Venezuela's Hyperinflation is One of the Worst Cases in the World

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Introduction

In 1998, Hugo Chávez won the presidential elections in Venezuela, and he remained in power until his death in 2013. Yet, his Bolivarian revolution will continue under the rule of his successor, Nicolás Maduro until present day. According to the World Economic Outlook database (IMF) the average annual inflation rate in 2013 was 40.7 percent and it has only been going up since then. In 2018 it averaged more than 65,000 percent. And when we measure the annual change in prices at the end of each year, we found that for the same year Venezuela's inflation rate was more than 130,000 percent.

Economist Steve Hanke inserted Venezuela into the world hyper-inflation table in 2016 when it reached a monthly inflation rate of 221 percent, this implied that every 18 days the price level was doubling (Hanke and Bushnell, 2016). It is the worst case currently in the modern world, in which a country that is not under a war conflict it has been heavily affected by this economic malaise. Whenever there is hyper-inflation, people must face scarcity of goods and services, and it becomes very hard for businessmen to carry out their activities.

Scarcity of goods and services was brought about by a combination of an expansive and untamed monetary policy together with price controls across different goods, and on top of that expropriation to private investment and property that began during Chávez's term. A massive wave of Venezuelans leaving their country not just by ordinary means but also by foot and boats has been a terrible corollary of these economic policies. Yet, this state of affairs has been recently alleviated by remittances sent by émigrés living and working abroad, that only the rise of the coronavirus pandemic stopped for a while.

Level of Inflation Rate in Venezuela for the Last Decades

Inflation is defined as the increase during a period of the price level within a country or region. The price level is an index of the prices of goods and services mostly traded in that country or region. Whereas hyper-inflation is defined as an inflation rate of at least 50 percent per month (Cagan 1956). All countries and even regions within each of them experience different levels of inflation. One of the characteristics of the macroeconomics of most countries today; developed and developing; it is that inflation rates are mostly under 20 percent a year. In the historical records of the monetary economics of countries with hyper-inflation since the 1800s there has been only 57 cases of countries or regions who have experienced with it, and Venezuela it is one of the most recent entry in that record (Hanke and Bushnell, 2016).

Figure 1 plots the annual end-of-period inflation rate between 1980 and 2021 for Venezuela. The chart, also, highlights the incredible spike in 2018 when inflation rate reached more than 130,000 percent, since then it has been decreasing but it is still above 5,000 percent as of recently. For instance, the same figure also includes the annual inflation rate for Latin America and the Caribe and, even though, it reached up to 300 percent before 2000 since then it has kept well below twenty percent, yet it is basically unnoticeable from the chart.

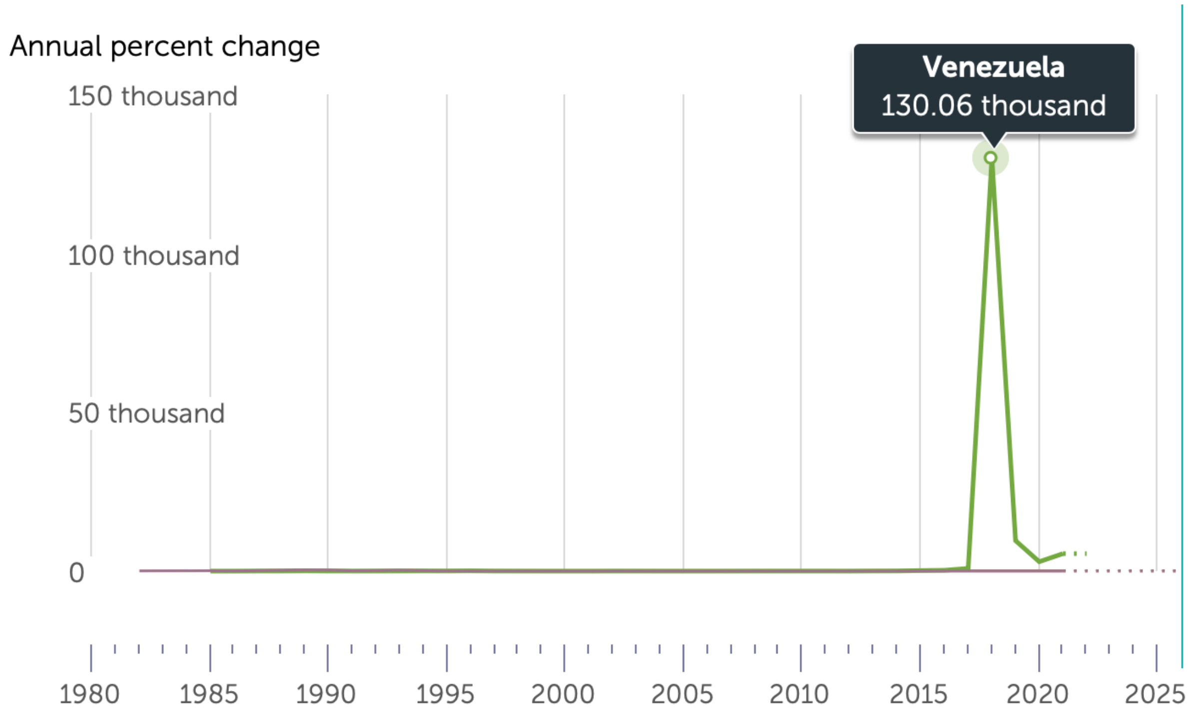

Figure 1: Annual Inflation Rate, end-of-period
Source: International Monetary Fund World Economic Database

