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THE CENTER FOR PREVENTIVE ACTION

Living with Hugo

U.S. Policy Toward Hugo Chávez's
Venezuela

Richard Lapper

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FOREWORD

Hugo Chávez poses a challenge to U.S. interests in the Americas. Just how much of a challenge, though, is a matter of disagreement among experts. With Venezuelan oil revenues soaring and U.S. influence damaged by Iraq and inequalities in the region, Chávez has successfully managed to broaden and deepen his own influence and appeal while serving as an active spoiler for the United States. Not surprisingly, this situation has spurred a host of reactions in the U.S. government and beyond regarding the seriousness of the problem and what to do.

Living with Hugo: U.S. Policy Toward Hugo Chávez's Venezuela, sponsored by the Council's Center for Preventive Action, proposes a strategic framework for U.S. policy toward Venezuela that in the long term is more likely to dilute Chávez's appeal and power than an approach based on direct confrontation. Richard Lapper argues that the aim is not to exaggerate the threat and recommends a policy in which the United States makes clear its willingness to cooperate with Caracas on pragmatic issues of mutual interest (despite Chávez's overblown rhetoric), while at the same time seeking to develop an understanding with select Latin American leaders on how to respond if Chávez crosses certain red lines in his foreign and domestic policies. As such, this report makes a practical and much-needed contribution to a debate that is sure to grow more heated and important with time.

Richard N. Haass
President
Council on Foreign Relations
November 2006

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Richard Lapper

VENEZUELA



Source: www.nationalgeographic.com/xpeditions/atlas/index.html?Parent=sameri&Rootmap=venezu.

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ACRONYMS

AD	Democratic Action Party
ALBA	Bolivarian Alternative for the Americas
COPEI	Political Electoral Independent Organization Committee
ECLAC	United Nations Economic Commission on Latin America and the Caribbean
FARC	Revolutionary Armed Forces of Colombia
FONDESPA	Fund for Social and Economic Development
FTAA	Free Trade Agreement of the Americas
GAO	Government Accountability Office
GDP	gross domestic product
IRI	International Republican Institute
Mercosur	Common Market of the South
NDI	National Democratic Institute
OAS	Organization of American States
OPEC	Organization of the Petroleum Exporting Countries
PDVSA	Venezuela Petroleum
USAID	U.S. Agency for International Development

COUNCIL SPECIAL REPORT

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INTRODUCTION

The popularity of the new political and economic model being developed in Venezuela has been a consistent source of aggravation for the U.S. government. Since first winning the presidency in December 1998, Hugo Chávez has been able through repeated electoral victories and radical constitutional reform to dominate Venezuela's government and public institutions. Undaunted by stiff U.S. opposition, President Chávez has launched what he calls a Bolivarian revolution, named after Simón Bolívar, a nineteenth-century leader of Latin America's independence wars. Chávez has reasserted the role of the state in the Venezuelan economy and developed extensive social programs to advance an anti-U.S., anti-capitalist crusade. New or newly reinvigorated alliances with established U.S. adversaries have helped internationalize Chávez's aims. Most alarming to those concerned with the health of Venezuelan democracy, Chávez and his allies have concentrated political power in the hands of the executive, curtailed the independence of the judiciary, shown limited tolerance for domestic critics, and openly intervened in the electoral politics of neighboring states.

Thus far, American policymakers have been unable to influence the Chávez government. U.S. credibility within multilateral forums, and throughout Latin America, has been limited by the war in Iraq and the perceived failure of the pro-market reforms that it championed in the 1990s. By contrast, Chávez's political stock in the region has risen, partly due to his willingness to spend the fruits of a very significant boom in oil revenues on anti-poverty, health, and development initiatives. U.S.-Venezuela relations were also seriously damaged by suspicions that Washington was involved in a brief military coup against President Chávez in 2002.

Yet, despite Chávez's tendency to publicly insult American leaders and whip up anti-American sentiment, the United States and Venezuela remain mutually dependent. Chávez relies on U.S. oil demand to sustain the Venezuelan economy; roughly 60 percent of Venezuelan oil exports are destined for the United States. Threats by Caracas to divert energy exports to China are not credible in the short term, given the tremendous infrastructure and transportation costs such a shift would involve.

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At the same time, Argentina, Brazil, and Mexico act as important counterweights to Venezuelan-style populism, and the defeat of Caracas-backed Ollanta Humala in the 2006 Peruvian presidential election highlighted the limits of Chávez's sway in Latin America. Venezuela's recent failure to win a nonpermanent seat on the UN Security Council likewise damaged the Chávez government's regional prestige. Overall, Venezuela's current dependence on trade with a variety of Latin American regional partners restricts the extent to which Chávez can fundamentally alter the hemispheric balance of power.

The United States can play a role in preserving that balance. American policymakers, however, have repeatedly overlooked the most important lesson of Chávez's rise to power: U.S. policy toward Latin America has consistently failed to address the region's most pressing social and economic problems: widespread social exclusion and poverty. The United Nations Economic Commission on Latin America and the Caribbean (ECLAC) estimated that some 40 percent of Latin America's over 500 million citizens live in poverty.¹ Although *chavista* social programs hardly represent a viable long-term development strategy, Chávez has been able to provide what financial austerity policies and macroeconomic stability could not: concrete improvements to the lives of the poor. For the moment, this success has boosted his popularity and diminished the appeal of the United States.

But Venezuela also suffers from considerable weaknesses. Venezuela's failure to diversify its economy and invest sufficiently in its hydrocarbons industry has made short-term growth dependent on oil prices. Should prices decline, Venezuela, along with countries that rely on Chávez's financial support, may face tough economic challenges. Even if oil prices remain high, further investment is necessary to create enough jobs for a growing workforce and make recent improvements in living standards sustainable. Yet, unless Venezuela is able to make its public sector more transparent, the government is unlikely to be able to attract adequate quantities of foreign capital.

With Chávez likely to win reelection in the December 3, 2006, presidential election, U.S. officials must look beyond his blustery rhetoric, examine his weaknesses,

¹ ECLAC, *Preliminary Overview of the Economies of Latin America and the Caribbean 2005* (United Nations, December 2005), p. 21.

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and think strategically about the way forward. The most suitable policy approach is to avoid demonizing Chávez, which only diminishes U.S. credibility and provides fodder for many of the Venezuelan leader's accusations. Instead, as long as Chávez does not take steps that fundamentally threaten essential U.S. interests in Latin America, the United States should demonstrate that it is willing to work with Venezuela on a pragmatic basis on such issues as counternarcotics and energy policy. At the same time, Washington should approach other regional powers, such as Brazil, Argentina, Mexico, and Chile, as well as other countries with historic ties to the region, such as Spain, to seek agreement on how to respond if Caracas takes unacceptable actions—for example, if Chávez amends Venezuela's constitution to permit unlimited presidential terms or attempts to destabilize another Latin American government. In the longer term, the most effective response to Chávez is for the United States to redirect its policy toward Latin American to address the underlying issues of poverty and inequality that fuel Chávez's appeal.

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THE RISE OF HUGO CHÁVEZ

For much of the twentieth century, Venezuela was considered an unlikely candidate for political crisis and economic turmoil. Endowed with vast energy resources, and unburdened by the serious ethnic, regional, or cultural divisions that complicate governance in many parts of Latin America, Venezuela enjoyed relative stability and prosperity.

In 1958, following seven years of dictatorial rule under General Marcos Pérez Jiménez, two prominent Venezuelan political parties agreed to present a minimum common program to voters and respect the results of a presidential election. The result was a “pacted democracy” that effectively permitted the Democratic Action Party (AD) and the Christian Democrats (Political Electoral Independent Organization Committee, or COPEI) to trade turns occupying the presidential palace. By managing and containing political competition, pacts among leading parties and interest groups created state-led industrialization, particularly in Venezuela’s all-important oil sector.

