

USAID/Ecuador

Annual Report

FY 2004

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Ecuador

Performance:

Background: Civilian governments have held power in Ecuador since 1979. However, a lack of restraint, entrenched regionalism, and opportunism have all weighed against the development of stable governments that produce rational agendas. A week of indigenous protests in January 2000, backed by the armed forces, effectively removed Ecuador's president, Jamil Mahuad, from power and replaced him with then vice-president, Gustavo Noboa. Under the new president, Ecuador became fully dollarized by September 2000. In the latter months of 2001, Mr. Noboa completed the first International Monetary Fund (IMF) stand-by agreement since the 1980s. USAID's assistance was vital for the success of this agreement. After that, however, the rate of reform slackened. The resignation of the Ministry of Finance amid a corruption scandal in 2002 triggered a downward spiral in the fate of the Noboa Government. In November 2002, a former army colonel, Lucio Gutierrez, won the presidential elections and took office in January 2003.

A deficient political culture in Ecuador has damaged the effectiveness of policymaking. For example, interest groups impeded the effective handling of the 1998-1999 banking crisis. Cronyism has been ubiquitous in recent years and has led to a series of corruption scandals.

The decision to dollarize in 2000 averted hyperinflation and stabilized the economy, bringing modest economic growth to the country. Private consumption returned to normal after a sharp drop, helped by the unfreezing of bank deposits. Remittances from abroad also rose, funding investment in construction and durable goods. Construction of a new heavy crude oil pipeline also provided a boost to investment, allowing the economy to grow in 2002. Still, much remains to be done before stability and prosperity help define the country's political and economic settings. GDP growth estimates have been scaled down for 2003 from 3% to 2.2%, based on a second quarter contraction of 0.8%. Unemployment rates will increase to almost 10% by the end of 2003. Furthermore, the World Bank listed Ecuador as having one of the region's highest infant mortality rates: 28 per 1,000 live births in the year 2000. The country ranked 93rd out of 173 in the 2002 edition of the United Nations Development Program's Human Development Index, over 20 places below Colombia and 11 places behind Peru.

Ecuador is one of the world's richest centers of biodiversity. With a total area roughly the size of Colorado, it holds about 10% of the world's plant species and 18% of bird species. However, the destruction of natural flora and fauna is threatening the country's rich biological diversity. The deforestation rate is the second highest in South America. The government designated 26 ecological protected areas, but the technical capacity necessary to manage these areas is, for the most part, lacking. The government remains in urgent need of international assistance to preserve Ecuador's biodiversity, especially the Galapagos Islands and the marine reserve.

Until 1998, when a peace treaty was signed, Peru was Ecuador's only significant external threat. Today the treaty is still respected and the conflict seems to have come to a permanent resolution. Nevertheless, a lack of funds in both sides of the southern border impedes full implementation of infrastructure and social services. This in turn, has had a detrimental effect in the social and economic conditions of communities along the border.

Since the end of the Peru-Ecuador dispute, the main concern has been with the northern border area. Criminal activity has intensified in the past years: farmers have reported being forced off their land by gunmen and oil companies have been victims of extortion and kidnapping. Criminal activity in the area has increased with such intensity that it is quickly becoming the most serious security issue now facing Ecuador. Colombia's increased efforts to eradicate illegal drug crops has increased pressure on the

rebels and has created a serious spillover effect into Ecuador. In fact, many Ecuadorians worry that the country is being pulled into the conflict itself or that corruption among the country's political class and armed forces could be exacerbated by the drug economy.