Why Hyperinflation Happened in Venezuela and the Government's Measures to Prevent it

How does hyper-inflation is caused? Exponential increases in the price level occur when there is a lot of money bills being printed in a short period of time, while the production of goods and services maybe increasing but to a much lower rate or not increasing at all. Inflation is the case wherein money is created under a moderate rate, but still to a greater rate than that of production of goods and services. In most countries central banks hold the monopoly of currency issued. In the case of Venezuela, it is its central bank; the Banco Central de Venezuela, who holds that power. Usually in a country like Venezuela fiscal pressures are the main reason behind such a frenzy money printing.

As a matter of fact, the Banco Central de Venezuela has had to adopt different policies to try to stop or disguise this hyper-inflation without being successful so far. For instance, President Chávez implemented in January 2008 a redenominated currency the Bolívar Fuerte (strong Bolivar) was issued at a rate of 1 to 1,000 of the old Bolívar currency. Yet again in 2018 President Maduro issue another currency, called Bolívar Soberano (Sovereign Bolivar), this time to a rate of 1 to 1,000,000 old bolivares. Just as recently as March 2021 a bill of 1,000,000 Bolívares Fuertes was only worth $0.52 USD.

The continuous depreciation of the currency to fund public expenditures has led to an unstoppable inflation rated that erodes the purchasing power of the Venezuelan population and affecting more disproportionately to those of lower quintiles in the national income distribution. In early 2012 the minimum wage in Venezuela was set at $360 USD per month but by 2015 it was already $31 USD, and by the end of 2019 it became only $2 per month. Other concomitant policies such as price controls in this country and private property confiscation by the government has led to serious scarcity of many goods including basic ones such as food staples and toilet paper. Increasing devaluation to cover government expenditure created hyperinflation, then the government tried to solve these problems by placing price controls and wage increases that brought about scarcity in food supplies and other basic goods. All these was happening meanwhile there was not a single threat of domestic or external conflict in the country.

Consequences of Hyperinflation in Venezuela

In late August 2018, the Venezuelan government devaluated in 95 percent the Strong Bolivar and, it suppressed from it five zeros to introduce the new currency Sovereign Bolivar. This was a monetary change that reduced in half the purchasing power of the domestic currency. Figure 2 shows a list of staple items for consumers with its price in Strong Bolivares and its equivalent price in US dollars just prior to the devaluation that implied that Strong Bolivares became worthless. During this time in the daily market exchange customers had to make their grocery payments with stacks of or bags filled with national bills just to be able to buy a small number of items. Imagine the transaction costs for both buyers and sellers, who had to carry those bags and, also, had space to place and keep them before to take that money to the nearest bank. This situation affected businesses in such a way that they would rather close instead of opening their stores. Since relative prices provide signals to take better decisions for buyers and sellers, whenever there is high devaluation and hyper-inflation this mechanism does not work any longer, and then economic exchange collapses like in this case. Also, in Figure 2 we observe that people in Venezuela was spending millions in their national currency just to buy chicken or meat, and even just one roll of toilet paper. Imagine that¡ The figure, also shows that meanwhile in US dollars these huge quantities of domestic currency barely represented a few dollars. Moreover, the monthly wage by this time was barely getting to US 30 dollars and decreasing day after day. In fact, by the end of 2018 was less than ten dollars.

