

Venezuela: The Chávez Government in 2002

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EXECUTIVE SUMMARY

Venezuela's President, Hugo Chávez Frías took office on February 3, 1999. A little over a year later he again tested the political waters and emerged from the elections held on 30 July 2000 with some 60 percent of the popular vote. Following contested changes to the national Constitution, President Chávez is now assured that his term will not expire until 2006, when he must sit out a term before being eligible to run for election again in 2013. Chávez is learning, however, that governing a country can be a difficult undertaking and he has seen his own personal grassroots support fall dramatically — his approval ratings stood at 55.8% in July 2001, but had fallen to 35.5% (Datanálisis) by year end.

He has been charged — by his increasingly vocal critics — of deliberately polarizing Venezuelan political life and being, at least implicitly, behind increased violence and intimidation directed at members of the political opposition. An avowed populist, Chávez has increasingly resorted to executive fiat to implement his policies and legislative program. Surrounding himself increasingly with military and ex-military figures, one cannot but escape the perception that the President is feeling somewhat isolated from his traditional base of political support and is possibly feeling somewhat threatened.

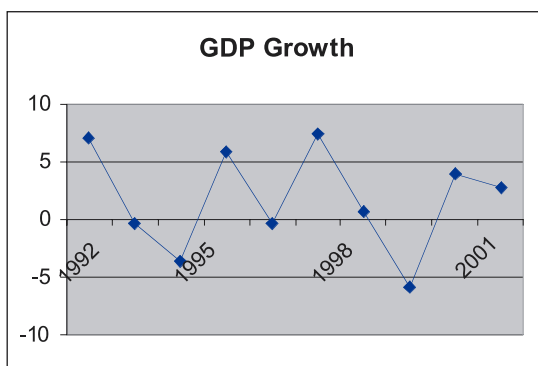
Externally, Venezuela under President Chávez has increasingly taken up stands that are seen by many observers as being in open opposition to the positions and sensibilities of the United States and other less powerful neighbours. While President Chávez denounced the September terrorist attacks on New York City and Washington, D.C. when he spoke before the United Nations Annual General Assembly, he decided to devote most of his speech to attacking what critics have called the neo-liberal Washington Consensus. He has publicly aligned himself with Cuban President Castro and has openly questioned the wisdom of Venezuela's participation in many of the Summit of the Americas initiatives — including the negotiation of a Free Trade Area of the Americas. In Venezuela's own backyard he has stirred up animosity with Colombia by his suspected support of guerrilla forces in that country, and has reopened the long dormant claim by Venezuela on territory controlled by Guyana.

A multiplicity of forces working in concert is almost guaranteed to promise that political, social and economic tensions will remain a fact of life for most Venezuelans. What is less clear is whether these forces could precipitate to a full blown political crisis in which President Chávez's departure from office could be as dramatic as his entry.



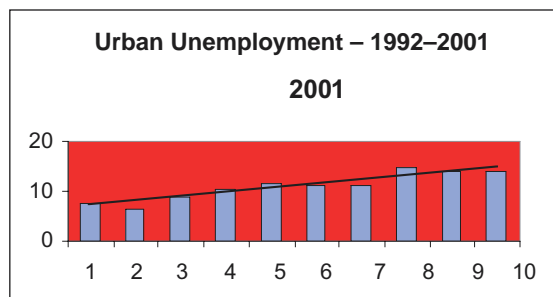
Revolutionary Speeches and Economic Realities

Venezuela's 24 million people have enjoyed little of the prosperity that many expected would accompany its enviable position as one of the world's largest producers of oil. It also has the world's third largest refining capacity. The petroleum sector dominates the economy, accounting for roughly a third of GDP, around 80% of export earnings, and more than half of government operating revenues. In 2001, the economy was moving toward an overall growth rate estimated at 3 percent, however, most of this growth was accounted for by the private sector as the influential state controlled oil sector (Petróleos de Venezuela S.A. or PDVSA) cut production in accordance with OPEC's attempt to stem the falling price of oil that had become evident at the end of 2000. In consequence of OPEC's policies — of which Venezuela is a strong supporter — export quotas were reduced by more than 400,000 barrels per day to some 2.67 million barrels. Despite these cutbacks, the average price of Venezuelan crude oil fell by around 20 percent compared to a year earlier. Venezuela, which sells approximately 55 percent of its oil production to the United States, has the largest proven oil reserves outside of the Middle East (some 77.7 billion barrels).



