VENEZUELA: A PATH OUT OF CRISIS

By the Brookings Institution Working Group on Venezuela

EXECUTIVE SUMMARY

In recent years, Venezuela has seen the rapid erosion of its economic standing and democratic credibility. Facing a global downturn in oil prices and an annualized inflation rate that is expected to exceed 1,000 percent in 2017, Venezuela’s economy is now one of the worst performing in the world. The resulting humanitarian situation is severe. Only 25 percent of the Venezuelan population is able to maintain a regular diet, while the poverty rate has grown to 82 percent and crime is widespread.

Yet despite these conditions, President Nicolás Maduro and his United Socialist Party of Venezuela have maintained their grip on power. One key to the durability of the Maduro government has been the choice to cultivate loyalty by filling senior government posts with officials who have the most to lose if ousted from power, including alleged narcotraffickers and other persons under investigation by U.S. federal prosecutors. More broadly, Venezuela’s system has become increasingly autocratic, undermining democratic institutions and elections, and repeatedly demonstrating its unwillingness to adapt social and economic policies to maintain a viable development model that satisfies the needs of the population.

Maduro has faced growing internal and external pressure to enact much-needed economic reforms. Domestically, the president’s approval rating has fallen below 30 percent, but the Venezuelan opposition is hampered by internal divisions, an inability to translate public mobilization into political victories, and repressive government action. Internationally, the government has received criticism from not only the United States, but also from regional countries and organizations that were previously reluctant to express concerns publicly.

The United States has struggled to exercise influence over Venezuela’s actions in recent years, but this moment of crisis could provide an opening for Washington to urge the Maduro government to change course. The United States should exercise leadership and support efforts to raise the Maduro administration’s costs of pursuing antidemocratic policies and lower the costs of a return to democracy.

To this end, we recommend that the United States initiate an immediate and sustained dialogue with key regional partners including Peru, Argentina, Brazil, and Colombia on how to address the crisis in Venezuela, which should include consideration of the following continuum of policy options:

1. The United States could expand its assistance to countries that until now have been dependent on Venezuelan oil, as a means to decrease regional support for and dependence on the Maduro government.

2. The United States could increase monetary assistance to credible civil society organizations and nongovernmental organizations able to deliver food and medicines to Venezuelans. By doing so,
the United States should make clear that international pressure aims to support democracy, not punish the Venezuelan people.

3. The United States could support efforts by the opposition in Venezuela to build an “off-ramp” that would split moderate elements of the government away from hardliners, encouraging the former to acquiesce to a transition to democracy by lowering their costs of exiting government.

4. The United States could coordinate with international institutions such as the International Monetary Fund (IMF) to offer financial incentives for holding free and fair elections in 2018, and for the opposition to unify and compete in those elections. Such coordination would also involve developing and publicizing a credible plan to restart Venezuela’s economy.

5. As a last resort, the United States could consider raising economic costs to the government through an expanded sanctions regime that aims to limit Venezuelan earnings from oil exports and block further financing. This policy is risky, given that the Maduro government would be able to more credibly shift blame for the economic crisis onto the United States, and should be accompanied by well-publicized efforts to deliver humanitarian aid through credible civil society and nongovernmental organizations.
INTRODUCTION

Venezuela has the largest reserves of oil in the world, but one of the worst performing economies. Since President Nicolás Maduro took office in 2013, Venezuela’s economy has contracted by about 30 percent, and its annualized inflation rate is expected to be above 1,000 percent in 2017.¹ According to a national survey conducted by three leading universities, the poverty rate increased to 82 percent in 2016 from 48 percent in 2014.²

Yet President Maduro’s administration has remained remarkably resilient in the face of a seemingly imminent economic collapse and political pressure from the U.S. Maduro continues to maintain complete control over his political party, and three of the four main branches of government (the opposition controls the National Assembly, although Maduro has blocked the assembly from fulfilling its constitutional role). The senior leadership of the armed forces and of the state-owned oil enterprise, Petroleum of Venezuela (PDVSA), continue to profess their loyalty to the administration and to the Bolivarian revolution instigated by Venezuela’s late President Hugo Chávez. Maduro has generally enjoyed regional support; only in the past year have key governments in the region begun to join the U.S. critiques of the state of affairs in Venezuela.

