

VENEZUELA

1. General trends

The Venezuelan economy expanded by 2.7% in 2001, compared to 4% the year before. GDP growth was driven by the private sector, while the public sector suffered from falling prices and production cuts in the oil sector. Inflation fell for the sixth straight year and came in around 12% in 2001, having run as high as 100% in 1996. Exports fell sharply in the wake of the economic slowdown, particularly in the United States, and because of the decision to cut oil production under an agreement reached with the Organization of Oil Exporting Countries (OPEC). Imports were favoured by exchange-rate policy and surged by over 10%. The resulting erosion of the trade balance caused a reduction in international reserves at the Central Bank of Venezuela (BCV).

EXTERNAL-SECTOR and inflation trends were strongly influenced by exchange-rate policy, which throughout 2001 and until early February 2002 was founded on a currency band system centred on a nominal parity set by BCV. In mid-February, however, the currency was put into a free float. Preliminary BCV figures reveal a balance-of-payments deficit of 2.5% of GDP, contrasting starkly with the surpluses recorded in 1999 and 2000. Overall reserves remained broadly stable around US\$ 20 billion, with the reduction in BCV reserves offset by an rise in the Macroeconomic Stabilization Investment Fund (FIEM).

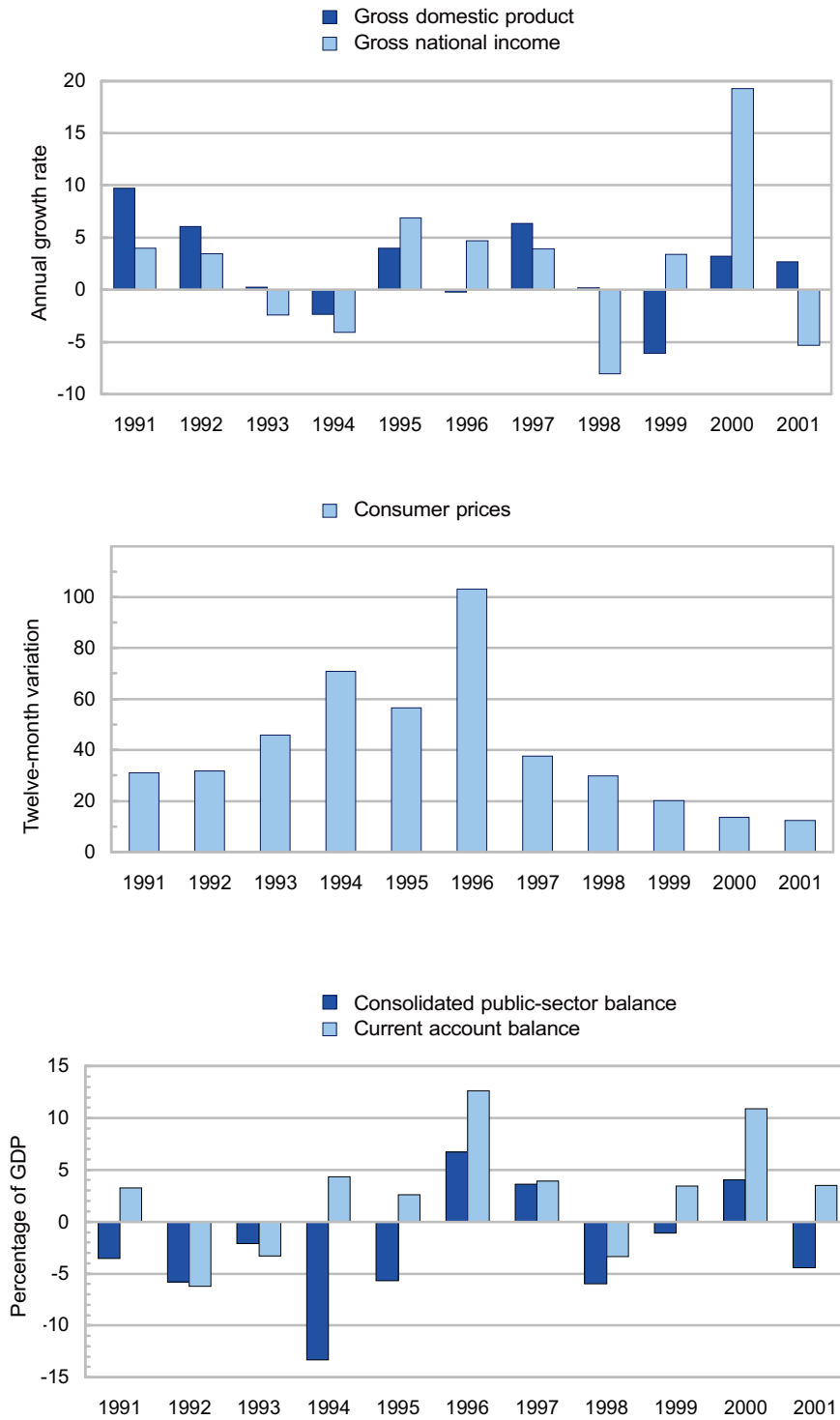
With economic growth stalling, the rate of unemployment fell slightly, and the fiscal deficit widened to over 4% of GDP.

