V. TRADE POLICIES AND PRACTICES BY SECTOR

(1) Overview

1. Petroleum is the cornerstone of Venezuela's economy and the key to understanding its overall sectoral structure. The Venezuelan oil industry is a large, vertically integrated world leader in its field. The industry not only contributes close to 18 per cent of GDP (including petroleum refining) but also generates between 70 to 80 per cent of the country's export income. The lion's share of that income reverts to the public treasury, thus giving the State the capacity to play a pre-eminent role in the development of industrial activities, infrastructure and services.

2. The development strategy adopted by Venezuela until the second half of the 1980s, based on import substitution and State ownership, led to an industrial structure dominated by a relatively small number of vertically integrated public sector groups, with key (often monopoly) rôles for State enterprises in such fields as aluminium, steel and petroleum. Input and output prices for agricultural products, and many retail prices of food items, were controlled. The State was also a major supplier of services (including construction), whose share of GDP rose to around 60 per cent. Manufacturing expanded behind high protection to some 14 per cent of GDP, highly dependent on the domestic economy and relatively uncompetitive in world markets - petroleum refining being a notable exception.

3. Non-traded activities expanded their output at the expense of import-competing sectors, agricultural in particular. As a result, the share of agriculture in the economy has diminished and now accounts for only 5 per cent of GDP. The sector has been unable to match the wages and profitability available in other activities and has been seriously affected by exchange rate policies. Although assistance appears moderate compared with some major world agricultural producers, input protection and domestic supports have maintained an agricultural sector isolated from international markets and largely characterized by low efficiency and high costs.

4. Venezuela's import-substitution strategy involved sizable production supports and high border protection. The latter included a range of trade instruments designed to protect mainly agricultural products, although manufactures also benefited, while services and mining were subject to highly restrictive investment rules. In addition, large oil revenues gave the State the ability to subsidize downstream activities through inexpensive inputs.

5. Following the sharp fall of oil prices in 1986, the State's capacity to provide support was greatly diminished and industrial policies began to shift. A process of progressive market opening and rationalization of the import regime has been underway since 1989 and investment restrictions in several industries have been drastically eased. The programme has produced sectoral realignments, particularly in certain key industries such as steel and agriculture, which have induced the restoration of assistance by mechanisms such as debt rescheduling, revised local content requirements and variable levies. Moreover, the rollback of protection has suffered some setbacks from policy harmonization within the Andean Group.

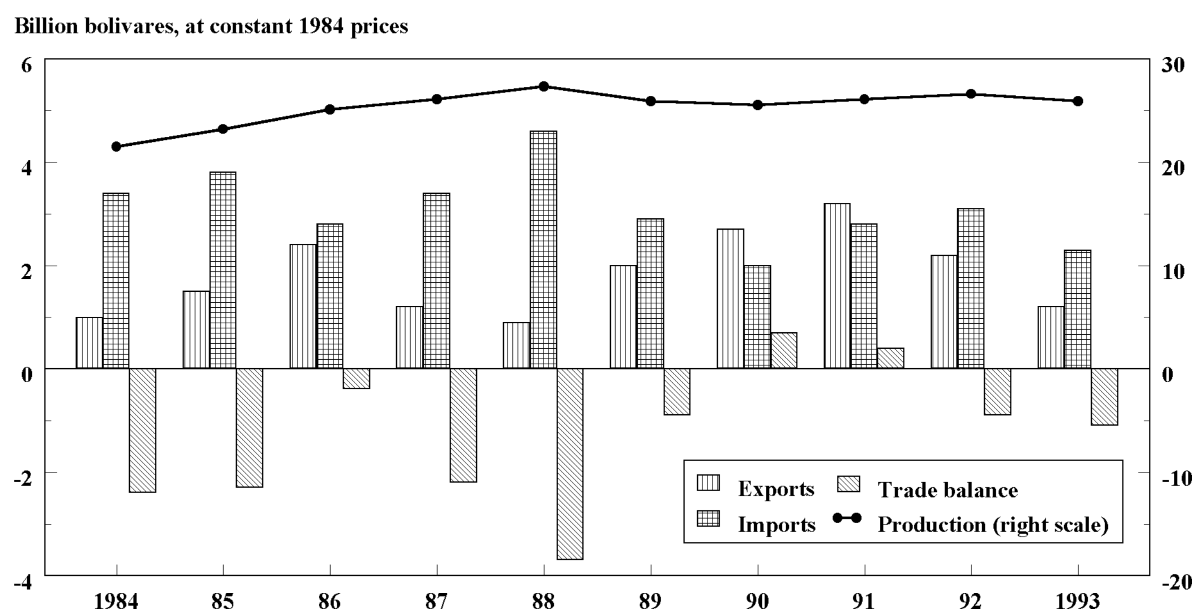
6. The general thrust of current industrial policy is to promote domestic value added. This policy is supported by tariff escalation and promotion of selected industrial "activity leader" groups. Such selective intervention could work against the improvement of resource allocation through a more neutral structure of trade and industrial policies. In the long-term the international competitiveness of non-oil sectors in Venezuela needs to be tackled with better management of oil revenues to counter the pressures they generate on the real exchange rate, as discussed in Chapter I.

(2) Agriculture

7. Agriculture employs 10 per cent of the labour force (compared to around 45 per cent in the early 1960s) and accounts for only 5 per cent of GDP. The expanding petroleum sector offered profits and wages unmatched by agricultural activities; oil income also accelerated urbanization and growth in the tertiary sector, while the policy emphasis on industrial growth coupled with upward pressures on the exchange rate from oil revenues seriously disadvantaged agriculture.[1] The sector survived on ad hoc compensatory measures, mainly subsidies, and guarantees on markets and prices.[2]

8. Higher priority was given to the sector in the mid-1980s, when a wide range of incentives was introduced and production rose significantly in real terms (Chart V.1). However, efficiency remained generally low and the fiscal cost of the incentives was high. Subsequent reductions in support and the economic recession of 1989 resulted in a sharp contraction in agricultural GDP, which a late and slow recovery has failed to restore.

Chart V.1
Evolution of agricultural production and trade



Source: Ministrio de Agricultura y Cria.

9. Venezuela's agricultural trade is small: in 1992 and 1993, agricultural products accounted for under 3 per cent of total exports and 1.5 per cent of imports. Typically, farm trade has been in deficit, but since the 1989 fall in internal demand this has been reduced or reversed (Chart V.1). In 1993, livestock activities (including milk production) accounted for 46 per cent of agricultural GDP, crops for 40 per cent and fishing for 7.2 per cent.

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[1]Up to 1989, there was also a system of multiple exchange rates which favoured agricultural imports (i.e., the exchange rate for the sector was over-valued relative to the market rate).

[2]Ministry of Agriculture and Livestock (1994), p. I-1.

(i) Institutional framework and policies

10. The legal framework for agriculture is complex; the Ministry of Agriculture and Livestock is responsible for policy towards the sector. In a statement prepared for this review, the authorities indicated that current policies seek to provide protection to food production and direct support to domestic producers; promote investment and exports; set up a safeguards system to protect domestic producers from import surges; foster the growth of the national agro-alimentary system; provide appropriate financing for production and marketing; and ensure stability in public policies through the creation of a law on agricultural development and food security.

11. In the past, government control was exerted over many farm output and input prices and retail prices of many food items. The small scale of operations and lack of technological innovation and investment resulted in low land and labour productivity. Inadequate property rights (including the lack of a satisfactory land registry system) inhibited the use of land as collateral for financing, with adverse implications for innovation and development.

12. A programme of agricultural reform was initially planned to begin in 1991 but was advanced to 1990 to address inflationary pressures arising from food price increases. The reform led to the simplification of the tariff structure, to comprise only four rates, with the maximum set at 20 per cent. As discussed in Chapter IV, there was also an elimination of import prohibitions, partial removal of imports reserved for the Government, a phasing-out of most export controls and reductions in quantitative import restrictions and tariff exemptions. Preferential exchange rates for agricultural inputs were eliminated, subsidies on fertilizers were phased out, and credit subsidies were reduced. In addition, guaranteed minimum prices for rice, coffee, corn, and milk, as well as coffee and cocoa marketing monopolies were eliminated.

13. Following the initial implementation of the liberalization programme, the Ministry of Agriculture and Livestock asserted that policies undertaken from 1989 mistakenly ignored the sector's unique characteristics and the inseparability of economic, social and political factors.[3] According to the Ministry, implementation of the reform programme led to a collapse of production in sensitive products, dismantling of the processing industry, depression in important rural regions, increased unemployment, rural exodus and an increased dependency on imported food.

14. The Ministry regards the downward trend in per capita food production as a clear sign that Venezuela's food security has been critically endangered. It believes that this trend and the deteriorating agricultural trade balance must be reversed as rapidly as possible. According to the Ministry, steps must also be taken to achieve a solid, diversified economy, including a strong agricultural sector without which, in its view, no nation has developed. In line with those concerns, and in response to the sector's criticism over liberalization, various changes have been made since 1993 that, in the authorities' opinion, would correct existing problems, particularly those affecting products considered "sensitive" and covered by the Andean System of Price Bands (Chapter IV(2)iv)).

15. The authorities have also highlighted the need to modernize the legal framework for the sector. With this objective, the draft law on agricultural development and food security, currently under preparation, seeks to integrate the sector into the international market while taking account of economic globalization and the formation of regional blocs. This should be accompanied by an efficient "trade

[3]Ministry of Agriculture and Livestock (1994), p. I-1.

defence system" and incentives to domestic production, to counteract long-term distortions in world agricultural markets and permit the preservation of domestic agriculture.

(ii) Measures affecting trade and production

16. Exports a number of agricultural items benefit from a tax credit of 10 per cent of their f.o.b value (Chapter IV(3)(x)). Some other exports are subject to licensing requirements (Chapter IV(3)(v), while banana sales to the European Union fall under a tariff quota. Venezuela is a member of the international agreements on coffee and cocoa (Chapter V(2)(iii)(b)).

17. Measures affecting agricultural imports include ad valorem tariffs and compound duties (Chapter IV(2)(ii)(b)), tariff surcharges (Chapter IV(2)(v)), variable import levies under the Andean System of Price Bands (Chapter IV(2)(iv)), while some products are subject to import licensing or prior authorizations (Chapter IV(2)(x)).

18. The main mechanism of protection for agriculture takes the form of variable levies additional to ad valorem tariffs. Such levies, introduced in 1991 as a part of a national price band system apply to imports of certain agricultural products originating outside the Andean Group. The system was modified in 1995 in the context of the harmonization of the CET by the Andean Group.[4] Under the Andean System of Price Bands, reference prices for "marker" products are used to calculate floor and ceiling import prices, which in turn serve as the basis to determine variable levies (Chapter IV(2)(iv) and IV(2)(viii)). The WTO Secretariat obtained insufficient information to permit a detailed anaylsis of this new system.

19. An analysis by Ramírez (1993) of protection provided by Venezuela's former variable levy system indicates that the levy's effects were unevenly spread across activities: from an ad valorem equivalent of 2 per cent for raw sugar to 44 per cent for milk (Table V.1).[5] As the levy came on top of the CET tariff, the combined nominal protection could be considerable. According to Ramírez, the variable levy system did not prevent a decrease in domestic agricultural prices caused by the trade liberalization programme, although it might have reduced the rate of decline. The system may also have had some partial success in dampening the variation in domestic producer prices (Chapter V(2)(iii)(b)).

Table V.1
Protection through variable levies as of August 1993
(US$ per tonne and per cent)

	Rice	Raw sugar	Refined sugar	Milk
		US$ per tonne		
FOB floor price	147	332	216	1,756
CIF floor price	164	357	241	1,906
Transport & Insurance	17	25	25	150
Variable levy	11	94	5	578
		Per cent		
Variable levy	7	36	2	44
Ad valorem tariff	20	20	20	20
Nominal protection	27	56	22	64

Source: Ramirez (1993).

[4]Decision of the Commission of the Cartagena Accord 371 (December 1994).

[5]The authorities emphasized that the national system analyzed by Ramiréz has been replaced by the Andean System and expressed reservations about various aspects of the analysis.

20. Certain consumer food items are subject to maximum retail prices and come under a monitoring system (Chapter IV(4)(iv)). Minimum prices apply to certain agricultural products considered sensitive; such prices, currently being phased out, are set through negotiations involving producers and industrialists.

21. Agriculture activities are exempt from revenue tax and tax on capital assets, while certain agricultural and basic food items are free from wholesale and consumption taxes (Chapter IV(2)(vi)).

(a) Credit

22. Between 1975 and 1988, preferential credit to the agricultural sector grew rapidly. The main institutions involved were the Farm Credit Fund (*Fondo de Crédito Agropecuario* - FCA), the Farm Credit Institute (*Instituto de Crédito Agrícola y Pecuario* - ICAP), and the now defunct Farm Development Bank (*Bandagro*). The FCA was set up in 1974 to provide medium- and long-term financing for infrastructure. It channels funds obtained from sources such as the Government, the Inter-American Development Bank and the Investment Fund of Venezuela (FIV) to official and commercial banks, rather than directly to farmers. Basic processing activities, post-harvest installations and milk cooling tanks are among the activities that have benefited from FCA credits.

23. The ICAP, also, attached to the Ministry of Agriculture and Livestock, was established in 1975 to provide credit to farmers and small producers. Funding comes from the Government and organizations such as the FCA. Credit to small producers is mainly given through programmes operated by the ICAP itself, including the *Fondo Nacional del Café* (FONCAFE) and the *Fondo Nacional del Cacao* (FONCACAO).

24. Preferential credit is provided mostly through interest rate ceilings, the establishment of minimum percentages for the agricultural portfolio of commercial banks, and an income tax exemption for banking operations related to agriculture. The concessional credit it provided resulted in strongly negative real interest rates for agricultural loans. Beginning in 1989, attempts were made to correct the situation by setting interest rates for agricultural loans at the equivalent of 85 per cent of the average market rate charged by the six largest commercial banks. However, small producers could, until recently, still benefit from ICAP credit at a rate of 3 per cent. The Government had also progressively reduced the minimum agricultural portfolio of commercial banks from 22.5 to 12 per cent, with a view to its eventual elimination. However, in April 1995 the agricultural portfolio was again raised to 17 per cent.

25. The authorities indicate that the spiralling cost of credit has led to falling investment in agriculture, with serious consequences on the production capacity of the sector. As a result, in 1994 small- and medium-sized producers were granted a seven-year debt repayment moratorium, with interest rates fixed at 45 per cent of the average rates charged by commercial banks. Through the liberalization of the legal bank reserves (*encaje legal)* held by the Central Bank, the Ministry of Agriculture and Livestock and the FCA provided Bs 25 billion to finance the 1994 winter cycle: credits were again granted through commercial banks at a preferential rate equivalent to 85 per cent of the market rate in accordance with the decree-law on refinancing.

(b) Inputs

26. Agricultural production receives support through the provision of a variety of services by public organizations, such as the National Fund for Agricultural Research (*Fondo Nacional de Investigación Agropecuaria*), which covers areas such as seed production and certification, veterinarian services and phytosanitary diagnoses. The Inter-American Institute for Agricultural Cooperation (*Instituto*

Interamericano de Cooperación para la Agricultura) is involved in policy planning, technology transfer, rural and agro-industry development and training. The National Agrarian Institute (*Instituto Agrario Nacional*), currently undergoing restructuring, undertakes land surveys (*catastros*) and development programmes to assist small- and medium-sized agricultural producers and participate in agro-forestry and eco-tourism developments.

27. Input subsidies have mostly taken the form of low-cost fertilizers, pesticides, irrigation and electricity, of which fertilizers have been the most important. Fertilizers were provided by the state-enterprise Pequiven until 1981 (Chapter V(4)(ii)(b)); that year and affiliated company, Palmaven, was subsidies to such inputs were equivalent to 90 per cent of the production cost, a policy which apparently led to significant fertilizer overuse. Fertilizer subsidies began to be reduced in 1990 and were finally eliminated in September 1993.

28. According to the authorities, the phasing-out of fertilizer subsidies led to a decrease of 48 per cent in fertilizer sales between 1989 and 1992. From 1991, a system of compensation was introduced under which the Ministry of Agriculture and Livestock provided a subsidy to cover part of the cost of fertilizer imports. Compensation was decreased annually 10 percentage points from a rate of 40 per cent between July 1990 and June 1991, and eliminated in September 1993.

(c) Assistance indicators

29. A recent study of support to agriculture in Venezuela indicates that the country provides moderate protection compared with some major world agricultural producers.[6] The results were based on the concept of the Support Indicator for the Agricultural Sector (*Indicador de Apoyo al Sector Agropecuario* - IASA), covering five major agricultural commodities (corn, milk, rice, sorghum and sugar).[7] The study found that while the average adjusted Producer Subsidy Equivalent for the whole OECD was 41 per cent in 1991, the comparable value for Venezuela was only 18 per cent.[8]

30. The IASA for the five products considered for Venezuela indicates that support was high in 1986, fell sharply until 1989, and has since edged up (Chart V.2). In money terms, total support for corn, milk, rice, sorghum and sugar was just over US$1,000 million in 1986, under US$30 million in 1989 and US$260 million in 1992.

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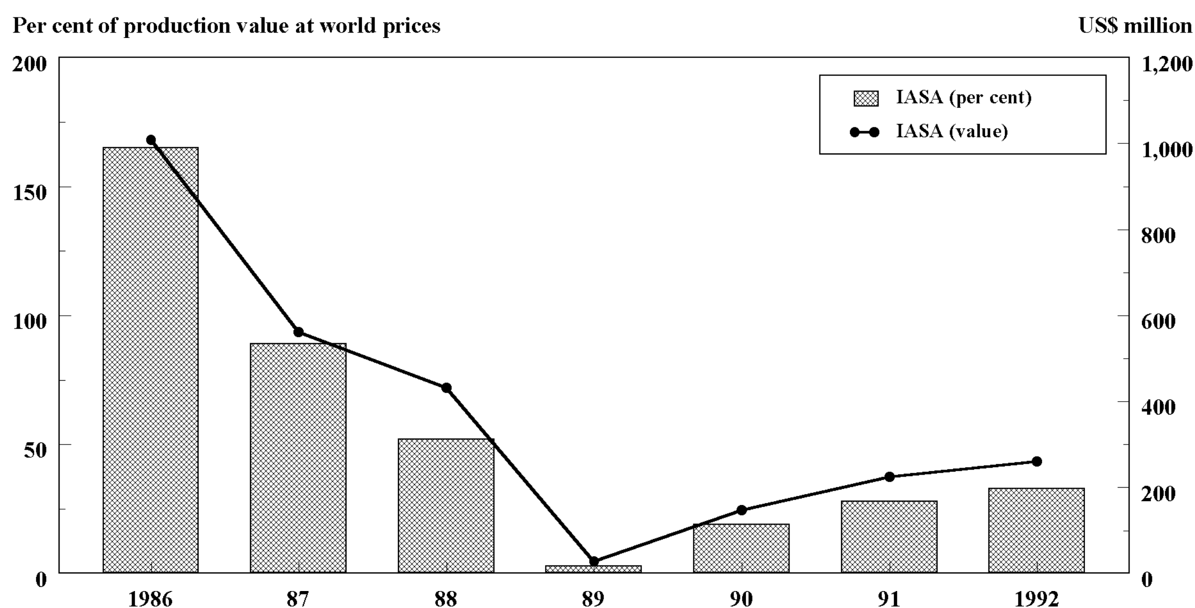
[6]Barceló and García (1993); the study, covering support to agriculture in the Andean Group, was commissioned by the Council of the Cartagena Agreement and the European Commission.

[7]The IASA is a measure of producer transfers resulting from policies affecting producer prices (including tariffs, minimum import prices, prior licensing) and input costs (fertilizers and short-term credit). The measure is equivalent to the Producer Subsidy Equivalent, adjusted by excluding aids with long-term impacts such as infrastructure investment and public expenditures in research, extension activities and irrigation.

[8]For the comparison, the OECD's Producer Subsidy Equivalent was adjusted by excluding aids with long-term impacts (see previous footnote) to make it comparable to the IASA. The following were the subsidy equivalents in 1991 by commodity, as a percentage of domestic prices, for Venezuela and the OECD (in parentheses): corn 15 (41), milk 28 (68), rice 5 (82), sorghum 19 (41) and sugar 14 (63).

Chart V.2
Total support (IASA) to main agricultural products [a]



a Includes corn, milk, rice, sorghum and sugar.

Source: Barceló and García (1993).

31. The support estimates suggest, contrary to a widespread view, that economic policies did not necessarily penalize the Venezuelan agricultural sector. While fertilizer subsidies were important in some cases, the support they provided was generally small. Indeed, the combined support given through fertilizer subsidies and credit never exceeded 10 per cent of the value of production and represent only a small fraction of the total IASA.

32. Most support was provided by internal price support measures. Accordingly, the fall in the IASA between 1986 and 1989 reflects a sharp fall in domestic prices during a period when world prices tended to increase. This underlines the substantial isolation of Venezuela's agricultural sector from the world market. Increases in support after 1989 appear related to the elimination of preferential exchange rates for food imports and the introduction of the national price band system.

(d) Uruguay Round commitments

33. In its Uruguay Round commitments, Venezuela undertook to cut financial support to agricultural producers from US$1.3 billion in 1995 to US$1.1 billion in 2004 (Chapter IV(4)(iv)). As discussed above, assistance to the sector appears to have already fallen significantly from the levels maintained during the 1986-1988 period, the base period used to calculate the initial amount of the Aggregate Measure of Support. Thus, it would appear that, provided assistance does not continue to creep up, Venezuela should have no insurmountable problems meeting its Uruguay Round support reductions commitments.

34. Venezuela's Uruguay Round commitments also include the progressive reduction of tax credits on agricultural exports: in 1986-1990, annual average expenditure on these subsidies was US$93 million, benefitting mainly bananas, coffee, fruits and cocoa (Chapter IV(3)(ix) and (x)).

35. In line with the Agreement on Agriculture, Venezuela has bound its tariffs on all agricultural products. Final rates will range from 10 to 135 per cent, with 73 per cent of lines bound at rates not greater than 40 per cent.[9] There are 74 products subject to special safeguard protection under Article 5 of the Agreement and for which final tariffs should be fully implemented by the year 2004; for all other items, bindings are applicable from 1995 (Chapter IV(2)(ii)(c)). In the context of minimum access opportunities in the Agreement, Venezuela included 62 products in its list of items subject to tariff quotas, at final bound rates set at 15, 20, 30 and 40 per cent (Chapter IV(2)(iii)).

(iii) Main agricultural commodities

(a) Livestock, meat and dairy

36. By value, livestock is Venezuela's largest agricultural group; in 1994 the value of cattle production alone more than equalled the combined value of the largest five crops. The major livestock products are cattle, poultry, milk and pigs (Chart V.3).[10]

37. Cattle production stagnated during the early 1990s, but increased slightly in 1994 (Table V.2). Cattle are subject to tariffs of 5 to 10 per cent; imports are small and highly variable, some 15,000 tonnes in 1993 and none in 1994. Beef imports are negligible; the tariff rate on beef is 20 per cent.

Table V.2
Livestock: volume and value of production

	1990	1991	1992	1993	1994
	thousand heads unless otherwise indicated				
Cattle	2,003	1,904	2,023	2,076	2,222
Poultry (million heads)	200	261	300	335	342
Milk (million litres)	1,452	1,461	1,529	1,407	1,562
Pigs	1,577	1,727	1,995	2,046	2,209
Sheep	144	151	155	…	…
Goats	707	734	742	…	…
	million bolivares at constant prices of 1984				
Cattle	7,130	6,778	7,203	7,392	7,910
Poultry	3,886	5,038	5,797	6,479	6,609
Milk	3,819	3,844	4,020	3,700	4,109
Pigs	1,200	1,314	1,518	1,557	1,681
Goats	174	181	183	…	…
Sheep	35	36	37	…	…

… Not available.

