



Ramiro Crespo
 Chairman of the Editorial Board
 WEEKLYREPORT@ANALYTICAINVESTMENTS.COM

ECUADOR WEEKLY REPORT®

KEY INDICATORS

For the week of Nov 13 – Nov 17, 2017

Raise Drawbridge

Over the loud objections of commerce associations, a new duty regime went into effect in Ecuador this week aimed at netting the finance ministry \$500m a year. After the government of president Lenin Moreno in June as promised completed the phase-out of the "emergency safeguards" introduced in March 2014 to stave off balance of payments problems, it sought a replacement, finding it in a new weight-based tariff scheme. For Mauro Andino, the head of the customs service (SENAE), it's just 10 cents that help to fight allegedly massive smuggling. For the economy, it's another monetary transfer to the public sector, with increasing red tape adding to the misery. As with the 5% capital export tax and the idea of increasing duties on some 375 goods to the maximum permitted by the World Trade Organization, the government says these measures keep liquidity inside the country by discouraging imports and thus protect Ecuador's use of the dollar.

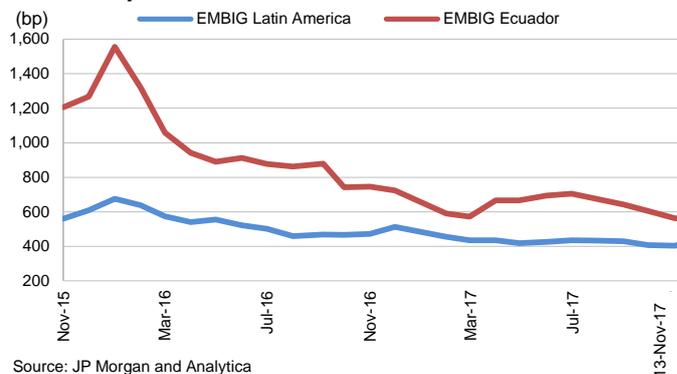
Under the new system, dubbed the "customs control rate," importers have to pay a duty according to the formula: 10 cents x declared net weight per item (gr) / "control unit" (gr), with the control unit defined in 98 chapters of the customs service's classification system. Chambers of commerce have published changes introduced by SENAE within the past few hours in its Ecuapass online system for goods as different as live chickens, toys, refrigerators, and industrial filters, proving completely discretionary changes to the body of rules and a lack of clarity for

Ecuador's Global Bond Prices

Bond	Last Price (end of the month)					
	17-Nov	Oct	Sep	Aug	Jul	Jun
Global 2020	108.04	109.10	108.03	107.39	106.12	105.83
Global 2022	113.34	113.13	111.77	110.05	108.20	106.83
Global 2023	105.93	104.90	103.39	102.34	100.12	98.55
Global 2024	100.83	100.89	99.14	98.22	95.60	93.52
Global 2026	108.63	108.04	105.60	105.25	102.56	100.71
Global Jun 2027	108.31	107.57	105.04	105.01	102.60	100.30
Global Oct 2027	103.31	102.40	-	-	-	-

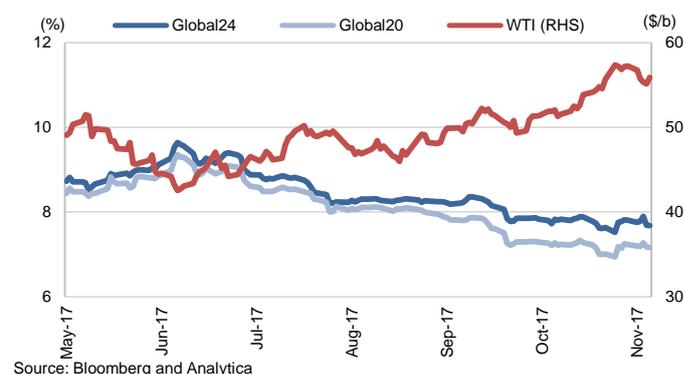
Source: Bloomberg and Analytica

EMBIG Spread



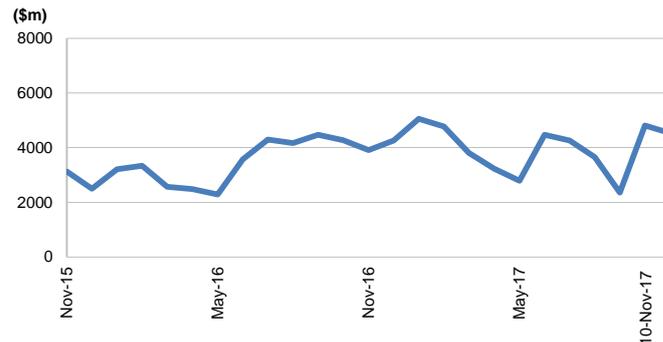
Source: JP Morgan and Analytica

Bond Yields vs. WTI in 2017



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

buyers. In all cases, the change increased the control charge significantly. As we reported last week, the price of an imported syringe has gone up by half, affecting the healthcare system supposedly so dear to the administration. Car assembly kits imported by vehicle manufacturers face prices rising by more than 16%. Importers have to pay the new fee on top of duties; thus, an air conditioner will go up another 20% on top of the 15% duty; the price of a Christmas tree will rise 71%, and that of a ping-pong table by 135%. Should a good weigh more than expected by the customs service, the duties will rise correspondingly. It remains unknown how SENAE calculates expected weights.