In an effort to stabilize oil prices, Venezuela helped spearhead the founding of the Organization of the Petroleum Exporting Countries (OPEC) in 1960. Between 1973 and 1978, oil prices and profits soared, thanks in no small part to the effects of the Arab oil embargo. Expanding financial resources derived from taxes and royalties charged to foreign oil companies fueled the creation of an extensive government bureaucracy.

Over time, however, Venezuelan democracy became corrupt, undermining popular support for the establishment. Because the AD and COPEI parties enjoyed privileged access to state resources, welfare benefits became increasingly concentrated among well-organized urban workers affiliated with those political parties. Consequently, popular trust in the political system diminished.

A decline in international oil prices in the early 1980s made it difficult for government officials to sustain the patronage networks and social programs underpinning political stability. By 1988, Venezuela’s current account deficit had reached 9.9 percent of gross domestic product (GDP), inflation had reached 30 percent, and net international reserves were negative \$6.2 billion. Official Venezuelan estimates placed an

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overwhelming majority of Venezuela's 19.5 million people in either relative or critical poverty.²

To stem increasing financial pressures, the government of Carlos Andres Pérez enacted a series of unpopular structural adjustment measures, introduced with the support of the International Monetary Fund. Increases in bus fares, prompted by cuts in subsidies on domestic petrol and diesel in February 1989, triggered massive riots in which hundreds of people lost their lives. The "Caracazo," as these tragic events came to be known, increased popular discontent and made it easier for nationalist and left-wing groups to win support. Lieutenant Colonel Hugo Chávez led one such group inside the Venezuelan armed forces, and stepped up plans to seize power through a coup d'état. The coup came to fruition in February 1992, and although the plot was unsuccessful, Chávez rose to national prominence as a result of a brief televised speech delivered shortly following his arrest.

While in prison between 1992 and 1994, Chávez began to reconsider *golpismo* (a belief in the effectiveness of coups d'état) and by 1996 had decided to pursue his political ambitions through electoral processes. With support for traditional parties dissipating and political disenchantment with the establishment growing, Chávez enjoyed a meteoric rise. After barely figuring in early opinion polls, Chávez won by a landslide in the December 1998 presidential election. On February 2, 1999, Chávez took office, pledging to overhaul the constitution, eliminate the corrupt two-party model, and increase antipoverty initiatives.

Once in office, Chávez immediately deployed army units to assist poverty-reduction and infrastructure projects. Simultaneously, the president clamped down on previously negligent tax collection practices for foreign oil companies. But the emphasis in his first year in office was preparation of a new constitution. In June 1999, Venezuelans elected members of a new constituent assembly, and by December 1999 a radically reformed constitution was approved by popular referendum. The popularity of the new constitution's bold social agenda aided the reelection of Chávez in June 2000 and

² Statistics from George W. Schuyler, "Perspectives on Venezuelan Democracy," *Latin American Perspectives* 23, no. 3 (Summer 1996), p. 21; Jonathan DiJohn, "The Political Economy of Economic Liberalisation in Venezuela," research paper no. 46, Development Research Centre, London School of Economics, June 2004, p. 4.

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assured the victory of many Chávez allies in legislative elections that same year. Meanwhile, world oil prices slowly began to climb, relieving fiscal pressures and allowing Venezuelan authorities to expand community assistance programs.

The prospect of further dramatic changes in government policy angered traditional elites and middle-class Venezuelans who viewed Bolivarian politics as an affront to democratic principles and a direct challenge to the status quo they had long enjoyed. On April 9, 2002, white-collar oil workers at Venezuela Petroleum (PDVSA) called for a two-day walkout in protest of the government's "politicization" of the company's board of directors. Several days later, pro-strike demonstrators clashed in the streets of Caracas with pro-Chávez activists, and in an ensuing gun battle at least eighteen people were killed.

When asked to repress the demonstrators, military leaders refused and demanded that the president leave office. Immediately, a small group of officers took control and invited Pedro Carmona, president of Fedecamaras, the main business federation, to become interim president. However, by closing the National Assembly and dissolving the Supreme Court, Carmona alienated many opposition politicians and soldiers who had originally supported the coup. To avoid further chaos, senior military officers invited Chávez back to power on April 13.

Having failed to oust Chávez in April, frustrated government opponents took part in a crippling general strike in December 2002. Thanks to unskilled Venezuelan workers, technical assistance from Iran, China, and Libya, and emergency oil supplies from Brazil, Chávez's government survived a nearly two-month shutdown of oil production.

Suspicious that Washington had supported activist groups associated with the coup and the strike led to a rapid deterioration of U.S.-Venezuelan relations and allowed Chávez to champion nationalist sentiment. Under pressure from not only the internal opposition, but also the Organization of American States (OAS), Chávez ceded to demands for a recall referendum, a mechanism introduced as part of the new 1999 constitution. In August 2004, Chávez won the contest emphatically, collecting 59.25 percent of the vote. Although opposition leaders alleged that the government had organized an elaborate fraud, international observers from the OAS and the Carter Center ruled that the referendum had been won fairly. Chávez's party, the Fifth Republic

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Movement, and its allies secured control of twenty-two out of twenty-four governorships in October 2004. In December 2005, the same political alliance won 100 percent of the 167-person National Assembly after opposition parties opted not to participate in the contest.

Domestic opponents will have a new chance to challenge Chávez at the polls on December 3, 2006. Manuel Rosales, governor of Zulia state, is seeking the presidency with the support of almost thirty political groups.

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CHÁVEZ'S REVOLUTION IN PRACTICE

Chávez's Bolivarian revolution has altered the structure of Venezuela's government and expanded the role of the state in economic decision-making. Increased social spending, funded by soaring oil revenues, has helped cement Chávez's domestic support.

STRENGTHENING THE EXECUTIVE

The 1999 constitution was intended to increase the autonomy and popular accountability of elected political representatives. New rules attempted to make judges more independent; diminish legislative bureaucracy; subject public officials to midterm recall referendums; and give greater autonomy to the electoral authority. To oversee this framework, a new "moral" branch of government was created by combining the offices of the public prosecutor, comptroller general, and public ombudsman.

In practice, however, the Venezuelan government has grown much more opaque and unaccountable. The National Electoral Council's membership is currently weighted four to one toward supporters of President Chávez, even though both the constitution and electoral law stipulate that the council should be independent. The executive branch has dramatically increased its influence over the judiciary. In 2004 the government reformed the basic law of the Supreme Court, increasing the number of judges from twenty to thirty-two. All new positions were filled by government sympathizers. In some cases, judges who have ruled against Chávez's wishes were dismissed. Far from representing a check on executive power, the new "moral" branch of government has centralized political control in the hands of the president. The public prosecutor Isaias Rodriguez is a pro-Chávez activist who has used his position to defend government interests.

For the most part, Venezuela continues to enjoy a free press, with major newspapers routinely calling for Chávez's removal from office and their owners actively involved in opposition politics. Yet the government has taken steps to indicate its limited tolerance for criticism. In 2004, a punitive media law placed restrictions on broadcast

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content, prompting media outlets to begin practicing self-censorship. Reporters Without Borders, Human Rights Watch, and the Inter American Press Association have criticized the use of alleged tax violations and other fabricated criminal offenses to harass opposition journalists.

The Venezuelan government has been frequently charged with corruption. Ninety-five percent of government contracts were awarded without competitive bids in 2004, leading to suggestions that bribery was widespread. Former Supreme Court Judge Luis Velázquez, considered an ally of Chávez's efforts to increase his influence over the court, was accused of accepting \$4 million in kickbacks in March 2006. Although high-profile government officials have publicly acknowledged and condemned particularly deplorable instances of corruption, so far none of the military officials accused of graft have been brought to trial.

In July 2006 the Venezuelan legislature drafted a proposal that would make it difficult for nongovernmental organizations receiving foreign donations to continue functioning. Though this measure is seen as a way to counter Washington's financial support of anti-Chávez groups, it also represents a dramatic challenge to the independence of all civil society organizations regardless of political affiliation.

