ECUADOR

1. General trends\

Economic activity in Ecuador —already lacklustre in 2017— was even more sluggish in 2018, with GDP growing by 1.4%, compared to 2.4% in 2017. Demand, supply and external factors all contributed to the downturn. The lack of buoyancy on the supply side was partly due to scant competitiveness in costs, which sustained increases in productivity were not able to offset. On the external front, while remittances did bolster income and internal consumption, the trend in oil prices —which are still well below those of five years ago— and the high cost of external loans greatly limited fiscal sustainability. As for the components of aggregate demand, both household and government consumption slowed, as did gross fixed capital formation. Exports proved to be the exception, in that they increased slightly (by 0.9% in 2018, compared to 0.7% in 2017). However, the goal —which was ultimately met— of narrowing the primary fiscal deficit (-5.8%, -3.2% and 1.3% in 2016, 2017 and 2018, respectively, in the non-financial public sector) was partly achieved thanks to a substantial reduction in public capital expenditure (27% in 2018, following declines of 12% in 2017 and 0.2% in 2016), contributing to lower growth in aggregate investment in 2018. Primary current expenditure expanded by 16%, principally due to increased purchases of goods and services. In addition to the progress in reducing the primary fiscal deficit, other measures were needed to resume a steady path of debt sustainability. To that end, the government negotiated and then signed an extended arrangement with the International Monetary Fund (IMF) at the beginning of 2019 that would allow it a more comfortable margin in servicing debt, which needed to be trimmed to more sustainable levels. The withdrawal of fiscal stimulus, an international outlook that does not presage any major changes for Ecuador and the maintenance of supply conditions for the short term suggest that GDP growth will be close to zero in 2019; most likely 0.2%.

2. Economic policy

Economic policy in 2018 focused on three main goals: stimulating demand by increasing current fiscal spending to prevent a recession; obtaining the (foreign and domestic) financing needed to close the spending-revenue gap; and adjusting incentives to promote private sector growth. The last of these three goals entails passing the Organic Law for productive development and attraction of investments, generation of employment, stability and fiscal balance, in addition to measures specifically geared to increasing oil production over the next few years. In this regard, the tender for private sector extraction within existing oil fields and repayment of part of the debt to providers of services and inputs should enable essential maintenance work to resume.

(a) Fiscal policy

In 2018, fiscal policy managed to narrow the deficit by significantly reducing capital expenditure, reining in wage outlays and providing incentives to pay income tax. Higher oil prices, compared to the two prior years, also helped. In fact, the non-financial public sector posted its lowest overall deficit (1.2% of GDP) since 2012 and the first primary surplus (1.3%). The difference was due to high interest payments, equivalent to 2.5% of GDP.

Total expenditure was stabilized at 37.1% of GDP, by lowering capital expenditure from 9.5% of GDP in 2017 to 6.6% of GDP in 2018, thereby offsetting the hike in current expenditure, which rose from

27.6% of GDP in 2017 to 30.5% in 2018. One government objective was to curb the increase in the non-financial public sector payroll, which it managed to reduce slightly, to 9.9% of GDP in 2018 from 10.1% in 2017. The expenditures that increased most as a percentage of GDP were: “Other expenditures”, consisting mostly of purchases of oil derivatives, which increased from 5.5% to 7.5% of GDP; spending on goods and services, which rose from 4.9% to 5.7% of GDP; and, finally, interest payments, which increased from 2.1% to 2.5% of GDP. The aforementioned cut in capital expenditure by the non-financial public sector partly explains the lower growth of gross fixed capital formation in 2018 (2.1% compared to a 5.3% increase in 2017).

Income increased from the equivalent of 31.7% of GDP in 2017 to 35.8% of GDP in 2018. Contributing most to that increase were: revenue from oil exports, which increased from 5.7% to 8.0%, and income tax revenue, which increased from 3.7% to 4.4%. Particularly important for the latter increase was the tax amnesty approved in June 2018, which waived fines and interest on past-due income tax. As regards tax revenue, prices for oil exported by Ecuador (Oriente-Napo varieties) were higher, at US$ 61 per barrel in 2018 (compared to US$ 46 in 2017 and US$ 35 in 2016), more than offsetting the 2.7% decline in oil output in 2018.

