



THE REPUBLIC OF ECUADOR
(the “Republic”)

Invites Holders of its 12 per cent. US Dollar Denominated Global Bonds due 2012 (the “2012 Bonds”) and its US Dollar Denominated Step-Up Global Bonds due 2030

(the “2030 Bonds” together with the 2012 Bonds, the “Bonds”),
to submit, in a modified Dutch auction, offers to sell any or all of the Bonds for cash

THE INVITATION WILL EXPIRE AT 6:00 P.M., CENTRAL EUROPEAN TIME, ON 15 MAY 2009, UNLESS EXTENDED OR EARLIER TERMINATED BY THE REPUBLIC IN ITS SOLE DISCRETION (THE “EXPIRATION DATE”). OFFERS MAY BE WITHDRAWN AT ANY TIME PRIOR TO THE EXPIRATION DATE.

The Republic hereby invites Holders (as defined herein) of the Bonds to submit one or more offers to sell any or all of their Bonds (each, an “Offer”) on the terms and subject to the conditions set out in this description of the invitation to Holders and the accompanying Letter of Transmittal (together, the “Invitation”).

For your convenience, the ISINs, Common Codes and CUSIPs of the Bonds are set out in Annex A to this document and the form of Letter of Transmittal is set out in Annex B to this document.

Once the Republic selects the 2012 Bonds Clearing Price (as defined herein), the Republic will accept all Offers relating to 2012 Bonds validly submitted that specify an Offer Price (as defined herein) equal to or less than the 2012 Bonds Clearing Price. Holders of 2012 Bonds accepted for purchase by the Republic pursuant to this Invitation, will receive, for each 2012 Bond sold, an amount in U.S. dollars equal to the 2012 Bonds Clearing Price. Once the Republic selects the 2030 Bonds Clearing Price (as defined herein), the Republic will accept all Offers relating to the 2030 Bonds validly submitted that specify an Offer Price (as defined herein) equal to or less than the 2030 Bonds Clearing Price. Holders of the 2030 Bonds accepted for purchase by the Republic pursuant to this Invitation will receive, for each 2030 Bond sold, an amount in U.S. dollars equal to the 2030 Bonds Clearing Price.

The Minimum Clearing Price for the 2012 Bonds is U.S.\$300 (the “2012 Minimum Clearing Price”). The Minimum Clearing Price for the 2030 Bonds is U.S.\$300 (the “2030 Minimum Clearing Price”). In each case these amounts are comprised of 29.5% plus 50 basis points and are expressed by reference to a face amount of U.S.\$1,000 of the applicable Series of Bonds.

Subject to the terms and conditions of the Invitation described herein, the Clearing Price for the Bonds accepted for purchase by the Republic will be paid on the Settlement Date (as defined herein) to the tendering Holders whose Offers are accepted.

None of the Republic, the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent (each as defined herein) makes any recommendation as to whether Holders should submit Offers or any representation or warranty, express or implied, as to either the merits or otherwise of submitting an Offer or the price at which any such Offer should be made.

The Republic has designated the Euroclear Bank S.A./N.V. (“Euroclear”) and Clearstream Banking, *société anonyme* (“Clearstream”) for the purposes of the Invitation. Accordingly if you wish to tender Bonds held through a clearing system other than Euroclear or Clearstream you must arrange either for that other clearing system to submit an Offer on your behalf through Euroclear or Clearstream (assuming it is capable of doing so) or you must arrange for your Bonds to be transferred to Euroclear or Clearstream before an Offer is submitted (see “Terms of the Invitation—The Designated Clearing Systems”). Custodians, direct participants and clearing systems may have deadlines prior to the Expiration Date for receiving instructions and should be contacted as soon as possible to ensure proper and timely delivery of instructions.

Questions and requests for assistance may be directed to the Joint Dealer Managers or MacKenzie Partners, Inc. (the “Information Agent”) at the applicable address and telephone number set out on the inside back cover of this document. Additional copies of this document, the Letter of Transmittal and related materials may be obtained from the Information Agent or the Luxembourg Agent (as defined herein).

Joint Dealer Managers

Lazard Frères Banque

Lazard Frères & Co.

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República del Ecuador

Ministerio de Finanzas
Avenida 10 de Agosto #1662
Quito, Ecuador

20 de abril de 2009

Para: Los Tenedores de los bonos 2012 y de los bonos 2030

Es de mi agrado presentarles la invitación de la República del Ecuador para que los Tenedores de los bonos 2012 y de los bonos 2030 ofrezcan dichos bonos en una subasta Holandesa modificada (*modified Dutch auction*). Todos los detalles relevantes de la operación se describen en la Circular de los Tenedores (*Noteholder Circular*), en la cual la presente carta se encuentra adjunta.

Reconocemos que las circunstancias que dan origen a la presente Invitación son inusuales. Dichas circunstancias derivan de aspectos que han venido desarrollándose dentro del país por un largo tiempo y que se remontan a la deuda que dió origen a la Oferta de Intercambio (*Exchange Offer*) llevada a cabo por la República en julio del 2000. Bajo dicha Oferta de Intercambio, los bonos 2012 y los bonos 2030 fueron emitidos a cambio de deudas anteriores, la mayoría de las cuales tenían su origen en los años 80. La Comisión de Auditoría Integral del Crédito Público (“CAIC”) fue creada en este contexto. La CAIC presentó su Informe Final de la Auditoría Integral al Crédito Público Ecuatoriano en el 2008 (el “Informe”).

Ciertos aspectos incluidos en dicho Informe fueron alarmantes. La CAIC encontró indicadores importantes de ilegalidad e ilegitimidad en el proceso de emisión de deuda. Siendo dicho Informe información del dominio público, la República analizó cuidadosamente, por varios meses, la ruta a seguir. Dicho análisis fue llevado a cabo por un grupo de personas provenientes del Ministerio de Finanzas y otras autoridades gubernamentales. En su análisis, este grupo de personas aplicó principios fundamentales a consideraciones tanto legales como económicas, así como en el impacto sobre las necesidades del país. Siempre hemos tenido en mente la necesidad de buscar un balance entre los intereses del pueblo Ecuatoriano y los intereses de los Tenedores, y es así que creemos que la estructura de la subasta Holandesa modificada que se presenta, en la cual la participación es voluntaria, refleja dicho balance.

Claramente la Invitación requiere del uso excepcional de recursos económicos por parte de la República y, no obstante que nuestras reservas se encuentran en sus niveles más bajos desde junio de 2007, hemos apartado los recursos económicos suficientes para destinarlos a la Invitación. Al precio mínimo de compra aplicable para los bonos 2012 y para los bonos 2030 tenemos suficientes recursos económicos para pagar a todos los Tenedores. Bajo la subasta Holandesa modificada, aquellos Tenedores participantes podrán especificar precios más altos que el nivel mínimo de compra y todos aquellos Tenedores que sean exitosos recibirán el mismo precio de compra. Asimismo, les agradeceremos considerar cuidadosamente el precio al que presentarán ofertas competitivas, lo anterior, toda vez que nuestras reservas se encuentran limitadas.

Bajo la administración del Presidente Correa, la República ha buscado implementar cambios políticos y económicos estructurales para el beneficio de la nación Ecuatoriana con el objetivo de revertir muchos años de abusos económicos que se remontan a los años 80. Un pilar fundamental del programa del Presidente Correa, es la nueva Constitución, la cual fue aprobada por el 66% de la población Ecuatoriana en septiembre del año pasado. La República se ha embarcado en un procedimiento de reestructuración integral de las instituciones económicas, políticas y sociales del país. Los retos que la República enfrenta en las áreas de pobreza y desigualdad son enormes y, estos nos han llevado a la necesidad de enfocarnos, principalmente, en los objetivos sociales, particularmente por lo que se refiere a las áreas de salud y educación. Los cambios económicos básicamente están destinados al mejoramiento de la regulación de los mercados, la construcción de un nuevo y más eficiente sistema financiero, incrementar la capacidad competitiva de la economía de la República, fortalecer la presencia de pequeñas y medianas empresas en la economía y participar en la integración de Latinoamérica. Asimismo, hemos procurado fortalecer nuestras relaciones con los organismos de desarrollo regional y reducido nuestra dependencia de otros organismos multilaterales.

Reformas estructurales a los sistemas tributario, monetario y bancario están siendo implementadas. El sistema tributario ha mejorado y la regulación a los sistemas financieros ha sido reestructurada.

Los Tenedores de los bonos 2012 y de los bonos 2030 deben estar conscientes que la presente Invitación se está llevando a cabo en medio de la crisis financiera que envuelve a la economía mundial. Lo anterior, ha tenido un efecto negativo en el flujo de remesas de trabajadores Ecuatorianos viviendo en el extranjero, así como en el precio de ciertas materias primas exportadas por la República. El petróleo representó durante el 2008, más del 50% de los ingresos de la República obtenidos de la exportación, razón por la cual, la caída en los precios del petróleo ha tenido un impacto negativo. La crisis financiera internacional amenaza con afectar a la República con más fuerza que a otros países que cuentan con regulación monetaria y políticas cambiarias convencionales. El régimen de dolarización implementado en el año 2000 significa que la República cuenta con recursos limitados para responder a los embates externos y para proteger a la economía nacional en contra de la crisis financiera mundial. A diferencia de muchos de los socios comerciales de la República que han implementado medidas monetarias y cambiarias considerables para proteger la posición de su balanza de pagos, la República únicamente se encuentra facultada para recurrir a su política tributaria y comercial, así como a ciertos aspectos de su política financiera para mantener la estabilidad económica, los niveles de liquidez necesarios para el funcionamiento del régimen monetario y para alcanzar un nivel aceptable en la balanza de sus cuentas.

Les solicitamos consideren la Circular de los Tenedores cuidadosamente y presenten Cartas de Transferencia (*Letters of Transmittal*) dentro de los periodos especificados. La República del Ecuador no tiene la intención de llevar a cabo otras invitaciones u ofertas relacionadas con los bonos 2012 y los bonos 2030. La Invitación está diseñada para que tanto los Tenedores de los bonos 2012 como de los bonos 2030 y la República pongan fin, de una manera aceptable, a un periodo difícil de la historia de la deuda extranjera de la República del Ecuador.

Agradecemos su comprensión y esperamos en un futuro restaurar nuestras relaciones con la comunidad de inversionistas nacional y extranjera.

Atentamente,



Maria Elsa Viteri Acaiturri
Ministra de Finanzas de la República del Ecuador

Unofficial Translation of Letter from the Minister of Finance of the Republic of Ecuador

20 April 2009

To: The Bondholders of the 2012 and 2030 bonds

I am pleased to present the invitation from the Republic of Ecuador to Bondholders of the 2012 bonds and 2030 bonds to tender these bonds through a modified Dutch auction. All relevant details are described in the Noteholder Circular in which this letter is contained.

We appreciate that the circumstances giving rise to this Invitation are unusual. They derive from concerns circulating within the country for some time relating to the provenance of the debt which gave rise to the Exchange Offer launched by the Republic in July 2000. Under that transaction the 2012 bonds and 2030 bonds were issued in exchange for prior claims, the majority of which trace their heritage back to the 1980s. As a result of these concerns, an independent body, the Commission of Integral Audit of Public Credit ("CAIC") was established. The CAIC published its report in 2008 (the "Report").

A number of the findings in the Report were alarming. The CAIC found significant indications of illegality and illegitimacy in the process of the debt being incurred. With the Report in the public domain the Republic considered carefully for several months the most appropriate route forward. These evaluations were conducted through a group comprising the Ministry of Finance and other governmental authorities which analysed the Report. In its evaluations this group sought to apply fundamental principles to both technical legal considerations and the impact on the needs of the country. In doing so we have always been mindful of the need to balance the interests of the Ecuadorian people and the Bondholders and we believe that the modified Dutch auction structure we now present, participation in which is voluntary, strikes this balance.

Clearly the Invitation will require an exceptional use of the Republic's resources and, whilst our reserves have dipped to their lowest levels since June 2007, we have set aside necessary funds for the purposes of this Invitation. At the minimum clearing price for the 2012 bonds and 2030 bonds we have sufficient resources to pay all Bondholders. Under the modified Dutch auction structure tendering Bondholders may specify prices higher than these minimum levels and all successful Bondholders will receive the same clearing price. We would ask you to consider carefully the price at which any competitive tender is submitted as we have only limited flexibility in the use of additional reserves.

Under President Correa, the Republic has sought to initiate deep political and economic changes for the benefit of the country and with a view to reversing many years of economic mismanagement dating back to the 1980s and earlier. A central pillar of this programme is a new Constitution and this was approved by 66% of the Ecuadorian population in September of last year. Ecuador has embarked on a comprehensive process of restructuring the country's economic, political and social institutions. The challenges which Ecuador faces in the areas of poverty reduction and inequality are considerable and this has led to a focus on social goals particularly in the areas of health and education. The economic changes focus primarily on improving the system of market regulation, constructing a new financial architecture, extending the competitive capacity of the Ecuadorian economy, strengthening the presence of the small and medium sized producers in the economy and participating in Latin-American integration. We have also sought to strengthen our relations with regional development institutions and reduced our reliance on other multilateral institutions.

Fundamental reforms of the fiscal, monetary and banking systems have started to be implemented. The tax system has been improved and the system of financial regulation has been restructured.

Bondholders of the 2012 and 2030 bonds will be aware that this Invitation is being made against the back drop of the severe international financial crisis. This has had a negative impact on the flow of remittances into Ecuador from workers abroad as well as contributing to a fall in the prices of several raw materials exported from the country. With crude oil representing more than 50% of the Republic's export revenues

in 2008, the recent oil price fall has also had a significant negative impact. The international financial crisis also threatens to affect Ecuador to a higher degree than other countries in the region who have conventional monetary and exchange rate tools. The dollarised regime adopted in 2000 means that Ecuador has limited policy instruments with which to respond to exogenous shocks and protect the economy against the global crisis. Unlike many of Ecuador's trading partners that have aggressively used monetary and exchange rate policy to protect their balance of payments position, Ecuador is only able to turn to fiscal, commercial and some financial policy instruments to maintain the stability of the economy, control required liquidity levels for a normal functioning of the monetary regime and to achieve an acceptable balance of its external accounts.

We encourage you to consider the Noteholder Circular carefully and to submit Letters of Transmittal within the specified timetable. The Republic of Ecuador does not intend to make any further invitations or offers in respect of the 2012 and 2030 bonds. The Invitation is designed to assist in allowing both the 2012 and 2030 Bondholders and the Republic to close, on an acceptable basis, a very challenging period in Ecuador's external debt history.

We appreciate your understanding and consideration and we look forward to restoring normal relations with the national and international investor community.

Yours sincerely

Maria Elsa Viteri Acaiturri
Minister of Finance of the Republic of Ecuador

CERTAIN INVITATION MATTERS

Holders may withdraw their Offers pursuant to the procedures described below at any time prior to the Expiration Date but not thereafter. In the event of a termination of the Invitation, the Bonds subject to Offers will be returned to Holders promptly. OFFERS MAY NOT BE WITHDRAWN AFTER THE EXPIRATION DATE.

Upon the consummation of the Invitation, the ability of a Holder to sell or buy Bonds not tendered pursuant to the Invitation is likely to be more limited than it was prior to the Invitation, which might adversely affect the liquidity, market value and price volatility of those Bonds. See “Certain Considerations—Considerations Relating to the Invitation” for more information.

Other than to the Joint Dealer Managers, the Republic will not pay any commissions or other remuneration to any broker, dealer, salesman or other person for soliciting Offers of Bonds. Tendering Holders will not be obligated to pay the fees of the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent.

The Republic expressly reserves the right, in its sole discretion, subject to applicable law, to: (i) terminate the Invitation and not accept any Offers; (ii) waive any and all conditions of the Invitation on or prior to the Acceptance Date; (iii) extend the Expiration Date; or (iv) amend the terms of the Invitation in one or more jurisdictions. These rights are in addition to the Republic’s right to delay acceptance of Offers submitted in the Invitation or to delay payment for the Bonds purchased pursuant to the Invitation to comply in whole or in part with any applicable law.

If the Invitation is terminated early, withdrawn or otherwise not consummated, the applicable Clearing Price will not be paid or become payable to Holders. In any such event, Bonds previously tendered pursuant to the Invitation will be promptly returned to the tendering Holders.

At any time and from time to time after the Expiration Date or earlier termination of the Invitation, the Republic, Ecuadorian governmental agencies or others acting on the Republic's or their behalf may acquire any Bonds, to the extent permitted by applicable law, through open market purchases or otherwise. There can be no assurances as to whether the Republic, Ecuadorian governmental agencies or others acting on its or their behalf may choose to pursue any such alternatives in the future.

See “Certain Considerations” for a discussion of certain factors that should be considered in evaluating the Invitation.

In this document, “U.S.\$” and “dollars” mean U.S. dollars.

IMPORTANT INFORMATION

In making your decision to submit an Offer, you must rely on your own examination of the Republic and the information contained herein. The Republic has not authorised anyone to provide you with information that is different from, or supplemental to, that appearing in this document. In offering your Bonds, you will be deemed to have acknowledged that you have reviewed this document.

If you wish to submit an Offer with respect to your Bonds, you must submit, or arrange to have submitted on your behalf, at or before the Expiration Time, a duly completed Letter of Transmittal and tender your Bonds, as described below. You may use a single Letter of Transmittal in respect of your 2012 Bonds and 2030 Bonds. If you hold only one Series of Bonds, the sections of the Letter of Transmittal relating to the Series of Bonds which you do not hold should be left blank. A Letter of Transmittal may be submitted only by a direct participant in Euroclear or Clearstream (we refer to any such direct participant as a "Holder"). Letters of Transmittal may be submitted by hand, by courier or by facsimile transmission. The procedures for submitting Letters of Transmittal and delivering Bond Instructions (as defined herein) are set out under "Terms of the Invitation—Procedures for Submitting Offers." If you wish to tender Bonds held through a clearing system other than Euroclear or Clearstream you must arrange either for that other clearing system to submit a Letter of Transmittal on your behalf through Euroclear or Clearstream (assuming it is capable of doing so) or you must arrange for your Bonds to be transferred to Euroclear or Clearstream before a Letter of Transmittal is submitted in respect of such Bonds.

A beneficial owner of Bonds held through a clearing system that is not a direct participant in Euroclear or Clearstream and who wishes to participate in the Invitation must instruct the direct participant through which such owner holds its Bonds to submit a Letter of Transmittal and Bond Instructions with respect to the offered Bonds on the beneficial owner's behalf and, by doing so, such beneficial owner agrees to all matters set out in such Letter of Transmittal and Bond Instructions. A letter of instruction is included in the materials provided along with this document, which letter may be used by a beneficial owner to instruct the direct participant or indirect participant to effect and submit (or procure the effecting and submission of) Bond Instructions and Letters of Transmittal.

This description of the Invitation does not constitute an offer to buy or an invitation to submit an Offer in any jurisdiction in which, or to or from any person to or from whom, it is unlawful to make such invitation under applicable securities or blue sky laws. If this description of the Invitation, the accompanying Letter of Transmittal or any other materials relating to the Invitation come into your possession, you are required by the Republic to inform yourself of and observe all applicable restrictions. In any jurisdiction in which the Invitation is required to be made by a licensed broker or dealer and the Joint Dealer Managers or any affiliate of the Joint Dealer Managers is a licensed broker or dealer in that jurisdiction, the Invitation is being made in that jurisdiction to the extent permitted by applicable law by the Joint Dealer Managers or that affiliate on behalf of the Republic.

The Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent make no representations whatsoever regarding this Invitation or the Bonds. The responsibility for the Invitation rests solely with the Republic.

By signing the Letter of Transmittal, each Holder will irrevocably: (i) release and discharge any and all claims it may have against the Joint Dealer Managers arising out of or in relation to the Invitation or the transactions contemplated thereby (the "Claims"); and (ii) agree not to sue the Joint Dealer Managers with respect to the Claims in any jurisdiction.

Neither the Joint Dealer Managers nor anyone acting on their behalf has independently verified this document and neither this document nor the form and substance of the disclosure herein has been approved by the Joint Dealer Managers. Accordingly, the Joint Dealer Managers make no representation or warranty, express or implied for the accuracy, completeness or adequacy of information contained herein or in any further information, notice or other document which may at any time be supplied in connection with the Invitation. Therefore, no liability to any party is accepted by the Joint Dealer Managers in connection with any of the above matters.

FORWARD-LOOKING STATEMENTS

This Noteholder Circular contains forward-looking statements. Forward-looking statements are statements that are not historical facts, including statements about the Republic's beliefs and expectations. These statements are based on current plans, estimates and projections, so you should not place undue reliance on them. Forward-looking statements speak only as of the date they are made. The Republic undertakes no obligation to update any of these statements in light of new information or future events.

Forward-looking statements involve inherent risks and uncertainties. The Republic cannot assure you that actual events or results will not differ materially from any forward-looking statements contained in this Noteholder Circular. In particular, a number of important factors could cause actual results to differ materially from the Republic's expectations. Such factors include, but are not limited to:

- adverse external factors, such as:
 - changes in the international prices of commodities (including oil) and/or international interest rates, which could affect the Republic's fiscal accounts, budgetary expenditures and the current account of the balance of payments;
 - changes in import tariffs and exchange rates, a recession or low economic growth affecting the Republic's trading partners, all of which could lower the growth or the level of exports of the Republic, a reduction in the growth or the level of income from tourism of the Republic, a reduction in the growth rate or a contraction of the Republic's economy and, indirectly, a reduction in tax revenues and other public sector revenues, adversely affecting the Republic's fiscal accounts;
 - a decrease in remittances from Ecuadorians residing and working abroad;
 - a decline in foreign direct investment, which could adversely affect the Republic's balance of payments and the level of the Central Bank's international reserves;
 - changes in the level of foreign aid or other external support provided by other countries;
 - the recent extreme contraction of liquidity in the international financial markets and equity, debt and foreign exchange market volatility, which could lead to domestic volatility and potentially lower international reserves;
 - decisions of multilateral institutions, such as the Inter-American Development Bank ("IDB"), regarding the terms of their financial assistance to the Republic; and
 - international geo-political tensions and uncertainties;
- adverse domestic factors, such as lower than expected fiscal revenues or a higher inflation rate, which could induce higher domestic interest rates. These factors could lead to lower economic growth, a decline in exports and income from tourism and a decrease in the Central Bank's international reserves;
- expectations regarding the payment of interest and principal with respect to the Republic's outstanding bonds and treatment of the Republic's outstanding bonds;
- expectations about the behaviour of the Ecuadorian economy if certain economic policies are implemented;
- political instability;

- changes to the Republic's current judicial system;
- changes in the Republic's relationship with other nations;
- policy changes instituted by future administrations in the Republic or mandated by the Ecuadorian National Assembly; and
- other adverse factors, such as climatic, seismic or political events.

SUMMARY TIMETABLE FOR THE INVITATION

The following summary timetable is qualified in its entirety by, and should be read in conjunction with, the more detailed information appearing elsewhere in this document. Unless otherwise defined herein, capitalised terms used in this summary have the respective meanings specified elsewhere in this document.

Date	Calendar Date	Event
<i>Launch - Commencement Date of the Invitation</i>	20 April 2009	Distribution of the description of the Invitation and the accompanying materials.
<i>Expiration Date</i>	6:00 P.M., Central European Time (“CET”), 15 May 2009 (unless extended by the Republic in its sole discretion)	Deadline for Submitting: (1) Letters of Transmittal to the Tender Agent or, if applicable, the Luxembourg Agent; and (2) Bond Instructions to the applicable clearing system (i.e., Euroclear or Clearstream only). ¹
<i>Acceptance Date</i>	At or around 2:00 P.M., CET, 26 May 2009	The Republic announces the Clearing Price for the Bonds that are accepted pursuant to the Invitation.
<i>Settlement Date</i>	29 May 2009	Payment of the Clearing Price for the Bonds accepted pursuant to the Invitation on the Acceptance Date.

¹ *The clearing systems and custodians for the Bonds may in accordance with their normal procedures establish earlier deadlines for the receipt of Bond Instructions from their participants. If you wish to tender Bonds held through any other clearing system than Euroclear or Clearstream, you must arrange to either (i) transfer the Bonds to either Euroclear or Clearstream, or (ii) have such other clearing system submit a tender on your behalf through Euroclear or Clearstream (assuming such other clearing system is capable of doing so). This process will take additional time. See “Terms of the Invitation—Procedures for Submitting Offers.”*

PURPOSE OF THE INVITATION

The Republic's objective in this transaction is to reduce the liability represented by the Bonds.

THE BONDS

In 2000, the Republic issued two series of U.S. dollar denominated bonds: 12 per cent. US Dollar Denominated Global Bonds due 2012 and US Dollar Denominated Step-Up Global Bonds due 2030.

Any reference to a "Series of Bonds" is to the 2012 Bonds or the 2030 Bonds as applicable.

Copies of the following documents will be available for inspection during normal business hours at the office of Dexia Banque International á Luxembourg (the "Luxembourg Agent") or Information Agent specified on the back cover of this document:

- the Trust Indenture for the 2012 Bonds;
- the Trust Indenture for the 2030 Bonds; and
- this Noteholder Circular, including the related Letter of Transmittal.

NO RECOMMENDATION

In considering this Invitation, Holders will need to make their own evaluation of the risks associated with participating in the Invitation and with not participating. **None of the Republic, the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent makes any recommendation as to whether Holders should submit Offers or any representation or warranty, express or implied, as to either the merits or otherwise of submitting an Offer or the price at which any such Offer should be made.**

TERMS OF THE INVITATION

General

On the terms and subject to the conditions of the Invitation (including, if the Invitation is extended or amended, the terms and conditions of any such extension or amendment), the Republic invites Holders to submit Offers in respect of the 2012 Bonds and to submit offers in respect of the 2030 Bonds in accordance with the procedures set out herein. You may submit Offers with respect to any number of the Bonds you hold. If and when the Republic accepts Offers to sell Bonds, it shall announce in a press release issued to an international news service, such as Bloomberg News or the Reuters News Service (each, a “News Service”), on an acceptance date that shall be on or about the eleventh calendar day following the Expiration Date (the “Acceptance Date”) the Clearing Price for the 2012 Bonds and the Clearing Price for the 2030 Bonds that are, in each case, accepted pursuant to the Invitation.

The Republic agrees that each Holder whose Offers are accepted will receive:

- (1) in respect of that Holder’s 2012 Bonds accepted for purchase, subject to the conditions of the Invitation, for each 2012 Bond, an amount in cash equal to the 2012 Bonds Clearing Price; and
- (2) in respect of that Holder’s 2030 Bonds accepted for purchase, subject to the conditions of the Invitation, for each 2030 Bond, an amount in cash equal to the 2030 Bonds Clearing Price.

The Clearing Price for the 2012 Bonds and the Clearing Price for the 2030 Bonds accepted by the Republic will, in each case, be determined by the Republic in its sole discretion following the modified Dutch auction process described below. The aggregate 2012 Bonds Clearing Price and the aggregate 2030 Bonds Clearing Price will be for the benefit of the tendering Holders whose Offers have been accepted by the Republic, and will be paid to the tendering Holders whose Offers were accepted in U.S. dollars on the date falling three Business Days after the Acceptance Date (the “Settlement Date”).

The Clearing Price will be the price paid for all rights relating to the applicable Bonds and accordingly there will be no separate or additional payment in respect of accrued interest.

Auction Procedures

In relation to any one Series of Bonds, you may not specify more than one Offer Price in a Signature Annex (which forms part of a Letter of Transmittal and is defined therein). Accordingly, if you wish to submit separate Offer Prices in relation to any one Series of Bonds that you hold, you must submit separate Signature Annexes in relation to each of those Offer Prices. (For example, if you hold only 2012 Bonds and you wish to specify three Offer Prices, you must submit three Signature Annexes, one for each Offer Price.) However, if you hold both 2012 Bonds and 2030 Bonds, Offer Prices in respect of Bonds you hold of both such Series may be set out in the same Signature Annex.

For each Offer you submit, you may either:

- (1) specify a minimum price that you would be willing to accept as the Clearing Price for the Bonds (such specified minimum price is referred to as the “Offer Price” for that Offer). The Offer Price should:
 - (a) be expressed in U.S. dollars as a price per U.S.\$1,000 face amount of the applicable Bond and in increments of U.S.\$1.00 (Offers expressed in other increments will be rounded upward to the nearest U.S.\$1.00); and
 - (b) not be lower than the Minimum Clearing Price; or
- (2) not specify any Offer Price.

Any Offer that is submitted with a specified Offer Price greater than the Minimum Clearing Price is referred to as a “Competitive Offer”. Any Offer that is submitted without a specified Offer Price is referred to as a “Non Competitive Offer”.

Discretion on the Part of the Republic; Selection of Clearing Price

The Republic reserves the right in its sole discretion not to accept any Offers. Further, the Republic may choose to select Offers for one Series of Bonds only. If the Republic decides to accept any Offers, the Republic in its sole discretion will select and announce the Clearing Price at which it will accept Offers. If the Republic decides to accept Offers in respect of the 2012 Bonds, the Clearing Price announced by the Republic and designated for these purposes in respect of the 2012 Bonds is the “2012 Bonds Clearing Price”. If the Republic decides to accept Offers in respect of the 2030 Bonds, the Clearing Price announced by the Republic and designated for these purposes by the Republic in respect of the 2030 Bonds is the “2030 Bonds Clearing Price”. The 2012 Bonds Clearing Price may not be less than the 2012 Minimum Clearing Price. The 2030 Bonds Clearing Price may not be less than the 2030 Minimum Clearing Price.

Any reference to a “Clearing Price” in respect of a Series of Bonds is, in relation to the 2012 Bonds, to the 2012 Bonds Clearing Price and, in relation to the 2030 Bonds, to the 2030 Bonds Clearing Price. Any reference to a “Minimum Clearing Price” in respect of a Series of Bonds is, in relation to the 2012 Bonds, to the 2012 Minimum Clearing Price and, in relation to the 2030 Bonds, to the 2030 Minimum Clearing Price.

Acceptance of Offers

Once the Republic selects the Clearing Price in relation to a Series of Bonds, the Republic will accept:

- (1) all Non Competitive Offers validly submitted prior to the Expiration Date for such Series of Bonds; and
- (2) all Competitive Offers validly submitted prior to the Expiration Date that specify Offer Prices equal to or less than the Clearing Price for such Series of Bonds.

Each Holder whose Offer is accepted by the Republic will have the benefit of the applicable Clearing Price, even if the Holder specified a lower Offer Price.

The Republic will not accept Competitive Offers in respect of a Series of Bonds that specify Offer Prices greater than the applicable Clearing Price.

Expiration Time and Date; Extension

The Invitation will expire at 6:00 P.M., CET, on 15 May 2009 (such time and date, the “Expiration Time” and the “Expiration Date”), unless extended by the Republic, subject to the Republic’s right to terminate or amend the Invitation as set out below under “Terms of the Invitation—Extension, Termination or Amendment; Announcement”.

Subject to applicable law, the Republic, in its sole discretion, may from time to time extend the Expiration Date by announcing such extension in a press release issued to the News Services on or prior to 2:00 P.M., CET, on the first Business Day following the Expiration Date, in which case the terms “Expiration Time” and “Expiration Date” will mean the latest time and date to which the Invitation has been so extended. “Business Day” means a day on which Euroclear and Clearstream and commercial banks in London are all open for business.

The Designated Clearing Systems

The Republic has designated the following clearing systems for purposes of the Invitation:

- (1) Euroclear; and

(2) Clearstream.

In particular, Bonds may not be tendered through The Depository Trust Company (“DTC”) and the Invitation will not be made eligible in DTC’s system. If you wish to tender Bonds held through any other clearing system than Euroclear or Clearstream, you must arrange either to (i) transfer the Bonds to either Euroclear or Clearstream, or (ii) have such other clearing system submit a tender on your behalf through Euroclear or Clearstream (assuming such other clearing system is capable of doing so). This process will take additional time. You are required to make yourself aware of the procedures and deadlines of such other clearing system in tendering your Bonds, and we cannot assure you that you will succeed in tendering your Bonds that are held through such other clearing system. For the risks involved in tendering Bonds through Euroclear or Clearstream if you hold Bonds through DTC or any other clearing system that is not Euroclear or Clearstream, see “Certain Considerations—Considerations Relating to Participating in the Invitation”.

Procedures for Submitting Offers

If you wish to submit an Offer with respect to your Bonds, you must submit, or arrange to have submitted on your behalf, at or before the Expiration Time, a properly completed and duly executed Letter of Transmittal. A properly completed and duly executed Letter of Transmittal (or manually signed facsimile thereof) and any other documents required by the Letter of Transmittal, must be received by the Tender Agent and, if applicable, the Luxembourg Agent, at the address set forth on the inside back cover page hereto at or before 6:00 P.M., CET, on the Expiration Date. Only direct participants in Euroclear and Clearstream, may submit Letters of Transmittal with respect to Bonds held in a clearing system. Letters of Transmittal may be submitted in the following ways:

- by facsimile to the Tender Agent (and, if you are in Luxembourg, to the Luxembourg Agent), at its facsimile number specified in the Letter of Transmittal and on the face of the Letter of Transmittal attached as Annex B to this Noteholder Circular; or
- by courier or by hand delivery to the Tender Agent (and, if you are in Luxembourg, the Luxembourg Agent), at its address specified in the Letter of Transmittal and on the back cover of this document. The Luxembourg Agent may have deadlines prior to the Expiration Date for receiving instructions and should be contacted as soon as possible to ensure proper and timely delivery of instructions.

In addition you must deliver Bond Instructions, in one of the following ways:

- if you are a direct participant in Euroclear or Clearstream, you must deliver Bond Instructions to Euroclear or Clearstream, by 6:00 P.M., CET, on the Expiration Date (or, if earlier, the deadline specified by the relevant clearing system), unless such deadline is extended; or
- if you are a beneficial owner of Bonds held in a clearing system, you must instruct a direct participant in Euroclear or Clearstream to deliver Bond Instructions on your behalf, and the direct participant must in fact deliver those Bond Instructions by 6:00 P.M., CET, on the Expiration Date (or, if earlier, the deadline specified by the relevant clearing system), unless such deadline is extended.

Bond Instructions must be delivered to and received by Euroclear or Clearstream, in accordance with their normal procedures on or prior to the deadlines established by each of those clearing systems. Note that such deadlines may be earlier than the time and date on which Bond Instructions are due pursuant to this Invitation. In any case, the related Bond Instructions must be received by Euroclear or Clearstream, as the case may be, at or before 6:00 P.M., CET, on the Expiration Date, or such earlier time and date as such clearing system may require, unless this deadline is extended by the Republic through notice to Euroclear and Clearstream or by press release issued to the News Services. In all cases, you are responsible for informing yourself of these deadlines and for arranging the due and timely delivery of Bond Instructions to Euroclear or Clearstream.

Direct participants in Euroclear and Clearstream must include in each Letter of Transmittal that is submitted pursuant to the Invitation the reference code for the Bonds that is generated by Euroclear or Clearstream upon the submission of blocking instructions.

Each Letter of Transmittal must have the same reference code as the Bond Instructions relating to it. No two Letters of Transmittal may contain the same reference code. The Republic, in its sole discretion, may consider invalid any Letter of Transmittal submitted without such reference code, or with a reference code that does not match the reference code in the corresponding Bond Instructions.

