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Collapsing Venezuela

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If Venezuelan President Hugo Chavez deliberately intended to sabotage his nation's economy, he would be hard-pressed to do anything different from what he is now doing to his country.

It has been widely reported that Mr. Chavez has been increasingly taking control of the oil, telecommunications and energy sectors, as well as the media. What has not been reported is the full extent of the corruption in Venezuela and how this ultimately will destroy the economy.

The financial scandal taking place is far bigger than Enron, and may ultimately even exceed the U.N. "oil-for-food" scandal, the biggest financial disgrace of all time. Venezuela has had a rapidly growing economy for the last few years, due to high oil prices, but the house of cards is about to collapse. The former Venezuelan representative to Transparency International, Gustavo Coronel, has documented how much of this corruption has taken place in a report published by the Cato Institute's Center for Global Liberty and Prosperity.

Forty years ago, Venezuela had become a functioning democracy and was experiencing solid economic growth, but beginning in the mid-1970s corruption increased. Partially as a result, Hugo Chavez was elected president in December 1998 on an anti-corruption platform.

In the years since, Mr. Chavez has been dismantling the independent political institutions and sharply reducing transparency. He has also stripped the Central Bank of its independence and misappropriated much of its reserves. Some of the funds have been used to buy billions of dollars of Argentine bonds, to buy influence in Argentina. That country has not been able to sell bonds in the international markets since its 2001 default because Argentina still has not come to an agreement with its private creditors, despite having extensive and growing foreign exchange reserves.

The Argentine bonds were then sold by the Venezuelan government to cooperative local banks at artificial rates as a way to get rid of the bonds. Venezuela established exchange controls several years ago to try to reduce capital flight, which immediately resulted in a parallel (black or free market) market, giving Venezuela two different exchange rates (the official and the black or free market rate).

The government uses the existence of these two rates to reward "friendly" banks and "intermediaries" (some of whom are known terrorists).

Since 2004, the Venezuelan Central Bank has transferred about \$22.5 billion to accounts abroad by the Chavez government, and about \$12 billion of that remains unaccounted for. It has also been reported that the gold reserves have been removed from the Central Bank.

Mr. Chavez has also set up a "development bank," which operates without transparency. As the Chavez government takes over more and more of private industry, it also ceases reporting on the financial results of those industries, such as the state-owned oil company, which operates Citgo in the U.S. Mr. Chavez announced this month he will take over the privately owned telecommunications and power companies, and we can expect that shortly after he does so his government will also stop reporting their finances. Increasingly, Mr. Chavez uses the massive oil revenues the country receives, as well as other government revenues, as his own private piggy bank.

Where has all the money gone? It has gone to buy foreign political influence and loyalties in places like Cuba, Bolivia, Nicaragua and even the United States (notably to subsidize some New England fuel oil consumers through a company controlled by members of the Kennedy family). The money has gone to buy weapons from Russia, Spain and elsewhere, endearing those countries to Mr. Chavez. The money has gone to local cronies for inflated infrastructure and economic development projects and to buy the loyalty of government officials and supporters, including judges.

The Venezuelan economy will collapse, despite massive oil revenues because we know socialist economies perform poorly. While the rest of the world has been moving away from socialism for the last quarter-century for good reason, Venezuela is becoming socialist. We know governmental use of central banks to basically print money to cover expenditures results in rising inflation and eventually monetary meltdown.

Venezuela no longer has an independent central bank, and inflation is already up to 17 percent and rapidly rising. We know countries thrive with economic freedom but decline without it, and Venezuela is now down to 126 out of 130 nations in the 2006 Economic Freedom of the World the most rapid decline ever (in 1995 it was No. 75). And, finally, we know that when a state becomes totally corrupt an economic collapse always follows.

Mr. Chavez and his cronies had already been spending far more than they were taking in before the recent drop in oil prices. Without a big jump back up to \$70 a barrel or more for oil, the Venezuelans will be increasingly squeezed, and you can bet the blood from the innocent Venezuelan people will be drained long before those on the take from Mr. Chavez agree to have their looting stopped.

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