Euler Hermes Economic Research

Country Risk Analysis

Uruguay

Meat in the sandwich?

General Information

GDP	USD46.7bn (World ranking 78, World Bank 2011)
Population	3.37 millions (World ranking 133, World Bank 2011)
Form of state	Constitutional Republic
Head of government	Jose "Pepe" MUJICA Cordano
Next elections	2014, presidential and legislative

Strengths

- Durable, democratic political system with a good degree of social consensus
- Strong business environment
- Generally balanced policy mix with downward trend in public and external debt-GDP ratios Successive left-of-centre governments have prioritised macroeconomic stability
- External balance overall strong

Weaknesses

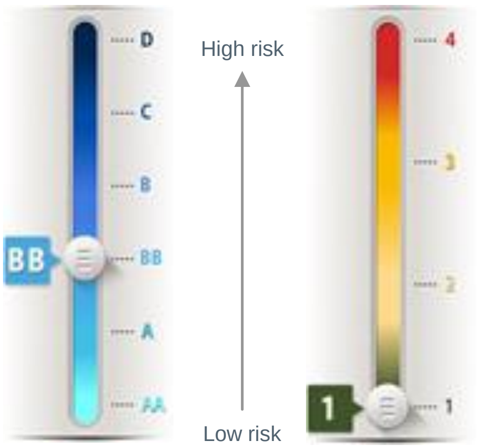
- Relatively high inflation and public debt-GDP ratio
- Banking system highly dollarized with large non-resident deposits
- Vulnerable to external shocks particularly via trade and financial links with larger neighbours, Brazil and Argentina

Country Rating

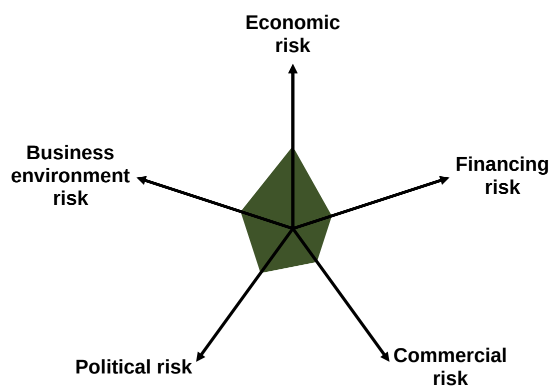
BB1

Country Grade

Country Risk Level



Risk Dimensions



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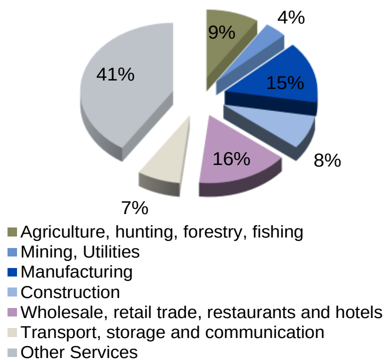
Economic Structure

GDP breakdown (% of total, 2010)



Trade structure (% of total, 2010)

By destination/origin

Exports		Rank		Imports
Brazil	19%	1	20%	Argentina
Various	13%	2	18%	Brazil
China	9%	3	12%	China
Argentina	7%	4	9%	United States
Germany	5%	5	5%	Venezuela

By product

Exports		Rank		Imports
Other Edible Agricultural Prod	18%	1	8%	Crude Oil
Meat	16%	2	6%	Refined Petroleum Products
Cereals	13%	3	5%	Plastic Articles
Non-Edible Agricultural Prod.	8%	4	4%	Other Edible Agricultural Prod
Fats	7%	5	4%	Pharmaceuticals

Sources: Chelem, UnctadStat, IHS Global Insight, Euler Hermes

Economic Forecast

	Average 2000-08	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	2.0	2.4	8.9	6.5	3.9	3.6	4.0
Inflation (%, end-year)	9.0	5.9	6.9	8.6	7.5	6.8	6.5
Fiscal balance (% of GDP)	-1.9	-1.7	-1.1	-0.9	-2.8	-2.4	-2.2
Public debt (% of GDP)	#N/A	62.7	58.0	57.8	59.4	56.3	52.9
Current account (% of GDP)	-1.2	-1.3	-1.9	-2.9	-5.3	-4.9	-4.7
External debt (% of GDP)	85.7	60.2	47.7	38.9	40.3	36.6	35.2