“Bond Instructions” means:

- irrevocable instructions to: (1) block any attempt to transfer your Bonds on or prior to the Settlement Date and (2) debit your account on the Settlement Date in respect of all of the Bonds that you have tendered, upon receipt of an instruction from the Tender Agent that such Bonds are accepted for purchase by the Republic;
- an irrevocable authorisation to disclose the name of the direct account holder in Euroclear and Clearstream, and information about the foregoing instructions;
- a confirmation that the direct participant submitting the Bond Instructions is concurrently delivering a Letter of Transmittal with respect to the Bonds,

subject to the automatic withdrawal of the irrevocable instruction in the event the Invitation is terminated by the Republic and your right to withdraw your Offer prior to the Expiration Time.

If you are not a direct participant in Euroclear or Clearstream, you must ensure that the Bond Instructions transmitted through the Euroclear or Clearstream direct participant can be reconciled with the Letter of Transmittal submitted on your behalf. To the extent that Bond Instructions cannot be reconciled with your Letter of Transmittal, your Letter of Transmittal may be deemed to have been improperly submitted and your Bonds will not be considered as offered.

Please submit a separate Bond Instruction for each Letter of Transmittal you submit. In no event should any Letters of Transmittal be sent to the Republic or any Ministry or agency of the Republic.

None of the Republic, the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent will be responsible for the communication of Offers by:

- beneficial owners to the direct participant in Euroclear or Clearstream, through which they hold Bonds; or
- the direct participant in Euroclear or Clearstream, to the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent, Euroclear or Clearstream.

If you hold your Bonds through a custodian, you should contact that custodian to discuss which of the above options can be used by your custodian to submit Offers on your behalf.

In any case, you are responsible for arranging the timely delivery of your Letter of Transmittal and Bond Instructions.

The method of delivery of the Letter of Transmittal, the Bonds and all other required documents, including delivery through Euroclear or Clearstream is at the option and risk of the Holder and, except as otherwise provided in the Invitation, delivery will be deemed made only when actually received by the Joint Dealer Managers.

No alternative, conditional or contingent Offers will be accepted. All Holders, by execution of the Letter of Transmittal (or a facsimile thereof), waive any right to receive any notice of the acceptance of their Offer.

Acceptance and Payment

On the terms and subject to the conditions of the Invitation, on the Settlement Date, the Republic will pay for the Bonds validly offered (and not withdrawn) and accepted by the Republic pursuant to the Invitation. Payments for Bonds purchased pursuant to the Offer will be made with same day funds.

In order to receive payment of the Clearing Price for your offered and accepted Bonds, you must deliver to the Republic (or the person nominated by the Republic) good and marketable title to the Bonds free and clear of all liens, charges, claims, encumbrances, interests, rights of third parties and restrictions of any kind and such Bonds are not be subject to any adverse claim or right. **The Republic reserves the right in its sole discretion to reject any Offer where it determines in its sole discretion that good and marketable title to the Bonds is not delivered.**

For the purposes of the Invitation, Bonds tendered pursuant to the Invitation will be deemed to have been accepted for payment by the Republic, and thereby agreed to be purchased, if, as and when the Republic gives written notice thereof (such notice, the "Notice of Acceptance") to the Joint Dealer Managers on the Acceptance Date. Once the Notice of Acceptance is delivered, the Republic's acceptance of Bonds will be irrevocable and will constitute a binding obligation of the Holders to sell such Bonds on the Settlement Date and a binding obligation of the Republic to pay the Clearing Price in cash. *Under no circumstances will interest on the Clearing Price be paid by the Republic by reason of any delay in making any payment later than any payment date specified herein.*

If the Clearing Price in respect of any Bonds accepted for payment is not paid by or on behalf of the Republic to Euroclear or Clearstream for onward distribution to the applicable direct participant in Euroclear or Clearstream by the date falling two Business Days after the Settlement Date then the applicable Bond Instructions will be automatically withdrawn, whereupon the binding obligation of the Republic to pay the Clearing Price and the obligation of any applicable Holder to sell such Bonds shall be cancelled and no other remedies will be available to the Republic or any such Holder.

The Bond Instructions with respect to Bonds tendered pursuant to Offers rejected by the Republic will be withdrawn as promptly as practicable.

Holders will not be obligated by the Republic, the Joint Dealer Managers, the Tender Agent, the Luxembourg Agent or the Information Agent to pay brokerage fees or commissions to any of them in respect of the Invitation. If you hold Bonds through a broker, dealer, commercial bank or financial institution, you should consult with that institution as to whether it will charge any service fees in connection with the Invitation. Holders will not be obligated to pay Ecuadorian transfer taxes on the purchase of Bonds pursuant to the Invitation except as otherwise specified in this document. See "Certain Tax Considerations".

Irrevocability; Withdrawal of Bonds

Each Offer and corresponding Letter of Transmittal will become irrevocable at the Expiration Time. However, any Offer and corresponding Letter of Transmittal may be withdrawn or revised prior to the Expiration Time by written notice from the person or entity signing the Letter of Transmittal, which notice must be delivered to the Tender Agent or, if applicable, the Luxembourg Agent by hand, courier or facsimile at its respective address specified on the back cover of this document. In addition, you should withdraw the Bond Instructions submitted to the applicable clearing system and, if applicable, submit new Bond Instructions that match your revised Offer.

If the Republic terminates the Invitation without accepting any Offers, all Offers, Letters of Transmittal and Bond Instructions shall automatically be deemed to be withdrawn. If the Republic accepts any Offers, any Offers not so accepted, together with the corresponding Letters of Transmittal and Bond Instructions, shall automatically be deemed to be withdrawn.

If the Invitation is extended or amended in one or more jurisdictions after the Expiration Date, Holders who have submitted Offers pursuant to the Invitation will not be able to withdraw or amend their Offers or related Letters of Transmittal; provided that the extension or amendment is not materially prejudicial to the interests of such Holders.

Irregularities

All questions regarding the validity, form and eligibility, including time of receipt, of any Letter of Transmittal, Bond Instructions, Offer or revocation or revision thereof or delivery of Bonds will be determined by the Republic in its sole discretion, which determination will be final and binding. The Republic reserves the absolute right to reject any and all Letters of Transmittal or Bond Instructions not in proper form or for which any corresponding agreement by the Republic to purchase would, in the opinion of the Republic's counsel, be unlawful. The Republic reserves the absolute right to waive any of the conditions of the Invitation or defects in Letters of Transmittal or Bond Instructions with regard to any Bonds. None of the Republic, the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent shall be under any duty to give notice to Holders of any irregularities in Letters of Transmittal, Bond Instructions or Offers, nor shall any of them incur any liability for failure to give such notice.

Extension, Termination or Amendment; Announcement

At any time before the Republic announces the acceptance of Offers by press release issued to the News Services, the Republic may, in its sole discretion, by press release issued to the News Services:

- terminate the Invitation, including with respect to Offers submitted prior to the time of termination;
- extend the Invitation past the originally scheduled Expiration Date; or
- amend the Invitation, from time to time, in any fashion.

If the Republic determines in its sole discretion to accept any Offers submitted pursuant to the Invitation, it will, at or about 2:00 P.M., CET, on the Acceptance Date, announce by press release issued to the News Services:

- the Clearing Price for each Series of Bonds in respect of which it is accepting Offers and the Republic's acceptance of Offers tendered at or below the applicable Clearing Price;
- the face amount of the Bonds not acquired by the Republic (or the person nominated by the Republic) following the acceptance of Offers under the Invitation.

In addition, the Republic will notify the Luxembourg Stock Exchange accordingly.

At any time after the Republic announces the acceptance of Offers by press release issued to the News Services, the Republic may in its sole discretion, by press release issued to the News Services, amend the Invitation in any fashion or extend the Invitation past the original Expiration Date; provided that any such amendment or extension does not adversely affect the interests of Holders who have submitted Offers pursuant to the Invitation. If the Invitation is extended or amended after the Expiration Date, Holders who have submitted Offers pursuant to the Invitation will not be able to withdraw or amend their Offers or related Letters of Transmittal; provided that the extension or amendment is not materially prejudicial to the interests of such Holders.

Holder Representations and Warranties

By submitting an Offer, you represent and warrant to each of the Republic, the Joint Dealer Managers, the Tender Agent, the Luxembourg Agent and the Information Agent that as of the date of the submission of your Offer, you own the Bonds being offered, you have full power and authority to sell, assign and transfer the Bonds being offered, and, if such Bonds are accepted for purchase pursuant to the Invitation, as of the Settlement Date, the

Republic (or the person nominated by the Republic) will acquire good and marketable title to the Bonds submitted for purchase free and clear of all liens, charges, claims, encumbrances, interests, rights of third parties and restrictions of any kind and such Bonds are not be subject to any adverse claim or right.

Methodology

The Clearing Price in relation to any Bonds selected by the Republic will have no necessary relationship to actual value. You should independently analyse the value of the Bonds and make an independent assessment of the terms of the Invitation. None of the Republic, the Joint Dealer Managers, the Tender Agent, the Luxembourg Agent or the Information Agent has expressed any opinion as to whether the terms of the Invitation are fair or makes any recommendation that you offer to sell Bonds or refrain from offering to do so pursuant to the Invitation, and no one has been authorised by the Republic, the Joint Dealer Managers, the Tender Agent, the Luxembourg Agent or the Information Agent to make any such recommendation.

Certain Other Matters

Bonds acquired by the Republic (or a person nominated by the Republic) pursuant to the Invitation may be held by the Republic or such person thereafter. If such a nomination is made, it is the Republic's intention that such person will acquire all rights, including rights in respect of voting currently exercisable by Holders or beneficial owners of the Bonds that are accepted pursuant to the Invitation.

The Republic reserves the right following the expiration or earlier termination of the Invitation to offer to purchase or exchange Bonds, in individually negotiated transactions or otherwise. Any decision to consider any new offer would depend on various factors, but the Republic has no intention to offer more favourable terms to those provided in the Invitation.

The Luxembourg Agent will be able to perform all services (or agency functions) in Luxembourg in connection with the Invitation. Copies of the following documents will be available for inspection during normal business hours at the office of the Luxembourg Agent specified on the back cover of this document:

- the Trust Indenture for the 2012 Bonds;
- the Trust Indenture for the 2030 Bonds; and
- this Noteholder Circular, including the related Letter of Transmittal.

The Invitation is, and any Offer and acceptance by the Republic will be, governed by and interpreted in accordance with the laws of England.

CERTAIN CONSIDERATIONS

You should consider carefully the following factors, as well as all other information in this Noteholder Circular, before deciding to tender the Bonds.

Considerations Relating to Participating in the Invitation

Holders should understand the schedule and terms of the Invitation before tendering any Bonds. In particular, Holders should be aware that the terms of the Invitation allow the Republic to terminate or extend the Invitation, to withdraw or amend the Invitation in one or more jurisdictions and to reject valid tender of Bonds, in each case at the Republic's sole discretion. Holders should also be aware that once they tender Bonds pursuant to the Invitation, after the Expiration Time, they will not be able to withdraw their tender except in certain limited circumstances.

The terms of the Invitation allow the Republic, in its sole discretion to the extent permitted by applicable laws, to extend or terminate the Invitation and not accept any Offers, to withdraw or amend the Invitation in one or more jurisdictions, and to reject valid tenders of Bonds. Accordingly, there can be no assurance that the tender of Bonds pursuant to the Invitation will be completed (in any particular jurisdiction or at all). Even if such tender is consummated, there can be no assurance that it will be completed in accordance with the schedule and terms set out in this Noteholder Circular.

Once Bonds have been tendered pursuant to the Invitation, tendering holders may not withdraw their tenders after the Expiration Time, except in certain limited circumstances described in "Terms of the Invitation — Irrevocability; Withdrawal of Bonds". Holders should be aware that the Republic expects the Invitation to be open for approximately 25 calendar days and that tenders will become irrevocable at the Expiration Time. Tendering holders should also be aware that the Republic expects that the period between the Expiration Time and the Settlement Date will be approximately 14 calendar days. The market price of the Bonds may fluctuate after Holders tender Bonds pursuant to the Invitation. Tendering holders, however, will not be able to effect transfers of any tendered Bonds unless they withdraw their tender prior to the Expiration Time or its tender is revoked. Withdrawals are not permitted after the Expiration Time except in limited circumstances and thus Holders who tender will not be able to benefit from favourable fluctuations in the market price of the Bonds. Further, tendering holders will not receive the 2012 Bonds Clearing Price and/or the 2030 Bonds Clearing Price in exchange for Bonds they tender until the Settlement Date. If completion of the Invitation is delayed, tendering holders may have to wait longer than expected to receive the 2012 Bonds Clearing Price and/or the 2030 Bonds Clearing Price, as the case may be, in respect of their Bonds during which time they will not be able to effect transfers of any tendered Bonds (except in limited circumstances when tenders may be withdrawn and are actually withdrawn). Bonds tendered in the Invitation must be "blocked" (for transfers to third parties pending completion of the Invitation) no later than the Expiration Time (and in practice such blocking is likely to be required at an earlier time given the procedures of the clearing systems and requirements of custodians or other relevant intermediaries).

There may be potential challenges to the Republic's payments in respect of the Invitation.

Creditors may attempt to attach, enjoin or otherwise challenge payments contemplated pursuant to the Invitation. Creditors have, in recent years, used litigation tactics against sovereign debtors that have defaulted on their sovereign bonds to attach or interrupt subsequent payments made by these sovereign debtors and this could extend to the payments contemplated pursuant to the Invitation. There can be no assurance that a creditor will not be able to interfere, through an attachment of assets, injunction, temporary restraining order or otherwise, with payments made in connection with the Invitation (including any payments due from the Republic upon settlement of the Invitation).

The Republic has established certain procedures for tendering holders to make their tenders. Any error committed in these procedures by a clearing system, a direct participant or a custodian, may result in the failure of a holder to tender or withdraw its Bonds or a delay in a holder's receipt of the 2012 Bonds Clearing Price and/or the 2030 Bonds Clearing Price, as the case may be, for its Bonds.

Any errors in the clearing systems, directs participants in the relevant clearing system and custodians may prejudice a tendering holder's ability to receive the 2012 Bonds Clearing Price and/or the 2030 Bonds Clearing Price, as the case may be, for its Bonds. A duly completed Letter of Transmittal must be received by the Tender Agent and, if applicable, the Luxembourg Agent no later than 6:00 PM CET on the Expiration Date. It is a pre-condition to the valid submission of a Letter of Transmittal that the reference code for blocking instructions for the Bonds being tendered is included. These blocking instructions are only given by Euroclear and Clearstream. Accordingly, after you contact and provide information to your custodian or other intermediary, you will have to rely on this institution and on the relevant direct participant and clearing system, to take the steps necessary for your Letter of Transmittal to be submitted properly and by the applicable deadline. This process may include several intermediaries. It is possible that any person or entity in this chain of tender may commit an error in submitting your tender. Any such error or delay in processing could result in your Letter of Transmittal being improperly submitted, arriving after the relevant deadline, or not at all, or the delivery of your 2012 Bonds Clearing Price and/or the 2030 Bonds Clearing Price, as the case may be, for your Bonds being significantly delayed.

None of the Republic, the Joint Dealer Managers, the Information Agent, the Tender Agent, or the Luxembourg Agent will be responsible for any such errors, or other failure by the clearing systems, direct participants, custodians or other intermediaries to comply with any of those tendering or withdrawal procedures.

You may only tender your Bonds if, prior to the Expiration of the Invitation, you hold them through Euroclear or Clearstream.

The Bonds were originally offered through DTC and through Euroclear and Clearstream. Nonetheless, in order to tender your Bonds, you must hold your Bonds through Euroclear or Clearstream or one of their participants. If you hold Bonds through DTC, you must transfer those Bonds to an account through Euroclear or Clearstream prior to the Expiration Time in order to tender your Bonds or have DTC as a direct participant in Euroclear or Clearstream tender your Bonds. See "Terms of the Invitation—Procedures for Submitting Offers". You are required to make yourself aware of the applicable procedures and deadlines with respect to DTC, Euroclear and Clearstream, as well as any brokers or other financial institutions where your interest in the Bonds are held, as applicable.

Considerations Relating to not Participating in the Invitation

Bonds that are not tendered or not accepted may remain in default indefinitely.

The 2012 and 2030 Bonds that are not tendered or accepted for purchase will remain outstanding. The Republic has no intention of resuming payments on these Bonds following the Expiration Date. Consequently, if you elect not to tender your Bonds (or you elect to specify a Competitive Offer and your Offer is not accepted) there can be no assurance that you will receive any future payments in respect of such Bonds.

The market for, and the price of, the Bonds may be adversely affected by the consummation of the Invitation.

Depending on, among other things, the amount of Bonds outstanding after the consummation of the Invitation, the Bonds may become less liquid and the volatility of the price of the Bonds may increase. After the consummation of the Invitation, the Bonds may trade at a discount compared to present trading prices depending on prevailing interest rates, the market for securities with similar credit features, the economic performance of the Republic and other factors. The Republic cannot assure you that after the consummation of the Invitation an active market in the Bonds will exist or give you any assurance as to the price or prices at which the Bonds may trade in the future.

The repurchase of Bonds by the Republic may adversely affect the price of the Bonds.

At any time and from time to time after the Expiration Date or earlier termination of the Invitation, the Republic, Ecuadorian governmental agencies or others acting on the Republic's or their behalf may acquire Bonds, to the extent permitted by applicable law, through open market purchases or otherwise. There can be no assurances as to whether the Republic, Ecuadorian governmental agencies or others acting on its or their behalf may choose to

pursue any such alternatives in the future. Also, there can be no assurance as to how any such purchases may affect the price of the Bonds.

There is potential for future amendments to the Bonds which remain outstanding.

Bonds acquired by the Republic (or a person nominated by the Republic) pursuant to the Invitation may be held by the Republic or the nominee. If a nomination is made, it is the Republic's intention that the nominee will acquire all rights, including, if the Republic does not control the nominee, rights in respect of voting currently exercisable by Holders or beneficial owners of the Bonds that are accepted pursuant to the Invitation. The Republic will then consider a range of amendments to the Bonds, which it will propose to Holders after the Settlement Date. Certain amendments to the Bonds may be made by the Republic and Holders of a simple majority by value of the Bonds.

Considerations Relating to the Republic

The enforcement of civil liabilities against the Republic may be difficult.

The Republic is a sovereign state. Consequently, it may be difficult for investors to obtain or realise in the United States or elsewhere upon judgments against the Republic. For example, Argentina defaulted on part of its external debt beginning in 2002. Holders of Argentinean bonds have had difficulty in attaining compensation from the defaulted issuer, and many have yet to receive compensation. In the event Holders of the Bonds were to attempt to enforce a civil judgment against the Republic, they may experience similar difficulty.

The Bonds are governed by New York law, and pursuant to the terms of the Bonds and the indentures, the Republic has submitted to the jurisdiction of the federal and state courts in the State of New York. Nevertheless, the new Constitution which was approved in 2008, requires that due care is taken that public debt does not affect national sovereignty. For a discussion of the Constitution, see "Republic of Ecuador—The new Constitution". To the extent submission to New York federal and state courts was seen to affect the Republic's national sovereignty, the Republic may view the submission provision to conflict with the articles of the Constitution. In addition, to the extent Holders were to bring suit in the Republic or attempt to enforce a foreign judgment in the Republic, under the laws of the Republic the property and revenues of the Republic are exempt from attachment or other form of execution before or after judgment.

In addition, pursuant to the terms of the Bonds and the indentures, the Republic has in the past waived its sovereign immunity (other than with respect to the laws of the Republic) with respect to actions brought against it under the Bonds or the indentures. Nevertheless, given the limitations of the U.S. Sovereign Immunities Act of 1976, as well as the immunity granted to the Republic under Ecuadorian law, holders seeking to attach assets of the Republic may not be able to do so within the Republic and may face difficulties doing so outside of the Republic.

A number of factors have impacted on and may continue to impact on revenues and the performance of the economy.

The economy of the Republic is highly dependent on petroleum revenues. Between 2004 and 2007, petroleum and petrochemicals accounted for approximately 50.8% of the Republic's total export revenues. During the same period, the petroleum and petrochemicals sector accounted for an average of approximately 30.7% of the Republic's GDP. Oil prices (measured by the West Texas Intermediate Crude barrel) reached a high of U.S.\$133.93 in 2008 and a low of U.S.\$47.98 in March 2009.

The volatility in the international price of petroleum has affected the revenues that the Republic derives from its petroleum exports. At current levels, the Republic's oil revenues will be significantly lower than the revenues earned in 2008 when the price of oil averaged U.S.\$80.04 per barrel. In the event the price of oil remains in its current trading range, or decreases, the Republic's revenues from oil will continue to be far lower than in prior years. In addition, there can be no assurance that Government revenues from petroleum exports will not continue to experience significant fluctuations as a result of changes in the international petroleum market. Concerns with respect to the current global recession, weakness of the world economy, terrorism, market volatility and certain geopolitical developments, such as ramifications from the ongoing war in Iraq and political instability in the Middle

East, may have a potentially adverse affect on the petroleum market as a whole. For example, the Organisation of Petroleum Exporting Countries (also known as OPEC) has asked its members (including the Republic) to curtail production in light of the global economic situation. Any sustained period of current oil prices or a further decline in international petroleum prices, especially if exacerbated by a decline in production, could adversely affect the Government's fiscal accounts and international reserves.

In addition to the effects of the volatility of the oil market, Congress has passed several laws that have increased the Government's budget, altered the established budgetary agenda and resulted in higher deficits. On April 26, 2009 there will be general elections and a new National Assembly will be formed. The legislators will face the challenge of forming a new legal and institutional framework pursuant to the new Constitution. The ensuing legislation will likely have an impact on public finance and on the Government's budget.

Many of the laws which have been passed by Congress to increase social spending have wide public appeal. Furthermore, President Correa has stated, in light of the global economic climate, that the Republic's priority will be to meet the Government's employment and social goals. The Republic may need to balance its social and employment goals with its budgetary constraints. Furthermore, as part of its strategy to confront the current global economic crisis, and especially in view of its difficulties related to the balance of payments, the Republic implemented a tariff for a period of one year in relation to 630 products, primarily consumer goods. The utilisation of these tariffs, which the Republic believes is a legitimate response given its economic circumstances, could incentivise its commercial partners to impose similar measures in response, which could impact the Republic's economy and therefore its revenues. These factors may make it challenging for the Republic to generate, through taxes, borrowing and other revenues, sufficient funds to meet its spending obligations.

The Republic is involved in a number of legal proceedings and disputes that could result in losses to the Republic as well as a decrease in foreign investment.

The Republic is currently involved in several legal proceedings, mainly related to contracts in the oil and electric sectors. For a description of these legal proceedings and other proceedings against the Republic, see "Republic of Ecuador—Legal Proceedings." If the foreign companies were to succeed, the awards could adversely impact the finances of the Republic. The Republic can offer no assurances as to whether or not such proceedings will be resolved in its favour.

The Republic has been involved in various disputes with the Occidental Exploration and Production Company ("Occidental") in connection with alleged breaches by Occidental of a participation contract entered into between Occidental and Petroecuador in May 1999 for the exploration and exploitation of hydrocarbons in the Oriente region. The Republic terminated its contract with Occidental in May 2006. As a result, Occidental began arbitration proceedings against the Republic with the World Bank's International Centre for Settlement of Investment Disputes ("ICSID") alleging its property was illegally confiscated and seeking U.S.\$1 billion in damages (subsequently increased to U.S.\$3.2 billion). The Republic challenged the jurisdiction of ICSID. President Correa announced in November 2007 that he did not recognise the jurisdiction of the World Bank's international arbitration panel. The Republic will continue its defence but will ultimately not recognise the Panel's jurisdiction. For more information on this claim, see "Republic of Ecuador—Legal Proceedings—Occidental—Breach of Contract Claim".

In April 2006, the Congress approved law 42-2006 which created the at-least 50% windfall profits tax. Subsequently, in October 2007, President Correa's administration, with the approval of Congress, increased the participation of the Republic with respect to oil profits from 50% to 99%. In connection with tax reform legislation, the Republic reduced this windfall tax rate to 70% for those companies which entered into new agreements prior to entering into longer term negotiated service contracts at the end of the year.

In response to the increase in the windfall tax, many private oil companies have instituted arbitration proceedings against the Republic. Some of these claims have settled in the past few years, and others have been withdrawn in return for new service contracts with the Republic. For more information on the renegotiation of the contracts, see "Republic of Ecuador—The Ecuadorian Economy—Principal Sectors of the Economy—Mining (Petroleum and Petrochemicals)—Exploitation". The increase in the windfall tax and the change to service contracts with foreign oil companies could materially adversely affect foreign investment in the petroleum sector.

The Republic faces challenges in its ability to access financing.

The Republic may have to rely in part on additional financing from the domestic and international capital markets in order to meet its future debt service obligations. Given the history of defaults, and more recently, selective defaults, the Republic may not be able access the international markets on favourable terms.

The Republic instituted a Dollarisation Programme in 2000, replacing the Ecuadorian sucre with the U.S. dollar. Due to the current market conditions, the Republic may be at risk if it cannot export sufficient amounts to receive additional dollars, as it has no ability to mint currency. The total of its exports and remittances need to outweigh the total of its imports. The disruptions currently experienced in the financial markets have led to reduced liquidity and increased credit risk premiums for certain market participants and have resulted in a reduction in available financing. Furthermore, by law the Republic's oil revenues can only be used to finance infrastructure projects.

The Republic's financial regulation, the banking insurance system, formerly regulated by *Agencia de Garantía de Depósitos* ("AGD"), is in transition. As of January 1, 2009, the *Corporación del Seguro de Depósitos* ("COSEDE"), pursuant to the Law of Creation of Financial Safety Net, will oversee the deposit insurance scheme, which is funded by the banks based on a percentage of total amounts deposited. AGD continues to liquidate the assets of the fourteen banks that failed as a result of the economic downturn that began in 1999; however, it is unclear which entity will have responsibility for any future bank failures. There is no indication whether or not, or when, this situation will be resolved.

REPUBLIC OF ECUADOR

Area and Population

The Republic is located on the north-western coast of South America and covers an area of approximately 99,054 square miles (256,549 square kilometres). The Republic borders Peru to the south and east, Colombia to the north and the Pacific Ocean to the west.

The Republic includes various geographic areas, including the Pacific coastal plains, the Sierra (consisting of the Andean highland region), the Oriente (characterised by the Amazonian tropical rain forest) and the Galapagos island region located in the Pacific approximately 600 miles from the coast. The Republic is traversed by the equator and lies entirely in the north and south tropical zones. The country's regional climates vary depending on altitude. The climate is tropical in the Pacific coastal plains and Oriente, predominantly temperate in the Sierra and maritime in the Galapagos.

According to the 2001 census conducted by the National Institute of Statistics, the Republic's population is approximately 12 million. Approximately 49.8% of the population lives in the Pacific coastal plains, 44.9% in the Sierra, 4.5% in the Oriente, 0.2% in the Galapagos and 0.6% in undelineated areas. From 1990 to 2001, the Republic's population grew at an average annual rate of approximately 2.05%. Estimates indicate that the Republic's population grew at an approximate average annual rate of 1.4% between 2001 and 2004. Approximately 61% of the Republic's population is urban. Guayaquil, which is located on the coast, is the largest city, with a population of approximately 2.4 million. Quito, the Republic's capital and second-largest city, with a population of approximately 1.8 million, is located in the Andean highland region on a plateau 9,350 feet above sea level. Cuenca, which is also in the highlands, is the third-largest city, with a population of 414,632. Spanish is the official language of the Republic. Kichwa and Shuar, two indigenous languages, are also considered official languages for intercultural relations.

Historically, the Republic has been a Catholic country. The new Constitution guarantees secular values as the underlying basis for civic affairs and the legal system. Whilst the Republic remains predominantly Catholic, recently evangelical Christianity has become more popular.

Under the new Constitution the Republic is a single multicultural and pluralistic society. Approximately 6.8% of the Republic's population identifies itself as indigenous. The indigenous population, together with other ethnic groups such as the afro-ecuadorians and montubios, have been marginalised from Ecuadorian society for decades. Under the new Constitution, the rights of these groups are recognised.

According to the Economic Commission for Latin America and the Caribbean (*Comisión Económica para América Latina y el Caribe*), or CEPAL, one of the five regional commissions of the United Nations, poverty and inequality remain two of Ecuador's main development challenges. The following table sets forth certain comparative information for the Republic relative to certain other countries based on data from the United Nations.

Selected Comparative Statistics

	Ecuador	Colombia	Bolivia	Peru	Venezuela
Per capita GDP ⁽¹⁾	U.S.\$4,341	U.S.\$7,304 ⁽²⁾	U.S.\$2,819	U.S.\$6,039	U.S.\$6,632
Life expectancy at birth (in years) ⁽¹⁾	74.7	72.3	64.7	70.7	73.2
Adult literacy rate (% of total population) ⁽³⁾	91.0%	92.8%	86.7%	87.9%	93%
Infant mortality rate (per 1,000 live births) ⁽⁴⁾	N/A	32/14	72/27	46/6	N/A
% of population below the poverty line ⁽⁵⁾	46.0%	64.0%	62.7%	53.1%	31.3 ⁽⁶⁾
Gini index ⁽⁷⁾	53.6	58.6	60.1	52.0	48.2

(1) Data are from 2005.

(2) These data are from World Bank estimates based on regression.

(3) These data refer to national literacy estimates from censuses or surveys conducted between 1995 and 2005.

(4) The first amount represents the poorest quintile of the population and the second amount represents the wealthiest quintile of the population. According to World Bank statistics, overall infant mortality for Ecuador was similar to that of Peru.

(5) These data refer to the most recent year available between 1990 and 2004.

(6) These data may refer to a year or period other than that specified, may differ from the standard definitions and/or may derive from only part of the country.

(7) The Gini index measures the extent to which the distribution of income (or consumption) among individuals or households within a country deviates from a perfectly equal distribution. A value of 0 represents absolute equality, a value of 100 absolute inequality.

Source: The human development indicator tables, compiled by the United Nations, provide a global assessment of country achievements in different areas of human development. Most of the data in the tables are for 2005.

Constitution, Government and Political Parties

The new Constitution

The Republic adopted a new Constitution following a national referendum on September 28, 2008. A large percentage of our population approved our new Constitution.

The new Constitution seeks to significantly change many facets of the Republic by creating a more just, diverse, democratic, pacifist society that respects the environment.

Social Welfare

The Constitution includes many progressive elements with respect to our social welfare system, including:

- free universal health care;
- free secondary education;
- equal rights for same-sex relationships;
- women's reproductive rights;
- right to quality housing;
- social security and food security;
- establishment of a sustainable economic system, including the distribution of wealth and the means of production; and
- redistribution of large landholdings.

Multiculturalism and Pacifism

The Constitution defines its goals in terms of multiculturalism, pacifism and relations with our neighbours, including:

- elevating certain indigenous languages, Kichwa and Shuar, to official languages for intercultural relations;
- defining the Republic as a pacifist state opposed to weapons of mass destruction and foreign military bases (the United States currently has a military base in the Republic);
- seeking further integration within Latin America; and
- achieving *Sumak Kawsay*, a life in harmony with nature.

The Environment

We believe our Constitution has gone further than those of other countries in expressing our respect for the environment, including:

- protecting the environment, which is significant given the importance of petroleum and mining to our economy;
- granting legal rights for nature to persist, maintain and regenerate its vital cycles by making it a duty of citizens to protect the environment and a duty of the Government to prosecute those that harm it; and
- protecting ecosystems and species from extinction.

Economic Sector

Our Constitution also provides for how we pursue our economic goals, including:

- strengthening Government control over the oil, mining, electricity, drinking water, telecommunications and agricultural sectors; and
- prohibiting a press monopoly.

The Constitution also limits the autonomy of the Central Bank and grants increased authority to the executive branch. It provides for the re-election of the President for a second four-year term. The Constitution requires a debt and finance committee (*Comité de Deuda y Financiamiento*) to approve all debt issuances by the Republic. Many of the laws to implement the terms of the new Constitution have not been enacted and the Republic expects that they will be enacted in the months following the presidential and congressional elections due to take place on April 26, 2009.

Executive

The President is the chief executive and is elected by direct popular vote to a four-year term with the option of re-election for an additional four-year term. The current president, Rafael Correa, had been acting as Minister of Finance and became President on January 15, 2007 after defeating the wealthy businessman Alvaro Noboa Ponton in the 2006 presidential elections. Pursuant to the new Constitution, President Correa will remain as president if he wins the April 2009 election. Under the Constitution, which expanded the Presidency to up to two consecutive four-year terms from one four-year term, President Correa may serve two additional full terms because he was elected to his first term in 2006, prior to the current constitution. He is a candidate in the presidential elections scheduled for April 26, 2009. The President's duties include the enforcement of the Constitution, the determination of foreign and economic policy and the maintenance of domestic order. The President is also the Commander-in-Chief of the Republic's armed forces, and appoints and leads the Council of Ministers.

In the past, the Republic has been a politically fragile country. There have been eight presidents in the Republic during the last ten years, three of whom were deposed by large popular movements with military support which gained the recognition of Congress. The current trend indicates improved political stability.

President Correa's administration has thus far seen coordination between the various branches of Government. The executive and legislative branch worked together prior to the enactment of the new Constitution and have been working together to implement laws that will give effect to the new Constitution.

President Correa's administration has undertaken a number of significant changes in the political and economic systems of the country.

The administration seeks to reform the role of our political, social and economic systems by:

- moving from an unregulated economy influenced by corporate interests to one that responds to the interests of the Republic's citizens;
- focusing on social goals, particularly in the areas of health and education;
- increasing the transparency of government through disclosure of information, including budget related information, and through an open bidding process for the purchase of Ecuadorian goods and services;
- increasing the involvement of citizens in government by reforming and adding a new branch of government to the executive, judicial, electoral and legislative branches — the *Consejo de Participación Ciudadana y Control Social* (Citizens Participation and Social Control Committee);
- increasing public investment and strengthening sovereignty by resolving the issues related to the 2012 Bonds and the 2030 Bonds; and
- reorganising Government services by grouping all of its functions under the following committees:
 - economic policy
 - production
 - internal and external security
 - social development
 - cultural and natural patrimony
 - policy
 - strategic economic sectors, such as oil, mining and fishing.

Legislative System

Until ratification of the new Constitution, the legislative branch consisted of a single-chamber Congress. It was composed of 100 members, all of whom were elected to represent the provinces. The number of representatives for each province was determined on the basis of population. Prior to the enactment of the new Constitution, President Correa convened a special Constitutional Assembly to draft the new Constitution. Five days after the approval of the Constitution, a 76-member interim Legislative and Fiscal Commission was created from the Constitutional Assembly to enact laws in the period prior to the formation of the National Assembly following the April 2009 parliamentary elections.

The following table shows the current composition of the Legislative and Fiscal Commission. The Acuerdo País, led by President Correa, currently holds a majority in the Legislative and Fiscal Commission.

Party	Number of Representatives
Acuerdo País	47
Independientes.....	2
Futuro ya.....	1
Pre-Acuerdo País.....	1
Movimiento Poder Ciudadano	1
Movimiento Popular Democrático.....	2
Pachakutik	2
Partido Social Cristiano.....	3
Partido Renovador Independiente Acción Nacional (P.R.I.A.N.).....	4
Movimiento Red Ética y Democracia (RED).....	2
Sociedad Patriótica.....	8
Una Nueva Opción.....	1
Izquierda Democrática	1
Movimiento Honradez Nacional.....	1
Total.....	<u>76</u>

Source: Ministry of Finance 2008.

The interim Legislative and Fiscal Commission will be replaced by a new unicameral national assembly after the April 2009 parliamentary elections. Pursuant to the Constitution, there will be fifteen representatives elected at the national level. In addition, two representatives will be elected by each province for a total of forty-eight provincial representatives. One additional representative can be elected per each 200,000 inhabitants in a province, and a province can elect one additional representative if the total population is above 150,000 but below 200,000 inhabitants.