Economic development has thus been overly dependent upon this sector, which is in turn heavily influenced by international events and trends. Despite respectable economic growth in 2001, when Venezuela's Gross Domestic Product increased by 2.8 percent and a full 4 percent a year earlier, Venezuela's economic growth performance has tended to fluctuate wildly over the last ten years. Continuing softness in oil prices, combined with low growth globally — particularly in the United States — and its own internal political tensions will likely mean that Venezuela cannot expect growth in the current year to be much beyond 1.0 to 1.2 percent. The continuing crisis in Argentina is also likely to entice emerging market investors to shift funds to perceived safer harbours.

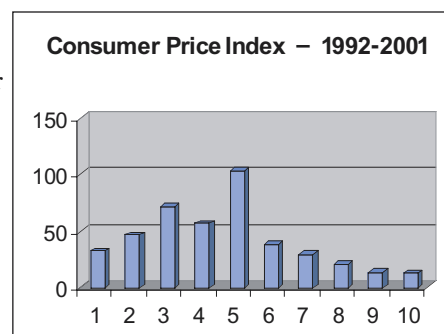
Compared to all of Latin America and the Caribbean which posted an average growth rate of 2.8 percent per year over the last ten years, Venezuela has only managed to post an average annual growth rate of 1.7 percent. As indicated, the lacklustre performance of the economy



has resulted in high levels of unemployment, particularly, in urban centres where most of Venezuela's population is concentrated. Urban unemployment has remained stagnant in the 14 percent range for the last three years — the period of time coinciding with the Chávez government. And while some improvements have been registered on the inflation front (the consumer price index peaked at 103 percent in 1996) year over year price increases have remained stuck at the 13 percent level for the last two years. The government's popularity has fallen consistent with the high unemployment rates that only alienate the urban poor and the continually rising prices that alienate the middle classes.

The government of President Chávez has sought to counter some of these trends, in particular by the creation of entities aimed at encouraging investment and streamlining approval procedures for new projects. In addition, new legislative instruments have been adopted with respect to the mining and electricity generating sectors and plans are underway to relax some of the prohibitive regulations governing development of the gas industry. Venezuela's Ambassador to the United States, Ignacio Arcaya, has been working to attract the interest of U.S. based oil companies and is a frequent visitor to the U.S. based oil industry in the southwest United States. That is, until Arcaya abruptly resigned for "family reasons" in January 2002, after apparently voicing his increasing concerns about the way in which Venezuela was being governed. Arcaya's resignation could make keeping the lines of communication to the U.S. government more difficult. A Venezuela-U.S. bilateral Tax Treaty has been in effect since January 2000, aimed at facilitating foreign investment. Venezuela has estimated that its substantial requirements in exploration, production and crude oil

production will be on the order of US\$26.5 billion over the period 2001–2005. Exxon-Mobil, the recently amalgamated oil giant, along with Sincor has received approval for a number of projects in the so-called Orinoco Oil Belt.



Venezuela has also more recently focused increased attention on the exploration and production of what are estimated to be vast reserves of natural gas. While North American markets are generally well supplied with natural gas, lower production and transportation charges from Venezuela could well mean additional opportunities for Venezuelan economic development in this sector. To encourage foreign participation, and to bring in badly needed technology and production know-how, Venezuela recently passed a new Gas Law that allows for foreign participation in exploration and production projects — at least six of which have already been approved. Venezuela has also put on line electricity transmission lines to valuable markets in northern Brazil and is in discussions aimed at interconnecting its gas pipelines with those of its neighbour Colombia. The first modernization of the Hydrocarbon Law, enacted in 1943 (the industry was nationalized in 1975) has been undertaken and among other things it provides for the following:



