

## **Rating Action: Moody's downgrades Assured Guaranty; lead insurer to A2**

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New York, January 17, 2013 -- Moody's Investors Service has downgraded the Insurance Financial Strength (IFS) rating of Assured Guaranty Municipal Corp. (AGM) to A2 from Aa3, the IFS rating of Assured Guaranty Corp. (AGC) to A3, from Aa3, and the IFS rating of Assured Guaranty Re Ltd. (AGRe) to Baa1 from A1. In the same rating action, Moody's also downgraded the senior unsecured debt ratings of both Assured Guaranty US Holdings Inc. and Assured Guaranty Municipal Holdings Inc., to Baa2, from A3. The outlook for the ratings is stable. A full list of rating actions on Assured Guaranty Ltd. (Assured) and its subsidiaries is provided below. The rating action also has implications for the various transactions wrapped by AGM and AGC as discussed later in this press release.

### **SUMMARY RATIONALE**

"Today's rating action reflects Moody's downward reassessment of Assured's business franchise, expected future profitability, and financial flexibility," said Moody's. "Assured operates in an industry that has not recovered from the financial crisis and, like its peers, will continue to struggle in the face of declining fundamentals, including a dramatic reduction in insurance usage, modest profitability and still-meaningful legacy risk."

While the characteristics of Assured's insured portfolio's credit quality and its capital adequacy generally remain strong (based on the data from September 30, 2012), Assured's positioning on key dimensions of financial strength, namely franchise strength, profitability, and financial flexibility have weakened over time largely as a result of enduring changes in the financial guarantor industry and the broader economic environment as discussed in greater detail in previous Moody's publications.

The combination of these characteristics, along with some residual uncertainty with respect to the potential for outsized losses relative to capital in the existing insured portfolio as well as more general unknowns with respect to future insured portfolio production and capital retention, lead to the overall A2 IFS rating assessment of the lead operating company.

### **RATING RATIONALE -- ASSURED GUARANTY MUNICIPAL CORP.**

We have positioned the IFS rating of Assured Guaranty Municipal Corp. (AGM, formerly Financial Security Assurance Inc.) at A2. As the principal active operating insurer within the Assured group, AGM is a key focus for our analysis of the consolidated group and an important reference point for our ratings of AGC and AGRe, entities whose underwriting profile has been sharply reduced in recent years. Moody's approach to rating the company is outlined in "Moody's Rating Methodology for the Financial Guaranty Insurance Industry", published in September 2006 and as further described in previous reports on the sector, including "Financial Guaranty Insurance: Frequently Asked Questions" (September 2012) and "The Changing Business of Financial Guaranty Insurance" (November 2008). Our methodology centers on an assessment of five key factors (outlined below), focusing on financial and operational metrics that are considered together with qualitative assessments and analyst judgment.

**Factor 1: Franchise Value and Strategy** -- Moody's assessment of this factor balances AGM's position as the sole active financial guarantor to survive the 2007-2009 US financial crisis intact against the dramatic decline of the industry. Structured finance business, which accounted for a meaningful portion of AGM's pre-crisis activity, has virtually disappeared. The target market for insuring US public finance issuance (now primarily mid-to-low investment grade municipal bonds) has also declined, and is now less than one-third its size in 2006. While AGM benefits from its position as the most active player in a smaller industry, its overall business activity, as measured by the present value of gross premiums written, remains well below pre-crisis levels. The secular narrowing of its business opportunities, and related pressure on value creation result in our low investment-grade (Baa) assessment of this rating factor.

**Factor 2: Insurance Portfolio Characteristics** -- AGM's insured portfolio is somewhat bifurcated from a risk perspective, with a historically low-loss core municipal book as well as exposure to certain sectors and credits experiencing material credit stress. Based on Assured's internal ratings, the portion of AGM's 3Q2012 insured net par outstanding considered below investment grade was roughly 3.3%. Under Moody's scenario analyses, AGM's credit risk ratio (expected loss) and tail risk ratio (stress case loss) were also consistent with a high investment-

grade score for this factor. In developing these estimates, certain adjustments were made to input parameters for Moody's Portfolio Risk Model to account for the 2010 recalibration of Moody's US public finance ratings to the global scale. However, the portfolio does have material exposure to legacy mortgage-related risks, which are highly sensitive to weakness in the macroeconomic environment, and large risks among individual municipal credits. We therefore consider the company's portfolio characteristics score to be in the A rating range.

**Factor 3: Capital Adequacy** -- Our assessment of AGM's point-in-time capital adequacy is very strong, reflecting the relative emphasis on municipal risks as well as loss-mitigation activities related to RMBS. Based on our base case estimated loss distribution, AGM holds claims-paying resources sufficient to cover losses at a confidence level corresponding to a high Aa score. In this analysis, insured RMBS and certain other stressed exposures are excluded from our Portfolio Risk Model, in order to allow for a separate detailed loss assessment of those transactions. Potential losses estimated for these stressed exposures are then combined with the modeled losses on remaining exposures to derive an aggregate loss distribution for the overall portfolio. However, estimates of capitalization can vary considerably based on underlying assumptions about default probability, loss-given default, and correlation. This kind of variability leads us to assess capitalization somewhat more conservatively than modeling might suggest, but still in the Aa range for this factor.

