

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

ECUADOR

COMPETITIVENESS ENHANCEMENT PROGRAM

(EC-L1004)

LOAN PROPOSAL

This document was prepared by the project team consisting of: Luis Giorgio (RE3/FI3), Project Team Leader; Francesca Castellani (RE3/RE3); Rosa Matilde Guerrero (COF/CEC); Mario Sánchez (RE3/SO3); Frank Nieder (RE3/FI3); Guillermo Arrivillaga (COF/CEC); Claudia Stevenson (RE3/FI3); Bernadete Buchsbaum (LEG/OPR); Maria Carina Ugarte (RE3/FI3), and Nathalie Cely (consultant).

CONTENTS

PROJECT SUMMARY

I.	FRAME OF REFERENCE	1
A.	Introduction	1
B.	Macroeconomic environment.....	1
C.	The need to enhance competitiveness in Ecuador	3
D.	Initiatives undertaken to enhance Ecuador's competitiveness	4
E.	The Bank's sector strategy	5
F.	The Bank's strategy with the country	6
G.	The Bank's support for sector reforms and lessons learned	6
H.	Strategic rationale for the program.....	7
I.	Complementary programs of the Bank and other international agencies	7
II.	THE PROGRAMMATIC OPERATION	9
A.	Objectives	9
B.	Core elements of the programmatic operation.....	9
III.	FIRST PROGRAMMATIC LOAN AND TRIGGER MECHANISMS	16
A.	Competitiveness of the real sector.....	16
B.	Competitiveness of the financial sector	18
IV.	EXECUTION OF THE PROGRAMMATIC OPERATION.....	21
A.	Execution	21
B.	Related technical support.....	22
C.	Monitoring and evaluation.....	23
D.	Other features of execution.....	24
V.	FEASIBILITY AND RISKS OF THE PROGRAMMATIC OPERATION	25
A.	Beneficiaries	25
B.	Effects and benefits of the programmatic operation.....	25
C.	Environmental and social considerations.....	26
D.	Risks	26

ANNEXES

Annex I	Policy Matrix
Annex II	Means of Verification Matrix
Annex III	Results Matrix

Proposed resolution

Electronic Links and References	
Basic socioeconomic data	http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata
Tentative lending program	http://portal.iadb.org/opsfilters/xmlToHtml.aspx?Output=HTML&AppName=PIPELINELOANS&Language=EN&Sort=&Link=Filter&Region=&Country=EC&Division=&PipCat=&OperType=LON
Private sector portfolio	http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=808546
Anex IV Policy Letter	http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=810582
Anex V Macroeconomic Assessment of the Country	http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=809715

ABBREVIATIONS

AEC	Agenda Ecuador Compite [National Competitiveness Agenda]
BCE	Banco Central del Ecuador [Central Bank of Ecuador]
BCI	Business Climate Initiative
BLR	benchmark lending rate
CAE	Corporación Aduanera Ecuatoriana [Ecuadorian Customs Corporation]
CAF	Andean Development Corporation
CEREPS	Cuenta Especial de Reactivación Productiva y Social y la Ejecución de Proyectos de Infraestructura, del Desarrollo Científico-Tecnológico y de la Estabilización Fiscal [Account for the Revitalization of Productive and Social Sectors, Infrastructure Projects, Scientific and Technological Development, and Fiscal Stability]
CESI	Committee on Environment and Social Impact
CNC	Consejo Nacional de Competitividad [National Competitiveness Council]
CNCF	Consejo Nacional de Capacitación y Formación Profesional [National Council on Vocational Training and Education]
CNPC	Consejo Nacional para la Reactivación Productiva y la Competitividad [National Council on Production Revitalization and Competitiveness]
CODEPYMES	Consejo Interinstitucional Público-Privado [Public-Private Interagency Council]
CORPEI	Corporación de Promoción de Exportaciones e Inversiones [Corporation for Export and Investment Promotion]
EMBI+	Emerging Markets Bond Index Plus
FEIREP	Fondo de Estabilización, Inversión Social y Productiva y Reducción del Endeudamiento Público [Stabilization, Social and Productive Investment, and Public Debt Reduction Fund]
FONDEPYMES	Competitive fund promoting initiatives to improve market access for SMEs
GDP	gross domestic product
IESS	Instituto Ecuatoriano de Seguridad Social [Ecuadorian Social Security Institute]
IFF	Intermediate Financing Facility
IMF	International Monetary Fund
ITC	Interagency Technical Committee
MEF	Ministry of Economy and Finance
MICIP	Ministry of Foreign Trade, Industrialization, Fisheries, and Competitiveness
NFPS	nonfinancial public sector
SBS	Superintendencia de Bancos y Seguros [Superintendent of Banks and Insurance]
SC	Superintendencia de Compañías [Superintendent of Companies]

SICE	Sistema Interactivo del Comercio Exterior [Interactive Foreign Trade System]
SMEs	small and medium-sized enterprises
WEF	World Economic Forum

PROJECT SUMMARY

ECUADOR COMPETITIVENESS ENHANCEMENT PROGRAM (EC-L1004)

Financial Terms and Conditions ¹				
Borrower: Republic of Ecuador Executing agency: Ministry of Economy and Finance			Amortization period:	20 years
			Grace period:	5 years
			Interest rate:	LIBOR
Source	Amount	%	Inspection and supervision fee:	0%
IDB (Ordinary Capital)	50 million	100	Credit fee:	0.25%
Local	0	0	Currency:	United States dollars from the Single Currency Facility
Total	50 million	100		
Project at a glance				
Project objective: Enhancement of Ecuador's competitive position through the increased productivity and efficiency of the real and financial sectors within a context of sustainable macroeconomic stability.				
Special contractual conditions: The borrower will have complied with the conditions set out in the policy matrix (Annex I) and, through the executing agency, will have submitted evidence detailed in Annex II on the conditions precedent to disbursement, including: (i) strengthening the institutional framework for competitiveness; (ii) improving customs procedures; (iii) simplifying business startup procedures; (iv) improving vocational-training services; (v) introducing a policy and mechanisms to encourage the competitive development of small and medium-sized enterprises (SMEs); (vi) promoting public-private business cooperation at the subnational level; (vii) introducing a new method for calculating the benchmark lending rate; (viii) promoting transparency in financing costs; (ix) enacting a Credit Bureau Law; and (x) promoting draft secured transactions and bankruptcy laws.				
Exceptions to Bank policies: None.				
Project consistent with country strategy: Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>				
Project qualifies as: SEQ <input type="checkbox"/> PTI <input type="checkbox"/> Sector <input type="checkbox"/> Geographic <input type="checkbox"/> Headcount <input type="checkbox"/>				
Verified by CESI on: 27 August 2004				

¹ The interest rate, credit fee, and inspection and supervision fee mentioned in this document are established pursuant to document FN-568-3 Rev. and may be changed by the Board of Executive Directors, taking into account the available background information, as well as the respective Finance Department recommendations. In no case will the credit fee exceed 0.75%, or the inspection and supervision fee exceed 1% of the loan amount.*

* With regard to the inspection and supervision fee, in no case will the charge exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

I. FRAME OF REFERENCE

A. Introduction

- 1.1 In the last few years, Ecuador's institutional situation has been highly volatile; since the initiation of conversations with the country, one presidential term ended ahead of time and there has been a high turnover of ministers and secretaries of State, including five different Ministers of Economy and Finance (MEF). Despite this fluid institutional environment, the government's technical teams have continued to prioritize activities to enhance competitiveness, thus contributing to keeping alive the public debate on the need to move forward with structural reforms.
- 1.2 The meeting of the Board of Governors of the Bank in Okinawa in April 2005 approved the New Lending Framework, allowing for the implementation of programmatic operations. The programmatic approach is particularly useful for supporting complex reforms, implemented in successive steps and requiring an ongoing active and systematic country dialogue. Moreover, the programmatic approach promotes the sustainability of State policies in changing political environments.
- 1.3 Because of the country's favorable short-term fiscal situation, associated with high oil prices and the windfall earnings stemming from the termination of the Occidental Petroleum Company's contract, in 2006 Ecuador's fiscal financing requirements dropped significantly. In this context, Bank support serves as a strategic instrument to consolidate State policies on competitiveness. Moreover, in a situation of institutional volatility like the one that has characterized Ecuador for a number of years, and in view of the presidential elections in October, the Bank's presence through a programmatic operation will make it possible to continue and deepen the dialogue with the country's current and future administrations.
- 1.4 This document submits for approval the Project Report of a programmatic operation with three one-tranche programmatic loans. The program is accompanied by a nonreimbursable technical-cooperation operation (EC-T1032), approved on 21 December 2005, to support the actions that must be implemented for the subsequent programmatic loans to be activated.

B. Macroeconomic environment

- 1.5 At the end of the 1990s, pressure to increase fiscal spending, low oil prices, and natural disasters, combined with a reduced influx of external financing after the Russian crisis of 1998, negatively affected the Ecuadorian economy. In 1999, the sucre was devalued by 171%; 20 banks, accounting for more than 50% of bank deposits, failed; and the government declared a moratorium on public-debt payments. As a result, gross domestic product (GDP) declined by 6%, in real terms, and inflation rate rose to 103%. In this economic climate, on 9 January 2000

Ecuadorian authorities adopted the United States dollar as the country's legal tender.

- 1.6 Since dollarization took effect, the Ecuadorian economy has stabilized and recovered to a significant degree. Between 2003 and 2005, in a context of fiscal consolidation, strengthening of the financial and external sectors, and lower public borrowing, GDP grew at more than 5.4% per annum, on average. In addition, inflation dropped to 3.1% in 2005.
- 1.7 The high price of oil has played a pivotal role in the economic performance seen in the last three years. It is estimated that in 2006 the country will grow by 4.4%, inflation will remain at 3%, and the current account of the balance of payments will record a surplus equivalent to 4.4% of GDP. In fiscal matters, according to the government's program, the overall nonfinancial public sector surplus is expected to reach 4.6% of GDP. Public borrowing is expected to represent 34% of GDP, down from 87% in 2000. In early September 2006, the Emerging Markets Bond Index Plus (EMBI+) stood at 532 basis points above United States Treasury bonds. In 2005, Ecuador returned to international markets when it issued 10-year bonds with a 10.75% yield, and in March 2006 it retired US\$740 million of the US\$1.25 billion in 12-year global bonds.
- 1.8 The current situation is significantly different as a result of the amendment to the Hydrocarbons Law and the termination of the contract with Occidental Petroleum. The government estimates windfall earnings of about US\$951 million for 2006 and US\$1.2 billion in 2007. These resources should help improve fiscal performance and public debt management and would be used, in part, to invest in energy sector infrastructure. Nonetheless, managing these surpluses poses the challenge of maintaining fiscal discipline and avoiding an unsustainable upsurge in domestic demand.
- 1.9 The Ecuadorian government has expressed its commitment to maintain macroeconomic stability; in particular, it expects to continue with the strategy of buying back and changing the structure of public debt. In addition, the country maintains an agreement with the International Monetary Fund (IMF) under which progress with implementation of the economic program is reviewed quarterly.
- 1.10 Despite the favorable climate, the risks for economic performance and sustainability remain. In addition to the need to maintain fiscal discipline, there are risks fundamentally associated with the competitiveness of the productive sector and external and financial vulnerability.
- 1.11 Regarding the competitiveness of the productive sector, difficulties in trade negotiations and the possible expiration of the Andean Trade Promotion and Drug Eradication Act could have negative consequences for exports. Moreover, the abundance of oil resources may cause a sharp increase in demand, spurring the

nontradable sector of the economy and displacing or harming the tradable sector (Dutch disease).

