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ECUADOR WEEKLY REPORT®

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Outside Help

Media reports this week obliged senior officials at the Ecuadorian Social Security Institute (IESS) to acknowledge that they have been seeking overseas debt. Although the amount borrowed is relatively small, the move has sparked criticism for several reasons, not least the fact that IESS has embarked upon overseas borrowing after the administration of president Rafael Correa eliminated the 40% annual subsidy governments had contributed to the system for decades. According to IESS officials, the institute continues to enjoy good financial health. The banks "practically invited the institution so it could acquire the loan directly, given IESS's financial solidity," IESS director general Geovanna León said in a television interview.

According to what the officials have told media, the near-$80 million loans at 6% interest rates follow up on similar deals contracted in March. Their statements however contradict with the two $78.3m, eight-year loans registered in the finance ministry's July foreign debt report, contracted from Deutsche Bank Spain. Proceeds are to go to accelerate new hospital equipment for hospitals in Guayaquil, Machala, and Quito. IESS president Richard Espinosa told Quito daily El Comercio that "IESS is in pretty good shape" but that if it had not obtained the fresh cash at this time "what would have happened is that the infrastructure that was planned for 2021 would not have been built." This implies that, whatever the spin, liquidity is perhaps not as good as the government insists.

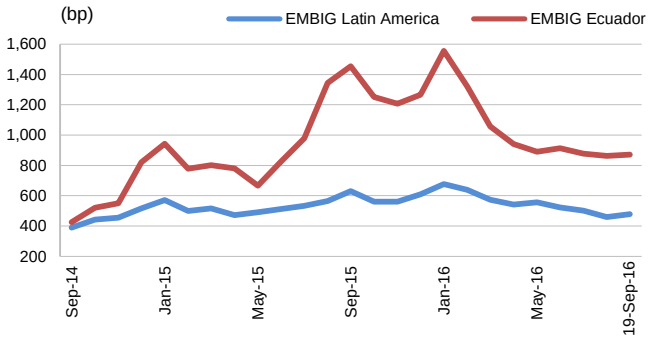
KEY INDICATORS

Ecuador's Global Bond Prices

Bond	Last Price								
	23/09/2016	Aug-16	Jul-16	Jun-16	May-16	Apr-16	Mar-16	Feb-16	Jan-16
Global 2020	103.28	102.30	100.49	99.38	100.28	95.21	90.54	79.08	74.92
Global 2022	104.17	102.89	100.03	N/A	N/A	N/A	N/A	N/A	N/A
Global 2024	90.41	88.05	87.49	87.64	89.44	88.04	82.88	72.81	69.63

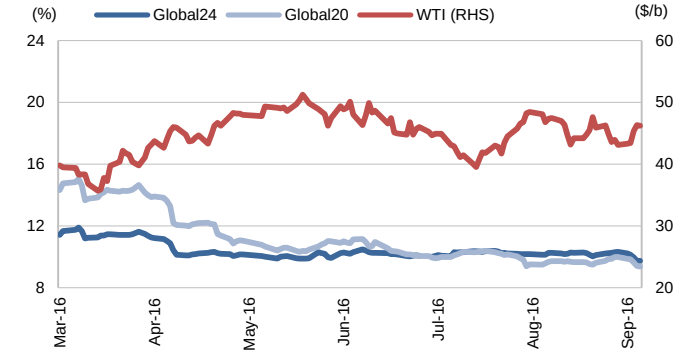
Source: Bloomberg and Analytica

EMBIG Spread



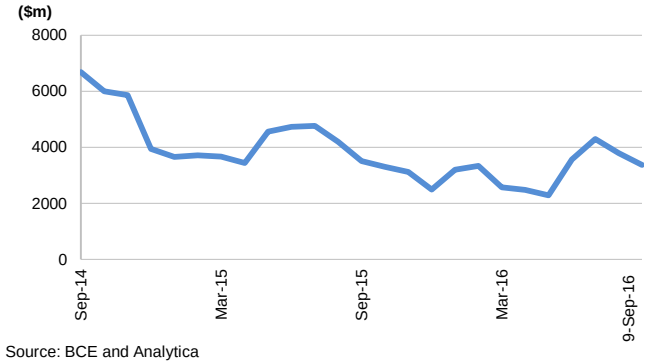
Source: JP Morgan and Analytica

Bond Yields vs. WTI in 2016



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

For former IESS officials, some of whom previously worked for the institute during the Correa years, the loans prove its financial muscle has sorely weakened. In its close to 90 years of existence, they mark IESS's first-ever steps as a debtor, rather than a creditor. Under Correa, IESS in 2010 lent state-owned oil company Petroecuador $165m to develop the Pañacocha oil field, more than half the $290m total investment, for just 5% and repayment through next year (the deal was agreed with Ramiro González, then president of IESS, now a controversial member of the Unidad (Unity) opposition coalition). If Ecuador had a liquid market for government bonds, IESS could have simply sold some of the numerous bonds it holds rather than acquiring debt at a sky-high interest rate.

The situation has raised other questions, several mentioned by Martín Pallares in the opinion portal 4Pelagatos: When Espinosa said that he was contracting offshore loans because the law didn't bar him from doing so, he was in fact breaking it, given that a civil servant may only do that which the law expressly allows him to do. According to Pallares, the loan shows government desperation to obtain funds and be able to continue cutting ribbons ahead of the elections of next February.

