

# MOODY'S

## INVESTORS SERVICE

### CREDIT ANALYSIS

## Manitoba, Province of

Canada

#### Table of Contents:

SUMMARY RATING RATIONALE	1
NATIONAL AND INTERNATIONAL PEER COMPARISONS	1
RATING OUTLOOK	1
KEY RATING CONSIDERATIONS	2
Financial Position and Performance	2
Debt Profile	3
Governance and Management Factors	4
Economic Fundamentals	4
Operating Environment	5
Institutional Framework	5
Application of Joint-Default Analysis	5
RATING HISTORY	6
ANNUAL STATISTICS	7
MOODY'S RELATED RESEARCH	10

#### Analyst Contacts:

TORONTO 1.416.214.1635

Jennifer A. Wong 1.416.214.3854  
*Assistant Vice President-Analyst*  
 Jennifer.Wong@moodys.com

NEW YORK 1.212.553.1653

Debra Roane 1.212.553.7815  
*Vice President-Senior Credit Officer*  
 Debra.Roane@moodys.com

LONDON 44.20.7772.5454

David Rubinoff 44.20.7772.1398  
*Team Managing Director*  
 David.Rubinoff@moodys.com

This Credit Analysis provides an in-depth discussion of credit rating(s) for the Province of Manitoba and should be read in conjunction with Moody's most recent Credit Opinion and rating information available on [Moody's website](http://www.moodys.com).

#### Summary Rating Rationale

The Province of Manitoba's Aa1 rating reflects the province's sound fiscal plan, which has produced generally balanced fiscal outcomes in recent years. While moderate cash requirements have increased the province's stock of debt, additions to debt have been broadly in line with economic and revenue growth, keeping the province's debt burden relatively stable. The province's fiscal flexibility is high and the proportion of revenue consumed by interest payments remains low at an estimated 5.9% in 2009-10. The Aa1 rating is also supported by the province's diversified economy, which tends to underperform the Canadian average in boom years, but outperform in years of weak economic conditions, providing a measure of stability.

#### National and International Peer Comparisons

The Province of Manitoba is rated in the mid-range of Canadian provinces, whose ratings remain in a narrow range of Aaa-Aa2. Manitoba's debt burden, while higher than that of some of its Western Canadian peers, remains below the Canadian median. Moreover, the province's diversified economy and resulting stability positions the province well relative to Canadian peers. On an international basis of comparison, Manitoba benefits from a higher degree of fiscal flexibility than many of its international sub-sovereign peers—including the highly-rated Australian states and German Länder—owing to the institutional framework within which Canadian provinces operate, supporting the high investment-grade rating.

#### Rating Outlook

The outlook is stable.

## Key Rating Considerations

### Financial Position and Performance

#### Strong and Stable Fiscal Results in Recent Years

Manitoba recorded a series of positive consolidated fiscal outcomes in recent years, owing to the province's containment of expense growth below revenue growth in most years. Between 2004-05 and 2008-09, consolidated surpluses averaged 4.3% of revenue, or 1.1% of GDP. As such, Manitoba's record of strong fiscal performance positioned the province well as the Canadian economy entered the recent downturn.

Manitoba's economic outperformance in 2008 relative to Canada was reflected in the province's 2008-09 fiscal results. While both revenue and expense growth slowed to 3.8% and 4.9% respectively, the province recorded a consolidated surplus of C\$470 million, equivalent to 3.6% of revenue or 0.9% of GDP. This is in contrast to other provinces, whose finances were hit harder by the impacts of the downturn. On a cash basis of accounting, the consolidated surplus in 2008-09 translated into a financing requirement of C\$440 million, or 3.4% of revenue (0.9% of GDP). This reflects primarily the accrual accounting presentation and the difference between amortization and cash outlays required for capital expenditures.

#### Some Deterioration but Expected to Return to Balance by 2014-15

The Manitoba economy recorded a small contraction in 2009 and in the fiscal year 2009-10, revenues were estimated to have contracted by 3.2% over the previous year, owing primarily to declines in tax receipts. Total expenses were estimated to have risen by 4.9%, resulting in a projected consolidated deficit of C\$555 million in 2009-10, equivalent to about 4.4% of revenues or 1.1% of GDP.