U.S. Interests and Goals: A democratic and prosperous Ecuador can advance Andean stability. The United States and Ecuador have maintained close ties based on mutual interests in maintaining democratic institutions; combating narcotrafficking; combating terrorism; cooperating in fostering Ecuador's economic development; building trade, investment, and financial ties; combating poverty; and participating in inter-American organizations. USAID's strategic objectives clearly support these interests. USAID is addressing democracy by strengthening transparency and accountability in democratic institutions, encouraging greater participation of traditionally excluded groups in democratic processes, and working to achieve greater consensus among regionally divided groups in the development of public policies. USAID is helping to prevent the drug economy to spillover into Ecuador by improving the living standards of communities in the northern border provinces. Activities are designed to strengthen grassroots organizations and also generate a higher community satisfaction with local governments through the improvement of social and productive infrastructure and services. USAID is contributing to the conservation of globally biological important areas in Ecuador, including indigenous territories in northern Ecuador that are vulnerable to the growing spillover effect of drug related violence in Colombia, and illicit crops; the Galapagos Marine Reserve and the Condor BioReserve that includes the watersheds that provide 70% of Quito's water. USAID is participating in Ecuador's economic development through a two-prong approach. One component concentrates on macroeconomic reforms through the improvement of fiscal policy, strengthening of investments, promotion of competitiveness, and the development of a strong and transparent financial sector. The other component focuses on strengthening urban and rural micro-enterprises and facilitates access of these micro-enterprises to financial and non-financial services.

Donor Relations: USAID/Ecuador has been a leader and catalyst in donor coordination across the board, being particularly effective regarding macroeconomic reforms with the large and influential programs of the multilaterals (International Monetary Fund (IMF), World Bank, Inter-American Development Bank (IDB), and the Andean Development Corporation (CAF)). USAID/Ecuador continues actively participating in regular donor coordination meetings of the Ministry of Foreign Affairs, facilitating the coordination efforts across all sectors related to the Mission's program, thus assuring more effective international assistance. Under the Northern Border Program, activities are coordinated with the IDB, Food and Agriculture Organization, American Red Cross, United Nations High Commissioner for Refugees (UNHCR) and the United Nations Development Program (UNDP). The Southern Border Program is coordinated with development agencies from Switzerland, Spain, and Japan. A governability roundtable has proven to be an effective coordination mechanism between the Democracy Program and the World Bank, IDB, the German Technical Cooperation, and the Swiss Development Agency. Environment activities are coordinated with bilateral donors (Germany, Switzerland, Spain and Netherlands) and with the World Bank, IDB and European Union.

Challenges: Ecuador continues to face great challenges, both in the political and economic arenas. In August 2003, the Pachakutik Movement, a mostly indigenous party, decided to abandon the alliance it had forged with the ruling party. Since then, the Gutierrez administration has had to rely on the traditional parties in Ecuador's Congress in order to pass legislation. As these parties are indebted to sectional interests, the government will need to make concessions to secure their support; this could ultimately damage the reform program. Moreover, there seems to be a growing perception that Gutierrez may not be able to finish his term owing to obstructionism from the opposition and external interest groups. And indigenous leaders have recently called for mobilizations scheduled for January 2004, asking for the resignation of Gutierrez. As a result, social conflict could potentially increase in the coming months. The economic policy agenda is defined principally by the stand-by agreement reached with the IMF. With much still to be done under this arrangement, the GOE will likely encounter greater difficulties, given its weak position within Congress and stiff opposition from the indigenous movement. Ecuador will likely fall short of the budget surplus of 6.4% of GDP predicted by the IMF for 2004, as delays in the tax reform and lower than expected growth prospects slow revenue growth. Falling oil production at ageing state-run installations paired with the possibility that oil prices will fall due to oversupply, will further limit Ecuador's economic growth in 2004. Finally, there is an increasing concern about the spillover effects of the

Government of Colombia's fight against drugs and guerilla movements and increased violence and criminal activity along the northern border. To make matters worse, there is speculation that Ecuador's armed forces may have participated in illegal arms sales to Colombian combatants.

