

# The Ecuador Report

## EXPLOSIVE PROFITS

Ecuador is opening up its natural wealth to investors



### IN-DEPTH SECTOR ANALYSIS

Mining - Oil - Agriculture - Real Estate

### ENERGY & MINING SPOTLIGHT

We talk to Carlos Pérez, Minister of Energy and Non-Renewable Resources

### TRADE SPOTLIGHT

Minister of Production, Foreign Trade, Investment & Fisheries, Iván Ontaneda, discusses Ecuador's growth plans

### ECONOMY SPOTLIGHT

We interview the Minister of Economy and Finance, Richard Martínez



# COUNTRY REPORT | ECUADOR



## Ecuador



**CAPITAL**  
Quito



**CURRENCY**  
US Dollar



**CONTINENT**  
South America



**OFFICIAL LANGUAGE**  
Spanish



**POPULATION**  
17.37 m

### Politics

#### PRESIDENT

Lenin  
Moreno

#### EXECUTIVE BRANCH

The current Head of Government is Lenin Moreno.

#### LEGISLATIVE BRANCH

A unicameral Congress of 137 members that are elected for a four-year term by proportional representation. The President also has the power to convene an executive cabinet to draft legislation, though this can be overruled by sufficient votes from Congress.

#### JUDICIARY BRANCH

The judicial branch of government is headed by a 21-member National Court of Justice in Quito, while the Constitutional Court interprets the constitution with regards to individual rights.

The last elections were held on April 2017 and the next are due in 2021.



### Global Rankings

86 114 123

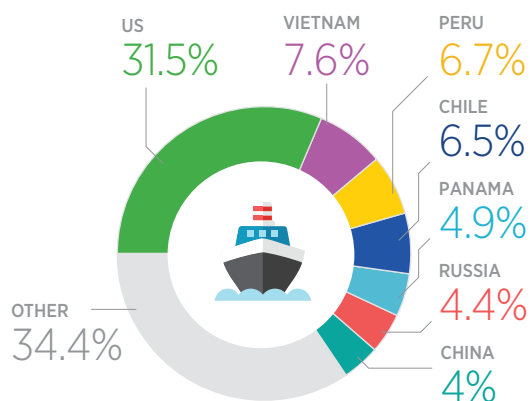
Competitiveness

Corruption

Ease of Doing Business

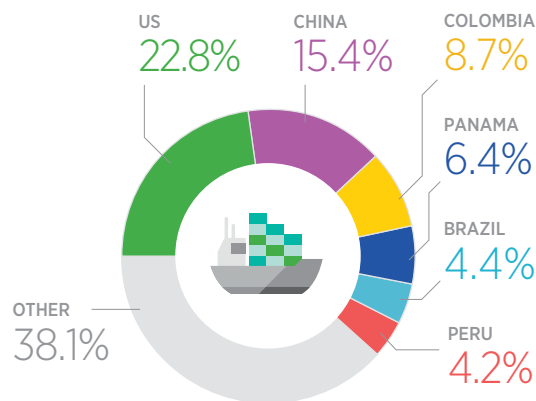
### Main Trading Partners

#### Exports



Petroleum, shrimp, bananas, cut flowers, cacao, coffee, wood, fish

#### Imports



Industrial materials, fuels and lubricants, nondurable consumer goods



INFLATION

0.3%



GDP (PPP)

\$108 bn



GDP GROWTH

0.2%  
2019 est



GDP PER CAPITA (PPP)

\$6,198

### National Tax Rates



CORPORATE

22%



PERSONAL INCOME

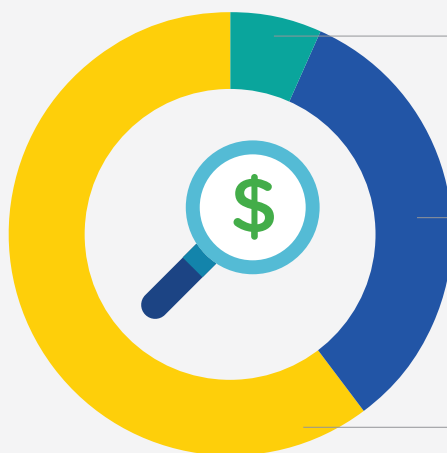
35%



SALES

12%

### GDP Composition



AGRICULTURE

6.7%



INDUSTRY

32.9%

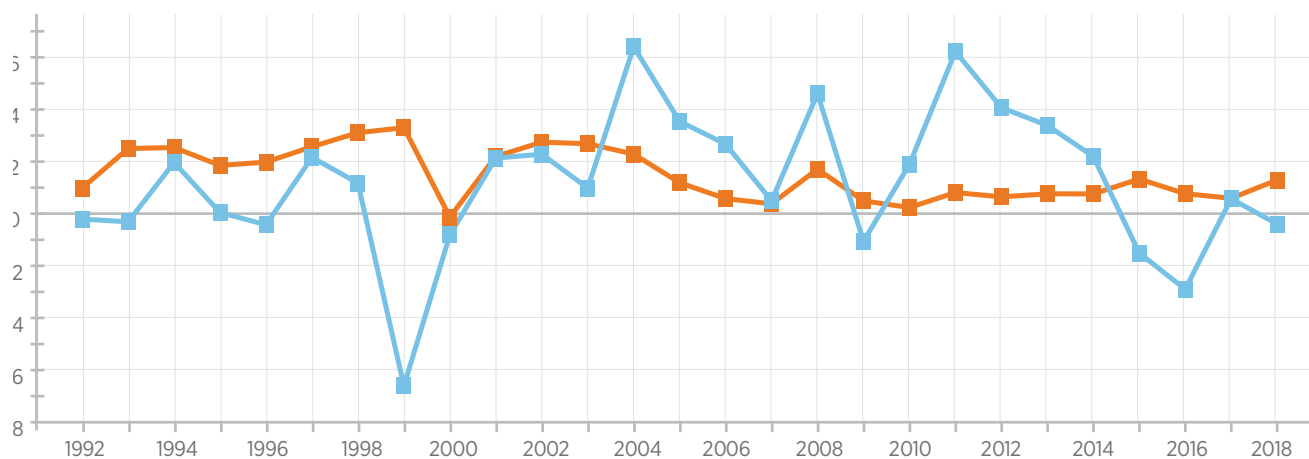


SERVICES

59.9%



■ GDP per Capita Growth (Annual %) ■ Foreign Direct Investment, Net Flows (% of GDP)



Sources: World Bank, Transparency International, World Economic Forum, BCRP



## THE UK VIEW:

HM Ambassador to Ecuador,

## Katherine Ward,

explains why the bilateral relationship is back with a bang...

**LATAM INVESTOR:**  
*Explain how the UK's relationship with Ecuador has changed recently?*

**AMBASSADOR WARD:** When I arrived in January 2017 the relationship was not positive. Ecuador's previous government granted asylum to Julian Assange, which allowed him to breach bail conditions in the UK and flee British law by remaining in the Ecuadorian Embassy in London. It caused a serious diplomatic incident between the UK and Ecuador, with some describing our relations as 'in the freezer'. As a result, there were no ministerial visits from either country, with our brief meetings in international fora merely confirming our disagreement on the Assange issue. By the time I arrived in Quito, British cooperation on most other agendas had also mostly ground to a halt.

In May 2017 a new president was elected. And even though Lenin Moreno was from the same political party, his attitude towards the Assange issue and the type of relationship he wanted with the UK was completely different than that of his predecessor Rafael Correa. So, we shifted our policy and began to engage Ecuador on issues where there was a clear interest for the UK.

In autumn 2017, Ecuador's then Trade Minister, Pablo Campana, included the UK in his first overseas visit, leading to the first ministerial meeting between Ecuador and Great Britain for several years. Ecuador's First Lady also paid a private visit to the UK that included some official meetings on gender issues, and we invited President Moreno to be the keynote speaker at the Global Disability Summit we held in London in summer 2018.

Earlier this year, the Ecuadorian government decided to put an end to the Assange issue. That led to the first visit of a UK minister to Ecuador in eight years, when Minister for Trade Policy George Hollingbery MP came to sign the Andean Continuity Agreement in Quito. In July, Sir Alan Duncan, then Foreign Office Minister responsible for the Americas, came to Ecuador to formally relaunch the bilateral relationship, sign a joint cooperation declaration and meet the President. So the bilateral relationship now is extremely good and very friendly.

**LAI:** *Will trade and investment between the two countries grow?*

**AW:** In 2016 Ecuador joined the EU Trade Agreement with Colombia and Peru. That led to a 143% increase in British exports to Ecuador in 2017. So, it was vital that we signed a continuity agreement that ensured the same terms of trade would exist after Brexit. We are pleased that is now in place with Ecuador, but ratification will take a few months. Both governments are working hard to ensure that there will not be any disruption to trade when the UK leaves the EU.

“  
**The IMF deal would have been unthinkable under the previous government**



Ambassador Ward

On the investment side, one of the sectors with the most potential is mining. We are part of a diplomatic group of mining countries that works

with mining companies and the mining chamber to try to help them resolve issues holding the industry back. We are also working to improve conditions for British investors in Ecuador. For example, we have started negotiations on a double taxation agreement, with a tentative agenda already arranged. Ecuador is also keen to have a new bilateral investment treaty with the UK, so we should see the investment climate continue to improve in coming years.

The change with this new government is more radical than people give it credit for. Indeed, I believe history will be kinder to Moreno's government than his current poll numbers suggest. The IMF deal would have been unthinkable under the previous government. In 2018 FDI rose by 127% to a historic high. A batch of ambitious economic reforms is due in the autumn, covering everything from labour law to the tax regime. If approved, the reforms could help transform the economy. Coupled with the anti-corruption measures taken by this government - which are beginning to be felt in the corruption perception index - we are seeing a steady improvement in the business environment.

**LAI:** *How is the British Embassy in Quito making the most of the improved relationship?*

**AW:** We have a small team here, so we have to prioritise our resources. One of the really positive developments with this government is the fight against corruption. Before she was given the role, we invited the new Prosecutor General to the UK to see our anti-corruption methods and we will continue to support her work. We have also been helping Ecuador combat narcotics and organised crime. Another

area of common interest is human rights. Both the UK and Ecuador want to fight gender inequality. In Ecuador, like in much of Latin America, there is a problem with violence against women and girls, so we are working with them to reduce that.

Environment is another area of strong cooperation. We are using British technology to run an environmental education programme with Ecuador's Science Museum and the Darwin Foundation, to enable Ecuadorian children, many who have never been to the Galapagos, to see and learn about the islands via virtual reality. We are backing Galapagos Conservation Trust's work to identify where plastics that arrive in the Galapagos come from. Meanwhile Ichthion, a British company started by an Ecuadorian student in the UK, received a £600,000 innovation grant from the British government to develop solutions to remove and recycle plastics from rivers. The Embassy is supporting Ichthion in its bid to introduce this technology in Ecuador.

**LAI:** *Does the UK need to beef up its diplomatic presence in Ecuador?*

**AW:** We've managed to do quite a lot with a small footprint, as many of the initiatives I mentioned above are delivered by collaborating with partners. But I hope we will be able to secure more staff to pursue the opportunities the relaunched bilateral relationship presents.

For trade, our team from the Department for International Trade can act as a point of contact for your readers when they come to Ecuador, providing contacts and local knowledge to help UK companies succeed. We are also

fortunate to have an excellent British Chamber of Commerce here.

In Ecuador the regional differences between the coast and the highlands are very marked so the chamber has two separate branches, one in Quito and one in Guayaquil. They support each other, share branding and have equal status; however, each tends to operate in their own sphere of influence. Depending on where a new UK company will be focused, they can work with the relevant branch of the chamber.

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## USEFUL CONTACTS

**Ecuador Trade Office, London**  
 Juan Carlos Yépez  
 Tel: +44 (0) 203 078 8040  
 jyepzf@proecuador.gob.ec

**British Chamber, Quito**  
 Diego Gordon  
 dgordon@camarabritanica.com.ec  
 +593 2 2250883

**British Chamber of Commerce Guayaquil**  
 Cira Villacreses  
 cira.villacreses@camarabritanica.com.ec  
 Tel: +593 4 3703870



## Ecuador Opens Up its Oil Industry to International Investors

*The Opec member needs foreign firms to help it capitalise on its oil wealth before new energy sources render it redundant...*

More than a century ago, legendary Ecuadorian president, Eloy Alfaro, signed the country's first ever oil exploitation contract. A flurry of further deals eventually saw Anglo Ecuadorian Oilfields, that would later become part of BP, emerge as the dominant player Ecuador's oil industry, producing steady amounts in the coastal province of Santa Elena.

Ecuador's coast may have been the starting point for the country's oil industry but it wasn't to remain its epicentre. Rumours of immense oil wealth in Ecuador's jungle continued to draw international investors east, with both Shell and Standard Oil conducting extensive exploration.

