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Balancing Centralization, Diversification, & Sustainability: Venezuela's Economic Crisis & International Cooperation

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Abstract: Venezuela's economic crisis, characterized by hyperinflation, is due to its over-reliance on oil exports which has led to a lack of diversification in the economy. This made the country one of the most vulnerable to external shocks due to the fluctuations in global oil prices. The absence of variety has impacted creativity and business creation significantly, resulting in insufficient investment in different industries and a failure to cultivate a more varied economy. The nation's infrastructure has also been impacted, and it is experiencing frequent power cuts, a lack of water, and an ineffective healthcare system. Thus, it is suggested that Venezuela should decentralize and focus on developing industries like agriculture, manufacturing, and renewable energy to recover its economy from the crisis. Collaboration from the IMF and World Bank, along with partnerships among nearby countries, is essential for economic stabilization. A plan that includes decentralization, diversification, and international collaboration is the most promising approach for resolving Venezuela's economic crisis and promoting lasting stability.

Keywords: Centralization, diversification, sustainability.

1. Introduction

Venezuela's oil boom began in the 1920s, and by the 1970s, the country had become one of the wealthiest in Latin America. The discovery of oil in the 1920s transformed Venezuela into a major oil, especially petroleum, exporter. By the mid-20th century, the country was one of the most developed in Latin America, field by its rich oil reserves. However, this wealth was unevenly distributed given that the oil sector largely drove the country's economic growth. Due to the collapse of oil prices in 2014, Venezuela suffered from a severe economic crisis, with inflation soaring to over 100% and GDP contracting by over 30%. Today, Venezuela is facing hyperinflation, a collapse in public services, a mass migration crisis, and a widespread poverty rate of 52%. The country's oil-based economy has proven unsustainable, leaving Venezuela unable to stabilize without significant reforms. This essay will examine the role of centralization in Venezuela's economic collapse, the urgent need for diversification, and how international cooperation could help guide the country toward a more sustainable and developed economy.

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2. Literature Review

Venezuela's economic crisis is a multifaceted issue, rooted in its concentrated dependency on oil to sustain its economy. Poor handling of oil revenue has played a key role in causing the crisis. Instead of spreading out the economy, the government has heavily depended on oil revenues, making the country susceptible to shifts in global oil prices. This has caused a decrease in funding for other areas, hindering progress and financial expansion. Moreover, the dominance of key industries like agriculture and manufacturing has impeded competition and innovation, leading to a failing economy. The lack of diversity in the economy has also led to increased dependence on imports, worsening the crisis even more. Scholars have identified these problems as important issues, emphasizing the importance of economic diversification and responsible administration of oil funds to rejuvenate the Venezuelan economy.

According to Harvard expert Ricardo Hausmann, Venezuela's economic crisis is said to be the largest economic collapse in human history that didn't involve war or state collapse. There has been a substantial decrease in the country's GDP, with certain projections indicating a drop of more than 50% [1]. This decline is double the size of the Great Depression in the United States, highlighting the seriousness of the crisis. The severe economic downturn has caused a large number of Venezuelans to leave the country, with approximately 10% of the population seeking improved living standards elsewhere [2]. This is all due to the inappropriate kind of macroeconomic policy used by presidents Hugo Chavez (1999-2013) and Nicolas Maduro (2013-present). Despite experiencing an economic upturn with the increased prices of natural resources like oil and gas, Venezuela's government did not reduce spending or boost savings. Instead of following in the footsteps of countries like Norway and Saudi Arabia by saving money during good times, Venezuela's government spent more than it earned while the economy was thriving [3]. Government expenditures exceeded revenues generated from taxes and other sources by a significant margin. Thus, leading to a shrinking economy within the country of Venezuela. Additionally, as stated in Francisco Rodriguez's report "Cooperative Responses to Venezuela's Crisis" (2024), the economic crisis in Venezuela necessitates a multifaceted strategy that includes collaboration from different parties. The report emphasizes the importance of a holistic approach that tackles the issues of the crisis, such as the weakening of the oil sector, insufficient institutional structures, and limited economic variety [4]. This shows that global collaboration, such as relaxing sanctions, can offer financial aid and promote structural changes. However, Venezuela's sustainability has been severely affected by the economic crisis in the country. The country experienced a major decrease in food security, as numerous Venezuelans faced challenges in obtaining healthy food. To begin with, the economic downturn has resulted in scarcities of essential products like food and medication. In addition, the country's hyperinflation also caused difficulties for locals in purchasing food, resulting in malnutrition. Also, the crisis had a notable environmental influence, as Venezuela's main industry was a significant producer of greenhouse gas emissions and this has caused severe repercussions for both the nation's environment and its population. The oil industry, vital to Venezuela's economy, plays a significant role in the country's environmental decline, resulting in negative impacts on the health of local communities.