The 2010-11 Budget projected a slight narrowing of the deficit to C\$545 million in 2010-11 as revenues start to recover along with the economy. The Budget also outlined the province's plan to return to balance by 2014-15. Concomitantly, the provincial government has made amendments to its balanced budget legislation in order to extend the period required to get back to balance to five years.<sup>1</sup> Revenue growth over the projection period is forecast to average 2.9%, while expenses are projected to grow by 1.8% over the same period. Expense growth restraint appears ambitious in light of recent experience as expenses grew at an estimated average annual growth rate of 6.2% from 2007-08 to 2009-10.<sup>2</sup> While the province has stated that expense restraint measures will include managing salary costs, reducing discretionary spending and prioritization of expenditures, specific measures have not yet been clearly outlined, and we will continue to monitor the province's progress in its consolidation plans. Nonetheless, Manitoba has a strong track record of fiscal prudence and is expected to continue with these fiscal management practices.

<sup>1</sup> The amendments to the *Balanced Budget, Fiscal Management and Taxpayer Accountability Act* specify an "economic recovery period" from April 1, 2010 to March 31, 2014 at the latest, after which the legal requirement to have balanced budgets is retained.

<sup>2</sup> This figure adjusts for the consolidation of school boards in 2007-08.

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## Debt Profile

### Debt Ratios Rising Moderately but Still Manageable

While the province's net direct and indirect debt is estimated to have risen to approximately C\$14 billion at March 31, 2010 from roughly C\$10 billion at March 31, 2005, this has roughly matched the growth in nominal GDP and provincial revenues. As a percentage of GDP, net direct and indirect debt remained relatively stable, hovering around 25% between 2004-05 to 2009-10, while this measure of debt as a percentage of revenue grew marginally over this period. Though debt has increased somewhat recently and is expected to increase over the near term, these debt ratios are considered manageable for Manitoba given the high degree of fiscal policy flexibility inherent in the institutional framework governing the way Canadian provinces operate.

The province's debt affordability remains high, as evidenced by the declining proportion of revenues consumed by interest costs, which declined to 5.9% in 2009-10 from 7.6% in 2004-05, largely as a result of lower interest rates. In the early years of the current decade, this ratio measured over 12%. This improvement in debt affordability illustrates the province's heightened shock-absorption capacity.

Foreign currency exposure has been eliminated on the province's debt portfolio for all but debt associated with Manitoba Hydro (discussed below). Manitoba Hydro, by virtue of its exports of hydroelectric power to the United States, has a natural hedge against USD-CAD currency fluctuations. Floating rate exposure, excluding short-term instruments and current maturities, was roughly 10% at March 31, 2010.

### Significant Borrowing for Manitoba Hydro, but Self-Supported

Roughly one third of the province's total direct and indirect debt is attributed to Manitoba Hydro and is considered to be self-supporting. This Crown Corporation's ability to meet its own financial obligations without recourse to provincial subsidies is a positive credit attribute for the province. In our view, the likelihood that the contingent liability represented by Manitoba Hydro's debt would materialize remains relatively remote.

Manitoba Hydro is currently planning for significant future capital expenditures with a view to increasing its generation and transmission capacity to meet domestic demand as well as to exploit export opportunities over the next 25-30 years. These projects include the 200MW Wuskwatim Generating Station, which has an estimated total capital cost of C\$1.6 billion (including the generation and transmission components) and is scheduled to come into service in December 2011. Other projects include the larger Keeyask (695MW) and Conawapa (1,485 MW) generating stations, with in-service dates estimated at 2018 (earliest) and 2022 respectively, as well as the construction of a third high voltage direct current line (Bipole III), targeted to be in service in 2017/18. The Bipole III line would allow power to be carried from new generation stations to southern parts of the province and to export markets. Manitoba Hydro intends to cover base capital expenditures with internally-generated funds from operations and to use external debt financing to fund expansion projects, requiring significant new debt financing over the next decade. We will continue to monitor developments with Manitoba Hydro's capital plan to ensure that our conclusion regarding the self-supporting status of the utility's debt remains appropriate.

### Province Addressing Pension Liabilities

In 2007-08, the province debt-financed C\$1.5 billion of the Teachers' Retirement Allowance Fund (TRAF) unfunded liability. Investments held for the TRAF and the Civil Service Superannuation Fund (CSSF), which totaled C\$2.2 billion in 2007-08, were reclassified and irrevocably restricted for pension purposes in 2008-09. As a result of the debt-funding of pension liabilities, the province's unfunded pension obligations declined to an estimated C\$1.8 billion at the end of 2009-10 (14.5% of revenue), from C\$3.3 billion at March 31, 2004 (32.9% of revenue). The government expects to continue this policy of debt-funding pension liabilities. We consider unfunded pension liabilities as debt-like and take them into account when establishing a government's credit profile. As such, we view Manitoba's debt-funding of unfunded pension liabilities as credit-neutral.

