INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

A SUMMARY STATEMENT

OF

ECUADOR'S CREDITWORTHINESS

July 10, 1950

Economic Department
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ECUADOR

ESSENTIAL STATISTICS

Area: 150,000 square miles

Population: 3.5 million

Currency:
Unit: sucre (symbol: $)
Parity: 13.50 sucres = U.S. $1

Foreign Trade:
Imports (1949): $44.6 million
Exports (1949): $27.7 million

Estimated Official Exchange Transactions on account of:
Imports (1949): $43.9 million (c.i.f.)
Exports (1949): $32.8 million

National Income in 1948: Estimated roughly equivalent to U.S. $125-150 million (about U.S. $40 per capita)

Budget:
Deficits: 15.9 million (U.S. $1.2 million)
1949: 16 million (U.S. $1.2 million)
1950: (first quarter ordinary)

Internal Debt: 112 million (U.S. $8.3 million)

External Debt: 24.3 million
Principal in Default: 12.5 million
Other: 11.8 million

Wholesale Prices:
1939: 100
Average 1945: 266
December, 1949: 373

Net Exchange Reserves:
December 31, 1948: 25.6 million
December 31, 1949: 13.6 million

Undisbursed Ex-Im Bank Loans, December 31, 1949: 13.2 million
A SUMMARY STATEMENT OF ECUADOR'S CREDITWORTHINESS

CONCLUSIONS

Studies made in the Economic Department yield the following conclusions:

1. For the next five or six years, the Ecuadorian balance of payments is likely to exhibit considerable stringency. Foreign markets for rice, the most important export commodity, are becoming circumscribed and will probably continue to shrink.

2. The high propensity to import is aggravated by earthquake reconstruction needs of considerable magnitude. However, the low level of available foreign reserves precludes the financing of further trade deficits.

3. If, as now appears probable, sizeable reductions take place in foreign capital investments, as well as in non-monetary gold exports, the balance of payments will be placed under increased pressure.

4. Assuming settlement of Ecuador's defaulted debt along lines of the Chilean agreement, and interest and amortization on the recent Eximbank loan of $7 million, service requirements amount to about 6% of estimated exports in 1950. This is a moderate proportion, and should not constitute an especially burdensome charge on Ecuador's balance of payments.

5. After 1955, the balance of payments outlook appears more
promising. By then, the effects of current development programs should begin to be seen in increased exports and smaller imports. It is also to be expected that most of the extraordinary reconstruction needs will have been met.

6. Since internal economic conditions in Ecuador depend in large measure upon foreign trade, the deterioration of the balance of payments position is reflected in domestic finances. A growing conflict for priority between earthquake reconstruction and development is also adding to the difficulty. The Government budget, which showed substantial surpluses in the three years ending 1948, registered deficits in 1949 and in the first quarter of 1950. Bank credit to the private sector, stimulated by Central Bank operations, has been increasing steadily and prices have risen. Present prospects are that new money will be created in order to finance reconstruction.

7. Analysis of Ecuador's internal financial position confirms the conclusion reached after a study of the country's external financial position: Ecuador can ill-afford to increase its debt burden during the next five years. While this conclusion does not foreclose the possibility of a small loan, directly linked to improving the condition of the balance of payments, it does imply that interest payments on any new loan must be low and amortization payments must be deferred until Ecuador's development programs, most of which depend on foreign credits, have had an opportunity to improve domestic production for export and for replacement of imports.

8. Ecuador's present difficulties (the collapse of the rice export market and the Ambato earthquake) are largely due to uncontrollable factors, and there is little that can be done in the short
run to remedy the situation. Ecuador's position is difficult, but it is not without hope; careful formulation and effective execution of a practical development program, which would also limit reconstruction expenditures in favor of economic development, could greatly improve its creditworthiness. The program would probably call for technical assistance over a period of some years. With technical assistance, supplemented by financial aid for development which fits into the framework of a well conceived program promising continuous and effective effort toward completion, much could be done to improve Ecuador's long-term balance of payments position; without such a program, it is difficult to see how Ecuador can halt domestic inflation and improve its creditworthiness.

