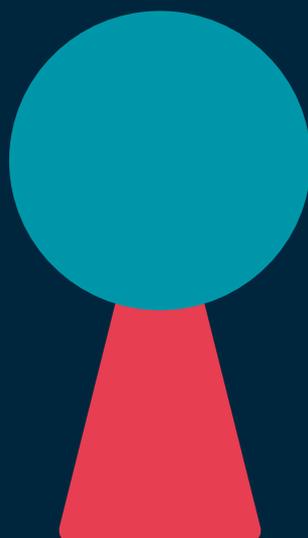


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ECUADOR FACES THE CHALLENGE OF ITS DEMOCRATIC OPENING

Quito, March 20, 2019

Today, Ecuador is undergoing an ongoing process to open its democracy. The historical economic and political frameworks for this shift date back to the beginning of the century, when the country reached a turning point in its economic and political fields. Following the financial crisis at the end of the 20th century, the Ecuadorian economy became dollarized in 2000. Regarding politics, change came after a crisis of representation and in political parties, first germinating when **Rafael Correa** was elected president in 2007, then beginning to blossom when current President **Lenin Moreno** began the process of opening up the country on several fronts.

ECUADOR SEARCHES FOR ITS FOOTING IN DEMOCRACY

In the first half of the 20th century, Ecuador had close to 25 presidents—probably the most volatile period it has experienced. Later, just as in most of Latin America, it had a military government in the 70s'. After its return to democracy (1979), several governments were able to reach the ends of their terms, though not without disturbance or threats of collapse. Then, due to the social turmoil between 1997 and 2007, Ecuador had eight presidents, a stark contrast to its one president from 2007 to 2017. This showcases the country's ongoing search for its footing in democracy, as well as the fact that political instability has always been present.

DEATH OF THE *SUCRE*, BIRTH OF THE DOLLAR AND ECONOMIC STABILITY

Improper management of its national currency led Ecuador to abandon the sucre at the beginning of the 21st century. Misuse of the exchange rate created fictitious competitiveness, and the *sucre's* value became precarious. This is why, even before fully incorporating the dollar, most transactions were already made with this currency; trust in the *sucre* was lost. In addition, devaluation favored exporters (who benefited from handling dollars). This gave rise to relationships—with results not always convenient for Ecuador—with those who made decisions regarding the exchange rate.

In January 2000, the Ecuadorian economy became dollarized and economic uncertainty began to subside, though it did not vanish completely. Inflation, which had risen past 100% at the end of the last century, began to decline, and real salaries improved as time went by. In the first five years of the 21st century, the Ecuadorian economy grew at a significant rate, poverty decreased and several regulations related to fiscal prudence were enacted.

These efforts rebuilt trust in the financial system, and both deposits and loans returned to a virtuous cycle of wealth creation. The country regained its economic equilibrium, but its political situation remained highly volatile.

POLITICAL PARTY CRISIS AND RAFAEL CORREA'S BREAK-IN

The political instability that permeated Ecuador from 1997 to 2006 gave rise to a new leader, one from outside the traditional system. Outsider Rafael Correa—who had only 3 % of voting intention in March 2006—wound up winning the elections on his promise to convene a Constituent Assembly and “re-found” the nation.

Correa, a nonconformist, took a socialist management style with the economy, treating the State as the protagonist and the private sector as a series of supporting actors. This is how, in 10 years under his government, the public economy went from representing 22% of GDP in 2007 to 44% in 2017.

This exponential growth is explained, among other reasons, by the Correa administration's oil prices and aggressive indebtedness, which included oil presales to China. It is also important to highlight how he abandoned the “macro-fiscal rules” and began regularly using contingency funds, which had existed at some point in the past.

On the political side, Correa set up a control system. New electoral rules made it virtually impossible for the opposition to occupy democratic space. The new “power of Citizenship Participation” coopted their participation and guided the process toward

appointing authorities who supported the current government. Court rulings were guided, and freedom of speech was affected by both sanctions to mass media and new regulations that resulted in self-censorship.

