Venezuela’s Shadow Economy.

Prepared for the conference “The Size and Importance of Venezuela’s Illegal Economies”
Latin American Program, Woodrow Wilson Center
January 14, 2020
The Government Financial Lifeline

- Prolonged recession and oil industry collapse have cut the government’s traditional revenue sources.

- US Sanctions places Venezuela in political isolation, prompting approach to less transparent associates.

- Sanction evasion prompts off-record transactions.

- Need to maintain rent distribution mechanism puts pressure on to find alternative revenue flows.

- Venezuela’s dollarization and services collapse pushes for unconventional transaction means.

- A de-facto liberalization pushes both private and public sector into harder to trace channels.
An industry a century in the past

Evolution of Venezuela's Oil Production

Sources: Baptista (2002), Pdvs a and Ecoanalítica.

Average increase 1943-1970: +118 kb/d
Average increase 1986-1998: +112 kb/d
Maximum increase 1947-1957: +159 kb/d
Depending more and more from Russia and China

Oil exports composition

- Cash generating barrels
- China debt service
- Rosneft debt service
- Petrocaribe & Cuba

Sources: Pdvsa, Mefbp and Ecoanalítica.
*Forecast.
Pressuring hard currency reserves

IR vs. Extrabudgetary resources

Sources: BCV and Ecoanalítica
And the usual rent distribution mechanism dries up

Exchange rate subsidy scheme

Public entities  Cadivi/Cencoex/Dipro  Sitme  Preferential CADIVI  Simadi/Dicom  Sicad I and II

Sources: BCV and Ecoanalítica.
The Venezuelan Political Marketplace

The Government controls key economic activity

- Gold production
- Oil imports
- Hard foreign currency supply
- Non-oil imports

Political groups fight access to rents

- Rent access through illegal paths

Loyalty price

The Government gives up control to interest groups

Maintains political cohesion
### The parallel economy

#### Income from *other* activities in 2018

<table>
<thead>
<tr>
<th>Activity</th>
<th>USD MM</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gold contraband</td>
<td>2,711.0</td>
</tr>
<tr>
<td>Gasoline contraband</td>
<td>1,860.3 - 2,790.5</td>
</tr>
<tr>
<td>Narcotic trafficking</td>
<td>2,650.0</td>
</tr>
<tr>
<td>Exchange rate subsidy</td>
<td>3,446.4</td>
</tr>
<tr>
<td>Overbilling</td>
<td>3,710.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>14.378.5 - 15.308.6</strong></td>
</tr>
</tbody>
</table>

Sources: OEA, UN Comtrade, TSI and Ecoanalítica.
The black market economy sources represented 31.9% of the income.
Renewed focus on imports overbilling

Imports overbilling

Sources: TradeMap, BCV and Ecoanalítica.
Rising gold transaction costs

In 2018 they sold USD 3,280 MM at USD 2,710 MM (17.3% discount)

Sources: UN Comtrade and Ecoanalítica
*Gold purchases in the local market reported to the BCV.
**After nationalizing gold (2011), export were higher that purchases done by the BCV.

In 2018 they sold USD 3,280 MM at USD 2,710 MM (17.3% discount)
Effects in the real economy

- Income from unorthodox sources finds its way to the real economy.
- Deepening transactional dollarization in an environment of looser regulations.
- Redirecting into Venezuela funds that cannot be taken to tax havens.
- Cash euros used as foreign exchange market stabilizer.
- Difficulty to discern dollars from criminal activities from legitimate ones.
Intervening in the currency exchange market

Euros in cash sold to the financial system (2019)

Sources: Ecoanalítica.
Imports become harder to track

Imports by origin (Top 10)

Sources: Official data reported by each country and Ecoanalítica.
Imports become harder to track

Imports by origin (Top 10)

Sources: Official data reported by each country and Ecoanalítica.
Getting tangled with other cash flows

Remittances to Venezuela (MM USD)

Sources: Banco Mundial, Cemla, BCV and Ecoanalítica
*Estimations.
Note: Current transfers from BCV are valued as remittances.
What to expect this year?

