

Credit Analysis

United States of America

Ratings

Foreign Currency	
Long-Term IDR	AAA
Short-Term IDR	F1+
Country Ceiling	AAA
Local Currency	
Long-Term IDR	AAA

Outlooks

Foreign-Currency Long-Term IDR	Stable
Local-Currency Long-Term IDR	Stable

Financial Data

United States of America	
USDbn	2009
GDP	14,039.6
GDP per head (USD 000)	44.6
Population (m)	314.8
International reserves	301.7
Net external debt (% GDP)	41.3
Central government total debt (% GDP)	65.3
CG foreign-currency debt	0
CG domestically issued debt (USDbn)	9,170

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Related Research

Applicable Criteria

- [Sovereign Rating Methodology \(October 2009\)](#)

Other Research

- [Guide to Sovereign Credit Report \(October 2008\)](#)
- [High-Grade Sovereigns and the Global Financial Crisis \(March 2009\)](#)
- [Sovereign Credit Risk in the Aftermath - Lessons from Japan \(November 2009\)](#)
- [Fiscal Exit Strategies Key to 'AAA' Sovereign Credit Outlook \(September 2009\)](#)
- [Global Economic Outlook \(December 2009\)](#)
- [Sovereign Review and Outlook \(December 2009\)](#)

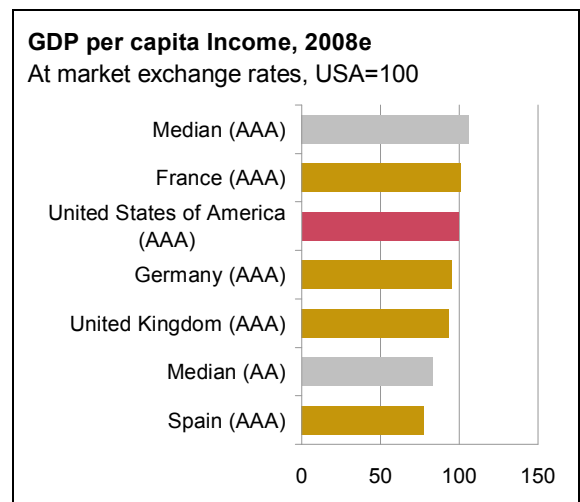
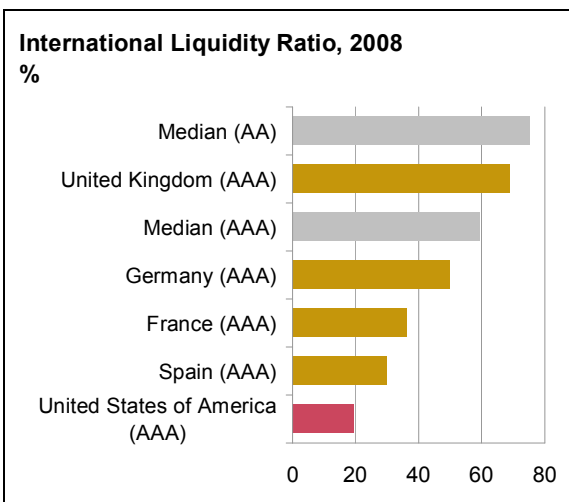
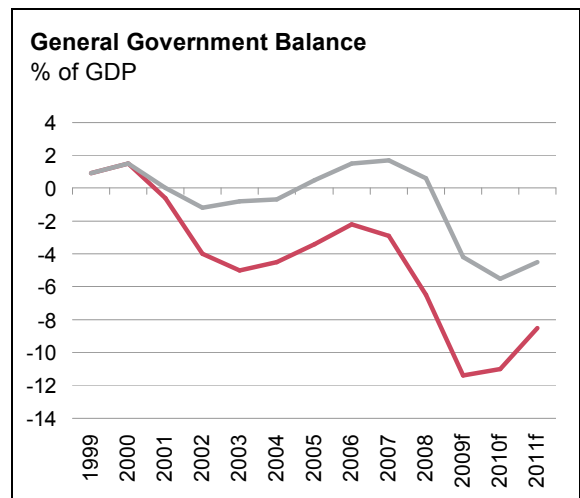
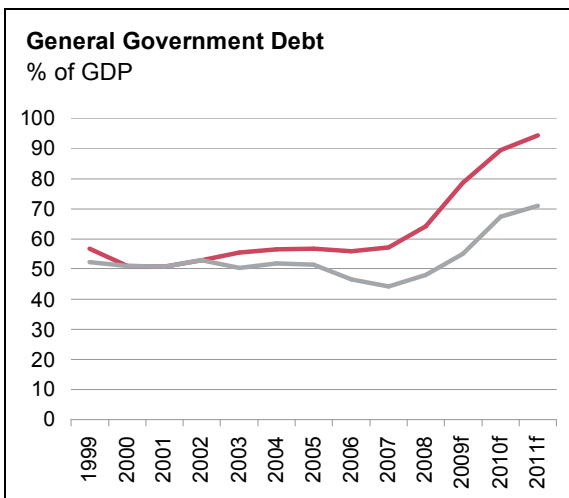
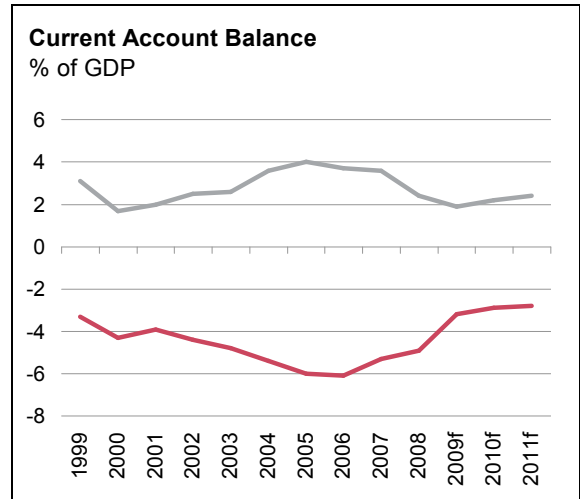
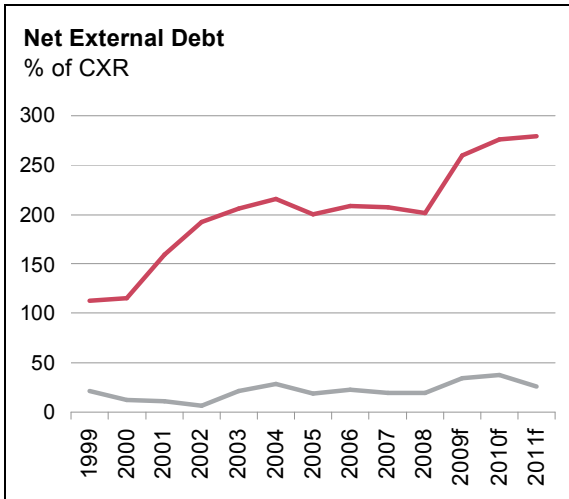
Rating Rationale

