

CREDIT ANALYSIS

Rate this Research



RATINGS

Uruguay

	Foreign Currency	Local Currency
Gov. Bond Rating	Baa2/STA	Baa2/STA
Country Ceiling	A2	A2
Bank Deposit Ceiling	Baa2	A2

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This Credit Analysis provides an in-depth discussion of credit rating(s) for Uruguay, Government of and should be read in conjunction with Moody's most recent Credit Opinion and rating information available on [Moody's website](#).

Uruguay, Government of

Overview and Outlook

Uruguay's Baa2 sovereign rating is supported by a strong institutional framework that reinforces political and social stability and makes the country an attractive destination for foreign direct investment (FDI). Comparatively large fiscal reserves and external buffers, along with a low central government debt burden and very strong liability management practices, also support creditworthiness.

These factors are balanced by credit challenges that include a relatively high, albeit decreased, share of foreign currency government debt and financial system dollarization. Persistently high inflation and a deterioration of structural fiscal balances have weighed on policy credibility, and led central government debt to inch up.

Real GDP growth has continued to moderate from over 5.5% over the past decade to 3.5% in 2014, in line with potential growth. We forecast that growth will slow to 2.6% in 2015 due to continued weak external conditions that will outweigh the benefits of lower energy prices on private consumption. Economic activity will likely accelerate to 3.1% in 2016 and remain near potential in 2017 and beyond.

Higher current spending has driven a structural widening of fiscal deficits in recent years, reflecting expansion of social programs, and increasing fiscal accounts rigidity. As the economy shifts to a lower level of output growth, excess revenues will no longer be available to offset the current growth in expenditures. Nevertheless, the new administration of President Vazquez is committed to fiscal consolidation and ensuring the sustainability of public finances.

Upward rating pressure could result from (1) a significant strengthening of the government's balance sheet through a reduction of the sovereign's debt and interest burden, and (2) a reduction in vulnerabilities through a significant decrease of financial system and government debt dollarization and addressing structural rigidities in the economy to achieve a higher level of potential growth.

Conversely, downward rating pressure could result from (1) a continued deterioration of structural fiscal balances and a weakening of the government balance sheet, or (2) a sustained and material erosion of external and financial buffers.

This Credit Analysis elaborates on Uruguay's credit profile in terms of Economic Strength, Institutional Strength, Fiscal Strength and Susceptibility to Event Risk, which are the four main analytic factors in Moody's [Sovereign Bond Rating Methodology](#).

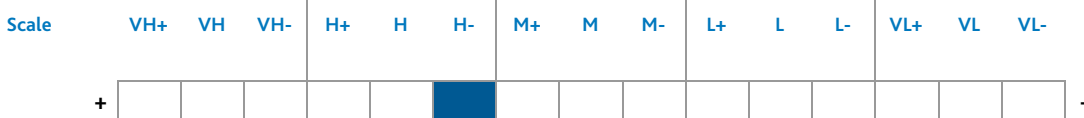
Rating Rationale

Our determination of a sovereign's government bond rating is based on the consideration of four rating factors: Economic Strength, Institutional Strength, Fiscal Strength and Susceptibility to Event Risk. When a direct and imminent threat becomes a constraint, that can only lower the preliminary rating range. For more information please see our [Sovereign Bond Rating Methodology](#).

Economic Strength: High (-)

Following a gradual deceleration in GDP growth, a stable economic outlook with balanced risks

Factor 1

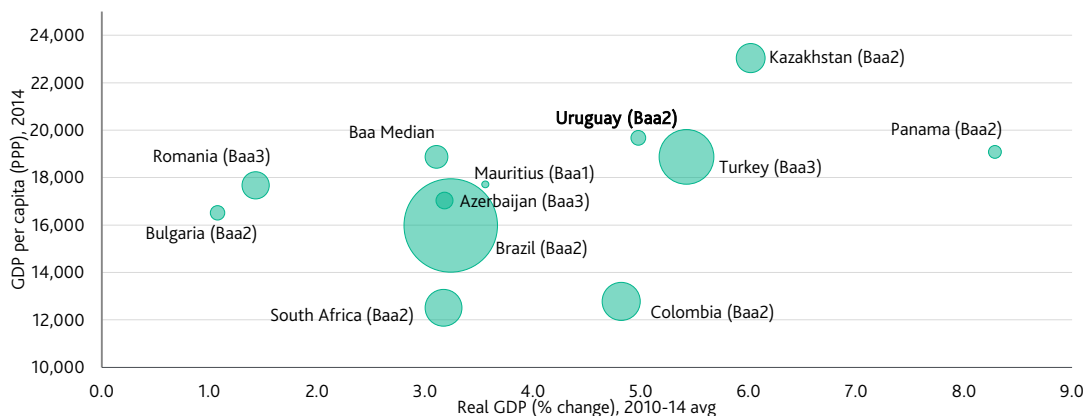


Economic strength evaluates the economic structure, primarily reflected in economic growth, the scale of the economy and wealth, as well as in structural factors that point to a country's long-term economic robustness and shock-absorption capacity. Economic strength is adjusted in case excessive credit growth is present and the risks of a boom-bust cycle are building. This 'Credit Boom' adjustment factor can only lower the overall score of economic strength.

Uruguay's sovereign ratings incorporate our 'High (-)' economic strength assessment on a global basis reflecting robust growth dynamics and a relatively high income per capita, counterbalanced by the low scale of the economy (see Exhibit 1). Uruguay's \$57.5 billion economy is comparable in size to that of Bulgaria (Baa2, \$55.8 billion), Panama (Baa2, \$45.7 billion) and Slovenia (Baa3, \$49.2 billion), but smaller than the \$137.5 billion 'Baa' median. Uruguay's \$19,679 per capita income on a purchasing power parity basis remains very much in line with peers (\$18,874 'Baa' median). Favorable economic prospects, reflected by potential growth of 3%-3.5% as estimated by the authorities and the International Monetary Fund (IMF), also support economic strength. The 'High (-)' economic strength ranking is shared by Colombia (Baa2 stable), Panama (Baa2 stable) and South Africa (Baa2 stable).

EXHIBIT 1

Uruguay's economic strength is supported by relatively high income levels and economic dynamism
 Size of the bubble = Nominal GDP (US\$ Bil., 2014)



Source: Haver Analytics and Moody's Investors Service

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

Foreign direct investment has been a key pillar of growth

Investment-to-GDP rates through 2011 lagged 'Baa' category medians but have since converged with them as a result of lower investment rates in peer economies (see Exhibit 2). In Uruguay gross investment picked up substantially in 2005-14 averaging 20.5% of GDP, up from less than 16% in 1995-2004. Although investment rates have traditionally lagged regional peers, investment in energy and telecommunications infrastructure remains largely adequate to meet the needs of the growing economy. The quality of transport infrastructure lags behind.

EXHIBIT 2
Investment ratios aligned with 'Baa' medians
Gross investment/GDP (%)

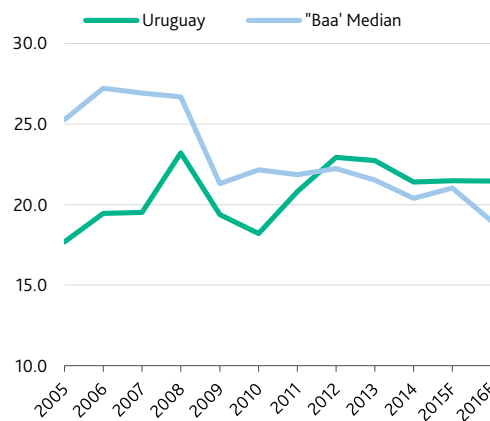
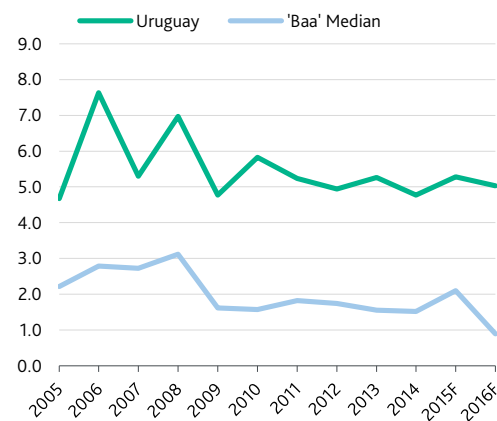


EXHIBIT 3
High FDI supports growth model
Net foreign direct investment/GDP (%)



Source: Haver Analytics and Moody's Investors Service

Uruguay's relatively open economy, favorable investment climate and strong institutional framework make the country an attractive destination for FDI. The level of FDI rates has outperformed peers (see Exhibit 3) and remains at high levels, becoming a key pillar for fixed capital accumulation and an important contributor to growth dynamics.