**Factor 4: Profitability** -- AGM sustained large losses during the financial crisis as a result of claims related to mortgage securitizations. However, profitability has rebounded in recent periods. For the three years ended December 31, 2011, AGM recorded an average statutory return on equity of 15.7%, aided by representation and warranties recoveries from mortgage originators and sponsors of RMBS. Profitability has also been enhanced by large opportunistic purchases of AGM-insured RMBS securities at deep discounts, which are financially beneficial but suggest a lack of investor confidence. Evaluated over longer time horizons, however, profitability has weakened notably, with 5-year and 10-year average statutory returns on equity at 0.5% and 6.8%, respectively, which lags those of its specialty insurance and reinsurance peers and, given the low levels of new business production, we believe AGM's profitability will remain under pressure. Consequently, Moody's views AGM's profitability to be consistent with a score in the single-A range.

**Factor 5: Financial Flexibility** -- AGM's financial leverage is characterized by a relatively modest debt load, and operating earnings coverage has been relatively strong over the past three years. As with profitability, however, earnings coverage is weaker when a longer time frame (e.g. five years) is considered. More importantly, in our view, various market indicators (such as the firm's low stock price relative to operating book value per share, and its elevated CDS spreads) suggest that the firm's financial flexibility in accessing new funds on a cost-effective basis could be quite constrained. For these reasons, we score AGM's financial flexibility in the Baa range.

#### WHAT COULD CHANGE THE RATING UP OR DOWN

The main rating sensitivities for AGM relate to the composition and performance of its insured portfolio as well as its capitalization and market support. The rating could be lowered if the quality of its insured portfolio meaningfully decreased or capital was withdrawn without an associated reduction of risk, or if profitability reduced materially. The rating could be upgraded if there were a significant rebound in business origination at attractive pricing levels and financial flexibility improved. However, fundamental challenges inherent in the business model make a return to the Aa rating level unlikely.

The A2 IFS ratings of Assured Guaranty (Bermuda) Ltd. and Assured Guaranty (Europe) Ltd. reflect a combination of formal and implicit support from AGM. The Baa2(hyb) ratings of Sutton Capital Trusts I-IV reflect the subordinated nature of the perpetual preferred stock of AGM that can be delivered to the trusts; AGM has an option to sell such securities to the Trusts at its sole discretion at any time.

#### RATING RATIONALE -- ASSURED GUARANTY CORP.

The A3 IFS ratings of Assured Guaranty Corp. (AGC) and its supported affiliate, Assured Guaranty (UK) Ltd., are positioned one notch below the A2 IFS rating of AGM reflecting its more limited stand alone franchise, as well as its weaker capital profile, insurance portfolio characteristics and profitability metrics. The Baa3(hyb) ratings of Woodbourne Capital Trusts I-IV reflect the subordinated nature of the perpetual preferred stock of AGC that can be delivered to the trusts; AGC has an option to sell such securities to the Trusts at its sole discretion at any time. Rating sensitivities for AGC are similar to those described above for AGM.

#### RATING RATIONALE -- ASSURED GUARANTY RE

The Baa1 IFS rating of Assured Guaranty Re Ltd. and its supported subsidiaries, Assured Guaranty Re Overseas Ltd. and Assured Guaranty Mortgage Insurance Company, is one notch below the A3 IFS rating of AGC and two

notches below the A2 IFS rating of AGM and reflects its limited independent franchise, its weaker relative capital profile, the more flexible Bermudian regulatory environment relative to the U.S., and its role as internal group reinsurer, optimizing the risk profile of its affiliated primary insurance writers. Rating sensitivities for AGRe are similar to those described above for AGM and AGC.

#### RATING RATIONALE -- SENIOR DEBT AND ISSUER RATINGS

The Baa2 senior unsecured debt rating of Assured Guaranty Municipal Holdings Inc. (AGM Holdings) is positioned at three notches below the IFS rating of its core operating subsidiaries to reflect the structural subordination of the parent companies relative to the operating companies. The three notch difference between AGM and AGM Holdings reflects the typical notching practice for U.S. insurance holding company structures.

The Baa2 senior unsecured debt rating of Assured Guaranty US Holdings Inc. (AG US Holdings) is aligned with that of AGM Holdings, reflecting its access to the financial resources of AGC, as well as subordinated access to those of AGM Holdings. The debt of AG US Holdings also benefits from a guarantee from Assured Guaranty Ltd.

The Baa2 issuer rating of Assured Guaranty Ltd. reflects its status as the ultimate parent company of the group with direct access to dividends from Assured Guaranty Re, which has substantial dividend capacity, as well as subordinated access to the resources of both AGM and AGC through intermediate holding companies. The provisional ratings of Assured Guaranty Capital Trusts I and II are aligned with the provisional subordinated debt ratings of their sponsor, Assured Guaranty Ltd.

