EXCHANGE MARKET REPORT

Year 17
August 2021

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Ecoanalítica
acompañando las buenas decisiones

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www.ecoanalitica.com

Av. Blandín, C.C. Mata de Coco, piso 5, oficina 5-E, La Castellana, Caracas, 1060, Venezuela.
(+58 212) 266 9080 / Fax (+58 212) 266 5119 / RIF J-31130403-7

History does not repeat itself, but it does rhyme

During July, the unofficial exchange rate rose 21.2% to VES/USD 3,894,264.1 by the end of the month, which represents the third highest inter-monthly increase since the beginning of 2021. The exchange rate increase was concentrated in the second half of the month, in a period between July 15th and 23rd, in which inter-annual variations went from an average of 0.2% to 2.2%.

Although at first glance such an increase may seem abrupt, it is a relatively expected movement of the exchange rate dynamics in Venezuela since 2019. As we explained in the Foreign Exchange Situation Report of June[1], exchange rate rhythms in Venezuela follow a "staggered" sequence in which periods of relative calm[2] are interrupted by more accelerated rises that will eventually return to a more moderate state; if no extended monetary shocks occur.

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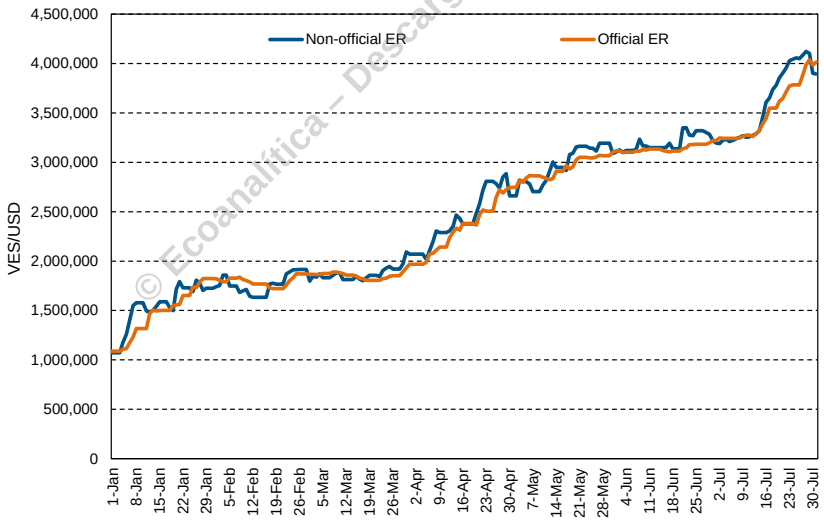
Daily exchange rate (2021)



Sources: BCV and Ecoanalítica.

[1] Foreign Exchange Situation Report No. 6 of 2021: *Following the path of the exchange rate tiles.*
[2] Where inter-daily variations tend to remain below 1.0%.

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A leap that looks like a big jump

This staggered trend can be seen in the progression of the inter-weekly variations[3] of the exchange rate, which show a pattern of one month with average increases above 4.0%, followed by two months with deceleration. The months with the highest average variations were January (11.8%), April (7.2%) and July (4.1%). The remaining months of the year averaged an increase of 1.6%.

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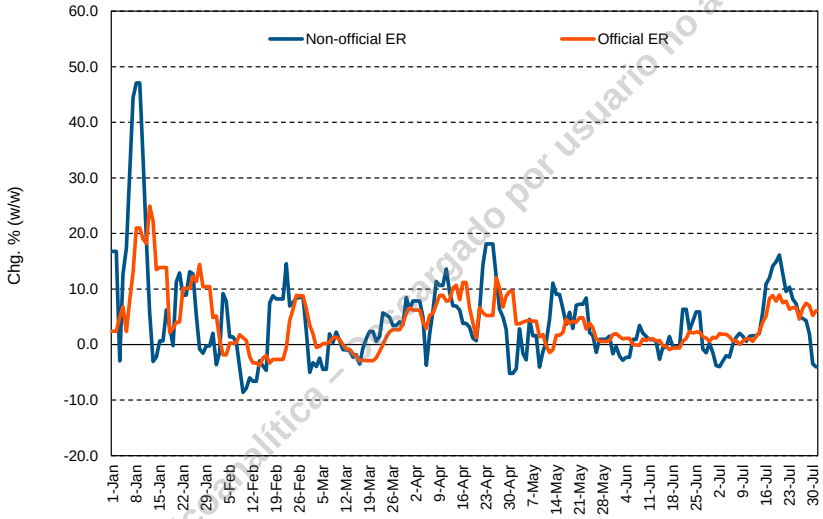
Weekly change of exchange rate (2021)



Sources: BCV and Ecoanalítica.

