Ecuador

1. General trends

The Ecuadorian economy grew by 2.7% in 2003, and a further 5.5% expansion is predicted for 2004, based almost exclusively on increased private-sector oil extraction. Nonetheless, the employment situation in 2004 is expected to be similar to what it was in 2003, with no improvement in sight.

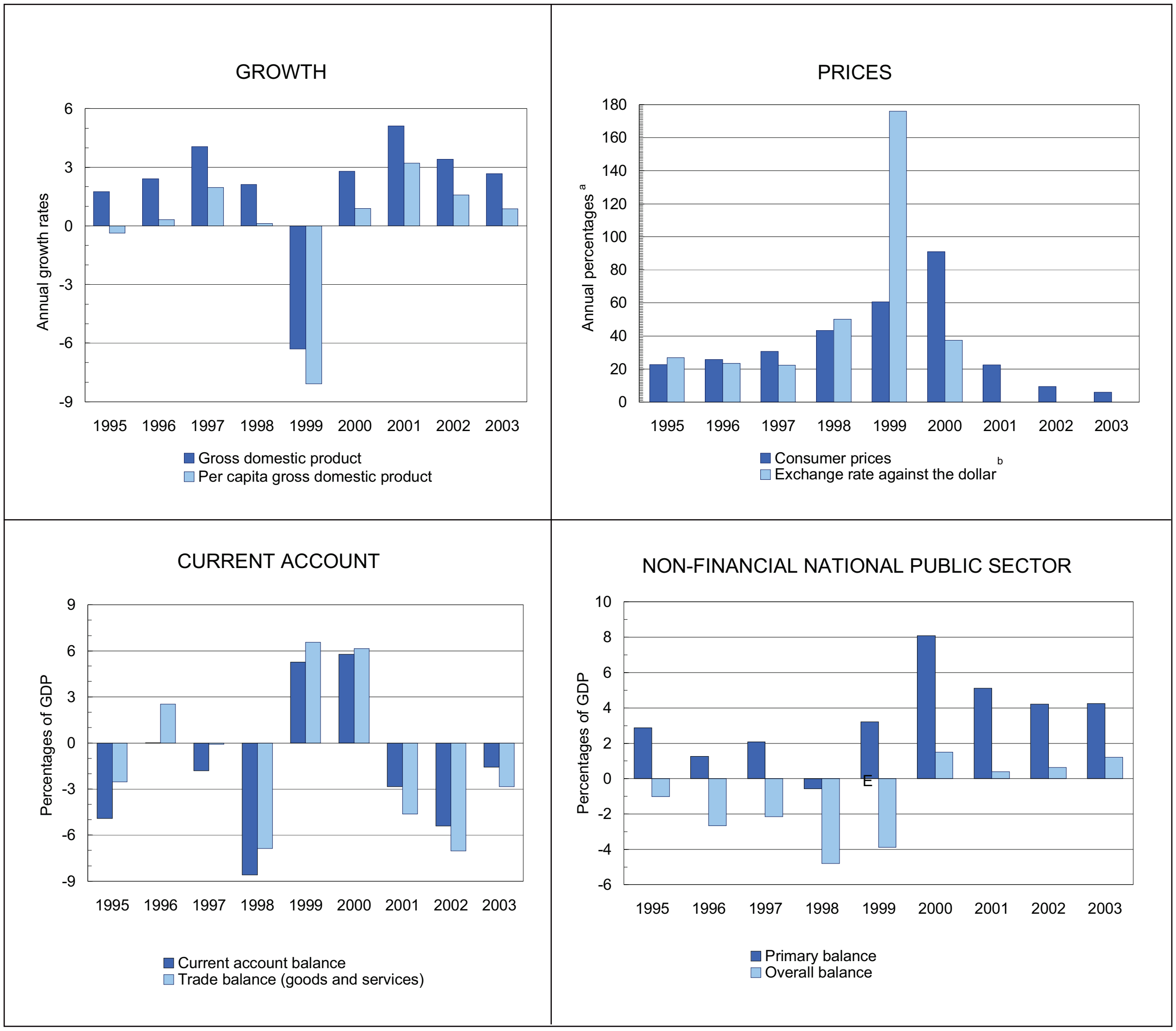
The government has striven to keep fiscal policy under control, but with ambiguous results. On the one hand, fiscal surpluses have been achieved and some necessary reforms have been implemented –such as unification of public-sector wages; on the other hand, wages and other current expenditures have systematically increased their share of the budget, while State enterprises involved in the oil, electricity and telephone sectors continue to perform far below par in terms of meeting the standards of efficiency needed to underpin sustained economic development. Public debt also remains high.

