INTERNATIONAL MONETARY FUND

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URUGUAY

February 2020

2019 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR URUGUAY

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2019 Article IV consultation with Uruguay, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its February 19, 2020 consideration of the staff report that concluded the Article IV consultation with Uruguay.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on February 19, 2020, following discussions that ended on December 17, 2019, with the officials of Uruguay on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on January 27, 2020.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Uruguay.

The document listed below has been or will be separately released.

Selected Issues

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INTERNATIONAL MONETARY FUND

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FOR IMMEDIATE RELEASE
February 20, 2020

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Concludes Article IV Consultation for Uruguay

On February 19, 2020, the Executive Board of the International monetary Fund (IMF) concluded the Article IV consultation[1] with Uruguay.

Recent Developments and Outlook

Uruguay is in an enviable position in many respects. The country enjoys political stability, strong governance and institutions, and a high degree of social cohesion. Following a decade and a half of robust growth, it also boasts high per capita income and low levels of poverty, inequality, and informality. Owing to prudent supervision and regulation, the financial sector remains resilient despite regional financial market volatility.

After a growth slowdown during 2018H2–2019H1, economic activity picked up in 2019Q3, with some recovery in consumption, exports, and private investment. The average growth in the first three quarters of 2019 was 0.2 percent. The current account balance has fluctuated around zero, with the positive trade balance offset by a negative income account. Inflation increased to 8.8 percent in December, outside of the target range, despite a negative output gap, due to both temporary factors and above-target expectations.

Spillovers from Argentina have been limited to the real sector and exchange rate channels. The financial sector—which had markedly reduced its exposure to Argentina—remains robust, and the sovereign spreads remain contained at low levels.

Fiscal balances deteriorated substantially. As the economy slowed, revenues declined, and current expenditures continued to increase. The budget for 2020—the last to be prepared by the current government—gives up on the achievement of the 2.5-percent-of-GDP deficit

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

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target and instead foresees a fiscal deficit for the consolidated public sector (CPS) of 4.6 percent of GDP in 2019 (excluding the cincuentones transactions[2]) and 3.8 percent of GDP in 2020. As of November, the twelve-month CPS deficit stood at 4.7 percent of GDP, aided by the impact of a favorable debt management operation in September (0.3 percent of GDP) and by lower interest payments from the central bank. The authorities have successfully issued longer-term bonds at favorable rates to cover their financing needs.

GDP growth is expected to rebound from an estimated 0.5 percent in 2019 to 2.1 percent in 2020 and 2.5 percent in 2021, as private and infrastructure investment projects ramp up, offsetting adverse spillovers from Argentina. Growth is expected to decline after 2021 as these investments run their course—but the level of real GDP is expected to be permanently higher. Inflation is expected to remain at around 8 percent in 2020 and then to decline gradually to the upper limit of the target range as temporary factors wear off and private-sector wage increases follow the declining path agreed in the last round of negotiations.

There are sizable upside and downside risks to the outlook. On the downside, economic developments in Argentina remain an outsized risk, even though the likelihood of direct financial spillovers is small. A host of global factors (trade disruptions, lower growth, abrupt declines in risk appetite, large swings in energy prices) and of local ones (loss of credibility and further increases in debt due to insufficient fiscal adjustment or delayed reforms and PPP projects) may undermine the expected recovery and limit medium-term growth. On the upside, the growth boost from investment projects may be larger than expected, given uncertainty about possible indirect effects.

Executive Board Assessment[3]

Directors commended Uruguay's favorable political economy, strong governance and institutions, a high degree of social cohesion, low levels of poverty, inequality, and informality, and the resilience of the financial sector. At the same time, they noted that domestic imbalances have emerged and debt has risen, while economic growth, investment, and employment have declined, and inflation has remained outside the target range. In this context, they stressed that the political and domestic economic landscape over the next few years presents an opportunity to decisively address these challenges.

Directors noted that, while gross financing needs are manageable due to the authorities' pre-financing policy and robust buffers, a continuation of current fiscal trends could undermine

[2] The proceeds from the large transactions related to the pension reform (*cincuentones*) are recorded as revenue in line with the Fund's methodology.

[3] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

debt sustainability. They agreed that there is a need to introduce a credible adjustment plan to put debt on a firm downward path and welcomed the authorities' commitment in this regard. This would require limiting the increase in current expenditure and reducing tax expenditure, while maintaining adequate provision of key public services and safety nets and preserving capital spending. Pension reforms would also be needed to ensure sustainability and adequate retirement income for future generations. Directors noted that a credible fiscal anchor could be introduced by revamping the medium-term fiscal framework with a binding fiscal rule.

Directors agreed that in the absence of negative shocks, monetary policy should continue to be focused on getting inflation and inflation expectations firmly at the mid-point of the target range. They highlighted the need for further enhancements to the inflation targeting framework and welcomed continued efforts to reduce dollarization and indexation. Improving financial intermediation will also be important. Directors noted that the exchange rate should continue to be used as a shock absorber and that reserve buffers should be kept above prudential norms.

Directors emphasized the importance of structural reforms to raise potential growth and maintain social progress. Closing infrastructure gaps is critical but needs to be complemented by actions to increase productivity growth to raise private investment. They underscored the need to improve education outcomes to help boost youth employment. Further wage flexibility could provide incentives for firms to create more, stable jobs and invest in on-the-job training to reduce the high unemployment. Continued efforts to integrate migrants and women into the labor market will also be important. Directors stressed that corporate governance reform is needed to improve the management and efficiency of state-owned enterprises.

Uruguay: Selected Economic Indicators

	2014	2015	2016	2017	2018	Projections 2019	2020	2021	2022	2023	2024
Output, prices, and employment											
Real GDP (percent change)	3.2	0.4	1.7	2.6	1.6	0.5	2.1	2.5	2.2	2.2	2.2
GDP (US$ billions)	57.2	53.3	52.7	59.5	59.8	57.4	58.4	61.5	64.2	67.0	69.8
Unemployment (in percent, eop)	6.6	7.5	7.9	7.9	8.4	9.2	8.4	7.7	7.5	7.5	7.5
Output gap (percent of potential output)	2.7	0.3	-0.3	0.1	0.0	-1.1	-0.6	-0.1	0.0	0.0	0.0
CPI inflation (in percent, end of period))	8.3	9.4	8.1	6.6	8.0	8.8	8.0	7.5	7.0	7.0	7.0
Exchange rate (UY$/US$, average)	23.2	27.3	30.2	28.7	30.6	...	...	...	...	...	...
Real effective exchange rate (percent change, eop)	-3.1	0.6	-5.7	5.8	2.1	...	...	...	...	...	...
	(Percent change, unless otherwise specified)										
Monetary and banking indicators 1/											
Base money	1.4	7.2	9.7	3.6	10.4	...	...	...	...	...	...
Broader M1 (M1 plus savings deposits)	3.7	5.6	8.4	15.2	8.8	...	...	...	...	...	...
M2	6.4	9.0	14.4	13.4	10.4	...	...	...	...	...	...
Growth of credit to households (in real pesos)	4.7	6.3	-0.5	2.5	1.2	...	...	...	...	...	...
Growth of credit to firms (in US$)	6.8	2.8	1.5	-4.2	2.4	...	...	...	...	...	...
Bank assets (in percent of GDP)	64.4	75.8	68.7	64.6	66.3	...	...	...	...	...	...
Private credit (in percent of GDP) 2/	27.1	30.2	28.1	26.1	27.4	...	...	...	...	...	...
	(Percent of GDP, unless otherwise specified)										
Fiscal sector indicators 3/											
Revenue NFPS	29.1	29.0	29.3	29.7	31.3	30.8	30.6	30.4	30.5	30.5	30.6
excluding *cincuentones* transactions	29.1	29.0	29.3	29.7	30.0	29.6	29.7	30.0	30.3	30.5	30.6
Cincuentones transactions	0.0	0.0	0.0	0.0	1.3	1.2	0.9	0.4	0.2	0.0	0.0
Primary expenditure NFPS	29.5	28.8	29.9	29.8	30.6	31.1	31.0	30.7	30.9	31.0	31.0
Primary balance NFPS	-0.5	0.1	-0.5	-0.1	0.60	-0.6	-0.5	-0.3	-0.4	-0.5	-0.4
excluding *cincuentones* transactions	-0.5	0.1	-0.5	-0.1	-0.7	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Primary balance BCU	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Interest NFPS	2.3	2.3	2.6	2.6	2.6	2.4	2.7	2.8	2.8	2.8	2.8
Interest BCU	0.6	1.3	0.7	0.7	0.8	0.5	0.5	0.2	0.2	0.3	0.3
Overall balance NFPS	-2.8	-2.2	-3.1	-2.7	-2.0	-3.0	-3.2	-3.0	-3.2	-3.3	-3.2
excluding *cincuentones* transactions	-2.8	-2.2	-3.1	-2.7	-3.3	-4.2	-4.1	-3.4	-3.4	-3.3	-3.2
Overall balance PS 4/	-3.5	-3.6	-3.8	-3.5	-2.9	-3.5	-3.8	-3.3	-3.5	-3.7	-3.6
excluding *cincuentones* transactions	-3.5	-3.6	-3.8	-3.5	-4.2	-4.7	-4.7	-3.7	-3.7	-3.7	-3.6
Gross debt NFPS	55.5	62.9	61.4	60.7	63.2	66.8	66.7	66.8	67.5	68.5	68.9
Gross debt PS	61.4	64.6	61.6	65.3	67.7	71.6	73.5	74.4	75.3	76.6	77.4
Net debt NFPS	45.2	49.7	49.7	49.5	52.1	55.8	55.8	56.0	56.8	57.9	58.4
PS debt net of liquid financial assets 5/	30.3	31.3	35.9	36.5	38.8	42.8	43.8	43.9	44.7	45.6	46.1
PS debt net of total financial assets	23.0	25.8	29.9	32.1	33.7	31.8	33.4	33.9	34.7	35.8	36.4
External indicators											
Merchandise exports, fob (US$ billions)	13.8	11.1	10.4	11.1	11.5	12.0	12.7	13.4	14.5	16.2	17.4
Merchandise imports, fob (US$ billions)	11.8	9.8	8.5	8.7	9.1	9.3	11.2	12.2	13.1	13.3	14.2
Terms of trade (percent change)	3.5	3.5	3.7	0.7	-0.5	3.6	5.2	2.5	1.9	1.6	0.8
Current account balance	-3.2	-0.9	-0.1	0.7	0.1	0.2	-2.7	-3.4	-3.4	-1.7	-1.8
Foreign direct investment	-4.4	-1.5	1.4	3.8	1.9	1.7	0.5	0.5	1.1	1.4	1.5
Total external debt + non-resident deposits	74.9	89.5	74.4	68.1	69.3	71.9	75.6	77.1	79.6	81.6	83.8
Of which: External public debt	33.7	37.1	31.6	30.4	32.6	36.1	36.8	38.3	40.8	42.9	45.1

External debt service (in percent of exports of g&s)	65.5	90.2	87.9	68.2	62.5	56.7	58.3	60.2	59.3	57.0	55.9
Gross official reserves (US$ billions)	17.6	15.6	13.5	15.9	15.5	14.5	15.6	16.8	17.8	18.8	19.8
In months of imports of goods and services	12.6	13.5	13.7	15.4	14.2	13.0	12.1	12.3	12.2	12.5	12.5
In percent of:											
Short-term external (STE) debt	188	173	196	242	255	246	251	257	260	263	267
STE debt plus banks' non-resident deposits	228	220	210	317	314	261	265	269	269	273	281

Sources: Banco Central del Uruguay, Ministerio de Economia y Finanzas, Instituto Nacional de Estadistica, and Fund staff calculations.

1/ Percent change of end-of-year data on one year ago.

2/ Includes bank and non-bank credit.

3/ The non-financial public sector (NFPS) includes the Central Government, Banco de Prevision Social, Banco de Seguros del Estado, local governments, and Non-Financial Public Enterprises.

4/ Total public sector (PS). Includes the NFPS and Banco Central del Uruguay.

5/ Gross debt of the public sector minus liquid financial assets of the public sector. Liquid financial assets arecalculated by deducting from total public sector assets the part of central bank reserves held as a counterpart to required reserves on foreign currency deposits.

INTERNATIONAL MONETARY FUND

URUGUAY

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION

January 27, 2020

KEY ISSUES

Context. Uruguay is in an enviable position in many respects. The country enjoys political stability, strong governance and institutions, and a high degree of social cohesion. Following a decade and a half of robust growth, the country boasts high per capita income, low levels of poverty and inequality, and a resilient financial sector. More recently, in a context of a volatile region and global uncertainties, challenges have emerged. Growth, investment, and employment have slowed; inflation and inflation expectations have remained persistently above target; fiscal accounts have deteriorated, and debt has increased. The political and economic landscapes—with the post-election mandate and a growth boost due to large private and infrastructure investments—present an opportunity to address these challenges and preserve the social compact for future generations.

Policy recommendations. The authorities should use this opportunity to reduce debt and bring inflation towards the mid-point of the target range, so as to rebuild buffers and manage sizable risks. In addition, the authorities should leverage Uruguay's institutional advantages to further improve the fiscal and inflation targeting frameworks and implement structural reforms, in order to raise potential growth and safeguard the achievements of the past decade. Policies should aim at nurturing conditions for higher private investment, addressing high youth unemployment, strengthening educational outcomes, improving the efficiency of state-owned enterprises, ensuring adequate pensions for future generations, and arresting the increase in crime rates. Flexibility of the exchange rate has served Uruguay well and should be retained.

Past advice. The authorities and staff have remained in broad agreement on the macroeconomic policy objectives. These include maintaining public debt on a sustainable trajectory, keeping inflation low, and allowing exchange rate to adjust in line with fundamentals. The fiscal deficit, however, has increased due to both lower growth and continued increases in spending (including due to pensions and other legally binding commitments). In addition, inflation has stayed outside of the target range.

Approved By:
Patricia Alonso-Gamo (WHD) and
Jeromin Zettelmeyer (SPR)

Discussions took place in Montevideo during December 5–17, 2019. The staff team comprised S. Pelin Berkmen (head), Natasha Che, Dmitry Gershenson, and Jose Torres (all WHD). David Vogel (OED) participated in key meetings, Sidonia McKenzie (Summer Intern) contributed to the preparatory work, and Luis Omar Herrera Prada (WHD) provided research assistance. Staff met with Minister of Finance Astori, Minister of Labor Murro, Director of the Office of Planning and Budget García, Central Bank President Graña, other senior government officials, as well as representatives of public enterprises, the private sector, academia, unions, and members of the newly elected government.

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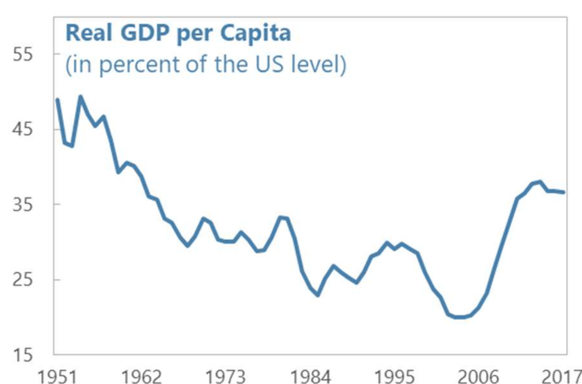
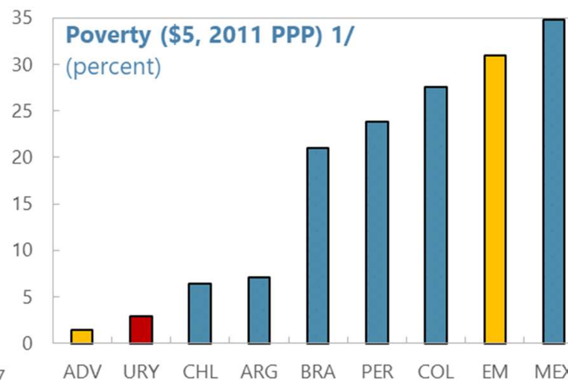
CONTEXT: ENVIABLE ACHIEVEMENTS BUT CHALLENGES EMERGED

1. **Uruguay is in an enviable position in many respects.** The country enjoys political stability, strong governance and institutions, and a high degree of social cohesion. Following a decade and a half of robust growth, it also boasts high per capita income and low levels of poverty, inequality, and informality. Owing to prudent supervision and regulation, the financial sector remains resilient despite regional financial market volatility.



Source: INS and IMF staff calculations



Source: WB WDI.
1/ URY data for 2017, last data available for other countries.

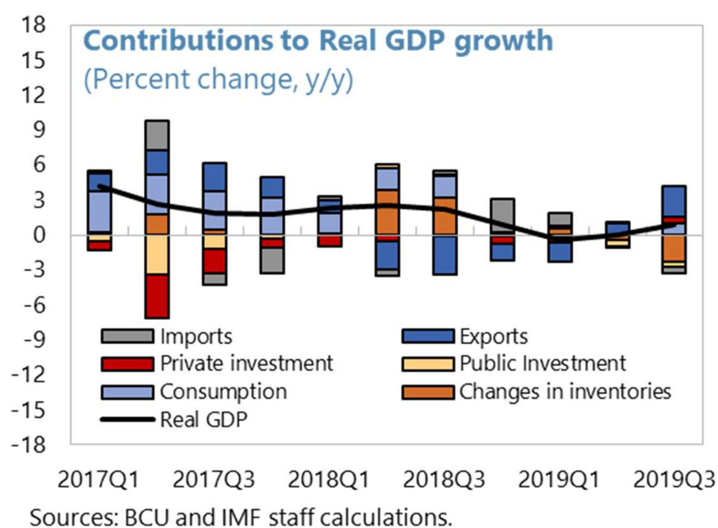
2. **Imbalances have emerged, however, and external conditions are less favorable.** Growth, investment, and labor participation have been on a declining trend in recent years, and internal imbalances (higher fiscal deficits, rising unemployment) have accumulated. Debt has increased, and inflation has remained outside of the target range. At the same time, the external position has remained robust, with the current account fluctuating around zero, and sufficient reserve buffers. In the past, Uruguay has taken advantage of the benign global conditions, including high commodity prices and robust external demand. Such favorable conditions, however, are no longer present, with sluggish global and regional growth, subdued commodity prices, elevated uncertainty, volatile capital flows, and bouts of financial turbulence in neighboring Argentina, although the low interest rate environment provides some breathing space.

3. **The political and domestic economic landscapes over the next few years present an opportunity for addressing Uruguay's economic challenges.** The new government, which assumes office in March 2020, will have a post-election mandate and will be helped by a growth boost from the construction of a new paper pulp plant (close to 5 percent of 2018 GDP) and oncoming public-private partnership (PPP) infrastructure projects (around 3½ percent of 2018 GDP) over the next few years. In addition, there is consensus across the political spectrum regarding key challenges.

4. The authorities should use this opportunity to reduce the accumulated imbalances and undertake reforms to safeguard past achievements and ensure continued income convergence. They should improve the fiscal position to reduce debt and bring inflation towards the mid-point of the target range. They should also leverage Uruguay's institutional advantages to further improve the fiscal and inflation targeting frameworks and implement structural reforms. A revival of productivity growth is critical to sustain the coverage and generosity of the welfare state and ensure fairness across generations. In this context, action is needed to improve education outcomes, youth employment, private investment and the efficiency of state-owned enterprises, as well as to ensure adequate pensions for future generations.

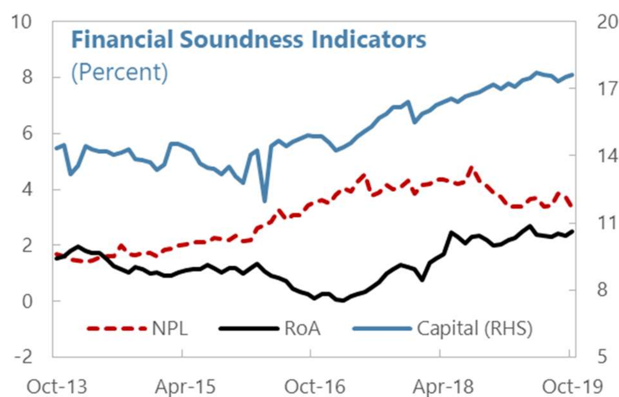
RECENT DEVELOPMENTS

5. The economy has softened, and inflation remained above target. After a growth slowdown during 2018H2-2019H1, activity picked up in 2019Q3, with some recovery in consumption, exports, and private investment. The average growth in the first three quarters of 2019 was 0.2 percent. The current account balance has fluctuated around zero, with the positive trade balance offset by a negative income account. Inflation increased to 8.8 percent in December, outside of the 3-to-7-percent target range, despite a negative output gap, due to both temporary factors (with meat prices contributing about 2½ percentage points to headline inflation) and above-target expectations.

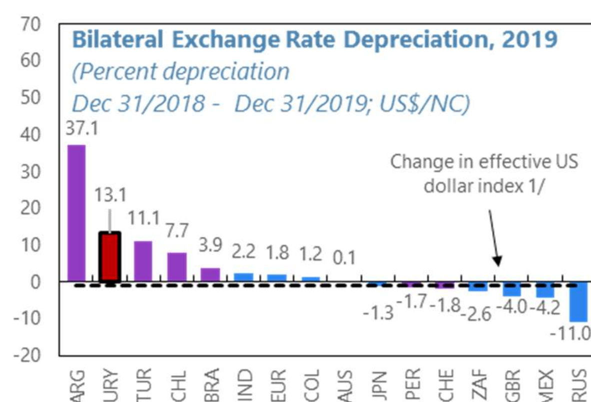


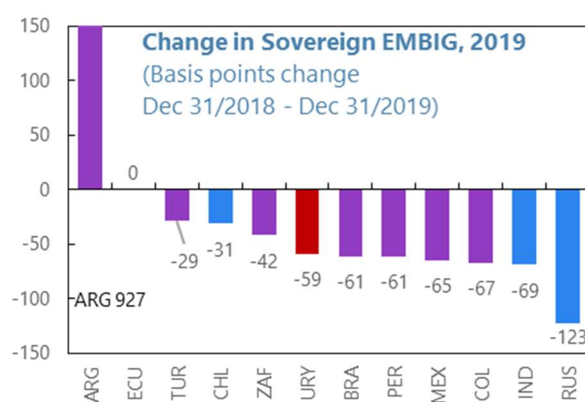
Sources: BCU and IMF staff calculations.

6. Spillovers from Argentina have been limited to the real sector and exchange rate channels, thanks to robust financial sector and ample reserve buffers. Tourism receipts from Argentina dropped by 34 percent in the first half of 2019 compared with the same period in 2018. The authorities allowed the exchange rate to adjust in an orderly manner, with the peso depreciating against the U.S. dollar by 13 percent during 2019. Intervention was geared to addressing disorderly market conditions and was two-sided. Reserves declined from US$15.6 billion in December 2018 to US$14.5 billion in December 2019 (25 percent of GDP). The financial sector—which had markedly reduced its exposure to Argentina—remains robust, and sovereign spreads are contained at low levels. With the depreciation of the currency, however, deposit dollarization has edged up.



Sources: BCU and IMF staff calculations.





Sources: Bloomberg Finance L.P.; Thomson Reuters Datastream; and IMF staff calculations.
1/ The effective US dollar index (BBDXY) is a measure of the value of the US dollar relative to a basket of US trade partners' currencies. The index depreciated by 0.9 percent since December 31, 2018.

7. Fiscal balances deteriorated substantially. As the economy slowed, revenues declined, and current expenditures continued to increase. The budget for 2020—the last to be prepared by the current government—gives up on the achievement of the 2.5-percent-of-GDP deficit target and instead foresees a fiscal deficit for the consolidated public sector (CPS) of 4.6 percent of GDP in 2019 (excluding the *cincuentones* transactions) and 3.8 percent of GDP in 2020.[1] The

[1] *Cincuentones* are persons over fifty years with income beyond a certain threshold who were allowed to voluntarily return to the public system (to compensate them for the possibility of low replacements rates stemming from the fact that their contributions to the old system were not recognized when the mixed pension system was created). The first cohort was allowed to move in 2018 and the process will end in 2022. These funds are recorded as revenue in line with the Fund's methodology and thus lower the fiscal deficit. They also lower the stock of public debt but do not alter public financing needs as the proceeds are being saved in a trust fund (ring-fenced until 2024). See Box 1 in *IMF Country Report 19/64*.

underlying fiscal balance has deteriorated since the budget projections. As of November, the twelve-month CPS deficit (excluding the *cincuentones* transactions) stood at 4.7 percent of GDP, aided by the impact of a favorable debt management operation in September (0.3 percent of GDP) and by lower interest payments from the central bank.[2] The authorities have successfully issued longer-term bonds at favorable rates to cover their financing needs.

Overall Fiscal Balance (percent of GDP)

		2017	2018	2019	2020
Baseline	CPS	-3.5	-2.9	-3.5	-3.8
	Excluding *cincuentones*		-4.2	-4.7	-4.7
	NFPS	-2.7	-2.0	-3.0	-3.2
	Excluding *cincuentones*		-3.3	-4.2	-4.1
Budget 2019	CPS			-3.4	-2.9
	Excluding *cincuentones*			-4.6	-3.8
	NFPS			-2.6	-2.2
	Excluding *cincuentones*			-3.8	-3.1
Budget 2018 1/	CPS				
	Excluding *cincuentones*		-3.3	-2.8	-2.5
	NFPS				
	Excluding *cincuentones*		-2.4	-1.9	-1.8

Sources: Ministerio de Economia y Finanzas and IMF staff calculations and projections.
1/ The 2018 budget predates *cincuentones*. Accordingly, *cincuentones* were not included in that budget presentation.

8. **The authorities and the IMF switched the focus of fiscal reporting for Uruguay from the CPS to the non-financial public sector (NFPS)** (Box 1). The NFPS-based reporting includes all the components of CPS except the central bank and provides a more appropriate and clear measure of the underlying fiscal situation.[3] The authorities continue to transparently communicate all the details of the fiscal accounts, including the impact of *cincuentones* on fiscal outturns. In this context, the IMF's fiscal analysis is based on the NFPS fiscal aggregates excluding *cincuentones* transactions, while WEO data present the NFPS fiscal aggregates including *cincuentones*.

[2] The NFPS deficit (excluding *cincuentones* transactions) was 4.2 percent of GDP in November, up from 3.3 percent of GDP in December 2018.

[3] The current NFPS debt numbers include the central bank capitalization bonds (amounting to 8.8 percent of GDP in 2018), which were netted out in the previous coverage.

EXPECTED RECOVERY BUT SIZABLE RISKS

9. The economy's long-term growth potential is estimated at around 2–2.5 percent, taking account of (i) low investment and (ii) declining labor force participation, partly reflecting demographic trends. Since 2015, growth has averaged at about 1½ percent, compared with an average of about 5 percent in 2006–14.

10. At the same time, the short-term outlook has improved. Staff projects growth to rebound from an estimated 0.5 percent in 2019 to 2.1 percent in 2020 and 2.5 percent in 2021, as investment projects ramp up, offsetting adverse spillovers from Argentina. Growth is expected to decline after 2021 as these investments run their course—but the *level* of real GDP is expected to be permanently higher by around 1 percent due to the productivity impact. Inflation is expected to remain at around 8 percent in 2020 and then to decline gradually to the upper limit of the target range as temporary factors (such as the passthrough from the currency depreciation and increase in some food prices) wear off and private-sector wage increases follow the declining path agreed in the last round of negotiations.

11. Uruguay's external position is broadly consistent with fundamentals and desirable policy settings (Annex I). Staff projects the current account deficit to widen to about 2-3 percent of GDP, as large investment projects and economic recovery raise imports, and tourism receipts from Argentina decline further, including due to Argentina's new tourism tax.[4] After the completion of the paper-pulp plant in 2022, exports are expected to increase. Foreign exchange reserves—at 180 percent of the ARA metric and 490 percent of short-term external debt—are adequate.

12. There are sizable upside and downside risks. On the downside, economic developments in Argentina remain an outsized risk, even though the likelihood of direct financial spillovers is small. A host of global factors (trade disruptions, lower growth, abrupt declines in risk appetite, large swings in energy prices) and of local ones (loss of credibility and further increases in debt due to insufficient fiscal adjustment or delayed reforms and PPP projects) may undermine the expected recovery and limit medium-term growth. On the upside, the growth boost from investment projects may be larger than expected, given uncertainty about possible indirect effects (Selected Issues Paper 2).

[4] Argentina's new tourism import tax imposes a surcharge of 30 percent for expenditures on hotels, airline tickets, and credit cards purchases outside Argentina.

Box 1. The Change in Fiscal Reporting

In 2019, the authorities and the IMF switched the focus of fiscal reporting from the consolidated public sector (CPS) to the non-financial public sector (NFPS).[1] The NFPS-based reporting includes all the components of CPS except the central bank, and therefore produces more clear measures of the underlying fiscal situation.

In Uruguay, the focus on the NFPS is appropriate and preferable to the CPS-based presentation for several reasons. With Uruguay being a small, open, and dollarized economy, the central bank intervenes in the foreign exchange market to prevent disorderly market conditions. Such interventions—either buying or selling of foreign currency—are sterilized by issuing/retiring the central bank paper (*Letras de Regulacion Monetaria*). Depending on the resulting stock of the outstanding central bank paper, the central bank incurs the interest cost.