OPPORTUNITIES AND CHALLENGES SURROUNDING A DEMOCRATIC OPENING DURING AN ECONOMIC CRISIS

Lenin Moreno's presidency was based on the fact that he belonged to the *Alianza PAIS* movement (through which he was elected) and his relationship with former President Correa (for whom he was vice president). Moreno's change of direction away from Correa was probably a consequence of the adverse economic situation and rise in corruption cases.

At the beginning of Moreno's administration, the close circle was occupied by people who were closer to Correa than to him. At the end of the first year, however, he removed the most relevant ones, and in his second year, his cabinet was made up of the "revolutionaries" they had never imagined.

“Moreno's change of direction away from Correa was probably a consequence of the adverse economic situation and rise in corruption cases”

There is still some uncertainty, but there are at least three signs of a democratic opening in Moreno's administration:

1. Economic opening. Ecuador has stopped supporting the Bolivarian Alliance for the Peoples of Our America (ALBA) and is now trying to join the [Pacific Alliance](#) and sign a trade agreement with the United States.

Ecuador also started a grant rationalization process, the Ministry of Finance is led by a highly respected business leader and the country has come to an agreement with some major multilateral banks.

2. Separation of powers. This element of democracy is not easy to achieve in the short-term, but there are signs of improvement; Moreno appointed a Constitutional Court with honest and highly respected judges.

3. Freedom of speech. Journalists work with less fear under Moreno than they did with Correa, and the current president has reformed the Communications Law with important improvements in this area. Furthermore, he signed the Chapultepec Declaration supporting freedom of speech earlier this year.

These positive changes also mean new challenges on the horizon, which might affect the final outcome. There are three main issues:

1. Governability. The biggest challenge faced by nations working toward their democratic opening is permanence in office and progress within a framework of governability. Without a strong majority in the National Assembly, a difficult-to-control legislative process presents complications for the system. Such an opening, without the proper political control, could lead to instability, as there are many actors seeking leadership roles who could begin competing for interests, which are often exclusive.

2. Institutionalism. It is very important for democratic processes to show progress and not run into the roadblocks of selfishness or current political interests. Among other benefits, institutionalization processes could benefit the fight against corruption.

3. Real economy. As long as political and social progress does not impact the real economy, the democratic opening Moreno is pursuing will likely be compromised. In Ecuador, 60% of working-age people do not have a formal job or live on informal employment. As long as formal employment does not increase,



opportunities do not multiply and progress toward reducing poverty remains minimal, the democratic opening processes will likely be affected.

2019 OUTLOOK

Regarding the economy, the Ecuadoran government reached an agreement with multilateral banks for US\$10.279 billion for the next three years, of which US\$4.2 billion is from the International Monetary Fund (IMF). The first disbursement, in March 2019, amounted to US\$650 million. This is a “breath of fresh air,” as far as resources are concerned. It is also a positive sign when considered alongside Moreno’s intended reforms, which intend to restore macroeconomic balance, among other goals.

The IMF has said it will look for a “rebalanced payroll; gradual and careful fuel grant optimization; reprioritization in capital expenditures, as well as goods and services; and fiscal reform.” In addition to this, the Minister of Finance has announced a broad tax reform. The commitments made in the Letter of Intent remain to be seen once it is unveiled.

It is highly probable that the disbursements agreed for 2019 will cover the looming financing gap.

There are three key elements that will influence this year’s economic dynamics: in 2020, a US\$1.5 billion bond will mature, implying either payment or renegotiation; disbursements from multilaterals will, in some cases, require austerity measures that could mean layoffs in the public sector; and the lack of a majority in the Legislative area could make it challenging to implement a plan to support these disbursements.

IN CONCLUSION

Ecuador is at a crossroads in its political and economic history. In fact, President Moreno calls himself a “transitional” leader. There’s a lot at stake. If the economic reforms prevail and successfully bring about the fiscal responsibility, caution and a return to macroeconomic balance they imply, we could see real improvements in Ecuador’s quality of life.

Furthermore, as long as the country’s political conditions, institutions and governments view the components of liberal democracy as a guiding light, we can expect better days for Ecuador’s political system. Otherwise, in a time of economic crisis, it would not be surprising if radicalism and populism were to find a new window to barge through.

AUTHOR



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