Comments on “The Monetary and Fiscal History of Uruguay, 1960-2017” by Gabriel Oddone and Joaquín Marandino

Inter-American Development Bank

Washington, September 25, 2018
Main comments

- Paper does an excellent job in linking fiscal deficits to monetary instability

- But it totally ignores how well (or not!) fiscal policy has been conducted over the business cycle in Uruguay

- Uruguay has been, and continues to be, extremely procyclical in fiscal policy

- Procyclical fiscal policy:
  - exacerbates the business cycle (the when-it-rains-it-pours phenomenon)
  - implies little, if any, fiscal savings during good times (which has contributed to current fiscal problems)
  - fails to build fiscal space for possible use of countercyclical fiscal policy in bad times
Historically, government spending has been procyclical in most developing countries, including LAC (1960-2017)

<table>
<thead>
<tr>
<th>Country</th>
<th>Average Correlation</th>
<th>Notes</th>
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</thead>
<tbody>
<tr>
<td>Industrial</td>
<td>-0.08**</td>
<td></td>
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<tr>
<td>Emerging (non-LAC)</td>
<td>0.24***</td>
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<tr>
<td>LAC</td>
<td>0.28***</td>
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</tbody>
</table>

Note: Procyclical government spending policy implies higher spending in good times and lower spending in bad times. Source: Kaminsky, Reinhart, and Végh (2004, updated)
Good news: Many LAC countries have switched to countercyclical fiscal policy after 2000 (but not Uruguay!)

Institutional quality and fiscal cyclicality: Chile versus Uruguay

Note: 20-year rolling-windows. Source: Frankel et al. (2013).
One hundred years of fiscal policy cyclicality: The case of Chile (1921-2017)

Chile has become increasingly less procyclical over time and is now clearly countercyclical.

Source: World Bank (OCE). Calculations based on the PELT algorithm (Pruned Exact Linear Time), which looks for multiple changepoints in fiscal cyclicality regime.
One hundred years of fiscal policy cyclicality: The case of Uruguay (1921-2017)

Uruguay has been highly procyclical for more than thirty years now

Source: World Bank (OCE). Calculations based on the PELT algorithm (Pruned Exact Linear Time), which looks for multiple changepoints in fiscal cyclicality regime.
Uruguay needs to fiscally adjust to preserve hard-won credit rating

Sources: World Bank staff estimates (September 2018) and Fitch Ratings. Source: Végh et al. (2018).
Conclusions

- Great paper to learn about relation between fiscal deficits and inflation, as well as different crises the country went through

- But how fiscal policy is conducted over the business cycle is a critical aspect of fiscal policy that cannot be ignored

- Uruguay has been procyclical for almost 35 years now

- Why? (This is the fundamental policy question at this point!)
Thank you!

(For sources of presentation, please see next slide)
Appendix: Main sources for presentation


