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## TDC A/S

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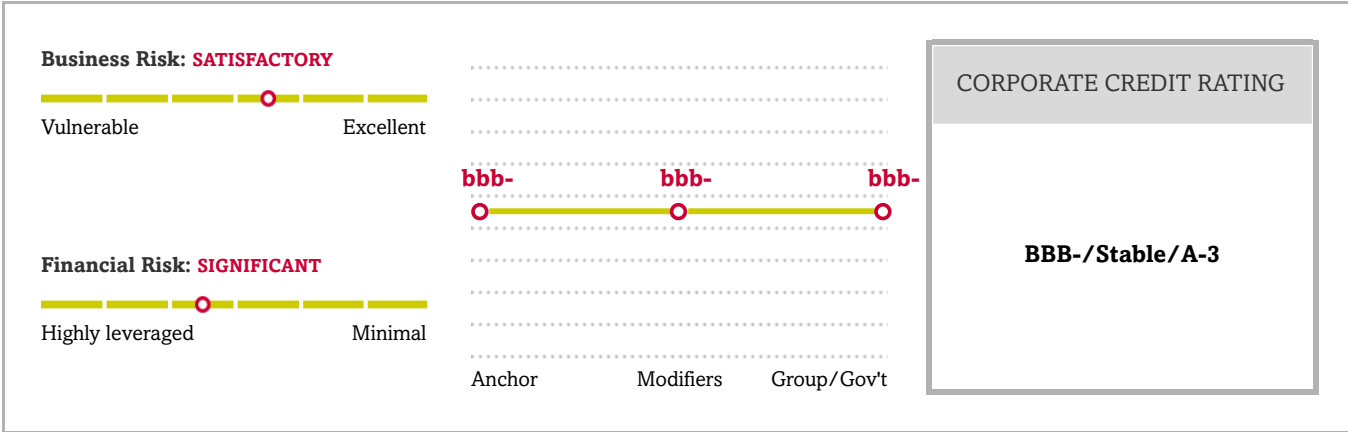
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# TDC A/S



## Rationale

Business Risk: Satisfactory	Financial Risk: Significant
<ul style="list-style-type: none"> <li>• Leading operator in the Danish fixed-line, cable, and mobile telecommunications markets.</li> <li>• Well invested high-speed fourth-generation mobile network, and ownership of both the national copper and largest cable network infrastructures in Denmark.</li> <li>• Growth opportunities in the less competitive Norwegian market, particularly in the consumer fixed segment.</li> <li>• Solid adjusted EBITDA margin exceeding 40%.</li> <li>• Fierce competition in domestic mobile and fixed-line markets, dampening revenues and EBITDA.</li> <li>• Limited scale and international diversification.</li> </ul>	<ul style="list-style-type: none"> <li>• Significant leverage after acquiring Get in 2014, and pressure on domestic EBITDA.</li> <li>• Meaningful free operating cash flow generation.</li> <li>• Relatively robust forecast discretionary cash flow of more than 5% of adjusted debt in 2017 and 2018, supported by dividend cuts in earlier years.</li> </ul>

## Outlook

The stable outlook on Danish telecom network operator TDC A/S mainly reflects S&P Global Ratings' view that the difficult market conditions in Denmark will stabilize over 2017 and 2018. In this outlook, we also factor in that market prices will not further deteriorate materially from current levels, supporting improvements in TDC's domestic operations and EBITDA trends in the next 18 months. We think that this will enable TDC to maintain adjusted debt to EBITDA between 3.0x and 3.5x, funds from operations (FFO) to debt sustainably above 20%, and free operating cash flow (FOCF) to debt at about 8%-10%.

### Upside scenario

We could consider upgrading TDC if domestic market conditions and operations improve more rapidly and significantly than we currently expect, resulting in EBITDA growth, combined with a financial policy that targets adjusted debt to EBITDA of sustainably less than 3.0x and FOCF to debt sustainably above 10%.

### Downside scenario

We could consider a downgrade if TDC's operating performance and EBITDA deteriorated more than we currently expect as a result of continued stiff competition in the domestic market, causing adjusted debt to EBITDA to rise sustainably above 3.5x, FFO to debt to fall below 20%, or FOCF to debt to weaken to less than 8% over a protracted period.

## Our Base-Case Scenario

We think competition in mobile and fixed telecom services in Denmark will remain intense in the next few years, but we do not expect the competition to worsen markedly relative to what we currently observe. Combined with the implementation of cost efficiency measures, we think TDC's domestic EBITDA decline will slow markedly in 2017 and likely stabilize in 2018. The benefits of recent asset disposals, the suspension of 2016 dividend payments and new dividends set from 2017, which are lower than in the years before 2016; and EBITDA growth in Norway; will in our view enable TDC to maintain credit metrics well within the thresholds for the current rating in the next two years.

