

Bolivarian Republic of Venezuela

The Bolivarian Republic of Venezuela saw its GDP shrink for the fourth year running in 2017, bringing the cumulative contraction to 31.9% with respect to GDP in 2013. Similarly, 2017 was the fourth consecutive year with inflation higher than two digits, and the second year running in which the inflation rate exceeded 300%. The official exchange rate of the bolívar against the dollar depreciated for the fourth straight year at more than double-digit rates. Despite the increase in prices for the Venezuelan oil basket, the monetary authorities injected heavy quantities of base money in order to finance the fiscal deficit, and accordingly the monetary aggregates grew at year-on-year rates of over 400%. The increase in crude oil prices pushed up exports by 9.0% and this, together with the drop in imports (26.0%), yielded a small surplus on the balance-of-payments current account, according to ECLAC estimates. If the tight external situation persists, the present scenario is expected to continue into 2018, with a further decline in GDP (-5.5%), rising inflation, a steep jump in the monetary aggregates, and a significant depreciation of the currency.

Although no up-to-date statistics have been published on the country's public finances, the trends in oil and non-oil revenues suggest that the tax authorities' collection capacities declined.¹ In this connection, the collapse of crude oil prices since 2013 has had a significant impact on the public finances. The earnings of *Petróleos de Venezuela* (PDVSA) have been sharply affected, dropping by 60.6% between 2014 and 2016, thereby cutting the fiscal contribution of PDVSA in those years. In 2017, rising prices for the Venezuelan basket (28.6%) produced a slight easing of the budgetary constraints facing PDVSA, but the drop-off in production recorded in 2016 and 2017 has limited the favourable impact of higher prices. The debt service faced by PDVSA in 2017 (over US\$ 5 billion in 2017, despite the debt swap arranged at the end of 2016), as well as the industry's rising imports of crude oil and derivatives (US\$ 2.6 billion on average over the past five years), have compromised the oil industry's fiscal contribution capacity.

During 2016, non-oil tax revenues grew by 185.6% in nominal terms, according to information from the National Integrated Customs and Tax Administration (SENIAT), and the cumulative amount between January and October 2017 shows an increase of 350.2% over the same period of 2016. The high levels of inflation prevailing in the Venezuelan economy have meant that, when corrected for price changes, domestic tax revenues, far from growing, were down by 29.1% in 2016 and by 53% in 2017.²

The direct external debt of the central government rose by US\$ 4.229 billion in 2016, up by 10% from the balance at the end of 2015. However, the central government's domestic debt, valued in dollars, shrank by 21% that year, reflecting the devaluation of the bolívar. In 2017 the fiscal authorities, PDVSA and certain public enterprises were faced with high levels of external debt service. In the case of the central government, payments exceeded US\$ 2.5 billion and they reach over US\$ 5 billion per year in 2018, 2019 and 2020. For its part, PDVSA owed more than US\$ 6 billion in principal and interest payments in 2017, and for the next three years its total debt service will be between US\$ 3 billion and US\$ 5.5 billion annually. The national government has announced a restructuring process for the external debt, which began on 13 November 2017. Between the end of 2016 and October 2017, the prices of Venezuelan bonds (central government or PDVSA) fell sharply, by more than 40%. As part of the

¹ The Ministry of Economy and Finance has not published figures on fiscal management since 2013, nor has it published data on the public debt since March 2017.

² The deflator used is based on the inflation rate reported to the International Monetary Fund (IMF) by the Central Bank (BCV) in 2016, and cumulative inflation reported by the National Assembly for 2017.

restructuring process, the government reached an agreement with its Russian counterpart to restructure the Venezuelan debt (US\$ 3.5 billion) owed to that country.

Monetary aggregates rose by more than 400% between October 2016 and October 2017. This is the third year running in which the monetary base has risen at three-digit rates, and it has been growing at year-on-year rates of over 70% for the last 15 quarters. In the third quarter of 2017, the year-on-year increase was 686.1%.

The performance of the monetary base is closely linked to the financing provided by the central bank to the public sector, in particular to PDVSA. In 2016, monetary financing reached 19.1 percentage points of GDP, and a breakdown of the monetary base between December 2016 and October 2017 shows that financing to non-financial public enterprises jumped by 977.7%, representing 1.8 times the balance of the monetary base.