In this sense, the behavior of the exchange rate during July is consistent with other periods of corrections since the beginning of 2019, where the persistent distortions of the Venezuelan economy configure an inertia naturally inclined to the rise, in which triggers in the exchange market will propitiate sharper oscillations; with the greatest volatility usually coinciding with the common budgetary shocks in the months of December-January[4].

[3] Calculations of inter-weekly averages made from daily data.
[4] Historically, the end of the 4th semester is accompanied by increases in the margin of public spending, relative increases in consumption, and payments to suppliers from the Executive Branch that put pressure on prices and the exchange rate until mid-January.

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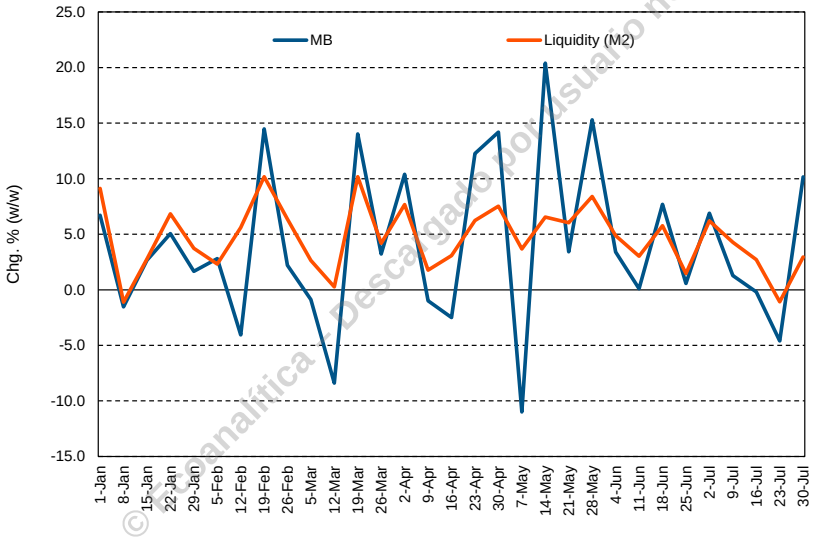
The usual suspects

Effective lace yields

During the first three weeks of July, the inter-weekly movements of the monetary base were below the average for the year (4.0%), with the weeks of July 16th and 23rd being the 8th and 9th occasion, respectively, in which nominal contractions have been recorded since the beginning of 2021. Subsequently, in the last week of the month, the monetary base recorded an increase of 10.2%.

Weekly change of monetary aggregates (2021)



Sources: BCV and Ecoanalítica.

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Increases in the monetary base and liquidity during July were not high, and their most pronounced positive variations followed the days of the highest exchange rate hikes; therefore, the increase in the exchange rate is not directly explained by a monetary shock from the monetization of fiscal activity.

However, when both indicators are taken together, there is a downward trend in the effective reserve requirement[5], which has gone from an average of 71.1% in January to 56.6% in July. This relaxation of the effective reserve requirement would imply a de

[5] Inverse of the monetary multiplier.