Assumptions	Key Metrics			
<ul style="list-style-type: none"> <li>Organic revenue decline of 2%-3% in 2017, mainly driven by the business-to-business (B2B) segment and--to a lesser extent--business-to-consumer (B2C) division in Denmark, followed by about flat revenues in 2018, due to easing domestic revenue pressures and growth in Norway.</li> <li>Adjusted EBITDA margins of 42.5%-44.5% in 2017 and 2018, as operating margin pressures are increasingly offset by cost savings.</li> <li>Capital expenditures (capex), including payments for mobile licenses, of about Danish kronor (DKK)4.2 billion--DKK4.5 billion (€565 million--€605 million) in 2017, decreasing to DKK4.0 billion--DKK4.3 billion in 2018, due to lower spending on strategic initiatives and network upgrades in Denmark.</li> <li>Dividend payments of about DKK800 million in 2017 and DKK840 million in 2018, in line with TDC's guidance.</li> </ul>		<b>2016a</b>	<b>2017e</b>	<b>2018e</b>
	EBITDA margin* (%)	43.2	42.5-44.5	42.5-44.5
	FFO to debt* (%)	24.6	23-25	25-27
	Debt to EBITDA* (x)	3.3	3.2-3.4	3.0-3.2
	FOCF to debt* (%)	9.1	8-9	9-11
	<p>*Fully adjusted by S&amp;P Global Ratings. FFO--Funds from operations. FOCF--Free operating cash flow. a--Actual. e--Estimate.</p>			

## Company Description

TDC is the leading telecom network operator in Denmark, providing fixed-line and mobile telephony, broadband, and TV services to consumers and business customers. In Norway, TDC provides cable TV, broadband, and--since 2017--mobile services under the Get brand, predominantly to household consumers, and it offers connectivity services for businesses. At the end of 2016 and excluding wholesale, TDC had approximately 2.6 million mobile subscribers, about 1.6 million broadband subscribers, and 0.7 million fixed-line telephony subscribers, as well as 1.8 million TV customers.

## Business Risk: Satisfactory

Our view of TDC's business risk profile is supported by its position as the leading telecom operator in Denmark, its well-invested mobile network, its ownership of Norwegian cable operator Get, as well as its solid EBITDA margins. At the same time, we consider intense competition in the Danish telecoms market, partly fostered by regulation, and moderate scale as the main constraints.

Although TDC's market shares for certain services have decreased in recent years, as of year-end 2016, the company continued to enjoy relatively high market shares in Denmark for fixed-line telephony services (62%), fixed-line broadband (54%), mobile services (40%), and pay TV (56%), according to company estimates. We also regard TDC's ownership of both the leading domestic copper and cable networks as an advantage, given that these represent alternative infrastructures for provision of TV, broadband, and fixed-line telephony services. For example, as

communicated in TDC's strategy for 2016–2018, this will allow TDC to focus investments on one infrastructure and avoid duplicate spending in areas where both networks overlap. Moreover, TDC's competitive positioning benefits from its well-invested fourth-generation (4G) mobile network, in our opinion. Thanks to investments in recent years, TDC's 4G coverage extended to more than 99.5% of the Danish population at the end of 2016. Furthermore, we think that TDC's ownership of cable operator Get, the second-largest provider of fixed-line broadband and TV in Norway, provides it with additional growth opportunities particularly in broadband. Capitalizing on its high-speed cable network, Get grew its residential broadband revenues by about 10% in 2016 (in local currency) through successful upselling of broadband to its TV customer base and higher average revenues per user (ARPU). As of Dec. 31, 2016, Get's market shares in broadband and TV amounted to 18% and 19%, respectively. Moreover, despite pressure on domestic EBITDA, we expect TDC will continue to produce robust adjusted EBITDA margins of more than 40% in our forecast for the next three years, supported by further efficiency measures.

TDC's exposure to the challenging market conditions in Denmark represents a key weakness in our assessment of its business risk. The company continues to face fierce competition in its B2B division as well as in the B2C segment, in particular for mobile services. This has led to a sharp decrease in revenues and EBITDA. In 2016, TDC's B2C and B2B EBITDA declined by about 7% and about 14%, respectively. However, we observed a partial stabilization of certain price points in consumer mobile over the course of 2016, and TDC managed to even slightly grow its B2C ARPU during the year in spite of headwinds from lower retail roaming rates. Although risks around renewed campaigns by competitors persist, we do not expect pricing in the B2C mobile segment to substantially decrease further from current levels, and we expect a gradual moderation of pricing conditions for business customers and pressure for TDC's B2B ARPUs in the second half of 2017.

