Date: 13 December 2007
Ref: 07-831

CESR's 2007 report on Credit Rating Agencies (CRA's):

Responses to a list of questions for the CRAs.

As a follow up of the meetings held with Credit Rating Agencies (CRAs) at the beginning of October and in order to obtain the necessary data to fulfil the European Commission's new request to review the role of CRAs in relation to structured finance on 14 November, CESR sent a letter asking for additional information to the 4 CRAs which have agreed to be part of CESR's voluntary framework.

On 20 November, CESR published the list of questions (Ref. CESR/07-781) submitted to the CRAs.

The questions dealt with the following areas of the structured finance market:
- Transparency of rating methodologies;
- Human resources allocated to rating and monitoring;
- Periodic monitoring of the ratings;
- Methodology changes;
- Potential conflicts of interest (i.e. remuneration structures of CRAs).

CESR publishes today, the responses to these questions, annexed to this document.

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Insight beyond the rating.

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December 7, 2007

DBRS Public Only Responses to CESR Request for Information sent on November 14, 2007

Transparency of methodology

1. **Publication of methodologies and assumptions:**
   a. Is there a section on your website devoted to the publication of your methodologies?

Yes, on dbrs.com see Methodologies and also see Rating Policies. Methodologies are in alphabetical order for Corporate industries and Structured Finance product groups.

   b. Do you provide explanations of the methodologies applied to the different categories of ratings for each asset class (e.g. RMBS, CDO, etc) separately by region?

Yes, each methodology contains a general overview and a description of the key analytical considerations that are reflected in our ratings.

   c. Do you provide the full method applied to each category of rating for each asset class (e.g. RMBS, CDO, etc.) separately by region?

Yes.

   d. Is all of the above information freely accessible or is part of it only available for subscribers?

Yes, our methodologies and rating policies are free of charge to the public.

2. **Publication of changes in methodologies and assumptions:** Are all changes/adjustments to your methodologies and assumptions **published** and, if yes, where exactly are they published?
   a. Is there a special section on your website where changes made to criteria can be reviewed over time?

DBRS has a methodology section on our website.

b. Do you publish reports that discuss the changes made to criteria?

Yes. When an update to an existing rating methodology or model has been approved, we publish a press release that announces the change and the implementation date of the changes, which assists in ensuring investors and issuers are aware of the changes.

For those asset classes that use models, we also announce changes to the assumptions used in the model in our model notes. DBRS models are posted to the website free of charge.

c. Do you have press conferences to announce and explain those changes?

We release our changes by way of press release and in some cases have supplemented this by way of teleconferences that are open to all market participants. DBRS has been an increasing user of conference calls for market participants to discuss major rating events, but to date, this medium is still used on a very selective basis.

3. Do you provide links/references to those publications mentioned in question 2 in the respective rating change reports (i.e. the announcement of a change would let the reader know where to find the related methodology)?

The press release indicates where on dbrs.com to find our methodologies. We do not provide a link between our methodologies and each rating report due to several factors: the high volume of rating reports; the fact that more than one methodology may apply /underlie each report; and the administration to keep the links current when a methodology is updated.

4. If changes have been made to your methodology for a particular product type (say US sub-prime RMBS) but previous issues have not been reviewed against this methodology how do you ensure this is clear to the marketplace? If the previous issues were being reviewed how would this be made public?

DBRS makes it clear by way of press release.

5. Is publishing the methods you use enough to meet the requirements of the IOSCO Code and ensure sufficient transparency or do you see further possibilities for **improving transparency/the understanding** of
   a. your ratings?
   b. your rating process?

DBRS publishes the meaning of its ratings, rating definitions and scales, supporting rating policies and the rating process under Rating Policies on dbrs.com.

While we believe the title Rating Policies is self-explanatory, we suggest there is a need to improve market understanding of what a rating is/is not, the role of a rating agency, the basis of the information we receive to conduct the rating and other aspects of the Corporate and Structured Finance rating processes. This would include using a disclaimer of sorts that is made very obvious to the reader as well as providing additional communication vehicles and educational forums to assist with more transparency and understanding.

6. What steps does your firm take, if any, to contribute to enhancing the financial education of investors or potential investors?

DBRS firmly believes in market transparency and education. To that end, we lead conference calls on a variety of topics including industry updates, specific issuers and current topics. We publish newsletters, commentaries and industry studies on an ongoing basis. We hold conferences in Canada, US and Europe on a variety of Corporate and Structured Finance areas, and we participate as speakers in other third party conferences.

7. Do you take steps to clarify any limitations to your ratings, including what they are intended to cover, or the methodologies and the assumptions underpinning them? How do you do this?

There is a section entitled Disclaimers on dbrs.com and our ratings reports include disclaimers.

8. Do you publish, and if so, where, your approach to the **use of confidential information** in rating of Structured Finance (SF) operations? Does it differ from that which you follow in "traditional" corporate rating?

The DBRS Code of Conduct ("DBRS Code") outlines our policy on the use of Confidential Information. The DBRS Code can be found under the Governance & Regulatory Affairs link on dbrs.com. It does not differentiate the use of confidential information between our Structured Finance and Corporate business. The DBRS Code sets out very clearly how confidential information is to be treated within DBRS by staff on a "need to know" basis only and a prohibition with outside parties except as an issuer may expressly authorize or as required by law. Breaches are not tolerated. DBRS also has internal guidelines in place regarding the disclosure of information between Corporate and Structured Finance groups.

9. Do you consult with industry as to what disclosure levels they would like to see for methodology and model assumptions?

At present, DBRS does industry consultation on a selected basis. We have begun to request public comment on proposed select new methodologies and policies prior to their *implementation, although this remains very limited at this time. There has been some debate whether this is a useful tool; however, we believe it can be a useful tool in providing investors an opportunity to share their issues and concerns regarding various sectors.*

Human Resources

10. Please provide us with the following information with regard to SF ratings and traditional ratings:
    a. Exhibit 4, 8 and 13 of your NRSRO application form.

See attached Exhibit 4 and Exhibit 8 of our NRSRO application. Note that the public exhibits of our NRSRO application including these documents can be found under Form NRSRO under the Governance & Regulatory Affairs link under dbrs.com

    b. The internal definition of the existing classes/levels of employees in the CRA's rating business: e.g. junior/mid/senior analysts, supervisors, committee analysts, lead analysts, etc? [1]

The same as highlighted on Exhibit 8.

17. Do you outsource part of the rating/surveillance process (e.g. data gathering, processing, modelling, etc.)? If yes:
    a. Please describe in which part(s) of the rating/surveillance process you make use of outsourcing and to what extent.
    b. What are the risks implied by such outsourcing and how do you tackle these?
    c. Do you consider the (economic) gains of such outsourcing to exceed the risks?

DBRS does not outsource any part of its ratings or surveillance process.

Monitoring of transactions

18. What drives the frequency of rating review for Structured Finance? Why is this frequency appropriate? Please outline the process that would lead to a rating being taken to review committee?

DBRS monitors all of our outstanding Structured Finance ratings on a frequent basis as our opinions or views may change over time as facts develop. Exogenous factors including

[1] This question is designed to enable the CRA to answer the other questions based on its **own** human resources structuring method as different CRAs may have different human resources structures or seniority definitions (junior/senior, analyst/supervisor…).

changes in the regulatory or legal environment, macroeconomic trends or outlook and observed trends in other similar types of transactions are always considered.

As part of the rating process, the issuer is responsible for sending performance reports that summarize the performance of the rated debt and the underlying assets to DBRS, usually with the same frequency as the payment of the rated debt, typically monthly or quarterly.

DBRS believes this level of review frequency is sufficient as the information contained within the issuer's reports is integral to our ability to monitor outstanding transactions and more frequent reviews without new data provided by the issuer would not provide additional value.

Upon receipt of the reports, DBRS surveillance analysts promptly review the performance reports. In addition to reviewing the transaction's compliance with the transaction's covenants and performance triggers outlined in the legal documents, DBRS analysts also review collateral performance trends including delinquency and loss patterns, both on a relative and absolute basis.

Current performance is assessed against DBRS expectations at transaction inception. Since collateral performance trends typically decline in advance of a breach of covenants, DBRS looks to anticipate performance issues on a forward looking basis through its review of collateral trends. Those transactions that perform outside of DBRS expectations or any other rating action taken on a credit (including rating confirmations) are reviewed and approved by a rating committee.

In cases where DBRS does not have sufficient information at the time to make an informed rating decision, a rating committee may place the issuer or security Under Review with Positive, Developing or Negative Implications. DBRS strives to resolve the Under Review status as expeditiously as possible.

19. Would regular reviews and announcements on the appropriateness of Structured Finance ratings - possibly based on some contractual deadlines (i.e. on a regular (quarterly/semi-annual basis) - help in preventing mass downgrades, improve the appropriateness of existing ratings? If not, why?

No, the process used by DBRS already results in rating changes being taken when such are appropriate. Regular reviews assist in ensuring that ratings are current and the quality of the rating methodology employed in addition to regular reviews of outstanding transactions assists in mitigating rating volatility.

20. What changes have you made in terms of the surveillance of ratings since the widespread RMBS and CDO downgrades earlier this year?

DBRS has always performed regular reviews for all outstanding ratings and publishes press releases or rating reports detailing the results of the reviews to the marketplace.

21. How is the appropriate portfolio size determined for Structured Finance monitoring analysts? Are there any internal procedures which dictate how many transactions a monitoring analyst should be responsible for?

At DBRS, the surveillance manager in concert with the Managing Director responsible for each individual business line determines the level of resources needed to address surveillance responsibilities. DBRS internal procedures do not dictate the number of transactions per analyst as the assignments are based on the degree of complexity of each sector's outstanding transactions, the degree of heterogeneity of transaction types in addition to other similar factors. As outlined in our response to question 15, this varies by asset class.

22. Are the costs of monitoring Structured Finance transactions fully covered by the fees charged specifically for monitoring when the rating agreement is initially made? What are the main incentives for maintaining effective monitoring of ratings?

The cost of monitoring Structured Finance transactions or Surveillance fees are included in the ratings fee for the first year. After that, an annual fee is due on the first anniversary date of the transactions date of issuance through the life of the transaction, or until the rating is discontinued. The main incentive for monitoring transactions is to maintain the accuracy of the assigned ratings over time, which means to ensure our ratings are prospective as possible. By reviewing the underlying data that supports Structured Finance transactions, determinations are made as to the accuracy of the ratings which are the basis for the confirmation and migration of ratings that are outstanding.

DBRS has an obligation to our investor constituents to provide current views on all of our outstanding Structured Finance ratings. DBRS reputation and standing in the marketplace could be eroded and could potentially suffer economically by not providing this service.

23. How is committee time dedicated to rating reviews versus that dedicated to new ratings determined, particularly for Structured Finance? Are there clear internal procedures on how committee time is prioritised?

DBRS maintains sufficient staff to ensure rating committees, for both new and existing ratings, are scheduled with equal priority. DBRS has detailed internal procedures that support the rating committee policy and process and that address how to deal with new ratings versus reviews.

24. Are the committee members reviewing a rating the same as those who approved the initial rating? Are there any internal procedures dictating the composition of the review committee?

DBRS maintains an established rating committee voter eligibility list for each sector within the Structured Finance business. The purpose of the list is to ensure that rating committees are comprised of staff with an appropriate level of experience and expertise in a sector. The Group Managing Director – Rating Committee, Group Managing Director – Structured Finance and Managing Director – Credit Policy are responsible for selecting each voter and evaluating membership periodically. Each voter is granted the responsibility to vote on rating committees for both initial and subsequent rating recommendations; however, the exact quorum for an initial rating may or may not be replicated for subsequent rating actions.

25. Is there a team of macroeconomic analysts within your firm responsible for systematically analyzing macro data coming in and building macroeconomic forecasts on which analysts can rely for their modelling/monitoring of ratings? If not, would this be useful?

DBRS does not currently employ a team of macroeconomic analysts within the firm that has the above named responsibility. We employ a Quantitative Analytics Group in addition to quantitative analysts within individual business lines that are responsible for supporting model development. The Structured Finance and Corporate groups liaise with regards to macroeconomic and industry conditions and the potential effects on outstanding Structured Finance transactions.

Methodology changes

27. What prompts a review of rating methodology? Is there a central team that reviews methodologies or is it dependant on individual business lines self-evaluating their models?

During 2007, DBRS implemented a Criteria Committee comprised of senior level Structured Finance staff with the purpose of reviewing and approving criteria in advance of publishing the criteria into the marketplace. The Criteria Committee is also tasked with reviewing existing methodologies on an annual basis and determining, if and when updates to methodologies should be published. In addition, the individual business lines are also responsible for identifying factors that may warrant a review and update of an existing methodology. The rationale for reviewing a methodology may be driven by the analysis of surveillance information, a potential change in the regulatory or legal landscape amongst other factors. The initial review of methodologies is conducted at the business line level prior to being raised to the Criteria Committee.

28. Have you made any changes to how you evaluate the appropriateness of your methodologies on an on-going basis in light of the RMBS and CDO downgrades of earlier this year?

We have not made a change as to how we evaluate the appropriateness of our methodologies. As mentioned above, DBRS periodically reviews its methodologies with the rationale for review driven by the analysis of surveillance information, a potential change in the regulatory or legal landscape amongst other factors.

29. When the methodology for a type of Structured Finance product (example being US sub-prime mortgage backed securities) is amended:

    a. Do you automatically review all existing ratings against the new methodology and take rating action based on this review? If not, what is the rationale behind this?
    b. How is the scope of the application of the change of methodology determined? In other words on what basis does your firm decide whether or not to apply a change to existing ratings or just to new issuances?
    c. Please explain in detail how is the timing of rating action determined across all affected ratings?

DBRS would evaluate all outstanding transactions against an updated methodology and would take rating action based on the results of the review. The DBRS Criteria Committee would determine the scope of the application of the change in methodology. Upon the release of an updated methodology, DBRS would publish a press release that included a list of outstanding transactions that are affected and provide the current, updated rating and rationale for the change, as part of the press release.

30. Does your firm at any time make any overall review of the changes to methodologies made, for instance during one year, and their impact on ratings to assess trends for instance? Would this be made public?

DBRS has not historically made significant changes to established methodologies prior to 2007. See response to #29 for what DBRS does on an individual basis. DBRS may consider such an overall approach as part of our planning process.

31. Is there a risk of originators 'gaming the system' i.e. keeping requested data sets high whilst other valid indicators of asset quality decline? If yes, what mitigation have you put in place to reduce this risk?

We understand the objective of this question is to find out how the rating agencies ensure that the information supplied by originators reflects the real situation of the assets, not omitting any relevant indicators.

DBRS does not audit or verify the information provided by originators but we do subject the information to a reasonableness test. We also participate in on-site reviews of the entities we rate and the reviews are conducted by seasoned professionals that maintain product expertise.

32. Do you feel that your approach to the assessment of the quality of underlying asset data is appropriate? Are you considering any changes in this area (specially in light of the recent events in the US sub-prime mortgage market)?

DBRS believes that our approach to the assessment of the quality of underwriting data is appropriate as we believe that the preponderance of issues in the U.S. sub-prime mortgage market is related to lax adherence to underwriting standards rather than asset data issues.

Conflicts of Interest

33. When you rate a Structured Finance operation do you offer services such as impact assessment and/or models of evaluation or optimisation of the securitization structure? Can you quantify[2] the number of cases where these kinds of services were offered? Would these services be performed by the analyst who rates the final structure?

No. For DBRS, impact assessment relates to Corporate issuers and means the feedback we provide at an issuer's request as to the effect of a potential specific transaction or event (such as a merger, acquisition, divestiture, new debt structure, or a change in the parent company) is likely to have on a rating. DBRS views this work as an extension of the typical rating relationship and not as a separate business line.

34. Is the analyst assigned to a certain Structured Finance rating deal allowed to give advice to the participants (before the rating is issued) about how to structure the deal in order to raise the rating? Is the analyst allowed to give feedback to the participants of a deal if the initial rating does not meet expectations? Are there limits to which elements of the deal can be addressed and to what extent (i.e. does the analyst provide suggested changes to the structure)? Is this covered in any internal policies? Is this interaction monitored by the agency?

[2] E.g. in percentage of total Structured Finance ratings issued, or by giving the indication "always", "often", "sometimes" or "never".

DBRS analysts are not permitted to give advice to the participants (before the rating is issued) about how to structure the deal in order to raise the rating. This would be akin to structuring transactions in which DBRS does not engage.

An analyst will provide feedback in the form of credit enhancement levels based on DBRS published methodologies and criteria but does not suggest changes to the structure. In Structured Finance transactions, issuers typically have expectations regarding rating levels for the securities that comprise their transaction's capital structure. DBRS applies its published methodologies and criteria to the proposed financial structure to determine the requisite level of credit enhancement at each rating level. Issuers or their agents may refine their structures or collateral pool and, as a result, may require additional discussions with DBRS analysts.

DBRS does not view the iterative process in rating Structured Finance transactions as involving additional conflicts of interest compared to Corporate ratings. Transparency of the ratings process and conflicts of interest are managed through an objective Rating Committee process which is used for all Structured Finance rating decisions.

DBRS is governed by an entity wide Code of Conduct that includes strict conflicts of interest policies and procedures including personal trading requirements that govern all management and staff, regardless of level, title and business sector.

35. Can factors such as greater complexity and/or innovative features in a Structured Finance deal lead to a higher than standard fee? If yes, please indicate how much these aspects can increase the initial level of the fees (as a percentage), how this increase is determined and who makes this decision.

DBRS has a standard set of up-front and surveillance fees that are shared with clients across products and regions. Generally, in Structured Finance these fees are charged on a per transaction basis and in certain cases there is an initial set up fee for larger program type ratings as well as transaction and surveillance fees. There are instances where the ultimate fees charged are higher than the indicated standard fees based on the complexity of the transaction being reviewed. Determining the amount of this fee is the joint responsibility of Business Development and the Managing Director in the relevant product group(s). While the specific percentage of increase varies greatly based on the nature of each transaction, the basis for the incremental fee increase is determined by the incremental level of effort required to accurately and thoroughly review each transaction.

This assessment is completed by the assigned rating analyst who provides this input to Business Development and/or the relevant Managing Director in the form of the incremental time and materials required to complete the rating. Based on these internal cost parameters, the incremental fee is then determined by the relevant Managing Director and/or the BD representative and communicated to the client.

Note that as outlined in the DBRS Code of Conduct, analysts may quote factual fee-related information and/or send standard fee schedules to current or proposed issuers, but DBRS analysts below Managing Director may not be involved in any fee discussions with clients.

Miscellaneous

37. Are you satisfied with the level of information received from servicers of European mortgage pools? Is this of a different quality, level of standardisation or frequency to information received in the US?

Mortgage pool information received in Europe varies depending on the jurisdiction with the United Kingdom being one of the more 'advanced' in terms of detail. Certain issuers/servicers are also relatively more active in producing timely and detailed reporting.

As a generalization, we suggest there is room for improvement in Europe, in terms of loan level information, frequency and other details in addition to the nature of standardization of definitions of items reported. Differing data and disclosure regimes in different European countries also present an added dimension of complexity.

38. Are ratings across different asset classes similar in terms of pace and pattern of migration? Would some form of volatility indicator be possible, and appropriate for Structured Finance ratings?

At present, DBRS does not separate product data within the Structured Finance business in this fashion. We separate our data between Corporate and Structured Finance, and the frequency and pattern of migration is different between these two businesses.

Within Structured Finance, the rating dynamics of different asset classes (and indeed different tranches within the same asset class) will be driven by a number of factors, including leverage, portfolio granularity and transaction structure. The use of quantitative models for transaction analysis can also introduce additional ratings volatility, which needs to be measured and mitigated wherever possible through methods such as stress testing. The development of volatility indicators would be a positive step in this direction, and would improve the transparency and understanding of the potential performance of ratings over time. However, DBRS suggests that the implementation of a new rating scale to capture volatility is likely not a workable solution given the discontinuity it would present between current and future rating scales of similar products. Such a move may lead to more confusion than confidence within the marketplace.

An alternative that DBRS would be more willing to consider would be the provision of additional information - complementary to the rating - that provides an indication of the potential degree of rating volatility. This could either be quantitative, in the form of *expectations of downgrade likelihood over a certain horizon (e.g. 1 year), or qualitative, in the form of scenarios that might lead to a downgrade."*

Exhibit 4A – Organization of DBRS Affiliates

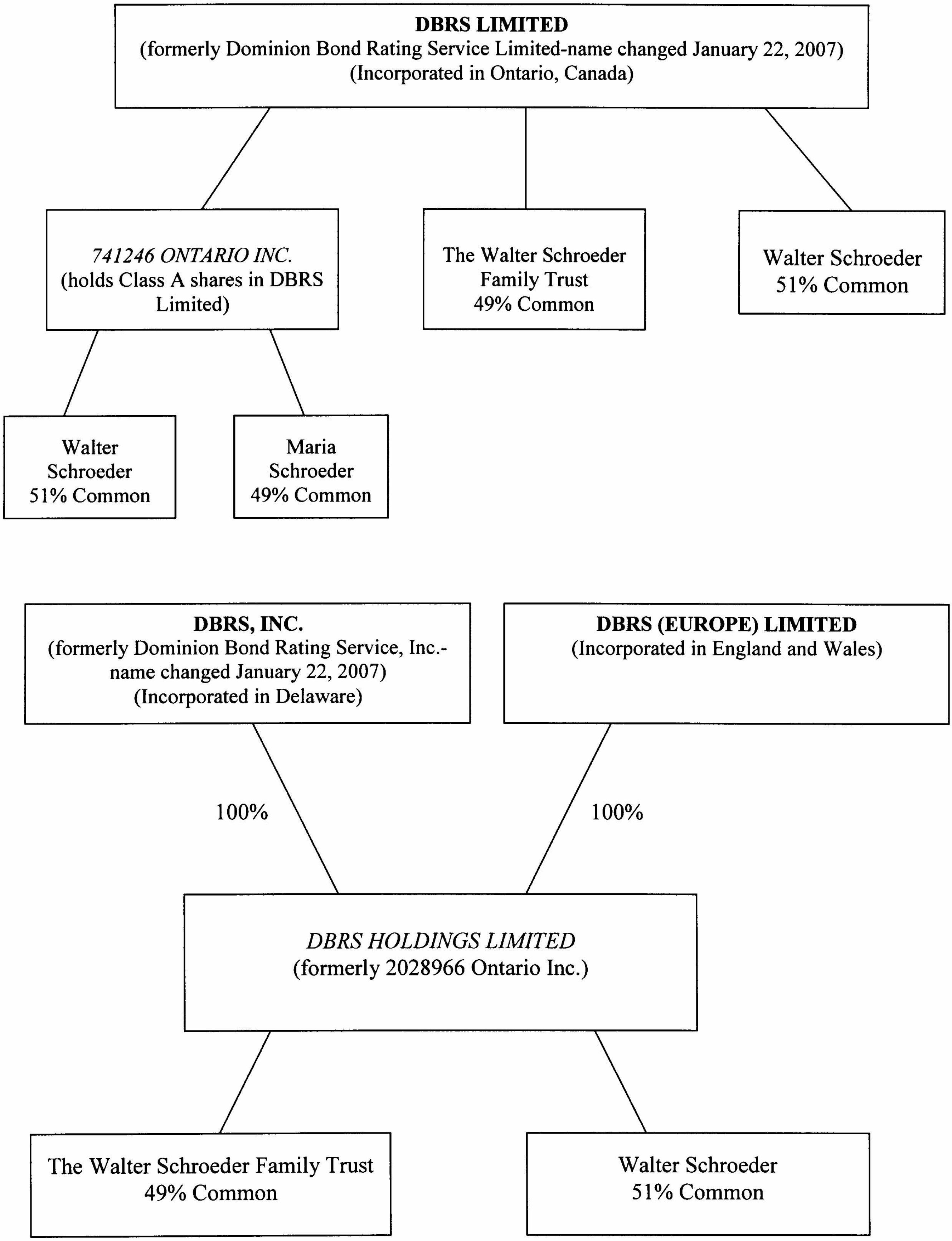

Exhibit 4B – Divisions, Departments, Business Units & Managerial Structure

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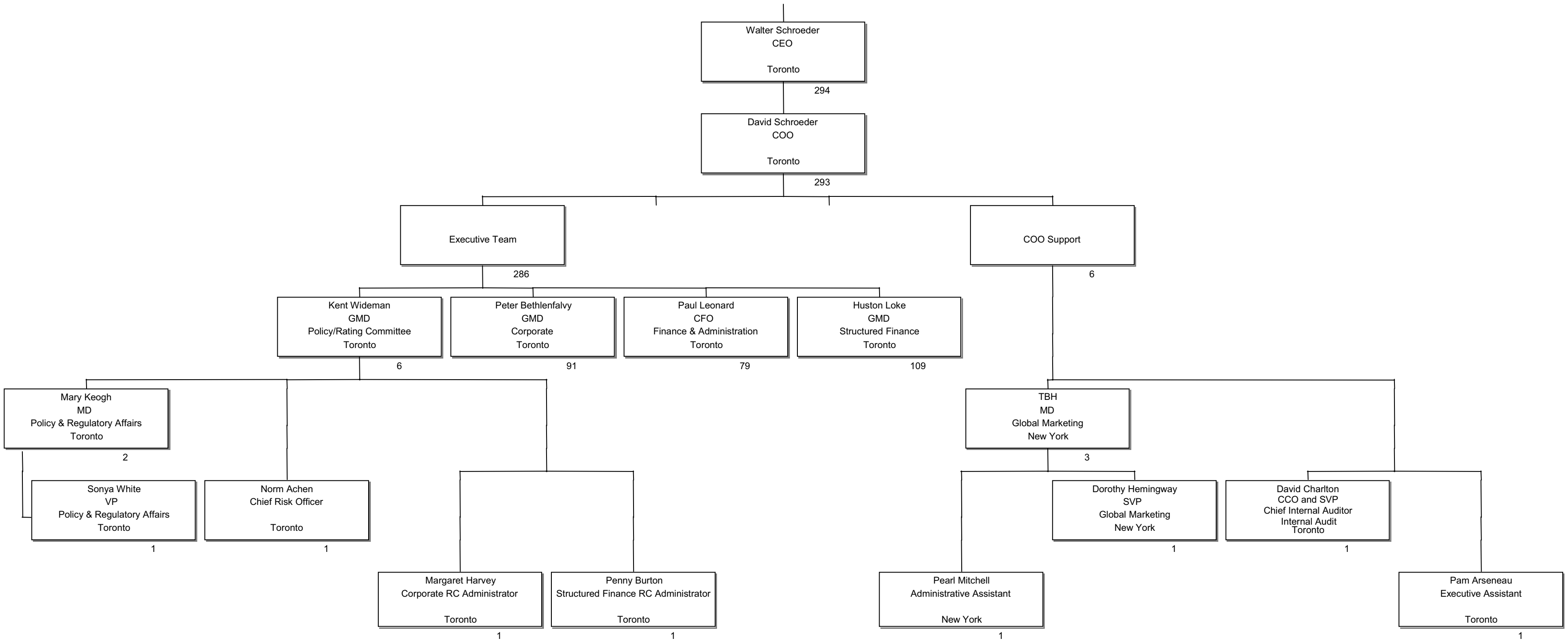
Executive Team



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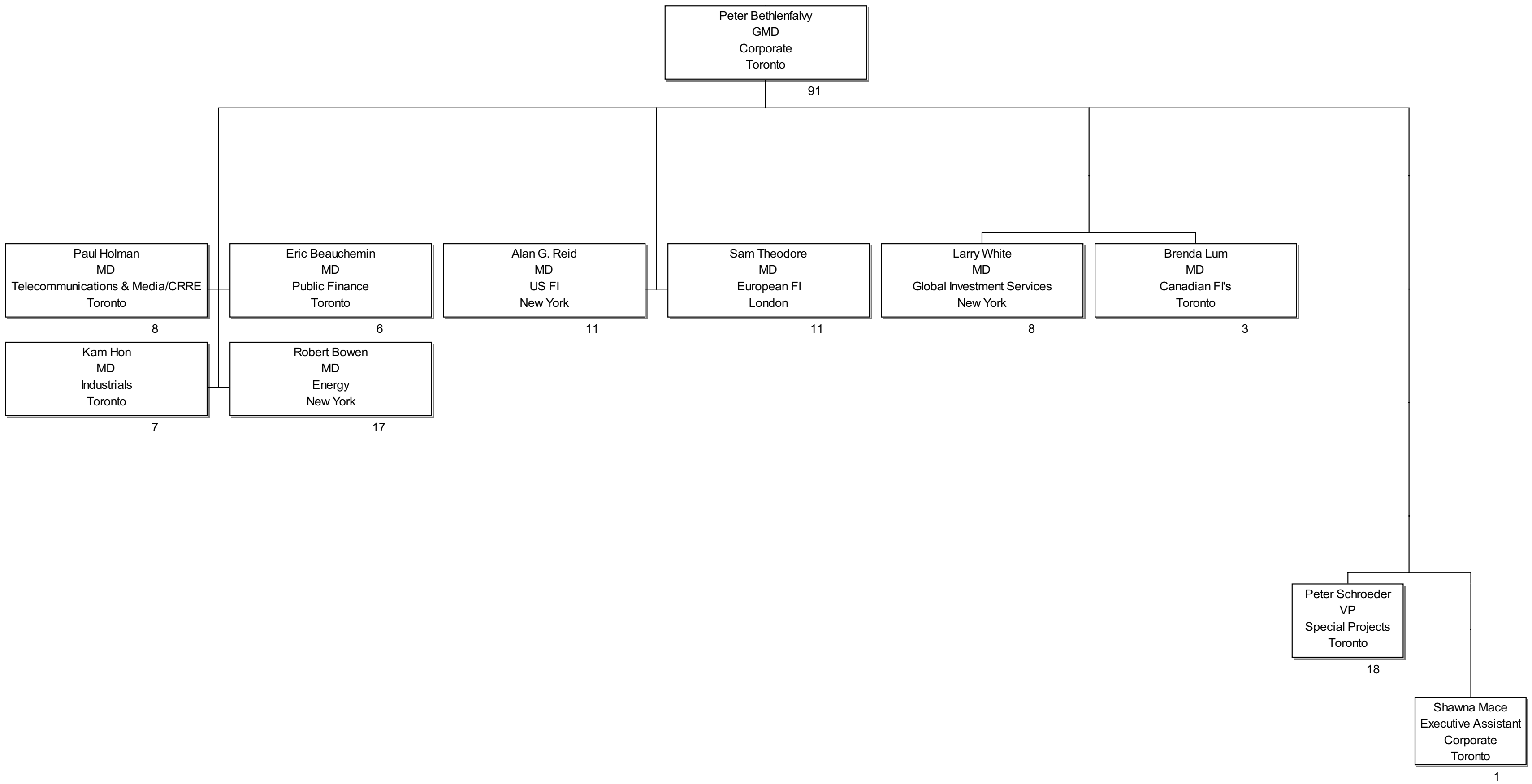
Corporate



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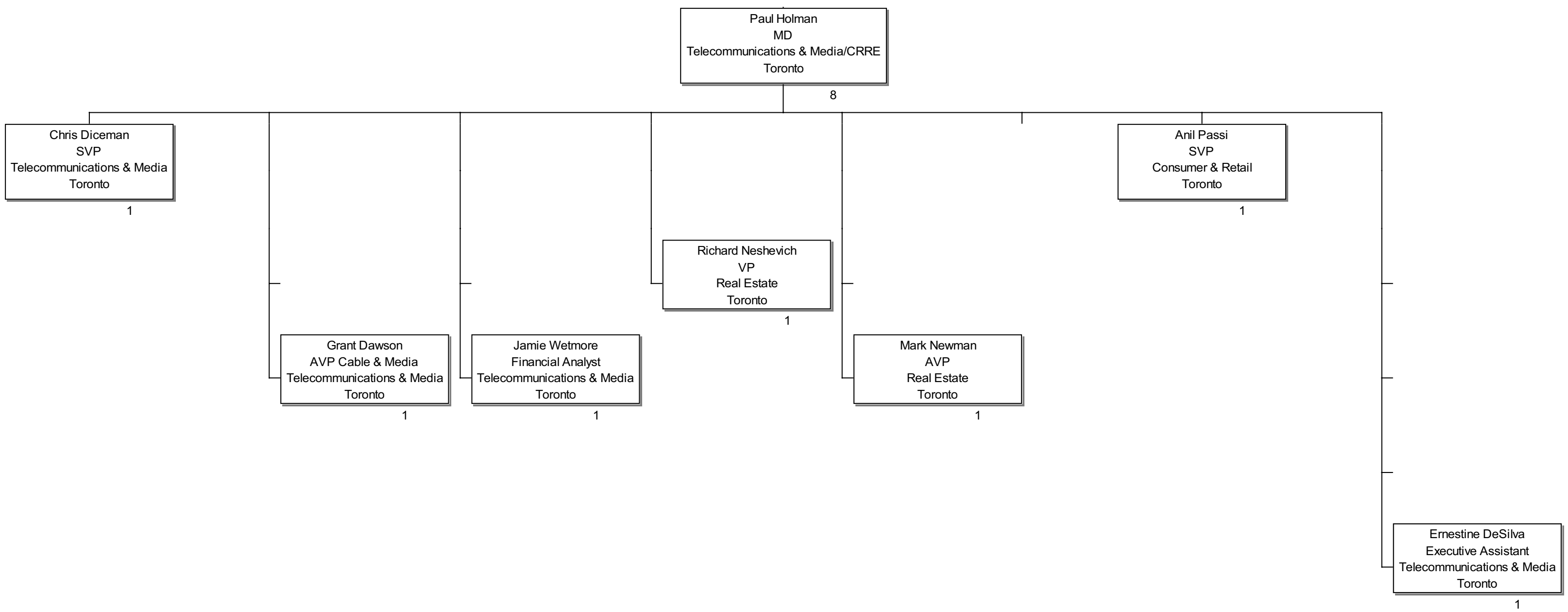
Corporate
Telecommunications & Media
Consumer/Retail/Real Estate



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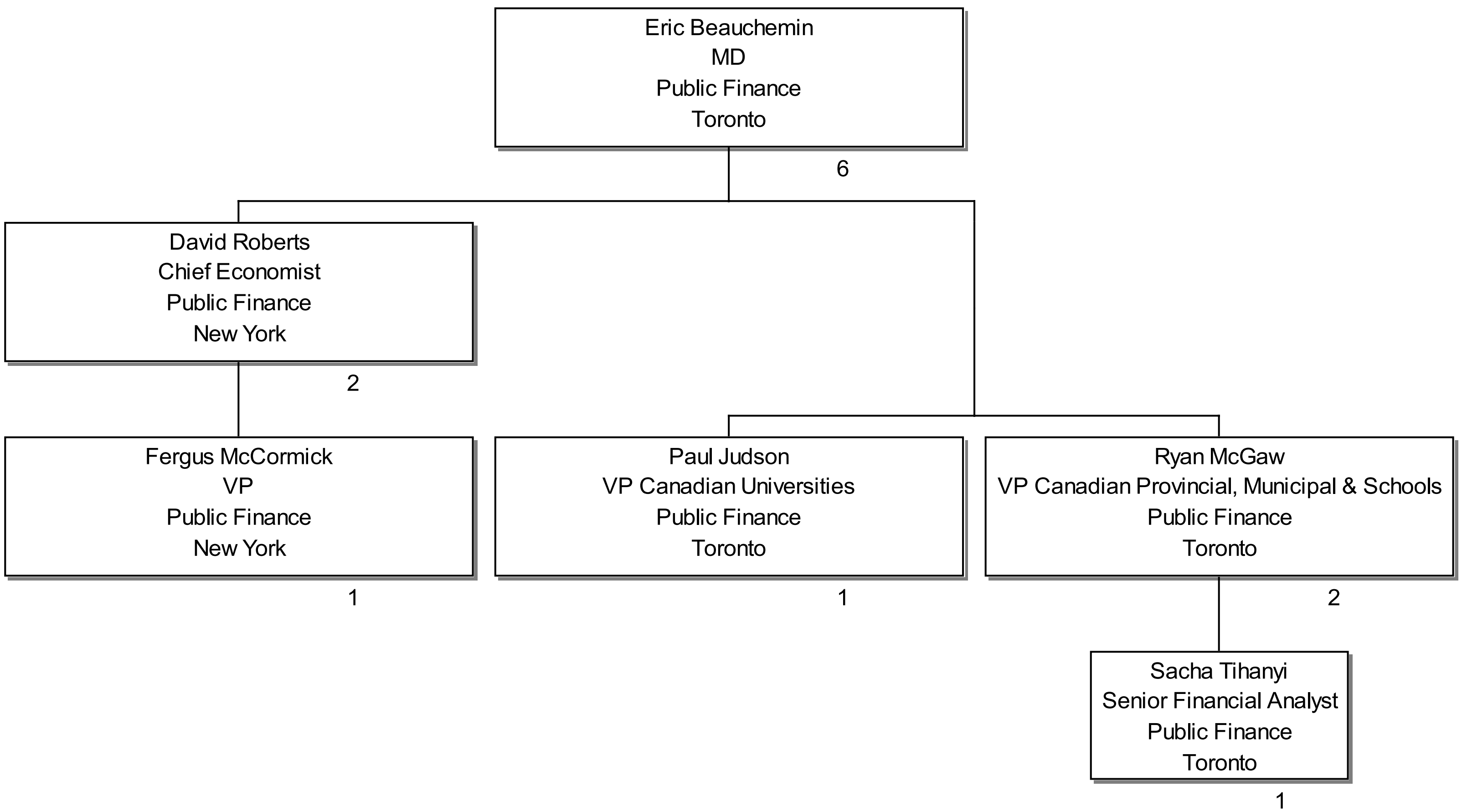
Corporate
Public Finance



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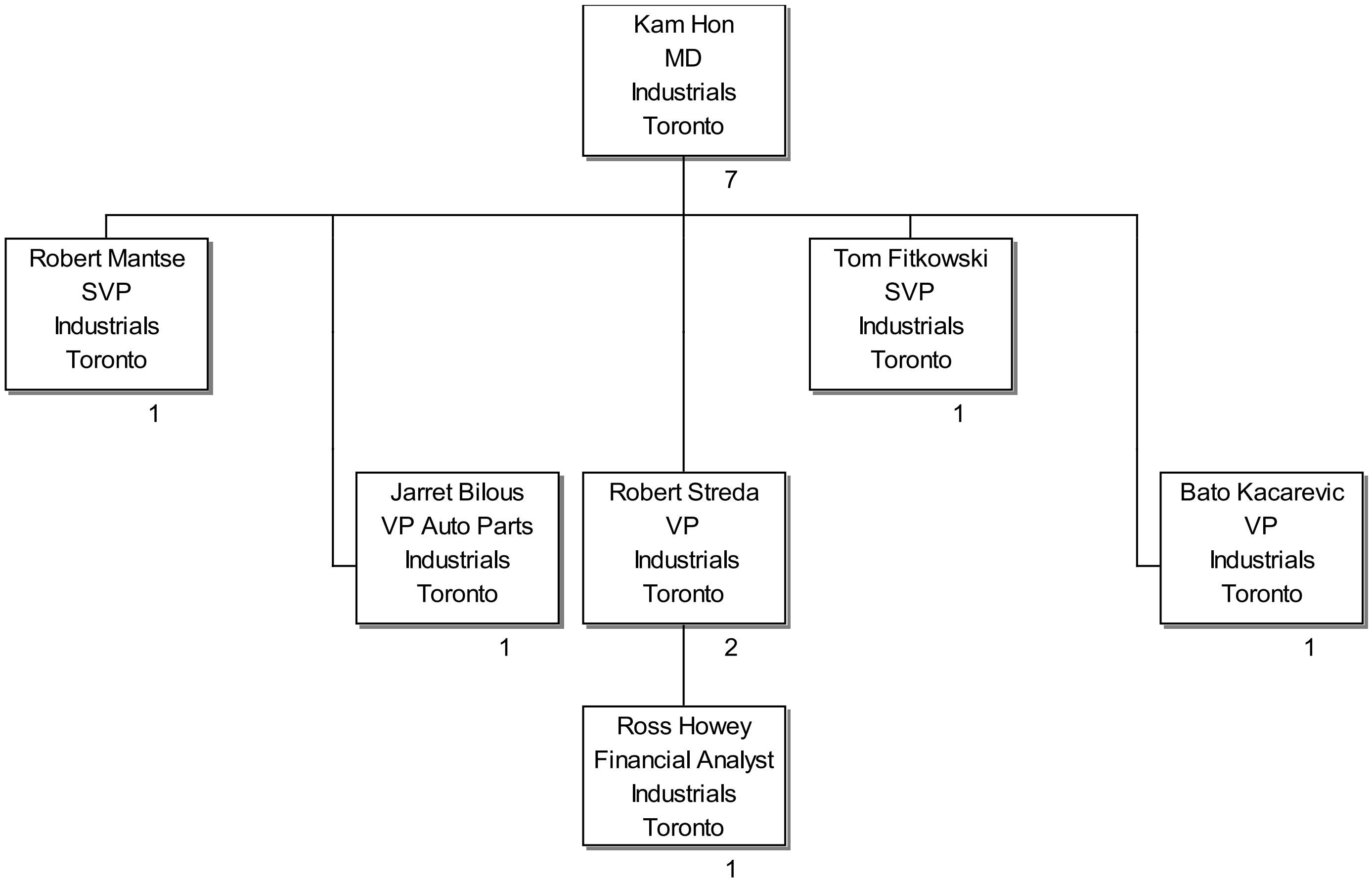
Corporate
Industrials & Natural Resources



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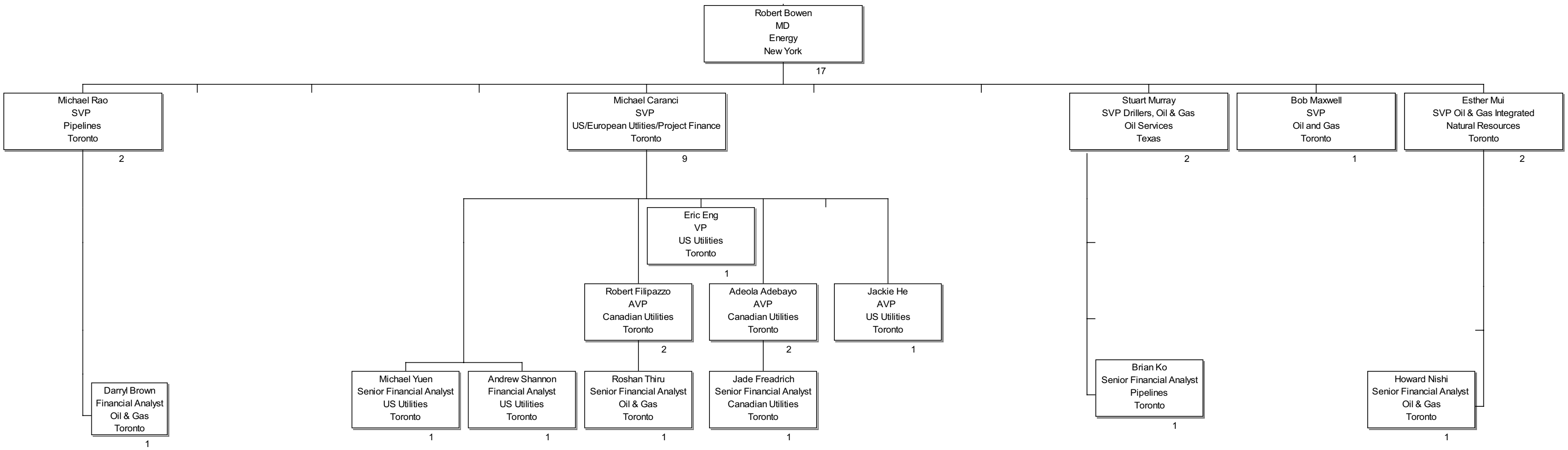
Corporate
Energy



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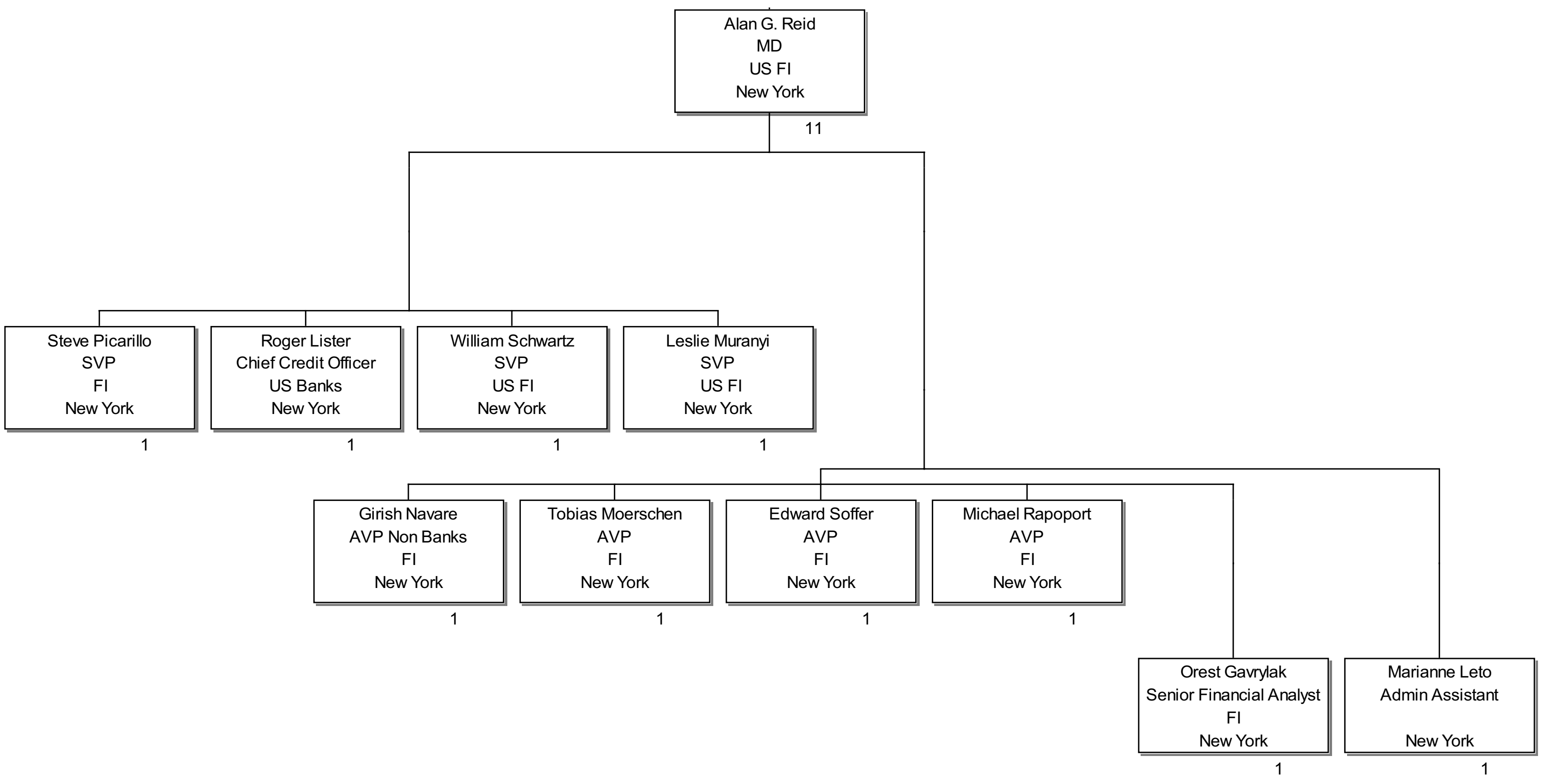
Corporate
US Financial Institutions



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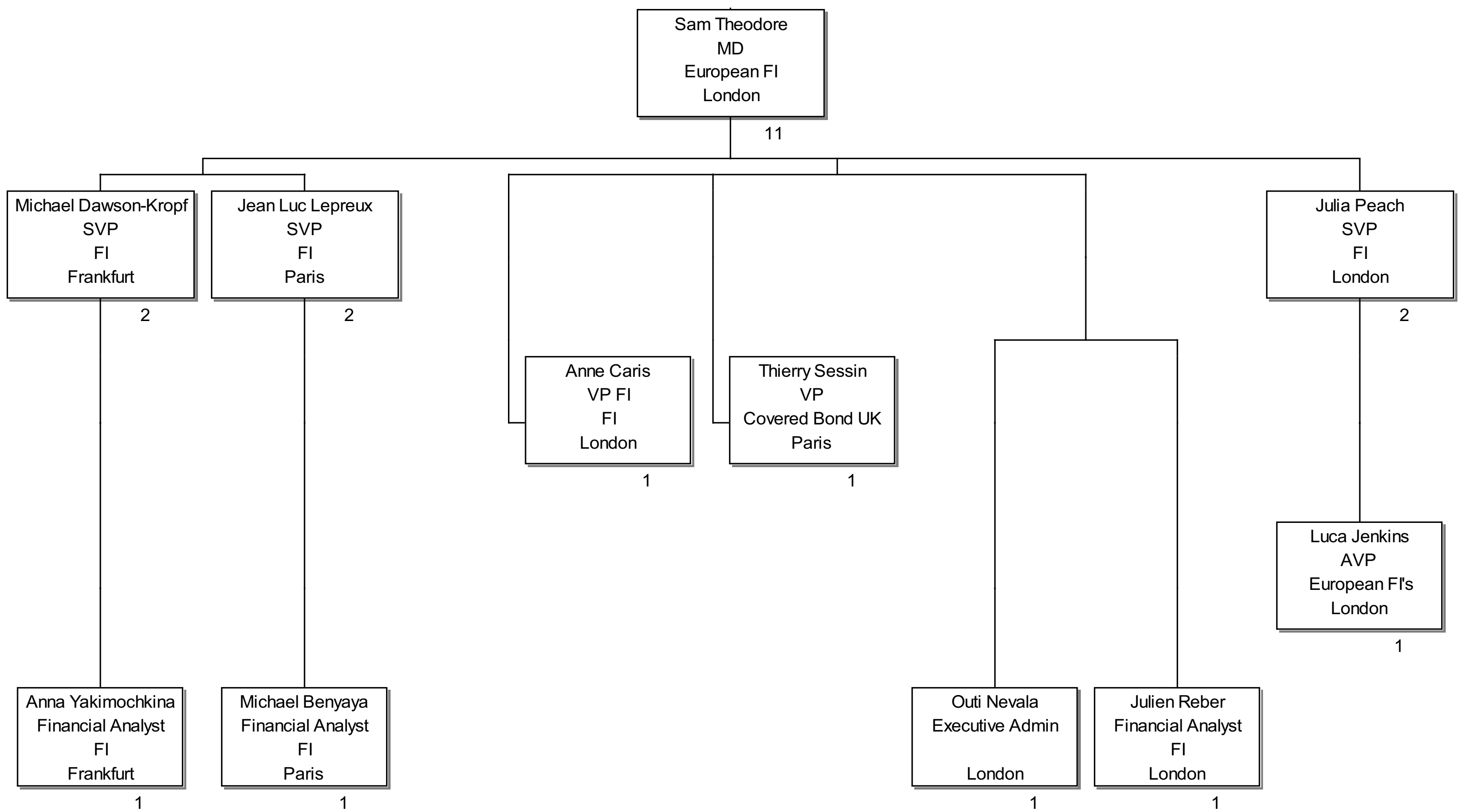
Corporate

European Financial Institutions



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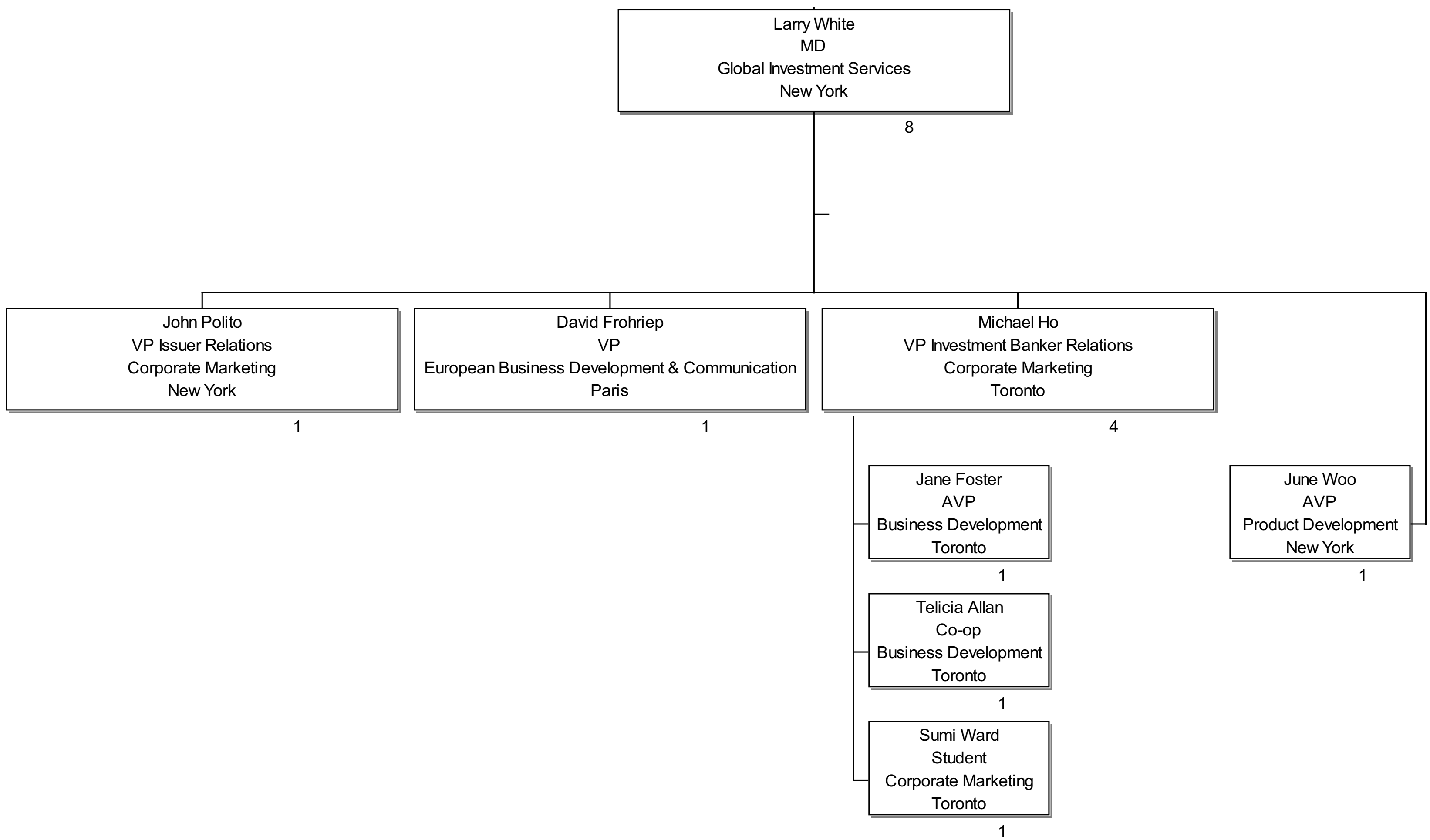
Corporate
Global Investment Services



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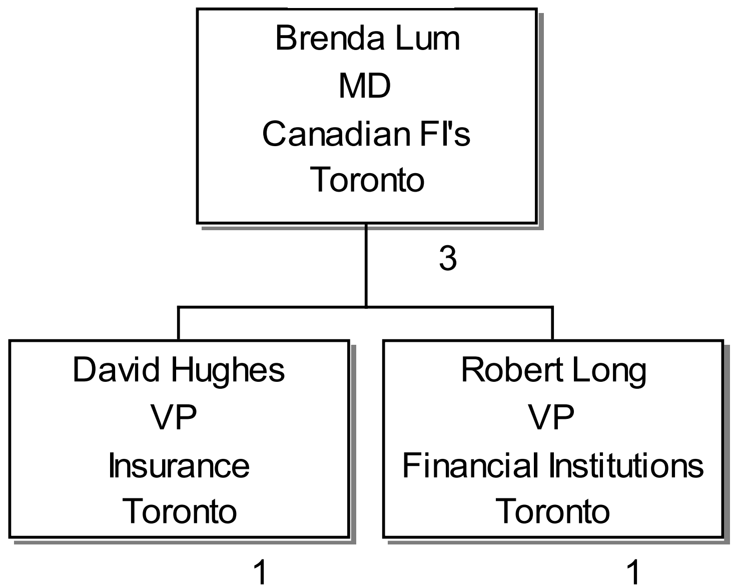
Corporate
Canadian Financial Institutions



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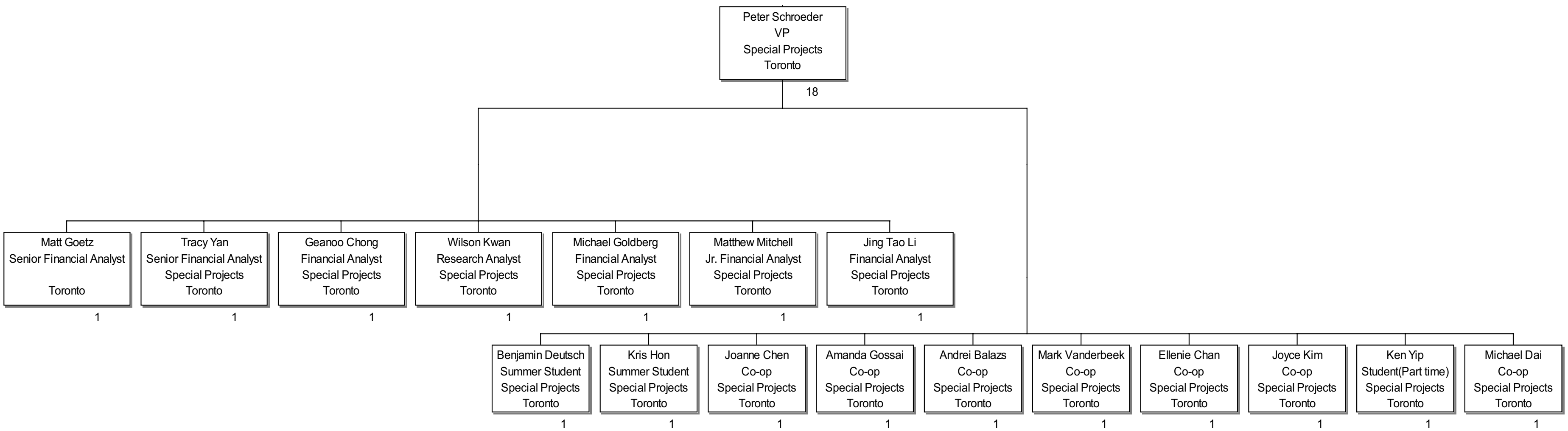
Corporate
Special Projects



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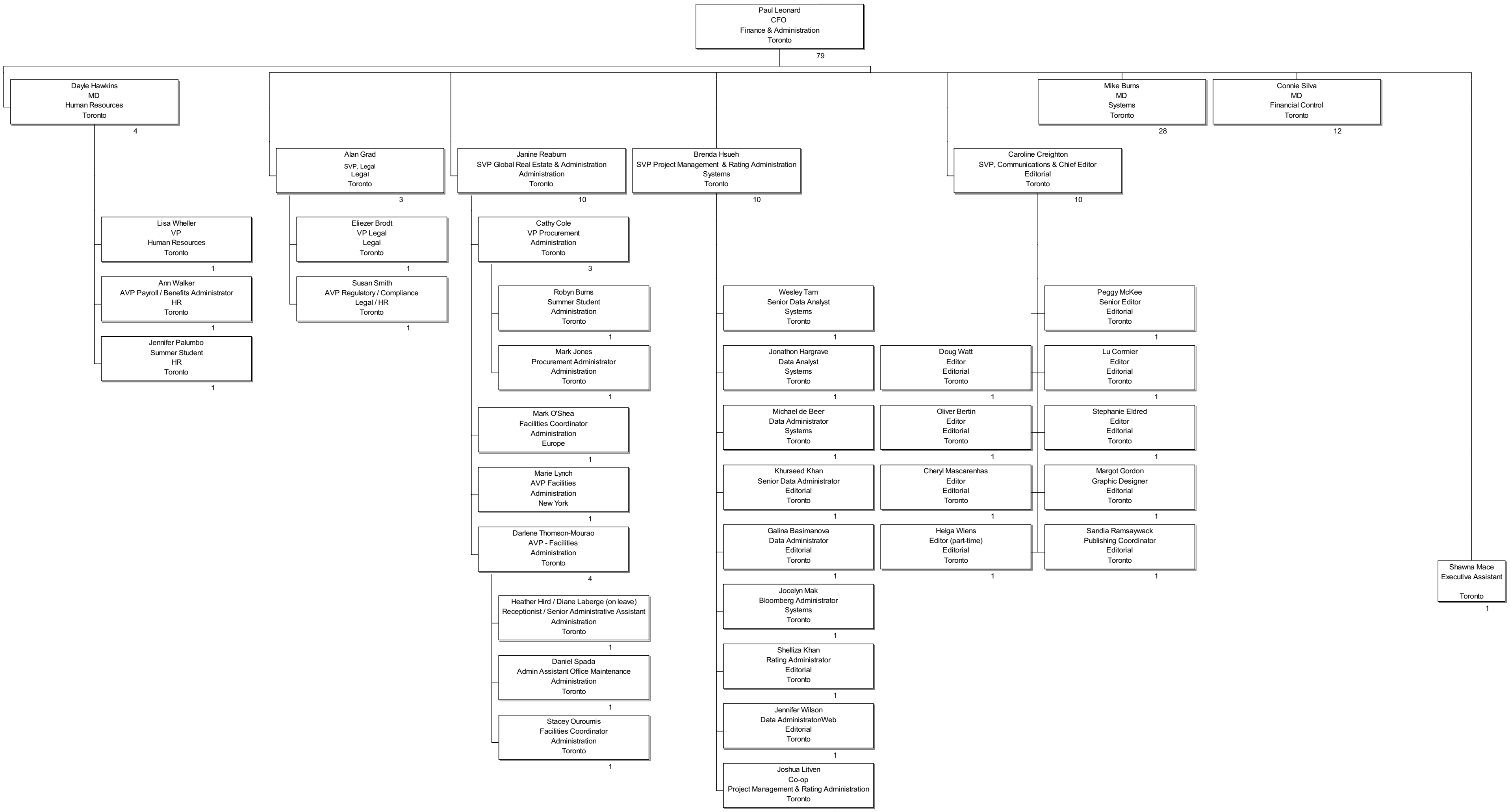
Finance & Administration



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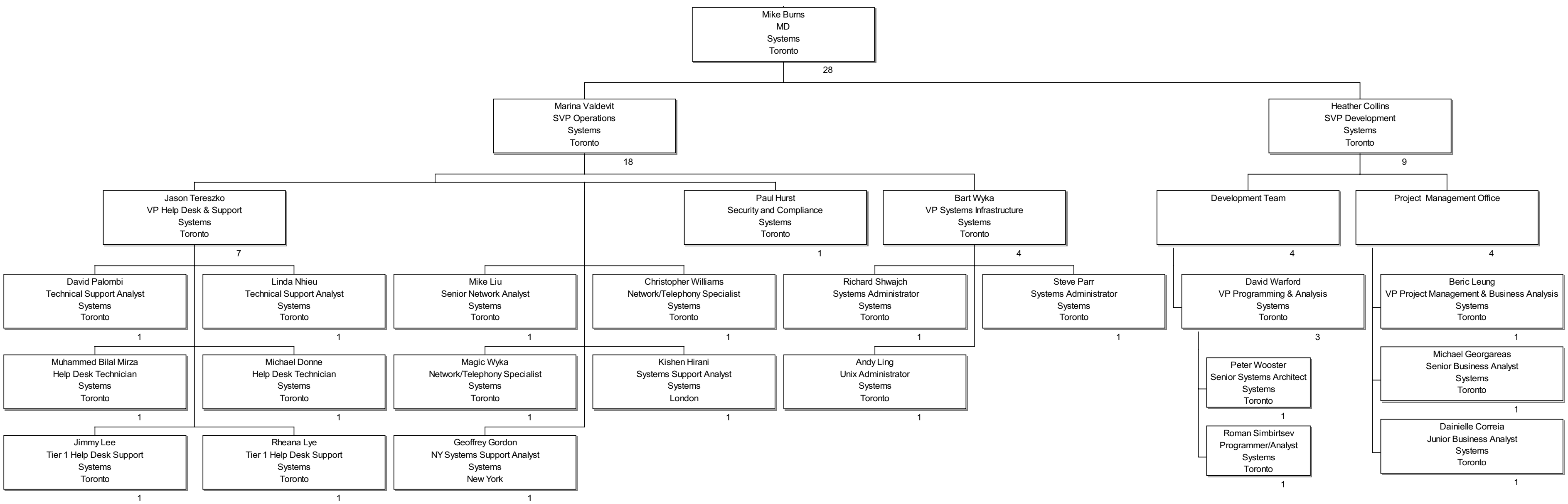
Finance & Administration
Systems



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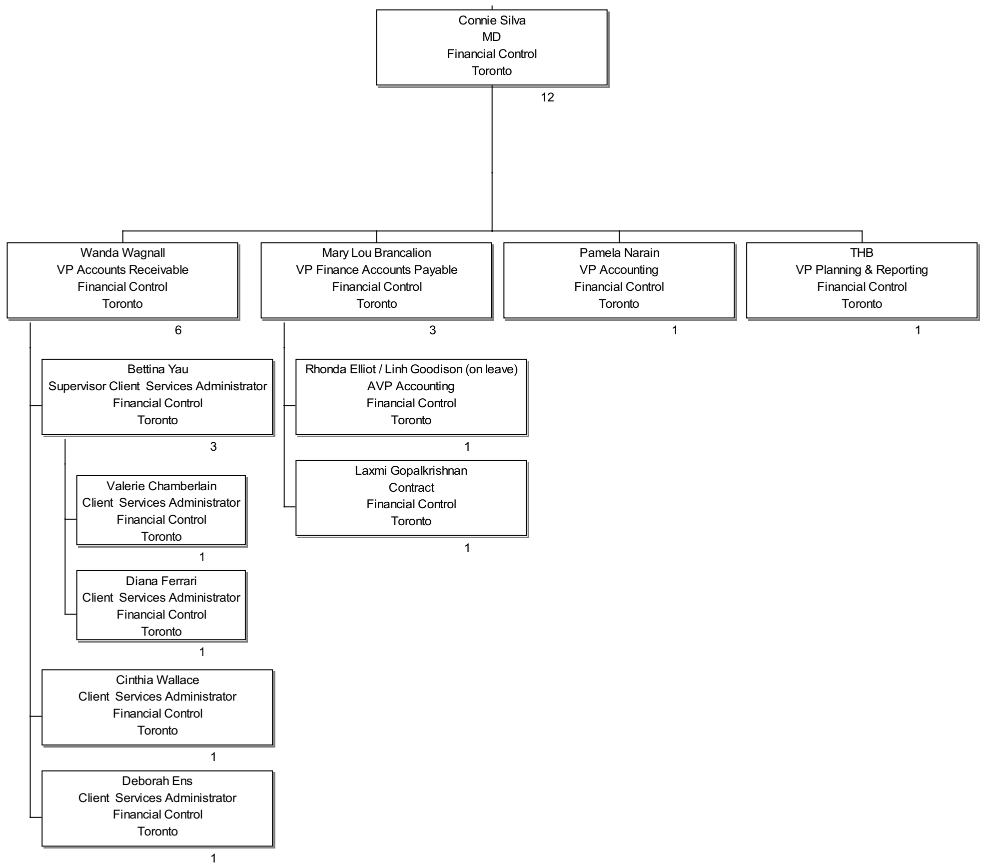
Finance & Administration
Financial Control



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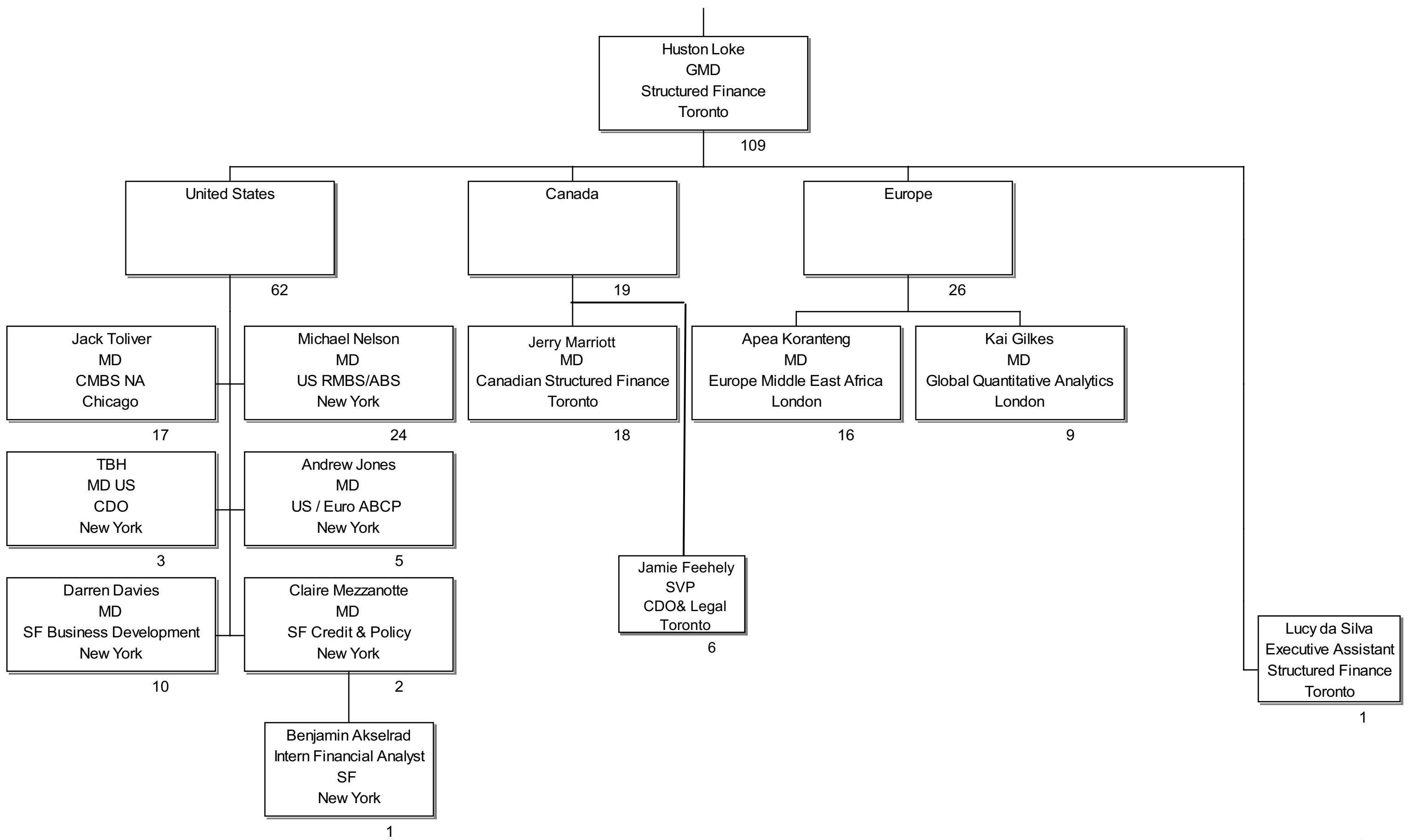
Structured Finance



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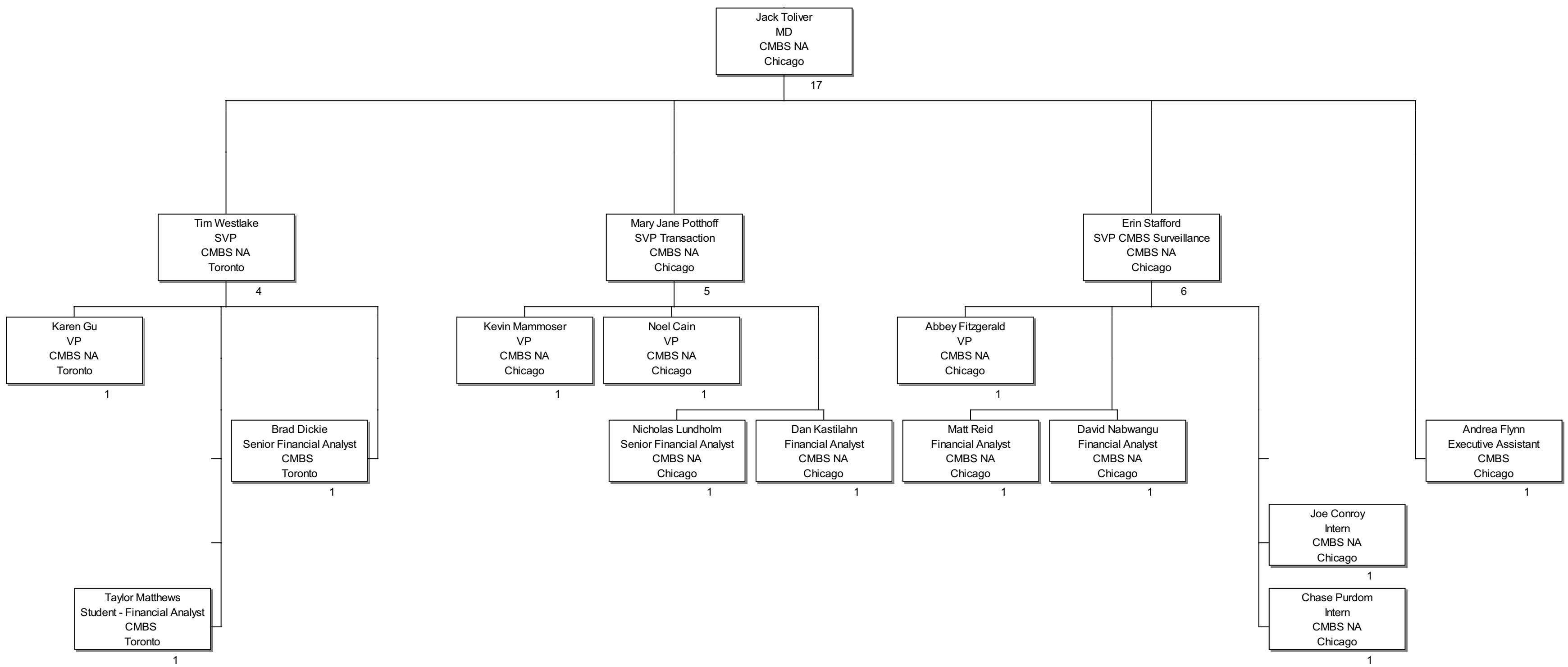
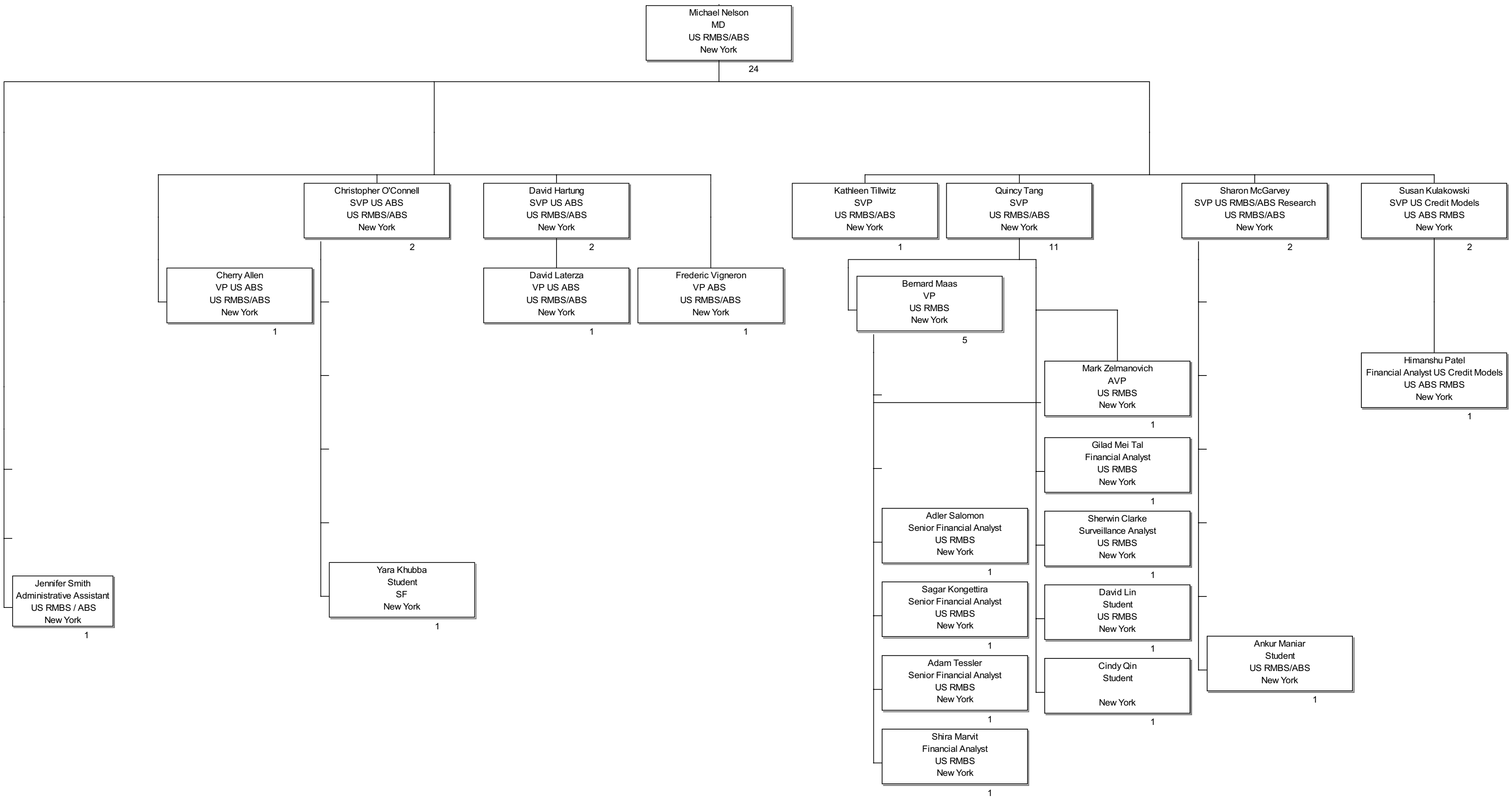
Structured Finance
Commercial Mortgage Backed Securities



Note: Figure below box indicates number of reports including manager themselves

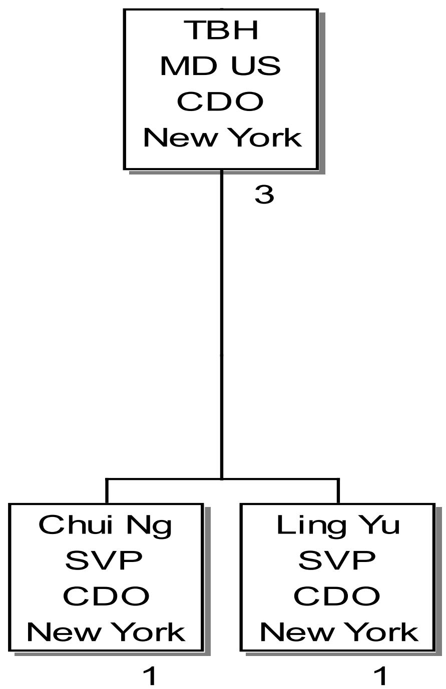
Structured Finance

US Residential Mortgage Backed Securities/Asset Backed Securities



Note: Figure below box indicates number of reports including manager themselves

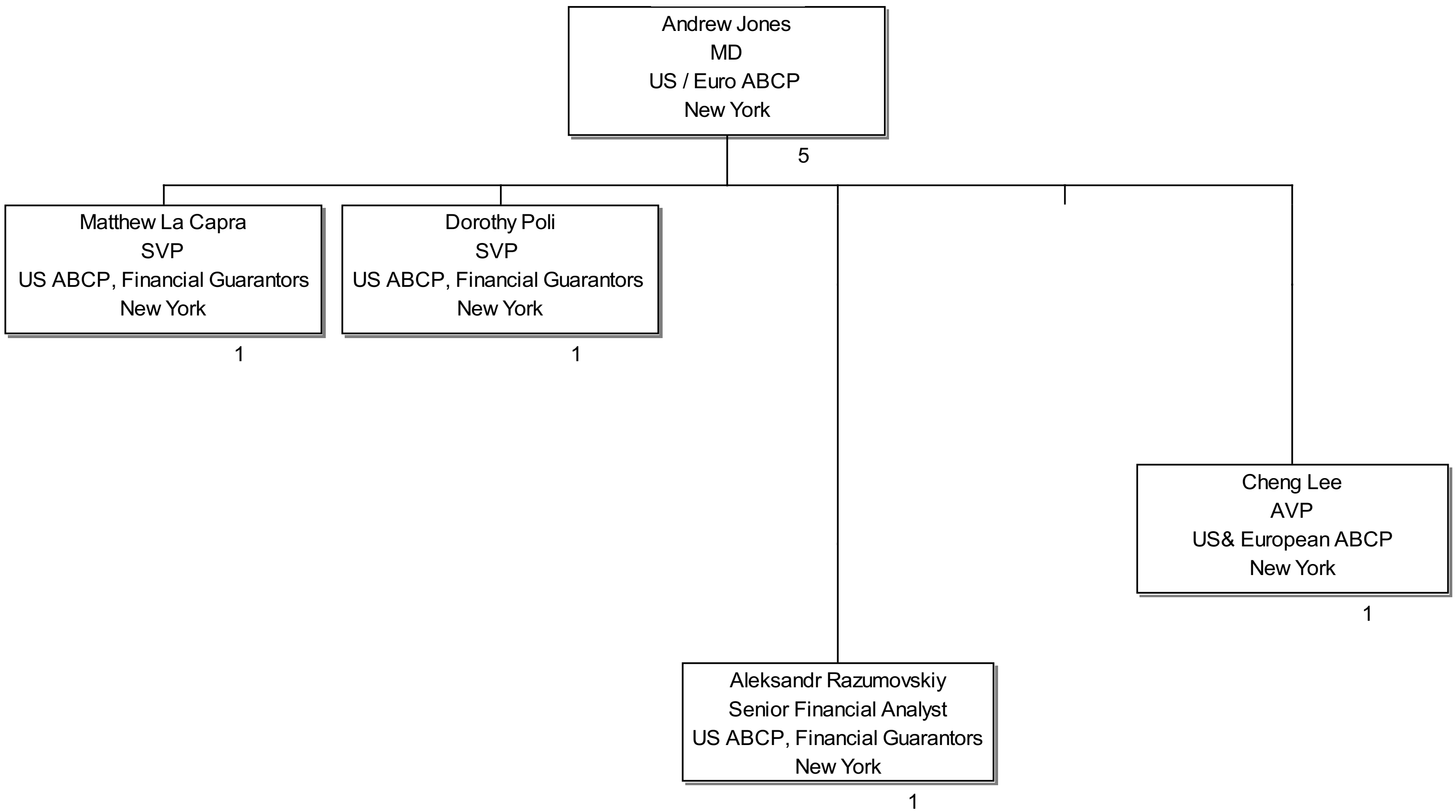
Structured Finance
Collateral Debt Obligations