- 1.12 Regarding capital flows, Ecuador continues to face obstacles to accessing international markets. Despite recent improvements, the country's risk rating, CCC+, is the lowest among Latin America issuers, and the country risk, as measured by the EMBI, is the highest in the region. Given this vulnerability, a possible deterioration in international markets could have a magnified impact on Ecuador's financial stability. Moreover, in the short term, the proposals to modify the legal framework governing the financial sector could introduce controls on interest rates and on the allocation of credit to the private banking system. This would be detrimental to the health and efficiency of the financial system. These factors exist in a changing political context, with presidential elections scheduled for October 2006.

C. The need to enhance competitiveness in Ecuador

- 1.13 The Growth Competitiveness Index of the World Economic Forum (WEF) indicates that in 2005 Ecuador's overall competitiveness did not improve, remaining in the fifth quintile of the sampling (103rd out of 117 countries).¹ When the figures are broken down, the indicator that has declined the most is that of quality of institutions, which fell from the 87th percentile in 2004 to the 97th in 2005. The Macroeconomic Environment Index improved compared with 2004, with Ecuador rising from the 86th to the 68th percentile, and in the Current Competitiveness Index the country remained in the 92nd percentile² (107th out of 117). Other WEF indicators, such as the Index of Ease of Access to Loans (83rd out of 117), also underscore the need for Ecuador to enhance its competitiveness.
- 1.14 Ecuador must respond to the demands of an economy characterized by high volatility and the absence of a monetary policy to act as an instrument of short-term macroeconomic stabilization. It must also meet the need for a flexible fiscal policy with instruments designed to minimize the fluctuations of the economic cycle. Given that the importance of the countercyclical nature of fiscal policy is proportional to the degree of vulnerability to external shocks (variation in the terms of trade, declining capital flows, natural disasters, etc.), the country needs a highly competitive private sector.
- 1.15 Moreover, the challenge of competitiveness is now heightened by the presence of trading partners relatively better positioned in competitiveness. This is the case of Colombia and Peru, which scored 57th and 68th in the sampling of 117 countries examined in the WEF's Growth Competitiveness Index.

¹ The Growth Competitiveness Index is a composite of the Macroeconomic Environment Quality Index, the Public Institutions Quality Index, and the Technology Index.

² The Current Competitiveness Index is a composite of the Strategy Index and the Business Quality Index.

- 1.16 Ecuador's economic infrastructure is a determining factor of competitiveness. Although in kilometers of paved roads, traffic density on the national highway network, and number of ports and airports, Ecuador is close to or exceeds the average for the countries of the region, in infrastructure management it has serious deficiencies. Furthermore, the condition of the infrastructure and the operation maintenance programs need to be reviewed to ensure greater efficiency. Likewise, the budget resources allocated to the sector are insufficient and the user-fee policy does not allow for adequate cost recovery. One of the main problems preventing efficient management of scarce resources is the proliferation of institutions with varying hierarchies and levels and with contradictory responsibilities and objectives. This impedes the implementation of a coordinated and effective policy.
- 1.17 In the energy sector, weaknesses in the regulatory framework distort price signals, limiting private-sector participation and the formulation of an optimal energy matrix. Lastly, fixed-line telephony coverage in Ecuador is below average for Latin America, as are cellular-telephone penetration and the number of Internet users.
- 1.18 In the science and technology sectors, including the potential for technological innovation by businesses, various indicators (including the State budget for science and technology and the number of researchers and scientists) point to Ecuador's need to place greater emphasis on and make a priority of development in this area to enhance competitiveness. The relatively low development of science and technology in Ecuador is largely explained by the low priority that the State has attached to investing in and carrying out projects, as well as political instability, the lack of incentives for private-sector investments, and the meager capacity to retain skilled personnel.
- 1.19 The costs in economic performance resulting from the sectoral weaknesses described above are aggravated by companies' limited access to lending, in particular in the case of micro, small, and medium-sized enterprises; the extensive red tape in customs procedures; and a model of technical and vocational-training services not directly geared to meeting firms' needs.

D. Initiatives undertaken to enhance Ecuador's competitiveness

- 1.20 The Consejo Nacional de Competitividad [National Competitiveness Council] (CNC), which was created in 2001 as a forum for effective cooperation and dialogue between the public and private sectors, seeks to design a national competitiveness strategy and identify the policies needed for its implementation. In March 2003, Executive Decree 1666 made the CNC part of the Executive Branch, although it is independently administrated and funded. It is headed by the President of the Republic or the person appointed by the President, and also includes eight ministers of State, the President of the Corporación de Promoción de Exportaciones e Inversiones [Corporation for Export and Investment Promotion] (CORPEI), seven representatives of the Private Advisory Council, and a labor representative.

- 1.21 The decree also charged the CNC with advising the President of the Republic on matters related to competitiveness enhancement and the leadership of the agencies involved as well as with developing the strategy and implementing the actions needed to reduce companies' transaction costs. In fulfillment of this responsibility, in October 2003, the CNC, following a public-private consultation process, presented Agenda Ecuador Compite [National Competitiveness Agenda] (AEC) 2003-2007.
- 1.22 The AEC has set two objectives: (i) raising economic productivity by bringing down costs, encouraging a more efficient use of the factors of production, and reducing risks and transaction costs; and (ii) promoting economic diversification to reduce dependence on primary products by encouraging the production of higher-value-added goods and services. In line with these objectives, the AEC is promoting improvements and reforms by prioritizing actions in eight competitiveness factors: (a) accumulation of human capital; (b) efficiency in public administration; (c) infrastructure; (d) commercial integration; (e) access to financing; (f) innovation and technology strategy; (g) appropriate institutional framework; and (h) proper natural-resource management. The CNC was charged with executing and monitoring the AEC by acting as a facilitator of dialogue between the public and private sectors and identifying and promoting the steps needed to enhance competitiveness.
- 1.23 In addition, the CNC was made responsible for spearheading and monitoring the implementation of the Agenda for Productive Development, which includes the commitments and agreements undertaken through free trade agreements. Hence, on 13 September 2005, the President of the Republic, through Decree 505, created the Consejo Nacional para la Reactivación Productiva y la Competitividad [National Council on Production Revitalization and Competitiveness] (CNPC). The President put the CNC in charge of fulfilling the CNPC's responsibilities as well as specific responsibilities related to the Agenda for Productive Development.

E. The Bank's sector strategy

- 1.24 The Bank's competitiveness strategy promotes actions in six priority areas: (i) the efficient mobilization of financial resources and capital; (ii) improved human resources and higher productivity; (iii) efficient provision of infrastructure services; (iv) development and assimilation of knowledge and technologies; (v) more effective support institutions for private productive activities; and (vi) competitiveness and the productive and sustainable management of natural capital. Similarly, the strategy makes clear that a prerequisite for these actions to be effective is a macroeconomic environment characterized by fiscal, financial, and external sustainability as well as economic stability. This programmatic loan envisages a set of actions consistent with the Bank's sector strategy.

F. The Bank's strategy with the country

- 1.25 The Bank's strategy with the country for the 2004-2006 period focuses on two priority areas: (i) helping lay the foundations to energize the productive structure (structural dimension); and (ii) promoting the protection of the most vulnerable groups and social development (social dimension). These two priority areas are supported by a crosscutting element: improving the effectiveness of public administration (institutional dimension). This program dovetails with the first of the priority areas described above.
- 1.26 With the public-private relationship as the linchpin, the Bank's strategy with the country calls for the Bank's action in favor of competitiveness to support institution-strengthening actions and changes in regulations on the execution of the AEC. The Bank will support the country in (i) changes in the institutional framework that will make it possible to implement the AEC; (ii) changes in the institutional framework to enhance legal certainty; and (iii) changes to regulations, reducing the risks of financial intermediation and the time needed to complete formalities and procedures.

G. The Bank's support for sector reforms and lessons learned

- 1.27 Competitiveness enhancement is a strategic area of the Bank's work with the countries, which in the past has primarily been implemented in the form of technical-cooperation operations. The Bank's experience with competitiveness-reform programs is recent. In 2003, two sector competitiveness programs were approved, in Peru (1503/OC-PE) and in El Salvador (1492/OC-ES); although these operations are relatively new, lessons can be learned from them on (i) the importance of the process of consensus building and consultation with the private sector in designing the planned actions; and (ii) the need to have a suitable institutional framework for competitiveness.
- 1.28 Six policy-based loans have been approved and executed in Ecuador, totaling US\$715 million, four of which were approved in 1994: the financial sector program (833/OC-EC) for US\$110 million; the agriculture sector program (831/OC-EC) for US\$92.5 million; the transportation services restructuring program (842/OC-EC) for US\$82.4 million; and the debt and debt-service reduction program (850/OC-EC) for US\$80 million. In 2000, the investment sector program (1259/OC-EC) was approved for US\$150 million and in 2003, the social sector program (1466/OC-EC) was approved for US\$200 million.
- 1.29 There were cancellations in the amount of resources approved for all six operations. In two cases, the cancellations were significant: the transportation services restructuring program canceled 66% of its resources and the investment sector program canceled resources equivalent to 19% of the amount originally approved. In both operations, some of the proposed objectives were not met because of lack of

continuity in the political commitment to implement the structural reforms. In addition, it should be noted that two operations were executed in the context of financial crises and political instability: the financial sector program and the social sector program. In the latter case, the second disbursement was approved with a number of conditions that were not fulfilled and others only partially fulfilled.

- 1.30 The lessons learned from implementing sector programs in Ecuador underline the need to maintain an ongoing dialogue with the country that promotes technical and political consensuses, which is why the programmatic approach is deemed suitable and effective. In addition, it is important to emphasize that technical-cooperation operations need to be developed that will support execution of the planned activities and at the same time strengthen the acting executing units if necessary.

H. Strategic rationale for the program

- 1.31 Enhancing economic competitiveness is a priority for a dollarized country. In addition, Ecuador faces disadvantages with respect to its competitors in export markets, meaning not only the Asian economies but also its subregional trading partners (Peru and Colombia).
- 1.32 The formulation and implementation of a National Competitiveness Strategy are the result of a dynamic process whose objective is a shared public-private vision of the country's challenges in this area. A programmatic operation favors an ongoing policy dialogue and makes it possible to support the country's efforts in designing and implementing a medium-term reform program; hence, it is an ideal instrument to strengthen the institutional framework, allow an ongoing debate, and reach a consensus on the actions required to enhance economic competitiveness.
- 1.33 The process of preparing the operation allowed the Bank to be part of the policy dialogue, particularly since mid-2005. During this period, instruments were identified that were considered important to the institutional framework for enhancing competitiveness, such as the establishment of the CNPC, and to the improved transparency of financial intermediation, such as the approval of the Credit Bureau Act by Congress.