By the 1960s the Oriente, as the area east of the Ecuadorian Andes is known locally, began producing commercial amounts of oil. That sparked an oil rush, with companies from around the world vying for blocks in Ecuador's jungle over the following three decades. Yet their status and business conditions would constantly change as different Ecuadorian governments altered national oil policy. New state oil companies emerged as major players in the industry, while various foreign firms left in protest at their treatment. That Ecuador, which joined international oil cartel Opec in 1973, should assume greater control over its natural resources was both fair and in keeping with prevailing global trends at the time. Yet the country's political

instability meant its oil policies would swing, pendulum-like, from 'investor friendly' to 'resource nationalism'.

The government of Rafael Correa, 2007 to 2017, oversaw a swing to resource nationalism. In a time of record commodity prices, a windfall tax was created to increase the state's share of profits. Meanwhile existing oil companies that had production sharing contracts with the Ecuadorian state saw them forcibly changed to service contracts. Now Moreno's administration is trying to attract international oil firms by creating more welcoming conditions for investors.

### Investor friendly

The man in charge of Ecuador's oil industry is Carlos Pérez, Minister for Energy and Non-Renewable Resources. The son of a former general manager of Anglo Ecuadorian Oilfields, Pérez grew up in the coastal oil camp of Ancon. Surrounded by expat oil workers he spoke English before he learned Spanish and went on to have a successful career in the industry, working for the likes of Halliburton before being headhunted by this administration.

"The service contract model that the last government favoured was not very attractive for international companies. We've changed that to a participation contract, which allows companies to book reserves. Another crucial element is that they are fair. We use a formula that means when

the oil price is high, both Ecuador and the companies benefit. And when it is low, we both suffer. That fairness has helped it attract oil and gas firms. For example, in our Intracampos Round we had successful bidders for seven of the eight contracts offered, with a total investment of \$1.2billion."

You would expect a minister to talk up his government's new oil contracts but many in the industry view them as a positive development. Fernando Emanuele is the CEO of Orion Energy, a privately-owned, Ecuadorian-focused oil company backed by British and Singaporean investors. In 2014 it acquired two blocks in the jungle in Ecuador's northeast and operates under the service contract model. Emanuele is keen to stress that the service contracts are not all bad, noting that, despite the name, the Ecuadorian version is different to service contracts in other countries, like Mexico. "If we don't produce, we don't get paid. We earn per barrel, so really, it's a revenue sharing contract with a fixed fee."

However, he agrees that there are some serious drawbacks. "We can't get reserved-based lending, which cuts off an important source of funding. That's because we rely on the state, in particularly the Ministry of Energy and Non-Renewable Resources' trading branch, PetroEcuador, to commercialise our oil. Once it sells the oil it repays us out of the national budget. That means that if the oil price falls or Ecuador has budgetary problems our payments can







Juan Cevallos, President, IJC

**“Some large energy infrastructure projects were hit by political problems so it remains to be seen if this government can have more success**

be delayed. In 2017, we didn't get paid for six months, which put us under enormous strain.”

The new participation contracts avoid that problem and therefore should succeed in attracting more investment. “We are planning to expand in Ecuador”, says Emanuele, “and will be bidding for some of the blocks coming available under the new contracts. We will stick to the northeast of Ecuador, where you have nearfield exploration opportunities. That's great for a mid-sized company like us because it's the type of exploration risk we can carry on our balance sheet. And if you find oil, then the infrastructure is already in place to take it to the market. There are some larger scale opportunities that will become available in the southeast of the country over the next decade but they are too big for us to take on.”

## New projects

Ecuador's oil industry officially began more than 100 years ago with Alfaro's first contract to the Englishman, Carlton Granville Dunne, in 1909 but there are still at least 4.7 billion barrels of oil that have been untouched. That's an incredible strategic asset for the country but one that may lose its value in the future as new energy technologies replace oil. Minister Pérez believes global oil demand will be in decline by 2040 and that “it's imperative that we make the most out of our resources now”. But with the right investment conditions the minister estimates that oil production could hit 700,000 within a few years, up from its current level of 550,000 barrels per day (bpd).

That 2040 deadline has given Ecuador's oil market a sense of urgency because there are several challenges that need to be overcome if the country is to make the most of its black gold. Ecuador's northeast oil basins are served by excellent infrastructure, with current pipeline capacity of 850,000 bpd. Yet decades of constant production mean these maturing basins are also becoming more geologically complex. Some of the most exciting, barely-touched oil basins are in the country's southern jungle but they come with social challenges, as some tribes are against the industry, coupled with a lack of infrastructure. Pipelines,

matter, says Emanuele. Orion's access to the northern pipeline “means we pay transport costs of less than \$3 per barrel – if we had to truck it the cost would be around \$20.”

Under the previous administration you would have expected state firms, such as national E&P firm Petroamazonas, to be called on to boost production and build infrastructure. But as Minister Pérez frankly admits in his exclusive interview with LatAm INVESTOR, the national oil firm, “lacks capital”. As a result, opportunities will be created for international firms.

“There is definitely a shift in the market environment and the government is embracing local and international investment to the oil and gas sector”, observes Juan Cevallos, founder and President of the eponymous oil production equipment supplier Importadora Juan Cevallos, known as IJC. His firm sources the best oil equipment from around the world and ►►

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+593 994 654-616 / +593 22330-577



maintains a well-stocked inventory to supply Ecuador's hydrocarbon industry. Cevallos is confident that it could help with a new southern pipeline, given that it is already a trusted partner of the \$1.4 billion northern oil duct, OCP. "Ecuador's largest international private-sector oil and gas investment so far was the OCP pipeline, that takes crude from Ecuador's northwest jungle region to the refinery on the coast. We worked on the construction of that project, providing the tubes, valves and joints it needed in 2003 and 2004. Then we have stayed as a partner, providing the spare parts for essential maintenance during the pipeline's operation. I'm proud to say that in 2007 OCP selected us as the best provider out of more than 700 other companies."

Fortunately for companies like IJC the new government has an ambitious portfolio of energy projects. The most urgent is the refinery, with the existing plant at Esmeraldas only able to process 110,000 bpd. Moreover, fuel produced by the 42-year-old refinery will soon fall foul of the International Maritime Organisation's new 0.5% sulphur regulations. The government is also inviting private-sector bidders for a new 300,000 bpd refinery, having decided to scrap the protracted, expensive and corruption-ridden attempt of the previous administration to build one.

The challenge for this government, says Cevallos, is not only attracting the investment but making sure the projects actually get built. "Some large energy infrastructure projects were hit by political problems so it remains to be seen if this government can have more success. For example, in 2014 we won an important contract to supply all of the fitting for the multi-use pipeline being built from Cuenca in the highlands to Pascuales on the coast.

Unfortunately, the project became enveloped in the Odebrecht scandal, that we are far removed from, but we are proud to have met the technical requirements. Likewise, we supplied the parts for a 90km, 48-inch diameter pipeline that was laid for the Refinería del Pacífico coastal refinery project. Again, we are proud to have fulfilled our duties but sadly that project has also been halted for political reasons."

## Environmental care

Ecuador is faced with a dilemma. The bulk of its proven oil reserves are to be found in the midst of its other great natural resource – the Amazon rainforest. Much of the oil is in or around Yasuní, a national park whose rainforest is one of the most biodiverse places on the planet. Previous president Correa floated an ambitious scheme for developed countries to pay to leave the oil untouched but it proved economically unviable. That means Ecuador, a country still struggling to provide its poorest with acceptable healthcare, education and housing, must find a way to use one endowment without damaging the other.

For many years that seemed impossible. The state, often inefficient or corrupt, proved unable to develop and enforce the stringent environmental standards needed to develop oil and gas in the Ecuadorian jungle, while some international companies were criminally negligent towards their ecological obligations. Fortunately, that changed in Correa's administration and Ecuador's oil and gas industry is now governed by strict local and international regulations.

Minister Pérez is clear that responsible production in the rainforest is vital if Ecuador is to realise its oil and gas potential. "In the ITT hydrocarbon deposit, which is one of our main targets, we have raised production to

80,000 barrels per day (bpd). But the potential is even greater, with scope for 200,000 bpd." The emphasis on environmental protection has led to a new type of oil service company that is capable of delivering safe energy projects in the rainforest. FYI Group, an Ecuadorian engineering and construction firm that specialises in energy, mining and water projects, is a good example. "We've built three production platforms in the ITT oil field", explains FYI Group CEO, Fabián Yar. "We did everything from definitive design to production.

These platforms were subject to four audits. First PetroAmazonas inspect your work, then the Ministry of Environment, then the international guarantor countries that have a commitment to protecting Yasuní and finally the community. One of our environment audits had 450 different items that had to be independently checked every month, so these were very stringent tests. It is probably one of the most controlled oil and gas areas in the world. I'm proud to say that not only did we pass the audits but we have won ecological awards for our care of the environment."

Ecuador will have to develop its own set of best practises and technology, because nowhere else in the world has identical conditions to Yasuní. FYI Group is leading the charge. "We created some innovative ecological solutions. For example, in one project our idea, which the client accepted, was to place a temporary road that can be removed when oil production stops. It means that eventually the jungle returns to its original state. We invest heavily in buying the most ecologically-friendly equipment and supplies from around the world to ensure that we minimise the environmental impact. Another innovation is that we don't use local wood for constructing the



campsite and the facilities. We bring our own prefabricated equipment.”

Extracting oil responsibly from the jungle is never going to be easy, explains Yar, but it’s not impossible. “Ecuador can and is exploiting its oil and gas potential in an environmentally responsible manner. The environmental regulations are among the strictest in the world, but if companies comply with them then they can make successful projects.”

With all this talk of the challenges, one may wonder why investors would come to Ecuador in the first place. Perhaps the best reminder comes from Orion Energy, which recently scaled back its pan-Latin American aims to concentrate on Ecuador. Emanuele notes that “as Mexico’s energy reform stalled, Venezuela sunk further into deep problems and even

“  
**It is probably  
one of the most  
controlled oil and  
gas areas in the  
world**

Colombia, which was the oil and gas darling of the region, struggled with poor infrastructure and too much competition for reserves that are not that big”, it became apparent that Ecuador is one of the most attractive countries in Latin America.

Alfaro was a force of nature - a revolutionary-turned-president who achievements, such as opening up the oil sector and building the Quito-Guayaquil railway, dragged Ecuador into the 20th century. Yet Ecuador



**FYI Group CEO,  
Fabián Yar**

has always been a tough country to govern and Alfaro was killed on the streets of Quito by a conservative mob. Fast-forward 100 years and another Ecuadorian reforming president, Lenin Moreno, is trying to modernise Ecuador’s oil industry. And while Moreno will hope to avoid Alfaro’s grisly fate, he too is looking to British investors to kickstart his hydrocarbon revolution. ■



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## ENERGY AND MINING SPOTLIGHT:

Minister for Energy and Non-Renewable Natural Resources,

# Carlos Pérez,

explains why Ecuador is welcoming UK investors...

**LATAM INVESTOR:** *Miners' biggest worry in Ecuador are the political risks; what is your ministry doing to mitigate them?*

**MINISTER PÉREZ:** We share the industry's concern and we are working on reducing the political risk. We have to show a different face of mining industry to the Ecuadorian people because the bad examples they have seen so far has triggered opposition from environmental and social groups. As a government we are attracting international companies, with best practises that will bring responsible mining to the country. Our challenge is to make the protestors realise that. Unfortunately, some of these protests are led by international NGOs from Europe and the US that are opposed to all forms of mining.

One way we are doing this is by cracking down on the illegal, informal mining that blights our country. We recently stopped 10,000 illegal miners in Buenos Aires, Imbabura province. This informal mining is linked to organised crime in Ecuador, Colombia and Venezuela, and causes much environmental and social damage. The other way we reduce political risk is by closely regulating the new legal miners coming to the country. We are very strict in ensuring they comply with their environmental and social obligations, for example we stopped one project for a year



because it hadn't fulfilled some technical safety requirements. We believe that this strict approach is good for the industry in the long run because it will help convince the Ecuadorian people that legal, regulated mining will not harm the country.

Of course, some of the political risk is out of our hands. In Rio Blanco, located in the Azuay province, mining was stopped after a judge misinterpreted the result of a local referendum. We're now working through the courts to get that decision overruled, as the project in question complies with all of the relevant legislation. The Constitutional Court has the final say when a community decides to challenge mining. As a government we are strongly communicating to the court that it should take rational decisions based on fact and Ecuadorian law. If it does so, then the type

of responsible mining we are encouraging should be allowed.

**LAI:** *What are the advantages of Ecuador as a mining jurisdiction?*

**MP:** Ecuador's most important competitive advantage is our geology. We have mineral rich sections of the Andes that haven't been exploited by miners. As a result, the mineral content of the rock being targeted in these initial projects is very high. We have had some of the world's largest copper and gold discoveries in recent years, which look like they will be turned into very profitable mines. That cost structure is further aided by the fact that we are a relatively small country, with good infrastructure coverage. We have an excellent road system and surplus power generation capacity, which means that new projects don't need to build massive amounts of infrastructure. We have further complimented these advantages by designing an excellent mining regime, with profit sharing that is in line with international standards.