Judicial System

The judicial system is comprised of administrative, trial and appellate courts and the Supreme Court. On April 16, 2005, before providing his resignation, President Gutiérrez removed all of the members of the Supreme Court by decree. President Palacio, who was appointed by Congress on April 20, 2005, began his administration with an entirely vacant Supreme Court. In May 2005, the Congress and President Palacio agreed on legal protocols to define the requirements for prospective members of the court. In addition to Constitutional requirements regarding legal education, professional experience and personal information, applicants were required to submit applications and participate in legal and psychological examinations. The candidates were ranked based on their results. The independent *Comité de Calificación, Designación y Posesión de Magistrados y Conjuces de la Corte Suprema de Justicia* (the “Qualifying and Appointing Committee for the Supreme Court Judges”) reviewed the prospective candidates and selected the top ten candidates. The remaining twenty-one positions were chosen by drawing names from the remaining pool of candidates. On November 28, 2005, the Committee named twenty-nine men and two women to the Supreme Court. The new justices were sworn in on November 30, 2005.

In accordance with Article 178 of the Constitution, the judicial system consists of the National Supreme Court (*Corte Nacional de Justicia*), the State Supreme Courts (*Cortes Provinciales de Justicia*) and the first instance courts (*Tribunales y Juzgados de Justicia*). Pursuant to the Constitution, the Supreme Court has 21 justices, who were appointed by the *Consejo de la Judicatura* (the “Judiciary Council”), as a result of a lottery among the prior 31 justices. The new justices were sworn in on October 28, 2008. In addition, our judicial system includes a judiciary council, which regulates, administers and audits the judicial branch of the Ecuadorian Government. The supreme judicial power is vested in the Supreme Court. In the new Supreme Court each justice holds one, unrenovable term of nine years.

The Public Defence Office (*Defensoria Pública*) and the Attorney General of the Republic (*Fiscalía General del Estado*) are independent entities within the judicial branch.

In addition, our indigenous communities may exercise judicial authority in accordance with their traditions and following their own set of rules. The exercise of this authority must comply and may not conflict with the Constitution as well as any international treaty entered into by the Republic with respect to human rights.

Electoral Authorities

In accordance with the Constitution, the National Electoral Council (*Consejo Nacional Electoral*) and the Electoral Contentious Courts (*Tribunal Contencioso Electoral*) are our electoral authorities. The council and courts are independent and autonomous.

Citizens Committee

The Constitution provides for the Transparency and Social Control branch of Government. This is known as the Citizens Committee and was created with the objective of establishing a more participative and transparent democracy, with the participation of its citizens at all levels of government. This participation is achieved through public hearings, assemblies, councils, the use of observers and other means. Further, the Constitution requires local government to have public sessions, with a chair left available for the participation of a representative of the citizens.

Economic Reforms

The Government is seeking to reform certain aspects of the Ecuadorian economy. Certain reform measures are being undertaken as legislative proposals which will require Congressional approval. Other reforms may be undertaken by the Executive branch and do not require Congressional review of approval. There can be no assurance that the reforms presented below will be implemented, and that if they are implemented, that they will achieve their stated goals.

Federal Budget Reforms

In April 3, 2008 Congress passed a law incorporating oil income into the federal budget and restructuring its use to finance investment projects. The law also provides certain rules with respect to public debt and the Debt and Finance Committee (*Comité de Deuda y Financiamiento*) which was created in accordance with Article 289 of the Constitution.

Tax Reforms

In December 2007 Congress passed two laws to combat tax evasion, improve the distribution of the tax burden and include new regulatory taxes. Through these measures, we seek to increase the distribution of wealth, simplify the payment of taxes and improve tax collection.

Electric Sector Reforms

As of June 2008, the state-owned electric distribution companies owed approximately U.S.\$1.3 billion to the electricity generation companies. In addition, the state-owned and private electricity generation companies owed approximately U.S.\$522 million to Petrocomercial, a state owned distribution company, for fuel purchases. Due to the fact that the Ministry of Finance and the distribution companies had some receivables that were used to set-off the electric sector debt, Congress authorised the set-off and the reduction of the public sector debt. Currently, the distribution companies owe U.S.\$73 million to the private electricity generation companies.

Restructuring of State-owned entities

We are seeking to improve Petroecuador's efficiency by restructuring certain technical and administrative operations in order to increase Petroecuador's levels of production and have taken advice from outside consultants. In addition, we plan to restructure comprehensively the Central Bank's operations to improve its administration of financial resources in the public sector and technical support for its economic decisions.

Bank Supervision

In December 2008, the interim Legislative and Fiscal Commission passed the *Ley de Red de Seguridad Financiera* (“Law of Creation of Financial Safety Net”), creating a four-tier regulatory framework for the Republic’s banking sector. Since its creation in 1998, the Agencia de Garantía de Depósitos, known as the AGD, was responsible for insuring the accounts of depositors in the Republic’s banking system. The AGD had a dual role: (i) to oversee the amounts the Government deposited with the Central Bank to protect depositors; and (ii) to help restructure banks in liquidation. As of January 1, 2009, a separate entity, the *Corporación del Seguro de Depósitos* (“COSEDE”), will oversee the deposit insurance scheme, which is funded by the banks based on a percentage of total amounts deposited. The AGD continues to liquidate the assets of the fourteen banks that failed as a result of the economic downturn that began in 1999; however, it is unclear which entity will have responsibility for any future bank failures. For a discussion of the new deposit insurance scheme and the AGD’s resolution of bank liquidations, see “Republic of Ecuador—The Financial System—Structure of the Financial System—The Agencia de Garantía de Depósitos” and “Republic of Ecuador—The Financial System—Structure of the Financial System — AGD Intervention in Financial Institutions”, respectively.

Oil Revenues

During 2008, the Law to Promote Responsibility, Stabilisation and Fiscal Transparency was amended. *Cuenta Especial Reactivación Productiva y Social, del Desarrollo Científico-Tecnológico y de Estabilización Fiscal* (“CEREPS”) was eliminated due to the enactment of the *Ley Orgánica para la Recuperación del Uso de los Recursos Petroleros del Estado y Racionalización Administrativa de los Procesos de Endeudamiento* (“LOREYTF”) and by the new Constitution. The Republic believes that the new law enhances transparency and flexibility to the budget process by providing enhanced management of state resources and prioritising social investments. The law also eliminated all predetermined use of resources; currently all of the Republic's resources go directly to a single account.

Local Governments

The Republic is divided administratively into twenty-four provinces. Each province is subdivided into municipalities that are further subdivided into parishes. Provinces are governed by a governor designated by the President, while municipalities are governed by mayors who are elected by popular vote. Governors are appointed by and under the authority of the President or the executive branch.

Each of the twenty-four provinces has a popularly-elected provincial council headed by a prefect. A municipal council is responsible for the government of each municipality. All provincial and municipal officials are popularly elected to four-year terms.

International and Regional Relations

The Republic has diplomatic relations with approximately 78 countries and is a member of a number of international organisations, including:

- the United Nations (“UN”), as a founding member, including many of its specialised agencies;
- the Organisation of American States (“OAS”);
- the World Health Organisation (“WHO”);
- the World Trade Organisation (“WTO”);
- the International Labour Organisation (“ILO”);
- the Andean Community;

- the Corporación Andina de Fomento (“CAF”);
- the Latin American Integration Association (“ALADI”);
- the Interamerican Development Bank (“IDB”);
- the Latin American Reserve Fund (“FLAR”); and
- the Organisation of Petroleum Exporting Countries (“OPEC”).

Since President Correa was elected in 2007, the Republic has changed the focus of its public sector debt. This has led to a focus on the Republic’s relationships with IDB, CAF and FLAR, two of which are located in Latin America. As the Republic has strengthened its relationship with Latin American-based multilateral entities, it no longer looks to borrow from the World Bank and IMF, the latter of which no longer has a representative based in the Republic. The primary objective of this new focus is to reduce our dependence on institutions such as the World Bank and the IMF. The Republic has also shifted its bilateral relationships, strengthening its economic ties with Canada, China, Iran and Venezuela among others. Concurrently, the Republic has renewed its bilateral economic involvement with the European Union and Colombia. Under the new Constitution, priority has been given to relations with Andean countries, Caribbean countries and Latin American countries generally.

In addition, there are trade arrangements between the Republic and various nations. See “Republic of Ecuador—Public Sector Debt—Multilateral Support (2004-2008)”.

The Republic became a member of OPEC in November 1973. In November 1992, the Republic resigned its membership and opted for observer status in OPEC. In October 2008, the Republic again became a full member of OPEC.

The Republic maintains close ties with most of its neighbouring countries and participates in several regional arrangements to promote trade, investment and services. As a member of ALADI, a regional external trade association, the Republic and the other signatories (Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Mexico, Paraguay, Peru, Uruguay and Venezuela) have worked to remove regional trade restrictions.

The members of the Andean Community (including, the Republic, Bolivia, Colombia, Peru and Venezuela) have worked to reduce or eliminate tariff barriers to trade. In 1992 and 1993, the Republic entered into bilateral trade agreements with Colombia, Venezuela and Bolivia. Under these agreements, these countries have agreed to levy uniform tariffs on goods from third parties.

In 1994, the Republic entered into a bilateral trade agreement with Chile liberalising trade between the two countries. In 1996, the Republic became a member of the WTO and became subject to the WTO’s rules on free trade.

On October 26, 1998, the Republic and Peru signed a peace agreement. This agreement settled a long-standing territorial dispute which had resulted in hostilities, most recently in January 1995, over territory located in the Oriente region. As a result of this treaty, the two countries have presented joint plans for the development of infrastructure and commerce in the border region.

On April 5, 2004, the Republic (as part of the Andean Community) concluded a free trade agreement with Mercosur. Mercosur is a customs union comprised of Argentina, Brazil, Paraguay, Uruguay, Chile and Bolivia which seeks to (i) create a full common market in goods, services and factors of production by eliminating or significantly reducing, in some cases over a period of years, import duties, tariffs and other barriers to trade among members, and (ii) apply external tariffs for trade with non-members. The Andean Community’s adherence to the agreement, which was originally agreed to in principle at a summit in July 2003, resulted in the creation of a South American free trade area.

The Republic is currently a beneficiary of certain preferential tariff benefits provided by the U.S. Government under the Andean Trade Promotion and Drug Eradication Act (the “ATP-DEA”). In exchange for its efforts to combat narcotrafficking in the Republic, certain Ecuadorian products, such as textiles and tuna, receive preferential tariff treatment from the United States Government. The Republic’s preferential status under ATP-DEA was extended through 2009. This preferential status continues to help the Republic’s trading activities with the United States.

On March 1, 2008, Colombian forces raided a camp of the Revolutionary Armed Forces of Colombia (“FARC”) that was based in Ecuadorian territory. This led to the death of FARC’s top rebel leader, Raúl Reyes. The Republic is focused on the need to establish stronger border control along its border with Colombia. Ecuador shares approximately 373 miles of bordering territory with Colombia and 950 miles with Peru. The Republic has recently ordered five military helicopters from India to help patrol its borders with Colombia and Peru. Any further militarisation by the Republic or its neighbours could exacerbate tensions and skirmishes.

In January 2009, the Republic, in reliance on its interpretation of the General Agreement on Tariffs and Trade, or GATT, imposed certain tariffs in order to protect its balance of payments. Accordingly, the Republic increased the tariffs on 630 products and limited the import of certain consumer goods (for instance, finished goods, luxury goods, and goods similar to locally produced goods). These policies were approved and implemented in February 2009, and currently are being discussed and defended before the Andean Community. The World Trade Organisation, or WTO, will also be considering these policies later this month.

There is a risk that other countries will raise the tariffs on the Republic’s exports in response to its proposed imposition of tariffs, and that these tariffs could lead to economic challenges as well as tensions with the Republic’s neighbours in the Andean Community.

THE ECUADORIAN ECONOMY

Historical Background

The Republic has rich natural resources and historically its agricultural sector and the export of primary products have dominated the Republic's economy. From the 1950s through the 1980s, the Government was extensively involved in the Republic's economy. During this period, the Government expanded long-standing policies with respect to import substitution designed to promote domestic industries and discourage imports. The Government also exerted significant influence over various sectors of the economy through state-owned development banks, exchange and interest rate controls and industry subsidies.

Following the Second World War, the Republic increased its banana exports by cultivating large areas along the coastline. The Government supported the increased infrastructure for the banana industry. As a result of various factors, including lower cost manual labour and diseases plaguing competing Central American banana plantations, we became the largest exporter of bananas to the United States. The Government applied the resulting increase in revenues to, among other things, finance public infrastructure projects and increase government jobs and salaries.

As the Central American banana plantations recovered, falling export prices led to a number of consequences, including a deficit in our balance of payments and rising unemployment. In spite of these difficulties, during the 1960s, the Ecuadorian economy improved as a result of diversification in our manufacturing sector as well as with respect to exports and imports. During this period, we increased our emphasis on meeting domestic demand through increased production of consumer durable goods.

The discovery of new petroleum fields in the Eastern provinces transformed the Republic during the 1970s into a producer of oil and made oil the Republic's most important export commodity. The rise in oil exports in the mid-to-late-1970s fuelled economic growth and brought sharp increases in Government spending and employment, financed principally by external borrowing and oil revenues. Real GDP increased by an average of 9.0% per year between 1971 and 1977. Between 1974 and 1979, the Republic's external debt grew from U.S.\$360 million to approximately U.S.\$1.4 billion. As the economy became increasingly dependent on oil revenues, the Government's participation in the economy also grew.

In the early 1980s, the Ecuadorian economy faltered as the international price of petroleum began to gradually decline, climatic conditions caused by El Niño damaged crops and infrastructure and the Republic lost some foreign markets for its traditional agricultural products. From 1982 to 1987, the Republic experienced a slowdown in economic growth, characterised by declining investment rates and increasing inflation, with Real GDP growth averaging 0.9% annually and GDP per capita decreasing at an average annual rate of 0.9%. Stabilisation plans implemented during this period did not succeed in avoiding a slowdown in economic growth. The collapse of world oil prices in 1986 reduced the Republic's oil export revenues by 50%.

In March 1987, an earthquake destroyed a large stretch of the SOTE pipeline, which was the Republic's only oil pipeline, together with pumping stations, resulting in an approximate six-month suspension in petroleum production. Confronted with the sudden interruption in the flow of oil revenues and with growing current account and public sector deficits, the Republic suspended debt service payments to most private creditors (but not to multilateral financial institutions) in early 1987 and adopted measures to limit imports. GDP declined by 6.3% in 1987.

The period from 1988 to 1992 was characterised by increasing oil export prices and reductions in Government spending in real terms. The Ecuadorian economy recovered, growing 10.9% in 1988, 0.3% in 1989, 1.1% in 1990 and 4.3% in 1991. Throughout this period, the Government pursued a gradual stabilisation policy. Despite the Government's policies and intervals of relatively strong economic growth, inflation rose sharply, averaging 57.1% annually during the period from 1988 to 1992 and reaching an annual rate of 60.2% in 1992.

During the presidency of Sixto Durán Ballén (1992-1996), the Government adopted a programme of economic reforms and introduced measures to reduce the public deficit, control inflation, strengthen the balance of payments and create conditions for sustained growth. Under this economic reform programme, inflation decreased

from an annual rate of 60.2% in 1992 to 22.8% in 1995. International reserves at the Central Bank increased from U.S.\$780 million as of December 31, 1992 to U.S.\$1.56 billion as of December 31, 1995. The consolidated non-financial public sector deficit decreased from 1.1% of GDP in 1992 to 1.3% of GDP in 1995. GDP also grew during this period, increasing by 1.9% in 1993, 4.7% in 1994 and 1.7% in 1995.

Following his election to the Presidency in 1996, President Abdalá Jaime Bucaram announced an economic programme requiring the approval of a series of tax increases and other measures by Congress. This economic programme, which included drastic reductions in electricity and natural gas subsidies, was not well received by Congress or by the public. Growing popular and congressional discontent, as well as allegations of widespread corruption within the Bucaram administration, ultimately led to the replacement of President Bucaram by congressional representative Fabian Alarcon in February 1997.

Upon taking office, President Alarcon began to implement an economic programme to reduce the fiscal deficit by increasing tax and debt collections and fixing profit margins for petroleum distributors. Despite these measures, the non-financial public sector deficit increased to 2.1% of GDP in 1997 as a result of a decrease in fiscal revenues resulting from significant damage caused by El Niño, the decision not to eliminate costly state subsidies as well as Congress' refusal to increase the value-added tax.

In 1998, President Jorge Jamil Mahuad's administration inherited fiscal and economic systems seriously weakened by the inability of the former administrations to establish and implement effective economic programmes. Upon taking office, President Mahuad presented an economic programme aimed at controlling inflation and reducing the fiscal deficit but the programme did not have a significant impact. During 1998, however, the Republic was confronted by additional economic challenges due to the overall reduction in capital inflows to emerging markets resulting from the devaluation of the Russian ruble and its effects on the international capital markets. Moreover, a significant decrease in petroleum prices, the effects of El Niño on the agricultural and fishing sub-sectors and the over-valuation of the sucre relative to the Republic's competing markets further reduced revenues to the Republic. As a result, average inflation increased to 36.1% in 1998 from 30.6% in 1997 and the fiscal deficit increased to 5.2% of GDP in 1998 from 2.1% of GDP in 1997.

The 1999 Economic Crises and Subsequent Reforms

In 1999, in response to the mounting economic difficulties facing the Republic, President Mahuad's administration took significant measures. Costly subsidies for liquefied petroleum gas, electricity and diesel fuel were slashed and tax reforms were implemented, including the reestablishment of the income tax (subsequent political pressure forced the Government to reinstitute the subsidy for liquefied petroleum gas). Despite these measures and other efforts aimed at controlling inflation and reducing the fiscal deficit, GDP decreased more than 6.3% in 1999, domestic inflation, increased 60.7%, unemployment surged, real wages plummeted, the sucre lost approximately 66% of its value against the U.S. dollar, and both poverty and income distribution worsened.

In February 1999, the Central Bank's decision to eliminate the exchange rate band and refrain from further market intervention to support the exchange rate produced additional difficulties for an already weakened banking system and nearly resulted in hyperinflation. In March 1999, in order to keep financial institutions afloat and in an effort to control inflation, the Government froze virtually all current dollar accounts and approximately half of current sucre accounts in Ecuadorian banks. Throughout 1999, 14 banks were closed or taken over by AGD. This extreme measure had the positive effect of temporarily stabilising the rate of inflation; nonetheless, it generated distortions and negatively impacted the economy and many of the Republic's institutions. Bank scandals and allegations of corruption exacerbated both economic and political instability. As AGD began to administer part of the banking system, many debtors stopped servicing their debts, further weakening the health of banks. The bank recovery plan had a steep fiscal cost: the Government issued U.S.\$1.4 billion in domestic bonds to capitalise or provide liquidity to banks administered by AGD. The Central Bank held these bonds until November 2008, when a reform of the usury law was passed, abolishing the Republic's liability. As a result of this economic crisis, towards the end of 1999 and the beginning of 2000, the Republic defaulted on its internal and external public debt.

Dollarisation Programme

In January 2000, following several weeks of severe exchange-rate depreciation, the Government announced that it would dollarise the economy. On March 1, 2000, the Congress approved the *Ley para la Transformación Económica del Ecuador* (the “Law of Economic Transformation” or “LET”), which made the U.S. dollar legal tender in the Republic. In addition to providing an official basis to dollarise the economy, the LET contained reforms aimed at strengthening fiscal discipline, encouraging flexibility in the labour market, improving banking supervision and establishing rules to encourage direct investment and privatisations.

The Dollarisation Programme imposed serious constraints to the economic policy of the Republic and has caused subsequent challenges to the design implementation of public policies and programmes, as there are few options the Government has to stabilise the economy and promote growth and development.

Authority of the Central Bank within the Dollarisation Programme

Pursuant to the LET and in furtherance of the Dollarisation Programme, the Central Bank developed relationships with the public sector and private financial system by promoting the economic stability of the Republic, contributing to the development of the economy and executing the monetary policy. In order to promote the Dollarisation Programme, the Central Bank administrated the payment system as well as the investment of the freely disposable international reserve. The Central Bank also acted as depository of public funds and as financial and tax agent for the Republic. Despite the new constraints placed on the Central Bank by the Dollarisation Programme, the Central Bank continues to follow some of its traditional microeconomic objectives, including fixing of interest rates; administrating and regulating the system of payments; administrating the reserves of the financial system; monitoring financial risk; and supervising the assets and liabilities of the international reserves. In addition, the Central Bank calculates the Republic’s economic growth, including economic trends by sector and in the aggregate.

To support the Dollarisation Programme, the Republic took a number of related actions, including:

- restructuring and strengthening the banking system by:
 - implementing a comprehensive corporate and household debt restructuring programme, aimed at restoring the cash-flow of enterprises and asset quality of the banking system;
 - redefining capital requirements to conform to standards established by the Basle accords; and
 - conforming loan classification and provisioning rules to international standards;
- enacting the Fiscal Responsibility, Stabilisation and Transparency Law in 2002, which was aimed at reducing public indebtedness and establishing greater transparency in the Government’s use of public funds;
- introducing austerity measures that significantly reduced public sector expenditures between 2003 and 2005;
- rescheduling the external debt owed to private and bilateral creditors; and
- establishing a programme to restore trade lines and interbank lines to Ecuadorian banks.

Pursuant to the new Constitution, the role of the Central Bank has changed in that its autonomy has been eliminated. The executive branch makes decisions concerning monetary policy, and the Central Bank implements and advises in accordance with this policy. In practice, however, the Central Bank’s functions have not changed substantially as a result of the new Constitution.

Gradual Economic Recovery: 2000-2003

The period between 2000 and 2002 was characterised by a gradual economic recovery. GDP expanded at a rate of 2.8% in 2000, 5.3% in 2001 and 4.2% in 2002, and inflation decreased from 91.0% in 2000 to 22.4% in 2001 and 9.4% in 2002. The improvement in the Ecuadorian economy during this period can be attributed to a number of factors, including, the Government's economic and social plan; increased internal demand; an increase in real wages; the assistance of multilateral financial institutions; a decrease in international interest rates; an increase in remittances from Ecuadorians residing and working abroad and the implementation of the Dollarisation Programme. The Ecuadorian economy improved during this period despite the general decline of international oil prices and a small decrease in petroleum production.

The Republic's economy continued to show signs of recovery in 2003. The Republic's improved economic performance in 2003 was primarily the result of a favourable external environment, the construction of the Oleoducto de Crudos Pesados Ecuador, S.A. (the "OCP") heavy crude pipeline that began in June 2001 and the implementation of the Law to Promote Responsibility, Stabilisation and Fiscal Transparency. As a result of these factors, overall GDP increased by 3.6% in 2003. Inflation continued to decline, falling to 6.1% as compared to 9.4% in 2002. The current account deficit declined sharply in 2003 to 1.5% of GDP, reflecting high international oil and commodity prices, a depreciation of the U.S. dollar, and a decrease in imports due to the completion of the construction of the OCP pipeline. High oil prices and restraint by the Government on non-wage spending helped improve fiscal performance in 2003. The primary surplus of the non-financial public sector increased to 4.7% of GDP in 2003. The non-oil primary deficit did not change from 2002, but remained at 1.4% of GDP in 2003. Aided by lending of multilateral financial institutions, the Government was also able to clear external arrears and reduce domestic payments arrears.

Continued Economic Improvement: 2004-2008

The Republic's economy showed continued improvement in 2004 as a result of a 25.3% increase in petroleum production, an increase in international oil prices and the declining value of the U.S. dollar, resulting in the improved competitiveness of Ecuadorian exports. Based on these factors, overall GDP increased 8% in 2004, even as non-oil GDP growth remained relatively unchanged at 3.6%. Inflation continued to decline, falling to 1.9% as compared to 6.1% in 2003. The recovery of the Republic's financial system also began to show signs of acceleration in 2004, as commercial banking deposits increased 25% from U.S.\$4.2 billion as of December 31, 2003 to U.S.\$5.4 billion as of December 31, 2004. During this period, short-term deposits increased by approximately U.S.\$487 million. The average lending interest rate continued to decline, from 11.4% at December 31, 2003 to 7.5% at December 31, 2004.

The first half of 2005 was marked by public unrest and large protests against the Government of President Gutiérrez. Nonetheless, the Republic's economy continued to show signs of stability and growth. The remainder of 2005 brought moderate economic growth and a stable increase in prices. The total growth of the Ecuadorian economy for 2005, in real terms, was approximately 6.0%. The non-financial public sector petroleum revenue in 2005 was greater than in 2004 due to higher prices for petroleum on the international market. Non-petroleum income increased more than 10% as compared to 2004. Average inflation for 2005 was 2.2%.

In July 2005, when President Correa was Minister of Finance, Congress voted to reform the existing *Ley Orgánica de Responsabilidad, Estabilización y Transparencia Fiscal* (the "Law to Promote Responsibility, Stability and Fiscal Transparency") and to use the funds accumulated in the *Fondo de Estabilización, Inversión Social Productiva y Reducción del Endeudamiento Público* ("FEIREP") for investments aimed at accelerating economic development. The FEIREP was transformed into a new special account called the CEREPS. The new law changed the rules under which funds were previously dispensed from the FEIREP and granted the Government greater flexibility to invest funds from the CEREPS to stimulate economic growth. As a result, funds which were previously available in the FEIREP to reduce Government debt were no longer available as they were meant to be allocated for social and technological purposes. Subsequently, CEREPS was eliminated in 2008 and currently all oil revenues are credited to a single account within the treasury.

In 2006, the economy grew at a rate of approximately 3.9% and the average inflation rate was 3.3%. The non-financial public sector showed a surplus. Because of that surplus, the final balance of the external debt was U.S.\$10.2 billion, approximately 24.7% of the GDP.

In 2007, when President Correa took office, the GDP continued to grow at a rate of approximately 2.5%. The balance of the Republic's foreign debt was U.S.\$10.6 billion, which was approximately 23.9% of the GDP and represented a 3.9% increase from 2006. President Correa proposed an economic reform plan that he began to implement in 2007. The plan focused on the distribution of national wealth, energy self sufficiency, social security and food security, among other things. For a description of President Correa's reforms, which included a more balanced relationship between the Government and the market, transparency in the budget process, a finance committee to authorise public debt, the fostering of development and prioritisation of social investment, see "Republic of Ecuador—Constitution, Government and Political Parties—the new Constitution".

The Republic's economy is estimated to have grown at a rate of 5.3%, in real terms, in 2008. The balance of the foreign debt was U.S.\$10.0 billion, which was approximately 19.2% of GDP. As of December 31, 2008, the freely disposable reserves amounted to U.S.\$4.4 billion. The average annual price attributed to Ecuadorian crude oil was U.S.\$61.80 per barrel in 2007 and U.S.\$80.04 per barrel in 2008. During the last months of 2008, the economy showed certain signs of the effects of the global financial crisis, especially the decrease in oil prices. The average rate of inflation in 2008 was 8.8%.

The service and agricultural sectors, as well as the fishing and manufacturing industries, have all grown from 2005 to 2008. In the period of 2005-2008, the Republic's annual GDP was not affected by the global crisis, and in 2007 and 2008 tariffs on imports (mainly raw materials) generally decreased. The GDP for 2009, however, is likely to be affected by the global crisis mainly because the Republic cannot issue additional currency and market oil prices have declined. In response to the crisis, the Republic has increased tariffs on 630 goods in January 2009. For a discussion of the imposition of these tariffs, see "Republic of Ecuador—Constitution, Government and Political Parties—International and Regional Relations".

The Global Economic Crisis

The global economic crisis has had and will likely continue to have a negative impact on the Republic's economy and financial system. Since the fourth quarter of 2008, the Republic has experienced increased unemployment, decreased revenues and lower rates of growth. As it does not have the ability to produce currency, the Republic is more limited than other countries in its options to respond to the current financial crisis. For example, in the event exports do not continue to exceed its imports, the Republic would need to rely on financing by multilaterals, increased tariffs, exchange controls, or similar measures. Remittances from abroad, another source of funds for the Republic's economy, decreased from U.S.\$759 million in the first quarter of 2008 to U.S.\$707 million in the third quarter of 2008. The combination of decreased global prices of its main exports, such as oil and food products, as well as the possible OPEC measures to decrease production of oil and a decrease in remittances from its foreign workers will negatively impact the Republic's economic outlook for 2009 and beyond.

Gross Domestic Product

The Ecuadorian economy experienced positive rates of real GDP growth between 2004 and 2008. In 2004 and 2005, the economy grew by 8.0% and 6.0%, respectively. In 2006 and 2007, the economy continued to grow, achieving growth rates of 3.9% and 2.5%, respectively. We estimate that the rate of economic growth will have increased to 5.3% in 2008 mainly due to an increase in the market price for oil and an increase in public investment. The Republic expects its GDP growth rate to decrease substantially during 2009 due to the decrease in the market price for oil as well as the current global recession.

The following tables set forth information regarding real GDP and expenditures, for the periods indicated.

Real GDP and Expenditures
(in millions of U.S.\$)⁽¹⁾

	For the year ended December 31,				
	2004	2005	2006	2007	2008 ⁽²⁾
Real GDP	32,642	37,187	41,763	45,789	52,572
Imports of goods and services.....	9,651	11,822	13,749	15,669	19,867
Total supply of goods and services	<u>42,294</u>	<u>49,009</u>	<u>55,512</u>	<u>61,458</u>	<u>72,440</u>
Final consumption:					
Government consumption.....	3,716	4,134	4,613	5,196	6,160
Private consumption	21,963	24,550	26,911	29,139	32,789
Total final consumption	<u>25,679</u>	<u>28,684</u>	<u>31,524</u>	<u>34,335</u>	<u>38,950</u>
Gross fixed capital formation	7,045	8,175	9,301	10,129	12,744
Changes in inventory	587	670	475	906	699
Exports of goods and services.....	8,982	11,480	14,213	16,088	20,048
Total final demand.....	<u>42,293</u>	<u>49,009</u>	<u>55,512</u>	<u>61,458</u>	<u>72,439</u>

(1) In constant 2000 dollars.

(2) Preliminary data.

Source: Central Bank.

Real GDP and Expenditure Growth
(% change from previous year)

	For the year ended December 31,				
	2004	2005	2006	2007	2008 ⁽¹⁾
Real GDP	8.0%	6.0%	3.9%	2.5%	5.3%
Imports of goods and services.....	11.0	13.7	9.4	7.3	8.6
Total supply of goods and services.....	8.9	8.2	5.5	4.0	6.4
Total final consumption	4.5	6.9	5.3	3.8	5.3
Government consumption.....	3.6	3.5	3.7	6.1	9.6
Private consumption	4.7	7.3	5.5	3.5	4.7
Gross fixed capital formation.....	4.9	10.9	3.8	2.5	14.2
Exports of goods and services.....	15.6	9.0	8.9	2.2	2.4
Total final demand.....	8.9	8.2	5.5	4.0	6.4

(1) Preliminary data.

Source: Central Bank.

Principal Sectors of the Economy

The following tables set forth information regarding the composition and rates of growth by economic sector of the Republic's real GDP for the periods indicated.

Real GDP by Sector (in thousands of U.S.\$) ⁽¹⁾

	For the year ended December 31,			
	2004	2005	2006	2007
Agriculture, livestock, hunting and forestry	1,989,038	2,153,881	2,415,554	2,664,854
Fishing	229,592	308,930	374,488	362,123
Mining ⁽²⁾	5,338,398	7,475,126	9,406,818	10,671,059
Manufacturing (excluding oil refineries)	2,881,168	3,295,962	3,697,641	4,081,430
Manufacturing of refined petroleum products	(1,357,306)	(2,078,955)	(2,867,058)	(3,190,170)
Electricity and water	578,502	541,106	538,496	610,907
Construction	2,680,057	3,099,723	3,822,000	4,162,006
Wholesale and retail commerce	3,998,987	4,402,323	4,822,321	5,357,175
Transportation, storage and communications	3,647,782	4,137,776	4,354,777	4,541,231
Financial intermediation services	669,603	895,357	1,086,617	1,121,868
Public administration and defence; social security	1,769,323	1,945,857	2,147,631	2,396,406
Private homes with domestic servants	50,181	48,163	53,680	60,804
Indirectly measured financial intermediation services	(705,136)	(783,616)	(1,005,368)	(1,147,967)
Other services ⁽³⁾	6,703,600	8,842,109	9,871,363	10,798,598
Other elements of GDP	3,045,168	2,903,200	3,044,270	3,299,050
Total real GDP	19,572,229	20,747,176	21,553,301	22,090,180

(1) In constant 2000 dollars.

(2) The mining sector includes the petroleum and petrochemicals sub-sector.

(3) Other services include hotels and restaurants, real estate, education, health and social services.

Source: Central Bank.

Real GDP Growth by Sector (% change from previous comparable period)

	For the year ended December 31,			
	2005	2006	2007	2008
Agriculture, livestock, hunting and forestry	5.0%	3.5%	4.4%	3.2%
Fishing	25.5	14.1	2.4	4.7
Mining ⁽¹⁾	1.1	1.0	(4.8)	(2.8)
Manufacturing (excluding oil refineries)	9.2	7.1	4.9	4.7
Manufacturing of refined petroleum products	(3.3)	(10.9)	(2.4)	N/A
Electricity and water	1.3	0.5	15.5	9.2
Construction	7.3	3.8	0.1	17.8
Wholesale and retail commerce	5.2	4.7	3.3	5.5
Transportation, storage and communications	8.9	7.2	5.7	N/A
Financial intermediation services	18.3	20.6	8.0	8.1
Public administration and defence; social security	1.9	2.8	5.9	10.7
Private homes with domestic servants	(4.5)	3.2	0.1	(1.5)
Indirectly measured financial intermediation services	8.8	24.2	11.6	2.4
Other services ⁽²⁾	31.9	11.6	9.4	N/A
Other elements of GDP	7.6	7.0	5.9	7.4
Annual change in Total GDP	6.0%	3.9%	2.5%	5.3%

(1) The mining sector includes the petroleum and petrochemicals sub-sector.

(2) Other services include hotels and restaurants, real estate, education, health and social services.

Source: Central Bank.

Mining (Petroleum and Petrochemicals)

Mining, the process through which the Republic extracts petroleum and other natural resources, constitutes one of the main economic sectors of the Republic. Petroleum is the Republic's most important mineral resource and constitutes the country's largest source of export revenues. Exports of petroleum and petrochemicals accounted for 47.1%, 51.1%, 53.1% and 51.8% of total exports in 2004, 2005, 2006 and 2007, respectively. The mining sector (including petroleum and petrochemicals) represented approximately 25.9%, 24.2%, 28.7%, 24.7% and 40.9% of the non-financial public sector's revenues in 2004, 2005, 2006, 2007 and 2008, respectively. In 2008, petroleum exports reached U.S.\$10.3 billion, accounting for 51.2% of total exports.

The following table sets forth information regarding the mining sector (including petroleum and petrochemicals) for the periods presented.

