

**Credit Opinion: Rabobank Nederland**

**Rabobank Nederland**

*Utrecht, Netherlands*

**Ratings**

<b>Category</b>	<b>Moody's Rating</b>
Outlook	Stable
Bank Deposits	Aaa/P-1
Bank Financial Strength	B+
Issuer Rating	Aaa
Senior Unsecured	Aaa
Subordinate -Dom Curr	Aa1
Jr Subordinate	Aa2
Preferred Stock	Aa2
Commercial Paper	P-1
Other Short Term	P-1
<b>Rabobank Curacao N.V.</b>	
Outlook	Stable
Senior Unsecured MTN	Aaa
Bkd Other Short Term	P-1
<b>Rabohypotheekbank N.V.</b>	
Outlook	Stable
Senior Unsecured MTN -Dom Curr	Aaa

**Contacts**

<b>Analyst</b>	<b>Phone</b>
Stephane Le Priol/Paris	33.1.53.30.10.20
Virginie Merlin/Paris	
Reynold R. Leegerstee/London	44.20.7772.5454
Stephane Herndl/Paris	

**Key Indicators**

**Rabobank Nederland**

	[1]2008	2007	2006	2005	2004	Avg.
Total assets (EUR billion)	567.67	570.50	556.46	506.57	483.57	[2]8.76
Total capital (EUR billion)	34.00	33.67	31.83	28.99	25.13	[2]9.68
Return on average assets	0.54	0.46	0.44	0.42	0.40	0.43
Recurring earnings power [3]	0.55	0.34	0.40	0.39	0.54	0.48
Net interest margin	1.53	1.29	1.32	1.39	1.53	1.43
Cost/income ratio (%)	71.14	79.85	76.34	76.00	72.24	74.73
Problem loans % gross loans	1.29	1.12	1.22	1.57	1.48	1.42
Tier 1 ratio (%)	10.20	10.70	10.70	11.60	10.90	10.94

[1] As of June 30. [2] Compound annual growth rate. [3] Preprovision income % average assets.

**Opinion**

**RECENT CREDIT DEVELOPMENTS**

Rabobank's net banking income (NBI) stood at EUR 6,081 million for the first half of 2008, up 7% from EUR 5,679 million for H1 2007. At the same period, its pre-tax income stood at EUR 1,759 million, up 7% from EUR 1,648 million for 1H 2007 and was supported by higher net interest income as well as by the positive impacts of the sale

of Alex and the consolidation of BGZ. Rabobank announced that the turmoil on the financial markets resulted in a net negative impact of EUR 529 million on its net profit. At end-June 2008, Rabobank's Tier 1 ratio stood at 10.2% on a Basel I basis (13.8% on a Basel II basis with transitional floor).

The additional impairments and provisions in the P&L announced by the bank in H1 2008 (EUR 486 million including EUR 157 million provision for bad loan) continued to be in line with Moody's expectations. The aforementioned impairments stemmed from revaluations on subprime-related securities for EUR 240 million (of which EUR 130 million on subprime RMBS and EUR 110 million on CDOs) and from provisions on monoline insurers for EUR 245 million. The remaining subprime-related exposures amounted to EUR 108 million at end-June 2008. Moody's notes that Rabobank has decided to scale down its non-client-related operations undertaken at Global Financial Markets.

Moody's further noted that Rabobank's AFS reserves suffered from a EUR 1,662 million negative impact in the first half of the year and stood at negative EUR 1,173 million at end-June 2008 (vs. positive reserves of EUR 489 million at year-end 2007). This derives mainly from negative fair value changes of EUR 1,433 million, EUR 788 million of which from fixed income securities.

## **SUMMARY RATING RATIONALE**

Moody's assigns a bank financial strength rating (BFSR) of B+ to Rabobank Nederland (Rabobank), which translates into a Baseline Credit Assessment of Aa2. The rating reflects conservative business profile and very strong financial fundamentals.

Rabobank's long-term global local currency (GLC) deposit rating is at the Aaa level based on the probability of systemic support which Moody's assesses as very high and which reflect its systemic position in the Dutch banking system. Rabobank is one of the two banks which dominate Dutch banking markets, with significant franchises in the domestic residential mortgage market, of savings accounts, and of SME business. It dominates the agricultural market with a share of over 80% of all lending. We believe that these market positions have been strengthened since the beginning of the crisis a year ago.

