Euler Hermes Economic Research

Country Risk Analysis

Venezuela

Uncertain times

General Information

GDP	USD316.5bn (World ranking 33, World Bank 2011)
Population	29.28 millions (World ranking 44, World Bank 2011)
Form of state	Federal Republic
Head of government	President Nicolas MADURO Moros (interim)
Next elections	2013, presidential

Strengths

- Large-scale energy resources.
- Moderate external debt levels.
- President Chavez has strong popular support, as confirmed in his re-election in late-2012.

Weaknesses

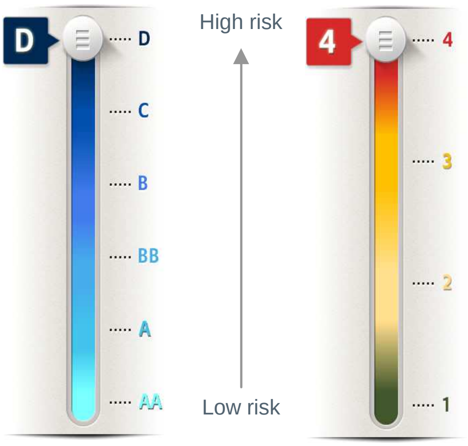
- Political system built around former president Chavez' populist/nationalist left-leaning Bolivarian Revolution. After his death there is considerable uncertainty over the future direction of the country and some risk to stability.
- Over-dependence on oil. (95% of export earnings.)
- Policies are highly interventionist and unsustainable without high oil prices.
- External balance in surplus, but FX reserves used to fund government spending and with relatively at central bank.
- Exchange controls to hold fixed exchange rate, with periodic devaluations to maintain fiscal revenues.
- Weak business environment. Heavy state intervention includes unpredictable nationalisation in various sectors.

Country Rating

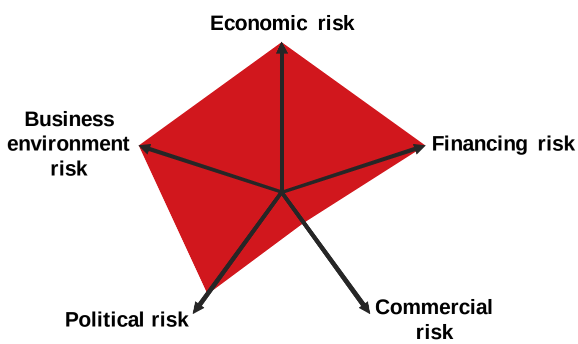
D4

Country Grade

Country Risk Level



Risk Dimensions



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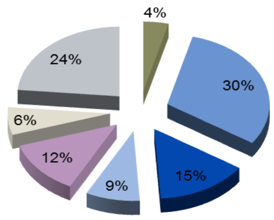
Economic Structure

GDP breakdown (% of total, 2010)



Sources: Chelem, IHS Global Insight, Euler Hermes

Trade structure (% of total, 2010)

By product

Exports		Rank		Imports
United States	50%	1	26%	United States
China	13%	2	14%	China
India	7%	3	10%	Brazil
Cuba	4%	4	5%	Panama
Singapore	4%	5	4%	Argentina

By destination/origin

Exports (% of total)		Rank		Imports (% of total)
Petroleum, petroleum products and related	84%	1	7%	Other industrial machinery and parts
Iron and steel	5%	2	7%	Medicinal and pharmaceutical products
Medicinal and pharmaceutical products	2%	3	6%	Specialised machinery
Metalliferous ores and metal scrap	2%	4	5%	Road vehicles
Non-ferrous metals	1%	5	5%	Electrical machinery, apparatus and appliances,

Economic Forecasts

	Average 2000-08	2009	2010	2011	2012f	2013f	2014f
GDP growth (% change)	4.8	-3.2	-1.5	4.2	5.5	3.0	3.2
Inflation (%, end-year)	20.9	25.1	27.2	27.6	19.5	29.0	27.0
Fiscal balance (% of GDP)	-0.2	-8.1	-5.9	-5.4	-7.5	-6.5	-6.0
Public debt (% of GDP)	35.9	33.8	40.2	46.8	51.0	55.0	60.0
Current account (% of GDP)	10.7	0.8	4.3	7.5	4.5	3.4	2.3
External debt (% of GDP)	32.4	24.3	38.4	35.0	28.0	29.0	30.0