**LAI:** *Ecuador's oil is in the jungle; how will it overcome the social, environmental and infrastructure challenges?*

**MP:** Obviously there are restrictions in the rainforest. We can't operate in Yasuni National Park, yet we are allowed

in a transition area. That also causes some delays, for example it took us six months to get the licenses for Ishpingo platforms A and B. But we have seen success in recent years. For example, in the ITT hydrocarbon deposit, which is one of our main targets, we have raised production to 80,000 barrels per day (bpd). But the potential is even greater, with scope for 200,000 bpd.

One of the main restrictions is that Petroamazonas lacks capital. As part of this government's austerity programme its budget was reduced this year. We are getting around that by inviting more private-sector companies, mostly international, to develop hydrocarbon projects. In the northern part of the jungle we already have all of the major infrastructure, such as pipelines and roads, that we need to develop the oil there. In the southern part of Ecuador, in blocks 86 and 87, we don't have the infrastructure needed to develop those oil projects.

There are also some social issues in the south, where tribes are against the industry. I believe that's because the government has not effectively explained the benefits and we will launch a new communication effort to show them how the industry can help develop their community. I think the south is more interesting for the majors because those blocks are less-well explored and have a much greater upside. The fields in the north are better-suited to mid-sized companies as they involve smaller capex but also have less upside. The biggest opportunities in Ecuadorian oil and gas will come when we open up the southern concessions, which we plan to do in the coming years.

**LAI:** *Ecuador has plenty of reserves; how high could production grow?*

**MP:** Our original plan on forming this government was to reach 700,000 bpd by

2021. I don't think we will make that target as the industry has been held back by delays on the environmental licenses in the north and tenders in the southern blocks. We are currently producing 560,000 bpd and I think we will end the year on 580,000 bpd.

Ecuador has 4.7 billion barrels of oil in proven reserves. The real figure is probably higher, for example in its annual energy review UK oil firm, BP, gives us a much larger figure. However, at the Ministry we like to use the most conservative, proven reserves amount. Either way that you look at it we have a lot of oil. Moreover, when you consider that global oil demand will probably stop growing after 2040, then it's imperative that we make the most out of our resources now. I believe the infrastructure needed in the south will take a few years to develop. When it comes online you would see a big leap forward our national production figures.

To attract the investment needed to develop our reserves and build the infrastructure we need to have competitive contracts. The service contract model that the last government had favoured was not very attractive for international companies. We've changed that to a participation contract, which allows companies to book reserves. Another crucial element is that they are fair. We use a formula that means when the oil price is high, both Ecuador and the companies benefit. And when it is low, we both suffer. That fairness has helped it attract oil and gas firms.

For example, in our Intracampes Round we had successful bidders for seven of the eight contracts offered, with a total investment of \$1.2 billion. It's also worth mentioning downstream. We need to upgrade our refining capacity as we currently have to import petroleum derivatives. Our existing refinery in Esmeraldas has to be upgraded to comply with new shipping fuel sulphur regulations, while we also need to boost

capacity with a new refinery.

**LAI:** *Tell us about the country's exciting renewable energy plans.*

**MP:** Ecuador already has a very green grid, with 85% of our electricity generated by hydroelectric plants. However, that dependence on hydro means that during rainy seasons we have a surplus of power, that we export to Colombia and Chile. But during September and October, when it is the dry season in the east of the country where most of our power plants are located, we have less hydropower. So, we want to balance our grid by building renewable projects on the west side of the country. We are looking at wind and solar. We will also have some natural gas to provide relatively clean baseload power. The gas plant will be between 500 MW and 1,000 MW and will also involve a gas import terminal as our local supplies are not sufficient. Finally, there are still two excellent, and very large, hydroelectric projects to be developed.

We have been blessed by nature so these wind and solar projects have incredible efficiency numbers. For example, the 110MW wind farm that we are tendering in Loja has a plant factor of 50%. We will be holding auctions, where the winning bids will have guaranteed PPAs from the state electricity company. We are also open to private initiatives from investors.

So, if someone approaches us with a renewable project that can guarantee clean energy at a competitive price, we will also give them a PPA and declare their project of national interest, which will speed up development. We also want to switch the Galapagos Islands from fossil fuels to renewable energy. That is a great opportunity for a renewable energy company to have a project in one of the natural wonders of the world.





# Gold Rush

*More gold and copper have been found in Ecuador in the last ten years than anywhere else on earth...*

Ecuador's metallic riches have been sought after since the days of the Inca empire. Gold mined from the south of modern-day Ecuador, in a province that is now called El Oro, was turned into intricate religious and ceremonial jewellery prized by the Incan's ruling class. Yet despite half-hearted attempts by the Spanish and then other international investors following Ecuador's independence in the 19th century, the country never fostered the type of large-scale mining industry that arose in Mexico, Brazil, Colombia, Peru or Chile.

Mining remained small scale, with an array of locally-owned mines in the country's south operating with varying degrees of formality. Different attempts by foreign miners to establish large operations during the 20th century were expropriated or sidelined as political instability brought radical changes in mining policy. As a result, no large sums of international capital, or leading technology, were brought to bear on Ecuador's mineral resources.

## Geological riches

But in today's globalised world it's increasingly difficult for national anomalies to buck international trends. As mining investors made fortunes along the Andes from Chile to Colombia, attention began to turn to the odd one out. Could it really be possible that Ecuador, blessed with so many other natural resources, just happened to have the only stretch of the Andes that couldn't support large-

scale mining?

Clearly not, says Giovanni Espinosa, CEO of Enami EP, Ecuador's state mining company. "Ecuador has a privileged location, immersed in the metalogical belt that runs along the Pacific Coast of South America, from Colombia to Chile. Only 10% of the country's territory has been explored for minerals, which shows the potential we have for further



Ron Hochstein, CEO of Lundin Gold

discoveries... Indeed, we've seen more mineral finds in Ecuador in recent years than anywhere else on earth."

That bullish view is shared by international mining firms. Jason Ward is the Country Manager of Solgold (LSE:SOLG), an Australian headquartered, Ecuador-focused London-listed, copper and gold miner. "The incredible scale and richness of Ecuador's mineral deposits allow you to make ambitious plays that wouldn't be possible elsewhere. If you look at us, we have 12 more targets to test which

will likely result in more discoveries. I can't see other countries with that type of scale and growth potential. Ecuador has not been explored compared to its neighbours and has multi-billion tonne deposits that can be turned into multi-generational deposits."

But it's not just that Ecuador has lots of metal, explains Nicholas Mather, Solgold's CEO. It has the right metals.

"Solgold is a porphyry copper-gold

**“The exit of Kinross really sent a strong message to the Ecuadorian government, which made them more willing to work with us**

exploration specialist. We like those targets because they contain two of the commodities that the world has an inexorably increasing demand for: copper and gold. The former will benefit from the move to renewable energy and electric cars, while the latter is the ultimate form of money." Solgold's prolific series of discoveries show that Ecuador is rich in both copper and gold. "Cascabel is the first [target] that will be developed", says Ward. "The MRE 2 showed 10.9 million tonnes of copper and 24 million ounces of gold, with another resource upgrade

due later this year.”

As a result, now no one doubts Ecuador’s mineral potential. But then it hasn’t been a lack of metals that has prevented the emergence of a modern mining industry in Ecuador. It’s been the legal, regulatory and fiscal conditions above ground that have scared off miners.

### Above ground

In 2015 the government of Rafael Correa unveiled new, investor-friendly mining taxes. In an unexpected move for a socialist firebrand that had previously tried to squeeze the industry, Ecuador hired international natural resource consultancy, Wood Mackenzie to help draft the fiscal regime. On paper Ecuador now had a solid mining law but given the country’s inconsistent track record with international investors – it is one of only two Latin American

countries to default on its sovereign debt in the 21st century – many were still nervous about committing capital. One of the first to make their move was Lundin Gold, which is part of the Lundin Group of Companies, a collection of publicly-listed resource-focused companies that are backed by the Lundin family from Sweden. Lundin Gold CEO, Ron Hochstein, remembers first scouting out the project in 2014.

“I came with Lukas Lundin to Ecuador to look at the Fruta del Norte project – one of the best undeveloped gold deposits in the world because of its size and gold grade. We had meetings with Kinross of course but Lukas also wanted reassurance from the government that it was serious about developing a mining industry. We judged that it was and then we moved forward, raising the equity to buy the property, which was tough both

because of Ecuador’s history and the challenging gold market at the time.”

Hochstein believes several factors strengthened Ecuador’s commitment to develop its mining industry. “The exit of Kinross really sent a strong message to the Ecuadorian government, which made them more willing to work with us. Also, the falling oil price in a dollarized economy that couldn’t devalue its currency like its neighbours increased government appreciation for mining. The higher oil prices had helped Ecuador to improve the standard of living and the country’s infrastructure, but these factors meant that many political figures began to see mining as a way to keep those gains in a period of low oil prices.”

Ward agrees that this government is serious about mining. “I think the political environment here is very ▶▶



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supportive of mining. We are starting to see established mining countries, such as Canada and Australia, reject projects because they are wealthy countries. Here Ecuador is just at the beginning of the journey and wants to use mining to have the economic growth that Canada and Australia have enjoyed. If you respect the laws here and act like a model company, you will get support.”

Miners already operating in the country also praise this government’s willingness to learn from its own mistakes. Ecuacorriente is the local

the government in 2013 and by 2019 had built the mine plus a processing plant capable of 60,000 tonnes of ore per day. Meanwhile Lundin began construction in July 2017 and was already producing by the fourth quarter in 2019. That shows that, despite the country’s reputation for stifling bureaucracy, mining projects can be developed quickly in Ecuador.

Ecuador also has several infrastructure advantages, says Mather. “It’s a small, compact country, packed with great mining targets. For Alpala we will have to build just 30 km of road to connect

fail, with only 3 in 1,000 becoming a mine. They are terrible statistics. I’d rather be working in Ecuador with a great chance of finding something than be drilling away in a perceived positive jurisdiction which has been over explored and has less chance of discovery.”

## Communities

Ecuador’s government also took a proactive approach with community relations. Across the world mining investors have learned the importance of gaining local support. However, in Latin America the combination of decentralised political systems, with weak states that lack presence in remote areas and an array of indigenous cultures, means that community opposition to mining projects can be particularly strong.

Ecuador created an advanced royalties programme, which means miners have to make upfront payments to the government for it to spend on community works around the project. They are significant sums, for example Ecuacorriente has paid about \$85million, which impact the net present value of a project, but help build local support for a mine. The government uses the money on amenities such as hospitals, water sanitation and schools, so the community benefits from mining before they started to see other impacts, such as increased truck traffic. Miners are then able to recoup the money from future royalty payments.

Of course, the government can’t handle all of a mine’s community relations. The advance royalties programme should help the project get off to a good start but then it’s down to each company to ensure that the community remains onside as the mine grows. Ward believes that its particularly important that the pioneers, like Lundin Gold and



**In developing Alpala, Solgold has been careful to protect the surrounding environment**

company of two behemoth Chinese conglomerates that have built, a \$1.5 billion copper project that became Ecuador’s first modern, large-scale mining operation when it entered into production in July 2019.

Mauricio Núñez, Ecuacorriente’s Vice President of Legal Affairs, hails the government’s willingness to listen. “They changed the sales tax structure, which allowed us to reclaim VAT once exports started. That helped boost the country’s competitiveness. They also removed the windfall tax, which was a real disincentive to investment.

Núñez’s positive assessment is backed up by the facts. Ecuacorriente signed its investment contract with

the mine to the country’s excellent highways. In other countries you have to build hundreds of kilometres of road to connect mines. The same goes for water supplies, which are abundant, and the electricity matrix, which is cheap, reliable and very renewable.”

Of course, challenges remain. For example, the closing of the mining cadastre has stalled the development of fresh projects. Meanwhile regulatory agencies are slow to issue permits as they struggle to gain the expertise and scale to handle the mining boom. However, Ward believes these teething problems pale in comparison to the potential. “The biggest risk in the mining industry is geological – not political. Nearly all exploration projects





# **SolGold is a leading exploration company focussed on the discovery and definition of world-class copper and gold deposits in Ecuador**



**SolGold first entered Ecuador in early 2013, and has since established Alpala as a Tier 1 copper-gold project. The resource at the Alpala deposit boasts a high grade core which will target early cashflow and an accelerated payback of initial capital.**

SolGold is currently investigating development and financing options to bring the project through to feasibility stage.

The geology and mining industry of Ecuador has been endorsed by a number of major companies investing in the country.

SolGold is the largest tenement holder in Ecuador. SolGold used its successful and cost efficient blueprint established at Alpala, to explore for additional world class copper and gold projects across Ecuador.

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SolGold employs a staff of over 650, 98% of which are Ecuadorean. We expect this number to grow significantly as the operations at Alpala, and across the country expand.

