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Venezuela: the anatomy of an IMF program to destroy a nation

by Peter Rush

On March 15, Venezuela's President Carlos Andrés Pérez implemented Phase II of his International Monetary Fund-approved austerity plan by floating the Venezuelan currency, the bolivar, and lifting most price controls. Overnight, importers were confronted with an increase of 162% in import prices, as the previous official exchange rate of 14.5 to the dollar was replaced with the free market rate of 38.

The measure has caused immediate panic in almost every sector of the Venezuelan economy. Thousands of businesses will soon face bankruptcy. Within the first 24 hours of the new measures, the publishers of 48 provincial newspapers warned a congressional committee that many of them would have to drastically curtail operations, or go out of business altogether, because the price of the imported newsprint on which they depend had just risen by more than 160%. Those that don't fold will have to jack up their prices, hurting sales. Many other sectors are expected to have similar crises. And the thousands of firms that owe over $6 billion in letters of credit contracted at the 14.5 bolivar rate must now honor these letters at 38, even though the goods that were imported have already been sold, and many of these are expected to go bankrupt as well, including many smaller firms.

But this is just the beginning. With imports accounting for at least 30% of domestic consumption of food and manufactured goods, the inflationary impact is expected to be at least 50% on average, in the near term, hitting hardest those who import consumer goods, but affecting every industry that depends on imported parts or raw materials—which is most of them. Since the vast majority of Venezuelans do not now earn enough to get by, the price increases will provoke a collapse of domestic sales and consequent unemployment.

Phase I of the IMF program, the raising of fuel and public transportation prices, which provoked the recent rioting and looting, and the Phase II measures launched on March 15, were both laid out a full year ago by an IMF mission that visited Venezuela in April 1988, as revealed in several secret Office Memoranda dated May 5, 1988, from the project directors to IMF Managing Director Michel Camdessus. These were expanded and scheduled as to precise date of implementation in the Letter of Intent signed by Venezuela on Feb. 27 in New York, as summarized in the excerpts that follow. The earlier memos zeroed in on several areas of prime concern, including exchange rate policy (unifying the exchange rate and floating the bolivar), lifting price controls, raising interest rates and eliminating foreign trade restrictions, but bemoans the fact that, for political reasons, the government was not inclined to make the "reforms" before the elections for fear of causing Pérez to lose.

Now, having won the elections, Pérez continues to carry out the Letter of Intent with precision.

Opposition attacks Pérez policy

"If, to a hungry person, one applies conditions that increase that hunger, it is not appropriate to tell him that within two or three years he will be able to begin eating again," former President and leader of the opposition Copei party Rafael Caldera said in a speech on the floor of the Venezuelan Congress March 9. He was referring to the pious affirmation in the IMF Letter of Intent that growth is only slated to begin two years from now. He attacked the "technicians" in the government who are applying measures "that necessarily worsen the situation," without regard to their present effects.

His criticisms were echoed by Copei economist and deputy José Miguel Uzcategui, who zeroed in on the true nature of the IMF program. "The philosophy of this economic package is anti-industrial . . . many companies are being condemned to total abandonment," he said in an interview with *El Nacional* March 10. "All of this means that the Pinochet model is being imitated, which destroyed Chilean industry for the sake of an opening to foreign markets. . . . It can be concluded that the government has no clear strategic objectives in the social areas," he concluded.

Inside an IMF Letter of Intent

In a rare leak, the Letter of Intent signed by Venezuela with the IMF on Feb. 27 was published in full March 3 in *El País* of Caracas. This document reveals that the Pérez government is proceeding in the implementation of its economic "reform" measures in precise conformance with what was agreed in the Letter of Intent, merrily proceeding as though the riots had never happened.

The package of "reforms" laid out in the Letter of Intent

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(see *Documentation*) is, taken at face value, a hideous consumer fraud, an internally self-contradictory document which throws in a few hollow promises of future growth to disguise the truth: that the concrete measures proposed ensure that Venezuela will never grow again. Taken on a deeper level, the program is intended to open up Venezuela to foreign takeover, starting with its petroleum, aluminum, and iron ore resources, and including the surrendering of economic sovereignty, foreign takeover of its financial system, and the gutting of all domestic industry. This was the reason why the banks permitted Venezuela, and many other countries, to become so highly indebted up through 1982, and it remains the goal today.