In September 2006 Chávez paved the way for the further extension of his power by proposing a 2010 referendum on whether to allow unlimited reelection. Rather than ending the exclusive practices of the previous four decades, the current government is replicating patterns of social and political privilege, albeit in favor of a once-marginalized political base.

IMPLEMENTING ECONOMIC RADICALISM

Chávez intends to conquer two of Venezuela's greatest problems—poverty and inequality—by constructing a socialist economy that “transcends capitalism.” This has consisted of three interrelated elements: an interventionist approach to economic management; the development of a cooperative and social enterprise sector that is heavily

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dependent on public subsidies; and a rapid expansion of state spending, primarily funded by higher oil revenues.

Although Chávez initially pursued a relatively cautious macroeconomic approach, this changed during and after the oil workers' strike of 2002–2003, when controls were introduced into the foreign exchange market. Importers now have to secure the permission of Venezuela's Exchange Administration Commission in order to obtain dollars and other foreign currencies. Price controls cover a range of basic products.

After imposing interest rate caps in 2004, the central bank issued guidelines stipulating how much credit can be allocated to each sector of the economy. New banking regulations also require that one-third of all loans go to small businesses, low-income mortgages, and state-favored sectors at below-market rates. All of these policies are opposed by the business sector and rates of private investment have fallen to relatively low levels.

At the same time, the government has taken steps to increase the size and health of the cooperative sector. A total of 108,000 cooperatives—which account for 5 percent of all jobs in Venezuela—are favored for federal loans and contracts. State-owned “social production” companies obliged to dedicate a portion of earnings to social and community projects have also emerged with increasing frequency. The government has also moved quite quickly in the last two years to establish cooperatives and state enterprises in the agricultural sector. Early in 2005 President Chávez began to implement a land reform decree (originally signed in 2001) designed to eliminate large estates. By May 2006 one hundred privately owned farms deemed to be “unproductive” by state assessors had been expropriated by the government or occupied by squatters.³

Finally, the government has significantly increased spending, directing large portions of oil revenues to social projects both through budgetary allocations and discretionary spending. Extra revenues have been generated by imposing new contracts with an increased state “take” (royalties and taxes) from foreign oil companies operating in Venezuela. National government revenues have risen from \$8.6 billion in 2001 to an estimated \$49 billion in 2006. Perhaps as much as \$7 billion per year are directed toward the government's Fund for Social and Economic Development (FONDESPA). Much of

³ Author's interviews with representatives of the National Ranchers' Federation of Venezuela.

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the money has been used to finance substantial increases in social spending organized and disbursed through new institutions built alongside existing state welfare programs. Named after key events or figures in Chávez's iconographic view of Venezuelan history, these *misiones bolivarianas* (Bolivarian missions) have become closely identified with Chávez's political movement. Currently, they provide more than a dozen services, including literacy training, basic health care, subsidized food, and education. Barrio Adentro, the health care program staffed by over 20,000 Cuban doctors, dentists, and sports trainers, is perhaps the most well known of Chávez's social projects.

Chávez has also emphasized alternative trade arrangements in order to counter the perceived injustice of U.S. free trade proposals. In an effort to provide additional leverage to the faltering trading bloc, Venezuela became a full member of the Common Market of the South (Mercosur) in July 2006. Chávez is also involved in the Bolivarian Alternative for the Americas (ALBA), which functions as a political alliance that helps facilitate economic assistance between member states Venezuela, Cuba, and Bolivia.

MANAGING PDVSA AND THE HYDROCARBONS INDUSTRY

Since the December 2002 general strike, Venezuelan officials have taken a more active role in PDVSA's daily affairs, supplanting the traditional autonomy of the state company's own board of directors. This process began in earnest in March 2003, when the government fired 18,000 strikers, including many senior managers and technicians.

Caracas is renegotiating oil contracts with foreign enterprises. By imposing tougher terms, increasing royalties, and abandoning association contracts signed in the 1990s, officials created more restrictive joint ventures dominated by PDVSA. In 2005 PDVSA replaced its registry of regular contractors with a list of state-owned social production companies. These changes have been accompanied by an increase in the opacity of PDVSA's accounts. Executives recently announced that they would no longer seek to raise bond finance on the U.S. market. As a result, the company will not be required to file accounts with the Securities and Exchange Commission.

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Chávez frequently says he intends to diversify markets for Venezuelan oil and broaden the range of foreign investors involved in Venezuela's hydrocarbons sector. In fact, on several occasions, he has threatened to stop shipments of Venezuelan oil to the United States or close Venezuelan-owned refineries in U.S. territory. Chávez took one step toward achieving his goals in August 2006 by signing several energy accords with China. The Chinese currently import just over 100,000 barrels per day from Venezuela, and they have committed to purchasing 500,000 barrels per day by 2011. Moreover, Beijing has agreed to provide Venezuela with "supertankers" for transoceanic shipment and construct twelve new offshore oil drilling sites.

For the immediate future, however, Venezuela remains heavily dependent on sales to the United States. Presently, Venezuela produces close to 2.7 million barrels of oil per day, 1.5 million of which go directly to the United States. Conversely, the United States obtains approximately 11 percent of its oil imports from Venezuela. Although the bulk of new ventures involve state-owned companies from Russia, Iran, China, India, and Brazil, three major U.S. oil companies—Chevron, Conoco Phillips, and Exxon Mobil—continue to hold significant investments in the country.

In 2005, Chávez announced plans to increase total production to 5.8 million barrels daily by 2012. Yet recent declines in world oil prices have postponed plans for expansion. On September 30, 2006, Venezuela joined Nigeria in announcing that it would temporarily cut total oil production by 50,000 barrels a day in an effort to guard against a further price fall. Overall, prices have declined roughly 20 percent from their peak in mid-July 2006, but still remain far above prices from several years ago. The big question is whether PDVSA will invest enough of its own resources to sustain production and refining capacity at current levels, let alone expand operations in the future.

MAXIMIZING OIL POWER

Greater control of PDVSA, higher royalties charged to foreign oil companies, and record-high oil prices have given the Chávez government plentiful resources not only for sustaining the social programs that underpin its popular support, but also for expanding

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its influence throughout Latin America. According to Venezuela's daily *El Nacional*, during the second half of 2005 and the first month of 2006 Venezuela agreed to spend \$25.9 billion in economic aid to its hemispheric partners, with the three largest amounts going to Brazil (\$4.38 billion), Cuba (\$4.34 billion), and Argentina (\$3.95 billion). Since 2005 Venezuela has bought more than \$3 billion of Argentine bonds and has offered similar (though less generous) financial support to Ecuador. Venezuela also finances "Operación Milagro," a generous medical program staffed by Cuban doctors offering free eye care to thousands of poor people across Latin America and the Caribbean. Finally, the government provides substantial resources for Telesur, a television network designed to offer a Latin American, left-wing perspective on the news.

Caracas has also distributed free or subsidized oil in an attempt to establish friendly relations with governments in the hemisphere. During 2005 Venezuela formed three joint ventures with neighboring countries to organize low-cost regional oil supplies: PetroCaribe, PetroSur, and PetroAndina. Chávez also provides subsidized oil to some low-income communities in the United States.

CONSOLIDATING CONTROL OF THE ARMED FORCES

Through organizational changes and senior appointments, Chávez has substantially tightened his control over the armed forces.⁴ The doctrine of *pensamiento militar* (military thinking), officially adopted in July 2005, implicitly views the United States and Colombia as Venezuela's immediate enemies. Accordingly, Venezuela has suspended all military-to-military links with the United States, and is working to develop an alternative network of military allies, particularly with Cuba.⁵

In order to better defend Venezuelan sovereignty and ensure domestic security, the National Armed Forces are working to upgrade their outdated weapons, communications, and surveillance systems, primarily with new equipment purchased

⁴ Indira A. R. Lakshmanan, "Venezuelan President Chávez's Military Moves Get Scrutiny," *Boston Globe*, July 17, 2005.

⁵ Juan Forero and Brian Ellsworth, "Venezuela Ends Military Ties and Evicts Some U.S. Officers," *New York Times*, April 25, 2005.

