

ECUADOR WEEKLY REPORT®

KEY INDICATORS

For the week of Dic 4 – Dic 8, 2017

Toxic Risks

Ecuador and oil company ConocoPhillips, a minority shareholder in an Amazon operation confiscated in 2009, ended their legal dispute this week, with the country agreeing to pay \$337m after it lost the arbitration suit before the International Center for Settlement of Investment Disputes. The payment is net of the \$42m ICSID had agreed with Ecuador that the company should pay for environmental cleanups at the oil blocks 7 and 21. ConocoPhillips's Burlington unit and majority shareholder Perenco had ceased operations in protest for the administration of president Rafael Correa's confiscation of their oil.

The dispute started over taxes after Ecuador imposed a 55% windfall tax on company oil profits after oil prices recovered from their late-1990s slump. Correa jerked it up to 99% in late 2007 to force the companies to negotiate new contracts. It took him four years to actually design a new contract scheme, leading to significant loss of output and thus of money for the government itself amid the industry's greatest-ever boom. The consortium of Perenco and Burlington took a hard line and sued before ICSID and refused to pay the tax. In response, Correa confiscated the oil, after which the companies said they would shut down production. The administration followed up by seizing their assets, arguing they were acting to protect the environment from damage.

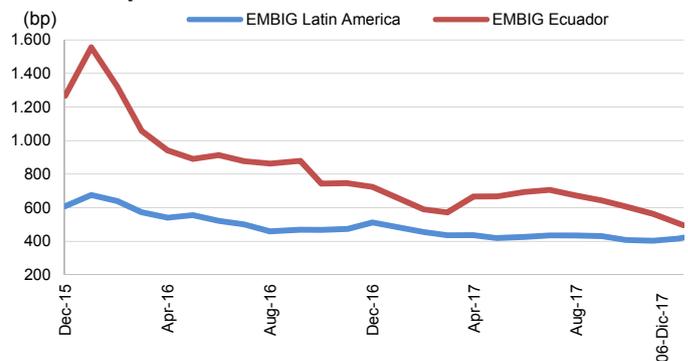
After losing the case, Ecuador paid \$75m on December 1, with the remainder due next April. ConocoPhillips called the solution mutually acceptable and said that the government "worked constructively"

Ecuador's Global Bond Prices

Bond	Last Price (end of the month)					
	8-Dec	30-Nov	Oct	Sep	Aug	Jul
Global 2020	110.11	109.64	109.10	108.03	107.39	106.12
Global 2022	116.73	115.86	113.13	111.77	110.05	108.20
Global 2023	109.53	108.46	104.90	103.39	102.34	100.12
Global 2024	105.30	104.42	100.89	99.14	98.22	95.60
Global 2026	113.17	112.45	108.04	105.60	105.25	102.56
Global Jun 2027	112.79	111.66	107.57	105.04	105.01	102.60
Global Oct 2027	107.54	106.82	102.40	-	-	-

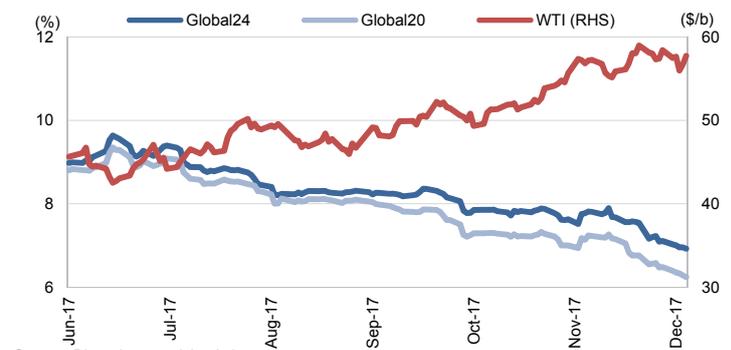
Source: Bloomberg and Analytica

EMBIG Spread



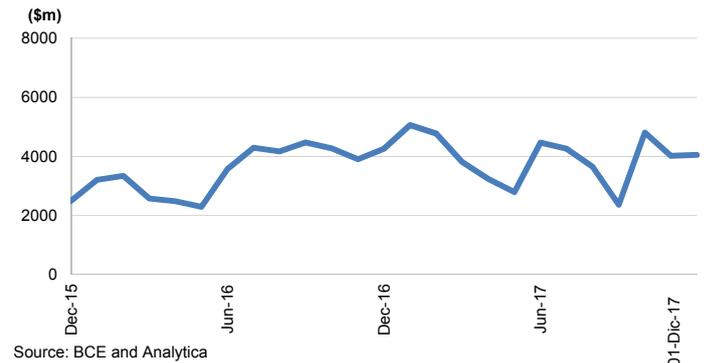
Source: JP Morgan and Analytica

Bond Yields vs. WTI in 2017



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

to close the issue. Asked about the government's willingness to work with oil companies to step back from legal disputes, finance minister Carlos de la Torre however only called it a payments agreement following the legal dispute, leaving the door open for the conflict to continue with Perenco. The decision now however sets the stage for Perenco to collect a somewhat larger amount than that won by ConocoPhillips now.

