# *The New Venezuelan Exceptionalism*

Partnership for Effective Public Administration and Leadership Ethics Issue Brief

Dorothy Kronick | January 23, 2020

From a distance it might seem that Venezuela fits neatly into a narrative about all of Latin America in recent years. After a golden decade of economic expansion beginning around 2004, the crash of commodity prices hamstrung economic growth across the region; the economic slowdown together with pervasive corruption spawned protests, strikes, even riots, and dramatic anti-incumbent upsets in elections from Brazil to Argentina to Mexico [Monaldi, 2019]. Venezuela, too, enjoyed a wild consumption boom beginning around 2004. Venezuela, too, suffered an economic downturn following the collapse of oil prices in 2014. And Venezuela, too, has been racked by protests, and is filled with voters who would like to oust president Nicolás Maduro.

But in fact, Venezuela is an outlier. While economic growth has merely slowed across the rest of the region, the Venezuelan economy has shrunk by more than 65%—the worst economic collapse on record in Latin America [Rodríguez, 2019a]. 65% is a lot. During the Great Depression, the U.S. economy shrank 26% [B.E.A., 2018]. After the fall of the Soviet Union, the Russian economy shrank 38% [Feenstra et al., 2015]. The Venezuelan economic crisis is so severe that the World Bank created a special "Latin America Without Venezuela" category for its glossy reports on regional economic performance [Monaldi, 2018b]. As one Venezuelan journalist put it, "commentators have long run out of superlatives to characterize the scale of the crisis" [Toro, 2019]. The human costs—hunger, illness, death, the suffering of millions of children—have been chronicled in a series of increasingly devastating reports from Anatoly Kurmaneav of the New York *Times* [Kurmaneav, 2019b,d,a,c, Kurmaneav and Herrera, 2019a,b]. The details are too painful to quote.

What went wrong? In this issue brief, I explain that the Venezuelan economic catastrophe is really two crises in one. The first began in earnest when the 2014 oil-price crash caught Venezuela unprepared: unlike many other oil economies, Venezuela had insufficient savings, inordinate levels of debt, and inadvisable (to put it mildly) policy responses to its new economic reality. But oil prices bounced back two years later—and the Venezuelan economy did not. As Rodríguez [2018] has argued, the divergence between oil prices and Venezuelan economic performance is difficult to explain without considering U.S. sanctions. This was Venezuela's second crisis: international economic isolation that has devastated the economy and, two years in, shows no signs of producing the political change that Venezuela so desperately needs.

## *Part I: The Classic 80s Crisis*

Between 2003 and 2012, Venezuela enjoyed the largest economic windfall in Latin America and the largest in Venezuelan history [Kronick, 2014]. The oil price soared and dollars poured into government coffers. But rather than save, the government of Hugo Chávez spent the bonanza on consumption [Rodríguez, 2008]. If the Chávez administration had followed the rules set down by the previous administration, Venezuela's rainy-day fund would have had been flush with hundreds of billions of dollars by the time oil prices crashed in 2014 [Toro, 2016]. Instead, reserves were perilously low and the government was heavily indebted. As the price of the Venezuelan oil basket fell by nearly two-thirds, from $95 per barrel in 2013 to $32 per barrel in 2016, per-capita GDP fell by half.

There was a time not so long ago when this type of boom and bust was typical of oil economies [Karl, 1997]. During the oil boom of the 1970s, for example, few oil exporters saved; when oil prices crashed in the 1980s, many oil economies crashed, too. But by the 2000s, this boom-bust cycle was no longer typical. Policymakers around the world learned to save when oil prices were high, building up reserves that could be used to fill in the gaps when oil prices inevitably declined. When oil prices fell in 2014, Venezuela was no longer the victim of a prevalent oil-economy disease—instead, Venezuela was "the sick man of OPEC" [Monaldi, 2018c].

