

Research Update:

BNP Paribas Long-Term Rating Lowered To 'AA-'; Ratings Affirmed On Four Large French Banks, SACPs Lowered

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Overview

- We have reviewed the five largest French banks in light of more difficult economic and funding market conditions, and are taking several actions on ratings and components of our ratings.
- Funding market dislocations and negative market sentiment have revealed that the funding and liquidity profiles of the five banks are more vulnerable than we had thought.
- In our view, we see weaker economic prospects for Europe, including the peripheral countries to which some French banks are significantly exposed.
- We expect lower earnings due to this more difficult environment and higher funding costs.
- We have revised our Banking Industry Country Risk Assessment on France to Group 2 from the lower-risk Group 1.
- We believe these banks will increase their capital ratios by 2013, but until then we are placing more emphasis on their currently moderate capital positions in our ratings.
- We are lowering our long-term rating to 'AA-' on BNP Paribas from 'AA'.
- We are affirming our ratings on BPCE, Crédit Agricole, Crédit Mutuel, and Société Générale, incorporating one notch of uplift for the potential of extraordinary government support.
- However, we are lowering the SACPs on these four banks to 'a'.
- We are lowering our ratings on most hybrid capital instruments by one notch for all five banks.
- Our outlook on France's five largest banks is stable.

Rating Action

On Oct. 14, 2011, Standard & Poor's Ratings Services took various rating actions on the five largest banks in France.

Among the various rating actions, we lowered our long-term counterparty credit rating on BNP Paribas and its core subsidiaries to 'AA-' from 'AA' and affirmed its 'A-1+' short-term counterparty credit rating. The outlook is stable.

In addition, we affirmed our 'A+/A-1' counterparty credit ratings on BPCE, Crédit Agricole S.A., Caisse Centrale du Crédit Mutuel, Banque Fédérative du Crédit Mutuel and Société Générale--as well as on all the core subsidiaries of these banks. We now factor one notch of government support (rather than none

previously) into our counterparty credit ratings on these four banking groups above their SACPs. At the same time, we lowered the SACPs on the banks by one notch to 'a'. The outlooks are stable.

Meanwhile, we are lowering by one notch our ratings on hybrid capital instruments that were previously rated three notches below the long-term counterparty credit rating, for all five banks (see Ratings List for details).

For cooperative groups, the ratings on the central body--Crédit Agricole S.A., Caisse Centrale du Crédit Mutuel, and BPCE-- reflect the creditworthiness of the entire cooperative group: Groupe Crédit Agricole, Groupe BPCE, and Groupe Crédit Mutuel.

Rationale

The rating action follows the downward revision of our Banking Industry Country Risk Assessment (BICRA) for France to Group 2 from Group 1, a reassessment of the banks' SACPs, and a review of the extraordinary support that we factor into the ratings on banks from the Republic of France (AAA/Stable/A-1+).

The BICRA change reflects our revised view of banking industry and country risk in France. (See "BICRA On France Revised To Group 2 From Group 1 On Higher Funding Constraints And Rising Housing Prices," published Oct. 14, 2011, on RatingsDirect). This change, in particular our revision of the economic risk score to '2' from '1', contributed to the one-notch lowering of the long-term ratings or SACPs. A weaker economic risk score increases the capital requirement for banks operating in France according to Standard & Poor's risk-adjusted capital measure.

The downgrade of BNP Paribas and the lowering of our SACPs on the four other banks primarily reflect our opinion that the financial profiles for all of these banks have weakened as a result of more difficult economic and funding market conditions ahead. We see that their funding and liquidity positions have become more vulnerable to adverse conditions than we had previously anticipated. In addition, we believe that credit risk has risen due to significant exposure to peripheral countries for some of the banks. For these reasons, we see lower earnings prospects for all five banks. We continue to believe that the moderate current capital position of BNP Paribas, BPCE, Groupe Crédit Agricole (subsequently referred to as Crédit Agricole), and Société Générale is a ratings weakness. Tighter funding conditions are prompting all five French banks to reduce their balance sheets or issue more expensive longer-term resources. In addition, in our opinion, competition to attract more stable customer deposits in France could increase funding costs as well.

The affirmations of our ratings on BPCE, Crédit Agricole, Crédit Mutuel, and Société Générale incorporate our view of their strong market position and business diversification, good asset quality, and lower but still adequate

profitability. In addition, we consider all of them highly systemically important in France and believe that extraordinary support from the French government would likely be available if needed. We therefore factor into our long-term rating on these four banks one notch of uplift over their SACPs, which now stand at 'a'.

