

URUGUAY

1. General trends

In the economic history of Uruguay, 2014 was a landmark year, marking as it did the twelfth consecutive year of expansion in a country traditionally characterized by low long-term growth and sharply fluctuating levels of activity.

Uruguay's GDP grew by 3.5% in 2014. Although this was above the regional average, it represented a marked slowdown from the expansion of 5.1% seen in 2013 and was the country's second lowest growth rate since 2004.

This slowdown is forecast to continue in 2015, although the country is still expected to outperform the regional average. Specifically, estimates of GDP growth in 2015 range between 2% and 3%, although some analysts expect rather less. Some of this growth will come from manufacturing, thanks to a new paper pulp mill that began operating in mid-2014, and from continued buoyancy in domestic demand, since global demand will be depressed.

The outcome of the October 2014 elections was another parliamentary majority for the ruling party, which thus remained in power. The new government benefits from a favourable social situation, with historically low levels of poverty and unemployment, little debt and good access to international credit. On the economic front, the major challenges it faces in the short term are to keep control of inflation (which has consistently exceeded the target range), reduce the fiscal deficit and maintain an acceptable level of economic activity in a more uncertain international context. With regard to the first of these, the government will have a crucial part to play in wage council negotiations between June 2015 and January 2016 that will create the framework for pay rises over the coming years. Its goal is to establish a framework that enables it to de-index the economy while catering to the needs of sectors (essentially tradable ones) that may have difficulty competing. A more restrictive fiscal policy is therefore likely, probably accompanied by a less contractionary monetary policy. In the medium term, the government needs to find the fiscal space to make good on its pre-election promises to set up a national care system and reform education.

2. Economic policy

(a) Fiscal policy

In 2014, the public sector ran a deficit of 3.4% of GDP, 1 percentage point more than in 2013. The fiscal deficit has been increasing in recent years, driven by greater public investment, inflation control measures and rising interest payments on the public debt.

The country continued with its expansionary fiscal policy, boosting aggregate demand via increased investment in State-owned enterprises and cuts in tax rates under certain conditions, as detailed below. Against this backdrop, the new government is expected to make tariff adjustments and reduce investment in State-owned companies over the course of 2015 with a view to cutting the fiscal deficit.

Despite the widening public sector fiscal deficit, though, there is still some scope to increase spending without jeopardizing debt sustainability, so long as net debt continues to be kept relatively low. At the end of December 2014, gross public sector debt was the equivalent of 58% of GDP, while net debt, calculated by subtracting reserve assets, stood at 21% of GDP, down 2 percentage points of GDP on the same period of 2013. In mid-2015 a new five-year budget will be approved, setting out the basis for public expenditure over the next five years. An austerity budget is expected for the first two years of the period, with the possibility of increased spending from 2017 if economic circumstances permit.

In August 2014, the value added tax (VAT) rate was cut by 2% for transactions made by electronic means (credit and debit cards, electronic payment instruments, direct debits, mobile telephones or the Internet) as part of a financial inclusion strategy given expression in Law No. 19210. This act is intended to increase the efficiency of payment methods, promote use of the financial system, reduce informality and combat fraud. A further temporary VAT reduction of 2% is in force for purchases made by certain means, such as debit cards or online bank transfers. The regulations for the act stipulate that from May 2017 onward all wage, pension and benefit payments must be made by bank deposit. The estimated cost of the reform is 0.1% of GDP in foregone tax revenue in its early years.

The government usually revises public tariffs (for electricity, fuel and telephony) in January of each year. Although the reference prices for 2015 suggested that tariffs were due to be lowered substantially, only minor adjustments were actually made. Several analysts have interpreted this as a veiled fiscal adjustment and a sign that the new government is concerned about the tax take, which was indeed below expectations in early 2015.

(b) Monetary policy

The Central Bank of Uruguay is continuing with its contractionary monetary policy, using the expanded M1 monetary aggregate (cash in circulation, demand deposits and savings deposits) as a benchmark. Specifically, the monetary authority intends to gradually bring down year-on-year growth in expanded M1, and in the last quarter of 2014 and the first quarter of 2015 it succeeded in keeping year-on-year movements in this indicator within its target range. By way of example, whereas the range set for year-on-year growth in expanded M1 was between 8% and 10% for the fourth quarter of 2014, the actual figure was 7%, below even the lower bound of the range. This reference band was selected with a view to bringing inflation down to within the target range of between 3% and 7% set for it in July 2014. A breakdown of expanded M1 shows that the money supply has contracted in real terms.