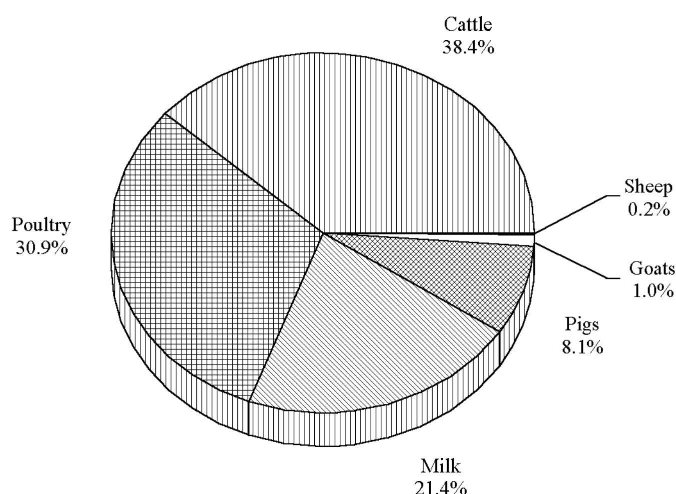
Source: Ministerio de Agricultura y Cria

[9]Part I, Section I-A, Schedule LXXXVI,Corrigendum, 25 March 1994. Of the 275 items in the schedule, 35 items were bound at rates of between 10 and 35 per cent, 45 at a rate of 30 per cent, 121 at a rate of 40 per cent, 33 at rates of between 48 and 100 per cent, and the other 41 at rates of between 105 and 135 per cent.

[10]The analysis in this and the following section is based on production and trade data supplied by the Ministry of Agriculture and Livestock.

Chart V.3
Value of main livestock products, 1992

Per cent of total value



Note: Total value was not available.

Source Ministrio de Agricultura y Cria.

38. Pig output has grown considerably but trade has been mostly small: imports came close to 1,800 tonnes in 1992 but then fell, while exports have increased from a very low base to reach 4,900 tonnes in 1994. Poultry output grew markedly between 1990 and 1994, the real value of production increasing 70 per cent during that period. Trade, however, has remained very small. According to the authorities, the industry's growth has been aided by measures taken against unfair competition.

39. Growth in both poultry and pork production has been facilitated by strong vertical integration. Both are generally produced under intensive conditions, with large scale use of high-value inputs (e.g. concentrated feed, veterinary products, etc.) and large units of production. In contrast, beef production is characterized by the use of traditional extensive production methods.[11]

40. The rapid growth in poultry production has increased availability and lowered prices relative to other meats, making chicken the most important meat consumed in Venezuela. Beef, for years the most commonly consumed meat, has now fallen behind chicken; pork occupies a distant third place.

41. Milk output, which declined in the 1980s, has tended to increase in recent years. Milk is the largest agricultural import, overseas purchases more than doubling between 1990 and 1991 when they reached 716,000 tonnes; imports fell to 379,000 tonnes in 1994. Small, variable quantities of milk are also exported (none in 1994).

[11]Marrero, Kyle and Lee (1993).

42. Milk has traditionally been the most protected agricultural product in Venezuela (Chart V.4). Practically all the assistance has derived from domestic price support measures. Thus, as internal prices fell in absolute terms and world prices rose, protection decreased, turning negative in 1989. The trend was then reversed, and in 1992 internal prices were again well above the world level. Subsidies reached that year the equivalent of US$95 per tonne.

43. Milk marketing costs in Venezuela are high, almost US$230 per tonne. Three firms control the market for dehydrated milk, the largest accounting for 60 per cent of the market. Barceló and García (1994, p. 101) link such oligopolistic structure to the relatively high penetration of imports in the market, despite official programmes to encourage the use of domestic milk.

44. Goat and sheep production increased somewhat between 1990 and 1992; trade in both products has been negligible.

45. Meat, poultry, milk and related products are considered by the authorities to be subject to particularly serious price instability or distortions and, for this reason, they have been made subject to the variable levy system (Chapter IV(2)(iv)). Dairy products are subject to a tariff rate of 20 per cent and, within the variable levy system, to a quota system. During part of 1993 and 1994, certain cheeses imported from the European Union were subject to countervailing duties.

46. Minimum producer prices are set for various milk types;[12] certain milks, cheeses, poultry and eggs are also subject to maximum retail prices.[13] Beef is subject to special classification procedures to ensure a better identification of products according to yield and quality. Foreign investment in milk dehydration is restricted (Chapter III(2)(ii)(d)).

47. The authorities have decided to renew their efforts to create and maintain the productivity and profitability of livestock activities; emphasis will be given to fostering entrepreneurial organizations and the modernization of collection, industrialization and marketing activities. As part of these efforts, the largest producer of pwedered milk has been privatized.

48. Under the minimum access opportunities of the Uruguay Round Agreement on Agriculture, Venezuela included pork and poultry in its list of items subject to tariff quotas, at bound rates set at 40 per cent. Milk, milk fat (including butter) and cheeses were also included in the list at rates of 30 and 40 per cent. Pork and poultry quotas are subject to no increases until 2004; small increases are contemplated in other quotas.[14]

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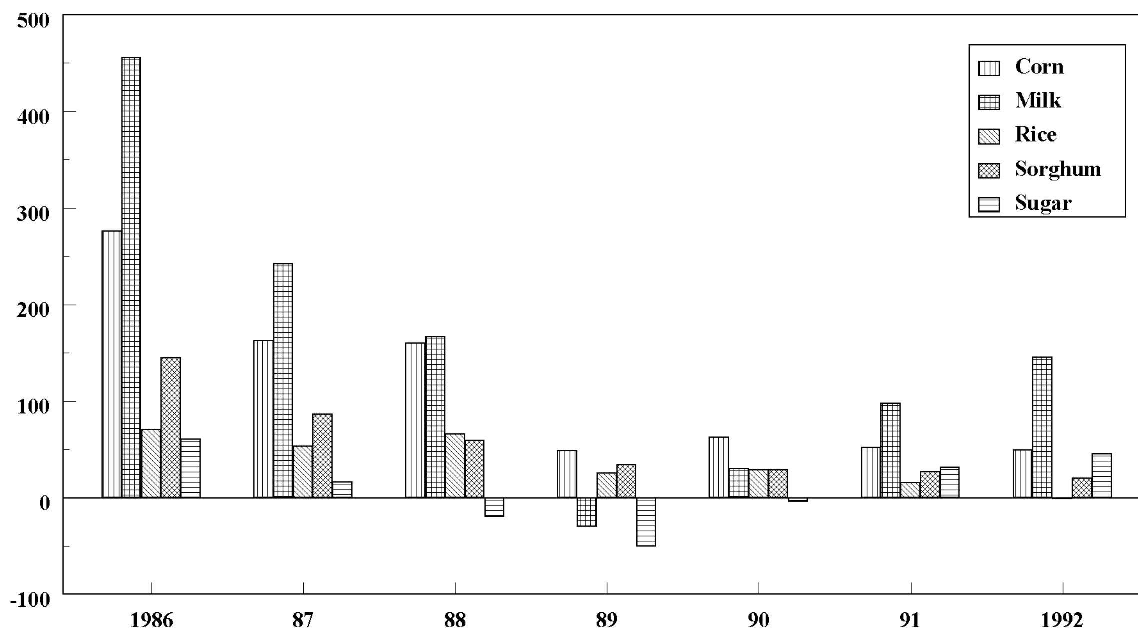
[12]Official Gazette 35560, 4 October 1994.

[13]Official Gazette 35661,25 February 1995.

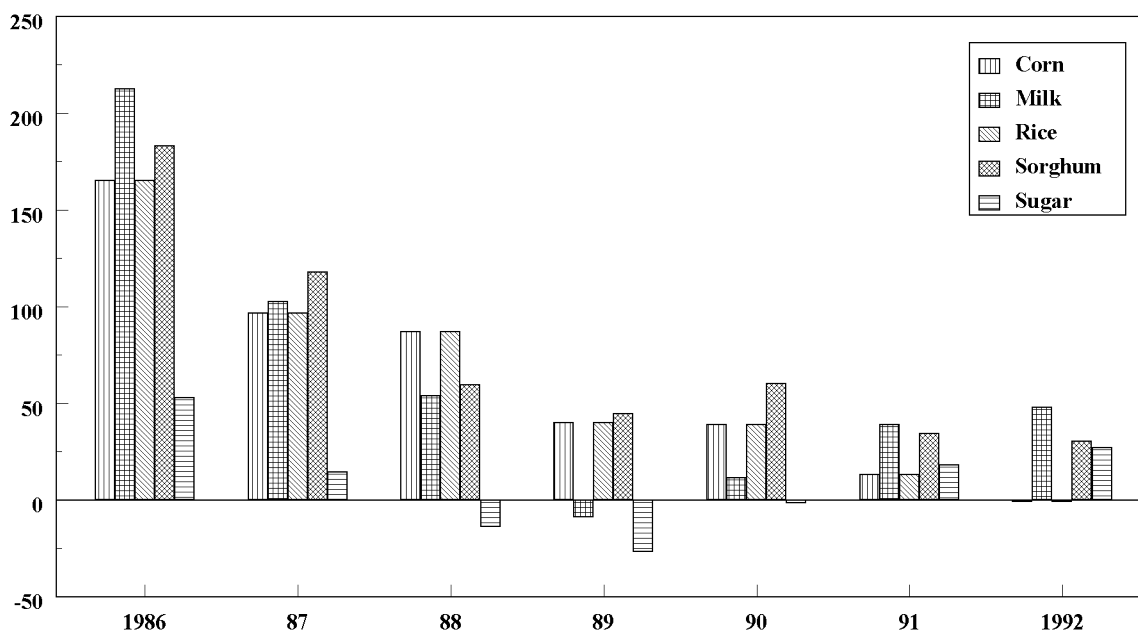
[14]Part I, Section I-B, Schedule LXXXVI, Corrigendum, 25 March 1994.

Chart V.4
Support (IASA) to corn, milk, rice, sorghum and sugar

(a) US$ million, current



(b) Per cent of production value at world prices



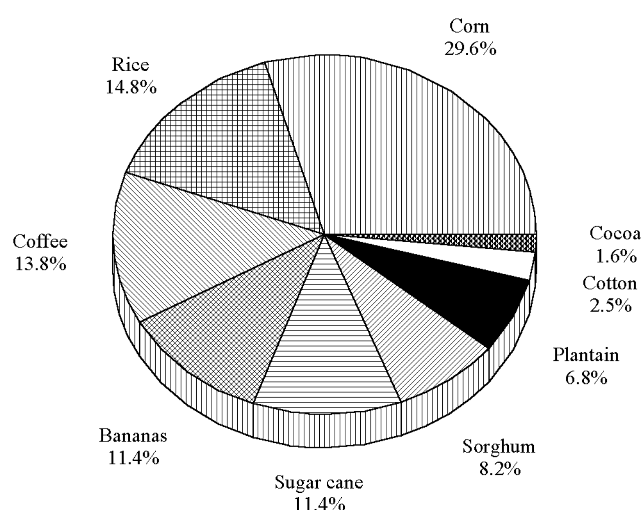
Source: Barceló and García (1994).

(b) Crops

49. The most important crops are, in decreasing order, corn, rice, coffee, bananas and sugar cane (Chart V.5).

Chart V.5
Value of main crops by product, 1994

Per cent of total value



Note: Total value was not available.

Source: Ministrio de Agricultura y Cria.

Cereals

50. Corn is Venezuela's main staple food. After significant increases, corn production tended to fall in the 1990s, although a strong recovery occurred in 1994 (Table V.3). Imports increased rapidly in 1993 and 1994, reaching 270,000 tonnes and 247,000 tonnes, respectively, up from only 2,400 tonnes in 1992. Exports varied between 312,000 and 523,000 tonnes during the 1990s.

51. Domestic corn prices were consistently maintained above world levels between 1986 and 1992, although the difference has narrowed as domestic prices have fallen and world prices increased. Corn production still benefited from considerable assistance, equivalent to some US$52 per tonne, in 1992 (Chart V.4). Of this, concessional credit contributed about 42 per cent and fertilizer subsidies some 13 per cent; the rest derived from internal price support measures.

Table V.3
Crops: volume and value of production,1988-94

	1988	1989	1990	1991	1992	1993	1994
			thousand tonnes unless otherwise indicated				
Corn	1183	921	1002	1025	852	842	1141
Rice	383	313	401	611	623	650	738
Coffee	71	73	76	73	69	66	79
Sugar cane	8333	7809	6902	7066	7128	6522	7664
Banana	…	…	1167	1215	1240	1116	1193
Sorgum	820	595	376	615	514	367	446
Plantain	…	…	507	558	568	541	535
Cotton	73	87	85	72	73	44	54
Cocoa	14	14	15	16	17	16	14
Sesame	…	…	50	45	21	14	9
Sugar	480	524	499	523	525	514	450
Tobacco	15	15	15	12	…	…	…
			million bolivares at constant prices of 1984				
Corn	…	…	2476	2531	2105	2081	2818
Rice	…	…	766	1166	1189	1242	1409
Coffee	…	…	1264	1214	1148	1100	1313
Sugar cane	…	…	980	1003	1012	926	1088
Banana	…	…	1060	1104	1127	1015	1084
Sorgum	…	…	655	1070	894	638	776
Plantain	…	…	609	670	682	650	643
Cotton	…	…	365	308	312	189	234
Cocoa	…	…	168	174	185	174	151
Sesame	…	…	197	176	83	56	36
Sugar	…	…	…	…	…	…	…
Tobacco	…	…	…	…	…	…	…

… Not available.

Source: Ministerio de Agricultura y Cria and EIU (1995

52. Sorghum production increased considerably in 1991 but has since contracted; according to official estimates, a large share of production is exported. Protection is high, with domestic prices maintained considerably above the world level. In 1992, support was equivalent to US$39.50 per tonne, of which 43 per cent was due to concessional credit and fertilizer subsidies.

53. Corn and sorghum account for some 75 per cent of the harvested area for cereals and for at least a third of the total harvested crop area. Corn is mostly produced on small farms, while sorghum production takes place mostly on medium- or large-scale units, using highly mechanized techniques. Although yields for both cereals have increased, they are still below those of the main producing countries in the region; production is vulnerable to weather conditions, especially rainfall variations. Sorghum is used almost exclusively as a feed grain, while corn has several other uses.[15]

54. Rice output fell in the second half of the 1980s, but recovered strongly in recent years, particularly sharp increases occurring between in 1991 and 1994. Trade is very small and highly variable, imports remaining mostly under 500 tonnes in the early 1990s but jumping to 75,000 tonnes in 1994, while annual exports during the period varied between nil and 136,000 tonnes.

[15] Marrero, Kyle and Lee (1993).

55. Venezuela has a number of regions suitable for rice growing; yields are in the order of 4.5 tonnes per hectare. The steady increase in rice production despite continuous falls in domestic prices appears to be explained by changes in the productive structure; both production and processing are now highly mechanized.

56. Rice benefited from an export subsidy of 10 per cent during 1991 and 1992, which seems to have been passed to producers only in part. Barceló and García (1994) attribute this situation to the oligopolistic nature of the industry, where one group controls 30 per cent of the market and five firms control 70 per cent. A sharp fall in domestic prices after 1989 appears to be linked to the elimination of the price support system, which apparently left producers in a weak bargaining position vis-a-vis agro-industrialists.

57. As internal rice prices have been falling and converging with world prices, the level of assistance to rice production has declined. Indeed, as internal prices fell below world prices in 1992, assistance became negative, with the only significant assistance extended through fertilizer subsidies.

58. Policy towards cereals for human consumption (including corn and rice) involves tariff escalation, with rates set for raw materials at 10, intermediate products at 15 and final goods at 20 per cent.[16] Cereal prices are also considered to be subject to instability or distortions and, thus, cereals have been included in the variable levy system. Corn, rice and sorghum are subject to a tariff rate of 15 per cent and, within the variable levy system, to a quota system.

59. Minimum producer prices apply to corn, rice and sorghum.[17] Rice and certain flours of corn, wheat and barley are also subject to maximum retail prices.[18]

60. Under the minimum access opportunities of the Uruguay Round Agreement on Agriculture, Venezuela included corn, rice, sorghum, millet, malt and wheat gluten in its list of items subject to tariff quotas, at final bound rates ranging from 15 to 40 per cent; in most cases the quotas are subject to no increases until 2004.

Coffee and cocoa

61. Coffee production fell during the early 1990s, recovering slightly in 1994. Most of the crop is consumed domestically, exports stood at some 17,000 tonnes in 1990, falling sharply thereafter and partially recovering to 10,300 tonnes in 1994. Coffee remains one of Venezuela's main export crops in value, aided in recent years by the strengthening of coffee prices.

62. Close to one million hectares are under coffee cultivation. Since a large number of low-income families are dependent on coffee growing, which also has a certain environmental value, the authorities feel compelled to maintain support programmes through such organizations as the National Coffee Fund (*Fondo Nacional de Café* - FONCAFE). The Fund, established in the mid-1970s is charged with the marketing of coffee and provides technical assistance; it also purchases and resells coffee through producers' organizations. Until recently, FONCAFE had a legal monopoly of coffee purchase and sale; now, producer organizations are also authorized to conduct this trade.

[16]Decree 1427, Official Gazette 234641, 23 January 1991.

[17]Official Gazette 35560, 4 October 1994.

[18]Official Gazette 35661, 25 February 1995.

63. Two main producer associations, PACCAS (*Productores Asociados para el Comercio del Café)*, a joint state/producer enterprise; CRAM (*Centro Regional de Acopio y Mercadeo*), a cooperative, exists as a alternative to the PACCAS. Both producer associations may buy, store and sell coffee either to the domestic coffee industry or to export. Prices were, until recently, determined by FONCAFE, which channelled payments from coffee processors and exporters through PACCAS and CRAM producers. According to Giacalone (1992), the system managed to secure common prices throughout the country and access to credit and technical advice, but resulted in the extreme dependence of producers upon the State.

64. Some PACCA (those with no outstanding debts with FONCAFE), were given the right in 1990 to buy and sell coffee independently. The Government maintained the right to buy and sell coffee from other PACCAS and from CRAM, and also to fix minimum prices for producers. It appears that the PACCAS can offer higher prices to producers.

65. Minimum producer prices apply to green coffee beans.[19] Ground coffee and various products containing coffee are also subject to maximum retail prices.[20]

66. There are some 66,000 hectares under cocoa cultivation; Venezuela's cocoa is high quality and attracts a price premium in world markets. Cocoa was formerly Venezuela's most import export crop, but due to weak producer prices output fell during the first half of the 1980s. There was then a modest recovery, with production stabilizing in the early 1990s but falling slightly in 1994. Exports account for some three-quarters of production. Small quantities are imported.

67. The National Cocoa Fund (*Fondo Nacional del Cacao* - FONCACAO) is charged with promoting and providing technical assistance to cocoa producers, financing domestic and international marketing production and programmes, establishing a price-fixing system, and support of production and processing. New Policies adopted in 1992 eliminated FONCACAO's monopoly on marketing, which has been opened up to producers organizations, individual producers or vertically integrated marketing firms.

68. Venezuela is a member of the International Coffee Organization (ICO), and has ratified the new International Coffee Agreement adopted in March 1994. Venezuela is also a member of the Association of Coffee Producing Countries, under which it is committed to retain 10-20 per cent of its export volume of coffee whenever world price developments activate the APPC's retention scheme (Chapter IV(3)(vi)). However, Venezuela is not currently bound by the retention system as the amount available for export does not reach the four million bags established as a minimum under the scheme.

69. In September 1994, Venezuela acceded to the International Cocoa Organisation,whose aims are to stabilize the world market for cocoa, to guarantee supplies at reasonable prices for producers and consumers and to promote the growth of the industry.

70. In accordance with international agreements, the Ministry of Agriculture and Livestock grants export permits for coffee and cocoa. All coffee exports must be accompanied by a certificate of origin. Coffee and cocoa exports benefit from an incentive equal to 10 per cent of their net f.o.b value (Chapter IV(2)(x)).

[19]Official Gazette 35560, 4 October 1994.

[20]Official Gazette 35661, 25 February 1995.

Bananas and plantain

71. In volume terms, plantain was Venezuela's second largest crop after sugar. Banana production edged up until 1992 but has since fallen slightly, both in volume and value (Table V.3). Export have grown from a small base amounting to some 38,000 tonnes in 1991, increasing sharply to 65,000 in 1992 and 71,000 tonnes in 1994. There are no imports. Plantain production has been constant during the 1990s; trade during that period was confined to a trivial quantity of exports in 1994.

72. A Framework Accord between the European Union and Venezuela and other three Latin American banana producers came into force on 1 January 1995.[21] According to the Venezuelan authorities, the accord offers a solution to the issues raised by the European Union's common banana régime (Chapter VI(1))(ii)). The Accord establishes a global quota of 2.2 million tonnes in 1995 for EU imports from Latin America and "non-traditional" imports from the ACP countries; Venezuela's share is 2 per cent of the global quota (Chapter IV(3)(viii)).

Sugar

73. Sugar cane production rose to 7.7 million tonnes in 1994, after some variation during the 1990s. Exports are generally negligible. Imports have risen to some 3 per cent of production in 1994.

74. Venezuela does not have an obvious advantage in the growing of sugar cane; yields are low (65 tonnes per hectare in 1989) and mill efficiency modest (about 7 per cent).[22] The country has 16 sugar mills, of which 11 are private, with a production capacity of around 600,000 tonnes of white sugar a year; the Government is privatizing the state-owned facilities.

75. Sugar mills own the Venezuelan Sugar Distributor (*Distribuidora Venezolana de Azucareros, DVA*). Since 1976, all sugar mills have been required to supply the whole of their production to DVA for distribution and sale. The DVA also handles all exports and imports.

76. In the 1960s, Venezuela was a net sugar exporter. However, following a freeze of domestic producer and retail prices during the 1970s, in an inflationary environment, the sector stagnated and the country became a net importer. Policies changed again in the early 1980s, when high domestic prices boosted the sector. Support turned negative between 1988 and 1990, mainly as a result of increasing world prices rather than from lower domestic prices; assistance then rose as world market prices weakened (Chart V.4).

77. Venezuela is a member of the Group of Latin American and Caribbean Exporters of Sugar (*Grupo de Países Latinoamericanos y del Caribe Exportadores de Azúcar*) established in 1974. The Group's objectives include to co-ordinate common approaches to production and marketing, to assist the industry's development, to help adopt common positions in international negotiations and to co-ordinate policies to achieve fair prices.

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[21]The Accord's other signatories are Colombia, Costa Rica and Nicaragua.

[22]Barceló and García (1993), p. 82.

78. Under the minimum access opportunities of the Uruguay Round Agreement on Agriculture, Venezuela included sugar cane and other sugars in its list of items subject to tariff quotas, at final bound rates set at 40 per cent; the quotas are subject to no increases until 2004.[23]

Other agricultural products

79. Cotton production increased during the 1980s, reaching 85,000 tonnes in 1990; it has since fallen considerably. According to official data, no trade in cotton has taken place during the 1990s. Downstream activities benefit from considerable tariff escalation.

(3) Fishing

80. All resources in Venezuela's exclusive economic zone are considered national patrimony. Under the fisheries law, the Ministry of Agriculture and Livestock regulates fishing activities, including the establishment of zones, seasons and quotas. Current policies towards the sector include:

- promoting and defending marine exports, through the establishment of appropriate sanitary and other regulations;
- protecting national production from unfair competition;
- promoting fishing and aqua-culture within the national agro-alimentary programme;
- establishing a bank for the promotion of new enterprises in the sector;
- improving co-ordination among ministries and other public agencies;
- developing extension programmes;
- rationalizing the marketing of marine products to increase fishermen's profits and protect domestic consumers;
- bringing up to date bilateral agreements, such as those with Suriname and Trinidad and Tobago, as well as establishing new accords with Caribbean and European Union countries; and
- strengthening Venezuela's participation in international organizations associated with tuna fishing.

81. In 1994, fishing employed some 62,000 workers, 62 per cent whom were employed in small-scale fishing, 13 per cent in deep-sea fishing and 25 per cent in fish processing. Small-scale production amounted to 195,000 tonnes; deep-sea fishing contributed 160,000 tonnes. Exports increased dramatically between 1988 and 1990, from US$14 million to US$98 million, but fell over the next two years, recovering in 1993 to US$82 million. Imports are growing from a small base, having reached US$6.5 million in 1993. The main export markets in 1993 were the United States, the European Union and Colombia.

