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Ecuadoran President Mahuad Adopts Dollar as Local Currency

by LADB Staff
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In a deepening political and economic crisis in Ecuador, with protesters demanding his resignation, beleaguered President Jamil Mahuad adopted the US dollar as the national currency, prompting the resignation of the Cabinet. Protests continued, however, as did calls for Mahuad to step down. Mahuad announced the resignations Jan. 10 and said his government would fix the plummeting sucre at a rate of 25,000 to the US dollar. 

After a two-month analysis, I have reached the conclusion that the dollarization system...is the way out for us, and it is how we must proceed," Mahuad said in his televised speech. For the last six months, Mahuad has faced increasing calls to step down as political opponents on both the left and right and business and labor leaders accused him of incompetence in handling Ecuador's economic crisis (see NotiSur, 1999-10-01, 1999-11-05).

In 1999, inflation topped 60%, the economy shrank 7%, and unemployment rose to 17%. The value of Ecuador's currency, the sucre, finished the first working week of 2000 down 17%, after plunging 67% in 1999. Last week, the central bank revised its 2000 inflation target to 65% from the 50% estimated previously.

Last September, after months of negotiations, the government signed a letter of intent with the International Monetary Fund (IMF), promising major economic reforms, higher taxes, and a stronger financial sector in return for an IMF loan. But the government has been unable to fulfill its promises, and the IMF loan has not been finalized.

Meanwhile, after 17 months in office, the assessment of Mahuad's performance could not be more negative. With no solid economic program nor the support of the IMF, and lacking sufficient political finesse to confront the crisis effectively, Mahuad has become the target for the people's frustrations. In August 1998, he took office with a 65% approval rating; in December 1999, it was 8%. More than 50% of Ecuadorans believe he should resign because he has not eased the economic crisis.

Not all Ecuador's troubles can be laid at Mahuad's feet. While he has little political savvy, the rest of the political class in Ecuador shares the blame. The parties are hopelessly splintered. No party has a coherent plan, and all politicians make the same speeches they have been making for years, blaming and threatening each other, yet steadfastly refusing to cooperate to resolve any of the mounting problems. Mahuad's mistakes and the decrepit and corrupt political system have prevented the implementation of any long-term plans, blocked efforts to modernize the country, and made developing a true democracy impossible.
Protests escalate after holidays

The Frente Unitario de Trabajadores (FUT), Ecuador's main labor federation with 600,000 workers, organized the latest protests against Mahuad's government, Congress, and the Supreme Court. Defying the state of emergency that Mahuad decreed, on Jan. 6 about 1,000 demonstrators marched on the presidential palace in Quito to demand the president's resignation. Police fired tear gas to disperse the crowds.

The Frente Popular, which includes unions, students, campesinos, and residents from poor barrios, joined the protests and have threatened an indefinite general strike for Jan. 15. Workers from the state oil company Petroecuador said they would strike Jan. 17.

In addition, the Confederacion de Nacionalidades Indigenas (CONAIE) is holding regional assemblies and proposing an "alternative government." Mahuad said he will finish his term, which runs until January 2003, and the armed forces so far are supporting him and constitutional rule.

Central bank opposed dollarization

Amid the worsening crisis, on Jan. 9, the president said he was dollarizing the economy, despite opposition from the central bank (Banco Central de Ecuador, BCE). He also said his 15-member Cabinet had resigned and he would name replacements in the coming days. A deal was hammered out with Congress to pave the way for approval of several economic reforms, he said, including "modernizing the state," interpreted by many to mean privatizing state industries. Mahuad said he was fixing the value of the sucre at 25,000 to the dollar to halt its devaluation. A year ago, the sucre was valued at 7,000 to the dollar.

Mahuad's move came just two days after the BCE said the solution to Ecuador's crisis would not be found in "rushed, crazy measures," and specifically discounted dollarization. Mahuad said he would call a special session of Congress to fire any BCE directors who tried to block the measure. Mahuad needed approval of the BCE, under the Constitution the body that sets monetary policy, and which is independent from the administration.

