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ECUADOR WEEKLY REPORT®

KEY INDICATORS

For the week of Oct 23 – Oct 27, 2017

More Than a Feeling

The Moreno administration this week piled billions of additional dollars onto the already sizeable body of evidence that his predecessor’s decade in office was indeed the most corrupt in Ecuador’s history – and also the least competent. Planning secretary Andrés Mideros, public works minister Paúl Granda and Jorge Wated, head of the public purchasing agency (SECOB), presented three reports that said that out of 737 roads, schools, courthouses and other infrastructure, 640 – 87% – have technical, financial, and/or legal problems. According to the officials, who didn’t necessarily play an illustrious role under the previous administration, this was only a first approximation to the scale of its failure to do this cleanly and properly. And it still leaves out mismanagement and white elephants at other public entities, including state-owned companies that Wated until recently oversaw.

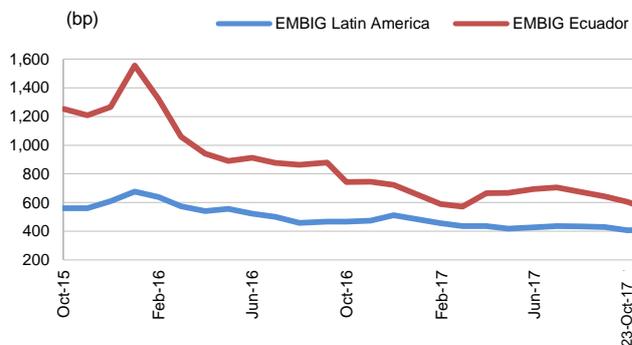
In total, under president Rafael Correa (2007-2017), the government budgeted some \$2.14b for the 640 projects in question, but costs increased to \$3.98b. The Moreno administration would need some \$956m as a whole to finish all of them. Some of the projects in question saw prices surge twelvefold or more. According to finance minister Carlos de la Torre, cited in Quito daily *El Comercio*, Ecuador lacks the money to complete them at least under the 2018 budget. The officials presented several particularly onerous examples of cost overruns. One particularly glaring case is the widening the road through the southern tip of the country, a little-traveled area to the

Ecuador's Global Bond Prices

Bond	27-Oct	Sep	Last Price (end of the month)				
			Aug	Jul	Jun	May	Apr
Global 2020	108.93	108.03	107.39	106.12	105.83	105.58	107.50
Global 2022	112.79	111.77	110.05	108.20	106.83	107.41	108.63
Global 2023	104.56	103.39	102.34	100.12	98.55	-	-
Global 2024	100.29	99.14	98.22	95.60	93.52	95.05	95.58
Global 2026	107.31	105.60	105.25	102.56	100.71	101.11	102.29
Global Jun 2027	106.45	105.04	105.01	102.60	100.30	-	-
Global Oct 2027	101.17	-	-	-	-	-	-

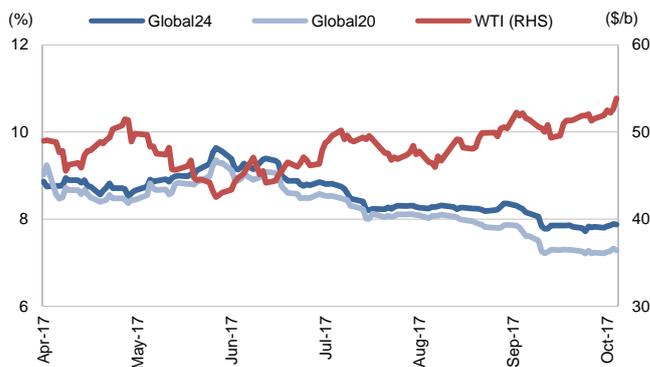
Source: Bloomberg and Analytica

EMBIG Spread



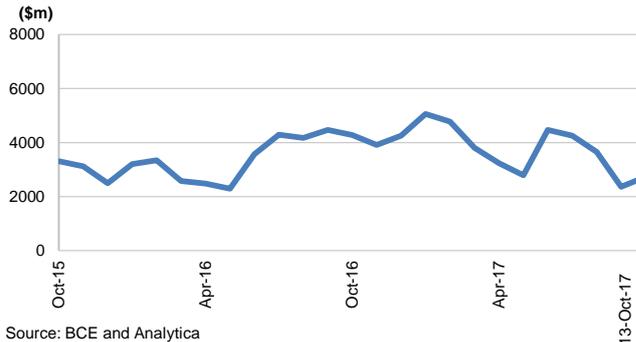
Source: JP Morgan and Analytica

Bond Yields vs. WTI in 2017



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

border with Peru. The price for the first part south of the hippie hangout Vilcabamba ballooned to \$152m from \$18.9m, and it's still missing four bridges to be finished. For the second part, to the border itself, the budget surged to \$214m from \$13m, an increase of 1546%. At that price, this segment won't be completed, according to Granda; 97% remains unfinished. Oddly, it was supposed to be finished in 2012, four years before the first part. Other abandoned projects include schools and hospitals.