The primary rating sensitivity of AGM Holdings, AG US Holdings and Assured Guaranty Ltd. is to the financial strength of the underlying operating companies and thus their ratings are likely to be positively/negatively impacted by upgrades/downgrades at AGM, AGC and AGRe.

#### RATINGS LIST

Issuer: Assured Guaranty (Bermuda) Ltd.

..Downgrades:

....Insurance Financial Strength, Downgraded to A2 from Aa3

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty (Europe) Ltd.

..Downgrades:

....Insurance Financial Strength, Downgraded to A2 from Aa3

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty (UK) Ltd

..Downgrades:

....Insurance Financial Strength, Downgraded to A3 from Aa3

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Capital Trust I

..Downgrades:

....Pref. Stock Shelf, Downgraded to (P)Baa3 from (P)Baa1

..Outlook Actions:

....Outlook, Changed To Stable

Issuer: Assured Guaranty Capital Trust II

..Downgrades:

....Pref. Stock Shelf, Downgraded to (P)Baa3 from (P)Baa1

..Outlook Actions:

....Outlook, Changed To Stable

Issuer: Assured Guaranty Corp

..Downgrades:

....Insurance Financial Strength, Downgraded to A3 from Aa3

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Ltd.

..Downgrades:

.... Issuer Rating, Downgraded to Baa2 from A3

....Multiple Seniority Shelf, Downgraded to (P)Baa2 from (P)A3

....Multiple Seniority Shelf, Downgraded to (P)Ba1 from (P)Baa2

....Multiple Seniority Shelf, Downgraded to (P)Baa3 from (P)Baa1

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Mortgage Insurance Company

..Downgrades:

....Insurance Financial Strength, Downgraded to Baa1 from A1

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Municipal Corp.

..Downgrades:

....Insurance Financial Strength, Downgraded to A2 from Aa3

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Municipal Holdings Inc.

..Downgrades:

....Junior Subordinated Regular Bond/Debenture, Downgraded to Baa3 (hyb) from Baa1 (hyb)

....Multiple Seniority Shelf, Downgraded to (P)Baa2 from (P)A3

....Multiple Seniority Shelf, Downgraded to (P)Baa2 from (P)A3

....Multiple Seniority Shelf, Downgraded to (P)Ba1 from (P)Baa2

....Multiple Seniority Shelf, Downgraded to (P)Ba1 from (P)Baa2

....Multiple Seniority Shelf, Downgraded to (P)Baa3 from (P)Baa1

....Multiple Seniority Shelf, Downgraded to (P)Baa3 from (P)Baa1

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from A3

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from A3

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from A3

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Re Ltd.

..Downgrades:

....Insurance Financial Strength, Downgraded to Baa1 from A1

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty Re Overseas Ltd.

..Downgrades:

....Insurance Financial Strength, Downgraded to Baa1 from A1

....Outlook, Changed To Stable From Rating Under Review

Issuer: Assured Guaranty US Holdings, Inc.

..Downgrades:

....Junior Subordinated Regular Bond/Debenture, Downgraded to Baa3 (hyb) from Baa1 (hyb)

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from A3

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from A3

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Sutton Capital Trust I

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa2 (hyb) from A3 (hyb)

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Sutton Capital Trust II

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa2 (hyb) from A3 (hyb)

..Outlook Actions:

....Outlook, Changed To Stable From Rating Under Review

Issuer: Sutton Capital Trust III

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa2 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

Issuer: Sutton Capital Trust IV

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa2 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

Issuer: Woodbourne Capital Trust I

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa3 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

Issuer: Woodbourne Capital Trust II

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa3 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

Issuer: Woodbourne Capital Trust III

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa3 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

Issuer: Woodbourne Capital Trust IV

..Downgrades:

....Pref. Stock Non-cumulative Preferred Stock, Downgraded to Baa3 (hyb) from A3 (hyb)

..Outlook Actions:

...Outlook, Changed To Stable From Rating Under Review

#### TREATMENT OF WRAPPED TRANSACTIONS

Moody's ratings on securities that are guaranteed or "wrapped" by a financial guarantor are generally maintained at a level equal to the higher of the following: a) the rating of the guarantor (if rated at the investment grade level); or b) the published underlying rating (and for structured securities, the published or unpublished underlying rating).

Moody's approach to rating wrapped transactions is outlined in Moody's special comment "Assignment of Wrapped Ratings When Financial Guarantor Falls Below Investment Grade" (May, 2008); and Moody's November 10, 2008 announcement "Moody's Modifies Approach to Rating Structured Finance Securities Wrapped by Financial Guarantors".

As a result of today's rating action, the Moody's-rated securities that are guaranteed or "wrapped" by AGC or AGM are also downgraded, except those with equal or higher published underlying ratings (and for structured finance securities, except those with equal or higher published or unpublished underlying ratings). For more information on affected credits please refer to the Financial Institutions page at [www.moodys.com/fig](http://www.moodys.com/fig).

The principal methodology used in these ratings was Moody's Rating Methodology for the Financial Guaranty Insurance Industry published in September 2006. Please see the Credit Policy page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

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