



Weekly Report

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*Fiscal spending:
Is this the Government's last
weapon?*

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Now that the parliamentary election is over and the results are in and have been digested, there is no doubt that in the medium term, the Administration will focus on reconnecting with voters and look for ways to win back the votes it lost. How does it plan to achieve this? In our opinion, the only thing that has worked for the Administration so far is spending. The question is, will this be enough this time?

**Oil, it always
comes back to
oil**

In Venezuela, it's clear that when oil prices are up, all budget restrictions disappear and the Administration can increase spending without having to increase taxes. This very privileged circumstance enjoyed by other governments that are fortunate enough to have an abundance of extremely valuable natural resources allows them to purchase the will and allegiance of key players and/or bankroll legions of followers. As we have mentioned in previous Reports, more than 80% of the swing in the President's popularity can be attributed to the increase (or cutbacks) in public spending. In other words, the President's ability as a great communicator, the radicalization process being implemented in the country, and the lack of an opposition

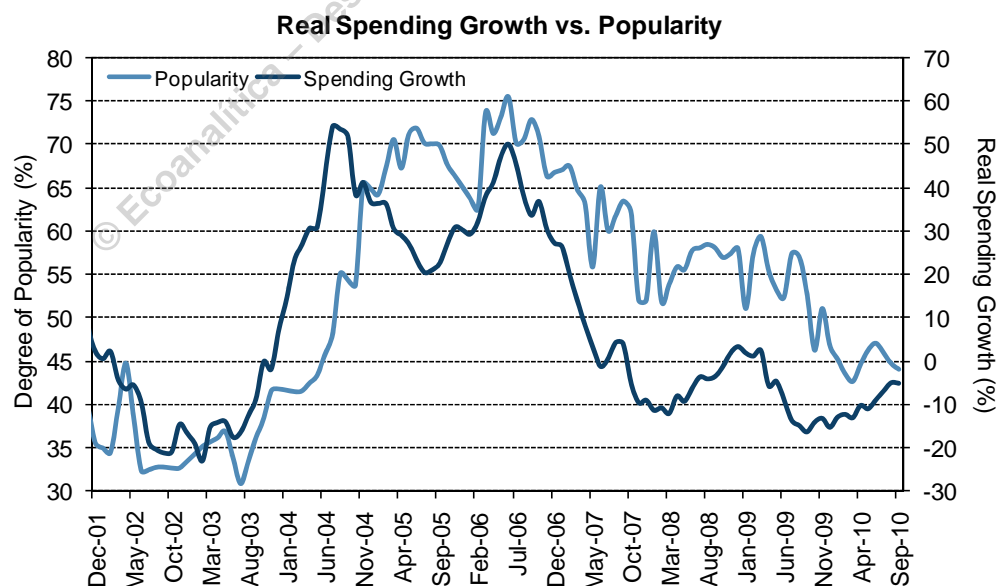


figurehead to stand against the President, among other things, represents the other 20% possible swing in popularity that could be reflected.

He's not infallible... It's just that there was a lot of cash involved

Many Venezuelans believe that the President is infallible, that any mistake he may make is all part of a more complex strategy. He's a great communicator that through an ironclad control of the media and weak institutions is able to hypnotize Venezuelans into supporting him without giving them anything in exchange.

Without wanting to take anything away from Hugo Rafael and any positive qualities he may have as a communicator and a candidate, but the main reason which explains his high, although dropping, popularity ratings with the people is public spending. The next graph shows public spending during the last few years in real terms and the President's popularity ratings.* The first thing that stands out is the high correlation level between the two variables (78%). In other words, this means that 8 out of every 10 times public spending increases (or gets cut), the popularity of the President also increases (or drops).



Sources: Oficina Nacional del Tesoro (MF), BCV, Datanálisis and Ecoanalítica

Each time it needs more

The affect on the President's popularity is not the same if you increase public spending by say VEF 20.0 billion when the initial Budget was set at

* The data comes from surveys taken by Datanálisis.





VEF 80.0 billion then if the initial Budget was set at VEF 180.0 billion. The higher percentage of increase in spending compared to the initial Budget amount, the more of a positive effect this increase in spending will have on the popularity ratings of the Administration, and vice versa; the higher percentage increase (or cutback) in spending in real terms, the more significant the increase (or drop) in popularity.

By simply working the numbers backwards, with the President's popularity as a dependent variable, and independent variables being public spending in real terms and the variation in percentage during the last 12 months, you find that 81.4% of the variation in the President's popularity can be explained by the level of public spending and its variations. In other words, this means that only 18.6% of the President's popularity has to do with other factors not related to public spending.

What happened in 2010?