Having been directed mostly to export-oriented projects, FDI has significantly enhanced the country's export potential, taking advantage of a workforce that by regional standards is highly educated. Although an important portion of foreign investment has been directed toward commodities production, light manufacturing related to primary sector activities has also benefited from the inflows. These inflows, along with the related technology transfer, have helped boost productivity gains throughout the economy and supported economic growth.

Greenfield investments have also contributed to boosting employment and raising real wages, which in turn has supported the strong consumption dynamics that underpin Uruguay's economic growth. Despite a relatively subdued rate of factor accumulation not attributable to demographics since the 2002 crisis, robust growth has been primarily derived from the direct and indirect benefits of FDI, which has acted as an amplifier of the economic cycle, and helped boost productivity.

We expect that even though FDI will remain robust through 2016, a gradual decline in inflows is likely, owing to a less favorable external environment. Productivity gains from new FDI are unlikely to materially boost economic growth in the near future, and there seems to be little impetus for increased investment from domestic sources. The public sector will likely cut capital expenditures as part of its consolidation strategy. Infrastructure and private sector investments will likely benefit from the government's greater emphasis on public-private partnership (PPP) projects, but the new framework is relatively untested. Overall,

a more subdued investment climate will also contribute to less volatile growth that is likely to remain near potential through 2017.

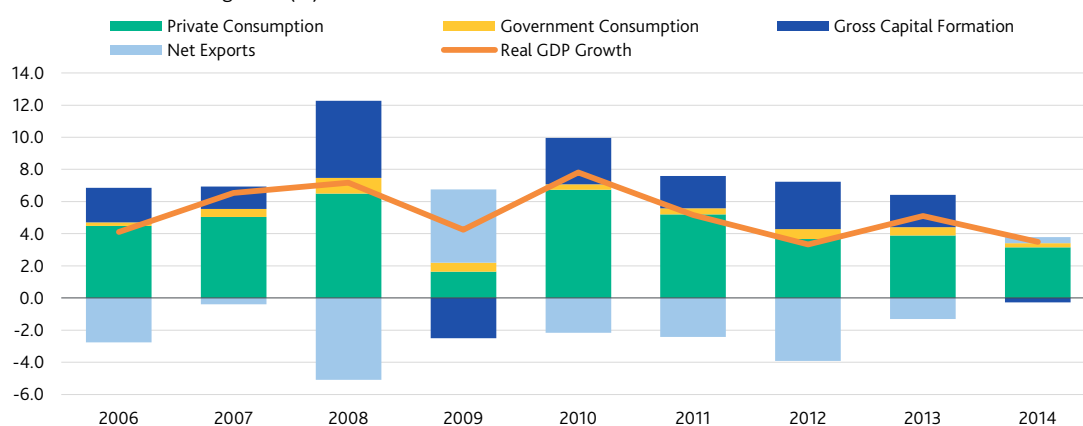
Declining investment has led to gradual economic deceleration, but pre-electoral spending supported economic activity against external headwinds

The economy performed strongly over the past decade despite volatile growth, and is weathering the regional slowdown. Real GDP growth moderated to 3.5% in 2014 from 5.1% in 2013. Private consumption growth remained robust despite a gradual slowdown from the very high levels of 2010-11, while declining private investment led to lower fixed capital formation, the main driver behind the slowdown in overall output growth (see Exhibit 4).

EXHIBIT 4

Moderating economic activity owing to lower investment

Contributions to real GDP growth (%)



Sources: Haver Analytics and Moody's Investors Service

Overall export receipts have slowed down markedly owing to weaker growth in Brazil (Baa2 negative) and Argentina (Caa1 negative), the two most important regional trading partners. Weak economic conditions in Argentina have weighed particularly on Uruguay's external services balance and prevented a further narrowing of the current account deficit.

Through the end of 2014, Uruguay's resilient domestic consumption was supported by improvements in the labor markets and continued consumer credit growth, reflecting higher employment and rising real and nominal wages. More importantly, pre-electoral public spending ahead of the October 2014 election helped offset the decline in private investment.

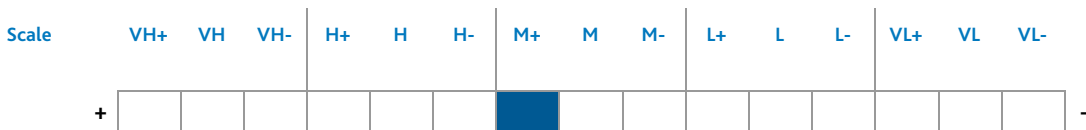
The weak economic outlook for Argentina and Brazil (Baa2 negative) will continue to dampen export demand and subdue Uruguayan manufacturing and services (particularly tourism), while also curbing FDI inflows. If the authorities pursue fiscal consolidation as announced by the new government, this will also act as a drag on growth. We forecast that the economy will slow down further in 2015, growing 2.6% for the year before accelerating to 3.1% in 2016 and 3.3% in 2017-18.

Upside and downside risks to the economic outlook remain balanced. Upside risks stem primarily from the possibility of large scale foreign investment projects materializing in the Uruguayan economy. Downside risks could arise from a further deterioration in regional economic conditions and lower commodity prices, but even if it were to persist, such economic weakness by itself would not lead to a deterioration in Uruguay's creditworthiness.

Institutional Strength: Moderate (+)

Despite very strong political institutions and social indicators, policy credibility and effectiveness remain weak

Factor 2

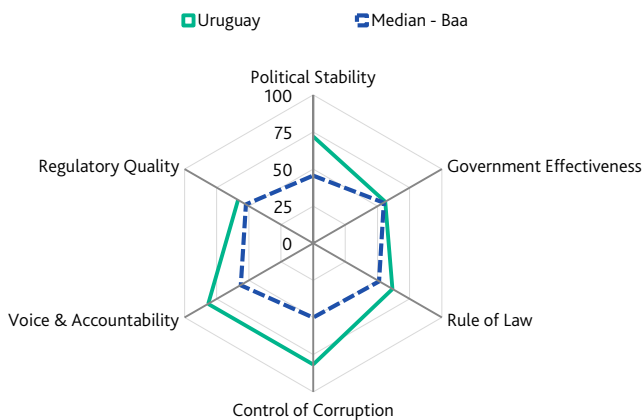


Institutional strength evaluates whether the country's institutional features are conducive to supporting a country's ability and willingness to repay its debt. A related aspect of institutional strength is the capacity of the government to conduct sound economic policies that foster economic growth and prosperity. Institutional strength is adjusted for the track record of default. This adjustment can only lower the overall score of institutional strength.

We rank Uruguay's institutional strength as 'Moderate (+)'. The assessment balances a strong institutional framework that reinforces policy predictability with still-evolving capabilities to effectively and credibly conduct these policies. The country's very favorable scores on the World Bank's governance indicators (see Exhibit 5) illustrate its political and social stability, which provides a supportive institutional foundation and a cohesive environment for developing and implementing economic policy. Social indicators, including those measured by the Human Development Index, also support these findings. Nevertheless, the authorities face important challenges to meet policy goals, as exemplified by stubbornly high inflation rates that remain above the official target range and a mixed track record of fiscal management. Other sovereigns that share a similar assessment of 'Moderate (+)' institutional strength include Bulgaria (Baa2 stable), Colombia (Baa2 stable) and the Philippines (Baa2 stable).

EXHIBIT 5

High government effectiveness indicators outperform 'Baa'-rated peers
(Percentile rank among rated sovereigns)



Sources: World Bank Governance Indicators and Moody's Investors Service

Relatively high inflation and low policy effectiveness hampers monetary credibility

Although we consider Uruguay's institutional framework and effectiveness to be high based on its World Bank Governance Indicators scores, we assess policy effectiveness and credibility, as measured by inflation performance, inflation volatility and fiscal performance, to be low relative to peers.

Inflation in Uruguay has historically been high, with consumer prices averaging increases of 7.5% per year over the past decade, compared to 4.3% for the median of Baa-rated sovereigns over the same time period (see Exhibit 6). Uruguay's persistently high inflation rates have been driven by (1) a high pass-through from fuel costs as the Uruguayan economy's reliance on imported oil makes domestic inflation highly vulnerable to the global level of energy prices, (2) pro-cyclical government spending, and (3) the prevalence of indexation mechanisms, particularly those involving wage negotiations; a common practice in Uruguay is for wage contracts to incorporate indexation clauses that explicitly incorporate last year's inflation into annual renegotiations.

EXHIBIT 6

Persistently higher-than-peers inflation rates...