3. Analysis and Discussion

3.1. The Role of Centralization in Venezuela's Economic Collapse

The Venezuelan government's centralized policies have led to the weakening of democratic protections and overall incompetence, ultimately contributing to the economic collapse of the nation. The consolidation of power has eroded the democratic processes that previously enabled checks and balances, resulting in a system that does not tolerate disapproval and diminishes the rule of law. With

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the government gaining more control over the media and public discussions, the information flow is limited, hindering citizens from making well-informed choices and overseeing their leaders. As a result, the US government, had a devastating effect on the country's economy, leading to a decline in oil production and a subsequent economic collapse [5].

Figure 1 indicates that Venezuela's economy went through a sharp decrease between 2014 and 2020. Their actual gross domestic product (GDP) decreased by around 5% in 2014 and continued to decrease annually, hitting a bottom of -30% in 2020. Therefore, representing the dangers of an intensely centralized economy that relies on a single source of revenue. Moreover, the volatility of Venezuela's GDP can be seen due to an intense fluctuation, which further represents the risk of a lack of diversification within the economy. Therefore, the Venezuelan government should aim to promote the growth of small businesses within the country.

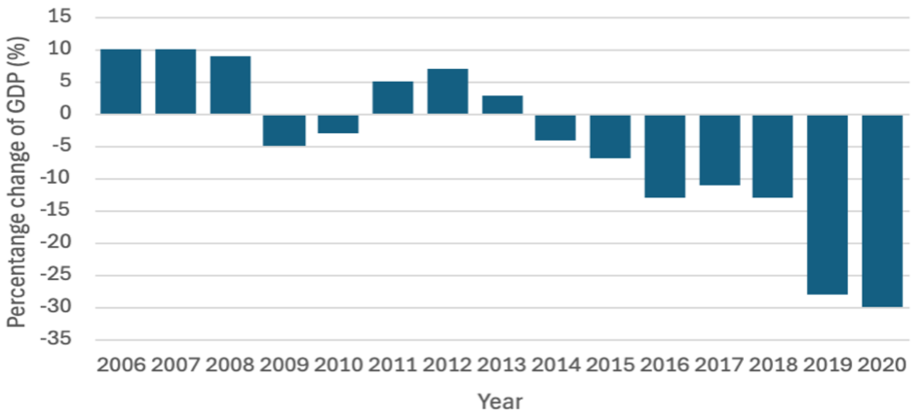

Figure 1: Annual percentage change of Venezuela's GDP (Data from IMF).

Figure 2 illustrates the crude oil production and exports in Venezuela from 1980 to 2017. There is a consistent decrease in production and exports, which worsened significantly after 1999 when Hugo Chávez assumed presidency and even more so after 2013 when Nicolás Maduro took office. This indicates that the economic crisis in Venezuela has had a notable effect on its oil sector [6]. The drop in production and exports may have played a role in the economic difficulties in Venezuela, as oil is a primary source of revenue for the nation, suggesting the role of centralization on the collapse of their economy. Finally, the concentration of power in the oil industry also hindered private investment in other sectors, leading to almost no possibility of diversification. Venezuela will have a hard time recovering economically if the economy is not decentralized and private businesses are not allowed to thrive.

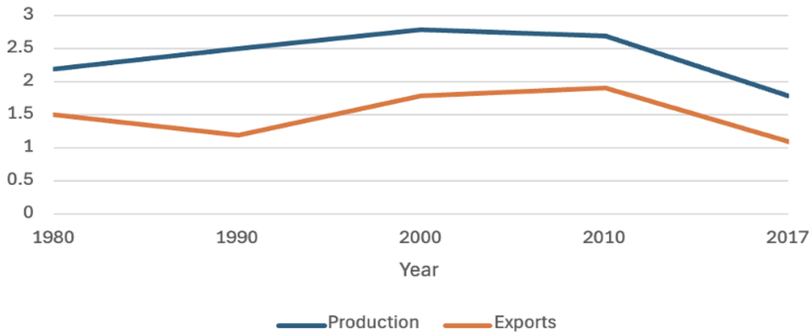

Figure 2: Venezuelan crude oil production and export (Data from OPEC).

