1.7 General Profiles of Industry in Venezuela

1.7.1 General

As discussed earlier, the Venezuelan economy depends heavily upon oil and international oil prices are a major factor for determining the country's GDP. This oil-dependent economic structure has not changed over the past decade. In fact, despite the government's efforts to foster the non-oil sector, the petroleum and natural gas sector (including petroleum refining) gained share of GDP from 22.3% in 1990 to 27.5% (preliminary) in 2000. In the non-oil sector, all industries other than service have been on the decline, down 10% between 1997 and 2000. Most non-oil industries are heavily affected by the country's oil revenues and their business cycle directly links to that of the oil sector.

The service sector in general increased share from 43% to 45% during the period, whereas other non-oil sector grew from 26% to 29%. In the non-oil sector, the manufacturing industry holds the largest share of 14% in 2000. The manufacturing industry includes the petrochemical industry and is thus affected by the oil market. Following the manufacturing sector, real estate and commerce hold 8% each. Agriculture only accounts for 5% of GDP. (Table 1.7.1)

The fast growing sector is transportation and communication, which grew 30% during the five-year period. On the other hand, the construction sector underwent ups and downs. After rapid growth between 1996 and 1997, it continued to shrink between 1997 and 2000. Finally, the public sector increased share from 35% to 40% at present.

As for employment, the farm sector accounts for around 10% and the manufacturing sector slightly below 14%. Personal and public services sectors hold the largest share of 29%, followed by commerce, restaurants and hotels (26%). Therefore, these sectors employ majority of labor force in the country (based on the preliminary figures reported by the former OCEI in 1999). Notably, the informal sector accounts for 52.4% of total employment.

1.7.2 Major industries

(1) Agriculture, forestry and fishery

Production in the primary sector, consisting of agriculture, forestry and fishery, accounted for 4.7% of the country's GDP in 1998, and its employment represented 13% of total work force. According to FAO's statistics, only 25% of cultivable land is used for agriculture, of which more than 80% is pastureland. 50% of primary production comes from cattle raising and grain production, 40% fruits, vegetables and dairy products, and 10% forestry and fishery. Overall, primary production grew at an annual average growth rate of 3.9% between 1965 and 1980 and 3.1% between 1980 and 1990.

In 1998, the country imported majority (64%) of total food consumption. As for grain and rice, local production mostly meets demand since the mid-1980s. The government has been striving to revitalize the farm sector since the 1970s and implemented a variety of programs in the 1980s and 1990s: currency devaluation (1983); termination of subsidy (August 1997), fixed price policy for selected farm products (1994 and 1997); designation of primary industries for priority development (establishment of special funds for development of fishery, forestry, maize, palm oil, and sugar in 1998; introduction of protective tariff for farm products; and promotion of farmland development in semi-urban areas.

(2) Non-oil mining

1) Iron ore mining and steel making

Venezuela is endowed with metallic resources. Iron ore reserves are estimated at 1.8 billion tons as of 1998. Iron ore mining and steel making operations was managed by a state enterprise under CVG, and 70% of their share was sold to private investors in 1998. In 1998, the enterprise reported loss of $230 million for fiscal 1998 and launched layoff of 2,000 workers. The government is reportedly considering sales of the remaining 30% share for full privatization. In 1999, the government announced "Buy Venezuelan" policy in an attempt to revitalize the sector.

2) Aluminum

The country has bauxite reserves of estimated 520 million tons. The aluminum industry emerged in the 1960s and four companies under CVG are exclusively operating key processes of aluminum production, as follows:

VENALUM:	Smelting
ALCASA:	Ingot production and rolling
CARBONORCA:	Production of carbon electrodes
BAUXILUM:	Bauxite production

However, the entire aluminum production complex is heavily indebted; the total debt is estimated at $1,250 million. On the other hand, production grew in seven consecutive years and dropped 586,000 tons in 1998. As the previous administration failed to decide on much-expected privatization and the debt issue will become a major obstacle to future privatization.

3) Coal mining

Coal resources in the country are deposited in Guasare, Suria, with estimated reserves exceeding 10 billion tons. They are exploited by a joint venture formed by CARBOZULIA (subsidiary of PDVSA) and a foreign private company since 1985. The long-term energy supply plan envisages annual production of 19.5 million tons in 2003.

(3) Oil and gas

The oil industry is undoubtedly a dominant economic base of the country and contributes 80% of government revenues. Crude oil is mainly produced in Maracaobo, Apure-Barinas and eastern part.

Crude production reached its peak level of 3.7 million barrels in 1970 and then dropped to 1,550,000 barrels in 1985. It gradually picked up and reached 2,260,000 barrels in 1990 when oil prices skyrocketed due to Iraq's invasion of Kuwait (which exceeded the OPEC production quota of 2 million barrels). Production further increased in the 1990s, 2.9 million barrels in 1996 and 3.2 million barrels in 1997. In 1998, the government announced a plan to produce 7 million barrels in 2007 and production was boosted to 3.9 million barrels. Then, the new administration decided on production cutbacks and the current production level appears to be 3 million barrels or lower.

The country's export revenue trends from crude oil and petroleum products are as follows:

1984	$14.7 billion

1985	$12.9 billion
1986	$7.6 billion

Crude oil prices collapsed to $12.8/BBL and then rose maintained high levels up to 1990.

1990	$13,912 million
1991 and 1992	Revenues declined
1993	$11,786 million (followed by continuous price hikes)
1995	$14,442 million
1996	$23.4 billion
1997	Down to $18,448 million (average crude price of $20.4/bbl)
1998	Price collapse due to the Asian economic crisis in late 1997 and oil supply glut; the crude price in February 1998 dropped to $11.1/bbl, the lowest level in the past nine years; production boosted to 3.9 million barrels under the plan to double production to 7 million barrels.
1999	Colnel Ugos Chabes??? was elected to president at the December 1998 general election and the Minister of Energy and Mining directed reduction of crude oil production.
July 1999	Crude price rose to $16.7

Crude oil prices in 2000 remained at around $30 per barrel, far exceeding the target price zone of $22 - $29 agreed by OPEC. A major factor for the high price level is the U.S., which crude oil and petroleum product inventories fell to the lowest level in the past four years and refineries are operated at 97% of capacity. Thus, crude oil prices are expected to maintain high levels for a while.

The oil industry has been making continuous investment, a total of $16 billion in the past five years and $5 billion in 2999 alone. Of total, more than 60% of capital investment was ordered locally. One of new projects is the development of heavy oil reserves in the Orinoco area, which is expected to attract foreign capital. At present, four development projects are underway and a total of $13 billion will reportedly be invested. Under the plan, production of medium synthetic crude will start at a rate of 600,000 barrels per day in 2004.

