ECUADOR

Table 1	2021
Population, million	17.9
GDP, current US$ billion	106.2
GDP per capita, current US$	5934.9
International poverty rate ($2.15)[a]	6.5
Lower middle-income poverty rate ($3.65)[a]	14.4
Upper middle-income poverty rate ($6.85)[a]	34.6
Gini index[a]	47.3
School enrollment, primary (% gross)[b]	99.0
Life expectancy at birth, years[b]	77.2
Total GHG emissions (mtCO2e)	98.4

Source: WDI, Macro Poverty Outlook, and official data.
a/ Most recent value (2020), 2017 PPPs.
b/ Most recent WDI value (2020).

The windfall from oil revenues is reducing short-term pressures on fiscal accounts, but public sector efficiency is critical for fiscal sustainability. Despite this, the polarized political and social context continues to limit the room for policy maneuvers and may prevent Ecuador from achieving its growth potential. Growth-enhancing reforms would require consensus-building around critical measures and proposing options to mitigate their potential adverse side effects on poor and vulnerable people while building their resilience.

Key conditions and challenges

With a fully dollarized economy and limited buffers, Ecuador has only partly recovered from the pandemic-driven recession. To address the unsustainable imbalances generated in the commodity boom, the government is committed to cementing fiscal sustainability, propelling private investment, protecting the most vulnerable, and addressing climate change-related challenges.

In the last few years, the authorities reduced the fiscal deficit to cement confidence in dollarization. They also mobilized multilateral financing to prevent a disordered adjustment with devastating effects on poverty. They restructured debt with international bondholders in 2020 and implemented a successful vaccination in 2021. Yet, they have struggled to foster growth and employment post-pandemic. Moreover, as oil prices have increased, so have pressures to expand expenditure.

Despite higher oil prices, long-term fiscal sustainability requires rationalizing current expenditure. Public sector efficiency is critical for securing fiscal sustainability, building fiscal buffers, and ending fiscal procyclicality while supporting vulnerable people and improving access to quality services.

With a narrow policy margin to fuel domestic demand, Ecuador would benefit from fostering private investment and productivity by, for example, modernizing labor regulation, streamlining insolvency management, reducing market distortions, and fostering agriculture. Besides its job creation potential, more private investment may help Ecuador to exploit untapped mining resources in an environmentally and socially sustainable way, enhance non-conventional renewable energy supply, and improve infrastructure.

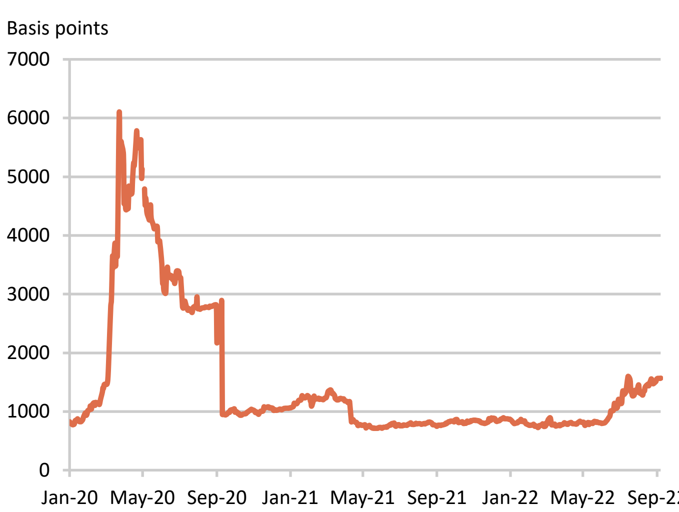
Addressing these challenges would require consensus around critical reforms in a fragmented National Assembly and a polarized society.

Recent developments

After the 2020 recession, GDP grew by 4.2 percent in 2021, thanks to a successful vaccination campaign, favorable external conditions, and expanding domestic credit. Poverty declined from 34.6 percent in 2020 to 31.7 percent in 2021, lifting almost half a million Ecuadorians above the $ 6.85-a-day 2017 PPP threshold. Vulnerable and middle-class populations also recovered, but the latter remained slightly below pre-pandemic levels.

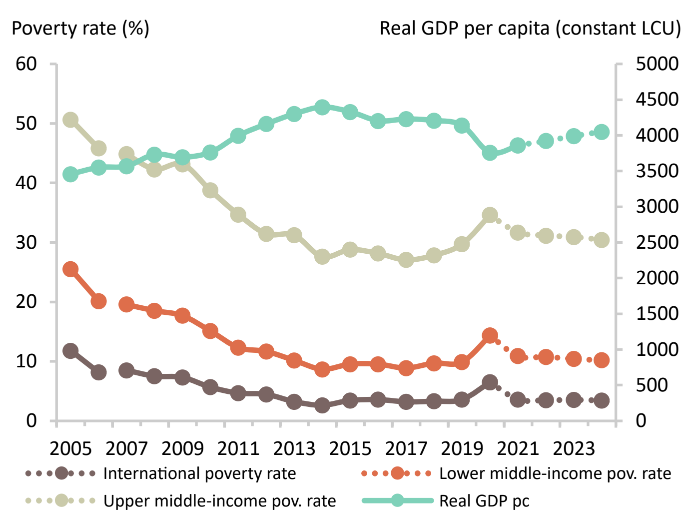
Growth eased to 3.8 percent y-o-y in the first quarter of 2022 due to slowing private consumption and surging imports. Recovery could further slow in the second quarter following an 18-day demonstration in June against high fuel prices, among other things. The social unrest paralyzed the country and increased EMBI from 800 basis points in early June to a peak of about 1,500 in early September.

