FOR
AGENDA

EBS/85/202 & Cor. 1

CONFIDENTIAL

August 23, 1985

To: Members of the Executive Board

From: The Acting Secretary

Subject: Ecuador - Staff Report for the 1985 Article IV Consultation and Review Under Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Ecuador and a review under its stand-by arrangement. A draft decision appears on page 28. Decisions regarding the completion of the review of the stand-by arrangement and the exchange system will be circulated at a later date, together with a supplement to this report.

Mr. Bonangelino (ext. 7148) is available to answer technical or factual questions relating to this paper prior to the Board discussion, which has been tentatively scheduled for Friday, September 20, 1985.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

ECUADOR

Staff Report for the 1985 Article IV Consultation and Review Under Stand-By Arrangement

Prepared by the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations, Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by Eduardo Wiesner and Manuel Guitian

August 23, 1985

Contents | Page

Contents

I. Introduction

The 1985 Article IV consultation discussions with Ecuador and the mid-term review under the current one-year stand-by arrangement were initiated in Quito in the period June 10-21, 1985 and were concluded in Washington on June 26, 1985. The representatives of Ecuador in the discussions included the Ministers of Finance and Public Credit; Commerce, Industry, and Integration; Natural Resources and Energy; Labor; and the General Manager of the Central Bank, as well as other senior officials of the public sector. The mission also met with representatives of the private banking community. The staff representatives in the mission were Messrs. Bonangelino (Head), Gronlie, Rennhack (all WHD), Antonaya (FAD), de Schaetzen (ETR), and Ms. Choy-Luy (Secretary-ADM).

Ecuador has made one purchase equivalent to SDR 21.1 million under the stand-by arrangement which became effective on March 11, 1985, thus bringing the Fund's holdings of sucres to 175.2 percent of quota, including 56.7 percent under the compensatory financing facility (Table 1). The second purchase, also in an amount equivalent to SDR 21.1 million, which was scheduled for May 15, 1985 has not yet been made; Ecuador has not complied with the performance criterion related to the unification of the offical and intervention markets for foreign exchange which applied to that purchase (see discussion below). It is now expected that the second and third purchases, for a total of SDR 42.2 million, will be made upon completion of the present review.

II. Background and Performance Under the Stand-By Program

Following several years of strong growth and balance of payments surpluses through 1980, economic activity in Ecuador weakened while inflation accelerated. Growth remained positive during the 1981-82 period mainly because of expansionary demand management policies which were adopted in the face of adverse external developments, particularly the weakening of world petroleum markets. However, such policies also gave rise to a marked widening of the current account deficit of the balance of payments. This development, together with a significant decline in the net inflow of capital in 1981-82, resulted in large reductions in the net international reserves of the Central Bank, including the accumulation of external payments arrears in 1982.

To reverse these trends and stem the loss of reserves, adjustment measures were adopted in 1982, including a devaluation of the sucre (the first in ten years) and an increase in taxes and administered prices. Additional measures were taken in early 1983 in the context of a stabilization program supported by a one-year stand-by arrangement, which became effective in July 1983. The program aimed at limiting the reserve loss of the Central Bank through the adoption of a crawling peg exchange system in the official market supplemented by a widening of the scope of the intervention market of the Central Bank. The program also called for a tightening of demand management policies, including a major strengthening of the public finances.

Table 1. Ecuador: Transactions with the Fund During Period of Arrangement

	Outstanding Dec. 31, 1984	1985 Jan.-Mar.	1985 Apr.-June	1985 July-Sept. 1/	1985 Oct.-Dec.	1986 Jan.-Mar.
	(In millions of SDRs)					
Transactions under tranche policies	157.5	21.10	--	42.20	21.10	21.10
Ordinary resources	(81.7)	(10.55)	(--)	(21.10)	(10.55)	(10.55)
Enlarged access resources	(75.8)	(10.55)	(--)	(21.10)	(10.55)	(10.55)
Repurchases	--	--	--	--	--	--
Ordinary resources	(--)	(--)	(--)	(--)	(--)	(--)
Enlarged access resources	(--)	(--)	(--)	(--)	(--)	(--)
Transactions under special facilities 2/	85.4	--	--	--	--	--
Purchases	(85.4)	(--)	(--)	(--)	(--)	(--)
Repurchases	(--)	(--)	(--)	(--)	(--)	(--)
Total Fund credit outstanding (end of period)	242.9	264.0	264.0	306.2	327.3	348.4
Under tranche policies	(157.5)	(178.6)	(178.6)	(220.8)	(241.9)	(263.0)
Special facilities 2/	(85.4)	(85.4)	(85.4)	(85.4)	(85.4)	(85.4)
	(In percent of quota)					
Total Fund credit outstanding (end of period)	161.2	175.2	175.2	203.2	217.2	231.2
Under tranche policies	(104.5)	(118.5)	(118.5)	(146.5)	(160.5)	(174.5)
Special facilities 2/	(56.7)	(56.7)	(56.7)	(56.7)	(56.7)	(56.7)

Source: International Monetary Fund.

1/ Assumes that the purchase equivalent to SDR 21.10 million which had been scheduled for May 15, 1985 will be made during July-September.

2/ Compensatory financing facility.

The stabilization program was implemented as planned. The public sector deficit declined from 6.8 percent of GDP in 1982 to virtual equilibrium in 1983 (Table 2). The current account deficit of the balance of payments was reduced from over 11 percent of GDP in 1982 to about 1.5 percent of GDP in 1983, and the overall balance of payments position shifted from a deficit of US$671 million in 1982 to a surplus of US$52 million in 1983, including a reduction of US$110 million in external payments arrears. At the same time, the economy experienced a severe reduction of output mainly because of damage caused by severe floods to agricultural production. The rate of price increase surged to over 50 percent during 1983 because of the disruptions in agriculture, the depreciation of the sucre, and adjustments in administered prices.

Economic growth resumed in 1984 and inflation was reduced to 25 percent. As the economy recovered from the impact of the floods, real GDP rose by 4 percent last year. The public sector deficit was less than 0.5 percent of GDP and the balance of payments registered an overall surplus of US$60 million in 1984,1/ including a reduction of external payments arrears of US$40 million.

After the expiration of the stand-by arrangement in mid-1984, rapid credit expansion by the Central Bank contributed to an accelerated depreciation of the sucre in the parallel market and threatened to put renewed pressure on prices. The new Administration, which took office in August 1984, moved quickly to forestall any significant deterioration. On September 4, 1984 the sucre was devalued de facto as most private foreign exchange transactions were shifted from the official to the more depreciated intervention market. After this action, the official market consisted primarily of public sector transactions (including exports of oil), selected import payments, and the servicing of external loans disbursed before September 4, 1984. At the same time, the practice of depreciating the sucre daily in the official market was terminated, and both the official and the intervention exchange rates were fixed at the levels reached on September 4.2/

Due to political pressures, however, about half of the imports initially shifted to the intervention market were returned to the official market in subsequent weeks, leaving about 40 percent of imports in the official market compared with 60 percent before September 4, 1984. The authorities also reduced the minimum financing period from 360 days and 180 days to 120 days for the majority of imports, and lowered certain import duties. In November 1984 the legal reserve requirement on demand deposits was raised, and toward the end of the year the authorities took additional measures, including an upward

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1/ This takes into account the debt relief provided by rescheduling under the aegis of the Paris Club of the arrears to official creditors which were accumulated in the period June-December 1984.

2/ The selling rates in the official and intervention markets were fixed at S/. 67.85 per U.S. dollar and S/. 96.50 per U.S. dollar, respectively.

Table 2. Ecuador: Main Economic Indicators

	1980	1981	1982	1983	Prel. 1984
		(Percentage change)			
Real GDP	4.9	3.9	1.2	-3.1	4.1
Real GDP (excluding petroleum)	6.7	3.7	1.7	-6.4	2.9
GDP deflator	19.5	14.3	17.8	37.9	35.7
Consumer Prices					
Average	12.8	14.7	16.3	48.4	33.0
End of period	13.7	17.3	24.4	52.5	25.1
Money and quasi-money 1/	26.2	11.4	21.0	32.0	47.0
		(In percent of GDP)			
Overall public sector balance	-4.6	-5.6	-6.8	-0.2	-0.4
Balance of payments current account 2/	-7.0	-10.0	-11.6	-1.4	-2.5
		(In millions of U.S. dollars)			
Overall balance of payments	226	-294	-671	52	60

Source: Central Bank of Ecuador; and Fund staff estimates.

1/ End of period.
2/ GDP converted to U.S. dollars using exchange rate implied by the 1971 purchasing power parity.

adjustment of interest rates and sharp increases in the domestic prices of petroleum products (by 65 percent for gasoline and 100 percent for diesel).

In support of Ecuador's economic program for 1985, the Fund approved the current stand-by arrangement on March 11, 1985. The program was designed to consolidate the gains made in 1983-84 and to continue the adjustment process. The objectives of the program are to attain balance of payments equilibrium in 1985 (after taking account of debt relief operations) and to reduce inflation further to about 20 percent. In support of these objectives the program calls for unification of the exchange system, pursuit of a flexible exchange rate policy, a further strengthening of the public finances, and a monetary policy consistent with the balance of payments and inflation aims of the program.

A key feature of the program is the unification of the exchange system. The stand-by arrangement called for unification of the official and intervention markets prior to the second purchase under the arrangement which was scheduled to take place on May 15, 1985, and for the complete unification of the exchange system through the transfer of all current transactions from the parallel market to the intervention market, before completion of the mid-term review.1/ As a part of the process of exchange market unification, in March and April 1985 the authorities transferred petroleum exports by the state oil company, public debt service payments for debt disbursed before September 4, 1984, and imports of food items and agricultural machinery from the official to the intervention market. In early June 1985 all transactions remaining in the official market, except imports of medicine and related items (about 9.5 percent of imports in 1984) and petroleum exports by foreign oil companies (19 percent of exports in 1984), were transferred to the intervention market.

Trade-related payment arrears to private creditors, which had been eliminated by early July 1984, re-emerged soon after the previous stand-by arrangement expired and reached US$100 million by mid-August 1984, before declining to US$60 million by the end of the year. These arrears were reported to have been eliminated by the end of February 1985, before approval by the Executive Board of the current stand-by arrangement. In clearing the arrears, sucre deposits equivalent to an amount estimated at the time to be about US$37 million were to have been returned to importers at the end of March for lack of proper documentation that the goods in question had been cleared through customs, with the remainder being settled in foreign currency. As it turned out, however, the deposits were not returned partly because of administrative delays but also due to strong pressures from importers who feared they would lose the exchange rate guarantee if the sucre deposits were returned to them; instead, importers were given 30 days from end-March

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1/ The current transactions in the parallel market are basically purchases and sales of foreign exchange for tourism, study, and medical care abroad.

to provide documentation (see EBS/85/25, Supplement 1, 3/8/85). Subsequently, two 30-day extensions were given with the second expiring on June 30, 1985. At the end of June the deposits corresponding to the arrears subject to verification had been reduced to the equivalent of US$38 million from US$56 million at the end of March.1/ Since the beginning of July the Central Bank has been engaged in the process of eliminating the remaining deposits by either returning them to the depositors or by providing foreign exchange if verified as genuine arrears.

The stand-by arrangement also contemplated that the prior import deposit requirements would be eliminated before the second purchase scheduled for May 15, 1985. The obligation to constitute such deposits was removed on March 28, 1985, but the authorities gave importers the option to continue making deposits as a means of obtaining an exchange rate guarantee from the Central Bank. This option was eliminated in early June in order to avoid possible exchange losses by the Central Bank.