Deposit growth in the financial sector has not led to a comparable increase in lending to local firms (especially small and medium-sized enterprises), while private banks have significantly increased the proportion of assets that they hold abroad. This fact, compounded by high country risk, should help to explain the high cost of credit in Ecuador.

Inflation abated further in 2003, falling to an annual rate of 2.9% in June 2004. The lowering of inflation since dollarization, together with the widespread nominal depreciation of the dollar against other currencies, contributed to a slight depreciation of Ecuador's real effective exchange rate during the period, although it remains at relatively low levels (appreciation) in historical terms.

The external sector has strengthened thanks to increased crude-oil exports and soaring prices for this product on international markets. External accounts were also favoured by the small increase in imports, reflecting weak growth in the non-petroleum sector and completion of the Heavy Crude Oil Pipeline (OCP). An even greater improvement in the external position is expected in 2004, thanks to increased oil production, although the country's increasing dependence on oil is a risk factor for the future.

Figure 1
ECUADOR: MAIN ECONOMIC INDICATORS



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] December-December variation.
[b] As of January 2000, the United States dollar was adopted as the country's official currency.

2. Economic policy

Economic policy in 2003 was mainly aimed at fulfilling the requirements set out in the stand-by arrangement signed with the International Monetary Fund (IMF) in March of that year. Although the agreement's fiscal targets were nearly achieved thanks to the government's efforts to maintain fiscal austerity, several of the reforms that had been agreed upon remained pending when the arrangement expired in April 2004, mainly for political reasons. These reforms include putting public telecommunications and electricity distribution firms under private management, together with tax reform and the liquidation of financial institutions that had been closed since the 1999 crisis. On the external front, Ecuador, like Colombia and Peru, is in the process of negotiating a bilateral free trade agreement with the United States.

(a) Fiscal policy

In 2003, the primary surplus of the non-financial public sector (NFPS) came in at 4.8% of GDP, while the overall surplus was 1.7%. Although this represented an improvement on the corresponding figures for 2002,[1] the 2003 stand-by arrangement with IMF envisaged a primary NFPS surplus of 5.2% of GDP. The central government primary surplus amounted to 2.7% of GDP in 2003, while the overall deficit was 0.4% of GDP.

On the expenditure side, central government wage payments grew by 11.5% in nominal terms, i.e., by over twice as much as total expenditure, thereby raising their share of total budgeted expenditure to 37% (6.9% of GDP). The income side was boosted by an 11.4% expansion in income tax receipts and a 14.6% increase in oil revenues, while VAT receipts grew by just 3.5% (despite a 2.7% expansion in output, and consumer price inflation of 6.1%). Admittedly, almost half the GDP increase came from the oil sector, which has less of an impact on VAT than other sectors of the economy, since 60.6% of the crude oil extracted in 2003 was exported.

In October 2003, Congress passed the Civil Service, Administrative Career and Public-Sector Wages Unification and Standardization Act with a view to cutting the wage bill and reducing the number of grades in the salary scale, on a standardized basis across the different public-sector bodies. The government has not yet carried out a tax reform to eliminate the earmarking of a large part of tax revenues.

For 2004, the revised tax base envisages a primary NFPS surplus equivalent to 5% and an overall surplus equivalent to 2.3% of GDP. The targets proposed for the central government are a primary surplus equivalent to 2.1% and an overall deficit of 0.8% of GDP. There are additional contingent expenditures, however, such as those associated with a suit that has been brought by private oil companies seeking reimbursement from the state of value added tax.[2] Central government borrowing requirements are expected to be covered mainly through domestic borrowing –especially from the Ecuadorian Social Security Institute (IESS), which can invest up to 50% of its assets in the public sector– and, to a lesser extent, through external funding from multilateral organizations. Nevertheless, the pension increases approved in 2004 could reduce the volume of funds available to the IESS for the purchase of public securities. It is unlikely that Ecuador will return to international capital markets this year, given the rise in interest rates in the United States, the high level of country risk (886 basis points on average in June 2004), and the low risk-rating of the Ecuadorian external debt. All of this would undoubtedly make external borrowing very costly in comparison to domestic financing.

