



The Financial Market in Venezuela

1964

2014



The Place to be

The Place not to be

The Financial Market in Venezuela from 1965 until today:

A socio-economic analysis fifty years after Dr. Henri Meier's dissertation

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The Agenda



Theoretical foundation of research



Empirical research and findings



Recommendations for Venezuela's future

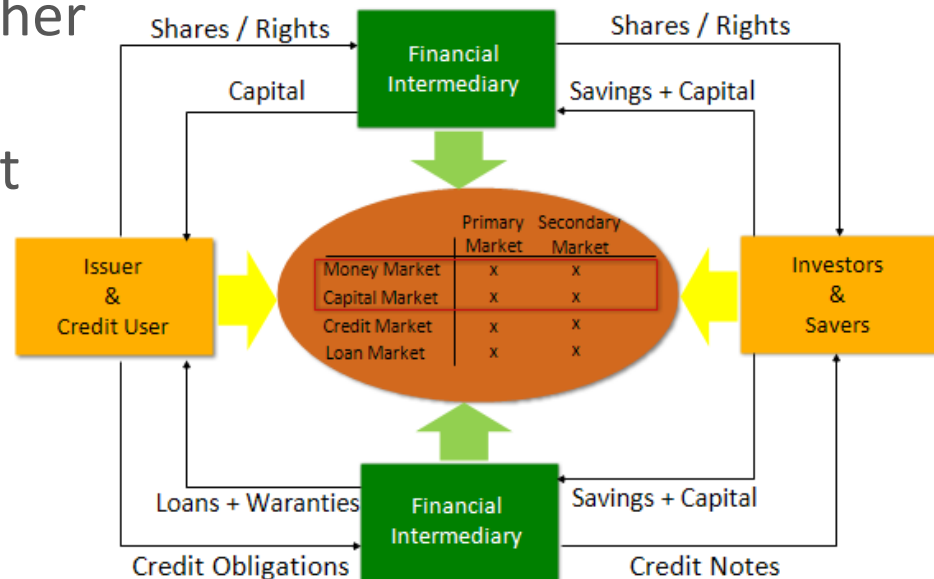


Questions & Discussion



Functioning and Relevance of financial markets

- Financial markets channel funds from savers to investors
- They essentially provide information, shift consumption and allocate risks
- From domestic minimarkets in 1964 to markets which are highly interconnected nowadays
- In 1964 there were neither secondary markets, nor an interbank market



Investments from an economic perspective

- Domestic Investments
 - Three periods (1965-1982, 1983-2005, 2006-2011)
 - Economy's dependence on the oil sector → dutch disease → lower competitiveness → process of deindustrialization
 - New boost lately thanks to public investments

