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ECUADOR WEEKLY REPORT®

For the week of February 1 – February 5, 2016

Feeling the Pain

In the lead gaffe of the day, president Rafael Correa on January 30 insisted that "call it what you will, crisis, recession; academically we know that we are not in a crisis." Irrespective of the subjectivity of the term, he went on to blame his government's academic woes on the fall of oil prices, disregarding that the crisis of 1998-2000, which he blames on bank deregulation, was more than anything else triggered by similar external events, including natural disasters and even lower oil prices (poor bank oversight did contribute to that crisis). Banks, now tightly regulated, felt the pinch of the recession in 2015, with net profit dropping 19% to $271m from $335m in 2014. Assets fell 8.2% on the year to $30.86bn from $33.62bn. Revenues, meanwhile, increased 5% to $3.52bn from $3.36bn in 2014, while spending including taxes and the 15% of profits distributed by law to employees rose 7.5% on the year to $3.25bn from $3.02bn.

The cooling economy has spooked Ecuadoreans who had kindly ignored some of the more dangerous comments made by bank regulators and other financial officials in the boom years. As a result, deposits have suffered. Given Ecuador's economic history and the current recession, the public has started to worry about the health of banks. Banks' gross portfolio

ECONOMIC INDICATORS

Ecuadorian Global Bonds (Feb 4, 2016)

	BID	ASK
Global 2024	67.00	68.00
Global 2030	67.00	73.00

Source: Bolsa de Valores de Quito

BCE International Reserves
In million US$

May, 2015	4,567.46	**25.00%**
Jul, 2015	4,771.97	**4.00%**
Sep, 2015	3,511.56	**-26.00%**
Nov, 2015	3,126.32	**-11.00%**
Jan 22, 2016	3,203.79	**2.48%**

Source: Banco Central del Ecuador

Inflation

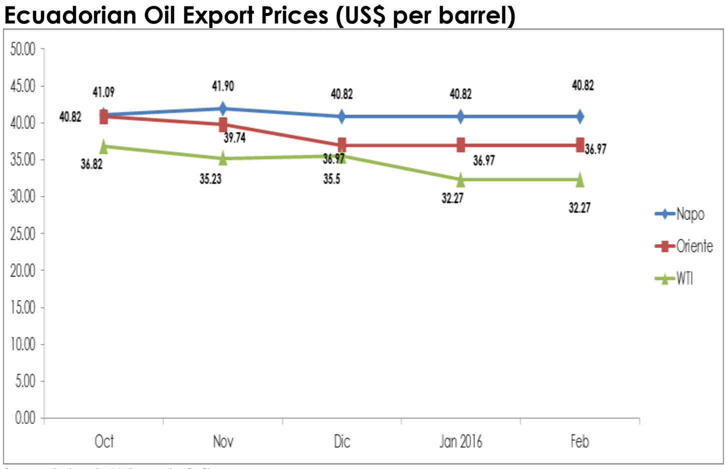
Jan	2015	0.31%
Year to Date		0.31%
Year on Year		3.09%

Banks – Short and long term Deposits
In million US$

Sep, 2015	14,498.80	**-1.28%**
Oct, 2015	14,582.60	**0.65%**
Nov, 2015	14,313.10	**-1.85%**
Dic, 2015	14,554.40	**1.69%**
Jan 22, 2016	14,718.70	**1.13%**

Source: Banco Central del Ecuador

Ecuadorian Oil Export Prices (US$ per barrel)



Source: Bolsa de Valores de Quito

declined 4.5% on the year to $18.77bn from $19.65bn the previous year. Total deposits showed double-digit declines of 12.9% on the year in 2015 to $22.62bn from $25.97bn, a fall of $3.35bn. Cash deposits, still more than a third of all deposits, fell by 19.7% to $8.02bn, down $1.19bn from $9.98bn. Savings deposits dropped 11.4% to $7.2bn from $8.13bn. Term deposits trailed, declining a more moderate 5.8% on the year to $7.4bn from $7.86bn. Of these, 61% are 90 days or less, while just 3% has a horizon beyond 361 days, reflecting the general lack of confidence in Ecuador's economy. The amount of deposits as a share of GDP thus fell below 25%, from 26.3% in 2014 to 22.8% in 2015. After growing at a heady rate around 10% annually through 2013 and until peaking at 15% in August 2014, deposit growth slowed and turned negative around the middle of 2015.