Consumer price inflation (end of period, %)

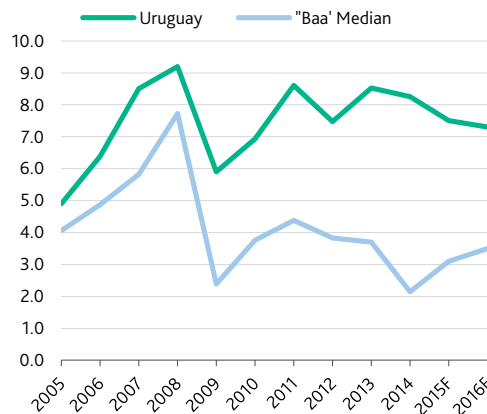
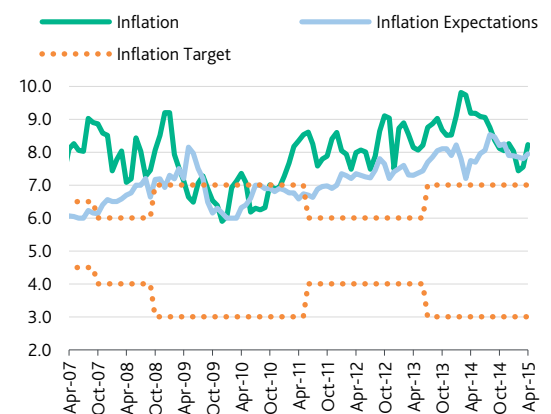


EXHIBIT 7

...weakens monetary policy credibility

%, year-on-year



Source: Haver Analytics and Moody's Investors Service

Not only have consumer prices shown high annual rates of inflation, but both actual inflation and inflation expectations have consistently exceeded the central bank's targeted range. The inability to meet these targets reflects weak policy effectiveness and low policy credibility (see Exhibit 7). The high dollarization of the economy and low levels of financial intermediation are a challenge to the management of monetary policy in Uruguay. Moreover, persistently high inflation rates weaken confidence in the peso, which itself curbs the economy's propensity to de-dollarize. The authorities' seeming tolerance for high inflation and lack of ability to bringing inflation back into the targeted range have undermined policy credibility, contributing to define a relatively high reference level for long-term inflationary expectations by economic agents.

In June 2013, the central bank began targeting monetary aggregates instead of the overnight interest rate and made known they would gradually reduce the pace of monetary expansion to 8% by mid-2015, down from an average of 12% before the announcement. The authorities highlighted that targeting the money supply will be a more effective tool for controlling inflation in Uruguay. Additionally, the central bank also announced that it would widen the inflation target band to 3%-7% from 4%-6% and extend the policy horizon to 24 months from 18 months.

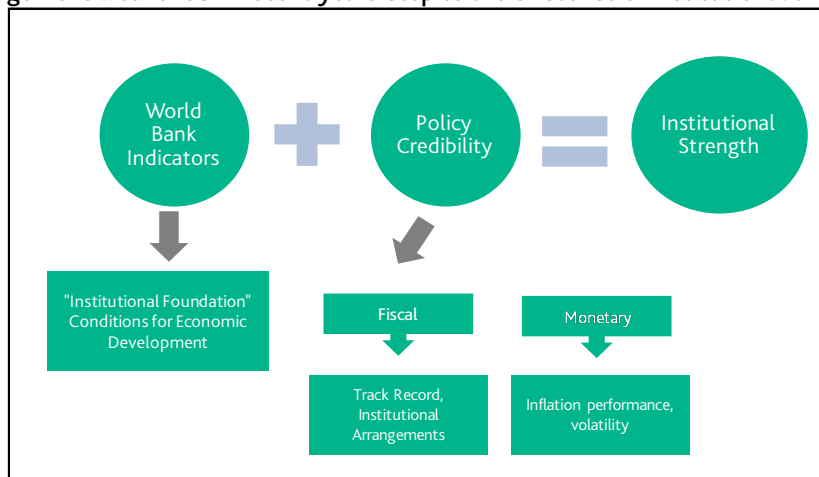
Despite the measures and a tightening of monetary policy, the effect has been marginal and as of end-April 2015 they have not brought inflation within the target range or had a significant effect on inflation expectations. The government has been increasingly resorting to heterodox measures to maintain the inflation rate below the 10% mark, including reducing public utility rates and striking price agreements with the private sector. Beyond the psychological effect of reaching double-digit inflation, the 10% mark is significant because it would trigger bi-yearly re-negotiation of wage contracts.

A mixed track record of fiscal management has undermined fiscal policy credibility

We believe that fiscal policy credibility is a function of both the track record of fiscal performance and the institutional arrangements that anchor it (see Exhibit 8). In this regard, the fiscal restraint exhibited through 2009 has abated and given way to a sustained weakening of structural fiscal balances reflecting expansion of social programs. The weakening comes despite the existence of a five-year budget framework and yearly ex-post revisions to fiscal performance.

EXHIBIT 8

Fiscal management weakened in recent years despite the existence of institutional arrangements



Sources: Moody's Investors Service

As a result of strong (above-potential) economic growth, government revenues frequently exceeded the authorities' original projections during 2005-2011 allowing the sovereign to accommodate increased spending without deviating from fiscal targets. Nevertheless, structural fiscal balances as calculated by the IMF have deteriorated on a sustained basis since 2009, with the structural deficit peaking in 2014. Headline deficits have also widened and halted the downward trend in debt metrics, despite a lengthy period of above-potential growth.

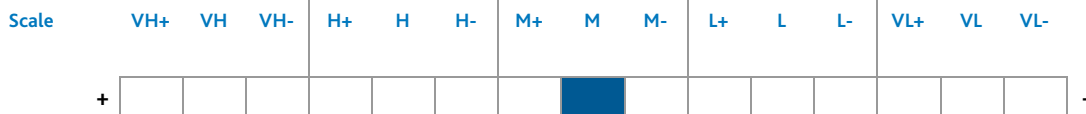
Uruguay's fiscal framework mandates that every new presidential administration that comes into office send to congress a proposed five-year budget within the first six months of its term. The budget and fiscal performance is reviewed on an annual basis. Although this institutional arrangement has helped anchor fiscal policy following the 2002 crisis, we note that the framework is not updated on a multi-year rolling basis, rather it guides performance only during the administration's term in office. Drawbacks include a lack of fiscal rules with sanction mechanisms, and little guidance for saving excess revenues from above-potential economic growth, which fosters pro-cyclical behavior.

As a result of these weaknesses, we believe that there is currently limited scope to respond to adverse shocks with counter-cyclical policies. Fiscal easing in the current context of lower growth would lead to an increase in government debt ratios and threaten the sustainability of public finances. In this regard, the automatic stabilizers built into Uruguay's tax regime and social spending would become the main policy tool for combating negative shocks. In such a scenario the level of economic growth would be the primary determinant of debt dynamics and the magnitude of potential fiscal deterioration.

Fiscal Strength: Moderate

If implemented, fiscal consolidation will support stable debt ratios

Factor 3



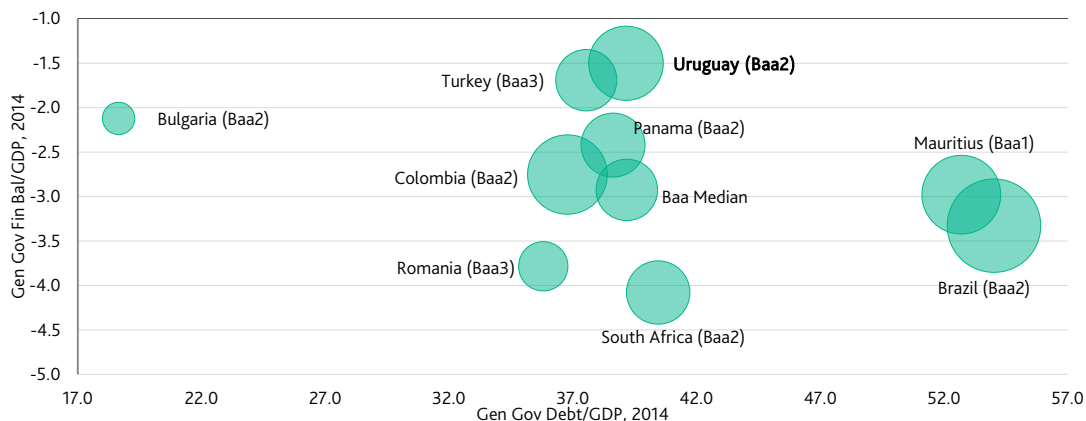
Fiscal strength captures the overall health of government finances, incorporating the assessment of relative debt burdens and debt affordability as well as the structure of government debt. Some governments have a greater ability to carry a higher debt burden at affordable rates than others. Fiscal strength is adjusted for the debt trend, the share of foreign currency debt in government debt, other public sector debt and for cases in which public sector financial assets or sovereign wealth funds are present. Depending on the adjustment factor the overall score of fiscal strength can be lowered or increased.