Note: Figure below box indicates number of reports including manager themselves

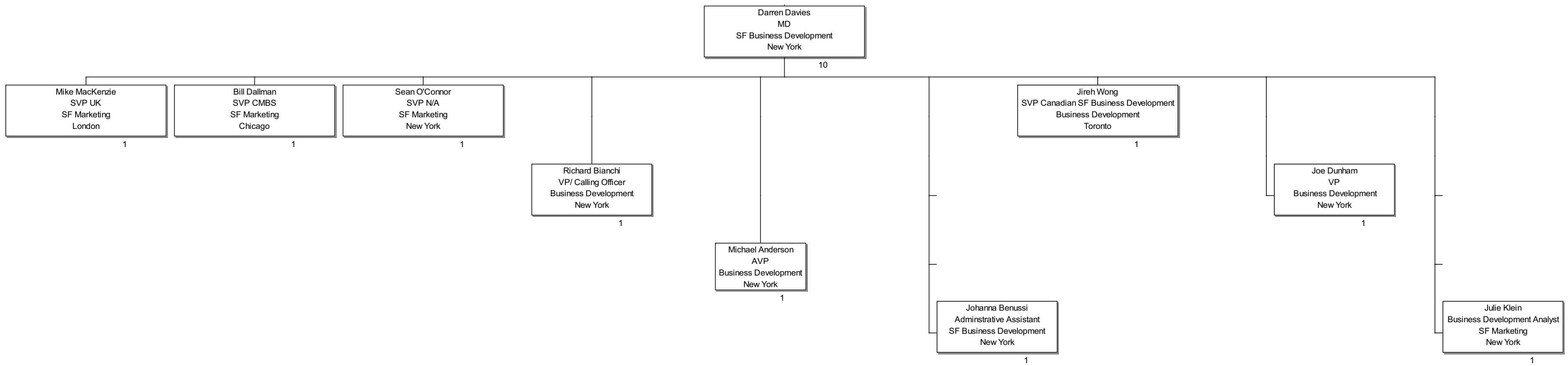
Structured Finance

US/Euro Asset Backed Commercial Paper



Note: Figure below box indicates number of reports including manager themselves

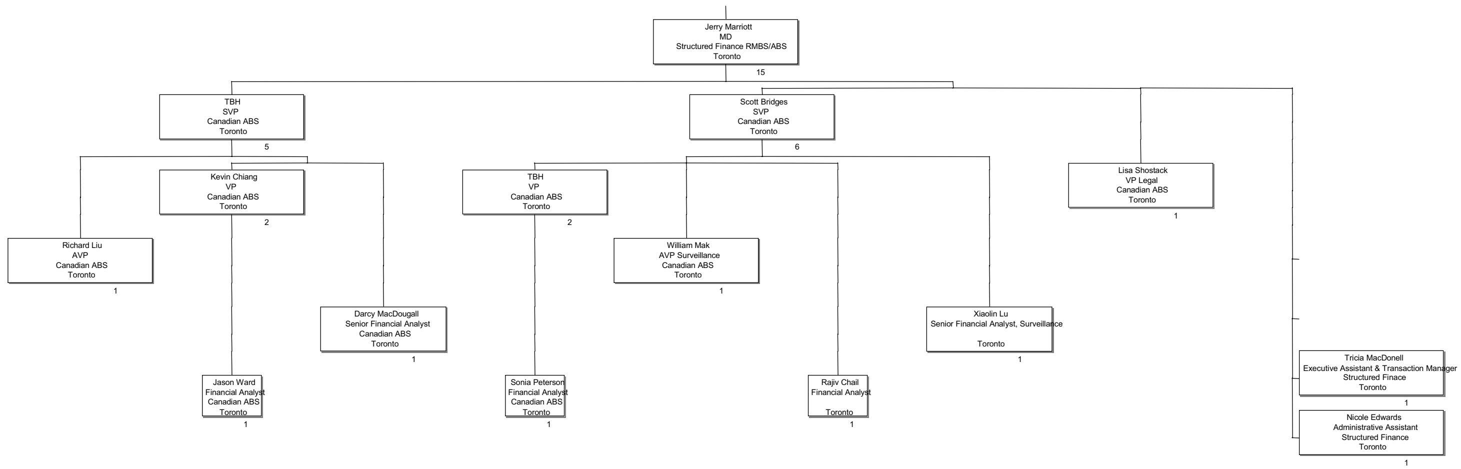
Structured Finance
Marketing



Note: Figure below box indicates number of reports including manager themselves

Structured Finance

Canadian Residential Mortgage Backed Securities/Canadian Asset Backed Securities



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Note: Figure below box indicates number of reports including manager themselves

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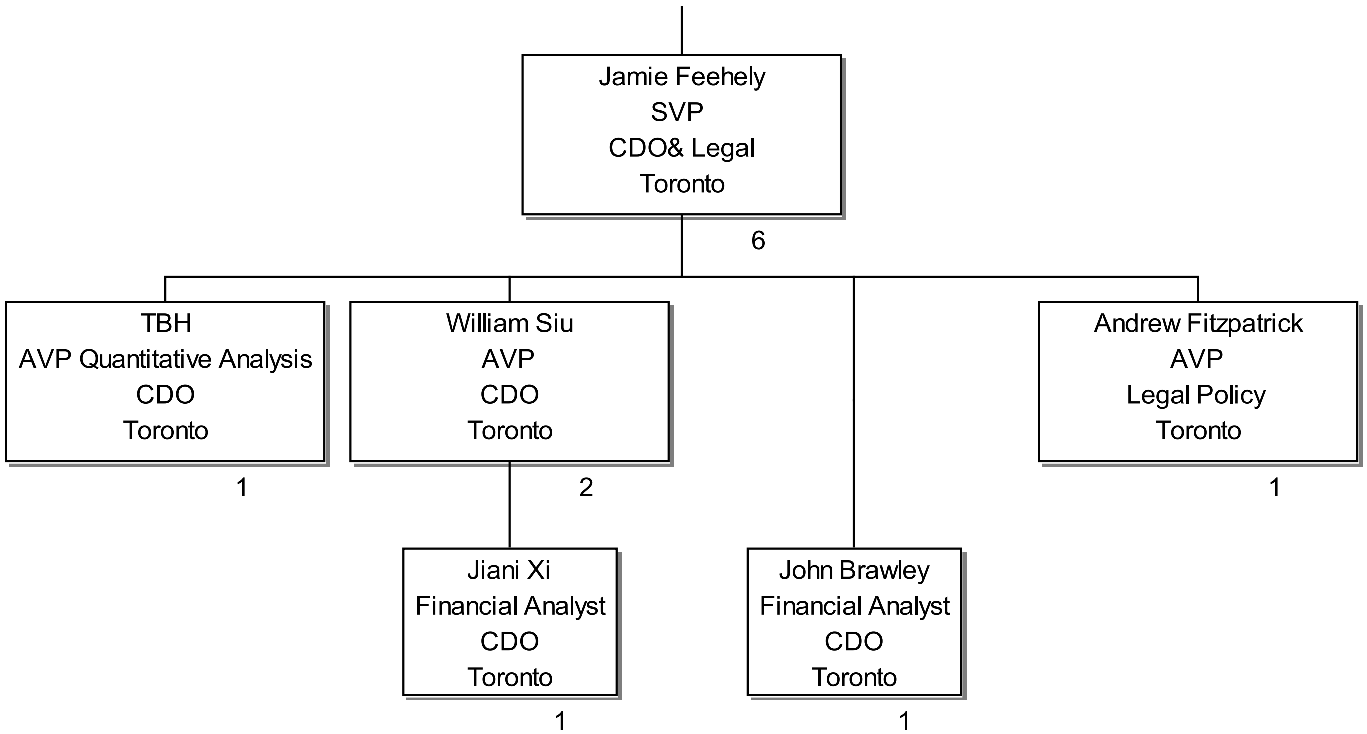
Canadian Collateral Debt Obligations



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Structured Finance
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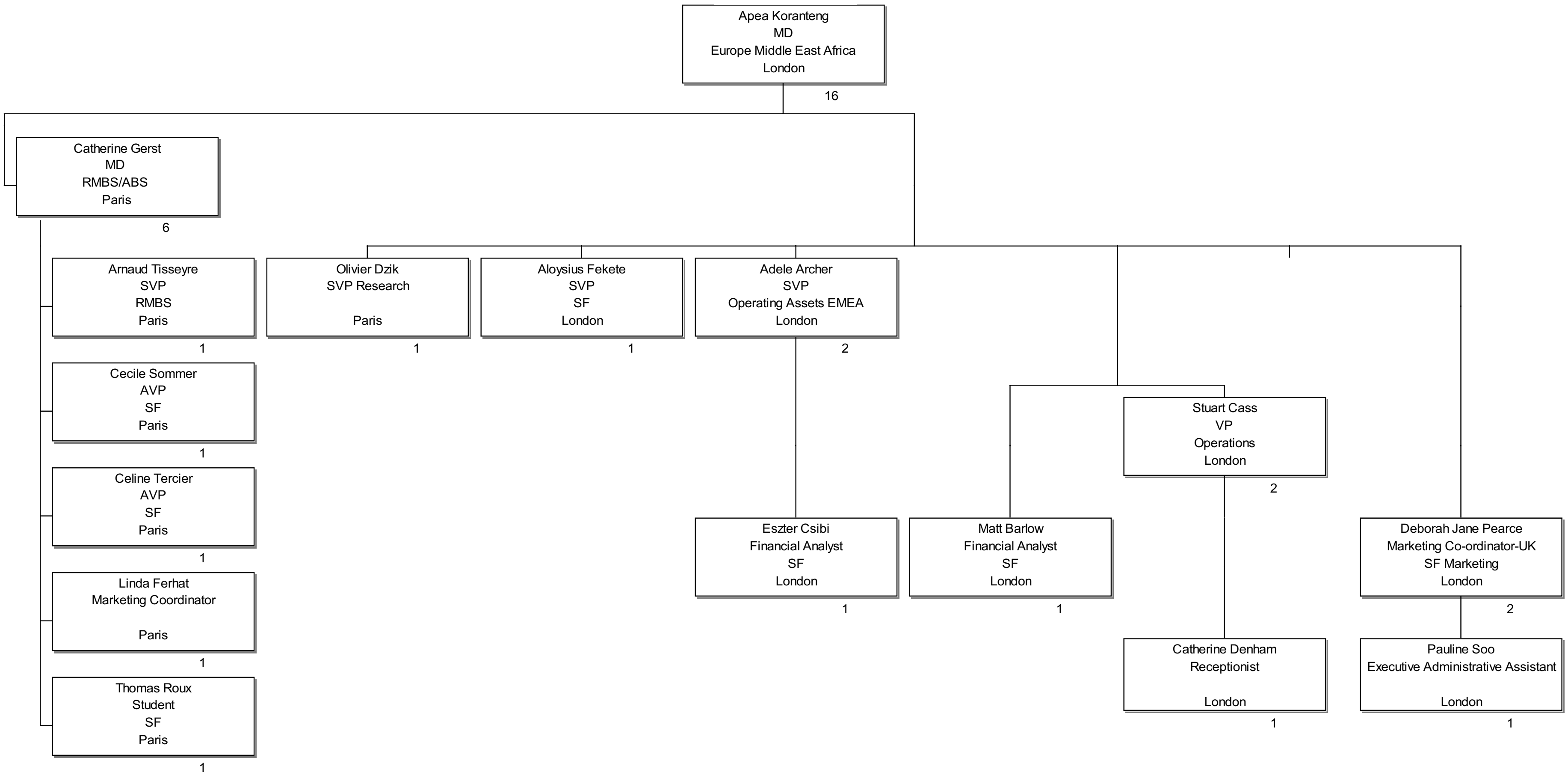
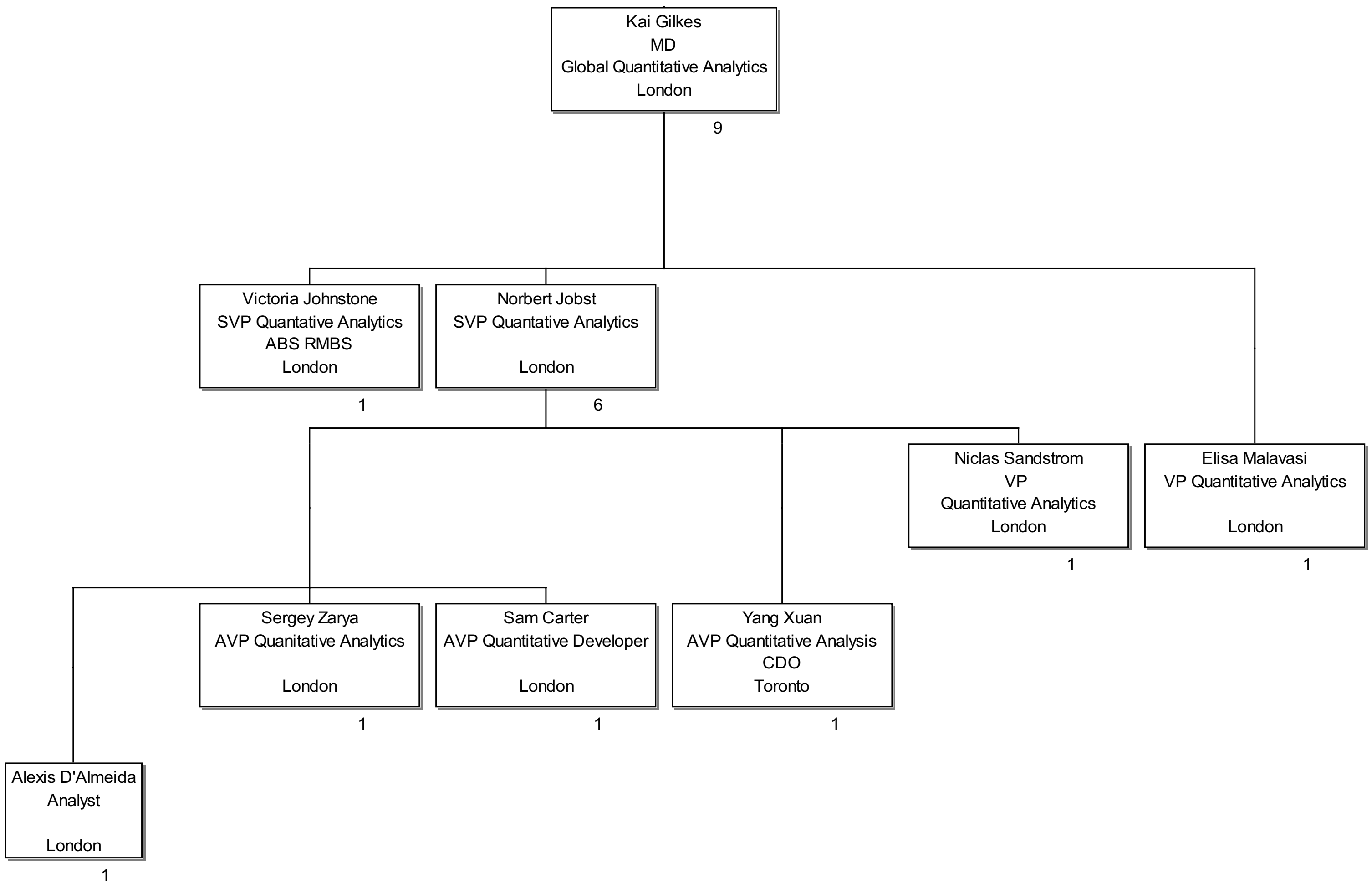


Note: Figure below box indicates number of reports including manager themselves

Structured Finance
Global Quantitative Analytics



Note: Figure below box indicates number of reports including manager themselves

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Information about DBRS Credit Analysts and Persons Who Supervise Credit Analysts

Credit Analysts – Current Total Number = 114

Analyst
A BA degree is generally required for this position, and enrollment in the CFA program is a plus. Individuals have 0 – 3 years experience and must have financial statement analytical abilities, spreadsheet skills and an understanding of basic financial concepts.

Senior Financial Analyst
This position typically requires an undergraduate or MBA degree, with enrollment in the CFA program as a plus. An individual is also required to have 1 – 2 years experience as an analyst, as well as strong research skills, financial statement analytical abilities, spreadsheet skills, a good understanding of basic financial concepts and growing industry knowledge.

Assistant Vice President
This position also typically requires an undergraduate or MBA degree. An individual is required to have 2 –5 years experience as an analyst as well as strong analytical skills, strong research skills, strong financial statement analytical abilities, a solid understanding of basic financial concepts, solid industry knowledge and growing financial markets knowledge, good communication skills and developing relationship management skills.

Vice President
An individual in this position typically has more than 5 years of experience since graduation from an MBA program or has a comparable combination of education and related experience as an analyst. This position requires solid analytical skills, strong writing abilities, good communication skills, solid knowledge of his/her industry and the financial markets and good relationship management skills.

Senior Vice President
An individual in this position typically has a minimum of 7 years of experience since graduation from an MBA program or has an equivalent combination of education and experience as an analyst. Outstanding analytical abilities, strong relationship management skills, excellent writing skills, excellent communication skills and in-depth knowledge of his/her industry and the financial markets.

These Senior Vice Presidents have no direct reports.

Credit Analyst Supervisors – Current Total Number = 30

Senior Vice President
An individual in this position typically has a minimum of 7 years of experience since graduation from an MBA program or has an equivalent combination of education and experience as an analyst. Outstanding analytical abilities, strong relationship management skills, excellent writing skills, excellent communication skills, in-depth knowledge of his/her industry and the financial markets and a strong ability to manage and mentor junior analysts are also required.

These Senior Vice Presidents have direct reports and analyze.

Managing Director
An individual in this position typically has a minimum of 10 years of experience since graduation from an MBA program or has an equivalent combination of education and experience as an analyst. This position also requires extremely strong analytical skills, significant in-depth knowledge of his/her industry and the financial markets, strong management/leadership skills and ability to mentor junior analysts, excellent relationship management abilities and highly developed communication skills. A member of "DBRS Management" is expected to think beyond his/her own sector and assist with the development of DBRS and its strategies on a wider scale.

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December 5, 2007

BY ELECTRONIC MAIL

Ms Ingrid Bonde
Chair
Task Force on Credit Rating Agencies
The Committee of European Securities Regulators (CESR)
11-13, avenue de Friedland
75008 Paris
France

Re: *Response to CESR Questionnaire, dated November 14, 2007*

Dear Ms. Bonde,

Please find attached our response to the questions submitted by CESR in your questionnaire dated November 14, 2007. We have attached a number of exhibits to provide further detail on our answers.

As many of the topics are complex, and we have sought to provide concise answers, we would also be very happy to participate in any further discussion which CESR may wish to organise as the process of preparing CESR's Consultation Draft continues.

Should you otherwise have any further queries, do not hesitate to contact myself on +44 20 7417 4362 or Susan Launi (susan.launi@fitchratings.com) on +44 20 7862 4070.

Sincerely yours,

Richard Hunter
Managing Director
Regional Credit Officer – Europe, Middle East, Africa and Asia
Fitch Ratings

CESR Request for information

Transparency of methodology

1. **Publication of methodologies and assumptions:**
   a. **Is there a section on your website devoted to the publication of your methodologies?**
   Our website contains a prominent "Criteria Report" section on the homepage of each major asset class. Criteria reports which apply to more than one asset class are listed under the "Criteria Report" section of each asset class covered.

   b. **Do you provide explanations of the methodologies applied to the different categories of ratings for each asset class (e.g. RMBS, CDO, etc) separately by region?**
   We provide separate regional criteria or regional addenda, where regional variations exist in the analysis (e.g. RMBS). Where limited or no regional variations are applied, global criteria are published (e.g. CDOs).

   c. **Do you provide the full method applied to each category of rating for each asset class (e.g. RMBS, CDO, etc.) separately by region?**
   See b. above.

   d. **Is all of the above information freely accessible or is part of it only available for subscribers?**
   All of Fitch's published criteria reports are available from Fitch's free-access web-site at www.fitchratings.com.

2. **Publication of changes in methodologies and assumptions: Are all changes/adjustments to your methodologies and assumptions published and, if yes, where exactly are they published?**

Major revisions are typically incorporated within updated criteria reports, as opposed to a separate catalogue of changes. All published criteria, including revisions, are made available to the public as discussed under question 1 above.

   a. **Is there a special section on your website where changes made to criteria can be reviewed over time?**
   The "criteria report" sections of the website noted under question 1 contain all published criteria relevant to outstanding ratings. No separate track record of individual criteria changes is maintained.

   b. **Do you publish reports that discuss the changes made to criteria?**
   Updated criteria reports typically discuss which, if any, changes have been made. Where changes are material, the criteria may demonstrate the impact with illustrative examples. We are currently investigating mechanisms by which the nature and impact of changes can be more readily identified.

   c. **Do you have press conferences to announce and explain those changes?**
   Where we believe the changes are material and that there is investor demand for more information, then a teleconference (or, in rarer cases, a series of live seminars) may be held. These are open to subscribers and non-subscribers alike and are advertised in advance via a press release.

3. **Do you provide links/references to those publications mentioned in question 2 in the respective rating change reports (i.e. the announcement of a change would let the reader know where to find the related methodology)?**

Where revision of criteria has led directly to material rating action, the relevant criteria report will typically be referenced in the text of the rating action commentary announcing the rating action. Criteria reports are, as noted under question 1, available to subscribers and non-subscribers alike from dedicated sections of our web-site, 24 hours a day. Major changes to criteria will be announced via a press release, and, as noted under question 2c above, may be accompanied by public teleconferences.

4. **If changes have been made to your methodology for a particular product type (say US sub-prime RMBS) but previous issues have not been reviewed against this methodology how do you ensure this is clear to the marketplace? If the previous issues were being reviewed how would this be made public?**

As noted in the answer to question 29a below, criteria changes may not result in the re-rating of all of the transactions that are subject to those criteria. Where the change in methodology does not result in materially different rating outcomes, and where individual transactions are performing in line with expectations, there will be no re-rating. Where the change in rating outcome is likely to be material upon application of new criteria, and/or where a transaction's performance varies notably, positively or negatively, from expectations, the transaction will be reviewed against the new criteria. Fitch has recently begun publishing a series of surveillance criteria reports detailing the exact triggers for rating actions on monitored ratings (e.g. "Downgrade Criteria for Recent Vintage U.S. Subprime RMBS", August 8, 2007, Exhibit P1 enclosed).

There are different mechanisms for signalling that ratings in a given sector are under review, typically either through "Rating Watch" designations or research commentary. Where specific issuers, transactions or tranches can be identified as potentially affected by a review, a "Rating Watch" designation may be applied. Alternatively, a large number of issuers or transactions could face a challenge which may result in rating actions, but where individual transactions cannot yet be identified as affected. In such cases, Fitch may issue a general commentary outlining the issues as they are currently perceived and the steps Fitch is taking to review such issues, with a view to establishing "Rating Watch" or other appropriate designations as expeditiously as possible.

We are currently also trialling usage of "Under Analysis" and "Rating Outlook" designations to enhance these signals. For example, in a number of structured finance sectors, where performance data indicates that a review of the rating may be appropriate, the "Under Analysis" designation may be applied almost immediately after receipt of the performance data by Fitch. In other sectors, indications drawn from performance data or other developments may be communicated using a "Rating Outlook". Details of these designations are enclosed in Exhibits P2 and P3.

5. **Is publishing the methods you use enough to meet the requirements of the IOSCO Code and ensure sufficient transparency or do you see further possibilities for improving transparency/the understanding of**
    a. **your ratings?**
    b. **your rating process?**

We believe our dissemination policy, both in the quantity and quality of documents published, and the free access of the public to these documents, meets the requirements of our own Code of Conduct ("Fitch's Code") and is consistent with the IOSCO Code of Conduct Fundamentals ("IOSCO Fundamentals"). As an increasing range of constituencies employ ratings, we continually review our dissemination policies and publications to ensure that the maximum amount of transparency is afforded. To that end, in the recent past we have published documents outlining “The Rating Process”, and “What Ratings Mean” (enclosed as Exhibits P4 and P5).

6. **What steps does your firm take, if any, to contribute to enhancing the financial education of investors or potential investors?**

As a provider of public opinions to the general financial marketplace, Fitch does not currently seek to limit the dissemination of its published ratings to a particular category of qualified investors. We do, however, share the policymaking community’s concerns that users of ratings should properly understand what ratings mean so that they may be used appropriately within the investment decision-making process.

Beyond the detailed and publicly-available criteria documents noted above, Fitch makes all of its ratings (and rating definitions) available, free of charge, via its websites. Fitch holds teleconferences on rating topics, which are free to the general public and advertised on public wire services. We hold workshops and seminars, which are generally provided at no charge to investors and other financial markets participants. Fitch also makes its analysts available to subscribers and non-subscribers alike, via telephone, e-mail or one-on-one visits to institutions; all rating action commentaries provide names and phone numbers of the relevant analysts to facilitate access to the analysts. Fitch publishes special reports on items of topical interest to the credit markets, many of which are available to non-subscribers.

7. **Do you take steps to clarify any limitations to your ratings, including what they are intended to cover, or the methodologies and the assumptions underpinning them? How do you do this?**

The broad limitations related to our ratings – their nature as opinions on credit risk, and not investment recommendations – are contained within our standard disclaimer, attached to all credit analysis reports and major publications, and replicated on our web-site. The definitions of the various rating scales are publicly available from our web-sites and publications, as well as from the common third-party market data vendors (e.g. Bloomberg).

We have also recently published a more detailed examination of what ratings do (and do not) address, titled “What Ratings Mean.” (Exhibit P5). We are currently examining mechanisms by which limitations to the analysis in the context of individual criteria may be more prominently highlighted.

8. **Do you publish, and if so, where, your approach to the use of confidential information in rating of structured finance (SF) operations? Does it differ from that which you follow in “traditional” corporate rating?**

All Fitch employees are subject to our Code of Conduct and related policies, including (without limitation) Fitch's Worldwide Confidentiality, Conflicts of Interest and Securities Trading Policy ("Compliance Policy"). Both the Code and the Compliance Policy are available on our free public website, www.fitchratings.com, under the "Code of Conduct" button at the bottom of the home page. We do not have a separate approach with respect to the use of confidential information in rating structured finance operations.

9. **Do you consult with industry as to what disclosure levels they would like to see for methodology and model assumptions?**

Fitch meets regularly with arrangers, issuers and investors to solicit feedback on our work product. We have not conducted a formal consultation on methodology disclosure levels generally, but market participants will typically take advantage of consultations on individual models and methodologies to provide feedback on areas which may be unclear.

Human Resources

10. **Please provide us with the following information with regard to SF ratings and traditional ratings:**
    a. **Exhibit 4, 8 and 13 of your NRSRO application form.**
    Exhibits 4 and 8 are attached as Exhibits P6 and P7. As you know, Exhibit 13 of the NRSRO application form is treated by the SEC as confidential. This Exhibit can be provided to CESR subject to its treatment as confidential.

    b. **The internal definition of the existing classes/levels of employees in the CRA's rating business: e.g. junior/mid/senior analysts, supervisors, committee analysts, lead analysts, etc?** [1]
    We have attached, as per question 10a above, the NRSRO Exhibit 4 description of staff roles as our Exhibit P7. For the purposes of CESR's analysis, we denote Senior Directors and above as supervisors. Senior Director is the minimum level of seniority required to ensure a quorum for a rating committee.

    c. **Historical data for exhibit 8 (information on number of analysts/supervisors) covering the 1997-2006 period split by:**

       I. **the staff levels identified in point (b) above.**

       II. **Worldwide, EU and US based.**

    Please find below the relevant data.

	Supervisors (SD & above)		*Other Analysts (D & below)*	
	US	*Non-US**	*US*	*Non-US**
1.1.2003	136	48	260	169
1.1.2004	149	58	269	207
1.1.2005	163	78	287	235
1.1.2006	179	98	316	274
1.1.2007	192	116	355	357

* excludes Latin America

    d. **What are the minimal educational and professional requirements for the different levels of employees (as defined in b) within the analytical staff, and have these requirements varied over the past 10 years? If they varied, how did they vary?**
    Typically we require that analytical staff have a bachelor's degree or equivalent. The employee base also contains analysts with postgraduate degrees, CFA charterholders, and holders of professional legal or accounting qualifications. These requirements have not varied over the past 10 years.

[1] This question is designed to enable the CRA to answer the other questions based on its **own** human resources structuring method as different CRAs may have different human resources structures or seniority definitions (junior/senior, analyst/supervisor…).

e. **The typical minimum number of years of experience according to levels of employees as defined in (b). Has this number evolved over the past 10 years? If so, how?**

While we promote on ability rather than based on minima of years of service, as a very rough guideline, the below table indicates the typical number of years' experience of credit analysis that employees at the following levels would be expected to have:

Title	*Typical Credit Analysis Experience*
Analyst	0-3 years
Associate Director	3-5 years
Director	5-8 years
Senior Director	8-12 years
Managing Director	12+ years

11. **Please provide us with figures on the annual turnover of employees over the period 1997-2006, split per level (as defined in (1.b)), covering I) SF ratings and II) traditional ratings.**

This data is attached for CESR's reference as Exhibit NP1.

12. **What are the risks presented by staff turnover to your ability to function effectively as a provider of accurate ratings and what steps do you take to mitigate these risks? Are these successful?**

Turnover, which averages just below 20% for the analytical groups as a whole over time, is an unfortunate aspect of the business of rating agencies that we have had to manage. The analysts at Fitch gain skills that are very valuable to investment banks, hedge funds, and asset managers, most of which are able to pay higher compensation than we do, as well as offer different perspectives on the capital markets.

The cost of turnover is that we have to replace our leavers, so the time spent recruiting, agency costs, and the potential in the recent competitive markets to have to pay higher salaries to replace people of a similar grade, are all components of the cost. Once replacement staff join, time is often spent training them before they are full contributors. At the same time, turnover, particularly at more senior levels, does bring in valuable new knowledge and skills from the marketplace.

We aim to minimize turnover essentially by making Fitch a good place to work. We attempt to offer a work/life balance where the time spent working late hours or weekends, and on last-minute travel, is generally quite reasonable. We also offer a relatively high degree of job security compared to investment banks. We offer a significant and increasing amount of training and development for our employees, and aim to move them into opportunities of increased scope or responsibility to further their career growth. We have various recognition programs for Excellent Credit achievements and Service Awards, as well as many other programs ranging from sports team sponsorships to charity committees to team building events, all with the aim of making Fitch a hospitable and productive work environment.

We are conscious that in an environment where more junior staff will naturally have a reasonably high turnover rate, it is important to consider retention of more senior staff as well. As such, we have an active program of identifying and fostering management talent within the company, including supervisor rotations through asset class and geography. We have an employee stock program which vests after three years of service. These measures, combined with the working environment and unique challenges/market access enjoyed by rating agency personnel, mean that our turnover at the supervisor level is, in general, significantly lower than for the population at large. It is also not uncommon for employees who have left Fitch to come back to work for us again later, and we encourage that through a modest alumni program.

13. Has it become harder to fill vacancies in structured finance ratings teams over the last 5 years? If yes, what has been done to ensure you continue to have sufficient resource and to ensure this does not affect the quality of your ratings?

Hiring conditions have in fact generally become somewhat easier relative to the position several years ago. As the structured finance market has grown and matured, with more institutions participating, and a greater general awareness of the technology of structured finance amongst the fixed income community, the available pool of qualified and experienced talent has also grown.

14. Typically, what is the composition of a monitoring/rating team in terms the job profiles and job levels and does this differ from teams that monitor/rate corporate bonds?

In contrast to corporate finance ratings, the lead analyst in charge of monitoring a structured finance transaction will not be the initial transaction analyst. However, committees to review transactions under surveillance will generally contain both transaction and surveillance team members. As noted in our answer to question 24 below, with the exception of the use of "screeners", the same quorum requirements generally apply to both transaction and surveillance committees.

15. Please provide us with information on the average number of deals and average number of transactions under surveillance per lead analyst by type of SF products in the following table format:

Type of product	*Approximate average number of deals per lead analyst in 2006 (primary rating) **	*Approximate average number of transactions under surveillance per lead analyst in 2006*
RMBS	9-10	100
CMBS	4-5	40
CDO	3-4	40
ABS	5-6	40

* both deals that resulted in a final rating and deals that did not result in a final rating

These numbers reflect the fact that there are very many structural and other qualitative factors required to be assessed at the initial transaction rating stage which do not typically require repeat analysis during the life of the transaction. Also, given the timeframe for our response, we have not been able to include deals that did not result in a final rating, which depresses the average deal numbers for transaction analysts, compared to surveillance analysts.

Further to your question at our meeting in Stockholm, we are also attaching the overall average numbers of structured finance transactions rated or monitored per analyst in the last five years, as an indicator of the degree to which resources are keeping pace with the growth in ratings.

Outstanding structured finance transactions per structured finance analyst as at:	
1.1.2003	23.6
1.1.2004	22.3
1.1.2005	20.1
1.1.2006	19.3
1.1.2007	18.1

16. What are the total annual wage costs in structured finance rating over the period 1997-2006?

This data is commercially sensitive, and can be provided to CESR subject to its treatment as confidential.

17. Do you outsource part of the rating/surveillance process (e.g. data gathering, processing, modelling, etc.)? If yes:

a. Please describe in which part(s) of the rating/surveillance process you make use of outsourcing and to what extent.

Limited use of outsourcing is made within structured finance in the areas described below. In each case, the outsourcing relates to data collation or data processing and not core analytical responsibilities.

Surveillance – Indirect Sourcing of Data: In the US, Fitch uses a third-party data vendor, Intex, as the source of much of its surveillance data for monitoring structured finance transactions. Intex is the market leader in this field, and the primary data source for most major market participants in the US.

Data is received by Intex from trustee and servicer reports. This data is then put into a standardized format by Intex and forwarded to their clients, including Fitch. On receipt of the data from Intex, Fitch runs automated tests to identify missing fields or fields with results that deviate from a reasonable pattern. Fitch analysts then replace/review the missing/deviating fields. At the same time (i.e. just after each monthly data-run), Intex will itself typically be receiving error reports from other market participants, and will forward those results to data recipients, including Fitch. This data scrubbing process usually takes 2 days, and generally involves review of a very small number of data points (less than 0.5% of the fields used). Error rates from a dedicated data transcription service of this nature are, in our experience, unlikely to be higher than would be the case were Fitch employees to take issuer/servicer data, and manually enter this into our surveillance databases.

Outside the US, no vendor currently offers comparable provision of raw surveillance data. Consequently Fitch does not have any similar arrangements outside the US, although Fitch continually reviews the product offering of different vendors.

Surveillance – Processing of Directly-Sourced Data: For a small number of asset groups both in the US and outside the US (e.g. US Student Loans, UK CDOs), surveillance data received by Fitch from trustees/issuers is passed to a reputable outsourcing company, which enters the data into Excel spreadsheets containing Fitch templates, and returns the data to Fitch in a homogenised format. Once the data is received in this format, similar validation checks to those described above are run.

Sourcing of annual financial statements: A limited number of annual reports of rated corporate entities are sourced from a reputable outsourcing company. Data from these reports is then entered by Fitch employees into Fitch's internal financial databases.

Formatting of research reports: Fitch supplements its desktop publishing resources with formatting staff from a reputable third-party outsourcing company to format research publications.

b. What are the risks implied by such outsourcing and how do you tackle these?

Principal Risks	*Principal Mitigants Employed*
Transfer of confidential data	Fitch only works with reputable third-party outsourcing companies, with which it has concluded appropriate confidentiality agreements.
Data processing inaccuracies	Fitch employs validation checks as noted above under question 17a.
Supplier failure	Fitch continually reviews the marketplace for alternative/substitute data suppliers. In the event of a primary vendor failure, the vast majority of data could be sourced directly from trustee reports or similar transaction sources, although there would be a delay while additional resources were redirected to manual entry of the data.

c. Do you consider the (economic) gains of such outsourcing to exceed the risks?
Clearly, we are conscious of the economic cost of poor data management, which could include inefficient operation and loss of reputation. Fitch currently believes that the mechanisms in place are appropriate to manage these risks in a cost-effective manner.

<u>Monitoring of transactions</u>

18. What drives the frequency of rating review for structured finance? Why is this frequency appropriate? Please outline the process that would lead to a rating being taken to review committee?

We review performance data as we receive it. If data shows a breach of a performance trigger, a process is started that may end with a committee, depending on the severity of the breach. If performance data do not indicate any material variation from expectations during the year, each transaction will nonetheless be subject to a formal review targeted to take place on an annual basis.

19. Would regular reviews and announcements on the appropriateness of structured finance ratings - possibly based on some contractual deadlines (i.e. on a regular (quarterly/semi-annual basis) - help in preventing mass downgrades, improve the appropriateness of existing ratings? If not, why?

Ratings are subject to continuous review, other than where expressly disclosed as point-in-time in nature. This means that any material event can cause a rating action for any rating at any time. In practice, continuous review results in regular, periodic formal reviews which are publicly disseminated (in the majority of cases) in affirmations, or (in the minority of cases) in rating changes.

That said, the periodicity of information availability inevitably leads to ‘bunching’ of actions. Rating actions driven by financial considerations are thus more likely to be taken in proximity to financial reporting periods (quarter- or year-ends for corporate entities, quarterly or monthly reporting dates for structured transactions). Equally, as discussed in question 29c below, where criteria are being revisited, or a major, sector-wide credit event occurs, it will often make sense to announce a series of rating actions simultaneously to better clarify the exact impact of the criteria revision or credit event. In such cases, our aim is always to arrive at an appropriate rating as swiftly as possible, rather than to target external dates such as financial quarter-ends.

The current situation is one that therefore largely arises from the information with which Fitch is working, and the operational constraints of our business, rather than from a series of policy or commercial decisions. It is not obvious to us that a further ‘bunching’ of rating actions to meet pre-determined dates would be either practicable or desirable.

20. What changes have you made in terms of the surveillance of ratings since the widespread RMBS and CDO downgrades earlier this year?

We had already increased the flexibility of resource allocation between transaction and surveillance teams at the start of this year, with, for example, senior staff transferring into the surveillance area from the transaction team in our US RMBS group. As part of our current internal assessment of our structured finance ratings approach, we are currently reviewing what additional or alternative measures may be appropriate to enhance our active surveillance of ratings.

21. How is the appropriate portfolio size determined for structured finance monitoring analysts? Are there any internal procedures which dictate how many transactions a monitoring analyst should be responsible for?

The portfolio size is typically determined with reference to transaction complexity amongst other factors. Managers within the analytical groups are responsible for supervising the allocation of workload to ensure adequate coverage of each transaction. As noted under question 15 above, relative workloads between transaction and surveillance teams reflect the fact that there are structural and other qualitative factors required to be assessed at the initial transaction rating stage which do not typically require repeat analysis during the life of the transaction.

22. Are the costs of monitoring structured finance transactions fully covered by the fees charged specifically for monitoring when the rating agreement is initially made? What are the main incentives for maintaining effective monitoring of ratings?

We would expect to cover our surveillance costs on a per-transaction basis from surveillance fees. Beyond this, the motivation for ensuring effective monitoring of ratings is the same as that for ensuring appropriate initial ratings – the maintenance of our reputation and the added transparency that our ratings and research add to the marketplace.

23. How is committee time dedicated to rating reviews versus that dedicated to new ratings determined, particularly for structured finance? Are there clear internal procedures on how committee time is prioritised?

Committees are scheduled as and when required, according to our rating and procedural criteria, as opposed to being scheduled to a regular timetable. Surveillance and transaction committees thus do not "compete" for a finite allocation of standing committee time. Fitch is staffed to ensure that sufficient analysts of appropriate experience are available to attend whenever committees need to be called.

24. Are the committee members reviewing a rating the same as those who approved the initial rating? Are there any internal procedures dictating the composition of the review committee?

Committee membership and voting quora generally do not differ between the initial committee and the surveillance committee, with the exception of the use of "screeners[2]." In accordance with our internal procedures, each committee requires a Senior Director or above as Chair, and a minimum quorum of analysts, and is subject to the same provisions regarding rating decision appeals and other committee management considerations.

[2] In certain asset classes, where performance data is reviewed by an algorithmic 'screen' to identify transactions whose performance metrics vary from expectations, transactions may be affirmed with a quorum of two analysts, including a Senior Director. Any other action (downgrade, upgrade, Rating Watch designation or Outlook change) would require the convening of a full committee.

25. Is there a team of macroeconomic analysts within your firm responsible for systematically analyzing macro data coming in and building macroeconomic forecasts on which analysts can rely for their modelling/monitoring of ratings? If not, would this be useful?

Fitch's sovereign analysts work with the structured finance group to develop agency-wide assumptions on matters such as interest-rate stresses, currency-rate stresses and economic growth. We are currently looking at expanding this capacity with additional econometric resources. In addition, our structured finance group is assisted by a Quantitative Financial Research team, which participates in the construction and validation of models.

26. **Please provide us with a breakdown of revenues from SF ratings for initial rating/surveillance. How is the relative size of each of these parts of the fee decided?**

Global structured finance billings for the financial year ended Sep. 30, 2007 arose approximately 83% from transaction fees and 17% from surveillance fees.

As with the transaction fee, the fees determined for surveillance will consider the relative level of complexity of the transaction, including additional counterparty opinions that may need to be updated to maintain surveillance on the transaction rating.

<u>Methodology changes</u>

27. What prompts a review of rating methodology? Is there a central team that reviews methodologies or is it dependant on individual business lines self-evaluating their models?

All outstanding rating criteria in all asset classes across corporate, structured and public finance are reviewed on a regular cycle as determined by the cross-disciplinary Credit Policy Board ("CPB"), the agency's most senior credit review body. CPB members are drawn from senior analytical staff active in the major corporate, structured and public finance rating groups. Updated criteria are submitted to either the CPB or one of its discipline-specific subsidiary Criteria Committees by the relevant rating group.

Additionally, where new developments occur that prompt a group to review its criteria, the group composes a new (or amended) criteria document which is submitted to a discipline-specific Criteria Committee. For structured finance, all criteria are submitted to the Structured Finance Criteria Committee ("SFCC"). Membership of the SFCC is drawn from staff titled Senior Director and above across the major asset classes, and from a cross-section of Fitch's major offices, both in and outside of Europe.

The criteria document is accompanied by a criteria submission form (example enclosed as Exhibit NP2) which summarises, amongst other matters, the scope of the criteria, the main changes proposed to the criteria, the derivation of the main forms of credit enhancement under the criteria, the principal assumptions underlying the criteria, additional relevant criteria referenced in the new document, and the historical and projected rating performance of securities in that sector.

The criteria document is subject to a vote. If there is no consensus on a criteria, the submission may either be returned to the group for re-working, or be escalated to the CPB for a final decision.

28. Have you made any changes to how you evaluate the appropriateness of your methodologies on an on-going basis in light of the RMBS and CDO downgrades of earlier this year?

We are currently undertaking an internal review process to investigate alternative and additional mechanisms by which criteria and methodologies can be reviewed more efficiently. This may involve enhancements to the current criteria review process outlined in question 27 above.

29. When the methodology for a type of structured finance product (example being US sub-prime mortgage backed securities) is amended:

a. Do you automatically review all existing ratings against the new methodology and take rating action based on this review? If not, what is the rationale behind this?

Existing transactions are reviewed according to the criteria under which they were originally rated. Thus, only in rare circumstances will a change in criteria, by itself, change a rating. Emphasis is generally placed on seasoning and performance trends, such as delinquency, loss, and prepayment rates as determinants of rating changes. Reflecting the importance to market participants of avoiding unnecessary rating volatility, if a deal is identified for a possible moderate downgrade based purely on a conservative criteria change, but performance of the transaction is strong, the rating may well remain unchanged. Similarly, if the transaction is flagged for an upgrade following a criteria change but performance indicates a negative trend, the rating may well be left unchanged.

However, in cases where a significant departure from the original expectations occurs, the transaction may be reviewed in accordance with the new criteria. For example, this has been the case recently for transactions in the US subprime RMBS and collateralised commodity obligations areas.

All surveillance of structured finance ratings is based upon the periodic reports made available to us by issuers of rated transactions and/or their agents. These tend to be monthly in the US markets and quarterly outside the US. As discussed at our meeting, in a number of areas, screening algorithms are used to monitor large volumes of performance data and prioritise transactions for further review. These surveillance screening algorithms are updated to reflect new criteria. Fitch is currently extending the use of these screening algorithms for application in those sectors with sizeable homogenous transaction structures.

b. How is the scope of the application of the change of methodology determined? In other words on what basis does your firm decide whether or not to apply a change to existing ratings or just to new issuances?

See a. above.

c. Please explain in detail how is the timing of rating action determined across all affected ratings?

Rating actions are typically published as shortly as reasonably possible following the review of a transaction. As discussed at our meeting in Stockholm, exceptions may be made, in two principle cases:

- Firstly, where Fitch has initiated a major revision of criteria. In such a case, we believe that it is generally accepted in the marketplace that a single announcement is preferable, in which criteria-related actions can clearly be distinguished from credit-related actions.

- Secondly, where an entire sector or asset class faces profound and largely common issues (usually, though not always, of a negative nature). In order to communicate effectively the scale of the "rating response" to these issues (be it large or small), it can on occasion be more transparent to briefly delay certain rating actions while the full extent of the concerns are reviewed across the entire sector or asset class. In most cases, the ratings with the most potential for up- or downgrade will be placed on Rating Watch as an initial step while these reviews are carried out.

  Equally, as was the case with our review of US sub-prime RMBS this year, it may be more practical to prioritise the review of ratings by apparent severity (the most likely or severely affected are reviewed first), and release the rating actions in "batches". At all times, it is our aim to communicate in our public commentary as transparently as possible the approach we are taking, and in particular the approach we will be taking on ratings yet to be reviewed. Equally, in such cases, our aim is always to arrive at an appropriate rating as swiftly as possible, rather than to target external dates such as financial quarter-ends.

30. Does your firm at any time make any overall review of the changes to methodologies made, for instance during one year, and their impact on ratings to assess trends for instance? Would this be made public?

Fitch does provide regular summaries of the impact of major criteria changes on discrete sectors (e.g. recent criteria developments in recovery ratings, short-term ratings and the RMBS and CDO markets). We do not provide a collective assessment of the aggregate impact of all criteria changes across all asset classes, but equally we do not consider that such a report would provide useful or manageable data for most rating users. The majority of rating users are focused on the current level of ratings, and the current amendments to methodologies for asset classes on which they themselves focus (together with the discrete sectoral reports described above).

31. Is there a risk of originators 'gaming the system' i.e. keeping requested data sets high whilst other valid indicators of asset quality decline? If yes, what mitigation have you put in place to reduce this risk?

As we aim for transparency in our rating criteria, it will be possible for market participants to identify generally the relative weightings of, and emphasis on, given factors within our analysis. The final rating decision is, however, taken by a committee, where individual transaction features may result in a shifting in the weighting or emphasis between factors for a given rating.

Additionally, as noted under question 27, all criteria are reviewed by discipline-specific Criteria Committees on a regular cycle, even where there has been no impetus from a given analytical team to review a sector's criteria. This regular review helps reduce the risk that a change in the validity of specific indicators (i.e. that one or more ratios, measures or qualitative factors have become more or less explicative of credit quality) goes unnoticed over time.

32. Do you feel that your approach to the assessment of the quality of underlying asset data is appropriate? Are you considering any changes in this area (specially in light of the recent events in the US sub-prime mortgage market)?

We are currently undertaking an internal review process to investigate alternative and additional mechanisms by which our structured finance rating process in general may be enhanced. Any material changes in methodology will most likely be previewed in consultation drafts.

Conflicts of Interest

33. When you rate a structured finance operation do you offer services such as impact assessment and/or models of evaluation or optimisation of the securitization structure? Can you quantify[3] the number of cases where these kinds of services were offered? Would these services be performed by the analyst who rates the final structure?

Fitch does not provide services of this nature.

34. Is the analyst assigned to a certain structured finance rating deal allowed to give advice to the participants (before the rating is issued) about how to structure the deal in order to raise the rating? Is the analyst allowed to give feedback to the participants of a deal if the initial rating does not meet expectations? Are there limits to which elements of the deal can be addressed and to what extent (i.e. does the analyst provide suggested changes to the structure)? Is this covered in any internal policies? Is this interaction monitored by the agency?

Analysts do not structure transactions or provide structuring advice. In the course of providing feedback to an issuer, analysts will not propose alternative assets, legal structures or target rating levels.

More specifically, as part of feedback to an arranger's proposed capital structure, analysts may identify credit enhancement levels within a given pool, consistent with one or more tranche rating levels, from which an arranger can deduce how much the size of each tranche may be varied from the original proposal to become consistent with Fitch's criteria for a given rating. These levels are the result of a committee discussion, and represent the application of Fitch's published and publicly-available criteria. The decision to alter (or not) enhancement levels, or any other structural, legal or economic element of the transaction, remains that of the arranger, based on the arranger's or originator's view of the economic merits or advisability of the capital structure in which they wish investors to participate.

As part of its communication training for analysts, Fitch operates dedicated training sessions for structured finance analysts, addressing the dialogue that is held with arrangers, investors and other parties.

35. Can factors such as greater complexity and/or innovative features in a structured finance deal lead to a higher than standard fee? If yes, please indicate how much these aspects can increase the initial level of the fees (as a percentage), how this increase is determined and who makes this decision.

More complex deals can lead to higher fees being charged. Business development staff would discuss a transaction expected to be of greater complexity with a manager within the structured finance group to gauge the additional complexity involved. This discussion would typically involve an indication from the analytical staff of approximate additional time required, and other additional costs related to on-site reviews or to the analysis of multiple counterparties within the transaction. The analytical manager may often be able to cite prior transactions of similar additional complexity or additional workload as reference points.

Using this information, the business development staff will determine an appropriate rating fee structure and communicate this directly to the issuer/originator, arranger or their agents. This communication, the issuance of a fee letter and all other discussions related to the fee letter will be handled in accordance with Fitch's published policy on fee negotiations.

[3] E.g. in percentage of total structured finance ratings issued, or by giving the indication "always", "often", "sometimes" or "never".

36. Please provide us with data about your remuneration structures and those of your management hierarchy in your parent company.

All analytical staff are assessed and rewarded based on their analytical performance and on the overall financial performance of Fitch. Remuneration is set by reference to performance against objectives that are set at the beginning and, where appropriate, revised during the middle of each year. No Fitch analyst, including any analyst working in any structured finance group, is compensated or evaluated on the basis of the amount of revenue that Fitch derives from issuers or securities that the analyst rates, or with which the analyst regularly interacts.

The only Fitch employees for whom pay levels are directly linked to revenues are some members of our subscriptions sales teams. These employees are separated by a firewall from rating analysts, in accordance with Fitch's Firewall Policy. These staff members are responsible for the marketing of subscriptions to both our research reports and related products, such as Valuspread.

We noted additionally at our meeting that deferred compensation programmes are open to analysts within Fitch titled Senior Director or higher, as disclosed in the financial accounts of our majority parent company, Fimalac S.A. Management at parent companies are remunerated based on the financial performance of Fitch and of any other subsidiaries in which the parent has a stake. We understand they also have deferred compensation or option schemes. We should also note that management at the ultimate parent companies do not participate in the rating process.

Miscellaneous

37. Are you satisfied with the level of information received from servicers of European mortgage pools? Is this of a different quality, level of standardisation or frequency to information received in the US?

In Europe, because there are more jurisdictions, there is typically a wider variance of data quality and frequency compared to the US. We do, however, regard the data provided as adequate for the ratings that we assign. Where we do not have sufficient information to assign or maintain ratings, ratings will not be assigned or maintained, as the case may be.

However, Fitch always welcomes additional and, in particular, more frequent information on transaction performance. As an example, as noted in question 29a above, the prevalence of quarterly reporting of structured finance performance data in Europe contrasts with the more usual monthly reporting in the US. More generally, we support any initiative to enhance transparency and require more public disclosure from originators for the benefit of investors. We believe that the structured finance market in both the US and Europe is often too opaque and that transparency can best be achieved by originators, servicers, issuers and arrangers making publicly available all information, both at issuance and throughout the life of a structured finance transaction, that they make available to rating agencies (in the context of their rating analysis). We further believe that the internet provides an excellent venue to host this information so that it is freely and publicly available to all interested parties. The public availability of this information would enable investors to make fully informed investment decisions without having to rely solely on credit ratings to determine credit risk and would allow investors to assess independently issues such as market and liquidity risk that credit ratings do not address.

38. Are ratings across different asset classes similar in terms of pace and pattern of migration? Would some form of volatility indicator be possible, and appropriate for structured finance ratings?

We have attached as Exhibits P8, P9 and P10 our most recent transition & default studies. From these it is evident that migration patterns do vary across groups in the short- and long-term. While fewer cycles of data are available for structured than for corporate asset classes, it may now be possible to study these relative performance characteristics in more depth and use this analysis to enhance the criteria development process. We expect this review to inform the broad-based review of structured finance methodologies which is currently underway.

Specifically on the question regarding additional information on rating volatility, we agree that this information can be valuable, and have been working on numerous features, including stability scores. In fact, Fitch was the first agency to introduce such scores, after a lengthy development period, in early 2006. At the time we initiated Stability Scores, these were designed precisely to highlight the differing performance characteristics of instruments which carried the same rating on the 'AAA' scale. At the time, it is fair to say that the market was less interested in rating stability, or indeed rating differentiation, given the generally higher appetite for risk at that time. As a result, penetration of the Stability Score concept in the market was limited.

In the meantime, we have worked on revising the Stability Scores to broaden the scope of products covered. Equally, it is fair to assume the market is now more sensitised to risk differentiation than it was in March 2006. As a result, we will be looking at proposing an enhanced version of the Stability Score process in due course.

More generally, Fitch has done much work researching the best way in which to reflect additional risks affecting issuers and transactions. Our discussions with institutional investors, central banks and other interested parties have indicated a marked preference for discrete scales for discrete dimensions of risk (i.e. one scale covering default risk, one scale covering loss severity etc.) rather than combinations of risks on the same scale. Examples of successful multiple-scale sectors include our bank and insurance sectors, with a range of Support, Individual and Financial Strength ratings complementing the mainstream Issuer Default Ratings. In contrast, other areas where multiple scales have been introduced have seen more muted investor uptake. It is important to note that we cannot 'force' usage of any of our scales, and equally we will withdraw scales for which we perceive low investor demand.

EXHIBITS
(Public)

EXHIBIT P1: Downgrade Criteria for Recent Vintage U.S. Subprime RMBS, August 2007

EXHIBIT P2: Scanning the Horizon - Rating Outlooks in European Structured Finance, June 2007

EXHIBIT P3: SMARTView: Fitch U.S. Structured Finance Monthly Public Reviews, May 2007

EXHIBIT P4: "The Rating Process", July 2006

EXHIBIT P5: "Inside Credit Ratings: What Ratings Mean", August 2007

EXHIBIT P6: NRSRO Form, Exhibit 4

EXHIBIT P7: NRSRO Form, Exhibit 8

EXHIBIT P8: US Structured Finance Transition Study 2007

EXHIBIT P9: European Structured Finance Transition Study 2007

EXHIBIT P10: Corporate Finance Transition & Default Study 2007

EXHIBITS
(Non-public)

EXHIBIT NP1: Staff Turnover, 2003-2007

EXHIBIT NP2: Structured Finance Criteria Submission Form

Residential Mortgage
Criteria Report

Downgrade Criteria for Recent Vintage U.S. Subprime RMBS

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Related Research
- "U.S. Subprime RMBS/HEL Upgrade/Downgrade Criteria," dated June 12, 2007
- "Subprime Collateral Trends and Early Payment Defaults," dated April 12, 2007
- "Examining Home Price Inflation and Residential Mortgage Foreclosure Rates," dated May 24, 2007
- "Structured Finance Distressed Recovery Ratings," dated April 25, 2006

Summary

An unfavorable home price environment and the resulting impact on high-risk mortgage products has caused delinquency and default levels to sharply rise on subprime transactions backed by recent vintage collateral, 2005 and forward. In response, Fitch Ratings has introduced new surveillance methodology for monitoring the performance of securities from these vintages. The new methodology is designed to recognize the performance profile and distinct risks inherent in the individual securities. Additionally, Fitch is providing greater transparency on a class-by-class level, providing investors with a forward-looking forecast of mortgage default and loss.

Fitch's fundamental approach to expected loss and loss coverage ratio analysis is detailed in "U.S. Subprime RMBS/HEL Upgrade/ Downgrade Criteria," dated June 12, 2007 *(available at on Fitch's web site at www.fitchratings.com)*. The report describes Fitch's process for determining an expected remaining loss percentage (EL), as well as the loss percentage that causes each class to take a principal loss, referred to as the break loss (BL) percentage, for each subprime residential mortgage-backed security (RMBS) monitored by Fitch. The criteria also details Fitch's use of loss coverage ratios (LCRs) for determining a bond's credit rating.

The revisions to Fitch's surveillance methodology reflect a higher default and loss severity assumption used for determining the EL. Since LCR is a function of EL, revisions were made to the LCR scale for determining recommended rating actions. BL components, such as prepayment rates, were also adjusted to reflect the slower speeds exhibited by these vintages. This report should be read in conjunction with Fitch's aforementioned criteria report.

Criteria Review: Risk Factors and Loss Forecasting Methodology

The 2005 and 2006 RMBS transactions have been affected by the risk factors that Fitch and others have detailed while tracking 2006 vintage performance. These risk factors include combined loan-to-value (LTV) ratios of up to 100% and loans with limited or no verification of borrower income (stated income). Most importantly, these mortgage pools are subject to a rapidly deteriorating home price environment, particularly in those regions of the country with concentrations of subprime mortgages.

Fitch's estimates of home price declines are based on the regional risk forecasts provided by University Financial Associates for use in Fitch's ResiLogic default and loss model. As of the second quarter-2007 (2Q07) forecast, peak-to-trough nominal home price declines for

2006 vintage mortgages, weighted for Fitch-rated loan distributions, are projected to average approximately 6%–8%.

Performing Loan Adjustment

The factors described above have contributed to very high levels of serious delinquency and default among late 2005 and 2006 securitizations. Fitch's revisions to its criteria for estimating total defaults gives greater weight to early performance as a predictor of long-term performance, given the broad trend of high delinquency and worsening home price forecasts. For each securitization Fitch's benchmark default assumptions for loans currently performing is subject to a multiple based on the observed performance to date. The default multipliers for collateral subject to rating actions taken on Aug. 1, 2007 after implementation of the new criteria ranged from 1.2 times (x) to 2.2x the benchmark default assumption, which increased the percentage of each mortgage pool expected to default by as much as 5.75%.

2/28 Hybrid ARM Adjustment

The other major adjustment to Fitch's expected loss criteria is a change to default expectations for 2/28 hybrid adjustable-rate mortgage (ARM) loans. Given the poor performance to date of recently originated mortgage pools, the weakening home price environment, and the growing evidence of poor mortgage underwriting coupled with borrower/broker fraud, Fitch believes that ARM resets will engender higher default rates than those assumed in the initial rating forecast and higher than the existing rates. The withdrawal by lenders of many mortgage refinancing options further exacerbates this risk. Therefore, Fitch is applying two additional multipliers to 2/28 ARMs.

For those ARMs without a piggy-back second lien, the default expectation is multiplied 1.2x. For those ARMs with a piggy-back second lien, the multiplier is 1.5x, reflecting the risk to borrowers with no or negative home equity. These multipliers increased the default assumption by 2%–4% for the RMBS acted on Aug. 1, 2007.

Second Lien Loss Severity Adjustment

In addition to these factors, the worst performing transactions have another attribute in common: the presence of a significant concentration of second liens in predominantly first-lien transactions. While many recent vintage transactions contain first liens that have an associated second lien, the second lien was typically not securitized in the same transaction. Rather, if the second lien was securitized, it was placed in a separate transaction backed entirely by second liens. However, many of the RMBS transactions are backed by pools containing in excess of 5% and, in some instances, more than 10% of second liens.

Very poor performance by second-lien mortgages has led to early and substantial downgrades of second-lien securitizations. Similarly, the presence of second liens that are defaulting rapidly and with very high loss severity is having and, in Fitch's opinion will continue to have, a substantial negative impact on the performance of RMBS backed by mixed pools of first and second liens. The poor delinquency performance of these transactions is captured in the default rate adjustment described above. The other feature of second liens that must be accounted for is loss severity, which for 100% CLTV second liens is typically 100%.

In analyzing each RMBS transaction, Fitch determines that the expected loss severity reflects the high percentage of defaulted second liens. Transactions with concentrations of second liens have projected lifetime loss severities of about 50%, whereas transactions with lower concentrations have a projected loss severity closer to 40%.

The combined effect of all the aforementioned adjustments will result in higher expected default and loss severity assumptions. The expected remaining loss on these transactions, as well as the expected loss as a percentage of the original balance, will also increase over levels derived by Fitch's prior methodology.

■ Rating Action Methodology

For each RMBS class, Fitch generates cash flows that estimate how much loss as a percentage of the outstanding balance each class can withstand before incurring a writedown (or loss) given Fitch's loss timing curve, prepayment curve, and interest rate assumptions. Fitch refers to this as the BL for the class. There has been one revision to methodology related to cash flow generation, reflecting the fact that prepayment rates for many transactions are currently running slower than Fitch's expected rates.

The cash flow analysis utilizes the slow observed speeds in the early life of the transaction; however, the speeds are gradually ramped up back to Fitch's standard assumptions over a 24-month time frame, so as not to give undue benefit to excess spread

Minimum Loss Coverage Ratio (MLCR) Benchmarks

Fitch Rating	MLCR
‘AAA’	2.50
‘AA+’	2.25
‘AA’	2.00
‘AA–’	1.75
‘A+’	1.60
‘A’	1.50
‘A–’	1.40
‘BBB+’	1.30
‘BBB’	1.20
‘BBB–’	1.10
‘BB+’	1.03
‘BB’	0.95
‘BB–’	0.88
‘B+’	0.82
‘B’	0.75
‘CCC’	< 0.75

generated by slower prepayments. The slower speeds will increase the level of loss a class can withstand and, therefore, raise the BL of the class.

In addition to revising the EL and BL methodology described above, Fitch has adopted a specific set of minimum loss coverage ratio (MLCR) benchmarks for determining recommended rating actions on these vintages. The Fitch LCR is computed for each class as the break loss divided by the expected loss (LCR = BL/EL). Fitch’s standard surveillance analysis utilizes MLCRs derived from new issue rating levels, with adjustments for seasoned vintages to reflect the volatility of expected losses.

For the evaluation of transactions from these vintages, Fitch has adopted a set of MLCRs that reflect the more severe current expected case based on the assumptions discussed above than that used in determining the original rating. As such, classes that cannot demonstrate an LCR of at least 1.1 are subject to ratings adjustments to below-investment-grade status. However the MLCRs also reflect Fitch’s opinion that the levels of loss that highly rated securities can withstand still represent unlikely events and, thus, the MLCRs are compressed relative to those for new issue ratings. Additionally, Fitch considers the expected time to pay off for highly rated classes. Those classes that are expected to pay off in 60 months or less are not recommended for downgrade based on MLCR.

For example, assume a transaction has a revised expected loss of 12% of the outstanding pool balance (EL = 12%). Cash flow analysis shows that the class currently rated ‘AAA’ (class A) can withstand losses equal to 32% of the outstanding balance before incurring a loss (class A BL = 32%), and the class currently rated BBB (class B) can withstand losses equal to 11.75% of the current balance (class B BL = 11.75%). In this example, class A would have an LCR = 32%/12%, or 2.67. Class B would have an LCR = 11.75%/12%, or 0.98. The class A LCR of 2.67 exceeds the minimum ‘AAA’ LCR of 2.5 and, therefore, is recommended for affirmation. The class B LCR of 0.98 fails to exceed the ‘BBB’ MLCR of 1.2, and so the class is recommended for downgrade. However, the class B LCR exceeds the MLCR for a rating of ‘BB’; therefore, the recommendation in this example is to downgrade to ‘BB’ from ‘BBB’.

Rating committees conducted by senior analysts review the EL, BL, and LCR indicators, which provide a basis for the recommended rating action. Fitch analysts also consider other factors that may be relevant to the rating action.

Increased Transparency

Rating actions taken on Aug. 1, 2007 based on Fitch’s revised surveillance methodology resulted in the ratings distribution highlighted in the table below.

Note that the average LCR in some rating categories is significantly higher than the minimum LCR. Classes that have been affirmed at their current rating often have LCRs greater than the minimum. The surveillance criteria does not provide for upgrades for unseasoned subordinate classes.

Fitch believes that the revised LCRs, combined with the revised expected loss methodology, provide

Rating Actions: Aug. 1, 2007

New Rating	No. of Classes	Balance ($ Mil.)	Average BL (%)	Average LCR
‘AAA’	120	16,865	37.75	2.85
‘AA+’	31	1,380	30.19	2.36
‘AA’	17	687	27.50	2.15
‘AA–’	17	418	24.84	2.00
‘A+’	18	411	22.13	1.82
‘A’	15	358	20.67	1.68
‘A–’	18	414	20.45	1.56
‘BBB+’	23	385	17.99	1.40
‘BBB’	19	293	17.22	1.27
‘BBB–’	21	325	15.80	1.15
‘BB+’	14	162	14.15	1.08
‘BB’	16	185	14.36	0.99
‘BB–’	16	178	12.85	0.91
‘B+’	6	49	12.13	0.84
‘B’	11	126	11.60	0.79
‘CCC’	20	186	11.55	0.65
Total	382	22,422		

Note: Numbers may not add due to rounding.

investors with timely, consistent opinions as to the relative credit quality of rated securities. Fitch will publish the BL and LCR for each transaction for these vintages placed "Under Analysis" on its SMARTView surveillance product. With these risk indicators, Fitch is providing this detailed information regarding the basis of subprime RMBS rating opinions to aid investors in considering those opinions as part of its ongoing risk analysis.

For 'CCC' rated classes, Fitch's standard surveillance methodology calls for the assignment of a distressed recovery (DR) rating to classes rated below 'B–'. Fitch will review the application of DR ratings in the context of the updated methodology and provide further commentary on the recovery prospects of deeply distressed securities.

European Structured Finance
Special Report

Scanning the Horizon — Rating Outlooks in European Structured Finance

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Summary

Fitch is today launching, Rating Outlooks in European Structured Finance (ESF) following the publication of an Exposure Draft on 30 April 2007 and the subsequent commentary period.

Rating Outlooks, which Fitch currently publishes for corporate, financial institutions, sovereign and municipal issuers, are being introduced for ESF tranches to provide more forward-looking information to the market. An Outlook indicates the likely direction of any rating change over a one- to two-year period. Outlooks may be Positive, Negative, Stable or, occasionally, Evolving. The Outlooks will be reviewed concurrently with the rating review for the transaction, and will be supplemented with a commentary describing Fitch's rationale for the Outlook.

Highlights

- Assigned at tranche level, providing an early indication of the potential future direction of the rating
- Accompanied by rating action commentary to explain collateral performance indicators and trends
- The Outlook reflects the changes in credit support over time due to performance and amortisation
- Rating Outlooks highlight prospective economic and sector developments affecting collateral

Distribution of Outlooks

The table on the following page shows the initial distribution of Outlooks across each of the ESF asset classes. As expected, the Positive and Negative distribution of the Outlooks broadly reflects the rating migration that has been seen in ESF over the last couple of years.

RMBS has the most Positive Outlooks, in terms of both numbers and the percentage of tranches rated. This is primarily due to the large number of RMBS deals that are well seasoned and have built up a cushion of credit support through prepayments and the amortisation of senior classes over the years.

Often in CMBS, prepayment is lumpy and less predictable and this is reflected in the lower number of Positive Outlooks. A large percentage of the rated CMBS tranches are also from relatively new deals and therefore lack the seasoning that benefits RMBS.

As a percentage, the number of Negative Outlooks in RMBS and CMBS is low, reflecting the stable rating migration of the past few years.

1 June 2007

ABS has the biggest percentage of Negative Outlooks, almost all of which refer to Corporate ABS. Three of the Positive Outlooks in the ABS sector correspond to ratings dependent on the Long-Term Rating of the Region of Sicily, whose Outlook is Positive. The distribution of Outlooks within the ABS category in this report includes those for Whole Business transactions, which are rated out of the Global Infrastructure and Project Finance Group since January 2007. For clarification, the distribution of Outlooks does not include any current Rating Watch actions outstanding.

Table 1: Distribution of Outlooks Assigned in ESF at 17 May 2007

	Positive	Stable	Negative	Total
ABS	8	475	17	500
RMBS	237	2,799	21	3,057
CMBS	41	984	7	1,032
Total	**286**	**4,258**	**45**	**4,589**

Source: Fitch

Table 2: Percentage Distribution of Outlooks

(%)	Positive	Stable	Negative
ABS	2	95	3
RMBS	8	92	1
CMBS	4	95	1

Source: Fitch

■ What is a Rating Outlook?

Fitch defines a Rating Outlook as follows:

An Outlook indicates the direction a rating is likely to move in over a one- to two-year period. Outlooks may be Positive, Stable or Negative. A Positive or Negative Rating Outlook does not imply a rating change is inevitable. Similarly, ratings for which Outlooks are "Stable" could be upgraded or downgraded before an Outlook moves to Positive or Negative, if circumstances warrant such an action. Occasionally, Fitch may be unable to identify the fundamental trend. In these cases, the Rating Outlook may be described as Evolving.

Rating Outlooks for ESF transactions will be assigned to the rating for each tranche, since developments in the performance of a transaction can affect the Outlook for different tranches in various ways. For example, a modest deterioration in the performance of a transaction's collateral might lead to a Negative Outlook for the most junior-rated tranche, but be consistent with a Stable Outlook for all the more senior tranches.

In contrast, the Rating Outlook in the corporate, financial institutions, sovereign and municipal sectors is assigned to the Issuer Default Rating of the issuer and reflects the financial trends and position of the issuer in its industry or sovereign context.

■ What do Rating Outlooks Add?

Rating Outlooks offer investors a forward-looking opinion about the medium-term prospects of a tranche's rating. Where appropriate, reviews of Rating Outlooks will be supplemented by comments giving reasons for the assigned or revised Outlooks. This is to provide the market with a better understanding of the potential future performance of the tranches' ratings.

■ How are Rating Outlooks Assigned?

Rating Outlooks will be assigned by a rating committee as part of the continuing monitoring of transaction ratings by Fitch's performance analytics teams. Rating Outlooks are to be assigned or reviewed as often as the Long-Term Ratings are reviewed. Ratings are reviewed as often as information is received, and a formal committee is convened whenever Fitch's ongoing monitoring identifies information that might justify a change of rating opinion or at least annually.

In assigning or reviewing Rating Outlooks in ESF, committees take into account:

- the latest collateral performance indicators and trends in performance;
- the amount of credit support available to each tranche as a result of the performance and, where relevant, amortisation of the transaction collateral;
- prospective developments in national or regional economic and/or sector outlooks that could affect collateral performance;
- the Rating Outlook on any supporting corporate, financial institutions or sovereign rating.

Newly rated tranches are expected to be assigned a Stable Rating Outlook at issue unless special circumstances exist. For example, an entity providing a supporting rating, which itself has a Positive or Negative Outlook, might justify the same Outlook being applied to the new ESF rating.

■ How Well-Correlated are Outlooks with Rating Changes?

Rating Outlooks are not intended to be perfectly correlated with subsequent rating actions. Indeed, a perfect correlation would imply that the assignment of a Positive or Negative Rating Outlook simply serves to delay the announcement of the subsequent rating change.

Some tranches assigned Positive or Negative Rating Outlooks may not experience a rating change within the two-year horizon. For example, the trends that support the Outlook might not be sustained or might develop more slowly than expected. Equally, some ratings are likely to be changed despite having a current Outlook of Stable. This will arise when Fitch becomes aware of information that gives clear justification for a rating change, but whose potential was not foreseen at the time that the Stable Outlook was assigned. This could arise, for example, as a result of a marked change in collateral performance or sector conditions, an event-driven change in a Supporting Rating, or the effects of fraud.

Occasionally a Rating Outlook may give a "perverse" signal of a rating change, such as a downgrade occurring from a rating with a Positive Outlook. The agency expects this to be a rare occurrence, but it could arise, for example:

- if the collateral performance gives a positive background, but a rating supporting the tranche is downgraded due to an event affecting the rating of a bank or corporate entity with a credit-sensitive role in the transaction;
- in the case of a changing pool of collateral, or a floating-rate CMBS transaction.

What Is the Difference Between Rating Watch and Rating Outlook?

Ratings are placed on Rating Watch to notify investors that there is a reasonable probability of a rating change and to indicate the likely direction of such a change. Rating Watch is often used in ESF when not enough information is available to make a final decision. Rating Watch is generally resolved in three to six months, whereas Outlooks imply a longer timeframe, generally 12-24 months.

Rating Outlooks will cease to apply whenever a tranche is placed on Rating Watch. Once a Rating Watch has been resolved, a new Rating Outlook will be assigned.

Where will Rating Outlooks be Published?

Rating Outlooks will be published on Fitch's website from 1 June 2007, alongside the relevant rating for virtually all the transactions Fitch rates in the European ABS, CMBS and RMBS sectors.

Changes to Rating Outlooks will be announced by a rating action commentary in the same manner as changes to ratings. Where appropriate, reasons will be given for a change in Rating Outlook.

Criteria Report

SMARTView

Fitch U.S. Structured Finance Monthly Public Reviews

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SMARTView is now available for U.S. commercial mortgage-backed securities, asset-backed securities auto loans and equipment leasing/loans, and residential mortgage-backed securities prime, Alt-A, and subprime transactions.

May 3, 2007

■ Summary

Fitch Ratings announces the implementation of SMARTView following a one-month comment period for its exposure draft, titled "S.M.A.R.T. Stamps (Fitch U.S. Structured Finance Monthly Public Reviews)," dated Aug. 3, 2006. The goal of SMARTView is to publicly disclose the results of monthly or quarterly reviews that each structured finance transaction undergoes. The frequency of reporting will depend on bondholder reporting of each asset class. SMARTView will provide evidence to the investor community that Fitch is actively monitoring each deal on a continuous basis. The assignment of SMARTView is Fitch's public announcement that, with the information available on any given day, the current ratings reflect Fitch's risk assessment of the transaction.

Fitch plans to begin implementation of SMARTView with commercial mortgage-backed securities (CMBS) and expects to follow suit with most of the remaining U.S. structured finance asset classes. SMARTView will be available to the public on Fitch's web site at www.fitchratings.com.

■ Use of SMARTView

Fitch strives to provide the most up-to-date and transparent ratings to the market. To meet this objective, Fitch has dedicated analysts who actively monitor all ratings on a continuous basis by closely tracking the underlying collateral. CMBS information is reported by the trustee and servicer on a monthly basis. As this information is received, it is run against various Fitch internal algorithms, which identify classes of a transaction as possible upgrade, downgrade, or affirmation candidates. Fitch analysts scrutinize the output to decide which deals need a review and which can be given a SMARTView date. Generally, those deals that require an in-depth review will be reviewed within a 30-day window.

■ Use of Rating Watch

The use of Rating Watch may be appropriate for transactions that do not receive an in-depth review and rating action commentary (RAC) within the 30-day window. Generally, Fitch is able to complete a transaction review within 30 days. Certain transactions may require additional analysis or information that is not readily available to determine an appropriate rating action. Placing classes in these transactions on Rating Watch will alert investors to a reasonable probability of a rating change and the likely direction of such a change. Rating Watch is classified as: Positive, indicating a potential upgrade; Negative, for a potential downgrade; or Evolving, indicating ratings might be raised, lowered, or maintained. Rating Watch is typically resolved over several months, so there may be months in which a deal's SMARTView is updated even though several classes are on Rating Watch.

Monthly Process

The following is an example of the monthly process:

- Days one through five:
  - Algorithms are run that place each class of every transaction into a potential upgrade, downgrade, or affirmation state.
  - Analysts review the algorithm outputs to identify those eligible for SMARTView dates or Under Analysis designations.
- Day five:
  - SMARTView dates are assigned to transactions not requiring an in-depth review. Transactions requiring an in-depth review will be labeled Under Analysis.
- Days five through 30:
  - Analysts perform in-depth reviews for transactions labeled Under Analysis, and RACs are issued. For these transactions, the date associated with SMARTView will be set to the RAC date.

Frequently Asked Questions

Below are some questions that have been asked frequently as Fitch analysts explain this process to market participants:

If ratings are meant to be long term, why add SMARTView?

Ratings are still considered to be long term. SMARTView is a public notification of Fitch's internal assessment, akin to affirming ratings on a monthly basis.

What is the difference between Under Analysis and Rating Watch?

Under Analysis indicates that a Fitch RAC will be issued within 30 days. The Under Analysis designation is at the deal level and not necessarily meant to alert investors to a directional movement in ratings, whereas Rating Watch is by class and directional.

If a deal receives a SMARTView date, is that a guarantee that no rating action will follow within 30 days?

Typically, Fitch receives information from the trustee and/or servicer on a monthly basis. However, if in the course of monitoring each transaction Fitch receives additional information, either public or private, that warrants an immediate rating action, Fitch will take that action.

Does the SMARTView process eliminate Fitch's goal of performing an in-depth review for each deal at least once annually?

Not for the time being. Fitch still aims to perform at least one in-depth review per year, regardless of whether a deal is identified as a potential upgrade or downgrade candidate. This review will ensure that any potential issues are evaluated, and Fitch will provide commentary to the market through a RAC. Over time, this process may prove redundant or unnecessary.

Will the use of SMARTView introduce ratings volatility?

No, Fitch is already using the process internally, and it has resulted in Fitch's timely rating actions. The use of SMARTView will not change the way Fitch makes rating decisions. Fitch has been using the underlying process for more than two years, and publications of SMARTView share the results with the entire market. The upgrade actions taken thus far in 2006 have predominantly resulted from defeasance and loan repayments. The resulting credit enhancement increases merit upgrades.

Fitch Ratings
KNOW YOUR RISK

The Rating Process

July 2006

Fitch has standardised procedures for the preparation of ratings and the conduct of rating committees. This report summarises the typical rating process for the majority of Fitch's traditional international scale credit ratings – procedures may vary including, for example, for the assignment of model-based quantitative ratings as well as asset manager, fund, servicer, operational risk or similar non-credit ratings. The paragraphs that follow should be read in conjunction with Fitch's "*Code of Conduct*", which was published in April 2005 and is available from Fitch's free public website, www.fitchratings.com.

The disclaimers set forth in Section 4 of Fitch's Code of Conduct apply equally here. Please note, inter alia, that, with the publication of this document, Fitch does not intend to assume, and is not assuming, any responsibility or liability to any party arising out of, or with respect to, this document. This document is not intended to, and does not, form a part of any contract with anyone and no one shall have any right (contractual or otherwise) to enforce any of this document's provisions, either directly or indirectly. Fitch may amend this document (and the process described herein) in its sole discretion, in any way Fitch sees fit at any time.

› Analytical Team

At the start of the rating process each rated entity or transaction is assigned to a primary analyst, who works with the support of a back-up analyst. For corporate and public finance ratings, the primary analyst is responsible for leading the analysis and formulating a rating recommendation, and is typically also responsible for the continuous surveillance of the rating during the life of its publication. While the primary analyst for structured finance transactions is also responsible for leading the analysis and formulating the initial rating recommendations for the transaction, in most cases, they transfer responsibility for the ongoing surveillance of the transaction to a dedicated surveillance analyst after publication. Although Fitch analysts have a wide range of backgrounds, the majority are recruited from banks, insurance companies, investment houses and the financial departments of major companies.

› Input from Rated Entities

Fitch's analysis and our rating decisions are based on information received from **all** sources. This includes relevant publicly-available information on the issuer, such as company financial and operational statistics, reports filed with regulatory agencies and industry and economic reports. In addition, the rating process may incorporate data and insight gathered by analysts in the course of their interaction with other entities across their sector of expertise.

The rating process also usually incorporates information provided directly by the rated issuer, arranger, sponsor or other involved party. This can include background data, forecasts, feedback on proposed analytical research and other communications. Depending on the availability of management and the frequency or urgency of contact, this information is gathered through face-to-face management and treasury meetings, during site visits or via teleconferences and other correspondence. In general, the main topics for discussion and key questions are provided in advance of any management meetings and an agenda is established to ensure a productive dialogue. However, additional questions can arise during the course of discussions.

With regard to corporate and financial institution ratings, an analyst's main dialogue will typically be with senior executives from the financial departments of a rated entity, such as the chief financial officer or group treasurer. Nonetheless, they may also have discussions with senior strategic management, including the chief executive officer and chief risk officer where appropriate, as well as senior operational managers. For sovereign rating visits, analysts will meet with key policymakers and senior representatives of various public sector institutions, such as the finance ministry and the central bank, as well as a number of informed outside observers of the political, economic and policy environment. Structured finance analysts will typically hold a dialogue with transaction arrangers and other agents of the issuer or originator, which in some cases will include site visits, on-site portfolio or servicer reviews and similar face-to-face discussions.

For entity ratings, while historical performance often provides a starting point for our analysis, the outlook for the entity is the primary consideration in the determination of the rating. As such, Fitch will take into consideration both Fitch's and, where appropriate, the entity's medium-term projections of operating and financial information. These forecasts are used not so much as point estimates of financial parameters, but rather to provide a "road map" of the entity's direction and the financial strategies that the entity is likely to use to achieve its strategic goals. At all times, Fitch must be satisfied that it has sufficient information to form a view on the creditworthiness of an entity or transaction. If Fitch does not have sufficient information either to assign or maintain a rating, then no rating will be assigned or maintained.

