

Santander Consumer Bank AG

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Table Of Contents

Major Rating Factors

Outlook

Rationale

Related Criteria

Related Research

Santander Consumer Bank AG

SACP	bbb+		+	Support	+1	+	Additional Factors	0
Anchor	a-			ALAC Support	0		Issuer Credit Rating	A-/Stable/A-2
Business Position	Moderate	-1		GRE Support	0		Resolution Counterparty Rating	A/--/A-1
Capital and Earnings	Strong	+1		Group Support	+1			
Risk Position	Moderate	-1		Sovereign Support	0			
Funding	Average	0						
Liquidity	Adequate							

Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> • Large market share in the consumer finance business in Germany. • Strong risk-adjusted profitability and capitalization. • High granularity of the loan portfolio. 	<ul style="list-style-type: none"> • Concentrated exposure to volatility in the consumer finance business. • Margin and volume pressure from intense competition. • Limited growth potential in the saturated German consumer finance market

Outlook: Stable

S&P Global Ratings' outlook on Germany-based Santander Consumer Bank AG (SCB) is stable. The outlook mirrors that on its parent Spain-based Santander Consumer Finance S.A. (SCF; A-/Stable/A-2), as we expect it to remain a core subsidiary and as such be directly affected by its parent's credit profile strengthening or weakening.

Downside scenario

As long as we continue to consider SCB a core member of SCF, any deterioration in SCB's stand-alone credit profile (SACP) would be offset by uplift from extraordinary group support. We could nevertheless lower the rating on SCB if we were to lower the rating on SCF. This could be triggered by a similar action on the ultimate parent Banco Santander or the Spanish sovereign, or if we believed Banco Santander Group's commitment to the SCF consumer finance business had weakened. In addition, a weakening of SCB's importance to SCF could lead us to lower the rating, although we view this as remote over the next 24 months.

Upside scenario

Conversely, a positive rating action on SCF would result in a similar action on SCB. An upgrade of SCF would be triggered by a similar action on both Banco Santander and the sovereign, or by our revision of SCF's status within the group to core.

An improvement in SCB's stand-alone creditworthiness alone would be unlikely to result in an upgrade of SCB. However, an upgrade could follow if we were also to assess SCB as insulated from SCF, or if we anticipated a distinct resolution strategy for SCB, independent from the rest of the group.

Rationale

Santander Consumer Bank AG is the German subsidiary of the Banco Santander Group, with a high market share in the domestic consumer finance business. The bank benefits from the currently low economic risks in Germany, but is exposed to revenue concentration in a more volatile segment of the banking sector. Despite a profit transfer agreement with its intermediate parent, SCB shows a strong capitalization, with a RAC ratio of 12.7%, and would likely benefit from further capital contribution in case of need. This capital strength is, in our view, offset by the concentration of SCB's loan book on consumer finance exposure. The funding and liquidity metrics look somewhat weaker than those of domestic peers, but the bank still benefits from its large share of retail deposits and its comfortable liquidity position. Being part of the wider Santander Group implicitly benefits our SACP assessment.

Furthermore, in our view SCB is a core subsidiary of its intermediate parent Santander Consumer Finance SA (SCF) and contributes about 35% to the parent's lending volume. We expect SCB's strategy will remain aligned with that of Banco Santander Group's consumer finance strategy, such that SCB would benefit from extraordinary group support in case of need. This is reflected in a one notch uplift to its 'bbb+' SACP, resulting in the 'A-' long-term issuer credit rating.

Anchor: 'a-' for banks operating only in Germany

Our bank criteria use our Banking Industry Country Risk Assessment (BICRA) economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating (ICR). Our anchor for a commercial

bank operating mainly in Germany is 'a-', based on an economic risk score of '1' and an industry risk score of '3'. We view the trends for economic risk and industry risk in the German banking industry as stable.

Germany's highly diversified, competitive, and flexible economy continues to perform well against the backdrop of a broader European recovery. The country's high degree of openness exposes it to downside risks from the external environment, but Germany's important buffers, such as a sizable net external creditor position and fiscal surpluses, should allow its economy to absorb external shocks and remain resilient. We expect Germany's strong house price growth will continue to cool, and increasing supply, falling demand, and gradually rising interest rates will ease price pressures. Moreover, dynamic house price increases were not the result of strong mortgage growth and we still consider a nationwide housing bubble unlikely over the next few years. Domestic nonperforming loans and associated credit loss provisions have bottomed out since their 2010 peak, but we expect they will remain in a favorable credit cycle for some time.

