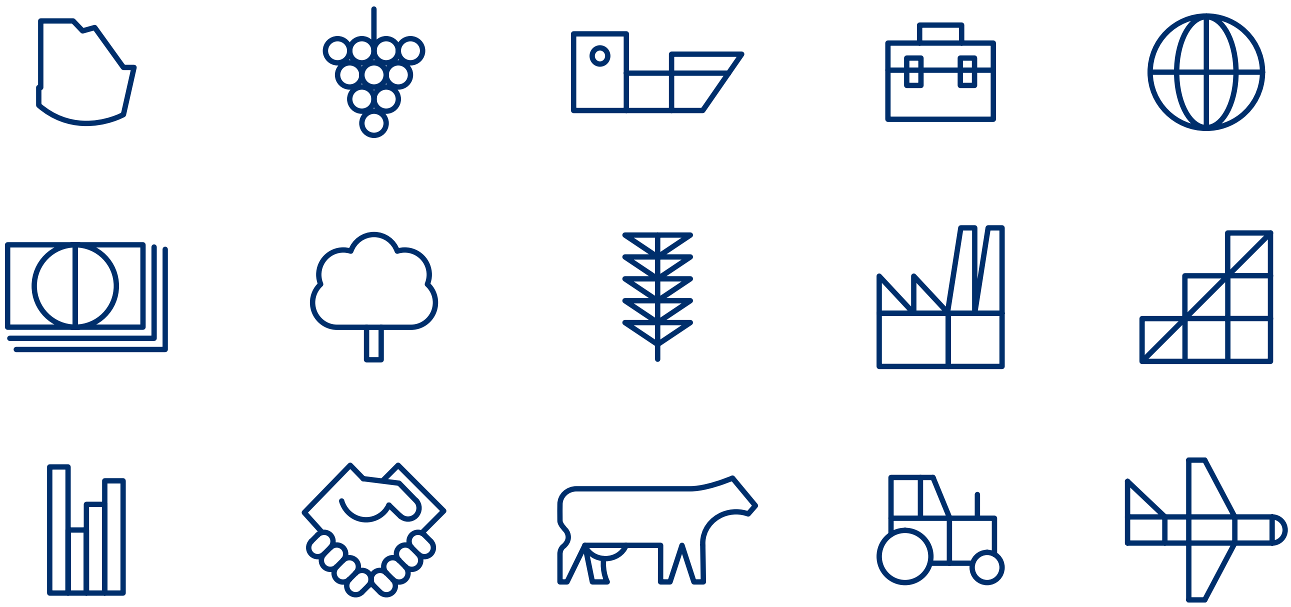
ANNUAL REPORT Foreign Trade

Uruguay XXI
PROMOCIÓN DE INVERSIONES
Y EXPORTACIONES



2016

Executive Summary

- Uruguayan exports of goods (including those from free trade zones) totalled **US$ 8,301 million in 2016, which constitutes a 7.3 % reduction compared to 2015.**

- In 2016, the fall in exports was explained by several factors. The weather affected some of the main crops, resulting in lower outputs. In addition, international reference prices dropped, which resulted in decreased exports.

- Over the last two months of 2016, there was a recovery of exports, which amounted to US$ 707 million in December 2016. which was 5% higher than the ones registered in December 2015.

- According to Uruguay XXI projections, exports of goods will increase by 6% in 2017. This growth would be explained mainly by an increase in exported volumes, and the stability or potential increase in prices. Furthermore, if current conditions remain unchanged, Uruguayan exports are likely to grow in 2018.

- Imports of goods, without considering oil and its by-products, reached US$ 7,387 million in 2016, a figure 13.6 % lower in the year-on-year comparison. The three main imported goods (vehicles, supplies for wind mills, and clothing) dropped 20%, 30%, and 10%, respectively.

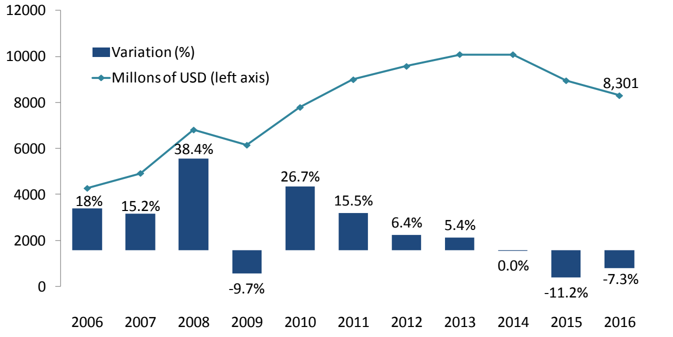
Uruguayan Exports of Goods in 2016

Uruguayan exports of goods, including those from free trade zones (FTZs), reached US$ 8,301 million in 2016, which constituted a 7.3% reduction in comparison with 2015[1].