› The Committee Process

Ratings are assigned and reviewed using a committee process. The primary analyst incorporates the information from their research into their rating recommendation and supporting committee package. During this time, they also typically maintain a dialogue with the entity to resolve any outstanding issues or to request additional information.

Committees consider the information contained in the committee package, and a consensus decision is reached on an appropriate rating, including, where appropriate, a Rating Outlook or Rating Watch designation. Where entity ratings are assigned, the determination of an Issuer Default Rating or Long-term issuer rating is the primary focus of the committee. Issue ratings will be assigned relative to this rating and take into consideration Fitch's opinion of the recovery prospects of different debt issues in the event of default.

The minimum committee size for rating decisions is generally four analysts, although many committees involve more analysts than this. The committee will generally include at least one analyst titled Senior Director or above. A Senior Director will typically average 6-7 years of tenure with Fitch, and/or a number of additional years of prior experience in the credit markets. The primary analyst for the credit will generally be one of the voters of record. Other voting members are chosen based on relevant experience. Rating committees frequently include analysts from outside the immediate asset class, sub-sector or geographic area of the entity under review, since peer analysis (on a transaction or entity basis) is a central element of the rating committees' discussions. Analysts joining Fitch are typically subject to a three-month non-voting 'probationary' period, but may attend committees as observers.

The rating committee considers the relevant quantitative and qualitative issues to arrive at the rating that most appropriately reflects both the current situation and prospective performance. If there are no unresolved issues, a rating is assigned and, to the extent feasible and appropriate, the outcome of the committee is communicated to the entity or, where applicable, their arranger/sponsor. If there are unresolved issues, the committee meeting may be suspended until the issues are resolved and a rating can be subsequently determined. Where an 'expected rating' is assigned, this usually relates to a transaction rather than an entity rating. It indicates that the transaction will carry a finalised rating at that level subject to the receipt of final documentation that conforms with the assumptions presented to the committee.

› Criteria Development

Rating decisions are made in accordance with the methodologies and criteria applicable to that sector. The methodologies themselves, and the criteria that determine rating levels within each major methodology, are created and revised by the analytical teams. New and revised criteria documents are reviewed by the agency's global Criteria Committees, covering Corporate Finance, Structured Finance, Public Finance and Emerging Markets. These Committees meet regularly and are composed of senior analysts from a balanced selection of different analytical groups and international offices. New criteria that affect a wider range of analytical areas, or propose a new rating scale, are additionally submitted to Fitch's multi-disciplinary Credit Policy Board, the senior-most analytical decision-making body of the agency. The Credit Policy Board also serves as an appeal forum for the agency's Criteria Committees.

› Differences of Opinion

If a committee cannot reach a consensus, an appeal procedure exists for a review of the rating. In addition, in certain circumstances, an issuer may also request a review as long as it provides, in a timely manner, new or additional information that Fitch believes to be relevant to the rating. However, rating affirmations, Outlook changes and Rating Watch actions are not generally subject to review at the request of the issuer.

Where a review is considered appropriate, senior analysts not previously involved in the committee process join members of the original rating committee to reconsider the rating analysis. Fitch aims to conclude the review of any new rating expeditiously and the review of any existing ratings within two business days. In cases where the review of an existing rating is not finalised during that period, the rating is typically placed on Rating Watch Negative. As noted in the Fitch Ratings Code of Conduct, Fitch reserves the right to publish a public rating if circumstances warrant, even though a review may be in process.

Appendix A illustrates the credit rating and appeal process in more detail.

› Access to Confidential Information

Analysts at Fitch regularly have access to confidential information. This is treated with appropriate sensitivity in accordance with Fitch's confidentiality policy (Fitch Ratings Worldwide Confidentiality, Conflicts of Interest and Securities Trading Policy), which is available from our free public website. Importantly, users of our ratings should be aware that the analysis and committee decision for all Fitch ratings is based on **all** information known to Fitch and believed by Fitch to be relevant to the rating decision. Therefore, information shared with one analytical group may be shared internally with another group if it is considered relevant.

Users of ratings should nonetheless be aware of the general limitations on the nature of the information that rated entities make available to rating agencies. Fitch does not, and has no obligation to, audit or verify the accuracy of data provided. Moreover, issuers may choose not to share certain pieces of information with external parties, including rating agencies, at any time. While Fitch expects that each issuer that has agreed to participate in the rating process, or its agents, will supply promptly all information relevant to evaluating both the ratings of the issuer and all relevant securities, the agency neither has, nor would it seek, the right to compel the disclosure of information by any issuer.

› Surveillance of Ratings

Unless they are of a 'point-in-time' nature, Fitch's ratings are monitored on an ongoing basis and Fitch is staffed to ensure that this is possible.[1] Analysts in all groups will initiate a rating review whenever they become aware of any business, financial, operational or other information that they believe might reasonably be expected to result in a rating action, consistent with the relevant criteria and methodologies. Thus, for example, an operational or fiscal deterioration, an acquisition, a divestiture, or the announcement of a major share repurchase may all trigger an immediate rating review. Consequently, the review process should be regarded as a continuous one. Ratings are also subject to formal periodic reviews.

› Rating Dissemination

Following the completion of a rating review, all rating actions for new or existing publicly-rated entities – whether an affirmation, downgrade, or upgrade, and including any decisions taken regarding either the Outlook or Watch status – are published on Fitch's free public website and simultaneously released to major newswire services. These rating action commentaries provide a brief rationale for the rating decision. The ratings of all publicly-rated debt issues of the issuer are also available from the public website, along with all current criteria and methodologies, and a broad selection of special reports. Access to the public website requires the reader to create a User ID and a password, but is available at no charge.

All public ratings, both of entities and individual debt issues, are also available free of charge from the Ratings Desk, for which contact details can be found on the public website. Analysts are available by telephone, e-mail and at various public forums to discuss the rationale for our ratings. Pre-sale research reports may also be made available on selected transactions.

Fitch makes every reasonable effort to ensure that the time between a rating committee determining a final rating action and the publication of that rating action and related commentary is as short as reasonably possible. Revisions to, or affirmations of, existing ratings generally occur by the end of the following business day at the latest, with many announcements occurring on the same business day. The timing of the announcement for initial ratings may be more flexible on occasion, but Fitch strives to ensure that the timing remains as expeditious as possible.

[1] 'Point-in-time' (PIT) ratings would be assigned, for example, to debtor-in-possession financings of bankrupt entities in the US, or in the case of ratings that are based purely on periodic quantitative scoring, such as Q-IFS ratings for insurance companies. Where ratings are constructed on a 'point-in-time' basis, this is clearly disclosed in the accompanying rating action commentary. Separate conditions can sometimes apply to the assignment of such ratings, as disclosed in the relevant methodology and, due to their PIT nature, these ratings are excluded from default rate calculations.

The timing of publication reflects the important balance to be maintained between an appropriate time being allotted, to the extent reasonably feasible and appropriate, for the rated entity to review the rating rationale for factual accuracy and the presence of confidential information, and the requirements of the users of ratings for timely and objective opinions. Where issuers provide comments on draft commentaries, Fitch duly evaluates this feedback. However, the review is aimed at the removal of any factual errors or references to non-public information and Fitch retains full editorial control over its commentaries.

In addition to our published rating action commentaries, which are the primary method for communication of our rating rationales, a longer research report is published on most issuers and made available to our subscribers. The main language of publication is English, but selected research reports are published in other languages where it is felt that this would be appropriate. On occasion, the rated entity may also distribute copies of its research reports issued by Fitch to banks, investors, customers or other interested parties.

› Product Range

In addition to published international and national scale ratings, Fitch offers a number of additional services within the core rating business:

- In certain circumstances, unrated entities may request a **credit assessment** from Fitch. A credit assessment provides an indication of the likely rating that an entity may receive if it were to request a full rating. The assessment is a rating-level opinion carried out by analysts from the same group that would assign a full rating, and can consider all materials that the requesting entity is prepared to provide for the assessment process.

- Fitch can also provide **Rating Assessment Service (“RAS”)** opinions to rated and unrated entities under certain circumstances. RAS opinions indicate to the issuer or their agent what rating level that issuer and its obligations would be likely to receive, given a set of hypothetical assumptions provided by the assessed entity. These might include details relating to a reconfiguration of the capital structure or the impact of an acquisition or disposal. This assessment is a rating-level opinion performed by the analytical group responsible for that entity, and feedback is provided to the assessed entity, or its agent, or the entity’s majority owner, or their agent, in writing, including a detailed list of assumptions and limitations applied in the assessment.

- Finally, Fitch also provides **shadow ratings** on entities and transactions where information is limited, where only an abbreviated analysis is required (for example, on one asset which forms part of a diversified pool), or where a specific element of the analysis has been omitted. The qualitative difference between such shadow ratings and a full rating is demarcated with the use of an asterisk (e.g. ‘BBB+*’) and described fully in any communication from Fitch regarding the shadow rating.

In most cases, these opinions – credit assessments, rating assessments and shadow ratings – are provided on a confidential basis. While they may be similar to ratings in many ways, they are not formal ratings and should not be employed by rating users without consideration of any limitations that they may have or any conditions attached to their use.

Fitch also prepares a limited number of **private ratings**, for example for entities with no publicly traded debt, or where the rating is required for internal bench-marking or regulatory purposes. These ratings are generally provided directly to the rated entity, which is then responsible for ensuring that any party to whom it discloses the private rating is updated when any change in the rating occurs. Private ratings undergo the same analysis, committee process and surveillance as published ratings, unless otherwise disclosed as 'point-in-time' in nature (see above).

› Timing of the Process

Fitch's global resources allow the agency to respond in a timely manner to requests for ratings and other credit opinions. The actual time taken to assign a new rating can vary, and will partly depend on the time required by the rated party to respond to information requests from Fitch and to review the rating feedback provided by the agency. However, Fitch will make reasonable efforts to accommodate the needs of the entity, both in terms of the timing of any rating visit and the completion of the subsequent review process.

As an example, Fitch typically assumes a timeframe of six to eight weeks to provide a full corporate, financial institution or sovereign rating. Structured finance ratings may be prepared over a longer period, as rating agencies are often involved at an earlier stage in the decision to undertake a structured finance transaction, but Fitch is staffed with sufficient resources to be able to respond in a flexible manner and prepare ratings within a shorter timeframe if necessary. The timings noted provide flexibility in the process and the least time pressure on the resources of the rated party.

› Fees

Fitch has a dedicated business development team that is able to assist with the process of issuers requesting a rating, and to deal with any commercial matters regarding the rating that may arise. Entities wishing to request a rating are encouraged to contact Fitch's business development staff in either of our head offices, in London and New York, or one of our many local offices. The location and contact details of each of our worldwide offices are available from our free public website.

The fees charged to entities for public ratings can be structured in a variety of ways, typically involving:

- a fixed-rate recurring base fee for an issuer rating or for the surveillance of a rating;
- a once-only transaction fee based on a percentage (typically several hundredths of one per cent) of the nominal value of a given transaction; or
- a combination of the two (i.e. a recurring or once-only fee that covers both issuer and transaction ratings).

Fees related to transaction volume may also be subject to a cap in a given year for a single issuer.

› Rating Withdrawals

Fitch reserves the right to withdraw any rating at any time for any reason, for example, due to a lack of information or lack of market interest. If an analyst is concerned that the information provided is insufficient to make a rating assessment of an entity or transaction, this will be discussed with the sector's Managing Director and, where appropriate, withdrawal of the rating will be proposed to a rating committee.

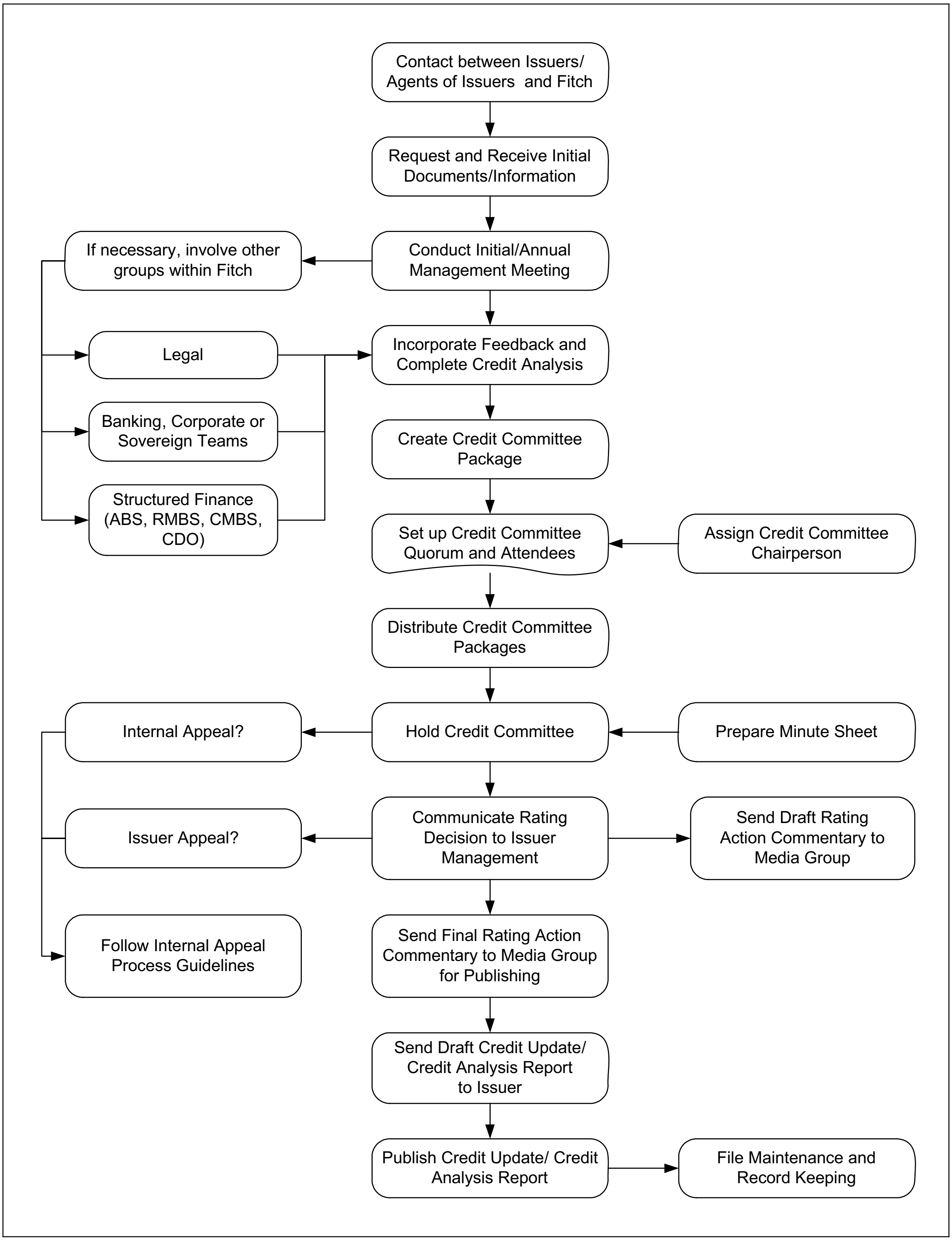
Quality Standards

Fitch places a great deal of importance on the consistency of its rating product. Thus, common processes apply for ratings assigned to entities in both emerging and developed markets and between all Fitch offices, irrespective of size or location. As mentioned earlier, the methodologies for each area of our business are generally constructed on a global basis, even where the emphasis added to individual criteria or specific qualitative or quantitative thresholds may vary from one jurisdiction to another. The scrutiny of new methodologies and criteria is carried out on an international basis and, in the case of methodologies significant enough to go before the Credit Policy Board, by senior analysts drawn from all of the agency's major analytical groups.

Additionally, Fitch operates a central group – the Credit Policy Group (CPG), headed by the Chief Credit Officer – which has a cross-sector mandate to review the performance of the agency's ratings. This performance review includes both quantitative measures, such as default and transition statistics and timeliness of response to events, and qualitative measures. Ad hoc reviews of individual transactions are carried out by the CPG based on price movements in the issuer's debt or equity instruments, news-flow or other market indicators.

Fitch also has a compliance examination group that conducts a compliance audit program designed continually to assess Fitch's compliance with the Code of Conduct and other established policies, procedures and controls with respect to Fitch's credit ratings and related activities. This group reports to Fitch's Chief Compliance Officer.

Appendix A: Credit Rating Process Flow Chart[2]



[2] Provided for illustrative purposes; timing and order of certain steps may vary

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Inside the Ratings:

What Credit Ratings Mean

August 2007

Fitch's credit ratings provide an independent, timely and prospective opinion on the creditworthiness of an entity or transaction. Fitch has built a reputation for insightful research and analytical excellence and has developed many different rating scales to address creditworthiness and other areas of relative financial strength. These include credit ratings using the traditional 'AAA' scale, first introduced by John Knowles Fitch in 1924. Fitch has since added Individual (financial strength) and Support ratings for banks, Insurer Financial Strength (IFS) ratings for insurance companies, Recovery Ratings and Distressed Recovery ratings for securities, asset manager ratings, managed fund volatility ratings and National scale ratings. This report will focus primarily on the traditional international long-term credit ratings of the 'AAA' scale – the scale with the broadest usage and the highest profile within the international capital markets.

This report is subject to the complete definitions of our ratings, set forth on our free public website, www.fitchratings.com, as well as the disclaimers with respect to ratings set forth in our Code of Conduct, also available on our website.

› What Do Credit Ratings Mean?

Fitch's credit ratings provide an opinion on the relative ability of an entity or transaction to meet financial commitments such as interest payments, repayment of principal, insurance claims or counterparty obligations. Credit ratings are used by investors as an indication of the likelihood of receiving their money back in accordance with the terms on which they invested. Fitch's credit ratings cover the global spectrum of corporate, sovereign (including supranational and sub-national), bank, insurance, municipal and other public finance entities, and the securities or other obligations they issue, as well as structured finance securities backed by receivables or other assets.

The rating scale is traditionally divided into two sections, "investment grade" and "speculative grade". "Investment grade" ratings (International Long-Term: 'AAA' to 'BBB-' (BBB minus), Short-Term: 'F1+' to 'F3') indicate relatively low to moderate credit risk. "Speculative grade" categories (International Long-Term: 'BB+' to 'D'; Short-Term: 'B' to 'D') signal either a higher level of credit risk or that a default has already occurred. Credit ratings express risk in relative rank order, which is to say they are ordinal measures of credit risk. Thus, they should be seen as broadly consistent indicators of relative vulnerability, rather than predictive indicators of actual, cardinal default rates. Obligations that are highly-rated have lower credit risk than lower-rated obligations, but the individual ratings themselves are not intended to be predictive of a cardinal frequency of default or a percentage expected loss.

Given the profound effect that economic cycles may have on cardinal default experience, and the differing economic cycles that sectors and regions may face, entities or issues which carry the same rating will be of broadly comparable, but not necessarily identical, credit quality[1]. Studies of default experience nonetheless provide users with both long-term and short-term average default experiences as a guideline indication.

[1] Excludes the US public or municipal finance debt market. Fitch's ratings on US public finance debt securities measure credit quality relative only to other US public finance debt securities. Default rates of most Fitch-rated US public finance debt securities have historically been significantly lower, and are expected to continue to be significantly lower, than other debt instruments rated comparably by Fitch.

Defining Creditworthiness

Credit ratings can apply both to entities and to individual obligations, and can be broadly separated into two types.

1. Ratings Which Address Relative Likelihood of Default ("First Dollar of Loss")

Corporate, bank, insurance and sovereign issuers are typically assigned Issuer Default Ratings (IDRs), which express creditworthiness in terms of relative measures of default likelihood.

Structured finance ratings are typically assigned to an individual security or tranche in a transaction, and not to an issuer. Ratings in structured finance primarily reflect the relative probability of default of the rated liability[2], and not its loss severity given a default, although loss severity on underlying *assets* is incorporated in the analysis.

2. Ratings Combining Relative Default Likelihood and Loss Severity

Individual securities or obligations of a corporate or sovereign issuer, in contrast, are rated on the long-term scale taking into consideration *both* the relative likelihood of default and the recovery given default of that liability. As a result, individual securities of entities, such as corporations, are assigned ratings higher, lower, or the same as that entity's issuer rating or IDR. The difference between issuer and security rating reflects expectations of the relative recovery prospects for each class of obligation. At the lower end of the ratings scale, Fitch now additionally publishes explicit Recovery Ratings in many cases to complement issuer and issue ratings.

	Corporate & Sovereign Finance	Structured Finance
Issuer	Rating covers Default	-
Issue	Rating covers Default/Loss Severity	Rating covers Default[2]

Foreign and Local Currency Ratings

International credit ratings relate to either foreign currency or local currency commitments and, in both cases, assess the capacity to meet these commitments using a globally applicable scale. As such, both foreign currency and local currency international ratings are internationally comparable assessments.

The local currency international rating measures the likelihood of repayment in the currency of the jurisdiction in which the issuer is domiciled and hence does not take account of the possibility that it will not be possible to convert local currency into foreign currency, or make transfers between sovereign jurisdictions (transfer and convertibility risk).

Foreign currency ratings additionally consider the profile of the issuer or note *after* taking into account transfer and convertibility risk. This risk is usually communicated for different countries by the Country Ceiling, which 'caps' the ratings of most, though not all, issuers within a given country.

[2] At the distressed level, elements of loss severity may be incorporated in structured finance bond ratings in the 'B' and 'C' categories

Loss Severity – How and When is it Included?

Loss severity (using an assessment of recovery given default) is included in instrument ratings in three significant ways.

Corporate Bond Ratings
Corporate issuer ratings (Issuer Default Ratings or "IDRs") reflect a relative likelihood of default. For the separate ratings of corporate bonds, loss severity is used to notch obligations relative to that issuer's IDR. A bond with average recovery given default expectations will be rated at the same level as the issuer's rating. A bond with notably above-average recovery given default expectations will be notched up from the IDR. A bond with notably below-average recovery given default expectations will be notched down from the IDR.

Structured Finance Bond Ratings
Structured finance bond ratings generally only reflect a relative likelihood of default (or "first dollar of loss"). However, to ascertain the likelihood of a default, loss severity of the underlying assets is typically analysed. For example, in analysing a portfolio of residential mortgages, both the default likelihoods and recovery prospects of individual mortgages will be considered, as both affect the cash flows available to the securitisation structure's bondholders. However, the rating of the bonds issued against this portfolio generally only consider the relative likelihood that cash flows jointly available from performing and liquidated mortgages support the relevant tranche of the securitisation, and prevent a default, and not the loss severity on that tranche if it does default.

Dedicated Recovery Ratings (Low Speculative Grade only)
As default and loss severity are two very different considerations, Fitch has pioneered additional, separate rating scales to represent 'recovery given default.' These ratings – 'RR1'-'RR6' for corporate and sovereign obligations and 'DR1'-'DR6' for structured obligations – relate to relative "bands" of potential loss severity. Introduced in 2005 and currently assigned to individual obligations at the lower end of speculative grade, Fitch will consider in future the appropriateness of extending the use of these loss severity ratings further up the ratings scale.

› Application of Rating Watch and Rating Outlook

Rating Watches and Rating Outlooks are mutually exclusive and have different meanings and purposes. There is no single test which can separate the two concepts, although one guiding principle is that a Watch should be applied in any case where a rating cannot be affirmed at its current level.

Rating Watch

Rating Watches indicate that there is a heightened probability of a rating change and the likely direction of such a change. These are designated as "Positive", indicating a potential upgrade, "Negative", for a potential downgrade, or "Evolving", if ratings may be raised, lowered or maintained. However, ratings that are not on Rating Watch can be upgraded or downgraded without being placed on Rating Watch first if circumstances warrant such an action.

A Rating Watch is typically event-driven and, as such, it is generally resolved over a relatively short period. The event driving the Watch may be either anticipated or have already occurred, but in both cases, the exact rating implications remain undetermined. The Watch period is typically used to gather further information and/or subject the information to further analysis. Additionally, a Watch may be used where the rating implications are already clear, but where a triggering event (e.g. shareholder or regulatory approval) exists. The Watch will typically extend to cover the period until the triggering event is resolved, or its outcome is predictable with a high enough degree of certainty to permit resolution of the Watch. Rating Watches can be employed by all analytical groups and are applied to the ratings of individual entities and/or individual instruments.

Rating Outlook

Rating Outlooks indicate the direction a rating is likely to move over a one- to two-year period. They reflect financial or other trends that have not yet reached the level that would trigger a rating action, but which may do so if such trends continue. The majority of Outlooks are generally Stable, which is consistent with the historical migration experience of ratings over a one- to two-year period. Positive or Negative rating Outlooks do not imply that a rating change is inevitable and, similarly, ratings with Stable Outlooks can be upgraded or downgraded without a prior revision to the Outlook if circumstances warrant such an action. Occasionally, where the fundamental trend has strong, conflicting elements of both positive and negative, the Rating Outlook may be described as Evolving.

Outlooks are currently applied to issuer ratings in corporate finance (including sovereigns, industrials, utilities, banks and insurance companies) and public finance outside the United States, issue ratings in public finance in the United States, to certain issues in project finance, to Insurer Financial Strength ratings, issuer and/or issue ratings in a number of national rating scales, and to the ratings of selected structured finance transactions.

Deciding to Assign a Watch rather than Change the Outlook

Timing is informative but not critical to the choice of a Watch rather than an Outlook. A discrete event which is largely clear and the terms of which are defined, but which will not happen for more than six months – such as a lengthy regulatory approval process – would nonetheless likely see ratings placed on Watch rather than a revision to the Outlook. An Outlook revision may, however, be deemed more appropriate where a series of potential event risks has been identified, none of which individually warrants a Watch but which cumulatively indicate heightened probability of a rating change. A revision to the Outlook may also be appropriate where a specific event has been identified, but where the conditions and implications of that event are largely unclear and subject to high execution risk over an extended period – for example a proposed, but politically controversial, privatisation.

› Cyclicality of Ratings and Rating Time Horizons

Fitch's traditional credit ratings are designed as "through-the-cycle" assessments. As such, they aim to react to fundamental changes in an issuer or transaction profile, and not temporary changes in condition. Fundamental changes could include relative issuer performance that falls above or below Fitch's original expectations in a sustained manner, a move towards deeper, longer cycles for a given industry, or a change in the operating environment based upon a fundamental increase or decrease in systemic risk.

Cyclicality will nonetheless have a profound impact on actual default rates. As a result, default rates often vary widely for a given rating category between any two given years. Pro-cyclical ratings that followed the cycle and tracked anticipated percentage default frequencies for each category, although they would produce results that are closer to cardinal default experience, would also display substantially more volatility than is the case for Fitch's traditional ratings. In turn this would reduce the ability of ratings to communicate relative changes in creditworthiness between two issuers, above and beyond cyclical developments affecting all issuers.

What Does a 'AAA' Rating Mean?

'AAA' ratings are defined as denoting "*the lowest expectation of credit risk*", further defined as an "*exceptionally strong capacity for payment of financial commitments*." As at June 30, 2007, 'AAA' obligors represented only 1% of Fitch's corporate and financial institution coverage. The absolute universe of 'AAA' ratings has however grown as structured finance issuance has grown. 'AAA' ratings are much more common for structured finance transactions (60% of outstanding ratings at June 30, 2007) due to the ability to "tranche" securities into various layers. A target rating level can usually be achieved through the amount of subordination, or "credit enhancement" created. In a tranching structure, the so-called equity layer represents the first loss position, and typically only after it is exhausted will each successive tranche potentially be exposed to loss. Thus, even with a high risk pool of assets, a senior layer can be sized with sufficient credit enhancement below it to absorb losses (i.e. equity, subordinated and/or mezzanine tranches) to create a security commensurate with a 'AAA' rating.

Crucially, for corporate and bank issuer ratings, and for structured finance instrument ratings, the 'AAA' rating refers to relative likelihood of default. It does *not* opine as to expected recovery given a default, or to relative market pricing or market liquidity. Investor assumptions regarding the characteristics of a 'AAA' rating other than relative default likelihood essentially derive from historical features associated with 'AAA' obligors and their obligations. While not included in Fitch's rating analysis, 'AAA'-rated debt is often assumed to have low loss severity rates and very high market liquidity – a logical assumption for highly-rated corporates, banks and sovereigns, as well as for many traditional structured finance instruments.

The fixed income market has, however, now expanded to include structured finance instruments which combine extremely low relative default likelihood, consistent with the 'AAA' rating, with the potential for either non-negligible levels of loss severity (e.g. through multiple tranching at the 'AAA' level), or with only limited liquidity (e.g. through bespoke construction). Thus traditional investor assumptions 'beyond the rating' regarding the characteristics of a 'AAA'-rated instrument may no longer be valid in all cases. Investors and other rating users should be aware of these developments when compiling and operating guidelines which incorporate ratings.

Rating Time Horizon

While ratings are attached to issuers without a formal time limit, and to transactions for the full maturity of the obligation, the analysis behind the ratings is based on assumptions today which may change as time passes, and is thus subject to a time horizon.

Ratings in the corporate and public finance sectors relate to entities that usually have no finite lifespan or immutable operating boundaries. As such, the ratings are subject to a wider array of exogenous and event-driven risks than is the case for structured finance. Corporate and public finance ratings are generally referred to as having a time horizon of 3-5 years, this being the period of greatest visibility for an entity's prospects.

That said, corporate and public finance ratings will incorporate some elements that are potentially very short-term in nature, such as liquidity position or crisis management performance, as well as some risk elements that have a much longer-term impact, such as potential technological obsolescence or exposure to long-cycle volatility. So, while the rating horizon is often referred to as 3-5 years for such entities, the ratings can reflect considerations that are unlikely to occur within the next five years but which are likely to occur in the longer run, if these are believed to present a material threat, or support, for the entity concerned. Equally, they may be driven by events of a much shorter-term nature, particularly where these affect issuer-specific or systemic liquidity problems.

For structured finance, the rating horizon is generally recognised as being the legal maturity of the note. However, a range of shorter- and longer-term considerations similar to those noted above for corporate and public finance issuers apply also to structured finance ratings, as the environment in which the instrument exists, and the transaction's own performance, can change over time.

› Treatment of Default

Default is typically defined by Fitch as one of the following:

- Failure of an obligor to make payment of principal and/or interest in accordance with the terms of any financial obligation;
- The bankruptcy filing, administration, receivership, liquidation or other winding-up or cessation of business of an obligor; or
- The distressed or other coercive exchange of an obligation, where creditors were offered securities with diminished structural or economic terms compared with the existing obligation.

As a legal matter, Fitch does not 'declare' a default on any obligation. Default, of both the obligations of entities and structured finance transactions, is determined by reference to the terms of the relevant documentation and is typically 'declared' by the trustee or another representative of the creditors. Fitch will assign default ratings where it has reasonably determined that payment has not been made on an obligation in accordance with the requirements of the obligation's documentation, and also where it believes that default ratings consistent with Fitch's definition of default are the most appropriate ratings to assign.

Ratings at Default

For IDRs or other issuer ratings, the threshold default event at which an issuer rating is lowered to 'D' will be that of the obligations, non-payment of which would generally best represent the uncured financial failure of that entity, most usually its senior debt obligations. Where the issuer has defaulted on some, but not all, of its financial obligations the IDR or issuer rating will generally be lowered to 'RD' (Restricted Default).

Where Fitch believes that a default has occurred for a corporate finance or sovereign issuer, only the issuer will be rated 'D' or 'RD'. Defaulted and distressed corporate obligations are not taken to 'D' on the international scale, but are rated along the continuum of 'B' to 'C' rating categories, depending upon their recovery prospects and other relevant characteristics. Fitch may choose to maintain an issuer's ratings once an entity or instrument has defaulted, but generally ratings are withdrawn once 30 days have elapsed from the assignment of a default rating.

In the case of structured finance transactions, where analysis indicates that an instrument is irrevocably impaired such that it is not expected to pay interest and/or principal in full in accordance with the terms of the obligation's documentation during the life of the transaction, but where no actual payment default in accordance with the terms of the documentation is imminent, the obligation may also be rated in the 'B' to 'C' categories, and will be assigned a Distressed Recovery ("DR") rating.

Default ratings are not assigned prospectively. Within this context, non-payment on an instrument that contains a deferral feature or grace period will not be considered a default until after the expiration of the deferral period (if any) or grace period. Deferrals in accordance with documentation will generally not represent a default, particularly in structured finance. The impact of deferral on ratings will depend on the circumstances surrounding the deferral. If the deferral is viewed as temporary for a corporate issuer, for example, then both IDR and affected issue rating may be unaffected, reflecting the expectation of a quick return to performing status. Conversely, if the deferral is viewed as the result of sustained deterioration in creditworthiness, any relevant IDR and issue rating will likely see negative pressure. In all cases, however, the deferred instrument, however, will not be rated as a defaulted bond until any deferral period and subsequent grace period have expired.

Default Experience

Default studies measure the actual level of default experienced at each rating level over one- and multiple-year horizons. Fitch uses default studies to assess whether the primary component of credit risk, the likelihood of default, is being appropriately rank-ordered by Fitch's rating scale on a relative basis. That is, default studies show whether issuers and/or securities rated 'AAA' have, in aggregate, defaulted less frequently than those rated 'AA' and so on, and whether this relationship has held over time and through the cycle.

Fitch does not generally rate to a specific probability of default and fully expects variations in default rates depending on economic and credit conditions. Indeed, default rates for each rating category are expected to worsen in difficult economic times and improve in good times. Nonetheless, the general pattern of higher default rates with each movement down the rating scale ('AAA' to 'AA' and so on) should consistently hold for each analytical sector. In particular, speculative grade ratings as a whole should experience substantially higher default rates than investment grade ratings as a whole.

Rating committees only use these historical default statistics as an abstract source of reference during their deliberations. As mentioned above, Fitch does not typically rate to specific default probabilities. Historic default rates are used as the basis for inputs into certain rating tools, such as the VECTOR models which are used by Fitch's structured products and structured finance groups. In this context, the rates are used to help assess relative creditworthiness between underlying components of the transaction only, and the use of these models is additionally subject to a qualitative committee overlay.

Comparability of Ratings across Sectors

It is Fitch's aim that creditworthiness should be broadly comparable by category across all major sectors of debt (with the exception of US Public or Municipal Finance, as mentioned above). For any given point in time or observation period, market conditions, regional factors and sector-specific influences may nonetheless cause issuers or obligations with a given rating in one sector to have different actual default or migration experience than issuers or obligations with the same rating in another sector.

This is an inevitable consequence of the combination of the rarity of default events, a "through-the-cycle" approach to ratings, and Fitch's goal of providing opinions to the fullest possible range of asset classes in all regions. Default is generally a low frequency event. Additionally this frequency exhibits high volatility across the economic cycle. The pool of ratings covered by an agency is also highly dynamic. As not all issuers in a given sector or region receive ratings simultaneously, coverage levels and concentrations may influence statistics. Methodologies are regularly revised in light of experience and new asset classes, with different rating migration characteristics, join the rated universe each year.

As an example of differing performance statistics, there have been more instances of multi-notch rating changes in structured relative to corporate finance, which can be attributed to the nature of structured transactions. As the latter typically involve fixed pools of assets whose performance expectations once realised are less fluid than corporate transactions, rating changes due to improving or deteriorating credit quality have a higher propensity to be multi-notch. In contrast, a company under duress typically has greater latitude in dealing with its circumstances, for example by seeking additional funding or selling non-core assets. This type of flexibility often contributes to more gradated rating changes on the corporate side than on the structured side.

As a result, although ultimate default rates are comparable across the major asset classes, actual default and migration experience will typically vary between sectors and regions within those asset classes. Over the very long-term, Fitch anticipates that actual default experiences will likely converge between sub-classes, as coverage levels and time series expand to support this analysis. Fitch will continue to monitor and publish research which looks at its rating performance in this context.

Broader Rating Considerations

A wide range of factors will feed into the determination of any rating, from cash generation, balance sheet or asset pool analysis to a review of the wider economic and financial outlook for the entity or transaction under consideration. A number of important factors can be incorporated to a greater or lesser extent – examples of how these factors may be included or excluded include:

- **Corporate Governance:** Fitch will typically combine external feedback on an entity's corporate governance with internal views formed by Fitch analysts from recent management actions, ownership and any interaction with management to form an opinion on an entity's corporate governance practices and the competence of the entity's management.

- **Tax and Legal Issues:** The analysis supporting a Fitch rating is generally conducted on the basis of the existing tax and legal regimes. However, clear pending changes in the tax or legal regime may be addressed on a case by case basis and commented on in the rating commentary and any supporting research reports. Where an existing or proposed tax affects a rating, assumptions may be made about the future rate of that tax in formulating stress tests. In the case of structured finance ratings, Fitch's analysis of the legal regime is based on the opinions and advice provided by transaction counsel. Fitch's legal staff or external counsel typically review these opinions to understand the extent to which legal risk may affect our analysis of the issuer/issuance, and thus our rating; but Fitch does not review legal opinions on behalf of investors or any other party.

The legal analysis performed by Fitch is not designed to supplant or replace that performed by transaction counsel, but is instead undertaken simply to understand the legal analysis provided by transaction counsel. The legal analysis therefore has a similar relationship to the transaction legal opinion as Fitch's financial analysis of a corporate debt issuer has to that issuer's audited financial statements.

› **Issue-Related Market Risk**: In assigning ratings to specific obligations of an issuer, Fitch takes into consideration the likely impact that market volatility will have on that issuer's ability to meet their obligations. However, Fitch distinguishes between:

- market risks that impact the issuer's ability to meet an obligation, which typically figure in the rating determination (e.g. exposure to commodity prices), and

- market risks that determine the nature or amount of the obligation regardless of the creditworthiness of the issuer (e.g. linkage to an index in an index-linked bond issued by a bank), which typically do not figure in the rating determination.

Where market risks are a determinant of creditworthiness, they are taken into consideration. Where this distinction is not clear or where a structured finance transaction is primarily designed to transfer a pure market risk, such as stock index risk or foreign exchange risk, to investors, the rating committee will apply the appropriate methodology, and elements of market risk considered in the analysis will be disclosed in Fitch's rating commentaries.

› **Event Risk:** Ratings provide an opinion based on assumptions, which cover many areas of an issuer's profile. Over time, such assumptions can change as events unfold. While ratings are forward-looking, many forms of event risk (e.g. merger & acquisition activity, fraud, natural disasters, etc) cannot practically be captured in an issuer's rating. As a result, event risks often cannot drive rating changes until they occur.

With regard to corporate bond ratings, covenant provisions within the relevant documentation can limit the financial impact of event risk on some (though not all) investors in an issuer's bonds. However, the complex interplay of investor behaviour and formal triggers required for such covenants to be effective means that generally they provide little benefit in corporate bond rating terms.

Ratings benefit can be achieved in project or special-purpose financings. For structured finance transactions, structural features are designed to insulate investors more effectively from event risk, mainly corporate strategy and investment risk, and as a result provide more tangible risk limitation. However, as event risk still affects underlying assets, the insulation is not complete, and structured finance ratings may also be subject to revisions based on event risk.

Other Limitations

In all cases, and as specified in our Code of Conduct, ratings are based on information obtained directly from issuers, underwriters, their experts and other sources that Fitch believes to be reliable. Fitch does not audit or verify the truth or accuracy of such information, and has undertaken no obligation to audit or verify such information, or to perform any other kind of investigative diligence into the accuracy or completeness of such information. This reflects Fitch's role, which is limited to gathering and analysing a variety of financial, industry, market and economic information, synthesising that information, and publishing independent, credible assessments of the creditworthiness of securities and issuers, thereby providing a convenient way for investors to judge the credit quality of various alternative investment options.

While the rating process in structured finance is an iterative one, Fitch does not structure transactions. Arrangers are able to combine and re-combine assets to achieve a target rating for the liability. Models published by Fitch to make its methodologies transparent are also sometimes used by arrangers/originators in their initial review of the assets that they wish to include in a transaction. The decision of which assets to allocate, and which ratings to target, nonetheless remains entirely that of the arranger or originator. The rating committee will not propose alternative assets to include in a transaction, suggest alternative rating levels that may be targeted, or develop alternative legal structures that could be applied.

In the surveillance process, while transactions may incorporate a rating confirmation feature, this does not constitute an endorsement by the agency of any change that may occur in the transaction. As such, Fitch does not 'require', 'approve', or 'endorse' issuer behaviour. This reflects the nature of the particular role filled by rating agencies. Any rating review is simply an observation of relative creditworthiness, and Fitch is indifferent to the level of any rating assigned.

Ratings are not a recommendation or suggestion, directly or indirectly, to buy, sell, make or hold any investment, loan or security or to undertake any investment strategy with respect to any investment, loan or security or any issuer. Ratings do not comment on the adequacy of market price, the suitability of any investment, loan or security for a particular investor (including without limitation, any accounting and/or regulatory treatment), or the tax-exempt nature or taxability of payments made in respect of any investment, loan or security.

The above information relates to credit ratings on the international scale as of 1 August 2007. Separate considerations may apply to non-credit ratings, quantitative ratings and market-implied ratings or national scale ratings applied in certain jurisdictions.

Frequently Asked Questions

"Does a credit rating communicate a percentage default expectation?"

No, credit ratings are an ordinal ranking. They communicate *relative* strength or vulnerability to credit events, rather than any absolute measure. Default experience has shown, historically, that default frequencies were higher in the 'BBB' category than in the 'A' category, higher in the 'B' category than in the 'BB' category, and so on. But the individual rating categories do not represent a predicted percentage or range of percentages.

"Does the rating address expected loss?"

Expected loss incorporates both likelihood of default and loss severity. Credit ratings primarily look at the first of the components rather than the second. The above table on page 2 and sidebar on page 3 indicate which of Fitch's scales look at both relative default likelihood and relative loss severity. Essentially, only the ratings of corporate, bank, insurer and sovereign *obligations* incorporate a consideration of both at all parts of the 'AAA'-scale.

However, default risk and loss severity are not perfectly correlated. A bond can thus combine low default risk with high loss severity. In combining these two potentially diverging considerations, the existing market convention is that credit ratings on corporate bonds give primacy to default risk rather than overall loss risk. The impact of loss severity on any corporate instrument's rating is therefore effectively limited to a maximum number of notches above or below that instrument's relative likelihood of experiencing a default.

Consequently, the choice to give primacy to default risk in the rating of individual instruments for corporate and sovereign finance limits the ability to provide an entirely ordinal ranking based upon expected loss. For their part, structured finance ratings only incorporate both elements in the rating of a bond when that bond is at a distressed level, similarly preventing an entirely ordinal representation of expected loss.

As markets evolve, Fitch will continue to review this approach for appropriateness.

"Should an investor expect two bonds with the same ratings to be comparable in all ways?"

The performance of bonds, in terms of credit risk and market risk, may vary substantially even where they have similar ratings. In terms of credit risk, as noted above, ratings can combine low default risk (which is represented in the rating), with high loss severity (which is either excluded from or reflected to a lesser degree in the credit rating). Migration characteristics vary between sectors, depending on the influence of factors such as event risk (for corporate finance) and seasoning (mainly for structured finance).

Pricing of the two instruments may also differ markedly for a variety of reasons. While the underlying credit risk attached to an instrument is one factor, it can frequently be outweighed by other considerations, including market supply/demand dynamics and liquidity. Pricing may be artificially suppressed or boosted depending on the amount of market demand for a particular type of asset, or for fixed income assets in general. New instruments issued by an issuer or sector with a large amount of paper already in the market may be more or less liquid as a result. Small or largely amortised issuances may be less liquid in the secondary market, as may larger issuances made by small/lesser known obligors.

"How does Fitch use models in deriving ratings?"

Models are used within Fitch to test significant volumes of data against assumptions determined by Fitch's analysts. For example, models are constructed which contain Fitch analysts' assumptions on mortgage or corporate bond recovery rates, or likely payment patterns on trade receivables. As such, the assumptions used in such models are typically reviewed by a committee as part of their construction.

In addition, with the exception of explicitly quantitative ratings[3], all credit ratings are subject to an individual committee process. The committee examines the output of the model as one factor, assessed against additional qualitative criteria, including structural, legal, operational and other risks.

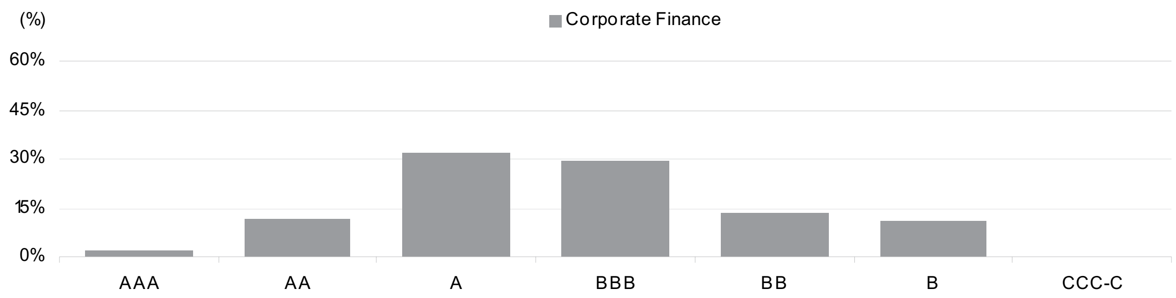
"What is the balance between quantitative and qualitative analysis?"

Fitch's ratings employ both qualitative and quantitative factors, other than in explicitly quantitative scales disclosed as such. While Fitch does not record, *ex ante,* particular weightings between qualitative and quantitative considerations, *ex post* analysis of corporate finance ratings indicates that over a cycle both are responsible in roughly equal measure for rating changes made to outstanding ratings.

[3] e.g. Quantitative-Insurer Financial Strength (or "Q-IFS") scores

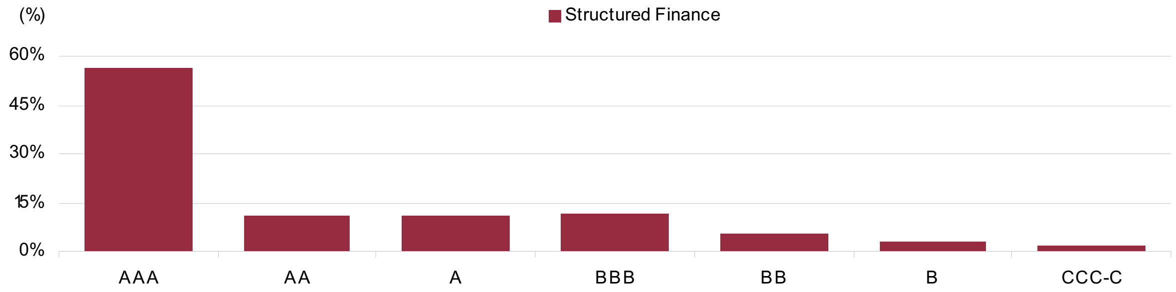
Rating Distribution

Global Rating Distribution
Corporate Finance Issuer ratings



Source: Fitch Ratings, as at June 30th, 2007

Global Rating Distribution
Structured Finance Instrument Ratings



Source: Fitch Ratings, as at June 30th, 2007

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Fitch, Inc.

Application for Registration as a Nationally Recognized Statistical Rating Organization (NRSRO)

Exhibit 4. Organizational Structure

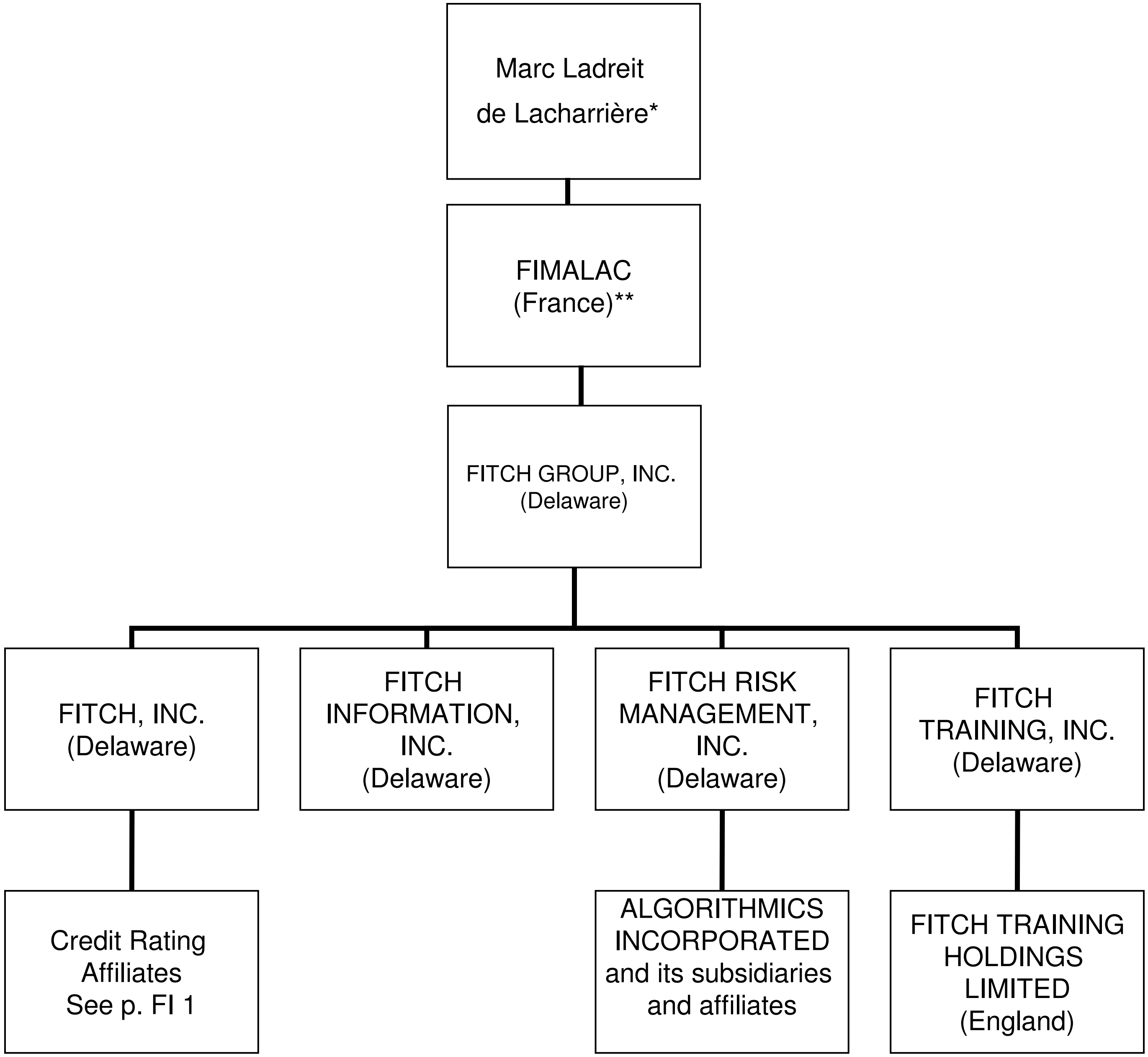
Please see two charts attached, reflecting the management structure and material affiliates of Applicant.

FitchRatings

Corporate Structure

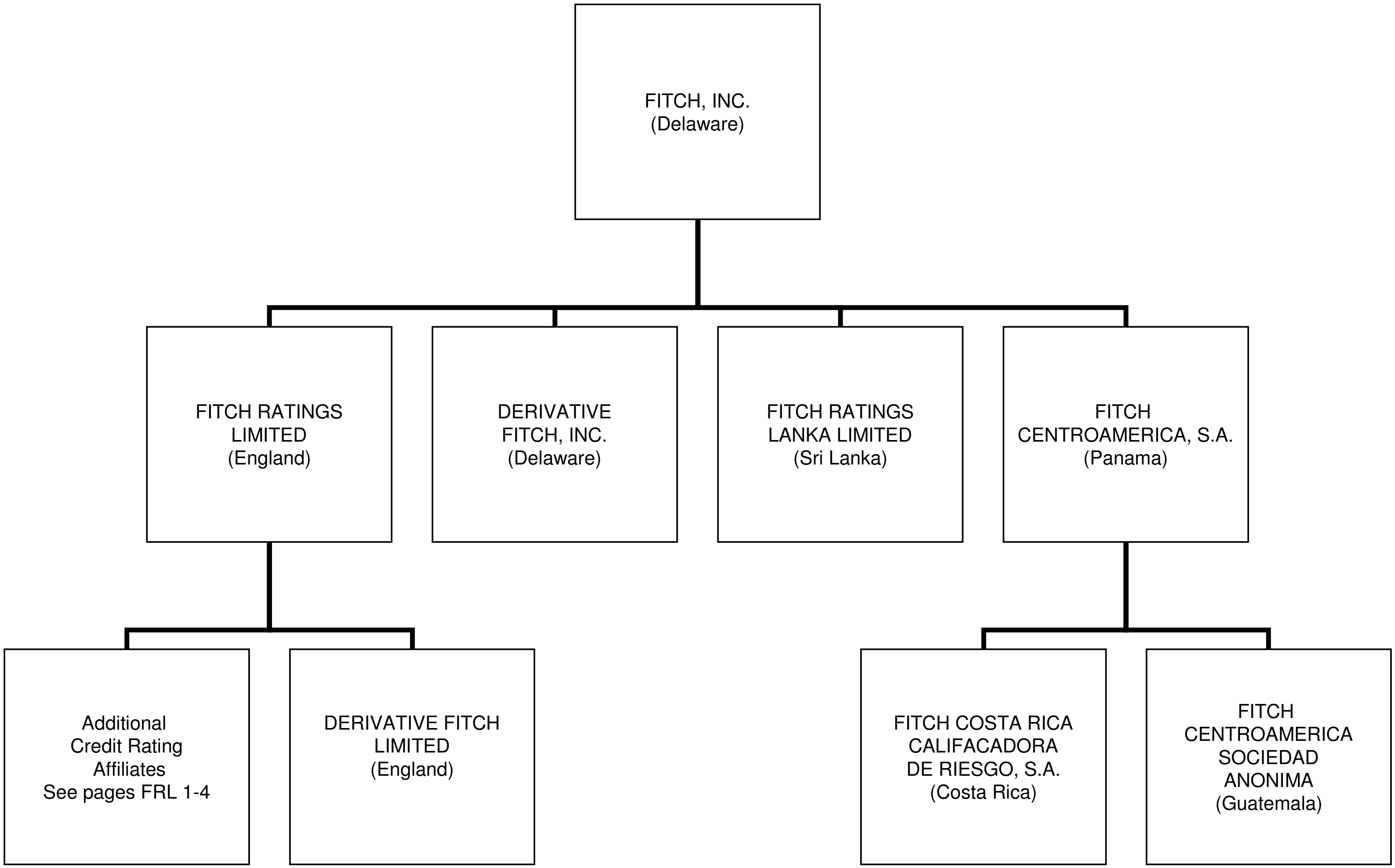
- **Stephen W. Joynt**
  President and CEO
  - **Paul Taylor, GMD**
    Global Corporate Finance
    Global Public Finance
    - Global Banks
    - Global Insurance and Financial Guarantors
    - Sovereigns
    - EMEA and Asia Corporates
    - U.S. Corporates
    - U.S. Public Finance
    - Latin America Operations
  - **Gloria Aviotti, GMD**
    Global Structured Finance
    Derivative Fitch
    - U.S. Structured Finance
    - EMEA Structured Finance
    - Asia Structured Finance
    - Quantitative Financial Research
    - Derivative Fitch
  - **Robert Grossman, GMD**
    Chief Credit Officer
    Credit Policy/Regulations
    - Credit Policy - Americas
    - Credit Policy - EMEA/Asia
    - Credit Market Research
  - **Peter G. Jordan, GMD**
    Global Business Development
    - Structured Finance Business Development
    - U.S. Corporate Finance Business Development
    - EMEA Corporate Finance Business Development
    - Asia Business Development
    - Product Development
    - Product Sales
    - Corporate Communications
  - **Charles D. Brown**
    General Counsel
    Chief Compliance Officer
  - **David B. Kennedy, CFO**
  - **Bernard de Lattre, GMD**
    London, EMEA, Asia Operations
  - **Nancy Stroker, GMD**
    Global Strategy, Administration, and Investor Relations
  - **Michael Dissinger, GMD**
    Information Technology and Information Services

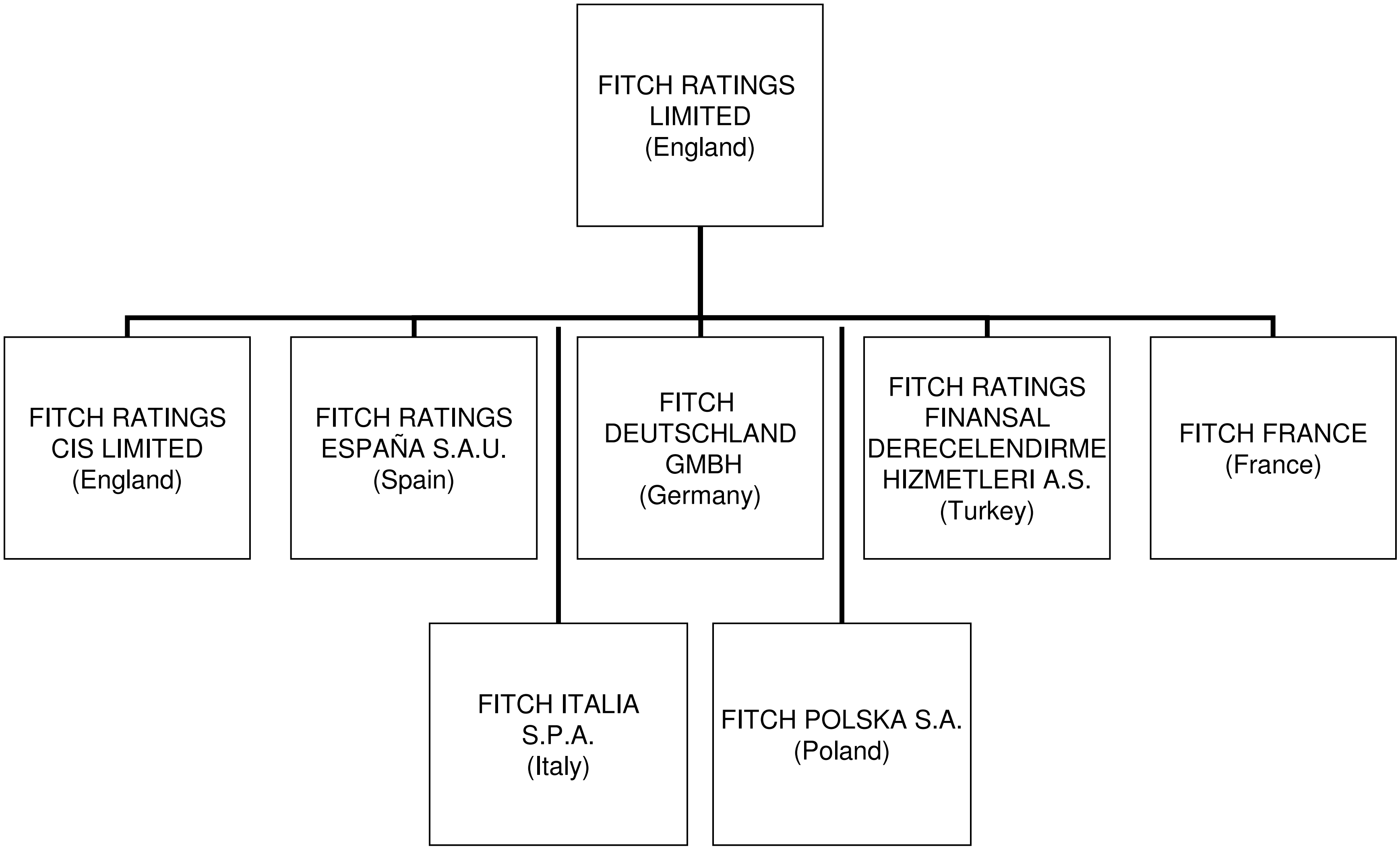
Last Modified Jun-18-2007



* Mr. de Lacharrière holds an indirect controlling interest in Fimalac.

** Fimalac holds an 80% equity interest in Fitch Group, Inc. The Hearst Corporation holds the remaining 20% interest.


FITCH, INC.
(Delaware)
FITCH RATINGS
LIMITED
(England)
DERIVATIVE
FITCH, INC.
(Delaware)
FITCH RATINGS
LANKA LIMITED
(Sri Lanka)
FITCH
CENTROAMERICA, S.A.
(Panama)
Additional
Credit Rating
Affiliates
See pages FRL 1-4
DERIVATIVE FITCH
LIMITED
(England)
FITCH COSTA RICA
CALIFACADORA
DE RIESGO, S.A.
(Costa Rica)
FITCH
CENTROAMERICA
SOCIEDAD
ANONIMA
(Guatemala)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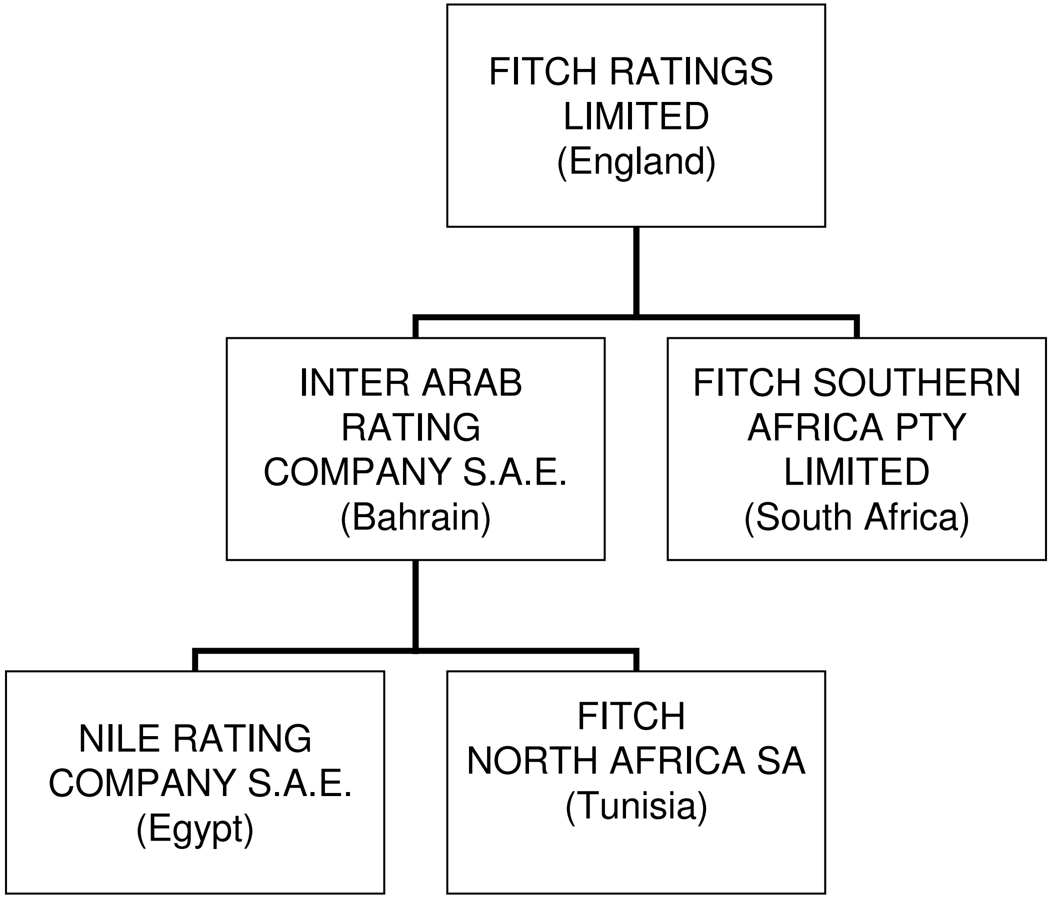
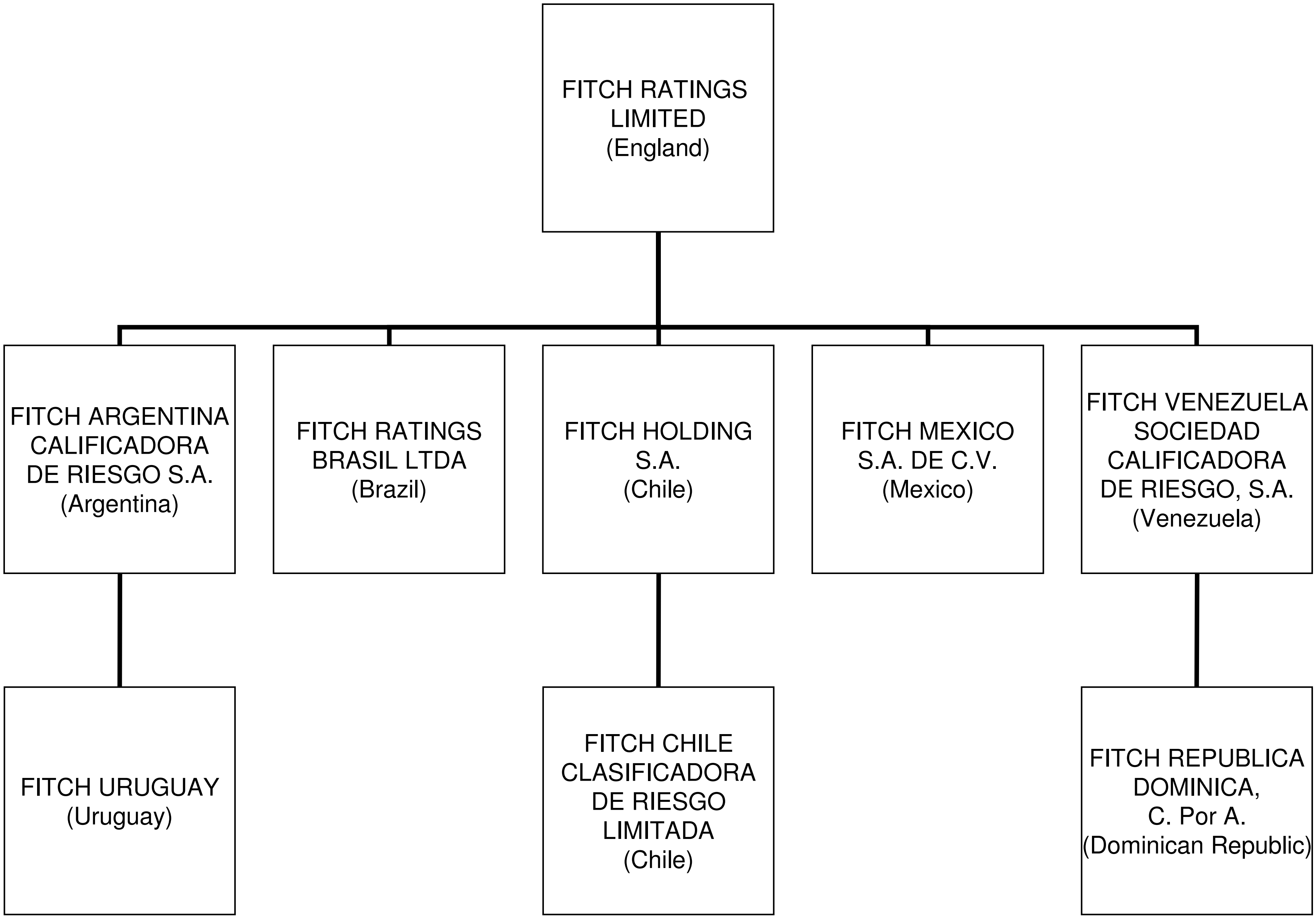
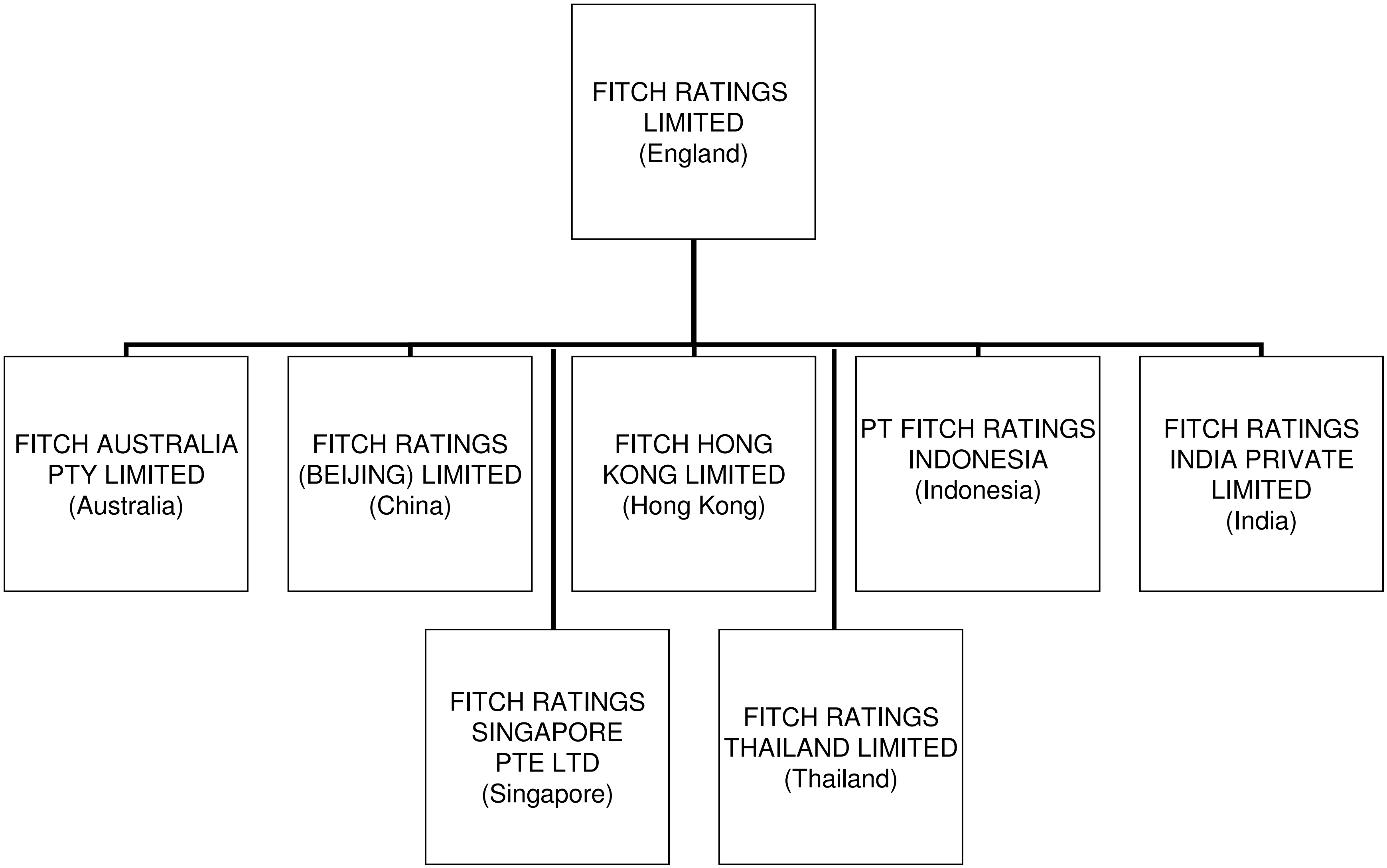
FITCH RATINGS CIS LIMITED (England)
FITCH RATINGS ESPAÑA S.A.U. (Spain)
FITCH DEUTSCHLAND GMBH (Germany)
FITCH RATINGS FINANSAL DERECELENDIRME HIZMETLERI A.S. (Turkey)
FITCH FRANCE (France)
FITCH ITALIA S.P.A. (Italy)
FITCH POLSKA S.A. (Poland)


FITCH RATINGS LIMITED (England)
INTER ARAB RATING COMPANY S.A.E. (Bahrain)
FITCH SOUTHERN AFRICA PTY LIMITED (South Africa)
NILE RATING COMPANY S.A.E. (Egypt)
FITCH NORTH AFRICA SA (Tunisia)


FITCH RATINGS LIMITED (England)
FITCH ARGENTINA CALIFICADORA DE RIESGO S.A. (Argentina)
FITCH RATINGS BRASIL LTDA (Brazil)
FITCH HOLDING S.A. (Chile)
FITCH MEXICO S.A. DE C.V. (Mexico)
FITCH VENEZUELA SOCIEDAD CALIFICADORA DE RIESGO, S.A. (Venezuela)
FITCH URUGUAY (Uruguay)
FITCH CHILE CLASIFICADORA DE RIESGO LIMITADA (Chile)
FITCH REPUBLICA DOMINICA, C. Por A. (Dominican Republic)

FRL 3


FITCH RATINGS LIMITED (England)
FITCH AUSTRALIA PTY LIMITED (Australia)
FITCH RATINGS (BEIJING) LIMITED (China)
FITCH HONG KONG LIMITED (Hong Kong)
PT FITCH RATINGS INDONESIA (Indonesia)
FITCH RATINGS INDIA PRIVATE LIMITED (India)
FITCH RATINGS SINGAPORE PTE LTD (Singapore)
FITCH RATINGS THAILAND LIMITED (Thailand)

Fitch, Inc.

Application for Registrations as a
Nationally Recognized Statistical Rating Organization ("NRSRO")

Exhibit 8. Certain Information about the Applicant's Credit Analysts.

The total number of credit analysts (including supervisors):	1120
*The total number of credit analyst supervisors:	302

*Credit analyst supervisors are defined as those analysts holding a title of Senior Director or above. Quorum requirements for ratings committees require at least one analyst with a title of Senior Director or above to be present.

See attached for a general description of minimum qualifications required of credit analysts and credit analyst supervisors.

Core Competencies – Analytic Functions

<table>
<tr><th>Level</th><th>Knowledge and Expertise</th><th>Knowledge Application/Problem Solving</th><th>Management</th><th>Communication</th><th>Quality Service</th><th>Leadership & Initiative</th></tr>
<tr>
<td>Analyst</td>
<td>Demonstrates:
Proficiency with the technical/functional aspects of the supporting role (e.g. modeling, Excel, proprietary systems & other technical tools)
Ability to think analytically (i.e. critically review and question information presented; consider impact/implications as appropriate)
Ability to read, comprehend and interpret relevant quantitative data
Ability to identify key analytical factors, issues and concerns
Basic understanding of the principal areas of rating methodology and, as appropriate, ability to assume some rating and/or review responsibility for certain credits and/or transactions with direct supervision (e.g. preparing rating packages, press releases, attending management meetings, modeling, document review)
"Independent" thought and contributes new ideas
Skills that include attention to detail, accuracy, follow -through, and efficient work processes/procedures
Awareness and understanding of Analyst Reference Guide, Code of Conduct, email retention policy & other relevant compliance policies, as applicable to role
Exhibits intellectual curiosity
Minimum experience – 0-2 years
Minimum Education – BA/BS Degree</td>
<td>Demonstrates:
Ability to analyze routine/basic analytical/business problems in a timely, orderly and insightful manner with diminishing supervision
Ability to use logical and sound judgment to address relevant issues or problems and arrive at appropriate solutions
Good judgment in knowing when to ask for assistance and when to act independently
Ability to independently support the analytical team by providing and enhancing information that the more senior analysts need
Understanding of how role contributes and relates to broader analytical/business efforts
Ability to "think like an analyst"
Strives to implement innovative ideas to improve efficiency of the group, team and/or department
Exhibits:
Confidence in analytical abilities
Improved presentation skills in committees
Beginning to make meaningful contributions at internal (and external, as appropriate) meetings</td>
<td>Demonstrates:
Ability to coordinate with colleagues at all levels to ensure smooth and efficient work processes/procedures
Awareness of when to seek clarification of needs and expectations when unsure
Increasing ability to anticipate problems/issues and take action to prevent/ minimize their impact
Ability to evaluate a course of action to improve process/product/service outcomes
Flexibility and willingness to consider alternatives; has a positive attitude toward change
Ability to manage self, time and schedule efficiently
Ability to manage multiple priorities
Exhibits discretion with respect to sensitive information.</td>
<td>Demonstrates:
Ability to present ideas and facts effectively verbally and in writing
Ability to use effective questioning and listening skills in order to identify parties' needs and expectations
Awareness of importance of keeping parties informed of progress toward goals
Professional demeanor and potential to effectively represent Fitch to outside constituencies
Ability to gather and give relevant information to others in a timely manner
Ability to work in small groups/teams effectively through active participation and contribution</td>
<td>Demonstrates:
Ability to develop and maintain effective professional working relationships with internal and external parties
Appreciation of importance of responding to the needs of internal and external parties in a timely, appropriate and professional manner (with diminishing supervision)
Awareness of the importance of consistently delivering quality products/services to internal and external parties
Ability to gain confidence and respect of co-workers, including peers and superiors</td>
<td>Demonstrates:
Ability to perform analytical (coverage) work with supervision of more senior staff in the department
Ability to share information, skills, and expertise as appropriate and work in collaborative manner
Ability to perform support work with diminishing supervision of more senior staff
Ability to value group achievement over individual recognition
Ability to take responsibility for actions, projects and assignments and consistently follow through to completion
Basic understanding of company vision and related initiatives
Exhibits ability & willingness to contribute to an enthusiastic, positive work environment
Work is performed under the direct supervision of more senior staff in the department
As appropriate, demonstrate ability to mentor/train more junior</td>
</tr>
<tr>
<td>Associate Director
(all of the above plus)</td>
<td>Demonstrates:
Full understanding of the principal areas of rating methodology and is able to identify key analytical factors, issues and concerns
Ability to evaluate relevant analytical/business problems in a timely, orderly and insightful manner
Ability to understand, evaluate and form opinions about relevant analytical issues
Ability to contribute uniquely to team goals with insightful research
Ability to take full rating responsibility for certain credits and/or transactions as a primary analyst with diminishing supervision
Adheres to Analyst Reference Guide, Code of Conduct, email retention policy & other relevant compliance policies, as applicable to role
Minimum Experience – 3-5 years
Minimum Education – BA/BS Degree</td>
<td>Demonstrates:
Ability to regularly contribute analytical insights to rating committees
Knowledge of industry, market, company, and issuer developments in the business unit
Serves as lead author on select research publications (e.g. industry publications, presale reports) and contributes to the development of others (e.g. criteria, methodology, special reports)</td>
<td>Demonstrates:
Ability to manage assigned projects or functions in the department within defined parameters
Ability to meet established deadlines
Ability to participate in internal and/or external meetings relevant to his/her area of expertise and is cognizant of serving as Fitch's representative to the market</td>
<td>Demonstrates ability to share opinions in a straightforward manner, even when it's difficult or unpopular to do so</td>
<td>Demonstrates:
Ability to develop strong working relationships with internal or external parties
Appreciation of importance of responding to the needs of internal and external parties in a timely, appropriate and professional manner (with limited supervision)</td>
<td>Demonstrates ability to:
Work independently with minimal management supervision
Oversee the work of others on assigned projects (in some cases)
Provide guidance and support to more junior level staff in the function, as required by manager or supervisor
Beginning to demonstrate ability to constructively challenge the usual way of seeing/doing things while championing creativity/ingenuity at all levels</td>
</tr>
</table>

Core Competencies – Analytic Functions

Level	Knowledge and Expertise	Knowledge Application/Problem Solving	Management	Communication	Quality Service	Leadership & Initiative
Director *(all of the above plus)*	Demonstrates: • Strong expertise and analytical knowledge of sector including a basic understanding of key credits • Prioritization, decision making, and conflict resolution skills • Ability to analyze and coordinate complex projects requiring in-depth knowledge of financial, specific technology and general business principles and a solid understanding of how the project, product or functional team impacts the organization. • Full knowledge of industry, market, company, and issuer developments in the business unit • Ability to lead a management review meeting in a credible and professional manner • In-depth knowledge of the organizational procedures & policies, products & services, including Analyst Reference Guide, Code of Conduct, & email retention policy. • Ability to contribute uniquely to team goals with insightful research • Ability to be responsible for full portfolio of credits/transactions • Strong interpersonal, analytical, problem solving, negotiating, and organizational skills • Possesses advanced skills in financial analysis and an understanding of accounting concepts (Corporates/FI) • Minimum Experience – 5-8 years • Minimum Education – BA/BS Degree	Demonstrates ability to: • Ensure consistent application of analytical techniques and findings on project or functional area; identifies, modifies, and develops appropriate analytical techniques and methods of identifying patterns and opportunities. • Distinguish between "nice to know" and "need to know" information • Apply analytical conclusions or implications across a broad array of issuers • Differentiate among symptoms, causes, and alternative solutions; develops appropriate frameworks and/or tools to address the issues • Exercise business and technical judgment to make timely, sound decisions consistent with the objectives of the position	Demonstrates ability to: • Define scope and business objectives within outlined framework • Coordinate & ensure project /team/product success • Bring leadership, perspective, and consistency of approach and quality assurance to assigned projects or functions • Make decisions that impact productivity, efficiency, and overall client service levels. • Manage increasing number of internal and external relationships. • Demonstrates ability to coach and develop staff for current and future responsibilities	Demonstrates ability to: • Communicate effectively with all levels inside and outside the organization verbally and in writing. • Facilitate communication and ensures team buy-in /understanding of project objectives, scope changes etc. • Effectively represent Fitch to outside constituencies	Demonstrates: • A high sense of urgency in managing all issues related to assigned issuers • Ability to participate in execution of strategic initiatives.	Demonstrates: • Leadership qualities and ability to provide general direction to more junior staff • Ability to lead projects that significantly impact the business • Ability to work independently without supervision • Ability to constructively challenge the usual way of seeing/doing things while championing creativity/ingenuity at all levels • Ability to consistently apply macro credit opinions across all sector issuers • Ability to handle a diverse workload and meet established deadlines • Exhibits qualities of role model for others in the group • May participate in the selection and hiring process in his/her group or department.
Sr. Director *(all of the above plus)*	Demonstrates: • Unquestioned expertise and analytical knowledge of sector, and increasingly seen as an "analytical leader" within the group • Strong knowledge of the broad debt and credit field • Strong interpersonal, analytical, problem solving, negotiation, influencing, prioritization, decision making, conflict management and strategic planning skills. • Ability to adjust from detailed to strategic view • Ability to take leading role in rating committee process • Ability to take leading role in criteria and methodology development • Business acumen • Regularly assumes committee chairman role • Promotes adherence to and knowledge of Fitch's policies and procedures including Analyst Reference Guide, Code of Conduct & email retention policy to the analytical group • Minimum Experience – 8-12 years • Minimum Education – BA/BS Degree	Demonstrates: • Ability to ensure consistent and effective application of criteria and current research in rating process • Ability to identify, modify, and guide use of appropriate analytical techniques • Ability to exercise credit and business judgment to make timely, sound and innovative decisions • Flexibility to adapt to rapidly changing business requirements and multiple short and long-term projects • Ability to write industry original research • Significant and consistent contributor to committees/projects outside direct product area, including criteria, credit policy etc.	Demonstrates ability to: • Delegate effectively • Set direction of and lead day to day activities for one or more transactions, projects, services, or functional area within the organization. • Influence strategic business decisions related to products or functional areas • Make meaningful contributions to the development of the department's business objectives • Serve as a role model in understanding and supporting overall department objectives, policies and procedures • Demonstrates strong 'people management' skills	Demonstrates: • Excellent oral and written communications skills • Ability to effectively represent Fitch to outside constituencies in all situations	Demonstrates ability to: • Establish and maintain effective internal and external relationships and gain their trust and respect • Create climate and set the tone for building relationships within organization • Define and implement strategic initiatives for enhancing internal/external client relationships and building loyalty • Viewed by outside parties (issuers, investors, bankers, media) as an industry expert.	Demonstrates ability to: • Lead and direct staff, as well as projects or functional areas that significantly impact business. • Develop strategies for achieving company vision • Create appropriate objectives for self and team and embrace role as steward for company vision • Analyzes department workload and recommend increases or decreases in staff • Identify talent and make effective hiring decisions • Serve as role model and mentor to staff as well as other members of the organization • Delegate work effectively by giving staff appropriate levels of responsibility and independence • Demonstrates leadership skills and ability to manage and lead functional and cross-functional teams.