Petroleum and Petrochemicals (in millions of U.S.\$, except for percentages)

	For the year ended December 31,				
	2004	2005	2006	2007	2008 ⁽³⁾
Total exports.....	8,982.5	11,480.3	14,212.8	16,088.1	20,047.6
Petroleum exports.....	3,898.5	5,396.8	6,934.0	7,428.4	10,568.3
Petrochemical exports.....	335.5	473.0	610.5	900.2	1,104.5
Total of petroleum and petrochemical exports.....	4,234.0	5,869.8	7,544.5	8,328.6	11,672.8
% petroleum and petrochemical exports/total exports.....	47.1%	51.1%	53.1%	51.8%	58.2%
Fuel and lubricant imports.....	1,138.4	1,814.6	2,541.3	2,765.3	3,391.6
Total imports.....	8,226.3	10,286.9	12,113.6	13,893.5	18,685.6
% Fuel and lubricant imports/total imports.....	13.8%	17.6%	21.0%	19.9%	18.2%
Non-financial public sector petroleum revenues.....	2,115	2,212	3,232	3,318	8,899 ⁽¹⁾
Total non-financial public sector revenues.....	8,177	9,014	11,344	13,210	21,743
% Non-financial public sector petroleum revenues/total non-financial public sector revenues.....	25.9%	24.5%	28.5%	25.1%	40.9%
Petroleum GDP ⁽¹⁾	2,785	2,779	2,641	2,375	2,204
Non-petroleum GDP ⁽¹⁾⁽²⁾	14,482	15,320	16,284	16,932	18,071
Total GDP.....	19,572	20,747	21,553	22,090	23,264
% Petroleum GDP / Total GDP.....	14.2%	13.4%	12.3%	10.8%	9.5%
Annual change of petroleum GDP.....	35.0%	(0.2)%	(5.0)%	(10.0)%	(7.2)%
Annual change in non-petroleum GDP.....	3.6%	5.8%	6.3%	4.0%	6.7%
Annual change in total GDP.....	8.0%	6.0%	3.9%	2.5%	5.3%

(1) In constant 2000 dollars.

(2) This includes two changes with respect to previous periods: (i) incorporation of the effects of the Organic Law and (ii) registration of the account for the financing of the importation of by-products.

(3) These data are for the period through November 2008.

Source: Central Bank.

The Republic believes that it has extensive but underdeveloped mineral resources, which include gold, silver, copper, iron, lead, zinc, uranium, magnesium, phosphates, limestone, kaolin, marble and sulphur.

The Republic's oil reserves are currently exploited directly by the state-owned oil company, Petroecuador, and through participation or service contracts with other Ecuadorian or foreign corporations. Oil exploitation operations are conducted under the supervision and regulation of the Ministry of Energy and Mines and Petroleum (*Ministerio de Energía y Minas y Petróleo*) acting through the General Directorate of Hydrocarbons. In 2005, 2006 and 2007, the hydrocarbons industry accounted for 21.5%, 20.9% and 19.4% of GDP, respectively.

Petroecuador's operations are divided among three subsidiaries, each with its own independent budget, accounting and administration. One division, Petroproducción, is responsible for drilling, lifting and well management, while the Oil Pipeline Division is responsible for crude oil transport. Petroindustrial operates the Republic's four refineries and Petrocomercial is responsible for distributing oil derivative products domestically. The International Trade Division is responsible for crude oil exports.

All revenues generated by Petroecuador are administered by the Ministry of Finance. Petroleum revenues are allocated on a periodic basis to the Government and certain agencies and instrumentalities. Prior to such allocation, the Ministry of Finance deducts the production costs of crude oil and its derivatives, as well as the costs of internal and external commercialisation and transportation, and also sets the budget for petroleum related investments.

Reserves

The following table sets forth information regarding the Republic's crude oil and free natural gas reserves as of the dates indicated.

Crude Oil and Natural Gas (crude oil in thousands of barrels; natural gas in billions of square feet)

	As of December 31 ,			
	2004	2005	2006	2007
Crude Oil	4,446,663.6	4,516,954.3	4,185,282.9	4,036,189.3
Production	192,248.0	194,027.0	195,523.0	186,536.0
Ratio Reserves-Production	23.1	23.3	21.4	21.6
Natural Gas (Gulf of Guayaquil)	131.5	159.8	185.2	208.9
Production	8.5	9.2	9.9	10.4
Ratio Reserves-Production	15.4	17.3	18.7	20.0

Sources: Petroecuador, General Directorate of Hydrocarbons and Central Bank.

Reserve classifications and methodologies used by Petroecuador differ in certain important respects from the reserve classifications and methodologies generally used by companies in the United States. Petroecuador reserve estimates focus on technical information and not on the economic feasibility of recovery, while U.S. estimates of reserves depend on assumptions about the price of oil and the cost of production that determine the economic recovery rate achievable at a particular field. U.S. estimates also depend on prices and costs as of the date the estimate is made. In addition, Petroecuador's reserve estimates have not been prepared or reviewed by an independent petroleum-engineering firm. Moreover, there are numerous uncertainties inherent in estimating quantities of crude oil and natural gas reserves. Accordingly, reserve estimates for Petroecuador included in this Noteholder Circular could be materially different from reserve estimates prepared in accordance with U.S. standards, or from the quantities of oil and gas that ultimately will be recovered.

The reserves estimated by Petroecuador are based on technical readings which allows the determination of the amount of petroleum reasonable in the subsoil using advanced exploitation methods.

Accounting

Accounting, auditing and financial reporting standards of Petroecuador are not comparable to those in the United States. Financial statements of Petroecuador have traditionally been prepared solely to comply with Ecuadorian tax requirements and are done in accordance with Ecuadorian Generally Accepted Accounting Principles (Ecuadorian GAAP), which are significantly different from U.S. GAAP. Because prices for domestic sales of petroleum derivatives have historically been set below international levels, the accounting system used by Petroecuador may not reflect true market valuations or opportunity costs.

Exploitation

Under the new Constitution, all subsurface resources are property of the state and, in the case of petroleum, its exploitation is undertaken directly by Petroecuador. The Constitution, however, permits the Government (including Petroecuador) to delegate the development of these resources to the private sector. Historically, foreign companies have played an important role in the development of oil production facilities. In 1982, the *Ley de Hidrocarburos* (the "Hydrocarbons Law") was amended to encourage foreign investment in the Republic's petroleum sector, permitting Petroecuador to enter into service contracts with private oil companies. In December 1993, the Hydrocarbons Law was again amended to introduce participation contracts and marginal field contracts,

and to terminate Petroecuador's monopoly in downstream activities and transfer the responsibility for dispute resolution under the various contracts from the Ministry of Energy and Mines and petroleum to the Superior Courts of Justice.

Following the 1993 amendment to the Hydrocarbons Law, two additional bidding rounds took place. Seven participation contracts were awarded in the seventh round, and three participation contracts were awarded in the eighth round. In 2006, the Hydrocarbons Law was again amended to allow the Government to earn higher profit through surplus-sharing mandates from oil produced and exported by private companies.

Under service contracts, a private company agrees to render to Petroecuador, at the company's own expense, exploration and exploitation services over specific areas. Petroecuador is required to repay amounts invested and costs incurred by the private company, plus a service fee. Additional returns are shared pursuant to formulas stated in each service contract.

Under participation or production-sharing contracts, Petroecuador delegates the exploitation and exploration of hydrocarbons to private companies. These companies explore and develop a designated area, bearing the entire cost and risk of investment. In return, each company receives an agreed percentage of the volume of oil extracted from the field subject to the contract.

Under marginal field contracts, private companies assume the costs and investment risk required to increase the production of existing fields. A "base curve" is established which consists of the projection of future production based on the historical production of each field, assuming that no additional investments are realised. All production under the "base curve" is owned by the Republic, although Petroecuador will recognise the private company's "base curve" production costs. Under the marginal field contracts, the private company must also transfer to Petroecuador a percentage of the production over the "base curve," agreed to in the marginal field contract. Under the Hydrocarbons Law, the Ministry of Energy and Mines and petroleum may classify as a "marginal field" any field that produces crude oil with a sufficiently low API, that is sufficiently removed from petroleum infrastructure or that accounts for less than 1% of the Republic's annual crude oil production.

The Government has periodically opened new blocks to exploration and exploitation through bidding rounds in which foreign and domestic corporations are invited to participate by responding to the Government's offer to enter into one or more of the forms of contract described above. Six bidding rounds took place between 1985 and 1990, resulting in the execution of thirteen service contracts for the exploration and exploitation of oil and gas deposits in thirteen blocks of territory: ten in the Oriente and three in the Guayas Province. As of December 31, 2004, twelve of these blocks have been renegotiated as participation contracts. In August 2005, several large and violent protests took place in the Amazon region of the Republic. Among the protesters' demands were increases in the Government's share of the production from the contracts with private companies and greater investment in public infrastructure by the private oil companies working in the region. Protesters disrupted crude production and vandalised pipelines and pumping stations.

In October 2005, Petroecuador's board of directors adopted the General Comptroller's recommendation to renegotiate all of the petroleum contracts according to the processes set forth in these contracts, which provide for mutual renegotiation of the contract terms by the parties under certain circumstances. In April 2006, the Congress approved law 42-2006 modifying the Hydrocarbons Law and determining a windfall tax on oil profits of at least 50%. In October 2007, President Correa's administration, with the approval of Congress, increased the windfall tax on oil profits from 50% to 99%, putting pressure on the companies to renegotiate their contracts. The new contract terms would transform the foreign-owned companies from participation contracts into service-provider contracts. All oil produced would belong to the Republic, and the Government would pay each company a service fee for its extraction work. The Republic later offered a reduction in the windfall tax to 70% for one year to those companies that signed temporary agreements which would become service contracts at the end of the year. In January 2008, the Government initiated negotiations with private companies regarding exploitation contracts in order to increase Government participation in the oil revenues resulting from increased market oil prices. During 2008, two private companies executed amended contracts with the Republic. Negotiations with the other companies continue.

As of December 31, 2008, there were seventeen private companies performing exploitation work in the Republic under different types of contracts. Repsol YPF, Andes Petroleum, City Oriente, Petroriental, Canadá

Grande, Perenco CNPC, Ecuador TLC and EDC have participation or production-sharing contracts with the Republic. Agip Oil has a service contract. Siperol has a strategic alliance contract. Tecpecuador, Petrolamerec, Palanda, Petrobel and Amazonas have marginal field contracts. In addition, Repsol YPF has a contract for specific services in the Tiracuno oil field and Pacific Petrol has a similar contract in the Gustavo Galindo Velazco oil field.

Production and Exports

The Republic's oil production increased from 2002 to 2004 due to increased exploitation of oil fields by private companies due in part to the OCP, oil pipeline which went on line in 2003. Oil production, however, then decreased from 120.4 million barrels in 2004 to 87.2 million barrels in 2008. This decrease reflected the return of Occidental's oil fields in Block 15 to the Republic in May 2006, causing production to decline. For a further discussion of the return of Occidental's oil fields to the Republic, see "Legal Proceedings—Occidental—Breach of Contract Claim". In 2008, oil production (excluding private companies) was 88.8 million barrels, a decrease of 5.9% from 2007.

In 2008, 50% of Petroecuador's crude oil was exported to the United States, 15.3% to Venezuela, 13.0% to Peru, and 11.4% to Chile. (The oil exports to Venezuela are primarily so that the oil is refined in Venezuela and then sent back to the Republic for further export or distribution.) Petroecuador currently exports approximately 77.5 million barrels of crude oil per year, which is predominantly obtained from the North-eastern Oriente region. During 2008, the Republic exported 127.4 million barrels, 77.5 million barrels comprised of Petroecuador's exports and 49.9 million barrels comprised of private company exports.

The following table sets forth information regarding Petroecuador's production, refinery consumption and exports of oil and related annual growth figures for the periods indicated.

Petroecuador's Production, Consumption Exports, Imports & Domestic Sales of Oil (thousands of barrels, except percentages)

	For the year ended December 31,							
	2005		2006		2007		2008 ⁽¹⁾	
	Amount	Annual Growth	Amount	Annual Growth	Amount	Annual Growth	Amount	Annual Growth
Production	70,972	(1.4)%	68,624	(3.3)%	62,151	(9.4)%	62,400	0.4%
Fiscal Production	63,235	(2.6)	86,307	36.5	91,173	5.6	95,383	4.6
Consumption (refineries) ⁽²⁾	54,499	(4.2)	54,858	0.7	54,795	(0.1)	56,760	3.6
Exports	66,496	3.9	85,579	28.7	81,022	(5.3)	92,896	14.7
Crude Oil	53,697	6.5	71,965	34.0	66,607	(7.4)	77,480	16.3
Imports	22,174	27.8	25,933	17.0	30,043	15.9	27,859	(7.3)
Domestic sales (derivatives)	61,933	9.1	65,767	0.7	65,171	(3.3)	67,447	3.6

(1) Preliminary data.

(2) This includes the three refineries of Esmeraldas, La Libertad and Amazonas.

Source: Petroecuador and Central Bank.

Transportation

Most of the Republic's crude oil production is transported through the Trans-Ecuadorian Pipeline System (the "SOTE"), which links Lago Agrio in the Oriente to the Balao export terminal on the Pacific coast. Until 2004, a small portion of the Republic's crude oil production was also transported through the Trans-Andean Pipeline which connected Ecuadorian fields in Lago Agrio to the Colombian export terminal of Orito. The SOTE was built by Texaco, and was transferred to Petroecuador in 1988. The SOTE has a capacity of approximately 390,000 bpd. In 2008, the SOTE transported 126.5 million barrels, averaging 345,700 bpd, an increase of 4.5% as compared with 2007.

In June 2001, the Republic awarded the construction and operation of the OCP heavy crude pipeline to Oleoducto de Crudos Pesados Ecuador S.A., a consortium of oil companies. The OCP was constructed at a cost of U.S.\$1.4 billion, all of which was paid for by the consortium. Construction was completed in September 2003, and

operations began in that same month. The contract for the operation of the OCP has a twenty-year duration, and terminates in 2023. At the expiration of this period, the OCP will become property of the Republic. The Ministry of Energy and Mines oversaw the construction of the OCP, and oversees its operation. The OCP is made up of two sections, the largest of which was designed to transport a maximum of 517,300 bpd and has a sustainable transportation rate of 450,000 bpd of crude oil of 18° to 24° API.

In 2004, the first full-year of operations, the OCP transported 62.4 million barrels, or an average of 170,888 bpd. As a result, the SOTE transported 118.4 million barrels in 2004, a decrease of 1.3% from 2003. In 2008, the OCP transported 48.5 million barrels of crude oil.

Refining

Petroecuador is the only company currently conducting refining activities in the Republic. Petroecuador owns three refineries (Esmeraldas, La Libertad and Amazonas) with processing capacities of 110,000, 45,000 and 20,000 bpd, respectively. Petroecuador also owns one associated gas processing plant (“Shushufindi”) with a processing capacity of 637.8 million barrels of liquefied petroleum gas with an average production of 1,747.6 barrels per day.

There is no private sector participation in the production of petroleum derivatives. In 2008, the three main refineries produced 60.3 million barrels of oil derivatives. The Esmeraldas refinery processed 65.3% of the Republic’s total derivatives production for domestic consumption, the Libertad refinery processed 22.9% of the Republic’s total derivatives production for domestic consumption, and the Amazonas refinery processed 11.8% of the Republic’s total derivatives production for domestic consumption (excluding the liquefied petroleum gas produced at Shushufindi). During 2008, the domestic consumption of oil derivatives increased to 67.4 million barrels, which represents an increase of 3.5% compared with 2007. As of this date, there is no private sector participation in the production of oil derivatives. However on July 15, 2008, Petroecuador and PDVSA Ecuador formed a new entity with an initial processing capacity of 300,000 bpd that may participate in the production of oil derivatives.

Distribution

In 1993, the Government implemented a free market in domestic fuel distribution which has led to a rapid modernisation of distribution facilities. The price at which gasoline may be sold to domestic distributors is fixed by the President in accordance with the Hydrocarbons Law. The price at which Petroecuador sells gasoline to domestic distributors is set according to variables such as domestic demand and its impact on public finances. Until 1998, the Government had fixed the maximum profit level for distributors at 18%. In 1999, the fixed margin was eliminated. In early 2000, the Government reinstated a 15% fixed margin for regular gasoline and diesel fuels (distributors remained free to set any margin for premium gasoline). Since 2003, the fixed margin has been fixed in cents per gallon. In 2008, the margin increased to U.S.\$0.171 per gallon for regular gasoline and U.S.\$0.137 per gallon for diesel. The margins were set by Presidential decree number 73 that was issued in August 2005. A president would need to issue a new decree to change the margins in the future.

Several multinational petroleum companies have established service stations in the Republic. Petroecuador, through its subsidiary Petrocomercial, also maintains a network of 150 service stations. On December 23, 2008, Petrocomercial inaugurated one service station in Guayaquil and has plans to open service stations in several other cities of the Republic, including Manabi, Manta and Quito. An important part of the commercial strategy of Petroecuador in 2008 has included distribution of natural gas to the south region of the Republic in order to reduce the consumption of liquefied petroleum gas (“GLP”); replacement of gasoline use with GLP use for taxis; and creation of network of service stations in order to compete in quality, service and price with the private oil companies.

In 2008, Petroecuador’s subsidiary, Petrocomercial, launched a number of strategic projects - production of natural gas for the southern region of Ecuador to reduce consumption of GLP; production of gas for taxis to reduce pollution and use of combustibles, improvements of the petroleum distribution network; development of network of petrol stations; and development of storage facilities in a maritime terminal at Monteverde for GLP, at a cost of approximately U.S.\$233 million.

Agriculture, Livestock, Hunting and Forestry

Before the discovery of petroleum fields in the Oriente provinces in the 1970s, the agriculture, livestock, hunting and forestry sector had traditionally been the largest contributor to the Republic's GDP. Of the Republic's total 27.1 million hectares, 7.8 million are devoted to agriculture and livestock. The Republic's diverse climatic conditions, varying altitudes and rich volcanic soil are well-suited to tropical and subtropical agriculture. The Republic's primary products from this sector, which are also the Republic's most significant non-oil export products, are bananas and shrimp. The Republic also exports significant amounts of coffee, flowers, cacao, tuna and wood.

The agricultural, livestock, hunting and forestry sector grew by 7.8% in 2005 and grew by 5.1%, 4.1%, and 3.55% in 2006, 2007 and 2008, respectively, primarily due to diversification into non-traditional agricultural products such as flowers, fruits, wood and tobacco. In 2008, this sector grew 3.5% and accounted for 10.4% of the GDP.

The Republic is the world's leading exporter of bananas. Between 2005 and 2008, the volume of the Republic's banana and plantain exports increased by 12.75%. In 2008, the value of Republic's banana and plantain exports grew 25.85%, primarily as a result of higher international prices.

The Republic also exports significant amounts of cacao. Cacao exports were U.S.\$118.1 million, U.S.\$143.3 million, U.S.\$197.3 million and U.S.\$201.6 million, in 2004, 2005, 2006 and 2007, respectively.

Non-traditional agricultural products, primarily flowers, have increased substantially since 2005. Total non-traditional exports were U.S.\$1.85 billion in 2004, U.S.\$2.3 billion in 2005, U.S.\$2.98 billion in 2006, U.S.\$3.55 billion in 2007 and U.S.\$3.94 billion in 2008. Flower exports grew an average of 17.5% per year during the 2005-2008 period.

Services

For purposes of internal analysis, the Republic aggregates the following sub-sectors of the economy into a single "services" sector: "construction", "electricity and water", "transportation, storage and communications", "wholesale and retail commerce", "public administration and defence", "social security", "financial intermediation services", "private homes with domestic servants", and "other services which include hotels and restaurants, real estate, education, health and social services".

The services sector constituted approximately 43.4%, 44.2%, 45.1% and 45.3% of GDP in 2005, 2006, 2007 and 2008, respectively. From 2004 to 2008, the "transportation and storage", and the "wholesale and retail commerce" sub-sectors, traditionally the largest components of the services sector, contributed an average 22.0% of GDP on an annual basis. The "transportation and storage" sub-sector increased by 5.1% in 2008, primarily as a result of the increase in the price of oil and other exports. The "wholesale and retail commerce" sub-sector grew 5.5% in 2008, primarily as a result of overall improvement in the economy.

Manufacturing

Manufacturing, excluding petroleum products, is dominated by consumer products such as food, beverages, textiles and paper, with a concentration on imported intermediate and capital goods. The two have increased during the period of 2004-2008 at an average rate of 23.9% and 21.9%, respectively. The manufacturing sector, on average, contributed 13.5% of GDP during the period from 2004 through 2008.

The Republic's principal manufactured non-petroleum exports are canned seafood, automobile assembly, processed coffee and cocoa. The manufacturing sector has improved since 2004. During 2004, 2005, 2006, 2007 and 2008 manufacturing grew 3.2%, 9.2%, 7.1%, 4.9% and 4.7%, respectively. Within the manufacturing sector, growth was substantial in the production of dairy, wheat, and beverages, as well as the processing and conservation of meat, among others.

The Republic's membership in international trade organisations and its status as a party to various multilateral agreements has contributed to the opening of new markets for the sale of Ecuadorian goods abroad and challenged domestic manufacturers to operate more competitively. The manufacturing sector, excluding oil refineries, totalled U.S.\$1.7 billion, U.S.\$2.2 billion, U.S.\$2.7 billion and U.S.\$3.1 billion in 2005, 2006, 2007 and 2008, respectively.

Fishing

The Republic is the largest shrimp producer in the Americas, and one of the largest producers in the world. Since 1999, global shrimp production was adversely affected by ichthyophthirius, more commonly known as "white spot disease", a ciliated parasite capable of affecting virtually all fish species. Between 1999 and 2003, white spot disease resulted in the death of a significant number of shrimp, and in a prohibition on the importation of shrimp larvae into the Republic. The Republic's shrimp exports, however, remained relatively stable during this time period, and the disease has been effectively controlled. Shrimp exports amounted to U.S.\$356 million in 2004 or 8.9% of total non-petroleum exports. In 2005, shrimp exports rose to U.S.\$458 million, and continued to rise to U.S.\$667 million in 2008. Shrimp exports represented approximately 10.0% of non-oil exports during that period.

Employment and Wages

The LET eliminated the concept of a minimum wage in the public sector and created the new concept of a unified wage (*remuneración unificada*) structure for public sector employees. In accordance with the LET, the *Consejo Nacional de Salarios* (the "National Council on Wages" or "CONADES") sets the minimum wage for workers in the private sector on an annual basis. The monthly minimum wage for a job in the private sector has increased 139.0% (in nominal terms) from U.S.\$97.7 as of December 31, 2000 to U.S.\$233.1 as of December 31, 2008. Public sector employee wages are based on the wage scale determined under the 2003 Civil Service and Administrative Career Law.

Until August 2007, the Republic measured unemployment and underemployment using the statistics prepared by *Facultad Latinoamericana de Ciencias Sociales* and the Central Bank ("FLACSO-BCE"). Since August 2007, the Republic has used the statistics from the National Institute of Statistics and Census and the Central Bank (*Instituto Nacional de Estadísticas y Censos y el Banco Central de Ecuador*), on INEC-BCE to measure employment and underemployment. The change in methodology may have caused a decrease in the measured rate of unemployment due to changes in definitions, process and other factors. Therefore the rates of unemployment for December 31, 2004-2006 are non-comparable to the rates for December 31, 2007 and 2008. During 2008, the lowest level of unemployment was reached during the months of July and August, both at 6.6%. The highest level of unemployment was registered in October 2008 at 8.7%. However by the end of 2008, the unemployment rate dropped to 7.3%. Furthermore in 2008, the underemployment rate was 48.8%.

The following table sets forth information regarding the unemployment and underemployment rates and real minimum wages as of December 31 for each of the years indicated. The Republic expects unemployment rates to increase in 2009 due to the effects of the global economic crisis on the Republic.

Wages and Unemployment

	For the year ended December 31,				
	2004	2005	2006	2007	2008
Unemployment rate (% of economically active population) ⁽¹⁾	9.9%	9.3%	9.0%	6.3%	7.3%
Underemployment rate (% of economically active population) ⁽²⁾	42.4%	49.2%	45.0%	44.0%	48.8%
Real minimum wage index ⁽³⁾	99.6	101.9	105.4	108.4	117.1

- (1) Refers to population at or above the minimum working age that is not employed and is willing to work (even if not actively seeking work) as a percentage of the total labour force. Unemployment statistics are reported by the Central Bank. Statistics reported by the Central Bank are gathered from the urban centres of Quito, Guayaquil, Cuenca and Ambato. Data are as of December 31 of each year.
- (2) Refers to individuals who are unable to obtain full-time work, to receive a salary meeting the official minimum wage or to perform activities related to their training.
- (3) Data are for December of each year, and includes the private sector minimum wage and complementary remuneration. January 1, 2004 through December 31, 2004 is used as the base period of 100 for this index.

Source: Central Bank. Unemployment statistics are provided to the Central Bank by the Latin American Faculty of Social Sciences (*La Facultad Latinoamericana de Ciencias Sociales – FLACSO*).

The following table sets forth information regarding the income distribution by quintile of the population for the periods indicated.

Distribution of Income by Population Quintile (in percentages)

	As of and for the year ended December 31,				
	Poorest 20% of the Population	Second Quintile	Third Quintile	Fourth Quintile	Richest 20% of the Population
1990.....	4.6%	9.2%	13.7%	20.5%	52.0%
1995.....	4.1	8.7	13.0	19.2	54.9
2001.....	1.7	5.9	10.8	17.3	64.3
2002.....	2.4	7.1	11.9	18.9	59.8
2003.....	2.6	6.1	12.4	20.2	59.3
2004.....	3.2	6.9	10.8	16.3	62.6
2005.....	4.0	8.9	14.6	20.4	52.3
2006.....	4.3	9.1	13.9	20.9	51.7
2007.....	4.3	9.1	13.1	20.1	53.3
2008.....	4.9	9.6	14.4	21.6	45.5

Source: Sistema Integrado de Indicadores Sociales del Ecuador (SIISE).

LEGAL PROCEEDINGS

The Republic is involved in certain litigation and administrative arbitration proceedings described below. An unfavourable resolution of any of these proceedings could have a material adverse effect on the Republic. The Republic can offer no assurances as to whether such proceedings will be successfully resolved in its favour. The proceedings described below are conducted pursuant to the mandatory arbitration provision contained in a bilateral treaty between the United States and the Republic entered into in 1997. The treaty aims to protect investors of both nations in the opposing country.

Occidental—Breach of Contract Claim

On September 16, 2004, Petroecuador sent Occidental a notice of breach of the participation contract for the exploration and exploitation of hydrocarbons in Block 15 alleging various grounds for forfeiture of the participation contract, including the unauthorised transfer of 40% of Occidental's rights and obligations under the participation contract to EnCana, the largest natural gas and oil producer in North America. Block 15 is one of the Republic's most productive oil fields. This notice initiated the forfeiture procedure set forth in the Hydrocarbons Law and the participation contract. On September 24, 2004, Occidental responded to the notice, and rejected all of the allegations contained in the notification of breach. Occidental has challenged the forfeiture procedures, claiming U.S.\$3.2 billion in damages. In May 2006, the Ministry of Energy and Mines declared the contract with Occidental to be terminated due to its alleged breach of the Hydrocarbons Law. As a result, all of Occidental's assets were transferred to the Republic. Through a filing with the arbitration panel CIADI in July 2006, Occidental's claims are based upon the alleged breach by Republic of its obligations under the bilateral treaty between the United States and the Republic. We expect that the arbitrators will resolve this suit by the end of the year. We continue to argue that Occidental breached the terms of the participation contract. There can be no assurance that the potential forfeiture of the Block 15 participation contract will not have an adverse effect on the Republic's crude oil production. In addition, there can be no assurance that the Republic will prevail in these proceedings.

Chevron Texaco

During the late 1960s, Texaco, now Chevron Texaco, operated a joint exploration concession with Gulf Oil Company in the Oriente region. In 1972, drilling operations began under the concession. In 1974, Petroecuador's predecessor company, CEPE, acquired 25% of the Texaco/Gulf concession. In 1977, CEPE bought Gulf's remaining interests and became a majority partner in the concession. Texaco remained in the consortium and served as the operator of the concession and the designer and builder of all of the consortium's facilities until 1989.

Chevron Texaco is currently facing claims brought by local residents and indigenous groups in the Republic since 1993 relating to environmental contamination alleged to have occurred as a result of the original consortium's activities in the Oriente region. In 2004, Chevron Texaco initiated arbitration proceedings against Petroecuador seeking to transfer all of these potential liabilities (currently estimated at U.S.\$1.2 billion by the claimants) to Petroecuador (i) as the successor to Gulf under the original consortium contract and (ii) based on an environmental release entered into by Petroecuador, the Republic and Texaco in 1998. Petroecuador petitioned to move the suit to the federal district court sitting in New York. The district court ultimately decided the case in favour of Petroecuador as Petroecuador was not originally a party to the consortium contract. Subsequently, Chevron Texaco appealed; the court of appeals ruled in favour of Petroecuador. Chevron Texaco may appeal this decision to the United States Supreme Court.

In addition, Chevron Texaco brought arbitration proceedings against the Republic before UNCITRAL. Chevron Texaco has alleged a breach by the Republic under the bilateral treaty between the United States and the Republic. These proceedings are ongoing. There can be no assurance as to the results of these legal proceedings or as to the timing of their possible resolution.

Windfall Profits Tax Litigation

A number of foreign oil companies have sued us in connection with the application of law 2006-42, which levied a 99% tax on the windfall profits of a number of foreign oil companies. For a description of the windfall profits tax, see "The Republic of Ecuador—The Ecuadorian Economy—Principal Sectors of the Economy—Mining

(Petroleum and Petrochemicals)—Exploitation”. As a result of the implementation of the windfall profits tax law, we are defendants in five arbitration proceedings, although one, with City Oriente, has settled. Two of the other four proceedings have been brought by Burlington Resources, Inc. and Perenco Ecuador Limited, with respect to Blocks 7 and 21, respectively. The remaining two proceedings were initiated by Murphy Ecuador Oil Company, Ltd., and Repsol YPF in respect of Block 16.

Burlington Resources, Inc.

Burlington Resources, Inc. filed an arbitration claim before the ICSID requesting that the windfall profits tax law not apply. Burlington argued that the provisions contained in the law violated international treaties agreed to by the Republic and the agreements entered into between Burlington and the Republic.

Furthermore, Burlington claims that the Republic and Petroecuador did not provide a safe environment for Burlington to carry out its exploration activities in Blocks 23 and 24 and that the Republic breached its obligation to pay fair consideration with respect to its expropriation.

Burlington is requesting to the arbitration panel that the Republic pay damages and losses caused to Burlington as a consequence of the Republic's breach of its contractual obligations, including interest. The arbitration panel has given a date for a hearing. There can be no assurance as to the results of these legal proceedings or as to the timing of their possible resolution.

Perenco Ecuador Limited

In April 2008, Perenco Ecuador Limited filed an arbitration claim before the ICSID against the Republic requesting that the windfalls profits tax law not apply, as well as other related claims.

Perenco has requested that the arbitration panel rule to prevent the Republic from collecting the taxes allegedly owed to the Republic by Perenco pursuant to the windfall profits tax law. There can be no assurance as to the results of these legal proceedings or as to the timing of their possible resolution.

Murphy Ecuador Oil Company, LTD.

In March 2008, Murphy Ecuador Oil Company, LTD. (independently and not as a member of the Block 16 Consortium) filed an arbitration claim against the Republic before the ICSID requesting that the windfall profits law not apply. This case is still pending and there can be no assurance as to the result of these legal proceedings or as to the timing of their possible resolution.

Repsol YPF, Murphy, CRS Resources, Overseas Petroleum

In June 2008, Repsol YPF (as common representative of the consortium integrated by Murphy Ecuador Oil Company Ltd., CRS Resources (Ecuador), LDC, Overseas Petroleum and Investment Corporation (“the Block 16 Consortium”)) filed an arbitration claim. Under the claim, Repsol YPF requested (i) that the windfall profits tax law not apply; (ii) a detailed description of the amount of oil transported through the SOTE pipeline; (iii) that certain taxes levied against the consortium members not apply; (iv) that the increase of oil transportation fees not apply to the consortium members; and (v) certain related claims against the Republic.

The Republic has executed an agreement with Repsol YPF, with respect to its claims referred to in clauses (i), (iii) and (iv) above. Likewise, the Republic and Repsol YPF executed a supplemental agreement by virtue of which they agreed to amend the original agreement into a services agreement under which the Republic becomes the owner.

The matters referred to in clauses (i), (iii) and (iv) above are still pending and there can be no assurance as to the result of the legal proceedings or as to the timing of the resolution.

Odebrecht—Breach of Contract Claim

In March 29, 2000, the Republic and Odebrecht, a leading Brazilian construction company, entered into an agreement whereby Odebrecht agreed to construct the “San Francisco” hydroelectric dam, the second-largest hydroelectric dam in Ecuador. The construction of the “San Francisco” dam was concluded in 2007, but was not functioning correctly because of the non-compliance with certain mechanical, electrical and equipment specifications. The dam stopped operating in June 2008. After negotiations between Odebrecht and us broke down, President Correa issued a decree accusing Odebrecht of “putting public service at risk”. In September 2008, we sent military troops to seize the dam.

We are planning to file an arbitration claim against Odebrecht for approximately US\$210 million in damages, alleging that Odebrecht failed to build the dam properly and illegally raised the price of the project.

BALANCE OF PAYMENTS AND FOREIGN TRADE

Balance of Payments

General

The balance of payments is used to record the value of the transactions carried out between a country's residents and the rest of the world. The balance of payments is composed of two accounts:

- the current account, which comprises:
 - net exports of goods and services (the difference in values of exports minus imports);
 - net financial and investment income;
 - net transfers; and
- the capital and financial account, which is the difference between financial capital inflows and financial capital outflows.

Current Account

One of the most important components of the current account is the trade balance. The five primary factors that drive the trade balance are:

- the relative rate of economic growth of a country as compared to that of its trading partners—generally, if a country's economy grows faster than that of its trading partners, its relative level of consumption of goods and services will tend to rise, and its level of imports will tend to increase more rapidly than its level of exports;
- the relative level of domestic prices against foreign prices, as reflected by the real exchange rate—generally, if a country's domestic prices rise relative to those of its trading partners, there is a tendency for the country's level of exports to decline, and for its level of imports to increase;
- changes in production costs, technology, and worker skills—more efficient production will tend to lower production cost, which in turn will tend to lower prices. As prices fall, there will be a tendency for the country's level of exports to increase;
- changes in consumer tastes, which may affect the demand for a country's goods and services abroad, and the demand for foreign products in the domestic market; and
- sudden increases or decreases in the price for the major exports of a country, particularly the fluctuations in the market price of oil.

The Republic recorded a current account surplus of U.S.\$348 million in 2005, U.S.\$1.6 billion in 2006, U.S.\$1.6 billion in 2007, which represented 0.9%, 3.9% and 3.6% of GDP in 2005, 2006 and 2007, respectively. For 2008, the Republic's current account balance deteriorated significantly, registering a lower surplus, mainly due to the decline in global oil prices and the increase in consumer goods imports. The Republic's current account surplus primarily reflected an increase in the market price of oil, as well as a favourable performance, both in volume and price, of non-oil exports. In recent years, remittances increased approximately U.S.\$2.4 billion in 2005, reflecting an increase of 33.9% as compared to 2004. The remittances totalled approximately U.S.\$2.9 billion in 2006 and U.S.\$3.0 billion in 2007, reflecting an increase of 19.3% and 5.5%, respectively. These remittances represent an average of 6.5% of GDP during the period 2004-2007. Of the Ecuadorians currently abroad, the majority are in the United States, with significant percentages of the remainder in Spain and Italy.

The following tables set forth information regarding the Republic's balance of payments for the periods indicated. The column heading 2008 (I) refers to the first quarter, 2008 (II) to the second quarter and 2008 (III) to the third quarter of that year. In the third quarter of 2008, the decrease in the current amount resulted from lower volumes of crude oil exports as well as the decrease in the market price of oil.

