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Uruguay Strategy View

The fiscal balance clocks in at -3.6% of GDP in February

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Uruguay's fiscal position showcased a very slight widening in February, with a rise in income sources being marginally outpaced by a similar increase in outlays. After a sizable compression in the fiscal deficit during 4Q23, the balance remained relatively stable in the first two months of 2024. The reduction during the last quarter of 2023 clocked in at nearly 0.8% of GDP and was principally driven by Nov-22 and Dec-22 dropping off the 12m rolling figures, as said months had accumulated significant one-off capex and non-personnel expenditures which bloated the fiscal figures until now. Without that effect, the compression in fiscal figures lost significant steam. In February, non-financial public sector income printed 26.9pp of GDP (+0.3pp relative to January). On the spending side, expenditures came at 27.6pp of GDP (+0.3pp relative to January), with the rise propelled by increases in Soc.Sec outlays and Transfers. In this context, the primary fiscal deficit excl. cincuentones came at -0.8pp of GDP, remaining flat relative to January. However, the consolidated public sector deficit excl. cincuentones did not follow suit, on behalf of rising interest payments. In this context, the headline deficit stood over the 3pp of GDP mark for sixteen months in a row. February's print came in at -3.6% of GDP— up from January's -3.5% of GDP gauge, albeit down from -3.8% of GDP in December—.

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In February, non-financial public sector income printed 26.9pp of GDP (+0.3pp relative to January). Central Govt & SocSec income clocked in at 26.9pp of GDP in February (+0.3pp relative to January). The main driver behind the rise was a +0.15pp increase in the Tax Revenue segment, which compounded with very minor increases in Soc.Sec contributions and other Income sources, subsections that also aided the print. The remainder of the segments showcased no variation relative to last month. On the other hand, the SOEs' primary balance, one of the main drivers of 2022's fiscal overperformance, came in at +0.8pp, flat relative to December's figures. Finally, the primary balance of Munis & BSE continues to stand near the neutral position, exhibiting no variation. All in all, non-financial public sector income in February improved by +0.3pp relative to January.

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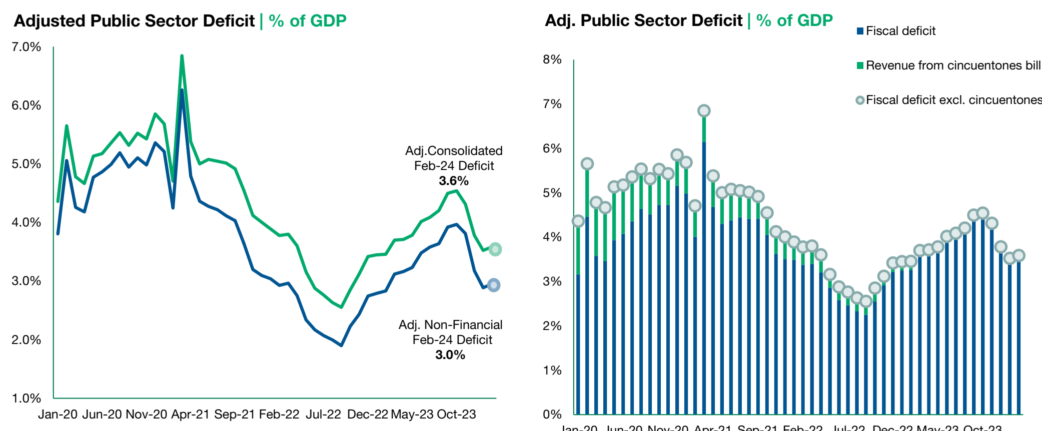
On the spending side, expenditures came at 27.6pp of GDP (+0.3pp relative to January), with the rise propelled by increases in Soc.Sec outlays and Transfers. In February, Central Govt & Soc. Sec. expenditures totaled 25.7pp (+0.3pp relative to January). The hike responded to minor increases in Soc.Sec outlays and Transfers, both of which rose by +0.1pp. In addition, both Personnel and Non-personnel expenditures exhibited small rises, which compounded contributed another +0.1pp to the print. The rest of the segments stood flat relative to January, completing the picture. However, interest payments did exhibit an increase, clocking in +0.1pp over Jan-24 figures. After compressing significantly in December, the compression in Public investment continues to flatline, as the segment remained constant relative to January, standing at 1.9pp of GDP mark. With non-financial public sector income rising by +0.3pp, non-financial public sector outlays rising by +0.3pp, and cincuentones revenues standing at 0.1pp of GDP, the primary deficit excl. cincuentones stood at -0.9pp in February— flat relative to January (-0.9pp), but tighter than December's (-1.1pp) and November's (-1.6pp) figures—.

