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Venezuela instability: market implications

The potential for regime change in Venezuela presents a complex mix of opportunities and risks for global oil markets, US-China relations, and regional stability. While the long-term outlook for oil supply and regional risk premium may improve, the transition period could be volatile, with significant implications for investors and policymakers alike.



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Key takeaways

- We think the most likely scenario in Venezuela is a continuation of the status quo or regime change involving an orderly transition to a more pro-Western government.
- Given the potential for Venezuela's bigger role in oil markets and growing competition between the US and China in South America, we think it is important to explore the potential transmission channels and market implications – what we term the "Venezuela trades".
- We think there is the potential for short-term gains for oil prices during instability, but likely lower prices over the longer term if Venezuela raises oil supply, and regime change could pave the way for a consequential sovereign debt restructuring.



VENEZUELA INSTABILITY: MARKET IMPLICATIONS

In our Outlook 2026, we identified several geopolitical bright spots around the world, including progress towards peace in Gaza, the containment of the Iranian regime, and even the possibility of an end to the war in Ukraine. However, these positive developments are counterbalanced by rising tensions between the US and Venezuela. The extent of US willingness to intervene remains uncertain.

Predicting Donald Trump's next move remains difficult and views within the US administration on Venezuela are mixed. We think a "boots on the ground" scenario is less likely as the US would be keen to avoid further destabilising the region and potentially increasing migration to the US. More likely in our view is therefore a prolonged period of tensions with the potential for limited missile strikes on strategic targets, or a form of managed exit for Venezuelan President Nicolás Maduro.

But we think the most likely scenario is a continuation of the status quo or regime change involving an orderly transition to a more pro-Western government. So, it is prudent to explore the potential transmission channels and market implications – what we term the "Venezuela trades" – starting with the implications for oil.

Implications for oil prices, US-China relations and regional risk

Hypothesis 1: Oil market reconfiguration – Regime change in Venezuela could ultimately increase global oil supply, intensify competition among producers, and lower energy prices after an initial period of volatility.

Venezuela holds the world's largest proven oil reserves (about 303 billion barrels, or 17% of global reserves, according to the International Energy Agency), yet sanctions and chronic underinvestment have slashed production to just 1.0-1.1 million barrels per day (mbpd), a third of its 1990s peak. Around 85% of this output (0.8-1.0 mbpd) is currently exported to China.

A pro-Western government in Venezuela could see sanctions eased and attract the necessary USD 80-100bn (Citi estimate) of international investment to raise production by 1-2 mbpd over a multi-year horizon. This

would effectively add the equivalent of a mid-sized Organisation of the Petroleum Exporting Countries (OPEC) producer to global supply. But any recovery in production would depend on OPEC+¹ quota negotiations, which may limit near-term supply increases.

However, a destabilised Venezuela – particularly if regime change is achieved through military intervention – could temporarily reduce production further, spiking prices before any long-term supply benefits materialise.

Hypothesis 2: US-China strategic rivalry in South America – China has become South America's largest trading partner and foreign investor, with deep stakes in energy, infrastructure and critical minerals (lithium, cobalt), as well as control over strategic ports like Chancay in Peru. A shift in Venezuela's government could force China to diversify its crude oil imports, modestly raising logistical costs but not fundamentally altering supply security.

In any case, uprooting China's entrenched position in Brazil, Argentina, and Chile – where it has secured access to a broad range of raw materials – will be far more difficult.

Still, we see the US as a much closer strategic and cultural ally to South America, as well as a larger investor. We are seeing politics shift broadly to the right in many South American countries due to security and economic issues – with important elections in Chile, Peru, Colombia and Brazil in the next 12 months. A right-leaning shift could push the region closer to the US and the Trump administration.

Hypothesis 3: Regional risk repricing – Orderly regime change could reduce regional instability and lower risk premium, but military intervention risks triggering new crises.

Venezuela's prolonged crisis has generated seven million refugees, a GDP collapse of over 75% since 2013², and spillover effects such as increased crime and armed group activity in neighbouring Colombia and Peru. This turmoil has contributed to higher sovereign bond spreads and investor caution across South America.

¹ A larger group consisting of OPEC members and other oil-producing countries.

² Source: **The Venezuelan Exodus: An Unprecedented Economic and Humanitarian Crisis**, IMF

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A stable, US-aligned government in Caracas could lower the risk premium for Venezuela and its neighbours, improving capital flows. However, military intervention could provoke a regional backlash, a fresh surge in refugees, and insurgency risks, especially in countries with governments not aligned with the US, such as Colombia and Brazil.

In our view, most positive economic effects would unfold only gradually, with instability dominating the near-term outlook.

Implications for Venezuela sovereign bonds

Regime change in Venezuela would also set the stage for a potentially very consequential sovereign debt restructuring, which could dominate the initial market reaction. The country's sovereign bonds have been in default since 2017 but have surged in price over 2025 on expectations that pressure from the Trump administration may lead to Caracas eventually regaining access to international bond markets.

The main determinant of the recovery value of Venezuela bonds is how quickly oil production could be increased as economic growth is highly correlated with the gross value of oil production. This would require significant capital investment over a long horizon.

We think a sovereign debt restructuring would involve an extended negotiation process and a recovery value in the range of 40 to 50 cents in the dollar would be a best-case scenario. Therefore, bonds trading in the low 30s look fairly valued in our view given the uncertain outlook.

Alongside a potential IMF programme, bilateral support from the US would also be key to Venezuela's longer-term recovery. That support could come in a similar form to the financing and currency support the Trump administration recently provided to Argentina, and private capital would also see significant opportunities in a reconstruction effort.

Market implications: possible short-term gains for oil

In summary, our expectations of continuing tensions in Venezuela may have considerable market implications:

- **Energy and commodities** – We think there is the potential for short-term gains for oil prices during instability, as well as a medium-term downside risk as Venezuelan supply recovers.
- **Emerging market debt** – If Venezuela regains market access, sovereign spreads in neighbouring countries may compress as stability improves. In the near term, market spillovers could be limited (assuming the worst humanitarian case of severe destabilisation and further migration is avoided), with Venezuela relatively economically isolated as a largely failed state. Distressed debt investors may also find opportunities in Venezuelan and Petróleos de Venezuela (the state oil company, known as PDVSA) bonds.
- **Currencies** – Oil-exporting currencies (such as the Colombian peso) may weaken if global energy prices fall. The Canadian dollar could weaken if the US pivots south for energy supply. South American FX could strengthen on improved sentiment but would remain volatile during any transition.
- **Equities** – South American financial services and infrastructure may benefit from capital inflows if reforms materialise. China-related sectors (eg, heavy industry, manufacturing) could face marginal cost pressures from higher raw material prices.
- **Risk management** – Investors may consider maintaining hedges for oil price volatility and monitoring political risk in Brazil and Colombia as potential offsets to regional stability gains.

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