82. The main export products are crustaceans, fish and crustacean preparations and fresh or refrigerated fish. The main species fished, by volume, are sardines and tuna. The tuna catch amounted to 81,164 tonnes in 1990, but fell the following year to 78,000 tonnes. Tuna fishing recovered in 1992 and 1993 but shrank again to 74,000 tonnes in 1994. Tuna fishing was seriously affected by a 1991 U.S. court decision placing an embargo on tuna imports from Venezuela on the grounds that killings of dolphins by the country's fleet were too high. Venezuela was involved as a third party to a GATT panel over the U.S. prohibition on imports of yellowfin tuna (Chapter VI(1)(iii)).

[23] Part I, Section I-B, Schedule LXXXVI, Corrigendum, 25 March 1994.

(4) Minerals (including fuels)

83. Minerals, including fuels, are far and away Venezuela's most important export sector. Petroleum alone accounts for between 75 and 80 per cent of total exports, depending on world prices; other major mineral-based exports include iron ore, aluminium, coal and gold. Mineral production is generally characterised by weak links with the rest of the domestic economy and the sector is, thus, mostly driven by developments in world markets. The State plays the leading role in mining, notably through Petróleos de Venezuela (PDVSA) and the Venezuelan Corporation of Guayana (CVG).[24]

84. Current objectives for mining and fuels are to chart the stock of mineral resources and further develop the sector, which is considered in the Stabilization and Economic Recovery Programme (PERE) as having huge expansion possibilities, readily exploitable in the short run. Policies to achieve those objectives include:

- modernizing the legal framework, in force since 1944, through the consolidation of regulations and a better definition of fiscal and sector-specific benefits;
- establishing the basis to allow private sector participation and increase national and foreign investment;
- setting up a clear set of regulations for land tenure, resource allocation and the control of environmental impacts;
- encouraging the sector's diversification by opening up new areas for exploitation;
- improving co-ordination among State agencies involved in the sector's promotion and development; and
- re-organizing the geological activities to improve the management, surveillance and control of the sector.

85. The mining sector receives little tariff protection, its products being subject to an average tariff of only 5.5 per cent, with most tariffs at a flat rate of 5 per cent. (Table AV.1). On the other hand, non-tariff measures are important in key mining activities. First and foremost, within the OPEC framework crude oil is subject to production quotas that impact significantly on Venezuela's exports. Moreover, both the national petroleum company and the state-owned iron ore mining firm have monopoly rights over the production and export of their products. The Central Bank limits the import and exports

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[24]The CVG (*Corporación Venezolana de Guayana*) is an independent State-owned organization with its own legal and financial status. The Corporation is charged with the establishment and coordination of State enterprises located in the Guayana Region. The following enterprises were part of the CVG group in 1990, either as subsidiaries or as mixed-capital ventures:

Energy CVG Electrificación del Caroni, C.A. (Edelca);
Iron and Steel CVG Siderúrgica del Orinoco, C.A. (Sidor), CVG Ferromineral Orinoco, C.A. (FMO), CVG Venezolana de Ferrosilicio, C.A. (Fesilven);
Aluminium CVG Bauxita Venezolana, C.A. (Bauxiven), CVG Interamericana de Alumina, C.C. (Interalumina), CVG Aluminio del Caroni, S.A. (Alcasa), CVG Industria Venezolana de Aluminio, C.A. (Venalum), CVG Carbones del Orinoco (Carbonorca);
Other mining CVG Compañía General de Minería de Venezuela, C.A. (Minerven), CVG Venezolana del Oro (Venorca), CVG Técnica Mineral (Tecmin), CVG Revemin II, C.A.;
Forestry CVG Proforca;
Services CVG Internacional, C.A. (INTERCVG);
Housing CVG Promotora del Desarrollo Urbano de la Region Guayana, C.A. (Produrgca), CVG Promociones Ferroca, S.A. (Ferrocasa).

of gold while other minerals are subject to export or import controls for security or environmental reasons (Chapter IV). Private investment in the sector remains restricted (Chapter III).

86. Venezuela made specific commitments under the General Agreement on Trade in Services (GATS) with respect to services incidental to mining. With respect to both market access and national treatment, Venezuela engaged itself not to place restrictions on consumption abroad or commercial presence; however, it undertook no commitments to accept cross-border supply or the presence of natural persons, except as indicated in its horizontal section (Chapter V(5)).

(i) Minerals other than hydrocarbons

(a) Coal

87. Total coal reserves are among the largest in the Americas, estimated at 570 million tonnes. Coal mining has been expanding rapidly since the mid-1980s with the exploitation of large deposits in the Guasare area in the north-west coast. Operations in that area are conducted by Carbozulia, a subsidiary of Petróleos de Venezuela S.A., in partnership with Enirisorses, S.P.A., Shell, Ruhr Kohle and Carbomar-Evan Energy. Coal production from the Guasare Basin reached 4.5 million tonnes in 1994 (Table V.4).

Table V.4
Mining Activity (excluding hydrocarbons)

	1989	1990	1991	1992	1993	1994
	Volume of production (million tonnes unless otherwise indicated)					
Iron ore	18.4	21.6	20.0	19.4	20.7	…
Coal	0.5	0.5	2.3	2.5	3.9	4.5
Bauxite	0.6	…	1.5	1.1	2.5	…
Gold (tonnes)	13.7	10.8	10.4	10.1	9.1	9.9
Diamonds (million metric carats)	300	475	475	670	575	…
	Value of production (billion bolivares)					
Iron ore	6.2	12.5	16.3	26.5	36.7	…
Gold	6.7	7.3	6.9	7.7	10.4	…
Coal	2.8	3.4	3.6	5.8	10.5	…
Bauxite	0.6	1.0	2.5	2.3	5.2	…
Diamonds	0.5	1.0	1.1	2.4	3.2	…

… not available

Source: Central Bank, Ministry of Energy and Mines, and Cepal (1995).

88. The Stabilization and Economic Recovery Programme (PERE), envisages expanding coal production to some 20 million tonnes per year by the year 2002 through joint ventures with private investors. The ambitious programme includes developing the Paso Diablo, Socuz, Norte and Cachiri mines in the Guasare district, and building a new railroad line and loading facilities. Agreements have already been signed with foreign companies for feasibility studies.[25] The aim is to produce 4.9 million tonnes per year from the Guasare fields by 1996, rising then as envisaged in the PERE.

89. This planned expansion is exclusively directed to export markets, aiming to make Venezuela one of the world's leading coal exporters. Foreign companies were being attracted by the prospects of significant discoveries (given the earlier lack of attention) and by favourable tax arrangements, including duty-free imports of foreign-manufactured mining equipment.[26] Expansion plans are also being assisted by other positive features, such as the deposits' low sulphur contents, high quality and low extraction costs. However, infrastructure costs are likely to be substantial and Venezuela is disadvantaged by its distance from key markets in the Far East.

(b) Iron ore

90. The main iron ore mining areas are located in the Guayana region. Reserves are estimated at about 13.9 billion tonnes among the world's ten largest. The industry developed from 50-year concessions granted in 1950 to two U.S. companies, which were nationalized in 1975.[27] The exploitation and marketing or iron ore is now managed by the state company Ferrominera Orinoco, a CVG subsidiary.

91. Ferrominera Orinoco has an installed capacity of 19.5 million tonnes per year for the production of sinter, pellet feed and lump ore, and operates a pelletiztion plant with a capacity of 303 million tonnes per year. Output fell sharply in the early 1980s, partly due to the recession in the world steel industry. It has since risen to reach close to 20 million tonnes in 1991, placing Venezuela among the world's ten largest producers. Ferrominera Orinoco plans to increase capacity to 25 million tonnes per year by the year 2000 as well as to construct a new pelletization plant with a capacity of 3.3 million tonnes per year and, in association with private investors, two modules of 4 million tonnes of concentrated iron ore.

92. Mining of iron ore is still the exclusive right of Ferrominera Orinoco and, thus, closed to private participation.

(c) Bauxite

93. Major bauxite deposits were proven in 1977 in the Sierra Los Pijiguaos region; proven reserves are estimated at some 200 million tonnes of high-grade ore (around 50 per cent aluminium oxide), a medium-size deposit by world standards. Trial shipments began in late 1986 and output rose to some 2 million tonnes in 1991, fell back in 1992 and rebounded in 1993 (Table V.4). The operations are

[25]Association agreements have been signed with Enirisorses, S.P.A. and Carbomar - Evan Energy, and intention letters have been exchanged with Shell and Ruhrkohle.

[26]An exemption from taxes on profits (*impuesto a la renta*) under Decree 1058 of 1986, expired in December 1994.

[27]U.S. Steel and Bethlehem Steel.

conducted by Bauxita Venezolana C.A. (Bauxiven), a CVG subsidiary; installed capacity is about 6 million tonnes per year. Production is aimed at the domestic aluminium industry.

(d) Gold

94. A major effort is currently under way to tap Venezuela's large ore reserves, estimated to be as much as 8,000 tonnes. CVG controls two affiliates operating in gold mining, Minerve C.A., which works deep-vein mineral deposits, and Venorca, which processes alluvial mineral. The first official gold export shipment took place in 1987; sales have since risen in an irregular fashion.

95. Smuggling of gold by prospectors is estimated at up to three times the level of official sales.[28] To reduce contraband and encourage new developments, in 1986 the Central Bank started purchasing supplies from miners at world prices translated at the free-market exchange rate. Other steps taken to reduce smuggling include setting aside areas for small scale mining and a reduction in the tax on gold production from 3 to 1 per cent, when the metal is sold to the Central Bank.

96. In 1995, the Central Bank announced a new gold mining policy under which mining companies will be allowed to sell 60 per cent of their gold abroad, the remaining 40 per cent will have to be sold in the domestic market (including sales to the Bank which previously absorbed 100 per cent of production). The policy change is aimed at encouraging private foreign and national investment.

97. Development plans seek to transform gold mining into a major exporting activity, aided by a new legal framework, guarantees for capital mobility and the same treatment for foreign and domestic investment. Small-scale mining operations will be authorized under strict controls to prevent illegal, environment-damaging activities. A modern fiscal régime and appropriate supervision are to ensure that the State benefits from gold mining.[29]

(e) Other non-fuel minerals

98. A significant volume of diamonds is produced, but there is again a large incidence of smuggling. Venezuela has sizable resources of uranium and thorium, with reserves amounting to some 40,000 tonnes and 300,000 tonnes, respectively. Other minerals include nickel (reserves of about 2.5 million tonnes), phosphates, copper, zinc, lead, silver, titanium and manganese.

(ii) <u>Petroleum</u>

99. In 1994, the petroleum sector's share in GDP was close to 24 per cent, with some 4.6 per cent derived from refining. Petroleum was also predominant in public sector revenue, albeit falling from 82 per cent in 1990 to 50 per cent in 1994. On the other hand, employment is low at some 80,000.

100. The oil sector's contribution to GDP is strongly affected by developments in the world market; it rose to just over 28 per cent of GDP in 1990 after the oil price rises resulting from the Gulf War. Petroleum GDP increased at a healthy rate of some 5 per cent in both 1993 and 1994, reflecting stronger demand and higher world prices, in contrast with the decline of total GDP in the same years.

[28]Allegedly, in the main Brazilian *garimpeiros*, who also appear to be involved in diamond smuggling.

[29]CORDIPLAN (1995), p.117.

(a) Institutional framework

101. The general thrust of policies in the petroleum industry is to maximize value added while ensuring the industry's continuing viability and its expansion in a manner consistent with Venezuela's other social and economic goals. These policies involve:

- proving and developing additional reserves of light and medium crudes;
- increasing and maintaining in the medium term (to the year 2000) an output capacity of 4.4 million barrels per day;
- consolidating Venezuela's natural markets through partial or total overseas acquisitions of refineries and distribution systems;
- creating joint ventures with foreign and national private partners; and
- incorporating the private sector to downstream and non-petroleum activities of PDVSA.

102. All hydrocarbon reserves are owned by the State; the law also reserves to the State the production and marketing of hydrocarbons. The State's paramount role in the sector is secured by its ownership of Petróleos de Venezuela S.A. (PDVSA), an enterprise charged with developing the national petroleum industry and planning, coordinating, supervising and controlling the activities of its subsidiaries, both in Venezuela and abroad (Box V.1).

Box V.1 Petróleos de Venezuela, S.A. (PDVSA)

PDVSA is a holding corporation wholly owned by the Government of Venezuela. It was formed after the oil industry was nationalized in 1976; the then state firm and the foreign oil companies were renamed and became operating subsidiaries of PDVSA. Through successive consolidations, the number of PDVSA's operating subsidiaries in Venezuela has been reduced to three: Corpoven, Lagoven and Maraven. These are vertically integrated operating companies engaged in all activities related to exploration, production, refining, transportation and marketing.

PDVSA's other subsidiaries in Venezuela are:

- Bitúmenes Orinoco (BITOR), a vertically integrated company that produces bitumen, and manufactures, transports and markets Orimulsion;
- Carbones de Zulia, S.A. (Cabozulia), in charge of commercial development of the Guasare coal deposits in western Venezuela;
- Petroquímica de Venezuela, S.A. (Pequiven), operates petrochemicals plants, many in joint ventures, and promotes investment in the petrochemical sector;
- PDV Marina, in charge of coordinating PDVSA's international tanker fleet;
- Intevep, the group's research and development centre;
- Bariven handles the Corporation's overseas purchases of equipment and materials through its PDVSA Services branches overseas; and
- Palmaven provides technical assistance to farmers and participates in conservation projects.

PDVSA has extensive equity holdings in petroleum refining, distribution and marketing systems in the Caribbean, Belgium, Germany, Sweden, the United Kingdom and the United States.

In the United States, the PDVSA group owns CITGO Petroleum Corporation as well as 50 per cent of the UNO-VEN Company, in partnership with UNOCAL. In 1993, a total of 312,000 barrels per day of Venezuelan crude was placed in CITGO refineries in the United States; CITGO marketed 100,000 barrels per day of refined products of Venezuelan origin, including 56,000 barrels per day of gasoline. It has over 12,500 stations operating under its own brand name in the eastern half of the United States, making it the second-largest gasoline retailer in that country. Two recently completed deals will allow it to expand rapidly in the U.S. mid-west. PDVSA is the biggest exporter of gasoline to the United States, with plans to boost exports in 1995 by 10,000 barrels per day to 60,000 barrels per day.

In Europe, the PDVSA group is an equal partner with VEBA OEL AG in Ruhr Oel GmbH, the largest refining company in Germany. PDVSA is also an equal partner with Neste Corporation of Finland in Sweden's AB Nynäs, which operates refineries in Sweden, Belgium and the United Kingdom. PDVSA units also operate oil refinery and storage facilities in Curaçao, Bonaire and the Bahamas.

PDVSA's subsidiaries abroad operate on a "net back" basis, that is, PDVSA guarantees them a percentage of the profits and the rest is absorbed by PDVSA.

103. PDVSA is subject to an onerous tax régime that requires it to pay mineral royalties, an export charge, a tax on assets and a high income tax (Box V.2). It is also required to meet domestic demand in full at prices which are substantially below those which it could obtain in the international markets. The fiscal burden may have undermined the company's ability to invest and led it to incur a substantial foreign debt (Box V.2). The magnitude and financing of the company's domestic and foreign investment programme is a matter of domestic debate, particularly at present when the Government itself is facing fiscal problems (Chapter I). Forgoing capital investments to make payments to the Government (its only shareholder) risks having an adverse impact on PDVSA's medium-term results and reduce its contribution to the economy.

Box V.2 Fiscal and financial arrangements in the oil industry

Petróleos de Venezuela S.A. (PDVSA) was conceived as a commercial enterprise, financially independent from the State. Its subsidiaries operate under a fiscal regime based on the system applied to foreign oil enterprises before their nationalization. The regime subjects PDVSA (strictly speaking, its subsidiaries) to three charges: a royalty (16.66 per cent), income tax (67.7 per cent) and a charge on the fiscal value of exports (with a maximum rate of 20 per cent). A law was passed in 1993 to phase out the charge on the fiscal value of exports by 1996. Beginning in 1994, a tax of 1 per cent on the average of the assets is also collected; this tax is creditable against the income tax.

PDVSA and its Venezuelan subsidiaries are entitled to a tax credit for new investments of up to 14 per cent of the amounts invested; the credit is subject to a cap of 2 per cent of the net taxable income. To ensure its financial independence, PDVSA collects from its subsidiaries 10 per cent of their export revenues, exempt from income tax.

PDVSA estimates that it was subject in 1991 and 1992 to an effective income tax rate of about 93.5 per cent, falling to just over 66 per cent in 1993. Mora and Espinasa (1994) estimated PDVSA's fiscal burden to be equivalent to at least 85 per cent of the company's profits. According to those authors, this fiscal burden has undermined the company's ability to maintain oil production and to adapt its domestic refineries to new international environmental standards.

Moreover, the company has considerably increased its foreign debt since 1991. This reached some US$3.8 billion in 1992 (equivalent to about 14 per cent of its assets), and some US$ 5.5 billion in 1993. According to the Petroleum Economist (November 1994), PDVSA's true financial position is not known with certainty, especially the liabilities arising from its pension fund, international agencies have downgraded its debt and privatization is being discussed seriously; however, the authorities rule out such a possibility.

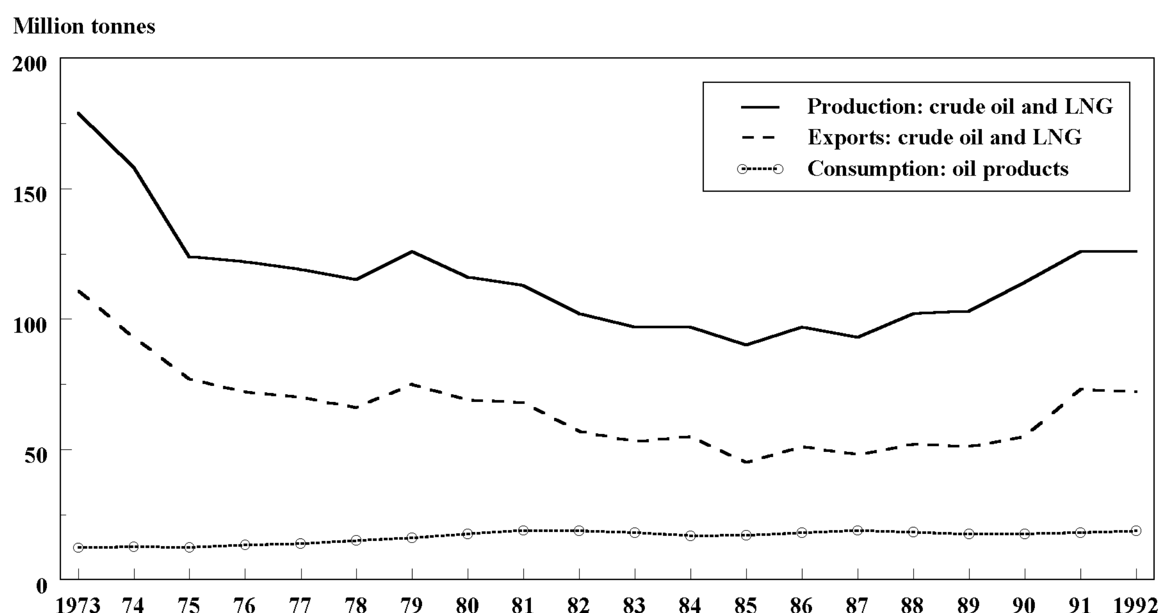
To halt further indebtedness, the authorities have adopted policies to attract private investment (Box V.5). With this objective, the income tax law of 1991 provided that joint ventures created to exploit natural gas and extra-heavy crudes pay an income tax rate of 34 per cent. This raises the possibility that PDVSA may have to pay two different income tax rates on similar projects depending on whether it is associated with a private partner.

Significant divergences have arisen at times between the Government and PDVSA regarding the degree of the company's financial independence. In 1982, the Venezuelan President, without consulting PDVSA's president or board, ordered the transfer of PDVSA's US$5.5 billion foreign exchange reserves held overseas to the Central Bank in order to boost international reserves. PDVSA's subsidiaries were then required to pay taxes in advance and purchase treasury bonds to help solve the public deficit problem. In other instances, the Government has utilized differential exchange rates to maximize its oil revenue (Mommer, 1994).

The magnitude and financing of the company's investment programme, both domestic and foreign, have also come under pressure from the Government's recurrent fiscal deficits. PDVSA's investments abroad were targeted for reduction in 1992, when the Venezuelan President gave instructions for the sale of PDVSA's stakes in its overseas refining ventures, which in the event were not realized (Petroleum Economist, November 1992). A more recent discussion arose in mid-1995, when the Finance Minister pressed the need to revise PDVSA's contribution to the treasury and help finance the country's budget deficit, while PDVSA's management stressed the importance of maintaining the investment programme and not compromising future oil output (Latin American Regional Reports - Andean Group, 29 June 1995).

104. Venezuela limits the production of crude petroleum and natural gas on conservation grounds.[30] According to the authorities, these policies do not discriminate between the domestic market and exports. However, in reality long standing domestic policies have stimulated domestic energy consumption (Chapter V(ii)(a) and Annex V.1). As a result, exports have experienced the brunt of the production restrictions (Chart V.6). Thus, in practice Venezuela's production restrictions are tantamount to export limits, and part of a coordinated attempt by the Organization of Petroleum Exporting Countries (OPEC) to influence world markets (Box V.3). Indeed, the authorities highlight the great importance that decisions taken within the OPEC framework have on Venezuela's exports.

Chart V.6
Venezuela's oil production, consumption and exports, 1973-92



Source: International Energy Agency (1994).

[30]At the time of its accession to GATT in 1990, Venezuela noted that, in accordance with Article XX(g) of the GATT, measures adopted to limit domestic consumption included the gradual increases in fuel prices, the development of alternative renewable sources of energy (hydro-electricity) and controls relating to motor-car engine capacity. In practice, little appears to have been achieved in most of these areas.

Box V.3 Venezuela's participation in OPEC

The first move towards the establishment of the Organization of Petroleum Exporting Countries (OPEC) took place in 1949 when Venezuela approached Iran, Iraq, Kuwait and Saudi Arabia to suggest talks and explore ways to improve communications between them. Those five countries formally established OPEC in 1960 as a permanent inter-governmental organization; as a founding member, Venezuela enjoys certain special rights within the organization. In addition to the founding members, OPEC has seven other full members (in order of accession, Qatar, Indonesia, Libya, United Arab Emirates, Algeria, Nigeria and Gabon).

OPEC's initial objectives have remained unchanged: to co-ordinate and unify the petroleum policies of member countries and to determine the best means of safeguarding their individual and collective interests; to seek ways and means of ensuring the stabilization of prices in international oil markets; to provide an efficient, economic and regular supply of petroleum to consuming nations and a fair return on capital to those investing in the petroleum industry. Over time, OPEC has also adopted policy guidelines calling for measures to prevent the deterioration of oil prices vis-à-vis traded manufactured goods and the establishment of a new international economic order.

Until the mid-1980s, OPEC provided the bulk of the world's oil supplies, but the emergence of a number of other oil-producing countries has made substantial inroads into OPEC's share of the market. Nevertheless, the organization still exercises considerable influence in the oil market thanks to its large petroleum reserves and spare production capacity. Venezuela has typically accounted for about 10 per cent of OPEC's production.

After the Middle East crisis of late 1973 triggered the first oil shock, OPEC followed a policy of setting official prices for crude oil and regulating supplies). After the disruption of Iranian oil supplies in 1979, OPEC tried to defend the record high oil prices (Chart V.8) by introducing a production quota system in 1982, efforts which failed to prevent a sharp price fall in 1986. In mid-1986 OPEC adopted an output ceiling system (Venezuela's production quota was set just over 1.5 million barrels per day) and later that year a fixed pricing system based on a basket of seven crudes. This basket, in which Venezuela's Tia Juana oil is included, serves as a reference for the market price but leaves each member country with flexibility to pursue its own market strategies. A system of production quotas is currently in place.

Venezuela's official position regarding OPEC includes its continuous participation in the organization, within which Venezuela is committed to defend moderate but stable prices in the long term and maintain a proactive position in the reconciliation of the interests of OPEC members (Cordiplan (1995), p.51).