With more public demand for cash, banks had to respond by reducing lending to maintain what they consider safe liquidity levels. This decline however was significantly lower than the fall in deposits: Banks lent companies (69.6%) and consumers (30.4%) $981m, or about 1% of GDP, less than in 2014. Corporate debt dropped 10.8% on the year to $8.5bn from $9.54bn a year earlier. Consumer debt fell 9.9% to $5.89bn from $6.53bn in the same period. Against the negative trend, real estate lending continued to grow, albeit more slowly than a mid-year peak of around 15%, but still topping 12%; mortgages ended the year at $1.77bn. Microcredit grew 9.8% on the year to $1.5bn. Unsurprisingly, non-performing loans (NPL) increased significantly overall to 3.7%, a rise of 0.8 percentage points from December 2014. Corporate borrowers have the lowest rate of NPL at 1.1%, followed by education at 5.1%,

Quito and Guayaquil Stock Exchanges

Equities Most Traded			
Issuing Company	**Cash Value** (From Jan 25 to Jan 29 , 2016) (In Thousands US$)	**Closing Price** (In US$)	**Last Date of Trade**
CORPORACIÓNFAVORITA C.A.	466.73	2.10	4/02/2016
BOLSA DE VALORES DE QUITO	75.00	75,000	29/01/2016
RETRATOREC S.A.	74.42	3.89	29/01/2016
CERVECERIA NACIONAL	49.80	66.00	28/01/2016
SOCIEDAD AGRICOLA E IND. SAN CARLOS	20.70	1.02	29/01/2016
HOLCIM ECUADOR S.A.	14.78	67.19	4/02/2016
FIDEICOMISO OMNI HOSPITAL	7.00	7,000	2/02/2016
INVERSANCARLOS	5.60	1.12	26/01/2016
CONCLINA S.A.	2.77	1.00	27/01/2016
BANCO GUAYAQUIL	1.83	0.52	29/01/2016

Source: Precios máximos y mínimos de acciones & Pulso Bursátil Semanal
Issued by: Bolsa de Valores de Quito.

Fixed Income					
Securities lead by Analytica					
Issuing Company	**Issue Type**	**Total Amount Issued** (In Thousand US$)	**Credit Rating**	**Term** (In years)	**Yield of Return**
OTECEL S.A.	Commercial Paper	50,000	AAA	1	4.25%
ECONOFARM SANA SANA	Securitization	12,500	AAA	5	7.25%
FARCOMED FYBECA	Securitization	12,500	AAA	5	7.50%
EDESA	Commercial Paper	10,000	AAA	1	5.25%
DEXICORP-GRUPO KFC	Commercial Paper	7,500	AA+	1	6.00%
URBANO EXPRESS	Securitization	4,000	AAA-	3	7.50%
		5,000		5	8.00%

microcredit of 5.7%, and consumers at 6.9%. Banks have had to cover the risk of increased NPL by provisioning $1.29bn, almost double the total amount of NPL. Additionally, NPL reached an erstwhile peak in November at $856.76m, falling to $687.2m in December. Christmas bonuses might have helped individuals get current with their loans in the last month of the year. Worryingly, the bank regulator since the end of June has failed to report the composition of credit according to risk levels; at the time, it rated 96.4% as less risky "A" and "B" loans. On the positive side, the administration has had a change of heart towards the banking industry. Rather than impose the harsh options permitted by the financial reform of 2014, which makes it possible for the government to push credit into certain favored industries, it has become concerned for financial stability, allowing some fees and interest rates to rise, although just marginally so far. While this will help banks' bottom lines, it won't necessarily lead banks to inject anti-cyclical cash into the economy.