### **Credit Strengths**

- Generally low-risk banking franchise, leading to predictable albeit modest earnings displaying low volatility
- Strong and defensible domestic market shares
- Solid financial condition
- Conservative underwriting culture, with limited market risk appetite
- Excellent capital levels, albeit of slightly weaker quality than historically due to presence of hybrids
- Group's cross support mechanism, which ensure that resources of the whole Rabobank group would be available should Rabobank Nederland, the rated entity, encounter difficulties

### **Credit Challenges**

- Strategic flexibility somewhat constrained by "closed" capital structure
- While in line with that of Dutch peers, Rabobank's operating efficiency is weaker than other banks in the B+ BFSR rating category
- Managing risks inherent in its growing non-banking and international operations - including insurance (the group has a 37% ownership in Eureko), and more material property-development operations following the acquisition of Bouwfonds, the Dutch real estate development company, as well as leasing, following the acquisition of Athlon.

### **Rating Outlook**

The outlook is stable on the BFSR based on the stable and consistent financial fundamentals and the bank's stable franchise in its core businesses and generally conservative risk profile.

The outlook is also stable on the deposits and debt ratings based on the stable BFSR and on the assessment of the probability of systemic support, which Moody's perceives unchanged at very high.

### **What Could Change the Rating - Up**

The BFSR could be upgraded if the bank's profitability metrics were to improve to levels comparable with those of higher-rated banks. However, we believe this may be difficult to achieve in the short-term given the bank's low risk strategy and cooperative group structure which focuses on earnings stability over profit maximisation.

The long-term deposits and debt ratings are already at the Aaa level.

### **What Could Change the Rating - Down**

A strategic direction which would lead to greater reliance on more volatile earning streams, including the insurance sector, could have negative rating implications on the BFSR. Moody's is monitoring Rabobank's on-going investments in its non-banking activities to the extent that they raise the bank's risk profile and weaken the quality of its earning to levels inconsistent with the bank's rating levels. Erosion of the bank's risk profile or increase in operational risk resulting from successive non-banking acquisitions could put pressure on BFSR, as would a deterioration of Rabobank's franchise in its core market or evidence of deteriorating financial fundamentals.

A downgrade of the long-term deposits and debt ratings could be triggered by a downgrade of the BFSR or by the perception by Moody's of a lower probability of systemic support in a case of stress. We view however the latter as unlikely because of the importance of Rabobank to the Dutch banking sector.

### **Recent Results and Company Events**

In early 2008 Rabobank consolidated on its balance sheet the assets of a Structured Investment Vehicle (SIVs) it sponsored, Tango Finance Limited. Tango Finance had total cash assets of approximately EUR 4.1 billion as of June 2008. This measure taken by Rabobank to assist in the orderly unwinding of Tango was not material given the minimal expected impact on the bank's Tier 1, which Moody's estimated at approximately 10 b.p., and the relatively small size of the assets assumed in relation to Rabobank's consolidated assets.

In early 2008, Rabobank completed the sale of Alex Beleggersbank to BinckBank, an internet broker

In January 2008, Rabobank acquired a 40% stake in Banco Regional, a Paraguayan bank focusing on the agricultural sector and rural regions of Paraguay.

In April 2008, Rabobank received approval from the Polish regulator to increase its ownership of Polish bank Bank Gospodarki Zywosciowej S.A. (BGZ) to 59.35% through the acquisition of an additional 12.87% stake.

BGZ has been consolidated in Rabobank's accounts as of end-June 2008.

In November 2008, Rabobank announced it had entered into a co-operation agreement with Rothschild. This agreement aims at worldwide cooperation in the field of M&A and equity capital markets advisory in the food and agriculture sectors.

Rabobank's NBI was up 7% to EUR 6,081 million at end-June 2008. Its net interest income was up 19% to EUR 3,919 million, its fees and commission income up 4.8% to EUR 1,473 million while its other income was down 29.7% to EUR 689 million, mainly as a result of subprime-related impairments and of weaker trading performance in the Global Financial Markets. At end-June 2008, its net income group share stood at EUR 1,759 million, up 7% from EUR 1,648 billion at end-June 2007. Rabobank had total assets of EUR 567.7 billion at end-June 2008 and a Tier 1 ratio (under Basel I) of 10.2% at end-June 2008 (YE2007: 10.7%).