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from Russia, China, Spain, and Brazil to arm and equip up to one million troops and reserves. According to government officials, the thrust of this military buildup is defensive. Chávez has pointed to the need for greater vigilance on Venezuela's borders, especially with Colombia, where paramilitary and guerrilla forces retain a long-standing presence.

DEVELOPING STRATEGIC FOREIGN RELATIONS

Venezuela's international relations run along two separate but intertwined lines: ideology and economics. In Latin America, Chávez draws upon a common heritage of economic struggle, pan-American sentiment, and the widespread perception that dependency on the United States and Europe is a cause of economic backwardness in order to rally support. In the rest of the world, he emphasizes Venezuela's status as a founding member of OPEC, and follows broader geopolitical and practical economic considerations, often with an anti-U.S. agenda.

Western Hemisphere

Ideological ties link the Venezuelan government to those countries and organizations historically associated with anti-Americanism in the Western Hemisphere. By consolidating a close and public friendship with Fidel Castro, Chávez has asserted his revolutionary credentials and attempted to position himself as a potential future leader of Latin American anti-imperialism. Whether Chávez can effectively lead a diverse Latin American left remains an open question. He has succeeded so far only to a limited extent.

To varying degrees, Presidents Evo Morales of Bolivia, Néstor Kirchner of Argentina, and Luiz Inácio Lula da Silva of Brazil share Chávez's belief that Latin America's social and economic inequalities are rooted in external dependence. President-elect Daniel Ortega in Nicaragua and Ecuadorian Presidential candidate Rafael Correa also hold this view. Most of these leaders have opposed recent U.S.-led free trade

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proposals and have worked to make diplomacy in the hemisphere more multipolar in nature. Presidents Lula da Silva and Kirchner, however, disapprove of Chávez's provocative style. Significant tensions have emerged between Venezuela and Brazil, especially over Chávez's influence in Bolivia, a country with which Brazil has traditionally maintained very close economic ties. Venezuela's vocal support for Bolivia's nationalization of Petrobras, Brazil's state-owned oil company, has notably strained dialogue between Brasilia and Caracas.

In other instances, Venezuelan foreign policy is dictated by energy and economic realities rather than ideology and principles. Chávez's trade policies are a case in point. Venezuela's extensive oil trade with the United States remains critical to the Chávez government's economic well-being. Venezuelan trade with the United States is booming. Non-oil exports to the United States grew by 116 percent in the first three months of 2006, increasing their importance to the Venezuelan economy. In turn, Venezuelans are importing more U.S. products, including cars, construction machinery, and computers. Although it may be Chávez's ultimate desire to end U.S.-Venezuelan interdependence, such close economic linkages cannot be easily dismantled.⁶

For Venezuela, even those relationships based on ideological ties often involve concrete economic benefits. If Chávez were able to help the Bolivian government build processing plants and extraction capacity, Venezuela would increase its importance as a regional energy player. Similarly, the PetroCaribe, PetroAndina, and PetroSur projects spread goodwill and increase Venezuela's financial leverage by converting oil subsidies into long-term, low-interest loans. More recently, Brazil, Argentina, and Venezuela have initiated plans to build a 10,000-kilometer gas pipeline stretching south from offshore Venezuelan gas fields toward Argentina, although most consider this project to be unviable. Venezuela's decision to seek full membership in Mercosur certainly carried political overtones, but it was also motivated by Chávez's desire to diversify his country's sources of trade.

Venezuelan relations with neighboring Colombia have been characterized by antagonism and distrust. To Chávez, Colombia represents a threat to Venezuelan national

⁶ Simon Romero, "For Venezuela, as Distaste for U.S. Grows, So Does Trade," *New York Times*, August 16, 2006.

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security because of its close military, political, and economic ties with the United States. For their part, Colombian authorities charge that the Chávez government allows members of the Revolutionary Armed Forces of Colombia (FARC), a guerrilla organization opposed to the government, to take refuge in Venezuelan territory.⁷

Yet, at times Chávez has been willing to pursue the pragmatic middle ground with Colombia. When bounty hunters operating in Caracas captured FARC leader Rodrigo Granda in 2004, both Venezuela and Colombia withdrew their ambassadors from each other's respective capitals, igniting a serious diplomatic crisis that threatened to imperil important economic ties between the two nations. Thanks to the mediation of Fidel Castro, both sides quickly resolved their differences and resumed negotiations regarding the construction of an important cross-border oil pipeline.

Beyond the Americas

Outside of Latin America, Chávez has exploited global hostility toward U.S. foreign policy and the war in Iraq by pursuing ties with a number of U.S. adversaries and strategic competitors. These include Syria, Russia, and Belarus. Most important, however, are Venezuela's growing ties to Iran and China.

Venezuela's collaboration with Iran is by no means new; both are key members of OPEC. Yet recent activities represent a sharp intensification of the two countries' public relationship. In a series of visits to each other's countries between July and September 2006, Chávez and Iranian President Mahmoud Ahmadinejad issued joint denunciations of the United States and signed a number of bilateral economic agreements. Iranian-owned factories in Venezuela are already beginning to construct tractors and automobiles, and the Iranian state-run oil company Petropars has expressed interest in helping Venezuela expand oil production. At a February meeting of the International Atomic Energy

⁷ The veracity of this accusation has not been definitively proven. Venezuela argues that any FARC presence in Venezuela should be seen in the context of a long-standing practice whereby successive Venezuelan governments maintain contacts with the organization in order to monitor potential implications for Venezuelan security. FARC leaders have expressed admiration for Chávez's revolution, calling its political movement the Bolivarian Movement for a New Colombia. However, the FARC is not a formal member of the *chavista* umbrella movement for Latin America, the Bolivarian Congress. Membership in this group is limited to organizations pursuing political power through electoral, rather than violent, means.

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Agency, Venezuela was one of three countries (along with Syria and Cuba) to oppose referring Iran to the UN Security Council over its nuclear program. Chávez has also supported Iran's view of geopolitics in the Middle East, comparing Israel's recent military engagement in Lebanon to Hitler's perpetration of the Holocaust. In complementary fashion, Iran backed Venezuela's recent campaign to secure a seat at the UN Security Council.

Relations with China are less politically motivated. Since 2005, Chinese investment in Latin America has grown as China seeks affordable natural resources to fuel its economic growth. Trade with China forms yet another part of Venezuela's attempt to diversify its sources of investment, though Latin America accounts for only about 3 percent of Chinese foreign trade.⁸ At the same time, Venezuela has manipulated this relationship for political advantage, threatening repeatedly to divert oil exports to East Asia and imperil U.S. national energy security.

International Organizations

Chávez has used international organizations such as the nonaligned movement, the OAS, and the UN as platforms for expressing his criticisms of American policies. During a General Assembly session in September 2006, the Venezuelan leader aggressively condemned U.S. "imperialist" intentions and publicly labeled President George W. Bush as "the devil." In an effort to earn a nonpermanent seat on the UN Security Council, Venezuelan authorities argued that Venezuela's presence on the council would help counteract "a model based on preventative war and a situation of permanent interventionism."⁹ Chávez's campaign for the seat raised fears that Venezuela would disrupt the UN Security Council's agenda, hinder the development of consensus positions, especially with regards to Iran, and seek to abolish the veto power of the

⁸ Kerry Dumbaugh and Mark P. Sullivan, "China's Growing Interest in Latin America," *Congressional Research Service Report for Congress* (Library of Congress, April 20, 2005), p. 2.

⁹ Bernardo Alvarez Herrera, ambassador of Venezuela to the United States, quoted in "Embajador de Venezuela en EEUU Defiende Candidatura para la ONU," *El Universal*, September 9, 2006.

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Security Council's five permanent members. For these reasons, Washington aggressively sought support for its preferred candidate: Guatemala.