However, Venezuela's OPEC membership is not without controversy. In 1992, PDVSA's president argued that the company's expansion plans were incompatible with OPEC output restrictions and asked for the reconsideration of Venezuela's participation in that organization; he also welcomed Ecuador's decision to abandon OPEC. In this respect, the Petroleum Economist (March 1995) pointed out that Venezuela has been producing over its OPEC production quota, with the excess officially going into storage. Clearly, increased production quotas will be required to accommodate PDVSA's expansion plans (Table V.6) or the production increases that may derive from private investment.

105. Venezuela exempted indefinitely services related to petroleum activities from the m.f.n. treatment envisaged under Article II of the General Agreement on Trade in Services (GATS). Such exemptions related to preferences granted under bilateral agreements with Brazil, France, Germany, and Central American and Caribbean countries for the distribution and marketing of petroleum and petroleum products, advisory services and exchange of technology.

(b) Petroleum production and exports

106. Venezuela is the world's fourth largest oil producer.[31] It plays a major role in the international oil market as it is one of the few petroleum exporting countries outside the Middle East with spare capacity. Production of crude, condensate and natural gas liquids reached an average of about 2.6 million barrels per day in 1993 (Table V.5). Venezuela's proven reserves of crude oil stood at the equivalent of about 70 years of production.[32]

Table V.5
Hydrocarbons production statistics, 1993

Proven reserves	
Petroleum (billion barrels, excluding extra-heavy oil)	64.4
Natural Gas (trillion cubic metres)	3.9
Production	
Crude oil ('000 barrels/day)	
Light (over 30 API)	891
Medium (22-30 API)	884
Heavy and extra-heavy (under 22 API)	635
Total crude	2,410
Condensate ('000 barrels/day)	40
Natural gas liquids and ethane ('000 barrels/day)	113
Natural Gas (million M^3/d):	
Production	115.5
Uses	
Oil industry operations	33.7
Re-injection	32.4
Sold	40.3
Exports	
Crude Oil ('000 barrels/day)	
Light (over 30 API)	270
Medium (22-30 API)	558
Heavy and extra-heavy (under 22 API)	663
Reconstituted	49
Total crude	1,540

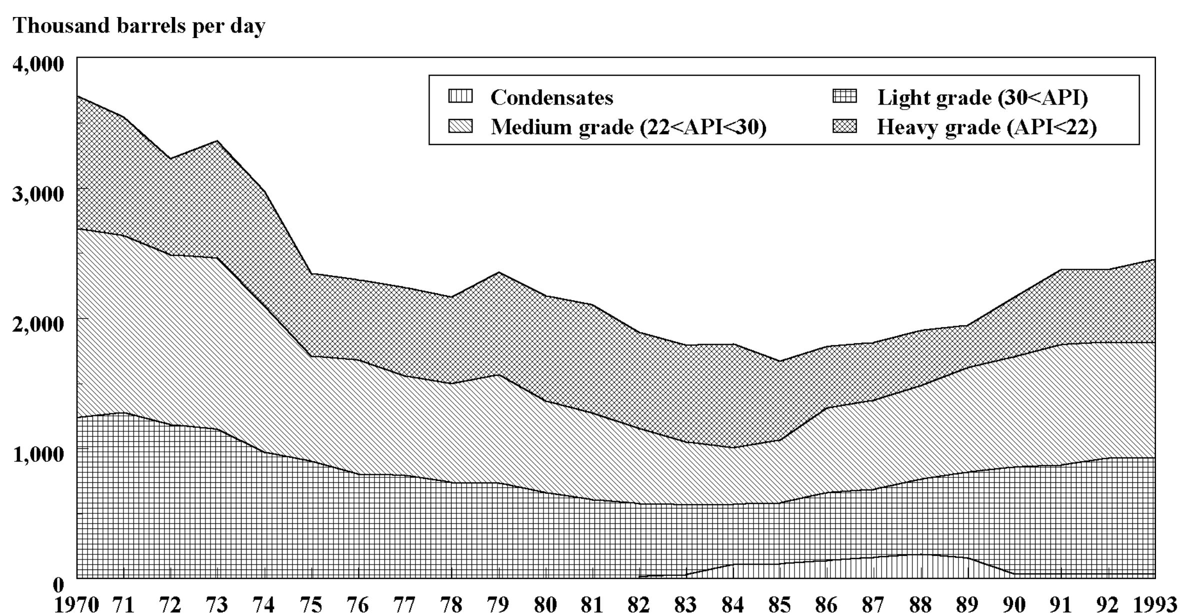
Source: PDVSA (1994).

[31]After Saudi Arabia, Iran and Mexico.

[32]Venezuela's oil reserves are the world's sixth largest, not counting its vast reserves of extra-heavy crude (up to 267 billion barrels) in the Orinoco oil belt.

107. Crude oil production peaked in 1970 at 3.7 million barrels per day (Chart V.7). In the context of OPEC efforts to maintain world oil prices through production quotas, output fell to a low of 1.7 million barrels in 1985, which did not prevent prices subsequently slumping to a 10-year low in 1986 (Chart V.8). With subsequent upward adjustments in OPEC's overall ceiling as prices rose in the late 1980s, Venezuela's allocation was raised to 1.95 million barrels per day for the first half of 1990. Before that, the country had effectively lifted its permissible exports by boosting output of concentrates;[33] to contribute to OPEC unity, Venezuela agreed in November 1989 to cut condensates output to a maximum of 37,000 barrels per day. There was a sharp increase in oil production in the latter half of 1990 with Venezuela playing an important role in maintaining world supplies following the suspension of exports from Iraq and Kuwait; combined with sharp price rises, oil revenues increased substantially that year. In an effort to offset subsequent price falls, crude output has risen since 1990, with Venezuela reportedly producing above its OPEC ceiling of 2.257 million barrels per day.[34]

Chart V.7
Production of crude petroleum by API gravity, 1970-93

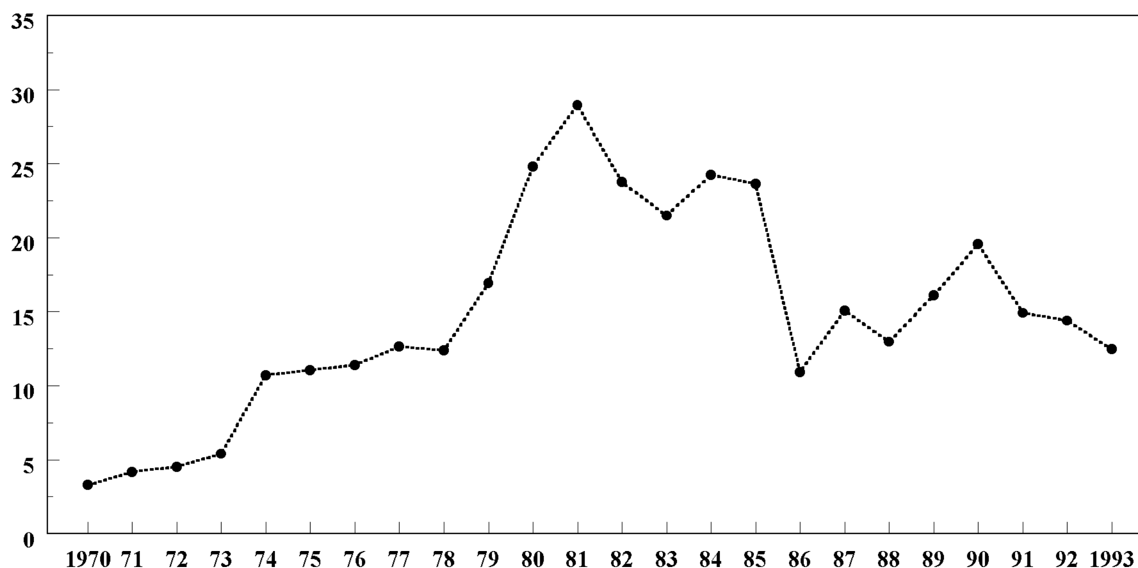


Source: PDVSA; and Central Bank of Venezuela.

[33]Extra light crudes which are not counted as part of OPEC quotas.

[34]Economist Intelligence Unit, Country Profile - Venezuela, 1994-95.

Chart V.8
Unit value of petroleum exports, 1970-93



a f.o.b. cost of U.S. crude oil imports from Venezuela; 1970 to 1972, WTO estimates.

Source: U.S. Department of Energy, Energy Information Administration, Monthly Energy Review, various issues.

108. In volume terms, Venezuela's main export markets for crude oil and refined products are the United States and Canada, absorbing almost 70 per cent of total exports in 1993, followed by Central America and the Caribbean, Europe and South America, with shares of 15.7 per cent, 9 per cent and 3.7 per cent, respectively. Despite the existence of the San José Pact with countries in Central America and the Caribbean, oil supplies to that area take place mainly on a commercial basis (Box V.4).

109. PDVSA's long-term Business Plan, defined in 1993, reflects the view that Venezuela's comparative advantage still lies in the oil sector, and the Plan aims at enhancing the presence of the oil industry in the national economy.[35] Between 1995 and 2003 crude production capacity is expected to increase by some 44 per cent while crude production should increase even more, by some 59 per cent (Table V.6). Refining capacity of PDVSA, in and outside Venezuela, is also to grow significantly. Considerable emphasis is to be placed on the exploitation of extra-heavy crude from traditional areas, as well as through integrated projects in the Orinoco Belt, and an expansion in Orimulsion production. If successful, these plans would go a long way toward pulling Venezuela's economy out of its current slump, but questions remain on the feasibility of achieving the needed expansions in exports within the constraints imposed by Venezuela's participation in OPEC.

[35] PDVSA (1994), p.8.

Box V.4 San José Pact

Under the San José Pact, first signed in 1980, Venezuela and Mexico each engaged to supply 80,000 barrels per day of hydrocarbons to Central American and Caribbean countries (Barbados, Costa Rica, El Salvador, Guatemala, Haiti, Jamaica, Nicaragua, Panama, and Dominican Republic). The agreement is automatically renewed each year.

Under the Pact, petroleum is supplied on purely commercial terms. Part of the invoice value is reserved in favour of the importing countries and can be returned as development aid in the form of tied loans. Such loans are equivalent to between 20 and 25 per cent of the invoice value of oil purchases, depending on the world oil price. For Venezuela, the loans are managed by the Investment Fund of Venezuela (FIV); at least 80 per cent of the loans must be used to acquire goods and services of Venezuelan origin. No more than 15 per cent of the FIV's resources may be committed to loans under the Pact, which has at times constrained the volume of loans. Venezuela grants loans worth some US$70 million annually under the programme.

The Pact guarantees oil supplies to beneficiary countries, a valuable benefit at the time the Pact was initially agreed but which is of less value today. Otherwise, the Pact's benefits relate not to energy per se but to financial assistance. The net benefits of such assistance are not easy to quantify as any concessional terms under which the loans may be granted must be considered against the requirement that the funds must be spent in Venezuelan goods and services. Loans are granted for periods of up to 12 years, with a three-year grace period. Interest rates are variable and linked to those charged on ordinary operations by the Inter-American Development Bank (IDB). In an attempt to tighten the credit terms, funds are no longer deposited with the central banks of the beneficiary countries and disbursements are suspended whenever payments fall into arrears.

110. As part of the effort to raise output capacity, foreign companies are to be allowed back into the industry on a limited basis (Box V.5). A major programme is also in train to develop the bitumen reserves of the Orinoco Belt. With this aim, PDVSA has developed a fuel for electricity generating plants, Orimulsion, of which two million tonnes were expected in 1993, 72 per cent to Europe and the remainder to Japan.[36] Orimulsion is considered by the Venezuelan authorities as a non-conventional hydrocarbon fuel and, thus, outside the country's OPEC quota; the target markets for Orimulsion are base-load electricity generation and existing under-utilized liquid-fuel fired power stations.[37]

[36] Orimulsion, jointly developed by British Petroleum and PDVSA, is the trade name of a natural bitumen dispersed in water. It is produced in Venezuela from the Orinoco belt by Bitor, a subsidiary of PDVSA.

[37] Orimulsion is pumped through pipelines, stored in conventional bunded tanks and transported in oil tankers; however, it is sold at coal-related prices. The European Union accords Orimulsion the same status as natural gas and coal for tax purposes.

Table V.6
PDVSA's business plan, 1995-2003
(Volumetric targets)

	1995	2003
Crude Production Capacity (million barrels/day)	3.2	4.6
Traditional areas	3.2	3.8
condensates, light, medium crudes	2.3	2.3
heavy, extra-heavy crudes	0.9	1.1
operational agreements	-	0.4
New areas	-	0.8
Crude Production (million barrels/day)	2.6	4.3
Natural Gas liquids (thousand barrels/day)	147	239
Liquified Natural Gas	-	6
Refining Capacity (million barrels/day)	2.4	2.8
Local	1.2	1.2
International	1.2	1.6
Orinoco belt - Integrated	-	0.3
Petrochemical Capacity (million tonnes/year)	5.0	11.1
Orimulsion Production (million tonnes/year)	4.8	20.0

- nil

Source: PDVSA

Box V.5 Foreign participation in the oil industry

Article 5 of the 1976 Hydrocarbons Law established that, in certain special cases, PDVSA or its subsidiaries may enter into joint ventures with private firms, provided that the State retains control of the venture, the association is for a fixed-term period, and a joint session of Congress authorizes the agreement. PDVSA must always be a majority partner in all its joint ventures.

The oil nationalization law also calls for disputes to be settled in Venezuelan tribunals under domestic laws, and under no circumstance may they be submitted to foreign arbitration. Under Article 127 of the Venezuelan Constitution, such a clause is implicit in all contract of "public interest", unless it is legally inadmissible (even Venezuela's bilateral treaty with the U.S. Overseas Private Investment Corporation, Chapter III(2)(iii), agrees to Venezuelan jurisdiction in disputes). According to the Petroleum Economist, November 1992, such a prohibition of international arbitration was a major obstacle for foreign participation in the LNG Cristobal Colon project.

PDVSA's financial constraints have compelled the authorities to make changes and accommodate the participation of foreign investors in areas that previously laid within the Corporation's exclusive domain. The new policy envisages three schemes:

- Strategic associations (joint ventures) for high-risk, high capital-investment projects to convert extra-heavy oil from the Orinoco Belt, and exploration and exploitation of light-oil areas.
- Operational agreements designed to re-develop a number of older, marginal fields through the award of development and production (service) contracts; all the hydrocarbons produced would be marketed by PDVSA or its subsidiaries.
- Risk exploration through production sharing agreements, to be applied to prospective areas with less information.

Strategic associations include two heavy-crude projects and the Cristobal Colon LNG project (Chapter V(2)(ii)(d)). A major innovation in this joint venture is the acceptance of international arbitration; although still subject to Venezuelan laws, any dispute is to be resolved by arbitration according to the rules of the International Chamber of Commerce in Paris and New York.

PDVSA indicated having signed by mid-1995 some 27 contracts with national and foreign companies to operate 14 oil fields. Production from those fields would reach just over 200,000 barrels per day in 1996, and rise to some 440,000 barrels per day by 2003. Required investment was calculated at some US$6.5 billion over 10 years. In mid-1995, some 11 risk exploration contracts were being negotiated, involving an investment of some US$11 billion.

(c) Natural gas

111. Venezuela's production of natural gas was 115 million cubic metres in 1993; proven reserves are equivalent to some 90 years, constituting one of the highest reserve-production ratios in the world.

112. The natural gas law of 1971 reserves the exploitation of natural gas for the State, and distribution and marketing are now in the hands of the PDVSA subsidiary, Corpoven. Policies with respect to natural gas involve:

- developing non-associated offshore natural gas reserves via liquification plants and export to Europe and the United States;
- promoting the use in Venezuela of natural gas as a motor vehicle fuel;
- using natural gas in power plants to free liquid fuels for export; and
- extracting the liquified components of enriched natural gas before its use.

113. The Cristobal Colón LNG project promises to give a substantial boost to the gas industry (Box V.5). In a major change in policy, foreign investors will hold a majority share in this project.[38] The project is envisaged to have a production capacity of 960 million cubic feet per day and a liquification capacity of 6 million tonnes per year; total investment would reach US$5.1 billion. Under the tax reform measures approved in mid-1991, an income tax rate of only 34 per cent will apply to the venture instead of the 67 per cent rate at present paid by PDVSA. The project was approved by Congress in 1993, but a weak world market and political uncertainty have slowed down progress.

(5) Manufacturing

114. The manufacturing sector accounted in 1993 for about 14 per cent of GDP and employment. The sector is with some exceptions, highly dependent on the domestic market; thus it grew steadily between 1984 and 1988, contracting with economic activity in 1989. Growth resumed between 1990 and 1992 but it has since turned negative as a result of depressed domestic demand (Chapter I).

115. Manufacturing, including petroleum refining, is dominated by processing of agricultural and mineral raw materials.[39] The five main sub-sectors in terms of total output are food products, petroleum refineries, transport equipment, other chemicals, and iron and steel. However, petroleum refining is by far the most important individual sub-sector in terms of value added, (Tables V.7 and V.8). Petrochemicals, plastics, glass, ceramics, metal products and motor vehicles have experienced particularly high, sustained rates of growth, which the authorities expect to be maintained.

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[38]Shell is to take 31 per cent, Exxon 29 per cent and Mitsubishi 8 per cent, with the remaining equity to be contributed by PDVSA's subsidiary, Lagoven.

[39]This chapter follows the ISIC classification in which petroleum refinery is treated as part of manufacturing.

Table V.7
Basic economic indicators for manufacturing, 1992
(Million bolivares and number)

ISIC Code	ISIC Description	Value of output	Value added	Purchase of materials and services	Wages and salaries	Employment (persons)	Number of establishments
				(Million bolivares)			
300	All manufacturing	1,898,298	885,027	1,013,271	186,379	495,179	10,374
311+ 312	Food products	348,021	107,312	240,708	28,146	89,266	2,538
313	Beverages	93,813	55,223	38,590	8,155	16,916	116
314	Tobacco	34,358	28,906	5,452	2,770	3,409	22
321	Textiles	48,471	19,588	28,883	7,609	23,862	227
322	Clothing	35,803	15,655	20,148	6,283	28,270	884
323	Leather products	10,253	3,043	7,210	1,123	5,281	114
324	Footwear	22,187	8,079	14,108	3,756	16,482	495
331	Wood products	10,145	3,858	6,287	1,741	7,754	304
332	Furniture except metal	18,902	7,378	11,525	3,099	15,145	942
341	Paper products	56,556	21,396	35,160	6,532	13,826	104
342	Printing	39,538	17,630	21,908	6,467	19,219	619
351	Industrial chemicals	94,151	44,182	49,969	10,701	13,206	118
352	Other chemicals, incl. pharm.	123,501	65,727	57,774	16,671	31,058	296
353	Petroleum refineries (a)	274,885	222,042	52,842	4,058	7187	14
354	Petroleum and coal products (a)	1,823	899	924	210	1163	26
355	Rubber products	24,767	11,324	13,443	2,981	7,422	62
356	Plastic products	43,441	17,508	25,933	6,459	21,954	446
361	Pottery and china	3,981	2,527	1,454	1,170	3,106	29
362	Glass and products	18,632	11,401	7,230	2,374	6,899	60
369	Other non-metallic mineral products	52,470	26,365	26,105	8,414	21,928	498
371	Iron and steel	105,981	52,959	53,022	8,874	25,377	159
372	Non-ferrous metals	86,197	22,299	63,898	6,289	13,168	84
381	Fabricated metal products	85,459	30,967	54,492	11,046	36,307	1,209
382	Non-electrical mach. incl. computers	44,594	18,468	26,127	5,579	17,450	308
383	Electrical machinery	52,057	20,222	31,834	7,169	18,894	237
384	Transport equipment	130,440	42,049	88,391	9,520	20,698	253
385	Professional and scientific equipment	7,151	3,867	3,284	1,590	2,955	51
390	Other manufactured products	45,328	4,611	40,717	1,808	6,356	169

a 1990 data.

Source: O.C.E.I., Encuesta Industrial Anual.

Table V.8
Relative importance of manufacturing industries, 1992
(As percentage of the sectoral total)

ISIC Code	ISIC Description	Value of output	Value added	Purchase of materials and services	Wages and salaries	Employmen t (persons)	Number of establishments
300	All manufacturing	100.0	100.0	100.0	100.0	100.0	100.0
311+ 3 12	Food products	18.2	12.1	23.4	15.6	18.0	24.4
313	Beverages	4.9	6.2	3.8	4.5	3.4	1.1
314	Tobacco	1.8	3.3	0.5	1.5	0.7	0.2
321	Textiles	2.5	2.2	2.8	4.2	4.8	2.2
322	Clothing	1.9	1.8	2.0	3.5	5.7	8.5
323	Leather products	0.5	0.3	0.7	0.6	1.1	1.1
324	Footwear	1.2	0.9	1.4	2.1	3.3	4.8
331	Wood products	0.5	0.4	0.6	1.0	1.6	2.9
332	Furniture except metal	1.0	0.8	1.1	1.7	3.1	9.1
341	Paper products	3.0	2.4	3.4	3.6	2.8	1.0
342	Printing	2.1	2.0	2.1	3.6	3.9	6.0
351	Industrial chemicals	4.9	5.0	4.9	5.9	2.7	1.1
352	Other chemicals, incl. pharm.	6.5	7.4	5.6	9.2	6.3	2.9
353	Petroleum refineries (a)	14.4	25.1	5.1	2.2	1.5	0.1
354	Petroleum and coal products (a)	0.1	0.1	0.1	0.1	0.2	0.3
355	Rubber products	1.3	1.3	1.3	1.7	1.5	0.6
356	Plastic products	2.3	2.0	2.5	3.6	4.4	4.3
361	Pottery and china	0.2	0.3	0.1	0.6	0.6	0.3
362	Glass and products	1.0	1.3	0.7	1.3	1.4	0.6
369	Other non-metallic mineral products	2.7	3.0	2.5	4.7	4.4	4.8
371	Iron and steel	5.5	6.0	5.2	4.9	5.1	1.5
372	Non-ferrous metals	4.5	2.5	6.2	3.5	2.7	0.8
381	Fabricated metal products	4.5	3.5	5.3	6.1	7.3	11.6
382	Non-electrical mach. incl. computers	2.3	2.1	2.5	3.1	3.5	3.0
383	Electrical machinery	2.7	2.3	3.1	4.0	3.8	2.3
384	Transport equipment	6.8	4.7	8.6	5.3	4.2	2.4
385	Professional and scientific equipment	0.4	0.4	0.3	0.9	0.6	0.5
390	Other manufactured products	2.4	0.5	4.0	1.0	1.3	1.6

a 990 data.

