ISSUER COMMENT

10 July 2026

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Government of Uruguay

Weaker growth outlook increases reliance on fiscal consolidation as debt rises

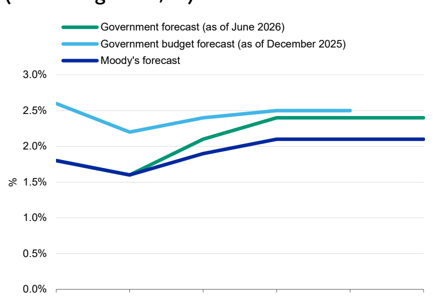
On 30 June, the government of Uruguay (Baa1 stable) submitted the Rendición de Cuentas, which closes the 2025 fiscal exercise and amends the 2025-2029 Budget Law for subsequent years. With this update, the government has revised the real GDP growth path downward to 1.8% registered in 2025 and to 1.6% projected for 2026, from 2.6% and 2.2% in the original 2025-29 budget, followed by a gradual recovery (see Exhibit 1). The 2025 performance reflects a temporary refining shutdown, weaker construction activity and a more challenging external environment, while the 2026 revision incorporates the global slowdown, oil-price volatility linked to the Middle East conflict and softer regional demand.

Despite weaker growth, the Ministry of Economy and Finance maintains the original headline and structural fiscal balance path through 2030 by offsetting lower revenue with cuts to operating spending and discretionary transfers in 2026. Even so, the consolidation path outlined in the mid-year review is insufficient to stabilize gross government debt which, in line with the government's projections, we expect to exceed 65% of GDP by 2030 from 59.8% in 2025. This path would remain consistent with the government's fiscal rule, which anchors net debt (excluding liquid assets of 3-4% of GDP over the forecast horizon) at 65%. However, the rigid spending structure, including indexed wages, social transfers and pensions, which together account for 86% of primary spending, leaves limited room for adjustment in the event of shocks, compounding fiscal vulnerabilities as the debt burden rises.

The mid-year review now projects 2026 revenue at 27.4% of GDP from 27% in 2025, a small deviation compared to 27.9% in the original budget. However, we see rising risks of fiscal slippage in 2027, when the budget projects revenue will jump by 0.9 percentage point (pp) to 28.3% of GDP (see Exhibit 2). The increase is underpinned by the five-year, 1.5 pp revenue package approved with the 2025-29 budget that relies primarily on administrative gains and base broadening rather than rate increases.

Exhibit 1

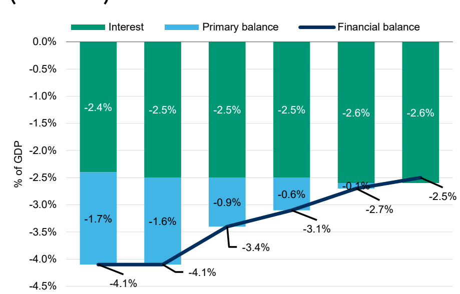
Weaker than budgeted real GDP growth increases fiscal adjustment effort ...
(real GDP growth, %)



Sources: Ministry of Finance and Moody's Ratings

Exhibit 2

... to meet unchanged headline (and broadly equivalent structural) fiscal targets
(% of GDP)



Sources: Ministry of Finance and Moody's Ratings

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The revenue package rests on three pillars: administrative efficiency gains (about 0.75 pp of GDP), which historically materialize slowly; localization measures, including the Domestic Complementary Minimum Tax and taxation of non-resident dividends (about 0.60 pp of GDP), whose yield and timing depend on international tax coordination; and technical adjustments on capital gains (about 0.15 pp of GDP). A reduction in tax expenditure on electric and hybrid vehicles from 2027, announced in the mid-year review, provides additional support. In our view, the focus on administrative measures helps preserve competitiveness but increases uncertainty around effective revenue yields, leaving medium-term consolidation contingent on sustained spending discipline.