In the end, neither Guatemala nor Venezuela secured the necessary two-thirds majority of votes in the General Assembly to assume the contested seat. After forty-seven rounds of voting, both countries conceded defeat and agreed on a compromise candidate: Panama. Not only did this outcome frustrate Venezuelan officials who had invested a significant quantity of political capital in the campaign, but it also represented a significant blow to the Chávez government's international agenda.

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U.S.-VENEZUELA RELATIONS

U.S.-Venezuela relations have deteriorated sharply in recent years and are now characterized by mutual suspicion and tension. American officials have been divided over how best to deal with Venezuela's centralization of power, nationalistic economic policies, and belligerent rhetoric while ensuring continued access to Venezuelan oil.

DEEDS NOT WORDS

In the late 1990s, a pragmatic policy of accommodation guided the American response to Chávez. The Clinton administration largely avoided direct confrontation, choosing instead to emphasize the disparity between the Venezuelan leader's radical rhetoric and his actual policies. Confident that U.S.-Venezuelan economic interdependence makes any real break in relations unfeasible, U.S. businesses have tended to favor such a cautious response.

Since President Bush entered office in early 2001, the tone of bilateral relations has deteriorated, and U.S. officials have become increasingly alarmed by the direction of the Venezuelan government under Chávez. Matters came to a head in April 2002, when the United States responded clumsily to the coup on April 11. On April 12, with Chávez held in custody at a military base, White House Press Secretary Ari Fleischer indicated that the United States looked forward to working with the transitional government, thereby giving the impression that the administration had welcomed, even supported, Chávez's forced departure. Such comments strongly contradicted the views of the Rio Group of Latin American foreign ministers, who unequivocally condemned the interruption of constitutional rule.

Although the United States signed an OAS motion condemning the breach in constitutional rule and a U.S. Inspector General investigation found that the local U.S. embassy had played no role in the coup, the Bush administration failed to dispel the

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widespread impression that it had been involved in planning it.¹⁰ Commentators in Venezuela, Latin America, and the United States continue to contend that U.S. democracy-support programs funneled money to pro-coup opposition factions. Chávez has used the coup's hazy legacy to fan anti-American fervor and discredit U.S. pro-democracy rhetoric as a guise for regime change. The Defense Department's 2005 decision to develop its first scenario for military conflict with Venezuela only reinforced Venezuela's suspicion of American motives.

Since his appointment in 2005, Assistant Secretary of State for Western Hemisphere Affairs Thomas Shannon Jr., a career diplomat, has cast a moderating tone to U.S. policy toward Venezuela. Yet, U.S.-Venezuela relations have not improved. Chávez has intensified his personal insults of the administration and noticeably expanded contacts with Iran. In February 2006 U.S. Secretary of Defense Donald H. Rumsfeld provocatively compared Chávez's election and subsequent turn to authoritarianism to that of Germany's Adolf Hitler.¹¹ Citing corruption in the Venezuelan agencies that control identity documents, as well as the government's failure to sufficiently crack down on Colombian narco-terrorists using Venezuelan territory as a staging ground, U.S. State Department officials have condemned the Venezuelan government's lackluster contributions to the war on terror and suspended sales of U.S. weapons and any military equipment with U.S. content to Caracas. In August 2006 the Central Intelligence Agency established a special joint mission to coordinate the collection of intelligence about Venezuela, Cuba, and, presumably, their ties to each other, while the State Department has suggested that Venezuela may present an impediment to a post-Castro transition in Cuba. Tensions surrounding Venezuela's campaign to secure a seat at the UN Security Council and Chávez's aggressive speech on the floor of the General Assembly have made dialogue all the more difficult.

¹⁰ U.S. Department of State, Office of Inspector General, "A Review of U.S. Policy Toward Venezuela: November 2001–April 2002," report number 02-OIG-003, July 2002, see <http://oig.state.gov/documents/organization/13682.pdf>.

¹¹ "Rumsfeld Likens Venezuela's Chávez to Hitler: Defense Chief Expresses Concern at 'Populist Leadership' in Latin America," Associated Press, February 3, 2006.

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ENERGY COOPERATION AND FOREIGN AID

According to the Government Accountability Office (GAO), ties between U.S. and Venezuelan energy officials have also deteriorated. Three years have elapsed since the last discussions between the U.S. Department of Energy and the Venezuelan Ministry of Energy. Oil production technology and information exchanges have become less frequent since 2003, damaging efforts to secure the modernization of one of the United States' most important suppliers of imported oil. Negotiations for a bilateral investment treaty initiated in the 1990s have also fallen by the wayside.

U.S. foreign aid programs continue in Venezuela, but in a limited capacity. According to the State Department's fiscal year 2007 budget, Venezuela will receive \$1 million in Andean Counter Drug Initiative funds this year—a decrease of nearly \$2 million since 2005—and \$1.5 million in Economic Support Funds to strengthen civil society and the rule of law. Most of these programs are administered by the U.S. Agency for International Development's (USAID) Office of Transition Initiatives and through its grantees, such as the National Democratic Institute (NDI) and the International Republican Institute (IRI). The scope of such efforts pales in comparison to the billions of dollars the Venezuelan government spends across the country on various social initiatives.

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WHY CHÁVEZ MATTERS

American interests in Venezuela—whether related to energy, democracy, economic development, trade, regional stability, or security—have remained notably consistent even as the Chávez government has sought to recast Venezuela’s posture in each of these areas.

ENERGY

Venezuela has been an important source of oil for the United States for more than half a century. It is the fourth-largest supplier of American oil imports (11 percent) behind Canada (18 percent), Mexico (17.5 percent), and Saudi Arabia (14 percent). U.S. refineries on the Gulf Coast rely heavily on Venezuelan crude, and Venezuelan-owned refineries are geared to provide the precise petrol and additive mixes demanded by complicated U.S. environmental regulations. The GAO recently reported that any move to completely replace oil from Venezuela with fuel from other suppliers would take several years and would require a significant increase in production capacity elsewhere in the world. For these reasons, Chávez’s threats to suspend sales of oil to the United States have raised concern among policymakers worried about American national energy security.

An immediate cutoff is highly unlikely. As important as Venezuelan oil is to the United States, Venezuela’s dependence on the American market is much more acute, with roughly 60 percent of exports destined for American refineries. As a result, any embargo would be more damaging to the Venezuelan economy than to the United States. Moreover, because oil revenues remain critical to the maintenance of *chavista* social programs, making good on threats to fundamentally alter existing trade flows would place the Venezuelan government’s domestic popularity at risk.

Chávez’s plans to gradually divert sales to China are similarly ambiguous for U.S. interests. Very few refineries outside of the United States are capable of processing

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significant quantities of Venezuelan heavy crude, and thus far the Chinese have not seemed especially eager to devote the time and money required for new construction. In geographical terms, the United States is clearly Venezuela's natural market for oil. The proposed Venezuela-Colombia pipeline may reduce shipping costs to East Asia, but selling oil to the United States will remain the prudent option. As it stands, Venezuela has had to drop the price of its oil below the global market rate to persuade China to buy.

From the Chinese perspective, Venezuela is only one piece of its global quest for natural resources. Because the Chinese actively work with major American oil firms, and because China has greater priorities with respect to the United States, whether over trade, its currency, Taiwan, or North Korea, Beijing appears to recognize that it has little to gain by strategically challenging the United States in the Western Hemisphere.

It also remains doubtful that Venezuela can expand its production as intensely as it has planned. According to most indicators, total production has barely returned to prestrike levels, with output at existing PDVSA-controlled fields declining by approximately 25 percent per year. Chinese commitments to construct twelve new offshore oil rigs represent significant help, yet are not nearly enough to increase total Venezuelan production to the proposed 5.8 million barrels a day by 2012. Increased royalty and tax rates combined with the government's lack of financial transparency could significantly depress future foreign investment potential.

Even if production fails to increase, and even if Chávez is willing to accept increased transportation expenses and submarket prices for political gain, the risk of disruption to American supplies is relatively small. Any limited loss to U.S. supply could be quickly mitigated with slightly more expensive substitutes from Africa or the Middle East. The threat that Chávez's policies immediately pose to U.S. national energy security thus is limited. Low transportation costs and the existing symmetries between Venezuelan drilling and U.S. refineries seem to ensure that oil will continue to flow northward.