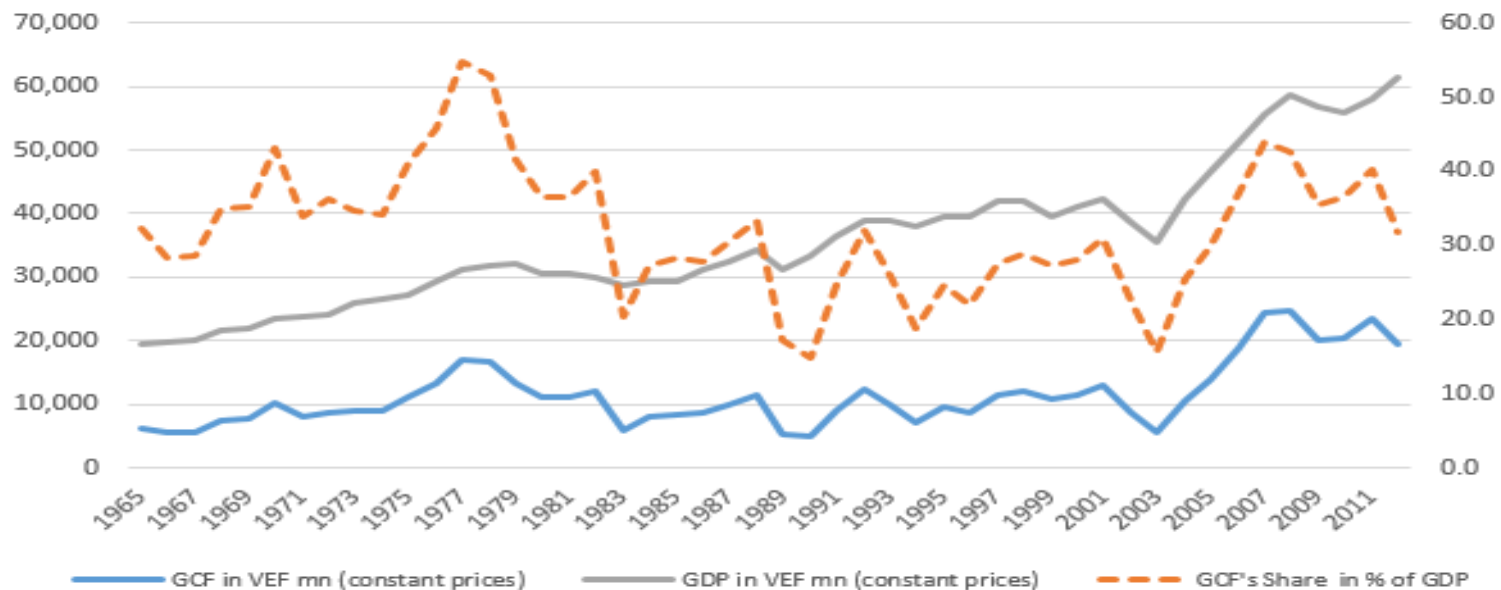
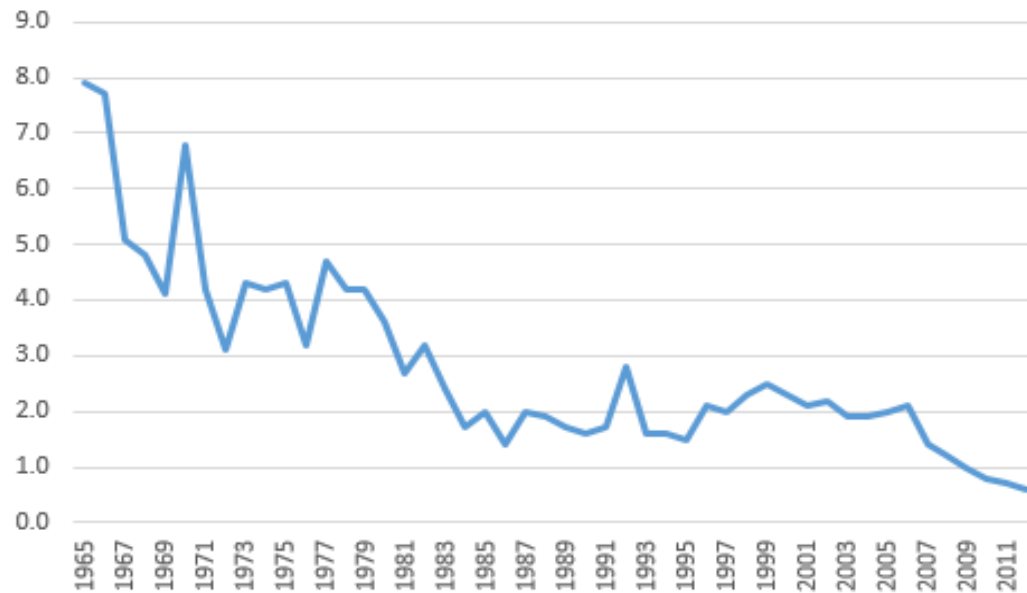


Figure: Development of the investment rate



Investments from an economic perspective

- Domestic Investments
 - Private alienation of capital
 - Withdrawal of foreign capital and, accordingly, know-how
 - Capital accumulation at historic low
 - very limited growth rate in the next 5 years



Development of non-oil private to public investment ratio in % of Venezuela



Savings from a business perspective

- Private Households then
 - Low saving rate
 - Irregular behavior of saving; consider effect of capital outflow
 - No saving mentality due to nanny state