As for many European banking industries, industry risk in Germany is intermediate, in our view. Returns in the German banking industry are broadly in line with many European peers' owing to low domestic credit losses and stability from granular earnings generation, but low interest rates and strong competition drag on profitability. Rising interest rates, which we expect from the second half of 2019, should increase German banks' profitability, while cost-reducing and efficiency-enhancing measures will improve German banks' unfavorable cost efficiency and fee generation ability. Generally sound underwritings practices should protect German banks' profitability from a rise in risk cost that typically accompanies material interest rates increases.

Well-funded and strongly capitalized savings and cooperative banking groups will continue to dominate Germany's retail banking market. Large banks, which carry riskier concentration and business risk, have become less vulnerable to economic risks due to deleveraging, de-risking, and recapitalization. The German banking system's institutional framework benefits from implemented and expected regulatory reforms resolving major deficiencies and improving accountability and transparency. The likelihood of the German government providing extraordinary support to systemic domestic banks is uncertain.

Table 1

Santander Consumer Bank AG Key Figures					
--Year-ended Dec. 31--					
(Mil. €)	2017	2016	2015	2014	2013
Adjusted assets	42,221.8	43,201.5	41,810.3	38,283.7	36,438.4
Customer loans (gross)	31,420.6	31,547.8	30,860.7	30,850.8	31,164.1
Adjusted common equity	2,546.3	2,511.9	2,747.9	2,710.0	2,606.3
Operating revenues	1,423.2	1,435.6	1,494.9	1,576.8	1,396.1
Noninterest expenses	838.2	807.4	850.8	906.2	829.9
Core earnings	486.9	532.0	511.6	563.9	466.2

Business position: Concentrated position in the German consumer finance market

We consider SCB's business position to be moderate, owing to its fairly concentrated business model. We see it as potentially more susceptible to swings in economic trends than a traditional retail bank's business model, however we note that SCB's operating income after credit losses proved relatively stable over the last economic cycle. Moreover,

Germany's highly competitive consumer finance market continues to limit SCB's growth potential as it aims to maintain risk-adjusted profitability. While the corporate banking activities have the potential to further diversify SCB's revenue streams and to profit from the global franchise of Banco Santander Group, we regard this more as a long-term possibility. Also, the retail mortgage business will only gradually develop, in our view.

These weaknesses are only partly offset by SCB's strong domestic market share of about 13% in the niche auto loan and consumer finance market. SCB's consumer finance division has one of the most cost-efficient operations among its peers. Its business position also benefits from the increased diversification realized through the acquisition of SEB AG's retail operations in 2011, which added domestic retail mortgages to the portfolio.

We expect the ongoing restructuring of its brands and branch network will have a positive earnings impact from 2020, through reduced operating costs and increased revenues. SCB's 2017 result was negatively impacted by €94.5 million in restructuring charges. We believe the increased efficiency will nevertheless enable SCB to better cope with a continued low interest environment and largely defend its market share in a very competitive market.

Table 2

Santander Consumer Bank AG Business Position					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Loan market share in country of domicile	N/A	1.1	1.1	1.1	1.2
Deposit market share in country of domicile	N/A	0.7	0.8	0.8	0.9
Total revenues from business line (currency in millions)	1,423.2	1,435.6	1,537.8	1,576.8	1,396.1
Retail banking/total revenues from business line	100.0	100.0	100.0	100.0	100.0
Commercial & retail banking/total revenues from business line	100.0	100.0	100.0	100.0	100.0
Return on average common equity	12.8	17.3	17.9	3.6	15.5

N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

Capital and earnings: Strong capitalization, despite profit transfer agreement

We assess SCB's capital and earnings as strong. This is based primarily on our forecasted S&P Global Ratings risk-adjusted capital (RAC) ratio of 12.0%-12.5% over the next two years. SCB usually upstreams all of its profits to SCF, based on a profit transfer agreement, and has historically been managed with a small capital buffer above the minimum requirements. Based on a common equity Tier 1 ratio of 12.5% as of year-end 2017, coupled with the bank's ambition to expand its lending business over the next few years, we expect a slight deterioration of our RAC ratio from 12.7% as of year-end 2017. The higher ratio compared to last year is mainly driven by the introduction of our revised risk-adjusted capital methodology.