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DEMOCRACY

The promotion of democracy has been a pillar of U.S. foreign policy toward Latin America since the end of the Cold War. The Bush administration has often emphasized that democratic governance remains a precondition for productive relations between Washington and Latin American nations. Such statements are based on the premise that representative liberal democracies are most likely to further regional peace and stability.

U.S. policymakers have been slow to understand why many in the region are skeptical about the American interpretation of these values. In October 2005 the polling organization Latinobarómetro reported that support for democracy had declined in a number of countries across the region since the mid-1990s. Few Latin Americans support a return to outright authoritarianism, yet decreased confidence in the ability of liberal democracies to meet basic social needs has created fertile terrain for Chávez and his followers to advance a political model based on anti-Americanism, “participatory” democracy, and a stronger economic role for the state.

In the eyes of many Latin Americans, U.S. support for democracy is inextricably linked to past support of anticommunist dictators or now defunct political parties whose economic stewardship deepened inequality and poverty. The war in Iraq has increased the unpopularity of the United States and exacerbated these perceptions. In Venezuela, lingering suspicions of U.S. involvement in the 2002 coup make American pro-democracy rhetoric seem insincere, even threatening. Capitalizing on such fears, Chávez has successfully rallied anti-American sentiment for domestic political gain.

The construction of a highly personalized, centralized political system in lieu of independent government institutions heightens the possibility of future domestic turmoil in Venezuela. Yet the capacity of the United States to influence the course of Venezuelan internal politics is limited. As long as Latin American partners opt to contain and manage the Chávez regime through trade, financial, investment, diplomatic, and multilateral ties, any U.S. efforts to change the nature of Venezuela’s government will likely be counterproductive. Limited U.S.-funded programs to support Venezuela’s civil society have been ineffective while feeding the perception that the United States aggressively seeks regime change.

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At the same time, the United States may be able to win regional allies and even build a regional consensus to prevent any further weakening of Venezuelan democracy, as would occur if elections were rigged or the constitution were amended to allow for unlimited presidential terms. Many regional governments would likely be willing to offer Washington support in opposing attempts by Chávez to destabilize other Latin American governments.

ECONOMIC DEVELOPMENT

U.S. policymakers have long promoted open markets and economic liberalization as the best protections for long-term growth, economic stability, and U.S. trade and other commercial interests. Venezuela's leaders have proposed an alternative economic development model for Venezuela based on state intervention and investments to improve social welfare.

On the surface, the results seem promising. With record-high oil prices and aggressive government social spending, Venezuela's GDP jumped by 18 percent in 2004 and nearly 10 percent last year. Overall exports have surged from under \$20 billion in 1998 to \$55.7 billion in 2005, increasing Venezuela's trade surplus from just \$4 billion in 1998 to around \$28 billion today.¹² As a result, Chávez has succeeded in reducing Venezuela's dependency on foreign borrowers and augmented the central bank's stock of dollar reserves. Whereas many oil-rich nations have failed to pass their profits to the poor, poverty levels in Venezuela have fallen significantly since 2003. In addition, the *misiones* have delivered important services to the urban poor.

Although the Venezuelan economy has posted impressive growth, Chávez's model of economic development is not sustainable in the long run. The government remains heavily dependent on continued high oil prices. At current rates of spending, a modest fallback toward \$30–\$40 per barrel could impose severe strains on the budget. Even if prices remain at current levels (nearly \$60 per barrel), the government may

¹² Statistics from World Bank Group, *World Development Indicators 2006* (Washington, DC, 2006); Hilfe Country Report, Janet Matthews Information Services, June 29, 2000.

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struggle to maintain revenues because investment in the oil sector has declined and private companies have deferred investment because of political risk.

Investment outside the oil sector has also been stagnant. Thousands of large, medium, and small businesses have closed. According to Venezuela's Central Bank, foreign direct investment has slumped from nearly \$5 billion in 1998 to \$1.5 billion in 2004.¹³ Hundreds of small cooperatives are being created with government support, but even the most optimistic Chávez supporters expect relatively few to survive. Meanwhile, Venezuela's roads, bridges, ports, and other vital infrastructure facilities are deteriorating. In 2006 these problems were highlighted by the collapse of a bridge and resultant extensive delays on the highway linking Caracas to the country's principal airport and seaport. Furthermore, only about one-quarter of the 110,000 new houses that Venezuela needs each year (to meet an overall deficit of 1.5 million) are being built.¹⁴

With oil prices expected to remain relatively high, the Chávez government has made extensive use of off-balance-sheet finance, liberally using funds from both the state oil company and the central bank to supply its social programs. A manager at Goldman Sachs Asset Management estimates that the government has a stock of at least \$12.5 billion to spend at its discretion without any sort of control.¹⁵ Stabilization funds originally designed to conserve a portion of windfall profits for future investment have been abandoned. And despite a dramatic boost to the nation's trade surplus, official ministry of finance figures show that from 1998 to 2004, the central government on average spent an amount equal to 3.2 percent of GDP more than it received each year.

Without financial transparency, foreign investment, non-oil-sector growth, and publicly accountable and independent institutions, Venezuelan officials will find it difficult to sustain economic growth and maintain current investments in education and health care. Even if oil prices remain relatively high, citizens will eventually demand a stake in an active, growing, and diverse economy, benefits that subsidized handouts cannot provide. Ultimately, these inconsistencies are far more likely to decrease support for Chávez than any form of American agitation for regime change.

¹³ Phil Gunson, "Chávez's Venezuela," *Current History*, February 2006, p. 62.

¹⁴ "Mission Impossible: Venezuela," *Economist*, February 16 2006.

¹⁵ Author interview, May 2006.

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In these ways, Venezuela's political and economic model is not a long-term alternative for the region. In fact, left-wing governments elected in recent years are choosing to pursue a mixed approach by combining market-oriented policies with social welfare strategies based on selective discretionary benefits for the poor. To varying degrees, Chile, Brazil, and Argentina have all made significant progress combating poverty while maintaining macroeconomic stability. Washington should do more to assist these efforts and craft policies that more equitably distribute the benefits of trade and financial liberalization. Doing so successfully will directly undermine the popular appeal of *chavismo* throughout the region.

TRADE

Under Chávez's leadership, Venezuela has attempted to diversify markets for its oil exports and attract a broader range of investors. This strategy has been pursued with a growing amount of belligerence toward U.S.-led free trade proposals. At the Summit of the Americas meeting in November 2005, the leaders of Brazil, Argentina, Paraguay, Uruguay, and Venezuela effectively buried the proposed Free Trade Agreement of the Americas (FTAA) by refusing to specify a deadline for talks. The major dispute centered on U.S. farm subsidies.

Yet, as in most strategic concerns, Chávez's bark in the trade arena is far worse than his bite. Venezuela's trade policies—particularly alternative, regional trade agreements—have little capacity to drastically harm American interests. By emphasizing social, cultural, and ideological exchanges, the ALBA acts primarily as a publicity tool. The Trade Treaty of the Peoples, proposed by Evo Morales in May 2006 and endorsed by both Chávez and Castro, fulfills a similar role. Rather than challenging the United States on hemispheric trade, the treaty synthesizes those leaders' political ideas. Both initiatives will confront major obstacles in the months ahead as Colombia, Peru, Panama, Uruguay, and possibly Paraguay pursue bilateral agreements with the United States.

Mercosur, which Venezuela joined as a full member in July 2006, faces similar difficulties in strengthening ties among its members. Although the Mercosur countries led

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the charge against the FTAA, continuing disputes between member states and the resistance of local vested interests to liberalization have undermined the effectiveness of the bloc. Moreover, opponents of President Lula da Silva in Brazil have criticized their government for allowing Venezuela to join Mercosur in the first place, arguing that Chávez will further delay trade integration and undermine the effectiveness of the bloc's embryonic institutions.

