



VENEZUELA'S NATIONAL ASSEMBLY ELECTIONS

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SUMMARY

- Venezuela's opposition coalition (Mesa de la Unidad Democrática, or MUD) won a sweeping supermajority in the National Assembly Elections on December 6, 2015 – a significant development, as the opposition has been the minority since 1999. The results reflect the growing public discontent with President Nicholas Maduro's handling of the economy, growing product shortages, and increasing crime rates and insecurity.
- The results directly threaten the ruling party's position and Maduro's presidency. Investors should monitor how the military and Partido Socialista Unido de Venezuela (PSUV) factions respond to these elections, as the results may further divide an already fragmented PSUV. If the opposition's factions remain united in the legislature, they may seek to remove Maduro from power.
- The opposition continues to face challenges. Maduro and the PSUV maintain their hold on the judiciary and executive, and will likely take further measures to insulate their power before the new assembly begins its term in January. Tensions between the legislature and other government branches could lead to clashes and political showdowns. Internal divisions within the MUD may make it difficult to implement major policy reforms.
- In the short term, these tensions, coupled with broader pressures such as low oil prices and rampant inflation, will limit the government's ability to deal with Venezuela's deteriorating economy. Over the longer term, however, this victory creates a momentum that could lead to a shift in economic policies and changes to the political landscape. Investors should be prepared to weather increased political and economic uncertainty in 2016
- Since Maduro assumed the presidency after Chavez's death, Venezuela has increasingly isolated itself from the international community. Investors should continue to monitor how the government will handle its debt payments and its relations with regional and traditional allies such as Brazil and China.

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THE RESULTS AND THEIR POLITICAL SIGNIFICANCE

Venezuela's opposition coalition won a stunning two-thirds majority in Venezuela's national legislative elections on December 6 after fifteen years as the minority. The MUD secured 109 seats and the PSUV held 55 seats in the 167-seat unicameral National Assembly. The three remaining indigenous representatives are allied with the opposition, securing the necessary seats to hold a two-thirds "supermajority." Although pre-election opinion polls indicated the opposition had strong popular support, many feared government intervention — after months of questionable tactics and electoral maneuvering — would prevent an opposition victory of this magnitude.

The opposition victory has significant symbolic value, and creates an opening for a substantial shift in Venezuelan politics. At the most basic level, the results prove the opposition can win elections in Venezuela. More significantly, the results challenge President Nicholas Maduro's claims of broad popular support for the PSUV's Bolivarian revolution and reflect growing frustration with his handling of the economic crisis and high crime rates in Venezuela. The country's economy continues its downward spiral, fueled by a drop in oil prices and inflation estimates topping 180 percent. Recent IMF predictions point to a GDP decline of 10 percent in 2015 alone. Rationing and scarcity of staple foods and basic consumer goods has further fueled popular discontent. Today, only 10 percent of Venezuelans have a positive view of the country's economic situation and 67 percent think Maduro should not finish his term, according to a reputable pollster.

The scale of the opposition victory—a legislative supermajority—grants the opposition significant powers within the Venezuelan political system. Notably, if the MUD is able to maintain coalition unity and the support of other loosely allied parties, the opposition has enough votes to call for a referendum on Maduro's presidency. The two-thirds supermajority also allows the MUD to approve a vote of no confidence against the vice-president and members of Maduro's cabinet. After two such votes, the vice-president and ministers would be removed from office and the president would be forced to name replacements. The majority is also strong enough to approve and rescind enabling laws, thus eliminating a tool the Maduro government and the PSUV-led National Assembly frequently used to augment presidential power. Moreover, a supermajority gives the opposition the ability to free political prisoners (including jailed opposition leader Leopoldo Lopez), control appointments to the judiciary (including to the Supreme Court), and to recall judges (including Supreme Court justices). In the long run, the opposition's influence on judicial appointments and a growing trend of judicial defections could help rebuild the independence of the courts in Venezuela. In the short run, however, the MUD victory is likely to lead to increased political instability while leaving Venezuela's economic troubles unresolved as the country moves forward under a sharply divided government.

For now, at least, Maduro has publicly accepted the PSUV's December 6 defeat. In a televised address following the announcement of the results Sunday night, Maduro blamed the PSUV loss on the opposition's "economic war" but also called on his followers to accept the results "peacefully," stating: "We have come with our morals, our ethics, to recognize these adverse results, to accept them and to say to our Venezuela that the constitution and democracy have triumphed." Maduro gave no indication, however, that he intended to cede control: "We have lost a battle today, but the struggle to build a new society is just beginning." Maduro (and Hugo Chavez, before him) has consolidated considerable power under the presidency, and the PSUV retains control of the judiciary, military, and the national media.



