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ECUADOR WEEKLY REPORT[®]

KEY INDICATORS

For the week of Feb 6 – Feb 10, 2017

Broken Glas

Unsurprisingly given president Rafael Correa’s dominance in the public sphere over the past decade, he has overshadowed the presidential campaign even though he’s not on the ticket. His political movement, Alianza Pais (sic), which Correa leads, nominated former vice president Lenín Moreno as his successor while keeping current vice president Jorge Glas on board as Moreno’s running mate. During this campaign, Correa’s protagonism has taken on shades of the bizarre amid his desperation to protect himself and his legacy. Despite the best efforts of the government’s top echelon to bury scandals, accusations of corruption have overshadowed the race thanks largely to a social network fracas with an estranged former partner that has held many in thrall.

Last week, a number of videos emerged on social networks of Carlos Pareja Yanuzzelli, one of Correa’s closest aides regarding the oil industry. More than a decade ago, both heavily pressured then president Alfredo Palacio to confiscate the assets of Occidental Petroleum (this cost the Correa administration \$1bn a year ago after losing the company’s suit). Pareja also held positions including oil minister, head of refining at Petroecuador, and the company’s presidency before resigning in May 2016 as news of corruption at the company finally broke thanks to the revelations of the Panama Papers.

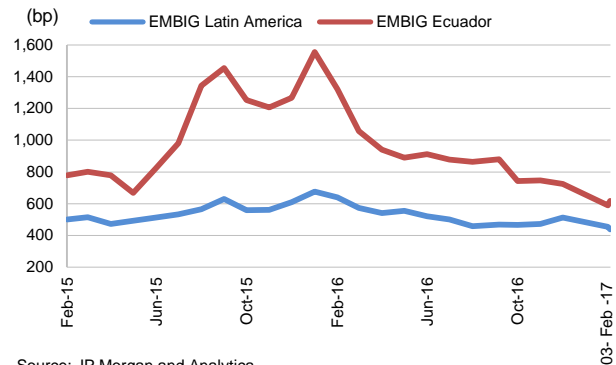
Correa blamed the media for the three videos because they had showed interviews of Pareja with reporters from newspaper *Expreso* and television broadcasters *Ecuavisa* and *Teleamazonas*, during

Ecuador’s Global Bond Prices

| Bond | 10/02/2017 | Jan | Last Price (end of the month) | | | | Aug |
|-------------|------------|--------|-------------------------------|--------|--------|--------|--------|
| | | | Dec | Nov | Oct | Sep | |
| Global 2020 | 108.58 | 109.52 | 107.89 | 105.54 | 106.13 | 102.51 | 102.30 |
| Global 2022 | 109.08 | 112.25 | 108.81 | 104.94 | 106.11 | 102.47 | 102.89 |
| Global 2024 | 97.30 | 99.07 | 95.92 | 92.15 | 94.55 | 90.25 | 88.05 |
| Global 2026 | 104.64 | 105.96 | 102.50 | N/A | N/A | N/A | N/A |

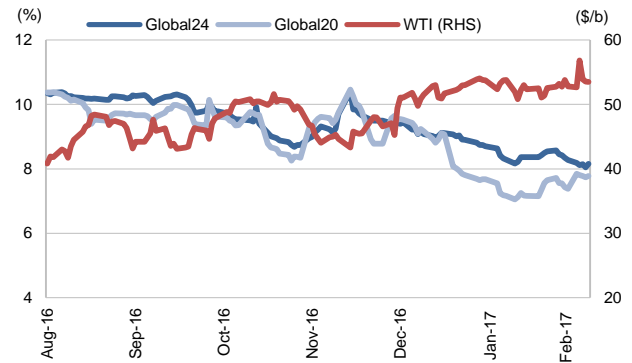
Source: Bloomberg and Analytica

EMBIG Spread



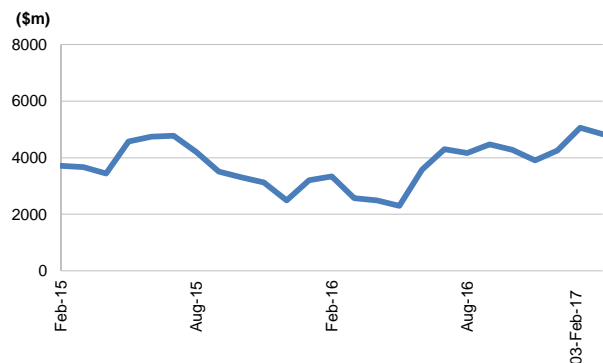
Source: JP Morgan and Analytica

Bond Yields vs. WTI in 2017



Source: Bloomberg and Analytica

International Reserves



Source: BCE and Analytica

which he said that the leader of the corruption ring at Petroecuador was none other than Glas. None of them had however made these interviews public. Later, he and his allies and Twitter cohorts linked them to the fugitive Isaías brothers because the room furnishings were the same. It was swiftly revealed that the furnishings, including curtains and lamps, were not the same because they were filmed at an Isaías residence in Miami, but because they were filmed at the Coral Gables Hyatt. Still, the government insists on linking the case to the Isaías and, through them, attacking conservative opposition candidate Guillermo Lasso (Creo) by saying that they had forced him to nominate Quito legislator Andrés Páez as his running mate (Páez had played a leading role in mobilizing anti-Correa protests in the capital in 2015). But as the dispute escalated and videos of Pareja blaming Glas while connected to a polygraph hit the internet, Correa counterattacked him on his Saturday propaganda broadcast, using epithets like “psychopath” and “drug addict,” and released private e-mails in which Pareja in October begged for clemency. Pareja became angry and emboldened, and released videos directed at Correa personally.