Uruguay's 'Moderate' fiscal strength assessment balances its relatively low central government debt burden, very strong liability management practices and fiscal reserve assets, against lingering vulnerabilities from having an elevated proportion of foreign currency debt and a relatively high interest burden. Debt ratios are very much in line with 'Baa' medians despite a weaker-than-peers debt affordability as measured by the interest payment-to-revenue ratio (see Exhibit 9). Sovereigns that share Uruguay's 'Moderate' fiscal strength ranking include Mauritius (Baa1 stable), Colombia (Baa2 stable) and Romania (Baa3 stable).

EXHIBIT 9

Uruguay's key fiscal metrics remain in line with peers

Size of the bubble = General government interest payments-to-revenue, 2014 (%)



Sources: Haver Analytics and Moody's Investors Service

Fiscal balance to remain unchanged in 2015, consolidation likely to begin in 2016

The central government deficit widened to 2.3% of GDP in 2014 from 1.5% in 2013. Current fiscal spending continued to grow faster than real GDP and exacerbated the sustained deterioration in the fiscal position since 2011. Revenue growth slowed to 9.2% in 2014 from over 17% the previous year, and was outpaced by a steady 13.6% growth in total expenditures.

Tax revenues declined to 16.5% of GDP from 17.1% in 2013 as a result of lower economic growth. Overall expenditures remained flat relative to GDP at 22.2%, reflecting increased pension payments following the

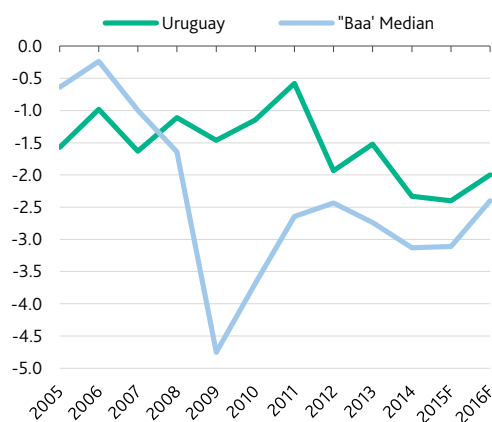
reforms to the system in 2009, and wage expense growth in excess of 15%. All major spending categories increased over 10%, although intermediate consumption growth was curbed to under 14% from 17.5% in 2013.

The lack of spending restraint during the Mujica administration (2010-15) resulted in a widening of the fiscal deficit every year that economic growth was under 5%, highlighting a weaker fiscal stance that relied on revenues derived from above-potential GDP growth in order to meet fiscal targets. As the economy shifts to a lower level of output growth, above-trend revenues will no longer be available to offset the current growth in expenditures. Although the deficit would continue deteriorating under a no-policy-change scenario and absent a strong increase in economic growth, the deterioration in the fiscal position would be limited and result in a modest increase in debt ratios that would not immediately threaten creditworthiness.

Nevertheless, the new administration of President Vazquez is committed to fiscal consolidation and ensuring the sustainability of public finances. Although the five-year budget has not yet been submitted to congress and specific consolidation measures have yet to be identified, the administration benefits from a proven track record of fiscal prudence from its previous term in office (2005-10). The authorities believe that expenditure restraint will be key to decreasing the fiscal imbalance, and are likely to focus their efforts on curbing wage and pension spending growth.

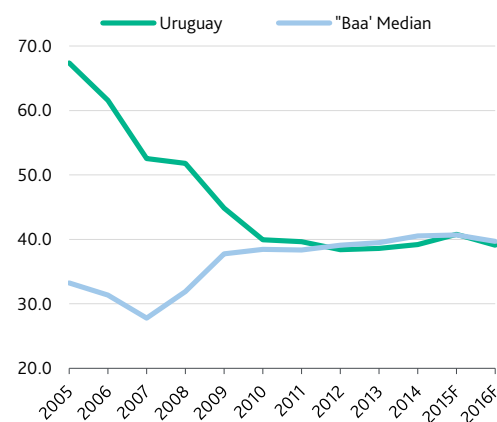
We forecast that the 2015 fiscal deficit will remain virtually unchanged, as consolidation measures would be implemented beginning 2016 after the new five-year budget framework is approved at the end of this year. Although nominal expenditure growth for 2015 is capped by the previous budget, suggesting a more limited increase in spending that would yield a lower deficit, the slowdown in economic activity in 2015 will also result in lower revenue growth that is likely to offset the expenditure savings. As a result, we expect that the deficit will reach 2.4% of GDP in 2015 and decrease to 2% in 2016 (see Exhibit 10).

EXHIBIT 10
Fiscal performance remains better than peers
General government financial balance (% GDP)



Source: Haver Analytics and Moody's Investors Service

EXHIBIT 11
Debt ratios also in line with 'Baa' medians
General government debt (% GDP)



Debt ratios will remain broadly stable through 2017

Fiscal easing, lower economic growth and the recent weakening of the exchange rate have halted the 2005-10 improvement in the sovereign's debt-to-GDP ratio and prompted a marginal increase to 39.2% in 2014 from a low of 38.4% in 2012 (see Exhibit 11). Despite the less benign trend, the sovereign's debt metrics remain well in line with 'Baa'-rated peers.

We forecast that debt will peak at just under 41% of GDP in 2015 and remain broadly stable at around 40% through 2017 given a slow but steady pace of fiscal consolidation. Risks to our forecast are balanced. Downside risks stem from a delay in tightening the fiscal stance to which we attribute a moderate probability, or a protracted period of low growth in Uruguay and its neighbors along with strong negative pressure on the exchange rate, a scenario with a low-to-moderate probability of occurring. The main upside risk comes from a stronger-than-expected recovery in economic activity related to Argentine growth performance that would result in a quickened pace of consolidation and a downward trend in debt metrics, which has a moderate probability of materializing in 2016.

Strong liability management and financial buffers are key credit strengths

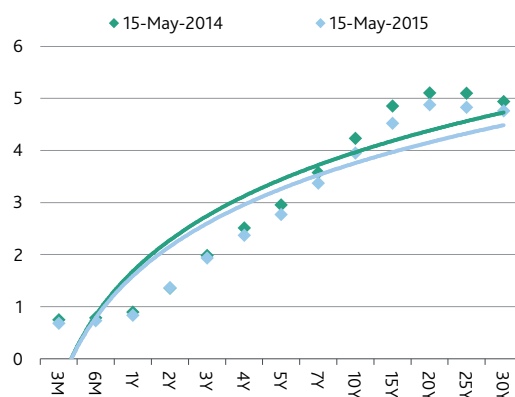
The government's debt management strategy has been focused on (1) reducing the share of foreign currency-denominated debt, (2) extending average debt maturity, and (3) building up financial buffers through precautionary liquidity reserves and contingent credit lines.

Although the sovereign's share of foreign currency-denominated debt remains elevated relative to peers at 48% versus a 'Baa' median of 29.7%, there has been a strong reduction over the past decade from levels of around 90%. We believe that further reductions in foreign currency debt are unlikely given the limited size of the domestic pool of financing and the lower cost of issuing externally relative to local-currency funding.

Liability operations by the debt management office have yielded a favorable maturity profile that currently stands at over 15 years, which is among the longest for sovereigns rated by Moody's. The sovereign's lengthy average maturity of debt greatly decreases rollover risk and allows the authorities to take a very opportunistic approach for issuing debt at favorable terms. In February, the sovereign reopened its 2050 global bonds, issuing \$1.2 billion at a yield of about 5 percent (see Exhibit 12), among the lowest in emerging market external issuances at comparable maturities at the time.