The outlook for 2002 is not very promising. Economic activity slumped in the first quarter, causing growth projections for the year to be downgraded further in view of the tricky political situation. A general strike in early April provoked a military uprising to remove

President Chávez, but he was restored to the presidency shortly afterwards in the wake of massive popular protest.

In the first quarter of 2002, reserves dropped to US\$ 15 billion from their late 2001 level of US\$ 19 billion. The announcement of a new foreign-exchange regime in February initially produced a sharp devaluation of 40% and by March the exchange rate was standing at over 1,000 bolívares to the dollar. Following a short-lived appreciation in April, it then climbed further to reach just under 1,200 bolívares per dollar by late June. This devaluation fed through into steep monthly increases in consumer prices: 1.8%, 4.2%, 2.1% and 1.1% in February, March, April and May, respectively. Cumulative inflation amounted to 9% in the first four months of 2002, with the estimated annual rate running at over 18%. A level of 20% or worse would place Venezuela among the region's highest inflation countries. The Middle East conflict and economic recovery in the United States drove up oil prices to over US\$ 27 per barrel, after they had been below US\$ 20 for most of 2001.

Figure 1
VENEZUELA: MAIN ECONOMIC INDICATORS



Source: ECLAC, on the basis of official figures.

2. Macroeconomic policy

The overriding objective of Venezuela's macroeconomic policy was to keep inflation on the downward track it has maintained since 1996. The main policy instrument involved anchoring the nominal exchange rate in a currency-band system maintained through BCV intervention in the foreign-exchange market. Monetary policy helped minimize the erosion of reserves, as interest rates climbed steeply. The proactive fiscal policy adopted to promote economic growth widened the fiscal deficit considerably in a context of shrinking revenues. In early 2002 the government made major changes to the main lines of economic policy, announcing a fiscal adjustment plan and replacing the currency band with a free floating system.

(a) Fiscal policy

Fiscal policy had to contend with a more hostile domestic and external environment than the year before, and by late 2001 the corresponding deficit had widened to 4.8% of GDP –well above its 3% target. Central government current income accounted for 20.4% of GDP, compared to 19.6% in 2000, thanks mainly to an increase in domestic receipts, while oil revenues dipped by 0.2 percentage points to 9.8% of GDP. A sharp increase in spending (4% of GDP) was chiefly to blame for the widening fiscal deficit in 2001, with both capital and current expenditures rising (by 1.3% and 2.7%, respectively). In the current expenditure category, purchases of goods and services were up by more than two percentage points of GDP, and on capital account both direct investment and capital transfers increased. Central government borrowing requirements were financed mainly from domestic sources, with minor support from external funding channelled through voluntary credit markets and loans from multilateral agencies. The authorities also drew US\$ 900 million in complementary financing from the Macroeconomic Stabilization Investment Fund (FIEM), as provided for under the Budget Act.