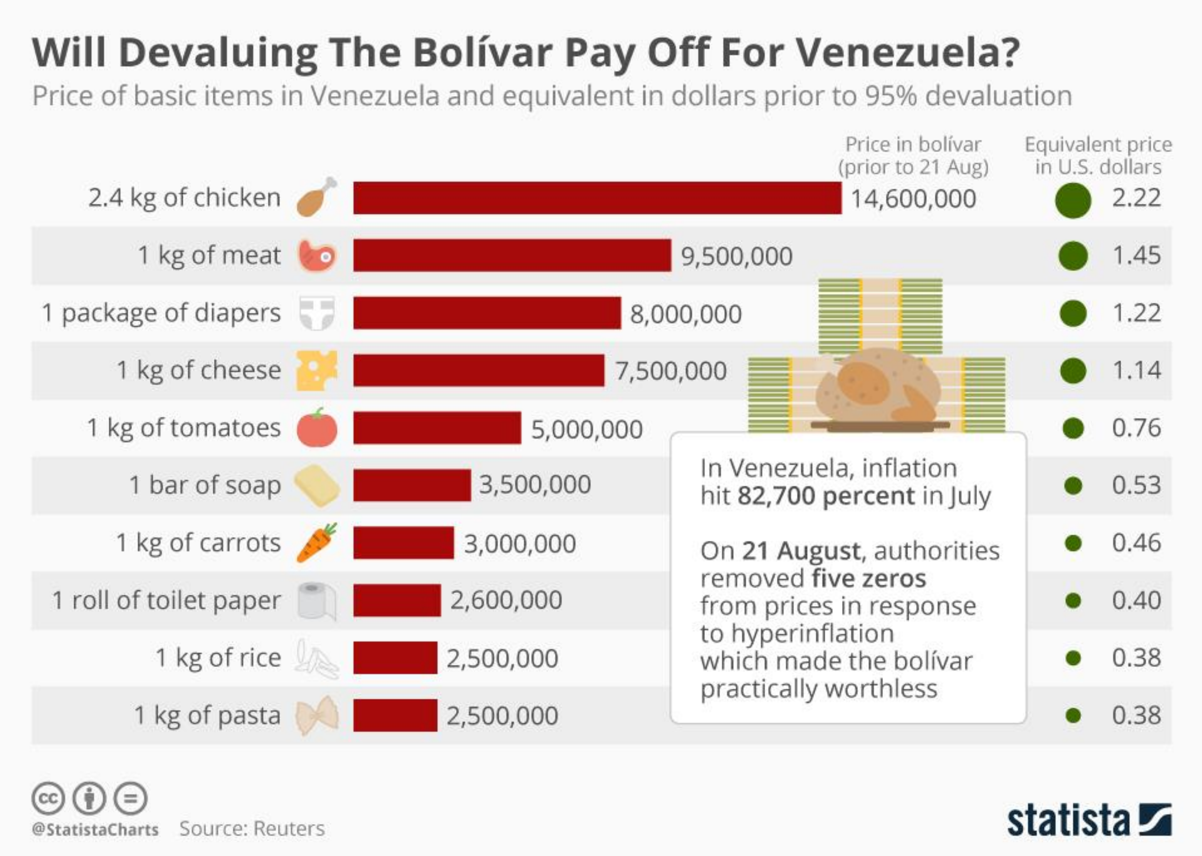

Figure 2: Bolivar's devaluation in Venezuela
Source: https://www.statista.com/chart/15186/price-of-basic-items-in-venezuela-and-equivalent-in-dollars/

Another terrible consequence of the hyper-inflation in Venezuela is the emigration of its population with a clear intention to never come back again to their beloved country, at least, not coming back to make a living there. According to a report from the United Nations High Commissioner for Refugees by December 2019 there were 4.8 millions of Venezuelans living abroad classified as refugees most of them in Latin America and the United States (UNHCR 2019). What is terrifying about the migration waves of Venezuelans across the continent is that they take high risks while doing this. For instance, poor families walk to cross borders from Venezuela through Colombia, passing through Ecuador to get to Perú and Chile. These two latter countries have been characterized by having a better demand for labor than the other countries. Families take with them their kids from all ages even pregnant women go by foot all along the highways spending nights out into the open and being exposed to all kinds of restrictions and bad conditions.

And with all the travails that Venezuelans were enduring, the coronavirus pandemic hit in 2020. First, those who were living abroad started to walk their way back to their home country. Yet again, suffering along the way all that implies to travel in such a way. Since borders were closed this time, they must pass through rivers and clandestine paths paying money to people guiding them to get to the other side each time they found a national border. On the other hand, those who were still managing to live in their home country saw how money sent by their relative abroad felt abruptly during this awful time.

Future Expectations and Implications

The social, economic and humanitarian crisis in Venezuela is profound. It is one of the worse crises faced by a country that is not under a military or civil conflict in the western hemisphere in the last forty years. The solution to such crisis will need an international coordination since the current government of President Maduro has been exerting oppression over his fellow citizens. It, also, continues holding his grip on power without any signs of being willing to adopt sounder economic policies or, at least, allowing free and transparent general elections.

International irregular groups, such as ex-members of the disarmed Colombian FARC; has found a safe haven in Venezuela due to the lack of state capacity to provide security by the government. Thus, posing higher risks to the region. It is a very delicate situation that demands that all countries who favor freedom and democracy help Venezuelans to solve this crisis for the sake of regional peace.

A regime that continuously oppresses its people, as it has been reported by protesters via their cellphones, violating their basic human rights and implementing public policies inspired in socialists' ideas that have been proved wrong over and over has left no solution to their citizens. Chavez's regime fare better than Maduro's just because of the commodity boom experienced during his term. But the wrong ideas and public policies were already taken place while Chavez was in power, Maduro just continued doing this, yet without the huge amount of money provided by the oil exportations of one the countries with the largest oil reserves in the world.

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