

July 28, 2009

**Research Update:**

# Ambac Assurance Corp. Ratings Lowered To 'CC' From 'BBB'; Outlook Developing

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## Research Update:

# Ambac Assurance Corp. Ratings Lowered To 'CC' From 'BBB'; Outlook Developing

## Overview

- Ambac Assurance Corp. continues to experience adverse loss development in its insured book of business.
- We believe that it is now likely that losses and reserve additions and impairments will deplete policyholders' surplus to levels below the regulator-required minimums.
- As a result, we have lowered our rating on Ambac to 'CC' from 'BBB'.

## Rating Action

On July 28, 2009, Standard & Poor's Ratings Services lowered its counterparty credit, financial strength, and financial enhancement ratings on Ambac Assurance Corp (Ambac) to 'CC' from 'BBB' and removed them from CreditWatch, where they were placed on June 24, 2009, with negative implications. The outlook is developing.

At the same time, Standard & Poor's lowered its counterparty credit rating on Ambac Financial Group Inc. (Ambac Financial) to 'CC' from 'BB' and removed it from CreditWatch negative. The outlook is negative.

In addition, Standard & Poor's lowered its ratings on Ambac's preferred stock and Ambac Financial's directly issued subordinated capital securities to 'C' from 'B' in light of the announced deferral of dividends.

## Rationale

This rating action reflects our view of the significant deterioration in the Ambac's insured portfolio of nonprime residential mortgage-backed securities and related CDOs, which has required the company to strengthen reserves to account for higher projected claims. The additional reserves will have a significant negative effect on operating results, which we believe will likely cause surplus to decline to below regulator-required minimums.

Ambac's policyholders' surplus was \$372 million as of March 31, 2009. Two CDO of ABS commutations that Ambac has announced could increase surplus marginally. However, the company has announced that it expects to increase CDO of ABS impairments by \$1.6 billion for the quarter and loss reserves by approximately \$800 million. These actions could lead to negative policyholders' surplus as of June 30, 2009.

Ambac's contingency reserves as of March 31, 2009, were approximately \$1.9 billion. The company has asked the Wisconsin Office of the Insurance Commissioner for permission to release some of the contingency reserves into surplus, but the Wisconsin regulator has yet to approve such an action.

## Outlook

The developing outlook on Ambac reflects the possibility that we could revise the rating to 'R' if there is regulatory intervention because of Ambac's expected weakened capital position. Alternatively, if the regulator approves the release of contingency reserves to bolster surplus, we could raise the rating, but in such circumstances we do not expect to raise the rating higher than the 'CCC' category.

The negative outlook on Ambac Financial reflects our view of the company's dependence on the dividending capabilities of Ambac to support its debt-service obligations. We would lower the rating if Ambac is not able to provide sufficient cash to allow Ambac Financial to service its debt.

Standard & Poor's believes that the credit characteristics of the underlying insured municipal, corporate, and structured transactions could be stronger than the Ambac-enhanced rating following the downgrade. For those issuers or issues for which we currently have an underlying rating (SPUR), Standard & Poor's will revise the rating on such obligations to the SPUR or the Ambac rating, whichever is higher. Standard & Poor's has suspended its ratings on issuers or issues that do not currently carry a SPUR.

A SPUR is our opinion of the stand-alone creditworthiness of an issuer or transaction--that is, the capacity to pay debt service on a debt issue in accordance with its terms, without considering an otherwise applicable bond insurance policy. The SPUR, once assigned, remains in place regardless of what happens to the rating on the credit enhancer and is subject to surveillance by Standard & Poor's.

## Related Research

- "Bond Insurance Industry Overview And Analytical Focus," June 29, 2006.

## Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Ambac Assurance Corp. Connie Lee Insurance Co. Ambac Assurance U.K. Ltd. Counterparty Credit Rating Local Currency	CC/Developing/--	BBB/Watch Neg/--
Financial Strength Rating Local Currency	CC/Developing/--	BBB/Watch Neg/--
Ambac Assurance Corp. Ambac Assurance U.K. Ltd. Financial Enhancement Rating Local Currency	CC/--	BBB/Watch Neg/--
Ambac Financial Group, Inc. Counterparty Credit Rating		

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Local Currency	CC/Negative/--	BB/Watch Neg/--
Ambac Assurance Corp. Preferred Stock	C	B/Watch Neg
Ambac Financial Group, Inc. Senior Unsecured	CC	BB/Watch Neg
Subordinated	C	B/Watch Neg

The complete list of ratings affected by today's actions will be available in the coming days. When available, the list can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com); click on Ratings on the left-hand navigation bar and then select Bond Insurance. Ratings information is also available on RatingsDirect ([www.ratingsdirect.com](http://www.ratingsdirect.com)). Our analysis of the impact of these rating actions is ongoing; we will post any additional rating changes at the same locations

Complete ratings information is available to RatingsDirect subscribers at [www.ratingsdirect.com](http://www.ratingsdirect.com). All ratings affected by this rating action can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com); select your preferred country or region, then Ratings in the left navigation bar, followed by Find a Rating.

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