



Market Commentary
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English Version

Insigneo Weekly Dispatch

Uruguay: The Power of an Informed Choice

Guidance on investments and the major structural factors behind your clients' portfolios.

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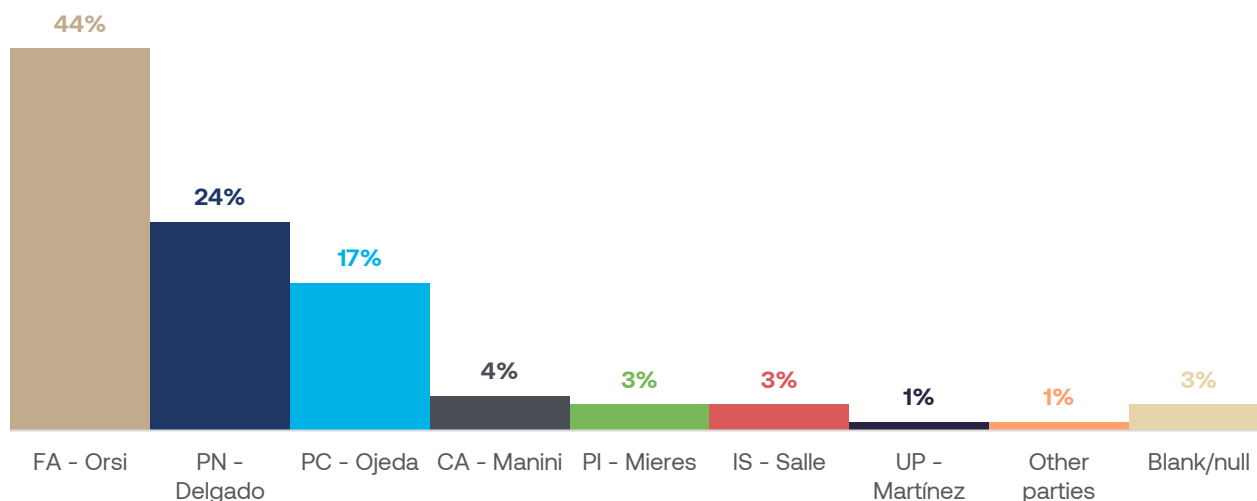


Uruguay: The Power of an Informed Choice

This Sunday, Uruguay will go to the ballots to elect its new president, both chambers of Congress, and to vote on two plebiscites - one related to security and the other a reform to the social security system. Given the current uncertainty surrounding the elections, we deemed it necessary to dive deeper into what these elections mean for the country in macroeconomic terms, and what to expect if the social security plebiscite makes it through the ballots.

To win the presidency, any candidate would need to get more than 50% of the votes; if no candidate receives that percentage of votes, a runoff will be held on November 24th. Therefore, the first thing that needs to be defined is the candidates taking part in this election. According to the latest polls available by Factum, the leading candidate is Frente Amplio's Yamandú Orsi with 44% of the voting intention, followed by Partido Nacional's Álvaro Delgado with 24%, and lastly, Partido Colorado's coalition represented by Andrés Ojeda with 17%.

Current voting intentions:



Source: Factum. Data as of October 6, 2024

The Frente Amplio coalition comes to these elections with an agenda more focused on social goals, such as expanding the coverage of social security, education, and health systems, and increasing the transfers to vulnerable segments of the population through the reduction of tax exemptions and revisions in special tax regimes. On the other hand, the incumbent party, Partido Nacional, is more focused on delivering what JPMorgan analysts denominated “second-round structural transformations,” which include a revamp of the current fiscal and monetary frameworks to eventually consolidate the disinflation process and return to the reduction of the fiscal deficit.

Meanwhile, Partido Colorado’s proposals exhibit a stronger emphasis on a primary surplus convergence achieved via a decrease in real spending, with this scenario being consistent with a dwindling trajectory of the debt/GDP ratio, as well

as with the creation of fiscal room that would help in reducing the tax burden.

However, one of the main issues in Sunday’s election is the referendum focused on the Uruguayan social security system. Currently, the country’s pension system is a mixed one. Workers make a 15% monthly contribution from their salaries to social security. These contributions go towards the social security entity known as BPS, and towards Pension Fund Management companies, AFAPs, which are responsible for saving each worker’s funds and investing them. Moreover, in the case of the BPS, the system is designed in a “solidarity” fashion, where the actively working population pays for the pensions of the current retirees.

In simple terms, the social security plebiscite aims to i) lower the retirement age again to 60 years,

which implies a reversal from a recently approved pension reform that had increased it to 65; ii) require pensions to be equal to the national minimum wage, which would imply a slight increase in the short-term pensions; and iii) give the state the monopoly over the social security system and forbid any private savings system towards retirement, therefore eliminating the AFAPs. The plebiscite, a proposal by Uruguay's communist party, has been backed by the national worker's convention – known in Uruguay as the PIT CNT – as well as by the social security workers' union, with its supporters presenting it as an act for social justice and as a response to the people's indignation against a system that only works for the most powerful, according to the union leader Karina Sosa, who also happens to work at BPS.