Balance of Payments
(in millions of U.S.\$)

	For the year ended December 31,				For the three months ended March 31,	For the three months ended June 30,	For the three months ended September 30,
	2004	2005	2006	2007	2008 (I) ⁽¹⁾	2008 (II) ⁽¹⁾	2008 (III) ⁽¹⁾
Current account	(541.9)	347.7	1,617.5	1,650.0	1,280.4	1,260.8	96.7
Trade balance ⁽²⁾	284.0	758.3	1,768.4	1,829.0	1,201.9	1,401.0	170.2
Exports (FOB).....	7,967.8	10,467.7	13,176.1	14,870.2	4,785.2	5,699.6	5,348.5
Petroleum and derivatives.....	4,234.0	5,869.8	7,544.5	8,328.6	2,964.2	3,757.0	3,420.6
Non-petroleum.....	3,733.8	4,597.8	5,631.6	6,541.6	1,821.1	1,912.7	1,927.9
Imports (FOB).....	(7,683.7)	(9,709.4)	(11,407.7)	(13,047.1)	(3,583.3)	(4,268.6)	(5,178.3)
Services	(953.7)	(1,129.9)	(1,304.7)	(1,371.5)	(336.5)	(397.8)	(404.3)
Rendered Services (credit).....	1,013.9	1,012.1	1,036.5	1,200.1	324.0	355.2	372.7
Transportation.....	340.5	335.2	352.2	347.6	86.8	99.2	103.5
Travel.....	462.5	485.8	489.9	623.4	165.4	187.4	206.6
Other.....	211.0	191.2	194.4	229.1	71.8	68.6	62.5
Received Services (debit).....	(1,967.7)	(2,142.0)	(2,341.3)	(2,571.6)	(660.5)	(753.1)	(776.9)
Transportation.....	(910.7)	(1,042.5)	(1,170.9)	(1,327.0)	(356.3)	(388.5)	(459.0)
Travel.....	(391.0)	(428.6)	(466.3)	(504.0)	(133.0)	(136.6)	(135.3)
Other.....	(666.0)	(670.9)	(704.1)	(740.6)	(171.2)	(227.9)	(182.6)
Investment Income	(1,902.4)	(1,941.6)	(1,950.0)	(2,047.1)	(402.3)	(500.3)	(412.0)
Inflows (credit).....	37.4	86.4	165.0	258.6	58.3	42.0	49.5
Employees' Remuneration.....	6.0	6.5	6.2	6.0	1.5	1.5	1.5
Others.....	31.4	79.9	158.8	252.7	56.8	40.5	48.0
Outflows (debit).....	(1,939.8)	(2,028.1)	(2,115.0)	(2,305.7)	(460.6)	(542.3)	(461.5)
Employees' Remuneration.....	(6.5)	(5.8)	(5.2)	(5.3)	(1.4)	(1.4)	(1.4)
Direct Investment Income.....	(964.0)	(1,003.9)	(977.4)	(1,160.1)	(197.3)	(171.7)	(225.2)
Portfolio Investment Income.....	(344.1)	(372.3)	(416.4)	(399.0)	(137.1)	(62.3)	(136.2)
Other Investment Income.....	(625.2)	(646.1)	(716.0)	(741.4)	(124.8)	(306.9)	(98.7)
Net transfers	(2,030.2)	(2,660.9)	(3,103.9)	(3,245.6)	817.31	757.9	742.8
Emigrant remittances.....	1,832.0	2,453.5	2,927.6	3,087.8	759.63	711.5	706.6
Capital and financial account	139.6	(101.7)	(2,088.9)	(275.0)	(661.6)	663.3	237.7
Capital Account	8.1	13.0	18.6	22.1	4.8	5.8	6.2
Financial Account	131.5	(114.8)	(2,107.4)	(297.0)	(666.4)	657.5	231.6
Direct Investment.....	836.9	493.4	270.7	193.3	419.8	102.3	299.6
Portfolio Investment.....	(190.3)	365.9	(1,383.9)	(118.3)	102.2	64.1	(196.9)
Other Investment.....	(515.2)	(974.0)	(994.3)	(372.0)	(1,188.4)	491.0	128.9
Errors and omissions	683.4	420.1	340.7	11.6	57.3	39.6	72.6
Total balance of payments	281.0	666.1	(130.6)	1,386.6	676.1	1,963.7	407.0
Financing	(281.0)	(666.1)	130.6	(1,386.6)	(676.1)	(1,963.7)	(407.0)

	For the year ended December 31,				For the three months ended March 31,	For the three months ended June 30,	For the three months ended September 30,
	2004	2005	2006	2007	2008 (I) ⁽¹⁾	2008 (II) ⁽¹⁾	2008 (III) ⁽¹⁾
International reserves ⁽³⁾	(276.9)	(709.6)	123.6	(1,497.5)	(622.7)	(1,959.5)	(408.3)
IMF loans	0.0	0.0	0.0	0.0	N/A	N/A	N/A
Exceptional financing, net ⁽⁴⁾	(4.1)	43.5	7.1	110.9	(53.4)	(4.2)	1.4

(1) Preliminary data.

(2) Includes unrecorded trade.

(3) These data correspond to freely disposable international reserves.

(4) These data refer to delays in the payment of debt, debt condonations and debt refinancing.

Source: Central Bank.

Capital and Financial Account

The capital and financial account measures valuations in assets and liabilities of the Republic as against the rest of the world (other than valuations from exceptional financings). The Republic's recorded capital and financial account deficits of U.S.\$102 million, U.S.\$2.0 billion and U.S.\$275 million in 2005, 2006 and 2007, respectively. Total foreign direct investment was U.S.\$493 million in 2005, U.S.\$271 million in 2006 and U.S.\$193 million in 2007. The portfolio investment line item, which recorded a deficit of \$1.38 billion in 2006, was partially due to the \$740 million redemption of the principal amount of the 2012 Bonds.

Foreign Trade

Merchandise and Services Trade

The Republic has historically been an exporter of primary goods and an importer of raw materials, capital and intermediate goods and manufactured products. The Republic's main exports are relatively limited in terms of sectors and export markets. Two primary export markets, the United States and the European Union, have been significantly affected by the current global recession. Between January and November 2008, a majority of the Republic's total exports were to the United States and the European Union. As a result, the Republic is seeking to expand the types of goods it exports as well as its trading partners, through development banks and other strategic initiatives. Since 1972, exports of petroleum and petroleum derivatives have comprised the majority of Ecuadorian export products. In 2005, 2006 and 2007, exports of petroleum and petroleum derivatives accounted for approximately 58.1%, 59.3% and 58.2%, respectively, of total exports. Between 2004 and 2007, non-traditional exports, which include, among others, flowers, vehicles, manufactured textile products and seafood, increased an average of 24.4%.

The Republic's total export trade has grown steadily during the period between 2004 and 2007. In 2008, total exports rose to U.S.\$18.4 billion, as compared to U.S.\$14.3 billion in 2007.

Trade Policy

The Republic's trade policy has focused on the strategic integration of the country into the international economy, as well as increasing the access of Ecuadorian goods and services to new markets, and reducing non-tariff barriers to trade until recently.

Until the late 1980s, the Republic used tariff barriers to protect its domestic industry against foreign competition. Import duties ranged from zero to 290%, with up to fourteen different rates.

In the early 1990s, the Government began to significantly liberalise its foreign trade policy. As a result of those reforms, the tariff structure was simplified, and currently consists of a seven-tiered structure (0%, 3%, 5%, 10%, 15%, 20% and 35%), with levels of 5% for most raw materials and capital goods, 10% or 15% for

intermediate goods and 20% for most consumer goods. A small number of products, including planting seeds, are subject to a tariff rate of zero, and the 35% tariff is exclusively applied to the automobile industry. Average tariff levels were reduced from 29% in 1989 to 6% in 2004.

In January 2009, the Republic, through the *Consejo de Comercio Exterior e Inversiones*, imposed tariffs of general applicability on some consumer goods imports, including products imported from countries with which the Republic has commercial treaties honouring preferential status. The Republic has said that the tariffs will only be enforced for one year in order to be able to restore its trade balance, as a consequence of the current economic climate. For a further discussion of the Republic's imposition of tariffs on 630 goods, see "Republic of Ecuador—Constitution, Government and Political Parties—International and Regional Relations".

In December 2007, the Republic introduced an exit tax of 0.5% on any currency leaving the country. This was subject to a number of exemptions. In December 2007, the Republic increased this exit tax to 1% and eliminated the applicable exemptions. The Republic was notified by the Andean Community in February 2009 that Colombia has asked the Secretary General of the Andean Community to investigate whether this exit tax should be properly regarded as a tax or a distortion of trade.

Regional Integration and Trade

The Republic's trade and regional integration policy consists of strategically entering new markets, promoting the growth of non-traditional exports and encouraging investment.

The Republic has intensified its efforts to strengthen trade arrangements with its primary trading partners, including:

- removing regional trade restrictions as a member of ALADI (a regional external trade association that includes the Republic, Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Mexico, Paraguay, Peru, Uruguay and Venezuela);
- reducing or eliminating tariff barriers to trade as a member of the Andean Community, except in relation to the temporary measure taken to increase the Republic's balance of payments in early 2009 as a result of the global recession;
- entering into bilateral trade agreements with Colombia, Venezuela and Bolivia that are aimed at levying uniform tariffs on goods from third parties;
- entering into a bilateral trade agreement with Chile in March 2008;
- negotiating a bilateral association agreement with Paraguay;
- restarting the process of negotiating with the European Union in respect of the Multiparty Commercial Agreement; and
- maintaining the preferential access to United States markets of certain goods under the ATP-DEA and with the European Union under the preferential trade status.

The following table sets forth information regarding exports for the periods indicated.

Exports (FOB)⁽¹⁾
(in millions of U.S.\$ and as a % of total exports)

	For the year ended December 31,									
	2004		2005		2006		2007		2008	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Crude oil	3,899	50.3	5,397	53.4	6,934	54.5	7,428	51.9	10,568	57.2
Bananas and plantains	1,024	13.2	1,084	10.7	1,213	9.5	1,303	9.1	1,639	8.9
Petroleum derivatives	335	4.3	473	4.7	611	4.8	900	6.3	1,104	6.0
Shrimp	330	4.3	458	4.5	588	4.6	613	.43	667	3.6
Cacao and cacao products	154	2.0	176	1.7	171	1.3	239	1.7	260	1.4
Coffee and coffee products	84	1.1	92	0.9	99	0.8	123	0.9	129	0.7
Tuna and other fish	82	1.1	115	1.1	128	1.0	169	1.1	185	1.0
Other products(2)	1,845	23.8	2,305	22.8	2,984	23.4	3,546	24.8	3,936	21.3
Total	7,753	100.0%	10,100	100.0%	12,728	100.0	14,321	100.0	18,490	100.0

(1) Data is for registered exports only.

(2) "Other products" consist of non-traditional primary and manufactured products, including canned seafood, flowers, vehicles, manufactured metals and chemicals.

Source: Central Bank.

The following table sets forth information regarding imports for the periods indicated.

Imports (CIF)⁽¹⁾
(in millions of U.S.\$ and as a % of total imports)

	For the year ended December 31,									
	2004		2005		2006		2007		2008	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Consumer goods	2,069	14.6	2,356	13.5	2,598	12.9	2,912	12.5	4,037	12.6
Non-durable goods	1,189	8.4	1,339	7.7	1,494	7.4	1,794	7.7	2,355	7.4
Durable goods	880	6.2	1,018	5.8	1,105	5.5	1,118	4.8	1,682	5.3
Primary materials	2,566	18.1	2,935	16.8	3,469	17.2	4,093	17.6	5,831	18.2
Agriculture	340	2.4	347	2.0	380	1.9	496	2.1	783	2.4
Industrial	2,039	14.4	2,318	13.3	2,754	13.6	3,228	13.9	4,587	14.3
Construction materials	187	1.3	269	1.5	335	1.7	369	1.6	461	1.4
Capital goods	1,944	13.7	2,557	14.7	2,829	14.0	3,319	14.3	4,501	14.1
Agriculture	36	0.2	42	0.2	43	0.2	52	0.2	87	0.3
Industrial	1,280	9.0	1,630	9.4	1,712	8.5	2,037	8.8	2,846	8.9
Transportation equipment	628	4.4	886	5.1	1,074	5.3	1,231	5.3	1,569	4.9
Fuel and combustibles	995	7.0	1,715	9.8	2,381	11.8	2,578	11.1	3,226	10.1
Other	1	0.0	5	0.0	1	0.0	3	0.0	13	0.0
Total	14,154	100.0%	17,417	100.0%	20,175	100.0%	23,230	100.0%	31,978	100.0%

(1) Data is for registered imports only.

Source: Central Bank.

Composition of Free Trade

The Republic's largest trading partners are the United States, the European Union, Venezuela and Colombia. The following table sets forth information regarding the country of destination of the Republic's exports.

Exports (FOB) (in millions of U.S.\$ and as a % of total exports)

	For the year ended December 31,							
	2005		2006		2007		2008	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Americas								
United States	5,050	50.0	6,825	53.6	6,169	43.1	8,373	45.3
Colombia	511	5.1	715	5.6	740	5.2	773	4.2
Venezuela	140	1.4	319	2.5	592	4.1	698	3.8
Other countries	2,547	25.2	2,498	19.6	4,018	28.1	5,211	28.2
Total Americas	<u>8,248</u>	<u>81.6</u>	<u>10,357</u>	<u>81.4</u>	<u>11,519</u>	<u>80.4</u>	<u>15,055</u>	<u>81.4</u>
Europe								
European Union (EU)								
.....	1,270	12.6	1,487	11.7	1,812	12.7	2,076	11.2
Italy	386	3.8	427	3.4	458	3.2	510	2.8
United Kingdom ..	74	0.7	69	0.5	99	0.7	153	0.8
Germany	201	2.0	223	1.8	248	1.7	300	1.6
Spain	218	2.2	296	2.3	357	2.5	417	2.2
Other countries	391	3.9	472	3.7	650	4.5	696	3.8
Rest of Europe	362	3.6	392	3.1	505	3.5	645	3.5
Total Europe ...	<u>1,632</u>	<u>16.2</u>	<u>1,879</u>	<u>14.8</u>	<u>2,317</u>	<u>16.2</u>	<u>2,721</u>	<u>14.7</u>
Asia								
Taiwan	5	0.0	6	0.0	16	0.1	20	0.1
Japan	73	0.7	123	1.0	106	0.7	102	0.5
Other countries	116	1.1	318	2.5	309	2.2	504	2.7
Total Asia	<u>194</u>	<u>1.9</u>	<u>446</u>	<u>3.5</u>	<u>431</u>	<u>3.0</u>	<u>626</u>	<u>3.4</u>
Africa	8	0.1	6	0.0	21	0.1	16	0.1
Oceania	16	0.2	31	0.2	20	0.1	17	0.1
Other countries	3	0.0	3	0.0	13	0.1	57	0.3
Total	<u>10,101</u>	<u>100.00%</u>	<u>12,722</u>	<u>100.00%</u>	<u>14,321</u>	<u>100.00%</u>	<u>18,492</u>	<u>100.00%</u>

Source: Central Bank.

The following table sets forth information regarding the country of origin of the Republic's imports for the periods presented.

Imports (CIF)
(in millions of U.S.\$ and as a % of total exports)

	For the year ended December 31,							
	2005		2006		2007		2008	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Americas								
United States	2,032	19.8	2,739	22.6	2,869	20.7	3,543	19.0
Colombia	1,397	13.6	1,547	12.8	1,522	11.0	1,784	9.5
Venezuela	451	4.4	430	3.6	1,316	9.5	2,586	13.8
Other countries	2,974	28.9	3,421	28.2	3,598	25.9	4,302	23.0
Total Americas	<u>6,854</u>	<u>66.6</u>	<u>8,137</u>	<u>67.2</u>	<u>9,305</u>	<u>67.0</u>	<u>12,215</u>	<u>65.3</u>
Europe								
European Union (EU)								
.....	1,069	10.4	1,210	9.0	1,240	10.0	1,577	8.4
Italy	116	1.1	171	1.4	162	1.2	202	1.1
United Kingdom ..	70	0.7	67	0.6	69	0.5	73	0.4
Germany	232	2.3	237	2.0	288	2.1	376	2.0
Spain	140	1.4	147	1.2	179	1.3	222	1.2
Other countries	511	5.0	588	4.8	542	3.9	704	3.8
Total EU	<u>1,069</u>	<u>10.4</u>	<u>1,210</u>	<u>10.0</u>	<u>1,240</u>	<u>8.9</u>	<u>1,577</u>	<u>8.4</u>
Rest of Europe	208	2.0	275	2.3	200	1.4	297	1.6
Total Europe ...	<u>1,277</u>	<u>12.4</u>	<u>1,485</u>	<u>12.3</u>	<u>1,440</u>	<u>10.4</u>	<u>1,874</u>	<u>10.0</u>
Asia								
Taiwan	151	1.5	108	0.9	114	0.8	150	0.8
Japan	360	3.5	457	3.8	543	3.9	769	4.0
Other countries	1,527	14.9	1,785	14.7	2,250	16.2	3,359	18.0
Total Asia	<u>2,038</u>	<u>19.8</u>	<u>2,350</u>	<u>19.4</u>	<u>2,907</u>	<u>20.9</u>	<u>4,278</u>	<u>22.9</u>
Africa	110	1.1	133	1.1	211	1.1	159	0.9
Oceania	7	0.1	7	0.1	13	0.1	27	0.1
Other countries	1	0.0	1	0.0	18	0.1	139	0.7
Total	<u>10,287</u>	<u>100.00%</u>	<u>12,113</u>	<u>100.00%</u>	<u>13,894</u>	<u>100.00%</u>	<u>18,692</u>	<u>100.00%</u>

Source: Central Bank.

Foreign Direct Investment

The Republic's foreign investment policy is governed largely by national implementing legislation for the Andean Community's Decisions 291 of 1991 and 292 of 1993. Generally, foreign investors are accorded the same rights of establishment as Ecuadorian private investors, and may own up to 100% of enterprises in most sectors without prior Government approval and face the same tax regime. There are no controls or limits on transfers of profits or capital.

Certain sectors of the Republic's economy are reserved to the state. All foreign investments in petroleum exploration and development in the Republic must be carried out under contracts with Petroecuador. See "Republic of Ecuador—The Ecuadorian Economy—Principal Sectors of the Economy—Mining (Petroleum and Petrochemicals)".

Foreign direct investment in 2007 totalled U.S.\$194 million, a 39.7% decrease as compared to the level of foreign direct investment in 2006. In 2005, foreign direct investment totalled U.S.\$494 million, a 41% decrease over the level in 2004. As of December 31, 2007, 62.8% of the Republic's total direct foreign investment was in the mining sector.

During the first nine months of 2008, 28.0% of the foreign direct investment was in the transportation, storage and communications sector, 20.0% was in the mining sector, 16% was in the commerce sector and 15% was in the manufacturing sector.

The following table sets forth information regarding foreign direct investment by sector for the periods indicated.

Foreign Investment by Sector
(in millions of U.S.\$ and as a % of total foreign investment)

	For the year ended December 31,									
	2004		2005 ⁽¹⁾		2006 ⁽¹⁾		2007 ⁽¹⁾		2008 ⁽¹⁾⁽²⁾	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Agriculture, forestry, hunting and fishing	72.9	8.7	23.9	4.8	47.3	17.5	24.2	12.5	12.7	1.5
Mining ⁽³⁾	385.4	46.0	198.3	40.2	(116.6)	(43.1)	(122.1)	(62.9)	161.3	19.6
Manufacturing	114.9	13.7	75.4	15.3	90.2	33.3	96.9	49.9	126.4	15.4
Electricity, natural gas and water	5.6	0.7	6.5	1.3	6.9	2.5	16.4	8.4	(4.3)	(0.5)
Construction	39.2	4.7	7.4	1.5	8.4	3.1	32.9	16.9	32.4	3.9
Commerce	103.2	12.3	72.5	14.7	32.3	11.9	79.4	40.9	131.8	16.0
Transportation, storage and telecommunications	73.7	8.8	17.5	3.5	83.3	30.8	(56.1)	(28.9)	226.7	27.6
Services rendered to firms	40.0	4.8	73.8	15.0	89.4	33.0	56.3	29.0	91.1	11.1
Social and personal services	2.1	0.3	18.0	3.6	29.5	10.9	66.3	34.1	43.5	5.3
Total	837.9	100.0%	493.3	100.0%	270.7	100.0%	194.2	100.0%	821.6	100.0%

(1) Preliminary data.

(2) Data is through September 2008.

(3) The mining sector includes the petroleum and petrochemicals sectors.

Sources: Central Bank, Superintendent of Companies and Superintendent of Banks.

The new Constitution contains certain principles relating to foreign investment, including promoting national and international investment (with priority being given to national investment and a complementary role being attributed to international investment); subjecting foreign investment to our national legal framework and regulations; prohibiting expropriation without indemnification; limiting access to strategic sectors, which will remain in state control; providing for disputes relating to international agreements to be resolved in a regional (Latin American) forum; and avoiding disputes between the Republic and private companies from becoming disputes between sovereigns.

The following table sets forth information on foreign direct investment by country of origin for the periods indicated. During 2007, the largest foreign investors, in net terms, were the United States, Panama, Brazil, France and Spain.

Foreign Investment by Country of Origin
(in millions of U.S.\$ and as a % of total foreign investment)

	For the year ended December 31,								For the nine months ended September 30,	
	2004		2005 ⁽¹⁾		2006 ⁽¹⁾		2007 ⁽¹⁾		2008 ⁽¹⁾	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Americas.....	711.8	85.1	509.8	103.3	144.6	53.4	(112.3)	(57.8)	498.0	60.6
United States.....	78.5	9.4	(77.2)	(15.6)	(159.8)	(59.0)	82.0	42.2	38.0	4.6
Andean Community ⁽²⁾	20.7	2.5	12.3	2.5	13.7	5.1	38.3	19.8	75.9	9.2
Colombia.....	11.8	1.4	1.0	0.2	19.9	7.3	21.2	10.9	6.8	0.8
Bolivia.....	0.0	0.0	0.0	0.0	0.7	0.3	0.0	0.0	16.6	2.0
Peru.....	2.0	0.2	8.9	1.8	(6.7)	(2.5)	1.4	0.7	34.8	4.2
Venezuela ⁽²⁾	6.9	0.8	2.4	0.5	(0.1)	0.0	15.8	8.1	17.7	2.2
Rest of Americas.....	612.6	73.2	574.7	116.5	290.6	107.3	(232.7)	(119.7)	384.1	46.7
Dutch Antilles.....	1.6	0.2	(2.8)	(0.6)	8.0	3.0	5.3	2.7	(1.6)	(0.2)
Argentina.....	12.6	1.5	1.7	0.3	2.9	1.1	7.4	3.8	21.3	2.6
Bahamas.....	113.7	13.6	28.3	5.7	(17.4)	(6.4)	(111.7)	(57.5)	(10.3)	(1.3)
Bermudas.....	2.1	0.3	2.2	0.4	(0.1)	0.0	2.2	1.1	1.2	0.1
Brazil.....	188.5	22.5	288.1	58.4	368.9	136.2	75.8	39.0	15.8	1.9
Canada.....	273.6	32.7	29.2	5.9	(251.7)	(92.9)	35.4	18.2	25.8	3.1
Chile.....	34.8	4.2	72.6	14.7	15.5	5.7	24.9	12.8	14.9	1.8
Cayman Islands.....	31.6	3.8	(1.6)	(0.3)	(9.6)	(3.5)	(356.6)	(183.4)	2.1	0.3
Virgin Islands.....	75.5	9.0	45.0	9.1	39.2	14.5	41.9	21.6	36.0	4.4
Mexico.....	(0.2)	0.0	7.3	1.5	42.6	15.7	(40.2)	(20.7)	248.1 ⁽³⁾	30.2
Panama.....	93.5	11.2	76.2	15.4	66.7	24.6	78.3	40.3	54.7	6.7
Uruguay.....	1.3	0.2	6.4	1.3	14.8	5.5	2.3	1.2	(28.6)	(3.5)
Other Countries.....	(216.0)	(25.8)	22.1	4.5	10.8	4.0	2.3	1.2	4.7	0.6
Europe.....	108.9	13.0	(0.1)	0.0	84.0	31.0	241.9	124.4	292.5	35.6
Germany.....	0.8	0.1	11.7	2.4	12.0	4.4	3.5	1.8	5.5	0.7
Belgium and Luxembourg.....	3.2	0.4	4.9	1.0	4.5	1.7	1.6	0.8	20.0	2.4
Denmark.....	0.0	0.0	0.5	0.1	0.4	0.1	(0.5)	(0.3)	0.0	0.0
Spain.....	0.6	0.1	2.7	0.5	6.9	2.5	72.7	37.4	104.7 ⁽⁴⁾	12.7
France.....	14.8	1.8	(0.8)	(0.2)	8.4	3.1	77.5	39.9	31.5	3.8
Holland.....	46.3	5.5	(43.1)	(8.7)	38.1	14.1	7.8	4.0	0.7	0.1
Great Britain.....	6.7	0.8	19.3	3.9	11.9	4.4	4.9	2.5	4.9	0.6
Italy.....	0.3	0.0	0.0	0.0	0.4	0.1	23.2	11.9	13.9	1.7
Romania.....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Sweden.....	6.9	0.8	1.0	0.2	1.5	0.6	(4.5)	(2.3)	0.2	0.0
Switzerland.....	19.7	2.4	3.6	0.7	7.0	2.6	3.1	1.6	24.5	3.0
Other countries.....	9.6	1.1	0.1	0.0	(7.1)	(2.6)	52.6	27.1	86.6	10.5
Asia.....	2.0	0.2	(19.5)	(4.0)	28.5	10.5	66.6	34.3	31.7	3.9
China.....	(7.7)	(0.9)	(19.9)	(4.0)	11.9	4.4	59.8	30.8	30.7	3.7
South Korea.....	0.0	0.0	2.1	0.4	0.1	0.0	0.3	0.2	0.0	0.0
Japan.....	0.5	0.1	0.2	0.0	0.0	0.0	0.0	0.0	0.1	0.0
Taiwan.....	0.0	0.0	0.0	0.0	0.0	0.0	1.2	0.6	0.2	0.0
Israel.....	8.7	1.0	(2.3)	(0.5)	(0.4)	(0.1)	0.2	0.1	0.1	0.0
Other countries.....	0.5	0.1	0.4	0.1	16.9	6.2	5.1	2.6	0.6	0.1
Oceania.....	13.8	1.6	0.3	0.1	0.5	0.2	(0.8)	(0.4)	0.0	0.0
Australia.....	13.8	1.6	0.3	0.1	0.5	0.2	(0.8)	(0.4)	0.0	0.0
Other countries.....	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other countries.....	0.4	0.0	2.9	0.6	13.3	4.9	(1.0)	(0.5)	(0.3)	0.0
Total.....	836.9	100.0	493.4	100.0	270.9	100.0	194.4	100.0	821.7	100.0

(1) Preliminary data

(2) In the second trimester of 2006, Venezuela was not a member of the Andean Community.

(3) Primarily reflects a telecommunication concession purchased by entities in Mexico and Spain in the Republic.

Sources: Central Bank, Superintendent of Companies and Superintendent of Banks.

THE FINANCIAL SYSTEM

The Central Bank

The Central Bank acts as the manager of the public sector's accounts and provides financial services to all public sector institutions that are required to hold their deposit accounts in the Central Bank. Management of these accounts primarily involves transfer operations between entities, including from the Government to other entities, and transfers to accounts in other banks, both foreign and domestic. The Central Bank is also the manager of the Republic's banking system. All domestic banks conduct their clearing operations through the Central Bank and hold their liquidity reserves at the Central Bank.

In addition, the Central Bank monitors economic growth and economic trends. To accomplish this task, the Central Bank has developed statistical and research methodologies to conduct analyses and policy recommendations on various economic issues.

The functions of the Central Bank were sharply reduced as a result of the Dollarisation Programme. The Central Bank no longer sets monetary policy or exchange rate policy for the Republic and the Ecuadorian economy is now directly affected by U.S. monetary policy, including U.S. interest rate policy. The LET, which made the U.S. dollar legal tender in the Republic, provided for the Central Bank to exchange, on demand, sucres at a rate of 25,000 sucres per 1 U.S. dollar. The LET also prohibited the Central Bank from incurring any additional sucre-denominated liabilities, and required that the Central Bank redeem on demand sucre coins and bank notes for U.S. dollars.

Pursuant to the new Constitution, the role of the Central Bank has changed further in that its authority and autonomy have decreased. In theory, the executive branch makes decision concerning monetary policy, and the Central Bank solely implements and advises in accordance with that policy.

The following table sets forth the composition of the Central Bank's balance sheet at December 31, 2008. The table reflects the four balances of the Central Bank - account one (the cash amount), account two (the financial reserve system), account three (the system of operations) and account four (other operations). The Central Bank adopted this presentation of its four balances following the implementation of the Dollarisation Programme.

Balance Sheet of the Central Bank
(in millions of U.S.\$)

	As of December 31, 2008⁽¹⁾
Account one (cash amount):	
Assets:	
Freely disposable international reserves	77.3
Liabilities:	
Currency in circulation	(77.3)
Account two (financial reserve system):	
Assets:	
Freely disposable international reserves	1,239.0
Liabilities:	
Bankers' deposits	(1,239.0)
Account three (system of operations):	
Assets:	
Remaining freely disposable international reserves	3,156.5
Government notes	571.5
Repurchase agreements	0
Total account three assets	3,728.0
Liabilities:	
Public sector deposits (non financial)	(3,718.4)
Obligations to multilateral financial institutions ⁽¹⁾	(3.6)
Central Bank U.S. dollar notes	0
Non-banking private sector deposits	(5.9)
Total account three liabilities	(3,727.9)
Account four (other operations):	
Assets:	
Other foreign assets ⁽²⁾	1,403.1
Other domestic assets	1,308.2
Total account four assets	2,711.3
Liabilities:	
Other liabilities ⁽³⁾	686.2
Capital and Reserves	1,754.8
Surplus due to Appraisals	116.3
Net Results	154.1
Total account four liabilities:	2,711.4
Total Freely Disposable International Reserve	4,472.8

(1) Corresponds to obligations assumed before IMF and FLAR.

(2) Includes contributions to international entities, *Andean Pesos*, and the collateral used for the Brady Bonds interests.

(3) Includes net results, currency adjustments, provisions and other liabilities.

Source: Central Bank.

Freely Disposable International Reserves

As of December 31, 2008, freely disposable international reserves were U.S.\$5.87 billion, a 28% increase from December 31, 2007. The increase was primarily the result of the increase in the market price of oil during the first two quarters of 2008.

The following table sets forth the freely disposable international reserves of the Central Bank as of the dates indicated.

Freely Disposable International Reserves
(in millions of U.S.\$)

	As of December 31,				
	2004	2005	2006	2007	2008
Assets:					
Gold	368	433	534	704	735
Cash	191	124	124	122	192
Deposits abroad	(13)	49	703	1,061	1,684

	As of December 31,				
	2004	2005	2006	2007	2008
Investments	806	1,495	628	1,580	1,836
Special drawing rights ⁽¹⁾	56	22	8	25	26
IMF reserve position	27	25	26	27	26
ALADI reserve position	2	(1)	0	2	(26)
Total assets	1,437	2,147	2,023	3,521	4,473

(1) A special drawing right is an international reserve asset, created by the IMF in 1969 to supplement the existing official reserves of member countries.
Source: Central Bank.

Inflation

The Republic measures the inflation rate by the percentage change between two periods in the CPI. The CPI is computed by the National Institute of Statistics based on a standard basket of 299 items of goods and services that reflects the pattern of consumption of urban Ecuadorian households in eight cities. The price for each good or service that makes up the basket of goods and services is weighted according to its relative importance in an average urban household's consumption pattern in order to calculate the CPI.

Prior to the adoption of the Dollarisation Programme, the Republic was plagued by high inflation. From 1994 to 1999, the inflation rate ranged from a low of 22.8% in 1995 to a high of 60.7% in 1999. In 1999 and early 2000, the sharp devaluation of the sucre contributed to an increase in the Republic's inflation rate, which reached 96.1% in 2000, one of the highest rates in Latin America.

The restrictions imposed by the Dollarisation Programme brought this to an end. The inflation rate decreased to 2.7% in 2004, 2.2% in 2005, 3.3% in 2006, 2.3% in 2007 and 8.4% in 2008. The increase in inflation in 2008 was primarily caused by increases in food prices due to climatic changes that affected the agricultural sector. In addition, international prices of fertilizer and agricultural commodities also increased. As a result of these increases, the Republic fixed the prices and limited the export of various agricultural products. For 2008, the Republic's rate of inflation was below the 9% average across the Americas. During January and February 2009, the monthly rate of inflation was 0.71% and 0.47%, respectively. Those percentages were significantly less than the rates registered during the same months of 2008 due to a decrease in commodity prices which began in the fourth quarter of 2008 as a result of reduced consumption.

Given the constraints of dollarisation, and the inability of the Republic to mint currency, the Republic is more vulnerable than other countries to external factors, such as the current global recession, the volatility of commodity and raw materials prices or natural disasters affecting the agricultural sector. The relative strength or weakness of the dollar relative to the currencies of the Republic's Andean trading partners also have affected the Republic's inflation rates during those periods.

The following table sets forth the rate of inflation in the Republic as measured by the CPI for the periods presented.

	% Change in CPI from Previous Year at Period End ⁽¹⁾
2004	1.95 ⁽²⁾
2005	3.46
2006	2.87
2007	3.33
2008	8.83

(1) The data reflect percentage change in consumer prices in urban areas over the twelve months ending on December 31 of each year.

(2) The methodology for calculating the CPI including the basket of goods analysed was changed as of December 2004. Therefore the result for 2004 is non-comparable with respect to subsequent periods.

Source: National Institute of Statistics.

Historical Interest Rates and Money Supply

Prior to the enactment of the Dollarisation Programme, the money supply consisted of bills and coins that were in circulation, or in deposit accounts held by the public at banking institutions. The enactment of the Dollarisation Programme has made it impossible to measure accurately the amount of currency in circulation, as the Central Bank is no longer the source of such currency.

The following table sets forth information regarding the average interest rates for the periods indicated.

Selected Interest Rates (in percentages)

	For the year ended December 31,			For the six months ended June 30,
	2004	2005	2006	2007 ⁽¹⁾
Central Bank stabilisation notes.....	2.15	2.99	2.92	5.18
Deposit interest rate.....	3.84	4.28	5.31	5.18
Average lending interest rate.....	7.48	8.59	9.27	9.89
Interest rate for other operations.....	12.94	11.72	10.93	11.29

(1) In July 2007, a new law went into effect which changed the interest rate methodology as discussed below.
Source: Central Bank.

In July 2007, the *Ley del Costo Máximo Efectivo del Crédito* went into effect to establish a new system for calculation of interest rates. The principal aspects of this law are:

- prohibition on charging commission for credit operations and pre-payments;
- prohibition on imposing any tariff that does not require the rendering of a service; and
- change in the methodology for calculating the maximum interest rate of the Central Bank, which methodology has since been declared unconstitutional and has been further amended so that the maximum rate equals the interest rates of credit operations of private financial institutions, in each relevant sector multiplied by an amount determined by the Central Bank.

As a direct consequence of the enactment of this law, both the active and passive interest rates have continuously decreased in all sectors of the economy. The Republic believes the new law marks a significant change to increase the transparency of the Government. The following table sets forth information regarding the average interest rates for the months indicated.