The one-notch downgrade of all hybrid capital instruments, which were previously rated three notches below the long-term counterparty credit rating, reflects our expectations of a somewhat higher risk of coupon deferral for all banks, in line with the negative rating actions we have taken on the five French banks and with our methodology. (See the Ratings List for details.)

French banks are currently facing risk-adverse capital markets, with a significant deterioration in their funding conditions since August 2011. They are reliant on wholesale funding because their loan books exceed their customer deposits and because of their presence in corporate and investment banking (CIB) activities. The deficit of deposits over loans is significant for BPCE and Cr dit Mutuel, but is in line with the average of large European banks for BNP Paribas, Soci t  G n rale, and Cr dit Agricole. On the other hand, these three banks have more CIB activities--with a stronger focus on corporate finance for Cr dit Agricole--that generate large balance sheets and significant short-term funding needs.

In our view, French banks have already started to adapt their funding profiles, especially with the issuance of longer-term debt and buildup of large buffers of eligible assets. In addition, because they have largely met their funding targets for 2011, we consider that French banks have some time to continue adapting their activity to new funding conditions. So far, French banks have made only marginal use of European Central Bank (ECB) funding and continue to benefit from good access to short-term funding in euros. As for other European banks, our assessment of liquidity incorporates our view of a supportive European environment, in terms of banking liquidity and support from the ECB. We incorporate these elements into the banks' SACPs.

As a result of difficult capital market conditions, BNP Paribas and Soci t  G n rale--the most exposed to the shortage of cheap U.S. dollar resources--have accelerated asset disposals, and are more quickly implementing strategic reviews of businesses originally intended to prepare for Basel III capital and liquidity regulations. Under similar constraints, Cr dit Agricole has announced a voluntary reduction in short-term funding needs and in some financing activities. We expect BNP Paribas, Soci t  G n rale, and Cr dit Agricole--and BPCE to a lesser extent--to reduce their presence in activities that demand higher leverage or that don't generate customer deposits (such as some CIB activities or some kinds of specialized lending). In France, we expect lending activities to slow, particularly in the mortgage market, and French banks to attract more household savings into retail customer deposits at the expense of mutual funds or insurance, at probably some higher cost.

We consider that the increasing cost of preserving liquidity by downsizing wholesale-funded activities, exiting some business segments--in particular

some U.S.-dollar-denominated financing--and continuing to raise more expensive longer-term resources and core deposits will contribute to weaker profitability for French banks in 2011 and 2012, on the top of a more difficult economic environment. While repricing efforts by banks could offset some of the higher funding costs, we believe this would reduce their capacity to boost capital through retained earnings.

BNP Paribas, and Crédit Agricole through its insurance subsidiary, are among the most exposed to Greek sovereign debt (Hellenic Republic; CC/Negative/C). However, we consider that the amounts remain moderate in proportion to their balance sheets and earnings capacities. Furthermore, our ratings, prior to today's rating actions, had already incorporated our estimates for an orderly restructuring of the Greek sovereign debt. We had lowered our ratings in May 2011 on Crédit Agricole because of its exposure to the Greek economy through its subsidiary Emporiki. The difficult economic prospects for Greece contribute to our expectation of pressure on Crédit Agricole's earnings in 2011-2012. French banks posted impairments on their Greek sovereign debt on June 30, 2011, on the basis of 21% of the principal of sovereign bonds that they plan to bring to the Institute of International Finance's Financing Offer for Greece launched in July 2011. This level of coverage is less conservative than what some other European banks have recognized and we don't rule out additional impairments. We already included such impairments in our earnings forecasts for the large French banks for 2011, consistent with our recovery rating of '4' for Greece, indicating an estimated 30%-50% recovery of principal by bondholders.

French banks have low sovereign exposure to Ireland and Portugal, the two other south European countries under EU/IMF adjustment plans, and Spain. The exposure to Italian sovereign debt is material for BNP Paribas and Crédit Agricole and not insignificant for the others. However, we consider that the credit risk, as signified by our 'A' rating on the Republic of Italy, is low. Both banks have also some sizable lending activity to the Italian private sector. We see that credit risk as moderate overall, but with a potential for rising provisioning needs. BNP Paribas also has some non-negligible lending activity to the Spanish private sector that represents an intermediate credit risk. Our view about Spanish credit risk is incorporated in our economic risk score on Spain of '4', which we recently revised from a lower-risk '3'.