- Over the years, the magnitude of this cost has been volatile and difficult to forecast. This has generated uncertainty around the CPS-based fiscal policy targets, which included central bank interest costs.
- Including the central bank balance in fiscal targets (the CPS-based presentation), which is not under the purview of the fiscal authorities, blurs the line between monetary and fiscal policies and creates undue tensions between both authorities.
- Finally, by reducing the concerns about the impact of monetary policy on fiscal accounts, this switch allows the central bank to focus better on its key objectives.

The authorities continue to transparently communicate the old (CPS-based) fiscal aggregates in addition to the new (NFPS-based) ones.

[1] The authorities initiated the change in early 2019, and the IMF reflected it in the October 2019 World Economic Outlook database.

Risk Assessment Matrix

Sources of Risk	Likelihood	Impact if Realized	Policy Response
Global and regional			
Rising protectionism and retreat from multilateralism.	**High**	**Low/Medium (↓)** Escalating and unpredictable trade actions could reduce cross-border trade flows, contribute to negative risks to investment and growth, and trigger market volatility.	• Use exchange rate as a shock absorber. • Continue efforts to diversify trade. • Use countercyclical macro tools to the extent there is space.
Sharp rise in risk premia.	**High**	An abrupt deterioration in market sentiment could trigger risk-off events, leading to increasing financing costs and depreciation of the currency.	• Use exchange rate as a shock absorber. • Rely on credible rules to maintain fiscal and inflation anchors. • Use liquidity buffers if needed. • Use countercyclical macro tools to the extent there is space.
Weaker-than-expected global growth.	**Medium/High**	**Low/Medium (↓)** In a synchronized and prolonged growth slowdown would reduce demand for Uruguayan exports and might lower agriculture and energy prices.	• Use exchange rate as a shock absorber. • Rely on credible fiscal rule to maintain credibility • Use countercyclical macro tools to the extent there is space. • Pass-through declines in oil prices to households.
Large swings in energy prices.	**Medium**	**Low/Medium** While higher oil prices would raise import and fiscal costs, lower agricultural prices would reduce export revenues.	• Use the oil price hedges. • Pass through oil price changes to households over the medium term. • Continue efforts to diversify trade beyond primary products.
Contagion from financial turbulence in Argentina	**Low**	**Medium/High (↓)** A worsening outlook for Argentina could worsen bilateral trade with Argentina through income and exchange rate effects. Depreciation of peso against the US dollar would suppress consumption.	• Use exchange rate as a shock absorber. • Rely on credible rules to maintain fiscal and inflation anchors and adjust if there is space. • Continue efforts to diversify trade. • Use countercyclical macro tools to the extent there is space.
A sharp increase in migration from Venezuela	**Low**	**Low (↑)** An increase in migration flows while initially may create fiscal pressures could help address aging pressures.	• Facilitate labor market integration of migrants.

Risk Assessment Matrix (Concluded)			
Domestic			
Insufficient fiscal adjustment	**Low/Medium**	**Medium (↓)** Insufficient fiscal adjustment, including due to expenditure rigidities, might lead to loss of credibility, raising financing costs, raising debt further, and suppressing growth.	• Introduce a credible adjustment plan starting from 2020, supported by a strong medium-term fiscal anchor.
Delayed progress in structural reforms	**Medium**	**Medium (↓)** A delay in addressing structural bottlenecks (such as in labor markets, education, pension reform) might reduce medium-term growth prospects.	• Start introducing structural reforms in 2020, leveraging the economic boom.
Higher multipliers for the UPM and PPP projects	**Medium**	**Medium (↑)** Combined with a favorable business environment, infrastructure projects can boost productivity more than expected.	• Continue to improve business environment to leverage productivity gains. • Save additional tax revenues to build fiscal buffers and as a countercyclical measure.
Cyber-attacks	**Low**	**Medium (↓)** Given the low level of fintech activity and bank credit, financial sector stability threats are limited, but confidence effects could be important.	• Continue efforts to increase cyber-security.

13. **The authorities were broadly in agreement with staff's views.**[5] They expected a gradual recovery in line with staff projections. They also noted that the headwinds from the financial turbulence in Argentina is expected to persist in the short term and that global trade-related uncertainty is negatively affecting outlook. The authorities remained optimistic on the expected positive impact of the large-scale investment projects and potentially a more robust economic recovery in Brazil. The authorities stressed that Uruguay's institutional strength, sizable reserve buffers, effective sovereign asset and liability management, and a flexible exchange rate will allow the country to manage external shocks.

POLICIES: SAFEGUARDING SUSTAINABLE AND INCLUSIVE GROWTH

A. Maintaining Fiscal Sustainability

14. **Under baseline projections, despite some fiscal measures supporting the projected improvement in fiscal balances, debt is expected to rise.** Staff projects the NFPS deficit (excluding *cincuentones*) to gradually decline from estimated 4.2 percent of GDP in 2019 to

[5] The authorities' views are the views of the incumbent government.

4.1 percent of GDP in 2020, and 3.2 percent of GDP in 2024.[6] This reflects a cyclical improvement of tax revenues, a normalization of state-owned enterprise profits, as well as some measures to contain expenditures (amounting to about 0.9 percent of GDP), given the political consensus on the need for a fiscal adjustment.[7] In addition, availability payments that the government is expected to pay to its private sector partners for the PPP projects are expected to reach ½ percent of GDP by 2024. NFPS debt is expected to increase from an estimated 67 percent of GDP in 2019 to 69 percent of GDP in 2024.[8]

15. While gross financing needs are manageable, fiscal space is diminishing (Annex II). Large financing needs for 2020 are expected be to be met in a context of coordinated public-sector asset-liability management, stable local currency funding from domestic institutions, the authorities' pre-financing policy, and sufficient buffers (in the form of nonfinancial-public-sector liquid assets and contingent credit lines). Sovereign risk spreads remain low, but the fiscal position has worsened, debt is elevated, and downside risks are sizable. Despite improvements, the shares of foreign-currency debt and of nonresident holdings remain relatively high, leaving debt vulnerable to exchange rate pressures and changes in risk sentiment. As a result, Uruguay's fiscal space—the room for discretionary fiscal policy without endangering debt sustainability—is at risk.

16. There is need to introduce a credible adjustment plan starting from 2020 to put debt on a firm downward path. Current fiscal trends, if they continue, could undermine debt sustainability and investor confidence. Bringing debt to its 2012–14 levels (about 10 percentage points of GDP lower than currently) over the medium term would place Uruguay comfortably within the range of investment-grade peers and rebuild space to accommodate future negative shocks without endangering sustainability.

17. Given the expected growth support from large investment projects, there is some room to frontload fiscal adjustment. Bringing the NFPS primary deficit from its current level of 1.8 percent of GDP to a surplus of 0.9 percent of GDP by 2024 would stabilize debt. Additional adjustment is needed to tilt down the debt ratio. On average, a ½-percent-of-GDP adjustment per year would reduce debt by 10 percentage points in 10 years. In the absence of negative shocks and to the extent that growth picks up, the authorities will have more scope to deliver a higher adjustment for the next couple of years. This would help reduce debt faster (including through lower future interest payments), ease the economic impact of the adjustment and reduce the adjustment needs going forward. If upside risks materialize, windfall revenues

[6] NFPS primary deficit (excluding *cincuentones*) is projected to fall from estimated 1.8 percent of GDP in 2019 to 1.4 percent of GDP in 2020 and 0.4 percent of GDP in 2024.

[7] The incoming government announced its intention to undertake a fiscal adjustment, although details were not available at the time this report was prepared.

[8] The IMF and the authorities use different methodologies to calculate debt-to-GDP ratios. The IMF uses local currency for both GDP and debt (the latter converted to pesos at end-period exchange rate), while the authorities use the GDP in U.S. dollars (converted at average exchange rate) and the stock of debt in U.S. dollars. In 2018, NFPS debt was 63.2 percent of GDP using the IMF methodology and 59.7 percent of GDP using the authorities' methodology.

resulting from the demand boost should be saved to both stabilize the economy and use the opportunity to reduce debt during good times.

18. A combination of measures would be needed. A transparent public information and communication strategy would help build consensus around the selected measures.

a. A sustainable adjustment would require limiting the increase in current expenditures. If, for example, current expenditures increase with inflation—rather than increasing with or faster than nominal GDP—debt would decline by 7 percentage points in 2024 relative to the current levels. However, given expenditure rigidities, such as in pensions, maintaining current expenditures flat in real terms may be too ambitious. In addition, careful consideration should be given to maintaining adequate provision of key public services and safety nets. In this context, a combination of measures such as keeping public wages in line with the private sector (to attract and retain talent while avoiding excessive costs), reducing public employment in non-critical sectors through natural attrition, and improving the efficiency of spending would support the adjustment.

b. Capital expenditures, already at low levels, should be preserved.

c. There is room to reduce tax expenditures—exemptions, reduced rates and tax credits—estimated at about 7 percent of GDP. About 60 percent of these expenditures are for the value added tax, where tax expenditures represent about 40 percent of collections. A cost-benefit analysis could help streamline exemptions, particularly those benefiting higher-income groups, those that have already achieved the desired outcomes or those that have not been as effective. This would both support fiscal adjustment, given the rigid structure of current expenditures, and allow the future use of exemptions as a stabilization tool in case of negative shocks.

19. Addressing growing pension spending is a priority to ensure sustainability. Uruguay boasts a comprehensive social security system, an impressive achievement and one of the pillars of the country's social stability. With the population aging and given the already high level of pension spending (around 11 percent of GDP, about a third of total expenditures), early action is needed to ensure sustainability and adequate retirement income for future generations. Reforms should be based on a comprehensive review of the entire system, supported by an informed social dialogue. Early action will also help smooth the transition to a revised system and release resources for other priority areas.

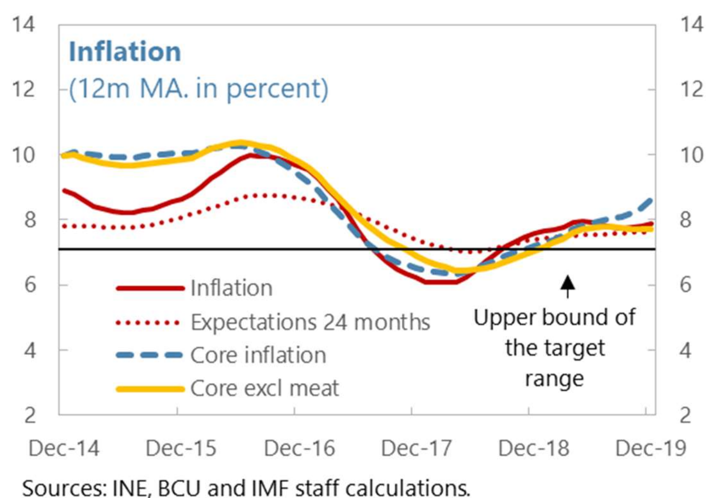
20. Fiscal adjustment should be accompanied by the introduction of a revamped medium-term fiscal framework (MTFF) (Annex IV). Given sizable downside risks, particularly if a gradual approach is chosen, there is a need to establish credibility of the adjustment plan from the outset. The introduction of a MTFF, encompassing a binding fiscal rule, would enshrine credibility by introducing a fiscal anchor that ensures medium-term sustainability. It would also help rebuild the necessary fiscal space to counter negative shocks without endangering sustainability. An improved MTFF could include (i) a rolling 3-to-5-year projection period,

irrespective of the government's term to reduce uncertainty; (ii) a strengthened fiscal rule (possibly an expenditure rule combined with a debt anchor); (iii) limited use of escape clauses in exceptional circumstances; (iv) strengthened accountability mechanisms to ensure better adherence to fiscal targets; (v) regular spending reviews to increase efficiency; (vi) more frequent updates of forecasts given frequent shocks; (vii) a broad coverage by setting a spending ceiling that is binding also for autonomous (Article 220) entities; and (viii) better coordination between the Office of Planning and Budget and the budget office of the Ministry of Economy and Finance (to link strategic priorities and program evaluations to budget allocations); (ix) further strengthened public investment management framework (particularly in the context of large PPP projects); and (x) disclosure of risks, including those associated with PPPs. Budgetary targets should be set for the NFPS, in line with the recent shift in the focus of fiscal reporting.

21. The authorities concurred on the need to reduce fiscal imbalances over the short and medium term, for which a social security reform will be crucial. They confirmed that the country needs to confront its fiscal problem and that the improvement in fiscal finances in the short term would come from increased revenue collection tied to a cyclical recovery, noting recent economic indicators pointing in that direction. They also emphasized the need to moderate discretionary spending, ruling out increases in tax rates, given an already-elevated tax burden. They conceded that the medium-term adjustment will ultimately depend on the capacity to control the rise in endogenous spending, although they stressed that about 80 percent of total spending is for social purposes. Thus, they emphasized that the country should leverage its room for maneuver, as evidenced by low sovereign risk spreads and borrowing costs and long debt maturities, to ease the impact of the consolidation on the most vulnerable. They confirmed that there is consensus on the need to reform the social security system and highlighted its urgency. They emphasized that both political will and wide-ranging social agreement are needed to undertake such a transformation. The authorities stressed that ultimately the reform should strive to preserve rights while making them compatible with fiscal constraints.

B. Lowering Inflation and Reducing Dollarization

22. Inflation and inflation expectations remain persistently above the top of the target range. The stance of monetary policy was tightened in October and December, with the indicative reference for the growth rate of the M1+ monetary aggregate lowered from 8-10 percent in 2019Q3 to 7-9 percent in 2019Q4 and to 6-8 percent in 2020Q1. Interest rates have increased by about 120 basis

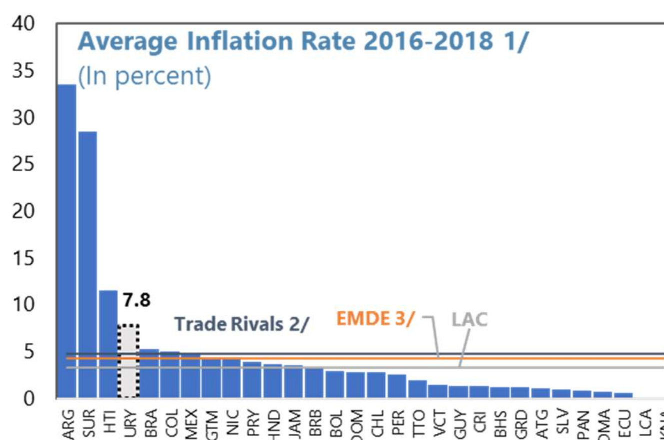


Sources: INE, BCU and IMF staff calculations.

points at the short end and by about 30 basis points at the longer end since September. Headline inflation continued to increase (to 8.8 percent in December), reflecting increases in meat prices, and core inflation and medium-term inflation expectations remained above the target range (with 24-month expectations at 7.7 percent).

23. Given the expected growth boost, the central bank will have more space to focus on reducing inflation towards the mid-point of the target range. If inflation stabilizes at current levels, it would leave Uruguay vulnerable to negative shocks, which could then raise inflation to double digits. As the monetary policy works through its lags and in the absence of negative shocks, monetary indicative references should continue to be adjusted until inflation and inflation expectations are firmly at the mid-point of the target range. The expected growth boost could help mitigate the tradeoffs from both monetary and fiscal tightening. Keeping inflation low and stable would also help support efforts to reduce dollarization and indexation, deepen financial markets, and reinforce policy credibility. The authorities should also continue to use the exchange rate as a shock absorber and interventions should be reserved for addressing disorderly market conditions—as they are now—and reserve buffers should be kept above prudential norms.[9]

24. Further enhancements to the inflation targeting framework could be considered to keep inflation low and stable at the mid-point of the target range. Conducting monetary policy is quite challenging in the presence of a high degree of dollarization, low credit-to-GDP ratio, remaining wage indexation, and frequent shocks to the exchange rate. At the same time, a low and stable inflation rate is key to addressing these challenges. Enhancements could focus on strategies, instruments, and communication practices. In particular, communicating a clearer hierarchy of objectives, with the primacy of price stability at the mid-point of the target range, and explaining in more detail the central bank's reaction function would guide expectations towards



Sources WEO, Moody's, S&P, Fitch, and IMF staff calculations.
1/ Group averages are estimated as simple arithmetic average and exclude Argentina, Belize, and Venezuela.
2/ Trade rivals as defined in "Dissecting economic growth in Uruguay" but excluding Argentina: Paraguay, New Zealand, Australia, Suriname, and Guyana.
3/ Emerging Market and Developing Economies (EMDE) according to the WEO classification.

[9] The peso moves broadly in line with global trends. The authorities, however, intervene in the foreign exchange market in response to large portfolio flows. See Box 2 in *IMF Country Report 19/64*.

the mid-point of the target range and reinforce the expectations channel, which would help reduce the burden on the interest rate channel.

25. Continued efforts to reduce the high degree of dollarization and indexation are welcome. The revised guidelines for wage bargaining councils—which introduced productivity considerations in 2018 and delinked wages from past inflation in 2015—are an important step towards reducing indexation. Both macroeconomic and price stability are critical to reducing dollarization. In addition, continued coordinated efforts to fine-tune regulatory measures, deepen financial markets, and provide hedging opportunities would help further encourage local currency holding.

26. The authorities expect inflation to fall to within the target range by late 2020. They stressed the role of temporary external factors—notably a spike in meat prices—in pushing the inflation above the 7-percent threshold. They also noted challenges emerging from managing multiple objectives (inflation, economic activity, and competitiveness). Accordingly, the authorities considered the current monetary policy stance to be adequate and the level of interest rates appropriate. They remain committed to maintaining a flexible exchange rate while ensuring proper functioning of the foreign exchange market. Enhancements to the conduct of monetary policy (including communications and the steps to further reduce financial dollarization) will be considered in the course of the BCU strategic review, to be initiated in 2020.

C. Financial Sector: Preserving the Resilience and Supporting Growth

27. The financial sector is resilient, but medium-term challenges remain. Due to prudent supervision and regulation, Uruguay's financial sector weathered the bouts of financial volatility in Argentina well. At the same time, financial intermediation is chronically low, with wide margins between credit and deposit rates. In addition, credit markets are segmented for dollar and peso loans (with very high rates for the latter), thereby weakening the monetary transmission mechanism.

28. The authorities are proceeding with appropriate steps to maintain financial sector resilience. Regulations on the net stable funding ratio—requiring that the liquidity profiles of banks' assets and liabilities be aligned—became effective in December. Regulation on countercyclical buffers—requiring banks to accumulate additional capital during boom times—was submitted for public consultation in December. In addition, investment limits for pension funds were modified to incorporate exposures to PPP projects to limit concentration risks.

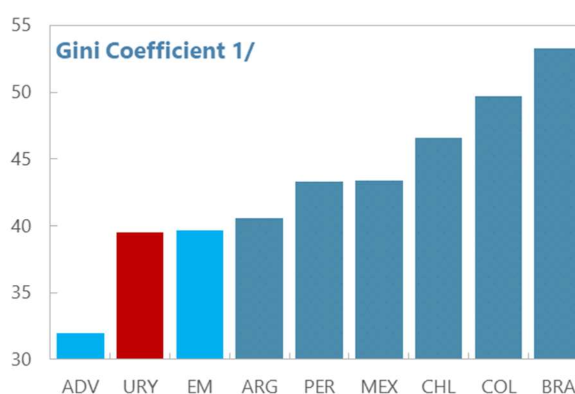
29. The authorities' efforts to deepen financial markets are welcome. These include efforts to (i) create benchmark curves; (ii) increase the liquidity of instruments in secondary markets; and (iii) foster financial inclusion and innovation, by providing free access to bank accounts, encouraging electronic transactions, and analyzing ways to improve the payments system. As a result, electronic points of sale almost doubled between 2014 and 2019, and the amount of cash withdrawals began to decline in 2018.

30. Financial regulation should aim to strike the right balance between enabling innovation and competition on the one hand and addressing risks to financial integrity, stability, and consumer protection on the other. Since the introduction of the regulation on peer-to-peer lending, no fintech company has registered. Continued collaboration across state agencies, the central bank, and the industry would help advance the common goal of financial development and inclusion, while ensuring proper risk management.

31. The authorities stressed that the financial system remains stable and profitable despite the challenging regional environment. They noted the demand-driven nature of credit. The authorities considered their peer-to-peer lending regulations appropriate, since they are geared towards maintaining financial stability and consumer protection in line with the mandate of the BCU.

D. Structural Reforms for Sustainable and Inclusive Growth

32. Uruguay has distinct structural strengths relative to peers. It has strong governance and institutions, political stability, a high degree of social cohesion, as well as low rates of poverty, inequality, and informality. Its citizens enjoy a strong safety net and adequate protection of their rights. Overall, Uruguay is one of the top performers on many environmental, social, and governance (ESG) indicators (the WB Sovereign ESG data framework).

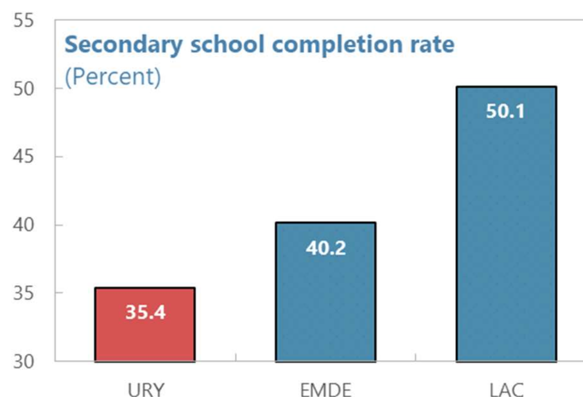


Source: WB WDI.
1/ For Uruguay, the data are for 2017. The latest available data for other countries.

33. The authorities are pursuing trade opportunities to fully capitalize on Uruguay's competitive advantages in agribusiness and professional services. After 20 years of negotiations, a trade agreement between Mercosur (Argentina, Brazil, Paraguay, Uruguay) and the EU—Uruguay's second largest trade partner—has been completed, but it still needs to be ratified. Another agreement—covering a wide range of issues, including tariffs, government procurement, and intellectual property—has been reached between Mercosur and EFTA (Iceland, Liechtenstein, Norway, and Switzerland). Finally, Uruguay and its Mercosur partners agreed to gradually phase out the intra-bloc import taxes.

34. Building on these strengths, further structural reforms are needed to ensure continued income convergence and maintain social achievements for future generations

(Selected Issues Paper 1). Closing infrastructure gaps is an important step but by itself will not be sufficient to raise growth to the levels seen in the past decade. A vibrant private sector is essential to support growth. To this end, Uruguay needs to improve its education outcomes and the business environment. In addition, a corporate governance reform would improve the management and efficiency of SOEs, which play a key role in the Uruguayan economy (Box 2).



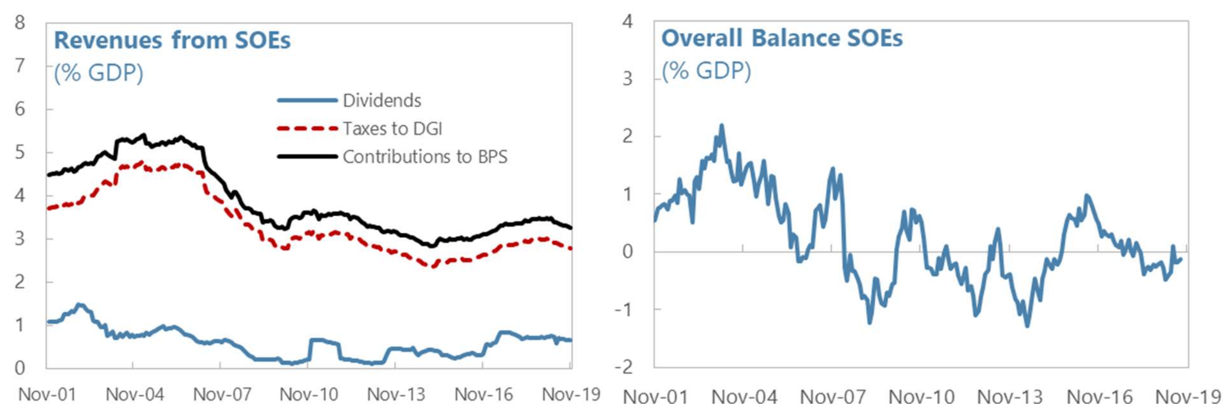
Source: UNICEF 2019.
Due to data limitations, some countries are not included. Unlike UNICEF's aggregation, LAC definition does not include Cuba .

35. The deterioration in labor market outcomes needs to be reversed. Employment and labor force participation have been falling in key sectors, and the unemployment rate has risen, particularly among the young (to around 30 percent). Younger generations have borne the brunt of the adjustment during downturns, increasing concerns about both intergenerational equity and potential insider-outsider issues (Selected Issues Paper 3). In addition, perception surveys indicate that there is room for further improvement in wage flexibility, labor-employer cooperation, and in conditions for attracting and retaining workers.

36. Policies should be geared towards high and stable employment while maintaining adequate worker protection. Changes to the wage council guidelines—which introduced productivity considerations and greater flexibility in wage setting—are a step in the right direction. Further flexibility (for small firms, low-productivity regions, and during downturns) could be considered to preserve rights and provide incentives for firms to create more stable jobs and invest in on-the-job training. Better aligning wage increases with productivity would also help raise skill premium and improve incentives for further education. In addition, improvements in business-labor cooperation and continued focus on education and training to recalibrate skills could support employment. Similarly, youth unemployment should be addressed in coordination with the education reform. Continued efforts to integrate migrants and women into the labor market would help offset pressures stemming from population aging.

Box 2. Reforms to Governance of State-Owned Enterprises (SOEs)

SOEs play a key role in the Uruguayan economy. As in many emerging countries, SOEs play a dominant role in the Uruguayan economy as they are seen as essential to address market failures (such as natural monopolies) and promote policy goals. There are about 15 SOEs operating in both competitive and non-competitive markets in the oil, electricity, telecommunications, financial, water and infrastructure sectors.[1] They have assets of about 25 percent of GDP, account for about 6 percent of value added, 7 percent of investment, 2.5 percent of jobs (with 37 thousand employees or 17 percent of public employment) and the services they provide have a weight of about 14 percent in the CPI. They are also an important source of fiscal revenues (including taxes, social security contributions and dividend payments) but their overall balance as a share of GDP fluctuates around zero.[2]



Source: MoF and staff estimates.

Some of the organizational and management practices for SOEs are aligned with international best practices.[3] SOEs publish annual reports, follow international accounting standards (for example, they use accrual accounting while the central government still has cash accounting) and their balances are audited by independent firms. Their financial statements are also revised by the Office of the Comptroller (CGN), the Office of Planning and Budget (OPP) and the National Audit Office (TCR). They must present five-year investment plans to the OPP, which are updated annually, and are required to comply with a set of performance targets agreed with the Ministry of Economy and Finance (MEF), including not just financial benchmarks but also indicators of the quality of service.[4] More recently the government has successfully implemented a public sector balance sheet approach which has allowed SOEs to hedge their FX mismatches and issue debt at lower costs (through forward sales, and joint issuance and debt exchanges).[5]

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[1] The largest SOEs include the petroleum, cement, and alcohol company ANCAP, telecommunications company ANTEL, electric utility UTE (although private-sector generation is allowed), water utility OSE, and the largest bank BROU.

[2] After running losses for five years, at end 2015, ANCAP was re-capitalized which involved the forgiveness of its US$0.6 billion (1 percent of GDP) debt to the government and the restructuring of some US$0.7 billion of the company's debt to commercial banks.

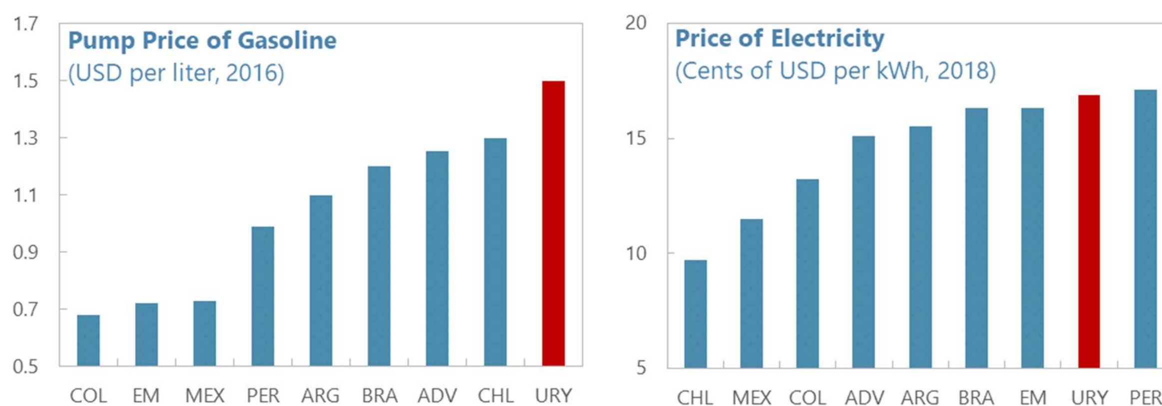
[3] See a compendium of best practice in OECD (2015), "Guidelines on Corporate Governance of State-Owned Enterprises".

