

## ECUADOR

### 1. General trends

Ecuador ended 2014 with GDP growth of 3.8%, which was 0.8 percentage points less than in 2013. This slowdown was largely accounted for by the drop in international oil prices and the resultant fall-off in public spending as oil revenues contracted. In this situation, private consumption was the main driver of growth, expanding by 3.9%.

2015 is expected to be a difficult year for the country, given an external environment of low oil prices, appreciation of the dollar against the currencies of key trading partners, and global demand that remains subdued. Growth in the economy over the current year will largely depend on the oil price and on access to external financing, and is expected to slow to around 1.9%.

Cumulative inflation stood at 3.7% in 2014, one percentage point more than in 2013. The cumulative 12-month rate to May 2015 was 4.5%. Nonetheless, economic sluggishness and dollar strength in 2015 will help restrain the inflationary pressures that could result from tax and duty increases and planned reductions in a number of State subsidies (including a 10.1% cut in fuel subsidies). In sum, cumulative inflation in 2015 is expected to be slightly above the 2014 rate.

The non-financial public sector had an overall deficit of 5.25%, wider by 0.65 percentage points than in 2013. Given expectations of a large drop in oil revenues and the government's intention of maintaining spending, a larger deficit is to be anticipated in 2015 if the necessary financing can be raised. A number of initiatives to strengthen the fiscal position were introduced in late 2014 and the early months of 2015, including tax measures, a reduction of the State's pension obligations and cuts in current and capital spending.

The balance-of-payments current account deficit fell to 0.6% of GDP in 2014, mainly because of a reduction in the goods and services deficit. Worker remittances have yet to recover from their sharp decline since 2008, when the international financial crisis broke out. The deficit is expected to rise in 2015 because of lower oil prices and dollar appreciation, although this may be partly offset by a range of trade policies.

To deal with the worsening of the trade balance and the reduction in international reserves in the fourth quarter, some tariffs were increased and safeguards introduced, among other measures. Depending on how the external sector evolves over the rest of the year, further measures can be expected to limit deficits and currency outflows.

### 2. Economic policy

#### (a) Fiscal policy

Fiscal policy remained expansionary in 2014, although less so than in previous years. Nominal non-financial public sector spending increased by 6.6% and the State's share of gross domestic product

(GDP) was 44.1%. On the revenue side, growth slowed even more, to 4.9%, so that the overall deficit rose to 5.3% of GDP (against 4.6% in 2013).

The most dynamic component of non-financial public sector revenue was the contribution of non-financial public enterprises, which grew by 40.1%, followed by tax revenue, which was up 5.8%, driven mainly by a higher total take from income tax (up 8.1%) and other taxes (up 5.7%). Meanwhile, oil revenues fell by 4.6%, owing to a drop in the crude price from July 2014.

The slowdown in overall non-financial public sector spending particularly affected capital expenditure, which grew by 5.0% (compared to 33.5% in 2013), reflecting the combination of contraction in public investment (by 0.3%) and expansion in investment by public enterprises (5.8%). Current spending was up by 7.5% (having increased by 10.4% in 2013), mainly because of growth in purchases of goods and services (20.1%) and in wages (6.5%).

The main sources of financing for the deficit were the issue of the 2014 sovereign bond for an amount of US\$ 2 billion in June 2014, together with fresh borrowing from institutions in China (both adding to the external public debt), in addition to issuance of long-term bonds that increased outstanding domestic debt. As a result, central government public debt rose to 27.8% of GDP in late 2014 from 23.1% the year before. Domestic debt rose from 10.5% to 12.5% of GDP and external debt from 12.6% to 15.4%.

The fiscal outlook for 2015 has been complicated by the falling price of the Ecuadorian crude blend, which, on average, will probably remain below the US\$ 79.7 a barrel projected in the budget — albeit above the forecast of US\$ 45 used by the central bank for its revised GDP growth estimates in June. The first budgetary adjustments to cope with lower oil revenues were announced in January 2015, specifically a cut of US\$ 837 million in public investment and of US\$ 580 million in current spending, along with further measures to increase revenues and cut fiscal outgoings. In addition, external financing has been secured in the form of new loans from China, as well as global bond issuances in March and May 2015, of US\$ 750 million each.

