

# BTI 2010 | Uruguay Country Report

<b>Status Index</b>	1-10	<b>9.25</b>	# 5 of 128	
Democracy	1-10	9.90	# 1 of 128	➔
Market Economy	1-10	8.61	# 11 of 128	↗
<b>Management Index</b>	1-10	<b>7.56</b>	# 1 of 128	

scale: 1 (lowest) to 10 (highest)    score    rank    trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

The BTI is a joint project of the Bertelsmann Stiftung and the Center for Applied Policy Research (C•A•P) at Munich University.

More on the BTI at <http://www.bertelsmann-transformation-index.de/>

Please cite as follows: Bertelsmann Stiftung, *BTI 2010 – Uruguay Country Report*. Gütersloh: Bertelsmann Stiftung, 2009.

### Key Indicators

Population	mn.	3.3	HDI	0.87	GDP p.c.	\$	11480
Pop. growth	% p.a.	0.3	HDI rank of 182	50	Gini Index		46.2
Life expectancy	years	76	UN Education Index	0.96	Poverty <sup>2</sup>	%	4.2
Urban population	%	92.2	Gender equality <sup>1</sup>	0.54	Aid per capita	\$	10.2

Sources: UNDP, Human Development Report 2009 | The World Bank, World Development Indicators 2009.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

## Executive Summary

The administration of President Tabaré Vázquez (2005 – 2010) has on the whole lived up to voters' high expectations. With an efficient hands-on approach, its experienced professional team has managed to get important reform legislation implemented, balance market incentives and social responsibility, modernize institutions and make the country, which experienced one of the deepest crises of its history in 2002, one of the region's best prepared in facing the international financial crisis that began in 2008.

During the period under review, the state of democracy in Uruguay was maintained at a high level, allowing the country to remain the BTI's best-performing democracy. By increasing the consistency with which it addresses the juridical, historical and moral dimensions of crimes committed under the military regime, a topic long postponed, the government may even have added to its credibility. Uruguay is a consolidated democracy under the rule of law, with a strong civil society, a high level of participation and no substantial defects.

In addition, the Vázquez years have brought a more consistent and systemic consolidation of the economy. Strong economic performance and structural reforms over the last years have given the country solid, well-capitalized and closely monitored financial institutions with high levels of international reserves. Due to continuous growth, rising export earnings and tax revenues, and strong foreign investment inflows Uruguay has been able to substantially reduce its public and foreign debts. Levels of public and private investment, and particularly foreign direct investment, have gone up and created jobs. Even if the pace may slow as a result of the international financial crisis, investment appears to be secured for future years, particularly by the construction of large cellulose and liquid gas conversion plants, by the public/private partnership projects of the new transport-infrastructure development program, and the substantial ventures that will be generated by the "Uruguay Round 2009," aimed at exploiting the recently discovered offshore natural gas reserves near Punta del Este. However, Uruguay's economy is

still vulnerable, not only structurally (with respect to size, dependency on the performance of neighbors and foreign markets, and high dollarization), but also with regard to the impact of the international crisis, even if the country's corporatist traditions and its relatively high degree of state interventionism may serve as some cushion.

The quality of governance has also been significantly improved during the last years, though not all items on the government's reform agenda have been implemented. Besides accomplishing more structural domestic reconciliation (between the "two Uruguays" that existed after the dictatorship) and some de-escalation of conflict in the relationship with neighboring Argentina, particular progress has been made in the areas of tax and health reform, social security reform, in parts of education reform and the reform of the financial institutions, and in many programs of economic de- and reregulation. Among the issues that have not been (sufficiently) addressed and remain on the agenda, we find, among others, highly contested matters such as the question of autonomy for the educational institutions; the basic parameters of the welfare systems; the pension schemes for state functionaries, the police, the military and the employees of the banking sector; and, in particular, the comprehensive reform of the civil service and the state administrative structures (*reforma del estado*) which so far has been postponed. Poverty, inequality, the improvement of tertiary education and R&D are other issues that need further attention.

First, however, Uruguayan politics in the years 2009 and 2010 will be dominated by intensified efforts to cope with the repercussions of the worldwide financial crisis, and by the upcoming elections in 2009 and 2010. As the record of the Frente Amplio government is on the whole impressive, the polls in March 2009 gave the Frente the upper hand over the opposition, of which the National (Blanco) Party continues to be the strongest component. Though in Uruguay's complicated political system much will depend on who will be the candidates for the presidency, a Frente victory does not appear unlikely, particularly if its two frontrunners, the more "centrist" Danilo Astori and more "leftist" José Mujica, can unite forces.

## History and Characteristics of Transformation

Since the Batllista reforms between 1900 and 1930, which were inspired by the various presidencies of José Batlle y Ordóñez of the Colorado Party, Uruguay has been a stable democracy throughout most of the twentieth century. It was characterized by an active and strong civil society (populated mostly by immigrants of European descent) as well as by affluence and significant distributive policies that turned the small, homogeneous and highly urbanized country into one of the first modern welfare states and formed the core of a unique developmental model. A boom in agricultural exports, mostly represented by cattle, lasted without interruption until the mid-1950s, and provided the basis for Uruguay's prosperity.

Triggering industrialization and modernization, this boom also promoted social integration, but left the country highly dependent on world markets for its traditional, almost monocultural export products.

One of the principal characteristics of the Uruguayan model was the early institutionalization of a peculiar system of competitive party democracy rooted in all segments of society and channeled through the two traditional parties, the Blancos (Partido Nacional) and the Colorados, with their various factions, lists and “sublemas.” The model combined a high degree of mobilized, participatory factionalism with mechanisms of integration and reform, which served decision-making and institution-building needs until the late 1960s. The democratic consensus was strong, social homogeneity high, and the state (along with the city of Montevideo) fulfilled major functions as the provider of collective goods and services. Significant national, ethnic, religious or social cleavages were nonexistent, with the exception of the classic rift between capital and labor. However, after the decline of export prices for cattle in the 1950s, the potential for distributive policies shrank and the Uruguayan model fell into crisis. An increasingly unimaginative and unreconstructed political class could not respond to the new political challenges, promote economic diversification or counter social deprivation. Instead, the established politicians, under the pressure of protests by the organized left and the insurgent “Tupamaros” urban guerrilla movement gradually handed power over to the military and some technocrats associated with them between 1967 and 1973.

Uruguay’s bureaucratic-authoritarian military regime lasted from 1973 to 1985. It was both qualitatively and quantitatively more repressive and did more damage to Uruguayan society, human capital and elites than did the military regimes in Argentina or Chile. Moreover, it did not solve any of the problems that had served to justify its installation, and ended in failure and decline. A period of transition followed (1985 – 1989), beginning in 1984 with negotiations between military “softliners” and the moderates of the opposition, and ultimately leading to a gradual transfer of power back to civilian politicians. Initially, the military tried to exclude some of its most fervent opponents in the moderate leftist Broad Front (Frente Amplio) and in the Blancos around Wilson Ferreira Aldunate, but they soon lost control, and the dynamics of the democratic process took over. Democracy in Uruguay can be considered to have been consolidated since the early 1990s. Restoration characterized the first period of re-democratization: not only was the constitution of 1967 restored, but also the personnel, as well as the complicated electoral and party system, with all its limitations in the establishment of clear mandates and legitimacy (it was not reformed until 1996). The necessary reforms of state structure, public administration, the welfare state and the heavy public sector of the economy got off the ground only slowly, and were postponed.

Institutional democratization was achieved by means of broad consensus and cooperation, because neither President Julio María Sanguinetti (1985 – 1989) of the Colorado Party (whose faction had not collaborated with the military, as had much of the rest of the party) nor his successors could command a majority in parliament. Most military personnel retained their military posts. The crucial problem of the military’s culpability for human rights violations during the dictatorship was, after three years of intense conflict, technically solved to the

satisfaction of the military. The decision was also politically unequivocal; a statute of limitations was written into law (*ley de caducidad*) and approved by a clear majority in a referendum in 1989. Confrontation with the historical and moral problems involved was thus postponed. Since then, there have been four successful democratic transfers of power. The first, in 1990, put the Blancos' candidate, Luis Alberto Lacalle (1990 – 1995) in power, while the second, in 1995, returned Sanguinetti (1995 – 2000) to power. The third installed Jorge Batlle (2000 – 2005), another traditional Colorado politician (though from a different faction), this time with broader legitimacy thanks to the reformed electoral system. It was not until March 2005 that the first non-traditional (though experienced) candidate could assume the presidency: Tabaré Vázquez of the Frente Amplio, who was Batlle's strongest rival in 1999, and who won the elections of October 2004 in the first round with an unprecedented majority.

