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La Mondiale

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Table Of Contents

Major Rating Factors

Rationale

Outlook

Corporate Profile: A Long-Established Life Insurer

Competitive Position: Strong Franchise In Selected Segments

Management And Corporate Strategy: Environment Challenges Strategic Goals, But Focus Remains On Life And Protection

Enterprise Risk Management: Adequate

Accounting: Reporting Under IFRS

Operating Performance: Good, But Competition And Low Interest Rates Might Hamper Long-Term Earnings Potential

Investments: Strong Investment Portfolio Overall, Although The Environment Challenges Investment Policies

Liquidity: Strong, On The Back Of Highly Liquid Assets

Table Of Contents (cont.)

Capitalization: Risk-Adjusted Capital Adequacy Is A Main Rating Weakness

Financial Flexibility: High Debt And Difficult Market Conditions Put The Focus On Internal Funding Sources

Related Criteria And Research

La Mondiale

Major Rating Factors

Strengths:

- Strong competitive position.
- Strong investments and liquidity.

Weaknesses:

- Dampened prospects for operating performance.
- Weakened capital adequacy and financial flexibility relative to the ratings.

**Operating Company Covered
By This Report**

Financial Strength Rating

Local Currency

BBB+/Negative/--

Rationale

The ratings on France-based mutual life insurer La Mondiale are supported by Standard & Poor's Ratings Services' perception of the group's strong competitive position, strong investments overall, and strong liquidity. Offsetting these positives is La Mondiale's weakened risk-adjusted capital adequacy, financial flexibility, and operating performance.

We view La Mondiale's competitive position as strong, sustained by a presence across the life insurance product range (both in pensions and savings) and specialized subsidiaries in France and Luxembourg. La Mondiale's specialized networks include a proprietary employee sales force. Its competitive position also benefits from partnerships with private banks and brokerage. Along with the AG2R group (main operating entity AG2R Prevoyance, A-/Negative/--), La Mondiale has formed the AG2R-La Mondiale Société de Groupe d'Assurance Mutuelle (SGAM), which provides comprehensive life, savings, pension, accident, and health coverage in France. Furthermore, Luxembourg-based subsidiary La Mondiale Euro-Partner (LMEP) is posting high growth, alleviating revenue declines at the group's French subsidiaries.

We view La Mondiale's investments as strong overall, with high credit quality at the average rating level of 'A', and declining equity exposures (to 8.3% in 2011 from 10.4% in 2010). Despite a lower-than-peers' average cash and short-term deposit allocation (2.6% at year-end 2011), we view La Mondiale's liquidity as strong, due to its mostly listed equities and investment-grade bonds. Although declining in line with global market trends, we do not view La Mondiale's net inflows as a material source of pressure on liquidity.

Equity market volatility and decreasing interest rates amid a competitive French savings market constrain La Mondiale's operating performance. La Mondiale's net earnings averaged €244 million over the past three years, translating into an average return on equity (ROE) of 14.1% over the same period. That said, some of this came from exceptional items that might not be renewed in the future. Short-term new business guarantees may also weigh on profitability. We consider La Mondiale's cost-cutting initiatives, like focusing on unit-linked products, and its increasingly cautious crediting policy to be mitigating factors. In our base-case scenario, we anticipate that La Mondiale will continue to rebuild its new business margins and maintain ROE of at least 10% in 2012 and 2013. We expect operating earnings to increase, supported by further cost cuts and cautious crediting policies.

La Mondiale's capitalization is good, but stands at the lower end of this assessment range, according to our criteria. Despite capital adequacy improvements on the back of retained earnings and lower volume growth over the past two years, we consider that capital adequacy is likely to remain a rating weakness over the next two years. We nevertheless expect La Mondiale to continue balancing its growth targets in line with its funding abilities, which is likely to result in further strengthening of its capital adequacy. Furthermore, we consider La Mondiale's ability to source external funding as limited by its already high level of debt on balance sheet relative to its total adjusted capital and to regulatory limits. Two-thirds of La Mondiale's subordinated debt--€400 million--is perpetual, but has a first call date in October 2013. In our base-case scenario, we assume that the group will manage its funding sources in such a way as to preserve its capital adequacy from further declines.

