

# **How Socialism Failed Venezuela**

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## Abstract

*In the 1970s, Venezuela was considered one of the wealthiest nations in the world. They enjoyed high oil prices after the discovery of OPEC, they were a democratized country in a continent where most of it was still undeveloped. Unfortunately, in the 1980s a major cut in oil prices caused economic turmoil, and leading into the 90s there were bloody riots, political disparity, attempted coups and building poverty. In 1998 came Hugo Chavez, a newly elected president to rid their economic issues and end corruption. However, that all turned out to be the opposite of what he did. The country of Venezuela today is seen around the world as a country of overrun corruption, economic depression, mass malnutrition and fierce dictatorship. While the country has the world's largest oil reserves, Venezuela struggles today in economic hardships, and many political leaders in our country have been debating how they went from the second wealthiest nation in the western hemisphere to a crushed society. This thesis dives into three big features as to how Venezuela collapsed: state ownership, social welfare programs, and political corruption. After extensive research, it concludes socialism is what really killed this nation, and a dangerous central government ran by a small group of corrupt elites now holds the destiny in their future.*

## Introduction

This thesis dives into three sections: state ownership, social welfare programs and political corruption. The three upcoming sections are relatable to the collapse of Venezuela because they are all causes of their economic downfall.

When Hugo Chavez came into power in 1999, he made a promise to his citizens: rid economic inequality and political corruption. It all sounded great, but it unfortunately didn't work, as they are now one of the most corrupt countries, and their attempt at economic equality ended up with economic collapse, destroying millions of citizens financially, and it is so bad that its citizens are fleeing to venture new opportunities.

This thesis is very unique because Latin American history is not well studied in many universities, and it is a big debate between the Democrats and Republicans on how Venezuela collapsed. I chose to explain what the leftist and conservative ideologies were behind each of Chavez's moves, and an informative explanation as to how each section failed. While the leftists theorize and admire a more socialist system, the conservatives prefer a more capitalist system. While there are pros and cons to each side, I found that the leftist movement and Chavez's "21<sup>st</sup> Century Socialism" was really the ultimate fault, but it was also thanks to Chavez and Maduro's corrupt regimes, from censoring and jailing those who publicly criticize their leaderships, to fundraising for the Hezbollah.

However, Chavez's "Bolivarian Revolution" was motivated through populism, and there was mass economic inequality in the country. The heads of the government would take large portions of oil profits and share it with the economic heads of the country. In fact, many of the poor before Chavez's run for presidency in 1998 didn't participate in Venezuelan politics because they felt they were never represented. Chavez brought hope to the country to make everyone's lives better, and although it sounded great, it ultimately failed, mainly due to the implementation of his socialist policies.

## State Ownership

Former President Hugo Chavez (1998-2013) sought state ownership of the oil industry to help with providing revenue for his social welfare programs. His reasons are tied with the history of Venezuela and its experiences with foreign countries.

Dating back to the Andinos in 1899 until their ruling came to an end in 1958 (except an interlude from 1945-48), five successive dictators controlled Venezuela. And among their controls was the oil industry. During their rule, the British and Dutch were granted generous contracts to enter Venezuela to work with their petroleum. After World War I, the United States came into competition against the British and the Dutch for standard oil, and by 1928 Venezuela became the world's largest petroleum exporter, and only behind the United States in oil production. The oil industry brought high paying jobs, and provided funding for extra government spending, government construction of railroads, streets, and port facilities. (J. L. McCoy et al. 2020)

Although the high paying jobs sounded great, the uneven distribution of oil prosperity was evident. Most Venezuelans continued to live in poverty as the housing, education and health needs were ignored by the state. (J. L. McCoy et al. 2020)

This disparity led to a political party called Democratic Action. Democratic Action drafted a tax decree to assure the nation it would receive at least half of the oil profits, and also encouraged labor unions to bargain for their rights. It supported equal health, housing, industrial development, agriculture and education policies. These reforms ended up causing a strong opposition from the conservative forces and resulted in a military coup in November of 1948.