[4] See further details on the Uruguayan case study in the World Bank (2014), "Tendencias del Gobierno Corporativo de las Empresas Públicas en América Latina."

[5] See further details on the Uruguayan case study in the IMF working paper 19/290.

Box 2. Reforms to Governance of State-Owned Enterprises (SOEs) (Concluded)

There is scope to improve their efficiency and transparency. Given that the supervision in Uruguay is done simultaneously by the OPP, MEF, line ministries and regulatory entities, SOEs tend to have diverse and sometimes conflicting objectives. For example, companies are required to be profitable and pay dividends to the government but must also execute investments to pursue social policies—such as subsidies for water, electricity and gas for vulnerable populations—which are not always profitable, not funded transparently from the budget and therefore involve cross subsidies.[6, 7] The lack of clear identification of multiple objectives and the strategy to optimize shareholder value while achieving socioeconomic goals makes it difficult to evaluate the results (leading to lack of accountability) and thus allows for inefficiencies (or the cost of cross-subsidies) to be translated to the final consumer (see charts). While SOEs are deemed autonomous, in practice they must coordinate tariffs with their respective ministries and the executive.



Sources: World Bank's WDI and Doing Bussines.

A corporate governance reform could further improve the management and efficiency of SOEs. Potential measures include the following: (i) SOEs need to be professionally managed, board member selections need to be transparent and merit based (boards are now appointed by the executive and commonly depend on party affiliation); (ii) SOEs should have manifest operational independence; (iii) they need to clearly present their main objectives in their annual report; (iv) their tariffs should be cost reflective and set by independent regulators; (v) they must unambiguously strive for a positive return of the invested capital (to maximize the value for society and optimize the use of resources); (vi) each line of business should transparently present its financial position, and the burden of social programs should be transparently financed from the general budget (instead of the current practice of cross-subsidies from profitable lines of business). A clear separation between the state's ownership function and market regulation can be achieved when costs related to various public policy objectives are transparently disclosed and funded by the state;[8] and (vi) the OPP could consider publishing an annual report matching the strategic goals of the state to the objectives of all the SOEs and their outcomes. These changes could help ensure that SOEs operate efficiently, transparently and in an accountable manner.

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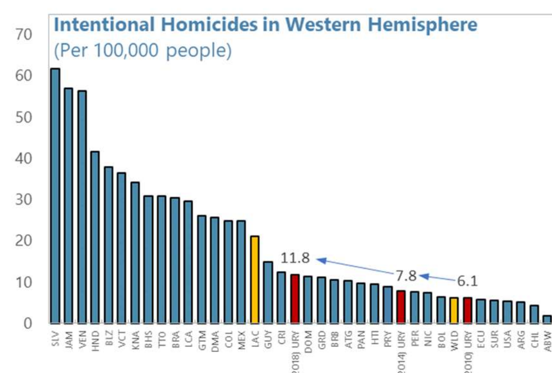
[6] See for example CERES (2019), "Empresas Públicas Primeros Pasos de Reformas."

[7] In fact, many SOEs have established satellite companies that operate under private-sector law which becomes a fertile ground for cross-subsidies across activities. See more details in Munyo and Regent (2015), "Empresas del Estado y eficiencia: La relevancia del ejercicio de la propiedad."

[8] The existing regulators in Uruguay (URSEA for water and electricity and URSEC for telecommunications) do not set prices and instead mostly focus on consumer's rights.

37. The increase in crime, albeit from a low base, needs to be addressed. In addition, in light of increasing money laundering risks, the authorities are encouraged to promptly implement recommendations of GAFILAT's[10] AML/CFT assessment, particularly to address risks from foreign proceeds of crime.



Sources: World Development Indicators (WDI) and Ministry of Interior of Uruguay. All observations—except Uruguay 2018—are for 2017 or earlier years reported to WDI.

38. In 2020, the authorities will implement the 2008 System of National Accounts, make a benchmark revision, and update the base year (from 2005 to 2012) for the GDP calculation. The authorities are planning to eventually switch from a fixed-base year to chain-linking method for the compilation of volume estimates, in line with international best practice.

39. The authorities concurred that structural reforms are essential for sustainable growth. They stressed the need to establish human capital as an area of Uruguay's competitive advantage and to improve the quality of education, in order to generate employment and provide skilled labor for the fast-growing global service export sectors. The authorities considered that the planned public investments will strengthen the quality of infrastructure and have a positive supply-side impact on growth. They agreed that wages should be allowed to continue adjusting according to productivity and noted that important progress on that front has already been made through revamped wage-setting guidelines. The authorities emphasized that institutional quality is a strong asset of Uruguay, which has created a stable social environment conducive to equitable growth. Finally, they concurred that there is room to further improve both the services provided by the SOEs and their governance.

STAFF APPRAISAL

40. Uruguay is well positioned to address the challenges that have emerged in the wake of the economic slowdown. Uruguay enjoys political stability, strong governance and institutions, a high degree of social cohesion, and low levels of poverty, inequality, and informality. In addition, the financial sector remains resilient despite regional financial market volatility, reserve buffers are sufficient, and staff assesses that the external position is broadly consistent with fundamentals and desirable policy settings. But imbalances have emerged, and external conditions have become less favorable. Growth, investment, and labor participation have been on a declining trend in recent years, and internal imbalances (higher fiscal deficits, rising

[10] Financial Action Task Force of Latin America.

unemployment) have accumulated. Debt has increased and inflation has remained outside of the target range.

41. The political and domestic economic conditions over the next few years present an opportunity for addressing Uruguay's economic challenges, but decisive actions are needed on multiple fronts. The new government will have a post-election mandate, and large-scale private investment and infrastructure projects will support growth. In addition, there is consensus across the political spectrum regarding key challenges. Action is needed on multiple fronts to reduce the accumulated imbalances and undertake structural reforms to raise potential growth and ensure intergenerational equity.

42. Under baseline projections, despite some fiscal measures supporting the projected improvement in fiscal balances, debt is expected to rise. While gross financing needs are manageable, current fiscal trends, if they continue, could undermine debt sustainability. In this context, there is a need to introduce a credible adjustment plan starting from 2020 to put debt on a firm downward path. In the absence of negative shocks and to the extent that growth picks up, the authorities will have more scope to deliver a higher adjustment for the next couple of years. This would help reduce debt faster and reduce the adjustment needs going forward. A combination of measures will be needed. A sustainable adjustment would require limiting the increase in current expenditures. Careful consideration should be given to maintaining adequate provision of key public services and safety nets. While capital expenditures, already at low levels, should be preserved, there is room to reduce tax expenditures. With the population aging and given the already high level of pension spending, reforms are needed to ensure sustainability and adequate retirement income for future generations, as well as to release resources for other priority areas. Given sizable downside risks, particularly if a gradual approach is chosen, there is a need to establish the credibility of the adjustment plan from the outset. A revamped medium-term fiscal framework, with a binding fiscal rule, would introduce a credible fiscal anchor, ensuring medium-term sustainability.

43. Inflation and inflation expectations have remained persistently above the top of the target range. If inflation stabilizes at current levels, it would leave Uruguay vulnerable to negative shocks, which could raise inflation to double digits. As the monetary policy works through its lags and in the absence of negative shocks, monetary indicative references should continue to be adjusted until inflation and inflation expectations are firmly at the mid-point of the target range. Further enhancements to the inflation targeting framework could be considered to keep inflation low and stable. These could focus on strategies, instruments, and communication practices. Continued efforts to reduce the high degree of dollarization and indexation are welcome. The authorities should also continue to use the exchange rate as a shock absorber and reserve buffers should be kept above prudential norms.

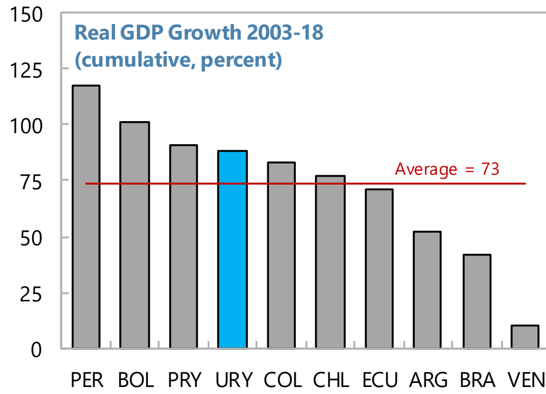
44. Building on Uruguay's institutional strengths, structural reforms are needed to raise potential growth and maintain social achievements for future generations. Closing infrastructure gaps is an important step but by itself will not be sufficient to raise growth to the levels seen in the past decade. A revival of productivity growth and private investment is critical

to sustain the coverage and generosity of the welfare state and ensure fairness across generations. In this context, action is needed to improve education outcomes and youth employment. Further wage flexibility (for small firms, low-productivity regions, and during downturns) could be considered to preserve labor rights and provide incentives for firms to create more stable jobs and invest in on-the-job training. A corporate governance reform would improve the management and efficiency of SOEs, which play a key role in the Uruguayan economy. The increase in crime, albeit from a low base, also needs to be addressed before it becomes macro-critical.

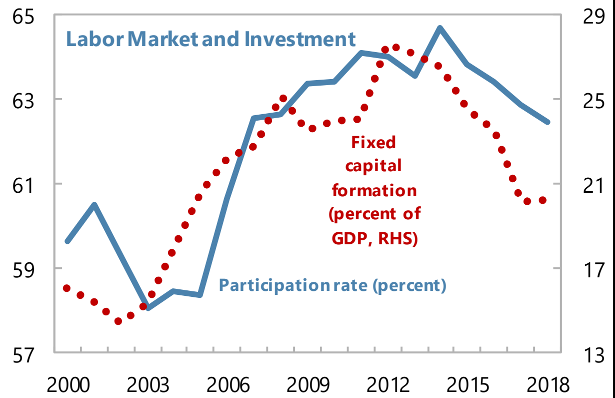
45. Staff proposes that the next Article IV consultation with Uruguay take place on the standard 12-month cycle.

Figure 1. Uruguay: Real Activity

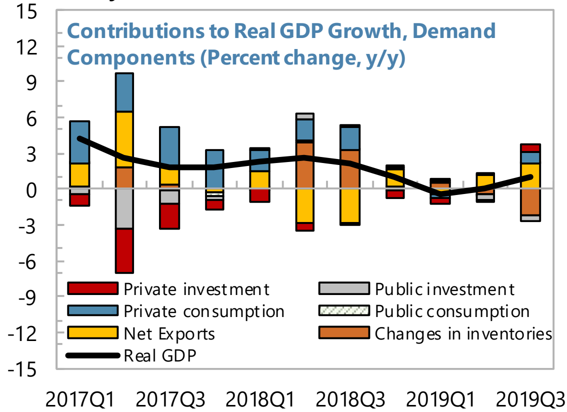
Uruguay's growth has been impressive...



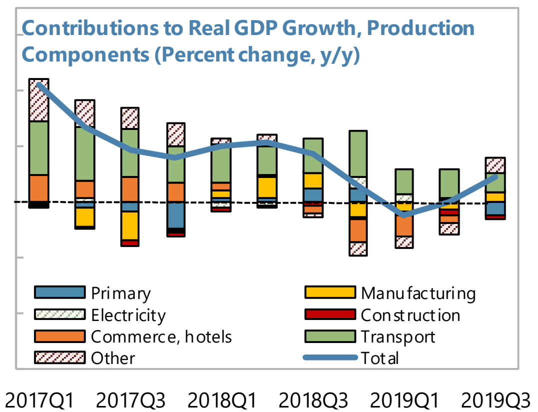
...although its drivers weakened in recent years.



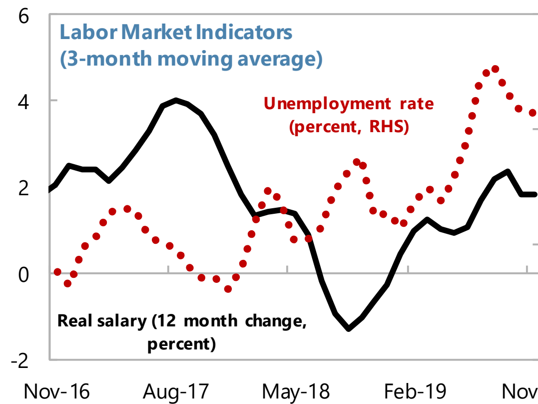
After a stagnation in 2019H1, economic activity started to recover in 2019Q3...



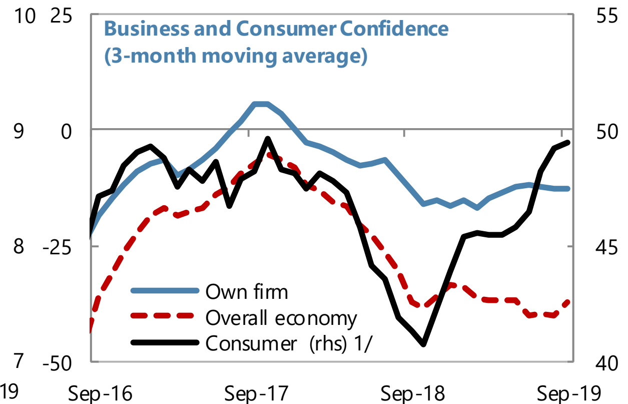
...but construction sector continued to contract.



The unemployment is elevated...



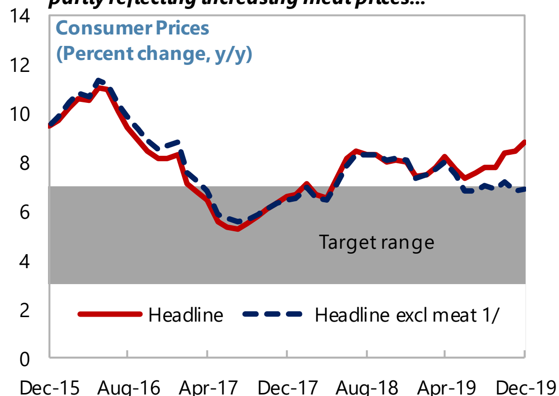
...but consumer confidence improved in line with salary gains.



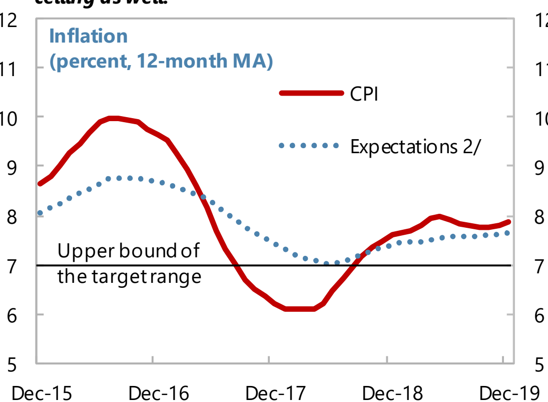
Sources: World Economic Outlook, Haver Analytics, Banco Central del Uruguay (BCU), Instituto Nacional de Estadistica, Bloomberg L.P., and IMF staff estimates and calculations.
1/ Values above 50 indicate that positive responses outnumber negative responses.

Figure 2. Uruguay: Inflation

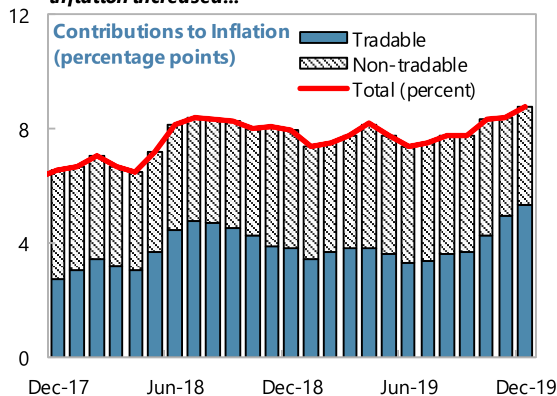
Inflation remains above the seven-percent ceiling partly reflecting increasing meat prices...



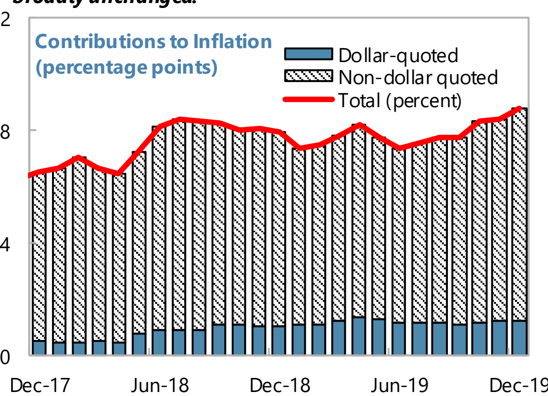
...and the medium-term expectations remain above the ceiling as well.



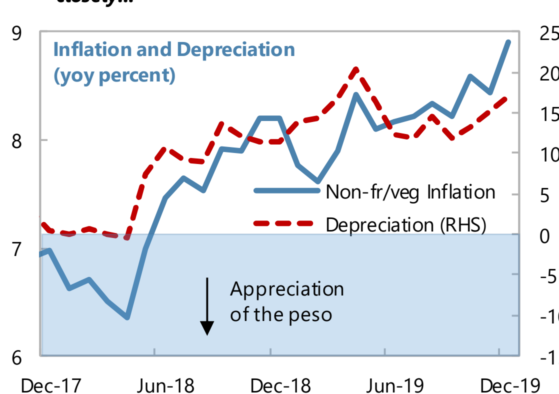
The contribution of tradable items to the total inflation increased...



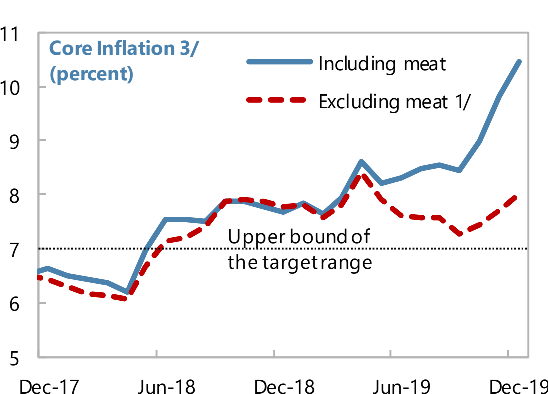
...while that of dollar-quoted items has remained broadly unchanged.



Inflation has followed the peso depreciation closely...



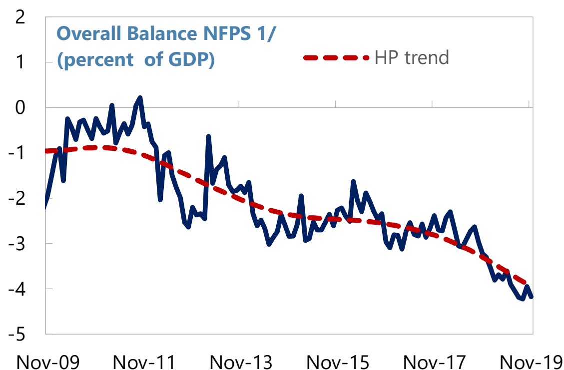
...and core inflation remains above the target range.



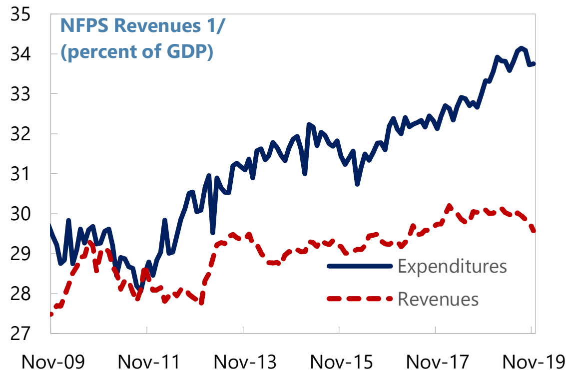
Sources: World Economic Outlook, Haver Analytics, Banco Central del Uruguay (BCU), Instituto Nacional de Estadística, Bloomberg L.P., and Fund staff estimates and calculations.
1/ Excluding meat and meat products.
2/ Expectations of inflation in the next 24 months.
3/ Core inflation is calculated as overall inflation, excluding administered prices, and prices of fruits and vegetables, in line with the BCU definition.

Figure 3. Uruguay: Fiscal Developments

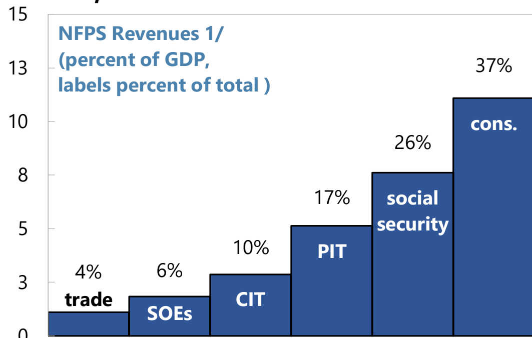
The fiscal deficit has deteriorated, particularly over the past 18 months...



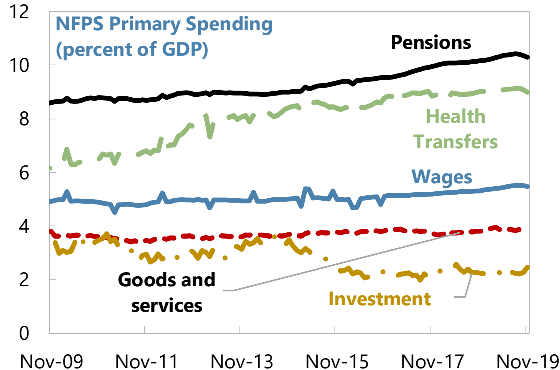
...due to a rise in spending, while revenues have remained sluggish as the economy slowed down.



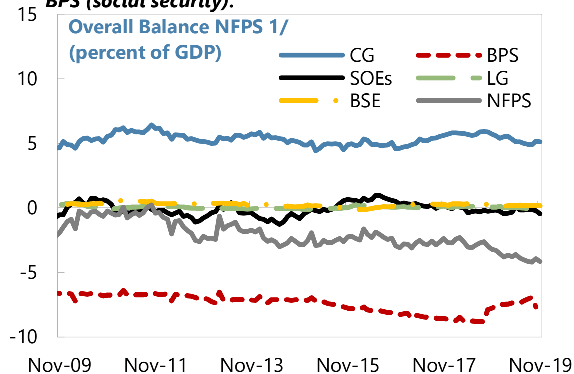
About 80 percent of revenue comes from taxes on consumption and labor, with only 10 percent from taxes on corporate income.



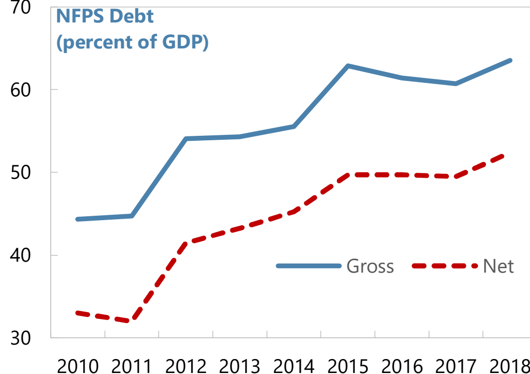
Sizeable increases in pension spending and health transfers outstripped the fall in SOEs' investments.



Thus, a sizeable central government (CG) surplus has not been enough to counter the deteriorating deficit of BPS (social security).



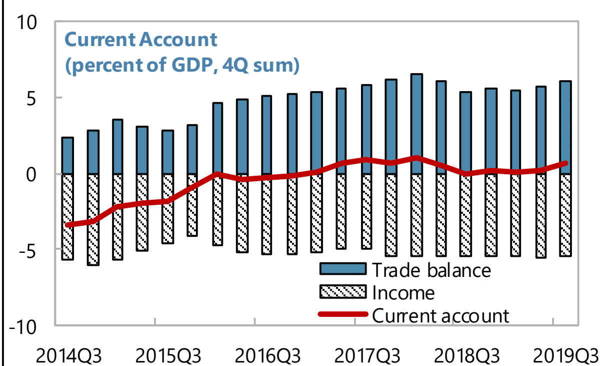
Despite the fiscal rule, which caps the rise in net debt, indebtedness has increased.



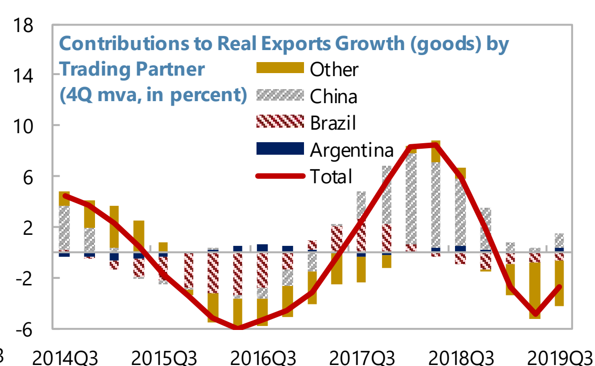
Sources: Statistics Agency, Minister of Finance, Central Bank and staff calculations.
1/ Excluding *cincuentones* transactions.

Figure 4. Uruguay: External Accounts

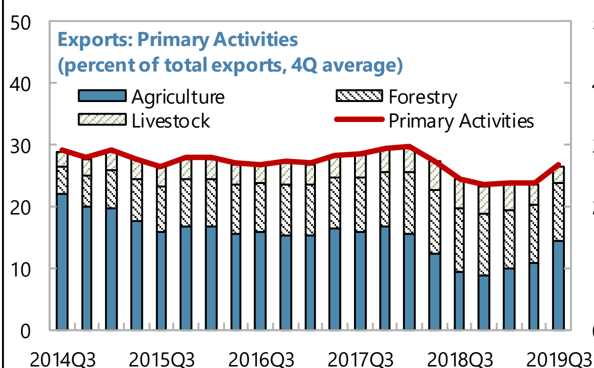
Current account surplus declined from end-2017 until early 2019 due to a deterioration in the trade balance...



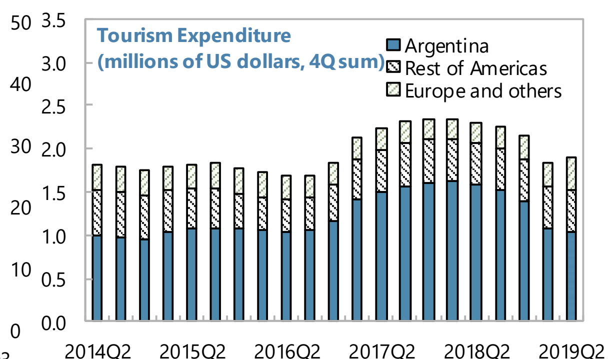
...as declining partner demand affected export performance.



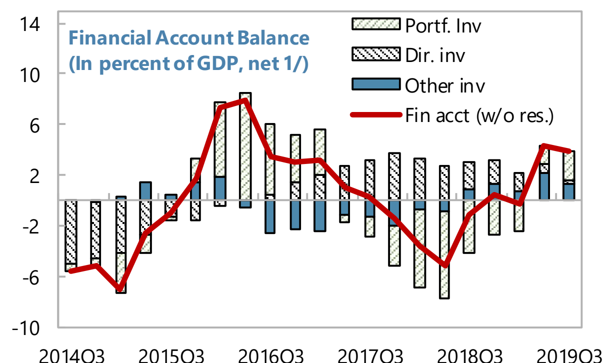
While the rebound from drought supported agricultural export volumes, lower prices of select goods dampened export values.



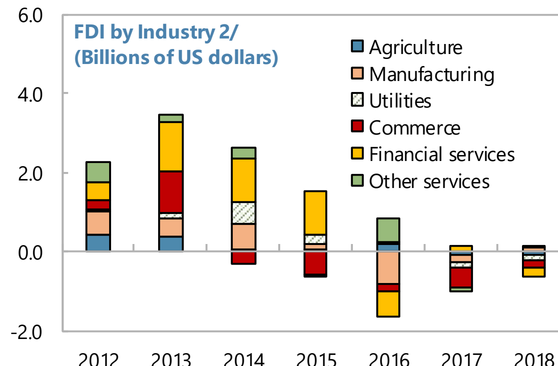
Fewer Argentinian tourists weakened service exports.



Capital outflows dominated across all investment categories in recent months...



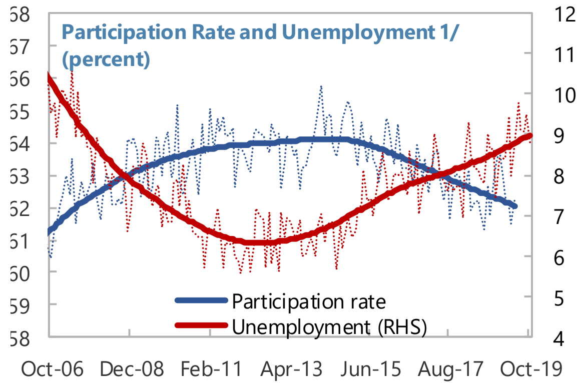
...while there has not been significant foreign direct investment over the past three years.