The government issued public debt on the domestic market equivalent to 5% of GDP, and made amortization payments amounting to 2%. Given the financial conditions prevailing on the domestic market, the average cost of public borrowing was higher than the year before. In the case of external financing, the government issued long-term bonds equivalent to 1%

of GDP on the European and Japanese markets, and continued to receive loans from multilateral and bilateral agencies.

(b) Monetary policy

The main objective of monetary and foreign-exchange policy was to maintain the downward trend of inflation. The exchange rate was held stable as a nominal anchor against inflation, while domestic monetary policy had the task of creating conditions to maintain international reserves at a level consistent with exchange-rate stability. The authorities therefore persisted with a crawling-peg system involving a currency band centred on a nominal parity depreciating at an average rate of 7% per year.

Monetary policy took a more active stance in 2001 aimed at instilling more orderly behaviour in the money market; and from May onwards BCV played a more influential role through open-market operations. In August, BCV raised the minimum reserve requirement on public-sector deposits from 17% to 30% in order to ease pressure on the local currency. In September, it resumed money-desk operations and began to issue certificates of deposit, thus offering investment alternatives in the form of local-currency denominated financial assets. In addition, the rediscount rate was raised to 37%, in order to increase the cost of holding short-term liquid assets and thus discourage investors from buying foreign currency. These measures, in conjunction with mounting uncertainty on international financial markets in the wake of the events of 11 September in the United States, caused demand for hard currency to fall sharply in the second half of September, which had the effect of stabilizing trends in the foreign-exchange market.

In terms of the main aggregates, monetary liquidity (M2) grew by 4.5% in nominal terms with respect to December 2000, while the monetary base expanded at a nominal rate of 12% over the same period. Expansion occurred mainly in the fourth quarter, following a period of stability in the earlier part of the year. A breakdown of the components of monetary liquidity reveals that currency in circulation outside the banking system expanded; savings deposits shrank by 2.3% with respect to December 2000; and time deposits declined sharply as savers revealed a preference for sight deposits and cash.