Despite stalled FTAA talks, stagnant World Trade Organization Doha round negotiations, and Venezuela's own alternative trade policies, trade throughout the region carries on and commercial ties between the United States and Venezuela are growing. Heightened tensions and furious rhetoric aside, both Venezuela and the United States have made clear that their ideological disputes will not trump the financial benefits each continues to derive from close economic ties.

REGIONAL INFLUENCE

Chávez's regional influence has grown substantially in recent years. Since 2005, his government has played a role in several election campaigns, implicitly and sometimes explicitly backing candidates sympathetic to his political outlook. Chávez won an important ally with the December 2005 election of Evo Morales as president of Bolivia, and has made no secret about his desire to win influence elsewhere. In Peru he supported Ollanta Humala, a radical nationalist and political outsider, who, although eventually defeated by a moderate anti-Chávez leftist, won more than 40 percent of the vote and dominated the balloting in large parts of the poorer south of the country. In Nicaragua, President-elect Daniel Ortega of Nicaragua is likely to become a close Chávez ally, as would Rafael Correa if he emerges as the victor in Ecuador's presidential contest. Chávez speaks favorably of Luiz Inácio Lula da Silva, who has won a second term as Brazilian president, while he enjoys a cordial relationship with President Néstor Kirchner of Argentina.

Despite these noteworthy trends, it would be a mistake to exaggerate Chávez's ability to influence regional political dynamics. Bolivian government officials have

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expressed a desire to act independently of Venezuela, and pressure from regional interests seeking greater autonomy may well limit the ability of President Morales to centralize power in the same way as Chávez. On numerous occasions, Latin American electorates have resisted the prospect of Venezuelan interference in their countries' internal affairs. President Alan Garcia's aggressive stance toward Caracas proved to be a vote winner in Peru. Similarly, accusations (probably unfounded) that Mexico's Andres Manuel López Obrador was close to Chávez helped Felipe Calderón turn the tables on his opponent and eventually win Mexico's election in July. More consolidated democratic and nationalist political cultures in Latin America, especially in countries such as Brazil, Argentina, Chile, and Uruguay, are generally resistant to the crude populist appeal and interventionist tactics of Chávez. For the same reasons, however, many Latin Americans view U.S. attempts to intervene in Venezuelan domestic politics are viewed with equal suspicion. As long as the United States is seen to covertly support opposition groups and promote regime change in Venezuela, U.S. denunciations of Chávez's own regional activities will ring hollow.

VENEZUELA AND IRAN

Despite international concerns about Iran's nuclear program and support for terrorism, Venezuela has strengthened its economic and political ties with Tehran through visits and economic arrangements. In March 2005 then Iranian President Mohammad Khatami visited Caracas to sign a number of bilateral economic agreements. Chávez used the occasion to voice support for Iranian nuclear ambitions. In July 2006 Chávez returned the favor by visiting Tehran and signing eleven commercial accords with the new Iranian President Mahmoud Ahmadinejad. Upon receiving the High Medallion of the Islamic Republic of Iran, Chávez announced that, "we [Venezuela] stand by Iran at every moment, in any situation." Iranian-owned factories in Venezuela are already beginning to construct tractors and automobiles, and the Iranian state-run oil company Petropars has expressed interest in helping Venezuela expand oil production.

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By more closely aligning his interests with Iran, Chávez risks alienating those Latin American allies whose cooperation and support are more vital to his hemispheric project. Currently, Chávez's economic ties with Tehran in no way compare to the significance of his trade with the United States, China, or other Latin American nations. Any international alliance that would place stress on these relationships may thus be untenable. The United States should seek the support of other Latin American governments in order to warn Chávez to keep his flirtation with Tehran within acceptable limits, such as excluding military or nuclear cooperation.

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U.S. POLICY RECOMMENDATIONS

President Chávez appears poised to win the December 2006 elections over opposition candidate Manuel Rosales. With oil prices showing little sign of protracted decline, Venezuela's leaders can be expected to continue the domestic and international largesse that has helped enhance their standing since 2003. A proposed referendum to abolish the current constitutional limits on reelection raises the prospect that, until Venezuela's opposition can mount a successful challenge, Chávez could remain in office indefinitely. Despite his failure to gain a seat at the UN Security Council, it is also probable that Chávez will continue to seek a prominent, indeed dominant, role as a voice channeling pervasive anti-American sentiment in Latin America and, more broadly, in the developing world.

In an effort to temper their once confrontational rhetoric toward the Chávez government, Bush administration officials have begun to focus their criticisms on a number of substantive arenas: narcotics, terrorism, human rights, and democracy. According to a 2006 State Department report, the Chávez government is “not fully cooperating” with U.S. antiterrorism efforts. In another report, the State Department asserts that Venezuela has “failed demonstrably” to crack down on the transshipment of illegal drugs through its territory, enforce money laundering legislation, and cooperate with U.S. counternarcotics officials. The United States has attempted to limit other countries, such as Spain and Brazil, from selling weapons to Venezuela—especially those weapons with U.S. content and technology. White House officials have also criticized “the deterioration of democratic institutions” in Venezuela, issuing a “vital national interests” certification that allows the U.S. government to fund opposition groups, primarily through USAID's Office of Transition Initiatives.¹⁶

Unfortunately, because of the benefit the Chávez government now derives from opposing the United States, and because of the bad blood that remains in the wake of the

¹⁶ See U.S. Department of State, *Country Reports on Terrorism 2005*, released April 2006; White House, “Memorandum for the Secretary of State: Presidential Determination on Major Drug Transit or Major Illicit Drug Producing Countries for Fiscal Year 2007,” press release no. 2006-24, September 15, 2006; U.S. Department of State, *2005 Country Reports on Human Rights Practices*, released March 2006.

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April 2002 coup, the prospect that such determinations will effectively influence Venezuelan policies is remote. Furthermore, because neither the United States nor Venezuela seems prepared at this stage to allow bilateral diplomatic tensions to jeopardize commercial ties within and beyond the energy sector, the U.S. government has little leverage in the near term to alter the Chávez government's political and economic strategies. For the same reason, Chávez is constrained from taking actions that could jeopardize his vital economic links to the U.S. market.

RHETORIC AND REGIME CHANGE

Because of the fungible nature of oil markets, the ineffectiveness of economic sanctions as a foreign policy tool, and the United States' damaged credibility within Venezuela and in Latin America, a policy of regime change, especially toward a country where the head of state has been fairly elected and reelected, is neither a plausible nor well-considered option. After all, Venezuela's head of state has been fairly elected and re-elected. The Venezuelan opposition does not appear strong enough to unseat Chávez through either legal or extralegal means. Furthermore, Venezuela's neighbors and the institutions into which they are grouped, such as the OAS, are highly unlikely to support any U.S. effort to destabilize Chávez. As a result, the United States would do well to avoid the perception that it is more interested in isolating and containing Venezuela than in pragmatically handling bilateral issues with Venezuela and addressing the region's broader socioeconomic dilemmas.

- President Hugo Chávez feeds on Venezuelan fears of U.S. political or military intervention. For this reason, the Bush administration and its successor should make crystal clear that the United States has no intention of intervening forcibly in Venezuela, either overtly or covertly. Such an assurance would diminish, though not extinguish, the plausibility of Chávez's claims to the contrary and provide some space for positive public diplomacy.

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- The White House and the Department of Defense, indeed all U.S. officials of the executive branch, should join the State Department in continuing to moderate the rhetoric used to characterize Venezuela, its head of state, and public officials. U.S. officials should refrain from using rhetoric that could be construed as caricature and name-calling.
- The United States is perceived to actively oppose Chávez's reelection in the December 3, 2006, presidential race and to be working in concert with the opposition candidate, Manuel Rosales. The United States should take pains to be seen as a neutral party in this contest, while encouraging opposition and *chavista* forces alike to fully exercise their right to vote.
- USAID, NDI, IRI, and all of their grantees in and outside of Venezuela must be subject to scrupulous oversight and scrutiny in order to guarantee the nonpartisan nature and constitutional commitments of their activities in Venezuela.

