

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

ECUADOR**IDB COUNTRY STRATEGY
2012-2017****SEPTEMBER 2012**

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ABBREVIATIONS

AECID	Agencia Española de Cooperación Internacional para el Desarrollo [Spanish Agency for International Development Cooperation]
ALBA	Alianza Bolivariana para los Pueblos de Nuestra América [Bolivarian Alliance for the Peoples of Our America]
AMIE	Archivo Maestro de Instituciones Educativas [Master File of Educational Institutions]
BCS-EC	The Bank's country strategy with Ecuador
CAF	Banco de Desarrollo de América Latina [Development Bank of Latin America]
CGE	Contraloría General del Estado [Office of the Comptroller General]
CONELEC	Consejo Nacional de Electricidad [National Electricity Board]
COOTAD	Código de Ordenamiento Territorial, Autonomía y Descentralización [Code of Territorial Planning, Autonomy, and Decentralization]
COPYFP	Código Orgánico de Planificación y Finanzas Públicas [Code of Planning and Public Finance]
COSIPLAN	Consejo Sudamericano de Infraestructuras y Planeamiento [South American Infrastructure and Planning Council]
OECD/DAC	Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD)
EIB	European Investment Bank
ENDEMAIN	Encuesta Demográfica y de Salud Materna e Infantil [Demographic and Mother/Child Health Survey]
ENEMDU	Encuesta Urbana de Empleo y Desempleo [Urban Employment and Unemployment Survey]
ENIGHUR	Encuesta Nacional de Ingresos y Gastos de Hogares Urbanos y Rurales [National Survey of Urban and Rural Household Income and Expenditure]
ENIPLA	Estrategia Intersectorial de Planificación Familiar [Intersector Strategy for Family Planning]
GAD	Gobierno autónomo descentralizado [decentralized autonomous government]
GCI-9	Ninth General Capital Increase, Ninth General Increase in the Resources of the Inter-American Development Bank
GDP	Gross domestic product
GEF	Global Environment Facility
ICB	International competitive bidding
IDB	Inter-American Development Bank
IIC	Inter-American Investment Corporation
INCOP	Instituto Nacional de Contratación Pública [National Institute of Public Procurement]
INEC	Instituto Nacional de Estadísticas y Censos [National Statistics and Census Institute]
MAE	Ministry of the Environment

MAGAP	Ministry of Agriculture, Livestock, Aquaculture and Fisheries
MF	Ministry of Finance
MIDUVI	Ministry of Urban Development and Housing
MIES	Ministry of Economic and Social Inclusion
MIES/INFA	Instituto de la Niñez y la Familia [Institute of Childhood and the Family]
MIF	Multilateral Investment Fund
MSP	Ministry of Public Health
MTOP	Ministry of Transportation and Public Works
NFPS	Nonfinancial public sector
NSG	Non-sovereign guaranteed
OVE	Office of Evaluation and Oversight
PDOT	Plan de Desarrollo y Ordenamiento Territorial [Territorial Development and Land Use Plan]
PEFA	Public expenditure and financial accountability
PIRSA	Programa de Infraestructura Rural de Agua y Saneamiento [Rural Water and Sanitation Infrastructure Program]
PME	Plan Maestro de Electrificación [Electrification Master Plan]
PNBV	Plan Nacional del Buen Vivir [“Good Life” National Plan]
RMI	Risk management index
SBS	Superintendencia de Bancos y Seguros del Ecuador [Superintendency of Banks and Insurance of Ecuador]
SENPLADES	Secretaría Nacional de Planificación y Desarrollo [National Planning and Development Secretariat]
SETECI	Secretaría Técnica de Cooperación Internacional [Technical Secretariat for International Cooperation]
SG	Sovereign-guaranteed
SIISE	Sistema Integrado de Indicadores Sociales del Ecuador [Integrated System of Social Indicators of Ecuador]
SNCP	Sistema Nacional de Contrataciones [National Public Contracting System]
SNDGR	Sistema Nacional de Gestión del Riesgo [National Risk Management System]
SNI	Sistema Nacional de Interconexión [National Interconnection System]
TC	Technical cooperation
UBNs	Unmet basic needs
USAID	United States Agency for International Development
WEO	World Economic Outlook

EXECUTIVE SUMMARY¹

Country context:	Ecuador's economy has seen a robust recovery since the 2009 recession. During this time the authorities have put emphasis on changing the country's development model, strengthening the role of the State as a driver of the economy and as provider of public goods and services. To continue the gains in terms of growth and poverty reduction, the country must further address the challenges that limit its development potential. This will require strengthening the country's infrastructure and human capital, and adapting the institutional structure to the new legal mandates, the needs of the productive sector, and social demands.
The IDB in Ecuador:	The Bank has traditionally been one of the country's main sources of international finance. Over the last five years, the Bank has represented on average around 23% of Ecuador's external public debt and 43% of multilateral debt. The active loan portfolio at 30 April 2012 comprised 23 sovereign guaranteed operations totaling US\$1.921 billion, and 46 non-sovereign guaranteed operations totaling US\$269.7 million. In addition to loans, the Bank is an important provider of technical assistance, knowledge products to benefit the country, and institutional support to the State apparatus.
2012-2017 Strategy:	The objective of this strategy is to contribute to inclusive and sustainable economic development in Ecuador by supporting the country's efforts to overcome the long term constraints on economic growth and the structural barriers to overcoming poverty. The Bank will focus on the following sectors: (i) energy; (ii) transportation and logistics; (iii) social development; (iv) access to finance; (v) fiscal management; (vi) urban sustainability; (vii) rural development; and (viii) natural disaster risk management. The topics of diversity and of climate change and environmental sustainability will be addressed as crosscutting issues in this strategy.
Lending framework:	The lending framework assumes average annual approvals of US\$350 million, or US\$2.1 billion for the period 2012-2017. This scenario projects a positive average net capital flow for the country of US\$198 million. The macroeconomic assumptions and the lending framework for this strategy are consistent with the macroeconomic projections and the financing strategy of the Government of Ecuador.

¹ This country strategy with Ecuador will remain in effect from the date of its approval by the Bank's Board of Executive Directors until March 2017.

Strategy implementation: There will be a multisector focus to some of the Bank's interventions, mainly in social development and urban sustainability, where the synergies and complementarities of the different lines of action identified in this strategy are particularly strong. Further action will be taken to strengthen the country systems for procurement and financial management, as well as to improve government audit and oversight mechanisms. Dialogue and coordination will also continue with the development partners active in the country.

Risks: A downturn in oil prices could adversely impact macroeconomic performance, creating demand for financing that exceeds the forecast. Another risk factor is the institutional weakness and insufficient capacity in some areas of the public sector. This strategy includes measures to mitigate those risks.

RESULTS MATRIX²

² At the request of the borrowing country, the results matrix will not be disclosed. The non-disclosure of this information is in accordance with the "country-specific information" exception in paragraph 4.1 i of the Bank's Access to Information Policy.

I. COUNTRY CONTEXT

- 1.1 Ecuador's economy has seen a robust recovery since the 2009 recession, achieving a GDP growth rate of 7.8% in 2011. During the five-year period 2007-2011, Ecuador grew at an average rate of 4.2%, or 0.4% more than the region as a whole (3.8%). While this strong performance can be explained primarily by the behavior of nonoil GDP,³ the country's macroeconomic performance is also linked to the international price of crude oil, through its impact on public finances and the external accounts.
- 1.2 Ecuador is engaged in a profound process of change in its development model, the main thrust of which was laid down in the Constitution adopted in 2008 and in the "Good Life" National Plan 2009-2013 ("Plan Nacional del Buen Vivir 2009-2013"). That model is based on strengthening the role of the State as a driver of the economy and as provider of public goods and services, primarily infrastructure, health, and education.⁴ This model has been implemented with resources from strengthened tax management, oil revenues, domestic savings, and external credit from multilateral sources (IDB and CAF), and increasingly from bilateral sources, in particular the People's Republic of China.
- 1.3 The strong recent economic growth, together with the government's social policies, have brought about a significant reduction in poverty and inequality.⁵ To continue these gains, however, the country must further address the gaps that limit its development potential. On one hand are the constraints on sustainable economic growth that stem from shortfalls in infrastructure, human capital and financial deepening, as well as the country's vulnerability to natural disasters and environmental degradation. On the other hand, there are structural barriers that make it difficult to escape from poverty: these include the persistent unequal access to social protection, quality health and education services, housing, and basic public utility services. These obstacles have a particularly intense impact on the rural sector and on indigenous and Afro-Ecuadorian communities.

II. THE IDB GROUP IN ECUADOR

- 2.1 The Bank has traditionally been one of the country's main sources of international finance. Over the last five years, the Bank's share of the external public debt has risen from 18% to 23.2%, and its weight in total multilateral debt has remained

³ The oil economy represents approximately 15% of GDP. Although in real terms the country's oil GDP has shrunk by around 8.3% over the last five years, during that same time nonoil GDP rose by 28.9%.

⁴ The continuity of these policies could depend on the outcome of the presidential and legislative elections scheduled for February 2013.

⁵ According to the National Employment, Unemployment, and Underemployment Survey of the National Statistics and Census Institute (INEC), the poverty rate as measured by income declined from 38% in 2006 to 28.6% in 2011, while the Gini index fell from 0.512 to 0.44 over that same span of time.

stable at around 44%.⁶ The Bank's activity in the country is in specific areas within a set of sectors that reflect the Bank's positioning and responsiveness in the delivery of technical assistance and institutional support to the State apparatus, in addition to its lending resources. More specifically, the Bank has solidified its status as Ecuador's main multilateral partner in such sectors as rural electrification, housing, health, education, rural land regulation, and risk management. It has also collaborated on a series of knowledge products to benefit the country, and at the same time has conducted technical cooperation (TC) and non-sovereign guaranteed (NSG) operations in support of private sector development, geared primarily to improving the financial services accessed by micro and small enterprises.