Meanwhile, JPMorgan estimates that if this reform were to pass, it would compromise Uruguay's medium-term sustainability, which could lead the incoming administration to increase taxes to finance the additional expenditures the plebiscite requires or risk potentially widening the fiscal deficit. In the medium term, should the elimination of the AFAPs come to fruition, this would be no small blow to the local fixed income market since the private funds held 37% of the issued public debt, according to 2022 data from the Uruguayan Ministry of Finance. Additionally, in 2023, Uruguay was able to meet the pillars of the Fiscal Rule established during the Lacalle Pou administration, a sign of the country's fiscal credibility, which could be jeopardized by a potential widening in the country's structural balance or by a higher net

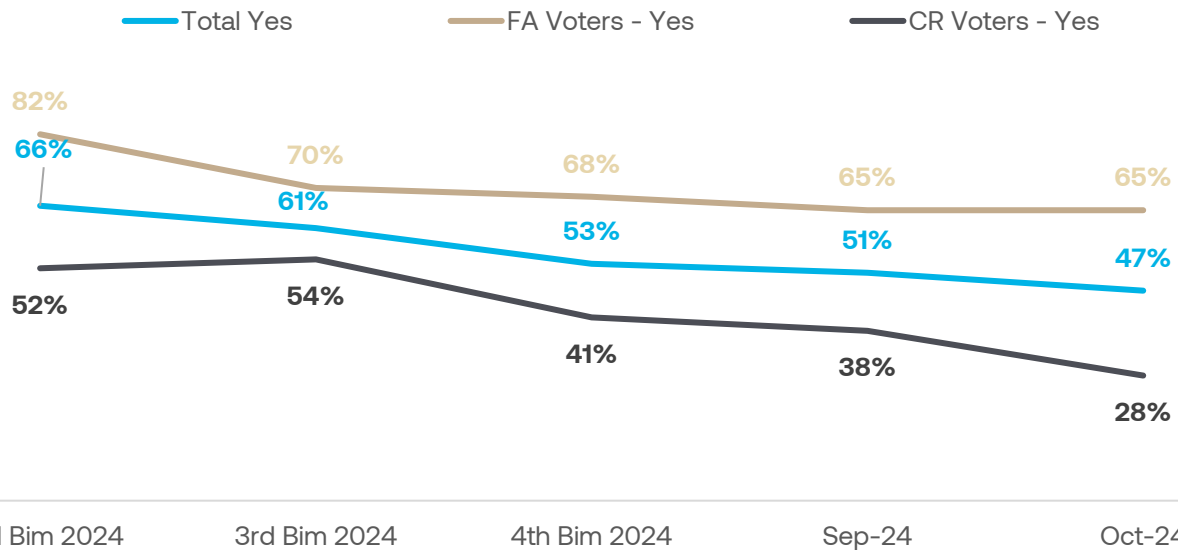
indebtedness – both Fiscal Rule pillars highlighted by the current administration.

Furthermore, the potential approval of the social security plebiscite could have deep implications for the country beyond the fiscal level. Recently, current president Lacalle Pou stated that the failure of the plebiscite would be critical for Uruguay to maintain its country risk at its current level, as well as to allow for new investments in the fields of construction, industrialization, and services that eventually generate additional employment. Against this backdrop, the Uruguayan peso – UYU – has been more volatile in the last month as the elections come closer.

Furthermore, current FinMin Azucena Arbeleche stated that she was aware of the observed investment outflows from foreign investors, which could have also partially propelled the UYU depreciation. The latter contrasts with the steady inflows that Uruguay had previously seen, underpinned by an attractive real rate and the country's reputation as a reliable, transparent market player – a trait that may be in jeopardy were the plebiscite to be approved.

The social security plebiscite has seen its favorability decrease in the last polls, with the last figures available from Factum displaying 47% of voting intention. This contrasts with the 66% of voting intention that the plebiscite had garnered in the second bimester of the year:

Voting intention for the Social Security Plebiscite:



Source: Factum. Data as of October 6, 2024 | FA stands for “Frente Amplio”, “CR” stands for “Republican Coalition”

The waning support for the referendum could be attributed to the vocal opposition it has received from all presidential candidates, as well as from the current administration. As previously stated, president Lacalle Pou recently affirmed that the approval of the plebiscite could bring additional challenges to the country while damaging the economic environment. Furthermore, the leading candidate Orsi has opposed the referendum, even if his party has abstained from taking a formal position.

Aside from the expressed worries from the incumbent and right-leaning political parties, the social security plebiscite has also raised concerns from independent think tanks. Specifically, the

Centro de Estudios de la Realidad Económica y Social – CERES – recently stated this reform would be a historical mistake for Uruguay, considering that even if the current pension system has room for improvement, the road to betterment is not through radical constitutional modifications that would be difficult to reverse in the future. Furthermore, some local market participants have highlighted that a potential approval of the social security plebiscite could be linked to an increase in the country’s expenditure and tax rate, which could eventually lead to higher inflation.

As the weekend nears, it is not a minor responsibility falling on the shoulders of the Uruguayan population. Even if voting for the

plebiscite is not mandatory, this is an example that showcases the importance of being an informed voter. Lastly, we would be remiss if we did not highlight a stat posted by [Opción Consultores](#) where it shows the correlation between how informed people are about the plebiscite and their voting intention: the more knowledgeable people are about the plebiscite, the higher their intention not to vote it.

The author wishes to thank Sofía Berrosteguieta for her invaluable contributions to the writing of this piece.



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