I. Complementary programs of the Bank and other international agencies

- 1.34 The Bank is currently preparing or executing several operations that complement this project. The most important of these include: (i) the foreign trade management support program (1524/OC-EC), whose fundamental aim is to help improve public management of foreign trade by strengthening the capacity to formulate, negotiate, and apply a comprehensive and consistent trade policy; and (ii) operation ATN/ME-8530-EC, mitigation of market-access barriers, whose basic aim is to help achieve compliance with nontariff regulations to improve the access of Ecuadorian companies to the United States market, through a systematic approach

for dealing with technical barriers to that market before and after the Andean Trade Preference Act expires.

- 1.35 The MIF projects whose characteristics mean that they complement this operation are: (i) cooperative SME operations in the floriculture value chain (EC-M1013). The purpose of the program is to develop, facilitate, and strengthen partnerships and cooperation between horizontally linked firms and enterprises in related fields in order to heighten the value chain's efficiency and effectiveness; (ii) the program for establishing a competitiveness strategy for Ecuador's fine aroma cocoa chain (EC-M1011), whose core objective is to increase the presence of fine aroma cocoa from Ecuador in conventional and specialty markets; and (iii) four small MIF operations related to the program to delegate authority to the Country Office, whose aim is to improve the marketing networks, competitiveness levels, and cooperative partnering of small and medium-sized enterprises (SMEs) in several sectors.
- 1.36 The Bank has been working actively with the government on the Business Climate Initiative (BCI) since February 2004. The analytical work conducted in this context was also taken into account to design this program. The program's policy matrix includes a series of components (i.e., a component on transaction costs for firms, access to financing) proposed in the BCI's action plan prepared in early 2005.
- 1.37 In May 2003, the World Bank approved the first phase of a fiscal and growth competitiveness programmatic loan for US\$50 million. In 2004, the CAF approved a hybrid operation to be funded with a US\$120 million loan for infrastructure initiatives that has a US\$1.8 million component to support competitiveness in the country. These funds would be used in ad hoc initiatives to (i) support production-integration initiatives with an export potential; (ii) disseminate and promote the competition law; (iii) strengthen the Ecuadorian Quality System to support the productive sector; and (iv) strengthen the in-bond assembly sector and implement initiatives to improve access to and the application of technology and connectivity. In addition, the CAF is supporting the country with a loan to achieve regulatory reform and encourage investment in the electricity sector.

II. THE PROGRAMMATIC OPERATION

A. Objectives

- 2.1 Competitiveness enhancement requires, inter alia, coordinating the implementation of suitable policies for investment in human and physical capital by advancing reforms in financial markets and establishing a coherent institutional framework. These elements, along with proper public-accounts management, are fundamental for furthering business development and encouraging private-sector investment. Consequently, the overall objective of the programmatic operation is the enhancement of Ecuador's competitive position, through the increased productivity and efficiency of the real and financial sectors, within a context of sustainable macroeconomic stability.
- 2.2 **Macroeconomic sustainability.** The Ecuadorian government's decision to dollarize the economy helped achieve macroeconomic stability, bringing down inflation and interest rates and lowering country risk. At the same time, the new exchange-rate regime has significantly limited the use of traditional monetary and exchange-rate instruments to address temporary imbalances. Consequently, fiscal policy took on greater importance as an instrument of macroeconomic sustainability. It also allowed for a suitable environment to develop structural reforms to energize Ecuador's productive structure and reduce volatility. The programmatic operation requires a stable, sustainable macroeconomic environment conducive to enhancing the country's competitiveness.

B. Core elements of the programmatic operation

1. Competitiveness of the real sector

- 2.3 In this core area of action, the programmatic operation calls for a series of steps backstopped by specific interventions to systemically deal with the causes of the problem. The aim of the actions is to: (i) strengthen the institutional framework for competitiveness; (ii) reduce transaction costs for firms by simplifying foreign-trade formalities and business startup procedures and by providing access to vocational-training services for firms' employees; and (iii) further SME competitiveness by establishing policies that encourage improvements in their business management, give them increased access to technology, and promote public-private cooperation at the subnational level, the natural setting for a large number of SMEs in Ecuador to conduct business.
- 2.4 In science and technology, the Bank will seek to incorporate actions to develop the science and technology system in the medium-term dialogue. Among the aspects to be included in this dialogue are strengthening relevant institutions (research centers, universities, and State entities); improving the overall conditions (educational level,

employee training, protection of property rights, and an enabling environment for private investment); and creating incentives for public and private investment in research and development (subsidies, tax incentives, and encouragement of public-private cooperation).

- 2.5 As part of the program, the medium-term aim of dialogue on infrastructure topics will be to promote (i) support for creating an institutional framework with more clearly defined duties and responsibilities, and (ii) support for sector policy development, improvement of planning processes, and development of user-fee and rate policies that guarantee sustainability and infrastructure expansion for the country to become more competitive.

a. Institutional framework for competitiveness

- 2.6 Although the AEC was designed through a participatory process, its implementation has not led to the expected progress, because the CNC has lacked: (i) clarity on the area of action; (ii) efficient organizational structure for decision-making; and (iii) sufficient private-sector participation and representation on its Board of Directors.
- 2.7 **Objective.** The programmatic operation proposes that the country be supported in strengthening the CNPC's institutional framework so as to coordinate and integrate multisectoral and interagency efforts. Fulfilling this objective requires (i) a precise definition of its authority, in particular, as a facilitator and coordinator of the National Competitiveness Strategy, of its implementation, and of the monitoring and evaluation of its execution; (ii) efficient institutional mechanisms for decision-making; and (iii) private-sector representation on its institutional bodies.

b. Transaction costs for firms

- 2.8 Three key issues requiring prompt attention have been identified: (i) Ecuadorian firms have high transaction costs because of the amount of paperwork required for clearing merchandise through customs; (ii) although the procedures for opening a business can be conducted through one-stop windows and user service centers, the agencies involved do not serve a sufficiently large geographic area, which imposes costs on users wanting their services; and (iii) the extent of employee vocational training in a firm correlates positively with its size, which creates significant competitive disadvantages for small firms.

(i) Improving customs procedures

- 2.9 In Ecuador, clearing goods through customs entails a high transaction cost for firms involved in foreign trade: an average of 17 days, and a maximum of 31 days, is

required to import goods.³ The WEF indicators for 2004 on customs efficiency and its impact on business place Ecuador in position 101 of 104.

- 2.10 **Objective.** Although Ecuadorian Customs has made important progress in collecting fees, its role as a foreign-trade facilitator needs to be enhanced. At present, physical valuation is carried out for clearing more than 70% of goods, and the system lacks an online computer system to streamline procedures. The programmatic operation intends to support the modernization of customs management to ensure that it has the tools with which to expedite procedures.

(ii) Simplification of business startup procedures

- 2.11 Business startup procedures in Ecuador have consistently improved.⁴ The maximum time needed to start a business through the one-stop windows of the Chambers of Commerce in Quito and Guayaquil and through the user service center of the Superintendencia de Compañías [Superintendent of Companies] (SC) is 30 days and the average is 15 days. The one-stop model makes available the provision of services by several public agencies, such as the SC, the Ecuadorian Social Security Institute, and municipios, and by private organizations such as chambers of commerce. The user service centers, which have been established by the SC, have succeeded in expediting services through the use of online information. These pilot cases are concentrated in large cities such as Quito and Guayaquil.
- 2.12 **Objective.** The simplification of business startup procedures would have a broader impact if the coverage of one-stop windows and user service centers were extended to other cities in the country and if the virtual-service model were promoted for cities where the application of the models mentioned above is not justified. The aim of the programmatic operation is to contribute to the expansion of coverage by these services.

(iii) Improving vocational training services

- 2.13 In 2001, the Consejo Nacional de Capacitación y Formación Profesional [National Council on Vocational Training and Education] (CNCF) was created. The CNCF administrates resources generated through a payroll tax and finances exclusively private-sector training activities by nonprofit organizations. Private-sector companies select from among the training proposals offered by CNCF-certified training centers. In 2003, the CNCF used 33% of its allocated budget (US\$4,005,825), approving 8,811 applications and providing training to more than

³ World Bank, Business Climate, Ecuador, 2004, p. 17.

⁴ Instituto de Desarrollo Empresarial [Business Development Institute], Estado de la Tramitología de Constitución de Empresas y de Comercio Exterior [Status of business startup and foreign trade bureaucratic processes], December 2004.

38,000 workers. Efficiency problems have hampered the allocation of resources and led to mismatches between the availability of and demand for training and inadequate quality control of services.

- 2.14 **Objective.** To introduce an effective and competitive mechanism guaranteeing a suitable supply of training for the business sector, the programmatic operation will support the CNCF in developing a system to ensure: (i) fostering competition in the provision of employee-training services; (ii) giving accreditation to companies providing these services in line with required quality standards; (iii) introducing a demand-driven system; and (iv) monitoring and evaluating the activities, outcomes, and impacts of the training programs, with the evaluations having an impact on the operation of the system.

c. Competitive development of SMEs

- 2.15 A review of business development programs implemented in Ecuador and conducted by the Bank⁵ shows that these programs characteristically (i) have multiple executing agencies; (ii) have different operating mechanisms and criteria; and (iii) are ineffective. In turn, although several public-private initiatives are being carried out, there is no formal mechanism to promote competitiveness at the local level.

(i) Policies and mechanisms for the competitive development of SMEs

- 2.16 Ecuadorian SMEs are characterized by (i) little inclination for establishing links; (ii) low propensity to innovate; and (iii) low quality of business management and of the goods and services they provide. Only 23% of firms say they have cooperation arrangements with other firms on production-related issues.⁶ The WEF indicators place Ecuador in position 100 of 117 in capacity to absorb and transfer technology. To become more competitive, Ecuadorian SMEs must strengthen their capacity to form partnerships, innovate, improve their business management, and raise their quality.
- 2.17 **Objective.** The splintered nature of business-development programs and their ineffectiveness point to the need for a comprehensive approach through a policy based on international best practices. The principles guiding the operation of the program stipulate that (i) initiatives to be financed should be demand-driven; (ii) selection criteria should be competitive and transparent; (iii) the beneficiaries should make a cash and in-kind counterpart contribution; and (iv) an independent evaluation and monitoring system should be in place.

⁵ Conducted by Multiplia.

⁶ Instituto de Investigaciones Socioeconómicas y Tecnológicas [Socioeconomic and Technological Research Institute], Diagnóstico de las PYMES [Diagnostic assessment of SMEs], 2002.