The end of Democratic Action came with its overthrow by dictator Perez Jimenez, crushing all the work the Democratic Action had achieved, and the 1950s was a period of Jimenez's consolidated power.(J. L. McCoy et al. 2020)

Following up, in 1963, the Democratic Action narrowly won the election for president by Raoul Leoni. And the opposing Christian Democrats party vanished and was replaced by a strong leftist labour party Democratic Republican Union. Then, Rafael Caldera's inauguration in 1969 marked the first time Venezuela peacefully switched power to an opposition electoral victor. In the early 1970s the country established majority control of foreign banks, took control of the natural gas industry, and declared a moratorium on the granting of oil concessions. (J. L. McCoy et al. 2020)

President Perez, the Democratic Action victor elected in 1973, nationalized the iron ore industry in 1975. Following the Arab-Israeli War of 1973, Venezuela, a founding member of OPEC, more than tripled the price of its oil. In 1976, Perez nationalized the petroleum industry. This resulted in a wave of spending that attracted thousands of South American immigrants, increased imports of food and luxury items, it also brought political corruption and waste, created a privileged economic elite, but did little to alleviate poverty.(J. L. McCoy et al. 2020)

This economic boom didn't last, as a recession occurred in the late 70s as a result of slashed world oil prices, which plunged the country into economic stagnation. Into the late 80s, this problem persisted with a decline of exports, growing unemployment and a downward trend of GDP. From 1989-1991, major protests, labor strikes, and an increasingly heated political debate emerged as Perez attempted to reduce tariffs and reduce government intervention in the economy. This followed a precipitated coup by Hugo Chavez in 1992. Then former president Caldera returned to power in 1993, running as an independent after breaking from the Social

Democratic party. Caldera released Chavez from prison before his trial ended, making him eligible to run for office. Hugo Chavez was then elected president in 1998. (J. L. McCoy et al. 2020) During his term, he pledged to lead the Bolivarian Revolution, a plan to implement social welfare programs to cure the economic inequality the country historically had, and rid foreign influence.

The Bolivarian Revolution derives its name from Simon Bolivar, a famous revolutionary that sought south American independence from the Spanish Empire. From 1813-1819, he led battles against Spain and successfully gained independence for Venezuela. (Simon Bolivar Biography | n.d.) Chavez wanted to create a system of income distribution that he claimed would “progressively eliminates the great difference that exists between a minority that has everything and a huge majority that has virtually nothing except hope.” (J. McCoy and Newman 2001) The Bolivarian Revolution includes state ownership. One reason for Chavez’s nationalization of the oil industry was to use oil revenues for social welfare programs.

The leftist forces in Venezuela chose to nationalize the oil industry because it’s the country’s most valuable and lucrative resource. They also have the world’s biggest crude oil reserves and want to secure the resource for development.

The issue with nationalizing their oil industry is the country’s leadership wouldn’t let foreign investment in their industry, therefore causing difficulties with developing enough oil. It wasn’t until 1997 when the country allowed foreign investment into their industry, and when investment came they were able to develop the heavy crude oil in the Orinoco belt, resulting in a recovery in 3.5 million barrels per day, nearly reaching its former high. (Rapier 2019a)

ExxonMobil, ConocoPhillips, Chevron, BP and Total are a few example of companies that planted investment in Venezuela’s oil industry. These companies invested money in

infrastructure and technology to help with the production of oil, resulting in billions of dollars. (Rapier 2019a)

Later in 2007, Chavez caused a disaster. When the oil prices were rising that year, his government sought more revenue from the oil, and demanded that the PDVSA (Petroleos de Venezuela, the Venezuelan state-owned oil company) gain majority control of the projects. ExxonMobil and ConocoPhillips refused, and as a result their assets were expropriated, meaning their ownership was stolen for state ownership. This move turned out to be highly illegal, resulting in compensation being granted to both companies. (Rapier 2019a) ConocoPhillips, for example, won \$2 billion in compensation. (Krauss 2018)

Chavez's failure to appreciate the capital investment made by foreign companies required to continue developing oil production, and when the oil prices were high, he funneled billions of dollars from it to the social welfare programs, but failed to reinvest in this industry, and following the expropriations, the oil production went on a steep decline, more than a 50% drop leading in 2018 from 2006. (Rapier 2019a)

If Chavez would never have forced expropriations on foreign investment, the oil industry would probably still be able to produce high amounts of oil. They needed foreign investment to get better at production, and then Chavez forced more control of the oil industry, leading to some investors leaving, and then Venezuela was forced to compensate these companies. The unappreciation of the capital-investment from foreign industries for oil production was the problem with Venezuela's state ownership.

