



Venezuela without Chávez: certainties and uncertainties about its future

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Hugo Chávez, undoubtedly one of the most influential Latin American leaders of recent times, died yesterday, February 5, 2013, after nearly 15 years in power in which he developed an iron-fisted control of the economy of Venezuela.

Four operations against the cancer he suffered from 2011 turned

him from power, which he left in the hands of his Vice President. Everything suggests that the near future will present few surprises, as the 'Chavista' Government, who foresaw his death months ago, could prepare a transition that will culminate in early elections as stipulated in the Constitution.

Mr. Chavez became a hero to Venezuela's poor by providing subsidized food, education and free health, paid for with revenue from oil sales. Human development indicators such as poverty, inequality and

child mortality decreased under his mandate.

Analysts (mainly Americans and Latin Americans) agree that the scheme of power in Venezuela will not change radically in the short term, when all indications are that the Vice President Nicolas Maduro will win elections that must be held in a month. However, without the charismatic figure of the leader, it is not clear that 'chavism' is capable of maintaining the Bolivarian revolution in the medium term, at least without reforms.



◀ A divided opposition is about to confirm that its candidate will be Henrique Capriles, the young 40 year-old advocate, Christian and auto defined as a “man of God”, that faced Mr. Chavez in the last presidential elections. He managed significant support, but was not able to beat the ‘giant’.

Capriles offered investors a friendly panorama to foreign investment and to free market, with promises to promote foreign investment and to decentralize the management of a highly politicized country.

Venezuelan bonds

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Venezuelan bonds suffered a fall the day following the death of President Hugo Chávez, whose death was reported after the close of Wall Street. After a historical day in the stock markets, which recorded higher levels than those previous to the financial crisis, investors sold

Venezuelan debt due to uncertainty about if the successor of President will know how to lead the country’s problematic economy.

The bonds, which offered higher yields than that offered mostly anywhere else, rallied in recent months due to the expectation of a transition in the Latin American Republic. But, but for the moment, they are experiencing the typical behaviour of an uncertain transition: there is concern about the future of the country.

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In fact, according to Moody’s, the country’s credit rating would be more affected by the political transition than the death of Chavez, because the uncertainty depends more on the next leader, his policies and his hold on authority. Moody’s revised the credit outlook on the country’s speculative B2 rating to negative in January.

Venezuelan sovereign bonds and those of state-run oil company Petróleos de Venezuela SA (PDVSA) rallied on news that Chavez’s condition had worsened, says Reuters agency. The rally faded, however, after Maduro alleged that “imperialist” conspirators had infected the president with cancer, among a plethora of conspiracies with domestic opponents.

This aggressive tone disappointed those who expected a more moderate leader, and now it seems that the market could have been rallied all these months on this idea of a transition towards a milder ‘chavism’. Now analysts are cautious.

Devaluation

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understand one without the other.

Capriles, opposition leader that faced Chavez in October 2012, promised he would stop nationalizations, create flexible business procedures to facilitate private entrepreneurship and keep popular social programs created by Chavez.

Opposition promises to stop nationalizations, create flexible business procedures to facilitate private entrepreneurship

From Mr. Chavez's successor investors expect that he continues the trend of social and state property, centralization, massive nationalizations, economic controls

and bureaucracy to start and operate ventures.

In Venezuela's, third oil producer in the OIPEP countries, oil revenues account for roughly 94 per cent of export earnings, more than 50 per cent of federal budget revenues, and around 30 per cent of gross domestic product. Apart from petroleum, the country's natural resources include natural gas, iron ore, gold, bauxite, diamonds and other minerals.

International support

Not only his millions of Venezuelan fans have long lamented the death of Hugo Chávez: most of the regional governments have expressed condolences at a time in which the axes of power in the region is teetering. Even the right-wing Sebastián Piñera, President of Chile, praised the "commitment of Chavez to Latin American integration".

An active regional actor, Venezuela favoured the economies of countries such as Cuba, who paid services as their doctors with cheap oil) and Nicaragua, a country that grew by more than 4% thanks to the support of Chavez to President Daniel Ortega. It is now expected that Mercosur allies, such as Argentina, Uruguay and Brazil, as well ALBA members Ecuador and Bolivia, continue to support the revolution that will try to perpetuate Maduro.

Also Colombia seems willing to continue deepening relations with Venezuela, judging by the statement of President Juan Manuel Santos yesterday, who thanked Chavez for his "mediation" in the peace process with the guerrillas of the FARC and reiterated his commitment to leave behind diplomatic incidents as the rupture of relations in 2010.

For now, it is expected that Maduro keeps both the "petrodiploamacy" with its southern neighbours and with China, as well as to renew ties

◀ exchange rate of 4.3 bolivars per dollar.

The decision does not seem to respond to a "currency war", with countries such as Japan trying to devalue their currencies in order to increase export competitiveness.

It may respond to a shortage of U.S. dollars, which is making it hard for the country to pay for imports. The devaluation, given its strong balance of payments, oil revenues will help narrow its deep budget deficit.

According to Bloomberg, South America's biggest oil producer is facing shortages of goods as the lack of dollars crimps imports. In the black market, the bolivar has weakened 53 percent to 18.39 per U.S. dollar in the past year.

Some analysts say that the Venezuelan bonds became a 'refuge' against the crisis, especially because of the expectations of a devaluation of the local currency, which would increase revenues by exporting of petroleum.

Transition and investment

Chavez's supporters, known as Chavistas, will likely give their votes to Maduro in elections expected within 30 days, though surprise could happen.

