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Credit Suisse Economics

Venezuela: A new phase?

- **All data available continue to suggest that the economy will grow this year for the first time since 2013, in line with our long-held forecast.** Positive factors fueling the economy include the positive income effect from high oil prices and the widespread use of foreign currencies in everyday activities. However, this is old news. What is new are Chavismo's negotiations with the opposition leadership and the opposition's decision to partake in an electoral process for the first time since 2018. It is far too soon to think that an end to the political impasse will come from these talks, but this is finally a positive sign. Mayoral and gubernatorial elections will take place in November, which might help in the return of democratic conditions. A bit of growth and a bit of improvement in politics? Maybe the country is finally entering into a new phase.
- **We are increasing our 2021 real GDP growth forecast to 5.5%, from 4.0% previously.** Our revision stems largely from the improvement in oil output and the faster-than-expected return-to-normal in mobility levels. Available data show that oil GDP is likely to increase between 3.0% yoy and 5.0% yoy this year, as opposed to our previous expectation of no growth. Meanwhile, mobility as of late September was above the pre-pandemic baseline, a much faster and stronger recovery than the one we initially envisioned. For 2022, we are revising our real GDP growth forecast to 4.5%, from 3.0% previously – our estimate for next year assumes stability in oil output and non-oil GDP growth of roughly 4.0%. Though mobility appears higher than in the rest of the region (relative to pre-pandemic levels), Venezuela's growth will likely underperform that of LatAm in 2021.
- **High inflation will likely persist, despite the government's decision to remove six zeroes from the bolivar starting in October.** We have long noted that bolivar inflation no longer has the impact in real activity it had in the past. However, as a reference, we are revising our 2021 year-end annual headline inflation forecast to 915%, from a previous estimate of 1,950%; for year-end 2022, our inflation forecast is of about 800%. We think that a reduction in scarcity levels might be aiding in decelerating price pressures at the margin. Authorities have stated that, as of October, the "digital bolivar" will be part of the legal tender – the central bank specified that the value of physical bolivar bills and digital bolivars would be the same. Venezuelans have relied on digital transactions for a long time, as the use of bills became cumbersome once hyperinflation kicked in. We think the digital bolivar may be just a measure to avoid the need to issue banknotes. Physical bolivar transactions are relatively non-existent at this point.

CONTRIBUTOR

Alberto J. Rojas
52 55 5283 8975
alberto.rojas@credit-suisse.com

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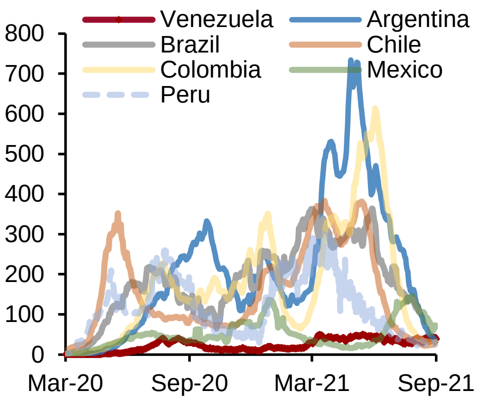
- **A favorable external backdrop and PDVSA's output recovery will likely lead to a current account surplus in 2021.** According to *Reuters*, Venezuelan oil exports averaged increased to 670kbpd in July/August 2021, up from 410kpbd a year ago. Using the Merey price basket, and several assumptions, we estimate that Venezuelan total exports could reach about $15bn this year. Meanwhile, we estimate imports are likely to total about $7.5bn. The trade merchandise account, plus a few other billions from remittances, are likely to tilt the current account balance toward a surplus of $3.4bn. We note that international reserves have remained range-bound between $6.2bn and $6.5bn for several quarters; we do not account for the IMF's SDR allocation of $5bn corresponding to Venezuela, as Mr. Maduro's government does not have access to it. We would expect the oil export inflows to lead to increases in the reserves, but so far this has not happened; we think a possible explanation is that export USD proceeds are not repatriated and sold to the central bank due to issues involving foreign financial sanctions.
- **We estimate that total foreign defaulted debt issued by Venezuela, PDVSA, and Elecar has reached roughly $36.0bn.** This includes both missed interest and amortization payments. On this front, we have not seen many developments, as bondholders remain in a standstill. An improvement in democratic conditions could lead to a more positive outlook, however. We note that a large reason why bondholders have not been more active toward Venezuelan assets is due to the US's decision to protect said assets and support the interim government of Juan Guaidó. A resolution to the political crisis would bring questions as to whether the protection of foreign assets is still required and heat up (even if just slightly) debt talks, in our view.
- **Regarding the COVID-19 situation, vaccinations are taking place, albeit at a slow pace.** As of early September, data from the Pan American Health Organization suggested that about 30% of the Venezuelan population had received at least one dose of the vaccine. The country is largely relying on the Sinopharm and Sputnik V vaccines, in line with our expectation that Chavismo would depend on geopolitical allies China and Russia. Mr. Maduro announced in early August that through the COVAX facility the country would get 6.2mn additional vaccine doses, which should help in speeding up the immunization campaign. We think that Venezuelan authorities will keep opening up the country in line with regional peers.
- **The opposition has decided to participate in the mayoral and gubernatorial elections set for 21 November.** This is the first time, since 2018, that the opposition leadership has agreed to be part of an electoral process. This decision follows the ongoing talks that are taking place in Mexico, with the support of Norway's government. Over the past few years, many negotiations have taken place, with the large bulk of them accomplishing hardly anything, as both parties have been unwilling to find palatable compromises. Thus, it is extremely hard for us to be optimistic that this time around is when everything will change. Having said that, this is indeed the first time that there is an agreement to have somewhat competitive elections – that is new and could be a first step toward an improvement of democratic conditions in the country.
- **The opposition seems divided, and it appears unlikely that there will be a cohesive coalition nationwide; thus, Chavismo might be competitive.** However, even in a scenario in which opposition candidates do not do well, a return to ballots and to electoral battles is better than the current scenario, in which the political crisis just deepens and there are no glimmers of change. Our hope is that after this election, both Chavismo and the opposition understand that the way out of this hole is through elections, no matter how bitter are the concessions required to get there.

