

The contents of this document are preliminary and subject to change.

GRAY/04/2277

September 13, 2004

**Statement by Mr. Duquesne on República Bolivariana de Venezuela
(Preliminary)
Executive Board Meeting 04/86
September 13, 2004**

We would like to thank staff for their comprehensive set of papers, as well as Messrs. Marti and Villavicencio for their detailed buff statement.

As recalled by many other directors as well as Messrs. Marti and Villavicencio, Venezuela is facing important challenges for its development and during this discussion today we will contribute to defining what could be a feasible way to durably strengthen the growth path.

Let me first say a few words about the recent political developments and their implications on the growth perspective. First, it is clear that the Venezuelan people have made a choice and it is now time to look forward. In this respect, we would like to emphasize that, broadly speaking, the country is not only in deep need of structural reforms, but also of a strong political – and social – consensus on the reforms. We thus urge the authorities to take advantage of the political turmoil's end to make further progress on that point and welcome the reassuring information provided in Messrs. Marti and Villavicencio's buff statement. We also found helpful the discussion in the staff report on the two policy scenarios, although we found them a bit too extreme. Nevertheless, to be fully effective, such a report should be published and we thus regret the authorities' decision of opposing its publication. In any case, we fully concur Mr. Reddell while encouraging a continuous dialogue between the authorities and the staff.

Let me now turn to the growth agenda. There are two issues: first, growth stabilization and second, growth enhancement.

Regarding the former, the staff report clearly highlights the fragility of the current situation: the economy and the fiscal stance are very much dependent on oil revenues. This dependency requires a strict control of expenditures and in this respect we fully share the staff's suggestion. Furthermore, a deeper reform of tax revenues should be implemented and, again, we fully endorse the staff suggestion, like broadening the VAT base and more generally reducing the non-oil fiscal deficit. Like Mr. Lushin and Mr. Steiner, we encourage the authorities to strengthen the role of the oil stabilization fund.

All these measures constitute a quite natural road-map to follow and the main issue is whether or not the authorities can secure the large consensus needed to implement these reforms, not even to mention the other required reforms.

This leads me to the second issue, namely improving the growth prospects in the medium and long run. We take note of the authorities' intention, as recalled by Messrs Marti and Villavicencio, to, I quote, "balance social and economic priorities". Fundamentally we share this point, but I would like to introduce some nuances. These two priorities should be seen as complements and not substitutes: improving social indicators is definitely a very efficient way to disseminate the advantages to be expected from the reforms.

Moreover, we urge the authorities to make every effort to improve the non-oil sector. The diversification of the economy should be a key priority to enhance the growth prospects and address social issues in a durable manner.

Like other directors, we are concerned by the declining level of investment and the authorities should react by leaving a greater part to the private sector in the economy.

Finally, we fully concur with the staff appraisal on monetary policy. Given the need for a tighter policy and the fact that open market operations won't be sufficient to contain pressures we recommend the relaxation of foreign exchange controls, as well as a gradual shift towards a flexible exchange rate system. However, we recommend caution in this process:

- given the likelihood of a decrease in oil price, depreciation pressures on the currency could materialize in the rather near future. We thus feel that reserves should be kept to a sufficient level so as to limit the risks of a financial crisis in case of a lifting of capital controls and should thus not necessarily be used to slowdown the depreciation of the currency;
- the banking system is still very fragile, and we suggest first strengthening it and deepening its surveillance. Like Mr. Padoan, Mrs. Indrawati and others we encourage the participation to the FSAP exercise.

With these comments, we wish the authorities all the best.