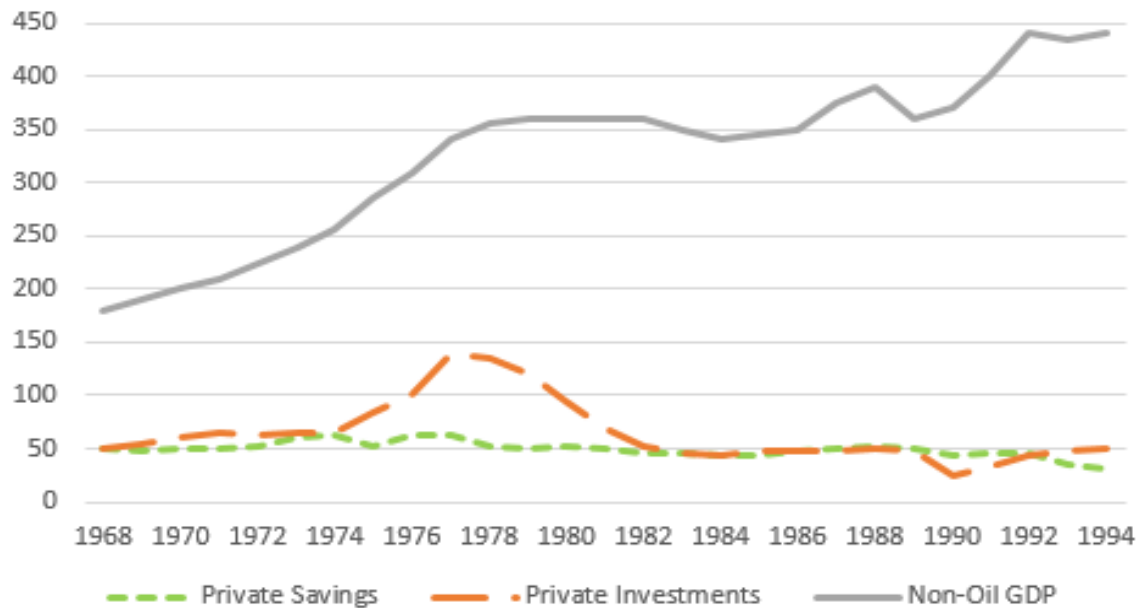


Figure: Development in mn Bolivares of 1984





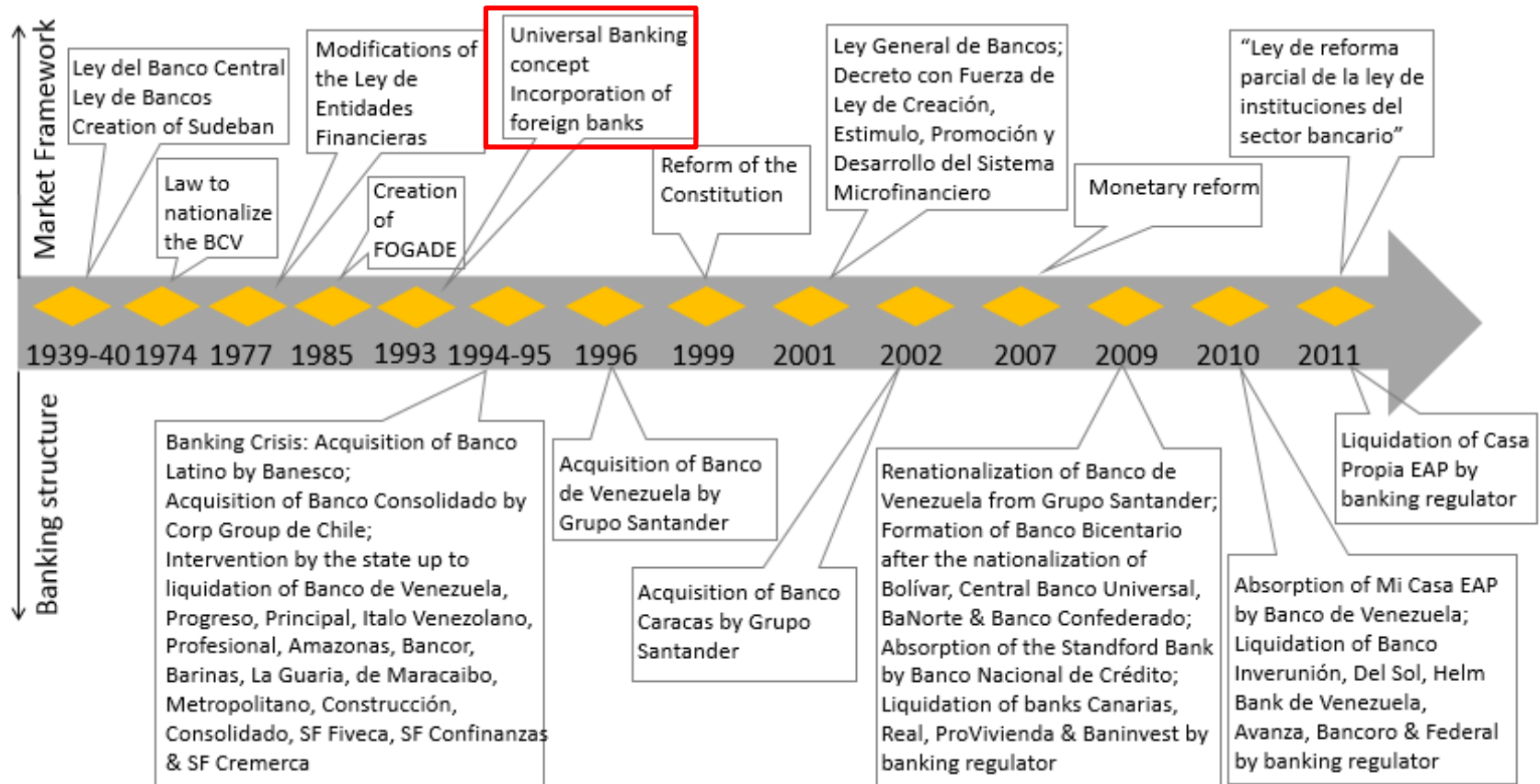
Savings from a business perspective

- Private Households now
 - Deterioration of private savings mostly due to high inflation and currency instability
 - Saving capacity
 - Poorer absolute living standard
 - Fairer distribution of the disposable income (GINI coefficient of 39 in 2011 compared to 48 in 1998)
 - But: a more equal society has not been reached in a sustainable way, e.g. by providing a high-quality education
 - Too low to function as a source of funding for domestic investments
 - Saving does not make sense
 - Investment opportunities are important to be looked at (market distortions in real estate, automobiles, electronic devices)