Among the additional measures, particular mention should be made of the December 2014 tax reform, which restricts deductible expenses, expands the tax base and raises the cost of taking and keeping foreign-exchange abroad. A tax amnesty enacted in April 2015 provides for forgiveness of fines and interest on back taxes and debts owed to the National Development Bank. On the spending side, in addition to the cutbacks announced in January, the State expects to save over US\$ 1 billion under the provision releasing it from its obligations in respect of the retirement pensions of the Ecuadorian Social Security Institute (IESS), approved in April as part of the Fundamental Law for Fair Employment and Recognition of Work in the Home. Taken together, these measures are expected to reduce State financing needs by some US\$ 3.5 billion.

#### **(b) Monetary and exchange-rate policy**

The Central Bank of Ecuador kept lending rate caps unchanged across all credit categories during 2014. Average lending rates also held fairly steady in all categories except corporate production, where there was greater volatility, with the average declining from 8.2% in November to 7.3% in December and staying at around that level for three months before rising back to 8.5% in March 2015.

The volume of lending by the private-sector financial system grew by 7.6% in the 12 months to December, as compared to growth of 11.5% the previous year. Public-sector lending, on the other hand,

underwent a sharp contraction of 16.5% relative to 2013. Meanwhile, lending by the Ecuadorian Social Security Institute Bank (BIESS) increased by 16.3%. As a result, lending by BIESS and the public sector combined was up by 5.0%.

The most dynamic categories in 2014 were private-sector mortgage lending and microcredit, with growth rates of 17.9% and 13.6%, respectively, following contraction in these same areas of activity during 2013, with declines of 1.2% and 1.1%. Meanwhile, BIESS mortgage lending grew by just 8.1%, following years of much stronger growth. As a result, the BIESS share of mortgage lending dropped to 64.8% in 2014, from 66.8% the year before.

Private-sector lending volumes during the first quarter of 2015 performed much as in 2014, with a growth rate of 7.9% driven by a pick-up in microcredit (16.3%) and mortgage lending (26.5%).

In April 2015, the Board of Monetary and Financial Regulation established a new mortgage lending policy to enhance incentives for social housing construction, lowering the BIESS mortgage rate from 8.48% to 6.0% (with no down payment) and the private-sector bank mortgage rate from 10.0% to 4.99% (with a 5% down payment).

Also in April, credit categories were modified and new rate caps were set, coming into force in May. Maximum rates of between 9.33% and 11.83% were set for the new priority commercial credit category, while the new ordinary commercial credit category was capped at 11.83%. Consumer credit was divided into an ordinary consumption category and a priority consumption category, both with a maximum rate of 16.3%. The caps for the new education, public interest housing and public investment categories were set at 9.0%, 4.99% and 9.33%, respectively. Microcredit caps were also adjusted, with the retail rate being cut from 30.5% to 25.5% and the extended accumulation rate raised from 25.5% to 30.5%.

To facilitate financial transactions, starting in late September 2015, public and private financial institutions will be required to accept and conduct transactions in the electronic currency introduced by the government in 2014.

The real effective exchange rate maintained its strengthening tendency during 2014, with an annual rise of 3.9% to December, owing to the inflation differential with the United States and the performance of the dollar against the currencies of Ecuador's other trading partners. In the 12 months to May 2015, this increase quickened to 7.5%.

#### **(d) Other policies**

In December 2014, trade measures were introduced in response to the sharp rise in the current account deficit during the fourth quarter of 2014 and a drop of over 40% in international reserves between September and December. Import tariffs were increased by between 5% and 40% on 588 capital goods items and on agricultural, textile and telecommunications inputs. Import quotas were also restricted, especially for vehicles, with both completely built-up (CBU) and complete knock-down (CKD) vehicles being affected.

A foreign-exchange safeguard was also announced in December for products from Colombia and Peru. This was rejected by the Andean Community, and following negotiations a general balance-of-payments safeguard under World Trade Organization (WTO) rules was announced in March for a period of 15 months, with rate variations of between 5% and 45%.

