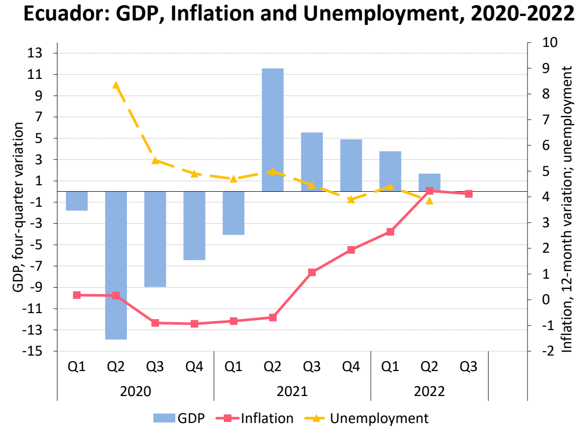
Ecuador

Since the sharp contraction in the second quarter of 2020, the Ecuadorian economy has been recovering more slowly than other countries in the region, but also more slowly than it did after previous crises, such as those of 2008 and 2015. In view of this, the Economic Commission for Latin America and the Caribbean (ECLAC) estimates that the country's GDP will grow by 2.7% in 2022 (compared to the 4.2% reported for 2021), to US$ 70.954 billion at constant 2007 prices, according to the methodology employed by the Central Bank of Ecuador. This is still below the level recorded in 2019, prior to the coronavirus disease (COVID-19) pandemic. This more sluggish economic activity is consistent with the weaker private consumption, which is the key driver of Ecuador's growth, and the limited impact of overall investment and government spending owing to fiscal policy management. The contribution of external demand has tended to be limited, with a decline in export volumes, reflecting an uneven recovery in terms of domestic supply and complex international conditions (the conflict in Ukraine and high commodity prices, including food).

In 2022, high oil prices on international markets are expected to have continued to affect the pace of the country's recovery, partly through its fiscal accounts, current account and levels of international reserves, which are tied to the domestic oil sector's production capacity. Thus, a positive overall outturn is expected for the non-financial public sector (0.4% to 0.9% of GDP) and for the oil trade balance (3.1% of GDP), as well as a notable level of international reserves (around 6.5% of GDP). However, the improvement in the oil trade balance is offset by a non-oil trade deficit (2.1% of GDP). Inflation is expected to remain high, with a year-on-year rate of close to 4.5% at year-end (1.9% in 2021). As regards unemployment, the rate should stabilize at around 4%, with an improvement closely linked to the high level of labour informality, which tends to strengthen inertia in terms of precarious working conditions and lower income. Given the worsening external conditions and the country's high degree of exposure, ECLAC projects that Ecuador's economic growth will slow more sharply in 2023, with GDP expanding by 2%.

Over the first three quarters of 2022, the non-financia l public sector maintained a surplus in nominal terms, both in the overall balance (1.9% of GDP) and in the primary balance (3.1% of GDP).[1] In light of the rise in tax revenues, particularly non-recurrent (oil) revenues, fiscal policy has aimed to contain increases in public spending, with the most significant cuts at the central government level.

Ecuador: GDP, Inflation and Unemployment, 2020-2022



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

Public revenues grew by 19%, driven by a large rise in oil revenues (31%) and an improvement in tax revenues (14%), largely in terms of value added tax (VAT), despite a recovery in income tax supported by a new tax reform (Organic Law for Economic Development and

[1] Refers to the update of estimated GDP as at September 2022 (US$ 116.010 billion).

Fiscal Sustainability). As they have become the main source of public revenues, oil resources pose complex challenges in terms of future fiscal accounts owing to their high volatility and the difficulties with expanding production of Ecuadorian crude oil.[2] In addition, part of these resources is used to finance certain recurrent expenses for key economic sectors (health and education).[3]

Ecuador: main economic indicators, 2020-2022

	2020	2021	2022 [a]
	Annual growth rate		
Gross domestic product	-7.8	4.2	2.7
Per capita gross domestic product	-9.2	2.8	1.3
Consumer prices	-0.9	1.9	4.0 [b]
Money (M1)	7.9	6.0	4.6 [c]
Real effective exchange rate [d]	-1.3	3.9	1.1 [b]
Terms of trade	-13.2	13.6	5.6
	Annual average percentage		
Open unemployment rate [e]	6.2	4.5	3.9 [f]
Central government			
Overall balance / GDP	-7.5	-3.9	...
Nominal deposit rate [g]	6.3	5.6	5.8 [b]
Nominal lending rate [h]	8.9	8.1	7.5 [b]
	Millions of dollars		
Exports of goods and services	42 992	56 561	74 681
Imports of goods and services	36 969	52 542	72 727
Current account balance	-639	-2 136	-3 081
Capital and financial balance [i]	-1 116	1 873	...
Overall balance	-1 754	-263	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
a/ Estimates.
b/ Figures as of October.
c/ Figures as of September.
d/ A negative rate indicates an appreciation of the currency in real terms. Refers to the global real effective exchange rate.
e/ Open unemployment rate includes an adjustment for workforce figures due to exclusion of hidden unemployment.
f/ Figures as of June.
g/ Benchmark deposit rate.
h/ Effective benchmark lending rate for the corporate commercial segment.
i/ Includes errors and omissions.

