



## Venezuela- Rise and Fall of The Economy

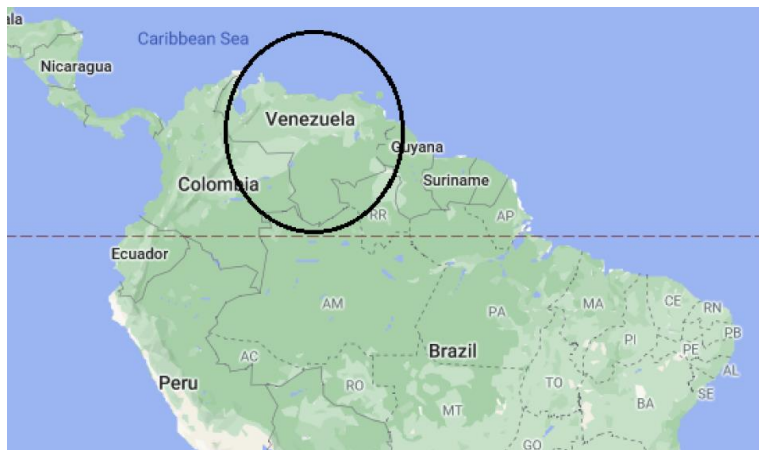
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Venezuela, a resource rich, wealthy, and one of the most highly urbanised countries of Latin America, located in the northern end of the continent of South America, bordering two seas and two countries -Caribbean Sea and the North Atlantic

Ocean, Colombia and Guyana respectively. The well-known capital of Venezuela is Caracas. Venezuela was once the 4<sup>th</sup> richest country in the world but today the Venezuelans starve for basic necessities of life like food and medicine.



**FUN FACT:** Almost every aspect of your life was once or is being dominated by the Venezuelan petroleum industry, part of every penny spent by you goes there, from your smartphones to your shoes, and from your laptop charger to your shampoos.

### Why did Venezuelan Economy fail?

Venezuelan economy failed due to three main reasons, first being decreasing production of oil, second decreasing production of non-oil commodities and third being the drawback of the economy in moving the resources to alternate industries when the oil industry started degrading.

### Venezuelan history before independence:

Venezuela became the first independent nation in South America. Venezuela, a country made up by around 1 million indigenous people following a culture known as **Timoto-Cuica**, was first colonized by the European powers in 1498 during the third voyage of Colobus, later during 1500s Spanish colonization took place and there came to be a tough competition between them of which Spain won and took power to set up various institutions in Venezuela. Key institution being Encomienda- under which the leader of the

indigenous people had to give food, mineral and labour as tribute to the colonist. Spanish colonist introduced livestock and mining in the region. Venezuelans' independence revolution begins in around 1811, led by Simon Bolivar also known as El Libertador. This independence revolution got fire by the Spanish placing high taxation and strict trade restriction, after which the Venezuelan Congress stepped ahead and formed the **Venezuelan Declaration of Independence**. Simon Bolivar even after facing several exile orders and defeats kept the fire on and formed an army named Patriots. The early 1900's was characterized by long civil wars and different government bodies and leaders were even not able to complete their terms of office due to political unrest. Venezuela formally got independence in 1830, when the **Grand Colombia Federation** was demolished due to internal and political disputes.



### Venezuelan history during Gomez dictatorship:



Venezuelan economy first discovered its oil well in 1914, named Zumaque I, in Mene Grande field on the east coast of Lake Maracaibo. During this time, the Venezuelan economy was almost dictated by Juan Vicente Gomez-which had the ability to stabilize the country, offering foreign investors firm trust over the economy.

Venezuela lacked skilled labour, knowledge and capital. Due to these reason Gomez gave opportunity to foreign oil companies-**Shell, Chevron and bp**, to research, drill and extract oil without imposing taxes and royalties, these countries also brought foreign investment and by which Gomez also gave oil concessions. During 1900's Venezuela became one of the founding members of the OPEC organization along with Iran, Iraq, Kuwait and Saudi Arabia-the major oil exporters, to control and influence the oil prices around the world.