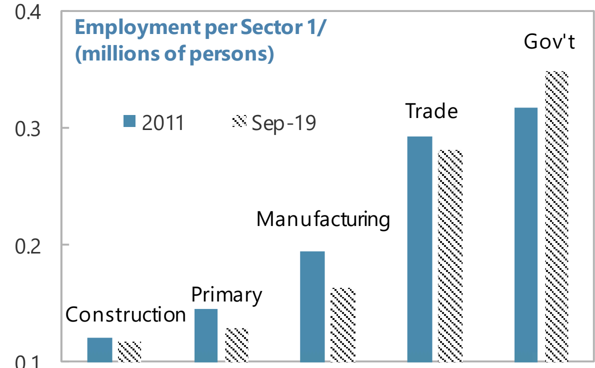
Sources: Banco Central de Uruguay (BCU), World Economic Outlook, Instituto Nacional de Estadística data, Haver Analytics, and Fund staff calculations.
1/ Positive means outflow.
2/ Positive means FDI inflow.

Figure 5. Uruguay: Labor Market Developments

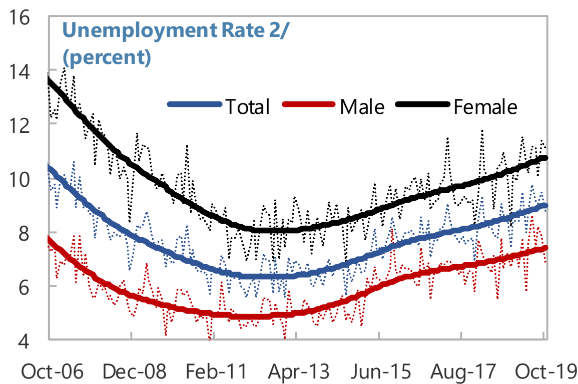
Labor market conditions have deteriorated since 2014, partly due to the economic slowdown.



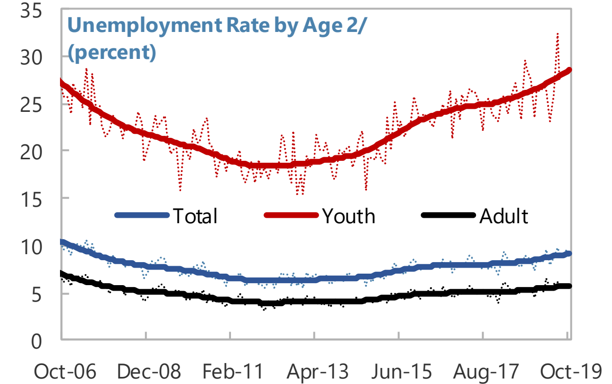
Most economic sectors have shed jobs except the government.



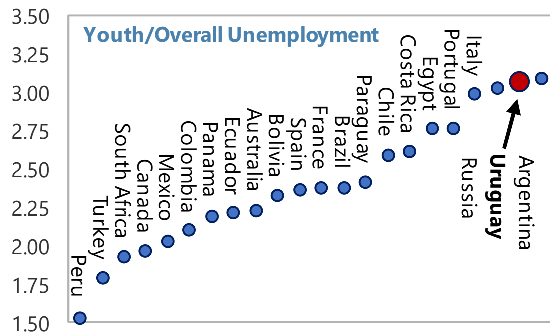
Both males and females have been affected...



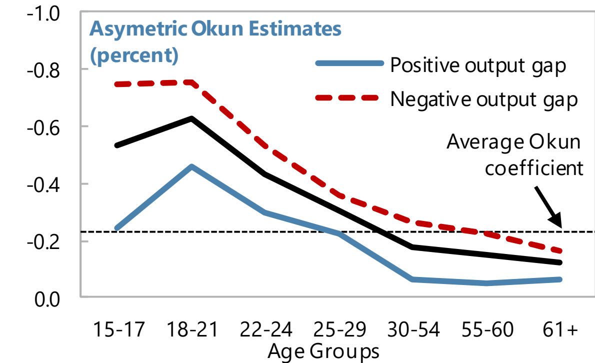
... but the young people bore the brunt of the deterioration.



The ratio of youth to overall unemployment is one of the highest in the world.



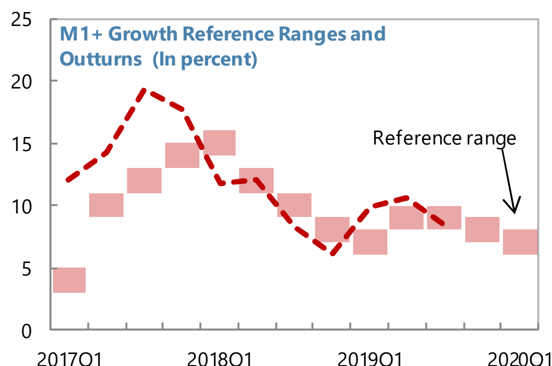
Youth unemployment is highly sensitive to busines cycle, particularly during downturns.



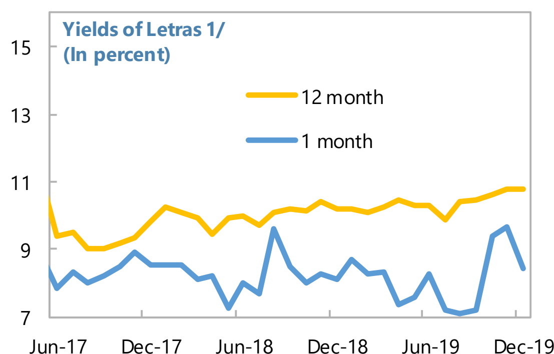
Sources: INE, ILO, World Bank, and IMF staff calculations.
1/ Government includes public administration and defense; social security; education; and social services and healthcare.
2/ Solid line HP trend.

Figure 6. Uruguay: Monetary Policy

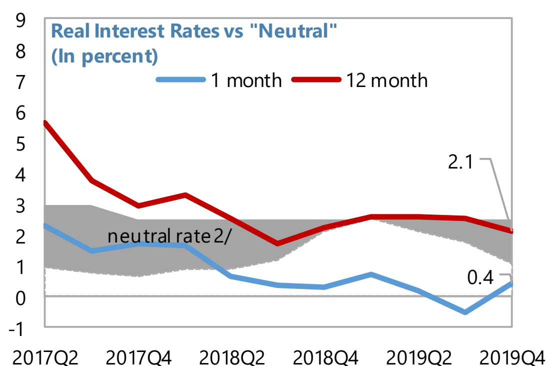
The central bank reduced its M1+ growth target for 2019Q4 and 2020Q1.



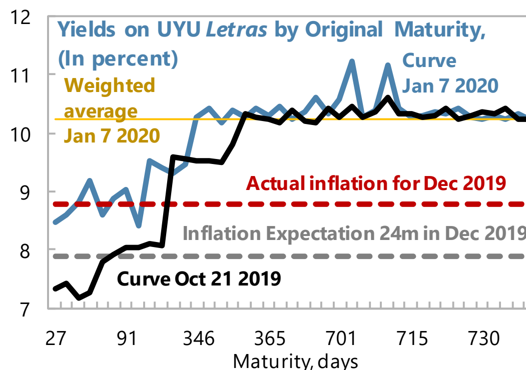
Nominal yields have started to increase.



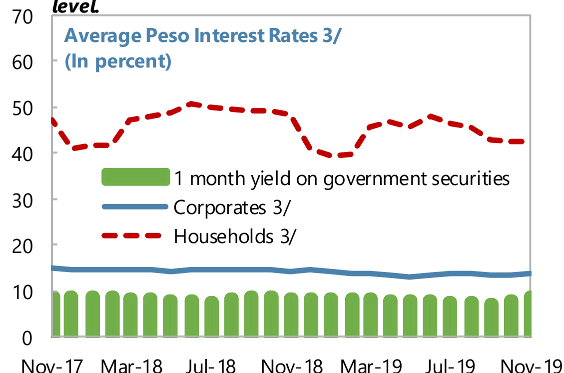
While the short-term real rates have increased, they remain below the estimated neutral rates.



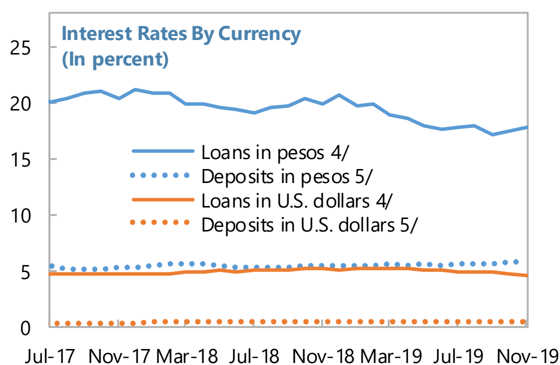
This is also reflected in the term structure of nominal yields.



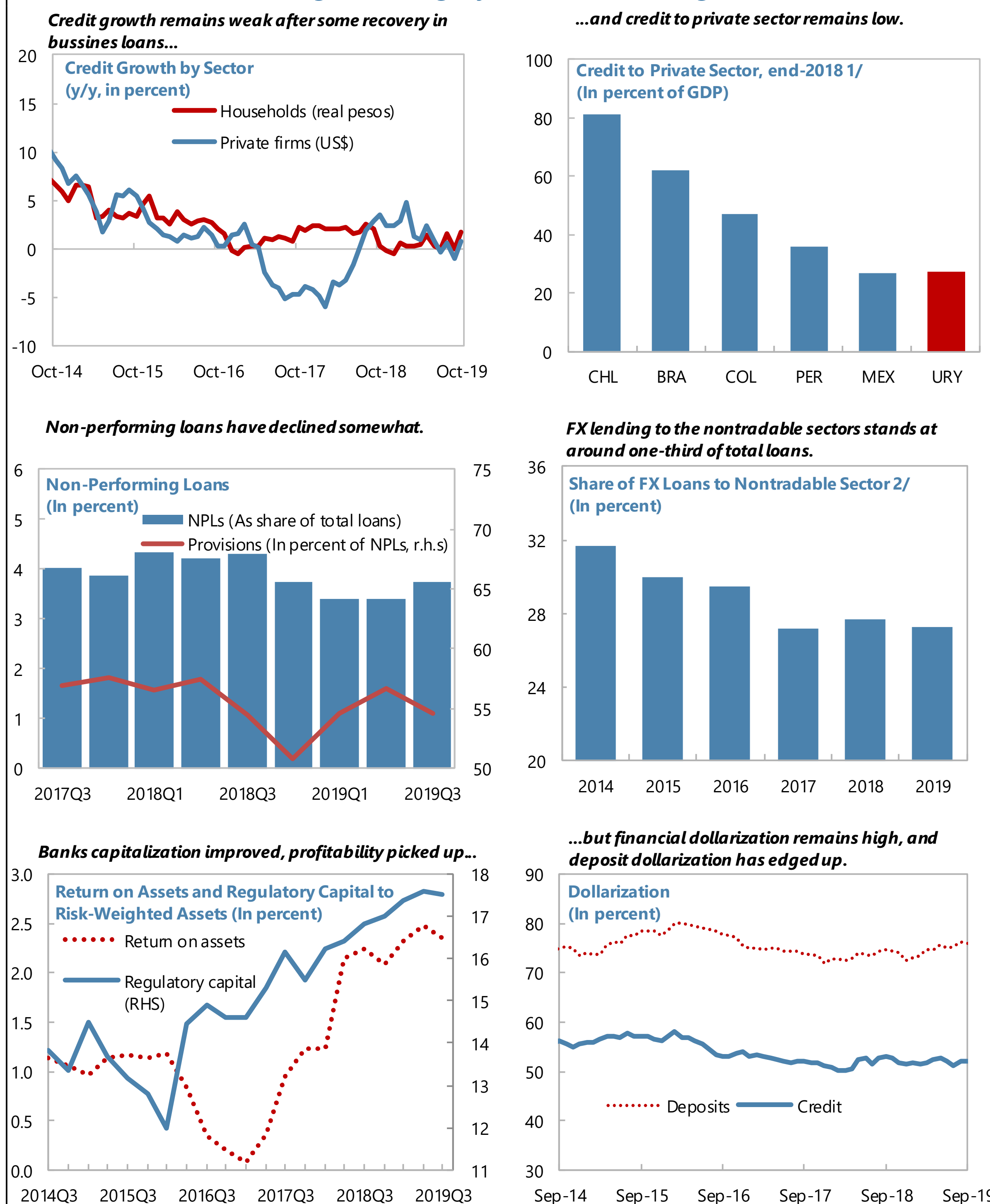
The transmision to bank lending rates has been muted, with peso interest rate for households already at a high level.



...and with a very large spread over US dollars deposits.



Sources: IMF, World Economic Outlook; Banco Central del Uruguay (BCU); and Fund staff estimates and calculations.
1/ Yields on BCU paper issued in nominal pesos.
2/ Lower limit of the neutral rate is the US real 1-month interest rate plus the risk premium, upper limit is the estimated potential growth rate.
3/ Average interest rates on new peso loans of up to one year.
4/ Annual effective interest rates, monthly weighted average, excluding restructured operations.
5/ Weighted average rate on totality of fixed term deposits.



Sources: IMF, World Economic Outlook; Banco Central del Uruguay (BCU); and Fund staff estimates and calculations.
1/ Data for Peru correspond to 2016.
2/ For 2018, data as of Q3; and for 2019, as of Q2.

Table 1. Uruguay: Selected Financial Soundness Indicators

	2013	2014	2015	2016	2017	2018	2019 1/
Currency composition							
Dollar loans in percent of total loans	56.3	55.5	57.9	54.4	51.9	50.5	50.4
Loan dollarization (constant exchange rate, January 2013) 2/	51.4	49.6	44.9	43.3	40.9	38.6	38.3
Dollar deposits in percent of total deposits	69.6	72.7	76.5	72.9	68.8	69.2	73.3
Deposit dollarization (constant exchange rate, January 2013) 2/	67.2	68.4	68.6	66.7	62.9	60.7	61.9
Credit cycle							
Private sector credit in percent of GDP 3/	22.6	24.7	26.9	27.7	25.2	25.3	26.6
Private sector credit growth in percent	17.3	8.8	1.5	1.9	2.7	0.5	-1.3
Bank soundness							
Regulatory capital in percent of risk-weighted assets	13.2	13.4	12.8	14.6	15.5	17.0	17.6
Asset quality							
Non-performing loans in percent of total loans	1.5	1.6	2.1	3.5	3.9	3.7	3.4
Specific loan-loss provisions in percent of non-performing loans	52.6	62.2	61.7	55.5	57.6	50.8	59.8
Implicit exchange rate risk 4/	33.1	31.7	30.0	29.5	27.2	27.7	27.3
Profitability							
Return on assets	1.3	1.4	1.1	0.6	0.7	1.9	2.4
Return on equity	13.1	15.6	12.5	6.4	6.6	18.4	22.9
Operating costs in percent of gross income	80.7	84.0	84.8	79.4	66.4	78.1	71.5
Liquidity							
Liquidity ratio 5/	49.3	51.8	54.5	51.3	48.5	73.0	77.4
Non-resident deposits in percent of total deposits	13.7	13.4	15.1	11.5	9.2	9.2	9.8
Deposits/Loans ratio in national currency 2/	1.0	0.9	0.8	0.8	0.9	0.8	0.9
Deposits/Loans ratio in foreign currency 2/	2.0	2.0	2.0	2.4	2.4	2.3	2.5

Sources: Banco Central del Uruguay, IMF Global Financial Stability Report, and Fund staff calculations.

Note: Unlike in previous staff reports, the data for *Banco Hipotecario del Uruguay* (BHU) are included.

1/ Data as of end October, unless otherwise specified.

2/ For 2019, data as of September.

3/ For 2019, data as of the third quarter.

4/ Foreign currency bank credit to borrowers without natural hedges as a share of total bank loans to the private sector. For 2018, data as of the third quarter and 2019 as second quarter.

5/ Liquid assets with maturity up to 30 days in percent of total liabilities expiring within the same period.

Table 2. Uruguay: Selected Economic Indicators

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
						Projections					
Output, prices, and employment											
Real GDP (percent change)	3.2	0.4	1.7	2.6	1.6	0.5	2.1	2.5	2.2	2.2	2.2
GDP (US$ billions)	57.2	53.3	52.7	59.5	59.8	57.4	58.4	61.5	64.2	67.0	69.8
Unemployment (in percent, eop)	6.6	7.5	7.9	7.9	8.4	9.2	8.4	7.7	7.5	7.5	7.5
Output gap (percent of potential output)	2.7	0.3	-0.3	0.1	0.0	-1.1	-0.6	-0.1	0.0	0.0	0.0
CPI inflation (in percent, end of period))	8.3	9.4	8.1	6.6	8.0	8.8	8.0	7.5	7.0	7.0	7.0
Exchange rate (UY$/US$, average)	23.2	27.3	30.2	28.7	30.6	...	...	...	...	...	...
Real effective exchange rate (percent change, eop)	-3.1	0.6	-5.7	5.8	2.1	...	...	...	...	...	...
	(Percent change, unless otherwise specified)										
Monetary and banking indicators 1/											
Base money	1.4	7.2	9.7	3.6	10.4	...	...	...	...	...	...
Broader M1 (M1 plus savings deposits)	3.7	5.6	8.4	15.2	8.8	...	...	...	...	...	...
M2	6.4	9.0	14.4	13.4	10.4	...	...	...	...	...	...
Growth of credit to households (in real pesos)	4.7	6.3	-0.5	2.5	1.2	...	...	...	...	...	...
Growth of credit to firms (in US$)	6.8	2.8	1.5	-4.2	2.4	...	...	...	...	...	...
Bank assets (in percent of GDP)	64.4	75.8	68.7	64.6	66.3	...	...	...	...	...	...
Private credit (in percent of GDP) 2/	27.1	30.2	28.1	26.1	27.4	...	...	...	...	...	...
	(Percent of GDP, unless otherwise specified)										
Fiscal sector indicators 3/											
Revenue NFPS	29.1	29.0	29.3	29.7	31.3	30.8	30.6	30.4	30.5	30.5	30.6
excluding *cincuentones* transactions	29.1	29.0	29.3	29.7	30.0	29.6	29.7	30.0	30.3	30.5	30.6
C*incuentones* transactions	0.0	0.0	0.0	0.0	1.3	1.2	0.9	0.4	0.2	0.0	0.0
Primary expenditure NFPS	29.5	28.8	29.9	29.8	30.6	31.1	31.0	30.7	30.9	31.0	31.0
Primary balance NFPS	-0.5	0.1	-0.5	-0.1	0.60	-0.6	-0.5	-0.3	-0.4	-0.5	-0.4
excluding *cincuentones* transactions	-0.5	0.1	-0.5	-0.1	-0.7	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Primary balance BCU	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Interest NFPS	2.3	2.3	2.6	2.6	2.6	2.4	2.7	2.8	2.8	2.8	2.8
Interest BCU	0.6	1.3	0.7	0.7	0.8	0.5	0.5	0.2	0.2	0.3	0.3
Overall balance NFPS	-2.8	-2.2	-3.1	-2.7	-2.0	-3.0	-3.2	-3.0	-3.2	-3.3	-3.2
excluding *cincuentones* transactions	-2.8	-2.2	-3.1	-2.7	-3.3	-4.2	-4.1	-3.4	-3.4	-3.3	-3.2
Overall balance PS 4/	-3.5	-3.6	-3.8	-3.5	-2.9	-3.5	-3.8	-3.3	-3.5	-3.7	-3.6
excluding *cincuentones* transactions	-3.5	-3.6	-3.8	-3.5	-4.2	-4.7	-4.7	-3.7	-3.7	-3.7	-3.6
Gross debt NFPS	55.5	62.9	61.4	60.7	63.2	66.8	66.7	66.8	67.5	68.5	68.9
Gross debt PS	61.4	64.6	61.6	65.3	67.7	71.6	73.5	74.4	75.3	76.6	77.4
Net debt NFPS	45.2	49.7	49.7	49.5	52.1	55.8	55.8	56.0	56.8	57.9	58.4
PS debt net of liquid financial assets 5/	30.3	31.3	35.9	36.5	38.8	42.8	43.8	43.9	44.7	45.6	46.1
PS debt net of total financial assets	23.0	25.8	29.9	32.1	33.7	31.8	33.4	33.9	34.7	35.8	36.4
External indicators											
Merchandise exports, fob (US$ billions)	13.8	11.1	10.4	11.1	11.5	12.0	12.7	13.4	14.5	16.2	17.4
Merchandise imports, fob (US$ billions)	11.8	9.8	8.5	8.7	9.1	9.3	11.2	12.2	13.1	13.3	14.2
Terms of trade (percent change)	3.5	3.5	3.7	0.7	-0.5	3.6	5.2	2.5	1.9	1.6	0.8
Current account balance	-3.2	-0.9	-0.1	0.7	0.1	0.2	-2.7	-3.4	-3.4	-1.7	-1.8
Foreign direct investment	-4.4	-1.5	1.4	3.8	1.9	1.7	0.5	0.5	1.1	1.4	1.5
Total external debt + non-resident deposits	74.9	89.5	74.4	68.1	69.3	71.9	75.6	77.1	79.6	81.6	83.8
Of which: External public debt	33.7	37.1	31.6	30.4	32.6	36.1	36.8	38.3	40.8	42.9	45.1
External debt service (in percent of exports of g&s)	65.5	90.2	87.9	68.2	62.5	56.7	58.3	60.2	59.3	57.0	55.9
Gross official reserves (US$ billions)	17.6	15.6	13.5	15.9	15.5	14.5	15.6	16.8	17.8	18.8	19.8
In months of imports of goods and services	12.6	13.5	13.7	15.4	14.2	13.0	12.1	12.3	12.2	12.5	12.5
In percent of:											
Short-term external (STE) debt	188	173	196	242	255	246	251	257	260	263	267
STE debt plus banks' non-resident deposits	228	220	210	317	314	261	265	269	269	273	281

Sources: Banco Central del Uruguay, Ministerio de Economia y Finanzas, Instituto Nacional de Estadistica, and Fund staff calculations.

1/ Percent change of end-of-year data on one year ago.

2/ Includes bank and non-bank credit.

3/ The non-financial public sector (NFPS) includes the Central Government, Banco de Prevision Social, Banco de Seguros del Estado, local governments, and Non-Financial Public Enterprises.

4/ Total public sector (PS). Includes the NFPS and Banco Central del Uruguay.

5/ Gross debt of the public sector minus liquid financial assets of the public sector. Liquid financial assets arecalculated by deducting from total public sector assets the part of central bank reserves held as a counterpart to required reserves on foreign currency deposits.

Table 3. Uruguay: Balance of Payments and External Sector Indicators

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
						Projections					
	(In billions of U.S. dollars, unless otherwise indicated)										
Balance of Payments											
Current account	-1.8	-0.5	-0.1	0.4	0.1	0.1	-1.5	-2.1	-2.2	-1.1	-1.2
Trade balance	2.0	1.3	1.9	2.4	2.4	2.8	1.5	1.2	1.4	2.9	3.2
Exports of goods	13.8	11.1	10.4	11.1	11.5	12.0	12.7	13.4	14.5	16.2	17.4
Imports of goods	11.8	9.8	8.5	8.7	9.1	9.3	11.2	12.2	13.1	13.3	14.2
Of which: Fuel products	1.7	1.0	0.7	0.9	1.2	1.0	1.1	1.1	1.1	1.1	1.2
Of which: Non-fuel products	10.1	8.8	7.7	7.7	8.0	8.2	10.1	11.1	12.0	12.2	13.0
Services balance	-0.4	0.4	0.8	1.3	0.9	0.7	0.4	0.4	0.4	0.4	0.4
Exports, f.o.b.	4.6	4.5	4.2	5.0	4.9	4.8	4.7	4.6	4.8	5.0	5.3
Imports, f.o.b.	5.0	4.1	3.3	3.8	4.0	4.1	4.3	4.2	4.4	4.7	4.9
Income balance	-3.4	-2.2	-2.8	-3.2	-3.2	-3.3	-3.5	-3.7	-4.0	-4.4	-4.9
Financial and capital account balance	-1.6	-0.6	-0.6	1.6	-0.1	0.2	-1.5	-2.0	-2.1	-1.0	-1.1
Foreign direct investment	-2.5	-0.8	0.7	2.2	1.1	1.0	0.3	0.3	0.7	0.9	1.0
Portfolio investment	-0.3	1.0	2.0	-1.9	-1.6	4.3	4.3	4.3	4.3	4.3	4.3
Financial derivatives and other investments (net)	-0.1	0.8	-1.2	-1.2	0.8	-4.0	-7.2	-7.8	-8.1	-7.3	-7.5
Change in reserve assets	1.4	-1.7	-2.2	2.4	-0.4	-1.1	1.2	1.2	1.0	1.0	1.1
Net errors and omissions	0.2	-0.4	-0.5	1.2	-0.3	0.0	0.0	0.0	0.0	0.0	0.0
Reserve Adequacy and External Indicators											
Gross official reserves (stock)	17.6	15.6	13.5	15.9	15.5	14.5	15.6	16.8	17.8	18.8	19.8
In months of imports of goods and services	12.6	13.5	13.7	15.4	14.2	13.0	12.1	12.3	12.2	12.5	12.5
In percent of short-term debt	187.6	173.0	195.8	241.8	254.9	245.7	250.5	256.6	259.5	262.8	266.9
	(As percent of GDP)										
Balance of Payments											
Current account	-3.2	-0.9	-0.1	0.7	0.1	0.2	-2.7	-3.4	-3.4	-1.7	-1.8
Trade balance	3.5	2.5	3.6	4.0	4.1	4.8	2.6	1.9	2.2	4.3	4.6
Exports of goods	24.1	20.9	19.7	18.6	19.3	20.9	21.8	21.8	22.6	24.2	24.9
Imports of goods	-20.6	-18.5	-16.1	-14.6	-15.2	-16.1	-19.2	-19.9	-20.4	-19.9	-20.3
Of which: Fuel products	3.0	1.9	1.4	1.6	1.9	1.8	1.9	1.8	1.7	1.7	1.7
Of which: Non-fuel products	17.6	16.5	14.7	13.0	13.3	14.3	17.3	18.1	18.7	18.2	18.6
Services balance	-0.6	0.8	1.6	2.1	1.4	1.2	0.7	0.7	0.6	0.6	0.6
Exports	8.1	8.4	7.9	8.4	8.1	8.3	8.0	7.5	7.5	7.5	7.7
Imports	8.7	7.6	6.3	6.3	6.7	7.1	7.3	6.8	6.9	6.9	7.0
Income balance	-6.0	-4.2	-5.3	-5.4	-5.4	-5.8	-6.0	-6.0	-6.2	-6.6	-7.0
Financial and capital account balance	-2.7	-1.1	-1.1	2.7	-0.2	0.4	-2.5	-3.2	-3.2	-1.5	-1.6
Foreign direct investment	-4.4	-1.5	1.4	3.8	1.9	1.7	0.5	0.5	1.1	1.4	1.5
Portfolio investment	-0.6	1.9	3.9	-3.2	-2.7	7.4	7.3	6.9	6.7	6.4	6.1
Financial derivatives and other investments (net)	-0.2	1.4	-2.2	-2.0	1.3	-7.0	-12.3	-12.7	-12.6	-10.8	-10.8
Change in reserve assets	2.4	-3.1	-4.2	4.1	-0.7	-1.9	2.0	2.0	1.5	1.5	1.5
Total external debt	72.0	82.1	75.9	69.3	69.3	71.9	75.6	77.1	79.6	81.6	83.8
Of which: Short-term debt (residual maturity)	16.4	17.0	13.1	11.1	10.2	10.3	10.7	10.7	10.7	10.7	10.6
Of which: External public debt	33.7	37.2	31.6	30.1	32.6	36.1	36.8	38.3	40.8	42.9	45.1
	(As percent of annual exports of goods and services)										
External Debt											
Total external debt (including non-resident deposits)	224	280	275	257	253	246	253	263	264	257	257
Debt service	65.5	90.2	87.9	68.2	62.5	56.7	58.3	60.2	59.3	57.0	55.9
Of which: Interest payments	1.1	1.2	1.2	1.2	1.4	1.3	1.3	1.4	1.5	1.6	1.7
	(Annual percent changes)										
External Trade											
Exports of goods in US$	3.7	-19.1	-6.9	6.6	4.3	4.3	5.8	5.2	8.2	12.0	7.1
Imports of goods in US$	-3.4	-16.5	-14.0	2.4	5.1	1.7	21.2	8.9	7.1	1.7	6.5
Export prices in US$	-0.4	-9.8	-3.5	2.9	1.8	1.5	5.0	0.7	0.5	0.9	1.5
Import prices in US$	-1.6	-8.2	-3.7	3.2	4.3	0.1	0.6	0.0	0.4	0.9	2.1
Terms of trade for goods	3.5	3.5	3.7	0.7	-0.5	3.6	5.2	2.5	1.9	1.6	0.8
Export volume (goods and non-factor services)	4.1	-10.3	-3.6	3.6	2.4	2.7	0.8	4.5	7.6	11.0	5.5
Import volume (goods and non-factor services)	-0.5	-5.5	-8.7	-1.1	0.0	2.3	21.3	9.9	7.4	1.3	4.5
Export volume (goods)	4.1	-10.3	-3.6	3.6	2.4	2.7	0.8	4.5	7.6	11.0	5.5
Import volume (goods)	-0.5	-5.5	-8.7	-1.1	0.0	2.3	21.3	9.9	7.4	1.3	4.5
Of which: Non-fuel products	1.1	-7.4	-8.1	-1.5	0.6	2.6	23.4	10.2	7.5	0.9	4.4
Of which: Fuel products	-9.4	13.4	-15.3	2.6	-4.0	-0.7	5.3	6.3	5.5	5.5	5.5

Sources: Banco Central del Uruguay and Fund staff calculations and projections.

