

Jan 20, 2012

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

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: Positive, Changed from Stable

RATIONALE:

Uruguay's economy is expanding steadily. The fiscal and financial systems have remained somewhat sound, and the current account deficit is limited. On the other hand, upward pressure on wages is strong and the inflation rate is fairly high. Slowing economies in Brazil and Argentina are also concerns. That said, R&I feels that Uruguay is now more resilient against external shocks, and has affirmed the Foreign Currency Issuer Rating at BB while changing the Rating Outlook to Positive. Even amidst challenging external conditions, there is a good probability that Uruguay's rating may be upgraded as long as the country can maintain steady economic and fiscal management.

Private consumption and investment drive Uruguay's economy. Real gross domestic production (GDP) rose 8.5% in 2010 and also appears to have reached the 6%-6.5% level in 2011 as well. Exports of primary goods like beef and dairy products are strong, and this absorbs the downward pressure on the economy from rising imports as domestic demand grows. There is active investment from abroad across a variety of fields, including paper manufacturing, agriculture and cattle breeding, automobile parts, and call centers. Expectations are higher that the economy will continue to expand over the medium to long terms.

Uruguay's current account deficit is small, and the country has enough foreign currency reserves for 10 months of imports of goods and services. The ratio of non-resident bank deposits has dropped considerably, so there is less risk of an outflow of funds. The banking system currently has ample liquidity. It maintains sufficient provisions for non-performing loans, as well as appropriate levels of core capital. Conditions do not warrant concerns about bank soundness.

Under the Fiscal Responsibility Law, public sector budget spending has been tightened, and this has resulted in the fiscal deficit being held to less than 2% of GDP since 2005. Uruguay's public debt balance stood at 56% of GDP as of end-September 2011. Though not a light burden, this is a considerable improvement from earlier levels. The government plans to cut the ratios of the fiscal deficit and public debt to GDP to 0.8% and 40%, respectively, by 2014. The ratio of rigid expenses like pension payments, public sector employee salaries, and interest payments is high and shrinking the fiscal deficit will not be easy, but R&I feels the targets can be achieved if Uruguay's government does not slip in exercising fiscal discipline while maintaining economic growth.

Amidst such economic conditions, Uruguay's unemployment rate was very low at 5.5% in November 2011. Collective wage agreements negotiated in the face of such a tight labor market lead to the expectation that wages will show strong growth in a number of sectors through 2014. The consumer price index (CPI) stands at more than 8%, above the 6% upper end of the inflation target range, and it is unlikely that inflation will ease for some time.

Uruguay's central bank has hiked interest rates multiple times since March 2011 and also raised the reserve requirement ratio significantly in May. Whether such monetary tightening measures will quell inflation remains to be seen. The real economy will also be impacted if significant rate hikes continue. The economies of neighboring countries Brazil and Argentina, which had been enjoying robust growth, have already started to correct. R&I will pay close attention to Uruguay's official policy management to see if the inflation rate can be lowered without the economy slowing considerably.

The primary rating methodology applied to this rating is provided at "R&I's Analytical Approach to

■Contact : Investors Service Division TEL.+81-(0)3-3276-3511 E-mail. infodept@r-i.co.jp
■Media Contact : Corporate Planning Division (Public Relations) TEL.+81-(0)3-3276-3438

Rating and Investment Information, Inc. Nihonbashi 1-chome Bldg., 1-4-1, Nihonbashi, Chuo-ku, Tokyo 103-0027, Japan <http://www.r-i.co.jp>

Credit ratings are R&I's opinions on an issuer's general capacity to fulfill its financial obligations and the certainty of the fulfillment of its individual obligations as promised (creditworthiness) and are not statements of fact. Further, R&I does not state its opinions about any risks other than credit risk, give advice regarding investment decisions or financial matters, or endorse the merits of any investment. R&I does not undertake any independent verification of the accuracy or other aspects of the related information when issuing a credit rating and makes no related representations or warranties. R&I is not liable in any way for any damage arising in relation to credit ratings (including amendment or withdrawal thereof). As a general rule, R&I issues a credit rating for a fee paid by the issuer. For details, please refer to <http://www.r-i.co.jp/eng/policy/policy.html>.

© Rating and Investment Information, Inc.

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>

ISSUER: **The Oriental Republic of Uruguay**

RATING: **Foreign Currency Issuer Rating
BB, Affirmed**

RATING OUTLOOK: **Positive, Changed from Stable**

■Contact : Investors Service Division TEL.+81-(0)3-3276-3511 E-mail. infodept@r-i.co.jp
■Media Contact : Corporate Planning Division (Public Relations) TEL.+81-(0)3-3276-3438

Rating and Investment Information, Inc. Nihonbashi 1-chome Bldg., 1-4-1, Nihonbashi, Chuo-ku, Tokyo 103-0027, Japan <http://www.r-i.co.jp>

Credit ratings are R&I's opinions on an issuer's general capacity to fulfill its financial obligations and the certainty of the fulfillment of its individual obligations as promised (creditworthiness) and are not statements of fact. Further, R&I does not state its opinions about any risks other than credit risk, give advice regarding investment decisions or financial matters, or endorse the merits of any investment. R&I does not undertake any independent verification of the accuracy or other aspects of the related information when issuing a credit rating and makes no related representations or warranties. R&I is not liable in any way for any damage arising in relation to credit ratings (including amendment or withdrawal thereof). As a general rule, R&I issues a credit rating for a fee paid by the issuer. For details, please refer to <http://www.r-i.co.jp/eng/policy/policy.html>.

© Rating and Investment Information, Inc.