Keeping in mind the analysis we just made, we can present a view of what happened during the last parliamentary election held in September 2010. First, according to the National Treasury Office (ONT), public spending between January and August 2010 was at VEB 140.1 billion, which compared to the same period last year was up by 20.2%, but in real terms it was down by 7.1%. To resume, the Administration cutback on public spending, being this was a very risky move given that 2010 was an election year in the middle of an economic recession. The Administration gambled and lost.

BALANCE FISCAL DEL GOBIERNO CENTRAL (VEF Millones)	August 2009	August 2010	Nominal Variation	Real Variation	January-August 2009	January-August 2010	Nominal Variation	Real Variation
Total Revenue	19.416	22.965	18,3%	-9,0%	138.335	137.603	-0,5%	-23,4%
Current Income	14.868	15.415	3,7%	-20,3%	108.659	111.640	2,7%	-20,9%
Ordinary revenue	10.517	12.923	22,9%	-5,5%	80.928	99.126	22,5%	-5,7%
Oil Revenue	3.248	6.103	87,9%	44,5%	29.106	33.885	16,4%	-10,4%
Non-Oil Revenue	7.269	6.819	-6,2%	-27,9%	52.011	65.240	25,4%	-3,4%
Extraordinary income	4.352	2.492	-42,7%	-56,0%	27.731	12.514	-54,9%	-65,3%
Financing Requirements	4.547	7.550	66,0%	27,7%	29.676	25.963	-12,5%	-32,6%
Total Expenditure	13.782	18.520	34,4%	3,3%	105.046	125.739	19,7%	-7,9%

Sources: BCV, ONT and Ecoanalítica

Why didn't it increase spending?

So, the question one has to ask is: why, if 2010 was an election year, did the Administration cut back on spending? The first answer that springs to mind is that the Administration didn't have the resources to spend. At **Ecoanalítica** we don't believe that this is the answer, because according to our estimates, at the close of August, extraordinary funds in local currency were at VEB 76.7 billion.





Government Resources	August - 2009 (US\$ bn)	August - 2010 (US\$ bn)	Variation (%)
In VEF	27,8	29,5	6,2%
BANDES	0,1	0,6	500,0%
BDT	0,3	0,4	33,3%
Deposits in the financial system	20,5	18,4	-10,3%
Fondo Miranda	1,6	2,8	75,0%
National Treasury	3,4	7,6	123,5%
FONDEN	1,9	1,5	-21,1%
In USD	14,1	12,3	-12,8%
FONDEN and National Treasure	7,1	7,6	7,0%
Other Funds	6,2	2,0	-67,7%
PDVSA	0,8	3,0	275,0%
Total	41,9	41,8	-0,2%

Source: Ecoanalítica

So, if this is the case, then there was another reason for the cutback in spending. There was a plan. At **Ecoanalítica**, we have two plausible theories:

1. The Administration decided not to increase spending in order not to complete lose control of inflation and the exchange market. This would be a novel idea for the Chavista Administration, since up until now the standing solution to most of its problems has been to throw more money at it, in other words, increase public spending (in order to generate growth), to the detriment of any hope of controlling inflation.
2. The Administration felt confident that the institutional changes it had implemented with respect to the electoral process, specifically redefining voting districts; it's control over the State; and its last minute effort to increase spending and spread the wealth around (last few weeks before the election), would be enough for it to win the election without it having to substantially increase public spending. These resources would be needed in the future for the real election, the 2012 presidential election.

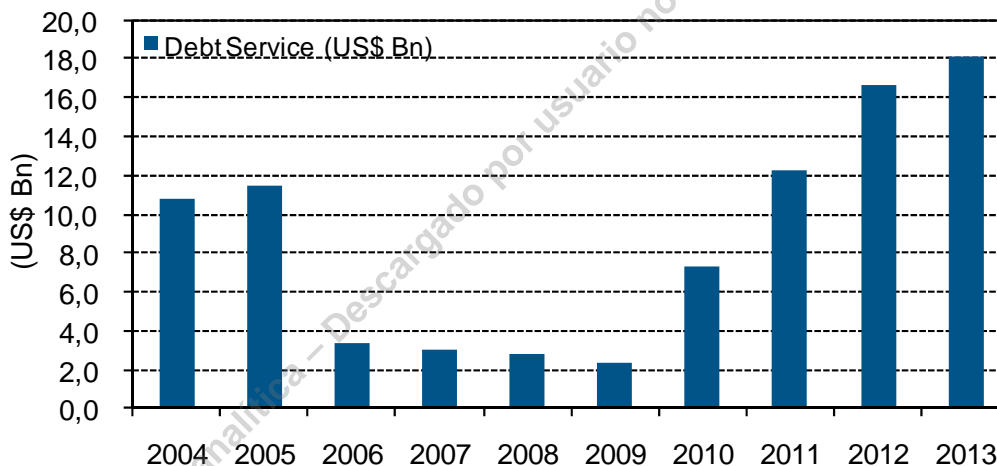
Chávez always learns

Taking into account the effect public spending has on the popularity rating of the President, and the less than ideal results the chavismo faction got in the last election, there is no doubt that Chávez will go back to doing what he does best: spend. This is why our outlook for the medium term is a substantial increase in public spending. In 2010, we estimate that the Central Government deficit will be at around the equivalent of 3.7