The government is expected to use the resources accumulated in the Fund for Stabilization, Social and Productive Investment and Reduction of Public Debt (FEIREP) to redeem public debt instruments, with the dual purpose of reducing country risk and relieving the heavy fiscal burden imposed by interest payments, which amounted to 3.1% of GDP in 2003.[3] Projections indicate

1 Both balances include US$ 130 million (0.5% of GDP) which the Office of the Under-Secretary of the Treasury "de-allocated" from central government expenditure in 2003.

2 A judgement in favour of an oil company was handed down in July by an international arbitration tribunal.

3 This fund consists of the proceeds of heavy crude sales corresponding to the State's share in private oil production. The act establishes that 70% of the monies accumulated in the fund must be used to buy back public debt.

Table 1
ECUADOR: MAIN ECONOMIC INDICATORS

	1995	1996	1997	1998	1999	2000	2001	2002	2003 [a]
	Annual growth rates [b]								
Gross domestic product	1.7	2.4	4.1	2.1	-6.3	2.8	5.1	3.4	2.7
Per capita gross domestic product	-0.4	0.3	2.0	0.1	-8.1	0.9	3.2	1.6	0.9
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	3.7	7.6	10.0	-3.0	9.1	-0.1	0.7	7.2	1.5
Mining	2.1	0.8	-1.9	-1.6	1.4	8.0	1.7	-3.5	6.5
Manufacturing	-1.4	-2.8	8.5	8.3	-23.5	-32.4	20.8	-0.3	9.2
Electricity, gas and water	-18.8	11.9	6.8	8.5	23.0	2.6	4.6	2.4	-3.0
Construction	0.4	1.3	2.7	-0.2	-24.9	18.3	4.0	14.7	0.5
Wholesale and retail commerce, restaurants and hotels	0.2	5.2	4.4	1.1	-11.3	3.8	4.3	3.7	1.8
Transport, storage and communications	4.6	3.2	8.2	9.4	-0.3	7.7	1.7	1.3	1.3
Financial institutions, insurance, real estate and business services	9.5	6.7	1.6	-5.0	-20.6	2.3	15.0	2.7	3.6
Community, social and personal services	-1.2	1.1	3.4	5.1	-1.3	5.8	1.6	1.3	0.0
Gross domestic product, by type of expenditure									
Consumption	2.2	0.4	4.3	3.6	-6.8	3.9	4.8	4.6	3.0
General government	4.5	-5.2	4.7	-2.2	-5.5	4.7	0.5	3.2	3.7
Private	1.8	1.4	4.2	4.5	-7.0	3.8	5.4	4.8	2.8
Gross domestic investment	-2.6	-8.8	12.5	14.2	-49.4	29.0	36.8	21.8	0.7
Exports (goods and services)	11.3	2.4	7.8	-5.1	7.8	-1.0	-1.3	0.9	5.0
Imports (goods and services)	7.9	-10.2	15.4	7.0	-29.5	15.8	17.2	17.2	2.9
	Percentages of GDP								
Investment and saving [c]									
Gross domestic investment	21.6	19.7	21.5	25.3	14.7	20.1	25.7	27.7	27.7
National saving	16.6	19.7	19.7	16.7	20.0	25.9	22.8	22.3	26.1
External saving	4.9	0.0	1.8	8.6	-5.3	-5.8	2.8	5.4	1.6
	Millions of dollars								
Balance of payments									
Current account balance	-994	3	-427	-2 001	877	921	-599	-1 315	-424
Merchandise trade balance	-66	962	523	-1 035	1 545	1 399	-397	-998	-71
Exports f.o.b.	4 468	4 940	5 371	4 319	4 516	5 057	4 781	5 198	6 197
Imports f.o.b.	4 535	3 978	4 849	5 353	2 971	3 657	5 179	6 196	6 268
Services trade balance	-445	-427	-543	-563	-451	-420	-572	-709	-691
Income balance	-924	-1 023	-1 027	-1 171	-1 307	-1 411	-1 269	-1 262	-1 434
Net current transfers	442	492	621	767	1 089	1 352	1 639	1 654	1 772
Capital and financial balance [d]	-458	-74	-89	1 216	-1 822	-6 628	369	1 188	561
Net foreign direct investment	452	500	724	870	648	720	1 330	1 275	1 555
Financial capital [e]	-911	-574	-813	346	-2 470	-7 348	-961	-88	-994
Overall balance	-1 452	-71	-515	-785	-945	-5 707	-230	-127	136
Variation in reserve assets [f]	178	-246	-251	460	492	-307	106	66	-152
Other financing [g]	1 274	317	767	326	453	6 014	124	62	16
Other external-sector indicators									
Real effective exchange rate (index: 2000=100) [h]	66.7	68.1	66.1	65.0	89.2	100.0	70.9	62.8	61.2
Terms of trade for goods (index: 1997=100)	89.3	97.9	100.0	89.0	94.9	110.6	102.0	104.7	108.3
Net resource transfer (% of GDP)	-0.5	-3.7	-1.5	1.6	-16.0	-12.7	-3.7	-0.1	-3.2
Total gross external debt (millions of dollars)	13 934	14 586	15 099	16 400	16 282	13 564	14 376	16 236	16 586
Total gross external debt (% of GDP)	69.0	68.6	63.9	70.5	97.6	85.1	68.4	66.8	61.8
Net profits and interest (% of exports) [i]	-17.8	-18.1	-16.9	-23.4	-24.9	-23.9	-22.5	-20.6	-20.2