**LSE: SOLG**

**TSX:SOLG**



Solgold, don't have a negative social or environmental impact. "From the very beginning we realised that we had to be a model company. That's because we are going to be one of the first major mining projects in Ecuador, so it's vital that we prove the industry can be responsible and sustainable. But also, because we have many more targets in the country, so Cascabel is our way of showing other communities that we can deliver economic and social development."

The problem, says Ward, is that much of the country doesn't really understand modern, responsible mining. "Most mining in Ecuador up to now has been informal and set a bad precedent." It's a point echoed by Carlos Pérez, Minister for Energy and Non-Renewable Resources. "We have to show a different face of mining industry to the Ecuadorian people because the bad examples they have seen so far have triggered opposition from environmental and social groups. As a government we are attracting international companies, with best practises that will bring responsible mining to the country. Our challenge is to make the protestors realise that." The government recently cracked down on 10,000 illegal miners in Buenos Aires, Imbabura province. Investigation revealed the mining operations were linked to organised crime groups from Ecuador, Venezuela and Colombia.

## Anti-mining movement

"I think if you take a bell curve of society's perception of mining you will find small amounts of people at either end who are intensely in favour or opposed to the industry and will never change their opinion", says Ward, "and a big majority in the middle who are open to learning about its impact. We have been appealing to rational Ecuadorians and showing them the

massive benefits that a modern, responsible mining industry can bring. I would say that every year since 2013 the overall attitude towards mining has improved slightly."

Choosing, modern, responsible mining instead of illegal, unsafe extraction would seem a no-brainer. But communities don't always understand the difference. Moreover, internationally-funded, anti-mining NGOs, that are opposed to any form of the industry, often spread misinformation and fake news about the new projects to stoke local opposition. In some cases, the protest leaders have even been found to have links to the illegal miners.

Javier Robalino Orellana, Managing Partner of Ferrere, Quito's leading corporate law firm and a specialist in mining, believes the sector needs more support. "It's important that the State continues sending a strong message in favour of large-scale responsible mining. I feel that's been missing recently."

Just before this magazine went to print, those in favour of modern, responsible mining received a huge boost from the Constitutional Court's decision to throw out two requests for mining referendums. Ecuador's mining industry had been nervously awaiting the decision, as the referendums could have meant that huge swathes of the country's mineral resources would be off limits to new mining projects. In theory the court ruling should never have been in doubt, says Robalino.

"My legal interpretation is that the Constitutional Court should continue rejecting these referenda requests as mining, just like water, oil or telecoms, is a strategic sector subject to central government policy."

That doubt was like a Sword of Damocles hanging over the industry and its removal is a positive step for both mining and Ecuador in general. "Mining is permitted in the constitution. It cannot be banned."

The decision was a vindication for the likes of Lundin Gold and Solgold that believed in the country from the beginning. Ward, who has lived in Ecuador since 2013, when Solgold came to the country, feels his company's faith has been rewarded. Now, notes Ward, Ecuador "is the focus of a modern gold rush with many of the world's largest mining companies already setting up offices here. As an early mover, we're happy to see more of the industry realise that this is the place to be. We've got the best projects and the influx of new companies should help broaden the industry's position in the country."

Lots of the most famous successful trades - think Soros shorting the pound or the hedge funds that spotted the US subprime crisis brewing - involve identifying an anomaly that isn't sustainable in the long run. There are country-specific reasons why Ecuador didn't develop a large-scale mining industry in the 20th century. But it seems unlikely that its citizens would have been content in the 21st had their country continued to miss out on the economic and social development mining has brought to their neighbours.

With tens of billions of dollars pouring into projects along the Andes it was only a matter of time before Ecuador opened up to international miners. The early movers may be reaping the advantages now but the sheer scale of Ecuador's opportunities mean there is plenty more to come for new investors. LatAm INVESTOR readers should take a closer look at the country.

# The Benefits of Mining in Ecuador

# **RESPONSIBLE MINING**

**4%**

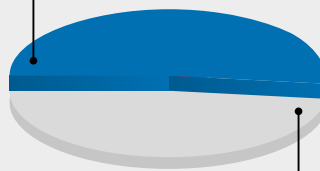
Contribution to GDP to 2021

**\$2.9 billion**

Projected investment to 2021

**53%**

Responsible mining



**47%**

Other sectors



**10**

Ecuadorian universities offering mining degrees

**267**

community projects funded in

Azuay, Imbabura and Zamora Chinchipe among others



**\$147 million**

Invested in local communities around projects



**33,000**

Direct jobs created by 2019



**\$715 million**

Mining tax revenues through to 2021



**1** Large-scale mining project in construction

**1** Large-scale mining project in production



**10%**

Mining tax revenues through to 2021

(This is likely to increase as Ecuador's mining industry matures)



Leading mining companies from Australia, Canada, Chile, the UK and the US have already invested in Ecuador



## Areas likely to see a positive impact



Generation of local supply chains



Increase in local authority tax take



Boost to local economies



Increased coverage of basic amenities in rural Ecuador



Development of social projects







# Brave New World

*Ecuador is starting a large-scale mining sector from scratch and it will transform the country...*

In homes and offices across Ecuador, excitement is growing about the coming mining boom. In July the country's first large-scale mining project started production, with a second mine due to begin operations in autumn. All of a sudden, mining, which had been touted as the panacea for Ecuador's struggling economy since the dying days of Rafael Correa's administration, seems real. Ecuadorians don't have to look far to see what the industry could do for their country. Chile has built Latin America's richest economy on the back of a well-organised mining industry.

Mining has the potential to solve many of Ecuador's acute needs. In particular mining can create macroeconomic stability, generate well-paid formal employment and transfer technology to local companies. For individual Ecuadorians it's a unique opportunity to better their standard of living while for the country it's a way to drive economic development. These benefits are important to investors too. The only way the industry can be successful in the long-run is if it benefits Ecuadorian society. Widespread public acceptance of mining will help protect it from the radical swings that characterise Ecuadorian politics. So, the onus is on international mining companies to ensure that Ecuador gains as much as possible from the industry.

## Dollar darling

For more than a decade Ecuador has been shunned by international investors. Its lowly status hit rock bottom in 2013 when Ecuador received the lowest amount of foreign direct

investment (FDI) per capita in the entire Latin American region. It's never nice to be ignored but the lack of investment is particularly dangerous for Ecuador, whose dollarized economy needs an inflow of hard currency – either from exports or FDI – to finance government expenditure. Ecuador brought in the dollar in 2000, in the midst of a financial crisis that had sent its old currency, the sucre, into a hyperinflation of 100%. Until 2014 high oil prices provided the export earnings Ecuador needed to maintain the dollar. But the subsequent oil price fall demonstrated the danger of depending on one volatile commodity and raised the spectre of Ecuador having to ditch the dollar.

That's why, in its final years, the government of Rafael Correa turned to mining. Correa may have been a populist but he also has an economics PhD and realised that the industry could diversify Ecuador's export earnings, attract

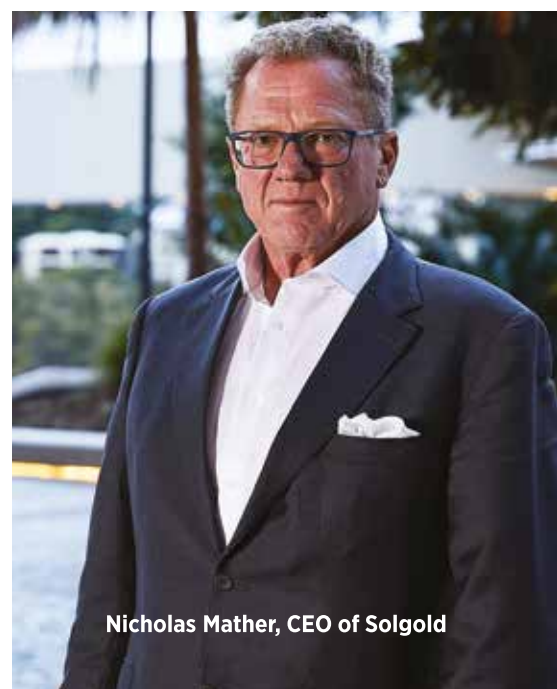
foreign direct investment and thereby increase the country's macroeconomic stability. The dollar is incredibly popular in Ecuador and trying to switch back to the sucre would be political suicide. Yet that could be forced on Ecuadorians by a prolonged period of low oil prices in the future. Now, thanks to mining, Ecuador's dollarized economy is a lot more sustainable.

This international investment isn't some abstract economic theory – it's already happening. In 2018 FDI to Ecuador increased by 126% to \$1.4billion. More than half of that money, 53%, came from mining. It's estimated that mining will lead to \$2.7billion of further FDI between now and 2021. All of the international investment is also helping with Ecuador's two other big problems – jobs and government spending.

## Work needed

Ecuador suffers from a lack of formal

**“Our ambitious plan could eventually help turn Ecuador into the second-largest copper producer on earth, creating opportunities for smelting, refining and manufacturing**



Nicholas Mather, CEO of Solgold

employment, which is why president Lenin Moreno pledged to create 500,000 new jobs by the end of his term. He looks unlikely to reach that goal as Ecuador's outdated and rigid labour market acts as a disincentive for employers. Indeed, his hopes now rest on passing a labour reform this autumn. However, in the meantime the mining industry is coming to the rescue with 33,000 direct jobs created so far.

In addition to the direct employment, the long supply chains of these vast mining operations also generate much more indirect employment. Ron Hochstein, CEO of Lundin Gold, whose goldmine, *Fruta del Norte*, enters production in the fourth quarter of 2019, has been working hard to involve local firms in the project. "We could contract everything in Quito but instead we foster local firms. The biggest success was with our catering company. Under Kinross these had been direct employees but we thought we could help them develop their own company. So, we decided to put the catering services out to tender and a new company made up of local former employees managed to win the contract. The Lundin Foundation gave them consulting and a loan for \$100,000 of working capital and from that beginning it has gone from strength to strength. It is now one of the largest businesses in the province, employing over 250 people. Moreover, it is having a further multiplier effect as other local people form companies to supply it."

"Before, most people in Ecuador thought that all natural resources were the same but examples like this show that they are not. Oil has the potential to generate lots of income for a country but mining can create many more jobs and related economic activities. Once you have a well flowing into a pipeline it doesn't need much to keep it going but mining can generate economic development due to the higher number

of employees and purchase of local and national goods and services throughout the operations phase."

### Tax take

Ecuador's government is – to use the technical term – broke. Under Correa it went from having the lowest government expenditure per capita to the highest. That proved unsustainable when oil prices fell and Correa had to borrow money from China through murky, oil-linked deals. As a result, his successor, Moreno, who inherited a fiscal crisis and burdensome external debt, had to go cap-in-hand to the IMF. In return for a \$10billion package of loans from the IMF and other multilaterals, Moreno has promised to cut government spending and raise revenues. In practice this has proved difficult and will need structural reforms to be passed by Congress in autumn. However, in the meantime mining has come to the rescue, with the industry expected to generate \$715million of taxes for the government between now and 2021.

All of the statistics mentioned above are impressive but they are only the beginning. Ecuador's mineral riches means it has the potential to become a global mining powerhouse. Hochstein, believes mining can reshape Ecuador's economy. "Ecuador has an incredible geological endowment and with the right conditions we could see mining grow to be around 20% of GDP like in Peru."

w Mather, CEO of Solgold, a copper and gold explorer that is developing a copper-gold mine in Ecuador and has a string of further concessions to be developed in the future, believes Ecuador can become a significant player in world mining. "Our ambitious plan could eventually help turn Ecuador into the second-largest copper producer on earth, creating opportunities for smelting, refining and manufacturing."

### Local partners

"There is a misguided perception that mining began with the arrival of the international companies", says Juan Carlos Peña, Commercial Director of ExoLuxen, a small gold mining and processing operation in Ecuador's southern province of El Oro. "Actually, there is a thriving industry of small to medium-sized local gold miners in the south of the country." Critics accuse the existing local miners of tax avoidance, environmental damage and money laundering for narco groups but Peña rejects the accusations. "Like in any industry there may be one or two payers breaking the rules but most of the Ecuadorian mining companies are responsible"

The smaller, local miners could prove interesting partners or acquisitions for incoming foreign firms looking to establish a foothold in the Ecuadorian market.

Another local player with partnership potential is Enami EP, the state mining company set up in 2010. Being the national company means Enami has been given some choice concessions and interesting tax breaks. However, Giovanni Espinosa, Enami's CEO, believes the firm's main asset as a partner is its network of local contacts. "Being a state company means that Enami offers solid intergovernmental relationships that streamline the paperwork and processes for developing a mine. Moreover, partnering with the national mining champion earns you goodwill with the local communities around your projects. Our social programmes and mechanisms are very strong and will help us avoid protests."