Ecuador has observed all quantitative performance criteria relating to the second and third purchases under the stand-by arrangement. As of June 30, 1985, the Central Bank's net domestic assets, its net credit to the public sector, and the external debt of the public sector were well below the established ceilings. As of the same date, the net official international reserves of the Central Bank were substantially above the target (Table 3). However, Ecuador's right to make purchases after April 30, 1985 is subject to the unification of the official and intervention exchange markets of the Central Bank and after July 31, 1985 is subject to the completion of the mid-term review. The program calls for full unification of the exchange system before completion of the mid-term review by incorporating in the unified market the current transactions presently in the parallel market.

In the attached cable dated August 2, 1985, the Minister of Finance and the General Manager of the Central Bank of Ecuador have confirmed that the indicative limits on the outstanding external debt of the public sector for the period January 1-February 28, 1986, shown in Table 4 of the memorandum annexed to their letter of intent of January 9, 1985 (EBS/85/25), are appropriate as performance criteria. At the time the stand-by arrangement was approved, these limits had been set as indicative and the authorities are now requesting by their cable that they be converted into performance criteria.

As mentioned earlier, the stand-by arrangement stipulates that Ecuador cannot make purchases after April 30, 1985 if the official exchange market and the intervention market are not unified. Since Ecuador did not unify these markets by that date, a waiver of this

1/ The amount of arrears subject to verification was revised by the Central Bank from the estimate of US$37 million as of the end of February 1985.

Table 3. Ecuador: Performance Under Stand-By Arrangement 1/

	1984 Dec.	1985 March	1985 June
(In billions of sucres)			
Net domestic assets			
Ceiling 2/	...	29.3	30.8
Actual	27.3	24.6	25.5
Margin/excess (-)	...	4.7	5.3
Net credits to public sector			
Ceiling 2/	...	-62.4	-72.7
Actual	-59.1	-69.1	-79.7
Margin/excess (-)	...	6.7	7.0
(In millions of U.S. dollars)			
Net international reserves			
Target 3/	...	71	91
Actual 4/	110.5	96 4/	116 4/
Excess/shortfall (-)	...	25	25
External debt 0-12 years			
Limit	...	5,750.0	5,750.0
Actual	5,648.5	5,643.4	5,636.4
Margin/excess (-)	...	106.6	113.6
External debt 0-1 year			
Limit	...	350.0	350.0
Actual	292.5	292.8	287.8
Margin/excess (-)	...	57.2	62.2

Source: Central Bank of Ecuador.

1/ The ceilings on net domestic assets, net credit to the public sector, and the targets for net international reserves presented in EBS/85/25 have been adjusted on the basis of actual figures for December 31, 1984 to preserve the flows projected in the program. These adjustments were stipulated in the footnotes to the Tables 1, 2, and 3 annexed to the authorities' letter of intent of January 9, 1985 attached to EBS/85/25.

2/ Ceilings applicable to quarters ending in the months indicated.

3/ Targets applicable to end-of-calendar quarter.

4/ As defined for the purpose of the program, sucre deposits in the Central Bank corresponding to external payments arrears have been included as reserve liabilities, except arrears to bilateral creditors, which were refinanced in April 1985 under the aegis of the Paris Club, and to foreign commercial banks, which were extended in 1984 in anticipation of a medium-term loan to settle such arrears. The remaining arrears amounted to US$60 million at the end of 1984, and were eliminated by March 4, 1985, except for arrears subject to verification which amounted to US$56 million at the end of March and US$38 million at the end of June, and which have been included as reserve liabilities.

performance criterion would be necessary even if Ecuador subsequently unified the exchange system. A recommendation for such a waiver would be made in a supplement to the present report if the full unification of the exchange system is effected before completion of the mid-term review by the Executive Board, as expected.

III. Report on the Discussions and Revised Projections for 1985

At the time the last Article IV consultation was completed by the Executive Board on June 20, 1984, the authorities were urged to address the structural problems of the Ecuadoran economy, particularly through the pursuit of flexible exchange and interest rate policies and by adjusting administered prices to more realistic levels. In recognition of the need to improve the efficiency of the economy, the new Administration, which took office in August 1984, moved quickly to initiate structural reforms by making large transfers of exchange transactions to the more depreciated intervention market and by raising domestic energy prices substantially. Subsequently, they introduced greater flexibility in interest rates. Executive Directors noted these improvements of policy at the time they considered the current stand-by arrangement.

This year's discussions with the Ecuadoran authorities centered on a review of the progress made in the implementation of the program with emphasis on the prospects for achieving its main objectives. The authorities emphasized the adjustment made in the context of the program, and they were encouraged by the response in terms of financial performance. The overall balance of payments results of the first half of the year had been favorable and the growth of domestic financial savings had been considerably faster than projected.

The authorities regretted, however, that inflation had failed to decelerate as envisaged. It had been expected that the rate of inflation would accelerate somewhat in the early months of the year because of the exchange rate measures and the adjustment of administered prices, particularly gasoline prices, but that it would subsequently decelerate to the pace projected in the program. Instead, the 12-month rate of inflation has accelerated from 25 percent in December 1984 to almost 30 percent in January 1985 and then remained close to that rate through June. The authorities attributed this development partly to the effect of bad weather on the production of food items and it was their view that inflation would soon begin to decelerate. They still believe that a decline in the rate of inflation could be achieved for the year as a whole, although of a smaller magnitude than originally projected; the end of year rate of inflation is now projected to be about 22.5 percent, compared with an original projection of 20 percent.

Looking ahead, the authorities expressed concern about the impact of the recent weakening of the international price of petroleum on public sector revenue and the current account of the balance of payments.

However, the authorities reiterated their determination to comply with the program by taking additional adjustment measures if these should prove necessary.

1. Fiscal policy

As mentioned above, the overall deficit of the public sector is estimated to have remained virtually unchanged in 1984 at less than 0.5 percent of GDP (Table 4). While the performance of the public enterprises and decentralized institutions weakened in 1984, the central government position improved from a deficit of 2.9 percent of GDP in 1983 to one of 0.9 percent of GDP in 1984. The program for 1985 calls for the public sector to generate a surplus equivalent to 3.4 percent of GDP, mainly on the basis of a sizable increase in petroleum revenue resulting from the unification of the exchange rate and the adjustment in the domestic prices of petroleum products at the end of 1984.

Revised projections, which incorporate the effects of a reduction in the estimated average export price of crude oil from US$27 per barrel to US$25 per barrel and a downward adjustment of public investment spending, indicate that the overall surplus in the public sector would be about 2.2 percent of GDP in 1985.1/ Despite the lower surplus being projected, the authorities believe that the programmed net buildup of deposits by the public sector in the Central Bank is still feasible as the net utilization of long-term project-related external financing is now estimated to be larger than originally envisaged. The revised estimate of external financing is still consistent with the existing limits on public sector external debt, which apply to debt with a maturity of up to 12 years.

The original program projection for public sector revenue for 1985 implies an increase of almost 6 percentage points of GDP with respect to the preliminary figures for 1984. Of this increase, petroleum revenue would provide nearly 5 percentage points of GDP, while other sources of revenue would recover from their low level of 1984 and increase by 1 percentage point. Based on the downward revision in the export price of oil referred to above, it is now expected that the petroleum revenue will be 2.9 percentage points of GDP lower than originally projected in the program. Nonpetroleum revenues are projected to exceed the program target in sucre terms, but are expected to fall somewhat short in terms of GDP. Thus, total public sector revenue is projected to fall 3.3 percentage points of GDP short of the program target.

1/ Based on a revised GDP projection for 1985. While the growth of real GDP for 1985 remains unchanged from the original program projection, the nominal GDP has been revised upward because the actual GDP in 1984 was higher than previously estimated and because of a higher GDP deflator now projected for 1985 (see table on Selected Economic and Financial Indicators, Attachment II).

Table 4. Ecuador: Summary of Public Sector Operations

	1983	Prel. 1984	1985 Program Original	1985 Program Rev.
	(In billions of sucres)			
Total revenue	152.5	216.7	311.2	303.4
Petroleum revenue	59.7	102.6	166.1	151.4
Nonpetroleum revenue	92.8	114.1	145.1	152.0
Total expenditure	153.1	219.6	279.4	281.4
Current	111.7	164.7	201.7	211.0
Capital	41.4	54.9	77.7	70.4
Overall surplus or deficit (-)	-0.6	-2.9	31.8	22.0
External financing	3.4	9.8	—	9.8
Drawings	8.5	18.7	14.5	19.8
Amortizations	5.1	8.9	14.5	10.0
Domestic financing	-2.8	-6.9	-31.8	-31.8
Central Bank (net)	-1.6	-6.3	-31.8	-31.8
Other banks	-1.2	-0.6	--	--
Other	--	--	--	--
	(In percent of GDP)			
Total revenue	27.4	27.6	33.4	30.1
Petroleum revenue	10.7	13.1	17.9	15.0
Nonpetroleum revenue	16.7	14.5	15.5	15.1
Total expenditure	27.6	28.0	30.0	27.9
Current	20.1	21.0	21.6	20.9
Capital	7.5	7.0	8.4	7.0
Overall surplus or deficit (-)	-0.2	-0.4	3.4	2.2
External financing	0.6	1.3	—	1.0
Drawings	1.5	2.4	1.6	2.0
Amortizations	0.9	1.1	-1.6	1.0
Domestic financing	-0.5	-0.9	-3.4	-3.2
Central Bank (net)	-0.3	-0.8	-3.4	-3.2
Other banks	-0.2	-0.1	--	--
Other	--	--	--	--

Sources: Ministry of Finance; Central Bank of Ecuador; and Fund staff estimates.

Under the program, public sector expenditure had been projected to reach 30 percent of GDP in 1985, a level that would imply an increase of 2 percentage points of GDP over the preliminary expenditure figures of 1984. However, because of the projected revenue shortfall (but taking into account the larger than expected recourse to net long-term external financing), the authorities will need to keep total public expenditure to less than 28 percent of GDP in 1985. Two thirds of this adjustment will fall on capital expenditure because of the relative lack of flexibility of current expenditures in the short term. In absolute amounts, total expenditure in 1985 will need to be kept very close to the level originally established under the program. The authorities reaffirmed their intention to keep total spending within the program limits and agreed that it was important to monitor revenue developments very closely so that expenditure policies can be tightened promptly should the position deteriorate from the revised projections.

The larger than anticipated net utilization of external financing by the public sector reflects higher disbursements of project-related loans from multilateral and bilateral sources and lower amortization payments reflecting the rescheduling with official creditors on a larger scale than earlier envisaged. The revised projection indicates that net external disbursements would be of the order of S/. 10 billion in 1985 (roughly US$110 million), which seems feasible both in relation to the level of public sector investment and to the actual amount disbursed in 1984 (approximately US$160 million).

Regarding the system of revenue earmarking, the authorities pointed out that all the additional revenue resulting from the transfer of oil exports from the official to the intervention market would be allocated to the budget. Beyond this, however, it appears that no further progress in this area can be expected in the near future. The staff emphasized the need to seek to reduce revenue earmarking further, and stressed the importance of dismantling this system as soon as feasible.