EXHIBIT 12

Uruguay sovereign global (\$) yield curve (%)

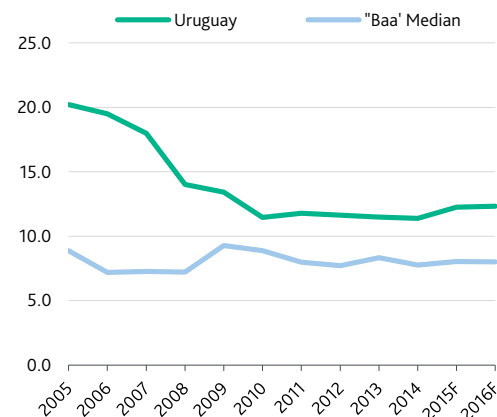


Source: Bloomberg, Haver Analytics and Moody's Investors Service

EXHIBIT 13

Overall affordability of debt is weaker than peers

General government interest-to-revenues (%)



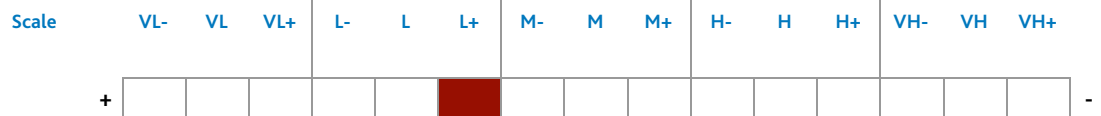
Nevertheless, extending the average maturity of debt and increasing the share of local currency debt has come at a price. The sovereign's interest-to-revenue ratio, an important measure of creditworthiness, remains elevated compared to peers despite a similar debt burden (see Exhibit 13), and reflects the high proportion of local currency debt that is indexed to inflation and the cost of developing a domestic debt market over a relatively short period of time.

Precautionary contingent credit lines have become an integral part of Uruguay's sovereign credit profile providing an additional financial buffer that further reduces credit risk and complements the sovereign's own cash reserves. Precautionary cash reserves that cover maturing principal payments for the next two years reached 3.8% of GDP, at year-end 2014. Additionally, the sovereign has access to contingent credit lines with multi-lateral development banks (WB, IADB, CAF, and FLAR) that are available on call for a total of 3.5% of GDP.

Susceptibility to Event Risk: Low (+)

Credit vulnerabilities sufficiently offset by buffers

Factor 4



Susceptibility to Event Risk evaluates a country's vulnerability to the risk that sudden events may severely strain public finances, thus increasing the country's probability of default. Such risks include political, government liquidity, banking sector and external vulnerability risks. Susceptibility of Event Risk is a constraint which can only lower the preliminary rating range as given by combining the first three factors.

We assess Uruguay's susceptibility to event risk as 'Low (+)'. Uruguay shares the ranking with Mauritius (Baa1 stable), Brazil (Baa2 negative), and Romania (Baa3 stable), among others. Event risk takes into consideration (1) political risks, both domestic and geopolitical; (2) government liquidity risk; (3) banking sector risks involving the crystallization of contingent liabilities on the sovereign's balance sheet; and (4) external vulnerability, reflecting balance of payments risks and exposure to sudden stops.

Track-record of policy continuity underpins very low domestic political risk

Political event risk is considered to be low on account of the policy continuity that different governments across the political spectrum have maintained. Credit risks resulting from political events are very low given that successive administrations have repeatedly endorsed principles that have led to conservative economic policies and the maintenance of macroeconomic stability.

President Vazquez's administration took office on 1 March 2015 and the president enters his second non-consecutive term of office with a strong mandate. We expect policies will remain broadly similar to those pursued by the outgoing administration, with a continued emphasis on social development (including healthcare, education and social transfers), but a greater focus on administrative efficiency. Main policy challenges include narrowing the fiscal deficit in a context of lower output growth, reducing inflation and pursuing reforms to add dynamism to economic activity.

Low borrowing requirements supports low government liquidity risk

A favorable maturity profile translates into low rollover risks. Given Uruguay's extended debt maturity, the government faces modest refinancing requirements over the medium term given yearly principal payments of 1.5%-2% of GDP over the next 5 years.

Combined with moderate fiscal deficits, the modest amounts of maturing debt result in fairly low gross financing needs. The sovereign's gross financing needs are likely to remain below 5% of GDP every year through 2019, among the lowest in the region for sovereigns rated 'Baa' and above.

Despite elevated financial dollarization, banking sector risk is low

Risk in the banking sector is deemed to be low. Key strengths of the banking system include: (1) high asset quality, with non-performing loans (NPLs) contained at under 2% of gross loans; (2) limited risk to the sovereign's balance sheet given the small size of the system (total system assets are under 35% of GDP); and (3) relatively high liquidity with the sector's loan-to-deposit ration remaining under 60%.

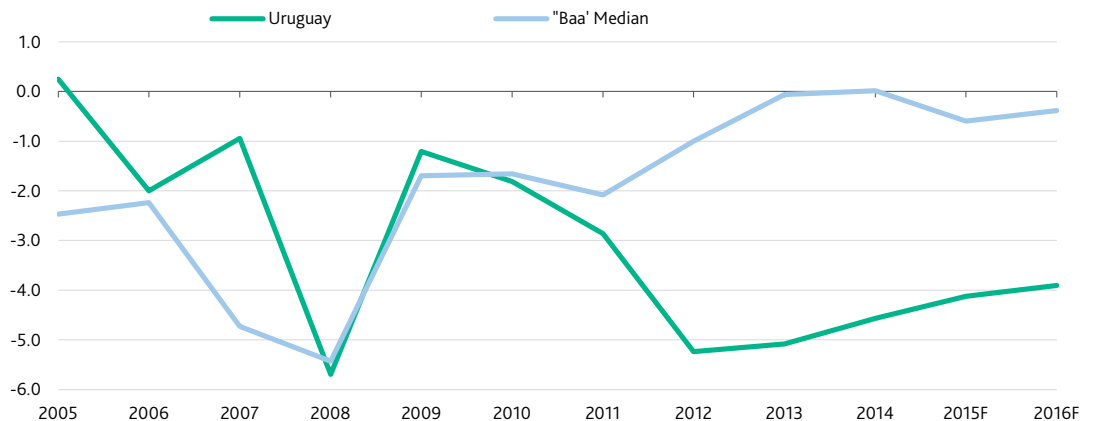
These strengths offset lingering concerns about the elevated level of financial dollarization, especially in terms of deposits. Foreign currency-denominated deposits account for 76% of the total, while dollar-denominated loans remain high at approximately half of the system's lending portfolio.

Deteriorating services balance will partly offset the benefits of lower energy prices, but current account deficit set to narrow

Changes in Uruguay's current account deficit largely reflect oil import dynamics and movements in the services balance (see Exhibit 14). Although the external imbalance has been covered by FDI since 2005 (with one exception, in 2012), the surplus on the net services balance has deteriorated substantially since 2011 due to lower tourism receipts from Argentina. Moreover, a drought in 2012 that necessitated higher oil imports for electricity generation exacerbated the negative shock and caused the deficit to widen to 5.2% of GDP from 2.9% in 2011.

EXHIBIT 14

Lower tourism inflows accounted for the brunt of the deterioration in the current account (% GDP)



Sources: Haver Analytics and Moody's Investors Service

As a result of the drought and increased oil imports in 2012, the state-owned power company, UTE, bore the cost of the increased oil imports, which had a negative effect on government finances. In 2013, the beginning of a prolonged economic slowdown and tighter foreign exchange controls in Argentina aggravated the negative shock from increased oil imports, maintaining Uruguay's current account deficit at 5.1% of GDP. With the transitory drought shock fading, a lower oil import bill contributed to narrowing the external imbalance to 4.6% of GDP, and the continued decline in oil prices through early 2015 will help decrease imports.

A comprehensive overhaul of the country's energy matrix through heavy investment in renewable energy (including wind and biomass) from 2010-2017 will eliminate reliance on fuel oil for electricity generation, and lower the share of energy generated by hydro power. The new matrix will curb existing vulnerabilities that can negatively affect economic growth and the fiscal and external accounts.

We forecast the current account deficit will gradually narrow toward 3.9% of GDP in 2016 given lower oil prices and decreased domestic demand for imports. A further deterioration in the services balance from lower tourism receipts should be marginal as we believe that the brunt of the adjustment has already taken place. The balance of risks is skewed to the upside. The external imbalance could strongly benefit from a recovery in Argentina's economy or a loosening of foreign exchange controls.

Although downside risks could materialize, we expect FDI will continue to cover most of the current account deficit. Despite the persistent deficit, the external indebtedness of the economy remains subdued, reflected in a low 14% of GDP deficit of the net international investment position. Official foreign exchange reserves reached 30% of GDP at the end of 2014, among the highest levels in the 'Baa' category, providing ample coverage for external payments in the event of a sudden stop and helping to keep vulnerabilities in check.

Rating Range

Combining the scores for individual factors provides an indicative rating range. While the information used to determine the grid mapping is mainly historical, our ratings incorporate expectations around future metrics and risk developments that may differ from the ones implied by the rating range. Thus, the rating process is deliberative and not mechanical, meaning that it depends on peer comparisons and should leave room for exceptional risk factors to be taken into account that may result in an assigned rating outside the indicative rating range. For more information please see our [Sovereign Bond Rating Methodology](#).