Table 1
VENEZUELA: MAIN ECONOMIC INDICATORS

	1993	1994	1995	1996	1997	1998	1999	2000	2001 ^a
Annual growth rates^b									
Growth and investment									
Gross domestic product	0.3	- 2.3	4.0	- 0.2	6.4	0.2	- 6.1	3.2	2.7
Per capita gross domestic product	- 2.0	- 4.5	1.7	- 2.3	4.2	- 1.8	- 7.9	1.3	0.7
Gross domestic product, by sector									
Goods	2.1	-1.4	4.9	2.3	8.0	-0.7	-8.5	2.8	1.9
Agriculture	3.0	-1.1	-0.5	2.0	2.4	0.6	-2.1	2.4	2.6
Mining	9.1	5.7	6.1	8.2	9.8	1.9	-9.5	4.7	1.1
Manufacturing	-1.0	-2.4	8.0	-3.0	5.1	-3.9	-6.4	2.1	-0.2
Construction	-5.5	-17.4	-5.0	1.1	17.2	-0.3	-16.5	-2.7	13.0
Basic services	1.4	-2.2	3.1	1.6	7.9	4.7	1.5	6.7	6.9
Electricity, gas and water	3.2	1.4	2.6	1.2	4.7	1.3	1.1	2.2	3.0
Transport, storage and communications	0.9	-3.4	3.3	1.7	9.0	5.9	1.6	8.1	8.1
Other services	-1.7	-2.7	0.9	-3.9	2.0	-0.1	-3.8	2.7	2.3
Commerce, restaurants and hotels	-4.0	-8.0	1.3	-7.2	4.1	-3.0	-9.6	4.0	3.4
Financial establishments, insurance, real estate and business services	0.7	-2.1	0.4	-3.3	3.0	1.0	-3.3	2.2	2.5
Consumption	- 0.7	- 4.7	1.2	- 4.9	5.0	0.1	- 3.2	3.9	4.9
General government	- 5.2	- 5.9	2.6	- 7.6	4.2	1.4	3.0	5.0	5.9
Private	0.1	- 4.5	0.9	- 4.4	5.1	- 0.1	- 4.3	3.7	4.7
Gross domestic investment	- 18.7	- 29.3	36.5	- 11.0	34.0	1.4	- 15.1	9.3	3.8
Exports of goods and services	12.0	8.1	6.3	7.8	9.4	4.2	- 10.8	5.5	2.2
Imports of goods and services	- 6.5	- 18.5	23.9	- 11.2	33.9	9.4	- 14.6	15.4	9.4
Percentages of GDP^c									
Gross national income	96.9	96.6	97.4	102.4	99.1	90.5	99.3	114.2	105.2
Gross domestic investment	21.3	22.4	20.9	21.5	23.3	24.0	22.2	22.6	21.7
National saving	15.9	17.9	21.0	28.8	25.1	15.8	23.8	37.9	25.6
External saving	3.1	- 4.1	- 2.8	- 12.9	- 4.8	4.5	- 5.5	- 18.6	- 6.2
Percentages									
Employment and wages									
Labour force participation rate ^d	58.2	59.1	61.6	62.2	63.8	65.1	66.3	64.7	66.1
Open unemployment rate ^e	6.6	8.7	10.3	11.8	11.4	11.3	14.9	14.0	13.4
Real average wage (index: 1995=100) ^f	124.4	104.8	100.0	76.7	96.3	101.5	96.8	90.5	96.7
Growth rates									
Prices (December-December)									
Consumer prices	45.9	70.8	56.6	103.2	37.6	29.9	20.1	13.4	12.3
Wholesale prices	47.4	89.5	43.6	105.8	17.3	23.3	13.6	15.8	10.2
External sector									
Terms of trade index: 1995=100) ^c	100.9	100.0	100.0	115.6	110.8	79.9	107.0	157.4	131.8
Nominal exchange rate (bolívars per dollar)	91	149	177	417	489	548	606	680	724.0
Real effective exchange rate for imports (index: 1995=100)	121.5	126.4	100.0	119.4	93.0	76.6	68.5	66.9	63.6
Millions of dollars									
Balance of payments									
Current account	-1,993	2,541	2,014	8,914	3,467	-3,253	3,557	13,112	4,365
Trade balance (goods and services)	90	4,529	3,848	10,501	6,019	-1,214	5,137	14,526	6,521
Exports	16,119	17,681	20,753	25,280	25,192	19,037	22,122	34,394	28,296
Imports	16,029	13,152	16,905	14,779	19,173	20,251	16,985	19,868	21,775
Capital and financial accounts ^g	2,117	-3,485	-3,458	-2,387	63	338	-2,508	-7,294	-6,435
Overall balance	...	...	...	6,527	3,530	-2,915	1,049	5,818	-2,070
Variation in reserve assets (- indicates an increase)	...	...	...	-6,274	-2,624	3,380	- 593	-5,314	2,259

Table 1 (concluded)

