

Mapfre Re, Compania de Reaseguros, S.A.

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Major Rating Factors

Strengths:

- Core to the Mapfre group.
- Strong operating performance, despite catastrophe losses.
- Strong competitive position in Spain and Latin America, and increasingly in the international reinsurance market.
- Strong capitalization.

Weaknesses:

- Moderate size in a consolidating global industry.
- High dependence on retrocession capacities arising from its role as the Mapfre group reinsurer.

Holding Company: Mapfre S.A.
Counterparty Credit Rating <i>Local Currency</i> A+/Negative/--
Operating Companies Covered By This Report
Financial Strength Rating <i>Local Currency</i> AA/Negative/--

Rationale

The ratings on Spain-based reinsurer Mapfre Re, Compañía de Reaseguros, S.A. (Mapfre Re) reflect its status as a core subsidiary of Spanish insurance group Mapfre S.A. (the Mapfre group or Mapfre; A+/Negative; main operating entities are rated AA/Negative), which is derived from Mapfre Re's role as the group's exclusive treaty reinsurer, the management's strong links with other parts of the Mapfre group, and the parent's track record of capital management to fund Mapfre Re's growth. Mapfre Re's predominantly proportional book of business is deemed to affect the entire Mapfre group's risk profile only marginally, while bringing valuable diversification in non-Spanish property businesses. Mapfre Re is also regarded as a center of excellence within the group.

On a stand-alone basis, the ratings on Mapfre Re also reflect the company's strong operating performance, strong competitive position, and strong capitalization. The company's modest size in a global, consolidating reinsurance industry, and its relative dependence on retrocession capacities arising from its role as the Mapfre group reinsurer offset these positive factors.

Outlook

The negative outlook on Mapfre Re reflects that on Mapfre S.A. As a core subsidiary of Mapfre S.A., the ratings on Mapfre Re will move in tandem with those on its majority shareholder.

Corporate Profile: Main Reinsurer Of Mapfre Group, And An Increasingly Global Franchise In The Open Market

Mapfre Re was initially established to underwrite the reinsurance needs of the Mapfre group and to act as its international arm. Since becoming autonomous in 1988, Mapfre Re has significantly developed its profile as an international reinsurer and in 2008 it ranked among the 20 largest reinsurers in the world. In 2000, it acquired Chatham Reinsurance Corp. (subsequently renamed Mapfre Reinsurance Corp.; MRC; not rated) in the U.S.

However, in 2006, all new and renewal reinsurance business underwritten by this entity was transferred to a U.S. reinsurance trust of Mapfre Re, while the Canadian business was transferred to a newly created branch office in Canada. Mapfre S.A. is the majority 91% shareholder in Mapfre Re, with the remaining stakes held by several international insurers. In 2008, Mapfre Re announced the formation of its new subsidiary Mapfre Re do Brasil Companhia de Resseguros.

Competitive Position: A Strong Presence In Spanish-Speaking Markets, And Leading Provider Of Proportional Capacity

Table 1

Mapfre Re, Compañia de Reaseguros, S.A. Competitive Position					
	--Year-ended Dec. 31--				
(Mil. €)	2009	2008	2007	2006	2005
Total revenue	1,392.5	1,219.1	1,071.1	932.8	885.3
P/C: Annual change in gross premiums written (%)	13.5	12.0	10.6	7.6	17.1
Life: Gross premiums written	175.9	123.9	123.2	101.0	95.7
Life: Annual change in gross premiums written (%)	42.0	0.5	22.0	5.5	32.2
P/C: Net premiums written	1,247.8	1,091.3	961.9	894.8	830.8
Life: Net premiums written	152.3	103.3	104.5	89.5	82.7
Annual change in net premiums written (%)	17.2	12.0	8.3	7.7	18.3
Total assets under management	2,161.8	1,898.9	1,738.6	1,568.6	1,463.1
Growth in assets under management (%)	13.8	9.2	10.8	7.2	23.7

Mapfre Re has a strong competitive position that is derived from two facets, such as:

- Its exclusive role as treaty reinsurer to the Mapfre group, which provides a fast-growing and profitable revenue stream and international recognition; and
- A growing and geographically diversified presence in the international reinsurance market, which leverages the financial strength of its parent, but also reflects the strength of its cedent relationships that underpins its mostly proportional-based treaties. This strong competitive position is partly offset by Mapfre Re's relatively modest size in a global, consolidating reinsurance industry.