2) Natural gas

Venezuela has proven natural gas reserves of 143 trillion square feet and estimated reserves of 458 trillion square feet, the fifth largest in the world. 90% of natural gas is produced as associate gas from oil wells, and the remaining 10% is available from gas wells in the central area. Gas production in 1998 totaled 5,270 million square feet. Gas pipelines, completed in 1990, connect gas wells in the Paria peninsula and industrial areas in the central and western parts (supply capacity of 22 million cubic feet/day).

The government encourages use of natural gas as part of its efforts to shift the oil-dependent economy. It promotes private investment in industries using methane and ethane gases, transportation fuel, gas transportation and sales under the presidential decree issued in January 1999. In August 1999, it amended the Hydrocarbon Act to encourage use of natural gas.

(4) Chemical and petrochemical industries

1) Petrochemical and other chemical industries

The petrochemical industry in Venezuela has been growing since 1978, as led by PEQUIVEN under PDVSA. At present, PEQUIVEN operates three complexes (El Tablazo, Moron and Jose). In 1984, capacity was tripled. In 1998, a bill to privatize the enterprise up to 49% of total share was approved by parliament, but the new administration rethinks the privatization plan. At the same time, the government is planning to expand operation. Nevertheless, the entire chemical and petrochemical industries have been declining since 1997, as show below, probably due to the decline in the domestic market and deterioration of international competitiveness.

	1997	1998	1999	2000
Number of enterprises	395	365	358	355
Employment	30500	21350	19200	18970
Operating rate (%)				
Basic chemical	80	80	80	82
Intermediate product	55	50	50	56
Sales ($ million)	3140	3011	2619	2776

Source: JICA Study Team

The petrochemical conference held by Venezuelan and U.S. chambers of industry and commerce has concluded that the industry's trouble originates from foreign exchange (overvaluation of Bolivar), high interest rates, decline in domestic demand,

and ineffective tax returns on import duties. Also, it has been pointed out that various concerns discourage foreign investors from the country.

(5) Food industry

The industry grew 7% in 2000, but intensive competition resulted in price rise of merely 8% compared to the inflation rate of 20%. Also, unreliable public transportation service and smuggling are major concerns for the industry. In particular, high transportation costs between Colombia and Venezuela, together with high incidence of product damage, are inhibiting growth of exports to the CAN countries.

(6) IT industry

The IT industry has been growing steadily in the country. Use of the Internet expands continuously, and intranet, B2C and B2B services are increasingly proliferated. Demand for outsourcing service, such as management of Web sites, is on the rise, while customer relations management (CRM) and supply chain management systems are adopted by an increasing number of enterprises. The Ministry of Science and Technology plans to promote software and Web content development businesses in rural regions.

(7) Energy

1) Electricity

The total installed generation capacity in the country reached 20GW as of 1998. Electricity consumption per capita reached 2,800KWh, the largest in Latin America, and 90% of households are electrified.

Hydropower accounts for 75% of electricity production, including the Guri dam in Guayana and a dam on the Caroni river. Power source development has been made by the private sector, but the decrease in government revenues makes it difficult to maintain a high level of investment to meet growing demand. In particular, transmission and distribution capacities are in short supply. In 1998, the government enacted the State Power Service Act to build the basis of privatization of the electricity sector. In October the same year, the government start the privatization process by selling SENECA at $63 million. In 1999, regional distribution networks were privatized by selling the 70% share to private investors.

TABLE 1.7.1 GDP (CONSTANT PRICE)

Economic Activities	Million Bolivar							Variation Percentage				
	2000(*)	share	1999(*)	1998	1997	1996	1995	2000/99	1999/98	1998/97	1997/96	1996/95
Oil Activities	160,366	27.5%	155,066	167,490	164,247	150,139	139,418	3.4	(7.4)	2.0	9.4	7.7
Petroleum and Natural	129,818	22.2%	123,342	136,256	133,420	121,368	111,959	5.3	(9.5)	2.1	9.9	8.4
Refinery	30,548	5.2%	31,724	31,234	30,827	28,771	27,459	(3.7)	1.6	1.3	7.1	4.8
		0.0%										
Non-oil Activities	407,699	69.8%	396,905	419,533	423,284	406,046	416,494	2.7	(5.4)	(0.9)	4.2	(2.5)
Producers of Goods	155,966	26.7%	153,382	168,549	173,839	163,085	166,866	1.7	(9.0)	(3.0)	6.6	(2.3)
Agriculture	28,359	4.9%	27,748	28,356	28,186	27,526	26,995	2.2	(2.1)	0.6	2.4	2.0
Mining	5,119	0.9%	4,724	5,275	5,520	5,174	5,042	8.4	(10.4)	(4.4)	6.7	2.6
Manufacture	82,620	14.1%	79,771	87,863	93,105	89,186	94,091	3.6	(9.2)	(5.6)	4.4	(5.2)
Electricity and Water	10,933	1.9%	10,711	10,593	10,459	9,987	9,864	2.1	1.1	1.3	4.7	1.2
Construction	28,935	5.0%	30,428	36,462	36,569	31,212	30,874	(4.9)	(16.5)	(0.3)	17.2	1.1
Producers of service	255,974	43.8%	247,584	255,481	253,898	246,960	255,262	3.4	(3.1)	0.6	2.8	(3.3)
Commerce	47,088	8.1%	44,783	50,774	53,079	50,702	55,451	5.1	(11.8)	(4.3)	4.7	(8.6)
Restaurants and Hotels	14,602	2.5%	14,613	14,913	14,665	14,404	14,700	(0.1)	(2.0)	1.7	1.8	(2.0)
Transport, Storage and Communication	36,545	6.3%	33,436	32,896	31,076	28,499	28,027	9.3	1.6	5.9	9.0	1.7
Financial y Security Institutions	6,360	1.1%	6,258	7,261	7,330	7,040	8,733	1.6	(13.8)	(0.9)	4.1	(19.4)
Real estate	47,359	8.1%	46,709	47,235	46,344	45,030	44,919	1.4	(1.1)	1.9	2.9	0.2
Lental service for company	19,035	3.3%	18,779	19,686	19,777	19,215	20,086	1.4	(4.6)	(0.5)	2.9	(4.3)
Serv. Communal, Social, Person, non Lucrative service	39,137	6.7%	38,552	38,768	38,052	36,951	36,433	1.5	(0.6)	1.9	3.0	1.4
Services of the General Government	45,848	7.8%	44,454	43,948	43,575	45,119	46,913	3.1	1.2	0.9	(3.4)	(3.8)
Minus: Serv. Bank. Imputed	4,241	0.7%	4,061	4,497	4,453	3,999	5,634	4.4	(9.7)	1.0	11.4	(29.0)
SUB-TOTAL	568,065	97.3%	551,971	587,023	587,531	556,185	555,912	2.9	(6.0)	(0.1)	5.6	0.0
Plus: Import duty	16,009	2.7%	13,917	15,535	14,003	9,321	10,715	15.0	(10.4)	10.9	50.2	(13.0)
TOTAL	**584,074**	100.0%	**565,888**	**602,558**	**601,534**	**565,506**	**566,627**	**3.2**	**(6.1)**	**0.2**	**6.4**	**(0.2)**

Source : B.C.V.
Note: * Priminary figure.