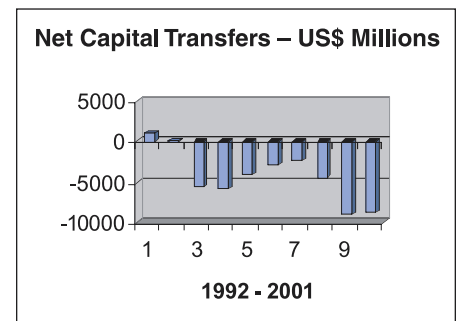
- For the first time since nationalization of the oil companies, it will allow U.S. companies — and any other private enterprises — to participate clearly and incontrovertibly in “primary activities;” that is, exploration, extraction, transport by special means, and storage of non-gaseous hydrocarbons. Private enterprises will be able to participate in primary activities as minority shareholders in mixed-capital (state-private) operating companies.
- For the first time since nationalization, domestic and foreign-private enterprises will be able clearly to participate in what the law defines as “industrial activities;” that is, distillation and purification of non-gaseous hydrocarbons. The transformation of derived products — for production of lubes, special oils, and petrochemicals — has been kept open to the private sector even after the nationalization law. Not only mixed-capital companies, but also fully private enterprises, will be allowed to take part in all of these businesses.
- Finally, for the first time since nationalization, the commercialization of certain products derived from natural hydrocarbons, directed to foreign markets, will be open to the private sector through both mixed capital companies and totally private companies. The domestic market for gasoline and other fuels was opened in 1998.

While President Chávez appears to be seeking greater foreign investment in the oil sector the populist side of him appears not to be able to resist persistent threats to nationalize the private banking sector. Such apparently contradictory approaches only serve to further heighten tensions in the commercial sector and to increase the sense of uncertainty prevailing in Venezuela today.

Venezuela’s financing needs are great; unfortunately, its options are limited at best. While Venezuela does not carry an overly large amount of foreign debt on its books, there are nevertheless some fairly widespread concerns about the government’s willingness to honour external obligations (heightened no doubt by the seesaw policies exhibited by Argentina) should the situation worsen. Thus, Moody’s rates Venezuelan sovereign debt at B2 — some five levels below investment grade. It is doubtful that

Venezuela would be able to raise even half a billion dollars on international markets should circumstances require. The chances that circumstances dictate the need for additional government funding are high. Every drop in the price of oil by one dollar results in a shortfall in government revenues of approximately some US\$750 million.

The most recent government forecasts a budget of US\$34 billion in 2002 based on the assumption of oil prices averaging \$18.50 a barrel — which is four dollars above what is likely. With his popularity already at worrisome levels, it is likely that President Chávez would resist further spending cuts and risk sending the poor and unemployed into the streets à la Buenos Aires.



The persistent trend of domestic capital leaving Venezuela is not something that can go unnoticed by foreign investors. In the last ten years — according to the United Nations Economic Commission for Latin America and the Caribbean (ECLAC) — it is estimated that in excess of some US\$40 billion has left the country in terms of net capital transfers. While Venezuela has always had difficulty holding on to its domestic capital — an entirely logical reaction given the country’s history of political and economic mismanagement — what is even more worrying has been the big jump in capital flight recorded since 1999 when President Chávez came into power. Capital flight more than doubled in 2000 (some US\$9 billion) over what had been, at least, stable levels previously. In 2001, the amount of money fleeing Venezuela dropped a bit but remained in the US\$8.8 billion range. This massive level of dis-investment — at a time when Venezuela is in desperate need of capital improvements, particularly in the critical oil sector — has left the country in a precarious position. As domestic capital flees, not only is it no longer available for productive investment but clear signals are sent to international markets which tend to respond by demanding a significant risk premium — leading to yet

higher domestic interest rates which make further capital investment economically difficult to justify.

Confrontation and political instability:

President Chávez is no stranger to situations in which his rule and leadership are under challenge. In some ways he appears to thrive in a context where political opinions are ever more polarized — a descriptive term that comes up frequently in the current political vocabulary of Venezuela. However, even President Chávez may have been surprised by the most recent



challenge to his regime; particularly since it came from within the movement (Movimiento Quinta República or MVR) founded by him and his Minister of Foreign Affairs, Luis Alfonso Dávila. Dávila, pictured left, is a former member of the military who rose to the rank of Colonel before

resigning his commission in 1990. The latest challenge comes in the form of the vote for the Presidency of the National Assembly. The official candidate in the MVR-dominated assembly, William Lara, garnered 85 votes in the 165 seat chamber (down from 120 votes in 2001) against the surprising candidacy — and strong showing — of MVR “rebel” Alberto Jordán Hernández who gathered the support of 73 votes.