While monetary policy remained contractionary, interest rates on financial management instruments (the short-term central bank debt securities called Monetary Management Bills) fell in late 2014 and early 2015 to between 10% and 14%, a sign that this instrument, which serves to constrict the money supply, was being used less. In a context of lower economic growth in the region and falling capital flows to emerging economies, lastly, the monetary authority decided it was advisable to phase out marginal reserve requirements on foreign-currency deposits, a contractionary measure that had been in force for four years.

(c) Exchange-rate policy

Since its most recent economic crisis, in the early 2000s, Uruguay has maintained a flexible exchange rate. The Uruguayan peso strengthened against the Brazilian real and the euro from mid-2014, and the country's products therefore became less competitive in Brazil and Europe, respectively its second- and third-largest markets. There were major swings in the exchange rate against the Argentine

peso in several months of 2014, with a negative impact on the balance-of-payments trade account both for goods (because of higher consumer goods imports) and services (because of an upsurge in outbound tourism). At the end of 2014, a dollar bought 24.3 Uruguayan pesos (14% more than in December 2013). The dollar began strengthening steadily in early 2015, so that by the end of May it stood at 26.8 Uruguayan pesos, with a rate of around 27.5 pesos expected by the end of the year. In the 12 months to May 2015, the dollar strengthened by 17%. In the current economic climate, a return to the bilateral real exchange rate levels seen in mid-2014 appears unlikely.

(d) Other policies

Uruguay has been involved in negotiations on the trade in services agreement (TISA) of the World Trade Organization (WTO) since mid-2014. This has proved controversial, since the country's traditional trading partners have not been party to these negotiations. TISA aims at taking trade liberalization further than the General Agreement on Trade in Services (GATS) in such areas as licensing, financial services, e-commerce, telecommunications, maritime transport and the temporary movement of natural persons.

It is generally accepted in the country that the increase in production in recent years has strained the existing infrastructure to the limit; upgrading it, particularly the road network, is therefore a priority for the government, which accordingly intends to promote use of Law No. 18786 on public-private partnership contracts for the implementation of infrastructure works and provision of related services, which has hitherto been little applied. The sectors in which public-private participation contracts can operate are highway, railway and port works, electricity, waste disposal and treatment, public works of social interest (prisons, health centres, educational establishments, housing, sports facilities and urban development works) and land settlement projects.

With a view to harmonizing and streamlining its policy instruments, the new government intends to approve the creation of a national competitiveness system, to be overseen by the Office of Planning and the Budget. This will replace the Production Cabinet, the Ministerial Cabinet for Innovation and the Interministerial Foreign Trade Commission, all set up by previous administrations. The purpose of this policy is to address the growing concern that the current model of development based on natural resources, which has been a source of growth in recent years, is showing signs of exhaustion. The initiative sets out from the diagnosis that there was duplication of effort in previous cabinets and that a more systematic and coordinated approach is needed to address the issue of competitiveness, an aspect of productive development that is vitally important given the current state of production factor accumulation.

3. The main variables

(a) The external sector

The current account deficit in 2014 was US\$ 2.623 billion, equivalent to 4.6% of GDP. Capital and financial account surpluses, however, made it possible to finance the deficit and increase reserve assets by US\$ 1.36 billion, equivalent to 2.4% of GDP. The current account deficit was slightly smaller than in 2013, but the net capital and financial account balance diminished by more. The current account balance reflects a performance that differed between the first and second half of the year, particularly as regards services and imports of inputs, as will be seen later.

Exports of goods were up by 1.2% in 2014, reflecting a 3.6% increase in volume and a 2.4% fall in prices. The largest decline was for primary products, particularly soybeans and wheat. The most recent data published by the central bank point to a slight downward trend in exports, chiefly explained by the fall in international prices for commodities, particularly soybeans. The worsening of economic conditions in the region has also contributed to the slowdown in exports, especially to Brazil, a trend that has continued this year. Demand from China has also fallen off in recent months. Income from inbound tourism was down by 8.4% in 2014, mainly because daily spending by tourists was lower and the average stay in the country shorter. This trend was reversed in 2015, however, with an increase in both visitor numbers and the average spend pushing up tourist revenues by 7%.

Imports contracted by 2.4% in 2014, on the back of a sharp drop in oil prices from the middle of the year that pushed down the value of oil imports by 16.2% and will have favourable effects on the trade balance in 2015. Putting oil, distillate products and electricity to one side, other imports were up by 1.8% at the end of 2014. This increase was mainly attributable to durable goods, excluding cars, imports of which fell off from the level they reached at the end of December 2013. Imports of capital goods, chiefly in the area of machinery and equipment, also rose significantly (by 9.4%) in 2013. Outbound tourism rose strongly from late 2013, peaking in the second quarter of 2014 when the price differential with Argentina narrowed, leading to a fall in outbound tourism in late 2014 and early 2015. Consequently, 2014 marked the end of the record services surplus, although data on inbound and outbound tourism in the first quarter suggest that it is likely to return in 2015.