1.8 Economic Development Plan

1.8.1 Economic Program 2001

The Venezuelan government announced Economic Program 2001, as continuation of Economic Program 2000. The program sets the primary objective to “achieve stable and continuous economic development” and calls for the establishment of the environment that is conducive to further stabilization of the currency, correction of high interest rates, and low inflation.

To promote economic development without inflation, the program sets forth the qualitative improvement of public expenditures as a means to induce investment by the private sector, thereby to revitalize and modernize the currently stagnant sectors. Furthermore, it emphasizes the importance of taxation from the non-oil sector to maintain a stable source of public expenditures, while relying on it as an effective means to control inflation.

Macroeconomic targets set for the year 2001 are summarized as follows.

TABLE 1.8.1 2001 MACROECONOMIC GOAL

Macroeconomic targets	2001
Real GDP growth rate(%)	4.5
Oil sector	4.1
Non-oil sector	4.7
Gross investment (net) (as percentage of GDP)	17.4
Public investment	8.0
Private investment	9.4
Government budget deficit (as percentage of GDP)	2.0
Ordinary income（MMUSD）	7,582.0
Foreign currency reserve（MMUSD）	18,136.0
Inflation rate (%)	
Spot	10.0
Average	11.1
Average exchange rate（Bs./USD）	725.0
Unemployment rate (%)	11.8
Lending rate（%）	19.0
Interest received（90 days）(%)*	10.0

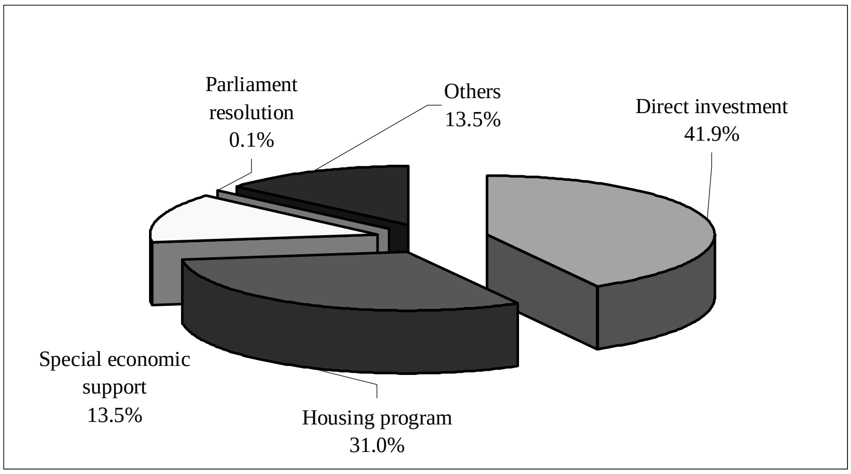
*90-day time deposit
Source: MPD

To ensure the further raise in standards of living of population, the government will allocate 58.7% of expenditures to social welfare and related items. Also, the following goals are defined:

a. To establish the basis of continuous public expenditures;
b. To increase tax revenues as a principal source of government budget;
c. To control an unstable element of government finance;
d. To reduce public debt;
e. To control money supply in accordance with demand in the production sector;
f. To lower interest rates;
g. To secure a trade surplus;
h. To establish a new financial institution;
i. To promote private investment in the private sector;
j. To modernize SMEs;
k. To develop the socioeconomic sector;
l. To promote technological upgrading and reinvestment in the agriculture and service sectors as well as in the industrial estates;
m. To diversify external trade within the framework of globalization and regional economic integration; and
n. To revitalize industry.

For FY2001, government revenues are expected to be 61.69% ordinary revenues and 38.31% special revenues. Of ordinary revenues, the oil and other mineral mining sectors account for 41.43% (assuming that the oil price is US$20.00/BBL) and IVA, corporate and personal income taxes, and iron and steel related 58.52%. As for special revenues, 57% comes from bonds, 22% FIEM (Macroeconomic Stabilization Investment Fund). Expenditures are classified into ordinary expenditures (70.4%), capital spending (15.3%) and financing (14.2%). Ordinary expenditures are divided into salaries and service provision (30.9%), general transfer (56.6%) and real estate leasing (12.0%). Capital spending consists of the following categories: infrastructure development and maintenance 41.9%, housing 30.0%, special economic support 13.5%, and others 13.6%.

FIGURE 1.8.1 PUBLIC SPENDING BY CATEGORY



Source: OCEPRE

As strategic guidance for the public spending program, the following actions are recommended:

1) To promote and stimulate technology support for small industries and cooperatives, provide assistance, and support their modernization;
2) To promote and expand priority infrastructure projects;
3) To provide support and assistance for the production sector, and implement functional recovery and upgrading plans for the existing service sector including education and transportation; and
4) To promote reforms and dynamism for the farm sector as a vital economic sector, including financial support for production, training technical support.

With these structural reforms, Economic Program 2001 envisages new deployment of economic activities with breadth and depth to accelerate the annual growth rate of investment from 16.7% in 2000 to 17.4% in 2001.

TABLE 1.8.2 INVESTMENT TRENDS AND FORECAST FOR 2001 (%)

Category	1999	2000	2001
Public investment	6.5	7.6	8.0
Government	0.8	1.0	1.0
PDVSA	4.1	4.9	5.3
Public enterprises	1.6	1.7	1.7
Private investment	8.0	9.1	9.4
Total growth rate	14.5	16.7	17.4

Source : Modelo Econométrico PECAn III

1.8.2 Industrial development plans

(1) Industrial development history

The Venezuelan economy has been relying on the oil sector since the start of commercial exploitation of petroleum resources in the 1920s. The government has been using rich oil revenues to take leadership in industrialization by providing public funds to a variety of industries in the form of subsidy or low-interest rate loans.

Venezuela enjoyed huge economic benefits from the oil booms in the late 1920s, the 1950s and the 1970s. During the first boom, the country earned revenues by granting foreign oil companies the right to explore and drill oil under the concessionary agreement. Most revenues were used for modernization of military force, normalization of government finance, and the development of government infrastructure, but little to industrialization programs.

