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**FEATURED Q&A**

# Will Ecuador's New Austerity Measures Lead to Unrest?

Ecuadorean President Lenín Moreno is cutting gasoline subsidies and public workers' salaries in order to plug the country's budget deficit. // File Photo: Ecuadorean Government.

**Q: Ecuador's government on Dec. 18 announced that it would cut gasoline subsidies and public workers' salaries in an effort to reduce the country's fiscal deficit by $800 million. Are these decisions the right ones for President Lenín Moreno's government to be making at this time? How much opposition will his government face over the moves? How important is it for Moreno to plug the budget deficit, and how would the austerity measures affect Ecuador's economy and, potentially, political stability?**

**A: Nathalie Cely, president of the Centro de Competitividad in Quito and former Ecuadorean ambassador to the United States:** "President Moreno inherited an economy with an urgent financing mismatch (long-term investment financed through short-term debt), as well as a large fiscal deficit. Because of these, the Moreno administration has not found fiscal space to implement countercyclical policies. In this context, any reduction in public spending will be recessionary. However, cutting fuel subsidies is a move in the right direction in order to make the public finances sustainable in the long run—fuel subsidies are inefficient and create distortions in the economy. Unfortunately, the proposed cuts have not been made within the context of a national dialogue (in order to reduce opposition), and the compensatory measures for the transportation sector that are being discussed could create black markets and other distortions in the economy. As the new year begins and vacations end, there will be increased political instability as different sectors and interest groups (transportation, taxis, private sector representatives) react to the proposed fuel

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The Central American country's government withdrew from the U.N.-backed International Commission Against Impunity in Guatemala, or CICIG. President Jimmy Morales has been a target of the commission and said it has overstepped its authority.

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Morales // Photo: Guatemalan Government.

POLITICAL NEWS

## Guatemala Pulls Plug on CICIG, Orders Officials to Leave

Guatemala's government on Monday withdrew from the United Nations-backed International Commission Against Impunity in Guatemala, or CICIG, and ordered the anti-graft body's officials to leave the country within 24 hours, Prensa Libre reported. The move was the latest in a battle between CICIG and President Jimmy Morales, whose government CICIG said it was investigating in mid-2016 in connection with alleged violations of campaign finance laws, The Wall Street Journal reported. Morales, who denies wrongdoing, has accused the commission of overstepping its bounds.

**U.N. Secretary General António Guterres said he "strongly rejected" Guatemala's decision.**

CICIG's expulsion from Guatemala followed the government's announcement last August that it would not renew the body's mandate past its expiration in September 2019. On Monday, Morales' government accelerated CICIG's removal from the country, with Guatemalan Foreign Minister Sandra Jovel saying the commission's investigators and prosecutors must leave within 24 hours. Jovel announced the decision after meeting in New York with U.N. Secretary General António Guterres. In a statement, Guterres said he "strongly rejected" the decision, adding that he expected the Central American nation's government to meet its obligations until the expiration of CICIG's mandate in September and also protect the commission's staff. Last August, soon after announcing that he would not renew CICIG's mandate past September, Morales banned the agency's head, Iván Velásquez, from re-entering the country. In her statement on Monday, Jovel said Guterres' support for Velásquez contributed to the government's decision to oust the commission. "It is regrettable that the secretary general, in a bid to maintain one person in the position, sacrificed the legitimacy of the commission," Jovel told journalists after meeting with Guterres, Reuters reported. "Therefore we reported to the secretary general that within 24 hours the agreement [that was struck to create CICIG] will be terminated by the Guatemalan government." Jovel accused CICIG of overstepping its authority. Many politicians in Guatemala have also criticized the commission, saying it violates the country's national sovereignty. However, anti-corruption activists have said the commission has produced positive results in fighting corruption. [Editor's note: See **Q&A** about CICIG in the Sept. 20 issue of the Advisor.]