In April 2015, the National Assembly passed the Fundamental Law for Fair Employment and Recognition of Work in the Home, which reforms a number of aspects of the Labour Code. The greatest change is the abolition of the 40% contribution the State was obliged to make to the retirement pensions of the IESS. Other elements of the reform include recognition for the unpaid work of housewives and their inclusion in the social security system (which should bring a further 1.5 million people into the IESS) and changes to employment contract types, bonuses, employment stability, profits and guarantees for expectant mothers and union officials in the event of dismissal. In addition, the highest pay in any given firm was capped at 20 times the lowest, with a view to narrowing the pay gap.

### **3. The main variables**

#### **(a) The external sector**

In 2014, the balance-of-payments current account deficit fell to 0.6% of GDP (a 0.4 percentage point improvement on 2013), owing to a reduction in the goods and services trade deficit.

Exports rose 6.7% by volume in 2014 (according to trade balance figures), with improvements across the board. Nonetheless, the drop in the average price of Ecuadorian crude from US\$ 95.87 a barrel in 2013 to US\$ 84.32 in 2014 meant that oil exports fell 5.7% by value even as they rose 7.0% by volume. At the same time, non-oil exports grew 5.9% by volume and 15.7% by value. The net result of these different trends was that total exports rose 3.6% by value, one percentage point less than in 2013.

The United States remains Ecuador's largest export market, although its share of the total dropped from 44.7% in 2013 to 43.8% in 2014. The share of the Latin American Integration Association (LAIA) countries increased from 24.9% to 28.5%, while those of the Andean Community and European Union countries dropped by 1.4 and 0.6 percentage points, respectively. This trend is expected to reverse in the latter case upon implementation of the trade agreement concluded in 2014, which is scheduled for September 2016. The Asian countries' share continued to increase, rising to 9.6% in 2014.

Imports grew by 2.2% in value terms during 2014, so that the trade deficit narrowed. This lower growth was due to a drop in import prices, since volume grew by 10.8%, with large increases in the categories of consumer goods, raw materials, and fuels and lubricants (owing to the need to import refined petroleum products because of the temporary shutdown of the Esmeraldas refinery). In the raw materials category, the volume of building material imports fell, reflecting the economic slowdown in the sector and the substitution of local products for imports. The volume of capital goods imports for industry also fell, in line with the sharp slowdown in gross fixed capital formation in 2014.

While the services deficit fell owing to an increase in the value of services provided, the income deficit grew because of increased profit repatriation and debt service. Net transfers rose in absolute terms but fell as a share of GDP. Worker remittances grew by 0.5% after contracting in 2013, but without regaining their 2012 level, let alone their 2007 peak. While remittances from the United States have been growing again since 2013, those from Spain have continued to contract, albeit more slowly since 2012.

The capital and financial account surplus dropped back to 0.4% of GDP in 2014 from 3.1% in 2013 owing to a sharp decline in flows in the other investment category, including commercial credits and loans. On the other hand, portfolio investment registered a large rise in debt securities associated with the issue of the 2014 sovereign bond for an amount of US\$ 2 billion. International reserves as of December

2014 were 3.9% of GDP, or 0.7 percentage points less than in the same period of 2013. This decline continued during the first months of 2015, and in early May reserves fell to a low of 3% of GDP, before recovering to around 3.7% by mid-June thanks to foreign-exchange inflows from global bond issues.

The trade balance went back into deficit in the first quarter of 2015, partly because exports fell 26.3% by value from the same period the year before. Specifically, the value of oil exports fell by 50.3% while their volume rose by 12.8%. Meanwhile, non-oil exports rose 1.6% by value and 7.6% by volume. Imports responded to the new trade restrictions with a drop of 6.1% by value and 3.5% by volume, but this reduction was not enough to offset the contraction in the value of exports.

### **(b) Economic activity**

GDP grew by 3.8% in 2014, continuing the slowdown that began in 2011. The largest contribution to growth was from private consumption, which rose by 3.9%, followed by gross fixed capital formation, up 3.7%. In the latter case this was a departure from the trend seen from 2010 to 2013, when major public investment projects resulted in double-digit growth rates in this segment. The contribution of net exports was negative, although less so than in 2013, since goods and services exports grew faster than imports (6.2% against 5.5%).