Around two thirds of the projects have been nearly finished or actually completed, but suffer from errors in contracts and other legal problems that have kept them from being used and/or maintained, according to Mideros. Cost increases in some supplementary contracts top a legal limit of 70% of the initial budget, leading to work stoppage. The by far largest share of the projects (529) were contracted through SECOB, but depended on other ministries. The interior ministry, run by José Serrano, now president of congress had problems with 211 police stations; the health ministry, with 113 clinics and hospitals; and education, run by Augusto Espinosa, a correísta hardliner, with 89 schools, not counting the seven failed projects at Correa's troubled Yachay universities mentioned in the reports, as well as 24 kindergartens (in Correa-speak, called "infant centers of good living"). A staggering 417 didn't even have building permits.

The presentation leaves major questions open. Projects like these all needed to have guarantees and the projects' completion, by law, needed to be insured. In the separate case of a flawed pipeline between Guayaquil and Cuenca, which cost more than \$600m, according to Petroecuador, which is fighting the Brazilian builder, Odebrecht, the insured guarantee is just \$17m. Mideros said that the government aims to finish all of the projects. We in this case agree with finance minister Carlos de la Torre that projects should be finished only if a careful review proves their usefulness outweighs the sunk

cost. In any case, Mideros acknowledged that legal changes will be required to be able to sign new contracts to finish them – changes that could easily be a problem for Moreno to obtain. Regardless of the outcome, the scandal provides more evidence that, in Ecuador, the best way to steal is by building public works.

Goodbye Sweet 16

President Moreno this week reformed decrees that had been among the most onerous limitations on basic freedoms under his predecessor: Decrees 16 and 739, which had de-facto eliminated the constitutionally protected right to freedom of association. "The idea is to dismantle all the bureaucratic arguments that impede social organizations from linking up," Moreno somewhat confusingly argued. Critics including the Inter-American Human Rights Commission for years criticized the decrees, which led to the dissolution of an unknown number of non-governmental organizations since 2013 (the government acknowledged 44, but media defense NGO Fundamedios says the official numbers don't add up). Prominent shuttered organizations included environmental NGO Pachamama and the hard-left teachers' union UNE, while the German Konrad-Adenauer-Stiftung and the US' USAID reluctantly left the country.

Pachamama's end, in particular, deserves mention. Correa closed it because of its opposition to oil development in the Amazon Southeast; the government falsely alleged that it had participated in violent protests in Quito against a tender of oilfields in the biologically diverse and sensitive area (the protests were almost completely non-violent and the police was suspiciously incompetent in protecting a Belarusian national who was briefly threatened). Yet it had been Pachamama, through its ties with US environmental lawyers, that had developed the concept of the "rights of nature" and through its

lobbying managed to have these enshrined in the 2008 constitution. Correa, who is scheduled to speak at the University of Geneva in Switzerland in the coming days, as he did when invited by the Vatican to contribute to discussions the *Laudato Si* environmental encyclical, will likely once again take credit for making the constitution supposedly environmentalist.

As has happened with numerous policy steps in his first months in office, while breaking with his predecessor in his personal handling of government, he has so far done little to do away with the problematic legal rules left behind by Correa. In the case of laws, this can pose challenges because, as in the case of the new legislation necessary to pass the handling of the mobile payments system to the private financial sector, this requires congressional action. But with the ruling Alianza País (sic) movement under extreme tension between correístas and morenistas, this would risk making the split open and shaking up the congress because AP would lose control of the body, in which it has an absolute but narrow majority (we believe the split is imminent anyway). In the case of associations and organizations, however, Moreno faced a much easier task because all he needed to do was roll back the situation as it was before Correa issued the decrees.

Instead, he chose to create a full new body of governance to regulate social organizations. Government officials insist this gives social organizations legal security and a roadmap to being established, and help foreign NGOs to increase operations (or return). According to *El Comercio*, foreign aid channeled through NGOs plunged from a peak of \$396m in 2011 to a paltry \$13.6m last year. The new regulations scrap a number of regulations aimed at controlling the foreign NGOs, rolling back some of Correa's putinism. Overall, social organizations remain under regulatory oversight of the respective ministry, as well as tax and customs bodies. The ministries, of course, are the most

potentially troubling; the amount of red tape they issue tends to be daunting and arbitrary. The role of government officials and civil servants in overseeing civil society remains problematic under the new rules, according to NGOs including Fundamedios. The administration will still have the capacity to dissolve a body for "deviating from the aims and objectives for which it was constituted;" bizarrely, a fall in membership to below a legal minimum; dedicating itself to "party politics;" and for committing crimes, but also for failing to comply with the new regulations. The new rules for civil organizations leave one of Ecuador's main regulatory problems intact: the right of administrators to impose draconian punishment while being prosecutor and judge.

Moreno's unnecessary decision to leave these elements there add to the general disappointment expressed by business leaders after he recently unveiled an economic plan that fell short on both helping the economy and creating a comprehensive road map out of the country's economic woes. By hesitating to act more firmly and put the rules fully in line with what both domestic and international human rights organizations demand only serves to prove critics right that he has yet to do more than to continue a kinder, gentler correísmo. It also still falls short of making sure the constitution is indeed the top law of the land because the decree once again erodes freedom of association. Freedom of association doesn't exist when it's subject to the whims of an individual leader's decrees.

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