Table 1 (concluded)

	1995	1996	1997	1998	1999	2000	2001	2002	2003 [a]
					Average annual rates				
Employment									
Labour force participation rate [j]	55.8	55.8	55.8	57.3	58.4	60.0	56.8	55.6	54.1
Unemployment rate [k]	7.7	10.4	9.3	11.5	15.1	14.1	10.4	8.6	9.8
Visible underemployment rate [l]	...	...	...	13.6	15.2	13.8	11.3	9.3	8.8
					Annual percentages				
Prices									
Variation in consumer prices (December-December)	22.8	25.6	30.7	43.4	60.7	91.0	22.4	9.4	6.1
Variation in producer prices	...	...	...	...	186.9	64.9	-5.6	17.7	4.5
Variation in nominal exchange rate (December-December) [m]	26.8	23.4	22.2	50.1	176.0	37.3	0.0	0.0	0.0
Variation in average real wage	10.0	5.4	-2.3	-4.0	-8.3	-4.7	12.5	...	...
Nominal deposit rate [n]	...	...	...	...	...	8.2	6.6	5.1	5.3
Nominal lending rate [n]	...	...	...	...	...	15.2	15.5	14.1	12.6
					Percentages of GDP				
Non-financial public sector									
Total income	22.8	21.9	19.9	17.3	21.1	25.9	23.5	25.8	25.7
Total expenditure	23.8	24.6	22.1	22.1	25.0	24.4	23.1	25.2	24.5 [o]
Net capital expenditure	5.9	6.8	5.3	5.0	6.0	5.0	6.6	6.5	5.4
Primary balance	2.9	1.2	2.1	-0.6	3.2	8.1	5.1	4.2	4.3 [o]
Overall balance	-1.0	-2.7	-2.1	-4.8	-3.9	1.5	0.4	0.6	1.2 [o]
Public debt	64.7	64.4	56.6	61.9	92.0	79.7	63.4	55.6	51.6
Domestic [p]	7.3	8.8	7.0	10.5	18.1	17.8	13.3	11.4	11.0
External	57.4	55.6	49.6	51.4	73.9	62.0	50.1	44.2	40.6
Interest payments (% of total income)	17.1	17.9	21.1	24.5	33.7	25.5	20.2	13.9	11.9
Money and credit [q]									
Domestic credit [r]	25.4	26.6	27.0	34.1	41.1	29.3	24.6	23.4	...
To the public sector	0.4	0.8	1.2	2.4	4.5	2.4	-1.3	-1.7	...
To the private sector	25.1	25.9	25.8	31.6	36.6	26.9	26.0	25.2	...
Liquidity (M3)									
Money stock and local-currency deposits (M2) [s]	...	...	...	...	...	22.1	22.0	23.1	20.2