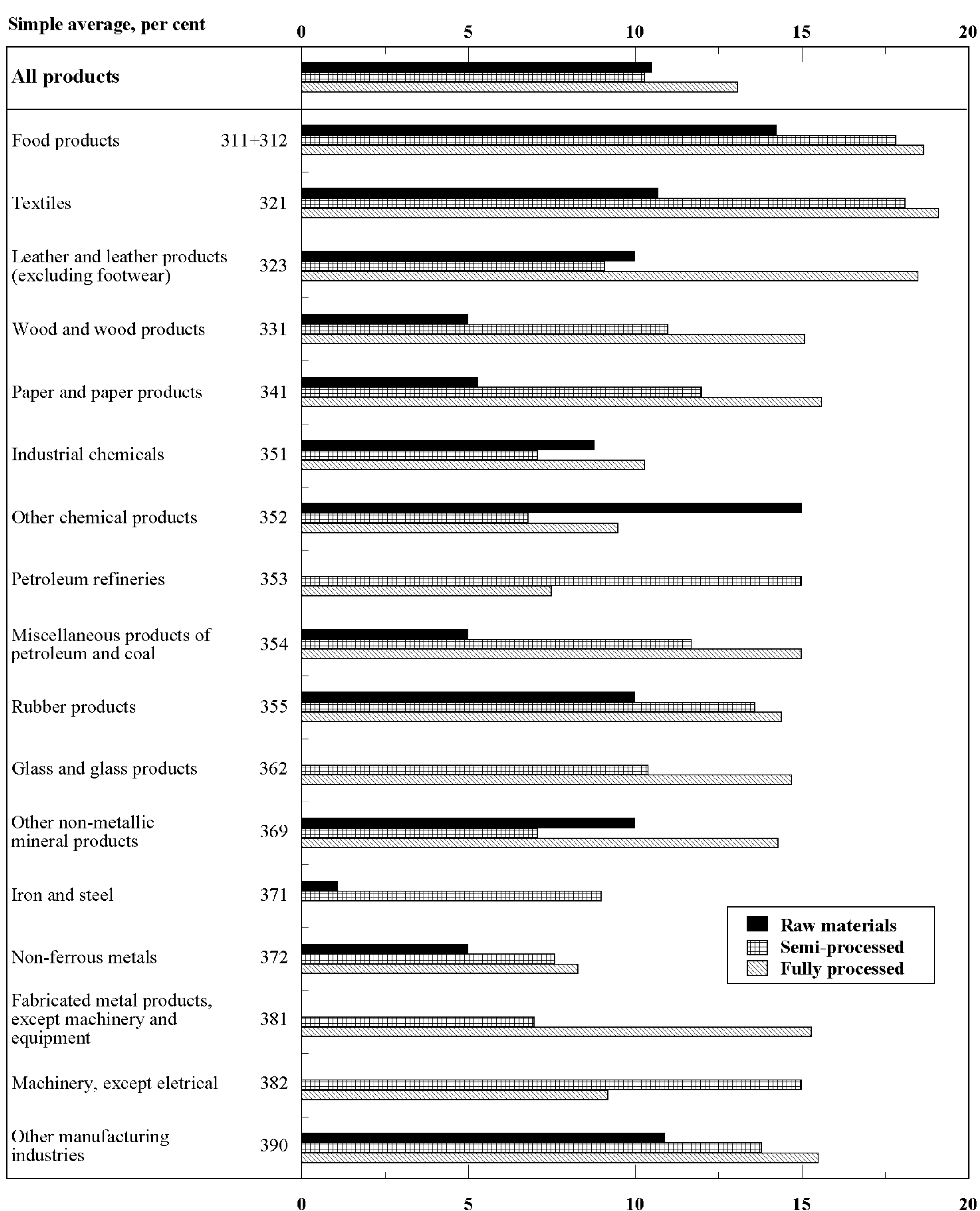
Source: O.C.E.I., Encuesta Industrial Anual; and WTO Secretariat calculations.

(i) Policies affecting manufacturing

116. Tariffs are not neutral across industrial sectors: tariff averages for manufacturing industries (defined at two-digit ISIC level) vary between 7.6 per cent for professional and scientific equipment to 18 per cent in food and beverages and in textiles and clothing (Table AV.1). Tariff peaks also occur in transport equipment, which are also excluded from Venezuela's Uruguay Round general commitments to bind maximum rates on manufactured goods at 35 per cent by the year 2000 (Chapter IV(2)(c)).

117. The authorities consider tariff escalation as useful to promote domestic value added. They also note that escalation is the only commercial policy instrument used for the promotion of industrial development. Tariff escalation is more obvious between raw materials and intermediates; by three-digit ISIC industry, escalation is particularly pronounced in textiles, wood products, paper products, and petroleum and coal products (Chart V.9). Strong reverse escalation occurs in a number of industries, notably other chemicals (including pharmaceuticals).

Chart V.9
Tariff escalation in manufacturing, Venezuela 1995



Source: WTO Secretariat.

118. The Stabilization and Economic Recovery Programme (PERE) notes that manufacturing has been particularly hard hit by the contraction of internal demand, high interest rates and material injury ("*daño importante")* to the textiles industry arising from unfair practices in international trade.[40] The growing debt burden on small- and medium-size enterprises is seen as particularly serious; the authorities plan to address this problem through restructuring of interest rates and repayment schedules.[41] Efforts are also to be made to help those enterprises improve quality, productivity and management practices in order to enhance their capacity to supply the large basic industries under the control of PDVSA and CVG (Chapter V(3)). CORPOINDUSTRIA is to finance technical assistance programmes and will promote cooperation among enterprises to achieve economies of scale.

119. The authorities also consider it necessary to strengthen instruments to counter "unfair" international competition. Measures to be taken, through executive decrees, include the enforcement of technical norms, penalizing under-invoicing and smuggling, as well as combating dumping and subsidies and undertaking an effective collection of anti-dumping and countervailing duties.

120. While acknowledging that the Guayana area was in the past targeted for special aid to develop basic industries, the authorities indicate that specific regional development policies no longer exist.[42] Currently, a policy of decentralization makes each region responsible for its own development policies, with the national Government playing a coordinating role.

121. According to the authorities, except for motor vehicles, sectoral policies are no longer pursued in Venezuela either to promote specific activities or to diversify production: only horizontal measures are used to foster industrial development, relying in particular on tariffs and similar measures (such as the ATPA, Chapter IV(2)(ii)(g), and free-trade zones, Chapter IV(3)(xiv)). Nevertheless, under the concept of "activity-leader groups" the State continues to promote large industrial projects through PDVSA and CVG (Chapter III(1)), hence implicitly favouring certain activities. In strategic cases, the State is to associate itself with private investors and efforts will be made to develop national suppliers and downstream processing. Care will need to be exercised that such activities are managed on a strictly commercial basis and that transactions between activities take place on "arm's length", otherwise there is a risk of implicit cross-subsidies between vertical activities with distortionary effects on the allocation of national resources (Annex V.1).

122. Industry benefits from under-priced fuels, a long standing feature of the Venezuelan market. Aid is also provided to small- and medium-sized enterprises through staff training programmes and concessional financing.[43] Potentially much more important, assistance is also provided through government-supported debt rescheduling and recapitalizations.

123. In addition, as detailed in Chapter IV, licences continue to apply to both the export and import of manufactured goods, sanitary certificates and other special requirements apply to a range of products

[40]Cordiplan (1994).

[41]This programme is to be undertaken by the Banco Industrial de Venezuela, CORPOINDUSTRIA and (non-intervened) private banks.

[42]The authorities also indicated that regional development objectives are pursued through the establishment of free-trade zones.

[43]For example, those operated by CORPOINDUTRIA, FONCREI and SOGAMPI.

such as foodstuffs, beverages, medicines and cosmetics, while other items are subject to special taxes and price equalization mechanisms, or to higher than average tariffs.

124. Notwithstanding Venezuela's significant efforts since 1989 to liberalize its economy and trade régime, remaining measures result in preferred treatment for certain manufacturing industries and, thus, the maintenance of inter-sectoral distortions. These could have effects beyond the local market, as Venezuela is in certain products an exporter large enough to influence foreign markets. On the other hand, as discussed later, the services sector has been relatively closed to foreign investment, and, to the extent that services are important inputs in the production of manufactured goods, higher costs in the services sector than exist internationally would be expected to have negative effects on manufacturing production. Moreover, services are also an important component in the delivery of manufactures to markets, and high costs in transport and insurance in particular may also affect the competitiveness of Venezuelan manufactures.

(ii) Main manufacturing industries

(a) Petroleum refineries

125. Venezuela has traditionally had an important domestic refining industry to process the country's large crude oil production (Chapter V(3)(ii)). Total capacity has changed little during recent years, although a major upgrading programme was undertaken in the early 1980s to raise the share of higher-value light products within total output. Venezuela adopted a policy of diversifying its exports by acquiring equity in overseas refineries; the strategy was aimed, first, at securing outlets for the country's large, heavy-crude deposits and, second, at lowering the country's exposure to volatile crude oil prices.[44] As a result, only about 32 per cent of domestic crude petroleum production was directly sold in 1994 to third parties in foreign markets.

126. The national oil company, *Petróleos de Venezuela S.A.* (PDVSA), is the world's third largest refiner of petroleum products.[45] PDVSA's domestic and international refineries processed an average of 1.8 million barrels per day of Venezuelan crudes in 1993, of which 47 per cent were processed in refineries outside Venezuela (Box V.1). PDVSA supplied 613,000 barrels per day of oil equivalent to the Venezuelan market in 1993: sales of refined products accounted for 61 per cent of that volume and of natural gas for the rest (Table V.9). Motor gasoline accounted for just under 50 per cent of domestic sales of refined products.

[44] However, Claessens and Varangis (1994) argue that PDVSA's downstream move has not reduced the volatility faced by Venezuela compared with the previous situation when the company was mostly a crude oil exporter; the volatility of crude oil prices appears not to be significantly higher than for refined products and both prices seem highly correlated.

[45] After Royal Dutch/Shell and Exxon.

Table V.9
PVDSA's refined production operations, 1993
('000 barrels/day)

Refining in Venezuela		
Refining capacity	1,182	
Processing level	1,017	
Products obtained:		
LPG	8	
Napthas/gasolines	368	
Kerosene	76	
Distillates	285	
Low sulphur residual	8	
High sulphur residual	272	
Special products	35	
Venezuelan local market sales		
LPG	63	
Motor gasoline	187	
Diesel	66	
Residual fuel oil	22	
Other products	38	
Total domestic market	376	
Exports		
Low sulphur residual	4	
High sulphur residual	204	
Others	422	
Refineries Abroad		
	Installed capacity	PDVSA share (%)
Germany		
Gelsenkirchen	220	50
Neustadt	140	25
Karlsruhe	140	16.25
Schwedt	170	18.75
Belgium		
Antwerp	14	50
United Kingdom		
Dundee	10	50
East Ham	25	25
Sweden		
Nynäshamn	25	50
Göteborg	12	50
United States		
Lake Charles	320	100
Corpus Christi	160	100
Paulsboro	84	100
Savannah	33	100
Houston	265	10
Chicago	153	50
Netherlands Antilles:		
Curaçao	310	leased

Source: PDVSA (1994).

127. Hydrocarbon-based products are considered as basic products and the Ministry of Energy and Mines is authorized to fix their wholesale and retail prices as well as transport charges. Refined products

are supplied to the domestic market at prices below production costs and well under their opportunity cost in the world market (Annex V.1).

128. Motor gasoline prices have been frozen in local currency since February 1992 and have thus fallen sharply in real and U.S. dollar terms. The authorities have given extensive consideration to increasing prices, but concerns about the political reaction of such an action had up to mid-1995 dissuaded them from raising prices. A special price regime is applied in border areas to make gasoline more expensive to foreign registered vehicles and reduce smuggling. The fishing fleet receives fuel at a preferential price and vessels under a Venezuelan flag pay lower prices than other ships.

129. Given the local availability of low-cost energy, Venezuela has historically run a highly energy-intensive economy. Primary energy requirements per GDP and per capita are higher than in most other developing countries, and the highest in the Andean region (Table V.10). This propensity is reflected in both high consumption of oil and of electricity. Internal consumption of petroleum products and natural gas amounts to about 400,000 barrels of oil equivalent per day; consumption of petroleum products has been influence

Table V.10
Energy intensities in Andean Pact countries, 1992

	TPES/GDP	TPES/Pop	Oil Req./GDP	Oil Req./Pop
Bolivia	0.41	0.28	0.25	0.17
Colombia	0.53	0.68	0.29	0.37
Ecuador	0.46	0.54	0.43	0.50
Peru	0.35	0.33	0.27	0.26
Venezuela	0.82	2.36	0.37	1.05

Note: TPES (total primary energy requirements) and oil requirements are in tonnes of oil equivalent and GDP is in thousand U.S. dollars.

Source: International Energy Agency (1994) by the level of economic activity and a policy of encouraging the substitution of oil by natural gas.

130. PDVSA faced potential difficulties in the U.S. market following the introduction at the beginning of 1995 of new U.S. gasoline regulations; the company believed that the new rules could affect up to 70,000 barrels per day of Venezuela's exports. Venezuela has initiated a dispute settlement procedure before the WTO to examine the issue (Chapter VI(1) (ii)(c) and VI(2)).

(b) Petrochemicals

131. Venezuela has a well established petrochemicals sector. These activities rely mostly on natural gas as fuel and feedstock, although imported inputs are also important. As a group, they accounted for just over 15 per cent of manufacturing value in 1992 (Table V.7 and V.8).[46] Some industries in this group are significant exporters (e.g., fertilizers), but petrochemicals as a group is a net importer. Tariffs for petrochemicals escalate from 5 to 15 per cent. The lower level applies to raw materials and basic feedstocks, most intermediates bear a 10 per cent rate, while finished products (mainly plastic resins) are subject to a 15 per cent tariff. Some consumer products, such as soaps and perfumes, and rubber products bear a 20 per cent tariff (Table AV.1).

[46]Including ISIC industries 351 through 356, except 353.

132. Production rose steadily form 540,000 tonnes in 1979 to close to three million tonnes in 1993. After years of poor results, the state petrochemicals producer, Pequiven, a PDVSA subsidiary, has become consistently profitable. Pequiven operates three petrochemical complexes, with an annual output of close to 2.5 million tonnes. It also has two subsidiaries and participates as a shareholder in some 16 joint ventures with the private sector. At present some 60 per cent of total output is geared towards the domestic market, but exports have increased sharply from US$242 million in 1991 to US$512 million in 1994. Production of oxygenates (methanol and MTBE) and olefines has increased significantly, while production of fertilizers and inorganic chemicals such as ammonia and sulphuric acid have remained stable (Table V.11).

Table V.11
Selected indicators of industrial production
('000 tonnes unless otherwise indicated)

	1988	1989	1990	1991	1992	1993	1994
Aluminium	425	539	598	605	570	575	…
Ammonia	641	647	666	547	491	651	615
Cement	6,199	5,269	6,005	6,339	6,585	6,869	…
Fertilizers	1,132	1,056	1,011	1,024	947	937	975
Methane	…	…	…	…	…	…	582
MTBE	…	…	…	333	438	414	510
Olefins	235	199	243	197	197	303	462
Plastic resins	228	192	217	213	252	288	294
Raw steel	3,646	3,196	2,997	3,304	4,263	4,000	…
Sulphuric acid	172	163	210	277	253	232	207
Tyres ('000 units)	5,203	4,177	3,951	4,710	4,696	5,119	…
Vehicle production ('000 units)	…	…	…	73	92	93	…

… Not available.

Source: Government of Venezuela, Economist Intelligence Unit (1995), Cepal (1995) and ILAFA (1995).

133. The Stabilization and Economic Recovery Programme (PERE) envisages the further development of the petrochemicals industry in two stages. First, efforts are to be made to improve the profitability of existing plants through, among other things, better operational reliability, infrastructure improvements, cost reductions and financial re-organization. Later, it is envisaged to install new capacity to produce methane and ethane derivatives, expanding annual capacity from 4 million tonnes in 1993 to some 11 million tonnes by the year 2002. The industry is also to be re-organized to increase private participation. Pequiven is already engaged in an investment programme, worth close to US$6 billion, aimed at increasing export capacity, with private investors playing an important role in the programme.

134. The PERE also contemplates the introduction of market prices for medicines, extending to the whole production-marketing chain, aimed at promoting competition and a better supervision by the State.[47] Hydrocarbon fuels and medicines are exempt from the wholesale and consumption tax (Chapter IV(2)(vi)).

[47]Cordiplan (1994), p. 77.

135. Since petrochemicals are not considered to be "traditional" exports, they qualify for export incentives (mainly duty drawbacks). Pequiven's legal statutes provide it with a number of tariff exemptions. However, the authorities have pointed out that the scope of such exemptions is limited by national and Andean legislation.[48] Polystyrene imported from the United States was subject to provisional anti-dumping duties in 1993; definitive duties were imposed in 1994.

(c) Basic iron and steel

136. With the intent of stimulating the development of secondary metal-using industries and the further processing of the country's large iron ore deposits (Chapter V(3)(b)), the Government began establishing an integrated steel industry in the mid-1960s. From its inception, the industry developed within an import substitution policy, requiring producers to give priority to supplying the needs of the domestic market; high trade barriers resulted in a large but internationally uncompetitive industry.

137. However, as part of the general trade reform, trade barriers began to be lowered in 1989, and tariffs, averaging 8.7 per cent are now below the manufacturing average of 12 per cent. As a result imports have increased reaching US$291 million in 1994. Exports are also substantially larger (US$647 million in 1994), the main destinations being the Andean Group, other South American countries, Mexico and the Caribbean. In recent years, the industry appears to have placed excess production on external markets during periods of slow domestic demand (Chart V.10).

138. Sidor, a CVG subsidiary, operates the oldest and largest steel mill; it is Venezuela's largest manufacturing enterprise after Petróleos de Venezuela, S.A. Annual capacity was raised from 1.2 to 4.8 million tonnes in the late 1970s, but there were serious teething problems and the build-up in output took much longer than initially envisaged. Sidor produced about 4 million tonnes of raw steel in 1993, of which some 1.5 million tonnes were exported.

139. Other producers in the industry include Sivensa, Venezuela's largest, publicly-traded steel-maker. The company plans to invest some US$90 million to raise production capacity of hot briquetted iron for export markets. Another company, *Venezolana de Ferrosilicio*, has an installed capacity of 55 million tonnes per year of ferrosilicon; about two-thirds of the production are exported.

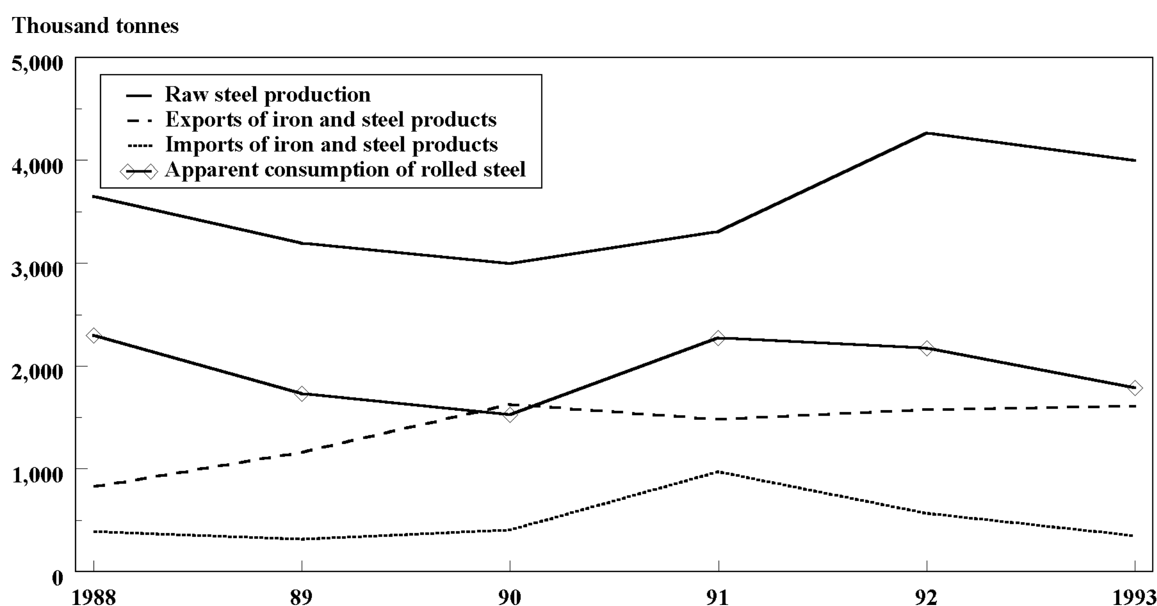
140. The trade liberalization programme has impacted seriously on the industry and major efforts have recently been necessary to restore its financial viability. A reconversion programme was completed in 1993 to close obsolescent facilities, reduce the work force and rationalize the product range. Domestic prices are also being adjusted to reflect conditions in world markets. As part of this programme, the Government assumed responsibility for Sidor's US$1.5 billion debt in 1991, capitalizing 60 per cent and extending SIDOR a 15-year loan to cover the remainder. Privatization plans are in place but the search for private investors has not started.

141. The Stabilization and Economic Recovery Programme (PERE) foresees the CVG undertaking "strategic associations" (joint ventures) for the modernization of existing steel plants and the establishment of new ones, notably a seamless tubes plant. Downstream associations, aimed at adding value to iron ore, are also to be promoted.

142. Sidor's legal statutes provided it until 1989 with a number of tax exemptions. Sidor also benefited from low-cost natural gas and electricity supplies but a process of gradual adjustments, started

[48]Decree 239 and Decision 282 of the Commission of the Cartagena Agreement.

Chart V.10
Production, consumption and trade of steel products



Source: ILAFA (1995), SIDOR (1993); and WTO estimates.

in 1989, has, according to the authorities, brought prices up to world levels. Export bonuses were paid on steel exports and all other "non-traditional" export, until 1991; loss-making firms like Sidor have been able to carry forward the associated tax benefits beyond 1991. Although export licensing has never used in practice, some steel products may be subject to such requirements to ensure the availability of supplies for the local industry. Steel profiles from Poland and Romania were subject to a dumping investigation in 1993; it was terminated in 1994 without duties having been imposed.

(d) Aluminium

143. Based on the availability of inexpensive electricity and locally-produced bauxite, Venezuela has emerged as an internationally competitive aluminium producer.[49] Aluminium production peaked in 1991, falling afterwards as a result of production problems (Table V.11). The industry accounts for a large share of total manufactured exports; main export markets were the European Union, Colombia, Japan, Mexico and the United States. Imports are small and tariffs (5 per cent) are below average. Despite its cost advantages, profitability is low, reflected in a low value-added relative to output. However, in recent years there have been increases in downstream investment and value-added production from both State-owned smelters and private companies. Output per employee is among the highest in manufacturing, reflecting the high capital intensity of the industry.

[49] Reportedly, it costs only US$0.47 per pound to produce aluminium in Venezuela; for comparison, using the most modern technology, costs average $0.65 per pound in Germany (The Economist, 18 January 1992).

144. In 1992 and 1993 production of alumina from bauxite amounted to some 1.5 million tonnes, of which about 80 per cent was absorbed by the domestic market. Output capacity is currently being expanded to 2 million tonnes per year, with further increments scheduled for the 1990s. The primary aluminium industry is dominated by companies with state participation: Venalum and *Aluminio del Caroni S.A.* (Alcasa).[50] Alumina is also produced by the state-controlled firm, Ineralumina. The latter operates an alumina plant which came on stream in 1983. Interalumina has now completed the process of replacing the imported bauxite with supplies from Bauxiven (Chapter V(3)(c)).

145. Venezuela's first plant for reducing alumina (the main input in aluminium production) to aluminium was established by Alcasa in 1967; capacity has progressively expanded to reach 210,000 tonnes per year. Venalum came on stream in 1973, with a capacity of 280,000 tonnes per year, now expanded to 430,000 tonnes per year. Venalum incurred losses between 1991 and 1993, production costs having fallen but not enough to allow the company to make a profit in the highly competitive international market.[51] Some 78 per cent of the production was exported (about 50 per cent went to Japan, 25 per cent to Europe and 20 per cent to the United States). Most sales are made under long-term contracts, mostly with companies with which Venalum has corporate links. In 1994, production reached record levels and profitability was restored.

146. The industry's difficult financial position is due in great part to high levels of indebtedness. To address this problem, a process of consolidation was undertaken which resulted in Bauxiven, Venalum and Interalumina merging in 1994 to create CVG Bauxilum, C.A. In an effort to improve short-term cash flows, Interalumina has increased alumina exports, which the authorities have indicated is expected to continue in order to increase capacity utilization, sales volumes and profits. However, the profitability of exports appears to be significantly lower than that of domestic sales.[52]

147. To decrease the Government's large losses in the firms operating in the aluminium industry, the Stabilization and Economic Recovery Programme (PERE) calls for CVG to open up the industry to private capital. The development strategy envisages lifting industry output to 2 million tonnes per year by the end of the century, but its implementation has been slow because of low international prices for aluminium and uncertainty about economic developments in Venezuela.

(e) Motor vehicles

148. The motor vehicle assembly industry was established in Venezuela on the basis of a highly protective policy, consisting of higher tariffs, import restrictions, local plant plans (based on tariff reductions for parts, limited to local value added - see later), and export incentives. Labour productivity is high compared with many other local industries, but profitability is low. The industry has achieved some export success, with the authorities indicating that the value of exports reached some

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[50]Alcasa is a joint venture of CVG and a U.S. minority partner (Reynolds); Venalum is a joint venture between CVG and various japanese and U.S. companies as minority partners.