The one consistent theme running throughout the Letter is the intent to crush wages and living standards. This is admitted even on the surface, when the Letter says that following a wage increase of 30% for public workers on March 1, wages will remain frozen for the remainder of the year, while inflation is anticipated to come in at 35.5%. Since the 30% wage hike merely compensates for previous inflation, real wages are therefore explicitly intended to be depressed a further 35% by the end of the year. But that's just for starters.

No hint is provided of how this 35% inflation estimate was calculated. In light of the revelations made by ex-IMF official Davison Budhoo (see *EIR*, Jan. 27, 1989) concerning IMF faking of figures of all kinds, one can be quite certain it is a cooked number, pulled from a hat, as a "plausible" lie to pacify the unwary.

First, the devaluation mandated in the Letter and implemented March 15 has raised, overnight, the cost of all imported goods by 162%. In 1988, Venezuela imported $10 billion in goods, a whopping 40% of the total of all goods produced in the country. Simple arithmetic establishes that at the very least, this devaluation must raise the price level—over the next few weeks—by 40% of 162%, or 65%. But hyperinflation has its own logic, and price increases will undoubtedly be substantially higher than that, for those companies able to avoid bankruptcy. By curious "coincidence," the Letter of Intent manages not so much as a single reference to the inflationary impact of the devaluation, although the pattern is well established, and although the Letter does find space for great detail on tertiary matters of far less gravity. Honesty was clearly inconvenient on this point.

And of course, with such a spurt in inflation, the bolivar cannot be expected to remain fixed at its new rate, but to continue devaluing at roughly the inflation rate—leading to yet more inflation, etc., in a vicious hyperinflationary spiral such as that witnessed in recent years in Brazil. The expectation in the Letter of 5% inflation by 1992 is intentional deception.

But inflation is programmed in from other quarters as well. The prices of all petroleum products, starting with gasoline, rose 94% in late February, to rise again by 70% next January, and to the world market level by 1992. Electricity and telephone rates are also to go up by 50% this year. But both rates could end up being raised much more if inflation exceeds 35%, as the purpose of all these increases is to increase government revenue, net of inflationary effects. In any event, all of these increases are much higher than the 35% predicted inflation rate, proving that this rate is a hoax.

Further attacks on real incomes are scheduled farther down the line, in the form of sales and value-added taxes, increased contributions to social security, and reinforced tax collection efforts, among others.

Business is equally hurt, even beyond the damage of the devaluation. With the liberalization of imports through a mixture of tariff reductions and eliminations, foreign imports will be able to compete and wipe out much of domestic industry. With the precipitous decline in real wages, domestic markets will shrivel and die, bankrupting many companies and limiting others strictly to what they can export. Interest rates, at 12% until February, are to be freed by May, to rise, most probably, to well above inflation, that is, minimally 45-50%, and probably much higher, dropping business borrowing to near zero. The devaluation ensures that investment in modernized plant and equipment will grind to a halt because of its exorbitant expense of imported machinery, and the collapse of sales. This makes a mockery of the idea that private investment will burgeon to both take up the slack of reduced public investment, and expand total investment from 20% to 24% of the GNP. A decline to 10% is more likely. A wave of bankruptcies is already forecast to begin almost immediately. In all of this, unemployment can be expected to skyrocket, increasing social costs.

Finally, the Letter assumes that Venezuela will be able to borrow or reschedule $6 billion in debt service it will owe in 1989. Even were this possible, it would increase total debt by at least this year's $4 billion due in interest, to $37 billion by 1990, and to at least $45 billion by 1992—incurring yet greater debt service charges. (The Letter also assumes $1.3 billion in returned flight capital, a pipedream. Far more likely is a massive outflow of flight capital.) In fact, the true debt is already technically at $40 billion, as the $6.7 billion in letters of credit are in effect unpaid debts. Yet the Letter mendaciously refers to the "reduction of the debt" and a "permanent solution of the foreign debt problem." Since in reality the banks will surely not finance the entirety of debt service, a large jump in non-petroleum exports—at the expense of domestic consumption—sharp reductions in imports, and extreme government budget cuts and increases in internal debt will be required.

All of this, were Pérez permitted to impose it, would merely open the country to being bought up at bargain prices, by the banks and multinationals for which the IMF does its dirtywork. To this end, the Letter also envisages the privatization of most public sector industries, and public/private "co-participation" for the remainder, presumably including the National Oil Company.