The two last years of the Batlle administration, despite his earlier achievement, were lost years for Uruguayan politics, characterized by inertia, parliamentary gridlock, isolation and a lack of imagination. By contrast, the four years of the Vázquez presidency, with its majority in parliament, have brought new dynamism and resolution into Uruguayan politics, even if the government has struggled at times to strike a balance between the liberal initiatives of its economic policy elites and the traditional (though moderate) interventionist demands of its more leftist clientele. Since 2005, the Vázquez administration has performed much better than expected. It has not been able to address all the problems of the country as scheduled, but on the whole it has achieved significant, in some cases structural reforms in a number of sectors (particularly health and social services, education, the tax system and public administration), in order to promote social justice, increase freedom of choice, and to make the state more effective and the economy more competitive.

While the transition to democracy in Uruguay was completed in less than a decade, the transformation of the economy, already begun under military rule, was more protracted. Here, the problems consisted in the need to modernize and diversify a traditional, dependent and crisis-ridden agricultural export economy; to deregulate the strong public sector and contain heavy state interference; and to reform the comprehensive but no longer affordable nor effective welfare state. At the same time, a new critical phenomenon had to be fought: growing misery and rapid impoverishment accelerated by military repression and excessive neo-liberal experimentation, which produced a 50% decline in real wages between 1970 and 1983. Despite stagflation, a high rate of capital flight and growing external debt, and despite the fact that Uruguay's economic transformation has been slowed by the country's particular corporatist traditions of seeking consensus, moderate and incremental solutions and limited risk (traditions which have provided a level of stability and inclusion unequalled in Latin America), significant progress was made between the mid-1980s and the late 1990s. Non-traditional exports were increased, debts periodically renegotiated, energy prices fell and many state-owned or state-controlled enterprises (*entes autónomos*) were deregulated and privatized despite persistent resistance voiced in referenda in 1992 and in December 2003. During most of the 1990s, economic growth rates hovered around 5%, and inflation and unemployment rates were contained at about 10% each.

Since the late 1990s, Uruguay has suffered the repercussions of the region's financial and debt crises. In 2002, Uruguay was thrown into deep recession. However, recovery began in 2003, and since then the Uruguayan economy has continuously improved its performance, even structurally (e.g., by diversifying industry and attracting new investments), although still within the limits allowed by the dependency of a small country with an open and dollarized economy on its weightier neighbors and the world markets.

## Transformation Status

### I. Democracy

#### 1 | Stateness

Uruguay has no stateness problems. The state has a monopoly on the use of force, and has no competitors.

Monopoly on the use of force

There is fundamental agreement on who qualifies as a citizen. All citizens have the same civic rights, and there is a fundamental acknowledgment of the constitution.

State identity

The state is defined as a secular order. Religious dogmas have no influence on politics or law. Church and state are separated. Uruguay was the first Latin American country to legalize homosexual marriage (as part of the law on “uniones concubinarias”) in December 2007, against fierce resistance of the Catholic Church. Legislation on abortion is more liberal than in most Latin American countries. A bill attempting to liberalize it even more was approved by the legislature in November 2008, but vetoed by President Vázquez.

No interference of religious dogmas

Uruguay has long-established differentiated administrative structures that are functional throughout the country, and capable of implementing political decisions and allocating resources. The administrative system is sufficiently efficient, though in some areas rather traditional and in need of reform. In recent years, the Vázquez administration has addressed the issue of state and administrative reform more thoroughly than did its predecessors.

Basic administration

#### 2 | Political Participation

Rulers are determined by general, free and fair elections. There is effective universal suffrage, and elections are carried out appropriately.

Free and fair elections

The democratically elected rulers have the effective power to govern; there are no veto powers or political enclaves.

Effective power to govern

There is unrestricted freedom of association and assembly within the basic

Association /

democratic order.

assembly rights

Citizens, organizations and the mass media can express opinions freely and without restrictions. The media is pluralistic. The press is privately owned, and some newspapers are still associated with political parties, although Uruguay's formerly lively scene, with its wide variety of high-quality party political presses, shrank under authoritarian rule. Radio and TV are both commercial and public.

Freedom of expression

### 3 | Rule of Law

There is a functioning system of checks and balances. The legislature, executive and judiciary operate independently of each other and mutually respect each other's prerogatives. There is a traditional tendency and often institutional pressure for government and parliament to find consensus. Government actions are subject to parliamentary and judicial review, and scandals usually come to light.

Separation of powers

The judiciary is traditionally independent, free from unconstitutional influence, differentiated and professionalized, although it may sometimes suffer from a lack of efficiency, particularly against organized crime, or slow procedures. There are mechanisms for judicial review of legislative and executive acts.

Independent judiciary

As a rule, corrupt officeholders are severely prosecuted under established laws. A spectacular case in 2007 was the indictment of a former director of the Municipal Casinos, a close party ally of presidential contender Danilo Astori.

Prosecution of office abuse

There are no restrictions on civil rights or impingement on human rights at present. However, human rights reports have criticized poor prison conditions. Government policies of non-discrimination have set high standards. Violence against women (mostly domestic) has continued to be a problem and is severely prosecuted. The Vázquez administration has also regained momentum in addressing the human rights violations and crimes of the past military regime, which had dwindled somewhat during the last years of the Batlle presidency. The government has increasingly insisted on due process of law against members of the authoritarian regime thought to be human rights violators. It has supported all possible cases of "exemption" from the 1989 statute of limitations law (ley de caducidad) that have been brought to court, and it has repealed earlier concessions of immunity for the military and the police. In February 2009, the government and both houses of parliament (Asamblea General), in responding to a particular query of the Supreme Court, each for the first time explicitly stated that they considered the statute of limitations law to be unconstitutional. Large swathes of the Frente Amplio have actively taken part in initiatives since 2007 calling for a referendum that would annul the statute of limitations. By spring 2009, these groups had nearly collected the number of signatures required to put the issue on the ballot. A number of former

Civil rights



military officials have been brought to court, and military officials living overseas have been extradited. In September 2007, the Appeals Court confirmed the 2006 convictions of former President Juan María Bordaberry and Foreign Minister Juan Carlos Blanco on charges of homicide associated with Bordaberry's authoritarian presidency (1973 – 1976). Former army chief and dictator Gregorio Conrado Álvarez was jailed in December 2007 for his part in the abduction, disappearance and death of political opponents during military rule. In March 2009, eight prominent members of the dictatorship were condemned to 20 or 25 years in prison for the killings of 28 Uruguayans in Argentina, marking a great step forward in terms of justice, and revealing, at the same time, the close collaboration between the Uruguayan and the Argentine dictatorship as a part of the so-called Operation Condor. A number of former police and military officers are in detention awaiting trial on similar charges.

#### 4 | Stability of Democratic Institutions

The democratic institutions work effectively and efficiently. As a rule, political decisions are prepared, made, implemented and reviewed in legitimate procedures by the appropriate authorities.

Performance of democratic institutions

Institutions are also accepted and supported by the relevant actors. There are neither significant semi-loyal or disloyal actors nor forces with veto powers. There is no indication of any putsch ambitions in the military.

Commitment to democratic institutions

#### 5 | Political and Social Integration

The Uruguayan party system is moderate and relatively stable. Both traditional parties, the Colorados (liberal and conservative) and the Blancos (conservative and liberal), and their various factions and elites (often families) have been deeply anchored in society for more than a century. Furthermore, the system was able to integrate a substantial newcomer in the 1970s, also deeply rooted in society: the moderate leftist Frente Amplio coalition (FA, later EP-FA). This party remained stable with around 20% of the vote between the early 1970s and late 1980s, has successfully governed the city of Montevideo since 1990, gained a greater majority in the mid-90s (31% in 1994), and has become the country's strongest political force since 1999. The integration of the former representatives of the underdogs, the excluded, the radicals and the ex-terrorists into the political system and the political class has been one of the greatest pacifying achievements of the Uruguayan transformation. In December 2002, the EP-FA concluded an alliance with the smaller left-liberal Nuevo Espacio (NE) of Senator Michelini, which finally secured its electoral victory in 2004. Traditionally dominated by Communists, ex-Tupamaro dissenters and various social democrats in the 1970s and 1980s, and later also by

Party system

Socialists (such as Tabaré Vázquez), the EP-FA has finally turned into a broad catch-all coalition, adding to its ranks moderate social democrats, liberals, human rights activists and even prominent representatives of the influential agricultural interest group Federación Rural, once a stronghold of the Blancos.