Furthermore, in addition to the obligation to provide wholesale access to its fixed line copper network, which is common for EU-based incumbent telecom operators, TDC also offers a broadband wholesale product based on its cable network, which reinforces competition in fixed broadband, in our view. Compared with larger European telecom peers, TDC is characterized by relatively limited scale and geographic diversification.

### Our Base-Case Operating Scenario

- In Denmark, we expect an organic revenue decline of 3%-5% in 2017, slowing to 0% to 2% in 2018, following ongoing repricing of the existing customer base in B2B mobile and continued decline for traditional landline services, as well as some headwinds in fixed-line broadband, where intense competition may constrain pricing and lead to some customer attrition.
- In Norway, we expect revenue growth of 3% to 5% in 2017 and 2018 (in local currency), supported by net customer additions and upselling of higher speeds in residential broadband, the launch of Get mobile, as well as improved revenue trends in the business segment from 2018.
- Adjusted EBITDA margins of 42.5%-44.5% in 2017 and 2018, as the phasing in of cost savings, some margin expansion in Norway, and gradually declining spending on special items compensates for operating pressure on domestic margins.
- NOK/DKK exchange rate of about 0.82 and €/DKK exchange rate of about 7.44.

## Peer comparison

Table 1

TDC A/S -- Peer Comparison				
Industry Sector: Diversified Telecom				
	TDC A/S	Koninklijke KPN N.V.	Elisa Corp.	Telia Company AB
Rating as of April 28, 2017	BBB-/Stable/A-3	BBB-/Positive/A-3	BBB+/Stable/A-2	A-/Negative/A-2
(Mil. €)	--Fiscal year ended Dec. 31, 2016--			
Revenues	2,827.5	6,801.0	1,635.7	8,780.9
EBITDA	1,220.2	2,553.0	599.5	3,133.6
Funds from operations (FFO)	1,001.1	2,002.5	514.0	2,636.0
Net income from continuing operations	264.6	363.0	257.1	1,425.9
Cash flow from operations	969.7	2,025.8	507.5	2,892.8
Capital expenditures	598.8	1,219.0	206.1	1,941.5
Free operating cash flow	370.9	806.8	301.4	951.4
Discretionary cash flow	357.7	329.7	78.2	(651.5)
Cash and short-term investments	226.8	1,319.0	44.5	1,513.6
Debt	4,069.3	8,066.2	1,250.5	8,174.0
Equity	2,881.2	3,361.6	971.3	9,896.1
<b>Adjusted ratios</b>				
EBITDA margin (%)	43.2	37.5	36.7	35.6
Return on capital (%)	6.4	8.2	16.4	9.4
EBITDA interest coverage (x)	7.6	3.8	21.3	9.8
FFO cash int. cov. (x)	5.5	5.7	24.6	11.1
Debt/EBITDA (x)	3.3	3.2	2.1	2.6
FFO/debt (%)	24.6	24.8	41.1	32.2
Cash flow from operations/debt (%)	23.8	25.1	40.6	35.3
Free operating cash flow/debt (%)	9.1	10.0	24.1	11.6
Discretionary cash flow/debt (%)	8.8	4.1	6.3	(8.0)

## Financial Risk: Significant

We derive our assessment of TDC's financial risk profile primarily from the company's significant leverage, resulting from the debt incurred for the acquisition of Get in 2014, and pronounced declines of EBITDA and free cash flow in the last few years. However, we note that TDC has taken a number of measures to prevent deterioration in its credit metrics, such as the suspension of dividend payments in 2016, the setting of more sustainable dividends from 2017, and the disposal of its Swedish subsidiary. We project that these measures, together with our expectation of stabilized EBITDA and FOCF in Denmark in 2017 and 2018, will enable TDC to maintain adjusted debt to EBITDA well within the 3.0x to 3.5x range and adjusted FFO to debt of well above 20% in the next two years. The dividend reductions that TDC implemented will also help to sustain what we view as relatively robust discretionary cash flow (DCF) generation for the rating, with forecast adjusted DCF to debt of 5%-7% in the next 24 months.