## Peru's Attorney General Tenders Resignation

Peruvian Attorney General Pedro Chávarry on Monday said he would resign this morning, following growing public outcry over his recent decisions in connection to the graft investigation involving Brazilian construction company Odebrecht, El Comercio reported. Chávarry said in a statement that he would present his resignation from the country's public ministry this morning out of "respect for my institution." His decision comes a little more than week after he dismissed two of the corruption case's lead prosecutors, a move he reversed after President Martín Vizcarra threatened to suspend him amid widespread criticism, Reuters reported. Chávarry has denied accusations that he was trying to meddle in the case. The two well-known prosecutors, Rafael Vela and José Domingo Pérez, are seen as key figures of the Odebrecht investigation. Last month, they reached a deal with the Brazilian firm to provide evidence on roughly $30 million in bribes it paid Peruvian politicians, which could lead to more charges against prominent figures includ-

NEWS BRIEFS

### Peru Bans Venezuela's Maduro, Cabinet From Entering Country

Peru has barred Venezuelan President Nicolás Maduro and his cabinet from entering the country, Foreign Minister Néstor Popolizo said Monday, Agence France-Presse reported. The move followed an announcement last week by 13 member countries of the so-called Lima Group that they would not recognize Maduro's new term, which officially begins Thursday. Popolizo said the ban also blocks bank transfers from people linked to the Maduro government, including family members.

### Head of Brazil's Environmental Protection Agency Resigns

The head of Ibama, Brazil's environmental protection agency, resigned Monday after new President Jair Bolsonaro criticized the agency over its budget, Reuters reported. Suely Araújo, who had led Ibama since 2016, stepped down after Bolsonaro tweeted suggestions that there were irregularities in the environmental agency's budget, which included $7.73 million to rent vehicles for use in tough terrains. Bolsonaro has frequently attacked the agency, which is tasked with fighting deforestation.

### Chile's Copper Production May Increase 30 Percent Over Next Decade

Chile's copper production could increase by almost 30 percent over the next 10 years, according to a report released Monday by Chilean state copper agency Cochilco, Reuters reported. The report says output from the South American country, which is already the world's top producer of copper, could reach a record of 7.25 million metric tons as early as 2025. Several new projects and expansions that are planned in the coming years would drive the rise in output.

ing former presidents suspected of accepting illicit payments. Odebrecht has acknowledged it had paid millions of dollars in bribes to officials in a dozen Latin American countries in exchange for public work contracts. [Editor's note: See related Q&A on corruption in Peru in the Dec.18 issue of the Advisor.]

**BUSINESS NEWS**

# PDVSA Signs Deal With U.S.-Based Energy Company

Venezuelan state oil company PDVSA has signed a deal with energy firm Erepla to help boost the South American country's crude oil production, the U.S.-based company said, Reuters reported Monday. Erepla said it will invest as much as $500 million to "revitalize oil production" at three Venezuelan oil fields, the Tía Juana Lago and Rosa Mediano fields in the western Lake Maracaibo region and in the Ayacucho 5 bloc in the Orinoco Belt, in return for a share of the oil produced. As part of the arrangement, Erepla said it would have "enhanced managerial participation" in PDVSA oil projects and be responsible for procurement, a key difference from previous joint ventures between the state company and oil majors, in which PDVSA has full operational control, the wire service reported. The agreement would still need to obtain an exemption from the Trump administrations' sanctions against Venezuela, which prohibit U.S. companies from providing financing to the Venezuelan government and state firms. Erepla is partly owned by Florida-based billionaire Harry Sargeant III, who has ties to the Republican Party. Erepla was only registered in November, according to Delaware state records, Reuters reported. The oil-rich South American country closed 2018 with the lowest record of crude exports in 28 years amid declining production, Bloomberg News reported last week. Venezuela exported 1.245 million barrels per day last year, the lowest since 1990.

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subsidy cuts. Furthermore, local elections are scheduled for March 24. This will surely increase political instability as candidates will make the proposed subsidy cuts an important campaign issue. Without doubt, it is important to reduce the fiscal deficit, as it is seen as a positive signal for foreign investment, and there is an urgent need for financial sustainability. However, the Moreno administration might be too optimistic in thinking that reducing the fiscal deficit and a more business-friendly rhetoric alone will result in the private sector becoming the engine of growth in the economy. Structural issues in productivity and competitiveness remain that will not be corrected by plugging the fiscal deficit. Because of this, there is a need for an integral economic plan that tackles the competitiveness and productive difficulties of the Ecuadorean economy, not just the fiscal aspects."