The cases are a reminder of the medium-term financial risks inherited from the flawed oil policies of Correa. Aside from Perenco, the settlement of Petrobras, which left Ecuador under the fee-based contract scheme imposed by Correa in 2010, is the largest of these. The two sides failed to reach agreement over the value of the assets handed over and now run by Petroamazonas, a state company. Approaching the end of Correa's term, Ecuador had to pay close to \$1b to Occidental early in 2016, a decade after the confiscation of its assets which Correa demanded as a political outsider, and from which Petroamazonas was formed. Recently, the current administration managed to settle a slightly smaller debt with oil services company Schlumberger. Painful as they are for taxpayers, these cases will be instrumental, as well as the reinstatement of production-sharing contracts, to fix relationships with the oil industry.

Belt and Sleeves

Rafael Correa announced that he would return to Ecuador in triumph to rip control of the country back from the "traitors," including president Lenin Moreno. He failed. During his 10 days here, he instead experienced how people have moved on, leaving him politically hobbled. This only partially came to benefit his successor, who struck a crippling blow to Correa by circumventing the Constitutional Court and decreeing the referendum for February 4. During the same time, a leaked audio featuring Eduardo Mangas, Moreno's

Nicaraguan chief of staff, undermined the fragile trust that Moreno had obtained among some of the voters to win approval rates as high as 80%.

Correa's trip was an exercise in futility. He flew in via a private plane to Guayaquil, where a mob of populist supporters led by Abdalá Bucaram, a former president deposed in 1997 amid corruption charges that nowadays look innocent, clashed with correístas, leading Correa to abandon the airport through the back door. Media estimated his supporters at around 700. He then embarked on a tour including Cuenca, from where his faction of Alianza País (sic), the ruling party, tweeted a grossly photoshopped picture implying a much bigger crowd. An event in Quito was similarly small. In Ibarra, protesters for the most part apparently organized by Democracia Sí, an organization that tacitly supports Moreno, so greatly outnumbered the correístas that thugs beat the path free for Correa's big black SUV.

It must have added insult to injury that Moreno pushed forward the referendum and pushed out Juan Pablo Pozo, as president of the electoral council (CNE) one of the most visible faces of correísta control over elections. The new CNE promptly waved through referendum and warned that any official who dared to try to block it now faces firing. The electoral court, meanwhile, argued that a demand a judge recuse himself delayed its decision on whether to recognize Moreno or Correa's longtime ally, Ricardo Patiño, as president of AP. Thus, Correa's planned "VII AP Congress" in Esmeraldas became a non-event, held at a hotel owned by the father of Alex Bravo, the former Petroecuador CEO found guilty of corruption after the city's chamber of congress canceled the permission someone had given to hold the conference in its facility. When he left Guayaquil a few days later, the number of well-wishers had dropped to 70. "What does it feel like, Rafael Vicente?" wrote Fernando Vega, a former priest from Cuenca who ended his support for Correa after the dubious 2007-2008 constitutional process, wondering how Correa is dealing with his loss

of influence and the public's rejection or indifference.

Moreno's victory however almost as quickly fizzled as the Mangas leaks made their way into the public debate. First, news site Focus Ecuador reported the comments, then the audio file of more than 30 minutes became public in which the chief of staff appeared to admit that Moreno lost the elections to Guillermo Lasso (CREO), who only conceded the election after weeks of protests fizzled out (sadly, it appears violent protests like in Honduras are more likely to attract international attention and action than the remarkably peaceful ones of Ecuador). Only thanks to the "fraud strategy" had Moreno inched past Lasso, Mangas said. Furthermore, in the recording, he downplayed Moreno's strategy of national reconciliation as a mere ploy to get opponents like indigenous groups and business interests into a feel-good mode, rather than conceding anything.

After first ignoring the scandal, the presidency issued a lackluster statement saying that his comments didn't reflect Moreno's thought. It did reinforce the appearance that a group of former correístas now aligned with Moreno are attempting at all costs to maintain their flawed heterodox macroeconomic policies and political control over Ecuador, as many critics have been pointing out. Mangas said the statement was taken out of context. Indeed, even though the length of the statements makes that claim somewhat ridiculous, the dynamics of the situation make it appear likely that the recording stemmed from early in the presidency and was leaked not by correístas, but by rivals jostling for proximity to Moreno. Correctly, interest groups are demanding results, not just dialogue. With a chance to veto the recent damaging economic package, Moreno has a near-term opportunity to prove the critics wrong.

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