(b) Economic activity

The Uruguayan economy expanded by 3.5% in 2014, with positive annual rates of GDP growth in most sectors of activity. Those contributing the most to growth were gas, electricity and water (specifically electricity generation and distribution, and particularly hydroelectric power, owing to plentiful rainfall), manufacturing industry (chiefly as a result of a new pulp mill becoming operational, since the rest of the sector is showing signs of stagnation) and transport and telecommunications (specifically telecommunications, an ever-expanding sector). In contrast, activity in construction and in the commerce, repair services, restaurant and hotel sectors was down. The performance of construction was attributable to the completion of major investment projects and, in particular, falling investment in real estate, while that of the other sectors reflected the slackness of the tourist season.

On the expenditure side, domestic demand in the final quarter of 2014 was slightly up on the same period of 2013, chiefly as a result of an increase of 4.0% in private sector final consumption spending. Meanwhile, gross capital formation declined and the trade deficit was smaller than in 2013. According to the survey of economic expectations published by the central bank, private sector analysts expect the economy to grow by between 2% and 3% in 2015, although the statistics are flattered by the inclusion of the new paper pulp exports in the first half of the year, worth about 1 percentage point of GDP.

Net foreign direct investment (FDI) contracted by 9% in 2014 to 4.6% of GDP. This was due to the completion of the pulp mill in the first half and a slowdown in real-estate investment in the resort town of Punta del Este after several years of strong activity. This was the lowest level of FDI for eight years.

(c) Prices, wages and employment

Year-on-year inflation stood at 8.26% at the end of December 2014, and at 8.23% in April 2015. Inflation has consistently exceeded the target range of between 3% and 7%, and a number of price restraint measures were therefore taken during 2014 with a view to bringing it down towards this target. The most successful of these concerned public utility tariffs, which increased by less than average consumer prices over the year, although the January 2015 price review (when reference prices were not followed) gave priority to holding down the fiscal deficit over controlling inflation. Economic operators expect inflation of around 8% or 9%, that is, in single digits, but above the target range, as has been the case now for some years.

The performance of the labour market was fairly stable in 2014. The early months of 2015 saw minor reductions in the economic activity and employment rates and an increase in the unemployment rate, which nonetheless remains at a historically low level. Specifically, in February 2015 the economic activity rate stood at 63.3%, the employment rate at 58.8% and unemployment at 7.1%, as compared to figures of 65.7%, 61.1% and 7.0%, respectively, in 2013. Real wages have continued to rise. By way of example, the year-on-year increase in the average real wage at the end of 2014 was 3.5%, and it continued to rise at a similar pace in the first few months of 2015. Pay has risen to a greater extent in the lowest-income sectors of the workforce in recent years, helping to reduce wage income inequality.