9. The Bank is not now in position to determine the essential characteristics of an investment program for Ecuador which would improve its creditworthiness. Information is lacking concerning the magnitudes which would be involved, the period over which assistance would be required, or even the extent to which the program would be aided by foreign financial credits. It is clear, however, that the Bank's attitude must be governed by the answers to such questions as these. It is not inconceivable that investigation might show that the needs are sufficiently moderate to justify a series of small loans, the combined effect of which would be to allow repayment and additional safe borrowing.

BALANCE OF PAYMENTS

10. Like other Latin American countries during the war, Ecuador was able to build up its gold and foreign exchange holdings substantially.
(from $4 million at the end of 1939 to $36 million at the end of 1944).

These reserves were still intact at the end of 1946 when relaxation of controls on an extensive list of import items led to a sharp rise of imports in 1947 over 1946 ($46 million as compared to $31 million).

Exports also increased (from $39 million to $45 million), but the rise was insufficient to compensate for the acceleration in imports which was largely responsible for raising the balance of payments deficit on current account from $1.4 million in 1946 to $11.3 million in 1947. The deficit was only slightly offset by capital inflow, and foreign reserves declined by about $10 million to $26.6 million. More effective import controls, achieved after consultation with the IMF, and continued expansion of exports, improved the situation in 1948, and the deficit on current account dropped to $5.8 million, being more than offset by capital transactions.

11. Continuation of controls in 1949 failed to reduce imports, which remained at $44 million as in the previous year. However, the deterioration of the 1949 balance of payments was due chiefly to a serious decline in the value of Ecuador's principal exports, rice and cacao, which reduced estimated receipts from exports to only $28.4 million. The 1949 current accounts deficit, estimated at $12.2 million, was met chiefly by the pledging of gold holdings for short-term loans from the Federal Reserve Bank of New York. As a consequence of the deficit, net international reserves declined by 47%, from $25.6 million at the end of 1948 to $13.6 million at the end of 1949. The decrease would have been greater had it not been for grants of $1.7 million from various countries to help cope with the effects of the devastating earthquake suffered in August 1949.
12. By December 31, 1949, net gold and foreign exchange holdings amounted to only 26% of the total money supply, compared with 53% one year before. Since under Ecuador's monetary law, corrective measures are obligatory when reserves fall below 40% of the circulating medium, the Government intervened. To meet the emergency, further restrictions on imports were imposed and the multiple exchange system was modified by increasing the sucre return to exporters in order to stimulate exports (particularly rice), and by raising the value of the dollar in relation to the sucre in order to curb imports.

13. The Ecuadorian exchange budget for 1950, formulated on the basis of these changes in the foreign trade regulations, forecasts a considerable improvement in this year's balance of payments on current account, which is expected to show a surplus of $2 million for the year, due mainly to the disposal in 1950 of part of last year's rice crop. Exports are budgeted at $38.9 million (an increase of $10.5 million over 1949) and imports at $37.2 million (down $7.1 million from last year), with miscellaneous revenues adding $0.3 million to the trade surplus of $1.7 million.

14. Even though the export price of rice is more likely to approximate 5 cents per pound instead of the 6.5 cent price included in the exchange budget, the budget appears to underestimate export receipts somewhat because coffee revenues were computed with an average price of only 31 cents per pound instead of the 38 cents which now seems likely. If adjustments are made on the basis of the lower rice and high coffee prices (using latest data on the size of these crops), it appears that receipts from exports may amount to $39.4 million instead of the $38.9 million officially estimated.
15. On the other hand, it seems doubtful whether the planned reduction of $7.1 million in imports from $44.3 million in 1949 to $37.2 million can be realized in view of the exceptional reconstruction needs generated by the Ambato earthquake. The cost of reconstructing the Ambato earthquake damage has been estimated at $80 million, of which $36 million will be needed to pay for imports. These figures may be somewhat excessive, but they give an order of magnitude of the financial problem with which Ecuador is faced. If the estimate is accurate and imports for reconstruction are divided equally for the next six years, imports in 1950 would total $43 million instead of $37 million. Against these expenditures would be applied the $2.6 million to be disbursed this year from the Eximbank loan and $39.4 million in exports, leaving a surplus of $1.0 million. It is clear, therefore, that while the import situation need not be as stringent as official estimates indicate, the Ecuadorian balance of payments will undoubtedly remain tight in 1950. Thus, for this year (until May 25, 1950), purchases of exchange have been $2.2 million higher than sales, largely due to the influx of funds from the sale of last year's rice stocks.