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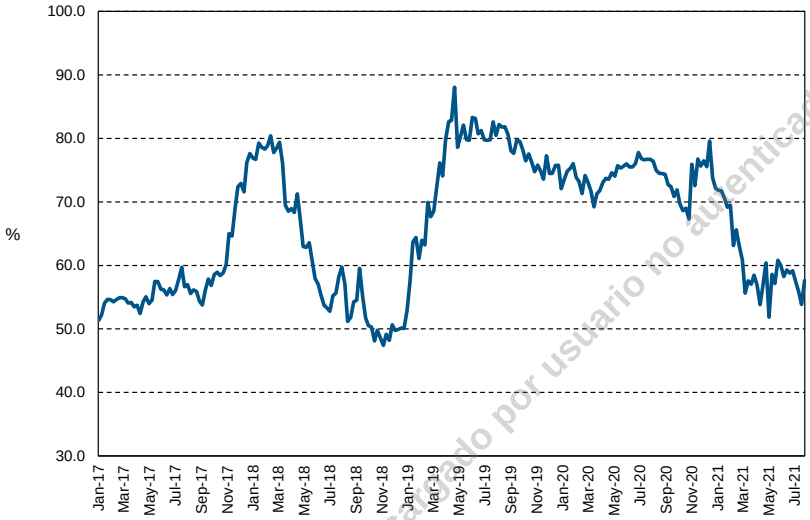
facto release of liquidity that can be directed to demand foreign currency in the exchange market, driving it upwards.

Effective reserve requirements



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Falling cash sales

Since the dismantling of the DICOM auction system in March 2019 and the launching of the foreign exchange desks, the most direct instrument used by the Central Bank of Venezuela (BCV) to intervene in the foreign exchange market and moderate its price increase has been the sale of foreign currency in cash to the financial system. Although the contraction in the size of the Venezuelan economy reduces the amount required to influence the foreign exchange market, the market continues to be sensitive to drops in the flows coming from the monetary authority.

For comparative purposes, during the first half of 2021, foreign currency sales were equivalent to USD 273.4 million[6], an increase of 136.1% over the same period of 2020, and averaging USD 45.5 million per month. July registered a substantial drop in these sales, totaling USD 23.3 million[7] in foreign currency sold to the financial system, the lowest amount since October 2020.

[6] USD 137.7 million and EUR 112.3 million.
[7] USD 6.4 million and EUR 14.3 million.

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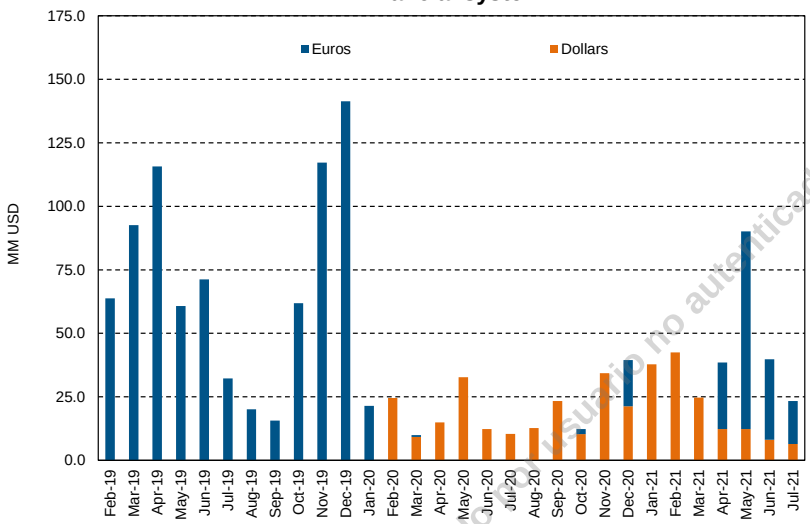
Foreign currency in cash sold by Central Bank to the financial system



*Euros converted to dollars using average monthly exchange rate USD/EUR.
Source: Ecoanalítica.

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Exchange rate appreciation continues

The exchange rate hike during July continued without reversing its general lag with respect to the general price level, which in essence makes the exchange rate cheaper in relative terms and fosters greater demand within the foreign exchange market. The counterpart of this dynamic is a rise in the cost of living in dollars, or the loss of purchasing power of foreign currency within the Venezuelan economy.

For the month of July, the cost of living in dollars rose by 5.8% with respect to the general price index[8], with communications and education services being the only items that fell against the US currency, with decreases of 6.8% and 3.2%, respectively. In cumulative terms, by the end of July, the cost of living in USD rose 25.8% since the beginning of 2021.