percentage points of GDP. In 2011, we expect this amount to increase slightly to 4.1 percentage points of GDP. Alongside this increase in public spending, we also expect the Administration to be quite aggressive with its borrowing policy. It's important to point out that between 2004 and 2008, the government's public debt service averaged US\$6.30 billion; during the 2009-2013 period it will be at around US\$11.30 billion. So, this increase in spending that we are predicting will be partially backed by an increase in borrowing.

Public debt service of the Central Government



Sources: MPPPF and Ecoanalítica

... And, what has been accumulated will also be spent

The fact that the President's popularity depends so much on public spending is one of the main reasons the Administration keeps significant amounts of resources saved in a number of different funds which are managed with very little transparency and are to be used at the sole discretion of the President. Definitely, Chavez cannot afford a drop in oil prices in times of choice unless you have enough money saved, and the election of the constitutional amendment in 2009 is a good example. With oil prices having dropped by almost 70%, the Chávez Administration was able to increase public spending to levels which allowed them to win the referendum which established that a sitting President may indefinitely run for re-election. In our opinion this is the expected scenario for the Executive for the Presidential elections of 2012.

What will be the impact of this increased spending?

The development of the GDP continues to show signs of key economic activities, which are the main generators of jobs, such as: manufacturing,



construction, commerce, transportation and storage, are still sliding. And, one has to point out that, the Venezuelan economy has not substantially improved, despite the fact that oil prices have rebounded and are higher than last year.

Despite all this, the Administration still doesn't show any signs of implementing any kind of re-activation plan for the economy which would include the participation of the economy and the business sector, as well as labor unions and workers. The Administration seems to be committed to maintaining a confrontational environment and continuing with its implementation of a new legal and institutional system which will continue to shape the social-production model it has proposed, giving the State supremacy and promoting other forms of organizing property, other than private property.

In the end, an Administration that for a number of different reasons (nationalizations, exchange controls, etc.) is less efficient and less able to make sure that public spending is actually reaching those in most need, is an Administration that is headed for significant drops in popularity. And, as we mentioned in our analysis of economic growth, maintaining public spending at those levels will just not be enough to maintain the President's popularity levels. The Administration will have to do more than just increase spending. The question is: will it be willing to?





Economic Tips

BCV publishes Regulations governing foreign currency market operations. Last week, the Central Bank of Venezuela (BCV) published its Regulations governing foreign currency market operations on its web-page, specifically those made using the SITME system. Article 10, paragraph 1 specifies that: “the Central Bank of Venezuela, in exercise of the policies in its power and in fulfillment of its functions, may participate, as well as authorize, purchase and sale operations in bolivars of bonds mentioned in this article, in accordance to the mechanisms it deems convenient...”

Nothing new. Publishing the regulation is just the formalization of what the banks have already been doing since the SITME system began. Furthermore, there are banks that are having problems with liquidity that are using bonds denominated in US-dollars as a guarantee for getting funds from the BCV. In answer to this situation, the BCV determined that it would limit the amount lent and what they need to do is to sell the bonds to other banks and this is why the resolution was issued.

INPC registers an increase of 1.1%. The National Consumer Price Index (INPC) reported a 1.1% increase during the month of September compared to the previous month. Accumulated inflation for the first 3 quarters of the year is at 21.2%, almost three points higher than what was registered last year at the same time (18.5%). The y/y variation is at 27.9%, almost 2 percentage points lower than what was registered last month (29.7%).

CPI for Caracas Metropolitan Area up by 1.3% in September. The BCV registered a 1.3% increase in the CPI for Caracas Metropolitan Area, the lowest m/m increase in 37 months. Accumulated inflation during the first 9 months of 2010 is at 21.8% with the y/y variation at 28.4%.

Core inflation also dropped on a month to month basis. Month to month core inflation went from 1.9% in August to 1.5% in September. Accumulated core inflation during the first 9 months of 2010 is at 20.5% with the y/y variation at 27.9%.

Shortages up and diversity down. Shortage and diversity indicators for the Caracas Metropolitan Area, though improving, got worse during the month of September. The shortage indicator was at 10.3%, up by 0.7 percentage points compared to the previous month (9.6%), but it is still a lot lower than the 13.2% registered in September 2009. The Diversity indicator dropped by 1.1 points, going from 176.1 to 175.0 in September (May 2003=100).



