

PUBLIC AFFAIRS

Economic Measures announced amid External Shocks

The Ecuadorian Government has announced measures to address fallout from the global crisis

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The global economic crisis resulting from the spread of COVID-19 represents a major external shock to the Ecuadorian economy. So far, the most notable effects have been a dramatic drop in the price of oil, appreciation of the dollar, and a significant increase in Ecuador's country risk. These three elements together caused major fiscal restrictions that have required the government to announce economic measures in an effort to limit the fallout.

A COMPLEX ECONOMIC SCENARIO

Ecuador still has a credit facility provided by the International Monetary Fund (IMF), which has been ongoing since March 2019. This has made obtaining financing from multilateral credit organizations possible and Ecuador has maintained access to international markets during this past year.

However, because Ecuador's government has been unable to meet certain goals related to increasing international reserves and certain regulations that did not make it through the nation's Congress, disbursements have been delayed. These issues arose at the end of 2019 and again in March 2020, so a new payment schedule is expected to be drafted. According to a press conference held on the evening of March 10, the new schedule will be ready in a few weeks. However, for now, the program remains unchanged.

The expansion of COVID-19 has affected the country, especially in regards to the economy, revolving around three main issues: reduction of oil prices, appreciation of the dollar, and increased country risk. On this last issue, the impact has been such that the risk increased to 2,792 points (March 9), surpassing even that of Argentina.

MEASURES TO TAKE THE CRISIS HEAD ON

In a nationally televised message, president Lenin Moreno announced the economic measures that the government believes to be necessary to take on the crisis.

According to Finance Minister Richard Martínez, this package will generate \$2.252 billion in revenue.

The details are as follows:

- \$1.4 billion in budget cuts. Of these, \$800 million will be in goods and services, while \$600 million will be in capital assets. He specified that "healthcare is not included in these cuts."
- Elimination of public institutions including: The Youth Secretary, 4 regulation and control agencies, 3 public companies, 4 technical secretariats, and the public media company.
- Reduction of public servants' salaries by "a small percentage" (without specifying exactly how much). He said that the idea is to avoid "massive layoffs."
- A one-time tax of 5% of the value on vehicles appraised at over \$20,000.
- External financing in the amount of \$2 billion, without specifying the sources (this amount would be outside of the overall global credit package mentioned above).
- Resetting some of the maturities of bilateral debt "to fit our new reality."
- An increase of 0.75% in income tax source withholdings made by companies, including "those from the banking, oil, and telecommunications sectors."
- Sending a Public Finance Code to the National Assembly as an urgent economic measure.
- The government obtained \$ 60 million from international agencies that have specific funds for emergencies "like coronavirus."

COMMENTARY AND OUTLOOK

The measures point in the right direction.

They seek to reduce public expenditures, but do not affect social spending (namely, in health), and will not affect the nation's poorest groups.

The package amount will be insufficient.

This is because the magnitude of the economic problem is much larger. It is important to keep in mind that even without this crisis, Ecuador already needed some \$10 billion in financing for 2020.

The plan still lacks detail. Especially in terms of financing sources, which apparently total \$2 billion, under better conditions than current financing options.

March will be an economically difficult month. Because the government needs about \$1 billion to pay off capital and interest on loans beyond its normal running expenditures. This means that payments to suppliers will likely be late.

A calming message about the financial sector. The president was emphatic in mentioning that the private financial system is strong, trustworthy, and has liquidity. This likely comes in response to doomsday rumors about a possible bank holiday.

No gasoline price variations were mentioned. At least in this package, no price increases were mentioned for regular unleaded fuel. While a decision on this matter is necessary on a structural level, it would be politically destabilizing.

Protests and social outcry. There will be some of this, but given the limited scope of the measures, the probability of destabilizing actions is rather unlikely. Regardless, additional measures that could significantly affect Ecuador in terms of its economy or incorrect messages could result in larger scale protests.

A difficult road ahead. These measures have yet to be implemented, and tax reforms will have to go through Congress. Given that this is a year before elections, the entire process could suffer setbacks and changes.

Immediate actions in the legislature. Tomorrow (March 11) the Congress's Administration Council will meet with leaders of the various political parties and the Ministry of Finance to deal with the country's economic situation. In all likelihood, they will discuss the reforms to be sent to the Congress and the measures that were announced.

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