MOODY'S

New York, May 17, 2023 -- Moody's Investors Service ("Moody's") has today affirmed the Government of Uruguay's ("Uruguay") long-term Baa2 issuer ratings and senior unsecured bond ratings and changed the outlook to positive from stable. In addition Moody's has also affirmed Uruguay's senior unsecured shelf ratings at (P)Baa2.

The key drivers of the rating decision were:

1. Strong institutions and governance delivered effective policy response to shocks, strengthening policy frameworks and providing track record of successful fiscal policy implementation

2. Prospects of better growth performance and continued commitment to the fiscal rule will support a reduction of the government debt burden

The rating action reflects Moody's assessment that reforms which have strengthened the fiscal and monetary policy frameworks will be preserved, contributing to enhance the sovereign credit profile. A stronger investment trend will support growth performance, facilitating fiscal consolidation and stabilizing Uruguay's debt metrics over the coming years.

Uruguay's local and foreign-currency country ceilings remain unchanged at A1 and A2, respectively. The four-notch gap between the local currency ceiling and the sovereign rating reflects low government intervention in the economy, strong institutions and predictable policies, low political risk and moderate external vulnerability risk. The one-notch gap between the foreign-currency ceiling and the local currency ceiling incorporates Uruguay's moderate policy effectiveness, which limits potential risks stemming from relatively high financial dollarization in the country, and an open capital account.

RATINGS RATIONALE

RATIONAL FOR THE POSITIVE OUTLOOK

FIRST DRIVER – STRONG INSTITUTIONS AND GOVERNANCE DELIVERED EFFECTIVE POLICY RESPONSE, STRENGTHENING POLICY FRAMEWORKS AND PROVIDING TRACK RECORD OF SUCCESSFUL POLICY IMPLEMENTATION

Uruguay's government implemented reforms to the fiscal framework starting in 2020, introducing a structural deficit target, a limit on real spending growth, and a net debt ceiling. Over the past three years, adhering to the parameters of the fiscal rule built a track-record of compliance with the fiscal rule and increased the credibility of fiscal policy. In 2022, the structural deficit was 2.4% of GDP, below the 2.6% target; real primary spending growth was -0.5%, below the 2.1% limit; and net indebtedness was $1.8 billion, below the $2.1 billion target. Moody's expects the government to continue complying with the targets achieving a structural fiscal deficit of 2.5% of GDP in 2023 and maintaining the level of indebtedness stable.

Congress has recently approved a social security reform bill that will support fiscal sustainability, stabilizing pension spending as a share of GDP over the long term. The reform extends the retirement age to 65 years from 60 years and increases benefits for vulnerable groups improving the equity of the system. The new pension law also allows current retirees to participate in the labor market and contribute to the pension system, alleviating fiscal pressures and expanding labor supply.

The central bank has revamped its monetary policy framework, improving the effectiveness of its policy rate and enhancing communication with the market. Moody's expects inflation will remain around 7% in 2023, moving into the inflation target range in 2024. The convergence of inflation with policy targets, as well as efforts to anchor inflation expectations and reduce dollarization of the domestic financial system will strengthen the credibility of monetary policy over time.

Uruguay's institutional and policy-making frameworks have been resilient and the authorities have demonstrated an ability to deliver effective policy response to shocks, enacting credit positive reforms during challenging economic circumstances. Approval of the fiscal framework and ratification through a referendum process supports the durability of this reform. Similarly, the social security reform indicates the ability of Uruguay's institutions to reach consensus around politically difficult reforms that have long-term economic and social impact.

In an environment which has been characterized by multiple shocks, Uruguay's institutions have been able to maintain political stability and social cohesion, while taking action on long-standing economic issues. Recent structural reforms support Moody's favorable assessment of Uruguay's institutions and governance strength which is placed above the median for Baa-rated peers.