We believe SCB's earnings generation, as a potential first line of defence in case of increasing credit losses, will remain strong, thanks to stable high-margin lending. We estimate an earnings buffer, which measures the capacity for a bank's preprovision earnings to cover normalized (annual average through the cycle) losses, of around 200 basis points (bps), which is stronger than that of most German retail banks.

Table 3

Santander Consumer Bank AG Capital And Earnings					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Tier 1 capital ratio	12.5	13.2	12.8	12.3	10.1
S&P Global Ratings' RAC ratio before diversification	12.7	12.6	12.1	11.8	11.5
S&P Global Ratings' RAC ratio after diversification	12.2	11.8	12.2	11.9	12.0
Adjusted common equity/total adjusted capital	99.9	99.8	99.8	99.8	99.8
Net interest income/operating revenues	79.6	80.6	78.7	74.6	76.9
Fee income/operating revenues	10.6	12.4	14.7	18.3	19.8
Market-sensitive income/operating revenues	(0.2)	0.0	N/A	N/A	N/A
Noninterest expenses/operating revenues	58.9	56.2	56.9	57.5	59.4
Preprovision operating income/average assets	1.4	1.5	1.6	1.8	1.5
Core earnings/average managed assets	1.1	1.2	1.3	1.5	1.3

N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

Table 4

Santander Consumer Bank AG RACF [Risk-Adjusted Capital Framework] Data					
(€ 000s)	Exposure*	Basel III RWA	Average Basel III RW (%)	S&P Global RWA	Average S&P Global RW (%)
Credit risk					
Government and central banks	1,761,687	0	0	12,216	1
Of which regional governments and local authorities	255,368	0	0	9,193	4
Institutions and CCPs	1,313,598	244,694	19	295,955	23
Corporate	8,303,285	6,186,300	75	5,228,032	63
Retail	21,872,614	10,125,275	46	10,734,357	49
Of which mortgage	4,089,370	454,963	11	828,237	20
Securitization§	2,077,866	453,216	22	919,955	44
Other assets†	385,472	233,225	61	347,125	90
Total credit risk	35,969,890	17,242,709	48	17,537,640	49
Credit valuation adjustment					
Total credit valuation adjustment	--	8,524	--	0	--
Market risk					
Equity in the banking book	3,956	1,191,113	30,108	34,616	875
Trading book market risk	--	0	--	0	--
Total market risk	--	1,191,113	--	34,616	--
Operational risk					
Total operational risk	--	2,278,517	--	2,532,856	--
(€ 000s)	Basel III RWA		S&P Global RWA	% of S&P Global RWA	
Diversification adjustments					
RWA before diversification	20,720,863		20,105,111	100	

Table 4

Santander Consumer Bank AG RACF [Risk-Adjusted Capital Framework] Data (cont.)				
Total Diversification/Concentration Adjustments	--		788,448	4
RWA after diversification	20,720,863		20,893,560	104
(€ 000s)	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	2,618,248	12.6	2,548,865	12.7
Capital ratio after adjustments†	2,618,248	12.6	2,548,865	12.2

*Exposure at default. §Securitisation Exposure includes the securitisation tranches deducted from capital in the regulatory framework. †Other assets includes Deferred Tax Assets (DTAs) not deducted from ACE. ‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of Dec. 31, 2017, S&P Global.

Risk position: Concentration risk in consumer finance loans

In our view, SCB's overall risk position is moderate and a relative weakness compared to larger peers. Our assessment reflects concentration risk in its loan book because it is heavily weighted toward German consumer finance exposures. We view the credit quality of such exposures as inherently more volatile and losses in a stress environment might be higher than for secured retail banking products like mortgages. In a severe economic downturn, losses could accumulate rather quickly. However, we note SCB's track record of limited losses compared with those of its pure consumer finance peers, demonstrating a more conservative approach to risk.

The current economic environment in Germany results in very favorable risk metrics, with a nonperforming loan ratio of 2.2% and cost of risk of 31 bps in 2017, on the same level as in 2016. We anticipate that these metrics have likely bottomed out and that cost of risk will normalize to 50 bps-100 bps over the medium term.

We understand that SCB intends to grow its retail mortgage as well as its corporate businesses but we doubt that this would lead to a material improvement in risk diversification within the next two-to-three years. In our view, the loan portfolio will continue to be dominated by car financing and unsecured consumer lending.

