INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/79

ECUADOR

March 2019

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR ECUADOR

In the context of the Staff Report for the 2019 Article IV Consultation and Request for an Extended Arrangement Under the Extended Fund Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board and summarizing the views of the Executive Board as expressed during its March 11, 2019, consideration of the staff report on issues related to the Article IV Consultation and the IMF arrangement.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 11, 2019, following discussions that ended on February 21, 2019, with the officials of Ecuador on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 4, 2019.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Ecuador.

The documents listed below have been or will be separately released:

Letter of Intent sent to the IMF by the authorities of Ecuador*
Memorandum of Economic and Financial Policies by the authorities of Ecuador*
Technical Memorandum of Understanding*
Selected Issues

*Also included in Staff Report

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International Monetary Fund
Washington, D.C.

Press Release No. 19/72
FOR IMMEDIATE RELEASE
March 11, 2019

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$4.2 Billion Extended Fund Facility for Ecuador

The Executive Board of the International Monetary Fund (IMF) today approved a US$ 4.2 billion (435 percent of quota and SDR 3.035 billion) arrangement under the IMF's Extended Fund Facility (EFF) for Ecuador. The Board's decision enables the immediate disbursement of US$652 million (equivalent to SDR 469,7 million, or 67.3 percent of Ecuador's quota). This arrangement provides support for the Ecuadorean government's economic policies over the next three years.

The Ecuadorian authorities' plan aims to create a more dynamic, sustainable, and inclusive economy for the benefit of all Ecuadorians. It is centered around four major priorities; boosting competitiveness and job creation; strengthening fiscal sustainability and the institutional foundations of Ecuador's dollarization; protecting the poor and most vulnerable; and improving transparency and bolstering the fight against corruption.

Following the Executive Board discussion, Ms. Christine Lagarde Managing Director and Chair, summarized the Board's findings:

"The Ecuadorian authorities are implementing a comprehensive reform program aimed at modernizing the economy and paving the way for strong, sustained, and equitable growth. The authorities' measures are geared towards strengthening the fiscal position and improving competitiveness and by so doing help lessen vulnerabilities, put dollarization on a stronger footing, and, over time, encourage growth and job creation.

"Achieving a robust fiscal position is at the core of the authorities' program, which will be supported by a three-year extended arrangement from the IMF. The aim is to reduce debt-to-GDP ratio through a combination of a wage bill realignment, a careful and gradual optimization of fuel subsidies, a reprioritization of capital and goods and services spending, and a tax reform. The savings generated by these measures will allow for an increase in social assistance spending over the course of the program. The authorities will continue their efforts to strengthen the medium-term fiscal policy framework, and more rigorous fiscal controls and better public financial management will help to enhance the effectiveness of fiscal policy.

“The authorities are committed to supporting job creation, restoring competitiveness and catalyzing private sector-led growth while increasing transparency and forcefully countering corruption. A more efficient tax system, public wage restraint, facilitating the hiring process, and a more efficient energy sector are important components of the authorities’ plan in this area.

“Building crisis-preparedness capabilities and strengthening the oversight of banks and cooperatives will help to strengthen financial sector resilience. The institutional foundations of dollarization will be supported by the authorities’ efforts, already underway, to increase the operational autonomy of the central bank and to build reserve buffers.

“Protecting the poor and most vulnerable segments in society is a key objective of the authorities’ program. In this context, the authorities plan to extend the coverage of, and increase the nominal level of benefits under the existing social protection programs. Work is also underway to improve the targeting of social programs.”

Ecuador: Selected Economic Indicators

	2016	2017	Est. 2018	Proj. 2019	Proj. 2020
Output					
Real GDP growth	-1.2	2.4	1.1	-0.5	0.2
Employment					
Unemployment (%)	5.2	4.6	3.7	4.3	4.7
Prices					
Inflation, average (%)	1.7	0.4	-0.2	0.6	1.2
Public sector 1/					
Revenue (% GDP)	30.3	32.0	36.3	35.2	38.3
Expenditure (% GDP)	38.6	36.6	37.2	35.2	34.6
Overall balance (% GDP)	-8.2	-4.5	-0.9	0.0	3.8
Debt (% GDP)	43.2	44.6	46.1	49.2	46.8
Money and credit					
Broad money (% change)	16.5	10.0	5.6	1.7	4.2
Credit to the private sector (% change)	6.2	16.4	14.9	4.4	5.7
Balance of payments					
Current account (% GDP)	1.3	-0.4	-0.7	0.4	1.4
FDI (% GDP)	0.8	0.6	0.9	1.1	1.1
GIR (in months of imports)	2.7	1.1	1.0	2.5	3.9
External debt (% GDP)	36.6	39.5	40.5	42.8	42.9

Sources: Central Bank; Ministry of Finance; National Statistical Institute (INEC); and Fund staff estimates/projections.

1/ Consolidated at the level of the non-financial public sector.

Press Release No. 19/84
FOR IMMEDIATE RELEASE
March 21, 2019

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2019 Article IV Consultation with Ecuador

On March 11, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Ecuador. At the same time, the Board approved a three-year Extended Arrangements under the Extended Fund Facility; a press release on this was issued separately.

The 2014 oil price decline exposed the underlying structural imbalances of Ecuador's economy, including the very high non-oil primary fiscal deficit and rising public debt. Following several quarters of economic contraction in 2015 and 2016, the economy returned to growth, with a rebound of 2.4 percent in 2017. Since then, however, growth has decelerated and is forecast to be 1.1 percent for 2018. An expansion in domestic demand has been met through a rise in imports, particularly following the removal of tariff safeguards. Cumulative inflation was negative for much of 2018 reflecting slow growth, the overvaluation of the real exchange rate, and broader imbalances in the economy.

The government lowered the non-oil primary deficit (including fuel subsidies) from 7.6 percent of GDP in 2016 to 5.3 percent of GDP deficit in 2018. The adjustment that took place in 2018 was largely a product of a reduction of capital spending and the temporary effects of a tax amnesty during the year.

The authorities plan to reduce the non-oil primary balance by 5 percent of GDP over the next three years. There are likely to be near-term costs to growth from the planned fiscal consolidation, but supply-side reforms are expected to improve growth prospects over the medium term. Inflation is likely to remain subdued throughout the next few years. This, alongside nominal wage restraint and improving productivity, should steadily erode the overvaluation of the real effective exchange rate, which will allow the maintenance of a current account surplus over the medium term. Fiscal consolidation will also enable a moderate build-up of reserves, from very low levels.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment[2]

Directors commended the authorities for their efforts to transform the economy and address Ecuador's complex macroeconomic and structural challenges. Directors welcomed the authorities' focus on strengthening the fiscal, financial, and institutional foundations, and emphasized that strong commitment to sound policies and reforms will be critical to reducing balance of payments vulnerabilities, consolidating macroeconomic stability, putting dollarization on a stronger footing, and fostering job creation and sustainable growth.

Directors welcomed the authorities' commitment to restore fiscal discipline and sustainability. They agreed that adjustment efforts should focus on a combination of expenditure and revenue measures. Directors saw need for a realignment of the public sector wage bill, careful reduction in untargeted subsidies, and reprioritization of capital and goods and services spending. They also emphasized the importance of making the tax system more equitable, growth friendly, and simpler. Directors acknowledged that while these fiscal efforts might impact growth in the near term, they are key to sustained and equitable growth over the medium term.

Directors welcomed the focus on lowering the debt to GDP ratio and complementing the existing expenditure growth rule with binding annual targets for the non oil primary balance. They concurred that the publication of timely and periodic in year reports to assess compliance with fiscal rules would further strengthen credibility. Over time, better public financial management, budget procedures, and procurement practices, combined with more rigorous fiscal controls, would make fiscal policy more effective.

Directors welcomed the authorities' commitment to protect the poor and the most vulnerable. To manage the impact of the economic transition and maintain societal support for the economic program, Directors encouraged the authorities to move quickly to expand the eligibility of social assistance programs, with better targeting and a higher level of benefits. Over the longer term, they called for action to improve education and health outcomes.

Directors underscored the importance of supply side reforms in restoring competitiveness. A more efficient tax system, public wage restraint, enhanced access to the formal labor market through improved hiring processes, and better governance will all contribute to a vibrant, private sector led growth model. Directors emphasized that there remains scope to remove trade barriers, improve the business climate, and create opportunities for greater private sector involvement.

To support dollarization, Directors endorsed measures to build financial resilience, remove impediments to effective financial intermediation, and strengthen the central bank, including through building up international reserves. To better anticipate and adapt to shocks, Directors recommended increasing the oversight of banks and cooperatives and building crisis preparedness and contingency planning capabilities. Directors considered that simplifying the complex system of liquidity regulations and gradually phasing out interest rate ceilings would

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

support greater access to financial intermediation. They commended the authorities' efforts to make the central bank more operationally independent, to strengthen its governance, and to restrict it from providing fiscal financing. Directors encouraged steps to strengthen the effectiveness of the AML/CFT framework.

Ecuador: Selected Economic Indicators

	2016	2017	Est. 2018	Proj. 2019	Proj. 2020
Output					
Real GDP growth	-1.2	2.4	1.1	-0.5	0.2
Employment					
Unemployment (%)	5.2	4.6	3.7	4.3	4.7
Prices					
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Sources: Central Bank; Ministry of Finance; National Statistical Institute (INEC); and Fund staff estimates/projections.

1/ Consolidated at the level of the non-financial public sector.

INTERNATIONAL MONETARY FUND

ECUADOR

March 4, 2019

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY

EXECUTIVE SUMMARY

Context: The authorities face a difficult situation. Wage increases have outpaced productivity growth over the past decade which, has led to a deterioration in competitiveness. This has been exacerbated by a strong U.S. dollar—Ecuador's economy is fully dollarized—leaving the real exchange rate overvalued. Public debt is high and rising, the government faces sizable gross financing needs, and international reserves are precariously low. The recent volatility in oil prices and tighter global financial conditions have exacerbated these strains.

Article IV: The Article IV discussions focused on diagnosing the nature of the imbalances facing Ecuador and the policy changes that will be needed to address them. At the center of the discussion was the proper calibration of the size, pace, and composition of the reduction in the fiscal deficit that will be needed in the coming years. In addition, there was broad agreement that fundamental supply-side efforts will be needed to foster competitiveness, create jobs, rebuild institutions, and make Ecuador a more attractive destination for private investment. Finally, improving the social safety net and increasing the effectiveness of public spending, particularly on health and education, will be essential to achieving strong, sustained, and socially equitable growth.

Program Objectives: Consistent with the findings of the Article IV, the authorities' policy plan seeks to decisively address the systemic vulnerabilities facing Ecuador. The goals of these policies are to boost competitiveness and job creation, protect the poor and most vulnerable, fortify the institutional foundations for dollarization, and to improve transparency and good governance to public sector operations while strengthening the fight against corruption.

Program Modalities: The proposed program would be a 36-month Extended Fund Facility with access of US$4.209 billion (SDR 3.035 billion, 435 percent of quota). The program has quarterly reviews and the full amount of Fund resources would be made available for direct budget support. Performance criteria have been established on the non-oil primary balance of the nonfinancial public sector (including fuel subsidies), net international reserves (excluding bank deposits held at the central bank), and on social assistance spending. There are continuous performance criteria to prevent new external payment arrears and to prohibit central bank financing of the nonfinancial public sector (both directly or indirectly through public banks). The program also includes a quarterly indicative target on the overall balance of the nonfinancial public sector.

Approved By
Nigel Chalk and Maria Gonzalez

Discussions were held in Quito (June 20 – July 4, 2018 and February 11−21, 2019). The mission also visited Guayaquil on June 26, 2018 and February 20, 2019, and Cuenca on June 25, 2018. The mission comprised A. Ivanova (Head), M. Ghilardi, and R. Mowatt (all WHD), R. Anspach (COM), S. Lizarazo (SPR), V. Lledo (FAD), M. Mansilla (MCM), M. Sabates (STA), and H. Weenink (LEG). A. Werner and N. Chalk (WHD) and A. Tombini and F. Rivadeneira (both OED) joined part of the mission.

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BACKDROP

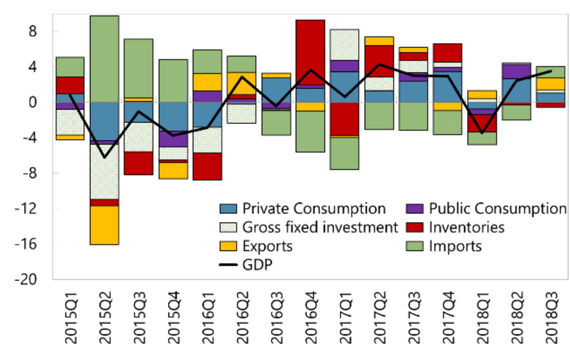
1. **The fall in oil prices and rise in the U.S. dollar in 2014–15 caused an abrupt downturn in Ecuador's fully dollarized economy in 2015–16.** After five consecutive quarters of contraction measured on a year-on-year basis, in the midst of which there was a major earthquake, the economy returned to growth at the end of 2016, with a rebound of 2.4 percent in 2017.

2. **The IMF provided balance of payments support following the April 2016 earthquake.** On July 8, 2016 the Executive Board approved a disbursement of SDR 261.63 million (about US$364 million) under the Rapid Financing Instrument. This disbursement helped the country meet an urgent balance-of-payments need due to the 7.8-magnitude earthquake that caused significant damages to infrastructure, housing, and agriculture, and killed 671 people. Reconstruction of the affected areas is still ongoing (Box 1).

3. **The current administration took office in May 2017.** Over the past 21 months, President Moreno has fashioned a pragmatic path, showing openness to engage with the private sector and the opposition. The Moreno administration has also been active in building stronger relationships with IFIs in support of their policy efforts. In particular, Fund staff have been working closely with the authorities on a range of technical assistance areas (e.g. in statistics, the fiscal responsibility framework, debt management, and financial policies). In February 2018, President Moreno obtained approval in an important national referendum for a range of institutional changes including restoring term limits for the presidency, strengthening the fight against corruption, reinstating the independence of the judiciary and control bodies, broadening environmental protections for certain areas, and eliminating the controversial real estate capital gains tax.

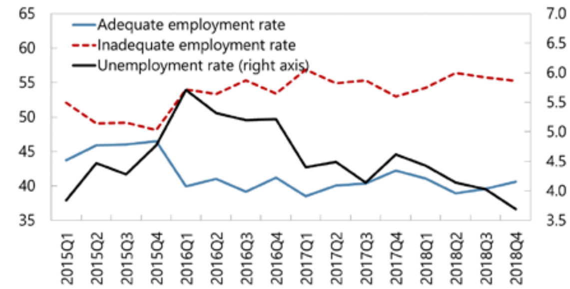
4. **Over the past year, growth has decelerated.** Year-on-year growth in 2018Q3 was 1.4 percent and growth is estimated to have been 1.1 percent for the year as a whole. An expansion in domestic demand has been met through a rise in imports, particularly following the removal of tariff safeguards. Despite the economic deceleration in 2018, private investment has been relatively strong. The unemployment rate fell to 3.7 percent in December although the share of the so-called "inadequate employment" (official definition includes, among others, those who are earning below the minimum wage) has increased. Cumulative inflation was negative for much of 2018 reflecting slow growth, the overvaluation of the real exchange rate, and broader imbalances in the economy.

Ecuador: Contributions to Growth, 2015-2018
(In percent, q-o-q, annualized)



Sources: Haver, BCE, and IMF staff calculations.

Ecuador: Labor Market
(In percent of labor force)



Sources: Haver, INEC, and IMF staff calculations.
Note: Inadequate employment refers to workers earning less than the minimum wage, or working less than full time while willing and able to work more hours.

5. Over the past year, the government has made progress in implementing reforms in a range of areas including:

- Reaching consensus in the National Assembly to pass the "Productive Development Law"[1] in August 2018 which contained:
  - A prohibition for (i) the BCE to purchase new public securities and bonds and (ii) for public financial institutions to hold domestic investment funds from the BCE as an indirect means to invest in securities issued by other public-sector entities;
  - A new fiscal framework that combines a formal debt anchor with a rule capping the growth of public spending (at Ecuador's long-term growth rate), supported by escape clauses and automatic correction mechanisms;
  - An oil stabilization fund that would eventually serve to smooth spending over the commodity cycle.
- Lowering the non-oil primary deficit (including fuel subsidies) from 7.6 percent of GDP in 2016 to 5.3 percent of GDP deficit in 2018. The deficit reduction that took place in 2018 was largely a product of a reduction in capital spending (of 2.3 percent of GDP). The fiscal position also benefited from the temporary effects of a tax amnesty during the course of the year (adding 1 percent of GDP to nonoil revenues).
- Beginning the process of reducing fuel subsidies by eliminating the subsidy on high octane gasoline (super gasoline) and reducing subsidies on regular gasoline and for the industrial use of diesel.
- Bringing transparency to the compilation of public debt statistics including by publishing a report by the auditor general that revealed the public debt was significantly higher than previously stated. The government has been working with Fund technical assistance to bring the

[1] "Ley para Fomento Productivo" in Spanish.

reporting of public debt into line with international best practice. This work allowed reconciling above- and below-the-line fiscal data as well as stocks and flows in the fiscal accounts for 2018 with minimal discrepancy, which provides reassurances on the quality of public debt statistics.[2]

- Completely removing import surcharges that were imposed in 2015 to address the country's deteriorating balance of payments situation following the decline in world oil prices.

- Strengthening the governance of public operations including by undertaking corruption investigations into bribes allegedly paid to government officials by a foreign construction company.

6. **Throughout the tenure of the current administration Ecuador has maintained its access to external financing.** In January 2018, Ecuador issued US$3 billion in 10-year bonds on international markets at a yield of 7.875 percent. Subsequently, as global financial conditions tightened and spreads on emerging market debt rose, Ecuador chose to issue collateral-like debt and undertake repurchase operations with international banks. In January of this year, the government placed US$1 billion in 10-year bonds at a yield of 10.75 percent.

Box 1. Earthquake Reconstruction

On April 2016 Ecuador was hit by a 7.8 magnitude earthquake mainly affecting the coastal provinces of Manabí and Esmeraldas. The earthquake killed 671 people and affected some 68,000 households. The authorities' joint assessment with the UN's Economic Commission for Latin America and the Caribbean estimated reconstruction costs of US$3.3 billion. More than 32,000 houses need to be rebuilt or repaired. Public infrastructure suffered considerable damage: 875 schools were affected (of which 325 suffered medium to severe damage), 48 health facilities (e.g., clinics and hospitals), 83 km of roads, more than 7,000 km of power lines, and damage to telecommunications and water facilities.

The emergency and initial response of the government involved dispatching more than 1,500 emergency personnel to the affected areas. Within the first two weeks of the disaster the government restored water and electricity access to most of the affected areas, set up 30 shelters, and provided medical care to over 31,000 people. The government gave cash transfers for food, and for families to find shelter (supporting about 43,000 households).

Earthquake Financing Sources
(In millions)

Entity	Funds
Solidarity law 1/	1,631
Inter-American Development Bank	367
International Monetary Fund 2/	365
European Investment Bank	175
China (grants)	226
China (loans)	156
Government budget	110
French Development Agency	100
Bonds	78
World Bank	69
Latin America Investment Facility	14
Other	9
Private donations	8
Total	**3,308**

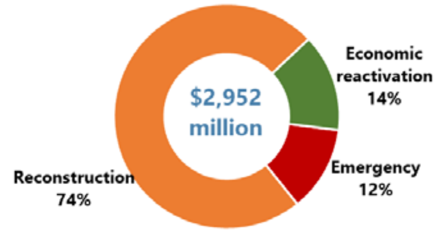
Source: Reconstruction Technical Secretariat.
1/ Temporary taxes introduced to finance the reconstruction.
2/ The IMF's RFI loan was for balance of payments support due to the earthquake, but was not necessarily used directly in the emergency or reconstruction effort.

[2] See "IMF Definition of Public Debt" in Selected Issues and Analytical Notes.

Box 1. Earthquake Reconstruction (concluded)

The government raised revenues to finance the emergency response and reconstruction. The "Solidarity Law" included a temporary increase in the VAT rate of 2 percent (raising about 1.6 percent of GDP). The government also received grants, and loans to finance the post-earthquake efforts. Almost ¾ of the funds went towards reconstruction of housing, roads, health and education facilities with the remainder used to help businesses recover and provide employment opportunities. The reconstruction work and the restart of economic activity has created more than 50,000 direct jobs, and about 126,000 indirect employment opportunities.

Earthquake Spending



Source: Reconstruction Technical Secretariat.

DIAGNOSIS

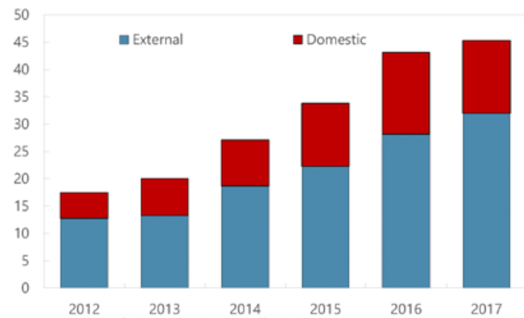
7. At the core of Ecuador's imbalances has been the pursuit of an unsustainable fiscal path. The 2014 oil price decline exposed the underlying structural imbalances of Ecuador's economy, including the very high non-oil primary fiscal deficit and rising public debt. The overall fiscal deficit peaked at 8.2 percent of GDP in 2016 (the non-oil primary balance including fuel subsidies was 7.6 percent of GDP in the same year). This deficit was financed largely by short-term domestic debt, a draw-down of central bank reserves, and the placement of debt in international markets at a high cost. By 2017, a rebound in oil prices, cuts to capital spending, a public sector hiring freeze, and the introduction of temporary tax measures after the April 2016 earthquake led to a reduction in the fiscal deficit to a still-high 4.5 percent of GDP. In 2018, cuts to capital spending and a better oil balance (mostly from higher oil prices earlier in the year) lowered the deficit to 0.9 percent of GDP. However, investor confidence has been eroded by lower oil prices and uncertainties surrounding the accurate measurement of the level of the public debt.[3]

8. Expenditure on wages and salaries and on fuel subsidies is relatively high compared with regional peers. The large expenditure increases of the past decade on wages and salaries have proven difficult to reverse, while poorly-targeted fuel subsidies remain a significant component of government expenditure.

[3] These concerns were amplified in April when a report was released by the comptroller that indicated that the public debt, measured in line with the national official debt definition, was higher than the official threshold of 40 percent of GDP.

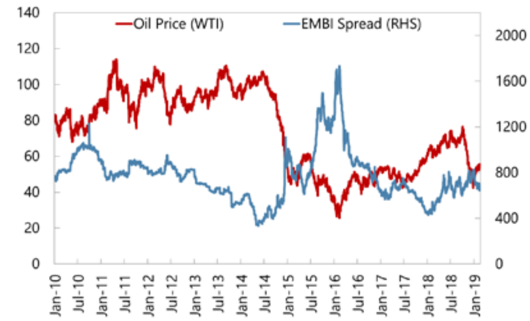
Fiscal Imbalances

Ecuador: NFPS Gross Consolidated Debt
(In percent of GDP)



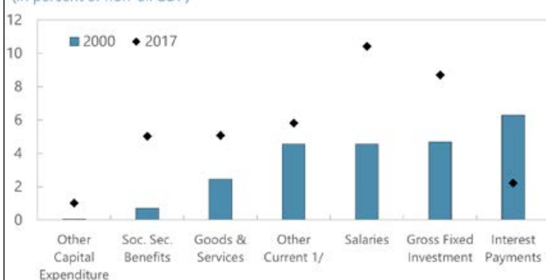
Sources: Ministry of Finance and IMF staff calculations.

Ecuador: EMBI Spread and Oil Price
(In US$ per barrel and basis points)



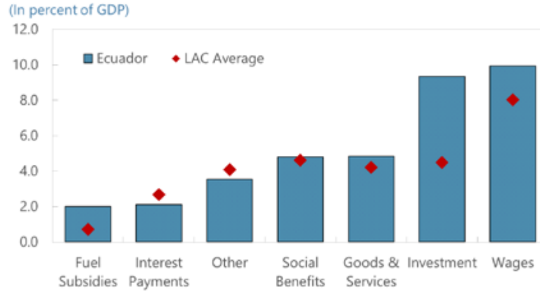
Source: Bloomberg.

Ecuador: Expenditure of the Non-Financial Public Sector, 2000 and 2017
(In percent of non-oil GDP)



Sources: BCE and IMF staff calculations.
1/ Includes fuel subsidies.

Ecuador Expenditure Composition, 2017
(In percent of GDP)

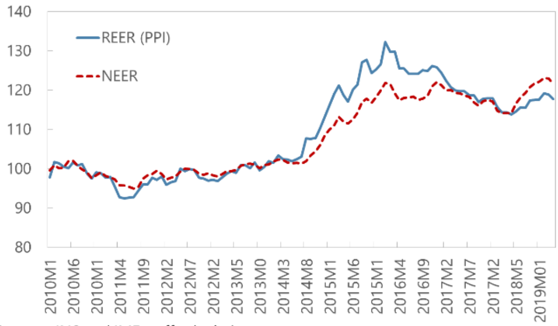


Sources: Fund staff calculations based on official sources.
Note: Sample size per indicator differs based on data availability.

9. **The foundations of the dollarized system have been undermined by a fiscal policy that is inconsistent with the constraints imposed by dollarization and, in parallel, by an erosion of domestic institutions.** The decision to dollarize the economy continues to receive significant public support. However, under the previous administration, policies steadily undermined the viability of the dollarization framework, mainly through central bank financing of fiscal spending. This, in turn, has resulted in an increase in balance of payments vulnerabilities, a high public debt-to-GDP ratio, inadequate reserve coverage, and an overvalued real exchange rate.

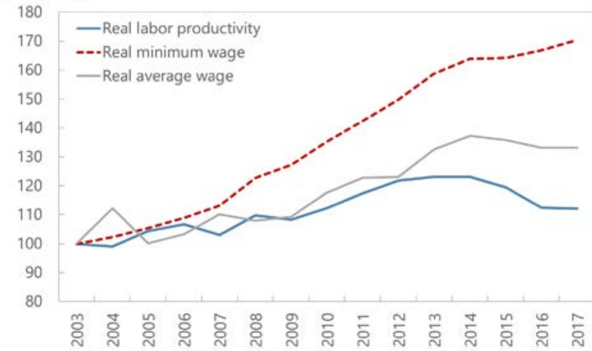
10. **Ecuador's external position is now judged to be weaker than the level that is consistent with medium-term fundamentals and desirable policies.** Wage growth has outpaced productivity growth over the past decade and, since 2014, the terms of trade have moved against Ecuador. The strong cyclical position of the U.S. economy and the appreciation of the U.S. dollar continue to add to Ecuador's external imbalances. The current account has been adjusting to the 2014–15 oil price shock, largely through a compression of imports, but the 2018 cyclically-adjusted current account remains at 3.7 percent of GDP below the estimated current account norm. The REER is judged to be overvalued by around 31 percent (Annex IV).

Ecuador: Real and Nominal Effective Exchange Rates
(Jan-10=100)



Sources: INS and IMF staff calculations.
Note: The effective exchange rates exclude Venezuela.

Ecuador: Real Labor Productivity and Real Minimum Wage
(2003=100)

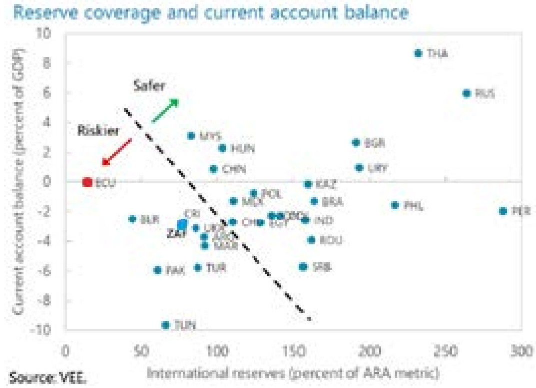


Sources: INEC, BCE, ILO and IMF staff calculations.

11. These external imbalances imply a significant gross external financing need (US$7.3 billion over the next 12 months). About one half of the US$7.3 billion arises from upcoming budgetary amortization payments to international creditors.

12. Ecuador's external imbalances are exacerbated by a very low level of international reserves, leaving the dollarized system highly vulnerable to a sudden shift in capital flows and terms-of-trade shocks. The stock of gross international reserves (GIR)[4] at end-2018 was US$2.2 billion (representing 12 percent of the Fund's ARA metric or about 1¼ months of imports). Ecuador's gross reserve coverage is the lowest of any emerging market economy. Net international reserves[5] are estimated to have ended 2018 at negative US$1.7 billion.[6]

Reserve coverage and current account balance



Source: VEE.

THE GOVERNMENT'S POLICY OBJECTIVES

13. To counter these vulnerabilities, restore growth, and improve social outcomes, the authorities have designed a comprehensive policy plan. This plan aims to put debt on a firmly downward path, build reserve buffers and restore international competitiveness, while also making substantive improvements to the social assistance system. The plan further envisages measures to restore central bank autonomy, tackle corruption, and increase transparency.

[4] This definition of GIR excludes non-liquid items included in the authorities' definition of reserves (primarily non-monetary gold) as well as encumbered reserves.

[5] Net international reserves net out obligations to the Fund (excluding direct budget support), encumbered gold reserves and other non-liquid items included in reserves, as well as the deposits of depository institutions that are held at the central bank.

[6] See "Reserve Adequacy" in Selected Issues and Analytical Notes.

Rebuild and Strengthen the Institutional Foundation for Dollarization

14. The authorities have adopted a credible and ambitious medium-term fiscal plan that will put the debt-to-GDP ratio on a firmly downward path. The goal of the government's plan is to increase the non-oil primary balance (including fuel subsidies) by 5 percent of GDP from 2019–21, with a substantial share of this taking place in the first year of the program. The improvement in the non-oil primary balance will be achieved by reductions in public employment and lower government wages; a gradual elimination of untargeted fuel subsidies; an overhaul of the tax system; and efforts to better prioritize spending on both capital outlays and goods and services. The authorities also intend to improve the medium-term framework for fiscal policymaking, upgrading both the fiscal responsibility framework (to provide meaningful medium-term constraints on fiscal policies) and debt management processes.

15. There is a strong commitment to restore autonomy to the central bank. The authorities have taken legislative and other steps to put an end to new central bank financing of the government and the quasi-fiscal activities of the central bank. The authorities intend to go further in the coming months to strengthen the central bank's autonomy and governance arrangements and to strengthen the central bank's financial stability oversight function.

Generate Employment and Growth Through Competitiveness

16. Supply-side constraints are also being addressed to restore international competitiveness. The authorities believe that a comprehensive tax reform, reform of fiscal institutions, labor market reform, and steps to increase financial sector resilience and ease capital market regulations will all contribute to improving the investment environment. These policies will provide a strong foundation to improve productivity and foster private investment, support the middle class, and further strengthen the foundations for dollarization. These reforms, together with the measures to restore fiscal sustainability are expected to realign the current account and the real effective exchange rate with their medium term fundamentals.

Promote Equality of Opportunity and Protect the Poor and Vulnerable

17. The authorities intend to replace untargeted energy subsidies with up-front improvements to the existing social assistance system. The authorities' plan will extend the coverage of, and increase the nominal level of benefits under, the existing conditional cash transfer program. Work is also underway to improve the targeting of social programs. The government will strengthen the non-contributory pension (an important safety net for the elderly) and expand existing programs to support the disabled. Finally, the government is examining options to increase the efficiency of education and health spending, particularly to improve outcomes for lower income households.

Ensure Full Transparency and Good Governance

18. A multi-pronged effort is underway to increase transparency and tackle corruption. Policy measures include improving fiscal transparency and procurement practices, including in the oil sector and for public infrastructure; adopting international standards for reporting of the public debt; preparing legislation to prevent and penalize corruption; publishing the financial accounts of the central bank and of public oil companies; and strengthening the framework for AML/CFT.

OUTLOOK AND RISKS

19. The authorities' plan to reduce the non-oil primary deficit by 5 percentage points of GDP over the next three years will put debt on a downward path starting in 2020, falling below 40 percent of GDP by 2023. The forecasts incorporate some near-term costs to growth from the planned fiscal consolidation, but supply-side reforms are expected to improve growth prospects over the medium term. There was agreement that growth in 2019 would likely be in the -0.5 to +0.5 percent range (although forecasts under the program are based on the weaker end of this range). The current account is expected to move from a deficit of 0.7 percent of GDP in 2018 to a surplus of around 0.4 percent of GDP this year. Inflation is likely to remain subdued throughout the next few years which, alongside nominal wage restraint and improving productivity, should steadily erode the overvaluation of the real effective exchange rate. Under the program baseline, it is assumed that the improvement in the fiscal position is sufficient to leave the sovereign completely financed. Gross reserves are expected to increase to about US$11.4 billion (63 percent of the ARA metric) by the end of the program.

20. There was broad agreement on the downside risks to this outlook (see Risk Assessment Matrix—Annex III).

- External risks are predominantly associated with a significant further fall in oil prices that could necessitate an even larger and perhaps more accelerated economic adjustment than is currently being planned, weighing on incomes and job creation. Such a scenario is likely to be associated with a much less hospitable environment in global capital markets at a time when fiscal financing needs will increase (because of the effect of the lower oil price on the nonfinancial public sector oil balance).

- A further upward move in the U.S. dollar would increase the overvaluation in the real exchange rate, worsen competitiveness and weigh on the external accounts. This would likely cause a more prolonged (and perhaps painful) period of disinflation, creating a headwind to growth, and putting downward pressure on the current account. As such, a stronger U.S. dollar would complicate the government's efforts to reduce external vulnerabilities.

- Domestic political and social opposition could create challenges for the implementation of the government's policy plans (particularly changes to fuel subsidies, the public-sector wage bill, and the tax system). It will be important that these policy changes are carefully calibrated and well-communicated to garner societal consensus.

Ecuador: Active Scenario

(Selected Indicators, Percent of GDP Unless Otherwise Specified)

		Projections					
	2017	2018	2019	2020	2021	2022	2023
Real							
Growth (percent change)	2.4	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation (avg.) (percent change)	0.4	-0.2	0.6	1.2	1.6	1.3	1.1
Fiscal							
Non-oil PB	-4.2	-1.8	-1.5	0.7	1.1	1.1	1.2
Non-oil PB (incl. fuel subsidies)	-6.2	-5.3	-3.3	-1.3	-0.3	-0.3	-0.4
Primary balance	-2.4	1.5	2.7	6.5	5.5	5.1	5.0
Overall balance	-4.5	-0.9	0.0	3.8	2.9	2.8	2.9
Debt (IMF)	44.6	46.1	49.2	46.8	45.2	40.8	36.6
Capital expenditure	9.3	7.0	7.1	6.8	6.0	6.4	6.3
GFN Fiscal ($ mil.)	17,475	8,889	5,903	2,523	1,442	3,149	2,933
Bonds - external ($ mil.)	6,471	4,504	1,137	0	0	642	1,057
Change in govt deposits ($ mil.)	562	1,043	2,719	2,154	2,774	0	0
BOP							
Current account	-0.4	-0.7	0.4	1.4	1.5	1.5	1.7
Non-oil Current account	-3.9	-4.9	-3.9	-3.1	-2.2	-2.1	-1.8
GFN External ($ mil.)	8,075	9,481	7,263	7,344	4,942	7,203	6,121
Foreign Direct Investment ($ mil.)	618	945	1,219	1,235	1,545	1,604	1,656
Public Sector Bonds ($ mil.)	6,471	4,504	1,137	0	0	642	1,057
Private Sector Borrowing ($ mil.)	935	4,032	3,504	4,705	1,994	4,956	3,408
Monetary							
GIR ($ mil.) 1/	2,006	2,158	4,999	7,761	11,397	11,845	12,944
in percent of ARA metric	12	12	28	43	63	65	71
less outstanding credit of the BCE to the IMF ($ mil.)	373	364	317	136	0	0	0
less short-term foreign liabilities ($ mil.)	0	300	0	0	0	0	0
less reserves of Other Depository Institutions (ODIs) at the BCE ($ mil.)	3,904	3,172	3,262	3,690	3,942	4,249	4,564
equals Program NIR ($ mil.) 2/	-2,271	-1,677	1,419	3,935	7,455	7,596	8,380
Underlying reserves ($ mil.) 3/	-2,271	-1,677	21	1,136	3,255	3,396	4,255
Decomposition of change in GIR							
Δ GIR ($ mil.) 2/	-2,210	153	2,840	2,762	3,635	448	1,100
o/w Δ bank reserves ($ mil.), incl. Other Financial Institutions (OFIs)	-995	-396	134	445	285	357	360
o/w Δ govt deposits ($ mil.)	562	848	2,719	2,154	2,774	0	0
o/w net IMF financing to the BCE ($ mil.)	0	0	-45	-181	-136	0	0
o/w Δ credit to public sector ($ mil.) (- = increase)	-978	-90	18	0	743	136	779
o/w gold transaction ($ mil.)	-376	0	0	356	0	0	0
o/w other ($ mil.)	-423	-209	14	-12	-31	-44	-39

Sources: Central Bank of Ecuador, Ministry of Finance, IMF staff calculations.