The next twenty-one years were the golden years of the resource rich country, as it became the second largest oil producer in the world and 90% of the country's export constituted of oil. In the process, Gomez kept prioritizing himself and his loyalties first by feeding them first. This inequality turned out to be harmful for the nation's growth as it exploded the growing social conflict and created imbalances in the political system.

Now, the question is that in what ways did it impact the overall economy?

These levels of oil production generated 2/3 of the government's income. The Venezuelan economy proved itself to be an example of "**resource cursed hypothesis**" which is when the natural resources of a nation become harmful for the country's development.

An economy of services emerged when the first bank of Venezuela opened and provided exceptionally high wages. The then farmers of Venezuela started leaving their inherited lands to go to cities to earn high from the oil money. This was the time period around 1929 and 1943, when the oil prices rose high abruptly and also the Venezuelan Bolivar value rose by 70% making it one of the strongest currency in the world, this had two significant impacts, firstly it made the cost of

imported goods cheaper and secondly it made goods being exported expensive which in turn has two impacts on the country's producers and consumers that is the producers think they can't export anything for cheap so production falls as demand for goods in international market falls because of its high prices, and consumers think that the foreign goods are the cheapest to buy so the demand rises for the foreign good. This was also the period of Great Depression so during this time the United States made its currency to fall against all other currencies in the world.

The result of this was that Venezuela started to import modern and luxury goods and the economy became highly dependent on oil and it can be assumed that Venezuela was moving towards being a completely specialized economy of oil. It was catching the economic effect called Dutch disease-an upsurge of a singular resource leads to strengthening of the nation's economy alongside making other industrial sectors less competitive. In Venezuela the agriculture and manufacturing sector suffered. By the year 1940, Caracas, the capital of Venezuela, became the world's most expensive city to reside in and was treated as the **dictator's paradise**.

### Venezuela after Gomez dictatorship:

After Juan Vicente Gomez died in 1935, he became one of the richest men in Latin America-owning monopoly power over many industries, owning large patches of land, by this he created the first army in the country to handle opposition oppressions. This was also the period when the world started recovering from the Great Depression but their occurred a political unrest in Venezuela, since people their demanded a democratic government and needed a better return on the exploitation of oil. And when their demands



were not fulfilled it also led to a labour strike in 1939. This was it time when they had no certain rules for the oil industry as the previously implemented Hydrocarbons Law and Income Tax Code were questioned. Changes were made to the Hydrocarbons Law, which made a base for the domestic refining of oil. In 1956 the Venezuelan government established the Venezuelan Institute of Petrochemicals in line with the hope of redeveloping the petrochemical industry.

After the following unrest and during the World War II, Madina took over the power and tried persuading President Roosevelt for help since Mexico completely nationalized its oil industry, in response President Roosevelt sent his advisory team for legal matters to help Venezuela which led to formation and implementation of a new oil law named as **Fifty-Fifty Principle in 1943**, which made the state the owner of fifty percent profits from the oil industry. But there happened to be a problem with this law, this made the Venezuelan oil industry less profitable than the Middle-Eastern Oil Industry for which a formal negotiation request was sent to the Middle-Eastern industry by which they too adopted to the Fifty-Fifty Law, which stabilised the profits from the oil industry in Venezuela as well.

A geopolitical conflict occurred in the middle-Eastern countries, which led to Egypt closing the Suel Canal and Iran nationalized its oil industry, which eventually made Venezuela earn a lot of foreign currency during that period. The public again took the charge and asked the government to rightly utilize the excess oil revenue, in response the government provided high subsidise to the gas prices making gas the cheapest for the Venezuelans and high revenue went into the military which made the Venezuelan military rule their nation for few decades ahead, after removing Madina from power.

They later reinstalled a dictator to the country named Perez Jimenez who ruled much like Gomez but during his term of office, Venezuela became richer, there were almost no taxes and regulations and contained rich population, which attracted the Western Companies into the country and they were permitted to do business as they wished to until it affected Jimenez power. With this, Jimenez saw a very wealthy nation coming ahead and therefore the nation was renamed to Republic of Venezuela. The republic of Venezuela was now becoming equipped with modern infrastructure, houses for poor, genuine corporate loans, schools, hospitals and luxurious hotels and restaurants.

