

Venezuelans chase dollars amid economy worries

At the moment, Venezuela's economy is booming, but there are signs of future trouble. Oil production is falling; inflation is running at 19 percent. Many Venezuelans are building up supplies of U.S. dollars to protect themselves.

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CARACAS --

Like many people they know in Caracas these days, Alfred and Norma Muñoz are bracing for what they believe is inevitable: a currency crash brought about by President Hugo Chávez's policies.

The middle-class couple plan to borrow as much as they can from a local bank and buy an apartment outside the country. If Venezuela's bolívar plunges against the dollar, they figure, the loan will be cheap to pay off in dollar terms, and the overseas apartment will hold its dollar value. "Plus, it gives you somewhere to flee if things really get bad," says Muñoz, who runs a small business.

At the moment, with oil at near record prices, Venezuela's economy is booming. The fourth-largest oil exporter to the United States has averaged 12.6 percent annual growth since 2004 -- the fastest in Latin America. Three-month waits to buy new cars are standard at Caracas dealerships amid a boom in consumer financing. Unemployment has fallen to single-digit rates for the first time in more than a decade.

CONCERNS AHEAD

But there are signs of trouble. Oil production is falling as the state oil company loses top managers and invests less. Inflation is running at 19 percent, according to the Venezuelan government, though many private economists say the rate is more like 25 percent, given the increasing role of a black market in hard-to-obtain goods. Partly as a result, the bolívar, officially fixed at 2,150 per dollar, has lost more than half its value on the black market.

The global credit squeeze caused by mortgage problems in the United States may give Venezuelans new reasons to worry. That's because oil prices could fall if, as some economists fear, a world slowdown in lending leads to a broad economic slump. Declining oil prices would deprive Chávez of income for his vast social programs and accelerate pressure on the bolívar.

In decades past, currency declines and hyperinflation have reared up across Latin America, destabilizing governments and spreading misery among ordinary people. Indeed, Chávez's own rise to power was helped by a financial collapse and soaring

inflation under the mid-1990s government of Rafael Caldera, which prompted exasperated voters to back Chávez in a 1998 election. If such problems emerge again in Venezuela, they could erode Chávez's popularity at home, as well as curtail his influence in the region by forcing him to cut back on foreign aid.

While the bolívar is weakening, many other oil nations are watching their currencies get stronger. The explanation for the discrepancy lies, at least in part, in Chávez's economic policies. His attempt to manage the economy for the benefit of the poor has produced unforeseen problems, which he has treated with unorthodox solutions that in turn have created new problems. With each policy turn, people like the Muñozes have become more convinced things will spin out of control.

Since 2003, Chávez has more than doubled government spending on free medical care, higher salaries, gasoline subsidies and other services. That created more demand for goods and services, which fueled inflation. Chávez then expanded price controls, which now cover meat, sugar, eggs, milk and other products. That led to food shortages as producers balked at selling their goods at the mandated prices. The shortages produced a black market, where prices have soared.

A FAMILIAR SCENE

This mixture of food shortages, black markets and rising inflation is déjà vu for the Venezuelans who have lived through three financial meltdowns since the 1980s. To protect themselves from a repeat, Venezuelans are trying to get their hands on dollars, further weakening the bolívar.

"We all know what is coming, we just don't know when," says David Macedo, who drives a delivery truck that supplies small grocery stores. When he has a few bolívares saved, he says, he often goes to the Caracas airport to buy dollars from arriving tourists. He pays far more than the official rate of 2,150 bolívares per dollar, but less than the black-market rate, now about 4,800.

Wealthier Venezuelans use credit cards to exploit the difference between official and black-market currency rates. Some have flown to the nearby island of Aruba and bought \$5,000 worth of gambling chips, the maximum overseas credit purchase allowed by the Venezuelan government, according to a person who arranges the trips. They cash in the chips for dollars, then, back at home, buy enough bolívares on the black market to pay the credit card, this person says.

Chávez came to power promising to use the country's oil wealth to benefit the poor. His economic problems started after a 2002 coup attempt and an oil workers' strike. The ensuing economic turmoil prompted many Venezuelans to take money out of the country, which threatened to bring down the banking system. Chávez stopped the capital flight by banning overseas money transfers and dollar purchases.

When oil prices rose, Chávez sharply increased spending, which helped him win crucial votes in 2004 and 2006. But the capital controls trapped new spending inside Venezuela, more than quadrupling the amount of bolívares in circulation. The bloated money supply undermined the bolívar and fueled inflation.

GOVERNMENT TO ACT

The Chávez government realizes the dangers and vows to tamp down inflation before it gets out of control. In July, it required banks to pay customers higher interest on deposits, in hopes of making the bolívar more attractive and encouraging savings. The new rate is only about half the inflation rate. Finance Minister Rodrigo Cabezas says the government will moderate spending for the first time in years and will keep the official exchange rate unchanged at least through 2009. "We have no plans for devaluation," he says.

Few economists who follow Venezuela are forecasting deep financial trouble soon, at least while oil prices remain high. But the longer-term prognosis is far from clear. Mark Weisbrot, co-director of the Center for Economic and Policy Research, a Washington think tank, who is generally supportive of Chávez, says the government has time to boost economic growth by investing in industries outside the oil sector. Other economists are more skeptical. They contend that the government isn't making enough long-term investments, such as building factories, and that it remains far too dependent on oil revenue.

"We don't know when a crash will happen," says Alberto Ramos, a senior Latin America economist at Goldman Sachs. "But Chávez is driving down the wrong side of the road."