

Ecuador

Ecuador's aim is to increase bilateral trade as well as bringing about a joint plan to develop Australian investments in sectors such as mining, telecommunications, tourism, general infrastructure and commercial agricultural products. Ecuador also seeks to increase relations in the fields of culture, science and technology, and to benefit from Australian technical assistance.

*Embassy of Ecuador*¹

Introduction

- 12.1 In 1822 Ecuador gained independence from Spain and joined the federation of Gran Colombia that included Venezuela, Colombia and Panama. The federation did not last long and in 1830 Ecuador seceded and became an independent country.
- 12.2 Ecuador has been shaped by instability in the political arena. There has been a number of defining features that have impacted on the economic and social development of the country. Soon after independence there emerged rivalry between the coast and the mountains. The landowners of the mountain region combined with the Catholic Church to create a formidable political alliance opposed by the rapidly growing banking and agricultural interests particularly cocoa on the coast. With the collapse of the global cocoa market in the 1920s and the Great Depression of the 1930s political instability emerged. Political stability was restored from 1948-1960 as the economy improved with the growing receipts from the export of bananas.²

1 Ecuador, Submission, p. 78.

- 12.3 Instability returned in the 1960s with the state expanding its role in the economy in keeping with international trends in economic theory. The military government of 1963-1966 took a strong anti-communist stance and a further government reserved petroleum exploration to the state in 1972. Modernisation of the state was in part paid for by petrodollars during the boom years of the 1970s and by heavy foreign debt commitments.
- 12.4 In 1978 a constitutional referendum provided the basis for a return to civilian rule in 1979. Since 1979 the political scene has been shaped by the tense relationship between the executive and the congress. The military still has considerable influence behind the scenes, it enjoys independence through their substantial commercial interests and is seen to be apart from the rivalry, corruption and inefficiencies of civilian political life.
- 12.5 Successive civilian governments have attempted to reform the economy but have met with limited success to date. In August 1998 President Mahuad took office. He inherited a struggling economy reeling from the effects of US\$2.6 billion in flood damage caused by El Niño, with Latin America's highest inflation rate and suffering from a slump in oil and banana prices. In March 1999 congressional refusal to pass a revised reform package led to a severe financial crisis, destroyed most of the banking system and left President Mahuad in a tenuous position.
- 12.6 In November 1999 Ecuador defaulted on its Brady bond debt that further damaged its international financial standing and deepened the internal political crisis.
- 12.7 In January 2000 President Mahuad declared a state of emergency and announced a plan to introduce dollarisation, a measure that was designed to control runaway inflation. What materialised was a coup that followed the withdrawal of support for President Mahuad by the head of the armed forces. The 3-man junta quickly relinquished power to Mahuad's Vice-President, Gustavo Noboa, following international pressure.
- 12.8 President Noboa has since obtained congressional passage for a law that implements structural economic reforms including dollarisation of the economy and the congress is reviewing aspects of the law to enable the IMF and other multilateral finance agencies to supply much needed short term funding.

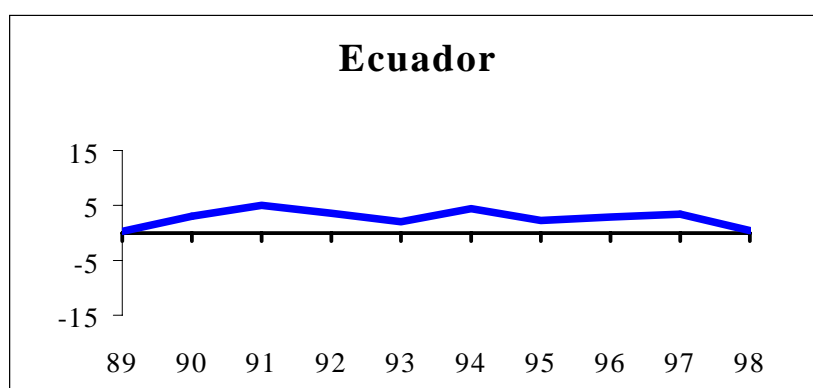
Overview of the Economy

- 12.9 In 1990 Ecuador embraced trade liberalisation that saw the elimination of import quotas, permits and subsidies. Trade liberalisation has stimulated the growth of non-traditional exports but Ecuador still relies on agriculture and oil exports and it is this reliance that makes it vulnerable to external price variations. It is the world's number one banana exporter and a significant exporter of prawns, cocoa and fish.
- 12.10 Ecuador's vulnerability has been exposed as it struggles with massive flood damage and a downturn in oil and banana prices in 1998.³ As a result the country is currently suffering its worst recession in 50 years with the economy contracting more than 7 per cent in 1999, unemployment exceeding 20 per cent and year-on-year inflation exceeding 70 per cent.
- 12.11 Agriculture, forestry and fishing have averaged 17.5 per cent of GDP in the last 10 years while the oil and mining sectors have averaged 12 per cent of GDP during that period.
- 12.12 With regard to the manufacturing sector it has dropped from around 18.7 per cent of GDP in 1987 to around 15 per cent today as trade liberalisation removed protective barriers and subsidies. Problems for the sector have been high interest rates and lack of credit.⁴
- 12.13 The tourism sector is performing well accounting for 15 per cent of GDP however a lack of infrastructure development has prevented expansion. Tourism is mainly focused on the world famous Galapagos Islands.
- 12.14 Real GDP growth was -7.5 per cent in 1999, the annual percentage change down from 0.4 per cent in 1998. Figure 12.1 shows real GDP growth for the ten years from 1989 to 1998.