3.2. The Need for Economic Diversification

Venezuela's heavy dependence on oil has made it particularly vulnerable to shifts in the global market. Despite having ample natural resources and potential in sectors like agriculture, tourism, and manufacturing, Venezuela has failed to make significant attempts to diversify its economy. The country's lack of economic variety left it susceptible to oil price volatility, and without sufficient oil revenue, the nation had no other industries to rely on. Norway, previously resembling Venezuela, offers a striking difference. Similar to Venezuela, Norway also has substantial oil reserves; however, Norway has actively worked to diversify its economy unlike Venezuela. Norway has made significant investments in various sectors, including fishing, forestry, and technology, and has set up a sovereign wealth fund to oversee its oil earnings. This diversification has allowed Norway to weather fluctuations in oil prices and maintain a stable economy. Thus, leading to a mixed global asset, preventing the economy from suffering from severe impacts during the fluctuations of oil prices [7]. In spite of being a significant oil exporter, Norway's varied strategy has led to continuous economic stability, as seen in its resilience to fluctuating oil market conditions.

Figure 3 demonstrates that a country with a more varied economy can boost its average GDP. During the time when Norway's economy was heavily reliant on oil, the percentage of GDP reached its highest point at 10%, while the current account balance increased to 30% by the year 2022. Therefore, proposing a more varied economy can boost a country's average GDP.

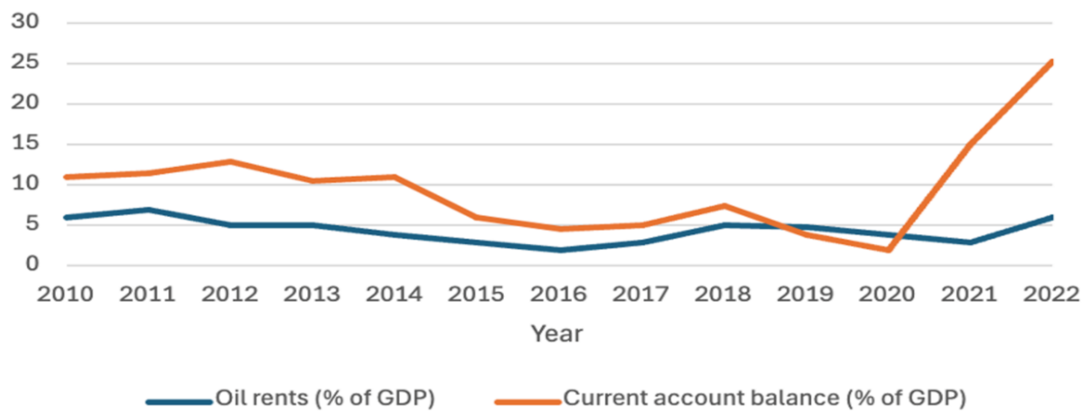

Figure 3: Oil rents and current account balance in Norway economy (2000-2022) (% of GDP) (Data from The World Bank).

In Venezuela, the oil revenues peaked in 2011 and have been consistently declining ever since. Oil revenues accounted for approximately 11% of the GDP in both 2010 and 2014 (shown in Figure 4). This demonstrates the reduced dependence on oil income in Venezuela's economy, probably as a result of a mix of factors like declining oil output and a move towards alternative economic industries. This tendency may indicate attempts to vary the economy and diminish reliance on oil, yet it also presents obstacles to the Venezuelan government in handling its finances and tackling its economic issues.

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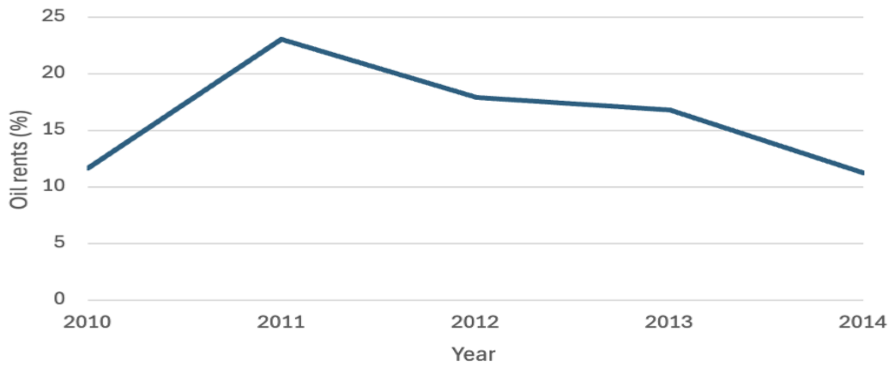

Figure 4: Oil rents (% of GDP) in Venezuela (Data from The World Bank).