Sources: IHS Global Insight, National sources, Euler Hermes

Economic Growth

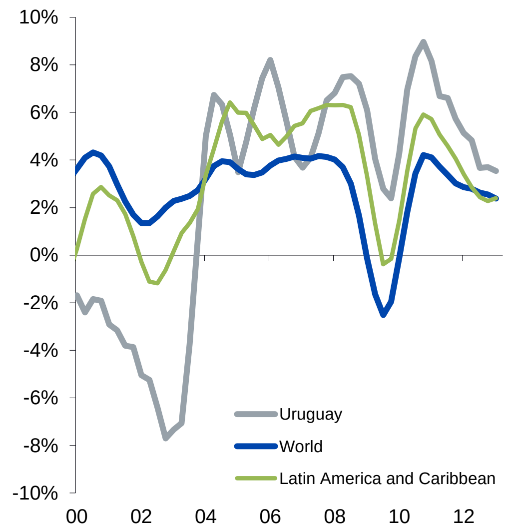
Vulnerable to external shocks but medium term growth relatively strong

The economy is highly vulnerable to external shocks, particularly given its small size and strong linkages via trade and the banking system with two much larger neighbours, Brazil and Argentina. Also, more than half of exports are commodities. Uruguay has weathered the global financial crisis well and GDP has grown by an annual average 5.4% in 2009-12. Real per capita income growth was good at an annual average 3.9% in the past decade.

Slower in 2012 and 2013, modest pick up in 2014

Growth slowed to 3.9% in 2012 from 6.5% in 2011 2013 and domestic demand should be sufficient to maintain a pace of 3.5% in 2013. Growth should improve in 2014 to 4% as global demand gains momentum.

GDP growth (y/y, 4 qtrs cumulated %)



Sources: IHS Global Insight, Euler Hermes

Economic Policies

Successive left-of-centre governments have continued to adopt a pragmatic policy framework, prioritising macroeconomic stability.

Capital inflows and inflation pressures

Monetary policy is framed against inflation targeting, currently 4-6%, though this has been complicated by currency inflows that have led to an over-strong exchange rate, forcing the central bank to impose capital controls on incoming investment. Inflation was 8.5% y/y in March (down from 8.9% in February) and though it should fall to 6.8% by end-2013 this will still be above target. The policy interest rate was raised by 25bps to 9.25% in December 2012 and banks' reserve requirements have also been raised, but the central bank has faced difficulties trying to sterilise monetary inflows (which it has not been able to do entirely successfully) to temper exchange rate appreciation, leaving the exchange rate increasingly over-valued (uncompetitive). Credit expansion has moderated in recent quarters, though it remains relatively high.

The latest IMF article IV consultation notes that “the financial system is small, sound, and liquid, and there are no generalized credit or real estate bubbles in the economy”. Non-performing loans in 2012 were 1.5% of total assets.

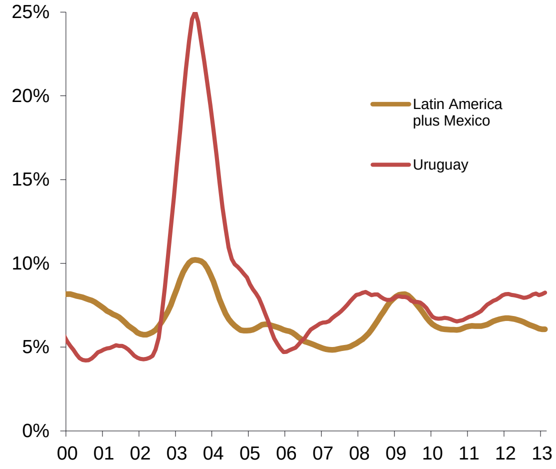
Positive debt dynamics

The consolidated public sector deficit (which includes the central bank) widened to -2.8% of GDP in 2012 from less than 1% in 2012, partly the result of an increase in public investment in infrastructure projects, but also because of increased expenditure on energy to cope with drought. The fiscal deficit should narrow in 2013 to -2.4%, a manageable level.