(ii) Promotion of public-private business partnerships at the subnational level

- 2.18 International experience (e.g., Colombia and Italy) shows that local efforts to design and implement plans for productivity enhancement and diversification of the local exportable supply through a public-private partnership approach have helped enhance the productivity of enterprises and the business climate in the regions in question.⁷
- 2.19 **Objective.** Implementation of the National Competitiveness Agenda to enhance the country's competitiveness requires a comprehensive approach and the coordination of public-private stakeholders at the local level. The programmatic operation is expected to establish a mechanism to promote local competitiveness so as to coordinate local public-private cooperation efforts and provide for implementing a cofinancing fund to design and implement local production plans.

2. Competitiveness of the financial sector

- 2.20 High credit costs and scarce access to financing can neutralize firms' efforts to enhance production efficiency and lower costs. In Ecuador, the cost of credit is nearly equally divided between the lending interest rate and the costs for administration expenses and fees charged by financial entities. Moreover, credit for the private sector is highly concentrated: 63% of the loans extended by the financial sector go to 1% of clients. The programmatic operation promotes transparency in financial information and greater access to financing for users of the financial system, with special emphasis on small and medium-sized clients.⁸

a. Transparency of financial intermediation

(i) Benchmark lending rate

- 2.21 In Ecuador there is an implicit ceiling on the interest rate charged by banks for loans, given that their lending rates may not exceed the Conventional Maximum Rate, which, in turn, may not be more than 50% higher than the benchmark lending rate (BLR).⁹ The Central Bank of Ecuador (BCE) calculates the BLR based on

⁷ For example, in Colombia, Comités Asesores Regionales de Competitividad Exportadora [Regional Advisory Committees on Export Competitiveness] have been implemented to promote competitiveness at the local level. In cities such as Bogota, Cali, Medellin, and Bucaramanga this has led to high levels of public-private cooperation including broad private-sector support, in particular of the chambers of commerce. (James Fox, Louis Berger Group Inc., Report on Competitiveness Promotion in Colombia and El Salvador, IDB, 2003).

⁸ Technical-cooperation operation EC/TC-1032 includes actions to evaluate progress in money-laundering control measures.

⁹ According to 2003 Financial Sector Assessment Program report, the way the BLR is calculated in Ecuador limits financial deepening and efficient resource allocation.

lending to companies with an annual sales volume greater than or equal to US\$5 million. The resulting rate (8.8%, in April 2006) limits the possibility of including other segments in the banking system, such as SMEs and medium- and low-income consumer sectors, whose risks exceed the values resulting from the Conventional Maximum Rate. The method of calculating the BLR hinders the growth of credit and encourages financial entities to charge, in addition to the interest rate, a series of commissions, premiums, and other fees to make loans profitable.

- 2.22 **Objective.** The programmatic operation calls for changing the method for calculating the BLR, in order to: (i) ensure that the implicit ceiling on the interest rate does not restrict lending; (ii) lessen the importance of fees and premiums in the financial burden; and (iii) encourage interest rates to reflect the market situation in terms of client type and risk levels. This will promote transparency in the prices charged for money and encourage competition in the financial market.

(ii) Cost of financing

- 2.23 Ecuador's regulatory framework for promoting transparency of information toward consumers of financial services lacks: (i) regulation of the information contained on the electronic boards of banking entities within each agency; (ii) a format for presentation, which should be disseminated through the webpages of each financial entity and of the Superintendencia de Bancos y Seguros [Superintendent of Banks and Insurance] (SBS); (iii) basic regulations on adhesion contracts; (iv) regulations on fees; (v) regulations on the information banks are to provide on expenses for collections without recourse to the courts; and (vi) regulations on the requirement to send advertising on interest rates and fees to the SBS prior to publication.
- 2.24 **Objective.** To disclose all information on effective rates, financial burden, or other similar charges, to all consumers. The programmatic operation supports establishing rules to ensure transparency and disclosure of information on the costs of financial services provided by regulated institutions.

(iii) Solvency of credit- and payment-system users

- 2.25 The lack of adequate and reliable information on borrowers' creditworthiness based on credit and payment histories prevents financial intermediaries from evaluating the quality of client credit risk. In an adequate legal framework, credit bureaus provide credit information, minimizing asymmetries. However, credit bureaus in Ecuador provide incomplete information that does not include favorable and unfavorable data or nonbanking information. The information banking entities receive does not allow them to perform low-cost evaluations of a potential client's risk and payment capacity. This constitutes a lack of transparency regarding the quality of bank assets and limits greater access to the financial market.

- 2.26 **Objective.** The programmatic operation promotes an efficient legal framework to improve the management of private credit-information systems (credit bureaus). An improvement in the quantity, quality, and accuracy of information on clients' and potential clients' credit histories will allow financial institutions to have suitable credit risk information on a larger number of clients at a lower cost. This should enable SMEs, low- and middle-income consumers, and other sectors to obtain more financing under better conditions.

b. Access to financing

(i) Secured transactions and bankruptcy

- 2.27 Ecuador has not implemented a suitable, efficient legal framework governing bankruptcy- and insolvency-resolution procedures and guarantees or promoted efficient guarantee-management systems. The financial system requires a regulatory framework allowing creditors to expeditiously demand payment from debtors who have declared bankruptcy or insolvency. Nor does the country have an effective system to manage secured transactions; this can raise client risk even further and therefore limit access to the financial market. These shortcomings have adversely affected the private sector's access to the financial market. This is particularly true of SMEs and low- and medium-income sectors, which rely fundamentally on secured transactions.
- 2.28 **Objective.** International experience shows that increased certainty in financial transactions diminishes the risk of default by clients, reduces the costs from insolvency and bankruptcy proceedings, leads to a lower financial burden and longer loan repayment periods, and attracts sectors once excluded from these services into the banking system, particularly SMEs and low- and middle-income consumers. The programmatic operation promotes establishing a legal structure that allows the creation, fine-tuning, and enforcement of secured transactions, the establishment of bankruptcy- and insolvency-resolution proceedings, and the creation of an efficient system for secured transaction administration.

III. FIRST PROGRAMMATIC LOAN AND TRIGGER MECHANISMS

- 3.1 The programmatic operation consists of three one-tranche loans, for a total amount estimated at US\$150 million. The activities included in the first tranche, estimated at US\$50 million, and the trigger mechanisms for the subsequent tranches, are described below, in accordance with the policy matrix in Annex II.¹⁰ As with the last two single-tranche loans that are part of the operation, the first loan requires a stable, sustainable macroeconomic environment conducive to the achievement of the country's competitiveness-enhancement objectives.

A. Competitiveness of the real sector

- 3.2 The activities carried out under the first programmatic loan corresponding to this core area of the program are intended to (i) consolidate the legal and administrative engineering of the CNPC's institutional framework; (ii) lay the foundation for actions to reduce business-transaction costs; and (iii) launch policies and mechanisms for the competitive development of SMEs at the national and subnational levels.

1. Institutional framework for competitiveness

- 3.3 The institutional framework will be strengthened through the enactment of an executive order (i) making the CNPC responsible for carrying out the competitiveness strategy; (ii) creating an Executive Committee of the Board of Directors to streamline the CNPC's decision-making process; (iii) identifying the duties of the CNPC's agencies; (iv) establishing mechanisms to appoint private-sector representatives and ensure that they participate in the different CNPC agencies; and (v) determining the CNPC's responsibilities for promoting the competitiveness of local production systems. As part of the process to create the CNPC, and in keeping with the guidelines of the executive order, the Board of Directors will approve a new operational and organizational structure and the Ministry of Economy and Finance will ensure that the budget resources needed for the CNPC to fulfill its duties are transferred. For subsequent programmatic loans to be prepared, evidence will be required showing that the CNPC is working expeditiously and that the private sector is actively represented on it.

2. Transaction costs for firms

a. Improving customs procedures

- 3.4 The Corporación Aduanera Ecuatoriana [Ecuadorian Customs Corporation] (CAE) will approve a plan to expedite customs procedures. The plan will include:

¹⁰ The amount of each of the subsequent programmatic loans is estimated at US\$50 million.

(i) streamlining procedures and enhancing control through a proactive risk-management system; (ii) improving the Sistema Interactivo del Comercio Exterior [Interactive Foreign Trade System] (SICE); (iii) implementing postauditing; and (iv) designing and implementing the Customs Valuation System. Preparation of the two subsequent programmatic loans will begin when the CAE has progressed in implementing the measures called for in the approved plan.

b. Simplification of business startup procedures

- 3.5 The SC will have established one-stop windows in Manta, Esmeraldas, Ibarra, and Riobamba, which will operate according to best practices in Quito and Guayaquil. Preparation of the subsequent programmatic loans will begin once the SC has progressed in defining and implementing the action plan for expanding the coverage of this type of service.

c. Improving vocational training services

- 3.6 The CNCF will design a strengthening plan based on the following principles: (i) fostering competition in the provision of employee-training services; (ii) giving accreditation to companies providing these services in line with required quality standards; (iii) introducing a demand-driven system; and (iv) monitoring and evaluating the activities, outcomes, and impacts of the training programs, with the evaluations leading to an impact on the operation of the system. The subsequent programmatic loans will begin once the CNCF's Board of Directors has approved the strengthening plan and progress has been made in implementing it.

3. Competitive development of SMEs

a. Policy and mechanisms for the competitive development of SMEs

- 3.7 The CNPC will approve an SME productive development policy agreed on by consensus with relevant public-private stakeholders. The policy will provide for the creation of a fund with budget resources to be awarded on a competitive basis. Named FONDEPYMES, the fund will be administrated by an independent agency and will focus exclusively on promoting initiatives to improve market access for SMEs. The fund will emphasize the cofinancing of production integration projects for (i) technological innovation; (ii) business management; and (iii) quality improvement.
- 3.8 To launch the SME competitive development support mechanisms, the first loan provides for (i) enacting an executive order establishing a Consejo Interinstitucional Público-Privado [Public-Private Interagency Council] (CODEPYMES) empowered to implement and oversee the operation of FONDEPYMES in accordance with principles established in the policy. CODEPYMES will have a technical secretariat that will draw up the guidelines for contracting the independent agency and FONDEPYMES's operating regulations.

- 3.9 For successive programmatic loans, the independent agency managing FONDEPYMES will have been contracted and begun operations, and the FONDEPYMES monitoring and evaluation system will have been designed.

b. Promoting public-private business partnerships at the subnational level

- 3.10 The CNPC's Executive Committee will have a mechanism for promoting local competitiveness, which is to include: (i) creating a fund with budget resources to be awarded on a competitive basis for promoting and cofinancing the design and implementation of local production plans; and (ii) an operational plan and the rules for carrying it out. An interagency committee composed of the MEF, the Ministry of Foreign Trade, Industrialization, Fishing and Competitiveness (MICIP), and CORPEI will rely on technical criteria to select the initiatives to be financed.
- 3.11 For the subsequent programmatic loans, it is expected that the fund will be fully operating, will have begun to cofinance subnational production plans, and will have implemented a monitoring and evaluation system. The CNPC's webpage will have a section providing information on (i) how to participate in competitive bidding and the outcomes of bids; (ii) local best practices; and (iii) mechanisms allowing localities to share information. At the beginning of the third programmatic loan, the CNPC is expected to continue to cofinance and implement local production plans. To facilitate the continued implementation of these processes, the CNPC will be responsible for disseminating information on designing local production plans and on best practices and lessons learned.