Table 4. Uruguay: Main Fiscal Aggregates

						Projections					
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
	(In billions of pesos, unless otherwise indicated)										
I. Primary balance NFPS (A+B+C)	-7	1	-7	-2	11	-13	-12	-7	-10	-15	-13
excluding *cincuentones* transactions	-7	1	-7	-2	-12	-36	-32	-16	-15	-15	-13
A. Primary balance of CG, BPS and NFPE 1/ 2/	-5	3	-9	-2	13	-7	-10	-7	-10	-15	-13
Revenues	387	422	465	508	573	616	684	754	827	903	986
Taxes CG	244	263	299	335	365	397	450	501	549	599	653
VAT and excise taxes	151	163	174	193	204	218	245	273	299	326	355
On income and profits	75	83	107	129	143	152	171	191	209	228	248
Other	18	18	19	13	18	27	34	37	41	45	49
Non tax CG	22	23	24	26	32	29	32	36	39	43	47
Social security (BPS)	101	109	118	131	163	176	190	198	211	225	245
of which: *cincuentones* transactions	0	0	0	0	23	24	19	10	5	0	0
Primary balance NFPE	20	27	24	16	13	14	12	19	28	36	41
Primary expenditures	392	419	474	509	560	623	694	760	837	917	999
Current	349	385	436	474	519	575	640	701	772	846	922
Wages	67	73	82	89	98	110	121	131	144	157	171
Goods and services	49	55	62	63	70	78	87	92	106	118	129
Social security benefits	210	239	269	302	329	361	404	447	489	534	582
Other	22	19	23	20	23	25	28	31	34	37	40
Capital	43	34	39	35	41	48	54	59	65	71	77
B. Primary balance of local governments	-2	2	1	1	1	-2	0	0	0	0	0
C. Primary balance of BSE 3/	-1	-4	1	-2	-3	-4	-2	0	0	0	0
II. Primary balance of the BCU 4/	-1	-1	-1	-1	-2	-2	-2	-2	-2	-2	-3
III. Primary balance of the PS (I+II)	-8	0	-9	-4	10	-14	-14	-9	-12	-17	-16
IV. Interest of the PS	38	52	52	56	63	57	72	72	82	91	100
A. NFPS 4/	30	33	42	44	48	47	60	68	76	83	90
B. BCU 4/	7	18	10	12	15	9	12	4	7	8	9
V. Overall balance of the PS (III+IV)	-46	-52	-61	-59	-53	-71	-86	-81	-94	-108	-116
A. NFPS 4/	-38	-32	-49	-46	-37	-60	-72	-75	-86	-97	-104
excluding *cincuentones* transactions	-38	-32	-49	-46	-61	-83	-91	-84	-91	-97	-104
B. BCU 4/	-8	-20	-12	-13	-16	-11	-14	-6	-9	-11	-12
VI. Overall balance PS excluding cincuentones transactions	-46	-52	-61	-59	-77	-94	-105	-91	-100	-108	-116
	(In percent of GDP, unless otherwise indicated)										
I. Primary balance NFPS (A+B+C)	-0.5	0.1	-0.5	-0.1	0.6	-0.6	-0.5	-0.3	-0.4	-0.5	-0.4
excluding *cincuentones* transactions	-0.5	0.1	-0.5	-0.1	-0.7	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
A. Primary balance of CG, BPS and NFPE 1/ 2/	-0.3	0.2	-0.6	-0.1	0.7	-0.3	-0.4	-0.3	-0.4	-0.5	-0.4
Revenues	29.1	29.0	29.3	29.7	31.3	30.8	30.6	30.4	30.5	30.5	30.6
excluding *cincuentones* transactions	29.1	29.0	29.3	29.7	30.0	29.6	29.7	30.0	30.3	30.5	30.6
Taxes CG	18.4	18.1	18.8	19.6	19.9	19.9	20.1	20.2	20.3	20.2	20.3
VAT and excise taxes	11.3	11.2	10.9	11.3	11.1	10.9	11.0	11.0	11.0	11.0	11.0
On income and profits	5.7	5.7	6.7	7.5	7.8	7.6	7.7	7.7	7.7	7.7	7.7
Other	1.4	1.2	1.2	0.8	1.0	1.3	1.5	1.5	1.5	1.5	1.5
Non tax CG	1.6	1.6	1.5	1.5	1.7	1.5	1.5	1.5	1.5	1.5	1.5
Social security (BPS)	7.6	7.5	7.5	7.7	8.9	8.8	8.5	8.0	7.8	7.6	7.6
of which: *cincuentones* transactions	0.0	0.0	0.0	0.0	1.3	1.2	0.9	0.4	0.2	0.0	0.0
Primary balance NFPE	1.5	1.8	1.5	0.9	0.7	0.7	0.5	0.8	1.0	1.2	1.3
Primary expenditures	29.5	28.8	29.9	29.8	30.6	31.1	31.0	30.7	30.9	31.0	31.0
Current	26.2	26.5	27.4	27.8	28.4	28.7	28.6	28.3	28.5	28.6	28.6
Wages	5.0	5.0	5.1	5.2	5.3	5.5	5.4	5.3	5.3	5.3	5.3
Goods and services	3.7	3.7	3.9	3.7	3.8	3.9	3.9	3.7	3.9	4.0	4.0
Social security benefits	15.8	16.4	16.9	17.7	18.0	18.1	18.1	18.1	18.1	18.1	18.1
Other	1.7	1.3	1.5	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Capital	3.2	2.3	2.4	2.1	2.2	2.4	2.4	2.4	2.4	2.4	2.4
B. Primary balance of local governments	-0.2	0.1	0.1	0.1	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
C. Primary balance of BSE 3/	0.0	-0.3	0.0	-0.1	-0.2	-0.2	-0.1	0.0	0.0	0.0	0.0
II. Primary balance of the BCU 4/	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
III. Primary balance of the PS (I+II)	-0.6	0.0	-0.5	-0.2	0.5	-0.7	-0.6	-0.3	-0.4	-0.6	-0.5
IV. Interest of the PS	2.8	3.6	3.3	3.3	3.4	2.8	3.2	2.9	3.0	3.1	3.1
A. NFPS 4/	2.3	2.3	2.6	2.6	2.6	2.4	2.7	2.8	2.8	2.8	2.8
B. BCU 4/	0.6	1.3	0.7	0.7	0.8	0.5	0.5	0.2	0.2	0.3	0.3
V. Overall balance of the PS (III+IV)	-3.5	-3.6	-3.8	-3.5	-2.9	-3.5	-3.8	-3.3	-3.5	-3.7	-3.6
A. NFPS 4/	-2.8	-2.2	-3.1	-2.7	-2.0	-3.0	-3.2	-3.0	-3.2	-3.3	-3.2
excluding *cincuentones* transactions	-2.8	-2.2	-3.1	-2.7	-3.3	-4.2	-4.1	-3.4	-3.4	-3.3	-3.2
B. BCU 4/	-0.6	-1.4	-0.8	-0.8	-0.9	-0.5	-0.6	-0.3	-0.3	-0.4	-0.4
VI. Overall balance PS excluding cincuentones transactions	-3.5	-3.6	-3.8	-3.5	-4.2	-4.7	-4.7	-3.7	-3.7	-3.7	-3.6
Memorandum Items:											
Real revenues growth (in percent)	1.9	0.1	2.7	4.1	6.9	-1.1	1.4	2.1	2.5	2.1	2.5
Real primary spending growth (in percent)	5.7	1.1	3.5	2.1	2.2	2.9	2.4	1.6	2.5	2.7	1.8
GDP (in billions of pesos)	1,331	1,456	1,589	1,708	1,831	2,002	2,238	2,477	2,708	2,959	3,224

Sources: Ministerio de Economia y Finanzas, Banco Central del Uruguay, and Fund staff calculations.

1/ Banco de Prevision Social (BPS).

2/ Non-financial public enterprises (NFPE).

3/ Banco de Seguros del Estado (BSE).

4/ Banco Central del Uruguay (BCU).

Table 5. Uruguay: Public Sector Debt and Financial Assets 1/

						Projections					
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
	(In billions of U.S. dollars, unless otherwise indicated)										
Public Sector Debt											
Gross debt of the public sector	33.5	31.4	33.4	38.7	38.3	38.4	41.9	44.7	47.3	50.2	52.8
of which:											
Non-financial public sector debt	30.3	30.6	33.3	36.0	35.7	35.8	38.0	40.1	42.4	44.9	47.1
Central bank debt	9.1	5.8	5.6	8.3	7.5	7.3	8.9	9.9	10.4	11.1	11.8
External debt of the public sector	18.4	18.1	17.1	17.9	18.4	19.4	21.0	23.0	25.6	28.1	30.8
Domestic debt of the public sector	15.1	13.3	16.2	20.9	19.9	19.1	20.9	21.7	21.7	22.1	22.0
Public Sector Financial Assets											
Gross financial assets of the public sector	21.0	18.9	17.1	19.7	19.2	21.4	22.8	24.3	25.5	26.7	28.0
of which:											
Financial assets of the non-financial public sector	5.6	6.4	6.3	6.7	6.3	5.9	6.2	6.5	6.7	6.9	7.2
Financial assets of the central bank	18.5	16.6	14.4	16.9	16.6	15.5	16.6	17.8	18.8	19.8	20.8
Liquid financial assets of the central bank 2/	11.4	9.8	7.6	10.4	10.1	9.6	10.7	11.8	12.6	13.4	14.2
Liquid financial assets of the public sector 2/	17.0	16.2	13.9	17.1	16.4	15.5	16.9	18.3	19.3	20.3	21.4
Net Public Sector Debt											
Gross debt minus liquid financial assets 2/	16.5	15.2	19.4	21.6	21.9	22.9	24.9	26.4	28.0	29.9	31.4
Public sector debt net of total financial assets	12.5	12.5	16.2	19.0	19.1	17.0	19.0	20.3	21.8	23.5	24.8
	(In percent of GDP, unless otherwise indicated) 1/										
Public Sector Debt											
Gross debt of the public sector	61.4	64.6	61.6	65.3	67.7	71.6	73.5	74.4	75.3	76.6	77.4
of which:											
Non-financial public sector debt	55.5	62.9	61.4	60.7	63.2	66.8	66.7	66.8	67.5	68.5	68.9
Central bank debt	16.6	12.0	10.4	14.0	13.3	13.7	15.7	16.5	16.6	16.9	17.3
External debt of the public sector	33.7	37.2	31.6	30.1	32.6	36.1	36.8	38.3	40.8	42.9	45.1
Domestic debt of the public sector	27.7	27.4	30.0	35.2	35.2	35.5	36.7	36.1	34.6	33.7	32.3
Public Sector Financial Assets											
Gross financial assets of the public sector	38.5	38.8	31.6	33.2	34.0	39.9	40.1	40.5	40.6	40.8	41.0
of which:											
Financial assets of the non-financial public sector	10.3	13.2	11.7	11.2	11.1	11.0	10.9	10.8	10.7	10.6	10.5
Financial assets of the central bank	33.8	34.1	26.6	28.5	29.3	28.9	29.2	29.7	29.9	30.2	30.5
Liquid financial assets of the central bank 2/	20.8	20.1	14.0	17.6	17.9	17.9	18.8	19.7	20.0	20.4	20.8
Liquid financial assets of the public sector 2/	31.1	33.3	25.7	28.8	29.0	28.9	29.7	30.5	30.7	31.0	31.3
Net Public Sector Debt											
Gross debt minus liquid financial assets 2/	30.3	31.3	35.9	36.5	38.8	42.8	43.8	43.9	44.7	45.6	46.1
Public sector debt net of total financial assets	23.0	25.8	29.9	32.1	33.7	31.8	33.4	33.9	34.7	35.8	36.4
Memorandum Items											
GDP (in billions of pesos)	1,331	1,456	1,589	1,708	1,831	2,002	2,238	2,477	2,708	2,959	3,224
GDP (in billions of USD)	57.2	53.3	52.7	59.5	59.8	57.4	58.4	61.5	64.2	67.0	69.8

Sources: Ministerio de Economia y Finanzas, Banco Central del Uruguay, and Fund staff calculations.

1/ Stocks are converted into pesos using the end of period exchange rate and divided by GDP.

2/ Liquid financial assets are given by deducting from total public sector financial assets the part of central bank reserves held as a counterpart to required reserves on foreign currency deposits.

Table 6. Uruguay: Statement of Operations of the Central Government 1/

	2013	2014	2015	2016	2017	2018
	(In percent of GDP, based on the 2001 GFS Manual)					
Revenue	31.1	28.9	30.4	41.3	38.0	40.1
Taxes	19.0	18.6	18.5	23.7	19.7	20.1
Social contributions	10.1	8.5	10.4	10.5	10.8	10.9
Grants	0.0	0.0	0.0	5.2	5.6	5.7
Other revenue	2.0	1.8	1.5	1.9	1.9	3.5
Expense	31.2	29.8	31.9	43.6	39.7	40.7
Compensation of employees	7.2	7.4	7.4	12.5	8.8	8.8
Use of goods and services	3.7	3.7	3.4	3.9	3.7	3.8
Consumption of fixed capital 2/	0	0	0	0	0	0
Interest	2.4	2.3	2.2	2.7	2.7	2.8
Subsidies	0.2	0.2	0.3	0.4	0.2	0.2
Grants	0.0	0.0	0.0	5.2	5.6	5.7
Social benefits	14.5	13.3	15.3	15.8	15.6	16.1
Other expenses	3.2	2.9	3.3	3.2	3.1	3.3
Net acquisition of nonfinancial assets	1.4	1.4	1.2	1.4	1.3	1.5
Gross operating balance	-0.1	-0.9	-1.5	-2.3	-1.7	-0.6
Net operating balance 2/	-0.1	-0.9	-1.5	-2.3	-1.7	-0.6
Net lending (+) borrowing (-)	-1.5	-2.3	-2.7	-3.7	-3.0	-2.0
Net acquisition of financial assets	-0.3	0.2	2.1	-1.8	-0.4	-0.7
By instrument						
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	-0.9	0.7	1.8	-1.0	-0.4	-0.9
Debt securities	-0.1	0.0	-0.1	-0.1	-0.1	0.2
Loans	0.8	-0.4	0.4	-0.7	0.1	0.0
Equity and shares	0.0	0.0	0.0	0.0	0.0	0.0
By residency						
Domestic	-0.3	0.2	2.1	-1.8	-0.4	-0.7
External	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	1.3	2.5	5.1	3.1	2.6	1.4
By instrument						
SDRs	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	2.1	2.3	4.9	2.3	2.6	1.0
Loans	-0.8	0.2	0.2	0.8	0.0	0.5
Equity and shares	0.0	0.0	0.0	0.0	0.0	0.0
By residency						
Domestic	-1.4	0.1	3.0	4.3	1.8	-0.2
External	2.7	2.5	2.1	-1.3	0.8	1.7
Memorandum items:						
Public sector net lending (+) borrowing (-)	-2.3	-3.5	-3.6	-3.8	-3.5	-2.9
Public sector primary balance	0.4	-0.6	0.0	-0.5	-0.2	0.5

Sources: Banco Central del Uruguay, and Fund staff calculations.
1/ Central government and Social Security Bank. Collection of above the line data for municipalities is not feasible at this moment. The below-the-line data for 2013-17 are not consolidated.
2/ Not compiled by the authorities until 2013.

Table 7. Uruguay: Central Government Stock Positions 1/

	2011	2012	2013	2014	2015	2016	2017	2018
	percent of GDP, based on the 2001 GFS Manu							
Net financial worth	-35.0	-33.5	-33.8	-35.3	-41.7	-41.3	-40.4	-43.4
Financial assets	10.4	9.9	8.9	9.1	9.5	9.4	8.9	9.6
By instrument								
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	6.8	6.6	4.7	5.3	5.8	6.5	5.7	5.1
Debt securities	2.5	2.5	2.2	2.2	2.1	2.1	2.1	3.4
Loans	0.6	0.5	1.7	1.2	1.3	0.5	0.9	0.8
Equity and shares	0.5	0.4	0.3	0.3	0.3	0.2	0.2	0.2
By residency								
Domestic	10.3	9.9	8.9	9.1	9.5	9.3	8.9	9.6
External	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0
Liabilities	45.4	43.4	42.7	44.4	51.2	50.7	49.2	53.0
By instrument								
SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt securities	34.6	34.3	35.1	37.0	44.2	43.7	44.0	47.1
Loans	10.7	9.1	7.6	7.4	7.0	7.0	5.2	5.9
Equity and shares	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
By residency								
Domestic	21.0	19.4	16.9	16.9	19.4	22.9	22.7	23.5
External	24.3	24.0	25.9	27.5	31.8	27.8	26.5	29.5

Sources: Banco Central del Uruguay, and Fund staff calculations.

1/ Central government and Social Security Bank. Data for 2013-18 are not consolidated.

Table 8. Uruguay: Monetary Survey

	2013	2014	2015	2016	2017	2018
	(End of period, in billion of pesos)					
Banco Central del Uruguay (BCU)						
Net foreign assets	331	408	458	399	461	517
Gross international reserves	348	428	467	394	459	504
Net domestic assets	-210	-286	-353	-285	-330	-379
Net credit to the public sector	76	71	31	60	104	99
Net credit to the financial system	-129	-192	-250	-202	-176	-205
Credit to the private sector	0	0	1	1	1	1
Securities issued by the BCU	-202	-202	-126	-125	-250	-250
Other	30	11	-49	-55	-56	-80
Peso monetary liabilities 1/	121	121	105	113	131	138
Public and Private Banks 2/						
Net foreign assets	65	74	144	177	168	201
Net domestic assets	438	531	615	611	633	660
Net credit to the public sector	20	33	38	39	36	43
Net credit to the financial system	190	232	251	250	285	273
Credit to the private sector	306	359	438	445	445	500
Other	-78	-94	-112	-123	-133	-156
Liabilities to the private sector (residents)	503	605	760	788	801	897
Banking System (Central, Private, and Public Banks)						
Net foreign assets	395	482	603	575	629	718
Net domestic assets	134	148	177	236	197	207
Credit to the public sector	96	104	69	98	140	142
Credit to the rest of financial system	-18	-31	-44	-6	50	51
Credit to the private sector	307	360	440	447	446	501
Other	529	630	780	811	826	925
Broad money (M-3)	529	630	780	811	826	925
	(In percent of total private credit) 3/					
Composition of Credit						
Credit to firms	57.4	59.3	61.3	60.9	57.3	56.7
Credit to households	42.6	40.7	38.7	39.1	42.7	43.3
Consumption	63.1	61.8	61.2	60.3	59.5	58.2
Car loans	1.0	1.3	1.4	1.7	2.1	2.9
Mortgages	35.9	36.9	37.5	38.0	38.4	38.9
	(Percentage change) 3/					
Memorandum Items:						
Base money	12.9	1.4	7.2	9.7	3.6	10.4
M-1	13.1	1.0	5.2	6.6	10.6	6.3
Broader M1 (M1 plus savings deposits)	15.0	3.7	5.6	8.4	15.2	8.8
M-2	13.7	6.4	9.0	14.4	13.4	10.4
M-3	19.2	19.3	23.7	3.9	1.9	11.9
Credit to firms (in US$)	16.2	6.8	2.8	1.5	-4.2	2.4
Credit to households (in real pesos) 4/	9.9	4.7	6.3	-0.5	2.5	1.2

Source: Banco Central del Uruguay.

1/ Peso monetary liabilities include base money and non-liquid liabilities.

2/ The Banco de la Republica Oriental de Uruguay (BROU), Banco Hipotecario de Uruguay (BHU; mortgage institution), private banks, financial houses and cooperatives.

3/ Percent change since one year ago. In pesos, unless indicated otherwise.

4/ Includes credit to households from banks and credit cooperatives.

Table 9. Uruguay: Medium-Term Macroeconomic Framework

	2014	2015	2016	2017	2018	Projections 2019	2020	2021	2022	2023	2024
	(Annual percent change, unless otherwise indicated)										
National Accounts											
Real GDP	3.2	0.4	1.7	2.6	1.6	0.5	2.1	2.5	2.2	2.2	2.2
Total domestic demand	2.3	-2.0	-0.4	0.7	2.4	1.4	7.1	4.0	2.9	0.8	2.4
Final consumption expenditure	2.9	-0.2	0.4	3.9	1.4	2.7	5.9	3.1	4.7	1.6	3.3
Private final consumption expenditure	3.0	-0.5	0.1	4.6	1.5	2.7	5.9	3.2	4.8	1.3	3.4
Public final consumption expenditure	2.5	2.2	2.9	-0.7	0.8	2.4	6.2	2.1	3.6	3.7	2.8
Gross capital formation	0.0	-9.0	-3.9	-13.0	7.3	-5.0	13.3	8.6	-5.4	-3.3	-2.5
Gross fixed capital formation	2.4	-9.2	-1.6	-15.7	-2.7	5.2	13.3	8.6	-5.4	-3.3	-2.5
Private fixed capital formation	-2.8	-8.5	-4.8	-11.9	-4.2	5.5	18.7	10.3	-6.2	-4.3	-2.9
Public fixed capital formation	28.7	-12.2	10.9	-28.9	3.8	4.0	-8.2	0.2	-1.0	2.0	-0.8
Change in inventories (contribution to growth)	-0.6	0.1	-0.5	0.6	1.7	-1.7	0.0	0.0	0.0	0.0	0.0
Net exports (contribution to growth)	0.7	2.6	2.1	1.8	-0.8	-0.9	-5.2	-1.9	-1.0	1.3	-0.4
Consumer Prices											
CPI inflation (average)	8.9	8.7	9.6	6.2	7.6	7.9	8.8	7.9	7.5	6.7	7.0
CPI inflation (end of period)	8.3	9.4	8.1	6.6	8.0	8.8	8.0	7.5	7.0	7.0	7.0
Balance of Payments											
Current account balance (percent of GDP)	-3.2	-0.9	-0.1	0.7	0.1	0.2	-2.7	-3.4	-3.4	-1.7	-1.8
Exports of goods and services (volume)	3.5	-0.6	-0.2	6.9	-4.8	-1.3	-1.9	0.8	4.8	7.4	3.8
Export of goods (volume)	4.2	-10.5	-3.5	1.1	4.1	0.7	3.5	5.4	5.6	6.0	2.5
Imports of goods and services (volume)	-0.5	-6.0	-8.7	-1.2	-0.5	3.4	8.5	9.6	8.4	8.5	6.0
Imports of goods (volume)	-0.5	-6.0	-8.7	-1.2	-0.5	3.4	8.5	9.6	8.4	8.5	6.0
Terms of trade (goods)	101.2	99.4	99.6	99.4	97.0	98.4	102.7	103.3	103.4	103.4	102.8
	(In percent of GDP, unless otherwise indicated)										
Public Sector Finance											
Primary balance NFPS 1/	-0.5	0.1	-0.5	-0.1	0.6	-0.6	-0.5	-0.3	-0.4	-0.5	-0.4
excluding *cincuentones* transactions	-0.5	0.1	-0.5	-0.1	-0.7	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Revenue	29.1	29.0	29.3	29.7	31.3	30.8	30.6	30.4	30.5	30.5	30.6
of which: *cincuentones* transactions	0.0	0.0	0.0	0.0	1.3	1.2	0.9	0.4	0.2	0.0	0.0
Primary expenditure	29.5	28.8	29.9	29.8	30.6	31.1	31.0	30.7	30.9	31.0	31.0
Structural primary balance	-1.3	-0.5	-0.8	-0.8	-1.0	-1.5	-1.2	-0.6	-0.4	-0.5	-0.4
Overall balance NFPS	-2.8	-2.2	-3.1	-2.7	-2.0	-3.0	-3.2	-3.0	-3.2	-3.3	-3.2
excluding *cincuentones* transactions	-2.8	-2.2	-3.1	-2.7	-3.3	-4.2	-4.1	-3.4	-3.4	-3.3	-3.2
Primary balance PS 2/	-0.6	0.0	-0.5	-0.2	0.5	-0.7	-0.6	-0.3	-0.4	-0.6	-0.5
excluding *cincuentones* transactions	-0.6	0.0	-0.5	-0.2	-0.8	-1.9	-1.5	-0.7	-0.6	-0.6	-0.5
Overall balance PS	-3.5	-3.6	-3.8	-3.5	-2.9	-3.5	-3.8	-3.3	-3.5	-3.7	-3.6
excluding *cincuentones* transactions	-3.5	-3.6	-3.8	-3.5	-4.2	-4.7	-4.7	-3.7	-3.7	-3.7	-3.6
Gross NFPS debt	55.5	62.9	61.4	60.7	63.2	66.8	66.7	66.8	67.5	68.5	68.9
NFPS financial assets	10.3	13.2	11.7	11.2	11.1	11.0	10.9	10.8	10.7	10.6	10.5
Net NFPS debt (gross debt minus financial assets)	45.2	49.7	49.7	49.5	52.1	55.8	55.8	56.0	56.8	57.9	58.4
Gross PS debt	61.4	64.6	61.6	65.3	67.7	71.6	73.5	74.4	75.3	76.6	77.4
Financial assets of the PS	38.5	38.8	31.6	33.2	34.0	39.9	40.1	40.5	40.6	40.8	41.0
Liquid financial assets of the PS 3/	31.1	33.3	25.7	28.8	29.0	28.9	29.7	30.5	30.7	31.0	31.3
Net PS debt (gross debt minus liquid financial assets)	30.3	31.3	35.9	36.5	38.8	42.8	43.8	43.9	44.7	45.6	46.1
External Debt											
Gross external debt	72.0	82.1	75.9	69.3	69.3	71.9	75.6	77.1	79.6	81.6	83.8
NFPS gross external debt	31.0	35.1	30.4	28.8	31.6	34.5	35.1	36.3	38.3	40.4	42.7
PS gross external debt	33.7	37.2	31.6	30.1	32.6	36.1	36.8	38.3	40.8	42.9	45.1
Gross international reserves (US$ billions)	17.6	15.6	13.5	15.9	15.5	14.5	15.6	16.8	17.8	18.8	19.8
Saving and Investment											
Gross domestic investment	21.2	19.7	17.8	15.2	16.5	18.0	22.2	23.9	22.8	21.7	21.3
Public sector gross investment	4.9	4.6	4.8	3.9	4.0	4.3	4.3	4.3	4.3	4.3	4.3
Private sector gross investment	16.3	15.1	13.0	11.3	12.6	13.7	17.9	19.6	18.5	17.4	17.0
Gross national saving	18.0	18.8	17.7	15.9	16.7	18.2	19.5	20.5	19.4	20.0	19.6
Public sector gross saving	0.4	0.1	-0.7	-0.6	0.2	-0.6	-0.8	-0.6	-0.8	-0.9	-0.8
Private sector gross saving	17.6	18.7	18.3	16.5	16.5	18.8	20.3	21.2	20.2	20.9	20.4
Unemployment and Output Gap											
Population (Mil)	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.6	3.6
Labor force participation (percent)	64.7	63.8	63.4	62.9	62.5	62.5	62.5	62.5	62.5	62.5	62.5
Employment growth (percent)	2.3	-0.4	-0.2	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3
Unemployment rate (percent)	6.6	7.5	7.9	7.9	8.4	9.2	8.4	7.7	7.5	7.5	7.5
Output gap (percent of potential output)	2.7	0.3	-0.3	0.1	0.0	-1.1	-0.6	-0.1	0.0	0.0	0.0

Sources: Banco Central del Uruguay, Haver Analytics and Fund staff calculations.

1/ The non-financial public sector (NFPS) includes the Central Government, Banco de Prevision Social, Banco de Seguros del Estado, local governments, and Non-Financial Public Enterprises.

2/ Total public sector (PS). Includes the NFPS and Banco Central del Uruguay.

3/ Liquid financial assets are given by deducting from total public sector financial assets the part of central bank reserves held as a counterpart to required reserves on foreign currency deposits.

Annex I. External Sector Assessment

Staff assesses that the external position is broadly consistent with fundamentals according to the External Balance Assessment (EBA) current account model. At the same time, according to both the EBA-Lite real effective exchange rate (REER) model and the EBA external sustainability approach, Uruguay is overvalued. External stability risks remain contained given the large reserve buffers.

1. The current account has weakened from end-2017 until early 2019, reflecting multiple factors. Following the adverse weather events in 2018, lower commodity prices of some commodities affected agricultural exports in late 2018 and 2019. External demand from the region, Argentina and Brazil in particular, has been weak. Tourism receipts from Argentina dropped by 34 percent in the first half of 2019 compared to the same period in 2018. The impact of these factors on the trade balance was limited due to lower imports, reflecting weak domestic demand. The current account has been fluctuating around zero, as the large negative income account (due to increased outflow of investment income) offset the positive trade balance.