The international community wonders who will take the reins of the country and if a new political project will be able to steer the country's ailing economy and to promote foreign investment. Venezuelan economy has been so influenced by politics in the last decade that it is impossible to



◀ with countries such as USA or Spain, which already has been quick to highlight its 'firm' relations with Venezuela.

Venezuela's economic challenges

In recent years the country's economy has experienced strong growth (4.2% in 2012), encouraged by the rise in prices of oil and a relative political stability that now looks again at risk.

Foreign Direct Investment has suffered in recent years, partially because of the exchange control policy established after the escape of foreign exchange that took place at the beginning of the 2000s.

The biggest macroeconomic problems his Government will have to face are the excessive dependence on oil and the Venezuelan national petroleum company inefficiency, PDVSA. Fluctuations in oil revenue have led to a predictable cycle

of deficit spending, currency devaluation, inflation, recession, and unemployment.

The nation suffers from crumbling infrastructure and an underperforming industry. Oil accounts for at least 90% of export earnings, compared with about 80% 10 years ago.

Therefore, the Venezuela economy continues to be based on the State oil company, in the hands of Chavez, with their huge profits has invested heavily in the housing sector and in social programs, but that presents obscurantism regarding its accounting.

The opposition also accuses the President of abandoning the maintenance of PDVSA, especially after an explosion in August at the country's largest refinery, in which 42 people were killed.

According to his critics, inefficient public companies dominate the country, in what looks like a growing

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trend, with the Government heavily involved in all sectors of the economy, to the detriment of the private capital.

Stable regime, instable environment

Another triumph of Chávez's PSUV would imply a certain 'Instable stability'. At the end of its mandate, the "Bolivarian revolution" will have had two decades to develop its project, but this not necessarily brings stability. The President

◀ tends to understand the policy of a capricious way, having even to proclaimed and approved legislation on a live broadcast, during his daily TV program, *Aló Presidente*, and that could also be expected from its Party, whoever runs it in the future.

The risk of an eventual nationalization does not guarantee the stability and security of the investment either.

“Venezuela is an exceptional case because of the policy of nationalizations and expropriations carried out Chavez during his term. A victory of Mr. Capriles, in this sense, would be more interesting for private enterprises, for the incentives that could be found to invest in the country,” said Flavia Freidenber, Director of the Spanish Institute of Latin America, to the Spanish journal *20 Minutos*.

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Finally, violence in Venezuela also does not favour a stable climate, with the risk of an eventual coup like the one of April 11, 2002 and the danger of urban violence, a growing problem that the ruling party admitted having failed to deal with. Caracas is one of the most violent capitals of America and the world, and the scourge of this violence particularly affects the poorest, hindering the growth of an emerging middle class.

Doing business in Venezuela

If Mr. Chávez’s successor desires to attract foreign investment in diversified areas, he should implement deep reforms that minimize the overwhelming bureaucracy and reinforce law and legal protection.

According to the World Bank’s



annual report *Doing Business*, Venezuela is positioned below most Latin American countries, and also well below regional media at the “business ease ranking”. The Bolivarian republic occupies the 177 position, below Brazil (126), a country where foreign investors have already serious difficulties, and below their allies Bolivia (153) and Ecuador (130), that are lower income countries. The regional average, of Latin America and Caribbean, is 95.

The worst indicators are registered in aspects such as trading across borders (166), paying taxes (183), protecting investors (179, on a ranking of 183 economies), and getting credit (189), but other issues are not easy either, such as getting

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electricity (155) and starting a business (147).

All these indicators are low, due to bottlenecks such as large numbers of procedures, long delays or high costs, (common problems in Latin American region) and weak legal rights and transparency in the business environment.

The performance of Venezuela is especially negative when it comes to trading across borders, given that the average process takes 49 days to export and 71 to import and costs around USD2.600 and USD 2.900 for a container. And starting a business requires 5 months and 17 procedures.

Opportunities for the investors

However, there are sectors of the Venezuelan market that beyond all this and are generating great benefits for those who decided to invest in the country, such as the tourism. Those who have invested in tourism in Venezuela argue that even with the problems of the country, tourism is maintained with good turnout, generating many jobs and opportunities for Venezuelans. The country also presents an opportunity to invest in real estate, infrastructure, construction and its related industries, such as construction materials and electricity.

Other opportunities arise from ▶

◀ importing products, since Venezuela it is highly dependent on imports and once in the country, the products have a high price. And there is an interesting market in the production of food products, in an attempt of compensating food imports.

The Government also announced, in 2010, several agreements of cooperation with Italy and Portugal for areas such as education, health, infrastructure, energy, housing, goods and services, food, telecommunications, science and technology.

Major projects of construction of social housing and infrastructure,

and projects such as the national railway plan and in the field of ports promoted by the National Institute of water spaces are especially relevant.

Also those related to the massive interurban passenger transportation and some roads; projects, materials and equipment for the generation and transmission of electricity; desalination plants, machinery for public works and mining; projects related to vocational and educational training and in general everything related to the publishing industry; the food industry; machinery, agricultural implements and irrigation systems; motor vehicles

and automotive components.

Direct purchases from the Government (public companies) should also be taken into account, such as the acquisition of machinery, agricultural inputs and implements.

In addition, small investors may also participate in public Stock market from 2011, which is open to private companies.

Despite the complicated economic situation in the country, the profitability is often found where there is an increased risk, but the entrepreneur must pay attention to the Government operations and adapt to the new procedures. ■