[51]Production costs fell to US$1,281 per tonne in 1993, when the average LME cash price was US$1,139 per tonne.

[52]In 1993, Interalumina domestic sales amounted to 1,176,000 tonnes with a value of Bs 21,560 million; equivalent figures for exports were 300,000 tonnes and Bs 4,080 million. The implicit unit values were about Bs 18,330 per tonne for domestic sales and Bs 13,580 per tonne for export sales: unit revenues for domestic sales thus appear to be one-third higher than for exports. Total production costs in 1993 were US$198.44 per tonne, equivalent to some Bs 18,024 per tonne (CVG, Interalumina, Inform Annual 1993 and WTO estimates).

US$746 million in 1994. That year, imports by the industry amounted to US$1,521 million, with parts for vehicle assembly totalling US$591 million.

149. Registrations increased rapidly in the mid-1980, but demand plummeted in 1989 due to the devaluation and lower real incomes. Assemblers shut down their plants for long periods; multinational companies had to make large capital injections into their local affiliates, leading to the disappearance of domestically controlled assemblers. A recovery in demand began in 1990.

150. A new motor vehicle policy was launched in 1990 giving the industry three years to adapt to more open external competition; the programme called for lower tariffs and reduced local content requirements. At 14 per cent, the tariffs for the industry as a whole are higher than the manufacturing average (12 per cent), and certain vehicles are subject to the highest rate in Venezuela' s tariff schedule, (35 per cent). The new policies also envisaged the free importation of new and used buses, and of new and used medium and heavy commercial vehicles, provided they were identical to locally produced models. Liberalization was accelerated in 1991 with the tariff rate on passenger cars with engines of up to 3000cc cut immediately from 40 to 25 per cent. As a result, the volume of imported vehicles increased, as did the number of assemblers.[53] More recently, car sales have been adversely affected by the raising of stamp taxes, the imposition of a new sales tax, the currency devaluation of the first half of 1994 and the later imposition of exchange controls.

151. Liberalization suffered a setback in 1993 with the harmonization of automotive policy within the Andean Pact. According to the authorities, motor vehicles is the only industry benefiting from special treatment, which, they argue, is made necessary by the high degree of protection the industry receives in industrialized countries. Under the new policy, motor-vehicle assembly plants complying with minimum local content requirements benefit from a concessional tariff rate of 3 per cent on imported Completely Knocked-Down kits (Chapter IV(2)(ii)(g) and IV(2)(xviii)). For participation in the scheme, the Ministry of Development has certain reporting requirements. The minimum local content is set at 30 per cent in 1995 for passenger cars and, generally, vehicles with a capacity of up to 16 persons or a weight of 4.5 tonnes; it is set at 15 per cent for other vehicles. These requirements are to gradually rise to 33 and 18 per cent by the year 1998.

152. The formula to calculate local content takes into account purchases of domestic vehicle parts, the value added of exported parts and vehicles, and the value of imported materials.[54] The scheme not only supports the use of locally produced parts over imports but provides an implicit subsidy to the export of parts and vehicles. Benefits to local assemblers using the scheme result from the lower tariff on imported kits vis-a-vis imported parts or assembled vehicles. Although the scheme is voluntary, most assemblers (14 firms in all) have joined it.

[53] Mitsubishi of Japan began local assembly in 1991 and Lada of Russia in 1992.

[54] Resolution 0001, 2 January 1995. Under the resolution, local content in percentage terms is computed from the expression (IN+ Vex)/(IN+ Mim)*100, where IN represents the purchases of domestic parts (or degree of national integration), Vex is the valued added in exports of parts and vehicles, and Mim is the value of imported materials. The value of Vex in the formula must not exceed 25 per cent of the minimum local content established for each vehicle category. As in practice that maximum is usually exceeded, the authorities consider that taking into consideration exports in the computation of local content has only a minor effect.

153. Passenger cars and motorcycles may be subject to a luxury consumption tax at a rate of 10 or 20 per cent on value depending on their price or engine capacity (Chapter IV(2)(vi)). Imports of used motor-vehicles other than those used in public transport are prohibited (Chapter IV(2)(ix)). Public transport equipment is exempt from the wholesale and consumption tax (Chapter IV(2)(vi)).

(f) Other industries

154. Venezuela has a large and well established food processing and beverages industry, protected by tariffs averaging some 18 per cent. The main imports are dairy products, animal and vegetable oils and fats and spirits. Canned fish (tuna) is the main food export (Chapter V(2)).

155. A modest textiles and clothing industry has been set up behind high tariffs, averaging 18 per cent for the sector as a whole; exports are modest (US$40.3 million), while imports exceed US$300 million (Tables V.7, V.8 and AV.1). The industry generates a large number of jobs, equivalent to some 11 per cent of manufacturing employment, but labour productivity, wages and profitability are below average.

156. While Venezuela never joined the Multifibre Arrangement, it has retained the right to use the transitional safeguard mechanism provided for in Article 6 of the WTO Agreement on Textiles and Clothing.[55] In that respect, Venezuela submitted a list of products accounting for just over 16 per cent of its 1990 volume of textile and clothing imports, and which are to be included in the first phase of integration under that Agreement.[56]

157. A medium-sized cement industry has also developed behind a below average tariff of 7.5 per cent, and total cement production reached almost 7 million tonnes in 1993 (Table V.11). The largest company, *Venezolana de Cementos* (Vencemos), produced approximately 50 per cent of that total, of which it exported about 1 million tonnes. A second firm, *Cementos Caribe*, produced about 900,000 tonnes of which some 400,000 were exported. A controlling stake in Vencemos was purchased in 1993 for about US$300 million by *Cementos Mexicanos.* Cement from Mexico was the subject of a dumping investigation initiated in 1992 and terminated in 1994; no anti-dumping duties resulted.

(6) Services

158. The services sector accounted for about half of Venezuela's GDP in 1993 and generated just over 60 per cent of total employment. Commerce, restaurants and hotels were responsible for the largest share of value added in the services industries, followed by financial and business services (Chart V.11).[57]

159. Non-factor service exports (credits) were valued at just under US$1.5 billion in 1993, or one-tenth the value of merchandise exports; tourist receipts were the largest single item, accounting for 37 per cent of service exports. Service imports (debits) were much larger at US$4.7 billion, equivalent to some 47 per cent of merchandise imports. Travel accounted for 44 per cent of service imports, and freight

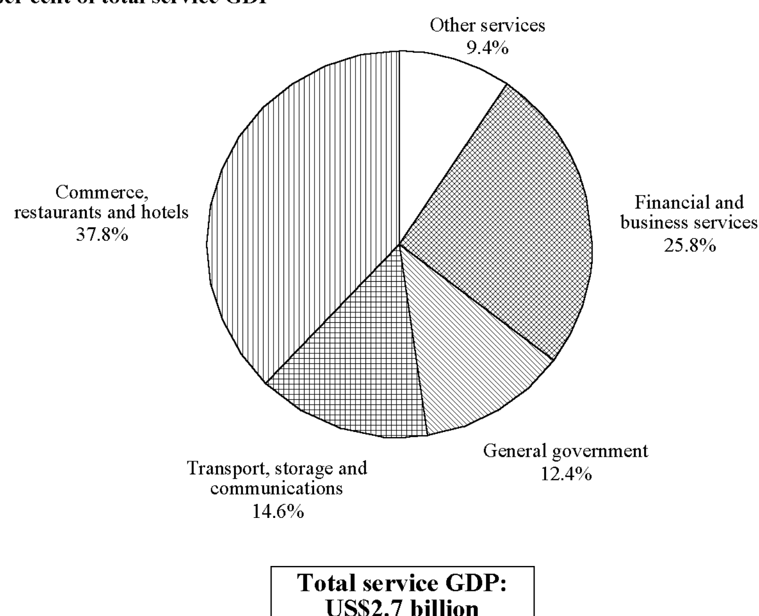
[55] WTO document G/TMB/N/29, 6 March 1995.

[56] WTO document G/TMB/N/54 28 April 1995.

[57] Data from the Central Banks show the share of services in GDP at 45 per cent and in total employment at 63 per cent. Estimates in Chart V.11 are subject to revision.

Chart V.11
Value added in services, 1993

US$ billion and per cent of total service GDP



Total service GDP:
US$2.7 billion

Source: International Monetary Fund.

and insurance for 29 per cent.[58] Venezuela's exports of commercial services were estimated to have increased only 18 per cent in nominal terms between 1983 and 1993; in contrast, service imports rose by some 74 per cent during the same period.[59] As a result, there was a considerable widening of the service trade deficit.

160. Inefficiencies in the services sector have at times imposed severe constraints on the rest of the economy. In the past, poor port handling was an impediment to non-oil exports, the telecommunications industry was backward and inefficient, financial services were poorly supervised with low profitability, and domestic tourist destinations were internationally uncompetitive. The ambitious restructuring process in train since 1989 has produced considerable gains in some areas; however, reform of the legal framework, necessary to support broader progress, has been slow and ongoing efforts are yet to produce significant improvements in key industries such as banking.

161. The State is an important supplier of services, including electricity, banking, insurance, transport, tourist facilities and, to a lesser extent, telecommunications. Such involvement is expected to decrease as the current privatization programme moves forward, aided by the recent, comprehensive opening to foreign investment of major industries such as banking, insurance and telecommunications.

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[58]Values and shares based on data provided by the authorities.

[59]GATT (1994); increases estimated from values in current U.S. dollars.

162. In the context of their ongoing efforts to attract foreign investment and liberalize the services sector, the authorities regard as important Venezuela's participation in the General Agreement on Trade in Services (GATS). This is based largely on the expectation of a long-term expansion of international trade in services and the growing linkage between trade in services and economic development.

163. The schedule concluded by Venezuela under the Uruguay Round GATS includes one major reservation in the section of "horizontal" commitments, whereby Venezuela reserved its right to apply limitations on market access and national treatment in all sectors included in its schedule. Exceptions were made for measures affecting the entry and temporary stay of natural persons in certain categories: administrative staff, managers and executives; specialists; and sellers of services (except in the financial service sector). All such categories are nevertheless subject to requirements and limitations, especially those laid down in the labour law.[60]

164. Among other agreements on services referred to by the authorities was the Free Trade Agreement of the Group of Three (*Tratado de Libre Comercio del Grupo de los Tres*),[61] which includes m.f.n. and national treatment clauses, as noted in Chapter II. The Cartagena Agreement covers tourism development, road transport, air transport and multi-modal transport. Other agreements concluded by Venezuela are those on the mutual recognition of higher education diplomas among Latin American and Caribbean countries (joined by Venezuela in 1976)[62]; educational, scientific and cultural integration (1990);[63] and the recognition of academic degrees (1911).[64] In addition, there are agreements on air transport; consulting, technology exchange and distribution services for petroleum; on film co-production as well as a number of treaties opening the way to specific service agreements, including the Economic Complementarity Accord (*Acuerdo de Complementación Económica*) with Chile and Brazil and the Trade and Investment Accord with CARICOM.

(i) Financial services

165. Under the GATS, Venezuela made specific commitments with respect to financial services (insurance and banking). In general, Venezuela accepted few engagements either in market access or national treatment, reserving its rights to maintain limitations on foreign participation in those activities. However, the restructuring of its financial system permitted Venezuela to make substantial improvements in its initial offer during the negotiations on Financial Services undertaken under the Ministerial Decision at Marrakesh. As a result, Venezuela accepted to bind market access for foreign financial institutions (including banking and insurance) with up to 100 per cent foreign ownership,

[60]Limitations included requirements that chiefs of industrial relations or personnel, captains of ships or aircraft and supervisors be Venezuelan nationals; that 90 per cent of the personnel of an enterprise be nationals; and that the total remuneration paid to foreigners, including manual workers and employees, does not exceed 20 per cent of the total remunerations paid in either category. The Ministry of Labour may authorize temporary exceptions to these provisions.

[61]Colombia, Mexico and Venezuela

[62]Thirteen countries participate, including the Holy See and Slovenia.

[63]The members of this agreement, *Convenio Andrés Bello*, are Bolivia, Chile, Colombia, Ecuador, Panama, Peru, Spain and Venezuela.

[64]Members are Bolivia, Colombia, Ecuador, Peru and Venezuela.

national treatment with regard to commercial presence of such institutions, and cross-border supply for reinsurance services.

166. In relation to financial services, the only measure in Venezuela's list of m.f.n. exemptions concerns the reciprocal treatment that may be requested for Venezuelan capital in a foreign country. These exemptions apply to all countries and have a duration of ten years.

(a) Banking and non-insurance financial services

167. The legal and regulatory framework of the financial system in Venezuela was, until the introduction of the new banking law in 1994, based on the principle of specialized banking. This resulted in a large number of institutions, just over 150 prior to 1994 (Table V.12). Nevertheless, the system was relatively concentrated, with the largest six commercial banks accounting for just over half of the total assets of the system.

Table V.12
Structure of the Financial System (except insurance), December 1993

	Main offices	**Branches and Agencies**	**Total Assets (billions of bolivares)**
Total	155	2,646	2,795.2
All commercial banks	47	2,261	2088.6
Foreign commercial banks	5	0	17.7
Other banking	37	335	310.8
Mortgage banks	16	71	171.0
Savings and loan system	20	257	120.9
Specialized banks[a]	1	7	18.9
Other financial institutions	71	50	396.7
Finance companies	37	50	285.5
Leasing companies	34	0	111.2

a Workers' Bank, dissolved end 1993.

Source: International Monetary Fund.

Box V.6 Commitments in Financial Services
Insurance

Venezuela made specific commitments with respect to three insurance services: (i) life and non-life insurance, (ii) reinsurance and (iii) insurance and reinsurance brokerage.

With respect to market access, Venezuela did not engage itself to accept cross-border supply in (i) and (iii). For risk reinsurance (ii), it agreed, subject to the authorization of the Insurance Superintendency, to allow foreign firms to maintain permanent representations and brokerage companies to represent firms not domiciled in the country; the Finance Ministry may prohibit reinsurance operations with specific companies. Venezuela did not commit itself to permit consumption abroad for (i) and (iii), while in (ii) the Finance Ministry may prohibit companies operating in the country to undertake transactions with specific companies.

In the three activities, the commercial presence of service providers is constrained by a prohibition on foreign subsidiaries, a condition that establishment authorizations be subject to the country's economic situation, possible reciprocity requirements. Staffing criteria are also established concerning the composition of management boards and executive personnel. Such staffing restrictions extent to service delivers through the presence of natural persons, with Venezuela not committed to accept the presence of foreign nationals.

With respect to national treatment, no bindings were made concerning the presence of natural persons in any of the three activities, except as agreed under horizontal commitments. Venezuela did not make commitments on cross-border supply or consumption abroad for (i) nor (iii), but no limitations with respect to those two forms of supply were placed on (ii). Venezuela assented not to place restrictions on commercial presence of any of the three activities.

Other financial services

Venezuela made specific commitments with respect to the following financial services: (i) banks and credit institutions, (ii) foreign exchange houses, (iii) capital markets, (iv) mutual fund management companies, (v) investment advisory services, (vi) securities brokerage and (vii) other banks and credit institutions, insurance and capital market.

With respect to market access, Venezuela agreed not to limit cross border supply in (vii), but made no commitment in the other six activities. It did not commit itself to permit consumption abroad with respect to (i), (ii) and (iv), but it agreed not to place limitations in the other four.

Except in (vii), reservations were made in all activities to limit the commercial presence of service providers. Such reservation include:

- reciprocal treatment may be required in the six activities;.
- for (i), authorizations, contingent on the country's economic situation, are required from the Bank Superintendency. The establishment of foreign-owned firms or subsidiaries, or firms incorporated overseas also requires the authorization of the Superintendency. Offices representing foreign firms not domiciled in Venezuela are only permitted to act as intermediates between the parties to a credit transaction. The Superintendency must authorized their change of address, closing or designation of representatives; those offices may not advertise their activities;
- for (i) and (ii), no less that half of the management board must be residents in Venezuela;
- for (iv), firms may not manage investment mutual funds with similar investment targets and sales plans; third parties managing mutual funds established in Venezuela must be incorporated in the country;

Box V.6 cont'd

- for (v), authorizations to serve as advisor on foreign securities, or establish contact with or represent foreign brokers are conditioned on the country's economic situation being appropriate for such services, as appraise by the Securities National Commission which may revoke authorizations if the situation changes; and
- for (vi), authorizations to offer foreign securities depend on the Government's opinion that granting them is in the national interest; the managers of brokerage firms must be residents in Venezuela.

Venezuela made no commitment to accept the presence of foreign nationals, except as indicated in its horizontal commitments. For (i) and (ii), it specified that at least half of the board members should be residents in Venezuela; in (vi), the same condition is required of managers of brokerage firms.

With respect to national treatment, Venezuela made no commitment to allow cross-border supply except in (vii). It made no commitments either with respect to consumption abroad in (i), (ii) or (iv), but agreed not to place restrictions in the other four activities. Except as provided in its horizontal commitments, for all seven activities Venezuela agreed not to place restrictions on commercial presence but did not engage itself to allow the presence of natural persons.

168. Commercial banks have traditionally formed the core of Venezuela's financial system, although other institutions operate in the money market, including mutual funds and consumer finance companies.[65] Financial firms in the capital market embrace mortgage banks, savings and loans entities and investment companies that extended credit to the industrial, agricultural and construction sectors. Among other private institutions, there are also investment houses, brokerages and savings banks.

169. The non-insurance financial system also includes several State-owned institutions channelling resources into the development of basic sectors. For example, Petróleos de Venezuela S.A. finances oil sector projects, the Venezuelan Corporation or Guayana (CVG) finances the mining and metallurgical sector, the Agriculture and Stock-raising Fund directs funds to the agricultural sector, and the Industrial Credit Fund and the Corporation for the Development of Small and Intermediate Industry finance the industrial sector. The National Housing Institute and the Urban Development Fund promote financing for the construction of low-income housing. The Investment Fund of Venezuela (FIV) has a key rôle in the process of privatization of public enterprises.[66]

170. Inspection, supervision, regulation and control of banks and other financial institutions is the responsibility of the Bank Superintendency (*Superintendencia de Bancos y otras Instituciones Financieras*). The Superintendency is attached to the Finance Ministry but is financially independent and has its own legal status. It oversees authorizations for the establishment of banks and other financial institutions, including the incorporation in Venezuela of branches of foreign institutions (Chapter

[65]Consumer finance companies were allowed under the former banking law to offer secured loans with commercial guarantees as well as credit for the purchase of travel tickets, vehicles, tourism and related activities.

[66] The FIV was established to re-invest surplus funds after the 1973 dramatic rises in oil prices but, since there were no important domestic projects at the time, the funds were placed in the foreign market and later returned to finance strategic domestic projects (Báez and Reyes, 1993, p. 71).

III(2)(ii)(b)). In addition to the Superintendency, the Central Bank and the Deposit Insurance Agency (FOGADE) play also major roles in the sector's operation and current restructuring efforts.[67]

171. Until the entry into force of the new banking law, there were severe restrictions on the entry of foreign banks; between 1975 and 1993, none were permitted except for Latin American institutions under reciprocal agreements. As a result, foreign banks have played a minor role in Venezuela's banking system. While some foreign investment has occurred since the introduction of the new legislation, it is too early to observe significant growth in foreign participation in the sector (Chapter III(3)).

172. The macroeconomic adjustment programme of 1989 (Chapter I) included legislative reforms to strengthen bank supervision and prudential standards governing financial institutions. The authorities submitted the proposed reforms to the legislature in mid-1991 but passage proved contentious and exceptionally lengthy (Box V.7). Furthermore, the macroeconomic reforms initially had a negative impact on the financial sector, as reduced economic activity and higher real interest rates led to an increase in non-performing loans, and currency devaluations undermined banks with significant net foreign exchange exposures.

173. A major crisis finally erupted in 1994, when the authorities were compelled to nationalize or close about one-third of the 47 banks in operation (Box V.8). According to the Venezuelan authorities, the string of bank takeovers during 1994 left the State with control of 50 per cent of the banking system, the banks affected accounting for about half of total bank deposits and including three of the five largest banks in terms of deposit shares. Given the close inter-corporate links in the financial system, the crisis spilled over to other parts of the financial sector. In the Stabilization and Economic Recovery Programme of 1994 (PERE), the authorities attributed the crisis to the lack of supervision by the Bank Superintendency, a poor-quality loan portfolio, low capitalization indices, excessive protection of national firms, and absence of timely reform of the banking law.

174. The direct fiscal cost in terms of spending to recapitalize or support ailing institutions or to pay depositors has been estimated at some US$9 - 11 billion, or some 13 per cent of GDP. The ultimate fiscal cost could be significantly higher, depending in part on the success of current efforts to restructure nationalized banks in a manner that re-establishes their financial viability. This will involve, inter alia, substantial reductions in overheads and branch networks, which are considered to be far too large.

[67]FOGADE was created in 1985 to provide insurance for local currency, private deposits and short-term financing at market rates to help restructure ailing financial institutions.

Box V.7 The banking law of 1994

A new Law for Banks and other Financial Institutions came into effect at the beginning of 1994 (Law-Decree 3228, Official Gazette 4649, 29 November 1993). Activities covered by the law include those of commercial banks, mortgage banks, investment banks, financial leasing companies, money market funds, foreign exchange bureaus and financial groups. The law establishes, regulations on minimum capital adequacy for each type of institution: for universal banks Bs 3 million, for commercial banks Bs 1.2 billion, for investment banks Bs 700 million and for mortgage banks Bs 600 million.

Authorization is required from the Bank Superintendency for establishing, closing or moving overseas branches, subsidiaries or affiliates of commercial banks incorporated in Venezuela; commercial banks also require authorization to acquire shares of banks incorporated abroad for amounts exceeding 20 per cent of the domestic bank's capital. Funds obtained in Venezuela by commercial banks may be used for investment and credit operations abroad, provided they do not in total exceed twice the bank's capital and reserves. The Central Bank may suspend or limit such operations for reasons of monetary policy.

The new law allows the establishment of universal banks, defined as those undertaking all the specialized transactions covered by the banking law, including international transactions. The Bank Superintendency may authorize universal banks resulting from the merger of specialized banks, the transformation of a specialized bank, or through the normal establishment procedures for new banks (Chapter III(2)(ii)(a)). Universal banks are subject to limits on investment abroad and the acquisition of shares; constraints also apply to type and amount of non-guaranteed current account credits and mortgages.

In order to address liquidity problems, or if the shareholders cannot produce the necessary capital within a specified period, the law provides for the Bank Superintendency to intervene in the financial institution by designating new administrators with broad powers to manage, dispose of, control and oversee the institution in question. Subsequent measures are coordinated with FOGADE and may include the rehabilitation, merger, or liquidation of the institution. Explicit provision for participation by foreign banks or investors is made; such participation is contingent on financial aid not being required from FOGADE. Liquidations involve first paying off mortgage credits and other preferential credits, followed by personal savings of up to Bs 100,000. The liquidation of a foreign bank would entail giving priority to persons domiciled in Venezuela.

The banking law establishes a special levy to finance the operations of the Bank Superintendency. The levy is set between 0.2 and 0.3 thousandths of the institution's average assets during the previous fiscal year, the precise contribution being set by the Superintendency's Council.

Box V.8 The banking crisis

Prior to the crisis of 1994, the banking sector was subject to powerful distortive forces over an extended period. The proliferation of specialized banks had led to the development of financial groups with high cost structures and poor profitability. The Central Bank fixed interest rates administratively, resulting in negative real earnings and decreased demand for domestic financial assets. The requirement that commercial banks channel part of their credit portfolios into specified sectors, such as agriculture, resulted in inefficient assignment of funds

There were also major weaknesses in the supervisory and regulatory framework governing financial institutions. The Bank Superintendency focused on monitoring formal compliance with banking regulations, rather than analyzing the solvency of financial institutions. Monitoring of financial groups proved extremely difficult: institutions were seldom monitored at group level and problem loans or losses could be diverted to institutions within the same group in order to escape strict supervision or prudential regulations. Bank interventions were administratively complex, solutions to problems were slow and often partial, prudential norms were not adequate and offshore operations were not properly monitored. (Government investigators were reportedly looking into the offshore holdings of Banco Latino, the first casualty of the crisis: bankers said that the practice of dumping non-performing loans into offshore subsidiaries had not been uncommon - Financial Times, 19 January 1994).