- 2.2 In the course of the last country strategy 2008-2011, the IDB approved US\$1.495 billion in sovereign-guaranteed (SG) loans, and portfolio execution was successful.⁷ The active portfolio of SG loans at 30 April 2012 comprised 23 operations for a total amount of US\$1.921 billion, distributed primarily among the following sectors: energy (8.5%), transportation (18.2%), education and health (21.9%), access to finance (2.6%), fiscal management and modernization of the State (19.1%), housing, urban development, and water and sanitation 18%), rural development and natural risk management (7.2%). This portfolio was supplemented by 39 TC operations totaling US\$25.5 million.
- 2.3 The NSG portfolio at 30 April 2012 comprised 46 operations for a total amount of US\$269.7 million,⁸ concentrated in the following areas: transportation (airport infrastructure), financial services, education, and access to services and opportunities in rural and urban fringe areas.

III. THE BANK'S COUNTRY STRATEGY 2012-2017

- 3.1 The objective of this strategy is to contribute to inclusive and sustainable economic development in Ecuador by supporting the country's efforts to overcome the long-term constraints on economic growth and the structural barriers to overcoming poverty. The following lines of action have been identified: (i) infrastructure, to foster the development of domestic and external markets and boost productivity; (ii) human capital, to ensure greater opportunities for income generation and stimulate total factor productivity; and (iii) public management, to adapt the new legal mandates to the needs of the productive sector and social demands. The strategy will capitalize on the close cooperation that the Bank has established with

⁶ During this same time the CAF has increased its activity in the country. Its share of external public debt and multilateral debt rose from 17.6% and 39.4%, respectively, to 23.8% and 45.2%. On the other hand, the weight of Ecuador's debt with the World Bank declined: whereas it represented 6.6% of external public debt and 14.7% of debt to international agencies in 2007, the respective figures for 2011 were 3.7% and 7.1%.

⁷ At the end of 2011, the active loan portfolio grew by 273% with respect to 2008, with record disbursements of US\$393.7 million in the last year.

⁸ This includes seven SCF operations for US\$175 million and 16 IIC operations for a total of US\$79 million. An additional 18 nonreimbursable TCs for US\$8.4 million and four SPs for US\$2.3 million are being executed through the MIF, and US\$5 million operation is being executed through OMJ.

the country in recent years in specific areas within a set of sectors where the principal constraints have been identified.⁹

- 3.2 The areas prioritized in this document reflect the shared priorities of the Government of Ecuador and the IDB, and were the subject of consultation with representatives of civil society. Given the Bank's position as the only multilateral institution active in the country together with the CAF, an intrasector targeting exercise has been conducted within a set of sectors. As a result, the strategy for 2012-2017 will focus on the following sectors: (i) energy; (ii) transportation and logistics; (iii) social development; (iv) access to finance; (v) fiscal management; (vi) urban sustainability; (vii) rural development; and (viii) disaster risk and natural resource management. The topics of diversity and of climate change and environmental sustainability will be addressed as crosscutting issues in this strategy.
- 3.3 The Bank will support knowledge generation and transfer to the country, as well as institution-strengthening, technical assistance and human talent, principally in the priority areas of this strategy. Technical cooperation will focus on supporting, originating, and implementing operations in these areas.

A. Energy

- 3.4 The country's primary energy mix is heavily dependent on fossil fuels, which account for around 87% of domestic energy consumption. In the electric power generation sector, the installed capacity in the National Interconnection System (SNI) at the beginning of 2012 was 4,291 MW. The SNI represents 88% of total effective power, with 50% hydroelectric and 38% thermal. The remaining 12% corresponds to noninterconnected systems. Generating capacity falls short of the demand for electricity, which is projected to grow at an annual pace of 6.5% for the period 2011-2020, even faster than the historical rate of growth in demand over the last 10 years (5.1%).¹⁰ Despite significant gains in recent years, there are also persistent energy efficiency problems in the transmission and distribution stages, where total electricity losses amounted to 15.7% in 2011, higher than the regional average for electricity losses of 10% to 12%. Although electricity service coverage has been extended, there is still room for improvement: the rural coverage rate is 90%, and urban coverage is 97.7%.

⁹ The selected target areas reflect the process of dialogue with the Government of Ecuador and the analysis of the country's principal development constraints and gaps, as illustrated in the electronic link on strategic alignment.

¹⁰ This problem is most acute between October and March, when the flow in the Paute River valley diminishes, requiring recourse to electricity produced by inefficient, outdated and failure-prone thermoelectric power plants. Generally speaking, the hydroelectric plants in operation are concentrated in the valleys where the water volume declines simultaneously in dry seasons, making the power generation matrix vulnerable to fluctuations in river flows.

- 3.5 The power supply deficit is the result of historical low levels of investment, especially in hydrogeneration and other types of alternative energy.¹¹ Technical problems in transmission and management shortcomings¹² in distribution have contributed to the levels of technical and nontechnical losses in the system. The high costs of implementing rural electrification projects has been an obstacle to swifter expansion of electricity coverage.
- 3.6 The Bank's engagement in the sector will support the country in its effort to promote the sustainable increase and diversification of generating capacity, system reliability, energy efficiency, and expanded coverage of electricity service. Priority will be given to interventions that increase hydroelectric generating capacity, using the concept of watershed complementarity to minimize seasonal flow problems and analyzing reliability in the face of extreme hydro-meteorological events. Steps will be taken to enhance energy efficiency in the power transmission and distribution stages, together with electrification projects that increase service coverage in urban fringe and rural areas. The NSG windows will support projects to develop alternative energy sources.
- 3.7 The main risks for the Bank's interventions in the sector have to do with delays in implementing the Electrification Master Plan (PME) in the course of adapting to the new legal framework soon to be approved. These risks will be mitigated by intensifying dialogue with the country and discussing in advance how implementation of the Electrification Master Plan can be made compatible with the new legal system. There are also environmental risks inherent in the scope of hydroelectric projects.¹³ The Bank's ample experience in this sector, together with strict adherence to its social and environmental safeguards policies, will help to mitigate these risks.

B. Transportation and logistics

- 3.8 Average travel times between cities have been shortened with the advances in road infrastructure,¹⁴ but to improve travel times further will require closing the gaps in the existing road infrastructure and any that may appear in the future.¹⁵ Of the

¹¹ Between 2000 and 2006 no new hydroelectric power plant came on stream, and the entire increase in generation capacity was provided by thermal power plants or imported energy. Since that time, generating capacity has been increased through projects such as San Francisco (230 MW), Mazar (170 MW) and Ocaña (26 MW). Between 2012 and 2016, an additional nine hydroelectric stations are expected to begin operation with a combined capacity of 2,779 MW

¹² The technical problems refer primarily to equipment inefficiency and the inadequate caliber of the conductors. Administrative and financial shortcomings result in problems with control processes, low levels of revenue collection, the excessive time needed to locate breakdowns and restore service, and the lack of information on power users, among other issues.

¹³ Glacier recession and the projected changes in precipitation patterns will over the long run influence the quantity of water available for hydroelectric generation, a factor that must be taken into account in assessing the risks associated with hydro projects.

¹⁴ The National Development Plan sets a target of shortening average intercity travel times by 10% by the year 2013.

¹⁵ In 2011 an estimated 22.1% of the national road system was carrying more than 8,000 vehicles per day.

43,762 km in the national road system, 21% is paved, with an estimated deficit of approximately 530 km.¹⁶ Those roads are concentrated in the State network administered by the central government: 92.3% of that network's 8,873 km is paved; 1,365 km (31.8%) is in need of rehabilitation, and ongoing maintenance is required to repair seasonal damage from rains. Furthermore, less than 5% of the provincial and cantonal road network, administered by the decentralized autonomous governments (GADs), is paved.

- 3.9 Road safety conditions are not up to standard. The death rate from traffic accidents is 16.3 per 100,000 inhabitants, and the number of traffic fatalities rose by 8.9% on average between 2008 and 2010. This situation is blamed primarily on lax enforcement of traffic signal rules and regulations, inadequate driver training and licensing (approved criteria), and poor road signage and signals.
- 3.10 Logistical obstacles have also been identified that undermine the competitiveness of Ecuador's productive sector. These include the shortage of specialized logistics platforms, the lack of security in certain links of the logistics chain, risks of cargo contamination, and delays and congestion in the removal of containers. There are also problems with the intermodal connection of passengers and freight between highways, ports, airports, border crossings, logistics centers, and waterways that affect domestic and regional trade.
- 3.11 In the roads subsector, the Bank's interventions will be targeted to support the country through expansion of the national road system and rehabilitation and maintenance of highways, incorporating safety, audits, and driver education, environmental sustainability, and adaptation to future changes in the intensity or frequency of extreme weather events.¹⁷ This support must include the GADs, which administer 80% of the road system (the provincial and cantonal portions) despite their lesser capacity for strategic planning. In the logistics subsector, interventions will target:¹⁸ (i) support for logistics platforms that will improve distribution processes and lower costs in the supply chain; (ii) support for regional integration by promoting the Amazon and Andean intermodal hubs¹⁹ and border crossings prioritized in the COSIPLAN agenda.²⁰

¹⁶ The source for data on national road system length is the Ministry of Transportation and Public Works (MTO). This deficit is calculated as the gap that must be bridged to achieve a regional development target of 0.038 paved kilometers per square kilometer.

¹⁷ The Bank's Regional Environmentally Sustainable Transport (REST) strategy and action plan will be taken into account here.

¹⁸ In addition, dialogue will be encouraged with key stakeholders to explore opportunities for private sector participation in ports and highways.

¹⁹ These intermodal hubs interconnect different modes of transportation including river, sea, and air.

²⁰ The South American Infrastructure and Planning Council (COSIPLAN) sponsors 31 priority projects for Latin American integration, of which Ecuador is participating in three: (i) the Peru-Ecuador border interconnection and the Caracas-Bogotá-Quito corridor; (ii) the Colombia-Ecuador border interconnection; and (iii) northeasterly access to the Amazon River.