Appreciation has slowed down since 2019, however, it will continue to be present in the Venezuelan economy to the extent that the exchange rate cannot be corrected without affecting prices, meriting future corrections. Situation fueled by a monetary policy

[8] 8.9% with respect to the core inflation index.

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disproportionately focused on containing the exchange rate in imperfect indexation environments; practically guaranteeing its lag with respect to inflation.

Variation of living costs in USD (%)

	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Cumulative variation[1]	Interannual variation[2]
Foodstuff and non-alcoholic beverages	-0.4	5.5	7.8	4.4	3.5	9.4	8.6	45.4	90.0
Alcoholic beverages and tobacco	6.0	-0.1	2.0	3.8	-5.5	2.7	10.6	20.4	14.8
Clothing and footwear	-2.5	-4.0	-3.5	-0.5	-8.6	2.1	2.4	-14.1	-33.6
Housing rent	-17.3	2.7	3.7	-2.8	-3.5	4.2	1.8	-12.4	-40.6
Home services except telephone	-3.5	9.2	12.1	5.8	-1.6	13.8	15.4	61.5	143.0
Home equipment	9.5	-0.8	3.2	1.6	-4.4	4.7	2.9	17.2	0.3
Health	-9.7	8.8	11.0	8.8	-1.5	8.8	5.7	34.4	44.8
Transport	-4.9	15.3	18.6	-6.5	-2.7	18.1	7.4	50.1	92.6
Communications	-19.0	18.4	17.4	-9.4	8.5	13.5	-6.8	17.0	41.2
Entertainment and culture	-19.1	-2.8	-0.5	-9.4	-9.6	0.4	0.2	-35.5	-51.5
Education services	-21.3	7.7	8.3	-7.9	-4.4	2.1	-3.2	-20.1	-37.4
Restaurants and hotels	11.3	6.2	10.2	9.3	-1.8	7.5	11.7	67.8	94.9
Other goods and services	-6.4	9.3	9.8	-1.2	-0.1	5.6	2.9	20.7	17.7
Underlying Inflation	**2.2**	**4.9**	**4.8**	**3.4**	**1.6**	**5.1**	**8.9**	**35.1**	**44.6**
NCPI Ecoanalítica (BCV methodology)	**-3.7**	**5.8**	**7.9**	**0.9**	**-1.0**	**8.1**	**5.8**	**25.8**	**35.7**

Source: Ecoanalítica.

[1]Cumulative inflation since the start of the year.

[2]Last twelve months' inflation.

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The usual suspects

At **Ecoanalítica** we consider that the exchange rate increase in July is not unusual or divergent from the general behavior of the exchange rate, especially when it reflects many of the distortions and imbalances of the Venezuelan economy; at the same time it reflects the general expectations of the economic agents regarding the performance of the same.

In this regard, we recommend that, when facing sudden exchange rate hikes, firms and households consider within their hedging strategy the positioning of foreign currencies with respect to the inflation of other items, in order to identify whether it is still relatively cheap compared to other goods and services. In addition, if the rise is identified as being associated with a lagged correction with respect to short-term prices, it is likely to eventually moderate, although not necessarily reverse, once the market is cleared of that initial impact.

Giorgio Cunto

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Parallel exchange rate projections

Fundamentals of upgrades:

Given the technical difficulties in making nominal exchange rate projections in a hyperinflationary environment, as mentioned in previous reports, **Ecoanalítica** is currently making adjustments to our predictive model. The results shown in this edition are the result of this adjustment process. Therefore, they present relatively significant changes with respect to the previous edition.