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### Governance and Management Factors

Manitoba, over the past several years, has relied on multi-year fiscal planning, prudent economic and revenue assumptions and ongoing expense restraint to maintain a strong financial profile. Overall, Manitoba displays strong governance and management factors. Fiscal management measures are supported by comprehensive and transparent financial reporting that is typical of governments in advanced industrial economies.

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### Economic Fundamentals

#### Diverse Economy and Stable Growth Strengthen Credit Profile

The Manitoba economy is highly diversified, which helps to reduce economic volatility associated with business cycles and certain specific local industries. The service sector—including finance and insurance, real estate, public administration and transportation—accounts for over 70% of real economic output, contributing to the province's overall economic diversity.

Manufacturing accounts for the largest share of the goods-producing sector, representing 11% of real GDP. The recent economic slowdown proved a considerable challenge for the Canadian manufacturing industry, with manufacturing output declining by about 12% in 2009. Manitoba's manufacturing sector, however, fared slightly better than the national average, recording a contraction of around 9%. The nature of Manitoba's manufacturing sector, which includes niche areas such as aerospace and transit buses, and its high level of diversification have helped it face difficult external conditions.

After underperforming the national average through the first part of the last decade (which saw relatively strong economic growth in Canada), real GDP declined 0.9% in 2009, outperforming the national average (contraction of 2.5%). Manitoba is less exposed to the US economy than most Canadian provinces; the province's exports to the United States account for approximately 67% of its foreign exports, compared to approximately 75% for the Canadian economy as a whole. As a result, the province was less affected by the recent US slowdown than Ontario or Quebec, which are more exposed to the health of the US economy. In further contrast to other provinces, Manitoba was one of only three provinces to record gains in employment, albeit modest, in 2009.

The Manitoba economy tends to underperform the Canadian economy in times of rapid economic growth and to outperform in economic slowdowns. The province's high degree of economic diversity—which implies the absence of a dominant sector that could act as a catalyst for growth in boom years and represent a drag on the provincial economy in recessions—is one factor that could

explain these trends. The province's economic diversity represents a major source of credit strength, ensuring a broad and productive tax base for the government.

As with the other provinces and the Canadian economy as a whole, Manitoba's economy is expected to resume growth in 2010 (provincial forecasts project growth of 2.5%). Though unemployment ticked up in 2009, Manitoba's labour market remains relatively tight as the 2009 unemployment rate of 5.2% was one of the lowest in the country and well below the national average of 8.3%. The population and labour force also continue to expand through net in-migration, particularly international immigration.

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### Operating Environment

The national operating environment in which Manitoba operates is typical of advanced industrial economies, characterized by high GDP per capita, low GDP volatility and a high ranking on the World Bank's Government Effectiveness Index, all of which suggest a minimal level of systemic economic, financial and political risk. As evidenced by Canada's record of continued economic expansion and political stability, the macroeconomic environment is robust and federal government institutions are responsive. Accordingly, the conditions that have historically preceded national crises associated with widespread defaults of regional and local governments are not present in Canada.

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### Institutional Framework

The Province of Manitoba, like all Canadian provinces, enjoys significant flexibility in its financial management. Compared to their counterparts in other countries, such as the German Länder and the Australian states, Canadian provinces enjoy far greater autonomy in terms of both the spending and revenue sides of their budgets. Unfettered access to a broad range of tax bases and the ability to alter expenditure programs provide Canadian provinces with substantial flexibility to meet fiscal challenges. As such, Canadian provinces benefit from a high degree of fiscal policy flexibility that is more akin to that of sovereign governments than to many of their international sub-sovereign peers. These positive institutional factors increase Canadian provinces' ability to manage through economic downturns and handle relatively high debt burdens. In conjunction with the high degree of fiscal flexibility, a system of fiscal transfers from the federal government, which seeks to reduce the fiscal disparities across the country, also provides support to Canadian provinces' creditworthiness.

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### Application of Joint-Default Analysis

The Aa1 rating assigned to Manitoba reflects the application of Moody's joint-default analysis methodology for regional and local governments. The province's rating is composed of two principal inputs: a baseline credit assessment of 3 (on a scale of 1-21, in which 1 represents the lowest level of credit risk) and a very high likelihood of extraordinary support from the federal government (rated Aaa, stable) to prevent a default by Manitoba, or any province. The very high likelihood of support reflects Moody's assessment of the incentive provided by the risk to the federal government's reputation if Manitoba, or any province, were to default, as well as indications of a moderately positive national government policy stance, as illustrated by the flexibility inherent in the system of federal provincial transfers.