Core Competencies – Analytic Functions

Level	Knowledge and Expertise	Knowledge Application/Problem Solving	Management	Communication	Quality Service	Leadership & Initiative
Managing Director *(all of the above plus)*	Demonstrates: • Business acumen through more senior and responsible professional experience in the broader capital markets • Analytical leadership • Expert skills and strong professional reputation in functional area of expertise • Ability to set & m aintain strategic direction for the business/group • Active participation in business development activities • Strong adherence to and knowledge of Fitch's policies and procedures including Analyst Reference Guide, Code of Conduct & email retention policy • Proven ability to manage a major portion of a department with significant autonomy through demonstrated knowledge, consistent good judgment and high level of organization. • Individual may be recognized as industry expert within coverage area(s) • Exhibits broad knowledge of the credit and debt industry • Able to serves as a resource for Fitch activities/staff from outside of business unit • Minimum Experience – 12 + • Minimum Education – BA/BS Degree	Demonstrates ability to: • Assess trends & patterns and identify & execute systemic solutions that enhance organizational growth • Position Fitch products (research, technology etc.) effectively to maintain/enhance market position • Structure organization to be nimble and responsive allowing for swift implementation and change in direction • Create an environment that fosters and rewards innovation within functional, project or product team • Ensure that department objectives fit within the strategic direction of the organization • Solve complex problems • Exhibits foresight and understanding of changing competitive landscape	Demonstrates: • Ability to positively impact profitability and strategic direction of the organization as a whole. • A high level of organizational skills • Ability to inspires confidence of staff • Exhibits approachability & fairness in all dealings	• Demonstrates ability to articulate emerging constituent needs & opportunities to build business and deploy resources to seize it	Demonstrates ability to: • Identify new opportunities to broaden and deepen current constituent relationships through product, service or consulting options with individual constituent or market segments • Maintain strong presence outside of the organization at industry events, investor events and conference calls • Exhibits sound business acumen and strategic agility in order to prioritize and balance constituent needs, internal resources and business opportunities. • Possesses very strong and respected presence outside of Fitch at industry events, investor events and conference calls.	Demonstrates: • Very strong management skills and leadership • Ability to direct all internal activities & initiatives within the department • Ability to assess department workload and secure appropriate resources. • Ability to train, develop, motivate and serve as role model for staff • Ability to create and reinforce an inspiring vision and sense of purpose, and motivate entire units of organization • Ability to create strong morale and team spirit, foster open dialogue within unit, and provide strategic guidance • Ability to works collaboratively with cross-functional peers • Willingness and ability to make difficult decisions • Respected by peers, subordinates, junior staff members and executive management. • An unquestioned team player who puts department and staff needs ahead of personal needs. • Oversee hiring decisions for function

FitchRatings
KNOW YOUR RISK

Structured Finance

Credit Market Research

Fitch Ratings 1991–2006 U.S. Structured Finance Transition Study

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Key Findings

- The upgrade-to-downgrade ratio for Fitch-rated U.S. structured finance securities was 5.3:1 in 2006, an improvement from the 3.2:1 ratio in 2005.
- Fitch U.S. structured finance tranches exhibited either a high degree of stability or improvement in 2006, with 98% of credits maintaining their rating or upgraded.
- The year's strong results extended to each of the major structured asset classes with upgrades readily exceeding downgrades across CMBS, RMBS, ABS, and CDOs. Upgrades were particularly strong in CMBS, which saw the number of positive rating actions double from prior-year levels.

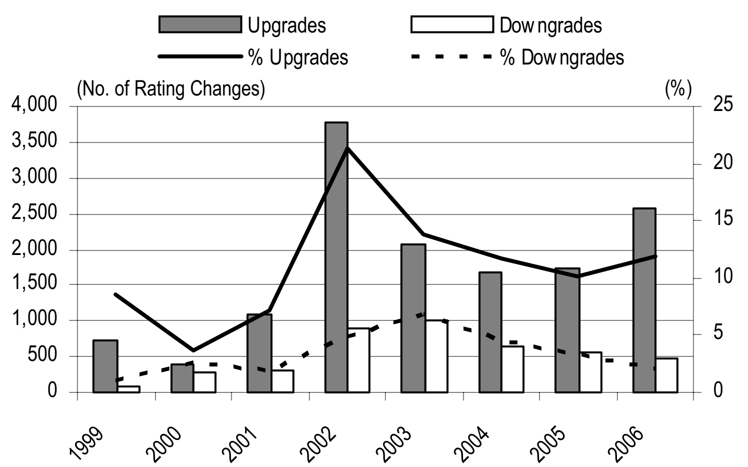
April 27, 2007

■ Summary

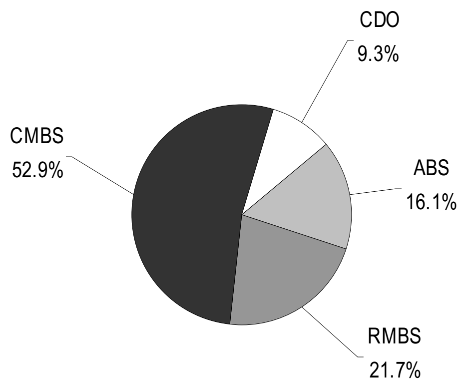
This new study offers a fresh look at the rating performance of U.S. structured finance securities rated by Fitch Ratings in 2006 and over the historical period from 1991–2006. Rating transitions are examined across the major structured finance sectors, including asset-backed securities (ABS), residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), and collateralized debt obligations (CDOs), which are now rated and monitored by Derivative Fitch, a wholly owned subsidiary of Fitch. Unless otherwise noted, manufactured housing (MH) and subprime mortgage migration rates are included in ABS.

In 2006, all eyes remained focused on the U.S. housing market and the consumer. While the housing market began to cool, the U.S. economy continued to perform well, with real gross domestic product growth of 3.3%. Unemployment remained at a low level (4.6%) and energy prices eased, providing a boost to corporate and consumer spending. However, with the slowdown in home price appreciation, the subprime mortgage sector experienced additional stress. But strength across other consumer and commercial assets contributed to another strong year for structured finance. The upgrade-to-downgrade ratio for Fitch-rated structured finance tranches improved to 5.3 to one in 2006, compared with 3.2 to one in 2005. The improvement in the ratio was attributed to both an increase in the number of upgrades, as well as a decrease in the number of downgrades. Structured finance upgrades totaled 2,571 in 2006, up from 1,744 for the prior year, while downgrades totaled 482 in 2006, compared with 549 in 2005.

Structured Finance Rating Changes

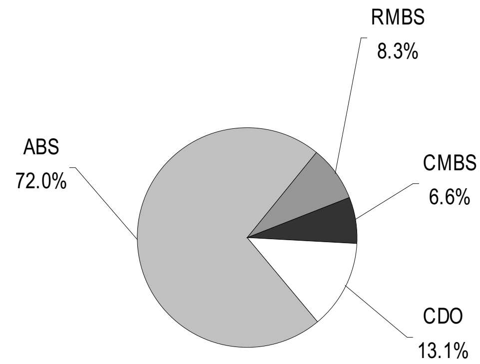


Fitch 2006 Upgrades by Sector



ABS -Asset-backed securities.
RMBS -Residential mortgage-backed securities.
CMBS-Commercial mortgage-backed securities.
CDO -Collateralized debt obligations.

Fitch 2006 Downgrades by Sector



ABS -Asset-backed securities.
RMBS -Residential mortgage-backed securities.
CMBS-Commercial mortgage-backed securities.
CDO -Collateralized debt obligations.

In general, rating performance improved across each of the structured finance sectors in 2006. In fact, almost every major structured finance sector (i.e. ABS, CDOs, CMBS, and RMBS) reported increases in upgrades and declines in downgrades. The one exception was the RMBS sector, which recorded a decline in the number of both upgrades and downgrades. However, given the drop in refinancing activity, this was not surprising and is a continuation of a trend that started in 2005, when interest rates started to climb higher.

For the second consecutive year, the CMBS sector drove the upgrade totals, and continued to do so in an even more pronounced fashion than in 2005. The CMBS sector accounted for more than one-half of total 2006 upgrades, a measurable increase from the 38.8% reported in 2005. CMBS upgrades reached 1,360 in 2006, more than double prior-year levels. The huge spike in positive rating actions was due to the increase in defeasance activity, which replaced underlying collateral with government securities, hence significantly boosting the credit quality of CMBS bonds. In addition, strong collateral performance and seasoning were also contributing factors.

Despite the decline in RMBS upgrades year-over-year, the RMBS sector still ranked second in upgrades, representing 21.7% of the total upgrades in 2006. A further testament to the overall positive performance in the RMBS sector was the degree to which positive rating actions continued to outnumber negative rating actions. For example there were 557 upgrades in 2006, compared with only 40 downgrades.

Not far behind in upgrades was the ABS sector, which recorded 415 positive rating actions for the year. Indeed, upgrades finally outpaced downgrades by a margin of 1.2 to one, a scenario not seen in more than a decade. The most notable development was the improvement in the MH sector, which experienced not only a decline in downgrades but also an increase in upgrades. In addition, the student loan sector also posted robust rating performance, with upgrades nearly double prior-year levels. Meanwhile, the subprime mortgage sector saw measurable increases in both positive and negative rating actions.

Similar to the other structured finance sectors, the CDO sector also recorded strong rating performance. Upgrades increased by 68.3%, totaling 239 in 2006, compared with 142 in 2005. Likewise, downgrades were nearly cut in half, with 63 negative rating actions in 2006, down from the 94 recorded in 2005. The upgrade figures were overwhelmingly driven by structured finance CDOs (SF CDOs).

Highlights

- The rating performance of Fitch-rated structured finance securities remained positive in 2006, with nearly every major sector recording increases in upgrades and declines in downgrades. Upgrades increased by 47.5%, totaling 2,571 in 2006, compared with 1,744 in 2005. Meanwhile,

Fitch U.S. Structured Finance Ratings Upgrade/Downgrade Averages

(%)

	1991–2005		2005		2006	
	Downgrade	Upgrade	Downgrade	Upgrade	Downgrade	Upgrade
'AAA'	0.8	N.A.	0.4	N.A.	0.4	N.A.
'AA'	1.4	12.3	1.4	11.5	0.5	11.2
'A'	2.6	11.7	2.1	11.1	0.9	11.5
'BBB'	4.2	9.9	3.2	8.0	3.1	10.0
'BB'	5.2	12.1	5.3	10.3	3.8	13.2
'B'	7.5	9.4	7.9	7.8	6.0	10.3
'CCC'	41.6	1.5	44.4	0.0	30.3	13.1

N.A. – Not applicable.

downgrades declined to 482 in 2006, down from the 549 recorded in the prior year. In addition, the upgrade-to-downgrade ratio improved to 5.3 to one in 2006, compared with 3.2 to one in 2005.

- The rating stability of Fitch-rated structured finance securities remained unchanged in 2006, with 86% of credits maintaining their rating. The increased volatility resulting from the jump in upgrades was offset by the corresponding decline in downgrades. In 2006, 11.9% of Fitch structured finance ratings were upgraded, compared with 10.6% in 2005, while 2.2% of credits were downgraded, an improvement from the 3.3% recorded in 2005.
- For the second straight year, the CMBS sector accounted for the bulk of upgrades in 2006, representing more than one-half of the total. Defeasance, strong collateral performance and seasoning all contributed to the positive rating actions. CMBS upgrades continued to tower over downgrades by a disproportionate amount, with an upgrade-to-downgrade ratio of 42.5 to one in 2006.
- Not unexpectedly, the structured finance downgrades were concentrated in the subprime mortgage and MH categories, resulting in the ABS sector accounting for approximately 75% of the total downgrades. The subprime mortgage sector had 249 downgrades in 2006, an 83.1% increase over the 136 recorded in the prior year. While the MH sector posted the second largest number of negative rating actions, at 53, downgrades declined by more than one-half from prior-year levels, as collateral performance slowly improved in the asset class.
- Nonmortgage ABS continued to perform well in 2006, with 145 upgrades and just 43 downgrades. The student loan sector contributed to the upgrade total, with 55 positive rating actions in 2006. In addition, the auto loan and credit sectors also experienced positive rating migration, with 41 and 26 upgrades, respectively.
- Rating stability in the RMBS sector improved to 91.2% in 2006, as rating activity, both on the upside and downside, slowed. This compares with a stability rate of 86.0% in 2005. Prepayments continued their downward descent in 2006 as interest rates slowly increased. In addition, many loans that were prime candidates for refinancing had already been refinanced. As a result, credit enhancement levels did not rise as quickly as they did in prior years, which contributed to the slowdown in upgrades.
- The CDO sector continued to show improvement in 2006, as the number of upgrades increased by 68.3% to 239, and the number of downgrades declined by 33% to 63. The upgrades were predominantly from the SF CDO sector. Positive collateral performance, seasoning, and deleveraging of CDO liabilities all contributed to the upgrades.

One-Year U.S. Structured Finance Transition Matrix: 2006*

(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
'AAA'	99.61	0.33	0.04	0.02	0.00	0.00	0.00	0.00	100.00
'AA'	11.22	88.25	0.49	0.05	0.00	0.00	0.00	0.00	100.00
'A'	4.74	6.76	87.61	0.75	0.09	0.00	0.00	0.05	100.00
'BBB'	1.35	2.34	6.27	86.91	2.30	0.52	0.11	0.20	100.00
'BB'	0.24	0.47	2.26	10.19	83.07	2.50	0.47	0.80	100.00
'B'	0.37	0.00	0.22	1.26	8.41	83.71	2.68	3.35	100.00
'CCC'	0.00	0.00	0.00	0.00	0.82	12.30	56.56	30.33	100.00

*Includes asset-backed, residential mortgage-backed, commercial mortgage-backed, and collateralized debt obligation securities.

U.S. Structured Finance Transition Matrices: 1991—2006*

(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
Average Annual									
'AAA'	99.28	0.46	0.15	0.06	0.01	0.01	0.01	0.02	100.00
'AA'	12.13	86.58	0.78	0.25	0.11	0.05	0.01	0.09	100.00
'A'	3.82	7.82	86.08	1.42	0.38	0.23	0.07	0.18	100.00
'BBB'	1.03	2.91	5.97	86.12	1.80	1.16	0.37	0.64	100.00
'BB'	0.25	0.90	3.07	8.02	82.81	2.24	0.88	1.85	100.00
'B'	0.10	0.09	0.57	2.18	6.58	83.16	2.65	4.68	100.00
'CCC'	0.00	0.00	0.00	0.00	0.77	2.31	56.83	40.09	100.00
Average Two-Year									
'AAA'	98.37	0.83	0.33	0.16	0.11	0.08	0.05	0.08	100.00
'AA'	20.38	76.70	1.27	0.70	0.34	0.24	0.08	0.28	100.00
'A'	9.25	11.44	74.58	2.28	0.75	0.60	0.34	0.75	100.00
'BBB'	3.38	6.01	8.98	73.20	2.70	2.41	0.84	2.48	100.00
'BB'	0.97	2.53	5.92	12.30	69.07	2.77	1.51	4.94	100.00
'B'	0.24	0.43	1.85	4.68	10.72	68.29	3.17	10.63	100.00
'CCC'	0.00	0.00	0.00	0.00	0.95	3.26	36.96	58.83	100.00
Average Three-Year									
'AAA'	97.22	1.21	0.51	0.33	0.23	0.24	0.11	0.16	100.00
'AA'	26.12	69.28	1.52	1.01	0.54	0.55	0.21	0.76	100.00
'A'	13.88	13.27	65.36	2.74	1.10	1.19	0.58	1.90	100.00
'BBB'	6.04	7.92	10.45	61.97	3.57	2.77	1.22	6.06	100.00
'BB'	2.14	3.98	7.35	14.46	58.08	3.43	1.65	8.92	100.00
'B'	0.63	1.02	3.10	6.31	12.46	55.92	3.76	16.80	100.00
'CCC'	0.00	0.00	0.00	0.18	1.05	2.63	26.27	69.88	100.00

*Includes asset-backed, collateralized debt obligation, resident ial mortgage-backed, and commercial mortgage-backed securities.

■ Rating Activity Still Strongly Skewed to the Upside for U.S. Structured Finance in 2006

Fitch structured finance ratings continued their robust performance in 2006, as both upgrades increased and downgrades declined. The upgrade-to-downgrade ratio for Fitch structured finance ratings was 5.3 to one in 2006, an improvement from the 3.2 to one ratio in 2005. Upgrades increased by 47.4% in 2006, reaching 2,571, compared with 1,744 in 2005. Meanwhile downgrades also declined to 482 in 2006, down from the 549 recorded in 2005.

For the second straight year, the CMBS sector represented the majority of upgrades, accounting for 52.9% of the total positive rating actions in 2006. Defeasance was the main driver behind many of the upgrades. In addition, robust collateral performance and scheduled amortization also contributed to positive rating actions. Continuing a trend that began in 2003, the RMBS sector posted another decline in upgrades, as refinancings continued to fall. RMBS upgrades totaled 557 in 2006, a 14.4% drop from the 651 in 2005. Nonetheless, the sector still performed well, with upgrades outnumbering downgrades by a large margin, recording an upgrade-to-downgrade ratio of 13.9 to one in 2006. The ABS and CDO sectors both posted improvements in positive rating actions, with increases of 51.5% and 68.3%, respectively. The student loan, MH, and auto sectors all contributed to positive ABS rating performance. In addition, because the subprime sector experienced many negative and positive rating actions, it also contributed to ABS upgrade totals. Meanwhile, the commercial real estate (CRE) sector overwhelmingly drove CDO upgrades.

Not unexpectedly, downgrades were concentrated in the subordinate notes of subprime mortgage and MH transactions, resulting in the ABS sector accounting for three-quarters of the total structured finance negative rating actions. The subprime mortgage sector posted 249 downgrades in 2006, an 83.1% jump over the 136 recorded in 2005. While the MH sector still accounted for a major portion of total downgrades, negative rating actions did finally begin to abate in the much maligned sector, declining 53.5% to 53 in 2006.

On the nonmortgage ABS side, rating performance improved, with upgrades generally rising and downgrades declining. In particular, the student loan sector had a strong showing, with 55 upgrades in 2006, nearly double the 29 in 2005. The auto loan and credit card sectors also contributed to the positive rating actions, with 41 and 26, respectively. The

2006 Rating Distribution Within Structured Finance

(%)

	ABS	RMBS	CMBS	CDO	All SF
‘AAA’	33	43	12	12	100
‘AA’	52	30	12	7	100
‘A’	56	23	12	9	100
‘BBB’	54	22	15	9	100
‘BB’	27	37	27	9	100
‘B’	10	48	39	3	100
‘CCC’ to ‘C’	57	15	24	4	100
Total	44	31	16	9	100

ABS – Asset-backed securities. RMBS – Residential mortgage-backed securities. CMBS – Commercial mortgage-backed securities. CDO – Collateralized debt obligation.
SF – Structured finance.

2006 Rating Distribution Within Each Sector

(%)

	ABS	RMBS	CMBS	CDO	All SF
‘AAA’	17	31	17	31	23
‘AA’	22	18	14	16	19
‘A’	26	15	16	20	20
‘BBB’	26	15	20	22	21
‘BB’	6	12	17	9	10
‘B’	1	9	15	2	6
‘CCC’ to ‘C’	1	0	1	0	1
Total	100	100	100	100	100

ABS – Asset-backed securities. RMBS – Residential mortgage-backed securities. CMBS – Commercial mortgage-backed securities. CDO – Collateralized debt obligation.
SF – Structured finance.

sharpest decline in downgrades was seen in the franchise sector, which had only 13 negative rating actions in 2006, compared with 56 in 2005.

Meanwhile, the RMBS sector displayed higher levels of rating stability, with 91% of credits remaining unchanged in 2006, up from the 86% in 2005. The decrease in upgrades was certainly a factor, as prepayments continued to decline. However, in general, prime and Alt-A bonds performed well in 2006. There were 557 upgrades in 2006, compared with only 40 downgrades.

When viewed across the major rating categories, structured finance rating performance either generally improved or remained the same. For example, at the ‘AA’ and ‘A’ levels, approximately 11% improved in 2006, essentially unchanged from the 2005 upgrade rates. For ‘BBB’ credits, 10% of tranches were upgraded in 2006, compared with 8% in 2005. Increases in positive rating actions were more visible at the below-investment-grade level, with 13% of ‘BB’ and 10% of ‘B’ credits upgraded in 2006, compared with 10% and 8%, respectively, in 2005. However, the largest move was at the ‘CCC’ level, where 13% of tranches improved in 2006, compared with none in 2005.

In addition, the improvement in structured finance rating performance was also evident in a decline in negative rating volatility. Downgrade rates in 2006 either generally declined or remained the same when compared with 2005 levels. For example, at the ‘AAA’ and ‘BBB’ levels, negative rating volatility in 2006 was exactly the same as in 2005, with 0.4% and 3.0%, respectively, downgraded. Meanwhile, 0.5% of ‘AA’ and 0.9% of ‘A’ credits were downgraded in 2006, an

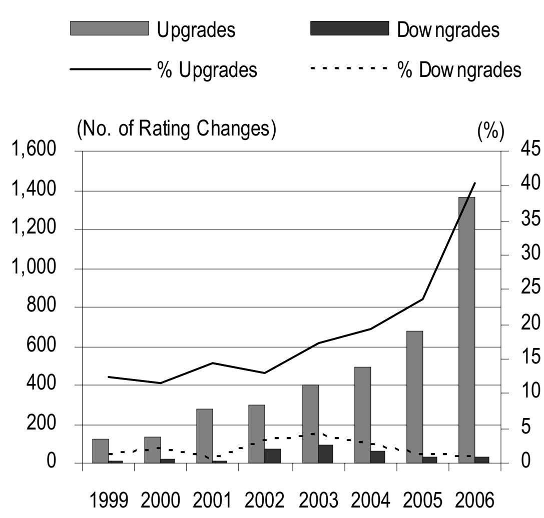
Average Annual Probability of Rating Either Remaining the Same or Being Upgraded: 1991–2006

(%)

	ABS	RMBS	CMBS	CDO*
‘AAA’	98.9	99.8	99.7	96.7
‘AA’	97.1	99.9	99.8	94.6
‘A’	96.1	99.8	99.5	93.1
‘BBB’	93.3	99.1	99.0	90.7
‘BB’	82.7	98.3	98.3	86.9
‘B’	66.6	96.5	95.8	80.1
‘CCC’	49.4	53.1	82.1	48.6

*Collateralized debt obligation (CDO) averages based on the 1995–2006 period. ABS – Asset-backed securities.
RMBS – Residential mortgage-backed securities. CMBS – Commercial mortgage-backed securities.

Commercial Mortgage-Backed Securities Rating Changes



Commercial Mortgage-Backed Securities One-Year Transition Matrix: 2006

(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	‘CCC’	‘CC’ and Below	Total
‘AAA’	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	55.04	44.96	0.00	0.00	0.00	0.00	0.00	0.00	100.00
‘A’	33.33	19.29	47.38	0.00	0.00	0.00	0.00	0.00	100.00
BBB’	8.41	13.27	20.06	58.11	0.15	0.00	0.00	0.00	100.00
BB’	0.35	1.41	6.50	25.13	65.73	0.70	0.00	0.18	100.00
B’	0.40	0.00	0.20	1.79	13.55	80.88	1.00	2.19	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	44.12	47.06	8.82	100.00

Commercial Mortgage-Backed Securities Transition Matrices: 1991—2006

(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	‘CCC’	‘CC’ and Below	Total
Average Annual									
‘AAA’	99.69	0.28	0.03	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	24.31	75.53	0.03	0.10	0.03	0.00	0.00	0.00	100.00
‘A’	8.56	12.55	78.39	0.37	0.14	0.00	0.00	0.00	100.00
BBB’	2.67	3.87	9.52	82.90	0.83	0.09	0.12	0.00	100.00
BB’	0.47	0.69	1.96	9.04	86.19	1.28	0.03	0.34	100.00
B’	0.26	0.07	0.22	0.73	5.03	89.50	2.15	2.04	100.00
‘CCC’	0.00	0.00	0.00	0.00	1.46	7.30	73.36	17.88	100.00
Average Two-Year									
‘AAA’	99.39	0.55	0.06	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	35.80	63.99	0.00	0.13	0.09	0.00	0.00	0.00	100.00
‘A’	17.33	15.42	66.37	0.55	0.33	0.00	0.00	0.00	100.00
BBB’	7.49	6.71	13.02	70.74	1.44	0.33	0.21	0.06	100.00
BB’	1.67	1.75	3.45	12.90	76.62	2.54	0.16	0.91	100.00
B’	0.55	0.23	0.83	1.66	7.44	79.86	3.93	5.50	100.00
‘CCC’	0.00	0.00	0.00	0.00	2.62	10.04	55.90	31.44	100.00
Average Three-Year									
‘AAA’	99.17	0.75	0.08	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	45.50	54.15	0.00	0.18	0.18	0.00	0.00	0.00	100.00
‘A’	24.84	18.09	55.94	0.68	0.39	0.00	0.00	0.05	100.00
BBB’	12.46	9.04	15.76	59.67	2.04	0.55	0.28	0.20	100.00
BB’	3.97	2.22	4.70	16.00	67.44	3.61	0.31	1.75	100.00
B’	1.44	0.66	1.08	2.04	8.88	69.95	5.64	10.32	100.00
‘CCC’	0.00	0.00	0.00	0.55	3.31	7.73	44.20	44.20	100.00

improvement from the 1.4% and 2.1% recorded in 2005. But again, the most measurable improvement was seen at the below-investment-grade level. For ‘BB’ tranches, 3.8% experienced negative rating volatility in 2006, compared with 5.3% in 2005. Similarly, 6.0% of ‘B’ and 30.3% of ‘CCC’ credits were downgraded in 2006, down from 7.9% and 44.4%, respectively, in 2005.

■ CMBS Upgrades Move Higher in 2006, Totaling 1,360

The CMBS sector continued with its torrid pace of upgrades, reporting a record 1,360 positive rating actions in 2006, fresh off the heels of the previous record-breaking 677 in 2005. Upgrades towered over downgrades by a significant amount, with an upgrade-to-downgrade ratio of 42.5 to one in 2006. There were only 32 downgrades last year, compared with 37 in the prior year.

The same factors that contributed to the record volume in 2005 persisted in 2006, although in greater magnitude. Defeasance, strong collateral performance, loan prepayments, and scheduled amortizations all contributed to the positive rating actions last year. However, defeasance was by far the overriding factor behind the build-up of credit enhancement levels, which prompted many of the Fitch upgrades. Defeasance is the process of replacing a mortgage on real estate with U.S. government obligations or other eligible securities as substitute collateral for a loan. The substitute collateral is sized to generate sufficient cash flow to match all debt service requirements of the loan. Defeasance has become a very cost-effective alternative for borrowers amidst the backdrop of rising real estate values and a relatively low interest rate environment.

CMBS upgrade activity in 2006 was overwhelmingly seen at the investment-grade level, with the ‘AA’ and

Asset-Backed Securities One-Year Transition Matrix: 2006*
(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
'AAA'	99.63	0.31	0.06	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	4.58	94.61	0.71	0.09	0.00	0.00	0.00	0.00	100.00
'A'	0.53	3.21	94.67	1.34	0.16	0.00	0.00	0.08	100.00
BBB'	0.00	0.20	2.30	92.47	3.66	0.81	0.20	0.36	100.00
BB'	0.00	0.00	0.36	1.08	89.19	5.41	1.26	2.70	100.00
B'	0.00	0.00	0.00	0.78	1.56	66.41	16.41	14.84	100.00
CCC'	0.00	0.00	0.00	0.00	0.00	0.00	60.32	39.68	100.00

*Includes home eqity and manufactured housing transactions.

'A' categories experiencing the highest percentages of upgrades, 55.0% and 52.6%, respectively. This represents a considerable improvement over average annual upgrades rates of 18.9% for 'AA' and 15.5% for 'A' credits reported during the 1991–2005 period. In 2006, 41.7% of 'BBB' tranches were upgraded, while 33.4% of 'BB' credits improved. The 'CCC' category also improved, with 44.1% of tranches upgraded in 2006.

■ 2007 CMBS Outlook

Fitch expects to see a continuation of the upgrade activity in 2007, albeit at a slower pace. However, upgrades are expected to outnumber downgrades by a large degree, with upgrades being primarily driven by collateral paydowns and defeasance of large loans. Meanwhile, downgrades are expected to occur in non-investment-grade tranches affected by adverse selection and deteriorating credit issues.

It is also worth noting that the 2006 vintage is particularly vulnerable to an economic downturn. Primary factors include a proliferation of high concentration volatile property types, including hotels, increased share of interest only (IO) loans, and aggressive underwriting practices. Moreover, Fitch expects these trends to continue in 2007, resulting in potentially increased volatility for this vintage as well.

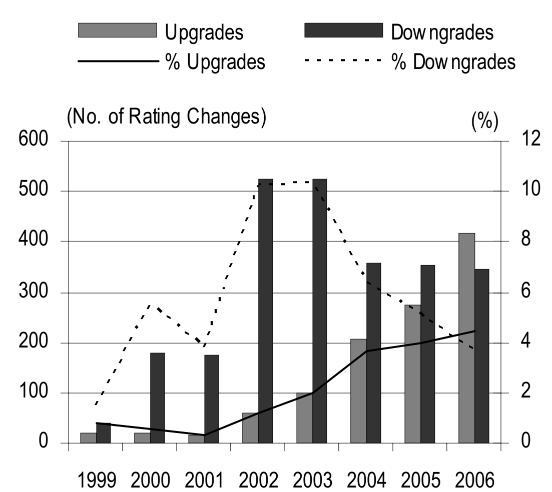
■ Upgrades Jump 51.5% in ABS Sector

The ABS sector continued to enjoy improved rating performance in 2006, as the number of upgrades increased sharply, while downgrade levels were almost flat. Upgrades jumped 51.5% to 415 in 2006, compared with 274 in 2005. Downgrades totaled 347 in 2006 slightly higher than the 342 reported in 2005. This led to a more favorable upgrade-to-downgrade ratio of 1.2 to one in 2006, up from the 0.80 to one in 2005.

In an interesting twist, the subprime mortgage sector not only accounted for the majority of downgrades, but also the bulk of upgrades. In 2006, there were 249 negative rating actions and 222 positive rating actions recorded in the sector. The downgrades were not unexpected, as the subprime mortgage sector has seen collateral deterioration in select transactions. The majority of upgrades in the sector were a reflection of strong collateral performance in some 2002–2003 transactions and built-up credit enhancement in some 2000–2001 transactions due to structural features that mitigated weak collateral performance. However, it should be noted that the sector's overall performance was quite stable, with 91.9% remaining unchanged in 2006. In addition, due to the sheer size of the subprime mortgage sector, rating movements can have a pronounced impact on overall ABS migration rates.

Meanwhile, the MH sector finally stabilized, as collateral performance and market fundamentals began to improve. Rising from negligible levels in

Asset-Backed Securities Rating Changes



Asset-Backed Securities Transition Matrices: 1991—2006*

(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
Average Annual									
'AAA'	98.86	0.66	0.26	0.09	0.03	0.01	0.03	0.06	100.00
'AA'	2.97	94.08	1.94	0.48	0.18	0.11	0.02	0.22	100.00
'A'	0.39	2.44	93.27	2.51	0.49	0.42	0.12	0.37	100.00
'BBB'	0.10	0.16	1.41	91.66	3.03	1.92	0.59	1.13	100.00
'BB'	0.05	0.32	0.27	2.07	80.05	6.76	2.93	7.57	100.00
'B'	0.10	0.00	0.10	0.20	0.88	65.36	10.30	23.06	100.00
'CCC'	0.00	0.00	0.00	0.00	0.29	0.00	49.14	50.57	100.00
Average Two-Year									
'AAA'	97.31	1.26	0.64	0.26	0.14	0.10	0.11	0.19	100.00
'AA'	4.85	87.76	3.43	1.61	0.70	0.63	0.24	0.77	100.00
'A'	1.27	4.08	86.07	4.24	1.13	1.12	0.64	1.46	100.00
'BBB'	0.21	0.58	2.28	82.07	4.44	4.24	1.43	4.75	100.00
'BB'	0.13	0.73	0.73	3.18	62.93	6.63	5.11	20.56	100.00
'B'	0.12	0.00	0.24	0.36	1.31	45.04	6.57	46.36	100.00
'CCC'	0.00	0.00	0.00	0.00	0.37	0.00	29.04	70.59	100.00
Average Three-Year									
'AAA'	95.25	1.79	1.03	0.63	0.28	0.37	0.23	0.43	100.00
'AA'	6.17	81.11	4.47	2.48	1.12	1.65	0.61	2.40	100.00
'A'	2.01	4.88	78.71	5.18	1.88	2.35	1.25	3.73	100.00
'BBB'	0.33	0.98	2.60	70.86	5.67	4.87	2.27	12.41	100.00
'BB'	0.18	1.18	0.72	2.44	47.96	7.51	5.16	34.84	100.00
'B'	0.15	0.00	0.29	0.00	2.05	33.82	5.12	58.57	100.00
'CCC'	0.00	0.00	0.00	0.00	0.00	0.00	15.69	84.31	100.00

*Includes home eqity and manufactured housing transactions.

2005, upgrades totaled 48 in 2006. Moreover, the improvement was also evidenced in the decline in negative rating actions, with downgrades dropping by more than one-half, to 56 in 2006. Nonetheless, the MH sector still ranked second in negative volatility, accounting for 16.1% of the total ABS downgrades in 2006.

Similar to MH, the franchise sector has also begun to stabilize. The frequency and severity of losses have finally begun to ease; however, the deals still remain under stress as much of their credit enhancement has been eroded. There were 13 downgrades in the franchise sector in 2006, a considerable improvement from the 56 downgrades in 2005.

The aircraft sector continued to be weighed down by escalating costs and increased losses. Negative rating actions were attributed to continued weakness in aircraft lease cash flow. In addition, the bankruptcy filings of both Delta Air Lines and Northwest Airlines also negatively affected the sector. The aircraft sector posted 19 downgrades, up from the 16 recorded in 2005.

On a more positive note, the student loan sector showed improvement, with 55 upgrades in 2006, compared with only 29 in 2005. Positive rating actions across Sallie Mae and Nelnet Inc. transactions contributed to the upgrade totals.

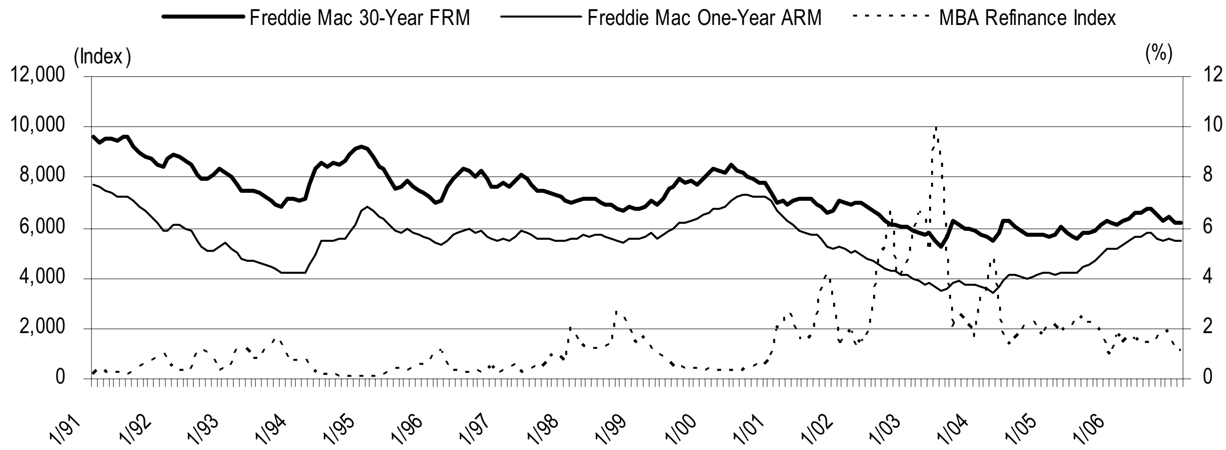
In general, upgrade rates increased when moving up the rating scale and downgrade rates increased when moving down the rating scale. For example, upgrades were the highest at the 'AA' level, where 4.6% of tranches migrated to 'AAA' in 2006. This was followed by 3.7% of 'A' and 2.5% of 'BBB' credits improving in 2006. Positive rating actions also

Average Annual Subprime Mortgage Transition Matrix: 1991—2006

(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
'AAA'	99.98	0.02	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	2.31	97.13	0.47	0.07	0.00	0.02	0.00	0.00	100.00
'A'	0.21	2.24	95.92	1.43	0.09	0.10	0.00	0.02	100.00
'BBB'	0.06	0.16	1.10	94.10	2.43	1.10	0.44	0.60	100.00
'BB'	0.09	0.09	0.00	0.84	88.54	4.66	1.68	4.10	100.00
'B'	0.00	0.00	0.22	0.00	1.34	75.89	7.37	15.18	100.00
'CCC'	0.00	0.00	0.00	0.00	0.00	0.00	55.83	44.17	100.00

MBA Refinance Index vs. Freddie Mac 30-Year FRM and One-Year FRM: 1991–2006



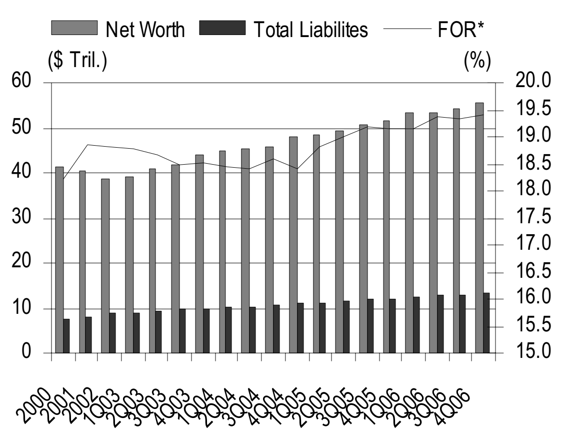
FRM –Fixed-rate mortgage. ARM –Adjustable-rate mortgage. Sources: Mortgage Bankers Association of America (MBA) and Freddie Mac.

occurred at the 'BB' and 'B' levels, where 1.4% and 2.3%, respectively, were upgraded in 2006. Downgrades were most prevalent at the below-investment-grade level, where the sharpest deterioration in credit was seen at the 'CCC' category, with 39.7% migrating downward in 2006. In addition, 31.3% of 'B' and 9.4% of 'BB' credits were downgraded in 2006. For perspective, nonmortgage ABS transition matrices are included in the Appendix on page 15.

■ 2007 ABS Outlook

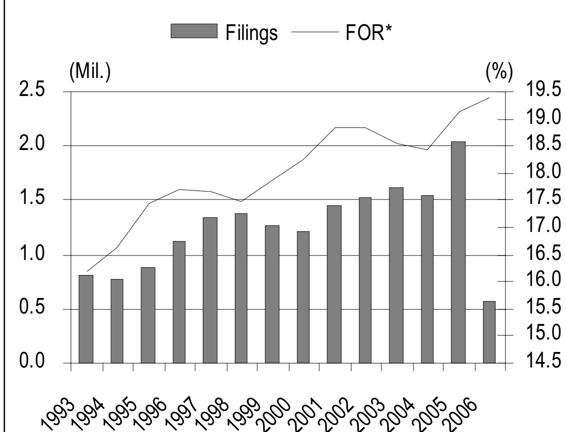
In 2007, Fitch expects performance in the consumer ABS sectors to remain positive, with a stable outlook on the prime auto, credit card, and student loan segments. However, for subprime consumer credits, Fitch remains cautious about asset performance over the intermediate term. Although, so far, the subprime credit card and auto sectors have remained resistant to problems in the mortgage sector, Fitch is closely monitoring the possible spill-over effect of higher mortgage defaults on subprime borrowers. Fitch will

Household Net Worth and Liabilities vs. Debt Service Burden



*Financial obligation ratio (FOR) as a percentage of disposable personal income. Source: Federal Reserve –Flow of Funds and Bureau of Economic Analysis.

Personal Bankruptcy Filings and Consumer Debt



*Financial obligation ratio (FOR) as percentage of disposable income. Sources: National Bankruptcy Research Center, U.S. Federal Reserve, and the Board of Govenors.

Residential Mortgage-Backed Securities One-Year Transition Matrix: 2006*
(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
'AAA'	99.52	0.48	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	5.69	94.31	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A'	1.18	7.84	90.99	0.00	0.00	0.00	0.00	0.00	100.00
'BBB'	0.40	1.00	6.28	92.02	0.30	0.00	0.00	0.00	100.00
'BB'	0.38	0.26	0.77	5.87	91.70	0.77	0.26	0.00	100.00
'B'	0.48	0.00	0.16	1.12	6.22	89.95	0.96	1.12	100.00
'CCC'	0.00	0.00	0.00	0.00	7.69	0.00	53.85	38.46	100.00

*Includes Alt-A and A-jumbo mortgage transactions.

also be carefully watching underwriting guidelines of lenders, especially in the subprime credit card and auto sectors. However, Fitch expects rating volatility for the majority of transactions in these sectors to be minimal due to current performance trends and healthy levels of excess spread available to absorb higher charge-offs.

For commercial assets, the equipment lease sector is expected to remain positive, while the franchise and small business loan sectors remain vulnerable to smaller net recoveries and long recovery times. In the aircraft sector, although operating lease fundamentals have improved and recent transactions employ more efficient structures, many pre-2001 transactions remain hampered by other considerations, such as maintenance expenses, volatile energy prices, and persistent industry weakness.

On the mortgage ABS side, MH transactions are expected to continue to stabilize, with a fairly even number of upgrades and downgrades. In the subprime real estate ABS sector, Fitch has a negative rating outlook for 2007, with expected declining asset performance. Weakening credit characteristics coupled with a challenging market environment paint the subprime landscape for 2007. In particular, the largest challenges lie ahead for the 2005 and 2006 vintages, when approximately three-quarters of hybrid adjustable-rate mortgages (ARM) borrowers are required to make a higher monthly payment with the scheduled rate adjustment at month 24.

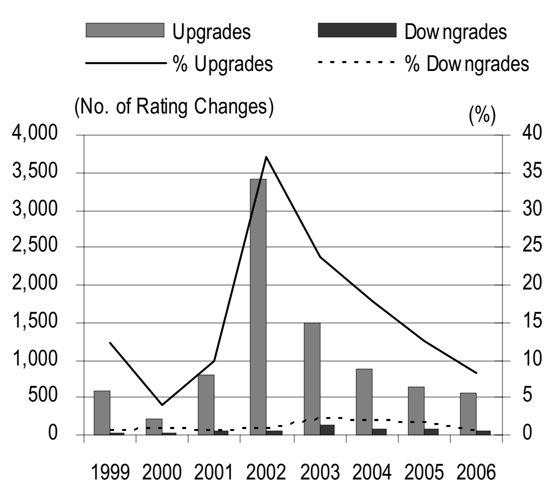
■ Upgrades Slow in RMBS But Still Greatly Outpace Downgrades

Rating stability in the RMBS sector improved in 2006, with 91% of ratings remaining the same, up from the 86% in 2005. However, the decrease in rating volatility was attributed to declines in both upgrades and downgrades. RMBS upgrades totaled 557 in 2006, a 14.4% drop from the 651 reported in 2005, while downgrades declined by nearly one-half, totaling 40 in 2006, compared with the 76 in 2005. The decline in negative rating activity was sharper than the drop in positive rating activity, resulting in an improved upgrade-to-downgrade ratio of 13.9 to one in 2006, compared with the 8.6 to one ratio in 2005.

Prepayments continued their downward descent in 2006, as interest rates slowly increased. The slowdown in prepayments resulted in less build-up in credit enhancement levels, the overriding factor behind the record level of upgrades seen during the 2001–2003 period. For the handful of downgrades that did occur in 2006, they were attributed to problem shelves in select bank conduits.

The majority of downgrades occurred at the non-investment-grade level, particularly in the 'CCC' category, which experienced the sharpest deterioration in credit quality, with 38.5% of tranches being downgraded in 2006. For 'BB' and

Residential Mortgage-Backed Securities Rating Changes



Residential Mortgage-Backed Securities Transition Matrices: 1991–2006*

(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	CCC’	‘CC’ and Below	Total
Average Annual									
‘AAA’	99.82	0.17	0.01	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	15.93	84.01	0.04	0.01	0.00	0.00	0.00	0.00	100.00
‘A’	6.57	13.21	80.01	0.20	0.01	0.00	0.00	0.00	100.00
BBB’	1.54	6.32	10.42	80.85	0.46	0.25	0.08	0.07	100.00
BB’	0.24	1.28	4.72	9.85	82.26	0.78	0.43	0.45	100.00
B’	0.05	0.12	0.81	3.29	8.35	83.87	1.41	2.11	100.00
CCC’	0.00	0.00	0.00	0.00	0.56	0.00	52.51	46.93	100.00
Average Two-Year									
‘AAA’	99.77	0.22	0.02	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	26.76	73.11	0.10	0.03	0.00	0.00	0.00	0.00	100.00
‘A’	15.92	18.83	64.77	0.37	0.11	0.00	0.00	0.00	100.00
BBB’	5.32	12.69	15.25	64.73	0.80	0.68	0.21	0.32	100.00
BB’	0.99	3.65	9.03	15.10	67.68	1.11	0.83	1.63	100.00
B’	0.14	0.61	2.65	7.03	13.97	67.83	2.15	5.61	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	0.00	30.41	69.59	100.00
Average Three-Year									
‘AAA’	99.62	0.35	0.03	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	33.41	66.38	0.17	0.05	0.00	0.00	0.00	0.00	100.00
‘A’	23.24	20.75	55.27	0.37	0.23	0.14	0.00	0.00	100.00
BBB’	9.54	15.82	16.86	54.32	1.27	0.77	0.38	1.04	100.00
BB’	2.07	5.99	11.15	17.97	56.82	1.40	1.05	3.56	100.00
B’	0.40	1.44	4.70	9.78	16.38	54.33	2.59	10.37	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	0.00	22.22	77.78	100.00

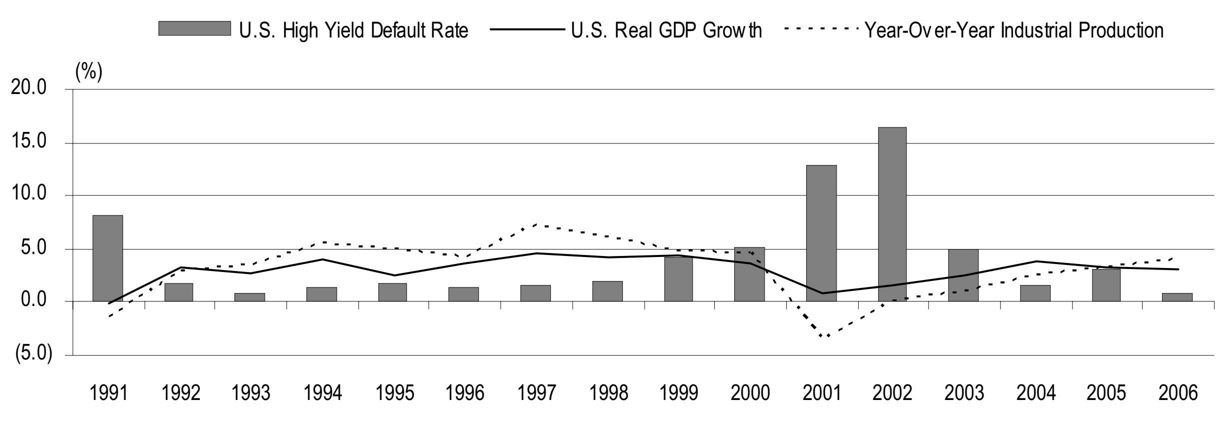
*Includes Alt-A and A-jumbo mortgage transactions.

‘B’ credits, negative rating actions were infrequent, with only 1.0% and 2.1%, respectively, downgraded. Meanwhile, at the investment-grade level, RMBS downgrades were either absent or minor in 2006. For example, at the ‘AAA’ level, 0.48% of credits were downgraded to the ‘AA’ rating category, while 0.30% of ‘BBB’ credits experienced negative rating actions. The ‘AA’ and ‘A’ categories did not experience any downgrades at all in 2006.

2007 RMBS Outlook

For both the prime and Alt-A sectors, Fitch has positive ratings outlooks, but declining asset performance outlooks. Weaker credit characteristics and a more challenging market environment will continue to cause

U.S. High Yield Dafult Rates vs. U.S. Real GDP Growth and Year-Over-Year Industrial Production: 1991–2006



GDP – Gross domestic product.

Collateralized Debt Obligation Transition One-Year Transition Matrix: 2006
(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	‘CCC’	‘CC’ and Below	Total
‘AAA’	99.51	0.16	0.16	0.16	0.00	0.00	0.00	0.00	100.00
‘AA’	10.83	87.58	1.59	0.00	0.00	0.00	0.00	0.00	100.00
‘A’	1.52	9.14	89.34	0.00	0.00	0.00	0.00	0.00	100.00
BBB’	0.23	0.68	7.45	88.26	2.48	0.90	0.00	0.00	100.00
BB’	0.00	0.00	1.41	9.86	81.69	6.10	0.47	0.47	100.00
B’	0.00	0.00	1.15	0.00	4.60	80.46	4.60	9.20	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	0.00	66.67	33.33	100.00

deterioration in prime jumbo mortgage collateral relative to the unusually strong performance of recent years. However, the large margin between the unexpectedly low losses incurred in recent years and the loss amounts typically credit enhanced for in prime structures will allow for a relatively significant increase in losses without a notable increase in the number of downgrades. Therefore, despite a relative deterioration in the prime asset performance, upgrades are expected to significantly outnumber downgrades.

Similarly, Fitch expects the Alt-A sector to experience deterioration in collateral performance due to generally weaker collateral attributes and a more challenging market environment. However, the deterioration in collateral performance is expected to only reduce the positive margin between the number of upgrades and downgrades.

CDO Upgrades on the Rise While Downgrades Continue to Decline

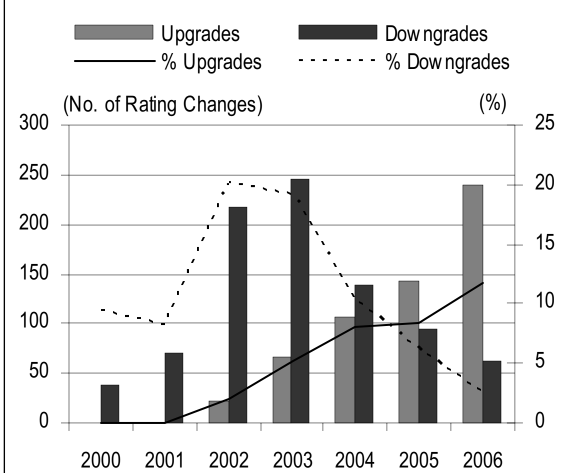
The CDO sector continued to show improvement in 2006, as the number of upgrades increased by 68.3%, totaling 239, compared with 142 in 2005. In addition, the number of downgrades declined by 33%, to 63 in 2006, down from the 94 reported in 2005. Last year marks the second consecutive year that CDO upgrades have outpaced downgrades. Indeed, the upgrade-to-downgrade ratio improved to 3.8 to one in 2006, compared with 1.5 to one in 2005.

The upgrades were overwhelmingly from SF CDOs (which includes CRE CDOs), diversified SF CDOs, and CDO squared transactions. The CRE CDO sector accounted for the vast majority of SF CDO upgrades, representing 75% of the positive rating actions in 2006. Most of the improvement recorded in the CRE CDO sector was attributed to upgrades in the CMBS market, which was largely a result of underlying loan defeasance. In addition, the seasoning of portfolios and deleveraging of CDO liabilities also contributed to the upgrades.

While SF CDOs increasingly grabs the lion share of the CDO rated universe, CDOs backed by corporate assets, including investment-grade or high yield bonds, declined in share. Uncharacteristically, investment-grade corporate bond CDOs posted a higher number of negative rating actions than high yield bond CDOs. Most of the downgrade activity in investment grade corporate bond CDOs was due to the exposure to the auto sector. The credit events of auto suppliers Delphi Corp. and Dana Corp. contributed to this negative rating volatility. In addition, the corporate issuer downgrades of Ford Motor Company and General Motors Corp., both of which are heavily referenced names, also contributed to the CDO sector’s poor performance.

Positive CDO rating performance in 2006 is most striking when viewed in the context of historical average annual migration rates. For example, at the ‘AA’ level, 10.8% of credits were upgraded in 2006, a more than four-fold increase over the

Collateralized Debt Obligation Rating Changes



Collateral Debt Obligation Transition Matrices: 1995—2006
(%)

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC'	'CC' and Below	Total
Average Annual									
'AAA'	96.68	1.77	0.82	0.55	0.05	0.09	0.05	0.00	100.00
'AA'	4.21	90.40	2.49	1.45	0.90	0.28	0.00	0.28	100.00
'A'	1.45	3.96	87.66	3.17	2.37	0.73	0.33	0.33	100.00
BBB'	0.24	0.43	3.04	87.04	3.18	3.23	1.04	1.80	100.00
BB'	0.10	0.00	0.40	4.17	82.21	6.16	2.49	4.47	100.00
B'	0.00	0.00	0.38	0.00	3.83	75.86	5.56	14.37	100.00
CCC'	0.00	0.00	0.00	0.00	0.95	0.95	46.67	51.43	100.00
Average Two-Year									
'AAA'	91.33	3.88	1.55	1.13	1.13	0.71	0.21	0.07	100.00
'AA'	6.59	80.33	4.22	3.91	2.57	1.13	0.10	1.13	100.00
'A'	2.61	6.12	76.13	5.22	3.51	2.51	1.30	2.61	100.00
BBB'	0.80	0.86	4.19	73.85	5.59	5.92	2.20	6.59	100.00
BB'	0.14	0.00	0.55	6.78	66.67	8.85	4.15	12.86	100.00
B'	0.00	0.00	0.53	0.00	6.86	59.63	5.01	27.97	100.00
CCC'	0.00	0.00	0.00	0.00	0.00	1.15	22.99	75.86	100.00
Average Three-Year									
'AAA'	84.19	6.39	2.13	1.91	2.58	2.13	0.56	0.11	100.00
'AA'	8.32	71.11	4.08	6.28	4.87	2.20	0.94	2.20	100.00
'A'	2.35	7.52	65.20	7.99	3.76	3.76	1.57	7.84	100.00
BBB'	0.58	0.77	4.15	61.81	8.20	7.71	2.60	14.18	100.00
BB'	0.00	0.20	0.39	5.70	54.81	10.61	4.13	24.17	100.00
B'	0.00	0.00	0.38	0.38	6.44	46.97	4.92	40.91	100.00
CCC'	0.00	0.00	0.00	0.00	0.00	1.67	16.67	81.67	100.00

average 2.4% upgraded over the 1995–2005 period. Similarly, improvement was also seen across 'A' and 'BBB' credits, which experienced upgrade rates of 10.7% and 8.4%, respectively, in 2006, considerable jumps over the historical annual averages of 3.6% and 2.5%, respectively.

This same positive pattern held true for downgrade activity. At the 'AAA' level, only 0.49% of tranches were downgraded in 2006, compared with an average 4.4% over the prior decade. Non-investment-grade credits also recorded significant declines in negative rating actions. For example, 7.0% of 'BB' credits were downgraded in 2006, a considerable improvement from the average 15% over the 1995–2005 period.

■ 2007 CDO Outlook

In 2007, Fitch expects to see fewer upgrades and more downgrade pressure in SF and CRE CDOs, as the structured finance sectors adjust to recent stress in the subprime mortgage market. Many of the newer vintage CRE CDOs contain relatively riskier assets, including condominium conversion, land, and construction loans, which are vulnerable to shocks in the U.S. economy. Similarly, RMBS CDOs are also expected to experience relatively fewer positive rating actions in 2007, as rising interest rates and slower home price appreciation likely will dampen prepayments.

For investment-grade corporate CDO, Fitch has a stable ratings outlook but a declining asset performance outlook. Although the sector will likely be affected by the increases in credit events and lower expected recoveries, the seasoning aspect will probably mitigate most of the deterioration. Likewise, Fitch also has a stable ratings outlook and a declining asset performance outlook for high yield bond CDOs.

■ Methodology

All Fitch U.S. structured finance (ABS, CDO, RMBS, and CMBS) long-term debt ratings from 1991–2006 were included in this study. Public, private, and 144A issues were included. If a new rating was picked up as a result of a merger, it was treated as a new rating as of the merger date. Fitch's continuing data enhancement efforts may result in slightly different statistics than in previously published studies. Therefore, this most recent study supersedes all prior versions.

The occurrence and timing of both rating upgrades and downgrades may be attributed to several factors. Upgrades generally result from increased levels of credit enhancement that are achieved as the collateral and transaction season past the asset specific default curve or as a result of upgrades of third-party credit enhancers. Factors associated with rating downgrades are more diverse. Collateral performance outside of expectations remains a primary cause. This may be due to aggressive underwriting caused by excessive market competition, small changes to underwriting criteria over time that cause the quality of originations to decline and servicing operational issues. These problems may also be exacerbated by the effect of an economic slowdown on consumers and businesses. Unforeseeable event risks such as fraud may also cause rating downgrades.

It is important to observe that the rating transitions outlined in this study represent a distinct historical period and may not represent future rating migration patterns. Transition rates are influenced by a number of factors, including credit enhancement, macroeconomic variables, and credit conditions.

To calculate transition rates, cohorts were created for each year from 1991–2006. A cohort is defined as a fixed pool representing the number of outstanding ratings at the beginning of a respective year. For example, the 2006 cohort may include ratings from 1996, 1997, 1998, and so on if these ratings were indeed outstanding at the beginning of 2006. However, if a new rating were picked up in the middle of 2006, that rating movement would be included in a future study in the 2007 cohort. Cohort should not be confused with vintage, which represents the year in which a transaction came to market.

The cohorts remain fixed over time, with the rating performance of all tranches in each cohort tracked accordingly. A tranche was defined as a class of securities or certificates within the same rating category. Pari passu tranches were treated as one observation. If a rating was withdrawn then it was not included in the analysis for the cohort year in which it was withdrawn since transition rates examine beginning-of-the-year ratings versus the end-of-the-year ratings. Furthermore, for the purposes of calculating average one- and two-year transition rates, the transition rates for each year were weighted by the number of tranches outstanding for each rating category at the beginning of the year or cohort. This was done to give a fair evaluation of rating performance, since the number of structured finance tranches rated by Fitch grew substantially over the period.

Appendix

Nonmortgage Asset-Backed Securities One-Year Transition Matrix: 2006

(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	‘CCC’	‘CC’ and Below	Total
‘AAA’	99.38	0.50	0.12	0.00	0.00	0.00	0.00	0.00	100.00
‘AA’	24.59	75.41	0.00	0.00	0.00	0.00	0.00	0.00	100.00
‘A’	2.88	4.20	91.59	0.66	0.44	0.00	0.00	0.22	100.00
BBB’	0.00	0.34	5.17	92.07	2.07	0.34	0.00	0.00	100.00
BB’	0.00	0.00	2.08	3.13	88.54	4.17	2.08	0.00	100.00
B’	0.00	0.00	0.00	2.08	2.08	77.08	12.50	6.25	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	0.00	68.00	32.00	100.00

Nonmortgage ABS Transition Matrices: 1991—2006

(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’	‘CCC’	‘CC’ and Below	Total
Average Annual									
‘AAA’	98.52	0.83	0.35	0.11	0.03	0.01	0.05	0.09	100.00
‘AA’	6.29	87.95	3.31	1.12	0.43	0.11	0.05	0.75	100.00
‘A’	0.62	2.82	92.55	2.07	0.68	0.42	0.16	0.66	100.00
BBB’	0.20	0.10	2.17	91.91	1.66	1.52	0.64	1.79	100.00
BB’	0.00	0.37	0.37	4.40	79.95	5.50	2.93	6.48	100.00
B’	0.30	0.00	0.00	0.60	0.90	70.27	8.41	19.52	100.00
CCC’	0.00	0.00	0.00	0.00	0.76	0.00	58.78	40.46	100.00
Average Two-Year									
‘AAA’	96.77	1.47	0.74	0.29	0.14	0.11	0.16	0.32	100.00
‘AA’	7.12	80.34	5.85	2.75	1.06	0.49	0.21	2.18	100.00
‘A’	1.89	4.20	85.91	3.33	1.18	1.05	0.50	1.94	100.00
BBB’	0.27	0.41	3.01	84.90	2.28	2.74	1.23	5.16	100.00
BB’	0.00	0.49	0.65	5.56	64.81	5.40	4.26	18.82	100.00
B’	0.38	0.00	0.00	1.15	0.38	53.26	6.13	38.70	100.00
CCC’	0.00	0.00	0.00	0.00	1.02	0.00	39.80	59.18	100.00
Average Three-Year									
‘AAA’	94.57	2.12	1.05	0.70	0.27	0.32	0.30	0.67	100.00
‘AA’	5.31	75.48	7.34	3.96	1.64	1.06	0.19	5.02	100.00
‘A’	2.66	3.49	81.77	4.11	1.71	1.78	0.84	3.64	100.00
BBB’	0.26	0.33	1.91	79.42	2.24	3.62	1.84	10.39	100.00
BB’	0.00	0.23	0.00	2.76	53.92	5.76	5.07	32.26	100.00
B’	0.50	0.00	0.00	0.00	0.50	40.00	5.00	54.00	100.00
CCC’	0.00	0.00	0.00	0.00	0.00	0.00	19.18	80.82	100.00

Average Annual Transition Matrices: 1991–2006

(%, Modifier Level)

	'AAA'	'AA+'	'AA'	'AA–'	'A+'	'A'	'A–'	'BBB+'	'BBB'	'BBB–'	'BB+'	'BB'	'BB–'	'B+'	'B'	'B–'	'CCC+' to 'CCC–'	'CC' and Below	Total
U.S. Structured Finance																			
'AAA'	99.28	0.10	0.27	0.09	0.03	0.10	0.02	0.01	0.04	0.02	0.00	0.01	0.01	0.00	0.01	0.00	0.01	0.02	100.00
'AA+'	23.37	74.69	1.34	0.13	0.06	0.03	0.16	0.03	0.00	0.03	0.00	0.10	0.03	0.00	0.03	0.00	0.00	0.00	100.00
'AA'	10.88	3.14	84.72	0.22	0.20	0.25	0.16	0.03	0.08	0.09	0.01	0.03	0.02	0.00	0.05	0.00	0.00	0.10	100.00
'AA–'	8.67	3.21	4.24	79.74	0.26	1.29	1.14	0.07	0.26	0.59	0.07	0.15	0.15	0.00	0.00	0.00	0.04	0.11	100.00
'A+'	5.26	3.14	5.28	3.14	80.86	0.25	0.25	0.25	0.75	0.20	0.05	0.20	0.05	0.05	0.13	0.03	0.05	0.05	100.00
'A'	3.70	1.92	4.36	1.24	2.63	83.93	0.43	0.21	0.50	0.34	0.06	0.18	0.04	0.01	0.14	0.03	0.07	0.22	100.00
'A–'	2.82	1.57	2.04	1.57	2.82	4.19	79.70	2.18	0.64	0.67	0.17	0.39	0.42	0.08	0.25	0.20	0.14	0.14	100.00
'BBB+'	1.84	0.87	2.17	1.14	3.25	3.47	2.93	78.46	0.54	0.98	0.46	0.54	0.46	0.05	2.22	0.19	0.30	0.11	100.00
'BBB'	0.98	0.66	1.45	0.92	1.73	2.88	1.18	2.78	83.95	0.61	0.27	0.90	0.21	0.06	0.44	0.12	0.28	0.58	100.00
'BBB–'	0.52	0.21	0.57	0.50	0.83	1.33	1.35	2.35	3.91	80.22	0.83	1.66	1.33	0.40	1.16	0.66	0.85	1.33	100.00
'BB+'	0.49	0.05	1.14	0.30	1.04	2.47	1.38	4.01	4.75	5.49	75.82	0.30	0.40	0.45	0.49	0.20	0.49	0.74	100.00
'BB'	0.22	0.11	0.50	0.26	0.57	1.59	0.88	1.66	3.71	2.10	3.24	80.20	0.35	0.23	1.37	0.40	0.76	1.86	100.00
'BB–'	0.12	0.00	0.30	0.06	0.18	0.30	0.59	0.42	1.25	2.26	4.04	3.86	76.47	1.43	2.26	1.31	2.08	3.09	100.00
'B+'	0.28	0.00	0.09	0.09	0.47	0.37	0.19	0.37	0.84	1.69	4.31	6.47	3.75	75.82	0.66	0.94	1.31	2.34	100.00
'B'	0.07	0.02	0.04	0.01	0.10	0.34	0.16	0.35	1.26	0.82	1.82	3.41	1.15	2.77	80.47	0.86	2.25	4.09	100.00
'B–'	0.14	0.00	0.07	0.07	0.00	0.00	0.07	0.00	0.14	0.00	0.35	1.06	0.28	1.06	2.62	78.30	5.96	9.86	100.00
'CCC' to 'CCC–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.22	0.33	0.22	0.22	0.33	1.76	56.83	40.09	100.00
U.S. Asset-Backed Securities																			
'AAA'	98.86	0.09	0.39	0.19	0.02	0.24	0.00	0.02	0.06	0.02	0.00	0.02	0.02	0.00	0.01	0.00	0.03	0.06	100.00
'AA+'	7.72	91.40	0.09	0.26	0.18	0.09	0.18	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.09	0.00	0.00	0.00	100.00
'AA'	2.48	1.96	92.53	0.35	0.62	0.65	0.39	0.08	0.15	0.18	0.00	0.10	0.05	0.00	0.12	0.02	0.02	0.29	100.00
'AA–'	1.20	0.35	1.98	90.40	0.49	2.19	1.62	0.00	0.21	0.92	0.07	0.21	0.14	0.00	0.00	0.00	0.07	0.14	100.00
'A+'	0.39	1.17	1.60	0.74	92.97	0.35	0.35	0.31	1.13	0.31	0.04	0.16	0.04	0.04	0.20	0.04	0.08	0.08	100.00
'A'	0.45	0.16	1.65	0.63	0.92	91.77	0.85	0.36	0.97	0.77	0.03	0.36	0.08	0.01	0.30	0.05	0.12	0.51	100.00
'A–'	0.07	0.07	0.21	0.21	0.49	0.97	89.72	4.10	0.83	0.97	0.21	0.14	0.69	0.21	0.35	0.35	0.21	0.21	100.00
'BBB+'	0.24	0.00	0.15	0.05	1.51	0.88	0.49	88.49	0.73	1.41	0.73	0.68	0.68	0.00	3.17	0.29	0.34	0.15	100.00
'BBB'	0.06	0.00	0.18	0.02	0.12	0.97	0.18	0.93	91.40	0.94	0.50	1.69	0.38	0.09	0.77	0.15	0.50	1.11	100.00
'BBB–'	0.06	0.00	0.00	0.00	0.00	0.17	0.00	0.06	0.41	86.24	0.99	2.55	2.38	0.64	2.09	0.81	1.22	2.38	100.00
'BB+'	0.00	0.00	0.60	0.00	0.20	0.00	0.00	2.00	2.60	0.20	89.00	0.40	0.40	1.40	0.60	0.20	1.20	1.20	100.00
'BB'	0.07	0.00	0.28	0.00	0.07	0.00	0.00	0.00	1.10	0.41	0.62	78.41	0.48	0.83	4.21	1.93	2.76	8.83	100.00
'BB–'	0.00	0.00	0.00	0.00	0.00	0.00	1.48	0.00	0.00	0.00	2.22	0.00	62.59	1.85	8.15	4.07	7.04	12.59	100.00
'B+'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.33	0.00	73.33	1.33	1.33	9.33	13.33	100.00
'B'	0.13	0.00	0.00	0.00	0.00	0.13	0.00	0.13	0.13	0.00	0.38	0.50	0.13	0.13	66.62	1.25	9.16	21.33	100.00
'B–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.68	0.00	44.90	17.01	37.41	100.00
'CCC' to 'CCC–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.29	0.00	0.00	0.00	0.00	49.14	50.57	100.00
U.S. Residential Mortgage-Backed Securities																			
'AAA'	99.82	0.04	0.13	0.00	0.01	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA+'	28.89	71.03	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.08	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	14.56	2.61	82.76	0.01	0.02	0.03	0.00	0.00	0.00	0.01	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA–'	15.97	6.23	5.59	72.20	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A+'	11.40	6.84	14.53	5.56	61.68	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A'	6.41	3.75	6.73	1.52	2.57	78.85	0.06	0.06	0.05	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A–'	3.41	4.75	5.49	2.82	5.04	3.71	73.15	1.34	0.00	0.15	0.00	0.15	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'BBB+'	2.52	2.04	6.45	2.99	6.13	8.33	3.62	65.25	0.16	0.00	0.16	0.16	0.16	0.00	1.89	0.00	0.16	0.00	100.00
'BBB'	1.52	1.32	2.84	1.91	3.45	4.71	1.51	2.50	79.46	0.08	0.01	0.39	0.04	0.00	0.09	0.03	0.07	0.07	100.00
'BBB–'	0.56	0.56	1.31	1.87	2.61	5.22	3.92	4.85	4.10	73.69	0.00	0.75	0.00	0.00	0.19	0.00	0.19	0.19	100.00
'BB+'	0.22	0.00	1.94	1.08	2.59	6.03	2.16	7.97	7.33	6.47	63.79	0.00	0.00	0.00	0.22	0.00	0.00	0.22	100.00
'BB'	0.23	0.16	0.60	0.38	0.82	2.27	1.25	2.23	4.72	2.04	2.67	80.82	0.15	0.03	0.70	0.09	0.41	0.41	100.00
'BB–'	0.41	0.00	1.63	0.00	1.22	1.22	1.22	1.22	3.66	6.10	4.47	4.88	69.51	0.00	0.41	0.41	1.63	2.03	100.00
'B+'	0.38	0.00	0.38	0.00	0.38	1.53	0.77	1.15	3.07	4.60	8.43	14.18	2.30	61.69	0.00	0.00	0.00	1.15	100.00
'B'	0.02	0.03	0.03	0.02	0.13	0.38	0.21	0.43	1.60	1.09	2.21	4.16	1.32	2.62	82.11	0.28	1.42	1.93	100.00
'B–'	0.76	0.00	0.76	0.76	0.00	0.00	0.76	0.00	0.00	0.00	0.00	4.58	1.53	1.53	6.11	67.18	3.82	12.21	100.00
'CCC' to 'CCC–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.56	0.00	0.00	0.00	0.00	52.51	46.93	100.00

Average Annual Transition Matrices: 1991–2006 (continued)

(%, Modifier Level)

	'AAA'	'AA+'	'AA'	'AA–'	'A+'	'A'	'A–'	'BBB+'	'BBB'	'BBB–'	'BB+'	'BB'	'BB–'	'B+'	'B'	'B–'	'CCC+' to 'CCC–'	'CC' and Below	Total
U.S. Commercial Mortgage-Backed Securities																			
'AAA'	99.69	0.10	0.17	0.00	0.00	0.03	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA+'	48.75	50.36	0.72	0.00	0.00	0.00	0.00	0.18	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	17.97	8.35	73.49	0.05	0.00	0.05	0.00	0.00	0.05	0.00	0.05	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA–'	23.90	8.18	10.06	57.65	0.00	0.00	0.00	0.00	0.00	0.21	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A+'	20.18	6.91	10.73	11.09	50.73	0.00	0.00	0.18	0.00	0.00	0.18	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A'	5.95	1.79	5.41	2.78	8.48	74.75	0.45	0.10	0.15	0.05	0.05	0.05	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A–'	7.37	2.28	3.32	3.11	4.77	9.23	69.09	0.21	0.21	0.21	0.00	0.21	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'BBB+'	6.22	2.57	4.33	2.84	5.14	6.90	9.07	61.71	0.54	0.41	0.00	0.00	0.00	0.14	0.00	0.00	0.14	0.00	100.00
'BBB'	2.52	0.81	1.41	0.86	1.61	3.58	3.42	8.41	75.88	0.91	0.20	0.25	0.05	0.00	0.05	0.00	0.05	0.00	100.00
'BBB–'	1.13	0.40	0.93	0.73	1.33	1.52	2.19	4.37	8.15	77.27	0.66	0.80	0.20	0.00	0.07	0.07	0.20	0.00	100.00
'BB+'	1.03	0.11	1.25	0.11	0.80	2.39	1.94	3.42	4.78	8.20	74.49	0.46	0.23	0.23	0.11	0.00	0.00	0.46	100.00
'BB'	0.42	0.00	0.42	0.07	0.00	0.56	0.35	1.18	2.22	4.24	7.64	80.56	0.69	0.56	0.56	0.14	0.00	0.42	100.00
'BB–'	0.00	0.00	0.11	0.11	0.00	0.22	0.34	0.22	1.35	2.47	4.83	5.51	82.36	1.24	0.79	0.22	0.11	0.11	100.00
'B+'	0.31	0.00	0.00	0.15	0.31	0.00	0.00	0.15	0.15	0.93	3.71	4.02	4.79	82.38	0.93	0.77	0.93	0.46	100.00
'B'	0.35	0.00	0.09	0.00	0.00	0.35	0.00	0.17	0.52	0.17	1.13	2.00	0.96	4.53	84.41	3.14	0.78	1.39	100.00
'B–'	0.11	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.21	0.00	0.42	0.53	0.11	0.74	2.85	86.51	4.64	3.90	100.00
'CCC' to 'CCC–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.73	0.00	0.73	0.73	1.09	5.47	73.36	17.88	100.00
U.S. Collateralized Debt Obligations*																			
'AAA'	96.68	0.59	0.77	0.41	0.27	0.27	0.27	0.09	0.27	0.18	0.00	0.05	0.00	0.05	0.05	0.00	0.05	0.00	100.00
'AA+'	9.22	70.05	17.05	0.46	0.00	0.00	1.38	0.00	0.00	0.00	0.00	1.38	0.46	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	3.56	5.10	84.71	2.21	0.29	0.77	0.96	0.10	0.58	0.58	0.19	0.10	0.19	0.10	0.29	0.00	0.00	0.29	100.00
'AA–'	2.09	2.09	2.09	80.63	0.00	2.09	4.19	1.05	2.09	1.05	0.52	0.52	1.05	0.00	0.00	0.00	0.00	0.52	100.00
'A+'	4.91	5.52	4.91	3.68	74.85	0.61	0.61	0.61	0.61	0.00	0.00	2.45	0.61	0.61	0.00	0.00	0.00	0.00	100.00
'A'	0.94	0.23	3.05	0.35	3.99	85.81	0.23	0.59	1.41	0.59	0.82	0.59	0.23	0.00	0.35	0.12	0.35	0.35	100.00
'A–'	1.20	0.20	0.20	0.80	2.80	4.40	80.20	1.60	1.80	1.40	0.60	1.80	1.00	0.00	0.80	0.40	0.40	0.40	100.00
'BBB+'	0.38	0.00	1.53	0.38	4.60	2.30	3.07	79.31	0.00	1.53	0.38	1.92	0.77	0.38	1.92	0.38	0.77	0.38	100.00
'BBB'	0.22	0.00	0.07	0.00	0.22	1.15	0.93	4.96	84.41	1.44	0.65	0.86	0.57	0.29	1.29	0.65	0.65	1.65	100.00
'BBB–'	0.22	0.00	0.66	0.00	0.22	0.44	0.66	1.32	2.87	74.83	1.77	2.21	2.65	1.32	2.43	2.87	2.43	3.09	100.00
'BB+'	0.00	0.00	0.00	0.00	0.56	0.56	0.56	2.22	3.89	4.44	76.67	0.00	2.22	0.00	2.78	1.67	2.22	2.22	100.00
'BB'	0.00	0.00	0.00	0.00	0.18	0.00	0.00	0.18	1.82	1.64	5.65	76.32	1.64	0.36	4.19	0.91	1.82	5.28	100.00
'BB–'	0.36	0.00	0.00	0.00	0.00	0.00	0.00	0.72	0.00	0.36	2.89	1.44	77.26	2.89	2.89	2.89	3.97	4.33	100.00
'B+'	0.00	0.00	0.00	0.00	2.38	0.00	0.00	0.00	0.00	0.00	0.00	5.95	3.57	71.43	0.00	4.76	1.19	10.71	100.00
'B'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.18	1.18	6.67	67.06	3.14	7.06	13.73	100.00
'B–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.55	2.19	0.55	2.73	1.09	70.49	5.46	16.94	100.00
'CCC' to 'CCC–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.95	0.00	0.00	0.00	0.95	46.67	51.43	100.00

*Represents 1995–2006 period.

Special Report

2006 European Structured Finance Rating Transition Study

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■ Summary

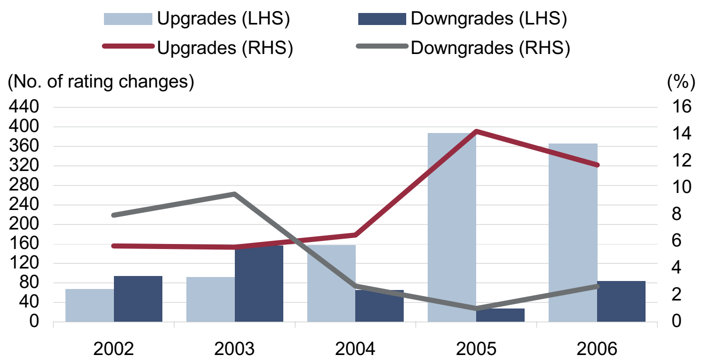
This report reviews the historical performance of European Structured Finance (ESF) transactions rated privately and publicly by Fitch Ratings between 1993 and 2006. It illustrates and comments on the performance of the major asset classes and major jurisdictions in 2006. The study may be a useful tool for those interested in entering new asset classes or new jurisdictions, as well as those who wish to review the relative performance of their portfolios.

Among the highlights for ESF in 2006, the report shows:

- rating performance remained strong in 2006, with an upgrade to downgrade ratio of over 4:1, but could not match the extraordinary strength of 2005;
- RMBS was the strongest sector with 99.9% of investment-grade tranches maintaining their rating or moving to a higher category;
- a particular sub-class of synthetic corporate CDOs accounted for most of the increase in downgrades during 2006; and
- the Netherlands was, again, the best-performing major country market, with 42 upgrades to a new rating category and no downgrades.

A positive balance of upgrades over downgrades prevailed in 2006 for the third year running. There were 366 upgrades and 83 downgrades, measured at the rating modifier ('+' and '-') level over the year – a ratio of over 4:1. This was less positive than 2005's 14:1 ratio, largely because downgrades slightly more than trebled from 27 in 2005. The chart below shows the course of the credit cycle in ESF over the past five years both in terms of the numbers of upgrades and downgrades at the modifier level and their proportion to the total numbers of observations for each year, all measured on the basis of transition study methodology (see *Scope of Study* below).

Western Europe – European Structured Finance Rating Changes 2002–2006



Source: Fitch

This is the fifth annual review of rating transitions for Fitch-rated ESF transactions and covers European asset-backed securities (ABS), residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS) and collateralised debt obligations (CDOs). The study aims to provide an indication of the relative stability of ESF ratings overall, by asset class and by jurisdiction.

Readers are urged to bear in mind that transition rates are historical and will not necessarily provide a reliable indication of future rating movements. In particular, they should recall that some structured finance sectors have yet to experience a stressful period, while others have experienced severe stress relatively early in their development but may demonstrate greater stability in the future. For some, further upgrades are less likely than in the past owing to the structure of the deal as, for example, notes revert from a sequential to a pro rata pay-down.

Highlights

The highlights of the transition data to end-2006 are summarised below and discussed further throughout this report:

- Rating performance remained strong in 2006, but the rate of improvement decelerated from 2005's extraordinarily strong performance, due to a modest decline in the number of upgrades and an approximately threefold increase in the number of downgrades.
- With 235 upgrades and 48 downgrades to new rating categories, the upgrade-to-downgrade ratio in 2006 was 4.9, compared with 16.4 for 2005.
- The proportion of one-year investment-grade observations maintaining the same or moving to a higher rating category fell to 98.46% in 2006 from an unusually high 99.53% in 2005, due to the increase in downgrades.
- An alternative indicator of rating change, the ESF Index of Rating Change, introduced by Fitch during 2006 as a way of measuring changes in the weighted-average probability of default as a result of rating changes, rose by 2.3% in 2006, after an increase of 5.1% in 2005, consistent with this transition study's conclusion that improvement in rating performance is decelerating.
- RMBS was again the best-performing sector: with only two downgrades to a new rating category (and a further three at the modifier level), 99.9% of its investment-grade observations in 2006 maintained the same or moved to a higher rating category.
- CDOs outperformed their long-term average, with particular strength in SME and structured finance CDOs, but this sector also accounted for 39 of the 48 downgrades to a new rating category in 2006, largely affecting synthetic corporate CDOs forming the inner level of CDO-squared transactions.
- CMBS maintained a strongly positive performance with 34 upgrades to a new rating category and only four downgrades.
- The ABS sector saw relatively few rating changes, with only four upgrades and three downgrades to a new rating category, including the first downgrade affecting the UK credit card sector.
- The Dutch market maintained its record as the only sector in this study never to have experienced a downgrade to a new rating category, while recording 42 upgrades.
- 99.65% of investment-grade observations of tranches backed predominantly by single-country collateral maintained the same or moved to a higher rating category in 2006; the corresponding figure for transactions backed by multi-country collateral (mainly CDOs) was 96.01%.
- Rating volatility increases, as would be expected, for longer observation intervals. The proportion of investment-grade observations over the period 1993-2006 that maintained the same or moved to a higher rating category was 97.79% for annual observations, 95.65% for two-year observations and 93.46% for three-year observations.
- The total number of observations in the study grew by 33% with the addition of 2006 data; all the growth came in the RMBS and CMBS sectors.