Figure 1: Covid-19 daily new cases

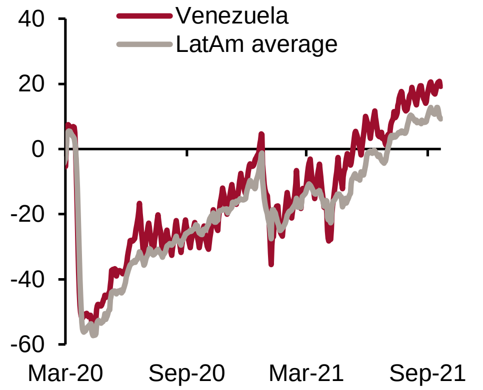
Seven-day moving average, per 1mn people



Source: Johns Hopkins University, Credit Suisse

Figure 2: Mobility tracker

% change in visits to retail and recreation sites, grocery and pharmacy stores, and workplaces compared with Jan/Feb 2020 baseline



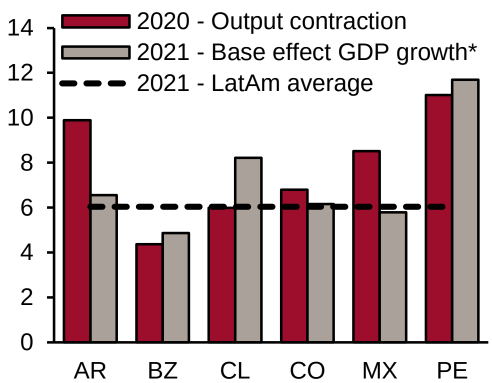
Source: Google community mobility reports, Credit Suisse

Venezuela's new COVID-19 infection data suggest that there have been no spikes in cases – the reliability of these figures is low, however.

Regardless, mobility indicators suggest that the country is opening up in line with regional peers; this has taken place slightly faster than we expected.

Figure 3: Real GDP analysis

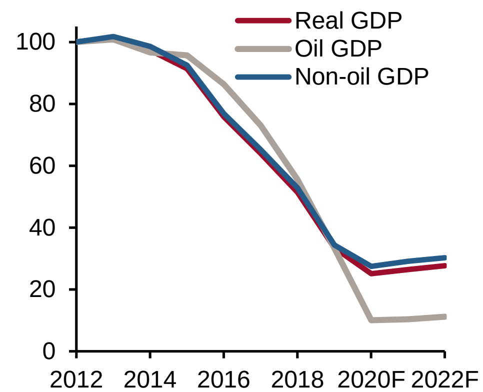
Percentage points (p.p.), dotted line is LatAm's average estimated base effect GDP growth