Projections

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Non-official exchange rate forecasts

Date	Actual value *	Forecast range					
		Low		Medium		High	
2020M01	72,027	12,790	19,447	23,049	45,421	**71,696**	72,027
2020M02	73,251	16,682	25,366	30,063	59,243	75,158	**93,947**
2020M03	89,197	16,212	24,651	29,216	85,451	91,299	**170,097**
2020M04	175,225	21,176	32,198	38,161	92,962	119,253	**237,964**
2020M05	195,647	65,528	107,279	187,981	207,635	268,682	**342,777**
2020M06	205,571	77,180	151,499	196,612	225,913	**241,724**	391,502
2020M07	11,974	84,624	172,993	233,829	294,665	351,803	**429,260**
2020M08	341,279	108,285	223,192	317,513	365,428	449,143	**522,311**
2020M09	432,117	110,036	340,751	374,678	**408,605**	449,288	489,971
2020M10	505,483	115,887	215,215	351,970	**488,724**	525,269	643,814
2020M11	1,034,437	174,338	362,381	528,195	697,768	849,775	**1,001,782**
2020M12	1,072,790	295,285	580,294	**1,128,906**	1,430,167	1,811,823	2,952,848
2021M01	1,724,778	355,685	796,865	1,156,080	**1,515,295**	2,002,887	2,593,191
2021M02	1,916,295	936,107	1,356,411	**1,776,714**	2,429,531	3,009,805	3,744,428
2021M03	2,069,946	1,002,311	1,452,340	1,833,827	**2,215,313**	3,328,354	4,441,396
2021M04	2,661,545	1,672,220	2,423,031	**2,627,365**	2,831,699	3,675,711	4,519,723
2021M05	3,090,404	1,782,075	2,582,211	**3,054,694**	3,527,177	4,172,566	4,817,955
2021M06	3,219,987	1,932,628	2,187,905	**3,323,873**	3,847,403	3,905,938	3,964,473
2021M07	3,902,095	2,121,454	3,073,947	3,574,630	**4,075,314**	4,739,099	5,402,885
2021M08		**2,266,303**	**3,283,831**	**3,789,332**	**4,294,834**	**4,922,003**	**5,035,978**
2021M09		**2,019,483**	**2,524,354**	**4,097,962**	**5,671,571**	**6,400,545**	**7,129,519**
2021M10		**1,962,835**	**2,453,544**	**5,709,147**	**8,964,749**	**10,485,575**	**12,006,400**
2021M11		**2,017,070**	**2,922,697**	**6,171,341**	**9,419,986**	**12,940,961**	**17,824,143**
2021M12		**1,608,360**	**2,330,484**	**6,274,307**	**10,218,129**	**16,529,015**	**22,839,901**

Sources: BCV, Ecoanalítica and own calculations.

*End-of-month; otherwise, if indicated.

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Foreign Exchange Market Indicators

Exchange rates indicators

Exchange Rate Indicators (VES/USD)			
	Jul-21	m/m (%)	y/y (%)
M2/IR*	347,036.9	14.7	1,309
RER**	8,194,482.2	28.3	1,765
Money desks ***	3,983,173.6	24.3	1,442
WER (Consumers)	3,642,218.1	14.8	1,364

Source: BCV, other Central Banks and Ecoanalítica

* End of month. ** Monthly average (Ecoanalítica). ***Last auction.

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Annual exchange rates indicators

Exchange Rates (VES/USD)					
	2018	2019	2020	Depreciation/ Appreciation	Real Depreciation/ Appreciation
Public Sector ER [1]	70.8	10,584.0	371,303.3	-97.15	-79.99
Imports ER [1]	111.5	10,841.1	377,475.2	-97.13	-79.65
Real ER [2]	3,754.0	151,121.0	1,855,226.8	-91.85	0.00
M2/IR [2]	91.1	4,328.0	91,554.3	-95.27	-95.07

Sources: BCV and Ecoanalítica

[1]Annual average. [2]Year ending.

*Information until November. Additionally, the calculations were made with the National Assembly's inflation.