## Social Welfare Programs

A big movement as stated above was the populist appeal of Chavez, and that was the “Bolivarian Revolution”, which is the implementation of mass social welfare programs to try dealing with the economic inequality in the country, and using oil profits to fund it.

In 1998, more than half of Venezuela’s population was below the poverty line. Annual inflation exceeded 30%. The voters rejected the traditional parties (Democratic Action and COPEI (Social Christian Party)), and voted for Chavez. His political platform promised to rid the country of corruption, help the poor and reduce the power of elites. He also pledged to create a new constitution, and in mid-1999 Venezuelans elected a constituent assembly dominated by pro-Chavez delegates and then came a new approval of a referendum. (J. L. McCoy et al. 2020)

Before Chavez, the wealthy and business owners prior to Chavez experienced and received an overvalued exchange rate, protection from foreign competitors, investment incentives, higher wages and job protection. In fact, between 1959 and 1980, investment incentives ranged from \$3.82 million to \$721.35 million, despite the collapse of the international petroleum market, massive national debt and increasing public and private indebtedness.(Crisp and Levine 1998) The top still enjoyed high amounts of wealth while the rest were dealing with economic blunders. Chavez saw issues like these, and when he ran for president in 1998, he promised to rid this economic inequality. He had policies that were meant to deplete economic inequality, but the implementation of them faced difficulties and eventually failed as we see Venezuela today.

There were three main policies carried out by his regime since 1999 that caused their current crisis: widespread nationalization of the private industry, currency and price controls, and the expansion of social welfare. (Martino 2019)

Chavez's quote "to those who own the land, this land is not yours. The land is not private, it is the property of the nation."(In Venezuela, Land Redistribution Program Backfires n.d.) It is a quote made when he began forcing the takeover of private land and distributing it to state ownership. One of Chavez's first actions was to start nationalizing the agriculture sector, by taking land from rich landowners and giving it to the poor. From 1999-2016, Venezuela robbed almost 15 million acres from its current owners. The problem with the nationalization of thousands of businesses is no government has the capacity to run all of them efficiently given the lack of profit it gives. The other problem with this is the government will sell products at a lower prices and hiring more employees than needed, they do this to please its voters they have. As state control increased with agriculture, food production fell 75% in two decades while the country's population increased by 33%. Later, electricity, water, oil, banks, supermarkets, construction and other crucial sectors were now controlled by the state.(Martino 2019)

However, Chavez was elected because of the populist appeal. Chavez did the stripping of land and price controls because he tried to get rid of the economic inequality. In 2002, an estimated 5% of the population owned 80% of the country's private land. Chavez quoted "The oligarchy is always on the attack and trying to say you are no good, they think they are the owners of the world." (Romero 2007) Chavez was elected to cure economic inequality, and his "21<sup>st</sup> Century Socialism" was supported by the majority of the population. The country has seen a small amount of people obtain the majority of wealth, and Chavez promised to do something about that.

Capitalism is the most efficient economic system. However, despite its commonality, economists criticize capitalism in that it produces inequality, economic instability, excess materialism and boom and bust cycles. (Pettinger 2019) Leftists argue that capitalism creates



monopoly power, which creates corporations to charge higher prices to consumers, thus leaving the poor with difficulties to purchase products. The biggest criticism is greed, in that a capitalist system can create incentives for managers to pursue profits over social welfare. Chavez saw this as an issue that was going too far, and it helps explain why socialism was popular in the country.

When it comes to nationalizing owned land also comes with price controls. The price controls were implemented to make resources more affordable, and the ceilings ensure that those who demand the product would have an easier time getting them. They are also there to prevent producers from prices that are too high to be consumed. It goes back to greed in capitalism, in that managers will be socially immoral and charge whatever prices they want, even if it is not good for the majority of the population.