The overall deficit narrowed from 5.4% of GDP in 2017 to 1.2% of GDP in 2018. Under the commitments entered into with IMF at the beginning of 2019, the goal is to eliminate the overall deficit in 2019 and achieve a surplus of 3.8% in 2020, which would entail reducing total expenditure from 37.1% to 35.2% of GDP in 2019 and to 34.6% of GDP in 2020, assuming that revenue projections for those years materialize. Achieving those goals poses a challenge: after five years of cuts, there is now less room to reduce capital expenditure, which was the chief means of curbing expenditure in 2018.

As in prior years, non-financial public sector debt increased, albeit at a slower pace. In December 2018, it was equivalent to 45.6% of GDP, compared to 44.6%, 38% and 33% in the three preceding years. The breakdown of the public debt, at December 2018, was 72% foreign debt and 28% domestic debt. One change introduced in the Organic Law for productive development and attraction of investments, generation of employment, stability and fiscal balance, published on August 21, was the ban on financing fiscal expenditure with central bank funds, which imposes greater discipline when it comes to spending.

(b) Monetary and exchange-rate policy

There were no major shifts in monetary policy during this period: the money supply continued to grow at a slower pace (up 3%, in the case of M1, and 5.7% in the case of M2 in 2018, compared to 8.4% and 10%, respectively, in 2017). As is to be expected in a dollarized economy, interest rates rose in response to interest rate hikes in the United States, as a result of the policy pursued by the Federal Reserve in that country, which is geared to gradually normalizing interest rates.

International reserves stayed at levels similar to previous years, fluctuating around an average of US$ 3.652 billion (equivalent to approximately one and a half months of imports): a figure similar to the average recorded since 2009.

The authorities have announced that the dollarization regime will be kept and strengthened, so that a devaluation remains out of the question and other ways of enhancing the competitiveness of domestic output will be needed. What is more, one of the explicit objectives of the arrangement with IMF is to continue and reinforce dollarization for the foreseeable future.

(c) Other policies

An extended arrangement was signed by Ecuador and IMF at the beginning of 2019. This arrangement includes the possibility of accessing up to US$ 4.20 billion in three years, mainly in order to reduce indebtedness to sustainable levels by providing the liquidity that the country needs to restructure its liabilities appropriately and to support a fiscal consolidation plan through the reduction and reallocation of expenditure, including support measures to mitigate the social impact of the adjustment. In addition to supporting and fostering greater fiscal austerity, the arrangement seeks to reinforce macrofinancial stability and enhance competitiveness in the Ecuadorian economy. With respect to macrofinancial stability, a series of measures are proposed for institutional strengthening of the central bank and more than doubling average holdings of international reserves. As regards enhancing competitiveness, the idea is to rationalize the use of subsidies, rein in salary increases and allow greater operational flexibility in the labour market; hence the importance of taking steps to mitigate the social impact.

Towards the end of May, IMF technical staff recommended authorizing a second disbursement in the amount of US$ 250 million, on top of the US$ 620 million authorized when the arrangement was first announced.

These signals have put Ecuador in a better position to restructure its debt by lowering the cost of refinancing, as recently seen with the sovereign bonds maturing in 2020, which Ecuador repurchased and replaced with bonds maturing in 2029 at rates below those it had previously been able to obtain.

In addition to the US$ 4.20 billion from IMF, the government managed to obtain financial support from other multilateral organizations, such as the Inter-American Development Bank (IDB), the World Bank, the Latin American Reserve Fund (FLAR), the European Investment Bank (EIB) and the French Development Agency (AFD) in the amount of US$ 6.0 billion, more than in previous years. Nevertheless, the fiscal targets agreed with IMF are ambitious and the short-term impact on economic activity and employment is likely to be significant.