What could be the expected alarming impact of this? The large business projects got corrupted, people believed that it's okay to bribe the authority and get done with their work since the authority only wanted to be richer and it was less costly to bribe the authority than investing in project. The public company started to fail, and social programs lacked desired efforts and Jimenez was not able to fulfill the promises he made to the military due to which the military power removed him from his office. The Venezuelan economy was flooded with hyperinflation due to high currency value of bolivar. Venezuelans only aimed at scoring high paying government job, there stood no competition among employees, it only had less of hard work compiled with high wages. Later, due to non-diversified Venezuelan economy, people started losing jobs and remained unemployed since the oil industry had high dependence and less to offer the Venezuelans. The agricultural sector suffered since high inflation rates forced the economy to set food rates at low prices, which almost removed the already low profits of the sector.

In the next decade there came many leaders and democratic setup, all tried expanding the oil revenues which led to formation of OPEC as the first petroleum cartel in 1960 which favoured the nations to set the oil prices rather than the oil companies. President Perez came in power during 1970's, he mandated for the public authorities to provide jobs, increased wages, The social spendings were way to high. The middle-eastern countries specially Israel involved in geopolitical conflict that hyped the oil prices to \$14 a gallon which tipped the Venezuelan oil profits which was too much for a small country like Venezuela to absorb, this situation called out **emergency** state to curb uncontrolled hyped inflation. With this bank kept the loan rates low to let people take out money and spend it even more. Hyperinflation rose by almost 12% every year and the middle-class range grew to 58% of the population in Venezuela. The giant businesses were dependent on government subsidies, most of the small business got bankrupted. 9% of the businesses made 75% of the goods in the economy.

#### **PDVSA:**

PDVCA is a step taken towards nationalizing of the oil and petroleum industry in 1976 and dissolved the state-owned company responsible for exploration which was done keeping in view that Venezuela will become the richest economy in the world. During year 1973, Venezuela exported 3.5 million barrels per day but by end of 2020 the



### **Arrival of Black Friday:**

February 18, 1983. Even after the storm Venezuela was facing, no one thought of what would happen if the oil prices fall.

And the unfortunate happened, Venezuelan economy got into huge debts. The government tried and took steps ahead to nationalize the petroleum industry but the falling oil prices during 1988. The government tried to not remove subsidies and investments, which in turn led the Venezuelan economy in great debts. Here comes the new President Luis Herrera Campins who tried to float the petroleum industry profits to get the nation out of foreign debts, which led to drainage of the only income the country was dependent on which devalued the Bolivar, to which a new exchange organization- Recadi- responded by fixing the bolivar exchange rate to 4.3-6 bolivar per dollar. The impact of this was huge, now the high cost of living standards became unaffordable. The Venezuelans did not follow any saving policy, which further led them to get even more involved in unethical and unlawful activities like corruption and bribing, they sold in black markets to earn higher returns and stored a lot more than needed in fear of future shortages, which led to of course shortage of commodities, they even smuggled them to neighbouring countries.

The economy contracted by 10% in 1989. The currency lost faith in international market and its value dropped down by 60% when Perez took away powers from Recadi, he did not pay debts, lifted price control and increased gas prices also decreased social spending. He ordered the military to take control over the riots happening, which brought us the death rates.

A new military leader was elected during the period (1998) who was born in poverty and so believed in democracy and socialist society, Hugo Chavez's. He formed a secret socialist military unknown to the dictator. Later the Venezuelans brought Chavez's into power by allowing him to make changes to the constitution, after which Chavez's changed the name of the country to Bolivarian Republic of Venezuela. He privatized some of the sectors like agriculture and also brought the petroleum sector under state control by enforcing 49 new laws under Bolivarian Revolution. The oil industry went into disguised privatisation as it needed investment, for which the foreign countries were allowed to interfere in the country's oil industry.

