INTERNATIONAL MONETARY FUND

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ECUADOR

October 2020

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

In the context of the 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.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 30, following discussions that ended on August 28, with the officials of Ecuador on economic developments and policies underpinning the IMF arrangement under the Extended Fund Facility. Based on information available at the time of these discussions, the staff report was completed on September 22, 2020.
- A **Staff Statement** updating information on developments after the staff report was completed.
- An **Assessment of the Risks to the Fund and the Fund's Liquidity Position**
- A **Statement by the Executive Director** for Ecuador.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
Washington, D.C.

IMF Executive Board Approves 27-month US$6.5 billion Extended Fund Facility for Ecuador

FOR IMMEDIATE RELEASE

- The IMF Executive Board approved today a 27-month arrangement under the Extended Fund Facility (EFF) for Ecuador, with access equivalent of US$6.5 billion. The Board's approval allows for an immediate disbursement equivalent of US$2 billion for budget support.
- The program aims to protect lives and livelihoods in the wake of the COVID-19 pandemic and continue to support efforts to stabilize the economy. This includes expanding social assistance programs, ensuring fiscal and debt sustainability, and laying the foundations for strong growth that benefits all Ecuadorians.
- Strengthening fiscal transparency and promoting governance are key planks of the authorities' reform agenda. These include adopting robust cash management practices, improving transparency in public procurement, and promoting debt transparency.

Washington, DC – September 30, 2020: The Executive Board of the International Monetary Fund (IMF) approved today a 27-month extended arrangement under the Extended Fund Facility (EFF) for Ecuador, with access equivalent to SDR 4.615 billion (661 percent of quota, equivalent of US$6.5 billion). The Board's approval allows for an immediate disbursement equivalent to US$2 billion, available to the budget. The EFF arrangement follows Fund emergency support to Ecuador in May this year (67.3 percent of quota, equivalent of US$643 million) and the previous EFF arrangement approved by the IMF Executive Board in March 2019 that was canceled in May 2020.

The new EFF arrangement will support Ecuador's policies to stabilize the economy and protect lives and livelihoods, expand the coverage of social assistance programs, ensure fiscal and debt sustainability, and strengthen domestic institutions to lay the foundations for strong, job-rich, and long-lasting growth that benefits all Ecuadorians.

Following the Executive Board's discussion on Ecuador, Ms. Kristalina Georgieva, Managing Director and Chair, issued the following statement:

"The Ecuadorian authorities have undertaken bold actions to address the deep economic and health crisis triggered by the COVID-19 pandemic. Early containment measures were key to slowing and stabilizing the spread of the virus. The authorities' policy response appropriately combined short-term measures to contain the adverse impact of the crisis, including significant liquidity support and increased cash transfers, with decisive early steps towards long-term sustainability of public finances.

"The successful debt exchange with external bondholders has provided substantial liquidity relief to Ecuador. The authorities have also obtained financing assurances from official creditors, commitments from international financial institutions, and are committed to complementing them with ambitious, yet realistic, fiscal consolidation as the recovery takes hold. The ongoing and decisive expansion of social assistance programs will strengthen social safety nets and allow the government to extend relief to vulnerable groups in a timely manner.

"Against this backdrop, the IMF-supported program under the Extended Fund Facility has two main objectives: first, mitigate the crisis by protecting lives and livelihoods, and restore macroeconomic stability; and second, ensure the sustainability of public finances and strengthen domestic institutions to lay the foundations for strong, job-rich, and long-lasting growth that benefits all Ecuadorians.

"The authorities have committed to unwind the crisis-related measures as the economy starts to recover. Fiscal sustainability would be anchored on the debt ceiling under the homegrown organic budget code (COPLAFIP) of 57 percent of GDP by end-2025. It would be underpinned by a combination of a progressive tax reform over the medium-term and expenditure measures that aim to align Ecuador with regional peers. The ongoing operationalization of COPLAFIP will enforce timely and accurate provision of fiscal data by non-financial public sector entities, improve fiscal monitoring and enhance public financial management. Formulating a debt management strategy early on of near-term obligations would help improve the maturity and cost structure of amortization payments in 2022.

"Strengthening fiscal transparency and promoting governance are key planks of the authorities' reform agenda. These include adopting robust cash management practices, improving transparency in public procurement, and promoting debt transparency. In addition, enforcing the rule of law, including through the adoption of landmark anti-corruption legislation by end-year, would protect the public purse, catalyze private investment, promote job creation and boost growth potential.

"Timely implementation of the envisaged reforms to promote the autonomy of the central bank and strengthen its institutional framework more broadly will be needed to back the commitment to Ecuador's dollarization regime. The authorities are committed to continue monitoring credit risk developments and to closely supervise financial institutions in the post-pandemic period. These efforts would require strong coordination among oversight bodies, which would be facilitated by establishing a Financial Coordination Committee.

"Uncertainty about the depth and duration of the pandemic remains high globally. Domestically, close coordination among government agencies, broad-based social dialogue and buy-in across the political spectrum for the program objectives and policies would mitigate significant implementation risks. Timely implementation of the program's prior actions to strengthen institutions and policy frameworks and efforts to secure broad public support for the program are steps in the right direction. These efforts have helped meet the criteria for the IMF to provide financing exceeding normal access."

INTERNATIONAL MONETARY FUND

ECUADOR

September 22, 2020

REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY

EXECUTIVE SUMMARY

Context. On May 1, 2020, the Executive Board approved an RFI (US$643 million, 67.3 percent of quota), to support the urgent needs of the Ecuadorean economy in the wake of COVID-19 crisis, and the authorities cancelled the three-year Extended Fund Facility arrangement (US$ 4.2 billion, 435 percent of quota). The macroeconomic situation has since deteriorated, prompting the authorities to request a 27-month EFF of SDR 4.615 billion (about US$6.5 billion, 661 percent of quota), to help restore macroeconomic stability, support the most vulnerable groups, and advance the structural reform agenda initiated under the previous EFF.

Program objectives. The program will be anchored on two main objectives: first, mitigating the crisis by protecting the lives and livelihoods of the population and restoring macroeconomic stability; and second, as the economy recovers, ensuring the sustainability of public finances and strengthening domestic institutions to lay the foundations for strong, job-rich, and long-lasting growth that benefits all Ecuadorians.

Program modalities. Staff estimates that Ecuador's financing needs through 2022 are around US$6.5 billion, after factoring in the successful restructuring of external bonds, specific and credible financing assurances on financing/debt relief from official bilateral creditors, other committed financing and good prospects for additional contributions from international financial institutions (IFIs), and an ambitious, yet realistic, fiscal consolidation. The proposed access would be made available to the budget.

Exceptional access. The proposed access level is subject to the four exceptional access (EA) criteria, which have been met (Box 1). Criteria 1 and 3 are met based on Ecuador's BOP needs and the sovereign's prospects for re-gaining market access. With the successful debt exchange of external bonds specific and credible assurances on financing/debt relief, other committed financing, and Ecuador's commitment to an ambitious plan to ensure fiscal sustainability, debt is assessed to be sustainable with high probability, allowing criterion 2 to be met. Criterion 4 is assessed to be met owing to the timely implementation of prior actions and commitments to early structural benchmarks in areas that strengthen institutions and policy frameworks and improve governance; the President signing a letter of support to the program

and the statement by the National Assembly in support of the broad program objectives. These steps have helped demonstrate Ecuador's institutional capacity to implement the EA program. The program remains, however, subject to substantive risks, given heightened uncertainties surrounding the global outlook, as well as domestic factors that warrant a continued commitment from future administrations and given limited buffers. Political assurances are deemed adequate; they have been received from a broad range of presidential candidates, who are supportive of program objectives and its key policies. One candidate expressed support for the program objectives and agreed to remain in close dialogue with Fund staff, including to help iron out divergence of views on policies; one candidate was not yet ready to engage in discussions. The EA criteria are complemented by the authorities ongoing communications effort as they seek to build public awareness and broad support for the policies underpinning the Fund-supported program.

Approved By	
Krishna Srinivasan (WHD) and Maria Gonzalez (SPR)	Discussions were held via videoconferences during July 29-August 28, 2020. The report was prepared by a team comprised of Ceyda Oner (head), Botir Baltabaev, Matteo Ghilardi and Constant Lonkeng Ngouana (all WHD), Fernanda Brollo (FAD), Mario Mansilla (MCM), Leandro Medina (SPR), Mariana Sabates Cuadrado (STA), Julien Reynaud (Resident Representative) and Juan Pablo Erraez (Resident Representative Office), with support from Ivan Burgara, Nicolas Landeta (all WHD) and Lizeth Crow (Resident Representative Office). Antonio Manzanera (FIN), Virginia Alonso and Jean-Luc Helis (both FAD), Richard Berkhout, Clifford Blair, Olya Kroytor, Ivana Rossi and Karla Vasquez (all LEG) participated in some meetings and provided substantive input in the formulation of conditionality, review of legislation, and in the drafting of relevant sections of the report. Alejandro Werner, Krishna Srinivasan (WHD), Afonso Bevilaqua and Pedro Fachada (OED) attended some meetings. Francisco Rivadeneira (OED) joined the mission.

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CONTEXT AND OVERVIEW

1. **Ecuador had preexisting vulnerabilities going into the COVID-19 crisis, which were being addressed with its 2019 extended arrangement under the Extended Fund Facility (EFF).** Ecuador was already in a weaker economic position before the COVID-19 pandemic began, reflected in the government seeking a 3-year EFF (about $4.2 billion, SDR 3,035 million or 435 percent of quota) that was approved by the IMF Executive Board in March 2019. That arrangement aimed at restoring growth, putting debt on a firmly downward path, building reserve buffers and restoring international competitiveness, improving governance as well as the policy and institutional frameworks, and making substantive improvements to the social assistance system.

2. **Under the 2019 EFF, the government made progress in pursuing an ambitious reform agenda** (Annex I). In particular, the authorities took significant steps aimed at improving fiscal balances, strengthening the institutional foundations of dollarization, and providing support to the vulnerable groups. These successes rested on the reform of fiscal institutions, initial steps to strengthen the independence of the central bank, the launching of governance and transparency reforms, and measures to strengthen the social safety net.

3. **Political fragmentation and capacity constraints nonetheless impeded program implementation.** A lack of coordination and cohesion among government entities significantly impeded the effective monitoring of the program and political fragmentation in the National Assembly led to either delays in the implementation or watering-down of key reforms. For instance, a major tax reform was watered down before it was approved by the Assembly, while central bank reform was substituted with partial legislation that addressed some of the key risks. The shortcomings in implementation were reflected in program targets being reset and also resulted in a case of misreporting in December 2019.

4. **Starting with the COVID-19 pandemic, a confluence of exogenous shocks in 2020 have compounded Ecuador's pre-existing vulnerabilities, putting severe stress on its economy.** Measures aimed at containing the pandemic, a slump in external demand, the collapse in oil prices, and a temporary disruption of oil production have all weighed on economic activity (which is projected to contract by 11 percent this year). This has led to a deep contraction of government revenues, which, along with an increase in spending to mitigate the socio-economic consequences of the pandemic, notably on health services and social support, have strained public finances further. The precipitous and unprecedented drop in global demand depressed Ecuador's exports, which were further weakened by the loss in competitiveness from a strong US dollar.

5. **The economic situation has continued to deteriorate since the Fund provided emergency assistance in May.** On May 1, 2020, the IMF Executive Board noted the cancellation by Ecuador of the previous three-year EFF and approved an RFI (about $643 million, SDR 469.7 million or 67.3 percent of quota), to support the urgent needs of the Ecuadorean economy in the wake of the COVID-19 crisis while allowing more time to craft a full-fledged program. The RFI covered only 8

percent of the estimated financing gap for 2020 at the time. Since then, the economic outlook has deteriorated, and financing gaps have widened.

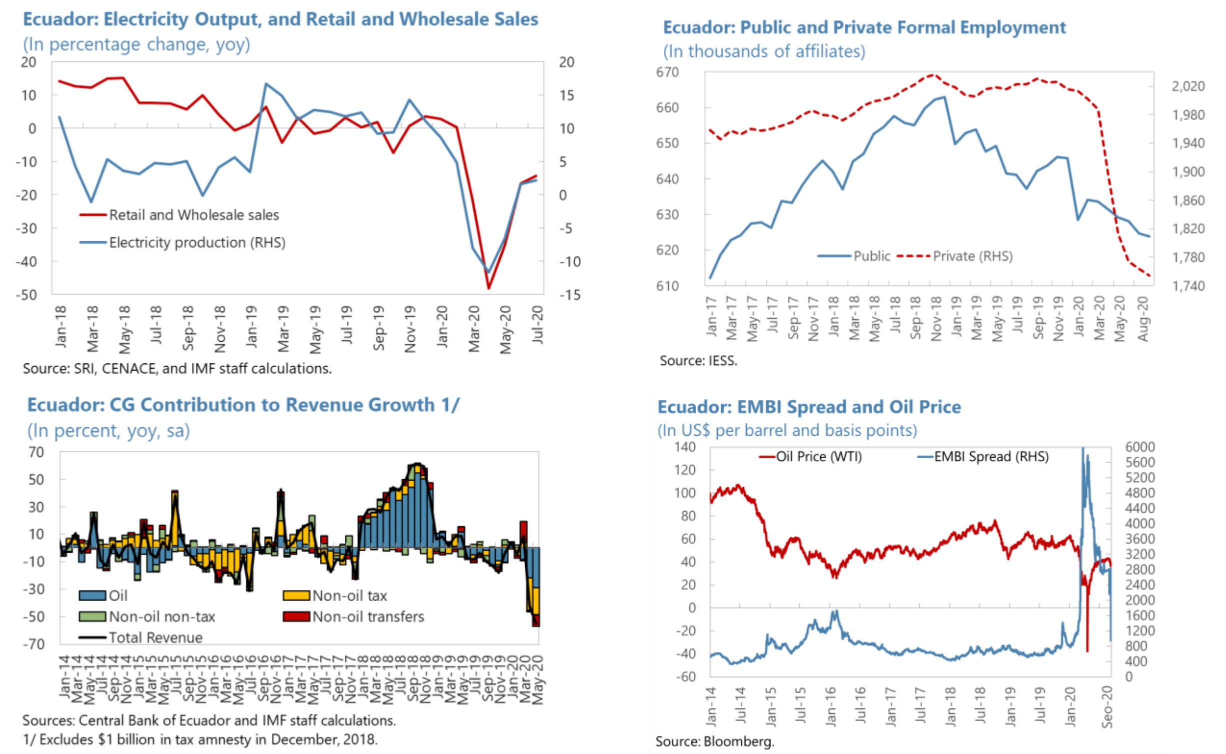
6. Facing difficult choices, the Ecuadorian authorities have remained committed to reforms and corrective actions in the face of the deep economic and health crisis. The authorities have reprioritized expenditure during the pandemic, redirecting much-needed resources into health and social spending. The amendments to the organic budget code (COPLAFIP) that had not passed the previous year were resubmitted and adopted, albeit with presidential intervention. The authorities took advantage of lower oil prices to implement an ambitious fuel subsidy reform to reprioritize spending, which will help domestic fuel prices gradually converge to international levels. They have also implemented corrective actions to address key weaknesses that had led to the issue of the misreporting, and made further progress in improving the institutional frameworks, with tangible improvements already materializing.

7. To help restore macroeconomic stability and pursue the unfinished reform agenda, the Ecuadorian authorities have requested a new 27-month EFF with exceptional access. The new EFF request (about $6.5 billion, SDR 4.615 billion or 661 percent of quota) will be anchored on two main objectives: first, mitigating the crisis by protecting the lives and livelihoods of the population and restoring macroeconomic stability; and second, as the economy recovers, ensuring the sustainability of public finances and strengthening domestic institutions to lay the foundations for strong, job-rich and long-lasting growth that benefits all Ecuadorians. Given the exceptional balance of payments needs, the proposed access level is above the normal access limit and subject to the exceptional access criteria (Box 1).

8. There are significant risks to the new Fund-supported program. Weaknesses in institutional capacity and a fragmented political landscape ahead of the elections in February 2021 pose a challenging environment for reforms. Successful implementation of the policies supported by the program will hinge on the buy-in and political will of the next administration and legislators in the National Assembly. With program policies being fully implemented, baseline macroeconomic projections materializing, and other creditors having provided the needed assurances, Ecuador's debt is sustainable with high probability and its capacity to repay is deemed adequate. However, there is little room for deviations, and slippages could severely strain Ecuador's capacity to repay, including through delayed capital market re-access. With policy levers being limited to fiscal policy in dollarized economies, any downside shocks such as a loss of confidence, a drop in oil prices, or shortfalls in financing would put an additional burden on fiscal policy to adjust.

BACKGROUND AND RECENT DEVELOPMENTS

Ecuador: High Frequency Indicators



9. The decline in oil prices, coupled with the damage to the oil pipelines have significantly dented export and fiscal revenues. In April, a landslide damaged two large crude oil distribution pipelines, disrupting production for about 5 weeks and resulting in a loss of about 14 million barrels. Concurrently, Ecuador mix oil prices plunged in 2020:Q2, touching US$27. These have dealt a heavy blow to export and fiscal revenues, with the former collapsing more than 45 percent (about US$600 million) between 2020:Q1 and 2020:Q2.

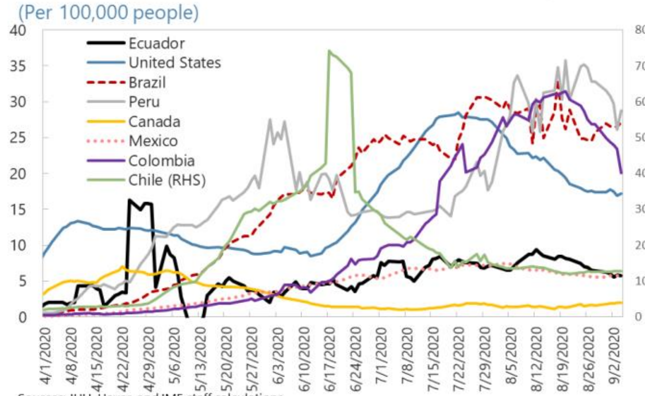
10. High frequency indicators point to a sharp decline in real activity, employment and fiscal revenues. Following an already weak Q4 of 2019, the economy suffered large losses in the wake of the COVID-19 crisis, with real GDP dropping by 2.4 percent (y-o-y) in 2020:Q1. The contraction in Q2 was likely sharper still, with the economic activity index plunging by about 35 percent (y-o-y) in April, to recover only to -15½ percent in June. Inflation edged up to 1 percent (y-o-y) in April/May reflecting food prices increases but retreated to -0.8 percent in August, driven by easing food inflation and declining transportation prices. The crisis led to massive private sector job losses (over 200,000 between March and June), pushing the unemployment rate to over 13 percent in June, from 3.8 at end-December 2019. Despite an appreciation of the US dollar, the current account registered a modest surplus of roughly $0.4 billion in 2020:Q1 mainly due to a sharp compression of imports that offset the decline in oil exports. The fiscal position improved in 2020:Q1, recording a surplus of about US$500 million at the NFPS level. However, it deteriorated significantly in Q2, reaching a deficit of about US$2.1 billion, on the back of lower tax revenues, COVID-related spending and social security contributions, resulting in the central government accumulating large domestic payment arrears, largely to other public entities.

11. The financial system appears to be stabilizing after a period of stress. Deposits in the banking system contracted by 2.8 percent at the onset of the Covid-19 crisis in March and credit growth declined sharply. A drain on the cash-in-vault of the central bank amid increased demand for cash tapered off since June. Bank capitalization and portfolio quality reportedly remain adequate and liquidity buffers have recovered, partly due to a significant drop in the credit demand.

12. After rising sharply in the wake of the crisis, the EMBI spread is normalizing, following the successful bond exchange and sovereign upgrades. With the tightening of global financing conditions in the wake of the COVID-19 pandemic, the EMBI spread, which was already elevated before the crisis, rose sharply to nearly 6000 bps. It has dropped below 1,000 bps following the rebound in oil prices and the successful completion of the market-friendly debt exchange of $17.4 billion in global bonds (¶18). S&P and Fitch recently upgraded Ecuador's sovereign credit rating from selective/restrictive default to "B-", on the back of the successful debt exchange and the staff-level agreement on the new EFF. Gross international reserves stood at about $3.2 billion at end-August, propped up by IFIs disbursements over the past few months, but NIR remains deeply negative.

13. Notwithstanding limited policy options, the authorities took decisive policy actions to mitigate the socio-economic impact of the pandemic on households and firms. The early containment measures focused on limiting the spread of the virus by closing the borders, public spaces and non-critical commercial activities, and imposing a nationwide curfew. These measures seem to have stabilized the pandemic outbreak, as the spread of the virus has slowed lately compared to other countries in the region (chart). Policy measures to protect lives and livelihoods amounting to $1.2 billion in 2020 included exceptional cash transfers to poor families ($250 million), distribution of food baskets, temporary relaxation of eligibility criteria for unemployment insurance ($372 million), and additional spending on health ($550 million). These measures were supplemented with a deferral of payroll contributions, tuition, health insurance, utilities, and housing support as well as temporary price controls for basic food items. Measures to support employment included the possibility of mutually agreed changes in labor contracts and introduction of shorter work week and more flexible work arrangements on a temporary basis.

Ecuador and Selected Economies: New COVID-19 Cases 1/
(Per 100,000 people)



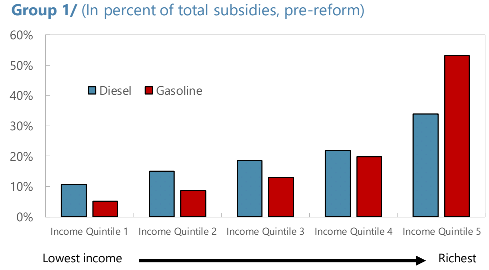
Sources: JHU, Haver, and IMF staff calculations.
1/ Calculated as the 5-day moving average of the difference between time t and time t-1.

14. Additional measures focused on supporting private credit and liquidity in the financial system. To address liquidity concerns in the financial system, the authorities reduced the banks' contribution rate to the Liquidity Fund by three percentage points of deposits (to 5 percent), freeing up about $950 million in liquid assets. This measure helped rebalance internal liquidity while the demand for cash also slowed gradually. In addition, they introduced an extraordinary deferral of private credit obligations on a voluntary basis (recently extended), mandated the revision of ceilings on interest rates, and introduced a working capital facility (*Reactivate Ecuador*) for enterprises partly financed by the World Bank. While the deferment measures will help support the real economy, if maintained for a prolonged period, they could weaken balance sheets of the financial institutions and represent downside risks for the financial system, especially during the transition to the *post*-emergency period.

15. Given limited options amid increased COVID-related spending and revenue shortfalls, the government also implemented fiscal measures to limit the impact of the crisis on the fiscal balances. From the onset of the crisis, the government proactively took measures to rationalize spending, which kept the deficit in Q2 under control. The measures (annual yield of $2.4 billion) included a sharp reduction in capital spending; temporary reduction in the number of working hours of public sector employees (excluding in critical sectors such as health, police, and the armed forces), with a corresponding reduction in the public sector wage bill; closure of selected SOEs and embassies; and cuts in goods and services spending.

16. To reduce economic distortions generated by fuel subsidies, the authorities reformed gasoline and diesel subsidies, which is expected to generate long-lasting fiscal savings and reduce inequality by reallocating government resources to lower income households. Gasoline and diesel subsidies involve high fiscal costs, accrue mostly to higher income households, given their higher consumption of fuel products and lead to large economic distortions – fuel subsidies can (i) magnify the macroeconomic and fiscal impact of volatile international prices; (ii) result in excessive environmental costs; and (iii) lead to illegal and disruptive cross-country smuggling. Aiming to reduce these economic distortions, the authorities introduced a gasoline and diesel subsidy reform in May 2020. The reform introduced a formula-based pricing mechanism for diesel and gasoline that links domestic retail prices to supply costs where monthly changes are capped to prevent large swings in retail prices. The subsidy reform is expected to generate long-lasting fiscal savings—part of which will be used to compensate low-income households for fuel price increases—and encourage more efficient energy use. The reduction of regressive subsidies (chart) will also allow the government to allocate more resources to strengthening the social safety nets, consistent with Ecuador's inclusive growth agenda.

Ecuador: Beneficiaries of Diesel and Gasoline Subsidies by Income Group 1/ (In percent of total subsidies, pre-reform)



Source: Schaffitzel et al (2019) "Can government transfers make energy subsidy reform socially acceptable? A case study on Ecuador. IDB Working Paper Series N ° IDB-WP-01026, and Staff calculations.
1/Average monthly income per-capita, in US$, is as follows: Quintile 1, $49.3; Quintile 2, $100.9; Quintile 3, $154.9; Quintile 4, $238.4; and Quintile 5, $591.8 (ENEMDU, 2018).

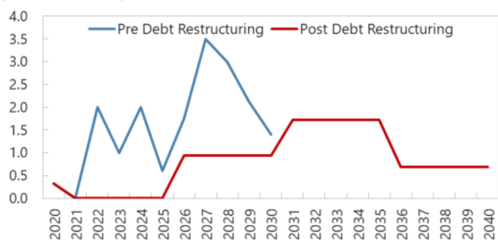
17. The recently amended organic budget code provides a strong anchor for public financial management. COPLAFIP, which was adopted in July 2020, was a key commitment under the government's previous EFF arrangement and constitutes a significant improvement over the previous legislation. It enshrines in legislation a public debt anchor of 40 percent of GDP to be achieved by 2032, with intermediate debt limits of 57 and 45 percent of GDP to be reached by 2025 and 2030, respectively—parameters consistent with ensuring public debt sustainability. The law establishes operational fiscal rules (central government level) to guide fiscal policy towards achieving the debt target of the nonfinancial public sector (NFPS) and includes other provisions for strengthening public financial management and reducing discretionary budget spending.

18. Foreseeing rising debt vulnerabilities, the authorities proactively restructured their global bonds in a market-friendly operation with very high participation. The authorities have successfully completed a bond exchange with the support of 98 percent of bondholders holding $17.4 billion of Ecuador's global bonds. The parameters of the operation were structured around the debt sustainability targets provided in the RFI, which were to reach a debt-to-GDP ratio of 55 and 45 percent in 2025 and 2030, respectively, and average gross financing needs of 6 percent over 2025-30. The new bonds extend the average maturity of Ecuador's external bonds by 10 years, to 2040, carry coupons with rates about half that of the old bonds and, importantly, begin principal amortization in 2026, providing ample liquidity relief in the next 5 years.[1]

Ecuador—Global Bonds Repayment Profile: Debt Restructuring Offer

Ecuador: Principal Payments

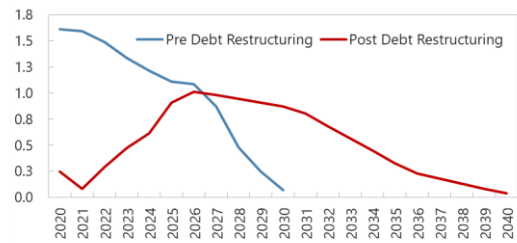
(In US$ billions)



Source: Ministry of Economy and Finance.

Ecuador: Interest Payments

(In US$ billions)



Source: Ministry of Economy and Finance.

OUTLOOK, AND RISKS

19. Economic activity is projected to contract by a record level in 2020, with only gradual recovery over the medium term. A collapse in real activity due to the containment measures (-8.2 ppts), drop in oil prices (-2 ppts), and damages to crude oil pipelines (-0.8 ppts), would drag the economy down by 11 percentage points this year, pushing many people into poverty. The projected recovery in 2021 is predicated on the positive base effect and further improvement in activity, in line with the outlook for the region and peer countries, as the pandemic continues to wane. In this regard, the Covax Facility that Ecuador has recently joined will help ensure the country gains access to the supply of vaccines if/when they become available. Over the medium term, growth is expected to revert gradually to its potential of 2½ percent, reflecting the impact of structural reforms planned during the program period in improving competitiveness and enabling a greater participation of the

[1] Using collective action clauses, the payment terms in the existing bonds held by non-consenting bondholders were amended to match the longest-dated exchange bond.

private sector in economic activity. Real GDP is, however, expected to return to its 2019:Q4 level only by 2025:Q2.

20. Inflation is projected to remain subdued. Staff expects inflation to average zero in 2020 as supply-side factors due to the lockdown are expected to be offset by the very weak aggregate demand and high unemployment. Inflation is forecasted to rise to 1 percent in 2021 as fuel prices increase to align with international prices, then remain low (1 percent in the medium term), helping to gradually restore competitiveness.

21. Asset quality is likely to deteriorate in the coming months. Once the crisis-related measures are rolled back and payment deferrals are lifted, NPLs will likely rise from the currently low 2.7 percent of total loans. Loan performance could further deteriorate due to longer-lasting disruptions in the chain of payments and as the economic slowdown impairs borrowers' credit service ability. In anticipation, private banks' provisioning coverage (generic and specific) has increased significantly (278 percent of reported NPLs at end-July). Non-banks and public banks have comparatively higher NPLs (4.3 and 8.1 percent, respectively) and also high provisioning coverage ratios. In addition, while liquidity is now higher than in the pre-crisis period (30 percent in liquid assets to short-term liabilities), system-wide deposits need to be monitored carefully (¶34).

22. The current account balance is projected to turn into a deficit in 2020 but is expected to recover over the medium term. The collapse in oil prices coupled with domestic disruptions in oil production due to the pipeline damages, is expected to cut oil export receipts in 2020 by half. The impact of the pandemic will also be felt in lower tourism-related income (by more than 30 percent, compared to 2019), and subdued worker's remittances (27 percent decline). The decline in goods and services exports is projected to be partly offset by the sharp import compression (by 19 percent) on the back of weak demand. As a result, the current account is expected to post a deficit of about 2 percent of GDP from a near-balanced position in 2019. In the medium term, the current account is expected to strengthen to 0.7 percentage points of GDP, supported by a partial recovery in global oil prices and internal devaluation. The growing role of the private sector as the economy strengthens and regains the confidence of investors, and higher private inflows—both FDI and portfolio flows—would contribute to reserves being built back up over the medium term.

23. Ecuador's external position is judged to be weaker than the level consistent with medium-term fundamentals and desirable policies (Annex V). The REER is judged to be overvalued by about 30 percent. Given dollarization, the limited scope for gains in price competitiveness calls for fiscal prudence as well as enhancing the business environment to attract foreign direct investment and promote medium-term growth.

24. The macroeconomic outlook is subject to considerable uncertainty and significant downside risks:

- Key near-term risks include a more severe and/or protracted COVID-19 pandemic, which could result in higher fiscal cost; a more protracted recovery of the domestic or global economy, which could lead to a more pronounced decline in fiscal revenues, delays in private sector recovery, and the intensification of domestic financial sector vulnerabilities; further collapses and/or volatility in oil prices, which could be accompanied by bouts of international financial volatility as the pace of global demand recovery remains uneven and asynchronous with a further sharp rise in risk premia that exposes financial vulnerabilities and might generate additional pressures on public and private finances. Importantly, the reemergence of social tensions, policy slippages, and a lack of political cohesion and social consensus in pursuing much-needed structural reforms could also undermine the outlook. Given that the burden of adjustment in dollarized economies falls on fiscal policy, downside risks materializing would likely require a greater fiscal effort to meet the debt targets enshrined in COPLAFIP and needed to secure debt sustainability. Long-term scarring from the crisis, the risks of increased protectionism and longer-term structural de-globalization can hurt longer-term growth prospects.

- On the flip side, a faster recovery of the global economy, trading partners, and oil prices, as well as an improved environment for asset monetization and a more depreciated US dollar, pose upside risks. Additional upside risks to growth stem from a more ambitious plan of structural reforms of the next government that could boost Ecuador’s productive capacity, including labor market reforms that improve competitiveness and promote private sector development and job creation.

OBJECTIVES AND POLICIES UNDER AN EXTENDED FUND FACILITY

25. The government is keen to pursue the structural reform agenda initiated under the previous EFF arrangement, advance it in key areas and leave the next administration with a well-managed economy and a stronger Ecuador. Consistent with the authorities’ homegrown *Plan de Prosperidad*, the EFF-supported program will aim to: first, mitigate the crisis by protecting the lives and livelihoods of the population and restoring macroeconomic stability; and second, as the economy recovers, ensure the sustainability of public finances and strengthen domestic institutions, including the foundation for dollarization, for strong, job-rich, and long-lasting growth that benefits all Ecuadorians. Improving transparency, governance and data quality and timeliness, will be key objectives that will be pursued throughout.

A. Expanding the Social Safety Net

26. An overarching and immediate priority of the program is to extend lifelines to households while increasing coverage of social assistance programs over time (Annex II). UNICEF estimates that the poverty rate would increase by 10 percentage points in 2020, pushing an additional 1.8 million persons into poverty. The authorities provided temporary social assistance support to vulnerable households during the COVID-19 outbreak. They are working with the World Bank on a strategy to strengthen the social safety net with a goal to more than double the coverage of low-income beneficiaries of cash transfers (from 37 percent of families in the bottom three deciles of the income distribution to 80 percent) by December 16, 2021 *(structural benchmark,* MEFP ¶4*)*.

This strategy envisages the gradual expansion of social assistance benefits (mostly through the conditional cash transfers program *Bono de Desarrollo Humano*) to 225,000 and 400,000 new beneficiary families in 2020 and 2021, respectively. The additional cumulative cost for expanding coverage is estimated at about $650 million between 2020 and 2022. This will be partly financed by gradually excluding non-poor families that currently receive social assistance benefits, which should yield cumulative savings of around $130 between 2021 and 2022, and also by the savings from the subsidy reform (¶16). A successful implementation of this initiative requires further political commitment, to facilitate and monitor the update of the information in the Social Registry in order to identify families below the poverty line. The authorities are implementing measures to monitor the progress in updating the social registry and expanding coverage.

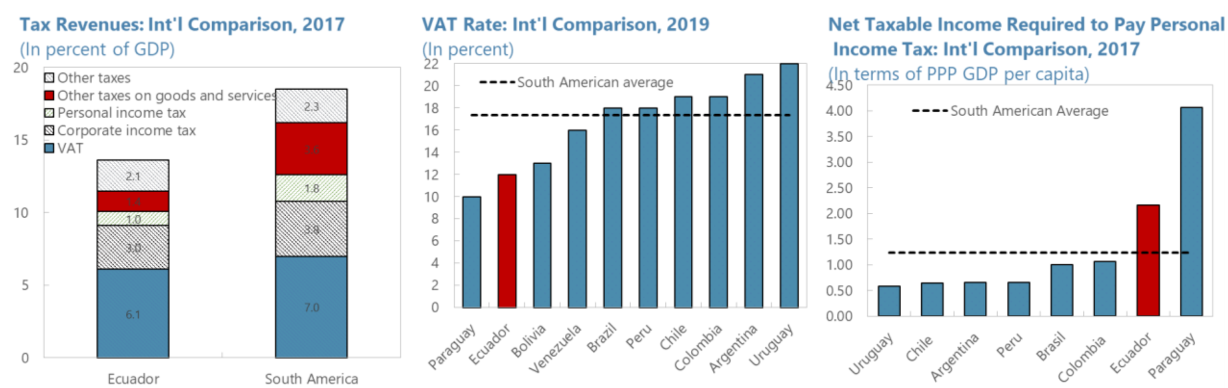
B. Restoring Fiscal Sustainability While Supporting the Population

27. The crisis this year justifies a higher fiscal deficit to accommodate the higher health and social assistance spending as well as the revenue shortfall. Revenues are expected to fall dramatically in 2020 compared to 2019, by $8 billion, due to lower oil prices and weaker economic activity. On the spending side, lower oil prices are expected to generate savings on imports of oil byproducts by $1.4 billion. The expenditure cuts that were implemented in Q2, of $2.4 billion annual savings (¶13) create the space for supporting vulnerable households and the health sector amid the Covid-19 pandemic (about $800 million) and expanding social security benefits (about $300 million). Taken together, these changes would result in the higher fiscal deficit reaching $8.3 billion in 2020, around $5 billion higher compared to 2019. The overall balance is expected to deteriorate by 5.7 ppt of GDP from the previous year.

Ecuador: Change in the Overall Fiscal Balance in 2020 (in million, $US)

	Change 2020-19
Revenues	**-7,908**
Oil Revenues	-3,247
Non-oil Revenues	-4,014
o.w. Tax Revenues	-2,610
Operating Surplus of SOEs	-647
Expenditures	**-3,011**
Current (excl. Covid-related spending)	-2,428
o.w. Wages and Salaries	-751
Goods and Services (excl. Covid-related spending)	-150
CFDD +SH	-1,594
Capital	-1,317
Interest Payments	-46
Extrabudgetary Expenses	-20
Covid-related spending	800
Overall Balance	**-4,898**

Ecuador and Latin America: Tax Revenues



Sources: WEO, OECD, IBFD, county tax law, and IMF staff calculations.

28. An ambitious, yet realistic path towards the sustainability of public finances will need to begin once the pandemic abates in 2021 and crisis-related measures are unwound.

- The largest mechanical improvements in the 2021 fiscal balance would come from the significantly lower interest payments following the successful bond restructuring operation (lower interest payments on debt), higher oil revenues owing to higher domestic sales prices, and from the improvement in economic activity bringing in higher tax revenues under existing policies. This would be supported by a rolling back of $800 million in COVID-related spending once the crisis subsides and from rationalizing capital expenditures and reducing spending on goods and services. These savings would create room for higher social spending in 2021, and still allow for an improvement in the overall balance of $5.4 billion (6 ppt of GDP) compared with 2020.

- More broadly, the program would target fiscal consolidation of 5.5 ppt of GDP of the overall NFPS balance over 2019-25 (about 5.5 ppt improvement in the non-oil primary balance including fuel subsidies), with the main goal of achieving public debt sustainability as now reflected in the debt targets enshrined in legislation by the recently adopted organic budget code (COPLAFIP). This consolidation, together with a restructuring of external bonds and financial support from bilateral and multilateral creditors will help restore sustainability by placing public debt firmly on a declining path. While ambitious, the size of the envisaged fiscal consolidation is realistic, considering Ecuador's historical performance in response to public debt increases (Annex III). The negative impact of fiscal consolidation on growth will need to be weighed against the confidence gains from the significant upfront improvements in the profile of public debt and near-term steps to strengthen domestic institutions, anchored by the authorities' reform program supported by the new EFF arrangement. Moreover, the ongoing expansion of social assistance programs to cover a higher share of poor families will allow the government to readily reach the most vulnerable segments of the populations and compensate them for the negative impact of fiscal measures (¶26).

Ecuador: Improvements in the Overall Fiscal Balance in 2021
(in million, $US)

	Change 2021-20
Revenues	**3,390**
Oil Revenues	1,025
Non-oil Revenues	1,723
o.w. Tax Revenues	1,040
Operating Surplus of SOEs	643
Expenditures	**-2,005**
Current	-13
o.w. Wages and Salaries	97
Goods and Services	-716
Other (incl. Social Spending)	638
Capital	-662
Interest Payments	-1,303
Extrabudgetary Expenses	-27
Overall Balance	**5,396**

29. Fiscal consolidation is envisaged to include both revenue and expenditure measures. The package is envisaged to include permanent measures balancing revenue increases (2½ ppts of GDP) and expenditure restraint (2.9 ppts of GDP), while protecting lower income families:

- *Growth-friendly tax reform* (*end-September 2021 structural benchmark*). Tax revenues in Ecuador remain low by regional standards, owing to low tax rates, a relatively small base, high personal allowances, complexity, and weak enforcement. Hence, an ambitious, smart and progressive tax reform, including a growth-friendly VAT reform, a reform of the PIT focused on the higher end of the income distribution, and the CIT reform geared towards base-broadening with the revenue gains starting to accrue in 2022 would be appropriate. These measures can generate a permanent yield of over 2½ ppt of GDP (text table). The VAT reform is expected to be progressive, having a smaller effect on lower-income households because a large fraction of the goods consumed by these households will remain exempt from VAT. The tax package will be complemented by measures to reduce compliance risk, including by creating a full-fledged Large Taxpayer Office (LTO) responsible for all tax administration functions.

- *Wage bill rationalization.* Ecuador's wage bill is above the average for Latin America, owing to large increases over the past decade (text chart). Reducing it would not only safeguard public finances but also help strengthen Ecuador's competitiveness. Overall, the wage bill rationalization would comprise a mix of employment reduction and lower salaries. In this regard, the authorities have extended the recent temporary reduction in working hours and employment through May 2021, with due account to public service delivery in critical sectors, including health, primary and secondary education, police and the armed forces. Medium-term measures would include continued wage cuts for new hires, hiring and promotion freezes, attrition (with a one for two replacement rate), and further employment rationalization in non-critical sectors.