The construction sector continued to slacken after its double-digit performance in 2011 and 2012. Nonetheless, the sector still grew by 5.5% (2.8 percentage points less than in 2013), and contributed 0.55 percentage points to GDP growth, second only to the oil and mining sector, which grew by 8.0% and contributed 0.81 percentage points. Services continued to increase their share, with contributions of 0.47 and 0.49 percentage points from commerce and from professional, technical and administrative activities, respectively. A negative factor was the sharp drop in oil refining (47.9%), owing to the temporary shutdown of the Esmeraldas refinery for repowering.

The oil sector was more dynamic than in previous years, despite falling prices. The country's crude oil output rose by 5.7%, driven by strong growth of 9.0% in the output of public enterprises, while the output of private-sector firms contracted by 4.5%.

Oil output at both public enterprises and private-sector firms during January-April 2015 was slightly lower than in the same period the year before. Given low crude prices, moreover, output is not expected to pick up significantly during the remainder of 2015. In fact, it was announced in April that State firms would cut output by 10,000 barrels a day by discontinuing production at the least efficient fields.

### **(c) Prices, wages and employment**

Cumulative inflation at the end of 2014 was 3.7%, one percentage point higher than in December 2013. The category contributing most to this rise was food and non-alcoholic beverages, which represents a quarter of the reference basket, with prices increasing by 4.5%. The categories with the largest increases were miscellaneous goods and services (6.3%), housing, water, gas, electricity and other (5.5%) and education (5.2%). Conversely, there was deflation of 0.3% in the communications category. The 12-month cumulative inflation rate to May 2015 was 4.5%. The categories contributing most were food and non-alcoholic beverages (with annual inflation to May 2015 of 5.3%), transport (7.0%), and housing, water, gas electricity and others (6.2%).

The average annual urban unemployment rate rose by 0.4 percentage points from 2013, to 5.1%. This increase does not seem to have been caused by the economic slowdown, however, since at the same time there was a small rise in the employment rate from 58.9% to 59.0%. Rather, it was an increase in the participation rate (from 61.8% to 62.2%) that drove the unemployment rate higher.

The minimum wage rose by 3.2% in real terms in 2014 (based on the standard minimum monthly wage plus the thirteenth and fourteenth wage payments). A nominal increase of 4.16% was agreed for 2015, which should represent a small real-terms rise.

