposes a sentence of 10 to 12 years of prison to anyone carrying guns without a permit.

2600 ex followers of Proyecto Venezuela joined the Psuv. Last Friday, in an act that took place in the Luis Mariano Rivera Theater in Cumana, 2600 ex-members of the political party Proyecto Venezuela joined the United Socialist Party of Venezuela (PSUV).

Sumate invites citizens to report abuse in the electoral campaign. The nongovernmental organization Sumate issued a public statement inviting any citizen who detects a violation or abuse in the electoral campaign, to make the corresponding report through the channels provided by CNE, including Electoral Supervisors, CNE Regional Electoral Offices located in the capital cities of all 24 federal entities of Venezuela, the CNE Political Participation and Financing Commission and the link DENUNCIAS – Electoral Campaign Supervision on the CNE website. Reports shall be supported by pictures and/or video, along with an explanatory letter.

Franklin Brito passed away. Franklin Brito died on August 30 of 2010 at the Military Hospital in Caracas. According to the autopsy, the cause of death was a septic shock and a respiratory arrest caused by protein and caloric malnutrition generated by the hunger strikes he subject himself to in several occasions to regain ownership of his lands expropriated in 2004 by the National Institute of Lands.



ECONOMIC OVERVIEW