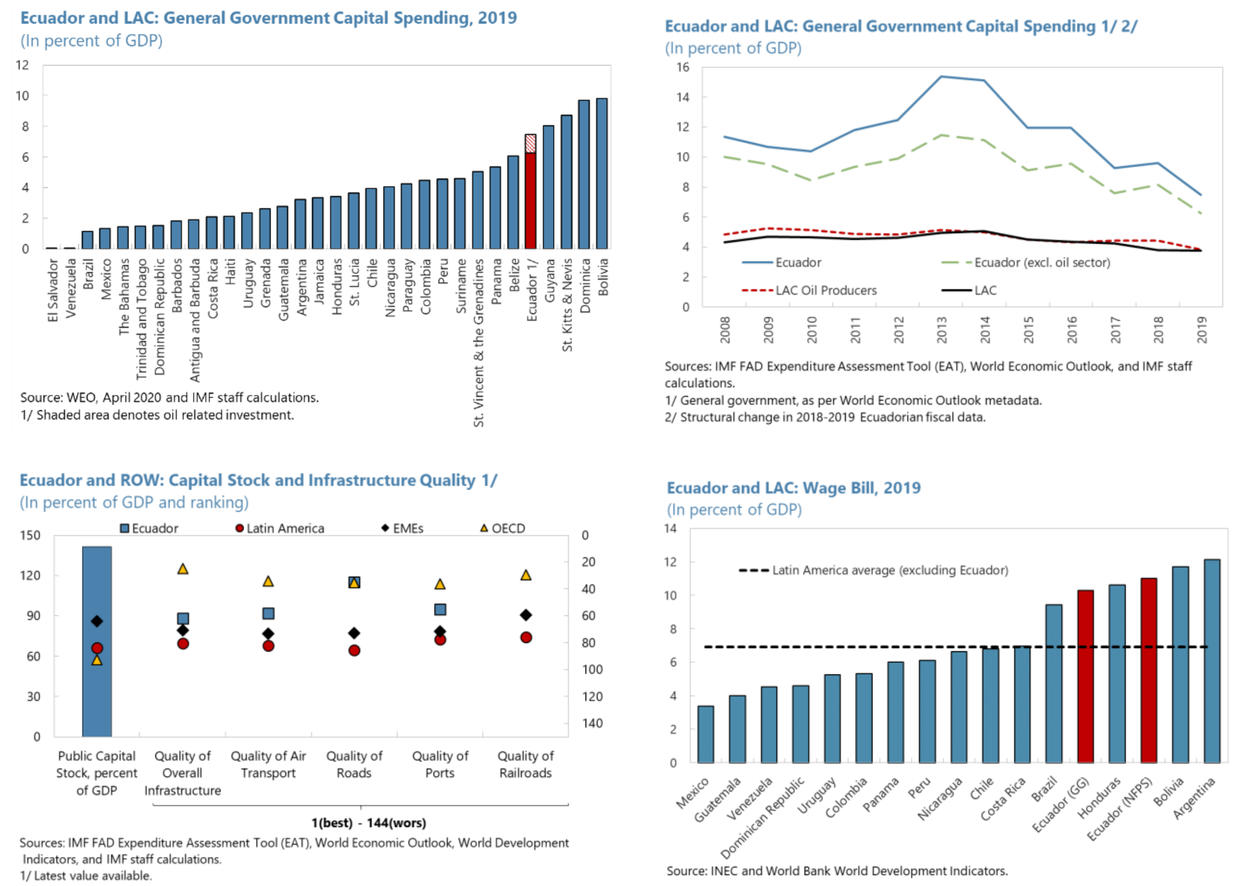
Ecuador: Tax Policy Measures and Estimated Yields (in percent of GDP)

	Estimated Yields
1. VAT	**1.38**
3 percentage point increase in VAT rate (from current 12 percent)	1.25
Reduction in VAT exemptions for the universities	0.02
Eliminate VAT refund to the elderly	0.11
2. Personal Income Tax	**0.65**
Inclusion of the 13th and 14th salaries in PIT base	0.09
Modification to the PIT brackets to increase progressivity	0.14
VAT creditable against PIT	0.40
Eliminate the reduced CIT rate for productive assets	0.02
3. Corporate Income Tax	**0.10**
Introduction of accelerated depreciation.	-0.20
Outflow tax creditable against the CIT	0.30
4. Others	**0.39**
Excise tax on gasoline	0.04
Expand base of the telecommunications tax	0.10
Introduction of an environmental tax on CO2 emissions	0.25
Total revenue increase	**2.52**

Source: Ministry of Finance and IMF staff calculations.

- *Improved public procurement for goods and services.* The program envisages savings in expenditure on goods and services of 0.7 percent of GDP by 2025, to be partly generated through improved procurement practices, including through increasing competitive procedures, consolidating procurement where economies of scale exist, and improving electronic procurement. The related fiscal savings built into the projections are more conservative than the findings in a recent micro-based study by the World Bank suggesting that higher fiscal savings are achievable without legislative changes.

Ecuador and LAC: Capital Spending, Infrastructure Quality, and Wage Bill



- *Rebalancing spending from fuel subsidies to social assistance*. The landmark subsidy reform, marked by the introduction of an automatic fuel pricing mechanism, is expected to generate long lasting fiscal savings, totaling almost $3 billion between 2020 and 2025 compared to a no-reform scenario under current oil price projections. Part of those fiscal savings (about 0.9 percent of GDP) will finance higher priority public spending, including the increase in social spending as the coverage of poor families improves under social programs. The expansion of coverage will allow the government to compensate families in need from the planned consolidation measures and higher fuel prices under the smoothing mechanism. A sound communication campaign around the underpinnings and benefits of the mechanism for the broader Ecuadorian society would be extremely important to ensure its sustainability.

- *Moderation in capital spending*. Reflecting Ecuador's still relatively high levels of public investment, with an already robust public capital stock (text chart), the program envisages prioritizing capital spending over the coming years towards projects that generate more growth and create jobs. Such efforts would save about 2.1 ppt of GDP over 5 years, while protecting investment in the oil sector, given the associated revenue and export receipts.

Select NFPS Fiscal Balances

(Change from previous year, in percent of GDP)

	2020	2021	2022	2023	2024	2025	2020-2025
Revenue	**-0.6**	**0.3**	**2.2**	**0.6**	**0.1**	**0.0**	**2.6**
Planned tax reform	0.4	0.0	2.0	0.6	0.0	0.0	3.0
Macroeconomic effect on tax revenues	-1.3	0.6	0.2	0.1	0.1	0.0	-0.4
Change in the prepayment of the income tax	0.3	-0.3	0.0	0.0	0.0	0.0	0.0
Expenditure (the negative sign represents an increase in spending)	**-1.9**	**3.0**	**0.8**	**0.8**	**0.2**	**0.0**	**2.9**
Wages and salaries	-0.7	0.5	0.3	0.2	0.1	0.1	0.6
Goods and services (exl. Covid-19 related spending)	-0.6	0.6	0.6	0.1	0.1	0.0	0.7
Goods and services - Covid-19 related health spending	-0.5	0.5	0.0	0.0	0.0	0.0	0.0
Other spending	-0.9	0.2	0.0	0.0	0.0	0.0	-0.7
Capital spending	0.2	1.3	0.2	0.4	0.1	0.0	2.1
Fuel subsidies	1.1	0.1	-0.1	0.0	0.0	0.0	1.1
Social spending	-0.5	-0.3	-0.2	0.1	0.0	0.0	-0.9
Total	**-2.6**	**3.3**	**3.0**	**1.4**	**0.3**	**0.0**	**5.5**

Sources: Ministry of Finance and IMF staff calculations.

C. Strengthening Fiscal Frameworks, Governance, and Transparency

30. Building on achievements and weaknesses identified in the previous EFF arrangement, the reforms will seek to improve public financial management practices, including transparency in management of public funds. The institutional and capacity weaknesses identified in the previous EFF arrangement have been partially addressed as part of corrective actions for misreporting. Further actions have been undertaken to strengthen effective and efficient management of public resources and to ensure better program performance and monitoring, but more needs to be done. In particular:

- operationalizing the organic budget code is a priority: a regulation (through a ministerial agreement) to report the data for the subsectors of the NFPS was adopted (*prior action*), to be followed by the adoption of the regulation to implement other July 2020 amendments to COPLAFIP (*structural benchmark for end-November, 2020*). To improve its effectiveness, the latter regulation should take the form of an executive decree, encompassing the earlier ministerial agreement on data provision. To complement these amendments, it would be important to strengthen the capacity to review and analyze fiscal data (last bullet), oversee NFPS operations, and identify and mitigate risks;

- improving cash and debt management: a financial plan was prepared and approved by the MEF Financial Committee for the budgetary central government for the remainder of the year (*prior action*), that improves the visibility on budget execution and financing for the months ahead; a similar plan for 2021 will be prepared (*structural benchmark for December 16, 2020*); and publishing a medium-term debt management strategy that includes operations in 2021, and which targets debt service for at least 2022 (*structural benchmark for end-February, 2021*);

- evaluating the existing stock of domestic payment arrears for the central government and selected relevant entities of the NFPS, and putting in place a framework to monitor and prevent further accumulation of arrears (*structural benchmark for end-April, 2021*). Meanwhile, as additional financing becomes available, the authorities will finalize an adequate plan to prioritize the clearance of properly verified outstanding payments accumulated during the pandemic, and to ensure transparency in the process.

- increasing efficiency of public spending, including through the procurement reform developed with the World Bank, enacting regulation mandating the publication of all public procurement contracts and the names of the awarded entities and their beneficial owner(s) (*prior action*), as well as improving fiscal transparency. Staff encouraged the authorities to work with the World Bank to revise the recent procurement decree for purchases in the health sector to improve its transparency and effectiveness.

- assigning staff from the Ministry of Economy and Finance (MEF) to work with technical assistance missions and experts assigned to Ecuador, including the long-term expert (LTX) in public financial management and the short-term expert (STX) in public finance statistics and the medium-term debt management strategy, in order to build and retain technical capacity. The work of the STX and LTX will need to be coordinated with other government agencies and supported by the BCE.

31. Transparency in public debt is integral to sound public financial management. The authorities have been publishing sovereign debt contracts as legally permissible and are committed to continue promoting transparency in all debt contracts going forward, drawing on World Bank's technical support. Such information would allow for a better comparison of cost of funds and candid assessment of risk trade-offs across sovereign debt instruments, guiding the management of the sovereign debt portfolio.

D. Strengthening the Central Bank Institutional Framework

32. Lasting institutional reform of the central bank is needed to strengthen dollarization. The BCE's balance sheet is protected by regulatory requirements implemented under the previous EFF arrangement precluding new central bank financing to the government. However, the failure to pass amendments to the monetary and financial code (COMYF) in late 2019 left the BCE with several unresolved issues, including: lack of independence and a clear mandate; weak governance; low coverage of financial sector deposits with liquid reserve assets; and no clearly defined role for the BCE in financial stability. The balance sheet of the BCE remains weakened by legacy assets. The authorities aim to have amendments to COMYF adopted by the National Assembly by end-January 2021 (*structural benchmark,* MEFP ¶16). In the meantime, to strengthen the institutional framework of the central bank, the Monetary Policy and Regulatory Board (JPRF) has adopted a resolution on the BCE external auditor selection and rotation policy (*prior action*, MEFP ¶17). The resolution incorporates best practices recommended by the 2019 safeguards assessment and will allow the BCE to develop the terms of reference for external auditor selection. The JPRF has also established an audit committee (*prior action*, MEFP ¶17). The audit committee will prepare a charter to align the BCE's internal audit with best international practices, ensure the independence of the BCE audit function, and expand its coverage to all BCE operations (*structural benchmark for end-November 2020*). The authorities plan to begin technical work on amendments to COMYF to reform the banking law to align it with international standards, with technical assistance from the Fund.

E. Safeguarding Financial Stability

33. The measures to alleviate liquidity constraints have helped stabilize the system but should be rolled-back as the crisis subsides. While the reduction in the rate of contribution to the liquidity fund provided timely support to the financial system in the wake of the crisis, the integrity of the liquidity fund should be preserved going forward. Further reductions in the contribution rate of financial institutions to the liquidity fund in the absence of systemic liquidity stress would undermine the fund's ability to provide the support it was designed for if ever needed. Preserving its risk pooling feature, including by providing temporary support to illiquid but solvent entities, through loans rather than lower contributions, would be important in this regard.

34. Further efforts are needed to strengthen crisis preparedness and management. Thus far, NPLs remain subdued and sufficiently covered with provisions, but to the extent the recovery is slow and uneven, a significant portion of the credits subject to deferrals may quickly turn into NPLs. Stress tests performed by the superintendency of banks suggest that existing capital buffers would mitigate the shock but liquidity support could be needed, including medium term funding; such funding will need to be identified. In addition, the resolution tools at the disposal of the superintendency are limited and will need to be upgraded. The authorities need to establish contingent arrangements in light of COVID-related uncertainties, though a more definitive solution will only be possible via reforming the Organic Code (COMYF). The Fund is providing technical assistance to develop stress-testing capabilities of the superintendency of banks, while the World Bank continues to work with the authorities on the medium to long term issues to improve financial intermediation. Staff will work with regulators to ensure that loan portfolios subject to payment deferral continue to be reported transparently.

35. Close coordination among financial sector agencies is essential to prepare for and combat future crises effectively. The authorities plan to establish a financial sector coordination committee comprising the Monetary Policy and Regulatory Board, Central Bank, Ministry of Economy and Finance, Superintendencies, and the deposit insurance, which will help strengthen the collaboration between the institutions in order to preserve financial stability and develop longer term plans for financial deepening (MEFP ¶21). Pooling institutional resources will allow analyzing problems comprehensively. A strong communications strategy is also needed to speak about important financial sector decisions in one voice.

F. Strengthening Competitiveness and Growth

36. Strengthening the legal framework for state-owned enterprises will help improve efficiency of public sector operations, increase productivity and encourage private sector development. The authorities are revamping a law for state-owned enterprises (SOEs) with assistance from the IADB. The law will seek to improve efficiency, increase transparency, and strengthen governance of SOEs. It aims at bringing SOEs to the same standards as private companies by requiring them to pay taxes at the same rate as private firms, complying with the same labor regulations, and adopting the same accounting standards. Regarding the latter, the law will eliminate one of the obstacles to the preparation of the audited financial statements by allowing SOEs to hire their own external auditors. The reforms to the SOE framework will need to be aligned with the recently approved COPLAFIP.

37. Improving the business climate and strengthening the rule of law would reduce the trust gap between Ecuadorians and public institutions, boost non-price competitiveness and foster private investment and job creation. Ecuador is below the LA6 average in global competitiveness indicators (90th out of 141 countries) (see Annex III).[2] Integral to improving the business environment and transparency is a stronger rule of law and enhanced governance and anticorruption frameworks. These would protect public finances, increase trust in public institutions, curb discretion, thereby limiting policy uncertainty and incentivizing private investment. In this regard, authorities have recently amended AML/CFT regulations to conduct enhanced customer due diligence when transacting with senior officials and PEPs (politically-exposed persons) in line with FATF standards. This was a pending commitment from the previous EFF. Consistent with the government's reform agenda started under the previous EFF arrangement, the new Fund-supported program envisages further reforms in governance and anticorruption (see Section C), including by adopting a regulation to enhance the online publication of asset declarations by high-level officials (*structural benchmark for end-November 2020*), adopting the previously submitted anticorruption legislation (*structural benchmark for end-December 2020*), and auditing COVID-related spending as committed under the RFI (*structural benchmark for end-June 2021*).

38. Ongoing initiatives to reduce labor market rigidity and align the minimum wage with productivity have the potential to improve resources allocation in the economy and enhance competitiveness. The authorities adopted several measures to reduce labor market rigidity as part of their policy response to the pandemic under the Humanitarian Law (*la ley humanitaria*). These included temporarily relaxing the eligibility criteria for unemployment insurance, the possibility for employers and employees to make mutually agreed changes to existing labor contracts, introducing shorter work weeks and more flexible work shifts arrangements. The Ministry of Labor estimates that 45,000 jobs were saved, and an additional 100,000 new ones created since the law was enacted in late June. The authorities are also working with the World Bank to anchor the minimum wage on macroeconomic factors such as inflation and productivity—the minimum wage is higher in Ecuador than in regional peers and has outpaced labor productivity in the past 5 years (Figure 5). Pending a comprehensive labor market reform over the medium-term, these measures, if consistently implemented in the coming years, can boost external competitiveness, improve resource allocation in the economy, and add to Ecuador's productive capacity.

39. Developing domestic capital markets would allow financial deepening and diversifying financing sources for the government and the private sector. The authorities are developing plans to deepen domestic capital markets. In particular, they are planning to standardize government securities, develop a yield curve, and lengthen maturities of government short-term

[2] The LA6 country group includes Argentina, Brazil, Chile, Colombia, Mexico, and Peru. Some of these indicators are perception-based.

instruments. Following up on Fund technical assistance recommendations, there is also scope to strengthen debt management by implementing a medium-term strategy to improve transparency and support lower cost financing, contribute to deepening domestic debt markets and reduce reliance on external funding. Other measures could include strengthening debt management office—particularly in the context of the reorganization of the Ministry of Economy and Finance, supplementing debt data publication with analytical assessment of debt portfolio and its risks and strengthening investor relations. These reforms can help increase the flow of resources from investors to corporations and to the government and eventually increase investment, productivity, and growth.

40. Advancing financial inclusion would expand opportunities for households and businesses and support inclusive growth. The authorities have designed, in collaboration with the World Bank, a strategy to promote financial inclusion by reducing the number of regulated interest rate segments, with implementation to start by end-January 2021. They intend to leverage the reduced reliance on cash by households and businesses during the pandemic, amid health concerns, to foster alternative modes of payments. Relying on alternative means of payment such as credit cards, online transfers, and online payment in e-commerce could bring operational efficiency to the BCE and the administration of government's cash transfer under social programs, help business grow and attract more investment, including from abroad, and increase financial inclusion.

PROGRAM MODALITIES

41. Access and phasing. The proposed access level is $6.5 billion (SDR4,615 million)—Ecuador's estimated residual financing needs in 2020–22—after factoring in a successful restructuring of external bonds, reprofiling of external bilateral debt, financing from IFIs and a medium-term fiscal consolidation path (Table 5). Fund financing would be made available to the budget. Access is proposed to be frontloaded, in line with the timing of the financing gaps (Table 9). Disbursements would initially be made through quarterly reviews in 2020, then move to a triannual cycle in 2021, when the fiscal QPC would be changed from central government to the NFPS balance, to allow more time for the effective monitoring of that QPC (see ¶42). Should additional financing become available this year, including from the World Bank and other creditors, authorities would not use it to raise the deficit but rather build deposits, to insure against downside risks to the outlook.

42. Quantitative conditionality (MEFP Table 1). Program performance would be monitored with a range of fiscal and quasi-fiscal targets to bring more transparency and accountability to fiscal policy. QPCs include: a floor on the overall balance of the central government until August 2021; a floor on the overall balance of the NFPS from August 2021 onwards; a floor on the accumulation of NFPS deposits at the central bank; non-accumulation of external payments arrears (continuous); and no net credit to government from the central bank (continuous). Indicative targets (ITs) include: a floor on the non-oil primary balance of the NFPS (including fuel subsidies) (NOPBS); a floor on the overall balance of the NFPS until August 2021; a floor on the net international reserves, and a floor on the coverage of the cash transfer programs for lower income households. The proposed targets aim to strike a balance between comprehensiveness, data timeliness and quality, and policy effectiveness/controllability:

- *Fiscal coverage.* While the previous EFF had a QPC on the NFPS balance, which directly maps to the debt anchor in the COPLAFIP, forecasting it in the absence of reliable and timely data on its subsectors—local governments, state owned enterprises (SOEs) and the social security fund—proved to be a vulnerability, evidenced by the misreporting case. Since then, source data has been corrected, but data lags remain long (and made worse temporarily by COVID-19) and requires cross-checking. That leaves little time within a quarter to observe progress towards the target and take corrective actions as needed. Therefore, the program would monitor the NFPS balance initially as an IT and make it a QPC starting with the August 2021 test date, until which time underlying data quality is expected to improve with support from an STX and Fund staff. In the meantime, having a QPC on the central government (CG) perimeter (budgetary central government and the account for financing the import of oil byproducts, CFDD) balances best the considerations above: (1) historical data have been corrected and monthly data are available as early as 20 working days; (2) the QPC on accumulation of NFPS deposits at the central bank (see below) would already reflect developments below-the-line for the broader spectrum of public entities, and if fiscal slippages were to occur above-the-line at the NFPS level, these would be seen in the IT on the NOPBS; and (3) NFPS entities outside the central government have contributed little to public debt, reflecting legal constraints on their borrowing.

- *Central bank reserves targets.* Because the Central Bank of Ecuador (BCE) has no policy levers to build reserves under the dollarization regime, any target on the BCE balance sheet is essentially a quasi-fiscal target (the BCE could adjust the required reserve ratio, but given the high levels of excess reserves, such a policy change would likely be ineffective, especially as a corrective action to meet quarterly targets). As such, NFPS deposits accumulation, controlled by public sector entities, is the main lever for affecting international reserves. Against that background, the QPC would be set directly on the accumulation of NFPS cash deposits at the BCE. Drawing on the lessons from the misreporting case, this target would serve as an early warning signal (observed at high-frequency) for fiscal developments above-the-line, in addition to ensuring that the government accumulates enough cash overtime to meet its prospective financial obligations, including vis-à-vis the Fund. Meeting this target will require strong coordination and communication not just between MEF and the BCE, but also between MEF and the subsectors of the NFPS. The QPC would be supplemented by a traditional NIR target as an IT to monitor the BCE balance sheet more broadly, even though reserves in dollarized economies are not comparable to those with own currencies.

- *Social assistance target.* Given the authorities' commitment to have more low-income households covered by the social assistance programs, an indicative target would track progress towards their goal of reaching 80 percent of low-income household by end-2021 (¶26). Monitoring coverage of families requires the authorities establishing a monitoring framework, on which they are receiving World Bank support, and coordinating well across the Ministry of Economy and Finance, the Ministry of Economic and Social Inclusion (MIES), and the social registry.

43. Capacity to repay. The proposed access level would result in peak Fund credit reaching $8.6 billion (874 percent of quota) in 2022. At the same time, gross financing needs (GFN, including Fund repayments), would range between 2.8 to 5 percent of GDP in the repayment period, lower than other exceptional access cases. Peak Fund obligations would constitute 5.1 percent of exports and 3.3 percent of government revenues—at or below median compared to other exceptional access cases—but be highly elevated as a share of gross reserves, peaking at 20 percent. Net international reserves are projected to remain deeply negative at program completion, making it critical to sustain access to financing and continuing creditor support. Although reserves in a dollarized economy are not straightforward to compare to those in countries with their own currencies, they still need adequate liquidity buffers for foreign and domestic payments. Against these considerations, staff judge that Ecuador would have adequate capacity to repay the proposed access levels, contingent on program implementation and support from other creditors that enable Ecuador to rebuild liquidity buffers. However, there is limited room for maneuver, and partial or non-implementation of the program could severely strain the capacity to repay (see Staff Supplement on Assessment of Risk to the Fund's Liquidity Position).

44. Financing Assurances. There are firm financing commitments for the first 12 months and has good prospects for the remainder, with the latter including additional support from IFIs and official bilateral creditors. This support is critical also for better burden sharing. Financing in post-program years is partly predicated on conservative assumptions concerning market access. The authorities see asset monetization as an important source of financing in the latter part of the program, with upside potential especially if successful implementation of the Fund-supported program improves risk appetite for Ecuadorian assets, and given that the underlying technical work for some asset monetization programs is fairly well advanced. Should there be shortfalls in the assumed financing, the authorities agree that additional fiscal efforts may be needed, despite their impact on growth.

45. Political Assurances. Political assurances are deemed adequate; they have been received from a broad range of candidates, who are supportive of program objectives and its key policies. One candidate expressed support for the program objectives and agreed to remain in close dialogue with Fund staff, including to help iron out divergence of views on policies; one candidate was not yet ready to engage in discussions.

46. Safeguards Assessments. The last assessment of the Central Bank of Ecuador was finalized in June 2019, therefore an updated safeguards assessment will not be required. A fiscal safeguards review will be needed, given that disbursements involve exceptional access of Fund resources with more than 25 percent directed to budget support. Staff will continue to monitor the implementation of recommendations from the last safeguards assessment. Two prior actions, on the BCE external audit and audit committee, directly address recommendations from that assessment. Most of the remaining ones require the enactment of the new central bank law.

47. Statistical Issues. Ecuador will continue to align government finance statistics to international best standards. A dedicated STA short-term expert (STX) will work closely with the authorities during peripatetic visits to (1) compile the GFS time series for the NFPS and its subsectors (central government, local governments, social security funds and SOEs) for historical and current data; and (2) prepare and roll-out a compilation guide for public finance statistics, with involvement of different NFPS entities (both are *end-May 2021 structural benchmarks*). In addition, staff will continue to work in close collaboration with the authorities on debt statistics and a wide range of economic statistics.

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 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 established a public procedure to follow in the event that a holder of these bonds requests the liquidation of the securities. 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. Article VIII/CFM. The authorities are committed to phase out the tax on transfers abroad, once the macroeconomic stability is restored, and the reserves position is strengthened. The tax constitutes both a capital flow management measure (CFM) under the Fund's Institutional View on Liberalization and Management of Capital Flows, and also an exchange restriction subject to Fund approval under Article VIII.[3] The authorities have requested temporary Fund approval for maintaining the exchange restriction arising from the tax on transfers abroad for balance of payments-reasons (see LOI).

[3] In addition, the SUCRE (Sistema Unitario de Compensación Regional de Pagos) regional payments arrangement also gives rise to a discriminatory exchange restriction since the period for settlement under the bilateral payment arrangement exceeds three months. This restriction has not been approved (please see SR No. 19/210).

Box 1. Assessment of Exceptional Access Criteria

Staff judge that the exceptional access criteria are met, as explained below.

Criterion 1—*The member is experiencing or has the potential to experience exceptional balance of payments pressures on the current account or the capital account resulting in a need for Fund financing that cannot be met within the normal limits.*

Ecuador is experiencing exceptional BOP pressures, stemming from the deepest recession on record and a loss of market access. The confluence of shocks described above has led to an estimated financing gap of $6.5 billion over 2020-22, even after the successful restructuring of global bonds, support from official bilateral creditors and IFIs, and an ambitious yet realistic fiscal consolidation. Since Ecuador currently has $2.3 billion (236 percent of quota) in credit outstanding to the Fund, access above $1.2 billion in 2020 and over $2 billion cumulatively would require exceptional access.

Criterion 2— *A rigorous and systematic analysis indicates that there is a high probability that the member's public debt is sustainable in the medium term. Where the member's debt is assessed to be unsustainable ex ante, exceptional access will only be made available where the financing being provided from sources other than the Fund restores debt sustainability with a high probability. Where the member's debt is considered sustainable but not with a high probability, exceptional access would be justified if financing provided from sources other than the Fund, although it may not restore sustainability with high probability, improves debt sustainability and sufficiently enhances the safeguards for Fund resources***.**

Ecuador's debt had become unsustainable following the RFI due to the continued deterioration in the macro-economic situation. However, public debt is now projected to steadily decline from its projected peak at end-2020 of 69 percent of GDP to 56½ percent by 2025 and 39.1 percent by 2030, after the successful debt restructuring, specific and credible assurances on financing/debt relief from bilateral and commitments from multilateral creditors in 2020-22, and resuming a path to further strengthen public finances on a sustained basis beginning next year, once the pandemic wanes, and continuing over the medium-term. Under those conditions, staff assess Ecuador's public debt to be sustainable with high probability.

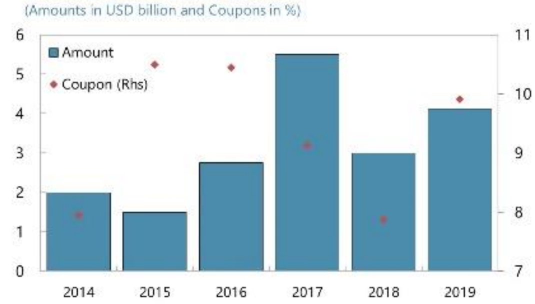
Stress tests show that the debt trajectory is sensitive to shocks to the primary balance and growth, particularly in the near term, making the sustained medium-term fiscal consolidation crucial for debt to remain on a sustainable path. The envisaged consolidation has been designed to be realistic to help improve its sustainability, but efforts will be required to stay on track, as the path is nevertheless ambitious. The recent adoption of the organic budget law, enshrining a debt ceiling of 40 percent of GDP by 2032, provides a key safeguard to debt sustainability; the program includes conditionality for operationalizing it in an expedited manner.

Criterion 3—*The member has prospects of gaining or regaining access to private capital markets within a timeframe and on a scale that would enable the member to meet its obligations falling due to the Fund.*

Until losing market access this year, Ecuador had sustained access to foreign financial markets, with long-term global bond issuances around $3-5 billion per year over the last four years, although the terms of this financing were often not favorable Historical evidence suggests that Ecuador has been successful in regaining access to the international capital markets within 24-36 months following a debt restructuring. While the global economic outlook is uncertain and markets are volatile in the current conjuncture, Ecuador's re-access to foreign capital could be supported by the wide perception that it negotiated the debt exchange with its creditors in good faith—with 98 percent of creditor support—and a robust implementation of the authorities' reform program. The EMBI spread has declined below 1000 bp (from 6000 bp in the wake of the pandemic), following the successful debt exchange and the staff-level agreement on the new Fund-supported program, with S&P and Fitch upgrading Ecuador's sovereign credit rating from default to B- in early September.

Ecuador: Global Bond Issuance[1/]

(Amounts in USD billion and Coupons in %)



[1/]The amount for each year corresponds to the sum of all issuances in that year and the coupon corresponds to the weighted average coupon across those issuances.
Source: Bloomberg

Box 1. Assessment of Exceptional Access Criteria (concluded)

Criterion 4—*The policy program provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment.*

The Ecuadorean authorities are fully committed and willing to implement the policies of the program and take the needed steps to ensure its success. They have demonstrated their commitment with important actions both under the previous EFF arrangement (see Annex I) and during the crisis period:

- Under the previous EFF arrangement, the authorities made progress in meeting the program objectives, including by (1) improving public finances (consolidating by 1.3 percentage points of GDP in 2019), submitted an organic budget law with fiscal rules and a debt anchor; (2) passing regulation prohibiting monetary financing; (3) initiating reforms on transparency and governance, including by submitting an anticorruption legislation; and (iv) strengthening the social safety net.
- Even in the midst of the pandemic and following the cancelation of the 2019 EFF arrangement, and notwithstanding a challenging domestic and global environment, the authorities have continued to pursue economic and structural reforms, including by adopting of the organic budget law, implementing an ambitious and potentially contentious fuel subsidy reform, and further rationalizing expenditure.

At the same time, shortcomings in institutional capacity and a challenging political environment have constrained implementation. The previous EFF arrangement and the incident of misreporting identified important technical capacity constraints and limited inter-agency coordination as the main underlying cause for deficiencies in the collection and compilation of fiscal statistics; more generally, there is a need to strengthen cohesive policymaking. In addition, lack of a stable political majority has led to long delays and shortfalls in implementing key commitments under the EFF arrangement, such as a deeper tax and central bank reforms.

The authorities have implemented corrective actions to address the deficiencies that resulted in misreporting, as previously reported to the Board, with tangible improvements in transparency and information provision to the Fund. Notwithstanding these encouraging developments, the authorities recognize the need to continue building capacity and strengthen institutions, for which they seek Fund support. Early and strong efforts under the new program in key areas, including by leveraging extensive capacity development from the Fund and other IFIs, as laid out in the MEFP, will improve institutional and political capacity and strengthen the prospects of success beyond the current administration.

The fragmented politics and upcoming elections can pose important risks to program implementation, making safeguards all the more important. The authorities have completed five prior actions in areas that improve institutional capacity, transparency, and policy making. They have also committed to a number of early structural benchmarks in similar areas, reflecting their resolve to leave the country with stronger policies and institutions for the next administration. These all demonstrate the political capacity to take action and strengthen the prospects of program success beyond the current administration. The President providing a letter of support to the program, and the parliamentary letter of support for program objectives demonstrate strong ownership and political capacity. The authorities are also implementing a robust communications strategy to build public support for the key objectives of the program to enhance the prospects of program success. Under the next administration, successful implementation will hinge on buy-in and political will from the legislators.

STAFF APPRAISAL

50. The Ecuadorian authorities' swift and decisive policy responses to the severe shocks this year has prevented a deeper crisis. The authorities' policy response appropriately combined short-term measures to contain the economic fallout from the crisis on the population and bold steps towards ensuring the long-term sustainability of public finances. The introduction of an automatic fuel pricing mechanism, ground work to strengthen the social safety nets, moderation in public wage bill, prioritization of expenditure all demonstrated their resolve and prevented the crisis from derailing public finances in the short term, ensuring that the country can meet its debt targets under COPLAFIP.

51. Continuing to expand the coverage of social assistance programs is essential for limiting the economic fallout from the crisis. Strengthening the social safety net will equip the government with the needed tools to reach vulnerable segments of the population in a timely manner. The current system has a relatively low coverage of families in need; the authorities' bold plans to expand coverage and better target the programs are expected to significantly improve the system. In the near term, the vulnerable households need to be supported through the downturn, which is adding to poverty. Going forward, compensating them for the potential adverse impact of fiscal consolidation should be an integral part of the overall fiscal strategy.

52. Starting an ambitious process to substantially strengthen public finances as the crisis subsides is critical to complement the debt exchange to ensure public debt sustainability. Rolling back exceptional crisis-related measures next year when the pandemic begins to wane and the economy starts to recover would both be the first step toward improving fiscal balances and would go a long way towards meeting the goal of debt sustainability. This should be complemented by a comprehensive fiscal package that includes both revenue and spending measures, to keep lowering debt over the coming years, align balances with peer countries, and improve external competitiveness.

53. The newly legislated fiscal policy frameworks should be operationalized swiftly to improve transparency in public financial management along with key measures to enhance the effectiveness of the anticorruption and AML/CFT frameworks. Expeditiously passing COPLAFIP-related regulations will make the landmark law operational and allow improvements in data collection as well. In addition, durably tackling the recurrent arrears problem requires adopting robust and permanent cash management practices, including cash forecasting over a relatively long horizon and overall financial planning. Equally important, improved transparency in public procurement and enhancing the anticorruption framework would strengthen accountability, reduce governance vulnerabilities, and protect the public purse. Continuing to promote debt transparency would allow for a better comparison of cost of funds and candid assessment of risk trade-offs across sovereign debt instruments in the management of the sovereign debt portfolio. The debt management strategy, planned for February 2021, is an opportunity to plan for operations to undertake in 2021 to address the upcoming amortizations in 2022 and beyond.

54. Enhancing the institutional framework for the central bank would strengthen the foundations of the dollarization regime. Ensuring the operational autonomy of the BCE and aligning its audit function to international standards would be critical to safeguarding the dollarization regime. Equally important, improved cash management practices by the Treasury would allow the government to anticipate cash shortfalls, limiting the temptation to recourse to ad-hoc alternative modes of financing *ex-post*, which if use widely as alternative means of exchange, could weaken the integrity of the dollarization regime.

55. Maintaining financial stability will hinge on preparing institutions for times of stress. The liquidity fund assets had been built up over a long period of time; further reductions in bank contributions should be avoided so that the fund has the resources to provide emergency liquidity and is able to pool risks across banks, as intended. Continued vigilance vis-à-vis credit risk accumulation and agility in supervision would help navigate the unchartered *post*-pandemic era. Coordination among oversight authorities would be strengthened through the planned Financial Coordination Committee. These arrangements should be complemented by developing a more robust legal framework for the financial system, including enhanced contingent arrangements. In addition, continuous assessment of the *Reactivate Ecuador* program is warranted to ensure it provides appropriate funding tools to help rebuild the balance sheets of viable firms.

56. A longer term comprehensive structural reform agenda is needed to raise Ecuador's growth potential, enhance transparency, and improve competitiveness. The authorities have also formulated priorities for a longer-term reform roadmap that would raise Ecuador's growth and create jobs if implemented. These reforms, including in the areas of governance, anticorruption, AML/CFT, public enterprises, labor markets, and the business environment, would address bottlenecks in the economy and start addressing the exchange rate overvaluation as assessed in Annex V.

57. Closing existing data gaps is critical for sound public finance management and will require deliberate efforts to build capacity. Diligently pursuing efforts to improve data quality should remain a priority. Close coordination between the Ministry of Economy and Finance and NFPS sub-sectors (central government, local governments, SOEs, and social security funds) are critical for the compilation of internally consistent fiscal statistics. Sound cash forecast will guide forward-looking budget decisions and limit accumulating domestic payment arrears. In this regard, the authorities should seek to leverage the technical support provided by the Fund—including through short- and long-term experts—and other partners to build and retain technical capacity in-house, including in the areas of fiscal statistics, cash forecast, debt transparency and management and financial surveillance.

58. Closer coordination across public sector agencies and far-reaching social dialogue is needed for a successful implementation of the Fund-supported program. Coordination is critical both at the policy and technical levels. The National Assembly's recent passing of the statement on Ecuador's high level policy objectives demonstrated the country's commitment to reform. Going forward, broad-based social dialogue around the policy tradeoffs faced by Ecuador against the backdrop of "lower for long" oil prices would strengthen domestic ownership and increase the chances of program success.

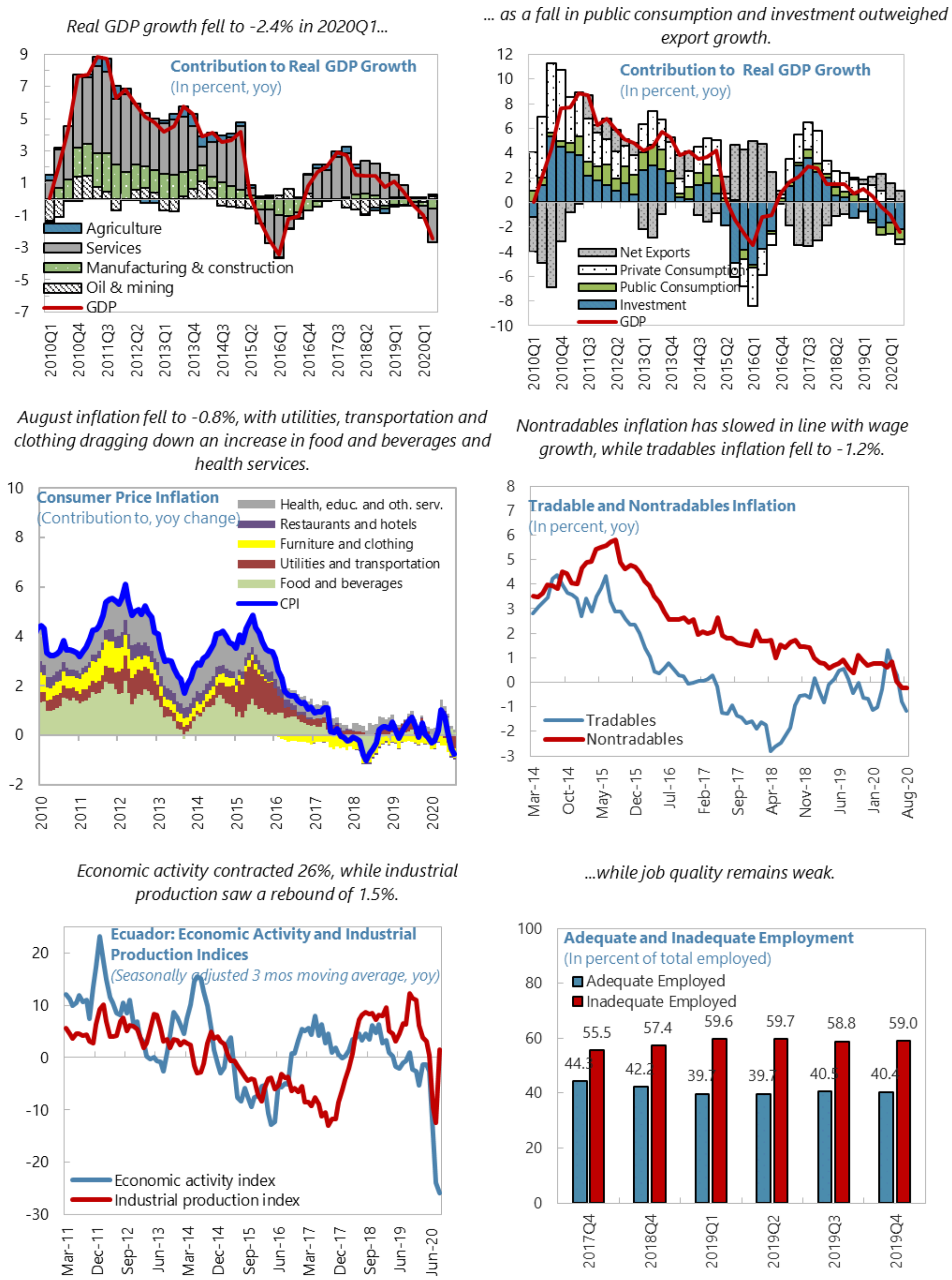
59. The program remains, however, subject to substantive risks. These include heightened uncertainties surrounding the global outlook, as well as domestic factors that could make program implementation challenging in the short and medium term, including limited buffers, the need to secure broad-based support for the program objectives and its key policies, and the political will of the next administration and legislators in the National Assembly.