Table 1  
ECUADOR: MAIN ECONOMIC INDICATORS

	2006	2007	2008	2009	2010	2011	2012	2013	2014 a/
	<b>Annual growth rates b/</b>								
Gross domestic product	4.4	2.2	6.4	0.6	3.5	7.9	5.2	4.6	3.8
Per capita gross domestic product	2.6	0.5	4.6	-1.1	1.8	6.1	3.5	3.0	2.2
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	4.3	3.4	1.7	1.7	0.7	7.9	0.8	5.6	2.8
Mining and quarrying	5.5	-7.5	0.0	-0.3	0.1	2.8	2.6	7.8	8.0
Manufacturing	4.1	3.2	9.1	-0.8	2.4	6.4	1.7	1.9	-0.1
Electricity, gas and water	0.0	17.1	30.0	-10.0	34.5	27.1	17.9	7.4	9.0
Construction	4.6	1.0	8.8	2.8	3.4	17.6	13.0	8.3	5.5
Wholesale and retail commerce, restaurants and hotels	4.4	0.4	10.0	-2.2	3.5	5.8	4.5	6.1	4.9
Transport, storage and communications	7.1	4.7	9.8	7.0	5.4	7.7	6.9	5.9	3.5
Financial institutions, insurance, real estate and business services	4.9	4.1	4.7	12.4	3.1	7.0	4.7	2.8	4.7
Community, social and personal services	3.3	5.2	4.2	-4.6	6.4	6.8	6.7	2.4	2.9
Gross domestic product, by type of expenditure									
Final consumption expenditure	4.3	4.4	6.2	0.9	7.2	5.7	4.1	4.0	3.8
Government consumption	3.8	5.7	11.1	11.6	4.4	8.7	11.1	7.7	3.6
Private consumption	4.4	4.2	5.4	-1.0	7.7	5.1	2.7	3.2	3.9
Gross capital formation	7.8	4.2	22.5	-7.3	10.5	11.5	3.7	11.7	3.3
Exports (goods and services)	7.1	0.0	3.0	-4.8	-0.2	5.7	4.7	2.4	6.2
Imports (goods and services)	9.8	7.1	14.4	-9.9	14.8	3.6	0.8	7.0	5.5
Investment and saving c/	<b>Porcentajes of GDP</b>								
Gross capital formation	22.5	22.7	26.4	25.6	28.0	28.1	27.8	28.8	28.1
National saving	26.2	26.0	29.2	26.1	25.8	27.6	27.6	27.7	27.5
External saving	-3.7	-3.3	-2.9	-0.5	2.3	0.5	0.2	1.0	0.6
Balance of payments	<b>Millions of dollars</b>								
Current account balance	1,739	1,887	1,767	309	-1,586	-402	-164	-984	-602
Goods balance	1,768	1,823	1,549	144	-1,504	-303	50	-493	-67
Exports, f.o.b.	13,176	14,870	19,461	14,412	18,137	23,082	24,569	25,686	26,604
Imports, f.o.b.	11,408	13,047	17,912	14,268	19,641	23,385	24,519	26,178	26,672
Services trade balance	-1,305	-1,371	-1,571	-1,282	-1,522	-1,563	-1,391	-1,495	-1,219
Income balance	-1,828	-1,968	-1,431	-1,274	-1,041	-1,259	-1,303	-1,395	-1,579
Net current transfers	3,104	3,403	3,221	2,722	2,481	2,722	2,480	2,399	2,264
Capital and financial balance d/	-1,870	-500	-833	-2,957	374	674	-418	2,830	177
Net foreign direct investment	271	194	1,058	308	166	644	585	731	774
Other capital movements	-2,141	-694	-1,891	-3,264	208	31	-1,003	2,099	-597
Overall balance	-131	1,387	934	-2,647	-1,212	272	-582	1,846	-424
Variation in reserve assets e/	124	-1,497	-952	681	1,170	-336	475	-1,878	411
Other financing	7	111	18	1,966	42	64	107	32	13
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	101.3	106.9	108.6	100.9	99.9	102.3	98.4	96.7	93.6
Terms of trade for goods (index: 2010=100)	91.0	93.5	102.6	90.8	100.0	110.0	111.7	113.1	112.9
Net resource transfer (millions of dollars)	-3,691	-2,138	-2,246	-2,264	-625	-522	-1,614	1,467	-1,389
Total gross external debt (millions of dollars)	17,099	17,445	16,900	13,514	13,914	15,210	15,913	18,801	24,296
Employment	<b>Average annual rates</b>								
Labour force participation rate g/	59.1	61.3	67.7	66.3	64.2	62.2	62.8	61.8	62.2
Unemployment rate g/	8.1	7.4	6.9	8.5	7.6	6.0	4.9	4.7	5.1
Visible underemployment rate h/	6.3	11.3	11.9	12.6	12.1	9.8	8.2	8.9	9.3

Table 1 (concluded)