1/ Excludes non-liquid and encumbered items included in the authorities' definition of GIR.

2/ GIR less outstanding debt to the IMF (excl. liabilities of the treasury), short-term foreign liabilities of the BCE, and bank reserves of ODIs.

3/ GIR less outstanding debt to the IMF (incl. liabilities of the treasury), short-term foreign liabilities of the BCE, and bank reserves of ODIs.

THE GOVERNMENT'S POLICY PLAN

A. Putting Public Debt on a Firmly Downward Path

21. Putting the public debt on a downward path will require a sustained reduction in the fiscal deficit. The authorities are planning to lower the non-oil primary deficit, including fuel subsidies, from 5.3 percent of GDP in 2018 to 0.3 percent of GDP by 2021. Around 2 percent of GDP of that effort would be accomplished in 2019. The overall fiscal balance is expected to move from a deficit of 0.9 percent of GDP in 2018 to a surplus of 2.9 percent of GDP by 2021. The public debt is forecast to peak at 49 percent of GDP in 2019 and fall below 40 percent of GDP and towards more prudent levels after 2023.[7]

22. The authorities intend to achieve this fiscal realignment through both revenue and spending measures

- ***Adopting a comprehensive tax reform.*** The authorities intend to develop a tax reform in the first half of 2019 (with the changes legislated by November and implemented in 2020-21) that will target an increase in revenue of 1½ to 2 percent of GDP. The goals of the reform will be to simplify the tax system and make it more growth-friendly and more equitable; to improve the business environment and encourage investment; to broaden the tax base and eliminate unwarranted tax exemptions, special regimes and preferences; to rebalance the system from direct to indirect taxation; and to phase out distortionary turnover taxes and levies on capital flows. The design of the reform will build on the recommendations of a recent IMF technical assistance mission; a Poverty and Social Impact Analysis (PSIA) by the World Bank could help ensure that the tax reform is equitable.

- ***The tax policy reform would be complemented with tax administration improvements*** including strengthening tax and customs operations and conducting a diagnosis of tax and customs operations (e.g. to raise compliance levels and to assess the potential risks and benefits of integrating the tax and customs administrations).[8]

- ***Phasing out the tax on transfers abroad.*** At the end of 2007, Ecuador introduced a tax on transfers abroad (*impuesto a la salida de divisas*) to minimize short-term capital flow volatility. The tax rate was increased from 0.5 percent in 2008 to 5 percent in 2012. The tax is imposed on current account transactions and constitutes an exchange restriction (subject to Fund approval under Article VIII). It also applies to capital account transactions and as such constitutes a capital flow management measure (CFM) according to the Fund's Institutional View on capital flows. The authorities intend to phase this tax out once macroeconomic stability is restored and the

[7] See Box 2 and "Calibrating Ecuador's Debt Ceiling" in Selected Issues and Analytical Notes.

[8] Further revenue gains may occur from the government's efforts to strengthen tax and customs administration but, to be conservative, this represents an upside to the baseline forecasts.

reserve position is strengthened and as a means to encourage inflows that will be used to finance new private investment.

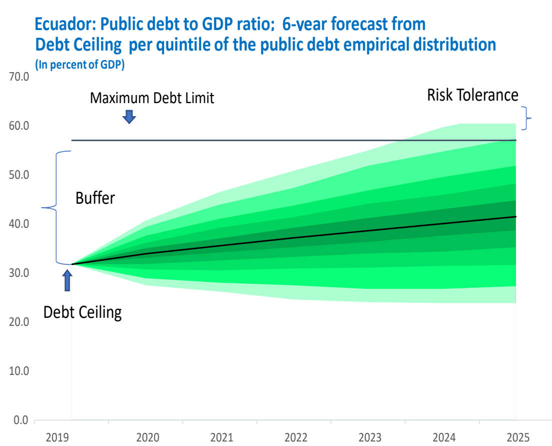
Box 2. Calibrating Ecuador’s Debt Ceiling[1]

The appropriate range for Ecuador’s debt ceiling is established as a level that ensures, with high probability, that the maximum debt limit (i.e., the level of the debt-GDP that creates debt distress with high probability) will not be breached. This involves a sequential approach of:

(1) *estimating a “maximum debt limit” from cross country data that keeps the probability of debt distress below a specific level.* A probit model was used, based on a sample of oil-exporting emerging markets, to estimate the probability of debt distress (i.e. when the EMBI spread exceeds 1000 bps) at different levels of public debt-GDP. The model controls for global factors (the degree of global risk aversion, level of oil prices) as well as Ecuador-specific inputs (e.g. the quality of institutions, the history of default, the level of the fiscal deficit). For Ecuador, the model suggests that keeping the probability of debt distress below 10 (15) percent would require keeping debt below 47 (57) percent of GDP.

(2) *simulating a distribution for future debt outcomes based on the past distribution of key macroeconomic variables*. This distribution embeds a fiscal reaction function estimated from past outcomes for Ecuador that yields an estimate of the primary balance, conditional on the macroeconomic outcomes for each stochastic simulation.

(3) *deriving a debt ceiling that ensures the probability of exceeding the maximum debt limit over the next six years is kept below 15 percent*. This would imply a debt ceiling of about 30 percent of GDP. A sensitivity exercise was also undertaken for different parameters for the maximum debt limit and for the likelihood of exceeding that ceiling.



Debt Ceiling -Estimated Past Behaviour

Probability of Debt Distress	Maximum Debt Limit (percent of GDP)	Debt Ceiling (percent of GDP) Risk Tolerance (percent)		
		5	10	15
5	32	4.4	7.7	10.7
10	47	17.3	22.4	25.1
15	57	26.3	31.7	34.7

Note: Debt ceiling obtained on the basis of estimated fiscal reaction function for a sample of commodity-exporting emerging markets.

Debt Ceiling - Market-led Fiscal Consolidation

Probability of Debt Distress	Maximum Debt Limit (percent of GDP)	Debt Ceiling (percent of GDP) Risk Tolerance (percent)		
		5	10	15
5	32	25.1	26.3	27.2
10	47	38.9	41	41.6
15	57	47.3	49.7	50.6

Note: Debt ceiling obtained on the basis of primary balance forecast path necessary to implement a fiscal adjustment capable of closing market

A separate exercise was conducted using the same methodology but assuming Ecuador’s fiscal reaction function is more prudent than that which prevailed historically. Such analysis shows that a 40 percent of GDP debt ceiling could be appropriate but only at risk tolerance levels and debt distress probabilities above 10 percent. In the longer term it would be desirable to reduce the debt ceiling to at least 30 percent.

[1] See Lledo, Sasson and Acevedo, “Enhancing Ecuador’s Fiscal Framework: Lessons from Second-Generation Rule-based Systems” IMF Working Paper, forthcoming, and ”Calibrating Ecuador’s Debt Ceiling” in Selected Issues and Analytical Notes.

Ecuador: Fiscal Consolidation Measures
(In percent of GDP – Non-financial public sector)

	2019	2020	2021	2019-2021
Revenue	**-0.3**	**1.4**	**-0.4**	**0.7**
2019 Tax reform	0.0	1.4	0.4	1.8
Earlier adopted tax changes 1/	-1.2	0.0	0.1	-1.0
Elimination of capital exit tax	0.0	0.0	-0.2	-0.2
Asset monetization (net) 2/	0.8	0.0	-0.8	0.0
Other revenues	0.1	0.1	0.0	0.2
Expenditure	**2.3**	**0.6**	**1.4**	**4.3**
Wages and salaries	0.5	0.3	0.2	1.0
Goods and services	0.5	0.1	0.1	0.8
Other spending	0.0	-0.1	0.0	-0.1
Capital spending 3/	0.0	0.4	0.6	0.9
Fuel subsidies 4/	1.7	-0.1	0.5	2.1
of which: Price Change	*1.3*	*-0.1*	*0.0*	*1.2*
Policy Change	*0.4*	*0.0*	*0.5*	*0.9*
Social spending	-0.4	0.0	0.0	-0.4
Total	**2.0**	**2.0**	**1.0**	**5.0**

Sources: Ministry of Finance and IMF staff calculations.

1/ For 2019, 1 percent of GDP is a one-off effect from tax amnesty collection in 2018, while 0.2 percent of GDP is the effect of other tax changes introduced in 2018.

2/ Refers to revenues from leasing of government assets to private sub-contractors for temporary use and maintenance. For 2019, this includes the proceeds from the concession of the Sopladora hydropower plant. For 2020, it includes the proceeds from the concession of electric lines.

3/ For 2019, the increase in capital spending following the implementation of the housing program "casa para todos" is broadly matched with capital cuts of similar amount in other areas.

4/ This includes: (i) increase in the price of retail, domestic and industrial gasoline, (ii) increase in the price of diesel for certain fishing categories, (iii) removal of the subsidies in industrial gas, and (iv) increase in the price of electricity.

- ***Realigning public sector wage bill.*** Public sector wages have risen 78 percent since 2007 and are now on average twice as high as private sector wages. In addition, public employment grew by 23 percent from 2005–15. The authorities intend to contain wage growth and reduce the workforce in various government entities, drawing on IMF technical assistance recommendations. To this end, the government has already announced a 10 percent reduction in the number of state enterprise workers, will renew only one of every two expiring contracts in the non-social sectors of the government, and will bring the wages of newly hired public employees into line with those prevailing in the private sector. These measures are expected to generate a cumulative reduction in the public wage bill of 1 percent of GDP by 2021, helping to restore competitiveness by also influencing private sector wage increases.

- ***Increasing social assistance spending.*** The phase-out in fuel subsidies and the projected slowdown in the economy will add to the need to support the poor and vulnerable through well-targeted social programs, including through the government's "Plan Toda Una Vida". To accommodate this need, the fiscal plan builds in an additional 0.4 percent of GDP of social assistance spending by the end of the program, phased in a front-loaded way to cushion the impact of reduction of fuel subsidies.

- ***Optimizing fuel subsidies.*** Untargeted fuel subsidies are currently around 3 percent of GDP. The authorities have already announced a reduction in subsidies on gasoline and industrial diesel. Also, since subsidies are ad valorem, the subsidy bill is being reduced in 2019 by the decline in global oil prices. Further subsidy reductions are planned for 2021. To ensure the phase-out of subsidies does not negatively impact the poor, the government is working with the World Bank to enhance the targeting and resources of the social safety net prior to any further reduction in subsidies for household consumption of fuel products. Subsidy reform will be carefully calibrated to promote social equity and efficiency and is not expected to have a major impact on retail consumer price levels.

- ***Greater efficiencies in goods and services spending.*** Improved procurement practices, in particular, in the health sector, and strengthening of controls on expenditure commitments will help support efforts to identify reductions in goods and services spending. At the same time, it will be important to ensure that service quality in the health care sector is not compromised. In addition, there will be small savings from reduction on travel expenses.

- ***Reductions in capital spending.*** Ecuador has very high levels of public capital spending relative to others in the region. However, there is evidence that part of the expenditure recorded under the capital spending—possibly as much as 20 percent—is misclassified current spending. The government intends to reduce capital spending by about 1 percent of GDP by 2021, largely through a better prioritization of projects and improvements in procurement practices.

23. The authorities also intend to take steps to improve public debt management. These include developing a domestic debt market by (i) phasing out direct placements; (ii) issuing benchmark securities through auction mechanisms, and (iii) accepting market interest rates for those issuances. The authorities intend to take steps to enhance communication with market participants, to improve debt statistics, and to formulate and publish a medium-term debt management strategy.

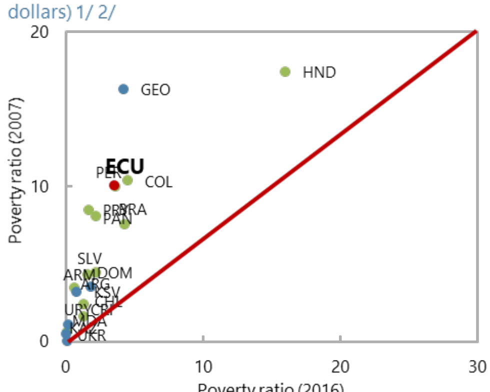
B. Promoting Shared Prosperity and Protecting the Poor and Vulnerable

24. Over the past decades, Ecuador has made important gains in social outcomes. The percentage of the population living below the national poverty line has fallen from 36.7 percent in 2007 to 21.5 percent in 2017 and the share of the population living below US$1.90 a day fell from 10 percent in 2007 to 3.6 percent in 2016. Nonetheless, poverty rates among the rural and indigenous populations remain high. Ecuador's public health and education spending, literacy and school enrollment, and life expectancy are broadly in line with the Latin American average (although infant mortality and malnutrition rates are high). Social assistance spending is high by regional standards and there is good coverage of those in the bottom 20 percent of the income distribution.

25. The authorities, however, see scope to do more by:

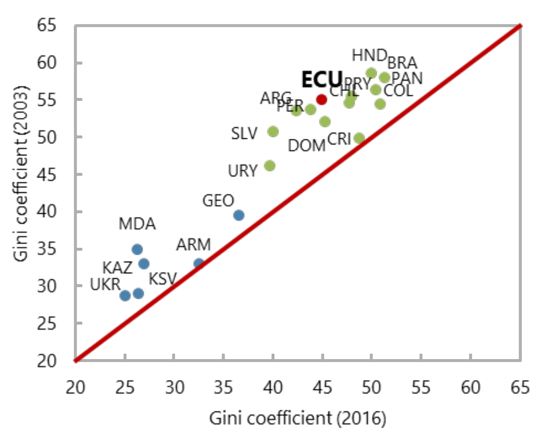
- Extending coverage, and increasing the level of benefits, under the existing "*Bono de Desarrollo Humano*" conditional cash transfer program (the current coverage is limited to about 40 percent of those households that are living in poverty).
- Increasing spending to support the disabled poor (such as "*Bono Joaquín Gallegos Lara*").
- In consultation with the World Bank, developing a plan to improve the targeting of social programs to ensure that the bulk of expenditures goes to the bottom 20 percent of the income distribution. This will include the development of social registry to improve targeting of social programs.
- Extending the coverage, maintaining the nominal level of benefits, and improving the targeting of the non-contributory pension (in consultation with World Bank technical support).
- Increasing the efficiency and quality of primary education and health spending to improve outcomes and enhance the quality of the labor force and external competitiveness of the economy (with technical support from other IFIs). A plan to achieve this objective would be published by end-September 2019.

Selected EM: Poverty Headcount Ratio, 2007 and 2016
(percent of population living under 1.9 constant 2011 PPP dollars) 1/ 2/



Source: World Development Indicators.
1/ Green dots correspond to LAC countries.
2/ 2015 numbers used in Poverty Headcount Ratio for Chile, Brazil, and Kazakhstan.

Selected EM: Gini Coefficient , 2003 and 2016 1/



Source: World Development Indicators.
1/ Green dots correspond to LAC countries.

C. A Better Medium-Term Fiscal Framework

26. Passage of the Productive Development Law and its regulations was an important step forward and further measures are being planned to make the new fiscal framework more effective (drawing on technical assistance recommendations outlined in Box 3). Future changes would include steps to complement the expenditure growth rule with binding annual targets for the non-oil primary balance, to ensure the institutional coverage of the debt and expenditure rule apply to the consolidated nonfinancial public sector (measured in line with international standards), and to strengthen the consistency and the enforceability of the framework. Such changes would be critical to contain Ecuador's historical overspending during oil price booms thus allowing for countercyclical policies during oil price busts and preserving fiscal sustainability over the entire cycle. The government also intends to introduce legislative reforms to modernize budget processes, strengthen internal and external controls, and improve fiscal transparency, bringing such areas into line with international best practice. These efforts will be guided by a public financial management action plan that will be developed with technical assistance providers.

Box 3. Priority Changes to the Fiscal Framework

Fiscal Rules. The following legal changes should strengthen rule design and implementation:

- Establish the necessary mechanism to ensure the effective operation of the expenditure rule underpinning the fiscal framework and its consistency with the Constitutional "golden rule" provision.
- Modify definitions to ensure that the expenditure rule and debt anchor applies to the nonfinancial public sector.
- Establish binding annual targets for the non-oil primary balance consistent with the debt anchor within a fully articulated medium-term fiscal framework
- Specify explicit escape clauses, automatic correction mechanisms (for deviations from the rules), and in-year fiscal reporting to strengthen enforcement.
- Ensure rules dictating the accumulation of assets for the stabilization fund do not jeopardize compliance with fiscal rules and the fiscal plan.
- Over the medium-term, consider lowering the debt ceiling below 40 percent to build additional fiscal buffers following oil price booms.

Budget Preparation, Execution and Control. The following changes in legislation and procedures should strengthen budget processes:

- Limit the Executive discretion to amend the budget and introduce a robust framework for allocating budget contingencies so as to give appropriate flexibility in budget execution.
- Prepare the annual budget through a top-down, medium-term, and transparent process including by changing procedures that fragment budget formulation and approval of capital and current expenditures.
- Impose on all central government entities hard annual budget and medium-term expenditure ceilings that are consistent with the overall fiscal framework.
- Develop, implement, and disseminate a mandatory methodology for cash projections
- Prepare a plan for the reduction in the current stock of Treasury Certificates (possibly with some of the stock swapped for government bonds) and restrict new issuance to facilitate cash management only. For fiscal policy purposes such instruments should be considered as part of the existing stock of public debt.
- Strengthen budget controls, including by ensuring central government entities enter their expenditure commitments into Ecuador's information management system (E-SIGEF).
- Enhance budget execution by eliminating the Cuenta de Financiamento de Derivados Deficitarios from the central government budget and recording it instead as current transfers.

Box 3. Priority Changes to the Fiscal Framework (concluded)

- Improve legislation, information collection systems, and procedures and perform a survey to identify, prevent, and clear domestic arrears, including by strengthening the system for commitment controls.

Fiscal Transparency. More transparent practices should include the publication of:

- A summary of the fiscal measures underpinning the budget with a full quantification and a statement of fiscal risks in the draft budget submitted to Parliament.
- Quarterly fiscal reports that monitor budget execution and the government's compliance with fiscal rules.

Undertaking a Fiscal Transparency assessment may provide useful guidance.

Over the medium to long-term, reforms should turn the fiscal framework more appropriate for resource-dependent economies that would build liquid financial assets (managed through a sovereign wealth fund); adopt net (financial) wealth as the fiscal anchor; and undertake a broad societal debate on how, or whether, net wealth should be transferred between generations.

27. Efforts are underway to increase fiscal transparency and adopt consistent international standards for the reporting of the public debt. The recent publication of public debt data in a manner that more closely matches international standards is an important step forward. The government is committed to quickly bringing all of its fiscal reporting in line with international standards (including by providing a detailed list of debt instruments by creditor and compiling public sector debt on a consolidated basis). Later this year, the government will begin publishing quarterly fiscal reports on budget execution of the nonfinancial public sector that will include an assessment of the government's compliance with the fiscal rules.

28. The central bank has recently published its financial statements. In line with recommendations from the Fund's safeguards mission, the authorities intend to change legislation to allow the publication of the auditors' opinion and notes on the financial accounts of the central bank (to bring such reporting into line with international best practice). The authorities are committed to implementing the International Financial Reporting Standards for the central bank's accounts in a phased way in the coming years.

29. The government intends to increase the transparency of the oil sector. This will include publishing audited financial statements of the state-owned oil companies, increasing the transparency of employment policies in oil companies, and reviewing the governance structure of these oil companies. Ecuador is also working to gain membership of Extractive Industries Transparency Initiative.

30. The Moreno administration is taking steps to improve governance and tackle corruption. A transitional Citizens' Participation and Social Control Council was appointed to oversee government operations and a Presidential corruption task force has been established. The latter has highlighted the need to (i) enhance the independence and powers of law enforcement agencies and the judiciary; (ii) strengthen domestic and international coordination on anti-corruption among different agencies; (iii) improve access to information about government operations (so as to facilitate civil society oversight) and (iv) strengthen procurement processes (including by statutorily requiring that all procurements contracts, and the winning bids/companies are published). To implement these changes the government will soon submit comprehensive anti-corruption legislation to the National Assembly. Finally, work is underway to improve the asset declaration regime for senior government officials.

31. The government is planning to strengthen the effectiveness of the AML/CFT framework to support anti-corruption efforts. In line with the FATF recommendations, an AML/CFT national risk assessment that gives proper consideration to corruption-related threats is being developed. The government will aim to ensure that banks and other relevant entities monitor their business relationships with senior officials. Additionally, they will ensure that proceeds of acts of corruption (as defined by the UN Convention Against Corruption) can be frozen, seized and confiscated.

D. A Stronger and More Independent Central Bank

32. The government intends to fully prohibit all direct and indirect central bank financing of the government and nonfinancial public sector. This prohibition will cover all types of direct and indirect financing, including the purchase of bonds issued by publicly owned enterprises and temporary advances, lending, the provision of guarantees to the government, its agencies, and state-owned entities. In 2016−17, the government drew around US$4.5 billion in central bank financing for the budget and has been using central bank resources to fund state banks and support quasi-fiscal operations. The 2018 Law on Productive Development has already introduced a number of welcome changes including a prohibition (i) on the purchase of new public securities by the central bank and (ii) of new central bank funding to public banks that is subsequently invested in securities issued by public sector entities[9]. This will allow the stock of these nonfinancial public sector obligations to the central bank to be reduced as they mature. The Monetary Board has recently adopted an additional measure to prohibit any increase in the central bank's domestic investment operations. Central bank emergency liquidity support to public banks would be preserved, however, consistent with prudential norms. The intention is that these prohibitions will be formalized later this year in amendments to the Monetary and Financial Organic Code.

33. A new legal framework will be introduced requiring the central bank, over time, to cover all its liabilities vis-à-vis banks with international reserves. This would be consistent with the need in dollarized economies for a backing rule that backs specific central bank liabilities (i.e. private and public bank reserves at the central bank and domestic currency (coins) in circulation) with international reserve assets. A transition period is needed, however, before sufficient reserves can be accumulated to fully meet this requirement.

[9] Public banks will, however, be allowed to hold government securities, as part of their operational activities, up to the prudential limits applicable to other institutions and funded by their own liquid resources.

34. Drawing on Fund technical assistance, further steps are intended to strengthen the central bank's institutional framework. The central bank's current legal framework contains multiple and unwieldy objectives and functions; the government intends to streamline these in line with best practice for dollarized economies. There are plans also to improve the central bank's governance arrangement and institutional autonomy including through the introduction of an independent central bank Board that has fiduciary responsibilities toward the central bank (the Board would take over responsibilities of the existing Monetary Board composed of ministerial representatives and a delegate representing the President). The central bank's financial autonomy and personal autonomy (i.e. the criteria and procedures for the appointment and dismissal of Board members) will also be strengthened and strong internal mechanisms will be introduced to ensure proper audit and accountability. In this respect, an Audit Committee, which is currently lacking, will be introduced and the central bank's Internal Audit function will be reformed in line with best practice. In the medium term, the authorities intend to strengthen the BCE's balance sheet, including by dealing with contingent liabilities linked to the legacy of the liquidated banks from the crisis in the 90s.

E. A More Resilient Financial System

35. The financial system remains stable although liquidity conditions are tightening. Deposits and credit contracted in 2015 but those pressures eased in 2016 as oil prices recovered and new regulations required commercial banks to repatriate overseas assets. Capital to risk-weighted assets is 13.4 percent, 3 percent of bank loans are nonperforming, and liquid assets are 28 percent of short-term liabilities. Nonetheless, private credit is growing at 15 percent y-o-y (largely financing household consumption) while deposits have been flat over the past year. This has eaten into bank liquidity and could raise the prospects for nonperforming loans in the future. Liquidity risks could also materialize if oil prices decline further. There have been some reports of rapid growth and increasing stress in cooperatives—which account for 16 percent of total system assets and 23 percent of total deposits. While the expansion of cooperatives is unlikely to create systemic strains, tighter financial supervision of these entities is warranted, in part to prevent regulatory arbitrage.[10,11]

36. Impediments to effective financial intermediation and sovereign-financial linkages need to be addressed. The total exposure of the commercial banking system to the central government and public banks represents about 38 percent of banks' net worth (mostly in central government paper). This partly is a result of various liquidity requirements (e.g. at least 60 percent of liquid assets have to be domestic assets and about 17 percent of deposits have to either be deposited at the central bank or held in other liquid instruments). To move toward a more competitive financial system, ceilings on interest rates should be eliminated (so as to allow financial

[10] In recent years, the superintendency of cooperatives has implemented the liquidation, merger, and absorption of many small entities without noticeable impact on stability. However, further consolidation of somewhat larger institutions will require specific contingency plans and an appropriate safety net to avoid spillovers in the system.

[11] See "The Cooperative Sector in Ecuador" in Selected Issues and Analytical Notes.

resources to be allocated according to relative risk and term) and the complex system of bank liquidity regulations should be replaced with minimum liquidity requirements that are aligned with international best practices. The authorities intend to work in this direction and will articulate a clear plan of action for such reforms during the course of the arrangement, drawing on planned Fund technical assistance.

37. The government intends to improve financial oversight and crisis preparedness by:

- Enhancing the banking resolution and crisis preparedness framework, including by reviewing the adequacy of the financial safety net (i.e. the deposit insurance scheme and the Liquidity Fund) coverage parameters and more clearly defining the deposit insurance fund's role in bank resolution. This may encompass changes to institutional arrangements and the legal powers of the regulatory agencies (the authorities have requested technical assistance in these areas).

- Enhancing the effectiveness of financial oversight by monitoring household indebtedness, collecting information on housing prices, and possibly imposing prudential limits on loan-to-value and debt-to-income ratios; and examining the need for cyclical factors in certain regulatory requirements.

- Supporting the recently-started diversification of the deposit insurance fund's assets away from Ecuadorian sovereign risks.

F. Reducing Labor Market Rigidities and Improving Competitiveness

38. The government intends to support the needed strengthening of the external position through a combination of supply side measures:

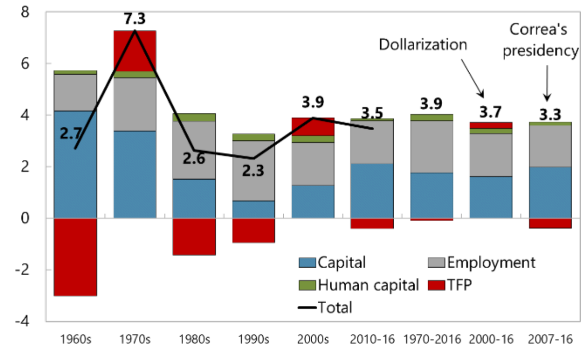
- Allowing for less-rigid labor contracts that can particularly support an increase in female labor force participation and youth employment opportunities. Policies supporting families with young children and ensuring provision of childcare programs will be continued.

- Increasing the probation period prior to an open-ended contract (after the probation period the employee becomes entitled to significant protections including severance payments). This would make hiring more attractive and support job creation.

- Reducing hiring and firing costs by eliminating severance payments for workers that voluntarily resign.

39. There is also scope for public policy to foster higher private sector productivity. Total factor productivity growth in Ecuador has been negative for much of the past decade.[12] Future increases in productivity will necessarily need to be sourced in private sector investments but there is a role for the government to support these private efforts by:

Ecuador: Contributions to Growth, 1960-2016
(In percent)



Sources: Central Bank of Ecuador, Penn World Table v9.0, and IMF staff calculations.

- Building a framework for public private partnerships to attract private capital into a range of infrastructure investments (which would both support a rise in productivity and lessen fiscal needs).

- Allowing private sector companies to take over the operations of certain public functions as concessions (potentially including airlines, utilities and other publicly owned enterprises) while retaining the ownership of these entities in public hands. The expected efficiency gains will help lower production costs, increase economy-wide productivity, and support diversification.

- Continuing the process of trade liberalization by seeking trade agreements with both regional and international partners. For example, Ecuador is committed to join the Pacific Alliance in the near future. Such an increase in international economic integration will facilitate private sector led-growth and ultimately raise living standards.

PROGRAM MODALITIES

40. Balance of payments need. Ecuador faces high gross external financing needs in an environment of tightening global financing conditions and, more recently, deteriorating terms-of-trade. International reserves are low, the country faces significant BOP vulnerabilities (which give rise to a clear BOP need), and the real effective exchange rate is overvalued. In this context, Fund resources, in the form of direct budget support, would provide the needed near-term balance of payments financing on favorable terms as the country improves its fiscal position. With the better fiscal outturn, gross international reserves are expected to increase to 63 percent of the ARA metric by the end of the arrangement.

41. Access and phasing. Access for the 3-year Extended Arrangement is proposed at US$4.209 billion (435 percent of quota, SDR 3.035 billion, or about 4 percent of GDP). Access will be made available upon completion of quarterly reviews of the program with the first review to be considered by the Board in June 2019, based on end-March performance criteria.

[12] See "Potential Output, GDP Nowcasting and Forecasting" in Selected Issues and Analytical Notes.

42. Budget support. It is proposed that the full amount of Fund access under the arrangement would be used for direct budget support. Fund resources would be deposited in the Treasury's account at the Central Bank of Ecuador and drawn down, as needed, to finance the budget. A memorandum of understanding will be established between the central bank and the government on their respective roles and obligations.

43. Conditionality and monitoring. Program performance would be monitored by quarterly reviews (see Table 1 of Attachment I) with:

- A floor on the non-oil primary balance, inclusive of spending on fuel subsidies, of the nonfinancial public sector (quantitative performance criterion, QPC).
- Non-accumulation of external payment arrears by the nonfinancial public sector (continuous performance criterion (PC)).
- A floor on the change in the stock of central bank's net international reserves (NIR), excluding bank deposits held at the Central Bank (QPC). While the program assumes no new market issuance by the government during the course of the arrangement, if there were to be new market financing then an adjustor to the NIR floor would automatically require that those resources be held in the nonfinancial public sector's deposits at the central bank (so boosting net international reserves).
- Zero new gross central bank financing of the non-financial public sector, either directly or indirectly through publicly owned banks (continuous PC).
- A floor on social assistance spending of the central government (QPC).
- A floor on the overall balance of the nonfinancial public sector (indicative target (IT)).

44. Ecuador has entered into certain sovereign repurchase agreements and other borrowing arrangements with collateral-like features (Box 4). The authorities have committed not to enter into new sovereign repurchase agreements or borrowing that encumbers international reserves during the period of the arrangement. They have also committed to providing full information on past and future borrowing with collateral-like features.

Box 4. Selected Borrowing Arrangements

Ecuador does not have any borrowing arrangements that, legally, would be considered collateralized. However, it has other types of non-standard borrowing arrangements.

Repurchase Agreements and Derivatives Agreements (current debt stock less than US$1.5 billion). Sovereign derivatives and repo agreements using gold reserves and government bonds. The Ministry of Economy and Finance of Ecuador and the Central Bank of Ecuador have collectively entered into two sovereign repurchase agreement operations and one derivatives agreement with international banks. The derivatives transaction involved the delivery of a combination of gold and bonds issued by the Republic of Ecuador to the international bank with gold being replaced on the central bank's balance sheet with derivatives. This gold is excluded from the measurement of gross and net international reserves for purposes of program conditionality. On the date of the derivatives transaction, the government received a loan of US$500 million from the international bank. Both the derivatives transaction and the loan have a term of 35-months, expiring in September 2020. The two repurchase agreements included delivery only of bonds of the Republic of Ecuador to the international banks. The government has received a total of US$1 billion in the course of the two transactions.

Borrowing with restricted funds (current stock of approximately US$3.5 billion) from certain Chinese banks. Ecuador sells a significant share of its oil revenues through off-take agreements with a range of global oil and petrochemical companies. Some of these off-take contracts were entered into in connection with multiparty agreements relating to loans provided by Chinese banks to the government of Ecuador. Some of these contracts also have 'tie ins' (contratos atados) involving tranches that are borrowed and paid in renminbi for specific projects selected by the Ecuadorian government and approved by the lender.

45. As prior actions, the government has already:

- Prohibited quasi-fiscal operations of the Central Bank, as well as any direct or indirect lending to the non-financial public sector, including that via public banks, through a decision of the Monetary Board (Junta de Política y Regulación Monetaria y Financiera).
- Published the Central Bank's financial statements.
- Provided detailed information on external non-financial public-sector debt, including information on all collateralized debt and debt with similar arrangements. This has allowed staff to compile accurate data on the consolidated non-financial public debt stock based on the GFSM2014 manual.

A range of structural benchmarks has also been established (see Table 2 of Attachment I).

46. Financing Assurances. The program is fully financed, given firm commitments for financing in the first 12 months of the arrangement as well as good prospects for full financing thereafter. The remainder of the gross external financing need in 2019 is expected to be met from IFI disbursements, including Fund budget support. This assessment is based on a comprehensive evaluation of the gross external and fiscal financing needs for the course of the arrangement. The current lending plans of the World Bank, Interamerican Development Bank, CAF, and FLAR have been verified with the various lenders and built into the current framework.

47. Capacity to Repay. Under the program scenario, Ecuador's capacity to repay is adequate. If all purchases are made as scheduled, Ecuador's projected payments obligations to the Fund would peak in 2026 at SDR 0.586 billion, placing a premium on safeguarding Fund resources well beyond the program period. Obligations relative to exports and reserves are at the high end compared with other program cases (since Ecuador is fully dollarized, it does not have the option of exchange rate depreciation to preserve international reserves and ensure its capacity to service debt). The existing stock of collateralized borrowing is assessed not to have a significant impact on Ecuador's capacity to repay. Assuming steadfast program implementation, public debt is expected to be sustainable and a successful IMF-supported program is expected to reduce perceived sovereign and balance of payments risks, lower spreads on sovereign debt (Box 5), and facilitate improved financing terms for both the private and public sector. This will serve to mitigate the risks to repayment to the Fund.

48. Lending into arrears. Ecuador maintains a residual amount of arrears to international private bond holders arising from outstanding claims on those international bonds that the authorities repudiated in 2008/2009. At that time, the majority of government obligations were repurchased by the government. However, US$52 million (including accrued interests) remain outstanding in the hands of individual creditors and the authorities have been unable to identify these creditors in order to settle the claims. The authorities have, however, contracted the services of an international advisor to search for, identify, contact, and negotiate with these outstanding bondholders. Staff's judges that good faith efforts have been made to reach a collaborative agreement with the remaining creditors and will continue to monitor evolving relations with these creditors, confirming, at each review, that the requirements under the policy on lending into arrears have been met. The authorities have indicated they have no outstanding arrears to bilateral or multilateral creditors.

49. Safeguards Assessment. The safeguards assessment of the BCE will be updated before the first program review. The most recent assessment, finalized in June 2017, raised serious concerns regarding the BCE's institutional framework. The BCE's subordination to the government and lack of autonomous objectives did not provide a sound system for the management of the bank's resources, including IMF disbursements. The program includes structural reforms to restore BCE's autonomy, and to strengthen its governance and accountability.

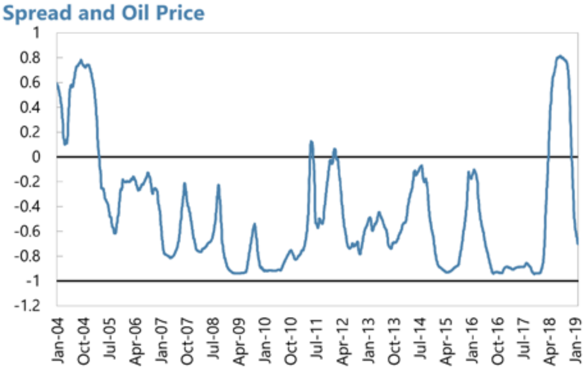
50. Statistical Issues. The authorities have received, and will continue to receive, technical assistance on government finance statistics, national accounts, balance of payments, and monetary and financial sector statistics.

