New York, August 02, 2011 -- Moody's Investors Service has confirmed the Aaa government bond rating of the United States following the raising of the statutory debt limit on August 2. The rating outlook is now negative.

Moody's placed the rating on review for possible downgrade on July 13 due to the small but rising probability of a default on the government's debt obligations because of a failure to increase the debt limit. The initial increase of the debt limit by $900 billion and the commitment to raise it by a further $1.2-1.5 trillion by yearend have virtually eliminated the risk of such a default, prompting the confirmation of the rating at Aaa.

In confirming the Aaa rating, Moody's also recognized that today's agreement is a first step toward achieving the long-term fiscal consolidation needed to maintain the US government debt metrics within Aaa parameters over the long run. The legislation calls for $917 billion in specific spending cuts over the next decade and established a congressional committee charged with making recommendations for achieving a further $1.5 trillion in deficit reduction over the same time period. In the absence of the committee reaching an agreement, automatic spending cuts of $1.2 trillion would become effective.

In assigning a negative outlook to the rating, Moody's indicated, however, that there would be a risk of downgrade if (1) there is a weakening in fiscal discipline in the coming year; (2) further fiscal consolidation measures are not adopted in 2013; (3) the economic outlook deteriorates significantly; or (4) there is an appreciable rise in the US government's funding costs over and above what is currently expected.

First, while the combination of the congressional committee process and automatic triggers provides a mechanism to induce fiscal discipline, this framework is untested. Attempts at fiscal rules in the past have not always stood the test of time. Therefore, should the new mechanism put in place by the Budget Control Act prove ineffective, this could affect the rating negatively. Moody's baseline scenario assumes that fiscal discipline is maintained in 2012, despite pressures for fiscal relaxation that often precede general elections and the difficult negotiations that are likely to arise due to the scheduled expiration of the so-called "Bush tax cuts" at the end of that year.

Second, further measures will likely be required to ensure that the long-run fiscal trajectory remains compatible with a Aaa rating. Specifically, Moody's expects to see a stabilization of the federal government's debt-to-GDP ratio not too far above its projected 2012 level of 73% by the middle of the decade, followed by a decline. Such a pattern would also support a smaller interest burden as a percentage of government revenues than is now projected. Wide political differences that have characterized the recent debt and fiscal debate, if they continue, could prevent effective policymaking around that time. Measures that further reduce long-term deficits would be positive for the rating; a lack of such measures would be negative.

Third, recent downward revisions of economic growth rates and the very low growth rate recorded in the first half of 2011 call into question the strength of potential growth in the coming year or two. Continued very low growth would make fiscal consolidation more difficult. As a result, Moody's will also be monitoring the pace of growth as it relates to the fiscal effort.

Finally, the US Treasury's cost of borrowing has remained low despite the recent political uncertainties surrounding the debt limit and the long-term fiscal outlook. While Moody's and economic forecasters generally expect interest rates to rise over the next few years, a rise in borrowing costs above and beyond what is now expected would threaten efforts at fiscal consolidation. Such a development would also be negative for the rating should it occur.

Moody's has also confirmed the Aaa ratings of certain US government-guaranteed bonds issued by the governments of Israel and Egypt, which had been on review for possible downgrade as a result of the review of the US government's bond rating.

The implications of this rating action for directly and indirectly related ratings will be reported presently through a separate press release.

FURTHER INFORMATION

Moody's previously discussed the review of the US government's rating and directly related credits in multiple documents that can be found on: www.moodys.com/USRatingActions

For a complete list of affected securities and additional analysis, please visit: www.moodys.com/USRatingActions.
REGULATORY DISCLOSURES

Please see the rating methodologies tab on the Credit Policy page on moodys.com for the relevant methodology for each action.

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