16. Ecuador's balance of payments prospects largely depend on:

a. The maintenance of export values in the face of increasing world supplies of, and lower prices for, the country's principal exports (especially rice, which with cacao made up 80% of Ecuador's 1948 exports, excluding non-monetary gold).

b. Improvement of the competitive positions of Ecuador's export commodities and the production of new commodities (for export as well as replacement of others now imported) through appropriate
development measures.

c. The extent to which imports, inflated by extraordinary requirements for reconstruction from the effects of last year's earthquake, can be kept in line with exports.

d. The ability to attract foreign capital.

e. The size of the external debt service, taking account of the $7 million recently loaned by the Export-Import Bank for earthquake reconstruction and the possibility of a settlement of the debt now in default.

**EXPORTS**

17. If Ecuador's balance of payments, unlike those of some other South American lands, has not been threatened by convertibility problems (about 80% of Ecuador's export-import trade moves within the dollar area), its vulnerability to changing market conditions for the country's exports was amply demonstrated last year. After enjoying a high level of exports in recent years, the value of rice exports dropped from $13.7 million in 1948 to $4.7 million in 1949, and cacao exports fell from $14 million to $8.9 million.

18. The discontinuation of international rice allocations, the shift of Latin America from a deficit-import to a surplus-export area for rice and the growing availability of surpluses for export from the Far East, all contributed toward reducing Ecuador's proceeds from rice exports in 1949. The fall in export values was accompanied by a 50% decline in the volume of rice shipped abroad by Ecuador, as well as a steady lowering of unit prices. To stimulate the liquidation of the 1,500 million pounds of rice which had accumulated by the end of last
year, the Government subsidized the export of rice in December 1949 by
temporarily raising the exchange rate returnable to rice exporters from
13.13 sucre to 17 sucre to the dollar. Through this device, Ecuador
had succeeded in liquidating four-fifths of its rice stocks by the end
of April of this year.

19. Ecuador's future as a rice exporter does not appear promising. Costs of production are relatively high and qualities are inferior.
The program of the Ecuadorian Corporacion de Fomento, assisted by the
IBEC, to improve quality and lower costs (which now seems assured as a
consequence of a recent Eximbank loan) may make it possible for Ecuador
to retain some of its markets, but competition from other producers,
particularly Siam, can be expected to intensify. The prospect is for
prices to continue to decline, with the possible level of stabilization
at about 2.5 cents per pound. Under these circumstances, Ecuador may
not be able to realize as much as $3 million a year from rice exports
in the not too distant future, although income from sales of rice in
1950 should be close to $6.4 million through the liquidation of the
carry-over from last year.

20. However, marketing prospects for Ecuador's cacao, once the
leading commercial crop, but now reduced to lesser importance by tree
diseases, are more favorable. While this year's crop may not be as
large as last year's, prices are expected to be higher, yielding in-
come in 1950 in the neighborhood of $8.7 million, about the same as
last year's exports. In the longer run, earnings from cacao exports
will depend on the success of current efforts by the Corporacion de
Fomento to counteract the falling production trend by the planting of
disease-resistant strains. If these activities are taken into account, present indications are that Ecuador could anticipate earnings of about $7 to $8 million annually from its cacao exports in the next five years.

21. The outlook for other Ecuadorian exports are also satisfactory. The prospects for coffee and bananas are especially good this year, it now being expected that coffee will yield $11.4 million at an average price of 38 cents per pound and bananas and fruits, $6.5 million. Although present coffee prices may not last for five years, the increasing importance of "washed" coffee exports from Ecuador should be reflected in high income and annual proceeds of about $8 to $9 million per annum from this source are a reasonable expectation. Exports of bananas and fruits can be expected to follow a rising trend, averaging about $7 to $8 million annually in the next few years. However, exports of panama hats and miscellaneous items are expected to remain at approximately current levels ($3.9 million and $2.5 million, respectively).