- 3.12 Despite the significant gains made in this area over the last few years, the main risk is the still insufficient institutional and planning capability and the resulting difficulties in developing and consolidating sector policies. There is also still uncertainty about the mechanisms for private sector participation. To mitigate those risks, projects will include an institutional strengthening and technical assistance component, and the mechanism for managing private sector participation will be improved.

C. Social development

- 3.13 Despite the great improvements made at the aggregate level in recent years,²¹ poverty levels as measured by unmet basic needs were still high in Ecuador at the end of 2010, especially among the most vulnerable groups, e.g. indigenous (77.2%) and Afrodescendent communities (47.2%), and in rural areas (72.2%). The persistence of this pattern reflects the structural barriers to escape from poverty that promote its intergenerational transmission. The combined effect of failings in the social protection system and unequal access to quality health and education services contribute to this vicious circle, increasing the likelihood that children and youths from the poorest families will suffer from chronic malnutrition, inadequate childhood development, insufficient investment in human capital, and risky behaviors that will affect them throughout their lives.²²
- 3.14 Between 2006 and 2010 the public budget for the social sector was increased from 4.6% to 8.2% of GDP, and progress was made in overcoming the fragmentation and scattering of public investment that had historically characterized the sector. Yet important challenges remain to solidify the territorial management and planning model that dictates and coordinates the delivery of social services. There is also a need for sufficient monitoring and follow-up to address the needs of families in an integrated manner and to overcome the lack of information that has on occasion made it difficult to renew and target social protection policies. Moreover, despite the substantial participation of poor families in early childhood

²¹ Between 2005 and 2010 poverty, as measured by unmet basic needs, declined from 51.6% to 41.8%, and extreme poverty from 25.8% to 16.6%. During that same time, poverty as measured by income fell from 42.2% to 32.8%, and extreme poverty from 21.6% to 13.1%.

²² There is empirical evidence that children living in the poorest homes are more likely to suffer chronic malnutrition, which affects 43.6% of children living in extreme poverty, and 28.3% of those living in poverty. Moreover, in comparison to the less poor, the poorest children are already one year behind in their cognitive development at age 6, a gap that translates into poor school performance (measured by grade promotion and performance on reading and mathematics tests). The school attendance rate for the poor rural population falls off sharply after age 12, while the fertility rate for teenagers living in extreme poverty is nearly double the rate for those not living in extreme poverty.

development programs in Ecuador, there are shortcomings in the quality of services that limit their impact on the cognitive and physical development of children.²³

- 3.15 In education, the government has been making a major effort to increase the coverage and equity of the system and to improve the quality of teaching. The net enrollment ratio for basic education rose from 91.1% in 2006 to 94.8% in 2010, during which time the enrollment gap between the average for the population as a whole and the indigenous and Afrodescendent communities was reduced by 2.2% and 2.5% respectively. Nevertheless, early education remains a great challenge: only one in four 3- and 4-year-olds attends a specialized education center, a situation that contributes to cognitive delay and diminishes future school performance for the most disadvantaged groups. Toward the end of the education cycle, at the baccalaureate level, the challenge is to keep young people in school, since despite recent progress the net enrollment rate at this level is still only 55%.²⁴ The quality of education is another issue, as demonstrated by the poor results on standardized tests, both national and international.²⁵
- 3.16 The epidemiological profile of the Ecuadorian population reflects the double burden of illness, with the persistence of infectious diseases and mother/child health problems typical of developing countries and the simultaneous increase in chronic and degenerative diseases that affect wealthier societies. Although the infant and under-5 mortality rates (18 and 20 per 1000 inhabitants) were close to the average levels for Latin America in September 2011, the maternal death rate (110 per 100,000 live births) is cause for concern.²⁶ Chronic or transmissible diseases are responsible for nearly half of premature deaths, the main causes of which are malignant tumors, followed by cerebrovascular diseases, ischemic heart disease, and diabetes. In nutrition, the main challenges are stunted growth and a rising tendency toward overweight among children, overweight and obesity in women of childbearing age, and iron-deficiency anemia both in children under 2 years and in women of childbearing age.

²³ In 2008, 36% of children attending the “Good Life” Early Childhood Centers were suffering from chronic malnutrition, 57% were anemic, and only 17% of those under 6 years in these programs showed cognitive development appropriate for their age. It should be noted, however, that this study was restricted to certain provinces and was conducted just before a number of actions were undertaken to improve the quality of early childhood development services.

²⁴ Moreover, in contrast to the situation in basic education, the indigenous and Afrodescendent gap vis-à-vis the rest of the population at the baccalaureate level has scarcely been reduced: the net enrollment rate of these two communities was only 28% and 29%, respectively.

²⁵ For example, on the test for the 2006 Second Regional Comparative and Explanatory Study (SERCE) conducted among pupils in grades 3 and 6, Ecuador received a median score significantly below the average for all participating countries, in both language and mathematics.

²⁶ Unlike the indicator shown in the Results Matrix, these child and maternal mortality figures come from the United Nations Observatory on the millennium Development Goals. Although based on official sources, their values are slightly higher than reported by the Ecuadorian authorities (under-5 mortality rate 15; infant mortality rate 11; maternal mortality rate 66.8). This is because the United Nations applies methodological criteria to ensure that the indicators it uses are comparable internationally, which may lead to discrepancies with national data.

- 3.17 Despite the government's efforts, the national health system is still suffering the consequences of historically low investment levels and shortcomings both in specific programs and in general policies that especially affect the most disadvantaged communities. More specifically, limited treatment capabilities and quality are apparent in public services, related to the poor state of infrastructure and facilities of the Health Ministry's line units, the distribution of human resources, and the inadequate allocation of resources for preventive care. Another challenge has to do with introducing an information system that will allow the collection and analysis of essential data on the epidemiological profile of the population and on the quality, efficiency, cost, and equity of health services.
- 3.18 The Bank's engagement in the social sector is intended to support the country in addressing the factors underlying the intergenerational transmission of poverty in Ecuador, through interventions in the following areas: (i) construct an Integrated Social Promotion and Protection System, with the emphasis on expanding and coordinating social services in poor areas and on supporting at-risk youth; (ii) expand the coverage and improve the quality of early childhood development services and combat malnutrition among the poorest children; (iii) bring more pupils into the education system, especially at the early childhood level and baccalaureate level, and in those parishes with the greatest education shortages; (iv) increase access to health services, to address the double burden of disease; (v) implement the new Comprehensive Healthcare Model and establish the Public Health Care Network, including development of the system's regulatory and oversight framework;²⁷ and (vi) strengthen the sector lead agencies.²⁸ In recognition of the multidimensional nature of this problem and of the synergies and complementarities among these lines of action, the Bank's interventions in the social sector will take a comprehensive approach whenever possible in order to maximize their impact. Additionally, NSG support by the Bank will take the form of interventions to support the expansion of coverage in higher education and access to quality health care services.
- 3.19 The main risk in this sector is that the lead agencies may have limited institutional capacity to move forward with the various reforms simultaneously in a context where there is not always a sufficient delimitation of responsibilities and some stakeholders are opposed to change. Another risk derives from the frequent turnover of staff and authorities in the sector, which hinders continuity and speed in implementing the reforms under way. To mitigate these risks, special attention will

²⁷ In this area, steps will be taken to strengthen treatment capabilities at the primary and basic secondary level of health care, as well as the health programs and the intercultural adaptation of care.

²⁸ In education, the emphasis will be on strengthening the new school management model by promoting: (i) development of a new pedagogical leadership among the system's directors; (ii) pedagogical coaching for new teachers entering the school system; (iii) strengthening of the assessment capacities of the education system's managers. In health care, the Ministry of Public Health will be strengthened, with emphasis on the collection, use, and exchange of information for sector trend analysis, monitoring, and evaluation, as well as on support for implementation of the new management model and the development of capacities in key areas within the ministry, at the central and deconcentrated levels.

be paid to institutional and operational strengthening of the sector, as well as to the development of effective communication strategies.

D. Access to finance

- 3.20 Although in recent years have seen significant progress in access by the population to banking services, often referred to as “bancarización,”²⁹ the indicators of financial deepening are still below the averages for Latin America, and very far from those seen in the Asian and industrialized countries. Levels of access to financial services are also inadequate, with only three bank branches and 12.8 ATMs for every 100,000 inhabitants, well below the regional medians of 14.1 and 14 respectively. There are also significant inequities, with access to such services much more limited among the low-income population and in some provinces, primarily on the coast and in the East.³⁰
- 3.21 The legal and institutional restructuring of the sector recently undertaken by the authorities is an important step toward correcting the weaknesses that have characterized the actors in the cooperative financial sector serving low-income groups, known as the “popular and solidarity-based economy.”³¹ Yet there are still significant challenges to the continued promotion of financial inclusion. The high costs faced by institutions in expanding their base of operation to the more remote areas of the country make it difficult to reduce the concentration of financial infrastructure in certain provinces, whereas the mandatory caps on interest rates may have served to restrict access to credit for poor families and small businesses with a high risk profile. There is also room for strengthening the infrastructure, structures and mechanisms for clearance and settlement, the oversight function, and the legal framework of the National Payments System administered by the Central Bank.
- 3.22 The Bank’s engagement in the sector is intended to support the country in addressing the problem of financial exclusion, with interventions at three levels: (i) at the macro level, policy changes will be supported to promote financial inclusion and protect the stability and sustainability of the financial system, in order to safeguard the interests of the user population, especially the most vulnerable groups; (ii) at the meso level, the financial architecture will be strengthened with special attention to the National Payments System, to make it more inclusive and efficient and offer financial services in the more remote geographic areas; (iii) at the micro level, direct support will be given to service providers through targeted interventions to increase access to financial services for lower-income people living

²⁹ The “bancarización” index, which is the ratio of the number of depositors to the total population, rose from 39% to 74% between 2001 and September 2011.

³⁰ For example, the percentage of the population belonging to the four poorest deciles with access to savings deposits is 6.5%, while for the four wealthiest deciles it is 20.8%.