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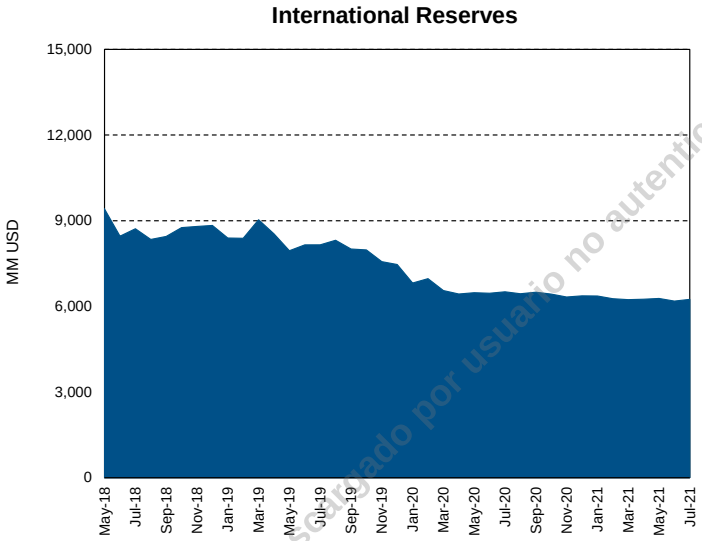
Foreign Currency Availability Indicators

International Reserves



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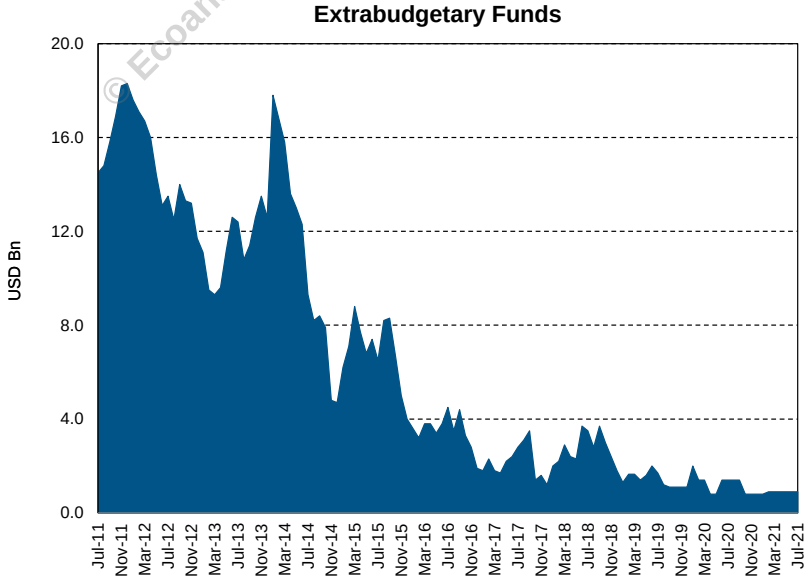
Extrabudgetary Funds



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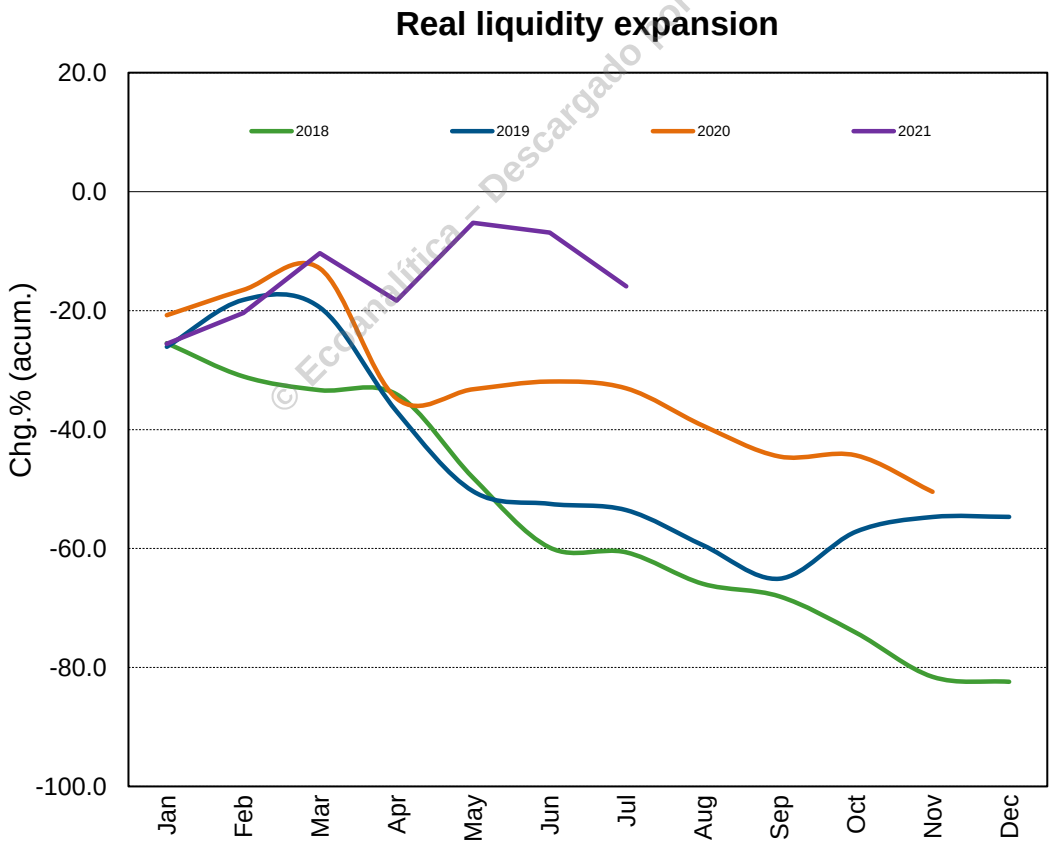
Non-Financial Debt with the Private Sector

