

Venezuela

Some of Venezuela's comparative advantages are widely acknowledged; among them, its privileged geographical location granting easy air, sea, and land access to international markets, along with its enormous tourism potentiality.

CONAPRI¹

Introduction

- 10.1 Venezuela was a Spanish colony from 1499 to 1821. A federation of Gran Colombia was formed that included the countries that had fought together under Simón Bolívar to defeat the Spanish. This federation comprising Venezuela, Colombia, Ecuador and Panama did not last long. Panama was annexed in 1821 and Ecuador and Venezuela seceded in 1830 to form independent countries.
- 10.2 Venezuela's political system has traditionally been one of the most stable and democratic in Latin America and since 1958, following the overthrow of a military dictatorship, presidential elections have been held every 5 years.
- 10.3 During the late 1980s through the early 1990s Venezuela's economy was in serious trouble that included a series of banking collapses throughout 1994 and 1995 exacerbated by high inflation and declining international reserves. The state of the economy brought about social and political instability.
- 10.4 In April 1996 the then President, Rafael Caldera, introduced *Agenda Venezuela* a macroeconomic stabilisation plan and structural adjustment

1 CONAPRI website <http://www.conapri.org> - *Venezuela Now Magazine*, 4th. Edition, 'Opinion: A Promising Future'.

program. Economic recovery dominated politics up until the 1998 elections and 1998 saw a severe and sustained decline in oil prices that drastically reduced export earnings and government revenue.

- 10.5 The 1998 presidential election saw the vote – some 80 per cent - dominated by two ‘independent’ candidates who campaigned for new parties at the cost of the traditional political parties. President Hugo Chávez Frias won a huge victory based on an electoral platform that promised a clean up of the political system and in combination with economic reform would lead to an improvement in the welfare of ordinary Venezuelans. His first year in office, 1999, saw major changes on the political front.
- 10.6 In April 1999 a referendum was held to vote for a new national assembly. July 1999 saw the election of the interim National Constituency Assembly and on 15 December 1999 the new Constitution, drafted by the assembly, was approved.
- 10.7 Under the new Constitution there are 5 power branches, the executive, legislative, judicial, electoral and moral branches. This last entity includes the ombudsman. The Constitution gives equal treatment to domestic and international investors and the term of the president has been extended to 6 years from 5 years with a re election clause.
- 10.8 Mega-elections under the new Constitution approved in December 1999 were to have taken place on 28 May 2000 but were postponed to 30 July 2000. President Chávez was re-elected comfortably.

Overview of the Economy

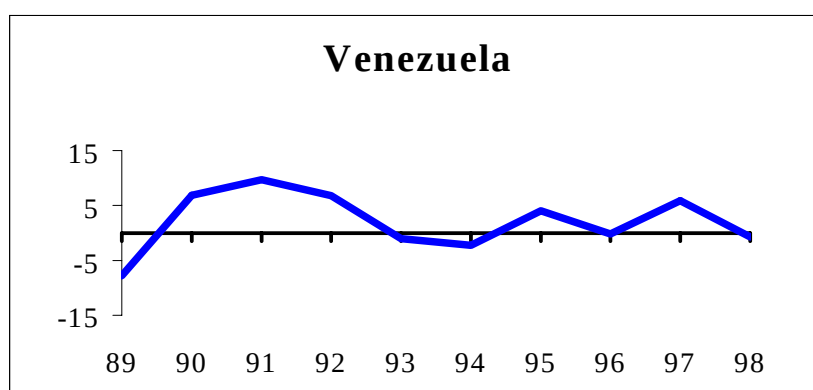
- 10.9 The Venezuelan economy is oil dependent. Commercial oil production began in the 1920s and has determined the performance of Venezuela’s economy ever since. The oil industry accounts for over a quarter of GDP, over 80 per cent of export earnings and half of government revenue.² The challenge for Venezuela is economic reform and diversification with the need to reduce its dependence on oil.
- 10.10 The size and importance of oil to the Venezuelan economy is clearly evident in how the industry is structured. The government controls the production of oil through the state-owned company PDVSA (Petroleos de Venezuela, S.A.). Incorporated in 1975 it was the vehicle through which the government appropriated all assets and operations of foreign oil companies in Venezuela in 1976. Since then PDVSA has evolved into one of the largest oil companies in the world, with investments and operations