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Preliminary figures. [b] Based on figures in dollars at constant 2000 prices. [c] Based on figures in local currency at current prices. [d] Includes errors and omissions. [e] Refers to the capital and financial balance (including errors and omissions), minus net foreign direct investment. [f] A minus sign (-) denotes an increase in reserves. [g] Includes the use of IMF credit and loans and exceptional financing. [h] Annual average, weighted by the value of merchandise exports and imports. [i] Refers to net investment income as a percentage of exports of goods and services as shown on the balance of payments. [j] Economically active population as a percentage of the working-age population, three cities; up to 1998, urban total. [k] Unemployed population as a percentage of the economically active population, three cities; up to 1998, urban total. Includes hidden unemployment. [l] Underemployed population as a percentage of the economically active population, three cities; up to 1998, urban total. [m] In January 2000, the country adopted the United States dollar as its official currency. [n] Benchmark rate in dollars, monthly average. [o] US$ 130 million that was de-earmarked from the central government accounts by the Office of the Under-Secretary for the Treasury (equivalent to 0.5% of GDP) has not been deducted for 2003. [p] Corresponds to the central government. [q] The monetary figures are annual averages. [r] Refers to net credit extended to the public and private sectors by commercial banks and other financial and banking institutions. [s] Includes foreign-currency deposits.

that FEIREP revenue for 2004, together with the funds remaining from 2003, will be sufficient to buy back US$ 394 million of debt. Ecuadorian external public debt (including amounts owed by the central bank) stood at US$ 11.493 billion in December 2003 (42% of GDP), while central government domestic debt amounted to US$ 3.016 billion (11% of GDP). The latter continued to grow in 2004, rising to US$ 3.272 billion by June.

(b) Monetary policy

Along with the sharp decline in country risk for 2003 (measured by the J.P. Morgan Emerging Markets Bond Index (EMBI)) from an average of 1,796 basis points in December 2002 to 840 points in December 2003, benchmark lending rates eased from 12.7% in December 2002 to 11.5% in December 2003, while deposit rates

Table 2
ECUADOR: MAIN QUARTERLY INDICATORS

	2002				2003 [a]				2004 [a]	
	I	II	III	IV	I	II	III	IV	I	II
Gross domestic product (variation from same quarter of preceding year) [b]	1.3	3.9	5.0	3.5	3.4	-0.8	2.1	6.0	5.9	...
Merchandise exports, f.o.b. (millions of dollars)	1 102	1 303	1 312	1 324	1 513	1 423	1 486	1 616	1 587	...
Merchandise imports, c.i.f. (millions of dollars)	1 434	1 730	1 680	1 587	1 549	1 601	1 666	1 718	1 663	...
International reserves (millions of dollars)	777	904	901	715	770	762	991	813	824	885
Real effective exchange rate (index: 2000=100) [c]	64.4	63.4	62.2	61.1	60.2	61.1	61.3	62.3	63.3	62.7
Urban unemployment rate	8.7	8.8	8.7	8.3	9.9	10.2	9.9	9.3	11.2	11.4
Consumer prices (12-month percentage variation)	13.2	13.3	11.3	9.4	9.2	7.6	7.5	6.1	4.0	2.9
Average nominal exchange rate (sucres per dollar) [d]	25 000	25 000	25 000	25 000	25 000	25 000	25 000	24 998	25 000	25 000
Nominal interest rate (annualized percentages)										
Deposit rate [e]	5.3	5.0	5.2	5.1	5.4	5.3	5.2	5.2	4.8	4.2
Lending rate [e]	14.9	14.4	13.8	13.1	13.3	13.0	12.2	11.9	11.5	10.6
Interbank interest rate [f]	1.9	1.4	1.2	1.1	1.1	0.9	0.8	0.8	0.7	0.8
Sovereign bond spread (basis points)	1 037	1 253	1 980	1 794	1 371	1 208	1 116	771	702	890
Domestic credit [g] (variation from same quarter of preceding year)	14.2	16.6	-6.9	-8.8	3.3	3.0	...	...	...	...
Non-performing loans as a percentage of total loans (%) [h]	42.5	39.4	24.6	24.1	25.0	24.6	23.8	20.7	19.7	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Preliminary figures. [b] Based on figures in dollars at constant 2000 prices. [c] Quarterly average, weighted by the value of merchandise exports and imports. [d] In January 2000, the country adopted the United States dollar as its official currency. [e] Benchmark rate in dollars, monthly average. [f] Interbank market, weighted average. [g] Refers to net credit extended to the public and private sectors by commercial banks and other financial and banking institutions. [h] Refers to total credit extended by the banking system.

held fairly steady at around 5.1%. In the first half of 2004, the lending rate fell slightly compared with its December 2003 level, although it did fluctuate somewhat. By the end of June 2004, the benchmark lending rate stood at 10.2% and the benchmark deposit rate at 4.1%. Rates and spreads remained relatively high, despite low international interest rates and the downward trend in domestic inflation in 2003 and the first half of 2004.