60. Capacity development (CD) should be a core pillar of Ecuador's IMF-supported program. Building human capital and knowledge to ensure a well-functioning and efficient public sector will deliver long-term gains for all Ecuadorians. The Fund, together with other IFIs, would continue to provide CD to Ecuador, particularly in the areas of government financial statistics, public financial management, and financial programming. Prioritizing CD needs by topic and timing will be important to ensure effectiveness and achieving lasting results.

61. Staff supports the authorities' request for a 27-month Extended Fund Facility with exceptional access. Ecuador's economic plan is carefully calibrated to support the population through the crisis, restore macroeconomic stability, ensure long-term fiscal sustainability, while fortifying the institutional foundations for inclusive private sector led growth. Early actions to strengthen institutions and policy frameworks will keep the country on stronger grounds through the transition to the next administration.

62. Staff also supports Board approval for the retention for a one-year period of the exchange restriction arising from the tax on transfers abroad for the making of payments and transfers on current international transactions, given that it is maintained for BOP reasons, is temporary and non-discriminatory.

Figure 1. Ecuador: Recent Economic Developments



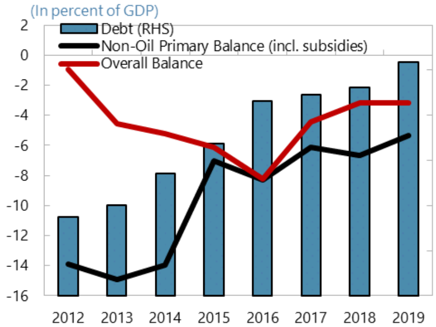
Sources: Central Bank of Ecuador, National Statistical Institute of Ecuador (INEC), and IMF staff calculations.

Figure 2. Ecuador: Fiscal Developments [1/]

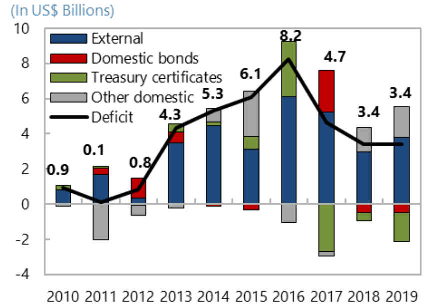
Rising fiscal deficits led to higher debt.

The deficit was financed largely by external bond issuances.

Debt and Fiscal Deficit
(In percent of GDP)



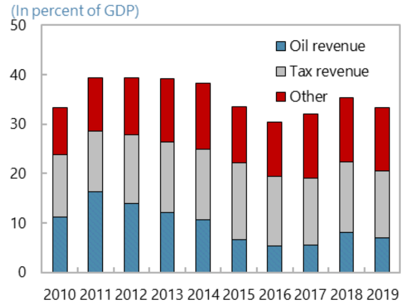
Fiscal Deficit and Financing Sources
(In US$ Billions)



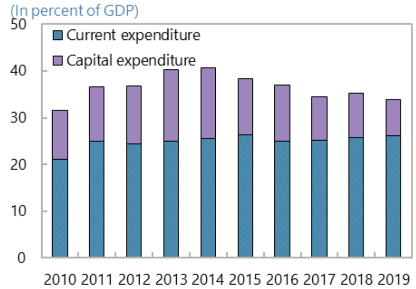
Revenues fell, in part due to the fall in oil revenues...

... while capital expenditure contraction helped offset the increase in current primary spending.

Revenues
(In percent of GDP)



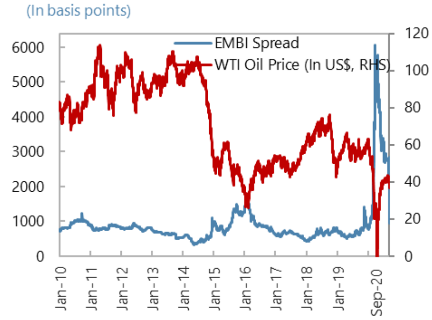
Primary Expenditures
(In percent of GDP)



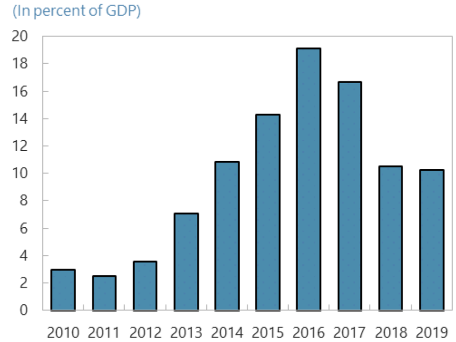
External and domestic events had significant, negative, effects on spreads, which had previously mirrored fluctuations in oil prices...

... which increased GFNs, eventually resulting in a bond restructuring.

EMBI Spread and Oil Price
(In basis points)



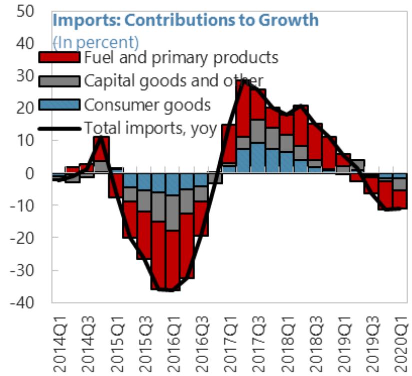
Gross Financing Needs
(In percent of GDP)



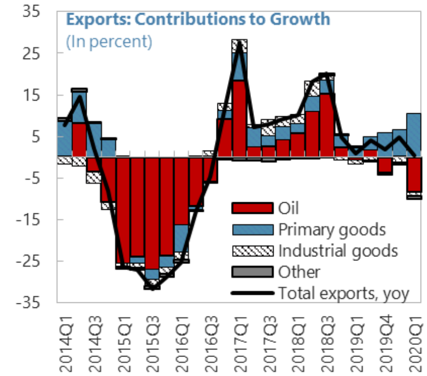
Sources: Central Bank of Ecuador, Ministry of Finance, Haver, Bloomberg, and IMF staff calculations.
1/ The data for Ecuador reflect net lending/borrowing for the Non-Financial Public Sector (NFPS). Ecuadorian authorities, in the context of the EFF approved in March of 2019 and with the technical support from the IMF Staff, are undertaking revisions of the historical fiscal data for the net-lending borrowing of the NFSP with the view of correcting recently-identified statistical errors, mostly in the recording of revenues and expenditures of the local governments. Fiscal data reported in the table for 2018 and 2019 reflect the corrected series while the data for earlier years are still under revisions and will be corrected in the subsequent WEO releases as the authorities proceed with the corrections in the earlier years, going as far back as 2012. The authorities are also working on reconciling historical revenue and expenditure data with financing.

Figure 3. Ecuador: A Vulnerable External Position

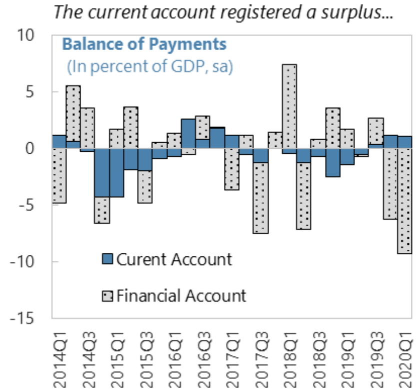
Import growth continued to decelerate in 2020Q1, decreasing to -11%...



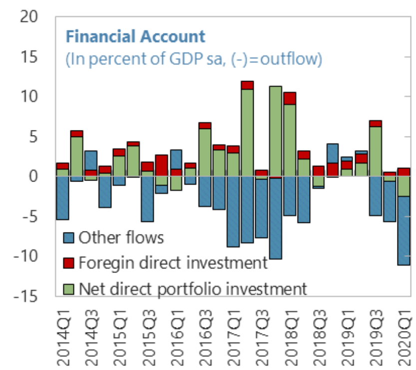
...while export growth fell to 0.6%.



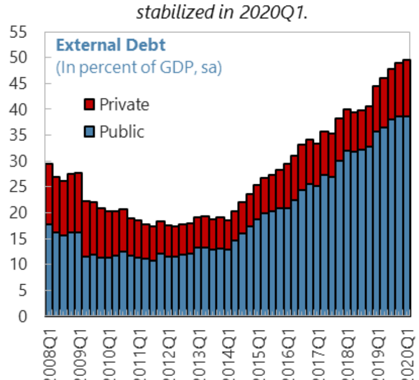
The current account registered a surplus...



... and FDI flows remained low.



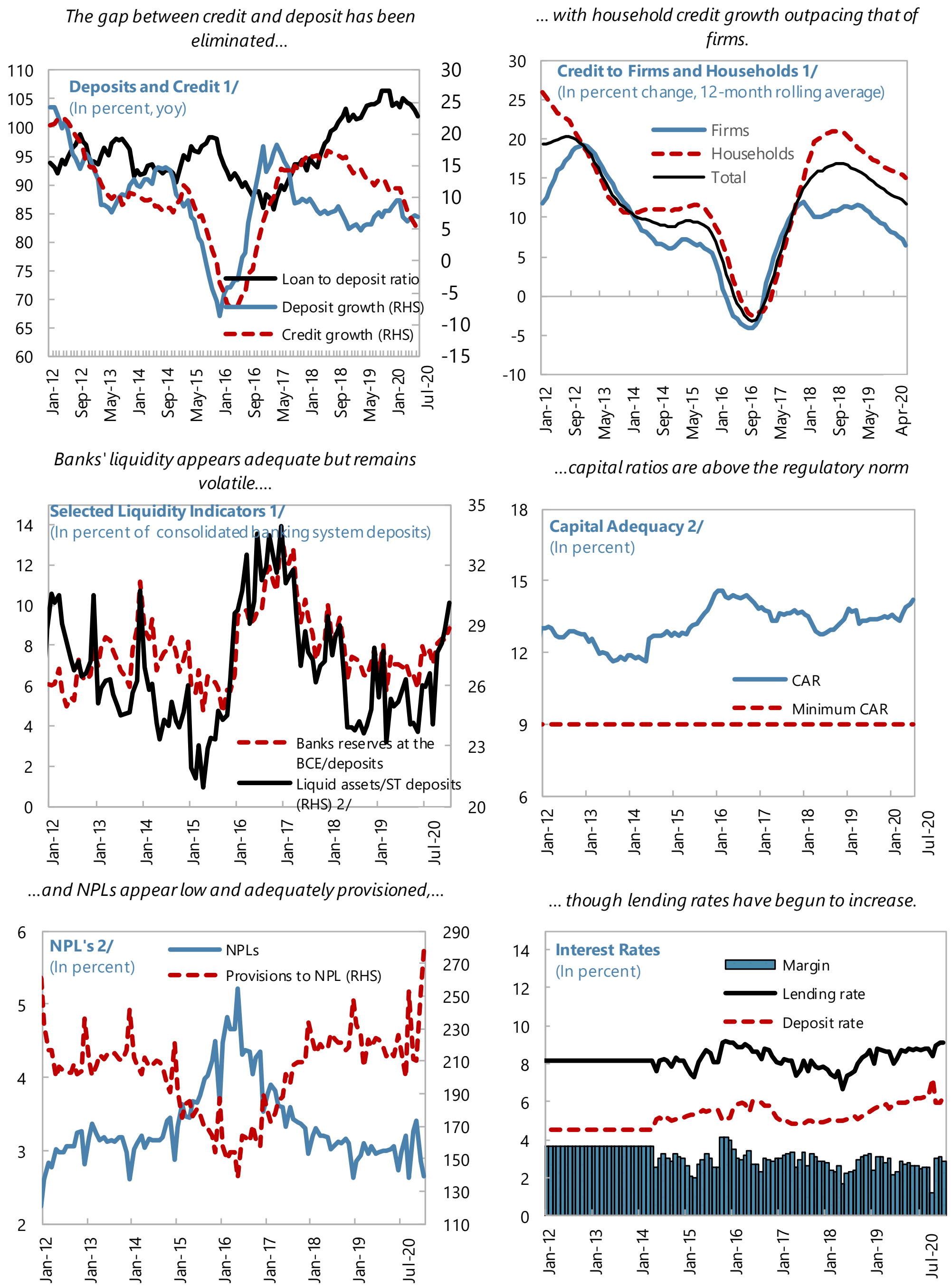
Both public and private external debt stabilized in 2020Q1.



... while GIR has slightly recovered after a sharp fall in early 2020.

Sources: Central Bank of Ecuador, STA BOP database, and IMF staff calculations.

Figure 4. Ecuador: Financial System Developments

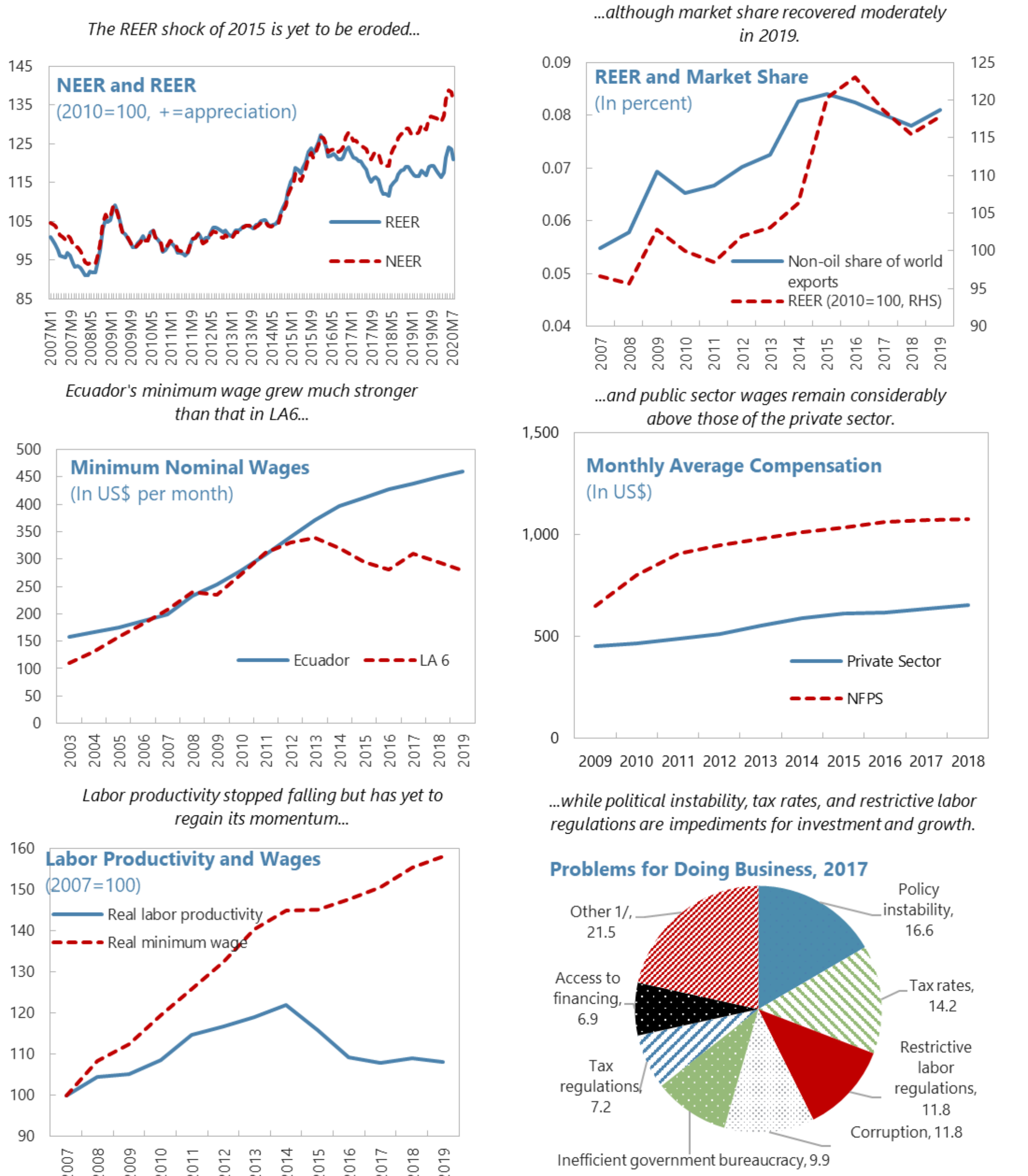


Sources: Central Bank of Ecuador, Superintendency of Banks, IMF Monetary and Financial Statistics, and IMF staff calculations.

1/ Loan to deposit data corresponds to Other Depository Institutions, which include private banks, *Banecuador*, *Banco del Pacifico*, private financial companies, mutualists, cooperatives, and credit card companies. While credit and deposit data corresponds to the whole financial system.

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

Figure 5. Ecuador: Competitiveness



Source: INEC, BCE, ILO, INS database, Haver, World Economic Forum (Executive Opinion Survey 2017), and IMF staff calculations.

1/ Other includes: Foreign currency regulations, poor work ethic in national labor force, inadequate supply of infrastructure, government instability/coups, restrictive labor regulations, tax regulations, insufficient capacity to innovate, poor public health, and crime and theft (in order of importance).

Table 1. Ecuador: Selected Economic and Financial Indicators

	2018	2019	2020	2021	2022	2023	2024	2025
	(Percent change, unless otherwise indicated)							
National income and prices								
Real GDP	1.3	0.1	-11.0	4.8	1.3	1.7	2.0	2.3
Domestic demand (contribution to growth)	2.2	-0.9	-13.1	5.6	0.8	1.0	1.8	2.2
External Demand (contribution to growth)	-0.9	1.0	2.1	-0.8	0.5	0.7	0.3	0.1
Consumer price index period average	-0.2	0.3	0.0	1.0	2.3	1.4	1.0	1.0
Consumer price index end-of-period	0.3	-0.1	-0.3	2.0	1.8	1.0	1.0	1.0
Banking system								
Net domestic assets	7.6	9.5	0.7	4.1	-3.2	-2.3	-4.3	-0.5
Liabilities	4.7	8.6	-2.3	6.6	2.1	1.9	1.5	1.6
Credit to the private sector	14.9	11.3	-1.8	8.2	3.2	3.2	3.5	3.8
External sector								
Exports	12.5	2.8	-21.1	6.2	4.7	4.4	4.5	4.3
Oil	27.3	-1.5	-40.7	14.4	4.2	3.5	3.2	3.1
Non-oil	5.3	5.8	-8.0	2.8	4.8	4.8	5.2	5.0
Imports	14.2	-1.7	-18.3	5.4	3.2	2.4	2.9	3.3
Terms of trade	1.3	-0.7	-10.7	3.8	-0.1	-0.4	0.7	0.8
Real effective exchange rate (2010=100)	115.4	117.8						
Real effective exchange rate, end-of-period (depreciation, -)	-2.8	2.0						
	(Percent of GDP)							
Current account balance	-1.2	-0.1	-2.0	-0.1	0.3	0.6	0.8	0.6
Public finances								
Revenue	35.3	33.4	30.1	31.6	34.6	35.2	35.5	35.5
Expenditure	38.5	36.6	39.0	34.6	34.0	33.3	33.1	33.3
Overall balance (deficit -)	-3.2	-3.2	-8.9	-2.9	0.6	1.9	2.4	2.3
Non-oil primary balance	-4.2	-3.1	-6.8	-3.6	-0.5	1.0	1.3	1.3
Non-oil primary balance (incl. fuel subsidies)	-6.7	-5.3	-7.9	-4.6	-1.6	-0.1	0.2	0.2
Public debt 1/	46.1	51.8	68.9	67.4	65.8	62.3	60.0	56.1
Domestic	12.4	13.9	17.2	15.5	14.9	13.8	13.8	12.6
External	33.8	37.9	51.7	52.0	50.8	48.5	46.2	43.5
Gross Financing Needs								
In percent of GDP	10.5	10.3	16.1	8.1	4.2	4.0	3.2	4.6
In percent of Exports	51.0	48.4	82.5	42.0	21.5	20.4	15.9	22.7
In percent of Revenues	29.7	30.7	53.4	25.7	12.2	11.5	9.0	12.9
	(Percent of GDP)							
Saving-investment balance								
Consumption	74.4	75.0	78.3	77.2	76.5	76.1	75.9	75.8
Private	59.7	60.5	62.0	62.5	62.7	62.7	62.7	62.7
Public	14.7	14.5	16.3	14.7	13.8	13.4	13.2	13.1
National saving	25.5	24.9	20.3	23.2	24.1	24.3	24.3	24.0
Private	19.1	20.3	21.7	19.7	17.2	16.6	16.1	16.0
Public	6.4	4.6	-1.4	3.5	6.8	7.7	8.2	8.0
Gross investment	26.7	25.0	22.4	23.4	23.7	23.7	23.5	23.4
Private 2/	18.7	18.3	15.9	17.9	18.4	18.7	18.6	18.5
Public	8.0	6.6	6.4	5.4	5.3	4.9	4.9	4.9
Memorandum items:								
Nominal GDP (US$ millions)	107,562	107,436	93,078	99,247	102,803	106,026	109,550	113,470
GDP per capita (US$)	6,318	6,222	5,316	5,589	5,709	5,807	5,917	6,043
Gross international reserves (US$ millions) 3/	2,158	2,933	2,475	3,275	5,007	6,345	8,151	8,787
Gross international reserves (as a percent of ARA metric)	12	15	13	17	24	30	38	40
Net international reserves (US$ millions) 4/	-2,895	-2,903	-7,848	-8,679	-8,039	-6,550	-4,134	-2,199
Oil price Ecuador mix (US$ per barrel)	60.6	55.3	35.6	39.8	41.0	42.0	42.8	43.6
Oil production (millions of barrels)	188.8	193.8	173.0	185.8	187.5	189.1	190.7	192.4
Exports of oil (millions of barrels) 5/	145.1	153.4	140.8	143.7	145.5	147.2	148.9	150.6

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 estimates are based on the IMF's Public Sector Debt Statistics: Guide for Compilers and Users (PSDSG).

2/ Includes inventories.

3/ GIR excludes non-liquid and encumbered assets.

4/ Net international reserves is equal to gross international reserves less outstanding credit to the IMF, short-term foreign liabilities of the BCE, deposits of other depository institutions and other financial institutions (excl. BIESS) at the central bank, and short-term liabilities of the central government, all derivative positions. Program exchange rates are those in effect on July 31, 2020 (see TMU).

5/ Includes both crude and derivatives.

Table 2a. Ecuador: Operations of the Non-Financial Public Sector (Net Accounting)
(in millions of US dollars, unless otherwise indicated)

		Est.	Projections					
	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	**37,996**	**35,914**	**28,006**	**31,396**	**35,562**	**37,278**	**38,923**	**40,337**
Oil revenue, net 1/	8,181	7,785	4,538	5,563	6,400	6,494	6,985	7,364
Nonpetroleum revenue	26,966	25,506	21,492	23,215	26,326	27,826	28,853	29,888
Taxes	15,422	14,490	11,880	12,921	15,663	16,829	17,490	18,119
Social security contributions 2/	5,541	5,863	4,959	5,534	5,732	5,912	6,109	6,327
Other	6,003	5,153	4,652	4,760	4,931	5,085	5,254	5,442
Operating surplus of public enterprises	2,849	2,623	1,976	2,619	2,836	2,958	3,085	3,085
O/w profits of oil companies withheld for investment	2,748	2,489	1,847	2,469	2,686	2,808	2,935	2,935
Expenditure	**41,412**	**39,319**	**36,308**	**34,303**	**34,961**	**35,308**	**36,268**	**37,755**
Primary expenditure	38,748	36,405	33,440	32,738	33,151	33,364	34,158	35,233
Current	27,603	28,023	26,395	26,383	26,726	27,162	27,857	28,705
Wages and salaries	10,323	10,190	9,438	9,535	9,590	9,645	9,874	10,109
Purchases of goods and services	4,735	4,643	5,043	4,327	3,882	3,904	3,933	4,074
Social security benefits 2/	5,382	5,773	6,080	6,033	6,249	6,445	6,659	6,897
Other	7,163	7,418	5,835	6,488	7,005	7,168	7,391	7,625
Cost of imports of oil derivatives	4,041	4,440	3,038	3,068	3,280	3,484	3,622	3,762
Payments to private oil companies (SH) 3/	1,521	1,337	1,145	1,130	1,130	1,130	1,130	1,130
Other	1,601	1,641	1,651	2,289	2,595	2,554	2,639	2,733
Capital	10,342	8,335	7,018	6,356	6,425	6,202	6,300	6,528
Fixed capital spending	9,941	8,193	6,883	6,212	6,277	6,049	6,142	6,364
O/w investment in oil	1,570	1,625	1,351	1,643	1,765	1,781	1,797	1,812
Net-lending	402	143	135	143	148	153	158	164
Extra budgetary expenses	803	46						
Primary balance	**-752**	**-491**	**-5,434**	**-1,342**	**2,411**	**3,914**	**4,765**	**5,104**
Interest	**2,663**	**2,914**	**2,868**	**1,565**	**1,810**	**1,944**	**2,111**	**2,522**
O/w external	2,314	2,577	2,505	1,281	1,533	1,679	1,845	2,241
Overall balance	**-3,415**	**-3,405**	**-8,302**	**-2,907**	**601**	**1,970**	**2,655**	**2,583**
Memorandum items:								
Non-oil primary balance 4/	-4,550	-3,361	-6,285	-3,532	-501	1,007	1,394	1,509
Non-oil PB (incl. fuel subsidies)	-7,156	-5,714	-7,336	-4,523	-1,617	-156	177	234
Cyclically Adjusted Non-oil Primary Balance	-4,583	-3,227	-4,057	-2,488	605	1,973	2,093	1,848
Oil balance 5/	3,798	2,871	851	2,190	2,912	2,907	3,371	3,595
Social Spending		1,016	1,446	1,774	1,998	1,875	1,875	1,875
Public Debt 6/	49,629	55,678	64,151	66,908	67,599	66,024	65,687	63,702

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 public debt estimates are preliminary and subject to revisions in accordance with the IMF's Public Sector Debt

Table 2b. Ecuador: Operations of the Non-Financial Public Sector (Net Accounting)
(in percent of GDP, unless otherwise indicated)

		Est.	Projections					
	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	**35.3**	**33.4**	**30.1**	**31.6**	**34.6**	**35.2**	**35.5**	**35.5**
Oil revenue, net 1/	7.6	7.2	4.9	5.6	6.2	6.1	6.4	6.5
Nonpetroleum revenue	25.1	23.7	23.1	23.4	25.6	26.2	26.3	26.3
Taxes	14.3	13.5	12.8	13.0	15.2	15.9	16.0	16.0
Social security contributions 2/	5.2	5.5	5.3	5.6	5.6	5.6	5.6	5.6
Other	5.6	4.8	5.0	4.8	4.8	4.8	4.8	4.8
Operating surplus of public enterprises	2.6	2.4	2.1	2.6	2.8	2.8	2.8	2.7
O/w profits of oil companies withheld for investment	2.6	2.3	2.0	2.5	2.6	2.6	2.7	2.6
Expenditure	**38.5**	**36.6**	**39.0**	**34.6**	**34.0**	**33.3**	**33.1**	**33.3**
Primary expenditure	36.0	33.9	35.9	33.0	32.2	31.5	31.2	31.1
Current	25.7	26.1	28.4	26.6	26.0	25.6	25.4	25.3
Wages and salaries	9.6	9.5	10.1	9.6	9.3	9.1	9.0	8.9
Purchases of goods and services	4.4	4.3	5.4	4.4	3.8	3.7	3.6	3.6
Social security benefits 2/	5.0	5.4	6.5	6.1	6.1	6.1	6.1	6.1
Other	6.7	6.9	6.3	6.5	6.8	6.8	6.7	6.7
Cost of imports of oil derivatives	3.8	4.1	3.3	3.1	3.2	3.3	3.3	3.3
Payments to private oil companies (SH) 3/	1.4	1.2	1.2	1.1	1.1	1.1	1.0	1.0
Other	1.5	1.5	1.8	2.3	2.5	2.4	2.4	2.4
Capital	9.6	7.8	7.5	6.4	6.3	5.8	5.8	5.8
Fixed capital spending	9.2	7.6	7.4	6.3	6.1	5.7	5.6	5.6
O/w investment in oil	1.5	1.5	1.5	1.7	1.7	1.7	1.6	1.6
Net-lending	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Extra budgetary expenses	0.7	0.0						
Primary balance	**-0.7**	**-0.5**	**-5.8**	**-1.4**	**2.3**	**3.7**	**4.3**	**4.5**
Interest	**2.5**	**2.7**	**3.1**	**1.6**	**1.8**	**1.8**	**1.9**	**2.2**
O/w external	2.2	2.4	2.7	1.3	1.5	1.6	1.7	2.0
Overall balance	**-3.2**	**-3.2**	**-8.9**	**-2.9**	**0.6**	**1.9**	**2.4**	**2.3**
Memorandum items:								
Non-oil primary balance 4/	-4.2	-3.1	-6.8	-3.6	-0.5	1.0	1.3	1.3
Non-oil primary balance (percent of non-oil GDP)	-4.5	-3.3	-7.0	-3.7	-0.5	1.0	1.3	1.4
Non-oil PB (incl. fuel subsidies)	-6.7	-5.3	-7.9	-4.6	-1.6	-0.1	0.2	0.2
Cyclically Adjusted Non-oil Primary Balance	-4.3	-3.0	-4.4	-2.5	0.6	1.9	1.9	1.6
Oil balance 5/	3.5	2.7	0.9	2.2	2.8	2.7	3.1	3.2
Social Spending		0.9	1.6	1.8	1.9	1.8	1.7	1.7
Public Debt 6/	46.1	51.8	68.9	67.4	65.8	62.3	60.0	56.1

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 public debt estimates are preliminary and subject to revisions in accordance with the IMF's Public Sector Debt Statistics: Guide for Compilers and Users (PSDSG).

Table 3. Ecuador: Non-Financial Public Sector Financing

(in millions of US dollars, unless otherwise indicated)

		Est.			Projections			
	2018	2019	2020	2021	2022	2023	2024	2025
Gross financing needs	**11,284**	**11,028**	**14,954**	**8,069**	**4,331**	**4,278**	**3,487**	**5,206**
Nonfinancial public sector deficit	3,415	3,405	8,302	2,907	-601	-1,970	-2,655	-2,583
Amortization	7,868	7,623	6,651	5,163	4,932	6,249	6,142	7,789
External	4,871	4,800	3,980	2,038	2,554	3,129	3,622	4,014
Multilateral	685	785	817	772	757	1,225	1,884	2,914
Bilateral	1,614	1,023	791	428	1,215	1,364	1,198	784
Private sector and other	879	2,124	2,237	720	488	448	448	225
Oil related financing	1,692	868	135	118	95	92	92	92
Domestic	2,998	2,823	2,671	3,124	2,378	3,120	2,520	3,775
Bonds	884	1,163	697	890	404	1,246	646	1,901
Treasury certificates	2,113	1,660	1,974	2,234	1,974	1,874	1,874	1,874
Gross financing sources	**11,284**	**11,028**	**14,954**	**8,069**	**4,331**	**4,278**	**3,487**	**5,206**
External	7,817	8,615	7,393	3,946	2,250	2,300	2,800	2,800
Multilateral	1,640	3,310	3,625	3,246	1,750	800	800	800
World Bank	236	653	1,428	1,076	100	100	100	100
Inter-American Development Bank	485	733	762	1,081	500	400	400	400
CAF	549	517	787	650	800	300	300	300
Other	370	6	4	439	350	0	0	0
IMF	0	1,401	643	0	0	0	0	0
Bilateral	978	738	998	700	0	0	0	0
Private sector and other	4,504	4,171	2,770	0	500	1,500	2,000	2,000
Oil related financing	695	445	0	0	0	0	0	0
Advance Payments for Contingencies		-48	0					
Domestic	2,175	2,444	3,561	2,624	1,081	1,978	687	2,406
Bonds	403	679	697	500	500	500	1,131	1,131
Bonds official	38	679	697	500	500	500	500	500
Bonds FPS	366	0	0	0	0	0	631	631
Treasury certificates	1,660	1,974	2,234	1,974	1,874	1,874	1,874	1,874
Change in deposits (+= drawdown)	-951	-23	-170	150	-1,292	-395	-1,687	32
Privatization and BCE transfers	0	0	0	0	0	0	0	0
Convenios de liquidez	564	-185	300	0	0	0	0	0
Other	498	0	0	0	0	0	0	0
Acquisition of fianncial assets	0	0	0	0	0	0	-631	-631
Net Arrears acumulation and other financing 1/	-823	0		0	0	0	0	0
Other liability to BCE			500					
Discrepancy	2,115	-31	0	0	0	0	0	0
IMF exceptional financing			4,000	1,500	1,000	0	0	0
Net financing	**3,415**	**3,014**	**4,302**	**1,407**	**-1,601**	**-1,970**	**-2,655**	**-2,583**
External	2,947	3,815	3,413	1,907	-304	-829	-822	-1,214
Domestic	-823	-379	890	-501	-1,297	-1,141	-1,833	-1,368
Net Arrears acumulation and other financing 1/	-823	0	0	0	0	0	0	0
Discrepancy	2,115	-423	0	0	0	0	0	0
Public Sector Debt 2/	**49,629**	**55,678**	**64,151**	**66,908**	**67,599**	**66,024**	**65,687**	**63,702**
External	36,323	40,748	48,161	51,569	52,264	51,435	50,614	49,399
o.w. oil related financing	629	716	581	463	368	276	184	92
Domestic	13,306	14,930	15,990	15,339	15,335	14,589	15,073	14,303
Bonds	5,417	5,120	5,120	4,729	4,825	4,079	4,563	3,793
Treasury certificates	1,660	1,974	2,234	1,974	1,874	1,874	1,874	1,874
Other liabilities	6,228	7,836	8,636	8,636	8,636	8,636	8,636	8,636
			(In percent of GDP)					
Gross financing needs	**10.5**	**10.3**	**16.1**	**8.1**	**4.2**	**4.0**	**3.2**	**4.6**
Nonfinancial public sector deficit	3.2	3.2	8.9	2.9	-0.6	-1.9	-2.4	-2.3
Amortization	7.3	7.1	7.1	5.2	4.8	5.9	5.6	6.9
Gross financing sources	**10.5**	**10.3**	**16.1**	**8.1**	**4.2**	**4.0**	**3.2**	**4.6**
External	7.3	8.0	12.2	5.5	3.2	2.2	2.6	2.5
Domestic	2.0	2.3	3.8	2.6	1.1	1.9	0.6	2.1
Arrears acumulation and other financing 1/	-0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Public sector debt 2/	**46.1**	**51.8**	**68.9**	**67.4**	**65.8**	**62.3**	**60.0**	**56.1**
External	33.8	37.9	51.7	52.0	50.8	48.5	46.2	43.5
Domestic	12.4	13.9	17.2	15.5	14.9	13.8	13.8	12.6

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

1/ Includes domestic floating debt and statistical discrepancy.

2/ 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 public debt estimates are preliminary and subject to revisions in accordance with the IMF's Public Sector Debt Statistics: Guide for Compilers and Users (PSDSG).

Table 4. Ecuador: Balance of Payments

(in millions of US dollars, unless otherwise indicated)

		Est.	Projections					
	2018	2019	2020	2021	2022	2023	2024	2025
Current account	**-1,335**	**-112**	**-1,864**	**-144**	**322**	**675**	**825**	**690**
Trade balance	-226	1,025	472	621	927	1,345	1,706	1,978
Exports, f.o.b.	22,133	22,774	18,119	19,228	20,114	21,006	21,972	22,938
Oil	8,802	8,669	5,142	5,882	6,131	6,348	6,552	6,753
Non-oil	13,331	14,105	12,977	13,346	13,983	14,658	15,420	16,185
Imports, f.o.b.	22,359	21,749	17,648	18,607	19,187	19,662	20,265	20,960
Oil	4,341	4,256	3,195	3,197	3,390	3,572	3,680	3,788
Non-oil	18,018	17,493	14,453	15,410	15,798	16,090	16,585	17,172
Services	-689	-763	-968	-982	-954	-907	-878	-860
Credits	3,242	3,320	2,480	2,656	2,808	2,927	3,043	3,163
Debits	3,930	4,083	3,448	3,638	3,762	3,834	3,922	4,024
Primary income	-2,829	-3,113	-3,426	-1,947	-2,098	-2,315	-2,629	-3,127
Credits	236	195	304	151	173	203	225	250
Debits	3,065	3,308	3,729	2,098	2,271	2,518	2,854	3,377
Secondary income	2,409	2,739	2,059	2,163	2,447	2,553	2,626	2,699
Of which: workers' remittances, net	2,578	2,595	1,906	2,000	2,278	2,379	2,446	2,513
Capital account	**-193**	**70**	**70**	**61**	**65**	**67**	**69**	**72**
Financial account	**-1,583**	**652**	**3,577**	**479**	**-345**	**-829**	**-1,463**	**-265**
Direct investment	-1,456	-938	-607	-673	-855	-901	-1,012	-1,155
Other public sector flows	-2,947	-3,815	-3,413	-1,907	304	829	822	1,214
Disbursements	-7,817	-8,615	-7,393	-3,946	-2,250	-2,300	-2,800	-2,800
Amortizations	4,871	4,800	3,980	2,038	2,554	3,129	3,622	4,014
Other private sector flows	2,819	5,405	7,597	3,059	206	-757	-1,273	-324
Errors and omissions	**-202**	**24**	**0**	**0**	**0**	**0**	**0**	**0**
Overall balance	**-146**	**-670**	**-5,371**	**-563**	**732**	**1,572**	**2,357**	**1,026**
Financing	**146**	**670**	**5,371**	**563**	**-732**	**-1,572**	**-2,357**	**-1,027**
Change in GIR (increase, -) 1/	-171	-713	908	-801	-1,732	-1,337	-1,806	-636
IMF net credit and loans	0	1,357	463	-136	0	-234	-551	-391
Other external financing 2/	317	26	0	0	0	0	0	0
IMF exceptional financing		0	4,000	1,500	1,000	0	0	0
Memorandum items:								
Current account balance (percent of GDP)	-1.2	-0.1	-2.0	-0.1	0.3	0.6	0.8	0.6
Oil balance (percent of GDP)	4.1	4.1	2.1	2.7	2.7	2.6	2.6	2.6
Exports	8.2	8.1	5.5	5.9	6.0	6.0	6.0	6.0
Imports	4.0	4.0	3.4	3.2	3.3	3.4	3.4	3.3
Non-oil balance (percent of GDP)	-5.4	-4.2	-4.1	-2.9	-2.4	-2.0	-1.9	-2.0
Goods export volume growth rate (percent)	-0.1	6.3	-7.7	1.9	2.8	2.9	2.2	2.1
Goods import volume growth rate (percent)	3.6	0.2	-16.3	5.5	1.1	0.5	1.5	2.0
Goods terms of trade growth rate (percent)	1.3	-0.7	-10.7	3.8	-0.1	-0.4	0.7	0.8
Oil price Ecuador mix (U.S. dollars per barrel)	61	55	36	40	41	42	43	44
External debt (percent of GDP)	42.5	48.2	60.2	57.7	57.5	57.8	57.1	54.8

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

1/ Reflects the national definition of gross international reserves.

2/ Includes foreign arrears and net flows from oil funds held abroad and flows associated with debt default and restructuring.

Table 5. Ecuador: External Financing

(in millions of US dollars, unless otherwise indicated)

		Est.	Projections					
	2018	2019	2020	2021	2022	2023	2024	2025
Gross external financing requirements	**10,080**	**9,139**	**10,293**	**6,759**	**6,860**	**7,229**	**7,645**	**8,108**
Current account financing need	1,335	112	1,864	144	-322	-675	-825	-690
Public sector amortizations	4,871	4,800	3,980	2,038	2,554	3,129	3,622	4,014
Private sector amortizations	3,875	4,227	4,449	4,577	4,627	4,775	4,849	4,784
Identified External Financing	**9,934**	**8,517**	**8,922**	**7,697**	**8,591**	**8,801**	**10,003**	**9,135**
Multilateral	1,640	3,310	3,625	3,246	1,750	800	800	800
Bilateral	978	738	998	700	0	0	0	0
Oil related financing	695	445	0	0	0	0	0	0
Private sector	4,504	4,171	2,770	0	500	1,500	2,000	2,000
Direct investment	1,456	938	607	673	855	901	1,012	1,155
Portfolio investment Financing	211	-235	-630	303	884	1,107	1,224	1,022
Other investment Financing	844	-942	-2,518	1,214	3,537	4,426	4,897	4,086
Net Transfers 1/	-395	94	70	61	65	67	69	72
IMF exceptional financing			4,000	1,500	1,000	0	0	0
Gross external financing sources	**10,251**	**9,900**	**9,385**	**7,560**	**8,591**	**8,566**	**9,451**	**8,744**
Identified External Financing	9,934	8,517	8,922	7,697	8,591	8,801	10,003	9,135
Past IMF Net Programs	0	1,357	463	-136	0	-234	-551	-391
Gross international reserves (-, increase) 2/	**-171**	**-713**	**908**	**-801**	**-1,732**	**-1,337**	**-1,806**	**-636**
Net international reserves, prog. definition (-, increase) 3/	**-397**	**7**	**4,945**	**831**	**-640**	**-1,489**	**-2,416**	**-1,935**

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/ Reflects the national definition of gross international reserves.