Non-Financial Debt with the Private Sector (USD MM)								
	1Q2020	2Q2020	3Q2020	2020	1Q2021	2Q2021	y/y (%)	q/q (%)
CADIVI -Non-settled imports	5.3	5.3	5.1	5.1	5.1	5.0	-20.8%	-5.7%
CADIVI -Dividends approved and unpaid	0.2	0.2	0.2	0.2	0.2	0.2	-63.0%	-0.5%
CADIVI -Rent and Services*	1.1	1.1	1.1	1.0	1.0	1.0	-42.9%	-0.1%
Mixed Companies - PDVSA partners	9.0	9.0	9.0	9.0	9.7	9.8	2.5%	2.7%
Total	**15.6**	**15.6**	**15.4**	**15.3**	**16.0**	**16.0**	**-10.6%**	**0.0%**

Source: Ecoanalítica
* Includes debt with airlines.

Monetary Indicators

Liquidity (M2)



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You should take into account

- ✓ The Central Bank of Venezuela (BCV) announced a new reconversion of the monetary cone to be effective as from October 1st of this year, which name will be "digital bolivar".
- ✓ This reconversion applies a monetary scale that divides all monetary amounts and all amounts expressed in local currency by one million bolivars. In addition, the BCV indicated that the reference exchange rate will continue to be determined in the Exchange Market System through the exchange bureaus of the banking entities.
- ✓ BCV announced that it will put into circulation bills of 5, 10, 20, 20, 50 and 100 digital bolivars, in addition to a coin with a value of 1 digital bolivar. These bills will have the same design on the front and back and only their color will vary.
- ✓ The month of July closed with a parallel exchange rate of VES 3,894,264.1; while the official exchange rate according to the BCV was VES 3,983,173.6. As for the monthly average, the exchange rate was approximately VES 3,602,479.8, while the official exchange rate averaged VES 3,531,764.1.
- ✓ The average official exchange rate in July increased 12.7% over the previous month, and has risen 231.8% since the beginning of the year.
- ✓ According to secondary sources from the Organization of the Petroleum Exporting Countries (OPEC), crude oil production of state-owned *Petróleos de Venezuela S.A.* (PDVSA) fell slightly last month to 512 mb/d, compared to 537 kb/d in June. However, according to Venezuelan government data, in July, the national oil industry produced 614 kb/d.
- ✓ The Venezuelan Finance Observatory (OVF, in Spanish) published the Economic Activity Index for the second quarter of 2021, which reflects a 3% drop in year-over-year terms and an increase of 8.36% in quarterly terms.
- ✓ According to Manuel León, OVF spokesman, the quarterly increase is mainly due to a rebound in oil production. In detail, the oil sector grew 8.5% in the second quarter of the year compared to its first quarter, however, on a year-over-year basis the index decreased 2.4%.
- ✓ León indicated that, if oil production rounds 540,000 barrels of oil per day, GDP would grow close to 4% by the end of the year.
- ✓ The OVF published its inflation figures for July which show a month-over-month price increase of 19%, a cumulative annual increase of 415.7% and a year-over-year increase of 1,984%.
- ✓ The month-over-month increase by items stood out in education (36.1%), home equipment (31.6%) and leisure (27.6%). In addition, the OVF indicated that in July, 162 minimum wages were needed to be able to acquire the Family Food Basket.
- ✓ Delcy Rodríguez informed that, as of November 30th, "*Exonerations are eliminated in 597 codes related to finished products that may be affecting national production (...) it is*

