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Will Venezuela follow Mexico?

David Goldman, Economics Editor, reports on his recent trip to Caracas and the choices facing the Herrera Campins government.

Venezuela's Christian Democratic President Herrera Campins, despite $14 billion in flight capital from the oil rich country in the past two years, has rejected plans offered him from a number of quarters to impose exchange controls in imitation of Mexico, whose controls program of Sept. 1 has eliminated 90 percent of Mexico's flight capital and permitted a sharp lowering of interest rates. Venezuela's failure to obtain a $3.5 billion "jumbo" credit, scuttled on the Euromarkets in the wake of the Mexican measures, and, more fundamentally, the predicted effects of economic depression on oil earnings, have heightened the outflow of capital.

Despite the half-century record of stability in the Venezuelan bolivar's parity with the dollar, a major devaluation is inevitable before year-end should the government maintain its stoic posture on exchange controls. The question is not whether Venezuela will impose controls, but whether it will do so after a shattering devaluation—as Mexico did—and whether its leaders will be able to pick up the pieces afterwards, as Mexico's leaders have shown they can.

Only the most forward-looking and the most backward-looking individuals inside the Venezuelan government understand that the brewing crisis has less to do with whatever short-term measures it takes than with a basic crisis in the international banking system. A few are looking towards a Mexican-type program applied to the entire Ibero-American continent, that is, an Ibero-American Common Market; Planning Minister Maritza Izaguirre's interview with *EIR* in September at the Toronto IMF meeting, expressing support for Mexico against international pressures, reflects the President's own viewpoint and that of most of his government. Some well-placed government officials, however, flatly predict that Venezuela will be ground up in the crisis.

But the government has yet to come to grips with the fact that the superficially encouraging monetary situation—the lowest inflation rate and the most stable currency on the continent—was bought at the expense of precisely those industrial and technological resources which might equip Venezuela to withstand the crisis almost at hand. Former President Carlos Andres Pérez, whose Social Democratic government gave way to the conservatives under Herrera Campins in 1979, had begun a broad, but formless, campaign of industrialization. Under the impetus of the Venezuelan central bank, the continent's most monetarist outside Chile, the new government raised interest rates and reduced industrial investment, reducing industrial production by roughly half in the last three years. But the central bank's stringency did not apply to the eye-popping levels of speculation on the Caracas real estate market, where condominium prices rival those in New York, or other wild excesses.

Central bank takes first defeat

The Herrera Campins government last month bucked the central bank for the first time since taking office, approving a $2.2 billion steel and coal mine project in Western Venezuela. The project is not merely important for Venezuelan industry; metallurgical coal, which the continent has in abundance, remains an undeveloped resource. Although the Ibero-American countries can not smelt enough steel to meet their entire requirements, they still must import 6 million tons of metallurgical coal, the only significant trade dependency in the entire area of industrial materials. Like a similar project underway in Colombia, the Zulia coal and steel project would represent a strategic step towards continental self-sufficiency, a baseline requirement for the ultimate success of a Common Market that might have to stand up against virtual total trade war from the United States and perhaps other industrial nations. The project will include a mine producing 4 million metric tons per year by 1992—a target year capable of moving forward—potentially meeting two-thirds of continental requirements, as well as a 480,000 ton flat rolling mill.

Especially significant in the long-delayed decision to advance the project is that it was taken in the face of bitter, open opposition by central bank president Leopold Díaz Brazual, who called it "unnecessary and costly." It is a very tentative move: Two-thirds of the project depends on foreign finance that will likely not be available in present market conditions, and the government has yet to propose how to finance the external infrastructure required to provide access to the plant. Nonetheless it is as much an indication of re-thinking inside the Venezuelan government as the unqualified support for Mexico's sovereign decisions expressed for the public record by Planning Minister Izaguirre, and reiterated to this writer in private conservations with a number of senior officials.

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The government's attention is still consumed in a comic-opera debate over the state of the present budget, in which the administration has coyly resisted central bank demands for austerity. Capital continues to flow out of the country, adding to the $14 billion in private assets abroad of Venezuelan citizens—$900 for every citizen of the country! Without exception, Venezuela among the leading Ibero-American countries has the least capacity to resist external pressures, and therefore depends most for its own future on the prospects for a regional Common Market. It has already vastly reduced industrial and related imports. Its present import structure is overwhelmingly oriented towards consumer goods, including food, more than half of which is imported. The import dependencies are astonishing; Venezuelan television features translations of U.S. commercials for dishwashing liquid, shampoo, and canned fruit!