Indeed, Mather is conscious that Solgold's projects must meet Ecuador's economic needs "The most important reason why investors in Solgold can be sanguine about the political risk of our project is that we are partnering the country. If you look at our development plan, we're not looking to high-grade the deposit and leave with big profits. We've designed it to maximise the lifecycle, which means more revenues for the government and employment for Ecuadorians... We've aligned our goals with the Ecuadorian people, which makes it politically sustainable in the long run."

Mauricio Núñez, Vice President of Legal Affairs at Ecuacorriente, the Chinese-backed firm that started production at the *Mirador* copper mine this July, notes the project will continue to benefit for Ecuador for many years. "We have already invested \$1.25billion, paid \$140million in taxes and paid \$85million in advanced royalties. But there is plenty more to come. We estimate that *Mirador* will generate \$4.2billion of production throughout the life of the mine, which will give the Ecuadorian economy a significant boost."

## Technology

Latin America is notoriously bad at investing in research and development. There are many regional factors at play, for example not a single Latin American university makes the top 100 global ranking, but Ecuador scores particularly poorly. According to the UN, Ecuador invests just 0.4% of its GDP on R&D compared to 1.7% in the UK. One fast way for Ecuador to catch up is for international firms to transfer technology to local ones. And that's exactly what's happening in the mining sector.

Building Ecuador's first large-scale subterranean mine meant Lundin Gold required expertise, technology and skills that weren't available in Ecuador, says Hochstein. "We needed to develop eight kilometres of tunnel so we contracted a joint venture made up of local EPC firm, Semaica, and a Chilean mining specialist, Mas Errazuriz. Semaica is a well-respected player in Ecuador that has underground experience with road tunnels and hydro plants but it needed some mining expertise from its partners. It successfully completed the tunnel for us and now Semaica has the expertise and technology to work on other mines in Ecuador."

**“ We recently finished Ecuador's largest ever mining tunnelling project for Lundin Gold ”**

The Semaica story is interesting because it serves as a case study for how Ecuador can leverage its mining boom and build a local service industry. For most of its history, the firm had nothing to do with mining. "Semaica is a two family-owned, Ecuadorian engineering and construction firm", explains the firm's Technical Director, Mauricio Martínez. "In a large country you have construction firms that specialise in a particular area, say roads or hotels. Yet my father, who founded this company with his close friend and partner, always told us that because Ecuador is a small country we should "specialise in Ecuador". What did he mean? That we have to adapt to what the country needs in each particular age. Twenty years ago, there was a hotel boom in Ecuador and we built the Marriott, Hilton and Sheraton at the same time in the same city. During that time people thought that we were hotel builders, but for the next 10 years there were no more hotels in Quito, so we focused on hospitals, universities, sports facilities, etc. And throughout our history we built what the country required."

What helped Semaica, and many of its peers, prepare for the mining industry was a spate of Ecuadorian energy projects. Over the past two decades the country has built sophisticated hydroelectric plants and hydrocarbon facilities.

"About 25 years ago we moved into civil engineering and tunnelling projects", recalls Martínez, whose firm is now one of Ecuador's leading hydroelectric plant builders. "It started with water tunnels for irrigation, as Ecuador has lots of water but in the eastern region instead of the highly productive Andes valleys. That tunnelling expertise also helped us win important road projects, as Guayaquil also has lots of traffic that needs to be moved to the other side of



**Semaica's Technical Director, Mauricio Martínez**



the hills. The emphasis on engineering and civil works transformed our company because it helped us gain the experience and skills to allow us to move later to the mining sector.”

With its project portfolio giving it the equipment and engineering experience all Semaica needed was a specialist mining partner, says Martínez. “In a consortium with Mas & Errazuriz, a Chilean company that has a lot of experience in subterranean mines, we recently finished Ecuador’s largest ever mining tunnelling project for Lundin Gold. It is an interesting project because it is the first time that an international mining company develops a world-class gold deposit in Ecuador. So, this is a huge mine, involving thousands of people that will last for decades. We built eight kilometres of tunnels – four down and four up – which allows them to send equipment and people to the bottom of the mine and return

with ore. This is Ecuador’s first taste of modern, responsible subterranean large-scale mining and it’s a great honour for Semaica to be involved in this project. More than just an honour it has also allowed us to become a leading engineering and construction player in Ecuador’s burgeoning mining industry.”

The arrival of international mining to Ecuador won’t just bring new technology; it also brings best practices from around the world. “In our job with Lundin Gold we realised that this company’s first priority is safety”, says Martínez. “If you don’t make that as part of your company’s DNA then you won’t get the work. These international mining companies prioritise safety above production, speed and even cost. That’s because they realise that in the long-run the industry isn’t sustainable if it’s not safe...That insistence on safety may be a barrier to entry for some Ecuadorian firms, who find it difficult

to change. For us, now we have made it part of Semaica’s DNA, it has become a competitive advantage... We found that once we’d integrated the safety-first concept into our entire business then it didn’t impact on the speed or cost of our projects. The best proof of that is the Lundin Gold project, which was completed six months in advance.”

Mining and Ecuador are a good fit. Ecuador has plentiful deposits of the copper and gold that miners need. Meanwhile the industry can provide the macroeconomic stability, jobs, taxes and technology that Ecuador requires. Mining will transform Ecuador and create wealth both for its people and the investors who risk their capital to launch the country’s large-scale mining sector. UK mining firms are strong in neighbouring Peru and Colombia – now it’s time for them to look for opportunities in Ecuador.



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## TRADE SPOTLIGHT:

Minister for Production, Foreign Trade, Investment and Fisheries,

## Iván Ontaneda,

explains why economic growth will pick up...

**LATAM INVESTOR:**  
*How are you planning to increase Ecuador's exports to the UK?*

**MINISTER ONTANEDA:**

Ecuador has a very diverse export offer. Even if you strip out petroleum you see that we have earned a leadership position in many international markets with products such as banana, shrimp, cacao and flowers. They are our traditional export products where we have worked over many years to gain a strong position in the EU, the US and Asia.

We are fortunate to have this base of solid export products, however, our challenge at the moment is to diversify with new goods and services. These can be agroindustrial, which build on our strong existing exports, but also in new areas. To achieve this diversification, we have to improve our productivity so that more of our exports can be competitive in international markets. At the Ministry we have been identifying consumer trends in our key markets and planning how our local production can exploit these opportunities. We are fortunate that the geographic and natural diversity of Ecuador means that we can grow a wide variety of agricultural products and therefore serve many different market niches.

**LAI:** *What opportunities will that export growth create for investors?*

**MO:** To help boost our productivity we are developing an incentive programme to encourage international investment in Ecuadorian export projects. Our programme offers tax incentives and a stable, favourable regulatory environment that supports exporters.

completely reject that route. Instead we are improving productivity so that our goods can compete in the international market regardless of the dollar. That boost to exports also helps to balance our current account, reducing the need for external financing. Since coming to power this government has enacted

**“The previous Ecuadorian government relied on heavy borrowing to sustain dollarization. However, we completely reject that route.”**



The crucial thing for your readers to understand is that this emphasis on productivity-led exports is part of a fundamentally different economic model. Ecuador has a dollarized economy, which brings many benefits – for example currency stability for international investors. However, that also creates a higher cost structure than in neighbouring countries, such as Peru and Colombia that can devalue their currencies. The previous Ecuadorian government relied on heavy borrowing to sustain dollarization. However, we

a series of laws to improve conditions for investors and they are already starting to take effect. In the last 18 months Ecuador has seen a large increase in FDI, which shows that international investors have faith in our new business climate.

**LAI:** *How strong is the relationship between the UK and Ecuador?*

**MO:** I am in close contact with the British Ambassador, Katherine Ward,

and our two countries now have a great political and commercial relationship. Previously, despite the political problems, there has been strong and growing trade between the two countries. Now, with the more positive political context, we expect that trade to grow even more quickly.

The bilateral relationship is in its best ever moment and that creates all sorts of business opportunities. I am focused on attracting more UK investment to Ecuador. We have our trade office in London, ProEcuador, which acts as a first point of contact for British firms that want to learn more about the opportunities in our country.

**LAI:** *Explain how this government's attitude to private investors is different to its predecessor.*

**MO:** British investment, and international investment in general, has been low in Ecuador over the past decade because there was little confidence. We see examples from around the world of how, when countries inspire confidence in the business environment and judicial system, they attract international capital. With this government we've been building a judicial framework that offers guarantees to international investors, so they can be sure the rules of the game won't change. Guarantees that investors can have their returns, which is their main priority. Last year we passed a law to boost production, attract investment, increase employment and achieve fiscal stability. We are now adding to that with extra measures to further help investment and boost production. That's why we've seen investment grow under this government.

In addition to our laws there have also been historic international agreements. For example, the deal with the IMF, shows

a new level of financial responsibility and transparency. For international investors it's a strong sign that Ecuador is back as a serious member of the global community. International integration is key for us. That's why we signed the Continuity Agreement with the UK, why we are looking to join the Pacific Alliance and why we are strengthening our ties with key export markets in Asia and North America.

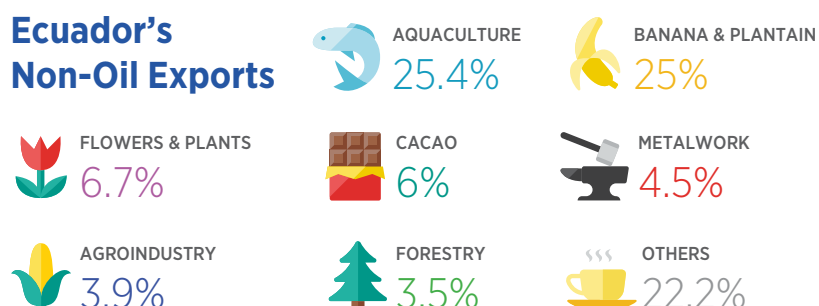
We realise that the world is becoming ever more integrated and for a small country like Ecuador to ride the coming waves of technology and innovation it is essential that we are part of international trade and investment networks. This government is trying to prepare the country so that it can ride the highway of growth. We know that trends such as the fourth industrial revolution and agriculture of the future, have the potential to catapult our country forwards. Ecuadorian people are hardworking and it's the role of this government to help the country position itself so that our citizens can benefit from the coming changes in the global economy. We want to make sure that Ecuador is ready for the 21<sup>st</sup> century.

**LAI:** *Ecuador is one of only two Latin American countries to default in the 21st century; is that now part of the past?*

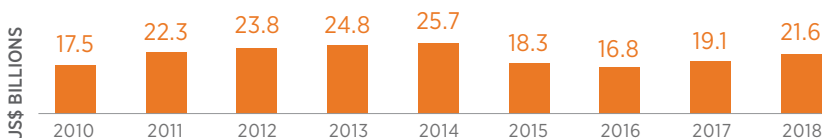
**MO:** When it comes to international investment the government of 2008 had a diametrically opposed view to the present administration. That is demonstrated by the laws, business environment and macroeconomic position that we have built during this administration. Investment decisions are based on perception so we have been very careful to send the right messages to the international community. Moreover, we have reinforced the new regulatory landscape, ensuring that it can't be easily changed on future political whims.

By signing up to international alliances and treaties we have guaranteed that future Ecuadorian governments will have to respect international investors' rights. For example, the IMF deal hasn't been easy for Ecuador but it's important to help us have working arrangements with other multilaterals and the international financial community.

### Ecuador's Non-Oil Exports



### Ecuador's Total Exports Including Oil



At present Ecuador's exports are closely correlated to oil prices, which leave the country exposed to volatile swings in its terms of trade. Minister Ontaneda is trying to strengthen Ecuador's external position by diversifying its basket of exports.



## Feed the World

*Ecuador's shrimp and banana exports dominate global markets but there is plenty of scope for the country to boost productivity and add value...*

For a small country Ecuador's agriculture sector punches above its weight. It's the world's largest exporter of both bananas and shrimp. What makes that even more impressive is the country's versatility. During the 19th and early 20th century it was a major cacao and coffee exporter. But when large-scale banana export farming was introduced in the 1950s, Ecuador soon became a global player. Likewise,

If it can solve these, then the country is well placed to benefit from rising world food demand in the 21st century.

### Natural blessings

One reason for Ecuador's strong agro-export industry is that it's been blessed with several natural advantages. Being on the equator gives it at least 12 hours of sun each day throughout the year, so there is no cold, dark winter to hit production. Depending on the crop that can allow for multiple harvests.

Ecuador's unique position also brings benefits to the banana industry, says Jorge Alex Serrano, CEO of Jasafrut, an Ecuadorian company that sells bananas under the Equapak brand to supermarkets in Asia, Europe and North America.

"We are the only major banana exporter in the southern hemisphere. That gives us a big advantage because it means that our peak harvest is at a time when production in the northern hemisphere is low. Moreover, another trait of our bananas is that they grow more slowly than in other countries. That would seem like a disadvantage, and it certainly means that we produce less fruit per hectare, but the final banana is a much denser product. Ecuadorian bananas' slow growing time mean they have more natural sugars than other bananas. As a result, it's a much more solid fruit that can withstand longer journeys and tastes great when it eventually arrives."