- The US government remains exceptionally creditworthy – supported by its pivotal role in the global financial system and the flexible, diversified and wealthy economy that provides its revenue base – despite an unprecedented deterioration in fiscal performance as a result of the recession, financial crisis and associated policy responses.
- The fact that US sovereign liabilities, both the dollar and government debt, remain the benchmark for financial markets across the globe gives the authorities unprecedented financing flexibility and enhances debt tolerance, even relative to other large ‘AAA’-rated sovereigns.
- This flexibility has allowed the government to take aggressive counter-crisis and counter-cyclical policy measures, which now appear to be working in terms of restoring stability to the financial sector and the economy. Over time these policy responses should work to allow the dynamism and flexibility of the economy – demonstrated over many decades – to reassert themselves again.
- However, the government faces significant medium term fiscal challenges with a sizeable structural deficit, a narrow tax base, limited expenditure flexibility and exposure to potential interest rate shocks due to the short duration and maturity of US government debt and a heavy reliance on foreign investors. Public debt on a general government (i.e. consolidated federal, state and local) basis is expected to rise to 89% of GDP in 2010 and 94% in 2011 from 79% of GDP in 2009, which would mark the highest level among ‘AAA’-rated sovereigns.
- Fitch judges there to be a sizeable structural component to the deficit that will not be eliminated by economic recovery and the unwinding of stimulus measures. Corporate taxes, in particular, collapsed in 2009 having been boosted by artificially strong financial sector profits and asset price gains prior to the recession and are unlikely to show a strong recovery. Fitch anticipates the economic recovery will be weak by the standards of previous recoveries - and less dynamic than assumed in the latest official medium term fiscal forecasts - as deleveraging continues to weigh on private sector demand.
- Public debt and debt service levels compare particularly poorly with ‘AAA’-rated peers when measured relative to fiscal revenue. General government debt to revenue was 330% at end 2009, the highest among ‘AAA’-rated sovereigns and compared to a long-run ‘AAA’ average of 118%. Debt interest is expected to exceed 10% of revenue by 2011 and is sensitive to interest rate shocks. Fiscal flexibility is also reduced by the limited scope for sizeable structural reductions in public expenditure, given low discretionary outlays and pressures on entitlement spending.
- The US’ high external debt burden, ongoing current account deficit and the large share of non-resident holdings of government debt (close to 50%) increase the potential for volatility in US asset prices. Increased foreign investor concerns about public debt sustainability or inflation risks could weaken the dollar and put upward pressure on interest rates.

Key Rating Drivers

- Significant structural fiscal policy tightening will be needed over the next three to five years to avoid government indebtedness approaching levels by the latter half of the decade that would bring pressure to bear on the US ‘AAA’ status.

Peer Comparison



— United States of America

— Medians

Rating Factors

Peer Group

Rating	Country
AAA	United States of America
	Austria
	Canada
	Denmark
	Finland
	France
	Germany
	Luxembourg
	Netherlands
	Norway
	Singapore
	Spain
	Sweden
	Switzerland
United Kingdom	
AA+	Australia
	Belgium
	Bermuda
	New Zealand

Source: Fitch

Rating History

Date	Long-Term Foreign Currency	Long-Term Local Currency
Oct 1995	AAA	AAA
Aug 1994	AAA	-

Source: Fitch

Summary: Strengths and Weaknesses

Rating factor	Macroeconomic	Public finances	External finances	Structural issues
Status	Neutral	Weakness	Weakness	Strength
Trend	Stable	Negative	Stable	Stable

Note: Relative to 'AAA' category
Source: Fitch

Strengths

- The US government has unparalleled financing flexibility as the issuer of the world's pre-dominant global reserve currency and the benchmark "risk free" borrower for global credit markets.
- The dollar accounts for two-thirds of the world's official FX reserves and over 86% of global currency trades, while US assets are equivalent to 40% of global financial assets and the economy 25% of global GDP. Liquidity in the Treasury market is more than 10 times that in large European government bond markets. The flight to dollars through the crisis and the authorities' provision of dollar liquidity to the world's other major central banks are clear evidence of the US's special status in the world financial system.
- A highly flexible and diversified economy which is able to effectively reallocate resources following shocks relatively quickly
- The record of growth and macroeconomic stability over the longer term is strong.

Weaknesses

- Public finances are weak. Extremely large fiscal deficits will drive public debt/GDP ratios to the highest levels among 'AAA's by end-2010. Moreover the government's revenue base is very low by 'AAA' standards, rendering debt and debt service burdens particularly high when measured relative to revenue. The budget is also quite sensitive to interest rate risk, thanks to a high share of short-term debt.
- The crisis revealed weaknesses in the financial system, including problems with the originate-to-distribute model of credit allocation, a fragmented financial regulation framework and the distortionary role of government-backed mortgage lenders and guarantors, Fannie Mae and Freddie Mac.
- External liabilities are high, reflecting persistent current account deficits and, in turn, low national saving rates. Continued reliance on foreign capital exposes the economy and the government to greater interest rate risk than surplus/net creditor economies such as Japan or Germany.

Local Currency Rating

There is no effective difference between the US's local- and foreign-currency creditworthiness, as the dollar remains the predominant global reserve currency. In virtually any foreseeable circumstance the US authorities would be able to exchange dollars for other major currencies to meet any FX debt service due. The entire stock of sovereign debt and 90% of GXD overall is in any case dollar denominated.

Country Ceiling

Given the dollar's pre-eminent role in global finance it is inconceivable that the authorities would seek to restrict international payment flows.

Large 'AAA' Fiscal Ratios

General government				
(% GDP)		'09	'10	'11
Deficit	US ^a	11.4	11.0	8.5
	UK	12.6	12.2	9.3
	France	8.3	8.5	7.4
	Germany	3.4	5.3	4.5
Debt	US ^a	78.6	88.9	93.6
	UK	69.1	81.0	90.3
	France	77.0	84.0	89.2
	Germany	74.8	79.2	80.2
Interest	US ^a	8.1	8.5	10.7
	(% rev.) UK	4.9	7.3	9.3
	France	6.6	6.9	7.1
	Germany	6.6	6.9	7.2

^a Calendar year
Source: Fitch

Outlook and Key Issues

US public finances are suffering their most severe deterioration since the second world war. The federal deficit was 10% of GDP in the fiscal year to end-September 2009 (FY09), the highest since 1945, and federal debt reached 53% of GDP, the highest since 1955. On a more internationally comparable general government basis, Fitch forecasts debt to rise from 64% at end-2008 to 90% of GDP at end-2010, the highest in the 'AAA' category. Undoubtedly the US's special status – as issuer of the world's dominant global reserve currency, with a hugely liquid government bond market acting as the global benchmark "risk free" interest rate – gives the authorities unparalleled financing flexibility and enhances debt tolerance relative to other large 'AAA's. This flexibility has allowed the government to take aggressive counter-crisis and countercyclical measures to support the economy and the financial system, and these appear to be taking effect.

However, while this mitigates near-term risks, it does not obviate medium-term concerns over the public finances. Little by way of medium-term fiscal consolidation measures have been set out to date and if GDP growth falls short of the optimistic rates assumed from 2011 in official projections, public debt ratios would continue to rise significantly over the medium term, absent structural fiscal tightening. Moreover, the debt and debt service burden is set to reach high levels relative to revenue by 2011, while the short maturity of public debt increases the sensitivity of the debt service burden to interest rate shocks. The depth of US asset markets limits the risk of such shocks, but the continuing shortfall of domestic savings and high share of public debt held abroad add to the risk of interest rate volatility.