Figure 1: February's fiscal figures



12m rolling - as % of GDP	Dec-21	Dec-22	Dec-23	Jan-24	Feb-24
NFPS Income	**27.0%**	**27.5%**	**27.7%**	**26.6%**	**26.9%**
Central Government	**19.1%**	**19.6%**	**19.7%**	**18.8%**	**19.0%**
Tax Revenues	*16.1%*	*16.7%*	*16.7%*	*16.0%*	*16.2%*
International Trade	*1.1%*	*1.2%*	*1.0%*	*1.0%*	*1.0%*
Others	*1.9%*	*1.7%*	*1.9%*	*1.8%*	*1.9%*
Soc.Sec contributions	6.5%	6.9%	7.3%	7.0%	7.1%
SOE primary balance	1.4%	1.0%	0.8%	0.8%	0.8%
BSE &Munis primary balance	0.2%	0.1%	0.0%	0.0%	0.0%
BCU primary balance	0.0%	-0.1%	0.0%	0.0%	0.0%
NFPS Outlays	**27.8%**	**28.2%**	**28.6%**	**27.3%**	**27.6%**
Central Govt. Primary Outlays	26.0%	25.8%	26.6%	25.4%	25.7%
Personnel spending	*4.7%*	*4.7%*	*5.0%*	*4.8%*	*4.8%*
Non-Personnel spending	*4.3%*	*4.0%*	*3.6%*	*3.4%*	*3.4%*
Pensions	*9.1%*	*9.0%*	*9.6%*	*9.2%*	*9.3%*
Transfers	*8.0%*	*8.1%*	*8.4%*	*8.0%*	*8.2%*
Public investment	1.8%	2.4%	2.0%	1.9%	1.9%
Public Sector Primary Balance	-0.7%	-0.6%	-1.0%	-0.7%	-0.7%
Interest payments	2.8%	2.7%	2.7%	2.7%	2.8%
Consolidated Public Sector Deficit	-3.5%	-3.2%	-3.7%	-3.4%	-3.5%
Cincuentones revenues	-0.5%	-0.2%	-0.1%	-0.1%	-0.1%
Adjusted Consolidated Public Sector Deficit	**-4.0%**	**-3.4%**	**-3.8%**	**-3.5%**	**-3.6%**

Source: TPCG Research based on MEF

Looking at 2024, we do expect the fiscal balance to improve due to cyclical factors, albeit major consolidation prospects continue to look unlikely. However, we envisage compliance with the fiscal rule, as the administration corrected its estimates upwards. With the final calculation of the structural deficit for 2023 finally complying with the first pillar of the fiscal rule, the administration was able to meet all three fiscal targets for the year, maintaining its very solid track record. According to the MEF, the deficit clocked in at -3.3% of GDP, 0.1pp wider than estimated. However, the structural deficit amounted to -2.7% of GDP, complying with the target established by the fiscal rule. The administration also respected the other two pillars during the year, managing to keep both the growth in real primary outlays and net indebtedness under the established caps. However, it is also true that the administration corrected the fiscal estimates for 2024 significantly and is now expecting a wider structural deficit. Initially, the envisaged target in the Budget Review seemed ambitious on paper, as it planned a 0.7pp consolidation relative to the budget baseline, putting headline figures at -2.6% of GDP by the end of Mr. Lacalle Pou's tenure. Now, said estimate has been corrected to a -3% of GDP deficit, which would result in a structural deficit of -2.9%. So, while headline figures should compress marginally, the structural deficit would widen by +0.2pp, suggesting that the administration's plans for 2024 are much more modest than

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initially envisaged. In addition, said correction practically ensures compliance with the target, as we do expect the efforts to have some baseline tailwind, as 2023's drought caused a significant drop in income sources, which is now bound to reverse, adding between 0.2pp and 0.3pp to revenues this year. This, in conjunction with some minor consolidation efforts, might yield a moderate, but noticeable improvement in fiscal figures this year. However, we believe the chances of the administration executing a considerable fiscal consolidation in an electoral year are 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. In this context, the upward correction in the structural deficit estimate also points in that direction.

CA flows recovered in 4Q23, while FDI flows started diluting

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In other news, 4Q23 BoP flows improved significantly relative to 4Q22, as Uruguay's current account deficit clocked in at USD468mn vs. USD892mn in 3Q23, with the tightening responding mainly to a reduction in Imports and rising Primary Income. Dissecting the tightening, the main driver behind the improvement came on the back of significantly stronger primary income flows, as the latter overperformed 4Q22 figures by +USD476mn, singlehandedly explaining 2/3rds of the current account's quarterly yoy variation. Even against a weak baseline, as 4Q22 was hit by the start of the drought, exports were unable to post an improvement, coming in flat (+USD4mn) in yoy terms. However, during 4Q23, international prices were not as favorable for Uruguayan exports, hampering their development and explaining the weak performance of the sector. On positive news, Imports lost some steam during 4Q23, weakening by -USD206mn relative to 4Q22. This put the change in the Goods balance at +USD211mn. While the Services Balance did clock in the black, its surplus was -USD44mn tighter than that of 4Q22. Service Imports rose by +USD36mn, while Exports dropped by -USD8mn relative to 4Q22, therefore putting the net variation of the Services balance at -USD44mn. All in all, the trade balance posted a +USD593mn surplus (+USD166mn vs 4Q22), finally regaining some ground after an initially weak first nine months of 2023. The other two-thirds of the improvement in Current Account metrics comes from the tightening in the Primary Income balance deficit, while Secondary income was mostly irrelevant for this quarter's BoP print. All in all, the Current Account balance experienced a +USD654mn improvement. In this context, the current account deficit compressed significantly in 12m-rolling terms, clocking in at -3.6% of GDP (-USD2.79bn) for 2023. This figure showcases a significant improvement relative to both the previous 3Q23 print of -4.5% of GDP (-USD3.45bn) and the end-2022 mark (-3.9% of GDP; -USD2.72bn).