	1993	1994	1995	1996	1997	1998	1999	2000	2001 ^a
External debt	Percentages								
Gross debt (as a percentage of GDP)	68.0	70.2	48.5	48.4	35.3	31.6	32.2	26.6	25.8
Net interest (as a percentage of exports) ^h	9.2	9.4	8.4	5.6	6.5	5.7	4.5	0.9	3.8
Central government	Percentages of GDP								
Current income	16.5	17.1	15.7	19.2	23.0	16.4	16.6	19.6	20.4
Current expenditure	14.7	17.5	15.7	15.1	17.2	16.5	16.0	17.7	19.0
Saving	1.8	-0.3	0.0	4.1	5.8	-0.1	0.6	1.9	1.5
Capital expenditure (net)	2.8	2.4	2.8	2.1	3.0	3.3	2.8	2.8	4.3
Financial balance	-2.9	-7.2	-4.3	0.6	1.9	-4.1	-2.6	-1.7	-4.3
Non-financial public sector balance	-2.1	-13.3	-5.7	6.8	3.6	-6.0	-1.1	4.1	-4.4
Money and credit	Billions of bolívars								
Net international reserves	1,013	1,419	1,964	6,035	8,260	8,209	10,062	11,591	9,890
Domestic credit ⁱ	1,705	3,004	4,905	5,590	7,839	9,431	10,371	11,823	13,928
To public sector	484	1,869	3,277	2,836	1,668	2,373	2,116	1,362	2,959
To private sector	1,221	1,135	1,628	2,754	6,171	7,058	8,255	10,461	10,969
Money (M1)	438	1,007	1,340	2,523	4,633	4,938	6,096	8,016	9,091
Local currency savings and time deposits	1,223	1,588	2,196	2,971	4,323	5,684	6,645	8,269	7,924
M2	1,661	2,596	3,536	5,494	8,956	10,622	12,741	16,285	17,015
Real interest rate (annualized, %)	Annual rates								
Deposit rate	12.1	-11.1	-22.1	-35.3	-24.4	0.2	-2.7	-1.3	1.4
Lending rate	17.1	-1.7	-13.1	-29.1	-19.4	6.8	6.0	6.9	10.5
Equivalent interest rate in foreign currency ^j	53.9	35.6	14.9	18.0	15.6	36.0	20.4	14.8	13.1

Source: ECLAC, on the basis of official figures.

^a Preliminary figures. ^b Based on constant 1984 bolívars. ^c Based on constant 1995 dollars. ^d Percentages of the working-age population. ^e Percentages of the economically active population. ^f Includes food and transport allowances. ^g Includes errors and omissions. ^h Refers to net interest as shown on the balance of payments, divided by exports of goods and services. ⁱ In addition to loans to the public and private sectors, includes the net amount entered under "other accounts". ^j Interest rate on deposits, deflated by the variation in the exchange rate.

Nominal interest rates behaved erratically in 2001. A period of instability in the first semester was followed by a steep hike in the third quarter in response to the central bank's tight monetary policy, with a drop in the last quarter and a new downward trend emerging at year's end. Real interest rates shadowed nominal rates, since inflation was broadly stable. High real rates drove up the cost of corporate and personal borrowing, keeping unemployment high and undermining GDP growth, which faded steadily between the first and the fourth quarters. As in earlier years, the financial system was affected by the high structure of interest rates on loans, compounded by sagging economic activity and currency-market pressures that took their toll on bank

deposits. This resulted in meagre nominal growth in the loan portfolio and a higher bank arrears index. Other effects included relative stability in deposits with respect to the balances recorded in December 2000, and a reduction in volumes traded on the capital market. Lending and deposit rates at the six largest banks trended slightly downwards for most of 2000 and the first quarter of 2001, reaching lows of 11% on deposits and 20% on loans, respectively, in February and April of the latter year. This trend was reversed in the second quarter, however, and both rates climbed steadily from then on. In September 2001 this rising trend suddenly gathered pace, as the lending rate shot up to 35.9% and the deposit rate surged to 19.4%.

Table 2
VENEZUELA: MAIN QUARTERLY INDICATORS

	1999				2000				2001 ^a				2002 ^a
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I
Gross domestic product (change from same quarter of previous year)	-8.5	-7.4	-4.3	-4.1	0.9	2.7	3.5	5.7	4.0	3.1	3.3	5.7	-4.2
Consumer prices (12-month variation, %)	27.6	23.4	21.2	20.1	17.6	16.5	16.0	13.4	12.5	12.5	12.2	12.3	17.6
International reserves (millions of dollars)	13,442	14,357	13,989	15,379	16,125	17,371	19,443	20,471	20,901	19,992	19,059	18,523	15,029
Real effective exchange rate ^b (index: 1995=100)	69.1	68.5	68.2	68.1	68.1	67.6	66.7	65.0	64.9	63.6	63.1	62.7	69.9
Money (M1) (change from same quarter of previous year)	-22.9	-16.5	-8.9	2.8	12.8	11.5	12.4	16.0	17.4	14.1	9.7	0.8	-17.3
Real interest rates (annualized, %)													
Deposit rate	0.9	-2.1	-6.7	-3.1	-2.0	-1.5	-1.2	-0.5	-0.9	0.3	3.0	5.4	1.1
Lending rate	6.5	4.7	5.9	6.9	7.9	6.6	6.8	6.4	7.9	8.0	13.4	14.3	14.9
Equivalent interest rate in foreign currency	30.4	21.2	13.8	16.3	15.8	15.4	14.3	13.6	10.9	12.6	15.9	18.5	20.3