2 DFAT, Submission, p. 301.

in Venezuela, North America,³ the Caribbean and Europe. It directly employs some 48,000 people and with assets in excess of US\$48 billion and revenues of US\$25 billion in 1998 it is by far the largest company in the Andean Pact and the Caribbean region. PDVSA's core interests besides oil includes gas, petrochemicals and Orimulsion® fuels.

- 10.11 Venezuela has a population of 23.4 million with GDP per capita of US\$4,054. Its CPI (annual per cent change) has fallen significantly from 99.9 per cent in 1996 to 35.8 per cent in 1998.⁴ CONAPRI forecasts an inflation rate (CPI per cent, year-end) of 17 per cent for 1999-2000, down from 19.0 per cent in 1999 and 29.9 per cent in 1998, the first time according to CONAPRI that the inflation rate has been less than 30 per cent in the last 30 years.⁵ The GDP trend growth for the period 1993 to 1998 was 1.7 per cent. Real GDP growth in 1997 was 5.9 per cent and it was 0.7 per cent in 1998 that represented a swing of 6.6 per cent. Figure 10.1 shows real GDP growth for the period 1989 to 1998.

Figure 10.1 Real GDP Growth – 1989-1998



Source *Australia's Trade with the Americas, 1993-94 & 1998, Department of Foreign Affairs and Trade, Canberra.*

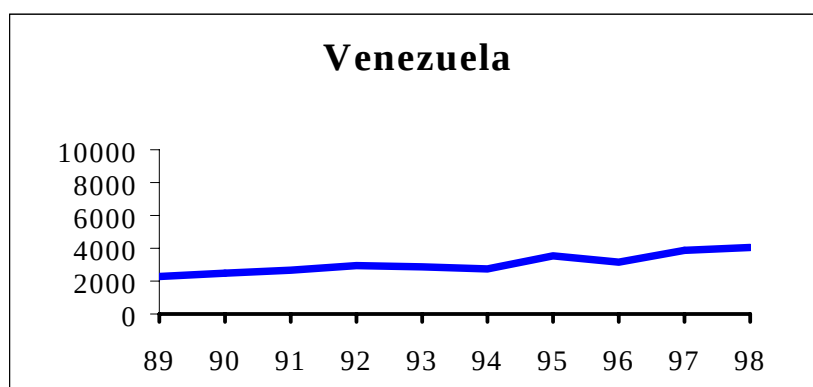
- 10.12 As DFAT notes the precarious nature of Venezuela's 'recovery' in 1997 was exposed with the strong growth not resulting from increased efficiency and production but from a strong oil market.⁶ In 1998 Venezuela had a current account deficit of US\$1.7 billion and in 1999 a surplus of US\$1.5 billion. GDP per capita over a ten-year period, 1989 to 1998 is shown in Figure 10.2.

3 PDVSA runs the Sidco (petrol stations) outlets in the US.

4 DFAT, *Australia's Trade with the Americas, 1998*, Commonwealth of Australia, 1999.

5 CONAPRI is the Venezuelan Investment Promotion Agency. Established in 1990, CONAPRI is a non-governmental organisation sponsored by the private sector and some government entities. Its task is the promotion of investment in Venezuela with special emphasis on attracting foreign capital. See CONAPRI website <http://www.conapri.org>

6 DFAT, Country Brief.

Figure 10.2 GDP Per Capita – 1989-1998

Source *Australia's Trade with the Americas, 1998, Department of Foreign Affairs and Trade, Canberra and IMF/IFS and EIU Country Reports.*