The public debt-GDP ratio is on a downward trend though it rose slightly in 2012 as a result of debt issuance to sterilise capital inflows and should fall to 55% in 2013. While it will be difficult to achieve the official 45% of GDP target in 2015, the maturity profile of the debt has improved significantly through active debt management and less than 50% of public debt is external debt.

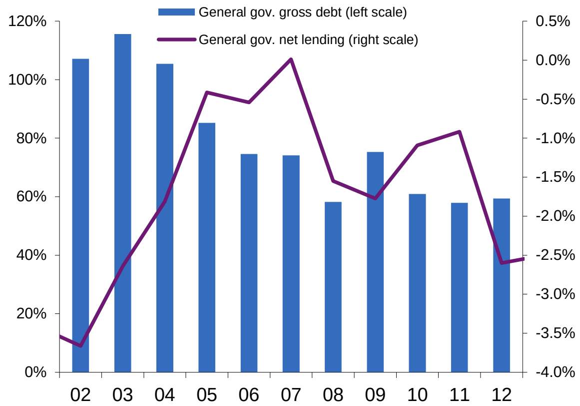
The government has also built-up fiscal buffers with deposits at the central bank.

Inflation rate (%)



Sources: IHS Global Insight, Euler Hermes

Fiscal balance and debt (% of GDP)



Sources: IHS Global Insight, Euler Hermes

Widening current account but strong FDI flows

The current account deficit widened to -5.3% of GDP in 2012 as energy and capital goods (associated with investment projects) increased, while export growth slowed on weaker demand and flat services income, as receipts from tourism was hit by restrictions on Argentine's travel abroad.

The deficit should narrow in 2013 and 2014, however, as export growth picks up in line with improved demand and import growth moderates.

Moreover the current account deficit is almost fully covered by strong FDI flows, limiting the need to build up external debt.

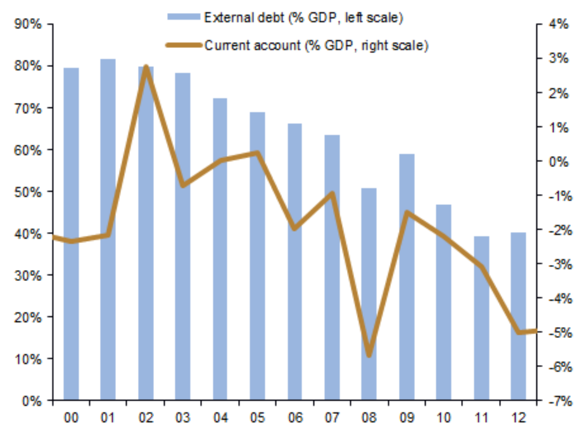
External debt on downward trend

External debt is moderate and has been on a downward trend since the mid-2000s. External debt is 40% of GDP, 158% of exports of goods and services and interest payments are less than 5% of exports of goods and services.

Foreign exchange reserves increase

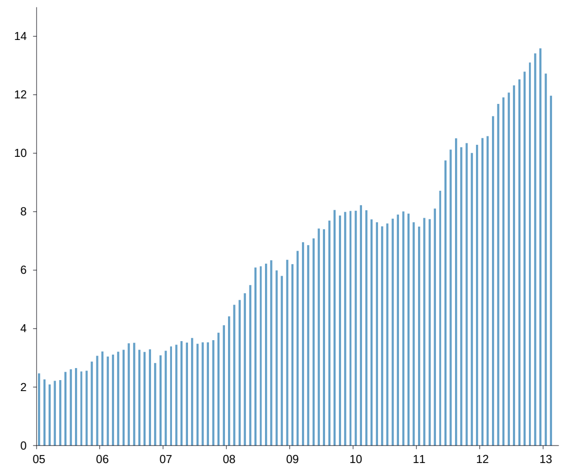
Foreign exchange reserves have increased steadily and cover 10 months imports of goods and services and more than 200% of external debt falling due (including ST) in 2013

External debt and current account (% of GDP)



Sources: IHS Global Insight, Euler Hermes

FX reserves (USDbn)



Sources: IHS Global Insight, Euler Hermes

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