Public spending expanded at a lower rate, 12%, owing t o an increase in recurrent expenditure (19%) and a fall in non-recurrent expenditure (14%). Among recurrent expenditures, there was an atypical increase in expenditure on consumption of goods and services (36%), because of the high cost of imported fuels and insufficient domestic refining capacity. In view of this situation, responsibility for the Petroleum Product Deficit Financing Account (CFDD) was transferred, by presidential decree, to Empresa Pública de Hidrocarburos del Ecuador (EP PETROECUADOR) from September 2022.[4] However, recurrent expenditures remained at around 23% of GDP, at a similar level to 2019, before the pandemic, owing to the limited impact of increases in other items (wages and salaries and transfers). Non-recurrent expenditures declined because public investment was lower, particularly in the case of the central government (37%), accounting for 1.1% of GDP in the period under analysis.

With the rebound in economic activity and the improvement in the fiscal position, the ratio of public debt and other non-financial public sector liabilities to GDP hit 52.3% in September 2022, down 5.7 percentage points from the same month of 2021. This reflects the current administration’s continued efforts to improve the profile of public debt (expanded access to multilateral financing, successful renegotiation of debt with China and approval of a new liquidity line with the Federal Reserve Bank of New York). This headway on an improved debt profile is expected to continue in 2023, probably with negotiation of a new agreement with the International Monetary Fund (IMF), along with increased access to domestic debt in the wake of high external financing costs and in view of country risk (the emerging market bond index (EMBI) stood at 1,030 points, on average, between January and September 2022).[5]

[2] Oil revenues accounted for 38% of total fiscal revenues (tax collection accounted for 35% of the total). Moreover, they were responsible for a larger portion of the rise in fiscal revenues (57%) than of the increase in tax revenues (27%).
[3] See Executive Order No. 170 which covers the 2021, 2022 and 2023 fiscal years.
[4] In terms of budget execution, the initial budget for the item hydrocarbon products for domestic market was US$ 4.289 billion, with an allocated total in September 2022 of US$ 4.943 billion. The Petroleum Product Deficit Financing Account also includes bank commissions for an amount equivalent to US$ 35 million.
[5] In December 2022, the Extended Fund Facility (EFF) agreement signed in 2020 with the IMF will come to an end with a final disbursement of US$ 700 million, upon approval of the sixth review of the arrangement.

Given the feedback between the real sector and the monetary sector, total liquidity (M2) slowed from the first quarter of the year, driven by a decline in demand deposits, reflecting continued less favourable conditions for private consumption (erosion of purchasing power, slower growth in incoming remittances and insufficient adequate employment).[6] Nevertheless, it remained high, representing 63% of GDP in September 2022. This slowdown in total liquidity was accompanied by more gradual accumulation of international reserves following the sharp rise since August 2020, to leverage import costs, as well as slower growth in remittances and multilateral disbursements received.

In this situation, the falls in the financial sector's new deposits have led to a rise in the deposit rate (from 5.6% to 6.1% between January and September 2022) to encourage domestic financing, given the high cost of external financing.[7] Credit to the private sector expanded at a slower pace from the first quarter of the year, coinciding with a rise in the effective lending rate, from 7.4% in January to 8.4% in September, partly reflecting a tightening of monetary policy worldwide. This is expected to further dampen investment, employment, and the recoveries of the country's productive sectors.

As previously mentioned, economic activity slowed, as real GDP grew by just 0.9% in the first half of the year, compared to 1.8% in the second half of 2021.[8] The contribution of domestic demand has weakened because of slower growth in private consumption, which accounted for 67% of GDP, growing 1.8% (2.3 percentage points less than in the second half of 2021). The slight rebound in gross fixed capital formation (2.4%) and government spending (0.8%) was not enough to reverse this trend. Total investment is the furthest from pre-pandemic levels, owing to a continued decline in public investment and lack of a firm recovery in private investment. Meanwhile, exports of goods and services grew by 0.5% following a 0.7% drop in the second half of 2021.

