

VENEZUELA

MOVIMIENTOS socialismo...

"MOVIMIENTO DE TIERRA PARA LA CONSTRUCCIÓN DEL COMPLEJO INDUSTRIAL PULPACA"
ZONA INDUSTRIAL MACAPAIMA

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INGENIERO INSPECTOR: ANTONIO YABUR C.I.V. 87809

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The president's secretive fund showers billions of dollars in oil revenue on projects that cheer voters, but raise questions about where the money is going

Chavez's murky spending spree

BY BRIAN ELLSWORTH AND EYANIR CHINEA
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UNFINISHED BUSINESS: A warehouse amid cleared scrub is about all there is to show for the hundreds of millions of dollars President Hugo Chavez's secretive Fonden fund has committed to a pulp and paper factory in central Venezuela. **REUTERS/STRINGER**

The site of what may someday be Venezuela's first newsprint factory today consists of little more than a warehouse, several acres of cleared tropical savannah, and two billboards bearing pictures of President Hugo Chavez.

More than five years after Chavez first hailed state-owned Pulpa y Papel CA as a vanguard "socialist business," there is little else to show here in rural southeastern Venezuela for the more than half a billion dollars that state investment fund Fonden set aside for the project.

As with many Fonden investments, tracking the money sent to Pulpaca, as the project is known, is difficult. A Pulpaca annual report for 2011 said the project was stalled for lack of funding. A manager at the dusty gates of the compound declined to comment. So did contractors involved. Requests for interviews with the industry ministry, charged with disbursing Fonden money for such projects, went unanswered.

Fonden is the largest of a handful of secretive funds that put decisions on how to spend tens of billions of dollars in the hands of Chavez, who has vowed to turn the OPEC nation's economy into a model of oil-financed socialism. Since its founding seven years ago, Fonden has been funneling cash into hundreds of projects personally approved by Chavez but not reviewed by Congress - from swimming-pool renovations for soldiers, to purchases of Russian fighter jets, to public housing and other projects with broad popular appeal.

The fund now accounts for nearly a third of all investment in Venezuela and half of public investment, and last year received 25 percent of government revenue from the oil industry. All told, it has taken in close to \$100 billion of Venezuela's oil revenue in the past seven years.

Fonden attracts scant attention beyond policy experts and Wall Street analysts. But it is at the heart of Chavez's promise to use Venezuela's bulging oil revenue to build new industries, create jobs and diversify the econo-



REVOLUTIONARY ROAD: President Chavez touts Fonden as a means of using Venezuela's oil revenue to achieve socialist ends; critics see it as a slush fund for buying off the electorate and indulging his whims. **REUTERS/MIRAFLORES PALACE/HANDOUT**

my in the service of his self-styled revolution.

Finding out how much of that money Fonden has spent, and on what, is not easy. The most detailed descriptions usually come from Chavez himself, rattling off multimillion-dollar investments on television while chatting with workers and extolling the virtues of socialism. Fonden does not regularly release lists of projects in its portfolio.

NO ACCOUNTABILITY

Adversaries excoriate it as a piggy bank that lets Chavez arbitrarily spend billions of dollars with little more than the stroke of a pen and perhaps a celebratory Tweet, with accountability to no one. The secrecy also makes it impossible to determine what went wrong - at Fonden, or at the ministry level, or on the ground - when a project like Pulpaca stalls.

"I'm shocked that we don't know exactly what has happened to \$105 billion," said Carlos Ramos, an opposition legislator who has led a campaign to extract more information about the fund from the finance

ministry. "That is not Chavez's money. That money belongs to 29 million Venezuelans and as such the information should be available to everyone."

Critics point out that since Fonden's creation, Venezuela's economy, rather than becoming more diversified, is even more dependent on its mainstay: In the first half of this year, oil accounted for 96 percent of export earnings, compared with about 80 percent 10 years ago.

The perception of secrecy has left investors unsure how to measure Venezuela's fiscal strength. Fitch Ratings this year warned it could downgrade the country's debt, in part because of transparency concerns. Those same concerns are also helping push up borrowing costs. Despite Venezuela's ample oil wealth, yields on the country's bonds are nearly equal to those of impoverished Pakistan, and higher than war-ravaged Iraq's.

"The visible portion that we can compare in Venezuela vis-à-vis other countries has declined considerably," said Erich Arispe, director in Fitch Ratings Sovereign

VENEZUELA CHAVEZ'S MURKY SPENDING SPREE



BANG FOR BUCKS: Fighter jets like these Russian Sukhoi Su-30s are among the purchases Chavez has made through Fonden, without approval from Venezuela's Congres. **REUTERS/JORGE SILVA**

Group. "I can't rate what I can't see."