Uniform Justice

Last May, thousands of soldiers got an e-mail from president Correa, who disregarded the chain of command to address them directly regarding his plans for military pension reform. The letter, which included some mistakes in grammar and punctuation, sought to rally soldiers to the cause by referring to a constitutional reform last year that introduced wording "guaranteeing" military pensions. He also denied that ISSFA forms part of the military, saying that the same constitution links it to the state-run social security system (with that, he's only a small step from declaring his control over private pensions too). Bizarrely, considering that his administration created an IESS investment and mortgage bank, he suggested that ISFFA's assets, which he put at $1.4b, had not been generated by ISSFA but through state contributions; "ISSFA hardly generates any income – nor does it have any reason to," he said. He also questioned them by putting the word "assets" in quotation marks. In closing, he told the men and women that he would continue to protect their rights, but told them to ask themselves "whenever they try to invoke a false corps spirit, how many of your brothers, fathers, spouses neighbors (sic) or acquaintances have social security?" and suggested that any soldiers who didn't support him politically were not "true soldiers of the Fatherland."

He got a reply from navy captain Edwin Ortega, who, while not insulting, was strongly critical and angry, providing a long list of grievances and telling the president that his decade in office "are summarized in a flagrant attack on our military principles and values," and reminding Correa of when he had called general Paco Moncayo a "troglodyte." The letter got him a formal complaint from the president, who said he was being dishonored as commander in chief and that Ortega failed to observe the obligation of soldiers to refrain from politics.

The military tribunal that reviewed Ortega however dismissed the charges. Correa angrily replied that his constitutional rights as commander in chief had been violated. Vanessa Wolf, a first-instance judge in Guayaquil found in favor of the president. Constitutional lawyers say that this hammers Ecuador's constitutional system, introduced with much fanfare in 2008 by Correa himself, because Wolf found that Correa indeed is commander in chief, not the constitutional court that the charter puts in charge of such questions. Ortega's defense meanwhile says that she violated the rule under which no person may face the same charges twice (nobody questions the authority of the first military tribunal). The second tribunal did meet this week; it failed to come to a decision as Ortega didn't attend (a

common occurrence for initial hearings in the Ecuadorian legal system).

The scale of the scandal has likely ended Ortega's military career, as he himself has begun to acknowledge on social networks. Another half dozen soldiers however also face similar charges, and the issue of how Ortega's pension will be handled will weigh on his exit from the navy as Correa has taken this issue personally. As we have mentioned previously, some analysts say that the president is provoking the military to move towards a coup to permit him to present himself as a victim amid the troubling economic situation. Retired general and former defense minister Oswaldo Jarrín however has said that the military won't swallow the bait. Bruised as it may be after a decade withstanding political attempts to undermine its independence, at the moment, unlike the case of Venezuela, it appears the armed forces will continue at arms' length from the government when it ponders its next steps following the February 2017 national elections.

All in the Family

On September 13, a political science student published an opinion column in government newspaper El Telégrafo on "The Art (or Science) of Disqualifying Democracies (Part I)." As of this week, the article had been viewed close to 77,000 times, a high number of hits for a first-ever publication – but linked, no doubt with the controversy the author sparked: she was Anne-Dominique Correa, the president's eldest daughter.

The fact that a major newspaper would give an undergraduate student space to write not one column, but three (parts two and three came out the same week) as an opera prima might be remarkable. Correistas beamed about the prodigious young author who dared to challenge established "northern," "pseudoscientific" thought about democracy. Critics noted two issues: first, the president's daughter getting published by a government newspaper and, second, the content of the text, a tepid questioning of liberal democracy under the guise of scientific analysis. It might as well have been written by Correa, repeating as it did his method of packaging superficial claims in a way that, by coincidence or design, populists from Donald Trump to Viktor Orbán trumpet on a daily basis (although the elder and younger Correa appear to believe they are pursuing some kind of ethno-nationalist Latin American system they don't bother to define clearly beyond being limited to being south of the US border).

The younger Correa picks up the glove against The Economist, one of her father's least favorite media outlets; she repeats two-year old claims of corporate shareholdings that are false; she also invents an "Economist Intelligence Unit of Democracy," failing to discern the difference between The Economist, the EIU, and the EIU's Democracy Index, an annual product. Several critics have noted the irony of her criticism of, to put it in correct terms, a British research institute rating democracies given that the UK is a monarchy, given that she would not have been able to publish her musings if her father was not the quasi-monarchical president.

Correístas of course were enraged at the criticism. After an Italian columnist quit El Telégrafo, saying the paper had rejected a column in which he criticized the paper's decision to publish the presidential prodigy, Correa blasted him as a "little clown nobody read" (indeed, a general critique of El Telégrafo) and complained about attacks on his family. In the past, his government and the judiciary have however pursued family members of critics, from journalists like Bloomberg's then-correspondent in Quito to indigenous leader Carlos Pérez Guartambel, among others. In this case, 4Pelagatos' editorial team received death threats in social media, with personal telephone numbers and addresses made public.

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