Active Interest Rates per Sector
(in percentages)

	<u>Aug 07⁽¹⁾</u>	<u>Sep 07</u>	<u>Oct 07</u>	<u>Nov 07</u>	<u>Dec 07</u>	<u>Dec 08</u>
Passive interest rate.....	5.53	5.61	5.63	5.79	5.64	5.09
Active interest rate.....	14.76	10.82	10.70	10.55	10.72	9.14
Active commercial interest rate.....	14.76	10.82	10.70	10.55	10.72	9.14
Maximum commercial interest rate.....	22.50	14.03	31.04	12.28	12.28	9.33
Pymes active commercial interest rate.....	N/A	14.17	14.10	13.31	13.15	11.13
Maximum pymes commercial interest rate.....	N/A	20.11	19.52	17.32	16.60	11.83
Active consumer interest rate.....	21.00	17.82	18.47	17.89	18.00	15.76
Maximum consumer interest rate.....	32.27	24.56	24.60	22.58	22.45	16.30
Active retail interest rate.....	N/A	25.92	24.96	21.17	21.23	18.55
Maximum retails interest rate.....	N/A	37.27	33.76	30.67	30.67	21.24
Active housing interest rate.....	12.90	11.50	12.15	12.19	12.13	10.87
Maximum housing interest rate.....	17.23	14.77	14.88	14.04	14.04	11.33
Active ref. microcredit increased accumulation interest rate...	23.90	23.06	24.75	23.27	23.50	22.91
Maximum microcredit increased accumulation interest rate...	41.86	30.30	31.97	31.80	30.85	25.50
Active ref. microcredit simple accumulation interest rate.....	N/A	31.41	36.24	34.04	31.55	29.16
Maximum microcredit simple accumulation interest rate.....	N/A	43.85	50.86	50.57	49.91	33.30
Active ref. microcredit subsistence interest rate.....	N/A	40.69	42.90	35.06	41.47	31.84
Maximum microcredit subsistence interest rate.....	N/A	45.93	48.21	48.21	48.21	33.90

(1) In July 2007, a new law went into effect which changed the interest rate methodology as discussed above.

Source: Central Bank.

Structure of the Financial System

Supervision of the Financial System

The financial sector consists of various financial institutions and the securities markets in accordance with the *Ley de Régimen Monetario y Banco del Estado*. The Superintendent of Banks regulates financial institutions, and the securities markets are regulated by the *Consejo Nacional de Valores* (“National Securities Commission” or the “CNV”). The *Ley General de Instituciones del Sistema Financiero* of 2004 (the “Financial Institutions Law”) regulates all private sector financial institutions, including banks, finance companies, savings and loan cooperatives, leasing companies, credit card issuers, brokerage houses and insurance companies. The Financial Institutions Law regulates public sector and private financial institutions with respect to their solvency, liquidation, financial prudence and other administrative matters.

The Ecuadorian banking system is composed of the Central Bank, private commercial banks and several state development and state-owned banks. As of December 31, 2008, Citibank Ecuador S.A. and Lloyds Bank, Ecuador were the only foreign banks operating in the Republic.

The Financial Institutions Law permits the establishment of universal banks (banks that can offer all types of banking services) and provides for equal treatment of foreign and domestic financial institutions. Ecuadorian financial institutions may establish foreign offices and invest in foreign financial institutions with the authorisation of the Superintendent of Banks. Foreign subsidiaries of Ecuadorian financial institutions must also conform to the guidelines established by the Financial Institutions Law to promote prudent banking and investment policies and ensure financial solvency. Each year, external auditors must provide opinions regarding capital adequacy, concentration of loans, interested debtors and asset risk classifications on both unconsolidated and consolidated

bases for all banks. The Republic believes that the Financial Institutions Law is consistent with the banking supervision guidelines established by the Basel Committee on Banking Supervision.

The Financial Institutions Law designates the Superintendent of Banks as the principal regulatory authority for the Republic’s financial system. The Superintendent of Banks is concerned primarily with prudential matters, including the capital adequacy, liquidity, earnings, management risks, solvency, and risk asset quality of financial institutions. The Superintendent of Banks is headed by a Banking Board. The Banking Board is composed of five members: the Superintendent of Banks, the General Manager of the Central Bank, two members appointed by the President and a final member appointed by the four other members.

Since the crisis of the banking system in the late 1990s during which a number of banks became insolvent, the Superintendent of Banks has worked to improve banking supervision standards. Since 2001, the Superintendent of Banks reformed the regulatory framework for banking supervision. As part of the reforms the Superintendent of Banks implemented measures that included the following:

- a capital adequacy ratio that requires capital and reserves as a percentage of risk-weighted assets to equal at least 9%;
- programmes for regulatory on-site audits and periodic reporting requirements that are published in national newspapers intended to ensure that banks comply with regulatory standards;
- uniform accounting risks for the financial system;
- evaluation of market risk based on:
 - liquidity risk, which derives from the incapacity of financial institutions to cover their liabilities and other obligations when due, in both local and foreign currency; and
 - interest rate risk, which refers to the potential losses of net income or in the capital base due to the incapacity of the institution to adjust the return on its productive assets (loan portfolio and financial investment) with the fluctuations in the cost of its resources produced by changes in interest rates; and
- a detailed method for classifying financial assets in terms of risk.

This method increased the amounts financial institutions are required to reserve in order to mitigate potential losses arising from their loans (“loan-loss reserves”). With respect to loan-loss reserves, current regulations impose reserve requirements based on risk categories and type of financial assets. These requirements have been introduced to bring them inline with international standards and to increase the average quality of the financial system’s loan portfolio.

The following table sets forth information regarding the risk categories and loan-loss reserve requirements currently in effect.

Risk Categories and Required Loan-loss Reserves
(in numbers of days past due, except for percentages)

Category	Commercial ⁽¹⁾	Consumer ⁽²⁾	Mortgage	Small Business ⁽²⁾	Loan-loss Reserve
A	0-30	0-15	0-90	0-5	1%-4%
B	30-90	15-45	90-270	5-30	5%-19%
C	90-180	45-90	270-360	30-60	20%-49%
D	180-270	90-120	360-720	60-90	50%-99%
E	>270	>120	>720	>90	100%

(1) For commercial loans, in addition to the number of days due, five factors are considered for classification among risk categories: debtor payment capacity, coverage and propriety of guarantees, risk information from the system (debtor’s file), debtor’s credit history and market risk and economic

environment. The risk categories contained in this chart apply to loans in amounts up to U.S.\$25,000. For loans of more than U.S.\$25,000, borrower's payment capacity, collateral and other factors need to be considered to define risk categories.

(2) Additional loan-loss reserves are required for consumer and small business loans because of the default rate on these loans.

Source: Superintendent of Banks.

The following table sets forth information regarding loans of the banking system by risk category as of December 31, 2008.

Classification of Aggregate Assets of the Ecuadorian Private Financial System
(as a % of total loans)

Category	As of December 31, 2008				
	Commercial loans	Consumer loans	Mortgage loans	Small business loans	Total
A	95.59%	95.67%	95.07%	98.70%	95.94%
B	2.09	1.78	2.24	0.64	1.83
C	1.21	1.05	1.15	0.09	1.02
D	0.55	0.33	0.42	0.39	0.45
E	0.55	1.17	1.12	0.18	0.76
Total	100.00%	100.00%	100.00%	100.00%	100.00%

Source: Superintendent of Banks.

The Agencia de Garantía de Depósitos

AGD was previously responsible for insuring the accounts of depositors in the Republic's banking systems. It was created as a response to the banking crisis of 1999 by the *Ley de Reordenamiento en Materia Económica en el área Tributario - Financiera* ("LME"). The AGD had a dual role: to oversee the amounts the Government deposited with the Central Bank to protect depositors and to help restructure banks in liquidation. As of January 1, 2009, the COSEDE, pursuant to the Law of Creation of Financial Safety Net, will oversee the deposit insurance scheme. The AGD will cease to exist on December 31, 2009. If on the date of termination the AGD has not resolved any regulatory matters related to specific financial institutions, the AGD will be able to execute its role for an additional six months or the Minister of Finance will assume its responsibilities regarding pending resolutions. The AGD continues to liquidate the assets of the fourteen banks which failed as a result of the downturn in 1999. There is some uncertainty as to which entity will have responsibility for any future bank failures.

AGD Sources of Liquidity

Prior to the enactment of the LET, financing for the provision of liquidity to capitalise financial institutions or for payment of guaranteed deposits was obtained by the AGD through the use of repurchase agreements. Upon request by the AGD, the Ministry of Finance issued an aggregate of U.S.\$1.4 billion of AGD notes that originally accrued monthly interest at a rate of 12.0% per year and had a maturity of 15 years (the interest rate on the AGD notes was changed to 9.35% in March 2000). These notes were purchased by the Central Bank and the funds from this transaction were provided to the AGD. Upon transfer of these notes to the Central Bank the AGD notes became obligations of the Ministry of Finance. The Ministry of Finance is entitled to receive money from the AGD from the liquidation of the AGD's assets to satisfy the Ministry of Finance's obligations with respect to the AGD notes. Earlier this year, the AGD notes were assigned to the Ministry of Finance at a 100% discount and were replaced by a common fund sourced by private banks as part of a new deposit insurance regulation.

Since the fourth quarter of 2002, the AGD's primary source of liquidity was income generated from its portfolio recovery process (including the sale of assets of liquidated financial institutions). As of December 31, 2008, the AGD had total assets of approximately U.S.\$550 million and liabilities of approximately U.S.\$1.2 billion.

Bank Resources

The following table sets forth information for the private banking system as of the dates indicated.

Private Bank Deposits (in millions of U.S.\$, except for percentages)

As of December 31,	Demand Deposits	Time Deposits	Total Deposits ⁽¹⁾	Annual Growth Rate of Deposits	Growth Rate of Deposits 2004-2008
2004	4,438	1,916	6,377	24%	N/A
2005	5,334	2,370	7,750	21%	N/A
2006	6,252	2,786	9,147	18%	N/A
2007	7,286	3,167	10,649	16%	N/A
2008	9,068	3,902	13,171	24%	106.5%

(1) These data include demand deposits, time deposits, reported operations, guarantee deposits and restricted deposits.
Source: Superintendent of Banks.

Banking deposits constitute the principal source of financing for the banking system. From December 31, 2004 through December 31, 2008, total deposits increased 106.5%, and those deposits constitute the principal source of financing for the banking system. Between December 31, 2004 and December 31, 2008, time deposits increased 104.3% from U.S.\$2.27 billion to U.S.\$3.84 billion. The lack of availability of financing from time deposits (as compared to demand deposits) made it somewhat difficult for the Republic's commercial banks to lend to borrowers that required medium and long-term financing. This difficulty has been less prevalent since 2002, as time deposits have gradually increased.

Foreign banks and financial institutions are also a source of liquidity in the Ecuadorian banking system. As of December 31, 2008, the balance of foreign liabilities in the banking sector amounted to approximately U.S.\$793 million, which was approximately U.S.\$102 million more than as of December 31, 2007. In accordance with the preliminary projections of the Central Bank, banking deposits will increase by 11.1% during 2009.

The following table sets forth information regarding the principal sources of financing with respect to total liabilities as of the dates indicated.

Classification of the Main Financing Accounts with Respect to Liabilities (as % of total liabilities)

As of December 31,	Demand Deposits	Time Deposits	Foreign Financing
2004	61%	26%	5%
2005	60%	27%	5%
2006	59%	26%	5%
2007	59%	26%	5%
2008	62%	27%	5%

Source: Superintendent of Banks.

The Republic's banks primarily use their resources to extend loans. Between 2004 and 2008, the Ecuadorian banking system's total loan portfolio increased by U.S.\$5.4 billion (135.7%), and past due loans decreased U.S.\$33 million (12%). Banks can lend only when they have at least a 70% loan to value ratio.

The following table sets forth information regarding the banking system's loan portfolio as of the dates indicated.

Banking System Loan Portfolio Balances
(in millions of U.S.\$, except for percentages)

<u>As of December 31,</u>	<u>Current Loans</u>	<u>Past-Due Loans</u>	<u>Total Loan Portfolio</u>	<u>Current Loans as a Percentage of the Total Loan Portfolio</u>	<u>Past-Due Loans as a Percentage of the Total Loan Portfolio</u>
2004	3,986	274	4,260	93.6%	6.4%
2005	5,169	266	5,435	95.1%	4.9%
2006	6,565	224	6,789	96.7%	3.3%
2007	7,355	216	7,571	97.1%	2.9%
2008	9,394	241	9,635	97.5%	2.5%

Source: Superintendent of Banks.

As of December 31, 2004, 6.4% of all loans in the banking system's total loan portfolio were past-due loans. Since 2005, the banking system's delinquency rate has gradually improved, and past-due loans represented 4.9%, 3.3%, 2.9% and 2.5% of the banking system's total loan portfolio as of December 31, 2005, 2006, 2007 and 2008, respectively. The improvement of the financial portfolio has been due to economic stability and growth, which has allowed an increase of the financial portfolio with a low level of risk. As of December 2008, 48.9% of all current loans were commercial, 28.9% were consumer, 13.7% were housing and 8.5% were microcredit.

The following table sets forth information regarding the number of past-due loans in different sectors of the economy as of the dates indicated.

Past Due Loans by Sector of the Economy
(in millions of U.S.\$ and as a percentage of past due loans)

	As of December 31,			
	2004		2008	
	U.S.\$	%	U.S.\$	%
Commercial.....	184	67.2	82	34.0
Consumer.....	68	24.8	107	44.4
Real estate.....	12	4.4	15	6.2
Small business.....	10	3.6	37	15.4
Total.....	<u>274</u>	<u>100.0%</u>	<u>241</u>	<u>100.0%</u>

Source: Superintendent of Banks.

The following table identifies the number of financial institutions regulated by the Superintendent of Banks as of the dates indicated.

Number of Financial Institutions

	As of December 31,				
	2004	2005	2006	2007	2008
Private Banks.....	25	25	24	24	25
National Banks.....	23	23	22	22	23
Private.....	22	22	21	21	22
Gov. Owned Banks	1	1	1	1	1
Foreign Banks.....	2	2	2	2	2
Other Financial Entities.....	53	59	58	59	55
Development Banks.....	32	39	38	39	37
Small Lending Inst.....	6	5	5	5	4
Savings and loans					
Associations.....	11	11	11	11	10
Public Banks.....	4	4	4	4	4
Insurance Companies.....	41	41	42	45	45
Insurance Companies.....	39	39	40	43	43
Reinsurance Companies..	2	2	2	2	2
Total.....	<u>119</u>	<u>125</u>	<u>124</u>	<u>128</u>	<u>125</u>

Source: Superintendent of Banks.

The following table identifies the loans made to the private sector and the deposits of the private sector as of the dates indicated.

Loans to the Private Sector and Private Sector Deposits
(in millions of U.S.\$)

	As of December 31, 2008	
	Loans	Deposits
Commercial banks.....	9,396	12,754
Government owned financial institutions ⁽¹⁾	1,522	576
Financial Institutions.....	812	527
Small lending institutions.....	230	318
Savings and loan associates.....	1,277	1,162
Foreign banks.....	239	417
Credit card-issuing entities.....	101	32
Total.....	<u>13,577</u>	<u>15,786</u>

(1) This includes development banks and mortgage banks.

Source: Superintendent of Banks.

The following table sets forth information regarding the allocation of principal asset accounts, with respect to total assets of the banking system as of the dates indicated.

**Allocation of the Principal Asset Accounts, with respect to Total Assets
Of the Banking System
(as a % of total assets)**

<u>As of December 31,</u>	<u>Portfolio of Current Loans</u>	<u>Investments</u>	<u>Foreign Investments</u>
2004	48%	38.1%	26.2%
2005	51	37.0	28.1
2006	54	35.2	27.5
2007	52	37.0	27.1
2008	55	35.3	22.8

Source: Superintendent of Banks.

As of December 31, 2008, the banking system represented 85% of the total assets of the private financial system. The banking system for the year ended December 31, 2008, realised a profit of U.S.\$283 million, which represented 13.3% of the Republic's total revenues and 0.54% of the Republic's nominal GDP. For the first two months of 2009, the profits of the banking system were U.S.\$38.3 million, and the Republic expects the profits of the banking system to decrease by approximately 30% in 2009 as compared to 2008. The banking system strengthened between 2007 and 2008, and the assets grew by 19.6% due to a 24% growth in deposits.

New Financial Safety Net

President Correa's administration determined that the financial safety net in place when President Correa took office was insufficient because there was no lender of last resort, the only Government response to a failing financial institution was liquidation, and there was insufficient deposit insurance.

Usually central banks act as lenders of last resort. Due to the Dollarisation Programme, however, the Ecuadorian Government's lending capacity was limited to the *Fondo de Liquidez del Sistema Financiero Ecuatoriano* (the "Liquidity Fund"), which, in December 2008, had only US\$155.5 million, or less than 1.2% of total banking deposits. President Correa's administration believed that the lack of a lender of last resort, increased the risks to the financial system and decreased liquidity within the system.

In respect of the banking resolution mechanism, Ecuadorian laws did not contemplate any efficient banking resolution mechanisms. In practice the only resolution for a failing financial institution was liquidation.

In light of these perceived deficiencies, the Republic passed the Financial Safety Net Law in December 2008. The new law created a four-tiered framework for the banking sector.

Lender of the last resort

In accordance with the Financial Safety Net Law, the Liquidity Fund acts as a lender of last resort for financial institutions. The Law was designed to strengthen the Liquidity Fund without reducing available funds in the banking system. Accordingly, contributions of the financial entities to the Liquidity Fund offset reductions in other mandatory contributions. We estimate that in the medium term the Liquidity Fund would represent between 10% of total banking deposits (approximately US\$1.2 billion) and the net capital of the Ecuadorian banking system (approximately US\$1.7 billion). As of March 31, 2009, the Liquidity Fund had approximately US\$408 million. The Superintendent of the Banks oversees and the Central Bank administers the Liquidity Fund.

Banking Resolution Scheme

The second tier of the Financial Safety Law is the creation of a banking resolution scheme called Exclusion and Transfer of Assets and Liabilities (*Exclusion y Transferencia de Activos y Pasivos*), or ETAP. Under ETAP

more healthy labour contingencies, deposits and assets can be excluded from the balance sheet of a troubled banking institution and transferred to a newly created entity or to one or more healthy banking institutions.

COSEDE

The third tier of the Financial Safety Law consists of the *Corporación Seguro de Depositos*, or COSEDE. In accordance with the Law and Resolution number JB-2009-1280, COSEDE administers the insurance deposit system of private financial institutions. COSEDE insures deposits up to US\$20,000.00 per account, whereas AGD could only guarantee up to US\$12,000.00 per account. At the moment, COSEDE holds approximately US\$140 million. In accordance with the Financial Safety Net Law, banks will be required to contribute to COSEDE an amount determined annually in accordance with the total amount of deposits held.

Superintendent of Banks

The fourth tier of the Financial Safety Law is that the Superintendent of Banks is authorised to increase the capital and reserves requirements of banking institutions.

Furthermore, the Superintendent of Banks is in charge of supervising the liquidation process of the banks that went bankrupt in 1999. This process must conclude by December 31, 2009.

National Assembly and President Correa have issued and promulgated all the regulations and resolutions required for the implementation of the Financial Safety Net Law.

Capital Markets

The Republic's capital markets have grown in recent years as the financial system has been modernised. Retail trading of debt and equity securities of private Ecuadorian issuers, however, has remained relatively limited. Most of the trading on the Republic's capital markets involves the purchase and sale of fixed income and government securities. The Ecuadorian capital markets consist of the Quito Stock Exchange and the Guayaquil Stock Exchange, both of which opened in 1969. As of December 31, 2008, the Quito Stock Exchange and the Guayaquil Stock Exchange listed approximately 165 issuers in total. Issuers that subscribe to one exchange automatically become listed on the other exchange.

The Ecuadorian capital markets are regulated by the *Ley de Mercado de Valores* (the "Capital Markets Law"). Under the Capital Markets Law, the stock exchanges are supervised by the CNV. The CNV is comprised of seven members, four from the public sector and three from the private sector. The CNV is responsible for formulating the general securities policies of the Ecuadorian capital markets and for regulatory oversight of those markets.

PUBLIC SECTOR FINANCES

General

The Non-Financial Public Sector Budget

The Constitution, the Budget Law of 1992, the Organic Financial Administration and Control Law of 1977 and the Organic Responsibility, Stabilisation and Fiscal Transparency Law of 2002 set forth the public sector's budget process. The Government (including the executive, legislative and judicial branches, special accounts, the Electoral Court and the Constitutional Court), the Social Security Institute ("IESS"), national defence services, local governments, publicly-owned companies (including Banco del Estado) and universities constitute the non-financial public sector. The Central Bank and the state development banks comprise the financial public sector.

Pursuant to the Constitution, the executive branch of the Government is required to prepare an annual budget that is designed to permit the implementation of the Government's social and economic development policies and the provision of public services. The levels of revenue, expenditure and debt are determined on the basis of the Government's macroeconomic projections and targets. The Ministry of Finance is primarily responsible for the preparation of the public sector's annual budget, based on guidelines issued by various planning agencies and other Ministries.

The Government's annual budget is required to include the revenues and expenditures of the non-financial public sector, excluding the IESS, autonomous agencies and state-owned companies. The Ministry of Finance prepares the Government's annual budget, which is forwarded to the President for informational purposes. The budget is simultaneously sent to the National Assembly for its approval. In accordance with the restrictions set in the Public Sector Budget Law of 1992 and other applicable legal provisions, the Ministry of Finance has the authority to modify the budget during its execution phase.

Provincial and local governments prepare their budgets in accordance with the guidelines prepared by the *Secretaria Nacional de Planificación y Desarrollo* (the "National Secretary of Planning and Development" or "SENPLADES," formerly "ODEPLAN") but are not bound by these guidelines since the Constitution granted autonomy to local and municipal governments. The mayor or prefect of each of these subdivisions is responsible for drafting the budget and submitting it for approval before the corresponding legislative bodies. The local budgets, upon approval, are made public and are implemented by the respective local governments. Local governments are responsible for sending a copy of their annual budgets to the Ministry of Finance for reference.

In 2002, in response to increasing Government expenditures, Congress enacted the Law to Promote Responsibility, Stabilisation and Fiscal Transparency, which was aimed at reducing public indebtedness and establishing greater transparency in the Government's use of public funds. During the second half of 2005, the Government, with the support of Congress, replaced the FEIREP that was previously created by the 2002 Law. FEIREP was replaced by CEREPS. This resulted in an increase in Government investment in social and productive sectors of the economy to strengthen the economic performance while limiting the current expenses.

During 2008, the Law to Promote Responsibility, Stabilisation and Fiscal Transparency was amended. CEREPS was eliminated due to the enactment of the *Ley Orgánica para la Recuperación del Uso de los Recursos Petroleros del Estado y Racionalización Administrativa de los Procesos de Endeudamiento* ("LOREYTF") and by the new Constitution. The Republic believes that the new law enhances transparency and flexibility to the budget process by providing enhanced management of state resources and prioritising social investments. The law also eliminated all predetermined use of resources; currently all of the Republic's resources go directly to a single account. In accordance with the terms of the new Constitution and, the macro economic rules and the restrictions on the assumption of public debt were changed as follows:

- permanent expenditures must be financed by permanent income; expenditures related to health, education and justice will be treated as preferential and may be financed by non-permanent income;

- public debt of income from petroleum products may not be used for current Government expenditures; and
- the Ministry of Finance will apply a continuous reduction in public debt, including external indebtedness, until the ratio of public debt to GDP reaches 40%.

Non-Financial Public Sector Accounts

In 2004, the non-financial public sector registered a surplus of U.S.\$707 million (equivalent to 1.9% of GDP). The surplus was primarily attributable to a significant increase in total revenues, which outweighed the minimum increase in total expenditures. In the same year, the oil revenues increased by approximately 27%, totalling U.S.\$2.11 billion (equivalent to 5.8% of GDP) due to an increase in the market price for oil. The non-oil revenues totalled U.S.\$5.72 billion (equivalent to 15.8% of GDP), and the tax revenue totalled U.S.\$3.59 billion (equivalent to 9.8% of GDP). The income arising from social security contributions totalled U.S.\$1.02 billion (equivalent to 2.8% of GDP). Total revenues were U.S.\$8.18 billion (equivalent to 22% of GDP).

In 2005, the non-financial public sector registered a surplus of U.S.\$266 million (equivalent to 0.7% of GDP). The surplus was primarily attributable to an increase in tax revenues, which totalled U.S.\$4.28 billion (equivalent to 11.5% of GDP). The total revenues in 2005 totalled U.S.\$9.14 billion (equivalent to 24.2% GDP). The total expenditures in 2005 totalled U.S.\$8.74 billion (equivalent to 23.5% GDP).

In 2006, the non-financial public sector registered a surplus of U.S.\$1.51 billion (equivalent to 3.6% of GDP). This was due to the approval of the amendment to the Hydrocarbons Law; the declaration by the Ministry of Energy and Mines of the early termination of the Republic's contract with Occidental Petroleum; and the enactment of the *Ley Orgánica de Creación del Fondo Ecuatoriano de Inversión en los Sectores Energético e Hidrocarburífero* ("FEISEH"), which created a trust to capture funds from the oil extracted on Block 15. In 2006, total revenues totalled U.S.\$11.34 billion (equivalent to 27.2% of GDP). Total expenditures totalled U.S.\$9.86 billion (equivalent to 23.6% of GDP).

In 2007, the non-financial public sector registered a surplus of U.S.\$948 million (equivalent to 2.1% GDP), a decrease of 37.21% as compared to 2006. The decrease in the surplus was primarily attributable to an increase in the total expenditures, due to an increase in public investments. In 2007, total expenditures totalled U.S.\$12.33 billion (equivalent to 26.9% GDP). Total revenues totalled U.S.\$13.21 billion (equivalent to 28.9% GDP). In 2007, the net result totalled U.S.\$1.80 billion (equivalent to 3.9% GDP).

In 2008, the fiscal statistics differed from prior years as a consequence of the following items that affected revenues and expenditures:

- in December 2007, the Constitutional Assembly enacted the *Ley Reformativa para la Equidad Tributaria en el Ecuador*, which eliminated the designated purposes for income tax revenues;
- as of March 2008, the expenditures incurred in the *Cuenta de Financiamiento de Importación de Derivados* were included in the general government budget; and
- in April 2008, the Constitutional Assembly enacted a new law which moved oil income to the central government's budget.

In 2008, the non-financial public sector registered a deficit of U.S.\$604.2 million (equivalent to 1.1% GDP). The deficit was primarily attributable to a significant investment in capital, which totalled U.S.\$7.23 billion (equivalent to 13.8% GDP). Total revenues increased to U.S.\$22.35 billion (equivalent to 42.5% GDP). The net result totalled U.S.\$122 million (equivalent to 0.2% GDP).

The following table sets forth actual revenues and expenditures for the consolidated non-financial public sector for the periods presented.

Summary of Consolidated Non-financial Public Sector Revenues and Expenditures ⁽¹⁾
(in millions of U.S.\$, and as a % of GDP)

	As of and for the year ended December 31,									
	2004	% of GDP	2005	% of GDP	2006	% of GDP	2007	% of GDP	2008 ⁽²⁾	% of GDP
Petroleum Revenue:										
Exports	1,638	4.5	2,133	5.7	3,232	7.7	3,318	7.2	8,899	16.9
Domestic sales	478	1.3	78	0.2	0	0	0	0	0	0
Total petroleum revenue	2,116	5.8	2,211	5.9	3,232	7.7	3,318	7.2	8,899	16.9
Tax Revenue:										
Income and profits	880	2.4	1,186	3.2	1,453	3.5	1,689	3.7	2,360	4.5
Value-added tax	1,887	5.1	2,167	5.8	2,445	5.9	2,753	6.0	3,104	5.9
Specific consumption taxes	270	0.7	308	0.8	345	0.8	349	0.8	474	0.9
International trade taxes	470	1.3	561	1.5	638	1.5	700	1.5	816	1.6
Other taxes	88	0.2	62	0.2	72	0	74	0	143	0.3
Total tax revenue	3,595	9.7	4,284	11.5	4,953	11.7	5,565	12.0	6,897	13.2
Social security contributions	1,024	2.8	1,109	2.9	1,555	3.7	1,795	3.9	2,077	4.0
Other	1,105	3.0	1,306	3.5	1,641	3.9	1,887	4.1	2,972	5.7
Public enterprises operating result	338	0.9	104	0.3	(36)	0	644	1.4	919	1.7
Total revenues	8,178	22.2	9,014	24.1	11,345	27.0	13,209	28.6	21,764	41.5
Current expenditure:										
Interest accrual:										
Foreign	623	1.7	662	1.8	752	1.8	764	1.7	685	1.3
Domestic	174	0.1	145	0.4	144	0.3	96	0.2	41	0.1
Total interest accrual	797	1.8	807	2.2	896	2.1	860	1.9	726	1.4
Wages and salaries	2,586	7.1	2,906	7.8	3,161	7.6	3,692	8.1	4,841	9.2
Purchases of goods and services	1,032	2.8	1,137	3.1	1,506	3.6	1,575	3.4	2,043	3.9
Social security benefits	665	1.8	1,184	3.2	1,226	2.9	1,276	2.8	1,507	2.9
Other	778	2.1	883	2.4	1,128	2.7	1,503	3.3	5,987	11.4
Total current expenditure	5,858	15.6	6,917	18.7	7,917	18.9	8,906	19.5	15,104	28.8
Capital expenditure and net lending:										
Fixed capital formation:										
Central government	710	1.9	829	2.2	829	2.0	1,670	3.6	4,308	8.2
Rest of general government	592	1.6	708	1.9	724	1.7	965	2.1	1,593	3.0
Public enterprises	299	0.8	284	0.7	348	0.8	561	1.2	1,233	2.3
Total fixed capital formation	1,601	4.3	1,821	4.8	1,901	4.5	3,196	6.9	7,134	13.5
Other capital expenditures	11	0	10	0	43	0	233	0.5	109	0.2
Total capital expenditure and net lending	1,612	4.3	1,831	4.8	1,944	4.5	3,429	7.4	7,243	13.7
Total expenditure	7,470	19.9	8,748	23.5	9,861	23.4	12,335	26.9	22,347	42.5
Adjustment on treasury accounts	0	0	0	0	(28)	(0.1)	(73)	(0.2)	0	0
Fiscal Balance, surplus/(deficit)	707	1.9	266	0.7	1,510	3.6	948	2.1	(604)	(1.1)
Primary Balance, surplus/(deficit) ⁽³⁾	1,503	4.1	1,073	2.9	2,407	5.8	1,809	3.9	121.6	0.2

(1) Revenues are cash; expenditures are accrued.

(2) Preliminary data.

(3) These data reflect the fiscal Balance plus interest on the public debt.

Source: Ministry of Finance.

Government Accounts

The following table shows the principal categories of Government revenues and expenses for the periods indicated.

Summary of Consolidated Central Government Sector Revenues and Expenditures⁽¹⁾ (in millions of U.S.\$, and as a % of GDP)

	As of and for the year ended December 31,									
	2004	% of GDP	2005	% of GDP	2006	% of GDP	2007	% of GDP	2008	% of GDP
Petroleum revenue ⁽²⁾	1,558	4.3	1,567	4.2	1,603	3.8	1,764	3.9	4,642	8.8
Tax revenue:										
Taxes on income and profits.....	702	1.9	937	2.5	1,068	2.6	1,268	2.8	2,339	4.4
Taxes on property.....	56	0.2	60	0.2	70	0.2	72	0.2	95	0.2
Taxes on goods and services:										
Value-added tax.....	1,720	4.7	1,975	5.3	2,228	5.3	2,509	5.5	2,825	5.4
Selected excise taxes.....	202	0.6	221	0.6	257	0.6	220	0.5	474	0.9
Total taxes on goods and services ..	1,922	5.3	2,196	5.9	2,485	5.9	2,729	6.0	3,299	6.3
Taxes on international trade:										
Import duties.....	454	1.2	547	1.5	618	1.5	679	1.5	834	1.6
Exit tax.....	0	0	0	0	0	0	0	0	44	0.1
Total taxes on international trade.....	454	1.2	547	1.5	618	1.5	679	1.5	878	1.7
Other taxes.....	32	0.1	2	0	3	0	3	0	4	0
Total tax revenue.....	3,166	8.7	3,742	10.1	4,244	10.2	4,751	10.5	6,615	12.6
Non-tax revenue.....	445	1.2	356	1.0	452	1.1	505	1.1	969	1.8
Transfers.....	10	0	387	1.0	480	1.1	1,471	3.2	1,618	3.0
Total revenues.....	5,179	14.2	6,052	16.3	6,779	16.2	8,491	18.7	13,844	26.2
Current expenditure:										
Wages and salaries.....	2,049	5.6	2,299	6.2	2,581	6.2	2,914	6.4	3,929	7.5
Purchase of goods and services.....	363	1.0	355	1.0	458	1.1	537	1.2	845	1.6
Interest payments.....	814	2.2	855	2.3	941	2.3	915	2.0	797	1.5
of which: on domestic debt.....	215	0.6	225	0.6	228	0.5	182	0.4	145	0.3
Current transfers.....	591	1.6	722	1.9	775	1.9	800	1.7	1,880	3.6
Other current expenditures:										
Solidarity Bond.....	173	0.5	172	0.5	185	0.4	389	0.8	432	0.8
Other.....	114	0.3	317	0.9	401	1.0	445	1.0	603	1.1
Total other current expenditures.....	287	0.8	489	1.4	586	1.4	834	1.8	1,035	1.9
Total current expenditure.....	4,104	11.2	4,720	12.8	5,341	12.9	6,000	13.1	8,486	16.1
Capital expenditure:										
Fixed capital expenditure.....	710	1.9	829	2.2	829	2.0	1,670	3.6	4,308	8.2
Capital transfers.....	658	1.8	671	1.8	814	1.9	956	2.1	1,293	2.5
Other.....	27	0	12	0	26	0	0	0	0	0
Capitalisation of liquidity fund.....	0	0	0	0	0	0	0	0	0	0
Total capital expenditure.....	1,395	3.7	1,512	4.0	1,669	3.9	2,626	5.7	5,601	10.7
Total expenditure.....	5,499	14.9	6,232	16.8	7,010	16.8	8,626	18.8	14,087	26.8
Discrepancy (unrecorded operations).....	0	0	0	0	(28)	(0.1)	(73)	(0.2)	0	0
Overall surplus or deficit.....	(320)	(0.7)	(180)	(0.5)	(231)	(0.6)	(135)	(0.1)	(243)	(0.6)

(1) Revenues are cash; expenditures are accrued.

(2) These data include transfers of 10% of FEIREP funds for social expenditures 20% of FEIREP fund for the stabilisation of oil revenues.

Source: Ministry of Finance.

The increase in deficit between 2007 and 2008 was primarily the result of a significant increase in total expenditure that was not setoff by the slightly less significant increase in total revenues. The Government's fixed capital expenditure increased by 158.0% between those two years.

Government Revenues

The Government derives its revenues primarily from:

- sales of petroleum;
- tax collection and import duties; and
- other revenue, including transfers.

In 2004, Government revenues totalled U.S.\$5.18 billion (equivalent to 14.1% GDP), of which U.S.\$1.56 billion (equivalent to 4.3% GDP) corresponds to petroleum revenue, U.S.\$3.17 billion (equivalent to 8.6% GDP) corresponds to tax revenue, U.S.\$445 million (equivalent to 1.2% GDP) corresponds to non-tax revenue and U.S.\$10 million (equivalent to approximately 0% of GDP) in respect of transfers received.