### Our Base-Case Cash Flow And Capital Structure Scenario

- Dividend payments of about DKK800 million in 2017 and DKK840 million in 2018, in line with TDC's guidance.
- DKK0.2 billion in annual coupon payments on TDC's hybrid debt.
- Capex, including spectrum payments, of 21%-22% of revenues in 2017, slightly higher than about 21% in 2016, due to planned speed upgrades in TDC's cable network and spending on strategic initiatives, such as the consolidation of IT systems, before decreasing to 20%-21% of revenues in 2018.
- Forecast reported FOCF of DKK2.0 billion–DKK2.2 billion in 2017 and DKK2.1 billion–DKK2.5 billion in 2018.
- Forecast reported DCF of about DKK1.0 billion–DKK1.2 billion in 2017 and DKK1.1 billion–DKK1.5 billion in 2018.

## Financial summary

Table 2

### TDC A/S -- Financial Summary

#### Industry Sector: Diversified Telecom

(Mil. DKK)	--Fiscal year ended Dec. 31--				
	2016	2015	2014	2013	2012
Revenues	21,031.0	24,366.0	23,344.0	24,605.0	26,116.0
EBITDA	9,077.0	10,142.5	9,862.5	10,014.5	10,289.0
Funds from operations (FFO)	7,447.2	8,013.8	7,936.4	7,441.0	7,517.7
Net income from continuing operations	1,968.0	(2,301)	2,463.0	3,119.0	3,593.0
Cash flow from operations	7,213.2	8,246.3	7,623.4	7,710.0	8,223.7
Capital expenditures	4,454.0	4,502.0	3,853.0	3,779.0	3,606.0
Free operating cash flow	2,759.2	3,744.3	3,770.4	3,931.0	4,617.7
Discretionary cash flow	2,661.2	2,141.3	809.4	895.0	1,025.7
Cash and short-term investments	1,687.0	363.0	4,746.0	1,172.0	973.0
Debt	30,267.7	34,427.6	38,789.2	27,133.4	27,074.5
Equity	21,431.0	17,578.0	18,647.0	20,384.0	21,513.0
<b>Adjusted ratios</b>					
EBITDA margin (%)	43.2	41.6	42.2	40.7	39.4
Return on capital (%)	6.4	7.4	8.4	8.5	10.3
EBITDA interest coverage (x)	7.6	7.3	7.2	7.3	7.0
FFO cash interest coverage (x)	5.5	6.2	5.9	5.5	4.9
Debt/EBITDA (x)	3.3	3.4	3.9	2.7	2.6
FFO/debt (%)	24.6	23.3	20.5	27.4	27.8
Cash flow from operations/debt (%)	23.8	24.0	19.7	28.4	30.4
Free operating cash flow/debt (%)	9.1	10.9	9.7	14.5	17.1
Discretionary cash flow/debt (%)	8.8	6.2	2.1	3.3	3.8

Note: All data are S&P Global Ratings-adjusted. DKK--Danish kronor.

## Liquidity: Adequate

The short-term rating is 'A-3'. We assess TDC's liquidity as adequate because we expect that liquidity sources will cover uses by more than 1.2x over the 12 months from Jan. 1, 2017. We think that TDC's risk management aims at ensuring adequate, though not necessarily strong liquidity at all times. In our view, TDC enjoys well-established, solid relationships with its banks.

Principal Liquidity Sources	Principal Liquidity Uses
<p>As of Jan. 1, 2017, principal liquidity sources over the ensuing 12 months include:</p> <ul style="list-style-type: none"> <li>• Cash balances of about DKK1.7 billion.</li> <li>• An undrawn committed unsecured revolving credit facility of €500 million (about DKK3.7 billion) due September 2021, and availability under other committed bilateral lines of about €145 million (about DKK1.1 billion).</li> <li>• Annual FFO of DKK6.4 billion–DKK6.6 billion.</li> </ul>	<p>As of Jan. 1, 2017, principal liquidity uses over the ensuing 12 months include:</p> <ul style="list-style-type: none"> <li>• Annual capex of about DKK4.2 billion–DKK4.5 billion.</li> <li>• Declared dividends of DKK802 million.</li> <li>• Coupon payments on TDC's hybrid debt of about DKK200 million.</li> </ul> <p>TDC's next sizeable debt maturity is a bond of €600 million (DKK4.5 billion) in February 2018.</p>

### Debt maturities\*

On Dec. 31, 2016:

- 2018: €600 million
- 2019: €400 million
- 2020: €350 million
- 2022: €500 million
- 2023: £425 million
- 2027: €800 million

\*Excluding TDC's hybrid debt.

## Covenant Analysis

TDC's backup facilities include a maintenance financial covenant that would be activated only if we lowered the long-term corporate credit rating to below 'BBB-'. In the event that this covenant was triggered, we estimate sufficient headroom of more than 20% in 2017-2018.

