NEWS ANALYSIS

By Nina Tulloch, Hogan Lovells International

Venezuela – the challenge continues

Venezuela is in a period of undoubted economic crisis. With inflation running at over 60%, a continuing recession and a credit rating of CCC, these are challenging times. The presidential elections have been slated for September 2015. It remains to be seen whether these will actually go ahead – so uncertain is the political climate.

Difficult economic and political environments do not traditionally lend themselves to a thriving insurance market. Premiums in 2013 were in the region of $13,290m with life premiums around $400m. Growth has been slow since then. Will the new currency exchange platform make any difference?

Venezuela does have an insurance market – but one that lacks capacity, especially for general liability and property covers. This means that many local insurance companies have had to go to the international reinsurance markets to find capacity – but that is no easy task when outwards reinsurance is expensive given that the currency exchange system has historically been so volatile.

The leading insurance companies remain domestic insurers – while there are generic prohibitions against non-admitted insurance, enforcement appears to be largely ineffective and penalties are rare. Foreign insurers can operate either as shareholders in a local company which has been licensed by the Venezuelan Regulatory authority or as a foreign reinsurer holding its own license. However, foreign and domestic insurers looking to reinsure undoubtedly feel the effect of the government's ever-changing regime of currency control.

"Difficult economic and political environments do not traditionally lend themselves to a thriving insurance market"

The country now has three official exchange rate tiers. There is the primary rate of 6:3:1 which is used for imports deemed to be essential (food, medicines, agricultural imports). Then there is the SICAD rate, an auction based system which permits purchase of foreign currency for imports. In February of this year, the government introduced a new foreign exchange trading platform known as SIMADI.

This new market is the government's fifth attempt in twelve years to meet demand for dollars and to try and eliminate illegal trading. The new platform allows banks and brokerages to trade cash and swap bonds at a rate agreed among themselves on a state operated exchange.

One potential advantage of the new system for insurers is that there are no longer the state imposed price pegs which be-set the old exchange systems. This new market gives foreign companies a way to repatriate earnings at a considerable discount.

The problem of foreign investors not being able to withdraw funds from Venezuela has long hampered growth and opening of the market. However, foreign insurers looking to invest are still caught by the Foreign Investment Act passed last year which places restrictions on outward capital movement and so it is not clear whether the introduction of SIMADI will have any significant effect.

However, US dollars are persistently in short supply which means that the government has not started to restrict residents to buying just USD 2000 a month and the new trading platform started out charging 172 (now 190) bolivars per dollar – only marginally better than the black market rate. Three months on and it is probably too early for insurance companies to judge whether the new exchange system allows for profitable trading in the country.

All of this looms in the shadow of expropriation which remains a significant issue and probably more so in the run up to the Presidential election. Expropriation is the means by which the government takes assets and businesses back under state control. The knock-on effect of this for insurance markets across all lines is potentially considerable and the uncertainty undoubtedly underpins continued slow growth in the sector. ■