The Fiscal Shock

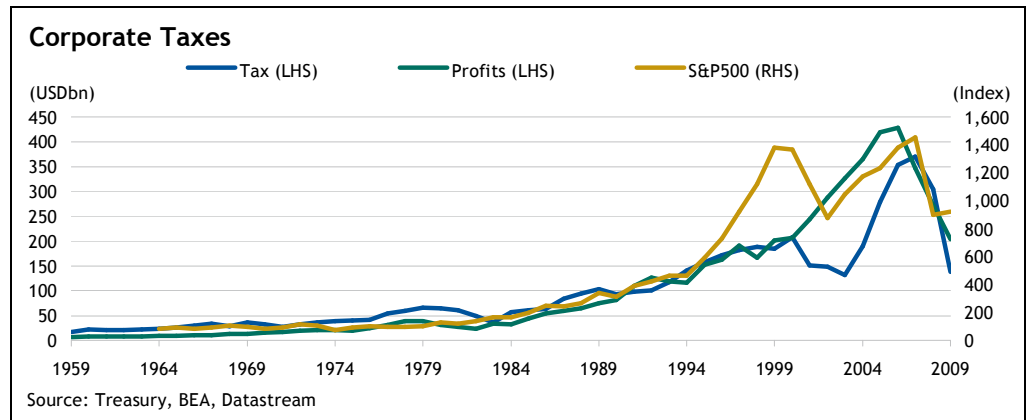
Three factors lie behind the deterioration in US public finances: the recession, outlays to support the financial sector, and the stimulus package. GDP fell by 3.8% between Q208 and Q209, the longest and deepest recession since 1950. According to the Congressional Budget Office (CBO), the economic slowdown contributed around 1.6pp to the 6.7% of GDP widening in the federal budget deficit between FY08 and FY09 through the operation of the "automatic stabilisers", with most of this cyclical deterioration coming on the revenue side.

Fiscal Support for the Financial Sector

(USDbn)	Committed	Outlays to date	Federal deficit impact ^a
TARP	700	364	154
GSE capital support	No limit	111	91
Treasury MBS purchases	No limit	314	0
Total	1,414	769	245
Total % 2009 GDP	10.1	5.4	1.8

^a FY09
Source: Treasury, CBO, Fitch

However, while part of the overall 18.2% decline in revenue reflected falling incomes, the fall was much larger than that in household and corporate incomes. Individual income taxes – which include non-wage income such as capital gains, dividends and pensions – fell by 20% compared with a decline of just 1% in wage-income-based social insurance receipts. More spectacularly, corporate taxes fell by a huge 54%, accounting for 40% of the overall decline in revenue. This was much larger than the roughly 15% decline in corporate profits as measured in the national accounts and would appear to reflect a high exposure of corporate tax receipts to the financial sector – where profits have fallen faster – and capital losses from corporate securities holdings (see chart Corporate Taxes). To the extent that financial-sector profits and asset prices had reached unsustainable levels prior to the recession, a considerable portion of these revenue losses may be permanent.



Fiscal support for the financial sector has taken many forms, but the largest single items have been the Troubled Asset Relief Programme (TARP) and equity injections to the government-sponsored enterprises (GSEs) Fannie Mae and Freddie Mac. As detailed in the table above, USD700bn was committed under TARP and an initial USD400bn for the GSEs (subsequently this limit was removed). In combination, this represents a commitment of fiscal resources of 10% of GDP, which is among the largest bail-out commitments seen among high-grade sovereigns through the crisis, broadly comparable with those in the UK, Spain and Switzerland. Gross outlays to date under TARP and for GSE capital support have been significantly smaller than the initial commitment at around USD455bn or 3.2% of GDP, but the Treasury has also made direct purchases of agency-backed mortgage-backed securities (MBS) of USD314bn, taking total outlays for financial support to 5.4% of GDP. The Treasury only includes the subsidy elements of these cash outlays in the deficit (based on estimates of the net present value losses on the transaction) and hence the impact on the FY09 budget deficit outturn of these transactions was much smaller at 1.8% of GDP. However, the full cash outlays are reflected in the rise in government debt, which was USD300bn greater than the deficit in FY09. As of December 2009, USD165bn of TARP outlays had been repaid.

In addition to direct budgetary support, the government's explicit contingent liabilities have also increased sharply through the course of the crisis. In September 2008 Treasury offered a guarantee to money market funds to ensure these did not "break the buck" for investors. At its peak, some USD3,217bn of funds were guaranteed (23% of GDP) but the guarantee was terminated in September 2009 with no losses for the Treasury. In addition, the Federal Deposit Insurance Corporation (FDIC) introduced a guarantee programme for newly issued bank debt with maturities of up to three years and guaranteed non-interest-bearing transaction accounts (USD304bn and USD736bn outstanding, respectively). Treasury also created the Asset Guarantee Programme in November to insure Citigroup against losses on a pool of "toxic" assets, with a maximum sovereign exposure of USD236bn but this has recently been terminated. Overall, USD1064bn (7.5% of GDP) of explicit guarantees are currently outstanding. The Treasury has not explicitly guaranteed GSE debts, but has strongly demonstrated its backing to assuage investor concerns – Fannie and Freddie had outstanding debts of USD1,600bn (11.4% GDP) at September 2009, excluding their guarantees on private MBS of around USD3trn.

The American Recovery and Reinvestment Act 2009 (ARRA) stimulus package was passed in February 2009. It contained a total of USD767bn of fiscal easing measures concentrated over FY09-FY11, with the largest impact in FY10 at 2.8% of GDP, making it one of the largest discretionary stimulus policies (in GDP terms) among the advanced G20 economies. ARRA included temporary income tax cuts and tax relief for firms, but the majority of the easing measures were on the expenditure side. The latter included higher infrastructure spending, increased social welfare payments, and transfers to the states to support health and education expenditure and avoid pro-cyclical fiscal tightening at the state level.

The scale of transfers to states in the ARRA highlights a further fiscal concern, namely the deteriorating budgetary health of sub-national governments. Around USD140bn of the total USD767bn ARRA package was in the form of aid to states, including USD87bn of Medicaid funding and the creation of a USD50bn State Fiscal Stabilisation Fund. State finances have been under unprecedented pressure due to the collapse in revenue, in turn reflecting rising unemployment and weak housing markets. Fitch recognises that state governments have a high degree of autonomy in setting tax rates and receive a somewhat lower share of their total revenue in the form of central government grants than the OECD average (at 9.6% of total state revenue compared with 14.4% respectively). In addition, state debt obligations are not guaranteed by the federal government. However, the scale of federal support provided through the recession underscores the relevance of Fitch's traditional wider "general government" measure – including state and local governments – in assessing the health of the public finances.

Fiscal Impact of 2009 Stimulus Act (ARRA)

(USDbn)	2009	2010	2011	2009-2019
Expenditure	120	220	126	576
Revenue	-65	-180	-8	-212
Deficit	185	399	134	767
As % GDP	1.3	2.8	0.9	5.4

Source: CBO, Treasury, Fitch

Funding Flexibility and Policy Response Mitigates Near-Term Concerns

The US's exceptional funding flexibility mitigates concerns about the near-term deterioration in the public finances and underlines the US's elevated debt tolerance, even relative to other large 'AAA's'.¹ The dollar's status as the leading global reserve currency and the unmatched liquidity of the US Treasury market – with daily turnover of around USD500bn, more than 10 times that in large European government bond markets – provides the government unparalleled near-term balance sheet flexibility. The strength of both the Treasury market and the dollar amidst crisis and the US's generous provision of dollar liquidity to other major central banks are clear testimony to its unique position.