Unemployment reached 9.6% in August. According to official figures released by the National Statistics Institute (INE), the unemployment rate stood at 9.6% during the month of August, 1.6 percentage points above the rate in August 2009 when stood at 8.0%. Moreover informality remained relatively stable at 43.4%, while the remaining formality 56.6% occupied.

Sitme figures. To date, US\$2,695 million have been negotiated through the Integrated System for Foreign Currency Transactions (Sitme), averaging US\$32,1 million a day, with an implicit exchange rate of VEB 5.3/US\$. Last week the traded amount reached US\$199.8 million, US\$30.0 million less than last week when braided US\$229.8 million.

Interest rate. The lending rate for the fourth week in September was at 17.8%, up by 17 base points compared to the previous week. Time deposits and savings rates were steady at 14.5% and 12.6%, respectively.

International reserves. International reserves increased by 1.8% going from US\$28,096 million during the fourth week in September to US\$28,600 million during the first week in October. Compared to the same period last year, international reserves dropped by 12.2%.

Monetary liquidity. Monetary liquidity for the fourth week in September was up by 0.6% compared to the previous week settling at VEB 260.11 billion, and up by 11.3% year to date in nominal terms and 17.4% in the last 12-months.

Oil Tips

Venezuela: largest natural gas reserves in Latin America. According to Pdvsa, Venezuela's proven natural gas reserves reach 178.8 trillion cubic feet of gas (tcf) and non-proven reserves reach 193 tcf. 85% of the proven natural gas reserves correspond to oil-related gas. This information places Venezuela as the eighth country in the world holding the largest proven natural gas reserves and first in Latin America.

Pdvsa to finance construction of homes. After recognizing the housing deficit and the number of homes in risky conditions are a "State problem," President Hugo Chavez informed he would destine US\$1.5 billion of the next Pdvsa bond issuing (US\$3 billion) for the development of an emergency plan to build homes. In Chavez's



own words, *"We have US\$3 billion to be sold by my pal Rafael (Ramirez, minister of Energy and president of Pdvsa). Out of those US\$3 billion, half will be used to kick that plan off (...) I am hereby announcing the allocation of VEB 6.45 billion (US\$1.5 billion) just for that plan as of right now.*

Considerable raise. According to Pdvsa's 2009 operational report, that year, the oil company destined US\$157 million for the development of housing complexes in Venezuela, through the company's contribution to social development. Mision Vivienda (Mission: Housing) alone received US\$133 million from Pdvsa last year. Moreover, through its affiliated company Pdvsa Desarrollo Urbano, US\$24 million were injected to housing developments located in La Vega and Filas de Mariches, in Caracas and Miranda, among others.

Pdvsa subjugated by the National Administration. From the National Development Fund (Fonden) which feeds from excess oil revenues, we can also say Pdvsa destined funds to home construction projects. The aforementioned fund received US\$600 million in 2009, out of which 54% went to new housing projects nationwide. Considering President Chavez's announcement for 2010 (US\$1.5 billion) and the amount allocated last year between Fonden and Pdvsa (US\$481 million), the increase of the state's contribution to housing developments will reach 212% this year. Once again this proves how Pdvsa is obedient to Chavez's commands. At *Ecoanalitica*, as we have mentioned in several occasions, we believe said actions will continue to damage the investment in production and exploration, necessary to reactivate the economy.

Socialist natural gas distribution network grows. 15 stockpile centers were incorporated to the Socialist Natural Gas Cylinder Distribution Network between August and September, to reach 47 working spaces. These spaces allow customers to acquire domestic gas cylinders promptly and supply the sector's Communal Shelves.

BP to present a plan to sell its assets. British Petroleum, facing enormous compensation expenses for the crude oil spill in the Gulf of Mexico, will present this October a plan to President Chavez to sell its assets in Venezuela to the Russian company TNK-BP. BP will deliver its proposal to Chavez during his tour of Russia and Asia next week. The sale could generate the British oil company up to US\$1 billion. The estimated indemnification to be paid by BP due to the giant oil spill reaches US\$30 billion.

US\$11.2 billion paid so far. Out of these estimated US\$30 billion to be paid by BP, they have already disbursed US\$11.2 billion. This information was revealed last Friday, coinciding with the official take over of BP's new general director, Bob Dudley. This sum includes expenses to contain and clean the spilled crude oil, the drilling of



auxiliary wells, the money paid to the affected North American states and to the federal authorities, as well as particular indemnifications.

Iraq now in third place. Iraq assured this week its proven oil reserves had increased considerably to place the country in the third position worldwide, right behind Saudi Arabia and Venezuela. The Iraqi Oil Minister, Husein Shahrastani, assured his country had “exploitable” reserves for 143.1 billion barrels, 24% more than the estimation released by the Organization of Petroleum Exporting Countries (Opec).