Documentation

What Venezuela signed away to the IMF

Excerpts from Letter of Intent signed by Venezuela to the International Monetary Fund on Feb. 27, in Washington:

The new administration . . . recognizes the necessity of putting into place a broad program of adjustments . . . [of implementing] important structural reforms in the fiscal, exchange rate, foreign trade and financial sectors. . . . In this effort, the Government of Venezuela expects to count on the total backing of the international financial community. . . . These accords would necessarily require the provision of financial flows at levels consistent with the requirements of the balance of payments and the country's economic development objectives . . . and incorporate new initiatives that permit the reduction of the debt, and thereby establish the basis for a permanent solution of the foreign debt problem of the country.

The medium-term policies . . . have as their fundamental objectives to: 1) strengthen internal savings; 2) promote incoming foreign capital; 3) diversify the economy through a liberalization and adjustment process . . . [which will] increase economic and social efficiency and strengthen the strategy of foriegn-oriented development. . . . It is expected that these policies . . . will permit a sustained growth of 4-5% in the medium term for the non-petroleum sector, at the conclusion of a transition phase of about two years.

To achieve these rates of growth, the investment/GNP ratio must increase from 20% in 1988 to 24%, mainly through an expansion of private sector activity. . . . The inflation rate for 1989 is estimated at about 35%, which should fall significantly in 1990 and by 1992-93 will approximate inflation in Venezuela's trading partners.

The fundamental element of the economic program of the Government consists in establishing a unified, floating exchange rate for the bolivar, a measure which will be implemented in March 1989. . . . To complement these exchange rate measures, the Government will introduce trade reforms in 1989. During March of 1989 . . . a program will be begun which will culminate by the end of the year in eliminating most quantitative restrictions on imports, [including] on luxuries. . . . Starting in April of 1989 . . . tariffs will be substantially reduced.

At the beginning of March 1989, the present system of price controls will be eliminated and a new system substituted involving no more than 25 essential products and services . . . principally foods, medicines and urban bus fares. . . . The fiscal and monetary targets of the economic program for 1989 have been calculated on the base of a projected nominal increase in GDP of 35.5% [0.5% after inflation—ed.]. The Government has decided to increase the price of petroleum products. . . . On Feb. 26, 1989, the price of 14 petroleum products . . . was increased an average of 94%. In January 1990 they will be increased again by at least 70%, with subsequent half-year adjustments to 1992 to bring prices to the international level.

The Government will continue a prudent wage policy, which should contribute to strengthening competitivity, increase employment and reduce inflationary pressures. . . . The wages of Government employees will increase as of March 1 about 30%, including the effect of a 54% increase in the minimum wage. There will be no further wage increases during 1989. . . . With the exception of the minimum wage, private sector wages will be fixed by collective bargaining or by individual accords.

The Government recognizes that restrictive monetary and fiscal policies are required to maintain exchange rate stability, reduce inflation and achieve a reduction of absorption [i.e., private consumption—ed.], in order to make [the absorption] consistent with the improvement expected to be achieved in the current account balance. . . . During 1989 the Finance Minister expects to finish designing a Sales Tax that would be introduced at the beginning of 1990 and will be converted into a value-added tax.

Government spending will be reoriented toward social services, spending for maintaining and modernizing public sector physical infrastructure will be increased, while spending for large investment projects will be reduced. . . . Tax collection mechanisms will be strengthened, by means of an increase in social security contributions. . . . Electricity rates . . . will increase 50% during 1989 in three stages, April, August, and December. At the same time the National Telephone Company of Venezuela will have a rate increase of 30% on April 1 and another in September to bring the year's total increase to 50%. The Government is developing a program of reprivatization that implies a total transfer of public sector property, or co-participation of the private sector with the public sector, in the next few years.

The total foreign financial requirements for 1989 are estimated at about $6 billion ($7.3 billion, minus $1.3 billion repatriation of capital). These requirements are expected to be covered by World Bank disbursements, IMF loans, commercial debt refinancing and new loans from the commercial banks.

The Government has eliminated, as of Feb. 17, 1989, controls on interest rates. . . . No later than March 17, the rediscount rate will be fixed at 30%, and will be adjusted weekly. The floating of the interest rate will promote more orderly financial intermediation. . . . The monetary base is projected to increase 26% in 1989.