Box 5. Determinants of Ecuador's Spreads[1]

Using the method proposed by Jorda (2005), the relationship between Ecuador's EMBI spreads and various determinants is estimated based on an unbalanced panel of 60 emerging market (EM) economies over the period 1990−2017. The estimated model suggests that:

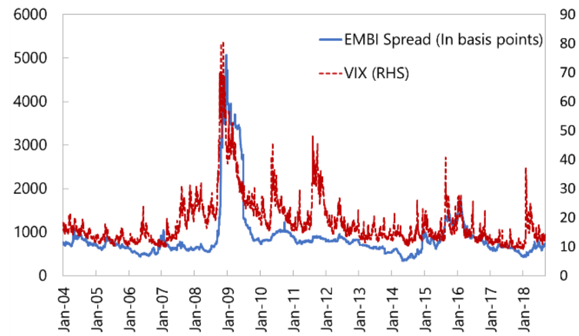
- The EMBI spread in Ecuador is negatively correlated with oil prices and positively correlated with global risk-aversion. Movements in global risk aversion have a bigger effect on borrowing costs for countries that have had past credit events.
- An improvement in the cyclically adjusted primary balance of 1 percent of GDP can reduce the EMBI spread by about 34bps. In addition, a 1 percent of GDP reduction in public debt reduces the EMBI spread by 7bps. This would suggest that the fiscal consolidation and reduction in the debt-to-GDP ratio under the authorities' policy plan could lower Ecuador's sovereign spread by 175 basis points.

Ecuador: 12-month Rolling Correlation between EMBI Spread and Oil Price



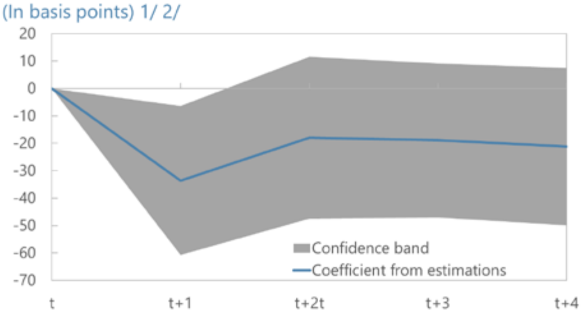
Sources: Bloomberg and IMF staff calculations.

Ecuador: EMBI Spread and VIX



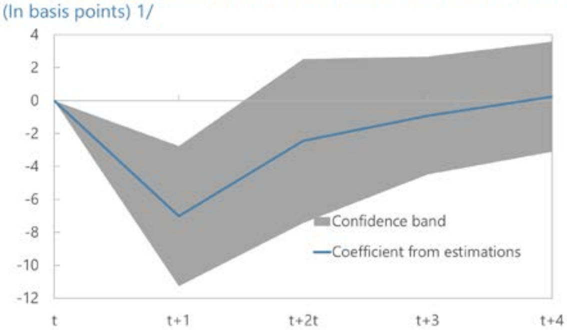
Source: Bloomberg.

Impact on EMBI Spread of a 1 Percent Reduction in CAPB
(In basis points) 1/ 2/



Sources: Bloomberg, WEO, ICRG, and IMF Staff calculations.
1/ CAPB refers to the Cyclically-Adjusted Primary Balance.
2/ Estimated on a sample of oil-exporting emerging market economies.

Impact on EMBI Spread of a 1 Percent Reduction in Debt-to-GDP
(In basis points) 1/



Sources: Bloomberg, WEO, ICRG, and IMF Staff calculations.
1/ Estimated on a sample of oil-exporting emerging market economies.

[1] See "EMBI Spreads: External Factors, and the Impact of Fiscal Consolidation" in Selected Issues and Analytical Notes.

STAFF APPRAISAL

51. **Ecuador is making important efforts to modernize its economy and strengthen the foundations for dynamic, sustainable, and inclusive growth**. These planned actions—to strengthen the fiscal position and increase competitiveness—will help reduce vulnerabilities, put dollarization on a stronger footing, and, over time, support growth and job creation. This will help protect Ecuador from a range of risks including those associated with a tightening of global financial conditions, global trade uncertainties, lower international oil prices, or the potential for a stronger U.S. dollar.

52. **Restoring prudence to fiscal policy will help achieve fiscal sustainability and improve competitiveness.** Government plans to reduce non-oil primary deficit including fuel subsidies by 5 percent of GDP over the next three years would reverse the upward trend in public debt and bring it to more prudent levels in the medium term. A broad-based fiscal reform, which addresses both excessive public spending and inefficiencies in the tax system, would go a long way in fulfilling this objective. Realignment of the public sector wage bill, an optimization of the system of fuel subsidies, and reduction in public spending on capital and goods and services are important components of expenditure reform. The tax reform should aim to make the tax system more equitable, growth-friendly, and simpler. While these fiscal efforts might in the near-term generate headwinds to growth they will lay the foundation for a more sustainable and equitable growth in the future.

53. **The efforts being taken to lower the debt-to-GDP ratio and to complement the existing expenditure growth rule with annual targets for the non-oil primary balance will strengthen confidence in the government's fiscal plans**. The intention to increase transparency and accountability through the publication of timely and periodic in-year fiscal reports to assess compliance with fiscal rules will further strengthen the credibility of the fiscal responsibility framework. Over time, better public financial management systems, improved budget procedures, improved procurement practices, and more rigorous fiscal controls will increase the effectiveness and efficiency of fiscal operations.

54. **It is essential to maintain the government's strong commitment to protecting the poor.** To prevent a deterioration of social conditions and maintain societal support for their economic plan, the government should move as quickly as possible to expand eligibility for social assistance, improve targeting, and increase the generosity of social assistance programs. This will also be an important prerequisite for further steps in phasing out the existing system of untargeted fuel subsidies. Over time, greater access to high quality primary education and health care will help build human capital and offer a path of opportunity and upward social mobility to all of Ecuador's citizens.

55. **Increasing competitiveness and productivity needs to be at the core of supply-side efforts**. Reforms to create a more efficient tax system, maintain restraint in public wages, eliminate rigidities in wages and prices, improve the reliability and efficiency of the energy sector and capital markets, and tackle corruption will all contribute to a more vibrant, private sector-led growth model.

There is also scope to remove trade barriers, improve the business climate, and create opportunities for greater private sector involvement both in infrastructure provision and in a range of services that are currently being provided by public entities.

56. Building financial resilience, removing impediments to effective financial intermediation, and strengthening the governance framework of the central bank will support the dollarized system. The planned efforts to further strengthen oversight for banks and cooperatives and to build up crisis-preparedness and contingency-planning capabilities will help Ecuador both anticipate and adapt to potential shocks. Going forward, it will be important to redesign the complex system of bank liquidity regulations and interest rate ceilings so as to simplify the system and support greater access to financial intermediation. The proposed steps to make the central bank more operationally independent, to strengthen its governance, and to prohibit it from providing fiscal financing will have an important impact in bolstering dollarization.

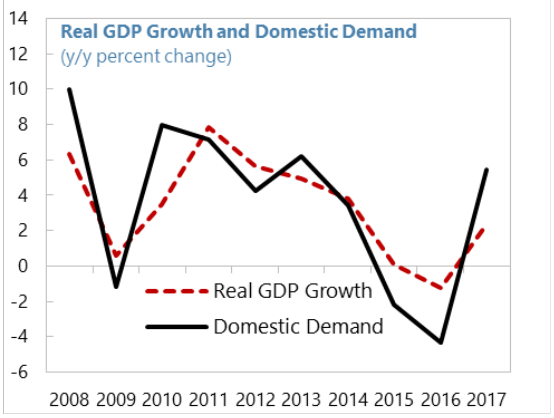
57. Staff fully supports the authorities' request for a 36-month Extended Fund Facility. The government's economic plans are well-designed to reduce Ecuador's vulnerability to downside risks, protect society's most vulnerable, and support growth and job creation. The efforts of the Ecuadorian government merit the support of the international community.

58. Staff also supports Board approval for the retention for a one-year period of the exchange restriction arising from the foreign exchange outflow tax given that it is maintained for BOP reasons, is temporary and non-discriminatory.

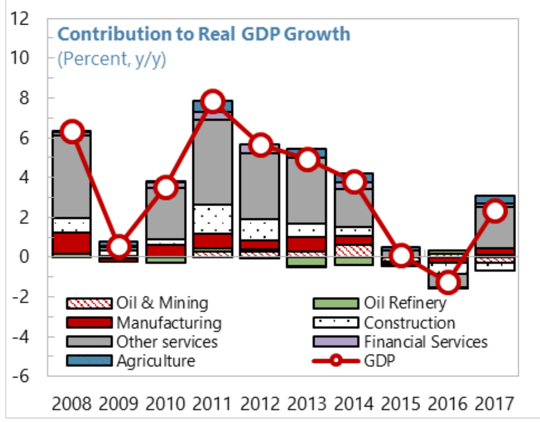
59. It is recommended that the next Article IV consultation takes place on a 24-month cycle.

Figure 1. Ecuador: Recent Economic Developments

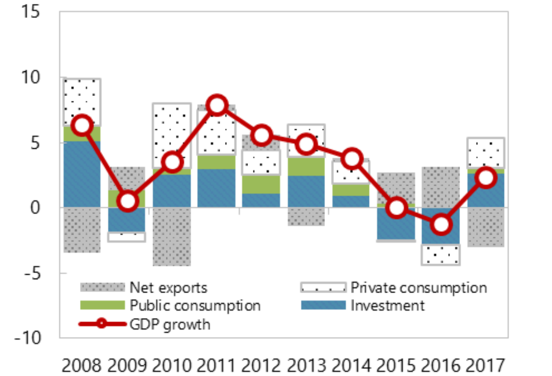
Growth started to recover in late 2016.



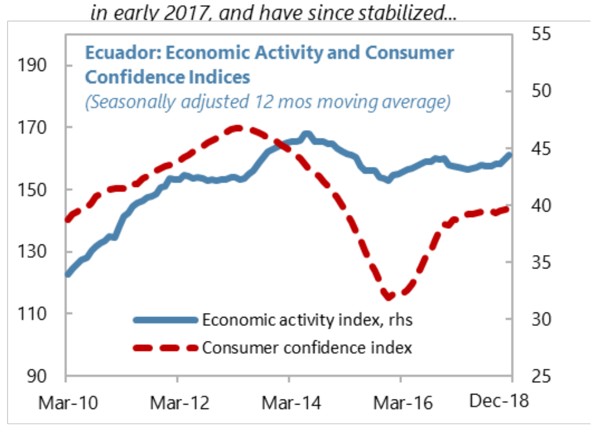
Other services were the main drivers behind 2017's recovery, but construction continued to be a drag on growth.



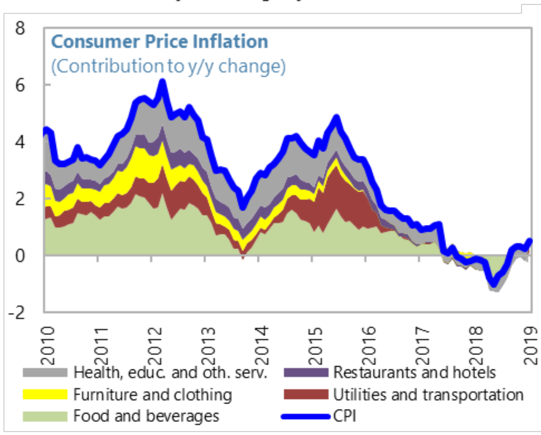
On the demand side, private consumption, and investment lead the rebound in 2017.



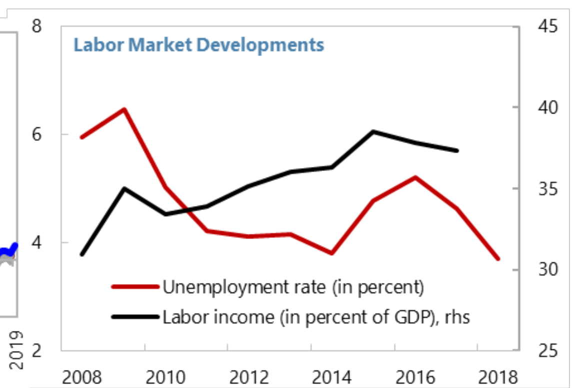
Consumer confidence and economic activity recovered in early 2017, and have since stabilized...



Deflationary pressures have started to subside and recently have slightly reversed.

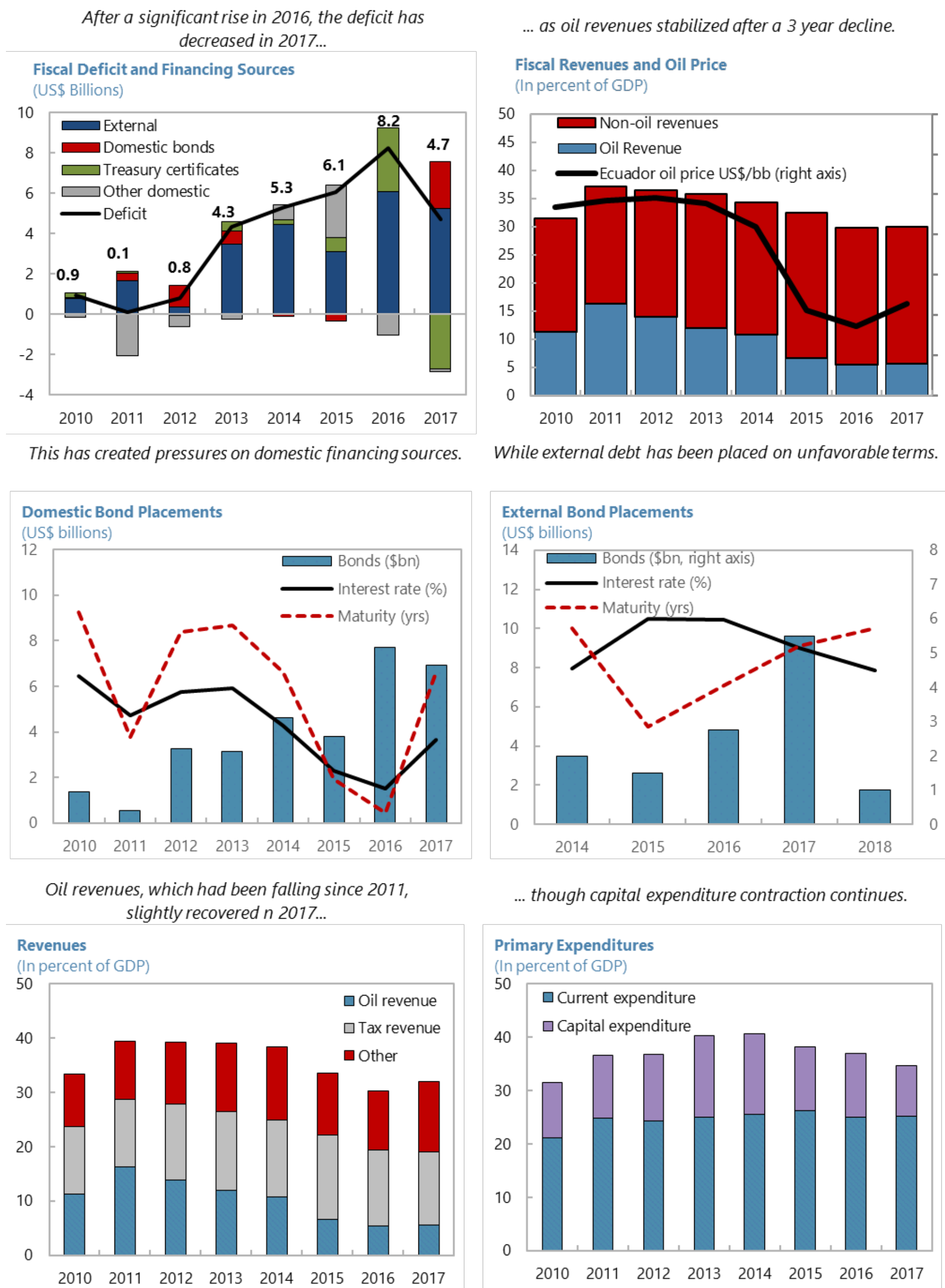


Unemployment has returned to pre-crisis levels.



Sources: Central Bank of Ecuador; National Statistical Institute of Ecuador (INEC); World Economic Outlook Database; and IMF staff calculations.

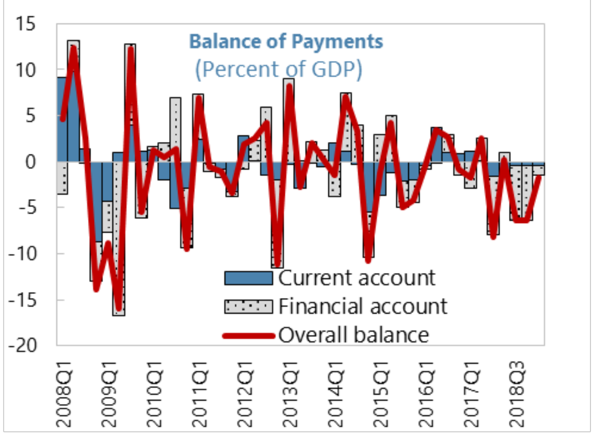
Figure 2. Ecuador: Fiscal Developments



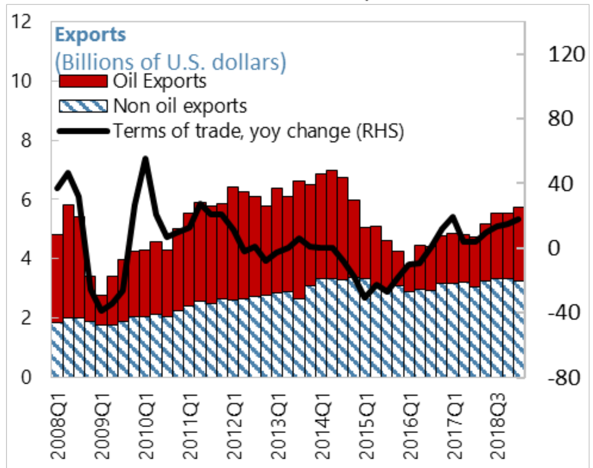
Sources: Central Bank of Ecuador, Ministry of Finance, Haver, and IMF staff calculations.

Figure 3. Ecuador: A Vulnerable External Position

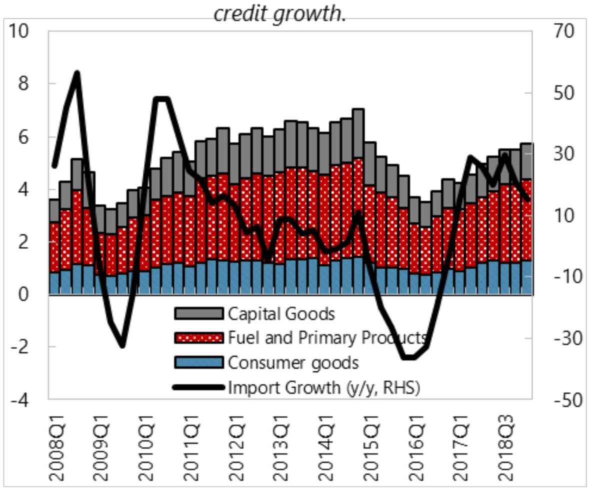
The current account turned negative in the second half of 2017...



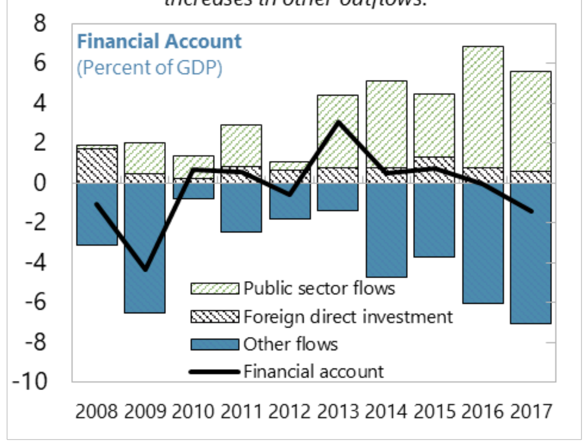
...due to low oil exports...



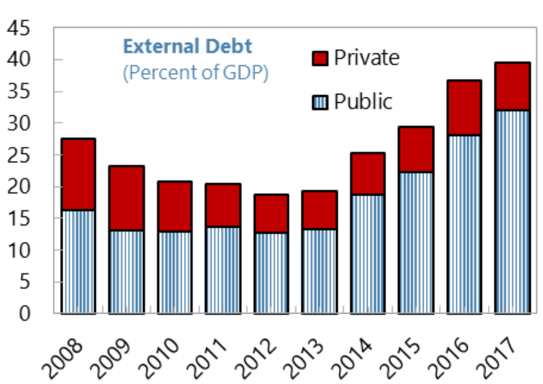
... and fast import growth caused by the lifting of the BOP safeguards and acceleration of credit growth.



High public sector borrowing was outweighed by sharp increases in other outflows.



External debt levels have been increasing....



...and international reserves remain very low.

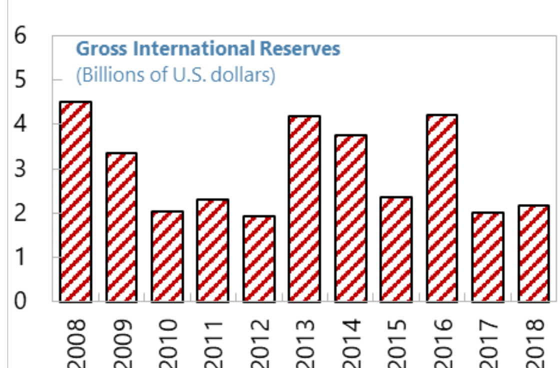
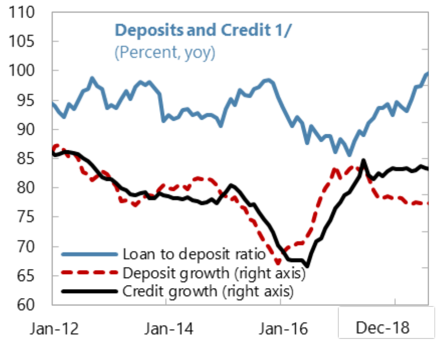
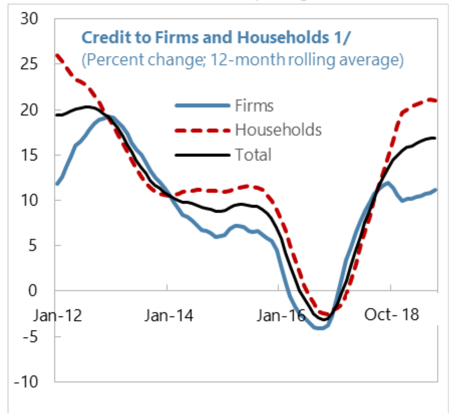


Figure 4. Ecuador: The Financial System has Recovered

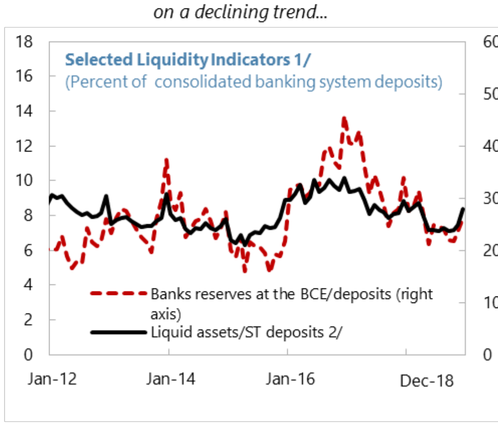
The strong pace of credit growth has been sustained, while deposit growth has been muted



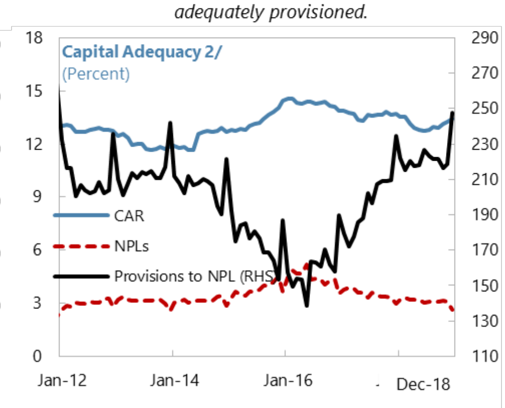
... with credit to households outpacing credit to firms.



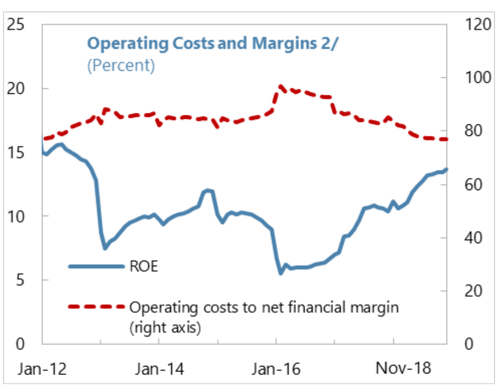
Banks' liquidity positions are still comfortable, but are on a declining trend...



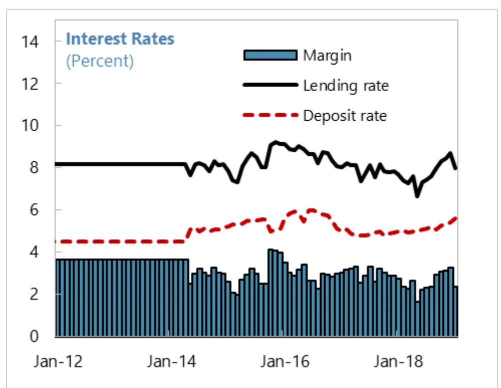
... capital ratios are adequate and NPLs are low and adequately provisioned.



Profitability has recovered, but operating costs are relatively high...



... while lending rates have begun to increase.



Sources: Central Bank of Ecuador; Superintendency of Banks; IMF Monetary and Financial Statistics; and IMF staff calculations and estimates.

1/ Data corresponds to Other Depository Institutions, which include private banks, *Banecuador*, *Banco del Pacifico*, private financial companies, mutualists, cooperatives, and credit card companies.

2/ Data corresponds to the private banks aggregate, which includes *Banco del Pacifico*.

Table 1. Ecuador: Selected Economic and Financial Indicators

				Prel.	Est.	Projections				
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Social Indicators										
Life expectancy at birth (years)	75.9	76.1	76.3							
Infant mortality (per thousand live births)	18.9	18.3	17.8							
Adult literacy rate	94.2	94.5	94.4							
Poverty rate at national line (total)	22.5	23.3	22.9	21.5						
Unemployment rate	3.8	4.8	5.2	4.6	3.7	4.3	4.7	4.8	4.6	4.5
Population (millions)	16.0	16.3	16.5	16.8	17.0	17.3	17.5	17.8	18.0	18.3
	(Percent change, unless otherwise indicated)									
National income and prices										
Real GDP	3.8	0.1	-1.2	2.4	1.1	-0.5	0.2	1.2	2.7	2.3
Domestic demand (contribution to growth)	3.6	-2.2	-4.3	5.3	3.4	-3.5	-1.1	1.2	2.6	2.0
External Demand (contribution to growth)	0.2	2.3	3.1	-3.0	-2.3	3.1	1.2	0.1	0.1	0.3
Consumer price index period average	3.6	4.0	1.7	0.4	-0.2	0.6	1.2	1.6	1.3	1.1
Consumer price index end-of-period	3.7	3.4	1.1	-0.2	0.3	0.5	1.6	1.5	1.2	1.0
Banking system										
Net domestic assets	20.7	1.4	20.6	18.3	7.5	-2.9	2.6	-1.2	9.8	7.2
Liabilities	11.0	-6.2	21.3	9.4	4.6	2.8	5.4	6.8	7.8	7.4
Credit to the private sector	8.7	-3.4	6.2	16.4	14.9	4.4	5.7	8.2	7.1	6.7
External sector										
Exports	4.8	-25.9	-8.7	12.0	12.8	0.1	4.5	1.5	3.1	3.5
Oil	-5.9	-49.8	-18.0	26.6	27.3	-8.7	4.6	-7.9	1.1	1.4
Non-oil	16.0	-7.0	-3.4	6.2	5.0	5.6	4.4	6.4	3.9	4.4
Imports	2.0	-20.8	-20.3	18.6	13.6	-6.5	0.5	2.1	3.9	3.6
Terms of trade	0.9	-13.4	0.7	7.7	7.5	-3.8	-0.1	-0.8	-0.9	-0.9
REER	107.8	122.5	123.3							
Real effective exchange rate (depreciation -)	2.9	13.6	0.6							
	(Percent of GDP)									
External current account balance	-0.7	-2.2	1.3	-0.4	-0.7	0.4	1.4	1.5	1.5	1.7
Public finances										
Revenue	38.4	33.6	30.3	32.0	36.3	35.2	38.3	35.5	34.8	34.7
Expenditure	43.6	39.7	38.6	36.6	37.2	35.2	34.6	32.6	32.0	31.8
Overall balance (deficit -)	-5.2	-6.1	-8.2	-4.5	-0.9	0.0	3.8	2.9	2.8	2.9
Non-oil primary balance	-7.4	-4.0	-6.7	-4.2	-1.8	-1.5	0.7	1.1	1.1	1.2
Non-oil primary balance (incl. fuel subsidies)			-7.6	-6.2	-5.3	-3.3	-1.3	-0.3	-0.3	-0.4
Public debt 1/	27.1	33.8	43.2	44.6	46.1	49.2	46.8	45.2	40.8	36.6
Domestic	8.4	11.5	15.0	12.6	12.3	12.5	11.9	10.9	10.4	8.8
External	18.7	22.3	28.1	32.0	34.4	37.3	35.4	34.9	30.9	28.3
Saving-investment balance										
Consumption	86.1	87.5	85.0	84.9	88.2	85.0	82.9	82.8	82.6	82.7
Private	58.6	61.2	59.9	59.8	60.5	59.6	57.9	58.9	59.4	59.4
Public	27.5	26.3	25.1	25.1	27.7	25.5	25.0	24.0	23.3	23.4
National saving	27.6	24.6	26.3	25.9	24.7	26.2	28.4	28.0	27.7	27.8
Private	17.8	18.8	22.6	21.1	18.7	19.0	17.9	19.1	18.5	18.7
Public	9.9	5.8	3.7	4.8	6.0	7.2	10.5	8.9	9.2	9.2
Gross investment	28.3	26.9	25.0	26.3	25.4	25.8	27.0	26.5	26.2	26.2
Private 2/	13.6	14.5	12.6	16.3	18.2	18.5	19.8	20.1	19.2	19.4
Public	14.8	12.3	12.4	10.0	7.2	7.3	7.2	6.4	7.0	6.8
Memorandum items:										
Nominal GDP (US$ millions)	101,726	99,290	99,938	104,296	107,511	106,289	107,730	110,571	114,783	118,502
GDP per capita (US$)	6,347	6,099	6,046	6,217	6,316	6,155	6,152	6,227	6,375	6,490
Gross international reserves (US$ millions) 3/	3,762	2,351	4,216	2,006	2,158	4,999	7,761	11,397	11,845	12,944
Gross international reserves (as a percent of ARA metric)	29	18	28	12	12	28	43	63	65	71
Net international reserves (program definition) 4/	1,065	423	-961	-2,271	-1,677	1,419	3,935	7,455	7,596	8,380
Underlying reserves 5/	1,065	423	-961	-2,271	-1,677	17	1,131	3,249	3,391	4,250
Oil price Ecuador mix (US$ per barrel)	84.0	42.1	34.5	45.6	60.4	47.8	48.7	49.4	50.0	50.7
Oil production (millions of barrels)	203.1	198.2	200.7	193.9	188.8	206.2	215.0	201.5	199.1	199.1
Exports of oil (millions of barrels) 6/	157.5	156.9	156.6	150.9	145.1	167.4	171.8	156.2	156.0	156.0

Sources: Ministry of Finance; Central Bank of Ecuador; Haver; World Bank Development Indicators; and Fund staff calculations and estimates.

1/ Gross debt consolidated at the level of the NFPS. Includes the outstanding balance for advance oil sales, treasury certificates, central bank loans, other liabilities and the stock of domestic floating debt. The 40 percent of GDP debt threshold applies to the official debt definition. The public debt estimates are preliminary and subject to revisions in accordance with the IMF's Government Financial Statistics Manual.

2/ Includes inventories

3/ GIR excludes non-liquid and encumbered items included in the authorities' measure of GIR.

4/ Program NIR is equal to gross international reserves less outstanding credit to the IMF (excl. budget support) and deposits of other depository institutions at the central bank.

5/ Underlying reserves refers to program NIR less outstanding obligations of the treasury to the IMF.

6/ Includes both crude and derivatives

Table 2a. Ecuador: Operations of the Nonfinancial Public Sector (Net Accounting)
(Millions of U.S. dollars, unless otherwise indicated)

					Prel.	Est.	Projections				
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	**37,260**	**39,032**	**33,322**	**30,314**	**33,426**	**38,991**	**37,465**	**41,291**	**39,215**	**39,924**	**41,080**
Oil revenue, net 1/	11,433	10,906	6,487	5,402	5,840	8,653	7,649	9,332	7,717	7,722	7,831
Revenue from oil exports	9,153	8,857									
Domestic sales of oil derivatives (CADID)	2,280	2,049									
Nonpetroleum revenue	22,630	23,939	25,758	24,294	25,473	27,702	27,035	28,939	29,228	30,252	31,298
Taxes	13,668	14,460	15,588	14,017	14,078	15,422	14,091	15,741	16,502	16,981	17,601
Social security contributions 2/	4,547	4,718	5,057	4,741	5,414	5,612	5,548	5,623	5,772	5,992	6,186
Other	4,416	4,761	5,113	5,535	5,981	6,668	7,395	7,574	6,954	7,279	7,511
Operating surplus of public enterprises	3,196	4,187	1,076	618	2,113	2,636	2,780	3,020	2,270	1,950	1,950
O/w profits of oil companies withheld for investment	3,041	3,999	833	487	2,077	2,636	2,780	3,020	2,270	1,950	1,950
Expenditure	**41,607**	**44,346**	**39,398**	**38,540**	**38,154**	**40,011**	**37,441**	**37,238**	**36,034**	**36,762**	**37,639**
Primary expenditure	40,637	43,323	37,976	36,980	35,945	37,334	34,638	34,244	33,180	34,060	35,137
Current	26,006	27,968	26,129	25,043	26,198	29,820	27,057	26,962	26,498	26,704	27,685
Wages and salaries	8,896	9,478	9,904	10,014	10,365	10,672	10,019	9,831	9,875	10,251	10,583
Purchases of goods and services	4,435	5,328	5,112	4,684	5,056	5,640	5,001	4,949	4,914	5,101	5,267
Social security benefits 2/	3,410	3,665	4,222	4,655	4,999	5,382	5,372	5,574	5,807	6,074	6,292
Other	9,265	9,497	6,890	5,691	5,777	8,126	6,665	6,609	5,903	5,278	5,543
Cost of imports of oil derivatives	5,511	6,103	3,788	2,332	2,889	4,041	2,993	3,066	2,578	2,681	2,786
Payments to private oil companies (SH) 3/	1,674	1,578	1,439	1,117	1,385	2,016	1,299	1,120	930	739	739
Other	2,080	1,815	1,664	2,242	1,502	2,069	2,373	2,423	2,395	1,857	2,018
Capital	14,631	15,354	11,848	11,937	9,747	7,514	7,581	7,281	6,682	7,356	7,452
Fixed capital spending	14,039	13,980	10,178	10,293	8,648	6,453	6,452	6,415	5,887	6,635	6,708
O/w investment in oil	3,708	4,023	2,804	2,375	1,766	1,669	1,753	1,827	1,713	1,692	1,692
Net-lending	592	1,375	1,669	1,644	1,099	1,061	1,129	866	796	721	745
Primary balance	**-3,377**	**-4,291**	**-4,655**	**-6,666**	**-2,519**	**1,657**	**2,827**	**7,047**	**6,034**	**5,864**	**5,943**
Interest	**971**	**1,024**	**1,421**	**1,561**	**2,209**	**2,677**	**2,803**	**2,994**	**2,854**	**2,702**	**2,502**
O/w external	714	829	1,143	1,335	1,850	2,306	2,409	2,589	2,491	2,384	2,236
Current balance	**10,283**	**10,040**	**5,772**	**3,710**	**5,019**	**6,494**	**7,604**	**11,335**	**9,863**	**10,518**	**10,893**
Overall balance	**-4,348**	**-5,314**	**-6,076**	**-8,226**	**-4,728**	**-1,020**	**24**	**4,053**	**3,181**	**3,162**	**3,441**
Memorandum items:											
Non-oil primary balance 4/	-6,958	-7,491	-3,944	-6,730	-4,395	-1,906	-1,558	709	1,268	1,304	1,378
Non-oil PB (incl. fuel subsidies)				-7,576	-6,469	-5,681	-3,506	-1,350	-317	-385	-425
Cyclically Adjusted Non-oil Primary Balance	-7,335	-8,095	-4,152	-6,354	-4,416	-1,725	-751	2,072	2,839	2,663	2,632
Cyclically Adjusted Non-oil Primary Balance (incl. fuel subsidies)	-14,481	-14,323	-5,859	-7,200	-6,490	-5,499	-2,699	14	1,254	974	829
Structural non-oil primary balance	-7,335	-8,095	-4,016	-5,441	-4,341	-2,180	-1,551	1,272	2,839	2,663	2,632
Structural non-oil primary balance (incl. fuel. subsidies)	-14,481	-14,323	-5,723	-6,287	-6,415	-5,955	-3,499	-786	1,254	974	829
Oil balance 5/	3,582	3,200	-711	64	1,876	3,563	4,385	6,338	4,766	4,560	4,564
Oil balance excluding oil investment	7,290	7,223	2,093	2,440	3,642	5,232	6,138	8,166	6,479	6,252	6,257
Public Debt 6/	19,056	27,543	33,558	43,139	46,533	49,597	52,293	50,393	49,986	46,824	43,383
Change in social spending, program definition							400	400	400		

Sources: Ministry of Finance; Central Bank of Ecuador; and Fund staff calculations and estimates.