This reduction occurs in a context of minimum growth of both international trade (an increase of barely 1.7% in volume according to the WTO) and the global economy. The main factors that explain this trend are the same as in 2015: commodity prices remained low, and the Chinese economy continued to slow down. Meanwhile, at a regional level, the recession in Brazil is still an obstacle, as well as Argentina's stagflation.

After a period of sustained growth in the exports of goods (an average increase of 7% over the last decade), Uruguayan exports of goods fell in 2015 and 2016 (see Graph No. 1). However, they are expected to recover its growth path in 2017.

Graph No. 1 – Uruguayan Exports

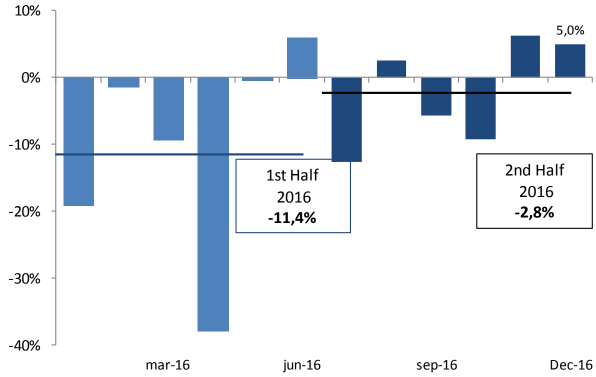


Source: Uruguay XXI based on data from the National Customs Administration, Nueva Palmira FZ, and Montes del Plata.

In regard to the **monthly export figures in 2016**, it is possible to distinguish the gap between the first few months and the end of the year. Whereas during the first half of the year foreign sales dropped 11.4 % in comparison with the same period of 2015, during the second half of the year, the drop was significantly lower (-2.8 %). In fact, over the last two months of the year there was a year-on-year increase in exports. In December 2016, external sales amounted for US$ 707 million and were 5% higher than the ones in December 2015.

In particular, the strong fall in April is essentially explained by the damage caused by heavy rains, which affected soybean exports in particular.

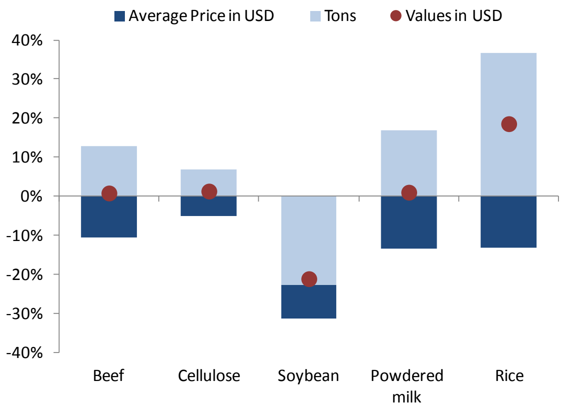
Graph No. 2 –Monthly Exports (Year-on-year variation %)



Source: Uruguay XXI based on National Customs Administration and Montes del Plata.

Analysing the **annual export figures** in 2016, the drop is mainly explained by lower prices. As shown in Graph No. 3, the exported volumes of major products rose (except for soybeans), while their average prices fell. The same happens with the rest of the exports. In the period January-November 2016, exports measured by volume dropped by 3%, while average prices decrease by 6.4 % (data from the Central Bank of Uruguay).

Graph No. 3 –Main Exported Products (Variation %, 2016)



Source: Uruguay XXI based on National Customs Administration and Montes del Plata.

[1] Exports from FTZs totaled US$1,913 million, and made it possible to soften the reduction in foreign sales. Meanwhile, exports from customs territory totaled US$7,087 million, 8 % less than in 2015. This includes sales of beverage concentrate from the Colonia FTZ, cellulose from the Fray Bentos and Punta Pereira FTZs, and pharmaceutical products from Zonamerica and Parque de las Ciencias.