The level of fragmentation is low if we count the parties and not their traditional factions (*listas*), as is volatility, unless votes swing due to a disappointed public or there is a major gap in perception between the candidates and their programs, as was the case in the October 2004 elections. In these elections, President Batlle's Colorados lost more than 20 percentage points compared to the previous elections in 1999 (dropping from 31.5% to 10.4%) whereas the oppositional Frente Amplio and the Blancos who had left the coalition government a year before gained more than 12 points each (respectively climbing from 38.2% to 50.4% and from 21.1% to 34.3%). The 2004 elections produced a significant realignment, and have changed the Uruguayan party system. While the three parties each commanded roughly one-third of the vote before 2004, the broadened Frente Amplio coalition now represents about half of the electorate, with both traditional parties combined accounting for the other half. In addition, the Colorados have reached the lowest point in their history. The alternatives have become clearer, reflecting the social cleavages.

A major (and indeed a secular) improvement was put in place with the electoral reforms of 1996, which had been postponed during the transition. These reforms decisively helped to streamline the party system, reduce fragmentation, and to broaden in particular the basis of the president's legitimacy. In the old system, the voters voted for the presidential candidates of the various factions within the parties, and the ticket with the highest plurality within the party receiving a plurality of votes was deemed the winner, resulting in elected presidents who usually had just 15% to 20% of the total vote. The reforms introduced primaries and a run-off election between the two leading contenders (*ballotage*), which has contributed to more stable majorities and strengthened the government's mandate. In the first presidential elections conducted according to the new rules (1999), this system cost frontrunner Tabaré Vázquez of the Frente Amplio the victory, because most of the Blanco voters voted one last time for Colorado veteran Batlle in the run-off after their own candidate had been eliminated. In the run-off Batlle received 51.6% and Vázquez 44.0% of the vote. The Frente finally triumphed in the 2004 elections due to severe disillusionment with the Batlle government's disappointing record: the Colorado candidate Guillermo Stirling came in last (10.4%) behind the Blanco Jorge Larrañaga (34.3%). Tabaré Vázquez, backed by a broad coalition (EP-FA-NM), won the presidency in the first round (with 50.4% of the vote), and the Frente coalition even won absolute majorities (also a new phenomenon) in both houses of parliament, coming in first not only in Montevideo (61.5%) but on average also in the departments of the interior (43%).

Well-organized internal factionalism, often along personalistic and family lines, has

been a decisive characteristic of Uruguayan parties for more than a century, and remains so today. In early March 2009, about four months before the presidential primaries scheduled for June 28, surveys showed ex-President Luis Alberto Lacalle to have a small lead over competitor Jorge Larrañaga among National (Blanco) party primary voters; in the Colorado party, Pedro Bordaberry clearly led Luis Hierro. Within the Frente Amplio the situation is more complex, because this alliance of more than 20 sizeable groups with very different historical trajectories is more heterogeneous, the divisions between the various factions are more entrenched, and rivalries are more visible. The strongest faction of the FA is the leftist Movimiento de Participación Popular (MPP) led by ex-Tupamaro leader José (“el Pepe”) Mujica, one of the country’s most popular politicians; second come the Socialists and their allies (now called Espacio 90), while the more center-left Vertiente Artiguista (led by Enrique Rubio) and Asamblea Uruguay (led by Danilo Astori) can also each muster significant support. The influence of the Communist Party has receded, but can occasionally be felt; in December 2007, the communists blocked the election of MPP candidate Constanza Moreira, a respected political scientist, to the post of FA party president.

At the party congress of December 2008, more than two-thirds of the delegates voted for Mujica as presidential candidate, but the congress also gave four other contenders permission to present their candidacies in the primaries. At the time of this writing, two of these had stayed in the race. In March 2009, Mujica was far ahead in the polls, with second place going to Danilo Astori, a highly respected liberal economist and successful minister of finance in the Vázquez administration, who resigned in autumn 2008 in order to organize his presidential campaign. Third place was held by Marcos Carámbula, the governor of Canelones and a relative newcomer to national politics, who had more support within the party ranks than within the electorate at large. As reasons of age and health may prevent Mujica from running, he will have the decisive say in nominating the final candidate of the FA. An Astori/Mujica presidential formula (which has been recommended by incumbent President Vázquez for some time) would be the strongest ticket the Frente Amplio could put to the voters. With regard to the party system it should be noted that these complicated selection processes have been taking place in good institutional order, and in civilized forms which even provided room for manifestations of solidarity between the various party factions.

Uruguay has a long history of interest representation, organization and pressure group formation as well as of defining the legal framework, the rules and the (partly corporatist) mechanisms of interest intermediation. There is a close-knit network of differentiated interest groups that cooperate, reflect competing economic and social interests, and tend to balance one another. These groups also have close ties to the political parties and the relevant bureaucracies. The primary traditional groups include the Federación Rural farmers’ organization and some of its regional middle

Interest groups

and small-size rivals; a number of industrial and business associations, and particularly the Cámara de Industrias del Uruguay (CIU); influential professional associations; and the traditionally strong and well-organized labor unions which since 1964 have been coordinated in the Convención Nacional de Trabajadores (CNT, now PIT-CNT). Many of these have old traditions closely related to the early emergence of the Uruguayan welfare state. After a period of relative decline between 1992 and 2004, the unions have recovered significantly beginning in 2005, in part because the government has revitalized the tripartite mechanisms of (mostly sectoral) collective bargaining.

Support for democracy in Uruguay is the highest in Latin America (with the exception of Costa Rica), has been entrenched for many years, and does not essentially depend on the performance of the particular government, as is the case in many other Latin American countries. This support has remained high even in periods of heavy discontent and party realignment. According to Latinobarómetro data, support for democracy in Uruguay rose from 75% in 2007 to 79% in 2008, and is now back to where it was in 2001 and in the late 1990s. Satisfaction with the way democracy works in the country has also gone up to more than 70%, by far the highest score in Latin America (in contrast, the scores during the Batlle government in 2004 fell below 50%). The authoritarian potential has receded by four percentage points, from the usual 10% between the late 1990s and 2007 to an all-Latin American record low of only 6% in 2008. Democracy and democratic attitudes are secure and consolidated in Uruguay.

Consent to  
democratic norms

Uruguay has a strong civil society that has formed the backbone of its traditional democracy, contributed much to the resistance to military rule (which in turn prompted the military to resort to extraordinary acts of repression), and facilitated the relatively smooth transition and democratic consolidation. There is a close-knit web of autonomous, self-organized groups, associations and organizations, including well-organized groups that have protested against human rights violations in prisons, the military regime's violation of human rights, or against maladministration of justice. More recently formed groups represent those who have been marginalized by the two decades of deregulation, who have sunk into poverty and moved to the slums surrounding Montevideo. Levels of interpersonal trust (whatever the practical difficulties in their measurement) rose between 2004 and 2008, to the second-highest level in Latin America.

Associational  
activities

## II. Market Economy

### 6 | Level of Socioeconomic Development

Uruguay is not a typical “third world” country. Indicators reflect a decades-long structural decline from earlier “first world” prosperity with all its legacies: a relatively high level of development for the Latin American context, a more balanced income distribution, low regional disparities and a solid, if technically antiquated and often obsolete infrastructure. Data suggest that the decline hit bottom in the severe crisis of the early 2000s, and that since around 2005 a structural recovery has set in. In principle, the country’s level of development permits adequate freedom of choice for all citizens, and no significant parts of the population are fundamentally excluded from society due to poverty, gender, education, religion or ethnicity. The HDI has improved from the values of 0.833 in 2002 and 0.851 in 2004 to 0.859 in 2006 (rank 47 out of 179 countries). The GDI value in 2006 was 0.856, or 99.7% of its HDI value (ranking 37 out of 157 countries), and the Gender Empowerment Measure (GEM) at 0.542 (rank 66 out of 108 countries). The U.N. Education Index stands at 0.942, and the adult literacy rate is incrementally improving, standing between 97% and 100%. Poverty, though it remains relatively limited in comparative terms, has become a major problem since the waves of induced impoverishment that started in the 1970s and 1980s. This new phenomenon persisted and expanded during the recession of the late 1990s and early 2000s, and began to recede only after 2004. The HPI-1 value of 3.3% for Uruguay in 2006 ranks 7th among 135 developing countries, and 5.7% of the population lives on less than \$2 a day (1990 – 2005). The Gini coefficient indicates an increase in inequality between 1999 and 2003, with the value rising from 42.3 to 44.9 (preliminary value for 2006: 45.2).