B. Competitiveness of the financial sector

1. Transparency in financial intermediation

a. Benchmark lending rate

- 3.12 The BCE will have at its disposal the design for a new method to calculate the benchmark lending rate (BLR), incorporating information on credit-market risk. For the subsequent programmatic loans, the new method must be used to calculate the BLR, a strategy to provide communication on the new method must have been designed and implemented, and information on this strategy must continue to be appropriately disclosed.

b. Cost of financing

- 3.13 The SBS will have approved a set of rules to promote transparency in and the disclosure of financial information. These rules, at a minimum, will refer to (i) information-disclosure procedures and requirements; (ii) the calculation and publication of financial costs; (iii) basic regulations on adhesion contracts; (iv) principles for improving customer service; and (v) the determination of

penalties in the event of rules violations. In addition, preparation of the subsequent programmatic loans will begin when evidence is provided that the SBS has designed a campaign to educate banking-services consumers, is ensuring that the financial burden is properly disclosed on a daily basis, and has improved its handling of customer complaints. To achieve this, it will have designed term and effectiveness indicators.

c. Solvency of credit- and payment-system users

- 3.14 A Credit Bureau Law, passed by the National Congress and based on best practices, will make it possible, at a minimum, to: (i) devise an explicit legal framework on credit bureaus; (ii) institutionalize the concept of borrower creditworthiness, encouraging information to flow from sources other than the financial system to credit bureaus; (iii) encourage integrity among credit-information agencies and ensure that information shared with them on persons included in the roster is protected; and (iv) penalize unfair competition practices.
- 3.15 For subsequent programmatic loans, evidence will be provided that the SBS has approved regulations to guide the enforcement of the new Credit Bureau Law. At a minimum, these regulations will: (i) establish mechanisms to encourage rapid response to consumer complaints regarding information; (ii) contain rules on the accuracy of the information; (iii) give guidelines for using specialized parametric models; (iv) provide rules to promote use of complementary financial and credit information from the nonfinancial sector on a person's or company's financial situation; (v) outline implementation of SBS bureau oversight. Credit bureaus will be producing, at a minimum, reports that include all favorable and unfavorable information from the credit and payment system and information from sources other than the financial system. The reports will also offer parametric credit-risk models, particularly on SMEs.

2. Access to financing

a. Secured transactions and bankruptcy

- 3.16 The SBS will have prepared the aforementioned draft legal reforms on insolvency and bankruptcy proceedings as well as on the administration and enforcement of secured transactions, based on best practices. In addition, an Interagency Technical Committee (ITC) composed of financial and nonfinancial public- and private-sector representatives will have been established to reach a consensus on the reforms.
- 3.17 Subsequent programmatic loans will be activated once the ITC has reached a consensus and two draft laws have been submitted to Congress as described below: (i) a draft legal reform on the administration and enforcement of secured transactions agreed on by the Interagency Committee by consensus. At a minimum, it will include transparent principles to reduce the cost of using personal property as

collateral; an effective, transparent, and reliable method for collecting debts (determination of priority and clear procedures for enforcing secured transactions); and a cost-effective system for recording secured transactions; (ii) a draft legal reform on insolvency and bankruptcy, agreed on by the ITC by consensus. At a minimum, it will outline prompt, effective, and impartial insolvency and bankruptcy proceedings and a system to prevent dividing a debtor's resources when individual creditors quickly file lawsuits, and it will provide guidelines on fair principles regarding the priority of creditors.

- 3.18 For the third programmatic loan, evidence must be provided that the country has the aforementioned legal reforms in place and that the SBS has approved a series of administrative and technical regulations in line with international best practices allowing the new legal framework to be enforced.

IV. EXECUTION OF THE PROGRAMMATIC OPERATION

A. Execution

- 4.1 **Borrower, guarantor, and executing agency.** The Government of Ecuador will be the borrower and guarantor of this program and the Ministry of Economy and Finance (MEF) will be the executing agency.
- 4.2 **Execution and administration.** The MEF is the executing agency of the programmatic operation. With the assistance of the CNPC, the agency directly responsible for implementing the national competitiveness strategy, it will provide technical support to the subexecuting agencies for execution of the various components of the programmatic operation. Table IV-1 shows the breakdown of responsibilities in the execution of each component of the programmatic operation.

Table IV-1. Responsibilities of the subexecuting agencies

Executing agency	MEF
Component	Responsible entity (subexecuting agency)
Macroeconomic sustainability	MEF
Institutional framework for competitiveness	CNPC
Improving customs procedures	CAE
Simplifying business startup procedures	SC
Improving vocational-training services	CNCF
Policies and mechanisms for the competitive development of SMEs	MICIP, through the Office of the Deputy Minister for SMEs
Promotion of public-private business partnerships at the subnational level	CNPC
Benchmark lending rate	BCE
Cost of financing, solvency of credit- and payment-system users, and access to financing	SBS

- 4.3 The work of the entities involved in the subsequent programmatic loans will be coordinated through interagency agreements between the MEF as the executing agency of the programmatic operation; the CNPC, as the lead agency responsible for the competitiveness strategy and technical support in the execution; and each subexecuting agency. These agreements will identify the preparatory activities for the subsequent programmatic loans, which will include: (i) the action plans delineating the tasks that each subexecuting agency will be carrying out and a timetable; and (ii) the format for and frequency of the delivery of information for the monitoring reports related to the fulfillment of conditions.

- 4.4 The MEF, as the executing agency of the programmatic operation, is the interlocutor with the Bank. Moreover, through the Office of the Deputy Finance Minister, it is responsible for the general oversight of the programmatic operation to ensure the timely fulfillment of its objectives and targets. This entails: (i) supervising progress in fulfilling the conditions contained in the Policy Matrix; (ii) providing the Bank with the technical, legal, and administrative information necessary to demonstrate fulfillment of the conditions for each programmatic loan to be disbursed; and (iii) supervising the fulfillment of the programmatic operation's outcome indicators.
- 4.5 As the agency responsible for overseeing the competitiveness strategy and for providing technical advice on the programmatic operation, the CNPC will support: (i) the MEF and the subexecuting agencies in issues related to the programmatic operation; (ii) the subexecuting agencies in implementing the action plans and products; and (iii) the MEF, with its own information and information provided by subexecuting agencies, on monitoring the programmatic operation's output and outcome indicators. The subexecuting agencies must comply with the agreements in terms of conditions, action plans, schedules, activities, budgeting, and preparation/compilation of information. The CNPC will be the subexecuting agency of two components of the programmatic operation (see Table IV-1)
- 4.6 For the execution of the programmatic operation, a full-time professional will support the MEF's Deputy Minister of Finance with the oversight and execution tasks. The CNPC will hire another professional to support the Board of Directors in the tasks specifically related to this programmatic operation. Each of the subexecuting agencies will name persons to be responsible for the respective components. In all cases, the highest authority of each subexecuting agency will be directly responsible for executing that agency's component.

B. Related technical support

- 4.7 The programmatic operation will receive resources (US\$587,600) from a technical-cooperation operation (EC-TC1032), which supports the subexecuting agencies in the activities mentioned above and related to the fulfillment of those agencies' objectives. The purpose of the operation is to contribute to the implementation of priority actions that promote: (i) the strengthening of the CNPC and competitiveness at the subnational level; (ii) a better business climate; (iii) the competitive development of SMEs; and (iv) the transparency of financial intermediation. This technical-cooperation operation is one of the main instruments that will facilitate execution of the programmatic operation.
- 4.8 Once the Competitiveness Enhancement Program has ended, the subexecuting agencies will assume responsibility for obtaining sufficient budget resources to continue the initiatives and activities undertaken within the framework of the loan to support policy reforms.

C. Monitoring and evaluation

- 4.9 **Monitoring.** The MEF, with the CNPC's support, will carry out the semiannual monitoring and the annual evaluation of the fulfillment of the program's conditions. This monitoring is intended to help enhance the effectiveness and coordination of the policies, programs, and institutions involved in the programmatic operation. The monitoring results will be made known to the Bank in semiannual status reports on the progress made and the challenges encountered during implementation of the programmatic operation's policy measures. Moreover, the CNPC will be encouraged to disseminate these results on its webpage, facilitating citizens' ability to monitor the AEC's progress.
- 4.10 **Evaluation.** Annex III summarizes the ("output" and "outcome") performance indicators to be measured over time to evaluate the effects of the reforms in light of their objectives. This annex sets baseline values and "outcomes" to be achieved in the medium-term (two years after the last disbursement of the last programmatic loan). The indicators were chosen because of their direct relationship with the actions called for under this programmatic operation. Measuring these outcomes poses theoretical and practical difficulties. Hence, extensive use should be made of administrative records and indicators available in the World Economic Forum's *World Competitiveness Report* and in the World Bank's *Doing Business Database*, which regularly monitor the competitiveness of economies throughout the world.
- 4.11 The CNPC, with support of the subexecuting agencies, will regularly compile the database and the progress reports to be used for each indicator. At the end of the two-year period following the disbursement of the last tranche, the MEF, with the support of the CNPC, will prepare a report on the evolution of the programmatic operation's objectives and indicators. Data pertaining to the execution period will be available for review when the Project Completion Report has been prepared.
- 4.12 The Ecuadorian government has made a commitment to ensure the availability of information needed to evaluate the outcome indicators three years after the completion of the programmatic operation. In accordance with the policy of ex post evaluation of operations, approved by the Board of Executive Directors on 15 October 2003 (see documents DEA/03/40 and GN-2254-5), this information will be made available to allow the Office of Evaluation and Oversight and other interested parties to conduct analyses and prepare reports pursuant to their own criteria. The authorities will fund an ex post evaluation of the programmatic operation.

D. Other features of execution

1. Execution period and disbursement schedule

- 4.13 The technical conditions for the first programmatic loan will have been fulfilled when the loan proposal is submitted for the consideration of the Board. The successive programmatic loans are expected to be disbursed in 2007 and 2008.

2. Policy Letter

- 4.14 The country and the Bank have agreed on a Policy Letter, which presents the programmatic operation within the government's broader economic and social strategy (Annex IV). The design of this operation began with the previous administration. The negotiation process was carried out in the context of significant changes in cabinet positions. Nevertheless, the government has maintained among its work priorities the development of activities to enhance competitiveness and help keep current in the public debate the need to implement structural reforms in this field. In this regard, the current Minister of Economy and Finance, in an official letter dated 10 August 2006, ratified the Policy Letter submitted by the previous Minister on 23 June 2006.

3. Inspection and supervision

- 4.15 The Bank will establish such inspection procedures as it considers necessary for the satisfactory execution of this operation. The borrower will cooperate with the Bank to that end, furnishing the necessary assistance and information.

4. Procurement

- 4.16 Because this is a policy-based loan, this operation involves no goods or services procurement.