In the 1950s, the government embarked on import substitution policy to encourage industrialization by protecting local industries. Various programs were implemented to encourage investment in local industries, while restricting imports of foreign products that compete with local ones. The government resorted to import restriction on industrial products by means of high tariff, import license and quota. In the 1960s, the government curtailed the granting of the exploration and drilling rights to foreign oil companies for the reason of resource conservation and actively promoted development of local oil industries. During the period, the center of the import substitution policy was shifted from consumer goods to intermediate goods, and metal and chemical industries emerged. Also state enterprises started oil drilling and refinery operations.

In the 1970s, crude oil prices jumped sharply as a result of the birth of OPEC and the first oil crisis, which more than compensated for the decline in oil production and brought enormous revenues to the country. In 1976, the government launched the fifth five-year development plan to transform the oil-dependent economy and promote industrialization and made aggressive investment in various industries. Also, it nationalized the oil industry and started commercial production of iron and steel and aluminum by taking advantage of rich ion ore and bauxite resources in Bolivar and hydropower. In the late 1970s, local industries were capable of producing most consumer goods for the domestic market, and infrastructure development progressed including power grids, roads and communication networks.

In the early 1980s, growth of the industrial sector slowed down due to the rise in raw material prices, the rise in wage, and the deterioration of momentum among investors. The government embarked on the sixth five-year plan, which emphasized the strengthening of competitiveness of local industries, the improvement of productivity and profitability of basic industries, including steel, aluminum and petrochemical, and the fostering of SMEs and agro-industries. In the meantime, it became apparent that state enterprises were losing money from their operations. Major factors, as pointed out, were the small domestic market, low levels of production technology, poor product quality, and the lack of management capabilities.

After 1989, the government abandoned its import substitution policy to promote liberalization of the domestic economy and trade. In 1990, the Perez administration announced the eighth five-year plan to aim at a smaller government, the economy led by private initiatives and export promotion. Under the plan, various policies and programs were established and implemented, including the liberalization of trade and foreign exchange, promotion of foreign direct investment, privatization of state enterprises, and liberalization of prices and interest rates.

During the period, Venezuela participated in regional free trade agreements, such as CAN and G-3, which expanded trade with these countries, especially with Colombia. While, the inflow of textile and apparel products from Colombia to the domestic market have considered to be one of the cause to damage SMEs in these industries, though industries processing natural resources and automakers in Venezuela have expanded sales in Colombia.

(2) Current industrial development strategy

The government's industrial development strategy sets forth objectives including country-wide re-industrialization, the development of the market environment to encourage fair competition, government support for lagging sectors, and creation of productive and continuous corporate alliances (production chain). In particular, an emphasis is placed on promotion of SMes and correction of regional disparity. According to the government's action plan for 2001, the following programs will be implemented.

a. Technical assistance from JICA: Strengthening of competitiveness of SMEs through the analysis of their current state (i.e., the present study)

b. Government procurement: The government will purchase goods and services worth $2,471 million, equivalent to 20% of its total procurement budget of $12,359 million.

c. Production chains: Development of five production chains that lead the country's industrial production activities

- Textile/apparel
- Aluminum
- Forestry, pulp and paper, graphics art
- Olefin, plastics
- Automotive

For these production chains, programs will be implemented for creation of employment opportunities, capacity expansion, revitalization of industries that face short-term difficult, industry expansion in GDP share, import reduction, and sales promotion in the domestic market.

d. Public credit and guarantee system: To facilitate commercial loans to SMEs (see 1.5).

e. Entrepreneur support program in technology and finance (Antonio Jose de Sucre, see 3.4.4)

f. Revitalization of inactive industries (companies): To bring idling industries (companies) to state control and modernize equipment or sell assets to new owners.

g. Rehabilitation and development of industrial parks: Rehabilitation of selected 10 industrial parks (see 3.4.9)

h. Export promotion: Marketing by small enterprises and organization of their efforts to develop and market new products

1.9 Small- and Medium-sized Enterprises

1.9.1 Small and Medium Manufacturing Enterprise Promotion & Development Law

The law[*] was enacted to promote small- and medium-sized manufacturing enterprises under Gazette No.5,552 dated November 12, 2001. The legislation process is summarized in Figure 1.9.1.

FIGURE 1.9.1 SME'S LAW APPROVAL DIAGRAM

MPC Drafts project and discusses with specialists and guild	→	General Law Office of the Bolivarian Republic of Venezuela Makes form and substance remarks	→	MPC Includes remarks
		Legislative National Assembly Seen and approved	←	Cabinet Approves

Deadline before November 2001

The definition of the SMMEs law was extensively discussed before its final determination. In principal, the definition is based on employment and the number of taxation units (UT – See 1.6 “Tax System” for definition) in consideration of inflation and its effects.

Classification of employment size was made in consideration of enterprises that accounted for 80% of total, under the participation of the Ministry of Production and Trade, INE (former OCEI), the central bank, and other relevant organizations. In the process, the scope of definition was narrowed down from “SMEs” to “SMMEs.” The final definition includes related industries that provide service for manufacturing industries, e.g., computer software and related industries.

Key points of the SMMEs law are summarized below.

[*] Note: Small and Medium Manufacturing Enterprise Promotion & Development Law (SMMEs law)

(1) Definition of SMMEs

Small manufacturing enterprises:	11 – 50 employees
	9,001 – 100,000 taxation units
Medium-sized manufacturing enterprises:	51 – 100 employees
	100,001 – 250,000 taxation units

It should be noted that the SMMEs law does not cover enterprises with 10 or less employees (microenterprises), while microenterprises are covered by the Microfinance Law, which was recently enacted. The Microfinance Law defines the microenterprise as a business enterprise or an association consisting of two or more persons or legal entities, which are engaged in production activities including service and have 10 or less employees, with annual sales of 9,000 or less taxation units. This definition does not overlap with that of SMMEs above. On the other hand, INE's statistics define the microenterprise as an enterprise with less than five employees and the small enterprise as an enterprise with more than five employees.

(2) Organization responsible for SMMEs promotion policy

A new organization in charge of SMMEs promotion policy, SME Development Bureau, will be established within the Ministry of Production and Comemrce. As an organization responsible for implementation of SMMEs promotion policy, the establishment of INAPYMI is mandated under the law.

1.9.2 Entrepreneurship Support

(1) Current state

Economic activities in Venezuela, except for basic industries, are concentrated in the central and northern coast area. To reduce excessive concentration, MPC has developed an industry revitalization program for other areas. The program consists of various programs including revitalization of industrial estates and entrepreneur support. MPC intends to build a supply chain under the 2001 industry revitalization program by developing new industries in lagging regions. It will also focus on the sectors that can take leadership in industrial activities.