2. Monetary policy

The general public's holdings of money and quasi-money (M2) moved up sharply in the last half of 1984 after the new Administration took office and, as noted earlier, transferred a large part of the foreign exchange transactions of the private sector from the official to the more depreciated intervention market and subsequently raised deposit rates (by 2-3 percentage points to the range of 20-22 percent). For the year as a whole, M2 grew by 47 percent (compared with 32 percent in 1983) with quasi-money increasing by 70 percent and money by 42 percent (Table 5); in real terms, the growth of M2 exceeded 17 percent during 1984. The improvement in the private capital account from 1983 to 1984 was in excess of US$500 million, equivalent to about 50 percent of M2 at the beginning of 1984.

Table 5. Ecuador: Banking System Operations 1/

	Dec. 1983 Actual			Dec. 1984 Actual			Dec. 1985 Program			Dec. 1985 Rev. Proj.		
	Central Bank	Other banks	Total	Central Bank	Other banks	Total	Central Bank	Other banks	Total	Central Bank	Other banks	Total
	(In billions of sucres)											
Net international reserves	4.7	--	4.7	10.5	--	10.5	4.7	--	4.7	10.5	--	10.5
Other foreign assets	--	-7.5	-7.5	--	-7.4	-7.4	--	-4.5	-4.5	--	-5.5	-5.5
Net domestic credit	67.4	181.6	249.0	116.9	245.5	362.4	133.7	307.6	441.3	135.5	320.1	455.6
Public sector (net)	-54.5	-3.5	-58.0	-59.1	-4.8	-63.9	-87.5	-3.9	-91.4	-90.9	-4.8	-95.7
Private sector	18.4	153.2	171.6	22.9	206.1	229.0	26.8	273.3	300.1	29.2	260.5	289.7
Net unclassified	103.5	31.9	135.4	153.1	44.2	197.3	194.4	38.2	232.6	197.2	64.4	261.6
Interbank transactions	41.7	-47.2	-5.5	70.0	-53.9	16.1	90.7	-90.7	--	80.9	-62.2	18.7
Credit	57.4	-67.4	-10.0	92.7	-89.3	3.4	117.6	117.6	--	111.1		
Deposits	-15.7	20.2	4.5	-22.7	35.4	12.7	-26.9	26.9	--	-30.2		
Intersystem transactions	12.6	--	12.6	36.9	--	36.9	37.0	-0.6	36.4	41.1	--	41.1
Allocation of SDRs	3.2	--	3.2	3.2	--	3.2	3.2	--	3.2	3.2	--	3.2
Medium- and long-term foreign liabilities	87.8	4.2	92.0	189.4	4.1	193.5	210.5	4.2	214.7	213.4	4.1	217.5
Liabilities to private sector	35.4	122.7	158.1	41.7	180.1	221.8	52.4	207.6	260.0	51.4	248.3	299.7
Currency in circulation	24.9	--	24.9	34.6	--	34.6	40.3	--	40.3	42.2	--	42.[illegible]
Demand deposits	0.7	52.8	53.5	0.7	76.1	76.8	1.0	87.3	88.3	0.9	97.6	98.5
Time and savings deposits	--	16.7	16.7	--	28.5	28.5	--	30.6	30.6	--	40.0	40.0
Certificates of deposits	--	--	--	--	--	--	--	--	--	--	18.0	18.0
Advance import deposits	3.7	--	3.7	--	--	--	--	--	--	--	--	--
Other sucre liabilities	5.5	36.7	42.2	5.6	53.8	59.4	9.8	63.9	73.7	7.6	67.0	74.6
Liabilities in foreign currency	0.6	4.1	4.7	0.8	6.2	7.0	1.3	4.0	5.3	0.7	5.7	6.4
Capital and reserves	--	12.4	12.4	--	15.5	15.5	--	21.8	21.8	--	20.0	20.0
	(In millions of U.S. dollars)											
Net international reserves and net foreign assets	49.5	-78.9	-29.4	110.5	-77.9	32.6	49.4	-47.4	2.0	110.5	-57.9	52.6

Sources: Central Bank of Ecuador; and Fund staff estimates.

1/ Foreign exchange account valued at S/. 95 per U.S. dollar.

Notwithstanding the increased flow of resources to the banking system during 1984, the growth of the system's net domestic assets turned out to be lower than had been projected earlier; the rate of increase in credit to the private sector was slower than had been expected and the increase in the public sector's net deposits with the Central Bank was larger than had been projected. In relation to liabilities to the private sector at the beginning of the year, credit to the private sector expanded by 36 percent but only by about 15 percent when adjustment is made for the amount corresponding to the special credit facility created as a counterpart of the private sector external debt assumed by the Central Bank ("stabilization credit") in connection with the rescheduling of private sector debt with foreign commercial banks.1/

As a result of these developments in domestic credit and the stronger than expected growth of financial savings, the net foreign asset position of the banking system at the end of 1984 was US$30 million higher than projected; the net international reserves of the Central Bank reached the equivalent of US$110.5 million at the end of 1984, compared with a projection of US$49.5 million (EBS/85/25, Supplement 1).

The growth of M2 continued to be strong during the first several months of 1985, and at the end of May it was 53 percent above the level of 12 months earlier; the increase in quasi-money was particularly strong in this period as it rose by 134 percent. Domestic prices increased by 29 percent over this 12-month period, and thus the increase in M2 in real terms was some 18 percent. While time and savings deposits grew by over 58 percent during the 12 months through May, more than half of the absolute increase in quasi-money originated in the new certificates of deposit which the banks were authorized to issue earlier this year. The savings mobilized by these certificates increased from zero to S/. 12 billion in three months and came to represent 27 percent of the holdings of quasi-money at the end of May; the sharp growth in certificates outstanding appears to have reflected in part the attraction of funds from outside the banking system.2/ The interest rate on

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1/ Under this refinancing scheme, the private sector pays the Central Bank, in accordance with the original maturities, the sucre amount of the external debt service on the basis of the exchange rate on the date of conversion. The Central Bank supports, through special rediscount operations ("stabilization credits"), the domestic banks which extend credit for the servicing of such debt. The Central Bank assumes the debt as it is being serviced in sucres by the private sector and charges a commission to cover the exchange risk. Initially, the maturity on stabilization credits ranged from 18 to 24 months. However, in October 1984 the maximum maturity on such credit operations was extended to 7 years, which is the term at which the private sector foreign debt assumed by the Central Bank has been rescheduled. Details on these operations are provided in EBS/83/230.

2/ The placement of such certificates reached about S/. 17 billion as of mid-July.

these certificates is determined freely in the market and have been in the range of 25-29 percent. Since the growth of credit to the private sector during the first part of this year was increasing at an annual rate similar to that projected under the program (about 25 percent), and since central bank credit to the public sector was well within the limits stipulated in the program (Table 6), the recent growth in M2 reflects a strengthening of the demand for financial assets on the part of the general public.

On the basis of these developments and the policies in place, M2 is projected to grow by 42 percent in 1985 and the banking system's total liabilities to the private sector are expected to rise by 35 percent; the latter compares with an original projection of 25 percent under the program. Moreover, with the faster growth now envisaged in the public's real holdings of domestic financial assets, the banking system would seem to be in a position to increase its net foreign assets position in 1985 rather than maintaining it unchanged as envisaged in the program. To ensure that the growth of central bank credit is consistent with the target for net official international reserves, the authorities not only intend to achieve the programmed net buildup of public sector deposits at the Central Bank but also stand ready to sell stabilization bonds to the banks and the private sector.

In view of the relatively strong growth of resources in the banking system, the authorities felt it was not urgent to raise controlled interest rates at this time, or to increase the flexibility of rates, for example, by lowering the minimum denomination of S/. 1 million on the new certificates of deposit. They noted that the deceleration of inflation and the interest rate adjustments of 1984 had reduced the gap between domestic inflation and interest rates during the last year and a half 1/ and they drew attention to the recent appreciation of the currency in the parallel exchange market from about S/. 120 per U.S. dollar in February 1985 to around S/. 107 per U.S. dollar in mid-July. Also, they emphasized that the reduction in the monthly rate of price increase that is expected during the second half of 1985 would go a long way toward assuring that controlled rates would be adequate.

3. Wage policy

The program assumed that wage increases in 1985 would be limited to the projected rate of inflation of 20 percent. However, after a political controversy, a 28.8 percent increase in the basic legal minimum wage plus increases in various cash benefits were put into effect from March 1, 1985. The Congress had sought to increase the

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1/ The interest rate structure was adjusted upward twice in 1984, by up to 6 percentage points for some lending and time deposit rates, and by 4 percentage points in the case of the savings rate. With these changes, the rate on savings deposits and nine-month term deposits became 20 percent and 22 percent, respectively.

Table 6. Ecuador: Central Bank Operations 1/

	Dec. 1984	March 1985		June 1985		Sept. 1985	Dec. 1985	
	Actual	Program	Actual	Program	Actual	Program	Program	Proj.
	(In billions of sucres)							
Net international reserves	10.5	6.8	9.1	8.7	11.0	9.6	10.5	10.5
Reserves	16.2	6.8	14.4	8.7	14.6	9.6	10.5	10.5
Arrears	-5.7	--	-5.3	--	-3.6	--	--	--
Net domestic assets	27.3	29.1	24.6	30.6	25.5	32.8	35.6	35.6
Net credit to public sector	-59.1	-62.4	-69.1	-72.7	-79.7	-81.7	-90.9	-90.9
Net credit to financial institutions	110.1	110.4	117.0	113.4	118.3	116.5	119.4	125.9
Commercial and development banks	(73.2)	(73.4)	(80.0)	(75.9)	(80.5)	(78.6)	(81.2)	(84.8)
Other financial institutions	(36.9)	(37.0)	(37.0)	(37.5)	(37.8)	(37.9)	(38.2)	(41.1)
Net credit to private sector	15.8	16.1	14.9	16.8	15.3	17.6	18.9	20.0
Medium- and long-term foreign liabilities	-189.4	-188.5	-192.1	-190.8	-193.3	-193.7	-198.9	-213.4
Other	149.9	153.5	153.9	163.9	164.9	174.1	187.1	194.0
Currency issue	37.8	35.9	33.7	39.3	36.5	42.4	46.1	46.1

Source: Central Bank of Ecuador, and Fund staff estimates.

1/ Foreign exchange accounts valued at S/. 95 per U.S. dollar.

basic legal minimum wage by an amount in excess of 50 percent, but this bill had been vetoed by the President. In a second round, the President accepted the total adjustment proposed by the Congress, provided a portion (17.5 percent) was delayed until January 1, 1986. The authorities regretted these developments, which despite their efforts to the contrary provided wage increases in excess of the projection. In the public sector, wage increases were awarded on a sliding scale declining to zero for public employees earning more than the minimum wage, except for teachers and members of the Armed Forces who were awarded increases above the public sector norm.1/ This sliding scale, and the fact that the salary increase only entered into effect in March, resulted in an estimated increase in the wage bill of about 20 percent, and thus was in conformity with the projection of the program.

The authorities explained that they intend to keep wage increases to a range of 15-18 percent next year. The staff emphasized to the authorities the need to pursue a restrictive wage policy in order to make a significant reduction of inflation in 1986 possible.

4. External policies

The overall balance of payments for 1984 turned out to have been stronger than had been projected. As mentioned earlier, after taking account of debt rescheduling operations, an overall surplus of US$60 million was achieved compared with a projection of equilibrium (Table 7).2/

The better than expected performance reflected developments in the capital account. The current account deficit widened to nearly US$250 million in 1984 from US$126 million in 1983, and was US$36 million higher than projected earlier because of a higher deficit on the services account. In fact, the trade surplus was US$145 million higher than had been envisaged. In terms of GDP, the current account deficit reached 2.5 percent in 1984 compared with 1.4 percent in 1983 and 2.3 percent estimated earlier. The larger net capital inflow than projected reflected mainly net inflows of private capital with net borrowing by the public sector in line with the forecast.