In 2005, Government revenues increased to U.S.\$6.05 billion (equivalent to 16.3% GDP), of which U.S.\$1.57 billion (equivalent to 4.2% GDP) corresponds to petroleum revenue, U.S.\$3.74 billion (equivalent to 10.1% GDP) corresponds to tax revenue, U.S.\$356 million (equivalent to 1.0% GDP) corresponds to non-tax revenue and U.S.\$387 million (equivalent to 1% of GDP) in respect of transfers received.

In 2006, total Government revenues increased to U.S.\$6.78 billion (equivalent to 16.2% GDP), of which U.S.\$1.60 billion (equivalent to 3.8% GDP) corresponds to petroleum revenue, U.S.\$4.24 billion (equivalent to 10.2% GDP) corresponds to tax revenue, U.S.\$452 million (equivalent to 1.1% GDP) corresponds to non-tax revenue and U.S.\$480 million (equivalent to 1.1% of GDP) in respect of transfers received.

In 2007, total Government revenues increased to U.S.\$8.49 billion (equivalent to 18.5% GDP), of which U.S.\$1.76 billion (equivalent to 3.9% GDP) corresponds to petroleum revenue, U.S.\$4.75 billion (equivalent to 10.4% GDP) corresponds to tax revenue, U.S.\$505 million (equivalent to 1.1% GDP) corresponds to non-tax revenue and U.S.\$1.47 billion (equivalent to 3.2% of GDP) in respect of transfers received.

In 2008, total Government revenues increased to U.S.\$13.80 billion (equivalent to 26.2% GDP), of which U.S.\$4.64 billion (equivalent to 8.8% GDP) corresponds to petroleum revenues, U.S.\$6.57 billion (equivalent to 12.5% GDP) corresponds to tax revenue, U.S.\$969 million (equivalent to 1.8% GDP) corresponds to non-tax revenue and U.S.\$1.61 billion (equivalent to 3.0% of GDP) in respect of transfers received.

Government Expenditures

Government expenditures are principally divided into current expenditures and capital expenditures.

The Constitution requires that 15% of current Government revenues (based on the Government's annual budget) and at least 5% of the non-permanent revenues be allocated to provincial and municipal governments.

In 2008, Government expenditures (excluding amortisation payments of public debt) were U.S.\$14.4 billion (equivalent to 27.4% GDP), compared to U.S.\$8.6 billion (equivalent to 23% GDP) in 2007 and U.S.\$7 billion (equivalent to 12.4% GDP) in 2006. In 2004 and 2005 Government expenditures (excluding amortisation payments of public debt) were U.S.\$5.49 billion (equivalent to 15% GDP) and U.S.\$6.23 billion (equivalent to 16.8% GDP), respectively.

Distribution of the Petroleum Revenues

The following table illustrates the average price of international sales of Ecuadorian petroleum from 2004 to December 2008.

Average Petroleum Prices (U.S.\$ per barrel)

2004.....	30.13
2005.....	41.01
2006	
March.....	46.80
June.....	58.16
September.....	49.34
December.....	45.83
2007	
March.....	48.37
June.....	56.94
September.....	64.68
December.....	77.21
2008	
March.....	88.02
June.....	117.36
September.....	88.68
December.....	26.09

Source: Central Bank.

The Republic has estimated that an increase of U.S.\$1 in the price per barrel of petroleum results in approximately a 3.8% change in net oil revenues of U.S.\$37.6 million in additional net revenues for the Government sector.

Taxation

National taxes are collected through two governmental agencies: the *Servicio de Rentas Internas* (“SRI”) and the *Corporación Aduanera Ecuatoriana* (“CAE”). The Director of the SRI is the president of the CAE.

The following table shows the composition of the Republic’s tax revenue during the following periods:

Tax Revenue of the Republic (as a % of total tax revenue)

	From the year ended December 31,				
	2004	2005	2006	2007	2008
Taxes on income and profits.....	22.2%	25.0%	25.2%	26.7%	35.6%
Taxes on property (vehicles).....	1.8	1.6	1.6	1.5	1.4
Value-added tax.....	54.3	52.8	52.5	52.8	43.0
Selective excise taxes ⁽¹⁾	6.4	5.9	6.1	4.6	7.2
Import duties.....	14.3	14.6	14.6	14.3	12.0
Exit taxes ⁽²⁾	0.0	0	0	0	0.7
Other taxes.....	1.0	0.1	0	0.1	0.1
Total taxes.....	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

(1) These data reflect taxes on alcohol, cigarettes and other similar items.

(2) These data reflect taxes levied on persons travelling from Republic.

Sources: CAE, SRI.

The Government has historically collected taxes in the form of personal and corporate income tax, value-added tax, customs duties, special consumption taxes and certain other taxes. Tax revenues accounted for 62.6%, 55.9% and 47.6% of the Government’s total revenue in 2006, 2007 and 2008, respectively. Income tax collections represented 35.6% of total tax revenue in 2008.

In accordance with the *Ley Reformativa para la Equidad Tributaria del Ecuador* of 2007, the application of the luxury tax was placed on cigarettes, phone service, alcohol and other recreational items.

With respect to personal income, in 2008, the first U.S.\$8,570 of income earned is not taxed. The basic personal income tax rate is 5% for incomes above U.S.\$8,570, which increases on a sliding scale up to a maximum 35% rate on incomes of U.S.\$87,300 or more.

Corporate income tax is levied at a rate of 25% subject to certain deductions for the reinvestment of income to enhance productivity. This corporate income tax is treated as having been paid by the shareholders with respect to dividends in order to allow them to benefit from tax credits abroad.

The value-added tax is a broad-based tax on services and on manufactured, refined and other finished goods, that is levied at a fixed rate of value-added at each stage of the production process at a 12% flat rate. Revenue from the value-added tax is the largest contributor to total tax revenue and represented 45% of the total tax revenue for 2008.

Social Security

Social security in the Republic is administered by the IESS, an autonomous public sector entity, as well as the Social Security Institutes of the Armed Forces and the Police, respectively (“ISSFA” and “ISSPOL”).

Social security benefits are a constitutional right for workers and their families designed to protect the insured in case of illness, maternity, unemployment, disability, old age or death. The social security system also provides financing for workers’ housing. The Republic’s social security system is financed by contributions from the Government, employers and employees. The level of employee contribution is based on an employee’s income.

Retirees benefit from the IESS system once they cease employment. As of December 2008, the IESS had 1.48 million beneficiaries, of whom 77% worked in the private sector and 23% worked in the public sector. Between 2003 and 2008, the total number of beneficiaries increased at an average annual rate of 5%.

In February 2009, the ISSFA had 87,879 beneficiaries, of whom 52,445 are in military active service and 35,434 are in military reserves. As of the same date, the ISSPOL had 57,291 beneficiaries, of whom 39,681 are active policemen and 17,610 are in police reserves.

Social security contributions by employers and/or employees is 22.5% of the salary of each employee, depending upon the particular sector in which an employee works or the type of job held. The general insurance coverage in case of disability, old age or death is 6.64% or 8.64% depending upon an employee’s job category. Furthermore, the Government is in the process of making reforms to the social security system, including the creation of a bank for its beneficiaries and reforms to the investment guidelines of the institute in order to allow an adequate allocation of its resources.

The following table sets forth information regarding revenues to and expenditures of the IESS programme.

Social Security System (IESS)⁽¹⁾
(in millions of U.S.\$, and as a % of total GDP)

	For the year ended December 31,									
	2004	% of GDP	2005	% of GDP	2006	% of GDP	2007	% of GDP	2008 ⁽²⁾	% of GDP
Revenues										
Social security contributions.....	1,038	2.8	1,121	3.0	1,572	3.7	1,808	3.9	2,090	3.9
Interest and profits	73	0.2	117	0.3	137	0.3	184	0.4	211	0.4
Current transfers from budgetary operations	243	0.6	344	0.9	343	0.8	378	0.8	417	0.7
Others	1	0	0	0	0	0	0	0	2	0
Total revenues..	1,354	3.7	1,582	4.2	2,051	4.9	2,371	5.1	2,720	5.1
Expenditures										
Wages and salaries.....	34	0.0	49	0.1	50	0.1	47	0.1	49	0.0
Purchases of goods and services.....	115	0.3	116	0.3	166	0.4	212	0.4	232	0.4
Current transfers	665	1.8	1,184	3.8	1,226	2.9	1,277	2.7	1,508	2.8
Net lending	(18)	0	(2)	0	17	0	233	0.5	109	0.2
Others	0	0	(1)	0	0	0	0	0	50	0.1
Total expenditures ..	797	2.2	1,346	3.6	1,459	3.4	1,769	3.8	1,948	3.7
Surplus/(Deficit)....	557	1.5	236	0.6	592	1.4	602	1.3	772	1.4

(1) Revenues are cash; expenditures are accrued.

(2) Preliminary data.

Source: IEES.

2009 Budget

In November 2007, Congress approved the budget for 2008. The 2008 budget was prepared by the Ministry of Finance in accordance with the assumptions set forth below. The 2008 budget will remain in effect until the April 2009 elections at which point the newly elected President will have three months to approve a new budget.

Principal 2008 Budget Assumptions

Gross domestic product	
Nominal GDP (in millions of U.S.\$).....	47,851.3
Real GDP growth rate ⁽¹⁾	4.2%
Inflation	
Domestic inflation (average over year).....	3.0%
Oil export price (U.S.\$/barrel).....	\$35.0
Oil export volume (millions of barrels).....	126.1

(1) These data reflect the % change from previous year.

Sources: Central Bank and Ministry of Finance.

In light of the global recession, the Republic is implementing a number of fiscal measures. These measures include:

- for the non-financial sector, improving the quality of expenditure to prioritise projects through an annual investment plan which helps to further the national development plan, such as building hydroelectric plants to alleviate energy subsidies;
- borrowing from multilateral entities to compensate for the challenging credit environment, and from friendly countries through bilateral loans to finance investment in the energy and other sectors; and

- approving laws to ensure responsible management of the Republic's finances and to promote its social and economic development.

PUBLIC SECTOR DEBT

General

Public sector debt in the Republic, including the Central Government's internal debt and the external debt of the non-financial and financial public sector, totalled approximately U.S.\$14.55 billion as of December 31, 2004, U.S.\$14.53 billion as of December 31, 2005, U.S.\$13.50 billion as of December 31, 2006, U.S.\$13.87 billion as of December 31, 2007, and U.S.\$13.73 billion as of December 31, 2008. In 2008, the Republic's public sector internal debt totalled approximately U.S.\$3.64 billion and the public sector external debt totalled approximately U.S.\$10.1 billion.

Approximately U.S.\$4.0 billion or 40% of the Republic's external debt is represented by Brady Bonds and three series of other bonds. In addition, as of December 31, 2008, approximately U.S.\$4.3 billion or 42.95% of the Republic's external debt is represented by debts owed to multilateral organisations and U.S.\$1.5 billion corresponds to the Republic's bilateral debt with other governments. As of December 31, 2008, the Republic's total internal and external debt represented 26.12% of GDP. Approximately 26.8% of the external debt is represented by the 2030 Bonds, approximately 5.4% by the 2012 Bonds, and approximately 6.7% by 9.375% U.S. dollar denominated Global Bonds due 2015 (the "2015 Bonds"). The Republic is in default on the Bonds but is current with payments on the 2015 Bonds.

In 2008, an independent Ecuadorian body, the Commission of Integral Audit of Public Credit ("CAIC") issued a report that found a number of irregularities associated with the issue of the Bonds and the debt which was exchanged for these Bonds in 2000. These matters included concerns with the legitimacy of the original claims, appropriate authorisations, sovereign immunity and the financial terms associated with the exchange offer under which the 2012 Bonds and 2030 Bonds were originally issued. For a further discussion of the CAIC Commission's report and its relevance to the Republic's proposal with respect to the 2012 Bonds and the 2030 Bonds, see the "Letter from Minister of Finance".

Since President Correa was elected in 2007, the Republic has changed the focus of its public sector debt. The Republic has focused its relationship on IDB, CAF and FLAR, two of which are located in Latin America. As the Republic has strengthened its relationship with these Latin American-based multilateral entities, it no longer looks to borrow from the World Bank and IMF, the latter of which no longer has a representative based in the Republic. The Republic's relationship with the IMF in 2000 was one factor in the restructuring of its debt, as it helped the Republic to obtain external financing when it exchanged Brady Bonds for the then-issued 2012 Bonds and 2030 Bonds.

Other than the Bonds, the Republic is not in payment default on any of its public sector debt.

The following table sets forth information regarding the internal, external and total public sector debt as of the dates and for the periods indicated.

Internal, External and Total Public Sector Debt
(in millions of U.S.\$)

	As of and for the period ending December 31,				
	2004	2005	2006	2007	2008 ⁽¹⁾
Public sector internal debt.....	3,489.0	3,686.2	3,277.6	3,239.9	3,645.1
Public sector internal debt as a percentage of GDP.....	10.7%	9.9%	7.8%	7.1%	6.9%
Public sector external debt.....	11,060.4	10,850.3	10,214.9	10,632.7	10,088.9
Public sector external debt as a percentage of GDP.....	33.9%	29.2%	24.5%	23.2%	19.2%
Total public sector debt.....	14,549.4	14,536.5	13,492.5	13,872.6	13,734.0
Total public sector debt as a percentage of GDP.....	44.6%	39.1%	32.3%	30.3%	26.1%

(1) Preliminary data.
Source: Ministry of Finance.

Internal Debt

Approximately 98% of the Republic's internal public indebtedness consists of originally issued dollar-denominated notes (total notes). Internal debt obligations are issued through the Ministry of Finance. As of December 31, 2008, 33.9% of the Republic's internal debt is represented by the AGD notes, 61.0 % of the Republic's internal debt is represented by long-term notes, 2.7% of the Republic's internal debt is represented by CFN Notes and 2.4% by BEDE notes.

In recent years, the Republic's treasury bonds (*Certificados de Tesorería* or "CETES") have represented an increasingly smaller portion of the Republic's internal debt. CETES represented less than 1% of the Republic's internal debt at each of December 31, 2007 and December 31, 2008, and approximately 11.9%, 18.5% and 8.9% of the Republic's internal debt at December 31, 2004, 2005 and 2006, respectively. CETES are primarily held by private financial institutions and Government entities.

The following table sets forth information regarding the Republic's internal debt obligations (excluding arrears).

Public Sector Internal Debt
(in millions of U.S.\$)

	As of December 31,									
	2004		2005		2006		2007		2008 ⁽¹⁾	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Notes										
Short-term notes.....	0	0	0	0	0	0	0	0	0	0
Long-term notes.....	1,449.6	41.5	1,374.6	37.3	1,389.5	42.4	1,716.0	53.0	2,224.8	61.0
AGD notes.....	1,241.7	35.6	1,241.7	33.7	1,241.7	37.9	1,236.8	38.2	1,236.8	33.9
CFN notes.....	246.8	7.1	195.9	5.3	174.5	5.3	133.8	4.1	97.7	2.7
Filanbanco notes.....	45.2	1.3	19.0	0.5	19.0	0.6	0	0	0	—
Total notes.....	2,983.3	85.5	2,831.2	76.8	2,824.7	86.2	3,086.6	95.3	3,559.3	97.6
CETES.....	414.6	11.9	680.5	18.5	292.6	8.9	0	0	0	0
Governmental Entities.....	91.1	2.6	174.5	4.7	160.3	4.9	153.3	4.7	85.8	2.4
Total internal debt.....	3,489.0	100.0	3,686.2	100.0	3,277.6	100.0	3,239.9	100.0	3,645.1	100.0

(1) Preliminary data.
Source: Ministry of Finance.

Medium- and Short-Term Notes

Since 2007, the Republic has not issued any short-term debt (due within one year), and it has no intention of doing so in the future. In general, the Republic's medium- and short-term obligations have been issued to finance development projects and to restructure or provide for revenue shortfalls in the government's budget for a given year. Notes issued for development projects are generally privately held by entities hired to undertake these

development projects. Notes issued for budget restructurings are placed on the Quito and Guayaquil stock exchanges and are currently held by both public and private holders.

In October 1999, the Government initiated a refinancing of U.S. dollar-denominated debt excluding such debt instruments held by the Central Bank, financial institutions under the control of the AGD and Ecuadorian municipalities. The AGD notes held by the Central Bank (originally maturing over a 15-year period and carrying an interest rate of 12% per annum) were rescheduled over a 15-year period at a fixed rate of 9.35%, and from July 2004 at a fixed rate of 3.9%. Earlier this year, the AGD notes were assigned to the Ministry of Finance at a 100% discount and were replaced by a common fund sourced by private banks as part of a new deposit insurance regulation. See “Republic of Ecuador—The Financial System—Structure of the Financial System—AGD Sources of Liquidity”.

Although municipal governments may incur debt through the Ministry of Finance if they follow certain requirements established by law, municipal governments have not issued such debt and have no current intention of doing so.

External Debt

The Republic has historically relied on four types of external debt sources: commercial banks, multilateral financial institutions, governments and supplier credits. As of December 31, 2008, public sector external debt totalled U.S.\$10.1 billion, of which U.S.\$3.9 billion consisted of the Bonds and 2015 Bonds.

The following table sets forth information regarding our public sector external debt (excluding arrears) as of the dates indicated.

Public Sector External Debt (in millions of U.S.\$)

	As of December 31,				
	2004	2005	2006	2007	2008 ⁽³⁾
Total Public sector external debt.	11,060.4	10,850.3	10,214.9	10,632.7	10,088.9
2012 Bonds ⁽¹⁾	1,250.0	1,250.0	1,250.0	510.0 ⁽²⁾	540.6
2015 Bonds	—	650.0	650.0	650.0	680.5
Brady Bonds	125.9	122.7	119.5	116.3	111.3
2030 Global Bonds ⁽¹⁾	2,700.0	2,700.0	2,700.0	2,700.0	2,700.0
Commercial Banks	222.1	211.4	183.2	160.4	131.7
Multilateral financial institutions	4,297.6	3,888.1	4,141.9	4,742.3	4,333.1
Foreign governments	2,425.6	1,999.6	1,829.6	1,684.9	1,530.0
Supplier credits	39.2	28.5	80.7	68.8	61.7

(1) This series of bonds is in default.

(2) Some of the bonds have been redeemed through regular market buybacks.

(3) Preliminary data.

Source: Ministry of Finance.

Projected Financing and Expenditures

The following table sets forth the Central Government’s projected financing sources and expenditures for 2009 and 2010. The information set forth in this table is forward looking information, based upon current plans, estimates, projections and assumptions, and it is subject to inherent uncertainties.

The information presented for 2009 is based on the Government’s macroeconomic plans and the proposed annual budget, which will be submitted to the National Assembly by the elected President within three months of election. The budget is divided into twenty different sectors, including social programmes and debt service. Under the Constitution, although the National Assembly has the right to make changes to the general allocation of funds from sector to sector, it does not have the legal authority to decide how those changes should be specifically effected within each sector. Under the Budget Law of 1992 and the Organic Financial Administration and Control Law of 1977, the Minister of Finance has the authority to reallocate funds to the debt service sector during the execution phase of the budget. In addition, under the Organic Financial Administration and Control Law, the Minister of

Finance has the authority to reallocate funds under the budget, as necessary, in order to pay all of the Republic's debt obligations.

No assurance can be made that actual financing requirements for both 2009 and 2010 will not be higher than projected, that actual sources of financing made available to the Central Government will not differ materially from those figures presented below or that projected uses of financing (even assuming subsequent reallocation of funds by the Minister of Finance) will be as described in the table below.

Central Government's Projected Financing and Expenditures
(in millions of U.S.\$)

	<u>2009 Projections</u>	<u>2010 Projections</u>
Financing Requirements	3,110	2,621
Central Government Deficit.....	2,084	1,802
Amortisations.....	773	1,005
Internal.....	293	434
Foreign.....	480	570
Repurchase / Prepayments.....	-	-
Others (including delayed payments)	252	(185)
Identified Financing	1,880	1,821
Bonds and Treasury Certificates.....	1,285	1,228
Internal.....	-	-
Foreign.....	1,285	1,228
Infrastructure projects expenditures.....	595	593
Internal	125	70
Foreign.....	470	523

Source: Ministry of Finance.

Multilateral Support (2004 - 2008)

During the years of 2004 - 2008, the Republic obtained financing from the World Bank, IDB, CAF and FLAR. Such financial support was used for the financing of infrastructure projects and the development of social governmental policies. In this regard, for the support of social, tax and debt collection, CAF granted a US\$1.3 billion loan to the Republic.

Likewise, BID granted a US\$434 million loan in favour of the Republic, in order for it to develop certain infrastructure projects, such as, airports and sewerage systems.

The Republic has started discussions with CAF, IDB and FLAR with a view to obtaining additional financing for investment projects.

Debt Restructuring

Brady Bonds and Eurobonds

In May 1994, the Government reached an agreement with its commercial bank creditors to restructure the Republic's medium and long-term commercial bank debt (the "Brady Plan"). The Brady Plan offered creditors the opportunity to exchange existing principal for either of two instruments: (i) 30-year notes of the same face amount (the "Par Notes"), with interest initially fixed at three percent and rising by increments over the first 10 years up to a rate of five percent or (ii) 30-year notes with a face amount equal to 55% of the face value of the debt exchanged (the "Discount Notes" together with the Par Notes, the "Brady Bonds") and bearing interest at the London Interbank Offered Rate ("LIBOR") plus 13/16 percent. The principal of Par Notes and Discount Notes was fully collateralised by 30-year U.S. Treasury notes and interest on such Notes was collateralised on a 12-month rolling basis. The Brady Plan also offered creditors the opportunity to exchange accrued and unpaid interest for two instruments: (i) 20-year notes bearing interest at LIBOR plus 13/16 percent (the "PDI Notes") and (ii) 10-year notes bearing

interest at LIBOR plus 13/16 percent and representing certain amounts of past due interest, accrued and unpaid, under the Consolidation Agreement (the “IE Notes”).

On December 21, 1994, the Republic issued U.S.\$191.0 million of IE Notes. On February 28, 1995, the Republic issued U.S.\$1.9 billion, U.S.\$1.4 billion and U.S.\$2.4 billion of Par Notes, Discount Notes and PDI Notes, respectively. The Republic also agreed to make certain additional cash payments in respect of past due interest.

On April 25, 1997, the Republic issued U.S.\$350 million of its 11.25% Fixed Rate Eurobonds due 2002 and U.S.\$150 million of its Floating Rate Eurobonds due 2004 (together, the “Eurobonds”).

In late 1999 and early 2000, the Republic defaulted on its Par Bonds, Discount Bonds, 11.25% Fixed Rate Eurobonds due 2002, Floating Rate Eurobonds due 2004, IE Notes and PDI Notes (together, the “Old Notes”). In June 2000, the Republic launched a global exchange offer whereby it offered the Bonds together with a cash payment for any and all of the Old Notes.

In December 2005, the Republic launched an issuance of the 2015 Bonds. The use of the proceeds of the 2015 Bonds was to buyback certain of the 2012 Bonds in accordance with their terms. The Republic is current with its payments on the 2015 Bonds. The last interest payment on the 2015 Bonds, which was due on December 15, 2008, was paid by the Republic in accordance with the relevant indenture. The Republic intends to make all payments on the 2015 Bonds as they become due and payable.

The Republic has defaulted on its interest payments for the Bonds. For further discussion of the Bonds, see “Letter from Minister of Finance”. The following table sets forth the results of the 2000 exchange offer.

Exchanged Bonds
(in millions of U.S.\$)

Type of Bond	Nominal Value	Value of Exchanged Bonds	Value of Unexchanged Bonds
Par Notes	1,655.4	1,598.5	56.9
Discount Notes	1,434.7	1,408.6	26.1
PDI Notes	2,728.3	2,650.2	78.1
IE Notes	124.0	119.8	4.2
Fixed Rate Eurobonds due 2002	350.0	337.0	13.0
Floating Rate Eurobonds due 2004	150.0	143.5	6.5
Total	6,442.4	6,257.6	184.8

Source: Central Bank.

An aggregate of U.S.\$3.95 billion of Bonds were offered as part of the 2000 exchange offer, of which U.S.\$2.7 billion were 2030 Bonds and U.S.\$1.25 billion were 2012 Bonds.

Paris Club

In June 2003, the Republic agreed with its Paris Club creditors to reschedule U.S.\$81 million of bilateral debt. Payments due on official development aid loans were rescheduled over a period of 20 years and those on other credits were rescheduled over a period of eighteen years. As of December 31, 2008, the Republic was in compliance with all of the terms of its Paris Club loans.

In recent years, the Republic has launched successful debt exchanges in Germany, Spain and Italy and is in the process of negotiating exchanges with France and Norway.

The following tables set forth information regarding the Republic's debt service profile for 2009 to 2019.

Public Sector Debt Service Profile
(in million of U.S.\$)

	2009		2010		2011		2012		2013	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
External Debt Payments⁽²⁾										
Multilateral (including the IMF).....	336.1	200.4	347.4	187.8	401.3	184.7	422.7	169.6	405.7	150.7
World Bank	82.8	21.3	91.1	18.6	85.4	15.4	75.7	12.5	70.5	10.0
Inter-American Development Bank ...	142.2	85.8	143.4	78.3	149.2	84.6	156.9	81.5	158.6	75.4
Andean Development Corporation	108.8	92.9	110.6	90.5	164.9	84.4	188.3	75.3	175.6	65.1
IMF	—	—	—	—	—	—	—	—	—	—
Others	2.3	0.4	2.3	0.4	1.8	0.3	1.8	0.3	1.0	0.2
Governments	184.2	58.5	145.1	50.8	130.2	44.5	128.7	39.3	124.8	33.6
Paris Club	76.2	35.9	48.5	32.7	57.8	30.2	61.5	27.5	65.5	24.4
Other loans.....	108.0	22.6	96.6	18.1	72.4	14.3	67.2	11.8	59.3	9.2
Brady Bonds	5.1	4.8	5.1	4.6	8.6	4.3	8.6	4.0	8.6	3.7
Global Bonds ⁽¹⁾	—	392.1	—	392.1	10.0	392.1	500.0	392.1	81.0	330.9
Commercial banks	24.7	6.3	24.3	5.1	20.9	4.0	20.3	3.0	19.9	2.0
Supplier credits	6.8	4.0	7.0	3.5	7.4	3.0	6.3	2.5	5.3	2.2
Total External Debt.....	<u>556.9</u>	<u>666.1</u>	<u>528.9</u>	<u>643.9</u>	<u>578.4</u>	<u>632.6</u>	<u>1,086.6</u>	<u>610.5</u>	<u>645.3</u>	<u>523.1</u>
Internal Debt Payments⁽²⁾										
Short-term notes.....	—	—	—	—	—	—	—	—	—	—
Long-term notes.....	229.6	141.1	360.2	129.6	377.2	104.3	142.0	82.1	158.3	72.6
AGD notes	—	14.2	—	14.2	—	14.2	—	14.2	315.6	14.2
CFN notes	48.6	3.8	49.1	1.7	—	—	—	—	—	—
Filanbanco notes	—	—	—	—	—	—	—	—	—	—
Total notes	<u>278.2</u>	<u>159.1</u>	<u>409.3</u>	<u>145.5</u>	<u>377.2</u>	<u>118.5</u>	<u>142.0</u>	<u>96.3</u>	<u>473.9</u>	<u>86.8</u>
Treasury bonds (CETES).....	—	—	—	—	—	—	—	—	—	—
Governmental Entities	14.8	6.6	15.1	5.3	15.4	4.1	14.8	2.8	11.9	1.7
Total internal debt	<u>293.0</u>	<u>165.7</u>	<u>424.4</u>	<u>150.8</u>	<u>392.6</u>	<u>122.6</u>	<u>156.8</u>	<u>99.1</u>	<u>485.8</u>	<u>88.5</u>
Total Public Sector Debt Payments.....	<u>849.9</u>	<u>831.8</u>	<u>953.3</u>	<u>794.7</u>	<u>971.0</u>	<u>755.2</u>	<u>1,243.4</u>	<u>709.6</u>	<u>1,131.1</u>	<u>611.6</u>

(1) These data include the 2012 Bonds and 2030 Bonds.

(2) Debt projection assumptions are on a cash basis, including disbursements of loans through December 2008. These data assume 6 month LIBOR of 2.5% for 2005 and 3.5% subsequently. These data assume no rescheduling of debt of any kind.

Source: Ministry of Finance.

Public Sector Debt Service Profile
(in million of U.S.\$)

	2014		2015		2016		2017	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
External Debt Payments⁽²⁾								
Multilateral (including the IMF)...	389.4	132.4	325.3	114.8	286.1	100.3	255.3	87.8
World Bank	60.6	7.5	41.7	5.4	30.2	4.2	23.2	3.3
Inter-American Development Bank	161.3	68.7	140.3	61.8	133.9	55.8	128.4	49.9
Andean Development Corporation	166.5	56.0	141.8	47.4	120.5	40.1	102.2	34.5
IMF	—	—	—	—	—	—	—	—
Others	1.0	0.2	1.5	0.2	1.5	0.2	1.5	0.1
Governments	125.0	28.6	122.2	23.6	123.9	18.8	125.4	13.6
Paris Club	73.4	21.2	76.3	17.6	83.6	13.9	91.1	9.7
Other loans.....	51.6	7.4	45.9	6.0	40.3	4.9	34.3	3.9
Brady Bonds	8.6	3.4	4.3	3.1	—	3.0	—	3.0
Global Bonds ⁽¹⁾	81.0	322.8	731.0	314.7	81.0	245.7	81.0	237.6
Commercial banks	15.4	1.1	6.5	0.5	3.4	0.2	1.5	0.1
Supplier credits	5.7	1.6	6.1	1.4	6.5	1.1	6.9	0.5
Total External Debt	<u>625.1</u>	<u>490.1</u>	<u>1,195.4</u>	<u>458.1</u>	<u>500.9</u>	<u>369.1</u>	<u>470.1</u>	<u>342.6</u>
Internal Debt Payments⁽²⁾								
Short-term notes.....	—	—	—	—	—	—	—	—
Long-term notes.....	352.1	61.8	350.0	38.7	199.9	15.0	—	—
AGD notes	921.3	14.2	—	—	—	—	—	—
CFN notes	—	—	—	—	—	—	—	—
Filanbanco notes	—	—	—	—	—	—	—	—
Total notes	<u>1,273.4</u>	<u>76.0</u>	<u>350.0</u>	<u>38.7</u>	<u>199.9</u>	<u>15.0</u>	<u>—</u>	<u>—</u>
Treasury bonds (CETES).....	—	—	—	—	—	—	—	—
Governmental Entities	9.5	0.7	2.8	0.3	1.5	0.1	—	—
Total Internal Debt	<u>1,282.9</u>	<u>76.7</u>	<u>352.8</u>	<u>39.0</u>	<u>201.4</u>	<u>15.1</u>	<u>—</u>	<u>—</u>
Total Public Sector Debt Payments ...	<u><u>1,908.0</u></u>	<u><u>566.8</u></u>	<u><u>1,548.2</u></u>	<u><u>497.1</u></u>	<u><u>702.3</u></u>	<u><u>384.2</u></u>	<u><u>470.1</u></u>	<u><u>342.6</u></u>

(1) These data include the 2030 Bonds.

(2) Debt projection assumptions are on a cash basis, including disbursements of loans through December 2008. These data assume 6 month LIBOR of 2.5% for 2005 and 3.5% subsequently. These data assume no rescheduling of debt of any kind.

Source: Ministry of Finance.

Total Public Sector Debt by Creditor and Debtor
As of December 31, 2008⁽¹⁾
(in millions of U.S.\$)

	<u>Debt stock⁽²⁾</u>	<u>Arrears⁽³⁾</u>	<u>Total</u>
By Creditor			
External Debt			
Multilateral.....	4,333.1	—	4,333.1
World Bank	623.9	—	623.9
Inter-American Development Bank	1,960.7	—	1,960.7
Andean Development Corporation	1,734.2	—	1,734.2
International Monetary Fund.....	—	—	—
Others	14.3	—	14.3
Governments.....	1,530.0	—	1,530.0
Paris Club	748.7	—	748.7
Other loans.....	781.3	—	781.3
Brady Bonds	111.3	—	111.3
Global Bonds ⁽⁴⁾	3,860.0	61.1	3,921.1
Commercial banks	131.7	—	131.7
Supplier credits	61.7	—	61.7
Total External Debt	<u>10,027.8</u>	<u>61.1</u>	<u>10,088.9</u>
Internal Debt			
Long-term notes.....	2,224.8	—	2,224.8
AGD notes	1,236.8	—	1,236.8
CFN notes	97.7	—	97.7
Filanbanco notes	—	—	—
Total notes.....	3,559.3	—	3,559.3
Treasury bonds (CETES).....	—	—	—
Governmental entities.....	85.8	—	85.8
Total internal debt	<u>3,645.1</u>	<u>—</u>	<u>3,645.1</u>
Total public sector debt	<u>13,672.9</u>	<u>61.1</u>	<u>13,734.0</u>
By Debtor			
External Debt			
Central government	9,004.6	59.0	9,063.6
Regional government.....	266.3	—	266.3
Petroecuador	100.6	1.3	101.9
EMETEL.....	97.4	—	97.4
Financial public sector.....	61.0	—	61.0
Other public sector.....	497.9	0.8	498.7
Total.....	<u>10,027.8</u>	<u>61.1</u>	<u>10,088.9</u>

(1) Preliminary data.

(2) These data include arrears to date.

(3) These data include interest plus past due interest.

(4) These data include the 2012 Bonds and 2030 Bonds.

Source: Ministry of Finance.

**Public Sector External Debt
by Creditor and Currency
As of December 31, 2008⁽¹⁾**
(in millions of U.S.\$)

		Debt Stock⁽²⁾
World Bank	U.S. dollar	623.9
Inter-American Development Bank (IDB)		1,960.7
	U.S. dollar	1,361.2
	Canadian dollar	13.6
	Euro	55.2
	British pounds	1.9
	Japanese yen	26.2
	Swiss franc	4.0
	IDB currency pool	496.1
	Danish krone	2.2
	Norwegian krone	0.2
	Swedish krona	0.1
Andean Development Corporation	U.S. dollar	1,734.2
IMF	SDR	—
Others		14.3
	U.S. dollar	—
	SDR	14.3
		1,530.0
Governments		
	U.S. dollar	895.7
	Canadian dollar	8.8
	Chinese yuan	2.7
	Euro	285.0
	British pounds	51.3
	Japanese yen	281.8
	Korean won	4.7
Brady Bonds	U.S. dollar	111.3
Global Bonds ⁽³⁾	U.S. dollar	3,921.1
Commercial Banks	U.S. dollar	131.7
Supplier Credits	U.S. dollar	61.7
Total external debt		10,088.9

(1) Preliminary data.

(2) These data include interest plus past due interest.

(3) These data include the 2012 Bonds and 2030 Bonds.

Source: Ministry of Finance

Public Sector External Debt by Currency
As of December 31, 2008⁽¹⁾
(in millions of U.S.\$)

	Debt Stock	%
American dollar.....	8,840.8	87.6
IDB currency pool.....	496.1	4.9
Euro	340.2	3.4
Japanese yen.....	308.0	3.1
IMF SDR	14.3	0.1
British pounds	53.2	0.5
Canadian dollar	22.4	0.2
Korea won	4.7	0
Chinese yuan	2.7	0
Swiss francs.....	4.0	0
Danish krone	2.2	0
Other currencies	0.3	0
Total.....	<u>10,088.9</u>	<u>100.00%</u>

(1) Preliminary data.
Source: Ministry of Finance.