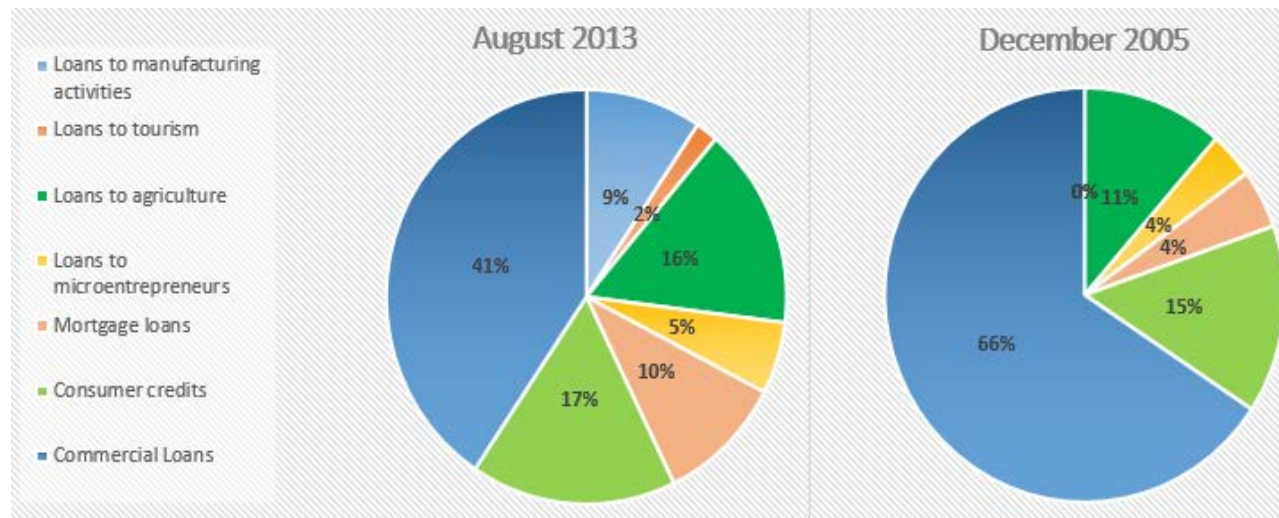
The institutional structure

- Development of the Venezuelan banking sector



The institutional structure

- Policies and regulations affecting the banking sector
 - Limits in the bank's collocation of foreign money
 - caused interventions and liquidations by the Sudeban
 - Regulation of the loan distribution to some economic sectors, “gabetas creditices” → shift in the distribution of the banks' loan portfolio
 - Regulation of the maximal interest rate for lenders
 - need for intervention by the BCV → domino effect





The institutional structure

- The Banco Central de Venezuela
 - Part of the pro cyclical economic policy
 - No pursuit of price stability
 - Source of funds for the PdVSA and other state-owned companies
 - Mandate today: promotion of growth
 - Ownership of securities worth VEF 232 bn
 - Appointment of loyal *chavistas* in the *directorio*
- no independence
- “el banco central ha perdido el norte desde los últimos años”
- Grisanti, senior economist at Veneconomía



The banking sector

- Universal banks

- Introduction of the universal banking concept in 1993
- Biggest sub sector
- Most profitable in Venezuela and in Latin America with three top ten places in all Latin American banks after RoC

→ “la banca está en su mejor momento” – Ramirez, Prof. UCV

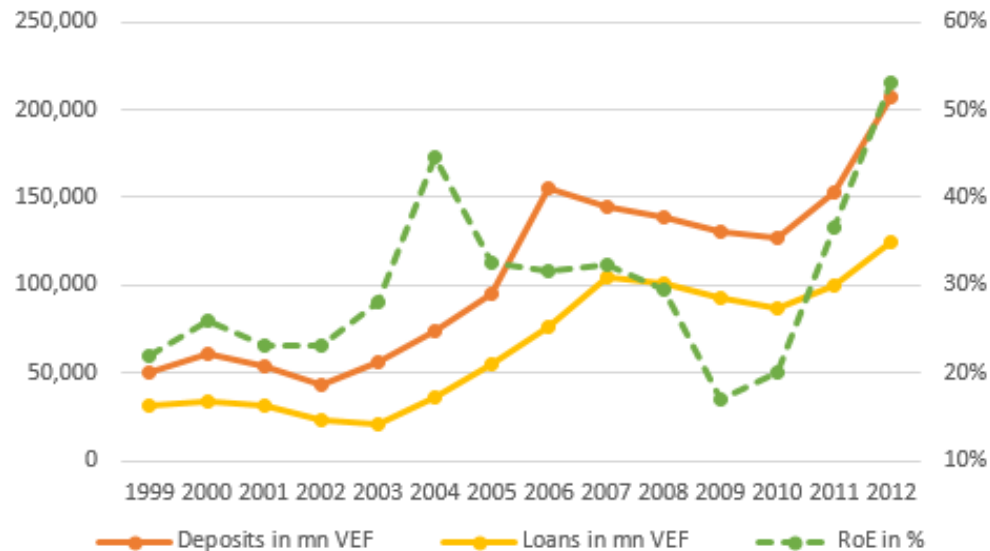


Figure: Development of loans and deposits in deflated prices and the Return on Equity