Figure 2: 4Q23 BoP figures

USDmn	2021	2022	2023	4Q22	4Q23	Δ
Current account	-1,472	-2,725	-2,797	-1,121	-468	654
Goods & Services	4,505	3,618	2,421	427	593	166
Goods	4,637	3,499	2,083	173	383	211
Exports	15,848	17,040	15,076	3,645	3,649	4
Imports	11,211	13,541	12,992	3,472	3,266	-206
Services	-132	119	337	254	209	-44
Exports	3,791	5,571	6,210	1,659	1,651	-8
Imports	3,923	5,452	5,873	1,405	1,442	36
Primary Income	-6,055	-6,483	-5,385	-1,581	-1,105	476
Secondary Income	78	140	167	34	45	11
Capital account	-30	3	2	-3	0	3
Financial Account	-173	-2,174	-2,331	-1,826	-925	901
Direct Investment	-1,507	-2,956	-4,241	-1,087	-204	883
Portfolio Investment	1,095	1,961	1,362	-266	-184	82
Derivatives	443	374	384	57	170	113
Other Investment	-1,047	24	-683	-178	-1,427	-1,249
Errors & Ommisions	1,329	548	464	-702	-457	244
Reserve Assets	843	-1,578	848	-352	720	1,072
12m-rolling GDP (USDmn)	**60,754**	**70,209**	**77,272**	**70,209**	**77,272**	**7,063**
Balance as % of GDP (12m)	-2.4%	-3.9%	-3.6%	-3.9%	-3.6%	-

Source: TPCG Research based on BCU

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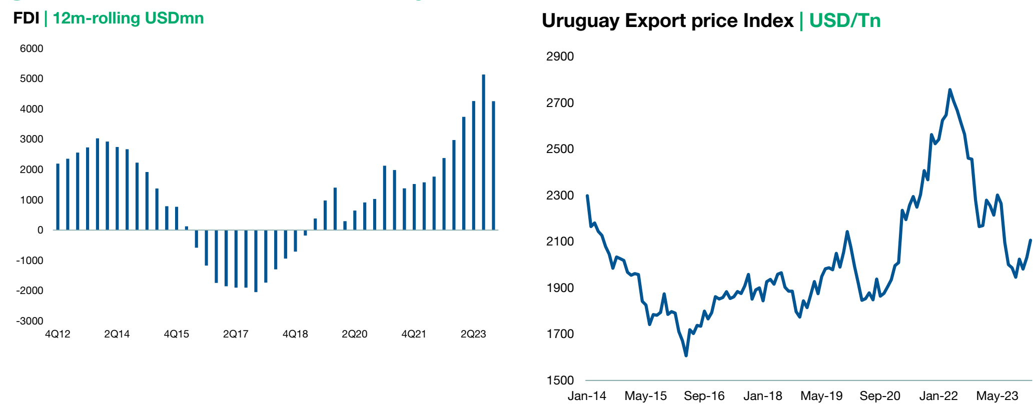
The tightening CA deficit partly explains the relatively flat performance of the FX, while the financial account continued to prove supportive, even if FDI is starting to lose steam after peaking in 3Q23. The performance of the current account during 2023 was foreseeable, posting a very weak first nine months of the year, followed by a relatively stronger 4Q23, which was aided by the baseline effect, as the 4Q22 CA print was very unsupportive. During 2023 exports were hit very hard by climatic factors and prices, plummeting by nearly USD2bn. Still, import dynamics, the services balance, and primary income managed to mostly offset this drop, as the current account balance did not deteriorate significantly relative to 2022, mostly accounted for by a strong 4Q23 and a very weak 4Q22. During this period, the performance of the FX was robust, even appreciating by 2.5% in nominal terms during 2023. Its performance was in turn supported by massive FDI inflows, which posted a significant increase relative to 2022. Specifically, direct investment rose by USD1.3bn relative to 2022. However, the peak in FDI was perceived in 3Q23, when the 12m rolling figures amounted to USD5.1bn. This figure was watered down significantly by the inclusion of the 4Q23, as it dropped to USD4.3bn. So, we find that, during the first three quarters of the year, the financial account via FDI managed to plug the gap caused by a widening CA deficit generated by the drought. However, this trend reversed in 4Q23, with a much more solid CA print managing to hold down the fort, while FDI figures started to dissolve. We believe this dynamic is strongly indicative of the performance of the external sector in 2024. With the UPM II project already completed, and exports bound to recover after the drought, especially agri-flows, we expect FDI figures to continue deteriorating going forward, weakening which should be compensated by a tighter current account deficit throughout the year.

Figure 3: FDI support started to waver, while the CA recovered some ground, even amidst relatively weak international prices.



Source: TPCG Research based on BCU

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