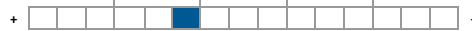
Sovereign Rating Metrics: Uruguay

Economic Strength

How strong is the economic structure?

Sub-Factors: Growth Dynamics, Scale of the Economy, Wealth

VH+ VH VH- H+ H H- M+ M M- L+ L L- VL+ VL VL-



Institutional Strength

How robust are the institutions and how predictable are the policies?

Sub-Factors: Institutional Framework and Effectiveness, Policy Credibility and Effectiveness

VH+ VH VH- H+ H H- M+ M M- L+ L L- VL+ VL VL-



Fiscal Strength

How does the debt burden compare with the government's resource mobilization capacity?

Sub-Factors: Debt Burden, Debt Affordability

VH+ VH VH- H+ H H- M+ M M- L+ L L- VL+ VL VL-



Susceptibility to Event Risk

What is the risk of a direct and sudden threat to debt repayment?

Sub-Factors: Political Risk, Government Liquidity Risk, Banking Sector Risk, External Vulnerability Risk

VL- VL VL+ L- L L+ M- M M+ H- H H+ VH- VH VH+



Economic Resiliency

VH+ VH VH- H+ H H- M+ M M- L+ L L- VL+ VL VL-



Government Financial Strength

VH+ VH VH- H+ H H- M+ M M- L+ L L- VL+ VL VL-



Rating Range:
Baa1-Baa3

Assigned Rating:
Baa2

Comparatives

This section compares credit relevant information regarding Uruguay with other sovereigns rated by Moody's Investors Service. It focuses on a comparison with sovereigns within the same rating range and shows the relevant credit metrics and factor scores.

EXHIBIT 15

Uruguay Key Peers

	Year	Uruguay	Panama	Mauritius	Turkey	Colombia	Bulgaria	Baa2 Median	Latin America & Caribbean Median
Rating/Outlook		Baa2/STA	Baa2/STA	Baa1/STA	Baa3/NEG	Baa2/STA	Baa2/STA	Baa2	Ba2
Rating Range		Baa1 - Baa3	A3 - Baa2	Baa1 - Baa3	Baa1 - Baa3	Baa2 - Ba1	Baa3 - Ba2	Baa1 - Baa3	Baa3 - Ba2
Factor 1		M+	H-	M	H	H-	L+	H-	M-
Nominal GDP (US\$ Bn)	2014	57.5	46.2	12.7	799.5	377.9	55.7	246.6	40.0
GDP per Capita (PPP, US\$)	2014	19,679	18,418	17,716	18,994	12,806	17,222	19,048	12,806
Avg. Real GDP (% change)	2010-2019	4.1	7.1	3.5	3.4	4.0	0.9	2.1	2.8
Volatility in Real GDP growth (ppts)	2005-2014	1.6	2.4	1.1	4.6	1.6	3.9	2.3	2.4
Global Competitiveness Index, percentile [1]	2015	31.5	57.8	65.7	60.5	42.9	52.6	52.6	28.9
Factor 2		H-	M	H+	M+	M+	M+	M+	M-
Government Effectiveness, percentile [1]	2013	56.2	53.9	67.1	55.4	45.3	48.4	54.3	38.2
Rule of Law, percentile [1]	2013	61.7	40.6	72.6	50.0	31.2	44.5	45.3	30.4
Control of Corruption, percentile [1]	2013	82.0	35.9	60.9	56.2	31.2	40.6	44.1	35.1
Avg. Inflation (% change)	2010-2019	7.7	3.8	4.3	7.0	2.9	2.0	3.7	4.0
Volatility in Inflation (ppts)	2005-2014	1.3	2.4	2.7	1.3	1.6	3.4	1.7	2.3
Factor 3		M	H+	M	M+	M	H	M	M+
Gen. Gov. Debt/GDP	2014	39.2	39.5	54.1	33.5	37.3	27.0	40.9	37.8
Gen. Gov. Debt/Revenues	2014	197.1	198.3	265.2	86.4	236.7	74.2	197.7	188.0
Gen. Gov. Interest Payments/Revenue	2014	11.4	8.4	12.7	7.7	13.6	2.0	9.2	8.8
Gen. Gov. Interest Payments/GDP	2014	2.3	1.8	2.6	3.0	2.3	0.7	2.4	2.0
Gen. Gov. Financial Balance/GDP	2014	-2.3	-4.1	-3.2	-1.4	-2.4	-2.8	-2.9	-2.6
Factor 4		L+	M-	L+	H-	M-	M+	M-	M-
Current Account Balance/GDP	2014	-4.6	-11.4	-7.2	-5.8	-5.2	0.9	-1.8	-4.5
Gen. Gov. External Debt/Gen. Gov. Debt	2014	36.0	36.4	24.4	34.9	50.7	--	28.4	55.1
External Vulnerability Indicator	2016F	61.6	19.5	12.3	176.8	51.0	57.8	40.8	57.8

Notes:

[1] Moody's calculations. Percentiles based on our rated universe.