Ecopetrol to increase production this year. The Colombian state-owned oil company Ecopetrol might boost its crude oil and natural gas production by 5% by the end of 2010, said the company’s executive president, Javier Gutierrez. Ecopetrol hopes to elevate production to 620,000 barrels per day (kb/d) by year end, up from the 590 (kb/d) reported in the end of June.

International oil baskets. At the close of the New York market last Thursday, October 7, the WTI was at US\$81.7/bl, showing a 2.1% increase compared to the US\$79.9/bl of the previous Thursday. The Brent increased by 1.6% to reach US\$82.8/bl, compared to US\$81.4/bl of Thursday, September 30.

Local oil basket price. The Venezuelan oil basket price increased last week, to close at US\$69.6/bl on Friday October, 01, up by US\$1.9 from the US\$67.7/bl registered the previous week. Meanwhile, the basket’s annual average kept constant in US\$69.5/bl.

Business Sector Tips

State presence in the banking system increases. The information handled by the Superintendence of Banks indicate that, as of December, 2009, public financial institutions controlled 46 out of every 100 bolivars held by the State in the banking system, a proportion that reached 57 as of the end of August of the present year. A clear example is the case of Banco de Venezuela, of which official business captures have increased by 149% in the last eight months, reaching VEB 10.12 billion, while Banesco, Mercantil and Provincial, the three largest private banks, reached VEB 7.06 billion altogether.

Volatility in the inter-bank market. Since the National Administration began to concentrate the State’s money in public banks, financial institutions that do not have a deposit base to easily allow them to compensate the withdrawal of these funds, need



to turn to the interbank market. Official numbers indicate that both the overnight interest rate and the loans requested on a daily basis have increased considerably. In September, the funds traded increased by 129% compared to the average of the first 8 months of 2010, to reach a daily average of VEB 2.07 billion. The overnight rate has reached an average of 10.2% in September, compared to the 2.2% averaged between January and August, peaking last week at 20%.

Currency authorized to bi-national chambers grow by 44%. According to numbers released last week by Cadivi, between January 1 and September 29 of 2010, a total of US\$2.17 billion were authorized for the companies representing Latin American Bi-National Chambers, to report a 44% increase compared to the same period of 2009 when US\$1.49 billion were authorized. Cadivi held a meeting with representatives of Latin American Bi-National Chambers last week at said institution's headquarters to continue with the permanent meetings being held with the different productive sectors.

Agroisleña expropriated. President Hugo Chavez announced the expropriation of Agroisleña, successor of Enriqye Fraga Alfonso with more than 50 years in Venezuela dedicated to the distribution and sale of agro-chemical products. The company is one of the private organizations of largest presence in the national agricultural sector with 52 agencies. For the north-summer cycle 2010-2011, Agroisleña was projecting to support the sowing of 30,000 hectares of rice, 10,000 of sunflower, 10,000 of vegetables and 3,000 of potatoes, not including the Special Financing Program for Agricultural Production (Pefpa) that funded the sowing of 31,800 hectares of rice, 29,500 of sorghum and 3,000 of soy.

Gold Reserve has been waiting since 2009. In April of 2008, the Government of President Hugo Chavez revoked all rights over the project Brisas and the promissory Choco 5 to the Canadian mining company Gold Reserve. The next year, the firm requested arbitration before the World Bank's International Centre for Settlement of Investment Disputes (Icsid). As of September 24, 2010, Gold Reserve announced it was demanding at least US\$1.93 billion from Venezuela for the expropriation of its participation in said gold mining projects. The nationalization policy has caused Venezuela to face several international law suits, totaling approximately US\$30 billion in accounts payable.

Cédula del buen vivir (Good living card) at 15%. Banco de Venezuela, the country's main financial institution, has started a plan to increase access to banking services with the consulting help of Caixa de Brasil. BCV published a resolution in the *Official Gazette* last week indicating the "good living card," a credit card to be accessible to any worker with a Banco de Venezuela payroll account, will have a minimum interest rate of 15%. It is worth mentioning this interest rate represents a huge advantage. In average, financial institutions charge 28.5% to finance purchases through credit cards.



Initially, the “good living card” will only be accepted in Biceabastos and Abastos Bicentenario.

Mi casa equipada (My fully-equipped house): 1,700 loans approved. Within the framework of the “Mi casa equipada” program, with which the Government is giving away 300,000 home appliances through Abasto Bicentenario, 1,700 loans have already been approved to acquire these products. The Minister of Trade, Richard Canan, said they had received 4,500 applications in the different public banks these last two weeks to acquire over 18,000 products including refrigerators, stoves and semi-automatic washing machines. Canan added they would be receiving said appliances on a weekly basis, and they expect to give away approximately 1,200,000 pieces in 2011.