Public Sector External Debt by Creditor
(in millions of U.S.\$, and as a % of total public sector external debt)

	2004		2005		2006		2007		2008 ⁽¹⁾	
	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%	U.S.\$	%
Official creditors:										
Multilateral debt:										
World Bank	853.2	7.7	816.9	7.5	762.2	7.5	698.5	6.6	623.9	6.2
Inter-American Development Bank	1,993.7	18.0	1,819.7	16.8	1,837.8	18.0	1,993.8	18.8	1,960.7	19.4
Andean Development Corporation..	1,139.4	10.3	1,154.7	10.6	1,202.4	11.8	1,867.0	17.6	1,734.2	17.2
International Monetary Fund	289.1	2.6	78.6	0.7	22.7	0.2	—	—	—	—
Others	22.2	0.2	18.2	0.2	316.8	3.1	183.0	1.7	14.3	0.1
Total multilateral debt	4,297.6	38.9	3,888.1	35.8	4,141.9	40.5	4,742.3	44.6	4,333.1	42.9
Bilateral debt:										
United States	162.9	1.5	133.1	1.2	105.5	1.0	93.0	0.9	82.3	0.8
Japan	427.9	3.9	329.4	3.0	295.6	2.9	277.1	2.6	302.9	3.0
Italy	422.5	3.8	371.7	3.4	344.2	3.4	329.4	3.1	302.3	3.0
Spain	312.1	2.8	251.1	2.3	249.3	2.4	251.2	2.4	246.8	2.4
Brazil	330.3	3.0	280.3	2.6	230.3	2.3	180.2	1.7	131.0	1.3
Other countries	769.9	7.0	634.0	5.8	604.7	5.9	554.0	5.2	464.7	4.6
Total official debt	2,425.6	21.9	1,999.6	18.4	1,829.6	17.9	1,684.9	15.8	1,530.0	15.2
Private creditors:										
Banking	222.1	2.0	211.4	1.9	183.2	1.8	160.4	1.5	131.7	1.3
Bonds (Brady and Global) ⁽²⁾	4,075.9	36.9	4,722.7	43.5	3,979.5	39.0	3,976.3	37.4	4,032.4	40.0
Suppliers	39.2	0.4	28.5	0.3	80.7	0.8	68.8	0.6	61.7	0.6
Total private sector debt	4,337.2	39.2	4,962.6	45.7	4,243.4	41.5	4,205.5	39.6	4,225.8	41.9
Total public sector external debt	11,060.4	100.0	10,850.3	100.0	10,214.9	100.0	10,632.7	100.0	10,088.9	100.0

(1) Preliminary data.

(2) These data include the 2012 Bonds and 2030 Bonds.

Source: Ministry of Finance.

CERTAIN TAX CONSIDERATIONS

The sale of Bonds pursuant to the Invitation and the receipt of the applicable Clearing Price may have important tax consequences to the Holders. A summary of certain Ecuadorian and U.S. federal income tax considerations for Holders that sell Bonds pursuant to the Invitation is set forth below. This summary is not comprehensive. In addition, tax considerations other than those arising under Ecuadorian law and the United States federal income tax laws are not discussed herein. Holders should consult their own tax advisors as to the tax consequences to them of selling their Bonds pursuant to the Invitation and the receipt of the Clearing Price.

Certain Ecuadorian Tax Considerations

All payments of the Clearing Price for Bonds offered for sale pursuant to the Invitation and accepted by the Republic, and any gains made by a Holder from such sale, will be exempt from any Ecuadorian income tax, including withholding tax, if the Holder is a foreign holder, i.e.:

- The Holder is an individual and is not resident in the Republic for tax purposes; or
- The Holder is a non-Ecuadorian entity and holds the Bonds directly and not through a permanent establishment or fixed base in the Republic.

There are no Ecuadorian stamp, registration or similar taxes payable by a foreign Holder in connection with Offers or sales of Bonds, pursuant to the Invitation.

Certain United States Federal Income Tax Considerations

TO ENSURE COMPLIANCE WITH UNITED STATES TREASURY DEPARTMENT CIRCULAR 230, HOLDERS ARE HEREBY NOTIFIED THAT: (1) ANY DISCUSSION OF UNITED STATES FEDERAL TAX ISSUES IN THIS DOCUMENT IS NOT INTENDED OR WRITTEN BY US TO BE RELIED UPON, AND CANNOT BE RELIED UPON, FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED UNDER THE U.S. INTERNAL REVENUE CODE OF 1986, AS AMENDED (THE "CODE"); (2) SUCH DISCUSSION IS WRITTEN IN CONNECTION WITH THE PROMOTION OR MARKETING OF THE TRANSACTIONS OF MATTERS ADDRESSED HEREIN; AND (3) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM THEIR OWN INDEPENDENT TAX ADVISORS.

The following discussion is a summary of certain United States federal income tax considerations for Holders who elect to participate in the Invitation. The discussion is general in nature and does not discuss all aspects of United States federal income taxation that may be relevant to a particular Holder in light of the Holder's particular circumstances or to certain types of Holders subject to special treatment under United States federal income tax laws (such as insurance companies, expatriates, tax-exempt organisations, partnerships or other pass-through entities and investors in these entities, persons holding Bonds as part of a straddle or a hedging, integrated, conversion or constructive sale transactions, financial institutions, brokers, dealers in securities or currencies, traders that elect to mark-to-market their securities, persons that acquire Bonds in connection with employment or other performance of services, persons that have a functional currency other than the United States dollar, and persons who have ceased to be United States citizens or to be taxed as resident aliens). In addition, the discussion does not consider the effect of any possible applicability of alternative minimum taxes, United States state or local taxes, non-United States taxes or any United States federal tax other than the income tax (e.g., estate and gift taxes). Further, this summary assumes that Holders hold their Bonds as the beneficial owners of such Bonds for U.S. federal income tax purposes, and that Holders hold their Bonds as "capital assets" (generally, property held for investment) within the meaning of section 1221 of the Code.

This summary is based on the Code and the applicable United States final and proposed income tax regulations (the "Treasury Regulations"), rulings, administrative pronouncements and judicial decisions thereunder as of the date hereof, all of which are subject to change or differing interpretations at any time with possible retroactive effect.

As used herein, a “U.S. Holder” means a Holder that is for United States federal income tax purposes (1) a citizen or resident of the United States, (2) a corporation (or other entity treated as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States or any political subdivision thereof, (3) an estate the income of which is subject to United States federal income taxation regardless of its source or (4) a trust (a) that is subject to the primary supervision of a court within the United States and the control of one or more United States persons as described in Section 7701(a)(30) of the Code or (b) that has a valid election in effect under applicable Treasury Regulations to be treated as a United States person.

If a partnership, including any entity or arrangement treated as a partnership for United States federal income tax purposes, holds Bonds, then the tax treatment of a partner in that partnership generally depends upon the status of the partner and the activities of the partnership. Partnerships holding Bonds and partners in these partnerships are urged to consult their tax advisors.

As used herein, a “Non-U.S. Holder” means a Holder that is not a partnership for United States federal income tax purposes and is not a U.S. Holder.

THIS SUMMARY OF CERTAIN UNITED STATES FEDERAL INCOME TAX CONSIDERATIONS CONSTITUTES NEITHER TAX NOR LEGAL ADVICE. HOLDERS ARE URGED TO CONSULT WITH THEIR OWN TAX ADVISORS REGARDING THE SPECIFIC TAX CONSEQUENCES AND RISKS TO THEM OF TENDERING BONDS PURSUANT TO THE INVITATION TO PURCHASE, INCLUDING THE CONSEQUENCES OF THE TAX LAWS OF ANY APPLICABLE NON-UNITED STATES AND UNITED STATES STATE AND LOCAL TAXING JURISDICTION.

Tax Consequences For Tendering U.S. Holders

A sale of Bonds by a U.S. Holder pursuant to the Invitation will constitute a taxable transaction for United States federal income tax purposes. A U.S. Holder generally will recognize gain or loss on the sale of a Bond in an amount equal to the difference between (1) the amount of cash received for the Bond except to the extent attributable to accrued but unpaid interest and (2) the U.S. Holder’s adjusted tax basis in the tendered Bond at the time of sale. Any amount attributable to accrued and unpaid interest (including accrued original issue discount, if any, not previously required to be taken into account by the U.S. Holder) generally will be treated as ordinary income for United States federal income tax purposes. U.S. Holders are urged to consult with their tax advisors as to whether there is original issue discount on the Bonds.

A U.S. Holder’s adjusted tax basis in a Bond generally will equal the U.S. Holder’s cost of the Bond subject to any adjustments, and, if applicable, (a) increased by the amount of any market discount with respect to the Bond previously included in the U.S. Holder’s gross income (pursuant to an election) and, if applicable, the amount of any accrued original issue discount with respect to the Bond previously included in the U.S. Holder’s gross income and (b) reduced (but not below zero) by any bond premium allowed as an offset against interest income with respect to the Bond.

Because the 2030 Bonds likely will be treated as bearing original issue discount, the gain recognized on the sale by a U.S. Holder of 2030 Bonds likely will be treated as ordinary income to the extent of the total amount of original issue discount for such Bonds not previously included in the gross income of any U.S. Holder. In the case of a U.S. Holder that acquired a Bond at a market discount (subject to a *de minimis* exception), any gain recognized upon the sale of the Bond will be treated as ordinary income to the extent that the market discount accrued during the period the U.S. Holder held the Bond, unless the U.S. Holder had previously elected to include accrued market discount in gross income on a current basis. Market discount generally equals the excess of the face amount of a Bond over the U.S. Holder’s tax basis in the Bond immediately after its acquisition, unless acquired at original issuance. Subject to the exceptions described in this paragraph, any gain or loss recognized generally will be capital gain or loss and, if the Bond has been held by the U.S. Holder for more than one year as of the tender date, long-term capital gain or loss. The use of capital losses is subject to limitations.

Tax Consequences for Tendering Non-U.S. Holders

Gain realized by a Non-U.S. Holder on the sale of a Bond pursuant to the Invitation and payments attributable to accrued but unpaid interest generally will not be subject to United States federal income or withholding tax unless (1) the gain or interest is effectively connected with the conduct by the Non-U.S. Holder of a trade or business in the United States and, if a treaty applies, the gain or interest is attributable to a United States “permanent establishment” or, in the case of an individual Non-U.S. Holder, a “fixed base” maintained by the Non-U.S. Holder (a “U.S. Trade or Business”) or (2) in the case of gain realized by a Non-U.S. Holder that is an individual, the Non-U.S. Holder is present in the United States for 183 days or more in the taxable year of the sale and certain other conditions are met.

Tax Consequences for Non-Tendering Holders

The Invitation will not affect the U.S. federal income tax treatment of Holders who do not sell their Bonds pursuant to the Invitation, including Holders who submit Offers pursuant to the Invitation but whose Offers are not accepted by the Republic.

Information Reporting and Backup Withholding

U.S. Holders. Certain non-exempt U.S. Holders may be subject to information reporting in respect of the Clearing Price paid to them in respect of Bonds sold pursuant to the Invitation. In addition, backup withholding may apply, currently at a rate of 28%, if the U.S. Holder fails to either (1) supply a taxpayer identification number and certain other information, certified under penalty of perjury, (2) certify eligibility for an exemption to backup withholding or (3) otherwise comply with the applicable backup withholding rules. Amounts withheld are allowable as a refund or a credit against the U.S. Holder’s federal income tax upon furnishing the required information on a timely basis to the Internal Revenue Service (the “IRS”).

Non-U.S. Holders. Payments of the Clearing Price to a Non-U.S. Holder in respect of Bonds sold pursuant to the Invitation generally will not be subject to information reporting or backup withholding, if such payments are effected through a non-United States office or a broker to an offshore account maintained by a Non-U.S. Holder. If, however, the broker is a “United States person”, a “controlled foreign corporation”, a non-United States person 50% or more of whose gross income is effectively connected with a U.S. Trade or Business for a specified three-year period, a non-United States partnership with significant United States ownership or a United States branch of a non-United States bank or insurance company, then information reporting will be required, unless the broker (1) has documentary evidence that the beneficial owner of the payment is not a United States person or is otherwise entitled to a backup withholding exemption and (2) the broker has neither actual knowledge nor a reason to know that the beneficial owner is not entitled to an exemption. Backup withholding, currently at a rate of 28%, will apply if the sale of Bonds is subject to information reporting and the broker has actual knowledge or reason to know that the beneficial owner is a United States person that is not an exempt recipient.

In addition, information reporting and backup withholding will apply to payments effected at a United States office of any broker, unless (i) the broker has documentary evidence in its records that the beneficial owner of the payment is not a United States person or is otherwise entitled to an exemption and (ii) the broker has no actual knowledge or reason to know that the beneficial owner is not entitled to an exemption.

Backup withholding is not an additional tax. Amounts withheld from payments to a Non-U.S. Holder under the backup withholding rules may be credited against such Non-U.S. Holder’s United States federal income tax liability and may entitle such Non-U.S. Holder to a refund, provided that the required information is timely furnished to the IRS.

This discussion of certain United States federal income tax considerations set forth above is included for general information purposes only. All Holders are urged to consult their own tax advisors to determine the United States federal, state and local and non-United States tax consequences to them of their participation or non-participation in the Invitation.

JURISDICTIONAL RESTRICTIONS

The distributions of this Noteholder Circular may be restricted by law in certain jurisdictions. Persons into whose possession this Noteholder Circular comes are required by the Republic to inform themselves of and to observe any such restrictions.

The Invitation is not being made, and Offers will not be accepted from or on behalf of any Holders, in any jurisdiction in which the making or acceptance thereof would not be in compliance with the securities, blue sky or other laws of such jurisdiction or would require any registration or filing with any regulatory authority. In any jurisdiction in which the Invitation is required to be made by a licensed broker or dealer and the Joint Dealer Managers or any affiliate of the Joint Dealer Managers is a licensed broker or dealer in that jurisdiction, the Invitation is being made in that jurisdiction to the extent permitted by applicable law by the Joint Dealer Managers or that affiliate on behalf of the Republic.

Chile

The Bonds have not been registered in the Securities Registry (*Registro de Valores*) of the Chilean Superintendency of Securities and Insurance (*Superintendencia de Valores y Seguros*) and the Invitation has not been submitted nor reviewed by the Chilean authorities.

Italy

Neither this Invitation made by this Noteholder Circular nor any of the information contained herein constitutes an offer or an invitation or solicitation to tender, offer or sell or a promotional message of any form to any person (natural or legal) resident in the Republic of Italy to purchase, exchange or acquire the Bonds, within the meaning of articles 1, paragraph 1, letter (v), and 101-bis et seq., of Legislative Decree dated February 24, 1998, No. 58. The Invitation is not being made and will not be made, directly or indirectly, in or into the Republic of Italy, whether by mail or by any means or other instrument (including, without limitation, telephonically or electronically) or any facility of a national securities exchange publicly or privately available in the Republic of Italy. Accordingly, copies of this Noteholder Circular and any related documents should not be mailed or otherwise forwarded, distributed or sent in, into or from the Republic of Italy and persons receiving such documents must not forward, distribute or send them in or into or from the Republic of Italy. Therefore, Holders are hereby notified that, to the extent such Holders are resident or located in the Republic of Italy, the Invitation is not addressed to them. Any person who may have a legal or contractual obligation to forward this Noteholder Circular and any other Invitation documents in the Republic of Italy should read this Noteholder Circular before doing so. Neither this Invitation, nor the Noteholder Circular or any other document or material relating to the Invitation, will be lodged with, cleared or registered by, the Commissione Nazionale per le Società e la Borsa (CONSOB) pursuant to Italian laws and regulations. Accordingly, neither the Noteholder Circular, nor any other document or material relating to the Invitation, may be distributed or made available in the Republic of Italy.

Liechtenstein

This Invitation is a private invitation; the transaction described herein is, therefore, not nor has it been subject to the review and supervision of the Liechtenstein Financial Market Authority.

Mexico

The information contained in this Invitation has not been reviewed or authorized by the Mexican Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*). The Bonds have not been registered with the National Securities Registry (*Registro Nacional de Valores*) and may not be publicly offered or sold in Mexico, and therefore, the invitation described herein does not constitute a public offering or invitation in Mexico. In making a decision, all Holders, including any Mexican Holders who may sell or purchase bonds from time to time, do so at their own risk.

Turkey

No information in this document is provided for the purpose of offering, marketing and sale by any means of any capital market instruments, including the Bonds, in Turkey. Therefore, this document may not be considered as an offer made or to be made to residents of Turkey. The bonds have not been and will not be registered with the Turkish Capital Market Board (the “CMB”) under the provisions of the Capital Market Law (Law no. 2,499). Accordingly, neither this document nor any other invitation material related to the Invitation may be utilized in connection with any general offering to the public within Turkey without the prior approval of the CMB. However, according to Article 15 (d) (ii) of the Decree No. 32, there is no restriction on the purchase or sale of the Bonds by residents of Turkey, provided that: they purchase or sell such Bonds in the financial markets outside of Turkey; and such sale and purchase is made through banks, and/or licensed brokerage institutions in Turkey.

Uruguay

The Invitation qualifies as a private placement in Uruguay. The Bonds subject to the Invitation are not and will not be registered with the Central Bank of Uruguay.

THE DEALER MANAGER AND THE AGENTS

The Republic has appointed Lazard Frères Banque and Lazard Frères & Co. to act as Joint Dealer Managers, MacKenzie Partners, Inc. to act as Information Agent, Lazard Frères Banque to act as Tender Agent, and Dexia Banque International á Luxembourg to act as Luxembourg Agent in connection with the Invitation. The Joint Dealer Managers may contact Holders regarding the Invitation and may request brokers, dealers, commercial banks, trust companies and custodians to forward the Invitation documents and related materials to beneficial owners of Bonds. The Joint Dealer Managers will also assist Holders with questions relating to the Invitation and the procedures for submitting the Offers and will provide Holders with additional copies of materials relating to the Invitation on request.

The Republic has agreed to pay the Joint Dealer Managers, Tender Agent and Information Agent customary fees for their services in connection with the Invitation. The fees of the Joint Dealer Managers include both an advisory fee as well as a fee based on a percentage of the principal amount of Bonds tendered. The Republic has also agreed to reimburse the Joint Dealer Managers, Information Agent, Tender Agent and the Luxembourg Agent for certain of their out-of-pocket expenses and to indemnify them against certain liabilities in connection with the Invitation.

**ANNEX A:
ISINS, COMMON CODES AND CUSIPS FOR 2012 BONDS AND 2030 BONDS**

2012 BONDS

(A) ISINs and Common Code

	Restricted Global Bonds	Unrestricted Global Bonds
ISIN	US27927WAE21	XS0115748401
Common Code	011574408	011574840

(B) CUSIP 27927WAE2

2030 BONDS

(A) ISINs and Common Code

	Restricted Global Bonds	Unrestricted Global Bonds
ISIN	US27927WAD48	XS0115743519
Common Code	11574386	011574351

(B) CUSIP 27927WAD4

**ANNEX B:
FORM OF LETTER OF TRANSMITTAL**

IMPORTANT NOTE: ONLY THE ATTACHED SIGNATURE ANNEX (THE “SIGNATURE ANNEX”) NEEDS TO BE SUBMITTED TO THE JOINT DEALER MANAGERS.

***IF YOU NEED ASSISTANCE IN COMPLETING THIS LETTER OF TRANSMITTAL, PLEASE
CALL LAZARD FRÈRES BANQUE AT +331 44 13 00 30***

LETTER OF TRANSMITTAL

relating to

**THE REPUBLIC OF ECUADOR
(the “Republic”)**

Invites Holders of its

12 per cent. US Dollar Denominated Global Bonds due 2012 (the “2012 Bonds”) and its US Dollar Denominated Step-Up Global Bonds due 2030 (the “2030 Bonds” together with the 2012 Bonds, the “Bonds”), **to submit, in a modified Dutch auction, offers to sell any or all of the Bonds for cash**

THIS INVITATION WILL EXPIRE AT 6:00 P.M., CET, ON 15 May 2009, UNLESS EXTENDED OR EARLIER TERMINATED BY THE REPUBLIC IN ITS SOLE DISCRETION (THE “EXPIRATION DATE”). OFFERS MAY BE WITHDRAWN AT ANY TIME PRIOR TO THE EXPIRATION DATE.

To:

Lazard Frères Banque

121 Boulevard Haussmann

75382 Paris Cedex 08

France

Attention: Back office Equateur

Reference: The Republic of Ecuador Invitation

Facsimile: +331 44 13 00 39

Telephone: +331 44 13 00 30

as Tender Agent

Dexia Banque Internationale à Luxembourg, société anonyme (69 route d’Esch, L - 2953 Luxembourg, Attention: Transaction Execution Group, facsimile: +352 4590 4227, telephone +352 45901), is acting as Luxembourg Agent for the Invitation. **A copy of any Letter of Transmittal delivered to the Luxembourg Agent must also be delivered to the Tender Agent.**

DELIVERY OF THIS LETTER OF TRANSMITTAL TO AN ADDRESS, OR TRANSMITTAL TO A FACSIMILE NUMBER, OF THE TENDER AGENT OTHER THAN AS SET OUT ABOVE WILL NOT CONSTITUTE A VALID DELIVERY. Deliveries by hand or courier must be clearly marked “Attention: Back Office Equateur; Reference: The Republic of Ecuador Invitation.” Please send only one copy of each Letter of Transmittal to the Tender Agent, whether by hand, courier or facsimile. Please do not send confirmation of any Letter of Transmittal, by the same or different means.

IN NO EVENT SHOULD A HOLDER SEND THIS LETTER OF TRANSMITTAL TO THE INFORMATION AGENT, THE REPUBLIC OR ANY MINISTRY OR AGENCY OF THE REPUBLIC.

AGREEMENTS AND ACKNOWLEDGEMENTS

The person or entity signing the Signature Annex hereto (the “Undersigned”) acknowledges receipt of the description of the Invitation dated 20 April 2009 (which together with this Letter of Transmittal constitutes the “Invitation”) pursuant to which the Republic invites the Holders (as defined in the Invitation) to submit one or more offers to sell any or all of their Bonds to the Republic for cash (each, an “Offer”), on the terms and conditions set forth in the Invitation.

Capitalised terms used but not defined herein have the same meanings given to them in the Invitation.

The Undersigned hereby submits an Offer to the Republic to sell the Bonds specified in the Signature Annex hereto on the terms and conditions set out in the Invitation. (If the Undersigned has attached more than one completed copy of the Signature Annex, the Undersigned hereby submits a separate Offer with respect to each such completed copy of the Signature Annex.) The Undersigned acknowledges that this Letter of Transmittal will not be considered to have been duly completed unless and until:

1. the Tender Agent and, if applicable, the Luxembourg Agent has received the Signature Annex hereto, duly completed and signed; and
2. a direct participant in Euroclear or Clearstream, as the case may be, has delivered Bond Instructions with respect to the Bonds. Please note that Bond Instructions must be delivered no later than 6:00 P.M., CET, on the Expiration Date, unless this deadline is extended through notice to Euroclear and Clearstream or by press release issued to the News Services.

The Undersigned hereby:

- (a) represents that it has delivered Bond Instructions with respect to the Bonds specified in the Signature Annex hereto to Euroclear or Clearstream, as the case may be, by encrypted electronic mail according to those institutions’ normal procedures;
- (b) further authorises the Joint Dealer Managers, the Tender Agent, Euroclear and Clearstream to take those actions specified in the Invitation with respect to the Bonds specified in the Signature Annex hereto;
- (c) further authorises the Joint Dealer Manager, the Tender Agent and the Luxembourg Agent, if applicable, to instruct Euroclear or Clearstream, as the case may be, as to the aggregate number of such Bonds that shall have been accepted for purchase pursuant to the Invitation; and
- (d) represents that it has instructed Euroclear or Clearstream, as the case may be, as to the account to which the Clearing Price should be credited.

The Undersigned hereby represents and warrants that the Undersigned owns, or has confirmed that the party on whose behalf the Undersigned is acting owns, on the date of submission, the Bonds being offered and has full power and authority to sell, assign and transfer the Bonds offered hereby, and that, if such Bonds are accepted for purchase pursuant to the Invitation, as of the Settlement Date, the Republic (or the person nominated, through the Tender Agent for these purposes) will acquire good and marketable title thereto, free and clear of all liens, charges, claims, encumbrances, interests, rights of third parties and restrictions of any kind and such Bonds are not subject to any adverse claim or right. The Undersigned will, upon request, execute and deliver any additional documents deemed by the Joint Dealer Managers, the Tender Agent or by the Republic to be necessary or desirable to complete the sale, assignment and transfer of the Bonds offered hereby.

The Undersigned hereby acknowledges that this Letter of Transmittal constitutes an irrevocable Offer to sell the Bonds specified in the Signature Annex hereto, on the terms and subject to the conditions of the Invitation (and subject to the Republic’s right to terminate or amend the Invitation at any time in its sole discretion and to a Holder’s right to withdraw this Letter of Transmittal prior to the Expiration Date). The Republic’s acceptance for payment of Bonds offered pursuant to the procedures described in the Invitation will constitute a binding agreement between the Undersigned and the Republic in accordance with the terms and subject to the conditions of the

Invitation. For the purposes of the Invitation, the Undersigned understands that Bonds validly offered (or Bonds defectively offered with respect to which the Republic has, or has caused to be, waived such defect) will be deemed to have been accepted by the Republic if, as and when the Republic gives written notice thereof to the Joint Dealer Managers.

Neither of the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent makes any representations whatsoever regarding the Invitation or the Bonds. The responsibility for the Invitation rests solely with the Republic. Accordingly, the undersigned hereby acknowledges and agrees that:

- (i) neither the Joint Dealer Managers nor anyone acting on their behalf has independently verified the Invitation and neither the Invitation nor the form and substance of the disclosure contained in the Invitation has been approved by the Joint Dealer Managers;
- (ii) the Joint Dealer Managers make no representation or warranty, express or implied for the accuracy, completeness or adequacy of information contained in the Invitation or in any further information, notice or other document which may at any time be supplied in connection with the Invitation; and
- (iii) no liability to any party is accepted by the Joint Dealer Managers in connection with any of the above matters.

The Undersigned agrees and acknowledges that any payment of the Clearing Price in respect of the Bonds that are specified in the Signature Annex hereto that is made by or on behalf of the Republic to Euroclear or Clearstream for onward distribution to the Undersigned will discharge the payment obligations of the Republic pursuant to the Invitation in an amount equal to the amount of the payment so received.

All authority conferred or agreed to be conferred by this Letter of Transmittal shall not be affected by, and shall survive, the death or incapacity of the Undersigned, and any obligation of the undersigned hereunder shall be binding upon the heirs, executors, administrators, trustees in bankruptcy, personal and legal representatives, successors and assigns of the Undersigned.

The Undersigned understands that the delivery of any Bonds is not effective until receipt by the Tender Agent of this Letter of Transmittal, or a manually signed facsimile hereof, properly completed and duly executed, together with all accompanying evidences of authority and any other required documents in form satisfactory to the Republic. All questions as to form of all documents and the validity (including time of receipt) and acceptance of Offers and withdrawals of Bonds will be determined by the Republic, in its sole discretion, which determination shall be final and binding.

By signing this Letter of Transmittal, the undersigned hereby irrevocably: (i) releases and discharges any and all claims it may have against the Joint Dealer Managers arising out of or in relating to the Invitation or the transactions contemplated thereby (the “Claims”); and (ii) agrees not to sue the Joint Dealer Managers with respect to the Claims in any jurisdiction.

This Letter of Transmittal shall be governed by and construed in accordance with the laws of England.

<p>THIS LETTER OF TRANSMITTAL WILL NOT BE VALID FOR ANY PURPOSE UNLESS ONE OR MORE COPIES OF THE SIGNATURE ANNEX HERETO IS SIGNED AND THE OTHER REQUIREMENTS OF THE INVITATION ARE MET.</p>
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INSTRUCTIONS

Forming Part of the Terms of the Invitation

1. *Delivery of Letter of Transmittal.* A properly completed and duly executed Letter of Transmittal (or manually signed facsimile thereof) and any other documents required by this Letter of Transmittal, must be received by the Tender Agent, and, if applicable, the Luxembourg Agent, at the address set out on the cover page hereto at or before 6:00 P.M., CET, on the Expiration Date. All Bond Instructions must be received by Euroclear or Clearstream, as the case may be, at or before 6:00 P.M., CET, on the Expiration Date, or such earlier time and date as such clearing system may require, unless this deadline is extended by the Republic through notice to Euroclear and Clearstream or by press release issued to the News Services.

Each Letter of Transmittal submitted with respect to Bonds held in Euroclear or Clearstream must contain a reference code for each Offer.

Direct participants in Euroclear and Clearstream must include in each Letter of Transmittal that is submitted pursuant to the Invitation the reference code for the Bonds that is generated by Euroclear or Clearstream upon the submission of blocking instructions. If you wish to tender Bonds held through any other clearing system than Euroclear or Clearstream, you must arrange either to (i) transfer the Bonds to either Euroclear or Clearstream, or (ii) have such other clearing system submit a tender on your behalf through Euroclear or Clearstream (assuming such other clearing system is capable of doing so). This process will take additional time.

Each Letter of Transmittal must have the same reference code as the Bond Instructions relating to it. No two Letters of Transmittal may contain the same reference code.

The Republic in its sole discretion, may consider invalid any Letter of Transmittal submitted without such reference code, or with a reference code that does not match the reference code in the corresponding Bond Instructions.

The method of delivery of this Letter of Transmittal, the Bonds and all other required documents, including delivery through Euroclear or Clearstream is at the option and risk of the Holder and, except as otherwise provided in this Instruction 1, delivery will be deemed made only when actually received by the Tender Agent.

No alternative, conditional or contingent Offers will be accepted. All Holders, by execution of this Letter of Transmittal (or a facsimile thereof), waive any right to receive any notice of the acceptance of their Offer.

2. *Signatures of Letter of Transmittal.* The Signature Annex attached to this Letter of Transmittal may be signed only by a direct participant in Euroclear or Clearstream as the case may be.
3. *Transfer Taxes.* Except as set forth in this Instruction 3, the Republic will pay or cause to be paid any Ecuadorian transfer taxes with respect to the transfer and sale of Bonds to it, or to its order, as described in the Description of Invitation. If payment of the Clearing Price is to be made to any person other than the Holder, the amount of any transfer taxes payable on account of the payment to such other person will be deducted from the Clearing Price unless satisfactory evidence of the payment of such taxes or exemption therefrom is submitted.
4. *Requests for Assistance or Additional Copies.* Questions and requests for assistance may be directed to the Joint Dealer Managers at the address and telephone number set out on the cover page hereto. Additional copies of this document, the Invitation and related materials may be obtained from the Information Agent or the Luxembourg Agent.

IMPORTANT: This Letter of Transmittal (or a facsimile hereof), together with Bond Instructions and all other required documents, must be received by the Tender Agent and, if applicable, the Luxembourg Agent, at or before 6:00 P.M., CET, on 15 May 2009, the Expiration Date.

SIGNATURE ANNEX – REPUBLIC OF ECUADOR INVITATION

PLEASE READ THE ENTIRE LETTER OF TRANSMITTAL AND THE DESCRIPTION OF INVITATION CAREFULLY BEFORE COMPLETING THIS SIGNATURE ANNEX.

INFORMATION AS TO THE OFFER BEING SUBMITTED

**All questions must be answered unless otherwise indicated below. In the event that more than one Offer is to be submitted, please use a photocopy of this Signature Annex.
Do not submit multiple Offers on the same Signature Annex.**

THE SIGNATURE ANNEX MAY ONLY BE COMPLETED BY THE DIRECT PARTICIPANT IN EUROCLEAR OR CLEARSTREAM HOLDING THE BONDS TO WHICH THIS SIGNATURE ANNEX RELATES. IF YOU ARE HOLDING BONDS THROUGH A CUSTODIAN, ONLY YOUR CUSTODIAN (OR THE DIRECT PARTICIPANT IN EUROCLEAR OR CLEARSTREAM HOLDING FOR YOUR CUSTODIAN) MAY COMPLETE THIS SIGNATURE ANNEX ON YOUR BEHALF.

IN THIS SIGNATURE ANNEX, YOU MAY ONLY SPECIFY A SINGLE OFFER PRICE PER SERIES OF BONDS. ACCORDINGLY, IF YOU WISH TO SPECIFY MORE THAN ONE OFFER PRICE FOR EITHER SERIES OF BONDS, SEPARATE SIGNATURE ANNEXES MUST BE SUBMITTED.

1. Name of Beneficial Owner (Optional but strongly recommended) _____

Contact Person _____

Address _____

Telephone (with international dialling code) _____

Facsimile (with international dialling code) _____

2. Contact information of the Direct Participant in Euroclear or Clearstream submitting this Letter of Transmittal Signature Annex:

Company Name _____

Contact Person _____

Address _____

Telephone (with international dialling code) _____

Facsimile (with international dialling code) _____

3. Reference code generated by Euroclear or Clearstream upon the submission of blocking instructions: _____

4. Name of Clearing System (*please tick only one*):

- Euroclear Clearstream

5. Account number of Direct Participant in Clearing System referred to above where Bonds are held and the Clearing Price is to be credited:

Please ensure you complete and submit one Signature Annex for each submission of Bond Instructions.

6. **Offer Price for 2012 Bonds:**

Please tick only one of the following boxes

- This is a Competitive Offer

Offer Price: U.S.\$ _____. Must be an increment of U.S.\$1.00.

- This is a Non Competitive Offer

The Offer Price for the 2012 Bonds should be expressed in U.S. dollars as a price per U.S.\$1,000 face amount of the applicable Bond and in increments of U.S.\$1.00 (Offers expressed in other increments will be rounded upward to the nearest U.S.\$1.00). The Offer Price should not be less than the 2012 Minimum Clearing Price.

Offer Price for 2030 Bonds:

Please tick only one of the following boxes

- This is a Competitive Offer

Offer Price: U.S.\$ _____. Must be an increment of U.S.\$1.00.

- This is a Non Competitive Offer

The Offer Price for the 2030 Bonds should be expressed in U.S. dollars as a price per U.S.\$1,000 face amount of the applicable Bond and in increments of U.S.\$1.00 (Offers expressed in other increments will be rounded upward to the nearest U.S.\$1.00). The Offer Price should not be less than the 2030 Minimum Clearing Price.

	ISIN Number	Common Code	Number of Bonds	Aggregate Face Amount
2012 Bonds	US27927WAE21 (Restricted)	011574408 (Restricted)		
	XS0115748401 (Unrestricted)*	011574840 (Unrestricted)*		

	ISIN Number	Common Code	Number of Bonds	Aggregate Face Amount
2030 Bonds	US27927WAD48 (Restricted)	11574386 (Restricted)		
	XS0115743519 (Unrestricted)*	011574351 (Unrestricted)*		

*delete as applicable

The Undersigned hereby makes all acknowledgments, representations, warranties, consents, agreements and authorisations described in the Letter of Transmittal to which this Signature Annex relates:

Company: _____

Signed by Authorised Signature: _____

Name of Authorised Signature: _____

Title: _____

Date: _____

THE TENDER AGENT

Lazard Frères Banque

121 Boulevard Haussmann
75382 Paris Cedex 08
France
Telephone: +33 1 44 13 00 30

THE LUXEMBOURG AGENT

**Dexia Banque International à
Luxembourg, société anonyme**

69 route d'Ersch L-2953
Luxembourg
Telephone: +352 4590 1

THE INFORMATION AGENT

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In London

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United Kingdom
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8057

Any questions or requests for assistance or for additional copies of this document and the Letter of Transmittal may be directed to the Joint Dealer Managers, Tender Agent, Luxembourg Agent or Information Agent at its telephone numbers set forth herein.

THE JOINT DEALER MANAGERS

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Lazard Frères Banque

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THE REPUBLIC OF ECUADOR