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Uruguay Strategy Flash

The fiscal balance clocks in at -4.5% of GDP in October

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Uruguay's fiscal position worsened in October, with a slight drop in income sources facing stable expenditures. The Government's policy agenda continues to concentrate on bolstering disposable income and real wages after the high inflation in 2022 put a strain on salaries. The administration still strives to consolidate the fiscal position, conveying a strong commitment to balancing government accounts in the medium term. However, its recent policy response to the drought has halted fiscal consolidation for the time being, with the climatic conditions being especially hard on revenue streams. In October, non-financial public sector income printed 27.4pp of GDP (-0.1pp relative to September). On the spending side, expenditures came at 29pp of GDP (+0.0pp relative to September), with a minor reshuffle inside the segment. In this context, the primary fiscal deficit excl. cincuentones came at -1.8pp of GDP, flat relative to September, and accumulating a 1pp deterioration YTD. The consolidated public sector deficit excl. cincuentones followed suit, worsening relative to September. In this context, the headline deficit stood over the 3pp of GDP mark for a full year now. October's print came in at -4.5% of GDP— up from -4.4% of GDP in September, -4.2% in August, and -4.1% in July—.

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In October, non-financial public sector income printed 27.4pp of GDP (-0.1pp relative to September). Central Govt & SocSec income clocked in at 27.4pp of GDP in October (-0.1pp relative to September). Even if the variation was minor, there were compensating changes in both directions inside the segment. Tax revenues experienced a positive change this month, improving timidly (+0.1pp) relative to September. However, the improvement was offset by a -0.1pp reduction in other income sources. Soc. Sec. contributions remained stable relative to September, which was mostly the case for the rest of the sectors. On the other hand, the SOEs' primary balance, one of the main drivers of 2022's fiscal overperformance, came in at +0.9pp, worsening by -0.1pp relative to September's figures. Finally, the primary balance of Munis & BSE continues to stand at the +0.1% of GDP mark. All in all, non-financial public sector income in October worsened by -0.1pp relative to September.

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On the spending side, expenditures came at 29pp of GDP (+0.0pp relative to September), with a minor reshuffle inside the segment. In October, the COVID Fund balance totaled -0.1pp of GDP— remaining stable relative to September and reducing its size by 0.5pp YTD. In this context, Central Govt & Soc. Sec. expenditures totaled 26.6pp (+0.2pp relative to September), mainly as Soc.Sec outlays experienced a +0.1pp increase, in addition to very timid increases in Wages and Non-personnel expenditure, which completed the picture. Instead, Public investment dropped by +0.2pp relative to September, with the segment standing at 2.5pp of GDP mark, offsetting the increase in Central Govt. Outlays. With non-financial public sector income dropping by -0.1pp, non-financial public sector outlays remaining level, and cincuentones revenues standing at 0.1pp of GDP, the primary deficit excl. cincuentones stood at -1.8pp in October—showing no variation relative to September, while showcasing increases relative to August's (-1.5) and July's (1.6pp) figures—.