The industry revitalization program contains the following two key projects:

a. Rehabilitation of industrial estate facilities
b. Implementation of the entrepreneur support program (Antonio Jose de Sucre Program)
   - Technical support for entrepreneurs
   - Provision of loan funds
   - Recruitment of tenant firms for industrial estates

Antonio Jose de Sucre Program (AJS Program) was started in 2000 for the purpose of creating employment opportunities and promoting industrialization with contribution to the national economy. The program was planned between the end of 1999 and January 2000 under the leadership of MPC's Vice Minister Office (Industry) and in cooperation of FONCREI, SOGAMPI and other organizations. Then it was launched in January 2001. The program is implemented for one year and will be implemented on a continuous basis. In the future, INAPYMI, as it starts up, will take leadership. At present, said program is reexamined by MPC, and it may be implemented again in 2002.

The program is planned by MPC's Vice Minister (Industry) Office an is managed by the following organizations:

a. Executive Committee: To decide financial (loan) policy for the program
b. Technical Committee: Program coordination and follow-up
c. Contest's Examining Jury: Evaluation of project contests, and announcement of results

d. Program’s National Coordinator: Promotion of local activities to achieve the project goal
e. Entrepreneur Assistance Office: Program’s advertisement and support for candidates
f. State Coordinators: State-level coordination and follow-up, promotion and information dissemination to related organizations, and communication of decision by Technical Committee
g. Regional Coordinators: Support for local implementation of programs

Actual procedures for implementation of the AJS program are summarized as follows:

a. Project promotion by State’s Coordinator and recruitment of entrepreneurs
b. Pre-registration with Entrepreneur Assistance Office
c. Technical assistance for project formulation and evaluation
d. Project proposal submission and presentation
e. Project evaluation
f. Announcement of results and loan application
g. Evaluation by the Ministry of Production and Trade after the project startup and follow-up

Note that, in the step “c,” FONCREI’s project evaluation method is used to help project formulation. As many candidates have no experience in project formulation, university professors and other professionals help develop a business plan on the basis of the evaluation method.

In the step “f,” SOGAMPI accepts a loan application and examines assets for collateral, including land, buildings and machinery that are currently owned or planned to be acquired. The entrepreneur is required to have his own funds that represent 30% of the total capital requirement. The project approved by SOGAMI will be further evaluated by BIV and FONCREI. Most projects which have reached this stage can receive loans.

In the year 2000 program, entrepreneurs to operate in the industrial estate are selected according to the following criteria:

Selection criteria

a. SMEs that meet the definition given in Gazette No.37034

b. Equity fund ratio of 30% or more
c. Use of own land for operation
d. Willingness to receive technical assistance
e. Project feasibility in the selected area

The previous provisions required the entrepreneur to operate in a designated industrial estate, provided that it is supported by necessary infrastructure. In the year 2001 program and afterwards, however, the obligation is abolished and the entrepreneur may select an area where he operates, provided that the selected area is considered by MPC according to its own evaluation criteria.

In the year 2000 program, 130 projects were chosen by the Ministry of Production and Trade, from 300 projects proposed. These projects include both existing firms and new startups and are classified according to industry, as follows:

Processing of farm products	37
Machinery and metal	16
Plastics	14
Textile	9

These projects are by no means new businesses. In the food processing sector, projects include productions of potato chips, frozen food, sausage, fruit processing, and yogurt.

Many entrepreneurs applying for or participating in the program are college graduates or students. Together with those who work for companies and intend to start their own business, they account for 70% of total, while 30% represent existing businesses that want to relocate for capacity expansion.

For the year 2001 program, PONCREI, SOGAMPI and BIV were scheduled to approve loans by mid-2001. However, no loan has been made under the year 2000 program after 34 projects were approved by SOGAMPI among 130 projects proposed to this date.

MPC plans to complete evaluation on the remaining 80 or so projects by the middle of August 2001, and at the same time, it will conduct investigation on financial institutions to analyze a cause for the situation where no loan has been extended to the selected projects.

Actual services related to implementation projects under the AJS program are provided by BANCO INDUSTRIA (loan) and MPC's Vice Minister Office (e.g., relocation, follow-up after installation, and guarantee). However, they do not agree on details of follow-up service, including support for entrepreneurs.

BANCO INDUSTRIA expects that loans are repaid and MPC hopes that entrepreneurs make success. Again, details of the loan scheme, methodology for success, and repayment conditions are not defined.

MPC realize that loans related to the AJS program are delayed because four organizations (MPC, SOGAMPI, FONCREI and BANCO INDUSTRIA) are involved in the program and apply different legal frameworks, procedures and regulations.

The year 2001 program as the second phase was started in May and June. MPC has modified the program and changed the requirements (factors) as follows.

1) To examine each entrepreneur to see if he is capable of implementing the project;
2) To check if the entrepreneur has expertise required to implement the project;
3) To check if the entrepreneur is capable of making adequate investment in the project by using his own funds;
4) To abolish the obligation to operate in any of the ten industrial estates and allow the entrepreneur to operate in an industrial area that meet specific requirements; and
5) To include expansion and revitalization of existing firms as eligible projects, in addition to entrepreneurs who start new business.

As a result, the year 2001 program reviews business plans according to the strict requirements because MPC feels that the program cannot be sustained under the previous method to encourage entrepreneurship by accepting proposals according to the less strict requirements.

To implement the year 2001 program promptly, MPC has reviewed the program and its content. As a result, it has developed guidelines by discussing strengths and weaknesses of the program and its implementation system, critical issues in an attempt to maximize effectiveness of the program through the streamlining of application procedures, target setting, and modification of basic assumptions and requirements.

This reflects the fact that many projects have been rejected in the loan application process after project formulation due to the lack of market study, the shortage of internal funds, and the lack of technical capability.

MPC has explained these problems to the Industrial Cabinet consisting of the Minister of Industry and directors general of various departments. And it was suggested that education and training for entrepreneurs and consultants as well as technical support would be required. Also, surveys were conducted to collect information on entrepreneur support programs in various countries, including their objective, effect and impact.

MPC, SOGAMPI and FONCREI discussed to identify sensible points in the program and possible corrective measures to be taken. And they agreed to take the following actions:

a. MPC studies feasible ways of education and training for entrepreneurs.

b. SOGAMPI analyzes a cause(s) for rejection of projects in loan application and studies the loan evaluation method. Also, it studies the desirable follow-up service for companies that have started projects.

c. FONCREI reviews and modifies the loan conditions contained in the Special Loan Agreement.

The sensible points recognized by MPC are summarized as follows:

a. Education and technical assistance schemes
b. Expansion of program eligibility to revitalization of existing firms, in addition to startups
c. Linkage of the entrepreneur support program with the ten industrial estates
d. Difference in legal framework among organizations involved in the program
e. Reinvestment in SOGAMPI (to relieve it from financial difficulty)

At present, MPC has started promotion of the year 2001 program. It intends to recruit entrepreneurs and consultants that are qualified for and interested in the program. It also promotes participation of universities.