As an erstwhile climax, Pareja said that, in fact, Correa was the one who was at the top of the corruption scheme, seeking to demonstrate this by revealing an e-mail from last June in which Correa said he would protect him. The exchange included orders for head of communications Patricio Barriga to unleash a media campaign to discredit the “miserable (Fernando) Villavicencio,” the investigative journalist whose muckracking set the ball rolling on revealing the extent of corruption in the government-controlled energy sector. The e-mail, according to Pareja, “proves that president Correa was behind everything, even of the most minimal, of all the details,” and also accused Correa of “treason” for his plan to hand over the Sacha oilfield. Incensed, Correa published the full exchange on Twitter, “so you can see how this poor man lies.” Other than providing context for the report,

Correa’s tantrum confirmed that the e-mail Pareja showed indeed was true, and additionally revealed that he was supposed to sign a deal with Halliburton to de-facto privatize the 70,000 barrel-a-day Sacha field for a desperately needed \$1.5bn loan. The exchange also included a cryptic message from Pareja saying that he had left “backups at the home of JG.” As Correa inadvertently revealed the address of his personal e-mail account, individuals began to send him more or less polite requests to resign.

Meanwhile, Pareja not only pointed his barbs at Correa and Glas. He also alleged that the prosecutor general, Galo Chiriboga, and the comptroller general, Carlos Pólit, had received briefcases full of cash in a Quito luxury hotel. Besides Pólit, other comptrollers had also been paid off to provide favorable reviews of the stalled Manta refinery project, Pareja said. So far, the government has paid more than \$1.5bn for a project that is currently a vast empty lot leveled by controversial Brazilian construction firm Odebrecht, at the heart of the giant corruption scandal that has hit governments throughout Latin America and parts of Africa. In that case, Chiriboga’s office drew ire of social networks after local whistleblowing web site Ecuadortransparente revealed that the prosecutor’s office in January had rejected evidence provided by its counterpart in the Brazilian state of Parana. Its argument was that it couldn’t hire a translator for the 26 pages of documents. Ramiro García, president of the Pichincha bar association, said this was a criminal act.

A further twist came when former president Abdalá Bucaram (1996/1997) from his Panamanian exile got involved in the dispute, accused several close associates of Correa of corruption, and said that in 2006, Pareja on behalf of Correa had sought support and funding from him and from Banco Pichincha lead shareholder Fidel Egas. On his part, Egas corroborated the claims regarding Correa’s request for money. After Egas refused him, in the early years of the presidency, Correa won a suit against the bank

for \$600,000 in a dispute that, according to the president, stemmed from a dispute over a \$140 credit card bill. In that case, Chiriboga represented the president.

Despite the immense scandal, the immediate impact on the election is unclear. The final polls of voting intent were inconclusive, and the street demonstrations called for February 9 attracted only small crowds. Polls continue to coincide only in a decline of support for Moreno and mostly incremental gains among other leading candidates, in particular Lasso. Two polls do predict a runoff as they estimate that Moreno will fail to capture 40% of the vote outright (he is still seen with more than a ten-point lead over Lasso). But current data, despite all the caveats associated with polling methodology, points to a nail-biter result. Correa, meanwhile, said that he is certain AP will retain a solid majority in the congress.

Another Loss

Ecuador lost another oil-related arbitration case, this time with Burlington Resources, a unit of ConocoPhillips. The company, at the time a minority partner of French oil company Perenco, sued for around \$1.5bn in damages after the Correa administration seized its assets in the country amid a tax dispute. While attorney general Diego García boasted about having reduced the damage awarded by the International Centre for Settlement of Investment Disputes (ICSID) to \$379.8m plus interest, the award comes as fiscal strain continues. Alleging mistakes in the suit, García said he would seek to have the ruling annulled.

Critics have focused their ire on García for losing yet another arbitration proceeding after Ecuador had to pay Occidental Petroleum close to \$1bn last year for confiscating its assets in 2006. Instead, more generally, the accountability of the state and its officials for populist handling of foreign investment and disregard for proportionality need to become part

of the debate. Indeed, the "tribunal's decision on damages sends a clear message that governments cannot expropriate investments without fair compensation," said Janet Carrig, ConocoPhillips's legal counsel, in a statement.

In this case, the Perenco/Burlington had refused to pay the increased windfall tax on oil sales after Correa in September 2007 had jerked the poorly-worded "minimum 50%" rule up to 99%. This led the Correa administration to seize and sell the oil, then prompting the companies to say they would abandon production altogether. Arguing that they had to avoid environmental and engineering damage, the government then had the fields confiscated. To a small extent, ICSID agreed, setting the damages claimed by Ecuador at \$42m. But with the present ICSID ruling setting a negative precedent, the damage in the Perenco-Burlington case is set to grow as a decision on the majority partner has yet to be announced.

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