Venezuela’s economic crisis has been devastating to the country’s population. The humanitarian situation is becoming so severe that only 25 percent of the population maintains a normal diet while a stunning 15 percent of the Venezuelan population is frequently forced to eat out of the trash.³ 80 percent of medicines and medical supplies are not available,⁴ and Venezuela’s strained hospital system is collapsing. This has serious implications for the control of potential epidemic diseases. The crisis has driven increased outward migration, especially along the land borders with Colombia and Brazil.

At the root of the country’s issues is an increasingly autocratic system which is unwilling to adapt social and economic policies to maintain a viable development model that satisfies the needs of the population. Regularly scheduled municipal and state elections, one of the few remaining elements of democracy in Venezuela, have been postponed arbitrarily in the past year. This forecloses an important avenue for change and raises doubts about whether the 2018 presidential elections will be held.

VENEZUELA’S TRANSITION FROM ILLIBERAL DEMOCRACY TO AUTOCRACY

President Maduro was elected by a razor-thin majority in 2013 following the death of his predecessor Hugo Chávez from cancer. Since his election, President Maduro’s popularity has steadily declined and his popular support has hovered between 20 and 30 percent for much of the past year.

An overwhelming opposition victory in December 2015 National Assembly elections, which produced a supermajority against the government, did not translate into political power. The Maduro administration used control over other branches of government, particularly the courts, to prevent the legislature from

accomplishing anything of consequence. President Maduro is ruling under an emergency economic powers decree under which he claims wide latitude for executive branch orders.

The Maduro administration controls nearly all media outlets in Venezuela, either directly or indirectly, via private sector actors loyal to the government. The result is that Venezuelans have been subjected to years of government-sponsored propaganda, and few have access to reliable information about the causes of the present crisis or access to information about the efforts by the opposition to address the present situation via their legislative majority or the governorships and mayoralties they do control.

The opposition’s efforts to organize a national referendum to remove the president from office, a move authorized under the Venezuelan constitution, were successfully blocked by the government, whose sympathizers control the National Electoral Council. If the referendum had been held before January 2017, Venezuela’s constitution would have mandated new presidential elections and a significant chance of opposition victory. Now, the referendum is no longer consequential because with less than two years left in the current presidential term, the constitution specifies that the recently appointed vice president, Tarek El Aissami, would take over following a recall.

A political dialogue between the government and the opposition, sponsored by the Vatican and the Union of South American Nations (UNASUR), has not produced serious results. The government has stonewalled key opposition demands, for example on the release of political prisoners, whose numbers actually rose to over 100 while talks were underway. The dialogue is now seen by many voters as part of the government’s successful efforts to delay the presidential referendum beyond a date when it would be consequential.

The opposition has been able to demonstrate massive convening power, but it has feared deploying it against the government because of the possibility of political violence. The largest protest was on September 1, 2016, when the opposition rallied the “Tomada de Caracas” with an estimated 500,000 people in the streets of the capital. The government allowed the protests to proceed peacefully in Caracas, but parallel protests in other major cities and towns were violently suppressed by police and pro-government paramilitaries known as “colectivos.”

The opposition’s divided leadership is facing increasing difficulties in maintaining a united front now that the recall referendum is no longer on the table, and the Vatican-promoted dialogue has produced few results. With December 2018 presidential elections on the horizon, at least three of the main opposition leaders are trying to position themselves to compete for the presidency, further straining opposition unity.

Lack of unity within the opposition leadership, the failure to translate popular mobilization into political change, and the inability of the legislature to bring about change have precipitated a significant shift in voter sentiment away from support for the opposition and toward the “ni/ni” voters (voters who support neither side).

The armed forces have repeatedly expressed loyalty to the Maduro administration and show few signs of supporting any move to unseat the president. Repressive duties fall to the civilian Bolivarian National

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Police and the Guardia Nacional (militarized national gendarmerie under Ministry of Defense), with more targeted repression being carried out by the Bolivarian National Intelligence Service (SEBIN).