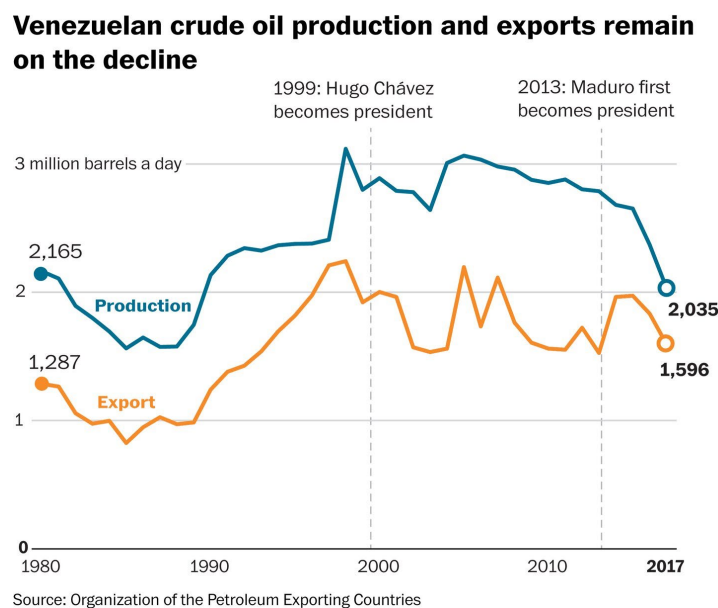
The Venezuelan government set price controls in 2003 on around 400 basic foods to counter inflation and protect the poor. The price controls led to an economic disaster, and shortages began appearing. Major private supermarkets suspended sales of beef for pricing sales above the government-set levels, and while Chavez has blamed the corporations themselves for being “unscrupulous speculators,” industry officials say government price controls have strangled profits.(Pearson 2007) Another issue with the price controls is when the ceiling is set below the market price, there will be excess demand or a supply shortage. This is because consumers will demand more because the goods are cheaper.(EconPort 2006)

When it comes to providing social welfare programs, the government must take more control of the economy to put an effort to making it work. That’s why the sectors above were nationalized. However, Chavez went further and implemented a currency control scheme, where the government would set an overvalued exchange rate between Venezuela and the United States. A goal of the scheme was to reduce inflation by overvaluing its currency, subsidizing

imported products. But the issue with this is the regime had to ration available US dollars to importers, and the other issue was the US dollar was more valuable than Venezuela's currency. This resulted in a black market for foreign currency and corrupt regime members assigned cheap US dollars obtained large profits. The scheme actually increased inflation since overvaluing the currency resulted in decreased oil revenues in Venezuelan currency, leading the regime to print money to cover the ensuing budget deficit. (Martino 2019)

Despite the government's enjoyment with higher government oil revenues due to a tenfold rise in oil prices from \$10 a barrel in 1999 to more than \$100 in 2008, the regime financed a growing deficit by printing more money. Expanded welfare programs and public-works projects resulted in more money printing. (Martino 2019)

Chavez's projects were economically unsustainable. Although from 1999-2008 the oil prices were high, the following years proved very troubling. Oil production remained steadily high until 2017, but the exporting of oil began to decline. (Venezuela's crisis in 5 charts - The Washington Post n.d.) The chart below shows.



Although Venezuela enjoyed high oil prices during the 2000s, after 2010 the chart shows a steady decline in production, and in more recent years a sharp drop in exporting oil.

According to cncb.com, Venezuela's hyperinflation hit 10,000,000% in 2019, and they now owe \$100 billion to foreign creditors, their state-run economic model wasted the world's largest oil reserves, and its educated, professional class has fled the country.(Sanchez 2019)

Venezuela ultimately failed with socialism because they ran very large budget deficits every year, even as oil prices skyrocketed from 2005-2014.(Toro 2017) The country is considered as a failed petrostate, oil sales account for 98% of export earnings and as much as 50% of its GDP. Oil production reached a new low in 2018 and has been declining for quite some time. Their GDP shrunk by double digits from 2015-2018, their debt is soaring as they have missed billions of dollars in payments since defaulting in late 2017. (Rocio Labrador 2019)

## **Political Corruption**

When it comes to politics, corruption can happen easily. When it comes to bigger central governments, it is often more prominent, and Venezuela is among many great examples of this. The political corruption from a worldwide view remains high throughout many levels of Venezuelan society. The survey based Corruption Perceptions Index (CPI) indicated with a score of 100 being perfectly clean, and 0 being as corrupt as possible, Venezuela's score is 35. (Transparency International n.d.)