V. FEASIBILITY AND RISKS OF THE PROGRAMMATIC OPERATION

A. Beneficiaries

- 5.1 The actions taken through this operation will benefit the business community overall, with the impact directed toward SMEs. The promotion of the institutional framework for competitiveness as a medium- and long-term policy, along with short-term actions to facilitate the reduction of business start up and customs-procedure transactions costs, benefits the business sector overall. The same applies to actions to promote transparency in intermediation costs and greater access to financing. The component of competitive development of SMEs directly benefits such enterprises.

B. Effects and benefits of the programmatic operation

- 5.2 Strengthening an institutional framework for competitiveness through the consolidation of the CNPC as an entity devoted to promoting a forum for ongoing dialogue between the public and private sectors will make it possible to: (i) have updated information on competitiveness and the business climate; (ii) promote interagency work in designing policies; and (iii) reach consensuses on reforms whose implementation requires public-private cooperation to ensure long-term sustainability. In the medium term, this set of tools, used in a context of macroeconomic stability, will improve Ecuador's relative competitive position.
- 5.3 The aim of the actions to reduce firms' transaction costs is to increase their productivity through better customs procedures, simplified business startup procedures, and increased access to more highly skilled human resources. These improvements, in turn, should allow firms to enter international markets. Regarding SMEs, the firms benefiting from the FONDEPYMES cofinancing are expected to enhance their productivity through greater operational efficiency based on better management practices, technology adoption, and lower transaction costs.
- 5.4 The promotion of public-private business partnerships at the subnational level is expected to lead to consensus-based production plans to improve the business climate and opportunities in the regions. These plans will facilitate the implementation of production integration and technological innovation projects, local information systems, and the diversification of the supply of exportable products. These improvements will be reflected in the economic and productive development of the regions. Hence, these local public-private business partnership mechanisms will also make it possible to reach consensuses that will complement the CNPC's efforts to establish a long-term competitiveness agenda in the country.
- 5.5 The programmatic operation seeks to facilitate the private sector's access to financing by encouraging transparency in credit costs and borrowers'

creditworthiness. Another aim of the operation is to lower the risk of financial transactions by promoting efficacy in commercial bankruptcy proceedings and the appropriate creation and use of secured transactions. These actions will directly benefit the business community overall and SMEs and low- and middle-income consumers in particular, by drawing them into the banking system and potentially enhancing their competitiveness.

C. Environmental and social considerations

- 5.6 Environmental and social criteria will be included that are appropriate for the activities to be financed by FONDEPYMES in the context of the SME productive-development policy and program. Regarding public-private business cooperation, relevant environmental and social criteria will be included in the operating regulations of the fund for cofinancing local production plans.

D. Risks

- 5.7 **Political risk.** The country has systemic problems that prevent reaching consensus on the structural reforms needed to promote sustainable growth. Ecuadorian society has been unable to reach the stage where it can have policies essential for long-term development objectives. These characteristics of Ecuador's political situation especially affect progress in processes requiring decisions to be taken to form governing bodies for key institutions and to move forward with legal changes. Such changes include laws facilitating firms' and consumers' access to financing through the defense of creditors' rights (bankruptcy law and secured transactions law). In addition, the possible approval of a bill submitted to the National Congress to restrict the operation of the financial system would undermine the suitable provision of services in that sector.
- 5.8 Consequently, there is no certainty regarding the political capacity to carry out reforms in the medium term to consolidate competitiveness as a tool for developing certain economic sectors. However, this risk is mitigated by the government's intention to move forward with the needed legal reforms. It is also mitigated by the programmatic operation, which will have technical-cooperation funding to help promote, build consensus on, and seek support for the proposed legal reforms among broad sectors.
- 5.9 **Institutional risk.** The CNPC was recently created as an extension of the CNC. Like all recently created institutions, it must go through a consolidation process and establish an institutional and technical reputation. This will allow it to play a leading role, as the agency responsible for, and the catalyst and promoter of, the processes to enhance competitiveness at the national level. To diminish the risk that the CNPC will not be able to promptly assume its role as the facilitator of public-private dialogue on competitiveness, the first programmatic loan calls for a series of strengthening actions.

- 5.10 **Execution risk.** This risk coincides with the limited implementation, monitoring, and oversight capacity of the country's public institutions and the lack of incentives to promote reform. As a mitigating factor, the programmatic operation provides for technical-assistance support and makes funds available to all subexecuting agencies during execution. This will allow for a more fluid implementation phase and contribute to the sustainability of reform by strengthening the institutions involved. Given the large number of subexecuting agencies, effective coordination is crucial for monitoring and executing the programmatic operation. Accordingly, the MEF is expected to initially take on this role, with the technical support of the CNPC.
- 5.11 **External risk.** In a dollarized economy characterized by a strong dependence on primary products, external shocks (lower oil prices, higher international interest rates, and declining flows of external financing) or the unsound management of fiscal policy would have an adverse effect on medium- and long-term macroeconomic sustainability and stability. The Bank has analyzed Ecuador's macroeconomic environment (Annex V). One of the inputs it used is the recent evaluation by the IMF, which points to a favorable short-term situation and structural vulnerabilities. The Bank is supporting the country's efforts to strengthen its management of public investment and debt.

COMPETITIVENESS ENHANCEMENT PROGRAM (EC-L1004)
POLICY MATRIX

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
I. Macroeconomic sustainability			
Contribute to macroeconomic sustainability through competitiveness-enhancing actions	The macroeconomic-policy framework is consistent with the objectives of the programmatic operation and with the guidelines set forth in the sectoral policy letter.	The macroeconomic-policy framework is consistent with the objectives of the programmatic operation and with the guidelines set forth in the sectoral policy letter.	The macroeconomic-policy framework is consistent with the objectives of the programmatic operation and with the guidelines set forth in the sectoral policy letter.
II. Institutional framework for competitiveness			
<p>Facilitate systematic, ongoing public-private consensus building at the national and subnational levels to enhance competitiveness</p> <p>Establish the CNPC¹ to manage the competitiveness strategy, facilitate its implementation, and evaluate its outcomes</p> <p>Strengthen the CNPC to allow it to effectively assume its duties</p>	<p>Decree issued by the President of the Republic (i) making the CNPC responsible for the National Competitiveness Strategy (National Competitiveness Agenda); (ii) creating an Executive Committee of the Board of Directors to streamline the CNPC's decision-making process; (iii) identifying the duties of the CNPC's agencies; (iv) establishing mechanisms to appoint private-sector representatives; and (v) determining the CNPC's responsibilities for promoting the competitiveness of local production systems.</p> <p>Resolution from the Board approving a functional organizational structure for the CNPC to fulfill the responsibilities set forth in the decree</p> <p>Transfer of budget allocations needed for the CNPC to fulfill its mandate</p>	<p>Under the responsibilities set forth in the executive order, the CNPC is operating efficiently and there is evidence of active private-sector participation.</p> <p>The CNPC has streamlined decision-making mechanisms, implemented an efficient operating structure, and strengthened its technical capability to advise the public and private sectors on competitiveness.</p> <p>The CNPC has carried out consensus-building activities between the public and private sector to update the AEC.</p>	The CNPC has deepened public-private dialogue to update the National Competitiveness Agenda (AEC).

¹ The CNPC replaced the CNC in accordance with Decree 505, dated 13 September 2005.

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
III. Transaction costs for firms			
Enhance competitiveness of firms by (i) reducing time and red tape in clearing merchandise through customs; (ii) reducing business start-up time; (iii) improving access to business information; and (iv) improving vocational-training services	<p>Improving customs procedures. The Corporación Aduanera Ecuatoriana [Ecuadorian Customs Corporation] (CAE) has approved an action plan prioritizing (i) the design and implementation of a risk-management system; (ii) the improvement of the Sistema Interactivo del Comercio Exterior [Interactive Foreign Trade System] (SICE); (iii) the implementation of postauditing; and (iv) the design and implementation of the Customs Valuation System.</p> <p>Simplification of business startup procedures. The Superintendencia de Compañías [Superintendent of Companies] (SC) has established one-stop windows in Manta, Esmeraldas, Ibarra, and Riobamba, which operate according to best practices in Quito and Guayaquil.</p>	<p>The CAE has made progress in implementing the action plan.</p> <p>The SC has approved and made progress on an action plan to (i) expand one-stop windows to two localities; (ii) expand coverage provided by the user service centers in Cuenca; and (iii) implement a pilot virtual window.</p> <p>The SC has designed an action plan to improve access to information.</p>	<p>The CAE has implemented the action plan.</p> <p>The SC continues to make progress in implementing the action plan.</p> <p>The virtual windows are working.</p> <p>The SC has implemented an action plan to improve access to business information.</p>
	<p>Improving training services. The Consejo Nacional de Capacitación y Formación Profesional [National Council on Vocational Training and Education] (CNCF) has approved an action plan to (i) foster competition in providing employee-training services; (ii) provide accreditation to companies offering these services in line with required quality standards; (iii) introduce demand-driven management of the vocational-training system; and (iv) monitor and evaluate the activities, outcomes, and impacts of the training programs with the evaluations leading to an impact on the operation of the system.</p>	<p>The CNCF's Board has made progress in implementing the action plan.</p>	<p>The CNCF has implemented its action plan.</p>

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
IV. Competitive development of SMES			
i. Policies and mechanisms for the competitive development of SMEs			
<p>Enhance SMEs' competitiveness and increase their access to lending in the financial system</p> <p>Develop efficient public-private mechanisms for cofinancing the activities of partnership forming, technology adoption, and improved business management so as to promote SME competitiveness</p>	<p>The Consejo Nacional para la Reactivación Productiva y la Competitividad [National Council on Production Revitalization and Competitiveness] (CNPC) has approved an SME productive-development program and policy based on the following principles: (i) that financed initiatives should be demand-driven; (ii) that selection criteria should be competitive and transparent; (iii) that there should be cash and in-kind cofinancing by beneficiaries; and (iv) that there should be an independent evaluation and monitoring system.</p> <p>The program provides for the creation of a fund with budget resources (FONDEPYMES), to be administrated by a private firm, and that focuses exclusively on promoting initiatives to improve market access for SMEs and emphasizes cofinancing production-integration projects for (i) technological innovation; (ii) business management; and (iii) quality improvements.</p> <p>CODEPYMES has been established to implement and supervise the operation of FONDEPYMES.</p> <p>CODEPYMES has approved the operating structure of the technical secretariat, has named the technical secretary and has approved FONDEPYMES's operating regulations.</p> <p>The MEF has allocated the resources necessary for the operation of FONDEPYMES.</p>	<p>The MEF has transferred the allocations necessary for FONDEPYMES to operate.</p> <p>The technical secretariat of the Consejo Interinstitucional Público-Privado [Public-Private Interagency Council] (CODEPYMES) is consistently working according to the policy principles.</p> <p>CODEPYMES has approved guidelines for contracting and then contracts an independent agency and a fiduciary firm to administrate FONDEPYMES.</p> <p>CODEPYMES has designed and implemented a plan to promote the activities to be cofinanced by FONDEPYMES.</p> <p>CODEPYMES has approved a monitoring and evaluation system for FONDEPYMES.</p>	<p>FONDEPYMES is operating according to the regulations.</p> <p>The monitoring and evaluation system is working.</p>