- 10.13 The Venezuelan economy experienced a particularly difficult year in 1998 as a result of a severe and sustained decline in oil prices that drastically reduced export earnings and government revenue. However the economy did display some positives and these were evident in the banking and construction sectors.
- 10.14 The factors of low oil prices and the political uncertainty surrounding the 1998 elections impacted on the Venezuelan economy. The recession through 1999 saw the economy contract by 7.2 percent despite a surge in oil prices in the second half of the year (from US\$7 per barrel to US\$25 per barrel).⁷ Unemployment levels rose to over 20 per cent, foreign and domestic investment stagnated and economic activity was paralysed. The exchange rate continued to be overvalued by an estimated 40 to 50 per cent making it extremely difficult for the non-oil sector to compete with imported products and for exporters to compete in international markets.⁸
- 10.15 The most positive aspect of the Venezuelan economy, according to DFAT, has been the decrease in inflation with the very weak demand due to the recession having a strong influence on the annual inflation rate of 19 per cent for 1999. Other positives include high levels of international reserves, a strong current account surplus and a government managed reduction to the fiscal deficit of around 3.1 per cent in 1999.⁹
- 10.16 The Venezuelan government's macro-economic goals for this year – 2000 – are:¹⁰

7 *ibid.*

8 *ibid.*

9 *ibid.*

10 Source, CONAPRI.

- Estimated inflation rate 15-17%
- GDP growth 2.2%
- Reduction of unemployment 2% (the official rate is around 15%)
- International reserves, year-end US\$16bn
- Fiscal deficit 1.5 – 2%
- Average foreign exchange rate Bs¹¹ 697 : US\$1

10.17 The government is aware that economic reform is necessary with policies that will stimulate growth and employment and diversify the economy. CONAPRI advised the Trade Sub-Committee when it was in Caracas that there had been a number of new economic announcements that will impact positively on Venezuela's economic environment, namely:

- VAT reduction from 15.5% to 14.5%.
- Suppression of the Financial Transactions Tax, effective May 15. Immediately for stock market transactions [removal of the 0.5 per cent tax on stock market transactions].
- Continuity of exchange and monetary policies.
- Minimum salary increase of 10% to US\$197 / month.
- Special plan for fiscal incentives for promoting exports and new employment;
 - ⇒ Income tax exoneration;
 - ⇒ Value added tax exoneration.
- Governmental purchases policy to benefit local content suppliers and integrators.
- Overhaul of industrial parks.

10.18 The taxation breaks in strategic sectors aimed at boosting employment include 80 per cent for farmers, 70 per cent in tourism and 10 per cent relief for construction, telecommunications and technology projects. In the agriculture sector the target is to increase land under cultivation by up to 50 per cent by the end of 2000, creating 10,000 jobs and reducing the dependency on imported food.¹² With the overvalued *bolivar* this may be difficult to achieve.

10.19 Increased foreign investment is critical to Venezuela. Without such investment Venezuela will find it very difficult to diversify its economy and to address domestic social issues. There is a need to bring certainty to investment law.