*Base effect growth is estimated assuming the last data point of SA Quarterly GDP holds unchanged in the balance of 2021.
Source: Statistics institutes, central bank, Credit Suisse

Figure 4: Real GDP

Indices, 100= 2012



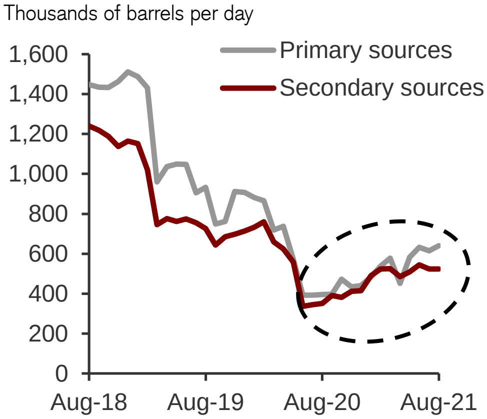
Source: Central bank, Credit Suisse

Latin America's base effect growth for 2021 is an average of 6.0%. Thus, if Venezuela's economy grows 5.5% this year, it would still be underperforming regional peers.

We now expect that both oil and non-oil GDP will contribute positively to economic performance in 2021 and 2022.

Figure 5: Venezuela's oil output as reported by OPEC

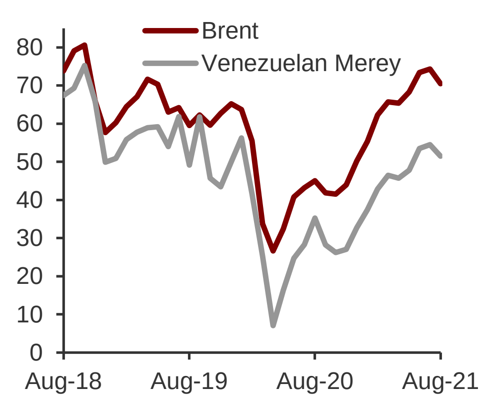
Thousands of barrels per day



Source: OPEC, the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

Figure 6: Oil prices

Monthly average, $ per barrel,



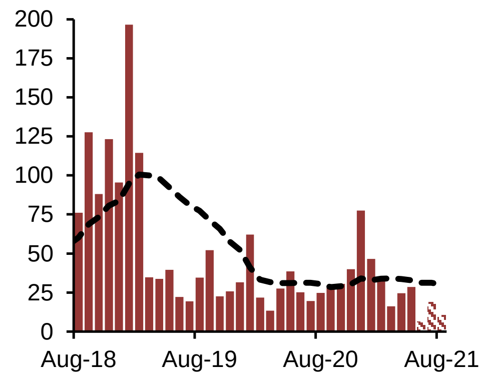
Source: OPEC, Credit Suisse

Petroleum output has continued to improve, in line with our expectations. Despite news about production issues in August, we expect the oil sector to continue recovering slowly.

The increase in oil prices will likely lead to greater income for the government.

Figure 7: Consumer price inflation

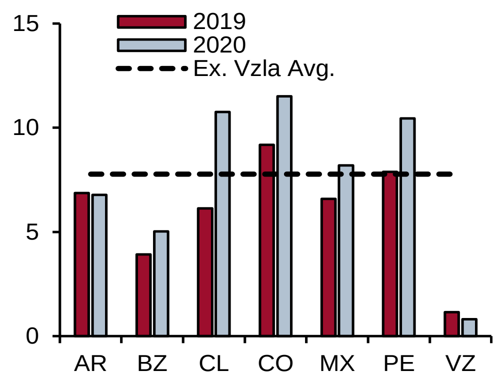
% mom; June, July and August data is from opposition-controlled National Assembly, dotted line is 12-month rolling average



Source: Central bank, Credit Suisse

Figure 8: Monetary base in selected countries

% of GDP



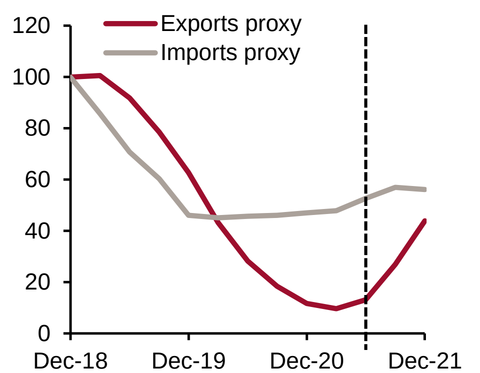
Source: Central banks, Credit Suisse

We have consistently noted that since foreign currency usage is so prevalent, we do not see much benefit on focusing on bolivar inflation; we highlight, though, that monthly inflation has decelerated.