3 See DFAT, Submission, p. 292.

4 DFAT, Country Brief.

Figure 12.1 Real GDP Growth – 1989-1998

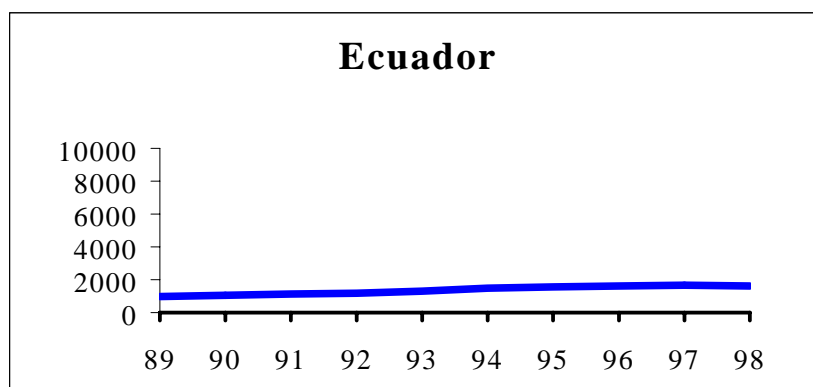


Source *Australia's Trade with the Americas, 1993-94 & 1998, Department of Foreign Affairs and Trade, Canberra.*

12.15 The inflation rate has jumped from 30.6 per cent in 1997, to 36.1 per cent in 1998 and up to a staggering 52.3 per cent in 1999. A major difficulty in Ecuador is the low domestic savings rate that leaves the country dependent on external finance.

12.16 The GDP per capita⁵ has remained fairly constant since 1994 with it being US\$1,102 in 1999. The GDP per capita for the period 1989 to 1998 is shown in Figure 12.2.

Figure 12.2 GDP Per Capita – 1989-1998



Source *Australia's Trade with the Americas, 1998, Department of Foreign Affairs and Trade, Canberra and IMF/IFS and EIU Country Reports.*

12.17 Ecuador became a member of the WTO in 1997 and is a founding member of the Andean Community. Ecuador has requested membership of APEC.

5 Ecuador's population was 12.17 million in 1998.

The Nature of the Trade and Investment Relationship

- 12.18 Information from the Central Bank of Ecuador shows that Australian investment activity in Ecuador is relatively scarce and is found in the mining sector. The Central Bank registered the first Australian investment in Ecuador in 1993, some US\$28.5 ('000), that grew to US\$689.3 in 1994, falling to US\$33.0 in 1995 and increasing to US\$1,600.5 in 1996 (the latest figure provided).⁶
- 12.19 Trade between Australia and Ecuador is not substantial and has remained static over the last 5 years. In evidence to the Committee the Ambassador of the Republic of Ecuador, HE Mr Posso-Serrano, emphasised the imbalance in the trade relationship with it being heavily in Australia's favour.⁷ Total Australian exports to Ecuador totalled \$17.0 million in 1998 and imports from Ecuador were valued at \$2.3 million.
- 12.20 Principal Australian exports in 1998 (latest available figures) were coated flat-rolled steel - \$7.61 million; confidential items - \$5.97 million; agricultural machinery (excl. tractors) - \$1.22 million and milk and cream - \$573,000.
- 12.21 Principal imports from Ecuador for 1998 were cocoa - \$1.21 million; coffee and coffee substitutes - \$270,000; veneers, plywood and particle board - \$171,000 and miscellaneous manufactures - \$124,000.
- 12.22 Leading import suppliers to Ecuador are the United States with 31.6 per cent of the total (1998 figures) followed by Colombia - 9.7 per cent, Japan - 8.4 per cent, Venezuela - 4.8 per cent and Germany on 3.9 per cent. Australia was ranked 34th with 0.2 per cent of the total. The United States is the dominant export market with 36.5 per cent of the total followed by Colombia and Chile on 7.6 per cent and 4.9 per cent of the total respectively. Australia does not register. From these figures it is clear that America dominates Ecuador's two-way trade, outstripping Ecuador's neighbour Colombia by a country mile.
- 12.23 Ecuador is very keen to expand trade and investment with Australia. Rather than continuing to look north, Ecuador is looking to diversify and has begun to look eastward for trade and investment opportunities. In 1998 Ecuador opened an Embassy in Australia. As the Ambassador noted:

We want to show our interest in this region and, particularly, in Australia. We know that we have economic problems with respect to keeping the embassy open here but, in any case, we have made the effort to open the embassy and to keep it open on this

6 Provided by Ministerio de Relaciones Exteriores, Republica Del Ecuador.

7 Ecuador, Submission, p. 78.

continent because we have a tremendous interest in raising our country's profile, both within Australia and within the Asia-Pacific region. We feel that Australia is a very important country, which will help us to project our profile.⁸

- 12.24 While the Trade Sub-Committee was in Quito it was emphasised to them that the relationship would be very much assisted if the Australian government were to open a mission in Quito. Currently the Australian Ambassador in Venezuela is accredited to Ecuador. Although the Committee appreciates that having a permanent presence in Ecuador would demonstrate a tangible display of interest, the current situation does not diminish the desire on both sides to expand the trade and investment relationship and with this desire comes a high level of interest and goodwill.
- 12.25 Australia has a number of key bilateral agreements with Ecuador namely a Treaty of Extradition signed on 13 October 1988 (came into force in 1990) and a Treaty on Mutual Assistance in Criminal Matters signed on 16 December 1993. Ecuador's Ministry of Foreign Affairs presented the Trade Sub-Committee with text of a draft Investment Promotion and Protection Agreement. The Trade Sub-Committee undertook to bring the draft text to the attention of the Australian government. The Committee has been advised that the matter is being considered. Ecuador is keen to put in place the mechanism to protect the investments of Australia in Ecuador.
- 12.26 During discussions Ministry of Foreign Affairs officials indicated they would like to see a double taxation agreement in place between Australia and Ecuador
- 12.27 The Ministry of Foreign Affairs has made the general direction that in order to extend the commercial relationship between the two countries it is necessary to develop a series of activities among which it sees the following as relevant:
- Deepen diplomatic links: the existence of the Ad-Hoc Consulates in Sydney and Melbourne represent elements which without any doubt will contribute to an intensification of commercial relationships, nevertheless it would be convenient to analyse the possibility to establish an Ad-Hoc Consulates [sic] in Perth, one of the main Western Australian cities, with remarkable economic, industrial and commercial success.
 - Extend and deepen information and knowledge about the characteristics of these markets (consumer habits, import structures, commercialisation mechanisms, etc.).

- Promote the realisation of country-specific market studies.
- Impulse [sic] the development of bilateral exchange through direct commerce (avoiding any triangulation).
- Promote missions of entrepreneurs that strengthen commercial and investment relationships.
- Stimulate participation at international fairs held in these markets.
- Analyse transport alternatives to those markets.
- Extend the conclusion of commercial and investment agreements that intensify these activities.⁹

12.28 Late last year the Consulates of the Republic of Ecuador, located in Melbourne and Sydney, saw the appointment of new Honorary Consuls, Mr Ian Millner in Sydney and Mr Andrew Jacobi in Melbourne.

Opportunities for Australian Business

12.29 One of the difficulties that Ecuador's Ambassador identified in developing the trade and investment relationship is the lack of understanding about what Ecuador can provide by way of product. This lack of understanding works in reverse too for Australian businesses to be able identify opportunities in Ecuador. This point came up in discussions the Trade Sub-Committee had with the Minister of Foreign Commerce, Industrialisation and Fishing in Quito.

12.30 The Ambassador noted that Ecuador is in the position to expand exports of products¹⁰ into Australia and one such product is cut flowers. Ecuador has a substantial fresh cut flower trade and it produces the best quality roses anywhere in the world and as the Ambassador pointed out:

The market in Australia could be very interesting for Ecuadorian producers. We are looking at the possibility of having a type of certification to show that we can prevent diseases in cut flowers. We probably also need better links with the quarantine service to show that there is no danger with our cut flowers and that the cut flowers cannot reproduce.¹¹

12.31 Discussions with the Minister of Foreign Commerce, Industrialisation and Fishing were wide ranging and areas of opportunity in Ecuador were canvassed. Ecuador is building an oil pipeline, selling telecommunications, selling 7 electricity companies, undertaking road construction, expanding fishing and flower exports – among the export

9 Provided by Ministerio de Relaciones Exteriores, Republica Del Ecuador.

10 See Ecuador, Submission, p. 78 for list.

11 Ecuadorean Ambassador, Transcript, 13 August 1999, p. 44.

markets for Ecuador's flowers are China and the EU. Ecuador's cut flower export industry offers an opportunity for cooperation with the Australian horticultural industry.¹²