For more details on the impairments and provisions linked to the credit crisis, please refer to the Recent Credit Developments section of this Credit Opinion.

### **DETAILED RATING CONSIDERATIONS**

Detailed considerations for Rabobank's currently assigned ratings are based on the latest financial report available, which has 2007 year-end figures, but also incorporate latest interim public information, notably from the H1 2008 reports from the bank. Moreover, the quantitative scores are based on the three-year averages for the years 2005-2007.

### **Bank Financial Strength Rating**

Moody's assigns a bank financial strength rating (BFSR) of B+, which translates into a Baseline Credit Assessment (BCA) of Aa2. The rating derives from Rabobank's very strong franchise in the Netherlands, its overall conservative risk profile and its sound financial fundamentals. The BFSR is also supported by the stability of the bank's earnings, very high quality credit quality metrics which have displayed low volatility over a ten-year period, and the bank's conservative underwriting culture which we believe is important in maintaining Rabobank's superior and historic stable credit culture.

As a point of reference, the BFSR is two notches above the score generated by Moody's scorecard, which fails to capture the quality of the profitability and efficiency metrics for a true cooperative Group such as Rabobank. Mutualist groups such as Rabobank aim at providing their members - which are the bank's shareholders - with lower service charges instead of maximising shareholders' profit.

#### Qualitative Factors (50%)

##### Factor 1: Franchise Value

Trend: Neutral

Rabobank's domestic banking business mix translates into a generally low risk profile and contributes to the stability of earnings which historically is a key characteristic of the group. However, its non-banking operations including insurance (37% stake in Eureka), property (acquisition of Bouwfonds, the Dutch property company active in real estate development business), and leasing could introduce a higher level of earnings volatility.

International operations are an area of growing strategic importance to Rabobank. This is being pursued through its "international retail" Strategy. While Rabobank's international expansion has generally been of solid quality, in Moody's opinion, the diverse and growing international "footprint" marginally raises Rabobank's risk profile. The outlook is stable for the bank's franchise value.

As a point of reference, the scorecard generated a score of A-, which is in line with our perception of the bank's franchise.

##### Factor 2: Risk Positioning

Trend: Neutral

The bank has strong risk management practices, which we believe is being extended to its non-banking operations. We expect that the bank's tradition of very tight credit process should continue to play a very important part in maintaining Rabobank's superior and historically stable credit quality. In particular we note the long-standing tradition of rigorous scoring of wholesale and other corporate credits and evaluation by a credit function which has independent reporting lines, above-average frequency of exposure reviews, determined by the latest internal score, leading to early alerts, tightly defined credit delegations across the group, with authorities being determined by the score assigned by the independent credit function, single obligor exposure monitoring and limit-setting capturing the exposures of all member banks (as well as all units holding securities).

We note that Rabobank fares relatively better than its Dutch peers with regards credit risk concentration, mainly thanks to the bank's focus on retail activities. Rabobank has however, in common with its peers, high group exposures towards other financial institutions.

Liquidity management is viewed as a strength given the bank's important retail deposit base, which proved more than resilient since the beginning of the financial crisis, and especially in the turmoil of September/October.

Market risk appetite is low and has shown little volatility. We note for instance that Rabobank has decided to scale down its non-client-related operations undertaken at Global Financial Markets as a result of the market turmoil. We view this decision as a positive factor in maintaining the bank's low risk profile and ensuring that potential losses remain within its risk appetite.

As a point of reference, the scorecard generated a score of B, which we believe is a fair representation of the bank's overall risk positioning and management.

##### Factor 3: Regulatory Environment

Please refer to Moody's Banking System Outlook for The Netherlands published in February 2008 to obtain a detailed discussion on Regulatory Environment.

##### Factor 4: Operating Environment

Trend: Neutral

Please refer to Moody's Banking System Outlook for The Netherlands published in February 2008 to obtain a detailed discussion on Regulatory Environment.

In light of the sizeable operations conducted outside of its home country, we have assessed Rabobank's overall operating environment and the outcome is slightly below Moody's perception of the operating environment for the Netherlands, although this does not weigh on our overall perception of the bank's intrinsic creditworthiness.