Main Exported Products in 2016

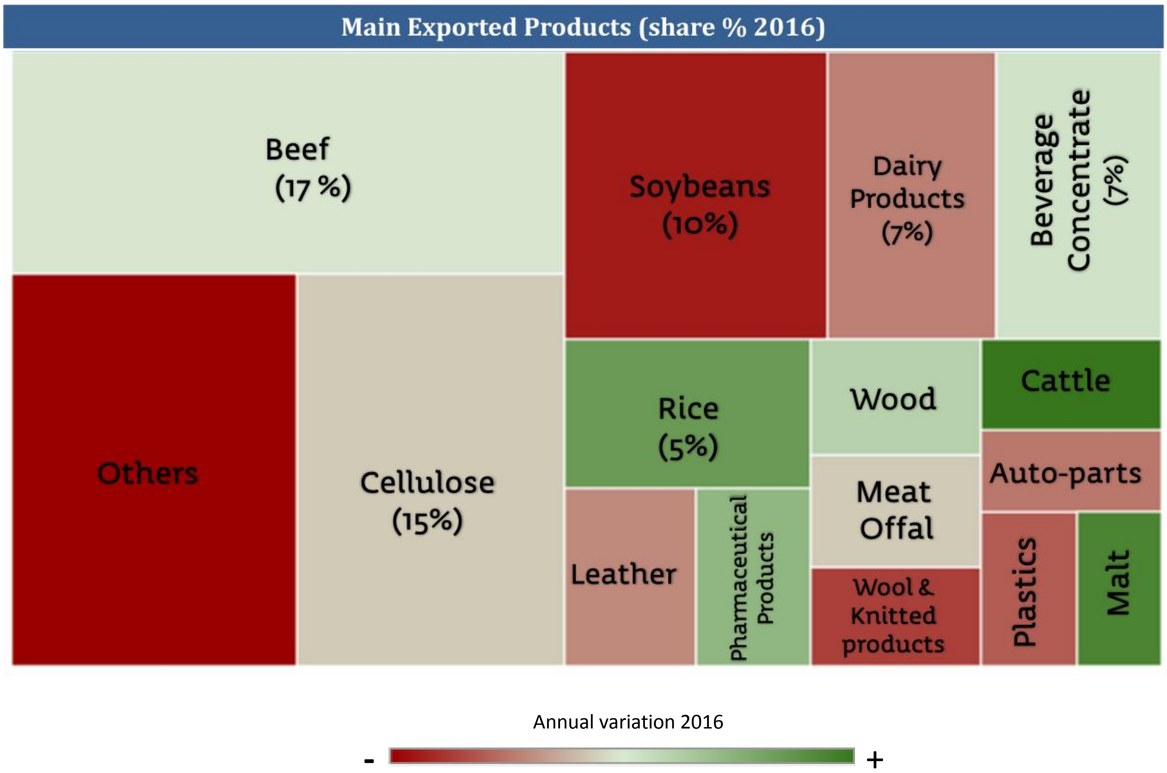
In 2016, **beef** was the main exported product, with sales of US$ 1,443 million. Although there is still a downward trend in export prices, exported volumes reached a new historic record, and their growth made it possible to make up for most of the price drop. The exported volume was approximately 420,000 tons (carcass weight)[2], 11% higher than in 2015, while average export prices dropped nearly 10%. The main destinations for Uruguayan beef were China and the United States. These two countries had a share in Uruguay's beef exports slightly under 50%.

Cellulose was once again second in the export ranking. Sales were relatively stable with a slight downward turn due to the fall in prices throughout the year. Exports totalled approximately US$ 1,242 million, 2% lower than in 2015. China was the main market for this product, with a share close to 37%, while the Netherlands (which operate as a distribution center for Europe) received close to 25% of the exported cellulose.

By mid-2016, UPM announced the intention of building a second cellulose plant in Uruguay. The schedule presented by the company established the plant's construction would begin in the second half of 2018, and the exports in 2020. Its production capacity would be similar to the total production of the two existing plants (over two million tons). Consequently cellulose would become the main exported product, with a share greater than 25% of the total. Moreover, Uruguay will produce around 5 million tons of cellulose a year. That volume would allow this country to become the second global exporter of this product since that year, after Brazil[3].