## Ratings Score Snapshot

### Corporate Credit Rating

BBB-/Stable/A-3



**Business risk: Satisfactory**

- **Country risk:** Very low
- **Industry risk:** Intermediate
- **Competitive position:** Satisfactory

**Financial risk: Significant**

- **Cash flow/Leverage:** Significant

**Anchor: bbb-****Modifiers**

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

**Reconciliation**

We do not apply a haircut to TDC's reported cash balances because all cash is pooled at the parent level and fully accessible. In arriving at our adjusted EBITDA, we deduct about DKK270 million of restructuring and redundancy costs that we consider to be operating costs. We assess TDC's €750 million hybrid bond as having intermediate equity content and treat 50% of the principal as debt and 50% of the coupons as interest expense.

**Table 3****Reconciliation Of TDC A/S Reported Amounts With S&P Global Ratings Adjusted Amounts (Mil. DKK)**

--Fiscal year ended Dec. 31, 2016--

<b>TDC A/S reported amounts</b>								
	<b>Debt</b>	<b>Shareholders' equity</b>	<b>EBITDA</b>	<b>Operating income</b>	<b>Interest expense</b>	<b>EBITDA</b>	<b>Cash flow from operations</b>	<b>Dividends paid</b>
Reported	24,186.0	24,206.0	8,488.0	3,548.0	782.0	8,488.0	6,828.0	196.0
<b>S&amp;P Global Ratings' adjustments</b>								
Interest expense (reported)	--	--	--	--	--	(782.0)	--	--
Interest income (reported)	--	--	--	--	--	17.0	--	--
Current tax expense (reported)	--	--	--	--	--	(556.0)	--	--
Operating leases	4,366.0	--	720.0	309.8	309.8	410.2	410.2	--
Intermediate hybrids reported as equity	2,776.0	(2,776.0)	--	--	98.0	(98.0)	(98.0)	(98.0)

**Table 3**

<b>Reconciliation Of TDC A/S Reported Amounts With S&amp;P Global Ratings Adjusted Amounts (Mil. DKK) (cont.)</b>								
Postretirement benefit obligations/deferred compensation	--	--	9.0	9.0	--	110.7	64.7	--
Surplus cash	(1,687.0)	--	--	--	--	--	--	--
Share-based compensation expense	--	--	135.0	--	--	135.0	--	--
Dividends received from equity investments	--	--	10.0	--	--	10.0	--	--
Asset retirement obligations	181.7	--	--	--	8.0	(2.7)	(1.7)	--
Non-operating income (expense)	--	--	--	13.0	--	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	--	--	10.0	--
Non-controlling interest/Minority interest	--	1.0	--	--	--	--	--	--
Debt - Accrued interest not included in reported debt	554.0	--	--	--	--	--	--	--
Debt - Derivatives	(109.0)	--	--	--	--	--	--	--
EBITDA - Gain/(Loss) on disposals of PP&E	--	--	(11.0)	(11.0)	--	(11.0)	--	--
EBITDA - Restructuring and redundancy costs	--	--	(274.0)	(274.0)	--	(274.0)	--	--
Total adjustments	6,081.7	(2,775.0)	589.0	46.8	415.8	(1,040.8)	385.2	(98.0)
<b>S&amp;P Global Ratings' adjusted amounts</b>								
	<b>Debt</b>	<b>Equity</b>	<b>EBITDA</b>	<b>EBIT</b>	<b>Interest expense</b>	<b>Funds from operations</b>	<b>Cash flow from operations</b>	<b>Dividends paid</b>
Adjusted	30,267.7	21,431.0	9,077.0	3,594.8	1,197.8	7,447.2	7,213.2	98.0

PP&E--Plant, property, and equipment.

## Related Criteria And Research

### Related Criteria

- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Telecommunications And Cable Industry, June 22, 2014
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Methodology And Assumptions: Assigning Equity Content To Corporate Entity And North American Insurance Holding Company Hybrid Capital Instruments, April 1, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012

- Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- Methodology: Hybrid Capital Issue Features: Update On Dividend Stoppers, Look-Backs, And Pushers, Feb. 10, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

## Related Research

- Credit FAQ: How "Permanence" Affects Our View Of Corporate Hybrid Capital Redemption And Replacement—An Update, Nov. 6, 2014

## Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
<b>Satisfactory</b>	a/a-	bbb+	bbb/bbb-	<b>bbb-/bb+</b>	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

## Ratings Detail (As Of April 28, 2017)

### TDC A/S

Corporate Credit Rating	BBB-/Stable/A-3
Junior Subordinated	BB
Senior Unsecured	BBB-

### Corporate Credit Ratings History

27-Nov-2015	BBB-/Stable/A-3
19-Sep-2014	BBB/Negative/A-2
18-Mar-2014	BBB/Stable/A-2

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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