

RatingsDirect®

Jyske Bank A/S

Primary Credit Analyst:

Sean Cotten, Stockholm (46) 8-440-5928; sean.cotten@spglobal.com

Secondary Contact:

Helena Cederloef, Stockholm (46) 8-440-5920; helena.cederloef@spglobal.com

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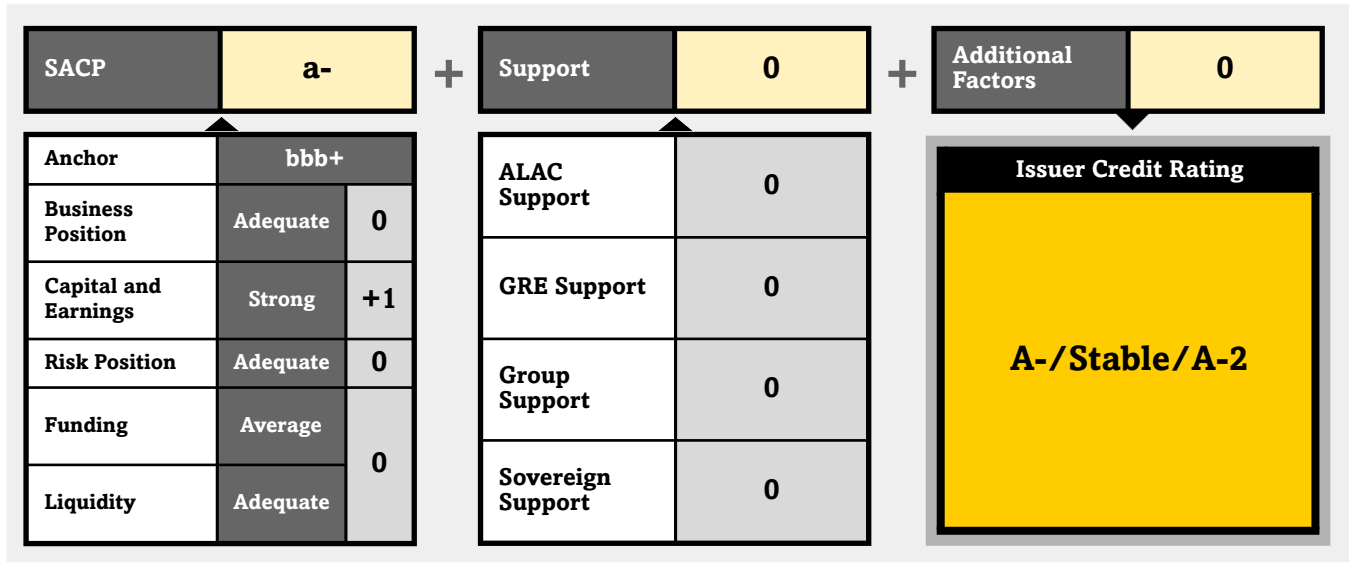
Major Rating Factors

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Related Criteria And Research

Jyske Bank A/S



Major Rating Factors

Strengths:	Weaknesses:
<ul style="list-style-type: none"> • A strong domestic franchise in retail and commercial banking. • Strong capitalization. • Resilient core earnings and profitability, despite low interest rate environment. 	<ul style="list-style-type: none"> • Relatively weak, but improving, asset quality metrics. • Use of short-term wholesale funding for mortgage loans. • Limited geographic diversity.

Outlook: Stable

The stable outlook on Jyske Bank A/S reflects S&P Global Ratings' view that Jyske will maintain a risk-adjusted capital (RAC) ratio sustainably above 10%. Our view of capital considers the bank's planned buy-back activity, resumption of dividend payments, and recent issuance of hybrid capital. It is also supported by stronger and more stable earnings, resulting from improved efficiency as the bank begins to benefit from synergies following the April 2014 merger with BRFkredit.

While presently unlikely, we could consider an upgrade if bail-in risks for senior unsecured creditors were reduced by the development of a significant additional loss-absorbing capacity (ALAC) buffer, which is not otherwise recognized in our strong capital assessment.