³¹ The recently approved law governing the popular and solidarity-based economy and financial sector calls for creation of a “Superintendency of the Popular and Solidarity-based Economy,” one objective of which is to promote these entities.

in areas with less financial deepening, such as programs to expand the network of points of sale, direct support for the creation of specialized products, or institution-strengthening. The NSG windows will also continue supporting the financial sector through the banking institutions and structures for financing and investment in capital markets.

- 3.23 One of the main risks for this sector has to do with the regulatory and institutional restructuring underway in the cooperative financial sector serving low-income groups, and with the possibility that the sector's lead agencies will reveal weaknesses that impede achievement of the Bank's objectives and programs, especially during the early years. To mitigate this risk, Bank operations will include technical support and close programmatic and sector dialogue, for which there is a roundtable for public-private dialogue on access to finance.

E. Fiscal management

- 3.24 With approval of the new National Constitution in 2008, the government launched a far-reaching process of reorganizing the State, with the consolidation of planning as a public management instrument and decentralization and deconcentration of the State as top priorities.³² These reforms have produced some positive results in the fiscal area, including an increase in tax revenue intake of 2.8% of GDP over the last five years and a larger share of direct taxes in total revenues. Yet certain challenges remain for achieving more efficient management of public resources. On the revenue side, there is still great dependency on oil revenues, which in 2011 represented 41% of total revenues of the nonfinancial public sector (NFPS). Moreover, while the tax evasion rate has fallen sharply in recent years, it is still relatively high: 40% for income tax and value-added tax (VAT) in 2011. On the expenditure side, there is room to improve the targeting of certain subsidies,³³ budget allocation mechanisms, incentives for efficiency and effectiveness in public management, and the instruments whereby the public sector identifies, prioritizes, and assesses the viability of its investments.³⁴ Lastly, the decentralized autonomous governments (GADs) need further strengthening to facilitate the transfer of responsibilities resulting from this process of decentralization.

³² The principal reforms pursued are: (i) designation of the National Planning and Development Secretariat (SENPLADES) as the agency responsible for planning and programming of public investment; (ii) approval of the Code of Planning and Public Finance (COPYFP), which organizes and governs the planning system and links it to the national public finance system of, thus regulating the functioning of the various levels of the public sector; (iii) approval of the Code of Territorial Planning, Autonomy, and Decentralization (COOTAD), redefining the fiscal relationship between the central government and the decentralized autonomous governments (GADs), which will have to generate their own resources as part of the State and share their revenues in accordance with the principles of subsidiarity, solidarity, and territorial equity.

³³ Whereas the poorest quintile receives 17% of transfers (social spending and energy subsidies), the richest quintile receives 21%.

³⁴ The fact that around 70% of investment projects under the Annual Investment Plan (PAI) enter without preinvestment studies helps to explain the performance and execution problems of 34% of projects.

- 3.25 The Bank's strategy will focus on supporting the government in implementing its new fiscal management framework through interventions designed to: (i) move toward a more efficient and progressive tax system with emphasis on direct taxation; (ii) enhance the equity and efficiency of public spending and raise the quality of the public investment cycle at all levels of government; (iii) strengthen and coordinate planning processes with the budgetary cycle and promote the use of evaluations for implementing a comprehensive system of results-based management at the national and subnational levels.
- 3.26 The main risk identified for the fiscal sector has to do with the challenges to be faced by the authorities in carrying out their ambitious agenda of reforms, in a context of multiple stakeholders with different objectives and interests, which will hinder implementation of the mandates in the Code of Planning and Public Finance (COPYFP) and the Code of Territorial Planning, Autonomy, and Decentralization (COOTAD). To mitigate this, the Bank will need to maintain and intensify the sector strategic dialogue with the authorities of the Ministry of Finance, the National Planning and Development Secretariat (SENPLADES), and other agencies involved in the sector, in order to ensure timely interventions with high value-added that respond to international best practices.

F. Urban sustainability

- 3.27 Although Ecuador has made significant gains in housing over the last decade, 21.7% of families are still living in overcrowded conditions, and 12.7% of dwellings are of substandard construction.³⁵ Approximately 70% of dwellings are built by the informal sector without regard to construction standards. The increasing pressure exerted by the urbanization process has added to this state of affairs. On the one hand, that pressure has given rise to informal settlements with limited access to basic public services and dwellings built from makeshift materials that make them particularly vulnerable to fire, natural disasters, and dangers to personal safety. On the other hand, as growth in the major cities has shifted economic activity into new urban hubs, the older city centers have declined, leading to the destruction or abandonment of the country's cultural heritage assets, many of which are not properly registered, preserved, or developed. Another factor underlying these urban dynamics is the weakness of the various public agencies responsible for them, which lack interagency coordination mechanisms, territorial planning and administration tools, and effective instruments for results-based management.
- 3.28 In urban areas the coverage rates for water and sewer services are 86.8% and 71%, respectively, but these figures conceal great discrepancies, and access is much more limited among the poor population.³⁶ These inequities are also apparent in solid waste collection, where coverage is 84.2% for urban areas as a whole but much

³⁵ According to census data, these figures were 26.3% and 23.5%, respectively, in 2001.

³⁶ An assessment conducted by the Pan American Health Organization in 2011 found that for the wealthiest urban quintile the coverage rate of home water and sanitation connections exceeded 95%, whereas for the poorest quintile the coverage was only 66% for water and 40% for sanitation.

- lower in the poorer neighborhoods and informal settlements, giving rise to urban “microdumps” and the burning of garbage. Notable among the factors underlying these shortcomings are the lack of orderly planning on the part of State institutions and the absence of clear criteria for targeting public resources, the absence of standards for measuring and controlling the quality of services, financial and staffing weaknesses at the relevant agencies and municipal institutions, and the absence of a legal framework that delimits the responsibilities for policy formulation, regulation, oversight, and management of services.
- 3.29 The use of public means of urban transportation is declining. In the Metropolitan District of Quito, this proportion has sunk from 80% in 1998 to 62.4% in 2009, and it is anticipated that, with no changes to the current mobility system, it will continue sinking to 59% in 2025. This trend is producing a sharp increase in congestion and in average travel times, which in turn is exacerbating environmental pollution and emissions levels, raising transport costs for productive activities, and worsening the quality of life of citizens. The main factors behind this trend are urban expansion, more vehicles on the road, poor organization and management of conventional transportation routes, and the insufficiency of existing mass transit corridors.
- 3.30 The Bank’s interventions in the urban sustainability sector will focus on the following areas: (i) strengthen the sector public agencies and service providers at the national and local levels by encouraging the development and adoption of territorial and land-use planning tools and coherent and comprehensive regulatory frameworks; (ii) encourage the generation of urbanized land at low cost and conduct urban development operations that allow the authorities to address the problem of informal settlements; (iii) support the construction of low-income housing with an emphasis on urban and periurban areas; (iv) contribute to the comprehensive improvement of neighborhoods and the revival of downtown urban areas, including the registration, rehabilitation, and restoration of heritage assets; (v) support investments to expand the coverage of water, sewer, and solid waste management services, with priority to underserved areas; (vi) support improvements in the capacity, speed, and comfort of public mass transit in Quito and the country’s principal cities, giving priority to adoption of an integrated system based on planning and land use management and on interactions between sustainable transportation and mobility. Lastly, the Bank will promote a comprehensive approach to sustainable, low-carbon urban development similar to the one proposed in the Sustainable Emerging Cities Initiative.³⁷
- 3.31 The main risks for Bank interventions in urban sustainability have to do with institutional factors and the fragmentation of roles and responsibilities, which hinders cooperation among the various sector public agencies at the different levels of government, threatening the sustainability of interventions and obstructing the

³⁷ This activity falls under the recently approved “Special Program of the Multidonor Fund for the Sustainable Emerging Cities Initiative.” The Bank’s activity in this crosscutting theme of the strategy will focus on the initiative’s three areas of: (i) environmental sustainability and climate change; (ii) sustainable urban development; and (iii) fiscal sustainability and governance.

implementation of national policies, when they exist. To mitigate these risks, the Bank will maintain ongoing and proactive dialogue with the sector lead agencies and with service providers, supporting the national government's efforts to strengthen the sector legal frameworks and develop policies and programs.

G. Rural development

- 3.32 Accounting for 9% of GDP (18%, if agroindustry is included) and 26% of the economically active population, agriculture is key to development of the rural sector, where the proportion of the population living in poverty (53% in 2010) remains far higher than in urban settings. In terms both of products for export and those destined for the domestic market, the yields in agriculture and forestry are low in comparison to other countries of the region, a situation that affects small and medium-size producers in particular. This is explained essentially by the following factors: (i) low levels of generation, transfer, and adoption of modern agricultural technologies and practices in rural areas;³⁸ (ii) sanitation problems and vulnerability to pests and diseases; (iii) inequality and informality in land tenure,³⁹ and poorly functioning markets for land; (iv) insufficient irrigation infrastructure and its poor condition, covering only an estimated 30% of the land area devoted to annual crops; (v) scarcity of credit, to which only 7.3% of farmers had access in 2000.⁴⁰
- 3.33 Given Ecuador's natural resource endowment, rural tourism is a nonagricultural activity with great potential for generating higher incomes, especially in areas with no comparative advantage in farming. The Galapagos Islands are a prime example where this approach could improve the socioeconomic and environmental impacts of tourism. Yet the archipelago's natural resources have tended to degrade in recent years, due mainly to three factors: (i) the growing number of tourists,⁴¹ which has not been accompanied by a concomitant increase in capacity for accommodating them; (ii) overfishing of the most profitable species; and (iii) poor land-use planning in the face of a resident population that is growing by around 6% a year, and exceeded 25,000 in 2010.
- 3.34 The main objectives of the Bank's engagement in the rural sector are to support the country in improving productivity for small and medium-scale farmers and generating nonfarm employment and incomes through sustainable use of the natural resource endowment (including forests and biodiversity) and the coastline. Accordingly, the work areas included in this strategy are: (i) boost the competitiveness of agriculture and forestry by promoting technological innovations and offering incentives for applying them in the field; (ii) improve standards for plant and animal health and food safety; (iii) support development of land markets and strengthen and clarify land ownership rights to promote rural investment; (iv) support irrigation development and its sustainable management, with due

³⁸ Fewer than 10% of farmers use certified seed, have machinery, or receive onsite technical assistance

³⁹ The Gini coefficient for land ownership is 0.8 in Ecuador, compared to a world average of 0.6.