2. The current account is expected to deteriorate over the medium term. For 2019–21, the overall trade balance is expected to deteriorate, as export growth slows—reflecting weak external demand, further declines in tourism receipts from Argentina in the coming tourism season in response to new export taxes, a decline in Argentine disposable income, and the appreciation of the Uruguay peso against the Argentine peso—and imports increase, with the economic recovery and the commencement of new infrastructure projects as well as of the new pulp plant construction by UPM.[1] These investments (amounting to over US$5 billion, or over 8 percent of 2018 GDP) are expected to require substantial foreign inputs in capital goods and intermediary materials and scheduled to be executed over the next 3-to-4 years. After the pulp plant is finalized in 2022, exports are expected to increase and imports will moderate, reducing the current account deficit.

3. Staff assesses that the external position is broadly consistent with fundamentals and desirable policy settings. This assessment is based, primarily, on a current account gap of less than 1 percent of GDP, according to the EBA current account model. At the same time, the EBA-Lite REER model, and the EBA External Sustainability approach show that the Uruguayan peso is overvalued.

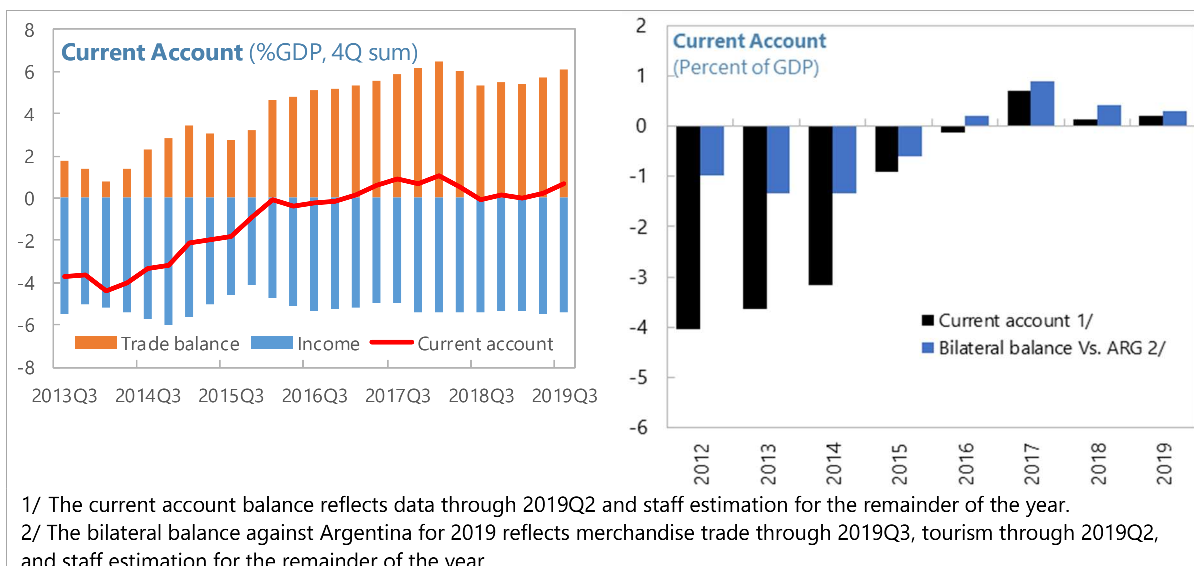
- *EBA current account model*. The external position is broadly in line with fundamentals. This assessment is primarily based on an adjusted current account balance that is at around the model's current account norm. The point estimation of the norm is -2.5 percent of GDP, with a 99 percent confidence interval of around [-3.8, -1.2]. The cyclically adjusted current account

[1] See the Selected Issues Paper on infrastructure investments.

Merchandise Trade Balance
(In percent of GDP)

	2013	2014	2015	2016	2017	2018	Proj. 2019
Trade balance	1.9	3.5	2.5	3.6	4.0	4.1	4.8
Exports	23.1	24.1	20.9	19.7	18.6	19.3	20.9
Imports	21.2	20.6	18.5	16.1	14.6	15.2	16.1
Fuel	3.6	3.0	1.9	1.4	1.6	1.9	1.8
Non-fuel	17.6	17.6	16.5	14.7	13.0	13.3	14.3
Capital	3.4	3.7	3.4	3.0	1.9	1.9	2.1
Consumption	4.9	5.1	5.0	4.7	4.8	4.9	5.3
Intermediary	8.4	8.2	7.4	6.3	6.0	6.1	6.6

Sources: Banco Central del Uruguay; and Fund staff calculations.



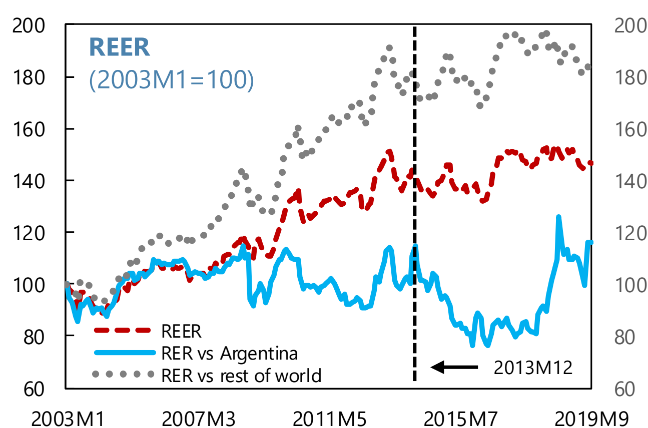
1/ The current account balance reflects data through 2019Q2 and staff estimation for the remainder of the year.
2/ The bilateral balance against Argentina for 2019 reflects merchandise trade through 2019Q3, tourism through 2019Q2, and staff estimation for the remainder of the year.

balance in 2019 is higher by 2.3 percent of GDP than the norm's point estimate. However, the current account is projected to deteriorate to a deficit of over 3 percent for the next couple of years (non-cyclically adjusted), as large investment projects pick up steam and raise imports. Moreover, the adjustment of the trade balance with Argentina is still ongoing and is expected to settle at its historical average (from a projected 0.1 percent of GDP surplus to -1.5 percent of GDP deficit), especially after the reinstatement of Argentina's tourism tax.[2] This reduces the adjusted current account gap to 0.8 percent of GDP. It is also important to note that the data for the current account balance includes import and re-export activities by

[2] Argentina's new tourism import tax imposes a surcharge of 30 percent for expenditures on hotels, airline tickets, and credit cards purchases outside Argentina. A similar tax was first implemented in 2012 and removed after 2015.

merchanting companies, whose domestic value added is currently not reflected in the GDP data (see IMF Country Report No. 18/23). The merchanting companies' activities were introduced in the current account statistics in 2016, which raised the current account balance, but not the GDP. In this context, when merchanting activities are excluded from the current account (consistent with the existing methodology of GDP compilation), the current account balance is around -2.3 percent of GDP, close to the norm.

- EBA-*Lite REER model* shows that the Uruguayan peso is 6.9 percent overvalued.[3] The Uruguay peso has depreciated in real effective terms by 3.6 percent since 2018 but remains elevated. The overall REER movements hides differing underlying trends. While the Uruguay peso has appreciated in real terms against the Argentine peso since 2018 (by 2.1 percent), it depreciated by 3.8 percent in real terms with respect to other countries.



- *The EBA external sustainability (ES) approach* assesses the REER to be overvalued (about 1.5 percent), given that the projected current account deficit for 2024 (1.8 percent of GDP) is below the level required to stabilize the stock of NFA at its current level (a deficit of 1 percent of GDP).

[3] September 2019 data is used.

Exchange Rate Assessment	Deviation from equilibrium (in percent) 1/	CA norm 5/	CA projection 6/	Difference
I. EBA - Current Account model 2/ 4/				
Baseline	-10.6	-2.5	-0.2	2.3
Adjusting for trade with Argentina	-3.7	-2.5	-1.7	0.8
II. External Sustainability (ES) approach 3/ 4/	3.3	-1.0 7/	-1.8 8/	-0.7
III. EBA-lite REER model	6.9			
Memo item:				
EBA - Current Account model 2/ 4/ 9/	-0.9	-2.5	-2.3	0.2

Source: IMF staff calculations.
1/ Positive values indicate overvaluation.
2/ Based on the December 2019 EBA results.
3/ Desk calculations based on the EBA ES approach.
4/ Using a CA elasticity of 0.22 (see RES EBA CA and EBA ES results for Uruguay).
5/ Cyclically-adjusted. Derived by adjusting the current account data for Uruguay prior to 2012 in line with revisions to the data since 2012.
6/ Cyclically adjusted.
7/ CA balance required to stabilize NFA in the medium-term.
8/ 2024 CA balance projection.
9/ Excluding merchanting company activities

4. **These varying results might reflect the following factors:** i) the asymmetric treatment of merchanting activities in the GDP and current account statistics, ii) quantities (trade balance) adjusting slower than prices (in response to recent REER changes) and recent export tax changes in neighboring Argentina, iii) the impact of lower FDI in recent years, which reduces imports in the short run, and export capacity in the long run; iv) ongoing structural changes, affecting potential GDP; and iv) the pressures on the exchange rate stemming from regional shocks and capital flows and diverging trends with respect to various trading partners.

5. **External stability risks for Uruguay remain contained.** Although gross reserves have dropped in 2019, they remain above the upper bound of the IMF reserve adequacy metric range, and other prudential indicators. This is considered appropriate given the high degree of financial dollarization of the economy and commercial banks' foreign currency requirements. Net reserves appear more than adequate to offset possible disorderly conditions in the foreign exchange market, if needed. Given the level of reserves, external stability risks are contained.

Gross International Reserves	
In billions of U.S. dollars (projection for end 2019)	14.5
In months of imports (2019)	13.0
In percent of:	
GDP (2019) 1/	25.2
Short-term external (STE) debt (2019)	490.5
STE debt and foreign currency deposits (2019)	63.8
STE debt and nonresident deposits (2019)	288.3
M2 (latest)	148.0
M3 (latest)	50.7
Memo items:	
IMF's new reserve adequacy metric range in US$, billions (2018) 2/	8.1 to 12.1
Banks' gross foreign assets (US$, billions, 2019Q2)	10.8
Ratio of gross reserves plus banks' foreign assets to STE debt and foreign currency deposits (percent)	111.4

Sources: Banco Central del Uruguay and Fund staff calculations.
1/ Reserves-to-GDP ratio calculated after converting GDP to U.S. dollars.
2/ Reserve adequacy metric range is the minimum reserve adequacy to 1.5 times the minimum.

Annex II. Public Sector Debt Sustainability Analysis (DSA)

In 2019, the authorities and the Fund switched the focus of fiscal reporting from the consolidated public sector (CPS) to the non-financial public sector (NFPS), which excludes the central bank.[1] Under the baseline scenario, the NFPS debt ratio is projected to gradually increase to around 68.9 percent of GDP, but its long average maturity (14 years) and substantial liquid assets (11 percent of GDP at end-2018) mitigate short-term risks.

1. At end-2018 gross debt was 63 percent of GDP, which includes:

- *Central government's debt:* 51 percent of GDP, with 14-year average maturity, and about one half denominated in local currency and ⅓ indexed to CPI.
- *Debt from other public corporations*: 3 percent of GDP (includes public enterprises and local governments).
- *Central bank capitalization bonds:* 9 percent of GDP.[2]

2. The NFPS holds assets amounting to 11 percent of GDP and access to contingent credit lines from multilateral institutions of about 4 percent of GDP.

- *Financial assets of the central government:* 5 percent of GDP, mostly held in liquid instruments (e.g., securities and deposits), in line with the government's prefunding policy of holding enough liquid assets to cover at least 12 months of debt service.
- *Holdings of BCU bonds and deposits at the BCU*: About 6 percent of GDP.[3]

3. Net debt was 52 percent of GDP in 2018.

Scenarios

4. The gross debt ratio is expected to gradually increase over the projection period. The negative impact of the depreciation of the peso and fiscal deficits is partly offset by the debt-reducing impact of the *cincuentones* transaction, and going forward, by the expected recovery in economic growth and low real interest rates. If real GDP growth, real interest rates, and other debt-

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[1] For the rest of this annex, numbers are quoted for the NFPS coverage.

[2] The first capitalization bond was issued in 2008 and further issuances were made in 2010, 2011, 2012 and 2013. At end 2018, all debt was consolidated into a single 30-year inflation-linked bond. This debt is not market based, its transactions do not involve cash and does not pay amortizations. In the previously used public sector coverage, this debt was netted out from the consolidated debt numbers as it is an asset of the central bank and a liability of the central government.

[3] In the previously used public sector coverage, these assets were netted out from consolidated assets as they are assets of the NFPS and liabilities of the central government.

creating flows remain at their projected level for 2024, the debt-stabilizing primary balance is estimated at 0.9 percent of GDP.

5. Baseline assumptions seem plausible, as staff's forecasts are not systematically biased (based on historical projection errors). Furthermore, fan charts show limited uncertainty around the baseline (the symmetric fan chart has a width of about 12 percent of GDP).

6. A historical scenario yields a downward-sloping debt ratio, since it assumes key macroeconomic variables will behave as in the previous decade where Uruguay experienced high growth and exchange rate appreciation as it recovered from the 2002 financial crisis and benefited from a positive terms-of-trade shock.

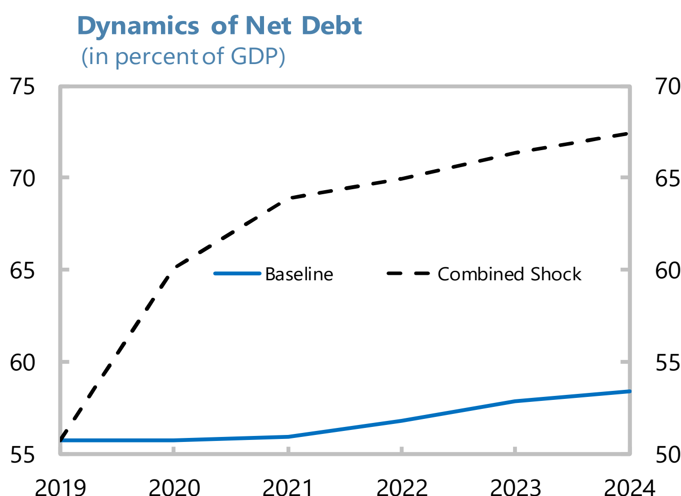
Risks

7. The share of debt held by non-residents is above its risk benchmark, but refinancing risks are limited given the sizable liquid financial assets and contingent credit lines of the central government (5 and 4 percent of GDP, respectively). Short-term debt is negligible (0.4 percent of GDP), reflecting the authorities' long-standing emphasis on extending maturities and minimizing roll-over risk.

Stress Tests

8. Debt dynamics are moderately sensitive to shocks. In a stylized downside scenario—which combines a permanent 20 percent exchange rate depreciation (relative to the baseline) with a temporary drop in growth and primary balances and a permanent increase in real interest rates—net debt would only increase about 17 percentage points as the valuation effects on foreign-currency assets partially offset the impact on debt. Fan charts of the projected debt distribution confirm that debt dynamics are generally manageable under statistical distributions of combined shocks, although they have deteriorated from last year. Gross debt would remain below 70 percent of GDP in 50 percent of cases.

Dynamics of Net Debt
(in percent of GDP)



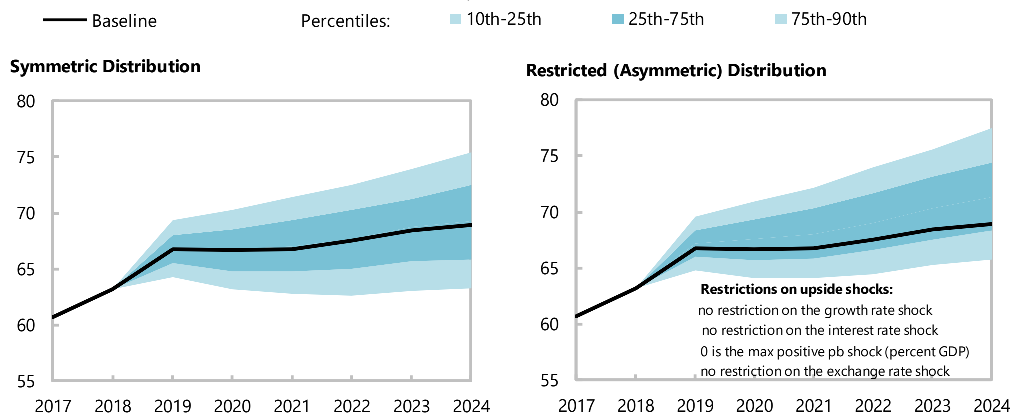
Source: Fund staff calculations.
Note: Combined shock as described in the text.

Figure 1. Uruguay: NFPS DSA Risk Assessment
(Nonfinancial Public Sector Debt)

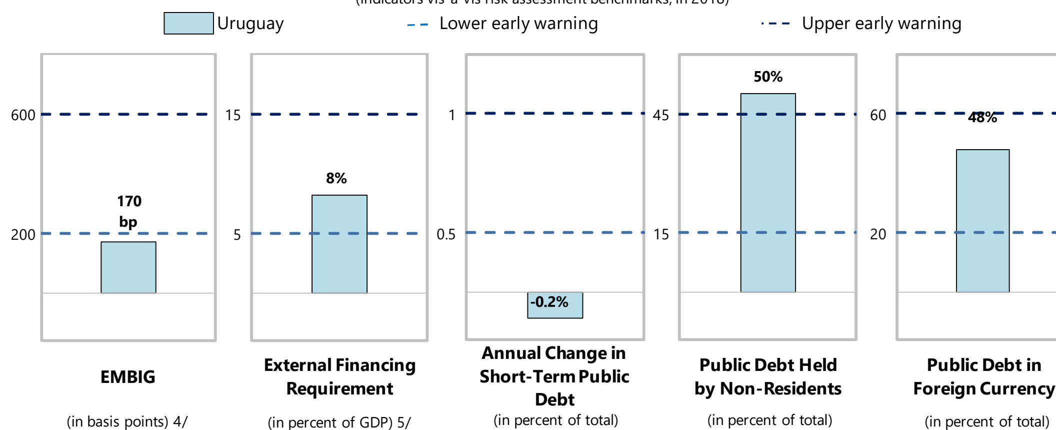
Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

Evolution of Predictive Densities of Gross Debt NFPS
(in percent of GDP)



Debt Profile Vulnerabilities
(Indicators vis-à-vis risk assessment benchmarks, in 2018)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white. Lower and upper risk-assessment benchmarks are:

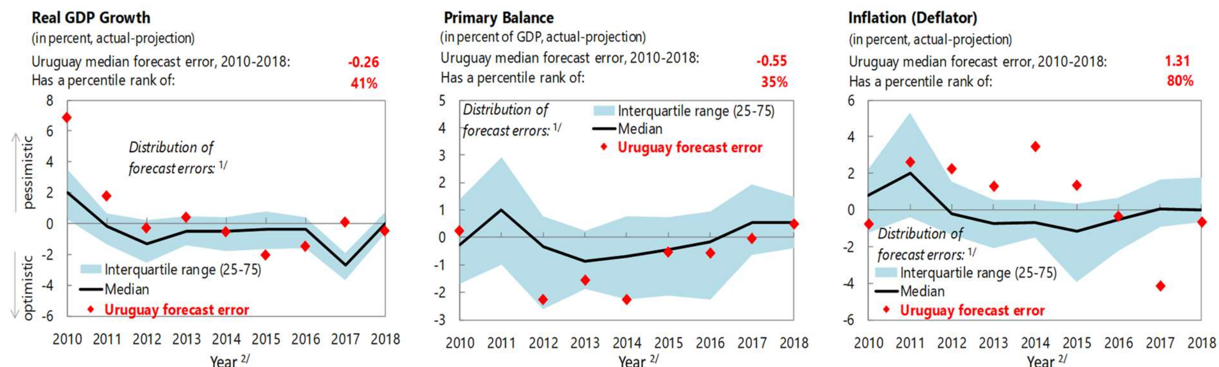
200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ EMBIG, an average over the last 3 months, 14-Sep-19 through 13-Dec-19.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

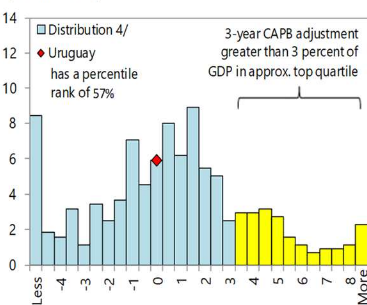
Figure 2. Uruguay: NFPS DSA—Realism of Baseline Assumptions

Forecast Track Record, versus surveillance countries

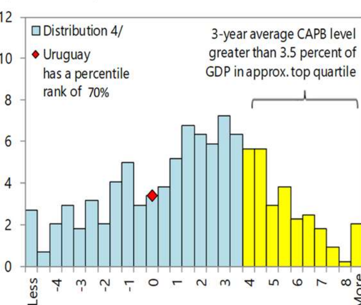


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)

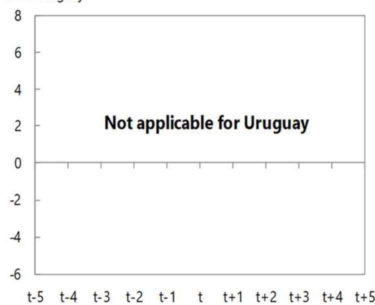


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis 3/

Real GDP growth
(in percent)
Uruguay



Source : IMF Staff.

1/ Plotted distribution includes surveillance countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Uruguay, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 3. Uruguay: NFPS DSA—Baseline Scenario

(in percent of GDP unless otherwise indicated)

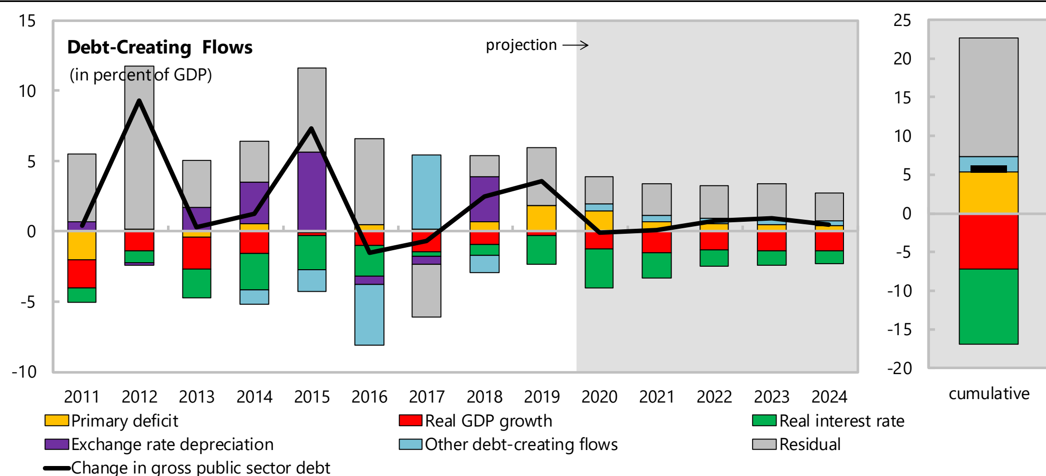
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2008-2016 [2/]	2017	2018	2019	2020	2021	2022	2023	2024
Nominal gross public debt	53.1	60.7	63.2	66.8	66.7	66.8	67.5	68.5	68.9
Public gross financing needs	4.7	6.0	6.4	8.3	7.7	8.8	9.3	7.9	9.2
Real GDP growth (in percent)	4.2	2.6	1.6	0.5	2.1	2.5	2.2	2.2	2.2
Inflation (GDP deflator, in percent)	8.0	4.7	5.5	8.8	9.5	8.0	7.0	6.9	6.6
Nominal GDP growth (in percent)	12.5	7.4	7.2	9.3	11.8	10.6	9.4	9.3	8.9
Effective interest rate (in percent) [4/]	5.3	4.3	4.2	5.2	5.1	5.2	5.3	5.3	5.3

As of December 13, 2019		
Sovereign Spreads		
EMBIG (bp) 3/		161
5Y CDS (bp)		74
Ratings	Foreign	Local
Moody's	Baa2	Baa2
S&Ps	BBB	BBB
Fitch	BBB-	BBB-

Contribution to Changes in Public Debt

	Actual			Projections							
	2008-2016	2017	2018	2019	2020	2021	2022	2023	2024	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	0.4	-0.7	2.4	3.6	-0.1	0.1	0.8	0.9	0.5	5.8	
Identified debt-creating flows	-4.4	3.1	1.0	-0.5	-2.1	-2.2	-1.6	-1.6	-1.6	-9.5	
Primary deficit	-0.7	0.1	0.7	3.0	2.3	1.1	0.8	0.5	0.4	8.0	0.9
Primary (noninterest) revenue and grants	28.5	29.7	30.0	29.6	29.7	30.0	30.3	30.5	30.6	180.7	
Primary (noninterest) expenditure	27.8	29.9	30.7	31.4	31.1	30.7	30.9	31.0	31.0	186.1	
Automatic debt dynamics [5/]	-3.0	-2.3	1.5	-2.4	-4.0	-3.3	-2.5	-2.4	-2.3	-16.9	
Interest rate/growth differential [6/]	-3.4	-1.8	-1.7	-2.4	-4.0	-3.3	-2.5	-2.4	-2.3	-16.9	
Of which: real interest rate	-1.5	-0.3	-0.8	-2.1	-2.8	-1.8	-1.2	-1.1	-0.9	-9.7	
Of which: real GDP growth	-1.9	-1.5	-0.9	-0.3	-1.3	-1.5	-1.3	-1.4	-1.4	-7.1	
Exchange rate depreciation [7/]	0.4	-0.5	3.2	...	...	...	...	...	...	...	
Other identified debt-creating flows	-0.8	5.3	-1.2	0.0	0.5	0.4	0.4	0.3	0.3	2.0	
Net privatization proceeds (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other debt flows (incl. asset purchases)	-0.8	5.3	-1.2	0.0	0.5	0.4	0.4	0.3	0.3	2.0	
Residual, including asset changes [8/]	4.9	-3.8	1.5	4.1	1.9	2.3	2.3	2.5	2.0	15.3	



Source: IMF staff.