Figure 1 illustrates this point. The shaded regions mark periods of sharp declines in oil prices. In the 1980s, the Venezuelan economy shrank along with that of fellow OPEC members Algeria, Indonesia, Iran, Iraq, Nigeria, and Saudi Arabia. (These are the six oil economies that (a) joined OPEC before 1972 and (b) have GDP series available beginning in the 1960s.) But when oil prices fell again in 2014, other countries were prepared. Venezuela was not.

Bolivia provides another illustrative comparison [Zambrano, 2013,

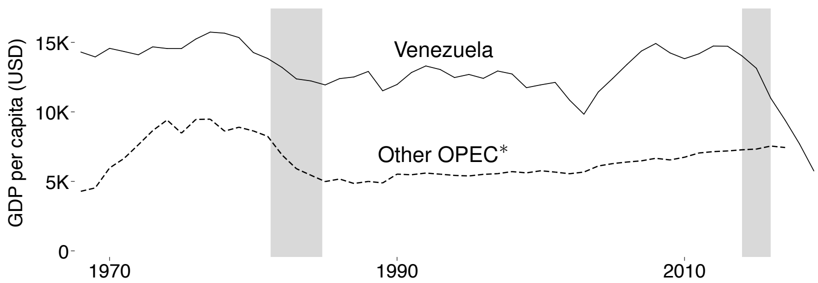


Figure 1: The shaded regions mark periods of sharp declines in oil prices; the lines plot real per capita GDP, in Venezuela and for an average of six other OPEC countries. In the 1980s, Venezuela experienced recession along with many other oil economies; by 2014, other countries had learned to save, making Venezuela "the sick man of OPEC" [Monaldi, 2018c].
*"Other OPEC" denotes the six oil economies that joined OPEC before 1972 and have GDP series available beginning in the 1960s: Algeria, Indonesia, Iran, Iraq, Nigeria, and Saudi Arabia. Source: World Bank.*

Kronick, 2014, Toro, 2017]. During the commodity-price boom of the 2000s, Bolivia's president Evo Morales resembled Hugo Chávez in many respects. They were allies. They used similar rhetoric: anti-elite, anti-imperialist, at times anti-capitalist. They rewrote their countries' constitutions along somewhat similar lines. But Morales, unlike Chávez, did not follow the typical "macroeconomic populist" path [Dornbusch and Edwards, 1991]. He saved Bolivia's economic windfall, building up international reserves, paying down debt, and—until his last years in office—maintaining a fiscal surplus. Chávez could have done the same for Venezuela. He didn't.

The causes of Venezuela's 2014–2016 economic implosion go beyond Chávez's macroeconomic mismanagement. His successor, Nicolás Maduro, turned out to be a worse president than even the most pessimistic observers (myself included) could have anticipated when he took office in 2013. Even conditional on the precarious fiscal situation that Maduro inherited, he could have taken steps in 2013 and 2014 to soften the blow of falling oil prices; instead, he doubled down on a byzantine tangle of controls, subsidies, and corruption that starved the Venezuelan economy of what little cash it did have and generated a retro problem that the rest of the region had long learned to avoid: hyperinflation [Kronick, 2015, Toro, 2018].

## *Part II: The Mystery of the Missing Imports*

Part One of Venezuela's economic catastrophe is thus sad but not mysterious. Dornbusch and Edwards [1991] long ago documented the destructive effects of "an approach to economics that emphasizes growth and income redistribution and deemphasizes the risks of inflation and deficit finance, external constraints, and the reaction of economic agents to aggressive nonmarket policies" (p. 9). The story of Venezuela's 2014–2016 recession thus follows the contours of a well-worn tale—even if it was anomalous by the time it happened, a 1980s drama playing out in the 2010s.

What happened next was different. Beginning in 2016, oil prices quickly recovered, doubling over a span of just two years. One might have expected the Venezuelan economy to rebound, too. Instead, the economic collapse accelerated.