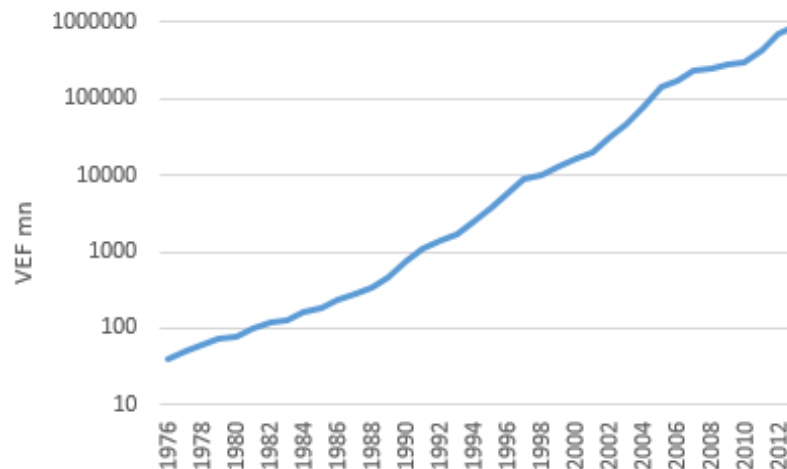
The banking sector

- Universal banks (II)

- Main reason for the inflating of the banking sector

- Regulated interest rates
- Massive expansion of the money supply → expansion of the banks' balance sheet; however: “money is now so cheap that it does not go first in investments but in airplanes and swimming-pools” - de Krivoy, former President of the BCV

→ no promotion and facilitation of productive investments





The banking sector

- Commercial banks
 - Domination of the financial system in Venezuela until 1990s
 - Drop of number of institutions from 40 in 1992 to just 1 in 2013
- Bancos con leyes especiales
 - Public institutions
 - Instituto Municipal de Crédito Popular, Banco de Comercio Exterior, Banco Nacional de Vivienda y Hábitat, Banco Industrial de Venezuela
 - Barely relevant but typical for public credit institutions



The banking sector

- Bancos de desarrollo
 - The public BANDES as a epitome (graph in VEF mn to constant prices of 2007)

ACTIVO	BANDES								Private Bancos de Desarrollo	
	2007	2008	2009	2010	2011	2012	6/30/2013	6/30/2013	6/30/2013	6/30/2013
DISPONIBILIDADES	13	281	38	11,059	11,108	13,343	11,029	28%	453	18%
Efectivo	1	-	1	0	0	8	76	0%	14	1%
Banco Central de Venezuela	1	-	20	4,336	982	5,091	3,074	8%	201	8%
Bancos y otras instituciones financieras del país	10	3	3	1	3	8	3	0%	208	8%
Bancos y corresponsales del exterior	1	278	15	6,720	10,122	8,236	7,876	20%	1	0%
INVERSIONES EN TÍTULOS VALORES	6,637	9,835	15,173	16,211	21,200	10,418	8,514	22%	1,072	42%
CARTERA DE CRÉDITOS	1,807	1,856	1,401	1,282	1,204	982	766	2%	897	35%
INTERESES Y COMISIONES POR COBRAR	178	116	113	101	207	191	209	1%	26	1%
INVERSIONES EN EMPRESAS FILIALES, ETC.	1,283	1,754	3,484	3,896	4,685	4,409	3,993	10%	0	0%
OTROS ACTIVOS	39	114	142	-	11,886	15,139	14,788	38%	86	3%
TOTAL DEL ACTIVO	9,957	13,956	20,352	32,549	50,290	44,481	39,298	100%	2,535	100%
PASIVO										
CAPTACIONES DEL PÚBLICO	-	-	-	-	-	-	-	0%	1,567	67%
OTROS FINANCIAMIENTOS OBTENIDOS	1	6,583	12,660	23,137	42,049	36,891	32,789	98%	726	31%
Obligaciones con instituciones financieras < 1a	1	30	-	34	2	753	539	2%	723	31%
Obligaciones por otros financiamientos > 1a	-	6,553	9,186	16,070	38,526	33,205	30,242	90%	-	0%
Others	-	-	3,475	7,033	3,521	2,933	2,007	6%	3	0%
INTERESES Y COMISIONES POR PAGAR	-	-	7	15	15	6	5	0%	6	0%
ACUMULACIONES Y OTROS PASIVOS	165	209	1,172	4,521	1,232	796	650	2%	42	2%
Others	-	1	1	0	15	6	0	0%	-	0%
TOTAL DEL PASIVO	167	6,793	13,840	27,673	43,297	37,693	33,444	100%	2,340	100%
Patrimonio	9,790	7,163	6,512	4,875	6,993	6,788	5,854		195	
TOTAL DEL PASIVO y Patrimonio	9,957	13,956	20,352	32,549	50,290	44,481	39,298		2,535	