This flexibility has allowed the government to undertake aggressive counter-crisis and counter-recessionary measures, which appear to be starting to take effect. In addition to the fiscal stimulus package and fiscal support for the financial sector, the Fed has seen its balance sheet expand sharply under the "quantitative easing" programme to around 15% of GDP from 6% before the Lehman Brothers collapse. In addition to government debt, the Fed has made substantial purchases of agency-backed MBS and other private-sector assets in an attempt to ease liquidity, revive the flow of credit, and lower interest rates in the wider economy.

The policy response has gained traction in stabilising the financial sector and the economy. In addition to the recovery in equity markets, credit spreads have narrowed across a wide range of security classes and issuance in asset-backed securities markets has picked up, thanks to the Fed's Term Asset-Backed Lending Facility programme. Furthermore, banks have been successful in raising substantial amounts of common equity from the market following the publication of the authorities' Supervisory Capital Assessment Programme in May 2009, with little recourse to the programme's backstop of additional Treasury capital. Credit default swaps on the major banks have declined to pre-Lehman levels and banks have been issuing term debt without a government guarantee since the summer. The thawing in credit markets has allowed the Fed to scale back many of its liquidity operations

¹ See "High-Grade Sovereigns and the Global Financial Crisis" under *Related Research* on the front page

in recent months, while some extraordinary fiscal measures, such as the guarantee for money market funds, have been allowed to expire.

On the economic front, GDP turned positive to the tune of 0.6% in Q309, of which 0.1% was explained by growth in government expenditure. Moreover, tax cuts enacted under ARRA have helped to support household disposable incomes, which grew by 1.3% in the year to Q309, in contrast to a decline of 1.6% in pre-tax income. Three quarters of the pick-up in consumers' expenditure in Q309 was explained by a 4.8% increase in spending on cars, related to the "cash for clunkers" programme. Fitch forecasts growth to recover to 2.4% in 2010, partly due to policy stimulus.

Risks to Medium-Term Public Debt Sustainability Remain

However, concerns remain over the medium-term fiscal outlook and in particular whether public debt ratios will be stabilised and reduced. While the Treasury's initial 2010 budget projected federal debt stabilising at 70% of GDP by 2011, the August 2009 budget update (see table below) showed debt ratios continuing to rise through to 2015, albeit by marginal amounts by the end of the period. The government has committed to "propose further steps in the 2011 Budget to reduce the deficit and stabilise debt at a prudent level" but at this stage there is an absence of firm medium-term consolidation measures. Tax cuts introduced by the Bush administration in 2001 and 2003 were due to expire in 2011, which would, along with the non-indexation of allowances for the Alternative Minimum Tax, have yielded around 1.5% of GDP in additional revenue; but the budget projections now assume these cuts will be extended and the allowances indexed.

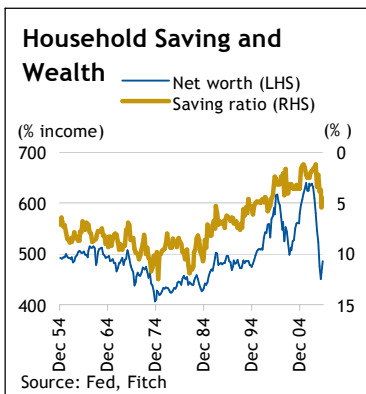
Official Medium-Term Fiscal Projections - Federal Government

(% GDP)	FY09	FY10	FY11	FY12	FY13	FY14	FY15
Revenue	14.7	15.7	17.1	18.4	18.6	18.7	18.8
Primary expenditure	25.9	26.1	24.6	23.3	23.2	23.0	22.7
O/w mandatory	15.8	14.9	13.9	13.0	12.9	12.9	12.7
Discretionary	8.8	9.8	8.7	7.8	7.4	7.1	6.9
O/w non- defence	3.6	4.1	4.8	4.3	3.9	3.7	3.5
Interest	1.2	1.4	1.9	2.4	2.8	2.9	3.1
Deficit	11.2	10.4	7.4	5.0	4.6	4.3	3.9
Debt	55.7	66.3	70.0	71.4	72.3	72.9	73.2
Memo: GDP growth	-2.8	2.0	3.8	4.3	4.3	4.1	3.6

Source: Treasury - mid-session review fiscal year 2010, August 2009

Moreover, official medium-term fiscal projections are based on optimistic forecasts that growth will average 4% a year from 2011. These forecasts are consistent with the view that neither the level nor the growth rate of potential GDP has been adversely affected by the crisis and that demand growth in the next five years will be sufficiently strong to close a very large negative "output gap" between actual and potential GDP. However, there are significant risks that sharp falls in investment and rising long-term unemployment could adversely affect supply-side growth potential, while large uncertainties exist about the historical level of potential GDP. Moreover, there is a material risk that private-sector de-leveraging pressures continue to weigh on demand growth into the medium term as households strive to improve balance sheets. As the chart shows, the decline in the saving ratio from the early 1990s was associated with sizeable gains in the household sector's net worth, but the latter has been reversed through the crisis and recession. Official growth forecasts from 2011 are 1% a year higher than the latest consensus forecast, and Fitch would expect growth to be closer to 2.75% to 3% a year. This would imply deficits around 0.5% of GDP larger in each year from 2011.

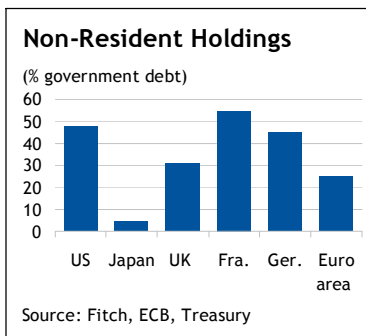
The projected improvements in the deficit are partly based on the phasing-out of stimulus and financial-sector support measures. However, they also assume a cyclical recovery in revenue, which may prove disappointing. For example, the



Healthcare Reform Impact

2010-2019, USDbn	Rep's Version	Senate Version
Broadening of insurance coverage	891	614
Cost savings	-456	-483
Revenue raising measures	574	264
Net impact on deficit	-138	-133

Source: CBO



budget assumes that corporate tax receipts recover sharply to above their post-1980s average – as discussed under *The Fiscal Shock* above, corporate taxes over 2005-2007 seem to have been heavily boosted by unsustainably strong asset markets and financial-sector profits which are unlikely to re-emerge.

The expenditure side of the budget is also unlikely to prove a major source of additional consolidation. Government spending is low by international standards and both defence and non-defence discretionary spending as a percentage of GDP are already projected to fall sharply over the medium term to their lowest levels since the mid-1990s. With regard to mandatory (or entitlement) spending, healthcare reform proposals currently at the final conference stage in Congress will significantly expand the coverage of healthcare insurance, including providing subsidies for individuals to purchase insurance from exchanges. This will be funded by cost savings on payments to healthcare providers in addition to tax increases. Both Senate and House of Representatives versions of the reform bill show small net reductions in the deficit over the next 10 years but the Senate version has a less generous broadening of coverage and lower tax increases (see table below).