Some senior leaders of the armed forces, mostly concentrated in the Guardia Nacional, are reputed to play a significant role in drug trafficking through Venezuelan territory. Military officers and soldiers are in control of food distribution, and frequently profit from this role given ongoing food shortages.8

President Maduro recently appointed Tarek El Aissami as executive vice president with a substantially greater policy role than previous vice presidents. El Aissami, a former student activist and later a government minister under President Chávez, is reputed to head one of the two largest drug trafficking networks in Venezuela. In February 2017, the U.S. Justice Department unveiled drug trafficking charges against him.9

President Maduro has been careful to surround himself with persons under investigation by U.S. federal prosecutors or who have been indicted or sanctioned for their crimes, such as drug trafficking. He may feel more secure in their loyalty knowing that his subordinates have nowhere else to go and therefore need to keep him in power to safeguard their own futures.

President Maduro likely fears new elections because of his deep unpopularity. Nonetheless, his grip on power is now sufficiently secure that the Venezuelan government has postponed the elections for governors and mayors originally scheduled for 2016. By doing so, he preserves control of a majority of state governorships currently held by his loyalists.

**DETERIORATING ECONOMIC SITUATION LEADS TO HUMANITARIAN CRISIS**

Historically, the Venezuelan economy has relied on oil exports. Crude oil accounts for about 95 percent of Venezuela’s export basket,10 resulting in high exposure to economic volatility based on oil prices. Following the rapid decline of oil prices in recent years, the country now faces scarcity of food and basic goods, sharply deteriorating public health,11 energy shortages, and widespread crime (in 2015, four times more people violently died in Venezuela than in Afghanistan).12 The government has nationalized all food distribution and has increasingly begun to make subsidized food packages available via local committees staffed by political loyalists. As the crisis deepens, Venezuelans are increasingly turning to speculators, bartering, and occasionally looting grocery stores.

The crisis could have been prevented with sound, countercyclical economic policies. Yet, the government did the opposite. During the oil boom of the 2000s, both public and private consumption continuously increased, mostly fueled by an unprecedented rise in imports per capita that jumped to a high of $2,000 in 2013 from $500 in 2003 (in constant 2015 dollars).13 Meanwhile, the country’s external debt


quintupled, isolating Venezuela from global financial markets, and handicapping the country when it came
time to absorb the negative external shock that hit in 2016. China remains as one of the few sources of
credit to the government, in the form of modest new loans or by delaying interest repayment. Yet, the
financial tools available to the government have not been enough to alleviate the crisis. In light of this, the
government has continued printing money to cover its unusually high fiscal deficit (estimated to be about
20 percent of GDP), intensifying the ongoing hyperinflation. The Venezuelan currency has lost over 98
percent of its value since early 2014 with respect to the U.S. dollar.

In large part, the mismanagement that led to the current humanitarian crisis originates in the system of
foreign currency exchange controls established in early 2003. Since then, Venezuelan firms rely solely on
government bureaucrats to access foreign currency to import raw materials or final goods. Control over
the allocation of foreign currency together with the plethora of controls, expropriations, regulations, and
inspections have almost extinguished local productive capabilities. As often happens with price controls,
a black market for foreign currency emerged in which a U.S. dollar was worth about two to three times
the lowest official exchange rate during 2010. Over these years, lobbying for official dollars and reselling
them in the black market was the most profitable game in town. As of today, the scarcity of foreign
currency is reflected in the unusually high price of $1 in the black market: about 400 times the lowest
official exchange rate.

It is important to note that the sudden reduction in the inflow of foreign currency goes beyond the drop
in oil prices. Corruption and poor management of PDVSA—Venezuela’s state-owned oil company—has
resulted in a significant drop in oil production to about 2 million barrels per day (bpd) from 3 million bpd
in the mid-2000s. This declining trend can only be reversed in the long run after important new
investments are made in productive capacity, investments that likely will not be available if oil prices
remain low. Modest increases in the price of oil, such as the ones seen in late 2016 and early 2017, are
not significant enough to overcome the current crisis and to avoid the unleashing of a foreign debt crisis
and eventual default.