Table 5

(%)	--Year-ended Dec. 31--				
	2017	2016	2015	2014	2013
Growth in customer loans	(0.4)	2.2	0.0	(1.0)	(1.1)
Total diversification adjustment/S&P Global Ratings' RWA before diversification	3.9	(3.9)	(0.7)	(0.4)	(3.8)
Total managed assets/adjusted common equity (x)	16.7	17.3	15.3	14.3	14.2
New loan loss provisions/average customer loans	0.3	0.3	0.4	0.3	0.3
Gross nonperforming assets/customer loans + other real estate owned	2.2	2.1	2.9	3.2	3.5
Loan loss reserves/gross nonperforming assets	89.5	96.3	94.7	92.2	99.1

Funding and liquidity: Franchise-based and online deposits, complemented by securitizations

Our assessment of SCB's funding profile as average in comparison with domestic peers considers relatively weak quantitative metrics that are offset by qualitative factors and its diversified funding sources. In 2017, SCB issued its first

senior bond of €500 million and its first covered bond (Pfandbrief) of €250 million. We expect further issuances in the coming years. In 2018, SCB also started its €3 billion Euro Commercial Paper program, which adds short-term flexibility.

The stable funding ratio, S&P Global Ratings' measure of available long-term funding relative to long-term funding needs, was 79% in 2017. This level is lower than local peers, who often show ratios comfortably above 100%. However, we expect this ratio will improve in the medium term with the issuance of covered bonds and senior unsecured bonds. We believe granular retail deposits, which currently cover 59% of the funding base, will remain the main funding source for SCB. While asset-backed securities (ABS) have historically been an important funding vehicle for SCB, the bank has recently retained most of them on its own balance sheet as available collateral for opportunistic funding from the European Central Bank (ECB).

In our view, SCB will have sufficient and highly diversified sources to unwind ECB funding until 2020. Selling the retained ABS to the market will also gradually benefit the quantitative metrics.

SCB's liquidity is adequate, in our view, based on the bank's negligible reliance on short-term wholesale funding. Its broad liquid assets cover 9% of its customer deposits, which is relatively weak in a peer comparison. We take comfort though, from its additional liquidity buffers in retained ABS, which we do not acknowledge as liquid assets but which could be sold in case of need. SCB has also proven its secured funding capability throughout the cycle. In addition, we consider the potential benefits and stability provided by SCB's membership in the Banco Santander Group, although no committed facilities exist to our knowledge. The regulatory liquidity coverage ratio was 133.6% as of year-end 2017.

Table 6

Santander Consumer Bank AG Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2017	2016	2015	2014	2013
Core deposits/funding base	74.2	77.5	81.1	88.9	89.9
Customer loans (net)/customer deposits	137.0	130.0	120.9	117.1	110.6
Long-term funding ratio	96.5	97.3	85.5	94.2	95.9
Stable funding ratio	79.5	79.8	74.8	80.9	90.3
Short-term wholesale funding/funding base	3.9	2.9	15.8	6.4	4.4
Broad liquid assets/short-term wholesale funding (x)	1.7	2.7	0.8	0.9	1.2
Net broad liquid assets/short-term customer deposits	4.3	7.1	(5.0)	(0.8)	1.1
Short-term wholesale funding/total wholesale funding	14.9	12.9	83.5	57.3	43.7
Narrow liquid assets/3-month wholesale funding (x)	5.2	3.0	0.8	1.2	1.4

Support: One notch uplift for parental support

The long-term rating on SCB is one notch higher than its intrinsic creditworthiness reflected in the SACP, because we align the rating with that on its intermediate parent company, Spanish Santander Consumer Finance SA. This reflects our expectation of extraordinary group support in case of need.

Our ratings on SCB do not benefit from uplift for additional loss-absorbing capacity. We understand that, unlike other group subsidiaries, the German operations have not been identified as a separate point of entry in the event of a

resolution of Banco Santander. Nevertheless, the rating on SCB could also benefit from the build-up of additional loss-absorbing capacity at the Banco Santander level.

Issue Ratings

The 'A-' issuer credit rating incorporates one notch of group support on top of the 'bbb+' SACP. We think this group support would also flow to SCB's outstanding senior subordinated bond. For the bond rating of 'BBB+' we deduct one notch from the 'A-' issuer credit rating to reflect the statutory subordination under German law, which makes these vanilla senior bonds subordinate in liquidation and resolution to other senior claims.