Key Achievements: Despite the many challenges that Ecuador continues to face, FY 2003 has been a year of great progress for the USAID program. The Mission has built upon lessons learned through implementation and has become more actively engaged in the issues that shape Ecuador's development. Ecuador's key economic and financial institutions have improved their administrative and technical capabilities and new sources of credit and credit monitoring are now available. Essential reforms have also been implemented to make local and national democratic institutions more effective, participatory, transparent and less corrupt. Important strides have also been made to better protect Ecuador's fragile biodiversity, and to provide services, employment and sustainable resources to vulnerable populations along its northern and southern borders. The challenge of the future will be to sustain and expand upon these successes in a climate of continued political and economic uncertainty.

1. **Biodiversity Conservation:** Through this SO, USAID seeks to strengthen Ecuador's capacity to protect its biodiversity by providing indigenous populations with technical assistance in natural resources management, territorial consolidation, conflict management and income generation. The program also promotes development of ecotourism in the Galapagos Islands as an alternative income source, public participation in conservation efforts, and supports the Galapagos National Park Service in its efforts to patrol and protect its Marine Reserve from illegal fishing and drug trafficking. In addition, USAID works closely with Ecuador's Ministry of Environment and non-governmental organizations to implement effective policies and laws that prevent the loss of grasslands and forests within Ecuador's Condor BioReserve, which provides 70% of the capital's water supply. In recent years, USAID programs have contributed to the management and conservation of 2.2 million hectares of land, the strengthening of local NGOs active in conservation and the passage of key laws such as the Special Law for the Galapagos. From 1990-2001, the rate of deforestation within Ecuador's protected reserves fell to less than 1/10 of the national average. USAID's new strategy beginning in FY 2004 hopes to build upon these past accomplishments through increased focus on protected areas and indigenous territories, institutional stability and building local capacity for improved natural resource management. In addition, a new Global Development Alliance (GDA) activity will test innovations in wood processing and marketing, thereby reversing the loss of forests by providing sustainable, alternative, high-value wood products.

2. **Southern Border:** In the wake of the peace agreement entered between Peru and Ecuador in 1998, USAID's Southern Border Program promotes border integration by improving the social and economic conditions of inhabitants in Ecuador's southern provinces. These improvements include increased access to social services (health, water and sanitation), technical assistance to local communities in land titling and natural resource management, and local government capacity building in service delivery, administrative management, and strategic planning. In FY 2003, 20 potable water systems were installed or upgraded and legal titles were established for over 38,000 hectares of land. In FY 2004, new social service projects will be extended to an additional 50,000 people, and six new local governments and six municipalities will receive technical assistance.

3. **Democracy:** Public confidence in, and support of the new administration are alarmingly low. To redress this situation, bolster regional stability, and prevent a return to non-democratic governments, USAID's Democracy Program seeks to strengthen support for democratic institutions through cultivating increased citizen participation, transparency and accountability. USAID focuses its efforts in four areas: justice reform, democratic local governance, anti-corruption, and elections support. In the justice sector, a major revision of the code of criminal procedure, increased independence and representation of women in the judiciary were among key initiatives. Further, some 15 municipal governments received technical assistance in support of public works (solid waste management, potable water, irrigation) and other infrastructure projects selected by local citizens. USAID NGO partners contributed to the issuance of a presidential decree in April 2003, that requires greater transparency in government contracting, improved public sector ethics, and the creation of an anti-corruption monitoring and evaluation system. Electoral activities include support for increased civic participation, campaign finance limitations and monitoring of national and sub-national elections. In FY 2004, support for these efforts will continue with emphasis on

anticorruption and local governance.

4. Northern Border: USAID's Northern Border Program seeks to contain the spillover of a coca/cocaine economy into Ecuador and to improve the quality of life for people living in the six provinces along Ecuador's northern border with Colombia. This multi-faceted program includes support for road construction and sustainable social infrastructure projects, assistance to local and municipal governments in land titling, strategic planning and financial management, and creation of job opportunities and licit income. In FY 2003, USAID-funded activities provided potable water, irrigation, roads and other critical infrastructure projects for over 110,000 poor residents of Ecuador's northern border, and five municipal governments received management training and other technical assistance. In FY 2004, these efforts will continue, with increased emphasis on job creation and public awareness of the dangers of illegal coca cultivation and cocaine use. For example, a new GDA activity involving the production of high-quality cacao for export will provide sustainable licit employment opportunities for northern border farmers.