Socioeconomic  
barriers

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	13686.4	17362.9	20022.7	<b>24253.8</b>
Growth of GDP	%	11.8	6.6	4.6	<b>7.6</b>
Inflation (CPI)	%	9.2	4.7	6.4	<b>8.1</b>
Unemployment	%	-	12.2	10.6	<b>9.2</b>

		2004	2005	2006	2007
Foreign direct investment	% of GDP	2.4	4.9	7.0	<b>3.6</b>
Export growth	%	30.4	16.3	2.7	<b>8.2</b>
Import growth	%	26.8	10.1	14.8	<b>6.7</b>
Current account balance	\$ mn.	3.1	42.3	-391.9	<b>-80.5</b>
Public debt	\$ mn.	7813.3	7779.2	8596.9	<b>9615.6</b>
External debt	\$ mn.	15159.7	14465.1	11189.9	<b>12362.6</b>
Total debt service	% of GNI	11.8	13.0	29.8	<b>6.2</b>
Cash surplus or deficit	% of GDP	-2.4	-1.5	-0.9	<b>-1.5</b>
Tax Revenue	% of GDP	17.8	17.9	18.6	<b>17.8</b>
Government consumption	% of GDP	11.0	10.9	11.2	<b>11.2</b>
Public expnd. on edu.	% of GDP	2.6	2.8	2.9	-
Public expnd. on health	% of GDP	3.6	3.4	3.6	-
R&D expenditure	% of GDP	-	-	0.4	-
Military expenditure	% of GDP	1.3	1.3	1.3	<b>1.2</b>

Sources: The World Bank, World Development Indicators 2009 | UNESCO Institute for Statistics | International Labour Organization, Key Indicators of the Labour Market Database | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security.

## 7 | Organization of the Market and Competition

The fundamental elements of a market economy and free competition are in place. Uruguay is by tradition an economically liberal country with corresponding institutions and guarantees, including those for the banking system, the capital market and foreign trade. One of the legacies of the 20th century, however, has been an entrenched tradition of state economic activities and state interventionism in a number of sectors (mostly infrastructure, energy and basic services) aimed at promoting development and securing the guarantees of the welfare state. Hence, the rules of the game have not always been consistent or uniform for all market participants. The process of deregulation, decentralization and privatization of state-owned or state-controlled enterprises began under the dictatorship. It has continued since, though at a slow pace, due to various crises and also to some reluctance on the part of politicians and voters. In a 2003 initiative (which also served as a rehearsal for the 2004 electoral coalition of the left with the strong support of the

Market-based  
competition

labor unions) and a subsequent referendum held in December 2003, 62% of voters rejected a 2002 law that permitted the state-owned fuel, alcohol and cement corporation ANCAP to form joint ventures with transnational companies. In October 2004, almost two-thirds (64.6%) of voters agreed that marketing of the country's water resources by privately owned companies should be barred by the constitution, and the majority voted a coalition into power that had campaigned against excessive privatization. However, there has been significant continuity in the Uruguayan governments' economic policies, and the Vázquez administration managed to strike a balance between the liberal convictions of Finance Minister Danilo Astori and some of the more interventionist demands of the leftist groups within the Frente Amplio. The government's current priorities include defining the functions and improving the performance of state-owned companies, and creating better mechanisms of coordination with the expanding private sector.

There is legislation regulating monopolies and oligopolies, but it has not been wholly consistent, leaving loopholes and failing to address the public and public/private sector. In July 2007, the Uruguayan government enacted the Trade Freedom and Free Competition Preservation Act (*Ley de Libertad de Comercio y Preservación de la Libre Competencia*) which entered into force in August, signaling a more consistent anti-monopoly policy in the future. The antitrust act repeals almost all previous regulations related to anti-competition matters and covers all persons (legal entities and individuals, public or private, national or foreign) except for the limitations established by law owing to reasons of general interest.

Anti-monopoly  
policy

Foreign trade has been continuously liberalized since the crisis of 2002. There is no more fundamental state intervention in free trade. It would be against the country's interests to intervene, with its buoyant exports and substantial import growth driven by large foreign direct investment projects. Among the ambitious projects are a second container terminal in Montevideo's expanding port, the extension and improvement of transport infrastructure (including the PLUNA airline), and a number of booming tax-free zones, around the new cellulose plants of Metsa-Botnia (Fray Bentos) and Ence (Punto Pereira), and elsewhere. The Zonamérica in Montevideo has particularly attracted software developers, logistics and communications companies, and other service industries. Due to the IMF-praised customs and tax reforms of the past four years, Uruguay has even attracted investment by cattle breeders from Argentina seeking to avoid Argentine export regulations and taxes. As a member of the Mercosur common market (Montevideo is the seat of the new Mercosur parliament) Uruguay has contributed to a number of initiatives aimed at enlarging and further integrating Latin America's free trade zones, but it has also struggled continuously (and mostly alone) against the common market's protectionist tariffs and mechanisms, which are not in the interest of the country's small and open economy. Instead, it has been pressing its partners to

Liberalization of  
foreign trade

account for economic asymmetries between the Mercosur economies and allow the smallest countries to sign separate bilateral free-trade agreements (FTA) with states outside Mercosur, particularly the United States. However, the partners' resistance (which has been intensified by the accession of Venezuela) and opposition from leftist sectors within Uruguay's governing party itself, have so far blocked negotiation of an FTA with the United States, and have slowed progress of the less-ambitious Trade and Investment Framework Agreement (TIFA) between the two countries, which was signed in January 2007.

Due to its location, political stability and liberal capitalist traditions, Uruguay has long been one of Latin America's principal financial centers. It has particularly attracted foreign capital and bank deposits from neighbors plagued by higher taxes and more intensive controls. The institutional foundations are in place for a solid banking system oriented towards international standards with functional banking supervision, minimum capital requirements and market discipline. Capital markets are open to domestic and foreign capital, and the mechanisms to cope with speculative investment have been significantly improved (and supported by substantial inflows of productive capital) in recent years. Reserve requirements have been increased, and the share of non-resident deposits, particularly from Argentina (a classical factor of vulnerability), has been reduced. Some state banks have been restructured (including the Banco Hipotecario del Uruguay (BHU), a housing bank), the supervisory framework has been strengthened, and various measures for further increasing the autonomy and the interventionist capabilities of the central bank are under way. Indicators show a well-capitalized banking system with high levels of international reserves and liquidity, and low non-performing loan ratios, though bank profitability declined somewhat in 2008. Standard & Poor's upgraded Uruguay from B+ to BB- in mid-2008. During the severe financial crisis that hit the Southern Cone region between 2001 and 2003, the Uruguayan banking system almost collapsed due to a crisis of liquidity, lack of supervision, fraud, corruption, and above all its high dependency on outside factors; it lost its investment grade ranking and was saved only at the cost of dramatically increased foreign debt levels. Its continuous recovery since that time has been facilitated not only by the good performance of macroeconomic indicators and the country's high level of attractiveness for investments, but by steady (though in the end slowly implemented) policies of structural reform.

Banking system

## 8 | Currency and Price Stability

Inflationary pressures have persisted since the end of the regional crisis (with inflation rates reaching almost 20% even in 2003) and inflation has slightly gone up from its low point of 4.7% in 2005, reaching 6.4% in 2006, 8.1% in 2007, and around 8% in 2008. However, the anti-inflation and exchange rate policies of the

Anti-inflation /  
forex policy



central bank and the government have been significantly improved in recent years. They have been consistent and in concert with other goals of economic policy. The autonomy and the monitoring and adjustment capabilities of the central bank have been further strengthened; the bank's monetary policy committee has, from September 2007 on, increasingly used regular monthly interest rate management as a key steering tool, in addition to a targeted money supply and reserve requirements. Financial prudential norms and supervision have been improved. The exchange-rate peg has been abandoned for a free float. The dollarization of the banking system has declined, but is still high. Intensified capital inflows triggered an appreciation of the currency which the central bank tried to contain until mid-2008, when the global financial crisis reduced the inflows and the exchange rate began depreciating again. When inflation in 2007 exceeded targets, the government implemented additional tax administrative measures aimed at securing more price stability, a mix that so far has been welcomed by the IMF. While the central bank continues to steer a restrictive course in monetary policy, interventionist fiscal measures appear likely to be increased in order to curb the more recent inflationary pressures which have been triggered since late 2008 by rising food (in particular wheat) and fuel prices, expanding domestic demand, and wage increases. The government has declared the reduction of food prices and control of food speculation to be one of its top priorities for 2009.