3/ Program net international reserves is equal to gross international reserves less outstanding credit to the IMF (incl. budget support to the Treasury), short-term foreign liabilities of the BCE, deposits of other depository institutions and other financial institutions (excl. BIESS) at the central bank, and short-term liabilities of the central

Table 6. Monetary Survey
(in millions of US dollars, unless otherwise indicated)

		Est.	Projections					
	2018	2019	2020	2021	2022	2023	2024	2025
I. Central Bank								
Net foreign assets	**3,902**	**4,628**	**3,345**	**4,351**	**6,122**	**7,494**	**9,338**	**10,017**
Of which: gross international reserves 1/	2,158	2,933	2,475	3,275	5,007	6,345	8,151	8,787
Net domestic assets	**1,108**	**-116**	**1,058**	**337**	**-1,336**	**-2,619**	**-4,538**	**-5,438**
Credit to the nonfinancial public sector, net	-2,086	-2,567	-620	-838	-2,127	-3,299	-4,378	-4,937
Of which: central government, net	1,398	1,130	2,124	2,087	903	-174	-1,155	-1,613
credits	3,035	2,932	4,093	3,716	3,716	2,937	3,567	3,022
debits	1,637	1,802	1,969	1,629	2,813	3,111	4,722	4,635
Credit to financial institutions	4,531	4,217	4,050	3,547	3,163	3,052	2,211	1,870
Other depository institutions	1,006	979	982	791	577	485	419	352
Other financial institutions	3,524	3,238	3,068	2,755	2,586	2,566	1,792	1,518
Credit to the private sector	17	13	11	12	13	13	13	14
Other, net	-1,353	-1,779	-2,384	-2,384	-2,384	-2,384	-2,384	-2,384
Liabilities	**5,011**	**4,512**	**4,403**	**4,688**	**4,786**	**4,876**	**4,801**	**4,579**
Currency and electronic money	84	81	70	74	77	79	82	85
Banks' reserves	4,859	4,377	4,278	4,559	4,655	4,742	4,665	4,440
Other depository institutions 2/	3,172	3,527	3,447	3,674	3,751	3,821	3,879	3,942
Other financial institutions 3/	1,688	850	831	886	904	921	785	498
Other 4/	68	54	54	54	54	54	54	54
II. Other Depository Institutions (ODI) and Other Financial Institutions (OFI) 2/ 5/								
Net foreign assets	**4,965**	**4,731**	**4,860**	**5,190**	**5,380**	**5,552**	**5,740**	**5,949**
Net domestic assets	**32,666**	**36,154**	**35,100**	**37,395**	**38,097**	**38,736**	**39,228**	**39,749**
Assets held at the BCE, net	1,757	2,502	2,520	2,793	2,962	3,124	3,182	3,246
Credit to the nonfinancial public sector, net	1,107	1,029	479	-320	-320	-320	-399	-399
Of which: central government, net	1,284	1,336	786	-13	-13	-13	-93	-93
Credit to the private sector	39,980	44,524	43,731	47,317	48,842	50,427	52,190	54,151
Other items, net	-10,179	-11,901	-11,630	-12,395	-13,387	-14,495	-15,745	-17,248
Liabilities	**37,631**	**40,885**	**39,960**	**42,585**	**43,476**	**44,288**	**44,968**	**45,699**
Of which: Private sector deposits	37,631	40,885	39,960	42,585	43,476	44,288	44,968	45,699
III. Consolidated Banking System								
Net foreign assets	**8,867**	**9,359**	**8,205**	**9,541**	**11,501**	**13,046**	**15,078**	**15,966**
Net domestic assets	**28,915**	**31,661**	**31,879**	**33,173**	**32,106**	**31,376**	**30,026**	**29,871**
Credit to the nonfinancial public sector, net	-979	-1,538	-141	-1,157	-2,447	-3,619	-4,777	-5,337
Credit to the private sector	39,998	44,537	43,742	47,329	48,854	50,440	52,203	54,165
Other items, net	-10,104	-11,339	-11,722	-12,999	-14,301	-15,446	-17,400	-18,957
Liabilities	**37,782**	**41,020**	**40,084**	**42,714**	**43,608**	**44,422**	**45,104**	**45,837**
Memorandum items:								
Credit to the private sector (percent change, yoy) 6/	14.9	11.3	-1.8	8.2	3.2	3.2	3.5	3.8
Deposits of the private sector (percent change, yoy) 6/	5.0	8.6	-2.3	6.6	2.1	1.9	1.5	1.6
Broad money (M2) (percent change, yoy)	5.7	8.0	-5.5	6.6	2.5	2.2	2.0	2.2
Broad money velocity	2.0	1.9	1.8	1.7	1.7	1.6	1.6	1.6
ODI and OFI's reserves at the central bank as a share of liabilities (percent) 2/ 3/	12.9	10.7	10.7	10.7	10.7	10.7	10.4	9.7
Credit to the private sector (percent of GDP)	37.2	41.5	47.0	47.7	47.5	47.6	47.7	47.7
Liabilities (percent of GDP)	35.1	38.2	43.1	43.0	42.4	41.9	41.2	40.4

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/ Reserves of OFIs includes deposits of *Corporación Financiera Nacional,* COSEDE, BIESS, and a transitory account for the payments system.
4/ Includes monetary deposits, *Titulos del Banco Central de Ecuador*, stabilization bonds, and accounts payable.
5/ OFI comprises *Corporación Financiera Nacional.*
6/ Consolidated banking system.

Table 7. Ecuador: Financial Soundness Indicators [1/]

	2015	2016	2017	2018	2019	Q2 2020
	(In percent, unless otherwise indicated; end-of-period values)					
Capital Adequacy						
Regulatory capital to risk-weighted assets (CAR)	14.4	13.9	13.7	13.4	13.5	14.1
Asset Quality and Distribution						
Nonperforming loans to gross loans	3.7	3.5	3.0	2.6	2.7	2.8
Provisions to nonperforming loans	187.1	189.5	234.4	247.7	225.6	252.8
Gross loans to assets	86.2	80.0	84.4	86.0	87.8	86.0
Earnings and Profitability						
Return on average assets (ROA)	0.9	0.6	1.0	1.4	1.4	0.6
Return on average equity (ROE)	9.0	6.7	10.4	13.6	13.9	5.7
Interest margin to assets	0.8	0.4	0.9	1.6	1.4	0.4
Noninterest expenses to spread	87.4	92.6	85.0	76.9	78.5	92.3
Liquidity						
Liquid assets to short-term liabilities	29.6	33.9	29.4	27.9	26.0	28.8
Deposit to loan ratio	126.1	137.0	121.9	111.8	109.5	112.4

Source: Superintendency of Banks.
1/ Values refer to private banks and *Banco del Pacifico*.

Table 8. Ecuador: Indicators of Fund Credit, 2020–2030
(in percent of GDP, unless otherwise indicated)

	Projections										
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Existing and prospective Fund arrangements					(millions of SDRs)						
Disbursements 1/	3,310	1,065	710	0	0	0	0	0	0	0	0
Stock of existing and prospective Fund credit	4,419	5,386	6,096	5,925	5,521	4,738	3,901	2,963	2,026	1,142	373
Obligations	57	214	147	334	568	959	983	1048	1010	918	780
Principal	33	98	0	172	403	783	837	938	938	884	769
Charges/interest 2/	25	115	147	162	165	176	146	110	72	34	11
Obligations, relative to key variables					(percent)						
Quota	8.2	30.6	21.0	47.8	81.4	137.5	140.9	150.2	144.8	131.5	111.8
Gross domestic product	0.1	0.3	0.2	0.4	0.7	1.2	1.2	1.2	1.1	1.0	0.8
Gross international reserves 3/	3.2	8.9	4.0	7.2	9.6	15.1	14.9	15.3	13.9	11.2	8.8
Exports of goods and services	0.4	1.3	0.9	1.9	3.1	5.1	5.0	5.1	4.7	4.1	3.4
Revenues of the NFPS	0.3	0.9	0.6	1.2	2.0	3.3	3.2	3.3	3.1	2.7	2.2
External debt service	0.6	3.0	1.8	3.8	6.1	9.9	9.5	10.2	9.8	19.5	16.8
Fund credit outstanding, relative to key variables					(percent)						
Quota	633.4	772.0	873.8	849.2	791.4	679.1	559.1	424.7	290.3	163.7	53.4
Gross domestic product	6.5	7.4	8.1	7.7	6.9	5.8	4.6	3.3	2.2	1.2	0.4
Gross international reserves	244.0	225.3	167.0	128.2	93.2	74.4	59.3	43.3	27.8	14.0	4.2
External debt	10.8	12.9	14.1	13.3	12.1	10.5	9.3	7.3	5.1	2.9	1.0
Memorandum items:											
Exports of goods and services (US$m)	20,599	21,884	22,922	23,933	25,015	26,101	27,177	28,259	29,506	30,768	31,978
External debt (US$m)	56,004	57,268	59,133	61,243	62,557	62,213	57,648	56,236	54,944	54,113	53,013
Quota (SDRm)	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7	697.7
Gross international reserves (US$m)	2,475	3,275	5,007	6,345	8,151	8,787	9,082	9,433	10,061	11,281	12,197
Gross international reserves (% ARA metric)	13	17	24	30	38	40	43	45	48	53	57
NIR, program definition (US$m)	-7,848	-8,679	-8,039	-6,550	-4,134	-2,199	-756	825	2,682	5,055	6,964
Nominal GDP (US$m)	93,078	99,247	102,803	106,026	109,550	113,470	117,661	122,126	126,756	131,532	136,521
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	0.7

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

1/ An RFI disbursement of 67% of quota took place in May 2020.

2/ Using the GRA rate of charge of 1.084 percent as of August 27, 2020 for projected charges/interest.

3/ GIR excludes non-liquid and encumbered assets.

Table 9. Ecuador: Proposed Access and Phasing Under the Extended Fund Facility (EFF) 1/

					Percent of quota 1/	
Review	Availability Date	Action	SDR million	US$ million 2/	Disbursement	Cumulative
	September 30, 2020	Board approval of EFF	1420.0	2000.0	203.5	203.5
First Review	December 15, 2020	Observance of continuous and end-September 2020 performance criteria, completion of first review	1420.0	2000.0	203.5	407.1
Second Review	April 15, 2021	Observance of continuous and end-December 2020 performance criteria, completion of second review	284.0	400.0	40.7	447.8
Third Review	August 15, 2021	Observance of continuous and end-April 2021 performance criteria, completion of third review	284.0	400.0	40.7	488.5
Fourth Review	December 15, 2021	Observance of continuous and end-August 2021 performance criteria, completion of fourth review	497.0	700.0	71.2	559.7
Fifth Review	April 15, 2022	Observance of continuous and end-December 2021 performance criteria, completion of fifth review	213.0	300.0	30.5	590.2
Sixth Review	August 15, 2022	Observance of continuous and end-April 2022 performance criteria, completion of sixth review	213.0	300.0	30.5	620.8
Seventh Review	December 1, 2022	Observance of continuous and end-August 2022 performance criteria, completion of seventh review	284.0	400.0	40.7	661.5
Total			**4615.0**	**6500.0**	**661.5**	

Source: IMF staff estimates

1/ Ecuador's quota is SDR 697.7 million.

2/ Based on the program exchange rate.

Annex I. The 2019 EFF Program: Key Objectives and Outcomes[1]

1. The 2019 three-year EFF – which disbursed US$1.4 billion out of the 4.2 billion originally envisaged - was designed to assist Ecuador's reform agenda. The Government's policy plan aimed at restoring growth, putting debt on a firmly downward path, building reserve buffers and restore international competitiveness, while also making substantive improvements to the social assistance system. Specifically, the plan was built on four pillars:

I. *Strengthening the institutional foundations of dollarization*. This required efforts on several fronts: (a) restoring prudence to fiscal policy by reducing the fiscal deficit and putting the public debt on a downward path; (b) strengthening institutional framework for the Central Bank by prohibiting all direct and indirect central bank financing of the government and introducing a new legal framework which requires the central bank to cover all its liabilities vis-à-vis banks with international reserves; and (c) boosting resilience of the financial system by improving financial oversight and crisis preparedness.

II. *Boosting competitiveness and job creation*. The Government's plan included a labor market reform that allows for less-rigid labor contracts and the introduction of a framework for public private partnerships to attract private capital and to allow private sector companies to take over the operations of certain public functions as concessions.

III. *Promoting shared prosperity and protecting the poor and most vulnerable*. The plan included measures to protect vulnerable groups through an increase in social assistance spending of 0.6 percentage points of GDP (or by about 100 percent compared to the level of 2018). This allowed to extend the coverage of, and increase the nominal level of benefits under, the existing conditional cash transfer program, programs to support the disabled and the elderly.

IV. *Restoring transparency and good governance to public sector operations*. The authorities planned to bring the fiscal reporting in line with international standards and to increase transparency in the oil sector. Moreover, to support anticorruption efforts, the authorities planned to introduce measures to strengthen the effectiveness of the AML/CFT framework.

2. During the short-lived program, the authorities advanced in some of the program objectives. In particular, the authorities: (i) improved public finances by consolidating the non-oil primary balance with subsidies by 1.3 percentage points of GDP in 2019 –the consolidation was led by capital expenditure cuts and reductions in public employment; (ii) submitted an organic budget law with fiscal rules and a debt anchor, and implemented other reforms to strengthen the framework for fiscal rules and public financial management; (iii) strengthened the institutional foundations of the central bank, mainly through a regulation prohibiting monetary financing; (iv) strengthened the social safety net by increasing spending on social assistance, developing a social assistance action plan, and publishing updated eligibility thresholds for social assistance; and (v)

[1] Prepared by Matteo Ghilardi.

initiated reforms on transparency and governance, including by submitting an anticorruption legislation.

3. Overall, implementation was mixed, complicated by a challenging political environment, and shortcomings in institutional capacity, which resulted in a misreporting incident. The lack of a stable political majority has led to long delays and shortfalls in implementing key commitments under the EFF, such as a deeper tax and central bank reforms. At the same time, the misreporting episode highlighted technical capacity constraints and limited inter-agency coordination, which were the underlying causes for deficiencies in the collection and compilation of fiscal statistics. The misreporting incident resulted in the cancelation of the 2019-22 EFF in April 2020.

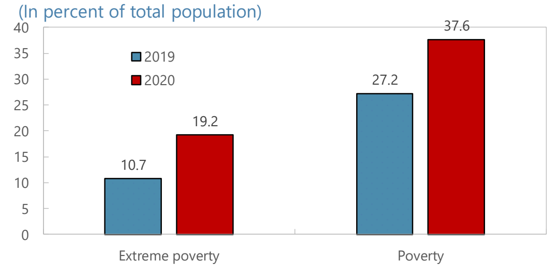
4. The authorities also took measures this year to address the problems highlighted in the misreporting report. In this context, the authorities: (i) reorganized the MEF to establish specific responsibilities for fiscal statistics and a system of check and balances for consistency and programming purposes; (ii) established and are operating a working group to coordinate the relevant information between the MEF and the central bank; (iii) provide fiscal data in a new detailed format, consistent with TA recommendations; (iv) revised and published aggregated and detailed fiscal data for 2019 onwards and established a calendar for historical revisions; and (v) prepared and distributed brief guidelines for the compilers of fiscal statistics.

5. More recently, despite the ongoing pandemic, the authorities have continued making progress on the reform agenda in the absence of a Fund-supported program. Notwithstanding a challenging domestic and global environment, the authorities: (i) adopted amendments to the organic budget law, which will help restore fiscal prudence by strengthening fiscal management practices, provide clear debt anchors, and clarify the fiscal rules framework; (ii) implemented an ambitious fuel subsidy reform, which is expected to generate significant savings over the medium term; and (iii) further rationalized expenditures, which would help meeting the fiscal consolidation targets.

Annex II. Social Assistance: Gaps and Way Forward[1]

1. **The COVID-19 pandemic has laid bare the limitations of the social protection system in Ecuador.** The health crisis, along with plummeting oil prices and a sharp drop in global demand, has had a devasting impact on Ecuador's economy, pushing a significant share of the population into poverty. The sharp drop in labor incomes triggered by the economic downturn, weak social insurance (reflecting high labor market informality) and low coverage of social assistance, leading to large increases in poverty and income inequality.[2] UNICEF estimates suggest that the economic downturn could push an additional 1.8 million people (450,000 families) into poverty in 2020, increasing the poverty rate from 27.2 percent to about 37.6 percent, and extreme poverty from 10.7 percent to about 19.2 percent (Figure 1).[3] The evidence suggests that these effects are (i) driven by the increase in the number of families below the poverty line; (ii) long lasting, and (iii) more pronounced in families with children.[4]

Figure 1: Ecuador: The Impact of COVID-19 Shock on Poverty
(In percent of total population)



Source: Encuesta Nacional de Empleo, Desempleo y Subempleo-ENEMDU and UNICEF – Inclusion calculations.

2. **The authorities have introduced temporary measures to protect vulnerable households affected by both the health and economic crisis, but the level of COVID-19 related social assistance is below that of most countries in Latin America.** In April the authorities announced a temporary cash transfer of $120 ("Bono de Protección Familiar por Emergencia"), with monthly payments of $60 in May and June, for 400,000 vulnerable families that were part of the social registry but were not enrolled in any social assistance program. This temporary assistance was extended to an additional 550,000 vulnerable families in June. Even with this extension, Ecuador's support to vulnerable households during the pandemic lags behind that of most Latin American countries, both in terms of the share of the population receiving COVID-19 related cash transfers and the spending on these transfers (Figure 2).

[1] Prepared by Fernanda Brollo.

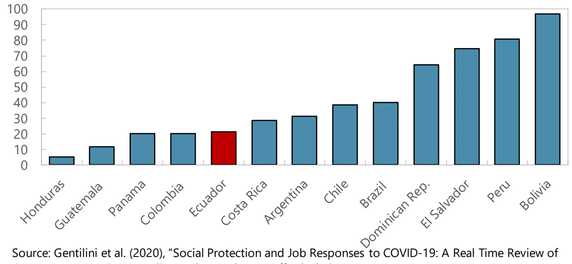
[2] The authorities temporarily relaxed the eligibility criteria for unemployment benefits in response to the crisis.

[3] These estimates include additional income from the emergency temporary cash transfers "Bono de Protección Familiar por Emergencia" of $120 to 950,000 families.

[4] The shock will hit harder family with children, whom were already in disadvantage compared to those without them. Furthermore, the poverty gap for these families will increase by 50 percent (from 8.1 percent to 12 percent). Multidimensional poverty among households with children will increase from 31.9 percent to 44 percent and extreme multidimensional poverty will almost double (from 12.9 percent to 23.4 percent). Simulations based on multidimensional poverty shows an increase in non-attendance school rates and child labor (from 8.5 percent to 13.0 percent and from 5.8 percent to 8.0 percent, respectively), which increase the vulnerability of households with children. The COVID-19 shock is estimated to represent a loss of 12 years in the road to eradicate poverty. In the case of households with children the loss of years would increase to 16.8 year.

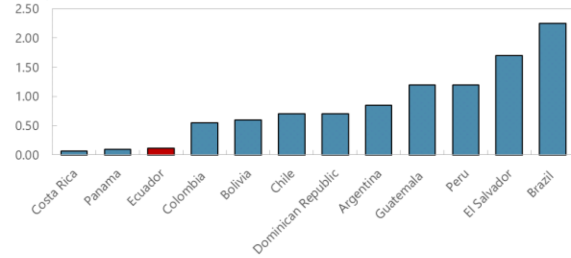
Figure 2. Ecuador and LATAM: COVID-19 Related Cash Transfers to Vulnerable Households

Coverage 1/
(In percent)



Source: Gentilini et al. (2020), "Social Protection and Job Responses to COVID-19: A Real Time Review of Country Measures"; IMF policy tracker; and IMF staff calculations.
1/ Coverage is defined as share of households covered by COVID-19 related cash transfers.

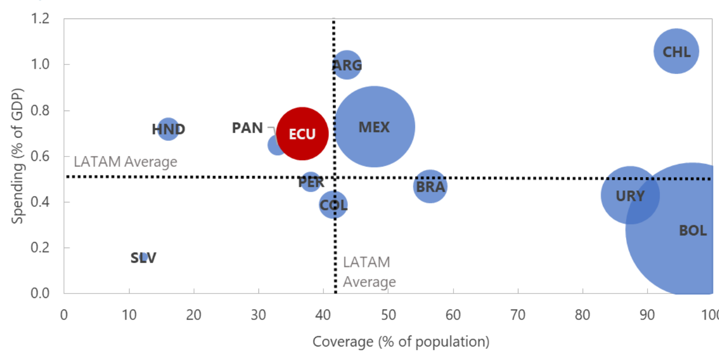
Spending
(In percent of GDP)



Source: Gentilini et al. (2020), "Social Protection and Job Responses to COVID-19: A Real Time Review of Country Measures"; IMF policy tracker; and IMF staff calculations.

3. **While temporary measures can help cushion vulnerable households from the impact of the shocks, a more fundamental reform is needed to expand the coverage of cash transfer programs and improve their targeting.** Spending on cash transfer programs in Ecuador is above the average for Latin America, but coverage of the poor is relatively low (Figure 3). This reflects benefit generosity and/or leakages to the non-poor. Overall, the benefit generosity is adequate. However, leakages to the non-poor is high. Given limited fiscal space, to increase coverage of the poor and reduce poverty, leakage to the non-poor may be gradually eliminated over time. However, eliminating leakages in the system requires caution due to recent changes in the composition of the poor as a result of the covid-19 shock. Therefore, updated information on family characteristics is crucial when designing the strategy to strengthening the social assistance system.

Figure 3: Ecuador and LATAM: The Impact of Social Assistance Cash Transfer Programs on Poverty 1/
(In percent)



Sources: Aspire -- The Atlas of Social Protection; IMF Social Protection tool; and IMF staff calculations.
1/ **The size of the bubbles denotes the impact of cash transfer programs on poverty headcount reduction**, calculated as follows: (poverty headcount pre-transfer – poverty headcount post-transfer)/(poverty headcount pre-transfer). Values are computed using the most recent available year for each country over 2008-2019. **Coverage** is defined as the percentage of the population in the bottom quintile of the income distribution covered by cash transfer programs. **Spending** is defined as total spending with cash transfers social assistance programs as percent of GDP. Cash transfer programs exclude social pensions.

4. **The authorities are committed to strengthening the safety net by expanding coverage of cash transfer programs**. A strong social safety net with high coverage of the poor is key not only to reduce poverty and shield vulnerable households from the effects of shocks, but also to readily deploy compensatory measures to mitigate the adverse impact of the much-needed fiscal consolidation. In collaboration with the World Bank, the authorities have developed a strategy to increase the coverage of social assistance programs from the current 37 percent of families in the bottom three deciles of the income distribution to 80 percent by December 16, 2021. Most of this increase is planned to happen by April 2021—the program includes an indicative target on the number of poor families covered under social assistance programs to help the authorities track progress toward their quantitative objective. Meeting this goal requires updating the information in

the Social Registry in order to identify families below the poverty line. To this end, the authorities have introduced measures to monitor the progress in updating the social registry and expanding coverage, including the operationalization of a committee composed of members of the Board of Directors of the Social Registry Unit (in the Presidential Secretariat), the General Secretariat of the Presidency, the Ministry of Economy and Finance, Secretariat "*Plan Todo Una Vida*", and as a participant, the Ministry of Economy and Social Inclusion. To the date, around 386,000 new poor families have their registry updated, and eligible to receive benefits. Ongoing progress with the interviews and household surveys, will allow a much higher number of new poor families with information validated in the social registry in the coming months.

Box 1. The Social Protection System in Ecuador

The social protection system in Ecuador focuses mostly on social assistance programs, mainly cash transfer programs and social pensions, due to high labor market informality. Social protection instruments generally fall into three categories: (i) social safety net (or social assistance); (ii) social insurance; and (iii) labor market programs. Social assistance programs are noncontributory interventions to help individuals and households cope with chronic poverty, destitution, and vulnerability. Social insurance programs are contributory interventions to help individuals manage sudden changes in income because of old age, sickness, or disability. Labor market programs are designed to protect individuals against loss of income from unemployment or to help individuals acquire skills and connect them to labor markets. The social protection system in Ecuador focuses on social assistance, due to the high degree of labor market informality which limits social insurance instruments. The social assistance system consists of a few conditional and unconditional cash transfer programs and complementary social services implemented by the Ministry of Economic and Social Inclusion (MIES). Cash transfers programs provide income support targeted to:

i) low - income households with children under 18 years old (Bono de Desarrollo Humano, BDH);

ii) poor households with the potential to carry out productive and income - generating activities (Crédito de Desarrollo Humano, CDH);

iii) low - income seniors over 65 years old (Pensión Adulto Mayor and Pensión Mis Mejores Años); and

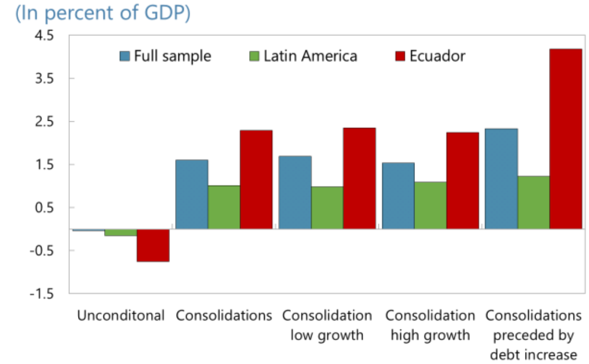
iv) vulnerable people with disabilities (Pensión para personas con discapacidad, Pensión Toda Una Vida and Bono Joaquin Gallegos Lara).

Annex III. Realism of Planned Fiscal Adjustment[1]

This annex examines the realism of the size of the fiscal adjustment embedded in the program's macroeconomic framework, by comparing Ecuador's recent history of fiscal adjustment to other developing countries. It provides evidence that (1) Ecuador's fiscal stance tends to adjust more to increases in public debt compared to its peers in normal times; and (2) its fiscal adjustment in response to increases in debt was even stronger under stress.

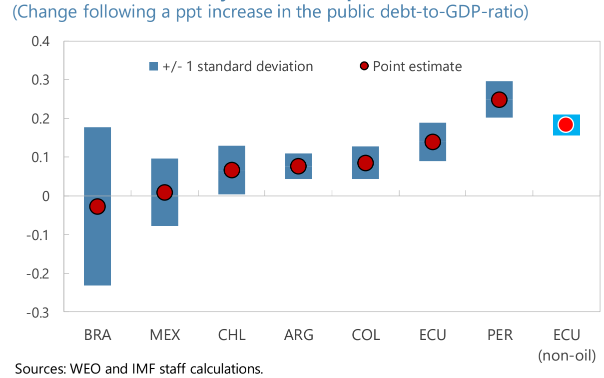
1. **Ecuador has historically adjusted its primary balance more than other developing countries on average, including during consolidation episodes following an increase in public debt.** We compare changes in primary balances in Ecuador to those in other developing countries', using 3 alternative measures. First, we consider the unconditional cumulative change in the primary balance over a 3-year rolling window. Second, we restrict the sample to consolidation episodes only—defined as 3-year periods for which the primary balance improves between the first and last year. Third, we made a distinction between fiscal consolidation during low growth and high growth episodes, with low/high growth episodes for each country defined as episodes during which average growth is lower/higher than the average growth in the sample for that country. Fourth, we focus on consolidation episodes that were preceded by an increase in public debt by at least 3 ppts of GDP.[2] A median improvement in the primary balance of 2.3 ppts of GDP during consolidation episodes in Ecuador is higher than the 1.6 ppts of GDP improvement on average in developing countries over the past two decades and more than double the 1 ppt consolidation in the sub-sample of Latin American countries.[3] Consolidation in Ecuador is on average also higher than that in other developing countries using the other two measures.[4]

Median Cumulative Change in the Primary Balance
(In percent of GDP)



Sources: WEO (April, 2020) and IMF staff calculations

Ecuador and LAC: Primary Balance's Response to Debt
(Change following a ppt increase in the public debt-to-GDP-ratio)



Sources: WEO and IMF staff calculations.

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[1] Prepared by Constant Lonkeng Ngouana.

[2] The results are robust to changes in the criterion for fiscal consolidation and the threshold for debt increases.

[3] The empirical median primary balance for consolidations in episodes of low growth is similar to the one obtained for consolidations in high growth episodes. This result, consistent with the country-specific estimates of fiscal reaction functions presented below, suggests that fiscal policy has been on average insensitive to the business cycle in developing countries, likely due to limited size of automatic stabilizers.

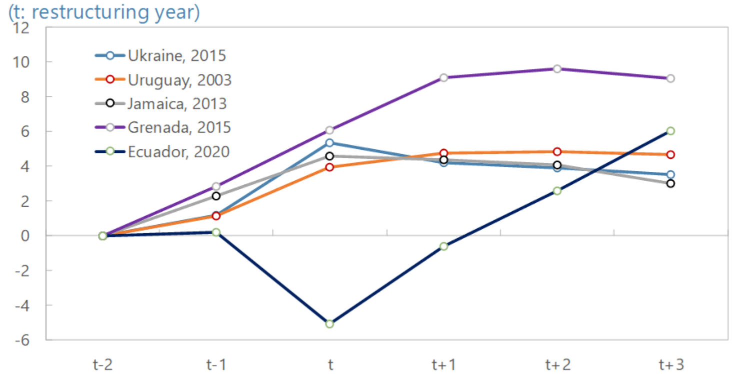
[4] The number of observations/episodes for computing the moments of the distribution of the primary balance for Ecuador is inevitably very small compare to the number of observations obtained when countries are pooled (full sample and the Latin America grouping).

Ecuador stands out even more when looking at the 75th percentile of the distribution rather than the average.[5]

2. Country-specific estimates of fiscal policy reaction suggest that Ecuador has typically reacted more strongly to public debt increases than all LA-6 countries but Peru.[6] Estimates suggest that the primary balance in Ecuador increases on average by 0.13 ppt of GDP in response to a one ppt increase in the public debt-to-GDP ratio, second only to Peru in the sample (0.25 ppts of GDP).[7,8,9] Given Ecuador's heavy reliance on oil revenues, we also estimated a fiscal reaction function using the non-oil primary balance. The estimated coefficient is slightly higher at 0.18 (second text chart).

3. Looking at the episodes of stress, the fiscal adjustment path embedded in the program scenario appears in line with that observed in countries that undertook debt operations in the past 20 years. Emerging market countries have generally implemented strong fiscal adjustments around debt restructuring episodes since the early 2000s, except when the starting primary balance was already relatively high (e.g., Jamaica in 2013). Ecuador's cumulative adjustment under the current baseline scenario (5 ppts of GDP over 6 years and 2.9 ppts of GDP over the first 3 years after restructuring) would be broadly in line with that of other restructuring cases in the sample.

Cumulative Change in Primary Balance in Restructurings
(t: restructuring year)



Sources: WEO and IMF staff calculations.

4. The experience from the two recent major oil price shocks also points to a possibility of large fiscal correction in Ecuador after the current shocks.[10] There is some evidence that the nature of the oil shock might matter for how Ecuador's fiscal policy reacts. While the country recovered relatively fast from a temporary (demand-driven) oil price shock around the global financial crisis of 2008 with little fiscal adjustment, the adjustment in the fiscal position was

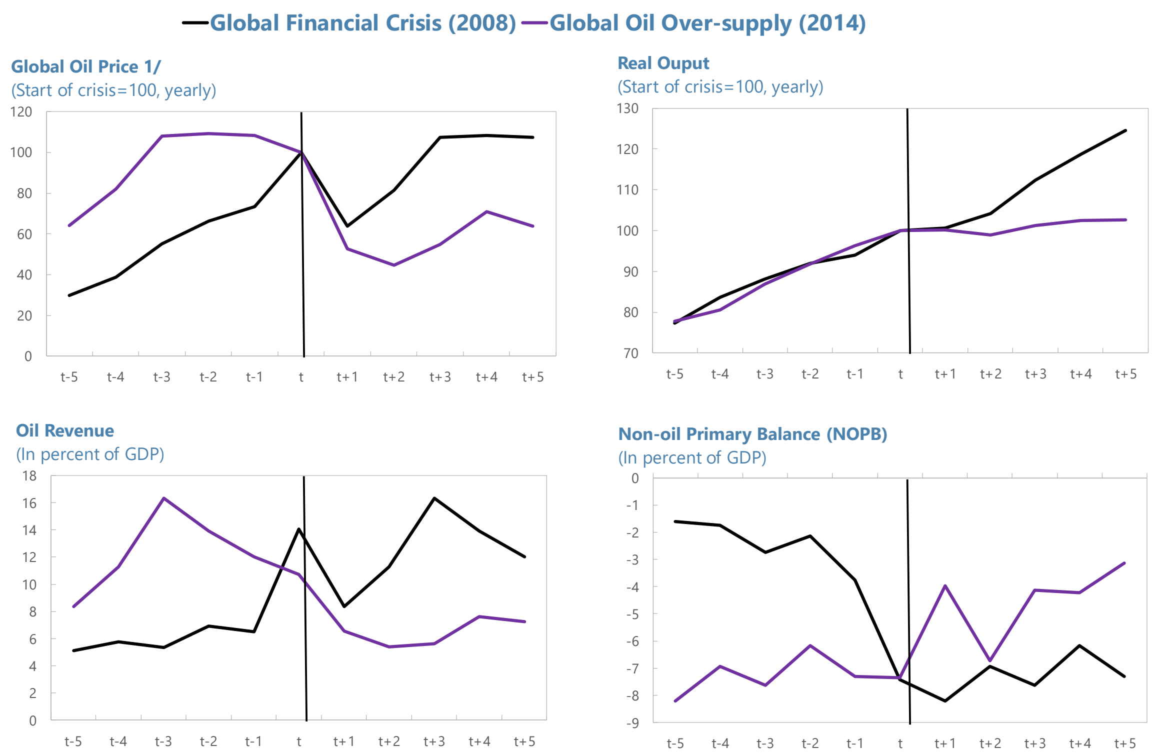
[5] The numbers for Ecuador relate to the broader non-financial public sector as opposed to a narrower coverage for some countries in the sample.
[6] LA-6 is made of Argentina, Brazil, Chile, Columbia, Mexico and Peru.
[7] We estimate the following Bohn equation, separately for Ecuador and each LA-6 country, to measure the response of the primary balance to public debt:

$$pb_t = \alpha + \rho d_{t-1} + \beta ygap_t + \varepsilon_t$$

where *pb* is the primary balance in percent of GDP, *d* is the debt-to-GDP ratio, and *ygap* is the output gap. We use robust standard errors.
[8] The smaller coefficient on debt in Chile may reflect the fact the debt has not been high enough historically to warrant a tightening in the primary balance.
[9] Controlling for the output gap in the regressions, we find that fiscal policy has not been counter-cyclical in the sample, with the exception of Chile and Peru.
[10] The multi-facetted nature of the current shock, uncertainties around it and initial conditions may reduce the information content of historical episodes in thinking about the current context.

pronounced following a more permanent (global over-supply) shock of 2014. At that time, public debt increased by 7 percentage points followed by an improvement in the non-oil primary balance by 3.4 percentage points of GDP in 2015 (elasticity of 0.5). The gains were unfortunately eroded in 2016 when the country was struck by a powerful earthquake, which deteriorated fiscal balances. Since the current oil price shock likely embeds a permanent component—oil futures for 2025 remain more than 20 percent below spot oil prices pre-shock—a large correction in Ecuador's fiscal position appears warranted.

Ecuador: Adjustment to Recent Oil Price Shocks



Sources: WEO, Bloomberg, and IMF staff calculations.
1/ t is the year in which the oil shock started.

Annex IV. Debt Sustainability Analysis[1]

Under baseline projections, Ecuador's public debt is assessed to be sustainable with high probability, thanks to the successfully concluded bond exchange, specific and credible financing assurances on financing/debt relief from official bilateral creditors, other committed financing and good prospects for additional contributions from international financial institutions (IFIs), and the envisaged fiscal consolidation. Public debt is expected to peak at 68.9 percent of GDP in 2020 and decline to 56.1 percent of GDP in 2025. Gross financing needs are about 16.1 percent of GDP in 2020, but they are forecasted to retreat to 4.6 percent of GDP by 2025, largely on the back of the debt restructuring operation. Despite the improvements in the debt dynamics, the declining debt path is vulnerable to a growth and primary balance shocks.

1. Definition and Debt Profile. Public-sector debt includes the obligations of the non-financial public sector (general government and non-financial sector state-owned enterprises). Under this measure, public debt more than doubled between 2012 and 2019 (from 17.5 to 51.8 percent of GDP).

2. Macroeconomic and Fiscal Assumptions. Growth in 2020 is forecasted at -11 percent while CPI inflation is expected to hover around zero. Growth is expected to recover in the medium term and reach 2.5 percent by 2025 - in line with the economy's potential – while CPI inflation is expected to converge to 1 percent. Thanks to the envisaged fiscal consolidation, the fiscal position is projected to improve gradually to reach a primary surplus of about 4.5 percent of GDP by 2025. This is conditional on continuous policy efforts resulting in an improvement of the non-oil primary balance with subsidies of 5.5 percent of GDP between 2019 and 2025. On the financing side, the framework envisages budget support from IFIs of US$3.6 billion in 2020, US$3.2 billion in 2021, and US$1.8 billion in 2022, excluding the EFF financing from the IMF; financing from China of US$1.7 billion in 2020 and $0.7 billion in 2021, and market access of US$0.5-2 billion from 2022 onwards. The framework includes i) the debt restructuring operation of external private bonds concluded on August 31, which lowered interest payments by about US$5.7 billion over 2020-25 and amortizations by US$5.6 billion over 2022-25, ii) the reprofiling of credit lines with CDB that was concluded on August 5, and iii) the reprofiling of credit lines with Eximbank on September 16, the latter two of which generate cumulative cash flow relief of about US$815 million in 2020-21.

3. Baseline Scenario. In the baseline scenario, public debt is projected to decline from its projected peak at end-2020 of 68.9 percent of GDP to 56.1 percent by 2025, implying that the public debt-to-GDP ratio will remain below the critical threshold for emerging economies of 70 percent of GDP. This is conditional on the success of the bond exchange offer and on a timely implementation of the envisaged fiscal consolidation package. Because of these factors, gross financing needs are also expected to decline significantly over the medium term, as they are projected to fall from 16.1 percent of GDP in 2020 to 4.6 percent of GDP by 2025. As a result, gross financing needs do not breach the low-risk threshold of 15 percent of GDP in the baseline scenario after 2020 (the heatmap

[1] Prepared by Matteo Ghilardi, with inputs from Leandro Medina.

reflects the 2020 projection of 16.1 percent, which is not affected by the restructuring). The realism analysis shows that the projected fiscal adjustment is in the top quartile when compared to experience of other countries (see Annex III on Ecuador's recent history of fiscal adjustment, comparing it to other developing countries, including LA-6 peers). The cyclically-adjusted primary fiscal adjustment over any of the three years during the projection horizon is above the threshold of 3 percent of GDP, while the average of the cyclically-adjusted primary balance for any consecutive 3-year period during the projection horizon is greater than the threshold of 3.5 percent of GDP.

4. Stress Tests. The debt restructuring operation and the fiscal consolidation path would reduce significantly debt and gross financing risks in the short- and medium-term. However, despite the improvements in the debt dynamics, the declining debt path is vulnerable to growth and a primary balance shock. The growth shock would bring the debt-to-GDP ratio to 74.3 percent in 2022 before declining below the critical threshold for emerging economies of 70 percent of GDP and reach 65 percent in 2025. Under current assumptions, public debt does not appear vulnerable to a real interest shock or RER shock, meaning that under these shocks the critical threshold is not crossed. Gross financing needs do not breach the low-risk threshold of 15 percent of GDP under any of the stress test scenario.

5. Risks and Vulnerabilities. Risks are tilted on the downside, which are enhanced by the global economic and financial uncertainty. Key near-term risks include a stronger-than-envisaged impact of the COVID pandemic and/or a more protracted recovery at the domestic or global level, which would result in lower fiscal revenues and higher fiscal costs. The framework also hinges on a steadfast implementation of the policy agenda which is needed to generate the needed fiscal savings. Any lags in mobilizing revenues, and containing and rationalizing spending could ultimately result in higher financing needs. A delay in market access, and/or lower support from bilateral and/or multilateral creditors would present substantive challenges, and potentially open financing gaps. 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 spreads has increased once-more the market perception risk to high. At about 73 percent of the total debt, non-residents' holdings of Ecuador's public debt are high but about half of external debt is owed to official creditors and therefore reduces this as a source of vulnerability.