## Quantitative Factors (50%)

### Factor 5: Profitability

Trend: Neutral

As a cooperative group, Rabobank is not aimed at maximising profitability, but rather at providing its members with lower service charges. This results in lower profitability metrics relative to peers rated in the same category, as evidenced by the Pre-Provision Profit as percentage of average Risk-Weighted Assets (PPP % avg. RWA), which stood at 1.10% at end-June 2008 (YE 2007: 0.76%).

We believe that profitability metrics should be adjusted to reflect the cooperative nature of Rabo's business and the impact it has on the bank's profit and loss account. When doing so, we perceive Rabobank's profitability as satisfactory.

We further note that the bank seeks stability of earnings and a conservative balance sheet as its key objectives and we view positively the bank's low earnings volatility over a multi-year (over 10 years) time frame.

As a reference, Moody's scorecard generates a score of D, which we believe is underestimated in light of the cooperative structure and objectives of the group.

### Factor 6: Liquidity

Trend: Neutral

Rabobank's liquidity is managed centrally and is tightly controlled across the group. We have no concerns about the quality of the bank's liquidity management.

At end-June 2008, the group had the following funding sources:

- Deposits (demand and savings) accounting for 53.5% of total funding
- Interbank (11.4% of total funding)
- Market funds (34.7% of total funding)
- Subordinated debt excluding hybrids (0.4% of total funding)

(The percentages above are calculated as the proportion of each contributor relative to the sum of the above listed items.)

As a bank primarily focused on the retail and agricultural businesses, Rabobank has a low proportion of liquid assets in its balance sheet, which mainly consists of loans and advances. We estimate that liquid assets accounted for 20.7% of total assets at end-June 2008 (estimated as the sum of cash, due from Central Banks, interbank and securities).

We further note that the proportion of liquid assets (as estimated above) has decreased from 25.2% at year-end 2007 (YE 2006: 28.6%; YE 2005: 32.2%) as a consequence of the steady growth of the loan portfolio over the same period and slight attrition of the securities and interbank investments, in line with the bank's conservative risk profile.

As a reference, the scorecard generates a score of C+, which is a fair representation of the bank's liquidity positioning.

### Factor 7: Capital Adequacy

Trend: Neutral

Rabobank's capital adequacy is solid and is a key element underpinning the current ratings. At end-June 2008, the bank's Tier 1 ratio stood at 11.2% under Basel 2 (with transitional floor) and it is our understanding that it is the bank's goal to maintain its Tier 1 ratio in excess of 10%.

We note that the RWA are expected to reduce significantly as a result of the reduction of the floor imposed during the period of transition to Basel 2. This is mainly explained by the high proportion of mortgage loans in Rabobank's balance sheet, as well as by collateral being taken into account in the calculation of required capital for corporate loans.

The bank has been able to maintain its solid capital adequacy in part through issuing Membership Certificates (MCs), which are recognised by the Dutch Central Bank as Tier 1 capital, as well as through the issuance of Trust Preferred Securities (TPS) and capital securities. We view the MCs as having extremely strong equity-like features.

As a reference, Moody's scorecard generates a score of A which is, in Moody's view, fully justified.

#### Factor 8: Efficiency

Trend: Neutral

As for its profitability, Rabobank's efficiency should be analysed in the context of the bank's cooperative structure and objectives. As the bank is not aimed at maximising profitability, but rather at providing its members with lower service charges, the cost-to-income ratio may appear below that of peers rated in the same category.

We believe that profitability metrics should be adjusted to reflect the cooperative nature of Rabo's business and the impact it has on the bank's profit and loss account. However, even when doing so, we perceive Rabobank's efficiency to be relatively low.

It is to be noted, however, that Rabobank made in recent years a concerted effort to improve efficiency across the group and in particular at the local Rabobanks via a programme it has named "Operation Service". The objective of Operation Service was to generate cost savings of EUR 200 million and to gradually reduce the number of full-time equivalent (FTE) employees by a further 1,200 at Rabobank Nederland. The bank also introduced a scorecard of performance measures for the local Rabobanks as a means of enhancing operating standards across the network. In addition, the number of local Rabobanks has been declining steadily as banks have been merging and group functions streamlined and at end-June 2008, the number of local Rabobanks fell to 161 at end-June 2008. A recent programme for local banks "Rabobank 2010" is introduced to create a more efficient design of processes within local banks.