Outlook

The negative outlook reflects our view that the current economic and investment market environment, particularly equity market volatility and low interest rate environment, could prevent La Mondiale from strengthening its financial profile to levels underpinning the ratings over the next 12 to 24 months.

We could lower the ratings over the next 12 to 24 months if La Mondiale does not meet the expectations underlying our base-case capital adequacy, capital, and financial flexibility assumptions. We could revise the outlook to stable if La Mondiale exceeds these expectations on a sustainable basis.

Corporate Profile: A Long-Established Life Insurer

Table 1

La Mondiale Selected Statistics					
	--Financial year ended Dec. 31--				
(Mil. €)	2011	2010	2009	2008	2007
Total gross premiums written	5,232	5,906	5,526	5,146	5,320
Net income	225.3	331.8	173.7	68.3	123.4
Post-tax return on technical reserves (bps)	45.0	70.0	41.3	17.1	31.7
Total assets	57,721	55,867	49,770	43,289	44,920

bps--Basis points.

Founded in 1905, La Mondiale is a France-based mutual insurer that writes life, savings, and pension business. It recorded €5.24 billion in gross written premiums (GWP) and €50.6 billion in assets under management at year-end 2011. La Mondiale derives almost 80% of GWP in France.

With the AG2R group, La Mondiale founded the "Société de Groupe d'Assurance Mutuelle" (SGAM) AG2R La Mondiale in 2008. The SGAM is a French legal framework that allows mutual insurers to create operational and financial solidarity links.

La Mondiale operates directly through its La Mondiale Expert network (LME; €1.41 billion GWP in 2011); and through operating subsidiaries held through La Mondiale Participations (LMPA; €3.82 billion GWP), a holding company 65%

owned by La Mondiale and 35% by Dutch insurer AEGON N.V. (A-/Stable/A-2).

- La Mondiale Expert sells pension, life/savings, disability, and health products to self-employed workers (the so-called "Madelin" business) and small enterprises through a network of 1,000 employees and partnerships with professional associations.
- La Mondiale Partenaires (LMP; €2.11 billion GWP) and La Mondiale Europartner (LMEP; €1.09 billion GWP) are the two main operating entities held under LMPA. They sell savings products to high-net-worth individuals, in France and in Luxembourg, respectively through private banks and independent financial advisors.
- Arial (€0.62 billion GWP), a 50-50 joint venture of LMPA and AG2R, offers group pension and protection coverage to large companies. Arial operates through direct sales (54% of the new business written in 2010), insurance brokers (27%), partnerships, and other AG2R and La Mondiale networks (19%).

Competitive Position: Strong Franchise In Selected Segments

Table 2

La Mondiale Business Statistics					
	--Financial year ended Dec. 31--				
(Mil. €)	2011	2010	2009	2008	2007
Total revenue	6,844	7,407	6,770	6,322	6,470
Life gross premiums written	5,232	5,906	5,526	5,146	5,320
Annual change (%)	(11.4)	6.9	7.4	(3.3)	(1.1)
Life net premiums written	5,092	5,764	5,298	4,871	5,042
Annual change (%)	(11.7)	8.7	8.8	(3.4)	(3.0)
Net premiums earned	5,092	5,764	5,302	4,872	5,042

La Mondiale's competitive position is strong, in our view, thanks to a long-standing focus on life, pension, and savings businesses, diversified distribution networks and product offering. Offsetting these strengths are the challenging operating environment and competitiveness in the French life and savings market.

Although its market share appears small, at 4.27% of French life and savings GWP, La Mondiale has established leading positions in its chosen niches, namely high-net-worth savings, the Madelin pensions, and group pensions and health. We view this success as attributable to a multichannel and multibrand approach, the ability to tailor products for specialized networks, and a partnership-oriented strategy. In 2011, La Mondiale's 11.3 % decline in premiums was more contained than the 14% for the French life insurance market. This is particularly attributable to La Mondiale's presence in pensions and its focus on Luxembourg in 2011. These attributes lead us to anticipate another contained midsingle-digit decline in La Mondiale's premiums in 2012. We also expect La Mondiale's net inflows to remain positive and slightly above 2011 levels.