11 Currency is the *bolivar*. CONAPRI point out that the *bolivar* is strongly overvalued against the US dollar.

12 DFAT, Country Brief.

The Nature of the Trade and Investment Relationship

- 10.20 The Australian–Venezuelan bilateral relationship has been relatively dormant until recently. In June 1996 the then Deputy Prime Minister and Minister for Trade, the Hon Tim Fischer, MP visited Caracas and as a result a number of key areas for development were identified including the mining, agriculture and maritime sectors. This was followed by an embassy-sponsored business round table on trade and investment opportunities in Venezuela that DFAT says has further sensitised both sides to the possibilities of increased commercial cooperation.¹³
- 10.21 Bilateral trade has been fairly modest and this is reflected in the balance of trade figures. The balance of trade is very much in Australia's favour. Venezuela as a country was ranked 106th in 1999 on the value of merchandise trade with Australia totalling \$17.2 million. This placed Venezuela 6th on the list of South American countries behind Brazil, Chile, Argentina, Peru and Colombia. On 1999 figures Venezuela as a destination for Australia's merchandise exports is ranked 92nd with exports totalling \$15.6 million. This is an increase of 3.4 per cent over the 1998 figure. The trend from 1994 to 1999 shows a 9.0 per cent growth.
- 10.22 As a source of merchandise imports Venezuela ranks 111th with imports into Australia totalling only \$1.6 million in 1999. This figure represents a 6.4 per cent decline over the previous year and a decline in the trend of 8.4 per cent over the period 1994 to 1999.
- 10.23 Major Australian exports to Venezuela in 1998 (latest available figures) were mechanical handling equipment - \$2.90 million; pigments, paint and varnishes - \$1.86 million; confidential items - \$1.27 million and agricultural machinery (excluding tractors) - \$1.24 million. Interestingly the next principal export was medicaments (including veterinary) that totalled \$1.04 million.
- 10.24 On the import front, the principal imports from Venezuela in 1998 were alcoholic beverages - \$417,000; oil seeds and oleaginous fruits 'soft' - \$372,000; refined petroleum - \$337,000 and aluminium - \$198,000.
- 10.25 The US dominates trade with Venezuela. It is Venezuela's leading import supplier accounting for 45 per cent of imports (1997). Colombia comes in 2nd place as a supplier with a mere 6 per cent of total imports, followed by Brazil and Mexico both on 5 per cent. Australia was ranked in 52nd spot on the import suppliers' list. As Venezuela's leading export market the US receives 51 per cent of total exports, followed by Colombia on 6 per cent,

Suriname on 5 per cent with Brazil accounting for 4 per cent of Venezuelan exports. As an export destination Australia ranked 64th.

- 10.26 Australia's interests in Venezuela focus on the mining and mining services sector. The significant Australian investor in Venezuela is BHP. BHP has a joint venture with Sivena worth US\$700 million constructing a hot briquetted iron plant (HBI) at Puerto Ordaz, 525 kilometres south east of Caracas in the Guayana region. The project is being undertaken by a company, Orinoco Iron, owned 50/50 by BHP and Sivena.
- 10.27 The project involved the acquisition of an existing HBI plant owned by Fior de Venezuela S.A. at Puerto Ordaz and the construction of an adjacent direct reduced iron plant manufacturing hot briquetted iron with associated infrastructure facilities.
- 10.28 The Trade Sub-Committee through the generosity of BHP was able to visit the HBI plant at Puerto Ordaz and the Guri Dam. When the Trade Sub-Committee visited the plant in late March it was nearing completion and the first briquette rolled off the production line on 29 May 2000. BHP is highly thought of in Venezuela. In discussions with key ministers and senior officials in Caracas and with Guayana officials, it was particularly evident that Australian business is very welcome in Venezuela. It was put to the Trade Sub-Committee that Australia does things the right way and BHP has been at the forefront of promoting this positive image of Australia in the way it has conducted its business in Venezuela. The Committee commends BHP.
- 10.29 Guri is the world's second largest hydro electric plant in terms of installed power after the Itaipú complex shared between Brazil and Paraguay. Guri is in 8th place among the 10 dams with the largest reservoir volume. Conceived in the mid 1950s, with the first stage of dam construction beginning in 1963 and the last stage being completed in 1986, the dam has the capacity to generate 50,000GWh per year. This is the equivalent of 300,000 barrels of oil a day that enables compliance with the policy to replace thermal electricity with hydro electricity, in order to export liquid fuels or save them for other purposes.¹⁴
- 10.30 Guri provides the power to the Guayana industrial region around Puerto Ordaz, which is one of the biggest industrial regions in the Southern Hemisphere and the development is most impressive. Not only does Guri provide power to the national grid it is now exported, with energy sales to Colombia and Brazil.
- 10.31 May 1999 saw the official inauguration of construction work at the Las Cristinas gold mine in the south-east of Venezuela. The project worth

14 CVG Edelca brochure, Caracas, 1997.

US\$575 million is a joint venture between Canada's Placer Dome and the Venezuelan government body Corporación Venezolana de Guayana (CVG)¹⁵ and its opening was seen as timely for the development of Venezuela's mining industry under the new government. An Australian company has won a significant contract to provide services at the Las Cristinas mine. P & O Catering and Services have secured the contract to provide catering and other remote location services at the mine. The contract is worth US\$15 million and is regarded as a significant contract in this business. The entry of P & O catering services into Venezuela is seen as auguring well for Australian business to gain other opportunities as they arise in the development of the mining sector.