Table 1
URUGUAY: MAIN ECONOMIC INDICATORS

	2006	2007	2008	2009	2010	2011	2012	2013	2014 a/
	Annual growth rates b/								
Gross domestic product	4.1	6.5	7.2	4.2	7.8	5.2	3.3	5.1	3.5
Per capita gross domestic product	3.9	6.3	6.8	3.9	7.5	4.8	3.0	4.7	3.1
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	5.3	-10.2	2.1	3.3	-1.5	13.2	-0.5	4.9	2.1
Mining and quarrying	19.0	6.3	1.7	31.1	35.5	-21.1	-2.3	19.7	-9.9
Manufacturing	4.8	8.3	8.1	5.2	2.6	2.0	-5.1	2.1	5.5
Electricity, gas and water	-25.7	50.2	-51.1	11.6	89.3	-24.2	-22.7	56.0	19.4
Construction	7.0	9.3	2.6	2.7	2.4	2.4	15.6	2.0	-1.8
Wholesale and retail commerce, restaurants and hotels	4.6	8.7	11.9	0.9	11.6	7.0	6.1	2.6	0.6
Transport, storage and communications	11.1	16.1	30.7	14.9	15.0	10.7	9.7	9.5	6.6
Financial institutions, insurance, real estate and business services	1.3	2.4	1.3	1.1	1.9	2.2	1.7	2.2	1.4
Community, social and personal services	0.4	3.8	8.0	4.4	3.9	6.9	5.2	6.1	4.8
Gross domestic product, by type of expenditure									
Final consumption expenditure	5.9	6.8	9.1	2.6	8.6	6.7	5.1	5.2	4.0
Government consumption	2.1	4.7	9.3	5.2	3.1	3.7	5.9	5.0	2.5
Private consumption	6.5	7.1	9.1	2.3	9.4	7.2	5.0	5.2	4.2
Gross capital formation	12.1	7.4	25.0	-11.2	15.2	9.9	13.9	8.6	-1.2
Exports (goods and services)	5.6	4.8	8.5	4.5	7.2	5.8	3.1	0.2	1.9
Imports (goods and services)	15.7	5.9	24.4	-8.7	13.7	12.5	13.5	3.5	0.5
Investment and saving c/	Percentajes of GDP								
Gross capital formation	19.5	19.5	23.2	19.6	19.4	20.9	22.8	22.7	21.4
National saving	17.5	18.6	17.5	18.4	17.6	18.0	17.6	17.6	16.8
External saving	2.0	0.9	5.7	1.2	1.8	2.9	5.2	5.1	4.6
Balance of payments	Millions of dollars								
Current account balance	-392	-220	-1,730	-384	-733	-1,374	-2,691	-2,924	-2,623
Goods balance	-499	-545	-1,714	-504	-527	-1,431	-2,361	-1,352	-918
Exports, f.o.b.	4,400	5,100	7,095	6,392	8,031	9,274	9,916	10,256	10,380
Imports, f.o.b.	4,898	5,645	8,810	6,896	8,558	10,704	12,277	11,608	11,298
Services trade balance	409	703	753	1,025	1,157	1,519	1,074	141	1
Income balance	-428	-516	-918	-1,043	-1,503	-1,618	-1,519	-1,842	-1,836
Net current transfers	126	137	148	138	140	156	115	129	129
Capital and financial balance d/	2,791	1,231	3,963	1,972	372	3,938	5,978	5,869	3,983
Net foreign direct investment	1,495	1,240	2,117	1,512	2,349	2,511	2,539	3,027	2,741
Other capital movements	1,296	-9	1,846	460	-1,977	1,427	3,439	2,842	1,242
Overall balance	2,399	1,010	2,233	1,588	-361	2,564	3,287	2,945	1,360
Variation in reserve assets e/	15	-1,005	-2,232	-1,588	361	-2,564	-3,287	-2,945	-1,360
Other financing	-2,414	-5	0	0	0	0	0	0	0
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	99.1	99.3	93.2	91.3	79.9	77.9	76.3	70.8	74.9
Terms of trade for goods (index: 2010=100)	88.6	88.7	94.1	96.9	100.0	101.8	105.7	107.5	111.5
Net resource transfer (millions of dollars)	-52	710	3,045	929	-1,131	2,320	4,459	4,027	2,147
Total gross external debt (millions of dollars)	12,977	14,864	15,425	17,969	18,425	18,345	21,122	22,862	24,192
Employment	Average annual rates								
Labour force participation rate g/	60.8	62.5	62.7	63.4	62.9	64.8	64.0	63.6	64.7
Open unemployment rate h/	11.3	9.8	8.3	8.2	7.5	6.6	6.7	6.7	6.9
Visible underemployment rate h/	13.6	12.9	10.8	9.2	8.9	7.6	7.4	6.9	6.9

Table 1 (concluded)