The banking sector

→ Most of the public credit institutes

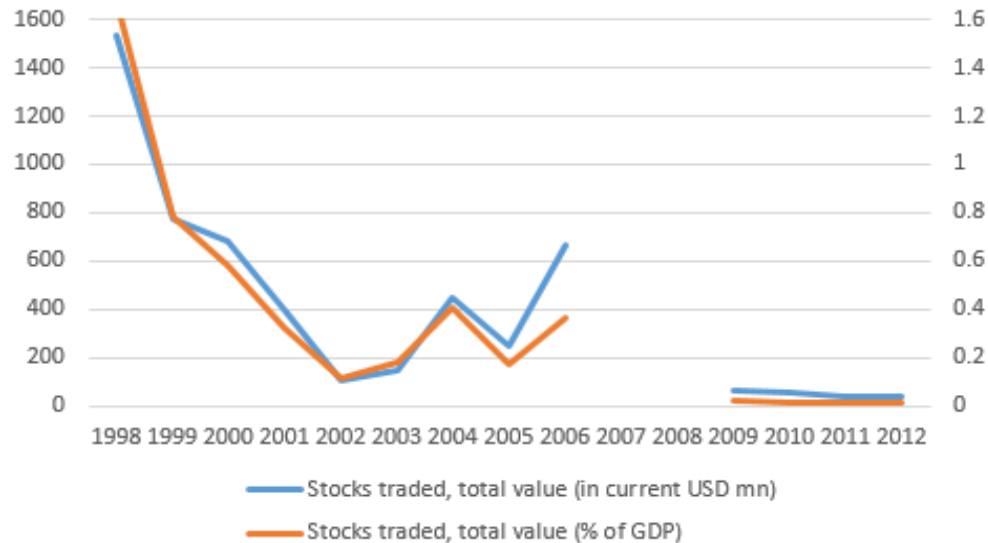
- ❖ NPL of 13.7% at the most profitable private bank Banco Bicentario vs. an average of 2.1% in private banks
- ❖ Inefficiency, irregularities combined with corruption and banking products that are far beyond the real needs
- ❖ Wrong business model
- ❖ Mismanagement
- ❖ Financial irregularities
- ❖ Barely any loans granted
- ❖ Average NPL of over 40%
- ❖ Annual losses of millions of bolivares covered by the government





The Capital Market

- Historically little attention to develop capital market; focus on banking and short-term economic growth
- Chávez: symbol of rotten capitalism and corruption
- Stock market: Drop of listed companies from 94 to 41 and drastic decrease of stocks traded
- Bond market: increase in importance due to government bonds





Recommendations for Venezuela's future

- How to promote private investments?
 - Short-term:
 - Laws to ensure property rights and to protect intellectual property
 - Reduction of the burden of government regulation
 - Revision of auditing and reporting standards
 - Strengthening of shareholder rights
 - Promotion of a flexible hiring and firing practice
 - Reduction of trade barriers
 - Medium-to long-term:
 - Establishment of a strong and independent BCV
 - Dollarization of the local currency
 - Establishment of a government pension/ oil fund
 - Fundamental change of the state and the Venezuelan society





Discussion

- How is it possible to change the state and the Venezuelan society fundamentally?
- What role can the elites play in guiding Venezuela? What's different than before?



