Is the Venezuelan Economy Stabilizing or Is the Worst Still to Come?

Venezuelan portal 15yÚltimo's latest editorial discusses the current economic reality and what may lie ahead.

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Lots of readers have asked us via social media what we think are the reasons that led the government and the Central Bank (BCV) to publish, all of a sudden, indicators that, also suddenly, stopped being published over three years ago.

Some conjured their own theses amidst the questions: that it might be part of the Oslo negotiations [with the opposition], or that a deal with the International Monetary Fund (IMF) was on the way. These two were the most common. Others wondered if the Chinese or Russians had pressured the government to do so.

Also among readers' concerns, but more pressing, was the issue of hyperinflation, whether the fact that the rise in consumer prices in March and April being below 50 percent meant we were out of the woods, whether it was good news, in the sense that the worst had passed and the economy was stabilizing.

Here are our thoughts on the matter:

On both matters, first of all, we need to point out that we cannot do what would be the first order of business in these cases. This would be to take into account the official explanations. However, this is not possible for the simple reason that there is no official version of the facts.

On what concerns the publication of economic indicators there has been no official comment, just like nothing was said when they disappeared. In that sense, what is produced is a vacuum where speculative theories prosper, either those who always look to make the government look bad or those who look to absolve it.

The same thing applies to inflation. But here the matter is more serious. The issue is that, according to the BCV, the National Index of Consumer Prices was at 34 and 33 percent in March and April, respectively (and May will surely be similar), after registering at 196 percent in January and 114 percent in February. Based on that, we would expect a party and an economic cabinet bursting with pride at their achievement: nothing less than putting an end to 15 months of hyperinflation. However, that's not what we're seeing. The attitude on the matter is one of complete silence, which mirrors what we saw when hyperinflation was rampant.

We know that communications is not, and has never been, the government's strong suit.

But in these cases we believe the silence has to do with other factors besides this deficiency.

Regarding the BCV indicators we don't believe, in the short term, that there is an agreement with the IMF in the works. Given the recent tendency in economic policy, nothing surprises us any more, but a deal with the IMF would seem a bit extreme. With the blockade and everything there are other multilateral bodies (for example under the umbrella of the United Nations) which could offer credit and "technical assistance" in economic matters, like we already see in other areas. Furthermore, there are also private entities, which due to the blockade would not come from this side of the world, but from China or Russia, which could offer new loans in the framework of the "strategic alliances" which the government is clearly very keen on.

What we mean is that what's usually associated with the IMF can be done by others, with a smaller political cost and reputational damage. They can even be presented as an alternative to the IMF in the framework of a multi-polar world, etc.

But however it turns out, whether the goal is to go to the IMF or another body, the truth is that the government's reorientation towards orthodox economics explains the publication of the indicators. It is quite clear that the image being presented is that of an economy that is normalizing or stabilizing, embracing the principles and guidelines of a "normal" economy. In other words, an open economy, with no major controls or "populist" regulations from the government, with ample assurances to national and international private investors, where instead of communards we have entrepreneurs, etc.

Now, if that's the case, and moving on to the second issue, why is the government not doing cartwheels after managing to slow down inflation, to the point where technically we are no longer in hyperinflation?

On this issue we think that, after everything that's happened, the government is conscious of the fragility of this modest achievement, in the sense that slowing down the rhythm of price increases doesn't mean doing away with its causes, which at this stage are quite a few and remain simmering.

Apart from that, and this is essential, we believe that the decision to not mention the subject has also to do with an awareness that the cost of the anti-inflation policies is very high and especially very unequally shared, in the sense that, basically, it is born by workers and medium to low income groups.

This is something we've been stressing: the essence of the anti-inflationary policies consists in shrinking people's purchasing power as much as possible, so that they won't buy dollars in the black market, – those who could afford it – thus stabilizing the exchange rate. But more than that, the goal is that people, in general, buy less of everything so that there's less pressure on prices to go up.

Let's be clear that no matter how efficient the political marketing is, this is something very hard to sell, especially for a government that defines itself in the tradition of Chavismo and the left.

That's why at the time we said that the three economic policy targets published by the BCV in late January [when it massively devalued the exchange rate and restricted Bolivars in circulation], together, represented a trilemma. The targets were: stabilizing the exchange rate, slowing down hyperinflation, and restoring purchasing power. We argued at the time that with the methods chosen it would be possible, in the best of cases, to achieve the first two but not the third, since the success of the first two depended on sacrificing the third. Time has proven us right.

In addition, it is also evident that the strategy to stabilize the exchange rate involves reducing the pressure on it, and insofar as the government doesn't have foreign currency to offer and the private sector actors that do refuse to do so, the lowering of pressure on the exchange rate can only be done by further raising it. In other words, devaluing the Bolivar (BsS), which is then reflected in prices. Therefore, in a strict sense, the rising tendency of the exchange rate is not eliminated but displaced.

In the framework of the new foreign exchange system run by the banks, which has been in place for a month now, the exchange rate has now gone over 6,000 BsS per dollar, some 800 more than when the system was set up, and with a rising tendency that will continue. It is worth pointing out that since [the monetary reconversion in] August, the exchange rate has devalued by more than 9,950 percent, which means the sovereign Bolivar has devalued with respect to the US dollar by more than 99%.

But what's most complicated about this issue is that an anti-inflationary strategy that relies on constricting monetary flows to reduce consumption has the added effect of contracting the economy even more. As a result, and as paradoxical as it may sound, the economic policy ends up joining forces with the blockade and amplifying the terrible effects it has on the economy and the country in general.

An anti-inflationary economic policy such as the one chosen by the government has contracting effects by itself, even in normal conditions. A good example of this can be seen in Argentina, where a monetarist economic policy with many similarities to the one seen in Venezuela has sunk the country in a three-year recession, on the heels of a period of growth under the government of Cristina Fernández. But in Venezuelan conditions the effects are much worse, if that's even possible by now. According to the very BCV, the country has seen six consecutive years of GDP contraction, which totalled 52 percent up until the third trimester of 2018. This means, in simple terms, that presently the economy is half as big as it was in 2012 and about the size of the one in 1999. Nothing suggests – quite the contrary – that the results of the missing trimester and of 2019 will buck the trend. Add to that that the effects of recent sanctions will start being felt in the second semester that we're entering, and the prospects are not good. All of this without even mentioning the electricity crisis, with a situation that is much more dire outside Caracas.

To summarize: in economics, as in many other things, one cannot exactly predict what's going to happen, only what's likely to happen if things continue as they are and nothing suggests otherwise, which is that far from a stabilization we're entering a very dangerous phase of contraction. We have to be very wary of mirages and of ending up eating more sand where it looked like there was water.

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