The deteriorating situation became a crisis in mid-January 1994 when the country's second largest bank in terms of deposits, Banco Latino, failed to meet its clearing obligations. The bank was initially closed, but reopened the following April as a state-owned bank. Following the closure of Banco Latino, other banks experienced abnormally large withdrawals and suffered liquidity difficulties; the Government kept them afloat in return for shares and other assets. This reflected the initial official policy of preventing a systemic crisis by avoiding bank closures through the injection of capital via FOGADE, financed by the Central Bank. The fiscal cost of these measures was magnified by the decision to allow depositors to withdraw deposits well above the legal guarantee provided by the law.

The auxiliary financing became a severe, spiralling burden and the authorities began closing ailing banks in mid-1994. Although depositors were compensated only in accordance with the legal guarantees, the fiscal cost was extremely high, official assistance amounting to several times the banks' capital bases. The high cost resulted in part from existing management being allowed to remain in place for some time, permitting insiders who would not have been covered by the deposit guarantee to withdraw their funds ahead of government intervention.

As the uncertainty regarding the new exchange control régime (Chapter I, Annex) intensified in the second half of 1994, so did the banking crisis; some banks experiencing large outflows from their offshore operations. In August 1994, the newly created Financial Emergency Board took measures to address the financial difficulties of a group of eight banks, including three of the six largest banks in terms of deposit shares. Measures included the de facto nationalization of Banco de Venezuela, the country's third largest bank. Plans to recapitalize other banks were drawn up, with FOGADE providing financial support to assist the banks' owners in their efforts to raise new capital. As the plans failed, the authorities nationalized Banco Consolidado and Banco Progreso, the country's fourth and sixth largest banks at the time. These interventions were conducted without closing the banks and with no restrictions on the withdrawal of funds by depositors.

175. In mid-1994, as the bank crisis deepened, the Government adopted legislation establishing a Financial Emergency Board (*Junta de Emergencia Financiera*). The Board was given responsibility for formulating and implementing policies to address the banking crisis; it comprises the heads of the Central Bank, FOGADE, the Bank Superintendency and three presidential appointees acting under

the Chairmanship of the Finance Minister.[68] The Board was given power to regulate the flow and use of funds in the inter-bank market, including the right to require banks with excess liquidity to lend to those facing liquidity shortages, a measure intended as an alternative to auxiliary financing from FOGADE; these powers have not been used. The Board may also remove and replace directors and executives, suspend an institution's licence to operate, and take over any or all of the company's shares in the name of the Government. The Banking Law empowers the Bank Superintendency to take similar actions.

176. A controversial tax of 0.75 per cent on debit transactions at banks lapsed at the end of 1994, but consideration was being given in mid-1995 to its reintroduction for business transactions but at a lower rate.[69]

(b) Insurance and other financial services

177. Venezuela's insurance industry was made up in 1994 of some 73 insurance and 11 reinsurance companies employing, respectively, some 11,000 and about 350 employees. Ten insurance companies had subscribed capital exceeding Bs 400 million and 33 companies capital of more than Bs 100 million.[70] Foreign reinsurance companies had six representative offices in Venezuela.

178. The number of insurance companies increased rapidly between 1989 and 1993, from 57 to 72; their total subscribed capital grew in real terms at an average annual rate of just over 9 per cent.[71] In 1992, the breakdown of collected net premiums, including reinsurance, was as follows: fire-related, 11 per cent; hospitalization and related, 30 per cent; life, 4.4 per cent; motor vehicles, 30 per cent; and transport, 3 per cent; other, 21.6 per cent.

179. Insurance activities are governed by a recently revised law (Box V.9), covering all insurance areas, including the operation of insurance and reinsurance brokerage companies and the activities of various specialists engaged in insurance activities. By mid-1995, new regulations to reflect the revised law had not been finalized and those dating from 1969 were still in force. Consideration was being given to the liberalization of the current system of detailed regulations affecting areas such as marketing, charges (including premiums), and policy conditions.

180. The revised legislation provides for the comprehensive opening of insurance and reinsurance operations to foreign capital, with some exceptions (Chapter III(2)(ii)(b)). Preferences remain, however,

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[68]Executive Decree 248, 27 June 1994. According to some observers, the Decree effectively gave the Government full, direct control over the country's banking system (Financial Times, 1 July 1994).

[69]Financial Times, 16 March 1994.

[70]There were also some 395 insurance and reinsurance brokerage firms, just over 4,000 insurance brokers, 12,000 exclusive agents, 116 risk inspectors, 1,600 loss settlement experts (*ajustadores de pérdidas*) and 1,100 valuation experts (*peritos avaluadores*).

[71]Between 1984 and 1993, premiums grew at an average real annual rate of about 3.5 per cent reaching a value of some Bs 141 trillion in 1993; the equivalent statistics for claims (*sinietros*) were 5.6 per cent and Bs 84 trillion

in favour of Venezuelan nationals with respect to management and the use of Venezuelan assets as reserves.[72]

Box V.9 Revised Law of Insurance Companies

The law governing insurance and reinsurance companies was extensively revised in 1995 by the Law Partly Reforming the Law of Insurance and Reinsurance Companies (*Ley de Reforma Partial de la Ley de Empresas de Seguros y Reaseguros*), Official Gazette 4865, 8 March 1995, which modified the Law of Insurance and Reinsurance Companies (*Ley de Empresas de Seguros y Reaseguros*), Official Gazette 1762, 8 August 1975.

The revised law strengthens the supervisory role of the Insurance Superintendency and establishes a special levy to finance its operations. The levy is set between 0.20 and 0.30 per cent of the net premiums collected by a company during the previous fiscal year; the precise contribution is fixed annually by the Finance Ministry. It also restructured the National Insurance Council (*Consejo Nacional de Seguros*), charged with providing advice to the Superintendency on economic and technical issues related to insurance as well as on rates and premiums that insurance companies may be required to apply.

The law has introduced a control system based on "solvency margins" to ensure that companies can honour their obligations by setting aside separate reserves based on the volume of premiums. Insurance companies are now barred from providing financial guarantees. Where a company is considered at risk, or fails to meets minimum reserve requirements, the law requires the Superintendency to direct the company to take measures to correct the situation within 90 days, after which the Superintendency is to intervene in the company; measures which may be taken subsequently include the transfer of the insurance portfolio to another company. Changes have been made to increase the protection to policy-holders through better dispute settlement mechanisms and greater transparency.

The revised law sets time limits for existing companies to adapt to the new requirements. Of the existing 73 insurance companies, only 17 meet the new minimum capital requirements in mid-1995; the other companies had until 30 September 1995 to provide half of the amount required to meet the capital norms, while the residual was to be subscribed no later than 23 December 1996. No domestic reinsurance company met the new minimum capital requirements; by mid-1995 only seven had expressed their intention to take measures to meet requirements. The securities were to be established with the Central Bank by 12 December 1996.

181. Insurance contracts concluded abroad have no effect in Venezuela unless the premiums have been paid to a company in Venezuela, in which case domestic rates remain in force. This constraint applies to personal insurance when the policy holders are domiciled in Venezuela, to insurance of property located there, and to insurance on ships, aircraft and other vehicles registered in Venezuela. Foreign companies can insure merchandise imports and exports. In principle, there is no obligation for exporters to sign contracts with domestic insurers to obtain export credit.

182. The inspection, supervision, regulation and control of insurance activities are the responsibility of the Insurance Superintendency (*Superintendencia de Seguros*), an autonomous agency attached to the Finance Ministry. The Superintendency's responsibilities cover insurance and reinsurance companies

[72]For example, under the revised law, actuarial reserves should consist of at least 30 per cent securities backed by Venezuelan national or regional authorities, or securities in bolivars backed by Latin american Governments or international financial institutions.

incorporated in Venezuela and insurance professionals.[73] It also supervises companies that do not fall under the banking law but which provide financial services to policy-holders; it may act independently in technical and accounting matters, and, when requested by the concerned parties, it is empowered to arbitrate disputes. The Superintendency has wide powers to impose fines and to initiate procedures leading to jail sentences of up to five years.

183. As a result of the crisis in the banking system, shares in insurance companies held by failing banks were acquired by FOGADE; the State has thus acquired 14 insurance companies. In some cases, insurance companies held their reserves in banks with which they had corporate links. As banks failed, associated insurance companies could no longer fulfil their reserve requirements; this is expected to result in the revocation of operating licences and liquidation of additional companies. The authorities expect the consolidation to reduce the number of insurance companies by half; a clearer picture may emerge by Autumn 1995. The restructuring of the sector is expected to offer foreign companies attractive acquisition targets, with particularly good expansion possibilities in health insurance.[74]

(ii) Tourism

184. Tourism accounted for about 3 per cent of Venezuela's GDP in 1993. The sector directly employed some 51,000 people in 1994; indirectly, it supported just under 160,000 posts (excluding food and beverage-related establishments). The number of visitors to Venezuela grew considerably during the 1980s, peaking at close to 600,000 in 1991 (Chart V.12). Overall, the number of outward bound tourists is comparable to that of visitors, and the external balance in tourist services is strongly negative, a situation that the authorities would like to reverse in the medium term.

185. Most tourists come from Europe and the United States; significant numbers also come from other American countries, notably Argentina, Brazil, Canada, Colombia and Trinidad and Tobago. The sector is believed to have considerable growth potential but Venezuela's strong currency has traditionally made it an expensive destination. Although recent devaluations have helped redress this situation, concerns about political instability and security appear to have dampened growth.

186. Although complete estimates were not available, State involvement in the tourist sector is sizeable and is widely consider to have reduced the sector's dynamism and ability to compete internationally.[75] Foreign investment has been low, although efforts are in progress to increase foreign participation. The authorities are implementing a comprehensive privatization programme designed to improve the level and quality of tourist services, with the State scheduled to either give in concession or sell all publicly-owned hotels and tourist developments by 1997; both CORPOTURISMO and the Investment Fund of Venezuela (FIV) are involved in the programme within the Framework of the New Law on Privatization.[76] Under the programmes, four hotels were privatized in 1992, one in 1994 and four are scheduled for privatization in 1996.

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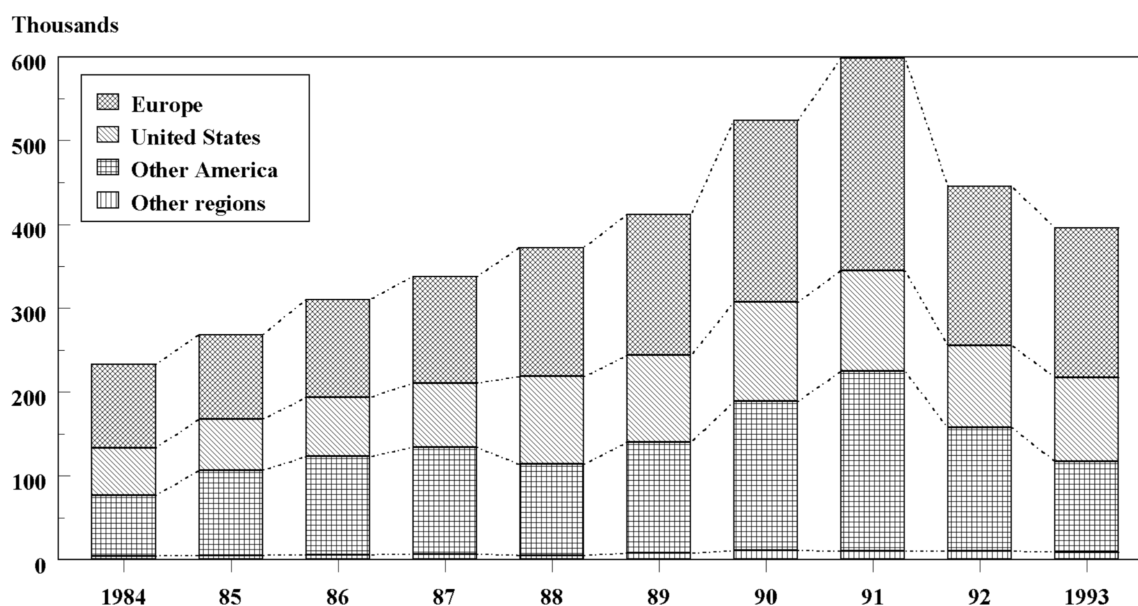
[73]These include loss settlement experts, valuation experts, risk inspectors, reinsurance brokerage societies and representatives of foreign reinsurance companies.

[74]In June 1995, Liberty Mutual acquired one of the largest insurance companies from FOGADE.

[75]CORPOTURISMO alone owns some 20 tourist accommodation properties, including 14 five- and four-stars hotels.

[76]Official Gazette No. 4634 of 22 September 1993.

Chart V.12
Tourist arrivals in Venezuela, 1984-93



Source: Ministry of Foreign Affairs.

187. Conditions for foreign investment in the tourist sector falls under the general legal framework for the treatment of foreign capital in Venezuela set out in Decree 2095 of 13 February 1992, with several public authorities involved in investment authorizations (Chapter III(2)(i)).[77]

188. Tourist activities are regulated by the Tourism Law of 1992.[78] The law charges the Tourism Corporation of Venezuela (*Corporación de Turismo de Venezuela*, CORPOTURISMO) with designating and implementing national policies for the sector; support at a regional level is provided by some 22 local offices. CORPOTURISMO is an autonomous office with independent legal status, assets and income. However, the larger part of CORPOTURISMO's annual budget comes from the Government (Bs 1,681.6 million out of a total of Bs 2,328.5 million in 1995). In 1994, a presidential commission on tourism was added to provide advice to the Presidency as well as to public and private organizations.[79]

189. Besides allowing them to engage in licensed activities and operate concessions, the Law of Tourism grants authorized operators certain fiscal advantages and preferential rates for public services. Entitlement to such benefits requires the payment of a fee to support the Tourist Capacitation and Promotion Fund (*Fondo de Promoción y Capacitación Turística*); the Fund also receives a share of

[77] Agencies involved include CORPOTURISMO, the National Council for Investment Promotion (CONAPRI), the Foreign Investment Superintendency (SIEX), the Foreign Trade Institute (ICE), and the Development Ministry (*Ministerio de Fomento*).

[78] Official Gazette, 21 December 1992.

[79] Presidential Decree 293, 3 August 1994.

the revenue from privatization.[80] The Law requires operators to give preference in hiring to graduates from Venezuelan tourist institutes.

190. Guidelines for the development of the tourism industry are set out in the Stabilization and Economic Recovery Programme (PERE). The tourism sector has been chosen as an "activity leader-group", with separate policies defined for domestic and international activities. For the latter, the strategy envisages increasing the number and length of stay of tourists, especially at the high end of the market.[81] Efforts are also being made to attract conglomerates able to undertake large investments and operate all tourist-related activities. The PERE envisages greater promotional activity abroad and the identification of new tourist markets to diversify the industry.

191. CORPOTURISMO supports the sector through two main credit programmes, one aimed at building inns and small lodging facilities (*posadas y paradores*) and a second whose objective is to finance the expansion and modernization of existing tourist facilities. The latter involves funds in the order of US$150 million, including US$75 million provided by the Inter-American Development Bank.

192. Plans have been prepared to improve the legal framework for the sector, in particular by creating a more secure environment for foreign and domestic investment and enhancing credit instruments. Legislation to reform the existing Law of Tourism was due to be submitted to Congress in 1995. Awaiting passage is a law on time-sharing, as are revisions to the regulations governing debt-capital conversions to adapt them to tourist projects. It is anticipated that the improved legal framework will address the proliferation of non-authorized tourist operations that has reduced tourist security and satisfaction.

193. Under the GATS, Venezuela made specific commitments with respect to hotel and resort operators, including restaurants; travel agencies and wholesale tourism services; and other services (such as holiday camps and auxiliary tourism enterprises). In all three categories and with respect to both market access and national treatment, Venezuela made commitments not to place restrictions on cross-border supply, consumption abroad or commercial presence; however, it made no commitment to accept the presence of natural persons, except as indicated in its horizontal section. Venezuela reserved its right to give preference to graduates of Venezuelan tourism institutes in employment, and to allow only certain foreign residents to own and operate tourist camps.

(iii) Transport

(a) Ports

194. The bulk of Venezuela's exports is handled by some 25 shipping terminals operated by Petróleos de Venezuela S.A.; such ports shipped some 16.5 million tonnes in 1994. There are private ports to export mineral products, in particular bauxite, coal and iron ore; such ports handle annually about 10 million tonnes. In addition, there are nine public general cargo ports that handle the vast majority

[80]The Fund has a separate administrative and financial status within CORPOINDUSTRIA; it is charged, among other, with training tourist professionals and the promotion of the sector, both in Venezuela and abroad.

[81]The appeal of such visitors is evidenced by the fact that they spend on average some US$4,000 per stay while other international tourist spend only one third of that.

of non-mineral trade and form the National Port System (*Sistema Porturario Nacional*).[82] This System handles annually some 4,500 vessels and a cargo volume of some 8.5 million tonnes, of which about 60 per cent is general freight and the rest is bulk cargo.

195. Until recently, ports were managed, planned and constructed by the National Ports Institute (*Instituto Nacional de Puertos*), attached to the Ministry of Transport and Communications. The Institute's activities were plagued by inefficient labour practices, and represented a serious handicap to non-mineral exporters. To address the situation, the authorities initiated in 1991 a restructuring process which led to the liquidation of the Institute and the privatization of port services.

196. As part of the restructuring process, port facilities have been transferred to state governments, with the eventual aim of privatization; administrative arrangements for individual ports vary by state.[83] State governments are currently undertaking studies to establish new charges for the use of port facilities, as well as the possibility of granting concessions for port operations by private firms. The authorities describe as highly encouraging the initial productivity gains from the restructuring: surcharges and the differential treatment of cargo have been eliminated and ports now operate round-the-clock all year long. Efforts are now under way to harmonize the criteria used by the states for the operation of ports.

(b) Maritime transport

197. Maritime transport is of great importance for Venezuela: by volume, some 95 per cent of the country's total foreign trade is carried by sea. Annual freight volumes amount to at least 100 million tonnes and associated payments are estimated to exceed US$1.5 billion. In mid-1995, Venezuela's merchant fleet comprised 24 vessels of over 1,000 Gross Registered Tonnes (GRT) with a total tonnage of 491,000 GRT.[84] The distribution by vessel type was: 24 general cargo ships (34,000 GRT), four oil tankers (407,000 GRT) and one mineral carrier (50,000 GRT). All oil tankers are owned by Petróleos de Venezuela S.A.. After years of losses the state shipping line, CAVN, was allowed to go bankrupt in late 1994.[85] A significant percentage of Venezuelan-owned vessels are registered under foreign flags and are not therefore included in the above figures on the Venezuelan merchant fleet.

198. Venezuela is a contracting party to the United Nations Convention on a Code of Conduct for Liner Conferences. Venezuela has entered into maritime cargo agreements with Colombia and Mexico within the framework of the G-3, as well as with the United States. The agreement with the United States specifies that "reserved cargoes" of either of the parties must be transported by carriers of the two parties or chartered by them. Although it formally expired in 1993; the terms of the agreement are still being observed pending the implementation of Decision 314 by the Commission of the Cartagena

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[82]The three most important are, in decreasing order of tonnage handled annually, La Guaira, Maracaibo and Guanta; the other six are Puerto Cavello, Guaranao, Carúpano, Puerto Sucre, El Guamache and La Ceiba.

[83] The port of La Guaira could not be transferred to a state government as it is located in the Federal District; instead it came under the control of a limited liability company owned by the Investment Fund of Venezuela (FIV).

[84]A substantial reduction compared with the situation in 1990, when the fleet comprised 63 vessels of over 1,000 GRT adding up to a total tonnage of about 847,000 GRT.

[85]This followed restructuring efforts involving significant public funds; a similarly disappointing experience with Aeropostal has convinced the authorities that trying to rehabilitate public firms before placing them for sale is often pointless.

Agreement. The Decision establishes the principle of free access to maritime cargoes on a reciprocal basis.

199. The conditions for vessel registration under a Venezuelan flag are restrictive: 80 per cent of the capital must be paid by Venezuelans, and the vessel's captain and 50 per cent of the crew must be Venezuelan nationals. Only vessels registered in Venezuela may engage in coastal shipping (Chapter III(2)(ii)(d)). Ships engaged in cabotage operations may purchase bunker fuel at local prices well below the world level. Venezuelan ships also receive preferential rates for certain port services, although the authorities estimate the actual benefits to be insignificant.

200. The authorities indicated that national carriers receive no market access preferences. However, current legislation reserves certain exports and imports to vessels complying with particular conditions of Venezuelan or State ownership (Box V.10).

201. While reforms in shipping were intended to increase competition, the transport authorities are concerned at the negative impact of the opening of maritime transport services. Particularly worrisome to the authorities was the fall in the number of vessels under Venezuelan flag, the largest reduction in tonnage terms having occurred in the fleet of general cargo ships. In addition, the number of shipyards has fallen from 30 in 1990 to seven in 1995, most of the closures affecting private companies. There has also been increased use of foreign flags by Venezuelan-owned vessels, and the growing control of the market by foreign companies is apparently a source of concern to the transport authorities.

202. It is estimated that there are about 18 Venezuelan-owned vessels with a tonnage of at least 400,000 GRT under the flag of an "open registry" country; of these, some 8 are oil tankers owned by Petróleos de Venezuela S.A. This situation is attributed to the high cost of registering and operating Venezuelan vessels, which includes minimum Venezuelan crew requirements in domestic vessels (the relatively high benefits such crews receive mean that Venezuelan-registered vessels incur higher labour costs than many foreign-flag vessels); the payment of sales tax (12.5 per cent of the ship's value), customs fee (1 per cent) and registration of ownership documents (1 per cent); and additional payments include registration duties (Bs 75,000) and navigation patent (Bs 30 per net register tonne).

203. The authorities believe that the growing control of maritime transport services by foreign interests has led to substantial increases in freight costs; the only documented complaint was risen by the Association of Aluminium Exporters and concerned the evolution of freight rates for aluminium shipments to the United States, which between January 1994 and March 1995 appear to have risen between 73 and 165 per cent.[86]

204. Venezuela exempted maritime freight transport services for an indefinite period from the m.f.n. treatment envisaged under Article II of the GATS; the exemption was required in the context of Venezuela's reciprocity requirement under Decision 314 by the Commission of the Cartagena Agreement. The reserve cargo arrangement with the United States was also subject to a m.f.n. exemption in Venezuela's GATS schedule. Venezuela has not to date taken part in WTO negotiations on maritime transport services.

[86]Rates cited for January 1994 and March 1995 for shipments from Venezuelan ports to U.S. destinations were, in U.S. dollars per 20-feet container: to New York/Baltimore, 900 and 1,820; to Jacksonville, 620 and 1,370; to Miami, 620 and 1,070; and to Gulf of Mexico ports, 620 and 1,645.

Box V.10 Law for the Protection and Development of the National Merchant Fleet

The Law (*Ley de Proteccón y Desarrollo de la Marina Mercante Nacional*, Official Gazette 30161, 25 July 1973) sets the legal framework for the protection and development of Venezuela's merchant fleet in all areas not covered by Decision 314 by the Commission of the Cartagena Agreement. The authorities have indicated that the Law's provisions on reserved cargoes are not applied except in dealings with countries themselves restricting the free flow of cargoes. In this context, the Law requires that exporters and importers of general cargo transport at least 50 per cent of such cargo in vessels complying with particular conditions. Initially no less than 10 per cent of the volume of exports and imports of petroleum, iron ore, whet and other bulk cargoes were to be reserved for the national fleet, which share was to increase to 50 per cent over time.

The Executive may also assign part or the whole of reserved cargoes of petroleum and iron ore to publicly-owned vessels. All imports and exports by public organizations or those with State participation must be transported in State-owned vessels or, if this is not possible, in vessels complying with the conditions described below. Foreign vessels may transport reserved cargoes provided reciprocity exists in the foreign market.