6. External Sustainability Analysis. The external debt-to-GDP is expected to increase to 51.7 by end-2020, primarily due to the effects of the current crisis on the current account balance and growth. However, in the medium-term, external debt is projected to decrease to 44.1 percent of GDP by 2025, supported by an improvement in the external position under program policies, especially under the consolidation of the fiscal stance and efforts to raise competitiveness by increasing productivity and reducing labor costs. The non-interest current account is expected to improve to a surplus of 3.4 percent of GDP by 2025, from a surplus of 1.2 in 2020 (well in excess of the 0.3 percent of GDP deficit needed to stabilize external debt). The external debt trajectory is most sensitive to the non-interest current account shock (e.g. terms of trade shock). While a large real exchange rate depreciation would create unstable debt dynamics, it is highly improbable scenario in Ecuador's dollarized system.

Figure 1. Ecuador: Public Debt Sustainability Analysis (DSA) – Baseline Scenario

(in percent of GDP unless otherwise indicated)

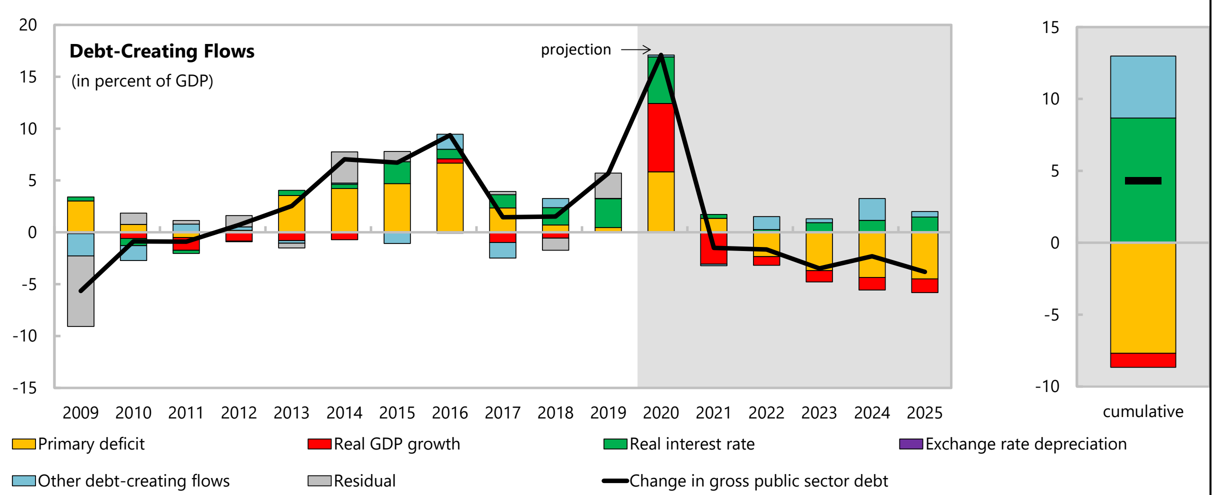
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2009-2017 [2/]	2018	2019	2020	2021	2022	2023	2024	2025
Nominal gross public debt	26.6	46.1	51.8	68.9	67.4	65.8	62.3	60.0	56.1
Public gross financing needs	9.2	10.5	10.3	16.1	8.1	4.2	4.0	3.2	4.6
Net public debt	21.6	40.2	45.9	61.9	61.0	58.3	54.7	51.1	47.6
Real GDP growth (in percent)	3.1	1.3	0.1	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation (GDP deflator, in percent)	2.9	1.8	-0.2	-2.7	1.8	2.3	1.4	1.3	1.3
Nominal GDP growth (in percent)	6.1	3.1	-0.1	-13.4	6.6	3.6	3.1	3.3	3.6
Effective interest rate (in percent) [4/]	4.6	5.7	5.9	5.2	2.4	2.7	2.9	3.2	3.8

As of September 18, 2020		
Sovereign Spreads		
EMBIG (bp) 3/		950
5Y CDS (bp)		n.a
Ratings	Foreign	Local
Moody's	Caa3	Caa3
S&Ps	B-	B-
Fitch	B-	B-

Contribution to Changes in Public Debt

	Actual			Projections							
	2009-2017	2018	2019	2020	2021	2022	2023	2024	2025	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	2.3	1.5	5.7	17.1	-1.5	-1.7	-3.5	-2.3	-3.8	4.3	
Identified debt-creating flows	2.3	2.7	3.2	17.1	-1.5	-1.7	-3.5	-2.3	-3.8	4.3	
Primary deficit	2.8	0.7	0.5	5.8	1.4	-2.3	-3.7	-4.3	-4.5	-7.7	0.7
Primary (noninterest) revenue and grants	35.0	35.3	33.4	30.1	31.6	34.6	35.2	35.5	35.5	202.6	
Primary (noninterest) expenditure	37.8	36.0	33.9	35.9	33.0	32.2	31.5	31.2	31.1	194.9	
Automatic debt dynamics [5/]	0.0	1.1	2.8	11.1	-2.7	-0.6	-0.2	-0.1	0.2	7.7	
Interest rate/growth differential [6/]	0.0	1.1	2.8	11.1	-2.7	-0.6	-0.2	-0.1	0.2	7.7	
Of which: real interest rate	0.5	1.7	2.8	4.5	0.4	0.3	0.9	1.1	1.5	8.7	
Of which: real GDP growth	-0.5	-0.6	0.0	6.6	-3.1	-0.8	-1.1	-1.2	-1.3	-1.0	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	-0.4	0.9	0.0	0.2	-0.2	1.3	0.4	2.1	0.5	4.3	
Deposits drawdown and privatization receipts (negative sign)	-0.4	0.9	0.0	0.2	-0.2	1.3	0.4	1.5	0.0	3.2	
Contingent liabilities	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	-1.2	2.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	



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. It also includes the issuance of domestic debt for the asset swap operation with the central bank.

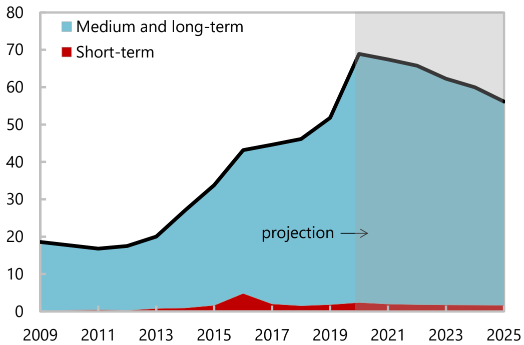
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

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

Composition of Public Debt

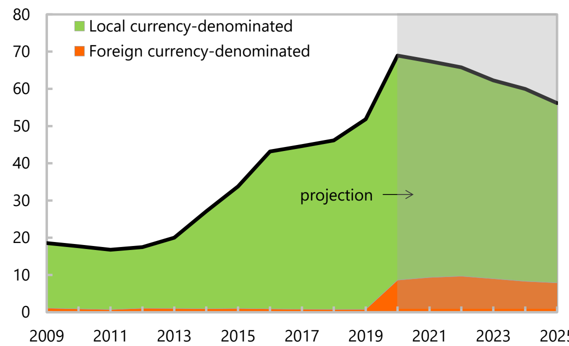
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

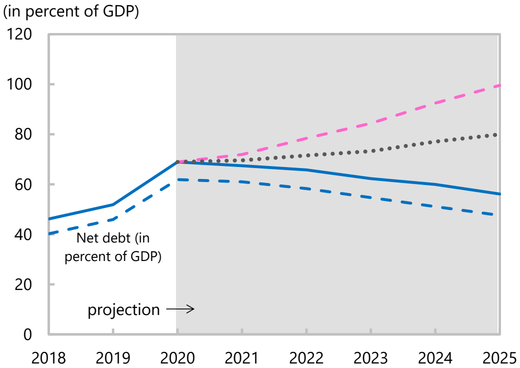


Alternative Scenarios

Baseline   Historical   Constant Primary Balance

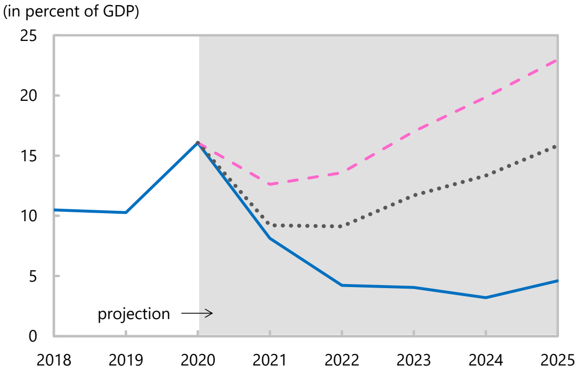
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

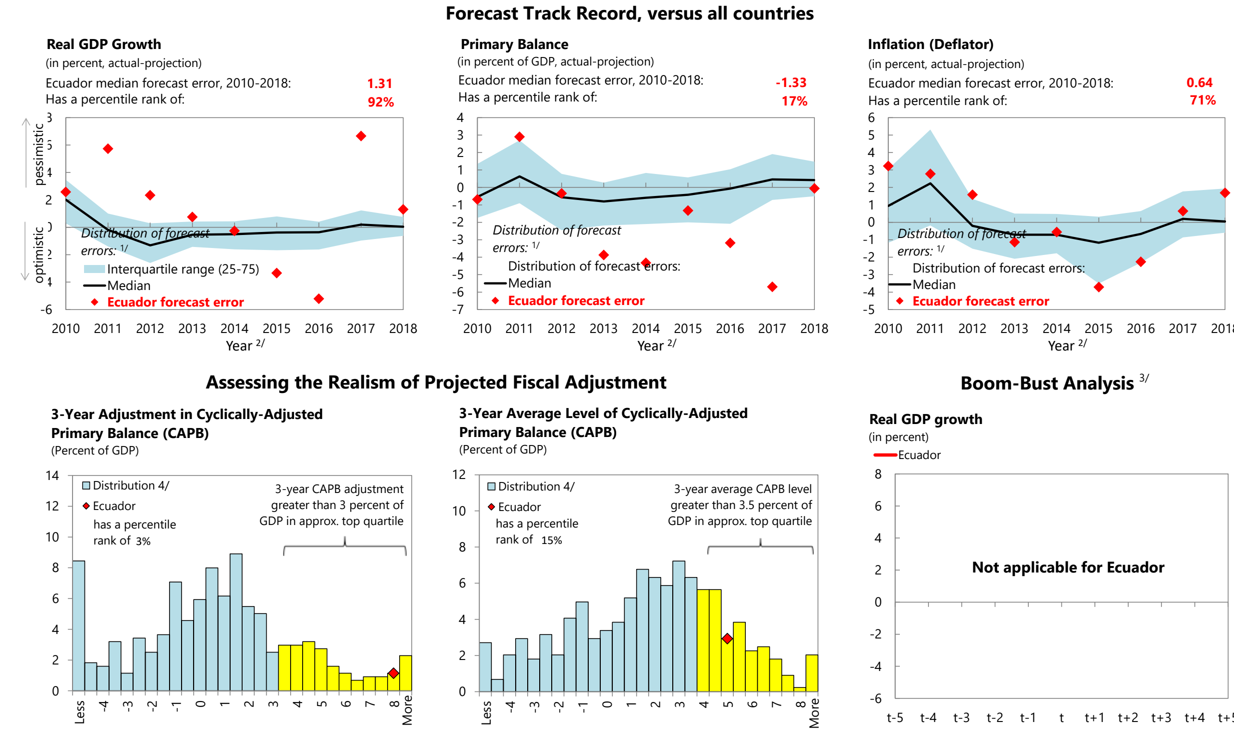
(in percent)

Baseline Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary Balance	-5.8	-1.4	2.3	3.7	4.3	4.5
Effective interest rate	5.2	2.4	2.7	2.9	3.2	3.8
Constant Primary Balance Scenario						
Real GDP growth	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary Balance	-5.8	-5.8	-5.8	-5.8	-5.8	-5.8
Effective interest rate	5.2	2.4	2.7	2.9	3.5	4.4

Historical Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-11.0	2.8	2.8	2.8	2.8	2.8
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary Balance	-5.8	-2.3	-2.3	-2.3	-2.3	-2.3
Effective interest rate	5.2	2.4	2.7	2.8	3.4	4.2

Source: IMF staff calculations.

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



Source : IMF Staff calcuulations.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

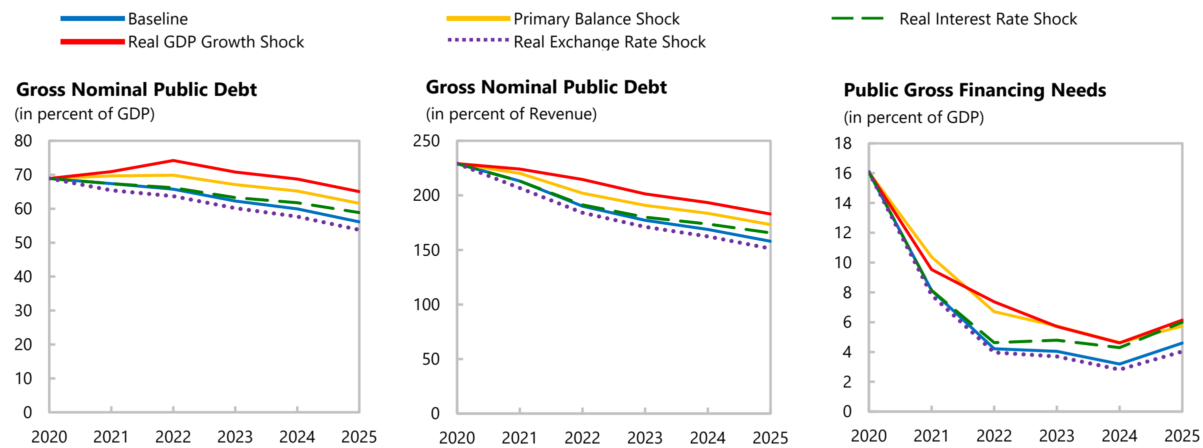
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Ecuador, as it meets neither the positive output gap criterion nor the private credit growth criterion.

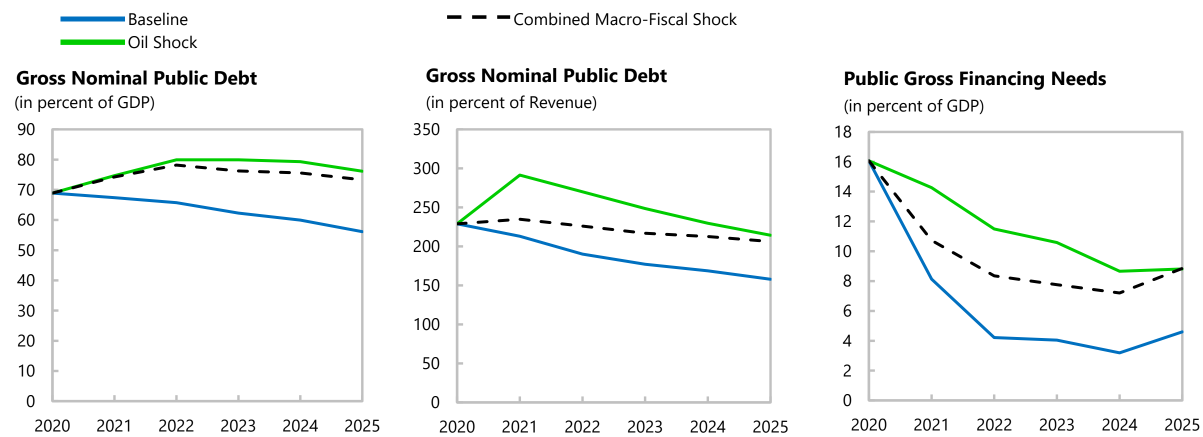
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 4. Ecuador: Public DSA – Stress Test

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

	2020	2021	2022	2023	2024	2025
Primary Balance Shock						
Real GDP growth	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary balance	-5.8	-3.6	0.5	3.0	4.0	4.4
Effective interest rate	5.2	2.4	2.8	3.0	3.3	4.0
Real Interest Rate Shock						
Real GDP growth	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary balance	-5.8	-1.4	2.3	3.7	4.3	4.5
Effective interest rate	5.2	2.4	3.3	3.8	4.4	5.4
Combined Shock						
Real GDP growth	-11.0	1.9	-1.6	1.7	2.0	2.3
Inflation	-2.7	1.1	1.6	1.4	1.3	1.3
Primary balance	-5.8	-3.6	0.0	3.0	4.0	4.4
Effective interest rate	5.2	2.5	3.4	4.0	4.8	5.8

	2020	2021	2022	2023	2024	2025
Real GDP Growth Shock						
Real GDP growth	-11.0	1.9	-1.6	1.7	2.0	2.3
Inflation	-2.7	1.1	1.6	1.4	1.3	1.3
Primary balance	-5.8	-2.5	0.0	3.7	4.3	4.5
Effective interest rate	5.2	2.4	2.7	3.0	3.3	3.9
Real Exchange Rate Shock						
Real GDP growth	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation	-2.7	8.4	2.3	1.4	1.3	1.3
Primary balance	-5.8	-1.4	2.3	3.7	4.3	4.5
Effective interest rate	5.2	2.5	2.7	2.8	3.1	3.7
Oil Shock						
Real GDP growth	-11.0	2.8	-0.7	1.7	2.0	2.3
Inflation	-2.7	1.8	2.3	1.4	1.3	1.3
Primary balance	-5.8	-7.4	-2.7	0.7	3.3	4.5
Effective interest rate	5.2	2.4	3.2	3.6	4.0	4.6

Source: IMF staff calculations.

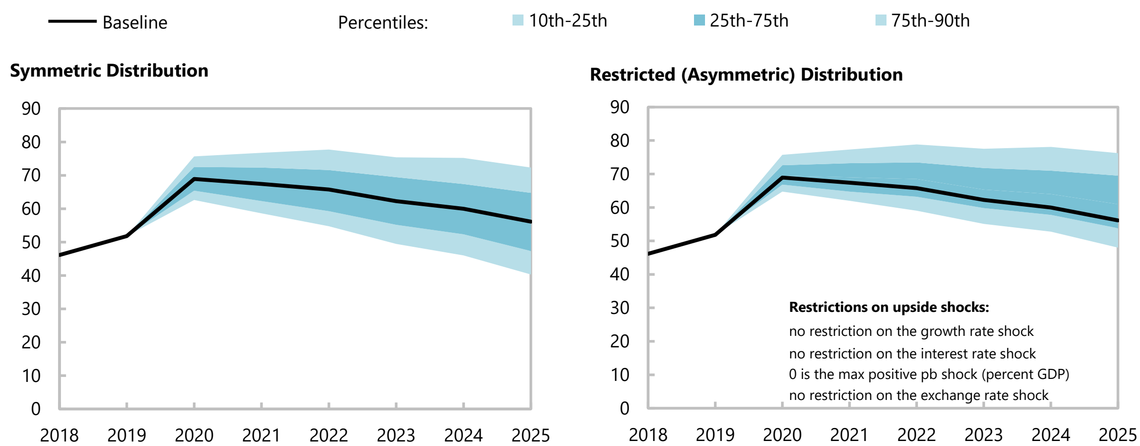
Figure 5. Ecuador: Public DSA Risk Assessment

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

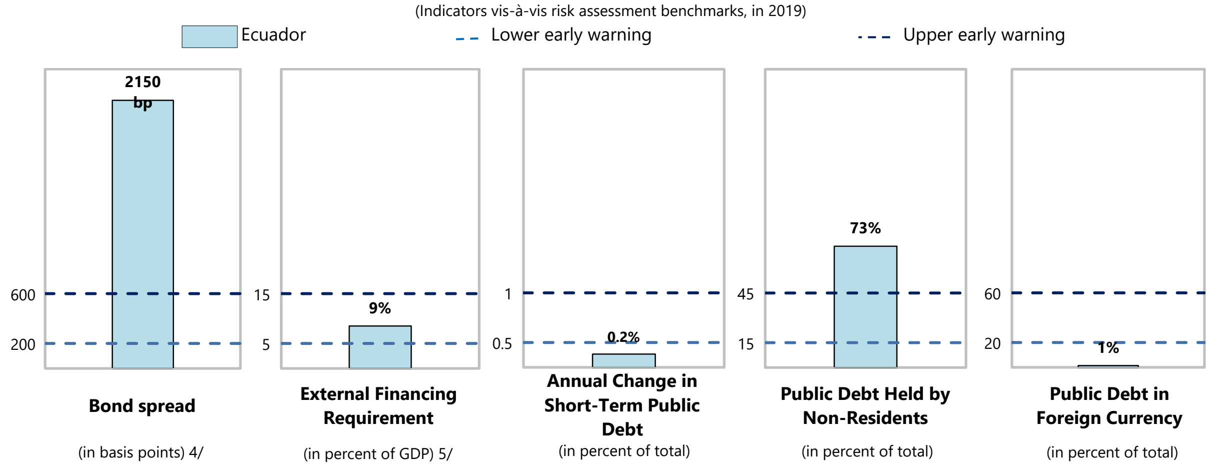
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2019)



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 month, 19-Aug-20 through 18-Sep-20.

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.

Table 2. Ecuador: External Debt Sustainability Framework, 2015-2025

(in percent of GDP, unless otherwise indicated)

	Actual					10-Year	10-Year	Projections						
	2015	2016	2017	2018	2019	Historical Average	Standard Deviation	2020	2021	2022	2023	2024	2025	Debt-stabilizing non-interest current account 6/
Baseline: External debt	30.0	36.6	41.1	42.5	48.2			**60.2**	**57.9**	**57.0**	**58.0**	**57.4**	**54.5**	**-0.3**
Change in external debt	4.8	6.6	4.5	1.4	5.6			12.0	-2.2	-0.9	1.0	-0.6	-2.9	
Identified external debt-creating flows (4+8+9)	1.5	-2.1	-2.0	-1.4	-0.7			7.5	-3.2	-1.9	-2.5	-2.8	-3.0	
Current account deficit, excluding interest payments	0.8	-2.9	-2.1	-1.4	-2.8			-1.2	-1.6	-2.6	-3.0	-3.3	-3.4	
Deficit in balance of goods and services	2.5	-0.6	0.4	0.9	-0.2			0.5	0.4	0.0	-0.4	-0.8	-1.0	
Exports	21.6	20.1	21.6	23.6	24.3			22.1	22.0	22.3	22.6	22.8	23.0	
Imports	24.1	19.5	22.1	24.4	24.0			22.7	22.4	22.3	22.1	22.1	22.0	
Net non-debt creating capital inflows (negative)	-1.3	-0.8	-0.6	-1.4	-0.9			-0.7	-0.7	-0.8	-0.9	-0.9	-1.0	
Automatic debt dynamics 1/	2.1	1.5	0.7	1.4	2.9			9.3	-0.9	1.5	1.4	1.3	1.4	
Contribution from nominal interest rate	1.5	1.7	2.2	2.6	2.9			3.2	1.8	2.3	2.4	2.5	2.7	
Contribution from real GDP growth	0.0	0.4	-0.8	-0.5	0.0			6.1	-2.7	-0.7	-0.9	-1.1	-1.3	
Contribution from price and exchange rate changes 2/	0.6	-0.6	-0.7	-0.7	0.1			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.3	8.7	6.5	2.8	6.3			4.5	1.0	0.9	3.5	2.2	0.1	
External debt-to-exports ratio (in percent)	139.0	182.2	190.2	180.4	198.3			271.9	262.8	255.7	257.1	251.3	237.0	
Gross external financing need (in billions of US dollars) 4/	9.1	5.3	8.1	10.6	9.1			10.3	6.8	6.9	7.2	7.7	8.1	
in percent of GDP	9.2	5.3	7.7	9.8	8.5			11.1	6.8	6.7	6.8	7.0	7.1	
Scenario with key variables at their historical averages 5/								**60.2**	**60.6**	**61.1**	**63.6**	**64.7**	**63.9**	**-0.8**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	0.1	-1.2	2.4	1.3	0.1	2.8	2.9	-11.0	4.8	1.3	1.7	2.0	2.3	
GDP deflator in US dollars (change in percent)	-2.5	1.9	1.9	1.8	-0.2	2.7	2.9	-2.6	1.8	2.3	1.4	1.3	1.3	
Nominal external interest rate (in percent)	5.8	5.8	6.4	6.6	6.8	5.7	0.8	5.7	3.1	4.0	4.3	4.4	4.9	
Growth of exports (US dollar terms, in percent)	-25.9	-6.3	12.3	12.5	2.8	6.2	14.9	-21.1	6.2	4.7	4.4	4.5	4.3	
Growth of imports (US dollar terms, in percent)	-20.8	-18.4	18.1	14.2	-1.7	5.6	16.7	-18.3	5.4	3.2	2.4	2.9	3.3	
Current account balance, excluding interest payments	-0.8	2.9	2.1	1.4	2.8	0.8	1.4	1.2	1.6	2.6	3.0	3.3	3.4	
Net non-debt creating capital inflows	1.3	0.8	0.6	1.4	0.9	0.8	0.3	0.7	0.7	0.8	0.9	0.9	1.0	

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.

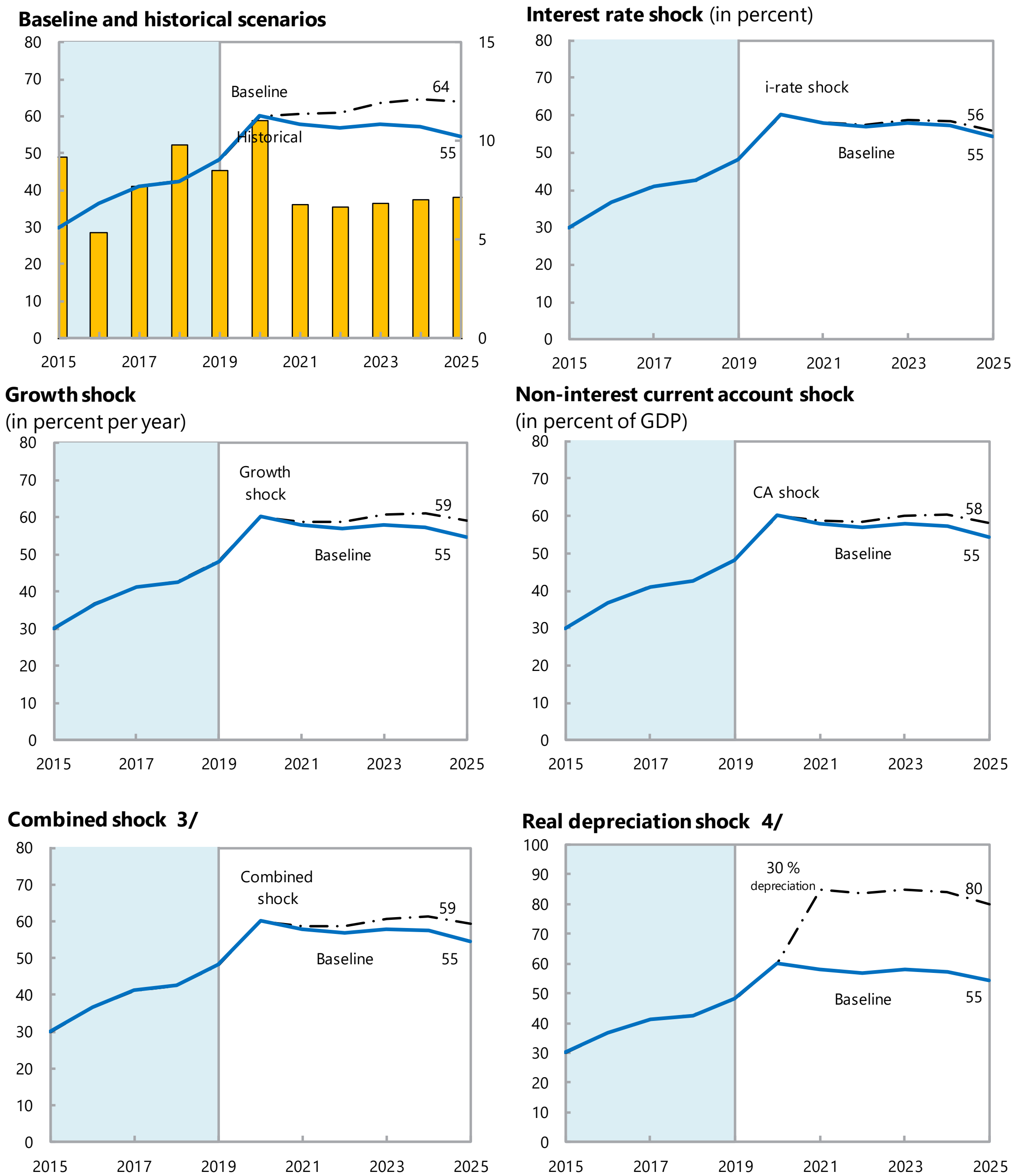
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

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.

Figure 5. 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 2021.

Annex V. External Sector Assessment[1]

The country's external position is assessed to be weaker than the level consistent with medium-term fundamentals and desirable policies and the real effective exchange rate is assessed to be about 30 percent overvalued. To realign the current account and the real exchange rate with the medium-term fundamentals, fiscal adjustment and structural reforms will be undertaken during the program period.

Current Account Position

1. **The current account was close to balance in 2019, finishing the year at -0.1 percent of GDP, compared to -1.2 in 2018.** The improvement in 2019 was mainly driven by trade, with a trade balance surplus of over $1 billion, explained by an increase in non-oil exports of almost 6 percent (mainly traditional exports, such as banana and particularly shrimp); and a compression in both oil and non-oil imports, as a consequence of both lower public and private sector demand.[2] Remittances and the service and primary income accounts remained stable. In 2020, the current account is expected to deteriorate to roughly -2 percent of GDP, due to the collapse in oil prices coupled with domestic disruptions in oil production from pipeline damages, and lower tourism-related income and subdued remittances inflows amid the pandemic—the decline in goods and services exports is projected to be partly offset by the sharp import compression on the back of weak domestic demand.

2. **Ecuador's external position is weaker than the level consistent with medium-term fundamentals and desirable policies (see text table).** In addition to the CA model, because Ecuador is a commodity-exporting country, the EBA lite consumption model for commodity exporters was also estimated.[3] This latter model is specially designed for commodity-exporting countries and better handles the impact of commodity price volatility. This model suggests a current account surplus norm of 3.4 percent of GDP, which would imply a current account gap of about -3.5 percent of GDP. The gap would need to be closed by a significant adjustment in the fiscal deficit and efforts to raise competitiveness by increasing productivity and reducing labor costs.

[1] Prepared by Leandro Medina.

[2] The decrease in public sector consumption is the result of measures to curb public spending; which translated into lower wages and salaries and purchases of goods and services including imports.

3 A key consideration is the ongoing debt restructuring, which would lower external liabilities, keeping all else constant.

Ecuador: External Sector Assessments for 2019 (in Percent) [1/]

	CA Norm	Underlying CA 2/	CA GAP	Elasticity 4/,5/	REER GAP
Consumption-based allocation rules	3.4	-0.1	-3.5	-12%	29
EBA-lite Current Account model 3/	0.4	-0.8	-1.2	-12%	10
EBA-lite REER (ELRER)			-1.2	-12%	9.8

Source: IMF staff calculations.

1/ The EBA-lite Current Account model and the consumption-based allocation rules approaches calculate the difference between the 2019 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/ For the EBA-lite model deviations of the current policies from the desirable policies consistent with the program objectives imply a policy gap of -0.6; mainly due to economic policies linked to private credit levels, growth, and fiscal policies, including public health expenditure policy.

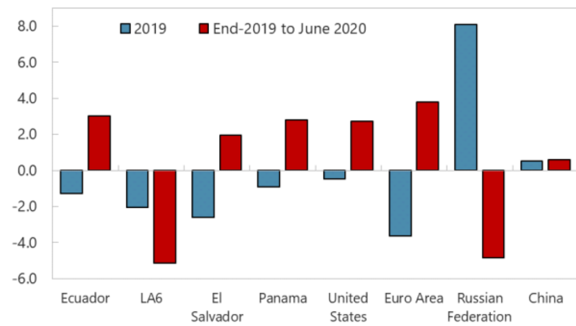
4/ The estimated price elasticity of the CA to changes in the REER is based on price elasticities of exports and imports of -0.23 and 0.3 respectively. The relatively low export elasticity (-0.23 vs -0.44 for other EMs) accounts for the impact of Ecuador's structural characteristics (inflexible labor 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.

5/ 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 WP/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 WP/16/107.

Real Exchange Rate and Competitiveness

Real Effective Exchange Rate

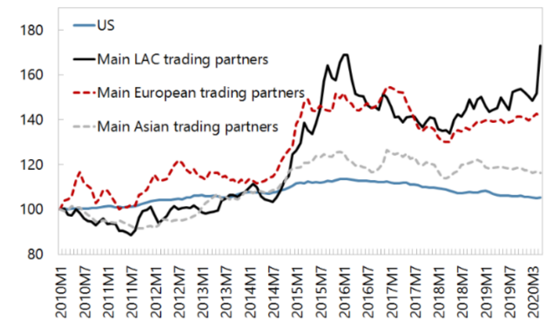
(Percentage change; increase = appreciation)



Sources: INS and IMF staff calculations.

Ecuador: Real Bilateral Exchange Rate

(Jan-10=100)

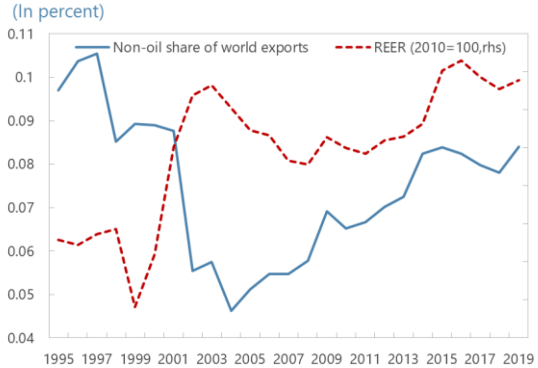


Sources: INS and Fund staff calculations.

3. **After a limited depreciation in 2019, as a result of the weakening of the US dollar, the currency has strengthened during the first part of 2020, particularly vis-a-vis LAC countries.** The REER depreciated by roughly 1 percent in 2019, driven by inflation below its trading partners and a slight depreciation in the US dollar. In the first 5 months of 2020, mainly driven by global factors, the currency has appreciated roughly 5 percent, mostly due to low inflation and an appreciation of the US dollar of 5 percent. It is worth noting that other dollarized economies followed this path (El Salvador, Panama), while large LAC trading partners such as Brazil, Colombia, and Mexico, depreciated by 25, 7, and 15 percent, respectively, in the same period. Non-LAC trading partners such as Euro Area, China, and the Russian Federation, present a mixed picture. Even those countries where the currency appreciated, it was much less than the US dollar and US dollar-pegged economies.

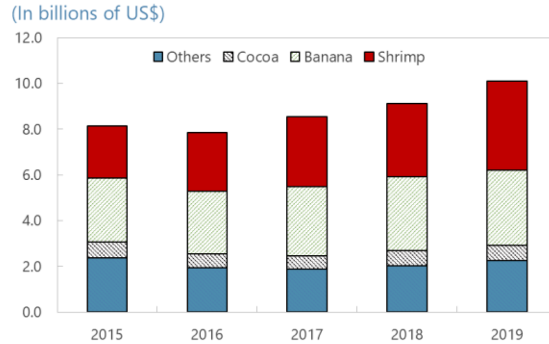
4. Ecuador has relatively high minimum wages, but average wages are not an outlier relative to corresponding productivity. Ecuador's minimum wage is one of the highest in Latin America, but the average wages are broadly in line with peers in the region. Moreover, the average wages also seem to match the level of labor productivity. Relatively lower inflation compared to trading partners observed recently has helped Ecuador regain competitiveness in real wages. This low inflation differential is expected to continue over the forecast horizon and beyond, given the negative output gap which only closes by 2027. Coupled with further increases in labor productivity, this should over time help restore competitiveness.

Ecuador: Export Market Share and REER, 1995-2019
(In percent)



Sources: WEO and IMF staff calculations.

Ecuador: Non-oil Exports
(In billions of US$)

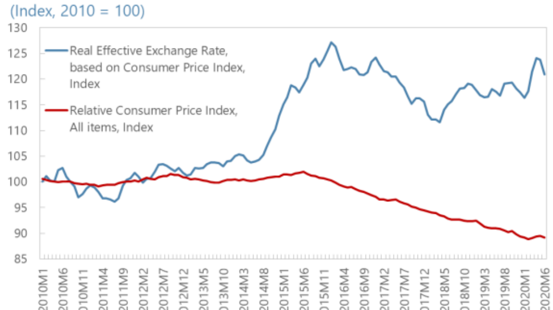


Source: Central Bank of Ecuador.

5. The business environment in Ecuador is relatively frail. Survey-based indicators point to weaknesses in product and labor markets regulation, among others. Thus, Ecuador ranks low in the Global Competitiveness Report (90th of 141 countries); behind the average of LA6 countries.

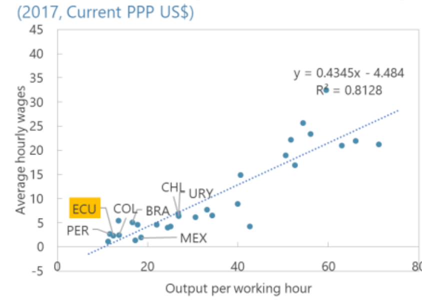
6. The US dollar appreciation has weakened competitiveness despite internal devaluation efforts. Dollar strength is a challenge for dollar pegs and dollarized economies, like Ecuador. In this context, avoiding real appreciation in a dollarized economy is hard unless inflation is consistently low. During Ecuador's recent internal devaluation period, the US dollar appreciated relative to emerging market currencies, which has debilitated Ecuador's competitiveness as its competitors, such as Colombia and Mexico, have seen their currencies depreciate substantially.

Ecuador: REER and Consumer Prices
(Index, 2010 = 100)



Source: IMF INS databse.

Ecuador and ROW: Wages and Labor Productivity
(2017, Current PPP US$)



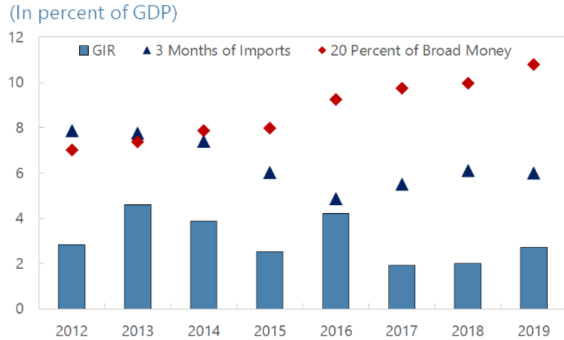
Source: ILO, Trading Economics, Penn World Tables 9.1, and IMF staff calculations.

7. The planned fiscal adjustment and structural reforms are expected to help realign the current account and the real exchange rate with their medium-term fundamentals. Reforms to create a more efficient tax system, restrain 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 0.7 of GDP.

Reserve Adequacy, Capital Flows and the International Investment Position

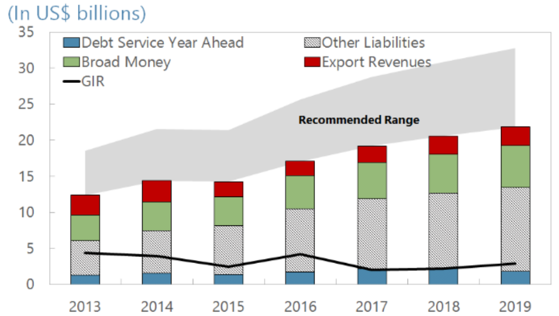
8. International reserves are well below levels adequate for prudential purposes and to support dollarization. Considering the standard reserve adequacy criterion and other complementary measures, the current stock of reserves in Ecuador is insufficient to mitigate potential shocks to the economy. At end-2019 the stock of gross international reserves (GIR) stood at US$2.93 billion (representing about 1.4 months of imports or 14.6 percent of the Fund's ARA metric). At end-July 2020 GIR reached US$3.04 billion.

Ecuador: Traditional Metrics
(In percent of GDP)



Sources: Central Bank of Ecuador and IMF staff calculations.

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

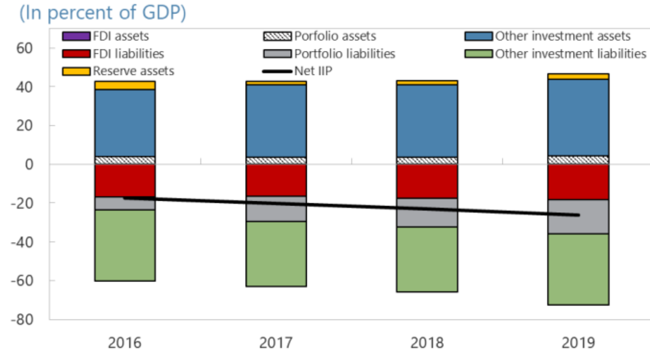


1/ Defined as 30% of external debt service for the year ahead, 20% of other portfolio liabilities, 10% of broad money, and 10% of exports of goods and services.
Sources: Central Bank of Ecuador and IMF staff calculations.

9. External financing needs have declined in 2019. External financing requirements amounted about US$9.1 billion in 2019, or 8.5 percent of GDP, with more than half stemming from debt service obligations of the public sector (almost US$5 billion). Private sector financing has declined markedly, and across the board, compared to 2018, a trend that could continue in 2020.