Ecuador's key productive activities once again showed unevenness in their recovery, as measured by the six-month change in value added, with particularly worse performance by the manufacturing industry and agriculture (main sources of employment) and stagnation in construction (the main source of investment).[9]

Imports of goods and services grew more slowly (2.9%) than in the second half of 2021 (5.2%), as a result of the trend in external purchases of goods (4.9%), with a subsequent easing, and a sharp contraction in service imports (7.1%).

Between January and September 2022, the country consolidated its overall trade surplus (2% of GDP) in nominal terms, owing to the positive trade balance for oil (US$ 3.335 billion), despite this being offset by the non-oil balance deficit (US$ 1.205 billion), which tended to widen over the year. Goods exports performed well, growing 28% year-on-year in value, driven by sales of Ecuadorian crude oil (up 38%) and shrimp (up 54%). This contrasts with the drop in export volumes (4.2%), which implies high exposure of exportable supply to price volatility on international markets (almost 80% of the value of this supply comes from shipments of commodities). Oil exports have continued to be affected by difficulties with returning the country's hydrocarbon output to previous levels. For the period from January to September 2022, total oil production was 130 million barrels, 89% of what was produced in

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[6] Most remittances received are channelled through the banking system. Between January and June 2022, they declined by around 18% in real terms compared to the second half of 2021, as a result of lower growth prospects, higher global inflation, rising interest rates and appreciation of the dollar.
[7] Based on data from the private, popular and solidarity-based financial sector, as reported by the Central Bank of Ecuador.
[8] The social demonstrations that occurred in June 2022 caused a loss of close to 1% of GDP, according to Central Bank of Ecuador estimates. See F. Villarreal, "Estimación de pérdidas y daños ocasionados por el paro nacional de junio de 2022", 1 October 2022 [online] https://www.bce.fin.ec/index.php/publicaciones/editoriales.
[9] In the first half of 2022, gross value added remained below pre-pandemic levels in 12 of the 19 industries (unlike in the Central Bank of Ecuador figures, the oil industry is separate from mining); key sectors include agriculture, construction, education, social services, health, manufacturing, oil and transportation.

the same period of 2019. In addition, the average spread between West Texas Intermediate (WTI) oil and the Ecuadorian crude basket widened to US$ 7.9, compared to US$ 4.9 in the same period of 2021. This may reflect a loss of competitiveness, as well as a decline in product quality. In addition, with the recent strengthening of the dollar, the real exchange rate has tended to appreciate, and the real exchange rate index (base year 2014) fell from 93.5 to 91.7.

Imports of goods increased both in volume (5.5%) and value (33%), which is explained by the impact of high costs linked to external purchases of fuel (44%) and raw materials (30%) driven by international conditions and the global pattern in inflation. This trend is therefore expected to slow, owing to a weakening of private consumption and economic activity.

In these circumstances, domestic inflation remained high —especially for a dollarized economy— with a variation of 4.1% in the consumer price index (CPI) in September 2022, compared to 1.1% in the same month of 2021.[10] Notably, transport, which exhibited a sustained increase in its price level from May 2021 onward, contributed less to inflation following the government measures to alleviate inflationary pressure from fuel price rises. However, food and non-alcoholic beverages have recently become more prominent, showing a rise of 7.2% in September 2022, compared to 0.4% in the same month of 2021, the highest value recorded since 2016. In terms of labour indicators, the unemployment rate stabilized, and in September 2022, stood at 4.1% of the economically active population. The unemployment rate was higher in urban areas and for women, reflecting structural rigidities. Notably, 52.1% of the employed population is in the informal sector. Full or adequate employment in the formal sector stood at just 28.9% of the economically active population, still below the pre-pandemic level recorded in September 2019 (30.7%). Average labour income stood at US$ 463 (constant December 2021 dollars) in September 2022 (compared to US$ 551 in January). Although inflation in Ecuador remains moderate compared to most countries in the region, the loss of purchasing power is not felt equally across the population, as the most vulnerable people spend a larger proportion of income covering food and energy needs, meaning that inequalities and poverty tend to grow.

In a context of worsening international conditions, ECLAC projects a more pronounced slowdown in economic growth for Ecuador in 2023, with GDP expanding by 2%. The projection is based on risks of external origin (uncertain outcome of the war in Ukraine, lower expected global growth and weaker trade outlook, tightening of monetary policy, persistent inflationary pressure, restricted external financing conditions and strengthening of the dollar) and internal origin (weakening of private consumption, low investment, problems in key production sectors, including oil, shortage of quality jobs and social instability).

[10] Another indicator of inflation, the producer price index (PPI) rose 7.45% year-on-year, with an increase of 5.2 percentage points compared to September 2021, and an average rate of 6.8% for the period from January to September.