1/ Net of operational cost.

2/ From 2011 on, includes additional public pension sytems which previously had not been consolidated into the NFPS accounts.

3/ Reflects service contract payments to private oil companies beginning in 2011.

4/ The primary balance less oil balance.

5/ Oil revenue plus profits of state-owned oil companies, which is retained for investment in the oil sector, less oil-related expenditure (the costs of imports of oil derivatives, service payments to private oil companies, and investment in oil).

6/ Gross debt consolidated at the level of the NFPS. Includes the outstanding balance for advance oil sales, treasury certificates, central bank loans, other liabilities and the stock of domestic floating debt. The 40 percent of GDP debt threshold applies to the official debt definition. The public debt estimates are preliminary and subject to revisions in accordance with the IMF's Government Financial Statistics Manual.

Table 2b. Ecuador: Operations of the Nonfinancial Public Sector (Net Accounting)
(Percent of GDP, unless otherwise indicated)

	2013	2014	2015	2016	Prel. 2017	Est. 2018	Projections 2019	2020	2021	2022	2023
Revenue	**39.2**	**38.4**	**33.6**	**30.3**	**32.0**	**36.3**	**35.2**	**38.3**	**35.5**	**34.8**	**34.7**
Oil revenue, net 1/	12.0	10.7	6.5	5.4	5.6	8.0	7.2	8.7	7.0	6.7	6.6
Revenue from oil exports	9.6	8.7									
Domestic sales of oil derivatives (CADID)	2.4	2.0									
Nonpetroleum revenue	23.8	23.5	25.9	24.3	24.4	25.8	25.4	26.9	26.4	26.4	26.4
Taxes	14.4	14.2	15.7	14.0	13.5	14.3	13.3	14.6	14.9	14.8	14.9
Social security contributions 2/	4.8	4.6	5.1	4.7	5.2	5.2	5.2	5.2	5.2	5.2	5.2
Other	4.6	4.7	5.1	5.5	5.7	6.2	7.0	7.0	6.3	6.3	6.3
Operating surplus of public enterprises	3.4	4.1	1.1	0.6	2.0	2.5	2.6	2.8	2.1	1.7	1.6
O/w profits of oil companies withheld for investment	3.2	3.9	0.8	0.5	2.0	2.5	2.6	2.8	2.1	1.7	1.6
Expenditure	**43.7**	**43.6**	**39.7**	**38.6**	**36.6**	**37.2**	**35.2**	**34.6**	**32.6**	**32.0**	**31.8**
Primary expenditure	42.7	42.6	38.2	37.0	34.5	34.7	32.6	31.8	30.0	29.7	29.7
Current	27.3	27.5	26.3	25.1	25.1	27.7	25.5	25.0	24.0	23.3	23.4
Wages and salaries	9.4	9.3	10.0	10.0	9.9	9.9	9.4	9.1	8.9	8.9	8.9
Purchases of goods and services	4.7	5.2	5.1	4.7	4.8	5.2	4.7	4.6	4.4	4.4	4.4
Social security benefits 2/	3.6	3.6	4.3	4.7	4.8	5.0	5.1	5.2	5.3	5.3	5.3
Other	9.7	9.3	6.9	5.7	5.5	7.6	6.3	6.1	5.3	4.6	4.7
Cost of imports of oil derivatives	5.8	6.0	3.8	2.3	2.8	3.8	2.8	2.8	2.3	2.3	2.4
Payments to private oil companies (SH) 3/	1.8	1.6	1.4	1.1	1.3	1.9	1.2	1.0	0.8	0.6	0.6
Other	2.2	1.8	1.7	2.2	1.4	1.9	2.2	2.2	2.2	1.6	1.7
Capital	15.4	15.1	11.9	11.9	9.3	7.0	7.1	6.8	6.0	6.4	6.3
Fixed capital spending	14.8	13.7	10.3	10.3	8.3	6.0	6.1	6.0	5.3	5.8	5.7
O/w investment in oil	3.9	4.0	2.8	2.4	1.7	1.6	1.6	1.7	1.5	1.5	1.4
Net-lending	0.6	1.4	1.7	1.6	1.1	1.0	1.1	0.8	0.7	0.6	0.6
Primary balance	**-3.5**	**-4.2**	**-4.7**	**-6.7**	**-2.4**	**1.5**	**2.7**	**6.5**	**5.5**	**5.1**	**5.0**
Interest	**1.0**	**1.0**	**1.4**	**1.6**	**2.1**	**2.5**	**2.6**	**2.8**	**2.6**	**2.4**	**2.1**
O/w external	0.8	0.8	1.2	1.3	1.8	2.1	2.3	2.4	2.3	2.1	1.9
Current balance	**10.8**	**9.9**	**5.8**	**3.7**	**4.8**	**6.0**	**7.2**	**10.5**	**8.9**	**9.2**	**9.2**
Overall balance	**-4.6**	**-5.2**	**-6.1**	**-8.2**	**-4.5**	**-0.9**	**0.0**	**3.8**	**2.9**	**2.8**	**2.9**
Memorandum items:											
Non-oil primary balance 4/	-7.3	-7.4	-4.0	-6.7	-4.2	-1.8	-1.5	0.7	1.1	1.1	1.2
Non-oil primary balance (percent of non-oil GDP)	-8.4	-8.3	-4.2	-7.0	-4.4	-1.9	-1.5	0.7	1.2	1.2	1.2
Non-oil PB (incl. fuel subsidies)				-7.6	-6.2	-5.3	-3.3	-1.3	-0.3	-0.3	-0.4
Cyclically Adjusted Non-oil Primary Balance	-7.7	-8.0	-4.2	-6.4	-4.2	-1.6	-0.7	1.9	2.6	2.3	2.2
Cyclically Adjusted Non-oil Primary Balance (incl. fuel subsidies)	-15.2	-14.1	-5.9	-7.2	-6.2	-5.1	-2.5	0.0	1.1	0.8	0.7
Structural non-oil primary balance	-7.7	-8.0	-4.0	-5.4	-4.2	-2.0	-1.5	1.2	2.6	2.3	2.2
Structural non-oil primary balance (including fuel. subsidies)	-15.2	-14.1	-5.8	-6.3	-6.2	-5.5	-3.3	-0.7	1.1	0.8	0.7
Oil balance 5/	3.8	3.1	-0.7	0.1	1.8	3.3	4.1	5.9	4.3	4.0	3.9
Oil balance excluding oil investment	7.7	7.1	2.1	2.4	3.5	4.9	5.8	7.6	5.9	5.4	5.3
Public Debt 6/	20.0	27.1	33.8	43.2	44.6	46.1	49.2	46.8	45.2	40.8	36.6
Change in social spending, program definition							0.4	0.4	0.4		

Sources: Ministry of Finance; Central Bank of Ecuador; and Fund staff calculations and estimates.

1/ Net of operational cost.

2/ From 2011 on, includes additional public pension sytems which previously had not been consolidated into the NFPS accounts.

3/ Reflects service contract payments to private oil companies beginning in 2011.

4/ The primary balance less oil balance.

5/ Oil revenue plus profits of state-owned oil companies, which is retained for investment in the oil sector, less oil-related expenditure (the costs of imports of oil derivatives, service payments to private oil companies, and investment in oil).

6/ Gross debt consolidated at the level of the NFPS. Includes the outstanding balance for advance oil sales, treasury certificates, central bank loans, other liabilities and the stock of domestic floating debt. The 40 percent of GDP debt threshold applies to the official debt definition. The public debt estimates are preliminary and subject to revisions in accordance with the IMF's Government Financial Statistics Manual.

Table 3. Ecuador: Nonfinancial Public Sector Financing

(Millions of U.S. dollars, unless otherwise indicated)

					Prel.	Est.	Projections				
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Gross financing needs	**6,741**	**11,035**	**14,181**	**19,086**	**17,475**	**8,889**	**5,903**	**2,523**	**1,442**	**3,149**	**2,933**
Nonfinancial public sector deficit	4,348	5,314	6,076	8,226	4,728	1,020	-24	-4,053	-3,181	-3,162	-3,441
Amortization	2,393	5,721	8,105	10,859	12,747	7,868	5,926	6,577	4,623	6,311	6,373
External	1,706	3,549	3,985	3,336	4,012	4,871	3,715	4,880	2,547	4,979	4,262
Multilateral	582	942	560	771	709	685	812	667	854	1,361	1,685
Bilateral	620	737	636	659	1,322	1,614	1,088	1,124	918	996	972
Private sector and other	33	35	898	399	845	879	989	2,709	247	2,177	1,160
Oil related financing	537	1,848	1,901	1,510	1,136	1,692	826	380	528	445	445
Domestic	687	2,172	4,120	7,523	8,735	2,998	2,211	1,697	2,076	1,332	2,112
Bonds	401	1,420	3,168	5,866	3,912	885	551	37	814	71	850
Treasury certificates	286	752	953	1,657	4,822	2,113	1,660	1,660	1,262	1,262	1,262
Gross financing sources	**6,741**	**11,035**	**14,181**	**19,086**	**17,475**	**8,889**	**5,903**	**2,523**	**1,442**	**3,149**	**2,933**
External	5,172	8,013	7,105	9,430	9,252	7,819	6,409	3,416	2,954	1,887	2,302
Multilateral	732	1,497	1,933	1,092	943	1,642	4,268	2,971	2,509	800	800
World Bank	2	7	115	18	175	236	978	644	122	100	100
Inter-American Development Bank	372	508	1,321	604	349	487	1,009	324	384	400	400
CAF	350	355	485	465	415	549	600	600	600	300	300
Other	8	627	13	5	4	370	278	0	0	0	0
IMF	0	0	0	0	0	0	1,403	1,403	1,403	0	0
Bilateral	2,491	1,180	957	2,267	658	978	559	0	0	0	0
Private sector and other	49	3,735	1,880	3,946	7,251	4,504	1,137	0	0	642	1,057
Oil related financing	1,900	1,600	2,335	2,125	400	695	445	445	445	445	445
Domestic	2,035	2,143	5,540	9,233	9,947	2,083	-507	-892	-1,512	1,262	631
Bonds	1,043	1,310	2,844	5,853	6,258	403	552	0	0	0	0
Treasury certificates	752	953	1,657	4,822	2,113	1,660	1,660	1,262	1,262	1,262	631
Change in deposits (+= drawdown)	240	-120	1,040	-1,443	-562	-1,043	-2,719	-2,154	-2,774	0	0
Privatization and BCE transfers	0	0	0	0	2,137	0	0	0	0	0	0
Other	0	0	0	0	0	1,062	0	0	0	0	0
Net Arrears acumulation and other financing 1/	-389	998	1,503	499	-1,643	-1,013	0	0	0	0	0
Discrepancy	-77	-118	32	-76	-81						
NFPS deposits 2/	**4,171**	**4,291**	**3,251**	**4,694**	**5,255**	**6,298**	**9,017**	**11,171**	**13,945**	**13,945**	**13,945**
Net financing	**4,348**	**5,314**	**6,076**	**8,226**	**4,728**	**1,020**	**-24**	**-4,053**	**-3,181**	**-3,162**	**-3,441**
External	3,465	4,464	3,120	6,093	5,240	2,949	2,694	-1,464	407	-3,091	-1,960
Domestic	1,348	-29	1,420	1,710	1,212	-915	-2,718	-2,590	-3,588	-71	-1,481
Net Arrears acumulation and other financing 1/	-389	998	1,503	499	-1,643	-1,013	0	0	0	0	0
Discrepancy	-77	-118	32	-76	-81	0	0	0	0	0	0
Public Sector Debt 3/	**19,056**	**27,543**	**33,558**	**43,139**	**46,533**	**49,597**	**52,293**	**50,393**	**49,986**	**46,824**	**43,383**
External	12,611	19,046	22,123	28,122	33,376	36,958	39,653	38,189	38,596	35,505	33,545
o.w. oil related financing	1,712	1,464	1,898	2,442	1,626	1,263	882	947	863	863	863
Domestic	6,445	8,497	11,435	15,018	13,157	13,273	13,274	12,838	12,024	11,953	10,472
Bonds	2,461	3,810	3,437	3,461	5,866	5,384	5,385	5,348	4,534	4,463	3,613
Treasury certificates	752	953	1,657	4,822	2,113	1,660	1,660	1,262	1,262	1,262	631
Other liabilities	3,232	3,735	6,341	6,735	5,178	6,228	6,228	6,228	6,228	6,228	6,228
					(In percent of GDP)						
Gross financing needs	**7.1**	**10.8**	**14.3**	**19.1**	**16.8**	**8.3**	**5.6**	**2.3**	**1.3**	**2.7**	**2.5**
Nonfinancial public sector deficit	4.6	5.2	6.1	8.2	4.5	0.9	0.0	-3.8	-2.9	-2.8	-2.9
Amortization	2.5	5.6	8.2	10.9	12.2	7.3	5.6	6.1	4.2	5.5	5.4
Gross financing sources	**7.1**	**10.8**	**14.3**	**19.1**	**16.8**	**8.3**	**5.6**	**2.3**	**1.3**	**2.7**	**2.5**
External	5.4	7.9	7.2	9.4	8.9	7.3	6.0	3.2	2.7	1.6	1.9
Domestic	2.1	2.1	5.6	9.2	9.5	1.9	-0.5	-0.8	-1.4	1.1	0.5
Arrears acumulation and other financing 1/	-0.4	1.0	1.5	0.5	-1.6	-0.9	0.0	0.0	0.0	0.0	0.0
NFPS deposits 2/	**4.4**	**4.2**	**3.3**	**4.7**	**5.0**	**5.9**	**8.5**	**10.4**	**12.6**	**12.1**	**11.8**
Public sector debt 3/	**20.0**	**27.1**	**33.8**	**43.2**	**44.6**	**46.1**	**49.2**	**46.8**	**45.2**	**40.8**	**36.6**
External	13.3	18.7	22.3	28.1	32.0	34.4	37.3	35.4	34.9	30.9	28.3
Domestic	6.8	8.4	11.5	15.0	12.6	12.3	12.5	11.9	10.9	10.4	8.8

Sources: Ministry of Finance; Central Bank of Ecuador; and Fund staff calculations and estimates.

1/ Includes domestic floating debt and statistical discrepancy.

2/ Includes deposits of pension funds, which are reported as nonfinancial public sector.

3/ Gross debt consolidated at the level of the NFPS. Includes the outstanding balance for advance oil sales, treasury certificates, central bank loans, other liabilities and the stock of domestic floating debt. The 40 percent of GDP debt threshold applies to the official debt definition. The public debt estimates are preliminary and subject to revisions in accordance with the IMF's Government Financial Statistics Manual.

Table 4. Ecuador: Balance of Payments

(Millions of U.S. dollars, unless otherwise indicated)

					Prel.	Est.	Projections				
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Current account	**-944**	**-678**	**-2,223**	**1,324**	**-373**	**-766**	**427**	**1,557**	**1,706**	**1,730**	**1,966**
Trade balance	-529	-63	-1,650	1,567	311	-174	1,341	2,248	2,091	1,950	1,966
Exports, f.o.b.	25,587	26,596	19,049	17,425	19,618	22,141	22,122	23,121	23,396	24,098	24,928
Oil	14,107	13,275	6,660	5,459	6,914	8,802	8,038	8,410	7,745	7,834	7,945
Non-oil	11,480	13,321	12,388	11,966	12,705	13,339	14,085	14,711	15,650	16,263	16,983
Imports, f.o.b.	26,115	26,660	20,699	15,858	19,307	22,315	20,781	20,873	21,304	22,147	22,962
Oil	5,927	6,417	3,950	2,490	3,182	4,341	3,419	3,492	3,579	3,721	3,860
Non-oil	20,188	20,243	16,748	13,368	16,125	17,975	17,362	17,380	17,725	18,426	19,102
Services	-1,420	-1,171	-805	-1,054	-994	-773	-599	-510	-482	-490	-484
Credits	2,041	2,346	2,391	2,140	2,300	2,579	2,629	2,749	2,855	2,976	3,101
Debits	3,461	3,517	3,197	3,194	3,294	3,352	3,228	3,259	3,337	3,466	3,585
Primary income	-1,372	-1,552	-1,731	-1,843	-2,355	-2,604	-3,206	-3,168	-2,991	-2,921	-2,810
Credits	113	121	140	164	187	280	383	530	543	590	604
Debits	1,485	1,673	1,871	2,007	2,542	2,884	3,589	3,698	3,535	3,511	3,414
Secondary income	2,376	2,108	1,963	2,654	2,665	2,786	2,890	2,987	3,088	3,191	3,293
Of which: workers' remittances, net	2,292	2,277	2,100	2,314	2,483	2,599	2,705	2,800	2,896	2,991	3,087
Capital account	**66**	**67**	**-69**	**-814**	**69**	**72**	**74**	**73**	**74**	**76**	**79**
Financial account	**-2,869**	**-411**	**-769**	**-798**	**1,542**	**-920**	**-1,007**	**468**	**-588**	**1,358**	**945**
Direct investment	-727	-772	-1,322	-767	-618	-945	-1,219	-1,235	-1,545	-1,604	-1,656
Other public sector flows	-3,465	-4,464	-3,120	-6,093	-5,240	-2,949	-1,291	2,867	996	3,091	1,960
Disbursements	-5,172	-8,013	-7,105	-9,430	-9,252	-7,819	-5,006	-2,013	-1,551	-1,887	-2,302
Amortizations	1,706	3,549	3,985	3,336	4,012	4,871	3,715	4,880	2,547	4,979	4,262
Other private sector flows	1,323	4,825	3,674	6,063	7,400	2,974	1,503	-1,163	-39	-129	641
Portfolio investment	958	2,235	407	1,745	761	1,419	523	-1,392	-762	-193	451
Other investment	364	2,590	3,267	4,318	6,640	1,555	979	228	722	64	190
Errors and omissions	**-145**	**-225**	**35**	**-101**	**-13**	**0**	**0**	**0**	**0**	**0**	**0**
Overall balance	**1,846**	**-424**	**-1,488**	**1,207**	**-1,859**	**225**	**1,508**	**1,162**	**2,369**	**448**	**1,100**
Financing	**-1,846**	**424**	**1,488**	**-1,207**	**1,859**	**-225**	**-1,508**	**-1,162**	**-2,369**	**-448**	**-1,100**
Change in GIR (increase, -)	-1,878	411	1,453	-1,763	1,808	-225	-2,865	-2,385	-3,635	-448	-1,100
IMF net credit and loans	0	0	0	365	0	0	1,357	1,222	1,267	0	0
Net EFF lending to BCE	0	0	0	0	0	0	0	0	0	0	0
Net lending RFI	0	0	0	0	0	0	-46	-181	-136	0	0
Net lending to Treasury	0	0	0	0	0	0	1,403	1,403	1,403	0	0
Exceptional financing 1/	32	13	35	191	51	0	0	0	0	0	0
Memorandum items:											
Current account balance (percent of GDP)	-1.0	-0.7	-2.2	1.3	-0.4	-0.7	0.4	1.4	1.5	1.5	1.7
Oil balance (percent of GDP)	8.6	6.7	2.7	3.0	3.6	4.1	4.3	4.6	3.8	3.6	3.4
Exports	14.8	13.1	6.7	5.5	6.6	8.2	7.6	7.8	7.0	6.8	6.7
Imports	6.2	6.3	4.0	2.5	3.1	4.0	3.2	3.2	3.2	3.2	3.3
Non-oil balance (percent of GDP)	-9.6	-7.4	-5.0	-1.6	-3.9	-4.9	-3.9	-3.1	-2.2	-2.1	-1.8
Goods export volume growth rate (percent)	4.1	5.8	-0.3	4.3	-0.3	-1.8	8.8	3.6	0.5	2.4	2.8
Goods import volume growth rate (percent)	7.7	4.9	-7.5	-10.5	16.0	8.4	-2.5	-0.5	0.5	2.3	2.1
Goods terms of trade growth rate (percent)	1.0	0.9	-13.4	0.7	7.7	7.5	-3.8	-0.1	-0.8	-0.9	-0.9
Oil price Ecuador mix (U.S.$ per barrel)	96	84	42	35	46	60	48	49	49	50	51
External debt (percent of GDP)	19.4	25.2	29.4	36.6	39.5	40.5	42.8	42.9	42.9	39.4	36.5

Sources: Central Bank of Ecuador; and Fund staff calculations and estimates.
1/ Includes foreign arrears and net flows from oil funds held abroad and flows associated with debt default and restructuring.

Table 5. Ecuador: External Financing

(Millions of U.S. dollars, unless otherwise indicated)

					Prel.	Est.	Projections				
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Gross external financing requirements	**4,328**	**6,844**	**8,802**	**5,092**	**8,075**	**9,481**	**7,263**	**7,344**	**4,942**	**7,203**	**6,121**
Current account financing need	944	678	2,223	-1,324	373	766	-427	-1,557	-1,706	-1,730	-1,966
Public sector amortizations	1,706	3,549	3,985	3,336	4,012	4,871	3,715	4,880	2,547	4,979	4,262
Private sector amortizations	1,677	2,617	2,593	3,079	3,690	3,844	3,974	4,022	4,101	3,954	3,825
Identified External Financing	**6,174**	**6,419**	**7,313**	**6,299**	**6,217**	**9,706**	**8,771**	**8,506**	**7,311**	**7,651**	**7,221**
Public Sector	5,172	8,013	7,105	9,430	9,252	7,819	5,006	2,013	1,551	1,887	2,302
Multilateral	732	1,497	1,933	1,092	943	1,642	2,865	1,568	1,106	800	800
Bilateral	2,491	1,180	957	2,267	658	978	559	0	0	0	0
Oil related financing	1,900	1,600	2,335	2,125	400	695	445	445	445	445	445
Private sector	49	3,735	1,880	3,946	7,251	4,504	1,137	0	0	642	1,057
Private sector	1,082	-1,436	242	-2,216	-3,092	1,815	3,690	6,420	5,686	5,688	4,840
Direct investment	727	772	1,322	767	618	945	1,219	1,235	1,545	1,604	1,656
Portfolio investment Financing	71	-442	-216	-597	-742	174	494	1,037	828	817	637
Other investment Financing	284	-1,766	-864	-2,387	-2,968	696	1,977	4,148	3,312	3,267	2,547
Net Transfers 1/	-79	-158	-34	-915	56	72	74	73	74	76	79
Gross external financing sources	**6,206**	**6,432**	**7,349**	**6,855**	**6,267**	**9,706**	**10,128**	**9,728**	**8,577**	**7,651**	**7,221**
Identified External Financing	6,174	6,419	7,313	6,299	6,217	9,706	8,771	8,506	7,311	7,651	7,221
Exceptional financing	32	13	35	191	51	0	0	0	0	0	0
IMF Net Financing	0	0	0	365	0	0	1,357	1,222	1,267	0	0
IMF Net EFF Financing	0	0	0	0	0	0	1,403	1,403	1,403	0	0
IMF Net RFI Financing				365			-46	-181	-136	0	0
Increase in NIR 2/	**-1,878**	**411**	**1,453**	**-1,398**	**1,808**	**-225**	**-2,911**	**-2,565**	**-3,772**	**-448**	**-1,100**
Increase in GIR	**-1,878**	**411**	**1,453**	**-1,763**	**1,808**	**-225**	**-2,865**	**-2,385**	**-3,635**	**-448**	**-1,100**
Financing Gap 3/	**32**	**13**	**35**	**556**	**51**	**0**	**1,357**	**1,222**	**1,267**	**0**	**0**
o/w closed by IMF Net Lending	0	0	0	365	0	0	1,357	1,222	1,267	0	0

Sources: Central Bank of Ecuador; and Fund staff calculations and estimates.

1/ Net transfers is defined as capital account flows plus unidentified flows (errors and omissions)

2/ Changes in NIR are defined as changes in GIR minus IMF net lending excluding direct budget support

3/ Financing gap is the difference between total external financing sources and identified external financing

Table 6. Ecuador: Monetary Survey
(Millions of U.S. dollars, unless otherwise indicated)

	2013	2014	2015	2016	2017	Est. 2018	Projections 2019	2020	2021	2022	2023
I. Central Bank											
Net foreign assets	**5,216**	**4,536**	**2,964**	**4,435**	**3,584**	**3,902**	**6,762**	**8,706**	**12,506**	**12,996**	**14,133**
O/w: gross international reserves 1/	4,178	3,762	2,351	4,216	2,006	2,158	4,999	7,761	11,397	11,845	12,944
Net domestic assets	**-1,173**	**-865**	**306**	**1,806**	**1,964**	**1,108**	**-1,602**	**-3,094**	**-6,593**	**-6,704**	**-7,462**
Credit to the nonfinancial public sector, net	-3,161	-2,738	-1,369	323	-1,230	-2,073	-4,775	-6,273	-9,410	-9,391	-10,153
O/w: central government, net	-981	92	614	2,840	1,556	1,169	-1,570	-3,024	-6,076	-5,930	-6,580
credits	71	903	1,314	4,311	3,044	3,048	3,048	3,698	3,321	3,321	2,542
debits	1,052	811	700	1,472	1,488	1,879	4,618	6,722	9,397	9,251	9,122
Credit to financial institutions	2,736	2,530	2,167	2,187	4,431	4,517	4,499	4,499	4,133	3,997	3,997
Other depository institutions	641	530	431	454	930	1,005	1,052	1,052	821	821	821
Other financial institutions	2,094	2,001	1,736	1,733	3,501	3,512	3,447	3,447	3,312	3,176	3,176
Credit to the private sector	27	26	27	24	20	17	17	17	18	18	19
Other, net	-775	-684	-520	-728	-1,258	-1,353	-1,343	-1,337	-1,333	-1,329	-1,324
Liabilities	**4,043**	**3,671**	**3,270**	**6,241**	**5,548**	**5,011**	**5,160**	**5,612**	**5,913**	**6,292**	**6,672**
Currency and electronic money	87	87	87	92	94	84	83	84	86	89	92
Banks' reserves	3,898	3,506	3,053	6,044	5,244	4,859	5,010	5,462	5,760	6,136	6,513
Other depository institutions 2/	3,302	2,697	1,927	4,825	3,904	3,172	3,262	3,690	3,942	4,249	4,564
Other financial institutions 3/	597	809	1,126	1,219	1,340	1,688	1,748	1,772	1,818	1,888	1,949
Other 4/	57	78	130	105	209	68	67	67	67	67	67
II. Other Depository Institutions (ODI) and Other Financial Institutions (OFI) 2/ 3/											
Net foreign assets	**5,534**	**5,891**	**5,391**	**5,826**	**5,633**	**4,972**	**4,032**	**3,442**	**2,761**	**2,868**	**2,963**
Net domestic assets	**22,117**	**24,580**	**22,392**	**26,968**	**30,166**	**32,653**	**34,666**	**37,338**	**40,801**	**44,083**	**47,474**
Assets held at the BCE, net	1,543	913	450	3,346	2,400	1,751	1,885	2,313	2,796	3,103	3,418
Credit to the nonfinancial public sector, net	931	1,612	1,379	1,972	1,959	1,108	1,108	1,108	741	742	742
O/w: central government, net	1,208	1,830	1,448	2,053	2,073	1,284	1,284	1,284	918	918	918
Credit to the private sector	26,785	29,131	28,141	29,886	34,785	39,976	41,739	44,120	47,736	51,110	54,538
Other items, net	-7,141	-7,075	-7,579	-8,236	-8,977	-10,182	-10,067	-10,203	-10,472	-10,871	-11,223
Liabilities	**27,651**	**30,471**	**27,782**	**32,794**	**35,799**	**37,626**	**38,698**	**40,780**	**43,561**	**46,951**	**50,438**
O/w: Private sector deposits	27,544	30,415	27,782	32,794	35,799	37,626	38,698	40,780	43,561	46,951	50,438
III. Consolidated Banking System											
Net foreign assets	**10,750**	**10,426**	**8,355**	**10,261**	**9,218**	**8,875**	**10,794**	**12,148**	**15,267**	**15,865**	**17,097**
Net domestic assets	**15,400**	**18,593**	**18,854**	**22,730**	**26,885**	**28,902**	**28,053**	**28,782**	**28,448**	**31,242**	**33,500**
Credit to the nonfinancial public sector, net	-2,230	-1,126	10	2,295	728	-965	-3,667	-5,165	-8,669	-8,649	-9,411
Credit to the private sector	26,812	29,157	28,169	29,910	34,805	39,994	41,756	44,137	47,753	51,128	54,557
Other items, net	-9,183	-9,437	-9,324	-9,475	-8,648	-10,126	-10,036	-10,190	-10,637	-11,236	-11,645
Liabilities	**26,149**	**29,019**	**27,209**	**32,991**	**36,103**	**37,777**	**38,847**	**40,930**	**43,714**	**47,107**	**50,597**
Memorandum items:											
Credit to the private sector (percent change, yoy) 5/	10.5	8.7	-3.4	6.2	16.4	14.9	4.4	5.7	8.2	7.1	6.7
Deposits of the private sector (percent change, yoy) 5/	12.9	10.4	-8.6	18.0	9.3	5.0	2.8	5.4	6.8	7.8	7.4
Credit to the nonfinancial public sector (percent change, yoy) 5/	38.1	64.5	-1.6	109.8	-17.0	-10.6	0.0	12.6	-12.8	0.0	-15.3
Deposits of the nonfinancial public sector (percent change, yoy) 5/	-5.8	5.1	-26.4	41.1	8.2	21.3	43.5	24.4	25.2	-0.1	-0.1
Broad money velocity	2.7	2.5	2.5	2.1	2.0	1.9	1.8	1.7	1.7	1.5	1.5
ODI and OFI's reserves at the central bank as a share of liabilities (percent) 2	14.1	11.5	11.0	18.4	14.6	12.9	12.9	13.4	13.2	13.1	12.9
Credit to the private sector (percent of GDP)	28.2	28.7	28.4	29.9	33.4	37.2	39.3	41.0	43.2	44.5	46.0
Liabilities (percent of GDP)	27.5	28.5	27.4	33.0	34.6	35.1	36.5	38.0	39.5	41.0	42.7

Sources: Central Bank of Ecuador; and Fund staff calculations and estimates.
1/ Excludes non-liquid and encumbered reserves included in the authorities' definition of GIR
2/ ODI include private banks, *Banecuador* (formerly *Banco Nacional de Fomento)*, *Banco del Pacifico*, private financial companies, mutualists, cooperatives, and credit card companies.
3/ OFI include *Corporación Financiera Nacional* and *Banco Ecuatoriano de la Vivienda*.
4/ Includes monetary deposits, *Titulos del Banco Central de Ecuador*, stabilization bonds, and accounts payable.
5/ Consolidated banking system.

Table 7. Ecuador: Financial Soundness Indicators 1/

	2010	2011	2012	2013	2014	2015	2016	2017	Q1	Q2	Q3	Q4
									2018			
	(In percent, unless otherwise indicated; end-of-period values)											
Capital Adequacy												
Regulatory capital to risk-weighted assets (CAR)	12.4	13.0	12.8	11.9	12.7	14.4	13.9	13.7	13.2	12.7	12.9	13.4
Asset Quality and Distribution												
Nonperforming loans to gross loans	2.2	2.2	2.8	2.6	2.9	3.7	3.5	3.0	3.2	3.0	3.1	2.6
Provisions to nonperforming loans	252.1	263.9	235.7	242.0	221.7	187.1	189.5	234.4	220.5	226.7	221.3	247.7
Gross loans to assets	87.6	89.3	86.0	84.2	86.2	86.2	80.0	84.4	84.8	86.7	86.9	86.0
Earnings and Profitability												
Return on average assets (ROA)	1.3	1.7	1.1	0.9	1.0	0.9	0.6	1.0	1.2	1.3	1.4	1.4
Return on average equity (ROE)	14.3	18.9	12.8	10.1	12.0	9.0	6.7	10.4	10.8	12.3	13.3	13.6
Interest margin to assets	1.2	1.4	0.9	0.8	1.0	0.8	0.4	0.9	1.1	1.4	1.5	1.6
Noninterest expenses to spread	82.1	79.7	86.3	86.8	84.3	87.4	92.6	85.0	81.8	78.2	77.2	76.9
Liquidity												
Liquid assets to short-term liabilities	32.4	28.7	30.5	30.7	26.0	29.6	33.9	29.4	29.0	23.9	23.6	27.9
Deposit to loan ratio	142.4	136.1	138.4	140.6	136.5	126.1	137.0	121.9	120.6	112.9	110.5	111.8

Source: Superintendency of Banks.

1/ Values refer to private banks and *Banco del Pacifico* .

Table 8. Ecuador: Indicators of Fund Credit 2019–28

(Units as indicated)

				Projections						
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
Existing and prospective Fund arrangements					(millions of SDRs)					
Disbursements 1/	1,011	1,011	1,011	0	0	0	0	0	0	0
Stock of existing and prospective Fund credit	1,241	2,121	3,035	3,035	2,981	2,770	2,391	1,885	1,379	873
Obligations	53	173	175	101	157	315	482	587	561	538
Principal	33	131	98	0	54	211	379	506	506	506
Charges/interest	20	42	77	101	103	104	102	81	55	32
Obligations, relative to key variables					(percent)					
Quota	7.5	24.8	25.1	14.5	22.5	45.1	69.0	84.1	80.4	77.1
Gross domestic product	0.1	0.2	0.2	0.1	0.2	0.4	0.5	0.6	0.6	0.5
Gross international reserves 2/	1.5	3.1	2.1	1.2	1.7	3.3	3.7	3.8	3.5	3.1
Unencumbered gross international reserves (baseline) 3/	1.5	3.4	2.2	1.3	1.7	3.3	3.7	3.8	3.5	3.1
Unencumbered gross international reserves (alternative) 3/ 4/	1.5	3.4	2.2	1.3	1.8	3.5	3.8	4.0	3.6	3.2
Exports of goods and services	0.3	0.9	0.9	0.5	0.8	1.5	2.2	2.7	2.5	2.3
Unencumbered exports of goods and services (baseline) 3/	0.3	1.0	0.9	0.5	0.8	1.5	2.2	2.7	2.5	2.3
Unencumbered exports of goods and services (alternative) 3/ 4/	0.3	1.0	0.9	0.5	0.8	1.5	2.3	2.7	2.5	2.4
Revenues of the NFPS	0.2	0.6	0.6	0.4	0.5	1.0	1.5	1.8	1.7	1.5
Unencumbered revenues of the NFPS (baseline) 3/	0.2	0.6	0.6	0.4	0.5	1.0	1.5	1.8	1.7	1.5
Unencumbered revenues of the NFPS (alternative) 3/ 4/	0.2	0.6	0.6	0.4	0.5	1.0	1.5	1.8	1.7	1.6
External debt service	0.5	1.6	1.8	0.9	1.6	3.0	4.7	5.9	5.8	5.7
Unencumbered external debt service (baseline) 3/	0.5	1.6	1.9	1.0	1.6	3.0	4.7	5.9	5.8	5.7
Unencumbered external debt service (alternative) 3/ 4/	0.5	1.6	1.9	1.0	1.6	3.1	4.9	6.2	6.0	5.9
Fund credit outstanding, relative to key variables					(percent)					
Quota	177.8	304.1	435.0	435.0	427.2	397.0	342.7	270.1	197.6	125.1
Gross domestic product	1.6	2.7	3.8	3.7	3.5	3.1	2.6	2.0	1.4	0.9
Gross international reserves	34.4	37.9	36.9	35.5	31.9	29.0	18.4	12.3	8.6	5.0
Unencumbered gross international reserves (baseline) 3/	35.7	41.4	37.8	37.7	31.9	29.0	18.4	12.3	8.6	5.0
Unencumbered gross international reserves (alternative) 3/ 4/	35.7	41.4	37.8	37.7	33.6	30.5	19.0	12.7	8.8	5.1
External debt	3.8	6.4	8.9	9.3	9.6	9.5	8.1	6.5	5.1	3.4
External debt excl. collateralized (baseline) 5/	3.9	6.5	9.0	9.3	9.6	9.5	8.1	6.5	5.1	3.4
External debt excl. collateralized (alternative) 5/ 6/	3.9	6.6	9.2	9.6	9.9	9.8	8.3	6.7	5.3	3.5
Memorandum items:										
Exports of goods and services (US$m)	24,751	25,870	26,251	27,073	28,029	28,945	29,731	30,537	31,365	32,216
External debt service (US$m)	14,024	15,491	13,269	15,210	14,008	14,553	14,183	13,823	13,472	13,130
o/w repos/collateralized borrowing (baseline)	179	651	262	686	0	0	0	0	0	0
o/w repos/collateralized borrowing (alternative)	179	651	262	686	632	657	640	624	608	592
External debt (US$m)	45,512	46,219	47,411	45,210	43,269	40,479	41,047	40,262	37,474	35,463
o/w repos/collateralized borrowing (baseline)	1,414	861	650	0	0	0	0	0	0	0
o/w repos/collateralized borrowing (alternative)	1,414	1,436	1,473	1,404	1,344	1,257	1,275	1,251	1,164	1,102
Quota (SDRm)	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7
NIR, program definition (US$m)	1,419	3,935	7,455	7,596	8,380	8,385	12,883	15,652	16,353	17,904
Gross international reserves (US$m)	4,999	7,761	11,397	11,845	12,944	13,260	18,060	21,177	22,263	24,227
Gross international reserves (% ARA metric)	28	43	63	65	71	73	98	114	119	128
Underlying reserves (US$m)	21	1,136	3,255	3,396	4,255	8,382	12,881	15,650	16,351	17,903
Nominal GDP (US$m)	106,289	107,730	110,571	114,783	118,502	122,025	126,326	130,778	135,387	140,159
SDRs per U.S. dollar	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7

Sources: Central Bank of Ecuador and Fund staff estimates and projections.