10. The Net International Investment Position (NIIP) reached -25.9 percent of GDP in 2019 and is forecasted to improve during 2020. 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.

Ecuador: IIP Composition
(In percent of GDP)



Sources: Central Bank of Ecuador and IMF staff calculations.

Appendix I. Letter from the President

Quito, September 17, 2020

Ms. Kristalina Georgieva
The Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, DC 20431, USA

Dear Ms. Georgieva,

Like many other countries, Ecuador has been severely affected by the Great Lockdown. However, as an oil exporter with a dollarized system, the dual shocks of the COVID-19 pandemic and fall in oil prices are resonating stronger in Ecuador. My government has taken strong economic policy measures, including renegotiating our privately held sovereign international debt and reprioritizing our public finances. Our productive and public systems have come under significant strain nonetheless, and our already vulnerable economy has been left with sizable financing needs.

My main goal is to leave a stronger and more prosperous Ecuador for the next several administrations. In this context, my government is committed to continue protecting the lives and livelihoods of the Ecuadorian people and restoring macroeconomic stability. We will continue to foster strong and inclusive growth, by ensuring the sustainability of public finances, strengthening domestic institutions and the foundations of the dollarization regime. Our commitment to these objectives and the policies to achieve them are further elaborated in the Letter of Intent signed by the Minister of Economy and Finance and the General Manager of the Central Bank of Ecuador, as well as in the Memorandum on Economic and Financial Policies and the Technical Memorandum of Understanding.

The financial support of the international community is critical to minimize the economic and social impact of the pandemic and to the success of our policy program. I therefore appeal to the IMF Executive Board to support the Government of Ecuador's program of reforms by approving a new Extended Fund Facility of 27 months with access of US$6,500 million.

I thank you and the Executive Board for your continued support of the Republic of Ecuador and look forward to continuing our strong partnership.

Yours sincerely,
/s/
Lenín Moreno
President of the Republic of Ecuador

Appendix II. Letter of Intent

Quito, September 17, 2020

Ms. Kristalina Georgieva
The Managing Director
International Monetary Fund
Washington, D.C.

Dear Ms. Georgieva:

1. Ecuador is going through one of the most difficult times in its history. Like many other countries, Ecuador has been severely affected by the COVID-19 pandemic. The crisis came at a time when our economy was going through a transition, and further weakened it. The strong containment measures we took to limit the spread of the virus and save lives, coupled with the dramatic drop in oil prices, a major export for Ecuador, and the collapse in global activity, has led to economic costs without precedent in our modern history. Our public finances have come under significant strain, and our already vulnerable economy has been left with sizable balance of payment and fiscal needs.

1. In our Letter of Intent dated April 27, 2020, where we requested emergency assistance from the IMF under the Rapid Financing Instrument, we described the ways in which we were responding to the crisis. The rapid support from the IMF, of US$643 million on May 3, provided emergency relief to our population and helped ease the strain on our health sector. Since then, we have continued to take measures to protect lives and livelihoods and limit the impact of the downturn on our public finances. In parallel, and as a sign of our commitment to fiscal responsibility, we adopted amendments to the organic code of planning and public finances (COPLAFIP) that will strengthen our fiscal framework, notably by incorporating a debt target aimed at ensuring fiscal sustainability, and also negotiated in good faith and reached agreement with our external bondholders to restructure our global bonds with near-full consent.

2. Our main goal for the remaining term of our administration is to leave a stronger and more prosperous Ecuador for the next several administrations. Our comprehensive social and macroeconomic program, *Plan de Prosperidad*, strives to achieve that objective. And with the support of the international community, we will build on the notable progress that has been made over the last two years, particularly on enhancing transparency, strengthening public financial management, and protecting the most vulnerable.

3. Notwithstanding these advances, our policy space to respond to the ongoing crisis remains limited. To that end, we have prepared a comprehensive economic plan that is elucidated in the attached Memorandum of Economic and Financial Policies (MEFP). The plan is anchored on two main objectives: First, we will support the economic recovery in the short term, and extend lifelines to our population by ensuring the most vulnerable Ecuadorians and the ones falling into poverty because of the pandemic will be covered by our expanded social assistance safety net. Second, we will undertake further reforms to strengthen domestic institutions, including the basis for dollarization, and anchor strong, durable and inclusive private sector-led growth. This includes managing our public finances prudently and mobilizing revenues, with the objective of ensuring fiscal sustainability in the medium and long term, including through an ambitious, yet realistic, fiscal consolidation starting next year. To help us meet the plan objectives, we kindly request IMF support for this policy package with a 27-month Extended Fund Facility (EFF) in the amount of SDR 4.615 billion (661 percent of quota and equivalent to about US$ 6.5 billion) to be provided for budget support.

4. As part of this comprehensive plan, we are committed to strengthening our public financial management systems by operationalizing the amendments to COPLAFIP and improving fiscal data, improving our cash and debt management frameworks, evaluating the existing stock of arrears and developing a framework to monitor and prevent further accumulation, and strengthening our procurement systems, the anticorruption framework, fiscal transparency related to COVID-related spending, and overall debt transparency. We will also promote the organic monetary and financial code (COMYF), the AML framework, the asset declaration regime, PPP regulations, and modernize labor contracts.

5. Given the high uncertainty regarding the outlook for the pandemic and its economic impact, we will exercise prudence in our fiscal policy. Rather than extending arrears, we intend to take early contingency measures to further postpone non-urgent expenditures, such as capital investment projects. We will also carefully roll-back COVID-related measures in due time to ensure adequate financing is dedicated to reactivating the economy.

6. Together with our homegrown policies, this new Fund arrangement will help cover Ecuador's urgent balance of payments and fiscal needs. The new arrangement will build upon progress made under the previous IMF-supported program and provide a valuable anchor for our economic policies. The new program will also continue to play a catalytic role in mobilizing international support, including from the World Bank, IADB, and CAF as well as our bilateral creditors, to ensure that the program is fully financed and helps restore access to international capital markets.

7. We will update the memorandum of understanding between the BCE and the Ministry of Economy and Finance that clarifies the responsibilities for timely servicing of the financial obligations to the IMF. 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 also request the IMF Executive Board's approval for retaining the existing exchange restriction arising from the tax on transfers abroad for the making of payments and transfers on current international transactions on the ground that the measure is maintained for balance of payments purposes. We intend to phase out this measure once macroeconomic stability is restored, and the reserve position is strengthened.

8. In line with our commitment to transparency, we will provide information requested by the Fund to assess our policy implementation and consent to the publication of this letter and the accompanying Executive Board documents on the IMF's website, to keep domestic and international agents informed about our policy actions and intentions. The government will consult with the Fund on additional measures that may be needed in the course of program implementation and in advance of revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation.

Sincerely yours,

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

Attachment I. Memorandum of Economic and Financial Policies
Attachment II. Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

Our government has a strong commitment to leave the next administration with a well-managed, and more equitable, efficient, and competitive economy. Our goal is to urgently address the macroeconomic needs caused by the crisis, expand our social safety nets, anchor fiscal sustainability, and continue to strengthen our institutions for a dynamic and more resilient Ecuador. This memorandum describes the key policies of our IMF-supported program under a 27-month Extended Fund Facility (EFF) arrangement, which builds on the previous EFF arrangement that started in 2019.

1. **We have made important progress over the last two years in implementing our policy plans in a range of areas, notably by enhancing fiscal transparency, strengthening public financial management, and protecting the most vulnerable.** In December last year, we reached consensus in the National Assembly to pass the *Ley de Simplificacion y Progresividad Tributaria* that aims to make our tax system more efficient and bolster much-needed revenues to put public debt on a sustainable path. In July this year, we passed amendments to the *Codigo Organico de Planificacion y Finanzas Publicas* (COPLAFIP), marking a significant improvement in public financial management practices by *inter alia* introducing new fiscal rules to contain spending growth and ensuring compliance with the debt rule mandated by our constitution. We have also reformed fuel subsidies by introducing a formula to keep domestic retail prices aligned with international prices while smoothing the adjustment for consumers. This new mechanism will generate efficiency gains and improve equity as we redirect related fiscal savings to better support lower income households and the vulnerable.

2. **While the COVID-19 pandemic has slowed the transition we embarked on and limited the impact on growth of our reforms, we remain committed to support economic recovery and maintaining the reform momentum to fundamentally and durably improve Ecuador's long-term prospects.** Our policy objectives for the remaining time of our tenure are stabilizing the economy and supporting lives and livelihoods in the immediate run, while continuing to pursue structural reforms that will strengthen the foundations for dollarization and anchor strong, durable and private sector-led inclusive growth in the period ahead. In this regard, we see this new arrangement as following through with the commitments we had made under the previous EFF arrangement that began in 2019 and advancing that agenda in the key areas of strengthening institutions. In practice, with the support of our partners, the new Fund-supported program will anchor our effort to (i) expand the coverage of social assistance programs; (ii) ensure debt sustainability with high probability, including through an ambitious, yet realistic, fiscal consolidation; and (iii) strengthen domestic institutions through enhanced transparency, governance, and better policy and legal frameworks. Our administration is committed to continuing with structural reforms and generating a broad and constructive policy debate in the following months. We will leave the next administration with a plan to assure continuity and fast implementation of key structural reforms in areas such as tax, labor, social security and monetary and financial reforms. Improving transparency, data integrity, governance, and the quality of management of public finances, will be key objectives of our program.

3. The following sections of this memorandum outline in detail our policy plans under Ecuador's Fund-supported program.

A. Expanding Our Social Safety Nets

4. To address the COVID-19 pandemic, our immediate priority is to support our population, notably the most vulnerable. We intend to extend lifelines to households while continually increasing the coverage of social assistance programs over time, in order to ensure all poor households are covered by our social programs. To meet this goal, we are upgrading the social registry and expanding the coverage of social assistance programs with the assistance of the World Bank. Measures to monitor this development we will activate the Interinstitutional Committee of the Social Registry Unit (in the Presidential Secretariat): the General Secretariat of the Presidency, the Ministry of Economy and Finance, Secretariat "Plan Todo Una Vida", and as a participant, the Ministry of Economy and Social Inclusion. The committee will meet on a monthly basis to review the Social Registry surveys, including the coverage of the population and social spending. Our objective is to more than double the coverage of the low-income beneficiaries from 37 percent to 80 percent by December 16, 2021 (*Structural Benchmark*). To ensure that we are on the path to meet this objective timely, we will increase in 225,000 by December 16, 2020 and 159,000 by April 2021 the number of families that receive social support gradually but rapidly.

B. Restoring Fiscal Sustainability While Supporting Our Population

5. Our overarching priority in the ongoing crisis has been to protect lives and livelihoods. For this purpose, we have taken several measures to ease the burden of the crisis on families, protect jobs, and support small and medium enterprises. At the same time, to keep our public finances in order, we took steps to generate savings, such as reducing the public wage bill, reforming fuel subsidies, and cutting non-essential spending. Even with these significant savings, the fiscal deficit is expected to grow in 2020, mainly because of the dramatic fall in revenues due to lower oil prices, weaker economic activity and the increase of public health spending due to COVID-19. Consequently, the crisis will put a strain on our public finances and increase public debt.

6. Our government is committed to restoring the sustainability of Ecuador´s fiscal accounts and leave the next administration with stronger institutions and a more robust public financial management framework. Our proactive and market friendly initiative to restructure our international bonds of $17.4 billion, which received more than 98 percent consent from the bondholders, is a testament to this commitment. With this agreement, we will be extending the maturities of our bonds by 10 years (with no principal payment until 2026) and lower coupons to about 5¼ percent (from 9¼ percent). The deal reflects our long-term view of fiscal policy and will help us make significant progress in attaining the debt target of 40 percent by 2032 that is enshrined in our new budget law COPLAFIP. As part of our comprehensive debt management strategy, we are also in active dialogue with our main bilateral financing partner, the People's Republic of China, to reprofile our obligations and secure new financing. We already reached an agreement for rescheduling $417 million of upcoming obligations in 2020-21 to 2022-24 with the China

Development Bank (CDB). We will continue to aim at further alleviating our debt burden, not only for our government but for forthcoming administrations.

7. Ensuring fiscal sustainability and meeting the debt limits in COPLAFIP will also require further and early action on fiscal policy. In order to quickly reverse the upward trajectory of our public debt-GDP ratio, and bring our debt below our benchmark target of 40 percent of GDP by 2032, we will, in 2021, roll back $800 million in COVID-related spending once the crisis subsides, coupled with cuts in capital expenditure of about $700 million to make room for higher social spending. Together with a rationalization of spending in other areas and an increase in tax revenues, this is expected to improve the overall balance by $5.4 billion from the previous year (6 ppt of GDP). Overall, a consolidation in non-oil primary balance including fuel subsidies of 5.5 percentage point of GDP over the period 2019-2025 (reflected in an improvement of 5.5 percent of GDP in the overall nonfinancial public sector (NFPS) balance) will be necessary to attain the debt targets. Elements of our fiscal package will include:

- *A tax reform yielding permanent revenues:* Our tax system still needs to be reinforced and improve, we have a relatively small base, high personal allowances, complexity, the income and value added tax revenues remain low by international and regional standards, owing to low tax rates and weak enforcement. Total tax expenses are also high: in 2018 they were $5.8 billion, 5.3 percent of GDP and 41 percent of tax collected by SRI. In order to finance the much-needed spending to support a more prosperous, fair and equitable Ecuador, we will submit a tax reform, elaborated in consultation with Fund staff, which would be approved by our National Assembly in the exercise of its powers and enacted by September 2021, including a growth-friendly VAT reform, a progressive reform of the PIT focused on the higher end of the income distribution, and a CIT reform geared towards base-broadening, yielding 2½ percentage points of GDP (*Structural Benchmark*). With this timeframe, the revenue gains can begin to accrue in 2022. The implementation of this tax package will be complemented by measures to reduce compliance risk, including by enhancing the Large Taxpayers Office (LTO) responsible for all tax administration functions, in particular in reinforcing its audit functions.
- *An adjustment in some public sector wage bill to support a more fair labor market:* Reducing public sector wages in temporary contracts will result in an overall improvement in labor market equity given the significant wage premium that public sector workers enjoy compared to those in the private sector. To safeguard fiscal finances as well as a strategy for maintaining employment, we temporarily reduced the working hours of public sector employees, excluding those in strategic sectors such as health, army and police and vulnerability conditions. We have announced that we will extend this measure until May 2021 to generate the savings for strengthening the social safety net. In addition, we will continue to carefully realign the wage bill through a balanced strategy of prudent decisions on the renewal of occasional contracts and new hiring of public employees, while assuring the quality of public services. We also plan to adjust the wages of newly hired public employees to align them more closely with those in the private sector.

- *A procurement reform to increase efficiency and ensure better governance of public funds*: In May, President Moreno promulgated a Decree to create a Unified System for the Purchase of Medicines and Strategic Goods for the Health Sector. Our objective is to increase transparency to fight and avoid price surcharges for medicines and medical supplies and to lower prices through a consolidated purchase process for health establishments and public hospitals. We will ensure that the transparency rules under the umbrella public procurement law apply to this sectoral decree, including the publication of information on public procurement contracts and the independent audit of COVID-19-related spending (as specified in the related prior action and structural benchmark in Table 2). Drawing on the World Bank's analysis, we will review the terms and modalities of the overall public procurement to improve efficiency in service delivery and generate fiscal savings. Envisaged changes include using more competitive bidding, improving planning, demand consolidation and outsource of inventory management with a logistics operator. We will identify specific areas in which efficiency gains and fiscal savings can be achieved and will incorporate in the 2022 budget. In addition, this initiative has a positive impact on the out-of-pocket health expenditure of the population and ensures the traceability of medicines and medical devices acquired by the State. Currently, the entities involved are adjusting their regulatory frameworks to allow the compliance with the Decree.
- *Improving resource allocation through fuel subsidies.* Fuel subsides benefit mostly the well-off, generate negative externalities for the environment, and contribute to smuggling. A key structural reform taken by this administration after the cancellation of the 2019 EFF was the implementation of an automatic fuel pricing mechanism to align domestic fuel prices with international prices. This mechanism will generate long lasting fiscal savings, encourage a more efficient energy use, reduce the depletion of natural resources and help preserve the environment. The fiscal savings from the reform will finance higher priority public spending, including the increase in spending required to strengthening our social safety net through expanded coverage of poor families under social assistance programs. The mechanism limits the monthly increase in prices, making the price adjustments gradual. To ensure greater transparency and generate incentives to seek the lowest possible import cost, we will pass a decree to modify the pricing formula, establishing a clear link between domestic retail prices and import prices set on the basis of a benchmark reference price. The decree provides the pricing formula and establishes that the regulator will set the specific reference prices. Moreover, while it is not our intention to deviate from the pricing formula, we will seek ways to limit discretion in the management of the pricing formula—in line with our commitment to make this reform permanent—and limit the risk of reversal when international prices rise down the road. We are implementing a communications strategy with the assistance of the World Bank to inform the general public of the motivation for and benefits of reform.
- *Moderation in capital spending. Given our robust public capital stock and our eye on fiscal sustai*nability, we need to spend on capital projects more efficiently. We will therefore prioritize capital expenditure projects in the coming years. Towards this objective, we plan to undertake a Public Investment Management Assessment (PIMA), supported by IMF technical assistance, to improve the public investment management cycle, increasing the transparency and efficiency of

public investment, ensuring that resources are allocated to promoting growth-enhancing investment in public infrastructure.

8. We will monitor progress towards our fiscal goals with the quantitative conditionality in Table 1. The NFPS balance is an important indicator of progress towards the debt limits enshrined in COPLAFIP. We will monitor it, initially through an indicative target, with the plan of improving the timeliness and reliability of the underlying data from subsectors before elevating it to the level of quantitative performance criterion applying to targets for end-August 2021. To prepare for this transition we will put in place the electronic data submissions systems and press upon subsectors to screen the data of individual entities before submitting. The speed of data transmission and transparency around data updates following original submissions should also be improved. Data submission will be based on actual execution as opposed to budgeted amounts.

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

C. Strengthening Fiscal Frameworks, Governance, and Transparency

10. We will continue to increase transparency and improve practices in Ecuador´s fiscal management. Increasing the transparency of our sovereign debt is a priority. We have been publishing sovereign debt contracts as legally permissible, and will continue to promote transparency in future debt contracts. We have adopted a regulation that requires publication of audited financial statements by all public enterprises. We look forward to the IMF providing soon one long-term expert (LTX) on public financial management (PFM) and one short-term expert (STX) on government finance statistics (GFS) (See Section G). These experts will help enhance fiscal and debt transparency, build capacity on cash management and financial planning, and manage fiscal risks related to subsectors of the non-financial public sector (NFPS).

11. To further anchor our commitment of improving fiscal policy management, we commit to the following measures:

- *Operationalize COPLAFIP*. The amendments to the organic budget code COPLAFIP that were adopted in July 2020 will be game changers for Ecuador's public financial management. In order to make the timely collection, accurate compilation and publication of fiscal data systematic, we will first adopt a regulation on data reporting by subsectors of the NFPS (*Prior Action*). We will subsequently adopt the regulations to fully operationalize the remaining amendments to the law by end-November (*Structural Benchmark*). The reorganization of the Ministry of Economy and Finance, which will be carried out later this year with support from the IADB and through which a fiscal risk unit will be established, will also support the implementation of the new law and enhance coordination among different levels of government.
- *Enhance transparency in public procurement*. As a *Prior Action* we will enact a regulation mandating the publication of all public procurement contracts along with key information such

as the names of the awarded entities and their beneficial owner(s), and ex-post validation of delivery on a dedicated government website to prevent the misuse of public resources. To further promote data synergies that improve the overall capacity to reduce opportunities for corruption, we will seek to swiftly implement this transparency reform and begin work towards complementary measures, including the updating of the register of entities participating in public procurement (registro único de proveedores) and the data requested by the company registry, to incorporate beneficial ownership identification requirements.

- *Avoid accumulation of arrears.* Given the significant cash pressures our treasury is facing in the context of the pandemic, we have been forced to prioritize cash payments to public entities primarily involved in supporting the health crisis, social protection and run large account payables to other public entities such as sub-national governments. Consequently, the central government arrears had increased significantly and to a lesser amount in the NFPS. Going forward, we will comply with our budget obligations. We will evaluate the existing stock of domestic payment arrears of the central government and selected relevant entities of the NFPS that were accumulated in 2020 by April 2021, and put in place a strategy to clear, monitor and prevent further accumulation, in line with IMF technical assistance recommendations (*Structural Benchmark*). We are working on the implementation of the new monitoring system.
- *Improve cash and debt management* (¶33). Durably tackling the arrears problem requires adopting robust and permanent cash management practices with strong inter-agency coordination. To that end, we will prepare a financial plan for the budgetary central government for the remainder of the year, which will ensure an adequate cash balance of the social security (*Prior Action*). We will prepare a similar plan for 2021, to be approved by the MEF Financial Committee, by December 16, 2020, which will be particularly important for an election year, absent a full budget (*Structural Benchmark*). We will also prepare and publish a Medium-term Debt Management Strategy (MTDS) by end-February 2021 to manage our sovereign debt portfolio transparently and ultimately prepare the market for our prospective access (*Structural Benchmark*). The MTDS, to be prepared with the support of IMF TA, will assesses the cost and risk trade-offs of the different sources of public funding, and establish a policy agenda. Overtime, our debt management strategy will be a conduit for our domestic debt development goals and achievements.

Fiscal Policy Inter-Agency Coordination

12. The success of our far-reaching reform efforts hinges on all agencies coordinating smoothly and knowing their role in making our policy program a success. Inter-agency coordination is all the more important in our dollarization regime, as policy levers are limited and developments in one area affect other areas of the economy.

- Close coordination within the NFPS is warranted, including because the COPLAFIP debt anchor is set at the consolidated NFPS level. This includes timely and accurate data submission by NFPS sub-sectors (see ¶8) to enable the MEF to compile fiscal statistics—conducting above-and below the line consistency checks—and provide Ecuadorians with an accurate picture of public finances at each point in time. This would allow the country to track progress towards intra-annual fiscal targets and the ultimate medium- and long-term debt targets.

- The dollarization regime also means that the health and integrity of the central bank's balance sheet depends heavily on fiscal outcomes. Our net international reserves co-move positively with the public sector´s deposits at the BCE and decline with short-term gold-collateralized foreign operations. Legacy financial linkages with public banks, reflecting past expansion of the BCE's balance sheet on the back of quasi-fiscal activities, is also a prominent feature of our central bank's balance sheet.

13. In addition to public financial management and financial stability, successfully implementing the structural reform agenda laid out in this MEFP and beyond hinges on the strong and consistent coordination among implementing agencies. We will set up a platform that brings together implementing agencies on a frequent basis, to foster synergy and track progress vis-à-vis our complementary commitments under the new reform plan. This administration sees the need to improve the yearly budgeting process to improve its financial management and transparency.

14. To better support the economy, we have embarked on a reorganization of the MEF, with support from the IADB, to transition towards a modern and forward-looking policy institution. The revamped ministry will have a dedicated statistics unit in the Vice Ministry of Finance with specific responsibility of collecting, processing and compiling fiscal statistics and with sub-units responsible for different sub-sectors of the NFPS. We have also established a unit in the Vice Ministry of Economy to provide an additional layer of cross-checking the fiscal statistics and undertake the financial programming exercise, and a fiscal risk unit for the evaluation, mitigation and management of risks to public finance. We intend to make some additional changes to the structure before implementation, including to ensure an adequate coverage of debt management activities through an administrative area that meets best international standards, including a front office in charge of interaction with the market, a middle-office for medium-term debt strategy and a back-office for recording. This administrative area would also coordinate closely with the S*ubsecretaria de Asuntos Monetarios* y *Financieros*.

D. Strengthening the Institutional Framework of our Central Bank

15. The dollarization regime protects the purchasing power of all Ecuadorian families and the financial value of their homes and other assets, allowing access to credit and better planning. Achieving these core objectives requires strengthening the institutional foundations of our central bank, including sound governance and a fortified clear legal framework.

16. The balance sheet of the BCE remains weakened by legacy assets from the 1999 financial crisis, the expansion of credit to the public sector that took place earlier in the last decade, by a significant payment-in-kind of government debt in 2017, and by a large amount of public sector securities held, which increased as a result of unwinding a gold swap operation of 2017. The *Ley de Fomento Productivo* passed in 2018 and other supplementary regulations already protect the Central Bank from key risks derived from direct and indirect budgetary financing. The BCE's balance sheet is now protected by regulatory requirements implemented under the previous EFF precluding new central bank financing to the government. However, the failure to pass amendments to the monetary and financial code (COMYF) in late 2019 left the BCE with several unsolved issues, including: (1) lack of independence; (2) weak governance; (3) low coverage of financial sector deposits with liquid reserves assets; and (4) lack of a clearly defined objective for the BCE and its role in systematic financial stability. Fortifying the institutional foundations of the BCE requires the consolidation of those safeguards and other amendments of the existing legal framework into a single piece of legislation. In addition, it will be key to set the BCE on a path of gradually building up international reserves in order to fully back both the deposits of private and public financial institutions held at the Central Bank and coins in circulation. In this regard, we will submit to the National Assembly, the amendments to the COMYF, elaborated in consultation with Fund staff and as committed to under the 2019 EFF, including the 2019 safeguards assessment and technical assistance, and enact this law approved by the National Assembly in the exercise of its powers by end-January 2021 (*Structural Benchmark*). This landmark reform will, among other things:

- Clearly define the objectives of the BCE and focus its functions on supporting the dollarization regime;
- Strengthen the operational autonomy of the BCE, including by establishing an independent Board that has fiduciary responsibilities to the Central Bank;
- Unwind past transactions that resulted in the Central Bank holding either directly or indirectly government debt, and reverting the transfer of equity in public banks to the Central Bank's balance sheet, and provide closure to the legacy bad bank from the 1999 crisis;
- Set the BCE on a path of gradually building up international reserves in order to fully back both the deposits of private and public financial institutions held at the Central Bank and coins in circulation.

17. Consistent with our commitment to transparency and good governance, we will strengthen the external audit of the BCE and establish an audit committee (*Prior Actions*), which would prepare a charter for approval by the Junta de Política y Regulación Monetaria y Financiera by end-November 2020 to align the BCE's internal audit with international standards, by, inter alia. making the audits independent, and expanding its coverage to all BCE operations *(Structural Benchmark)*.

E. Boosting the Resilience of our Financial System

18. Our financial system has entered the crisis strong, liquid, and well-capitalized. The measures we put in place early on, including injecting liquidity into the system by lowering banks' contributions to the liquidity fund and allowing loan payment deferrals, have helped stabilize the system. Going forward, as the economic slowdown puts strains on the system, we will ensure greater supervisory scrutiny, particularly of cooperatives which have grown rapidly, with the support of Fund technical assistance in the area of stress testing. We will also ensure that loan portfolios subject to payment deferrals are reported and recorded transparently, and that resolution tools at the disposal of the Superintendency of Banks are upgraded. We will fine tune the design of the credit facility (Reactivate Ecuador) we established to support microenterprises and SMEs in accordance with the needs of the market and consider appropriate rates that stimulate intermediation as well as longer tenors. Once conditions permit, we will ensure that crisis measures are rolled-back.

19. Fiscal pressures starting late last year forced us to pay certain claims from suppliers via ad-hoc issuance of government bonds and CETES. Thus far the issuance for this purpose has reached $224 million; suppliers are able to liquidate these securities in the secondary market with no intervention, albeit at a discount. We have decided to cap the stock of issuance for this purpose at $500 million, and work with the IMF on a time-bound implementation plan to avoid potential disruption in the domestic debt and money markets.

20. In the next twelve months the post-COVID environment will demand exceptional effort of the supervisory authorities. To buttress this effort, we will start preparatory work to modernize our financial framework, with technical support from the Fund, with the objective of strengthening the supervision functions of the superintendencies, aligning them with international best practices, including by upgrading the available resolution toolkit. Equally important, we have crafted, in collaboration with the World Bank, a strategy to promote more financial inclusion by reducing the number of regulated interest rate segments. We plan to start to implement the strategy by end of January 2021.

21. In addition, to ensure a continued effective monitoring and adequate policy response to the needs of the different layers of our financial system, we will make official the formation of a financial coordination committee. The main purpose of the committee will be to prevent financial instability, and foster information sharing, communication and joint analysis among the Monetary Board, Central Bank, Ministry of Economy and Finance, Superintendencies, and the deposit insurance agency, without overlapping with the legal competencies of these institutions. The committee will also support the post-emergency policy making and the design of a medium-term strategy for financial deepening.

22. In the meantime, we will remain vigilant of the liquidity stance in the market. The liquidity fund is a key safeguard and the emergency lending tool for the financial system in Ecuador's dollarized economy. Our goal is to ensure that it acts as a risk pooling tool, it is well resourced, and provides support where needed. To that end, in coordination with the IMF, we will re-examine the liquidity fund's lending options to optimize the impact of its assistance via lending to solvent but illiquid entities. In case that the necessity arises, the authorities will coordinate with the IMF prior to take any decision related to the fund.

23. The Covid pandemic creates a health concern about the use of cash and has sped up technological absorption by individuals and businesses. This creates an opportunity to further incentivize alternative forms of payments. Promoting alternative means of payment—such as credit cards, online transfers, and online payment in e-commerce—that reduce use of cash can bring operational efficiency to the BCE, increase financial inclusion, reduce potential sources of COVID contagion, and even facilitate cash transfers for social policy. To the extent that new options for payment remain fully backed by deposits, they will strengthen dollarization. We will revise sources of red tape and disincentives in the use of these technologies, with a view to allow further adoption of those technologies.

F. Strengthening Competitiveness and Private Sector-led Growth

24. 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.

25. Promoting good governance and effective anticorruption and AML/CFT frameworks are fundamental efforts in this regard. Our commitment to address governance, corruption and ML/TF vulnerabilities requires solid legal foundations in line with international standards and good practices, and sustained efforts towards its effective implementation.

26. To this end, we are committed to improving the business climate and strengthening the rule of law to reduce the trust gap between Ecuadorians and public institutions, boost non-price competitiveness and foster private investment and job creation. Integral to improving the business environment is a stronger rule of law and enhanced transparency. To enforce the rule of law, protect the public purse and align our anticorruption and AML/CFT frameworks to international standards and good practices, we will:

- Enact the anticorruption law, currently before the National Assembly, following its adoption by the National Assembly in the exercise of its powers, by end-December 2020 to ensure that acts of corruption are criminalized in line with Articles 15 to 30 of the United Nations Convention (*Structural Benchmark*).
- Publish additional information online, including itemized information on incomes, assets and liabilities, and ensuring the easy, searchable, and timely access to declarations of high-level officials, and/or politically exposed persons (PEPs) based on regulations adopted by the General Comptroller, at the request of the government, to enhance the online publication of asset declarations by end-November 2020 (*Structural Benchmark*). This step is part of a broader reform to the asset and interest disclosure regime for high-level public officials to update it in line with international good practices while not infringing on the domestic privacy protection rules.
- We will use our regulatory and supervisory tools to ensure that financial institutions and other designated non-financial businesses and professionals are required to conduct enhanced customer due diligence when transacting with senior officials and PEPs, in line with FATF Recommendation 12. We will also conduct a broader review of the AML/CFT legal framework to ensure it is in line with FATF standards and strengthen the implementation of a risk-based approach to AML/CFT bank supervision, with technical support from Fund staff.

- Conduct an independent audit of COVID-related spending by end-June 2021 by the Office of the Comptroller General, as per our commitment to the Fund when securing emergency financing in May under the RFI, to ensure that emergency funds were used as originally intended (*Structural Benchmark*).

27. We are committed to strengthening the framework for the operation of state-owned enterprises. This will help improve efficiency of public sector operations, increase productivity and growth. In the near term, we will seek to complete the merger of PetroAmazonas and PetroEcuador to achieve economic of scale and improve efficiency in the refinery of oil products, and eliminate seven state-owned enterprises (SOEs). For that purpose, we are revamping the law for SOEs with IADB support, and will seek to improve transparency and strengthen SOEs governance, and align SOEs standards to that for private companies.

28. As we continue our transition towards making the private sector the main growth engine in Ecuador, we are developing, with IADB support, a PPP framework that will lay the foundations for private sector participation in areas currently handled by the government and which do not fall under the traditional remit of the public sector. Our approach is not to substitute PPPs for government's core functions, but to consider them as part of a mechanism that allows us to tap into private sector expertise. Over time, allowing private sector companies to take over the operations of certain public functions through private delegations while retaining the ownership of these entities in public hands would bring important efficiency gains, increase economy-wide productivity, and support the diversification of our economy. Cognizant of the associated fiscal risks, the ongoing reorganization of the Ministry of Economy and Finance (MEF) sets up a fiscal risk unit that will *inter alia* evaluate the viability of PPPs projects, including quantification of risks to the public sector's balance sheet, and propose ways to mitigate them. Such risks will be clearly presented in our fiscal risk statement, to be developed starting with the 2022 budget.

29. We will continue to work on developing domestic capital markets to allow financial deepening and diversifying financing sources for the government and the private sector, with technical assistance from the United States Treasury. We intend to standardize government securities, replace, on a voluntary basis, the non-standardized and excessively short-term government debt securities held by market participants, including the BIESS, with standardized, longer-term ones, develop a yield curve, and lengthen maturities of government short-term instruments. These reforms can help increase the flow of resources from investors to corporations and to the government and eventually increase investment, productivity, and growth.

A Structural Reform Agenda to Ensure Continuity and a Smooth Transition

30. There are a number of structural reforms that will need to be carried out in short, medium and long term. The current administration is committed to preparing a plan for these reforms so as to ensure a smooth transition and for the next administration to be able to implement as soon as possible:

- *Tax reform* – As mentioned previously, our country needs an ambitious tax reform, including a growth-friendly VAT reform, a reform of the PIT focused on the higher end of the income distribution, and the CIT reform geared towards reducing tax expenses and base-broadening with the revenue gains starting to accrue in 2022.

- *Improving government services provision*. Ecuador needs to accelerate the use of technology to transform the way the government provides services to its citizens: to digitize government services, reduce red tape, reduce time and costs of doing business, increase transparency and help reduce the size of the government. A recent IADB study showed that Ecuador has one of the highest government processes (red tape), with only a quarter of the services available online. The Ministry of Telecommunications, through its program *Ecuador Digital,* aims to transform the country to a digital-based one, for which the objective is to have all government process online by 2022, and 80 percent by the end of the current administration. Similarly, the government aims at improving its Doing Business targets with the assistance of the World Bank and IFC.

- *Modernize the labor market*. In order to improve competitiveness, Ecuador needs to improve and modernize the labor market to allow new forms of labor contracts that can particularly support an increase in female labor force participation and youth employment opportunities. Since June 22, when the Humanitarian Law was in effect, more than 100,000 jobs have been created and 45,000 jobs have been saved through the mechanism of emergency hour reduction. Other reforms have been made through secondary legislation ("acuerdos ministeriales") to facilitate job creation and improve competitiveness.

- *Reinforce the sustainability of social security.* IESS is in a challenging situation, requiring structural changes to ensure its sustainability and the optimization of the use of its resources to guarantee the provision of services. BIESS, as the manager of pension funds, needs to be modernized and generate wealth to its pension holders.

- *Economic integration*. Continuing the process of trade integration by seeking trade agreements with both regional and international partners will facilitate private sector-led growth and ultimately raise living standards. Ecuador is committed to join the Pacific Alliance in the near future, and with the support of multilateral institutions, should analyze the tariff schedule to identify the main obstacles and identify the actions to simplify import requirements and reduce import costs, particularly of production inputs and capital and promote competitiveness

G. Capacity Development

31. With the support of our international partners, we have ensured that our government officials received the best capacity development programs, to support our commitment to bringing our institutions to the highest international standards. Building human capital and knowledge, to ensure a well-functioning and efficient public sector, will deliver long term gains for all Ecuadorians. Over the last two years, we have benefited from over 25 technical assistance missions from the Fund, mostly directed to the MEF, the BCE and our national customs services. We intend to continue our deep efforts and make good use of the capacity development possibilities under this new Fund-supported program, with a focus on government financial statistics, public financial management, and importantly on financial programming.

32. A critical area in which we intend to continue to build capacity is the modernization of our government financial statistics (GFS) to align our current standards to international best practices, including in terms of transparency. In this regard, we will seek to fully leverage support from a Fund-provided STX in GFS, including by identifying and assigning dedicated staff to work closely with the expert, and following up on the expert's recommendations. We will ensure responsibility for the compilation of GFS and Public Debt Statistics Compilation Guide (PSDS), including from the MOF, Central Bank, and public entities that supply the relevant source data. We will identify one senior official (deputy director or director) from each statistical agency involved in the compilation of fiscal and public sector debt statistics and one senior official of Petroecuador and Petroamazonas as designated counterparts to the experts. The Undersecretary of the Ministry of Finance will be responsible for the timely completion of the remedial actions under the misreporting agreement and for achieving the outputs and indicators as agreed with the experts and the IMF. We will extend this capacity building activity to staff from other public entities where possible, including the SRI and the BCE, consistent with our approach to inter-agency coordination, in order to build and maintain capacity across the wide public sector. The STX will work with us through May 2021 to:

- Compile and publish the corrected GFS and PSDS time series for the period of 2012 to 2019, above and below the line, disaggregated by subsectors, as committed under the corrective actions under the misreporting case, by end-May 2021 (*Structural Benchmark*);

- Compile and prepare a GFS and PSDS compilation guide for the NFPS to assist source data suppliers and users of fiscal data, as committed to the Fund to address the issue of misreporting of statistics under the canceled EFF, and disseminate it to relevant agencies by end-May 2021, including national statistics compilers for GFS and PSDS, as well as the providers of the underlying source/accounting data to generate more traction and commitment between them (*Structural Benchmark*);

- (1) Construct a timely set of preliminary fiscal data to be used as an early warning system to monitor targets under the program, in line with IMF recommendations; (2) check data consistency; and (3) analyze the reasons of possible differences between these preliminary data and the final data.

33. We are also fully committed to improving our cash and debt management. In this regard, staff across the MEF will work closely with a Fund-provided LTX in public financial management (PFM) (from October) to improve our functional capacity in undertaking core PFM functions related to cash projections in particular, and the production of a financing plan going forward. We intend to institutionalize our work with the LTX by assigning dedicated staff to the project and documenting the practices learned throughout, so as to retain knowledge in-house and hedge against the risk of staff turnover. We will ensure that our work with the LTX is fully coordinated with our effort with the STX in GFS, including through periodical meetings and in coordination with the Resident Representative. The LTX will, among other supportive activities, provide methodological and training support to MEF staff to undertake:

- Cash and financing planning, monitoring of budget execution, updating plans, fiscal reporting;
- Fiscal risks identification and management related to NFPS subsectors;
- Arrears strategy and monitoring on prevention, clearance, and reporting;
- Budget processes, including expenditure commitments control, cash and accruals basis of reporting, extended use of FMIS in NFPS entities, procurement and enhanced transparency;
- Coordination in collecting and analyzing the required data and information from the entities to develop the above tasks.

34. We count on IMF technical assistance to implement our plans to enhance the quality of financial oversight and the banking legal framework. In the short term, the superintendency of banks will receive support to improve its stress testing capacity; a short-term expert would further improve the policy response during the post-emergency transition. In addition, other technical assistance to work on a better alignment of the banking law with international standards of supervision, regulation, and banking resolution, will be needed during the program.

35. Finally, we have been working with the Fund over the last 12 months on customizing a Financial Programming and Policies (FPP) course for Ecuador. Our staff at MEF and the BCE have already received virtual training on FPP, and the core mission that would deliver a customized macro-framework is now scheduled for delivery in October. The FPP training—which we see as a continuation of a series of macro-fiscal-financial courses for our government officials—will allow our staff working in different areas and relevant public entities to study the inter-linkages among different sectors of the economy and run internally consistent policy scenarios. By bringing together staff from different agencies, the strong inter-relations among the different sectors of the economy, inherent to the FPP's framework, will also practically illustrate the role of inter-agency coordination.

H. Communications

36. Ecuador is at a critical juncture, requiring the nation to come together to navigate the health and economic crises, while designing solutions for tackling pressing socio-economic challenges, including adjusting to low for long global oil prices when the crisis subsides. Consistent with our approach of building a more sustainable and inclusive economy, we will engage the full spectrum of the Ecuadorian society closely to build social consensus around the reform agenda and increase the prospects of the program's success. Towards this goal, we have developed and started implementing a far-reaching communications strategy at end-August 2020, articulating the benefits of the program to the current and future generations of Ecuadorians.

37. The program will be monitored based on the conditionality set out in Tables 1, and 2, based on definitions in the Technical Memorandum of Understanding attached hereto. It is expected that the first review will take place on or after December 15, and the second on or after April 15.