22. Summarizing the foregoing estimates, Ecuador's average annual export trade receipts during the next five years may turn out as follows compared with estimated export proceeds in 1950 and actual receipts in 1949, in millions of dollars:

<table>
<thead>
<tr>
<th>Commodity</th>
<th>1949</th>
<th>1950</th>
<th>1951 - 1955</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rice</td>
<td>$4.7</td>
<td>$6.4</td>
<td>$3.0</td>
</tr>
<tr>
<td>Cacao</td>
<td>8.9</td>
<td>8.7</td>
<td>8.5</td>
</tr>
<tr>
<td>Coffee</td>
<td>5.0</td>
<td>11.4</td>
<td>8.5</td>
</tr>
<tr>
<td>Bananas and fruit</td>
<td>3.8</td>
<td>6.5</td>
<td>7.5</td>
</tr>
<tr>
<td>Panama hats</td>
<td>4.0</td>
<td>3.9</td>
<td>4.0</td>
</tr>
<tr>
<td>Other</td>
<td>2.0</td>
<td>2.5</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$28.4</strong></td>
<td><strong>$39.4</strong></td>
<td><strong>$36.5</strong></td>
</tr>
</tbody>
</table>
23. While an annual level of exports in the neighborhood of $36.5 million during the next five years is within the expected order of magnitude, higher exports should be possible to a country whose natural resources, although not strikingly rich, are nevertheless appreciable. Although no thoroughgoing investigations have been completed, suggestions have been made that potentialities for development exist in forest products, fishing and canning and animal husbandry. However, regardless of the vigor with which development proceeds, projects in these areas can hardly be expected to add appreciably to Ecuador's exports before 1955.

**Imports**

24. Of more immediate significance to Ecuador's balance of payments are the attempts of the Corporacion de Fomento to stimulate and improve domestic production of wheat and cotton as well as the Government's plan to reorganize and modernize the textile industry. Should these programs achieve a measure of success, substantial cuts in imports would be possible, since textiles and cereals constitute a sizeable proportion of Ecuador's imports (30% of 1948 imports).

25. Without stimulating internal production of commodities to substitute for imports, however, no appreciable decline in imports is foreseeable in the next few years. The bulk of Ecuador's imports consist of commodities which are not produced domestically (55% of the imports are capital goods and 15% foodstuffs) and the need for them has intensified as a consequence of the earthquake and the inception of the development programs.

26. Some decline in world import prices is to be expected.
This factor, and the possibility of substituting domestic production for imports, may bring some reduction in imports. There is also the possibility that the sucre eventually will be devalued. However, the effect of devaluation might have had on increasing exports and diminishing the demand for imports has been anticipated to a considerable extent by the series of special deviations from the official rate decreed from time to time and computed to be already equivalent to an effective devaluation of over 20%. Taking all probabilities into account, it is conceivable that annual imports can be maintained at about $40 million during the next five years. Imports of capital goods could be cut by curtailing some development programs, but this would only result in the delay or elimination of projects intended to relieve pressure on Ecuador's balance of payments.

EXCHANGE SYSTEM AND THE IMF

27. Under an Emergency Law for International Transfers enacted in Ecuador in June 1947, the Fund approved the application of taxes and surcharges on the sale of exchange which raised the effective rates above the par value of 13.50 sucres to the U.S. dollar to 15.04 sucres for essential imports and 23.54 for luxury imports. Without the Fund's consent, Ecuador thereafter modified its exchange system in December 1949 to provide a subsidy of 3.87 sucres to the dollar for rice exports and 1.87 sucres for general exports, raising the effective rates for these exports to 17 and 15 sucres, respectively. The higher rate for rice exports was considered temporary until April 30, 1950, but was extended for a month because the 1949 rice stocks had not been fully exported by the end of April. It has just been extended again until November 1950.
New buying rates were also established for 25 minor exports, and on the import side, commodities were shifted to more restrictive categories and higher rates were imposed on luxury imports.