Scope of Study

This study tracks the migration of the Long-Term Ratings assigned to ESF tranches by Fitch over successive one-, two- and three-year periods, commencing at the beginning of 1993. In keeping with Fitch's standard methodology for transition analysis, where a transaction, or series of transactions from a single master trust, includes two or more tranches ranking pari passu, only one of these tranches is taken into account in the calculations, since the whole set will always share the same rating. At times, this study describes the

Table 1: Western Europe: One-Year Rating Transition Matrix, 2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	98.73	1.19	0.08	0.00	0.00	0.00	0.00	0.00	100.00
AA	15.01	83.00	1.81	0.18	0.00	0.00	0.00	0.00	100.00
A	1.70	12.61	83.65	2.04	0.00	0.00	0.00	0.00	100.00
BBB	0.19	0.57	9.25	88.87	0.94	0.19	0.00	0.00	100.00
BB	0.00	2.48	0.62	4.35	91.93	0.62	0.00	0.00	100.00
B	0.00	0.00	0.00	3.33	3.33	90.00	3.33	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	14.29	71.43	14.29	100.00

Source: Fitch

resulting database as containing only "independent" tranches.

The majority of the tabular analysis in this report is based on transitions between rating categories such as 'AAA', 'AA' and 'A', and does not include rating changes within a rating category arising from the addition or subtraction of a rating modifier such as '+' or '-'. However, at times it is appropriate to analyse ESF transitions down to the modifier level; where this occurs, it is clearly noted.

On occasions, some of the cells in the transition matrices will be based on a limited number of observations and should be interpreted with caution. In particular, this affects most of the speculative-grade ratings and some specialised asset and country sectors.

Readers should note that all the cells in the transition matrices are rounded to two decimal places; as a result of that rounding, the totals across each published row might not always add to 100.

A summary of the methodology and definitions used in the study is set out in *Appendix 1*. Fitch's continuing data enhancement efforts may result in slightly different statistics than in the previously published study. As a result of that, this study supersedes the previous version.

Appendix 2 provides a listing of all publicly rated ESF tranches whose rating changed during 2006.

Fitch publishes rating transition studies for other market sectors, including for the structured finance market in the US. The most recent of these, "*Fitch Ratings 1990-2006 US Structured Finance Transition Study",* was published on 27 April 2007 and is available on the agency's website.

■ Performance Stays Good in 2006

For the third year in a row, upgrades comfortably exceeded downgrades in 2006, following three successive years between 2001 and 2003 with a positive net balance of downgrades over upgrades.

In 2006, there were 235 (279 in 2005) upgrades to a new rating category and correspondingly 48 (17 in 2005) downgrades. For the three positive years 2004-2006, the total number of upgrades to a new rating category exceeded downgrades by 616 to 117, a ratio of over 5:1. In contrast, for the three negative years 2001-2003 that preceded this period, upgrades to a new rating category fell short of the number of downgrades by 118 to 210, a ratio of a little above 0.5. The higher numbers in the more recent period reflect in part the rapid growth in the market, discussed further below.

Table 1 shows the one-year transition matrix for all Fitch-rated ESF securities for 2006 alone.

In transition matrices such as Table 1, the beginning-of-year ratings are represented by the row headings and the end-of-year ratings by the column headings. The percentages shown across each row represent the proportions of observations that began the year in that rating category and ended the same year in the rating categories shown in each column heading.

Table 2: Western Europe: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	98.46	1.36	0.16	0.02	0.00	0.00	0.00	0.00	100.00
AA	11.65	86.07	2.00	0.19	0.05	0.05	0.00	0.00	100.00
A	1.96	8.02	87.33	2.14	0.22	0.22	0.00	0.11	100.00
BBB	0.45	0.98	5.75	89.92	1.78	0.53	0.36	0.22	100.00
BB	0.00	0.56	0.69	5.56	87.78	3.06	0.97	1.39	100.00
B	0.00	0.00	0.00	3.00	2.00	79.00	9.00	7.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	2.44	68.29	29.27	100.00

Source: Fitch

The 'AA' row in Table 1, for example, shows that 15.01% of tranches with a beginning-of-year rating in the 'AA' category ended the year at 'AAA', while 83.00% remained in the 'AA' category, 1.81% ended the year in the 'A' category and 0.18% were downgraded to the 'BBB' category. Each year for which a security is outstanding and carries a rating both at the beginning and the end of the year counts as one observation when deriving annual matrices.

Table 1 shows the significant proportions of upgrades recorded in all rating categories except 'AAA' (which cannot be upgraded), with the 'AA' and 'A' categories performing especially strongly.

A longer-term perspective on rating transition in ESF is provided by Table 2, which shows the average annual transition matrix for 1993-2006. This table takes account of all one-year observations available from the beginning of 1993 until the end of 2006.

Table 3, drawn from data in Tables 1 and 2, shows the proportions in each rating category that maintained the same or moved to a higher rating category during 2006 and compares this with the annual averages across the whole 1993-2006 period. While the 2006 proportions in each rating category exceed the 1993-2006 average, the nearly threefold increase in the number of downgrades to a new rating category in 2006 compared to 2005 caused the proportions maintaining the same or moving to a higher rating category in 2006 in all the investment-grade categories ('BBB-' and above) and in the 'CCC' category to fall from the very high levels recorded in 2005. The relative safety of the overall ESF market is underlined by the strong figures in the final row of Table 3, which shows that 98.47% of all observations in 2006 maintained the same or moved to a higher rating category. The lower figure of 85.71% for ratings in the 'CCC' category should be interpreted with caution due to the relatively small number of observations in that category.

If Fitch's calculations include rating changes that involve only the addition or removal of a rating modifier, such as '+' and '-', but no move to a new rating category, this noticeably increases the observed volatility of ratings. In 2006, there were 131 upgrades and 35 downgrades by one or two rating notches that did not move the rating concerned into a new rating category. For 2006 alone, the proportion of observations maintaining the same or moving to a higher rating at the modifier level was 97.3% (compared with 98.5% at the rating category level in Table 3). For 1993-2006, the corresponding proportion was 96.4% at the modifier level (97.4% at the rating category level).

Table 3: Western Europe: Proportions of Annual Observations Maintaining the Same or Moving to Higher Rating Categories by Initial Rating Category

All asset classes

(%)	2006	1993–2006
AAA	98.73	98.46
AA	98.01	97.72
A	97.96	97.31
BBB	98.87	97.10
BB	99.38	94.58
B	96.67	84.00
CCC	85.71	70.73
Average	**98.47**	**97.36**

Source: Fitch

Appendix 3 sets out the one-year transition matrix at the modifier level for all ESF asset classes for 2006 alone and the average annual matrix for 1993-2006. However, it is important to note that the transition measures for some initial rating levels may be affected by the small sample sizes involved. Transition statistics for ratings including a modifier generally need to be used with caution. Some 74% of beginning-of-year ratings between 'AA+' and 'CCC-' in the 1993-2006 data were allocated in the middle of the relevant rating category, without a modifier.

Table 4 shows the average two-year transition matrix for ESF as a whole for the 1993-2006 period. This analyses rating transitions between the beginning and end of each two-year period, beginning with 1993-1994 and moving forward in 12 annual steps until 2005-2006. Only ratings that were outstanding at both the beginning and end of any given two-year

Table 4: Western Europe: Average Two-Year Rating Transition Matrix, 1993–2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	97.05	2.28	0.46	0.14	0.07	0.00	0.00	0.00	100.00
AA	22.82	73.21	3.32	0.36	0.14	0.14	0.00	0.00	100.00
A	6.13	13.57	74.95	3.77	0.58	0.37	0.26	0.37	100.00
BBB	1.07	3.53	9.87	79.47	3.13	1.07	0.73	1.13	100.00
BB	0.41	0.83	3.73	9.94	73.50	6.63	1.04	3.93	100.00
B	0.00	0.00	0.00	6.67	5.00	51.67	15.00	21.67	100.00
CCC	0.00	0.00	0.00	0.00	0.00	3.33	36.67	60.00	100.00

Source: Fitch

Table 5: Western Europe: Average Three-Year Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	95.52	3.48	0.59	0.18	0.24	0.00	0.00	0.00	100.00
AA	27.46	66.88	4.41	0.88	0.13	0.25	0.00	0.00	100.00
A	8.86	18.79	64.97	4.76	0.74	0.74	0.49	0.66	100.00
BBB	2.44	4.68	12.65	70.35	4.57	1.59	1.17	2.55	100.00
BB	0.63	1.26	7.23	14.15	60.38	8.81	0.00	7.55	100.00
B	0.00	0.00	0.00	3.13	6.25	28.13	25.00	37.50	100.00
CCC	0.00	0.00	0.00	0.00	0.00	4.76	9.52	85.71	100.00

Source: Fitch

period are included among the observations for that period.

The higher rating volatility seen in the two- and three-year transition matrices is strongly related to the seasoning of the collateral, the structure of the transactions, as well as macro-economic factors. In particular, more seasoned portfolios are more likely to experience rating changes than pools with less seasoning.

There are also several technical reasons for expecting two- or three-year transition rates to be higher than for annual periods and this is clearly shown by comparing Tables 4 and 5 to Table 2. Table 4 is based on over 8,100 two-year observations, some 35% fewer than the number underlying the corresponding annual averages shown in Table 2. Table 5, showing a three-year average transition matrix for the first time, is based on just over 5,000 observations.

This reflects the fact that only tranches first rated in years up to 2003 are included in the three-year matrix, those rated up to 2004 in the two-year matrix, whereas tranches first rated in 2005 will show a one-year transition history. In addition, any tranches redeemed before the third or fourth calendar year-end after they were first rated will not be in existence long enough to create a two- or three-year observation, respectively.

For the average three-year data, the proportion of investment-grade observations remaining the same or moving to a higher rating category was 93.46%, just over two percentage points less than for the average two-year data, which in itself was two percentage points down on the annual data.

The increase in volatility in each of the categories from ‘AA’ down to ‘BB’ in the two-year matrix is between 10 and 14 percentage points, reflecting higher proportions of rating changes in each direction. In the large ‘AAA’ category, which can not experience upgrades, volatility increased by less than one and a half percentage points when moving to the two-year matrix. More significant increases in the proportions of downgrades were evident in the ‘B’ and ‘CCC’ categories. This reflected, in part, the relatively small numbers of observations in these categories and, in part, the continuing effects that collateral deterioration has had on a few transactions over several years. For the first time, in 2006, an upgrade from the ‘CCC’ rating category occurred in both the annual and two-year transition matrices, one tranche moving to the ‘B’ category.

Volatility in the three-year matrix increased in each rating category when compared with the two-year data. In the ‘B’ and ‘CCC’ categories, the majority of observations experienced downgrades to a lower rating category within the three-year period, although both of these categories included only limited numbers of observations.

Only one tranche experienced a downgrade to distressed levels during 2006. The class C notes of Eurostar II CDO, a high yield bond CDO, were downgraded to ‘C’ from ‘CCC’ during the year.

■ Other Perspectives on Rating Changes

Rating transition matrices present a different perspective on the measurement of rating change, compared with the frequently-quoted simple comparison of the numbers of upgrades and downgrades in the course of a year. The matrices measure transitions between one year- (or period-) end and the next, ignoring changes in the first or last calendar year (or period) of a tranche’s life. The matrices also count rating changes for “independent” tranches only, whereas the simpler measure counts all tranches subject to rating change, regardless of whether they rank pari passu with other tranches subject to change or not. In addition, the transition matrices offer more sophisticated analysis by showing the extent of the rating transition across rating categories, whereas in the simple count of upgrades and downgrades, no account is taken of the size of the rating change. Finally, the transition matrices put the numbers of rating changes into context by expressing them as a percentage of the number of observations, important in a market growing as rapidly as ESF.

During 2006, Fitch introduced another perspective on the measurement of the effect of rating change with the launch of the ESF Index of Rating Change. The index measures the change in the estimated weighted-average probability of default of ESF securities in issue as a result of rating changes. Details of the index's calculation are given in "*How Much Does Size Matter? The Measurement of Rating Change*", published on 22 November 2006 and available on the agency's website. The most recent update of the index, to Q107, was published on 25 April 2007 as "*Ahead Again – Index of Rating Change to March 2007*".

The index extends the perspective provided by the transition matrices in two directions. First it takes account of the fact that the traditional letter rating scale is not linear by using Fitch rating factors. The Fitch rating factors are estimates of the probability of default associated with each rating level. Second, the index weights each tranche in the calculation by its value outstanding at the beginning of the period. This reflects a view that investors are likely to be more affected by a change in the rating of a large tranche than they are in the case of a small tranche.

Table 6 shows the changes in the index, measured over calendar years, alongside the simple ratio of upgrades to downgrades for the year, including all pari passu tranches affected, and a common summary measure from transition analysis, the percentage of tranches whose ratings remained at the same or moved to a higher rating level (including any modifier) in each year.

All three measures agree that 2003 was a year of weak rating performance, although that is perhaps most marked by the index measure, influenced by a number of multi-notch downgrades to speculative-grade ratings, particularly among CDOs and the Welcome Break ABS transaction, causing the probability of default to deteriorate markedly.

The index presents a much weaker picture than the other measures for 2004. The index in 2004 was particularly affected by the downgrade of the very large USD1.57bn class A1 notes of the CDO Sabre Funding No 1 Limited to 'CCC' (a Fitch rating factor of 48.52) from 'BBB' (Fitch rating factor of 3.74). This downgrade alone accounted for 13.8 percentage points of the 18.2% decline in the index. Even after recognising that factor, however, the index still presents a more negative picture than either of the other two measures, again reflecting the fact that the downgrades in 2004, on average, carried more weight in terms of value and size of movement than the upgrades.

Table 6: Western Europe: Alternative Measures of Rating Change

	Index of rating change (% change)	Upgrades/ downgrades	Transition: maintained same or higher rating level (% of observations)
2003	-11.3	96/147	90.46
2004	-18.2	153/68	97.33
2005	+5.1	409/37	99.01
2006	+2.3	433/116	97.35

Source: Fitch

In 2005 and 2006, the upgrade/downgrade ratio was boosted by a number of upgrades for relatively small mezzanine and junior tranches in amortising RMBS issues, as a result of which the average downgrade in each year had a more significant effect on the index than did the average upgrade. In 2006, for example, 13 of the downgrades were a result of the downgrade of the rating for the Republic of Italy to 'AA-' from 'AA', but the affected tranches were large, totalling EUR12.1bn. The steady increase in outstandings in the market also dampened the effect of individual rating changes in both directions on the weighted-average probability of default in each succeeding year.

Fitch continues to offer the broader perspective provided by the ESF index of rating change by publishing quarterly updates to the index for the market as a whole and by asset class early in each calendar quarter.

Performance by Asset Class

Table 7 summarises the pattern of rating changes to new rating categories by asset class in 2006. Overall volatility of 9.1% is modestly lower than in 2005 (10.4%) and the upgrade/downgrade ratio has fallen substantially, to 4.9:1 in 2006 from 16.4:1 in 2005. The largest single factor behind these changes was a less positive year for CDOs, with 73 fewer upgrades and 36 more downgrades than in 2005.

The substantial differences between the numbers of upgrades and downgrades in the final lines of Tables 6 and 7 reflect differences in definition: Table 6 includes all upgrades and downgrades of one notch or more affecting all tranches with ratings at the beginning and end of the year; the numbers in Table 7 are on the transition study definition, including only one of each set of pari passu tranches outstanding and counting only rating changes to a new rating category, omitting notch movements that leave the rating within the same rating category.

Table 7: Western Europe: Rating Changes During 2006 (Independent Tranches Moving to a New Rating Category Only)

	Upgrades	Downgrades	Total changes (% of obs)
ABS	4	3	7 (2.6)
CDO	112	39	151 (12.0)
CMBS	34	4	38 (10.2)
RMBS	85	2	87 (7.1)
All ESF	235	48	283 (9.1)

Source: Fitch

Table 8: Western Europe: Proportion of Investment-Grade Observations Maintaining the Same or Moving to Higher Rating Categories (Annual Averages by Asset Class)

(%)	2006	1993–2006
ABS	98.83	97.97
CDO	96.79	95.78
CMBS	99.11	98.93
RMBS	99.91	99.63
All ESF	98.46	97.79

Source: Fitch

Rating volatility, as measured in Table 7, fell in all asset classes except RMBS, where upgrades almost doubled to 85 from 44 in 2005, lifting volatility to 7.1% from 5.3% in 2005.

A good summary indicator of transition performance in the Western European market is the proportion of investment-grade observations (rated 'BBB-' or above) that remain in the same or move to a higher rating category. Table 8 shows that performance measured by this indicator was stronger in 2006 than for the average of the whole period 1993-2006 for each asset class, for the second year in a row. This reflects the continued recovery from the difficult credit environment of 2001-2003.

There is a suggestion in these data that the upswing in this phase of the ESF credit cycle is beginning to flatten out, since the proportions of investment-grade observations maintaining the same or moving to a higher rating category fell in 2006 for ESF as a whole and for three of the four main asset classes. Only in RMBS did this proportion improve, due to a reduction in the already small number of downgrades during the year.

It is interesting to look at the experience of ABS, CMBS and RMBS as a group, excluding CDOs, which at times have performed differently to the other three sectors. Table 9 shows the average annual transition matrix for these three sectors for 1993 to 2006. Investment-grade securities in these sectors have performed very strongly, with 99.1% of investment-grade observations maintaining the same or moving to a higher rating category. Performance has been weaker in the speculative grades, although the limited numbers of observations in these categories means that the figures need to be interpreted with caution: there were 13 downgrades of 'BB' tranches, four of 'B' tranches and only two in the 'CCC' category.

Table 10: Western Europe: Numbers of Observations by Year by Asset Class

	2004	2005	2006	1993–2006
ABS	293	291	269	1,820
CDO	1,149	1,270	1,259	5,048
CMBS	238	257	373	1,335
RMBS	753	903	1,227	4,294
All ESF	2,433	2,721	3,128	12,497

Source: Fitch

Table 10 shows that the ESF market continues to grow strongly, with the number of independent observations in 2006 being more than 400 or some 15% greater than in 2005. As a result, the total number of observations over the 1993-2006 period increased by 33% to over 12,000. The growth was led by the RMBS sector, with a strong contribution also from the much smaller CMBS sector. The CDO sector, which has been one of the main engines of the market's growth since 1998, experienced a modest decline in its number of observations in 2006,

Table 9: Western Europe: Average Annual Rating Transition Matrix, 1993–2006 ABS + CMBS +RMBS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.73	0.27	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	8.89	90.54	0.57	0.00	0.00	0.00	0.00	0.00	100.00
A	1.42	7.64	89.51	1.42	0.00	0.00	0.00	0.00	100.00
BBB	0.41	0.48	5.59	91.96	1.36	0.07	0.00	0.14	100.00
BB	0.00	0.26	0.78	6.23	89.35	2.08	0.26	1.04	100.00
B	0.00	0.00	0.00	0.00	0.00	84.62	7.69	7.69	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	60.00	40.00	100.00

Source: Fitch

Table 11: Western Europe: One-Year Rating Transition Matrix, 2006 – ABS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	0.00	100.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.00	2.82	94.37	2.82	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	1.89	96.23	1.89	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	10.00	90.00	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

the first year in which that has happened. This is the result of redemptions and retirements of previous years' CDO tranches modestly outnumbering new issues in 2006. However, CDOs remain the largest sector in the study, with just over 40% of 2006's observations.

The following sections comment on each of the main asset classes in turn, looking behind the aggregate figures where appropriate.

ABS

Overall in 2006, 98.8% of investment-grade observations in the ABS sector maintained the same or moved to a higher rating category, a modest increase from the 98.2% seen in 2005.

At the rating modifier level, 3.0% of observations showed upgrades and 3.7% recorded downgrades, giving a ratio of upgrades to downgrades of 0.8. The effect of the transitions of ABS securities to new rating categories in 2006 alone is shown in Table 11.

Table 12 shows the average annual transition matrix for 1993-2006.

Consumer ABS

The Fitch pan-European consumer index report, "*Eye on Europe – The Fitch European Consumer ABS Performance Index 2007 (Vol I)",* published on 18 April 2007 and available on the agency's website, explained that the performance of securitised consumer assets in Europe deteriorated in H106, mainly due to poor performance in the UK credit card sector.

However, excluding UK credit card ABS, the European consumer ABS sector experienced positive performance in 2006, as indicated by several Fitch rating upgrades. These included Italian leasing ABS such as Agri Securities S.r.l., Agri Securities S.r.l. Series 2002-1, Mecenate Leasing S.r.l., Mercantile Finance S.r.l., and Venice, Portuguese consumer/auto ABS such as Lusitano Finance No. 2, Nova Finance No. 2, BMORE No. 2 and Silk Finance No. 2 Plc. and a Spanish consumer ABS, Santander Consumer Finance Spain 02-1. The upgrades typically resulted from the highly seasoned nature of some of the transactions and consequent increased levels of credit enhancement. Fitch also took into consideration the positive performance of these transactions in terms of delinquency, default and loss, and excess spread ratios. For all upgraded tranches, Fitch's default and loss transaction parameters were better than the agency's expectations set at closing and enough excess spread was available to cover losses.

Credit Cards

There was one independent downgrade in 2006 for UK credit card ABS, the first of its kind, and no upgrades. Fitch downgraded certain pari passu tranches in the Pillar master trust. The performance of the UK credit card transactions deteriorated in 2006 and Fitch published several press releases and special reports commenting on that in general and on a deal-specific basis. The negative performance exhibited by UK credit cards was mainly driven by a sharp increase in charge-offs observed in all trusts to the extent that most have breached Fitch's base-case assumptions. This sharp increase was driven by a

Table 12: Western Europe: Annual Average Rating Transition Matrix, 1993–2006 – ABS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.53	0.47	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	4.11	94.06	1.83	0.00	0.00	0.00	0.00	0.00	100.00
A	0.94	3.38	93.42	2.26	0.00	0.00	0.00	0.00	100.00
BBB	0.60	0.00	2.11	92.45	4.23	0.30	0.00	0.30	100.00
BB	0.00	0.00	1.30	5.19	85.71	3.90	0.00	3.90	100.00
B	0.00	0.00	0.00	0.00	0.00	75.00	12.50	12.50	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	33.33	66.67	100.00

Source: Fitch

Table 13: Western Europe: One-Year Rating Transition Matrix, 2006 – CMBS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	16.25	83.75	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	7.14	8.33	80.95	3.57	0.00	0.00	0.00	0.00	100.00
BBB	1.32	0.00	6.58	92.11	0.00	0.00	0.00	0.00	100.00
BB	0.00	3.45	0.00	3.45	93.10	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	85.71	14.29	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

combination of deterioration in the consumer debt environment and a sharp increase in bankruptcies and individual voluntary arrangements (IVAs). Yield and monthly prepayment rates (MPRs) have remained reasonably stable across all trusts. Excess spread has deteriorated as a result of stable yield and rise in charge-offs and the trapping mechanisms have been triggered in several Fitch-rated trusts.

In April 2006, Fitch issued a press release warning that changes to delinquent account management at Egg, the originator and servicer, were a potentially significant modification to the profile of the credit card portfolio as they made the level of charge-offs reported to date not comparable with charge-off policies typically applied in credit card transactions, thus leading to uncertainties over charge-off levels. As a result of these changes, and because of a marked deterioration in trust performance, Fitch downgraded all class C notes of Pillar to ‘BBB-’ from ‘BBB’ in October. These notes were subsequently put on Rating Watch Positive in April 2007, following a return to more conservative data reporting and the issue of a private note to increase the credit enhancement available to the class C notes.

European Corporate ABS (Excluding Whole Business)

Performance has remained remarkably stable in 2006. As corporate ABS (excluding whole business securitisation (WBS)) is a broad, heterogeneous asset group, any rating actions are usually attributable to situations specific to the transaction rather than any generalised trends across the sector, including the case of corporate securitisations, which are often exposed to seller/servicer risk.

In the case of Cassa Depositi e Prestiti TAV (ISPA TAV), Fitch downgraded all series to 'AA-' from 'AA' due to counterparty, as opposed to performance, reasons. This is because the ratings of these series are credit-linked to the foreign and local currency Issuer Default Ratings of the Republic of Italy and these were downgraded in Q4.

Of the European aircraft transactions, Fitch downgraded two tranches of Iberbond 2000 Ltd in Q106 as a result of asset value declines since the transaction closed. All ratings for the other two Iberbond transactions (1999 and 2004 Plc) were affirmed. In general, aircraft values and lease rates have shown a marked recovery since the trough of 2002–2003.

Whole Business

In 2006, the overall performance of WBS transactions was stable with six tranches downgraded (from Craegmoor Funding No 2 Ltd and Wightlink Finance Ltd) and three junior tranches (Avebury Properties Ltd, UK Care No 1 Ltd, PHF Securities No 1 Ltd) upgraded. Fitch lowered the ratings of the class B1, B2 and M notes of Craegmoor, as well as the underlying ratings of its senior tranches, which are guaranteed by a monoline insurer, as a result of performance issues, largely relating to poor cost control. However, the performance of Craegmoor seems to have entered a stable or improving stage and in Q107 Fitch removed the Rating Watch Negative placement from certain of its ratings on Craegmoor. The single-tranche Wightlink transaction was downgraded to speculative grade from ‘BBB’, again due to performance issues, but was redeemed shortly after

Table 14: Western Europe: Average Annual Rating Transition Matrix, 1993–2006 – CMBS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.68	0.32	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	10.96	88.70	0.33	0.00	0.00	0.00	0.00	0.00	100.00
A	3.42	7.76	86.34	2.48	0.00	0.00	0.00	0.00	100.00
BBB	1.10	1.47	3.66	92.67	1.10	0.00	0.00	0.00	100.00
BB	0.00	0.89	0.89	4.46	90.18	2.68	0.00	0.89	100.00
B	0.00	0.00	0.00	0.00	0.00	90.91	9.09	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 15: Western Europe: One-Year Rating Transition Matrix, 2006 – RMBS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	11.67	88.33	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.39	12.84	86.77	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.41	11.16	88.02	0.41	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	3.03	95.45	1.52	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

this rating action. The transition study records only two upgrades and two downgrades in this sub-sector, because underlying ratings for guaranteed tranches are not included in the study and several other rating actions affected pari passu tranches or tranches redeemed during the year.

The UK pub sector's performance remained stable in 2006 despite changes in regulations (smoking ban in Scotland in March 2006, new licensing regime in England and Wales) and the persistence of cost pressures (above-RPI increases in national minimum wage, utilities, Sky TV). In the sale-and-leaseback nursing home sector, several transactions have been redeemed to date, following upgrades due to improved performance over the past two years. In other sectors, performance was transaction-specific but generally stable.

Since January 2007, WBS are no longer rated by Fitch's European Corporate ABS team but rather by Fitch's Global Infrastructure and Project Finance Group.

CMBS

European CMBS continued to perform strongly throughout 2006, as shown in Table 13, almost matching the good performance of the previous year. Out of nearly 380 tranches rated by Fitch in 2006, the surveillance group upgraded 49 independent tranches at the modifier level and downgraded six, compared to 44 upgrades and three downgrades in 2005.

Three of the transactions downgraded in 2006 were credit-linked to the Issuer Default Ratings of telecommunications companies: British Telecom is the main tenant in Premiertel and Telereal whereas Imser featured Telecom Italia. When both companies were downgraded to 'BBB+' from 'A-' in 2006, all credit-linked tranches in the three transactions were downgraded to reflect the reduced credit quality of the tenants. In addition, two further downgrades of a similar character were also seen on a modifier level in relation to FIP Funding and Mutina in October 2006, when the foreign and local currency Issuer Default Rating of the Republic of Italy was lowered to 'AA-' from 'AA'.

Only one of the downgrades was directly related to the performance of a transaction itself, this being Coronis (European Loan Conduit No. 8) Plc, issued in 2001. The class F notes of that deal were downgraded to 'CCC+' from 'B' due to the underperformance of the Bridge Properties Investments Limited loan and the increased likelihood of a loss allocation to the junior notes. Triggered by financial problems of the largest tenant, the borrower had been unable to top up the previously depleted escrow accounts. In addition, the interest coverage ratio fell below the default trigger of 1.1x. Both events constituted an event of default.

On the more positive side, the upgrades were predominantly triggered by a high volume of prepayments and better performance of the assets in the CMBS portfolios, which contributed to an increase in credit enhancement levels for those transactions. The majority of the upgrades occurred within the UK, as a reflection of stable economic conditions and a robust real estate market.

Table 16: Western Europe: Average Annual Rating Transition Matrix, 1993–2006 – RMBS

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.82	0.18	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	9.68	90.13	0.19	0.00	0.00	0.00	0.00	0.00	100.00
A	1.05	9.78	88.49	0.67	0.00	0.00	0.00	0.00	100.00
BBB	0.12	0.35	7.53	91.54	0.35	0.00	0.00	0.12	100.00
BB	0.00	0.00	0.51	7.65	90.31	1.02	0.51	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	85.71	0.00	14.29	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

Table 17: Western Europe: One-Year Rating Transition Matrix, 2006 – CDOs

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	97.27	2.56	0.17	0.00	0.00	0.00	0.00	0.00	100.00
AA	18.77	77.01	3.83	0.38	0.00	0.00	0.00	0.00	100.00
A	1.71	18.29	76.00	4.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	1.26	10.06	86.16	1.89	0.63	0.00	0.00	100.00
BB	0.00	5.36	1.79	5.36	87.50	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	6.25	6.25	87.50	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	20.00	60.00	20.00	100.00

Source: Fitch

Despite the adverse economic circumstances in Italy, the performance of the non-performing deals also appeared to be positive throughout 2006. 14 tranches in this sub-sector were upgraded through the year, due to much better performance than expected by Fitch at the time of issuance.

RMBS

2006 saw a further improvement, to 99.91%, in the percentage of investment-grade observations in RMBS that maintained the same or moved to a higher rating category, slightly above the long-term average of 99.63%. The rating transition matrix for 2006 is shown in Table 15, while the annual average rating transition matrix for the period 1993-2006 is set out in Table 16.

In 2006, two prime tranches and three sub-prime tranches were downgraded at the modifier level, following comparative totals of eight downgrades in 2005 and five in 2004.

Across Europe, notably in less seasoned deals in the UK sub-prime sector and also in Portugal, arrears continue to rise as interest rates rise. As a result, the outlook for ratings in the sub-prime sector is stable while that for prime is stable to positive.

Prime RMBS

German RMBS again produced the only performance-related downgrades in the prime arena, following poor collateral performance in Provide Home 2001-1. At the time of the downgrade approximately one third of the portfolio consisted of second-lien loans. Given experience elsewhere in the German RMBS market, these loans are expected to adversely impact on loss severities as all first-lien loans must be paid in full ahead of the second charge loans. Previous years' downgrades related to Provide GEMS, all tranches of which were affirmed during 2006, following downgrades in each of the previous two years.

On a positive note, upgrades from one rating category to another totalled over 60 as increased prepayment rates in many countries, together with predominantly sequential pay-down structures, led to healthy growth in credit enhancement. The Netherlands accounted for a majority of the upgrades, as in 2005, as performance of Dutch RMBS remained strong throughout 2006. In the UK, 10 independent tranches were upgraded to new rating categories solely as a result of the review of the first 10 issues from the so-called "capitalist" structure of the Granite master trust.

Sub-Prime RMBS

May 2006 saw the first performance-related downgrade of any UK sub-prime tranches when the class M2a, B1a and B2a notes from Farringdon Mortgages No. 1 were downgraded. The first two classes did not change rating category, each being downgraded by one notch, while the B2a notes were downgraded to 'B' from 'BB'. The rating actions followed high arrears and unexpected expenses in the transaction.

Higher arrears and losses were seen across the sector during 2006, predominantly in issues from recent entrants to the market. While rising interest rates accounted for some of the increase, it is also worth noting that these new players have more aggressive

Table 18: Western Europe: Average Annual Rating Transition Matrix, 1993–2006 – CDOs

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	96.69	2.88	0.37	0.05	0.00	0.00	0.00	0.00	100.00
AA	14.33	81.73	3.40	0.37	0.09	0.09	0.00	0.00	100.00
A	3.15	8.86	82.52	3.73	0.70	0.70	0.00	0.35	100.00
BBB	0.52	1.93	6.06	86.08	2.58	1.42	1.03	0.39	100.00
BB	0.00	0.90	0.60	4.78	85.97	4.18	1.79	1.79	100.00
B	0.00	0.00	0.00	4.05	2.70	77.03	9.46	6.76	100.00
CCC	0.00	0.00	0.00	0.00	0.00	2.78	69.44	27.78	100.00

Source: Fitch

underwriting criteria than the more established market participants.

Following the recovery in the UK mortgage market in 2006, principal payment rates increased during the year. As a consequence, and despite the reversion to pro rata pay down for some deals, performance reviews of the more seasoned transactions resulted in over 20 independent tranches being upgraded, up from the six upgrades seen in 2005.

The UK continued to account for all issues in this sector in 2006.

CDOs

In 2006, European CDOs demonstrated strong ratings performance relative to the aggregate historical data set; however, performance has slightly deteriorated relative to 2005, which was a remarkably stable year. With the exception of the 'BB' and 'B' categories, which experienced no downgrades in 2005 or 2006, the percentage of tranches downgraded increased in 2006 relative to 2005. However, when 2006 transition figures are compared to transition figures collected from 1993 onward, 2006 still demonstrates relatively strong performance. With the exception of a marginal decline in the 'AA' category, all categories showed a higher percentage of ratings that either maintained or improved.

There were 89 downgrades in 2006, measured at the modifier level and including pari passu tranches, relative to 15 downgrades in 2005. All CDO upgrade and downgrade figures presented in the following sub-sections are on a comparable basis. The increase in downgrades was largely due to exposure to the US automotive industry as well as general credit deterioration as a result of leveraged corporate acquisitions. As stated in Derivate Fitch's 2007 outlook piece *("2007 Global CDO and Credit Derivatives Outlook"*, published 13 December 2006), this trend is expected to continue throughout 2007.

Balance Sheet SME CLOs

European balance sheet CDOs experienced strong performance in 2006 with 32 tranches upgraded, and 40 fully redeemed. 137 tranches were affirmed, and there were no downgrades. Most of the upgrades were the result of increases in credit enhancement due to robust deleveraging within the Spanish SME market.

IG Corporates and CDO-Squared

The majority of the downgrades in 2006 were isolated to the synthetic corporate CDOs forming the inner level of CDO-squared transactions. These transactions are often tightly structured with very little cushion above the required subordination levels.

Leveraged Loan CLOs

CDOs backed by leveraged loans enjoyed a solid year with 154 affirmations, no downgrades and one upgrade. 38 tranches were redeemed in full. As most of the CLOs remained in the reinvestment period, upgrades were rare. As transactions exit the reinvestment period and begin to amortise sequentially, upgrades are expected to become more frequent.

High Yield Bond CDOs

These are primarily older-vintage transactions that are well into the amortisation period. Despite past problems, the sector has benefited from deleveraging. In 2006, eight tranches were upgraded, and only one tranche suffered a downgrade. 28 tranches were affirmed and six tranches were fully redeemed.

Structured Finance CDOs

Structured finance CDOs experienced strong performance driven by deleveraging. 47 tranches were upgraded in 2006 and only one tranche suffered negative rating action. 81 tranches were affirmed and 25 were fully redeemed.

■ Performance by Country

The performance of ESF tranches classified according to the country in which the majority of the assets are based is examined in the following section. The six largest issuing countries (France, Germany, Italy, the Netherlands, Spain and the UK (and Ireland)) are each discussed separately in this analysis, while the remaining European countries are grouped together in an "Other" category.

Where transactions are backed by collateral from a variety of different countries, they have been excluded from this part of the analysis. This enables a meaningful comparison of performance by country for the jurisdictions listed. In practice, the transactions excluded for this reason are, in the main, CDOs backed by international collateral from both European and non-European obligors, although a small number of pan-European CMBS transactions are also excluded.

Table 19 shows the performance of each of the country groups in the study both for 2006 alone and for 1993-2006, measured as the proportion of investment-grade observations maintaining the same or moving to a higher rating category.

Table 19: Country Performance: Proportion of One-Year Investment-Grade Observations Maintaining the Same or Moving to a Higher Rating Category (%)

Country	2006	1993–2006
Netherlands	100.00	100.00
Other	100.00	99.46
France	100.00	99.41
Spain	99.66	99.52
Germany	99.65	98.93
UK (& Ireland)	99.54	99.12
Italy	99.19	98.69

Source: Fitch

For all the countries, the 2006 performance on this measure was equal to or better than the long-term average, reflecting the improved general credit environment. Neither the Netherlands, France nor the Other group of smaller countries experienced any downgrades during 2006. For comparison, the tranches backed by multi-country collateral and excluded from the country analysis have performed rather less well: in 2006, 96.01% of investment-grade observations in this dataset maintained the same or higher rating category, while for 1993-2006 this proportion was as low as 94.66%.

Table 20 goes on to show the numbers of upgrades and downgrades to a new rating category in 2006 by country segment, placing this in context by showing the number of observations from each country as well.

For the second year in a row, the Netherlands experienced the highest number of rating changes, with 42 upgrades and no downgrades, as well as displaying the highest volatility with 14% of observations resulting in a change to a new rating category.

The UK was again much the largest market, accounting for 34% of total country-specific observations in 2006, more than double the share of the next largest, Germany. The Spanish and Dutch markets enjoyed strong growth in observations as a result of new issues comfortably outpacing retirements and both countries moved ahead of Italy on this measure.

France, the smallest public market identified here, had the fewest rating changes, with four upgrades and no downgrades. However, the least volatile of the country groups was the Other Countries group, where only 3% of observations experienced migration to a new rating category, all upgrades.

Table 20: Numbers of Upgrades, Downgrades and Total Observations by Country, 2006 Only

Country	Upgrades	Downgrades	No. of observations
UK (& Ireland)	31	5	716
Germany	25	1	329
Spain	22	1	307
Netherlands	42	0	304
Italy	22	2	253
Other	5	0	154
France	4	0	67

Note: Changes to a new rating category only
Source: Fitch

The multi-country transactions that lie outside this country analysis accounted for 998 independent observations in 2006, 84 of them being upgrades to a new rating category and 39 downgrades.

The following sections show the annual average rating transition matrices for each identified country for 1993-2006, together with a commentary on performance. *Appendix 4* shows the one-year 2006 tables for each country.

UK (Plus Ireland)

The UK and Ireland experienced a higher number of rating transitions in 2006, following something of a reduction in 2005. In 2006, 60 independent tranches were upgraded at the modifier level, up from the 31 upgrades seen during 2005. Eight independent tranches were downgraded in 2006, again at the modifier level, up from six in 2005. Long-term performance at the rating category level is summarised in Table 21.

The majority of 2006 upgrades were to tranches from RMBS deals, 60% of which were prime and 40% UK non-conforming. The latter sub-sector experienced a pick-up in the rate at which the portfolios paid down, following the slow-down in the UK mortgage market in 2005. Also, several lenders adopted a more aggressive stance with regards to possession procedures, instructing lawyers once borrowers are two months in arrears, rather than waiting for them to be three months down.

These two factors have resulted in greater build-up in credit enhancement, allowing more upgrades.

Rating actions in UK prime RMBS transactions were driven by the January 2006 upgrades to the so-called “capitalist” deals from Northern Rock’s Granite master trust.

Table 21: UK and Ireland: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.90	0.10	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	5.83	93.95	0.22	0.00	0.00	0.00	0.00	0.00	100.00
A	1.66	5.12	91.69	1.52	0.00	0.00	0.00	0.00	100.00
BBB	0.44	0.44	3.82	93.53	1.76	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	6.15	89.39	2.23	0.00	2.23	100.00
B	0.00	0.00	0.00	0.00	0.00	85.71	14.29	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	33.33	66.67	100.00

Source: Fitch

Overall in the UK mortgage market, arrears, possessions and losses are on the increase as the three interest rate rises from August 2006 to date, coupled with higher energy and council tax bills, start to have an impact on borrowers' disposable income. However, performance generally remains in line with expectations.

The downgrades in the UK were spread across the three asset classes other than CDOs and affected the non-conforming transaction Farringdon Mortgages No 1 plc, the whole-business deal Craegmoor Funding No.2 Ltd, the class C notes issued from the Pillar Funding Master Trust (as explained in *ABS – Credit Cards* above) and the CMBS deals Premiertel plc, Telereal Securitisation plc and Coronis (European Loan Conduit No 8) plc.

Germany

In Germany, the stable to positive performance trend from 2005 continued in 2006 across all asset classes. Measured at the modifier level and counting actions affecting independent tranches only, upgrades comfortably outnumbered downgrades by 33:2 (25:9 in 2005), mainly owing to a number of upgrades in the SME CDO sector. At the same time, 294 ratings were affirmed.

The only negative rating actions (one across rating categories, one at the modifier level) affected classes C and D of the Provide Home 2001-1 transaction, a synthetic RMBS structure referencing a pool of mortgage loans originated by Aareal bank. Other classes of more seasoned RMBS transactions were either affirmed or upgraded by one notch reflecting the otherwise stable to positive performance of the segment.

Most of the upgrades to a new rating category related to SME CDO transactions, similar to last year's pattern. In particular, transactions with longer performance histories have shown a reduction in the average outstanding defaults due to more of their defaulted loans reaching the completion of the workout stage. Realised losses have only slightly increased as recoveries have remained at high levels. The performance expectation for the SME sector is positive based on the improved economic environment evidenced by decreasing corporate insolvencies for the second consecutive year. On the other hand, the more concentrated transactions in the mezzanine CLO segment will remain an area to watch as individual insolvencies can significantly affect their performance.

The ABS sector, dominated by auto ABS transactions, has again shown a stable performance despite increasing private insolvencies. Underwriting guidelines have so far effectively protected the transactions against any negative impact. A stable to positive development is expected for 2007 in light of the economic recovery and lower unemployment rates.

The German CMBS sector is continuously gaining importance given the record issuance levels of 2006 mainly caused by the large multifamily transactions. In 2006, three tranches of a seasoned transaction (Real Value One) were upgraded based on the strong performance and the deleveraging of the deal. Most

Table 22: Germany: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.33	0.67	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	7.55	91.98	0.47	0.00	0.00	0.00	0.00	0.00	100.00
A	1.05	6.27	90.59	2.09	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.74	3.69	94.46	1.11	0.00	0.00	0.00	100.00
BB	0.00	1.92	1.28	2.56	92.31	1.28	0.64	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	83.33	8.33	8.33	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

Table 23: Italy: Average Annual Rating Transition Matrix, 1993–2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.72	0.28	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	10.84	87.95	1.20	0.00	0.00	0.00	0.00	0.00	100.00
A	2.93	7.69	86.81	2.56	0.00	0.00	0.00	0.00	100.00
BBB	1.05	1.05	3.68	92.63	1.58	0.00	0.00	0.00	100.00
BB	0.00	0.00	5.26	2.63	89.47	2.63	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

of the more recent structures will only enter their first review during the course of this year.

Italy

2006 was another year of very good performance for Italian securitisation deals as summarised in Table 3 in *Appendix 4*, with 37 upgrades to independent tranches at the modifier level and nine downgrades. Similar to 2005, the downgrades affected mainly deals credit-linked to the rating of a specific entity (corporate or public) as a result of the downgrade of the reference entity. This was the case for the Cassa DP TAV bonds, following the downgrade of Cassa Depositi e Prestiti, for Patrimonio Uno and FIP Funding, following the downgrade of the Italian Republic and for the IMSER transaction, credit-linked to Telecom Italia.

The overall performance of the Italian market for the period 1993-2006 is described in Table 23. In particular, it should be noted that the positive performance trend already seen in the past three years, has continued also in 2006. With the growth of the market and the number of upgrades registered in the past three years, the marginal contribution of the few deals that have recorded downgrades in the past is diminishing and this is reflected in improving performance numbers. For example, the percentage of ‘AAA’ observations that remained unchanged for one-year transitions over 1993-2006 has improved slightly compared with the 1993-2005 transition matrix moving to 99.72% from 99.65% (it was 99.16% for 1993-2003).

The Italian CMBS sector, during 2006, showed an excellent performance and benefited from a number of upgrades, especially in the non-performing loan (NPL) sector. As noted above, three CMBS deals, Patrimonio Uno, FIP Funding and Imser, were downgraded due to their credit link to entities that have been downgraded in 2006.

The Italian ABS sector has seen downgrades for TAV bonds, credit-linked to Cassa Depositi e Prestiti. On the other hand, this sector has seen five upgrades of leasing transactions due to good performance of the underlying portfolios.

The RMBS sector in Italy has shown a very good performance in terms of rating actions, with 14 tranches upgraded and no downgrades.

Fitch does not expect to see any significant change to this positive picture throughout 2007, and, taking into consideration the improvements in the Italian economy seen during 2006, expects the credit outlook for Italian deals to remain stable.

The Netherlands

The Netherlands, as in 2005, saw strong performance throughout 2006. RMBS continues to dominate issues from the country with some 85% of observations in this year’s study coming from this asset class. Other asset classes are experiencing an increased share of Fitch-rated Dutch deals, hence explaining the 5 percentage point drop in the RMBS share over the year to end-2006. The absence of downgrades to a new rating category is again evident in the 1993-2006 transition matrix in Table 24.

Table 24: Netherlands: Average Annual Rating Transition Matrix, 1993–2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	26.61	73.39	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.40	17.39	82.21	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.40	13.20	86.40	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	9.88	90.12	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 25: Spain: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	23.85	74.62	1.54	0.00	0.00	0.00	0.00	0.00	100.00
A	0.00	12.95	86.01	1.04	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	8.33	91.67	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	18.92	81.08	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

In November 2006, 51 tranches of Dutch RMBS were upgraded at the modifier level. These upgrades followed healthy growth in credit enhancement, as pay-down of the notes is sequential. Also, the rate of pay-down of the portfolios increased as competition intensified in the Dutch mortgage market.

The effects of the recession of 2003 appear to have been worked out, as arrears began to trend downwards from mid-2005. Many lenders have introduced more active strategies with regards to foreclosures and, as a result, losses are expected to stabilise. Even during the recession, Dutch house prices remained very stable.

These changes in practice have been reflected in data from Kadaster, which show that although the number of foreclosures rose to nearly 2,000 in 2005 from just over 1,500 in 2004, the final total for 2006 is expected to be slightly lower at around 1,800.

Spain

The performance of Spanish transactions in 2006 was excellent with a total of 48 independent tranches being upgraded at the modifier level and only two being downgraded. The downgrades affected both classes of notes issued by Iberbond 2000 Ltd, an aircraft financing transaction, with the class A notes downgraded to ‘A-’ from ‘A+’ and the class B notes going to ‘BBB’ from ‘A-’.

Table 5 in Appendix 4 shows the one-year rating transition rate of all outstanding Spanish tranches rated by Fitch for calendar year 2006. As can be seen, the upgrade activity concentrated on tranches starting the year with ratings in the ‘AA’, ‘A’ and ‘BBB’ categories. The majority of upgrades occurred in RMBS and CDO transactions, with one ABS deal being upgraded.

The RMBS sector accounted for the majority of upgrades at the modifier level during 2006 with 30 tranches being upgraded. The underlying pools of assets on existing deals continue to perform well, backed by the strong Spanish economy and the still strong housing market during 2006. This very positive rating migration is a consequence of the healthy performance of the outstanding transactions and delinquency levels which, although slowly increasing, remain low in comparison to other European countries.

CDO deals also performed strongly in 2006, with 17 upgrades to independent tranches. There were no downgrades and 130 independent tranches were affirmed. For the SME market, the Spanish SME CDOs continued to be among the best performing markets in the region with the lowest level of cumulative delinquencies and defaults in Europe. With regards to CDOs of Cedulas Hipotecarias (CHs), the adequate collateralisation ratios of all the CH issuers contributed to the affirmation of their ‘AAA’ credit ratings.

Last but not least, one auto loan securitisation deal had a tranche upgraded at the modifier level in 2006.

This good performance not only reflects the favourable economic environment in Spain but also stems from the fact that the underlying assets are

Table 26: France: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	99.38	0.62	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	2.56	97.44	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.96	1.92	97.12	0.00	0.00	0.00	0.00	0.00	100.00
BBB	2.94	2.94	5.88	85.29	0.00	0.00	0.00	2.94	100.00
BB	0.00	14.29	0.00	0.00	85.71	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 27: Other Countries: Average Annual Rating Transition Matrix, 1993–2006
All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	6.43	93.57	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.84	8.44	90.30	0.42	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	5.43	91.30	2.17	0.00	0.00	1.09	100.00
BB	0.00	0.00	0.00	5.00	90.00	5.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

granular, standard, amortising assets, and fairly stable in the long run.

France

2006 was another year of stable performance for the relatively small French public securitisation market. Out of 67 independent tranches issued against French portfolios, four were upgraded during the course of the year and there were no downgrades.

The four upgraded tranches related to two CMBS transactions: Titan Europe 2004-2 plc and Leto (European Loan Conduit No. 18) FCC. The positive rating actions in these two multi-borrower deals were mainly triggered by significant prepayment of the portfolios which, in turn, resulted in improved credit enhancement levels.

Other Countries

This category covers ESF transactions from the remaining western European countries surveyed by Fitch, i.e. Austria, Belgium, Finland, Greece, Portugal, Sweden and Switzerland. Just over half the observations in this group in 2006 came from Portugal, with the remainder widely spread.

As shown in Table 7 in *Appendix 4*, there were no negative rating actions affecting securitisations from any of these countries in 2006. In contrast, five tranches were upgraded, four of which were issued from two RMBS transactions: Portugal's Nostrum Mortgages 2003-1 Plc and Sweden's Farms Securitisation Limited. The fifth upgraded tranche related to a Portuguese ABS portfolio of auto loans: Lusitano No. 2 Plc. These positive rating actions were mainly caused by payoffs and ongoing amortisation.

■ Subsequent Developments

Fitch publishes regular summary information on rating actions and sector outlooks within ESF during the course of each year. In particular, recent performance information has been reviewed in "*European and Asia Pacific Structured Finance – Q107 and End-2006 Rating Performance Update*", published on 25 June 2007. The ESF Index of Rating Change, referred to on pages 5 and 6 above, is also updated in the first month of each calendar quarter, most recently in "*Ahead Again – Index of Rating Change to March 2007*", published on 25 April 2007. These reports are available on the agency's website.

Appendix 1

Methodology

In producing the transition tables, all rating transitions were weighted identically, regardless of the year of the observation. A ***"transition"*** for a specified period compares the beginning-of-period rating with the end-of-period rating for each tranche in the study. Each independent rated tranche (see *Pari Passu Tranches* below) counts equally, regardless of its value.

To calculate transition rates, cohorts were created for each year (or two years) of the study period. A one-year ***"cohort"*** is defined as a fixed pool representing the number of ***"observations"*** of ratings outstanding at both the beginning and end of a respective year. Cohorts should not be confused with ***"vintages"***, which represent the year in which a transaction came to market.

In calculating average transition rates over the whole period of the study, the transition rates for the individual cohorts in the period are weighted by the number of observations in each cohort. This leads to a fair evaluation of rating performance, since the number of tranches rated by Fitch has grown substantially over the 14-year period under analysis.

Rating Transition Measurement

For most of the analysis in this transition study, a rating change is counted only when a rating moves from one ***"rating category"*** into another, e.g. from the 'AA' category to the 'A' category. Changes resulting merely in the addition or subtraction of one of the ***"rating modifiers"***, '+' or '-' within a rating category – e.g. to 'AA' from 'AA+' or to 'BBB' from 'BBB-' – do not affect the transition matrices in this study, unless explicitly noted otherwise. In particular, the transition matrices in *Appendix 3* are based on analysis of rating changes at the modifier level.

Multiple upgrades or downgrades of the same tranche in the same cohort count as a single transition.

Categories

The **asset class categories** in this study are ABS, CDO, CMBS and RMBS, with the following footnotes:

- Structured Investment Vehicles (SIVs) are grouped under the CDO ratings.
- Only asset-backed commercial paper (ABCP) programmes that issue medium-term notes (MTNs) with Long-term ratings are included in this study. Qualifying programmes are classified according to the nature of the underlying assets.
- All NPL transactions are classified as CMBS, since all these transactions are either dominated by CMBS or at least have a CMBS component.

Geographically, this study covers Fitch's ESF ratings in western Europe and excludes transactions in emerging markets (Turkey, eastern Europe, the Middle East and Africa).

The research looks separately at the six most active European SF markets: the UK (including Ireland for this analysis), Germany, Italy, the Netherlands, Spain and France. The last category in the study, "Other", covers the remaining western European countries, which have been less active individually; these include Austria, Belgium, Finland, Greece, Portugal, Sweden and Switzerland.

Transactions involving assets that are not primarily located in a single jurisdiction (e.g. most CDOs and a small number of CMBS transactions) are excluded from the country analysis.

Qualifying Time Periods

For a tranche to be included in the cohort for a particular year, it needs to be rated both at the start and the end of the year. For example, a multi-country CDO of corporate CDS that closed in June 2002 and had its rating withdrawn in February 2005 will only have been included in the 2003 and 2004 cohorts.

Withdrawn Ratings

If a rating is withdrawn, it is generally excluded from the cohort for the year of its withdrawal. However, if a rating is withdrawn following a default or a downgrade to the 'CC' category or below (at which level eventual default is regarded as likely), the tranche is included in the cohort for the year in which that event occurred as a transition from its start-of-period rating to its final rating of 'CC and below'.

Pari Passu Tranches

In the calculation of transition rates, pari passu tranches (ranking equally in terms of priority over the security, but differentiated by currency, interest rate profile, repayment timing or, in the case of master trust structures, issue timing) are counted as one observation. This reflects the fact that the ratings for a set of pari passu tranches will all change at the same time. As a dataset, tranches that exclude multiple pari passu tranches are described as ***"independent tranches"***.

Cautionary Notes

Results for some sectors and geographical regions may be distorted by the fact that there are relatively few independent observations. For example, there are few observations for speculative-grade tranches and the more specialised asset or country sub-sectors.

Throughout this study, all rating transitions are weighted equally, regardless of the value of securities in issue affected by the transition.

Transition rates reflect historical rating performance and are not necessarily a guide to absolute or relative performance in the future.

As a result of continuing data enhancement, the historical data used in this study may differ slightly from that used in previous similar studies. For that reason, this study supersedes the previous ESF transition studies.

Duff and Phelps (DCR) Ratings

Fitch emerged from the merger between Fitch IBCA and DCR in 2000. Accordingly, DCR structured finance ratings that have been converted to the Fitch scale are included in this study.

Appendix 2

Rating Changes, January to December 2006

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
06 Jan 2006	Granite Mortgages 01-1 Plc	Series 1 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 01-1 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 01-1 Plc	Series 2 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 01-1 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 01-2 Plc	Series 1 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 01-2 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 01-2 Plc	Series 2 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 01-2 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 01-2 Plc	Series 2 Class D	RMBS	UK	Upgrade	BB+	BBB+
06 Jan 2006	Granite Mortgages 02-1 Plc	Series 2 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 02-1 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 02-1 Plc	Series 2 Class D	RMBS	UK	Upgrade	BB+	BBB
06 Jan 2006	Granite Mortgages 02-1 Plc	Series 3 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 02-1 Plc	Series 3 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S1/B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S1/C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S2/B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S2/C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S3/B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 02-2 Plc	Class S3/C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 1 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 2 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 3 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-1 Plc	Series 3 Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 1/Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 1/Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 2/Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 2/Class C1	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 2/Class C2	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 2 Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 03-2 Plc	Series 3/Class C	RMBS	UK	Upgrade	BBB	A-
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 1 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 1 Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 2 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 2 Class M	RMBS	UK	Upgrade	A	AA

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 3 Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 3 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 03-3 Plc	Series 3 Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 04-1 plc	Series 1, Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 04-1 plc	Series 1, Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-1 plc	Series 1, Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 04-1 plc	Series 2, Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-1 plc	Series 2, Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 04-1 plc	Series 3, Class B	RMBS	UK	Upgrade	AA	AA+
06 Jan 2006	Granite Mortgages 04-1 plc	Series 3, Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-1 plc	Series 3, Class M	RMBS	UK	Upgrade	A	AA
06 Jan 2006	Granite Mortgages 04-2 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-2 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-2 Plc	Series 3 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-3 Plc	Series 1 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-3 Plc	Series 2 Class C	RMBS	UK	Upgrade	BBB	BBB+
06 Jan 2006	Granite Mortgages 04-3 Plc	Series 3 Class C	RMBS	UK	Upgrade	BBB	BBB+
16 Jan 2006	Craegmoor Funding No.2 Ltd	Class B1	ABS	UK	Downgrade	BBB-	BB+
16 Jan 2006	Craegmoor Funding No.2 Ltd	Class B2	ABS	UK	Downgrade	BBB-	BB+
16 Jan 2006	Craegmoor Funding No.2 Ltd	Class M	ABS	UK	Downgrade	A	A-
17 Jan 2006	Jupiter Quartz Finance Plc Series 2004-2	Class A	CDO	Global (Blend)	Downgrade	AA	AA-
17 Jan 2006	Jupiter Quartz Finance Plc Series 2004-2	Class B	CDO	Global (Blend)	Downgrade	AA-	A+
19 Jan 2006	Caesar Finance 2000 S.A.	Class B	CDO	Global (Blend)	Upgrade	B+	BBB-
20 Jan 2006	Programma Dinamico S.p.A. due 2012	Secured CLN	CDO	Italy	Downgrade	AAA	AA
24 Jan 2006	GC FTGENCAT II, TDA	Class AS	CDO	Spain	Upgrade	AA+	AAA
24 Jan 2006	GC FTGENCAT II, TDA	Class BG	CDO	Spain	Upgrade	AA	AAA
24 Jan 2006	GC FTGENCAT II, TDA	Class BS	CDO	Spain	Upgrade	A	A+
24 Jan 2006	GC FTGENCAT II, TDA	Class C	CDO	Spain	Upgrade	BBB	BBB+
31 Jan 2006	Jupiter Quartz Finance Plc Series 2004-1	Class A	CDO	Global (Blend)	Upgrade	AA	AA+
31 Jan 2006	Jupiter Quartz Finance Plc Series 2004-1	Class B	CDO	Global (Blend)	Upgrade	AA-	AA
03 Feb 2006	Quartz Finance Plc Series 2003-2 (Green Bay)	Class A	CDO	Global (Blend)	Downgrade	AAA	AA-
03 Feb 2006	Quartz Finance Plc Series 2003-2 (Green Bay)	Class B	CDO	Global (Blend)	Downgrade	A-	BBB+
03 Feb 2006	Phoenix 2002-1 Limited	Class C	CDO	Global (Blend)	Downgrade	BB+	BB-
03 Feb 2006	Petra Capital Limited Series 2002-1	Class B	CDO	Global (Blend)	Upgrade	AA+	AAA
03 Feb 2006	Petra Capital Limited Series 2002-1	Class C	CDO	Global (Blend)	Upgrade	A+	AA
03 Feb 2006	Petra Capital Limited Series 2002-1	Class D	CDO	Global (Blend)	Upgrade	BBB	BBB+
15 Feb 2006	Wightlink Finance Ltd	8.14 per cent. secured notes due 2024	ABS	UK	Downgrade	BBB	BB+
21 Feb 2006	European Loan Conduit No. 8 plc (Coronis)	Class C commercial mtge-backed floating-rate notes	CMBS	UK	Upgrade	AA	AAA

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
21 Feb 2006	European Loan Conduit No. 8 plc (Coronis)	Class F commercial mtge-backed floating-rate notes	CMBS	UK	Downgrade	B	CCC+
22 Feb 2006	Trevi Finance 2 S.p.A.	Class B	CMBS	Italy	Upgrade	A	AAA
22 Feb 2006	Trevi Finance 3 S.r.l	Class A	CMBS	Italy	Upgrade	AA-	AA
22 Feb 2006	Trevi Finance 3 S.r.l	Class B	CMBS	Italy	Upgrade	A-	A
22 Feb 2006	Trevi Finance S.p.A.	Class B	CMBS	Italy	Upgrade	A	AAA
01 Mar 2006	Bamburgh Finance No. 1 Plc	Class B	CMBS	UK	Upgrade	AA	AA+
02 Mar 2006	Victoria Funding (EMC-III) plc	Class B	CMBS	UK	Upgrade	AA	AAA
02 Mar 2006	Victoria Funding (EMC-III) plc	Class C	CMBS	UK	Upgrade	A	A+
03 Mar 2006	Ares Finance 2 S.A.	Class C	CMBS	Italy	Upgrade	AA	AAA
03 Mar 2006	Ares Finance 2 S.A.	Class D	CMBS	Italy	Upgrade	BBB	A
03 Mar 2006	Ares Finance 2 S.A.	Class E	CMBS	Italy	Upgrade	BB	BBB
03 Mar 2006	International Credit Recovery (ICR 4): Island Finance	Class B	CMBS	Italy	Upgrade	AA	AA+
03 Mar 2006	International Credit Recovery (ICR 4): Island Finance	Class C	CMBS	Italy	Upgrade	A	A+
03 Mar 2006	Residence 2000-1	Class B Notes	RMBS	Germany	Upgrade	A-	A
06 Mar 2006	Agrisecurities S.r.l.	Class 1-B	ABS	Italy	Upgrade	A-	A
06 Mar 2006	Agrisecurities S.r.l. Series 2002-1	Class B	ABS	Italy	Upgrade	A-	A
13 Mar 2006	Merak CDO Ltd Series 2005-01 and 2005-02	Series 2005-1	CDO	Global (Blend)	Downgrade	AA+	AA
13 Mar 2006	Merak CDO Ltd Series 2005-01 and 2005-02	Series 2005-2	CDO	Global (Blend)	Downgrade	AA	AA-
14 Mar 2006	Bishopsgate CDO	Class A	CDO	Global (Blend)	Downgrade	AAA	AA+
17 Mar 2006	Real Estate Capital No.2 Plc	Class B	CMBS	UK	Upgrade	AA	AAA
17 Mar 2006	Real Estate Capital No.2 Plc	Class C	CMBS	UK	Upgrade	A	AA
22 Mar 2006	Avebury Properties Ltd	Class B secured fixed-rate note	ABS	UK	Upgrade	BB	BBB
03 Apr 2006	Craegmoor Funding No.2 Ltd	Class B1	ABS	UK	Downgrade	BB+	BB-
03 Apr 2006	Craegmoor Funding No.2 Ltd	Class B2	ABS	UK	Downgrade	BB+	BB-
03 Apr 2006	Craegmoor Funding No.2 Ltd	Class M	ABS	UK	Downgrade	A-	BBB-
04 Apr 2006	Nova Finance No.2 plc	Class B	ABS	Portugal	Upgrade	AA	AA+
06 Apr 2006	Bifrost Investments Limited- Series 19	Class 5D	CDO	Global (Blend)	Downgrade	AA+	AA
06 Apr 2006	Bifrost Investments Limited- Series 19	Class 7C	CDO	Global (Blend)	Downgrade	AAA	AA+
06 Apr 2006	Bifrost Investments Limited- Series 19	Class 7D	CDO	Global (Blend)	Downgrade	A	A-
06 Apr 2006	Bifrost Investments Limited- Series 19	Class 10C	CDO	Global (Blend)	Downgrade	AA+	AA
06 Apr 2006	Bifrost Investments Limited- Series 19	Class 10D	CDO	Global (Blend)	Downgrade	A-	BBB+
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 5B	CDO	Global (Blend)	Upgrade	AA	AAA
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 5C	CDO	Global (Blend)	Upgrade	A	AA

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 7B	CDO	Global (Blend)	Upgrade	AA	AAA
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 7C	CDO	Global (Blend)	Upgrade	A	A+
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 10B	CDO	Global (Blend)	Upgrade	AA	AA+
06 Apr 2006	Bifrost Investments Limited- Series 13 Junior	Class 10D	CDO	Global (Blend)	Downgrade	BBB	BB+
10 Apr 2006	Monument Securitisation (CMBS) No. 2 Limited	Class C floating-rate notes due 2013	CMBS	UK	Upgrade	AA	AAA
10 Apr 2006	Monument Securitisation (CMBS) No. 2 Limited	Class D floating-rate notes due 2013	CMBS	UK	Upgrade	BBB+	A
10 Apr 2006	Monument Securitisation (CMBS) No. 2 Limited	Class E floating-rate notes due 2013	CMBS	UK	Upgrade	BB+	BBB-
20 Apr 2006	Imser Securitisation S.r.l.	Class B1	CMBS	Italy	Downgrade	A-	BBB+
20 Apr 2006	Imser Securitisation S.r.l.	Class B2	CMBS	Italy	Downgrade	A-	BBB+
20 Apr 2006	Imser Securitisation S.r.l.	Class B3	CMBS	Italy	Downgrade	A-	BBB+
24 Apr 2006	Xelo III Series 2005 (Como II)	Single tranche	CDO	Global (Blend)	Downgrade	AAA (RWN)	BBB-
26 Apr 2006	Leek Finance Number Eleven Plc	Class Ba	RMBS	UK	Upgrade	A	A+
26 Apr 2006	Leek Finance Number Eleven Plc	Class Bb	RMBS	UK	Upgrade	A	A+
26 Apr 2006	Leek Finance Number Eleven Plc	Class Bc	RMBS	UK	Upgrade	A	A+
26 Apr 2006	Leek Finance Number Ten Plc	Class B	RMBS	UK	Upgrade	A	A+
26 Apr 2006	Leek Finance Number Ten Plc	Class M	RMBS	UK	Upgrade	AA	AA+
27 Apr 2006	Concerto I BV	A-1	CDO	Netherlands	Upgrade	AA	AAA
27 Apr 2006	Concerto I BV	A-2	CDO	Netherlands	Upgrade	AA	AAA
27 Apr 2006	Concerto I BV	A-3	CDO	Netherlands	Upgrade	AA	AAA
27 Apr 2006	Concerto I BV	1 combination	CDO	Netherlands	Upgrade	AA	AAA
04 May 2006	Santander Consumer Finance Spain 02-1	Class B	ABS	Spain	Upgrade	A	A+
09 May 2006	Silk Finance No.2 Plc	Class B	ABS	Portugal	Upgrade	AA	AAA
15 May 2006	Melchior CDO I S.A.	Combination	CDO	Global (Blend)	Upgrade	B DR3	B+
18 May 2006	Betsen CDO Limited series 2004-2A/2B	Class 2B	CDO	Global (Blend)	Upgrade	AA-	AA
18 May 2006	Farringdon Mortgages No. 1 Plc	Class B1a	RMBS	UK	Downgrade	BBB	BBB-
18 May 2006	Farringdon Mortgages No. 1 Plc	Class B2a	RMBS	UK	Downgrade	BB	B
18 May 2006	Farringdon Mortgages No. 1 Plc	Class M2a	RMBS	UK	Downgrade	A	A-
18 May 2006	Farringdon Mortgages No. 1 Plc	Class B1a	RMBS	UK	Downgrade	BBB	BBB-
18 May 2006	Farringdon Mortgages No. 1 Plc	Class B2a	RMBS	UK	Downgrade	BB	B
18 May 2006	Farringdon Mortgages No. 1 Plc	Class M2a	RMBS	UK	Downgrade	A	A-
26 May 2006	Castanea One Plc	Class B	CMBS	European	Upgrade	AA	AAA
26 May 2006	Castanea One Plc	Class C	CMBS	European	Upgrade	A	AA

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
05 Jun 2006	Dinamico B.V secured Credit-Linked Notes due 13 Dec 2012 (Postevita 4)	Dinamico B.V	CDO	Italy	Downgrade	AA	A+
05 Jun 2006	Programma Dinamico S.p.A due 17 Dec 2012 (CSFBI PV 4)	Secured CLN	CDO	Italy	Downgrade	AA	A+
05 Jun 2006	Programma Dinamico B.V. due 15 Dec 2012	Secured CLN	CDO	Italy	Downgrade	AA	A+
09 Jun 2006	Panther CDO I BV	Class I	CDO	Netherlands	Upgrade	AAA	AAA
27 Jun 2006	Eirles Two Limited Series 125-128	Series 125	CDO	Global (Blend)	Upgrade	BBB	A-
27 Jun 2006	Eirles Two Limited Series 125-128	Series 126	CDO	Global (Blend)	Upgrade	A	AA-
27 Jun 2006	Eirles Two Limited Series 125-128	Series 127	CDO	Global (Blend)	Upgrade	AA+	AAA
27 Jun 2006	Eirles Two Limited Series 134-137	Series 134	CDO	Global (Blend)	Upgrade	BBB	A-
27 Jun 2006	Eirles Two Limited Series 134-137	Series 135	CDO	Global (Blend)	Upgrade	A	AA-
27 Jun 2006	Eirles Two Limited Series 134-137	Series 136	CDO	Global (Blend)	Upgrade	AA	AAA
27 Jun 2006	Eirles Two Limited Series 101-104	Series 103	CDO	Global (Blend)	Upgrade	AA	AAA
27 Jun 2006	Eirles Two Limited Series 101-104	Series 104	CDO	Global (Blend)	Upgrade	A	AA-
27 Jun 2006	N Tsar Portfolio CDS (Eirles Two Series 101-104)	Class D CDS	CDO	Global (Blend)	Upgrade	AA	AAA
27 Jun 2006	N Tsar Portfolio CDS (Eirles Two Series 101-104)	Class E CDS	CDO	Global (Blend)	Upgrade	A	AA-
30 Jun 2006	Quartz Finance PLC Series 2005-1 (Kingsbury)	Class A	CDO	Global (Blend)	Upgrade	AA	AA+
04 Jul 2006	Bifrost Investments Limited - Legolas Series 1	D	CDO	Global (Blend)	Upgrade	AA+	AAA
04 Jul 2006	Bifrost Investments Limited - Legolas Series 1	F	CDO	Global (Blend)	Upgrade	AA	AA+
04 Jul 2006	Bifrost Investments Limited - Legolas Series 2	B	CDO	Global (Blend)	Upgrade	AA+	AAA
04 Jul 2006	Bifrost Investments Limited - Legolas Series 2	D	CDO	Global (Blend)	Upgrade	AA+	AAA
04 Jul 2006	Bifrost Investments Limited - Legolas Series 2	F	CDO	Global (Blend)	Upgrade	AA	AAA
06 Jul 2006	Mayu BV	Asset-backed index notes	CDO	Netherlands	Downgrade	AAA	AA-
06 Jul 2006	Programma Dinamico S.p.A.	Asset-backed notes	CDO	Italy	Downgrade	AAA	AA-
06 Jul 2006	Tsar 05	C	CDO	Global (Blend)	Upgrade	AA	AAA
06 Jul 2006	Tsar 05	D	CDO	Global (Blend)	Upgrade	A	AA-
06 Jul 2006	Tsar 05	E	CDO	Global (Blend)	Upgrade	BBB	A-
06 Jul 2006	Eirles 4 Series 9	Series 9	CDO	Global (Blend)	Upgrade	A	AA-
06 Jul 2006	Eirles 4 Series 10	Series 10	CDO	Global (Blend)	Upgrade	BBB	A-
06 Jul 2006	Eirles 4 Series 15 & 16	Series 15	CDO	Global (Blend)	Upgrade	BBB	A-
06 Jul 2006	Eirles 4 Series 15 & 16	Series 16	CDO	Global (Blend)	Upgrade	BBB-	BBB+
06 Jul 2006	Eirles 4 Series 48 and 54	Series 54	CDO	Global (Blend)	Upgrade	BBB-	BBB+
06 Jul 2006	Eirles Two Limited Series 110	Series 110	CDO	Global (Blend)	Upgrade	AAA	AAA
06 Jul 2006	Eirles 2 Series 117	Series 117	CDO	Global (Blend)	Upgrade	A	AA-
06 Jul 2006	Tsar 08 Portfolio Credit Default Swap	D	CDO	Global (Blend)	Upgrade	AA	AAA
06 Jul 2006	Tsar 08 Portfolio Credit Default Swap	E	CDO	Global (Blend)	Upgrade	A	AA-
06 Jul 2006	Tsar 08 Portfolio Credit Default Swap	F	CDO	Global (Blend)	Upgrade	BBB	A-
06 Jul 2006	Eirles 4 Series 74 -77 (TSAR 8 Repack)	Series 74	CDO	Global (Blend)	Upgrade	BBB	A-
06 Jul 2006	Eirles 4 Series 74 -77 (TSAR 8 Repack)	Series 75	CDO	Global (Blend)	Upgrade	A	AA-
06 Jul 2006	Eirles 4 Series 74 -77 (TSAR 8 Repack)	Series 76	CDO	Global (Blend)	Upgrade	AA	AAA
06 Jul 2006	Nostrum Mortgages 2003-1 Plc	Class B	RMBS	Portugal	Upgrade	A+	AA-

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
07 Jul 2006	Bifrost Investments Limited- Series 1	B	CDO	Global (Blend)	Upgrade	AA+	AAA
07 Jul 2006	Bifrost Investments Limited- Series 2	B	CDO	Global (Blend)	Upgrade	AA+	AAA
07 Jul 2006	Bifrost Investments Limited- Series 3	B	CDO	Global (Blend)	Upgrade	AA+	AAA
11 Jul 2006	HVB Real Estate 2001-1	Class C	RMBS	Germany	Upgrade	BBB+	A-
11 Jul 2006	Marble Arch Residential Securitisation Ltd No 1	Class B	RMBS	UK	Upgrade	A	AA+
11 Jul 2006	Marble Arch Residential Securitisation Ltd No 2	Class B	RMBS	UK	Upgrade	BBB	A
11 Jul 2006	Marble Arch Residential Securitisation Ltd No 2	Class M	RMBS	UK	Upgrade	A+	AA
12 Jul 2006	Mecenate Leasing S.r.l.	Class B	ABS	Italy	Upgrade	AA	AA+
14 Jul 2006	Tsar 04 (ANTS) CDS + Eirles 4 Limited Series 6, 7 & 8	C	CDO	Global (Blend)	Upgrade	AA	AAA
14 Jul 2006	Tsar 04 (ANTS) CDS + Eirles 4 Limited Series 6, 7 & 8	D	CDO	Global (Blend)	Upgrade	A+	AA
14 Jul 2006	Tsar 04 (ANTS) CDS + Eirles 4 Limited Series 6, 7 & 8	E	CDO	Global (Blend)	Upgrade	BBB	A-
14 Jul 2006	Tsar 04 (ANTS) CDS + Eirles 4 Limited Series 6, 7 & 8	Series 7	CDO	Global (Blend)	Upgrade	AA	AAA
14 Jul 2006	Tsar 04 (ANTS) CDS + Eirles 4 Limited Series 6, 7 & 8	Series 8	CDO	Global (Blend)	Upgrade	A+	AA
14 Jul 2006	Alexandria Capital Series 2004-6 RHODES CDO	B	CDO	Global (Blend)	Upgrade	AA+	AAA
14 Jul 2006	Bifrost Investments Limited- Series 19	5D	CDO	Global (Blend)	Downgrade	AA	AA-
17 Jul 2006	Bifrost Investments Limited- Series 11	10C	CDO	Global (Blend)	Downgrade	AA+	AA-
17 Jul 2006	Bifrost Investments Limited- Series 11	7C	CDO	Global (Blend)	Downgrade	AAA	AA+
17 Jul 2006	Bifrost Investments Limited- Series 11	7D	CDO	Global (Blend)	Downgrade	A+	A
17 Jul 2006	Premiertel p.l.c.	Class B	CMBS	UK	Downgrade	A-	BBB+
17 Jul 2006	Telereal Securitisation PLC	Class B2	CMBS	UK	Downgrade	A-	BBB+
17 Jul 2006	Telereal Securitisation PLC	Class B3	CMBS	UK	Downgrade	A-	BBB+
17 Jul 2006	Telereal Securitisation PLC	Class B4	CMBS	UK	Downgrade	A-	BBB+
18 Jul 2006	Eurostar I CDO	B	CDO	Netherlands	Upgrade	C DR5	CC DR6
18 Jul 2006	Eurostar II CDO	B	CDO	Netherlands	Downgrade	B DR2	CCC+ DR2
18 Jul 2006	Alexandria Capital Series 2004-1: SAQQARA CDO High Grade Synthetic CDO of ABS	C-1	CDO	Global (Blend)	Upgrade	AA+	AAA
18 Jul 2006	Alexandria Capital Series 2004-1: SAQQARA CDO High Grade Synthetic CDO of ABS	C-2	CDO	Global (Blend)	Upgrade	AA+	AAA
19 Jul 2006	Eirles Two Series 143,144,145 and Class B Tranche Credit Default Swap	Series 143	CDO	Global (Blend)	Upgrade	AA	AAA
24 Jul 2006	Antenore Finance S.p.A.	Class B	CMBS	Italy	Upgrade	AA	AA+
25 Jul 2006	Eirles Four Limited Series 42 Synthetic Investment-Grade CDO	Series 42	CDO	Global (Blend)	Downgrade	BBB-	B+
04 Aug 2006	Iliad Investments Plc Series 5	Series 5 EUR	CDO	Global (Blend)	Upgrade	AA+	AAA
04 Aug 2006	Iliad Investments Plc Series 5	Series 5 USD	CDO	Global (Blend)	Upgrade	AA+	AAA
04 Aug 2006	Russian Mortgage Backed Securities 2006-1 S.A	Class A	RMBS	Russian Federation	Upgrade	BBB+	A-
07 Aug 2006	Bifrost Investments Limited- Series 12	10C	CDO	Global (Blend)	Upgrade	A	A+
07 Aug 2006	Bifrost Investments Limited- Series 12	5C	CDO	Global (Blend)	Upgrade	AA+	AAA
07 Aug 2006	Bifrost Investments Limited- Series 12	5D	CDO	Global (Blend)	Upgrade	A-	AA-
07 Aug 2006	Bifrost Investments Limited- Series 12	7C	CDO	Global (Blend)	Upgrade	A+	AA
07 Aug 2006	Bifrost Investments Limited- Series 12	7D	CDO	Global (Blend)	Upgrade	BBB	A-

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
09 Aug 2006	Tiepolo Finance 2 S.r.l	Class A	CMBS	Italy	Upgrade	AA+	AAA
09 Aug 2006	Tiepolo Finance 2 S.r.l	Class B	CMBS	Italy	Upgrade	A+	AA-
09 Aug 2006	Tiepolo Finance S.r.l	Class B	CMBS	Italy	Upgrade	AA	AA+
10 Aug 2006	Iliad Investments Plc Series 6	Series 6 USD	CDO	Global (Blend)	Upgrade	A+	AA
10 Aug 2006	Iliad Investments Plc Series 6	Series 6 USD	CDO	Global (Blend)	Upgrade	A+	AA
10 Aug 2006	Lusitano Global CDO No. 1	C	CDO	Global (Blend)	Upgrade	AA	AAA
11 Aug 2006	White Tower 2004-1 plc	Class B	CMBS	UK	Upgrade	AA	AAA
11 Aug 2006	White Tower 2004-1 plc	Class C	CMBS	UK	Upgrade	A	AA
17 Aug 2006	Iliad Investments Plc Series 1	Class B	CDO	Global (Blend)	Upgrade	AA+	AAA
17 Aug 2006	Iliad Investments Plc Series 1	Class C	CDO	Global (Blend)	Upgrade	A	AAA
17 Aug 2006	Iliad Investments Plc Series 3	C	CDO	Global (Blend)	Upgrade	A-	AA
21 Aug 2006	CDO Master Investments 2 S.A	B Series 1	CDO	Global (Blend)	Upgrade	AA	AAA
21 Aug 2006	CDO Master Investments 2 S.A	C Series 1	CDO	Global (Blend)	Upgrade	BB-	BBB
21 Aug 2006	Hohensyburg CDO^2 with ABS	A-1	CDO	Global (Blend)	Downgrade	AAA	AA+
21 Aug 2006	Hohensyburg CDO^2 with ABS	B-1	CDO	Global (Blend)	Downgrade	AA	A+
21 Aug 2006	Iliad Investments Plc Series 12	A EUR floating	CDO	Global (Blend)	Upgrade	AA	AAA
22 Aug 2006	PHF Securities No.1 Ltd	Class A2	ABS	UK	Upgrade	BBB-	BBB
22 Aug 2006	UK Care No.1 Ltd	Class A2	ABS	UK	Upgrade	A+	AA
25 Aug 2006	Lusitano Finance No. 2 Plc	Class C	ABS	Portugal	Upgrade	A	AA-
25 Aug 2006	Iliad Investments Plc Series 2	B	CDO	Global (Blend)	Upgrade	AA	AAA
25 Aug 2006	Iliad Investments Plc Series 2	C	CDO	Global (Blend)	Upgrade	BB	BBB
01 Sep 2006	Aurum Investments SA. Series 1	B	CDO	Global (Blend)	Upgrade	AA+	AAA
01 Sep 2006	Aurum Investments SA. Series 1	C-1	CDO	Global (Blend)	Upgrade	AA-	AA
01 Sep 2006	Aurum Investments SA. Series 1	C-2	CDO	Global (Blend)	Upgrade	AA-	AA
01 Sep 2006	Aurum Investments SA. Series 1	D	CDO	Global (Blend)	Upgrade	A+	AA-
01 Sep 2006	Helix Capital (Netherlands) B.V. Series 2001-5	2001-5A	CDO	Netherlands	Upgrade	AA	AAA
01 Sep 2006	Helix Capital (Netherlands) B.V. Series 2002-12 A,B,C	2002-12A	CDO	Netherlands	Upgrade	AA	AA+
01 Sep 2006	Helix Capital (Netherlands) B.V. Series 2002-12 A,B,C	2002-12B	CDO	Netherlands	Upgrade	BB	BBB-
06 Sep 2006	Concerto II B.V.	B Senior notes	CDO	Netherlands	Upgrade	A-	A
08 Sep 2006	Apulia Finance S.r.l.	Class B	RMBS	Italy	Upgrade	A	AA-
08 Sep 2006	Argo Mortgage S.r.l.	Class B	RMBS	Italy	Upgrade	AA+	AAA
08 Sep 2006	Argo Mortgage S.r.l.	Class C	RMBS	Italy	Upgrade	BBB+	A+
08 Sep 2006	BPV Mortgages S.r.l.	Class B	RMBS	Italy	Upgrade	A	A+
08 Sep 2006	CR Firenze Mutui S.r.l.	Class B	RMBS	Italy	Upgrade	A	A+
08 Sep 2006	CR Firenze Mutui S.r.l.	Class C	RMBS	Italy	Upgrade	BBB	BBB+
08 Sep 2006	Claris Finance S.r.l.	Class B	RMBS	Italy	Upgrade	AA	AAA
08 Sep 2006	Claris Finance S.r.l.	Class C	RMBS	Italy	Upgrade	BBB	A
08 Sep 2006	Giotto Finance Plc	Class B	RMBS	Italy	Upgrade	A+	AA
08 Sep 2006	Grecale S.r.l.	Class B	RMBS	Italy	Upgrade	A	AA-
08 Sep 2006	Intesa Sec. S.p.A.	Class B notes	RMBS	Italy	Upgrade	AA+	AAA
08 Sep 2006	Mantegna Finance S.r.l.	Class B	RMBS	Italy	Upgrade	A+	AA