As for most European peers, capital at French banks has increased over the last 18 months, but remains for us an identified weakness for the ratings on the banks--except Crédit Mutuel. According to our risk-adjusted capital ratio before diversification at year-end 2010, the capital positions of BNP Paribas, BPCE, Crédit Agricole, and Société Générale were lower than the average ratio for their European peers. The change in the BICRA economic risk score to '2' from the lower-risk '1' results in a moderate change in the French bank RAC ratio before diversification, ranging from a 10 basis point (bps) decline for BNP Paribas' to a 35 bps decline for the Crédit Mutuel group, the most affected by this change.

Our counterparty credit ratings on BNP Paribas, BPCE, Crédit Agricole, and

Société Générale incorporate our expectation that they will continue to further increase their capital position over the coming 24 months, in their effort to address stricter regulatory capital requirements under Basel III. We expect such an improvement to continue to take place through retained earnings but with more emphasis on reduction of risk-weighted assets than we expected some months ago. The plans that BNP Paribas, Société Générale, and Crédit Agricole recently announced to reduce their balance sheets, and meet or raise their capital targets under Basel III support this medium-term expectation. We are of the view that deleveraging will enhance capitalization over time. However, in the short term, it may not because of the earnings and funding challenges they face.

Our higher rating on BNP Paribas than on its four domestic peers reflects Standard & Poor's opinion of its comparatively stronger business profile that incorporates greater and more successful business diversification. Our rating on BNP Paribas also reflects its better earnings generation, resulting from resilient underlying revenue streams in most business lines and the absence of significant pocket of risks--as well as its more moderate risk appetite and stronger risk culture.

We view BNP Paribas as having high systemic importance in France. The long-term rating does not incorporate notches of explicit uplift for potential extraordinary support from the French government given its already high rating that reflects only its SACP.

Outlook

Our overall expectation of the environment in which French banks operate is that the French economy will remain resilient. Amid subdued economic growth, we expect that the banks will continue to generate lower but still adequate profits from their domestic market.

We could move to a more negative view about the French banking industry if French and European economic and market conditions turn out to be tougher than our base case, moving for instance toward a double-dip recession, which is likely to hurt asset quality and earnings. Or, in case of a prolonged disruption of capital markets that would reduce access to euro-denominated resources.

BNP Paribas

Our stable outlook on the long-term 'AA-' rating illustrates our expectation that the bank will continue to post satisfactory financial performances in the coming years. It also incorporates our opinion of the resilience of the bank's asset quality, and a strong improvement in its capital and funding structure, with the delivery of its significant deleveraging plan. Net operating income after cost of risk should remain sound but should decline in 2011 in our opinion compared with sound results in 2010, because of pressure on revenue, rising overhead expenses, and some additional impairments on financial assets.

We could consider a downgrade for any of the following reasons:

- If the group fails to steadily improve its capital position over the next two years to a level more consistent with its ratings.
- If fragile capital market conditions in Europe negatively affect the bank more than we expect in 2011 and 2012, particularly given its sizable trading book and investment portfolio.
- If funding constraints that force BNP Paribas to deleverage and reduce activities become so important that they jeopardize its business position or business diversification.

An upgrade appears unlikely until after capital market and economic conditions have clearly stabilized in Europe and we determine that BNP Paribas' financial profile has improved markedly.

Société Générale

The stable outlook reflects our expectation that Société Générale will post adequate although still subdued core earnings in 2011 and 2012. We also expect Société Générale's capitalization to improve regularly, notably on the back of its more aggressive focus on deleveraging measures and the acceleration of its transformation plan. We believe the bank's fundamental business profile will hold.

A negative rating action could result if Société Générale's earnings deteriorate materially--notably in case of an unexpected market shock or write-offs exceeding our expectations. Still, given the bank's high systemic importance in France, we would expect government support to be forthcoming in case of need. We consider that this support would act as a counterbalance to a weaker SACP and limit the possibility of downside effect on Société Générale's ratings.

Conversely, we consider any positive action on Société Générale's rating as remote in the near term, amid a more challenging operating environment. We believe that Société Générale's ability to post a substantial recovery in its financial performance that would result in a material improvement in its risk-adjusted capitalization is unlikely. Any positive development would first show up in an increase in the SACP to the level of the current counterparty credit ratings.

BPCE

The stable outlook reflects our expectations that Groupe BPCE will be able to cope with the more challenging operating conditions it is facing. While the group's core earnings in 2011 and 2012 will remain under its underlying earnings capacity, we are of the view that they should remain adequate, allowing for a gradual improvement in capital ratios. In the coming quarters, we also expect the banking group to seek tightened management of its balance sheet and contain its risk profile. Finally, we do not rule out divestments of noncore assets to free up capital.