Get a Job

Around the crack of dawn, dozens of working-age men assemble on Cuenca's central San Francisco square, filling up the eastern half of the square. Many wait for hours before getting work in some of the dwindling construction projects. Some don't succeed at all. Formal employment has been falling too, as evidenced by high-profile layoffs at the likes of Indurama, also based in Cuenca, which let go 400 staffers, and Maresa, which shuttered its 38,000-a year car assembly plant in northern Quito mid-December, axing 300 jobs. While the administration denies any involvement, both companies' fates illustrate the failures of government intervention. In the case of Indurama, the company invested heavily in new induction ranges. The Correa administration has heavily promoted the use of induction to cook as a soft way to phase out the liquefied petroleum gas subsidy, thanks to the abundance of electrical energy it predicts the new hydroelectric plants will start to provide this year. Regardless of how successful this rather challenging project might prove, president Rafael Correa undermined the company's efforts doubly: In December 2014, he ordered a punitive tax on the gas-fueled ranges the company manufactured, doubling their price. Once Indurama had already pushed deeply into the production of the new induction ranges, Correa was still dissatisfied with consumers' lack of enthusiasm for the new technology, and announced he would have 130,000 units imported at cut-rate prices from China, with which Indurama couldn't compete. In the case of Maresa, the government argued that Mazda, the company whose cars the company was assembling, discontinued its BT-50 model, the sole one under production. At the Frankfurt motor show last September, Mazda sales managers told reporters that sales would be discontinued in Europe but that "we have some other markets within the Mazda family talking about taking BT-50, so there is a good chance the number of countries taking it will grow into the future." The outlook for Maresa's plant meanwhile is unclear, and testimony for the lack of success the government's protectionism has had. A much-quoted Deloitte survey from late 2015 said most jobs had been lost in construction over the year (-27.6%), followed by oil companies (-26.9%), and the automotive sector, with 21.2% of jobs lost.

The latest employment data finally acknowledged the loss of jobs. INEC, the statistics and census bureau, registered an unemployment rate of 4.77% for its three-month survey of 31,092 households in December. A year earlier, the rate came in at 3.8%. Administration officials tout the still low rate as "the lowest in Latin America," and, indeed, it is still significantly below the regional average estimated at 6.7% by the United Nations' Economic Commission for Latin America and the Caribbean. Labor minister Leanardo Berrezueta said the latest data was, happily, below a previously unannounced 5% target. The figure, which would imply full employment in an industrialized country, however comes with a major caveat. In 2014, INEC changed its measure of "underemployment" by introducing the term of "adequate" and "inadequate" employment. As critics alerted at the time, the modification resulted in a fall in the "underemployment" category, which previously remained stubbornly close to 55%, reflecting how few people actually have steady jobs. With the weakening economy, the number of people in "adequate" jobs dropped to 54% from 56.4% at the end of 2014, and still shows huge numbers of people don't hold stable jobs. Out of 7.5m economically active Ecuadorians, 800,000 earn the monthly minimum wage of $366. Among government staffers not permanently employed, 5,500 out of 90,000 failed to get their temporary contracts extended, according to Berrezueta.

To deal with the deteriorating situation, Berrezueta announced some welcome plans, including tax breaks for hiring, and, perhaps most importantly, options for employers to hire workers for individual projects, such as a construction project or work limited to planting season. Sadly, an unexpected letter from Correa and Berrezueta to employees severely undermined the trust of entrepreneurs in the government's sincerity. Worried about how Correa's political movement might fare in the 2017, the letter aimed to prove the government's leftwing credentials. The letter, delivered to hundreds of companies, thanked employees for their work, reminded them of Argentine-Cuban revolutionary Ernesto "Che" Guevara, and pledged "the supremacy of human work over capital," led by Correa's revolution. In response, Ecuador's Entrepreneurial Committee said it was "deeply worried" by the letter, asking the labor ministry to refrain from sending similar messages in the future, given the private sector's dominant role in providing jobs in the country. The president refused to consider this. "How sad that the entrepreneurs have gotten angry," he responded in an ironic tone.