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
08 Sep 2006	Mecenate S.r.l.	Class B	RMBS	Italy	Upgrade	A+	AA+
08 Sep 2006	Siena Mortgages 00-1 S.p.A.	Class C notes	RMBS	Italy	Upgrade	BBB+	A-
12 Sep 2006	Mercantile Finance S.r.l	Class C	ABS	Italy	Upgrade	BBB	A+
13 Sep 2006	Southern Pacific Financing 04-A Plc	Class C	RMBS	UK	Upgrade	A	A+
13 Sep 2006	Southern Pacific Financing 04-A Plc	Class D	RMBS	UK	Upgrade	BBB	BBB+
13 Sep 2006	Southern Pacific Financing 04-A Plc	Class E	RMBS	UK	Upgrade	BB	BB+
13 Sep 2006	Southern Pacific Securities D plc	Class B	RMBS	UK	Upgrade	BBB	AA
13 Sep 2006	Southern Pacific Securities D plc	Class M	RMBS	UK	Upgrade	A+	AA+
13 Sep 2006	Southern Pacific Securities E Plc	Class B1	RMBS	UK	Upgrade	BBB	AA
13 Sep 2006	Southern Pacific Securities E Plc	Class B2	RMBS	UK	Upgrade	BBB	AA
13 Sep 2006	Southern Pacific Securities E Plc	Class M1	RMBS	UK	Upgrade	A+	AA+
13 Sep 2006	Southern Pacific Securities E Plc	Class M2	RMBS	UK	Upgrade	A+	AA+
13 Sep 2006	Southern Pacific Securities F Plc	Class M1	RMBS	UK	Upgrade	A	AA
13 Sep 2006	Southern Pacific Securities F Plc	Class M2	RMBS	UK	Upgrade	A	AA
13 Sep 2006	Southern Pacific Securities G Plc	Class B	RMBS	UK	Upgrade	A	A+
13 Sep 2006	Southern Pacific Securities G Plc	Class M	RMBS	UK	Upgrade	AA-	AA
21 Sep 2006	Provide Home 2001-1 plc	Class C credit-linked notes	RMBS	Germany	Downgrade	A	A-
21 Sep 2006	Provide Home 2001-1 plc	Class D credit-linked notes	RMBS	Germany	Downgrade	BBB	BB+
21 Sep 2006	Provide Home 2001-1 plc	Class C credit-linked notes	RMBS	Germany	Downgrade	A	A-
21 Sep 2006	Provide Home 2001-1 plc	Class D credit-linked notes	RMBS	Germany	Downgrade	BBB	BB+
22 Sep 2006	Taurus CMBS No. 1 plc	Class B	CMBS	UK	Upgrade	AA	AAA
22 Sep 2006	Taurus CMBS No. 1 plc	Class C	CMBS	UK	Upgrade	A+	AA
22 Sep 2006	Taurus CMBS No. 1 plc	Class D	CMBS	UK	Upgrade	A	A+
25 Sep 2006	MBS-4 V.B.S.	Class B	RMBS	Belgium	Upgrade	AA	AA+
26 Sep 2006	Xelo III Public Limited Company Series 2005 (Firecrest 7)	Firecrest 7	CDO	Global (Blend)	Upgrade	AA	AA+
03 Oct 2006	Harbourmaster CLO 2 Ltd	S	CDO	Global (Blend)	Upgrade	A	AA-
06 Oct 2006	Alexandria Capital 2004-13B: RHODES 2 CDO	B2b	CDO	Global (Blend)	Upgrade	AA+	AAA
06 Oct 2006	Classic Finance B.V	Series 2002-1C	CDO	Netherlands	Upgrade	AA+	AAA
06 Oct 2006	Classic Finance B.V	Series 2002-1D	CDO	Netherlands	Upgrade	AA	AA+
09 Oct 2006	Intesa Sec NPL S.p.A	Class C	CMBS	Italy	Upgrade	AA	AAA
09 Oct 2006	Intesa Sec NPL S.p.A	Class C	CMBS	Italy	Upgrade	AA	AAA
09 Oct 2006	Ulisse S.p.A	Class B	CMBS	Italy	Upgrade	AA-	AAA
09 Oct 2006	Delphinus 2000-I B.V.	Junior Class C fixed-rate notes	RMBS	Netherlands	Upgrade	AA-	AAA
09 Oct 2006	Delphinus 2000-II B.V.	Junior Class C fixed-rate notes	RMBS	Netherlands	Upgrade	BBB+	AA-
09 Oct 2006	Delphinus 2000-II B.V.	Mezzanine Class B mortgage-backed notes	RMBS	Netherlands	Upgrade	A+	AAA
09 Oct 2006	Delphinus 2001-I B.V	Class B Mezzanine mortgage-backed notes	RMBS	Netherlands	Upgrade	A	A+
09 Oct 2006	Delphinus 2001-I B.V	Class C junior mortgage-backed notes	RMBS	Netherlands	Upgrade	BBB	BBB+
10 Oct 2006	Pillar Funding Series 2002-1 plc	Class C	ABS	UK	Downgrade	BBB	BBB-
10 Oct 2006	Pillar Funding Series 2003-1 plc	C1	ABS	UK	Downgrade	BBB	BBB-

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
10 Oct 2006	Pillar Funding Series 2003-1 plc	C2	ABS	UK	Downgrade	BBB	BBB-
10 Oct 2006	Pillar Funding Series 2004-1 plc	Class C1	ABS	UK	Downgrade	BBB	BBB-
10 Oct 2006	Pillar Funding Series 2004-1 plc	Class C2	ABS	UK	Downgrade	BBB	BBB-
10 Oct 2006	Pillar Funding Series 2004-2 plc	Class C	ABS	UK	Downgrade	BBB	BBB-
10 Oct 2006	Pillar Funding Series 2005-1 Plc	Class C	ABS	UK	Downgrade	BBB	BBB-
11 Oct 2006	Farms Securitisation Limited	Class B notes	RMBS	Sweden	Upgrade	AA	AAA
11 Oct 2006	Farms Securitisation Limited	Class C notes	RMBS	Sweden	Upgrade	A+	AA
11 Oct 2006	Farms Securitisation Limited	Class D notes	RMBS	Sweden	Upgrade	BBB+	A
11 Oct 2006	Mortgages No. 5 Plc	Class B1	RMBS	UK	Upgrade	A	AA
11 Oct 2006	Mortgages No. 5 Plc	Class B2	RMBS	UK	Upgrade	A	AA
11 Oct 2006	Mortgages No. 5 Plc	Class M	RMBS	UK	Upgrade	AA	AAA
11 Oct 2006	Mortgages No. 6 Plc	Class D	RMBS	UK	Upgrade	BBB	BBB+
17 Oct 2006	BMORE No.2 Limited	Junior notes	ABS	Portugal	Upgrade	AA+	AAA
19 Oct 2006	Astrea S.r.L	Class A	CDO	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 1	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 2	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 3	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 4	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 4-2	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 5	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 6	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 7	ABS	Italy	Downgrade	AA	AA-
19 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 8	ABS	Italy	Downgrade	AA	AA-
20 Oct 2006	C.P.G. Societa di Cartolarizzazione a.r.l. 2003-1	A2	CDO	Italy	Downgrade	AA	AA-
20 Oct 2006	Patrimonio Uno CMBS S.r.l.	Class C	CMBS	Italy	Downgrade	AA	AA-
20 Oct 2006	Patrimonio Uno CMBS S.r.l.	Class D	CMBS	Italy	Downgrade	AA	AA-
20 Oct 2006	Cassa Depositi e Prestiti TAV (formerly known as Infrastrutture)	Series 4-3	ABS	Italy	Downgrade	AA	AA-
20 Oct 2006	Mutina S.r.l.	Class A	CMBS	Italy	Downgrade	AA	AA-
20 Oct 2006	FIP Funding S.r.l.	Class A1	CMBS	Italy	Downgrade	AA	AA-
20 Oct 2006	FIP Funding S.r.l.	Class A2	CMBS	Italy	Downgrade	AA	AA-
27 Oct 2006	Tsar 15 CDO Eirles Two Ltd Series 223-227	Series 225 D-1	CDO	Global (Blend)	Upgrade	AA+	AAA
27 Oct 2006	Tsar 15 CDO Eirles Two Ltd Series 223-227	Series 226 D-2	CDO	Global (Blend)	Upgrade	AA	AA+
30 Oct 2006	Smile Securitisation Company 2001-1 B.V.	B1	CDO	Netherlands	Upgrade	AA+	AAA
30 Oct 2006	Smile Securitisation Company 2001-1 B.V.	B2	CDO	Netherlands	Upgrade	AA+	AAA
30 Oct 2006	Smile Securitisation Company 2001-1 B.V.	C1	CDO	Netherlands	Upgrade	AA-	AA
30 Oct 2006	Smile Securitisation Company 2001-1 B.V.	C2	CDO	Netherlands	Upgrade	AA-	AA
07 Nov 2006	AyT FTGENCAT I, FTA	BF	CDO	Spain	Upgrade	AA	AAA
07 Nov 2006	AyT FTGENCAT I, FTA	C	CDO	Spain	Upgrade	BBB+	A
07 Nov 2006	AyT FTPYME I FTA	B	CDO	Spain	Upgrade	BBB	A
07 Nov 2006	AyT FTPYME I FTA	F2	CDO	Spain	Upgrade	AA	AAA
07 Nov 2006	FTPYME Bancaja 2 Fondo de Titulizacion de Activos	Class B	CDO	Spain	Upgrade	A+	AA-

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
07 Nov 2006	FTPYME Bancaja 3 Fondo de Titulizacion de Activos	B	CDO	Spain	Upgrade	AA+	AAA
08 Nov 2006	FTPYME Foncaixa 1, FTA	B	CDO	Spain	Upgrade	A	A+
08 Nov 2006	GC FTGENCAT II, Fondo de Titulizacion de Activos	BS	CDO	Spain	Upgrade	A+	AA
08 Nov 2006	GC FTGENCAT II, Fondo de Titulizacion de Activos	C	CDO	Spain	Upgrade	BBB+	A
07 Nov 2006	Promise-Z 2001-1 Plc	B	CDO	Germany	Upgrade	AA	AAA
07 Nov 2006	Promise-Z 2001-1 Plc	C	CDO	Germany	Upgrade	A	AA
07 Nov 2006	Promise-Z 2001-1 Plc	D	CDO	Germany	Upgrade	BBB	A
07 Nov 2006	Promise-Z 2001-1 Plc	E-1	CDO	Germany	Upgrade	BB	BBB
07 Nov 2006	Promise-Z 2001-1 Plc	E-2	CDO	Germany	Upgrade	BB	BBB
08 Nov 2006	Arena 2001-1 BV	Class B	RMBS	Netherlands	Upgrade	AA+	AAA
08 Nov 2006	Arena 2001-1 BV	Class C	RMBS	Netherlands	Upgrade	BBB	BBB+
08 Nov 2006	Arena 2002-1 B.V.	Class B	RMBS	Netherlands	Upgrade	AA-	AA+
08 Nov 2006	Arena 2002-1 B.V.	Class C	RMBS	Netherlands	Upgrade	BBB+	A
08 Nov 2006	Arena 2003-1 B.V	Class B	RMBS	Netherlands	Upgrade	A+	AA+
08 Nov 2006	Arena 2003-1 B.V	Class C	RMBS	Netherlands	Upgrade	BBB+	A-
08 Nov 2006	Dutch MBS 00-1 B.V.	Class C subordinated notes	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	Dutch MBS 00-1 B.V.	Class D subordinated notes	RMBS	Netherlands	Upgrade	BBB+	A+
08 Nov 2006	Dutch MBS 01-1 B.V	Class B	RMBS	Netherlands	Upgrade	AA+	AAA
08 Nov 2006	Dutch MBS 01-1 B.V	Class C	RMBS	Netherlands	Upgrade	A+	AA-
08 Nov 2006	Dutch MBS 01-1 B.V	Class D	RMBS	Netherlands	Upgrade	BBB+	A
08 Nov 2006	Dutch MBS 99-I B.V.	Subordinated class D	RMBS	Netherlands	Upgrade	A	AA-
08 Nov 2006	Dutch MBS 99-II B.V.	Subordinated class C notes	RMBS	Netherlands	Upgrade	AA+	AAA
08 Nov 2006	Dutch MBS 99-II B.V.	Subordinated class D notes	RMBS	Netherlands	Upgrade	A-	A+
08 Nov 2006	Dutch MBS 99-III B.V.	Subordinated class C notes	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	Dutch MBS 99-III B.V.	Subordinated class D notes	RMBS	Netherlands	Upgrade	A-	A+
08 Nov 2006	Dutch MBS IX B.V	Class C	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	Dutch MBS IX B.V	Class D	RMBS	Netherlands	Upgrade	BBB+	A
08 Nov 2006	Dutch MBS XI B.V.	Class B	RMBS	Netherlands	Upgrade	A	AA-
08 Nov 2006	Dutch MBS XI B.V.	Class C	RMBS	Netherlands	Upgrade	BBB	BBB+
08 Nov 2006	Dutch Mortgage Portfolio Loans I B.V.	Mezzanine Class B mortgage-backed notes	RMBS	Netherlands	Upgrade	AA	AA+
08 Nov 2006	E-MAC NL 2002-I B.V.	Class B	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	E-MAC NL 2002-I B.V.	Class C	RMBS	Netherlands	Upgrade	BBB+	A+
08 Nov 2006	E-MAC NL 2002-I B.V.	Class D	RMBS	Netherlands	Upgrade	BB+	BBB
08 Nov 2006	E-MAC NL 2003-1 B.V.	Class B	RMBS	Netherlands	Upgrade	A	AA
08 Nov 2006	E-MAC NL 2003-1 B.V.	Class C	RMBS	Netherlands	Upgrade	BBB	BBB+
08 Nov 2006	E-MAC NL 2003-1 B.V.	Class D	RMBS	Netherlands	Upgrade	BB	BB+
08 Nov 2006	E-MAC NL 2003-II B.V.	Class B	RMBS	Netherlands	Upgrade	A	AA
08 Nov 2006	E-MAC NL 2003-II B.V.	Class C	RMBS	Netherlands	Upgrade	BBB	BBB+
08 Nov 2006	E-MAC NL 2004-1 B.V.	Class B	RMBS	Netherlands	Upgrade	A	A+

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
03 Nov 2006	Europa Two Limited	Class E fixed-rate secured notes due 2027	CMBS	European	Upgrade	BBB	A
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) I B.V.	Subordinated class C notes	RMBS	Netherlands	Upgrade	A	A+
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) IV B.V	Class B	RMBS	Netherlands	Upgrade	AA+	AAA
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) V B.V	Class B	RMBS	Netherlands	Upgrade	A+	AA+
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) V B.V	Class C	RMBS	Netherlands	Upgrade	BBB	A
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) VI B.V	Class B	RMBS	Netherlands	Upgrade	A	AA+
08 Nov 2006	Holland Euro-Denominated Mortgage-Backed Series (Hermes) VI B.V	Class C	RMBS	Netherlands	Upgrade	BBB	A-
08 Nov 2006	Lusitano Mortgages No.1 Plc	Class B	RMBS	Portugal	Upgrade	AA	AA+
08 Nov 2006	Lusitano Mortgages No.1 Plc	Class C	RMBS	Portugal	Upgrade	A	A+
08 Nov 2006	Magellan Mortgages No. 1 Plc	Class B	RMBS	Portugal	Upgrade	AA	AA+
08 Nov 2006	Match I (2002-I) B.V.	Class B	RMBS	Netherlands	Upgrade	A	A+
08 Nov 2006	Match I (2002-I) B.V.	Class C	RMBS	Netherlands	Upgrade	BBB	A-
08 Nov 2006	Pelican Mortgages No.1 Plc	Class B	RMBS	Portugal	Upgrade	AA-	AA+
07 Nov 2006	Real Value One	Class B FRN amortising credit-linked notes	CMBS	Germany	Upgrade	AA	AAA
07 Nov 2006	Real Value One	Class C FRN amortising credit-linked notes	CMBS	Germany	Upgrade	A	AAA
07 Nov 2006	Real Value One	Class D-1 FRN amortising credit-linked notes	CMBS	Germany	Upgrade	BBB	AA
08 Nov 2006	STReAM I B.V	Class B	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	Saecure 2 B.V.	Class B	RMBS	Netherlands	Upgrade	AA-	AAA
08 Nov 2006	Saecure 2 B.V.	Class C	RMBS	Netherlands	Upgrade	A	AA
08 Nov 2006	Saecure 2000-1 B.V.	Subordinated class C fixed-rate notes	RMBS	Netherlands	Upgrade	AA	AAA
08 Nov 2006	Saecure 2000-1 B.V.	Subordinated class D fixed-rate notes	RMBS	Netherlands	Upgrade	BBB+	A-
08 Nov 2006	Saecure 3 B.V.	Class B	RMBS	Netherlands	Upgrade	A+	AA-
08 Nov 2006	Saecure 3 B.V.	Class C	RMBS	Netherlands	Upgrade	BBB+	A-
08 Nov 2006	Stichting Eleven Cities No. 1	Class B	RMBS	Netherlands	Upgrade	A+	AA
08 Nov 2006	Stichting Eleven Cities No. 1	Class C	RMBS	Netherlands	Upgrade	BBB+	A-
08 Nov 2006	Stichting Memphis (2003-I)	Class B	RMBS	Netherlands	Upgrade	A+	AA-
08 Nov 2006	SwAFE 1 B.V	Class B	RMBS	Netherlands	Upgrade	AA+	AAA
10 Nov 2006	Venice S.r.l	Class B	ABS	Italy	Upgrade	BBB	A
09 Nov 2006	FTPYME TDA CAM 2	2SA	CDO	Spain	Upgrade	A	A+
21 Nov 2006	FTPYME Bancaja 1 Fondo de Titulizacion de Activos	B	CDO	Spain	Upgrade	BBB	BBB+

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
22 Nov 2006	FTPYME ICO-TDA 4, Fondo de Titulizacion de Activos	2 SA	CDO	Spain	Upgrade	AA	AAA
20 Nov 2006	FTPYME TDA SABADELL 2	2 SA	CDO	Spain	Upgrade	AA	AA+
21 Nov 2006	IGLOO II Finance Plc	C	CDO	Global (Blend)	Upgrade	A	AA
21 Nov 2006	IM BANCO POPULAR FTPYME 1 FTA	B	CDO	Spain	Upgrade	A	A+
21 Nov 2006	IM Ceres 1 Cajamar F.T.A.	B	CDO	Spain	Upgrade	BBB	A
22 Nov 2006	Nymphenburg 2002-1 Limited	Class C	CMBS	European	Upgrade	AA	AAA
22 Nov 2006	Nymphenburg 2002-1 Limited	Class D	CMBS	European	Upgrade	A	AAA
22 Nov 2006	Nymphenburg 2002-1 Limited	Class E	CMBS	European	Upgrade	BBB	A
22 Nov 2006	Titan Europe 2004-1 plc	Class B	CMBS	UK	Upgrade	AA	AAA
22 Nov 2006	Titan Europe 2004-1 plc	Class C	CMBS	UK	Upgrade	A	AAA
22 Nov 2006	Titan Europe 2004-1 plc	Class D	CMBS	UK	Upgrade	BBB-	BBB+
22 Nov 2006	Titan Europe 2004-2 plc	Class C	CMBS	France	Upgrade	A	AAA
22 Nov 2006	Titan Europe 2004-2 plc	Class D	CMBS	France	Upgrade	BBB-	A
29 Nov 2006	BBVA 3 FTPYME	B	CDO	Spain	Upgrade	A	A+
29 Nov 2006	BBVA-2 FTPYME - ICO, Fondo de Titulizacion de Activos	Series DSA	CDO	Spain	Upgrade	AA	AAA
29 Nov 2006	BBVA-2 FTPYME - ICO, Fondo de Titulizacion de Activos	Series ESA	CDO	Spain	Upgrade	BBB+	A-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	B1	CDO	Global (Blend)	Upgrade	AA	AAA
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	B2	CDO	Global (Blend)	Upgrade	AA	AAA
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	B3	CDO	Global (Blend)	Upgrade	AA	AAA
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	B4	CDO	Global (Blend)	Upgrade	AA	AAA
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	C1	CDO	Global (Blend)	Upgrade	A	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	C2	CDO	Global (Blend)	Upgrade	A	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	C3	CDO	Global (Blend)	Upgrade	A	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	D1	CDO	Global (Blend)	Upgrade	BBB	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	D2	CDO	Global (Blend)	Upgrade	BBB	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	E1	CDO	Global (Blend)	Upgrade	BB	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	E2	CDO	Global (Blend)	Upgrade	BB	AA-
27 Nov 2006	Deutsche Bank Aktiengesellschaft CAST 2000-1	E3	CDO	Global (Blend)	Upgrade	BB	AA-
28 Nov 2006	FTPYME SANTANDER 1 FTA	Class B2	CDO	Spain	Upgrade	AA	AA+
28 Nov 2006	FTPYME SANTANDER 1 FTA	Class C	CDO	Spain	Upgrade	A	A+
28 Nov 2006	AyT Genova Hipotecario III, (Fondo de Titulizacion Hipotecario)	Class B	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	AyT Hipotecario Mixto II, Fondo de Titulizacion de Activos	Class CH2	RMBS	Spain	Upgrade	BBB-	BBB
28 Nov 2006	Bancaja 4, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	AA-	AA+
28 Nov 2006	Bancaja 4, Fondo de Titulización Hipotecaria	Class C	RMBS	Spain	Upgrade	A-	A+
28 Nov 2006	Bancaja 5, Fondo de Titulización de Activos	Class B	RMBS	Spain	Upgrade	A+	AA+
28 Nov 2006	Bancaja 5, Fondo de Titulización de Activos	Class C	RMBS	Spain	Upgrade	BBB	A-
28 Nov 2006	Bancaja 6, Fondo de Titulizacion de Activos	Class B	RMBS	Spain	Upgrade	A+	AA-
28 Nov 2006	Bancaja 6, Fondo de Titulizacion de Activos	Class C	RMBS	Spain	Upgrade	BBB	BBB+
28 Nov 2006	Bankinter 7, Fondo de Titulizacion Hipotecaria	Class B	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	Bankinter 7, Fondo de Titulizacion Hipotecaria	Class C	RMBS	Spain	Upgrade	BBB	BBB+
28 Nov 2006	Foncaixa Hipotecario 2, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	AA	AA+

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
28 Nov 2006	Foncaixa Hipotecario 3, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	AA-	AA
28 Nov 2006	Foncaixa Hipotecario 4, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	AA-	AA
28 Nov 2006	Foncaixa Hipotecario 5, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	A	AA-
28 Nov 2006	Foncaixa Hipotecario 6, Fondo de Titulización Hipotecaria	Class B	RMBS	Spain	Upgrade	A	AA-
28 Nov 2006	Hipocat 5, Fondo de Titulización de Activos	Class B	RMBS	Spain	Upgrade	AA+	AAA
28 Nov 2006	Hipocat 5, Fondo de Titulización de Activos	Class C	RMBS	Spain	Upgrade	A+	AA
28 Nov 2006	Hipocat 6, Fondo de Titulizacion de Activos	Class B	RMBS	Spain	Upgrade	AA	AA+
28 Nov 2006	Hipocat 6, Fondo de Titulizacion de Activos	Class C	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	Hipocat 7, Fondo de Titulizacion de Activos	Class B	RMBS	Spain	Upgrade	AA	AAA
28 Nov 2006	Hipocat 7, Fondo de Titulizacion de Activos	Class C	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	Hipocat 7, Fondo de Titulizacion de Activos	Class D	RMBS	Spain	Upgrade	BBB	BBB+
28 Nov 2006	Hipotebansa IX Fondo de Titulización Hipotecaria, S.A.	Class B	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	Hipotebansa VIII Fondo de Titulización Hipotecaria, S.A.	Class B	RMBS	Spain	Upgrade	A	A+
28 Nov 2006	MBS Bancaja 1, Fondo de Titulizacion de Activos	Class C	RMBS	Spain	Upgrade	A+	AA-
28 Nov 2006	MBS Bancaja 1, Fondo de Titulizacion de Activos	Class D	RMBS	Spain	Upgrade	BBB	BBB+
28 Nov 2006	TDA 19 - MIXTO, Fondo de Titulizacion de Activos	Class B	RMBS	Spain	Upgrade	A	AA-
28 Nov 2006	TDA 19 - MIXTO, Fondo de Titulizacion de Activos	Class C	RMBS	Spain	Upgrade	BBB	A-
28 Nov 2006	TDA 19 - MIXTO, Fondo de Titulizacion de Activos	Class D	RMBS	Spain	Upgrade	BB+	BBB-
28 Nov 2006	TDA CAM 1, Fondo de Titulizacion de Activos	Class B	RMBS	Spain	Upgrade	A	A+
06 Dec 2006	EuroLiberte Plc	B	CDO	Global (Blend)	Upgrade	AA	AAA
06 Dec 2006	EuroLiberte Plc	C	CDO	Global (Blend)	Upgrade	BBB+	A-
06 Dec 2006	EuroLiberte Plc	D	CDO	Global (Blend)	Upgrade	BBB	BBB+
05 Dec 2006	FTPYME TDA CAM 1, FTA	2SA	CDO	Spain	Upgrade	A+	AA
04 Dec 2006	Lambay Capital Securities Plc	Tier-one	CDO	Global (Blend)	Upgrade	A-	A
13 Dec 2006	PMI 2 Finance S.r.l.	B	CDO	Italy	Upgrade	AA	AA+
13 Dec 2006	PMI UNO Finance S.r.l.	B	CDO	Italy	Upgrade	AA	AA+
13 Dec 2006	PMI UNO Finance S.r.l.	C	CDO	Italy	Upgrade	BBB	BBB+
13 Dec 2006	Promise Color - 2003-1 plc	B	CDO	Global (Blend)	Upgrade	AA	AAA
13 Dec 2006	Promise Color - 2003-1 plc	C	CDO	Global (Blend)	Upgrade	A	AA
07 Dec 2006	Ares Finance S.r.l.	Class C	CMBS	Italy	Upgrade	AA	AAA
07 Dec 2006	Ares Finance S.r.l.	Class D	CMBS	Italy	Upgrade	A-	A+
08 Dec 2006	European Loan Conduit No. 11 Plc (Feronia)	Class C	CMBS	UK	Upgrade	AA	AAA
08 Dec 2006	European Loan Conduit No. 11 Plc (Feronia)	Class D	CMBS	UK	Upgrade	A	AA
08 Dec 2006	Self-Storage Securitisation B.V.	Class B	CMBS	European	Upgrade	A	A+
08 Dec 2006	Self-Storage Securitisation B.V.	Class C	CMBS	European	Upgrade	BBB	BBB+
12 Dec 2006	Bauhaus Securities Ltd	Class B notes	RMBS	Germany	Upgrade	A	A+
12 Dec 2006	Haus 2000-2 Ltd	Class B notes	RMBS	Germany	Upgrade	A	A+
12 Dec 2006	Provide Blue 2004-1	Class B	RMBS	Germany	Upgrade	AA	AA+
12 Dec 2006	Provide Blue 2004-1	Class C	RMBS	Germany	Upgrade	A	A+
12 Dec 2006	Provide Blue 2004-1	Class D	RMBS	Germany	Upgrade	BBB	BBB+
12 Dec 2006	Provide Comfort 2002-1 Plc	Class B	RMBS	Germany	Upgrade	AA	AA+

Rating Changes, January to December 2006 (Continued)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
12 Dec 2006	Provide Comfort 2002-1 Plc	Class C	RMBS	Germany	Upgrade	A	A+
13 Dec 2006	Aire Valley Finance (No.2) Plc	Class B notes	RMBS	UK	Upgrade	AA+	AAA
13 Dec 2006	Aire Valley Finance (No.2) Plc	Class C notes	RMBS	UK	Upgrade	BBB+	A+
13 Dec 2006	Auburn Securities 3 Plc	Class M	RMBS	UK	Upgrade	A	A+
13 Dec 2006	First Flexible No. 4 Plc	Class B	RMBS	UK	Upgrade	BBB	A
13 Dec 2006	First Flexible No. 4 Plc	Class M	RMBS	UK	Upgrade	A	AA-
13 Dec 2006	Shipshape Residential Mortgages No.1 Plc	Class C notes	RMBS	UK	Upgrade	AA-	AAA
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class B1a	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class B1b	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class M1	RMBS	UK	Upgrade	AA	AAA
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class M2	RMBS	UK	Upgrade	A	AA
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class B	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class M1	RMBS	UK	Upgrade	AA	AAA
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class M2	RMBS	UK	Upgrade	A	AA
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class B1a	RMBS	UK	Upgrade	BBB	A-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class B1c	RMBS	UK	Upgrade	BBB	A-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2a	RMBS	UK	Upgrade	A	AA-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2b	RMBS	UK	Upgrade	A	AA-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2c	RMBS	UK	Upgrade	A	AA-
20 Dec 2006	Bishopsgate CDO	Class A	CDO	Global (Blend)	Upgrade	AA+	AAA
15 Dec 2006	Coriolanus Limited Series 1	A	CDO	Global (Blend)	Upgrade	AA	AAA
15 Dec 2006	Coriolanus Limited Series 1	B	CDO	Global (Blend)	Upgrade	BBB	A
15 Dec 2006	Promise-I 2000-1	C-1	CDO	Global (Blend)	Upgrade	AA	AAA
15 Dec 2006	Promise-I 2000-1	C-2	CDO	Global (Blend)	Upgrade	AA	AAA
15 Dec 2006	Promise-I 2000-1	D-1	CDO	Global (Blend)	Upgrade	A	AAA
15 Dec 2006	Promise-I 2000-1	D-2	CDO	Global (Blend)	Upgrade	A	AAA
15 Dec 2006	Promise-I 2000-1	E-1	CDO	Global (Blend)	Upgrade	BB	A
15 Dec 2006	Promise-I 2000-1	E-2	CDO	Global (Blend)	Upgrade	BB	A
19 Dec 2006	Business Mortgage Finance 1 PLC	Class B	CMBS	UK	Upgrade	BBB	A-
19 Dec 2006	Business Mortgage Finance 1 PLC	Class M	CMBS	UK	Upgrade	A	AA
19 Dec 2006	Business Mortgage Finance 2 PLC	Class M	CMBS	UK	Upgrade	A	A+
20 Dec 2006	Leto (European Loan Conduit No.18) FCC	Class E	CMBS	France	Upgrade	BBB	AAA
20 Dec 2006	Leto (European Loan Conduit No.18) FCC	Class F	CMBS	France	Upgrade	BB	AA
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class B1a	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class B1b	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class M1	RMBS	UK	Upgrade	AA	AAA
14 Dec 2006	Residential Mortgage Securities 14 Plc (RMS 14)	Class M2	RMBS	UK	Upgrade	A	AA
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class B	RMBS	UK	Upgrade	BBB	A
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class M1	RMBS	UK	Upgrade	AA	AAA
14 Dec 2006	Residential Mortgage Securities 15 Plc (RMS 15)	Class M2	RMBS	UK	Upgrade	A	AA
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class B1a	RMBS	UK	Upgrade	BBB	A-

Rating Changes, January to December 2006 (Concluded)

Date	Issuer	Class	Asset type	Country	Rating action	Previous rating	New rating
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class B1c	RMBS	UK	Upgrade	BBB	A-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2a	RMBS	UK	Upgrade	A	AA-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2b	RMBS	UK	Upgrade	A	AA-
14 Dec 2006	Residential Mortgage Securities 16 Plc (RMS 16)	Class M2c	RMBS	UK	Upgrade	A	AA-

Source: Fitch

Appendix 3

Western Europe: Modifier Level Rating Transition Matrix – All Asset Types

3.1: One-Year Rating Transition Matrix, 2006

(%)	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC+	CCC	CCC-	CC and below	Total
AAA	98.73	0.48	0.16	0.56	0.08	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA+	32.61	55.43	3.26	3.26	5.43	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	11.23	10.18	74.15	3.39	0.26	0.26	0.52	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA-	12.82	5.13	12.82	66.67	1.28	0.00	0.00	0.00	0.00	1.28	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A+	1.94	5.83	14.56	9.71	66.02	0.97	0.97	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	1.90	0.24	3.81	5.00	8.57	78.81	0.95	0.00	0.48	0.24	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A-	0.00	0.00	4.69	3.13	6.25	9.38	62.50	12.50	1.56	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
BBB+	0.00	0.00	0.00	1.03	4.12	7.22	7.22	79.38	1.03	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.26	0.00	0.00	0.52	0.26	2.84	4.64	5.93	82.73	2.06	0.77	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
BBB-	0.00	0.00	0.00	0.00	0.00	2.22	0.00	4.44	2.22	84.44	2.22	0.00	2.22	2.22	0.00	0.00	0.00	0.00	0.00	0.00	100.00
BB+	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	3.70	7.41	85.19	0.00	3.70	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.85	2.56	0.00	0.85	0.00	0.00	2.56	0.85	2.56	88.89	0.00	0.00	0.85	0.00	0.00	0.00	0.00	0.00	100.00
BB-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
B+	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	16.67	16.67	0.00	0.00	66.67	0.00	0.00	0.00	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	5.88	88.24	0.00	5.88	0.00	0.00	0.00	100.00
B-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	14.29	85.71	0.00	0.00	0.00	0.00	100.00
CCC+	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	25.00	0.00	25.00	25.00	0.00	25.00	100.00
CCC-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

3.2: Average Annual Rating Transition Matrix, 1993–2006

(%)	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC+	CCC	CCC-	CC and below	Total
AAA	98.46	0.56	0.47	0.33	0.09	0.02	0.04	0.00	0.00	0.02	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA+	25.09	67.70	2.06	1.37	2.06	0.69	0.69	0.00	0.00	0.00	0.00	0.34	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	9.60	5.29	81.66	1.89	0.78	0.26	0.26	0.07	0.13	0.00	0.00	0.00	0.00	0.07	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA-	9.29	5.57	7.12	73.68	2.17	1.24	0.62	0.00	0.00	0.31	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A+	2.39	3.35	8.13	6.94	71.77	4.55	1.20	0.24	0.00	1.20	0.00	0.24	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	2.06	0.59	3.38	2.25	4.70	84.72	0.69	0.24	0.78	0.24	0.00	0.00	0.10	0.05	0.10	0.00	0.00	0.00	0.00	0.10	100.00
A-	0.68	0.34	1.69	3.73	3.05	5.08	73.90	5.08	2.03	2.03	0.34	0.34	0.34	0.34	0.68	0.00	0.00	0.00	0.00	0.34	100.00
BBB+	0.68	0.00	1.03	0.34	2.40	6.16	6.16	80.48	1.37	0.34	0.00	0.00	0.00	0.68	0.00	0.00	0.00	0.34	0.00	0.00	100.00
BBB	0.39	0.28	0.28	0.34	0.73	1.96	2.02	4.59	85.95	1.06	0.84	0.50	0.22	0.17	0.06	0.17	0.00	0.17	0.00	0.28	100.00
BBB-	0.61	0.00	1.21	0.00	0.00	0.61	0.61	3.03	2.42	80.00	1.82	1.82	3.64	1.21	0.61	0.00	0.00	2.42	0.00	0.00	100.00
BB+	0.00	0.00	0.00	0.00	0.87	0.00	0.00	6.09	5.22	1.74	78.26	0.87	1.74	2.61	0.00	0.87	0.00	0.87	0.00	0.87	100.00
BB	0.00	0.00	0.19	0.57	0.00	0.76	0.00	0.19	2.48	2.10	2.29	87.02	1.53	0.57	0.57	0.38	0.00	0.00	0.38	0.95	100.00
BB-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	77.78	2.47	7.41	2.47	1.23	3.70	0.00	4.94	100.00
B+	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	3.45	3.45	3.45	0.00	3.45	62.07	0.00	6.90	3.45	10.34	3.45	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	2.38	0.00	0.00	0.00	0.00	2.38	76.19	7.14	2.38	0.00	0.00	9.52	100.00
B-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	3.45	75.86	0.00	10.34	0.00	10.34	100.00
CCC+	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	50.00	0.00	0.00	50.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	3.03	0.00	3.03	60.61	0.00	33.33	100.00
CCC-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

Appendix 4 – Country Performance – One-Year Rating Transition Matrix

Table 1: France: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	0.00	100.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	6.25	0.00	93.75	0.00	0.00	0.00	0.00	0.00	100.00
BBB	12.50	0.00	12.50	75.00	0.00	0.00	0.00	0.00	100.00
BB	0.00	50.00	0.00	0.00	50.00	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00	100.00

Source: Fitch

Table 2: Germany: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	17.65	82.35	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	3.28	8.20	88.52	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	3.28	3.28	91.80	1.64	0.00	0.00	0.00	100.00
BB	0.00	8.11	2.70	2.70	86.49	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

Table 3: Italy: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	20.00	80.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	3.45	10.34	82.76	3.45	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	9.26	90.74	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	16.67	83.33	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 4: Netherlands: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	31.25	68.75	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	1.59	19.05	79.37	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	1.52	18.18	80.30	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	5.26	94.74	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 5: Spain: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	17.86	82.14	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.00	15.63	82.81	1.56	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	10.53	89.47	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	9.09	90.91	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	100.00	0.00	100.00

Source: Fitch

Table 6: UK and Ireland: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	5.88	94.12	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.70	9.15	88.73	1.41	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	6.25	93.06	0.69	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	2.00	96.00	2.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	85.71	14.29	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

Table 7: Other Countries: One-Year Rating Transition Matrix, 2006

All asset types

(%)	AAA	AA	A	BBB	BB	B	CCC	CC and below	Total
AAA	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
AA	3.23	96.77	0.00	0.00	0.00	0.00	0.00	0.00	100.00
A	0.00	7.32	92.68	0.00	0.00	0.00	0.00	0.00	100.00
BBB	0.00	0.00	3.57	96.43	0.00	0.00	0.00	0.00	100.00
BB	0.00	0.00	0.00	0.00	100.00	0.00	0.00	0.00	100.00
B	0.00	0.00	0.00	0.00	0.00	100.00	0.00	0.00	100.00
CCC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Source: Fitch

FitchRatings
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Corporate Finance

Credit Market Research

Fitch Ratings Global Corporate Finance 2006 Transition and Default Study

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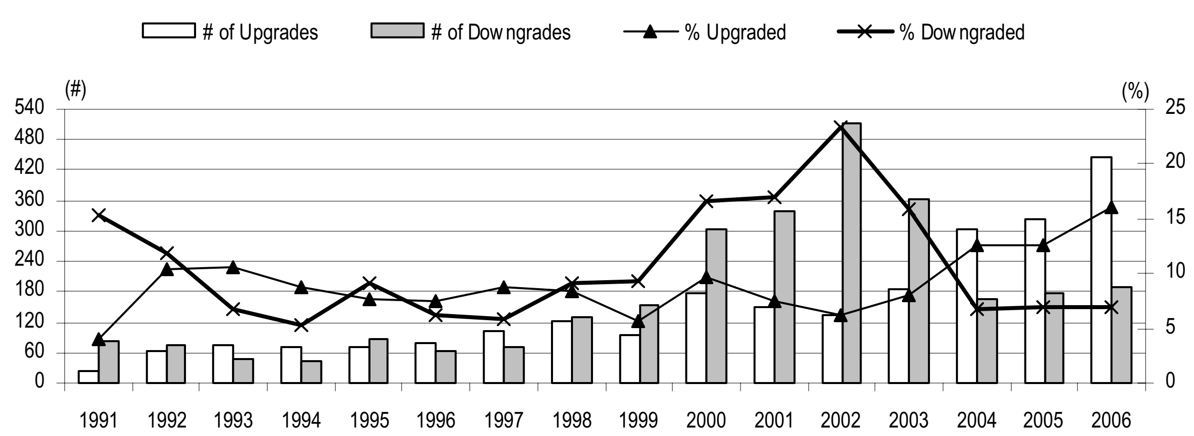
■ Summary

This study, updated through 2006, examines rating transition and default rates across Fitch's global corporate rating universe both over the most recent year, 2006, and over the long term, capturing the period 1990–2006. The study provides data and analysis on the stability of Fitch's corporate ratings and the ability of Fitch's ratings to predict default.

Overall, the benign global credit environment that has held the credit markets firmly in its grasp since 2004 persisted in 2006, yielding greater positive rating activity than negative. For the third consecutive year, upgrades surpassed downgrades, due most notably to upgrades among financial institutions and emerging market entities. For the year, upgrades affected 16.1% of Fitch's global corporate ratings universe, while downgrades affected 6.9%. The Historical Rating Changes chart below reflects the increase in upgrades over year-earlier activity, with upgrades climbing 37% in 2006, while downgrades moved up more modestly, increasing 7% year-over-year. The 2006 ratio of downgrades to upgrades (calculated at the modifier level and examining year-over-year rating movements) of 0.4 to 1.0 in 2006,

Fitch Global Corporate Finance Historical Ratings Changes*



*Compares beginning of year rating with end of year rating, does not count multiple rating actions throughout the year.

April 20, 2007

Fitch Ratings Global Corporate Finance Rating Movements Across Major Rating Categories
(%)

	1990–2005		2005		2006	
	Downgrade	Upgrade	Downgrade	Upgrade	Downgrade	Upgrade
‘AAA’	4.03	N.A.	6.56	N.A.	4.26	N.A.
‘AA’	7.88	0.10	2.24	0.00	1.20	0.00
‘A’	5.32	2.51	2.70	1.60	3.36	2.66
‘BBB’	5.08	4.67	5.69	4.62	2.78	6.95
‘BB’	10.49	7.54	4.61	8.55	9.02	13.41
‘B’	5.93	14.23	2.80	29.91	1.92	13.94
‘CCC’ to ‘C’	30.38	18.77	12.50	27.50	2.50	37.50

N.A. – Not applicable. Note: Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics.

shows an improvement over the ratio of 0.5 to 1.0 recorded in both 2005 and 2004. Similar to the preceding two years, 93% of ratings remained the same or experienced upgrades in 2006, while over the long term, on an average annual basis for the period 1990–2005, the share of ratings remaining the same or upgraded was 88%. Fitch’s rating stability was especially pronounced at the investment grade level, both for the most recent year with 94% of ratings either stable or upgraded, compared with 89% over the long-term 1990–2005 period.

Fitch-rated defaults declined to only two in 2006, compared with a total of eight recorded in 2005. Therefore, the 2006 annual default rate based on Fitch-rated issuers was just 0.07%, falling below the 0.29% reported in 2005. In fact, the 2006 annual default rate was Fitch’s lowest issuer-weighted annual default rate since the 0.08% recorded in 1997. Fitch’s default statistics continued to echo the temperament of the broader corporate market. For example, Fitch’s U.S. high yield par value default rate, based on the entire U.S. high yield market, was only 0.8% in 2006, down from an already low 3.1% in 2005 and considerably lower than the index’s long-term average annual default rate of approximately 5%[1]. Beyond the United States, Fitch’s European par-based high yield default rate for 2006 reached 0.6%, up modestly from the 0.5% reported in 2005, but nonetheless very low.

There continued to be a strong relationship between Fitch’s ratings and default risk. The 1990–2006 average annual default rate for Fitch’s investment-grade corporate ratings, for example, was just 0.10% through 2006. In contrast, Fitch’s average annual speculative grade default rate was 2.94%. Furthermore, an analysis of Fitch’s rating performance using Lorenz curves and Gini coefficients covering the period 1990 - 2006, again revealed that Fitch’s ratings exhibit a strong ability to predict default. Fitch’s Gini coefficients were 87.5%, 78.2% and 75.4% over one-, three- and five-year horizons, respectively.

Of note, Fitch continued the rollout of its long-term issuer default rating (IDR) methodology among its international corporate finance ratings in 2006, via U.S. and international banking, finance and insurance, as well as international industrials and power and gas. The IDR—a benchmark probability of default indicator—replaced Fitch’s long-term issuer rating, a proxy for default risk previously used as the central data point in Fitch’s Corporate Transition and Default Studies. For additional information concerning these rating enhancements, visit Fitch’s Website at www.fitchratings.com.

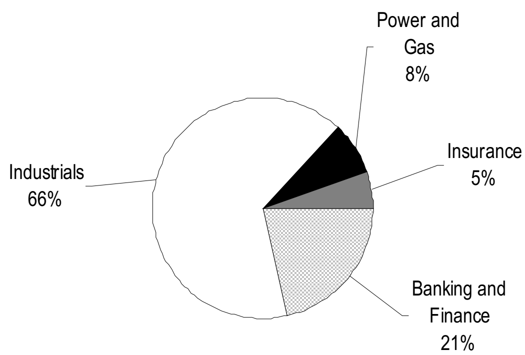
Fitch Global Corporate Finance Rating Actions By Sector — 2006*

	Downgrades		Upgrades	
Sector	No.	% of Sector Ratings	No.	% of Sector Ratings
Banking and Finance	41	3.3	216	17.1
Industrials	125	13.6	151	16.5
Power and Gas**	15	4.4	43	12.5
Insurance	10	4.1	35	14.2

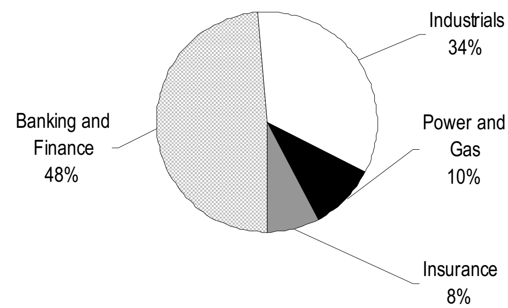
*Compares beginning of year rating to end of year rating; does not count multiple rating actions throughout the year. Rating changes defined at the modifier level, making a distinction between +/-.
**Previously referred to as Global Power.

[1] Please see the Fitch report, “The Shrinking Default Rate and the Credit Cycle—New Twists, New Risks” (dated Feb. 20, 2006), available at www.fitchratings.com.

Fitch Ratings Global Corporate Finance Distribution of Downgrades by Sector — 2006



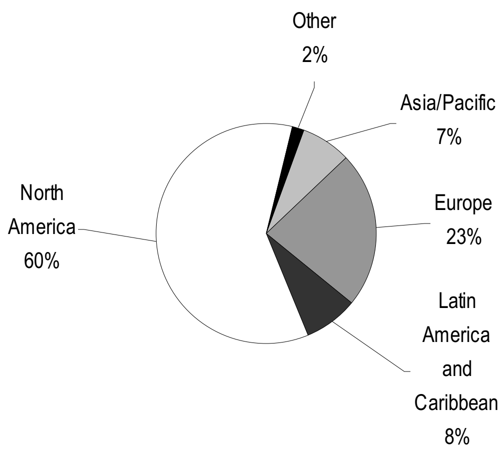
Fitch Ratings Global Corporate Finance Distribution of Upgrades by Sector – 2006



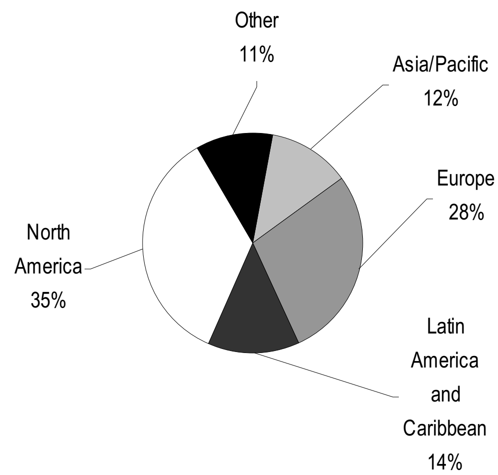
Highlights

- In 2006, upgrades continued to surpass downgrades for the third consecutive year, and at a slightly wider margin with a ratio of downgrades to upgrades on a year-over-year basis of 0.4:1.0 compared with 0.5:1.0 recorded in 2005.
- In addition to more moderate downgrade activity in recent years, compared with the 2000-2003 period, the past three years have witnessed a substantial rise in upgrades across the Fitch-rated universe. Fitch upgrade totals yielded their highest level at the end of 2006, as Fitch-rated entities receiving an upgrade reached 16.1%, climbing from the 12.5% recorded in both 2005 and 2004. Meanwhile, downgrades held relatively steady over the past three years, representing 6.9% of all rating activity in 2006.
- On an industry sector basis, in 2006 upgrades increased significantly over year-earlier levels, as banking and finance issuers observed upgrades surpassing downgrades at a pace of five to one, up from three to one in 2005. Driving a portion of the upgrades within the financial sector were upgrades linked to sovereign-related actions and country ceiling upward revisions, as well as merger and acquisition (M&A)-related activity. In contrast, downgrades edged lower within all sectors, except industrials, which climbed 51% year-over-year, a result of rising downgrades among North American and European industrial issuers, which combined represented 89% of all industrial downgrades in 2006.
- Improving economic conditions and Fitch-rated country ceiling upward revisions among many emerging market nations also contributed to significant positive rating activity among emerging market-based issuers. Nearly 40% of Fitch-rated emerging market issuers were affected by an upgrade, while only 5% experienced a downgrade.
- One component of 2006 rating activity that changed significantly from 2005 was the increase of multi-notch upgrades compared to multi-notch downgrades. Multi-notch upgrades exceeded their counterpart by two to one. In the same breath, rising stars easily exceeded fallen angels at the same pace—two to one. In both instances, this was a reversal from 2005 results that reported both fallen angels and multi-notch downgrades outpacing their positive equivalents.
- In 2006, only two Fitch-rated defaults were recorded: a single U.S. auto supplier, Dana Corporation; and one Uruguayan bank, Cooperative Nacional de Ahorro y Credito (COFAC). In fact, Fitch's 2006 annual default rate hit a low not observed in 10 years—0.07%.
- The ability of Fitch's ratings to predict default, as measured by calculating the Gini coefficient over the period 1990–2006, once again reflected strong historical rating performance for Fitch ratings. The resulting Gini coefficients for one-, three-, and five-year horizons were calculated as 87.5%, 78.2% and 75.4%, respectively.

Fitch Ratings Global Corporate Finance Distribution of Downgrades by Region — 2006



Fitch Ratings Global Corporate Finance Distribution of Upgrades by Region — 2006



■ Strong Global Economic Growth Boosts Credit Quality for Third Consecutive Year

Corporate rating activity—upgrades and downgrades—is defined here at the modifier level (i.e., 'A+' to 'A') as opposed to the broad or major rating category (i.e., 'A' to 'BBB'). Overall, credit quality displayed remarkable resilience in 2006, once again benefiting from the strength of the global economy, corporate profitability and the ease of bank lending practices. Although signs of fracturing appeared within the weakening U.S. automotive industry, the housing market slowdown, rising energy costs and interest rates, as well as geopolitical-related anxiety—all of which were unable to play the role of spoiler to global economic growth, as major global economies expanded at a rate of 2.9% in 2006.

On a year-over-year basis, 2006 witnessed greater positive rating activity than the previous year, with a downgrade to upgrade ratio of 0.4 to 1.0, compared with 0.5 to 1.0 in 2005. In fact, positive rating activity was at an all-time high for Fitch-rated corporate entities. Momentum coming off 2005 was on the upside and stayed that way, with 16.1% of all ratings receiving upgrades, while 6.9% of ratings were downgraded. In addition, low defaults were another reflection of improved credit quality, the absence of negative rating volatility, and ultimately the strength of the global economy. Thus, the resulting annual default rate for Fitch-rated issuers reached just 0.07% in 2006, below the 0.29% reported in 2005.

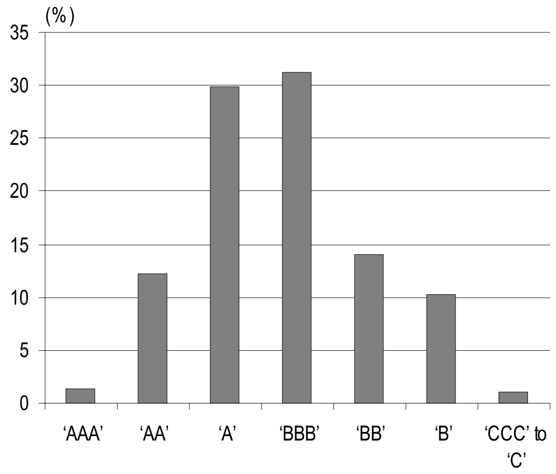
Downgrades edged modestly higher in 2006, up 7.3% over 2005 totals. Industrials carried the brunt of downgrades, accounting for 66% of all downgrades received by Fitch-rated issuers in 2006. Members of the automotive industry continued to shoulder some of the burden, as manufacturers and auto suppliers continued to experience first-hand the decline of the U.S. automotive industry, as weakening performance led to downgrades and a default, Dana Corp. Additionally, increased leverage and M&A-associated downgrades were well represented, as were downgrades due to other shareholder-oriented activities. Initiatives to benefit shareholders, at the expense of creditors, were heavy-handed in 2006, spurring downgrades on either side of the Atlantic, as issuers engaged in leveraged buyouts (LBOs) and debt-financed share buyback programs, among other shareholder-friendly activities.

Fitch Global Corporate Finance Rating Actions By Region — 2006*

	Downgrades		Upgrades	
Region	No.	% of Regional Ratings	No.	% of Regional Ratings
Asia/Pacific	14	4.0	54	15.4
Europe	44	5.9	125	16.9
Latin America and Caribbean	15	9.0	61	36.5
North America	115	8.2	156	11.1
Other	3	2.9	49	47.6

*Compares beginning of year rating to end of year rating, does not count multiple rating actions throughout the year. Rating changes defined at the modifier level, making a distinction between +/-.

Fitch Global Corporate Finance Ratings Distribution by Rating Category* — 2006



*End of year ratings, as of Dec. 31.

Banking and finance downgrades accounted for 21% of all downgrades in 2006, compared with 29% a year earlier. Downgrades among financial institutions were largely the result of weakening operating performance with just a hint of M&A-related downgrades. Insurance industry related downgrades were modest, responsible for only 5% of all downgrades. Likewise, power and gas entities accounted for just 8% of all Fitch-rated downgrades in 2006, in stark contrast to the credit erosion experienced in 2001 and 2002, when the sector accounted for 20% and 21%, respectively, of all downgrades.

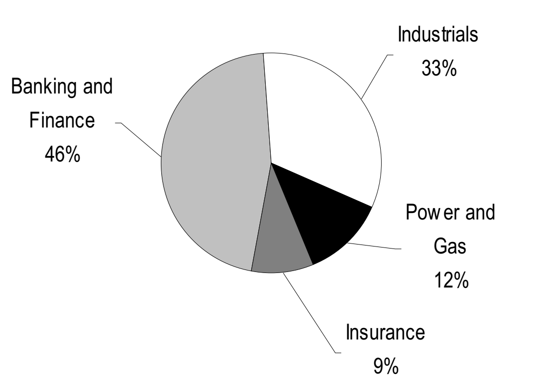
■ North American and European Industrials Dominate Downgrades in 2006

Regionally, North America captured the lion's share of downgrades with 60%, mirroring 2005's negative rating activity. The majority, or 69%, of the North American downgrades originated within the industrials sector, with auto and related, media and entertainment, and telecom accounting for the majority of negative rating activity. Weakness pervaded the U.S. auto sector dealing a number of negative rating actions, while shareholder initiatives, M&A activity and increasing leverage accounted for the majority of media and telecom downgrades.

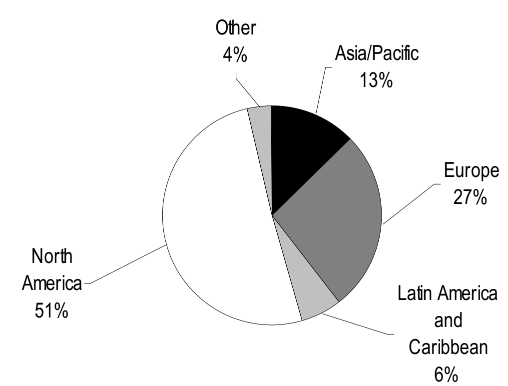
Europe, Latin America and the Caribbean, and Asia/Pacific aligned closely with year-earlier figures, accounting for 23%, 8%, and 7% of all Fitch downgrades, respectively. However, negative rating activity was most notable where it was absent— among emerging markets countries. Downgrades were few in number as improving economic conditions translated into positive rather than negative rating activity; only 5% of emerging market issuers were recipients of downgrades in 2006.

Another indication of the positive credit environment was the decline, albeit slight, of multi-notch

Fitch Global Corporate Finance Ratings Distribution by Sector — 2006



Fitch Global Corporate Finance Ratings Distribution by Region — 2006



Note: May not add to 100% due to rounding.

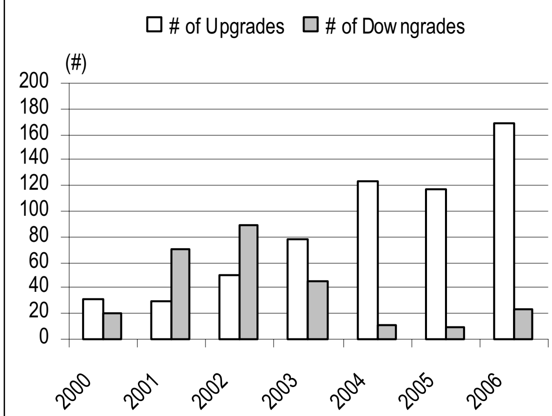
downgrades in 2006, falling 14.5% from year-earlier totals. The majority of these issuers resided in developed markets, as opposed to emerging markets, while auto-related, including both the corporate and financing arms of Ford Motor Company (Ford, to 'B' from 'BB+') were well represented among multi-notch downgrades. Furthermore, fallen angels took a dive in 2006, off by nearly half from year-earlier figures. Most fallen angels were located in North America; however, with an even market sector distribution. Notable 2006 fallen angels included U.S. automotive supplier Lear Corporation (to 'B' from 'BBB–') due to performance issues, and publisher-broadcaster, Tribune Co. (to 'BB+' from 'A–'), cited for shareholder-related initiatives.

Upgrades Strong Among Emerging Market Issuers in 2006

Turning to upgrades, 2006 totals easily outpaced downgrades, and bettered upgrade totals from 2005 and previous years as well. In 2006, upgrades jumped 37% over year-earlier totals, as positive rating activity touched every corner of the market. Upgrades affected 16.1% of the Fitch-rated corporate universe, up from 12.5% in 2005 and 2004. Several factors contributed to the bounty of upgrades, including, for one, the strong global economy, which spurred improving economic conditions in many major markets, as well as emerging market countries. This positive setting led to sovereign and sovereign-related upgrades, as well as contributed to country ceiling upward revisions that resulted in upgrades among emerging market issuers. Heated M&A-related activity was once again a factor, as M&A volume rose 40% over year-earlier figures to top $3.6 trillion on a global basis in 2006.

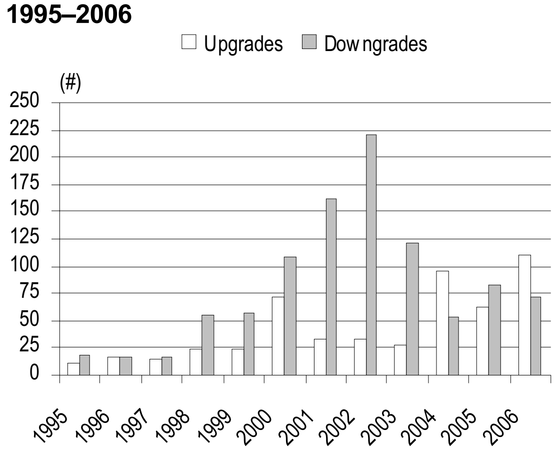
On a sector basis, positive rating activity was up across the board. Banking and financial institutions, registered the most upgrades—48% of all upgrades in 2006. Financial institution upgrades climbed 25% over levels recorded in 2005. As mentioned, several

Fitch Global Corporate Finance Emerging Market Historic Rating Activity*



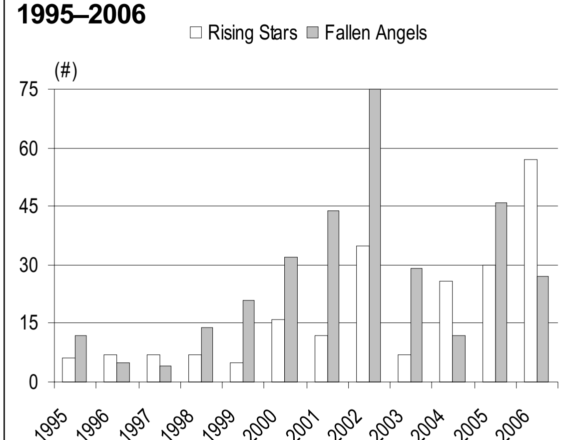
*Compares beginning of year rating with end of year rating, does not count multiple rating actions throughout the year. EM – Emerging market.

**Fitch Global Corporate Finance Multi-Notch Ratings Actions*
1995–2006**



*A multi-notch rating action is defined here as an upgrade or a downgrade of more than one notch examining rating changes on a year-over-year basis.

**Fitch Global Corporate Finance Fallen Angels and Rising Stars*
1995–2006**



*A Fallen Angel is an issuer downgraded from an investment grade to a speculative grade rating. A Rising Star is an issuer upgraded from a speculative grade to an investment grade rating.

factors contributed to the increase in banking and finance upgrades, most notably improving performance coupled with sovereign and/or country ceiling-related upgrades.

Additionally, industrials experienced an increase in positive ratings actions in 2006, elevating industrial upgrades by 42% from 2005. Industrials also account for 34% of all Fitch-rated upgrades on the year. Insurance and power and gas both moved ahead of year-earlier upgrade activity, power and gas by 59% and insurance nearly twofold, most notably on improving performance and leverage reduction.

Improving economic conditions extended to emerging markets in 2006, as a number of countries received sovereign upgrades, which in turn resulted in positive rating activity among domiciled issuers. Sovereign upgrades exceeded downgrades by 7 to 1, with 11 of the 13 upgrades bestowed upon emerging markets countries. Additionally, country ceiling upward revisions for 40 countries also led to rating upgrades among some domestic corporations and financial institutions. Country ceilings are, in effect, a cap on all foreign currency ratings of entities originating within each country Fitch rates. These constraints on foreign currency ratings capture the risk of exchange controls or transfer and convertibility risk. The revisions reflect improvements in these areas among many emerging market economies, as emerging markets have become an integral part of the global economy.[2] Moreover, Fitch's review of bank support among sovereigns within the Gulf Cooperation Council (GCC) of Middle Eastern nations, yielded upgrades for 28 banks located in the region.[3]

The combination of sovereign and country ceiling rating activity in 2006 contributed to upgrades for 37% of all Fitch-rated emerging market corporate finance issuers, compared with just 5% downgraded. See the Emerging Market Historic Rating Activity chart on page 6, detailing the changes in emerging markets rating activity since 2000.

North American and European issuers combined represented 63% of all Fitch upgrades in 2006. North America, Europe, and Latin America and the Caribbean experienced a rise in positive rating activity year-over-year, while upgrades took a tumble among Asia/Pacific issuers in 2006, off 27% from 2005.

Multi-notch upgrades climbed in 2006, up nearly 80% thanks in large part to sovereign-related upgrades, country-ceiling revisions and the M&A activity previously mentioned. Similarly, rising stars exploded in 2006 as well, outpacing year-earlier totals by 90% and outpacing fallen angels by more than 2 to 1. Notable non-sovereign, non-M&A related rising stars included Xerox Corporation and Legrand SA both to 'BBB–' from 'BB+', and both cited for reducing leverage.

■ Fitch Rating Migration Rates

An examination of the 2006 one-year rating migration data at the broad or major rating categories pinpoints the movement of ratings both up and down the rating scale (see the Global Corporate Finance Migration Rates table on page 8). The vertical left-hand column identifies ratings outstanding at the beginning of 2006, while the horizontal axis offers information on the migration pattern for those ratings by year's end. The table reflects the stability of Fitch's ratings over each rating category, most notably at the investment grade level, from the top left-hand corner, beginning with 'AAA' at 95.7% and following the diagonal to the right in order to examine the stability of each consecutive rating category. Overall Fitch's 2006 rating migration data revealed much more stability and positive, rather than negative, rating volatility, comparable to data from both 2005 and 2004.

The downgrade activity revealed no major surprises within the broad rating category detail for 2006, as downgrades edged up only within the 'A' and 'BB' rating categories. The single 'A' rating category experienced a downgrade rate of 3.4%, marginally higher than the 2.7% rate for 2005; however, this was lower than the average annual rate of 5.3% for the 1990–2005 period. Downgrades within the 'BB' category also rose year-over-year, to 9%, as a still relatively modest number of high yield issuers moved further into speculative grade territory.

Downgrade rates among the other major rating categories in 2006 either decreased or remained

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[2] Please see the Fitch report, "Country Ceilings" (dated Aug. 17, 2006), available at www.fitchratings.com.

[3] Please see the Fitch report, "Review of Bank Support in the GCC — Update" (dated Nov. 15, 2006), available at www.fitchratings.com.

comparatively unchanged year-over-year. For instance, in 2006, the share of 'AAA' and 'BBB' rated issuers downgraded were 4% and 3%, respectively, compared to 7% and 6% for the same respective categories in 2005. One area where the downgrade rate decreased substantially was among the 'CCC' to 'C' range, where negative rating activity fell from 12.5% to just 2.5% in 2006 compared with 2005, as defaults faded even at the lowest rating levels.

Speculative grade issuers, due to their highly levered operating and financial profiles, are more sensitive to economic swings and are generally more subject to rating changes than investment grade issuers. For instance, examining Fitch's 2006 rating activity at the modifier level during a positive credit environment revealed that 11% of investment grade issuers received upgrades, compared with 31% of speculative grade issuers. When examining data from a period of weaker credit quality, such as 2001, the reverse is true, generating greater negative rating volatility among both categories of issuers; however, similar to the previous example in that the changes are more pronounced at the speculative grade level, with 28% of speculative grade issuers receiving a downgrade in 2001, compared with 15% of investment grade issuers.

To this point, the biggest year-over-year changes among upgrades, when examining the annual transition tables at the broad rating category, were situated within speculative grade ratings. Although investment grade ratings held reasonably stable, this was not the case within speculative grade territory, where the largest swings in upgrade ratios among the rating categories were located at 'BB' and 'CCC' to 'C' with 13% and 38% of rated issuers upgraded,

Fitch Global Corporate Finance Migration Rates Across the Major Rating Categories*

(%)

2006

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC' to 'C'	'D'	Total
'AAA'	95.74	4.26	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	0.00	98.80	1.20	0.00	0.00	0.00	0.00	0.00	100.00
'A'	0.00	2.66	93.98	3.01	0.35	0.00	0.00	0.00	100.00
'BBB'	0.00	0.46	6.49	90.27	2.67	0.12	0.00	0.00	100.00
'BB'	0.00	0.00	0.49	12.93	77.56	8.78	0.00	0.24	100.00
'B'	0.00	0.00	0.00	0.96	12.98	84.13	1.92	0.00	100.00
'CCC' to 'C'	0.00	0.00	0.00	0.00	5.00	30.00	62.50	2.50	100.00

Average Annual Global Corporate Finance Transition Rates: 1990–2006

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC' to 'C'	'D'	Total
'AAA'	95.96	4.04	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	0.09	92.53	7.03	0.31	0.02	0.02	0.00	0.00	100.00
'A'	0.02	2.50	92.35	4.75	0.24	0.03	0.07	0.03	100.00
'BBB'	0.01	0.27	4.67	90.25	3.78	0.51	0.23	0.27	100.00
'BB'	0.04	0.07	0.19	8.14	81.29	7.17	1.76	1.34	100.00
'B'	0.00	0.00	0.00	0.76	13.42	80.46	3.76	1.60	100.00
'CCC' to 'C'	0.00	0.00	0.00	0.30	1.20	18.32	55.26	24.92	100.00

Average Two-year Global Corporate Transition Rates: 1990–2006

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC' to 'C'	'D'	Total
'AAA'	92.51	7.36	0.14	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	0.18	85.35	13.67	0.68	0.13	0.00	0.00	0.00	100.00
'A'	0.03	4.74	85.45	8.70	0.69	0.12	0.11	0.17	100.00
'BBB'	0.05	0.49	8.40	82.34	5.94	1.28	0.54	0.96	100.00
'BB'	0.05	0.24	0.62	14.34	68.59	9.54	2.35	4.27	100.00
'B'	0.00	0.00	0.09	2.06	24.33	65.74	3.40	4.38	100.00
'CCC' to 'C'	0.00	0.00	0.00	0.72	1.81	30.80	31.16	35.51	100.00

Average Three-year Global Corporate Transition Rates: 1990–2006

	'AAA'	'AA'	'A'	'BBB'	'BB'	'B'	'CCC' to 'C'	'D'	Total
'AAA'	88.61	10.61	0.62	0.16	0.00	0.00	0.00	0.00	100.00
'AA'	0.25	78.60	19.42	1.52	0.17	0.03	0.00	0.00	100.00
'A'	0.03	6.95	79.14	11.79	1.38	0.23	0.09	0.38	100.00
'BBB'	0.11	0.66	10.88	76.75	7.35	1.80	0.56	1.89	100.00
'BB'	0.00	0.36	1.69	17.43	59.11	11.34	2.71	7.36	100.00
'B'	0.00	0.00	0.24	3.80	26.72	58.31	2.85	8.08	100.00
'CCC' to 'C'	0.00	0.00	0.00	1.31	6.11	32.31	17.47	42.79	100.00

*Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics.

Fitch Ratings Global Corporate Finance Average Cumulative Default Rates: 1990–2006
(%)

%	1 Year	2 Year	3 Year	4 Year	5 Year
'AAA'	0.00	0.00	0.00	0.00	0.00
'AA'	0.00	0.00	0.00	0.03	0.06
'A'	0.03	0.16	0.32	0.48	0.73
'BBB'	0.26	0.87	1.61	2.53	3.47
'BB'	1.24	3.64	5.78	7.82	9.84
'B'	1.47	3.66	6.16	8.59	11.16
'CCC' to 'C'	22.93	30.72	35.64	41.63	43.41
Investment Grade	0.10	0.34	0.64	0.96	1.31
High Yield	2.94	5.75	8.25	10.74	12.72
All Corporates	0.61	1.27	1.89	2.51	3.04

Fitch Ratings Global Corporate Finance Issuer Default Rates*

	Number of Fitch-Rated Defaults	Default Rate (%)
1990	6	1.35
1991	10	1.81
1992	4	0.63
1993	0	0.00
1994	0	0.00
1995	1	0.11
1996	2	0.19
1997	1	0.08
1998	6	0.42
1999	13	0.77
2000	8	0.42
2001	19	0.81
2002	47	2.04
2003	25	1.02
2004	3	0.12
2005	8	0.29
2006	2	0.07

*Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics.

respectively in 2006. Similarly, the only rating level that resulted in a reduction in upgrades year-over-year was 'B', which declined to 14% in 2006 from 30% in 2005.

■ Fitch-Rated Issuer Defaults Contract Further in 2006

Fitch-rated defaults dropped considerably in 2006, to only two, down from eight documented in 2005. Thus, Fitch recorded an annual default rate of just 0.07%, down from 0.29% in 2005, and a 10-year low for Fitch-rated issuer defaults. No concrete trend surfaced between the two Fitch-rated defaulters. The defaulting issuers—a single U.S. auto supplier, Dana Corp. (Dana), and one Uruguayan bank, Cooperative Nacional de Ahorro y Credito (COFAC), whose operations were again suspended by Uruguayan authorities—were completely unrelated. However, Dana, extended 2005's trend of serious distress within the U.S. auto industry. Together with General Motors Corp. and Ford's downgrades further into speculative grade territory in 2006 and additional non-Fitch rated auto defaults, it is clear that the U.S. auto industry continues to struggle and experience credit deterioration among a considerable share of its market participants.

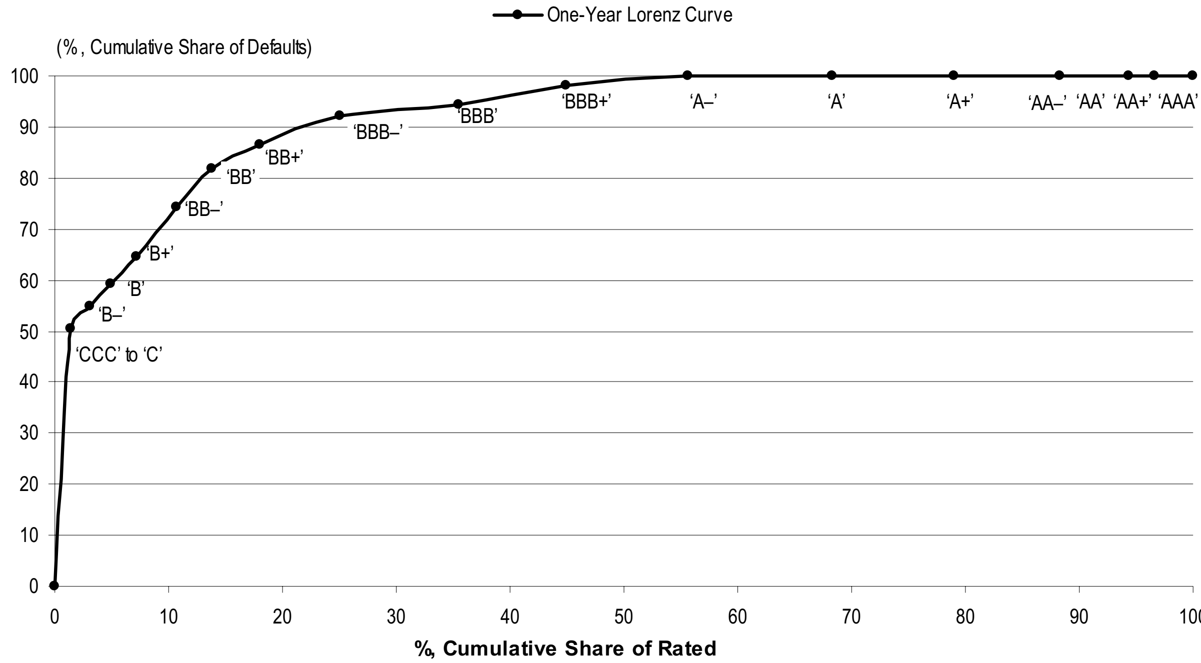
The long-term average annual default rate for Fitch-rated corporate issuers fell to 0.61% through 2006. The complete snapshot of default rates from one- through five-year periods at the major or broad rating categories is available in the Average Cumulative Default Rates table above. As per the data, the probability of default increases considerably with each incremental movement down the rating scale, but in particular when the movement coincides with a shift from investment grade to speculative grade.

As mentioned in previous studies, there are a few items worth noting with respect to the historical default frequencies displayed on this page. Default rates at the 'B' level, for example, appear modest relative to data reported by the other major rating agencies. This is due to Fitch's historically more limited coverage of the high yield market. However, the effect is diminishing quickly as Fitch's high yield market share grows. For example, as shown in the table Fitch Ratings Global Corporate Finance Most Recent Three-Year Cumulative Default Rates

Fitch Global Corporate Finance Ratings Gini Coefficients
(%, 1990–2006)

Time Horizon		
One-Year	Three-Year	Five -Year
87.5	78.2	75.4

Fitch One-Year Global Corporate Finance Rating Performance
(1990–2006)



(CDRs), on page 14 of the Appendix, the three-year CDRs for the 'BB' and 'B' categories for the 2004 cohort were 0.35% and 2.60% respectively, low due to the benign credit environment but illustrating a more meaningful gap than the average long-term three-year CDRs for 'BB' and 'B' issuers of 5.78% and 6.16%. Fitch expects the gap to continue to widen and other data-related anomalies to disappear as both sample sizes and observation years continue to grow. For a more detailed description of the methodology used to calculate Fitch's default rates see the Methodology section beginning below.

In order to broaden the traditional analysis of rating performance described above—specifically, the examination of rating performance utilizing default frequencies and rating transition rates—two additional measures of rating predictability were again computed for this recent study, the Lorenz curve and the Gini coefficient. The Lorenz curve is constructed by first ordering the population of ratings from the worst credit quality ('CCC' to 'C') to the best credit quality ('AAA') and then plotting the cumulative share of issuer ratings against the cumulative share of defaulters. This visual assessment of ratings performance is shown in the Fitch Corporate Finance Rating Performance chart above. The Gini coefficient summarizes the results of the Lorenz curve into a single statistic that ranges between 0% and 100%. A Gini of 100% would indicate that ratings had perfect ability to predict default.

The resulting Gini coefficients for the Fitch global corporate finance rating universe for the one-, three- and five-year time horizons over the 1990–2006 period are reported in the Fitch Global Corporate Finance Gini Coefficients table on page 9. The one-year accuracy ratio of 87.5%, the three-year accuracy ratio of 78.2%, and the five-year accuracy ratio of 75.4% continue to indicate a strong historical rating performance for Fitch. As shown in the one-year Lorenz curve above, speculative grade ratings ('BB+' and lower), while representing only 18% for all Fitch-rated global corporate issuers over the one-year period from 1990–2006, account for virtually 90% of all Fitch-rated defaults.

■ Fitch Transition and Default Methodology

All Fitch global, publicly rated, corporate finance long-term debt issuer ratings from 1990 to the present are included in Fitch's transition and default rate calculations.

Fitch employs a static pool approach in calculating its default and transition data. The static pools or,

Parameters of the Fitch Corporate Issuer Default Rate

- Statistical data captured in this study is based on the long-term IDR, where assigned, or historically the long-term issuer rating (a proxy of default risk). For those issuers not assigned an issuer level rating, an algorithm was used to derive an IDR proxy from the outstanding rated debt at year-end.
- Includes Fitch worldwide publicly rated corporate finance issuer IDRs and long-term debt ratings encompassing industrials, utilities, insurance, banks (includes bank holding companies, main subsidiaries and subsidiaries with debt outstanding) and other financial institutions.
- Structured finance, municipal, private placement and sovereign ratings were excluded from the study.
- Short-term issuer and debt ratings were also excluded from the study.
- The restrictive default (RD) rating is a default and counted as such.
- One-year default rates were calculated by dividing the number of defaulted issuers by the number of outstanding rated issuers at the beginning of each respective year.

alternatively, cohorts, are created by grouping issuer ratings according to the year in which the ratings are active and outstanding at the beginning of the year. For example, issuers with ratings outstanding at the beginning of 1990 constitute the 1990 static pool or cohort, with the same true for the 1991, 1992 and additional cohorts. Issuers newly rated by Fitch in any given year are included in the following year's cohort. For example, the performance of ratings initiated in mid-1995 would be followed as part of the 1996 and future cohorts. Ratings withdrawn mid-year are excluded from subsequent cohorts since they are no longer active, but are monitored for defaults. Defaults on withdrawn ratings are included in Fitch's average annual and multi-year default statistics.

Fitch's continuing data enhancement efforts may result in slightly different statistics than in previously published studies. Therefore, this most recent study supersedes all prior versions. In addition, comparisons with earlier Fitch corporate finance transition and default studies should be viewed within the context of the differing methodologies, whether rating movements were analyzed across the broad rating categories or at both the modifier and flat levels.

Transition Rates

In order to calculate one-year transition rates, Fitch examines the performance of ratings outstanding at the beginning of a calendar year and at the end. Withdrawn ratings are excluded from the transition table calculations since they do not fit this criteria, namely that the ratings be outstanding over a full year or over the full period under observation.

Issuer ratings may reside in multiple static pools, as long as their ratings are outstanding at the beginning and end of the year or multiple year horizons under observation. For example, the annual performance of an issuer rating initiated in 1994, and therefore outstanding at the beginning of 1995, and withdrawn in 1999, would be included in the 1995, 1996, 1997 and 1998 static pools. The rating's performance over multiple year horizons would also be included in the two-year, three-year and four-year transition rates for each of the cohorts noted, but excluded from five-year transition rates since the rating was withdrawn in year five and was not outstanding for five full years as part of any cohort. (In other words, as part of the 1995 cohort, this rating's performance would be monitored over a one-year period, 1995; two-year period, 1995–1996; three-year period, 1995–1997; and four-year period, 1995–1998). In all, Fitch's transition data contain 17 static pools or cohorts from 1990 to 2006, allowing for 17 unique one-year transition rates, 16 two-year transition rates, 15 three-year transition rates, and so on.

The one-year transition table on page 8 provides information on all rating movements by rating category from the beginning of a respective year to the end of that year. As illustrated in the transition table, the vertical left-hand column identifies ratings outstanding at the beginning of 2006, while the horizontal axis offers information on the migration pattern for those ratings by year's end. For example, the transition table reveals that 98.80% of issuers rated 'AA' at the beginning of 2006 remained 'AA' over the course of 2006 and that while none were upgraded, 1.20% were downgraded to the 'A' rating category. Multiple-year transition rates provide similar insight into rating performance, but over longer time horizons.

The occurrence and timing of both rating upgrades and downgrades for corporate issuers can be attributed to changes in qualitative and/or quantitative factors. Both qualitative and quantitative measures are used to assess the business and financial risks of corporate issuers. Qualitative analysis includes examining industry risk, operating environment, market position, management and accounting policies. In contrast, the quantitative aspect of Fitch's corporate ratings focuses on a company's policies in relation to operating strategies, acquisitions and divestitures, leverage targets, dividend policy and financial goals. An important component in the analysis is the company's ability to generate cash, which is reflected by the ratios that measure profitability and coverage on a cash flow basis.