In FY2001, MPC will hold a project formulation course in 5 out of 12 states, covering project evaluation, approval and loan.

1.9.3 Comparison of SME promotion policies in Colombia, Ecuador, Brazil and Mexico

(1) Colombia

In the country, the law to establish the foundation of SMS promotion policy is enacted under Decree No.590 dated on July 10, 2000. It sets forth ten objectives including integrated promotion of microenterprises and SMEs, the creation of competitiveness in the market, and the improvement of institutional conditions for entrepreneurship and business management. The institutional framework is based on the PYME Premier Council led by the Ministry of Economic Development and consisting of related ministers, together with the premier council to support microenterprises. Definitions of MEs and SMEs in Colombia are as follows:

Microenterprises:	10 or less employees, monthly gross sales measured by minimum wage level, less than 501
Small enterprises:	11-50 employees, 501 – 5001
Medium-sized enterprises:	51-200 employees, 5001 – 15000

The market access/export promotion policy is led by the Ministry of Trade, and individual programs are implemented by PROEXPORT-COLOMBIA, an organization under the ministry. The program, called "EXPOPYME," is implemented for 18 regions and specific product types.

The program receives cooperation from the Ministry of Trade, PROEXPORT, ACOPI, BANCOLDEX, associations, universities and colleges, and CONFECAMARAS. Universities and colleges provide necessary education and training on a contract basis. BANCOLDEX is responsible for the second floor finance. On the other hand, FONMIPYME provides support related to human resource and technological development. In addition, Ley 35, 1993 and Ley 550, 1999 form the basis of financial access and entrepreneur support. SME support in Colombia is characterized by the program-based approach that is implemented in cooperation of related organizations.

(2) Ecuador

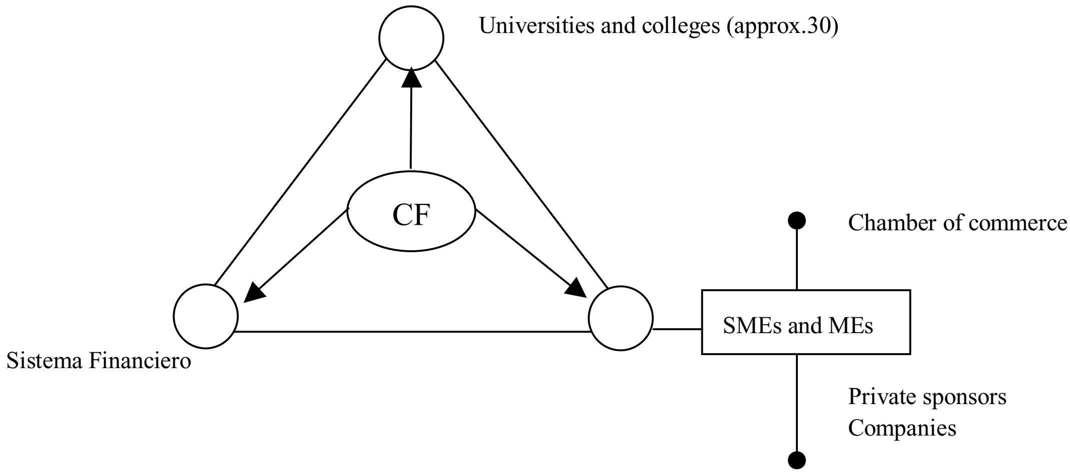
Ecuador has the SME law that was enacted in the 1970s under assistance of CEPAL. The law, however, does not meet the needs of the time as economic liberalization progresses rapidly because it relies on exemption and reduction of tariff on imported capital goods and similar measures. As the country faces political and economic stagnation, a proposal is developed to promote support programs that are based on private initiatives. Definitions of MEs and SMEs in Ecuador are as follows:

Microenterprises:	10 or less employees, working capital of $25,000 or less
Small enterprises:	49 or less employees, less than $112,000, no real estate
Medium-sized enterprises:	99 or less employees, over $112,000

Note: 97% of enterprises in the country are microenterprises.

At present, there is no institutional framework to support the program, and the government is expected to establish it as the formation of FTAA is slated for 2005. On the other hand, support for private enterprises is provided by CAPEIPI, the chamber of commerce and industry for small enterprises, and CFN, financial corporation. CAPEIPI has four exhibition facilities of varying size and holds exhibitions for local companies, CAN countries and other foreign companies at a rate of around 10 cases per year. It also has offices representing 8 product items, food, leather and shoes, graphics design, woodworking, construction materials, metal and machinery, chemical, and textile. Furthermore, it has training rooms for various skills and offers training courses that are open to the public, with certain charges. Called "Instituto de Capacitacion de la Pequena Industria de Picincha," the program offers the following courses, which duration is 20 hours on the average: 1) boiler maintenance; 2) objective-based management techniques; 3) thermodynamic cooling system; 4) human relations; 5) accounting at microenterprises; 6) collection method; 7) motivation for excellency; 8) computer basic; 9) industrial maintenance plan; 10) efficient secretarial work; 11) warehouse management; 12) industrial energy management; and 13) integrated debt management.

On the other hand, CFN, which mission is to support productivity improvement in the private sector, is now providing active support for MEs and SMEs under the current economic downturns. A general configuration of the above support system is illustrated below.



For instance, “Peograma de Capacitacion de Micro/Pequena Empresas” is implemented under the support of IDB Fund. On the other hand, various programs related to development of social infrastructure are carried out, including support for poor people or aboriginals via Fideicomiso, and support related to the rapid increase in overseas workers who work in the U.S. and Spain. CFN has training rooms for program implementation as well as seminar rooms, a folk art product display, a help disk for microenterprises, while providing market information. Overall, SME support in Ecuador focuses on person-to-person consultation and advice using private initiatives.