Hugo Chavez promised to rid corruption when he ran for his presidency, and it turned out to be an unfulfilled promise. In 2003, Chavez fired 19,000 employees of the state oil company PDVSA (Petroleos de Venezuela, S.A.), and replaced them with employees loyal to his

government. Not only was this a dirty move, it also eliminated a lot of the skilled and experienced employees that worked for the company. (Rapier 2017b)

In 2004, Chavez and his legislative allies completed a political takeover of its Supreme Court, and filled it with his supporters and made new measures to wash justice from the court. Since then, the court lost its role in checking executive power, which helped destroy their constitution. (Human Rights Watch 2012)

With this move, Chavez gained the ability to rule by decree. In December 2010, the National Assembly passed an enabling law that granted Chavez to rule by decree on a wide range of issues for 18 months. By November 2011, he adopted over 20 legislative decrees. (Human Rights Watch 2012)

The media, once able to criticize political figures, is now oppressed. The government has discriminated against media that air political opponents' views, which gives stronger power to the government to limit speech. Not only is television censored, but the internet has also been under oppression as well when in 2010 the National Assembly extended its statute. The telecommunications law grants the government to suspend or remove freedom to private outlets.(Human Rights Watch 2012)

The government took a step further and began prosecuting government critics. In July 2011 Oswaldo Alvarez Paz, a member of an opposition political party, was sentenced to two years in prison for criticizing the Chavez administration on TV saying so-called "false information" claiming Chavez was not a democrat and "Venezuela has turned into a center of operations that facilitates the business of drug trafficking."(Human Rights Watch 2012)

Crime has been another issue. The police in Venezuela have been known for its corruption with the state and abusing their own powers among its people. Between 2000 and

2009 for example, law enforcement killed an estimated 7,998 people, and another estimation is that police commit one of every five crimes.(Human Rights Watch 2012) The book *Bumerian Chavez*, written by Emili Blasco, contains a number of allegations that point to formerly high ranking Chavistas (men who were loyal to Chavez), and among those accusations was drug trafficking. The book describes a scene in 2007 between Chavez and the high command of the Columbian Marxist guerilla group, the FARC, in which the FARC would give drugs to the Venezuelan government in exchange for military weapons and cash. The drugs would be stashed inside the cattle. It also discusses how the Chavistas would illegally monitor the vote count to alter the results in favor of Maduro and describes how Nicolas Maduro (at the time he was Chavez's foreign minister) negotiated with the Hezbollah, an Islamist extremist group, to fundraise in Venezuela.(Nagel 2015)

Along with the fundraising negotiated between the Hezbollah and Maduro, the United States in 2008 accused Venezuela providing financial aid to the terrorist group, including the Venezuelan Embassy in Damascus, Syria. Venezuela's temporary ambassador Ghazi Nasr Al-Din in Syria gave two Hezbollah representatives specific bank accounts to deposit contributions towards the terrorist group.(Treasury Targets Hizballah in Venezuela n.d.)

In 2008, more than \$22.5 million in dollar transfers were made to foreign accounts, and at least half of that remains unaccounted for. It is believed this money was being used to buy political loyalties in the region in countries like Cuba and Bolivia, both socialist/communist states.(Coronel 2008)

Chavez's promise to clear corruption in the country's political spectrum was disingenuous. Its collapse of democracy, and also the rise of his dictatorship, grew more and more as his time in office progressed. However, Chavez was diagnosed with cancer, and on

March 5<sup>th</sup>, 2013, he died after his battle. Chavez's successor, Nicolas Maduro, was now assigned as acting president until the presidential election on April 14, 2013. Maduro won the election, and the corruption continues until today.

Maduro has not only faced an allegation of working with the Hezbollah, but he has faced numerous allegations of corruption. His highlights include the two nephews of Maduro's wife have been involved in illegal activities such as drug trafficking, with some of their funds allegedly funding Maduro's campaign in 2013. Included in the drug trafficking allegations comes with how the military was actively involved with transporting cocaine to Haiti. And Venezuela's first lady was seen flying out of Bolivar International Airport transporting 800 kilograms of cocaine. The pilots were members of the presidential security and transportation unit such as Pedro Miguel Rodriguez, lieutenant colonel in the Venezuelan Air Force and military official Pablo Urbano Perez.(Yagoub 2017)