⁴⁰ This percentage is likely higher now, thanks to the expansion of lending programs by public banks.

⁴¹ Visitor arrivals rose from 68,989 in 2010 to 185,028 in 2011.

regard to shifting precipitation patterns; (v) support conservation of the natural heritage and biodiversity of the Galapagos Islands, and contribute to their sustainable use through comprehensive management of tourism and land-use planning that will contribute to the planned development of basic infrastructure and will reduce pressure on natural resources. NSG support to the private sector will focus on projects to bring small producers into the supply chains for both domestic and export markets.

- 3.35 The main risks have to do with the sector's institutional instability and its impact on the capacity to deliver projects on schedule. In the case of the Galapagos, the risks to be considered relate to the institutional and coordination capacity of the executing agencies and the opposition from certain private interests, primarily in the fishing and tourism industries. To mitigate these risks, the Bank will make close dialogue with the authorities and executing agencies a top priority, and put an emphasis on analysis and planning of the institutional aspects of operations. It will also work to identify the stakeholders involved and their interests, so that these can be factored into the operation design.

H. Natural disaster risk management

- 3.36 Between 1900 and 2009 Ecuador was struck by 65 large-scale disasters that caused more than 13,000 deaths and affected 3.6 million people. The direct physical damage caused by seismic events during this time is estimated at US\$1.535 billion, while total economic losses associated with the El Niño phenomenon (1982-1983 and 1997-1998) were around US\$3.9 billion. Of all the events that caused emergencies or disasters between 1970 and 2007, 68% were climate-related. If an extreme event occurred, the projected cost to Ecuador in loss of public infrastructure could be as high as US\$2.7 billion. In the most recent application of the risk management index (RMI), which measures the country's performance in the main aspects of disaster risk management (DRM), Ecuador scored 26.75 out of 100, corresponding to an "incipient" performance level (IDB, 2010).
- 3.37 Despite some recent progress in the area of governance,⁴² Ecuador does not have legislation to structure the National Decentralized System of Risk Management (SNDGR). Development of that law and its implementing regulations, along with strengthening of the associated institutions, are important challenges for the coming years. In terms of prevention, efforts to incorporate DRM into the education system are just getting under way, and disaster preparedness at the community and municipal level is often inadequate. Moreover, the limitations of the monitoring mechanisms handicap DRM planning, with the shortcomings especially pronounced when it comes to analyzing specific risks such as landslides and local vulnerabilities. DRM has yet to be built into the Territorial Development and Land-Use Plans (PDOTs). In terms of disaster management, there are weaknesses in emergency response resulting from lack of institutional coordination and not enough training and equipment for the response teams.

⁴² The National Risk Management Secretariat (SNGR) was created in 2009, with ministerial rank.

- 3.38 The Bank's engagement in DRM is intended to help the country reduce the vulnerability of population groups exposed to natural threats by strengthening the SNDGR, specifically through the following actions: (i) strengthen DRM governance, both at the national level through consolidation and institutionalization of the regulatory framework, and at the municipal level through implementation of that framework; (ii) promote a culture of prevention through training at the community level and in schools; (iii) analyze the risk of landslides in the most vulnerable municipios, incorporating this information into the PDOTs, and build risk mitigation works at the local level; (iv) strengthen emergency response capability through institutional strengthening, infrastructure provision,⁴³ and preparedness activities at the national and local levels.
- 3.39 The main risks associated with this sector are institutional weaknesses and the lack of interagency coordination. These weaknesses stem from the still-incipient process of consolidating the SNDGR at the national level and from the transition of the SNDGR from the national to the local level. To mitigate these risks, institutional strengthening actions will be pursued nationally and locally.

Crosscutting issues

I. Diversity

- 3.40 The socioeconomic indicators for the indigenous and Afrodescendent population remain significantly worse than for the rest of the population. Compared to a national average of 32.8% (41.8%, if measured by unmet basic needs), poverty indexes are as high as 65.8% for indigenous and 38.5% for Afrodescendent people (77.2% and 47.4%, if measured by unmet basic needs). These gaps have multiple causes, some of which are related to the priority sectors in this strategy: (i) informality of land tenure and the consequent vulnerability to appropriation and exploitation of the resources associated with that land; (ii) less access to basic services, mainly water and sanitation;⁴⁴ (iii) lower quality and coverage of education;⁴⁵ (iv) unequal access to health care, especially maternity services.⁴⁶
- 3.41 The Bank will take a crosscutting approach to the problems affecting indigenous and Afro-Ecuadorian peoples, with the emphasis in the following areas: (i) expand the coverage of basic services to these groups; (ii) extend education coverage in

⁴³ For example, support for firefighter stations.

⁴⁴ Whereas the coverage rates for water and sanitation services are 78.5% and 66.6%, respectively, among the white population, the rates for the indigenous population are 42.9% and 27.7%, and the rates for the Afrodescendent population are 73.8% and 52.9%.

⁴⁵ The illiteracy rate among the indigenous population is 25%, whereas it is 7.3% and 6.8%, respectively, among the Afrodescendent and mestizo populations. The national average is 8.2 years of schooling, but for indigenous peoples it is 4.2 years, and for Afro-Ecuadorians, 7.3 years.

⁴⁶ Whereas 93% of Ecuadorian women receive some type of professional assistance during childbirth, this proportion falls to 55% for indigenous women. This contributes to the fact that, according to the 2001 census, indigenous children are twice as likely to die in their first year of life as children of other ethnicities.

rural areas with large indigenous and Afrodescendent populations; (iii) improve access to health care services for indigenous and Afro-Ecuadorian communities.

J. Climate change and environmental sustainability

- 3.42 Between 1970 and 2007 Ecuador saw a gradual increase in the number of anomalous climate events, which are the cause of more than two thirds of all the disasters that strike the country and are associated with 78% of deaths and 84% of dwellings destroyed and/or damaged. In addition, between 1990 and 2006 greenhouse gas emissions rose by 55%, attributable primarily to the energy sector, transportation, and the conversion of forests to farming and other productive uses. The lack of a consistent climate change mitigation and adaptation strategy has aggravated the impact of these phenomena and trends. Contributing factors are the weak institutional capacity of the main actors, insufficient intersector coordination among them, and lack of basic information and analysis on vulnerability and risk and on cost-effective options for mitigation and adaptation.
- 3.43 In energy, transportation and logistics, fiscal management, urban sustainability, rural development, and natural disaster risk management the Bank has identified the following areas for possible support: (i) close the knowledge and information gaps; (ii) strengthen the institutional capacity of the main public and private actors in the sector, at both the national and subnational levels; (iii) promote initiatives to reduce vulnerability and encourage adaptation, mitigation of greenhouse gases, and sustainable management of agricultural systems, forests, and biodiversity; (iv) support territorial and land-use planning and other measures required to strengthen mitigation, adaptation, and reduction of vulnerability to climate change; (v) adopt energy efficiency measures and promote low-emissions energy sources in housing and transportation. The NSG windows will support the crosscutting area of environmental sustainability through “green lines” for financing projects with a positive environmental impact, particularly as they relate to climate change and the reduction of greenhouse gas emissions.

K. Areas of dialogue

- 3.44 The dialogue and knowledge support areas will include: (i) competitiveness and innovation, primarily on issues of promoting private sector investment in innovation and entrepreneurship; (ii) labor markets, on issues of efficiency, pensions, and informality; (iii) citizen security, on issues of achieving higher levels of public safety and violence prevention.

IV. LENDING FRAMEWORK

- 4.1 The lending framework assumes average annual approvals of US\$350 million, or US\$2.1 billion for the period 2012-2017.⁴⁷ This scenario projects a positive average net capital flow for the country of US\$198 million, consistent with an increase in

⁴⁷ The financial and nonfinancial terms of each loan contract will be negotiated, case by case, for each project between the IDB and the Government of Ecuador.

the Bank's share of multilateral debt⁴⁸ from 45% to 48%, a reduction of multilateral debt as a fraction of total external debt from 42% to 25%, and a constant balance of 3.5% of GDP for the country's debt with the Bank.

- 4.2 The lending framework for the period 2012-2017 was determined by projecting an average economic growth rate of 4.1%, average annual growth of 6% in outstanding multilateral debt, average growth of 17% in external debt, and an average public deficit of 3.8% of GDP.
- 4.3 The macroeconomic assumptions and the lending framework for this strategy are consistent with the macroeconomic projections and the financing strategy established in the "Medium-Term Macroeconomic Scenario" and "Four-Year Fiscal Program" prepared by the Ministry of Finance of Ecuador.⁴⁹ The country's execution capacity was also considered in determining the lending scenario.

The Bank's Country Strategy with Ecuador 2012-2017
Lending Scenario
(in US\$ millions)

	2012	2013	2014	2015	2016	2017	Average
Approvals	250	410	360	360	360	360	350
a) Disbursements	350	350	380	380	380	380	370
b) Repayment (principal)	157	159	173	165	177	201	172
Net capital flow (a-b)	193	191	207	215	203	179	198
c) Interest and fees	84	82	78	73	68	62	75
d) Total repayment (b+c)	241	241	251	238	245	263	246
Net cash flow (a-d)	109	109	129	142	135	117	124
Total external debt/GDP	18.7%	21.4%	23.5%	25.3%	27.4%	28.8%	24.2%
Multilateral debt/Total external debt	42.1%	36.0%	32.3%	29.9%	26.9%	24.8%	32.0%
Balance of debt outstanding with IDB	2,523	2,714	2,921	3,136	3,340	3,518	3,025
IDB debt/GDP	3.5%	3.5%	3.5%	3.5%	3.5%	3.4%	3.5%
IDB debt/Total external debt	18.9%	16.4%	14.9%	14.0%	12.7%	11.8%	14.8%
IDB debt/Multilateral debt	44.8%	45.5%	46.2%	46.8%	47.3%	47.7%	46.4%

V. STRATEGY IMPLEMENTATION

- 5.1 In order to implement this strategy and achieve the expected outcomes, interventions in the areas of social development and urban sustainability may be of

⁴⁸ The lending framework assumes that the IDB and the CAF are the only multilateral institutions that would maintain growing debt balances with Ecuador in the period under consideration. It also assumes that CAF disbursements could slow during this strategy period with respect to the past, since Ecuador represents a substantial fraction of its portfolio (17%) in comparison with other member countries. Although the IDB's share of multilateral debt would increase, that debt would decline as a fraction of total external debt, given recent trends and the country's external financing requirements.