La Mondiale's experience in pension business is one of the key drivers of its competitiveness in the market. Amid more volatile individual savings, pension business has provided La Mondiale with stable inflows, and 6% average growth over the past three years. We expect this segment to drive La Mondiale's long-term growth, sustained by the "Madelin" framework for the self-employed, where La Mondiale ranks No. 2. and which represents 28% of total GWP.

The volume-driven, competitive, and volatile high-net-worth savings (HNWS) business gives La Mondiale upside

potential when the economic environment is positive. La Mondiale's main vehicle for HNWS, LMP, has a leading position in the segment thanks to its expertise in providing flexible and competitive savings guarantees to its private banking channels. LMP's active partnership approach enables it to cope with volatile partnerships and contain pressure on premium collection. However, this segment exposes La Mondiale to severe competition, net inflow pressure, and narrowed margins in a challenging environment, such as the current tough conditions in the French market, which will likely continue in the foreseeable future. Through new partnerships, we expect LMP to continue defending its positions. However, we expect the current investment market challenges to lead LMP to tone down its relatively aggressive guaranteed rates policy and to further balance growth targets with funding and operating performance constraints.

Luxembourg based subsidiary LMEP is likely to increasingly play a recipient role for some categories of LMP's policyholders. Evidence is its GWP, which grew a solid 33% to €1.1 billion in 2011, leading its share in La Mondiale's total premiums to reach 21% of GWP in 2011, against 14% in 2010.

With a strong position cemented through the joint expertise and client bases of its parent companies La Mondiale and AG2R, Arial is the No. 2 player in group pensions in France, with a 14.4% market share. Arial also has a comprehensive product range for protection and pensions for large corporations. Arial's business remains subject to some volume volatility, though, owing to its large part of single premium contracts.

Management And Corporate Strategy: Environment Challenges Strategic Goals, But Focus Remains On Life And Protection

We view AG2R-La Mondiale's strategy as focused because it builds on the two groups' complementary expertise. La Mondiale's strategy is to grow organically in its historical niches: pensions and savings. It is closely linked with that of AG2R, which aims to grow in accident and health. We view operational links between AG2R and La Mondiale as growing, with regular synergies built over time.

Strategy

La Mondiale aims mainly to maintain growth in its chosen markets, while exploring new, low-capital-intensive partnerships. AG2R and La Mondiale have had a joint strategic plan since 2009 and a common umbrella brand "AG2R La Mondiale." The current, three-year 2012-2014 plan aims to focus on client relationships and profitable growth. We view the 2.5% target increase in annual GWP as difficult to achieve through 2014, but consider that La Mondiale's focus to be more capital- and efficiency-driven in the current environment. For instance, La Mondiale has taken steps to strengthen its regulatory solvency ratio. Consequently, we expect its strategy to be less driven by growth targets and more by capital consumption and operating performance than in 2011.

Operational management

The AG2R-La Mondiale SGAM has one CEO and five deputy CEOs. The deputy CEOs are responsible for different business segments and support functions but they all cover both AG2R and La Mondiale. The SGAM has one executive committee, while AG2R and La Mondiale still have separate boards of directors. This recognizes the difference between the two groups' governance histories, while aiming at smoothly embedding the partnership in the two cultures. The operational workforces operate by line of business (protection, savings, and pensions) at the SGAM

level and back office departments are common. Finally, distribution channels have been placed under joint networks (for example, savings, convenience ["Réseau de Proximité"], and enterprises).

Financial management

We view financial management as one of La Mondiale's key areas of focus because the current market environment poses significant challenges to management as it seeks to find the balance between size and earnings growth. The group has built internal tools based on Solvency II driven metrics to allow having an assessment of risk-adjusted capital adequacy. Based on this La Mondiale is likely to set up a risk tolerance framework and implement measures to comply with this framework. Currently, the company targets an annual return on equity of 10%, and currently manages solvency on a consolidated regulatory basis, where it targets maintaining at least 110% of regulatory requirements, excluding unrealized gains. We understand it aims to increase this coverage to 140% by 2014 to prepare for the implementation of Solvency II.

