Uruguay

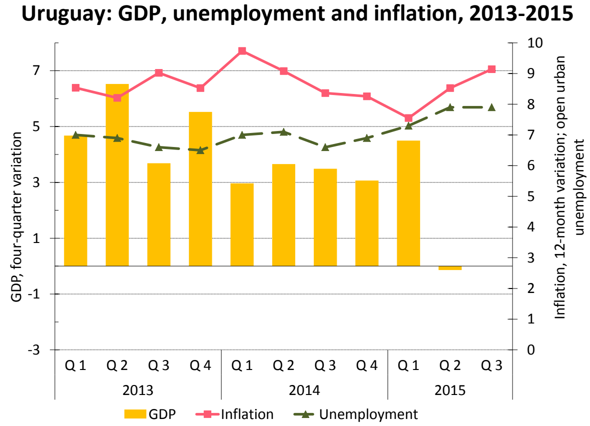
Against a backdrop of great international and regional uncertainty, Uruguay is expected to post moderate economic growth in 2015: around 1.5% for the year as a whole, the lowest rate since the country's most recent economic crisis which occurred in the early years of the new century. Uncertain international demand, stagnating private consumption, and declining private investment are the main factors behind this performance. In this lacklustre context, the new government approved a moderately expansionary budget in order to avoid sending negative signals to business in the country.

Fiscal policy remains expansionary, albeit less so than in recent years, and the public sector continues to drive aggregate demand. In the 12 months ending September 2015, the overall public sector balance stayed in deficit, by 3.5% of GDP, 0.1 percentage points wider than at the previous year's close. The composition of the deficit has also changed. Public enterprises have made a positive contribution to the fiscal accounts, helping to compensate for reduced central government revenue. The lower investments meant that the public sector primary deficit narrowed to 0.1% of GDP; but higher interest payments cancelled out that better primary outturn. The net debt in June 2015 amounted to US$ 12.5 billion, equivalent to 24% of GDP. Given the prevailing economic uncertainty, the government has decided to produce a budget for its first two years only, instead of for a five-year period as is normal. Although the budget is in line with official projections, these are more optimistic than those of the private sector so an additional fiscal effort may be needed in the coming years. On the fiscal front, under the investment promotion policy, temporary stimulus was approved for investments to be undertaken in 2016, reflecting concern about declining private investment levels. The central government has also reached agreement with departmental government representatives to raise the rural property tax.

Monetary policy was heavily influenced by the trend of the dollar. In the second quarter of the year, regulatory changes were made to begin gradually eliminating the marginal reserve requirements applicable to foreign investors purchasing government bonds, which had been established during an episode of massive short-term capital inflows. With a view to raising cash, the government issued a dollar-denominated bond with relatively low interest rates, which was very well received by the market. This was seen as a vote of confidence in the country in a regional context of extreme caution.

In the third quarter, several measures were adopted to cushion the adverse domestic-market impacts of the international financial market volatility. As part of this, the Central Bank of Uruguay (BCU) bought back monetary management bills and agreed on a debt swap with the Ministry of Economy and Finance. The buy-back helped to ease pressures on the foreign-exchange market, by allowing payments to bill holders to be made in dollars, while the debt swap helped to ease the quasifiscal deficit, among other things. These operations caused a drop in available international reserves, thereby reversing the uptrend of recent years.

Uruguay: GDP, unemployment and inflation, 2013-2015



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

Consistently with the foregoing measures, monetary policy has remained contractionary; the target ranges for year-on-year variations in broad M1 have gradually narrowed to fluctuate between 7% and 9% in the third quarter of 2015. Consumer credit, measured in dollars, retreated slightly between January and September 2015, whereas lending to the agriculture and commerce sectors expanded in that period.

In the first 10 months of the year, the dollar exchange rate rose by 21%. Exchange-rate volatility led the central bank to intervene in the market several times, generally to avert spikes in the dollar price. Nonetheless, the real bilateral exchange rate with Brazil, the market with which relative price differences are most significant for Uruguay, remained stable in 2015 (albeit with fluctuations).