Historical

From its origins as a writer of mainly Mapfre group reinsurance, Mapfre Re has developed a strong stand-alone competitive position. Nonaffiliated business has been stable at about 63% of total premiums written over several years, as the pace of Mapfre group's international expansion has been matched by Mapfre Re. Premium growth has been exceptional since Mapfre Re started writing open market reinsurance business in 1982. The success of this organic growth is attributable to Mapfre Re's higher international market profile in recent years, particularly in Latin America, and more recently in Europe.

Mapfre Re has a strong relationship with its cedents, reflected in its very high client retention ratio (approximately 93% for the whole portfolio; 90% for the nonaffiliated business), and the fact that just under 70% of its premiums are written directly (although this figure includes affiliated business). A large number of Mapfre Re's new clients are coming from brokers, however. Contrary to market norms, Mapfre continues to offer coverage mostly on a proportional basis, which made up 71% of the portfolio in 2009; the remainder was split between XL and

Facultative, 22% and 7%, respectively. This provides Mapfre with a more defensive position in the reinsurance market than some of its peers and reflects both the strength of its cedent relationships and the structure of the reinsurance arrangements with the Mapfre group. This binds Mapfre Re more closely to the pricing discipline of the primary market, however. Property is the dominant class of business overall, representing 61% of total premium in 2009 (including catastrophe business), but motor, accident, health, and credit reinsurance provide a reasonable level of diversification overall.

Including intragroup cessions, Mapfre Re is the market leader in Spain by virtue of Mapfre group's position. Historically, Spain and Portugal had a relative high weight in the overall portfolio. Nevertheless, their significance is reducing in line with the international expansion of Mapfre Re's parent; their share of total premium has halved from 46% in 2004 to 23% in 2009.

Internationally, Mapfre Re operates in 104 countries, with a strong franchise in Spain, Europe, and Latin America, together with smaller operations in the U.S., Middle East, and Asia. Mapfre Re is able to write specialist products in these markets by utilizing the product expertise of the Mapfre group. The European operations are well spread and a branch office was opened in Munich in 2007 to develop Mapfre Re's presence in Central and Eastern Europe, including Russia (see chart 2). The establishment of a locally incorporated subsidiary in Brazil has strengthened the Mapfre group's presence in that market and in Latin America generally.

Prospective

We believe that Mapfre Re will maintain its strong competitive position in the Iberian and Latin American markets while further increasing its presence in the international reinsurance markets by leveraging the financial strength of the parent, Mapfre group, and its existing strong cedent relationships. Mapfre group is expected to remain a reliable source of revenue growth over the rating horizon. Nevertheless, we expect the proportion of nonaffiliated business to affiliated to remain stable at two-thirds to a third, as Mapfre Re expands its presence and its capacity in the international markets. In our view, Mapfre S.A.'s growth plans for its Massachusetts-based subsidiary Commerce Group Inc. (main operating entities are rated A/Stable/--) will increase the weighting of U.S. risks and motor business in Mapfre Re's portfolio over the long term. The geographic composition of the portfolio is expected to remain fairly stable over the next two years. As one of only a handful of reinsurers that has applied for local status in the recently liberalized Brazilian market, Mapfre Re has preferential access to 60% of cessions in the Brazilian market until 2010, reducing to 40% until 2013. Competition in this market is likely to be intense initially. However, we do not expect Mapfre Re to write a large volume of business at the outset.

Overall, we expect strong growth of at least 15% in 2010 based on Mapfre Re's impressive January 2010 renewal experience, even after allowing for the effect of weakening Euro and the currency devaluation in Venezuela. The rate of growth is also reflective of Mapfre Re's financial strength, its growth in emerging markets, its relatively low penetration of the major reinsurance markets globally, and its very low operating expenses, which provide a competitive advantage.

Management And Corporate Strategy: Long Standing And Integrated With The Mapfre Group

We view Mapfre Re's management and strategy as strong. The management team is long standing and knowledgeable, and is focused on supporting the strategic and financial objectives of its parent while continuing to grow its own international franchise. Mapfre Re remains a center of excellence within the Mapfre group, and the

senior management team has supported the development of the international operations of the parent in recent years. Mapfre Re is also the "test-bed" for the development of economic capital modeling within the Mapfre group.