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
ii. Promote public-private business cooperation at the subnational level			
Promote public-private business cooperation at the subnational level as part of the National Competitiveness Strategy	<p>The CNPC has an effective mechanism to promote competitiveness of subnational production systems that includes (i) a fund with budget resources for cofinancing local production plans; (ii) the fund's operating regulations, containing transparent selection and eligibility criteria; and (iii) the plan to promote the fund.</p> <p>The MEF has allocated the resources needed to operate the fund.</p>	<p>The MEF has transferred the allocations necessary for the fund to operate.</p> <p>The CNPC has implemented the plan to promote the fund.</p> <p>The CNPC's webpage has a section that includes (i) information on how to participate in competitive bidding; (ii) invitations to participate in the fund and its results; and (iii) relevant information and best practices for local public-private initiatives.</p> <p>The CNPC has implemented a monitoring and evaluation system.</p>	The cofinancing mechanism is operating.
V. Transparency in financial intermediation			
i. Benchmark lending rate			
The benchmark lending rate (BLR) reflects credit-market risks, using a new calculation method	The BCE has at its disposal the design of a new method for calculating the BLR that reflects credit-market risks.	<p>New methodology approved by the Board of the BCE.</p> <p>New methodology in effect and the BLR disclosed.</p> <p>The BCE has designed and adopted a communication strategy on the methodology of the BLR design and implementation.</p> <p>Determination of costs of banking products in accordance with market conditions.</p>	New methodology in effect and the BLR disclosed

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
ii. Cost of financing			
Have a system for disclosing information that is reliable, timely, and substantive and that can be accessed and compared by financial-service consumers	The Banking Board has approved rules to ensure transparency and disclosure of information on the costs of financial services provided by regulated institutions. The rules must cover, at a minimum: (i) information-disclosure procedures and requirements; (ii) the calculation and publication of financial costs; (iii) basic regulations on adhesion contracts; (iv) principles for improving customer service; and (v) the determination of penalties in the event of rules violations.	Daily disclosure of the financial burden (rates, commissions, and premiums) at the offices of financial institutions and on the SBS's webpage, for the different types of loans and clients (SMEs and consumers). Oversight plans, including the review of transparency rules that have been designed.	Disclosure system in operation. Oversight plans implemented.
		Conceptual proposal of a consumer-education campaign on banking services designed by the SBS. SBS complaints unit restructured.	Education campaign adopted and evaluated. Complaints unit operating.

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
iii. Solvency of credit- and payment-system users			
<p>Establish a legal framework that (i) promotes access to credit, improving the management of private credit-information systems (credit bureaus); and (ii) strengthens bureau oversight</p>	<p>Credit Bureau Law approved by the National Congress and published in the Official Register, which, at a minimum: (i) devises an explicit legal framework on the existence of credit bureaus; (ii) institutionalizes the concept of borrower creditworthiness, encouraging information to flow from sources other than the financial system to credit bureaus; (iii) encourages integrity among credit-information agencies and ensures that information shared with them on persons included in the roster is protected; and (iv) penalizes unfair competition practices.</p>	<p>Resolution of Banking Board that regulates, according to best practices, the new credit-bureau law and that (i) defines mechanisms that encourage rapid processing of consumer complaints regarding information; (ii) establishes rules on the truthfulness of information; (iii) fosters the use of specialized parametric models; (iv) establishes rules on and promotes the use of complementary financial information and nonfinancial-sector credit information and that clarifies the financial situation of a person or firm; (v) promotes healthy-competition practices between credit bureaus; and (vi) outlines a plan for SBS supervision of the credit bureaus.</p> <p>Plans for credit bureau supervision designed.</p> <p>Credit bureaus producing, at a minimum, reports that include all favorable and unfavorable information of the financial system, as well as information from sources other than the financial system.</p>	<p>Credit bureaus offering parametric credit-risk models, particularly on SMEs.</p> <p>Supervision plans for credit bureaus implemented.</p>

Objectives of the programmatic operation	Conditions of the first programmatic loan	Trigger mechanisms of the second programmatic loan	Trigger mechanisms of the third programmatic loan
VI. Access to financing			
A. Secured transactions and bankruptcy			
Promote access to financing by establishing a legal framework that improves insolvency and bankruptcy proceedings for individuals and legal entities and the administration and enforcement of secured transactions	The Interagency Technical Committee (ITC) created and composed of financial and nonfinancial public- and private-sector representatives to reach a consensus on the legal reforms on insolvency and bankruptcy proceedings as well as on the administration and enforcement of secured transactions.		
	Draft legal reform on administering and enforcing secured transactions, prepared by the SBS, that includes, at a minimum: (i) transparent principles to reduce the cost of using personal property as collateral; (ii) an effective, transparent, and reliable method for recovering loans (determining priority and clear procedures for enforcing guarantees) and; (iii) a cost-effective system for recording guarantees.	Legal reform that promotes using and recording secured transactions, agreed on by consensus by the ITC and sent to Congress. Online guarantee-management system designed.	Legal reform that promotes using and recording secured transactions approved. Administrative and technical regulations allowing the implementation of the new legal framework on using and recording secured transactions, approved by the SBS. Online collateral-management system working.
	Draft legal reform on insolvency and bankruptcy, prepared by SBS, that includes, at a minimum: (i) outline of prompt, effective, and impartial insolvency and bankruptcy proceedings; (ii) outline of a system to prevent dividing a debtor's resources when individual creditors quickly file lawsuits; and (iii) determination of fair principles for the priority of creditors.	Legal reform on insolvency and bankruptcy proceedings agreed on by consensus by the ITC and sent to Congress.	Legal reform on insolvency and bankruptcy proceedings approved. Administrative and technical regulations allowing the implementation of the new legal framework for bankruptcy and insolvency procedures approved by the SBS.

COMPETITIVENESS ENHANCEMENT PROGRAM (EC-L1004)
MEANS OF VERIFICATION MATRIX

Objectives of the programmatic operation	Conditions of the first programmatic loan	Means of verification
I. Macroeconomic sustainability		
Contribute to macroeconomic sustainability through competitiveness-enhancing actions	The macroeconomic-policy framework is consistent with the objectives of the programmatic operation and with the guidelines set forth in the sectoral policy letter.	Evaluation of the Bank using as one of the inputs information provided by the IMF as part of the monitoring of the country's macroeconomic situation
II. Institutional framework for competitiveness		
Facilitate systematic, ongoing public-private consensus building at the national and subnational levels to enhance competitiveness. Establish the CNPC ¹ to manage the competitiveness strategy, facilitate its implementation, and evaluate its outcomes. Strengthen the CNPC to allow it to effectively assume its duties.	Decree issued by the President of the Republic (i) making the CNPC responsible for the National Competitiveness Strategy (National Competitiveness Agenda); (ii) creating an Executive Committee of the Board of Directors to streamline the CNPC's decision-making process; (iii) identifying the duties of the CNPC's agencies; (iv) establishing mechanisms to appoint private-sector representatives; and (v) determining the CNPC's responsibilities for promoting the competitiveness of local production systems. Resolution from the Board approving a functional organizational structure for the CNPC to fulfill the responsibilities set forth in the decree. Transfer of budget allocations needed for the CNPC to fulfill its mandate.	Decree from the Office of the President of the Republic. Resolution of the Board of the CNPC approving the functional organizational structure of the CNPC MEF budget resolution
III. Transaction costs for firms		
Enhance competitiveness of firms by (i) reducing time and red tape in clearing merchandise through customs; (ii) reducing business start-up time; (iii) improving access to business information; and (iv) improving vocational-training services.	Improving customs procedures. The CAE has approved an action plan prioritizing (i) the design and implementation of a risk-management system; (ii) the improvement of the Sistema Interactivo del Comercio Exterior [Interactive Foreign Trade System] (SICE); (iii) the implementation of postauditing; and (iv) the design and implementation of the Customs Valuation System.	Resolution of the CAE Board approving the action plan

¹ The CNPC replaced the CNC in accordance with Decree 505, dated 13 September 2005.

Objectives of the programmatic operation	Conditions of the first programmatic loan	Means of verification
	<p>Simplification of business startup procedures. The SC has established one-stop windows in Manta, Esmeraldas, Ibarra, and Riobamba, which operate according to best practices in Quito and Guayaquil.</p> <p>Improving training services. The CNCF has approved an action plan to (i) foster competition in providing employee-training services; (ii) provide accreditation to companies offering these services in line with required quality standards; (iii) introduce demand-driven management of the vocational-training system; and (iv) monitor and evaluate the activities, outcomes, and impacts of the training programs, with the evaluations leading to an impact on the operation of the system.</p>	<p>Agreement establishing one-stop windows in Manta, Esmeraldas, Ibarra, and Riobamba</p> <p>Approval of the action plan by the CNCF</p>
IV. Competitive development of SMEs		
(i) Policies and mechanisms for the competitive development of SMEs		
<p>Enhance SMEs' competitiveness and increase their access to lending in the financial system</p> <p>Developing efficient public-private mechanisms for cofinancing partnership forming, technology adoption, and improved business management so as to promote SME competitiveness</p>	<p>The CNPC has approved an SME productive-development program and policy based on the following principles: (i) that financed initiatives should be demand-driven; (ii) that selection criteria be competitive and transparent; (iii) that there should be cash and in-kind cofinancing by beneficiaries; and (iv) that there should be an independent evaluation and monitoring system.</p> <p>The program provides for the creation of a fund with budget resources (FONDEPYMES), to be administrated by a private firm, and that focuses exclusively on promoting initiatives to improve market access for SMEs and emphasizes cofinancing production-integration projects for (i) technological innovation; (ii) business management; and (iii) quality improvements.</p> <p>CODEPYMES has been established to implement and supervise the operation of FONDEPYMES.</p> <p>CODEPYMES has approved the operating structure of the technical secretariat, has named the technical secretary, and has approved FONDEPYMES's operating regulations.</p> <p>The MEF has allocated the resources necessary for the operation of the FONDEPYMES</p>	<p>CNPC resolution approving the SME productive-development program and policy</p> <p>Executive order implementing the policy and creating CODEPYMES and FONDEPYMES</p> <p>CODEPYMES's resolutions (i) appointing the technical secretary; (ii) approving the functional structure of the technical secretariat; and (iii) approving FONDEPYMES's operating regulations</p> <p>MEF budget resolution</p>