5. Economic Opportunities: Over 60 percent of Ecuador's people live in poverty. USAID's approach to this problem is two-pronged: first, through macroeconomic reforms intended to stimulate growth, develop strong, transparent financial institutions and encourage trade and foreign investment. The second involves increasing rural and urban microentrepreneurs' access to capital and financial services. Although future macroeconomic advances will depend largely upon the government's continued willingness to change, in 2003, USAID secured endorsements from the Gutierrez Administration and signed important collaborative agreements with the Ministry of Finance and the Superintendence of Banks. USAID-funded technical assistance to Ecuador's Internal Revenue Service (SRI) led to marked improvement in its tax collection and administrative capacities. USAID also funded vital support to develop a set of supervisory manuals for the microfinance sector, organize and strengthen credit unions, and secure authorizations for the first private credit bureaus in Ecuador's history. In FY 2003, an additional 37,150 customers received credit assistance. In FY 2004, USAID will expand upon these activities by funding continued technical assistance to the microfinance sector, commissioning an assessment of Ecuador's trade deficiencies, and necessary structural reforms, and implementing a trade-capacity building program to complement an existing Inter-American Development Bank (IDB) effort.

Country Close and Graduation:

Results Framework

518-001 Biodiversity Conserved in Selected Protected Areas , Their Buffer Zones and Indigenous Territories

IR1.1 Governmental and non-governmental institutions developed adequate capacity to govern natural resources management, demonstrating transparent, accountable governance

IR1.2 Sustainable natural resources management practices adopted

IR1.3 Sustainable financing mechanisms contribute to conservation efforts

518-002 Increased Use of Sustainable Family Planning/Maternal Child Health Services

518-011 Improved Social and Economic Conditions of Inhabitants along the Peru-Ecuador Border, Thereby Promoting Border Integration

SO Level Indicator(s):

Number of beneficiaries in the target region whose lives are improved by access to social services, improved natural resources management practices and/or effective local governments.

IR11.1 Increased access to major infrastructure.

IR11.2 Expanded income-generating opportunities for small and micro entrepreneurs.

IR11.3 Increased availability and access to social services, with emphasis on health, water, and sanitation.

IR11.4 Improved natural resource management in selected areas along the border.

IR11.5 Increased private investment in the border area.

IR11.6 Improved capacity of local governments to plan projects and implement services.

518-012 Increased Support for the Democratic System

SO Level Indicator(s):

Decreased perception of corruption.

Increased legitimacy of justice system.

Increased legitimacy of local governments.

IR12.1 Improved transparency and accountability of key democratic institutions.

IR12.2 Greater inclusiveness of democratic processes.

IR12.3 Increased policy consensus in key democratic areas.

518-013 Spread of the Andean Regional Coca/Cocaine Economy into Ecuador Contained

IR13.1 Citizen satisfaction with performance of local democratic institutions increased.

IR13.2 Licit income and employment opportunities increased.

IR13.3 More effective enforcement of laws related to counter narcotics and violent crimes.

IR13.4 Government of Ecuador public forces more effectively defend security in northern border area.

IR13.5 Ecuadorian public recognizes that coca/cocaine economy is a national problem.

518-014 Increased Economic Opportunities for the Poor

SO Level Indicator(s):

Key governmental institutions strengthened for an improved macroeconomic environment.

Number of microfinance credit clients increased by approximately 350%

IR14.1 Increased access to microfinance services.

IR14.2 Macroeconomic policies/environment for more equitable growth improved.

518-XXX Economic Growth

518-YYY Health Initiatives