Source: ECLAC, on the basis of official figures.

^a Preliminary figures. ^b Refers to exchange rate for imports.

(c) Foreign-exchange policy

As mentioned above, until the beginning of February 2001 Venezuela's foreign-exchange policy was based on a crawling peg system, which involved a band centred on a nominal parity devaluing at a projected rate of 7% per year. The real effective exchange-rate index has shown a clear trend towards appreciation in recent years (amounting to a cumulative 40% by the end of 2001, if 1996 is taken as the base year) though this was less pronounced in the final year (6%).

Exchange-rate appreciation has undermined the competitiveness of non-traditional exports. These consist largely of non-petroleum products, and, although they only accounted for 20% of total exports in 2001, this was a four-percentage-point increase over the previous year. The value of petroleum exports shrank by over 20%, however. More importantly, the rise in the real exchange rate lowered the cost of imports, which have expanded strongly in recent years –by over 10% in 2001 alone.

In 2001 the resistance of the currency-band regime was put to the test as the bolívar came under pressure. The viability of the band began to look fragile, especially

in August and December, when the central bank had to defend the exchange rate by drawing on international reserves, placing restrictions on foreign-currency purchases and raising interest rates.

(d) Structural reforms

Venezuela has undergone sweeping changes in its political, economic and institutional structure over the last few years. The starting point for the reforms was the new Constitution of the Bolivarian Republic of Venezuela; although this came into force in November 1999, it provides a two-year period for the enactment of related legislation. By late 2001, the legislature had drafted 171 laws, 99 of which had been passed and the remainder were at various stages of discussion.

The enabling act of November 2000 authorizes the government to pass decrees with force of law on a wide range of economic and social issues. By the end of 2001 the President had issued 53 legal decrees with far-reaching repercussions on the economy's productive sectors, covering social security, hydrocarbons, land and agricultural development, ports, coastlines and water bodies, among others.

The Central Bank of Venezuela Act was passed in the second half of 2001, establishing the fundamental objectives of BCV as maintaining price stability and preserving the value of the currency, while promoting harmonious development of the national economy. The responsibilities of BCV include implementing the

macroeconomic coordination agreement to be prepared in conjunction with the Ministry of Finance. This aims to guarantee a consistent economic policy, and to promote and safeguard economic stability, in order to ensure social well-being and human development.

3. The main variables

(a) Economic activity

The Venezuelan economy faltered in 2001, with GDP growing by just 2.7% compared to 4% in 2000. This was attributable to weaker activity in the public sector, which slipped by 1.3%, while the private sector grew by a robust 5.1% compared to 4.5% a year earlier.

Domestic demand remained buoyant, expanding by 4.7%, while fixed investment recovered strongly (12%). Consumption growth broadly followed the path of domestic demand, while inventories fell back sharply. Aggregate demand was constrained by sluggish export growth, especially in oil, which accounts for three quarters of the total. Public-sector exports slumped by 5%, although this was offset by higher foreign sales by the private sector. Aggregate supply was substantially higher than in 2000, thanks to a 10% expansion in imports.