A final risk relates to the potential for interest rate shocks. The average maturity of federal debt has shortened to below four years as T-bill issuance was stepped up to deal with unexpected financing needs through 2008 and 2009. This is short by international standards and implies a rapid feed-through of interest rate shocks to the budget. Treasury projections assume T-bill rates rise to 4% and 10-year notes to 5.3% by 2013, but investor concerns about the impact of quantitative easing on inflation or fiscal risks could result in faster increases. While the depth of the Treasury securities market mitigates the risk of large interest rate shocks, the current account deficit and the high share of non-resident holdings – which rose to 48.3% at end-2008 from 31% in 2000 (see chart) – increase the risk of volatility in yields. A 1pp rise in real interest rates would add 0.5% of GDP to expenditure in 2011 and push central government interest payments to 15% of revenue.

Forecast Summary

	2005	2006	2007	2008	2009f	2010f	2011f
Macroeconomic indicators and policy							
Real GDP growth (%)	3.1	2.7	2.1	0.4	-2.5	2.4	2.7
Consumer prices (annual average % change)	3.4	3.2	2.9	3.8	-0.3	0.8	0.6
Short-term interest rate (%) ^a	3.2	5.0	5.0	2.1	0.3	0.3	0.8
General government balance (% of GDP)	-3.4	-2.2	-2.9	-6.5	-11.4	-11.0	-8.5
General government debt (% of GDP)	56.7	55.9	57.2	64.2	78.6	88.9	93.6
LC per USD (annual average)	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Real effective exchange rate (2,000 = 100)	83.5	83.0	78.6	75.1	80.3	77.0	78.0
External finance							
Current account balance (USDbn)	-748.7	-803.5	-726.6	-706.1	-454.3	-417.4	-417.2
Current account balance (% of GDP)	-6.0	-6.1	-5.3	-4.9	-3.2	-2.9	-2.8
Current account balance plus net FDI (% of GDP)	-5.4	-6.1	-6.2	-5.0	-3.9	-3.1	-3.3
Net external debt (USDbn)	3684.6	4515.5	5157.6	5275.0	5800.2	6218.7	6681.8
Net external debt (% of GDP)	29.6	34.1	37.4	36.5	41.3	43.1	44.7
Net external debt (% of CXR)	200.7	209.1	207.5	201.9	260.0	276.0	279.6
Official international reserves including gold (USDbn)	170.4	212.9	241.7	294.6	301.7	314.3	327.2
Official international reserves (months of CXP cover)	0.8	0.9	0.9	1.1	1.3	1.4	1.4
External interest service (% of CXR)	16.9	20.7	22.6	18.1	29.2	29.9	33.1
Gross external financing requirement (% int. reserves)	457.4	607.0	384.2	295.4	155.4	141.7	135.9
Memo: Global forecast summary							
Real GDP growth (%)							
US	3.1	2.7	2.1	0.4	-2.5	2.4	2.7
Japan	1.9	2.1	2.3	-0.6	-5.4	1.0	1.2
Euro area	1.8	3.0	2.7	0.6	-4.7	-0.2	2.0
World	3.3	3.9	3.6	1.7	-3.3	1.4	2.5
Commodities							
Oil (USD/barrel)	54.4	65.4	72.6	97.0	60.0	70.0	80.0

Source: Fitch

Comparative Analysis: Macroeconomic Performance and Policies

United States of America

	2009						
	France 'AAA'	Germany 'AAA'	Spain 'AAA'	UK 'AAA'	US 'AAA'	'AAA' median	'AA' median
Real GDP (5yr average % change)	0.9	0.6	1.7	0.7	1.1	1.2	2.5
Volatility of GDP (10yr rolling SD)	1.7	2.4	2.5	2.4	1.9	2.4	2.3
Consumer prices (5yr average)	1.7	1.8	2.8	2.5	2.6	1.9	2.4
Volatility of CPI (10yr rolling SD)	0.8	0.7	1.2	0.8	1.2	0.8	1.3
Years since double-digit inflation	27.0	-	25.0	28.0	28.0	n.a.	n.a.
Unemployment rate	9.1	8.2	18.4	7.8	9.3	7.8	5.7
Type of exchange rate regime	EMU	EMU	EMU	Floating	Floating	n.a.	n.a.
Dollarisation ratio	-	-	5.0	-	0.8	13.8	25.0
REER volatility (10yr rolling SD)	3.0	2.8	2.0	6.4	6.8	2.8	3.4

Source: Fitch

Strengths

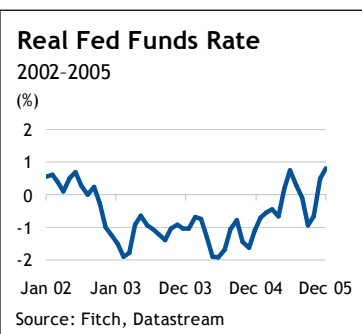
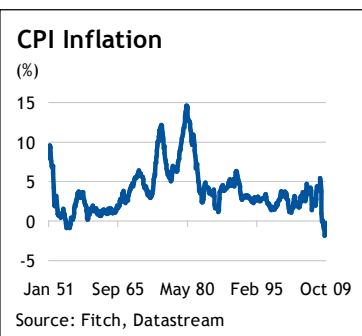
- Economic growth has been faster than in other major 'AAA'-rated economies over the long term, reflecting a highly flexible and innovative market economy.
- Inflation has been low and stable since the early 1990s, in large part the legacy of Fed Governor Paul Volcker's sustained monetary tightening in the 1980s.
- An aggressive macroeconomic policy response after the Lehman's collapse has contributed to a stabilisation in US and global financial markets and a nascent recovery in economic activity. While headline CPI inflation saw negative readings earlier in 2009 the core rate (excluding food and energy) remains at 1.7%, suggesting that deflation risks are contained.

Weaknesses

- The economy has just suffered its deepest and longest recession since WW11 as a result of the financial crisis and sharp retrenchment by the highly indebted household sector.
- The scale of the adjustment confirms that growth had been unsustainably strong in the middle of the decade, as indicated by Fitch's Macro-Prudential Indicator, based on trends in credit growth and asset prices. With deleveraging pressures continuing, growth is likely to fall short of the rates seen in historical recoveries over the medium term.
- Monetary policy conditions were excessively lax in the middle of the decade, with the federal funds rate negative in real terms (deflated by CPI) over 2003 to 2005 (see chart). This is likely to have contributed to the subsequent credit bubble.

Commentary

Macroeconomic policy settings are currently at full tilt in pursuit of recovery. This inevitably entails a risk of inflation over the medium term if policy stimulus is not withdrawn rapidly enough. The Fed has been keen to articulate the various tools at its disposal to withdraw monetary stimulus when they believe the time is right (including, for example, reverse repos, non-renewal of liquidity facilities, interest rate increases and asset sales) and with labour market conditions continuing to deteriorate, deflation risks still seem the larger worry. However, investor concerns about inflation could emerge if accommodative monetary policies are seen to remain in place for too long, particularly if a strategy to stabilise and reduce public debt fails to emerge. Fears of "fiscal dominance" – whereby inflation goals are subverted to easing the government's debt burden – could start to undermine the credibility of the monetary policy framework and weaken the dollar.