1/ The salary increase in the public sector was applied in the following manner: the full absolute increase in the basic minimum wage was applied to salaries in the range of S/. 6,600 (basic minimum wage prior to March 1, 1985) - S/. 14,700 per month, and for the salary range of S/. 14,701 - S/. 16,600 the increase was the difference between S/. 16,600 and the actual salary which applied until March 1, 1985. There was no increase for salaries in excess of S/. 16,600 per month.

2/ It should be noted that the projection for the overall balance of payments deficit for 1984 in EBS/85/25 did not take into account debt relief granted by the Paris Club in 1985 for payments which fell due in the period June-December 1984.

Table 7. Ecuador: Summary Balance of Payments

	1982	1983	1984	1985 Prog.	1985 Rev.
	(In millions of U.S. dollars)				
Current account	-1,195	-126	-248	-210	-300
Trade account	162	957	1,056	963	931
Exports, f.o.b.	(2,343)	(2,365)	(2,623)	(2,713)	(2,581)
Petroleum	/1,525/	/1,750/	/1,835/	/1,904/	/1,764/
Other	/818/	/615/	/789/	/809/	/817/
Imports	(-2,181)	(-1,408)	(-1,567)	(-1,750)	(-1,650)
Services account	-1,377	-1,107	-1,324	-1,193	-1,251
Services, credit	(391)	(323)	(350)	(410)	(410)
Services, debit	(-1,768)	(-1,430)	(-1,674)	(-1,603)	(-1,661)
Interest 1/	/-767/	/-711/	/-837/	/-808/	/-776/
Fund charges	/--/	/-3/	/-13/	/-25/	/-25/
Other	/-1,001/	/-716/	/-824/	/-770/	/-860/
Transfers	(20)	(24)	(20)	(20)	(20)
Capital account	524	178	308	74	300
Public sector	660	608	231	42	218
Drawings 2/	*(883)*	*(698)*	*(403)*	*(297)*	*(415)3/*
Interest rescheduled	(--)	(43)	(15)	(--)	(--)
Amortization 4/	(-700)	(-121)	(-187)	(-255)	(-197)
Other 5/	(477)	-12	--	--	--
Private sector	-136	-430	76	32	82
Direct investment	(40)	(50)	(50)	(75)	(75)
Drawings 2/	(806)	(12)	(--)	(--)	(--)
Interest rescheduled	(--)	(5)	(3)	(--)	(--)
Amortization 4/	(-630)	(-117)	(-25)	(-83)	(-69)
Other 6/	(-352)	(-380)	(48)	(40)	(76)
Overall balance	-671	52	60	-136 7/	--
Net official international reserves (increase -)	460	58	-20	41	60
Arrears (decrease -)	211	-110	-40 8/	-41	-60
Financing gap	--	--	--	-136 7/	--
Memorandum items					
Total debt relief	555	2,091	1,207	1,044	1,139
Public debt	19	1,083	584	1,044	1,028
Principal	(19)	(1,039)	(568)	(1,044)	(1,028)
Banks	/19/	/972/	/502/	/1,044/	/906/
Paris Club	/--/	/37/	/66/	/--/	/122/
Other	/--/	/30/	/--/	/--/	/--/
Interest	(--)	(44)	(16)	(--)	(--)
Paris Club	(--)	(15)	(16)	(--)	(--)
Other	(--)	(29)	(--)	(--)	(--)
Private debt	536	1,008	623	--	111
Principal	(536)	(1,003)	(620)	(--)	(111)
Paris Club	/--/	/27/	/33/	/--/	/38/
Regulation 101/83 9/	/--/	/854/	/587/	/--/	/73/
Other 10/	/536/	/122/	/--/	/--/	/--/
Interest: Paris Club	(--)	(5)	(3)	(--)	(--)
	(In percent of GDP)11/				
Current account	-11.6	-1.4	-2.5	-2.0	-2.7

Sources: Central Bank of Ecuador; and Fund staff estimates.

1/ Includes interest payments rescheduled.
2/ On a cash basis.
3/ Excludes US$179 million of a US$200 million loan from commercial banks to be used for elimination of arrears to banks which were extended in anticipation of the loan.
4/ Net of debt relief.
5/ Includes petroleum-related credit.
6/ Includes errors and omissions.
7/ Financing gap corresponding to debt service payments to official creditors, expected to be refinanced under the aegis of the Paris Club in April, 1985.
8/ Excludes arrears on debt servicing to official creditors which accumulated during June-December 1984, which were rescheduled under the aegis of the Paris Club in April 1985.
9/ Private debt assumed by the Central Bank of Ecuador.
10/ Privately arranged refinancing, partly conducted under Regulation 1202/82.
11/ GDP converted to U.S. dollars using exchange rate implied by the 1971 purchasing power parity.

The projected current account deficit for 1985 has been revised upward to US$300 million from the original figure of US$210 million. A key factor in the revision is the downward adjustment of oil prices. As discussed earlier, the average price of oil in 1985 has been revised downward by US$2 to US$25 per barrel, nearly US$2.50 per barrel lower than the average price in 1984. The revised assumption is consistent with a decline in the price to about US$24 per barrel in the second half of the year. The export volume of crude and oil derivatives also has been revised downward slightly. As a result of these changes, the value of petroleum exports is expected to be almost US$1.8 billion in 1985, or some US$140 million lower than originally projected.

It is expected that the export shortfall will be partly offset by a slower growth of imports than previously envisaged and, as a result, *the current account deficit is likely to be about US$90 million larger* than originally projected and about US$50 million larger than in 1984. The revised deficit is equivalent to 2.7 percent of GDP, compared with an original projection of 2 percent of GDP.

Despite the larger current account deficit now envisaged, the authorities and the staff believe that the target of overall balance of payments equilibrium for 1985 can be achieved because net capital inflows to the public and private sectors are likely to exceed the projection of the program. The upward revision in net private capital inflows is based on developments in the first months of the year and appears to reflect a more positive response than had been expected from the private sector to the Government's exchange and interest rate policies.

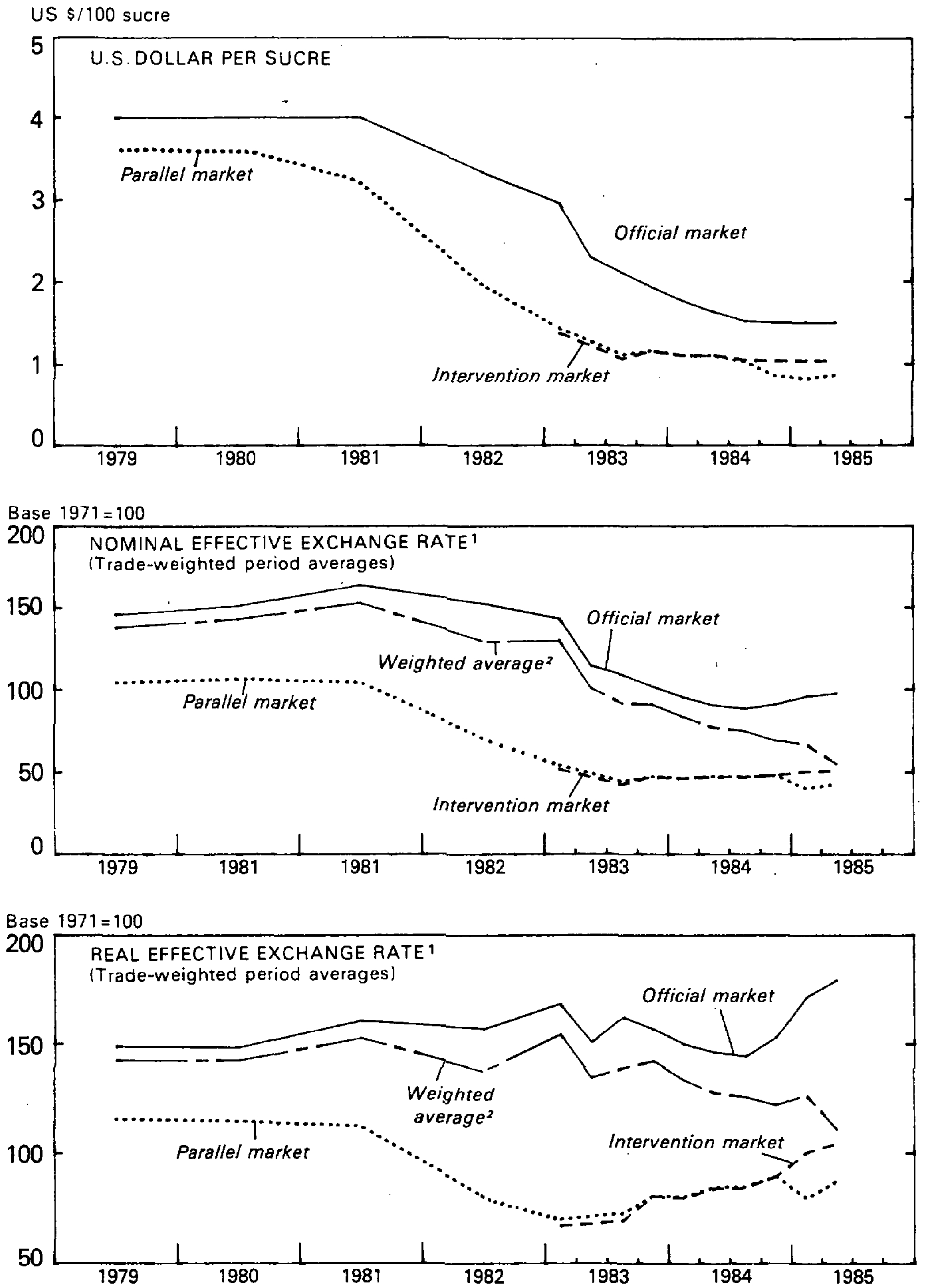
Despite the delays in completing the transfer of foreign exchange transactions from the official to the intervention market, the authorities felt that on the whole they had made significant progress toward unification of the exchange system. They reaffirmed their intention of completely unifying the exchange markets before the completion of the mid-term review by the Executive Board, including the transfer to the intervention market of all transactions remaining in the official market, and the incorporation in the unified market of all current transactions presently in the parallel market. Moreover, the authorities restated their determination to manage the exchange rate in the unified market flexibly and are studying alternative modalities for flexible exchange rate management. A decision on this is expected shortly as the authorities intend to begin implementing the flexible exchange rate system as soon as the markets are unified.

With the transfer of transactions from the official to the intervention market since September 4, 1984, the sucre has depreciated in real terms by approximately 12 percent through May 1985 (Chart). However, such a depreciation has not fully offset the loss of competitiveness experienced over several years through 1981. The authorities

CHART 1

ECUADOR

CHANGES IN THE VALUE OF THE ECUADORAN SUCRE



Sources: *International Financial Statistics;* Central Bank of Ecuador; and Fund staff estimates.

[1] Foreign currency denominated index. An appreciation of the sucre is shown by an upward movement.

[2] Until March 1983, it is calculated as an average of the official and parallel market rate, weighted by the distribution of current transactions between the two markets. Thereafter, it is calculated as an average of the official, parallel and intervention market rates, weighted by the distribution of current transactions between the three markets.

have indicated that the planned unification of the exchange market and introduction of flexible exchange rate management will permit them to achieve this objective.