28. The Government's interest in maintaining revenues which flow from its multiple currency practices has germinated some resistance to proposals for the termination of these practices. At Ecuador's request, the Fund recently approved the extension of the country's multiple currency practices until November 30, 1950. The Ecuadorians have been reported as very well satisfied with the results obtained from the revisions in the exchange system made last December. On the other hand, IMF officials view the modifications in the exchange rates as complicating the Ecuadorian exchange system and as representing a partial de facto depreciation under which the par value of the sucre has lost its meaning. The Fund officials also feel that the present system, although encouraging exports and curtailing imports, is not an adequate solution of Ecuador's payments problem.

FOREIGN INVESTMENTS

29. In the four years between 1946 and 1949, foreign private direct investment in Ecuador was substantial, totalling about $25 million. However, it has been declining steadily from a high of $8 million in 1946 and is believed to have amounted to only $4 million in 1949, 50% of the total originally expected. With the termination of operations by the Royal Dutch Shell Group and the Standard Oil Company of New Jersey this year (which have invested some $40 million in petroleum explorations in Ecuador since 1937) and the expected closing down of the country's largest foreign-operated gold mine this year (which will
mean the end of annual dollar income which, in 1949, was $800,000),
the prospects for attracting foreign capital do not appear to be
favorable at this time. Moreover, plans for early development of a
fish cannery with foreign capital now seem to have been delayed. If,
as seems probable, sizeable reductions occur in foreign capital inflow
over recent years, as well as in non-monetary gold exports (which
amounted to $2.6 million in 1948), Ecuador's balance of payments will,
of course, be placed under increased pressure.

FOREIGN DEBT

30. At the end of December 1949, Ecuador's outstanding exter-
nal debt totalled some $24.3 million. This amount is expected to in-
crease to $37.5 million as undisbursed Export-Import Bank credits are
utilized in full. In addition, nearly $20 million in interest arrears
has accumulated on a portion of the debt, totalling $12.5 million, in
default since 1929. The defaulted debt, largely held in Great Britain,
is part of an old loan to finance the Guayaquil and Quito Railway in the
late 1890's; the remaining indebtedness, which is being serviced regu-
larly, consists of inter-governmental credits extended to Ecuador since
the beginning of World War II, primarily loans from the Eximbank.

31. Discussions have taken place between the Ecuadorian Govern-
ment and the British Council of Foreign Bondholders concerning a settle-
ment of the defaulted debt, but no agreement has been reached to date.
Differences between the Ecuadorian offer and the Council's requests do
not seem insurmountable and a settlement should therefore be possible.
If it is assumed that the terms of the 1948 Chilean debt settlement
(which presents a recent pertinent example) are followed in settling the
Ecuadorian debt, that all Eximbank credits are utilized by their closing dates, and that about one-third of the defaulted debt is held in Ecuador (as there is reason to believe), annual service charges on Ecuador's entire debt would amount to some $2.2 million in 1950, rise to a maximum of $3.0 million in 1951, and decline gradually thereafter. Service requirements for 1950 amount to about 6% of estimated exports. Normally, this proportion would not be considered particularly high for a country in Ecuador's position, but an added annual burden of about $1.0 million to cover service charges on the defaulted debt and the new $7 million Export-Import Bank loan would add to the rigidity of Ecuador's burdened balance of payments.

Moreover, it appears that further increases in Ecuador's debt burden for reconstruction and development activities are almost certain since the low level of international reserves excludes further financing of import deficits. In view of the unfavorable prospects for the Ecuadorian balance of payments in the next five years, however, any substantial increase in external indebtedness does not appear manageable. After 1955, the outlook would seem to be more promising. By that time, the effects of present development programs should begin to be felt in the balance of payments. It is also to be expected that most of the extraordinary reconstruction needs will have been met by 1956 and that a margin between export receipts and imports will appear from which funds for servicing additional loans can be allocated.

INTERNAL DEVELOPMENTS

33. Internal economic conditions in Ecuador are largely
dependent upon foreign trade, exports accounting for an estimated 23% of the national income (estimated for 1949 at 3,868 million sucres or $287 million at the official rate of exchange). Until the latter part of 1948, the relatively satisfactory position of Ecuador's balance of payments induced an expansion of domestic economic activity which expressed itself in considerable part in pressure for consumption goods imports and in non-productive investment.