Table 1. Ecuador: Quantitative Performance Criteria and Indicative Targets, 2020-2021

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

	End-Sept. 2020	End-Dec. 2020	End-Apr. 2021	End-Aug. 2021
	Program	Program	IT	IT
Quantitative performance criteria				
1. Overall balance of the budgetary central government and CFDD (*floor*)[1/]	-2,894	-5,095	-1,146	-3,223
2. Accumulation of NFPS deposits at the central bank (*floor*)[1/]	0	589	232	97
3. Non-accumulation of external payments arrears (*continuous PC*)	0	0	0	0
4. (No new) Gross credit to government from the central bank (*continuous PC*)	0	0	0	0
Indicative targets				
6. Non-oil primary balance of the NFPS (including fuel subsidies) (*floor*)[1/]	-2,539	-6,825	-628	-1,934
7. Overall balance of the NFPS (*floor*)[1/]	-2,706	-6,662	-234	-804
8. Change in the stock of NIR - program definition (*floor*)[1/]	-2,200	-3,939	-300	-1,100
9. Coverage of the cash transfer programs for lower income households - number of families (*floor*)[1/]	62,240	225,557	158,964	278,187

Note: Aggregates and adjustors as defined in the Technical Memorandum of Understanding (TMU).

[1/] For 2020 targets, cumulative change from July 1, 2020. For 2021 targets, cumulative change from January 1, 2021.

Table 2. Ecuador - Prior Actions (PAs) and Structural Benchmarks (SBs)

Reform area	Structural Conditionality	Objectives	Due date
	Prior Actions		
Fiscal framework	Adopt a regulation, in consultation with Fund staff, to implement the July 2020 amendments to COPLAFIP requiring the reporting of fiscal data from public sector entities, including GADs, social security entities and state-owned enterprises, to the Ministry of Economy and Finance, detailing the coverage of information (revenue, expenditure, assets, liabilities), periodicity of information provision and enforcement mechanisms in case of non-compliance.	Strengthen budget execution and program monitoring beyond the central government; Improve institutional capacity	PA
Transparency and governance	Enact/amend regulation to mandate the publication on a government website of all public procurement contracts, and the names of the awarded entities and their beneficial owner(s), the names of the public officials awarding the contracts, and the ex-post validation of delivery of the contracted services, providing access to the corresponding documents.	Improve expenditure control, including COVID related spending, and governance to mitigate corruption	PA
Cash management	Deliver to IMF staff a PGE financial plan, prepared in consultation with IMF technical assistance and approved by the MEF Financial Committee, with detailed monthly forecast of revenues, expenditures and financing for the rest of year 2020.	Improve institutional capacity and identify early warning signs of impending liquidity constraints	PA
BCE	Pass a JPRF resolution allowing the BCE to adopt an external auditor selection and rotation policy that should provide for longer term mandates (three-five years), and include technical requirements for central banking experience, compliance with International Standards on Auditing, and experience in the application of IFRS.	Improve the BCE's audit mechanisms	PA
BCE	Pass a JPRF resolution creating an audit committee, which should be composed of external non-executive members with relevant professional experience, especially in the area of audit and IFRS.	Improve the BCE's audit mechanisms	PA
	Structural Benchmarks		
Fiscal framework	Adopt a regulation, in consultation with Fund staff, to implement the July 2020 amendments to COPLAFIP, among others, with regards to public debt, the MTFF, budget preparation and expenditure ceilings, preparation and publication of a fiscal strategy document, budget execution, cash management and arrears, budget modification procedures, fiscal risk management framework, corrective measures regime, and the fiscal rules framework.	Strengthen the public financial management framework and fiscal discipline, and increase fiscal transparency	End-Nov. 2020

Table 2. Ecuador - Prior Actions (PAs) and Structural Benchmarks (SBs) (continued)			
BCE	The JPRF will approve an internal audit charter prepared by the BCE Audit Committee aligned with international standards to provide for: (i) the function's mandate and independence; (ii) coverage of all BCE's operations, (iii) adoption of a risk-based approach, (iv) an internal and external quality assessment program, and (v) regular reporting to an independent oversight body.	Improve the BCE's audit mechanisms	End-Nov. 2020
Transparency and AML/CFT	Enhance the existing online publication of asset declarations ensuring the easy, searchable, and timely access to declarations of high-level public officials and/or politically exposed persons (PEPs), and publishing additional information online, including itemized information on incomes, assets and liabilities, based on regulations adopted by the General Comptroller, at the request of the government.	Strengthen anticorruption and AML/CFT and protect the public purse	End-Nov. 2020
Cash Management	Deliver to IMF staff a PGE financial plan for the year 2021 approved by the Financial Committee.	Improve institutional capacity and identify early warning signs of impending liquidity constraints	Dec. 16, 2020
Transparency and Governance	Enactment of the anticorruption legislation, approved by the National Assembly, including measures to ensure that acts of corruption are criminalized in line with Articles 15 to 30 of the United Nations Convention Against Corruption.	Strengthen anticorruption and protect public finances	End-Dec. 2020
Organic Monetary and Financial Code (COMYF) reform of the Central Bank framework	Enactment of amendments to the Central Bank's legal framework, elaborated in consultation with Fund staff as committed to under the 2019 EFF, in line with the substantive elements and constitutional process described in MEFP ¶16.	Strengthen the autonomy and governance framework of the BCE	End-Jan. 2021
Debt management	Publish a Medium-Term Debt Management Strategy (MTDS), prepared with the support of IMF TA, which assesses the cost and risk trade-offs of the different sources of public funding, and establishes a policy agenda.	Facilitate domestic debt market development, promote medium-term debt management, and increase transparency of public debt policies	End-Feb. 2021
Domestic arrears	Share with IMF staff an updated arrears' clearance strategy with the updated information on the stock of arrears as of end 2020 based on quarterly flows for central government and selected relevant entities of the NFPS in line with IMF technical assistance recommendations.	Strengthen the monitoring and reduce accumulation of payment arrears	End-Apr. 2021

Table 2. Ecuador - Prior Actions (PAs) and Structural Benchmarks (SBs) (concluded)

Fiscal Statistics	Correct and publish the historical NFPS data, both above- and below-the-line, back to 2012.	Improve quality of fiscal statistics	End-May 2021
Fiscal Statistics	Prepare a compilation guide, in consultation with IMF TA, and disseminate it to data providers across the NFPS through a workshop.	Improve quality of fiscal statistics	End-May 2021
Transparency	Undertake an independent audit of COVID-19-related spending by the Office of the Comptroller General by mid-2021 and publish the results on a government website.	Improve expenditure control, including COVID related spending, and governance	End-Jun. 2021
Tax reform	Enactment of a tax reform, elaborated in consultation with Fund staff, aimed at generating revenue and improving the overall efficiency of the tax system, in line with the substantive elements and constitutional process described in MEFP ¶7, bullet 1.	Improve the efficiency of the tax system	End-Sep. 2021
Social assistance	Complete the upgrade of the social registry and expand the coverage of the social assistance program to at least 80 percent of families in the bottom three deciles of the income distribution.	Strengthen the social safety net	Dec. 16, 2021

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) and indicative targets (ITs) 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. All references to "days" indicate "calendar days", unless stated otherwise.

3. **Program exchange rates.** For the purposes of the program, the exchange rates of the U.S. dollar for the duration of the program are those that prevailed on July 31, 2020 as shown in Table 1.

Table 1. Ecuador Program Exchange Rates

US Dollar to Euro	0.85
US Dollar to Renminbi	6.98
US Dollar to Yen	105.83
US Dollar to SDR	0.71
US Dollar to British Pound	0.76
US Dollar to South Korean Won	1,191.03
US Dollar to Swiss Franc	0.91
US Dollar to Canadian Dollar	1.34
US Dollar to Danish Krone	6.32
US Dollar to Swedish Krone	8.78
US Dollar to Norwegian Krone	9.10
US Dollar to Australian Dollar	1.40
US Dollar to Mexican Peso	22.28
US Dollar to Colombian Peso	3,732.71
Gold prices (US$/ounce)	1,975.86

Source: Bloomberg, as of July 31, 2020.

Table 2. Ecuador Quantitative Performance Criteria and Indicative Targets, 2020
(In millions of US$, unless otherwise indicated)

	End-Sept. 2020	End-Dec. 2020	End-Apr. 2021	End-Aug. 2021
	Program	Program	IT	IT
Quantitative performance criteria				
1. Overall balance of the budgetary central government and CFDD (*floor*)[1/]	-2,894	-5,095	-1,146	-3,223
2. Accumulation of NFPS deposits at the central bank (*floor*)[1/]	0	589	232	97
3. Non-accumulation of external payments arrears (*continuous PC*)	0	0	0	0
4. (No new) Gross credit to government from the central bank (*continuous PC*)	0	0	0	0
Indicative targets				
6. Non-oil primary balance of the NFPS (including fuel subsidies) (*floor*)[1/]	-2,539	-6,825	-628	-1,934
7. Overall balance of the NFPS (*floor*)[1/]	-2,706	-6,662	-234	-804
8. Change in the stock of NIR - program definition (*floor*)[1/]	-2,200	-3,939	-300	-1,100
9. Coverage of the cash transfer programs for lower income households - number of families (*floor*)[1/]	62,240	225,557	158,964	278,187

Note: Aggregates and adjustors as defined in the Technical Memorandum of Understanding (TMU).
[1/] For 2020 targets, cumulative change from July 1, 2020. For 2021 targets, cumulative change from January 1, 2021.

4. In addition to the performance criteria listed in Table 2 above, 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 imposition or intensification of import restrictions for balance of payments reasons;
(iii) no introduction or modification of multiple currency practices;
(iv) no conclusion of bilateral payments agreements that are inconsistent with Article VIII of the IMF Articles of Agreement.

These four performance criteria will be monitored continuously.

QUANTITATIVE PERFORMANCE CRITERIA: DEFINITION OF VARIABLES

A. Floor on the overall balance of the budgetary central government and CFDD

Definitions

5. The budgetary central government (Gobierno Central or CG hereafter) and CFDD, for the purposes of the program, consist of the budgetary central government (PGE, including universities) and the account of financing oil derivatives, namely Cuenta de Financiamiento de Derivados Deficitarios (CFDD).

6. The overall balance of CG and CFDD is defined as the total revenues of the CG and CFDD minus thier total spending.

7. Total revenues are recorded on cash basis.

Revenues explicitly included are:

- Revenues from oil exports;
- Revenues from the domestic sales of oil derivatives;
- Interest revenues;
- Tax revenues (ingresos tributarios);
- Other revenues (otros ingresos);
- Proceeds from asset monetization (i.e. revenues from the leasing of assets owned by CG and CFDD).

8. Total spending is recorded on an accrual basis and comprises spending on wages and salaries (sueldos y salarios), purchases of goods and services (compra de bienes y servicios), interest expenditure (interés), other current spending, capital expenditures (including capital transfers and other investment outlays). Other current spending also includes the cost of imports and local purchases of petroleum derivatives (Cuenta de Financiamento de Derivados Deficitarios).

9. Government-funded, public-private partnerships will be treated as traditional public procurements. CG obligations that are accrued on public private partnerships would be recorded transparently in budget data and measured as part of the CG 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.

10. 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.

11. 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

12. All fiscal data referred to above and needed for program monitoring purposes will be provided to the Fund within 45 days from the end of each test date as shown in Table 2. Preliminary monthly data will be provided with the lag of no more than 30 days after the end of each month.

Adjustors

13. Adjustor on oil prices: The floor on the overall balance of the budgetary central government and CFDD will be adjusted upward/downward by US$23.85 million at corresponding test dates for each US$1 per barrel that the average Ecuador mix crude oil price is above/below the program assumption defined in the Table 3. This adjustor is capped at US$119.33 million at corresponding test dates. The average price of Ecuador mix oil price will be calculated as the total value of crude oil exports divided by the total volume of oil exports over the period since the prior test date.

Table 3. Ecuador—Adjustor due to Oil Price Differences Relative to Program Assumptions

	2020			2021	
	Q2	Q3	Q4	April	August
Ecuador mix crude oil price (US$ per barrel)	27.0	36.4	38.1	39.2	39.9

Source: Ministry of Finance and IMF staff estimates

B. Floor on the accumulation of non-financial public sector deposits at the central bank

Definitions

14. The Non-Financial Public Sector (NFPS, Sector Público No-Financiero) for the purposes of the program consists of the CG and CFDD, as defined above, Decentralized Autonomous Governments (including municipal governments, provincial governments and parish boards), Social Security Funds (including IESS, ISSFA, ISSPOL and BIESS), Non-Financial State Owned Enterprises (SOEs, detailed in Table 4), Development Bank of Ecuador (BDE) as well as accounts related to the payments to private operators of oil concessions (Ministerio de Energia y Recursos Naturales no Renovables). The Central Bank of Ecuador falls outside of the NFPS perimeter.

Table 4. Ecuador: Non-Financial Public Sector Corporations Covered Under the Definition of NFPS

Empresa Pública de Exploración y Explotación de Hidrocarburos Petroamazonas - PAM
Empresa Pública de Hidrocarburos del Ecuador Petroecuador - PEC
Empresa Pública Flota Petrolera Ecuatoriana-EP FLOPEC
Empresa Nacional de Ferrocarriles del Ecuador – ENFE (*)
Empresa Pública Línea Aérea del Ecuador TAME (*)
Empresas Públicas Menores (Empresas de Agua Potable)

(*) SOEs in liquidation process, which will be in fiscal data until the liquidation process finishes.

15. Deposits of the NFPS at the Central Bank of Ecuador (BCE) include all depository liabilities (time and on-call deposits) at the BCE of the NFPS, as defined above.

Monitoring

16. The accumulation of NFPS deposits at the BCE at each test date will be measured as the change in the stock of deposits between the first and last day of the corresponding test dates as shown in Table 2.

17. NFPS deposits at the BCE data will be provided to the Fund at weekly frequency within 5 business days following the end of the week.

Adjustors

18. Adjustor on external borrowing. The floor on the accumulation of NFPS deposits will be adjusted upward/downward by the amount of NFPS borrowing from non-residents above/below that envisioned under the program, as reported in Table 5 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 5. Adjustor Due to International Borrowing in Shortfall/Excess vis-a-vis Program Assumptions

	2020		2021	
	Jul-Sep	Oct-Dec	Jan-Apr	May-Aug
Total market issuance consistent with program targets (cumulative) 1/	0	0	0	0

1/ For 2020: cumulative from July 1

19. Adjustor on disbursements from multilateral institutions and China. The floor on the accumulation of NFPS deposits will be adjusted upward/downward by the amount of the excess/shortfall in program loan disbursements from the IMF, other multilateral institutions (the IADB, World Bank, CAF, and FLAR), China, and grants, relative to the baseline projection reported in Table 6. 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 6. Adjustors Due to Shortfall/Excess in Program Loan Disbursements by Multilateral and Bilateral Creditors

	2020		2021	
	Jul-Sep	Oct-Dec	Jan-Apr	May-Aug
Expected disbursements of program loans by multilaterals 1/	2075	4725	600	1150
Expected disbursements from China 1/	0	1700	700	0

1/ For 2020, cumulative from July 1. For 2021, cumulative from January 1, 2021.

20. Adjustor on oil prices. The floor on the accumulation of NFPS deposits will be adjusted upward/downward by US$23.85 million at corresponding test dates for each US$1 per barrel that the average Ecuador mix crude oil price is above/below the program assumption defined in Table 3. This adjustor is capped at US$119.33 million at corresponding test dates. The average price of Ecuador mix oil price will be calculated as the total value of crude oil exports divided by the total volume of oil exports over the period since the prior test date.

C. 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 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 (i) external debt obligations (principal and interest) falling due after September 30, 2020 that have not been paid within 90 days of the due date, considering the grace periods specified in contractual agreements, as well as (ii) payment arrears on goods delivered or services rendered by external entities.

Coverage

24. This performance criterion covers the NFPS. 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

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

restructuring; and (iii) arrears resulting from the nonpayment of commercial claims that are the subject of any litigation initiated prior to September 30, 2020.

Monitoring

This PC will be monitored on a continuous basis.

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

Definitions

25. **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.[2]

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 NFPS will be provided within five business days to the Fund.

INDICATIVE TARGETS (IT): DEFINITION OF VARIABLES

E. Floor on the non-oil primary balance of the non-financial public sector

Definitions

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

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

29. 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).

30. Primary non-oil revenues are recorded on cash basis.

[2] For the purpose of this target, any restructuring of the debt originally owed by the Ministry of Economy and Finance to Goldman Sachs that was subsequently transferred to the BCE will not be considered as financing to the NFPS.

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);

31. 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. 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).

32. Petroleum product subsidies include, but are not limited to, subsidies for gasoline, diesel, jet fuel, av gas, fuel oil and liquefied petroleum gas. Subsidies are defined as a difference between the distributor sale price of the product and the cost of this product. The cost of the product is a weighted average between the cost of imported petroleum derivative products and the cost of domestically produced petroleum products, cost of transportation, storage, and commercialization. For the cost of domestically produced petroleum products, the export price of eastern crude (opportunity cost) is considered as raw material, as well as the cost of refining. The import cost includes the price at FOB value plus freight and insurance.

33. 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.

34. 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.

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

35. All fiscal data referred to above and needed for program monitoring purposes will be provided to the Fund within 60 days from the end of each test date as shown in Table 2. The data submission would also include below the line data. Preliminary monthly data will be provided with the lag of no more than 45 days after the end of each month.

F. Floor on the overall balance of the non-financial public sector

Definitions

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

37. 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.

38. 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).

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

Monitoring

40. 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 days after the end of each test date as shown in Table 2 and preliminary data with the lag of no more than 45 days after the end of each month.

Adjustors

41. Adjustor on oil prices. The floor on the overall balance of the NFPS will be adjusted upward/downward by US$23.85 million at corresponding test dates for each US$1 per barrel that the average Ecuador mix crude oil price is above/below the program assumption defined in the Table 3. This adjustor is capped at US$119.33 million at corresponding test dates. The average price of Ecuador mix oil price will be calculated as the total value of crude oil exports divided by the total volume of oil exports over the period since the prior test date.

G. A floor on the change in the stock of Net International Reserves (NIR)

Definitions

42. Net International Reserves (NIR) of the central bank are computed under the program 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 banks and deposits of other financial institutions 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.

43. Usable gross international reserve assets comprise all readily available claims on non-residents denominated in convertible foreign currencies and controlled by monetary authorities, consistent with the Balance of Payments and International Investment Position Manual (Sixth Edition). Specifically, they include: (i) currency and deposits; (ii) monetary gold; (iii) holdings of SDRs; (iv) the reserve position in the IMF; (v) securities (including debt and equity securities); (vi) financial derivatives; and (vii) other claims (loans and other financial 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.

44. 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;
- Short-term liabilities of the central government with maturity of less than 30 days
- The stock of IMF credit outstanding
- 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 banks held at the BCE comprise:

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

The deposits of other financial institutions at the BCE comprise:

- All liabilities of the BCE to other financial institutions (*otras sociedades financieras*, as defined in the BCE's Metodología: Información Estadística Mensual, 4th Edition of May 2017), with the exception of deposits of the BIESS, including those held in trust funds ("fideicomisos BIESS y fideicomisos IESS).

H. Adjustors to the floor on the change in the stock of net international reserves

45. Adjustor on external borrowing. 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 5 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.

46. Adjustor on multilateral and bilateral disbursements. The floor on net international reserves will be adjusted downward/upward by the shortfall/excess in loan disbursement by multilateral institutions (the IADB, World Bank, CAF, and FLAR), bilateral partners (e.g., China) and grants, relative to the baseline projection reported in Table 6. 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.

47. Adjustor on oil prices. The floor on the on net international reserves will be adjusted upward/downward by US$23.85 million at corresponding test dates for each US$1 per barrel that the average Ecuador mix crude oil price is above/below the program assumption defined in the Table 3. This adjustor is capped at US$119.33 million at corresponding test dates. The average price of Ecuador mix oil price will be calculated as the total value of crude oil exports divided by the total volume of oil exports over the period since the prior test date.

Monitoring

48. The change in net international reserves (NIR) will be measured as the cumulative change in the stock of NIR at each test date relative to the stock on June 30, 2020 (which stood at US$ -4,807 billion for the end-September and end-December 2020 test dates, and relative to the stock of NIR on December 31 of the preceding year for subsequent test dates.

49. Foreign exchange asset and liability data will be provided to the Fund at weekly frequency within 5 business days following the end of the week.

I. Floor on social assistance coverage of poor families under central government's social programs

Definitions

50. Social assistance coverage of poor families for the purpose of the program is computed as the sum of all active beneficiary families in the three bottom deciles of the income distribution that benefit from at least one social assistance programs. Poor beneficiary families are defined according to information in the RS2018. Coverage expansion will occur through the following social assistance programs: Bono de Desarrollo Humano (BDH), Bono de Desarrollo Humano Variable (BDH-V), Personas con discapacidad, Pensión para Adultos Mayores, Mis mejores años, and Pensión Toda Una Vida. The level (size) of benefits of any of the cash transfer programs in the bottom three deciles of the income distribution should not be reduced (with respect to their level on September 30, 2020).

Monitoring

51. Monthly data on (i) number of poor families with at least one active beneficiary in any of the social assistance programs, and (ii) monthly data on numbers of registries with information updated and validated following SR2018 by income decile will be provided to the Fund with a lag of no more than 30 days after the end of each month.

OTHER INFORMATION REQUIREMENTS

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

52. In accordance with IMF Government Finance Statistics Manual (GFSM) 2014 and Public Sector Debt Guide for compilers and users total gross debt covers 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.

53. 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.

54. For the purpose of the program, Ecuador's NFPS debt includes the following instruments:

- Debt Securities including short term liquidity instruments (held by nonresidents, and by residents not included in the Non-Financial Public-Sector entities)
- Loans
- Other Accounts Payables

55. 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

56. The data on NFPS stock of debt in US$ will be provided to the Fund monthly with a lag of no more than 60 days after the end of each month. The data submission will also include cross-holdings among NFPS entities.

Daily

57. Daily monetary and financial data in the template agreed with Fund staff, no later than 1 business days after the end of the day. This template at least will include: (a) movements of international reserves by inflows and outflows. b) Main balance sheet accounts of financial institutions, broken down by private banks, cooperatives and mutual banks. c) Daily oil production.

Weekly

58. Consolidated balance sheets of the banking system, by main accounts, including deposits in the banking system, available funds, credit to the private sector, and credit to the government.

59. BCE balance sheet. Financial indicators: deposits of banks at the BCE

60. Weekly monetary data in the template agreed with Fund staff, no later than 5 business days after the end of the week.

61. Weekly data on international reserves and foreign currency liquidity, in line with SDDS requirements (see http://data.imf.org/?sk=2DFB3380-3603-4D2C-90BE-A04D8BBCE237)**, no later than 5 business days after the end of the week.**

Monthly

62. Data on stocks and flows (above- and below the line), disaggregated by each subsector of the NFPS (budgetary central government and CFDD, rest of the central government, subnational governments, SOEs and social security) using the templates previously agreed with the IMF team. One template with the detailed data on revenues and expenditures of each of the subsectors and the consolidations between them, and the other template data by subsectors with a summary of above the line data and the comparison with the below the line data for monitoring the statistical discrepancy and data on stocks of financial assets and liabilities and the financing (below the line data) also by subsectors.

63. 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.

64. 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.

65. 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.

66. Export price of Ecuador mix crude oil, with a lag of no more than 20 days after the closing of each month.

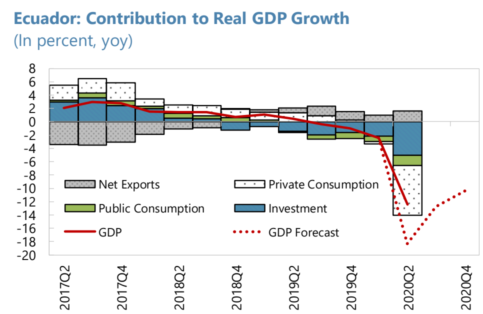
Quarterly

67. Detailed balance of payments data, no later 90 days after the end of the quarter.

Statement by the Staff Representative on Ecuador
September 30, 2020

1. This statement provides information that has become available since the staff report was finalized. This information does not alter the thrust of the staff appraisal.

2. **Preliminary National Accounts data indicate that economic activity declined by 12.4 percent (y-o-y) in 2020:Q2 (compare to a 2.3 percent decline in 2020:Q1).** The contraction in Q2—driven by sharp declines in investment and private consumption (chart)—was milder than staff's forecast of 18.4 percent (y-o-y). High-frequency indicators point to continued improvements in 2020:Q3, with a y-o-y decline in economic activity index at 12½ percent in July against 15½ in June. With the 2020:Q2 growth outturn better than anticipated, staff will re-assess annual growth projections as more high-frequency data become available.



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

3. **The authorities have launched an investigation into a potential financial fraud involving the police force pension fund (*Instituto de Seguridad Social de la Policía Nacional*, ISSPOL).** About $532 million (about 0.6 percent of GDP) of ISSPOL's assets (a third of the fund's balance sheet) could be compromised due to transactions that occurred during 2014-2017. Preliminary cash flow analysis indicates that the fund would be able to continue to meet its payment obligations in the coming months with no urgent need for a cash injection. With the process being in early stages and information so far limited, it is not yet clear whether, when, and by how much the emerging pension liabilities will need to be absorbed by the central government. Since ISSPOL is consolidated with other government agencies in the non-financial public sector (NFPS), public debt and NPFS balance targets may not be affected. However, to the extent that the central government has to bear additional costs beyond program assumptions, those would have to be reflected in the program and could potentially open further financing gaps (up to a maximum corresponding to the estimated fraudulent amount of $532 million).

4. **The authorities have passed the COPLAFIP regulation on data provision, meeting the last of the five prior actions of the new program.** The regulation—one of two COPLAFIP regulations under the program—took the form of a ministerial agreement. The regulations for the rest of the amendments, which is a structural benchmark for November 2020, will be adopted by an executive decree encompassing the ministerial agreement on data provision.

5. **Updated World Bank financing plans for Ecuador indicate slightly lower disbursements by a cumulative $58 million over 2020–22.** The Bank informed staff this week

of some changes to their disbursement plans as below. These will be reflected in the projections in the next review.

Ecuador—Projected World Bank's Disbursements
(in millions of US dollars)

	2020	2021	2022	Cumulative
Program profile	1,428	1,076	100	2,604
Updated profile	1,481	935	130	2,546

Source: The World Bank

INTERNATIONAL MONETARY FUND

ECUADOR

September 23, 2020

ASSESSMENT OF THE RISKS TO THE FUND AND THE FUND'S LIQUIDITY POSITION

EXECUTIVE SUMMARY

The supplement assesses the risks to the Fund arising from Ecuador's request for a 27-month arrangement under the Extended Fund Facility (EFF) and its effects on the Fund's liquidity position, in accordance with the policy on exceptional access. The proposed access of SDR 4.6 billion (661 percent of quota), with frontloading of the first two purchases, would exceed the annual and cumulative access limits under the GRA. Ecuador has prior outstanding credit to the Fund of SDR 1.6 billion (236 percent of quota) following purchases under the RFI and its previous EFF arrangement.

Key Issues and Findings

- Ecuador's capacity to repay is adequate under the baseline, but subject to significant risks and contingent on full program implementation and financing from other creditors.

- The proposed EFF arrangement will have a moderate impact on liquidity. Upon approval, the Fund's Forward Commitment Capacity would decline by about 3 percent.

- Ecuador will become the sixth-largest borrower after first-year drawings, and Fund exposure to Ecuador would peak at 38 percent of the current level of the Fund's precautionary balances.

- Risks to the program and to the Fund are elevated, including from the frontloading of access ahead of key reform measures requiring legislative approval. Strong early actions and support from a broad range of political candidates for the objectives of the program are critical to mitigate risks.

Approved By
Andrew Tweedie and Maria Gonzalez

Prepared by the Finance and Strategy, Review and Policy Departments.

CONTENTS

INTRODUCTION

1. The note assesses the risks to the Fund arising from Ecuador's request for a 27-month arrangement under the Extended Fund Facility (EFF) and its effects on the Fund's liquidity, in accordance with the policy on exceptional access. The Ecuadorian authorities have requested a 27-month arrangement under the Extended Fund Facility with access of SDR 4.6 billion (661 percent of quota) to help alleviate exceptional balance-of-payments pressures in the wake of multiple severe external shocks, restore macroeconomic stability, and support structural reforms. With outstanding credit to the Fund currently at 236 percent of quota, the proposed frontloaded access upon program approval and at the First Review of SDR 2.8 billion (407 percent of quota) and cumulative access during the program period exceeds the respective access limits and require exceptional access.

BACKGROUND

2. Ecuador currently has outstanding credit to the Fund of SDR 1.6 billion (236 percent of quota) from a partially drawn EFF arrangement in 2019, and RFI purchases in 2016 and 2020.

- Ecuador purchased SDR 469.7 million (67 percent of quota) in May 2020 to meet urgent balance of payment (BOP) needs following the COVID-19 outbreak, with Ecuador one of the hardest hit countries in Latin America.

- The previous EFF arrangement was approved on March 11, 2019, for an amount of SDR 3.0 billion (435 percent of quota). Three out of eleven scheduled reviews were completed before the program went off track, with only 145 percent of quota drawn before cancellation of the arrangement in April 2020. Misreporting of fiscal data after the completion of the combined second and third reviews masked significantly larger than targeted fiscal deficits. This incidence revealed serious shortcomings in institutional capacity and limited inter-agency coordination, the main cause of the deficiencies in the collection and compilation of fiscal accounts data. While the 2019 EFF arrangement was active, the authorities took steps to improve public finances, strengthen the foundations for dollarization, and enhance the social safety net.

- Ecuador also purchased SDR 261.6 million under the RFI in 2016, following an earthquake that caused significant damage to infrastructure, housing and agriculture. Of this, SDR 163.5 million remains outstanding (pending repurchases through August 2021).

3. Ecuador has long history of borrowing from the Fund. The country was among the top users of Fund resources prior to the mid-1990s, though with a mixed track record of program implementation. Past access was significantly less than under the current EFF:

- Prior to the 2019 EFF, Ecuador's arrangements were Stand-By Arrangements (SBAs): two approved in the 2000s, two in the 1990s and five in the 1980s (Table 1). An SBA was approved on March 23, 2003, for an amount of SDR 151 million (60 percent of quota), with SDR 60 million (21.6 percent of quota) purchased before the SBA went off track after the First Review. The

12-month SBA approved in April 2000, with access of SDR 227 million (75 percent of quota), was fully drawn. Two prior SBAs in the 1990s went off track. The SBA approved on May 11, 1994, originally for 23 months, was augmented in November 1994 (SDR 43.9 million) to support a debt operation, bringing total access to SDR 174 million, but was cancelled in early December 1995. Ecuador had been among the top users of Fund resources prior to the mid-1990s.

- Ecuador has never incurred arrears to the Fund. However, Ecuador's debt became unsustainable earlier this year following the RFI purchase due to the macro-economic situation deteriorating further since then, requiring a debt operation to reduce financing needs and restore debt sustainability. Ecuador has an extensive prior history of restructurings since the 1980s, including in 1999–2000, 2003–04, and most recently in 2008–09. Ecuador adopted full dollarization in response to the 1999–2000 crisis.

4. Ecuador's external and public debt stocks are elevated following rapid increases in recent years and are highly susceptible to macroeconomic and fiscal shocks. Public external debt is projected to reach 52 percent of GDP at end-2020 (Table 2)—about double the median of recent exceptional access cases (Figure 1), with advanced economies accounting for most borrowers with higher public external debt burdens. Obligations to the private sector and to official creditors comprise roughly equal shares (DSA). Total public debt is projected to peak at 68.9 percent of GDP at end-2020, up from 20 percent of GDP at end-2013, also well above the median of comparators. Public debt is projected to ease over the medium term, conditional on full adherence to program policies and the debt operation, but would remain well above the median exceptional access case.

5. Ecuador faced significant financing constraints that prompted the recent debt restructuring. Public gross financing needs (GFN) are projected to reach 16.1 percent of GDP at end-2020, compared with around 7 percent of GDP at end-2013, with the impact of the COVID-19 and oil price shocks projected to drive up GFN relative to exports (82.5 percent) and government revenue (53.4 percent) at end-2020. In response to these increasing debt vulnerabilities, the authorities recently concluded a bond exchange covering US$17.4 billion of outstanding global bonds. As discussed in the staff report, the debt exchange generated significant reductions in interest payments (US$5.7 billion over 2020–25) and amortizations (US$5.6 billion over 2022–25). In addition, the reprofiling of bilateral obligations to Chinese creditors is expected to yield around US$815 million in savings in 2020–21. Bilateral assurances have been provided up to 2022. Ecuador's residual financing needs are estimated at some US$6.5 billion over 2020–22, before Fund support.

6. Reducing GFNs and restoring sustainability is contingent on fully implementing program policies, following the successful debt restructuring and the securing of needed bilateral financing assurances for 2021–22 to make debt sustainable with high probability. Public external debt service at end-2020 is projected at 7 percent of GDP (compared to 2.5 percent at end-2013), or 32 percent of exports. Going forward, on account of the debt operation, external debt service is projected around 15–20 percent of exports in 2021–23, rising to a peak of 28 percent in 2026–27—below the median of exceptional access cases of nearly 40 percent of exports (Table 3; Figure 3b, Panel 1). Gross financing needs are projected at around 5 percent of GDP by 2025 (see

DSA), within program parameters, assuming fiscal consolidation and materialization of bilateral and multilateral financing as per existing assurances, and market access under normal conditions.

ACCESS UNDER THE EFF ARRANGEMENT—RISKS AND IMPACT ON FUND FINANCES

A. Risks to the Fund

7. Access under the proposed EFF arrangement would exceed both annual and cumulative limits and significantly increase the Fund's exposure to Ecuador (Figure 2). Proposed access of SDR 4.6 billion (661 percent of quota) corresponds to remaining estimated financing gaps of some US$6.5 billion in 2020–22, after accounting for contributions towards closing gaps from a successful restructuring of external bonds, reprofiling of external debt, financing from IFIs and official bilateral creditors, and fiscal consolidation. With current credit outstanding to the Fund at SDR 1.6 billion (236 percent of quota), the proposed front-loaded access under the arrangement would exceed both the annual limit (currently 245 percent of quota) and cumulative limit (435 percent of quota). After the scheduled purchases at approval and first review, both in 2020, credit outstanding will rise to SDR 4.4 billion, making Ecuador the sixth-largest borrower in absolute terms and the fourth-largest under a full drawing scenario and compared with current exposures for other members. If Ecuador makes all purchases as scheduled, peak Fund exposure would reach 874 percent of quota in 2022, a little above the median of exceptional access cases (845 percent of quota).

8. While most metrics of peak exposure and peak obligations would be broadly comparable to other exceptional access cases, peak Fund exposure and debt service would be high in relation to international reserves (Figures 3a and 3b).

- Peak Fund credit outstanding will be slightly above the median relative to total external debt (16.3 percent), and below the median for GDP (8.4 percent) and government revenue (25 percent). Relative to gross international reserves (GIR), Fund credit peaks at 252 percent in 2020, the highest among comparators, given currently low reserves. Notwithstanding rapid projected reserve accumulation (Table 2), Fund credit is projected to remain elevated at 77 percent of GIR in 2025, when EFF repurchases begin, and to average 41 percent over 2025–30.[1]

- Debt service to the Fund is relatively stretched out in line with EFF terms, reaching around SDR 1 billion annually during the period 2025–29. Peak metrics for debt service to the Fund relative to exports and to public debt service are below the median of comparators (Figure 3b). However, notwithstanding the rapid projected accumulation of reserves projected in the baseline, debt service to the Fund would peak at a relatively high 16 percent of GIR in 2027; and

[1] While the central bank does not intervene in foreign exchange markets, GIR remains relevant for assessing capacity to repay in fully dollarized economies such as Ecuador, given the public sector's need to retain adequate liquidity buffers for both foreign and domestic payments.

net international reserves are projected to remain deeply negative at program completion, making it critical to sustain access to financing and continuing creditor support.

9. Capacity to repay is adequate under the program's baseline assumptions, but subject to elevated risks and contingent on full program implementation and financing from other creditors (Table 3). The program entails a number of necessarily ambitious economic policies and objectives, underpinning a sustained recovery and significantly improved liquidity situation under the baseline (Table 2), including through a resumption of market access as well as support from official creditors. Restoring liquidity buffers underpinned by program implementation is critical since, as a fully dollarized economy, Ecuador has very constrained room for policy maneuver in case of possible new shocks. While access under the program is heavily frontloaded,[2] several commitments requiring legislative approval—including the central bank law and tax reforms—are scheduled for later implementation. Capacity to repay could be severely constrained if the program is not implemented as envisaged under the baseline.

- In a downside scenario where the program is not implemented beyond the first review, access to Fund resources and other IFIs could be cut off, leading to the reemergence of large financing gaps if Ecuador does not regain market access.

- In a stress test where macroeconomic conditions do not improve (historical scenario, Table 3), Fund credit could peak at 347 percent of GIR in 2022, and average 144 percent over 2025–30. The ratio of Fund obligations falling due to GIR in this scenario would peak at 60 percent in 2027, suggesting liquidity constraints on repayment even if other indicators (obligations to the Fund relative to GDP, exports and government revenue) would remain more contained.

10. Enterprise risks are elevated. The new program will increase risks associated with Fund lending, which are already significant in light of the COVID-19 pandemic. As noted in the staff report, risks to the program arise from an uncertain economic outlook, weaknesses in institutional capacity,[3] a fragmented political landscape and forthcoming elections, and could lead to policy slippages and/or reversals, and larger-than-envisaged financing gaps. These would, in turn, pose risks to Ecuador's capacity to repay. Key mitigation measures include conditionality under the program, including quantitative targets, which would allow for course correction; the pace of fiscal consolidation that will be calibrated to be mindful of growth; early actions to strengthen institutional capacity and address pressing issues, building on the recent approval of amendments to the organic budget code; demonstration of political capacity to implement policies ahead of program approval; and a robust communication strategy to secure broad buy in for program objectives. Residual risks need to be weighed against the reputational risk of the Fund not supporting a member facing

[2] The need for this high degree of frontloading could have been mitigated with additional financing from key IFIs and/or further direct support from bilateral creditors.

[3] This includes capacity to implement reforms to fiscal data reporting, which are needed to ensure timely provision of data—in a new format consistent with TA recommendations—needed for program monitoring.

enormous challenges and that stands ready to take the necessary steps to address them consistent with resolving its balance of payments needs.

11. Income risks are expected to be moderate to low. The proposed EFF arrangement is expected to generate additional lending income for the Fund and contribute to precautionary balances, which at end-FY2020 stood at around SDR 16 billion, about 3.5 times the proposed access. GRA charges based on the proposed drawings are projected to total around SDR 1 billion (152 percent of quota) through 2034. This represents 12.7 percent of the projected lending income through FY 2026, based on existing arrangements under the GRA. The income risks from the proposed EFF arrangement are expected to be moderate to low, though subject to uncertainty regarding global interest rates. Income from the largest borrower would remain dominant. However, in the event of arrears after drawings under the proposed EFF arrangement, the residual burden sharing capacity will be insufficient to cover them. GRA charges for Ecuador would amount to SDR 115.4 million in 2021, and peak at SDR 176.3 million by 2025, far higher than the Fund's residual burden-sharing capacity.

B. Impact on the Fund's Liquidity Position and Credit Exposure

12. The proposed arrangement will have a moderate impact on the Fund's liquidity position. The Forward Commitment Capacity (FCC), which stands at SDR 160.4 billion as of September 18, 2020, will fall by about 3 percent, following the approval of this arrangement (Table 4). No additional second-round impact is expected given that Ecuador is not a member of the Financial Transactions Plan (FTP).

13. The proposed EFF arrangement would significantly increase the Fund's exposure to Ecuador (Table 4, Figures 4 and 5).

- Ecuador will become the sixth-largest borrower by December 2020, following purchases at approval and at completion of the first review, combined with the RFI purchase in May 2020. Compared with current exposures for other members, if Ecuador makes full drawings under the arrangement it would account for 7 percent of total credit outstanding under the GRA, higher than Pakistan and Greece (currently the fourth and fifth largest borrowers, respectively).

- GRA exposure to Ecuador would amount to over one quarter of the Fund's precautionary balance after first year drawings, rising to 38.2 percent by 2022 when the exposure peaks (assuming the current level of precautionary balances at end-FY20).

- Credit concentration to top five borrowers would rise from 73.0 percent to 74.4 percent, considering Ecuador's first year drawings.

- Ecuador's share of repurchases in total current repurchases is projected to increase rapidly from 0.3 percent in 2023 to 66.7 percent by 2028, based on current arrangements. However, this ratio is expected to moderate as new arrangements are approved.

