GRAY/19/506
Revised

March 7, 2019

**Statement by Mr. Razafindramanana, Mrs. Boukpessi, and Ms. Nankunda on Ecuador (Preliminary)
Executive Board Meeting
March 11, 2019**

We thank staff for their well-written report and Mr. Tombini and Mr. Rivadeneira for their insightful Buff statement.

Economic activity in Ecuador continues to suffer from the adverse effects of external shocks, including the sharp decline in oil prices and the US dollar appreciation, which have negatively affected the country's financial position and competitiveness. Wage increases have further dampened the latter. The medium-term outlook is titled to the downside with risks stemming from further decline in prices of oil, continuous appreciation of the real effective exchange rate (REER), tighter external financing conditions and possible political and social strains which could constraint the implementation of the authorities' policy plan. We also note the high and still rising debt as well as the low level of international reserves.

Against this backdrop and given the authorities' stated commitment to address the imbalances and structural challenges identified in their discussions with Staff, **we support the proposed three-year Extended Arrangement under the Extended Fund Facility (EFF) to assist the country meet large financing needs.** Fund support will be key to sustain the authorities' efforts aimed at ensuring fiscal sustainability, enhancing resilience to future shocks and laying solid foundations for a sustainable and inclusive growth while protecting the most vulnerable.

We broadly agree with staff assessment and policy recommendations and wish to emphasize the following points.

We commend the authorities' strong commitment to restore fiscal discipline and sustainability which is crucial to swiftly bring the public debt below 40 percent of GDP.

We note the upfront adjustment plan underpinned by a comprehensive policy package to lower the non-oil primary balance including subsidies by 5 percent of GDP by 2021. On the revenue side, we welcome the upcoming reform of the tax system along with further measures to enhance tax administration. On the spending front, the authorities are encouraged to sustain their efforts in containing the wage bill, rationalizing other expenditures—including the misclassified capital spending—and overhauling fuel subsidies while protecting the poor. As such, the focus on accelerating poverty reduction as indicated in Messrs. Tombini and Rivadeneira's Buff statement is appreciated. Moreover, we look forward to the authorities' strategy aiming at better targeting social programs and benefits, notably in education and health, and improving safety nets for the vulnerable groups. *Staff's comments on the timing and status of preparation of this upcoming strategy is welcome*.

Recent changes in the medium-term fiscal policy framework, notably the ban of budget financing by the Central Bank of Ecuador (CBE), are significant steps towards enhancing fiscal discipline, encouraging transparency and accountability, and strengthening the autonomy of CBE. They are also critical to establishing sounder oil cash management during boom periods, to building buffers to help create fiscal space necessary to meet countercyclical needs, and to maintaining fiscal sustainability. Regarding efforts to curb public, we look forward to the public financial management action plan by end April 2019 and *would appreciate staff's update on the related technical assistance received so far and/or planned looking forward.* We welcome the steps taken in improving governance and addressing corruption, including the implementation of the Citizens' Participation and Social Control Council, and the efforts to improve the country's AML/CFT framework in line with international standards.

We encourage the authorities to press ahead with measures to safeguard the financial and liquidity system with the view to minimize financial stability risks and support growth. In this context, while we note that the banking sector is sound and stable, with adequate capital and profitability ratios, emerging risks from a rapid pace of credit growth of both corporates and households call for appropriate macroprudential measures and closer oversight. Ensuring financial stability is also predicated on the authorities addressing the sovereign-financial linkages. Furthermore, strengthening the CBE's governance and independence framework as well as preserving its liquidity and reserves are warranted to support the dollarized economy. Attention should also be given to enhancing the supervisory, regulatory and crisis preparation frameworks to build financial resilience. The last FSAP for Ecuador took place in 2004. An update could be envisaged as it would allow discussions on options for strengthening the financial sector. *Staff' view will be appreciated.*

On structural reforms, we urge the authorities to implement the envisaged measures to foster competitiveness and reduce labor market rigidities. We take positive note of the authorities' comprehensive reforms to address existing rigidities in the labor market. Reforms should also aim at easing regulations and enhancing competition in the goods and services and financial markets more broadly. Finally, participation in Regional Trade Agreements (RTAs), with the benefit of strengthened productivity and competitiveness, could buttress Ecuador's trade and external position.

With these remarks, we wish the Ecuadorian authorities further success in their endeavors.