34. Evidence of latent inflation appeared in Ecuador soon after the end of the war, but the Government's fiscal policy does not seem to have been responsible for this development. Disclosed figures on the ordinary and extraordinary budget and special accounts from 1946 to 1948 show net surpluses totalling 28.2 million sucres ($2.1 million). Although not all of the Government's operations were included in the disclosed accounts, evidence of the basic soundness of the Government's fiscal position is furnished by the decrease of Central Bank credits to the Government from 155 million sucres ($11.5 million) at the end of 1946 to 52 million ($4.2 million) at the end of 1948.

35. Throughout the period, however, bank credits to the private sector were expanding, such credits (excluding rediscounts by the Central Bank) increasing from 494 million sucres ($36.6 million) at the end of 1945 to 694 million ($51.4 million) at the end of 1948. The inflationary impact of credit expansion in the private sector of the economy was partially offset by a reduction in the Government's obligations to the Central Bank and liquidation of international reserves.

36. Consequently, money supply increased only moderately, from 624 million sucres ($46.9 million) at the end of 1945 to 653 million ($48.3 million) at the end of 1948. In spite of the small increase
in money in circulation, the relative deficiency of consumer goods was reflected in the movement of wholesale prices of home-consumed goods, the index for which rose from 266 (January/June 1939 = 100) at the end of 1945, to 388 at the end of 1948.

37. On the whole, however, internal economic conditions in Ecuador were not unsatisfactory before the end of 1948. Such, at least, was the belief of the Government, which initiated a rather ambitious development program toward the middle of that year. Funds for the Corporacion de Fomento, established in 1947, were provided by diversion of the surcharge of 5 sucrea (37 cents) per dollar on the sale of exchange for certain categories of imports which had originally been used to repay the Government's debt to the Central Bank and the creation of a Security Stabilization Fund. A Development Bank, which heads 15 provincial banks, was also created and the operation of the system was financed by a tax and surcharge on the sale of foreign exchange, loans from the Central Bank and private deposits.

38. The combined impact of the Ambato earthquake and the deterioration of the Ecuadorian balance of payments have resulted in the diversion of substantial resources of the new development entities from the original purposes of these organizations. About 15 million sucres ($1.1 million) has been expended by the Corporacion de Fomento alone on works and assistance in the regions damaged by the earthquake. Moreover, since last December, the receipts from the exchange surcharge which were to be allocated to the Corporacion, have been used to finance the subsidy on rice exports through the multiple exchange system. Unless other means of financing are found (no easy matter in the present circumstances), or production is increased, future activities of the
Corporacion appear dependent upon increased budget allocations or direct aid from the Central Bank, either of which methods of financing is likely to have inflationary effects.

39. Manifestations of increasing inflationary pressures were clearly apparent in 1949. According to the latest reliable data, the ordinary and extraordinary budgets closed with a combined deficit of 31.9 sucre $2.4 million), although surpluses in special accounts appear to have reduced the overall operating deficit of the Government to 15.9 million sucre (§1.2 million). Bank credit, aided by Central Bank discounting, continued to expand, rising 20% during the year to 747 million sucre (§55.3 million). Heavy Central Bank discounting operations $50 million sucre (§3.7 million) in 1948 and 150 million sucre (§11.1 million) in 1949 originally were started to offset the downward trend of business activity, but more recently these operations are explained by the necessity for financing the Government's rice support program. Responding to the inflationary effects of the fiscal deficit and credit expansion, the wholesale price index of home consumed goods (January/June 1939 = 100) increased from 390 in December 1948 to 442 in March 1949. However, the deflationary counteraction of the balance of payments deficit of $13.6 million (180 million sucre), which kept the increase in money supply down to only 9% during the year, also was responsible for a recession in the price index to 373 by December, 1949.