To transport reserved cargoes, vessels must be registered in Venezuela, conform with the established crew requirements, and

- if owned by a natural person, the proprietor should be a Venezuelan domiciled in the country or, in case of shared ownership, at least 80 per cent of the ownership should be in the hands of Venezuelans domiciled in the country; or
- if owned by a company, this should be incorporated in the country and have its main operations and offices in Venezuela, the president and manager and at lest three-quarters of the executives should be Venezuelan and no less than 80 per cent of the shares must be held by Venezuelans.

Reserved cargoes may also be transported by foreign-flag ships leased or hired by domestic shipowners. Such vessels must comply with the requirements for Venezuelan registration and the domestic shipowners must have obtained a permit from the Ministry of Communications. The conditions for obtaining such permits include that the total gross tonnage of the leased or hired vessel does not exceed 50 per cent of the gross tonnage of the shipowner's national vessels, that the shipowner agree to increase within five years his own tonnage by a volume equivalent to that leased or hired, and that he comply with the established crew requirements. Leased and hired oil tankers and iron ore carriers are exempted from these requirements.

The Law also declares the shipbuilding industry to be of national interest. It stipulates that, provided conditions are similar to those offered by other national shipyards, only vessels built and repaired in State-owned shipyards may be used by public organizations or those with State participation.

205. In the transport sector, Venezuela made specific commitments under the GATS only with respect to maritime freight services and maritime auxiliary services (cargo handling, and storage and warehouse). In those activities, and with respect to both market access and national treatment, Venezuela committed itself to not placing restrictions on consumption abroad or commercial presence. However, it did not commit itself to accept the presence of natural persons, except as indicated in its horizontal section; neither did it engage to permit cross-border supply.

(c) Other transport

206. Some 2.5 million motor vehicles were in circulation in 1989, of which about 1.5 million were passenger cars and close to 500,000 were trucks. While tariffs for international and national cargo transport may be set freely, urban and "extra-urban" passenger carriers operate in a relatively restrictive

environment, all operators requiring special authorizations and tariffs being subject to official approval. Freight carriers must be cooperatives established and domiciled in the country; tariffs are market-determined. Most road transport companies are privately owned. Nationals of other Andean Pact countries may buy, own and operate Venezuelan-registered trucks under the same terms and conditions as nationals; nationals of other countries are excluded from such arrangements.

207. The railway network is limited: there are only 223 kilometres of track; additional lines totalling some 100 kilometres are expected to be opened soon. A National Railroad Plan envisages extending the rail system to 2,000 kilometres by the year 2005 but the Plan's long-term financing is uncertain. The State owns all tracks and rolling stock. There are also private lines, dedicated to the transport of minerals. Tariffs and transport schedules are subject to official approval.

208. In 1994, internal air services carried just over 5.5 million passengers and 7,700 metric tonnes of freight; international departures amounted to 3.1 million passengers and some 76,000 metric tonnes of cargo were transported. Venezuelan firms account for about 20 per cent of total international air cargo; their share of passenger traffic is some 50 per cent.

209. Authorization is required to construct and operate airports and associated services. Airports are under the authority of either the Minister of Transport and Communications, the State Governments or an autonomous Institute (*Instituto Autónomo Aeropuerto Internacional de Maiguetía*). The Minister of Transport and Communications controls auxiliary navigation and air traffic services. In international airports, the Government may offer concessions on services. All airport charges must be authorized by the authorities. For air services to and from non-Andean Pact countries, the authorities issue operating licences for international transportation services based on the principle of equal opportunity. Aircraft must have a concession or permit to operate in Venezuela. Only Venezuelan-registered aircraft may operate local air transport services. Fuel and airport charges are lower for national than for international services.

210. The Andean Pact countries have adopted a regional "open skies" policy. For non-commercial landings, member States have granted each other the right to overfly their territories, National regional firms are granted automatic authorization to provide non-regular passenger, cargo and mail services. Designated national firms authorized to offer regular international services for passengers, cargo and mail enjoy guarantees of free market access within the region.[87]

211. Venezuela's main international carrier, VIASA, was privatized in 1991;[88] however, the Government retained a "golden"share that gives it veto power over matters of national interest. There exists a number of domestic carriers, all privately owned, which also offer a limited number of international flights (the main one being Avensa). Aeropostal, the state-owned domestic carrier, went bankrupt in 1994 after unsuccessful attempts at privatization.

212. Venezuela made specific commitments with respect to private courier services under GATS. Regarding both market access and national treatment, Venezuela has no restrictions on commercial presence in Venezuela nor on consumption abroad, but did not commit itself to accepting cross-border supply or the presence of natural persons, except ad indicated in its horizontal section.

[87]Decisions of the Commission of the Cartagena Agreement 297 (12 June 1991), 320 (15 June 1992), 360 (10 June 1994) and 361 (10 July 1994).

[88]Spain's Iberia and the Venezuela's Banco Provincial gained control of 60 per cent of the stock.

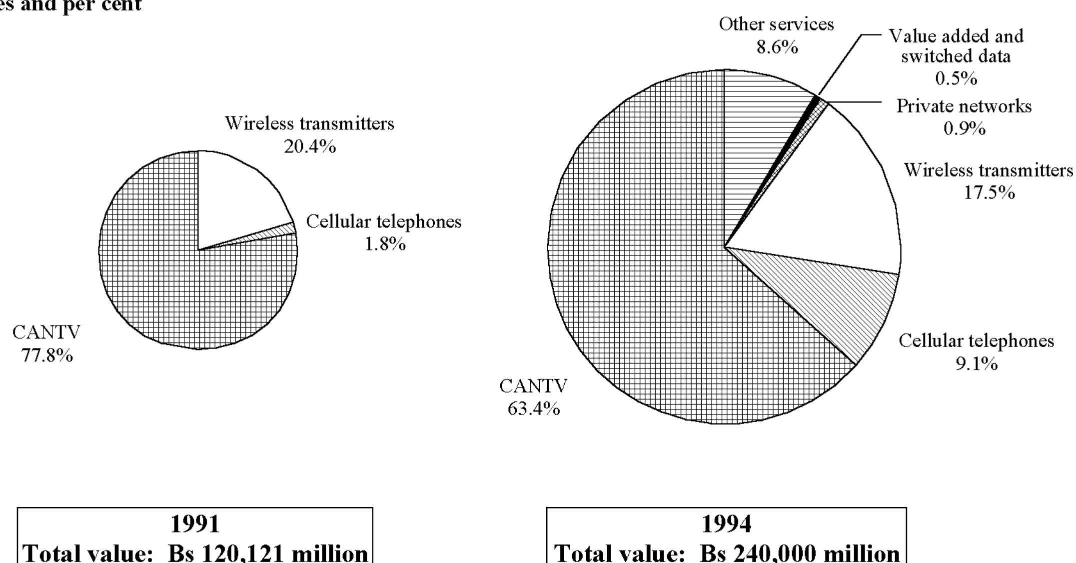
(iv) Telecommunications

213. There are more than 3,500 private firms in Venezuela's telecommunications sector, of which some 60 are major. They include the national telecommunications company, CANTV, as well as private companies providing diverse services, such as cellular-telephones, private networks, switched data networks (*redes conmutadas de datos*), trucking, paging systems (*buscapersonas*), medical attention via radio, vehicle location, cable television and value-added services. Although no precise estimates are available, the authorities estimate conservatively that international transactions account for between 25 and 30 per cent of the total value of telecommunications services provided.

214. According to the authorities, the opening of the sector since 1991, allowing private participation and establishing a new regulatory framework, has created at least 8,000 new jobs, with total employment in the sector reaching some 32,000 in 1994. During 1991-94, the total value of telecommunication services doubled in real terms and several new services were introduced (Chart V.13).[89] However, efforts are still being made to address some remaining problems: for example, only 40 per cent of the demand for basic telephone services is met and connections between CANTV and other services providers are limited.

Chart V.13
Telecommunications sector, 1991 and 1994

1994 prices and per cent



Source: CONATEL.

[89]Before 1991, services included basic telecommunications, paging services, telex and (*líneas muertas*). In 1995, services also encompassed cellular telephones, trucking, value added (electronic mail, video text, data bases, etc.), tele-medicine, international paging services, vehicle location, pay television, private networks, video conferences, voice mail (*correo de voz*) plus features such as detailed invoicing and abbreviated dialling.

215. Current legislation on telecommunications dates back to 1940.[90] The Government sets the tariffs for such services, taking into account international agreements and fiscal needs. A system of minimum and maximum tariffs is supplied for services subject to competition. Taxes stipulated for services in private hands comprise a payment based on the length of the lines; this payment must be at least 12 per cent of the gross income of cable operating firms, and 5-10 per cent for other operators (currently collected at a rate of 5.5 per cent). Radio and television concessionaires pay 1 per cent on the gross value of invoicing plus a charge per broadcasting station. Rural installations and public interest operations may be exonerated from payment of some of those charges.

216. The State has the exclusive right to establish and operate communication systems. Under the current law, only legal or natural persons domiciled in Venezuela may be granted concessions by licences to provide telecommunication services. There are no limitations regarding foreign capital participation in operating enterprises, except in radio and television. Radio and television operations are reserved to national investors, who must control at least 80 per cent of the total capital;[91] exempted from these requirements is ownership of cable and UHF television by nationals of Andean Pact countries. Approval is required for changes in the participation of shareholders, who must accept to carry out specific development plans as condition for their concessions.

217. The telecommunications sector is supervised by the National Telecommunications Commission *(Comisión Nacional de Telecomunicaciones*, CONATEL). The Commission, created in 1991, is an autonomous agency attached to the Ministry of Transport and Communications.[92] Its responsibilities include the administration of the electromagnetic spectrum and the promotion of the sector, especially the coordination of initiatives to develop international telecommunications. CONATEL also approves the service contracts governing relations between concessionaires and final consumers, and oversees the correct application of technical norms.

218. The introduction of a new telecommunications law is seen as a priority by the telecommunication authorities. This would be designed to give legal and financial autonomy to CONATEL, placing it on an equal footing with the private sector that it regulates. Other changes considered particularly important would include a better delineation of the State's regulatory authority, increasing the legal security for private investment, and establishing the rule of reciprocity in the provision of trans-border services. Further improvements would involve securing the inter-operability of all networks, the use of the market mechanism to assign the electromagnetic spectrum, reducing and liberalizing the setting of tariffs and dedicating a portion of revenues for research, human development and CONATEL's operation.

219. Basic telecommunication services are provided under a régime of "limited competition" that allows the recently privatized national telephone company a monopoly in that area (Box V.11). However, competition is free in all non-basic services. All such services may connect to the basic network, except for private networks for which connection is generally not possible. The Government is not involved in the operation of telecommunications services, except those used by the petroleum industry and the armed forces.

[90]Law of Telecommunications, 29 July 1940.

[91]Concessions in these areas are granted by the Ministry of Transport and Communications.

[92]Presidential Decree 1826, Official Gazette 31801, 18 September 1991.

Box V.11 Compañía Anónima Teléfonos de Venezuela (CANTV)

In view of notorious inefficiency and the need for heavy investments for modernization, the Government sold in 1991 a controlling stake in Venezuela's national telecommunications company, CANTV, to a consortium led by foreign investors. The consortium, Venworld Telecom, is the largest foreign investor and the largest private investor in Venezuela. The group paid some US$1.89 billion for 40 per cent of CANTV's shares; it includes GTE with 51 per cent of the consortium, Telefónica Internacional de España, Electricidad de Caracas, Venezuela's largest private power company, the Banco Mercantil group and AT & T. The Government placed in trust 11 per cent of the shares for CANTV employees.

CANTV was given a monopoly until November 2000 in basic telecommunication services to ensure the development of the basic network. To achieve this objective, a development programme has been agreed that specifies progress to be made in particular periods; in this context CANTV has developed a US$6 billion capital spending programme for up to the year 2000.

The authorities pointed out that CANTV's sale has so far resulted in 800,000 new subscribers, the installation of more than one million lines, the introduction of a digital system, decongestion of domestic and international long-distance calls and the widespread use of optical fibres; on the other hand, problems remain in relation to invoicing, unjustified service cuts, slow reconnections and CANTV's poor image among users, which do not perceive a relationship between tariff rises and service quality. Overall, the company has reportedly improved Venezuela's telecommunications services substantially since it was privatized, but it has not yet established a reliable and modern network (Financial Times, 22 September 1994).

CANTV is Venezuela's largest private borrower abroad; strict foreign exchange controls and slow processing of applications for U.S. dollars made servicing its debt difficult and rescheduling was required. The currency devaluation, high inflation and exchange controls forced CANTV to cut back its capital investment programme in 1994, and planned capital outlays of about US$700 million for 1995 were reduced by over 50 per cent (Financial Times, 22 September 1994). Rate increases approved for CANTV's services have been below inflation, failing to offset the higher local currency costs of imported capital goods caused by the devaluation.

The Government plans to sell its remaining 49 per cent in CANTV as soon as market conditions improve.

220. Pricing for basic telecommunication services is set through a "price cap" system. An exception is made for residential services, where international calls subsidize domestic services, a situation that is being progressively corrected, with cross-subsidies planned to be eliminated by 1997. All non-basic services are subject to minimum and maximum tariffs, which are designed to allow the market to set actual tariffs.

221. The authorities regard the resale of international telecommunication services by off-shore foreign companies, which are neither registered nor taxed in Venezuela but make use of the domestic network (e.g. "call back" services), as a serious problem and have banned such services.[93]

222. Venezuela has excluded radio amateurs from m.f.n. treatment under Article II of the GATS for an indefinite period; the exemption was made in the context of Venezuela's participation in the

[93]Resolution 002, Ministry of Transport and Communications - CONATEL, Official Gazette 35183, 31 March 1993.

Inter-American convention on radio amateur services and bilateral agreements with Germany, Spain, Portugal and Sweden.

223. Under the GATS, Venezuela made specific commitments with respect to other telecommunication services (cellular telephone, radio based services and satellite services and systems). With respect to market access and national treatment, Venezuela bound itself not to place restrictions on consumption abroad or commercial presence; however, it did not commit itself to accept cross-border supply or the presence of natural persons, except as indicated in its horizontal section.

224. Venezuela participates in the Negotiating Group on Basic Telecommunications but, by mid-1995, had yet to submit an offer.

(v) Electricity

225. Venezuela's electric power industry is made up of five State enterprises, Edelca and Cadafe being the largest, and 12 private firms.[94] State participation takes place through the Investment Fund of Venezuela (FIV) which is the principal shareholder in publicly-owned enterprises, these account for over 80 per cent of installed generation capacity. In the past, both public and private enterprises have incurred financial problems related to the cost of debt servicing and the authorities' reluctance to increase tariffs in line with growing costs.

226. The Government's stated policy objectives for the electricity industry are to guarantee the quality and quantity of power supply to the domestic market, maximize its net contribution to foreign exchange earnings and contribute to the country's sustainable development. According to the authorities, this policy presupposes State control over energy resources. Under current legislation, the industry is regulated by an inter-ministerial commission under the presidency of the Minister of Energy and Mines. The commission is charged with price setting, approval of expansion plans and overseeing service quality.

227. The electricity industry is governed by numerous Presidential Decree and Ministerial Resolutions which are now being consolidated into a single law that was to be presented to Congress at the end of 1995. The draft legislation foresees separation of the State's regulatory and operational responsibilities, opening the electricity industry to competition, guaranteeing access of suppliers to the national power gird and restructuring the subsidies offered to low-income residential users.

228. Electricity rates are fixed administratively through joint resolutions of the Ministry of Development and the Ministry of Energy and Mines, taking account of the advice of the regulatory commission (*Comisión Reguladora de Energía Eléctrica*). The authorities state that a process is under way to ensure that prices reflect supply costs at different voltages, to correct the distortions in the current price schedule and to facilitate private investment; from 1 January 1996, a new price schedule currently under design will come into force. In the meantime, the authorities feel that changes to the price structure are reducing cross-subsidization, encouraging productivity and quality gains and maintaining financial viability in a high inflation environment.

229. The electricity sector has been chosen as an "activity leader-group" to make use of spare capacity and planned expansions to supply growing demand in eastern Colombia and northern Brazil. The authorities expect electricity exports to increase from their present negligible level to some

[94]The largest private company, Electricidad de Caracas, is one of the major companies quoted on the Caracas Stock Exchange.

US$100 million within a decade. Privatization plans are also being drawn up but the lack of a proper legal framework is seen as a major obstacle.

(vi) Other services

230. Venezuela exempted from the m.f.n. treatment envisaged under Article II of the GATS a number of service areas not covered in the sectors discussed above. For example, some professional services governed by special laws (Chapter III(2)(i)) were exempted for an indefinite period.[95] For audiovisual services, a ten-years exemption, automatically extended for the same period, was made to cover the agreement on co-production of cinematographic works with Chile. An exemption for an indefinite period was also made in relation to the Ibero-American Cinematographic Integration Agreement and the Latin American Cinematographic Co-production Agreement.[96]

231. Under GATS, Venezuela made specific commitments with respect to various types of business services governed by special laws. For economic and management consulting services as well as professional services, Venezuela made a commitment not to place restrictions on consumption abroad, both in relation to market access and national treatment; however, it did not commit itself to accept cross-border supply, commercial presence or the presence of natural persons (except as indicated in its horizontal section).

232. For advertising, computer and related services, market research and opinion polling, and translation and interpretation services, engagements were made, both concerning market access and national treatment, not to limit consumption abroad, commercial presence or cross-border supply (although the latter requires domestic legal representation in some cases); as in other service sectors, no commitments were made to accept the presence of natural persons (except as indicated in the horizontal section).

233. With respect to construction and engineering services, Venezuela agreed not to place restrictions on consumption abroad or commercial presence; however again, it did not commit itself to accept cross-border supply or the presence of natural persons, except as indicated in its horizontal section.

[95]Such professional services relate to legal, accounting and auditing, architectural, engineering and integrated engineering, urban planning and landscape architectural, and computer and related activities.

[96]In addition to Venezuela, those agreements include Argentina, Brazil, Colombia, Cuba, Dominican Republic, Ecuador, Italy, Mexico, Nicaragua, Panama, Peru and Spain.

Annex V.1 Resource rents and downstream processing

234. Venezuela has large, low-cost hydrocarbon and other mineral resources and much of its industry was built on the premise that such advantages can be passed to downstream activities in the form of inexpensive inputs. This, it was often argued, constituted Venezuela's competitive advantage. An alternative view is that inputs supplied below world price levels are a form of subsidy which undermines the efficient use of national resources. Consistent with this view, the authorities noted that "nowadays, a new approach is being considered that is to gradually obtain for the hydrocarbon producers f.o.b. prices in their sales in the Venezuelan domestic market".

235. Venezuela's cost advantage in the production of hydrocarbons is clear: in 1993, average production costs amounted to US$1.25 per barrel of oil equivalent; in contrast, the average world price for Venezuelan crude oil was US$12.10 per barrel.[97] The difference between the world price and full production costs represents an "economic rent". For Venezuela, assuming a production cost of US$2 per barrel, the cumulative value of such rents between 1973 and 1992 would have amounted to some US$220 billion had all oil production been sold at prevailing world prices. Setting aside low transfer prices to user industries and consumers, a more conservative estimate of the value of rents is the amount of taxes paid by PDVSA; between 1976 and 1994, these reached to US$14.8 billion. It is the value of such flows that makes their distribution so important and gives the State both the ability to pay for social services and the potential capacity to subsidize activities.

236. It is often asserted that, provided they cover production costs, economic efficiency does not require internal input prices to approximate world prices. Under this view, it would be justifiable to set domestic prices in Venezuela below international levels; domestic downstream users should not be obliged to pay the economic rent component implicit in world prices because petroleum resources belong to the nation. As mentioned below, PDVSA incurred between 1991 and 1993 an average annual loss of about US$376 million on domestic downstream sales, which over 20 years would have represented transfers to downstream operation of some US$7.5 billion.[98] Such cost savings may have been passed to downstream users in the form of less expensive inputs and to consumer of final goods. They may also have been in part dissipated through the maintenance of high-cost production structures or through profit-taking.

237. Through the mechanism described above, users of tradeable inputs (such as petroleum, mineral ores, and related processed products) would have benefited from a subsidy equivalent to the difference between the domestic price and the inputs f.o.b. export price. The latter offers the best benchmark for the opportunity cost of an exportable resource. Domestic prices below such benchmark lead to an excessive consumption of the input in question; the effect is not confined to only that one input, for an over-use of all complementary inputs ensues while substitutes become under-used. In the Venezuelan case, this mechanism is consistent with the observation that the country's economy is highly energy intensive (as well as capital intensive). The authorities have indicated being conscious that domestic fuel prices were lower than in world markets and that such a situation cannot be maintained

[97]The production costs quotedconsist of lifting costs (including labour, maintenance and supplies), administrative expenses and depreciation applicable to support equipment associated with production activities (PDVSA, 1994). Those costs do not include new investments required to maintain and increase production capacity.

[98]The actual losses would have varied over time with fluctuations in world prices and domestic sales: the estimate of US$376 million is probably conservative as, relative to 1991-93, lower domestic sales during the whole 1974-93 period would have been more than offset by higher prices.

indefinitely; they pointed to adjustments initiated in September 1995 to start to bring domestic prices to international levels.

238. Venezuela's institutional arrangements and market structure would appear to facilitate the use of vertical cross subsidies in the form of input under-pricing. For one, the Ministry of Energy and Mines is authorized to fix all wholesale and retail energy prices. Moreover, given the proliferation of vertically integrated groups and widespread State involvement in most industrial activities, especially in the key processing industries of aluminium, petrochemicals and steel, transfer pricing potentially provides a primary mechanism to channel subsidies.[99]

239. Petróleos de Venezuela S.A. explicitly notes that domestic users are supplied with refined products at prices below production costs: "During 1993, 1992 and 1991 PDVSA provided 137, 133 and 124 million barrels, respectively, of refined petroleum products to the Venezuelan domestic market at prices regulated by the Venezuelan government and mostly below the market prices at which the crude oil is transferred to PDVSA's downstream operations. During 1993, 1992 and 1991, average sales prices were US$5.61, US$6.91 and US$7.60 per barrel, respectively, and losses on sales of these products amounted to approximately US$422, US$375 and US$332 million, respectively, before income tax."

240. Despite high taxes and low domestic prices, the profitability of petroleum refining in Venezuela remains high. Economic indicators for the petroleum refineries industry (ISIC 353) show that the value added in that industry amounted to about 80 per cent of its value of output, a share more than double the average for manufacturing as a whole (Table V.7).[100] As only about 1.5 percentage points of value added accrued to labour, the rest, just over 79 percentage points, may be considered as profits. Even considering the capital-intensive nature of petroleum refining, such profits are high. Relative to the average for all manufacturing of 37 per cent, returns in petroleum refining are 42 percentage points higher, equivalent to Bs 115 billion of US$2.4 billion.[101] Such above average returns are linked to the low cost of inputs to refineries, which represent only about 20 per cent of the value of production (the equivalent for all manufacturing is 53 per cent).

241. Venezuelan refineries are considered to be efficient by world standards. The authorities noted that refineries "operating as in an open market, considering crude oil, other feedstocks and products were commercialized at international prices" would be internationally competitive and profitable. In this regard, estimates made by PDVSA in 1990 indicated a Net Refinery Margin of US$1.29 per barrel, equivalent to a profit before tax of US$445 million.

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[99]In petroleum, the vertical integration is complete: from extraction to retail sales of refined products overseas (Box V.1). Vertical integration is also strong in steel and aluminium production. In the first, the Government controls the firms engaged in coal and iron mining, steel making and some downstream operations. In aluminium, government-controlled companies are engaged in bauxite mining, alumina production and aluminium refining. The State also supplies natural gas, electricity and other fuels to both aluminium and steel operations.

[100]This share was particularly high in 1990, the only year for which complete data were available; data for the period 1984 to 1991 suggest that a more typical share is about 65 per cent. According to the authorities, the economic indicators for petroleum refineries refer to an industry integrated from the oil well to the refinery.

[101]Data for refineries refers to 1990 and those for manufacturing as a whole to 1992. Above average profits are estimated as 42 per cent of the 1990 value of output in oil refining; the dollar value is obtained using the average exchange rate for 1990 of Bs 47.17 per U.S. dollar.