R&I

NEWS RELEASE

May 02, 2011

The Oriental Republic of Uruguay: R&I Affirms BB, Stable

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

ISSUER: **The Oriental Republic of Uruguay**
Foreign Currency Issuer Rating: BB, Affirmed
Rating Outlook: Stable

RATIONALE:

The economy of Uruguay has been robust. With the current balance deficit controlled at low levels and direct investment rising, the country has few concerns about its international balance of payments. Uruguay continues to exercise fiscal discipline under the Financial Responsibility Law; its fiscal concerns are thus few. That said, its robust economy is partially assisted by accelerated inflows of capital due to quantitative easing by the advanced European countries and the U.S. The rising inflationary pressure resulting from capital inflows is a cause for concern. In consideration of such circumstances, R&I has affirmed the BB Foreign Currency Issuer Rating with a Stable Rating Outlook. A rating upgrade may come into sight if stable economic management paves the way for improving fiscal conditions despite possible changes in the global financial environment.

Uruguay's real GDP in 2010 grew 8.5% from a year earlier. With its private consumption and investment acting as a growth driver, the country rebounded strongly from the global financial crisis. Exports centering on primary products such as beef have been firm. This has somewhat offset the negative impact on the economy from the rising imports associated with expansion of domestic demand. Overseas direct investments have grown in various sectors including papermaking, farming/stock-raising, auto parts and call center and this is expected to shore up economic growth potential over the medium to long term. Regarding the growth projection for 2011, the government cited in March a possible upward revision to its previous estimate of 4.5%.

Meanwhile, the inflation rate is gaining speed, with CPI rising 7.7% in February, exceeding the upper end of the target range of 7% set under Uruguay's monetary policy. The central bank raised the policy rate by 100 basis points to 7.5% on March 26. Despite its stance of a tighter monetary policy, whether the central bank will be able to contain inflationary pressure remains to be seen. There also remains a possibility that capital outflows will occur if quantitative easing is reversed in the advanced European countries and the U.S. Implications for the real economy should be remarkable if the central bank is forced to implement additional sharp rate hikes. Even so, the current account deficit is small, and Uruguay secures international reserves equivalent to more than nine months' worth of goods and services imports. R&I believes there is limited concern about an immediate shortage of foreign currency liquidity.

Uruguay's fiscal deficit has been kept at low levels since 2005, when the country enacted the Financial Responsibility Law, which tightened budget control for the public sector. With the interest payment burden eased through reduction of the debt ratio, coupled with a recovery of public companies' results, the fiscal deficit of the public sector in 2010 was contained at 1.1% of GDP, which was basically in line with the budget. The government plans by 2014 to further reduce fiscal deficit to 0.8% and cut the public debt ratio to around 40% from 57.6% at the end of 2010, while keeping the ratio of annual capital spending for social infrastructure to GDP at a high level of 3.5%.

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.
http://www.r-i.co.jp/eng/cfp/about/methodology/index.html

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