	2006	2007	2008	2009	2010	2011	2012	2013	2014 a/
<b>Prices</b>	<b>Annual percentages</b>								
Variation in consumer prices (December-December)	2.9	3.3	8.8	4.3	3.3	5.4	4.2	2.7	3.7
Variation in producer prices (December-December)	7.2	18.2	-28.3	33.0	16.7	12.5	-3.4	3.8	-19.1
Variation in minimum real wage	3.3	3.9	8.5	3.6	6.4	5.2	5.2	6.1	3.2
Nominal deposit rate i/	4.4	5.3	5.5	5.4	4.6	4.6	4.5	4.5	4.9
Nominal lending rate j/	8.9	10.1	9.8	9.2	9.0	8.3	8.2	8.2	8.1
<b>Central government</b>	<b>Percentajes of GDP</b>								
Total revenue	14.7	16.6	22.3	18.5	21.7	21.7	22.3	21.6	20.3
Tax revenue	9.1	9.3	10.6	11.6	12.6	12.3	14.0	14.5	14.4
Total expenditure	14.9	16.8	23.3	22.7	23.3	23.3	24.2	27.4	26.6
Current expenditure	11.4	11.6	13.7	14.3	14.1	13.1	13.7	15.1	14.9
Interest	2.0	1.8	1.3	0.8	0.8	0.8	0.9	1.2	1.4
Capital expenditure	3.6	5.2	9.6	8.5	9.2	10.1	10.5	12.3	11.7
Primary balance	1.8	1.7	0.3	-3.5	-0.9	-0.7	-1.0	-4.5	-5.0
Overall balance	-0.2	-0.1	-1.0	-4.2	-1.6	-1.6	-2.0	-5.8	-6.4
Central government public debt	26.5	25.2	20.6	14.9	17.8	17.3	20.2	23.1	27.8
Domestic	7.0	6.4	5.9	4.5	6.7	5.7	8.9	10.5	12.5
External	19.5	18.8	14.7	10.4	11.1	11.6	11.3	12.6	15.4
<b>Money and credit</b>	<b>Percentages of GDP, end-of-year stocks</b>								
Domestic credit	15.3	16.1	15.3	17.3	22.1	23.6	25.9	27.8	30.1
To the public sector	-6.0	-6.2	-7.9	-5.9	-2.8	-3.1	-1.7	-0.5	1.1
To the private sector	21.3	22.3	23.2	23.2	24.8	26.7	27.7	28.4	29.0
Monetary base	...	8.9	9.9	11.1	10.7	10.6	11.5	13.5	14.7
M2	...	21.8	27.1	29.0	31.2	32.5	34.5	36.2	38.8

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 2007 prices.

c/ Estimates based on figures denominated in dollars at current prices.

d/ Includes errors and omissions.

e/ A minus sign (-) indicates an increase in reserve assets.

f/ Annual average, weighted by the value of goods exports and imports.

g/ Urban total.

h/ Urban total. Up to 2006, the figures relate to Cuenca, Guayaquil and Quito

i/ Weighted average of the system effective deposit rates. Up to July 2007, reference deposit rate in dollars.

j/ Effective benchmark lending rate for the corporate commercial segment. Up to July 2007, reference lending rate in dollars.



Table 2  
ECUADOR: MAIN QUARTERLY INDICATORS

	2013				2014				2015	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Gross domestic product (variation from same quarter of preceding year) b/	3.6	4.1	5.6	5.2	4.3	3.8	3.7	3.5	3.0	...
Gross international reserves (millions of dollars)	3,804	4,204	4,137	4,206	4,164	4,467	6,139	5,272	3,680	4,004 c/
Real effective exchange rate (index: 2005=100) d/	97.6	96.8	96.4	96.0	94.4	95.2	94.2	90.7	86.5	86.2 c/
Consumer prices (12-month percentage variation)	3.5	2.9	2.1	2.3	3.0	3.4	4.1	3.8	3.8	4.4 c/
Wholesale prices (12-month percentage variation)	-1.9	-0.8	5.3	2.0	1.2	4.7	-2.7	-11.3	-24.1	-19.2 c/
Nominal interest rates (average annualized percentages)										
Deposit rate e/	4.5	4.5	4.5	4.5	4.5	4.9	5.0	5.1	5.3	5.4 f/
Lending rate g/	8.2	8.2	8.2	8.2	8.2	8.0	8.1	8.2	7.5	8.3 c/
Interbank rate	0.5	0.7	0.8	0.8	0.8	0.8	0.8	0.9	1.3	1.8 f/
Sovereign bond spread, Embi + (basis points to end of period) h/	700	665	628	530	508	376	484	883	865	824
Stock price index (national index to end of period, 31 December 2005 = 100)	138	140	142	148	152	156	161	168	169	173
Domestic credit (variation from same quarter of preceding year)	15.5	17.2	16.7	17.4	20.2	19.4	12.1	13.7	14.5	11.7 f/
Non-performing loans as a percentage of total credit	4.9	4.6	4.5	4.4	4.6	4.7	4.6	4.5	4.6	4.5 f/

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 2007 prices.

c/ Figures as of May.

d/ Quarterly average, weighted by the value of goods exports and imports.

e/ Weighted average of the system effective deposit rates.

d/ Figures as of April.

g/ Effective benchmark lending rate for the corporate commercial segment.

h/ Measured by J.P.Morgan.