The rating transitions outlined in this study represent a distinct historical period and may not represent future rating migration patterns. Transition rates are influenced by a number of factors, including macroeconomic variables, credit conditions and corporate strategy. The statistics presented here document the performance of Fitch-rated obligors. In general, the transition rates are similar to statistics reported by the other two major rating agencies. However, some sectors may show less deterioration than reported in the overall marketplace due to Fitch's market share composition. It is useful to examine the performance of Fitch ratings on a relative scale, within each rating category. In addition, it is important to point out that while transition matrices are presented at both the modifier and flat levels in this study, all other statistical analysis was conducted at the modifier level, unless noted otherwise.

■ Default Rates

Fitch's default rates are calculated on an issuer basis, as opposed to dollar amounts. First, defaults are examined by year for each static pool and individual rating category. For example, if 25 issuers defaulted in 2002, and the 2002 static pool consisted of 2000 issuer ratings, the resulting annual default rate for all ratings in 2002 would be 1.3%. If 10 of these defaults consisted of defaults among issuers rated 'BB' at the beginning of the year and the 'BB' cohort at the beginning of the year totaled 500, the 'BB' 2002 default rate would be 2% (10/500).

From these annual default rates, Fitch derives average annual default rates by weighing each cohort's default rates by the number of ratings outstanding in the given cohort relative to the number of total ratings outstanding for all cohorts. In other words, following the example above, the 2002 'BB' annual default rate of 2% might be followed by a 2003 'BB' annual default rate of 1%. A straight average of these two rates would ignore potential differences in the size of the two cohorts. Rather, weighing the results based on the relative number of 'BB' ratings outstanding in 2002 and 2003, gives greater emphasis to the results of the 'BB' cohort with the most observations.

The same technique is used to calculate average default rates over multiple year horizons. For example, the two-year default rate for the 2002 'BB' rating pool would be averaged with the two-year default rate for the 2003 'BB' rating pool by weighing the default rates by the relative size of each pool.

For example, any defaults produced by the 2002 'BB' cohort (the static pool) over the two-year time horizon are summed and divided by the number of 'BB' ratings outstanding at the beginning of 2002 to arrive at the simple 2002 two-year CDR for the 'BB' category. If a total of 15 issuers carrying 'BB' ratings at the beginning of 2002 default over the subsequent two years and 250 issuers were rated 'BB' at the beginning of 2002, 6.0% would be the resulting two-year CDR for the 'BB' rating category, if 10 issuers defaulted in year one and 5 in year two. The 2002 two-year 'BB' default rate would then be averaged with the 2003 two-year 'BB' default rate (using the same methodology just described) by weighing the results of the two by the relative number of 'BB' ratings outstanding in 2002 and 2003. (This is the general approach for calculating average cumulative default rates over multiple year horizons.)

Fitch Definition of Default

Fitch defines default as one of the following:

- Failure of an obligor to make timely payment of principal and/or interest under contractual terms of any financial obligation;
- The bankruptcy filing, administration, receivership, liquidation, or other winding-up or cessation of business of an obligor; or
- The distressed or other coercive exchange of an obligation, where creditors were offered securities with diminished structural or economic terms compared with the existing obligation.

■ Withdrawn Ratings

With regard to withdrawn ratings, all public ratings are included in the static pool data until the ratings are withdrawn and are then excluded from future static pools.

For the purpose of calculating default rates, however, Fitch tracks withdrawn ratings on a continual basis, and includes defaults on withdrawn ratings for the cohorts in which the ratings were active and outstanding. For example, a 'BB' issuer's rating is outstanding in 1995 and is withdrawn in 1997. The issuer defaults in 1999. The default would be included in the 1995 five-year default rate, 1996 four-year default rate and 1997 three-year default rate.

Appendix 1A

Fitch Ratings Global Corporate Finance Average Cumulative Default Rates: 1990–2006
(%, Modifier Level)

	1 Year	2 Year	3 Year	4 Year	5 Year
‘AAA’	0.00	0.00	0.00	0.00	0.00
‘AA+’	0.00	0.00	0.00	0.00	0.00
‘AA’	0.00	0.00	0.00	0.07	0.15
‘AA–’	0.00	0.00	0.00	0.00	0.00
‘A+’	0.00	0.08	0.21	0.28	0.37
‘A’	0.00	0.06	0.14	0.28	0.50
‘A–’	0.11	0.36	0.68	0.98	1.42
‘BBB+’	0.24	0.54	0.98	1.64	2.24
‘BBB’	0.14	0.81	1.82	2.78	3.74
‘BBB–’	0.47	1.38	2.16	3.34	4.76
‘BB+’	0.72	2.49	4.48	6.28	7.98
‘BB’	1.41	5.15	7.65	10.85	13.92
‘BB–’	1.71	3.67	5.73	7.16	8.74
‘B+’	1.46	3.77	6.60	8.88	9.25
‘B’	1.41	4.02	6.18	8.99	14.67
‘B–’	1.54	3.10	5.56	7.78	10.73
‘CCC’ to ‘C’	22.93	30.72	35.64	41.63	43.41
Investment Grade	0.10	0.34	0.64	0.96	1.31
High Yield	2.94	5.75	8.25	10.74	12.72
All Corporates	0.61	1.27	1.89	2.51	3.04

Appendix 1B

Fitch Global Corporate Finance Ratings Default Statistics for Basel II Users
(%)

Ten-Year Average of Three-Year Cumulative Default Rates (CDRs)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’
1995–2004	0.00	0.00	0.34	1.67	5.84	6.42

Most Recent Three-Year Cumulative Default Rates (CDRs)
(%)

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’
2004	0.00	0.00	0.00	0.24	0.35	2.60

	‘AAA’	‘AA’	‘A’	‘BBB’	‘BB’	‘B’
2003	0.00	0.00	0.00	0.54	1.19	3.13

Appendix 2

Fitch Global Corporate Finance Transition Rates at the Modifier Level

(%)

	'AAA'	'AA+'	'AA'	'AA–'	'A+'	'A'	'A–'	'BBB+'	'BBB'	'BBB–'	'BB+'	'BB'	'BB–'	'B+'	'B'	'B–'	'CCC' to 'C'	'D'	Total
One-Year : 2006																			
'AAA'	95.74	4.26	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA+'	0.00	94.59	0.00	5.41	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	0.00	1.19	92.86	3.57	2.38	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA–'	0.00	0.00	6.10	92.96	0.47	0.47	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A+'	0.00	0.00	0.41	7.88	87.97	3.32	0.41	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A'	0.00	0.00	0.00	0.65	4.90	90.20	2.61	0.98	0.33	0.00	0.33	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A–'	0.00	0.00	0.00	0.32	1.58	10.41	80.13	5.99	0.63	0.32	0.32	0.32	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'BBB+'	0.00	0.00	0.00	1.31	0.33	1.64	12.46	74.10	8.52	1.31	0.00	0.00	0.33	0.00	0.00	0.00	0.00	0.00	100.00
'BBB'	0.00	0.00	0.00	0.00	0.30	0.00	2.37	14.24	77.74	3.56	0.30	0.30	1.19	0.00	0.00	0.00	0.00	0.00	100.00
'BBB–'	0.00	0.00	0.00	0.00	0.00	0.00	1.36	3.17	15.84	71.95	2.71	4.07	0.45	0.00	0.45	0.00	0.00	0.00	100.00
'BB+'	0.00	0.00	0.00	0.00	0.00	0.74	0.74	0.74	4.41	25.74	54.41	2.94	0.00	0.00	10.29	0.00	0.00	0.00	100.00
'BB'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.82	0.82	5.74	26.23	53.28	4.92	2.46	5.74	0.00	0.00	0.00	100.00
'BB–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.66	0.66	11.18	22.37	56.58	5.92	1.32	0.66	0.00	0.66	100.00
'B+'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.23	0.00	0.00	8.64	13.58	62.96	13.58	0.00	0.00	0.00	100.00
'B'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.52	7.58	19.70	60.61	7.58	3.03	0.00	100.00
'B–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.64	0.00	1.64	3.28	3.28	13.11	73.77	3.28	0.00	100.00
'CCC' to 'C'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	2.50	0.00	2.50	2.50	0.00	27.50	62.50	2.50	100.00
Average Annual : 1990–2006																			
'AAA'	95.96	2.02	1.54	0.48	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA+'	0.51	84.29	11.99	2.36	0.17	0.34	0.17	0.00	0.17	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'AA'	0.00	2.53	81.75	11.10	3.51	0.39	0.19	0.19	0.00	0.26	0.00	0.00	0.06	0.00	0.00	0.00	0.00	0.00	100.00
'AA–'	0.04	0.04	3.89	85.19	7.99	2.03	0.51	0.17	0.08	0.00	0.00	0.00	0.00	0.00	0.00	0.04	0.00	0.00	100.00
'A+'	0.00	0.11	0.55	5.24	83.91	7.86	1.42	0.36	0.36	0.18	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
'A'	0.06	0.00	0.27	1.16	5.59	82.81	6.68	1.89	0.89	0.18	0.21	0.12	0.03	0.00	0.03	0.00	0.06	0.00	100.00
'A–'	0.00	0.00	0.11	0.26	1.13	7.16	79.96	8.54	1.42	0.77	0.15	0.18	0.00	0.04	0.00	0.04	0.15	0.11	100.00
'BBB+'	0.00	0.00	0.08	0.25	0.62	1.44	8.04	77.10	8.66	1.69	0.78	0.25	0.37	0.17	0.04	0.00	0.25	0.25	100.00
'BBB'	0.00	0.00	0.11	0.15	0.07	0.67	1.64	7.92	80.89	4.83	1.12	1.23	0.41	0.30	0.22	0.07	0.22	0.15	100.00
'BBB–'	0.06	0.06	0.00	0.17	0.22	0.22	0.33	1.71	10.94	76.30	5.19	2.15	1.16	0.39	0.22	0.17	0.22	0.50	100.00
'BB+'	0.00	0.19	0.00	0.00	0.00	0.10	0.29	0.97	2.92	13.02	69.97	4.86	1.85	1.55	2.04	0.29	1.17	0.78	100.00
'BB'	0.00	0.00	0.00	0.00	0.00	0.13	0.00	0.13	1.02	2.66	12.44	67.13	6.35	2.79	2.03	1.78	2.03	1.52	100.00
'BB–'	0.12	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.70	0.93	4.30	10.45	67.83	4.53	5.81	1.28	2.21	1.86	100.00
'B+'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.35	0.17	0.35	0.52	5.03	19.97	60.59	6.94	1.74	2.78	1.56	100.00
'B'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.22	0.67	1.56	5.79	21.16	59.69	6.46	2.90	1.56	100.00
'B–'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.48	0.48	0.24	0.24	0.73	1.45	4.60	12.59	71.43	6.05	1.69	100.00
'CCC' to 'C'	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.30	0.00	0.00	0.60	0.30	0.30	0.90	3.90	13.51	55.26	24.92	100.00

Appendix 3
Fitch-rated Global Corporate Finance Defaults 1990–2006*

Issuer Name	Rating at Beginning of Year	Industry Sector	Country
1990			
Allied Stores	'CCC'	Industrials	United States
Ames Department Stores, Inc.	'CCC'	Industrials	United States
Bank of New England Corporation	'CCC'	Banking and Finance	United States
Federated Department Stores, Inc.	'CCC'	Industrials	United States
Franklin Savings Association	'BB+'	Banking and Finance	United States
Greyhound Lines, Inc.	'CCC'	Industrials	United States
1991			
Carter Hawley Hale Stores, Inc.	'BB–'	Industrials	United States
Columbia Energy Group	'BBB'	Power and Gas	United States
Columbia Savings and Loan Assn.	'CCC'	Banking and Finance	United States
Continental Airlines Holdings, Inc.	'CCC'	Industrials	United States
Continental Airlines, Inc.	'CCC'	Industrials	United States
National Gypsum Company	'CCC'	Industrials	United States
Orion Pictures Corporation	'CCC'	Industrials	United States
People Express	'CCC'	Industrials	United States
Southeast Banking Corporation	'BB+'	Banking and Finance	United States
USG Corporation	'CCC'	Industrials	United States
1992			
Adience Inc.	'CCC'	Industrials	United States
El Paso Electric Co.	'B–'	Power and Gas	United States
First City Financial Corp.	'CCC'	Banking and Finance	United States
R.H. Macy Co.	'CCC+'	Industrials	United States
1995			
Dow Corning Corporation	'BBB–'	Industrials	United States
1996			
Grupo Simec, S.A. de C.V.	'CCC'	Industrials	Mexico
Kapital Haus, S.A. de C.V.	'CCC'	Banking and Finance	Mexico
1997			
First Merchants Acceptance Corp	'BB+'	Banking and Finance	United States
1998			
Chilesat S.A.	'BBB–'	Industrials	Chile
CRIIMI MAE, Inc.	'BB'	Banking and Finance	United States
P.T. Polysindo Eka Perkasa	'BB'	Industrials	Indonesia
Philip Services Corp	'BB+'	Industrials	Canada
Polysindo International Finance	'BB'	Banking and Finance	Indonesia
Reliance Acceptance Group, Inc.	'CCC'	Insurance	United States
1999			
ARM Financial Group, Inc.	'A–'	Insurance	United States
Bufete Industrials, S.A.	'BB–'	Industrials	Mexico
Grupo Tribasa, S.A. de C.V.	'BB–'	Industrials	Mexico
Hidroelectrica Piedra del Aguila S.A. (HPDA)	'BB'	Power and Gas	Argentina
Loewen Group International, Inc.	'BB–'	Industrials	United States
Menatep Bank	'C'	Banking and Finance	Russian Federation
Mobile Energy Services Co., L.L.C.	'CCC'	Power and Gas	United States
P.T. Inti Indorayon Utama	'CCC'	Industrials	Indonesia
SBS-AGRO Group	'C'	Banking and Finance	Russian Federation
Service Merchandise Company, Inc.	'CCC'	Industrials	United States
United Companies Financial Corp.	'B'	Banking and Finance	United States
United Export Import Bank	'C'	Banking and Finance	Russian Federation
Zenith Electronics Corporation	'CCC'	Industrials	United States

*Rated by Fitch at the beginning of the year in which they defaulted. Note: Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics. *Continued on next page.*

Appendix 3
Fitch-rated Global Corporate Finance Defaults 1990–2006* (Continued)

Issuer Name	Rating at Beginning of Year	Industry Sector	Country
2000			
ContiFinancial Corp.	'C'	Banking and Finance	United States
Daewoo Corporation	'CCC'	Industrials	Republic of Korea
Heilig-Meyers Company	'BB'	Industrials	United States
MacSaver Financial Services	'BB'	Banking and Finance	United States
Owens Corning	'BBB–'	Industrials	United States
Reliance Group Holdings, Inc.	'BB+'	Insurance	United States
Sunterra Corporation	'BB+'	Industrials	United States
Supercanal Holding S.A.	'CCC'	Industrials	Argentina
2001			
AEI Resources, Inc.	'CCC'	Industrials	United States
AMRESCO, Inc.	'BB–'	Banking and Finance	United States
Asia Pulp & Paper Co. Ltd	'B–'	Industrials	Indonesia
BROKAT Infosystems AG	'B'	Industrials	Germany
Comdisco, Inc.	'BBB+'	Industrials	United States
Enron Corp.	'BBB+'	Power and Gas	United States
Federal Mogul Corp.	'BB–'	Industrials	United States
FINOVA Capital Corp.	'CCC+'	Banking and Finance	United States
Focal Communications	'B'	Industrials	United States
Lakah Group	'CC'	Industrials	Egypt
Netia Holdings BV	'B+'	Industrials	Poland
Pacific Gas & Electric Co.	'BBB+'	Power and Gas	United States
Polaroid Corporation	'BB–'	Industrials	United States
Rhythms NetConnections Inc.	'B–'	Industrials	United States
SANLUIS Corp., S.A. de C.V.	'BB'	Industrials	Mexico
Southern California Edison Co.	'A–'	Power and Gas	United States
W.R. Grace & Co.	'BBB–'	Industrials	United States
Winstar Communications	'B–'	Industrials	United States
XO Communications, Inc.	'B'	Industrials	United States
2002			
Aguas Argentinas S.A.	'CC'	Power and Gas	Argentina
AMERCO	'BBB'	Banking and Finance	United States
Amtrade International Bank	'BB'	Banking and Finance	United States
Bahrain International Bank	'BBB–'	Banking and Finance	Bahrain
Banco Bisel	'CC'	Banking and Finance	Argentina
Banco Comercial del Uruguay	'BBB–'	Banking and Finance	Uruguay
Banco de Galicia y Buenos Aires	'CC'	Banking and Finance	Argentina
Banco De Inversion Y Comercio Exterior	'CC'	Banking and Finance	Argentina
Banco de la Provincia de Buenos Aires	'CC'	Banking and Finance	Argentina
Banco Hipotecario	'CC'	Banking and Finance	Argentina
Banco Rio de la Plata	'CC'	Banking and Finance	Argentina
BBVA Banco Frances	'CC'	Banking and Finance	Argentina
BCE Teleglobe	'B+'	Industrials	United States
BMB Investment Bank (formerly Bahrain Middle East Bank)	'B+'	Banking and Finance	Bahrain
Capex S.A.	'CC'	Power and Gas	Argentina
Conseco Finance Corp.	'CCC'	Insurance	United States
Conseco, Inc.	'B–'	Insurance	United States
Cornerstone Propane Partners L.P.	'BB–'	Power and Gas	United States
Cornerstone Propane, L.P.	'BB'	Power and Gas	United States
Edelnor S.A.	'B+'	Power and Gas	Chile
Edenor S.A.	'CCC'	Power and Gas	Argentina
Eletropaulo Metropolitana Eletricidade de Sao Paulo S.A.	'BB–'	Power and Gas	Brazil
Farmland Industries, Inc.	'BB–'	Industrials	United States
FLAG Limited	'BB+'	Industrials	Bermuda
FLAG Telecom Holdings	'B+'	Industrials	Bermuda

*Rated by Fitch at the beginning of the year in which they defaulted. Note: Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics. *Continued on next page.*

Appendix 3
Fitch-rated Global Corporate Finance Defaults 1990–2006* (Continued)

Issuer Name	Rating at Beginning of Year	Industry Sector	Country
2002 (Continued)			
GenTek Inc.	'BB–'	Industrials	United States
Hamilton Bancorp Inc.	'CCC'	Banking and Finance	United States
Hamilton Bank N.A.	'CCC'	Banking and Finance	United States
Hidroelectrica Piedra del Aguila S.A. (HPDA)	'CC'	Power and Gas	Argentina
HSBC Bank Argentina	'CC'	Banking and Finance	Argentina
Imagen Satelital S.A.	'CC'	Industrials	Argentina
InPower Limited	'BB'	Power and Gas	United Kingdom
Intermedia Communications Inc.	'BBB+'	Industrials	United States
Kmart Corp.	'BB+'	Industrials	United States
MetroGas S.A.	'CC'	Power and Gas	Argentina
NATG Holdings, LLC	'CCC–'	Industrials	United States
Pecom Energia S.A.	'B–'	Power and Gas	Argentina
Telecom Argentina Stet-France Telecom S.A.	'CC'	Industrials	Argentina
Transener S.A.	'CC'	Power and Gas	Argentina
Transportardora de Gas del Norte S.A.	'CC'	Power and Gas	Argentina
TXU Eastern Funding	'BBB+'	Power and Gas	United States
TXU Europe plc	'BBB+'	Power and Gas	United Kingdom
U.S. Industries, Inc.	'B'	Industrials	United States
Union Acceptance Corp.	'B+'	Banking and Finance	United States
Viasystems	'CCC'	Industrials	United States
Williams Communications Group	'CCC+'	Industrials	United States
WorldCom, Inc.	'A–'	Industrials	United States
2003			
AES DRAX Energy Limited	'C'	Power and Gas	United Kingdom
AES DRAX Holdings Limited	'CC'	Power and Gas	United Kingdom
Allegiance Telecom, Inc.	'CCC'	Industrials	United States
Asarco Incorporated	'CCC–'	Industrials	United States
Atlas Air Worldwide Holdings Inc.	'CCC'	Industrials	United States
Avon Energy Partners	'BBB–'	Power and Gas	United Kingdom
British Energy plc	'C'	Power and Gas	United Kingdom
Compania Internacional de Telecomunicaciones S.A. (COINTEL)	'CC'	Industrials	Argentina
Corporacion Durango, S.A. de C.V.	'B+'	Industrials	Mexico
DVI Inc.	'B+'	Banking and Finance	United States
Empresas Municipales de Cali S.A.	'CCC'	Power and Gas	Colombia
Fleming Companies, Inc.	'BB–'	Industrials	United States
Grupo Iusacell Celular, S.A. de C.V.	'C'	Industrials	Mexico
Grupo Iusacell, S.A. de C.V.	'C'	Industrials	Mexico
Mirant Americas Generation	'BB'	Power and Gas	United States
Mirant Corp.	'BB'	Power and Gas	United States
Mississippi Chemical Corp.	'CCC–'	Industrials	United States
Mutual Risk Management Ltd.	'CCC–'	Insurance	United States
Northwestern Corp.	'BBB'	Power and Gas	United States
Petroleum Geo-Services ASA	'CCC'	Power and Gas	Norway
Solutia Inc.	'B'	Industrials	United States
Telefonica de Argentina S.A.	'CC'	Industrials	Argentina
Transportadora de Gas del Sur (TGS)	'C'	Power and Gas	Argentina
Trenwick America Corp.	'CC'	Insurance	United States
WestPoint Stevens, Inc.	'CCC–'	Industrials	United States
2004			
Commercial Bank Credittrust	'CCC+'	Banking and Finance	Russian Federation
Finmatica SpA	'B+'	Industrials	Italy
TermoEmcali Funding Corp.	'CC'	Power and Gas	Colombia
2005			
Asarco Incorporated	'CCC'	Industrials	United States

*Rated by Fitch at the beginning of the year in which they defaulted. Note: Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics. *Continued on next page.*

Appendix 3
Fitch-rated Global Corporate Finance Defaults 1990–2006* (Continued)

Issuer Name	Rating at Beginning of Year	Industry Sector	Country
2005 (Continued)			
Calpine Canada Energy Finance ULC	‘CCC+’	Power and Gas	United States
Calpine Corp.	‘CCC+’	Power and Gas	United States
Cooperativa Nacional de Ahorro y Credito (COFAC)	‘CCC’	Banking and Finance	Uruguay
Delphi Corporation	‘BBB–’	Industrials	United States
Delta Air Lines	‘C’	Industrials	United States
Entergy New Orleans Inc.	‘BBB–’	Power and Gas	United States
Northwest Airlines, Inc.	‘B’	Industrials	United States
2006			
Cooperativa Nacional de Ahorro y Credito (COFAC)	‘CC’	Banking and Finance	Uruguay
Dana Corporation	‘BB–’	Industrials	United States

*Rated by Fitch at the beginning of the year in which they defaulted. Note: Data enhancement efforts may lead to slightly different results than previously published. Current study supersedes all prior statistics.

Ms. Ingrid Bonde
Director General
Finansinspektionen
3, Brunnsgatan Street
Stockholm
Sweden

30 November 2007

Re: Moody's Investors Service ("MIS") Response to the Committee of European Securities Regulators ("CESR") Expert Group on Credit Rating Agencies

Dear Ms. Bonde:

Further to our meeting in Stockholm on 5 October 2007 and your letter dated 14 November 2007 to Mr. Raymond McDaniel, I am pleased to attach MIS's written responses to the supplementary questionnaire enclosed in the 14 November letter. We hope that these responses will assist CESR in its annual review of the credit rating industry.

MIS requests that our responses to the following questions, contained in Annexes 1 to 4, be kept confidential:

Question 10.a – Exhibit 13 to our Form NRSRO Application (Annex 1)
Question 10.c (Annex 2)
Question 11 (Annex 3)
Question 16 (Annex 4)

We have asked for confidential treatment for these responses because MIS is a business and detailed information about compensation, staffing and turnover is a valuable company asset. Such information would be valuable to recruiters and businesses with whom we compete for talent. Consequently, public disclosure of this information could adversely affect our ability to recruit and retain employees.

If I can be of further assistance to CESR in conducting its work in relation to rating agencies, please do not hesitate to contact me.

Yours sincerely

Frédéric Drevon
Head of Europe, Middle East and Africa ("EMEA")
Senior Managing Director

MIS's Responses to CESR Questionnaire (dated 14 November 2007)

Transparency of methodology

1. Publication of methodologies and assumptions:

a. Is there a section on your website devoted to the publication of your methodologies?

Response: Yes. Methodologies can be accessed from our *Credit Policy* webpage. There is a link from our *Home Page* www.moodys.com to the *Credit Policy* webpage and then from the *Credit Policy* webpage to our *Rating Methodologies* webpage. The *Rating Methodologi*es webpage lists all rating methodology-related publications. Methodologies are listed in chronological order, with the most recent documents listed first. Users can re-sort the publication list by date (oldest first or newest first), title (ascending or descending alphabetical order) or sector (in ascending or descending chronological order).[1]

b. Do you provide explanations of the methodologies applied to the different categories of ratings for each asset class (e.g. RMBS, CDO, etc) separately by region?

Response: While many MIS methodologies have global application, we have developed more detailed and/or nuanced methodologies in circumstances where distinctions between particular regions or jurisdictions warrant a tailored methodology. Thus, we believe that high quality, consistent ratings are best achieved by the application of either a global or regional methodology while at the same time being sensitive to differences that may arise in different jurisdictions (such as accounting practices, bankruptcy regimes and competitive environments).

In the structured finance sector, we have published extensively on regional and jurisdiction-specific methodological approaches. For example, in the residential mortgage-backed securities ("**RMBS**") sector, we have published jurisdiction-specific[2] as well as regional[3] methodologies.

c. Do you provide the full method applied to each category of rating (e.g. RMBS, CDO) separately by region?

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1 MIS also has established dedicated webpages that bring together all relevant publications for issues of significant interest to investors. For example, on MIS's homepage, there is a link to a dedicated webpage, *Subprime & the Credit Markets*. There are also dedicated webpages for different sectors and asset classes. These sector and asset class webpages have their own *Rating Methodologies* links.

2 See e.g. *Moody's Approach to Rating Dutch RMBS*, December 2004 (Document SF37202); *Moody's Approach to Rating Spanish RMBS: The MILAN Model*, April 2005 (Document SF49068); *Moody's Approach to Rating Belgian RMBS*, September 2006 (Document SF79604); *Moody's Updated Methodology for Rating UK RMBS*, November 2007 (Document SF112854); *Moody's Approach to Rating Residential Mortgage-Backed Securities in Japan*: *Supplemental Series 13 – Loan by Loan Model and Loss Rate Distribution Assumptions*, November 2007 (Document SF113431); and *Rating US Option ARM RMBS – Moody's Updated Rating Approach*, September 2007 (Document SF104771).

3 See, e.g. *Moody's Approach to Rating RMBS in Emerging Securitisation Markets – EMEA*, June 2007 (Document SF97186) and *Moody's Approach to Rating Latin American Residential Mortgage-Backed Securities*, May 2002 (Document SF13805).

Response: Please see our response to Question 1.b.

d. Is all of the above information freely accessible or is part of it only available for subscribers?

Response: All of MIS's rating methodologies are made freely available to the public and are disclosed on our website,[4] subject only to the condition that an individual who wishes to use our website register and accept the associated "Terms and Conditions" and "Privacy Policy".[5] There is no initial or ongoing fee to become a registered user.

2. *Publication of changes in methodologies and assumptions:* Are all changes / adjustments to your methodologies and assumptions published and, if yes, where exactly are they published?

a. Is there a special section on your website where changes made to criteria can be reviewed over time?

Response: The *Rating Methodologies* webpage (accessible from a link on the *Credit Policy* webpage) lists and provides links to rating methodology-related publications. These include publications concerning significant amendments to methodologies and/or significant, systematically applied assumptions underlying our analytical approaches. MIS's assumptions are also factored into our models. The assumptions and inputs used in each model can be altered so that users can manipulate it to cater for various scenarios and better understand MIS's approach. MIS also publishes reports that highlight changes in our rating models, thereby enabling investors to track such changes.

MIS makes the following structured finance rating models freely available to registered users of our website:

MARVEL (MIS's Analytical Rating Valuation by Expected Loss);
MIS's CDOROM™ ;
MIS's STARFINDER; and
MIS's ABSROM™.

MIS also makes available on a subscription basis the following model-based tools, which enhance users' ability to analyse markets, compare the credit risks of different transactions, assess their credit exposures and/or monitor their portfolio's credit risk:

Moodys' CDOEdge™;
CDOROM data feed;
Performance Data Service ABS/RMBS; and
Performance Data Service CDO.

b. Do you publish reports that discuss the changes made to criteria?

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4 While MIS makes its rating methodologies publicly available, our credit ratings are opinions that are formulated by rating committees who consider qualitative as well as quantitative factors and must exercise judgment in the application of our methodologies.

5 It is possible to become an anonymous, registered user. We discuss registration (including the applicable Terms and Conditions) in more detail in our response to Question 7.

Response: Revised methodologies discuss the material changes that have been made to the prior version of the methodology. As discussed in more detail in our response to Question 30, MIS has published special reports that summarise changes in methodologies and assumptions over a specified period of time for sectors with large, dynamic credit markets.

c. Do you have press conferences to announce and explain those changes?

Response: It is not MIS's usual practice to hold press conferences or teleconferences to announce a new or modified rating methodology. As we indicated in MIS's *Code of Professional Conduct* (the "**MIS Code**")[6] and in our *Report on the Code of Professional Conduct*[7] *(*the "**MIS Report**"*)*, we publish our new and modified rating methodologies on our website. Methodologies that have a particularly broad reach and/or involve material modifications to existing methodologies or related significant practices, procedures and processes are announced via press release. We have also organised teleconferences to explain methodological changes where we believe there is significant market interest in such a teleconference.

Consistent with Section 3.13 of the MIS Code, where feasible and appropriate, proposed material modifications to rating methodologies and related significant practices, procedures and processes are made subject to a "Request for Comment" from market participants, prior to implementation of the change. Requests for Comment, which have their own dedicated webpage linked to our *Credit Policy* webpage, explain and seek the input of users of our credit ratings on the proposed changes. We believe this practice enhances analytical transparency and provides us with valuable input from users of our credit ratings, thereby enhancing methodological rigor.

3. Do you provide links/references to those publications mentioned in question 2 in the respective rating change reports (i.e. the announcement of a change would let the reader know where to find the related methodology)?

Response: When MIS effects a "Credit Rating action" (i.e. issues or changes a "Credit Rating"), it publishes a "Credit Rating Announcement"[8] on the MIS website. As we indicate in Section 3.2 of the MIS Code, Credit Ratings and a brief explanation of the rationale for the rating action remain on the MIS's public website for at least seven calendar days.

Where MIS changes a Credit Rating because of a change in the issuer's circumstances, the Credit Rating Announcement does not include links or references to methodology-related documents.[9] Credit Rating Announcements published on our website include a hyperlink from the issuer name to a webpage for that issuer, which is accessible to our subscribers. That webpage includes a hyperlink to a *Related Research* webpage for that issuer. The *Related*

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6 Revised October 2007, available at www.moodys.com.

7 April 2006, at p. 18, available at www.moodys.com.

8 These capitalised terms are defined in the MIS Code. A "Credit Rating" is defined to mean "MIS's current opinion regarding the relative future creditworthiness of an entity, a credit commitment, a debt or debt-like security, as determined by a rating committee and expressed using its established Aaa to C alpha-numeric rating scale, or other Credit Rating scales as identified from time to time by MIS". "Credit Rating Announcements" are "those written communications, including press releases, that publicly announce to the market a new MIS Credit Rating or a change to an existing MIS Credit Rating".

9 Please refer to our responses to Questions 4 and 29 for a discussion of the circumstances in which existing ratings are reviewed in light of changes to methodologies.

Research webpage includes links to a variety of documents, including a selection of applicable methodologies.

4. If changes have been made to your methodology for a particular product type (say US sub-prime RMBS) but previous issues have not been reviewed against this methodology how do you ensure this is clear to the marketplace? If the previous issues were being reviewed how would this be made public?

Response: Not all changes to methodologies have an impact on existing ratings. For example, methodological changes for structured finance asset classes tend to be incremental, reflecting, e.g. new trends regarding transaction structures, new forms of collateral being provided for a particular asset class or the emergence of new products that fit within the methodology's broad parameters. Such methodological changes are relevant for new issues but unlikely to affect existing, rated issues. In addition, for most asset classes (e.g. a structured transaction where the securities amortise or are collateralised by amortising assets), once the structured securities have been issued, our analysis will place more weight on the actual, rather than expected, performance of the underlying collateral for the securities. Actual asset performance becomes an increasingly more important factor as the securities season. For such transactions, changes to a methodology are unlikely to affect an existing rating.[10] Accordingly, it is implicit in the description of the change in methodology that existing ratings were not affected.

As part of the process for developing a revised methodology where MIS believes that the revision could affect existing ratings, MIS's usual practice involves an assessment (or "dimensioning") of the potential impact. Where MIS issues a Request for Comment in respect of a proposed amendment, a summary of this assessment would be included in the publicly disclosed "Request for Comment" discussed in our response to Question 2.c. above. Such disclosure is intended to assist users of our credit ratings in determining whether or not existing ratings might be affected by the change in methodology.

Where MIS believes that a proposed revision of a methodology could affect existing ratings, our usual practice when we publish the final version of a revised methodology is either: (1) to have already reviewed the potentially affected, existing ratings so that rating actions can be published as soon as the methodology is published; or (2) to disclose a timeline for the review of existing ratings. Historically, the nature of many structured finance methodological changes has meant that such reviews or announcements of timelines for review occurred rarely because most methodological changes were unlikely to affect existing ratings (for the reasons described above).

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[10] For example, RMBS methodologies indicate how MIS assesses the expected loss associated with a specific portfolio of loans using historical default and recovery data provided by the originator or based on comparable portfolios and benchmarking. The methodology also indicates how much credit enhancement (e.g. over-collateralisation) is necessary, depending on the level of expected loss. Once a transaction has received a rating, MIS collects and analyses actual performance data as part of the monitoring process. If the methodology is changed (e.g. to require more credit enhancement for a portfolio of loans with certain characteristics), this change in methodology will not be relevant for transactions that are performing at or above expectations, since additional credit enhancement is unnecessary. These previously rated transactions, however, would continue to be subject to monitoring. With respect to under-performing transactions, additional credit enhancement may not be required but such transactions would be selected for further review and might be downgraded, in accordance with standards reflected in the revised methodology.

5. Is publishing the methods you use enough to meet the requirements of the IOSCO Code and ensure sufficient transparency or do you see further possibilities for improving transparency/the understanding of:

a. your ratings?
b. your rating process?

Response: Transparency in the ratings system requires relevant ratings information, performance information and rating methodologies to be made available on a timely basis. MIS is fully committed to transparency in our rating process. MIS has a substantial, electronic library of communications, available on our website, explaining the meaning of our ratings, describing our rating process and disclosing our rating methodologies. In October 2007, we also published the revised MIS Code. MIS believes that the provisions it has adopted in the MIS Code relating to transparency fully implement the relevant provisions in the *Code of Conduct Fundamentals for Credit Rating Agencies* issued by the Technical Committee of the International Organisation of Securities Commissions (the "**IOSCO Code**")[11] and ensure sufficient transparency regarding our methodologies.

While we believe that our publications satisfy the requirements in the IOSCO Code and ensure sufficient transparency, we seek continuously to make it easier for our website's users to search for and retrieve the information we make available. For example, we are in the process of enhancing our website's search function so that taxonomically-driven searches can be carried out. We are committed to better understanding the evolving needs of the various users of moodys.com and developing mechanisms to further enhance the accessibility of the information we provide.

MIS is also pursuing certain initiatives designed to enhance investors' understanding of our ratings and rating process. For example:

Transparency regarding quality of information: Relevant data for modelling or estimating future risk can never be definitive and may under-represent infrequent periods of extreme stress. As a result, models of future collateral performance involve a high degree of human judgment. The layering of risks and potential for interactions among those layers can give rise to "perfect storm" situations. To address these concerns, the approval of new models and methodologies will address the quality and completeness of underlying data and estimate the sensitivity of results to a range of input error. A summary discussion of these findings will be included in MIS's published methodology and, where relevant, transaction or issuer-focused research reports that MIS publishes.

Framework analysis: Rating committees are expected to bring to bear a range of practical credit experience to complement the output of methodologies and models. Legal risks, third party performance and modelling risk may be considered. Rating committees often discuss expectations about the likely impact of broader economic stress, changes in market behaviour, the competitive environment and management performance. It is important that credit rating agencies publicly communicate these assumptions and expectations (subject to confidentiality obligations, for example, in the case of issuer-specific or competitive information), which can significantly affect ratings. Consequently, MIS has initiated a *Global Financial Risks Perspectives* series

[11] December 2004 (Document Number 180), available at www.iosco.org.

to communicate our views on broad risks to the financial stability of global capital markets. For analytic purposes, on an annual basis MIS will establish several, possible global economic and financial scenarios that stress or vary current market or business conditions. These scenarios will be used to assist thinking about the likely future performance of our ratings and may be discussed in industry or sector outlook comments to enhance transparency. Furthermore, additional assumptions about macroeconomic, financial, market, regulatory or political developments that are deemed significant to a rating decision will be noted in MIS's relevant research. New issue reports for certain structured securities will also discuss the degree and kind of stress that might cause rated securities to suffer a material impairment.

New analytical tools for investors: Investors might make better, more informed use of credit ratings if they are used together with valuation tools and volatility metrics. For example, Moody's Wall Street Analytics, a division of Moody's Corporation ("**MCO**") that is separate from MIS, recently announced a new discounted cash flow valuation ("**DCV**") tool that is intended to enhance the transparency of US collateralised debt obligations ("**CDOs**") by providing independent fundamental valuation information.[12]

We suggest, however, that whether or not investors actually track changes in our methodologies also depends, in part, on their willingness to, and ability to stay abreast of, changes in complex, global capital markets, with which our rating process and methodologies must also necessarily keep pace. Consequently, and especially in periods when markets are robust and buoyant, we may publish far more content than the market is willing or able to read.

Furthermore, despite numerous publications, misunderstandings about the objectives and actual performance of our ratings persist. We are particularly concerned that some professionals making investment decisions on behalf of others have not demonstrated a willingness to invest their time to read the information we make available to the public and our subscribers regarding the meaning of, and appropriate uses of, our ratings. We believe that authorities, credit rating agencies and market participants need to work together to facilitate the development of effective incentives that will motivate investors, especially those paid to make investment decisions on behalf of others, to:

develop a complete understanding of the meaning and appropriate use of ratings and track developments in rating methodologies and rating processes applicable to the issuers and securities in which they invest; and

remain informed about developments in rating methodologies.

6. What steps does your firm take, if any, to contribute to enhancing the financial education of investors or potential investors?

Response: As noted in our response to Question 5, MIS makes a significant amount of information available without charge to investors and potential investors regarding the meaning of ratings, our rating process and our rating actions. We also host frequent

[12] The new service, called Credit Values DCV, will enable subscribers to compare the DCV of their securities to trading values based on pre-defined or user-defined parameters and calculate the sensitivity of the DCV to different market and credit conditions. This service will also facilitate the assessment of ratings volatility.

conferences and teleconferences on credit-related matters.[13] Many of our briefings and teleconferences are available without charge to registered users and presentation materials are often published on our website in an online archive for past events that can be accessed by registered users.

In addition, MIS and MCO support financial education through various mechanisms. For example, MCO has established a Credit Markets Research Fund to promote the study of credit markets and credit-related topics. MCO has also established the Moody's Foundation®, a charitable foundation whose primary donation focus is secondary and higher education with a focus on economics, finance and mathematics. MCO also supports employee volunteerism, including with respect to initiatives that support financial education.

MIS makes available to subscribers various credit-related publications, such as our "weekly credit trends" publication, a "credit perspectives" series in various analytical sectors, numerous industry studies or outlooks[14], market overviews (such as year end reviews for each structured finance asset class in different regions[15]) and banking system outlooks[16]. In addition, MCO through Moody's Analytics offers for purchase a range of wide range credit training services, including seminars in various regions, E-learning and books.

7. Do you take steps to clarify any limitations to your ratings, including what they are intended to cover, or the methodologies and the assumptions underpinning them? How do you do this?

Response: As part of our responsibility to the market, we believe it is important to emphasise our ratings' attributes and limitations.[17] In particular, we have made it clear that our ratings are not designed to address any risk other than credit risk and should not be used for any purpose other than as a gauge of default probability and expected credit loss. Our ratings are not, and should not be treated as, statements of fact about past occurrences, guarantees of future performance or investment recommendations. The likelihood that debt will be repaid is just one element, and in many cases not the most material element, in an investor's decision-making process for buying credit-sensitive securities. Credit ratings do not address many other factors in the investment decision process, including the price, term,

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[13] See e.g. Moody's Germany: Financial Institutions Conference 2007 (Frankfurt, 25 October 2007).

[14] See e.g. *Industry Outlook: French Life Insurance*, October 2007 (Document 104934).

[15] See e.g. *Special Report: 2006 Review and 2007 Outlook: Italian Structured Finance*, January 2007 (Document SF90245).

[16] See e.g. *Banking System Outlook: Denmark*, November 2007 (Document 105786).

[17] For examples, see our publications such as: *Understanding Moody's Corporate Bond Ratings and Rating Process*, May 2002; *Comments from Moody's Investors Service on the European Commission Services' New Capital Adequacy Directive: Recognition and Supervision of ECAIs*, January 2003; *Measuring the Performance of Corporate Bond Ratings*, April 2003; *Moody's Investors Service Response to the Director General Internal Market Services' Working Document on the Implementation of the European Parliament and Council Directive 2003/6/EC on Insider Dealing and Market Manipulation*, April 2003; *Moody's Investors Service Comments on the Securities and Exchange Commission's Concept Release on Rating Agencies and the Use of Credit Ratings under the Federal Securities Laws*, July 2003; *Are Corporate Bond Ratings Procyclical?*, October 2003; *Statement of Raymond McDaniel at the 29th Annual Meeting of the International Organization of Securities Commissions*; October 2003; *Statement of John Rutherfurd at the 30th Annual Meeting of the International Organization of Securities Commissions*; April 2005; *Moody's Investors Service Comments on the Securities and Exchange Commission's Rule Proposal on the Definition of Nationally Recognized Statistical Rating Organization*, June 2005; the MIS Code, June 2005 (revised October 2007); *Response of Moody's Investors Service to The Committee of European Banking Supervisors' Consultation Paper on the Recognition of External Credit Assessment Institutions*, September 2005.

likelihood of prepayment, liquidity risk or relative valuation of particular securities. We have consistently discouraged market participants from using our ratings as indicators of price, as measures of liquidity or as recommendations to buy securities.

We describe our ratings' attributes and limitations on our website and in a variety of publications. For example, the *About Moody's* webpage includes a hyperlink to our *Rating Approach* webpage, which describes our approach to credit rating analysis and includes a hyperlink to our publication, *Moody's Rating System*. Likewise, the MIS Code clearly and prominently explains what ratings are and what they are not. It also states that MIS relies on issuers and their agents to provide accurately, timely and complete information and that MIS does not independently verify the information it receives, has no obligation to perform due diligence with respect to the information it receives and does not, in fact, carry out such due diligence.[18]

Each of our rating reports states clearly that:

> MIS's credit ratings and financial reporting analysis observations, if any, are and must be construed solely as statements of opinion and not statements of fact or recommendations to purchase, sell or hold securities.
>
> Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling.

Furthermore, to become either a registered user, with access to the free content such as rating methodologies on moodys.com, or a paid subscriber, a person must scroll through the entire text of Moody's "Terms of Use" and "Privacy Policy" and then click a box to acknowledge that he or she has read and agreed to the Terms of Use and Privacy Policy. The Terms of Use include the following disclaimer:

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[18] Section II of the MIS Code states, in part:

"Credit Ratings are MIS's current opinions of the relative future creditworthiness of entities or instruments, not statements of current or historical fact. Credit Ratings do not constitute investment or financial advice, and Credit Ratings are not recommendations to purchase, sell, or hold particular securities. Credit Ratings do not comment on the suitability of an investment for any particular investor. MIS issues its Credit Ratings with the expectation and understanding that each investor will make its own study and evaluation of each security that is under consideration for purchase, holding, or sale.

MIS Credit Ratings are based on information obtained by MIS from sources believed by MIS to be accurate and reliable, including but not limited to Issuers and their agents and advisors (e.g., accountants, legal counsel, and other experts). MIS relies on Issuers and their agents to provide accurate, timely, and complete information.

MIS has no obligation to perform, and does not perform, due diligence with respect to accuracy of information it receives or obtains in connection with the rating process. MIS does not independently verify any such information. Nor does MIS audit or otherwise undertake to determine that such information is complete. Thus, in assigning a Credit Rating, MIS is in no way providing a guarantee or any kind of assurance with regard to the accuracy, timeliness, or completeness of factual information reflected, or contained, in the Credit Rating or any related MIS publication."

> "You expressly agree that (a) the credit ratings and other opinions provided via any of the Websites are, and will be construed solely as, statements of opinion and not statements of fact as to creditworthiness or recommendations regarding credit decisions or decisions to purchase, hold or sell any securities or endorsements of the accuracy of any of the data or conclusions, or attempts to independently assess or vouch for the financial condition of any company; (b) each rating or other opinion will be weighed, if at all, solely as one factor in any investment or credit decision made by or on behalf of you; and (c) you will accordingly make your own study and evaluation of each credit decision or security, and of each issuer and guarantor of, and each provider of credit support for, each security or credit that you may consider purchasing, holding, selling, or providing."

For specific sectors, MIS has also made available to the market, analytic tools providing full access to the detailed assumptions underlying our analysis. For example, in July 2005 MIS launched Moody's Mortgage Metrics, which has a specific subprime mortgage module that complements the prime module to cover the whole spectrum of RMBS. Moody's Mortgage Metrics is an analytic tool enabling the market to assess the risks and credit enhancement levels of residential mortgage loan pools. The model incorporates a wide array of in-depth variables. Moody's Mortgage Metrics accounts for the complex interaction of economic stresses, market dynamics and loan performance by modelling links between local economic shifts, loan and pool-level defaults and loan loss severity. The model also provides qualitative inputs, including MIS servicer ratings and assessments of origination, underwriting, skill and appraisal quality. Consequently, the market has had full access to the detailed assumptions underlying our RMBS analysis and has been able to manipulate the model to cater for any number of scenarios to test the limitations of our assumptions in any given situation.

MIS is also making more information available about our approach to monitoring particular classes of structured finance transactions.[19] This includes information about the assumptions in the models we use in our monitoring activities. These publications facilitate better dialogue with users of our ratings, thereby enhancing their understanding of the rating (and associated monitoring) process.

8. Do you publish, and if so, where, your approach to the use of confidential information in rating of structured finance operations? Does it differ from that which you follow in "traditional" corporate rating?

Response: Our approach to the use of confidential information is the same in respect of rating structured finance transactions as it is for other issuers and issuances. See Section 3.B of Part III of the MIS Code.

9. Do you consult with industry as to what disclosure levels they would like to see for methodology and model assumptions?

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[19] See e.g. *Surveillance Process for Moody's-Rated ABS and RMBS in EMEA*, August 2007 (Special Report, SF105658); *Surveillance Process for Moody's-Rated RMBS and ABS*, March 2007 (Special Report, Document SF95523); and *Moody's Approach to Monitoring CMBS Ratings in Japan,* October 2005 (Special Report, Document SF62932). In addition, in November 2007, MIS launched a new European service, called EMEA Performance Data Services ("EMEA PDS"), which makes all performance information across all transactions available via a single, interactive web platform to subscribers. The platform includes the same data, risk analytics, reporting and warning alerts that MIS's surveillance analysts use to monitor credit in structured finance transactions.

Response: As noted in our responses to Questions 2.c and 4, the MIS Code provides that, where feasible and appropriate, we will employ a "Request for Comment" process with respect to proposed material modifications of our methodologies and related, significant practices, procedures and processes. MIS also regularly engages in dialogue with users of MIS's ratings, soliciting feedback on existing methodologies and models as well as suggestions for improvements. MIS staff also make presentations at industry conferences, which create additional opportunities for discussion of our methodologies and the needs of users of MIS's ratings. In addition, MIS's rating methodology publications include the contact names and telephone numbers of the rating group, thereby enabling people to contact our analysts and their managers directly to discuss our methodologies.

<u>**Human Resources**</u>

10. Please provide us with the following information with regard to SF ratings and traditional ratings:

a. Exhibit 4, 8 and 13 of your NRSRO application form

Response: Exhibits 4 and 8 of MIS's Application Form to become a Nationally Recognised Statistical Rating Organisation ("**NRSRO**") are publicly available on our *Regulatory Affairs* webpage.

Exhibit 13 of our NRSRO Application Form is attached as Annex 1 to our response. It contains compensation data (total and median compensation data for credit analysts), which we consider to be sensitive information. Accordingly, we request that this document be kept confidential.

b. The internal definition of the existing classes/levels of employees in the CRA's rating business: e.g. junior/mid/senior analysts, supervisors, committee analysts, lead analysts, etc?

Response: MIS uses the following terminology to differentiate the different levels of professional, analytical staff: (1) managers; (2) senior analysts; and (3) junior analysts.

Managers hold the titles of (in ascending order) of Team Managing Director, Group Managing Director or Senior Managing Director. Team Managing Directors generally oversee rating teams that focus on a particular industry or asset class within a region. Their responsibilities generally include, among other things, managing rating assignments, overseeing and monitoring outstanding credit ratings, chairing rating committees, reviewing written research and ensuring that credit policies are appropriately implemented within their respective teams. Some Team Managing Directors oversee groups of specialists (e.g. in Accounting, Corporate Governance or Risk Management Assessment) who work with credit analysts in rating groups. Group Managing Directors generally manage large, regional subdivisions within the global rating groups (e.g. the European Corporate Finance Group). Senior Managing Directors oversee the activities of our global rating groups (such as the global Financial Institutions Group), our specialist groups and/or our major business regions, such as EMEA (i.e. Europe, the Middle East and Africa).

Senior analysts hold the titles of (in ascending order) Vice President-Senior Analyst, Vice President-Senior Credit Officer or Senior Vice President. Senior analysts typically are given primary responsibility for the credit analysis of a portfolio of issuers or obligations and are assigned to such issuers or obligations based on their relevant experience and training. Lead analysts typically are senior analysts.[20] As lead analysts, senior analysts often supervise the work carried out by junior analysts relating to issuers or transactions for which the senior analyst has primary responsibility. Some senior analysts (e.g. Senior Vice Presidents and Senior Credit Officers) have supervisory responsibilities with respect to certain aspects of a rating group (or sub-group's) work (such as the work of a surveillance team in our Structured Finance rating department), under the overall supervision of a Team Managing Director. Nevertheless, MIS classifies them as senior analysts, not managers.

Junior analysts hold the title of (in ascending order) Statistical Analyst, Associate Analyst, Analyst or Assistant Vice President-Analyst. Back-up analysts typically are junior analysts, but for certain issuers or obligations might also be senior analysts. Some Analysts and Assistant Vice President-Analysts may serve as lead analysts, although usually they will have responsibility for a smaller portfolio and less complicated credits than senior analysts with lead analyst responsibilities.

Analysts belonging to specialist teams have similar titles to those held by credit analysts (e.g. Analyst or Vice President-Senior Analyst) and work with credit analysts in rating groups.

Each rating group has one or more credit officers, who oversee rating quality for the group, or a region or industry within the group. These senior employees (typically holding titles at the level of Senior Vice President or Team Managing Director) ensure consistent application of MIS's rating methodologies and policies within and across rating groups, implement procedures for monitoring credit ratings and support the development and implementation of new methodologies and analytical initiatives. Credit officers who perform this credit policy function full time are called Chief Credit Officers. Other credit officers (e.g. regional or industry credit officers) perform this credit policy function on a part-time basis in combination with other responsibilities.

MIS does not have analysts who are designated as "committee analysts". The composition of our rating committees and the number of participants in a rating committee depend on the specific circumstances of the credit under consideration and, as appropriate, may include analysts from different rating groups, analysts with different levels of seniority and analysts with specialist expertise. Our rating committee process is described in detail in the MIS Report.[21]

c. Historical data for exhibit 8 (information on number of analysts / supervisors) covering the 1997-2006 period split by:

I. the staff levels identified in point (b) above.

II. Worldwide, EU and US based.

[20] Typically, MIS assigns responsibility for analysing an issuer or obligation to two analysts. The primary analyst typically is referred to as the "lead analyst" and the secondary analyst typically is referred to as the "back-up analyst". Please refer to our responses to Questions 14 and 18 for a discussion of how monitoring is conducted in our Structured Finance rating department, where responsibility for monitoring many asset classes is allocated to dedicated teams of surveillance analysts.

[21] See section II, Part A.4.b (pp. 8-9).

Response: Please refer to Annex 2, for which we have requested confidential treatment.

d. What are the minimal educational and professional requirements for the different levels of employees (as defined in b) within the analytical staff, and have these requirements varied over the past 10 years? If they varied, how did they vary?

Response: MIS's typical requirements when hiring analytical staff are set out below, but MIS does not have minimum requirements. MIS may hire or promote personnel based on other qualifications that MIS deems acceptable.

Junior analysts: A primary degree typically is required, preferably in finance, economics, accounting or computer science. In addition, a master's or other advanced degree in finance, economics or a related field, or a professional qualification such as Chartered Financial Analyst or Certified Public Accountant, is preferred. At least two years of prior work experience in areas such as financial or investment analysis typically is required, along with exposure to areas such as research, economics, statistics and quantitative modelling.

Senior analysts: A master's or other advanced degree in finance, economics, accounting, law or a related field typically is required and a professional qualification such as Chartered Financial Analyst or Certified Public Accountant is preferred. At least four years of prior work experience in financial or investment analysis, including credit analysis and familiarity with the relevant business sector, typically is required.

Managers: A master's or other advanced degree in finance, economics, accounting or a related field typically is required, and a professional qualification such as Chartered Financial Analyst or Certified Public Accountant is preferred. At least ten years (and frequently as much as 15 years) of prior work experience in credit analysis, portfolio management or other relevant capital markets experience typically is required, including demonstrated ability in the skills needed to lead senior credit analysts.

Credit officers: Some credit officers hold the title of Team Managing Director or Group Managing Director and, accordingly, the typical minimum requirements for these credit officers are those applicable to managers. Other credit officers are senior analysts and will have experience and qualifications that significantly exceeds the typical minimum requirements for senior analysts noted above.

e. The typical minimum number of years of experience according to levels of employees as defined in (b). Has this number evolved over the past 10 years? If so, how?

Response: Our response to Question 10.d sets out our typical experience requirements for analytical staff. We do not have minimum requirements. During the past ten years, our typical experience requirements have not changed significantly across most of our rating teams. Across many areas of our practice, however, we have observed that, as credit markets have evolved, experienced analysts joining MIS have brought with them a wider and/or deeper set of relevant skills and more relevant industry (and asset class) knowledge than in the past. For example, we have hired more analysts with master's degrees in financial engineering or statistics, substantial experience in modelling and/or substantial legal experience relating to structured finance transactions.

In our Structured Finance department, we have in more recent years hired more junior analysts with limited relevant work experience but strong academic qualifications and then invested significant resources in training them and providing them with practical experience. Please refer to our response to Question 13, where we describe the systems and processes to ensure that this practice does not compromise the quality of our analysis.

11. Please provide us with figures on the annual turnover of employees over the period 1997-2006, split per level (as defined in (10.b)), covering I) SF ratings and II) traditional ratings.

Response: Please refer to Annex 3, for which we have requested confidential treatment.

12. What are the risks presented by staff turnover to your ability to function effectively as a provider of accurate ratings and what steps do you take to mitigate these risks? Are these successful?

Response: Staff turnover presents both opportunities and risks for a credit rating agency, as it does for any other business that operates in the financial markets and relies upon the intellectual capital of its staff. The nature and extent of the opportunities and risks depend upon various factors. For example, internal turnover (i.e. an employee changing positions within an organisation) is often a net positive for the organisation, since the employee's new team can benefit from his or her experience, contacts and skills acquired with the old team. Also, the organisation retains the knowledge that the transferring employee acquired in his or her prior position. By contrast, external turnover of highly skilled professionals can present a greater risk, principally in terms of the potential loss of intellectual assets and also in terms of direct turnover costs. The magnitude of the potential loss is greater if the departing employee is a highly valued, senior credit professional or manager. (On the other hand, the departure of a relatively less qualified and effective employee and recruitment of better qualified, highly respected and more effective new employee can be a net positive.) In addition, the direct and indirect costs of turnover will vary depending on such factors as the local job market and the relative scarcity of similarly skilled professionals.

MIS mitigates the risks associated with turnover among its skilled professionals in several ways. First and foremost, MIS employs systems and practices that are intended to reduce reliance upon any single individual's contribution to the credit rating process, ensure consistent and efficient decision-making and preserve institutional memory. The cornerstones are MIS's rating committee process, our Credit Policy function, our adherence to published rating methodologies and our training programmes.

One important function of the rating committee process is to foster consistency and efficiency across MIS while ensuring that the integrity of the rating process is maintained. Rating committees bring together senior analysts from different rating groups and with varying perspectives and expertise relevant to the issuer or obligation being considered, as well as junior analysts who benefit from the learning opportunity and are encouraged to express fresh perspectives. Accordingly, the potential loss of intellectual assets associated with the departure of an individual analyst is mitigated, since the rating committee process ensures that a number of individuals will be familiar with the issuer or obligation, the relevant industry and applicable rating methodologies. New analysts (at junior or senior levels) can be brought up the learning curve quickly through opportunities to participate in rating committees with MIS staff who are familiar with the issuer, industry and relevant methodologies. MIS also benefits from turnover in the sense that new analysts are encouraged to express fresh perspectives in rating committees in an environment where, ultimately, decisions about ratings are made by the committee as a whole (on a majority vote basis) and never by a single individual.

Likewise, MIS's usual practice of making two analysts, a lead analyst and a back-up analyst, responsible for carrying out credit analysis of particular issuers and obligations, reduces the risks associated with the potential departure of a particular individual.[22]

MIS's independent, Credit Policy function also helps to mitigate the potential risks associated with external turnover among professional staff by exercising informed oversight over the process for generating rating opinions as well as the development and vetting of rating methodologies. The overall Credit Policy structure is overseen by MIS's Chief Credit Officer, who is directly accountable to the President of MIS and reports quarterly to the Chief Executive Officer and Chairman of MCO and the MCO Board of Directors. The Credit Policy structure has four components:

> The Chief Credit Officer presides over the Credit Policy Committee (the "**CPC**"), which comprises senior managers representing our principal rating groups worldwide. The CPC sets high-level rating policies for each of the rating groups, monitors appropriateness and completeness of rating methodologies and approves any significant changes to MIS's rating methodologies and procedures. The CPC has operational arms in the form of rating group committees, which oversee analytics and procedural issues in each of MIS's major rating groups. There are also topic-specific rating committees, which focus on providing methodological guidance on topics that cut across MIS's franchises and/or jurisdictions.
>
> The Credit Policy and Research Team, which reports directly to the Chief Credit Officer and is independent of the rating groups, assesses the performance of ratings (e.g. by conducting and publishing default studies).
>
> A matrix of full-time chief credit officers in the rating groups, as well as industry and regional credit officers, work with the rating groups, each other, credit committees, the CPC and the Chief Credit Officer to ensure that rating methodologies and policies are implemented consistently across the organisation.
>
> MIS has an extensive professional development and training programme that has been designed to enhance the quality of MIS's rating analysis and analysts' understanding of relevant policies and procedures. MIS analysts are required to meet annual, continuing education requirements by completing MIS's courses or approved, external courses. Oversight of MIS's professional development group lies with the Credit Policy and Research Team, which is responsible for regularly evaluating the professional development group and reporting to MIS's CEO on its effectiveness.

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[22] Please refer to our responses to Questions 14 and 18 for a discussion of how monitoring is conducted in our Structured Finance rating department, where responsibility for monitoring many asset classes is allocated to dedicated teams of surveillance analysts.

MIS also uses human resource mechanisms to assist with our staff retention goals. These mechanisms include, among other things, the following:

a long-term equity compensation plan with a multi-year vesting schedule;

depending on the requirements of the jurisdiction where an employee works, retirement income plans that may vest only after an employee has completed several years of service;

an educational assistance programme whereby MCO covers the cost of tuition, books and registration fees where the relevant criteria for the employee and proposed programme are met;

a workplace flexibility policy enabling employees, in appropriate circumstances, to enter into flexible work arrangements including tele-commuting, part-time work and/or job sharing;

a range of personal benefits, including a medical plan, dental plan, insurance programmes and, in some jurisdictions, company-paid access to a health advocacy service, a "life care" service and a financial planning service, all of which help employees deal with issues and concerns arising in their personal lives, thereby improving quality of life; and

a comprehensive community involvement programme, which recognises, encourages and supports employees' volunteer activities, thereby helping employees develop their skills and interests and fostering employee loyalty as well as providing benefits to the communities in which MCO operates and its employees live.

13. Has it become harder to fill vacancies in structured finance teams over the last 5 years? If yes, what has been done to ensure you continue to have sufficient resource and to ensure that this does not affect the quality of your ratings?

Response: Vacancies arise either when employees leave the Structured Finance department (turnover) or when new positions are created. Until recently, there was keen competition within the industry to recruit and retain experienced credit professionals with structured finance expertise. There is some correlation between high activity in structured finance markets and demand for credit analysts in this field. Overall, we believe that turnover levels within the Structured Finance department have been within manageable and expected ranges.

MIS has had success in recruiting experienced and highly qualified senior staff to increase the number of senior analysts and managers in Structured Finance. To fill some junior analyst positions, our Structured Finance department has in recent years recruited some staff with limited experience but strong academic qualifications and then invested significant resources in training them. Junior analysts receive extensive initial and ongoing formal training as well as on-the-job training under a lead analyst's supervision and participate regularly in rating committees (but without voting rights). More experienced analysts directly supervise all of the analytical work carried out by less experienced junior analysts, who are assigned tasks of limited complexity until they have completed the relevant training and proven themselves capable of handling more complex, analytical tasks. Analysts do not serve as lead analysts until MIS is satisfied that they have the necessary skills, experience and knowledge to fulfil such a role. Accordingly, we believe that the potential risks of recruiting some junior analysts with limited, relevant work experience at the outset of their careers with MIS are mitigated by our training programmes, supervisory practices, the rating committee process, the use of published methodologies and our Credit Policy function.

14. Typically, what is the composition of a monitoring/rating team in terms of the job profiles and job levels and does this differ from teams that monitor/rate corporate bonds?

Response: We believe that the organisation and composition of MIS's rating groups and analytical teams are key components of our efforts to produce globally consistent credit ratings. We refer you to page 5 of the MIS Report, available on our website, for a fuller description of how MIS is organised.

In both the fundamental and structured finance rating sectors, analytical teams responsible for conducting analysis for a particular issuer or debt security typically consist of a managing director, a lead analyst and a back-up analyst, as well as specialists (where appropriate) and junior analysts. All significant telephone calls, meetings and on-site visits would normally be attended by both the lead analyst, the back-up analyst and, where possible, the managing director. As we explain in more detail in responses to Questions 12, 23 and 24, all MIS ratings are assigned by rating committees.

Except for credit ratings that clearly indicate that they do not entail ongoing monitoring, once a credit rating is published, MIS will monitor it on an ongoing basis. In the rating groups that make up our Fundamental department[23], monitoring is conducted continuously by the same analytical team that is responsible for the initial rating. This team is supported by institutional monitoring processes overseen by MIS credit officers. Please see our response to Question 18 for a more detailed description of the monitoring process.

In our Structured Finance department, monitoring of many asset classes[24] is performed by dedicated teams of monitoring analysts. For other asset classes (e.g. esoteric asset classes), the analytical team that is responsible for the initial rating is responsible for monitoring the transaction. For rating groups that use dedicated teams of surveillance analysts, the team usually consists of junior and senior credit analysts, statistical analysts and programmers (who develop data queries used by credit analysts and improve the databases). These staff report to a Team Managing Director. In addition, as discussed in more detail in response to Question 17, MIS leverages its human resources allocated to the monitoring function in Structured Finance (and in other rating groups) by outsourcing some basic data processing and software development relevant to the monitoring process.

15. Please provide us with information on the average number of deals and average number of transactions under surveillance per lead analyst by type of SF products, in the following table format:

Response: The table below contains global data. Our systems only track those transactions where MIS issues a final rating. The second column in the table proposed by

23 MIS's Fundamental department consists of three divisions: (1) corporate finance; (2) financial institutions; and (3) public, project and infrastructure finance.

24 For example, we have dedicated monitoring teams that cover various RMBS in many regions, including the U.S., EMEA and Asia. We also have dedicated monitoring teams for CDOs in the U.S. and EMEA.

CESR called for information regarding the "average number of transactions under surveillance per lead analyst in 2006" for different asset classes. The information requested is not representative of an MIS surveillance analyst's typical workload. This is because, for many asset classes, individual members of MIS's monitoring teams are not allocated a specific portfolio of credits to monitor. Instead, the monitoring function generally operates as follows. First, MIS maintains (and is continuing to develop) its own independent database of performance data, which is updated by the performance information received from servicers and trustees. Using MIS's proprietary software applications, the entire universe of outstanding ratings is screened automatically[25] to identify "outliers" (i.e. securities where transaction performance indicates that the current rating may not accurately reflect the current credit risk of the security). Once an outlier has been identified, it is allocated to a member of the monitoring team for review. Members of the monitoring teams also are given assignments to review particular vintages of securities, such as those relating to a particular year or originator, even where the set of ratings does not reveal any outliers.

Consequently, MIS believes that the following figures would be more representative of a surveillance analyst's workload:

- the average number of outliers analysed by each surveillance analyst; or
- the number of rating upgrades and downgrades taken by MIS in respect of a particular asset class, relative to the number of surveillance analysts in that sector.[26]

While our systems do not readily track at a global level how many outliers are analysed in each asset class in a given year, they do track how many transactions are upgraded or downgraded. Accordingly, we have provided the average number of transactions that were upgraded or downgraded per rating analyst in 2006 in the second column of the table below.

Type of product	**Average number of transactions per lead analyst in 2006 (primary rating) ***	**Average number of transactions that were upgraded/downgraded per monitoring analyst in 2006.**
RMBS	18.5	19.5
Asset-backed commercial paper ("**ABCP**")	10.6	0
Asset-backed securities ("**ABS**")	10.7	20.1
Commercial mortgage-backed securities ("**CMBS**")	4.7	17.6
CDOs (excluding structured notes)	15.7	20.3
Covered bonds	3.0	0
Structured investment vehicles ("**SIVs**")	6.4	0.14

* Includes only transactions that resulted in a final rating since this is what our systems track

Another factor that is relevant to the assessment of the surveillance analysts' workload is MIS's ability to re-assign analysts who are not working at full capacity to areas where there is

[25] Typically, screening would take place either quarterly or monthly depending on the timetable for receipt of performance data provided for in the securities' terms and conditions.

[26] A figure based on the number of upgrades and downgrades, divided by the number of relevant analysts for the relevant sector, slightly underestimates the average number of transactions reviewed by surveillance analysts. This is because some transactions that are reviewed by a surveillance analyst will not, ultimately, be upgraded or downgraded (since rating actions are taken by a rating committee and not by any individual analyst).

greater demand for their services. For example, in recent months a number of analysts who had been working on initial ratings for certain asset classes have been devoting a significant proportion of their time to monitoring. Accordingly, if the number of outliers identified by MIS's proprietary systems increases substantially, MIS has the capacity to re-assign analysts to monitoring functions to handle the increased workload.

16. What are the total annual wage costs in structured finance rating over the period 1997-2006?

Response: Please refer to Annex 4, for which we have requested confidential treatment.

17. Do you outsource part of the rating/surveillance process (e.g. data gathering, processing, modelling, etc.)? If yes :

a. Please describe in which part(s) of the rating/surveillance process you make use of outsourcing and to what extent.

Response: MIS outsources some aspects of certain tasks, principally basic data processing and software development. In relation to our Structured Finance department, the outsourced work includes processing trustee and servicer report data for CDOs and carrying out some very limited software programming. In the EMEA region, MIS also outsources the processing of data received from trustees and servicers in relation to RMBS and ABS transactions. In relation to our Fundamental department, the outsourced work principally consists of helping to create software programmes and processing information, such as financial statements and filings, into a format that MIS analysts can use as part of their analysis. As we discuss in more detail in our response to Question 17.b, MIS does not outsource any substantive aspects of the credit analytical function.[27]

b. What are the risks implied by such outsourcing and how do you tackle these?

Response: The potential risks associated with MIS's decision to outsource certain tasks include risks associated with the maintenance of confidential information and preserving data security, compliance with MIS's policies, procedures and obligations and risks associated the quality of the outsourced work. MIS addresses these potential risks by, among other things:

ensuring that we choose appropriate suppliers;
including appropriate obligations and protections in our contractual relationships with the firms to which we outsource tasks;
maintaining rights to review and audit the supplier to verify the quality of work done as well as compliance with the contract, confidentiality and data security standards and MIS policies and procedures;
providing for appropriate oversight by senior MIS staff of decisions regarding outsourcing and of outsourcing practices themselves; and
limiting the scope of the tasks that are outsourced.

MIS has designated personnel to be responsible for actively managing and supervising our outsourcing relationships and has established a senior-level outsourcing committee, which

[27] MIS has entered into relationships around the world with rating agency affiliates, which participate in MIS's rating process as appropriate in accordance with the terms of our affiliation with them.

oversees the outsourcing process. As part of our supervisory practices, MIS manages the means by which information is downloaded or received by the entity and satisfies itself that there are suitable internal control and checking mechanisms in place at the entity. MIS also supervises the quality of the information that is received from the entities to which we outsource tasks. For example, MIS analysts either review the file or work product or audit a sample of the work to check the data. In the latter case, MIS notes any errors resulting from the audit and arranges for them to be corrected. Where our reviews and audits indicate an accuracy rate of nearly 100%, we continue to audit smaller samples of the work product.

MIS does not outsource any substantive aspects of the credit analytical function. For example, MIS does not outsource rating analysis, research, the development of rating methodologies or monitoring of rated securities (including, e.g. responsibility for identifying transactions for review).

c. Do you consider the (economic) gains of outsourcing to exceed the risks? Please motivate.

Response: The outsourcing process adds value by enabling MIS analysts to focus on the substantive aspects of rating analysis and research while ensuring that basic data programming, data processing and software development needs are met. MIS believes that the staff of the firms to which we outsource tasks (e.g. data processing and software development) have sufficient skill and expertise to perform these functions effectively and efficiently, subject to the controls described in our response to Question 17.b, at a lower labour cost than if MIS's analysts performed these functions themselves. This division of labour enables MIS's analysts to focus their attention on substantive credit analysis, thereby leveraging the specialised knowledge and experience of our credit analysts and improving the quality of MIS's rating analysis.

Monitoring of transactions

18. What drives the frequency of rating review for structured finance? Why is this frequency appropriate? Please outline the process that would lead to a rating being taken to review committee.

Response: MIS's monitoring process in our Structured Finance department is a three-pronged process that commences upon the publication of our rating. First, as indicated in our response to Question 15, the surveillance team receives and processes data from regular servicer and/or trustee reports. Second, the surveillance analyst assesses the data and, if necessary, a rating analysis is conducted, often in conjunction with the lead analyst involved in the initial rating action for the transaction. Third, where necessary, the surveillance analyst (or his or her manager) convenes a rating committee to vote on and authorise the publication of a rating action.[28] (For asset classes where it is more appropriate for the lead analyst to be responsible for monitoring, the lead analyst would be responsible for ensuring the performance of the functions attributed to the surveillance analyst in the description set out above.) MIS has published a number of reports describing our monitoring approaches for specific structured finance asset classes.[29]

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28 Please refer to our responses to Questions 23 and 24 for a discussion of the rating committee process.

29 See e.g. *Surveillance Process for Moody's-Rated RMBS and ABS*, March 2007 (Special Report, Document SF95523); *Moody's Approach: The CDO Monitoring Process,* September 2002 (Rating Methodology, Document SF16450); *Surveillance Process for Moody's-Rated ABS and RMBS in EMEA,* August 2007

The frequency of MIS's monitoring process in Structured Finance typically is determined by the scheduled payment dates for the rated securities for two reasons.[30] First, the receipt of transaction performance data from the trustee or the servicer is driven by these payment dates. Second, until the payment date, it will not be clear whether there has been any shortfall in payment and thus whether a rating adjustment needs to be considered. Consequently, MIS's structured finance monitoring process typically occurs either monthly or quarterly, depending on the frequency with which the trustees and servicers generate and provide data to MIS. If MIS receives performance data or other information between scheduled payment dates that indicate material deterioration or improvement in the creditworthiness of the securities, we would take appropriate action at that time. The transaction performance data is further informed by MIS's analysis of macroeconomic conditions.

MIS incorporates qualitative as well as quantitative analysis into our monitoring process. Quantitative analysis involves using tools such as models that enable surveillance staff to compare actual asset performance against the performance expected at the time of the initial rating assignment. MIS judiciously reviews each deal, analysing transaction-specific information as it becomes available rather than relying exclusively on broader market data or speculation.

In terms of process, MIS's best practice guidelines for rating committees specify who is responsible for convening a rating committee and which analysts or managers can require that a rating committee be convened. For existing ratings in our Structured Finance department, the analyst responsible for monitoring the transaction or the analyst's manager is responsible for convening a rating committee. Any team member, including a non-voting member, can request that a rating committee be convened. A rating committee for an existing transaction must be convened if requested by any of the new transaction lead analyst, a Senior Vice President who has been authorised to chair rating committees, a credit officer who has been authorised to chair rating committees, the Team Managing Director, Group Managing Director, Senior Managing Director, the Chief Credit Officer for the Structured Finance department or MIS's Chief Credit Officer.

19. Would regular reviews and announcements on the appropriateness of structured finance ratings - possibly based on some contractual deadlines (i.e. on a regular (quarterly/semi-annual basis) - help in preventing mass downgrades, improve the appropriateness of existing ratings? If not, why?

Response: MIS does not believe that announcements about the appropriateness of structured finance ratings according to a prescribed timetable or schedule would prevent mass downgrades or improve the appropriateness of existing ratings for the following reasons. First, structured finance securities are inherently more likely to exhibit correlated rating changes than corporate finance securities. As we explain in more detail in our response to Question 38, rating changes tend to be correlated among debt instruments that have similar fundamental drivers of credit risk. Structured securities, by design, eliminate much of the

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(Special Report, Document SF105658); and *Moody's Approach to Monitoring CMBS Ratings in Japan,* October 2005 (Special Report, Document SF62932).

[30] The scheduled payment dates are defined by the securities' terms and conditions.

potential, idiosyncratic risk that drives issuer-specific rating changes.[31] Consequently, when broad economic factors that drive collateral performance deviate sharply from expectations, a large number of structured securities within the same sector and of the same vintage are likely to be similarly affected, either through upgrades or downgrades. Accordingly, it is difficult to eradicate the possibility of mass downgrades for structured securities.

Second, ratings are already monitored on an ongoing basis and MIS changes our ratings when our opinion about the fundamental creditworthiness of the obligation changes. A requirement to announce on a quarterly or semi-annual basis that our rating had not changed would saturate the market with redundant and potentially confusing or obfuscating information. Arbitrary review dates could inappropriately focus investor and issuer attention on those dates, rather than on credit-relevant events and inadvertently conceal significant rating actions. Paradoxically, publishing more information could reduce the usefulness of the rating and impair transparency.

20. What changes have you made in terms of the surveillance of ratings since the widespread RMBS and CDO downgrades earlier this year?

Response: MIS is continuing the trends toward establishing separate monitoring teams in Structured Finance and expanding the amount of resources allocated to these teams. These trends began in 2004, well before the RMBS and CDO downgrades earlier this year. Likewise, MIS has been implementing a number of automated processes and systems, including proprietary applications, to routinely sift through entire databases of transactions, updating performance statistics and flagging rating outliers. The rollout of these initiatives also began before the RMBS and CDO downgrades.[32] In addition to the pre-existing trend toward allocating more resources to monitoring activities[33], MIS recently has been allocating more resources to the function of communicating our monitoring activities to the market.

21. How is the appropriate portfolio size determined for structured finance monitoring analysts? Are there any internal procedures which dictate how many transactions a monitoring analyst should be responsible for?

Response: Please see our response to Question 15 above.

22. Are the costs of monitoring structured finance transactions fully covered by the fees charged specifically for monitoring when the rating agreement is initially made? What are the main incentives for maintaining effective monitoring of ratings?

Response: Yes. MIS's structured finance monitoring fees for most asset classes are charged on a per transaction basis and are intended to fully cover the monitoring costs for the relevant transaction. Fees for ongoing monitoring generally are fixed amounts, payable either at the time of the initial rating (and recognised for accounting purposes over the expected life

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[31] Applying modern portfolio theory, many investors seek to eliminate as much potential, idiosyncratic risk from their portfolio as possible. This is one of the principal reasons why they purchase structured finance securities.

[32] See e.g. our discussion, *Surveillance Process for Moody's-Rated ABS and RMBS in EMEA*, August 2007 (Special Report, SF105658).

[33] In addition, as noted in our response to Question 15, in recent months a number of analysts who had been working on initial ratings for certain asset classes have been devoting a significant proportion of their time to monitoring.

of the instrument) or on an annual basis. While for a few asset classes in some regions, the fee schedules do not expressly provide for a separately identified, monitoring fee, MIS nevertheless has factored the cost of monitoring the transaction over its life into the rating fee. Accordingly, the costs of monitoring structured finance transactions are fully covered by the portion of the fees that either is specified in the fee schedule or that MIS attributes for internal purposes to monitoring costs when it determines the appropriate rating fee for the transaction.

Fundamentally, issuers seek ratings from rating agencies because investors demand ratings before they will purchase the issuer's debt. Investors will only demand those ratings that they deem credible. Therefore, the value of our ratings business depends on our credibility with investors. Our business need to maintain investor confidence in the quality and integrity of ratings is the principal incentive for conducting effective monitoring of our ratings.

23. How is committee time dedicated to rating reviews versus that dedicated to new ratings determined, particularly for structured finance? Are there clear internal procedures on how committee time is prioritised?

Response: MIS does not have standing rating committees or analysts designated as "committee analysts". Rating committees are convened whenever there is a need to deliberate upon a potential rating action and, as discussed in more detail in our response to Question 24, the composition of rating committees varies.

MIS's *Core Principles for the Conduct of Rating Committees* (the "**Core Principles**")[34] state that the rating committee process is designed to foster a free exchange of views among participants with full consideration of dissenting or controversial views. The rating committee focuses on the specific issuer or obligation being rated and is not formulaic. Accordingly, the duration of a rating committee is a function of the complexity and novelty of the issues to be considered, as well as the amount of information that the rating committee needs to evaluate and discuss. Discussion in a rating committee continues as long as necessary to ensure that the relevant issues (including differences of opinion) are thoroughly discussed, assumptions are tested and a fully reasoned opinion is articulated that is supported by the rating committee (by majority vote). In other words, regardless of whether a rating committee is considering a new rating or an existing rating, the rating committee takes as long as it needs to take to reach a conclusion.

24. Are the committee members reviewing a rating the same as those who approved the initial rating? Are there any internal procedures dictating the composition of the review committee?

Response: The MIS Code, MIS's publicly available Core Principles and internal policies that provide specific guidance on best practices for the conduct of rating committees in different rating groups collectively address the composition of rating committees. Section 1.8 of the MIS Code provides that MIS will organise its rating committees to promote continuity and avoid bias in the rating process. The Core Principles, which apply to all rating committees and address the broad themes covered in more specific guidance, emphasise that the composition of rating committees should be based on expertise and diversity of opinion.

In practice, the composition of a particular rating committee varies, depending on factors such as the nature and complexity of the credit rating being assigned, the novelty of issues under

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[34] April 2006 (Document 97097), available on www.moodys.com.

consideration and the need to involve specialists (e.g. from our accounting, corporate governance or risk assessment teams) or those with geographic sector expertise. As emphasised in the Core Principles, facilitating the expression of diverse opinions and testing underlying assumptions is also relevant in selecting participants for a rating committee. Finally, while including a sufficient number of senior analysts in a rating committee is essential, junior analysts are invited to participate for training purposes and to encourage the expression of fresh perspectives.

Consequently, a rating committee that deliberates upon an existing rating likely will involve a number of the same members who participated in the rating committee that decided the initial rating. The amount of time that passes between rating committees is also likely to affect to some extent the composition of a rating committee. For example, if the individual who was the lead analyst for the issuer or transaction when the rating was initially decided is still the lead analyst when the rating is reviewed, he or she is expected to serve as the lead analyst in the rating committee unless he or she is unavailable (in which case, the back-up analyst will fulfil the role of the lead analyst).

The involvement of specific individuals in a rating committee is less important than the impact of MIS rating committee policies and practices[35] designed to encourage the expression of diverse opinions, test underlying assumptions, maintain objectivity and ensure consistent decision-making from issuer to issuer in accordance with MIS's methodologies. MIS's rating committee practices are also intended to prevent decision-making in rating committees from being dominated by a single individual, while ensuring that experienced and knowledgeable analysts and managers make a substantial contribution to the analytical process.

25. Is there a team of macroeconomic analysts within your firm responsible for systematically analyzing macro data coming in and building macroeconomic forecasts on which analysts can rely for their modelling/monitoring of ratings? If not, would this be useful?

Response: MCO has a capital markets economics team whose members are based in New York and London. They provide economic data and commentary focused on the credit markets. The team comments on the corporate credit cycle and the impact of economic news on corporate balance sheets, bond yields and spreads, and issuance of securities. This team's outputs are made available to MIS's rating analysts for their analysis and modelling. In addition, as described in more detail in our response to Question 5, MIS has initiated a *Global Financial Risks Perspectives* series to communicate our views on broad risks to the financial stability of global capital markets.

26. Please provide us with a breakdown of revenues from SF ratings for initial rating/surveillance. How is the relative size of each of these parts of the fee decided?