Sources: IHS Global Insight, National sources, Euler Hermes

Economic Growth

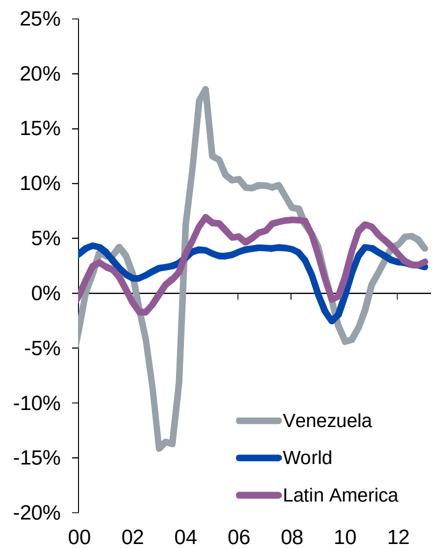
Growth accelerated in 2012 ahead of elections…

Growth of GDP accelerated in 2012, boosted by public spending (investment and subsidies) ahead of presidential elections in October. Petroleum remains crucial, as the sector accounts directly for 11% of GDP and 95% of goods exports. In 2012 output of the sector increased by just 1.5%, after a small fall in 2010 and the state oil company, PDVSA, is widely thought to lack sufficient technical resources to make the necessary investment. Electricity shortages also remain a problem. Annual average growth of real per capita GDP was 1.5% in the past ten years.

…but will slow in 2013-14

We expect growth to slow to 3% in 2013 followed by 3.2% in 2014. However, downside risks are evident. These include: i) political uncertainty arising from the death of President Chavez ii) uncertainty over oil prices iii) weak investment prospects arising from interventionist policies and iv) the need to slow public spending to sustain the fiscal balance, which will be helped but not by the latest devaluation in February, but is unlikely to occur ahead of another election, indeed in the near term the election will probably boost spending.

GDP growth (y/y, 4 qtrs cumulated %)

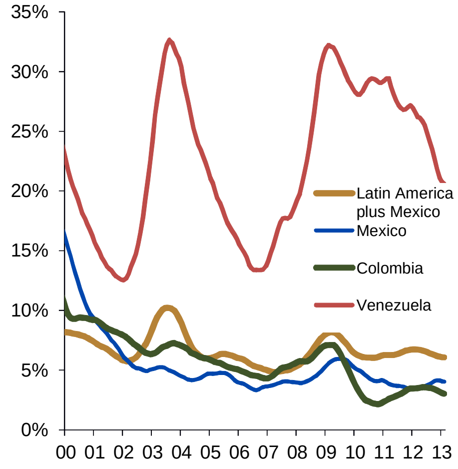


Sources: IHS Global Insight, Euler Hermes

Economic Policies

The overall policy framework is highly populist and interventionist, based on high levels of social spending in support of former president Chavez' leftist Bolivarian revolution, accompanied by nationalisation of sectors and companies in support of these objectives. However, the current policy mix is unbalanced and ultimately unsustainable, especially if oil prices were to fall. The most likely scenario at this point is that Chavez' chosen successor, interim president Maduro, will win the election which should be called shortly and will try to consolidate the broad thrust of policies, but will face a more governance pressures than his predecessor, as it will not be not be easy for him (or anyone) to replicate Chavez' charismatic leadership.

Inflation (%)



Sources: IHS Global Insight, Euler Hermes

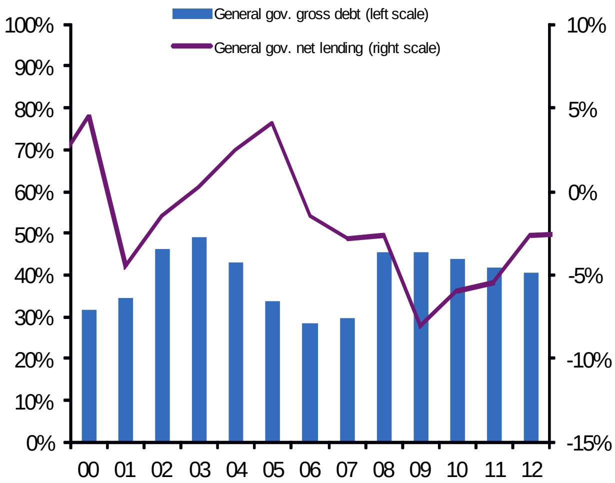
High inflation, FX controls and periodic devaluation…