3. The main variables

(a) The external sector

The balance of payments deteriorated in 2018, with exports growing just 0.9% (0.7% in 2017) and imports growing at a much slower rate of 5.8% in real terms (compared to 12.2% in 2017). In current value terms, nevertheless, growth was more buoyant, with the total value of goods exports increasing by 12% over the prior year. Most of that pick-up came from oil exports, which, measured in dollars, grew by 27%, compared to the 5% growth of non-oil exports. Explaining the increase was the improved average price for Ecuadorian crude in 2018, which, despite fluctuating, was substantially higher than in 2017 (the Oriente-Napo basket price was US$ 61 in 2018 and US$ 46 in 2017). The shrimp sector contributed most to the growth of non-oil exports. Imports increased by 15.9%, outweighing the increase in the value of exports. Much of the increase occurred in imports of inputs, followed by imports of consumer goods and, to a much lesser extent, of capital goods (20.4%, 13.7% and 11.3%, respectively), a scenario consistent with the slowdown in investment.

The negative foreign trade balance is also consistent with the path followed by the (2014 base-year) real effective exchange rate, which began 2018 with an index of 92.6 and stayed high until April, but fell over the rest of the year to close at 89.5.

The current account deficit at the end of 2018 was US$ 1.358 billion, almost triple the prior-year deficit (US$ 481 million). Only the services balance improved, with its deficit down to US$ 700 million (from US$ 1.2 billion), thanks to increased revenue from tourism. In addition to the deterioration in the goods balance, the income and transfers balances also worsened. The deficit on the income account increased by 18.7% compared to 2017, mainly because of a 19.5% increase in investment income payments. The downturn in the transfers balance (with a surplus 9.6% lower than in 2017) occurred despite a moderate 6.7% increase in remittances to the country, driven by upbeat growth in the United States, which were not enough to offset the marked increase in non-governmental remittances out of Ecuador. In fact, remittances to the rest of the world increased by 26.8% over 2017. More than three-quarters (77.3%) of the outflows stemmed from remittances by Peruvian, Colombian and Chinese citizens.

(b) Economic activity

The 1.4% growth of GDP in 2018, comprising a 4% annual decline in the gross value added of oil exports and an increase of 2% in the non-oil gross value added, occurred against a backdrop of lacklustre aggregate demand, barely stimulated by a real-terms increase of 2.9% in public consumption expenditure, 2.7% in household expenditure, 2.1% in investment goods and a meagre 0.9% up-tick in exports. This insipid growth in expenditure was accompanied by very mixed sectoral output, where the fastest growing sectors were aquaculture and shrimp fishing, social and health services, and accommodation and food services (which grew by 8.6%, 4.3% and 4.0%, respectively), while the poorest performers were oil refining, fishing (excluding shrimp) and the oil and mining sector, which fell by 10%, 3.5% and 2.9%, respectively. Two traditionally important sectors for employment, commerce and construction, posted moderate real-terms growth in 2018 (3.1% and 0.6%, respectively).

The oil sector is likely to undergo marked fluctuations again in 2019. One key question is how long the stoppages at the Esmeraldas refinery will last, given their impact on derivatives output. The first scheduled shut-down was already extended for another 60 days, which suggests that the contraction in refining will be more severe than the Central Bank of Ecuador projected (a 9.8% drop in 2019). As for crude oil extraction, the current quota of 520,000 barrels/day agreed on with the Organization of the Petroleum Exporting Countries (OPEC) is still above the effective average for 2018 (516,000 barrels per day (bpd)), although an agreement is likely to be reached to increase the quota to 535,000 bpd, considering, among other factors, lower output from the Bolivarian Republic of Venezuela and Angola. The extra output would most likely come from the private companies that won the round of smaller oilfield tenders in 2018.