The apparently widening split within the MVR is traced by many to the popular street protests mounted in December 2001, against what many had charged was an increasingly authoritarian governing style of President Chávez. Within the movement, some such as Interior Minister Luis Miquilena, who was forced to resign in mid-January 2002, were seen as favouring a more conciliatory approach to the widening opposition to Chávez's rule. Given that Miquilena was widely acknowledged to have played a mentoring role vis-à-vis Chávez in his earlier years, the split from within could be wider and deeper than is acknowledged publicly.

Miquilena — the former leader of the Venezuelan Communist Party — was replaced by retired Captain Ramón Rodríguez Chacín — the former director of the secret police. As Andrés Oppenheimer — the widely read columnist of the *Miami Herald* recently proclaimed — the funny thing about Venezuela is that it appears to have an elected military government.

If moderates exist — and they apparently do — then they are facing off against what are known as the hardliners. This is the section of the MVR that urges the

government to consolidate and deepen the Bolivarian Revolution that Chávez claims to have launched. Chávez's decision to stand firm in the face of growing domestic and international opposition is taken as a sign that the hardliners are on the rise from within. Chávez can be consoled, however, by the knowledge that the traditional political parties in Venezuela remain distinctly unpopular with the populace who — not without some significant justification — associate the traditional political elite with massive levels of corruption and political ineptitude.

For the time being, President Chávez can still — apparently — count on support from the country's armed forces, many of whose former members dominate the top cabinet and other executive positions of government. To many, the loyalty of the armed forces appears to be genuine in the sense that recent financial figures do not indicate a massive reallocation of government resources in their direction since Chávez came to power. The military's budget is just over US\$930 million and represents just 0.9 percent of GDP (compared to Canada's 1.3%) or about 3.7 percent of total government spending.

On the other hand, loyalty from the military may not be so hard to understand given their significance in numbers and key positions within the structure of government. The Vice President, Diosdado Cabello, is a former Lt. Col.; the Vice Minister of Foreign Affairs, Arévalo Méndez, is a serving General. Retired military officers are also currently serving as the heads of the state owned oil company (PDVSA), as well as the national telecommunications company (Conatel). Chávez has always called his revolution a civilian-military one. Patria Para Todos (PPT) ex-party leader, Pablo Medina, once stated it was more like a military-civilian alliance — which is a very different matter.



Venezuelans disenchanted with their government have to struggle with yet another peculiarity of Venezuelan political life. And that is the traditional importance placed on personal leadership or the intent to build political parties around individual leaders. Recent historical examples are found in the persons of former

presidents Carlos Andrés Pérez and Rafael Caldera and current President Hugo Chávez. When trust in institutions has evaporated, individual voters have a tendency to transfer their hopes and aspirations to individual political leaders. The leader becomes *the* electoral movement but only after the fact is it discovered that they are incapable of playing the role a political party habitually plays as assimilator of the interests and needs of broad sectors of society and equally important as a critical channel of communications between society and the institutions of the State.

Friction with the United States:

Venezuelan foreign policy under President Chávez appears to take particular pride in its — possibly temporary — ability or willingness to thumb its nose at the United States. That Chávez holds a particular enmity against the U.S. is clear — his speeches, at the United Nations and elsewhere, leave little doubt about that — but what puzzles many observers is the apparent silence to the simple question: to what end? The following are the main points of confrontation between the Chávez government and the United States:

- the initial opposition to Plan Colombia and the declaration of its neutral stance on the Colombian guerrilla issue;
- the refusal to allow U.S. military planes over-flight clearance in Venezuelan territory;
- the rapprochement with the Cuban government;
- the rapprochement with countries for which the U.S. — rightly or wrongly — has longstanding problems such as Libya, Iran, Algeria and Iraq;
- the rejection of Washington's offer to assist in the disaster caused by the mudslides in Vargas state;



- ejection of the U.S. military liaison unit from Venezuela's military headquarters complex on the perimeter of Caracas on the eve of Castro's birthday visit in 2001.

Even the instruments of diplomacy have not gone unscathed in the building friction between Venezuela and the U.S. President Chávez has — for all intents and

purposes — fired his own Ambassador to Washington, while at the same time had the U.S. Ambassador to Venezuela Donna J. Hrinak called into the Venezuelan Foreign Ministry to explain some public remarks that Ambassador Hrinak had apparently made vis-à-vis Venezuela's attitude toward the U.S.-led war on terrorism in Afghanistan.

