

## **Banking crisis challenges Venezuela's Chávez**

*Geri Smith*

*Will problems at some banks bring an end to Venezuela's well-connected Boli-bourgeoisie? Some are under arrest.*

They're called the Boli-bourgeoisie, a small cadre of favored Venezuelan businessmen who have become wealthy through their connections to President Hugo Chávez. Although their nickname comes from Simón Bolívar, the Latin American liberation hero in whose name Chávez has been steering the country toward socialism since taking office a decade ago, their motivation is less revolutionary than capitalistic.

Thanks to several years of high world oil prices, Chávez went on a government spending spree, and the Boli-bourgeoisie tapped billions in petrodollars to build flashy personal empires.

But with oil prices down from their 2008 highs, tight public finances are squeezing Chávez' "Bolivarian Revolution" and focusing attention on the excesses of the Boli-bourgeoisie.

Since Nov. 20 the government has closed seven banks, ordered the arrest of 27 bankers, and forced out a loyal cabinet minister to prevent a banking scandal from turning into a full-fledged financial crisis. The shakeup threatens to fracture support for the President at a time when falling oil revenue is forcing Chávez to trim popular antipoverty programs that have been key to his long tenure in the presidential palace.

### Threat to nationalize

Chávez, who took office in 1999 promising to end corrupt links between government and business, was caught off balance by the revelation that several banks owned by his supporters were in financial trouble after engaging in questionable business practices. Some were seriously undercapitalized, others were apparently lending top executives large sums of money, and at least one financier couldn't prove where he got the money to buy his banks in the first place. On Dec. 4, Chávez threatened to nationalize the entire banking system but backtracked after the country's benchmark dollar bonds plunged and some of the 1.2 million affected bank account holders rushed to withdraw funds.

Two days later he accepted the resignation of Science & Technology Minister Jesse Chacón, whose brother, Arne Chacón, a former Army officer who had become wealthy as head of one of the seized banks, was arrested. Another top businessman, Ricardo Fernández Barrueco, who owned several of the affected banks and had made a fortune importing food for the government's subsidized food program, was also jailed on embezzlement and other charges. The government has asked Interpol to arrest nine others.

"We are demonstrating that there are no untouchables here," Chávez said in a television appearance, part of an effort to quell criticism by political backers who found the behavior of the magnates—who are also sometimes referred to as Boli-garchs—offensive in a country where around half the population lives in poverty. Many of the newly rich businessmen flaunted their wealth publicly, snapping up corporate jets, yachts, real estate, and race horses.

### Careful not to overreach

In recent years Chávez has made steady progress in his efforts to expand government control over key sectors of the economy, from agriculture to electricity, cement, and oil. Two years ago the government expropriated a number of major oil projects belonging to international oil companies, and in May it nationalized more than 70 oil-service companies to which state-

owned oil company PDVSA owed billions of dollars. The company is suffering a cash crunch caused by low world oil prices.

In July the government took over Banco de Venezuela, owned by Spain's Banco Santander, paying \$1.05 billion.

Although many people believe Chávez would like to expand government control of the banking system, a recent poll showed that 70% of Venezuelans are opposed to outright nationalization, and the President seems to understand that can't be a short-term goal. "Chávez was acutely aware that if he went too far in taking over the banks, he would put the economy at risk," says Michael Shifter, vice-president at the Inter-American Dialogue, a policy think tank in Washington. "He's smart enough to know when to stop."

Following his reelection in 2006 to a third term, Chávez enjoyed approval ratings exceeding 70% as he capitalized on high world oil prices to fund antipoverty initiatives. Chávez's business backers also benefited from a consumption boom that fueled imports of everything from food to luxury vehicles. Earlier this year Chávez won a referendum eliminating presidential term limits, allowing him to run for reelection indefinitely.

#### A plunge in the polls

But collapsing oil prices and a 5% drop in Venezuelan oil production this year forced cuts in government spending on Chávez's health, education, literacy, and subsidized-food programs. Those programs had been reaching 46% of Venezuelans, but by mid-2009 just one quarter of the population was receiving benefits. Chávez's approval rating fell from 57% in February to 46% in October, according to Datanalisis, a Caracas firm that conducts nationwide political polls and market research.

"A big part of his popularity has been linked to people's ability to consume, and the drop in oil prices has had a big impact on that," says Datanalisis director Luís Vicente León. In addition, water shortages and electricity blackouts have worsened in recent months, further eroding support for the government.

Still, Chávez retains the support of nearly half of all Venezuelans, and he continues to have an uncanny ability to transform economic and political crises, even those of his own making, into pluses. This latest financial upheaval may actually end up strengthening him as he portrays the ousted bankers as "vulgar thieves" and "pickpockets,"—even though they were among his favored supporters until very recently.

#### Shifting alliances

The banking and corruption crisis, however, underscored schisms in Chávez's government coalition. The crackdown on the errant bankers sends a clear message to other supporters that they must hew more closely to the revolutionary message. "This reflects a power struggle and shifting alliances between the different factions within the government and among its backers," says Roberto Bottome, editor of VenEconomía, an economics newsletter published in Caracas. "Some of these guys were getting too big for their britches and had to be reined in," he says.

Chávez had to move quickly to restore consumer confidence in banks, as Venezuelans remember well a 1994 banking crisis that led to the closure of half the nation's banks and the loss of many depositors' life savings. For now, Venezuela's banking crisis appears to be under control: The seven banks taken over so far account for around 12% of total deposits, while the country's top 10 banks, which account for more than two-thirds of deposits, are profitable and well-capitalized.

But Ruth Krivoy, an economist and former president of the Venezuelan Central Bank from 1992 to 1994, notes that Chávez still faces some tough economic realities. Although the price of Venezuelan crude has rebounded to around \$72 a barrel from a January low of \$35, the government is expected to post a fiscal deficit equal to 5% of gross domestic product this year and around 10% in 2010, she estimates. Oil revenue accounts for 90% of Venezuela's exports and half the government's budget.

The economy is in recession for the first time since 2003, shrinking by 4.5% in the third quarter from a year earlier, and is likely to shrink by 2.2% for 2009 overall. Inflation is running at 29%, one of the world's highest rates. And while the official exchange rate for the Venezuelan Bolivar is 2.15 per U.S. dollar, the recent turmoil has helped push the currency to nearly 6 to the dollar on the parallel market.

With congressional elections coming in September, Chávez is determined to restore calm so he can maintain his overwhelming majority, since he needs a two-thirds vote to push through his reform agenda. He may well manage to do so, as Venezuela's splintered opposition has failed to capitalize on Chávez's foibles. "The model Chávez has created over the past decade is definitely showing some soft spots," says Shifter. "But he is resilient and shouldn't be underestimated."

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