

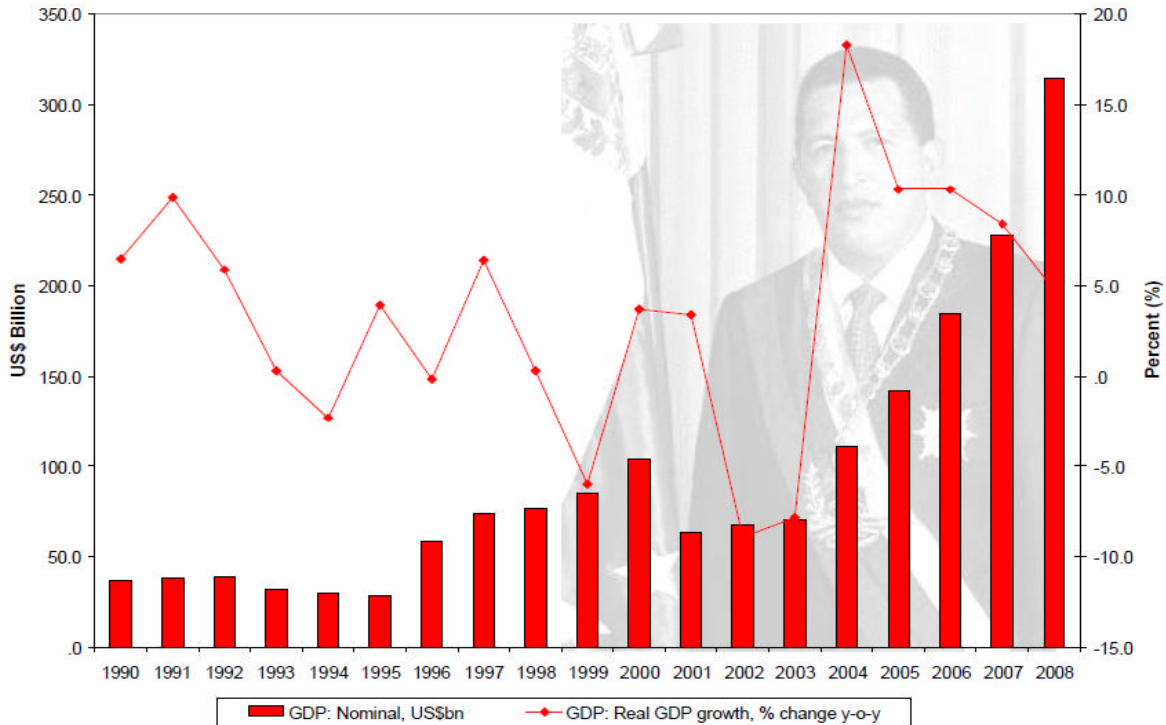


Chavez, the Man behind the chatter...

If you asked any financial investor about the single most important driving factor in Venezuela, without a doubt the response would be President Chavez. Chavez, a man despised for his random outbursts which usually send the market into disarray and loved for his passion for the poor, was once named one of Time Magazine's 100 most influential people in the world. But influence is only part of the equation as true character and leadership is shown by performance. Many have argued over Hugo Chavez' socialist-type governance and some have even called him a dictator with justified reasoning but like a student passing a test, Chavez' true worth is shown via an assessment of the macroeconomic statistics over his tenure as the President of the Bolivarian Republic of Venezuela.

His reign as president started ten years ago when he was sworn into presidency after winning the December 1998 elections with a 56% majority vote. Having been elected, he made changes to the constitution and was then re-elected under the new constitution in 2000 where he served his first term until 2006. In 2006, he was again re-elected with a 61% majority vote for his second term which he is currently serving and a change to the constitutional referendum in February of this year now allows him to seek another term in office. His term in office was by no means a smooth ride as Venezuela was, and to some extent still is, fraught with social and political upheaval. Real Gross Domestic Output (GDP) was unavoidably affected by each of these upsets. For example, as shown in the Chart 1, a national strike in addition to a coup in 2002 – 2003 resulted in a drastic decline in real GDP. However, Venezuela's real GDP, under Chavez' terms in office, has enjoyed impressive growth rates when compared to the growth rates seen in the pre-Chavez era (Chart 1).

Chart 1: Venezuela GDP Statistics



Source: *Business Monitor International*

Throughout his tenure, Chavez has held in high esteem the ideals of socialism rather than capitalism. To re-iterate his position and a quote that suggests his discomfort with the US economic ideals, in a speech in 2005 he stated, *'I am convinced that the way to build a new and better world is not capitalism. Capitalism leads us straight to hell.'* Stemming from his interest in socialism, his policies have been aligned towards the equal distribution of wealth and power and looking after the needs of the poor and it would therefore be unjust not to mention the change in the standard of living throughout his term. One of the most recognized measures of standard of living is the Human Development Index (HDI), created by economists Amartya Sen and Mahbub Ul Haq in 1990. According to the HDI, Venezuela's standard of living has continuously improved under the Chavez administration. Also "Poverty has been dropping in an important manner over the last ten years, from 49% in 1998 to 26.4% in 2009," said Elias Eljuri, president of Venezuela's National Statistics Institute. The Unemployment rate has also declined over the last ten years, falling from 11% at the end of 1998 to its current level of 8%. This is still favourable compared to the unemployment rate seen in similarly rated B+ (by Standard and Poor's) countries which typically has a rate of 11.5%. A recent study by Bloomberg indicated that Venezuela has an extremely high misery rate when compared to the rest of the world suggesting that much work still needs to be done in the social arena.