(3) Brazil

Brazil does not have any law concerning industrial policy/SME promotion policy. There is a private organization to provide support for SMEs, called SEBRAE, which was established under Law 9841/99. SEBRAE has office in each state. According to the government as basic policy for SME support in the country aims to promote development of SMEs under private initiatives, develop human resources by using vocational training facilities approved by the Ministry of Labor, to supplement public education under jurisdiction of the Ministry of Education, and provide assistance for individual support projects in the planning process, including joint planning efforts with SMEs and funding support. Definitions of SMEs and MEs in the country are summarized as follows:

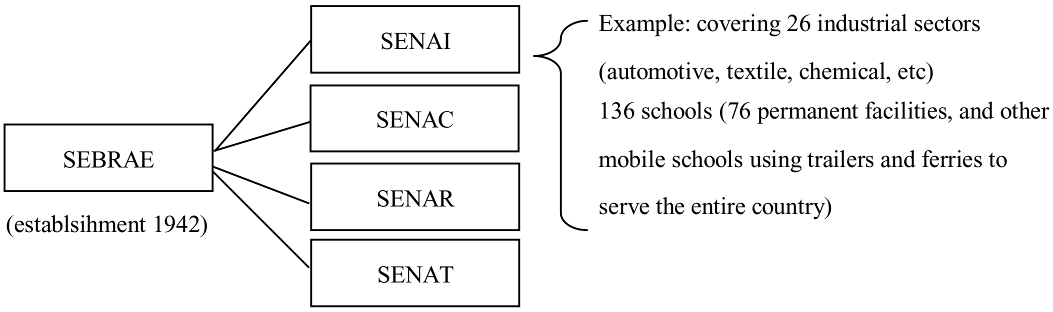
Microenterprises:	19 or less employees (9 or less for those in the commerce sector)
Small enterprises:	20-99 employees (10-49)
Medium-sized enterprises:	100-499 (50-99)

Large enterprises: 499 or over (99 or over)

SEBRAE is funded by contribution from private enterprises, equivalent to 0.3% of salary and wage. There are four vocational training institutes, which are specialized in respective industry fields, namely SENAI (industrial sector, including fishery, communication, subway, railway), SENAC (commerce), SENAR (agriculture) and SENAT (transportation). Their activities are also funded by contribution from companies in each sector, equivalent to 1.0% of salary and wage.

As for market access/project creation activities, SEBRA works together with any of the four organizations according to the field. For instance, “overseas work project” and “shopping district revitalization project” have been conceived and implemented by SEBRA.

Organization for human resource and technology development



To improve access to financial service, SEBRAE takes lead in initiating joint projects with SMEs and raises funds under support of international financial institutions (IDB) and commercial banks. As for entrepreneur support, SEBRAE uses its nationwide organization and also promotes foreign investment to foreign chambers of commerce and industry.

SME support in Brazil appears to emphasize human resource development using private initiatives (especially rural regions) and the project approach that mobilizes participation of SMEs. Also, as the country has built up broad industrial bases, especially manufacturing, within the country, high levels of education and training are required to support them.

(4) Mexico

The country does not have the law that focuses on promotion of SMEs and MEs, while related provisions are found in various laws, including the Public Administration Law (Article 34), the Federal Law (Article 3 – Promotion of Microenterprises and Folk Craft), Regulation for National Councils (Article 1, Paragraph 5, concerning SMEs and MEs), and the Rules of the Ministry of Economy (Article 16, Paragraph 5). The primary purpose of the government's SME support is to help develop lagging regions, link education and finance sectors to human resource development and financial access required by MEs and SMEs, and enable them to benefit from international trade agreements in which the country takes part. Official definitions of SMEs and MEs in the country, as specified in the gazette dated March 30, 1999, are summarized as follows.

Employment	Manufacturing	Commerce	Service
Microenterprises	0～30	0～5	0～20
Small enterprises	31～100	6～20～21～50	
Medium-sized enterprises	101～500	21～100	51～100
Large enterprises	Over 501	Over 101	Over 101

The government has recently established an institutional framework for SME policy. On March 6, 2001, Vice Minister in charge of SMEs was newly created as part of amendment to the Decree on the Establishment of the Ministry of Economy, and under the vice minister's office, five departments were established to handle various services related to SME promotion and supervise educational and other organizations that were also newly created. As for improvement of market access, the government intends to promote contribution to regional development through promotion of MEs and SMEs and devise a general scheme to reinforce and support supply, promotion, sales and distribution of exportable products. Human resource development is spearheaded by Red CETRO-CRECE under the Ministry of Economy. Improvement of financial access will be promoted by several programs including special loan programs such as "Programa nacional de Financiamiento al Microempresario." These programs are designed to upgrade informal/microenterprise sectors to formal sectors by providing financial support that is essential for many entrepreneurs.

TABLE 1.9.1 COMPARISON TABLE FOR SME POLICY IN NERALY COUNTRIES

Item	Colombia	Ecuador	Brazil	Mexico
Basic law	Ley No. 590 July 10 2000	Codified in the 1970s under assistance of CEPAL	*No specific law concerning industrial policy/SME promotion policy *SEBRAE (SME support center) established under Law 9841/99	*Public Administration Law, Article 34 *Federal Law, Article 3 – Promotion of Microenterprises and Folk Craft *Regulation for National Councils, Article 1, Paragraph 5, concerning SMEs and MEs) *Rules of the Ministry of Economy, Article 16, Paragraph 5
Objective	*Integrated promotion of microenterprises and SME *Creation of competitiveness in the market *Improvement of institutional conditions for entrepreneurship and business management (10 items in total)	However, the law does not meet the needs of the time as economic liberalization progresses rapidly because it focuses on exemption and reduction of tariff on imported capital goods. A proposal is being drafted to promote support programs that are based on private initiatives.	SME policy focuses on SME promotion under private initiatives and development of human resources by using vocational training facilities approved by the Ministry of Labor	*SME promotion support *Development of lagging regions *Linking education and finance sectors to human resource development and financial access required by MEs and SMEs *Support for MEs and SMEs to obtain benefits from international trade agreements in which the country takes part.
Definition	*Microenterprises: 10 or less employees, monthly gross sales measured by minimum wage level, less than 501 *Small enterprises: 11-50 employees, 501 – 5001 *Medium-sized enterprises: 51-200 employees, 5001 – 15000	Note: 97% of enterprises in the country are microenterprises *Microenterprises: 10 or less employees, working capital of $25,000 or less *Small enterprises: 49 or less employees, less than $112,000, no real estate *Medium-sized enterprises: 99 or less employees, over $112,000	*Microenterprises: 19 or less employees (9 or less for those in the commerce sector) *Small enterprises: 20-99 employees (10-49) *Medium-sized enterprises: 100-499 (50-99) *Large enterprises: 499 or over (99 or over)	Employment / Manufacturing / Commerce / Service Microenterprises: 0 30 / 0 5 / 0 20 Small enterprises: 31 100 / 6 20 / 21 50 Medium-sized enterprises: 101 500 / 21 100 / 51 100 Large enterprises: 501over / 101over / 101over
Institutional framework	PYME Premier Council led by the Ministry of Economic Development and consisting of related ministers Notably, Premier Council on Microenterprises	Will be revised toward the integration of FTTA	*SEBRAE is funded by contribution from private enterprises, equivalent to 0.3% of salary and wage. *Four vocational training institutes, which are specialized in respective industry fields, namely SENAI, SENAC, SENAR and SENAT, also funded by contribution from companies in each sector, equivalent to 1.0% of salary and wage.	*On March 6, 2001, Decree on the Establishment of the Ministry of Economy was amended to establish Vice Minister in charge of SMEs. *Under the vice minister's office, 5 departments were established, together with educational and other organizations.
Market access	EXPOPYME (export promotion program) (Related law: Ley 80, 1993)	CAPEIPI (chamber of small- and medium-sized enterprises) Supported by CFN (national loan coporation)	SABRE and the four training institutes work together to plan and implement projects.	*Promotion of plans related to regional development through promotion of SMEs and MEs *Development of an official scheme to support strengthening of supply, advertisement, sales and distribution of
Human resource/technology development	Establishment of FOMIPYME (technology development and modernization fund)	Conducted by CAPEIPI and CFN in cooperation of private sponsors	*Private organizations under the four institutes conduct training nationwide. *They own trucks and ships for mobile schooling.	Human resource/technology development by Red CETRO-CRECE (under the Ministry of Economy)
Financial market access	Investment and loan support (Ley 35, 1993)	Under assistance of international organizat	SEBRAE takes lead in initiating joint projects with SMEs and raises funds under support of international financial institutions (IDB) and commercial banks to engage in town development or other	Promoted by several programs including special loan programs such as "Programa nacional de Financiamiento al Microempresario.": Programa Nacional de Financiamiento al Microempresario
Entrepreneur support	Resource and taxation support (Ley 550, 1999)	Support under private initiative	SEBRAE uses its nationwide organization (Brazil Entrepreneur Support Program,	Designed to upgrade informal/microenterprise sectors through