Maduro stated before the election that he might turn to “governing with the people in a civil-military union,” although this seems unlikely at the moment. He will undoubtedly try to sideline the new MUD-led National Assembly as much as possible, and will continue to blame the opposition for difficult economic realities. On December 8, during his weekly program, Maduro called for the resignation of his cabinet, assured that he will replace the 12 retired judges in the Supreme Court before January, and called for an “extraordinary meeting” for December 10 with the PSUV. In spite of his defiance, the defeat increases the probability that Maduro will not finish his term in office – ousted by an MUD-led referendum or by infighting among PSUV officials looking to find someone to blame for their poor electoral showing.

While the MUD emerges from the election in a strengthened position, it too will face significant challenges. The MUD is a loose alliance of more than two dozen parties, lacking a single leader or a clear policy objective apart from the overarching desire to defeat *Chavismo*. The need for unity (required to win elections) is less pressing now that the election has ended in victory for the coalition, and individual party preferences and personal ambitions could divide the opposition coalition as it attempts to legislate. At a macro level, the group’s largest challenge stems from potential internal divisions between a faction within the opposition that advocates for faster reform and another that is content to wait for Maduro and his government to “self-destruct.” Such a division could in turn undermine the opposition’s sustained unity – necessary to drive reform in the face of the PSUV’s firm grip on the presidency and judiciary – thereby empowering the Maduro government. If the opposition can maintain a unified front, however, it could legislate a profound shift in Venezuelan policy by implementing major economic reforms.

OUTLOOK FOR 2016

Venezuela will continue to confront a challenging set of problems in 2016, including negative growth, inflation, and deteriorating government finances due to low oil prices and government mismanagement. Given the prospect of a divided government, it is unlikely that the opposition’s substantial victory will lead to an immediate shift economic policy, particularly as the Maduro government has shown no indication that it plans to change course in 2016. Weathering this increasingly unstable economic environment will remain difficult in 2016, as foreign investors will continue to struggle to expatriate dollars or operate effectively in Venezuela.

Domestic Outlook

On the economic front, 2016 is likely to be even more painful for Venezuelans with a deep recession continuing relatively unabated. The IMF predicts the economy will contract 10 percent in 2015 and 6 percent in 2016. Given the tepid outlook for oil prices and the current economic slowdown in China (which in the past has provided life-giving loans to Venezuela), Venezuela will struggle to meet its debt obligations in 2016. Although the Maduro government has publicly committed to honoring its national and international debt, there is a very real possibility that it will be forced to default on at least some of its obligations in 2016. In the last two months alone, Venezuela has paid over \$4 billion in maturing debt, and the country will have another \$10.8-12 billion come due in 2016. The Central Bank’s liquid reserves have fallen to under \$15 billion (from \$22 billion at the end of 2014). Contributing to the negative short-run outlook, neither the PSUV nor the MUD will want to take responsibility for the necessary but painful economic reforms that could restore stability and growth; and the MUD lacks a unified, comprehensive economic program to replace the vision of *Chavismo*. Moreover, the executive bears primary



responsibility for economic policy in Venezuela. As a result, the recent opposition victory is unlikely to improve Venezuela's economic outlook in the short run.

Ongoing economic troubles will likely increase domestic unrest and instability, further impeding economic output. Protests in 2014 and 2015 – at times violent – demanded lower inflation and greater security, as well as measures to reduce the scarcity of staple goods. In the absence of policy reform addressing these issues, these types of protests will continue. Thus far, anti-Maduro demonstrators and opposition protestors have faced harsh government crackdowns, including the use of military force, earning the condemnation of democratic watchdog Human Rights Watch and other international observers. Under a 2015 Defense Ministry resolution, the Venezuelan armed forces have the power to “maintain and ensure stability,” including the judicious use of firearms to control “public meetings and peaceful demonstrations.”

Aside from ongoing civil unrest, the election results are likely to increase internal divisions within PSUV. Much of the current disenchantment in Venezuela is with Maduro; Hugo Chavez is remembered more fondly. The phrase “Maduro is not Chavez,” separating Maduro from Chavez's legacy, is increasingly heard across Venezuela. There has been some speculation in the media that, if the PSUV continues to lose traction among Venezuelans, Maduro may be ousted by forces from within his own party. The dissident Marea Socialista faction left PSUV in early 2015 — charging PSUV leaders with corruption and a betrayal of *Chavista* ideals — a relatively small blow to PSUV but an indication of internal conflict. Following the legislative defeat last Sunday, larger fissures within PSUV may become more visible. Already there are signs that party leaders are banding together in several factions, in an effort to protect their own positions against future opposition victories and potential criminal charges (immunity only applies to sitting legislators).