ASSESSMENT

14. The proposed EFF arrangement is designed to restore macroeconomic stability and advance key structural reforms. Ecuador experienced multiple external shocks that compounded pre-existing vulnerabilities. The economic and social impact of COVID-19 has been severe. Since the approval of the RFI purchase in May, the economy has continued to deteriorate. In response, the proposed EFF-supported program aims to stabilize the economy, support lives and livelihoods, advance reforms to strengthen domestic institutions and the foundations for dollarization, and anchor strong, durable and inclusive private sector-led growth beyond the crisis. Exceptional access is needed under the proposed EFF arrangement to help close financing gaps and support the authorities' efforts, with proposed access exceeding both annual and cumulative limits,

15. While Ecuador's capacity to repay is adequate under the program's baseline assumptions, it is subject to significant risks and contingent on full program implementation and financing from other creditors. As highlighted in the staff report, key near-term risks include a more severe and protracted global pandemic, persistently low oil prices, and the reemergence of social tensions. These risks—if they materialize in the current context of constrained institutional capacity, a fragmented political landscape and forthcoming elections—could lead to policy slippages and/or reversals, and larger-than-envisaged financing gaps. Moreover, with Ecuador's liquidity buffers limited and policy levers under dollarization limited to fiscal policy, any further downside shocks—such as a loss of confidence, a drop in oil prices, or shortfalls in financing from other creditors—would add to the burden on fiscal policy. The frontloading of access and backloading of critical reforms, including the central bank law and tax reforms, pose additional risks.

16. Successful program implementation is therefore critical. If program policies are fully implemented as envisaged, building on the recent successful debt exchange and support from official creditors, Ecuador's debt would be sustainable with high probability and its capacity to repay adequate. Program implementation ahead of May 2021 elections will require substantial recourse to executive powers, and after the elections will hinge on legislative support. Strong early actions to continue strengthening institutions and policy frameworks, including through prior actions and early structural benchmarks, and support from a broad range of presidential candidates for the objectives of the program are thus critical to mitigate risks to program implementation. Political assurances are deemed adequate. However, there is little room for slippage, as partial or non-implementation would delay capital market re-access and the rebuilding of liquidity buffers, risk reemergence of the pressures that led to the current crisis, and severely strain Ecuador's capacity to repay the Fund.

17. The proposed access under the EFF will have a moderate impact on Fund's liquidity and will significantly increase the Fund's exposure to Ecuador. On approval of the arrangement, the proposed access would reduce Fund's liquidity by about 3 percent. Ecuador will become the sixth-largest borrower after the first-year drawings, after Greece, while credit concentration to the top five borrowers would rise from 73.0 percent to 74.4 percent. GRA exposure to Ecuador would amount to 38 percent of the Fund's precautionary balances (assuming the current level at end-FY2020) if all purchases are made as scheduled.

Table 1. Ecuador: IMF Financial Arrangements and Fund Exposure, 1983–2030
(In millions of SDRs)

Year	Type of New Arrangement	Date of Arrangement	Date of Expiration or Cancellation	Amount of New Arrangement	Amount Drawn	Fund Exposure 1/	
1983	SBA	25-Jul-1983	24-Jul-1984	158	158	204	
1984						243	
1985	SBA	11-Mar-1985	10-Mar-1986	106	106	327	
1986	SBA	15-Aug-1986	10-Jun-1987	75	15	398	
1987						345	
1988	SBA	04-Jan-1988	28-Feb-1989	75	15	301	
1989	SBA	15-Sep-1989	28-Feb-1991	110	39	247	
1990						186	
1991	SBA	11-Dec-1991	10-Dec-1992	75	19	128	
1992						73	
1993						52	
1994	SBA	11-May-1994	11-Dec-1995	174	99	136	
1995						117	
1996						101	
1997						99	
1998						49	
1999						0	
2000	SBA	19-Apr-2000	31-Dec-2001	227	227	113	
2001						151	
2002						227	
2003	SBA	21-Mar-2003	20-Apr-2004	151	60	262	
2004						187	
2005						55	
2006						15	
2007						0	
:							
:							
2016						262	
2017						262	
2018						262	
2019	EFF	11-Mar-2019	01-May-2020		1,012	1241	
2020	RFI + Requested EFF				*3,310*	*4,419*	2/ 3/
2021	Requested EFF				*1065*	*5,386*	2/
2022	Requested EFF				*710*	*6,096*	2/
2023						*5,925*	2/
2024						*5,521*	2/
2025						*4,738*	2/
2026						3,901	2/
2027						2,963	2/
2028						2,026	2/
2029						1,142	2/
2030						373	2/

Source: IMF Finance Department.

1/ As of end December, unless otherwise stated.
2/ Figures including transactions under the proposed program are in italics. Fund exposure is derived assuming purchases are made as per schedule and Ecuador remains current on all its scheduled repurchases.
3/ Includes a purchase of SDR 469.7 million under the RFI in May 2020, and purchases of SDR 1,452 million upon approval of the EFF and SDR 1,452 million upon completion of the first review.

Table 2. Ecuador: Selected Macroeconomic Indicators, 2013–25

(Baseline; in percent of GDP, unless otherwise indicated)

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Real GDP (percentage change)	4.9	3.8	0.1	-1.2	2.4	1.3	0.1	-11.0	4.8	1.3	1.7	2.0	2.3
Inflation (percent, period average)	2.7	3.6	4.0	1.7	0.4	-0.2	0.3	0.0	1.0	2.3	1.4	1.0	1.0
Fiscal balance	-4.6	-5.2	-6.1	-8.2	-4.5	-3.2	-3.2	-8.9	-2.9	0.6	1.8	2.4	2.3
Current account balance	-1.0	-0.7	-2.2	1.1	-0.1	-1.2	-0.1	-2.0	-0.1	0.3	0.6	0.8	0.6
Gross financing needs	7.1	10.8	14.3	19.1	16.7	10.5	10.3	16.1	8.1	4.2	4.1	3.2	4.7
External public debt	13.3	18.7	22.3	28.1	32.0	33.8	37.9	51.7	52.0	50.9	48.5	46.2	43.5
Total public debt	20.0	27.1	33.8	43.2	44.6	46.1	51.8	68.9	67.4	65.8	62.3	60.0	56.1
Memorandum items:													
Nominal GDP (US$ million)	95,130	101,726	99,290	99,938	104,296	107,562	107,436	93,078	99,247	102,803	106,026	109,550	113,470
Gross international reserves (US$ million)	4,178	3,762	2,351	4,216	2,006	2,158	2,933	2,475	3,303	5,042	6,341	8,108	8,644

Sources: Ecuadorian authorities and IMF staff estimates and projections.

Table 3. Ecuador: Capacity to Repay Indicators, 2020–30 1/2/

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Exposure and Repayments (In SDR millions)											
GRA credit to Ecuador	4,419.5	5,386.4	6,096.4	5,924.7	5,521.3	4,738.2	3,901.1	2,963.3	2,025.5	1,141.9	372.8
(In percent of quota)	633.4	772.0	873.8	849.2	791.4	679.1	559.1	424.7	290.3	163.7	53.4
Charges due on GRA credit 3/	42.3	24.6	115.4	146.7	162.2	164.8	176.3	145.9	110.4	72.3	34.2
Repurchases under EFF	0.0	0.0	0.0	54.2	168.6	665.6	837.2	937.8	937.8	883.6	769.2
Repurchases under RFI	32.7	98.1	0.0	117.4	234.9	117.4	0.0	0.0	0.0	0.0	0.0
Debt service due on GRA credit	173.1	213.5	146.7	333.8	568.2	959.3	983.1	1,048.2	1,010.1	917.7	779.8
Debt and Debt Service Ratios 4/											
In percent of GDP											
Total external debt	60.2	57.7	57.6	57.8	57.1	54.7	51.0	47.9	45.0	42.5	40.3
External debt, public	51.7	52.0	50.9	48.5	46.2	43.5	40.1	36.9	33.8	31.2	28.8
GRA credit to Ecuador	6.7	7.6	8.4	7.9	7.1	5.9	4.7	3.4	2.3	1.2	0.4
Public external debt service	7.0	3.3	4.0	4.6	5.1	5.6	6.4	6.4	6.2	5.8	5.6
Debt service due on GRA credit	0.3	0.3	0.2	0.4	0.7	1.2	1.2	1.2	1.1	1.0	0.8
In percent of Gross International Reserves											
Total external debt	2,263.2	1,734.8	1,173.5	965.7	770.9	717.9	679.0	643.2	586.6	515.2	451.4
External debt, public	1,946.2	1,562.1	1,037.1	811.3	624.1	570.4	534.2	495.7	441.1	378.5	323.2
GRA credit to Ecuador	251.6	229.8	170.4	131.6	95.9	77.2	62.2	45.9	29.4	14.8	4.3
Debt service due on GRA credit	9.9	9.1	4.1	7.4	9.9	15.6	15.7	16.3	14.7	11.9	9.0
In percent of Exports of Goods and Services											
Public external debt service	31.5	15.2	17.9	20.3	22.3	24.5	27.7	27.5	26.8	24.6	23.7
Debt service due on GRA credit	1.2	1.4	0.9	2.0	3.2	5.2	5.1	5.2	4.8	4.2	3.4
In percent of General Government Revenues											
Public external debt service	23.2	10.6	11.5	13.0	14.3	15.9	18.0	17.9	17.6	16.2	15.6
Debt service due on GRA credit	0.9	1.0	0.6	1.3	2.1	3.4	3.3	3.4	3.2	2.8	2.3
In percent of Total External Debt											
GRA credit to Ecuador	11.1	13.2	14.5	13.6	12.4	10.8	9.2	7.1	5.0	2.9	1.0
In percent of Total Public External Debt											
GRA credit to Ecuador	12.9	14.7	16.4	16.2	15.4	13.5	11.6	9.3	6.7	3.9	1.3
In percent of Total Public External Debt Service											
Debt service due on GRA credit	3.8	9.1	5.0	9.7	14.3	21.1	18.4	19.0	18.0	17.1	14.5
Historical Scenario 5/											
In percent of GDP											
GRA credit to Ecuador	6.7	8.2	9.2	9.0	8.4	7.2	5.9	4.5	3.1	1.7	0.6
Debt service due on GRA credit	0.3	0.3	0.2	0.5	0.9	1.5	1.5	1.6	1.5	1.4	1.2
In percent of Gross International Reserves											
GRA credit to Ecuador	251.6	306.7	347.1	337.3	314.4	269.8	222.1	168.7	115.3	65.0	21.2
Debt service due on GRA credit	9.9	12.2	8.4	19.0	32.4	54.6	56.0	59.7	57.5	52.3	44.4
In percent of Exports of Goods and Services											
GRA credit to Ecuador	30.2	36.8	41.7	40.5	37.8	32.4	26.7	20.3	13.9	7.8	2.5
Debt service due on GRA credit	1.2	1.5	1.0	2.3	3.9	6.6	6.7	7.2	6.9	6.3	5.3
In percent of General Government Revenues											
GRA credit to Ecuador	22.2	27.1	30.7	29.8	27.8	23.8	19.6	14.9	10.2	5.7	1.9
Debt service due on GRA credit	0.9	1.1	0.7	1.7	2.9	4.8	4.9	5.3	5.1	4.6	3.9

Sources: Ecuadorian authorities, IMF Finance Department, and IMF Staff estimates.
1/ Assumes full drawings and indicators based on the baseline macroeconomic scenario presented in the staff report.
2/ Includes GRA basic rate of charge, surcharges, service fees, and SDR charges.
3/ Includes charges due on GRA credit and repurchases.
4/ Staff projections for external debt, GDP, gross international reserves, and exports of goods and services, are based on the staff report for the new EFF.
5/ Assumes that GDP, GIR, exports of goods and services, and government revenue under the baseline scenario stay at the 2020 level over the projection period.

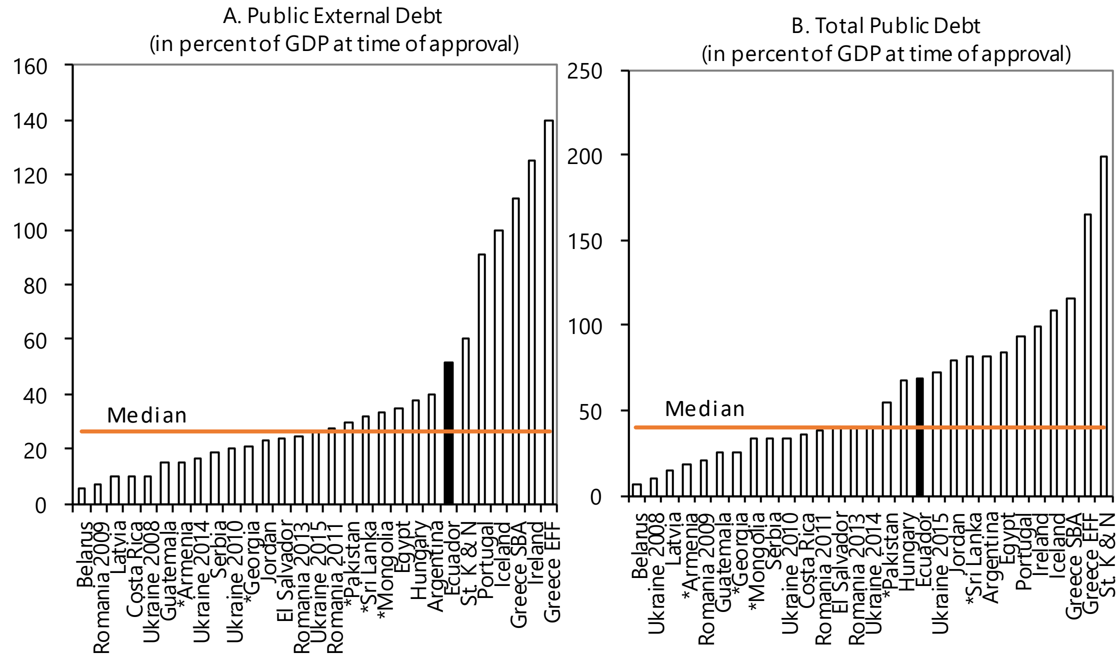
Table 4. Ecuador: Impact on GRA Finances
(millions of SDR unless otherwise noted)

	As of 09/18/2020
Liquidity measures	
Current one-year Forward Commitment Capacity (FCC)	160,400.0
Impact of the approval of the EFF arrangement on the FCC 1/	-4,615
(in percent of current one-year FCC)	-2.9
Prudential measures	
Fund GRA credit outstanding to Ecuador 2/	3,032
In percent of current precautionary balances	19.0
In percent of total GRA credit outstanding	3.4
Fund GRA credit outstanding to top five borrowers	62,090
In percent of total GRA credit outstanding	73.0
In percent of total GRA credit outstanding including Ecuador's first year drawings under the EFF	74.4
Ecuador's annual GRA charges in percent of Fund's residual burden sharing capacity for 2020/21	639
Memorandum items	
Fund's precautionary balances (end-FY2020)	16,000
Fund's residual burden-sharing capacity 3/	16.6

Sources: Ecuadorian authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ A single country's negative impact on the FCC is defined as the country's sum of new Fund credit and undrawn commitments minus repurchases one year forward.
2/ Projected credit outstanding for Ecuador at time of approval of the proposed EFF arrangement based on the current repayment schedule and including first drawing.
3/ Burden-sharing capacity is calculated based on the floor for remuneration which, under current policies, is 85 percent of the SDR interest rate. Residual burden-sharing capacity is equal to the total burden-sharing capacity minus the portion being utilized to offset deferred charges and the loss in capacity due to nonpayment of burden sharing adjustments by members in arrears.

Figure 1. Debt Ratios for Recent Exceptional Access Arrangements 1/ 2/

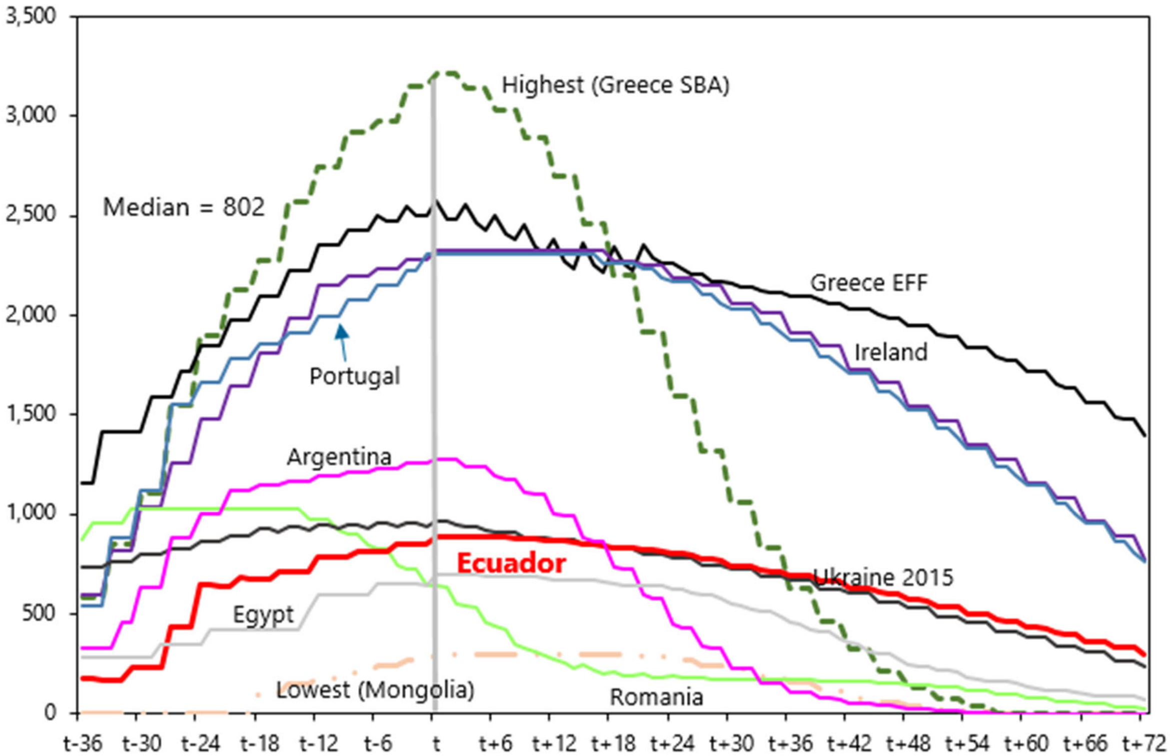


Source: IMF Finance Department.

1/ Estimates as reported in relevant staff reports on the request or augmentation of SBAs or EFF arrangements approved since September 2008. For Ecuador, Fund purchases in 2020 are included.
2/ Asterisks indicate PRGT-eligible countries at the time of the program.

Figure 2. Credit Outstanding in the GRA around Peak Borrowing [1/]

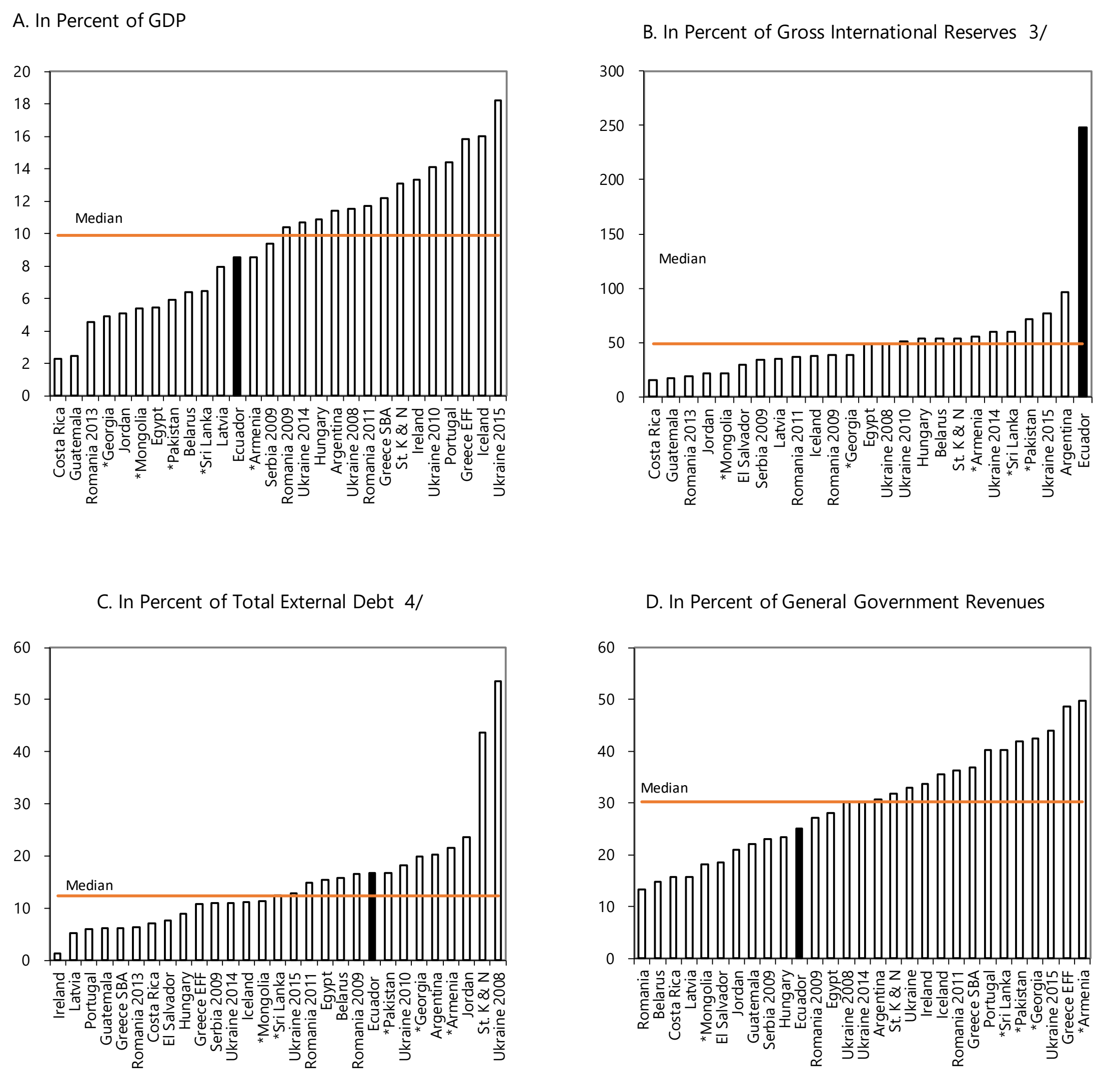
(in percent of quota [2/])



Source: IMF Finance Department.

1/ Peak borrowing "t" is defined as the highest level of credit outstanding for a member on a given month. Repurchases are assumed to be on an obligation basis.
2/ Based on quotas at the time of approval, i.e., pre-14th Review quotas for all countries except Argentina and Ecuador. Median credit outstanding at peak is 845 percent of quota; average is 1,043 percent of quota.

Figure 3a. Peak Fund Exposure Ratios for Recent Exceptional Access Cases 1/ 2/



Source: IMF Staff estimates, and World Economic Outlook.

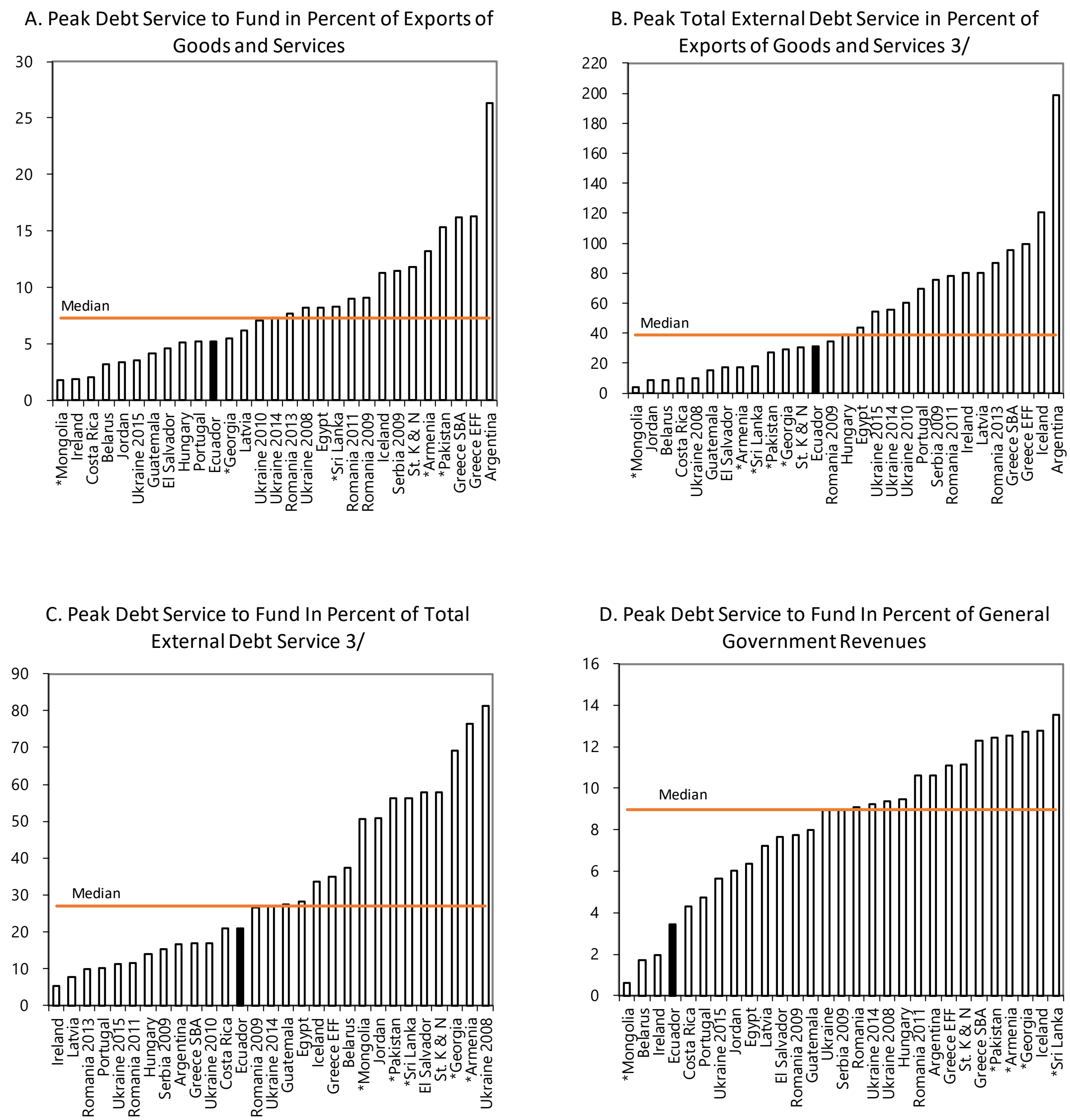
1/ Estimates as reported in relevant staff reports on the request of SBAs or arrangements under the EFF approved since September 2008.

2/ Asterisks indicate PRGT-eligible countries at the time of the program. In Panel F, Georgia's debt service to the Fund includes one from PRGF loan.

3/ Excluding arrangements with members belonging to the euro area at the time of the approval of the arrangement: Greece, Ireland, and Portugal. For Ecuador, peak relative to GIR is in 2020 (Table 2).

4/ For arrangements of which total external debt (or debt service) ratio is not available, public external debt ratio is shown instead.

Figure 3b. Peak Debt Service Ratios for Recent Exceptional Access Cases [1/ 2/]



Source: IMF Finance Department.

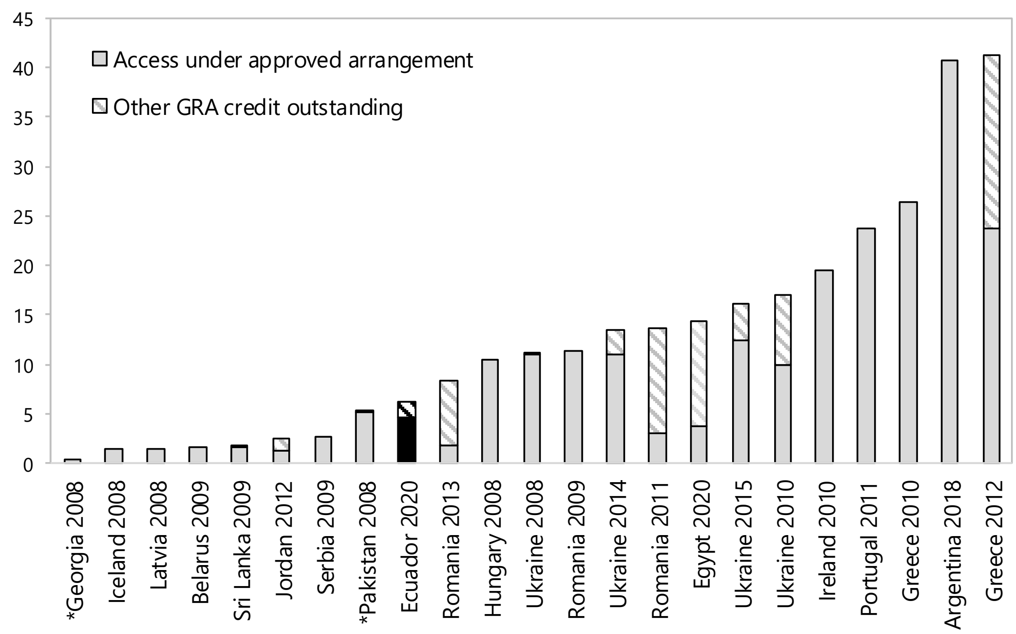
1/ Estimates as reported in relevant staff reports on the request of SBA, or arrangements under the EFF approved since September 2008.

2/ Asterisks indicate PRGT-eligible countries at the time of the program. Georgia's debt service to the Fund includes one from a PRGT loan.

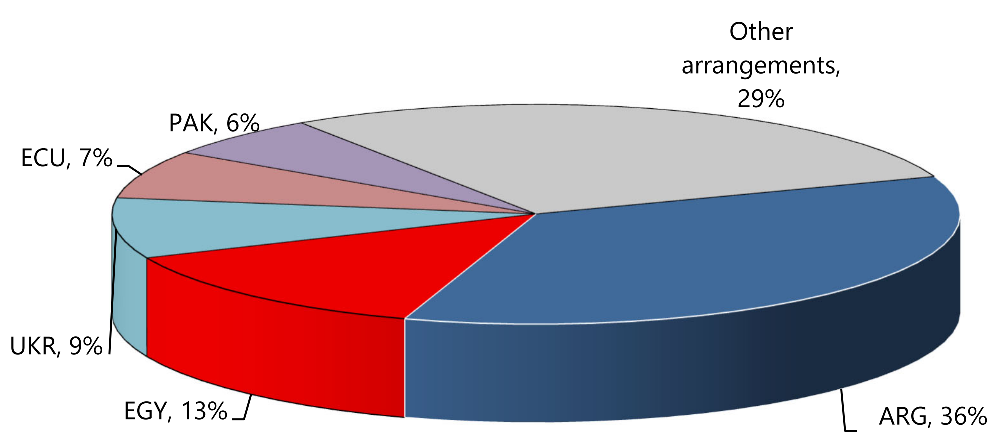
3/ For arrangements of which total external debt (or debt service) ratio is not available, public external debt ratio is shown instead.

Figure 4. Exceptional Access Levels and Credit Concentration

A. Total Access of Recent Exceptional Access Arrangements 1/
(in billions of SDRs)



B. Credit Concentration of Fund GRA Exposure 2/
(as a percentage of total credit outstanding)

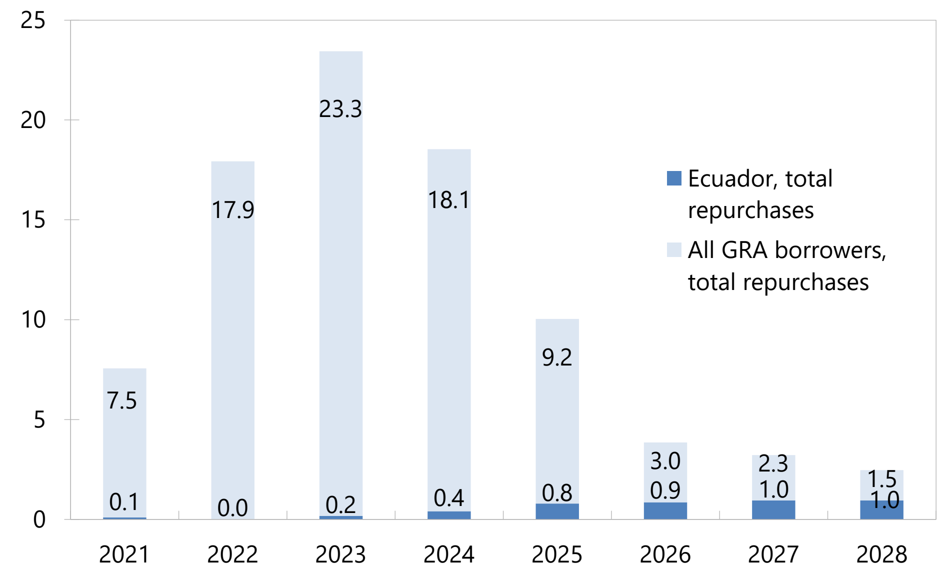


Source: IMF Finance Department.

1/ Does not include FCL arrangements as well as arrangements with relatively low access in SDRs. Asterisks indicate countries that were PRGT-eligible at the time of approval.
2/ Total credit outstanding refers to credit outstanding as of July 31st, 2020 plus Ecuador's proposed access under the EFF.

Figure 5. Ecuador: Share of Total Scheduled Repurchases to the GRA

(in billions of SDRs)



Source: IMF Finance Department.

Statement by Afonso Bevilaqua, Executive Director for Ecuador, Pedro Fachada, Alternate Executive Director, and Francisco Rivadeneira, Advisor to Executive Director
September 30, 2020

On behalf of our Ecuadorian authorities, we would like to express our sincere gratitude to the Managing Director for her support to Ecuador's economic policies and structural reforms agenda. We also thank the mission team for the balanced and comprehensive reports and welcome Ms. Oner to her fist formal Board meeting in her new responsibility as IMF mission chief for Ecuador.

Ecuador's economic environment remains extremely challenging as the country continues to face much stronger-than-anticipated headwinds. Nevertheless, the Ecuadorian authorities underscore their commitment to sound macroeconomic and financial policies. They thank Executive Directors for understanding the exceptional circumstances confronting Ecuador and for supporting the 27-month Extended Fund Facility (EFF) with exceptional financing equivalent to 661 percent of quota. They take the opportunity to, once again, express their gratitude to Executive Directors for the emergency support approved on May 1, 2020 to help address the COVID-19 health crisis, which continues to have enormous social and economic consequences for the entire country.

Recent Economic Developments

The COVID-19 pandemic has had devastating effects on Ecuador, worsening an already difficult economic situation. Containment measures to prevent the spread of the virus combined with other exogenous shocks—the collapse in oil prices, the fall in remittances and in external demand for Ecuadorian goods and services, the temporary damage to the country's main oil pipelines, and global risk aversion—creating what can be described as a real economic tsunami.

Despite early efforts to contain the outbreak, including the closure of non-essential activities and a nationwide lockdown, the virus has continued to spread in Ecuador and to affect the day-to-day life of millions. The country has surpassed the mark of 130,000 cases to date, with the epicenter of the pandemic moving in recent months from Guayaquil on the coast to the capital Quito. More than 11,000 have died at the national level while about 100,000 have recovered from the virus so far.

The authorities have acted decisively to contain the impact of the COVID-19 pandemic and other shocks on the economy. Nevertheless, the effects on the real sector have been massive, with staff projecting a 11 percent contraction in real GDP this year. In parallel, the unemployment rate has increased by nearly 10 percentage points in the first half of 2020 and is projected to increase further in the remaining of the year. Similarly, the fiscal outlook has been substantially impacted, with the public sector facing on the one hand lower tax revenues and lower oil receipts, and on the other hand higher health and social spending. The external accounts have also deteriorated, in part due to the rigidities of the dollarization regime, which the authorities intend to preserve at any cost.

Protecting the most vulnerable segments of the population including those falling into poverty has remained a key priority for the authorities since the outset of the COVID-19 crisis. Estimates by UNICEF mentioned by staff in the report point to an increase in both poverty and extreme poverty of some 10 percentage points this year, which, if confirmed, would erase much of the social progress enjoyed by the Ecuadorian people in recent years. Some of the measures taken by the authorities in recent months have comprised expanding targeted cash transfers, direct food distribution programs, and a reduction of the time required for eligibility for unemployment benefits. The new EFF contemplates plans to strengthen further the social safety net, including by more than doubling the coverage of cash transfer programs in 2021 with the assistance of the World Bank.

Preserving Macroeconomic Stability

Despite the challenging circumstances, the Ecuadorian authorities remain deeply committed to macroeconomic and institutional stability, with a special focus on restoring fiscal sustainability, strengthening the pillars of the dollarization and improving competitiveness. While concentrating on addressing the short-term impact of the health crisis, the authorities have also worked preparing the basis for a strong and inclusive post-COVID recovery.

The authorities continue to advance crucial fiscal reforms. The approval by the National Assembly of the Organic Code of Planning and Public Finances (COPLAFIP)—a key reform under the cancelled 2019 EFF—was a milestone, establishing a clear fiscal anchor over the long-term and strengthening public financial management. The COPLAFIP also addresses some of the shortcomings that led to fiscal misreporting—a problem inherited from previous administrations that the current authorities have tackled with resolve and transparency—establishing strengthened accounting and reporting practices for the different levels of the public sector, thus ensuring that fiscal statistics are timely, credible and follow international best practices.

Several other measures have been taken to strengthen fiscal compilation and reporting, including the institutional restructuring of the Ministry of Economy and Finance and enhancements in data exchange and communication channels between different areas of the public sector (Ministry of Economy and Finance, Central Bank, social security entities and local governments). Many of these improvements were recommended by and implemented with IMF technical assistance. More generally, these encouraging developments have not led to complacency and the authorities plan to leverage on the new EFF arrangement to support further capacity building in key areas to strengthen institutions and ensure policy continuity.

Significant progress has also been achieved this year regarding inefficient fuel subsidies, with the introduction of a fuel pricing band mechanism. This reform will generate significant savings over the long run and create space to accommodate the increase in social spending targeted to those affected by the rise in fuel prices and really in need of support.

Apart from savings from fuel subsidy reform, the authorities continued to reprioritize spending to contain the fiscal deficit in 2020, including by reviewing capital expenditure and reducing the wage bill through a combination of lower working hours and employment in the public sector, particularly with the closure of several public entities and enterprises.

Additionally, a historical landmark for Ecuador has been the agreement with bondholders, ensuring favorable conditions with an approval rate of 98 percent. The parameters of the agreement followed the last IMF debt sustainability analysis and are consistent with the long-term public debt targets embedded in the COPLAFIP. The operation entails significant interest savings during the 5-year grace period and extends the average maturity of Ecuador's external bonds by 10 years, with a substantial reduction in coupons.

Once the COVID-19 crisis is over, the authorities intend to initiate a strong fiscal consolidation program. The planned adjustment amounts to 5.5 percent of GDP for the overall nonfinancial public sector over a five-year period, with measures roughly distributed on the revenue and expenditure sides. In this regard, we take note of staff's empirical work demonstrating that this fiscal adjustment path is realistic and consistent with past Ecuadorian experience (Annex III).

The authorities have been advancing their transparency, good governance and anti-corruption agendas, including with implementation of prior actions for the current EFF. Important measures have been taken to increase transparency in public procurement, strengthen the anti-corruption framework, enhance transparency in public debt and budget spending, and improve the anti-money laundering regime. They will continue to prioritize actions in the area, such as enhancing assets declaration of politically exposed persons, criminalizing acts of corruption and implementing the Extractive Industries Transparency Initiative (EITI) to ensure efficiency and transparency in the management of Ecuador's natural resources.

The authorities remain committed to promote the Organic Monetary and Financial Code (COMYF) and strengthen the autonomy of the Central Bank of Ecuador (BCE). Improvements in the auditing function of the BCE have already been implemented as part of the prior actions to the EFF. Work also continues on the structural reforms agenda aimed at transforming the Ecuadorian economy and promoting competitiveness and private sector led-growth, including modernizing the business environment, restructuring the oil sector and reforming the Public-Private Partnerships (PPP) framework.

Program Issues

Program financing of $6.5 billion is equivalent to the estimated financing gap for 2020-2022. The authorities are grateful to management and staff for agreeing on a frontloaded access, which will allow the quick clearance of arrears and provide a welcome expansionary stimulus to the economy. The authorities successfully engaged with bilateral creditors to obtain financial assurances. In the case of China, Ecuador's main bilateral creditor, it has been possible to secure financing support for 2020 and 2021 and reprofile substantial part of the debt.

The EFF program brings strong political assurances. President Moreno has taken a personal interest in the IMF program and is determined to ensure its successful implementation during his term, as highlighted in his letter to the Managing Director attached to the staff report. The President and leaders of most of the political forces represented at the National Assembly have publicly stated their support to the fundamental principles and reforms agreed with the IMF. Additionally, staff has been able to maintain a constructive high-level dialogue with some of the main candidates that are running in the 2021 presidential elections. In sum, this is clearly a program with high degree of ownership and reassuring engagement of not only the current administration, but also of a broad spectrum of political forces.

Final Remarks

This EFF program with exceptional access is crucial for Ecuador to be able to overcome the harsh humanitarian and economic crisis that the country is facing and avoid a scenario of disruption that could lead to the collapse of the monetary regime and risks to democratic representation and social stability. The authorities are confident that the measures already taken and the additional actions agreed under the EFF will help Ecuador's economy emerge stronger and more resilient in the post-COVID environment.