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MBA 678 – International Business

Case Study –Venezuela under Hugo Chavez and Beyond

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The case discussion questions are :

1. Under Chávez's leadership, what kind of economic system was put in place in Venezuela? How would you characterize the political system?

A/ Under Chavez's leadership, Venezuela operated under a command economy. A command economy is an economic system where the allocation of resources, including determination of what goods and services should be produced, and in what quantity, is planned by the government. Soon after taking office, Chavez worked to consolidate his hold over the apparatus of government. A constituent assembly, dominated by Chavez followers, drafted a new constitution that strengthened the powers of the presidency. Chavez also gained government control over the media.

A 2003 study by the World Bank concluded Venezuela was one of the most regulated economies in the world and that state controls over business activities gave public officials ample opportunities to enrich themselves by demanding bribes in return for permission to expand operations or enter new lines of business. Under Chavez's leadership, Venezuela's political system could be characterized as social democracy. Social democracy is a political movement advocating a gradual and peaceful transition from capitalism to socialism by democratic means. Socialism is a way of organizing a society in which major industries are owned and controlled by the government rather than by individual people and companies.

Furthermore, Consistent with his social rhetoric, Chavez has progressively taken various enterprises into state ownership and has required that other enterprises be restricted as "workers' cooperatives" in return for government loans. In addition, the government has begun to seize large rural farms and ranches that Chavez claims are not sufficiently productive, turning them into state-owned cooperatives.

2. How do you think that Chávez's unilateral changes to contracts with foreign oil companies will affect future investment by foreigners in Venezuela?

A unilateral change is any change made in the provisions of a contract without the consent of all parties involved. Chavez extended government control over foreign oil producers doing business in Venezuela, which he accused of making outsize profits at the expense of a poor nation. In 2005, he announced an increase in the royalties the government would collect from oil sales from 1 percent to 30 percent, and he increased the tax rate on sales from 34 to 50 percent.

Due to these extreme changes implemented by Chavez, it seems apparent to me that foreign investors would be unlikely to want to work in and with Venezuela in the future. This lack of foreign investment into Venezuela's oil industry would have a negative effect on the overall economy of the country, as oil accounts for 70 percent of the country's exports. Another example involves that of Russia. Russia does what it wants when it wants. Unilateral changes that Russia makes in contracts with different items make it unlikely that foreigners should or would want to invest in Russia.

The Russian government is very controlling and corrupt, which ultimately decreases the amount of foreign investment in Russia. Russia seizes and controls many enterprises so that the state can benefit from them. The economy and state of doing business there is too up and down for foreigners to want to set up shop there. There is too much uncertainty that it would not be advisable to invest there. Take your money and invest it elsewhere.

3. How will the high level of public corruption in Venezuela affect future growth rates?

As stated in the article, Venezuela was ranked in 2012 165th out of 174 nations of the level of corruption. Because of the corruption happening in the country many people are going to want to leave, which will lower their population count.

Once people see that people are leaving then people won't want to visit or move. Therefore these high levels of corruption rates will affect future growth rates.

4. During the latter part of Chávez's rule, Venezuela benefited from high oil prices. Since 2014, however, oil prices have fallen substantially. What has the effect of this been on government finances and the Venezuelan economy?

High oil prices helped the Chavez government to gain higher income through the export of oil and it helped in reducing unemployment, decreasing poverty, and funding the other social programs. Here, Chavez also made an error of not consolidating upon these export values and took erroneous decisions such as replacing experts by his own people that siphoned the funds for their own benefits. When the oil price came down, then earning the government from the export of oil, also came. Further, the volume of exports also came down. It reduced the major source of income and the government has to restrict its finances.

For this purpose, many people were laid off that pushed unemployment to a new high. The poverty level was also at the highest level. Besides, the poor value of domestic currency laid to the inflation in the economy and there was a lack of availability of the necessary goods. It created social anarchy in the country and pushed the economy on the verge of total collapse.

5. During the Chávez years, many foreign multinationals exited Venezuela or reduced their exposure there. What do you think the impact of this has been on Venezuela? What needs to be done to reverse the trend?

I believe that with these multinationals exiting Venezuela it did have an impact on society. Inflation is one of the things that happened, because of the shortage of products coming into the society it has begun to collapse. The new leaders need to work out a way to get supplies coming back into the country. Multinationals are a blessing and a curse simultaneously. While they employ lots of people and pay for local services, they have a big problem too. They do not invest in the host country, instead of expropriating profits to the home country.

This is not always a terrible thing as long as they are employing thousands of people. Sure it would be better if the local country could do what the multinational does but it can't.

For instance, Ireland's economy has doubled multiple times due to the lowering of tax rates as an inducement to multinationals. Mexico is a mess and a disaster in every way, the only way they have remained afloat is via the multinationals that build lots of things there and expropriate profits.

It is a misnomer of the socialist core philosophy that multinationals drain and steal the assets of the country. They use the assets, which is what a nationalized company would do as well. What multinationals fear most is instability and nationalization! As this is socialist dogma, whenever they get a whiff of it, they make plans to leave.

As a result, the Chavistas are compromised by losing the multinationals. The profits that are sent out of the country would have hurt the country much less than the incompetent, inefficient, and corrupt management that took over. Multinationals become multinationals not because they are stupid, they are so because they are really good at their respective businesses.

Reference:

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