Thousands of PDVSA employees went on strike and protested against Chavez's when he

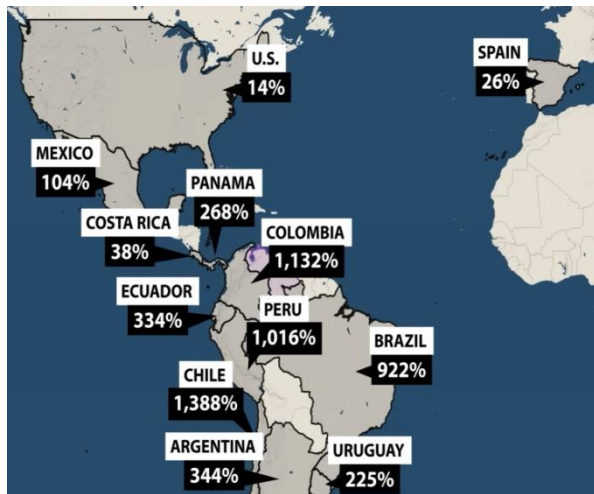
appointed new members to the board of the company which did not even had experience, Chavez did so because the government's revenue from the oil industry kept on declining even if the industry was growing. In response to the protest, under Chavez's presidency around 20,000 employees were shot dead and were called the supporters of enemies of the nation.

The Venezuelans got really worried about their future in this country which made them to establish a new currency exchange body in the country called Cadivi, so they could exchange their currency for other stable currencies. Venezuela came under the same vicious circle again, where the banks started offering loans at very lower rates and again the Venezuelans started to spend more and save less. But one fortunate thing this time was that the economy stabilized this time unlike the 1980's.

By 2008 the price of oil increased by 600%. But Chavez like other leaders did not save the oil revenues but instead utilized them in various giant socialist agendas, like he brought thousands of doctors all the way from Cuba, provided high paying jobs to poor, established schools and hospitals, etc. Venezuelans again thought that their lavish days of the 70's came back under Chavez's rule.

### **Inflation reached 65,000% by 2019.**

By the end of Chavez death in 2013, Venezuela as a state owned the highest profits an oil rich country ever held which was around 90% of profit from each barrel of extracted oil, under Chavez's principle of 21<sup>st</sup> century socialism. Chavez just like all previous capitalist leaders did not invest in productivity of the companies in the economy, nor agriculture sector goals fulfilled and he did not care how the Venezuelans were spending their money. The black-market rates were so low that people automatically dwelled into illegal activities. The economy market to black-market rate lied almost in the ratio 400:1. Venezuelans just ruthlessly spent money in satellite TVs, cosmetic surgeries until the 2008 economic crisis came up when the oil prices fell down again and Venezuela did not have money to import basic necessities which it did not produce like food. The irony is that, Venezuelans did not have enough fuel to survive, but the fact that they have the largest oil reserves in the world. And people survive on Food not Crude oil.



Chaves's successor, Nicholas Maduro, followed and worked on the ideologies of Chaves, even after having complete knowledge about the declining oil prices which further led to exodus of Venezuelans from the country, collapse of public services, shortage of basic necessities and poverty drastically increasing. In 2015 Venezuela had more than 30.1 million people but by the end of 2020, it was left with only a population of 28.4 million people.

All this had the worst impact someone could ever imagine on the Venezuelans.

It had a bad political system throughout the 1900's which led to its constant declines since the government in power was corrupted and focused on maintaining position and wealth. In the 2000's the government did not make up to its expectations. The **United States Human Right Abuse Report** on Venezuela, July 2019, issued a report stating evidences that security forces under Maduro government committed around 6800 extrajudicial killing from January 2018 to May 2019.

Venezuela was so highly triggered by the 2014 oil shock that even when the global oil prices rebounded, Maduro government was too slow to address the issue and blamed the country's downfall on a foreign economic war. Even when efforts were made to introduce new digital currency in the economy- **Petro in February 2018**, it failed. The economy contrasted and hyperinflation was relieved including the prices for necessities became affordable. The people of Venezuela failed to keep the checks and balances of the government. The Venezuelans did not know how to utilize the abundant oil revenue for the purpose of saving and investment. But their choice of cosmetic surgery was a smart investment.