To date, the U.S. has — for the most part — failed to strike at the bait, if that is what President Chávez is indeed offering. In largely ignoring President Chávez, the U.S. is perhaps hoping that he will simply quieten down or — as is more likely — simply be ignored by fellow leaders in the region. Colombia's leadership is already cool to their neighbour and Chávez has proven incapable of attracting other Latin American leaders to whatever band he believes he is leading. The U.S. absorbs a good deal of Venezuela's oil exports but does not feel any particular need to extend that relationship — for the moment — to anything beyond a simple commercial exchange.

Conclusions:

Social, political and economic tensions are likely to continue to build in Venezuela during the course of the next year. Economic growth will remain far below the level necessary to make significant inroads in the reduction of poverty or the stabilization of economic conditions. Inflation and interest rates will continue to hover in the low teens and high thirties respectively, and more money will leave than will come into the country. The middle classes — already apprehensive about their future place in Venezuelan society — will continue to measure each speech and gesture of their President and will find him wanting on most counts. The military are unlikely to be provoked into any sort of action — beyond the accommodation currently being practiced — unless the potential spark of civil unrest gives rise to yet another, and probably currently unknown, populist saviour figure around whom Venezuelans can temporarily rally.

The personal popularity of the President will continue its downward path, arresting only when it reaches the core of his most fervent supporters. That level — historical antecedent tells us — is probably around a fifth to a quarter of the population. Support by a fifth or a quarter of a population is enough of a foundation on which to build larger coalitions of political support. But only if the foundation is not infected with the sort of ideological rigidity that President Chávez has demonstrated to date. Could he turn his numbers — as political pundits are prone to characterize them — around? Possibly yes, but beyond populism Chávez has demonstrated remarkably few political skills.

So what should others do in such circumstances?

For a start, countries in the Western Hemisphere in particular need to maintain close observation of developments inside Venezuela. A marginal increase — possibly temporary — in diplomatic staff assigned to Latin American, U.S., Canadian and European embassies in Caracas could send a signal to the Chávez government that others are watching developments closely. Relations and linkages to disaffected sectors of Venezuelan society should not be neglected for that is where the trouble — if it comes — will start.

Second, support and direct assistance could be extended, especially by foundations and philanthropic organizations, to Venezuela's increasingly beleaguered independent media. The media (along with the Church) has, to date, played a critical role in holding the government accountable and in focusing the spotlight of public attention to its actions. Foreign news organizations — especially those based in the Western Hemisphere — should consider increasing their coverage of Venezuelan

related developments. Enhanced coverage, which would undoubtedly meet editorial requirements for news gathering, would better inform a non-Venezuelan audience of developments.

Third, the leadership of Western Hemisphere based multilateral institutions — such as the Organization of American States and the Inter-American Development Bank — should ratchet up their engagement with Venezuela's leadership. Strong messages in support of democratic institutions and processes should leave the Venezuelan leadership with no illusions as to the potential political and economic costs of any deviation from the path of constitutional democracy. The strong role played by certain key individuals, such as the OAS Secretary General, César Gaviria, in resolving the recent crisis in Peru provides the necessary mandate and justification for engagement vis-à-vis Venezuela.

And we can wait and see.

RÉSUMÉ

Le président du Venezuela, Hugo Chávez Frías, a débuté son premier mandat présidentiel le 3 février 1999. Un peu plus d'un an après, il mesura sa popularité une seconde fois le 30 juillet 2000 en remportant plus de 60 % du suffrage exprimé. Après avoir apporté des modifications contestées à la Constitution nationale, le président Chávez est maintenant assuré de conserver son mandat jusqu'en 2006; ne pouvant se représenter immédiatement à la fin de ce mandat, il devra s'armer de patience et attendre les élections en 2013 pour être éligible à nouveau. Cependant, Chávez doit réaliser que l'art de gouverner n'est pas chose facile car sa cote de popularité auprès des Vénézuéliens est en chute libre. Si en juillet 2001, il bénéficiait de l'appui de 55,8 % de la population, ce chiffre n'était plus que de 35,5 % (Datanálisis) à la fin de l'année.

De plus en plus virulents, ses critiques l'accusent de polariser délibérément la scène politique du Venezuela et d'être implicitement un partisan de la campagne de violence et d'intimidation dont sont victimes les membres de l'opposition. Populiste avoué, Chávez tend maintenant à prendre des décisions arbitraires pour mettre en œuvre ses politiques et son programme législatif. En s'entourant davantage de militaires et d'ex-militaires, il semble s'isoler quelque peu de sa base traditionnelle de partisans politiques et doit, d'une certaine façon, se sentir menacé.