La Mondiale calculates embedded value internally, using it as an ex-post monitoring tool but not yet as a business and profitability monitoring tool.

Enterprise Risk Management: Adequate

We view La Mondiale's enterprise risk management (ERM) as adequate, thanks to adequate risk controls on main risks: market, interest, and longevity risks.

The importance of ERM to the ratings on La Mondiale is moderate. The company's niche-focused strategy and France-focused exposure are counterbalanced by the complexity, capital consumption, and granularity of its product and fund range, however. La Mondiale's multiple distribution network strategy also adds to the importance of ERM.

Jointly operated with AG2R, the risk management department produces risk reporting, supervises effectiveness of risk controls, and coordinates risk-adjusted projects such as Solvency II. The department set up a risk committee in 2009, built a separate group risk management from the financial department in 2011, and is increasingly deploying efforts to spread risk culture across the group. The recent risk mapping exercise is also indicative of the group's adequate risk culture. In our view, one of the main weaknesses of the department's ERM is the lack of an explicit risk tolerance framework.

Market risk management is adequate, in our opinion. The group uses basic risk-return indicators to test strategic asset allocation, based on a value-at-risk approach, and regularly monitors concentration and liquidity risks.

Although it has not developed a full internal economic capital and full asset-liability modeling, La Mondiale is significantly enhancing its modeling in the areas of value and solvency measurement. This has prompted the development of tools that measure stochastic embedded values and risk-based capital adequacy.

The lack of a consolidated modeling platform and the still-absent explicit risk tolerance framework, in our view, continue to prevent La Mondiale from performing strategic risk management.

Accounting: Reporting Under IFRS

Standard & Poor's bases its analysis of La Mondiale on the consolidated accounts of the La Mondiale group, including the nonrated insurance entities LMP, LMEP, and Arial.

La Mondiale reports according to International Financial Reporting Standards (IFRS). Starting from the published figures, we perform certain adjustments in forming our opinion on capital adequacy and operating performance. These include eligible hybrid capital not recognized as equity under IFRS, unrealized capital gains on property assets, and an adjustment for the present value of the value of in-force. Our assessment of operating performance relies on published information and unpublished figures, such as La Mondiale's internal calculation of embedded value.

Operating Performance: Good, But Competition And Low Interest Rates Might Hamper Long-Term Earnings Potential

Table 3

La Mondiale Operating Statistics					
	--Financial year ended Dec. 31--				
(Mil. €)	2011	2010	2009	2008	2007
Net income	225.3	331.8	173.4	68.3	123.4
Return on equity (%)	10.6	18.8	13.1	5.8	10.3
Post-tax return on technical reserves (bps)	45.0	70.0	41.3	17.1	31.7
Investment portfolio					
General account invested assets	42,118	38,281	34,419	29,072	28,409
Separate accounts/unit-linked assets	12,707	13,690	12,320	10,387	14,509
Portfolio composition (%)					
Cash & cash equivalents (%)	0.3	0.3	0.3	0.5	0.6
Total bonds (%)	82.5	84.8	82.3	81.4	78.1
Common stock (%)	6.6	8.8	10.4	9.6	13.3
Real estate (%)	5.0	5.6	6.3	7.7	7.2
Total mortgages and loans (%)	5.6	0.6	0.7	0.8	0.8
Investments in affiliates (%)	0	0	0	0	0
Total portfolio composition (%)	100	100	100	100	100

bps--Basis points.

We view La Mondiale's operating performance as good, mainly thanks to the contribution of its investment performance and increasingly controlled expense bases. On the negative side, the effects of equity market volatility and decreasing interest rates, amid a competitive market landscape in La Mondiale's flagship product lines is likely to dampen earnings capacity over the next two years and weaken profit fundamentals over a longer term.