40. Partly because of the difficulties inherent in the balance of payments and partly because of the burdens imposed by earthquake reconstruction, Ecuador's internal financial position promises to remain strained in the immediate future and for the next few
years. It is ironic that the greater the Government's success in curbing imports, the greater will be the danger of inflation, unless output can be increased correspondingly. The financial cost of reconstruction is estimated at some 60 million sucres ($4.4 million) per annum in 1951-55; in 1950, planned expenditures for this purpose came to 80 million sucres ($5.9 million). It is difficult to see how Ecuador can finance expenditures of these magnitudes in a noninflationary manner without continuing to divert resources from development. This situation presents Ecuador's officialdom with the unhappy dilemma of choosing between reconstruction and development. It is safe to assume that political expediency and economic necessity will make the choice difficult and that increasing inflation will be the probable result.

41. The extraordinary budget for 1950, which is largely devoted to earthquake reconstruction, illustrates the difficulty. Out of total estimated expenditures of 138 million sucres ($10.2 million), 55 million sucres ($4.1 million) will come from the Central Bank and the state Security Stabilization Fund. An expansion of the money supply to the extent of such financing is therefore foreseeable. Late reports also indicate that the ordinary budget for 1950, which was balanced at 383 million ($28.7 million), has registered a deficit in the first quarter of the year to the extent of 16 million sucres ($1.2 million).

POLITICAL SITUATION

42. When he assumed power on August 31, 1948, President Galo Plaza endeavored to initiate a vigorous development program, resorting freely to foreign technical aid. Besides assistance received from IBEC and the Export-Import Bank, missions were invited from and sent by the
United Nations, Mexico, and the FAO. In spite of these efforts, the President's hopes have largely been disappointed, partly because of the deterioration in Ecuador's export position, partly because of the Ambato earthquake, and in part because the IBRD has not found it possible to support his ideas financially with the speed or on the scale the President evidently expected. These developments have endangered his own tenure of office (which expires on August 31, 1952) and diverted his attention from economic to political problems.

43. Congressional elections were held in June 1950. The Movimiento Civico Democratico Nacional, Plaza's party, failed to carry the three largest cities in the country, Quito, Guayaquil and Cuenca, and lost its majority position in the legislature. Evidence is not wanting that Galo Plaza feels the growing insecurity of his position (two abortive attempts to overthrow him have been reported). Even much-needed development has had to give way as a consequence of the uncertain political climate, a noteworthy example being the paving of the Quevedo-Manta Highway which would help economic progress of the Sierra and stimulate development of Manta as a first-rate port. A loan of $3.2 million for this purpose was approved by the Export-Import Bank, but the Plaza Administration has not dared to allow construction to proceed because of bitter opposition from Guayaquil, which fears competition from Manta.

CONCLUSIONS

44. An analysis of Ecuador's domestic financial prospects confirms the conclusion reached on the basis of the country's external financial position: Ecuador can ill afford to increase its debt burden
during the next five years. While this conclusion does not foreclose the possibility of a small loan, directly linked to improving the condition of the balance of payments, it does imply that interest payments on any new loan must be low and amortization payments must be deferred until Ecuador's development programs, most of which depend on foreign credits, have had an opportunity to improve domestic production of commodities for export and for replacement of imports.

45. Ecuador's present difficulties (the collapse of the rice export market and the Ambato earthquake) are largely due to uncontrollable factors, and there is little that can be done in the short run to remedy the situation. Ecuador's position is difficult, but it is not without hope; careful formulation and effective execution of a practical development program, which would also limit reconstruction expenditures in favor of economic development, could greatly improve its creditworthiness. The program would probably call for technical assistance over a period of some years. With technical assistance, supplemented by financial aid for development which fits into the framework of a well conceived program promising continuous and effective effort toward completion, much could be done to improve Ecuador's long-term balance of payments position; without such a program, it is difficult to see how Ecuador can halt domestic inflation and improve its creditworthiness.

46. The Bank is not now in position to determine the essential characteristics of an investment program for Ecuador which would improve its creditworthiness. Information is lacking concerning the magnitudes which would be involved, the period over which assistance would be required, or even the extent to which the program would be
aided by foreign financial credits. It is clear, however, that the Bank's attitude must be governed by the answers to such questions as these. It is not inconceivable that investigation might show that the needs are sufficiently moderate to justify a series of small loans, the combined effect of which would be to allow repayment and additional safe borrowing.