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ECUADOR WEEKLY REPORT®

KEY INDICATORS

For the week of Jul 9 – Jul 13, 2018

Carlito's Way

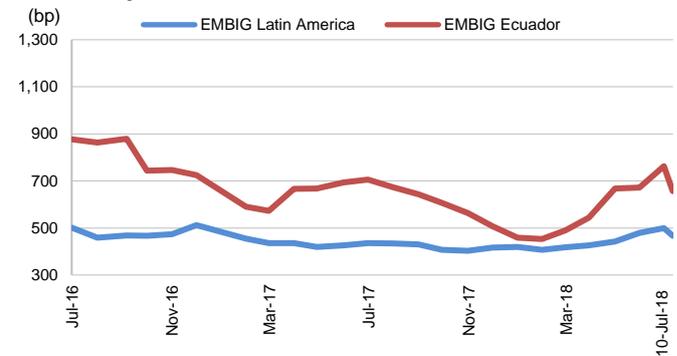
Over the next few days, the cream of Correísmo will parade before prosecutors to testify regarding the murder of air force general Jorge Gabela in 2010. More than a dozen former cabinet members, some of whom are now legislators or in the current administration, have been called to comment on their involvement in the handling of the case. As high-profile as it is, it's just one of the criminal cases snowballing around former president Rafael Correa (2007 – 2017). President Lenín Moreno in a meeting with foreign correspondents last week expressed shock and embarrassment at having served as a two-term vice president (2007 – 2013) under a regime that could be responsible for crimes as severe as murder. It's thus becoming more and more difficult not to call Correa's regime criminal, given the evidence of the central nature that bribery and other crimes held under his administration.

Gabela was an adamant opponent of the purchase of Hindustani Aviation Ltd. Dhruv helicopters, most of which crashed. Correa insisted the murder was "common crime," which his widow, Patricia Ochoa, refused to believe. A subsequent investigation was never fully made public; a part of the report appears to have been mutilated, and those called to testify may have been responsible for what would amount to a cover-up. The long list of these officials includes former interior minister and current legislator José Serrano; former justice minister Ledy Zúñiga; former defense minister Fernando Cordero; María Fernanda Espinosa, former defense minister and foreign

Bond	Last Price (end of the month) 2018						
	13-Jul	29-Jun	May	Apr	Mar	Feb	Jan
Global 2020	105.13	102.24	104.12	103.10	108.42	108.75	109.98
Global 2022	105.77	102.55	105.36	105.54	111.06	113.07	116.32
Global 2023	97.82	93.71	97.75	97.89	104.68	106.64	110.12
Global 2024	92.87	89.25	94.06	94.11	100.70	102.06	106.04
Global 2026	97.50	93.58	99.08	98.50	107.37	110.44	114.40
Global Jun 2027	97.06	93.33	98.70	98.11	107.08	110.35	113.76
Global Oct 2027	93.02	89.16	94.49	94.36	102.19	105.58	109.17
Global 2028	87.76	84.02	88.66	88.53	96.76	99.23	102.04

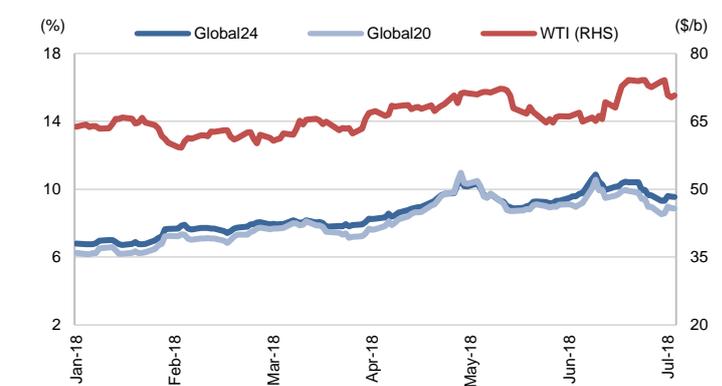
Source: Bloomberg and Analytica

EMBIG Spread



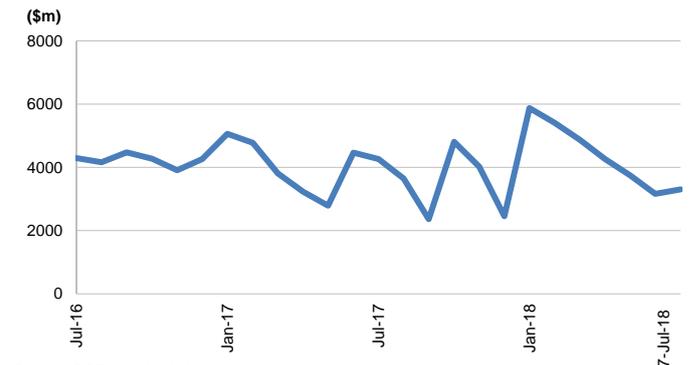
Source: JP Morgan and Analytica

Bond Yields vs. WTI 2018



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

minister and president-elect of the next United Nations General Assembly; former oil minister and prosecutor general Galo Chiriboga; former interior minister César Navas; current legal secretary Johana Pesántez; and former chief of staff and chief propagandist, Vinicio Alvarado, among others.