It will be important to track how closely key PSUV figures remain linked to Maduro in the coming months. Of particular significance is Diosdado Cabello, the outgoing president of the National Assembly and the second most powerful figure within the PSUV. Cabello and Maduro are widely seen as representing separate factions within the government: Cabello, a former army lieutenant, holds more influence among the armed forces, intelligence, and national security. Although Cabello has followed the government's lead in accepting the election results, the opposition victory has deprived him of his legislative position and power base. Cabello may decide that a Venezuela without Maduro is better for PSUV and for his own position. Even if Maduro does not face internal revolt, however, his political situation is far weaker in the aftermath of the December 6 elections. There is likely to be significant short-term political instability as PSUV adjusts to the new reality.

International Outlook

In exposing the eroding popular support for *Chavismo*, the elections have also further undermined Maduro's position internationally. Since Maduro has come to power, Venezuela has increasingly isolated itself from the international community. Aside from a two week tour to engage OPEC partners on securing a more favorable price of oil – a trip with few results – Maduro has done little to improve Venezuela's international standing.

Venezuela's reliance on China for economic aid may be increasingly tenuous as it enters 2016. Over the past year, China has lent billions of dollars to Venezuela and other Latin American countries, however it



may be prove reluctant to continue this support next year amidst slowing growth at home and the current political and economic conditions in Venezuela. On December 7, China's Ministry of Foreign Trade said that the country is open to working with Venezuela, but will wait until political conditions stabilize. Indeed, China has been historically reticent to lend to countries where there is near-term political uncertainty, and appears to be unwilling to show any support for Maduro until the post-electoral political scenario becomes more clear.

While Sunday's elections were relatively smooth and Maduro has initially seemed willing to accept the overwhelming electoral defeat, his government's spotty record on human rights and democratic transparency has nevertheless hurt his credibility in the region, including with traditional regional allies. In November, more than 150 legislators from Brazil, Chile, Colombia, Costa Rica, Peru and the U.S. signed an open letter to Venezuela asking for free, transparent, and democratic elections. Similarly, Organization of American States Secretary General Luis Almagro sent a letter to the Venezuelan electoral council urging fair electoral practices.

The Maduro administration can no longer rely on support from some of its regional allies the way Chavez did. Brazil, a traditionally strong partner, is less likely to support the Maduro government under President Dilma Rouseff, who is more concerned with her political survival than maintaining strong relations with region. On November 22 conservative, pro-business Mauricio Macri won the election to be Argentina's next president and quickly demonstrated that his government would be at odds with Maduro's administration. After his victory, Macri announced his intention to seek Venezuela's suspension from the South American trade bloc Mercosur based on the Maduro administration's human rights record, though after the results of the Venezuelan election, Macri backtracked. After Maduro closed down the Colombian border in August, the relationship between neighbors remains tense. In the wake of the successful elections, international scrutiny is likely to continue, and pressure on Maduro and the PSUV could mount quickly should the government be seen as engaging in questionable political and economic tactics to maintain control of the country.

The election results were welcomed in the United States, and could serve to ease the strained relationship between the two countries. On December 7, Secretary of State John Kerry released a statement noting that the U.S. is ready to support a dialogue among all parties of the government. Relations between the two countries remain complicated despite certain diplomatic efforts led by Counselor to the U.S. Secretary of State Tom Shannon – who has engaged with Venezuela's leaders over the last year on a number of trips to Caracas and the region – and Venezuela's Charge d'Affairs to the U.S. Maximilian Arvelaiz, who has sought to improve bilateral dialogue. Recent U.S. sanctions and ongoing investigations on key officials, including arrests of the First Lady's two nephews for drug trafficking, and the defection of Venezuelan prosecutor Franklin Nieves to the United States—and his public statement that the closely followed trial and sentencing of opposition leader Leopoldo Lopez was a sham – have exacerbated the already tense bilateral relationship. Still, for its part, the U.S. shares concerns with regional leaders such as Brazil over Venezuela's economic trajectory and its implications for regional stability. Investors should continue to monitor the administration's broader regional priorities and their impact on its bilateral relationship with Venezuela.