As a reference, Moody's scorecard generates a score of D, which is slightly below our own perception of the bank's efficiency, in light of the above mentioned cooperative structure and objectives of the group.

#### Factor 9: Asset Quality

Trend: Neutral

We view the bank's asset quality as strong due to the bank's conservative underwriting policies with stable and low levels of impaired loans. Historically Rabobank has experienced very low credit losses which have been in the narrow fluctuation range of between 13 and 27 basis points of gross loans (Moody's estimates).

This is driven by the high proportion of domestic loans to individuals (around 70% of total loans at end-June 2008) coupled with the high proportion of mortgage loans in its loan and a sound level of collateralization of the impaired loans.

As a reference, Moody's scorecard generates a score of B, which is broadly in line with our own view on the bank's asset quality.

### **Global Local Currency Deposit Rating (Joint Default Analysis)**

Moody's assigns a global local currency deposit ratings of Aaa to Rabobank. The rating is supported by Rabobank's Bank's Baseline Credit Assessment (BCA) of Aa2 and Moody's opinion of a very high probability of systemic support should a crisis occur. This is a reflection of the bank's nationwide retail network with a dominant (> 20%) market share of deposits and loans and its critical role to the country's national payment or clearing system (i.e. the system would collapse if bank defaulted). Netherlands is a low support country.

### **Foreign Currency Deposit Rating**

Moody's Foreign currency deposit ratings for Rabobank are Aaa/P-1 with a stable outlook.

### **Foreign Currency Debt Rating**

Moody's Foreign currency debt ratings for Rabobank are Aaa/P-1 with a stable outlook.

## **ABOUT MOODY'S BANK RATINGS**

Bank Financial Strength Rating

Moody's Bank Financial Strength Ratings (BFSRs) represent Moody's opinion of a bank's intrinsic safety and soundness and, as such, exclude certain external credit risks and credit support elements that are addressed by Moody's Bank Deposit Ratings. BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank's ability to honor its domestic or foreign currency obligations. Factors considered in the assignment of BFSRs include bank-specific elements such as financial fundamentals, franchise value, and business and asset diversification. Although BFSRs exclude the external factors specified above, they do take into account other risk factors in the bank's operating environment, including the strength and prospective performance of the economy, as well as the structure and relative fragility of the financial system, and the quality of banking regulation and supervision.

#### Global Local Currency Deposit Rating

A deposit rating, as an opinion of relative credit risk, incorporates the BFSR as well as Moody's opinion of any external support. Specifically, Moody's Bank Deposit Ratings are opinions of a bank's ability to repay punctually its deposit obligations. As such, they are intended to incorporate those aspects of credit risk relevant to the prospective payment performance of rated banks with respect to deposit obligations, which includes: intrinsic financial strength, sovereign transfer risk (in the case of foreign currency deposit ratings), and both implicit and explicit external support elements. Moody's Bank Deposit Ratings do not take into account the benefit of deposit insurance schemes which make payments to depositors, but they do recognize the potential support from schemes that may provide assistance to banks directly.

According to Moody's joint default analysis (JDA) methodology, the global local currency deposit rating of a bank is determined by the incorporation of external elements of support into the bank's Baseline Credit Assessment. In calculating the Global Local Currency Deposit rating for a bank, the JDA methodology also factors in the rating of the support provider, in the form of the local currency deposit ceiling for a country, Moody's assessment of the probability of systemic support for the bank in the event of a stress situation and the degree of dependence between the issuer rating and the Local Currency Deposit Ceiling.

#### National Scale Rating

National scale ratings are intended primarily for use by domestic investors and are not comparable to Moody's globally applicable ratings; rather they address relative credit risk within a given country. A Aaa rating on Moody's National Scale indicates an issuer or issue with the strongest creditworthiness and the lowest likelihood of credit loss relative to other domestic issuers. National Scale Ratings, therefore, rank domestic issuers relative to each other and not relative to absolute default risks. National ratings isolate systemic risks; they do not address loss expectation associated with systemic events that could affect all issuers, even those that receive the highest ratings on the National Scale.