The authorities explained that the delays in clearing the trade-related payments arrears under verification, referred to in Section II, were caused mainly by administrative problems and have informed the staff that significant progress in clearing these arrears has been made in recent weeks. The authorities are confident that they would be able to completely eliminate these arrears in a short period of time and in any event before completion of the mid-term review by the Executive Board.

With regard to external debt management, the Ecuadoran authorities reached agreement in principle earlier this year with their external commercial bank creditors on a multiyear refinancing arrangement of public debt for the period 1985-89. In securing the agreement with the banks, the authorities undertook to seek a new stand-by arrangement with the Fund in 1986, and to request semiannual consultations under the enhanced Article IV consultation procedures for each year after 1986 during the term of the refinancing agreement, i.e., through 1996. The commercial banks will reschedule all new and previously refinanced maturities falling due in 1985-89, amounting to about US$4.2 billion. For 1985 the agreement includes refinancing of US$979 million, a new loan of US$200 million, most of which will be used to pay off trade-related debts to the banks which, as mentioned earlier, had been extended in 1984, and the maintenance of trade credit lines. The agreement for the US$200 million loan is expected to be signed by mid-August and the rescheduling contract shortly thereafter.

At a meeting of the Paris Club in April 1985, Ecuador secured the restructuring of the maturities on its official and officially guaranteed external debt falling due over the three-year period 1985-87, as well as the rescheduling of arrears on principal outstanding on such debt at end-1984. The Agreed Minute of the Paris Club provides for interest to be paid according to original schedules and for interest in arrears to be paid before September 30, 1985. The official creditors will reschedule 100 percent of the unpaid principal which fell due in the period June-December 1984 and payments falling due in 1985; 85 percent of those which will fall due in 1986; and 70 percent of those which will fall due in 1987. Negotiations for the signing of the corresponding bilateral agreements are presently under way.

The agreement under the Paris Club is contingent upon an arrangement with the Fund in the upper credit tranches being in place through March 10, 1987. For the remainder of the consolidation period, the Agreed Minute provides that the rescheduling is conditional upon creditors reaching a positive assessment that, inter alia, "Ecuador either has an arrangement in the upper credit tranches with the International Monetary Fund expiring not sooner than December 31, 1987, or has set forth in the process of consultation with the Fund, and is implementing, a comprehensive and satisfactory economic program including quantitative quarterly targets and limits, and covering the period up to December 31, 1987. In making their assessment, the participating creditor countries will have available both the staff report indicating whether Ecuador's program advances the adjustment effort implemented in the previous stand-by programs and the Fund Managing Director's summary of the Board discussions."

Because a larger amount of principal payments was eligible for refinancing than had been anticipated previously, the amount of debt relief obtained is nearly identical to the assumptions of the stand-by program, even though interest payments were not covered as had been envisaged earlier.

As a result of these debt rescheduling agreements, Ecuador's debt servicing burden for 1984 and 1985 has been reduced substantially. On an accrual basis (but taking previous debt restructuring into account) the debt service ratio averaged 75 percent in 1984 and 1985 but was reduced to about 35 percent in both years as a result of the agreements concluded in 1985.

In the area of trade policy, the authorities have taken a number of measures to liberalize imports. In September 1984 certain import duties were lowered, the minimum financing requirement for imports was reduced and the bulk of the import prohibitions imposed in 1982 and not yet removed were lifted. At the end of February 1985 the remaining import prohibitions were eliminated and in late March 1985 the advance import deposit requirement was also lifted. In addition, a bilateral payments agreement with a Fund member was cancelled earlier this year. The authorities indicated that the minimum import financing requirement would be reduced further; as a first step they intend to raise the cash payment portion from the current maximum of 20 percent. Moreover, the authorities saw no reason to continue any of the barter requirements which were introduced in 1982 as part of the emergency measures taken at that time and they intend to remove these requirements soon.

The authorities are currently in the process of modifying Ecuador's regulations affecting foreign investment and revising the tariff structure, two changes which the staff feels will be conducive to strengthening Ecuador's balance of payments in the medium to longer run. The proposed changes contemplate a more liberal policy on profit remittances, broaden the legal rights of investors in cases of investment disputes, allow foreign investors to purchase shares in local companies, and give foreign investors access to long-term domestic credit. The authorities are also planning to eliminate the requirement that foreign investments be joint ventures with domestic companies in order to gain access to the domestic market or to export outside the Andean region. The proposed tariff reform involves the adoption of the Brussels nomenclature, the lowering of the maximum tariff rates, and the reduction of the dispersion in tariff rates.

IV. IBRD Operations in Ecuador

Net disbursements by the IBRD to Ecuador increased sharply in 1984, to almost US$50 million, from an average of about US$30 million in the preceding four years (Statistical Appendix Table 13). This increase reflected higher gross disbursements, which reached nearly US$67 million. Of this, about 70 percent represented credit to small- and medium-sized industrial firms, some 10 percent was for highway construction, with the remaining amount allocated to a wide variety of projects. In the first six months of 1985 the Bank disbursed US$19.0 million.

The IBRD made no new loan commitments to Ecuador in 1984, but issued an economic report (No. 5094-ES) in October 1984 as the basis for formulating the Bank's medium-term lending strategy, under which the Bank would support macroeconomic adjustment policies and sectoral reform. As a follow-up to the report and at the request of the authorities, the IBRD also undertook an evaluation of the public sector investment program in which it expressed the view that priority should be given to projects oriented toward export activities. The IBRD staff indicated that investments in the petroleum sector should continue to be attractive, as significant increases in output are feasible. Transmission lines for electric power and secondary road construction also were viewed favorably, although caution was stressed with respect to the further expansion of hydroelectric generating capacity and the construction of primary roads.

The IBRD lending program for the medium term would support policies aimed at reducing economic distortions and generating foreign exchange and could include program as well as project lending. In particular, on the basis of an appropriate exchange rate policy, the Bank is seeking to support a process of trade liberalization, the implementation of an efficient energy pricing policy, the development of a more flexible interest rate regime, and improvements in public sector management. These policies would be supported by a five-year lending program which could range from US$300 to US$500 million and would focus on agriculture, industry, infrastructure, and energy. To the extent possible, the Bank expects to emphasize faster disbursing loans that make limited fiscal demands and permit the use of existing investments. More specifically, a US$100 million agricultural sector loan, a US$30 million small scale enterprise credit operation, and a US$100 million industrial finance operation are being processed.

V. Medium-Term Outlook

The staff has revised the medium-term outlook for Ecuador's balance of payments and debt servicing on the basis of the latest available indicators. In spite of the downward revision of oil prices, the broad conclusion presented in EBS/85/25 still appears to be applicable. Provided that satisfactory policies are pursued, Ecuador should be able to maintain a viable balance of payments position throughout the remainder of the 1980s; however, in 1990 after the present rescheduling agreement with foreign commercial bank expires, a sizable financing requirement would reappear (Table 8). While the authorities believe that by that time the country should be able to obtain replacement financing on a voluntary basis, the possibility of a significant gap would point to the need for further strengthening the adjustment policies.

The principal revision concerns oil exports. In view of the present weakness of the oil markets, the staff has revised the previous assumption of 6 percent annual growth of oil exports for the period 1986-90, to increases of about 5 percent on average for 1986-87 with the rate of growth rising gradually to around 6.5 percent by 1990. In line with earlier projections, export volume is assumed to increase at an annual rate of 3 percent to some 82 million barrels by 1990, which is thought to be feasible in view of the present efforts to expand domestic production and in the light of Ecuador's low share in total world output. According to the revised projections, after a decline of about 10 percent in 1985, the price of oil is assumed to increase by about 2 percent on average in 1986-87, 3 percent in 1988, and 3.5 percent thereafter. These price assumptions, which imply a continued decline of oil prices in real terms, are below those used for the purpose of the latest WEO exercise.

The authorities' commitment to a flexible exchange rate policy and to the maintenance of an adequate level of external competitiveness should make possible a gradual acceleration in the rate of growth of non-oil exports; the average rate of growth assumed for the period 1986-90 (7.6 percent) is similar to that registered during the period before the appreciating trend of the sucre in the first half of the 1970s. The revised medium-term scenario envisages an increase in the ratio of imports to GDP from 14.7 percent in 1985 to 15.3 percent by 1990. These assumptions are estimated to be broadly consistent with a growth of real GDP of some 2 3/4 percent on average during the next five years.

Interest payments are expected to continue to increase until 1987 when they will reach just under US$900 million; thereafter, they will decline gradually as foreign indebtedness stabilizes and then slowly declines. Interest rate assumptions have been revised downward from the medium-term scenario presented in EBS/85/25 by about 1 percentage point to 9.5 percent for the three-month LIBOR and 10 percent for the U.S. prime rate. Noninterest service payments are assumed to remain around 7.7 percent of GDP throughout the period, while service income is assumed to increase from about 4 percent of GDP in 1985 to slightly over 5 percent by 1990. Based on these assumptions, the current account deficit is projected to widen to about US$325 million by 1987 and then gradually decline to around US$50 million by 1990. In relation to GDP, the current account deficit would decline throughout the period from about 2.7 percent in 1985 to 0.3 percent by 1990.

EBS/85/202
Corrected: 9/17/85

Table 8. Ecuador: Medium-Term Balance of Payments Projections

	1984	1985	1986	1987	1988	1989	1990
	(In millions of U.S. dollars)						
Current account	-248	-300	-311	-324	-217	-140	-47
Trade account	1,056	931	948	959	990	1,032	1,069
Exports, f.o.b	(2,624)	(2,581)	(2,719)	(2,874)	(3,066)	(3,288)	(3,525)
Petroleum	/1,835/	/1,764/	/1,853/	/1,947/	/2,065/	/2,202/	/2,347/
Other	/789/	/817/	/866/	/927/	/1,001/	/1,086/	/1,178/
Imports	(-1,567)	(-1,650)	(-1,771)	(-1,914)	(-2,076)	(-2,256)	(-2,456)
Service account	-1,324	-1,251	-1,284	-1,313	-1,242	-1,212	-1,161
Service credits	(350)	(410)	(482)	(556)	(639)	(731)	(833)
Service debits	(-1,674)	(-1,661)	(-1,766)	(-1,869)	(-1,881)	(-1,943)	(-1,994)
Interest payments 1/	/-850/	/-801/	/-839/	/-873/	/-811/	/-794/	/-761/
Other service debits	/-824/	/-860/	/-927/	/-996/	/-1,069/	/-1,198/	/-1,233/
Transfers	20	20	25	30	35	40	45
Capital account	308	300	335	284	214	102	-200
Direct investments	50	75	100	120	140	160	180
Medium- and long-term debt	210	149	235	164	74	-58	-380
Drawings 2/	(403)	(415)	(548)	(570)	(548)	(534)	(544)
Amortization 3/	(-211)	(-266)	(-313)	(-406)	(-474)	(-592)	(-925)
Interest rescheduled	(18)	(--)	(--)	(--)	(--)	(--)	(--)
Other	48	76	--	--	--	--	--
Overall balance	60	--	24	-40	-3	-38	-247
Net international reserves (increase -)	-20	60	-37	-28	-32	-37	-63
Arrears (decrease -)	-40	-60	--	--	--	--	--
Financing gap	--	--	13	68	35	75	310
Memorandum item							
Current account in percent of GDP	-2.5	-2.7	-2.6	-2.5	-1.6	-0.9	-0.3
Net international reserves (in months of imports)	0.8	0.8	1.0	1.1	1.2	1.3	1.5

Sources: Central Bank of Ecuador; and Fund staff estimates.