Credit to the private sector, measured in nominal terms, has grown at annualized rates of more than 60% from the fourth quarter of 2013, and in the third quarter of 2017 it grew by 322.1%. Given the sharp rise in prices, however, this has meant a decline of over 30% in credit at year-on-year rates since the first quarter of 2016. Nominal interest rates have remained quite stable but, when corrected for inflation, they represent highly negative real interest rates that, together with falling incomes, have discouraged demand for assets denominated in bolívares.

The exchange-rate regime underwent modifications in May 2017, with the announcement that sales of foreign exchange through the floating exchange rate system (DICOM, the supplementary exchange rate used to pay for non-essential priority imports) would be made within a band that would vary according to market conditions, while at the same time maintaining the exchange rate applied for public sector imports. Taking the DICOM exchange rate as a benchmark, the bolívar depreciated by 396% between January and November 2017, and by 1,645% if the exchange rate on the parallel market is used as the benchmark. In September 2017, the exchange authorities announced the use of such currencies as the yuan, the rouble and the rupee on the Venezuelan exchange market.

The country's international reserves fell by 32.8% in 2016, after dropping 25.9% in 2015. In October 2017, the international reserves stood at their lowest level of the last 21 years: US\$ 9.767 billion, representing a drop of 11.1% from the value at the close of 2016. This performance reflects the fact that inflows from international trade (essentially oil exports), foreign investment and external borrowings (bonds or loans) have been inadequate to cover debt obligations and imports. In an effort to boost its external liquidity, the central bank has liquidated a portion of its holdings of dollar-denominated PDVSA bonds, at discounts exceeding 70%, and has resorted to selling its holdings of gold.

ECLAC estimates, based on information provided by the Organization of Petroleum Exporting Countries (OPEC) and trade data supplied by the country's principal trading partners, indicate that Venezuelan exports shrank by 28% in 2016, and imports were down by 42%.³ In 2017, the outcome should show a surplus on the current account (around 0.7% of GDP) for the first time since 2014. The terms of trade rose by 13% this year, after falling by 41% in 2015 and 16% in 2016.

According to OPEC, the country's average daily crude oil production in 2016 fell by some 216,000 barrels, representing a contraction of 9.1% with respect to 2015. In 2017, to October, the fall in crude oil output was 112,000 barrels a day, representing a 5.4% decline from the value in 2016. Accordingly, the cumulative drop since 2013 has been 400,000 barrels a day. Crude oil refining has also

³ At present there is no official information available on the balance of payments or the national accounts since 2015.

been affected, and activity at the country's main refineries has slowed, while output of the base metals firms has been impacted by problems with the generation and distribution of electricity and other inputs.

Another factor that hurt economic activity in the fourth quarter of 2016 and in the first half of 2017 was the announcement, in December 2016, that the 100 bolívar bank note was being withdrawn from circulation: that denomination was the most widely used in the Venezuelan economy at that time, accounting for 38% of total bank notes in circulation, and 76.4% of the value of currency in circulation.⁴ In this setting, ECLAC estimates that GDP will shrink by 9.5% in 2017, representing the fourth consecutive year of contraction since 2013. If the external restriction persists, and given moderate growth in crude oil prices, the country will very likely remain in recession, and ECLAC consequently estimates that GDP will shrink by 5.5% in 2018.

For 2016, the central bank reported an inflation rate of 302.7% to the International Monetary Fund (IMF).⁵ Inflationary pressures have continued in 2017, and this is expected to be the third straight year with a triple-digit inflation rate.⁶ The reasons for the soaring inflation include steep growth in the monetary aggregates, financing of the fiscal deficit with the proceeds of monetary emission, the sharp depreciation of the exchange rate, wage increases and severe restrictions on obtaining foreign currency.

Taken together, the components of the minimum wage (basic minimum wage and food bonus) were raised six times during 2016, for a cumulative increase of 454%. In 2017 the minimum wage was boosted again on six occasions, and the cumulative increase was 403%. The National Statistics Institute (INE) has not published data on the labour market since April 2016.

⁴ Although the announcement was made on 11 December 2016, the government has extended the use of these banknotes, given delays in the delivery of the new banknotes. At the time of writing, the 100 bolívar banknote was still in circulation.

⁵ See International Monetary Fund (IMF), World Economic Outlook Database [online], October 2017.

⁶ Since January 2017, the National Assembly has been publishing a national price index, according to which, in October 2017, cumulative inflation was 857.6% with respect to December 2016, and average monthly inflation was 25.7%.