NEWS RELEASE

Feb 05, 2020

R&I Affirms BBB, Changes Outlook to Positive: Oriental Republic of Uruguay

Rating and Investment Information, Inc. (R&I) has announced the following:

ISSUER: **Oriental Republic of Uruguay**

Foreign Currency Issuer Rating: BBB, Affirmed
Rating Outlook: Positive, Changed from Stable

RATIONALE:

Uruguay is a socially stable country with a high income level. While the country has a traditional worker protection culture like other South American countries, it ranks among the best in Latin America particularly for democracy, lack of corruption, adherence to the rule of law and strong ESG credentials, which gives it the potential to grow into a business hub for the region. The economy will likely pick up in the medium term, with a large investment project slated to start using domestic and foreign capital. Although the current account is expected to move into deficit, it is unlikely to be a significant destabilizing factor. Fiscal risk is kept in check under a prudent debt management policy. Expectations are high for pension and labor market reforms, which will be in the hands of the new administration to be inaugurated in March 2020. In consideration of these factors, R&I has affirmed the Foreign Currency Issuer Rating at BBB and changed the Rating Outlook to Positive.

Uruguay receives the highest evaluation in Latin America for political and social stability. On the environmental front, most of the country's energy is generated through renewable sources, and the government is keen on adopting environmentally motivated tax policies.

Uruguay's economic growth is stagnant due in part to the depreciation of the currencies of South American countries including its own and economic turmoil in neighboring Argentina. Meanwhile, UPM-Kymmene Corp., a major paper manufacturer in Finland, is scheduled to construct its second mill in Uruguay, and public investments in the construction of related infrastructures, such as railways and port facilities, are going on ahead of the project. These factors will drive medium-term economic growth. Containing inflation remains a key challenge in the macroeconomic policy realm and requires sustained efforts.

The current account has been in surplus since 2017. Once infrastructure investments are underway in earnest, imports of capital and intermediate goods are expected to increase. Needless to mention, exchange rates and terms of trade will also matter a great deal. Even if the current account moves back into deficit, however, R&I does not believe that the deficit will become a significant destabilizing factor, as long as it is caused mainly by a surge in imports related to foreign direct investment. There is no concern about foreign currency liquidity.

Since 2012, the government had taken a relatively expansionary fiscal stance. The current administration focuses on fiscal consolidation, but its efforts are centered on tax and utility rate hikes. Partly because of pressure from within the left-wing government, it has not embarked on spending cuts so far. If a rise in public pension premiums caused by a special factor is excluded, the fiscal balance keeps deteriorating.

The ratio of outstanding public debt to gross domestic product (GDP) is relatively high, standing at 66% as of end-June 2019. If, however, short-term borrowings by the central bank for liquidity management purposes and the government's preliminary borrowings to cover redemptions for the next 12 months are excluded, the outstanding debt was 33% of GDP. Given this, together with credit lines from multilateral development banks and prudent debt management practices, actual fiscal risk has been mitigated.

Maintaining a sound fiscal position is essential to the stability of Uruguay's economy, which is small and exposed to changes in the external environment. The focal point is on whether the new administration, which will take office in March 2020, will be able to implement the pension reform and

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other initiatives and thereby rein in structural expenditures.

The primary rating methodology applied to this rating is provided at "R&I's Analytical Approach to Sovereigns". The methodology is available at the web site listed below, together with other rating methodologies that are taken into consideration when assigning the rating.
https://www.r-i.co.jp/en/rating/about/rating_method.html

R&I RATINGS:

ISSUER:	**Oriental Republic of Uruguay**
	Foreign Currency Issuer Rating
RATING:	**BBB, Affirmed**
RATING OUTLOOK:	**Positive, Changed from Stable**

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