1/ Includes IMF changes.
2/ Starting 1986 it includes disbursements from nonbank sources only.
3/ Net of amounts rescheduled.

Gross capital inflows have been revised upward compared with the projections in EBS/85/25, mainly to reflect disbursements on new project-related loans signed since October 1984. Net capital inflows are expected to decrease over the period 1986-89, as amortization payments increase under the multiyear rescheduling arrangement with foreign commercial banks, and to become negative in 1990, the first year not covered by the rescheduling agreement with banks. Under these assumptions, the balance of payments is expected to record a deficit of less than US$20 million on average a year during 1986-89. If the authorities' desire to increase net international reserves to 1.5 months of imports by 1990 is taken into account, this would open a financing gap of about US$50 million on average in each of these four years, which the authorities consider manageable. As earlier indicated, in 1990 the gap would widen to slightly over US$300 million as the period of debt relief would be completed.

On the basis of the above assumptions, the external debt would decline from more than 70 percent of GDP in 1984 to 47 percent in 1990. The debt service ratio is projected to remain around 38 percent of exports during 1986-89, but would have averaged about 60 percent in the absence of the multiyear debt restructuring arrangements concluded in 1985. For the reasons noted above, the debt service ratio is expected to rise to 40 percent in 1990 (Table 9).

The above scenario indicates that Ecuador's external position is sustainable over the medium term if adequate policies are followed. However, as noted in EBS/85/25, Ecuador remains particularly sensitive to developments in the world oil markets. For instance, if petroleum prices were to remain constant at their present level throughout the period, a financing gap equivalent to 1.1 percent of GDP would appear in 1987-88, and would rise to 2 percent in 1989 and 3.8 percent in 1990.

VI. Staff Appraisal

The domestic and external imbalances that developed in Ecuador during the early 1980s have been substantially reduced during the last two years. In 1985 Ecuador's public sector is expected to register a surplus and the overall balance of payments is projected to be in equilibrium. The Ecuadoran Government took a series of adjustment measures in 1982, and in mid-1983 a comprehensive stabilization program was adopted and supported by the Fund with a one-year stand-by arrangement. After the expiration of the arrangement, a brief return to expansionary policies threatened to put renewed pressure on prices and the balance of payments, but the new Administration, which took office in August 1984, moved quickly to arrest the impending deterioration and developed the stabilization program for 1985 which is supported by the current one-year stand-by arrangement.

Table 9. Ecuador: Medium-Term External Debt 1/

(In millions of U.S. dollars)

	1982	1983	1984	1985	1986	1987	1988	1989	1990
Debt outstanding 2/	6,186	6,899	7,180	7,672	7,950	8,045	7,993	7,880	7,460
Of which: IMF	--	209	231	313	328	238	112	57	17
Debt service	2,652	2,997	2,249	2,207	2,114	2,293	2,151	2,148	1,726
Principal paid	1,330	238	211	267	317	496	600	647	964
Of which: banks	(1,066)	(126)	(87)	(85)	(35)	(101)	(209)	(304)	(609)
IMF	(--)	(--)	(--)	(--)	(5)	(90)	(126)	(55)	(40)
Principal renegotiated	555	2,042	1,188	1,139	958	913	740	707	--
Of which: banks	(555)	(1,826)	(1,089)	(979)	(883)	(864)	(740)	(707)	(--)
Interest paid	767	665	832	801	839	873	811	794	761
Of which: banks	(646)	(582)	(724)	(599)	(588)	(602)	(534)	(506)	(458)
IMF	(--)	(3)	(13)	(25)	(30)	(28)	(19)	(11)	(7)
Interest renegotiated	--	49	18	--	--	--	--	--	--
Of which: banks	(--)	(2)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Arrears	--	--	--	--	--	--	--	--	--
Principal	(--)	(--)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Interest	(--)	(--)	(--)	(--)	(--)	(--)	(--)	(--)	(--)
Memorandum items									
Debt/GDP 4/									
Including IMF	60	74	72	68	66	62	58	57	47
Excluding IMF	60	72	70	66	63	60	57	52	46
Debt service/exports of goods and services									
Before relief	97	114	75	74	66	67	58	53	40
After relief	77	35	36	36	36	40	38	36	40
Interest payments/exports of goods and services									
Before relief	28	27	29	27	26	25	22	20	17
After relief	28	25	28	27	26	25	22	20	17

Sources: Central Bank of Ecuador; and Fund staff estimates.

1/ Consistent with the medium-term balance of payments projection.
2/ Registered public and private debt of all maturities, including short-term debt converted into medium-term debt.
3/ Including $200 million bank loan to refinance payments due to banks in 1984 and which had been deferred.
4/ GDP in sucres through 1984 was converted into U.S. dollars using the exchange rates implied by the 1971 purchasing power parity. Thereafter, GDP in U.S. dollars is assumed to grow at 7.4 percent per annum in nominal terms.

The staff welcomes the improvement in public finances which has taken place in recent years, reflecting both the implementation of expenditure restraint and an increased revenue effort. With regard to the fiscal program for 1985, the staff notes that petroleum revenue is likely to fall substantially short of the earlier estimate, and that the overall public sector surplus will be smaller than originally projected despite a significant reduction in investment spending from the level envisaged under the program. However, the authorities expect to achieve the planned net buildup of deposits by the public sector in the Central Bank, owing to a greater net utilization of long-term external credits for development projects. To ensure that the net improvement in the public sector's creditor position vis-a-vis the Central Bank is indeed achieved, the authorities will need to maintain strict control over public spending and to monitor closely revenue developments so that adjustments can be made in a timely fashion should there be indications that the revised projection is not being met.

Although Ecuador is making progress in improving the assessment of foreign trade taxes through better valuation procedures, the responsiveness of nonpetroleum revenue in general remains less than satisfactory. Such revenue has declined in relation to GDP for a number of years, and is expected to increase in 1985 to a large extent because of the depreciation of the sucre. The staff urges the authorities to address this problem as a matter of priority to provide a buffer against adverse movements in revenue from the petroleum sector. The staff acknowledges the progress which has been made in reducing revenue earmarking by ensuring that the increase in oil revenue resulting from the shift of oil exports to the intervention market goes fully to the budget. Nonetheless, the staff would like to encourage further progress in this area and would urge the authorities to overcome any constraints which stand in the way of completely dismantling the system of revenue earmarking.

In the area of monetary policy, the staff would note that the growth of domestic financial savings since September 1984 has been stronger than had been projected. This has reflected mainly the favorable response by the private sector to the exchange rate actions taken since that time, the increase in controlled interest rates toward the end of 1984, and the introduction of certificates of deposit at market-determined rates of interest earlier this year. Meanwhile, controlled interest rates have remained negative in real terms since the inflation rate has not come down as had been expected. The staff would urge the authorities to continue to adjust controlled interest rates to bring them to levels that are positive in real terms, and to further increase interest rate flexibility by lowering the minimum denomination on the new certificates of deposit.

Regarding wage policy, the staff is concerned about the size of the increase in minimum wages granted in March 1985, which exceeded the increase envisaged under the program. While the staff recognizes that the impact of the salary increase on public sector outlays will be similar to what had been originally envisaged, the effect on wage formation undoubtedly has been negative. The staff is concerned that the 1985 salary decisions will make it more difficult to achieve the sought reduction of inflation. The staff would urge the authorities to strengthen their efforts to ensure that wage decisions are consistent with the deceleration of inflation being sought.

The staff welcomes the actions taken by the authorities to shift foreign exchange transactions from the official to the intervention market. While unification of the official and intervention markets has been delayed, the staff notes the intention of the authorities to unify the exchange system in the near future and to exercise exchange flexibility in the unified market. Through the pursuit of a flexible exchange rate policy the authorities intend to assure that external competitiveness is maintained and also ensure that the balance of payments objectives of the program will be achieved. Pursuit of this policy would facilitate the implementation of the planned reduction and simplification of import tariffs, which can be expected to contribute to the improvement of resource allocation in Ecuador and to the growth of exports. The staff also would encourage the authorities to adopt the proposed revisions of the foreign investment regulations designed to attract direct foreign investment to Ecuador.

The conclusion this year of multiyear agreements for the restructuring of Ecuador's commercial and official external debt will significantly reduce the country's debt service burden and should facilitate economic growth. Nevertheless, the staff would caution that a lasting solution to Ecuador's debt management problems requires continued restraint in the public sector's net use of external credit and, more generally, the maintenance of sound financial and exchange rate policies.

Ecuador maintains restrictions on the making of payments and transfers for current international transactions and a multiple currency practice which are subject to Fund approval. The exchange restrictions are in the form of a restriction giving rise to external payments arrears, a minimum financing or barter requirement, and bilateral payments agreements with a Fund member. The multiple currency practice arises from the multiple exchange rate system in effect in Ecuador. Ecuador recently eliminated a multiple currency practice arising from an advance deposit requirement for imports and cancelled a bilateral payments agreement with a Fund member. The approval of these restrictions and multiple currency practices was extended by the Executive Board until September 30, 1985 or the completion of the 1985 Article IV consultation with Ecuador, whichever is earlier (EBD/202/85). Pending the expected actions noted above for unification of the exchange market, the staff is not recommending further approval beyond the applicable date for the exchange restrictions and multiple currency practices maintained by Ecuador.

Finally, it is recommended that the next Article IV consultation with Ecuador be held on the standard 12-month cycle.

Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to Ecuador's exchange measures subject to Article VIII, Sections 2 and 3, in light of the 1985 Article IV consultation with Ecuador conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Ecuador maintains restrictions on the making of payments and transfers for current international transactions in the form of a minimum financing or barter requirement for imports, of an exchange restriction giving rise to external payments arrears and of a bilateral payments agreement with a Fund member. Ecuador also maintains a multiple currency practice arising from a multiple rate system. The Fund welcomes the recent elimination of the multiple currency practice arising from the advance import deposit scheme and the termination of a bilateral payments agreement with a Fund member. The Fund encourages Ecuador to eliminate the remaining multiple currency practice and exchange restrictions as soon as possible.

Fund Relations with Ecuador
(As of June 30, 1985, unless otherwise indicated)

I. Membership Status

(a) Date of membership: December 27, 1945
(b) Status: Article VIII

A. Financial Relations

II. General Department

(a) Quota: SDR 150.7 million

(b) Total Fund holdings of sucres: SDR 414.7 million or 275.2 percent of quota

(c) Fund credit:
Of which:

	Amount	Percent of Quota
Fund credit	264.0	175.2
Credit tranches	(92.3)	(61.2)
Compensatory financing	(85.4)	(56.7)
Enlarged access	(86.3)	(57.3)

III. Arrangements and Special Facilities

(a) Current stand-by arrangement:

(i) Duration: From March 11, 1985 to March 10, 1986
(ii) Amount: SDR 105.5 million
(iii) Utilization: SDR 21.1 million

(b) Arrangements during the last ten years:

(i) Duration: From July 25, 1983 to July 24, 1984

(ii) Amount: SDR 157.5 million

(iii) Utilization: SDR 157.5 million

(b) Compensatory financing facility:

(i) Date of approval: October 26, 1983
(ii) Amount: SDR 85.4 million

IV. SDR Department

(a) Net cumulative allocation: SDR 32.93 million

(b) Holdings: SDR 0.6 million or 1.7 percent of net cumulative allocations

B. Nonfinancial Relations

V. Exchange Rate: Ecuador has two exchange markets operated by the Central Bank. An official market where prior to September 4, 1984 the exchange rate was adjusted periodically. Since that date the buying rate has been set at S/. 66.50 per U.S. dollar and the selling rate at S/. 67.85 per U.S. dollar. The Central Bank also operates an intervention market where prior to September 4, 1984 the value of the sucre was allowed to fluctuate. Since that date the buying rate has been fixed at S/. 95.00 per U.S. dollar and the selling rate at S/. 96.50 per U.S. dollar. In addition there is a legal parallel market in which quotations fluctuate daily. On June 30, 1985, the buying rate in this market was S/. 110 per U.S. dollar.