La Mondiale has demonstrated the ability to post stable earnings given its average of €244 million in net earnings over the past three years (representing a 14.1% ROE over the same period). We consider La Mondiale's cost-cutting

initiatives, higher-than-average unit-linked share in sales, and an increasingly cautious crediting policy as fundamental factors we expect will gradually sustain earnings. However, investment market conditions if persisting might leave La Mondiale with less potential to realize exceptional gains similar to those which boasted earnings over the past three years. The base case assumptions underlying our ratings include expectations of ROE in excess of 10% in the coming two years, supported by normalized net earnings of at least than €200 million. We also expect new business margins to improve constantly over the next two years.

Competition in savings markets will likely continue to pressure La Mondiale's margins. In the past, this has led La Mondiale to serve higher-than peers-credited rates, despite the gradual reduction in its credited rates in recent years (including a 30 basis-point decrease in 2011). The group has achieved decreases in credited rates thanks to a higher-than peers, albeit cautious, focus on corporate bonds, through which it has obtained generally higher investment returns. The group may gradually shift away from this policy, however, focusing more on capital consumption constraints versus investment return targets.

Investments: Strong Investment Portfolio Overall, Although The Environment Challenges Investment Policies

La Mondiale's investment portfolio is strong overall, in our opinion, thanks to the strong credit quality in its fixed-income portfolio, on average, and a liability driven asset allocation enabling the group to monitor interest rate risk while ensuring sufficient returns to policyholders. Market risk remains high, however, owing to material, albeit declining, exposures to equities and real estate.

Credit risk

We consider La Mondiale's exposure to credit risk as comparatively strong among its peers, because it has invested 81% of debt instruments of its general fund in issues rated 'A-' and above, with 'AAA' issues representing 21% of the total bond portfolio and an average rating of 'A+' on the total bond portfolio at the end of December 2011. Exposure to subordinated debt represents 12% of the portfolio, but mainly consists of lower Tier 2 debt, of which 85% Standard & Poor's rates at 'BBB' or higher, and which is diversified into numerous different issuers. As of April 2012, La Mondiale had limited exposure to government bonds issued by Greece (€2 million), Spain (€773 million), Italy (€343 million), and Portugal (€155 million), and has experienced no default on financial institutions so far.

Market risk

La Mondiale's exposure to market risk is still sizable, in our opinion, through its 8.3% investment in equities at year-end 2011 (down from 10.4% at year-end 2010). This exposes La Mondiale's net assets to material volatility, as evidenced by the €327 million unrealized losses in the equity book at year-end 2011. Concentrations in the equity portfolio are limited thanks to geographic and sector diversity (the largest exposure represents only 4% of total equities and the portfolio is made up of investments with 59 issuers).

Property assets add to La Mondiale's exposure to market risk as they represented 5% of total investments at year-end 2011. This exposure has softened the overall decline in asset values through sizable unrealized gains (€766 million on the same date), illustrating La Mondiale's long-term, revenue driven approach in investing in real estate.

Interest rate risk

La Mondiale's exposure to interest rate risk is an increasing area of focus in the current and foreseeable low interest rate environment. The company has a meaningful duration gap owing to the very long term nature of its pension business, which exposes it to reinvestment risk. However, we view positively La Mondiale's declining long-term guaranteed rate policy. La Mondiale has sharply reduced liabilities with long-term guaranteed rates in recent years (reserves with guaranteed rates of more than 3.5% dropped to 14.5% in 2011 from 53% in 2000). High guarantees at LME, which carries an average guaranteed rate of 2.69%, compensate lower guarantees at LMP, where the rate averages 0.95%. Furthermore, La Mondiale manages interest rate risk through a high asset allocation in fixed-income bonds (98% of the total bond portfolio at April 2012), with an average duration of 6.7 years, while seeking to maintain a static duration gap around seven years (7.4 years at year-end 2011).

Liquidity: Strong, On The Back Of Highly Liquid Assets

Liquidity is strong, in our opinion, because of La Mondiale's positive annual net inflows. Liquidity issues could arise from very high lapses or increased mortality rates, but would be mitigated by strong balance-sheet liquidity, with publicly traded assets representing more than 80% of technical reserves. In addition, one-half of La Mondiale's reserves relate to its pensions business, which for the most part cannot be freely surrendered by policyholders.