Uruguay's fiscal and debt policies have been directed towards the support of macroeconomic stability, and performed significantly better during the period under review than in the previous years. This fact was equally due to better economic performance and to the implementation of at least some planned and long-overdue policy reforms. In this sense, the tax reform of July 2007 was a landmark. It simplified the tax system in many ways and finally introduced a personal income tax, which had been demanded by the FA for some time. Even if some of its provisions (thresholds, percentages) were modified under pressure from middle-class interests, the tax reform and parallel tax administration and customs reforms have helped improve the efficiency of tax collection and streamline the respective agencies. Public revenues went up in 2007 (reaching 33.8% of GDP) and showed little substantial change by the end of 2008, staying in line with expenditures. The reduction of public sector debt continued in 2007 and 2008. While it had amounted to over or around 100% of GDP in the years after the Southern Cone crisis (2003 – 2004), it dropped from 2005's level of 75% to 62% in 2007 and 58% in 2008. Before the global financial crisis began to affect Uruguay at the end of 2008, a further decline to 53% was predicted for 2009; spending on public debt was targeted to fall to 22% of public expenditure in this year (this figure was 34% in 2004).

Due to continued and in 2008 even extraordinary macroeconomic growth (8.9%), high earnings from a diversified export sector, strong foreign direct investment

Macrostability

inflows and rising tax revenues Uruguay has also been able to reduce its external debt and debt service loads. Along the lines of the previous, post-crisis general debt restructuring in 2003, as well as its own renegotiation policies of 2005 and 2006, the Vázquez administration continued to reduce short-term debt through adequate debt management operations during the review period. The 2007 IMF review under the 2005 – 2006 Stand-By Arrangement stated that the government’s policies were paving the way for Uruguay’s exit from IMF financial support. The 2008 report noted that the government’s prudent macroeconomic policies and deep-rooted structural reforms have enabled Uruguay to significantly reduce vulnerability, improve its debt profile and to contain the effects of the recent turmoil in global financial markets, even though the economy’s still-high level of dollarization presented a risk and fiscal policy had been somewhat expansionary. Public spending indeed rose in 2008, basically for human resources, social and sustainability programs, infrastructure expansion and the promotion of productive investment, and it may continue to do so in the electoral year 2009. However, the Vázquez administration’s economic team, led by finance ministers Danilo Astori and Álvaro García (after September 2008), has so far managed to keep the modest budget deficit (between 0.5% and 1.5% of GDP) within target range.

## 9 | Private Property

Uruguay has a liberal capitalist tradition; property rights and the rules regulating the acquisition, benefits, use and sale of property are well-defined and usually safeguarded. Potential restrictions like temporary measures aimed at fighting systemic crises (as in 2002) or crime are strictly regulated by law. In line with the government’s explicit policy to attract and promote private investment, legal protection for investors has continued to improve during the last years, as have incentives.

Property rights

Private enterprises are the norm, and the privatization of state enterprises has progressed since the 1980s, mostly for financial reasons. One of the most spectacular recent cases was the sale of the PLUNA state airline in 2002. However, a significant state sector remains. Privatization has slowed since the Southern Cone crisis, partly due to economic circumstances, but also in line with the corporatist traditions of the country. Citizens, with good reason, have shown clear reluctance to go too far in privatization, particularly in areas such as basic services and utilities, as the outcome of the referenda on water and ANCAP (a state-owned company involved in the production of petroleum products, among other things) in 2003 and 2004 demonstrated. The majority of the political elites, including the governing Frente Amplio, have followed a similar course. In recent years the government has been highly successful in its intensified strategies and campaigns to attract foreign private and corporate investment. It has also been flexible with regard to business

Private enterprise

design and the particular forms of cooperation. In many cases, new forms of bi- or multinational public/private ventures have appeared to best serve everybody's interests. When launching a large \$400 million transport-infrastructure development program in October 2008, the government even managed to convince skeptics within its own party of the need to promote private sector participation in infrastructure development, and for a concessions model aimed at boosting competitiveness in public works. The creation of a public-private integration institute to facilitate initiatives and coordination between the two sectors is being debated. Bigger cooperative projects may develop in the hydrocarbons exploration and production sector, in order to exploit the substantial offshore natural gas (perhaps also oil) reserves of an estimated 85 billion cubic meters in the Punta del Este and Pelota Basins that have been discovered recently and are expected to provide a potential for exporting between 7 and 8 million cubic meters of natural gas per day. In December 2008, the government and ANCAP launched the "Uruguay Round 2009," calling for bids (due by 1 July 2009) for exploration and production contracts for the 11 prospected areas. Already, most of the usual transnational corporations operating in this sector have voiced interest. The general idea is that the exploiting firms and ANCAP will share profits.

## 10 | Welfare Regime

In this field substantial progress has been made in recent years, firstly because the extension and improvement of social services was a high priority for the government, and secondly because the performance of the economy permitted a substantial internal restructuring of government expenditure. Between 2004 and 2009 the share of social expenditure in the government's budget rose from 35.7% to 49.1%. Uruguay had long been a traditional bureaucratic welfare state based on distribution at a very high level, built along European lines, but for decades it had no longer been able to deliver, and the claims of the insured had been devalued. When the Vázquez administration came into office in 2005, the Uruguayan welfare state was in plain crisis, though it still displayed Latin America's highest level of spending on social protection (more than 20% of GDP as compared to an average of about 5%). Like all traditional systems of social provision, it needed comprehensive reform and restructuring as a result of demographic change (Uruguay's population has the highest average age of any in Latin America) and rising emigration rates among younger people, significant unemployment oscillating between 10% and 15% (2003 – 2006), an extended informal sector of an estimated 40% of the labor force (2003), and the need for more efficiency and equity. Social security, unemployment and health insurance were in particular need of restructuring, and substantial cuts had to be made in the early retirement, pensions and benefit schemes of an overstaffed and privileged, though neither highly professionalized nor efficient civil service (with strong unions). By December 2008, some of these

Social safety nets

parameters had significantly changed. More than 150,000 new jobs had been created during the Vázquez administration's tenure. Unemployment had fallen to a record low below 7% (in Montevideo below 6%), formal employment had gone up (by 25% in the private sector alone between 2004 and 2007, most of it in construction, industry and trade) reaching a record high of 57% in 2007, wages had increased, and the poverty rate had fallen continuously. Though most of this change was due to the economy's improved performance (and the government's cautious economic and financial policies supporting this trend), it was also backed up and secured by the Frente Amplio government's social policy reforms, which occurred in two waves.

In its first two years, the administration implemented many urgent and occasionally inconsistent ad-hoc measures such as reducing public health costs and cutting many benefits, while further subsidizing the deficit of the Banco de Previsión Social budget (without structural modifications). However, it also launched a two-year emergency plan targeting poverty (PANES), and allocated extra funds with a focus on food, health, family benefits for the unemployed and poor, and education in problem areas. The plan made use of available resources, particularly in the health sector, and combined the traditional mechanisms of unemployment insurance and welfare benefits for the needy with new requirements of the "workfare" type. In 2007 PANES was succeeded by a more ambitious, comprehensive and extended social and welfare scheme (Plan de Equidad), addressing all sectors involved including social security, family benefit payments, social assistance for the elderly and disabled, anti-poverty programs (including food stamps), unemployment and education. In particular, child benefit payments (asignaciones familiares) were increased and substantially extended, encompassing most minors under age 18 (around 700,000 in total in 2009). New, comprehensive health-care reform legislation came into effect in January 2008. In addition to extending the number of beneficiaries (including, among others, almost 400,000 children in 2008 alone), it established an integrated national health system (Sistema Nacional Integrado de Salud, SNIS), creating a fund to provide health care for pensioners and people in formal employment which will be financed by contributions from the state, private employers (5% of payroll) and employees (3% – 6%), and is designed to pay private and public health care providers (like the health maintenance organizations (HMOs) in the United States) according to a differentiated scheme. The reforms of the various (widely autonomous) agencies administering the social security schemes for the different sectors of the employed population (cajas) have not yet been finished nor coordinated. Nor has the structural problem of pensions and benefits for the state civil servants, the military and the police been systematically addressed; the budget for 2009 suggests that their wages and pensions will be raised to levels seen prior to the Southern Cone crisis.