Another key factor is the impact of fiscal adjustment, since it would dampen gross fixed capital formation and general government final consumption: the components of expenditure that made the second and third largest contributions to GDP growth in 2018 (0.49% and 0.44%, respectively). Given the weight of these factors in the economy, we estimate that GDP growth in 2019 will be noticeably lower than the 1.4% posted in 2018, and its value would be 0.2%.

(c) Prices, wages and employment

In 2018, Ecuador experienced a third consecutive year of very small increases or drops in the aggregate price level. Measured by the consumer price index (CPI), in the year cumulative inflation was 0.3% (-0.2% in 2017 and 1.1% in 2016). Cumulative inflation through May 2019 was 0.2%, double that for the prior-year period. However, the anticipated fiscal adjustment is likely to exert downward pressure on that trend. The prior-year tendency is being repeated, in the sense that the food and non-alcoholic beverages segment is driving prices lower. However, the recent increase in transport prices, triggered by the rise in the international oil price, is pushing in the other direction.

The slight trend toward a decline in the quality of employment has continued. Indeed, the percentage of adequate or full employment nationwide was 40.6% in December 2018, below the 42.3% of December 2017, and March 2019 figures confirm the trend. On the positive side, the (national total) unemployment rate remains low (3.7% in December 2018, compared to 4.6% in December 2017).

Several indicators point to a very modest increase in wages in 2018. The unified basic wage rose by 2.9% in 2018, while average real wages in the private sector posted a 2.7% hike, according to Ministry of Labour data. Thirdly, according to National Institute of Statistics and Censuses (INEC) data published in March 2018, for all employees (wage earners and independent workers) the annual average monthly wage —that is to say, the average of the measurements taken in March, June, September, and December— was 1.8% higher in 2018 than in 2017 (US$ 344 a month, compared to US$ 338). Broken down by gender, that increase is mostly found among women, whose annual average wage increased by 4.1%, compared to 0.6% for men. Despite that, a comparison of these annual averages still shows a considerable ongoing wage gap in favour of men in 2018: US$ 371 compared to US$ 300 a month, slightly less of a gap than in 2017 (US$ 369 for men, compared to US$ 288 for women).