- 12.32 The Trade Sub-Committee met briefly with delegates from FEDEXPOR – the Ecuadorean Exporters' Federation - and CORPEI¹³ – the Ecuador Export and Investment Promotion Corporation. They identified opportunities for Australian expertise and investment in the wood and fishing sectors. CORPEI has a small commercial office in Canberra.
- 12.33 For Australian business, Ecuador is a market that is open to Australian investments in energy and mining, telecommunications services and equipment, tourism, general infrastructure including port infrastructure and commercial agriculture products. They are particularly interested in the formation of joint ventures. The provision of technical assistance and capital is critical for the development of Ecuador.
- 12.34 Although the economy is small in Ecuador and there are significant structural difficulties, Ecuador like Colombia can be viewed as a *greenfields* investment opportunity for those Australian businesses who wish to get in on the ground floor and take advantage of the low start up costs.

Mining

- 12.35 It was explained to the Trade Sub-Committee that the state of mining in Ecuador is Jurassic Park-like and that the sector needed greater development and Australia with its mining expertise would be extremely well placed to provide assistance.
- 12.36 The Ministry of Energy and Mines and Ecuador's mining chamber wish to see an increase in foreign direct investment and new mining laws will give security to investors. One aspect that will be examined is a guarantee that there will be no variability in the amount of taxes – it was said that the intention was that VAT would stay but royalties would be eliminated. Interestingly members of the Trade Sub-Committee met an Australian who has been in Ecuador for 9 years in the mining sector. He commented that he has not struck any barriers to doing business and on a dollar risk basis he sees Ecuador as the best place for investment as it is *cheap to get into*.

12 DFAT, Submission, p. 293.

13 CORPEI – the Corporation for Promotion of Exports and Investments was created under the Foreign Trade and Investments Law (LEXI) of 9 June 1997. CORPEI is a private non-profit organisation created to contribute to the economic growth of Ecuador.

Tourism

- 12.37 Ecuador's performing sector is tourism. Ecuador is promoted as *Your natural destiny* and it is a tourist's paradise. It is located at the centre of the world and has a diversity of landscape and culture. The country has the Pacific Coast, the Andean Highlands, the Amazon Basin and Galapagos. The Galapagos Islands – the natural sanctuary of evolution - are world famous and Ecuador is extremely conscious of managing the environment on the islands.
- 12.38 Eco-tourism is becoming increasingly important to Ecuador along with adventure holidays, health tourism and agri-tourism. There are significant opportunities for Australian business in this sector with its experience in developing and promoting tourism to become a major contributor to the Australian economy. As a result of discussions in Quito the Ecuadorean Foreign Ministry proposed to convene a meeting of tourist experts in Ecuador and the outcomes of that meeting will give the opportunity for Australia to provide technical input into the industry.

Infrastructure

- 12.39 On the infrastructure front, the Trade Sub-Committee noted in discussions with ministers and government officials in Quito, that there was considerable scope for airport and road redevelopment opportunities using Australian expertise. CONAM (National Modernisation Council) is looking at airport development both at Quito and Guayaquil (Ecuador's second largest city that is located on the southern coast) as a private sector BOT investment. On the drawing board is port development at Manta – located in the centre of Ecuador's Pacific Coastline. The authorities want to build a road from Manta and on to Brazil and develop Manta as a transfer port for distribution to the rest of South America.
- 12.40 Ecuador suffers energy shortages and Australia is at the forefront of solar technology that could be used to alleviate the shortages.¹⁴ DFAT points out that Australian land management and irrigation systems could be used to overcome a lack of agricultural infrastructure.¹⁵

Market Access Issues

- 12.41 There are a number of market access issues that impact on doing business in Ecuador. The banking system is weak and there are custom clearance delays. Most of the banks are government owned and now the

14 DFAT, Submission, p. 293.

15 *ibid.*

government is wishing to put the ownership back into private hands. Other market access issues include the arbitrary issuance of import permits to protect local producers and the imposition of some formal and informal quantitative restrictions on certain imports.

- 12.42 There was a monopoly in the telecommunications sector but the Trade Sub-Committee was advised by CONAM that laws have been passed to open up oil and gas, telecommunications and energy. Now 50 per cent of telecommunications and electricity bodies can be sold and there will be important changes to social security and the management of pension funds in Ecuador.
- 12.43 Ecuador is a founding member of the Andean Community and under the Andean Trade Preference Act, Ecuador enjoys duty free access on a number of its products entering the US market. With the Andean Community a common external tariff of 5-20 per cent took effect in 1995. Moreover Ecuador has bilateral free trade agreements with Chile, Colombia and Venezuela that do provide trade barriers to exporting countries like Australia.
- 12.44 It is too early to determine the impact of dollarisation on the Ecuadorean economy through a reduction in the level of inflation, a decline in interest rates, stimulation of the private sector, and a better risk assessment to attract increased foreign investment.