Will construction be reactivated? One week ago, President Hugo Chavez recognized that home construction was a pending issue for this Government, and on Monday, before the foreign press, he once again said all the authorities needed to dedicate themselves to solve this problem. During the first six months of 2009 (a period in which a contraction was already present), official entities completed 12,500 homes, but during the first half of 2010, public institutions built only 5,000 housing solutions, for a 60% contraction. 2,000 homes were built in the second quarter. President Chavez announced the construction of housing units would be boosted with resources obtained from the Chinese fund. Out of the US\$4 billion obtained from the Chinese loan, US\$1 billion will be used to build no less than 25,000 homes.

State also present in the automotive sector. The State presence in the so called “strategic sectors” keeps expanding to other areas of the economy. The National Administration authorized Corporation ZGT, manufacturer of the Chinese cars Chery, to produce in Venezuela. The approval of this new assembling project was given under the mixed company concept, since the State will control 51% and the private company will own 49% of this joint venture, said the Ministry of Science, Technology and Intermediate Industries. According to data handled by the Ministry, as of June of 2009, the Administration had 20 assembling projects under analysis, distributed as follows: 2 for vehicles, 4 for SUVs and trucks, 5 for tractors, 1 for semi trucks and buses and 8 for motorcycles. According to sources in the automotive sector, the companies’ target was not to establish alliances with the State, but it seemed the Administration would not authorize new investments unless the projects were associated with the Government.

Ice-Cream Company EFE shut down. After eight days of halted production at Helados EFE, one of the companies of the Polar Group, the plant has only two days of inventory left, so they are not able to guarantee product presence in its points of sale nationwide. Manuel Larrazabal, EFE’s business director said the union conflict had



caused loss to the company for VEB 7.5 million, and assures there is “no ice-cream to be sold.” Larrazabal said the strike was affecting 1,700 workers (1,200 administrative employees and 500 plant workers); plus another 1,500 ice-cream street vendors that depend on the company. The plant’s annual production is 30 million liters per year, but so far, EFE has produced only 17 million liters of ice-cream, a 43.3% contraction.

Conviasa to reduce 30% of its flight routes. Two weeks after all national flights were put on hold, the state-owned airline Conviasa resumed operations. In the opinion of the vice minister of Transportation and Communications Infrastructure Management, Arturo Gil, these 15 days were enough to carry out the assessment, rectification and re-launching of the airline, although the restructuring process continues. The reduction of approximately 30% of the airline’s flight routes was decided to optimize the services and maintenance of the current fleet comprising 5 aircrafts. Other aircrafts in service are estimated to arrive soon, to reach eight, but the recovery process will also require a financial appraisal to see how these new aircrafts can be incorporated to the fleet.

Will they increase the fleet? According to the Chinese news agency Xinhua, the National Administration, by way of the minister of Trade, Richard Canan, along with officials from Science and Technology and Transportation and Communications are currently negotiating with China the renewal of Conviasa’s fleet, which has been in service for approximately 20 or 30 years.

Alcasa bankrupted. The accumulated loss of Alcasa as of July, 2010 was VEB 1,396 million, informed the president of that company, Elio Sayago to the company’s workers through the institution’s bulletin La Hoja de Aluminio, asking them to study the coming sacrifices. Alcasa, with an original installed capacity of 205 thousand tons/year, has been in crisis since 2004, though it has been known for two decades that it requires a deep transformation and technological modernization to become productive once again.

Bandes almighty. Banco de Desarrollo Economico y Social de Venezuela (Bandes) finances 127 megaprojects from the Chinese-Venezuelan Joint Fund, such as the construction of railroads, thermal-electric plants, subway systems, agricultural projects, basic industry projects, health and housing projects and universities, so was announced by the president of Bandes, Edmee Betancourt.





World Crisis Tips

Bank of Japan reduces reference interest rate. Last Tuesday, the Bank of Japan's (BoJ) monetary policy committee unanimously decided to reduce the reference interest rate to a range between 0% and 0.1%, a rate that was previously set at 0.1%, and committed to maintaining this quantitative easing until achieving price stabilization. BoJ also committed to purchasing financial assets to expand the monetary liquidity for a total of ¥35 trillion (approximately US\$419 billion), including Japanese Government Bonds, corporate debt and Japanese real estate investment funds.

US GDP growth estimates revised slightly high. The Conference Board released the final US GDP growth rate for the second quarter of 2010, which was established in 1.7% (q/q seasonally adjusted annual rate, SAAR), after having published a 1.6% in preliminary figures and 2.4% before that in the advance. Regarding the second quarter of 2009, the US GDP grew by 3%.

US Service sector recovers in September. During September, the services and construction sectors' composite index recovered by 3.3%, going from 51.2 points in August to 53.2 points, slightly better than consensus expectations (52), but still below its level of July (54.3), which sets these sectors' the growth rate during the third quarter of 2010 below the one reported in the second quarter. Historically (since the beginning of the series in 1997), there has been a 65% correlation between this index and the GDP growth (SAAR) in this sectors.