1/ An RFI of 37.5% of quota disbursed in 2016; assumes an EFF of $4.2 billion disburses beginning in 2019.

2/ GIR excludes non-liquid and encumbered items included in the authorities' measure of GIR.

3/ Subtracting debt service on repos (collateralized debt).

4/ The alternative scenario is a sensitivity test which assumes the share of debt service on collateralized debt, relative to total debt service, remains at 2022 levels.

5/ Subtracting repos (collateralized debt).

6/ The alternative scenario assumes that the share of collateralized debt in total debt remains at 2019 levels.

Table 9. Ecuador: Proposed Access and Phasing Under the Extended Fund Arrangement

Review	Availability Date	Action	SDR million	US$ million	Percent of quota 1/ Disbursement	Cumulative
	March 11, 2019	Board approval of EFF	469.70	651.47	67.32	67.32
First Review	June 15, 2019	Observance of continuous and end-March 2019 performance criteria, completion of first review	180.65	250.57	25.89	93.21
Second Review	September 15, 2019	Observance of continuous and end-June 2019 performance criteria, completion of second review	180.65	250.57	25.89	119.11
Third Review	December 15, 2019	Observance of continuous and end-September 2019 performance criteria, completion of third review	180.65	250.57	25.89	145.00
Fourth Review	March 15, 2020	Observance of continuous and end-December 2019 performance criteria, completion of fourth review	252.92	350.79	36.25	181.25
Fifth Review	June 15, 2020	Observance of continuous and end-March 2020 performance criteria, completion of fifth review	252.92	350.79	36.25	217.50
Sixth Review	September 15, 2020	Observance of continuous and end-June 2020 performance criteria, completion of sixth review	252.92	350.79	36.25	253.75
Seventh Review	December 15, 2020	Observance of continuous and end-September 2020 performance criteria, completion of seventh review	252.92	350.79	36.25	290.00
Eighth Review	March 15, 2021	Observance of continuous and end-December 2020 performance criteria, completion of eighth review	252.92	350.79	36.25	326.25
Ninth Review	June 15, 2021	Observance of continuous and end-March 2021 performance criteria, completion of ninth review	252.92	350.79	36.25	362.50
Tenth Review	September 15, 2021	Observance of continuous and end-June 2021 performance criteria, completion of tenth review	252.92	350.79	36.25	398.75
Eleventh Review	December 15, 2021	Observance of continuous and end-September 2021 performance criteria, completion of eleventh review	252.91	350.79	36.25	435.00
Total			**3035.0**	**4209.5**	**435.0**	

Source: IMF staff estimates

1/ Ecuador's quota is SDR 697.7 million

Annex I. Implementation of Past Fund Policy Advice

The 2016 Article IV discussions focused on fiscal measures to rebalance the size and composition of revenue and spending; financial sector measures to preserve liquidity, support confidence, and enhance crisis preparedness; and measures to foster competitiveness.

1. Fiscal policy: The 2016 Article IV consultation recommended a reduction of the government wage bill through a revision of the public compensation package, the elimination of fuel subsidies with automatic adjustment of retail prices to international prices, a permanent increase in VAT and elimination of exemptions, and expenditure prioritization. Staff also called for improvements in fiscal transparency.

- The government has thus far not managed to reduce the wage bill but has announced a 10 percent reduction in the number of state enterprise workers. It also plans to renew only one of every two expiring contracts in the non-social sectors of the government, and it will bring the wages of newly hired public employees into line with those prevailing in the private sector.
- On fuel subsidies, the subsidy on high octane gasoline has been eliminated, as has the subsidy for diesel for industrial use. The subsidy on regular and ecological gasoline has been reduced. A process of public dialogue has begun on the remaining subsidies, which is expected to result in better targeting.
- The temporary increase in VAT was removed in 2017 rather than made permanent, as had been recommended by staff, and the most recent Productive Development Law introduced further tax exemptions.
- On fiscal transparency, some progress has been made with the revision and publication of more accurate public debt numbers, and more open communication channels with financial markets.

2. Financial sector policy: The 2016 Article IV report contained various recommendations aimed at increasing the resilience of the system. These related to curtailing central bank financing of the budget, reducing unnecessary financial regulation, and introducing more tools to enhance crisis preparedness.

- The Moreno administration ended direct central bank budget financing, but the BCE continued lending to public banks for budget financing purposes (the public banks used central bank funds partly to buy government-issued paper). The Productive Development Law introduced a prohibition (i) for the BCE to purchase new public securities and bonds, and (ii) for public financial institutions holding domestic investment funds from the BCE to invest in securities issued by public sector entities.
- The central bank has continued to issue Títulos del Banco Central (TBCs) although the outstanding stock had diminished to less than US$1 million by the end of January 2019.

- Interest rate ceilings remain in place. Regulations on minimum liquidity requirements remain as complex as in 2016, although there is an intention to review the regulatory gaps.
- Some initial steps have been taken to introduce risk management tools but a more comprehensive framework for macroprudential policy is needed.
- The authorities agree with the objective of diversifying the deposit insurance fund away from government paper; however, the fiscal financing imperative requires a gradual approach.
- In the Productive Development Law, there is a provision for phasing out the capital exit tax (*Impuesto a la Salida de Divisas*) and a reduction in the rate is planned as part of the program.

3. Structural reforms: Staff's recommendations were to reduce public sector and minimum private sector compensation, to shift from direct to indirect taxes, and to allow for less rigid working hours and contracts. Staff also recommended increasing productivity by easing regulations, enhancing competition, and improving institutions.

- Some progress has been made on eliminating rigidities through the introduction of different types of labor contracts in certain sectors. However, the private sector has thus far been slow to embrace the new contracts.
- Modifications have been made to oil and mining legislation to address past disincentives to foreign investment, including improving oil production-sharing contracts.
- The Productive Development Law eliminated the burdensome minimum corporate tax.
- In general, private sector representatives reported a significantly less hostile regulatory environment compared with the recent past.

4. Statistics: The 2016 Article IV consultation stressed the importance of strengthening data provision and of revising official growth projections more frequently.

- Financial Soundness Indicators and monetary statistics are now regularly provided to the IMF, although with some gaps in coverage.
- The authorities are working on the transition to the sixth BOP manual and expect to have revised BOP figures by September 2019.
- The authorities also recently received technical assistance on government finance statistics and public debt statistics, which should help with the transition to GFSM 2001 and a recent Fund TA mission on national accounts statistics provided support to a GDP rebasing project.

Annex II. Debt Sustainability Analysis

The public debt will be placed on a sustainable path with the strong fiscal improvement envisaged.[1] Debt is expected to peak in 2018–19 at around 50 percent of GDP and decline to 36.6 percent by 2023. The gross financing need is about 8.9 percent of GDP in 2018, but it declines to around 6 percent of GDP in 2019 and fall to 2.8 percent of GDP in the medium term. The projected deficit reduction is large, but a front-loaded effort is warranted to contain the increase in debt and reduce vulnerabilities. The declining debt path is particularly vulnerable to an oil shock like the one in 2015, or to a sharp deceleration in growth.

1. Definition and debt profile**.** The public-sector debt in this debt sustainability analysis (DSA) includes the obligations of the non-financial public sector (central government and non-financial sector state-owned enterprises), as reported by the authorities, as well as liabilities under oil related financing, treasury certificates, central bank lending to the government, and other liabilities. Under this measure, public debt more than doubled between 2012 and 2017 (from 17.5 to 45.4 percent of GDP). At end-2017, there was an additional 7.4 percent of GDP of accounts payable from SOEs, local governments and the social security that has now been included in debt.[2] There is also almost 3 percent of GDP in contingent liabilities that come mainly from the commercial operations of the oil companies and from potential settlements with some international oil companies. External debt accounted for about 68 percent of total debt at end-2017, of which about half was owed to official creditors. The short-term debt stock fell rapidly in 2017 (from 6.2 to 2.1 percent of GDP), as the government paid the central bank, and swapped some treasury certificates for long-term bonds. This reduction in short-term debt also resulted in a significant reduction in gross financing needs in 2018.

2. A prudent debt ceiling in Ecuador should not be higher than 40 percent of GDP. Given that Ecuador has a volatile revenue-to-GDP ratio due to the oil revenue and that it has not established a track record of achieving substantial and durable expenditure consolidation over the past decade, the debt threshold for Ecuador should be lower than the one for other emerging market economies. This would provide a safety margin against the risk of default or severe budget funding problems. Empirical evidence indicates that, for emerging market economies, sustaining a debt-to-GDP ratio above 50 percent of GDP may be difficult. Previous IMF work (WEO, 2003) found that the median public debt-to-GDP ratio for emerging markets in the year before a default was about 50 percent of GDP, and that once public debt exceeds a threshold of 50 percent of GDP the conduct of fiscal

[1] Staff's definition of public debt includes liabilities under oil related financing, treasury certificates and central bank financing, and other liabilities (including floating debt), which are not considered in the authorities' official definition, see Figure 1.

[2] A TA mission from STA on GFSM took place in August 2018 to help the authorities with the proper recording of debt statistics.

policy in emerging market economies is not consistent with fiscal sustainability.[3] Moreover, WEO (2003) argues that a sustainable debt level is lower for countries that have relatively low revenue-to-GDP ratio, high volatility of the revenue-to-GDP, as well as a weak track record of fiscal consolidations. Lledo, Sasson, and Acevedo (forthcoming) estimates maximum debt limits (MDL) and debt ceilings for Ecuador. In line with IMF (2018)[4], they define the former as the limit beyond which the likelihood of a debt distress event becomes significant and the latter as the threshold below which a debt distress event can be avoided (the MDL cannot be reached) with high probability even when negative shocks occur. To contain the probability of debt distress at less than 10 percent Ecuador's MDL is estimated at 47 percent of GDP. The probability of avoiding that MDL will be higher than 90 percent if a debt ceiling no higher than 40 percent of GDP is chosen under the assumption that fiscal policy would react to negative fiscal shocks through the implementation of a timely and durable fiscal consolidation. A debt ceiling closer to 30 percent of GDP would be necessary if the past fiscal policy track record is expected to continue. All these considerations seem to indicate that a prudent debt ceiling in Ecuador should not be larger than 40 percent of GDP and it would be desirable to lower the debt ceiling close to 30 percent in the longer term.

3. Macroeconomic and fiscal assumptions**.** Growth is projected at about 2 percent and inflation (GDP deflator) at about 1 percent over the medium term. The fiscal position under the staff proposed scenario is projected to improve to reach a primary surplus of about 5 percent of GDP by 2022. Under these assumptions, the gross financing needs of the public sector are projected to fall from 16.7 percent in 2017 to 5.6 percent of GDP in 2019 and closer to 2.5 percent of GDP in the medium term. The public-debt-to GDP ratio is projected to peak in 2018–19 at 49.2 percent of GDP, and slowly decline to 36.6 percent by 2023.

4. Stress tests. Gross financing needs do not breach the low-risk threshold of 15 percent of GDP under any of the stress-tests scenarios. However, since GFN was above the 15 percent threshold in 2017, the DSA heatmap identifies high risks in GFN under the different shocks. The significant reduction in short-term debt in 2017, which reduced GFN in 2018 and onwards, considerably reduced GFN as a source of risks going forward. The consolidation path proposed by staff would reduce GFN risks significantly by frontloading the adjustment. The public-debt-to GDP ratio will breach 50 percent of GDP in the event of real GDP growth shock, an oil shock or a combined shock. An oil shock like the one experienced in 2014–15 would be very detrimental to debt sustainability as debt could reach almost 65 percent of GDP by 2023.

5. Risks and vulnerabilities. The public DSA risk assessment identifies the ratio of public debt held by non-residents as a high risk for Ecuador, while the widening of the spread since the beginning of the year has increased once-more the market perception risk to high. At about 68 percent of the total debt, non-residents' holdings of Ecuador's public debt are high but about

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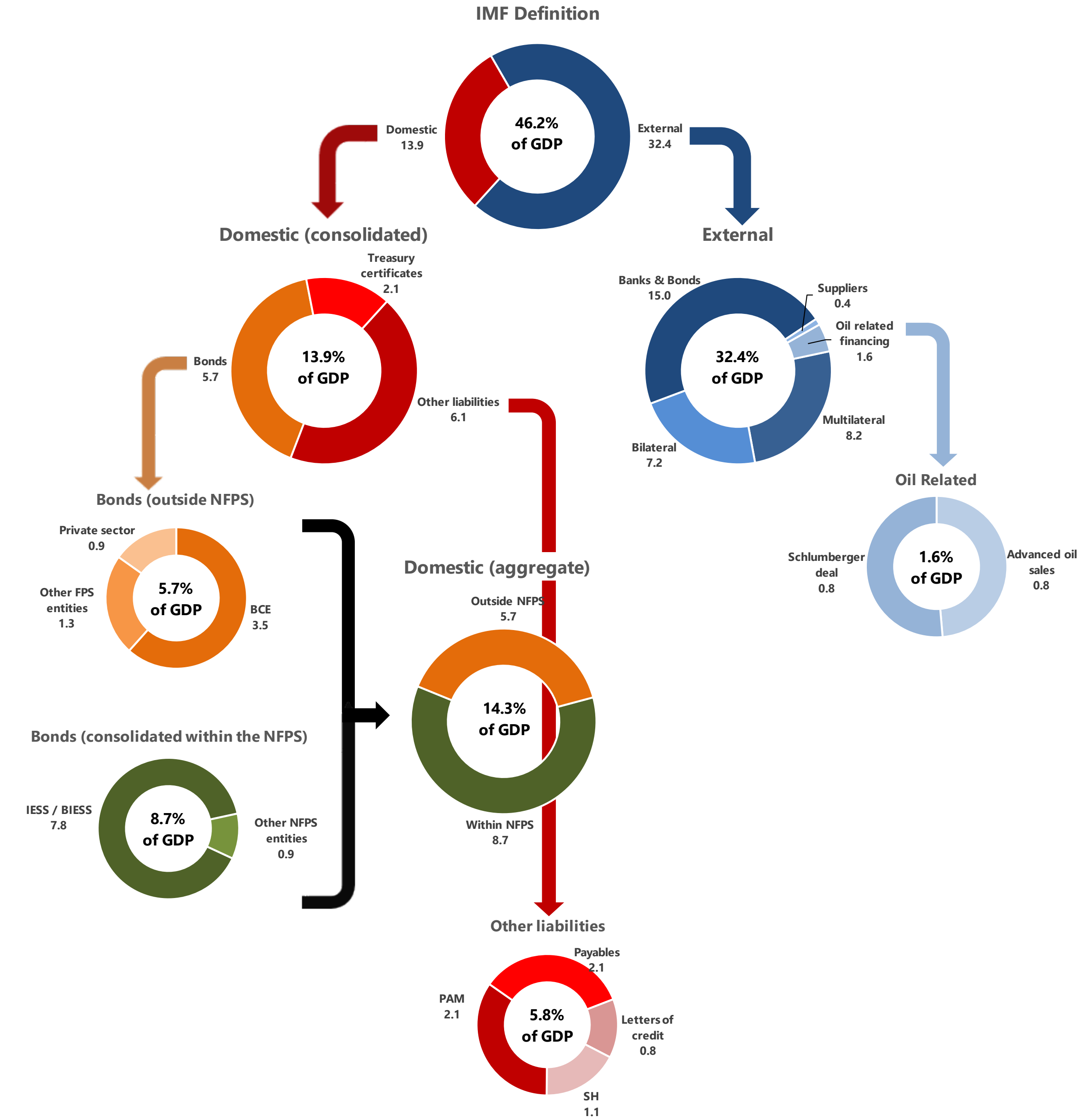
[3] See also IMF, 2013, Staff Guidance Note for Public Debt Sustainability Analysis in market Access Countries.

[4] International Monetary Fund, 2018, "How to Calibrate Fiscal Rules. A Primer" IMF How-To-Note, https://www.imf.org/en/Publications/SPROLLs/How-To-Notes (Washington).

half of external debt is owed to official creditors and therefore reduces this as a source of vulnerability. Near-term external debt rollover risks are somewhat limited (no sovereign bond matures before 2020). In 2017 there was a rapid decrease in domestic short-term debt, financed mainly by the central bank as the government reduced its short-term liabilities with the central bank by about 3.3 percent of GDP in 2017. The change created pressures on the central bank's balance sheet, because the liquidity of its assets has declined.

6. External position. The current account is projected to return to a surplus of 0.4 percent of GDP in 2019, from a small deficit of 0.7 percent of GDP expected in 2018. Over the medium-term, the current account surplus is expected to widen to 1.7 percent of GDP, helped by the expected improvement in the fiscal position. The external debt-to-GDP ratio is projected to decrease to 28.3 percent of GDP by 2023, from 37.3 percent in 2017. The external debt trajectory is sensitive to the non-interest current account shock (e.g. terms of trade shock). While a large (30 percent) real exchange rate depreciation would create unstable debt dynamics, it is an improbable scenario in a dollarized system. The relatively large external financing requirements coming due over the medium term (6.6 percent of GDP on average for 2018−23) leaves Ecuador vulnerable to sudden-stops in its access to external capital markets that would require a painful domestic adjustment.

Figure 1. Ecuador: Gross Debt Consolidated at the Non-Financial Public Sector Level, End-2018

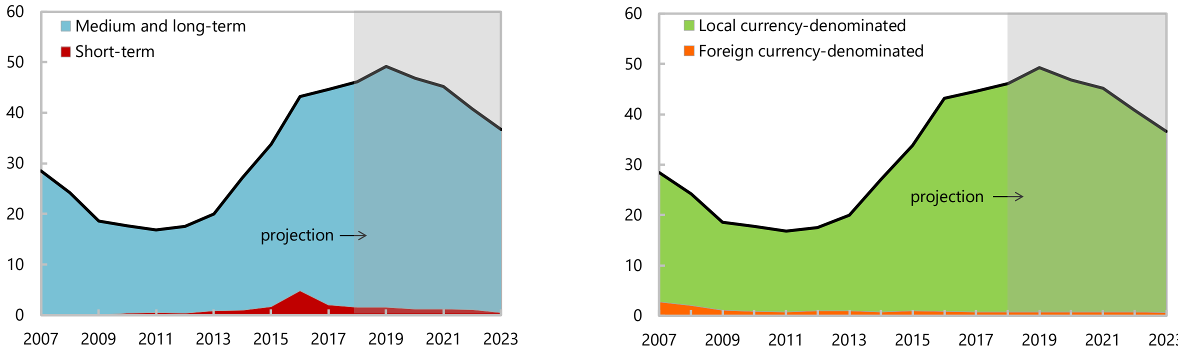


Source: Ministry of Finance; and IMF staff estimates.
Note: The domestic bonds held within the NFPS are consolidated, and thus do not add to the NFPS debt. PAM is Petroamazonas, and SH is the Hydrocarbons Secretary.

Figure 2. Ecuador: Public DSA—Composition of Public Debt and Alternative Scenarios

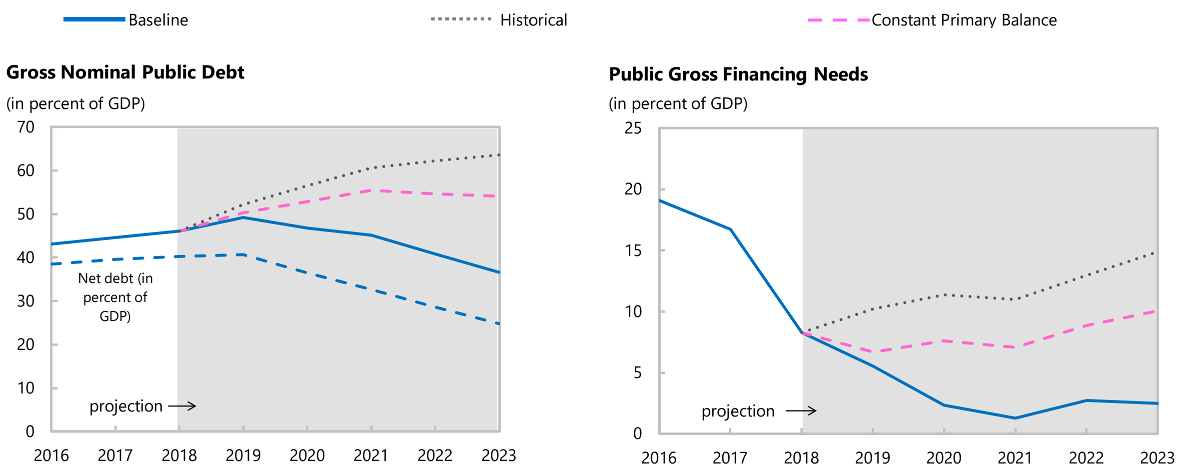
Composition of Public Debt

By Maturity (in percent of GDP) **By Currency** (in percent of GDP)



Alternative Scenarios

Gross Nominal Public Debt (in percent of GDP) **Public Gross Financing Needs** (in percent of GDP)



Underlying Assumptions
(in percent)

Baseline Scenario	2018	2019	2020	2021	2022	2023
Real GDP growth	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary Balance	1.5	2.7	6.5	5.5	5.1	5.0
Effective interest rate	5.8	5.7	5.7	5.7	5.4	5.3
Constant Primary Balance Scenario						
Real GDP growth	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary Balance	1.5	1.5	1.5	1.5	1.5	1.5
Effective interest rate	5.8	5.7	5.7	5.5	5.3	5.2

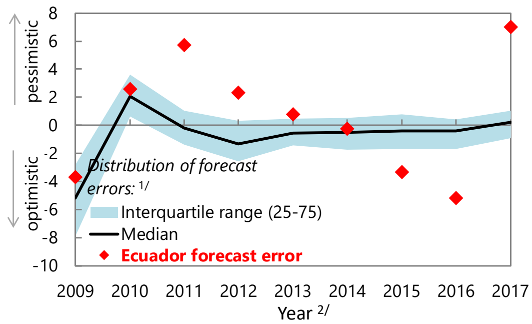
Historical Scenario	2018	2019	2020	2021	2022	2023
Real GDP growth	1.1	3.4	3.4	3.4	3.4	3.4
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary Balance	1.5	-2.3	-2.3	-2.3	-2.3	-2.3
Effective interest rate	5.8	5.7	4.8	3.9	3.2	2.9

Source: IMF staff calculations.

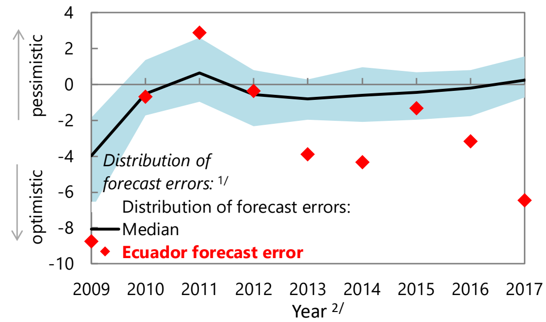
Figure 3. Ecuador: Public DSA—Realism of Baseline Assumptions

Forecast Track Record, versus all countries

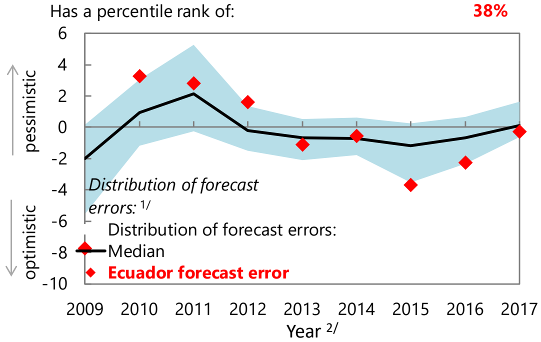
Real GDP Growth
(in percent, actual-projection)
Ecuador median forecast error, 2009-2017: **0.75**
Has a percentile rank of: **93%**



Primary Balance
(in percent of GDP, actual-projection)
Ecuador median forecast error, 2009-2017: **-3.18**
Has a percentile rank of: **7%**

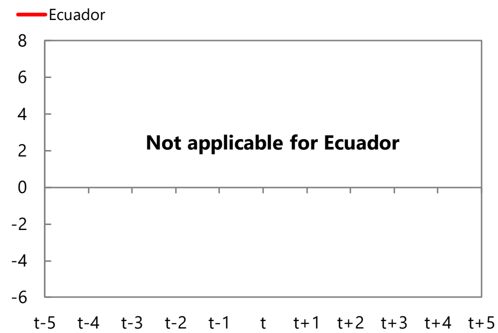


Inflation (Deflator)
(in percent, actual-projection)
Ecuador median forecast error, 2009-2017: **-0.56**
Has a percentile rank of: **38%**



Boom-Bust Analysis 3/

Real GDP growth
(in percent)

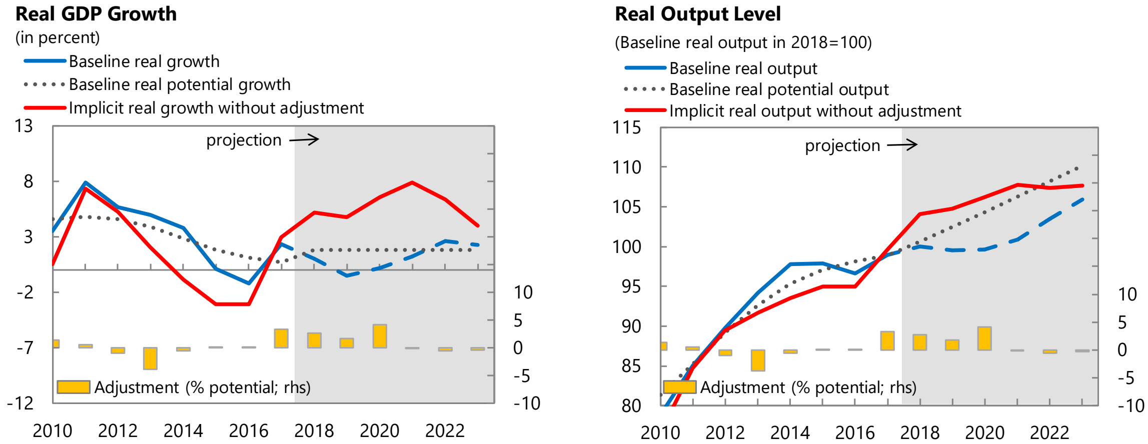


Source : IMF staff calculations.
1/ Plotted distribution includes all countries, percentile rank refers to all countries
2/ Projections made in the spring WEO vintage of the preceding year
3/ Not applicable for Ecuador, as it meets neither the positive output gap criterion nor the private credit growth criterion.

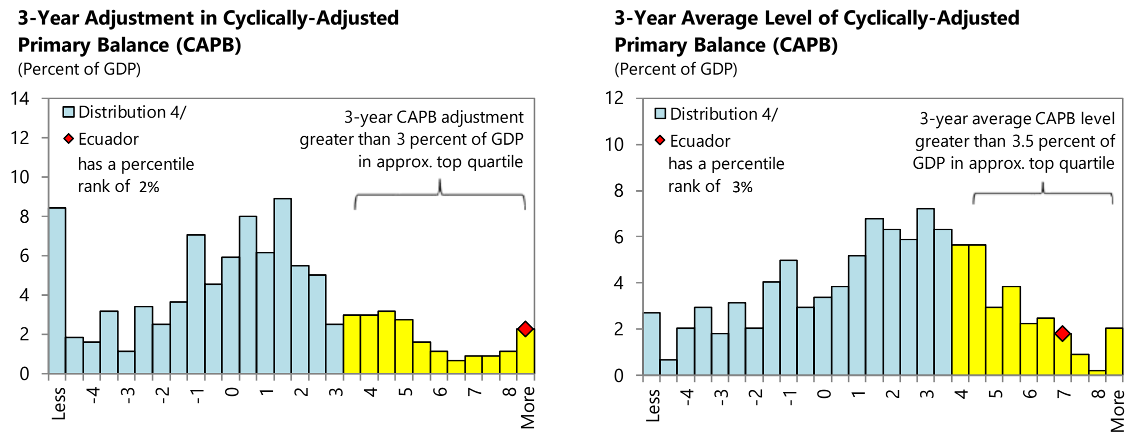
Figure 3. Ecuador: Public DSA—Realism of Baseline Assumptions (concluded)

Growth and Level of Output in Absence of Fiscal Adjustment

Assumed multiplier of 1, persistence of 0.6



Assessing the Realism of Projected Fiscal Adjustment

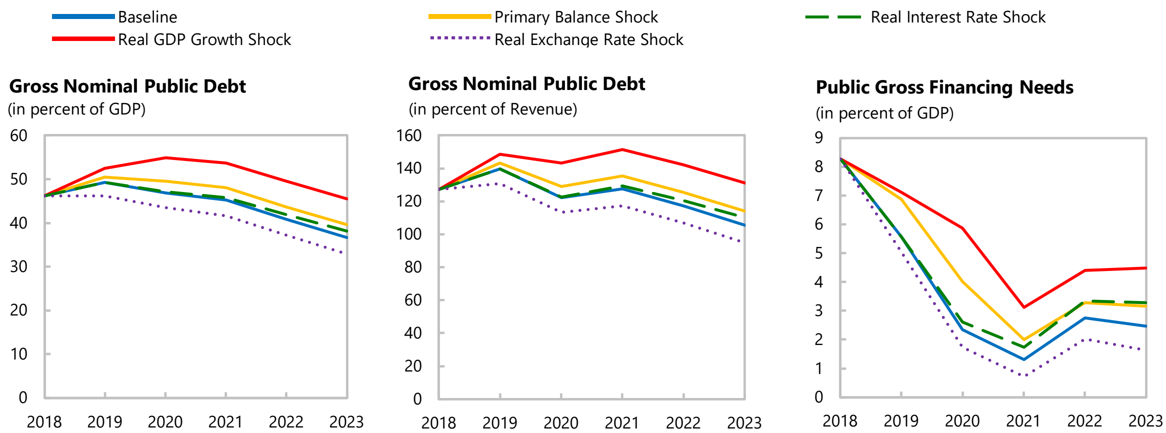


Source : IMF staff calculations.

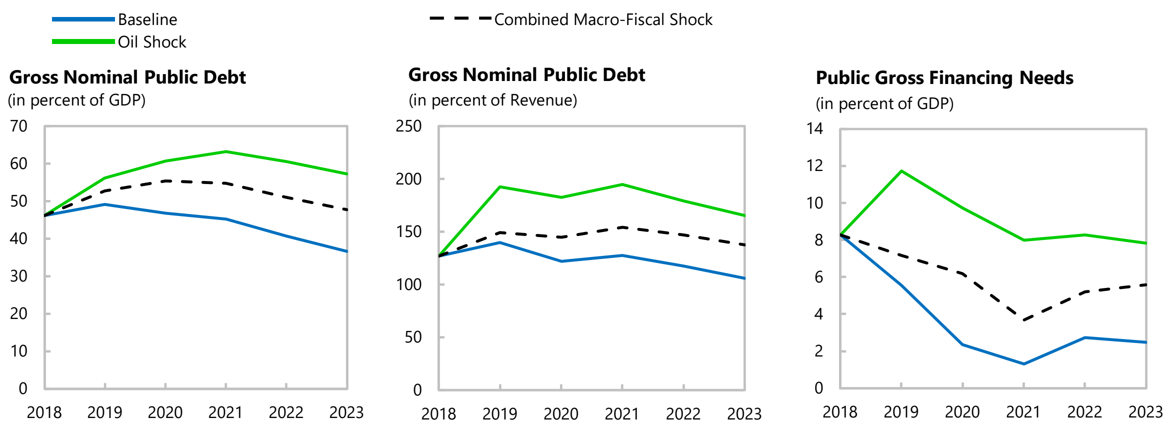
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 4. Ecuador: Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

Primary Balance Shock	2018	2019	2020	2021	2022	2023
Real GDP growth	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary balance	1.5	1.4	5.2	5.5	5.1	5.0
Effective interest rate	5.8	5.7	5.8	5.7	5.5	5.4
Real Interest Rate Shock						
Real GDP growth	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary balance	1.5	2.7	6.5	5.5	5.1	5.0
Effective interest rate	5.8	5.7	6.3	6.4	6.4	6.4
Combined Shock						
Real GDP growth	1.1	-3.4	-2.8	1.2	2.7	2.3
Inflation	2.0	-1.4	0.5	1.4	1.1	0.9
Primary balance	1.5	1.4	4.1	5.5	5.1	5.0
Effective interest rate	5.8	5.7	6.3	6.5	6.5	6.6

Real GDP Growth Shock	2018	2019	2020	2021	2022	2023
Real GDP growth	1.1	-3.4	-2.8	1.2	2.7	2.3
Inflation	2.0	-1.4	0.5	1.4	1.1	0.9
Primary balance	1.5	1.4	4.1	5.5	5.1	5.0
Effective interest rate	5.8	5.7	5.8	5.7	5.5	5.4
Real Exchange Rate Shock						
Real GDP growth	1.1	-0.5	0.2	1.2	2.7	2.3
Inflation	2.0	6.0	1.2	1.4	1.1	0.9
Primary balance	1.5	2.7	6.5	5.5	5.1	5.0
Effective interest rate	5.8	5.7	5.7	5.6	5.4	5.3
Oil Shock						
Real GDP growth	1.1	-2.5	-1.8	1.2	2.7	2.3
Inflation	2.0	-0.7	1.2	1.4	1.1	0.9
Primary balance	1.5	-3.3	1.5	2.5	4.1	5.0
Effective interest rate	5.8	5.7	6.4	6.5	6.2	6.1

Source: IMF staff calculations.