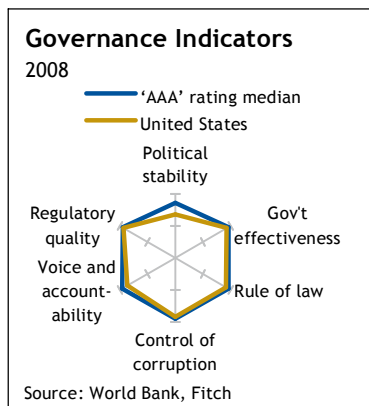


Comparative Analysis: Structural Features

United States of America

	2009						
	France 'AAA'	Germany 'AAA'	Spain 'AAA'	UK 'AAA'	US 'AAA'	'AAA' median	'AA' median
GNI per capita PPP (USD, latest)	34,400	35,940	31,130	36,130	46,970	37,480	32,145
GDP per capita (USD, mkt. exchange rates)	43,165	41,073	32,700	35,832	44,601	45,806	31,283
Human development index (percentile, latest)	96.2	88.4	92.3	89.0	93.4	93.7	88.5
Ease of doing business (percentile, latest)	83.6	86.9	66.5	97.9	98.4	91.3	92.4
Trade openness (CXR and CXP % GDP)	34.5	47.5	35.8	41.0	17.5	n.a.	n.a.
Gross domestic savings (% GDP)	18.0	22.2	22.7	12.8	11.3	22.8	24.1
Gross national savings (% GNP)	17.8	23.1	20.0	12.3	13.6	23.1	23.4
Gross domestic investment (% GDP)	20.3	19.1	25.6	14.7	13.6	20.3	22.4
Private credit (% GDP)	110.7	111.1	193.8	211.8	195.5	136.1	134.9
BSR indicators						n.a.	n.a.
Bank system CAR ^a	10.1	12.9	11.4	12.7	14.2	n.a.	n.a.
Foreign bank ownership (% assets)	-	16.5	10.0	55.3	14.8	n.a.	n.a.
Public bank ownership (% assets)	-	36.1	40.0	23.0	-	33.0	17.9

^a 2008
Source: Fitch and World Bank



Strengths

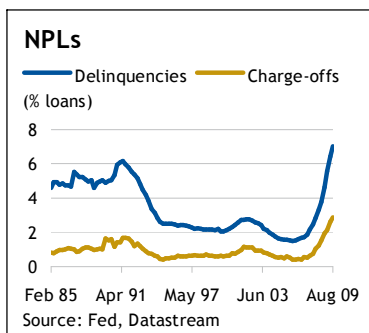
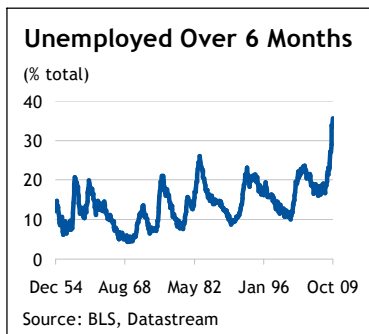
- The US has a large, high-income, wealthy and diversified economy.
- The highly flexible economy is able to reallocate resources following shocks with relatively little friction. The US typically scores very highly on measures of labour and product market flexibility. Labour mobility is high and evidence of corporate restructuring is clear.
- The business environment is strong.
- The US has unparalleled international bargaining power.
- The country enjoys political stability, strong institutions and respect for rule of law.

Weaknesses

- The crisis revealed weaknesses in the financial system, including problems with the originate-to-distribute model of credit allocation, a fragmented financial regulation framework and the distortionary role of government-backed mortgage lenders and guarantors, Fannie Mae and Freddie Mac. Substantive reforms are underway, but Fannie and Freddie continue to play a dominant role and growing role in housing finance.
- Rising long-term unemployment as a result of the length of the recession could weigh on growth in supply-side potential over the medium term.
- The national savings rate is still low.

Commentary

The deterioration in underwriting standards in the boom years has exacerbated asset quality problems in the financial sector. Mortgage delinquencies have risen to nearly 7% in the conforming sector and 26% in subprime. FDIC reported 552 “problem” financial institutions in Q309 with assets of USD346bn, the highest since 1993, while 95 institutions have failed during the crisis (see chart). Government liquidity and solvency support has stabilised the sector, but the stock of bank credit is falling, while it is unclear whether the securitisation channel will re-emerge as a major source of credit growth once emergency Fed measures are phased out. This could be an additional drag on medium-term growth.



Comparative Analysis: External Finances

United States of America

	2009					Last 10 years	
	France 'AAA'	Germany 'AAA'	Spain 'AAA'	UK 'AAA'	US 'AAA'	'AAA' median	'AA' median
GXD (% CXR)	673.1	324.9	551.4	1167.7	863.3	307.3	265.6
GXD (% GDP)	224.5	161.2	179.5	465.9	137.2	167.1	125.1
NXD (% CXR)	94.2	-4.2	275.2	82.4	260.0	21.9	59.2
NXD (% GDP)	31.4	-2.1	89.6	32.9	41.3	12.4	22.2
GSXD (% GXD)	29.8	24.9	15.9	3.8	28.0	19.0	13.1
NSXD (% CXR)	153.6	55.9	49.3	34.6	200.8	15.9	-0.5
NSXD (% GDP)	51.2	27.7	16.1	13.8	31.9	9.5	-0.3
SNFA (USDbn)	0.0	-936.1	0.0	0.0	-4479.7	-0.2	0.3
SNFA (% GDP)	0.0	-27.7	0.0	0.0	-31.9	0.0	1.8
Ext. debt service ratio (% CXR)	85.3	49.8	83.5	68.2	29.4	37.6	30.0
Ext. interest service ratio (% CXR)	20.9	10.5	25.1	19.6	29.2	11.1	9.8
Liquidity ratio (latest)	31.1	45.6	13.3	74.8	17.6	55.0	47.9
Current account balance (% GDP)	-2.2	4.3	-6.6	-2.1	-3.2	2.6	1.0
CAB plus net FDI (% GDP)	-5.3	0.4	-6.7	-1.7	-3.9	1.3	-0.5
Commodity dependence (% CXR, latest)	12.2	12.5	13.1	8.9	10.1	12.0	13.0
Sovereign net FX debt (% GDP)	-4.6	-3.5	-0.1	-2.4	-2.1	-	-

Source: Fitch

Strengths

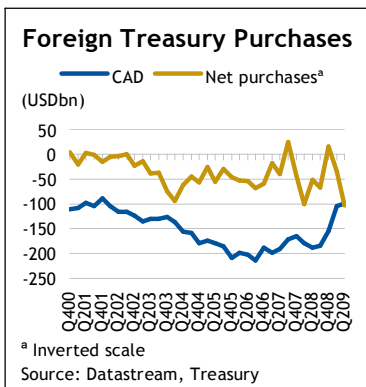
- The dollar’s dominant reserve currency status affords the US many advantages. Residents are readily able to borrow externally in dollars (over 90% of GXD is denominated in dollars); overseas holdings of dollar cash generate seigniorage revenue; and the currency benefits from flight to quality and liquidity in periods of global financial market stress. It also renders FX liquidity risks irrelevant.
- Net income surpluses continue to be recorded on the current account despite rising net external liabilities. Apparently superior rates of return on US overseas investments have partly reflected the depreciation of the dollar over recent years (enhancing the dollar value of residents’ foreign-currency assets) and have led some economists to speculate that the US has unrecorded foreign assets (“dark matter”). Either way, this has helped to mute the rise in US net external liabilities associated with the savings/investment shortfall.