Manufacture keeps growing but in a moderate pace. During September, the ISM (Institute of Supply Management) manufacturing index remained over 50 points, indicating 14 consecutive months of expansion, but the growth rate continued to moderate itself, going from 56.3 points in August to 54.4 in September.

Case/Schiller home price index fell in July. After the expiration of the tax credit offered by the US Government for first-time home buyers, home prices in the main 20 US cities showed a 0.1% decrease in July, compared to the previous month, though still 3.2% higher than the prices reported in July of 2009. Home prices between regions maintained the same behavior of the last few months, west cities showed an increased raise of prices compared to the last 12 months: San Francisco, 111.2%; San Diego, 9.3%; Los Angeles, 7.5%; while in Tampa, Charlotte and Las Vegas, average prices continue showing negative y/y variations: -3.2%, -3.5% and -4.8% respectively.



Confidence keeps recovering in Europe. The European Union's general confidence index kept moving up over its historical average (100), to reach 103.4 points in September, up from 103.1 in August, to establish itself within percentile 75 of the historical series (since 1994). In order to make unbiased comparisons between sectors and countries, we use the location of indexes in percentiles: retail sales lead the ranking in percentile 92, followed by the industrial sector (71), consumer confidence (43), followed by services and construction, both in percentile 30. Comparing by country, we can observe how Germany widely surpasses the rest of the continent by reaching percentile 92, while France sets itself on percentile 52, the UK in percentile 41, Italy in Percentile 32 and finally Spain in percentile 18.

Moody's might reduce the Irish debt rating. Moody's Investors Service announced this week they are studying the Irish economy for a possible reduction of its sovereign debt rating, currently Aa2, since there is less uncertainty regarding the Irish government's ability to maintain its financial strength.

Good growth outline for Latin America. The Inter American Development Bank (IADB) is projecting a regional GDP growth rate between 5.5% and 6% for 2010, while the International Institute of Finance (IIF) is projecting a 5.7% growth, well aligned with the IADB projection, and 4.3% for 2011.

Political Tips

PSUV lost in 22 states. The pro-Chavez machine didn't work in 22 states and was barely able to maintain the votes registered 19 months ago in Merida and Tachira. The worst numbers (in percent loss of votes) for Chavez followers were registered in Amazonas, where PSUV lost 30 points compared to 2009; in Sucre, the decrease reached 17 points and 15 in Lara. Anzoátegui, one of the surprises in last Sunday's election, reported an 8-point decrease in vote intervention.

Who goes to Latin Parliament? The National Electoral Council gave credentials as representatives before the Latin American Parliament to all 12 candidates who won in the election of Sunday September 26. The representatives proclaimed by the United Socialist Party of Venezuela (PSUV) are Roy Chaderton, Roy Daza, Rodrigo Cabezas, Ana Elisa Osorio, Walter Gavidia and Carolus Wimmer. The winning candidates who will represent the Unity party are Timoteo Zambrano, Henry Ramos Allup, Jose Sanchez, Delsa Solorzano and Francisco Garcia. Dalia Herminia Yanez was also announced as winner for the indigenous representation before Latin Parliament.



CNE completed the last audit to the parliamentary election. The National Electoral Council's director of political participation, Luis Emilio Rondon, informed that on Saturday October 2 the CNE had finished the second stage of the audit process of the September 26 parliamentary election results, as well as the review of the machines used in the election, with the participation of representatives of the different political organizations, domestic observers and external auditors.

MUD to challenge alleged inconsistency of records in Carabobo. The candidate for the Democratic Unity Table in the fifth circuit of the Carabobo State, Julio Castillo, assured he was preparing along with his attorneys a formal challenge letter to be presented to the CNE reporting an alleged inconsistency of data in some records issued in said entity in the September 26 parliamentary election. Castillo said the document would be introduced before the CNE once they had gathered "all the evidence."

PPT: to reform electoral law. Patria para Todos (PPT) proposed an urgent task to the National Assembly to be installed on January 5, 2011: reforming the Organic Law of Electoral Processes. *"If both Government and opposition want to work for democracy and we are all welcome in Venezuela, then they should both agree on this reform urgently,"* said Luis Fuenmayor Toro, head of campaign of PPT. Toro also highlighted the leadership of President Hugo Chavez had been falling for the last four years, so it is time to modify certain laws.

Dietrich: Either Venezuela changes its model or it will collapse just like Cuba. Mexican Sociologist and Politics pundit Heinz Dietrich assures in an article that Chavez has only 8 months to rectify his nation's path. Dietrich says the Head of State has been incapable of *"dismantling the opposition electoral block,"* even though the conditions to do it are given, such as *"the exorbitant oil prices, a practically absolute executive and legislative discretion, the absence of opposition in the National Assembly and an extraordinarily fragmented opposition, without a national project and worthy leaders."* The analyst estimated the circumstances will not improve for the Government within the next eight months since *"the insufficient oil prices, the economic inefficiency and the high inflation"* will not allow it to keep earning as it had been doing since 2003.