Selon de nombreux observateurs, en matière de politique extérieure, le Venezuela du gouvernement Chávez a souvent pris des positions allant à l'encontre des intérêts américains ainsi que de ses voisins hémisphériques. Bien que le président Chávez ait condamné les attaques terroristes du 11 septembre à New York et Washington, D.C., il a néanmoins, lors de son discours à l'Assemblée générale annuelle des Nations Unies, consacré la plus grande partie de son discours à attaquer ce que les critiques ont appelé la politique néo-libérale du « *Washington Consensus* ». Il s'est rangé publiquement du côté du président cubain, Fidel Castro, et a ouvertement remis en question la pertinence de la participation du Venezuela à plusieurs initiatives du Sommet des Amériques, notamment les négociations pour une Zone de libre-échange des Amériques. Il a également soulevé l'ire de la Colombie qui le soupçonne de supporter les forces de la guérilla dans ce pays. De plus, il a relancé une vieille dispute frontalière en contestant une partie de l'intégralité territoriale de la Guyana.

La concertation accrue des multiples forces politiques en présence garantit que les tensions politiques, sociales et économiques resteront très présentes dans la vie quotidienne des Vénézuéliens. Ce qui demeure incertain est de savoir si ces forces politiques réussiront à déclencher une crise politique capable de précipiter la chute de Chávez avec le même éclat dramatique que lors de son ascension politique.

RESUMEN

El Presidente venezolano, Hugo Chávez Frías, asumió la dirección del país el 3 de febrero de 1999. Luego de poco más de un año, Chávez probó suerte nuevamente y logró imponerse con alrededor del 60% del voto popular en las elecciones celebradas el 30 de julio de 2000. Tras polémicos cambios constitucionales, Chávez ha asegurado su permanencia en el poder hasta 2006, fecha en la que deberá dejar la presidencia por el término de un período de mandato antes de poder aspirar al puesto otra vez en 2013. No obstante, Chávez está empezando a comprender que gobernar un país puede ser una tarea difícil, al tiempo que su apoyo popular desciende a niveles inquietantes. En julio de 2001 el Presidente contaba con un 55% de aprobación, sin embargo a finales de año ese apoyo había descendido al 35.5% (Datanálisis).

Sus detractores lo acusan de polarizar la vida política de la nación de manera deliberada y de estar, implícitamente al menos, detrás del auge de violencia e intimidación que se comete contra la oposición política. Chávez es un declarado populista que recurre cada vez más a su autoridad ejecutiva para implementar sus políticas y programa legislativo. Asimismo, el creciente número de militares tanto en activo como retirados con que se rodea nos hace pensar que el Presidente se siente un poco aislado de su base tradicional de apoyo y que quizás se está sintiendo algo amenazado.

En el terreno internacional la Venezuela de Chávez ha adoptado posturas que para muchos observadores están en clara confrontación con las posiciones y sensibilidades de los Estados Unidos y de otros vecinos menos poderosos. A pesar de que el Presidente Chávez denunció los ataques terroristas contra Nueva York y Washington D.C. el pasado septiembre, decidió dedicar la mayor parte de su discurso ante la Asamblea General de las Naciones Unidas para arremeter contra lo que los críticos llaman la política neoliberal de *Washington Consensus*. Chávez también se ha alineado públicamente con el presidente cubano Fidel Castro, y abiertamente ha puesto en tela de juicio la pertinencia de la participación de Venezuela en muchas de las iniciativas de la Cumbre de las Américas entre las que se encuentra la negociación del Área de Libre Comercio para las Américas. Incluso en su propio traspatio, Chávez ha avivado discrepancias con Colombia debido a sospechas sobre su apoyo a las fuerzas guerrilleras de ese país. Igualmente, ha resucitado una vieja reclamación de Venezuela sobre territorios que están bajo el control de Guyana.

La confluencia de numerosos factores seguramente hará que las tensiones políticas, sociales y económicas sean una realidad inevitable en la vida de la mayoría de los venezolanos. Lo que no está muy claro es si esos factores podrán provocar una total crisis política en la que la caída del Presidente Chávez sea tan dramática como lo fue su ascenso.

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