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Uruguay Strategy Flash

The fiscal balance clocks in at -4.0% of GDP in July

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Uruguay's fiscal position came in unchanged in July, with increasing income sources matching the rise in 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 July, non-financial public sector income printed 27.5pp of GDP (+0.1pp relative to June). The increase came mainly from a recovery in Soc.Sec contributions, which drove the hike. On the spending side, expenditures came at 28.9pp of GDP (+0.2pp relative to June), with increasing Soc. Sec. outlays and Transfers. In this context, the primary fiscal deficit excl. cincuentones came at -1.3pp of GDP, worsening by -0.1pp relative to June, and accumulating a 0.8pp deterioration YTD. In this context, the -0.1pp variation in the primary position in July was accounted for by a 0.1pp hike in NFPS income, and a 0.2pp increase in NFPS outlays. Inversely, the consolidated public sector deficit excl. cincuentones remained level due to a reduction in interest payments. In this context, the headline deficit stood over the 3pp of GDP mark for the ninth month running. July's print came in at -4.0% of GDP— stable from 4.0% of GDP in June, albeit up from 3.7% in May, April, and March—.

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On the spending side, expenditures came at 28.9pp of GDP (+0.2pp relative to June), with increasing Soc. Sec. outlays and Transfers. In July, the COVID Fund balance totaled -0.1pp of GDP— dropping by -0.1pp relative to June and reducing its size by 0.5pp YTD. In this context, Central Govt & Soc. Sec. expenditures totaled 26.2pp (+0.2pp relative to June), as Soc.Sec outlays and Transfers experienced twin 0.1pp of GDP rises, contributing 0.2pp to the general increase in expenditure. Public investment showcased no variation relative to June, with the segment standing at 2.7pp of GDP mark, having no effect on the monthly change of the headline deficit. With non-financial public sector income rising by +0.1pp, non-financial public sector outlays increasing by +0.2pp, and cincuentones revenues standing at 0.1pp of GDP, the primary deficit excl. cincuentones stood at -1.3pp in July—over June's 1.2pp print, May's 1.0pp result and April's 0.9pp mark—.

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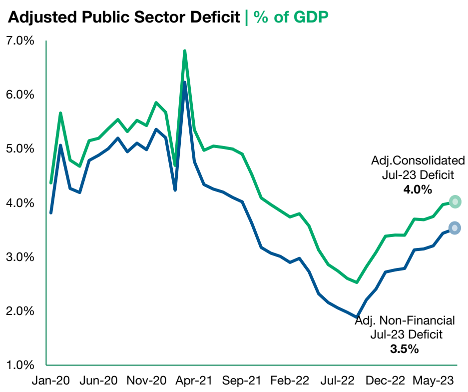
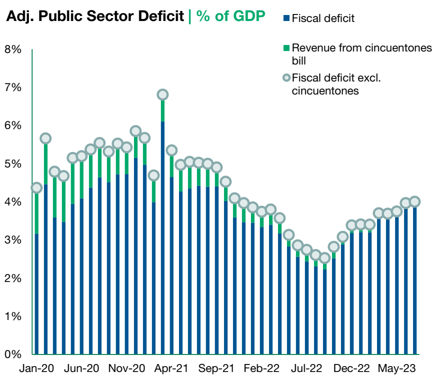
We continue to believe the slow but steady deterioration of the fiscal position is credit negative, even if we don't expect it to affect valuations in the short run, with the widening fiscal deficit starting to threaten compliance with the fiscal rule this year. The administration has made a significant 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 0.6pp 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 under threat. The budget law establishes a -2.7% structural deficit for 2023. With the headline figures exhibiting a -3.9% 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 as the year advances. 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.

Figure 1: July's fiscal figures





12m rolling - as % of GDP	Dec-21	Dec-22	Jun-23	Jul-23	Dec-23*	Dec-24*
NFPS Income	**26.7%**	**27.1%**	**27.5%**	**27.5%**	**25.8%**	**26.0%**
Central Government	**18.9%**	**19.3%**	**19.3%**	**19.3%**	**18.9%**	**19.0%**
Tax Revenues	*15.9%*	*16.5%*	*16.6%*	*16.6%*	*16.1%*	*16.2%*
International Trade	*1.1%*	*1.1%*	*1.1%*	*1.1%*	*1.1%*	*1.1%*
Others	*1.8%*	*1.7%*	*1.6%*	*1.6%*	*1.7%*	*1.8%*
Soc.Sec contributions	6.4%	6.8%	6.9%	7.0%	6.9%	7.0%
SOE primary balance	1.4%	1.0%	1.2%	1.2%	0.1%	0.3%
BSE &Munis primary balance	0.2%	0.1%	0.1%	0.1%	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%**	**28.7%**	**28.9%**	**26.6%**	**26.3%**
Central Govt. Primary Outlays	25.8%	25.4%	26.0%	26.2%	25.3%	25.2%
Personnel spending	*4.6%*	*4.6%*	*4.7%*	*4.8%*	*4.6%*	*4.6%*
Non-Personnel spending	*4.3%*	*3.9%*	*3.7%*	*3.7%*	*3.5%*	*3.5%*
Pensions	*9.0%*	*8.9%*	*9.2%*	*9.3%*	*9.1%*	*9.1%*
Transfers	7.9%	8.0%	8.3%	8.4%	8.1%	8.0%
Public investment	1.8%	2.4%	2.7%	2.7%	*1.2%*	*1.1%*
Public Sector Primary Balance	-0.7%	-0.6%	-1.2%	-1.3%	-0.8%	-0.3%
Interest payments	2.8%	2.6%	2.7%	2.6%	2.4%	2.3%
Consolidated Public Sector Deficit	-3.5%	-3.2%	-3.9%	-3.9%	-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%**	**-4.0%**	**-4.0%**	**-3.3%**	**-2.6%**

Source: TPCG Research based on MEF

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