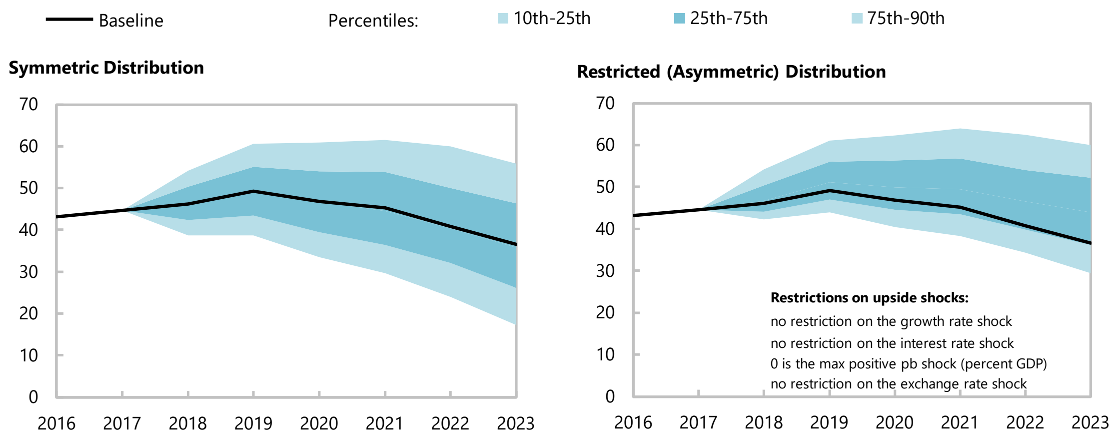
Figure 5. Ecuador: Public DSA Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

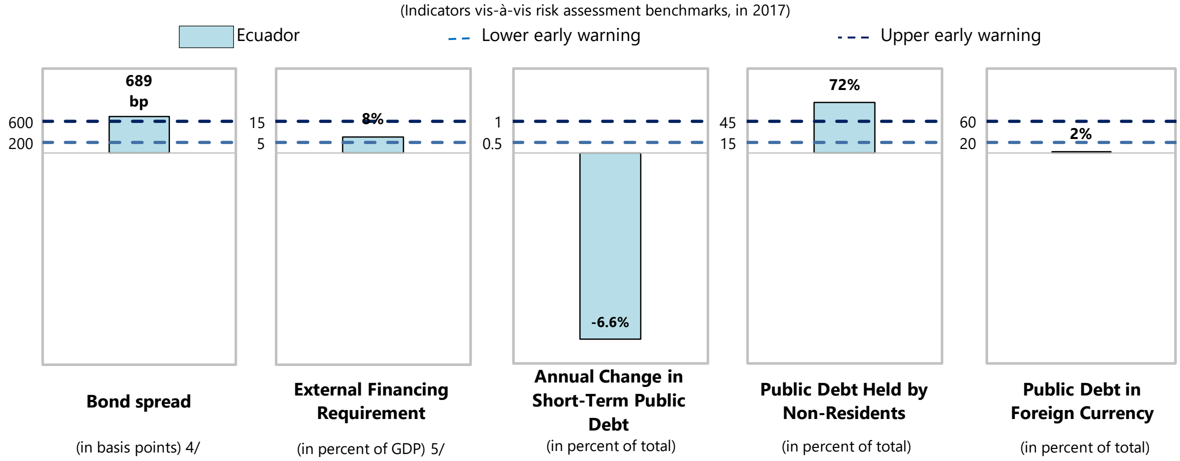
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2017)



Source: IMF staff calculations.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

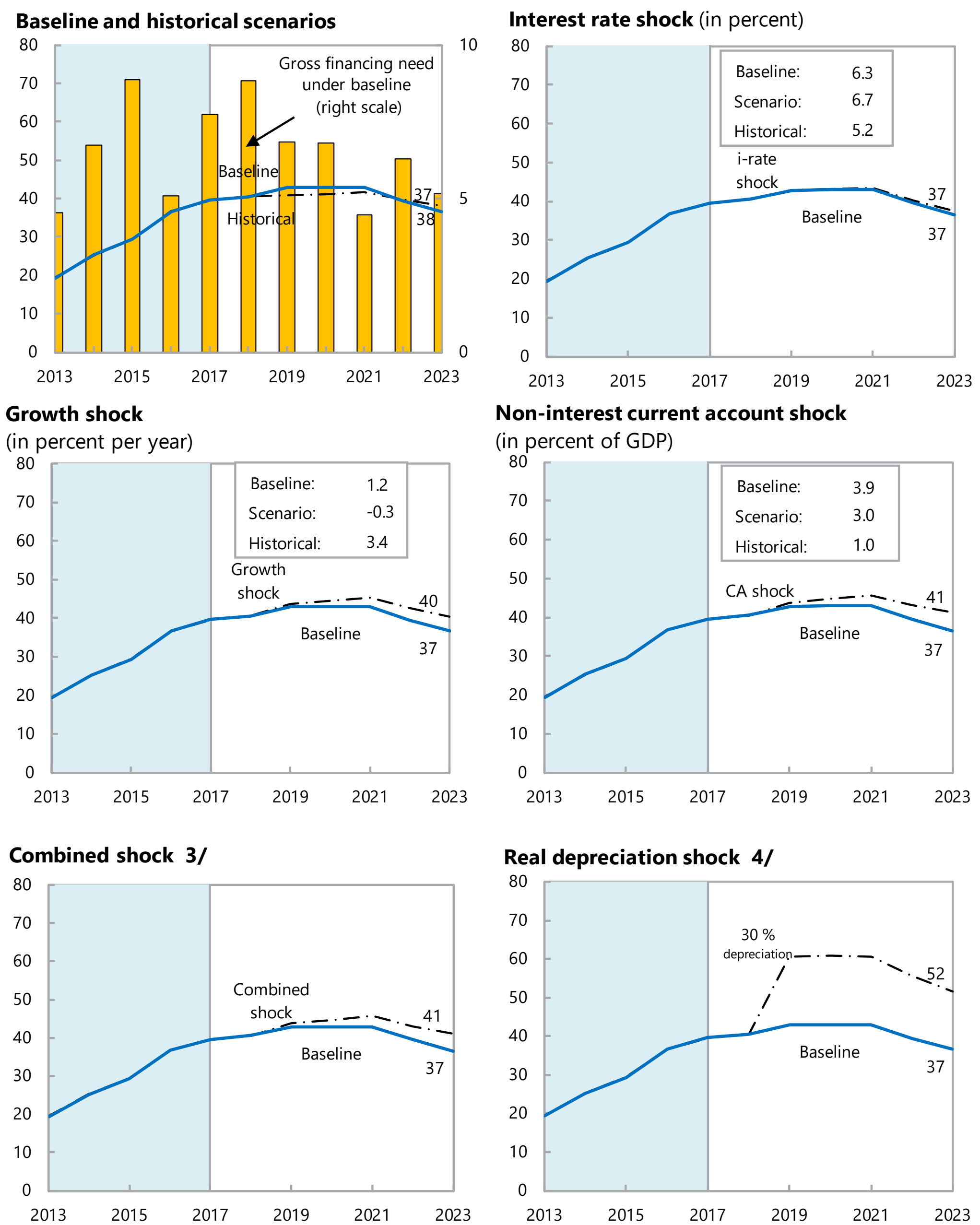
200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 17-Nov-18 through 15-Feb-19.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 6. Ecuador: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2018.

Table 1. Ecuador: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

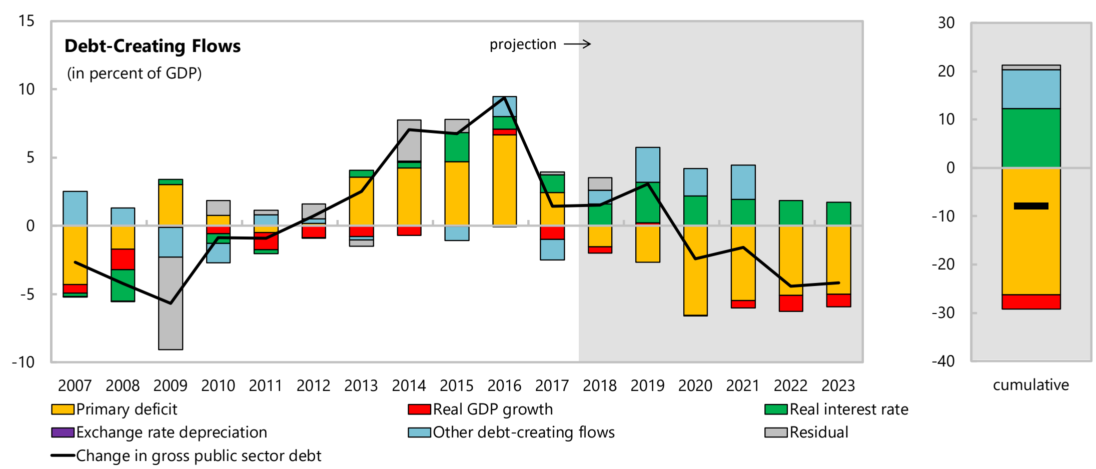
(In percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of February 15, 2019		
	2007-2015 [2/]	2016	2017	2018	2019	2020	2021	2022	2023	Sovereign Spreads		
Nominal gross public debt	22.7	43.2	44.6	46.1	49.2	46.8	45.2	40.8	36.6	EMBIG (bp) 3/		726
Public gross financing needs	5.4	19.1	16.8	8.3	5.6	2.3	1.3	2.7	2.5	5Y CDS (bp)		n.a
Net public debt	16.9	38.5	39.6	40.3	40.7	36.4	32.6	28.7	24.9			
Real GDP growth (in percent)	3.9	-1.2	2.4	1.1	-0.5	0.2	1.2	2.7	2.3	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	4.8	1.9	1.9	2.0	-0.7	1.2	1.4	1.1	0.9	Moody's	B3	B3
Nominal GDP growth (in percent)	8.9	0.7	4.4	3.1	-1.1	1.4	2.6	3.8	3.2	S&Ps	B-	B-
Effective interest rate (in percent) [4/]	4.7	4.7	5.1	5.8	5.7	5.7	5.7	5.4	5.3	Fitch	B-	B-

Contribution to Changes in Public Debt

	Actual			Projections							
	2007-2015	2016	2017	2018	2019	2020	2021	2022	2023	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	0.3	9.4	1.5	1.5	3.1	-2.4	-1.6	-4.4	-4.2	-8.0	
Identified debt-creating flows	0.4	9.5	1.2	0.6	3.1	-2.4	-1.6	-4.4	-4.2	-8.9	
Primary deficit	1.1	6.7	2.4	-1.5	-2.7	-6.5	-5.5	-5.1	-5.0	-26.3	0.8
Primary (noninterest) revenue and grant	35.0	30.3	32.0	36.3	35.2	38.3	35.5	34.8	34.7	214.8	
Primary (noninterest) expenditure	36.1	37.0	34.5	34.7	32.6	31.8	30.0	29.7	29.7	188.4	
Automatic debt dynamics [5/]	-0.7	1.3	0.3	1.2	3.2	2.1	1.4	0.7	0.8	9.3	
Interest rate/growth differential [6/]	-0.7	1.3	0.3	1.2	3.2	2.1	1.4	0.7	0.8	9.3	
Of which: real interest rate	0.0	0.9	1.3	1.6	2.9	2.2	1.9	1.9	1.7	12.3	
Of which: real GDP growth	-0.7	0.4	-1.0	-0.5	0.2	-0.1	-0.5	-1.2	-0.9	-2.9	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	1.4	-1.5	1.0	2.6	2.0	2.5	0.0	0.0	8.0	
Fiscal, General Government, Total finan	0.0	1.4	-1.5	1.0	2.6	2.0	2.5	0.0	0.0	8.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euroar	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	-0.1	-0.1	0.2	0.9	0.0	0.0	0.0	0.0	0.0	0.9	



Source: IMF staff calculations.

1/ Public sector is defined as non-financial public sector.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 2. Ecuador: External Debt Sustainability Framework, 2013–23

(In percent of GDP, unless otherwise indicated)

	Actual					10-Year	10-Year	Projections						
	2013	2014	2015	2016	2017	Historical Average	Standard Deviation	2018	2019	2020	2021	2022	2023	Debt-stabilizing non-interest current account 6/
Baseline: External debt	19.4	25.2	29.4	36.6	39.5			**40.5**	**42.8**	**42.9**	**42.9**	**39.4**	**36.5**	**-0.5**
Change in external debt	0.6	5.8	4.2	7.2	2.9			1.0	2.3	0.1	0.0	-3.5	-2.9	
Identified external debt-creating flows (4+8+9)	-1.2	-1.3	1.5	-2.3	-1.8			-0.6	-1.4	-2.7	-3.4	-4.0	-3.9	
Current account deficit, excluding interest payments	0.0	-0.4	0.8	-3.1	-1.7			-1.5	-3.2	-4.2	-4.1	-3.9	-3.9	
Deficit in balance of goods and services	2.0	1.2	2.5	-0.5	0.7			0.9	-0.7	-1.6	-1.5	-1.3	-1.3	
Exports	29.0	28.5	21.6	19.6	21.0			23.0	23.3	24.0	23.7	23.6	23.7	
Imports	31.1	29.7	24.1	19.1	21.7			23.9	22.6	22.4	22.3	22.3	22.4	
Net non-debt creating capital inflows (negative)	-0.8	-0.8	-1.3	-0.8	-0.6			-0.9	-1.2	-1.2	-1.4	-1.4	-1.4	
Automatic debt dynamics 1/	-0.4	-0.2	2.0	1.6	0.5			1.8	3.0	2.7	2.1	1.3	1.4	
Contribution from nominal interest rate	1.0	1.0	1.4	1.8	2.1			2.2	2.8	2.8	2.6	2.4	2.2	
Contribution from real GDP growth	-0.9	-0.7	0.0	0.4	-0.8			-0.4	0.2	-0.1	-0.5	-1.1	-0.9	
Contribution from price and exchange rate changes 2/	-0.6	-0.6	0.6	-0.5	-0.7			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	1.8	7.2	2.7	9.5	4.7			1.5	3.7	2.7	3.4	0.5	1.1	
External debt-to-exports ratio (in percent)	66.7	88.6	136.1	187.0	188.2			176.2	183.9	178.7	180.6	167.0	154.4	
Gross external financing need (in billions of US dollars) 4/	4.3	6.8	8.8	5.1	8.1			9.5	7.3	7.3	4.9	7.2	6.1	
in percent of GDP	4.5	6.7	8.9	5.1	7.7			8.8	6.8	6.8	4.5	6.3	5.2	
Scenario with key variables at their historical averages 5/								**40.5**	**40.9**	**41.0**	**41.7**	**39.7**	**38.2**	**-1.6**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	4.9	3.8	0.1	-1.2	2.4	3.4	2.9	1.1	-0.5	0.2	1.2	2.7	2.3	
GDP deflator in US dollars (change in percent)	3.1	3.0	-2.5	1.9	1.9	4.0	4.4	2.0	-0.7	1.2	1.4	1.1	0.9	
Nominal external interest rate (in percent)	5.7	5.8	5.4	6.0	5.9	5.2	0.8	5.8	6.9	6.6	6.2	5.9	5.9	
Growth of exports (US dollar terms, in percent)	4.8	4.8	-25.9	-8.7	12.0	5.0	19.8	12.8	0.1	4.5	1.5	3.1	3.5	
Growth of imports (US dollar terms, in percent)	6.7	2.0	-20.8	-20.3	18.6	5.7	20.9	13.6	-6.5	0.5	2.1	3.9	3.6	
Current account balance, excluding interest payments	0.0	0.4	-0.8	3.1	1.7	1.0	1.8	1.5	3.2	4.2	4.1	3.9	3.9	
Net non-debt creating capital inflows	0.8	0.8	1.3	0.8	0.6	0.8	0.4	0.9	1.2	1.2	1.4	1.4	1.4	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate.
e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex III. Risk Assessment Matrix

Risk Assessment Matrix (RAM)[1]				
Source of Risk	**Risk Likelihood**	**Impact**		**Policy Advice**
		Rating	**Channel**	
Country specific risks:				
External financing shortfalls due to Ecuador-specific events	Medium	High	Balance of payments and fiscal financing pressures	Fiscal, financial and supply side policies (described in the report) to restore stability.
Political and social opposition to policy changes under the program	Medium	High	A rolling back of commitments to fiscal measures could result in a failure to meet program targets	Careful calibration of fuel subsidy, tax, and wage reforms, and a well-thought-out communication strategy
Natural disaster (earthquake or eruption of the Cotopaxi volcano)	Low	High	Negative impact on investment, exports, and growth.	Fiscal, financial and supply side policies (described in the report) to create space to respond. Seek international financial support in recovery efforts.
Regional risks:				
Increase in flow of migrants from Venezuela	Medium	Medium	Fiscal and social pressures.	Fiscal policies in the near term to create space to respond.
External risks:				
Sharp tightening of global financial conditions	High	High	Balance of payments and fiscal financing pressures	Fiscal, financial and supply side policies (described in the report) to restore stability.
Weaker-than-expected global growth / Significant U.S. slowdown / Significant China slowdown/	Medium / Medium / Low/ Medium	High	Negative impact on investment, exports, and growth.	Fiscal, financial and supply side policies (described in the report) to restore stability.
Rising protectionism and retreat from multilateralism	High	Medium	Negative impact on investment, exports, and growth.	Fiscal, financial and supply side policies to strengthen competitiveness.
Unsustainable macroeconomic policies in systemically important countries	Medium	Medium	Impact on investment, exports, and growth.	Fiscal, financial and supply side policies to strengthen competitiveness.
Lower energy prices	Medium	High	Pressure on fiscal and external accounts.	Fiscal, financial and supply side policies (described in the report) to restore stability.

[1] Based on the July 2018 GRAM. The RAM shows events that could materially alter the outlook (both the current policies and staff's proposed scenarios). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the scenarios projections ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Annex IV. External Sector Assessment

The country's external position is assessed to be weaker than the level consistent with medium-term fundamentals and desirable policies. The real effective exchange rate is assessed to be about 30 percent overvalued. Consistently with this view, Ecuador's non-oil export share has been declining through time as high wage inflation has eroded Ecuador's international competitiveness. Over the medium term as result of the fiscal adjustment and the structural reforms that will be undertaken during the program period the current account is expected to reach a surplus of around 1.7 percent of GDP. This will realign the current account and the real exchange rate with the medium-term fundamentals.

Current Account Position

1. **The current account position exhibited a sharp shift into surplus in 2016 as a consequence of import compression that reversed during 2017.** In 2018 the deficit is expected to continue widening. Ecuador's current account position improved during 2016 to record surplus of 1.4 percent of GDP. However, this adjustment of 3.6 percent of GDP was underpinned by a recession at home and by the imposition of temporary tariffs on imports to safeguard the balance of payments position. The trade surplus reached 1.6 percent of GDP notwithstanding a reduction of 1½ percent of GDP in exports (relative to 2015). Remittances and the service and primary income accounts remained stable as a percent of GDP. For 2017, exports grew by 12 percent and with the safeguards in place for the first half of the year, the trade balance turned into a small surplus of 0.3 percent of GDP, and the current account was also close to balance (a deficit of 0.3 percent of GDP). For 2018, the trade balance is expected to be closed to balance while the current account is expected to turn into a deficit of 0.7 percent of GDP.

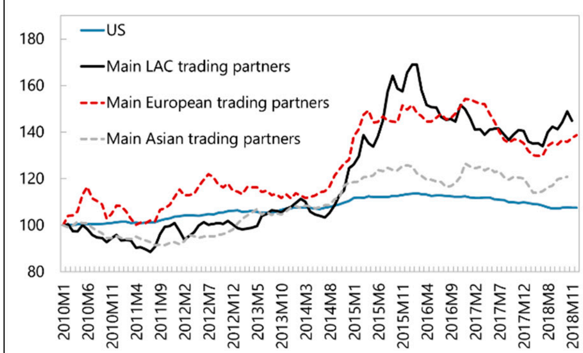
2. **Ecuador's external position is weaker than the level consistent with medium-term fundamentals and desirable policies (see Table 1).** Estimates based on a consumption-based allocation rules model specially designed to take into account characteristics of oil-exporting countries suggest a current account surplus norm of 3.0 percent of GDP. The 2016 current account surplus was 1.3 percent of GDP. However, once adjustment is made for the impact of temporary import safeguards and for Ecuador's cyclical position, the underlying current account was a deficit of 0.4 percent of GDP. In 2017, the underlying current account deficit rose to 1.6 percent of GDP as growth recovered and the temporary import tariffs were removed in the second half of 2017. In 2018, imports have continued to grow at a fast pace (13.5 percent). This would imply a 3.7 percent of GDP current account gap that would need to be closed by a significant adjustment in the fiscal deficit and efforts to raise productivity and reduce labor costs.

Real Exchange Rate and Competitiveness

3. **After a significant appreciation in 2014–15 the REER has weakened**. The REER depreciated by 6.6 percent in 2017, due to inflation remaining below trading partners (Ecuador's average inflation has fallen to -0.2 percent, from 0.4 percent in 2016) and a depreciation of the U.S.

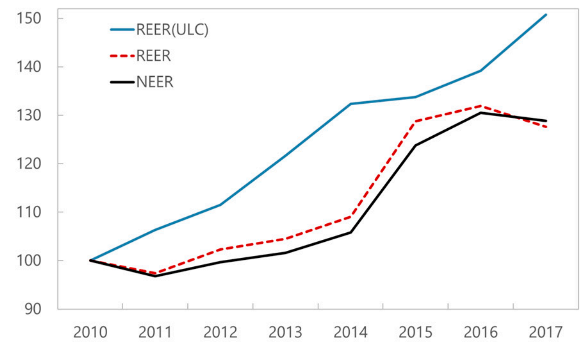
dollar. In 2018 the REER has appreciated by 1.8 percent despite inflation continuing being low, due to the appreciation of the U.S. dollar. The nominal effective exchange rate depreciated by 4.0 percent during 2017 but such depreciation has fully reversed during 2018.[1]

Ecuador: Real Bilateral Exchange Rate
(Jan-10=100)



Sources: INS and Fund staff calculations.

Ecuador: Real and Nominal Effective Exchange Rates
(2010=100)



Sources: INS, ILO, and Fund staff calculations.

Ecuador: External Sector Assessments for 2018 (in Percent) 1/

	CA Norm	Underlying CA 2/	CA GAP	Elasticity 5/,6/	REER GAP
Consumption-based allocation rules	3.0	-0.7	-3.7	-12%	30.6
Investment-based allocation rules 3/	0.1	-0.7	-0.8	-12%	6.7
EBA-lite Current Account (ELCA) 4/	2.2	-1.1	-3.3	-12%	27.0
EBA-lite REER (ELRER)					5.7

Source: IMF staff calculations.

1/ The ELCA and the consumption-based allocation rules approaches calculate the difference between the 2018 CA balance and the estimated CA “norm”.

2/ The underlying CA corresponds to the cyclically adjusted CA for the EBA-lite CA model, and to the actual CA for the other models.

3/ The investment-based allocation rules calculates the difference between the 2018 CA balance and the model’s CA norm once it is adjusted by taking in account seasonal factors that are not considered in the model.

4/ For the EBA-lite model deviations of the current policies from the desirable policies consistent with the program objectives imply a policy gap of -3.4. From this policy gap 15 percent is due to economic policies linked to private credit levels and growth, while the remainder of the gap is explained by fiscal policies, including public health expenditure policy.

5/ The estimated price elasticity of the CA to changes in the REER is based on price elasticities of exports and imports of -0.23 and 0.3 respectively. The relatively low export elasticity (-0.23 vs -0.44 for other EMs) accounts for the impact of Ecuador’s structural characteristics (inflexible labor markets, high unit labor cost relative to labor productivity and low economic diversification) on exports response to changes in terms of trade, and it is in line with the export elasticities of other commodity exporting economies.

6/ Export and import elasticities differ from those used in the EBA-lite template. The elasticities have been calibrated to account for specific features of the Ecuadorian economy, which is an oil-producer and are in line with the estimates reported in IMF Working Paper No. 10/180 for 2004 i.e. after the acceleration of oil production in Ecuador. These estimates are also in line with those reported for other oil exporters in IMF Working Paper No. 16/107. Importantly, qualitative conclusions of the assessment are robust to a range of elasticities, including those employed in EBA-lite, which imply a CA elasticity to the REER of -0.17 and are based on a panel estimation of export and import elasticities that are common across countries in the sample.

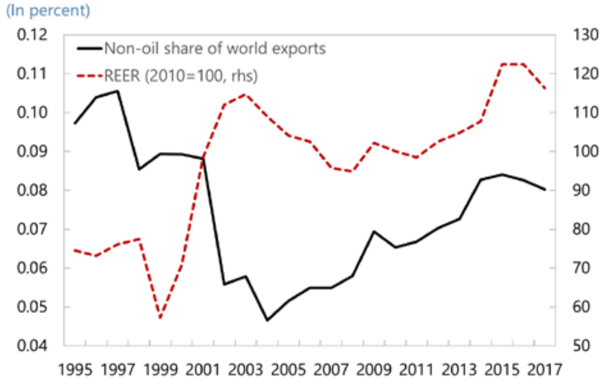
[1] The REER and the NEER series do not include Venezuela as the recent evolution of this country’s price level and official exchange rate are viewed to distort these measures

4. Ecuador's real effective exchange rate (REER) is assessed to be 31 percent overvalued. The consumption-based allocation rules model suggests that the exchange rate is overvalued by about 31 percent.[2] The assessed REER gap by the EBA-lite current account model (ELCA) **suggests** an overvaluation of 27 percent, the EBA-lite real exchange rate model (ELRER) points to an overvaluation of 6 percent. The investment-based allocation rules model, estimates a current account norm of 0.1 percent of GDP which would correspond to an overvaluation of 7 percent.[3] This leaves Ecuador in need of either a sustained period of deflation or a significant rise in productivity to reverse this overvaluation.

5. Consistent with this view, Ecuador's non-oil export market share has been declining. In the wake of the U.S. dollar appreciation of 2014–16, Ecuador lost around one-tenth of its global non-oil export market share.

Ecuador: Export Market Share and REER, 1995-2017

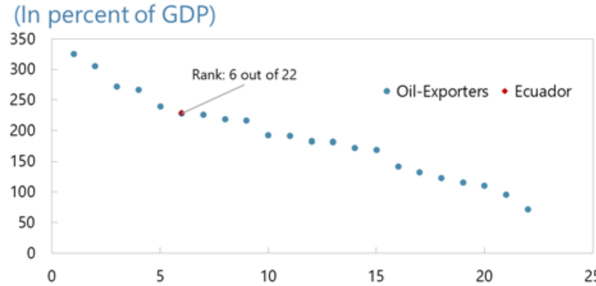
(In percent)



Sources: INS, WEO, and IMF staff calculations.

Ecuador: Capital Stock, 2015

(In percent of GDP)



Source: ICSD database and IMF staff calculations.

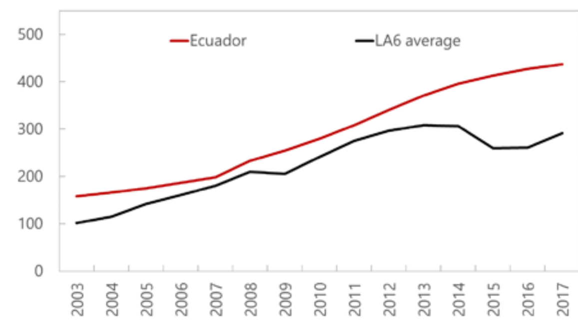
6. High wage inflation has eroded Ecuador's international competitiveness. Ecuador's minimum wage is one of the highest in Latin America, is more than 60 percent higher than the LA6 average and more than 40 percent higher than the average for Latin America and the Caribbean. For several years, the minimum wage in Ecuador has been increasing steadily while regional competitors have largely seen a low or negative change in minimum wages in U.S. dollar terms. Real wages have also been on an upward trend since 2003 that has been broad-based across sectors (although with some signs of leveling out in 2015). Wage gains in health, social services, retail and the oil sector have been particularly rapid. Over the same period, labor productivity mostly stagnated and even began to decline in 2013, resulting in a significant increase in unit labor costs: Staff estimates suggest that between 2009 and 2016 real

[2] The consumption based allocation rules methodology requires i) sustainability of the CA trajectory, i.e., the net present value (NPV) of all future oil and financial/investment income (wealth) be equal to the NPV of imports of goods and services net of non-oil exports; ii) the CA needs to support intergenerational equity and some precautionary savings in view of volatile oil prices—through an appropriate pace of accumulation of net foreign assets. Import trajectories ("annuities") are calculated in this case under a constant real per capita annuity.

[3] Ecuador's level of investment can be considered as sufficiently high for an oil exporting economy (top 25 percent in the group of oil exporters) and Ecuador continues to maintain market access albeit at high cost. According to the guidance provided in the "Background Notes on Review of the EBA-lite" (2018) the investment-needs model is better suited for countries that have large investment needs and lack market access, which is not the case for Ecuador at the moment. Therefore, staff believes that the consumption-based allocation methodology is more appropriate for the analysis of the CA and REER gaps for Ecuador than the investment-based allocation methodology.

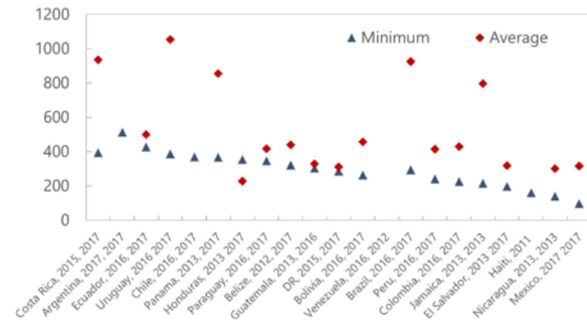
wages annual growth rate on average outpaced labor productivity annual growth by 4.6 percentage point (37 percent total growth rate over the 7 years).

Ecuador and LA6: Minimum Nominal Wages, 2003-2017
(USD per month)



Sources: Country authorities, Haver, ILO, WEO, and IMF staff calculations.
Note: LA6 includes Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.

Latin America: Minimum and Average Nominal Wages
(US$ per month)

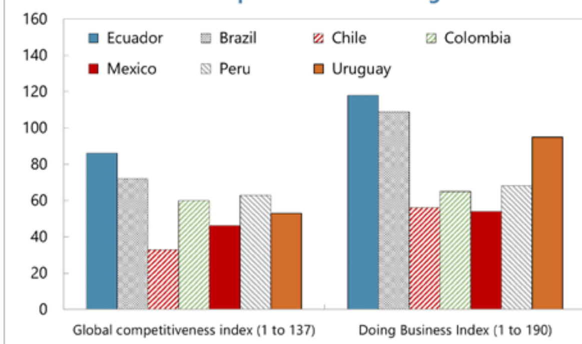


Sources: Country authorities, Haver, ILO, and IMF staff calculations.
Notes: The first (second) date after the country name is the time reference for the minimum (average) wage.

7. Ecuador's business environment is also relatively weak.[4] The Global Competitiveness Index indicates that Ecuador's relative position is behind the LA6 countries, and behind 70 percent of the 138 countries covered by the index. The Doing Business Index suggests that Ecuador is behind 60 percent of the 190 countries covered by the index. Ecuador's main weaknesses are linked to the difficulty in starting a business and in resolving insolvencies. Also, the availability of credit is more challenging than in the rest of LA6.

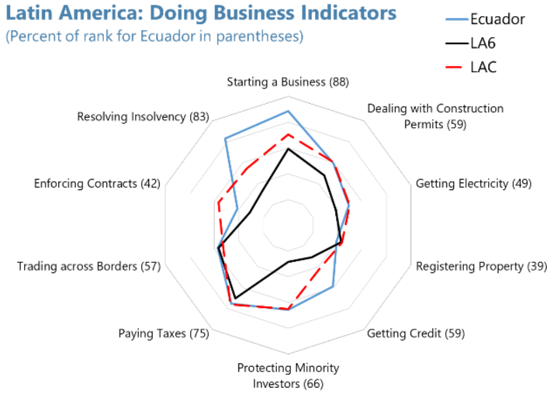
[4] The Doing Business Index is compiled by the World Bank, Global Indicators (GIG) Department and measures aspects of business regulation affecting domestic small and medium size firms. The Global Competitiveness Index is compiled by the World Economic Forum (WEF) and assess economic competitiveness based on the institutions, policies, and factors that determine the level of productivity of 138 economies. For both indices the terms and conditions under which the indicator is collected, processed and disseminated are publicly available along with external reviews of the data compilation process, but there is no internationally accepted statistical standard for the indicators and their compilation is unlikely to capture all relevant concepts, at the same time while the compiler makes efforts to validate source data some data may be outdated or have imperfect proxies and there is no report of degree of uncertainty around point estimates.

Ecuador and LA6: Competitiveness Rankings



Sources: World Economic Forum Global Competitiveness Report October 2018 and Doing Business Report 2018.

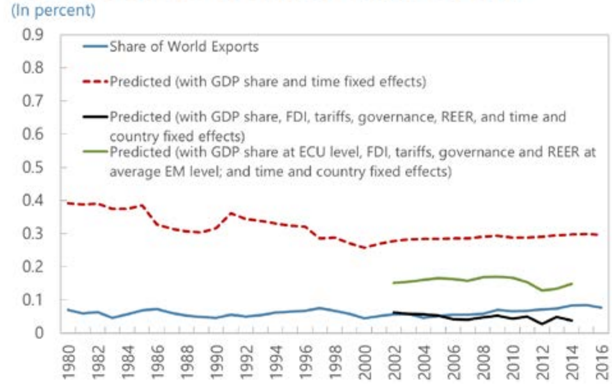
Latin America: Doing Business Indicators
(Percent of rank for Ecuador in parentheses)



Source: Doing Business Report 2018.

8. Ecuador's export performance would benefit from lower tariffs and better domestic institutions. A regression of world export share that controls for the size of a country's economy, the size of FDI, average tariff, the quality of institutions, and real exchange rate shows that Ecuador's export share is lower than other countries with a similar profile. Ecuador share of world GDP would forecast a share four times as large as Ecuador's actual export share (red line). The analysis would suggest that reducing tariffs, strengthening institutions, and eroding the overvaluation by productivity improvements and containing wage growth could almost double Ecuador's global market share.

Ecuador: Non-Oil Export Market Share, 1980-2016
(In percent)



Sources: INS, WEO, and IMF staff calculations.

9. The ratification of a trade agreement with the European Union in 2017 is an important step towards improving Ecuador's competitiveness. Over the past decade, the European Union became a major trading partner for Ecuador, especially as a result of the Multilateral Trade Agreement and the broadening of the applicability of the Generalized System of Preferences. In January 2017, Ecuador joined the EU-Colombia/Peru Trade Agreement which envisages the eventual elimination of tariffs for all industrial and fisheries products[5], greater market access for agricultural products, public procurement and services, and further reduction in technical barriers to trade. Importantly, from Ecuador's perspective the EU-Colombia/Peru Trade Agreement improves access for its main exports to the European Union (fisheries, cut flowers, coffee, cocoa, fruits, nuts, and bananas). Finally, the agreement includes commitments on the enforcement of labor and environmental standards, as well as rapid and effective dispute settlement procedures.

[5] The tariff cuts, however, will be implemented over 17 years, with the EU liberalizing almost 95 percent of tariff lines upon entry into force, and Ecuador about 60 percent.

10. Import tariffs imposed at the end of 2017 were eliminated by June of 2018. These tariffs corresponded to a per unit surcharge fee of US$0.10 to 6000 products imposed in November 2017. Staff estimates suggested that such measure was approximately equivalent to an average increase of 2.25 percent in tariffs and could have reduced imports by US$400 million per year. The measure could also have had a negative impact on exports receipts, as 45 to 50 percent of imports are inputs into exported goods (mostly oil). Staff estimates suggested that the import costs could have reduced exports by approximately US$50 million per year. However, under the pressure from Andean Community, the government eliminated the surcharge.

11. Fiscal adjustment and the structural reforms that will be undertaken during the program period are expected to realign the current account and the real exchange rate with their medium term fundamentals. Reforms to create a more efficient tax system, maintain restraint in public wages, eliminate rigidities in wages and prices, improve the reliability and efficiency of the energy sector and capital markets, and tackle corruption will all contribute to restore international competitiveness. Over the medium term the current account is expected to reach a surplus of 1.7 of GDP, which is consistent with the restoration of international competitiveness according to the consumption-based allocation rules model.

Capital Flow, Reserve Adequacy, and the Stock Position

12. Ecuador has a five percent tax on financial transfers abroad above specific thresholds (including payments for certain imports).[6] Revenues from this tax amounted to 0.8 percent of GDP in 2016. The tax constitutes both an exchange restriction subject to Fund approval under Article VIII and a CFM on capital outflows. [7] The government announced that it plans to phase out the tax on financial transfers.

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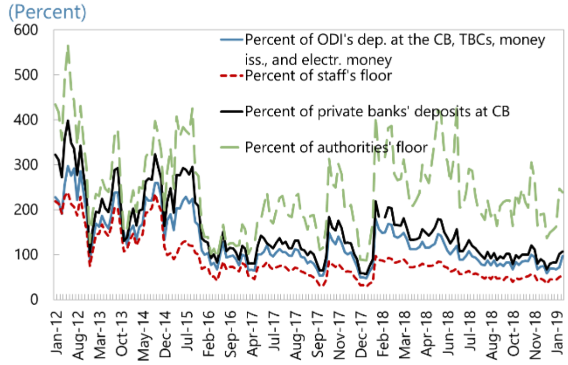
[6] Many trade related imports (i.e. essential materials, machinery and equipment) are exempted from the tax, and for other commercial import transactions, the importer may receive a tax credit. The tax seems to affect all types of flows, irrespectively of their maturity, the tax exempts some flows after five years. While dividends on investments are exempt, equity sales are subject to the tax. Outward investments by residents are also subject to the tax. In July of 2016 the authorities revised the tax on outflows by introducing a waiver for transactions of up to US$5,000 annually related to trips abroad that are paid via credit or debit card. While this change loosened the existing **restriction**, the authorities also extended the application of the 5 percent tax to any cash carried abroad (for each trip related to tourism) in excess of US$1,098 for each adult and US$366 for each minor, which constituted an **intensification** of the existing **exchange restriction**.

[7] With the balance of payments outlook having deteriorated and Ecuador now seeking a Fund program, the current circumstances can be considered as crisis or imminent crisis conditions. In this context, this might not be the right time to remove the tax on transfers abroad (as CFM), but the measure should not be permanent, and plans should be made for phasing it out once macroeconomic stability is restored, and the reserve position is strengthened.