Soybean was the third most exported product in 2016. This year's weather affected crops at production, logistics, and harvest levels. These accounted for exported volumes 23% lower than the previous harvest. Nevertheless, the average export price went from US$370 to US$378 per ton. This increase partially compensates the 21% drop in export volumes. In regard with destination markets, China maintained its significant share (73%), while Germany, Argentina, and the Netherlands were other relevant destinations, despite having minor shares.

Dairy products were fourth in the 2016 export ranking with over US$ 563 million exported, although the unfavorable context, mostly explain by the downward trend of international prices. In particular, powdered milk and cheese, the sector's main products, saw their prices drop 13% and 24%, respectively. Additionally, purchases from Venezuela, one of the most important markets for



Source: Uruguay XXI based on data from the National Customs Administration, Nueva Palmira FZ, and Montes del Plata.

[2] Out of the total, 86 % is frozen meat, and the remaining 14 % is chilled meat.

[3] If the market remains stable.

Uruguayan dairy products, were virtually non-existent this year. In spite of this situation, the Brazilian market virtually doubled the exported value of 2015. Powdered milk constituted 78% of dairy sales to this destination country.

Beverage concentrate, exported from the Colonia FTZ, had sales 2% higher than in 2015, which amounted for US$ 557 million. Mexico, the Philippines, and Guatemala were the main destinations.

Rice was the product that had the greatest positive impact in 2016 exports. This cereal's sales exceeded 980 thousand tons, which makes 2016 the third year with a higher exported volume. The sector managed to dodge the effects of the weather throughout the year, particularly at the time of sowing and harvesting, although losses are estimated to reach 160 thousand tons. In addition, rice was the country's second agricultural product, with figures exceeding US$ 434 million. These records put Uruguay in the top 10 for global rice exporters, supported by the fact that rice is considered a "premium" product thanks to the technology and integration applied to the productive chain.

Concerning market destinations, Brazil regained the significance it had some years ago in this sector, and represented 24% of the sales in 2016, followed by Peru with the same share percentage. Moreover, 7% of the total was sold to Mexico. It is important to mention that 70,000 tons were exported to Colombia as part of a 200,000-ton contingent. The aforementioned set Colombia fourth among rice destinations this year, which reveals the importance of the regularization of the phytosanitary protocol between the Agricultural Institute of Colombia and the Ministry of Livestock, Agriculture and Fisheries.

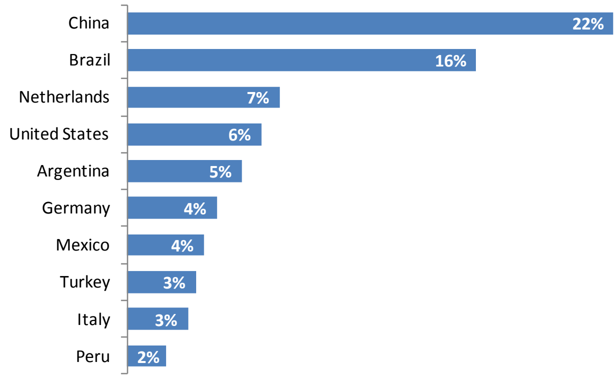
Another product with an outstanding performance in 2016 was cattle, with a 26% year-on-year growth. Turkey was the main market, receiving 94% of the total. Additional products showed positive variations, such as malt, pharmaceutical products (from FTZs and customs territory), wood, and citrus fruits. Vehicles, auto-parts, wool and knitted products, and rubber are among the products that had a negative impact.

Main Export Destinations in 2016

China was the main destination for Uruguayan exports in 2016, with a share of 22% of the total exports. Purchases from that country exceeded US$ 1,840 million, a figure 12% lower in the year-on-year comparison. China is Uruguayan's larger purchaser for the 3 main exported products. In 2016, it was the destination of 73% of Uruguayan soybeans, 37% of its cellulose, and 35% of its beef.

In spite of the recessive context of its economy, **foreign trade to Brazil grew 2% in 2016 in comparison with 2015**, and exceeded US$ 1,322 million. This growth allowed Brazil's share in Uruguayan exports to grow by 2%. Dairy products boosted the growth in this market, particularly due to powdered milk and cheese. In both cases, average prices fell (7% and 21%, respectively), but this fall was compensated for increases in volume that more than doubled the increases from 2015 and allowed this type of product to remain the most exported to Brazil. Other important products in that market were malt and plastics, which are mostly sold within companies. Lastly, rice sales were significant: they went from 27 thousand to 240 thousand tons, and totalled US$ 104 million.