Chavez's control over the country's purse-strings - unprecedented for any Venezuelan president in more than 50 years - will be a key advantage in his bid for re-election on Oct. 7. Projects successfully executed with billions of dollars in Fonden financing - housing, hospitals and public transportation lines - have improved the lot of Venezuela's poor, many of whom are already fans of Chavez's leadership.

"It's magnificent. It means we can have access to health care, education. All of this is for the people," said Domingo Gonzalez, 58, after being treated for hypertension at a new Caracas hospital funded by Fonden. "People say Chavez is throwing the money away, but that's obviously a lie, because otherwise we wouldn't have hospitals like this one," he said at the hospital gate near the slum of Petare, where middle-class Caracas merges with a chaotic jumble of narrow winding streets and ramshackle homes.

At the same time, Chavez is under grow-

25%

Percentage of Venezuela's oil revenue last year that went to Chavez's Fonden national investment fund

ing opposition fire over abandoned or half-built projects, including some that received millions of dollars from Fonden. A fleet of modern busses for a transit project in the city of Barquisimeto, which received \$301 million from Fonden, were left sitting idle so long that vines started growing inside them.

Some information about Fonden's outlays can be found in annual reports of government ministries. The finance ministry last year released a partial list of projects, following pressure by Ramos, the opposition legislator. A link on Fonden's website

apparently dating from 2007 also provided a partial list of projects, but was taken offline in the first week of September. A cryptically worded internal Fonden document leaked to the press provides an outline of its financial investments, though it omits key details, such as losses on holdings.

Other publicly available data is provided at irregular intervals and in formats that often do not allow for comprehensive comparisons. Public officials pressed for additional information are as laconic as Chavez is loquacious. A Reuters reporter at a Fonden event who approached the finance minister - the fund's president - to ask questions was physically restrained by two security personnel.

Venezuela's public finances have never been particularly transparent, and much of the oil industry's proceeds have been squandered for more than 100 years.

Early 20th century dictator Juan Vicente Gomez passed out concessions to friends while enriching himself. The country be-

came known as “Saudi Venezuela” during the 1970s oil boom, but corrupt politicians wasted and stole much of the bounty, and Venezuela’s economy was in ruins by the 1980s, after oil prices crashed.

Chavez’s vow to direct oil revenue to the poor was music to the ears of millions and helped propel him to the presidency in a landslide election victory in 1998.

Fulfilling that promise required years of struggle for control of state oil company *Petroleos de Venezuela SA*, a tussle that would be a major factor in sparking a bungled 2002 coup. A two-month oil industry walkout meant to force Chavez from power gave him the opportunity to sack PDVSA’s opposition-linked management, as well as half the company’s staff, leaving him firmly in control of oil revenue. He also sharply raised royalties and taxes on all producers operating in Venezuela.

In 2005, as oil prices were reaching new highs, Chavez found a way to sidestep bureaucracy and speed up spending.

Rather than creating a new state agency, Chavez founded a corporation: National Development Fund Inc, universally known as Fonden. Its status as a corporation owned by the finance ministry lets it disburse billions of dollars in state money while subject to few of the reporting and disclosure requirements that apply to government entities.

Money funneled through Fonden is ultimately spent by government agencies, similar to funding from Congress. But it doesn’t require congressional approval. Instead, Fonden outlays begin with Chavez’s approval and are viewed by a board of directors made up of his closest allies.

They include Finance Minister Jorge Giordani, a septuagenarian economist considered the brains behind the country’s byzantine price and currency controls, and Oil Minister Rafael Ramirez, who is also president of PDVSA.

Industry Minister Ricardo Menendez, who oversees the Pulpaca pulp and paper project,

also has a seat on the board, as does long-time Chavez ally Vice President Elias Jaua.

It is not clear how often the group meets, and it does not publish meeting minutes.

In one of his many grand plans, Chavez has vowed to turn the geographic center of Venezuela, a sparsely populated savannah where lush vegetation grows out of reddish soil, into a vibrant “City of Aluminum.”

The flagship project for the plan is an aluminum rolling mill called *Servicios de Laminacion CA*, or Serlaca, in the town of Caicara.

The company’s most recent annual report shows Serlaca had spent at least \$312 million on the project by 2011. A subsidiary of Italian company Salico had been tasked with building equipment for the plant, according to an aluminum industry trade publication dated October 2010 posted on

Fonden at various times bought risky, high-yield securities in efforts to expand its resources while helping Chavez’s foreign allies Ecuador and Honduras.

Salico’s website. Salico did not respond to a request for comment.