Diosdado Cabello, a member of Venezuela's National Assembly, has been considered to have a major role in corruption in the country. Cabello has been accused of being a leader of the Cartel of the Suns, an alleged government drug trafficking gang in Venezuela. In 2015, there were reports that he had been involved with drug trafficking, and figures estimated about five tons of narcotics passed through Venezuela weekly, produced by the Columbian FARC. On December 11, 2014, a witness claimed he saw Cabello specifically order departure of boats with tons of cocaine, and there is evidence that tons of money is stored for illegal business, claimed by the US Drug Enforcement Administration (DEA). (Blasco 2015)

Venezuela still remains as a threat to democracy. In 2018, the Trump Administration proposed to list Venezuela as a state sponsor of terrorism, escalating tensions between the US and Venezuela.(Hudson 2018) Still an ongoing crisis in Venezuela is the presidential election

from May 20, 2018. There have been many disputed results of the election between Juan Guaido and Maduro. Protests and foreign diplomatic pressures flow into the country, and when Maduro was sworn in for his second six-year term on January 10, 2019, the National Assembly, now led by the opposition, declared Maduro a “usurper” (take power illegally or by force).(Drafting 2019) And not only is there strong outrage against Maduro, many international organizations such as the European Union, and most Latin American Countries(Drafting 2019) and in the US, President Trump at his 2020 State of the Union he included Juan Guaido and declared him as the real president of Venezuela; the people in the room both Democratic and Republican stood together and clapped their hands showing they are standing behind Guaido.(Wyss 2020)

Maduro’s regime is not only undemocratic, it has also become a dictatorship. He was able to run over the opposition-led National Assembly and swear himself in for another six-year term. The country’s ties with terrorist groups and drug trafficking should not only scare people across the world, but it should also wake everyone up and feel blessed to live in a country like the United States where we have freedom of speech, freedom to assemble and a government that has not been ran over with tyranny. Political corruption not only helped wreck this country, but it has also made other countries unwilling to help them. Venezuela’s foreign minister in 2020 rejected a proposal announced by US Secretary of State Mike Pompeo to lift sanctions if they accept a plan for a transitional government. (Sesin 2020)

Maduro deepened his governing style ever since his predecessor died, and has gone further in ruining democracy and instead has been noticed as a dictator. Maduro has continued to rule with his family, close friends and the military as well.(Maya 2018) Thanks to Chavez, Maduro has made the depletion of checks and balances worse, and the corruption cases are at unmeasurable heights.(Maya 2018)

While the US and Venezuela go back and forth with political battles, the core issue lies within their country, and unfortunately the citizens and government of Venezuela are still unable to overthrow Maduro. Hopefully, the issue with the country's corruption will end.

## **Socialism Destroyed Venezuela**

While leftists may argue that socialism was not to blame, but the decline of oil prices and the failure of Chavez investing properly in social welfare was what caused the collapse, the collapse was ultimately caused by socialism. Prior to the Bolivarian Revolution, there may have been economic disparities, but when Chavez implemented his social welfare programs it made their situations a lot worse.

In Chavez's efforts to make Venezuela a communal state, he did it by force, and not by negotiations. Sure, 80% of the land was owned by 5% of the population, but Chavez forced land out of people's hands, and the same goes with the forced expropriations on foreign oil companies like Exxon Mobil and ConocoPhillips, and it all led to lawsuits and attacks on the Venezuelan government.

Another huge cause were Chavez's price controls. Price controlling in the long run will lead to shortages, rationing, and deterioration of product quality. The price controls not only destroyed privately owned stores, it also ruined the ability to keep up with increasing inflation, therefore resulting in foreign demand in food because food supply in Venezuela was deteriorated from an excess demand and too low of prices.

Chavez's implementation of his welfare programs and the funding he wanted to use for it was impossible. It was a fantasy that he wanted to bring to reality and now we see Venezuela as a suffering country thanks to his Bolivarian Revolution, which is also plagued with corruption. It



is worth noting that oil prices is never a good idea to rely on for consistency because it never has been; it is a worldwide capitalist market game where prices fluctuate.

Although capitalism is an economic system which can bring economic inequality, it is still considered the best system to run. Venezuela is a good example of the opposite: the country wanted economic equality, which ultimately failed and now they suffer from an undemocratic ruler, hyperinflation, malnutrition, high crime, high levels of corruption and foreign countries are afraid to invest in their market.

The government is not here to provide everything, a government is made to protect our rights and defend our nation. *“A government big enough to give you everything, can take away everything.” – Gerald Ford*

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