Weaknesses

- Persistent current account deficits reflect low private saving rates before the recession and, more recently, large fiscal deficits which are being funded, to a significant extent, by non-residents.
- Net external debt (NXD) as a percentage of GDP is more than three times the ‘AAA’ median, and the negative net international investment position is also large at 24% of GDP. Net sovereign external debt accounts for three-quarters of NXD, reflecting a sharp rise in foreign holdings of US Treasury securities since 2000. There was also a sharp rise in net external debt of the non-bank private sector in the run-up to the recession associated with rapid increase in private-sector leverage partly funded across international capital markets through securitisation.

Commentary

The willingness of foreign investors – in particular Asian central banks – to fund the US current account deficit has supported the dollar and helped keep long-term interest rates low in recent years. But by the same token any abrupt change in these investors’ appetite for dollar assets – e.g. as a result of shifting exchange rate policies or concerns about fiscal sustainability or inflation – could have sizeable negative impacts on the dollar and on bond prices.

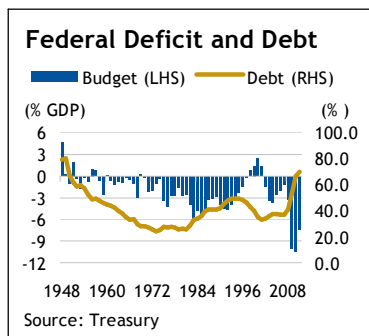


Comparative Analysis: Public Finances

United States of America

	2009					Last 10 years	
	France 'AAA'	Germany 'AAA'	Spain 'AAA'	UK 'AAA'	US 'AAA'	'AAA' median	'AA' median
Budget balance (% GDP)	-8.3	-3.4	-12.4	-12.6	-11.4	0.0	-0.2
Primary balance (% GDP)	-5.4	-0.7	-10.5	-10.7	-9.3	2.1	1.8
Revenue and grants (% GDP)	47.3	41.6	31.2	39.6	25.9	43.6	40.4
Volatility of revenue/GDP ratio	1.8	2.7	7.1	2.9	6.4	2.8	3.6
Interest payments (% revenue)	6.2	6.6	6.0	4.9	8.1	4.9	5.4
Debt (% revenue)	162.9	176.9	186.2	174.4	303.4	118.3	88.1
Debt (% GDP)	77.0	73.7	58.1	69.1	78.6	50.8	39.9
Net debt (% GDP)	76.3	72.1	53.3	66.6	76.6	41.7	30.3
FC debt (% total debt)	0.0	0.8	0.7	0.0	0.0	2.5	6.7
CG debt maturities (% GDP)	13.1	8.5	5.0	7.0	19.1	9.2	10.3
Average duration of CG debt (years)	5.3	4.5	4.8	10.3	-	4.8	4.1

Source: Fitch



Strengths

- The federal debt market is the benchmark for global credit markets. Market depth and liquidity are unmatched. Turnover in US Treasuries is over USD500bn a day, equivalent to global equity market turnover, compared with roughly USD20bn to USD30bn for large European government bond markets.
- Fiscal transparency is extremely high, with tight controls and monitoring of budgets and intense scrutiny from the legislature (including the CBO). “Notionally funded” social security accounts ensure that the implications of demographic trends on future pension spending are measured accurately.
- A track record of fiscal consolidation including in the second half of the 1990s under the Clinton administration’s Omnibus Budget Reconciliation Act.

Weaknesses

- Extremely large fiscal deficits will result in gross general government debt/GDP rising to the highest level among ‘AAA’s by end-2010.
- The government’s revenue base is narrow and relatively volatile. Debt/revenue and interest/revenue ratios were among the highest in the ‘AAA’ universe in 2008, though the latter fell in 2009 due to low interest rates. Corporate and income tax receipts have fallen precipitously this year, having been boosted by unsustainably high corporate profits and asset prices pre-crisis.
- While refinancing risk is not a credit concern in light of Treasuries’ global benchmark status, the short maturity structure of public debt increases interest rate risk. The Treasury is, however, aiming to increase the maturity of federal debt over the medium term.
- An effective medium-term fiscal framework is lacking. The statutory federal debt limit – specified in nominal dollar terms – has not been an effective discipline on budgetary policy and is frequently revised upwards. It was last raised by USD290bn to USD12,394bn on 28 December 2009, but with the federal deficit running at over USD1trn year and a current actual debt level (on the relevant measure) of USD12,290bn, it is highly likely that the limit will need to be revised again soon.

Public Debt Measures

Sep 09	(USDbn)	(% GDP)
Federal	7,552	52.9
State and local	1,831	12.8
Other liabilities ^a	1,193	8.4
General government	10,574	74.1

^a Includes Treasury non-marketable debt owed to public-sector employee pension funds. The majority of Treasury non-marketable debt is held by social security funds, i.e. within general government
Source: Fed, Treasury, Fitch

Commentary

While the FY09 federal deficit outturn was extremely large at 10% of GDP, this was significantly less than initial expectations of 12.9%, thanks to lower-than-anticipated outlays to support the financial sector. This could continue to be a source of positive fiscal surprises, as the Treasury now expects that further TARP outlays will be less than projected in the August 2009 mid-year update.

Fiscal Accounts Summary

(% of GDP)	2006	2007	2008	2009f	2010f	2011f
General government						
Revenue	30.4	30.7	28.3	25.9	26.7	28.2
Expenditure	32.6	33.6	34.8	37.3	37.7	36.7
O/w interest payments	2.8	3.0	2.7	2.1	2.3	3.0
Primary balance	0.6	0.1	-3.7	-9.3	-8.7	-5.5
Overall balance	-2.2	-2.9	-6.5	-11.4	-11.0	-8.5
General government debt	55.9	57.2	64.2	78.6	88.9	93.6
% of general government revenue	183.9	186.1	226.6	303.4	333.1	332.0
General government deposits	0.3	0.4	2.6	1.9	1.9	0.5
Net general government debt	55.7	56.7	61.6	76.6	87.1	93.2
Central government						
Revenue	19.3	19.5	17.3	15.0	15.6	17.1
O/w grants	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure and net lending	21.1	21.7	22.8	25.1	25.3	24.5
O/w current expenditure and transfers	20.6	21.0	21.6	23.8	24.0	23.2
- Interest	2.1	2.3	2.0	1.6	1.7	2.2
O/w capital expenditure	0.5	0.7	1.2	1.3	1.3	1.3
Current balance	-1.3	-1.5	-4.3	-8.8	-8.4	-6.2
Primary balance	0.2	0.0	-3.4	-8.6	-8.0	-5.2
Overall balance	-1.9	-2.2	-5.4	-10.1	-9.7	-7.4
Central government debt	35.0	35.0	42.1	65.3	73.2	78.1
% of central government revenue	181.5	180.1	243.1	436.7	469.8	458.0
Central government debt (USDbn)	4,632	4,839	6,086	9,170	10,570	11,680
By residency of holder						
Domestic	2,529	2,486	3,007	5,420	6,307	6,878
Foreign	2,103	2,353	3,079	3,750	4,364	4,758
By place of issue						
Domestic	4,632	4,839	6,086	9,170	10,570	11,680
Foreign	0.0	0.0	0.0	0.0	0.0	0.0
By currency denomination						
Local currency	4,632	4,839	6,086	9,170	10,570	11,680
Foreign currency	0.0	0.0	0.0	0.0	0.0	0.0
In USD equivalent (eop exchange rate)	0.0	0.0	0.0	0.0	0.0	0.0
By maturity						
Less than 12 months (residual maturity)	1,177	1,137	1,177	2,406	3,200	3,490
Average maturity (years)	4.8	4.8	3.8	3.8	3.3	3.3
Average duration (years)	-	-	-	-	-	-
Memo						
Nominal GDP (USDbn)	13,245	13,808	14,441	14,040	14,433	14,950