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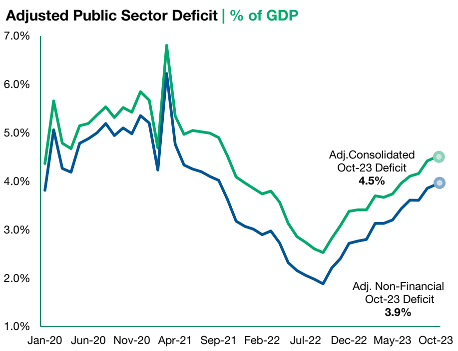
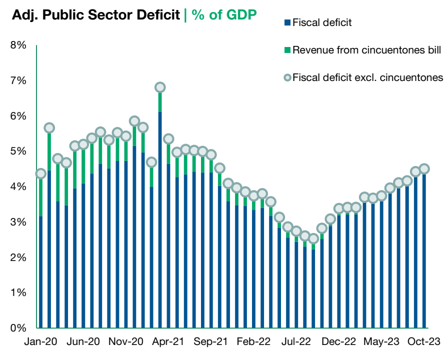
With only two months remaining, the substantial deviation from fiscal targets suggests the administration will have trouble complying with the first pillar of the fiscal rule for the first time in its tenure. The administration has made a significant effort to cleanse public finances since the start of its tenure, and the major effect of the drought on the economy has generated a slowdown in revenue streams and forced the administration to deploy some fiscal stimuli. However, the administration is carrying a significant deviation from this year's fiscal targets, which already proposed no additional fiscal consolidation, leaving the fiscal position flat relative to 2022. In this context, the government envisages the fiscal deficit to total -3.3pp of GDP, now carrying nearly a 1.2pp deviation from year-end targets. In this context, after complying with all three pillars of the fiscal rule since its creation, it seems these are increasingly becoming under threat. While the government should be able to meet both the requirements regarding the cap to the increase in primary expenditure and the net indebtedness cap, the first pillar, the binding structural balance, does seem more difficult to accommodate. The budget law establishes a -2.7% structural deficit for 2023. With the headline figures exhibiting a -4.5% deficit, it is difficult to envisage a convergence to the target by year-end. Still, after an expenditure-heavy 4Q22 that collected significant one-off outlays, the rolling 12m figures should showcase an improvement in November and December. We expect the fiscal deficit to close near the -3.5% mark in 2023. Even if the administration has some leeway this year due to the drought, if it misses the 2023 targets, the chances of fulfilling the planned consolidation for 2024 (which would drive the deficit back to -2.6% of GDP in 2024), would deteriorate considerably. This could be concerning given the chances of the administration executing a considerable fiscal consolidation in an electoral year are already low, especially as the govt. coalition does not part as the top dog in the race, trailing the FA in voting intention. We believe that, under severe political strain, for 2024 we expect the need to win back voters should prime over any consolidation effort the administration is prepared to execute, a problem which could compound with the possibility of a bloated 2023 deficit. In this scenario, we continue to believe the slow but steady deterioration of the fiscal position is credit negative, even if we don't expect it to affect valuations in the short run, with the widening fiscal deficit threatening compliance with the fiscal rule this year.

Figure 1: October's fiscal figures





12m rolling - as % of GDP	Dec-21	Dec-22	Sep-23	Oct-23	Dec-23*	Dec-24*
NFPS Income	**26.7%**	**27.1%**	**27.5%**	**27.4%**	**25.8%**	**26.0%**
Central Government	**18.9%**	**19.3%**	**19.4%**	**19.4%**	**18.9%**	**19.0%**
Tax Revenues	*15.9%*	*16.5%*	*16.6%*	*16.7%*	*16.1%*	*16.2%*
International Trade	*1.1%*	*1.1%*	*1.1%*	*1.1%*	*1.1%*	*1.1%*
Others	*1.8%*	*1.7%*	*1.7%*	*1.7%*	*1.7%*	*1.8%*
Soc.Sec contributions	6.4%	6.8%	7.1%	7.1%	6.9%	7.0%
SOE primary balance	1.4%	1.0%	1.0%	0.9%	0.1%	0.3%
BSE &Munis primary balance	0.2%	0.1%	0.0%	0.0%	0.1%	0.1%
BCU primary balance	0.0%	-0.1%	0.0%	0.0%	-0.1%	-0.1%
NFPS Outlays	**27.5%**	**27.8%**	**29.0%**	**29.0%**	**26.6%**	**26.3%**
Central Govt. Primary Outlays	25.8%	25.4%	26.4%	26.6%	25.3%	25.2%
Personnel spending	*4.6%*	*4.6%*	*4.8%*	*4.9%*	*4.6%*	*4.6%*
Non-Personnel spending	*4.3%*	*3.9%*	*3.8%*	*3.9%*	*3.5%*	*3.5%*
Pensions	*9.0%*	*8.9%*	*9.3%*	*9.4%*	*9.1%*	*9.1%*
Transfers	*7.9%*	*8.0%*	*8.4%*	*8.4%*	*8.1%*	*8.0%*
Public investment	1.8%	2.4%	2.6%	2.5%	*1.2%*	*1.1%*
Public Sector Primary Balance	-0.7%	-0.6%	-1.7%	-1.7%	-0.8%	-0.3%
Interest payments	2.8%	2.6%	2.7%	2.7%	2.4%	2.3%
Consolidated Public Sector Deficit	-3.5%	-3.2%	-4.3%	-4.4%	-3.2%	-2.5%
Cincuentones revenues	-0.5%	-0.2%	-0.1%	-0.1%	0.0%	0.0%
Adjusted Consolidated Public Sector Deficit	**-4.0%**	**-3.4%**	**-4.4%**	**-4.5%**	**-3.3%**	**-2.6%**

Source: TPCG Research based on MEF

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