⁴⁹ For the period 2012-2015, the government projects average annual financing requirements of 6.6% of GDP, covered essentially with external resources.

a multisector nature, designed in a coordinated manner with simultaneous actions in several different areas of development to leverage the complementarity and synergies among them. To ensure effective inclusion of the crosscutting issues of climate change and environmental sustainability and diversity, the Bank will build them into the programmatic dialogue and the design of the specific operations. In the energy (hydroelectric generation) and transportation sectors, in particular, the country's environmental systems will be supported, so as to anticipate and attempt to mitigate the potential impact that Bank-financed projects might have on the communities involved.

- 5.2 The Bank's experience and track record on operations with subnational governments have been successful in Ecuador. In order to channel resources to a greater number of municipios, the Bank will work with Banco del Estado as executing agency.
- 5.3 The Bank will continue to support the system for monitoring executing agencies, sponsored by the Ministry of Finance, in order to solidify the processes and practices that have led to substantial improvement in the execution of operations.⁵⁰

A. Country system

- 5.4 In the procurement and contracting area, the Government of Ecuador evaluated its National Public Contracting System (SNCP) using the OECD/DAC methodology in 2011 with Bank support. The final report of that evaluation was approved by the government and published on the official public procurement website. The report identified challenges related to strengthening the following aspects of the SNCP: (i) oversight system; (ii) protest mechanisms; (iii) integration with the financial management system; and (iv) single system. The government is currently weighing implementation of a first generation of reforms identified during the evaluation, and the National Public Contracting Institute (INCOP) is developing a strategic institutional plan for the period 2012-2015 with Bank support.
- 5.5 At the request of the Government of Ecuador, the Bank is exploring the possibility of using country procurement systems on Bank-financed operations. That analysis is being conducted in accordance with the terms and procedures established in the "Guide for Acceptance of the Use of Country Procurement Systems" (document GN-2538-6).
- 5.6 In terms of public financial management, the government has developed a strategic plan for modernizing the administration, one that includes the development and implementation of a new public financial administration law, development and implementation of the National Public Finance System (SINFIP), and strengthening of human resources, as well as the Integrated Financial Management System (SIGEF). The Bank has worked in close coordination with the Ministry of Finance to consolidate use of the e-SIGEF system for management of Bank-financed

⁵⁰ For a description of these processes and practices, see the document "Herramientas y modalidades de ejecución en Ecuador" [Execution tools and modalities in Ecuador].

- operations of the central government. In this respect, the Bank is supporting the strengthening of the accounting and reports subsystem through technical consulting engagements, with a view to expanding its use to all projects financed with external resources. The progress made allows use of the budget and cash management subsystems for executing Bank operations, and greater use could be made of the accounting and reporting subsystem during the period of this strategy.
- 5.7 In terms of government oversight, the Bank has worked with the Office of the Comptroller General (CGE), which directs the internal and external government oversight system, to evaluate technical aspects of that institution. The evaluation found that the CGE has a medium level of development, with important challenges looking forward and areas in need of technical and professional development, supported by institutional strengthening activities. The Bank is currently working together with the CGE to design a plan of action that would lead to institutional strengthening and enable future use of the government internal audit and external control function in Bank operations.
- B. Coordination with other development partners**
- 5.8 The Government of Ecuador is closely coordinating the work of its development partners, primarily through the Technical Secretariat for International Cooperation (SETECI), National Planning and Development Secretariat (SENPLADES), and Ministry of Finance. To encourage coordination and dialogue with respect to nonreimbursable resources, SETECI has established a Global Dialogue Forum that involves most of the institutions operating in the country. In addition to the thematic discussion groups being identified by SETECI, there have been a number of initiatives to foster coordination at the sector level. For example, the Economic Fabric Roundtable (“Mesa de Tejido Económico”), in which the IDB participates, brings together representatives of international donors and various government agencies for regular discussion of issues relating to productive development and financial inclusion. Donors also meet periodically to address the issue of risk management.
- 5.9 In addition to the coordination mechanisms described above, the Bank maintains ongoing communication with other entities in order to avoid duplication, exploit synergies, and maximize the effectiveness of its interventions. As the CAF is, together with the Bank, the principal multilateral partner of Ecuador, coordination with that institution has been particularly important in the preparation of transportation, energy, and housing operations. The Bank has also worked closely with the Spanish cooperation agency (on the rural water and sanitation infrastructure program), with USAID (on support for the small-scale coastal fishery), and with the European Investment Bank (on the Quito Metro), among others. This coordination effort will be pursued during the period of the new strategy.

VI. RISKS

- 6.1 Despite its strong recent macroeconomic performance, Ecuador could be adversely affected by a downturn in oil prices. It cannot be ruled out, therefore, that with a deterioration in the economy's external conditions, the demand for financing could exceed that forecast in the financial flow scenarios of this strategy. To mitigate this risk, the Bank will continue to support development of the nonoil economy, and in this way contribute to a gradual reduction in the country's exposure to volatile commodity prices. The Bank's economic monitoring instruments will also be used to track this risk.⁵¹
- 6.2 Another risk is the weak institutional capacity in some areas of the public sector as well as insufficient coordination among the different levels of government, which could affect execution of some projects. This weakness is attributable in part to the frequent turnover of staff, the fragmentation of roles and responsibilities, and the difficulty in advancing simultaneously on the multiple reforms undertaken by the government. To mitigate this risk, the Bank will continue to give priority to close dialogue with the authorities, joint supervision of operations, and the inclusion of institutional strengthening components in its interventions.
- 6.3 Presidential and legislative elections will be held in February 2013, so there is a risk that the shared priorities of the IDB and the government may shift. To mitigate this risk, the strategy has focused on target areas where there is a broad national consensus, as reflected in the consultations held with Ecuadorian civil society.
- 6.4 The adoption of a multisector focus in the social development and urban sustainability areas constitutes another risk in terms of coordinating project design and execution, both within the Bank and in the country, especially when subnational actors are involved. To mitigate this risk, the Bank will reinforce dialogue with SENPLADES and support its capacity for planning, coordination, evaluation, and monitoring in these areas. It will also take advantage of the corporate mechanisms being introduced to foster a multisector approach in its interventions. Furthermore, the multisector project approach will be introduced gradually, as the Bank and country gain experience with interventions of this type.

⁵¹ Annual analysis of the macroeconomic sustainability of borrowing member countries is being conducted under the GCI-9 mandate.

ANNEX I MAIN MACROECONOMIC AND SOCIAL INDICATORS

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
<i>Real Sector Indicators</i>										
Nominal GDP (US\$ millions)	24,718	28,409	32,646	36,942	41,705	45,504	54,209	52,022	57,978	65,945
GDP per capita (in current dollars)	1,952	2,212	2,506	2,795	3,110	3,345	3,927	3,715	4,082	4,578
GDP per capita, PPP (in current dollars)	5,174	5,377	5,919	6,371	6,789	7,024	7,586	7,581	7,828	8,335
Real GDP (growth, %)	3.4	3.3	8.8	5.7	4.8	2.0	7.2	0.4	3.6	7.8
<i>Fiscal indicators (% of GDP)</i>										
Primary balance	4.3%	4.5%	4.6%	2.9%	5.8%	4.2%	1.9%	-3.6%	-0.9%	-0.2%
Overall balance	0.9%	1.6%	2.2%	0.7%	3.6%	2.3%	0.6%	-4.3%	-1.6%	-1.0%
Public debt	57.24%	51.06%	44.57%	39.35%	32.35%	30.49%	25.34%	19.67%	23.00%	22.08%
External public debt	46.0%	40.4%	33.9%	29.4%	24.5%	23.4%	18.6%	14.2%	15.0%	15.2%
<i>External indicators</i>										
Current account (% GDP)	-4.9%	-1.4%	-1.5%	1.3%	4.2%	3.7%	2.7%	-0.2%	-3.1%	n.d.
Foreign direct investment (% GDP)	3.2%	3.1%	2.6%	1.3%	0.7%	0.4%	1.9%	0.6%	0.3%	n.d.
Unrestricted international reserves (US\$ millions)	1,008	1,160	1,437	2,147	2,023	3,521	4,473	3,792	2,622	2,958
Unrestricted international reserves (% GDP)	4.1%	4.1%	4.4%	5.8%	4.9%	7.7%	8.3%	7.3%	4.5%	4.5%
Remittances (% GDP)	5.8%	5.7%	5.6%	6.6%	7.0%	6.8%	5.2%	4.8%	4.0%	3.7%
<i>Monetary and foreign exchange indicators</i>										
Inflation rate (end)	12.5	7.9	2.7	3.1	2.87	3.32	8.83	4.31	3.33	5.41
Growth of monetary aggregates (M2)	21.0%	2.9%	17.8%	19.2%	15.5%	15.1%	21.9%	7.8%	17.8%	19.7%
Real exchange rate index	92.5	91.2	95.2	98.2	98.2	102.8	102.5	95.8	95.2	93.4
<i>Social indicators</i>										
Population (thousands)	12,660.7	12,842.6	13,027.0	13,215.0	13,408.0	13,605.0	13,805.0	14,005.0	14,204.9	14,483.5
Poverty rate	n.d	50%	44%	42%	38%	37%	35%	36%	33%	29%
Extreme poverty rate	n.d	26.6%	22.7%	21.6%	16.9%	16.5%	15.7%	15.4%	14.8%	13.1%
Unemployment rate	7.8%	9.3%	9.9%	9.3%	9.0%	6.1%	7.3%	7.9%	6.1%	5.1%
Total underemployment rate	30.7%	45.8%	42.5%	49.2%	45.0%	50.2%	48.8%	50.5%	47.1%	44.2%
<i>Sources: Central Bank of Ecuador, Ministry of Finance, National Statistics and Census Institute, International Monetary Fund (WEO).</i>										