Response: As described in more detail in our response to Question 22, for a few asset classes in some regions, MIS incorporates the cost of monitoring a transaction when the initial rating fee is determined but does not specify a separate monitoring fee in the fee schedule. Structured finance monitoring fees vary by asset class, reflecting the complexity of

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[35] These policies and practices are summarised in the MIS Report at pp. 8-9.

monitoring a transaction until its maturity or earlier rating withdrawal.[36] A further consideration in determining monitoring fees is the ongoing work load; aspects of the initial rating analysis involving substantial analytical input (such as a review of the legal documentation) may not be subject to significant change thereafter. Accordingly, the proportion of total revenues represented by monitoring fees varies among asset classes. It also can vary from one financial period to another.[37]

Our systems do not track the data in the format CESR has requested and, consequently, we cannot provide a precise answer as to the exact proportion of revenues from structured finance ratings that are associated with initial ratings versus monitoring. In order to respond to CESR's query, we have estimated that, excluding transactions where monitoring fees are not listed separately in the fee schedule, approximately 16.6% of structured finance revenues in 2007 would be attributable to monitoring fees.[38] We wish to emphasise that this figure is an estimate based on readily available data for one financial quarter. Accordingly, this figure may not accurately represent the typical breakdown between initial rating fees and monitoring fees.[39]

<u>Methodology changes</u>

27. What prompts a review of rating methodology? Is there a central team that reviews methodologies or is it dependant on individual business lines self-evaluating their models?

Response: Reviews of rating methodologies usually are initiated either by the rating team that is responsible for a particular sector and the associated methodology or by a person or group associated with MIS's Credit Policy function. In the ordinary course of business, the rating team with responsibility for a particular sector periodically initiates a review and update of the existing methodology, e.g. to reflect shifting industry trends and/or methodological evolution. For example, many reviews of methodologies have taken place in recent years to enhance the level of transparency with respect to our rating process. The rating department's chief credit officer, who is responsible for the integrity and effectiveness of ratings practice within the department, may also recommend that the rating team review the rating methodology. Another source of information that could trigger a review of a methodology is ratings performance in a particular sector that is consistently better or worse than the average

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[36] In general terms, asset classes that require greater analytical input as the structure evolves over the life of the transaction are subject to higher monitoring fees. For example, CMBS transactions typically are collateralised by a limited number of assets that perform in an idiosyncratic manner. Furthermore, since there are relatively few assets in the pool, the performance of any one asset could materially affect the overall performance of the security. Monitoring such transactions requires more analytical input. By contrast, RMBS transactions typically are collateralised by large pools of homogeneous assets, any of whose performance is unlikely to have a material impact on the overall performance of the security.

[37] For example, if very few new transactions are rated in a given quarter, then the proportion of revenues associated with monitoring fees in that quarter is likely to be higher than in a quarter where a larger number of new transactions receive ratings and the total population of existing ratings subject to monitoring is not significantly different from the quarter where few new transactions were rated.

[38] Our projection is based on structured finance revenue data for the first quarter of 2007. We assumed that the proportion of total structured finance rating revenues classified as "initial rating fees" and "monitoring fees" would not change throughout 2007.

[39] For example, there are some asset classes where many annual monitoring fees typically are paid in the fourth quarter of the financial year. Accordingly, a projection using data only from the first quarter of the financial year can underestimate the proportion of monitoring fees paid annually for that asset class.

that is published in the default studies carried out by MIS's Credit Policy Research group. MIS's Chief Credit Officer, the CPC or the standing rating committee for the relevant business line (e.g. the Structured Finance Rating Committee) could also recommend that a methodology be reviewed.[40]

Regardless of who initiates a review of a rating methodology, the review process will involve the rating team (including the Team Managing Director), the rating department's chief credit officer, the relevant credit committee for the rating group, any appropriate topic-specific credit committee (e.g. the Risk Transference and Securitisation Committee) and the CPC. Changes to a methodology affecting a large number of corporate ratings or affecting more than one major business sector are approved by the Fundamental Credit Committee as well as the CPC.

28. Have you made any changes to how you evaluate the appropriateness of your methodologies on an on-going basis in light of the RMBS and CDO downgrades of earlier this year?

Response: With respect to our methodologies for RMBS and CDOs in particular, we have made some changes to our methodologies and published a Request for Comment on proposed enhancements to non-prime RMBS securitisation transactions.[41]

With respect to our Credit Policy function in general, as indicated in our responses to earlier questions, MIS believes it has a robust, independent Credit Policy function that exercises informed oversight over the development and vetting of rating methodologies, as well as the process for generating rating opinions. Nevertheless, we continuously seek to strengthen our Credit Policy function and thereby enhance the quality and integrity of our methodologies and rating processes. Over the past several years, on our own initiative and in the light of evolving expectations that have flowed from initiatives such as the IOSCO Code, the CESR Expert Group's annual review of credit rating agencies and the recognition process for External Credit Assessment Institutions under Basel II, as well as developments in credit markets such as those we have experienced in 2007, we have re-evaluated our existing structures, policies and practices. Accordingly, while MIS believes that the recent developments in structured finance credit markets do not call for a fundamental change in the way we evaluate the appropriateness of our methodologies on an ongoing basis, we recognise that there is always room for further improvement. For example, MIS's Credit Policy Research team, which is independent of the rating groups, is now conducting periodic, independent reviews of data, methodologies and models used in the rating process to identify areas in need of update or further analytical investment.

29. When the methodology for a type of structured finance product (example being US sub-prime mortgage backed securities) is amended:

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[40] While changes to methodologies usually are initiated either by the relevant rating group or by a person or group associated with the Credit Policy function, other groups could also initiate a change. For example, someone in another rating group who believes that a methodology should be changed could bring these views to the attention of either the relevant chief credit officer for the rating group that ordinarily works with the methodology in question or the Chief Credit Officer.

[41] *Moody's Proposes Enhancements to Non-Prime RMBS Securitization*, September 2007 (Document SF110639).

a. **Do you automatically review all existing ratings against the new methodology and take rating action based on this review? If not, what is the rationale behind this?**

b. **How is the scope of the application of the change of methodology determined? In other words on what basis does your firm decide whether or not to apply a change to existing ratings or just to new issuances?**

c. **Please explain in detail how is the timing of rating action determined across all affected ratings?**

Response: As we discussed in our response to Question 4, for many structured finance asset classes, post-rating performance of the security is the most relevant consideration. For such asset classes, transactions that are not performing well are reviewed immediately against the new methodology. By contrast, transactions that are performing well and amortising quickly are less likely to be reviewed against the new methodology (although their ongoing performance is monitored).

By way of another example, it can be foreseen in some circumstances that the changes to a methodology will affect only a relatively small proportion of existing ratings. One such example would be ratings that lie close to a boundary between two different rating levels and that have performance metrics that would be sensitive to a change in a relatively heavily weighted rating factor that has been amended. In such circumstances, these "vulnerable" ratings may be reviewed immediately, while other existing ratings will be subject to ongoing monitoring but not a transaction-specific review.

In sequencing reviews of existing structured finance ratings that are potentially affected by changes to a methodology, MIS will consider whether or not the collateral is homogeneous. If the collateral is homogeneous, then it is feasible to review all rated transactions (e.g. in a particular vintage) simultaneously. For transactions where there is significant variability in the collateral, MIS believes it is preferable to review the most vulnerable transactions first.

30. Does your firm at any time make any overall review of the changes to methodologies made, for instance during one year, and their impact on ratings to assess trends for instance? Would this be made public?

Response: MIS does not conduct time-tabled and scheduled, firm-wide reviews of all changes that have been made to all methodologies and their impact on ratings. Rather, our reviews are based on actual changes in the market or the dynamics of a given sector. In addition, because the universe of issuers and obligations that we rate is both large and diverse, a scheduled review of all sectors may have limited value. By contrast, for some sectors with large, dynamic credit markets where our methodologies are modified more frequently to keep pace with innovation and credit market trends, we have published special reports that summarise changes in methodologies over a specified period of time. For example, in August 2007, we published *US Subprime-Overview of Recent Refinements to Moody's Methodology: July 2007*.[42]

As indicated in our response to Question 12, MIS's Credit Policy function exercises oversight over the development and vetting of new methodologies and changes to methodologies. Our

42 (Document SF104301).

Chief Credit Officer and the chief credit officers for our rating departments work with rating departments and each other to share information about methodological evolution and enhance consistency in methodologies across rating groups. We also refer you to our response to Question 28, where we discuss the role of the Credit Policy function in developing and reviewing methodologies.

MIS produces and publishes a variety of reports that address, on an aggregate basis, matters such as the performance of ratings over time, rating transitions, and default and recovery (or loss rates). MIS also regularly publishes special reports in the form of industry "outlooks" in our Corporate and Financial Institutions rating groups and annual or semi-annual "reviews" in our Structured Finance rating group.[43] In these publications, MIS reviews recent trends and express opinions about the likely impact of these trends on ratings.

31. Is there a risk of originators 'gaming the system' i.e. keeping requested data sets high whilst other valid indicators of asset quality decline? If yes, what mitigation have you put in place to reduce this risk?

Response: Most originators operate in good faith and provide us with the information we have requested, but they are not compelled to give us data, nor do they necessarily maintain all of the potential data that might be useful in judging asset quality. MIS's role in the rating process is not to conduct due diligence to assess the accuracy of the information provided to us, and we cannot completely eliminate the possibility of fraud on the part of the originator.

There are risks of originators gaming the system, with the various "games" being revealed over time – and subsequently evolving into new games as the original games are discovered. MIS does take steps to mitigate the risk of fraud, or gaming, although the risk cannot be eliminated altogether. These steps include regular reviews of our methodologies with a view to creating enhancements in our analysis, sceptically reviewing the information we receive, factoring into our analyses assessments of macroeconomic data that might influence the performance of the underlying transaction, closely monitoring the performance of individual transactions relative to their peers and encouraging greater transparency in structured finance transactions. In addition, MIS rates transactions submitted by diverse originators and also receives information about the investment portfolios and operations of many, different financial institutions and other market participants. Receiving relevant data from multiple sources across the market enhances our ability to review and raise questions about the data we receive from originators, servicers and trustees. If MIS determines that the information we are receiving is not as relevant as originally expected, we begin to ask for additional data. Finally, if we believed that we no longer had sufficient data to support a rating, following a rating committee deliberation, we would withdraw the rating and make the reason for such withdrawal public in a press release.[44]

We believe that improvements in the content and quality of the performance data that is provided to us could assist in reducing the risk of gaming. Please see our response to Question 37 below. Without these measures, we believe that the information asymmetry that exists between credit rating agencies and originators may continue to contribute to the risk of gaming.

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[43] See e.g. *Special Report – 2006 Review and 2007 Outlook: EMEA ABS: Volumes Maintained; SMEs and Emerging Markets to Continue Driving Growth in 2007*, January 2007 (SF90437).

[44] Language similar to the following typically would appear in such a press release: "The rating has been withdrawn because Moody's believes it lacks adequate information to maintain a rating. Please refer to Moody's Withdrawal Policy on moodys.com."

32. Do you feel that your approach to assessment of the quality of underlying asset data is appropriate? Are you considering any changes in this area (specially in light of the recent events in the US sub-prime mortgage market)?

Response: Prior to the recent developments relating to subprime mortgages, market participants and MIS generally were comfortable with the processes we describe below regarding MIS's role in the residential mortgage securitisation market. This may no longer be the case. As noted in our response to Question 28, we have published a Request for Comment on proposed enhancements to non-prime RMBS securitisation. We are also in discussions with investors and issuers about whether or not they see an additional role for rating agencies or other parties in this process.[45]

Credit rating agencies are one of many participants with historically well-defined roles in the residential mortgage securitisation market. In particular, we are users of information and we do not conduct any "due diligence" on these loans as that role is currently conducted by two separate parties at separate times during the loan origination and securitisation process. First, the lender or originator of the loan conducts due diligence when it extends the mortgage loan to the borrower. Second, the investment banker that arranges the structured finance vehicle conducts due diligence, consistent with its role as underwriter. In particular, it is responsible for determining whether the loans in a specific pool meet underwriting standards. Underwriters often hire a due diligence firm to investigate whether or not the underlying loans are in compliance with the originator's stated underwriting criteria, and the originator is generally required to buy back loans that are subsequently revealed to be in violation of its stated criteria. Accounting firms are charged with verifying that the summary information relating to the loan pools matches the underlying characteristics of the pool. In addition, in RMBS transactions the transaction sponsor (or the original lender) provides to the securitisation trust representations and warranties that each underlying mortgage loan meets the requirements of applicable laws.

MIS comes into the residential mortgage securitisation process well after a mortgage loan has been made to a homeowner by a lender and then identified to be sold and pooled into a residential mortgage-backed security by an originator and / or an investment bank. We do not participate in the origination of the loan, we do not receive or review individual loan files for due diligence and we do not structure the security.

Consequently, our role in the structured finance market is fundamentally the same as the role we have played over the last hundred years in the corporate bond market: we provide a public opinion (based on both qualitative and quantitative information) that speaks to one aspect of the securitisation, specifically the credit risk associated with the securities that are issued by securitisation structures. MIS uses information provided by others. Accordingly, while we intend to scrutinise carefully the information we receive, we are not the appropriate entity to audit the data.

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[45] MIS is aware that some market observers and authorities are questioning the degree to which credit rating agencies have participated actively in the securitisation process. If MIS provided additional services in this area, this would enhance our level of participation.

Conflicts of Interest

33. When you rate a structured finance operation do you offer services such as impact assessment and/or models of evaluation or optimisation of the securitization structure? Can you quantify[46] the number of cases where these kinds of services were offered? Would these services be performed by the analyst who rates the final structure?

Response: MIS does not offer discrete services such as impact assessment, optimisation of securitisation structure or evaluations of models in connection with the rating process for a structured finance transaction.[47] As part of the analytical process for rating a structured finance transaction, MIS analysts consider the structure that is presented to them and then, following a rating committee, provide a rating assessment to the issuer or originator. If the structure that was first presented is altered by the originator or issuer, MIS analysts would analyse the new structure and, following a rating committee, provide an updated rating assessment. A single rating fee is charged for the whole rating process; there is no incremental fee if MIS is asked to analyse a revised transaction structure. At no point do MIS analysts offer services other than this core rating service in connection with the rating process for the structured finance transaction. Please refer to our response to Question 34, where we discuss in more detail how analysts engage in a dialogue with participants as part of the rating process.

MIS also publishes rating methodologies and makes a number of structured finance rating models available to the market either on a free or subscription basis but we do not offer as a service the evaluation of others' models.

34. Is the analyst assigned to a certain structured finance rating deal allowed to give advice to the participants (before the rating is issued) about how to structure the deal in order to raise the rating? Is the analyst allowed to give feedback to the participants of a deal if the initial rating does not meet expectations? Are there limits to which elements of the deal can be addressed and to what extent (i.e. does the analyst provide suggested changes to the structure)? Is this covered in any internal policies? Is this interaction monitored by the agency?

Response: MIS does not structure, advise on, create or design securitisation products. We are not competent to, and we do not, recommend one proposed structure over another. Structures are designed by arrangers and investment bankers to fit the needs of particular investors. We are not privy to many of the discussions that contemplate features of a securitisation (especially non-credit related features) and we do not know who the ultimate investors in the transaction will be.

However, in rating any structured security (or any corporate or governmental security), we may hold numerous, in-depth analytical discussions with issuers and/or their advisors. These discussions do not transform credit rating agencies into investment bankers, consultants or advisors. Instead, they serve the dual purpose of: (1) helping us better understand the

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46 E.g. in percentage of total structured finance ratings issued, or by giving the indication "always", "often", "sometimes" or "never".

47 Moody's Analytics, a separate division of MCO from MIS, offers many analytic tools that subscribers can use to, among other things, evaluate for themselves structured finance securities and securitisation structures. Credit Values DCV (described in our response to Question 6) is one such tool offered by Moody's Analytics.

particular facts of the transaction as proposed by the issuer; and (2) clarifying to the issuer the rating implications of our methodologies for that transaction.[48]

In circumstances where there is considerable performance history for the particular asset and where the structure has been used previously, our published methodologies may provide sufficient transparency about our analytical approach to significantly reduce the need for detailed "back-and-forth" discussions. In contrast, we have more extensive conversations with issuers who are securitising new asset classes or using novel structures. In these situations, issuers present circumstances that are different from those we have discussed in our published methodologies (revealing limitations of a "one-size-fits-all" approach). Therefore, we need to engage in a dialogue to assess the attributes of the proposed transaction against existing, published methodologies.

Importantly, MIS does not receive incremental or additional payments for holding such discussions. We believe, however, that these discussions help enhance overall market transparency and stability, in that both issuers and investors have a better understanding of our analytical approach and the ratings that result.

The interactions of MIS (and its credit professionals) and other entities participating in structured finance transactions are addressed in Section 2 of Part III of the MIS Code, the *MCO Code of Business Conduct* and implementing internal policies of general application.

Regardless of the fact that MIS does not structure, create or design securitisation products, we are aware that a perception persists that rating agencies are involved in these activities. We are considering various means to address more effectively this misperception.

35. Can factors such as greater complexity and/or innovative features in a structured finance deal lead to a higher than standard fee? If yes, please indicate how much these aspects can increase the initial level of the fees (as a percentage), how this increase is determined and who makes this decision.

Response: Yes. Greater complexity, innovative features and other factors require substantial analytical time in order to rate the transaction can result in higher fees.

Fees for rating structured finance transactions generally are based on the nominal issuance amount of the transaction, the applicable asset class and the anticipated complexity, as established in our fee schedules. If it is necessary to have discussions regarding the fee schedules, our intermediary and issuer relations personnel (who are not involved in the rating process) conduct such discussions.[49]

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[48] Similar discussions take place with corporations contemplating changes in financial structures or business strategies (e.g. regarding the potential rating implications of a share buy-back programme on a corporate issuer's senior unsecured debt obligations) or with new corporate issuers to whom MIS has not previously assigned a rating.

[49] Section 2.12 of the MIS Code provides that "MIS will not have Analysts who are directly involved in the rating process initiate, or participate in, discussions regarding fees or payments with any entity they rate." In a limited range of circumstances, a manager who supervises credit analysts may participate in a discussion about fees in order to provide expert input, e.g. about the type of transaction to be rated. If this occurs, then pursuant to Section 2.12 of the MIS Code, that manager will not, thereafter, participate in any rating process involving the entity or transaction in question.

36. Please provide us with data about your remuneration structures and those of your management hierarchy in your parent company.

Response: MCO is listed on the New York Stock Exchange and registered with the US Securities and Exchange Commission ("**SEC**"). Accordingly, MCO is required to publish and file with the SEC detailed annual disclosure about how it compensates its chief executive officer, chief financial officer and its three other most highly compensated executive officers, as well as its board members. The relevant information is contained in our annual Proxy Statement on Schedule 14A, which can be accessed through a link on our *Shareholder Relations* webpage.

Provision 2.11 of the MIS Code states:

> *"……Analysts will not be compensated or evaluated on the basis of the amount of revenue that MIS derives from Issuers that the Analyst rates or with which the Analyst regularly interacts"*

MIS's remuneration structure and policies are crafted to protect and enhance the long-term value of our rating franchise. To achieve this, we must attract, retain and motivate talented and knowledgeable individuals and then provide them with incentives to act in a manner consistent with our long-term objectives. This involves, among other things, striking the appropriate balance between short and longer-term compensation and benefits, and between fixed and performance-linked compensation.

MIS's remuneration program for analysts and managers consists of: (1) an annual base salary; (2) performance-linked annual cash and longer-term equity incentives; and (3) personal benefits such as medical insurance, retirement benefits and an educational assistance programme. The performance-linked components of our plan are broadly classified into two areas – cash and equity.

> <u>Annual Cash Incentive Awards</u>: MIS has two annual cash incentive award plans, one for individuals at the Managing Director or higher level and one for other, professional staff. Individuals at the Managing Director or higher level are eligible to participate in the Executive Performance Incentive Compensation Plan ("**EPIC**"). EPIC is described in our 2007 Proxy Statement.[50] Those analysts not entitled to participate in EPIC are eligible to participate in our Performance Incentive Plan ("**PIP**").[51]

[50] Cash incentive awards made pursuant to EPIC are funded by MCO's successful achievement measured against pre-set targets. The sum of all individual payment calculations made at the end of the year contributes to the "annual funding" described in the MCO Proxy Statement. Aggregate funding in a given year depends on MCO's financial performance against targets relating to growth both in operating income and earnings per share. Individual awards are based on evaluations of the individual's accomplishments in the past year and contributions to strategic objectives, as well as consideration of specific retention or incentive objectives for the individual.

[51] Under PIP, eligible individuals can receive an annual cash incentive award based upon two factors: (1) the performance of MCO (excluding Moody's KMV), measured as a ratio of actual annual operating income to budgeted annual income; and (2) an evaluation of individual performance. Individuals eligible to receive awards under PIP are assigned a Target Incentive Opportunity, expressed as a dollar figure. Individuals can receive 100% or their Target Incentive Opportunity, or more, or less, depending on their individual performance and how our operating income measures up to our budgeted operating income.

Long-Term Equity Incentive Plan: MCO's long-term equity incentive compensation plan is designed to reward and motivate analysts at the level of Assistant Vice President-Analyst or higher and our managers for their individual performance, as well as for overall company performance, over a multi-year period. Each long-term equity incentive award consists of approximately 50% stock options and 50% restricted stock, based on the fair market value of MCO's common stock on the date of grant. Analyst equity awards (both restricted stock and stock options) vest in equal instalments over four years, as do stock option grants awarded to executives. Restricted stock awarded to our executives at the Managing Director or higher level vests over a target period of four years.[52] The restricted stock awards granted to senior analysts below the level of Managing Director vest in equal instalments over four years.

We believe that our long-term equity compensation plan is appropriate as the potential appreciation in stock options provides long-term motivation incentives, while the restricted stock grants reduce the leverage in the plan and help retain employees even in a period where their stock option grants are "under water". Additionally while many companies provide for stock options to vest over three years, we have chosen a longer, four-year vesting period for our stock options to encourage a longer-term orientation in our employees. Likewise, a four-year vesting period applies to most awards of restricted stock.

Miscellaneous

37. Are you satisfied with the level of information received from servicers of European mortgage pools? Is this of a different quality, level of standardisation or frequency compared to information received in the US?

Response: The frequency with which we receive information from servicers of European mortgage pools depends upon the reporting requirements set by the terms of transaction. In the United States, transactions tend to have monthly reporting requirements while in Europe, the transactions tend to have quarterly reporting requirements.

MIS believes that the timeliness and quality of the performance data is crucial to MIS and the users of our ratings and research. The quality of data across all geographic regions varies. Some originators or servicers provide timely and complete performance data, while others do not. Consequently, MIS finds that in some cases, surveillance analysts need to ask questions about the content of the data we receive before that data can be normalised and incorporated into our databases for monitoring purposes. This extends the monitoring process.

MIS believes that greater standardisation in the presentation and content of performance data would facilitate more efficient monitoring and, ultimately, enhance transparency.

38. Are ratings across different asset classes similar in terms of pace and pattern of migration? Would some form of volatility indicator be possible, and appropriate, for structured finance ratings?

[52] The vesting period can be shortened to three years or lengthened to five years depending on the extent to which MCO achieves certain targets relating to growth in operating income. We use operating income growth as a vesting performance trigger for these awards because we believe that this measure closely tracks whether the company is successfully building its business over the long term.

Response: After a security is issued, an issuer's credit profile may change and this may, as a result, prompt both a rating change and a change in the price of the security. Some investors may experience trading or mark-to-market losses or gains. Since MIS's credit ratings reflect only the risk that investors will experience losses from defaults, the credit ratings do not directly assess the risk that the ratings themselves will change, nor do they address the risk that active investors will experience trading losses or gains.

Securities that carry the same credit rating are expected to experience similar credit losses over long periods of time across multiple credit cycles. MIS does not, however, expect that securities that carry the same credit rating will necessarily experience similar ratings volatility, either with respect to the frequency of rating changes (upgrades or downgrades) or with respect to the number of rating notches changed when ratings do change.

For example, until recently, the frequency of rating changes was notably greater for corporate than for structured ratings. This difference did not reflect differences in monitoring processes, as new information was being reviewed by analysts at least as often in structured finance as in the corporate sector. Rather, the historically lower frequency of rating changes in structured finance may have resulted from the more limited set of circumstances that might prompt a rating change in that sector and by the fixed maturity date targeted by most structured ratings. Since corporate ratings have an indefinite horizon, any enduring change in corporate credit risk will be reflected in all the corporation's debt ratings. Since structured finance securities typically have finite, medium-term maturities, many changes in the credit environment that would affect the credit quality of new issuances have few credit risk implications for securities that are already near their expected redemption dates.

When rating changes do occur, the magnitude of the changes tends to be larger in the structured sector for a number of reasons.[53] Some securities experience higher-than average volatility immediately prior to redemption because they have amortised substantially and their performance (against a small remaining balance) depends directly on the performance of a small, residual pool of collateral assets. In other cases, transactions are structured to withstand a wide variety of extremely adverse credit environments, so the frequency of rating change is low. The only events that can cause their ratings to change are rare but "catastrophic" changes in risk that materialise suddenly in a very short period of time, often causing large rating changes.

In such sectors, rating changes are correlated among debt instruments that have similar fundamental drivers of credit risk. Corporations operating in the same industry and geographical region are likely to experience upgrades and downgrades at the same time. Similarly, structured securities in the same asset class, issued at roughly the same time, are particularly likely to be upgraded and downgraded at the same time. The risk of correlated rating changes, however, is probably higher in structured finance than in corporate finance because structured securities, by design, eliminate much of the potential, idiosyncratic risk that drives issuer-specific rating changes. Consequently, when broad economic factors that drive collateral performance deviate sharply from expectations, a large number of structured securities within the same sector and of the same vintage are likely to be similarly affected either through upgrades or downgrades.

[53] This phenomenon is discussed in MIS publications such as *Structured Finance Rating Transitions: 1983-2006*, January 2007 (Document 101833) at p. 7.

Investors might make better, more informed use of credit ratings if they are used together with various volatility metrics.[54] Volatility tools can provide investors with some dimension of the nature and degree of fluctuation (up or down) to which a given security might be subject. To the extent that investors prefer not to be exposed to such fluctuations, they can choose to avoid holding such a security, even if the security meets the investor's rating criteria. Some examples of volatility measures include the following:

> Rating volatility: By measuring the historical frequency and scale of rating changes, MIS could construct volatility predictions for (1) individual entities or instruments; (2) by rating level or asset class; or (3) any combination thereof. Such metrics would provide context as to the likely stability of a rating over time.[55] MIS is attempting to develop a methodology that would provide for the assessment of ratings volatility as a function of certain behaviours or events that are relevant to the key metrics considered as part of the rating process. For example, the methodology could provide for an opinion on the ratings volatility of different RMBS tranches in circumstances where expected losses on the underlying assets doubled. The methodology could then be applied to the related CDO tranches (i.e. whose securities are collateralised by different RMBS tranches). Such opinions could assist investors in comparing the volatility of securities with the same credit rating. This methodology is in an early stage of development and MIS is still evaluating its potential usefulness to users of credit ratings.
>
> Price volatility: Some fixed income securities tend to exhibit considerable price movement over time, often independent of changes in credit risk. Since a highly rated security may have high price volatility or low price volatility, investors may be well-served to understand the historical price volatility associated with an instrument before investing.
>
> Asset volatility: For structured securities, the price or credit volatility of the underlying assets used as collateral could help investors anticipate potential credit and/or valuation problems in the structured instrument itself. For example, useful metrics for mortgage-backed securities might include house price volatility or volatility in underlying macroeconomic fundamentals for the geographies to which an RMBS is exposed. Some regions experience relatively large swings in house prices and unemployment while others do not. Further insight into these dynamics could help inform investors' security selection and portfolio management decisions.

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[54] The new Credit Values DCV tool enables subscribers to conduct a sensitivity analysis with respect to changes in assumptions (e.g. regarding market or credit conditions), thereby facilitating an assessment of both potential rating and price volatility.

[55] As described above, MIS's ratings in different sectors, e.g. structured finance versus corporate ratings, have historically demonstrated similar levels of accuracy but different levels of volatility. From one perspective then, ratings performance is comparable; from another, it is not.

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5 December 2007

Ms. Ingrid Bonde
c/o CESR
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Via e-mail : secretariat@cesr-eu.org

Dear Ms Bonde

CESR request for information

Thank you for your letter dated 14 November 2007.

Standard & Poor's Ratings Services ("Ratings Services") welcomes the opportunity to respond to the request for information attached to your letter and we enclose our response to all of the questions that you sent us, except those that call for confidential information (which we discuss further below).

We understand that CESR intends to publish responses received from the rating agencies engaged in this process of dialogue. As you are aware, we have significant concerns about making public in this way information which is not already in the public domain and which is commercially sensitive. For that reason we propose to send you, under separate cover, our responses to questions 10(a) insofar as this relates to Exhibit 13 to Ratings Services' Form NRSRO application form, 10(c), 11, 15, 16 and 26.

Before we send you that confidential information, we should be grateful if you would confirm to us that CESR will only provide it to those CESR Secretariat staff, or those staff within the members of the CESR task force, who need access to it for the purposes of preparing CESR's report, and then only if those staff members are subject to a national law duty of confidentiality that will restrict them from disclosing the information further.

We should also be grateful for your confirmation that this confidential information will not be disclosed to anyone else (including the CESR members who do not sit on the task force) or incorporated in any public CESR document, even in aggregated form, in such a way that it could be identified as having been produced by Ratings Services. We look forward to receiving your response to this request and to working with the CESR task force as it prepares its second annual report to the European Commission.

Sincerely yours,

Vickie A. Tillman
Executive Vice President
Standard & Poor's Credit Market Services

cc : Raquel Garcia, CESR
Javier Ruiz, CESR

CESR request for information

Response of Standard & Poor's Ratings Services ("Ratings Services")

Transparency of methodology

1. Publication of methodologies and assumptions:
    a. Is there a section on your website devoted to the publication of your methodologies?

Response: Ratings Services structured finance assumptions, criteria and methodologies are public – they are either published on our public website at www.standardandpoors.com – criteria or Ratings Services will freely disclose them upon request.

    b. Do you provide explanations of the methodologies applied to the different categories of ratings for each asset class (e.g. RMBS, CDO, etc) separately by region?

Response: The core methodology for assigning ratings of structured finance securities is principles-based and globally consistent. This approach enables Ratings Services to respond to the market's evolving needs and enhances the global comparability of the ratings which are assigned. Other methodology publications that address structural, legal and modelling aspects for distinct asset classes may be more jurisdiction- or region-specific.

    c. Do you provide the full method applied to each category of rating for each asset class (e.g. RMBS, CDO, etc.) separately by region?

Response: As discussed in 1b above, our detailed methodology publications are jurisdiction- or region-specific where applicable. They describe our methods to as full a level of detail as possible. However, it is important to remember that our ratings are ultimately assigned and reviewed by committees formed of analysts who use their experience and judgement to come to a rating opinion. Ratings are not derived via any single, rigidly-applied approach for a given asset class in a given region. It is therefore not possible for us to be fully prescriptive in our methodology publications. Instead, we aim to be fully transparent regarding the risks we are aiming to assess, and the principles we apply.

    d. Is all of the above information freely accessible or is part of it only available for subscribers?

Response: This information is freely accessible.

2. Publication of changes in methodologies and assumptions: Are all changes/adjustments to your methodologies and assumptions published and, if yes, where exactly are they published?
    a. Is there a special section on your website where changes made to criteria can be reviewed over time?

Response: All material changes to methodologies and assumptions are published on Standard & Poor's public website at www.standardandpoors.com – criteria.

    b. Do you publish reports that discuss the changes made to criteria?

Response: Yes, where we consider that investor interest warrants it. In such cases, the report typically sets out in the introduction what criteria changes have been made, while the specifics of those changes are set out in the relevant section of the report. Furthermore, such reports referring to criteria changes are accompanied by a press release which gives an overview of what the criteria relate to and where they can be found. The press releases are available on newswires such as Bloomberg, Reuters and Associated Press, as well as on our public website.

c. Do you have press conferences to announce and explain those changes?

Response: We hold press conferences where we believe investor interest is broad enough to warrant this. In 2005, Ratings Services initiated a process for obtaining market feedback on certain significant criteria and policy actions. We note that most changes to methodologies are merely refinements that have no material impact on outstanding ratings, or changes to reflect evolution in the relevant asset class or market rather than changes in underlying principles. As mentioned above, Ratings Services actively solicits feedback on its criteria and methodologies.

3. Do you provide links/references to those publications mentioned in question 2 in the respective rating change reports (i.e. the announcement of a change would let the reader know where to find the related methodology)?

Response: In circumstances where rating actions result directly from changes in underlying methodology, Ratings Services will clearly indicate the impact and reason for the methodology change, and will reference the relevant methodology publication and update the methodological piece as soon as practicable thereafter.

4. If changes have been made to your methodology for a particular product type (say US sub-prime RMBS) but previous issues have not been reviewed against this methodology how do you ensure this is clear to the marketplace? If the previous issues were being reviewed how would this be made public?

Response: When we announce and publish details of any new methodology, the associated publication would make clear the scope of transactions to which the new methodology is intended to apply. If previous issues were being reviewed, then those that were deemed sufficiently likely to see a rating action would typically be placed on CreditWatch, in accordance with our usual CreditWatch policy.

5. Is publishing the methods you use enough to meet the requirements of the IOSCO Code and ensure sufficient transparency or do you see further possibilities for improving transparency/the understanding of
    a. your ratings?

Response: Ratings Services Code of Conduct, Section 3A in particular conforms to the IOSCO Code provisions on transparency. Hence we believe that publication of our methodologies and other material as outlined in the Ratings Services Code of Conduct is consistent with and therefore sufficient to meet the requirements of the IOSCO Code. Ratings Services has also made repeated statements and outreach to market participants about the nature and role of its credit ratings in order to enhance their transparency. In particular Ratings Services has made clear that its credit ratings represent an opinion of the likelihood that a particular obligor or financial obligation will repay principal and interest in a full and timely fashion. Ratings Services is committed to learning lessons from recent events in the credit markets, including any lessons on the role of credit rating agencies. We will continue to make further efforts aimed at broadening understanding of what ratings *are and how they behave, as part of our wider publishing and market outreach efforts beyond publication of our methodologies.*

b. your rating process?

Response: We believe that publication of our methodologies and other material as outlined in the Ratings Services Code of Conduct is consistent with and therefore sufficient to meet the requirements of the IOSCO Code. As referred to in the previous response, Ratings Services has made repeated statements about the nature and role of credit ratings and has also sought to respond to issues raised in recent months in connection with the rating processes of credit rating agencies. We are making, and will continue to make, every effort to enhance our communications regarding our rating process. Ratings Services will give additional attention to refining its communications strategy to target understanding of its ratings and ratings process.

6. What steps does your firm take, if any, to contribute to enhancing the financial education of investors or potential investors?

Response: Ratings Services goes to great lengths to reach out to investors and the public at large to communicate the nature and role of ratings. By way of example, we hold regular events, such as public conferences, seminars, targeted roundtables, teleconferences and speaking engagements by analysts and other ratings staff. We also provide an extensive programme of training events, details of which can be found at www.standardandpoors.com > Research and Knowledge > Events and > Training.

Beyond this, Ratings Services regularly requests formal and informal comment on proposed rating methodology changes. In addition, we also interact regularly with financial market regulators around the world in a spirit of openness and with a view to contributing to a fair, transparent and robust structured finance market. A key part of those initiatives is to bring clarity to the wider public on credit ratings and the rating process. An example is our "Glossary of Securitization Terms" which is available free on our public website in eight languages and was first published (in English) in 2003.

7. Do you take steps to clarify any limitations to your ratings, including what they are intended to cover, or the methodologies and the assumptions underpinning them? How do you do this?

Response: Ratings Services' criteria and methodology publications, in particular its rating definitions which are publicly available on the S&P public website, clearly address what a rating speaks to and what it does not speak to.

8. Do you publish, and if so, where, your approach to the use of confidential information in rating of structured finance (SF) operations? Does it differ from that which you follow in "traditional" corporate rating?

Response: As for corporate and government ratings, Ratings Services' Confidential Information Policy and Ratings Service' Code of Conduct (reflecting the relevant provisions of the IOSCO Code) also apply to structured finance ratings. Both the Confidential Information Policy and the Ratings Services Code of Conduct are published in the Ratings section of our public website under "Policies, Criteria & Definitions".

9. Do you consult with industry as to what disclosure levels they would like to see for methodology and model assumptions?

Response: As part of the outreach activities mentioned in our response to question 6 above, we regularly discuss these issues with market participants. For the most part we find that the industry values the level of disclosure we currently provide. In cases where participants envisage more detailed disclosure of methodologies as being desirable, this is often not practically possible for the reasons outlined in our response to question 1c above.

Human Resources

10. Please provide us with the following information with regard to SF ratings and traditional ratings:
    a. Exhibit 4, 8 and 13 of your NRSRO application form.

Response: Exhibits 4 and 8 of Ratings Services' Form NRSRO application form are attached to this response. Exhibit 13, which is supplied separately, was submitted to the US SEC on a confidential basis and Ratings Services requests that CESR maintain its confidentiality.

    b. The internal definition of the existing classes/levels of employees in the CRA's rating business: e.g. junior/mid/senior analysts, supervisors, committee analysts, lead analysts, etc? [1]

Response: Consistent with our Form NRSRO filing (Exhibit 8) and SEC regulations, our credit analysts participate in determining our credit ratings and supervisors are responsible for supervising analysts who perform credit rating activities. There are other classes of employees who may participate in or support our credit rating activities, including in shared services such as our IT, Legal, Communications, Compliance and Finance departments.

    c. Historical data for exhibit 8 (information on number of analysts/supervisors) covering the 1997-2006 period split by:
        I. the staff levels identified in point (b) above.
        II. Worldwide, EU and US based.

Response: Our response is supplied to CESR separately on a confidential basis.

    d. What are the minimal educational and professional requirements for the different levels of employees (as defined in b) within the analytical staff, and have these requirements varied over the past 10 years? If they varied, how did they vary?

Response: The general educational and professional qualifications for credit analysts and supervisors are a college or university-level education plus MBA, CFA, JD or other relevant degrees or designations and experience as noted in (e) below. As best as our records reflect, these qualifications have not varied significantly over the past 10 years. We hire quantitative analytics personnel who hold PhDs.

    e. The typical minimum number of years of experience according to levels of employees as defined in (b). Has this number evolved over the past 10 years? If so, how?

Response: The general years of experience for credit analysts is from two to ten years (depending on job level - junior, mid and senior) of relevant professional experience or

[1] This question is designed to enable the CRA to answer the other questions based on its **own** human resources structuring method as different CRAs may have different human resources structures or seniority definitions (junior/senior, analyst/supervisor…).

experience in their practice area. For supervisors, qualifications generally are from five to ten years (depending on job level-mid to senior) of experience in their practice area. As best as our records reflect, these qualifications have not varied significantly over the past 10 years.

11. Please provide us with figures on the annual turnover of employees over the period 1997-2006, split per level (as defined in (1.b)), covering I) SF ratings and II) traditional ratings.

Response: Our response is supplied to CESR separately on a confidential basis.

12. What are the risks presented by staff turnover to your ability to function effectively as a provider of accurate ratings and what steps do you take to mitigate these risks? Are these successful?

Response: We are conscious that staff turnover is an important factor to be taken into account in maintaining the quality of our ratings. We consider that the processes we have in place to ensure the skills and resources required in the context of the rating committee process and the quality control processes applied to that process enable Ratings Services to successfully avoid any risks that might be posed by staff turnover. Ultimately if Ratings Services were not in a position to devote sufficient resources to a new rating assignment, it would not be taken on. Whilst we are aware that staff turnover tends to be cyclical in nature, we continue to have in place an active recruitment programme to ensure the replacement of members of staff who leave and to ensure an effective talent pipeline. To this end, we have established a team of dedicated recruiters in New York, London and other locations globally. We maintain active contact with universities and recruitment agencies. We also place vacancies both on our public website and on external recruitment websites. We believe that these measures work well.

13. Has it become harder to fill vacancies in structured finance ratings teams over the last 5 years? If yes, what has been done to ensure you continue to have sufficient resource and to ensure this does not affect the quality of your ratings?

Response: It has become more difficult to fill vacancies in the last few years due to heightened competition for talent but we consider that the processes referred to in the response to the previous question effectively meet those challenges. It is worth noting that we have also strengthened our in-house training programme for structured finance analysts to enhance the quality of the rating process and ratings issued by Ratings Services. In the US Structured Finance practice, we generally hire 18 to 25 MBAs per year into an internship programme from which we recruit them as permanent staff.

14. Typically, what is the composition of a monitoring/rating team in terms the job profiles and job levels and does this differ from teams that monitor/rate corporate bonds?

Response: The rating review (surveillance) group is made up of the full range of job levels and profiles. Analysts are assigned to transactions according to the complexity of those transactions, more senior analysts being assigned to more complex transactions. However, review committees are subject to clear standards of composition, including analyst grade and experience and quorum. They do not differ in profile from teams that monitor corporate bonds with the only key difference that, in structured finance, the monitoring and review of ratings is carried out by a dedicated team, separate from (but generally equal in terms of profile and experience as) the initial ratings team.

15. Please provide us with information on the average number of deals and average number of transactions under surveillance per lead analyst by type of SF products in the following table format:

Type of product	Average number of deals per lead analyst in 2006 (primary rating) *	Average number of transactions under surveillance per lead analyst in 2006
RMBS		
CMBS		
CDO		
ABS		
(additional if necessary)…		
…		

* both deals that resulted in a final rating and deals that did not result in a final rating.

Response: Our response is supplied to CESR separately on a confidential basis.

16. What are the total annual wage costs in structured finance rating over the period 1997-2006?

Response: Our response is supplied to CESR separately on a confidential basis.

17. Do you outsource part of the rating/surveillance process (e.g. data gathering, processing, modelling, etc.)? If yes:
    a. Please describe in which part(s) of the rating/surveillance process you make use of outsourcing and to what extent.

Response: It is not our practice to outsource parts of the rating and surveillance process. In the European region, for example, data processing for structured finance may be handled by a subsidiary company of The McGraw-Hill Companies, Inc. ("McGraw-Hill") with the activity under the direct management of an internal team of data specialists. Some cash flow modelling is also handled by a recently acquired wholly-owned subsidiary of McGraw-Hill.

    b. What are the risks implied by such outsourcing and how do you tackle these?

Response: Not applicable.

c. Do you consider the (economic) gains of such outsourcing to exceed the risks?
Please motivate.

Response: Not applicable.

Monitoring of transactions

18. What drives the frequency of rating review for structured finance? Why is this frequency appropriate? Please outline the process that would lead to a rating being taken to review committee?

Response: The ongoing rating review process varies depending upon asset class or transaction type but generally tracks to the frequency with which we receive transaction-related reports. This is typically monthly or quarterly, given typical bond payment and/or reporting timelines for the rated transaction. These periodic reviews serve to identify any transactions whose performance at a bond or asset level indicates that more detailed analysis may be required to confirm whether the current ratings remain appropriate.

Examples of this review process are:

- For Residential Mortgage Backed securities (RMBS) and Asset Backed Securities (ABS) (e.g. those backed by credit card receivables, auto loans etc), aggregate asset data on variables showing such as delinquencies, losses and prepayment rates are processed on receipt each reporting period and breaches of pre-defined triggers are automatically flagged. Those triggers include performance considerations such as the growth in delinquency levels, the ratio of delinquencies to available credit enhancement etc. All transactions flagged by this system are subject to detailed analytical review as appropriate including a review of loan level data, credit and cash flow modelling. Where such a detailed review indicates that the current rating may not be appropriate, the responsible analyst will present their findings and recommended action to a full rating committee, which will decide upon any rating change, CreditWatch placement, or affirmation of the current rating. Many final rating actions will be preceded, pending a fuller analysis, by a CreditWatch placement.

- For Commercial Mortgage Backed Securities (CMBS) and cash-flow CDOs, a similar process to RMBS/ABS is followed, with triggers being met, tests and exceptions identified on each reporting period and forwarded to the assigned surveillance analyst for detailed review and subsequent action as above.

- For synthetic CDOs (CDS), the current reference portfolio for every rated transaction is run through our credit model (CDO Evaluator) each month. For each CDO tranche where this process identifies that the current level of credit enhancement is insufficient to support the current rating, or that the current level of enhancement is sufficient to support a higher rating, there will be a prompt CreditWatch placement. Typically within the same month the portfolio will be re-analysed using the credit model and appropriate rating action taken. The outputs of this analysis for all publicly rated transactions are published each month in S & P's Global SROC (Synthetic Rated Overcollateralisation) report.

In addition to the standard periodic review process applied to all rated transactions, events such as changes of ratings on transaction supporting parties may also initiate review and potential rating actions.

19. Would regular reviews and announcements on the appropriateness of structured finance ratings - possibly based on some contractual deadlines (i.e. on a regular (quarterly/semi-annual basis) - help in preventing mass downgrades, improve the appropriateness of existing ratings? If not, why?

Response: As described above, regular reviews are already in place, which are typically monthly or quarterly in frequency. As a result, the existing downgrades are indeed maintained at an appropriate level. Multiple downgrades (or upgrades) are not commonplace and when they do occur are generally a reflection of market dynamics, rather than a reflection of our surveillance process. There will be occasions when economic circumstances, or even a single event, impact a number of rated transactions at the same time. For example, the default of a corporate entity referenced in the portfolios of a large number of synthetic CDOs could cause a correspondingly large number of CDO ratings to be downgraded at the same time. Similarly rapid US house price deterioration might be expected to affect the ratings of numerous US RMBS tranches at the same time.

20. What changes have you made in terms of the surveillance of ratings since the widespread RMBS and CDO downgrades earlier this year?

Response: Please see attached publications detailing revisions to assumptions applied in the rating of US sub-prime and other RMBS and CDO of ABS.

November 2007

11.09.07 Standard & Poor's Enhances LEVELS® 6.1 Model

11.05.07 Standard & Poor's Alters Assumptions For LEVELS 6.1 Release

October 2007

10.24.07 Criteria: Request For Comment: Providing U.S. RMBS Monthly Loan-Level Performance Data To Standard & Poor's (PDF)

10.23.07 Criteria: Proposed File Format: Standard & Poor's Request For Ongoing U.S. Residential Loan-Level Information

10.22.07 Article Details S&P's Approach To Use Of Loss Curves For Determining Default Probability (PDF)

10.19.07 Standard & Poor's Revised Default and Loss Curves for U.S. Subprime RMBS (PDF)

10.17.07 Standard & Poor's Ratings Services Reviews Ratings on Certain U.S. Residential Mortgage-Backed Securities Issued in 2007 (PDF)

10.16.07 S&P Alters Modeling Assumptions For Step-Down Provisions To Enhance Credit Support For US RMBS

10.09.07 Standard & Poor's Revises Assumptions For Analyzing U.S. RMBS Pools That Contain Modified Loans

21. How is the appropriate portfolio size determined for structured finance monitoring analysts? Are there any internal procedures which dictate how many transactions a monitoring analyst should be responsible for?

Response: The size of portfolio assigned to individual analysts will depend in large part on the nature of the surveillance process and structural and other complexities of the transaction type. For example, an analyst responsible for the surveillance of synthetic CDOs, where the process is primarily model-driven, will have the capacity to monitor a far higher number of ratings than, say, an analyst with responsibility for monitoring a portfolio of CMBS transactions. A capacity model is maintained to ensure that the ratios remain appropriate.

By way of illustration, the number of surveillance analysts in Europe has increased by 20% since the start of 2007 while the number of transactions under surveillance increased by 15%.

22. Are the costs of monitoring structured finance transactions fully covered by the fees charged specifically for monitoring when the rating agreement is initially made? What are the main incentives for maintaining effective monitoring of ratings?

Response: Yes, the costs of monitoring the ratings are covered by the fees charged for monitoring when the rating agreement is initially made.

There are a number of motivations for maintaining effective monitoring. Not least of these are the integrity of the ratings and the reputational risk to the company of not doing so. From an organisational standpoint, structured finance surveillance analysts' role and responsibility is the ongoing monitoring of ratings, so they are not subjected to conflicting calls on their time between initial ratings and ongoing monitoring. Their management reporting line is through to a senior manager responsible for ratings surveillance who has no responsibility for initial ratings. All the objectives that are set and by which their performance is measured relate to effective and timely monitoring of ratings.

23. How is committee time dedicated to rating reviews versus that dedicated to new ratings determined, particularly for structured finance? Are there clear internal procedures on how committee time is prioritised?

Response: As stated above, surveillance in structured finance is carried out by a separate team from initial ratings. There is, therefore, no competing call on their time between rating review committees and initial ratings.

24. Are the committee members reviewing a rating the same as those who approved the initial rating? Are there any internal procedures dictating the composition of the review committee?

Response: The rating review committees are led by and predominantly peopled by surveillance analysts. Primary analysts may attend if their specific knowledge of the initial ratings is considered to be of value in the review deliberation.

There are required standards for committee composition including analyst grade and experience and minimum quorum make up. These apply and are adhered to equally for rating reviews and initial ratings.

25. Is there a team of macroeconomic analysts within your firm responsible for systematically analyzing macro data coming in and building macroeconomic forecasts on which analysts can rely for their modelling/monitoring of ratings? If not, would this be useful?

Response: There are two macroeconomists in the company who work closely with the ratings group to provide direction as to macroeconomic trends and forecast. Additionally, within the surveillance group there is a dedicated research team which studies and incorporates macroeconomic data within its research for the purposes both of external publication and to inform the internal rating and review processes.

26. Please provide us with a breakdown of revenues from SF ratings for initial rating/surveillance. How is the relative size of each of these parts of the fee decided?

Response: Our response is supplied to CESR separately on a confidential basis.

Methodology changes

27. What prompts a review of rating methodology? Is there a central team that reviews methodologies or is it dependant on individual business lines self-evaluating their models?

Response: Reviews of rating methodologies can be prompted by a number of different factors. For example, over time our ongoing surveillance process could identify a systematic link between strong (or weak) observed performance trends and a certain transaction characteristic, which is not reflected in our rating methodology. In this case we might consider including that transaction characteristic as a differentiating factor in our rating analysis.

We note, however, that observed performance that is weaker or stronger than historical averages is not on its own a sufficient reason to review our assumptions, since these may still be correctly reflecting the relationship between, say, the transaction's collateral characteristics and credit enhancements and the long-term range of performance possibilities: the sector may simply be going through a performance cycle.

We would consider reviewing methodologies if we became aware of internal feedback raised in relation to the rating and/or surveillance functions or external (market) feedback, for example from investors, but in all cases we would take an independent view in relation to these cases.

There is a centralised criteria function, operating through regional criteria officers, the Structured Finance global criteria function and our Analytical Policy Board, which reviews these matters over and above the feedback from individual rating committees. This function *ensures that the process of criteria review and any proposed methodology changes are consistent with global practice. Individual business lines will provide feedback on the suitability of models but the central criteria function co-ordinates any review of methodology.*

28. Have you made any changes to how you evaluate the appropriateness of your methodologies on an on-going basis in light of the RMBS and CDO downgrades of earlier this year?

Response: Our methodologies remain under review in order to evaluate their appropriateness on an ongoing basis. We have not made any changes as to how we evaluate their appropriateness.

While our structured finance ratings process is the product of decades of analytical experience and excellence, we are always looking for ways to enhance that process and our analytics. This is a longstanding Ratings Services principle and is especially true when, as with recent subprime loans, developments indicate that historically-rooted behavioural patterns that have served as solid foundations for analysis may lack their prior value.
Ratings Services, and its Analytical Policy Board in particular, continuously evaluate the appropriateness of existing methodologies and criteria on an ongoing basis. It also drives a continuous enhancement process – as methodology and criteria are not static.
In light of developments in the US subprime market, and as part of our constant commitment to enhancing our analytical processes, Ratings Services has already initiated a number of steps:

- *We have significantly heightened the stress levels at which we rate and surveil transactions to account for deteriorating performance as evidenced by data we have received. We have also increased the frequency of our review of rated transactions;*
- *We have modified our LEVELS® model to incorporate these new stress levels and other changes recently made to our ratings assumptions, as announced in earlier press releases;*
- *We recently acquired IMAKE Consulting and ABSXchange. These services have long provided data, analytics and modelling software to the structured finance community and we feel they will further enhance our in-depth surveillance process;*
- *We have also undertaken a survey of originators and their practices, particularly with respect to issues of data integrity. We are in the process of compiling the results of this survey and will publish those results when finalized; and*
- *In addition to these steps, we continue to look at areas in which we can further enhance our analysis and processes. Some of the areas include:*
    - *Our policies and procedures to manage potential conflicts of interest;*
    - *The quantity and quality of data available to us; and*
    - *Modification of our analytics to reflect changing credit behaviours.*

29. When the methodology for a type of structured finance product (example being US sub-prime mortgage backed securities) is amended:

    a. Do you automatically review all existing ratings against the new methodology and take rating action based on this review? If not, what is the rationale behind this?

Response: Our ratings represent our current view of the default risk on different structured finance securities. Some changes to our criteria and/or methodologies reflect a shift in the *way we interpret information about the securities themselves or the economic environment, and in these cases there may be a corresponding shift in our opinion of the securities' default risk. If significant, these should be reflected in changes to our existing ratings. When a particular methodology or a piece of criteria is amended we always consider whether or not any existing ratings are likely to be affected as a result, and if so, which ones. This analysis is carried out on a case-by-case basis, as further detailed below. Where we consider that the ratings may be affected, we conduct a full review and take rating action where we find it to be appropriate.*

b. How is the scope of the application of the change of methodology determined? In other words on what basis does your firm decide whether or not to apply a change to existing ratings or just to new issuances?

Response: Amendments to our methodologies effectively represent changes to the process by which we form our opinions of default risk. This may or may not mean that those opinions themselves will change as a result. When we change a methodology we first determine whether or not it makes sense to apply it to just new issuances, or to some (or all) existing ratings. This depends on the type of methodology change under consideration. For example, if it became standard industry practice to solicit a new piece of information from residential mortgage borrowers at the point of loan origination, and we considered that using this information could enhance our interpretation of the loan's likely credit performance, then we might change our methodologies to take this into account. However, if such information was only available for new loans being securitized from a certain point going forward, it would clearly not be possible to apply the new methodology to existing transactions.

Even in cases where the new methodology could be applied to existing ratings, the impact on existing ratings might not be material. For example, the methodology change might only relate specifically to securitised loans with fewer than six months' seasoning. Since relatively few loans in existing transactions might have fewer than six months' seasoning, the rating impact might be immaterial for seasoned transactions. In determining the scope of application of any methodology changes we therefore test the materiality of any rating changes that would be implied from applying the new methodology to existing ratings, before deciding on the scope of the change.

c. Please explain in detail how is the timing of rating action determined across all affected ratings?

Response: When we have determined the scope of application of any methodology change we will perform a rating analysis to determine which ratings are relatively likely to change as a result of applying the new methodology, in advance of announcing the methodology change. Announcement of the methodology change would then be accompanied by rating actions on the affected transactions, typically in the form of appropriate CreditWatch placements - positive, negative, or developing - according to the provisions of our normal CreditWatch policy and standards. These CreditWatch placements would then typically be resolved within 90 days, or alternatively, we would publish further information if the CreditWatch resolution were to take longer than 90 days.

30. Does your firm at any time make any overall review of the changes to methodologies made, for instance during one year, and their impact on ratings to assess trends for instance? Would this be made public?

Response: Any changes made to our methodologies remain under review on a constant basis - to the extent that the findings of that ongoing review process result in a change in *methodology and/or were of particular interest to the market we would make such changes public.*

31. Is there a risk of originators 'gaming the system' i.e. keeping requested data sets high whilst other valid indicators of asset quality decline? If yes, what mitigation have you put in place to reduce this risk?

Response: To the extent that there is a risk of originators "gaming the system", we always reserve the right to ask for further information. If we consider that the information we have received is inadequate or insufficient we will raise this and if we do not obtain adequate responses to our requests, our practice is to decline to rate the transaction or withdraw a rating that had already been issued.

32. Do you feel that your approach to the assessment of the quality of underlying asset data is appropriate? Are you considering any changes in this area (specially in light of the recent events in the US sub-prime mortgage market)?

Response: While evaluating the credit characteristics of the underlying mortgage pool is part of our RMBS ratings process, Ratings Services does not rate the underlying mortgage loans made to homeowners or evaluate the granting of those loans in the first place.

Originators make loans and verify information provided by borrowers. They also appraise homes and make underwriting decisions. In turn, issuers and arrangers of mortgage-backed securities bundle those loans and perform due diligence. They similarly set transaction structures, identify potential buyers for the securities, and underwrite those securities. For the system to function properly, Ratings Services relies, as it must, on these participants to fulfill their roles and obligations to verify and validate information before they pass it on to others, including Ratings Services.

Our role in the process is reaching a credit opinion on whether or not the underlying loans as represented to us will generate sufficient cash to pay timely interest and ultimate principal on the securities issued by the RMBS transaction in a range of stressful economic scenarios. That is the relevant issue for assessing the default risk of those securities.

In the response to question 28, we presented some of the steps we are taking to enhance our analytical processes in the area of US RMBS.

Conflicts of Interest

33. When you rate a structured finance operation do you offer services such as impact assessment and/or models of evaluation or optimisation of the securitization structure? Can you quantify[2] the number of cases where these kinds of services were offered? Would these services be performed by the analyst who rates the final structure?

Response: Ratings Services offers services related to structured finance products in addition to credit ratings, such as, for example, models allowing market participants to evaluate

[2] E.g. in percentage of total structured finance ratings issued, or by giving the indication "always", "often", "sometimes" or "never".

potential securitisation structures with the same tools used by Ratings Services' analysts - and products providing an insight into Ratings Services' surveillance process in relation to certain transactions. Ratings Services structured finance group does not provide any "advisory" or "consulting" services. Analysts are not involved in the actual structuring of securities or entities that Ratings Services rates. Such structuring is the function and responsibility of the issuer, its investment bankers and financial advisers.

34. Is the analyst assigned to a certain structured finance rating deal allowed to give advice to the participants (before the rating is issued) about how to structure the deal in order to raise the rating? Is the analyst allowed to give feedback to the participants of a deal if the initial rating does not meet expectations? Are there limits to which elements of the deal can be addressed and to what extent (i.e. does the analyst provide suggested changes to the structure)? Is this covered in any internal policies? Is this interaction monitored by the agency?

Response: Ratings Services' analysts do not advise issuers as to how to structure transactions. In practice, analysts do talk to issuers as part of the ratings process, just as analysts have traditionally had discussions with corporate issuers with respect to the rationale behind the rating their securities. This dialogue provides benefits to the market. Critical to our ability to rate transactions is a robust understanding of those transactions. Reading documents and reviewing the results of modelling are important, but so is communication with those responsible for the transaction itself. Through dialogue with issuers and their representatives our analysts gain greater insight into transactions to be rated, including any modifications to those transactions that may occur as the process goes forward. This dialogue promotes transparency as to our ratings process which regulators have consistently encouraged.

This dialogue does not amount to "structuring" by Ratings Services, even in cases where the discussion is about the effect different structures may have on ratings. Ratings Services does not tell issuers what they should or should not do. Our role is reactive. Using our models and publicly available methodologies, issuers provide us with information and we respond with our considered view of the ratings implications. In the process, and as part of our commitment to transparency, we also may discuss the reasoning behind our analysis.

Some issuers structure transactions so as to achieve a specific rating result as a variety of potential structures could merit a particular result. Our role is to come to a view as to the structures presented, but not to choose among them. Again, we do not compromise our criteria to meet a particular issuer's goals. As Ratings Services makes methodologies publicly available, the market can assess in a straightforward manner whether the methodology was applied, thereby reinforcing Ratings Services' interest in consistent application of the methodologies and their credibility.

35. Can factors such as greater complexity and/or innovative features in a structured finance deal lead to a higher than standard fee? If yes, please indicate how much these aspects can increase the initial level of the fees (as a percentage), how this increase is determined and who makes this decision.

Response: Rating Services generally receives fees from issuers, arrangers or their agents. While Ratings Services makes its fee structure available, the fees for any specific transaction depend on the complexity of the issuer, issue or structure to be rated and the time needed to complete the analysis. As such, rating fees are not "mechanical".

In accordance with the Ratings Services Code of Conduct, analysts who are directly involved in the rating process do not initiate or participate in discussions regarding fees or payments for any ratings they are involved in. Rating fees are negotiated or determined by commercial *staff ("originators"). While Ratings Services' analysts may speak to originators regarding the analytical work involved for a particular rating, they are not involved in any commercial discussions with issuers or in fee-related discussions relating to such issue.*

36. Please provide us with data about your remuneration structures and those of your management hierarchy in your parent company.

Response: We take very seriously the particular provisions of the IOSCO Code relating to "CRA Analyst and Employee Independence".

In particular, provision 2.11 of the Ratings Services' Code of Conduct provides as follows:

"2.11 Reporting lines for Analysts and their compensation arrangements shall be structured to eliminate or effectively manage actual and potential conflicts of interest. An Analyst shall not be compensated or evaluated on the basis of the amount of revenue that Ratings Services derives from issuers or issues that the Analyst rates or with which the Analyst regularly interacts".

Ratings Services structures its employee compensation arrangements to minimise the potential for conflicts of interest to arise. Individual compensation does not depend on the number of ratings that an individual manages, the specific level of ratings assigned, or the revenue directly generated by those ratings. Ratings Services has both a base salary program and an incentive compensation plan.

Base salaries for analytical personnel in Ratings Services are established to reflect comparable external market data. Ratings Services periodically reviews updated market compensation data in order that its salary ranges remain competitive.

The incentive plan pool for each plan year is calculated using Ratings Services' actual prior year net operating income and a baseline incentive rate for the current plan year. The baseline incentive rate is reviewed each year and may be modified based upon general business conditions, retention needs, competitive compensation practices and market conditions. Individual incentive compensation is determined by Ratings Services management based on qualitative performance factors as summarised in our formal Performance Management Process.

Regarding our "parent company" compensation, you will be aware that Standard & Poor's is a division of The McGraw-Hill Companies, Inc. The McGraw-Hill Board Compensation Committee's report in the spring 2007 proxy statement stated that the main objectives of its executive compensation program are as follows:

- *To enable it to hire and to retain high calibre executive talent.*
- *To provide appropriate incentives for both individual and business performance.*
- *To build value for shareholders by requiring that a significant portion of executive compensation is tied to performance.*
- *To encourage the acquisition of a significant ownership stake in the company.*
- *To offer a total compensation package at the median level of executive compensation of its competitors in the publishing, information and media, and financial services industries when target levels of performance are met, while offering the opportunity for its executives to exceed the median for outperforming target goals and conversely, paying below median if the target goals are not achieved.*

Miscellaneous

37. Are you satisfied with the level of information received from servicers of European mortgage pools? Is this of a different quality, level of standardisation or frequency to information received in the US?

Response: In Europe, for residential mortgage transactions we receive comprehensive aggregate portfolio and underlying loan level data either on a regular ongoing basis or as required for full rating review. The timeliness and completeness of such data is actively monitored. We continue to work with issuers and servicers to increase the ratio of transactions for which loan level data is received on a regular, ongoing basis as opposed to on request. In the U.S., we receive substantial pool and security level information such as delinquency, loss, credit support and bond level cashflow detail and analysis, as well as certain data for loan level analysis, through third party providers. We have alerted the public that we will be requesting loan level data directly from servicers in the near future, and we anticipate that more expansive use of loan level data in the U.S. will coincide with our collection of increasing amounts of such data and our development of additional analytical tools.

For commercial mortgage transactions, the level of data received is quite sufficient to monitor and maintain ratings.

38. Are ratings across different asset classes similar in terms of pace and pattern of migration? Would some form of volatility indicator be possible, and appropriate for structured finance ratings?

Response: Our approach to ratings, in both policy and practice, is intended to provide a consistent framework for assessing default risk within and across geographies and sectors. Therefore, our ratings on RMBS, for example, are intended to have similar meanings to our ratings on CDOs, in terms of default risk. The same applies when comparing our structured finance ratings with, say, our corporate ratings. As an example, the three-year average default rate for 'AAA' structured finance ratings has been around 2 basis points (bps), compared to around 9 bps for corporate ratings. At 'BBB', the corresponding figures are 168 bps and 132 bps respectively.

However, for a number of reasons the ratings on structured finance securities may well display different dynamics in terms of pace and pattern of migration. Different asset classes may be subject to different economic cycles. For example, ratings on transactions backed by corporate risks could be undergoing upgrades while consumer-backed transactions could simultaneously be undergoing downgrades. Also, as a result of their structures, different transactions have inherently different risk dynamics, which could lead to different rating behaviour over time. For example, structures that feature granular asset pool with stable credit quality and sequential amortization of the rated notes (e.g. certain European RMBS transactions) typically experience a steady upward pressure on their ratings as they season, all else being equal. On the other hand, certain European CMBS transactions that are backed by only a handful of loans can experience sudden moves in tranche ratings if a large loan prepays, thereby significantly changing the composition of the asset pool and the liability structure.

Our ratings themselves do not comment on their future likely volatility. It may be possible to design a separate qualitative or quantitative rating volatility measure for some asset classes. We are currently assessing the practicalities and commercial viability of producing such an additional product.

Exhibit 4. Organizational structure. **X** ☐ Exhibit 4 is attached to and made a part of this Form NRSRO.

The Applicant, Standard & Poor's Ratings Services, is a separately identifiable division of Standard & Poor's, which is in turn, a division of The McGraw-Hill Companies, Inc. McGraw-Hill is comprised of three segments, described below. In addition, it has certain corporate subsidiaries that are not engaged in active business, but rather hold or operate purely corporate assets (such as real estate).

Education Segment

The McGraw-Hill Education segment serves the elementary and high school (el-hi), college and university, professional and international markets with a broad range of educational materials, assessments, and learning solutions. This segment comprises two operating groups: the School Education Group and the Higher Education, Professional and International Group.

Financial Services

The Financial Services segment operates under the Standard & Poor's (S&P) brand. Standard & Poor's provides independent credit ratings, indices, risk evaluation, investment research and data to investors, corporations, governments, financial institutions and investment managers and advisors, globally.

Information & Media

The Information & Media segment comprises two operating groups, which provide business information, insight and analysis in various formats on a global basis: the Business-to-Business Group (comprised of *BusinessWeek*, J.D. Power and Associates, McGraw-Hill Construction, Platts and *AviationWeek* brands), and the Broadcasting Group.

Attached below are:

(1) McGraw-Hill Subsidiary List - all subsidiaries of The McGraw-Hill Companies, indicating the segment or segments to which they belong
(2) Applicant Organizational Charts – showing:
    a. Business Units and Departments
    b. Managerial Structure

<u>Exhibit 4 Attachments</u>

McGraw-Hill Subsidiaries

Applicant Organization Charts

Exhibit 8. Certain information regarding the credit rating agency's credit analysts and credit analyst supervisors. **X** ☐ Exhibit 8 is attached to and made a part of this Form NRSRO.

The total number of credit analysts as of December 31, 2006:	1,025
The total number of credit analyst supervisors as of December 31, 2006:	222

Qualifications for credit analysts are generally as follows:

- Junior Analysts: MBA, CFA, JD or other relevant degrees or designations and from two to five years of relevant professional experience
- Mid-level Analysts: MBA, CFA, JD or other relevant degrees or designations and from five to seven years of experience in practice area
- Senior Analysts: MBA, CFA, JD or other relevant degrees or designations and seven to ten years of experience in practice area

Qualifications for credit analyst supervisors are generally as follows:

- Mid-level Supervisors: MBA, CFA, or JD or other relevant degrees or designations and from five to seven years of experience in practice area
- Senior Supervisors: MBA, CFA, or JD or other relevant degrees or designations and from seven to ten years of experience in practice area

Subsidiaries of The McGraw-Hill Companies, Inc.

McGraw-Hill Subsidiary	Segments	State/Jurisdiction of Incorporation	Percentage of Voting Securities Owned
BizNet.TV, Inc.	Information & Media	New York	100
Capital IQ, Inc.	Financial Services	Delaware	100
*Capital IQ Information Systems (India) Pvt. Ltd.	Financial Services	India	100
*CapitalKey Advisors (Europe) Limited	Financial Services	United Kingdom	100
CTB/McGraw-Hill, LLC	Education	Delaware	100
Funds Research USA, LLC	Financial Services	Delaware	100
Grow.net, Inc.	Education	Delaware	100
International Advertising/McGraw-Hill, Inc.	Information & Media	Delaware	100
J.D. Power and Associates	Information & Media	Delaware	100
*J.D. Power Asia Pacific, Inc.	Information & Media	Japan	100
*J.D. Power and Associated, Gmbh	Information & Media	Germany	100
*J.D. Power Australia Pty Ltd	Information & Media	Australia	50
*J.D. Power Automotive Forecasting U.K. Limited	Information & Media	United Kingdom	100
*Power Information Network, LLC	Information & Media	Delaware	100
-Power Information Network, Inc.	Information & Media	Delaware	100
McGraw-Hill Broadcasting Company, Inc.	Information & Media	New York	100
McGraw-Hill Interamericana, Inc.	Education	New York	100
McGraw-Hill International Enterprises, Inc.-Education	Education	New York	100
*McGraw-Hill Interamericana do Brasil Ltda.	Education & Financial Services	Brazil	100

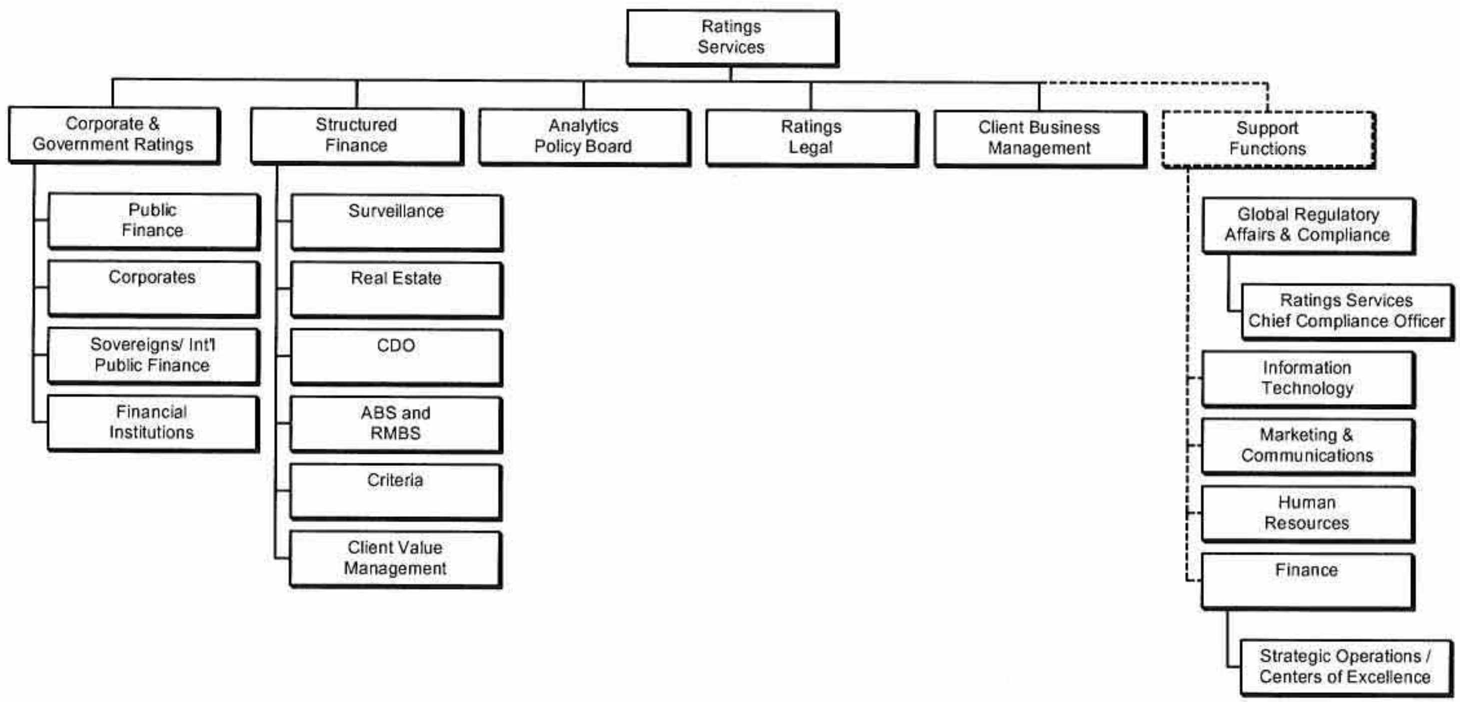
Subsidiaries of The McGraw-Hill Companies, Inc.

McGraw-Hill Subsidiary	Segments	State/Jurisdiction of Incorporation	Percentage of Voting Securities Owned
McGraw-Hill Australia Pty Limited	Education	Australia	100
*McGraw-Hill Book Company New Zealand Limited	Education	New Zealand	100
*Mimosa Publications Pty Ltd.	Education	Australia	100
-Carringbush Publications Pty Ltd.	Education	Australia	100
*Dragon Media International Pty Ltd.	Education	Australia	100
-Platypus Media Pty Ltd.	Education	Australia	100
-Yarra Pty Ltd.	Education	Australia	100
*Standard & Poor's (Australia) Pty Ltd.	Financial Services	Australia	100
*Standard & Poor's Information Services (Australia) Pty. Ltd.	Financial Services	Australia	100
McGraw-Hill Education Private (India) Limited	Education	India	66.25
McGraw-Hill Holdings Europe Limited	Corporate	United Kingdom	100
*McGraw-Hill Finance Europe Limited	Corporate	United Kingdom	100
*McGraw-Hill Iberia, Inc.	Corporate	Delaware	100
*McGraw-Hill/Interamericana de Espana, S.A.	Education	Spain	100
-Standard & Poor's Espana, S.A.	Financial Services	Spain	100
*McGraw-Hill International (U.K.) Limited	Information & Media, Education and Financial Services	United Kingdom	100
-Open International Publishing Limited	Education	United Kingdom	100
*Standard & Poor's AB	Financial Services	Sweden	100
*The McGraw-Hill Companies GmbH	Financial Services, Information & Media and Education	Germany	100

Subsidiaries of The McGraw-Hill Companies, Inc.

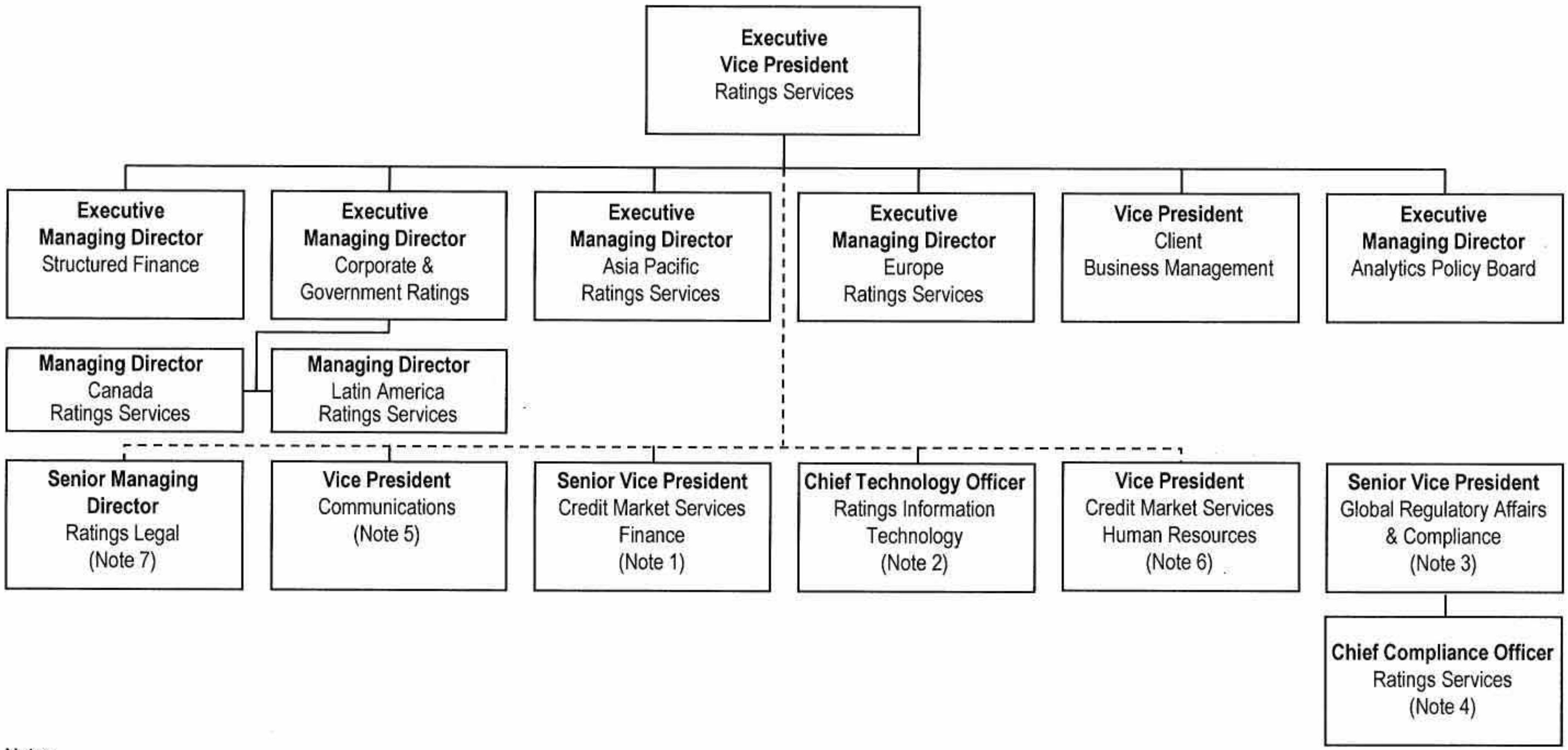
McGraw-Hill Subsidiary	Segments	State/Jurisdiction of Incorporation	Percentage of Voting Securities Owned
*The McGraw-Hill Companies SA	Information & Media, Education and Financial Services	France	100
*The McGraw-Hill Companies S.r.l.	Financial Services and Education	Italy	100
*The McGraw-Hill Companies Limited	Financial Services & Corporate	United Kingdom	100
*Xebec Multi Media Solutions Limited	Education	United Kingdom	100
-The McGraw-Hill Companies Switzerland GmbH	Education	Switzerland	100
McGraw-Hill Information Systems Company of Canada Limited	Information & Media	Ontario, Canada	100
McGraw-Hill/Interamericana de Chile Limitada	Education	Chile	100
McGraw-Hill/Interamericana de Venezuela S.A.	Education	Venezuela	100
McGraw-Hill/Interamericana Editores, S.A. de C.V.	Education	Mexico	100
*Grupo McGraw-Hill, S.A. de C.V.	Education	Mexico	100
McGraw-Hill/Interamericana, S.A.	Education	Panama	100
McGraw-Hill Ryerson Limited	Education	Ontario, Canada	70.1
MHFSCO, Ltd.	Education	U.S. Virgin Islands	100
Shortland Publications	Education	New Zealand	100
Standard & Poor's, S.A. de C.V.	Financial Services	Mexico	100
*Grupo Standard & Poor's, S.A. de C.V.	Financial Services	Mexico	100
The McGraw-Hill Companies (Canada) Corp.	Financial Services	Nova Scotia, Canada	100

S&P Ratings Services Business Units / Departments



STANDARD & POOR'S

Managerial Structure – Standard & Poor's Ratings Services



Notes:

1. Direct report to Senior Vice President, Finance & Administration, Standard & Poor's
2. Direct report to Senior Vice President, Technology, Standard & Poor's
3. Direct report to McGraw-Hill Legal; does not report to Ratings Services
4. Direct report to Senior Vice President Global Regulatory Affairs & Compliance, Standard & Poor's
5. Direct report to Senior Vice President, Marketing & Communications, Standard & Poor's
6. Direct report to Vice President, Human Resources, Standard & Poor's
7. Direct report to McGraw-Hill Legal

STANDARD & POOR'S

S&P Ratings Services – Locations Where Ratings Issued

U.S. and Canada	Latin America	Europe	Asia Pacific
New York, NY	Mexico City, Mexico	London, England	Melbourne, Australia
Boston, MA	Buenos Aires, Argentina	Paris, France	Hong Kong
Chicago, IL	Sao Paulo, Brazil	Frankfurt, Germany	Singapore
Dallas, TX		Milan, Italy	Tokyo, Japan
San Francisco, CA		Madrid, Spain	
Toronto, Canada		Stockholm, Sweden	
		Moscow, Russia	

STANDARD
&POOR'S

Ref.: CESR/07-835

Vickie A. Tillman
Executive Vice President of Credit Market Services
Standard & Poor's
55 Water Street
New York
NY 10041-0003
USA

Stockholm, 11 December 2007

Dear Ms Tillman,

Following your letter dated 5 December 2007 enclosing your public responses to the request of information submitted by CESR on 14 November and making the provision of the confidential responses conditional upon CESR agreeing to a number of requests, I would like to clarify the following aspects.

Firstly, the deadline for submissions of the responses (both public and confidential ones) has already expired. As you know, the deadline was initially set for 26 November and then, following your request, extended to 30 November. Your response, including only the public answers, was received on 5 December.

Secondly, in relation to your request of clarification of our confidentiality policy, I would like to remind you that our policy on confidentiality was already explained to you in my letter of 14 November and had previously been anticipated in an email sent on 5 November: *"As we understand that you may have some difficulties in making some of the requested information public, we would kindly ask you to identify those answers that you would prefer to keep confidential.* ***CESR won't be publishing those responses although we might include in the report some aggregated data in relation to those issues.*** *Nevertheless, we do intend to publish all the questions attached and we will be highlighting the answers as confidential if we are not authorised to publish them. Please note that some responses might be treated as confidential by some agencies and not by others".*

Besides, I would like to make clear that for the preparation of its report CESR does not restrict the circulation of the information among its members or the observers of the task force (European Commission and CEBS). Having said this, I can inform you that staff of our members (who are persons employed by national regulators) are bound by professional secrecy by their national legislation and that the members of CESR Secretariat are also bound by professional secrecy in accordance with art. 7.4 of the CESR Charter (accessible at our website).

Finally, I would like to inform you that in our report we will explain what impact the lack of response from S&P to certain questions has on CESR's ability to describe the issues, to draw conclusions on them and on our overall final advice to the European Commission.

Yours sincerely,

Ingrid Bonde