- 10.32 Australian business has scored other successes in Venezuela. Bodegas Pomar, a division of Polar industries, Venezuela's beverage, food processing and distribution group, is now importing Australian wine through the Hardy's group. Conferry purchased a fast ferry from Austral Ships in Western Australia following the inaugural voyage of the Australian-made fast ferry in August 1999.
- 10.33 Education is one of the fastest growing sectors for Australia in South America. The University of Wollongong has been actively promoting education in South America since 1996 and Venezuela along with Colombia is the focus of the university's efforts.
- 10.34 IDP Education Australia focused its attention on the South American market in 1999. In September 1999 Australian Education International (AEI) and IDP held an education exhibition in Caracas that attracted some 5000 people. In February this year IDP held a further exhibition – *Study Australia Fair* – that covered the sectors of university, vocational education and training, foundation / pathways to university, ELICOS and schools. IDP plans to open an office in Caracas.
- 10.35 Venezuela acknowledges that Australia has advances in technology and education. It recognises Australia has a strong culture and the importance of sharing that culture. The possibility of establishing a good trading relationship also involves a good education and cultural relationship. Cultural links between Australia and Venezuela have developed strongly in recent years and awareness about Australia has been raised through the following events:

15 The CVG is a large state owned organisation responsible for the resource rich Guayana region in south-east Venezuela. The CVG is responsible for commercial development in the region and is a partner in a number of large projects in the region including iron ore mines, aluminium and steel mills, hydro-electric complexes and forestry projects. It is a partner in the Orinoco Iron project through the company CVG Ferrominera Orinoco.

- In August 1996 the Caracas based choir *Cantoria Alberto Grau* toured Sydney and Canberra.
 - In May 1997 the local theatre company *Teatro Unicornio* mounted a successful season of a translated version of David Steven's *The Sum of Us* and completed a second season six months later.
 - Aboriginal art has enjoyed a strong presence in Venezuela with the *Prints of Seven Aboriginal Artists* exhibition in September-October 1998. This was followed by the *Seasons of the Kunwinjku* exhibition (part of the Sydney 2000 Reaching the World Cultural Festival) held in Caracas in April-May 1999 and Maracaibo in May-June 1999.
 - The modern string quartet *Elektra* visited Caracas in April 1999.
 - The Handspan Theatre Company performed their award winning production of Picasso's *Four Little Girls* at the XI Caracas International Theatre Festival in 1997. This led to the engagement of two Australian groups for the 2000 festival - *Strange Fruit* and *Stalker*. *Stalker* was performing during the Trade Sub-Committee's visit to Caracas in March 2000.
 - A photographic exhibition and mini-film festival were also held during 1999.¹⁶
- 10.36 The Australian Embassy in Caracas notes that the Sydney 2000 Olympic Games have stimulated considerable interest in Australia and the Embassy has worked with the Venezuelan National Olympic Committee to promote the Games as widely as possible. With the generous support of a number of members of the Australia - Venezuela Business Advisory Council (AVBAC) the Embassy arranged for the sponsorship of a Venezuelan athlete to live and train in Australia for a three month period from November 1999 to February 2000.¹⁷
- 10.37 Venezuela is very keen to have a good and transparent relationship with Australia and assisting the building of strong links is the AVBAC. The Council was formed in 1998 at the initiative of the Australian Embassy. It has become the focal point for bilateral commercial cooperation. Members are drawn from a broad cross-section of the Venezuelan and Australian business community and government representatives. The group has improved the quantity and quality of mutual knowledge about the respective markets and assists in developing synergies between the commercial, cultural and political aspects of the bilateral relationship.