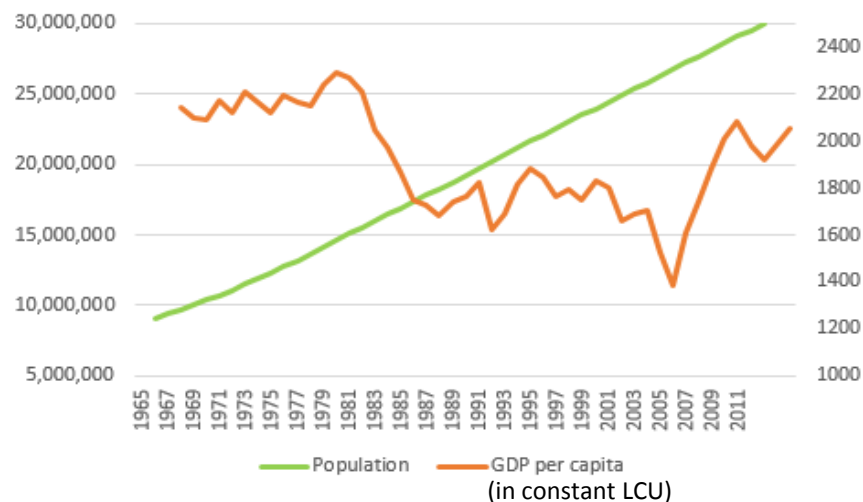
Annex: Investments

- Determining Factors

- The Exploitation of the Oil Deposits

- Not enough investments made to at least maintain the current oil production and to exploit the oil deposits efficiently

- The Population Development



- Political Decisions

- Broken promise of “sembrar petroleo”



Annex: Investments from an economic perspective

- Capital Exports and Imports

- Capital Flight due to confidence crisis in the Bolivar - countervailed by capital imports until around 1998
- Illegal capital flights of in total USD 3.8 bn from 2001 to 2010
- Decrease of FDI from USD 4.7 bn in 1998 to -2.6 bn in 2010; in 2013 recovery on a low level
- Foreign Exchange reserve melt down from USD 42 bn to 21 bn

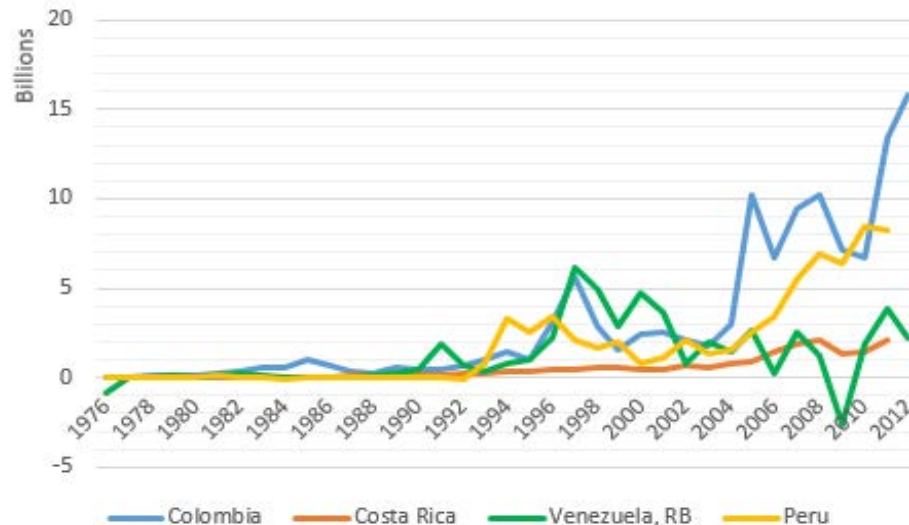


Figure: Development of FDI in current USD



Annex: Savings from a business perspective

- Corporations
 - Managed against all theoretical concepts because of Venezuela's macroeconomic idiosyncrasy
 - The level of indebtedness of around 50% (compared to around 100% in Latin America)
 - High payment capacity of 1.7 x their debt → idle money



Annex: Savings from a business perspective

- The Public Budget

- Explosion of public debt since 2009 to over USD 100 bn or 72% of Venezuela’s GDP; soon to be reached 100% according to experts
- Decreasing income (33% of GDP in 2006 to 23% in 2011)
- Increasing expenditures (VEF 53 bn in 1999 to VEF 117 bn in 2009)
- Heavy, protracted burden in the future