13. Ecuador's international reserves have been on a downward path since early 2014, reflecting fiscal dominance, typical of fully dollarized economies, in a scenario of strong terms of trade shock.[8,9] The overall declining trend in the stock of reserves has been heavily influenced by BCE financing of the central government. All assets, including reserves, in the BCE balance sheet are funded by deposits of banks, nonbanks, and public institutions (mainly the central government, local governments, SOEs, and the social security).

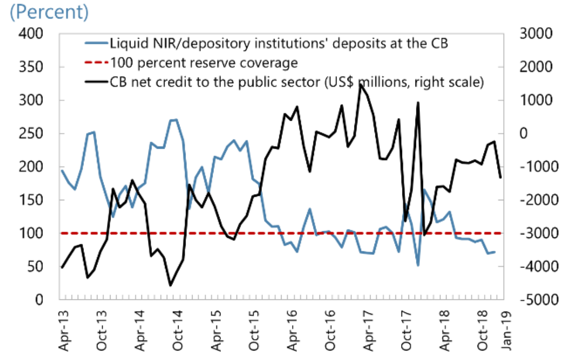
Ecuador: Liquid NIR Ratios, 2012-2019
(Percent)



Sources: Central Bank of Ecuador and IMF staff calculations.

14. Partly determined by legal requirements[10] and the positive commodity cycle, most depositing entities at the BCE maintained fairly stable or increasing net-depositor positions until 2014. At end-2017, international reserves fell to critical lows (US$2 billion, 52 percent of banks deposits at the BCE) recovering only with an international loan disbursement in January 2018. Since then, following the oil price upturn and general economic recovery, banks have been drawing down their BCE deposits to fund credit to the private sector, while foreign financing allowed the central government to improve at times its position with the central bank.

Ecuador: Liquid NIR and Net Credit to the Public Sector
(Percent)



Sources: Central Bank of Ecuador; and IMF staff calculations and projections.

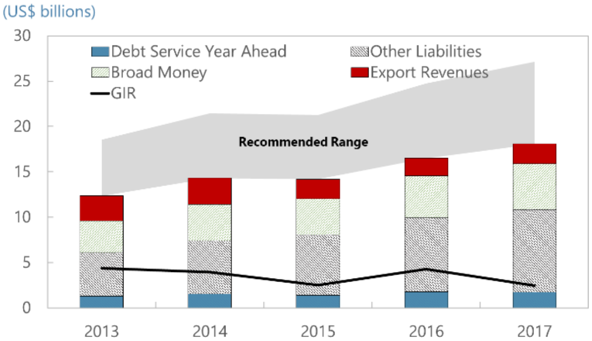
[8] For the purpose of assessing adequacy, gross reserves include: cash, deposits in foreign banks, investments, gold, SDRs, reserve position at the IMF; and liquid net reserves include: cash, deposits abroad, investments, and gold.

[9] See "Reserve Adequacy" in Selected Issues and Analytical Notes.

[10] Until the latest reform of the monetary framework in 2014 the BCE had an accounting system that avoided the comingling of public and private funds.

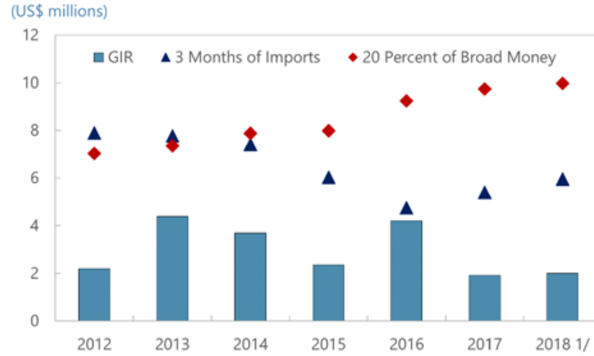
15. Reflecting those trends, the composition of the BCE's balance sheet also shifted towards domestic assets. Since late in the last decade Ecuador chose not to accumulate significant reserves, in part due to a robust public investment plan that directed proceeds from the positive commodity cycle to investment projects. However, international liquidity remained above minimum prudential levels. After 2014, the mounting financing needs of the government and the drying external financing has resulted in significant pressures on the BCE balance sheet. This led to a shift in the composition towards domestic assets (e.g. lending to the central government) and, correspondingly, to lower coverage of banks' deposits with reserves.

Ecuador: Reserve Adequacy to Risk-Weighted Metric 1/
(US$ billions)



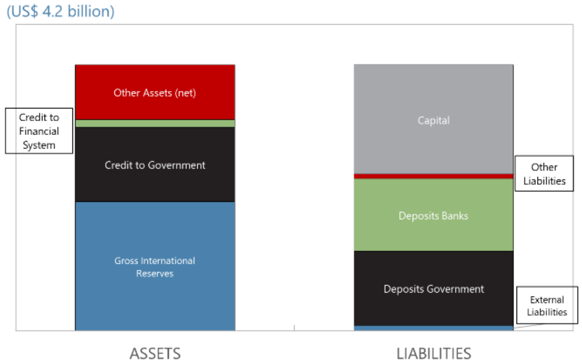
Source: Fund staff calculations and estimates.
1/ Defined as 30% of external debt service for the year ahead, 20% of other portfolio liabilities, 10% of broad money, and 10% of exports of goods and services.

Ecuador: Traditional Metrics
(US$ millions)



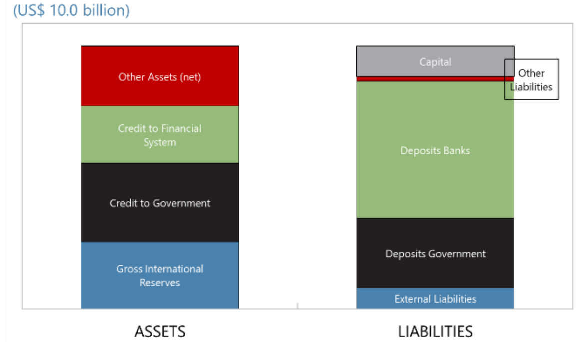
Sources: Central Bank of Ecuador and IMF staff calculations.
1/ Estimated.

Ecuador: Central Bank Balance Sheet, 2006
(US$ 4.2 billion)



Source: IMF Monetary and Financial Statistics.

Ecuador: Central Bank Balance Sheet, 2018 1/
(US$ 10.0 billion)



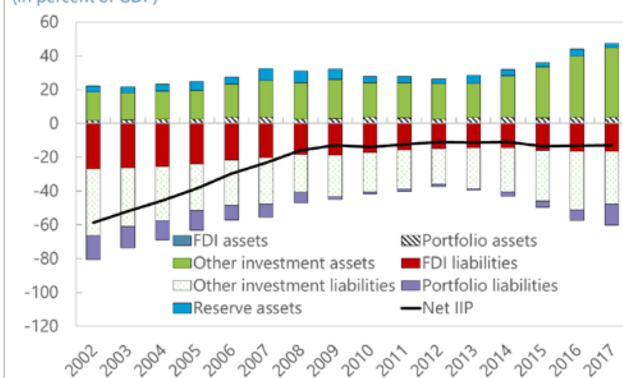
Source: IMF Monetary and Financial Statistics.
1/ As at end-October.

16. International reserves are well below levels adequate for prudential purposes and to support dollarization. Considering the standard reserve adequacy criterion and other complementary measures, the current stock of reserves in Ecuador is insufficient to mitigate potential shocks to the economy. At end-2018 the stock of gross international reserves (GIR) stood at US$2.1 billion (representing about 1¼ months of imports or 12 percent of the Fund's ARA metric). However, this amount was funded by US$3.2 billion of deposits of other depository institutions held at the central bank and US$0.363 billion in obligations to the Fund, making evident a reserve coverage gap. To supplement the ARA metric, staff also estimated a floor on reserves that comprises the minimum liquidity buffers needed to confront potential reserve drains from the banking and fiscal sectors. Up until 2015 all these claims were comfortably covered by NIR, including a fiscal buffer based on the volatility of the credit to the public sector and contingent liabilities. However, since 2016, as public financing needs ballooned and external financing to the government dwindled, the margin of coverage of these requirements faded. At end-2017, liquid reserves stood at 50 percent of staff's supplemental metric, although it has recovered somewhat since then on the basis of sovereign debt issuance.[11]

17. Gross financing needs are significant and are expected to increase over the medium term. The gross external financing requirement for 2018 is estimated at about US$9.4 billion, or 8.8 percent of GDP, with about half stemming from debt service obligations of the private sector. For 2019 these financing needs are forecasted to be US$7.3 billion, or 6.8 percent of GDP. Public sector amortizations in percent of GDP are expected to rise over the medium term. The large principal repayments on external debt coming due over the medium term (an estimated 4.0 percent of GDP on average for 2018−24) leave Ecuador vulnerable to sudden stops in access to external capital markets, though such risk is mitigated by Ecuador's decision of seeking a Fund program.

18. The Net International Investment Position (NIIP) reached -12.9 percent of GDP in 2017 and is forecasted to maintain this level during 2018. Official IIP statistics show that large increases in debt liabilities in recent years—for which there is no sectorization available, but likely primarily driven by government borrowing—have been mostly offset by an accumulation of foreign assets by the private sector.[12]

Ecuador: IIP Composition
(In percent of GDP)



Source: BCE.

[11] See "Reserve Adequacy" in Selected Issues and Analytical Notes.

[12] See "Is Ecuador Experiencing Deposit Outflows? Interpreting Data from the Balance of Payments" in Selected Issues and Analytical Notes.

Appendix I. Letter of Intent

March 1, 2019

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C.

Dear Ms Lagarde:

1. Ecuador is embarking upon a historic transition that will both modernize the economy and strengthen economic growth and job creation for generations to come. These efforts are being undertaken with special regard to Ecuador's vulnerable citizens ensuring their living standards improve as this transition proceeds. We are moving ahead with the utmost transparency, which we believe should be the hallmark of a modern Ecuador, leaving behind the opaque practices of the recent past and consulting closely with the Ecuadorian people as we embark upon our program of prosperity.

2. It is in this context that we are asking for the support of the International Monetary Fund. We have updated our comprehensive social and macroeconomic program called *Plan de Prosperidad*, which is detailed in the attached Memorandum of Economic and Financial Policies. This economic program is aligned with the objectives of our National Development Plan and has the achievement of the U.N. Sustainable Development Goals 2030 as its north star. Our program is based on four basic tenets: (i) to rebuild and strengthen the institutional foundations of dollarization; (ii) to generate employment and growth through more competitiveness; (iii) to promote equality of opportunity and protect the poor and vulnerable; and, (iv) to ensure full transparency and good governance. Additionally, strengthening Ecuador´s dollarized system will require efforts on the following fronts: restoring prudence in fiscal policy, strengthening the institutional framework of the Central Bank; boosting resilience of the financial system, and supporting job creation through competitiveness and growth.

3. To implement our program, we are requesting a three-year extended arrangement under the IMF's Extended Fund Facility in the amount equivalent to SDR3.035 billion (435 percent of quota and the equivalent of US$4.21 billion). We are requesting that the full amount of this Fund financing be made available for budget support. We have also secured support to our program from other international partners that have collectively agreed to provide additional financing of about US$6 billion over the course of the next three years.

4. The Ecuadorian government will collaborate with Fund staff to keep track of economic developments and performance under our program and we stand ready to take additional policy decisions that may become necessary to achieve our program objectives. In accordance with Fund policies, we will consult with the IMF on the adoption of these decisions and in advance of any changes to our policy plans. We are committed to providing the Fund with timely and accurate data in order to facilitate the tracking of our progress in the implementation of our program.

5. In line with the government's transparent approach to policymaking, we consent to the publication of this letter, the Memorandum of Economic Policies, and the Staff Report associated with our request for support.

Sincerely yours,

/s/	/s/
Richard Martínez Alvarado Minister of Economy and Finance	Verónica Artola Jarrín General Manager The Central Bank of Ecuador

Attachments:

1. Memorandum of Economic and Financial Policies
2. Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

1. The foundations of our dollarized economic system have been undermined by a steady erosion of domestic institutions, including the independence of the Central Bank; by a weakened system of public governance; and by persistent fiscal imbalances that are inconsistent with our dollarized economy. It is our strong commitment to reverse these trends in order to leave the next administration with a well-managed, and more socially equitable, efficient, and competitive economy.

2. We have already made important progress in implementing our policy plans in a range of areas. In August of last year, we reached consensus in the National Assembly to pass the "*Ley de Fomento Productivo*". This law put an end to Central Bank financing of the budget and introduced a new fiscal framework that will help guide policies and reduce our public debt in the short and medium term. We are also carefully reducing the cost and distortions rooted in how fuel subsidies are provided, generating efficiencies and social equity as we redirect those resources to better support for lower income households.

3. The following sections of this memorandum outline in detail our policy plans for the coming three years that will underpin our goals of strengthening the institutional foundations of dollarization, raising the living standards of our most vulnerable citizens, bolstering competitiveness and job creation, and ensuring our government is accountable to the people that it serves.

Restoring Prudence to Fiscal Policy

4. Over the past decade, our total public debt has almost doubled from 24 percent of GDP in 2008 to 46 percent of GDP in 2018 according to IMF metrics and institutional coverage. This happened despite Ecuador benefitting from unusually high world oil prices during this period. Buffers, including the Central Bank's international reserves and savings in the Oil Fund, have been eroded and the government's ability to respond to national emergencies has been seriously weakened.

5. At this stage, with global financial conditions tightening and an uncertain outlook for global oil prices, the government is committed to restoring order to Ecuador´s fiscal accounts. Our goal is to quickly reverse the upward trajectory of our public debt-GDP ratio and, over time, bring our debt below our benchmark target of 40 percent of GDP. That target will once again become a legally binding limit on future public indebtedness. Our fiscal plan is carefully designed to minimize the impact of this transition on the real economy and the living standards of the Ecuadorian people, helping generate opportunities in the near future. To bridge this transition, we are asking the Fund to provide temporary financing to the budget.

6. Our intention is to continue reducing the Non-Financial Public Sector non-oil primary deficit including fuel subsidies, by an additional 5 percent of GDP over the next three years. The burden of the realignment of our fiscal position will mostly be borne by streamlining the operations of the government but also with a broad-based effort on the part of the people of Ecuador. This effort will remain focused on promoting high quality employment, and on continued wide access to services, including health and education. The main pillars of this effort includes the following: (i) a realignment of the public sector wage bill respecting labor rights and protecting the provision of services; (ii) an optimization of the system of fuel subsidies to benefit the poor and vulnerable and reduce distortions; (iii) a reform of the tax system to make it more equitable, growth-friendly and simpler (structural benchmark under the program); and, (iv) a reduction in public spending on capital and goods and services. The savings and revenues generated from these efforts will allow us to increase spending on social assistance and phase out the distortionary tax on transfers abroad once macroeconomic stability is restored and the reserve position is strengthened.

7. A significant down-payment on this deficit reduction effort will be made in 2019. This year, we intend to achieve our fiscal goals largely through a reduction in primary spending. The measures envisaged for 2019 include:

- A careful realignment of the wage bill through a balanced strategy of wage restraint and prudent decisions on the renewal of occasional contracts and new hiring of public employees. We have already announced measures in this regard, including changes in state-owned enterprises. We also plan to renew only one of every two expiring contracts in the non-social sectors and will harmonize the wages of newly hired public employees with those in the private sector, which are currently generally lower than public sector wages;

- Continued optimization of fuel subsidies through the normalization of diesel prices for industrial purposes reducing distortions and ensuring that the intended population benefits from the subsidy. This continued optimization will get Ecuador closer to having a system to administer fuel subsidies in a way that promotes social equity and efficiency and reduces the environmental and health effects of excessive consumption. We also expect to continue to benefit from savings resulting of the increases in gasoline prices that were implemented in 2018. It is worth noting that these and future policy decisions will be designed not to affect the poor and vulnerable and that they are expected not to have a major impact on retail consumer price levels;

- Improving the terms and conditions in the procurement of goods and services by using competitive bidding, framework and wholesale agreements, making processes more transparent and timely and improving inventory management;

- Updating the schedule of fees charged for government services to more accurately reflect their costs and the markets they serve;

- Leasing concession rights of public assets to private partners ensuring that they remain under public ownership. This will be done with utterly transparent process maximizing the benefit to the state, ensuring coverage of services will not be affected and protecting the budget from contingent liabilities.

8. Part of the savings and revenue generated from these measures will allow the government to increase social assistance spending and provide greater support to the most vulnerable. *Plan Toda Una Vida,* the Government´s emblematic program will be strengthened. This program ensures access to health, education, safe and healthy habitat, housing and water by all segments of the population with emphasis on the most vulnerable, women, the elderly and disabled. It is our strong commitment to ensure that all Ecuadorian citizens have access to equal opportunities and a decent and fulfilling life.

9. We also intend to strengthen the structural underpinnings of our fiscal system. The revisions to the medium-term fiscal policy framework contained in the *Ley de Fomento Productivo* were a major step forward in creating a consistent, prudent, and accountable framework for the conduct of fiscal policies. We intend to strengthen this framework by complementing the expenditure growth rule with binding annual targets for the non-oil primary balance. As an end-June structural benchmark under the program, we will review the Law and corresponding regulations to ensure that public debt is comprehensively defined and, for statistical purposes, is measured on a consolidated basis in line with international standards; that the institutional coverage of the debt and expenditure rule apply to the nonfinancial public sector, that the necessary mechanisms are put in place to ensure the effective operation of the expenditure rule and its interaction with the constitutional "golden rule"; that rules dictating the accumulation of assets for the stabilization fund do not jeopardize compliance with fiscal rules and our fiscal plan; and that escape clauses, automatic correction mechanisms (e.g. for past deviations from the fiscal rules), and in-year fiscal reporting are strengthened.

10. To increase our accountability to the Ecuadorian people we will strengthen our current system of data disclosure, provision and monitoring at all stages of the budget cycle as well as institute clear and automatic enforcement mechanisms and effective sanctions for non-adherence to the law. We are also working with technical assistance experts to modernize our budget processes.

11. Amendments to the *Código Orgánico de Planificación y Finanzas Públicas* will ensure that the role of the Minister of Economy and Finance as the fiscal oversight authority is strengthened; that annual budgets are prepared in line with best international practices; that binding expenditure ceilings are introduced in line with the overall fiscal framework; that government discretion to amend approved budgets is limited and a robust framework for contingency allocation is introduced; that budget execution is kept in check by comprehensive, timely, and proper government accounting and reporting as well as the adoption of better cash management practices and commitment controls. As part of these efforts, we intend to create a system of information collection on domestic expenditure arrears, assess the current stock of expenditure arrears, and implement institutional arrangements to better report on and control expenditure commitments (structural benchmarks under the program by end-June and end-September). We will work with technical assistance experts from international institutions to modernize our budget and cash management processes and controls. We intend to publish an action plan aimed at strengthening our public financial management by the end of April and submit to the National Assembly the relevant legislative amendments by the end of June (structural benchmarks under the program).

12. In order to safeguard the creditworthiness of our country, we commit to refrain from new government international borrowing arrangements that are based on repurchase agreements or the pledging of Central Bank assets.

Strengthening the Institutional Framework of the Central Bank

13. Our strong commitment to the dollarization regime requires that the institutional basis governing the Central Bank is rebuilt and fortified with a clear legal framework. These efforts to strengthen dollarization will ensure that the purchasing power of all Ecuadorian families is protected and the financial value of their homes and other family assets is maintained, allowing access to credit and stability and predictability when making economic decisions.

14. Regrettably, the institutional foundations of the Central Bank of Ecuador have been seriously eroded but the recently passed *Ley de Fomento Productivo* has prohibited the Central Bank from investing in securities issued by public sector entities.

15. To reinforce these already-legislated limits on Central Bank budgetary financing, we have recently issued a regulation of the Monetary Board of the Central Bank that prohibits all future quasi-fiscal activities of the Central Bank as well as direct and indirect lending to the government or public sector (including loans, advances, guarantees or transactions that indirectly support lending operations of the public sector). We intend to incorporate these changes into legislation (i.e. *Código Orgánico Monetario Financiero*) by end-September (a structural benchmark under the program). We underline, however, that the Central Bank will continue to be able to provide temporary liquidity support to public banks, if needed for prudential purposes. We also intend to unwind past transactions that resulted in the Central Bank holding either directly or indirectly government debt (including the recent transfer of equity in public banks to the Central Bank's balance sheet).

16. To further strengthen the basis for dollarization, our goal is to gradually build international reserves over the remainder of this administration to ensure that, by the end of this arrangement, that international reserve assets of the Central Bank fully back both the reserves of private and public financial institutions held at the Central Bank and coins in circulation.

17. Finally, as an end-May structural benchmark, we will submit to Cabinet an overhaul the legislative underpinnings of Central Bank activities. We intend to ensure the Central Bank has clear objectives and limited functions, designed to fully support the dollarization regime. This will include strengthening operational autonomy by establishing an independent Central Bank Board that has fiduciary responsibilities to the Central Bank and building a strong internal and external audit function. As a first step in this process, and consistent with our commitment to transparency and good governance, we have recently published the past externally-audited financial statements of the Central Bank.

Boosting Resilience of the Financial System

18. We are confident that our financial system is strong, liquid, and well-capitalized. We have seen private credit growing at a rapid pace and the economic slowdown is likely to put strains on the system calling for greater supervisory scrutiny, particularly of cooperatives which have grown rapidly of late. To improve our ability to better understand and manage financial stability risks, we intend to strengthen our monitoring of household indebtedness and housing prices and will consider whether macroprudential requirements—such as loan-to-value ratios for mortgage lending—are needed.

19. To bolster confidence in the banking system, we intend to re-examine our banking resolution procedures, our crisis preparedness framework, and the adequacy of the liquidity fund and deposit insurance scheme. Over time, we will diversify the deposit insurance fund's assets away from sovereign debt.

20. Finally, to deepen financial intermediation and reduce sovereign-financial linkages we intend to simplify the various liquidity requirements that face banks to better align minimum and domestic liquidity requirements with international best practice. The liquidity constraints imposed on the financial sector will be gradually removed in order to achieve a simpler and more efficient reserve requirement system. To create a more competitive financial system, we intend to improve our interest rate policies to foster savings, investment and production.

Supporting Job Creation, Competitiveness and Growth

21. Our administration is committed to restoring the international competitiveness of our economy and to catalyzing private sector-led growth while raising living standards for all of Ecuador's people. Our goal is to make Ecuador a preferred destination for businesses worldwide and to boost employment and reduce informality in the economy. This will require fundamental changes on a number of fronts including:

Tax Regime. The government will publish a plan of the tax changes by end-August and submit to the National Assembly by end-October a legislation to upgrade our current system of taxation to make it more equitable, growth-friendly and simpler (structural benchmarks under the program). The goals of the tax reform will be to: (i) simplify the tax system, (ii) broaden the tax base; and, (iii) eliminate unwarranted and unequitable tax exemptions, special regimes and preferences which now benefit the more wealthy segments of the population; (iv) rebalance the system from direct to indirect taxation; and (v) phase out distortionary turnover taxes and levies on transfers abroad. The revenue yield from this reform will be enhanced by strengthening the current system of tax and customs administration, including the merger of tax and customs authorities.

Entrepreneurship. Our administration is committed to foster entrepreneurship and innovation as a way to bolster job creation and growth. In addition to the measures established in the *Ley de Fomento Productivo,* we are currently discussing an Entrepreneurship Law that will eliminate obstacles to business formation and operation and provide a strong legal framework for new businesses.

Housing. Our housing program "*Casa Para Todos*" will help promote job creation and activity in the construction sector while, broadening the opportunity for low and middle-income households to own their own home. We are partnering with private businesses and financial institutions in this effort and are confident that broader home ownership will provide a path for wealth creation, help the poor move out of poverty by increasing their ownership of assets and providing them a safe and healthy habitat, while also strengthening and expanding the middle class.

Labor Markets. Ecuador is in urgent need of a labor market reform that will improve access to formal jobs -especially by women and young workers-; and increase the ability and willingness of entrepreneurs and firms to hire and grow. A labor reform will involve adapting to market and social conditions, carefully rolling back the current constraints that result in less opportunities for the unemployed. With this reform we intend to gradually reduce implicit hiring costs and provide a strong incentive to create new jobs and for small and medium enterprises to grow. This reform will will converge to a labor market that adapts to different industries and responds to the needs of women and the youth.

Public-Private Partnerships. To encourage private investment, we will legislate an institutional framework for public-private partnerships guided by best international practices. We believe this will increase productivity, lessen the pressures on the budget, and create efficiency gains to support economy-wide increases in productivity.

Capital Market Regulations. To provide capital for new investments, we are examining our legal framework for capital markets to increase the flow of resources from investors to corporations that are in need of financing.

Trade. Our administration has already taken steps in opening Ecuador to world trade. The *Ley de Fomento Productivo* ensured companies will have access to international arbitration mechanisms in line with our constitutional framework. This should attract foreign investors. Our recent trade agreements with the European Union and the European Free Trade Association (EFTA) could further increase business opportunities and incentivize private investment. Our intent is to continue seeking trade agreements with both regional and international players. In this regard, we are in the process of joining the Pacific Alliance, and we expect these negotiations to be concluded in the near future.

Gender equality. While Ecuador compares favorably to other countries in the region on pay gap between men and women, we are committed to further promote fairness and gender equality. We will continue our policies of supporting families with young children and ensuring provision of childcare programs. The introduction of a broad range of employment contracts will particularly benefit women who may prefer to work part-time or in temporary employment likely increasing their participation in the workforce. Other policies aimed at making the labor market more dynamic could help stimulate the growth of the services sector, which would support participation of women in the labor market. We are committed to the reduction of gender-based violence in all its forms as shown by the recently approved legislation to prevent and eradicate it.

Promoting Shared Prosperity and Protecting the Poor and Vulnerable

22. Our nation is proud of the gains we have made in supporting those who struggle to make ends meet in their daily lives. "Plan Toda Una Vida" is a government priority and we intend to expand the coverage of the program during our administration as our poverty rate must be reduced further. Poverty rates among the rural and indigenous populations are particularly worrying. We are committed, therefore, to do more to protect the neediest members of our society. Our economic program will incorporate a significant increase (of around US$400 million) on social assistance spending in 2019 and we will maintain a floor on social assistance spending of 1 percent of GDP throughout the life of our program.

23. We are currently working with international partners to extend coverage and raise the level of benefits for the existing "*Bono de Desarrollo Humano*" conditional cash transfer program. We also intend to increase spending to support our disabled population through the "*Bono Joaquín Gallegos Lara*" program and the elderly through the "*Mis Mejores Años*" program. We intend to expand the coverage of our system of non-contributory pensions and will design a comprehensive plan to better target our social programs, ensuring their resources are concentrated on supporting those most in need. These programmatic changes will be supported by an update and modernization of the social registry (which identifies those citizens in need of assistance). This will ensure proper targeting and information management of administrative data.

24. We are committed to strengthen the efficiency and quality of primary education and health spending to improve our education and health outcomes and to underpin our longer-term efforts to build human capital and improve inclusion and mobility. Learning, preventive health and stunting are areas where our social programs will be working. We will identify efficiency gains in sectoral budgets without sacrificing coverage and quality of service provision, while prioritizing investments with high human capital returns (publication of an action plan by end-September is a structural benchmark under the program).

Transparency and Good Governance

25. Much has been achieved in promoting transparency and fighting corruption in the country during the present administration, but there is a lot more to be done, through a multi-pronged strategy that covers various areas (outlined below). The combination of these efforts will help improve the business climate, lower the cost of public financing, and support private investment and job creation.

Anti-Corruption Legislation. At the core of our strategy will be a broad anti-corruption law that we intend to submit to the National Assembly later this year (an end-September structural benchmark). The legislation will enhance the independence and power of law enforcement agencies and the judiciary; strengthen domestic and international coordination of anti-corruption efforts among different agencies; and improve access to information about government operations to facilitate civil society oversight. In advance of this legislation, this administration has already taken steps to improve governance through the appointment of a transitional Citizens Participation and Social Control Council last year. This will deepen our commitment as signatories of the United Nations Convention against corruption.

Fiscal policy. We are working to increase transparency and improve practices in Ecuador´s fiscal management. Our recent publication of public debt data that is in conformity with international standards is an important first step. We are committed to publishing greater information on our draft budget to better quantify fiscal measures and risks and to better assess our compliance with our fiscal rules. We are working with international partners to strengthen our public procurement processes and will, in the near future, require all procurement contracts to be published always in compliance with the regulations protecting personal data. Additionally, we are improving our budget management practices to ensure transparency, timeliness, quality and efficiency, and will encourage observatories to hold the government accountable on its commitments. As part of our transparency effort, we will provide detailed information on external non-financial public-sector debt, including information on all collateralized debt and debt with similar arrangements to the IMF on regular basis (prior action and quarterly structural benchmarks for end-March, end-June, end-September, and end-December under the program).

Central Bank. As discussed above, we have already published the Central Bank's financial statements for 2017 and will publish future statements as they become available. In 2019, we intend to produce the financial statements of the Central Bank in conformance with International Financial Reporting Standards and will begin publishing financial statements of the Central Bank under this new standard starting in 2021.

Oil Sector. We will begin publishing externally-audited financial statements of the state-owned enterprises, including oil companies (adoption by end-June of the regulation to ensure publication is a structural benchmark under the program) and will increase the transparency of employment policies in oil companies. To achieve greater efficiencies and improve governance, we intend to merge the operations of the two state-owned oil companies, in coordination with the Inter-American Development Bank. To further institutionalize transparency in our oil sector, over the course of the extended arrangement we will seek technical assistance to assist us in pursuing membership of the Extractive Industries Transparency Initiative.

Anti-Money Laundering and Countering Financing of Terrorism. In line with the FATF standard, we intend to develop an AML/CFT national risk assessment that properly prioritizes corruption-related threats. We will also use our regulatory and supervisory tools to ensure that banks and other relevant entities adequately monitor business relationships with senior officials and that the existing asset declaration regime for senior government officials is strengthened. The Government has recently sent draft legislation to the National Assembly to strengthen the framework to ensure that the proceeds of acts of corruption can be frozen, seized and confiscated in line with the Constitution and the United Nations Convention Against Corruption.

26. The program will be monitored based on performance criteria, indicative targets, and structural benchmarks as set out in tables 1, and 2 based on definitions in the TMU attached hereto. It is expected that the first review will take place on or after June 15, the second on or after September 15, and third on or after December 15.

Table 1. Ecuador: Quantitative Performance Criteria and Indicative Targets 2019
(in millions of US$, unless otherwise indicated)

	2019			
	End-Mar	End-Jun	End-Sep	End-Dec
Fiscal Targets 1/				
Quantitative Performance Criteria				
Floor on non-oil primary balance of the non-financial public sector, including petroleum subsidies	-712	-885	-2,450	-3,506
Floor on social assistance spending of the central government	175	440	705	1,040
Indicative Targets				
Floor on overall fiscal balance of the non-financial public sector	277	890	354	24
Monetary Targets 1/				
Quantitative Performance Criterion				
Floor on the change in the stock of NIR - program measure	1,823	2,627	2,788	3,097
Continuous Performance Criteria 2/				
Ceiling on the change in external payment arrears 3/	0	0	0	0
Ceiling on the new gross central bank direct financing of the NFPS and indirect financing to the NFPS through the public banks	0	0	0	0

Sources: Central Bank of Ecuador, Ministry of Finance, IMF staff calculations.
1/ Cumulative flow from January, 1 to the test date.
2/ Continuous performance criteria must be observed at all points in time.
3/ Excluding interest on earlier obligations resulting from the 2008 swap that have not been claimed by creditors even though authorities pursued them in good faith.

Table 2. Ecuador: Prior Actions and Structural Benchmarks

Prior Actions

1. Passage by the Monetary Board (Junta de Política y Regulación Monetaria y Financiera) of a regulation that prohibits quasi-fiscal spending by the Central Bank, as well as any direct or indirect lending to the non-financial public sector, including that via public banks. This PA covers the purchase of securities, advances, or guarantees, or financial transactions that are a condition precedent for lending operations entered into by the government. This PA does not cover trade credits.

2. Publication of the Central Bank's financial statements.

3. Provision of detailed information on external non-financial public-sector debt, including information on all collateralized debt and debt with similar arrangements, such as repo transactions, debt requiring escrow or other encumbered accounts overseas that may serve the function of collateral, and other similar debt involving the pledge, sale/resale, or encumbrance of assets. The information on collateralized debt and debt with similar arrangements will include all contracts related to such debt; information on the escrow or similar accounts overseas that may serve as the function of collateral; and detailed information for each creditor on the stock of debt, its terms (including on the amounts pledged, sold/resold, or encumbered, as well as any related commitments or obligations to purchase related or unrelated goods and/or services from the lender), and expected repayment schedules.

Structural Benchmarks

		Objective	Date
1.	Provision of detailed information on new external non-financial public-sector debt incurred during the previous quarter, including on all collateralized debt and debt with similar arrangements, such as repo transactions, debt requiring escrow or other encumbered accounts overseas that may serve the function of collateral, and other similar debt involving the pledge, sale/resale, or encumbrance of assets. The information on collateralized debt and debt with similar arrangements will include all contracts related to such debt; information on the escrow or similar accounts overseas that may serve as the function of collateral; and detailed information for each creditor on the stock of debt, its terms (including on the amounts pledged, sold/resold, or encumbered, as well as any related commitments or obligations to purchase related or unrelated goods and/or services from the lender), and expected repayment schedules.	To ensure transparency of new debt operations.	End-March, June, September, and December 2019

Table 2. Ecuador: Prior Actions and Structural Benchmarks (continued)

		Objective	Date
2.	Publication of an action plan, in coordination with IMF technical assistance, to strengthen public financial management aimed at preparing budgets with a top-down approach and medium-term orientation; implementing sound budget execution and cash management practices, and transparent fiscal reporting.	To improve budget processes.	End-April 2019
3.	Submission to the Cabinet, in coordination with Fund staff, of amendments to the Central Bank's legal framework to (i) introduce autonomous governance arrangements, (ii) improve its objectives and functions in line with best practice, (iii) provide for the phased-in recapitalization of the Central Bank, (iv) introduce a backing rule that requires a timetable to cover specific Central Bank liabilities with international reserve assets and (v) introduce a prohibition on quasi-fiscal activities of the Central Bank and on monetary financing of the government that prohibits quasi-fiscal spending by the Central Bank, as well as any direct or indirect lending to the non-financial public sector, including that via public banks (this covers the purchase of securities, advances, or guarantees, or financial transactions that are a condition precedent for lending operations entered into by the government but not trade credits), and (vi) introduce modifications to allow for the publication of external auditor's opinion and detailed notes.	To strengthen the institutional underpinnings of dollarization.	End-May 2019
4.	Submission to the National Assembly of amendments to the Organic Code of Planning and Public Finances and any other relevant laws, in consultation with Fund staff, to (i) limit the discretion of the Executive to amend the annual budget that is approved by the National Assembly and introduce a robust framework for a contingency reserve in the budget, (ii) restrict the use of CETES (treasury certificates) for short-term financing and develop a plan of reducing the current stock of CETES, (iii) explicitly define the institutional coverage of the public debt and expenditure rules to be the consolidated nonfinancial public sector (NFPS); (iv) adopt binding annual targets for the NFPS non-oil primary balance; (v) introduce the necessary mechanisms to support the effective operation of expenditure rule and	To strengthen fiscal management and clarify the fiscal rules framework.	End-June 2019

Table 2. Ecuador: Prior Actions and Structural Benchmarks (continued)

		Objective	Date
	its interaction with the Constitutional "golden rule," (vi) adopt a standardized definition of arrears and strengthen the commitments control system, and (vii) introduce clear deadlines for the submission of invoices by the provider and payment date, which could vary by the type of goods and service provided to the government.		
5.	Adoption of a government regulation to ensure the publication of audited, annual financial statements by all state-owned enterprises starting in fiscal year 2019.	To strengthen transparency of state enterprises.	End-June 2019
6.	Modernize computer systems to introduce necessary changes to collect information on domestic payment arrears of the central government.	To strengthen expenditure controls.	End-June 2019
7.	Submission of an anti-corruption legislation to the National Assembly including measures to (i) ensure that acts of corruption are criminalized in line with the UNCAC and that preventive measures, in particular with a focus on public officials, are implemented, (ii) freeze, seize and confiscate proceeds of acts of corruption in line with FATF Recommendation 4, and (iii) ensure that banks and other relevant institutions and professions are required to implement enhanced customer due diligence on senior officials in line with FATF Recommendation 12.	To improve governance and tackle corruption.	End-September 2019
8.	Publication of a plan, in coordination with IMF technical assistance, to upgrade our current system of taxation to make it more growth-friendly, simpler, and more equitable. The tax reform will be aimed at improving revenue mobilization, increasing efficiency, simplicity, and equity, shifting from direct to indirect taxes, and reducing exemptions and preferential treatment. This reform will target an increase in revenues of 1½ to 2 percent of GDP by 2021.	To improve the tax system.	End-August 2019
9.	Submission to the National Assembly, in consultation with Fund staff, of amendments to the Central Bank's legal framework to (i) introduce autonomous governance arrangements, (ii) improve its objectives and functions in line with best practice, (iii) provide for the phased-in recapitalization of the Central Bank, (iv) introduce a backing	To strengthen the institutional underpinnings of dollarization.	End-September 2019

Table 2. Ecuador: Prior Actions and Structural Benchmarks (concluded)

		Objective	Date
	rule that requires a timetable to cover specific Central Bank liabilities with international reserve assets and (v) introduce a prohibition on quasi-fiscal activities of the Central Bank and on monetary financing of the government that prohibits quasi-fiscal spending by the Central Bank, as well as any direct or indirect lending to the non-financial public sector, including that via public banks (this covers the purchase of securities, advances, or guarantees, or financial transactions that are a condition precedent for lending operations entered into by the government but not trade credits), and (vi) introduce modifications to allow for the publication of external auditor's opinion and detailed notes.		
10.	Submit to IMF staff a plan of arrears clearance based on the survey of arrears at the central government level.	To strengthen expenditure controls.	End-September 2019
11.	Publication of an action plan, in coordination with World Bank technical assistance, to strengthen the efficiency and quality of primary education and health spending.	To improve education and health outcomes.	End-September 2019
12.	Submission to the National Assembly, in consultation with Fund staff, of a broad-based growth-friendly tax reform aimed at improving revenue mobilization, increasing efficiency, simplicity, and equity, shifting from direct to indirect taxes, and reducing exemptions and preferential treatment. This reform will target an increase in revenues of 1½ to 2 percent of GDP by 2021.	To improve the tax system.	End-October 2019

Attachment II. Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the performance criteria (PCs), indicative targets (ITs), and that will be applied under the Extended Fund Facility, as specified in the Memorandum of Economic and Financial Policies (MEFP) and its attached tables. It also describes the methods to be used in assessing the program's performance and the information requirements to ensure adequate monitoring of the targets.