Source: JICA Study Team

1.10 Summary of Environmental Conditions for SMEs (Major Issues)

1.10.1 Macroeconomic and Social Environments

(1) The country's GDP growth rate has been declining year after year. While the oil sector continues firm growth, the non-oil industry, particularly the manufacturing sector is staggering in recession. The national economy is still dominated by the oil sector. Inflation has been subsided after 1996, but the foreign exchange policy to keep the strong current, continued as part of price control measures, adversely affects competitiveness of domestic industries. The policy is considered to be one cause for deterioration of manufacturing industries in the country.

(2) Population has been growing at over 2% annually. During the past decade, it grew faster than GDP. Accordingly, total labor force has been growing at an annual 3.7%, but employment has been increasing at only 1.4%. The jobless rate has been on the steady rise. Working population in the agriculture sector has been on the rise, whereas that in the manufacturing sector shows continuous declines. The tertiary industry records the highest growth to account for 67% of total employment. Employment in the mining and oil sectors accounts for a meager 0.65% of total and declines further.

(3) As for the industrial structure measured by GDP share, the service sector holds the highest share of 43.8%, followed by the oil industry 27.5% and the non-oil industry 26.7%, which declines further. Income distribution is largely made through the agriculture, forestry, fishery, manufacturing and service sectors, but as the manufacturing industry continues to shrink and decreases employment, losing its position as a major income distribution mechanism.

1.10.2 Business Environment

(1) Trade

In both exports and imports, the U.S. accounts for over 50% of the country's external trade. Crude oil and petroleum products account for 75 – 85% of total exports. Colombia is the second largest trade partner in exports and imports of non-petroleum products. The country enjoys a trade surplus on account of oil exports, but its trade structure is highly skewed in terms of both commodity and country.

As economic integration and trade liberalization are expected to progress in the future, Venezuela aims to develop new exports markets in addition to Andes countries and Brazil, including the Caribbean, Central America, EU and Asia. Furthermore, other policy priorities are placed on modernization of the customs clearance system and the upgrading of the trade-related information system.

(2) Investment

During the five-year period between 1993 and 1997, foreign direct investment (FDI) represented an annual average 33% of total investment made in the country. FDI reached its peak level of 89% in 1994, which dropped sharply thereafter to 17.3% in 1997. By sector, FDI has been accounting for dominant share in the construction sector (an average 99%) as well as the transportation and communication sector (86%).

In the manufacturing sector, FDI's share is also fairly high at an average 78.8%. Thus, investment in the sector is mostly made by foreign firms, while local capital accounts for slightly above 20%. Nevertheless, the manufacturing sector has been steadily losing its share since 1993, from 56% to 35% in 1995 and 12% in 1997.

With the decline in the share of the manufacturing sector, FDI has been maintaining a very high share probably because of the high capital cost in the country.

(3) Number of enterprises

In the manufacturing sector, food processing, machinery and metal, and forest product processing industries account for a combined share of 62.4% of the total number of establishments. Within the three industries, SMEs represent 94.5% of total. They account for 92.6% of all manufacturing establishments. By region, five provinces??? in the north (Miranda, Carabobo, the federal state, Lara and Aragua) boast a combined share of 64%, while six departments (Guarico, Cojedes, Nueva Esparta, Apure, Amazonas and Delta Amacuro) have less than 1% each, with a combined total of 2.4%.

(4) Finance

Financial service for SMEs in the country has a number of problems. First of all, there is a large difference in interest rate (spread) between deposit and lending, indicating a high cost at banks. There is no commercial bank that extends long-term (over five years) loans, discouraging capital spending by the manufacturing industry. There is a long-term loan program directed to the manufacturing sector, but it is not widely used because of various problems that impede the use. Lending rates, although declined recently, are still high, at an average 24% in 2000. They are much higher for SMEs, usually over 30% and 40% in some cases.

The line of credit allocated to SMEs is very limited, not to mention troublesome application procedures (burdensome documentation requirements) and the long examination and approval process. This is because commercial banks invest most of their assets (more than 80%) in government bonds and other low-risk securities, while only 3% of total assets go to SME loans. Also, 70% of loan disbursements are concentrated in the five industrialized provinces that are all located in the north-central area.

A public loan guarantee organization for SMEs, SOGAMPI, is not large enough to provide sufficient service. It should be expanded for better service, together with the establishment of FOPYME and RGF. In addition, the capital market should be developed. The existing securities exchange in Caracas does not function fully and cannot serve as a vehicle to promote venture capital.

(5) Taxation

There is no taxation system covering SMEs. The reimbursement system for IVA and import duties for export promotion is improving by speeding up the procedures. Local tax incentives should preferably be offered to promote local industrialization. At present local taxes vary in type and rate among provinces and municipalities.

1.10.3 Industry Profiles

(1) Production trend by sector

In terms of GDP share in 1999, the oil sector surpassed the non-oil industry and recorded the second largest share next to the service sector. In 2000, the service sector accounted for 44% of GDP, the oil industry 28% and the non-oil industry 27%. During the past five years, the annual average growth rate of GDP was the oil industry 2.84%, agriculture 1.0%, and service 0.06%, whereas the manufacturing industry –2.57%. The non-oil sector recorded negative growth of 1.34% to indicate the continued tendency to increase presence of the oil sector. In the non-oil sector, food processing, information, forestry and fishery industries have been steadily growing.