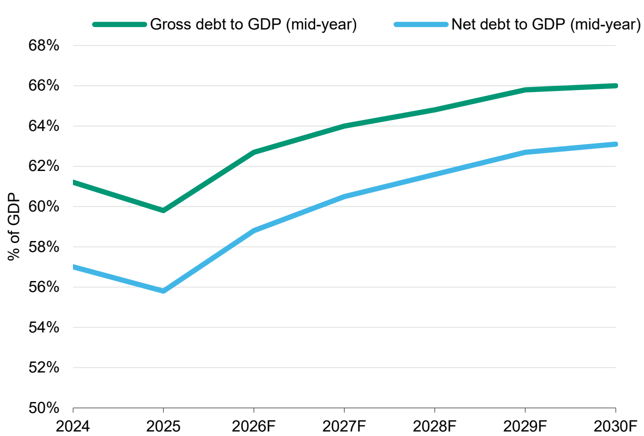
On the expenditure side, the mid-year review confirms structurally elevated outlays of 31%-32% of GDP in 2026-30, driven by stronger social transfers (rising to 8.7% of GDP from 2027, from 8.3% in 2024), pension outlays at 10% of GDP in 2025, and higher capital spending (to a still-modest 1.5% of GDP from 2025, versus 1.2% previously). The early-retirement option at 60 rather than 65 (subject to lower pension benefits and a solidarity supplement for lower-income retirees), now under government consideration following the Social Dialogue consultation, could in our view raise pension spending depending on its final design, though Banco de Previsión Social (BPS) estimates the incremental cost at only around 0.15 percentage points of GDP by 2040.

On the financing side, the central bank's strengthened inflation-targeting track record since 2023 continues to support two positive trends: the gradual expansion of local currency (LC) debt to 56% of total debt in 2025, from 44% in 2019, which reduces currency risk; and the shift toward non-indexed, fixed-rate LC issuance away from CPI- or wage-indexed variable-rate debt (see Exhibit 4), which reduces the pass-through of inflation and wage dynamics into debt service costs, allows nominal GDP growth to gradually erode the real debt burden and strengthens the government's control over its medium-term fiscal trajectory.

Meanwhile, we expect the government's dialogue with the Pension Savings Fund Administrators (AFAP), established on 4 May 2026 with preliminary conclusions due in July 2026, to provide clarity on the administration of private pension savings raised by the institutional changes proposed under the April 2026 Social Dialogue report.[1] Representing about 30% of GDP, private pension funds are a key institutional investor base critical to the further development and depth of local markets.

Exhibit 3

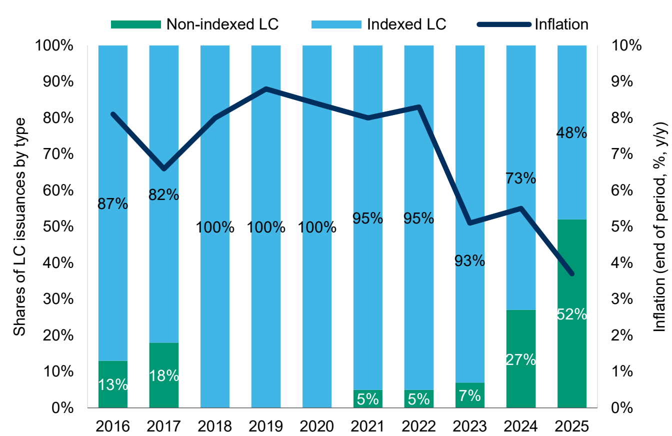
Debt burden is on an increasing trajectory, reducing fiscal shock absorption capacity
(% of GDP)



Net debt is defined as gross debt minus the government's liquid assets.
Sources: Ministry of Finance and Moody's Ratings

Exhibit 4

Tighter inflation control supports shift toward non-indexed local currency debt issuance
(Local currency debt issuance by type (LHS); end of period inflation, %, y/y (RHS))



Indexed local currency (LC) issuances include CPI-indexed and wage-indexed variable rate issuances
Sources: Ministry of Finance, Central Bank and Moody's Ratings

Endnotes

1 That report recommended centralizing administration of individual savings accounts under a new public entity, integrated with the system's other pillars.

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