The slowdown in production reflected a 0.9% dip in the oil sector, which hurt public-sector output (where oil accounts for approximately two thirds of the total) and squeezed fiscal revenues. In addition to the production cuts agreed with OPEC, activity in the petroleum sector was further weakened by the economic slowdown in developed countries, especially in the United States, which meant a reduction in oil exports. Private-sector growth was strongest in non-tradables: construction (13%), communications (11.5%), commerce (4.2%), manufacturing (3.2%), and electricity and water (3%). The expansion recorded in the construction sector represented a confident recovery following three successive years of decline, and was of major importance since construction is the largest job-creator per unit of investment and historically has provided a large proportion of total employment. Growth in this sector depends largely on public works and government-funded housing projects.

The transport, warehousing and telecommunications sector took second place in terms of economic performance. Telecommunications was the fast-growing segment, following a decade of sustained growth that has averaged 14% over the last four years. Technological

progress has turned this segment into the supplier of a wide range of services. Manufacturing accounts for the largest share of GDP apart from oil, and has consistently produced around 15% of GDP during the last decade, compared to the 27% generated by oil. The increase in manufacturing output (3.2%) represents a recovery in contrast to the steep declines of a few years ago.

(b) Prices, wages and employment

Inflation has fallen steeply in Venezuela over the last few years. Following rates of 100% in 1996, 40% in 1997 and 30% in 1998, it continued its downward path to 20% in 1999, 13% in 2000 and 12% in 2001. Despite representing a levelling-off and departure from the trend, the 2001 inflation figure is the lowest since 1986. The inflationary slowdown was largely the result of the exchange-rate anchor, which controlled the pace of currency depreciation and had knock-on effects on the price of imported goods. Unlike previous years, in 2001 there was no significant difference between the cumulative rates of inflation for tradable and non-tradable goods.

Unemployment rose to 16.4% in January 2002, compared to 15.8% a year earlier, but the monthly rate of open unemployment in the first seven months of the year was lower than in the same part of 2001. The rate then rose sharply in August, before falling back over the remainder of the year to stand at 11.5% in December.

(c) The external sector

The dollar value of total exports declined by 18% in 2001, largely because of a 23% slump in public-sector exports, including both the oil and non-oil segments, which were down by 23.1% and 10.4%, respectively. As expected, Venezuela's economy was hurt by the negative turn of events in the oil market. Three of the four production cuts agreed upon with OPEC in 2001 were implemented (in February, April and September), which meant a total reduction of 407,000 barrels per

day. The fourth cut took effect on 1 January 2002, shaving a further 175,000 barrels off daily output.

Despite the OPEC policy, the average price of Venezuelan crude dropped steadily, from US\$ 23.2 per barrel in January to US\$ 15.5 in November. On average, the price of Venezuela's petroleum-product basket decreased by US\$ 5.4 dollars with respect to its 2000 level. Public-sector non-oil exports slid by around 10.4%, mainly because of lower exports of iron ore (8.5%), aluminium (5.6%) and gold (83.4%).

Private-sector exports shrank by just 6.6%, thanks largely to an expansion of about 9% in foreign sales of non-petroleum products, whereas those of petroleum sector contracted by 1.3%. The more-than US\$ 6 billion decline in the value of petroleum exports resulted from a 20% drop in the price obtained by Venezuela's petroleum-product basket, combined with a 2.4% decline in the volume exported. Private-sector non-oil exports

performed particularly strongly, expanding by 6.5% to surpass US\$ 5 billion in value.

The balance of payments posted an overall deficit of US\$ 2 billion in 2001, chiefly caused by the slump in petroleum exports, while the current account surplus dwindled from US\$ 13 billion in 2000 to just over US\$ 4 billion in 2001. Another factor behind the erosion of the current account surplus was the surge in imports, which grew by US\$ 1.8 billion (11.6%). The services account recorded a deficit of over US\$ 3 billion, 8% up on the previous year's figure. The capital account improved in 2001 thanks to favourable trends in portfolio investment, but a negative balance on errors and omissions meant a sharp fall in reserves of about US\$ 2 billion. The nominal exchange rate stood at 760 bolívars to the dollar at the end of December 2001, representing a cumulative depreciation of 8% for the year as a whole.