One possible explanation for the above is the fact that private banks have placed a large proportion of their funds in highly liquid assets, many of which are held in investments abroad earning very poor returns: the sum of "notes, coins and deposits held by non-residents" and "non-equity securities held by non-residents" represented 23.1% of the total assets of private banks open in June 2004. This strong preference for liquidity abroad is due partly to the absence of a lender of last resort (although there is a liquidity fund), and it would also seem to indicate the sector's determination to maintain an "insurance policy" denominated in hard currency, "contracted" outside the country, notwithstanding the high opportunity cost involved.

The Ecuadorian financial sector has strengthened since the 1999 crisis, and bank assets have grown significantly. In 2003 and early 2004, however, credit to non-financial enterprises expanded proportionately less: while the former increased by 24% between February 2003 and June 2004, the latter rose by 17.6%. To underpin the development process, the country clearly needs to ensure greater access to credit and lower interest rates to its production sector (especially the tradable goods and labour-intensive segments).

(c) Other policies

Ecuador regained a degree of exchange-rate competitiveness vis-à- vis its trading partners in 2003 (a 2.6% depreciation between December 2002 and December 2003), owing essentially to nominal depreciation of the United States dollar against other currencies and despite the fact that its domestic inflation was even higher than that of the United States, thereby resulting in a real appreciation of 3.9% with respect to that country. The largest real bilateral depreciations relative to the country's major trading partners occurred with the euro (16.4% between December 2002 and December 2003), the Brazilian real (27.8%) and the Chilean peso (11.3%).

Between December 2003 and May 2004, the real effective exchange rate strengthened only slightly (0.7%) as a result of the opposing effects of appreciation of the dollar against the euro, devaluation of the Venezuelan currency and appreciation of the Colombian peso. Thus, the real effective exchange rate in May 2004 was still 9.7% below (i.e., an appreciation) the average recorded between January 1992 and December 1998, before the 1999 crisis.

3. The main variables

(a) Economic activity

Ecuador's GDP grew by 2.7% in 2003, generating an increase in per capita GDP of 0.9%. Almost half of that growth was attributable to the expansion of private oil production during the last quarter of 2003, following the coming-on-stream of the Heavy Crude Oil Pipeline (OCP), which doubled the country's crude oil transport capacity. However, owing to sluggish private consumption and a reduction in gross fixed capital formation, the non-oil economy scarcely grew at all. The other sectors that contributed to growth in 2003 were services (including commerce) and, to a lesser extent, manufacturing.

Growth of 5.5% is projected for 2004, based almost exclusively on the increase in private oil production. The oil companies that form part of the OCP consortium financed the construction of the pipeline by signing "ship-or-pay" contracts originally for an aggregate total of 390,000 barrels per day. Under these contracts, the firms stand to lose money if they fail to extract and transport crude through the pipeline in the volumes contracted in each case –thereby providing a major incentive to expand crude output for firms whose shipping capacity currently exceeds production. In contrast, production by Petroecuador has been on the decline in recent years, falling by 36.8% between 1993 and 2003. This could stabilize in 2004, however, if the firm's outsourced drilling operations prove successful. The other sectors of the Ecuadorian economy are not expected to grow much: bad weather has hurt the banana sector, and this has been compounded by the inclusion of Eastern European countries in the European Union quota regime; the shrimp industry was accused of dumping, and sanctions were imposed upon it in the United States, its main market; and cocoa-producing areas were also afflicted by poor weather in early 2004.

In 2003, the government invited bids for private investments in four of the fields currently operated by Petroecuador, but the Special Committee on Competitive Bidding declared the process null and void in April 2004. For the time being, it is uncertain when this bidding process will be resumed, since it is contingent upon a prior reform of the Hydrocarbon Act. Petroecuador's insufficient level of investment in both extraction and prospecting for new reserves poses a problem. Private activity will probably remain the only source of increases in oil reserves in 2004.