By 2011, construction of the equipment had been stalled for 18 months for lack of funding, and the project had piled up debts with construction contractors, according to Serlaca’s annual report. A visit last month to the site showed only a clearing with a concrete foundation and structural skeleton for the main factory.

Two union leaders and a civil engineer interviewed at the gates of the site said the project was moving at a snail’s pace and contractors were using their own money to keep it from grinding to a halt. They said infighting between unions had killed seven workers since construction began four years ago.

Complaints from the neighboring community grew as the project remained stalled, and Caicara’s mayor accused Serlaca’s president of using company funds to advance

his political career. The industry ministry in 2011 named a committee to look into the project, but Serlaca’s president – later sacked by Chavez – blocked the group’s efforts.

In a televised broadcast in March from Havana, where he was receiving treatment for cancer, Chavez complained the project was moving too slowly and offered a plan to restart it: \$500 million from Fonden.

Serlaca’s current president did not respond to calls seeking details about the additional funding.

With cash rushing into Fonden faster than it can build new roads and factories, the fund often has billions of dollars to invest in securities.

But as the leaked internal report shows, Fonden at various times bought risky, high-yield securities in efforts to expand its resources while helping Chavez’s foreign allies. Its unusual portfolio has included bonds issued by ally Ecuador, high-yield derivative securities issued by Lehman Brothers, and Honduran bonds purchased to support then-President Manuel Zelaya.

By 2008, these investments had become problematic: Lehman went bankrupt, and Ecuador declared a partial debt default. In addition, Fonden unloaded the Honduran bonds – purchased at a concessionary rate of 0.75 percent – months after buying them because Zelaya was ousted in a military coup.

Fonden hasn’t revealed whether it lost money in these operations and if so, how much it lost. The fund sold off some of the assets and swapped the remainder for \$960 million worth of derivative securities called structured notes, according to the internal Fonden report obtained by Reuters.

But it offers no detail on the market value of those securities. The report does say that Fonden’s auditors pointed out that the fund had not adequately valued some \$1.8 billion in complex fixed-income securities. That represented close to a quarter of its liquid assets of \$7.9 billion in late 2011, according to the finance ministry’s latest annual report.

Government leaders bristle at the idea

that Fonden is Chavez's slush fund. But Fonden appears to have violated its own internal rules about which investments it does and doesn't make.

A Fonden 2007 instruction sheet for agencies seeking funding says it does not finance the purchase of buildings, vehicles or shares in companies. But by 2010, it had disbursed nearly \$700 million to buy shares in a retailer and two cement-makers - payments generated by several nationalizations ordered by Chavez. It also set aside \$46 million to buy an embassy building in Moscow, and \$19 million to buy a fleet of busses for use during the 2007 America's Cup soccer championships.

The president's office received almost \$10 million from Fonden, according to the leaked internal report. The office did not respond to requests for clarification.

Fonden also gave \$156 million to a social program called Mothers of the Barrio that provides cash stipends to mothers in extreme poverty, contradicting its stated mission to make "productive investments" that create jobs and spur development.

The national comptroller's office noted that in 2009 it detected "presumed irregularities" by Mothers of the Barrio, including payments to women who were not regis-

tered in the program and did not meet the conditions for participation. The women's ministry, which oversees the program, did not respond to requests for comment.

Fonden has also become a conduit for financing joint projects with Cuba, bankrolling at least \$6.1 billion and disbursing at least \$5.1 billion for some of the hundreds of ventures the two allies had signed as of 2010.

Fonden does not say what the projects are.

SOFTWARE TO SCRAP METAL

Press releases from bilateral meetings mention only several of the projects signed at each one, which run the gamut from a software development firm to a scrap-metal recycling operation. An agency overseeing the projects called the Cuba-Venezuela Joint Commission, which reports to the oil ministry, did not respond to requests for information.

For Pulpaca, the two billboards at the site provide details on what has been visibly completed to date: around \$43 million to clear land and build the warehouse. Its last annual report says that as of 2011, it had spent nearly \$530 million.

On a visit in August, silence hung over the compound. Trucks and bulldozers sat

idly parked in rows. There was no sign of activity, or of the football-field-size machines that will be needed to turn Caribbean pine into paper.

Even so, it continues to enjoy financial support from the government. Around the time Pulpaca said it was struggling to move forward, Congress approved an additional \$305 million for the project. That, combined with the Fonden outlays, brings total funding to \$845 million.

And that's not all. Pulpaca said in a recent presentation that it will need \$1.4 billion to complete the newsprint factory.

Additional reporting by German Dam and Maria Ramirez in Puerto Ordaz, and Gustavo Palencia in Tegucigalpa; editing by Kieran Murray and John Blanton

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