ANNEX II LENDING FRAMEWORK

Fiscal situation. Fiscal performance has improved. In 2011 the overall fiscal deficit of the nonfinancial public sector (NFPS) declined for the third consecutive year, closing at -1.02% of GDP, with a primary deficit of -0.25% of GDP. The steady move toward values near fiscal balance reflects, on the one hand, the entrenchment of an ongoing process of optimization in tax revenue collection, and, on the other hand, the favorable trend in the price of oil. Stronger tax management has produced a sustained increase in tax revenue intake, which has grown at an average annual nominal rate of 13% approximately since 2007, reaching 13.7% of GDP⁵² at end-2011. Higher oil prices⁵³ have boosted the proceeds from petroleum exports to the equivalent of 20% of GDP at end-2011. The rising trend in expenditure partly reflects the increase in public investment, which ended 2011 at 14.9% of GDP, representing 31% of total outlays.

Medium-term financing requirements. In the medium term, the forecasts contained in the four-year budget program indicate that the government will maintain its current public investment policy, resulting in public deficits averaging 3.9% of GDP for the period 2012-2015. These scenarios could change, if the global environment shifts in ways that affect the price of oil or tax revenues through a slowing of economic activity in the country.⁵⁴ The gross financing requirements of the public sector are expected to decline as a percentage of GDP.

Ecuador: NFPS Financing Requirements
(% GDP)⁵⁵

	2012	2013	2014	2015
Gross financing requirements	8.0%	6.1%	6.3%	6.1%
Deficit (Surplus)	5.9%	4.1%	3.0%	2.7%
Amortization	2.1%	2.1%	3.3%	3.4%
Financing	8.0%	6.1%	6.3%	6.1%
Domestic	1.8%	0.7%	1.0%	0.6%
External	6.1%	5.4%	5.3%	5.5%

Source: Four-year Budget Program, Ministry of Finance.

⁵² Calculated on the basis of the value-added tax (VAT), special excise tax (ICE), income tax (IR), and customs duties.

⁵³ According to statistics from the Central Bank of Ecuador, the average price of oil was US\$60 per barrel at end-2007 and US\$97 at end-2011

⁵⁴ These future scenarios assume an oil price of US\$82.80 per barrel for the period 2012-2015. If repayment obligations are fixed in the short term, better oil prices would reduce the public-sector deficit, entailing lower financing requirements.

⁵⁵ The domestic financing component includes cash holdings and accounts payable.

ANNEX III ANALYSIS OF MACROECONOMIC RISKS

Overview. Following the recession in the context of the international financial crisis, Ecuador has returned to the path of robust economic growth that characterized most of the last decade. Despite three consecutive quarters of negative growth between end-2008 and mid-2009, the economy has recovered strongly since that time, with annual GDP growth of 3.6% in 2010 and 7.8% in 2011. The economy is projected to slow gradually in coming years, and the government forecasts growth rates of 5.4% in 2012, 4.4% in 2013, and 3.3% in 2014 and 2015.

Despite the rise in oil prices since mid-2009, the Ecuadorian economy has been running twin deficits. First, fiscal policy has kept the NFPS in a deficit position since 2009, although this has tended to moderate in the last two fiscal years (the primary deficit declined from 3.6% of GDP in 2009 to 0.9% of GDP in 2010, and to 0.2% of GDP in 2011). Second, the current account balance has also been negative since that same year. This is due to the behavior of the trade balance, where deficits (0.4% of GDP in 2009, 3.4% of GDP in 2010, and 1% of GDP in 2011) reflect the strength of nonoil imports, such that the oil trade surplus was insufficient to balance the external accounts.

The magnitude of the deficits described above is still moderate and does not pose an immediate threat to Ecuador's macroeconomic sustainability. Nevertheless, these imbalances are significant in a formally dollarized economy, where the authorities lack the ability to use monetary and exchange policy as instruments of macroeconomic adjustment. In this context, four risks have been identified that could affect the country's macroeconomic performance over the period of the new strategy. The first has to do with the volatility of oil prices and the possibility that a fall could widen the twin deficits described above. The second relates to the nonoil trade balance, which could deteriorate further and thereby affect the economy's external accounts. The third is the possibility that the NFPS could face sporadic liquidity problems in coming years. The fourth is the possibility that an economic slowdown could destabilize the financial system.

Oil price volatility. Although the oil economy represents less than 15% of Ecuador's GDP, and the recent growth has been concentrated in the nonoil sector, the crude oil price is an important determinant of the country's macroeconomic performance. First, oil revenues averaged one third of total NFPS revenues in the last five years. Second, during that same time, oil exports accounted for more than 50% of the country's total exports. Thus, abrupt corrections in the crude oil price, such as occurred during the international financial crisis,⁵⁶ tend to force a fiscal adjustment and sharply reduce the value of exports, with the consequent impact on aggregate demand.⁵⁷ There is no cushioning for these fluctuations, as Ecuador does not have mechanisms for stabilizing oil revenue, or any monetary or exchange

⁵⁶ The average price of oil exported by Ecuador fell from more than US\$96 per barrel in the first three quarters of 2008 to less than US\$30 per barrel between December 2008 and March 2009. From mid-2009 onward, the crude oil price began rising again, and has averaged more than US\$100 per barrel since late 2011.

⁵⁷ The international financial crisis forced the government to cut public spending by 3.4% in 2009, when the value of exports dropped 25% below their 2008 level.

instruments to minimize the impact of external shocks. Although the high oil prices of the last three quarters⁵⁸ are expected to continue in the short term, given the uncertainties still plaguing the world economy, new downturns in commodity prices cannot be ruled out. Due to the persistence of the twin deficits described above, the authorities would have less fiscal headroom than in 2008-2009 for coping with a new round of international commodity price cuts. This means that, in such a scenario, the impact on aggregate demand would be greater than the one during the international financial crisis.

Behavior of the nonoil trade balance. In recent years the negative nonoil trade balance has grown, reaching US\$8.546 billion in 2011, equivalent to 13% of Ecuador's GDP. That deficit is of such magnitude that, despite the recent oil boom and the still-high worker remittances flowing into the country, the overall trade balance and the current account balance have also fallen into deficit. Since the Ecuadorian economy is formally dollarized and attracts only a limited volume of international financing, a worsening of this trend could become a problem if the monetary base were to begin leaking abroad, as this would impact the country's growth outlook. This risk helps to explain the government's recent activism on the trade front and the steps it has taken to promote nontraditional exports and discourage outflows of foreign exchange.⁵⁹ The long-term sustainability of Ecuador's dollarized monetary system could depend on the success of these efforts to restore external balance to the economy.

NFPS financing difficulties. At around 22% of GDP at the end of 2011, Ecuador's public debt is unlikely to enter an unsustainable path during the period of the new strategy. However, there is a risk that the projected NFPS financing requirements for the coming years may pose liquidity problems from time to time. To lend continuity to the ambitious public investment program under way, the Government of Ecuador projects annual external financing requirements averaging 5.5% of GDP during the period 2012-2015.⁶⁰ The government has not had access to international financial markets since the credit event of 2008, when Ecuador suspended the servicing of two global bonds, although it should be noted that its credit rating was recently revised upwards by several rating agencies. This means that the NFPS is currently covering its financing requirements with funds provided by public multilateral creditors and nontraditional bilateral lenders, primarily the People's Republic of China.⁶¹ The risk here is that the funds provided by these creditors may at times

⁵⁸ For 2012, the United States Department of Energy is forecasting even higher prices of WT1 oil, at \$105.70 per barrel.

⁵⁹ These measures are authorized in the Production Code approved by the government in 2010, which establishes a series of mechanisms to improve the export offerings of sectors with greater value than those that have tended to dominate the country's exports. There has also been a progressive increase in the tax rate on currency outflows, which at the end of 2011 stood at 5%, and nonautomatic import licenses were introduced in that same year.

⁶⁰ The four-year budget program is based on intentionally conservative assumptions about oil prices, which means that in practice the NFPS financing requirements tend to be lower than projected because the actual oil price is higher.

⁶¹ Ecuador's bilateral debt with the People's Republic of China at end-June 2012 stood at US\$2.557 billion, equivalent to 25.5% of the total external public debt.

fall short of NFPS financing requirements, especially if the country's access to capital markets remains constrained.

Stability of the financial system. Banking penetration indexes have improved in Ecuador in the last several years, such that at end-2011, the stock of deposits exceeded 32% of GDP, and bank lending was 24.5% of GDP. The pace of credit expansion has been particularly brisk since the 2009 recession, with a growth rate of 18% in 2011. This credit expansion does not yet appear to have entailed any deterioration in the quality of bank balance sheets, and the proportion of past-due loans in the total portfolio has remained stable at around 3% for private banks, whereas for public banks it has in fact declined, to 5.7%. Other indicators suggest that the financial system's liquidity and solvency ratios as well as the profitability of the banking business are at adequate levels.⁶² Yet there are still risks to the financial system's stability, as the recent strong economic growth could obscure the real solvency situation of many debtors. This risk is particularly significant in the case of Ecuador, since, despite the creation in 2008 of a liquidity fund and a deposit insurance scheme, the dollarization of the monetary system means that there is no lender of last resort with the capacity to issue money. Thus, it cannot be ruled out that a deeper than anticipated slowdown of the economy might give rise to an episode of financial instability, to which the authorities would have little ability to respond, and which would adversely impact the country's macroeconomic performance.