BILATERAL ISSUES

The domestic-political benefit and international prestige President Chávez gains as a prominent anti-American opponent may well, even after the election, be greater than the benefits he perceives of more cooperative bilateral ties with Washington. Nevertheless, it may still be possible to pursue a pragmatic relationship with Venezuela. The United States has successfully conducted its bilateral affairs with other countries whose governments, either in deed or word, challenge American interests. Continued trade acts as a strong disincentive against a more dramatic escalation of conflict.

The United States and Venezuela might fruitfully pursue negotiations on several issues of mutual concern. These include regional and border security, the environment, immigration, energy, drugs, terrorism, and the spread of infectious diseases. The response of the Venezuelan government to proposals for bilateral dialogue will provide an important barometer of whether Chávez is prepared to find common ground with the United States.

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- After the December 2006 presidential election, the Bush administration should offer to hold working-level discussions with Venezuelan officials on a range of specific bilateral issues, such as border security, energy, drugs, and public health. This gesture from Washington would help demonstrate to the region that the United States is trying to work pragmatically with Caracas, despite Chávez's rhetoric. If Caracas rejects the overture, the United States would be in a stronger position to convince other countries in the region that Chávez is at fault for failing to reduce tensions.
- Venezuela should be invited to participate in a regional dialogue on energy security. An organization such as the Western Hemisphere Energy Cooperation Forum, a proposal outlined in the as yet to be passed Energy Diplomacy and Security Act of 2006, might allow both sides to resume long-stalled discussions on shared energy interests.
- Venezuela should also be invited to participate in the Inter-American Development Bank's program supporting sustainable energy and biofuel development in Latin America.

REGIONAL DIALOGUE

Moderating rhetoric, vetting the impartiality of U.S. democracy support programs, and proposing bilateral talks will help the United States shed the perception that its policies are guided by partisan fervor rather than principled pragmatism. This does not mean, however, that the United States should grant *carte blanche* to Venezuelan authorities. The humiliating defeat of Venezuela's efforts to secure a UN Security Council seat may have damaged its international credibility and temporarily dampened the bluster of its international diplomacy. Nonetheless, U.S. officials should continue to closely monitor Venezuela's domestic political environment and international ties, particularly with Iran. Because U.S. unilateral leverage in the country is so limited, the best way for the United States to ensure that its interests are not directly threatened is to pursue a diplomatic

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strategy that seeks to mobilize regional support to constrain Chávez's actions in the future.

- The United States should open a discussion with other regional leaders, such as Brazil, Chile, Argentina, and Mexico, on how to respond in the event that Chávez crosses certain “red lines” in his domestic or foreign policy. While it will be difficult to achieve regional consensus on specific red lines—much less on how to respond in the event that such red lines are crossed—it would be a useful exercise to discuss potential areas of agreement. There may be common opposition to any Chávez effort to amend the constitution to allow for unlimited presidential terms, support instability in neighboring countries, or develop a military relationship with Iran. The existence of this regional dialogue could help deter Chávez from taking unacceptable actions and pave the way for a joint response in the event that he takes steps that cause a crisis in Venezuela or the region.
- The potential for such an overture to succeed depends heavily on the tone with which the United States approaches its regional partners. Conversations should be exploratory in nature and conducted in a spirit of mutual respect. Admittedly, the United States may face an uphill battle convincing some countries that discussions of this nature are in their interest, especially for nations with significant economic links to Venezuela. Only if this initiative occurs simultaneously with a broader shift in Washington's approach to Latin America can it achieve positive results.

U.S. POLICY TOWARD LATIN AMERICA

In a region that is traditionally suspicious of American power, widespread skepticism toward American foreign policy and the recent decline of U.S. moral authority makes it especially urgent that the United States work to redress Latin America's major problems: poverty, insecurity, political polarization, and crises in governance. Just as the Council on Foreign Relations' Center for Preventive Action *Andes 2020* Commission argued in

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2004, a smart U.S. policy agenda toward the Andean region—Venezuela, Colombia, Ecuador, Peru, and Bolivia—must better balance pro-democracy and counternarcotics agendas with initiatives aimed at reducing social exclusion and inequality. The same principles can and should be applied to Latin America as a whole.

Achieving such a difficult goal will require innovative, flexible approaches to free trade and resource nationalism, as well as a willingness to work closely with hemispheric partners—Brazil, Argentina, Mexico, to name a few—that remain open to socially responsible integration efforts. The U.S. Congress should evaluate the utility of spending billions of dollars on the drug war while also considering adjustments to the Millennium Challenge Account criteria, so that poor communities in middle-income countries can become eligible for assistance. A more effective strategy will entail greater flexibility in the awarding of aid and other assistance contracts so that local firms, not just American companies and entities, are eligible for bidding. Also necessary is renewed public dialogue about the kinds of adjustment assistance and other fairness measures that can accompany free trade agreements to offset the inevitable dislocations that small producers, especially in agriculture, will face. Lastly, government officials must understand the impact of the perceived injustice of U.S. immigration policies on American credibility throughout the hemisphere. Over the long term, this strategy will help to reduce the appeal of leaders such as Chávez.

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CONCLUSION

President Chávez thrives on conflict with the United States. His domestic popularity is directly linked to his success in delivering long-absent social welfare improvements to poor Venezuelans. Though limited, Chávez's regional appeal draws upon a discourse emphasizing inequality, poverty, and social justice. Despite Chávez's political theater, his ability to harm U.S. interests is actually quite limited. His economy is heavily dependent on access to U.S. markets, particularly oil markets. Indeed, the biggest beneficiary of Venezuela's strong commercial ties to the United States is the Venezuelan government itself, which directly controls PDVSA. Although President Chávez plays on anti-American sentiment in the region, Latin American electorates largely resist outside involvement by anyone, even those individuals with appealing antiestablishment, anti-American ideologies. Other regional leaders act as important counterweights to Chávez's populism and do not want to see an escalation of tensions between the United States and Venezuela sparked by provocations from Caracas.

To deal with Chávez, the United States needs both a long-term and a short-term strategy. In the short term, the United States should be seen in the region as ignoring Chávez's theatrics and seeking to work pragmatically on issues of bilateral and regional concern, such as energy security, terrorism, poverty reduction, the environment, and the spread of infectious diseases. By offering to expand bilateral working-level discussions with Caracas after the December 2006 presidential election, Washington wins either way—whether Chávez accepts or rejects the American “peace” overture. Such a practical approach, even if it fails to yield significant results, may make Latin American governments more willing to work with the United States collaboratively in an effort to establish a clear set of boundaries that Venezuela will not be permitted to cross.

In the long term, the United States needs to tackle the underlying problems of inequality and poverty that feed Chávez's appeal. Restoring U.S. leadership will require a significant shift in how the United States articulates its vision for the Andean region and Latin America as a whole. It is imperative that American government officials begin to directly and openly acknowledge the profound social schisms that most Latin Americans

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face each day. Only by attacking the root causes of inequality that fuel Chávez's involvement in the affairs of fragile states can the United States regain credibility as an advocate of democracy in the hemisphere.

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Richard Lapper has been Latin America editor at the *Financial Times* since May 1998, where he guides its coverage on Latin America both in the newspaper and online. He writes most of the *Financial Times*' editorials on the region and edits, often writes Latin America Agenda, a weekly online analytical column, and contributes frequently to the newspaper's features pages. Mr. Lapper joined the *Financial Times* in 1990 and was insurance correspondent, capital markets editor, and financial news editor before assuming his current position. He has had a long association with Latin America, making his debut in journalism in 1980 as a Central America correspondent with the London-based *Latin America Newsletter*, subsequently writing on a wide range of development and financial issues for publications including the *Economist Intelligence Unit*, *South Magazine*, and *Caribbean Insight*. Mr. Lapper is currently based in Sao Paulo, Brazil, but travels frequently within the region and in the United States.

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