Capitalization: Risk-Adjusted Capital Adequacy Is A Main Rating Weakness

We view capitalization as a rating weakness for La Mondiale, owing to the low level of risk-adjusted capital adequacy relative to the ratings, and the reliance of total adjusted capital on soft, market-sensitive capital items. Increasing charges relating to credit risk add to the weakness of capital adequacy, despite management actions to address capital adequacy weaknesses to a degree.

Capital adequacy

Lower unrealized gains on La Mondiale's equity investments, coupled with increased credit risk, markedly affected the group's risk-based capital adequacy in 2011. In addition, buffers like the deferred profit-sharing reserve, to which we give credit in our capital model, have decreased as the group has had to partially fund credited rates to policyholders. Earnings generation and lower capital charges related to market risk were offsetting factors but capital adequacy remains low compared with the current rating. La Mondiale's solvency I margin coverage, without taking account unrealized positions, stood at 126% at year-end 2011, versus 116% at year-end 2010, mostly due to lower volumes.

La Mondiale's reserving is adequate in our opinion. It manages annuity risk by updating longevity tables using the latest industry best estimates, as required by local regulation. The group carries out annual internal testing of annuitant mortality on its annuity portfolio. This serves as a consistency check between actual and expected claims experience, aiming to maintain sufficient reserves.

Reinsurance

The bulk of La Mondiale's insurance risk is annuitants' longevity, which is not reinsured, as is common practice for almost all market participants. For its protection business, the group has a per-risk and per-event excess-of-loss and

stop-loss coverage that leaves low retention levels. "

Financial Flexibility: High Debt And Difficult Market Conditions Put The Focus On Internal Funding Sources

Table 4

(Mil. €)	--Financial year ended Dec. 31--				
	2011	2010	2009	2008	2007
Total assets	57,721	55,867	49,770	43,289	44,920
Financial leverage including additional pension deficit as debt (%)	24.1	25.2	28.3	36.5	35.9
Liquid assets/ technical reserves (%)	98.6	98.6	96.9	91.5	98.2
Reinsurance utilization (%)	2.7	2.4	4.1	5.3	5.2

Owing to growth expectations, we expect La Mondiale's additional capital needs to be limited in the coming two years.

The group's financial flexibility is constrained by its limited ability to raise debt, owing to regulatory limits, despite leverage and coverage ratios which we do not see, on an absolute basis, as a source of pressure on the ratings. La Mondiale's hybrid debt totaled €656 million at year-end 2011, corresponding to debt leverage of 17% according to our criteria. Fixed-charge coverage in 2011 was 10.9x (versus 12.5x in 2010) and remains what we consider as manageable. The group's debt is close to the regulatory limit while approaching the 25% total adjusted capital threshold under our criteria.

Furthermore, a substantial €400 million of La Mondiale's debt, although contractually perpetual, has a first call date in June 2013. Given the high dependence of capital adequacy on such debt, management's decision with regard to this debt issue could have an impact on our perception of the group's financial flexibility or capital adequacy. In our base-case scenario, however, we anticipate that La Mondiale would primarily aim to preserve its risk-adjusted capital adequacy at levels at least in line with those at year end 2011.

Lastly, in our assessment of La Mondiale's financial flexibility, we don't factor in the financial solidarity terms of the AG2R-La Mondiale SGAM, because we view them as limited. Consequently, we don't expect these terms, if exercised, to materially affect La Mondiale's credit quality.

Related Criteria And Research

- Interactive Ratings Methodology, April 22, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurer Capital Model, June 7, 2010
- Group Methodology, April 22, 2009

Ratings Detail (As Of October 29, 2012)

Operating Company Covered By This Report

La Mondiale

Financial Strength Rating

Local Currency

BBB+/Negative/--

Counterparty Credit Rating

Local Currency

BBB+/Negative/--

Junior Subordinated

BBB-

Domicile

France

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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McGRAW-HILL