VI. Last Article IV Consultation: The 1983 Article IV consultation and a review with the Fund under the stand-by arrangement were completed by the Executive Board on June 20, 1984 (EBS/84/92 and SM/84/106). The following decision was adopted:

"1. The Fund takes this decision relating to Ecuador's exchange measures subject to Article VIII, Sections 2 and 3, in the light of the 1983 Article IV consultation with Ecuador conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Ecuador maintains restrictions on the making of payments and transfers for current international transactions in the form of bilateral payments agreements, minimum financing or barter requirements for imports, and as evidenced by external payments arrears, as well as a multiple currency practice, as described in EBS/84/92. The Fund encourages Ecuador to continue the simplification of its exchange system by an early unification of the exchange rate and removal of the restrictions on payments and transfers for current international transactions. In the meantime, the Fund approves the multiple currency practice, including reclassification of transactions from the official to the free market, as they may occur, and the exchange restrictions in the form of minimum financing or barter requirements for imports and as evidenced by external payments arrears, through the end of the stand-by arrangement."

VII. Statistical Data: The currentness and coverage of Ecuador's statistical data in the IFS is considered reasonably adequate at this time, although the currentness of the government finance data could be improved.

VIII. Technical Assistance: a) from February 1981 to July 1984, the Fund provided technical assistance to Ecuador in the area of government accounting and financial reporting. The objective was to assist in the introduction of an accounting system prepared with Fund advice, and to provide on-the-job training for officials in the office of the Comptroller General and in other government agencies; b) during 1983 and the first half of 1984, the Fund--through its Central Banking Department--provided technical assistance in the form of an advisor to the Central Bank of Ecuador.

Ecuador: Selected Economic and Financial Indicators

	1980	1981	1982	1983	Prel. 1984	Prog. 1985	Proj. 1985
(Annual percent changes, unless otherwise specified)							
National income and prices							
GDP at constant prices	4.9	3.9	1.2	-3.1	4.1	2.5	2.5
GDP deflator	19.5	14.3	17.8	37.9	35.7	22.0	25.5
Consumer prices (average)	12.8	14.7	16.3	48.4	33.0	24.0	27.4
Consumer prices (end of period)	13.7	17.3	24.4	52.5	25.1	20.0	22.4
External sector (on the basis of U.S. dollars)							
Exports, f.o.b.	18.3	--	-7.9	0.9	10.9	8.9	-1.6
Petroleum exports	34.7	8.8	-11.7	14.8	4.9	6.1	-3.9
Imports, f.o.b.	6.9	5.3	-7.6	-35.4	11.3	10.8	5.3
Export volume	-1.2	-2.3	-2.3	11.2	0.5	9.9	5.2
Import volume	-8.2	-3.1	-17.7	-41.0	10.5	3.8	1.4
Terms of trade (deterioration -)	6.6	-5.8	-16.1	-17.2	9.6	-7.4	-9.8
Nominal effective exchange rate (depreciation -)1/	3.5	--	-9.4	-28.1	-24.8	...	...
Real effective exchange rate (depreciation -)1/	-0.4	4.9	-5.3	-3.5	-8.2	...	...
Central government budget							
Revenue	63.1	4.4	14.2	34.1	66.2	64.2	71.5
Total expenditure	69.2	34.6	14.9	15.1	42.6	32.3	35.9
Money and credit 3/4/							
Domestic credit	19.3	23.2	56.5	58.2	100.7 5/	30.0 5/	45.0
Public sector 4/	(-5.0)	(-11.4)	(7.9)	(-8.9)	(-3.7)	(-15.3)	(-14.3)
Private sector	(19.9)	(22.9)	(23.1)	(52.1)	(36.2)	(27.6)	(27.4)
Money and quasi-money (M2)	26.2	11.4	21.0	32.0	47.0	26.0	42.0
Velocity (GDP relative to M2)	5.5	5.8	5.8	5.8	5.6	5.9	5.0
Interest rate (savings deposits)	6.0	6.0	12.0	16.0	18.0	20.0	20.0
(In percent of GDP)							
Overall public sector balance	-4.7	-5.6	-6.7	-0.2	-0.4	3.4	2.2
Central government savings	0.4	-1.5	-1.2	-0.3	1.4	5.8	5.2
Central government deficit (-)	-1.9	-5.3	-4.9	-2.9	-0.9	2.9	2.7
Foreign financing	(0.6)	(2.2)	(2.4)	(-0.4)	(1.7)	(-0.6)	(0.4)
Domestic financing	(1.3)	(3.1)	(2.5)	(3.3)	(-0.8)	(-2.3)	(-3.1)
Gross domestic investment	26.1	23.2	25.2	19.0	20.5	16.5	23.0
Gross national savings	19.1	13.2	13.6	17.6	18.0	14.5	20.3
Current account deficit (-)6/	-7.0	-10.0	-11.6	-1.4	-2.5	-2.0	-2.7
External debt 6/7/	50.7	58.5	59.9	74.1	72.5	73.5	68.4
Of which: public sector	(38.5)	(44.0)	(44.2)	(66.0)	(68.7)	(73.5)	(65.2)
(In percent of exports of goods and services)							
Debt service							
Before rescheduling	47.3	71.3	97.0	113.8	75.4	70.1	73.7
After rescheduling	47.3	71.3	76.7	35.4	35.6	36.7	34.8
Interest payments							
Before rescheduling	17.2	20.8	28.1	26.6	28.6	25.9	26.8
After rescheduling	17.2	20.8	28.1	24.7	28.0	25.9	26.8
(In millions of U.S. dollars, unless otherwise specified)							
Change in net international reserves (increase -)	-226	294	671	-52	-60	-136	--
Net official international reserves (increase -)	(-226)	(294)	(460)	(58)	(-20)	(410)	(60)
Arrears (decrease -)	(--)	(--)	(211)	(-110)	(-40)9/	(-410)	(-60)
Financing gap	(--)	(--)	(--)	(--)	(--)	(-136)10/	(--)
Gross official reserves (months of imports of the following year)8/	6.0	4.3	3.9	6.0	5.6	...	...

1/ Until March 1983, the effective exchange rate is calculated as an average of the official and parallel market rates, weighted by the distribution of current transactions between the two markets. Thereafter, it is calculated as an average of the official, intervention, and parallel market rates, weighted by the distribution of current transactions between the three markets.

2/ Reflects in part a change in the distribution of petrol revenue in favor of the budget.

3/ In relation to liabilities to the private sector at the beginning of the period.

4/ Includes adjustment for gold revaluation in 1982.

5/ Includes credit to finance amortizations in sucres of private sector foreign debt assumed by the Central Bank. Excluding such credit, the increase in domestic credit becomes 46.9 percent in 1983, 80 percent in 1984, and 42.5 percent in 1985. The definition of domestic credit used in this table includes net domestic credit as defined in Table 5 plus the interbank float and central bank credit to the nonbank financial system.

6/ GDP in sucres was converted into U.S. dollars using the exchange rate implied by the 1971 purchasing power parity.

7/ Registered public and private debt of all maturities, including use of Fund resources.

8/ Gold valued at US$300 per troy ounce.

9/ Includes an estimated US$91 million of unpaid debt service to official bilateral creditors, to be rescheduled under the aegis of the Paris Club in 1985.

10/ Amount projected to be rescheduled under the aegis of the Paris Club in 1985.

Ecuador--Statistical Issues

1. Outstanding statistical issues

a. Government finance

Only annual data through 1982 are published in IFS. These data are as reported in the GFS Yearbook and relate to the budgetary Central Government.

The 1984 GFS Yearbook includes data on revenue, expenditure, and lending minus repayments for the budgetary Central Government. There is a need to expand the coverage of the data in the statistical and derivation tables by including data for all extrabudgetary units (autonomous entities) and the Ecuadoran Social Security Institute. It is also important to include in the Yearbook, data on financing and debt for the consolidated Central Government. Data for provincial and local governments extend only through 1980. It is also important to reduce the time lag in order to improve the presentation for Ecuador in the Yearbook.

b. External trade and prices

Foreign trade data on a customs basis are uncurrent and are updated with central bank payments' data for current periods. The valuation procedures for certain export commodities need to be reviewed and updated for publication in IFS. The authorities do not currently compile trade indices and the available basic trade statistics need to be examined with respect to their appropriateness for the compilation of trade indices. The weights of the wholesale price index are outdated (base 1974).

c. International banking

Ecuador reports the external accounts of its monetary authorities, private banks, and development banks in an aggregated form, but there is no breakdown between nonresident banks and nonresident nonbanks.

d. Technical assistance

A technical assistance mission in money and banking statistics visited Ecuador in early April 1985 and a report on the work of the mission was sent to the authorities in June 1985.

2. Coverage, currentness, and reporting of data in IFS

The table below shows the currentness and coverage of data published in the country page for Ecuador in the August 1985 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the Central Bank, which during the past year have been provided on a timely basis, although the currentness of the government finance data could be improved.

Status of IFS Data

		Latest Data in August 1985 IFS
Real Sector	- National Accounts	1983
	- Prices	May 1985
	- Production	April 1985
	- Employment	n.a.
	- Earnings	n.a.
Government Finance	- Deficit/Surplus	1982
	- Financing	1982
	- Debt	n.a.
Monetary Accounts	- Monetary Authorities	January 1985
	- Deposit Money Banks	December 1984
	- Other Financial Institutions	December 1984
External Sector	- Merchandise Trade: Value	March 1985
	Prices	December 1984
	- Balance of Payments	1983
	- International Reserves	June 1985
	- Exchange Rates	June 1985

AUGUST 2, 1985

MR. J. DE LAROSIERE

MANAGING DIRECTOR

INTERNATIONAL MONETARY FUND

WASHINGTON, D.C. 20431

WE WOULD LIKE TO CONFIRM THAT THE INDICATIVE LIMITS ON THE OUTSTANDING EXTERNAL DEBT OF THE PUBLIC SECTOR OR GUARANTEED BY THE PUBLIC SECTOR WITH ORIGINAL MATURITY OF UP TO AND INCUDING 12 YEARS AS SPECIFIED IN TABLE 4 OF THE MEMORANDUM ANNEXED TO OUR LETTER OF INTENT OF JANUARY 9, 1985 ARE APPROPRIATE AS PERFORMANCE CRITERIA FOR THE PERIOD JANUARY 1-FEBRUARY 28, 1986.