Equality of opportunity exists in principle, and its level has somewhat improved in recent years, after a long period of deterioration in which marginality and poverty reached critical dimensions. There are a number of institutions, traditional and new, designed to compensate for gross social differences, and the Vázquez government's emergency programs have intensified their numbers and activities. Women have equal access to education, public office, and other public goods. In 2005, the ratio of women's to men's adult and youth literacy rates was 1.01, and the ratios of female to male enrollment in primary, secondary and tertiary education were respectively 0.98, 1.16 and 2.03. The ratio of estimated female to male earned income in 2005 was 0.55, a figure that has not changed substantially in recent years. The GDI value in 2006 was 0.856, the GDI/HDI ratio 99.6% (putting Uruguay at 37th place of 157 countries), and the gender empowerment measure (GEM) was 0.542 (putting the country at 66th place of 108 countries). Unemployment rates among men were 8% in 2006, as compared to 14% among women. In January 2009 total unemployment in Montevideo jumped from 5.9% (in December 2008) to 8.4%, but unemployment among women rose from 7.6% to 11.1%.

Equal opportunity

## 11 | Economic Performance

During the review period the Uruguayan economy, given the size and the problems faced by the country, performed extraordinarily well, certainly in comparison to the years of crisis after 2002, but also compared to the preceding two years of the Vázquez administration, when rapid recovery had already set in. The GDP continued to grow, from a respective 6.6% and 7% in 2005 and 2006 to 7.4% in 2007 and an impressive 8.9% in 2008. Unemployment declined, from around 12% and 11% respectively in 2005 and 2006 to 10.3% in 2007 and 9.8% in 2008. In December 2008 it reached a low of less than 7%. Wages have gone up. The trade balance was moderately negative due to the high rate of imported capital goods, but the service balance was positive at an even higher level. Public and foreign debts have been significantly reduced; the debt service ratio (as a percent of exports of goods and services) fell from 92.5% in 2006 to 25.0% in 2007 and 16.5% in 2008. Tax revenue has risen, and though the budget was not balanced, it fell within target range, with deficits under control. Gross capital formation has risen steadily. On the whole the government's explicit strategy of attracting private and foreign direct investment has been successful: FDI has gone up, particularly in 2006 and 2007, but is still much under the medium-range sustainability threshold of 20% of GDP and may not continue at the same pace in 2009. The total of public and private investment rose by 30% in the first half of 2008. The only indicator that has not been improved is inflation: This rose from 4.7% in 2005 and 6.4% in 2006 to 8.1% in 2007 and between 7% and 8% in 2008.

Output strength

## 12 | Sustainability

Environmentally compatible growth has been taken into account in important portions of economic life. Environmental concerns are effectively addressed in many sectors that depend upon them, such as modern stockbreeding, wine production, tourism, water and sanitation, rural development and irrigation. Environmental awareness has made some progress lately in the public discourse and in some of the government's programmatic and planning statements. But on the whole, ecological concerns tend to be subordinated to efforts to promote growth, attract foreign investment, and diversify and modernize production, which still are considered to be the principal economic goals. Rural out-migration, poverty and the extension of slum settlements around Montevideo have also limited the chances for environmental improvement. Long delays in modernizing a number of key state enterprises in the energy sector by means of public/private partnership also frustrated environmentalists; here some change took place in 2008 when state-owned electric power company UTE launched the first of a number of projected renewable energy joint ventures (partly with Spanish investors), among them a wind park. The national development agency (CND), with the support of the World Bank, has initiated a program to improve energy efficiency in both the public and private sectors. A key issue of transnational environmental conflict, from 2005 on, has been the construction of a pulp mill by Finnish investor Metsa-Botnia on the Uruguay river near Fray Bentos, on the border with Argentina, which has prompted violent protests and border blockades by Argentine and international environmental activists. Both sides have appealed more than once to the International Court of Justice, inflammatory rhetoric flared, and a full-fledged conflict between the two countries ultimately developed. However, the dispute has been contained by recent, intensive communication and cooperation between the two governments on a number of other issues, changes in personnel, and Uruguay's decision not to build a second cellulose plant (operated by ENCE, a Spanish company) at the same site as originally planned, but at Punto Pereira on the Rio de la Plata, which will not face the same type of Argentine resistance. In March 2009, President Vázquez proposed the creation of a fund to manage the effects of climate change, which would be supported by all groups of society. The future exploitation of the rich offshore natural gas reserves near Punta del Este from 2010 on will present another opportunity for testing the political weight of ecological awareness.

Modern infrastructure exists in principle, but needs modernization despite significant recent progress in a number of fields, particularly primary and secondary education. In these sectors solid and differentiated institutions exist, but had suffered severely from budget cuts, lack of discipline and reduced efficiency in the decades before 2005. The Vázquez years, in contrast, have been characterized by a strong expansion of educational investment. Between 2004 and 2009, public

Environmental  
policy

Education policy /  
R&D

spending on education almost doubled (from 16.6 billion to 30 billion pesos at constant prices) and is expected to amount to 4.5% of GDP in 2009. In this year, Uruguay will be the first country in the world to provide a personal laptop for every child in school (Plan Ceibal). Infrastructural, anti-poverty, social and educational policies for children will be further coordinated and extended within the framework of the ambitious and demanding 2010 – 2030 national strategy for childhood and adolescence (ENIA), which was launched in 2008. The traditional, still overwhelmingly public tertiary sector is underfunded and lacks sufficiently professionalized M.A. and Ph.D. programs in many areas, and is not yet internationally competitive despite some recent progress. This is particularly true for the institutions of advanced studies and R&D, where the impact of the catastrophic scientific brain drain triggered by the military regime is still being felt. However, the development of new curricula, individual reforms and a debate over the needs and shape of educational reform have begun to bear fruit. Competition from private universities is being felt. According to the UNDP, public expenditure on education in 2002 – 2005 was 2.6% of GDP (or 7.9% of total expenditure). One of the weakest points of Uruguayan policy performance is a very low R&D expenditure, totaling less than 0.3% of GDP between 2000 and 2005.

## Transformation Management

### I. Level of Difficulty

On the whole, structural constraints on governance are moderate to low in Uruguay, at least in comparison to the rest of Latin America, or even the rest of the world. The country is small, homogeneous, Western, and rich in agricultural resources. It possesses all critical institutions, and has a long institutional and behavioral tradition of democracy and socially responsible market economy. There are no stateness problems, the level of education is relatively high and civil society is strong. The only structural constraints result from the country's small size, its severe losses of human capital under military rule, its still-high debt, its extreme dependence on foreign capital and markets, and on the economic performance of its larger neighbors and the global economy. Thus, room to maneuver often has been narrow, particularly during the 2002 – 2003 recession and financial crisis and their aftermath. Since that time, the country has recovered substantially, but is still structurally vulnerable.

Structural  
constraints

As has been stated above in more detail, Uruguay has strong, differentiated and long institutionalized civil society traditions, and a developed participatory civic culture which has been conducive to democracy and long periods of social peace. However, trust in institutions and social trust have suffered due to the perceived processes of rapid downward mobility, marginalization and impoverishment (even among segments of the middle classes) as a consequence of dictatorship, neoliberal reforms, unemployment, and the economic and financial crisis.

Civil society  
traditions

There are no significant ethnic or religious cleavages and conflicts. Social cleavages and conflicts between capital and labor, and between the “ins” and “outs” of power and society, have been increasing since the days of military rule, and eventually led to political polarization. For a long time these cleavages have been represented by the division between the traditional Colorado and Blanco Parties, speaking for the “ins” and the establishment, and the Frente Amplio coalition, giving voice to the “outs” or underdogs. This has changed somewhat due to the fact that the Frente has been governing the country since 2005. However, even before this time, cleavages have never been completely irreconcilable, often depending rather on the country's economic and political performance.

Conflict intensity



## II. Management Performance

### 14 | Steering Capability

Uruguay's political leadership has shown itself to be committed to constitutional democracy and a socially responsible market economy. Moreover, it has been determined to secure and improve both by means of substantial, well-designed policies of reform which have given these goals priority over short-term expediency. The Vázquez administration has managed to organize broad support for its priorities, focusing on more social responsibility, a war on poverty, a more active state role promoting the economy and public-private partnership programs, as alongside (often controversial) tax, social, health, educational and administrative reforms. It helped that the president was able to establish cabinet discipline and to organize cooperation, for a crucial time, between the influential spokesmen of the liberal and the leftist sectors of the Frente Amplio, Danilo Astori and José Mujica, thus holding the heterogeneous coalition together. In March 2008 he changed half his ministers, making the cabinet slightly more centrist, but no less determined. To date the government's esprit de corps and the devotion of its members to implementing agreed-upon policies have appeared to be extraordinary, particularly when compared to earlier Uruguayan governments.