Operational management

Mapfre Re has a tightly centralized underwriting policy, operating through branches rather than local companies, which is also more cost efficient. There are a few exceptions, notably in Brazil, which brings a higher degree of sovereign-related risk; however, Mapfre Re's Brazilian subsidiary benefits from comprehensive reinsurance protection from the parent. Local offices are restricted to underwriting only and are permanently linked to a central information technology system in Madrid. This enables a detailed understanding of the make-up of Mapfre Re's business, and facilitates a good balance of the portfolio as viewed by territory, line of business, and type of reinsurance contract. Mapfre Re's strengthening market profile has enabled it to attract high-quality personnel from its competitors to achieve a wider understanding of other markets and practices.

Financial management

Mapfre Re's financial strategy is conservative and focused on long-term goals, particularly with regard to international development. Capital management is strong, with capital allocated and returns measured by profit center, by country, and by line of business. The implementation of an updated version of its economic capital model is expected to further strengthen Mapfre Re's capabilities in this discipline. Capital injections from the parent to finance future growth were a feature of past years, but more recently this growth has been self-financed. The main financial targets are a combined ratio of below 100% and return on equity (ROE) of above 12%. Mapfre Re is one of the largest profit centers for the Mapfre group, representing almost 13% of net income as at half-year 2010. We do not expect Mapfre Re to exhibit the level of earnings volatility of other global reinsurers as the group would not want its consolidated results to be an outlier relative to its insurance peers. Prospectively, we do not believe that the dividend requirement placed on Mapfre Re by its parent will affect its capital base nor limit its growth.

Accounting: Few TAC Adjustments To IFRS Numbers

Mapfre Re reports under International Financial Reporting Standards (IFRS). We have made few adjustments to the reported numbers, and only in respect of calculating total adjusted capital (TAC) and classifying investments according to the appropriate asset class.

In calculating TAC in the Standard & Poor's capital model, we have made adjustments for the discounted value of loss reserves and a charge has been applied for Mapfre Re's estimate of its annual aggregate 1-in-250 year catastrophe loss, which represents about 30% of the total capital requirement.

Operating Performance: Strong, With Ability To Withstand Catastrophe Losses

Table 2

Mapfre Re, Compañia de Reaseguros, S.A. Operating Performance					
	--Year-ended Dec. 31--				
(Mil. €)	2009	2008	2007	2006	2005
P/C: Return on revenue (%)	12.4	13.0	14.0	12.7	6.9
P/C: Return on revenue including realized and unrealized gains/(losses) (%)	12.4	13.0	14.0	12.7	6.9
Return on equity (%)	14.2	14.1	12.8	12.2	N/A
Return on adjusted equity (%)	13.3	11.7	12.7	12.1	7.1

Table 2

Mapfre Re, Compañia de Reaseguros, S.A. Operating Performance (cont.)					
Return on capital (%)	20.4	17.6	19.4	18.3	N/A
P/C: Net loss ratio (%)	63.6	65.1	60.0	57.6	67.6
P/C: Total net expense ratio (%)	29.9	30.4	31.6	34.8	32.0
P/C: Net combined ratio (%)	93.5	95.4	91.6	92.3	99.7
P/C: Net investment income to net premiums earned (%)	6.8	9.7	6.5	5.7	7.1
Life: Net acquisition expense ratio (%)	21.4	25.4	22.3	20.0	18.9
Life: Net administrative expense ratio (%)	1.6	1.9	2.2	3.6	0.7
Life: General expense ratio (%)	21.9	28.4	21.3	21.4	17.8
Life: Change in administrative expenses (%)	21.1	(12.9)	(29.2)	457.0	N.M.
Life: Administrative expenses to reserves (%)	0.8	1.8	1.5	2.3	0.4

N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

We consider Mapfre Re's operating performance as strong. Mapfre Re's core business in Spain and Portugal has consistently produced excellent returns, reflected in the average combined ratio of 94.5% between 2005-2009, with a standard deviation of about 3% during this period. The strength of Mapfre Re's earnings is well illustrated by its ability to withstand the impact of losses from hurricane Klaus in 2009 and, more significantly, the Chile earthquake in 2010, the largest loss event in the history of the Mapfre group. We believe that the gradual change in the composition of the portfolio and the dilution of business in Iberia may weaken the quality of earnings, but not dramatically so. Overall, Mapfre Re's performance has been more stable than the industry over a 10-year period.