Source: Treasury department, Federal Reserve and Fitch estimates and forecasts

External Debt and Assets

(USDbn)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Gross external debt	4,505	5,086	5,851	6,304	7,720	9,677	11,667	14,737	18,613	19,258
% of GDP	45.9	50.2	55.9	57.5	65.9	77.7	88.1	106.7	128.9	137.2
% of CXR	314.5	389.9	460.5	465.0	484.5	527.1	540.1	592.9	712.3	863.3
By maturity										
Medium - and long-term	2,457.5	2,774.5	3,191.7	3,438.7	4,165.2	5,881.7	7,211.7	9,121.8	13,198.5	13,655.9
Short-term	2,047.7	2,311.9	2,659.6	2,865.4	3,554.9	3,795.0	4,454.7	5,615.2	5,414.4	5,602.0
% of total debt	45.5	45.5	45.5	45.5	46.0	39.2	38.2	38.1	29.1	29.1
By debtor										
Monetary authorities	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.0
General government	1,615.8	1,792.7	2,113.7	2,366.1	2,810.7	3,150.0	3,571.9	4,047.9	4,867.3	5,397.3
O/w central government	1,034.2	1,051.2	1,246.8	1,523.1	1,849.3	2,033.9	2,103.1	2,353.2	3,078.7	3,750.0
Banks	1,411.3	912.5	1,009.5	1,284.9	1,579.8	1,706.2	1,977.2	2,138.3	2,071.6	2,086.6
Other sectors	1,478.0	2,381.2	2,728.1	2,653.1	3,329.6	4,820.5	6,117.4	8,550.7	11,674.1	11,774.1
Gross external assets (non-equity)	2,854	3,003	3,408	3,504	4,282	5,992	7,151	9,579	13,338	13,457
International reserves, incl. gold	129.6	128.6	149.2	170.0	182.9	170.4	212.9	241.7	294.6	301.7
Other sovereign assets nes	85.2	85.7	85.3	84.8	83.1	77.5	72.2	94.5	624.1	0.0
Deposit money banks' foreign assets	961.6	807.9	850.2	934.4	1,109.7	1,281.7	1,641.5	2,021.6	1,789.0	1,909.0
Other sector foreign assets	1,679.2	1,979.3	2,314.0	2,301.4	2,899.3	4,444.9	5,217.4	7,186.1	10,631.2	10,631.2
Net external debt	1,651	2,084	2,443	2,800	3,438	3,685	4,516	5,158	5,275	5,800
% of GDP	16.8	20.6	23.3	25.5	29.4	29.6	34.1	37.4	36.5	41.3
% of CXR	115.3	159.7	192.3	206.5	215.8	200.7	209.1	207.5	201.9	260.0
Net sovereign external debt	1,402.3	1,577.1	1,869.8	2,097.7	2,538.0	2,884.4	3,279.8	3,676.2	3,949.5	4,479.7
% of GDP	14.3	15.6	17.9	19.1	21.7	23.2	24.8	26.6	27.3	31.9
Net bank external debt	449.8	104.6	159.4	350.5	470.0	424.5	335.7	116.7	282.6	177.6
Net other external debt	-201.2	401.9	414.1	351.7	430.3	375.7	900.0	1,364.6	1,042.9	1,142.9
Net international investment position	-1,331	-1,869	-2,038	-2,087	-2,246	-1,925	-2,184	-2,140	-3,470	-3,924
% of GDP	-13.6	-18.5	-19.5	-19.0	-19.2	-15.5	-16.5	-15.5	-24.0	-27.9
Sovereign net foreign assets	-1,402	-1,577	-1,870	-2,098	-2,538	-2,884	-3,280	-3,676	-3,950	-4,480
% of GDP	-14.3	-15.6	-17.9	-19.1	-21.7	-23.2	-24.8	-26.6	-27.3	-31.9
Debt service (principal & interest)	324.8	309.1	275.6	266.2	314.9	397.4	678.5	653.2	482.0	655.1
Debt service (% of CXR)	22.7	23.7	21.7	19.6	19.8	21.6	31.4	26.3	18.4	29.4
Interest (% of CXR)	18.5	18.6	15.6	13.5	13.5	16.9	20.7	22.6	18.1	29.2
Liquidity ratio (%)	25.6	25.2	19.2	17.9	18.5	17.5	16.5	19.1	19.5	17.6
Net sovereign FX debt (% of GDP)	-1.3	-1.3	-1.4	-1.6	-1.6	-1.4	-1.6	-1.8	-2.0	-2.1
Memo										
Nominal GDP	9,817.0	10,127.9	10,469.9	10,960.7	11,712.5	12,455.8	13,244.5	13,807.5	14,441.4	14,039.6

Sources: NBP, IMF, World Bank and Fitch estimates and forecasts

Balance of Payments

(USDbn)	2006	2007	2008	2009f	2010f	2011f
Current account balance	-803.5	-726.6	-706.1	-454.3	-417.4	-417.2
% of GDP	-6.1	-5.3	-4.9	-3.2	-2.9	-2.8
% of CXR	-37.2	-29.2	-27.0	-20.4	-18.5	-17.5
Trade balance	-843.5	-826.9	-836.3	-459.3	-272.4	-417.2
Exports, fob	1,019.6	1,142.5	1,281.0	1,090.8	1,097.9	1165.2
Imports, fob	1,863.1	1,969.4	2,117.3	1,550.1	1,370.3	1582.4
Services, net	83.2	125.5	140.3	130.0	0.0	175.0
Services, credit	432.1	500.7	545.6	520.0	550.0	600.0
Services, debit	348.9	375.2	405.3	390.0	550.0	425.0
Income, net	48.1	90.8	118.2	25.0	20.0	0.0
Income, credit	682.2	818.9	764.6	600.0	580.0	600.0
Income, debit	634.1	728.1	646.4	575.0	560.0	600.0
O/w: Interest payments	447.5	561.9	474.2	651.5	674.0	791.0
Current transfers, net	-91.3	-116.0	-128.4	-150.0	-165.0	-175.0
Memo						
Non-debt-creating inflows (net)	-74.0	-81.3	72.1	-70.0	0.0	-45.0
O/w equity FDI	-82.2	-209.1	-37.0	-100.0	-25.0	-75.0
O/w portfolio equity	8.2	127.8	109.1	30.0	25.0	30.0
O/w other	-3.9	-1.9	1.0	-1.0	-1.0	-1.0
Change in reserves (-= increase)	-2.4	0.1	4.8	-0.3	-0.4	-0.2
Gross external financing requirement	1,034.5	817.8	713.9	457.9	427.4	427.2
Stock of international reserves, incl. gold	212.9	241.7	294.6	301.7	314.3	327.2

Sources: IMF and Fitch estimates and forecasts

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