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a tax policy aimed at promoting national development and national production, tariff exonerations are being eliminated".

- ✓ The Vice President indicated that this policy was discussed with the different economic sectors of the country and that this policy does not affect the national industry, but that where national production is not enough and imports must be made, this process is facilitated. According to Rodríguez, the measure seeks to create jobs and save foreign currency.
- ✓ At the annual meeting of *Fedecámaras*, Delcy Rodríguez announced the establishment of a working group together with the private sector to promote domestic production and substitute imported products, in order to achieve foreign currency savings and bet on the transformation of the economic model.
- ✓ Nicolás Maduro announced the installation of a Presidential Council of Economy with two objectives; one of these is to create a "*productive export map of the Venezuelan economy, the substitution of imports... On the one hand, we substitute, we satisfy needs, we continue creating jobs, we continue creating wealth and, on the other hand, we are clearly establishing all the exporting capacity*".
- ✓ The Vice Minister for Asia, Middle East and Oceania, Capaya Rodríguez, and the Vice Minister of Foreign Trade of the Ministry of Economy, Finance and Foreign Trade, Héctor Silva, held a meeting to create an inter-ministerial strategy to boost trade relations with the countries of the Association of Southeast Asian Nations (Asean), made up of Malaysia, Indonesia, Brunei, Vietnam, Cambodia, Laos, Myanmar, Singapore, Thailand and the Philippines.
- ✓ The UK Foreign Office issued a statement to the UK Supreme Court stating that its government recognizes Juan Guaidó as the only legitimate president of Venezuela, an intervention that adds up to determine the ownership of the nearly USD 1 billion in monetary gold stored in the vaults of the Bank of England, a dispute that has not yet concluded.
- ✓ The World Bank ranked the Venezuelan economy as the third worst economy in the world to invest in, according to its *Doing Business* index. In this index, the Venezuelan economy ranks 188th out of 190 economies analyzed, only above Eritrea and Somalia.

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Av. Blandín, C.C. Mata de Coco, piso 5, oficina 5-E, La Castellana, Caracas, 1060, Venezuela.
(+58 212) 266 9080 / Fax (+58 212) 266 5119 / RIF J-31130403-7

ECOANALÍTICA'S TEAM

Alejandro Grisanti / Director
agrisanti@ecoanalitica.net / @agrisanti
Asdrúbal Oliveros / Director
asdrubalo@ecoanalitica.net / @aroliveros
Pedro Palma / Director
pedrop@ecoanalitica.net / @palmapedroa
Cristina Rodríguez / Director
cristinar@ecoanalitica.net
Luis Arturo Bárcenas / Senior Economist
luisb@ecoanalitica.net / @barcenasluis
Giorgio Cunto Morales / Economist
giorgioc@ecoanalitica.net / @giorgiocunto
Corina Fung / Economist
corinaf@ecoanalitica.net / @corinafung7
Jhoan F. Castellano/ Economist
jhoanc@ecoanalitica.net / @castellanojhoan
Diego Santana Fombona / Economist
diegos@ecoanalitica.net / @diegosantanaf

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RESEARCH ASSISTANT
Diego Almau
Michelle Garbán
Mariana Fernández
María Paula Matheus

CONTACT US
Venezuela:(+58-212) 266 9080/ Fax: (+58-212) 266 5119
United States: (+1 212)-994 1850
ventas@ecoanalitica.net
www.ecoanalitica.com
@ecoanalitica