	2006	2007	2008	2009	2010	2011	2012	2013	2014 a/
Prices	Annual percentages								
Variation in consumer prices (December-December)	6.4	8.5	9.2	5.9	6.9	8.6	7.5	8.5	8.3
Variation in producer prices (December-December)	8.2	16.1	6.4	10.5	8.4	11.1	5.9	6.3	10.6
Variation in nominal exchange rate (annual average)	-1.8	-2.4	-10.8	7.8	-11.2	-3.7	5.1	0.9	13.6
Variation in average real wage	4.3	4.7	3.5	7.4	3.3	4.0	4.2	3.0	3.4
Nominal deposit rate i/	1.7	2.3	3.2	4.0	3.7	4.4	4.2	4.3	4.4
Nominal lending rate j/	10.7	10.0	13.1	16.6	12.0	11.0	12.0	13.3	17.2
Central government	Percentajes of GDP								
Total revenue	21.6	21.0	20.6	20.3	20.7	20.6	19.9	20.7	19.9
Tax revenue	19.0	18.4	18.2	17.9	18.1	18.3	17.9	18.2	17.7
Total expenditure	22.6	22.6	21.7	21.7	21.9	21.1	21.8	22.2	22.2
Current expenditure	21.2	21.1	19.8	20.2	20.2	19.7	20.4	20.8	20.8
Interest	4.2	3.8	2.9	2.7	2.4	2.4	2.3	2.4	2.3
Capital expenditure	1.4	1.5	1.8	1.6	1.7	1.5	1.4	1.4	1.4
Primary balance	3.2	2.1	1.8	1.3	1.2	1.8	0.4	0.9	-0.1
Overall balance	-1.0	-1.6	-1.1	-1.5	-1.1	-0.6	-1.9	-1.5	-2.3
Non-financial public sector debt	60.6	57.2	44.5	53.3	39.9	38.4	40.2	36.9	37.4
Domestic	16.9	14.9	13.2	18.6	13.6	14.9	15.1	12.2	11.3
External	43.7	42.3	31.4	34.7	26.3	23.6	25.1	24.8	26.1
Money and credit	Percentages of GDP, end-of-year stocks								
Domestic credit	...	...	...	15.1	18.4	18.3	17.4	18.6	19.2
To the public sector	...	...	...	-2.3	-2.8	-3.9	-4.9	-4.8	-3.8
To the private sector	...	...	...	19.2	20.4	20.2	20.4	20.4	20.3
Others	...	...	...	-6.0	-5.9	-5.2	-4.6	-5.4	-5.8
Monetary base	4.6	5.7	5.6	5.4	5.4	5.7	6.0	6.4	6.2
Money (M1)	7.6	8.6	8.7	8.7	9.8	10.2	9.9	9.9	8.8
M2	11.8	13.2	13.4	13.7	15.8	16.8	16.5	16.6	15.6
Foreign-currency deposits	33.8	27.4	31.8	25.4	26.5	26.7	25.7	28.3	31.5

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 2005 prices.

c/ Based on values calculated in national currency and expressed in current dollars.

d/ Includes errors and omissions.

e/ A minus sign (-) indicates an increase in reserve assets.

f/ Annual average, weighted by the value of goods exports and imports.

g/ Nationwide total. Up to 2005, urban total.

h/ Urban total.

i/ Local-currency fixed-term deposits, 30-61 days

j/ Business credit, 30-367 days.

Table 2
URUGUAY: MAIN QUARTERLY INDICATORS

	2013				2014				2015	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Gross domestic product (variation from same quarter of preceding year) b/	4.3	3.2	2.5	4.7	4.1	6.0	3.0	4.6	2.4	...
Gross international reserves (millions of dollars)	10,807	11,905	12,564	13,386	13,137	14,701	15,715	16,173	16,376	17,547 c/
Real effective exchange rate (index: 2005=100) d/	78.0	76.4	75.5	76.4	74.6	74.7	77.0	70.2	66.9	65.3 c/
Open unemployment rate e/	6.3	7.2	7.1	6.3	7.0	6.9	6.6	6.5	7.0	...
Employment rate f/	59.7	59.6	59.3	60.4	59.0	59.4	59.0	60.3	60.6	...
Consumer prices (12-month percentage variation)	7.8	8.0	8.0	8.5	8.7	8.1	8.9	8.6	9.6	9.2 c/
Wholesale prices (12-month percentage variation)	5.8	5.6	8.0	6.3	5.2	1.7	3.0	5.8	9.5	11.3 c/
Average nominal exchange rate (pesos per dollar)	19.52	20.35	21.41	19.69	19.11	19.60	21.64	21.40	22.18	22.92
Nominal interest rates (average annualized percentages)										
Deposit rate g/	4.3	4.2	4.5	3.7	4.1	4.1	4.3	4.8	4.3	4.0 h/
Lending rate i/	11.9	12.1	11.9	11.9	12.2	12.1	12.9	16.0	17.5	18.2 c/
Interbank rate	8.8	8.8	8.8	9.0	9.3	9.2	...	...	...	...
Monetary policy rates	8.8	8.8	8.8	9.0	9.3	9.3	...	...	...	...
Sovereign bond spread, Embi Global (basis points to end of period) j/	127	173	139	127	173	235	200	194	192	170
International bond issues (millions of dollars)	-	-	-	500	-	-	2,000	-	-	...
Domestic credit (variation from same quarter of preceding year)	27.5	13.3	18.1	-4.6	10.3	9.6	-4.4	1.6	-5.4	1.0 h/
Non-performing loans as a percentage of total credit	2.8	2.6	2.5	2.4	2.3	2.2	2.0	1.8	1.7	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 2005 prices.

c/ Figures as of May.

d/ Quarterly average, weighted by the value of goods exports and imports.

e/ Urban total.

f/ Nationwide total.

g/ Local-currency fixed-term deposits, 30-61 days

h/ Figures as of April.

i/ Business credit, 30-367 days.

j/ Measured by J.P.Morgan.