A decline in poverty would suggest that much was done to address the needs of the poor and this was indeed true. Under Chavez' rule, the latest statistics from the Sistema de Indicadores Sociales de Venezuela (Integrated Social Indicators System of the Bolivarian Republic of Venezuela) show that social spending increased 194% from 17 million bolivars in 1999 to 49.7 million bolivars in 2007. A fairer comparison is seen by looking at social spending as a percentage of GDP and also as a percentage of total public spending (Table 1), both of which have increased within the time period given.

Table 1: Venezuela's Social Spending

	1998	2006
As a % of Public Spending	47.6	54.8
As a % of GDP	8.2	13.6
Sources: Sistema de Indicadores Sociales de Venezuela (SISOV) and author's calculations		

In particular, the major categories of spending are focused on education and social security but one can argue that Venezuela and Latin America, by extension, still has one of the highest crime rates in the world.

Increased social spending has also had implications for the fiscal accounts. The general government balance has fluctuated from deficit to surplus due to poor fiscal management and to changes in oil prices. In 2009, Venezuela is expected to post a deficit of 5.4% of GDP, the worst fiscal deficit for Venezuela since 2003 when the national strike limited the flow of oil revenues to the government. The challenge in 2009 is the actual decline in oil prices accruing from the uncertainty in the global economy combined with continued levels of elevated expenditures. International investors have been urging greater fiscal prudence as continued mismanagement of funds are already having and could have further negative rating consequences for the country. Immense controversy has surrounded the nationalization drive upon which Chavez has embarked over the past two years. He announced his intention to nationalize key industries such as electricity, telecommunications, and strategic oil operations as it has been suggested that past private ownership in these industries made them relatively unresponsive to the domestic needs but whether becoming state-controlled will solve this problem is questionable. Such a move has had dire effects on Foreign Direct Investment (FDI). Since Chavez took office in 1999 net FDI has turned negative. It represented 5.1% of GDP in 1998 but as at 2007, it represented -0.7% and with more news of nationalization, this ratio could potentially worsen.

Debt balances and external balances such as the current account balance and International Reserves remain relatively robust. Prior to Chavez' years in power, the current account balance was highest in 1996 at USD 8.9 billion. In 2008, Venezuela recorded a balance of USD 39.2 billion but this is expected to quickly turn into a deficit in 2009 as oil prices plunged. With a turnaround in oil prices and a belief that global economic recovery is near, the external balances could improve going into elections in 2012. Debt expressed as a percentage of GDP has also declined over the years.

Though Chavez is a source for concern to international investors because of his outspoken and controversial nature, the external balances have improved during his tenure. Also, on the social front he successfully increased spending and lowered the unemployment rate and for that, credit is due. One can, however, ask that in an oil rich country such as his, (and as in many other countries in the world blessed with such a natural resource) could he have done more? The better management of funds on the fiscal side could have gone further to serve the needs of not only the poor but the entire population for which he has the responsibility to serve.

FINANCIAL & ECONOMIC INDICATORS

As at 24 September, 2009

<u>Exchange Rate/US\$</u>	<u>Closing Value</u>	<u>Previous Week</u>
Yen	91.27	91.08
Euro	1.47	1.47
Jamaica	89.10	89.10
Guyana	204.90	205.20

<u>Commodity Prices</u>	<u>Closing Value</u>	<u>Previous Week</u>
Crude oil (US\$/bbl)	65.89	72.47
Natural Gas (US\$/mmbtu)	3.56	3.46
Gold (US\$/Troy Ounce)	994.10	1,013.60

Eurobond Indices (As at 24-09-09)

Lehman Brothers Global Aggregate Index (Return % YTD)	7.45
JP Morgan EMBI+ (Basis points)	330
JP Morgan Central America and Caribbean Index (CACI) (YTD return %)	31.90

<u>Policy Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
United States	0.13	0.18
Euro Zone	1.00	1.00
Japan	0.13	0.10
Brazil	8.75	8.75
Trinidad	6.75	6.75
Jamaica	12.50	12.50
Barbados	2.50	2.50

<u>Market Interest Rates (%)</u>	<u>Closing Value</u>	<u>Previous Week</u>
US 90-day T-Bill	0.09	0.09
US 10-Yr Treasury	3.38	3.39
3-month UK Libor	0.56	0.59
Japan 90-day T-Bill	0.28	0.28
Brazil 90-day T-Bill	8.65	8.60
TT 90-day T-Bill	1.98	2.46
Jamaica 90-day T-Bill	16.39	16.72
Barbados 90-day T-Bill	3.65	3.65

Sources: Bloomberg, J.P. Morgan, CMMB, Central Bank of Trinidad and Tobago, Bank of Jamaica, Central Bank of Barbados, www.lehman.com

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