⁶² At end-2012 the liquid assets of the Ecuadorian banking system covered 51.3% of its short-term liabilities. The capital ratio for private banks was around 12.9%, while return on assets (ROA) and return on equity (ROE) were 1.3% and 10.1%, respectively.

ANNEX IV SUMMARY OF COORDINATION ACTIVITIES

The Ecuadorian government coordinates the activities of international cooperation agencies primarily through three institutions: the Technical Secretariat for International Cooperation (SETECI), the National Planning and Development Secretariat (SENPLADES), and the Ministry of Finance. SETECI is a public agency charged with negotiating, managing, and harmonizing grant funds from donors, and therefore plays a central role in the Ecuadorian International Cooperation System. To advance with implementation of the Paris Declaration principles, SETECI hosts meetings of the Global Dialogue Forum, which provides an avenue for direct dialogue between international cooperation and government agencies. Thematic discussion groups are also being established, where this dialogue and coordination work will be done on a sector-by-sector basis. SENPLADES, as the institution responsible for planning the country's development, also has an important place in this system since, to be approved, all investment programs and projects must in practice be submitted for its consideration. Lastly, the Ministry of Finance allocates funds to the projects prioritized by SENPLADES, giving it a central role in coordinating the distribution of funds borrowed by Ecuador from its multilateral and bilateral creditors.

Initiatives have also emerged at the sector level as dialogue forums where coordination activities also take place. Of particular interest is the Economic Fabric Roundtable ("Mesa de Tejido Económico"), in which the IDB participates, which brings together public institutions such as the Central Bank, the Superintendency of Banks and Insurance (SBS) and various ministries, cooperation agencies such as AECID and USAID, and private institutions to address questions relating to financial inclusion and the country's productive development. Regular meetings are also held with international cooperation agencies as part of risk management.

Following is a summary of the Bank's most recent coordination activities:

1. Coordination with the CAF on transportation and roads.
2. Coordination with the CAF and the EIB, which is expected to lead to cofinancing for constructing the Quito Metro.
3. Cofinancing with the Spanish Agency for International Development Cooperation (AECID) under the Rural Water and Sanitation Infrastructure Program (PIRSA).
4. As part of the Small-scale Coastal Fisheries Project, the Bank is coordinating with USAID, which is financing the Sustainable Coastlines and Forests project, complementary to this operation.
5. Use of GEF allocations for the Ecuador Marine and Coastal Biodiversity Project.
6. Collaboration with the Pan American Health Organization for a workshop on integration of the public health system.

ANNEX V RECOMMENDATIONS OF THE OVE COUNTRY PROGRAM EVALUATION

<p>Recommendations of the OVE country program evaluation 2008-2011</p>	<p>Incorporation into the Bank's country strategy with Ecuador 2012-2017</p>
<p><i>The Bank should be bolder in engaging in policy dialogue. As one of the country's main lenders, the Bank should be in a position to contribute to the government's efforts to define a national agenda to reduce the country's economic vulnerability to exogenous factors and to improve the business climate and competitiveness indexes.</i></p>	<p>Partially agree. The Bank has played an active role in designing certain sector policies, principally through investment loans and technical cooperation operations. This dialogue should continue and be fostered in the future. However, it is much more difficult to impact the country's macroeconomic management because the authorities have not sought dialogue in that regard. Although the Bank is one of the country's main lenders, as stated in the report, the volume of resources mobilized hardly gives it the leverage described in the report. In the period 2007 to October 2011, nonfinancial public sector investment was US\$29.7 billion, whereas the Bank disbursed US\$1.136 billion. This means that the Bank financed just over 3.5% of public sector investments.</p>
<p><i>The Bank should continue prioritizing sectors that can address problems of competitiveness, inequality and social exclusion. Given the Bank's limited capacity to meet the country's financing needs, the Bank should:</i></p> <p><i>a. Redesign support so that it leverages other investments, for example by (i) helping to improve regulatory frameworks for infrastructure sectors to attract public-private partnerships and foreign investments; (ii) continuing to finance institutional components of projects, learning from past experience; and (iii) contributing to improve corporate governance in oil and electricity companies.</i></p> <p><i>b. Expand support to help address urban and rural inequalities. The Bank should continue its support for health, education, water and sanitation programs in poor urban and rural areas, benefiting from the Bank's accrued experience in these areas.</i></p> <p><i>c. Avoid demands in which economic benefits did not clearly justify the Bank's support, such as the Transportes Aéreos Militares del Ecuador (TAME) Project.</i></p>	<p>Agree. The Bank has gained substantial experience in the areas of competitiveness, inequality, and social exclusion in Ecuador, which remain priorities under the new country strategy now in preparation. We also agree that, given the limited volume of resources the Bank is able to contribute, efforts should be made to emphasize the institutional and policy component of projects, so as to catalyze other investments for the country. We also believe the Bank's new country strategy should continue addressing the inequalities between urban and rural areas. Moreover, project programming and preparation activities include an exhaustive analysis of the strategic relevance, performance, and additionality of each project.</p>

<p><i>The Bank should continue strengthening Ecuador's planning, evaluation, and monitoring capacity by working with the Secretaría Nacional de Planificación y Desarrollo (SENPLADES), the entity responsible for originating the National Plans that are the framework for the Country Strategy.</i></p>	<p>Agree. SENPLADES—the National Planning and Development Secretariat—is a key institution with which the Bank has been working directly through several operations contributing, for example, to helping the government identify the potential of public-private partnerships as efficient management mechanisms. It should also be noted that SENPLADES is involved indirectly in all Bank programs, since they are subject to its review prior to approval. We therefore agree that the Bank needs to continue working with SENPLADES under the new country strategy.</p>
<p><i>The Bank should continue promoting sharing of experience and common training programs for national and subnational executing agencies. In addition to technical cooperation at the appraisal phase of projects, the Bank could contribute to the country's capacity to handle Bank projects by promoting seminars and workshops with personnel responsible for executing Bank's projects. The aim is to strengthen the agencies that have lower institutional capacities and reduce the imbalances among them, thereby contributing to greater efficiency and effectiveness in project execution</i></p>	<p>Agree. The new country strategy is taking this recommendation into account. The Bank has provided direct support for executing agencies through a series of capacity-building seminars focusing on financial management of procurement and fiduciary risk management. For example, 37 workshops were held in 2010 and 2011 to help all executing agencies implement the new integrated project management model</p>

ANNEX VI DEVELOPMENT EFFECTIVENESS MATRIX

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX	
<p>In August 2008, the Board of Directors approved the Development Effectiveness Framework (document GN-2489) to increase the evaluability of all Bank development products.</p> <p>The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."</p>	
<p>COUNTRY STRATEGY: ECUADOR 2012-2016</p> <p>STRATEGIC ALIGNMENT. <i>Measures two dimensions: (i) the extent to which the objectives of the strategy are consistent with the country's development challenges and with the government's priorities and plans; and (ii) use of a mix of products (financial, knowledge, technical assistance) to attain the objectives, and identification of other cooperation agencies and their areas of action.</i></p> <p>Consistency of strategic objectives: <i>The strategy identifies the following areas of work: (i) energy; (ii) transportation and logistics; (iii) social development; (iv) access to finance; (v) fiscal management; (vi) urban sustainability; (vii) rural development; and (viii) natural disaster risk management. The topics of diversity and of climate change and environmental sustainability will be addressed as crosscutting issues in the strategy. All areas selected for Bank intervention address development challenges and are consistent with the priorities set by the Government of Ecuador. In addition, the selected work areas result from the dialogue between the country and the Bank.</i></p> <p>Mix of products and participation by other donors: <i>The strategy proposes to use different Bank instruments, such as SG operations, NSG operations, and TC operations with a multisector approach. The strategy takes into account interventions by other multilateral cooperation agencies including USAID, AECID, and the European Investment Bank.</i></p> <p>EFFECTIVENESS: <i>Measures whether the country strategy is likely to achieve its intended objectives, through an examination of four dimensions of effectiveness.</i></p>	
Effectiveness dimensions	%
I. Sector diagnostics	
- Identifies the main problems based on empirical evidence	100
- Identifies the main beneficiaries	100
- Identifies and measures the factors that contribute to the problems identified	100
- Presents the policy framework and a sequence for Bank intervention	100
- The diagnostic corresponds to the objectives presented in the strategy	100
II. Results matrix	
- The expected outcomes are clearly defined	100
- The indicators are outcome indicators and are SMART	97
- The indicators have baselines	100

Thirteen sector notes were presented to support the strategy ; all are validated.

-100% of the notes clearly identify the main sector problems based on empirical evidence.

-100% of the notes identify the potential beneficiaries in each area of intervention.

-100% of the notes identify or measure the factors that contribute to the problems identified.

-100% of the notes identify the policy framework and a sequence for Bank actions.

-In 100% of the notes, there is consistency between the note and the proposed strategic objectives.

Results matrix: The results matrix contains 18 strategic objectives for Bank action and 31 indicators to track progress.

- 100% of the strategic objectives clearly identify expected outcomes.

- 97% of the indicators used are outcome indicators and are SMART; the other 3% are either unsuitable for measuring expected outcomes or need to be specified more precisely.

- 100% of the indicators have baselines.

Country systems: All financial management and procurement subsystems have been assessed. Some of the financial management subsystems will be strengthened. All country systems will be used during the strategy period.

Lending framework: The strategy contains an analysis of the country's financing requirements, and provides an estimate of the amount of financing that could be provided by the Bank. The lending framework is consistent with the macroeconomic projections and the country's financing strategy.

Risks: Measures three dimensions: (i) identification of factors that actually do or might affect attainment of the proposed objectives; (ii) definition of mitigation measures; and (iii) monitoring mechanisms.

The strategy identifies the risks associated with Bank participation in each of the strategic sectors and identifies mitigation measures. It also identifies macroeconomic and institutional risks, as well as implementation risks relating to the coordination challenges of the multisector approach.