While markets are wary of the ability of the Venezuelan government and PDVSA to service their debt, so
far the government has managed to keep its solvency intact. Yet, after failed attempts to perform debt
swaps with borrowers during the fall of 2016, doubts on whether the government and PDVSA will keep
servicing their debt keep increasing. Default is perceived by some as a real possibility. Foreign reserves
have fallen to $10.4 billion as of March 2017,\(^4\) the lowest level since June 1996. The next big service
payment of about $3.7 billion is scheduled for April 2017.\(^5\)

Yet, unofficial reports suggest that the government continues to make extraordinary efforts to reduce the
debt burden in the very short term, such as by negotiating significant “haircuts” from debtors (such as
Petrocaribe states) as well as by negotiating further deals with China or planning debt swaps with private
creditors. The ability of the government to keep serving its debt remains doubtful, and an eventual default
on PDVSA and/or sovereign bonds is still perceived as a real possibility.

\(^4\)“Update 2-Venezuela’s PDVSA pays $1bln bond, foreign reserves tumble,” Reuters, October 28, 2016,
http://www.reuters.com/article/venezuela-phx-idUSL1N1CY1H3.

CHANGING INTERNATIONAL DYNAMICS OFFER OPPORTUNITIES FOR INFLUENCE

The United States has very little influence over, or even access to, senior Venezuelan government officials. The Venezuelan government has cut off nearly every routine cooperative mechanism that exists between the two governments, including law enforcement cooperation and military-to-military relations.

Ironically, the United States is still Venezuela’s largest export market for its oil. The U.S. is one of the few importers that pay market value for Venezuelan oil, thereby helping the regime stay afloat. The rest of Venezuela’s oil is used to repay loans from China or to subsidize its allies and partners in the Bolivarian Alliance for the Peoples of Our America (ALBA). For example, Cuba continues to receive subsidized fuel from Venezuela, although at lower quantities, in exchange for provision of health, education, and security services.  

Venezuela’s diplomatic ties to Russia and China have grown steadily. Russia has been a key exporter of weapons to modernize the Venezuelan armed forces, and China has provided over $50 billion in a “loan-for-oil” scheme. Venezuela is now in arrears to both of these creditors, but neither Russia nor China want to rock the boat for fear that a future opposition-led government would refuse to honor loan commitments on the grounds that the Maduro administration entered into them illegally (without legislative approval).

Until recently, U.S. criticism of the lack of democracy and human rights in Venezuela had little support in Latin America or internationally. Now, the leadership of the Organization of American States (OAS) and of key countries in the region such as Argentina and Peru are more openly critical. Mercosur has suspended Venezuela for failing to meet its economic and political membership criteria. But the region is still struggling to come to an agreement on how to approach the Venezuelan crisis.

Venezuela’s petro-diplomacy in the region, particularly among the Caribbean island states, is in question as the price of oil has dropped and the Maduro administration’s ability to continue to provide access to subsidized oil has faded. As the crisis worsens in Venezuela, its soft power is diminishing.

UNASUR has attempted to mediate a dialogue in conjunction with the Vatican, but the Venezuelan opposition views the organization as politically partisan and pro-government, thus contributing to the failure of the dialogue.

Under the leadership of Secretary General Luis Almagro, former foreign minister of Uruguay, the OAS has debated the Venezuelan question more openly in the past 18 months. But the member states remain divided on policy toward Venezuela, although a growing number agree with Almagro’s call for sanctions on the country under the Inter-American Democratic Charter. The OAS is viewed as biased by the Venezuelan government.

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POLICY OPTIONS

Bearing in mind the international obligations the United States and OAS member states assumed by signing the Inter-American Democratic Charter on September 11, 2001, we recommend that the U.S. government work with partners in our hemisphere to help Venezuelans ensure that relatively free, fair, and consequential multiparty elections are held no later than the end of the present constitutional period in 2018.