Jorge Alex Serrano, CEO of Jasafrut

**“Ecuador is the only major banana exporter in the southern hemisphere**

following the arrival of modern shrimp farming in the 1970s it didn't take Ecuador long to build up a strong position.

Banana and shrimp are now Ecuador's two largest non-oil exports, helping to diversify its economy. They look set to expand further as the growing global population and the rise of the emerging market middle class, boosts demand for high-quality, healthy food like Ecuadorian shrimp and bananas. Moreover, Ecuador's dominant position in shrimp and banana comes despite several structural challenges in key areas such as infrastructure and labour.

The biggest change within the year is from wet to dry season, which is particularly marked on the west coast. But even dry season is rarely a problem for farmers as Ecuador has abundant freshwater supplies. It's also far from the hurricane path that can devastate some of its competitors in Central America and the Caribbean. Meanwhile its coast is the site where the cold Humboldt Current, travelling north from the Antarctic, meets the warm El Niño current, coming south from Central America. The clash of currents, leads to one of the world's most abundant fish stocks. That supports Ecuador's tuna exporters.

That natural advantage has helped the Ecuadorian banana conquer distant markets, says Serrano. "Our position on the west coast of Latin America actually puts us at a logistical disadvantage to our competitors in major markets. For example, we are further from Europe than the banana growers in Colombia, Central America and the Caribbean. We are also a lot further from Japan and China than the growers in the Philippines. Nevertheless, thanks to their superior quality, our bananas do well in all of those markets."

### Social impact

Producing great tasting fruit is a



good start but it's not enough to win market share in developed markets like the UK. Increasingly consumers look for fruit that also delivers a positive environmental and social impact. For example, about ten years ago Tesco, began purchasing fruit directly from growers, instead of going through international traders. In addition to looking for competitive, nice fruit, Tesco wanted companies that met the stringent new environmental and social requirements being demanded by the UK market. Initially Serrano hoped to help his family's large banana firm work with Tesco, but when a large order from an existing customer made that impossible, he decided to set up Jasafrut in 2013. Since then he has been working with socially and environmentally responsible small-to-medium sized third-party growers to supply Tesco, and other supermarkets around the world, with his Equapak brand of bananas.

"One area where we are really strong is our community work through the Equapak Foundation. In other countries, Tesco tends to work with large plantation owners. Jasafrut is the one of the few organisations they partner that is made up of small growers. Tesco realised that lots of the small growers that supply bananas to Jasafrut, don't have the scale, resources or training to implement their own social responsibility programmes.

"So, we made an agreement with Tesco where they would shave a couple of pennies of the price of each box and give us the money to found the Equapak Foundation. It has allowed us to set up health and education programmes for the communities and workers around our banana growers. They've also given us expert advice so that we could really maximise the impact of the foundation. For example, instead of just gifting a computer to a

community, we have a computer lab with a trained assistant that helps the young children use the computers for productive purposes such as their homework. The Equapak Foundation helps Jasafrut stand out from other banana growers in Ecuador. While the fact we are helping such small growers implement these programmes helps us stand out from other banana growers in the region."

Politicians across Latin America often talk about adding value to agriculture. Normally they're thinking in terms of industrial processes, for example turning a pineapple into pineapple juice, which is regarded as more developed. But with social and environmental consciousness shaping demand in major markets, producing fair-trade, sustainable bananas is another way to add value.

## Ecosystem

Ecuador's natural advantages are a key factor in its strong agro-export position. However, technology, best practices and logistics all determine a product's competitiveness in the international market place. Traditionally Ecuador has imported key farming technology, such as machinery and agro-chemicals, from abroad but over the last two decades local players have begun to emerge.

A good example is Ecuadorian fertilizer, feed and

seed provider Agripac, that LatAm INVESTOR readers will remember from our 2015 Ecuador Report. Since we last interviewed General Manager, Gustavo Wray, Agripac's annual sales have hit \$300million, up from around \$200million back then. Agripac's growth story, shows how Ecuador's agro-export sector is becoming increasingly sophisticated. "We began life representing international firms like ICI, however, over the last decade we've begun to increase our proprietary production. All of our feed range, from pets to shrimp, is produced by us in Ecuador and now accounts for approximately 30% of group sales."

Servicing Ecuador's shrimp boom has driven growth, explains Wray. "Over the last five years Ecuadorian shrimp production has rocketed and recently overtook banana as the country's main non-oil export. Indeed, Ecuador is now the world's largest shrimp exporter. Agripac has been supporting that growth as we have invested heavily in our shrimp feed manufacturing




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 jorgealex@equapak.ec  
 (+593) 7 295 0469  
 (+593) 7 295 2000  
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 Sucre y Gral. Serrano  
 El Guabo - El Oro - Ecuador








facilities.”

Agripac has been fortunate that Ecuador’s shrimp industry has taken off. However, the boom has also bought its own pressure, explains Wray. “Ecuador’s new status as the world’s largest shrimp exporter means its produce has to fight international competition. In demanding markets, such as the UK, that means increasing scrutiny is being put on the whole production chain. So, we’ve obtained the highest food safety and quality certificates, such as Global GAP and HACCP, which ensures that shrimp raised on our feed can enter any market.”

It’s not just Ecuador’s shrimp that’s facing competition. The strong growth in the local market has attracted the world’s top feed producers to Ecuador. Yet Wray is confident Agripac’s feed can withstand the test. “Because we’ve invested heavily in our research centres and factories, we now have the same technology as the multinational feed producers.” As a result, says Wray, “our product is the same, or in some cases better, quality.”

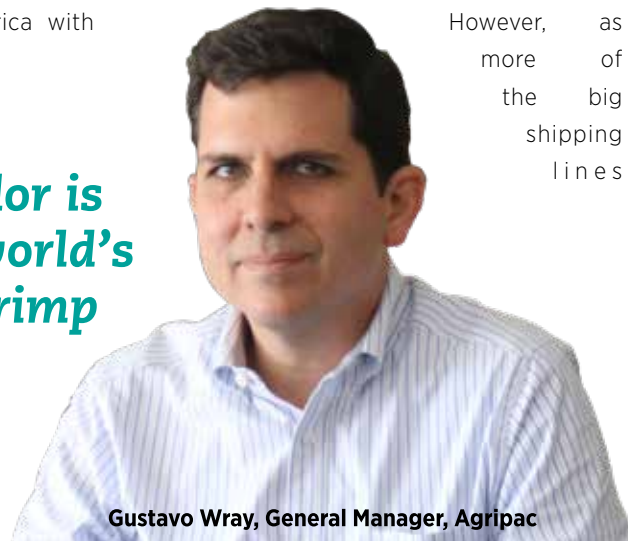
Wray’s confidence is supported, not only by Agripac’s growing domestic sales, but also its recent international expansion. “This January we opened our first store outside of Ecuador, with a new shop in Tumbes, in the north of Peru. Peru’s aquaculture industry is only just beginning, so our expertise and product range puts us in a good position to support its shrimp farmers.”

## Logistics leverage

Once farmers have produced excellent agricultural products, they then have to get them to market. That looks set to become a lot easier for Ecuadorian producers with the opening of the \$1.2 billion DP World Posorja container

terminal this year. It’s Ecuador’s first deepwater port and improves the country’s position on the global trade map, explains Ernst Schulze, the DP World Posorja CEO that oversaw the development of the project. “When the Panama Canal was upgraded in 2016 it led to the creation of larger NeoPanamax ships that can carry up to 13,000 containers. These larger vessels are the future of shipping in the Americas yet they were unable to dock at any Ecuadorian port. Now, with DP World Posorja, Ecuador is directly connected to the major shipping routes.” Posorja began commercial operation in August, with the EuroSal service that connects the West Coast of South America with the Caribbean and

“Ecuador is now the world’s largest shrimp exporter”



Gustavo Wray, General Manager, Agripac

Northern Europe. It’s a boost for British-Ecuadorian trade relations as the first European stop on Eurosal vessels coming from Ecuador is the UK.

“DP World Posorja is a cracking project”, says Nick Armstrong, President of the British Chamber of Commerce Guayaquil. “For years Ecuador has been planning a deepwater port and now it has finally built it. The existing port at Guayaquil is efficient and run by a well-respected international ports operator but it is limited by its access river. Ships visiting the port have to negotiate 60 kilometres of river, which is complicated by changing tides that

prevent larger ships from making the journey. Posorja is a purpose-built port on the coast, which can handle the biggest ships in the world. The fact that it can serve larger ships, and that they don’t have to deviate much from already established shipping routes, means that shipping containers to and from Posorja should be much cheaper than to Guayaquil port.”

The challenge at the moment, says Serrano, is the supporting infrastructure. “At the moment the transport cost of trucking goods the extra distance to the new deepwater port in Posorja makes it a more expensive option. However, as more of the big shipping lines

start offering services there then the maritime costs will reduce, making

the overall package more competitive. Moreover, DP World is building a barge terminal near Guayaquil that will provide a cheaper alternative to trucking containers to the port.”

Another benefit of DP World Posorja is that it’s pushing the pre-existing Ecuadorian ports to up their game, says Armstrong. “In the long term it can only be a positive for importers and exporters in Ecuador as it is also encouraging the existing ports in Guayaquil and Machala to improve



their offer. So, it gives us more options and it will make Ecuador more competitive. Eventually it should make Ecuadorian goods cheaper to bring to the UK and vice versa. Moreover, Ecuador has a strategic location so a deepwater port here has potential as a regional transshipment hub.” Indeed Schulze believes Posroja will eventually become a regional distribution hub for agro exports and a future phase of the project includes a 100-hectare logistics park.

## Challenges

The new port is a positive example of Ecuador tackling the type of structural challenge that can hold back its agro-exporters. However, there are plenty more hurdles to overcome. “We have the typical developing country problems”, says Jymy Riera of Banabio, a medium-sized banana producer from El Oro province in southern Ecuador. “The bureaucracy should be more efficient to support the export companies. Infrastructure is also a challenge. For example, some shipping lines don’t stop at Bolivar Port, our local southern terminal, so we have to truck bananas north to the Port of Guayaquil. That is hindered by

the poor state of the road. Ecuadorian agricultural exporters have been asking for this to be fixed for a long time and we hope more attention will be paid in the near future. However, it’s not all bad. We’ve been pleased with the help of ProEcuador in helping us meet potential international buyers in new markets.”

An expensive workforce is another problem that’s especially acute in the labour-intensive agriculture industry, says Serrano. “Our labour costs are very high with a minimum wage of more than \$400. Moreover, labour law is very rigid, with high penalties for firing workers. Moreover, social security obligations add 15% to the company’s cost per employee, while we also have to give each worker three additional pay cheques throughout the year, which increase the total average wage to \$600 per month. That forces banana growers to be conservative, because if prices drop and you have to reduce headcount it creates a hefty redundancy bill. In effect the redundancy bill exacerbates cashflow problems during difficult market conditions, and it has caused several firms to go bankrupt.”

The agro-exporters aren’t the only ones to have spotted these challenges. Both the IMF and the Moreno government have highlighted inefficiencies in Ecuador’s economy that need to be”, says Pablo Zambrano, President of the Chamber of Industries and Production, Ecuador’s largest chamber of commerce. “However, for it to improve the productivity and competitiveness of the Ecuadorian Economy there are five key areas that it needs to improve: electricity, labour reform, state bureaucracy, education and innovation.” We have presented this strategic plan to the government and are hopeful that it will manage to pass at least some of these reforms. Ultimately, it’s a transition government that doesn’t have to worry about being popular so it can take difficult measures.”

The IMF, which made the Ecuador loan on the understanding that it would implement structural reforms, will be hoping that Zambrano’s optimism is well founded. If the government does manage to make these improvements then Ecuador’s world-beating agro-export industries will become even stronger.



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## ECONOMIC SPOTLIGHT:

Minister of Economy and Finance,

# Richard Martínez,

on his plans to get Ecuador back on track...

**LATAM INVESTOR:**  
*How is your ministry trying to stimulate the Ecuadorian economy?*

**MINISTER MARTÍNEZ:**

The severe macroeconomic distortions accumulated over the last ten years demanded a radical change of policy and wide-ranging structural reforms. We created the Prosperity Plan roadmap that is based on four pillars: fiscal consolidation, monetary stability, equality of

opportunity, social protection and work, and the efficient, transparent management of resources.

It has been a difficult task of reengineering policy. Reconstructing the catastrophe of '21st Century Socialism' in the country will take lots of time, but at least now we are paving a path that will take us to a better place. Little by little, we are building a more reliable, stable and sustainable country with ordered public finances, international openness and a business environment that's attractive for private-sector investors. We are also deepening social assistance and welfare for the marginalised in our society. This titanic work of economic recuperation is a challenge but we have already achieved important results.