2. Any variable that is mentioned herein for the purpose of monitoring a PC or IT and that is not explicitly defined, is defined in accordance with the Fund's standard statistical methodology, such as the Government Finance Statistics. For any variable or definition that is omitted from the TMU but is relevant for program targets, the authorities of Ecuador shall consult with the Fund staff on the appropriate treatment to reach an understanding based on the Fund's standard statistical methodology.

3. Program exchange rates. For the purposes of the program, the exchange rate of the U.S. dollar for the duration of the program is set as shown in Table 1.

Table 1. Ecuador Program Exchange Rates

US Dollar to Euro	0.87
US Dollar to Renminbi	6.70
US Dollar to Yen	108.89
US Dollar to SDR	0.71
US Dollar to British Pound	0.76
US Dollar to South Korean Won	1,112.72
US Dollar to Swiss Franc	0.99
US Dollar to Canadian Dollar	1.31
US Dollar to Danish Krone	6.52
US Dollar to Swedish Krone	9.05
US Dollar to Norwegian Krone	8.43
US Dollar to Australian Dollar	1.37
US Dollar to Mexican Peso	19.11
US Dollar to Colombian Peso	3,106.50
Gold prices (US$/ounce)	1,321.25

Source: Bloomberg, as of January 31, 2019.

4. In addition to the performance criteria listed in Table 1 of Attachment I the arrangement will include the performance criteria standard to all Fund arrangements, namely:

(i) no imposition or intensification of restrictions on the making of payments and transfers for current international transactions;

(ii) no introduction or modification of multiple currency practices;

(iii) no conclusion of bilateral payments agreements that are inconsistent with Article VIII of the IMF Articles of Agreement;

(iv) no imposition or intensification of import restrictions for balance of payments reasons;

These four performance criteria will be monitored continuously.

Quantitative Performance Criteria: Definition of Variables

Floor of the Non-Oil Primary Balance of the Non-Financial Public Sector, Including Petroleum Subsidies

Definitions

5. The Non-Financial Public Sector (NFPS, Sector Público No-Financiero) for the purposes of the program consists of the central government (PGE, including universities), Decentralized Autonomous Governments (including municipal governments, provincial governments and parish boards), Social Security Funds (including IESS, ISSFA, ISSPOL and BIESS), Non-Financial Public Corporation (detailed in the table below) and Development Bank of Ecuador (BDE).

Table 2. Ecuador: Non-Financial Public Sector Corporations Covered Under the Definition of NFPS

Empresa Pública de Exploración y Explotación de Hidrocarburos Petroamazonas EP
Empresa Pública de Hidrocarburos del Ecuador Petroecuador EP
Empresa Pública Flota Petrolera Ecuatoriana-EP FLOPEC
Ferrocarriles del Ecuador Empresa Pública - FEEP
Empresa Pública TAME Línea Aérea del Ecuador TAME EP

6. The non-oil primary balance of NFPS, including petroleum subsidies, is defined as the non-oil primary balance of the NFPS minus spending on subsidies on petroleum products.

7. The non-oil primary balance of the NFPS is defined as total non-oil revenues (ingresos no petroleros) minus primary non-oil spending (gastos primarios no petroleros). Primary non-oil revenues are recorded on cash basis.

Revenues explicitly included are:

- Tax revenues (ingresos tributarios), but excluding corporate income tax paid by state-owned oil companies;
- Social security contributions (contribuciones sociales);
- Other revenues (otros ingresos);
- Proceeds from asset monetization (i.e. revenues from the leasing of assets owned by the non-financial public sector);
- Revenues that are explicitly excluded from primary non-oil revenues are:
- Interest income (recorded on cash basis);

- Proceeds from the sale of financial assets;
- Revenues from the privatization of government-owned entities;
- Revenues from oil exports;
- Revenues from the domestic sales of oil derivatives;
- The operating surplus of state-owned oil companies (PetroAmazonas and PetroEcuador);

8. Primary non-oil spending is recorded on accrual basis and comprises spending on wages and salaries (sueldos y salarios), purchases of goods and services (compra de bienes y servicios), social security benefits (prestaciones sociales), other current spending, capital expenditures not related to oil investment, and net lending. Other current spending excludes cost of imports of petroleum derivatives (Cuenta de Financiamento de Derivados Deficitarios) and payments to private operators of oil concessions (Ministerio de Energia y Recursos Naturales no Renovables).

9. Subsidies on petroleum products include, among others, subsidies on gasoline, kerosene, diesel, natural gas and liquified petroleum gas. The subsidies are defined as the difference between the retail sales price of a product and the cost of this product. The cost for imported petroleum derivative products will be estimated as import price plus transportation, storage and commercialization costs and for domestically-produced petroleum products as refinery gate price plus transport, storage and commercialization costs.

10. Government-funded, public-private partnerships will be treated as traditional public procurements. NFPS government obligations that are accrued on public private partnerships would be recorded transparently in budget data and measured as part of the NFPS government deficit as they accrue. The accrued but not settled obligations related to these public private partnerships will be transparently recorded either as public debt or as a contingent liability of the government (e.g. public guarantees) depending on the nature of the obligation.

11. Costs associated with divestment operations or the liquidation of public entities, such as the cancellation of existing contracts or severance payments to workers, will be recorded as spending.

12. All expenditures recorded as a credit in "Account 99" (due to the lack of corresponding budget allocations) will be recorded as spending above-the-line on an accrual basis as the spending obligations accrue.

Monitoring

13. All fiscal data referred to above and needed for program monitoring purposes will be provided to the Fund within 60 calendar days from the end of each quarter. Preliminary monthly data will be provided with the lag of no more than 45 days after the end of each month.

A floor on social assistance spending of the central government.

Definitions

14. Social assistance spending for the purpose of the program is computed as the sum of all central government spending (both recurrent and capital) on the following social assistance programs:

- Bono de Desarrollo Humano
- Bono de Desarrollo Humano Variable
- Pensión Adultos Mayores
- Pensión Mis Mejores Años
- Pensión Para Personas Con Discapacidad
- Bono Joaquín Gallegos Lara
- Registro Social

Monitoring

15. Data recorded at monthly frequency will be provided to the Fund with a lag of no more than 30 calendar days after the end of each month.

A floor on the change in the stock of Net International Reserves (NIR) – program measure.

Definitions

16. Net International Reserves (NIR) of the central bank (program measure) are defined as the balance of payments concept of NIR and are computed as the US dollar value of the usable gross international reserve assets of the BCE minus (i) gross reserve-related liabilities to nonresidents of the BCE, and (ii) the reserve holdings of domestic commercial banks held at the BCE. Non-U.S. dollar denominated foreign assets and liabilities will be converted into U.S. dollar at the program exchange rates.

17. Usable gross international reserve assets comprise all readily available claims on non-residents denominated in convertible foreign currencies, consistent with the Balance of Payments Manual (Sixth Edition). In particular, they include the (i) monetary claims, (ii) free gold, (iii) holdings of SDRs, (iv) the reserve position in the IMF, and (v) holdings of fixed income instruments.

Specifically excluded from gross international reserves are:

- Any precious metals or metal deposits, other than monetary gold, held by the BCE
- Assets in nonconvertible currencies and illiquid assets
- Claims on residents.

- Any reserve assets that are pledged, collateralized or otherwise encumbered (in so far as those assets are not already excluded from gross international reserve assets of the central bank), including assets tied up in repurchase agreement transactions.
- Net positions with ALADI and SUCRE.

Gross reserve-related liabilities comprise:

- All short-term liabilities of the BCE vis-à-vis non-residents denominated in convertible foreign currencies with an original maturity of one year or less;
- The stock of IMF credit outstanding but excluding credit transferred by the Fund into a Treasury account to meet the government's financing needs directly.
- The nominal value of all derivative positions (including swaps, options, forwards, and futures) of the BCE, implying the sale of foreign currency or other reserve assets.

The reserve holdings of domestic commercial banks held at the BCE comprise:

- All liabilities of the BCE to other depository institutions ("otras sociedades de depositos", as defined in the BCE's Metodología: Informacion Estadística Mensual, 4th Edition of May 2017)

Adjustor to the floor on the change in the stock of net international reserves

18. The floor on net international reserves will be adjusted upward/downward by the amount of borrowing from non-residents above/below that envisioned under the program, as reported in Table 3 below and net of issuances related to liability-management operations that have no net impact on the outstanding stock of NFPS debt. International borrowing will comprise issuance of international bonds.

Table 3. Ecuador: Adjustors Due to International Borrowing in Excess of Program Assumptions

	2019			
	Q1	Q2	Q3	Q4
Expected program market issuance	0.0	0.0	0.0	0.0

19. The floor on net international reserves will be adjusted downward/upward by the shortfall/excess in program loan disbursements from the IMF and other multilateral institutions (the IADB, World Bank, CAF, and FLAR) as well as grants, relative to the baseline projection reported in Table 4. Program loan disbursements are defined as external loan disbursements (excluding project financing disbursements) from official creditors that are freely usable for the financing of the NFPS budget operations.

Table 4. Ecuador: Adjustors Due to Shortfall in Program Loan Disbursements by Multilaterals

	2019			
	Q1	Q2	Q3	Q4
Expected disbursement of program loans by multilaterals	651	529	1251	401

Monitoring:

20. The change in net international reserves will be measured as the change in the stock of NIR at each test date relative to the stock on December 31, 2018 which stood at negative US$1.7 billion. Foreign exchange asset and liability data will be provided to the Fund at weekly frequency within 5 business days.

Ceiling on external payment arrears by the non-financial public sector.

Definitions

21. External debt is determined according to the residency criterion except in the case of the debt securities for which the criterion is the place of issuance of the instrument.[1] The term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take several forms; the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); ii. Suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and iii. Leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the program, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

22. Under the definition of debt set out above, arrears, penalties and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are

[1] As defined in Guidelines on Public Debt Conditionality in Fund Arrangements, Decision No. 15688-(14/107).

debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

23. External payment arrears for program monitoring purposes are defined as external debt obligations (principal and interest) falling due after March 11, 2019 that have not been paid within 90 days of the due date, considering the grace periods specified in contractual agreements.

Coverage

24. This performance criterion covers the non-financial public sector. This performance criterion does not cover (i) arrears on short-term trade credit or letters of credits; (ii) arrears on debt subject to renegotiation or restructuring; and (iii) arrears resulting from the nonpayment of commercial claims that are the subject of any litigation initiated prior to March 11, 2019.

Monitoring

This PC will be monitored on a continuous basis.

Ceiling on new gross central bank direct financing to the NFPS and indirect financing to the NFPS through the public banks.

Definitions

25. Central bank (BCE) direct financing to the NFPS and indirect financing to the NFPS through the public banks includes overdraft transfers from the BCE to the entities of the NFPS as defined above, advance distribution of unrealized profits from the BCE, the BCE acquisition of government debt on the primary market or by purchase from public institutions, and the BCE lending to public banks for the purpose of acquisition of government debt on the primary market or by purchase from public institutions.

Monitoring

26. This PC will be monitored on a continuous basis. Monthly data on amortizations and disbursements of credit to NFPS and to publicly-owned banks for the purpose of financing the non-financial public sector will be provided within five business days to the Fund.

Indicative Targets (IT): Definition of Variables

A floor on the overall balance of the non-financial public sector (IT).

Definitions

27. The Non-Financial Public Sector (NFPS) is defined as above.

28. The overall balance of the NFPS is defined as the non-oil primary balance of the NFPS plus the oil balance of the NFPS plus interest revenues of the NFPS minus interest expenditures of the NFPS.

29. The oil balance of the NFPS will be defined as the sum of (i) revenues from oil exports, (ii) revenues from the domestic sales of oil derivatives, and (iii) the operating surplus of state oil companies (PetroAmazonas and PetroEcuador) minus the sum of (i) expenditures on investment in the oil sector, (ii) expenditures on imports of petroleum derivatives (de Financiamento de Derivados Deficitarios), and (iii) payments to private oil companies (Ministerio de Energia y Recursos Naturales no Renovables).

30. NFPS interest expenditures are measures on cash basis while all other expenditures are measured on accrual basis.

Monitoring

31. All fiscal data referred to above and needed for program monitoring purposes will be provided to the Fund with a lag of no more than 60 calendar days after the end of each quarter and preliminary data with the lag of no more than 45 days after the end of each month.

Other Information Requirements

32. In addition to the data needed to monitor program conditionality, the authorities will also provide to Fund staff the following data so as to ensure adequate monitoring of economic variables:

33. For the purpose of the program, NFPS debt stock will be defined in accordance with IMF Government Finance Statistics Manual (GFSM) 2014 and Public Sector Debt Guide for compilers and users. Namely, total gross NFPS debt will cover all liabilities that are debt instruments. A debt instrument is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future. The following instruments are considered debt instruments:

- Special drawing rights (SDRs);
- Currency and deposits;
- Debt securities;
- Loans;
- Insurance, pension, and standardized guarantee schemes; and
- Other accounts payable.

34. All liabilities included in the GFSM balance sheet are considered debt, except for liabilities in the form of equity and investment fund shares and financial derivatives and employee stock options. Equity and investment fund shares are not debt instruments because they do not require the payment of principal or interest. For the same reason, financial derivatives are not considered debt liabilities because no principal is advanced that is required to be repaid, and no interest accrues on any financial derivative instrument.

35. Following the above manuals, Ecuador's debt should include the following instruments:

Debt Securities

- (hold by nonresidents, and by residents non-included in the Non-Financial Public-Sector entities)
- Bonds
- Treasury certificates
- Loans
- Other Accounts Payables
- Advanced oil sales
- Schlumberger deal
- Arrears with resident suppliers

36. Any liabilities issued by entities of the NFPS, held as an asset by other entity of the NFPS should be netted out. Since the consolidation is done at the level of NFPS, central bank lending to the government is included in the stock of NFPS debt.

Monitoring

37. The data on NFPS stock of debt in US$ will be provided to the Fund monthly with a lag of no more than 30 calendar days after the end of each month.

Weekly

38. Consolidated balance sheets of the banking system, by main accounts, including deposits in the banking system, available funds, and credit to the private sector; BCE balance sheet; Financial indicators: interest rates, deposits of banks at the BCE, interbank rates.

39. Monetary data in the template agreed with Fund staff, no later than 5 business days.

Monthly

40. NFPS financing data compiled based on the detailed information on financial assets and liabilities, namely, deposits, loans, securities, equities, other accounts payable including oil related, and their amortizations, disbursements and arrears accumulation when the information on the latter becomes available.

41. NFPS cash flow data from the beginning to the end of the current fiscal year, with a lag of no more than 60 days after the closing of each month. This will include expected monthly amortizations and repayments on NFPS debt as defined above.

42. Provision of detailed information on collateralized debt and debt with similar arrangements, such as repo transactions and other similar debt involving the pledge, sale/resale, or encumbrance of assets within 2 weeks of signing new contracts. The information on collateralized debt and debt with similar arrangements will include all contracts related to such debt; information on the escrow accounts overseas that serve as collateral; and detailed information for each creditor on the stock of debt, its terms (including on the amounts pledged, sold/resold, or encumbered, as well as any related commitments or obligations to purchase related or unrelated goods and/or services from the lender), and expected repayment schedules.

Quarterly

Detailed balance of payments data, no later 90 days.

INTERNATIONAL MONETARY FUND

ECUADOR

March 4, 2019

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY—INFORMATIONAL ANNEX

Prepared by: The Western Hemisphere Department (In Consultation with other Departments)

CONTENTS

FUND RELATIONS

(As of February 19, 2019)

Financial Relations

Membership Status: Joined: December 28, 1945

General Resources Account:	**SDR Million**	**% Quota**
Quota	697.70	100.00
IMF's Holdings of Currency (Holdings Rate)	930.80	133.41
Reserve Tranche Position	28.53	4.09

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	288.36	100.00
Holdings	5.49	1.90

Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
Emergency Assistance (RFI)	261.63	37.50

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Mar. 21, 2003	Apr. 20, 2004	151.00	60.40
Stand-By	Apr. 19, 2000	Dec. 31, 2001	226.73	226.73
Stand-By	May 11, 1994	Dec. 11, 1995	173.90	98.90

Overdue Obligations and Projected Payments to Fund[1]
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2018	2019	2020	2021	2022
Principal		32.70	130.82	98.11	
Charges/Interest	1.98	7.87	6.31	3.73	2.72
Total	**1.98**	**40.58**	**137.13**	**101.85**	**2.72**

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative: Not Applicable

Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable

Safeguards Assessment: A safeguards assessment of the BCE was concluded in June 2017 in connection with the 2016 disbursement under the RFI. The assessment found that, following legal changes in 2014, the BCE's institutional framework did not provide sound safeguards for an independent management of its resources. The BCE's internal audit mandate and capacity needed strengthening. While the BCE is audited by an international audit firm, transparency should be enhanced through the full publication of the audited financial statements and adoption of IFRS. Notwithstanding recent amendments to the legal framework that prohibit certain mechanisms of lending to government, progress in implementing safeguards recommendations has been slow. The BCE has published the financial statements for 2017 and 2018 but not the auditor's notes or opinions. The safeguards assessment will be updated before the first program review.

Nonfinancial Relations

Exchange Rate Arrangement:
On February 12, 1999 the central bank abandoned the exchange rate band and floated the sucre. On March 9, 2000 the economy was dollarized at 25,000 sucres per U.S. dollar. The de jure and de facto exchange rate arrangement is an arrangement with no separate legal tender; there are local coins (small denomination) in circulation in the amount of about US$80 million. Ecuador has accepted the obligations of Article VIII, Sections 2, 3, and 4 but maintains an exchange restriction subject to Fund approval arising from a 5 percent tax on transfers for the making of payments and transfers on current international transactions. The tax was waived for the outflows relating to bank loans of over one year for specific sectors identified in the Productive code (e.g. housing and microfinance). More recently, waivers were added for transactions up to US$5,000 annually related to trips abroad that are paid using a debit or credit card, while at the same time extending the tax so that any cash taken abroad for tourism in excess of US$1,098 for each adult and US$366 for each minor will also be taxed at 5 percent.

FSAP: The most recent FSAP took place in 2004.

Last Article IV Consultation:
On July 8, 2016 the Executive Board concluded the 2016 Article IV consultation.

Technical Assistance:

FAD	Non-Resource Revenues, January/February 2019
STA	External Sector Statistics, January/February 2019
FAD	Wage Bill Reform, January 2019
MCM	Debt Management, December 2018
STA	National Accounts Statistics, November 2018
FAD	Public Financial Management, September 2018

STA	Government Finance Statistics and Public Debt Statistics, August 2018
STA	Monetary and Financial Statistics, August/September 2017
STA	Balance of Payments Statistics, August/September 2017
MCM	Network Analysis Toolkit, January 2016

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

- World Bank: http://www.worldbank.org/en/country/ecuador
- Inter-American Development Bank: https://www.iadb.org/en/countries/ecuador/overview

STATISTICAL ISSUES

(As of February 19, 2019)

I. Assessment of Data Adequacy for Surveillance
General: In spite of some shortcomings, macroeconomic data are broadly adequate for surveillance purposes.
National Accounts: The Central Bank of Ecuador (BCE) disseminates GDP series with base year 2007. Currently, quarterly and annual National Accounts data are published based on the expenditure and production approaches, both in current and constant 2007 prices. For 2017, the size of the GDP revision between the last two estimates (disseminated in March and July 2018) was significant. The income-based National Accounts are published on an annual basis, up to 2017 (data for 2016 are semi-definitive and for 2017 are provisional). Similarly, the supply and use tables (at current and constant prices), and the integrated economic accounts are disseminated for the period 2007–17. Annual gross fixed capital formation is disseminated by product under the expenditure-based GDP, and the sectoral breakdown is available up to 2016, including the disaggregation of private and public capital formation (only in current prices). The Central Bank of Ecuador has started a project to update the base year of the national accounts.
Price Statistics: The CPI has national coverage of urban cities and is based on 2011/2012 weights. Since January 2015, the CPI base year has been changed to 2014. The PPI is a fixed base Laspeyres-type index with weights based on the 2013 figures of the national accounts. International good practices recommend updating prices weights every five years.
Government Finance Statistics: The authorities publish central government and nonfinancial public sector operation statistics based on the 1986 GFS Manual. It would be advisable for the authorities to switch to the 2014 GFSM Manual, and to improve the classification of expenditures and revenues. In particular, it would be useful to report oil revenues and expenditures on gross bases and explicitly show gross revenue from exports and domestic sales separately. The Ministry of Finance has begun consolidating the statistics on Non-Financial Public Sector (NFPS) and is planning to release detailed Debt Statistics Data. It is advisable to start dissemination of the consolidated NFPS Debt Statistics Data broken down by sector.
Monetary and Financial Statistics: The BCE compiles monetary statistics generally following the methodology of the *Monetary and Financial Statistics Manual*. The BCE reports detailed monthly monetary data for the central bank and other depository corporations using the standardized report forms (SRFs). Data for other financial corporations are being compiled but still not available for publication. An integrated monetary database meeting the monetary data needs of the BCE, WHD, and STA is in operation. Core financial soundness indicators (FSIs) for deposit-takers and five (out of 13) encouraged FSIs are reported to STA on a monthly basis. No FSIs on other sectors/markets are reported.
External sector statistics: Ecuador compiles and disseminates quarterly balance of payment and annual international investment position (IIP) statistics. However, the authorities should strengthen compilation and dissemination and migrate to the sixth edition of the Balance of

Payments and International Investment Position Manual (*BPM6*). As a SDDS subscriber, Ecuador also reports the prescribed quarterly external debt data to the World Bank and disseminates monthly data on the Template on International Reserves and Foreign Currency Liquidity in its National Summary Data Page. However, it does not submit the template to STA, data are not timely, the dissemination format slightly differs from the standardized format, and the national definition of reserve assets is not fully aligned with the *BPM6*. The authorities should strengthen efforts to implement 2017 mission recommendations and remote advice provided by STA to improve quality and coverage of balance of payments, IIP, and reserves data template in the context of a dollarized economy. The authorities should improve the coverage of the non-financial private sector and the estimates of currency and deposits, compile quarterly IIP, improve classification and detail, and use source stock data (not accumulated flows) for the IIP. It is essential to improve interdepartmental and interinstitutional cooperation to make better use of available source data for compiling ESS.	
II. Data Standards and Quality	
The country has been a SDDS subscriber since March 27, 1998 and met all SDDS requirements on July 14, 2000.	

Ecuador: Table of Common Indicators Required for Surveillance
(As of February 19, 2019)

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	2/15/2019	2/20/2019	W	W	W
Reserve/Base Money	1/31/2019	2/13/2019	M	M	M
Broad Money	1/31/2019	2/13/2019	M	M	M
Central Bank Balance Sheet	2/15/2019	2/20/2019	W	W	W
Consolidated Balance Sheet of the Banking System	2/8/2019	2/20/2019	W	W	W
Interest Rates[2]	2/15/2019	2/20/2019	W	W	W
Consumer Price Index	01/2019	2/2019	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2018	2/2019	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	2018	2/2019	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Q4/2018	2/2019	M	M	M
External Current Account Balance	Q3/2018	2/13/2019	Q	Q	Q
Exports and Imports of Goods and Services	12/2018	02/2019	M	M	M
GDP/GNP	Q3/2018	12/31/2018	Q	Q	Q
Gross External Debt	12/2018	12/2018	M	M	M
International Investment Position[6]	2017	4/06/2018	A	A	A

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

Statement by Alexandre Tombini, Executive Director for Ecuador, and Francisco Rivadeneira, Advisor to Executive Director

March 11, 2019

1. On behalf of our Ecuadorian authorities, we thank IMF management and staff for their engagement and support to Ecuador's economic program. Mindful of the enormous challenges ahead, our authorities reaffirm their commitment to pursue sound macroeconomic and financial policies and are grateful to the Executive Board and the international community for their assistance in the socio-economic transformation of the country.

2. After years of excessive government intervention and large public spending, the Ecuadorian authorities have initiated a fundamental change of the country's economic structure. The current administration has recognized that the model of the past decade was unsustainable, especially in an environment of lower oil prices, highly uncertain global growth prospects, and volatile financial conditions. To support the authorities' program, the international community is committing US$10.2 billion to Ecuador over the next three years, including—in addition to the IMF—financing by the World Bank, the Inter-American Development Bank (IDB), the Development Bank of Latin America (CAF), the Latin American Reserve Fund (FLAR) and other international financial institutions. Contingent to Executive Board's approval, the Fund will contribute about USD 4.2 billion (435 percent of quota) to this effort, under an Extended Fund Facility (EFF) arrangement.

3. The authorities' economic vision is centered at creating a sustainable, dynamic, inclusive, and environment-friendly economy based on four main pillars: (i) restoring the foundations of the dollarization regime; (ii) improving competitiveness, growth, and job creation; (iii) promoting shared prosperity while protecting the poor and the vulnerable; and (iv) fostering transparency, public accountability, and good governance. The authorities are well-aware that strengthening the foundations of a dollarized economy will require substantial efforts on several dimensions, including restoring fiscal sustainability, the central bank's institutional role, and enhancing the overall soundness and resilience of the financial system.

4. To achieve their objectives, the Ecuadorian authorities have already taken important steps. For instance, in August 2018 the National Assembly passed the Productive Development Law (*Ley para el Fomento Productivo*), which, among other provisions, forbid the financing of the budget by the Central Bank of Ecuador (BCE), strengthened the fiscal framework, and stimulated private investment and job creation through tax incentives. The authorities have also reduced discretionary public spending and have started unwinding fuel subsidies, while protecting the most vulnerable segments in society. Accordingly, the non-oil primary deficit (including fuel subsidies) was lowered by an estimated 2.3 percent of GDP from 2016 to 2018.

5. Nonetheless, the authorities are adamant that more needs to be done to achieve their objectives. Therefore, they are prepared to take the necessary steps on the fiscal, financial,

institutional and competitiveness fronts to support the current monetary regime and lay the groundwork for a more prosperous and balanced economy that creates formal jobs through private investment together with a sustainable fiscal stance.

Fiscal Policy

6. The Ecuadorian authorities are strongly committed to restore fiscal discipline and sustainability. Their overarching objective is to quickly reverse the recent upward trend in public debt and, over time, bring it below 40 percent of GDP. To achieve that objective, the authorities' plan to continue reducing the non-oil primary deficit (including fuel subsidies) by an additional 5 percent of GDP over the course of the EFF arrangement. This will be reached by a combination of expenditure and revenue measures. The fiscal strategy has been carefully formulated to minimize its impact on the real economy. Importantly, part of the fiscal savings achieved in 2019 will provide space to increase social spending by around 0.4 percent of GDP. Looking forward, the authorities aim at maintaining a floor on social assistance spending of about 1 percent of GDP until 2021.

7. A significant part of the strategy to reduce the non-oil primary deficit will be attained upfront, in 2019. This will include a careful streamlining of the wage bill through wage restraint, limits to new hires and temporary contracts in the public sector and better alignment of wages of new hires with those of the private sector, further optimization of fuel subsidies for industrial use, improvement of public procurement processes, and an update of certain fees charged by the public sector. The authorities also target revenue gains stemming from concessions to the private sector.

8. Over the medium-term, reforms of the tax system will contribute to strengthen the fiscal position and facilitate investment. In the second half of 2019, the authorities plan to submit to the National Assembly a broad-based and growth-friendly tax reform. This reform will increase efficiency and equity while simplifying the tax system and reducing exemptions and preferential treatment, targeting an increase in revenues of 1.5 to 2 percent of GDP by 2021.

9. The authorities are also working to improve public financial management and intend to publish an action plan by the end of April. The action plan includes improved controls for expenditure commitments and domestic expenditure arrears, among other features.

10. The authorities are committed to strengthen the fiscal framework to enhance fiscal discipline and promote transparency and accountability. They plan to complement the current expenditure growth rule with binding annual targets for the non-oil primary balance. They also intend to review legislation to ensure that the public debt ratio is defined and measured in line with best practices, inconsistencies are eliminated, budget execution data is promptly disclosed, and future breaches to the legislation leads to effective sanctions.

11. The fiscal program anticipates that with the financial assistance provided by the international community, there will be no need, in principle, to access the international capital markets.

Central Bank Policy

12. The fact that monetary policy is constrained in a dollarized economy does not imply that there is no role for the central bank. The Ecuadorian authorities are committed to rebuild and modernize the institutional basis and structure of the BCE. They wish to consolidate the new institutional framework in legislation, ensuring that the BCE has clear objectives and functions, designed to support the dollarization. This will include strengthening the bank's operational autonomy by, among other measures, establishing an independent Board that has fiduciary responsibilities and creating strong internal and external audit functions. As a first step in this process, and consistent with the authorities' commitment to transparency and good governance, they have recently published BCE's past externally-audited financial statements.

13. Monetary financing of the deficit has been eliminated. In complement to the provisions of the Productive Development Law of 2018, regulation has been approved regarding the prohibition of all quasi-fiscal activities of the BCE. Direct and indirect lending to the public sector, including loans, advances, guarantees or any other transaction that indirectly support lending of the public sector have been duly regulated. The authorities intend to incorporate these changes into legislation by the end of 2019. The BCE will still be able to provide temporary liquidity support to public banks for prudential and financial stability purposes.

14. The authorities want to gradually rebuild international reserves to more prudent levels. It is their intention to ensure that, by the end of 2021, international reserves fully back the monetary reserves of private and public financial institutions held at the BCE plus coins in circulation.

Financial Sector

15. The Ecuadorian financial system remains sound, liquid, and well-capitalized. Nonetheless, the authorities are aware that risks to financial stability should not be neglected, particularly in the context of relatively rapid credit growth in some segments of the system. They intend to improve the monitoring of household indebtedness and house prices and may consider the need to adopt macroprudential measures to contain risks. They are also willing to support financial resilience. In order to do so, they will reassess banking resolution procedures, crisis preparedness, and the adequacy of the liquidity fund and deposit insurance scheme.

16. The authorities plan to simplify and establish more efficient liquidity requirements for banks to deepen financial intermediation and better align with international best practice. They also plan to improve interest rate policies to foster a more competitive financial system and encourage savings, investment and production.

Competitiveness and Job Creation

17. Ecuador is committed to restore international competitiveness and to attract private sector investment. This will require fundamental changes on a number of fronts, including promoting

labor market flexibility, improving infrastructure and the business environment, developing capital markets, and opening up the country to external trade.

18. Labor market reform to reduce informality, remove rigidities and facilitate access to jobs—especially for women and the youth—is a priority. This will involve carefully rolling back restrictions imposed by the current system on labor contracts and eliminating rigidities that increase hiring costs. Less rigid labor contracts will particularly benefit women and young workers that may prefer part-time jobs or temporary employment. The authorities expect that these initiatives will not only provide strong incentives for firms to create new jobs, but also bring workers from the informal to the formal sector.

19. The authorities are committed to foster entrepreneurship and innovation and are currently discussing an Entrepreneurship Law that will generate a strong legal framework to business formation and operation. To provide capital for new ventures, the capital markets' legal framework is currently being reassessed. The introduction of an institutional framework for public-private partnerships (PPPs), guided by best international practices is also in consideration.

20. On the external trade front, the authorities have already taken steps to opening Ecuador to world trade. Recent trade agreements with the European Union and the European Free Trade Association (EFTA) have increased business opportunities, and the country is in process of joining the Pacific Alliance. There is clear interest to close the negotiation process with other partners, including the United States. Ecuador is also undertaking conversations with the OCDE with the aim of accessing the organization in the future.

Social Policies and Governance

21. Poverty indicators in Ecuador have improved markedly since the end of high inflation and the adoption of dollarization in 2000. The share of the population living below the poverty line fell to 21.5 percent in 2017 from 64.4 percent in 2000, with most of the improvement being made between 2000 and 2006. The authorities are determined to resume progress on this front. Under the EFF arrangement, social assistance spending has been protected. To accelerate poverty reduction, the current administration established the plan *Toda Una Vida* and will continue to expand its coverage. The authorities are also extending coverage and raising the level of benefits for their Human Development Bond conditional cash transfer program. Specific social programs for the disabled and the elderly are also being strengthened. At the same time, the authorities are preparing a comprehensive strategy to better target their social programs and ensure that resources are used to support those most in need. This strategy will encompass improvements in the registration of beneficiaries, as well as other institutional enhancements.

22. Over a longer horizon, the authorities remain committed to strengthen the efficiency and quality of primary education and health spending, to better develop and tailor human capital to the needs of a dynamic and modern economy.

23. Much has been achieved in promoting transparency and fighting corruption in Ecuador during the present administration. However, the authorities recognize that there is room for

further progress on this front. They are committed to continue advancing good governance and combating corruption to improve the business climate, lower the cost of public financing, and support private investment and job creation.

24. The authorities intend to submit to the National Assembly later this year a broad anti-corruption law. This legislation will enhance independence and power of law enforcement agencies and the judiciary, strengthen domestic and international coordination of anti-corruption efforts, and improve access to information about government operations. Prior to this legislation, a transitional Citizens Participation and Social Control Council was appointed last year.

25. A large part of the anti-corruption strategy is related to more transparency of fiscal data and better accountability of public servants. The authorities remain committed to enhance the transparency of the draft budget process. Monitoring the adherence to the fiscal framework will be strengthened with the publishing of more timely data on the budget execution and fiscal outturns. The authorities are also working to strengthen public procurement processes and, in the future, will require all procurement contracts to be published.

26. In the case of Ecuador, any anti-corruption strategy should address risks of mismanagement of the oil wealth. The authorities will begin publishing externally-audited financial statements of the two state-owned oil companies and will increase the transparency of their employment policies and practices. They intend to merge their operations to achieve synergies and improve governance. To further institutionalize transparency in the oil sector, the authorities will seek technical assistance during the period of the EFF to pursue membership of the Extractive Industries Transparency Initiative (EITI).

27. The authorities also plan to develop an AML/CFT national risk assessment in line with FATF standards that prioritizes corruption-related threats. They will use their regulatory and supervisory tools to ensure that banks and other entities adequately monitor business relationships with senior public officials, and that the existing asset declaration regime is strengthened. The authorities plan to submit legislation to the National Assembly later this year to ensure that the proceeds of acts of corruption can be seized.

Economic Prospects and Final Considerations

28. The authorities are confident that their economic program will be successful in generating growth, jobs and prosperity to the Ecuadorian people. They see staff's short and medium-term GDP projections to be highly conservative. They agree that their fiscal consolidation effort can be contractionary, but this impact will be offset by the overall improvement in business and consumer confidence, better expectations on future economic developments, reduction in private and public financing costs, and increase in bank liquidity and credit stemming from the elimination of the external financing gap for the next three years. In this regard, Ecuador will offer a great opportunity to the Fund to better understand the working and idiosyncrasies of a dollarized economy, especially in the context of a positive confidence shock.