Source: Moody's, national sources

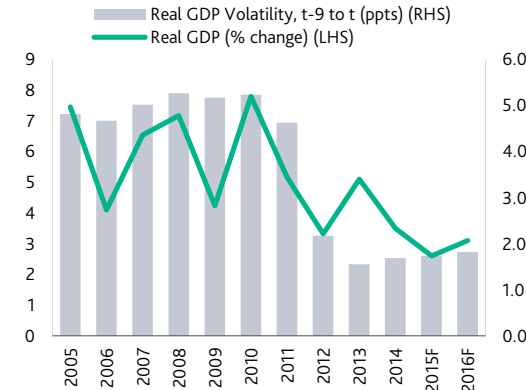
Appendices

Chart Pack

Uruguay

EXHIBIT 16

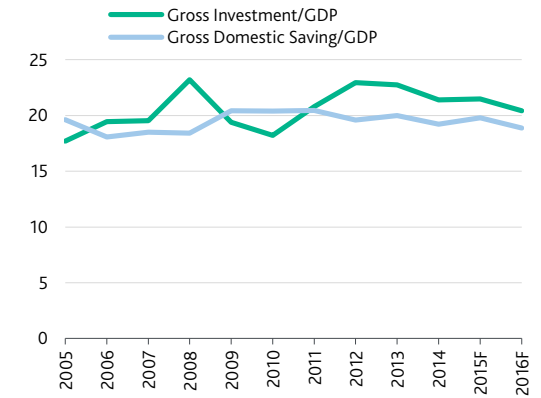
Economic Growth



Source: Moody's

EXHIBIT 17

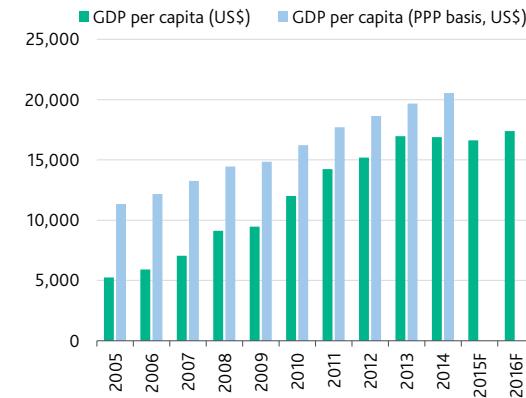
Investment and Saving



Source: Moody's

EXHIBIT 18

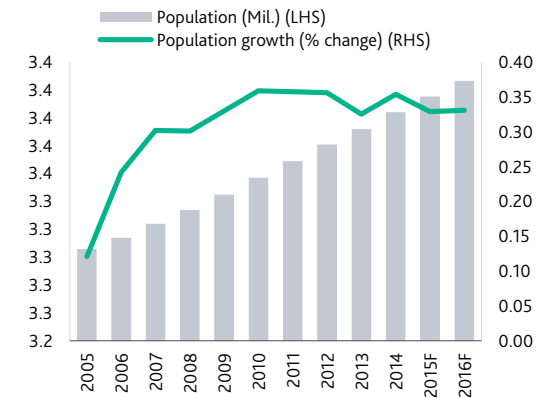
National Income



Source: Moody's

EXHIBIT 19

Population

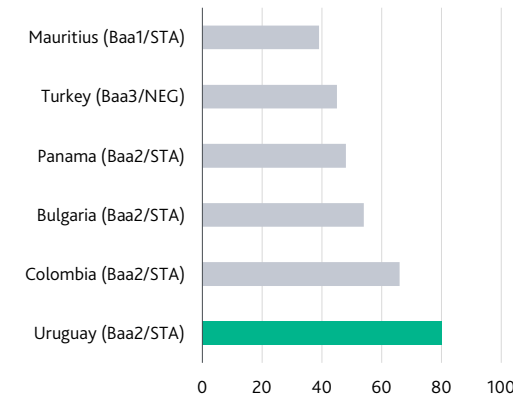


Source: Moody's

EXHIBIT 20

Global Competitiveness Index

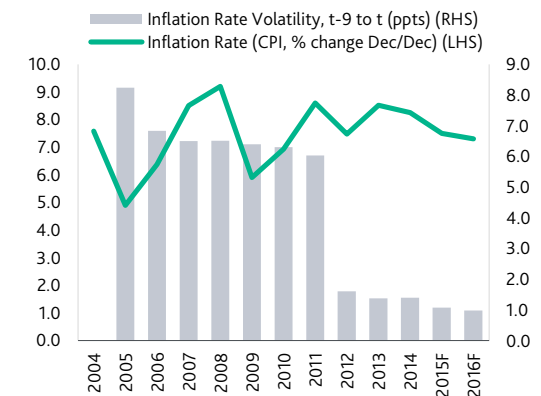
Rank [80] out of 144 countries



Source: World Economic Forum

EXHIBIT 21

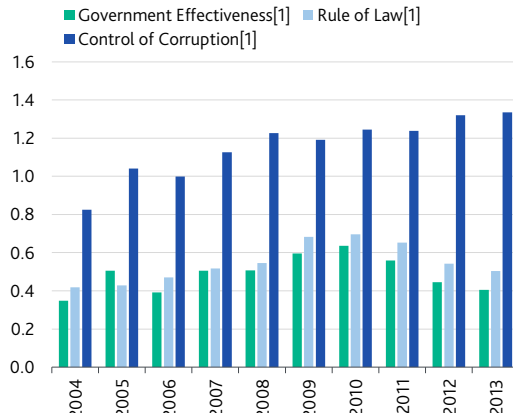
Inflation and Inflation Volatility



Source: Moody's

EXHIBIT 22

Institutional Framework and Effectiveness

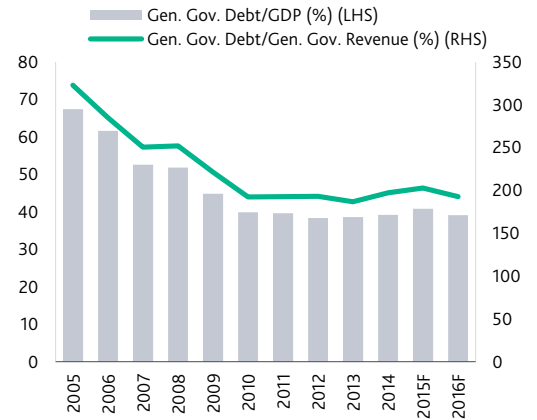


Notes: [1] Composite index with values from about -2.50 to 2.50: higher values correspond to better governance.

Source: World Bank Governance Indicators

EXHIBIT 23

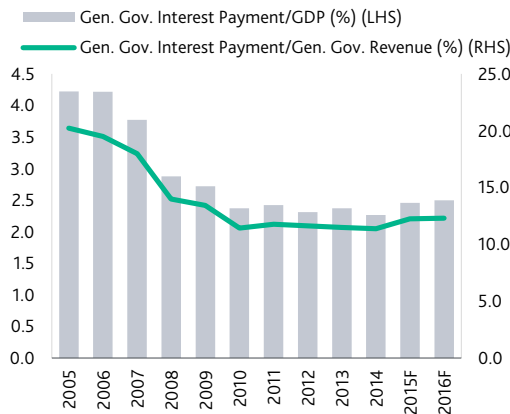
Debt Burden



Source: Moody's

EXHIBIT 24

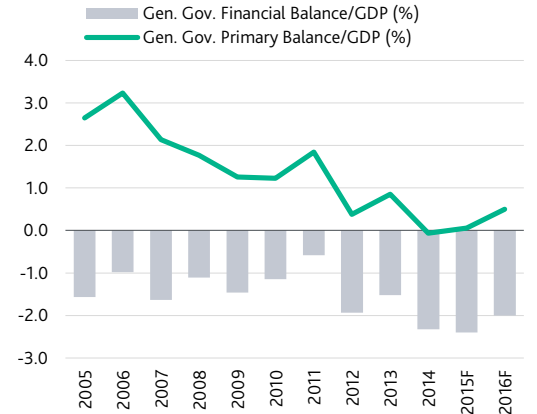
Debt Affordability



Source: Moody's

EXHIBIT 25

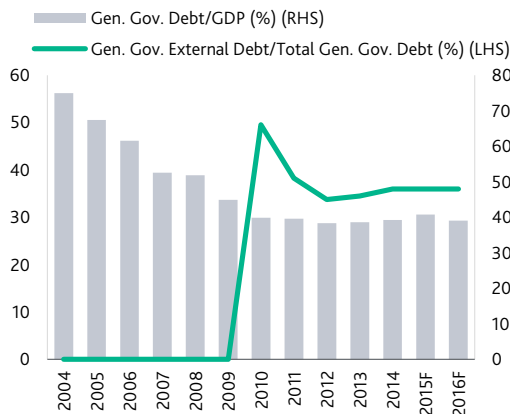
Financial Balance



Source: Moody's

EXHIBIT 26

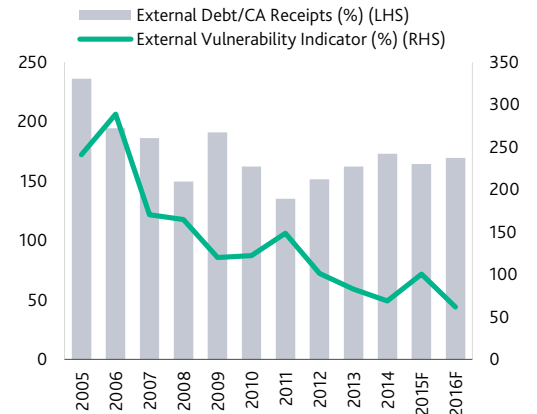
Government Liquidity Risk



Source: Moody's

EXHIBIT 27

External Vulnerability Risk



Source: Moody's

Rating History

Uruguay

	Government Bonds			Foreign Currency Ceilings				Date
	Foreign Currency	Local Currency	Outlook	Bonds & Notes		Bank Deposit		
Rating Affirmed	Baa2	Baa2	Stable	--	--	--	--	May-15
Rating Raised	Baa2	Baa2	Stable	A2	--	Baa2	--	May-14
Rating Raised	Baa3	Baa3	Positive	--	--	Baa3	--	July-12
Outlook Changed	Ba1	Ba1	Positive	--	--	--	--	January-12
Rating Raised	Ba1	Ba1	Stable	Baa1	--	Ba2	--	December-10
Review for Upgrade	Ba3	Ba3	RUR+	--	--	--	--	July-10
Rating Raised	Ba3	Ba3	Stable	Ba1	--	B1	--	January-09
Review for Upgrade	B1	B1	RUR+	--	--	--	--	August-08
Rating Raised	B1	B1	Stable	Ba2	--	B2	--	December-06
Review for Upgrade	B3	B3	RUR+	--	--	Caa1	--	September-06
Rating Raised	--	--	--	B1	--	--	--	May-06
Outlook Changed	B3	B3	Stable	--	--	--	--	November-04
Rating Lowered	B3	B3	Negative	B3	--	Caa1	--	July-02
Rating Lowered	B1	B1	Negative	B1	--	B3	--	July-02
Review for Downgrade	Ba2	Ba2	RUR-	Ba2	--	Ba3	--	May-02
Rating Lowered	Ba2	Ba2	Negative	Ba2	NP	Ba3	NP	May-02
Review for Downgrade	Baa3	Baa3	RUR-	Baa3	P-3	Baa3	P-3	April-02
Outlook Changed	--	--	Negative	--	--	--	--	February-02
Rating Assigned	--	Baa3	--	--	--	--	--	October-98
Rating Raised	Baa3	--	--	Baa3	P-3	Baa3	P-3	June-97
Outlook Assigned	--	--	Stable	--	--	--	--	March-97
Rating Assigned	--	--	--	--	NP	Ba2	NP	October-95
Rating Assigned	Ba1	--	--	Ba1	--	--	--	October-93