Resolution Counterparty Ratings (RCR)

We have assigned 'A/A-1' Resolution Counterparty Ratings (RCR) to SCB as we assess the resolution regime in Germany to be effective and the bank as likely to benefit from bail-in resolution powers being applied to the group if it reaches nonviability.

The RCR is a forward-looking opinion of the relative default risk of certain senior liabilities that may be protected from default through an exemption from bail-in.

Related Criteria

- Criteria - Financial Institutions - General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria - Financial Institutions - General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria - Financial Institutions - Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Santander Consumer Bank AG's New Commercial Paper Program Assigned 'A-2' Rating, June 20, 2018
- Germany-Based Santander Consumer Bank AG's Senior Unsecured Nonpreferred Notes Assigned 'BBB' Rating, Sept. 25, 2017
- Reduced Funding Risks Lead To Upgrades At Several Spanish Banks, April 6, 2018

- Banco Santander S.A., March 16, 2018
- Santander Consumer Finance S.A., Jan. 26, 2018
- Banking Industry Country Risk Assessment: Germany, Nov. 2, 2018

Anchor Matrix										
Industry Risk	Economic Risk									
	1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of December 6, 2018)

Santander Consumer Bank AG

Issuer Credit Rating	A-/Stable/A-2
Resolution Counterparty Rating	A/--/A-1
Commercial Paper	A-2
Senior Subordinated	BBB+

Issuer Credit Ratings History

06-Apr-2018	A-/Stable/A-2
12-Jun-2017	BBB+/Stable/A-2
03-Apr-2017	BBB+/Positive/A-2
30-Mar-2017	BBB+/Stable/A-2

Sovereign Rating

Germany	AAA/Stable/A-1+
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Related Entities

Abbey National Capital Trust I

Preferred Stock	BB
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Banco Santander (Brasil) S.A.

Issuer Credit Rating	BB-/Stable/B
<i>Brazil National Scale</i>	brAAA/Stable/brA-1+
Junior Subordinated	CCC
Subordinated	B-

Banco Santander-Chile S.A.

Issuer Credit Rating	A/Stable/A-1
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Ratings Detail (As Of December 6, 2018) (cont.)

Commercial Paper	
<i>Foreign Currency</i>	A-1
Senior Unsecured	A
Subordinated	A-
Banco Santander S.A.	
Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/--/A-1
Certificate Of Deposit	
<i>Local Currency</i>	A-1
Senior Subordinated	A-
Senior Unsecured	A
Short-Term Debt	A-1
Subordinated	BBB+
Banco Santander S.A. (New York Branch)	
Commercial Paper	
<i>Foreign Currency</i>	A-1
Banco Santander Totta S.A.	
Issuer Credit Rating	BBB-/Positive/A-3
Resolution Counterparty Rating	BBB/--/A-3
Senior Unsecured	BBB-
PSA Banque France	
Issuer Credit Rating	BBB/Stable/A-2
Commercial Paper	A-2
Senior Unsecured	BBB
Santander Bank, N.A.	
Issuer Credit Rating	A-/Stable/A-2
Senior Unsecured	A-
Short-Term Debt	A-2
Subordinated	BBB+
Santander Consumer Finance S.A.	
Issuer Credit Rating	A-/Stable/A-2
Resolution Counterparty Rating	A/--/A-1
Commercial Paper	
<i>Local Currency</i>	A-2
Senior Subordinated	A-2
Senior Subordinated	BBB+
Senior Unsecured	A-
Short-Term Debt	A-2
Subordinated	BBB
Santander Holdings U.S.A Inc.	
Issuer Credit Rating	BBB+/Stable/A-2
Preferred Stock	BB+
Senior Unsecured	BBB+

Ratings Detail (As Of December 6, 2018) (cont.)

Santander UK Group Holdings PLC

Issuer Credit Rating	BBB/Stable/A-2
Junior Subordinated	B+
Senior Unsecured	BBB
Short-Term Debt	A-2
Subordinated	BB+

Santander UK PLC

Issuer Credit Rating	A/Stable/A-1
Resolution Counterparty Rating	A+/-/A-1
Junior Subordinated	BB
Junior Subordinated	BB+
Preference Stock	BB
Senior Unsecured	A
Short-Term Debt	A-1
Subordinated	BBB-

Sovereign Real Estate Investment Trust

Preferred Stock	BB+
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*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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