Prioritization

The government has implemented many of its reforms effectively. Legislation on a great number of important issues has been passed during the last years, among them controversial reforms affecting tax and health, social security, education and financial institutions, along with many schemes and programs for deregulation, empowerment and social assistance. A number of pilot public-private partnership operations have been launched, focusing on infrastructure development, communications, port operation and transportation services, among others. However, the government has not been able to implement all reforms effectively, due to the necessity of compromise between the coalition's different sectors, particularly the more liberal factions on one side, and the MPP, the Socialists and the unions on the other. Thus, many important aspects of the highly contested state bureaucracy reform (reforma del estado) have been debated and postponed, as has the overhaul of the pension plans for state employees, the police, the military and the employees of the banking sector; the final charter of the central bank; and the question of autonomy for educational institutions. In addition, noticeable gridlock has been produced by the government's need to work through the unreconstructed administrative and bureaucratic structures, for which the hands-on presidential office and the efficient planning and budgeting office (OPP) have served only in part as substitutes.

Implementation

The political leadership's capabilities with respect to policy innovation and complex learning have, on the whole, improved considerably compared to earlier governments. Issues are in general debated openly, arguments exchanged and listened to, and political leaders usually have little problem revising their positions in the light of new information. Where needed, experts are consulted or further research commissioned. In cases of deeply engrained interests or ideological positions revision may take longer, but there have been such cases in which policy has been redirected or compromise reached, at least on the part of the government and its parliamentary supporters. One very personal exception occurred in November 2008 when parliament passed a law liberalizing abortion. President Vázquez, whose opposition to this measure had long been known, vetoed it and even unexpectedly left the Socialist Party that had supported the bill.

Policy learning

## 15 | Resource Efficiency

In the last two years, the use of available economic and human resources by the government has continued to improve, though still more incrementally than categorically. Many of the earlier administrations' poor practices have been abolished or contained, but significant structural problems remain. The quality, efficiency and effectiveness of public administration have so far been improved only in some sectors; it is still overstaffed, and personnel costs are too high, though they have shrunk. The longstanding practice of hiring short-term employees (asesores) instead of permanent civil servants has declined since 2006. More government agencies than previously are now lobbying for competitive recruiting procedures, against the opposition of entrenched interests. Some agencies have also been restructured by sectoral reform legislation (on taxes, health, social security, education and the like). The modest budget deficit usually has remained within target range and is under control, and the country's debt level has been significantly reduced. Budget transparency has been further improved, as have auditing (SEV) and oversight (SIIF) functions in more areas of public administration than before. Mechanisms of coordination and control have been strengthened by the efficient planning and budgeting office (OPP), led by Enrique Rubio. This agency has also taken an important role (and become a modest think tank) in planning the reform, modernization and rationalization of the public administration. In contrast, the slow and traditional bureaucracy set up by Sanguinetti in 1995 in order to prepare for the "Reforma del Estado," which produced unsatisfactory results, seems to have lost influence. Plans for decentralization have not advanced much (and may not be as vital in a small country as they are in Bolivia or Brazil), but they have been increasingly operationalized and figure prominently on the government agenda for the years to come.

Efficient use of assets

The government's capability to coordinate conflicting interests and objectives into coherent policy has continued to improve significantly during the last two years. Even in the previous years, President Vázquez exercised leadership with more resolve than had his predecessor Batlle. As time has passed, almost all political actors in the government camp and in the important institutions have become accustomed to the necessity for coordination. Conflicts within the government have been reduced, while friction, redundancies and lacunae have become less significant. What still remains is the difficult and often time-consuming task of mediating between and balancing the governing coalition's various factions and groups, particularly the administrative and professional elites, who are mostly liberal with a leftist tendency, and the MPP, the Socialists and the labor unions of the PIT-CNT. Thus, some issues have not yet been settled, and a number of reform projects have had to be postponed or have been implemented only in the parts the various groups involved could agree upon.

Policy  
coordination

The government continued to fight and successfully curb corruption throughout the period under review. Most of the traditional and new integrity mechanisms have functioned, and scandals have been reported. The passage of anti-drug legislation strengthened anti-corruption measures, as did the 1998 Transparency Law's (Ley Cristal) creation of a Financial Investigations Unit and criminalization of a broad range of abuses of power by officeholders (including money laundering). The Dirección General Impositiva (DGI) has successfully fought tax and fiscal evasion and corruption under the leadership of the energetic Eduardo Zaindestat, one of the few top officials of the Batlle administration kept aboard by Vázquez (until 2007). Public officials are subject to financial disclosure laws. Sworn financial statements are required from all public servants, including the president, and the government requires all its agencies to produce regular public reports. A political-party financing law, passed in March 2009, sets clear standards of transparency and sets a limit on private donations to political parties which also receive state money to fund election campaigns.

Anti-corruption  
policy

## 16 | Consensus-Building

All significant political actors in Uruguay have agreed since 1985 that building and extending a market-based democracy are overriding goals. A high capacity for consensus has been a particular asset of the Uruguayan political system and civil society for a century. Its traditional democracy always has tended toward consensus or consociational democracy, with a number of corporatist arrangements. Moderation, compromise, a generalized capacity to form coalitions and the search for consensus on (often incremental) reformist projects have characterized the course of traditional Uruguayan politics. Most presidents have appointed members of various parties and factions, including the opposition, to the cabinet or other high

Consensus on goals

office (from which these figures usually resign shortly before the subsequent elections). The integration of the civilized left, represented by the new Frente Amplio, into this broad reformist consensus has been one of the major achievements of Uruguay's transformation since the 1980s, though this took time.

Not even the more accentuated marginalization and social polarization of recent decades (particularly since the Southern Cone crisis), and the subsequent party realignment before and during the 2004 elections, have substantially affected this basic consensus. When the Batlle government, inspired by neoliberal ideas or suggestions from the IMF, eventually tried to break out of the established consensus, a consensus-seeking political society either ignored the administration's proposals or voted them down (e.g., the plans to privatize basic services and energy, deep cuts in the social and health sector, efforts to terminate debate on the crimes of the military regime, or efforts to ally too closely with the United States). The more cautious approach of the Vázquez government has on the whole been more successful, notwithstanding a few similar experiences of containment or resistance (often from within the government's own ranks). These instances have included the proposed closer trade alliance with the United States (and in particular, the idea of a free trade area), and the thresholds included in the new personal income tax, on both of which the government ultimately gave way.

There are no significant anti-democratic veto actors in Uruguay. Reformers usually can co-opt most of their democratic competitors by pursuing slightly different strategies and priorities.

Anti-democratic  
veto actors

The political leadership generally succeeds in managing political cleavages so that they do not escalate into irreconcilable conflicts; social conflicts have not to date become irreconcilable in Uruguay. In fact, the Vázquez government has done much better than its predecessor in moderating its demands and programs, mediating between divergent interests, broadening its coalition, addressing and avoiding the dangers of polarization, and building bridges within and beyond the government coalition.

Cleavage /  
conflict  
management

In general, political leadership in Uruguay must assign a key role to civil society actors in deliberating and determining policies. Civil society traditions have been deeply entrenched for nearly a century in Uruguayan politics, political parties, factions and interest organizations. Neither repressive military rule nor weak or inconsistent leadership by democratic politicians has been able to substantially damage them. In addition, the history and programmatic orientation of the various factions of the Frente Amplio and the government has convinced them of the necessity of broad civil society involvement, and they have tried to further encourage, promote and institutionalize participation in many ways.

Civil society  
participation

The Vázquez administration has regained momentum in addressing the human rights violations and crimes of the past authoritarian regime, which had somewhat dwindled during the Batlle presidency's last years. It has also had to respond to the pressing debates on historical memory and "justice," and political and moral responsibility, which have increasingly come up since 2005. As the question of punishing military regime functionaries had first been technically "solved" by way of a statute of limitations (ley de caducidad) approved in a 1989 referendum, and all related historical, political and moral questions had been postponed, the issue was naturally bound to resurface again, and even more vehemently. When it did, the debate was characterized by the fact that many of the human rights, victims' and civil society groups concerned insisted on the priority (at least in terms of sequencing) of "justice" and the establishment of a culture of historical memory over "reconciliation." The frictions this eventually produced, even within the government's camp, have so far been cautiously moderated by the president and the Frente leaders, and consensus seems to be growing. The government also has increasingly insisted on applying a due process of law to perpetrators of abuses during the authoritarian regime. From 2005 on, it has supported all possible cases of exemption from the statute of limitations law as they were brought to the courts. In February 2008, it repealed earlier concessions of immunity for the military and the police. In February 2009, the government and both houses of parliament (Asamblea General), in responding to a particular query of the Supreme Court, stated explicitly for the first time that they each considered the statute of limitations law to be unconstitutional. However, the parliament has so far been reluctant to repeal the law, a position still in line with the tactical orientation of the Frente Amplio's 2004 electoral program. But since 2007, the Frente party congress has supported and large sectors of the party have actively taken part in initiatives calling for a referendum voting on annulment of the statute of limitations law. By spring 2009, these groups had collected nearly the number of signatures required to succeed.