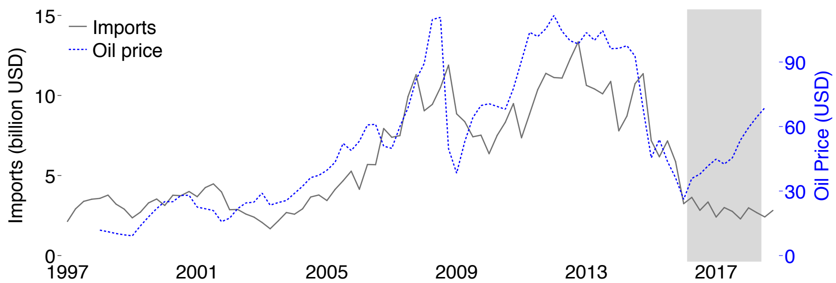


Figure 2: This graph plots the price of Venezuelan oil and Venezuelan imports (the principal source of domestic consumption). Between 1997 and 2016, imports tracked the oil price; after 2016, imports tanked even as the oil price recovered. *Source: Rodríguez [2018], BCV.*

Figure 2 illustrates this divergence. Between the 1990s (if not before) and 2016, imports—which constitute most of what Venezuelans consume—closely tracked the oil price [Rodríguez, 2018]. During the great recession of 2008–2009, for example, imports collapsed with the price of oil and then quickly bounced back. But in 2017–2019, imports kept collapsing even as the oil price rose.

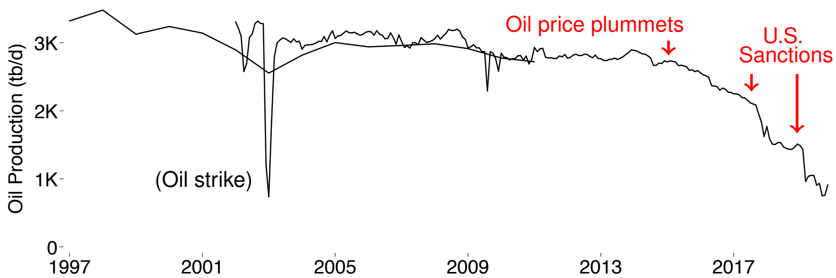


Figure 3: This graph plots Venezuelan oil production from 1997 through 2019. After a long slow decline under the Chávez administration (1999–2012), oil production dropped quickly when oil prices plummeted in 2014; when the U.S. imposed financial sanctions in August 2017 and oil sanctions in January 2019, production plunged twice more. *Source: Rodríguez [2018], BCV.*

The proximate cause of these missing imports is clear: oil production toppled, and rising prices don't help an economy that can't get the oil out of the ground. Figure 3 plots oil production over the same period shown in Figure 2 (1997–2019); after a long slow decline during the Chávez administration (1999–2012), production dropped faster beginning in 2014, when oil prices fell by 50% over just two months. As Rodríguez [2019b] observed, production slumps during periods of low prices are not surprising: production also declined (at a similar rate) in Colombia, Mexico, and other oil producers during this period. What is unusual is that Venezuelan production did not tick up again when oil prices rebounded. Instead, Venezuelan oil production plummeted twice more: after August, 2017, when the United States imposed financial sanctions, and after January, 2019, when the United States imposed oil sanctions [Rodríguez, 2019b].

Beyond the highly suggestive time trend in Figure 3, there are good reasons to believe that U.S. sanctions contributed to the decline of oil production in Venezuela. Indeed, that is what they were designed to do. The 2017 financial sanctions and related measures made it difficult for Venezuela's national oil company to get the cash it needed for basic operations [Monaldi, 2018a, Rodríguez, 2019b]. The 2019 sanctions made things worse, not only preventing oil sales to the United States but also hindering sales to other countries. Moreover, other countries subject to oil sanctions have suffered the same fate: oil production plummeted after the imposition of sanctions in Iraq, Iran, and Libya [Rodríguez, 2019b].

This, then, was Part II of Venezuela's economic crisis: just when oil prices began to rise, it became very difficult for Venezuela to sell oil. In the words of one Venezuelan journalist, "The Venezuelan economy was a drunk floundering in a choppy ocean, struggling to stay afloat, begging for a life buoy. The Trump administration threw it a hammer instead" [quoted in Kristof, 2019].