A **Francisco X. Swett, former Ecuadorean minister of finance, member of Congress and central bank president:** "In round numbers, and before any adjustments but after revenues from sales, the 'fuel subsidy' in Ecuador is worth $1.5 billion to $2 billion, depending on the price of crude. It is an expensive proposition that has consumed one third of all crude export income since 1974. It is also largely regressive, socially inefficient, a limiting factor in the development of Ecuador's oil sector, a source of rampant corruption and, in the current fiscal situation, an unviable proposition. To get around the issue, the previous government imposed, to no avail, all kinds of taxes and levies on automobile use because the largest subsidy component is for diesel feed in power generation, public and freight transportation, fisheries, industrial use and cross-border smuggling. The reduction of the subsidy (which to date has been directed against gasoline uses) represents about a tenth of financing needs. Therefore, its impact, while not marginal, will not cure the runaway fiscal problem, which remains unyielding. The gradual approach is no longer very effective, and the way the policy is being implemented (pre-announcing the adjustments, including of diesel) is politically inept, and it is widely associated with the need to enter into an IMF program (which will also require the VAT to be increased to 15 percent). Finally, it is not assured that Moreno will not backtrack as he begins to feel the heat of opposition from different sectors and despite the loss of political capital, which has already been squandered by hesitation and ineptitude."

> **"It is not assured that Moreno will not backtrack as he begins to feel the heat of opposition..."**
> **— Francisco X. Swett**

A **Ramiro Crespo, president of Analytica Securities in Quito:** "The Moreno administration has taken a slightly larger step toward correcting Ecuador's incredibly wasteful fuel subsidy regime. The move signals to investors and, potentially, the IMF that it is committed to tackling some issues that were anathema to previous governments, which feared that fuel-related rioting could lead to a collapse in government. This has not happened; the streets remain calm, which is encouraging, perhaps also because of the government's conciliatory approach to special interest groups, in particular public transit (which in Ecuador, like most of Latin America, is mostly private) and taxi cooperatives, which will be exempt from fuel hikes thanks to a new subsidy system. It remains to be seen how bravely the government can move along the reform path, as its need to negotiate with transportation interests

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underscored its weakness. It still leaves the potential of arbitrage of fuel prices with Colombia and Peru open to crafty fuel mobsters. Overall, it would have been better for Moreno and of course Ecuador to have taken these steps a year ago after winning the referendum, but at the time, his cabinet still had a strongly left-wing character. The latest measures only reduce spending by less than one percentage point of GDP. The cut in top civil servants' salaries is largely symbolic and, as in the case of fuels, we're only at the beginning of meaningful reform. The recent scandals about legislators extorting aides in a sort of public-hiring pyramid scheme only underscores this."

A **Walter Spurrier, president of Grupo Spurrier and director of Weekly Analysis in Guayaquil, Ecuador:** "These are the right moves. Moreno seems to have struck the right balance between the need to reduce the fiscal deficit and the social and political impact of measures. There have been no protests. The measures have a negative effect on the president's popularity, but so does economic stagnation. The two parties that aim to win the next presidential election, PSC and CREO, want Moreno to finish his term, and are presumably relieved that Moreno is tackling the fiscal problem; together with the president's Alianza PAIS, they have an ample assembly majority. The government's major concern is a Correa resurgence. However, there are several corruption cases now with the courts involving Correa and his retinue; in addition, there is an order for his arrest in the case of the botched kidnapping in Bogotá of an exiled opponent. From a fiscal standpoint, the measures are too mild. Ecuador needs to improve its fiscal accounts by some $5 billion. This could not be the full extent of adjustment in 2019. There must be a more decisive payroll reduction. The authorities have announced transferring the operation of government corporations to businesses (the Constitution restricts privatization) and expect to obtain a $4 billion payment for CNT, the state telecommunications company. A more intractable problem than the fiscal one is competitiveness. Without an export boost, or an influx of foreign investment, Ecuador's capability to import will be limited, and so will household consumption expansion. Until these two major issues are overcome, Ecuador is due for very sluggish economic growth."

> **"From a fiscal standpoint, the measures are too mild."**
>
> **— Walter Spurrier**

*The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at* **gkuleta@thedialogue.org**.



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