The monetary base in Venezuela is minimal in comparison with peers; however, economic activity is clearly taking place. The advent of the digital bolivar is in line with authorities' interest in minimizing/eliminating the use of bolivar banknotes, in our view.

Figure 9: Export and import proxies

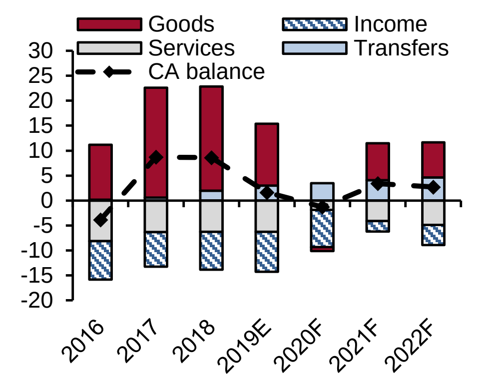
Sep-18=100, 4-quarter rolling basis, CS forecasts after dotted line



Source: IMF, OPEC, the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

Figure 10: Current account balance

$bn



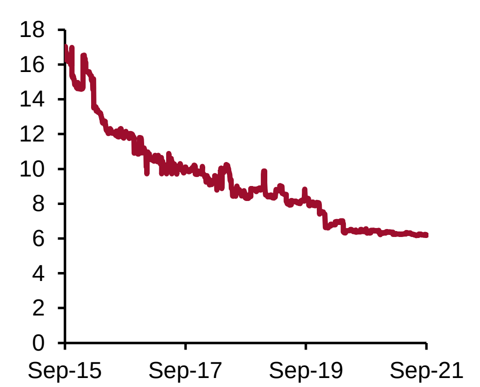
Source: Central bank, PDVSA, Credit Suisse

Imports have increased in line with the improving domestic demand; higher oil prices will lead to greater USD export inflows.

The improvement in terms of trade will likely result in a robust trade merchandise balance; this, along with remittance inflows, should lead to a current account surplus of over $3.0bn in 2021. For 2022, we expect similar dynamics to take place.

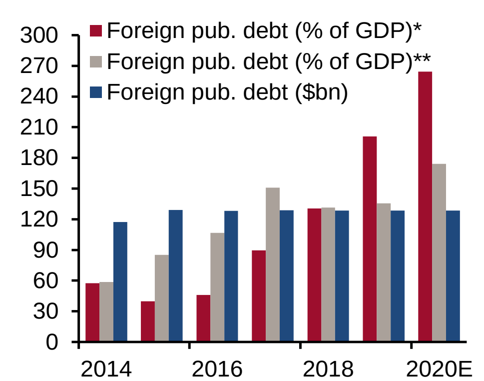
Figure 11: Gross international reserves

$bn, note that we are excluding the IMF SDR allocation corresponding to Venezuela



Source: Central bank, Credit Suisse

Figure 12: Foreign public debt metrics



* We use the IMF nominal GDP estimate as the denominator.
** We use the CS nominal GDP estimate as the denominator.
Source: IMF, Central bank, PDVSA, Credit Suisse

International reserves have remained stable at between $6.2bn and $6.4bn over the past few quarters; we find no compelling reasons to think they would decline in a higher USD inflow environment.

The crisis has shrunk the economy to around a quarter or a fifth of the size it was in the early 2010s. Total foreign debt is likely around 200% of GDP. Any future debt renegotiation will involve a steep haircut, in our view.