## *But are sanctions working?*

Some have argued that the sanctions-exacerbated phase of Venezuela's economic contraction—and any attendant human suffering—constitute a reasonable price to pay for ousting Nicolás Maduro. It is beyond the scope of this Issue Brief to assess that argument on ethical grounds. Empirically, though, it seems that Trump administration policies have not pushed Venezuela toward political transition [Smilde and Ramsey, 2020]. One year after Washington recognized Juan Guaidó as the interim president of Venezuela, Nicolás Maduro retains de facto control of the country. Guaidó's approval ratings have fallen and his congressional majority has dwindled [Rodríguez, 2020]. Even President Trump has expressed disappointment about the apparent failures of his political strategy, claiming that

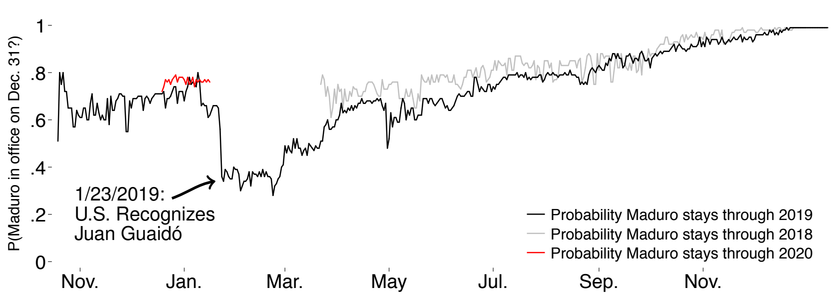


Figure 4: Using data from the online prediction market PredictIt, this graph plots the implied probability that Nicolás Maduro would remain in office at the end of each of three years: 2018 (gray line), 2019 (black line), and 2020 (red line; data through January 16). When the U.S. recognized Juan Guaidó as president on January 23, 2019, gamblers became much more bearish on Maduro's chances—but that sentiment quickly faded.

advisors misled him [Gearan et al., 2019].

Prediction markets endorse this general pessimism. Figure 4 plots the implied probability (based on betting through PredictIt) that Maduro would remain president of Venezuela at the end of each year. Admittedly, these betting markets are thin. But for what it's worth, the few people willing to put money on their predictions are no more optimistic about a Maduro exit now than they were one year ago—before the world had heard of Juan Guaidó.

## *What's next?*

Brand-new data show glimmers of hope for the Venezuelan economy in 2020. Oil production, and thus imports of much-needed goods, stabilized toward the end of 2019, perhaps reflecting Maduro's growing ability to skirt U.S. sanctions by quietly selling oil to various buyers. And ironically, the sanctions-induced economic collapse pushed the government toward (economic) liberalization: long-standing exchange and price controls were lifted, alleviating goods shortages at least in the capital, Caracas. In December, fortunate Venezuelans with savings and/or remittances from family members abroad were able to shop for Christmas gifts [Faiola et al., 2019].

There is no such hope on the political horizon. If Venezuela's calamitous economic performance compares unfavorably with that of other Latin American countries, the political landscape compares yet more unfavorably. While voters across much of the rest of the region have ousted incumbents at the polls, the administration of Nicolás Maduro relentlessly violates Venezuelans' political rights. While the tragic killing of 29 protesters in Chile made international headlines [AP, 2019], Venezuelan security forces murder thousands of civilians every year [UNHCHR, 2019], far more per capita even than the notoriously brutal Brazilian police [Correa et al., 2019, p. 166]. Under Nicolás Maduro, Venezuelans have suffered the worst wave of state violence in the region (outside of civil war) since the right-wing military dictatorships of the Cold War period. The comparison highlights a stark reversal of political fortune: once Latin America's model democracy, Venezuela is now the region's exceptional dictatorship. That seems unlikely to change in 2020. One can only hope that, as often happens, political progress takes the world by surprise.

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