- Low chances of a political change.
- Economy, firms and business reduction.
- Illegal market expansion.
- Almost irreversible degree of informal dollarization.
- Continued pressure over external accounts.
The Executive will have to reduce expenses

<table>
<thead>
<tr>
<th>Item</th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Oil Exports (mb/d)</td>
<td>1.35</td>
<td>1.0</td>
<td>0.7</td>
</tr>
<tr>
<td>Energy Agreements (mb/d)</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Oil Imports (mb/d)</td>
<td>0.1</td>
<td>0.2</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>Effective Oil Exports (mb/d)</strong></td>
<td>1.4</td>
<td>1.1</td>
<td>0.7</td>
</tr>
<tr>
<td>Brent Price (USD/bl)*</td>
<td>69.7</td>
<td>65.7</td>
<td>59.9</td>
</tr>
<tr>
<td>Venezuelan Oil Basket Price (USD/bl)*</td>
<td>61.9</td>
<td>59.6</td>
<td>51.5</td>
</tr>
<tr>
<td><strong>Oil Income (Billion USD)</strong></td>
<td>31.8</td>
<td>23.1</td>
<td>13.9</td>
</tr>
<tr>
<td><strong>Oil imports (Billion USD)</strong></td>
<td>3.5</td>
<td>3.7</td>
<td>2.1</td>
</tr>
<tr>
<td>Oil Imports (Diluents and Supply)</td>
<td>0.0</td>
<td>-1.0</td>
<td>-0.9</td>
</tr>
<tr>
<td>Other Oil Imports</td>
<td>28.2</td>
<td>18.4</td>
<td>10.9</td>
</tr>
<tr>
<td><strong>Non-Oil Income (Billion USD)</strong></td>
<td>2.5</td>
<td>6.3</td>
<td>6.6</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td>30.7</td>
<td>24.7</td>
<td>17.5</td>
</tr>
<tr>
<td><strong>Expenditure</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other imports (Billion USD)</td>
<td>9.1</td>
<td>5.9</td>
<td>5.9</td>
</tr>
<tr>
<td>Net services</td>
<td>6.2</td>
<td>5.8</td>
<td>5.6</td>
</tr>
<tr>
<td>Net rents</td>
<td>8.0</td>
<td>7.9</td>
<td>7.6</td>
</tr>
<tr>
<td>Current Transfers</td>
<td>-2.0</td>
<td>-2.7</td>
<td>-2.0</td>
</tr>
<tr>
<td>External Debt Service (Billion USD)</td>
<td>4.5</td>
<td>1.2</td>
<td>0.6</td>
</tr>
<tr>
<td>Private Capitals Outflow (Net)</td>
<td>-2.3</td>
<td>-1.1</td>
<td>-1.0</td>
</tr>
<tr>
<td><strong>Total Expenditure</strong></td>
<td>23.4</td>
<td>16.9</td>
<td>16.7</td>
</tr>
<tr>
<td><strong>Result</strong></td>
<td>7.3</td>
<td>7.8</td>
<td>0.8</td>
</tr>
<tr>
<td><strong>Financing (MM USD)</strong></td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Oil income retained by the USA</td>
<td>0.0</td>
<td>-3.1</td>
<td>0.0</td>
</tr>
<tr>
<td>Net Flow with China</td>
<td>-4.2</td>
<td>-3.2</td>
<td>-3.2</td>
</tr>
<tr>
<td>Net Flow with Russia (Rosneft)</td>
<td>-3.2</td>
<td>-1.9</td>
<td>-0.5</td>
</tr>
<tr>
<td><strong>Net Result</strong></td>
<td>-0.1</td>
<td>-0.3</td>
<td>-2.8</td>
</tr>
</tbody>
</table>

Sources: BCV, Menpet, Pdvsa and Ecoanalítica

* Considers a 90 day lag due to the internal dynamics of the oil market
1 We take into account the reexported imports
2 Considers non-oil imports and other imports from the oil sector
ECOANALÍTICA, C.A.

www.ecoanalitica.com
asdrubalo@ecoanalitica.net
(58-212) 266.9080
Twitter & Instagram:
@aroliveros / @ecoanalitica