SECOND DRIVER – PROSPECTS OF BETTER GROWTH PERFORMANCE AND COMMITEMENT TO THE FISCAL RULE WILL SUPPORT A REDUCTION IN THE GOVERNMENT DEBT BURDEN

The drought that started in December 2022 will weigh on economic activity in the near term, but Moody's expects GDP growth to exceed the rate observed before the pandemic in the coming years. Additionally, the economic impact of the drought will be partially offset by increased tourism and pulp production on the supply side, and strong private consumption on the demand side.

Moody's expects average annual growth of 2.7% in 2024-25, compared to just below 1% before the pandemic. Investment made a strong contribution to growth in 2021-22 with the ratio of investment to GDP going to 18.4% in 2022 from a low point of 14.6% in 2019. Stronger investment will address a key weakness in Uruguay's growth dynamics that persisted for several years. Economic growth will be supported by the operations of a new pulp mill and a pipeline of investments in infrastructure projects. In addition, the $1 billion-investment in railway infrastructure, financed through a public-private partnership model, is underway, connecting the port of Montevideo with the plant.

On the back of continued commitment to the fiscal rule, Moody's expects government debt will decline and stabilize at around 55% of GDP over the next 2-3 years from 61% in 2021, with the interest-to-revenue ratio remaining around 9%. Effective liability management has improved the sovereign's credit profile reducing interest and refinancing risks by extending average maturity and increasing the share of fixed-rate debt.

RATIONALE FOR RATING AFFIRMATION

The rating affirmation reflects Uruguay's strong institutions and governance relative to peers and Moody's expectations that debt metrics will remain in line with Baa-rated peers.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Uruguay's ESG Credit Impact Score is neutral-to-low (CIS-2) reflecting its exposure to social risks, exposure to environmental risks and broad societal consensus that supports its governance.

Uruguay's exposure to environmental risks as neutral-to-low (E-2 issuer profile score). The country's large coastline is not susceptible to major flooding, and extreme weather events are rare in the region. The main risk is disruptive weather effects like excessive rains or droughts, which would affect the agricultural sector.

Exposure to social risks is neutral-to-low (S-2 issuer profile score). The country's aging population, coupled with the population's predilection for social expenditure, will weigh on public finances in the coming years absent policies to address the challenges faced by the social security system. A deterioration in the labor market, for the younger population in particular, also poses social risks. However, adequate provision of social services and a mature political system that develops policies based on consensus help mitigate social risks.

The influence of governance on Uruguay's credit profile is positive (G-1 issuer profile score). The country has a long history of strong institutions and a consensus-based tradition that leads to durable policy decisions and supports social cohesion.

GDP per capita (PPP basis, US$): 24,340 (2021) (also known as Per Capita Income)

Real GDP growth (% change): 5.3% (2021) (also known as GDP Growth)

Inflation Rate (CPI, % change Dec/Dec): 8% (2021)

Gen. Gov. Financial Balance/GDP: -4.1% (2021) (also known as Fiscal Balance)

Current Account Balance/GDP: -2.5% (2021) (also known as External Balance)

External debt/GDP: 79.4% (2021)

Economic resiliency: baa1

Default history: At least one default event (on bonds and/or loans) has been recorded since 1983.

On 12 May 2023, a rating committee was called to discuss the rating of the Uruguay, Government of. The main points raised during the discussion were: The issuer's economic fundamentals, including its economic strength, have materially increased. The issuer's institutions and governance strength, have materially increased. The issuer's governance and/or management, have materially increased. The issuer's fiscal or financial strength, including its debt profile, has materially increased.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Uruguay's sovereign credit rating would be upgraded if the government continues to comply with fiscal rules leading to stabilizing debt burden. An improved and sustained growth performance supported by a steady rebound in private investment would also support rating upgrade.

The outlook could change back to stable if renewed fiscal pressures emerge due to reversal of recent fiscal reforms or if banking system-related contingent liabilities materialize and require sovereign support. A return of persistent low growth rates would also put downward pressure on Uruguay's credit profile.

The principal methodology used in these ratings was Sovereigns published in November 2022 and available at https://ratings.moodys.com/rmc-documents/395819. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1288235.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

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