## Rating History

### Province of Manitoba

DATE	RATING
November 2006	Aa1
January 2003	Aa2
September 1998	Aa3
May 1985	A1
September 1975	Aa
October 1968	A

## Annual Statistics

<b>Province of Manitoba</b>					
<b>DEBT STATEMENT (C\$ MILLIONS, AS AT 3/31)</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010F</b>
Treasury Bills and Promissory Notes	325	325	850	1,185	1,500
Canada Pension Plan	756	606	597	492	480
Direct Debentures	18,237	18,923	20,252	20,906	22,314
Other	1,021	1,047	756	742	358
<b>Total Direct Debt</b>	<b>20,339</b>	<b>20,901</b>	<b>22,455</b>	<b>23,325</b>	<b>24,652</b>
<b>Guaranteed Debt</b>					
Manitoba HydroBonds and Promissory Notes	485	670	347	398	251
Other Guarantees	83	87	94	92	102
<b>Total Direct and Indirect Debt</b>	<b>20,907</b>	<b>21,658</b>	<b>22,896</b>	<b>23,815</b>	<b>25,005</b>
Less:					
Manitoba Hydro	6,625	6,640	7,142	7,836	8,289
Manitoba HydroBonds and Promissory Notes	485	670	347	398	251
Direct Debt Sinking Fund	3,918	4,118	3,334	2,741	2,582
<b>Net Direct and Indirect Debt</b>	<b>9,879</b>	<b>10,230</b>	<b>12,073</b>	<b>12,840</b>	<b>13,883</b>
<b>DEBT TRENDS (AS AT 3/31)</b>					
Net Direct and Indirect Debt (C\$ millions)	9,879	10,230	12,073	12,840	13,883
As % GDP	23.7	22.7	24.8	25.3	27.7
As % Personal Income	29.3	28.7	31.8	32.0	34.2
Per Capita (C\$)	8,384	8,640	10,116	10,647	11,361
As % Total Revenues	92.1	93.7	97.1	99.4	111.0
Total Direct and Indirect Debt	20,907	21,658	22,896	23,815	25,005
% Hydro Debt	31.7	30.7	31.2	32.9	33.1
Total Foreign Currency Debt (Before Hedges)	5,672	6,286	5,890	6,178	5,158
As % Total Direct and Indirect Debt	27.1	29.0	25.7	25.9	20.6
Foreign Currency Debt Net of Hedges (C\$ Millions)	2,838	2,804	2,706	3,005	2,426
As % Total Direct and Indirect Debt	13.6	12.9	11.8	12.6	9.7
Short-Term Debt	2247.0	1941.0	3118.0	3364.0	3141.0
As % of Total Direct and Indirect Debt	10.7	9.0	13.6	14.1	12.6
Actuarial Pension Liability (Surplus) (C\$ millions)	3,430	3,460	2,300	2,003	1,813
As % of GDP	8.2	7.7	4.7	3.9	3.6
As % of Revenue	32.0	31.7	18.5	15.5	14.5
Total Employer Cash Contributions [1]	319	426	1,976	155	466
As % of Revenue	3.0	3.9	15.9	1.5	3.7

[1] In 2008 this includes a special contribution of C\$1.5 billion, which was borrowed in the capital markets by the province to fund pension plans.



**Province of Manitoba****CONSOLIDATED REVENUES AND EXPENSES  
(C\$ MILLIONS, YEAR ENDING 3/31)**

	2007	2008	2009	2010F	2011B
<b>Revenues</b>					
Personal Income Tax	2,130	2,285	2,455	2,654	2,421
Corporate Income Tax	311	367	386		247
Payroll Tax (Health and Education)	318	341	357		282
Retail Sales Tax	1,277	1,391	1,486		1,669
Net Income of Government Business Enterprises	627	946	807	687	699
Federal Transfers	3,317	3,597	3,866	4,072	4,126
Other	2,940	3,510	3,558	5,089	3,278
<b>Total Revenues</b>	<b>10,920</b>	<b>12,437</b>	<b>12,915</b>	<b>12,502</b>	<b>12,720</b>
<b>Expenses</b>					
Health	4,005	4,224	4,586	4,851	5,085
Family Services and Housing	1,142	1,224	1,321	1,321	1,326
Education	2,397	3,218	3,154	3,240	3,419
Community, Economic and Resource Development	1,280	1,406	1,582	1,834	1,819
Debt Service	835	815	830	739	767
Other	831	974	972	1,072	848
<b>Total Expenses</b>	<b>10,490</b>	<b>11,861</b>	<b>12,445</b>	<b>13,057</b>	<b>13,264</b>
<b>Consolidated Surplus/(Deficit)</b>	<b>430</b>	<b>576</b>	<b>470</b>	<b>(555)</b>	<b>(545)</b>
<b>Cash Financing Surplus/(Requirement)</b>	<b>365</b>	<b>(560)</b>	<b>(440)</b>	<b>(913)</b>	<b>(1,317)</b>