We would consider a negative rating action if economic conditions worsen, leading to an unexpected rise in loan losses, or if the group's structured assets significantly impair its profitability, significantly weakening its turnaround.

Still, we continue to expect government support to be forthcoming in case of need, according to our classification of Groupe BPCE as a bank of high systemic importance. We consider that this support would act as a counterbalance to a weaker SACP and limit the possibility of downside effect on the ratings.

A sustainable recovery in the group's profitability that would result in significantly stronger capital would be positive for BPCE's stand-alone creditworthiness. However, we consider this as a remote scenario. Any positive development would first show up in an increase in the SACP to the level of the current counterparty credit ratings.

Crédit Agricole S.A.

The stable outlook reflects our view that Crédit Agricole will succeed in adapting its funding needs to the more difficult market conditions that have prevailed since mid-2011. We believe that Crédit Agricole will demonstrate resilient underlying performance in 2011, despite our projections for a less dynamic operating environment in the second half. The stable outlook also factors in our expectations that Emporiki Bank of Greece S.A. will continue to weigh on the group's financial profile. We believe that the group has sufficient retained earnings capacity to absorb possible losses related to its operations in Greece, and to continue building up capital at a pace, and up to a level, that we see as consistent with the 'A+' rating.

We could lower the ratings if earnings deteriorate materially, notably if impacts stemming from the group's exposures to the troubled Greek economy go beyond our current expectations, or if market events trigger unexpected impairments and hamper a strengthening of capitalization to the level that we expect. Nevertheless, in such circumstances, Crédit Agricole's high systemic importance in our view carries with it the likelihood that government support would materialize and limit downside effects.

We could raise the ratings if Emporiki turns around asset quality and profitability and if Crédit Agricole strengthens its capital position beyond our current expectations. At this stage, we consider the achievement of both of these conditions as a remote scenario. Any positive development would first show up in an increase in the SACP to the level of the current counterparty credit ratings.

Crédit Mutuel

The stable outlook incorporates our expectation of a strong capital base, moderate although improving efficiency in retail, and a moderate risk profile.

The outlook also factors in our expectation that the group will be able to manage the currently complex market and funding conditions, and that underlying performance will generally show some resilience in 2011, despite our view for a less dynamic operating environment in the second half of the year. We still expect only gradual delivery of diversification benefits from recent acquisitions. Notably, Cofidis S.A. will have to cope with the changes to France's legal framework for consumer financing activities resulting from new legislation in the sector ("Lagarde law").

We could lower the ratings if unexpected risks arise in consumer finance operations or in capital market activities that would impair the group's earnings capacity. A material deterioration in capitalization would be negative for the ratings, but the group's high systemic importance carries with it the likelihood that government support would materialize and limit the negative credit effects.

Conversely, we could upgrade the group if we see a sustained improvement in the performance of domestic banking, or a rebound in the earnings generation of recent acquisitions that would improve consolidated performance overall. Any positive development would first show up in an increase in the SACP to the level of the current counterparty credit ratings.

Related Criteria And Research

All articles listed below are available on RatingsDirect on the Global Credit Portal, unless otherwise stated.

Related criteria

- Bank Rating Analysis Methodology Profile, March 18, 2004
- Bank Capital Methodology And Assumptions, Dec. 6, 2010
- How Systemic Importance Plays A Significant Role In Bank Ratings, July 3, 2007
- Franchise Stability, Confidence Sensitivity, And The Treatment Of Hybrid Securities In A Downturn, Dec. 1, 2008
- Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Related research

- French BICRA Changed To Group 2 From Group 1 On Higher Economic Risks, Oct. 12, 2011
- French Banks Proved Resilient To Crisis But Will Need To Bulk Up Ahead Of Stricter Regulation, Feb. 11, 2011
- Long-Term Sovereign Rating On Greece Cut To 'CC' On Likely Default; Outlook Negative, July 27, 2011

Ratings List

Downgraded

To

From

BGL BNP Paribas S.A.

