



ANNUAL MEETING OF THE BOARDS OF GOVERNORS

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**ADDRESS BY THE GOVERNOR FOR ECUADOR
AT THE SECOND PLENARY SESSION**

Carlos Julio Emanuel

1. It is an honor for me to address you in this beautiful and hospitable city of Fortaleza, on the occasion of the Forty-third Annual Meeting of the Board of Governors of the Inter-American Development Bank and the Seventeenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation.
2. I wish to salute President Enrique Iglesias for his indisputable leadership in combating poverty in our countries. I also salute the entire professional staff of the Bank for their work in implementing the guidelines for the antipoverty campaign laid down by President Iglesias and the Board of Executive Directors.
3. I would like to speak for a few minutes about recent political and economic trends in Ecuador, which can be analyzed in two, clearly identified stages. The first relates to the Ecuadorian economy before dollarization, which we may call "the old economy", including the economic and political events that took place during and up to the end of the 1990s.
4. The second stage relates to the Ecuadorian economy after dollarization, which we call the new Ecuadorian economy, and which began approximately in January 2000. At that time, an official decision was announced to adopt dollarization, after the Ecuadorian people had gradually but inexorably decided unofficially to conduct their transactions in dollars.
5. The first stage, that of the old economy, has already been sufficiently reviewed, and is very well known internationally. The idea of the new economy, however, has not been sufficiently analyzed and understood and therefore deserves a brief explanation.
6. In the old economy, the problems were not significantly different from those that affected other Latin American countries: poor economic and political management and the resulting instability. In our country, for example, we suffered the impact of a war with Peru during the 1990s, as well as the problem of El Niño, which destroyed much of our infrastructure, and a sharp fall in international prices for our principal exports. Unfortunately, the measures that were taken to deal with these problems only made the situation worse.

Thus, the disorderly and accelerated growth in currency issues was the prelude to a sharp devaluation such as we had never before experienced. This in turn precipitated a crisis in the country's productive and financial sectors, resulting in the bankruptcy of thousands of firms and dozens of financial institutions and pushing unemployment figures to their highest level in our history as a republic.

7. Ecuador needed a radical change in economic policy. Dollarization constituted a "confidence shock" that meant a significant transformation for our country.

8. This is how the process was implemented. In the first place, it is important to recognize that there had been an informal, unofficial and spontaneous process of dollarization during the 1990s, so that when the official and essentially political decision was made to move to the dollar, roughly 80 percent of transactions were already being conducted in dollars. In the second place, between 9 January 2000, when the dollar was officially adopted, and December of that year, the process of exchanging sucres for dollars delivered by the Central Bank was completed. Official dollarization of the economy thus took place in an orderly manner in less than one calendar year.

9. What is the hallmark of the new Ecuadorian economy? We have economic and financial stability. **With the new monetary system, we adopted a policy that guarantees economic agents that monetary creation will never again be used as a policy for promoting economic activity, and neither will devaluation be used as a weapon for competition.** Ecuador, then, has renounced the possibility of issuing domestic currency in order to finance fiscal deficits, and it will not distort the terms of trade through devaluations. The drop in the inflation rate from 90 percent in 2000 to 14 percent in February of this year sends a clear signal to economic agents that we are converging towards international inflation rates, which means that our goal of a single-digit change in the price index by the end of the year is clearly within reach.

10. The Ecuadorian government is committed to promoting wealth creation through a market economy, with a price system that adequately reflects changes in macroeconomic variables. A stable economic system allows economic agents, including national and foreign investors, to have realistic expectations about the future. At the same time, consumers are in a better position to choose when they can examine various alternatives to maximize their earnings. This is why we are convinced that dollarization is an irreversible step towards a real economy.

11. Under the dollarization system, our gross domestic product has grown at a rate of 5.4 percent, the highest rate in Latin American and one of the highest in the world, thanks to the stimulus it has given to investment and the confidence it has inspired among economic agents. Our public finances ended the fiscal year with a surplus for the second year in a row, and for the first time in 18 years we were able to complete a program with the International Monetary Fund successfully. It is clear that dollarization, while it represents a straitjacket in monetary terms, also helps to establish sound public finances.

12. We never believed that dollarization would be a panacea or magic wand for solving all our economic problems. Nevertheless, it has been very useful in correcting the many distortions that have riddled our system for decades. It is a necessary but not a sufficient step

towards achieving sustainable economic development that will help improve the well-being of the Ecuadorian people. It is an option that Ecuador adopted to address an unprecedented crisis, and one that we are keeping in place because of the results it has produced.

13. Yet while we have made great progress, we are aware of the need to press ahead with structural reforms. We are working actively to privatize the electricity and telecommunications sectors and to contract all customs services to the private sector under concession. The National Competitiveness Agenda, which is a priority of our government, seeks to reduce the "Ecuador cost" through measures that will eliminate red tape and high interest rates in order to promote exports and foreign direct investment.

14. In keeping with the foregoing, the program that we are negotiating with the International Monetary Fund for the year 2002 calls for growth in gross domestic product of 4 percent, a reduction of inflation to the single-digit level by the end of the year, and a balance in the public accounts, under the assumption of US\$17 per barrel of oil. However, we expect to be able to end the year with another surplus, since the assumed oil price is considered conservative, and because there will also be the impact of higher non-oil revenues, which in the first months of this year exceeded initial forecasts. In addition, we are sending to the National Congress, through the "economic emergency" route, a unified draft of the Fiscal Accountability Act, which includes elements of fiscal discipline and the creation of an Oil Stabilization Fund, in order to prevent the additional oil revenues that we will start to receive in 2003 once the heavy crude pipeline (OCP) is in service and the new proven oil reserves in the ITT region and other fields come on stream from being used to cover current expenditures.

15. The new Ecuadorian economy, as we have seen, is quite different from the old. **We have made enormous progress in the last two years, and this deserves to be properly reported to international analysts, investors and opinion leaders, who still highlight negative historic events that occurred in the old economy and that cannot be repeated under current circumstances.**

16. In light of the upcoming Monterrey Summit, where the presidents of more than 30 countries will be discussing the future of international financial organizations, I want to offer a few thoughts about how we in Ecuador view this challenge, and in particular the role of the IDB.

17. In light of the calls from various forums to rethink the very existence of multilateral institutions, the Ecuadorian government would like to take this opportunity to say that the IDB as an institution is too important not to continue strengthening it. In this respect, I want to highlight one of the many interesting proposals contained in the Report of the External Advisory Group headed by former Minister Angel Gurría, and which has been submitted for our consideration at this Annual Meeting. In particular, incentives should be strengthened to encourage more active participation by the private sector, for example by establishing a new institution in which the IDB would be associated not only with other international organizations but also directly with private firms and institutions.

18. Lastly, I would like to recognize the supremely useful work performed in recent years by the Multilateral Investment Fund (MIF), the member of the IDB group dedicated to

promoting the private sector in Latin America. The MIF has been playing a key role in introducing new approaches to develop markets and innovation. We believe that the MIF has planted a seed that must be preserved and nourished, and accordingly we fully support the generous initiatives to replenish its resources.