Countries promote sustainable economic growth by reducing reliance on a single industry or sector through economic diversification. This is essentially crucial for countries such as Venezuela given their over dependence on natural resources to promote economic growth. For example, Venezuela could foreign directly invest in infrastructures and seek inspiration from other countries [8]. By doing so, Venezuela has the potential to draw foreign investment to the country, resulting in a stronger flow of income and better economic conditions.

3.3. International Cooperation for Sustainable Development

Venezuela's ability to overcome its current economic and political crisis relies heavily on international collaboration, as it offers a route for the country's recovery. Even though economic sanctions have definitely added to the struggles experienced by Venezuelans, they also offer a special chance to begin reforms in politics and economics. These sanctions can be used by the global community to promote positive changes in the nation. Tying the removal of sanctions to the Venezuelan government's adoption of significant reforms could help improve transparency in governance, crucial for rebuilding trust with local and global partners. Furthermore, decentralization reforms have the potential to strengthen local governments and communities, promoting a more inclusive political atmosphere. Diversifying the economy is also crucial for reducing Venezuela's dependence on oil exports and building a stronger economy. By working together internationally, Venezuela can be directed towards a future that is richer and more secure.

Economic support from international organizations like the International Monetary Fund (IMF) and the World Bank is essential for nations encountering financial difficulties, as it offers the necessary funds to stabilize the economy and enforce essential reforms. The IMF is instrumental in assisting countries in managing inflation and stabilizing their currency through providing financial support and offering guidance on policies. This assistance can aid in rebuilding trust in the economy, drawing in international investments, and establishing a more secure financial atmosphere. Conversely, the World Bank concentrates on sustainable growth by implementing long-term development projects. It offers financing and knowledge for infrastructure initiatives like highways, harbors, and communication networks, vital for economic advancement. Furthermore, the World Bank assists in developing skills in important fields such as farming and sustainable energy, allowing nations to expand their economies and decrease reliance on unstable industries. Combined, these establishments provide extensive assistance to encourage economic stability and advancement.

Moreover, nearby Latin American nations have a strong interest in Venezuela's recovery because of the significant burden the mass migration crisis has placed on countries such as Colombia, Brazil, and others in the area. The arrival of Venezuelan migrants has strained resources and services, leading to social and economic challenges that these countries are keen to tackle. In order to reduce these

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tensions and support regional stability, there is a significant push to improve regional trade agreements and establish investment partnerships. Cooperative initiatives like these could lead to increased economic unity, promoting growth and stability throughout Latin America. By collaborating, these nations can develop a stronger and more interconnected economy within the region, which will be advantageous for everyone.

Additionally, the Europe commission aids the improvement of Venezuela's economic growth. In 2024, The EU has earmarked approximately €50 million in humanitarian assistance to address the most pressing needs of Venezuelans. The funding emphasizes providing health and nutrition, protection, education, food assistance, shelter, and legal aid, among other areas of intervention, highlighting the significance of global collaborations [9].

Furthermore, World Vision has been actively addressing the Venezuela crisis through their program since 2019. From 2019 to March 2024, over 2.1 million people were impacted by initiatives in Venezuela aimed at child protection, education, food security, clean water access, sanitation and hygiene, and livelihoods [10]. This can effectively aid the local Venezuelans by improving their quality of life.

4. Conclusion

To address Venezuela's economic crisis, a multifaceted approach is needed. Decreasing the concentration of the oil sector is necessary, with a focus on prioritizing economic diversification for a more robust and sustainable economy. Global collaboration, which may involve lifting sanctions, has the potential to aid in these initiatives by offering financial aid and promoting structural changes. Furthermore, policy makers can encourage involvement from the private sector as they support the development of small businesses. These efforts not only boost economic activity but also result in a higher tax revenue for the government. This increased income can boost economic development in the country, ultimately lowering the poverty level in the area. Additionally, the Venezuelan government should implement policies that support the growth of smaller businesses, leading to higher economic activity and more tax revenue for the government. As a result of implementing these countermeasures, Venezuela can strive to attain a steadier and enduring economy, reducing its reliance on the oil industry, and enhancing the general welfare of its population, improving their standards of living.

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