Alvarado's brother Fernando, meanwhile, has been called to testify regarding the kidnapping of opposition activist Fernando Balda in Bogota in 2012. Fernando Alvarado will call in from Nigeria, where he is for unknown reasons. Others potentially fingered in that case are former foreign minister and defense minister Ricardo Patiño; Patiño's brother, Raúl, a former head of the intelligence secretariat; Correa's lawyer and former presidential legal secretary Alexis Mera. Correa, who according to a policeman implicated in the case said used the alias "Carlitos" during the kidnapping, this week declined to testify from the consulate in Belgium, to where he moved to live with his Belgian wife last year, alleging a lack of guarantees, an inexplicable maneuver (and an insult to the Belgian police that protect the consular offices). Prosecutor general Paúl Pérez will wrap up this investigation next week and will likely charge Correa for playing a role in the bizarre crime.

This is only part of his legal problems. The comptroller general, Pablo Celi, has submitted further evidence of white-collar crimes in the issuance of public debt. Short term debt in the form of treasury certificates (CETES) between \$1.7b and \$2.3b was issued with disregard for the legal limit of 360 days on the maturities. It was also illegally used to pay off government debt. Celi piled this latest evidence against Correa and former finance ministry officials onto that from the earlier investigation. He also announced further analysis of 69 privately-administered investment funds with a combined worth of \$1.2b taken over by BIESS, the bank of the social security institute created under Correa.

Ecuador's legislature is meanwhile working on a law to seize embezzled funds. The president of the

National Assembly, Elizabeth Cabezas (a former aide of Jorge Glas, Correa's vice president and Moreno's running mate now serving six years for corruption), says the bill will allow the return of \$24b in money squirreled away under his administration. At nearly a quarter of annual GDP, that figure demonstrates the staggering scale of corruption under Correa. Additionally, Moreno has spoken of negligence along the troubled Colombian border related to drugs trafficking, also under Correa. The burying of investigations and altering of records by the judiciary, slandering of people by Correa and the administration in propaganda broadcasts and the numerous violations of human rights at the hands of the public force are well documented and systematic. All of this needs to be kept present when Correa, now reduced to a desperate drama queen, presents himself in interviews as a victim of political persecution, particularly by Belgian authorities considering his extradition. It should also be made clear to European public opinion how disgraceful the support for the former president by the likes of politicians like Jean-Luc Mélenchon is.

Pat on the Back

For 2018, the fiscal situation appears to be holding steady at a critical level. The finance ministry under Richard Martínez is working on improving relations with the markets and trying to end the aggressive debt spiral everyone knows is unsustainable. While selling debt was out of the question at the peak of the recent spike in bond market yields, Ecuadorean debt performed well in recent days. Some market skeptics are beginning to gain a modicum of confidence in the economic team's capacity to deliver on spending cuts. The International Monetary Fund, which spent two weeks in Ecuador for Article IV consultations ahead of July 4, publicly lauded their efforts. Even without an economic IMF assistance program, this amounts to some real financial help, no strings attached.

At the close of this edition, the details of an expected line-item veto of the fast-track “Productive Development Law,” which calls for taking the deficit down to zero before interest payments by 2021, remain unknown. Still, the IMF in its post-mission statement called the bill an important step for fiscal policy. The visit went so well that the IMF called it “impeccably organized,” with major efforts underway (not just prodded by the comptroller general) to boost transparency. The Fund noted that the banking system is in good shape and that Ecuador is not fully to blame for the economic predicament in which it finds itself. The fall in the price of oil and the exchange rate, the latter overvalued according to the statement, has led to an ongoing adjustment process (in this regard, we do assign blame to government officials, particularly president Correa, for exacerbating problems because of excessive besides corrupt spending rather than insulating the economy against external shocks). The IMF also notes the cooling of the economy in the first quarter of this year, in which it shrank 0.7% on the quarter (please see our Ecuador Monthly Report for further information). This was before the current economic team agreed to take the helm, and before the passing of the economic package, which creates important corporate income-tax breaks to hopefully accelerate investment and thereby employment and overall growth.

The big issue, of course, is debt, particularly the large fiscal deficit and the tight amortization schedule. The non-financial public-sector deficit at 4.8% of GDP last year shows a large deficit, “particularly for a dollarized economy.” The IMF notes elements that have and may continue to provide support, including “higher oil prices, temporary tax measures, cuts in capital spending, and a public sector hiring freeze,” but adds that “a more balanced and frontloaded fiscal consolidation would help boost confidence, reduce borrowing costs and reach more sustainable deficit levels more quickly.” The question is hopefully more “when” rather than “if,” with the next budget due by

the end of October. Furthermore, Ecuador needs to build up a reserve cushion, the IMF adds. That is hopefully in the cards, but only after 2021, according to the current status of the economic bill.

Still, hard work remains ahead in the shape of “prompt and decisive actions to address the vulnerabilities in the economy” as there are risks in the global economy, some of which have already materialized like the short-term fall in oil prices thanks to US president Donald Trump’s attack on Chinese imports. These include “softening the rigidity of the labor market, broadening a set of trade agreements, improving the efficiency and reliability of the energy sector,” all of which are anathema for a large part of the leftwing constituency of president Moreno’s electorate. Hopefully, the continued fight against corruption, which the IMF supports, will allow Moreno to put the blame on Correa for what will be a tough political fight he has so far tried to avoid at all costs. Some analysts want Ecuador to approach the IMF for financial support as soon as possible, which currently appears only a measure of last support. In the meantime, the verbal support of the IMF amounts to a bit more money in the bank.

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