16 DFAT, Country Brief.

17 *ibid.*

- 10.38 Following the severe flooding in Venezuela in December 1999 that caused massive landslides along the country's coast, the Venezuelan government made an international appeal for emergency relief. Estimates of the death toll have suggested that as many as 50,000 people may have died. In response to the emergency relief appeal the Australian Government, through AusAID, contributed \$100,000 for the provision of medicines, clothing and bedding.¹⁸

Opportunities for Australian Business

- 10.39 CONAPRI outlined a range of business opportunities in Venezuela when the Trade Sub-Committee met with them that included telecommunications and aluminium strategic associations.
- 10.40 Other areas that CONAPRI is seeking foreign investment in are:
- Forestry plantations.
 - African palm.
 - Infrastructure:
 - ⇒ Railways;
 - ⇒ Waterways;
 - ⇒ Roads;
 - ⇒ Electric power.
 - Tourism.
- 10.41 The Trade Sub-Committee had particularly valuable discussions with the Minister for Production and Trade and the Vice-Ministers of Agriculture, Tourism, Trade and Industry. The discussions were wide ranging and it was clearly evident that Australia has the expertise to make major inroads in capturing the opportunities that are available in Venezuela and the rest of South America.

Mining and Mining Services

- 10.42 Venezuela's mining industry is underdeveloped and accounts for less than 1 per cent of GDP. This is due to the dominant role of the petroleum industry in the economy and the previously unfavourable foreign investment regime. The mining industry has been identified as a key sector by the government particularly as a source of export revenue and

inputs for domestic industry.¹⁹ A new mining law has been passed that has a number of incentives that will enable the sector to begin to develop.

10.43 Venezuela has abundant mineral wealth and some of the world's largest reserves of iron ore, aluminium, nickel and gold. The construction of the Las Cristinas gold mine and P & O catering services' success in winning the contract at the mine provides enormous scope and impetus for Australian service industries to examine seriously the market in Venezuela.

10.44 With regard to aluminium strategic associations, CONAPRI outlined the following business opportunities:

■ Bauxilum:

- ⇒ Construction and operation of bauxite moisture reduction plant, using a BOT scheme;
- ⇒ Estimated investment amount: US\$100 million.

■ Alumina operator:

- ⇒ Commercial agreement to increase production to 2 million MT;
- ⇒ Estimated investment amount: US 200 million.

■ Lamination plant:

- ⇒ Private investor assumes technological update;
- ⇒ Private investment would be capitalised;
- ⇒ Estimated investment amount: US\$30 million.

■ Port on Orinoco River:

- ⇒ Remains in State's hands;
- ⇒ Asset leasing to a private operator to increase capacity and uses.

■ Alcasa: Lines I and II (currently closed):

- ⇒ Private investor would assume technological and environmental update to resume operations;
- ⇒ Private investment would be capitalised;
- ⇒ Estimated investment amount: US\$60 million.

■ Lines III and IV, Line V (project) and Carbonorca:

- ⇒ The State offers assets of Line III and IV, the project for Line V and assets of Carbonorca;
- ⇒ Private investor builds Line V with its own financing;
- ⇒ Estimated investment amount: US\$600 million;

⇒ State's share would be minor.

Gas Exploration

- 10.45 In a meeting with the Ministry of Energy and Mines the Trade Sub-Committee was informed that Venezuela wants to develop its gas industry and is now looking for gas as part of the strategy to decrease reliance on oil and diversify the economy. Australia's success in gas exploration and gas exports was discussed and keen interest was shown in the expertise that Australia has in this field. It would be of value for Australian business to follow up on such openings especially as Venezuela recognises the need for international investors and have made changes in the law in relation to the gas and electricity sectors. Electricity generation, the Trade Sub Committee was told, is now completely open allowing any foreign company to come in and invest. Furthermore the government is opening up the laws for prospective exploration of gas.
- 10.46 Venezuela has a plan for natural gas but as part of this plan it will need to increase the price of petrol (around US 24c a litre in March 2000) so as to remunerate the industry and control the use of gasoline. There are opportunities here given Australia's experience in the utilisation of natural gas, such as its use in public transport.
- 10.47 PDVSA noted that there are a wide range of opportunities in gas and petrochemicals and it expects Australia to come along with its companies and share in the opportunities. It plans to exit from one of its core interests, the coal business.