BCE president Pablo Better resigned immediately after Mahuad's announcement. The remaining members approved the plan late Jan. 10. Dollarization would essentially require that Ecuador abandon its currency, close the central bank, and surrender effective control of monetary and fiscal policy in return for lower inflation and borrowing costs. It would involve the conversion of salaries and financial and trade deals from sucres into dollars.

The US Treasury Department, with sole authority to print dollars and monitor the use of US currency abroad, has not encouraged dollarization in Ecuador, though it has not publicly opposed the move. Political analyst Cesar Montufar was critical, saying the move would erode the nation's sovereignty and make "the president of the US Federal Reserve" Ecuador's true president.

The IMF said on Jan. 10 it would provide technical help as Ecuador adapts its banks and tax system to the conversion to the dollar. Ecuador, which last year became the first country to default on both its Brady and Eurobond debt, resumes talks with IMF officials in Quito this week. "In light of the
announcement yesterday by the government of Ecuador of its intention to move the economy to full dollarization, the IMF is prepared to send a fact-finding mission to Quito to provide technical assistance in adapting their fiscal and banking strategies to dollarization," said IMF Managing Director Michel Camdessus.

Economists are divided about whether the step makes sense for a country in crisis. Some say abandoning a weak currency in favor of the dollar could shore up confidence. Others warn that quick monetary fixes are no substitute for overhauling the weak banking system and improving fiscal policies. "We are closely watching developments in Ecuador," a senior Treasury official said. "Strong underlying economic policies, including policies to ensure sound banking sector and public finances, will be essential for Ecuador to achieve economic and financial confidence."

"If the dollarization plan acts as a catalyst for other appropriate policies and for politicians to accept the need for reforms, then it could prove a turning point," said Peter West, Latin American economist for BBV Securities. "But dollarization does not solve anything by itself." Economic analyst Alberto Acosta said the decision would have two effects, one political and one financial. "Politically, the president has declared war against the popular sectors," since the monetary conversion will directly affect salaries of workers, whose average income is less than US$100 a month, said Acosta. He said those sectors will surely react strongly, since the government is again opting for solutions that benefit the powerful. Economically, said Acosta,

Mahuad has recognized "that his economic policy has failed and that in the short term there might be a reduction of inflation, but the Ecuadoran economy remains at high risk to what happens internationally." Protests continue Frente Popular president Luis Villacis said the protests would continue until Mahuad resigns and allows the formation of a "government of national unity," with representatives of the Catholic Church, social movements, the armed forces and "honest business leaders."

"Nobody believes Mahuad, nobody trusts him to lead, everyone wants him out because he has been unable to resolve the crisis that has plunged the people into the deepest misery of their lives," said Villacis. He said the civic groups also want to end the country's economic dependence on the IMF. "The IMF has always played around with Ecuador," said Villacis. "It has imposed policies that have only aggravated social problems and its prescriptions are one of the main reasons the country is immersed in one of the most serious crises of its history, perhaps the worst."

The Coordinadora de Movimientos Sociales de Ecuador said the decision "signifies a deepening of the neoliberal model that has aggravated the country's problems and will sink the majority in greater misery." "The announcement of dollarization only means that the family food basket is more out of the reach of the Ecuadoran people," said Villacis. "The solution to the country's crisis is not solved with monetary measures. What would resolve the crisis is injecting money for production, which is paralyzed in Ecuador."

Villacis said the FP had called for a moratorium on the foreign debt, instead directing that money to reactivate various sectors, and that certain prices be frozen. He said dollarization would benefit large businesses and exporters, but "the people will be left with their devalued sucres." [Sources:
El Nuevo Herald (Miami), 01/06/00; The Miami Herald, 01/07/00, 01/08/00; Clarin (Argentina),
01/07/00, 01/09/00; CNN, 01/06/00, 01/09/00, 01/10/00; Spanish news service EFE, 01/06-08/00,
01/10/00, 01/11/00; The New York Times, 01/10/00, 01/11/00; The Financial Times (London), 01/11/00;
Associated Press, 01/07/00, 01/10-12/00; Reuters, 01/08/00, 01/10-12/00]

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