In 2009, net income increased by over 8% to €112.5 million, which maintained the ROE at 14%. The improvement in net results reflects a stronger underwriting performance, with a non-life combined ratio that improved to 93.5% (95.5% in 2008), helped by a slightly higher income from investments, which, despite lower yields, increased to €93 million in 2009 from €89 million in 2008. This result is more than respectable when viewed in the context of the severe downturn in the Spanish economy and the consequent trend of increasing claims across the whole Spanish insurance industry. It is also impressive when one takes into account the €42 million gross losses derived from the July 2009 European hailstorms and from hurricane Klaus, which hit France and Spain in January 2009. The majority of the Klaus losses emanated from France; however, some were derived from Spain, although the Consorcio de Compensación de Seguros (CCS), the government-backed Spanish catastrophe reinsurer, covered the majority of these claims. The net loss to Mapfre Re from Klaus was further limited by the structure of its catastrophe retrocession program.

Mapfre Re appears to have a very low cost operating structure. This pricing advantage appears to have been leveraged by Mapfre Re in paying a high level of commissions (including profit commissions) to its cedents. Mapfre Re has incurred operating expenses of less than 3% of net earned premiums in each of the last five years, but has paid commissions equivalent to about 30% of the same figure. This is partly reflective of the proportional business that dominates Mapfre Re's portfolio, which attracts higher commissions than nonproportional contracts.

Prospective

In our view, prospective earnings will remain strong. The strength of Mapfre Re's earnings (and indeed its retrocession program) is well illustrated by the fact that the company's €64 million net result at the second-quarter 2010 is leading it to leave its full-year profit forecast unchanged, despite incurring some €200 million gross losses from the Chile earthquake earlier this year. This constitutes the largest loss event in the history of the Mapfre group

and has caused it to re-evaluate its exposure concentrations and pricing in that country. The company's 2010 result will also be slightly affected by losses from hurricane Xynthia.

While premium rates in primary insurance have generally been softening worldwide, the reinsurance market renewals in 2010 have seen evidence of both hardening and softening, depending on the sector and/or geographical region. Even after allowing for the catastrophe losses mentioned above, we still anticipate that Mapfre Re's sound underwriting discipline and proven expertise in its operating markets will result in a combined ratio comfortably below 100% in 2010, returning to around 95% or lower in 2011. We believe that these factors, together with a conservative investment strategy and higher business volumes, will flow through to earnings, with an ROE above the 12% target in both years.

The acquisitions by Mapfre S.A. in Turkey and the U.S. could bring additional volatility into Mapfre Re's earnings in future years, principally due to the catastrophe exposure in these markets. Mapfre Re has a trading history with the newly acquired Turkish business, however, while the U.S. business that has now been fully reinsured into Mapfre Re is mostly motor risk, so the downside risk is expected to be limited.

Investments: Low Credit Risk, But Moderate Exposure To Equity Markets

Table 3

Mapfre Re, Compañia de Reaseguros, S.A. Liquidity And Investments					
	--Year-ended Dec. 31--				
(Mil. €)	2009	2008	2007	2006	2005
High-risk assets to total invested assets (%)	17.3	23.8	18.9	19.2	14.3
Illiquid invested assets to total invested assets (%)	9.0	13.9	5.3	6.2	7.2
Net investment yield (%)	4.0	4.5	3.9	3.6	3.8
Net investment yield including all capital gains/(losses) (%)	3.9	5.5	4.1	3.6	4.5
Investment portfolio composition					
Cash and cash equivalents (%)	3.0	1.8	1.8	2.9	4.0
Bonds (%)	79.7	74.5	79.3	78.0	81.7
Common stock (%)	8.3	9.9	13.6	13.0	7.1
Investments in affiliates (%)	0.6	0.6	0.8	0.8	0.9
Other investments (%)	5.3	10.0	0.8	1.0	1.1
Total portfolio composition (%)	100.0	100.0	100.0	100.0	100.0

Strategy

Standard & Poor's regards Mapfre Re's investments as strong. Credit risk is low. Market risk decreased with the lower allocation to equities since 2008. Active responsibility for all Mapfre group investments is centralized within Mapfre's investment management division. The asset allocation follows Mapfre group's investment policy, which we consider as conservative.

Credit risk

Credit risk is low, with over 70% of the fixed income portfolio rated 'AA' or higher, with the remainder principally held in 'A' rated securities. The corporate bond portfolio is heavily weighted to financial services issuers, but is globally diversified.