Drug dealer financed the Government. Walid Makled, aka *"The Arab,"* a Venezuelan entrepreneur and alleged drug dealer wanted in extradition by the United States said he had given money to the Government before the referendum, without specifying for which electoral process. Makled, also known as *"The Turkish,"* accused of drug trafficking in Venezuela, assured he had enough evidence to prove his relation with the Government. Makled explained in an interview released last Wednesday on the



Colombian channel RCN, that the alleged operation took place *“through the former Governor of Carabobo, Luis Felipe Acosta Carlez, for approximately two million dollars.”*

Improving relations. Colombian chancellor, Maria Angela Holguin announced yesterday that her meeting with her Venezuelan homologue, Nicolas Maduro, would take place at the end of this week in Cucuta. Both chancellors will have a chance to check the labors of all five commissions addressing different aspects of the bi-national relation, and this will be the occasion to tune up the agenda of the future meeting between Colombian President Juan Manuel Santos and Venezuelan President Hugo Chavez, to take place at the end of October. The commissions address the debt payment and the re-boosting of commercial relations, an economic complementation agreement, the development of a social investment plan in the border, the development of a set of infrastructure works and the crime issue.

Luis Reyes Reyes, candidate to the Government of Lara by PSUV. President Chavez already announced his candidate to Governor of the Lara State for the regional election of 2012: Luis Reyes Reyes, parliament candidate elect on September 26. President Chavez did not ignore his candidate's condition as parliament representative, and indicated he would serve as representative for two years to then run for election in the Government of Lara, an office he occupied twice before.

Law of Regulation of Health Institutions under discussion this week. The draft of the Law of Regulation of Public and Private Health Institutions was submitted this week before the National Assembly's Social Development Commission. The draft, that was proposed a year ago by the Health Sub-commission and has nearly 100 articles, aims to regulate the services offered in private and public hospitals and clinics. Among the regulations are professional fees within a range, the standardization of the surgical act in all private health centers, the cost of medicine, real medicine consumption and use of instruments during hospitalizations and the submission of clear and simple bills showing patients' expenses, said Representative Tirso Silva.

Speeding up. The Venezuelan Parliament will start a selection process to appoint 43 magistrates for the Supreme Court of justice. The NA will choose 11 main magistrates and 32 substitutes before the end of the legislative period 2006-2011, so was informed last Thursday by Representative Saul Ortega, president of the NA Candidacy Committee for the selection of magistrates. The Citizen Participation Commission only awaits the NA board of directors' instructions to begin the public consultation of the laws regarding the people's power such as the Organic Law of Communal Groups. This was indicated by the president of this organization, Ulises Daal, who assured the report of said legal instrument was ready to be taken to the social street parliament. Daal reminded the report for the first discussion of the Organic Law for the Impulse



and Development of the Communal Economy was also ready to be discussed in plenary session. Personally, Daal thinks the Organic Law of Communal Groups will be sanctioned this year.

And more. The president of the Defense Commission, Juan Jose Mendoza, announced that 60% of the report to continue with the second discussion of the draft of the Law of Disarming was ready. The parliament representative stated that several proposals had been presented during the public consultation of the normative, some of which had already been included in the legal instrument, but others had to be incorporated. The new Organic Labor Law is also in this year's agenda. The President of the Social Development Commission, Rafael Rios, informed that the special commission working on its study would start reviewing the draft next Tuesday. In turn, the new Penal Code will seemingly need to wait a bit longer. At the Domestic Policy Commission they don't believe they'll be able to sanction it in 2010, for it comprises 900 articles.

But it is the people who legislate. The first vice president of the National Assembly, Dario Vivas, assured that in the next legislative period the National Assembly would work different than it has been working so far: Representatives will not consult laws with the people, the people will, in an assembly of citizens that will submit proposals before the Parliament. *"Parliament is the legislating people, that's the motto that earned us the victory in the September 26 election,"* said the re-elect representative of circuit 5 of Caracas.

Venezuela denies links with ETA. President Chavez issued a statement indicating his Government "rejected" any links with ETA and stating people can not give credit to statements by "two vicious criminals" of the terrorist organization. Chavez said he had asked the Venezuelan chancellor, Nicolas Maduro, to release a statement rejecting the information about the alleged training of two alleged ETA members in Venezuela. Spanish National Audience Judge Ismael Moreno dictated last Monday a ruling stating the ETA member deported to Venezuela in 1989, Arturo Cubillas, gave training courses in 2008 to the alleged ETA members Javier Atristain Gorosabel and Juan Carlos Besance Zugasti, both arrested last Wednesday in Spain.





ECONOMIC OVERVIEW