Objectives of the programmatic operation	Conditions of the first programmatic loan	Means of verification
(ii) Promotion of public-private entrepreneurial cooperation at the subnational level		
Promote public-private business cooperation at the subnational level as part of the National Competitiveness Strategy	<p>The CNPC has an effective mechanism to promote competitiveness of subnational production systems that includes (i) a fund with budget resources for cofinancing local production plans; (ii) the fund's operating regulations, containing transparent selection and eligibility criteria; and (iii) the plan to promote the fund.</p> <p>The MEF has allocated the necessary resources for the operation of the Fund</p>	<p>Resolution of the CNPC that approves the establishment of the operational plan, of the operating regulations, and of the fund's promotional plan.</p> <p>MEF budget resolution</p>
V. Transparency in financial intermediation		
(i) Benchmark lending rate		
The BLR reflects credit-market risks, using a new calculation method.	The BCE has at its disposal the design of a new method for calculating the BLR that reflects credit-market risks.	Document with the new method for calculating the BLR, prepared by the BCE
(ii) Cost of financing		
Have a system for disclosing information that is reliable, timely, and substantive and that can be accessed and compared by financial-service consumers	The Banking Board has approved rules to ensure transparency and disclosure of information on the costs of financial services provided by regulated institutions. The rules must cover, at a minimum: (i) information-disclosure procedures and requirements; (ii) the calculation and publication of financial costs; (iii) basic regulations on adhesion contracts; (iv) principles for improving customer service; and (v) the determination of penalties in the event of rules violations.	Publication, in the Official Register, of the Banking Board resolution on rules ensuring transparency and disclosure of information on the costs of financial services and financial burden
(iii) Solvency of credit- and payment-system users		
Establish a legal framework that (i) promotes access to credit, improving the management of private credit-information systems (credit bureaus); and (ii) strengthens bureau oversight.	Credit Bureau Law approved by the National Congress and published in the Official Register, which at a minimum: (i) devises an explicit legal framework on the existence of credit bureaus; (ii) institutionalizes the concept of borrower creditworthiness, encouraging information to flow from sources other than the financial system to credit bureaus; (iii) encourages integrity among credit-information agencies and ensures that information shared with them on persons included in the roster is protected; and (iv) penalizes unfair competition practices.	Publication of the Credit Bureau Law in the Official Register.

Objectives of the programmatic operation	Conditions of the first programmatic loan	Means of verification
VI. Access to financing		
A. Secured transactions and bankruptcy		
<p>Promote access to financing by establishing a legal framework that improves insolvency and bankruptcy proceedings for individuals and legal entities and the administration and enforcement of secured transactions</p>	<p>The ITC created and composed of financial and nonfinancial public- and private-sector representatives to reach a consensus on the legal reforms on insolvency and bankruptcy proceedings as well as on the administration and enforcement of secured transactions.</p> <p>Draft legal reform on administering and enforcing secured transactions, prepared by the SBS, that includes, at a minimum: (i) transparent principles to reduce the cost of using personal property as collateral; (ii) an effective, transparent, and reliable method for recovering loans (determining priority and clear procedures for enforcing guarantees); and (iii) a cost-effective system for recording guarantees.</p> <p>Draft legal reform on insolvency and bankruptcy, prepared by SBS, that includes, at a minimum: (i) outline of prompt, effective, and impartial insolvency and bankruptcy proceedings; (ii) outline of a system to prevent dividing a debtor's resources when individual creditors quickly file lawsuits; and (iii) determination of fair principles for the priority of creditors.</p>	<p>Resolution of the SC creating an ITC</p> <p>Two signed minutes corresponding to two ITC meetings confirming that the mandate for which it was created is being fulfilled</p> <p>Draft legal reform on enforcing guarantees prepared</p> <p>Draft legal reform on insolvency and bankruptcy formulated</p>

COMPETITIVENESS ENHANCEMENT PROGRAM (EC-L1004)
RESULTS MATRIX

Objectives of the programmatic operation	“Output” Policy actions (upon conclusion of the programmatic operation)	“Outcome” (starting two years after the last disbursement)
I. Macroeconomic sustainability		
Contribute to macroeconomic sustainability through competitiveness-enhancing actions		
II. Institutional framework for competitiveness		
<p>Facilitate systematic, ongoing public-private consensus building at the national and subnational levels to enhance competitiveness.</p> <p>Establish the CNPC¹ to manage the competitiveness strategy, facilitate its implementation, and evaluate its outcomes.</p> <p>Strengthen the CNPC to allow it to effectively assume its duties.</p>	<p>The CNPC has streamlined decision-making mechanisms, implemented an efficient operating structure, and strengthened its technical capability to advise the public and private sectors on competitiveness</p> <p>The CNPC has deepened public-private dialogue through the active participation of the advisory committees to update the National Competitiveness Agenda</p>	<p>1. Ecuador has raised its relative competitiveness position</p> <ul style="list-style-type: none"> ➤ WEF’s Growth Competitiveness Index shows a relative improvement (percentile), with the country climbing at least 4 positions within 2 years. ➤ WEF’s Microeconomic Competitiveness Index shows a relative improvement (percentile), with the country climbing at least 4 positions within 2 years <p>Baseline: 2005</p> <p>2. The CNPC has consolidated, has earned a reputation for technical competence, and has a high degree of credibility among private stakeholders.</p> <ul style="list-style-type: none"> ➤ Survey of main competitiveness stakeholders on operation and credibility of the CNPC. <p>Baseline: will be prepared with the support of technical-cooperation operation EC/TC-1032.</p>

¹ The CNPC replaced the CNC in accordance with Decree 505, dated 13 September 2005.

Objectives of the programmatic operation	“Output” Policy actions (upon conclusion of the programmatic operation)	“Outcome” (starting two years after the last disbursement)
III. Transaction costs for firms		
<p>Enhance competitiveness of firms by (i) reducing time and red tape in clearing merchandise through customs; (ii) reducing business start-up time; (iii) improving access to business information; and (iv) improving vocational-training services.</p>	<p>The CAE has improved customs procedures by conducting the following activities to facilitate foreign trade: (i) designing and implementing a risk-management system, (ii) improving SICE, (iii) implementing postauditing, and (iv) designing and implementing the Customs Valuation System.</p> <p>The SC has simplified business startup procedures by (i) opening one-stop windows; (ii) expanding the coverage provided by the user service centers; and (iii) implementing a pilot virtual window.</p> <p>The CNCF has implemented an action plan that includes (previous) (i) fostering competition in providing employee-training services; (ii) giving accreditation to companies providing these services in line with required quality standards; (iii) introducing demand-driven management of the vocational-training system; and (iv) monitoring and evaluating the activities, outcomes, and impacts of the training programs, with the evaluations leading to an impact on the operation of the system.</p>	<p>Enhancement of firms' productivity</p> <ul style="list-style-type: none"> ➤ 50% reduction in the number of days needed to clear goods through customs (baseline 2005: 31 days, CNPC); ➤ 50% reduction in the number of days needed to start a business (baseline 2005: will be prepared with the support of technical-cooperation operation EC/TC-1032); ➤ 30% increase in demand and coverage of vocational-training services (baseline: will be prepared with the support of technical-cooperation operation EC/TC-1032).
IV. Competitive development of SMEs		
<p>Enhance SMEs' competitiveness and increase their access to lending in the financial system</p> <p>Develop efficient public-private mechanisms for cofinancing partnership forming, technology adoption, and improved business management so as to promote SME competitiveness</p> <p>Promote public-private business cooperation at the subnational level as part of the National Competitiveness Strategy</p>	<p>Based on the SME productive development policy:</p> <ol style="list-style-type: none"> a. In keeping with the SME productive-development policy, the CODEPYMES has been created to implement and oversee a fund with budget resources (named FONDEPYMES), in accordance with policy principles. b. FONDEPYMES is operating according to the approved regulations, and competitiveness-enhancement business projects have been cofinanced. c. The CNPC has an effective mechanism to promote competitiveness of subnational production systems and has cofinanced local productive plans. 	<p>Enhanced the productivity and partnering of firms supported by the FONDEPYMES</p> <ul style="list-style-type: none"> ➤ 40% improvement in the WEF indicator that measures partnering (baseline 2004: Ecuador is in the 80th percentile); ➤ Improvement of at least 5% in the productivity of firms receiving FONDEPYMES funding. (Baseline: will be prepared with the support of technical-cooperation operation EC/TC-1032).

Objectives of the programmatic operation	“Output” Policy actions (upon conclusion of the programmatic operation)	“Outcome” (starting two years after the last disbursement)
V. Transparency in financial intermediation and VI. Access to financing		
<p>Use new method for calculating BLR, which reflects credit-market risks.</p> <p>Have a system for disclosing information that is reliable, timely, and substantive and that can be accessed and compared by financial-service consumers</p> <p>Establish a legal framework that (i) promotes access to credit, improving the management of private credit-information systems (credit bureaus); and (ii) strengthens bureau oversight</p> <p>Promote access to financing by establishing a legal framework that improves insolvency and bankruptcy proceedings for individuals and legal entities and the administration and enforcement of secured transactions</p>	<p>The BCE calculates the BLR that reflects credit-market risk, using the new method</p> <p>Approval of rules to ensure transparency and disclosure of information on the costs of financial services provided by regulated institutions, approved by the Banking Board</p> <p>Daily disclosure of the financial burden (rates, commissions, and premiums) of financial institutions and on the SBS's webpage, for the different types of loans and clients (SMEs and consumers)</p> <p>Approval and regulation of the Credit Bureau Law</p> <p>Credit bureaus producing, at a minimum: (i) reports that include all favorable and unfavorable information regarding the financial system; and (ii) at least two credit bureaus offer parametric credit-risk models, particularly on SMEs and middle- and low-income consumers</p> <p>Approval of the legal reform that promotes using and recording secured transactions</p> <p>Administrative and technical regulations allowing the implementation of the new legal framework on using and recording secured transactions, approved by the SBS</p> <p>Online guarantee-management system working</p> <p>Approval of the legal reform on insolvency and bankruptcy proceedings</p>	<ul style="list-style-type: none"> ➤ Income from services as a share of the total income of all financial entities in system decreases to 30% (baseline: 2005, 50%) ➤ Increase of 30% in the average ratio between loans extended in the financial system to SMEs, and GDP (baseline: will be prepared with the support of technical-cooperation operation EC/TC-1032) ➤ A reduction of at least 40% in the incidence of complaints at the SBS specialized unit (baseline 2005, to be calculated with the support of technical-cooperation operation EC/TC-1032) ➤ 40% improvement in the 41 steps and 388 days currently required to enforce guarantees, and the same reduction in their current cost, equivalent to 15.3% of lending operations, as well as in the Creditor Rights Indicator, which is currently 3, compared with 3.8 in the region and 6.3 in the Organisation for Economic Co-operation and Development. (Doing Business Indicators). ➤ Reliable, simplified archive making it possible to establish, improve, and enforce secured transactions ➤ 30% improvement in the time and recovery indicators of creditors of bankrupt firms: baseline: (i) 4.3 years, (ii) 20.7 cents.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

C/10/8/06
29/10/06

PROPOSED RESOLUTION DE-___/06

Ecuador. Loan ___/OC-EC to the Republic of Ecuador
Competitiveness Improvement Program

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Republic of Ecuador, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a competitiveness improvement program. Such financing will be for an amount of up to US\$50,000,000 from the Single Currency Facility of the Ordinary Capital resources of the Bank, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

LEGIII/EC-799802-06
EC-L1004