Market risk

The bulk (80%) of the portfolio remains invested in very high quality bonds. As long as interest rates remain at the current low level, we expect the composition of the bond portfolio to be more weighted toward corporate bonds with yields higher than sovereigns. Market risk decreased further in 2009 due to the group's decision to reduce the equity weighting of its portfolio from 10% to 8%. We do not anticipate this strategy changing over the next 12-24 months, unless equity markets rebound and volatility is reduced. The remainder of the portfolio is held in property (3%), cash (3%) and other (5%). Mapfre Re is exposed to above-average foreign exchange risk, with about 15% of total premiums transacted in five Latin American currencies. With the exception of Chile due to local requirements, Mapfre Re generally holds these assets in U.S. dollars to minimize the sovereign-related risk.

Asset-liability management

The largely short-tail nature of Mapfre Re's portfolio means that asset-liability management is not regarded as a major issue. The currency mismatch is noted above.

Liquidity: Very Strong Coverage Of Liabilities, Strong Cashflows

Liquidity is very strong, with 70% of assets held in highly liquid assets, which exceeded net technical reserves by nearly 1.5x in 2009. Net operating cashflow decreased slightly to €170 million in 2009 from €183 million in 2008, but still reflects the strong revenue growth and profitability.

Capitalization: Strong, Retained Earnings Will Finance Organic Growth

Table 4

Mapfre Re, Compañia de Reaseguros, S.A. Capitalization					
--Year-ended Dec. 31--					
(Mil. €)	2009	2008	2007	2006	2005
Reinsurance utilization (%)	31.8	32.8	33.4	31.5	31.7

Mapfre Re has strong capitalization. Capital adequacy is very strong and is expected to remain so as long as future growth continues to be financed by a high level of earnings retention. The quality of capital is strong, reflecting the absence of financial leverage, the predominantly short-tail book of business, Mapfre Re's favorable reserve development, and the generally conservative risk-retentions. Reinsurance dependence is high, however.

Reserves

We view Mapfre Re's reserves as adequate. The mostly short-tail book of business has produced small run-off profits over a long period of time. On new international lines of business with a longer tail, such as motor, tail reserves are calculated based on the yearly estimated ultimate loss ratio until development patterns can be observed over at least five years.

Retrocession

Mapfre group business is protected by a retrocession program down to a low retention level. Nonaffiliated treaty business is underwritten without retrocession, however, except for a single event and aggregate property catastrophe cover, and catastrophe excess of loss protection on the life and personal accident portfolios. This reduced level of spend is consistent with market practice in recent years due to the availability of cover in the retrocession market at an economic price.

Mapfre Re has the advantage of not being heavily exposed to catastrophe risks in Spain, which are largely covered by the CCS, although hurricane Klaus raised some uncertainties about the scope of protection provided by the CCS which have since been clarified. Mapfre Re is, however, exposed to major perils including hurricanes in Europe, the U.S., and the Caribbean. More notably, the losses in Chile have highlighted the company's exposure to earthquakes, not only in Latin America but also in Turkey. The outward catastrophe program is structured so that it would provide protection only up to a one-in-100 year event for certain perils. Having placed additional sideways cover for 2009 to protect it against an accumulation of large events, Mapfre Re has since bought an additional €25 million cover per event.

The retrocessionnaires used by Mapfre Re are of strong quality; 88% of covers placed in 2010 were with companies rated in the 'A' range or higher. The reinsurance utilization ratio remains higher than peers at 32%, but this reflects the group's role as reinsurer to the Mapfre group, through which risks are passed into the global reinsurance market. Mapfre Re's exposure to amounts outstanding from reinsurers is reasonably low at 25% of reported capital.

Financial Flexibility: Strong History Of Support From Its Parent

Mapfre Re's financial flexibility (defined as the ability to source capital relative to requirements) is strong, reflecting its core status within the Mapfre group. Over recent years organic growth has been financed through retained earnings and we expect this to continue. Should it be required, the parent group's commitment to funding growth at Mapfre Re has been amply demonstrated.

Ratings Detail (As Of August 6, 2010)*	
Holding Company: Mapfre S.A.	
Issuer Credit Rating	
Local Currency	A+/Negative/--
Senior Unsecured (1 Issue)	A+
Subordinated (1 Issue)	A-
Operating Companies Covered By This Report	
Mapfre Re, Compañia de Reaseguros, S.A.	
Financial Strength Rating	
Local Currency	AA/Negative/--
Counterparty Credit Rating	
Local Currency	AA/Negative/--
Mapfre Global Risks, Compañia Internacional de Seguros y Reaseguros S.A.	
Financial Strength Rating	
Local Currency	AA/Negative/--
Issuer Credit Rating	
Local Currency	AA/Negative/--
Domicile	Spain

*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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