Education

- 10.48 In the 1998 AEI study on opportunities for Australian education in South America, Venezuela was included, and AEI made a number of observations. At the postgraduate level where the US is the favoured destination for Venezuelan students, there are opportunities in the areas of engineering – industrial materials, mechanical, environmental, petroleum; geology and mining exploration. AEI notes that postgraduate programs in environmental management may be of interest.²⁰ There are also opportunities for Australian education consultancies to assist in improving education in Venezuela through vocational education and training and to utilise Australia's expertise through the Australian Qualifications Framework that is well developed and highly respected internationally.

20 AEI, Exhibit No 4, p. 35.

Telecommunications

- 10.49 The business opportunities that CONAPRI said will become available in the telecommunications sector involve:
- New concessions on wireless telephone service:
 - ⇒ LMDS;
 - ⇒ WLL.
 - Internet as a national priority service.
 - New Telecommunications Law.
 - End of *limited competition* period on basic and international phone services.
- 10.50 The National Legislative Council – the interim congress - passed the 2000 Telecommunications Bill on 1 June 2000 that establishes a modern legal framework for the development of the telecom industry in Venezuela. Basic telephony services are held under a temporary monopoly by CANTV, the national telecommunications company, with the monopoly due to expire on 27 November 2000. This telecom monopoly has been one of a number of market access issues impacting on Australian business. The next round of market opening will take place from 27 November with the new legislation establishing telecom services as economic activities of general interest and public and social usefulness.
- 10.51 The National Telecommunications Plan drawn up by CONATEL, the National Telecommunications Commission who has the watchdog role, contains long – 12 years, medium – 6 years and short term goals. Major objectives include:
- All citizens having access to a telecom terminal.
 - A leading role for Venezuela as a business telecommunications centre within the Andean Community and the Caribbean region, with services export potential.
 - The Venezuelan government to become an intensive user of information and telecommunications technologies.
 - The development of high levels of research and higher education capabilities in telecommunications.
- 10.52 Shorter term goals include the concessions that CONAPRI alluded to:
- The adoption of third generation cellular technologies as the next platform in video, voice and data transmission.

- Auction LMDs bands for corporate/business basic telephony market in the second quarter of this year.
- Auction WLL bands for residential basic telephony market in the third quarter of this year.

10.53 Venezuela is one of the Latin American countries with the highest wireless service use per capita with more than 4 million subscribers so that the change to third generation technologies represents a huge business potential.

Tourism

10.54 Venezuela is wishing to develop its tourist industry and in particular eco-tourism. Venezuela has five areas of eco-tourism and the tourism ministry is working very closely with the environment ministry to develop this as a business. There is little doubt that Australia is extremely well placed to be a player in this development through the sharing of its expertise.

Agriculture

10.55 With regard to agriculture, this sector has had little attention paid to it given the focus on oil. The demand for agricultural imports, particularly milk powder and livestock is strong but there are inadequate levels of investment in the sector. Venezuela is seeking to develop this sector and one of its focuses is on the production of cereals. This is yet another area that has potential for Australian interests.

Market Access Issues

- 10.56 In evidence to the Committee DAFT noted a number of market access issues that affect business in Venezuela. Notwithstanding the progress that has now been made on the telecoms monopoly there are some other areas of difficulty.
- 10.57 Customs clearance delays can be experienced. There are still legal uncertainties and uncertainties in taxation demand with the three-tiered fiscal regime. As in other countries in South America there is inadequate protection of intellectual property rights and widespread piracy.