1/ Public sector is defined as non-financial public sector.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

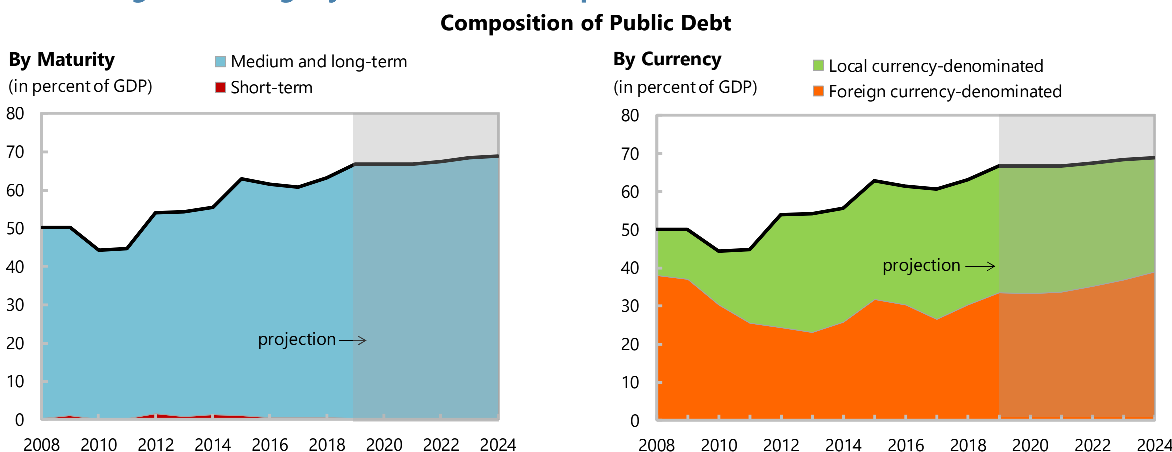
7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

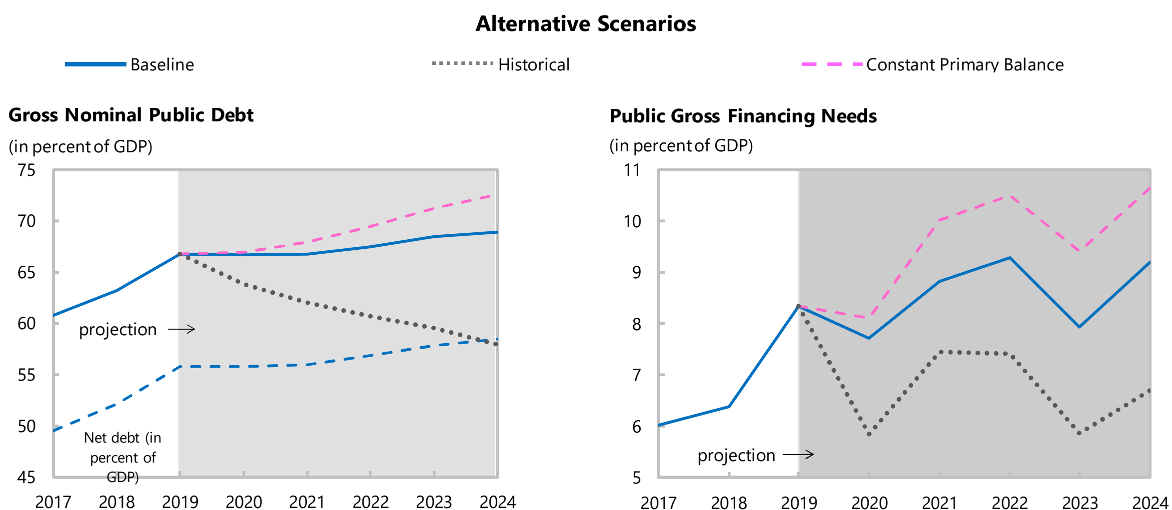
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 4. Uruguay: NFPS DSA—Composition of Debt and Alternative Scenarios

Composition of Public Debt



Alternative Scenarios



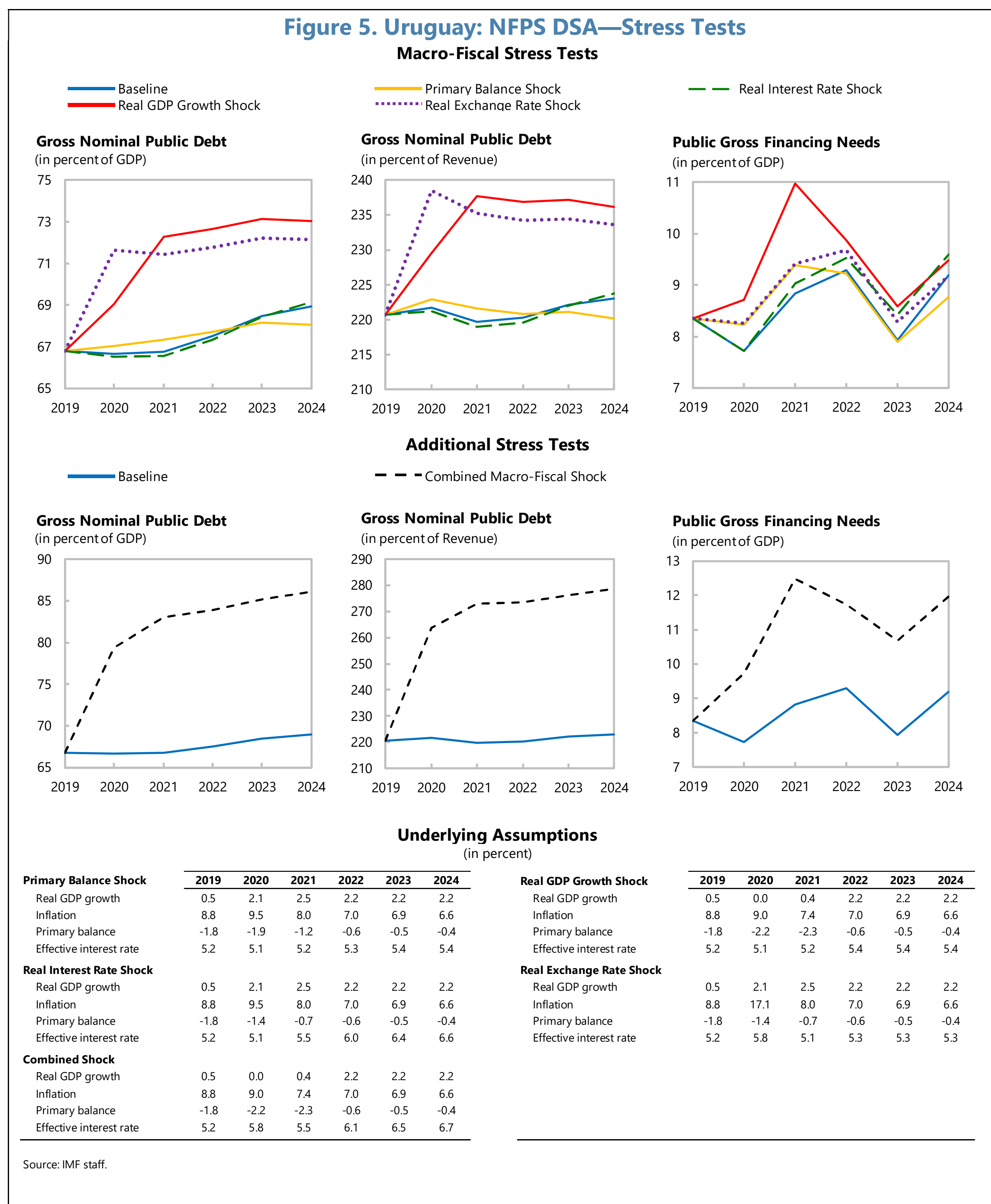
Underlying Assumptions
(in percent)

Baseline Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	0.5	2.1	2.5	2.2	2.2	2.2
Inflation	8.8	9.5	8.0	7.0	6.9	6.6
Primary Balance	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.1	5.2	5.3	5.3	5.3
Constant Primary Balance Scenario						
Real GDP growth	0.5	2.1	2.5	2.2	2.2	2.2
Inflation	8.8	9.5	8.0	7.0	6.9	6.6
Primary Balance	-1.8	-1.8	-1.8	-1.8	-1.8	-1.8
Effective interest rate	5.2	5.1	5.2	5.3	5.4	5.4

Historical Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	0.5	3.5	3.5	3.5	3.5	3.5
Inflation	8.8	9.5	8.0	7.0	6.9	6.6
Primary Balance	-1.8	0.4	0.4	0.4	0.4	0.4
Effective interest rate	5.2	5.1	5.2	5.3	5.3	5.3

Source: IMF staff.

Figure 5. Uruguay: NFPS DSA—Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	0.5	2.1	2.5	2.2	2.2	2.2
Inflation	8.8	9.5	8.0	7.0	6.9	6.6
Primary balance	-1.8	-1.9	-1.2	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.1	5.2	5.3	5.4	5.4
Real Interest Rate Shock						
Real GDP growth	0.5	2.1	2.5	2.2	2.2	2.2
Inflation	8.8	9.5	8.0	7.0	6.9	6.6
Primary balance	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.1	5.5	6.0	6.4	6.6
Combined Shock						
Real GDP growth	0.5	0.0	0.4	2.2	2.2	2.2
Inflation	8.8	9.0	7.4	7.0	6.9	6.6
Primary balance	-1.8	-2.2	-2.3	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.8	5.5	6.1	6.5	6.7

Real GDP Growth Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	0.5	0.0	0.4	2.2	2.2	2.2
Inflation	8.8	9.0	7.4	7.0	6.9	6.6
Primary balance	-1.8	-2.2	-2.3	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.1	5.2	5.4	5.4	5.4
Real Exchange Rate Shock						
Real GDP growth	0.5	2.1	2.5	2.2	2.2	2.2
Inflation	8.8	17.1	8.0	7.0	6.9	6.6
Primary balance	-1.8	-1.4	-0.7	-0.6	-0.5	-0.4
Effective interest rate	5.2	5.8	5.1	5.3	5.3	5.3

Source: IMF staff.

Annex III. External Debt Sustainability Analysis

1. External debt in Uruguay peaked in 2015 at 82 percent of GDP but fell to around 69 percent of GDP in 2017–18 (see Table). The improvement in the current account relative to earlier years has contributed to this downward movement. About 45 percent of the external debt is owed by the public sector.

2. Gross external debt is estimated to increase to around 72 percent of GDP in 2019, and projected to continue rising afterwards, where favorable automatic debt dynamics are offset by the projected current account deficits and the financing of PPP projects.

3. Gross external financing requirements are expected to increase over the medium term with higher non-interest current account deficit and amortization of longer-term debt. Non-debt creating capital inflows are expected to alleviate the increase in the long-term ratio of external debt to GDP to some extent.

4. Stress tests indicate that the standard growth and interest rate shocks would have a minimal impact on external debt. Shocks to the non-interest current account and a combined shock (to the real interest rate, growth and current account) would have a greater, but still moderate, impact.

5. The main risk to Uruguay's external debt sustainability is an exchange rate depreciation. A counterfactual 30 percent exchange rate depreciation would increase the external debt-to-GDP ratio by over 40 percentage points, other things being equal (see Figure). Nonetheless, given Uruguay's sizable gross international reserves and liquidity buffers, risks to external debt sustainability remain contained.

Table 1. Uruguay: External Debt Sustainability Framework, 2014–2024

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2014	2015	2016	2017	2018			2019	2020	2021	2022	2023	2024	Debt-stabilizing non-interest current account 7/
Baseline: External debt 1/	72.0	82.1	75.9	69.3	69.3			**72.0**	**75.7**	**77.3**	**79.8**	**81.9**	**84.0**	**-2.2**
Change in external debt	5.8	10.2	-6.2	-6.6	0.0			2.7	3.7	1.6	2.5	2.1	2.2	
Identified external debt-creating flows	-0.8	1.7	0.7	3.5	-9.3			1.2	-1.1	-0.4	-1.1	-3.0	-3.0	
Current account deficit, excluding interest payments	1.2	-1.4	-2.1	-2.7	-2.5			-2.4	0.4	1.1	1.0	-0.8	-0.8	
Deficit in balance of goods and services	-2.8	-3.2	-5.2	-6.1	-5.5			5.6	2.9	2.1	2.4	4.5	4.8	
Exports	32.1	29.3	27.6	27.0	27.4			28.8	29.4	28.9	29.7	31.3	32.1	
Imports	-29.3	-26.1	-22.4	-20.9	-21.9			-23.3	-26.5	-26.7	-27.3	-26.8	-27.3	
Net non-debt creating capital inflows (negative)	4.4	1.5	-1.4	-3.7	-1.9			-1.7	-0.5	-0.5	-1.1	-1.4	-1.5	
Automatic debt dynamics 2/	-6.4	1.5	4.2	10.0	-4.9			5.4	-1.0	-0.9	-1.0	-0.8	-0.8	
Contribution from nominal interest rate	1.6	2.1	2.3	2.5	2.1			2.2	2.2	2.3	2.3	2.4	2.5	
Contribution from real GDP growth	-1.9	-0.3	-1.4	-2.2	-1.0			-0.4	-1.4	-1.8	-1.6	-1.7	-1.7	
Contribution from price and exchange rate changes 3/	-6.1	-0.3	3.3	9.6	-6.1			3.5	-1.8	-1.4	-1.7	-1.5	-1.5	
Residual, incl. change in gross foreign assets 4/	6.5	8.5	-6.9	-10.1	9.3			1.0	5.8	2.6	3.7	5.3	5.2	
External debt-to-exports ratio (in percent)	224.1	279.9	275.3	256.7	252.7			249.6	257.5	267.7	268.9	261.6	261.6	
Gross external financing need (in billions of US dollars) 5/	12.7	13.4	11.6	9.3	8.8			8.1	10.4	11.5	12.1	11.6	12.1	
in percent of GDP	22.2	25.1	22.1	15.7	14.6			14.1	17.8	18.7	18.9	17.3	17.4	
Scenario with key variables at their historical averages 6/						7-Year Historical Average	7-Year Standard Deviation	**72.0**	**77.9**	**80.8**	**84.7**	**90.4**	**95.9**	**0.8**
Key Macroeconomic Assumptions Underlying Baseline														For debt stabilization
Real GDP growth (in percent)	3.2	0.4	1.7	2.6	1.6	2.5	1.4	0.5	2.1	2.5	2.2	2.2	2.2	
GDP deflator in US dollars (change in percent)	10.1	0.5	-3.8	-11.3	9.6	0.8	8.3	-4.9	2.5	1.9	2.2	1.9	1.9	
Nominal external interest rate (in percent)	2.8	3.0	2.7	3.0	3.4	3.0	0.2	3.1	3.2	3.2	3.2	3.2	3.2	
Growth of exports (US dollar terms, in percent)	1.6	-15.0	-7.0	10.6	2.0	-1.6	9.8	1.0	3.7	3.3	7.3	10.2	6.9	
Growth of imports (US dollar terms, in percent)	-3.0	-17.0	-15.2	5.3	5.5	-4.9	10.8	1.9	15.9	6.0	6.6	2.6	6.2	
Current account balance, excluding interest payments	-1.2	1.4	2.1	2.7	2.5	0.7	1.9	2.4	-0.4	-1.1	-1.0	0.8	0.8	
Net non-debt creating capital inflows	-4.4	-1.5	1.4	3.7	1.9	-1.1	3.5	1.7	0.5	0.5	1.1	1.4	1.5	

1/ External debt includes non-resident deposits.

2/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

3/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

4/ For projection, line includes the impact of price and exchange rate changes.

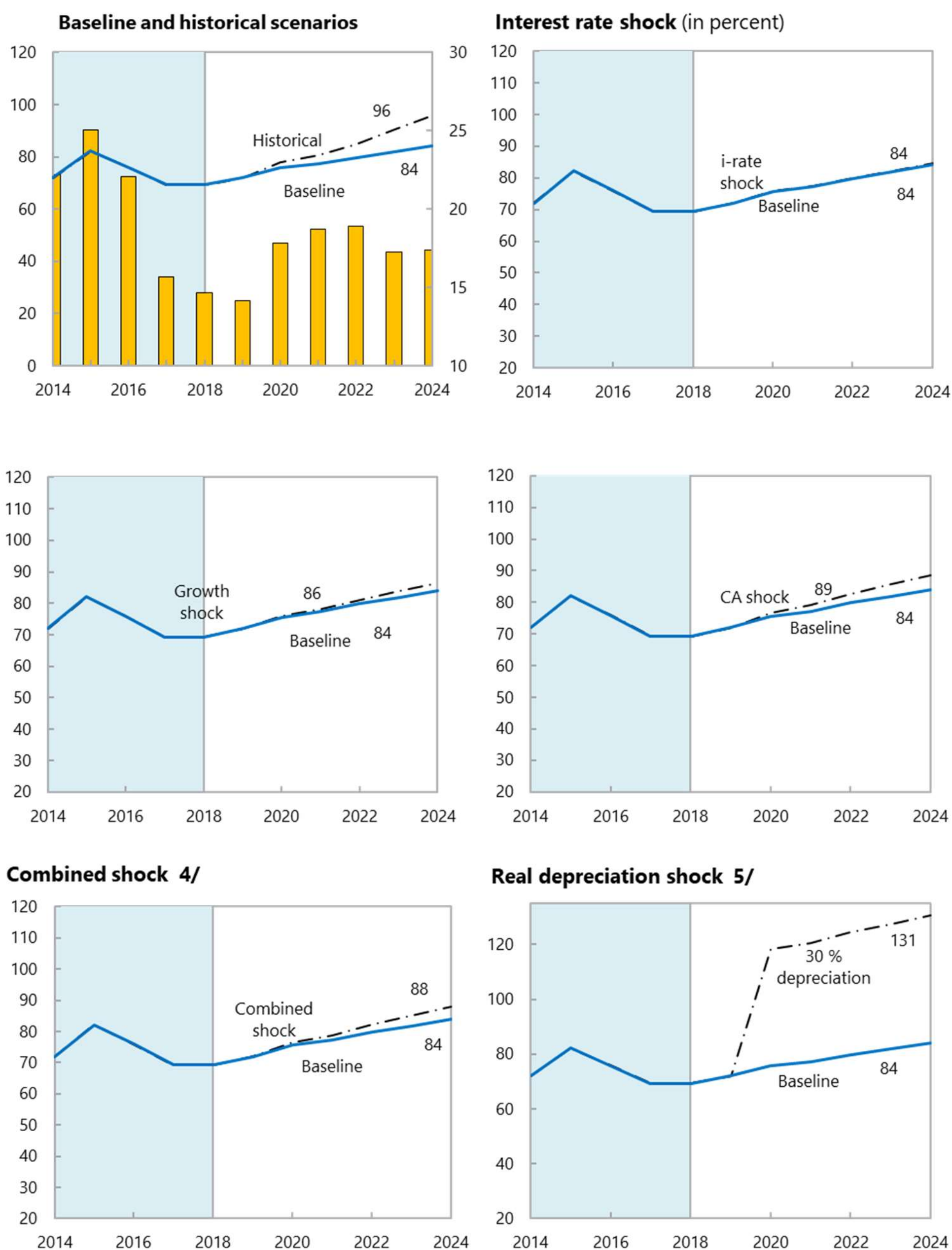
5/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

6/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

7/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 1. Uruguay: External Debt Sustainability: Bound Tests 1/ 2/ 3/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Six-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the six-year period, and the information is used to project debt dynamics five years ahead.
3/ External debt includes non-resident deposits.
4/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
5/ One-time real depreciation of 30 percent occurs in 2019.

Annex IV. Medium-Term Fiscal Framework

1. **Uruguay has significantly improved its MTFF with some features aligned with best practices.**[1] The Ministry of Economy and Finance (MEF) produces a top-quality annual budget execution report which provides accurate representations of recent developments, explains policy priorities and policy changes, and presents projections (but only for the remaining part of the government's term).[2] Budget documentation is easily available (online) and the MEF also provides detailed, timely and transparent monthly updates on the state of fiscal accounts. Parliament approves the previous year's budget execution report based on audited reports by the Court of Accounts (which is independent of the executive and reports to parliament, all documents are also publicly available). In addition, the MEF staff has adequate technical capacities, particularly in the Budget, Macro and Debt Management units.

2. **Uruguay's framework has important elements of risk management.** The MEF maintains contingent credit lines with multilateral institutions of about 4 percent of GDP and a prefunding policy of holding sufficient liquid assets to cover at least 12 months of debt service (currently about 5 percent of GDP). Law 18.786 caps the net present value of PPP liabilities (actual and contingent) and annual commitments (with private stakeholders) at 7 and 0.5 percent of (the previous year) GDP, respectively.

3. **The budget has some safeguards to prevent election-related spending.** 12 months prior to elections (every five years in October), the Executive cannot alter the budget, as it is considered the next government's prerogative, and to avoid politically motivated increases in spending. In addition, during those months, Parliament cannot approve Social Security norms, nor create civil servants' positions. Finally, during the 12 months before the new government steps in (in February), civil servants cannot be hired (except in education and defense).

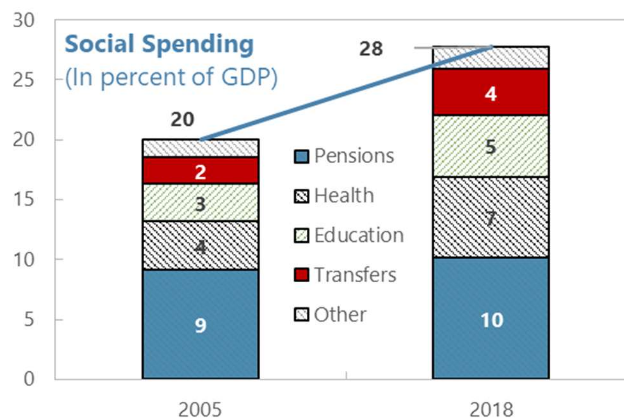
4. **Nevertheless, the current framework has important shortcomings.** While the budget is for five years, in practice, Uruguay does not yet reap the full advantages of having a multi-year budget to improve planning, prioritize expenditures, ensure debt sustainability, and deliver countercyclicality.

a. *The budget horizon* is fixed and loses its medium-term aspect with the progression of the government's tenure. Thus, as the administration approaches the end of its term, the

[1] See more details in OECD (2019), "Towards modern budgeting practices in Uruguay."

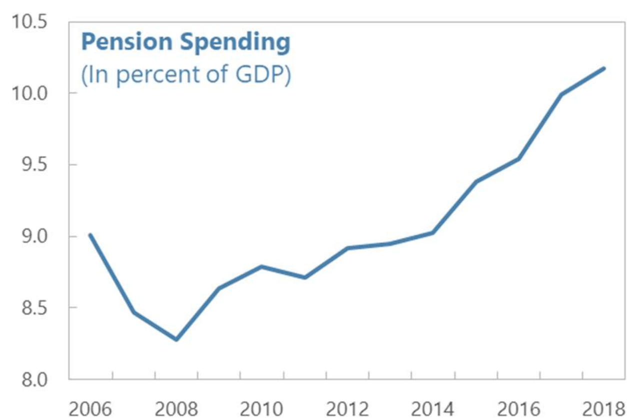
[2] A five-year budget is presented to parliament by each new government on the first six months of its period (presented by end August after being sworn in at the beginning of March). In the meantime, the incoming government continues to execute the budget from the previous administration. Thereafter, an annual budget execution report (Rendición de Cuentas) is presented to parliament each June.

budget's projections and targets may no longer provide credible limits, particularly after large shocks.



b. *Spending rigidities* make achieving targets and adjusting to cyclical conditions difficult. First, the budget creates allocations which are considered as spending entitlements. Although the annual execution reports could in principle introduce policy changes (as was done in some earlier years), it is difficult to reduce a budget allocation in case of need (e.g., during downturns). Second, discretionary government spending is only about 20 of the total spending. Since most spending is endogenous and considered as social, any discussion on rationalization is inherently difficult.[3] In particular:

- Pension spending has rapidly expanded (over the past decade) and currently accounts for about 1/3 of spending, reflecting an aging society, the welcome almost universal coverage, and the constitutionally mandated wage indexation—Article 67 of the constitution establishes that pensions need to be adjusted by the average increase in wages.[4] This implies that retirees benefit from productivity improvements of existing workers.



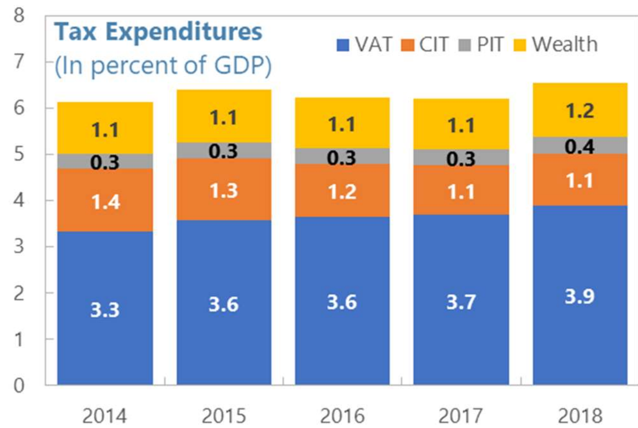
Sources: MoF and MIDES.

[3] The authorities define endogenous spending as the one mandated by laws or determined by policy choices from previous administrations and thus cannot be controlled.

[4] Pension spending not only includes the social security but also the police and military special regimes. The special regimes for independent professionals, notaries and bank workers, are not included in the fiscal accounts.

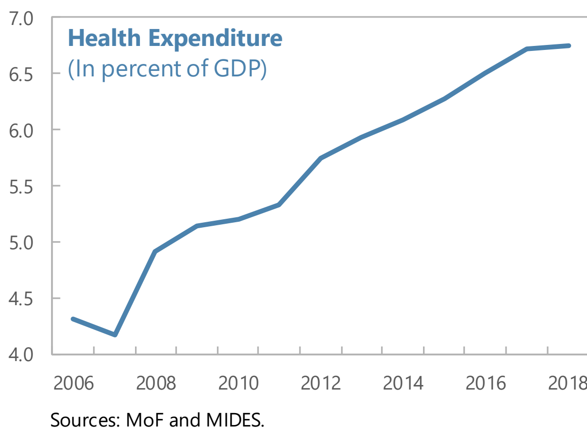
- Wages represent about 15 percent of expenditures.[5] About 12 percent of civil servants cannot be dismissed (as stated in Article 60 of the constitution, which excludes teachers, health professionals, military and police). The previous budget law (for the period 2010-2014) stated that nominal adjustments should at least be linked to past inflation. Over the past decade, on average, public employment and real public wages increased by about 2 and 2.5 percent per year, respectively.

c. Tax expenditures are estimated by the tax administration directorate (DGI) to be about 7 percent of GDP, including exemptions, reduced rates and tax credits. Estimates are publicly available and updated (on average) every three years. About ¾ of these expenditures are for the VAT and CIT, with tax expenditures representing about 40 percent of collections for each of those taxes. Tax expenditures for VAT have increased by about 0.6 percent of GDP in the past four years, with others remaining broadly constant.

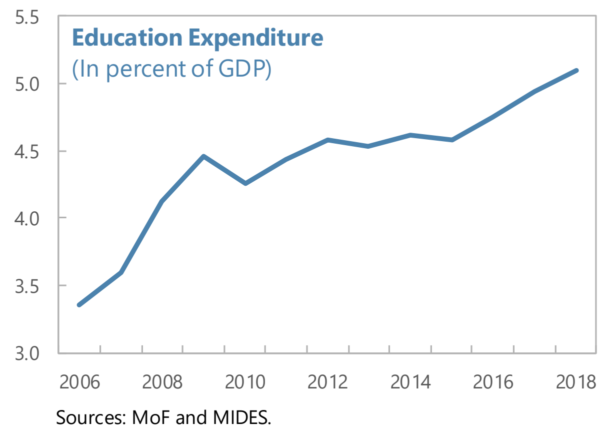


Source: DGI.

d. *Budget fragmentation:* Article 220 of the constitution allows some autonomous entities greater flexibility on the management of their budget and to present independent budget proposals to the legislative (if no agreement is reached with the MEF). Article 220



Sources: MoF and MIDES.

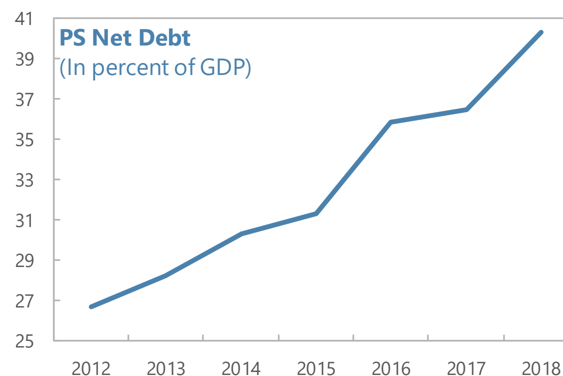


Sources: MoF and MIDES.

[5] About 1/5 of workers are employed by the government (roughly equally split between health, education and public administration).

institutions currently account for about 1/3 of spending including those in charge of health and education, which have significantly expanded in the recent years.[6]

e. *Limited de-facto accountability:* While the budget execution is discussed in parliament every year, there are no clear consequences for missed targets. Under the current design, objectives serve more as "aspirations" than targets. Although Law 17.947 of 2006 limits the annual increase in the net debt of the consolidated public sector (the limit varies each year and is set on inflation indexed units since 2008), often escape clauses have been applied to allow the targets to be achieved, and the rule has not precluded the increase in net debt. The law and its exceptions are complicated, making its monitoring difficult. In fact, the public must wait for the execution report to learn whether the government has "complied with the law".



Source: MoF and staff estimates.

f. *No direct link of performance evaluations to the budget:* While design, implementation and performance evaluations are done by the Office of Planning and Programing (OPP), these are not used in the budget to discuss allocations. In addition, there is insufficient use of spending reviews of social programs as an ongoing feature of the budget process.

g. *Risk disclosure:* budget documents do not analyze risks surrounding projections and contingent liabilities.

h. *Coverage:* Budgets set the fiscal targets for the consolidated public sector (inclusive of the central bank). This extensive coverage, although good for transparency, mixes fiscal and monetary policy objectives (the central bank's deficit is mostly affected by sterilization costs from FX intervention policy, which is intended to prevent disorderly market conditions and is outside the control of the fiscal authority). Taking into account of these considerations, in 2019, the authorities switched the focus of fiscal reporting from the consolidated public sector (CPS) to the non-financial public sector (NFPS).

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[6] All OECD countries have autonomous institutions for the Judiciary, Administrative, Electoral or Audit courts, but their scope is significantly broader in Uruguay. The largest Art. 220 entities are the Public Education National Administration (ANEP), the University of the Republic (UdelaR) and the State Health Services Administration (ASSE). The list of Art. 220 entities has expanded over the past decade (Uruguayan Technological University in 2012, Institute of Meteorology in 2013, Attorney General's Office in 2015, Institute for Youth Social Inclusion in 2015, and the Public Transparency and Ethical Board in 2015).

i. *Spending efficiency:* Health and education outcomes are in line with the rest of the region but below advanced country standards, suggesting room for efficiency gains. For example, although the number of teachers (per 100 students) in both primary and secondary education are close to the OECD average, PISA scores and enrollment in secondary education are worse. Similarly, although the number of doctors and coverage (lower out-of-pocket costs) are better than the OECD average, life expectancy and infant deaths are worse. This suggests there might be room to make savings by improving the efficiency of public spending in health and education, without damaging the quality or access to these services.