For the administration, the new system will fight widespread cheating on customs forms. According to Andino, importers declare some 70% of goods at prices below 5 cents, well below retail price, which it sees as an indication of fraud. Cynically, Andino says that the scheme is a service fee for SENAE's fight against smuggling. According to the automotive association AEAE, the price of cars will go up by up to \$4,700 – whoever is buying a car is thus theoretically paying the customs service thousands of dollars for the service of combatting smuggling brought on by the government's high-duty regime. In a joint statement, the chambers of commerce of Cuenca, Guayaquil, and Quito said that the plan "evidently seeks to collect funds, disproportionately and without a direct or justified relationship to the cost of the service" allegedly being supplied. They also warned that it risks running afoul of the trade deal with the European Union and runs counter to the trade agenda that foreign trade minister Pablo Campana promoted during a recent multi-country tour. Exporters, too, will lose competitiveness thanks to the prices they will have to pay for imports necessary to produce. In the short term, it appears the system will go ahead however: A judge defeated an injunction filed by Guayaquil's chamber of commerce, telling it to seek justice through other, slower channels.

Morally Bankrupt

For all the disputes within Alianza Pais (sic), the political vehicle that has nominally governed for more than a decade now, it can still hold together to defend one of its own, even if the individual in question is presumed politically responsible for covering up some of the most vile crimes imaginable: close to 900 cases of pederasty at Ecuador's public schools. This week, the so-called Legislative Administrative Commission (CAL), with 5 AP members out of 7 though AP has just 74 of the 137 seats in congress, blocked the impeachment of Augusto Espinosa (AP), the education minister during whose three years in office the recorded cases of sexual abuse went ahead (we will spare readers the horrid details of the crimes committed against young children). To protect Espinosa, currently a legislator of the minority AP faction that pledges allegiance to president Moreno's predecessor, Rafael Correa, the CAL's majority didn't even shy away from using documents manipulated by Silvia Salgado, a friendly socialist legislator.

The Correa administration had already obtained a very poor reputation for its handling of pederasty by using the control over the judiciary in two high-profile cases, a physical education teacher at French private school La Condamine (he was a colleague of Anne Malherbe, the president's wife, who vouched for him), and Jorge Glas Viejó, the vice president's father. Also, the AP majority in the constitutional assembly already in 2008 amnestied the convicted pederast Floresmilto Villalta. Beyond this, however, hundreds of cases began to be reported over the middle of the year all over the country. The scandal began to emerge late May with 41 cases reported at Quito school Academia Aeronáutica Mayor Pedro Traversari (Aampetra) dating back to 2012, which in August led to the installation of an ad-hoc congressional committee of the same name, led by Salgado, the socialist legislator mentioned above. The story that emerged was one of widespread abuse accompanied by a disturbing track record of attempting cover-ups,

blaming children and parents, and other negligence seen at private schools like the French school Lycée La Condamine in Quito as well as the public Colegio Réplica Aguirre Abad in Guayaquil. Correísmo, above all, had an interest in keeping a lid on the reports because they cast a huge doubt on the success of Correa's alleged revolution in schooling. The 1,680-pupil Réplica Aguirre Abad played a special role as a model since Correa himself kicked off the Pacific Coast school year in the newly built facility in April 2013. To underscore the break with the past, the Correa administration insisted on replacing the very word "school" with "educational unit" throughout the country (though one might say that universities, too, are "educational units").

According to Gustavo Jalkh, the head of a judicial review board called the Consejo de la Judicatura, in the last two years, judges issued 1,074 sentences following 4,864 complaints for sex crimes against children and juveniles. While the courts appear to have indeed been active, the Aampetra committee found that perhaps 9% of cases had actually found their way there. The general picture that emerged was one of widespread negligence and even collusion to keep teachers who had committed these atrocities on the payroll in places as far apart as Guayaquil and the small Andean town of Chunchi. Thousands of teachers and principals work in the system despite lacking minimum qualifications. Criticism centered on Espinosa as the man who bore political responsibility for the abuse. Much like vice president Jorge Glas, who insists there is no proof of his corruption despite mountains of evidence the prosecution has compiled against him (sufficient to force him to stand trial in the coming weeks), Espinosa refused to acknowledge any responsibility, despite admitting that the ministry new of about 100 cases a year.

Opposition legislator Jeannine Cruz (CREO) sought to have Espinosa impeached for his administrative failings, which was possible until a year after he left office (Espinosa resigned in November

2016 to run for congress), collecting 49 signatures, enough to start the proceedings. But, as mentioned above, the AP majority in the CAL voted against his impeachment, citing insufficient evidence. Salgado, who acted similarly in previous years, presented the CAL with a final report the other members of the Aampetra committee found unrecognizable, blaming the mixup on underlings. The CAL voted on what she presented, duly finding there was no evidence to imply that Espinosa should be impeached. Hours later, the statute of limitation ran out. Like the congress, the CAL is presided by José Serrano, a former human rights lawyer controversial for his repressive handling of indigenous protests during his tenure as Correa's interior minister. AP may be split between correístas and morenistas, but both sides include individuals with dubious track records, for whom parliamentary immunity is important. Serrano is using his influence to make sure these stay protected. Moreno may feel more comfortable the larger the group of AP legislators and former Correa aides that publicly supports him, but actions like the protection of Espinosa are costing him popularity among voters.

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