On the environmental front, the lawsuit brought against Texaco for environmental damage in Amazonia is still in the courts.[4] Environmental issues are particularly important given the government's interest in launching the Ishpingo-Tambococha-Tiputini (ITT) project. This area contains vast reserves of heavy crude, but its development will require huge capital outlays and will entail operating in ecologically sensitive areas. The

4 The firm (now Chevron-Texaco) operated in the area until 1992 and carried out a US$ 40 million restoration programme between 1995 and 1998.

failure of the April 2004 competitive bidding process underscored the need to identify environmental hazards in the areas in question in order to reduce uncertainty surrounding the value of the assets to be leased out and thereby raise expected returns for the government. The environmental issue is inextricably linked to sustainable development in Ecuador, given the country's wealth in terms of biodiversity and its tourism potential.

(b) Prices, wages and employment

Inflation fell to 6.1% in 2003 and is expected to ease further in 2004, with the 12-month figure slated to reach 2.9% by June 2004. Cumulative inflation during the first half of 2004 was 1.7%, with non-tradables posting notably smaller price hikes than in the same period a year earlier.

Despite the moderate growth rates recorded in recent years, employment has not picked up. Between May 2003 and May 2004, total unemployment[5] grew from 10% to 11.5%, while the overall employment rate fell slightly (-1.8%). No improvements are expected in job creation in 2004, since growth will be based on the oil sector, which does not generate strong demand for labour. The minimum real wage in May 2004 was slightly higher (2.1%) than in May 2003.

(c) The external sector

The balance-of-payments current account deficit improved during 2003, narrowing by 67.7% from US$ 1.315 billion to US$ 424 million, owing mainly to a drastic reduction in the merchandise trade deficit. The large external debt and the foreign investment flows of recent years generated an increase in factor payments abroad, which grew by 13.2% to US$ 1.454 billion. Remittances from workers abroad increased by 7.5% to US$ 1.54 billion.

Two points should be noted as regards the balance-of-payments financial account. First, FDI grew by 21.9% to stand at US$ 1.555 billion, thanks mainly to investments in the production and transport of hydrocarbons. Second, the category "other investments", which includes financial transactions that are neither portfolio nor direct investments, showed a net capital outflow of US$ 1.261 billion; this was concentrated, as indicated earlier, in the purchase of foreign assets (US$ 904 million).

The high export earnings recorded in 2003 (up by 19.9%) were attributable to the buoyancy of hydrocarbons and petroleum products (55% of the increase) and to more modest increases in bananas, vehicles and tinned fish. The 26.8% rise in oil export earnings reflected high prices and the increase in private crude production volumes following the coming-on-stream of the new pipeline (OCP). Among non-oil exports, bananas were the most dynamic category in 2003 (up by 13.4%), thanks to increased production and despite lower prices than in 2002. While shrimp exports grew by 9.1% in 2003, they have not yet regained the levels attained before the appearance of the white spot virus. Coffee and cocoa exports also had a good year, thanks to stronger prices.

Imports displayed weak growth in 2003 owing to the completion of the OCP and a slowdown in the non-oil economy, despite a vigorous expansion in fuel and lubricant imports. This increase (US$ 596.7 million, 156% higher than in 2002) was mainly due to Petroecuador's inability to supply the domestic market with petroleum products, compounded by a sharp rise in the international prices of hydrocarbon derivatives. Imports of consumer goods expanded by 4.2%, while imports of capital goods fell by 11.6%.

Oil exports are expected to improve further in 2004, although higher import prices (particularly for fuels) could affect the current account, given the country's need to import petroleum distillates. Workers' remittances are likely to remain high, and FDI will continue to flow into the oil sector, and particularly to firms that are part of the OCP consortium, although the amounts involved may be lower than in 2003.

In the first half of 2004, exports –led by oil– grew by 19.2% with respect to the same period in 2003. Hydrocarbon exports should continue to perform well throughout the year, but the outlook is less promising for nearly all other sectors. Banana exports, in particular, were down 12.9% in the first half of 2004, and the sector is facing a reduction of purchases by Eastern European countries following their admission to the European Union on 1 May 2004.[6]

Imports grew by 13.2% in f.o.b. terms in the first half of 2004, owing mainly to price increases. Raw materials account for nearly half (47.6%) of the increase in total imports, while fuels and lubricants account for another quarter, reflecting high prices on the international market. Total imports of capital goods rose by just 4.2% during the period due to the sluggishness of investment in both the crop-farming and industrial sectors.

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5 In Cuenca, Guayaquil and Quito.

6 The European Union announced an import quota for bananas from all sources that is significantly lower than Ecuador's sales to the region in 2003. To compensate for this, the country is seeking new markets for banana exports (especially China).