Annual Statistics

Uruguay

	2007	2008	2009	2010	2011	2012	2013	2014	2015F	2016F
Economic Structure and Performance										
Nominal GDP (US\$, Bil.)	23.4	30.4	31.7	40.3	48.0	51.4	57.5	57.5	56.8	59.6
Population (Mil.)	3.3	3.3	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4
GDP per capita (US\$)	7,043	9,108	9,465	12,000	14,236	15,198	16,959	16,883	16,618	17,392
GDP per capita (PPP basis, US\$)	13,258	14,444	14,847	16,235	17,723	18,638	19,679	20,556	--	--
Nominal GDP (% change, local currency)	16.6	15.8	12.3	13.1	14.6	12.7	12.9	13.4	10.1	10.4
Real GDP (% change)	6.5	7.2	4.2	7.8	5.2	3.3	5.1	3.5	2.6	3.1
Inflation (CPI, % change Dec/Dec)	8.5	9.2	5.9	6.9	8.6	7.5	8.5	8.3	7.5	7.3
Gross Investment/GDP	19.5	23.2	19.4	18.2	20.8	22.9	22.7	21.4	21.5	20.4
Gross Domestic Saving/GDP	18.5	18.4	20.4	20.4	20.4	19.6	20.0	19.2	19.8	18.9
Nominal Exports of G & S (% change, US\$ basis)	14.8	34.7	-6.5	23.7	19.4	4.9	1.6	-0.5	3.2	3.0
Nominal Imports of G & S (% change, US\$ basis)	13.7	50.7	-21.6	22.6	26.1	16.0	1.0	-2.7	1.0	2.5
Openness of the Economy [1]	59.2	65.2	53.4	51.7	53.3	54.9	49.7	48.9	48.7	48.5
Government Effectiveness [2]	0.51	0.51	0.60	0.64	0.56	0.44	0.41	--	--	--
Government Finance										
Gen. Gov. Revenue/GDP [3]	21.0	20.6	20.3	20.7	20.6	19.9	20.7	19.9	20.1	20.3
Gen. Gov. Expenditures/GDP [3]	22.6	21.7	21.7	21.9	21.1	21.8	22.2	22.2	22.5	22.3
Gen. Gov. Financial Balance/GDP [3]	-1.6	-1.1	-1.5	-1.1	-0.6	-1.9	-1.5	-2.3	-2.4	-2.0
Gen. Gov. Primary Balance/GDP [3]	2.1	1.8	1.3	1.2	1.8	0.4	0.9	-0.1	0.1	0.5
Gen. Gov. Debt (US\$ Bil.) [3]	13.43	13.54	16.33	16.05	18.45	20.65	21.25	21.53	21.81	23.51
Gen. Gov. Debt/GDP [3]	52.5	51.8	44.9	39.9	39.6	38.4	38.6	39.2	40.8	39.1
Gen. Gov. Debt/Gen. Gov. Revenue [3]	250.4	252.1	221.3	192.4	192.8	193.0	186.8	197.1	202.9	192.6
Gen. Gov. Int. Pymt/Gen. Gov. Revenue [3]	18.0	14.0	13.4	11.4	11.8	11.6	11.5	11.4	12.2	12.3
Gen. Gov. FC & FC-indexed Debt/GG Debt [3]	74.0	72.0	69.0	66.0	51.0	45.0	46.0	48.0	48.0	48.0
External Payments and Debt										
Nominal Exchange Rate (local currency per US\$, Dec)	21.50	24.35	19.63	20.09	19.90	19.40	21.39	24.33	27.50	27.00
Real Eff. Exchange Rate (% change)	0.27	9.52	2.69	11.92	1.97	3.13	6.63	-1.69	--	--
Current Account Balance (US\$ Bil.)	-0.22	-1.73	-0.38	-0.73	-1.37	-2.69	-2.92	-2.62	-2.34	-2.33
Current Account Balance/GDP	-0.9	-5.7	-1.2	-1.8	-2.9	-5.2	-5.1	-4.6	-4.1	-3.9
External Debt (US\$ Bil.)	14.86	15.42	17.97	18.43	18.34	21.12	22.86	24.26	23.80	25.26
Public Sector External Debt/Total External Debt	76.6	71.7	73.0	71.5	78.7	78.9	78.9	78.7	78.8	79.0
Short-term External Debt/Total External Debt	23.9	27.4	27.8	28.1	21.1	22.9	21.9	22.1	22.7	22.5
External Debt/GDP	58.2	59.0	49.4	45.8	39.4	39.3	41.5	44.2	44.5	42.0
External Debt/CA Receipts [4]	186.2	149.5	190.8	162.0	135.1	151.4	162.2	172.9	164.4	169.4
Interest Paid on External Debt (US\$ Bil.) [5]	0.67	0.60	0.53	0.58	0.60	0.53	0.76	0.78	0.85	0.77
Amortizations Paid on External Debt (US\$ Bil.) [5]	0.36	0.75	0.44	1.24	2.24	2.32	2.07	1.58	7.20	0.84
Net Foreign Direct Investment/GDP	5.3	7.0	4.8	5.8	5.2	4.9	5.3	4.8	4.2	4.0
Net International Investment Position/GDP	-9.0	-6.7	-10.1	-6.1	-10.0	-14.4	-13.9	--	--	--
Official Forex Reserves (US\$ Bil.)	4.11	6.35	7.64	7.17	9.77	13.06	15.72	17.02	18.00	18.70
Net Foreign Assets of Domestic Banks (US\$ Bil.)	2.34	1.72	2.79	4.91	4.76	3.65	3.02	3.05	--	--

Uruguay

	2007	2008	2009	2010	2011	2012	2013	2014	2015F	2016F
Monetary, Vulnerability and Liquidity Indicators										
M2 (% change, Dec/Dec)	3.8	28.6	-2.6	22.1	18.0	10.0	19.2	19.3	--	--
Monetary Policy Rate (% per annum, Dec 31)	7.25	7.75	6.25	6.50	8.75	9.25	9.25	9.25	--	--
Domestic Credit (% change Dec/Dec)	-8.0	61.1	-9.4	27.7	6.2	20.2	27.4	13.8	--	--
Domestic Credit/GDP	25.0	34.8	28.1	31.7	29.4	31.3	35.4	35.5	--	--
M2/Official Forex Reserves (X)	2.5	1.9	1.9	2.4	2.1	1.7	1.6	1.5	--	--
Total External Debt/Official Forex Reserves	361.3	243.0	235.1	257.0	187.9	161.8	145.4	142.5	132.2	135.1
Debt Service Ratio [5] [6]	12.9	13.1	10.2	16.0	20.9	20.4	20.1	16.8	55.6	10.8
External Vulnerability Indicator [7]	170.4	164.5	120.0	122.1	148.5	101.0	82.9	68.8	100.3	61.6
Liquidity Ratio [8]	19.2	25.0	26.5	25.9	40.6	47.9	59.1	72.0	--	--
Total Liab. due BIS Banks/Total Assets Held in BIS Banks	24.1	26.9	27.8	41.9	50.7	48.1	62.1	63.6	--	--
"Dollarization" Ratio [9]	79.8	81.9	78.1	75.3	72.4	72.2	73.7	76.6	--	--
"Dollarization" Vulnerability Indicator [10]	110.3	105.3	94.7	92.4	85.0	83.1	81.6	84.1	--	--

Notes:

[1] Sum of Exports and Imports of Goods and Services/GDP

[2] Composite index with values from -2.50 to 2.50: higher values suggest greater maturity and responsiveness of government institutions

[3] Central government

[4] Current Account Receipts

[5] Excludes private sector before 2010

[6] (Interest + Current-Year Repayment of Principal)/Current Account Receipts

[7] (Short-Term External Debt + Currently Maturing Long-Term External Debt + Non Resident Deposits due over one year)/Official Foreign Exchange Reserves

[8] Liabilities to BIS Banks Falling Due Within One Year/Total Assets Held in BIS Banks.

[9] Total Foreign Currency Deposits in the Domestic Banking System/Total Deposits in the Domestic Banking System

[10] Total Foreign Currency Deposits in the Domestic Banking System/(Official Foreign Exchange Reserves + Foreign Assets of Domestic Banks)

Moody's Related Research

Credit Opinion:

- » [Uruguay, Government of](#)

Sovereign Outlook – Latin America:

- » [Credit profiles stabilizing amid lower growth, moderate external vulnerabilities, March 2015 \(1003498\)](#)

Rating Methodologies:

- » [Sovereign Bond Ratings, September 2013 \(157547\)](#)
- » [Sovereign Default and Recovery Rates 1983-2014, April 2015 \(1004870\)](#)

Moody's Website Links:

- » [Sovereign Risk Group Webpage](#)
- » [Sovereign Ratings List](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Related Websites

For additional information, please see:

- » The Ministry of Economy and Finance's website: <https://www.mef.gub.uy/>
- » The Central Bank's website: <http://www.bcu.gub.uy/Paginas/Default.aspx>

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