A combination of balking by Venezuela's creditors, virtually certain as the confrontation between Mexico and the International Monetary Fund dominates Ibero-American debt questions, and further softening of world oil trade could throw the apparently stable economy into chaos overnight. The country's biggest problem is that only 1 in 40 of its citizens is an industrial worker, against 1 in 12 in the United States, and 1 in 6 in the Soviet Union, the latter two at much higher levels of productivity. Thirty percent of the population is rural, cut off by bad infrastructure from the cities, and largely excluded from the money economy. It is vastly overweight in terms of real estate, financial, retail, governmental, and other services, supported by oil revenues which have already dropped 20 percent over the past year.

Although Venezuela, until recently, was able to obtain the best terms of any Ibero-American nation on the Euromarket, the debate over the size of the country's debt was a hint that a submerged problem may surface in an unpleasant fashion very quickly indeed. The Finance Ministry last week disputed the claim that the total debt, estimated by another governmental agency, was $34 billion, rather than the $28 billion the Finance Ministry cited. In fact, the total debt, including the highly sensitive interbank market obligations of Venezuelan private banks, is probably closer to $40 billion; if the private dollar debts of Venezuelan citizens were included, e.g., billions of dollars of mortgage debt against American real estate, the total would be even higher.

American bankers' biggest immediate worry with respect to Ibero-America is an uncalaculated sum of short-term interbank loans, believed to total $10 to $15 billion, excluding Mexico; the Venezuelan portion is at least $4 billion and perhaps $6 billion. New York branches and agencies of Venezuelan, Brazilian, Colombian, and Argentine banks have booked interbank, i.e., federal funds, credit lines to most of the big New York banks and also foreign institutions' branches in New York, of $5 to $15 million apiece. In addition, their Caribbean outlets have borrowed heavily on the interbank deposit market. New York banks are now scrambling to transform these short-term loans into straight commercial lines, under the control of their country-lending departments; but the possibility of a chain-reaction drawdown of such interbank lines haunts bankers, who fear a repetition of the Banco Ambrosiano's recent repudiation of the $400 million obligations of its Luxemburg subsidiary.

Odd thinking at national oil company

The odd plan of General Rafael Alfonzo Ravard, president of the national oil company Petroleos de Venezuela, to divert 500,000 barrels a day, more than one-sixth of the country's production, to a special debt-amortization fund, will not be put into effect, because the country is moving into a situation where it can afford no such thing. But the thinking at the national oil company runs in jarring contrast to the Ibero-American perspective germinating elsewhere in the country. Its adviser, R. A. Irving Jahn, a Venezuelan-born Englishman who speaks Spanish with an accent resembling actor Robert Morley's, waved off the idea that Venezuela's problem was lack of industrial technology. "You can always find a mercenary engineer," he said in a Sept. 16 discussion at the oil company's Caracas headquarters. "The problem is administration. Small societies like Venezuela's are good at putting large numbers of blue-collar workers to breaking rocks, because you can whip them if they don't work hard enough; but they are very bad at putting large teams of white-collar people to administering large programs, because whipping an architect or engineer doesn't make them produce better. They have no motivation or training, and are mainly interested in making a great deal of money quickly."

Irving does not believe the International Monetary Fund will have much more success in dealing with Venezuela than it has had recently with Mexico. "The United States and the IMF are living outside the real world," he said. "They don't understand the force of nationalism. This means a breakup of the American imperial power; to understand this you must read Gibbon. And that is perhaps a good thing." But left-wing "Castroism" and right-wing reaction are, Irving concluded, the "upper and nether millstones" between which Venezuela would be ground up.

That alternative Mexican President Jose López Portillo averted, by breaking the back of the political forces who would contribute to such a conflict through the bank nationalization of Sept. 1. It is not excluded that Venezuela may become what Mexico refused to become: the hideous example to the rest of the continent that Irving described. And the errors of Mexican policy are magnified several times over in the Veneuzelan case, i.e., neglect of infrastructure, industry, and agricultural productivity in favor of an import-based consumer boom with the durability of a paper boat in a tropical storm. At least in context of a mutual support program, of the sort that Venezuelan Minister Izaguirre suggested in her Sept. 7 interview with *EIR*, Venezuela may turn in time to avert the worst consequences of its past mistakes. But much will depend on what the Herrera government does in the immediate weeks ahead.