Latinvex

Argentina and Venezuela: Outlook Worsens

Recent changes in Argentina and Venezuela will worsen the business and economic environments.

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Economic policies in Argentina and Venezuela are expected to worsen, making it even harder for local and foreign firms to operate in those countries, experts warn.

The appointment on Monday of Axel Kicillof, a leftist economist, as economy minister in Argentina increases the likelihood of a double exchange rate for the dollar as well as more radical policies aimed at restricting the private sector.

“Already there are indications that his ministry is considering the introduction of a two or three-tier exchange rate system, comprising separate rates for tourists as well as for importers and exporters,” IHS Global Insight analyst Carlos Caicedo wrote today. "The latter is a reflection of the government's serious concerns about dwindling foreign reserves.”

Kicillof, who was the mastermind behind the 2012 nationalization of Repsol’s assets in Argentina, is known to be conflictive, avoid compromises and sees power as a way to impose his Marxist and Neo-Keynesian model, Argentina’s leading newspaper La Nacion says in a profile. “He is convinced that businesspeople are suspect by nature,” the paper says.

The appointment of Kicillof led to the resignation yesterday of commerce secretary Guillermo Moreno, who controlled prices and imports using strong-arm tactics that earned him a reputation as a bully, according to Bloomberg.

The resignation had been expected as Kicillof was seen as the new head of economic policy, according to a briefing from public relations company Edelman on Tuesday.

Kicillof is now expected to choose a successor for Moreno that would respond to his orders, Edelman said in a briefing today.

While Moreno’s image had deteriorated in recent months due to the failure of fighting inflation and legal problems over his confrontation with independent economists, his overall policies will likely continue, providing continued headaches for companies doing business in Argentina. “Nothing would change if the person named to replace Moreno continues with the same kind of politics and decisions taken up to now,” Edelman says.

Further strengthening Kicillof was the appointment of his ally Juan Carlos Fabegra as the new president of the Central Bank.

“The reshuffle shows [President Cristina] Fernandez maintains firm control of her government, but also that her last two years in office will not deviate from the controversial policies that have led to the introduction of a string of currency, price, and import controls, which have significantly undermined the country's business environment,” Caicedo says.

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Meanwhile, on Tuesday, Venezuela’s national assembly granted President Nicolas Maduro decree powers for up to a year.

“A package of laws is now likely to be approved in the next few days [that will] likely ... cause further deterioration of the already-affected business environment in Venezuela, leading to further government intervention, more inflationary pressure, and scarcity of goods. This will in turn exacerbate the ongoing economic crisis in Venezuela, potentially increasing the risks of looting and political instability,” IHS Global Insight analyst Diego Moya-Ocampos wrote in an analysis today.

A planned law of costs and prices will introduce more price controls and percentage caps on profits for companies operating in all sectors of the economy, while a law of foreign trade will condition the granting of dollars for imports to certain commitments over price and conditions on the selling of imported products, he says.

“A law of corruption is also expected to be approved, which will be aimed at putting more pressure on retailers and manufacturers and …new legislation is also likely to include simplified and shortcut procedures for expropriation and for authorities to take over assets of companies suspected of "speculating" even in sectors considered as non strategic by the government,” Moya-Ocampos says.

Should a percentage cap on profits be introduced, this will clearly become a game changer for those businesses operating in an already hostile business environment, he warns. Previously, private businesses had seen the high regulatory burden and intense controls by these forces mitigated by the potential of the Venezuelan market. Indeed, under Chávez, businesses benefited from record high oil prices and were still capable of generating significant revenues and profits, Moya-Ocampos points out.

“The change of the risk-reward equation will most likely force them not to renew their inventories and probably shut down their businesses,” he warns. “During 14 years of Chávez rule, businesses had faced increased expropriation risks and difficulties to repatriate funds, but never limits on their profit margins, which had been the only driver to stay in Venezuela.”

Before the decree powers, Venezuela was expected to see GDP growth of only 1 percent this year, the lowest of any country in Latin America, according to a Latinvex analysis of estimates from the International Monetary Fund (IMF). Next year, it was expected to have an expansion of 1.7 percent, which would be the second-lowest in the region after El Salvador.

Meanwhile, the reluctance of businesses to replenish their inventories is likely to trigger shortages of non-essential goods, such as electric appliances, gadgets, and automotive parts, adding to the already existing of food and basic goods.

“This in turn will lead to further inflationary pressures at a time when annual accumulated inflation has reached 54.3 percent,” Moya-Ocampos predicts.

Venezuela is likely to have the world’s highest inflation rate this year, according to a Latinvex analysis of forecasts from the IMF for 188 countries. Iran, the second-worst country, will likely see inflation of 42.3 percent.

However, currency expert Steve Hanke calculates that Venezuela’s inflation is actually much higher. “The implied annual inflation rate in Venezuela is actually now in the triple digits, coming in at a whopping 283 percent,” he writes in an analysis published by the Cato Institute.