Table 1
ECUADOR: MAIN ECONOMIC INDICATORS

	2010	2011	2012	2013	2014	2015	2016	2017	2018 a/
	Annual growth rates b/								
Gross domestic product	3.5	7.9	5.6	4.9	3.8	0.1	-1.2	2.4	1.4
Per capita gross domestic product	1.8	6.2	4.0	3.3	2.2	-1.4	-2.7	0.9	0.0
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	0.7	7.9	0.8	6.7	7.6	2.9	0.9	5.5	3.2
Mining and quarrying	0.1	2.8	2.6	2.9	6.6	-2.1	1.5	-2.8	-2.9
Manufacturing	2.4	6.4	4.1	2.2	0.2	-0.8	-0.9	3.6	0.0
Electricity, gas and water	34.5	27.1	17.9	11.5	6.5	9.0	0.5	9.6	3.5
Construction	3.4	17.6	12.2	7.4	4.7	-0.8	-5.8	-4.4	0.6
Wholesale and retail commerce, restaurants and hotels	3.5	5.8	4.6	6.5	3.3	-1.1	-3.5	5.5	3.3
Transport, storage and communications	5.4	7.7	7.0	8.9	3.5	2.6	0.6	0.4	1.5
Financial institutions, insurance, real estate and business services	2.7	6.5	5.0	1.6	5.1	0.5	-1.9	-1.1	0.6
Community, social and personal services	5.6	7.1	6.6	4.9	4.1	2.5	0.5	2.2	2.5
Gross domestic product, by type of expenditure									
Final consumption expenditure	7.2	5.7	4.2	5.0	3.5	0.3	-2.0	0.0	3.6
Government consumption	4.4	8.7	11.1	10.3	6.7	2.1	-0.2	3.2	2.9
Private consumption	7.7	5.1	2.9	3.9	2.7	-0.1	-2.4	3.7	2.7
Gross capital formation	10.5	11.5	4.2	9.5	3.4	-9.2	-11.5	-11.7	11.7
Exports (goods and services)	-0.2	5.7	5.5	2.6	6.2	-0.6	1.4	0.7	0.9
Imports (goods and services)	14.8	3.6	0.8	7.0	4.8	-8.2	-9.6	12.2	5.8
Investment and saving c/	**Percentages of GDP**								
Gross capital formation	28.0	28.1	27.8	28.5	28.3	26.9	25.0	23.9	25.3
National saving	25.8	27.6	27.6	27.5	27.6	24.6	26.3	23.5	24.0
External saving	2.2	0.5	0.2	1.0	0.7	2.2	-1.3	0.5	1.3
Balance of payments	**Millions of dollars**								
Current account balance	-1 565	-400	-153	-944	-678	-2 223	1 324	-481	-1 358
Goods balance	-1 504	-303	50	-529	-63	-1 650	1 567	311	-263
Exports, f.o.b.	18 137	23 082	24 569	25 587	26 596	19 049	17 425	19 618	22 123
Imports, f.o.b.	19 641	23 385	24 519	26 115	26 660	20 699	15 858	19 307	22 386
Services trade balance	-1 522	-1 563	-1 394	-1 420	-1 171	-805	-1 054	-1 103	-710
Income balance	-1 019	-1 257	-1 289	-1 372	-1 552	-1 731	-1 843	-2 354	-2 794
Net current transfers	2 481	2 722	2 480	2 376	2 108	1 963	2 654	2 665	2 409
Capital and financial balance d/	352	672	-429	2 790	253	734	-117	-1 377	1 266
Net foreign direct investment	166	644	567	727	772	1 322	767	618	1 401
Other capital movements	187	28	-996	2 063	-519	-588	-885	-1 996	-135
Overall balance	-1 212	272	-582	1 846	-424	-1 489	1 207	-1 859	-92
Variation in reserve assets e/	1 170	-336	475	-1 878	411	1 453	-1 763	1 808	-225
Other financing	42	64	107	32	13	36	556	51	317
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	99.4	102.1	98.1	96.4	93.3	85.1	83.8	87.4	85.7
Terms of trade for goods (index: 2010=100) g/	100.0	112.4	112.1	113.2	106.7	80.0	75.7	83.5	93.1
Net resource transfer (millions of dollars)	-625	-522	-1 611	1 450	-1 286	-961	-1 404	-3 681	-1 211
Total gross external debt (millions of dollars)	13 914	15 210	15 913	18 744	24 115	27 813	34 181	40 397	44 296
Employment	**Average annual rates**								
Labour force participation rate h/	62.5	62.5	61.7	62.1	63.2	66.2	68.2	68.8	67.0
Unemployment rate i/	7.6	6.0	4.9	4.7	5.1	5.4	6.8	5.6	5.2
Open unemployment rate j/	6.1	5.0	4.2	4.0	4.3	4.7	5.9	5.0	4.7
Visible underemployment rate h/	12.1	9.1	7.9	9.9	10.6	11.7	15.7	17.0	15.4

Table 1 (concluded)