People tend to ignore the macroscopic view of the economy or the international political and so did the Venezuelans when Maduro came into power and the nation's wealth started to decline. Since Maduro unlike Chaves set in conditions of declining oil prices had to withdraw many social programs, started receiving a lot of backlashes from its own ministers and was accused by the opposition (Democratic Unity Coalition) of

manipulating the supreme court orders for holding power in the nation.

A power struggle started in Venezuela, when Maduro ignoring the opposition demands declared to constitute the establishment of a constituent assembly. Maduro, in an attempt to control prices, also set the exchange rate in the nation in such a way that did not align with the prevailing international exchange rate.

The covid-19 had a significant impact on the economy of exacerbating economic challenges. Since Venezuelans were prone to informal, crowded sectors of job, it was difficult for them to obey the covid-19 norms. The Maduro Government turned routinely towards its international financial bankers- China, Iran and Russia for loans since private creditors were unable to purchase Venezuelan debts. The government also imposed many prices control equipment on basic food items, increased gas prices for the first time in two decades and lifted long standing bans on gold, Diamond mining in the Amazon River, though illegal mining was already happening there. These measures helped the poverty level to decline by 50.5% in 2022 and the economic growth was of significant 6%. The government narrowed the budget deficit from 30% of GDP in 2018 to 4.5% of GDP in 2021.

During 2022, around 7.7 million Venezuelans required medical assistance but the health sector collapsed much before covid-19. Diseases such as diphtheria and measles became a major concern. Houses did not have liable access to clean water. The United Nations launched **2022 Humanitarian Response Plan for Venezuela** on August 15 requesting for \$795 million in funding.

Subsequent U.S. sanctions on the Venezuelan economy targeting the government,



central bank, gold mines, restricted Venezuela's access to the U.S. U.S. imposed several sanctions on Venezuelan economy and individuals as well-Obama government sanctioned Venezuela on the basis of human rights abuse, corruption and antidemocratic actions. The broad aim of Trump's administration on Maduro's extra authoritarian activities was to allow for free and fair elections by cutting off his revenue from different sources. Four significant sanctions made were-Visa Revocation and Sanctions on Individuals (Jan 2019 to August 2020), Financial Sanctions (August 2018 to March 2019), Sectoral Sanctions (November 2018) and Sanction on Maduro's Government (August 2019). The sanctions relief under discussion may open the U.S. and European roots for Venezuela to trade allowing greater economic growth.

The fact that half of the economy still lives in poverty cannot be ignored. And is accompanied by illegal and immoral activities like illegal gold mining, human trafficking- criminal groups sometimes in collaboration with corrupt officials, involve themselves in within the country women trafficking rural to urban areas to serve as prostitutes and to other close by nations as sexual slaves, children are forced into labour and men are also sold the same way. The U.S. department of State ranked Venezuela as Tier 3 for the ninth consecutive year in its June 2022 **Trafficking in Person Report**, and people also get into money laundering and asset forfeiture. The U.S. also extends its concern towards Venezuela not cooperating fully with united states antiterrorism efforts since 2006 which is pursuant to section 20A of the Arms Export Control Act, this kind of a response **prohibits** all U.S. commercial arms sales and retransfers to Venezuela, the most recent of which was made in May 2020 and published in June 2, 2020.

During 1973, Venezuela exported 3.5 million barrels per day but by the end of 2020 the amount dropped to less than 6 lakh barrels a day even after it is well proven that Venezuela has more oil reserves than any other country in the world. If Venezuela gets back to pumping 3.5 million barrels per day it would still take over 237 years for the country to run out of oil. Since 2021 Venezuelan economy has begun to contract and stabilize a little bit leading to stairs of growth again but it will take a long time for the Venezuelans to climb up the deep Wells of oil it got itself into.

Venezuela has an **idiosyncratic feature** of oil industry which makes the specialized inputs and necessary institutions not valuable for production of other commodities or sectors like the agricultural

sectors. Because of which it was difficult to shift away from oil industry during times of oil price depreciation. Still, Venezuela needed to be more diversified in terms of the sectors it incorporated specially it should have been self-reliant for basic medical and food commodities.

**SOURCES:**

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