#### Foreign Currency Deposit Rating

Moody's ratings on foreign currency bank obligations derive from the bank's local currency rating for the same class of obligation. The implementation of JDA for banks can lead to high local currency ratings for certain banks, which could also produce high foreign currency ratings. Nevertheless, it should be noted that foreign currency deposit ratings are in all cases constrained by the country ceiling for foreign currency bank deposits. This may result in the assignment of a different, and typically lower, rating for the foreign currency deposits relative to the bank's rating for local currency obligations.

#### Foreign Currency Debt Rating

Foreign currency debt ratings are derived from the bank's local currency debt rating. In a similar way to foreign currency deposit ratings, foreign currency debt ratings may also be constrained by the country ceiling for foreign currency bonds and notes; however, in some cases the ratings on foreign currency debt obligations may be allowed to pierce the foreign currency ceiling. A particular mix of rating factors are taken into consideration in order to assess whether a foreign currency bond rating pierces the country ceiling. They include the issuer's global local currency rating, the foreign currency government bond rating, the country ceiling for bonds and the debt's eligibility to pierce that ceiling.

#### About Moody's Bank Financial Strength Scorecard

Moody's bank financial strength model (see scorecard below) is a strategic input in the assessment of the financial strength of a bank, used as a key tool by Moody's analysts to ensure consistency of approach across banks and regions. The model output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

#### **Rating Factors**

#### **Rabobank Nederland**

Rating Factors [1]	A	B	C	D	E	Total Score	Trend
<b>Qualitative Factors (50%)</b>						<b>B+</b>	
<b>Factor: Franchise Value</b>						<b>A-</b>	<b>Neutral</b>
<b>Market Share and Sustainability</b>	x						
<b>Geographical Diversification</b>		x					
<b>Earnings Stability</b>	x						
<b>Earnings Diversification [2]</b>							
<b>Factor: Risk Positioning</b>						<b>B</b>	<b>Neutral</b>
<b>Corporate Governance [2]</b>							
- Ownership and Organizational Complexity							
- Key Man Risk							
- Insider and Related-Party Risks							
<b>Controls and Risk Management</b>		x					
- Risk Management		x					
- Controls		x					
<b>Financial Reporting Transparency</b>			x				
- Global Comparability	x						
- Frequency and Timeliness				x			
- Quality of Financial Information			x				
<b>Credit Risk Concentration</b>			x				
- Borrower Concentration			x				
- Industry Concentration		x					
<b>Liquidity Management</b>		x					
<b>Market Risk Appetite</b>	x						
<b>Factor: Operating Environment</b>						<b>A</b>	<b>Neutral</b>
<b>Economic Stability</b>	x						
<b>Integrity and Corruption</b>	x						
<b>Legal System</b>	x						
<b>Financial Factors (50%)</b>						<b>C</b>	
<b>Factor: Profitability</b>						<b>D</b>	<b>Neutral</b>
<b>PPP % Avg RWA</b>				0.88%			
<b>Net Income % Avg RWA</b>				0.92%			
<b>Factor: Liquidity</b>						<b>C+</b>	<b>Neutral</b>
<b>(Mkt funds-Liquid Assets) % Total Assets</b>				17.28%			
<b>Liquidity Management</b>		x					
<b>Factor: Capital Adequacy</b>						<b>A</b>	<b>Neutral</b>
<b>Tier 1 ratio (%)</b>	11.00%						
<b>Tangible Common Equity % RWA</b>	9.27%						
<b>Factor: Efficiency</b>						<b>D</b>	<b>Neutral</b>
<b>Cost/income ratio</b>				77.40%			
<b>Factor: Asset Quality</b>						<b>B</b>	<b>Neutral</b>
<b>Problem Loans % Gross Loans</b>		1.30%					
<b>Problem Loans % (Equity + LLR)</b>		15.81%					
<b>Lowest Combined Score (15%)</b>						<b>D</b>	
<b>Economic Insolvency Override</b>						<b>Neutral</b>	
<b>Aggregate Score</b>						<b>B-</b>	
<b>Assigned BFSR</b>						<b>B+</b>	

[1] - Where dashes are shown for a particular factor (or sub-factor), the score is based on non public information

[2] - A blank score under Earnings diversification or Corporate Governance indicates the risk is neutral

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