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Prices	**Annual percentages**								
Variation in consumer prices (December-December)	3.3	5.4	4.2	2.7	3.7	3.4	1.1	-0.2	0.3
Variation in producer prices (December-December)	6.9	3.1	2.0	3.1	3.1	-0.7	1.7	0.4	-1.1
Variation in minimum real wage	6.4	5.2	5.2	6.1	3.2	0.2	1.6	2.0	3.2
Nominal deposit rate k/	4.6	4.6	4.5	4.5	4.9	5.3	5.7	4.9	5.1
Nominal lending rate l/	9.0	8.3	8.2	8.2	8.1	8.3	8.7	7.9	7.7
Central government	**Percentages of GDP**								
Total revenue	21.7	21.7	22.2	21.4	20.0	20.5	18.6	17.4	18.7
Tax revenue	12.6	12.3	13.9	14.4	14.2	15.7	14.0	13.5	14.2
Total expenditure	23.3	23.3	24.2	27.2	26.3	24.3	24.1	23.3	22.3
Current expenditure	14.1	13.1	13.6	15.0	14.7	14.6	14.5	15.0	15.9
Interest	0.8	0.8	0.9	1.2	1.4	1.8	1.9	2.4	2.7
Capital expenditure	9.2	10.1	10.5	12.2	11.6	9.7	9.6	8.3	6.4
Primary balance	-0.9	-0.7	-1.0	-4.5	-4.9	-2.1	-3.6	-3.5	-0.9
Overall balance	-1.6	-1.6	-2.0	-5.7	-6.3	-3.8	-5.6	-5.9	-3.6
Central government public debt	17.8	17.3	20.1	22.9	27.5	30.9	35.7	41.3	42.6
Domestic	6.7	5.7	8.8	10.4	12.3	12.6	12.5	14.2	12.5
External	11.1	11.6	11.2	12.5	15.2	18.3	23.2	27.1	30.1
Money and credit	**Percentages of GDP, end-of-year stocks**								
Domestic credit	22.1	23.6	25.8	27.6	29.8	29.9	34.4	36.4	38.6
To the public sector	-2.8	-3.1	-1.7	-0.5	1.1	1.5	4.5	3.0	1.7
To the private sector	24.8	26.7	27.6	28.2	28.7	28.4	29.9	33.4	36.9
Monetary base	10.7	10.6	11.4	13.4	14.5	16.7	21.3	21.3	21.0
M2	31.2	32.5	34.4	35.9	38.3	38.4	44.5	46.9	47.8

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/ Nationwide total
h/ Urban Total. Includes hidden unemployment.
i/ Includes an adjustment for workforce figures due to exclusion of hidden unemployment.
j/ Weighted average of the system effective deposit rates. Up to July 2007, reference deposit rate in dollars.
k/ Effective benchmark lending rate for the corporate commercial segment. Up to July 2007, reference lending rate in dollars.

Table 2
ECUADOR: MAIN QUARTERLY INDICATORS

	2017				2018				2019	
	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/	1.7	2.1	2.9	2.8	1.8	1.4	1.5	0.8	...	...
Gross international reserves (millions of dollars)	4 491	3 498	3 425	3 759	5 327	3 726	2 957	2 596	3 630	3 786 c/
Real effective exchange rate (index: 2005=100) d/	85.0	86.1	88.4	89.9	88.6	86.8	84.2	83.3	83.4	84.0 c/
Consumer prices (12-month percentage variation)	1.0	0.2	0.0	-0.2	-0.2	-0.7	0.2	0.3	-0.1	0.4 c/
Wholesale prices (12-month percentage variation)	-2.7	-1.0	-1.2	1.3	2.6	2.4	0.8	-1.1	-0.9	0.5 c/
Nominal interest rates (average annualized percentages)										
Deposit rate e/	5.0	4.8	4.9	4.9	5.0	5.0	5.2	5.3	5.7	5.7 c/
Lending rate f/	8.1	7.7	8.0	7.8	7.5	7.2	7.7	8.5	8.5	8.6 c/
Interbank rate	1.9	1.5	1.1	0.9	0.9	1.0	1.3	1.3	1.3	1.3 c/
Sovereign bond spread, Embi + (basis points to end of period) g/	666	706	606	459	544	761	622	826	592	619 c/
Stock price index (national index to end of period, 31 December 2005 = 100)	159	171	179	185	188	196	204	202	201	201
Domestic credit (variation from same quarter of preceding year)	16.0	15.2	11.2	6.4	3.1	10.1	13.7	14.7	15.7	10.9 h/

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.
f/ Effective benchmark lending rate for the corporate commercial segment.
g/ Measured by J.P.Morgan.
h/ Figures as of April.

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