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Certificate Of Deposit	AA-/A-1+	AA/A-1+
BNP Paribas Personal Finance		
Certificate Of Deposit		
Foreign Currency	AA-/A-1+	AA/A-1+
Fortis Bank S.A./N.V.		
Certificate Of Deposit	AA-/A-1+	AA/A-1+
BNP Paribas		
Senior Unsecured (165 issues)	AA-	AA
Subordinated (29 issues)	A+	AA-
Junior Subordinated (17 issues)	A-	A
BGL BNP Paribas S.A.		
Senior Unsecured (18 issues)	AA-	AA
Subordinated (2 issues)	A+	AA-
BNP Paribas Capital Trust		
Preference Stock (1 issue)	A-	A
BNP Paribas Capital Trust III		
Preferred Stock (1 issue)	A-	A
BNP Paribas Capital Trust IV		
Preferred Stock (1 issue)	A-	A
BNP Paribas Capital Trust VI		
Preferred Stock (1 issue)	A-	A
BNP Paribas Fortis Funding		
Senior Unsecured (10 issues)*	AA-	AA
Subordinated (18 issues)*	A+	AA-
BNP Paribas U.S. Medium-Term Note Program LLC		
Senior Unsecured (4 issues)**	AA-	AA
Subordinated (1 issue)**	A+	AA-
Banca Nazionale del Lavoro SpA		
Senior Unsecured (2 issues)**	AA-	AA
Subordinated (1 issue)**	A+	AA-
Fortis Bank S.A./N.V.		
Senior Unsecured (11 issues)	AA-	AA
Subordinated (13 issues)	A+	AA-
Junior Subordinated (3 issues)	A-	A
Certificate Of Deposit (1 issue)	AA-	AA
Downgraded; CreditWatch/Outlook Action	To	From

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BNP Paribas Cardif Counterparty Credit Rating	A+/Stable/--	AA-/Negative/--
Cardif Assurance Vie Cardif-Assurances Risques Divers Counterparty Credit Rating		
Local Currency	AA-/Stable/--	AA/Negative/--
Financial Strength Rating Local Currency	AA-/Stable/--	AA/Negative/--
Downgraded; CreditWatch/Outlook Action; Ratings Affirmed	To	From
BNP Paribas Counterparty Credit Rating	AA-/Stable/A-1+	AA/Negative/A-1+
BGL BNP Paribas S.A. Fortis Bank S.A./N.V. BNP Paribas Securities Services BNP Paribas Personal Finance Counterparty Credit Rating	AA-/Stable/A-1+	AA/Negative/A-1+
Downgraded; Ratings Affirmed	To	From
BNP Paribas Personal Finance Certificate Of Deposit Local Currency	AA-/A-1+	AA/A-1+
BNP Paribas Certificate Of Deposit Local Currency	A-1+	A-1+
Ratings Affirmed		
BNP Paribas Certificate Of Deposit (1 issue) Commercial Paper (1 issue)	A-1+	A-1+
BGL BNP Paribas S.A. Commercial Paper (2 issues)	A-1+	
BNP Paribas Canada Commercial Paper (1 issue)	A-1+	
BNP Paribas Finance Inc. Commercial Paper (1 issue)**	A-1+	
BNP Paribas Fortis Funding Commercial Paper (1 issue)*	A-1+	
BNP Paribas Personal Finance		

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Certificate Of Deposit (1 issue)	A-1+	
Fortis Funding LLC		
Commercial Paper (1 issue)*	A-1+	
*Guranteed by Fortis Bank S.A./N.V.		
**Guranteed by BNP Paribas.		
Ratings Affirmed		
BPCE		
BRED-Banque Populaire		
Credit Agricole S.A.		
Natixis S.A.		
Caisse Centrale du Credit Mutuel		
Banque Federative du Credit Mutuel		
Societe Generale		
Counterparty Credit Rating	A+/Stable/A-1	
Certificate Of Deposit	A+/A-1	
Downgraded		
BPCE		
Credit Agricole S.A.		
Banque Federative du Credit Mutuel		
Caisse Federale du Credit Mutuel Nord Europe		
Credit Mutuel Arkea		
Societe Generale		
Junior Subordinated (16 issues)	BBB	BBB+
CA Preferred Funding Trust		
Preferred Stock (1 issue)	BBB	BBB+
CA Preferred Funding Trust II		
Preferred Stock (1 issue)	BBB	BBB+
CA Preferred Funding Trust III		
Preference Stock (1 issue)	BBB	BBB+
CL Capital Trust I		
Preferred Stock (1 issue)	BBB	BBB+
Guaranteed by Crédit Lyonnais		
Credit Lyonnais		
Junior Subordinated (1 issue)	BBB	BBB+
SG Capital Trust I LLC		
Preferred Stock (1 issue)	BBB	BBB+
SG Capital Trust III		

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Preference Stock (1 issue)	BBB	BBB+
SG Preferred Capital II LLC Preference Stock (2 issues)	BBB	BBB+

N.B. This list does not include all ratings affected.

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