<b>FINANCIAL TRENDS (YEAR ENDING 3/31)</b>	2006	2007	2008	2009	2010F
% Change in Revenue	6.8	1.8	13.9	3.8	(3.2)
As a % of Revenue					
Consolidated Surplus (Deficit)	3.5	3.9	4.6	3.6	(4.4)
Cash Financing Surplus (Requirement)	(1.7)	3.3	(4.5)	(3.4)	(7.3)
Interest Expense	7.4	7.6	6.6	6.4	5.9
Intergovernmental Transfers	28.9	30.4	28.9	29.9	32.6
% Change in Expenses	9.6	1.4	13.1	4.9	4.9
As a % of Expenses					
Health	37.2	38.2	35.6	36.9	37.2
Education	22.9	22.9	27.1	25.3	24.8
Interest Expense	7.6	8.0	6.9	6.7	5.7
As a % of GDP					
Revenues	25.8	24.3	25.5	25.7	24.9
Expenses	24.9	23.3	24.3	24.7	26.0
Consolidated Surplus (Deficit)	0.9	1.0	1.2	0.9	(1.1)
Cash Financing Surplus (Requirement)	(0.4)	0.8	(1.1)	(0.9)	(1.8)
Health Expenses	9.3	8.9	8.7	9.1	9.7
Expenses Per Capita (C\$)	8,784	8,860	9,938	10,319	10,685



**Province of Manitoba**

<b>ECONOMIC TRENDS (YEAR ENDING 12/31)</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
Population in 1000s	1,178	1,184	1,194	1,206	1,222
Real GDP (2002 C\$ millions)	38,603	39,880	41,394	42,079	41,685
% Growth	2.0	3.3	3.8	1.7	-0.9
Nominal GDP (C\$ millions)	41,512	44,957	48,727	50,324	50,200
% Growth	4.4	8.3	8.4	3.3	-0.2
Personal Income (C\$ millions)	33,705	35,600	38,024	40,198	40,597
Per Capita (C\$)	28,605	30,067	31,859	33,332	33,222
As % Canadian Average	89.2	88.5	89.3	90.7	91.2
Personal Disposable Income (C\$)	26,386	28,028	29,841	31,911	32,393
As % Personal Income	78.3	78.7	78.5	79.4	79.8
Employment Growth (%)	0.6	1.2	1.6	1.7	0.0
Participation Rate	68.6	68.8	69.4	69.6	69.4
Unemployment Rate	4.8	4.3	4.4	4.2	5.2
Manufacturing Shipments (C\$ millions)	13,688	14,862	16,168	16,378	14,568
Housing Starts (units)	4,731	5,028	5,738	5,537	4,174
Retail Sales (C\$ millions)	12,372	12,874	14,016	14,980	14,915
Per Capita (C\$)	10,500	10,873	11,743	12,421	12,205
CPI, All Items	106.6	108.7	110.9	113.4	114.1
Inflation Based on CPI % Change	2.7	2.0	2.0	2.3	0.6

## Moody's Related Research

### Credit Opinion:

- » [Canada, May 2010](#)

### Special Comments:

- » [Canadian Provinces: Conditions Remain Challenging, February 2010 \(122837\)](#)
- » [Moody's 2010 Outlook for Sub-Sovereigns, January 2010 \(121563\)](#)

### Statistical Handbook:

- » [Non-U.S. Regional and Local Governments, June 2010 \(125279\)](#)

### Rating Methodologies:

- » [Regional and Local Governments Outside the US, May 2008 \(107844\)](#)
- » [The Application of Joint-Default Analysis to Regional and Local Governments, December 2008 \(99025\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not

Report Number: 126909

**Authors**Jennifer A. Wong  
Aaron Wong**Production Associate**

Amanda Ealla

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