Venezuela: Selected economic indicators

	2014	2015	2016	2017	2018	2019E	2020E	2021F	2022F
National accounts, population and unemployment									
Real GDP growth (%)	-3.9	-6.2	-17.0	-15.7	-19.6	-35.0	-25.0	5.5	4.5
Growth in real private consumption (%)	-3.4	-8.9	-19.4	-16.2	-20.1	-37.2	-26.1	5.8	4.8
Growth in real fixed investment (%)	-16.9	-20.4	-45.1	-45.3	-37.5	-42.8	-22.3	3.5	5.3
Fixed investment (% of GDP)	27.5	23.4	15.5	10.0	7.8	6.1	4.8	n.a.	n.a.
Nominal GDP ($bn)	200.0	151.6	120.0	85.3	97.9	94.8	73.8	n.a.	n.a.
Population (mn)	30.1	30.6	30.5	28.5	27.5	25.5	25.5	25.0	25.5
GDP per capita ($)	6,642	4,959	3,934	2,994	3,560	3,719	2,895	n.a.	n.a.
Unemployment (% of labor force, end-year)	5.9	6.3	7.0	6.7	6.8	n.a.	n.a.	n.a.	n.a.
Prices, interest rates and exchange rates									
CPI inflation (%, December to December)	68.5	180.9	350.0	844.4	130015	9585	2959.8	915.1	791.6
CPI inflation (%, average)	62.2	121.7	270.6	433.3	65133	19906	2355.1	1645.5	740.9
Nominal wage growth (% year-on-year change) (1)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Exchange rate (VEB per USD, end-year) (2)	27.0	47.7	122.0	2152	700	54700	1,108,000.00	n.a.	n.a.
Exchange rate (VEB per USD, average) (2)	21.7	61.8	255.4	2232	115	12847	325,000.00	n.a.	n.a.
90 day deposit rate (%, end-year)	14.5	15.1	14.9	14.5	15.0	n.a.	n.a.	n.a.	n.a.
Fiscal data									
Consolidated public sector overall balance (% of GDP)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Consolidated public sector primary balance (% of GDP)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Consolidated public sector expenditure (% of GDP)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Money supply and credit									
Broad money supply (M2, % of GDP)	46.2	42.9	33.9	66.7	7.2	3.3	2.3	n.a.	n.a.
Broad money supply (M2, % year-on-year change)	66.7	100.0	160.0	1122.1	63232.0	4945.6	1286.8	n.a.	n.a.
Domestic credit (% of GDP)	21.4	33.9	40.1	21.9	6.2	2.0	3.3	n.a.	n.a.
Domestic credit (% year-on-year)	80.5	111.5	139.9	585.6	964.0	2376.6	2465.8	n.a.	n.a.
Domestic credit to private sector (% of GDP)	21.0	33.3	39.5	21.4	5.9	1.9	3.2	n.a.	n.a.
Domestic credit to private sector (% year-on-year)	78.8	112.7	140.6	580.1	933.3	2337.5	2506.9	n.a.	n.a.
Balance of payments									
Exports (goods and non-factor services, % of GDP)	37.3	24.6	22.8	39.9	34.4	19.5	7.5	n.a.	n.a.
Imports (goods and non-factor services, % of GDP)	23.6	22.0	13.6	14.1	13.1	6.5	8.6	n.a.	n.a.
Exports (goods and non-factor services, % change in $ value)	-15.9	-50.1	-26.4	24.2	-1.0	-45.0	-70.0	170.0	5.0
Imports (goods and non-factor services, % change in $ value)	-17.4	-29.5	-50.9	-26.6	6.3	-52.0	3.0	20.0	15.0
Current account balance ($bn)	4.9	-16.1	-3.9	8.7	8.6	1.6	-1.3	3.4	2.7
Current account (% of GDP)	2.5	-10.6	-3.2	10.2	8.8	1.7	-1.7	n.a.	n.a.
Net FDI ($bn)	1.9	-3.4	0.4	0.0	-2.3	0.2	-0.3	-0.2	0.0
Scheduled debt amortization ($bn)	4.5	4.7	3.6	4.6	2.9	4.1	6.1	3.8	4.8
Foreign debt and reserves									
Foreign debt ($bn, end-year)	135.8	151.0	149.9	150.0	148.4	148.4	148.4	148.4	148.4
Public ($bn)	117.2	129.2	128.1	128.8	128.5	128.5	128.5	128.5	128.5
Private ($bn)	18.6	21.8	21.8	21.2	19.9	19.9	19.9	19.9	19.9
Foreign debt (% of GDP, end-year)	67.9	99.6	124.9	175.7	151.6	156.5	201.1	n.a.	n.a.
Central bank gross FX reserves ($bn)	22.1	16.4	11.0	9.5	9.2	7.5	6.3	6.0	6.5
Central bank gross non-gold FX reserves ($bn)	7.3	6.3	3.3	3.0	3.7	2.6	2.2	2.1	2.3

(1) Public and private sector wages. (2) Expressed in VEF through 2017 and VEB starting in 2018; 2014-2019 estimates represent a weighted average exchange rate across official and unofficial foreign exchange markets.

Source: Central Bank, IMF, INE, Ministry of Finance, PDVSA, the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

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