**LAI:** *What have been your main achievements so far?*

**MM:** In 2018 we cut the fiscal deficit to 3% of GDP from 8%, the lowest it's been for six years. That was helped by a bumper tax take of more than \$15billion, the highest since 2000. We have implemented an austerity programme and eliminated or merged 13 government ministries and departments. We also cut the pay of high-level bureaucrats by 15% and minister wages by 20%. Finally, our changes to petrol and diesel subsidies, saved the state \$432million.

But it's not just about the state, we've also stimulated the business environment. 2018 saw a record amount of private-sector investment, worth more than \$4billion. That's been led by our Production and Investment Law, which encouraged companies to pledge \$9.4billion of investment in the coming years. Meanwhile our non-oil exports grew by 5%. Outside of Ecuador our plans received a big vote of confidence with a package of loans from the IMF and development bank loans totalling \$10.2billion, while our new attitude is reflected in our current attempts to join the Pacific Alliance and the OECD.

**LAI:** *Ecuador has a fiscal crisis; how are you managing it?*

**MM:** We inherited chaotic fiscal situation, so we had to adopt firm and responsible decisions to clean up public finances. We reinstated the autonomy of the Central Bank and created a transparent register of public debt, which allows the public to know the exact amount of the country's external obligations. We also drew up a General State Budget, which sets spending limits for specific government entities to prevent unjustified spending.

We are also working on further reforms that we hope to pass in congress. We hope to improve local capital markets, refine the legislation for public private partnerships (PPPs) and, most urgently



of all, we want to reform the labour law and the tax code.

**LAI:** *What advantages, apart from the money, does the IMF agreement bring?*

**MM:** The backing of the international community, reflected by the IMF deal, shows the world believes in our Prosperity Plan. The international community decided to support the Ecuadorian state in our ongoing process of transformation and economic recuperation. Clearly the financial support is important to balance fiscal accounts but we've also used the money for social programmes, entrepreneurship and protecting the most vulnerable. Moreover, with this improved image of Ecuador, we are now more attractive to international investors and more likely to join groups like the OECD and the Pacific Alliance.

**LAI:** *How is your ministry trying to boost the competitiveness of the Ecuadorian economy?*

**MM:** This isn't just a challenge for Ecuador - in all of the region we see structural competitiveness problems. What's more, in the Ecuadorian case it's important to see where we're coming from and how we're changing. During the last decade, the private sector had limited participation as a motor of development. Now we are returning it to the role it deserves as the main actor in driving competitiveness and employment.

Clearly there is still a lot that needs to be done but the indicators already show an improvement. For example, the Economist's Infrascope ranking measures the environment for infrastructure PPPs. Ecuador climbed to 12th place in 2018, from 19th in 2017, thanks to the better political support for private investment and PPPs. The Economist notes that the government is pushing for the private

sector to lead large infrastructure projects. Indeed, the report shows that Ecuador is now above the regional average in terms of regulations and business environment.

We will keep working on the framework needed so that our economy can be competitive. We passed the Production and Investment Law, which has powerful tax incentives to boost economic output and employment. For example, there is no corporation tax on the profits generated by new investments for 12 years across the country, 15 years if it's for basic industry and 20 years for frontier zones and tourism. And the figures show that our approach is working. In 2018 we received \$1.4billion of FDI, a record high for Ecuador.

**LAI:** *The tax on repatriating dividends is an obstacle for foreign investment; will you cut it?*

**MM:** We have important reforms on the way that aim to give us a solid and efficient tax system that attracts investment. It is clear that the repatriation tax has failed. It didn't achieve its original objective, when it was created by the previous government, to stop dollars from leaving the country. Instead it just became another way of collecting revenue. However, to eliminate it immediately would impact the country's fiscal goals. As our macroeconomic situation improves, we will progressively try to reduce this tax.

**LAI:** *Will you sign a double tax agreement with the UK?*

**MM:** Ecuador and the UK are making solid progress with our bilateral commercial agreement. The double taxation agreement is one of our priorities and work on that will begin in October of this year. Also, as a

government we are open to one day signing a new investment treaty with the UK. This comes on top of the deal Ecuador, Colombia and Peru all signed with the UK in May to continue applying the preferential tariffs that currently exist under the EU deal.

**LAI:** *What are the best investment opportunities in Ecuador for UK firms?*

**MM:** Mining is an important sector for investors. Between now and 2021 we hope to receive \$3.8billion in mining investment, while the sector should generate exports of \$3.6billion. Over the same period the sector should account for 4% of GDP, so it's a massive opportunity for British investors.

We also have other strategic sectors that are important for external investors, such as our power grid, road infrastructure and oil and gas fields. We hope that British firms will be participating in the forthcoming tenders. Finally, there are a plethora of investment opportunities in private-sector projects, especially in agroindustry, tourism and real estate.

**LAI:** *How are you boosting British investment in Ecuador?*

**MM:** It's not just down to our ministry to attract international investment, all of the government is working on it. The flow of foreign direct investment from the UK to Ecuador is trending in the right direction but it is still too small. More British companies are coming and in 2018 we received \$35million, which was the largest annual UK investment in the last decade. Our aim is to increase these figures and we will do that by strengthening the relationship between both countries. Now we are a country that is open to the world and with a good business climate that encourages economic powers like the UK to invest.



# Creating Legal Certainty for Investors

*Ecuador's government has unveiled a new law to attract investment. We analyse how much protection it gives investors...*

No-one doubts that Ecuador has world-class mining, oil and agricultural investment opportunities. Nor do they question this government's willingness, even its need, to open these sectors up to international investors. But Ecuador's volatile political history, peppered with expropriations and defaults, scares off many investors. To assuage fears the government unveiled a new investment and production law. The *Ley Orgánica para el Fomento Productivo, Atracción de Inversiones, Generación de Empleo y Estabilidad y Equilibrio Fiscal* to give it its full title.

During LatAm INVESTOR's many interviews with various government officials, from minister level downwards, we repeatedly heard that the new law offers assurances for UK investors. Patricia Armijos, Sub-Secretary of Investment at the Ministry of Production, Foreign Trade, Investment and Fisheries, highlights that the law brings "long-term stability for national and foreign investors". She notes that "in addition to legal security, it grants a series of incentives for attracting new investments to the country". In particular, Armijos emphasises that the law allows the private sector to seek arbitration if the state breaks the terms of the investment contract with a company, which she sees as an important guarantee for investors.

Many in the private sector have reacted positively to the new law. In addition to serving as President of the British Chamber of Commerce in



**Javier Robalino Orellana, Managing Partner of Ferrere in Ecuador**

**“The deal with the IMF is an important step in the right direction**

Guayaquil, Nick Armstrong is also a director at Ecuadorian feed, seed and fertiliser provider, Agripac. "Along with other leading firms, Agripac made an investment commitment, because the new law offered tax incentives for investors", says Armstrong. "That encouraged us to buy a seed business from Pronaca and also to upgrade our feed mill and double its capacity so that it can meet growing domestic and international demand."

### Legal perspective

One person especially well placed to analyse the pros and cons of the new law is Javier Robalino Orellana, Managing Partner of Ferrere in Ecuador. Ferrere is the only multi-jurisdictional purely South American law firm, with 250 lawyers in Bolivia, Ecuador, Paraguay and Uruguay. While Robalino has represented multinationals in various local and international commercial and investment disputes. "The new

law is an improvement for investors", says Robalino, "but more protection is needed."

"In May 2017, one of the last acts of Correa's government was to cancel Ecuador's 11 remaining bilateral investment treaties. It was a spiteful act, designed to hamper future foreign investment as it removed security for foreign businesses coming to Ecuador. Three of the investment treaties, those with Italy, Netherlands and Spain, were renewed automatically but they are due to end in 2021-2022. Companies that had already invested before the cancellation are still protected under the treaties' sunset provision, however, any fresh investment is not. Ecuador is now working to renegotiate the treaties but they will have to be ratified in each country's parliaments, meaning it will probably take five years to recover all 11." "In the meantime, the idea is that the new law helps to attract investors by offering

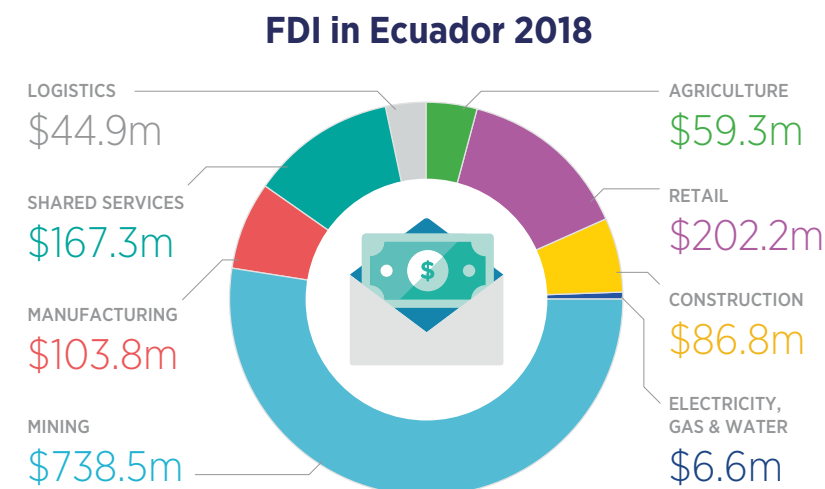


them some protection. Originally it was hoped that this law would include 'arbitration without privity'. This would allow private foreign investors, whose business has no contract with the state, to sue Ecuador if the country breached its investments rights, say by asset expropriation. It's one of the protections that existed in Ecuador's former bilateral investment treaties, so it was hoped the new law could bring this guarantee back. Unfortunately, the version of the law that was ultimately passed in 2018 was far weaker. It only allows for companies that have a direct contract with the state to have access to arbitration. Moreover, they can only dispute the narrow terms of the law – that is to say the company's investment pledge and the state's tax incentives. Arbitration under this law can't cover something more fundamental, such as expropriation. As a result, new international investors coming to Ecuador now have less power than they would have had under the old bilateral investment agreements."

So, this government has improved the situation but it still has some way to go before it completely repairs the damage of its predecessor. "The new production and investment law enhances the investment protection agreement – known as an IPA or *convenio de inversion*", explains Robalino, and "it provides tax incentives and certain protection." However, "the bilateral investment treaties are a broader umbrella protection that covered issues such as: fair and equitable treatment, expropriation, free remittance of funds, full protection and security and most-favoured nation status. It's vital that Ecuador signs new treaties. In the meantime, it must look for other ways to reassure investors."

### A lot done, more to do

It's doing just that, says Armijos. "The government has created the



Strategic Committee for Investment Promotion and Attraction [CEPAI by its Spanish acronym], which houses a multidisciplinary body for attracting and maintaining foreign investment in Ecuador. It approves investment projects and helps the private sector realise them." There is also a big push to improve the business environment, says Armijos, with Ecuador accepting a proposal from the World Bank Group to adopt measures to help the country climb up the Doing Business Rankings.

Indeed, one of the most exciting initiatives is the 'Single Window', which will attempt to cut through Ecuador's notorious red-tape by creating one point of contact for investors that need to interact with various government departments and entities. Finally, it is working on an upgraded version of the investment and production law, which it's hoped will be passed by congress at the end of this year.

Alejandro Echeverri, Chairman of the British Chamber of Commerce in Quito, is optimistic that conditions will improve for international investors. "A positive trait of this government is that it is willing to listen. We have seen repeated examples of suggested policies being modified after dialogue with the private

sector. That's a marked difference from the previous administration, which would threaten firms that tried to criticise its policies." Echeverri accepts that "legal security is a big issue for foreign investors coming to Ecuador as our history of changing the rules of the game understandably worries some international companies." However, he stresses that there are ways to mitigate these risks. For example, the chamber runs a conflict resolution centre that helps companies settle disputes without lengthy litigation in local courts.

Undoing a decade of '21<sup>st</sup>-century socialism' was never going to be an easy task. This government deserves credit for its efforts, but much still remains to be one. Robalino believes this is a "crucial period" for Ecuador. "In order to get a significant increase in foreign investment, Ecuador needs to show consistency. We need to demonstrate that we're a serious country. The deal with the IMF is an important step in the right direction, as it binds us to making improvements. Laws are good but what investors really need is stability, effective responses and steady policies." LatAm INVESTOR readers will be hoping that Ecuador's world-class investment opportunities are accompanied by better business environment.



## Power of Property

*As Ecuador's economy enters a period of prolonged growth, its property market looks promising for international investors...*

Throughout this report you'll have read about structural factors that should drive Ecuador's economy over the next decade. The opening of the mining industry will see inflows of vast sums of international capital and expat workers. The arrival of investment and people will be supported by the Ecuadorian oil industry's new turn to the private sector. Meanwhile the country's agro-export boom will funnel increasing amounts of dollar earnings into the hands of farming groups across the country. It all suggests that by the mid-2020s Ecuadorian GDP, which is currently

flatlining, will be growing at 5% per year. And one of the biggest winners of the country's economic boom should be its stagnating property market.