Graph No. 4 – Main Destinations of Exported Goods – 2016



Source: Uruguay XXI based on data from the National Customs Administration, the New System in Nueva Palmira, and Montes del Plata.

The Netherlands stayed on the growing trend shown in 2015, with a 3% variation in 2016. Despite cellulose was the main exported product for the ninth consecutive year -with US$ 320 million-[4], beef was the product with the greatest positive effect in the increase of exports to this market. Beef sales were 29% higher than in 2015, reaching US$ 159 million in 2016, and they reached an average annual growth of 19% over the last decade. Finally, and in spite of a 46% retraction in amounts sold, soybeans remained the third product exported to this market.

[4] It is worth mentioning that the Netherlands operate as a distribution center in Europe for part of the cellulose exported to that destination.

The United States regained their significance as a destination for Uruguayan exports and ranked fourth. Sales to that country totalled US$ 509 million in 2016, which shows a 19% retraction in comparison with 2015. This fall can be explained by lower sales of the three main products sent to that market: beef (which dropped at a similar rate as overall sales), cellulose, and leather. The fall in the amounts of beef can be explained both by lower volumes and by average prices 9% lower than in 2015. Some of the products that had a positive variation in 2016 are wood, wood products, and fish. Furthermore, just like in 2015, the United States were the main destination of Uruguayan citrus fruits, after trade negotiations in 2013 made it possible to start selling to this market.

Argentina took fifth place: US$ 437 million were exported to that destination in 2016, which signified a slightly decrease by 5% in the current year taking into account that Argentine imports experienced an overall drop in 2016[5]. Auto-parts were once again the main exported product, with US$ 82 million. In addition, we must highlight that sales of soybeans in the neighboring country reached a historic peak: US$ 49 million. These sales were completed using a new method: soybeans were transported on barges from the Port of Montevideo to the Port of San Lorenzo, in Santa Fe province[6]. Other products that stood out due to their growth were plastics, cleaning products, and pharmaceutical products.

Other relevant destinations for Uruguayan exports in 2016 were: Germany -mostly due to higher exports of beef and soybeans, in addition to the fact that they began to import cellulose from Uruguay-; Turkey –thanks to cattle sales-; Peru –rice-; Paraguay –tobacco-; and Philippines –beverage concentrate-.

Uruguayan Imports in 2016

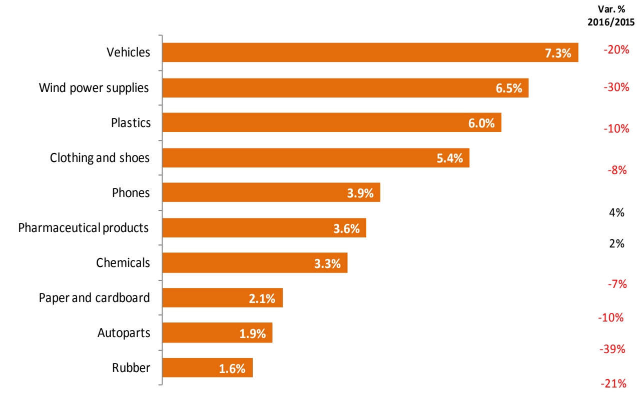
Imports of goods also fell in 2016, but at a higher rate than exports. External purchases, without considering oil and its by-products, reached **US$ 7,387 million in 2016**, a figure **13.6% lower in the year-on-year comparison**.

Vehicles were the country's main import in 2016, with US$ 542 million: 59% were cars, 30% trucks, and the remaining 11 % other vehicles. Supplies for wind mills were the second imported product, with US$ 477 million, a figure 30% lower than in 2015. Imports of these products are expected to fall significantly in 2017 given that the installed wind energy capacity has already maxed out.

Plastic imports totalled US$ 444 million in 2016, and they mostly came from the region: 42% of the total purchases came from Brazil, Argentina, and Chile.

Purchases of clothing and shoes also stood out, they exceeded US$ 400 million and had China as the supplier of over half of the total imports. Phones were the fifth imported product in 2016, with figures 4% higher in the year-on-year comparison. China and the United States were the main suppliers.