REGARDS,

FRANCISCO SWETT
MINISTER OF FINANCE
AND PUBLIC CREDIT

CARLOS JULIO EMANUEL
GENERAL MANAGER
CENTRAL BANK OF ECUADOR

Table 10. Ecuador: Sectoral Origin of GDP

(In millions of sucres at 1975 prices)

	1980	1981	1982	1983	Prel. 1984	Proj. 1985
GDP at market prices	147,622	153,443	155,265	150,529	156,630	160,521
Agriculture and livestock	21,198	22,647	23,101	19,721	21,048	21,400
Petroleum and mining	15,070	15,992	15,527	19,711	22,063	22,857
Manufacturing	26,807	29,159	29,584	29,541	28,909	29,508
Construction	6,906	7,239	7,285	6,638	6,469	6,715
Commerce	24,789	25,032	25,562	22,468	23,743	24,337
Transport and communications	10,038	10,517	10,687	10,539	10,852	11,199
Electricity, gas, and water	1,115	1,117	1,241	1,443	1,729	1,821
Real estate	6,530	6,722	6,965	7,150	7,359	7,570
Public administration	13,709	14,000	14,224	14,423	14,610	14,902
Other	21,460	21,018	21,089	18,895	19,848	20,212

Sources: Central Bank of Ecuador; and Fund staff estimates.

Table 11. Ecuador: Central Government Operations 1/

	1980	1981	1982	1983	1984	1985 Proj. Prog.	1985 Proj. Rev.
	(In millions of sucres)						
Total revenue	41,113	42,714	48,864	67,104	108,853	174,546	180,160
Petroleum revenue	14,324	15,430	21,477	30,292	49,262	101,033	101,995
Nonpetroleum revenue	26,789	27,284	27,387	36,812	59,591	73,513	78,165
Tax revenue	24,513	25,782	25,865	34,918	54,104	70,989	72,027
Taxes on income and profits	(4,411)	(6,417)	(6,277)	(7,515)	(10,252)	(12,667)	(13,860)
Property taxes	(229)	(326)	(355)	(377)	(156)	(170)	(250)
Taxes on goods and services	(8,282)	(8,502)	(9,954)	(13,653)	(21,025)	(23,813)	(27,370)
General sales tax	/4,432/	/5,319/	/6,304/	/7,381/	/11,361/	/12,680/	/14,000/
Selective excise taxes	/3,850/	/3,183/	/3,650/	/6,272/	/9,664/	/11,133/	/13,370/
Taxes on international trade	(11,195)	(10,920)	(10,044)	(13,031)	(20,797)	(31,850)	(28,377)
Import duties	/10,122/	/10,340/	/10,044/	/12,143/	/19,151/	/29,774/	/26,298/
Export duties	/1,014/	/555/	/18/	/54/	/61/	/128/	/159/
Exchange profits tax	/59/	/25/	/194/	/834/	/1,585/	/1,948/	/1,920/
Other taxes	(1,469)	(938)	(995)	(1,056)	(1,928)	(2,489)	(2,250)
CATs and IERAC (-)	(-1,073)	(-1,321)	(-1,972)	(-714)	(-54)	(--)	(-80)
Nontax revenue	1,423	1,152	1,522	1,369	2,809	1,500	1,200
Transfers	853	350	--	525	2,678	1,024	2,538
Total expenditure	46,600	60,681	69,070	83,752	114,157	147,370	153,248
Current expenditure	39,774	47,680	53,904	69,343	95,957	120,787	128,248
Wages and salaries	10,639	12,621	13,567	16,550	19,652	24,348	24,348
Purchases of goods and services	1,112	1,650	1,840	2,780	3,604	4,890	4,411
Interest payments	3,913	4,979	8,814	14,426	18,790	36,087	33,900
Current transfers	19,213	20,916	23,479	28,922	40,654	43,870	48,260
Other current expenditures	4,897	7,514	6,204	6,665	13,257	11,592	16,969
Capital expenditure	6,826	13,001	15,166	14,409	18,200	26,583	25,000
Fixed capital formation	3,786	6,452	8,537	7,224	11,937	15,785	16,095
Capital transfers	3,040	6,549	6,629	7,185	6,263	10,573	8,905
Other capital expenditures	--	--	--	--	--	225	--
Overall surplus or deficit (-)	-5,487	-17,967	-20,206	-16,648	-5,304	27,176	26,912
Financing	5,487	17,967	20,206	16,648	5,304	-27,176	-26,912
External financing (net)	1,553	7,658	10,006	-2,266	11,704	-5,329	4,888
Disbursement	(3,083)	(9,579)	(15,332)	(--)	(...)	(--)	(...)
Amortization	(1,530)	(1,921)	(5,326)	(2,266)	(...)	(5,329)	(...)
Domestic financing (net)	3,934	10,309	10,200	18,914	-6,400	-21,847	-31,800
Central Bank	(2,096)	(3,705)	(5,560)	(14,387)	(-6,400)	(-22,907)	(-31,800)
Bonds	(1,838)	(6,604)	(4,640)	(4,527)	(--)	(1,060)	(--)

Table 11. Ecuador: Central Government Operations 1/ (Concluded)

	1980	1981	1982	1983	1984	1985 Proj. Prog.	1985 Proj. Rev.
	(In percent of GDP)						
Total revenue	14.0	12.2	11.7	12.2	13.7	18.7	17.9
Petroleum revenue	4.9	4.4	5.2	5.5	6.3	10.9	10.1
Nonpetroleum revenue	9.1	7.8	6.5	6.7	7.4	7.8	7.8
Tax revenue	8.3	7.4	6.1	6.4	6.7	7.5	7.1
Taxes on income and profits	(1.5)	(1.8)	(1.5)	(1.4)	(1.3)	(1.4)	(1.4)
Property taxes	(0.1)	(0.1)	(0.1)	(0.1)	(--)	(--)	(--)
Taxes on goods and services	(2.8)	(2.4)	(2.4)	(2.4)	(2.6)	(2.6)	(2.7)
General sales tax	/1.5/	/1.5/	/1.5/	/1.3/	/1.4/	/1.4/	/1.4/
Selective excise taxes	/1.3/	/0.9/	/0.9/	/1.1/	/1.2/	/1.2/	/1.3/
Taxes on international trade	(3.8)	(3.2)	(2.4)	(2.4)	(2.6)	(3.3)	(2.8)
Import duties	/3.5/	/3.0/	/2.4/	/2.2/	/2.4/	/3.1/	/2.6/
Export duties	/0.3/	/0.2/	/--/	/--/	/--/	/--/	/--/
Exchange profits tax	/--/	/--/	/--/	/0.2/	/0.2/	/0.2/	/0.2/
Other taxes	(0.5)	(0.3)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
CATs and IERAC (-)	(-0.4)	(-0.4)	(-0.5)	(-0.1)	(--)	(--)	(--)
Nontax revenue	0.5	0.3	0.4	0.2	0.4	0.2	0.4
Transfers	0.3	0.1	--	0.1	0.3	0.1	0.3
Total expenditure	15.9	17.5	16.6	15.1	14.6	15.8	15.2
Current expenditure	13.6	13.7	12.9	12.5	12.3	12.9	12.7
Wages and salaries	3.6	3.6	3.3	3.0	2.5	2.6	2.4
Purchases of goods and services	0.4	0.5	0.4	0.5	0.5	0.5	0.4
Interest payments	1.3	1.4	2.1	2.6	2.4	3.9	3.4
Current transfers	6.6	6.0	5.6	5.2	5.2	4.7	4.8
Other current expenditures	1.7	2.2	1.5	1.2	1.7	1.2	1.7
Capital expenditure	2.3	3.8	3.7	2.6	2.3	2.9	2.5
Fixed capital formation	1.3	1.9	2.1	1.3	1.5	1.7	1.6
Capital transfers	1.0	1.9	1.6	1.3	0.8	1.2	0.9
Other capital expenditures	--	--	--	--	--	--	--
Overall surplus or deficit (-)	-1.9	-5.3	-4.9	-2.9	-0.9	2.9	2.7
Financing	1.9	5.3	4.9	2.9	0.9	-2.9	-2.7
External financing (net)	0.6	2.2	2.4	-0.4	1.7	-0.6	0.4
Disbursement	(1.1)	(2.8)	(3.7)	(--)	(--)	(--)	(--)
Amortization	(0.5)	(0.6)	(1.3)	(0.4)	(--)	(0.6)	(--)
Domestic financing (net)	1.3	3.1	2.5	3.3	-0.8	-2.3	-3.1
Central Bank	(0.7)	(1.2)	(1.3)	(2.6)	(-0.8)	(-2.5)	(-3.1)
Bonds	(0.6)	(1.9)	(1.2)	(0.7)	(--)	(0.2)	(--)

Sources: Ministry of Finance; Central Bank of Ecuador; and Fund staff estimates.

1/ The Central Government includes the Budget and FONAPAR.

Table 12. Ecuador: Exports by Principal Products

(Value in millions of U.S. dollars; volume in thousands of metric tons; unit value in U.S. dollars per kilogram; unless otherwise indicated)

	1980	1981	1982	1983	1984	1985 Prog.	1985 Rev.
Total	2,544	2,544	2,343	2,365	2,623	2,713	2,581
Petroleum crude	1,394	1,560	1,388	1,644	1,679	1,766	1,625
Volume 1/	39.6	45.4	42.7	59.3	61.3	65.4	65.0
Unit value 2/	35.2	34.4	32.5	27.7	27.4	27.0	25.0
Petroleum derivatives	193	166	136	106	156	138	139
Volume 1/	8.0	5.8	5.3	4.1	6.2	6.0	5.6
Unit value 2/	24.1	28.7	25.7	25.9	25.1	23.0	24.8
Bananas	237	216	213	153	136	158	150
Volume	1,347	1,277	1,261	910	924	1,041	1,000
Unit value	0.176	0.169	0.169	0.168	0.147	0.152	0.150
Coffee	132	106	138	149	178	169	169
Volume	54.0	56.0	73.9	75.0	72.0	70.0	72.0
Unit value	2.45	1.89	1.87	1.98	2.47	2.41	2.35
Cocoa, unprocessed	31	44	63	8	96	61	94
Volume	14.0	27.0	43.0	6.0	47.0	33.2	47.0
Unit value	2.24	1.62	1.47	1.40	2.05	1.84	2.00
Cocoa, processed	180	106	56	26	50	58	44
Volume	61.0	48.0	48.0	27.0	28.0	30.8	28.0
Unit value	2.95	2.20	1.16	0.98	1.77	1.87	1.56
Fish products	130	182	211	207	231	244	255
Other	247	164	137	72	99	120	105

Sources: Central Bank of Ecuador; and Fund staff estimates.

1/ In millions of barrels.
2/ U.S. dollar per barrel.

Table 13. Ecuador: Financial Relations with the IBRD

(In millions of U.S. dollars)

	Commitments 1/	Disbursed: Total	Disbursed: In 1985 2/	Undrawn
A. IBRD Operations 3/				
Total	365.3	177.8	19.0	187.5
Agriculture	15.5	12.0	1.5	3.5
Technical assistance	11.0	10.5	0.1	0.5
Transportation	72.5	31.0	2.4	41.5
Rural development	86.0	12.7	3.0	73.3
Industry	60.6	51.0	7.4	9.6
Financial sector	60.0	55.5	2.0	4.5
Housing	35.7	4.0	2.6	31.7
Education	16.0	1.1	--	14.9
Public sector	8.0	--	--	8.0

B. IBRD disbursements

	1980	1981	1982	1983	1984	Jan.-June 1985
Net disbursements	25.8	37.5	24.2	29.3	49.5	5.6
Disbursements	34.0	54.1	41.2	47.2	66.7	19.0
Repayments	8.2	16.6	17.0	17.9	17.2	13.4

Source: IBRD.

1/ Active portfolio.
2/ Through June 30.
3/ As of June 30, 1985.