Reconciliation

## 17 | International Cooperation

Uruguay is a small, dependent, risk-prone and indebted country with an open and highly dollarized economy. As such, it must closely cooperate with international financial institutions, bilateral donors, and public and private investors. There is broad consensus on this among political elites, even if opinions may differ in nuance. Uruguayan political leadership has made well-focused use of international assistance, applying it to the country's economic and structural transformation, the domestic policy agenda, infrastructural and educational programs, the fight against poverty, and the promotion of research and development. The Vázquez administration, in particular, has intensified and systematized the search for joint ventures and projects, and has improved mechanisms of consultation and

Effective use of support

coordination. Thanks to a strong macroeconomic performance, the government has also been able to increase the number of decisions in which it could set its own priorities.

During the review period, the international community considered the government to be a credible and reliable partner. The country's good standing has been maintained by a sequence of governments since the 1980s, and is tied particularly to the fact that Uruguay, in contrast to Argentina, has avoided default and bankruptcy and always succeeded in cautiously renegotiating its debts in time, even under the pressures of severe crisis (such as between 2002 and 2004). Due to the country's good economic performance and its ability to implement structural reforms in line with international requirements and expectations, the Vázquez government, was able to attract significantly more foreign investment and partners for joint ventures. In March 2009 the World Bank considered Uruguay to be one of the region's best-prepared countries in facing the international financial crisis. Standard & Poor's upgraded Uruguayan bonds in mid-2008 from B+ to BB-.

Credibility

Uruguay's political leadership has continually demonstrated a willingness to cooperate with neighboring countries in regional and international organizations. It has successfully built and expanded as many cooperative international relationships as possible, and promoted regional and international integration. Uruguay is a member of the Union of South American Nations (UNASUR) community, and more importantly, of the Mercosur common market. It has held this group's presidency, contributed to its organization and infrastructure, and recently starting hosting the group's parliament. Uruguay has also promoted free trade agreements with Mexico, Peru and the Andean Community, and has supported plans for a Latin American customs union, better currency coordination, and more openness, often in a push-and-pull alliance with Brazil. It joined the Banco del Sur soon after this organization's foundation in 2008. Efforts by the Batlle and Vázquez governments to achieve a free trade agreement (FTA) with the United States provoked domestic opposition and resistance from the country's Mercosur partners, so that in the end only a watered-down Trade and Investment Framework Agreement (TIFA) between the two countries could be signed in January 2007. During the last two years, President Vázquez has been particularly outspoken in his criticism of the common market's protectionist tariffs and mechanisms which work against the interests of the country's small and open economy. He has asked Mercosur partners to take economic asymmetries between economies into account, allowing the smallest countries to sign separate bilateral free-trade agreements with outside states, but so far in vain. By contrast, the de-escalation of the conflict between Uruguay and Argentina over the construction of two pulp mills and cellulose plants (which are among the biggest private investments in the country) on the Uruguay River near Fray Bentos on the border represents a significant achievement. The conflict had escalated in recent years due to violent protests on the Argentine side, dueling legal

Regional  
cooperation

actions and a lack of sufficient crisis management on both sides. What helped to contain it was the replacement of Uruguay's Foreign Minister Reinaldo Gargano by the more diplomatic Gonzalo Fernández in March 2008, and the decision to build the second plant at a different location, in Punto Pereira on the La Plata River. More recently, cooperation between the two countries has strengthened again in a number of sectors, such as fighting the illegal drug trade and consumption, and in an agreement to construct a liquid natural-gas conversion plant in Uruguay. Argentine investment in Uruguayan agriculture and stock farming has also gone up substantially.

## Strategic Outlook

In 2009 and 2010, Uruguayan politics will be dominated by intensifying efforts to cope with the repercussions of the worldwide financial crisis, and by the upcoming elections in June (primaries) and October 2009 (national) and in May 2010 (departmental). With regard to the financial crisis the country appears to be in a relatively good position. Many experts, including the World Bank, have assessed Uruguay as being one of the region's best prepared countries. A strong economic performance and recent structural reforms have given the country solid, well-capitalized and well-monitored financial institutions with high levels of international reserves and liquidity. Vulnerability has been significantly reduced. Due to continuous growth, rising export earnings and tax revenues, and strong foreign investment inflows Uruguay has been able to reduce its public and foreign debts substantially. Careful debt management continued even after the crisis began to take hold: In March 2009, half of the country's \$400 million debt to Corporación Andina de Fomento was paid off, with complete retirement of the debt announced for mid-year. At the same time, the government issued and sold new bonds totaling \$300 million. Public, private and foreign direct investment levels have risen, creating more than 150,000 jobs, in great part due to government campaigns and incentives offered to investors. Even if the pace of foreign investment slows under the impact of the international financial crisis, there are a number of big projects in the pipeline which might be able to compensate for decline in other fields, including the construction of a second pulp mill at Punto Pereira and a liquid natural gas conversion plant, the public/private joint venture projects of the new transportation infrastructure development program (e.g., port extension, modernization of the railway system, highways), and the substantial ventures that will be generated by the "Uruguay Round 2009," aimed at exploitation of the offshore natural-gas reserves near Punta del Este.

Yet despite all its achievements, Uruguay's economy is still vulnerable, not only structurally (with reference to its size, its dependency on the performance of neighbors and foreign markets, and its high dollarization), but also with regard to the impact of the international crisis. A recent boost in cellulose and paper exports can still be felt, prompted by the opening of the Metsa-Botnia pulp mill, and Uruguay's expanding software development industry is still in good shape. But the early months of 2009 saw declines in exports, especially in the dairy and textile sectors, and in manufacturing, this due to receding domestic demand. Though somewhat cushioned by the crisis, inflationary pressures have persisted, particularly due to rising fuel and food prices that the government has sought to contain through fiscal and administrative measures. Wages have been increased in recent years, for good reason, and a further rise may be necessary in a number of sectors. The actors involved in collective bargaining in 2009 will have to resist going beyond what is economically feasible, despite it being an election year.

Economic growth is expected to fall to between 3% and 4% in 2009, and unemployment has begun to go up again after its record low of December 2008. The budget is expected to go a bit more into deficit, and the country has experienced a slight depreciation, higher interest rates, and



an increase in country risk. Due to its earlier achievements, Uruguay was hit relatively late by the repercussions of the worldwide crisis, and at the time of this writing, in spring 2009, the country's economic situation could not be considered to be dramatically endangered. It even appears that the country's corporatist traditions and institutions, its relatively high degree of state interventionism, and the mixed economy that contained privatization and speculation have all been assets with regard to limiting exposure. But the longer the crisis persists, and the more its impacts increase in intensity and extend to more sectors, the more the country's structural dependency and vulnerability may come into play. This also has to do with the fact that many of the structural reforms on the government's agenda have been implemented only in part, as part of a compromise, or have had to be postponed.

Impressive reforms have recently been made in many fields, including tax and health care, social security, education, financial institutions, and economic de- and re-regulation. However, many other important issues have not been sufficiently addressed, and thus remain on the agenda. This includes the highly contested matters of the final central bank charter; the question of autonomy for educational institutions; the basic parameters of the social and welfare systems; pension schemes for state employees, the police, the military and the employees of the banking sector; and in particular a comprehensive reform of the civil service and state administrative structures (*reforma del estado*) which has to date been postponed, but has become increasingly urgent on efficiency as well as economic grounds. Poverty has been reduced, but still exists, particularly in neglected rural areas. Inequality has not receded, and the extremely low share of R&D expenditure in Uruguay is one principal factor impeding many achievements that might otherwise become sustained and structurally stable.

Structural reform legislation may not advance too much in 2009 because this year will be an election year, and most political energies will be spent on campaigning. In addition, departmental (municipal) elections will take place on 9 May 2010. As the record of the Frente Amplio government is on the whole impressive, disenchantment among its followers may be minimal. The party's leaders are popular, and polls taken in March 2009 gave the Frente the upper hand over the opposition, among which the National (Blanco) Party continues to be by far the strongest. The Colorados increasingly appear to be a "historic" party. How the various Frente factions are represented in the party's parliamentary group may also make some difference for future legislation.