The United States should exercise leadership and support efforts to raise the Maduro administration’s costs of pursuing antidemocratic policies and lower the costs of a return to democracy in Venezuela. To this end, we recommend that senior leaders in the United States should begin an immediate and sustained dialogue with key regional partners on how to address the crisis in Venezuela. President Trump or Secretary of State Rex Tillerson should call on long-standing critics of the present situation in Venezuela, such as President Pedro Pablo Kuczynski of Peru and President Mauricio Macri of Argentina, as well as increasingly like-minded heads of state, such as President Michel Temer of Brazil and President Juan Manuel Santos of Colombia, to hear their ideas and build a consensus on next steps. Such a dialogue should include consideration of the following continuum of policy options:

1. The U.S. could expand its assistance, especially in the area of energy security, to small Caribbean island states that have until now depended on subsidized access to Venezuela’s oil, in order to win their support for a regional effort to facilitate the return to democracy in Venezuela. Together, this can lead to the invocation of the Inter-American Democratic Charter as a first step unless the Venezuelan government takes credible and sustained measures toward convening postponed elections and ensuring the holding of presidential elections by the end of the current constitutional period.

2. The U.S. could increase monetary assistance to credible civil society organizations and nongovernmental organizations able to deliver food and medicines to Venezuelans. It should also visibly and publicly help front-line states address refugee flows with increased humanitarian aid. The U.S. government should publicize the availability of humanitarian assistance to make it clear that international pressure seeks to support democracy and not punish the Venezuelan people.

3. The United States could give preference to policies that contribute to efforts by the opposition in Venezuela to build an “off-ramp” that encourages moderate elements of the government to acquiesce to a transition to democracy because they are able to envision a future in which they can remain in Venezuela, even if they do not remain in power. Of these moderate elements, the most important is the armed forces. A large majority of the military is not involved in the worst crimes of the regime, particularly those that fall under U.S. or international jurisdiction. This majority is more likely to acquiesce to a transition of power if they receive credible commitments about their institutional and professional futures. The United States should signal to both the opposition and the government that following successful free, fair, and multiparty elections, it will focus its prosecutions and sanctions only on crimes that are violations of international laws or treaties, or those committed within the jurisdiction of the United States. Crimes committed within the Venezuelan jurisdiction should be addressed via local judicial processes. This may include various forms of justice, but this is ultimately up to Venezuelans themselves.

4. The United States could offer significant incentives for the holding of free and fair presidential elections in 2018 and for the opposition to unify and compete in those elections. This includes the offer of significant bilateral and multilateral support once such elections are held. Such support would involve coordinating with multilateral organizations such as the International
Monetary Fund (IMF) to develop and publicize a credible and generous plan to restart Venezuela’s economy on a path to growth in a way that includes protection for the most vulnerable elements of the population. Because average Venezuelans fear IMF economic prescriptions, it is important to communicate that an IMF-designed structural adjustment program would lead to increased consumption rather than further economic contraction as new funding becomes available for imports, particularly those inputs required to revive private production.

5. As a last resort, the United States could consider raising economic costs to the regime via an expanded sanctions regime. This would involve applying the full range of financial tools available to the United States to limit Venezuelan earnings from oil exports or to block further financing with the aim of shocking the Venezuelan government into changing course. This would need to be done in concert with stepped-up humanitarian assistance to front-line states and to local humanitarian organizations with a credible presence in Venezuela.

This last option carries significant risks. A broad sanctions policy would seriously damage relations with the majority of Latin American states. As has occurred with sanctions in other places, the Maduro administration would have the opportunity to more credibly shift blame onto the United States for its domestic policy failures and justify further authoritarian measures as needed to defend against a threat from the United States. And humanitarian assistance, particularly over the objections of the Venezuelan government, may not compensate for the impact of broad sanctions on average Venezuelans.

The members of the Brookings Institution Working Group on Venezuela are Dany Bahar, Charles T. Call, Richard Feinberg, Bruce Jones, Ted Piccone, and Harold Trinkunas. The Working Group members broadly agree with the analysis, conclusions, and recommendations presented in this paper, but not necessarily with every specific element. The views expressed here do not reflect the views of the broader Institution, its management, or its other scholars.

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