	Education (% GDP)	Pisa Score	Enroll Prim (percent)	Enroll Sec (percent)	Teachers Prim (per 100 stud.)	Teachers Sec (per 100 stud.)	Health (% GDP)	Out-of Pocket (percent)	Infant Deaths (per 1,000 people)	Hospital Beds (per 1,000 people)	Nurses (per 1,000 people)	Doctors (per 1,000 people)	Life Exp. (years)
Argentina	5.5	422	99.2	90.8	5.8	8.2	2.7	15.8	8.8	5.0	4.2	3.9	76.9
Brazil	6.2	395	96.3	81.7	4.9	6.0	3.8	43.6	12.8	2.2	7.4	1.9	75.1
Chile	5.4	443	94.7	88.7	5.6	5.4	7.8	34.8	6.1	2.2	0.1	1.0	79.5
Colombia	4.5	410	92.9	77.5	4.2	3.8	5.2	20.2	12.2	1.5	1.1	1.8	75.1
Ecuador	5.0		91.6	85.3	4.1	4.8	4.4	40.5	12.2	1.5	2.1	1.7	76.5
Mexico	4.9	416	95.3	81.2	3.8	5.9	3.1	40.4	10.9	1.5	2.6	2.2	76.6
Peru	3.9	394	95.7	89.3	5.8	7.0	3.4	28.3	11.1	1.6	1.5	1.1	75.9
Uruguay	4.9	430	99.6	88.2	9.1	7.9	7.7	17.4	6.4	2.8	5.8	3.9	77.1
average	5.0	416	95.7	85.3	5.4	6.1	4.8	30.1	10.1	2.3	3.1	2.2	76.6
LAC	4.7	405	91.9	76.3	5.3	6.2	3.9	34.2	15.4	2.2	2.3	1.4	74.3
EMs	4.5	420	90.7	77.2	5.1	6.9	4.0	32.5	15.6	3.1	3.7	1.7	73.3
OECD	5.3	492	95.9	92.8	7.4	8.5	7.2	19.6	3.5	4.7	9.3	3.3	81.0

Source: World Development Indicators - WB.

5. The newly elected government has a window of opportunity to introduce some elements of MTFF to reinforce fiscal discipline and countercyclicality and better allocate resources towards strategic priorities. 2020 will be the first year of the upcoming government and is thus an opportune time to adapt some features of a well-functioning MTFF to the forthcoming five-year budget. While there is no one-size-fits-all model, a new framework could incorporate some aspects of the below considerations:

6. Rolling forecast periods: To ensure continuity and reduce uncertainty towards the end of the presidential term, budget updates could provide forecasts with rolling windows. This would mean keeping a fixed 3-to-5-year projection period consistently, including at the end of the government's term. This would help reduce uncertainty towards end of the government's term and increase the credibility of fiscal policy in case of negative shocks by demonstrating the adjustment path, thereby increasing the fiscal space.

7. Binding fiscal rules: There is a need to introduce a new fiscal rule to ensure fiscal discipline and support countercyclicality. Country experiences show that successful rules generally have broad institutional coverage, are tightly linked to fiscal sustainability objectives, are easy to understand and monitor, and support countercyclical fiscal policy (IMF SDN 18/04). To be effective, fiscal rules should have three main properties—simplicity, flexibility, and enforceability. These three properties are sometimes difficult to achieve simultaneously.

a. **In case of Uruguay, an expenditure rule combined with a debt anchor could deliver these objectives.** A debt rule provides a direct link to sustainability and is easy to

monitor and communicate. But by itself, it does not provide short-run operational guidance; does not have an economic stabilization feature; and could be met by undesirable temporary measures or affected by factors outside of the government's control. An expenditure rule could be the ideal complement, as it would provide the needed operational guidance and allow for economic stabilization. Such combined rule would trigger the required fiscal adjustment while introducing some countercyclicality by constraining spending during booms but without requiring adjustments to counteract cyclical reductions in revenues. The constraint could be placed on total public spending, to provide a more transparent signal of the available fiscal space and avoid the incentives for creative accounting that come with a golden rule clause.

b. **Other fiscal rules could also be explored but there are trade-offs.** For example, a debt rule can be combined with a balanced budget rule, but such a rule does not have economic stabilization role and can be affected by factors outside of the government's control. Another option is a debt rule combined with a structural/cyclically adjusted balance rule, which are more suited for countries with strong public financial management systems and are subject to moderate and predictable cycles. Such a rule will provide economic stabilization function and allows for one-off/temporary factors. But correcting for cyclical developments in real-time is complicated, especially with Uruguay undergoing structural changes, which makes the estimation of potential output/cyclical component difficult, and prone to external shocks. In addition, this would require a precise definition of one-off (temporary) factors to avoid their frequent (opportunistic) use. Finally, its intrinsic complexity makes it more difficult to communicate and monitor and susceptible to policy mistakes.

8. Escape clauses should have (i) a limited and clearly defined set of events triggering the operation of the clause, (ii) time limits on how long fiscal policy can deviate from the targets in the rule, and (iii) a requirement for fiscal policy to return to the targets after the operation of the escape clause is terminated and possibly offset the accumulated deviations.

9. Budget estimates could be more frequently updated (if enough resources are in place). This would allow the government to regularly monitor available fiscal space, and adjust policies as needed to remain within targets, particularly given Uruguay's exposure to volatile external circumstances.

10. Public investment management framework could be further strengthened. There is a need for keeping track of, and ensuring funding for, investment projects which typically have longer implementation cycles than the MTFF and political cycle. To address this issue, both linking the government's strategic medium-term plan (which sets long-term development objectives and priorities) to the budgetary process and introducing a framework that tracks projects from their inception until their ex-post evaluation, would be helpful. A state-of-the-art public investment management framework is particularly important given the ongoing large PPP projects.

11. Budgetary targets should be set for the non-financial public sector (NFPS). Given that the central bank's debt (and deficit) reflects regular monetary and liquidity operations and that there is no monetary financing of the fiscal deficit, fiscal targets should be set for the NFPS. This would limit the volatility and uncertainty of the targets as they would no longer be affected by the costs of sterilized interventions (not under the control of the fiscal authority).

12. A broad expenditure coverage (budget unity): The MEF should ideally be responsible for defining a binding overall ceiling that covers all public expenditure, including those of Article 220 Entities, which ensures fiscal sustainability and improves the allocation of limited resources.

13. Strengthened accountability: Ultimately, the credibility of fiscal policy depends on its ability to demonstrate how today's assessment of the current and future budgetary position is consistent with previously formulated medium-term plans. In cases of deviations from targets, some mechanism for accountability must be in place. Placement of responsibility requires that both the MEF and parliament treat seriously large deviations from multiyear expenditure plans that threaten compliance with government's commitments. Various options for such mechanisms exist including requiring responsible ministries to have forecast overspending regularized through a claim on the central contingency reserve or to accept an offsetting reduction in expenditure ceilings in outer years.

14. Fiscal councils: authorities could consider establishing an independent fiscal council (as in Chile, Colombia and Peru). Such institution could provide an unbiased assessment on the credibility of government's forecasts, the fiscal space assessment (spending envelope), and plans to achieve targets. Importantly, it could play a crucial role in holding governments to account for performance against past multiyear plans. It could also help enforcing rules by providing an independent voice on their implementation, which could be a formal or informal "check" on the execution of fiscal plans and performance.

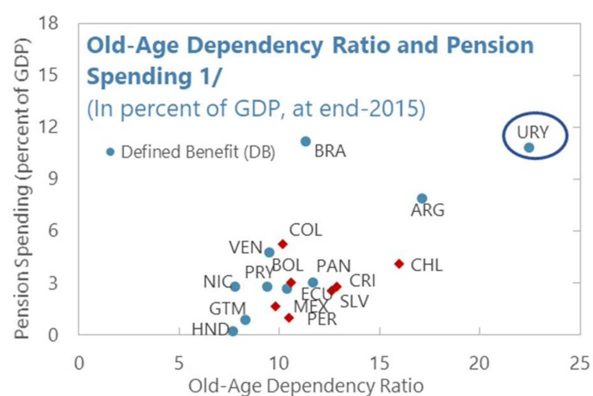
15. Enhancing risk disclosure: The government could consider full disclosure of information on all material risks in a fiscal risk report (as an appendix to the annual budget implementation report). Such a disclosure can create stronger incentives to ensure that all risks are identified, quantified, and managed. Disclosure can help promote earlier and smoother policy responses to changing circumstances and increase confidence among stakeholders on the quality of fiscal management. It could reduce uncertainty for investors and taxpayers and improve access to international capital markets during difficult times.

a. **Fiscal exposure to macroeconomic risks** can be assessed by means of sensitivity or scenario analysis. Sensitivity analysis shows the impact of small changes in the forecasts of key variables (e.g., borrowing costs, GDP growth, real exchange rate, or commodity prices), taken one at a time, on government revenues and expenditures. Scenario analysis entails the design of alternative plausible combinations of macroeconomic variables to check the robustness of the fiscal and debt positions to large simultaneous adverse developments in key parameters (e.g., a "low-growth" scenario).

b. **Fiscal liabilities and risks connected to PPPs:** Risks related to PPP projects (for example stemming from availability payments set in U.S. dollars) should be monitored and transparently presented.

16. Public expenditure reviews: While health and education outcomes are broadly similar to those in other Latin American countries, there may be scope to provide the same services (both in terms of quality and coverage) with less expenditure. More broadly, regular use of in-depth strategic and policy focused spending reviews could help increase efficiency, create fiscal space for priority spending, and strengthen the link between the government's strategic goals and budget allocations.

17. Reducing spending rigidities is essential for fiscal sustainability. In this context, reforms are needed to ensure fiscal sustainability the social security regime and provide adequate pensions for future generations. Such reforms should encompass a comprehensive review of the entire system. In addition, public wages should remain comparable to those in the private sector, to attract and retain talent but avoiding excessive costs.



Source: United Nations 2015. *World Population Prospects: The 2015 Revision* and countries' authorities.
1/ For Uruguay, pension spending includes special pension regimes.

INTERNATIONAL MONETARY FUND

URUGUAY

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

January 27, 2020

Prepared By | Western Hemisphere Department (in consultation with other departments)

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FUND RELATIONS

(As of November 30, 2019)

Membership Status: Joined: March 11, 1946; Article VIII

General Resources Account:	**SDR Million**	**%Quota**
Quota	429.10	100.00
IMF's Holdings of Currency (Holdings Rate)	342.89	79.91
Reserve Tranche Position	86.21	20.09

SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	293.26	100.00
Holdings	214.49	73.14

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Jun 08, 2005	Dec 27, 2006	766.25	263.59
Stand-By	Apr 01, 2002	Mar 31, 2005	1,988.50	1,988.50
of which SRF	Jun 25, 2002	Jun 24, 2003	128.70	128.70
Stand-By	May 31, 2000	Mar 31, 2002	150.00	150.00

Overdue Obligations and Projected Payments to Fund[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

		Forthcoming			
	2019	2020	2021	2022	2023
Principal					
Charges/Interest		0.63	0.63	0.63	0.63
Total		0.63	0.63	0.63	0.63

Implementation of HIPC Initiative: Not Applicable

Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable

As of February 4, 2015, the Post-Catastrophe Debt Relief Trust has been transformed to the Catastrophe Containment and Relief (CCR) Trust.

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Ex-Post Assessment. The last Ex-Post Assessment of Longer-Term Program Engagement was considered by the Executive Board on August 29, 2007 (Country Report No. 08/47).

Exchange Rate Arrangement. The currency is the Uruguayan peso (UY$). Uruguay's de jure and de facto exchange rate arrangements are classified as floating. Since June 2013, monetary policy targets the growth rate of M1 plus saving deposits as the intermediate instrument. On January 6, 2020, the exchange rate in the official market was UY$37.2 per U.S. dollar. Uruguay has accepted the obligations of Article VIII and maintains an exchange rate system free of restrictions on payments and transfers for current international transactions.

Article IV Consultation. Uruguay is on the standard 12-month consultation cycle. Discussions for the 2018 Article IV consultation took place during February 13, 2019 (IMF Country Report No. 19/64). Staff discussions for the 2019 Article IV consultation were conducted in Montevideo during December 5–17, 2019.

FSAP Participation and ROSCs. A Financial Sector Stability Assessment (FSSA) was considered by the Executive Board on June 28, 2006 (Country Report No. 06/187). An FSAP Update was conducted in 2012 and the FSSA was published on May 31, 2013 (Country Report No. 13/152). A ROSC module on fiscal transparency was published on March 5, 2001. A ROSC module on data dissemination practices was published on October 18, 2001. A ROSC on Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) was published on December 12, 2006 (Country Report No. 06/435). A data module ROSC was published on February 11, 2014 (Country Report No. 14/42).

Technical Assistance 2009–19.

DPT	Purpose	Date of Delivery
FAD	Public Financial Management	November 2018
	Revenue Administration (Follow-up)	November 2017
	Assist with strengthening customs' reform strategy and implementation of the governance framework	November 2015
	Tax Administration, PFM (Follow-up)	October 2015
	Treasury Management	August 2014
	Tax, customs, and social security administration	August 2014, March 2014, November 2012, November 2011, September 2010
	Performance Informed Budgeting	March 2011
	Private public partnership	May 2010

LEG	Structures and tools for strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	October 2017
	Structure and tools for strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	November 2016
	Structure and tools for strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	March 2016
	Structure and tools for strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	October 2015
	Structure and tools for strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	March 2015
	Assist the authorities on strengthening the AML/CFT capacity of the Superintendency of Financial Services and the Financial Intelligence Unit	October 2014
	Follow up of the implementation of the AML/CFT National Strategy	October 2013
	Assist the authorities on the launch of the recently designed AML/CFT national strategy	June 2012
	Assist the authorities on the elaboration of a risk-based national strategy enhancing the AML/CFT regime	December 2010
	Conduct a money laundering/terrorist financing country risk assessment consistent with the objectives of the national AML/CFT strategy	January, April, and July 2009
MCM	Sovereign Asset and Liability Management and Development of the Local Currency Government Bond Market	September 2016
	Bank resolution	June 2014
	FSAP update	September 2012
STA	Trade Margins and Commercialization Channels	September 2016
	Balance of Payments and International Investment Position Statistics.	April and October 2015
	Data ROSC reassessment	August 2012

RELATIONS WITH OTHER INTERNATIONAL INSTITUTIONS

- World Bank: https://www.worldbank.org/en/country/uruguay
- Inter-American Development Bank: https://www.iadb.org/en/countries/uruguay/overview
- Development Bank of Latin America: https://www.caf.com/es/paises/uruguay/

STATISTICAL ISSUES

(As of [January 8, 2020])

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings but is broadly adequate for surveillance. Most affected area is national accounts.
National accounts: In 2009, the Uruguayan authorities completed a revision of national accounts statistics, in which they updated the benchmark year (from 1983 to 1997), set the reference period for the volume estimates in 2005, and adopted the *System of National Accounts (SNA) 1993*. However, national accounts statistics still have some shortcomings: the benchmark year is obsolete, expenditure GDP contains some residual components, fixed ratios are used for various activities, coverage of the enterprise survey is limited, the update of the business register is partial, source data for some components of GDP are of poor quality, and information on the informal economy is inadequate. GDP time series on the BCU website are available starting in 1997. A national accounts rebasing project (to 2012) is underway, and the new figures, in line with the 2008 *SNA*, will be disseminated in 2020.
Prices: The base period for the consumer price index is December 2010 = 100. The CPI has national coverage, and it does not cover either the implicit rent or the net acquisitions of owner-occupied dwellings. The reselection of the sample of detailed products has not been done for an extended period (the current weights are based on the 2005-06 household income and expenditure survey). Producer price indices (March 2010 =100) for national products are available, but do not cover utilities, construction, and services, and exported output. The CPI and PPI would benefit from a more regular and frequent schedule of weight updates.
Government finance statistics: Official data on the central administration, the state owned enterprises and the social security system are disseminated regularly and on time. However, above-the-line data (revenue and expenditure) for local governments are not available. Monthly data for financing and quarterly data for debt for the central government and total public sector are disseminated on the BCU website from 1999 onwards, but no information is reported for publication in the *International Financial Statistics*. Annual information submitted for the *Government Finance Statistics Yearbook* covers the consolidated central government (budgetary central government plus social security funds) and consolidated general government, but COFOG is not reported and local governments information belongs to financing operations only; thereby, consolidated general government's covers only operations and stocks on financial assets and liabilities.
Monetary and financial statistics: Monetary and financial statistics are prepared in accordance with the IMF's *Monetary and Financial Statistics Manual (2000).* The authorities report monetary data for the central bank, other depository corporations, and other financial corporations (OFCs) using the standardized reporting forms (SRFs). However, data for the OFCs are limited to off-shore financial institutions. A mission to expand the institutional coverage of OFCs and compile the SRF for OFCs with full institutional coverage was proposed to the authorities and is expected to take place in 2020.

<table>
<tr><td colspan="2">Financial sector surveillance: The authorities participate in the IMF's Coordinated Direct Investment Survey (CDIS), Coordinated Portfolio Investment Survey (CPIS), and Financial Soundness Indicators (FSIs) databases. However, only annual FSIs data for deposit-takers and other financial corporations are being reported. FSIs on nonfinancial corporations, households, market liquidity, and real estate markets are not available. The BCU disseminates FSIs for individual banks on a monthly basis and generates FSIs for the banking system weighting individual bank FSIs by their asset share. Uruguay reports data on several series indicators of the Financial Access Survey (FAS) including the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs).</td></tr>
<tr><td colspan="2">External sector statistics: Balance of payments and international investment position statistics are compiled and published on a quarterly basis. Data are compiled following the recommendations of the sixth edition of the Balance of Payments Manual. Uruguay disseminates the international reserves and foreign currency liquidity data template, submits quarterly external debt statistics to the World Bank's Quarterly External Debt Statistics (QEDS) database, and participates in the Coordinated Portfolio Investment Survey (CPIS) and the Coordinated Direct Investment Survey (CDIS).</td></tr>
<tr><th colspan="2">II. Data Standards and Quality</th></tr>
<tr><td>Uruguay subscribed to the SDDS in February 2004 and is in observance.</td><td>Data ROSC published on October 1, 2001.

A data reassessment ROSC on CPI, PPI and NA was published in February 2014.</td></tr>
<tr><th colspan="2">III. Reporting to STA</th></tr>
<tr><td colspan="2">Both the consumer and wholesale price indices are reported on a regular and timely basis for publication in the International Financial Statistics (IFS). The authorities do not provide trade price and volume indices for publication in the IFS.

Annual GFS are regularly reported to STA for publication in the Government Finance Statistics Yearbook. No high frequency GFS are reported for publication in the International Financial Statistics.

Uruguay reports to STA balance of payments and IIP data for publication in the IFS and the Balance of Payments Statistics Yearbook.</td></tr>
</table>

Uruguay: Common Indicators Required For Surveillance (As of January 10, 2020)							
	Date of latest observation	Date received	Frequency of Data 7/	Frequency of Reporting 7/	Frequency of Publication 7/	Memo items:	
						Data Quality – Methodological Soundness 8/	Data Quality – Accuracy and Reliability 9/
Exchange Rates	01/09/20	01/10/20	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities 1/	01/09/20	01/10/20	D	D	D		
Reserve/Base Money	11/19	01/02/20	M	M	M		
Broad Money	11/19	01/02/20	M	M	M		
Central Bank Balance Sheet	11/19	01/02/20	M	M	M		
Consolidated Balance Sheet of the Banking System	11/19	01/02/20	M	M	M		
Interest Rates 2/	11/19	12/17/19	D	D	D		
Consumer Price Index	12/19	12/06/19	M	M	M	O, LO, O, O	LO, O, O, LNO,
Revenue, Expenditure, Balance and Composition of Financing 3/– Central Government 4/	11/19	12/31/19	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt 4/ 5/	Q3/19	12/31/19	Q	Q	Q		
External Current Account Balance	Q3/19	12/31/19	Q	Q	Q		
Exports and Imports of Goods and Services	11/19	12/31/19	M	M	M		
GDP/GNP	Q3/19	12/17/19	Q	Q	Q	LO, LO, LO, LO	LNO, LNO, LO,
Gross External Debt	Q3/19	12/31/19	Q	Q	Q		
International Investment Position 6/	Q3/19	12/31/19	Q	Q	Q		

1/ Includes reserve assets pledged or otherwise encumbered as well net derivative positions.
2/ Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
3/ Foreign, domestic bank, and domestic nonbank financing.
4/ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
5/ Including currency and maturity composition.
6/ Includes external gross financial asset and liability positions vis-à-vis nonresidents.
7/ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).
8/ This reflects the reassessment provided in the data ROSC (published in February 2014 and based on the findings of the mission that took place during August 20–31, 2012) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning (respectively) (i) concepts and definitions, (ii) scope, (iii) classification/sectorization, and (iv) basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).
9/ Same as footnote 9, except referring to international standards concerning (respectively) (i) source data, (ii) assessment of source data, (iii) statistical techniques, (iv) assessment and validation of intermediate data and statistical outputs, and (v) revision studies.

Statement by Mr. Chodos, Executive Director,
and Mr. Vogel, Advisor on Uruguay
February 19, 2020

Uruguay and the Fund

The Uruguayan authorities would like to express their gratitude to staff and Management for the frank and fruitful dialogue held over the past years. In many cases, through this dialogue, the authorities and staff concurred with similar views, while differences prevailed in other cases; beyond that, the relationship between Uruguay, a founding member of the institution, and the IMF has been absolutely candid and respectful. In this opportunity of the 2019 Article IV Consultation, IMF staff, particularly Ms. Berkmen and her team, have made relevant contributions by clearly assessing Uruguay's strengths, challenges, risks, and opportunities─always in a constructive and collegial manner.

"Enviable Position"

The authorities were pleased to read the concept underlined by staff in the first paragraph of the report: "Uruguay is in an enviable position in many respects. The country enjoys political stability, strong governance and institutions, and a high degree of social cohesion". In times where some of the most relevant risks that the global economy and, particularly, the region are stemming from social and political instability, Uruguay remains a bastion of institutional and social stability.

For example, the country ranks first in Latin America in the widely followed Democracy Index 2019 published by The Economist Intelligence Unit, and in fifteenth position worldwide, placed in the select group characterized as "full democracies". Furthermore, according to Transparency International, Uruguay has the lowest level of perceived corruption among its Latin American peers and it is almost in the first decile among 180 countries in the world. In addition, among some other indicators, Reporters without Borders ranks Uruguay 19th in the 2019 World Press Freedom Index. It is worth mentioning that

during Uruguay's electoral year, which ended in November 2019, and the subsequent transition period that will end on March 1, 2020, there has been no kind of noise in the economic, political, and social fields. Uruguay is very proud of these institutional achievements built throughout an important part of the country's history.

Growth, Investment, and Employment: Uruguay is Poised for a Significant Boost in Foreign Direct Investment (FDI)

In 2019, Uruguay posted its seventeenth year of consecutive growth rates. Admittedly, over the past years, since 2015, growth has been more tepid. In the Selected Issues paper's chapter on Dissecting Economic Growth in Uruguay, staff mostly focus on the external factors behind the substantial growth observed in 2004-14. It is also important to highlight what happened in the following five years: Uruguay continued growing although at smaller rates, while Argentina suffered three years of recession, financial turmoil, and extreme volatility of its exchange rate system. Meanwhile, Brazil suffered a severe recession in 2015 and 2016 and, thereafter, an anemic recovery until 2019. The diversification process carried out by Uruguay over the past two decades, in terms of markets and products, constitutes a critical factor to understand how Uruguay has been able to avoid correlating with regional trends.

Needless to say, sluggish investment and unemployment have been matters of concern. It is important to mention that for this year and the coming years, growth projections are higher than the rate observed in 2019, more in line with Uruguay's potential growth. It is important to note that the upcoming large FDI inflows will be predominantly headed into the export sector and transport infrastructure network.

The Uruguayan authorities broadly agree with the set of reforms suggested by staff in the Selected Issues paper. This would allow Uruguay to further increase its potential growth and inclusiveness. Particularly, the authorities concur with the importance of enhancing the quality of education, and the fact that low population growth and aging pressures could be alleviated by further raising female participation and further facilitating integration of immigrants into labor market. Meanwhile, in recent years, Uruguay has also undertaken a process of financial inclusion, with objectives related to continue reducing evasion and informality, progress on decreasing inequality, and advancing financial development.

Fiscal Issues: Concerns and Strengths

Developments in terms of economic activity have substantially impacted fiscal accounts, which have been a matter of concern for the authorities. The authorities and staff agree on the need to put debt on a firm downward path. Although Annex II of the staff report rightly notes that projected debt distribution confirms that debt dynamics are generally manageable, it is quite clear that the debt dynamic has deteriorated over the past years and should be

addressed. In this regard, staff poses relevant suggestions throughout the report, for instance, in paragraph 18.

There are many reasons to be optimistic that these challenges will be successfully faced. One of these reasons relates to Uruguay's political stability and maturity. Given the rigid government spending profile, staff highlights the consensus across the political spectrum regarding key challenges; one of the most important challenges, in this regard, is associated to addressing growing pension spending. The authorities fully agree with what is stated in the report: "reforms should be based on a comprehensive review of the entire system, supported by an informed social dialogue".

Another important institutional aspect to be underscored is associated with the country's Medium-Term Fiscal Framework (MTFF), which is well-described in Annex IV of the staff report, stressing the significant progress observed in the country's MTFF. Naturally, there are areas which need improvements. In this regard, the authorities have mentioned the importance of increasing the quality of spending and performance evaluations.

Inflation and the Exchange Rate

Inflation pressures have built up over the past few months from an acceleration of tradable prices, especially meat prices, which was partially offset by more subdued non-tradable inflation. Of course, inflation has been another matter of concern for the authorities, who have maintained a moderately contractive bias in their monetary policies. Meanwhile, Uruguay continues with its flexible exchange rate regime, a key policy to cushion external shocks; interventions on both sides of the market have been limited to smooth abrupt movements that do not respond to fundamentals. The Uruguayan authorities take note of staff's assessment that "Uruguay's external position is broadly consistent with fundamentals and desirable policy settings". Furthermore, the current account of the Balance of Payments has been in surplus since 2017, which compares favorably with other regional economies.

Financial Buffers

Uruguay has made substantial achievements in strengthening macroeconomic and financial stability. International reserves are close to 25 percent of GDP, providing the Central Bank with substantial foreign exchange liquidity in an eventual event of a temporary shock. International reserves remain above the upper bound of the IMF reserve adequacy metric range.

Prudential measures anchored in the implementation of the Basel regulatory framework also played an important role in ensuring financial stability: the banking sector continues to present sound financial indicators, including high capital levels and adequate liquidity buffers. Meanwhile, during the economic slowdown, Uruguay's sound financial system

reaped the fruits of years of critical reforms in its public banks and regulatory and supervisory frameworks.

Active debt management has played a key role in mitigating financial vulnerabilities associated with risks of currency and maturity mismatches. This was accomplished by reducing the share of government debt denominated in foreign currency, lengthening the average maturity of debt, and smoothing its redemption profile. Today, the average maturity of Uruguay's debt is 14 years, debt in local currency is close to 44 percent, while debt is at a fixed rate of 94 percent of the total.

Uruguay's authorities are pleased with the recently issued IMF Working Paper (WP/19/290) entitled "Sovereign Asset and Liability Management in Emerging Market Countries: The Case of Uruguay". The study provides an overview of the experience of Uruguay in measuring and managing financial risk exposures within the consolidated public sector. It also describes the coordination mechanisms established between public sector institutions (DMU, Treasury, Central Bank, and main State-Owned Enterprises) to bring sovereign assets and liabilities within the scope of portfolio decision-making. Using Uruguay as a case study, it distills policy-relevant lessons that could apply to other emerging markets in achieving a more cost-effective management of public sector debt and resilience of public finances.

While the robustness of Uruguay's financial buffers does not at all substitute the need to reinforce the country's fiscal consolidation process, it mitigates the need to take hasty measures over a short period of time.

Environmental, Social and Governance (ESG) Practices, and Sustainability Commitments

Sustainable and impact investments are becoming key drivers of global capital allocation decisions. Investors are increasingly embedding ESG factors into their sovereign creditworthiness assessments, reshaping their fixed-income investment strategies. Likewise, multilateral institutions are more frequently incorporating responsible investment and sustainability standards to their loan disbursement programs.

As staff notes, Uruguay is a top performer on ESG fundamentals among emerging markets. Over the last five years, Uruguay's energy matrix has shifted towards renewable resources: in 2019, 98 percent of electricity generation was based on renewal sources of energy, on the back of a dramatic increase in wind power. In turn, less reliance on fossil fuels has limited the exposure of fiscal finances to climate-related risks (such as droughts). As underscored on many other occasions, Uruguay is distinguished for the stability of its political system, social cohesion, low poverty rates and inequality indicators, as well as the absence of civil unrest. All these factors are reflected in J.P. Morgan's ESG-adjusted benchmark index, where Uruguay has the largest country weighting across 73 emerging markets.

Conclusion

Amidst multiple negative external shocks from the region and world economy over the past years, Uruguay has stayed the course, warranting the IMF staff's laudatory concepts. Naturally, there are a number of relevant challenges lying ahead, particularly from the domestic side on the fiscal front. At the same time, Uruguay exhibits important strengths and assets which provide clear reasons to be optimistic that the country will be able to successfully address them. These include its robust financial buffers, sound institutions, the ample consensus across the political spectrum on how to address key challenges, and Uruguay's impeccable record of honoring commitments.