During the Correa years Ecuador's property market boomed. That was mainly down to high oil prices, which pumped money into the local economy, and the government's efforts to boost mortgage lending through the state bank. Unsurprisingly, when oil prices fell and finances dried up, the real estate market also suffered a correction. Now, with Ecuador's economy barely avoiding recession, the property market has stabilised, albeit at lower levels than the peak of its oil and credit-fuelled boom.

That context means Ecuadorian real estate is fairly priced at present. When the economic drivers highlighted in this report start to take effect it is likely the property market will

experience significant upside. In short, Ecuadorian real estate provides a way for international investors to play the country's strong economic growth in the future.

### Beachside profits

Ecuador's leading property developer is Pronobis, part of the Consorcio Nobis, a group of companies led by Isabel Noboa, one of Ecuador's wealthiest businesspeople. Since being founded in 1997, Pronobis has built around 50 projects, from international hotels to mixed-use urban developments. Its latest flagship project, Karibao, is a beachside community in Engabao, an unspoiled spot on Pacific coast, just 90 minutes from Guayaquil.

High-end, beachside community developments can be found across the Americas but Karibao is the first luxury project of its type Ecuador. As a result, Pronobis has been taking time to get it just right, explains CEO Juan Albán. "We spent the last few years fine-tuning the master plan, taking the latest trends and market needs into account. We've reduced the building density and increased the size of the spectacular crystal lagoon. The new design offers better views of the sea and more harmony with the natural spaces that surround the project."

Pronobis has also been tweaking Karibao's offer for investors. "We want to give our clients more customised options, so we now have apartments, land lots and single-family beach



Pronobis CEO, Juan Albán

“The real estate sector in Ecuador has to adapt to the new trends that the market demands



houses.”

Of course, Ecuador has plenty of nice houses by the beach, but what makes this project stand out is the scale, quality and amenities. Its main feature is a landscaped lagoon, developed by Crystal Lagoons, a Chilean firm with a unique water technology that’s now patented in 190 countries. But it’s also supported by first-grade infrastructure, such as a specially-built access road to the Guayaquil highway, a 16-floor apartment building and a club house.

### Upgrading Ecuador’s cities

The advantage of buying something by the beach is that if your investment plans don’t come to fruition you are still left with a spectacular place to spend your holidays. But for investors looking for a more diversified way to play Ecuador’s resurgent economy then there are interesting options in the country’s cities.

Like many urban conurbations in the spacious New World, Ecuador’s cities have spread horizontally. Coupled with insufficient public transport systems, that’s forced people to spend increasing amounts of time stuck in traffic jams between their work and homes. For example, in Guayaquil one of the newest residential areas, Vía a la Costa, is about 20 km from the city centre.

The solution, says Albán is to start building upwards. “The real estate sector in Ecuador has to adapt to the new trends that the market demands. For example, we need to develop mixed-use projects that include retail, residential and offices, that allow people to travel less, creating more time for themselves and their families. Another challenge is to develop innovative projects that generate sustainable development, using technology to create intelligent buildings that are more efficient.”

It’s an approach that ProNobis has pioneered in Ecuador over the last 22 years with its ‘ciudades dentro de ciudades’ (cities within cities) concept. In Guayaquil it has built Ciudad del Sol (Sun City), which combines offices, apartments and hotels with Ecuador’s largest shopping centre. It has also built Ciudad del Rio (River City), which combines offices, apartments and a hotel with one of the city’s most pleasant open spaces – a landscaped promenade along the River Guayas. Moreover, Pronobis isn’t just focusing on Ecuador’s largest cities, it has built similar mixed-used developments in smaller cities along the coast. There is a Ciudad del Mar (Sea City) in Manta to the north and another Ciudad del Sol in Machala in the

south. It’s also about to launch a new project in the highland city of Cuenca.

Perhaps the most attractive characteristic of Ecuador’s property market for international investors is that it is dollarized. “It means that investors have stable future returns”, explains Alejandro Echeverri, President of the British Chamber of Commerce in Quito. “Many people would say that Peru or Colombia are more attractive markets than Ecuador but when you look at the devaluation in their currencies over the last five years you realise that international investors will have taken a big hit. That hasn’t happened in Ecuador.”

It’s a good point, because even if some property in Colombia and Peru is listed in dollars, ultimately local wages, which help determine prices, are paid in local currency. In Ecuador the entire economy is dollarized, meaning investors don’t have to worry about currency risk.

In the 19th century, Baron Rothschild, who profited by investing during the Battle of Waterloo, famously quipped, “the time to buy is when there is blood in the streets”. Thankfully there is no blood in the streets of Ecuador, but its efforts to cut fiscal deficits constrain the economy. That’s cooled the real estate market and created a buying opportunity for several of the new projects being developed. But when Ecuador’s economy bounces back, property prices will soar.



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Ecuador's Ambassador to the United Kingdom,

## Jaime Marchán Romero

explains why his country is welcoming UK plc...

**LATAM INVESTOR:**  
*How is the relationship between the UK and Ecuador?*

### AMBASSADOR MARCHÁN:

The strengthening of Ecuador's relationship with the United Kingdom, established some 187 years ago, is an imperative of foreign policy defined by President Lenin Moreno. Following these directives, bilateral relations have begun to experience an encouraging upturn. Our purpose is to deepen the ties between our two countries.

**LAI:** *How do you plan to improve that relationship as the new Ambassador?*

**AM:** 'to these signals and, at diplomatic and political levels, the UK positively responded last June with the official visit to Ecuador of Sir Alan Duncan, the then

Minister for the Americas at the FCO.

**LAI:** *How will the removal of Julian Assange from the Ecuadorian Embassy help to improve the relationship between the two countries?*

**AM:** The end of the asylum of Mr Assange was resolved independently by Ecuador in strict compliance of international law and it was never conditioned to the improvement of our bilateral relations with the United Kingdom.

**LAI:** *How important is the Continuity Trade Deal signed between the UK and Ecuador?*

**AM:** The Continuity Trade Agreement signed between the UK and Ecuador confirms the commitment between the parties to maintain the current preferential tariffs and conditions established under the Trade Agreement with the European Union, in the case that the UK exits the EU without an agreement. It also establishes the willingness to start negotiations for a trade deal with the UK as soon as Brexit takes place.

The Continuity Agreement is very important since provides a clear indication to Ecuadorian exporters and British importers that trade will continue, in the same preferential conditions, after Brexit.

**LAI:** *Ecuador has seen some high-level political corruption*

*scandals. How much of a challenge is graft for British firms in Ecuador?*

**AM:** It's public knowledge that this government has implemented firm legal and institutional measures to combat the serious cases of corruption of the previous government and other cases that are being investigated. Thanks to these measures, now any individual or company can directly report corruption cases. The fight against corruption is one of the national and international priorities of the current government.

**LAI:** *Ecuador's previous administration defaulted on a sovereign debt. Does this government have a different attitude towards international investors?*

**AM:** In the Joint Declaration between Ecuador and the United Kingdom, signed during Sir Alan Duncan's visit to Ecuador, a trade and investment section was included in order to encourage greater investment by British companies in Ecuador. Both countries agreed to relaunch the talks towards an agreement to avoid double taxation, explore new initiatives to eliminate trade and investment barriers, and seek new opportunities to promote trade with the support of trade missions of both parties.

We are also resuming the talks to achieve an investment protection agreement with the British government. There is



already a proposal that will be examined with the British Government as soon as Brexit is resolved.

**LAI:** *What are the most exciting investment opportunities in Ecuador for UK?*

**AM:** We are promoting new tenders for Villonaco II and Villonaco III, two wind farms, while El Aromo is an exciting photovoltaic project. We will also continue to promote investment opportunities in mining projects. Some tenders will be announced soon, and we want British mining companies to participate in the process.

Moreover, with our future incorporation to the Pacific Alliance we hope to attract British investments in the food and beverage, agricultural, tourism infrastructure and pharmaceutical sectors.

**LAI:** *What are the most exciting trade opportunities in Ecuador for UK?*

**AM:** We see great potential to increase the participation of our products in the British market. The trend of British consumption lies in personal well-being, social responsibility, ethics, innovation and quality. These elements are aligned with our export offer.

It is important to highlight that part of our daily work as the Embassy of Ecuador in the United Kingdom is to identify business opportunities for British importers and Ecuadorian suppliers. In this sense, our Commercial Section (PRO ECUADOR) works on trade show encounters, trade missions and promotional campaigns, among others means, which have given successful results for the access of new products.

Ecuadorian suppliers participate in

the most important food and drink trade shows in the United Kingdom through our Commercial Section. For example, the IFE 2019. This trade show has allowed many exporters to access the British market. In addition, we are covering more niche markets with our recent participation at the Natural & Organic Products Europe Show, which focuses on natural and organic products with high nutritional value. This year, non-traditional fruits and bananas were promoted, through a trade mission organized within the London Produce Show.

We plan to expand the range of scenarios in which we will participate in the United Kingdom, in order to strengthen the access of our products after Brexit.

**LAI:** *What are Ecuador's competitive advantages as a trade or investment partner compared to other countries in Latin America?*

**AM:** The fact that Ecuador used the US dollar as its national currency allows firms to plan their investment in a more stable scenario. Our inflation rate per year is below 1%, which encourages secure investment. The Ministry for Production, International Trade, Investment and Fisheries has worked on a series of new tax incentives for new investments in our country. They will be grouped in two laws to promote production through foreign direct investment.

British companies have a great opportunity to

work with local companies both the goods and service industries. Many food and beverage producers in Ecuador have high-standard international certifications. This would allow them to be not only suppliers, but also co-packers of British brands.

Another opportunity for British companies specialised in food, flowers, such as roses, and fashion accessories, among others, would be that they can see Ecuador as a destination to open subsidiaries or factories of their products.

There are also plenty of opportunities to work together in other areas, such as technological solutions for agriculture, data protection management, bank transfers and product development. I would like to end by saying that diplomacy and trade and business opportunities work together since both consist in knocking on doors that will open new ways for reciprocal achievements.

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## Final Word

*Ecuador is opening up its economy to international investors and that's creating a unique opportunity...*

As you'll have read in this report, Ecuador has some world-class investment opportunities. In the mining sector, it's been the location for the planet's biggest gold and copper discoveries over the last decade. In banana and shrimp, it's the leading global exporter. And in oil and gas it's one of the few Opec members that is opening up untouched hydrocarbon basins to international investors. Meanwhile the economic growth that these sectors should generate is likely to boost its depressed property market. In short this is a once-in-a-generation opportunity for investors.

Ecuador's current appeal is based on its newfound commitment to attracting international investment. Investors will worry about how long that can be maintained. With elections

due in 2021 and ex-president Rafael Correa still able to rely on 30% of the electorate a volte face can't be ruled out. That's why it's so important that incoming companies use this window to demonstrate the benefits they can bring to the Ecuadorian people. As Solgold CEO, Nicholas Mather, explained in our mining feature, "The most important reason why investors in Solgold can be sanguine about the political risk of our project is that we are partnering the country... We've aligned our goals with the Ecuadorian people, which makes it politically sustainable in the long run."

Indeed, that's a theme throughout our report. Whether it's the banana company, JasaFrut, that has created a community foundation with Tesco, to benefit local people, or the oil service companies working in the jungle that take extra care with the environment. Pronobis even adjusted the design for Karibao, its beachside real estate project, to be more in keeping with local needs. For this new wave of international investment to be sustainable in the long-term it needs to avoid social or environmental problems.

### Pioneers

Being one of the first in a new inflow of international investors involves extra work. But it also comes with perks. The principal being that there is less competition. This doesn't just apply to new mining concessions or oilfields but throughout the economy. Nick Armstrong is the President of the British Chamber of Commerce

and Director of Agripac, a feed, seed and fertiliser firm, which has been in Ecuador for 40 years. "Once you learn to navigate the waters here, it is a very attractive market. It is a country where there is still a lot to be done, profit margins can be high and there is less competition... I can only draw on the experience of my own company, Agripac. Ecuador has been good to us."

Another interesting quirk of the Ecuador story is that it's not just opening up to international investors. It's particularly keen to attract British firms. That's partly down to Ecuador's efforts to wean itself off its dependence on China, whose influence grew in the Correa years. But also because the removal of Julian Assange from the Ecuadorian Embassy in London removed a thorn that damaged UK-Ecuador relations for many years. Armstrong says the benefits from the new mood between the two countries are already tangible. "The fact that the relationship between the UK and Ecuador is improving so quickly makes me bullish on the prospects for British firms in the country. We have had lots of visits by UK ministers to Ecuador in recent months while the Ecuadorians have reciprocated and sent members of their government." The visits have already yielded results with Ecuador signing a Continuity Trade Agreement with the UK.

British firms can be forgiven for overlooking Ecuador during the past, difficult decade. However, they won't forgive themselves if they miss the boom.



**Nick Armstrong, President of the British Chamber of Commerce, Guayaquil**



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