The government has taken various measures to ease inflation, which is structurally outside the target range of 3%-7%, with the consumer price index (CPI) up by 9.46% in the 12 months ending November 2015. Because of certain clauses written into employment and pricing contracts, the government's real concern is that inflation may breach the 10% threshold. Several factors combined in driving inflation, which is slightly above the previous year's level. On the one hand, lower aggregate demand and the fall in international prices helped to ease upward pressure on domestic prices. On the other hand, the rising dollar exchange rate increased the cost of imported goods. In July, the government and supermarket chain suppliers agreed to freeze prices on 1,400 articles during the months of August and September.

Uruguay: main economic indicators, 2013-2015

	2013	2014	2015 [a]
	Annual growth rate		
Gross domestic product	5.1	3.5	1.5
Per capita gross domestic product	4.7	3.1	1.1
Consumer prices	8.5	8.3	9.2 [b]
Real average wage	3.0	3.4	1.5
Money (M1)	11.7	6.1	6.9 [b]
Real effective exchange rate [c]	-4.7	5.5	1.8 [b]
Terms of trade	-3.5	3.8	3.4
	Annual average percentage		
Open urban unemployment rate	6.7	6.9	7.9
Central government			
Overall balance / GDP	-1.5	-2.3	-2.8
Nominal deposit rate [d]	4.3	4.4	5.0 [b]
Nominal lending rate [e]	13.3	17.2	16.9 [b]
	Millions of dollars		
Exports of goods and services	13,738	13,671	12,199
Imports of goods and services	14,849	14,494	12,454
Current account balance	-2,825	-2,538	-2,265
Capital and financial balance [f]	5,748	3,898	738
Overall balance	2,923	1,360	-1,527

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
a Estimates.
b Figures as of October.
c A negative rate indicates an appreciation of the currency in real terms. Refers to the extraregional real effective exchange rate.
d Deposit rates in local currency for 31 to 60 days.
e Business credit, 30-367 days.
f Includes errors and omissions.

In 2015, Uruguay's trade deficit narrowed from the previous year's figure, thanks to a larger fall in imports than in exports, which were down by around one sixth. The main components of both flows have shrunk overall, although half of the decline in exports was attributable to falls in both prices and volumes of agricultural exports (basically soybeans). On the import side, 40% of the reduction is explained by a drop in oil imports. On the services account, all categories showed downturns on average, except exports of travel services, which rose during the year thanks to a successful tourism season. Nonetheless, this positive change was partly offset by a widening of the income account deficit, as a result of larger remittances abroad. Consequently, the balance-of-payments current account deficit is expected to narrow by 0.5 percentage points of GDP. In terms of international trade policy, the government decided to withdraw from the Trade in Services Agreement (TiSA), an initiative involving most developed members of the World Trade Organization (WTO).

Foreign direct investment (FDI) in 2015 was down by about 20% on the previous year's level, owing to regional instability, falling commodity prices and the completion of several large investment projects in 2014.

The slowdown in output growth in 2015 has been the outcome of several balancing factors. On the expenditure side, the key driver was net exports, since both private consumption and investment performed only modestly. On the production side, the fastest-growing sectors have been manufacturing and transport and communications, while construction and the supply of electricity, gas and water are projected to have contracted, the latter owing to inclement weather conditions in the first half-year.

Reflecting the more sluggish economic conditions, labour market indicators deteriorated gradually during the year. Activity and employment rates fell by 2 and 3 percentage points, respectively, between late 2014 and September 2015, whereas the national unemployment rate rose by over one percentage point in the same period, to reach 8.0%. Real wages in the second semester were unchanged from their year-earlier level, following several years of continuous expansion.

In addition to the increase in tax benefits for investments noted above, the government plans to drive a robust infrastructure programme starting in 2016. This will include public works concessions under the public-private partnership mechanism —an instrument that looks set to be used more widely in the coming years. Amid great regional and global uncertainty, economic growth will likely remain weak in 2016, with GDP rising by 1.5%, depending partly on the economic performance of Uruguay’s two neighbours, Argentina and Brazil.