FIGURE 1 **Ecuador** / Emerging Market Bond Index



Source: JP Morgan Chase.

FIGURE 2 **Ecuador** / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

While employment reached pre-pandemic levels in June 2022 (64 percent), underemployment (24 vs. 20 percent) and informality (69 vs. 61 percent) remained above. Moreover, labor income remains 10 percent below pre-pandemic, affecting vulnerable people the most.

The 12-month rolling fiscal deficit dropped from 1.7 percent of GDP in December 2021 to 0.2 percent in May 2022. Higher oil revenues, tax measures passed in late 2021, and low public investment more than offset the expansion of current expenditure resulting from increasing interest payments and fuel subsidies. After freezing gasoline and fuel prices in late 2021, the authorities reduced them by US$0.15 per gallon in June 2022 to end social unrest.

The Russia-Ukraine war hit banana exports, but the trade surplus remained stable as climbing imports offset higher oil prices and mining exports. Together with multilateral funding, this surplus increased international reserves. Moreover, as banks continued using their excess liquidity to foster domestic credit, dollar inflows kept the money supply growing.

Annual inflation rose from 1.9 percent in December 2021 to 3.8 percent in August 2022 due to food and transport prices. Slow growth, dollarization, and controlled fuel prices have kept inflation relatively low compared to the rest of the region. Even though poor households were only mildly affected mostly due to being net food producers, vulnerable and middle-class populations suffered the most.

Outlook

Despite high oil prices, growth is projected to slow to 2.8 percent in 2022 due to ongoing consolidation and the recent social unrest. Moreover, after a modest rebound in 2023, growth is expected to stabilize near 2.8 percent from 2024 onwards. Given the need to maintain prudent fiscal management, social and political polarization can jeopardize investor confidence and growth-enhancing reforms.

Despite higher fuel subsidies, the fiscal deficit is projected to turn into a surplus from 2022 onwards due to improved oil revenues. The 2021 tax reform will also increase revenues through a mix of measures, including permanent changes to personal income tax brackets and exemptions. Similarly, the government is expected to continue improving efficiency to reduce expenditure and enhance service provision. The public sector is expected to accumulate savings, while fiscal surpluses and growth are projected to reduce public debt from 62 percent of GDP in 2021 to 55 percent by 2024.

The current account balance will increase in 2022 due to high oil and other commodity prices. Surging imports, however, will gradually reduce this surplus over the projection period. Despite low foreign investment, current account surpluses and external financing will expand the money supply and international reserves.

Despite the inflation spike in 2022 due to the Russia-Ukraine conflict, poverty is expected to fall to 30 percent in 2024 as improving labor conditions move households from the bottom of the income distribution into the vulnerable and middle-class categories.

Poverty and inequality reduction hinge on sustained GDP growth, which is exposed to various risks. In addition to its vulnerability to international oil price fluctuation and tightening financial conditions, Ecuador's prospects are exposed to natural disasters, like floods and earthquakes, new waves of social unrest, and political instability.

TABLE 2 Ecuador / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2019	2020	2021	2022e	2023f	2024f
Real GDP growth, at constant market prices	0.0	-7.8	4.2	2.8	3.0	2.8
Private Consumption	0.3	-8.2	10.2	2.9	3.4	2.8
Government Consumption	-2.0	-5.1	-1.7	2.2	-0.8	-0.3
Gross Fixed Capital Investment	-3.3	-19.0	4.3	1.5	5.1	5.0
Exports, Goods and Services	3.6	-5.4	-0.1	5.1	2.9	2.7
Imports, Goods and Services	0.3	-13.8	13.2	3.8	3.1	2.8
Real GDP growth, at constant factor prices	0.3	-7.4	3.8	2.7	3.0	2.7
Agriculture	1.6	0.4	3.4	2.1	2.1	2.1
Industry	0.2	-10.0	0.5	3.8	2.9	2.6
Services	0.1	-7.2	5.8	2.2	3.3	2.9
Inflation (Consumer Price Index)	0.3	-0.3	0.1	3.3	2.2	1.7
Current Account Balance (% of GDP)	-0.1	2.7	2.8	2.7	2.5	2.0
Net Foreign Direct Investment Inflow (% of GDP)	0.9	1.1	0.6	1.3	1.4	1.4
Fiscal Balance (% of GDP)	-3.4	-7.1	-1.7	1.0	1.7	1.7
Debt (% of GDP)	51.4	60.9	62.2	60.8	57.3	55.0
Primary Balance (% of GDP)	-0.6	-4.2	-0.3	2.5	3.2	3.4
International poverty rate ($2.15 in 2017 PPP)[a,b]	3.6	6.5	3.6	3.5	3.5	3.4
Lower middle-income poverty rate ($3.65 in 2017 PPP)[a,b]	9.9	14.4	10.9	10.8	10.4	10.2
Upper middle-income poverty rate ($6.85 in 2017 PPP)[a,b]	29.7	34.6	31.7	31.2	30.9	30.4
GHG emissions growth (mtCO2e)	-0.1	-2.9	2.7	0.7	0.3	0.2
Energy related GHG emissions (% of total)	36.5	34.9	35.8	36.1	36.1	36.0

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.
Notes: e = estimate, f = forecast. Poverty lines are expressed in 2017 PPP, resulting in changes from earlier editions that used 2011 PPP. See pip.worldbank.org.
a/ Calculations based on SEDLAC harmonization, using 2020-ENEMDU. Actual data: 2020. Nowcast: 2021. Forecasts are from 2022 to 2024.
b/ Projections using microsimulation methodology.