Graph No. 5 –Main Imported Products (Share % and var. % 2016)



Source: Uruguay XXI based on National Customs Administration.

Considering imports' source countries, China had a share of 21% of the total, and purchases from this supplier dropped 12% in comparison with 2015. Purchases of clothing and phones stood out for this source. Brazil and Argentina were the next sources, with retractions of 5% and 13%, respectively. Vehicles were the main product imported from Brazil, and plastics from Argentina. The sources with the most positive incidence were Egypt (due to imports of urea for agricultural use), Morocco (phosphates for fertilizers), and Spain (supplies for wind mills).

[5] They grew 15 % according to data from Penta Transaction.
[6] Source: El País "*Uruguayan soybeans for Argentina, a good export*"

Exports Will Grow Again in 2017

According to WTO estimations, 2016 would be the year with the lowest growth of global trade of goods since the 2009 crisis. This moderate growth (1.7 % measured in volumes) is explained by the weak growth of global economy, as well as different structural factors such as a lower trade liberalization rate and a lower expansion of global value chains.

The economic weakness of China and Latin America was particularly relevant for Uruguayan exports. Besides, there was a downward trend in commodity prices since 2014, led by oil, which only began to revert by mid-2016.

During the last few months of 2016, the global scenario showed some signs of recovery. The WTO expects a greater dynamism of global trade in 2017, although there will be some uncertainties[7]. Commodity prices also show a slight recovery and, according to the IMF and the World Bank, in 2017 product prices will increase, but still at lower levels than 2014.

However, analysts agree that both of our neighbors' economies will probably start growing in 2017.

The international stage -set by higher commodity prices and a moderate regional and global growth-, together with a local context of higher production in the agricultural exporting sector, make it possible to forecast an increase in Uruguayan exports for 2017.

According to Uruguay XXI estimates, exports of goods, including FTZs, would increase by 5.7% in 2017. As shown in Table 1, this growth would be explained basically by an increase in exported volumes, and the stability or potential increase in prices of the main exported products. If current perspectives remain unchanged, exports could be expected to continue growing in 2018.

However, there are several risk factors that need to be taken into account. More protectionist policies in the United States or economic instabilities resulting from an inappropriate resolution of Brexit could affect global trade dynamics. Meanwhile, the gradual deactivation of the FED's expansionary policy and the international liquidity withdrawal in dollars has already started to put pressure on the depreciation of all other currencies.

Table No. 1 – Uruguay Exports – Projections

		Variation 2017		
	Millions of USD	**Value**	**Volume**	**Price**
Beef	1,473	1 %	+	+
Cellulose	1,280	2 %	=	+
Soybeans	1,107	25 %	+	=
Dairy products	769	35 %	+	+
Beverage concentrate	563	0%	=	=
Rice	457	6 %	+	+
Meat Offal	228	1 %	+	=
Malt	204	26 %	+	-
Pharmaceutical products from FTZs	129	20 %	+	=
Wheat	57	-48 %	-	-
Others	2,491	-2 %		
Total	**8,758**	**5.7%**		

Note(*): Includes pharmaceutical products and beverage concentrate.
Source: Estimation by Uruguay XXI based on the Agricultural Statistics Bureau of the Ministry of Livestock, Agriculture and Fisheries, the National Meat Institute, the National Milk Institute, and the IMF.

At a regional level, the economic situation was worse than expected at the beginning of the year. Argentina went into an economic recession whilst analysts estimate a decrease in 2.3% GDP in 2016[8]. Meanwhile, in the middle of a context of political instability that included the impeachment of President Dilma Rouseff, the economy in Brazil remained in a deep recession, the longest in the last few decades.

If the currencies of other partners or trade competitors move at a different speed, the price competitiveness of Uruguayan exports might be affected.

A "hard landing" in China seems unlikely, but an economic slowdown of the Asian giant might interrupt the increase in prices of commodities exported by Uruguay.

Among emerging countries, the greatest uncertainties still come from the region. Neither Brazil nor Argentina are showing signs of recovery in their economic activity, and

[7] Growth will range between 1.8 % and 3.1 %.
[8] According to the latest survey of economic expectations conducted by the Central Bank of Argentina.

they are expected to consolidate only in 2018. Although Uruguay has managed to decouple from the region, it is still a relevant factor for our country's economic growth.

For charts with detailed information about exports, visit: Statistical Appendix.

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