Inflation eased in 2012, partly as a result of controlled prices and the absence of devaluation, but is set to accelerate again in 2013 towards 30% by year-end from just under 20% at end-2012. Real interest rates are negative as monetary policy is geared to the fixed exchange rate which is managed through foreign exchange controls to prevent chronic capital flight. The exchange rate is also subject to periodic devaluation, the latest of which (32%) was in February 2013. As periodic devaluation is required to maintain government revenues and spending, further devaluations are likely at intervals.

The fiscal deficit has widened….

IMF estimates of the general government balance point to an increase in the deficit in 2012 to -7.4% of GDP from -5.4% in 2011, while the primary deficit (before taking account of interest payments) has widened to -6.3% from -4.7%. In 2010-12, according to IMF estimates, public expenditure as a % of GDP has increased from 37% to 44%. Moreover, there are substantial off-budget expenditures, including expenditure by PDVSA and FODEN (the government development fund, which utilises transfers from central bank reserves, leaving an opaque picture overall, but one that is unsustainable without high oil prices.

Fiscal balance and General government debt (% GDP)



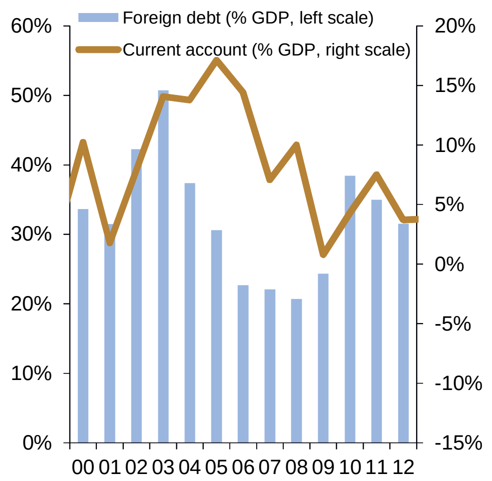
…and public debt is increasing

According to IMF estimates the general government debt-GDP ratio is rising sharply, from 26% in 2008 to an estimated 51% in 2012. The ratio is likely to continue to increase, hitting 60% in 2014.

The current account surplus is declining…

The current account surplus is likely to have fallen to 4.5% of GDP in 2012 from 8.6% in 2011, as imports surged ahead of the elections, while export growth was fairly modest. The surplus will probably fall further in 2013 and 2014, though much depends on oil prices. Foreign direct investment (FDI) inflows are quite low, reflecting many uncertainties, not least government nationalisations in various key sectors. Indeed, net FDI flows were probably negative in 2012.

External debt and current account (% of GDP)

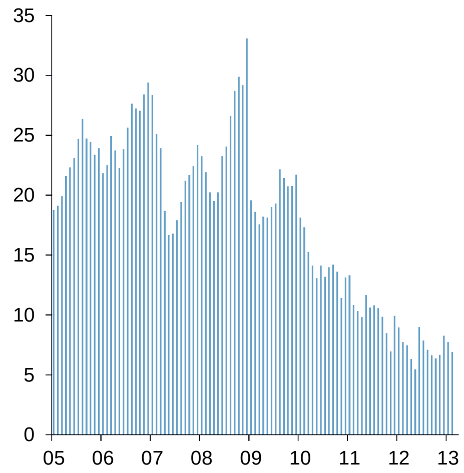


Sources: IHS Global Insight, Euler Hermes

…foreign exchange reserves have fallen

Official foreign exchange reserves (excluding gold) have fallen sharply and cover less than 1.5 months imports of goods and services and only around an estimated 25% of external debt payments (M/L term and ST) falling due in 2013. There has been an increase in gold reserves, however, and transfers from central bank reserves to government funds. External debt ratios, however, have remained relatively low and servicing will be managed through controls on access to foreign exchange.

FX reserves (USDbn)



Sources: IHS Global Insight, Euler Hermes

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