We could consider a downgrade if the bank is unable to maintain progress in terms of asset quality metrics. In particular, a reversal of the recent improvements in loan impairments could lead us to reassess the group's risk position or change our capital projections. We continue to monitor the improvements in refinancing risk for Denmark's mortgage institutions, including Jyske's subsidiary, BRFkredit. We could lower the ratings if the trend of improvement in the funding and liquidity profile were to reverse.

Rationale

We base the ratings on Jyske on its 'a-' anchor, and our view of the group's adequate business position as Denmark's fourth-largest banking group with a strategic focus on growing its share of the domestic mortgage market. Jyske's capital and earnings position is strong, in our view. We project the RAC ratio to remain between 10.5%-11.0% over the next two years, from 10.2% in June 2016. We assess Jyske's risk position as adequate and expect continued improvements in the asset quality of the bank in combination with declining risks of further provisions as the Danish economy improves. Our view of Jyske's funding as average and liquidity as adequate reflects continued measures to improve the maturity profile of BRFkredit's covered bond funding.

Anchor: 'bbb+' given that Jyske operates predominantly in Denmark

Under our bank criteria, we use our Banking Industry Country Risk Assessment's economic risk and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. Our anchor for a commercial bank operating only in Denmark is 'bbb+', based on an economic risk score of '3' and an industry risk score of '4'.

We view Denmark as a politically stable, wealthy, and high-income country that has suffered since the 2008-2009 global financial market crisis. The economy is competitive and diverse and once again in an expansionary phase, with house price appreciation and credit growth expected to increase in the coming two years. Although decreasing, household debt remains high and a constraint to our assessment of economic risk. Consequently, we expect Denmark's economy will continue improving, supported by its balanced fiscal policy flexibility and strong external position following a decade of sizable current account surpluses.

We view the regulatory environment in Denmark as in line with that of other EU countries. We observe an overall improvement in the banking sector's profitability that, in our view, should continue through cost-cutting and decreasing losses. This should enable the sector, including lower yielding mortgage banks, to report a return on equity (ROE) of 8%-9% for 2016-2017. We also note the banking sector's higher reliance than peers' on functioning wholesale markets. However, we expect this dependence will reduce further, due to continuing measures by individual banks and the regulator.

Table 1

Jyske Bank A/S Key Figures					
	--Year-ended Dec. 31--				
(Mil. DKK)	2016*	2015	2014	2013	2012
Adjusted assets	562,401	543,311	541,566	261,933	258,207
Customer loans (gross)	389,117	360,888	345,089	115,364	110,071
Adjusted common equity	28,877	28,310	27,068	17,047	15,258
Operating revenues	6,907	10,241	8,518	8,239	7,516
Noninterest expenses	4,110	5,615	5,533	4,791	4,825
Core earnings	1,914	2,515	445	1,808	596

*Data as of Sept. 30.

DKK--DKK-Danish krone. N.A.--Not available. N/A--Not applicable. N.M.--Not meaningful.

Business position: Diversified revenues by segment and nationwide business coverage

We assess Jyske's business position as adequate. At September 2016, Jyske's consolidated assets were Danish krone (DKK) 562 billion (€75 billion at DKK7.43 to €1), placing it just outside of Europe's top-50 banks by size. The Jyske Bank Group, including mortgage lending BRFKredit, is the fourth-largest lender in Denmark and has about 10% market share of system-wide loans and core customer deposits, reflecting significant growth in mortgage lending since 2014.

Jyske's retail banking and mortgage lending provide revenue and nationwide coverage, resulting in a business risk profile that, in our view, reflects the risks associated with the Danish economy. Jyske has historically been particularly strong in small and mid-size enterprise (SME) lending and deposit gathering in the Jutland region. However, the acquisition of BRF in 2014 increased its exposure to residential and commercial real estate customer base in the Copenhagen and Aarhus regions. Jyske is also the largest shareholder in agricultural mortgage lender DLR Kredit, where it owns 12.6%.

Jyske continues to increase its relative share of mortgage lending as Danish corporates continue to deleverage. The mortgage growth has more than offset the decline in corporate and SME lending, lowering the bank's overall risk profile and reducing top line margins (chart 1).

We anticipate that Jyske's strategy of focusing on relationship-based commercial banking for households and SMEs will remain its focus. Jyske also provides other value-added services such as asset management, mainly to retail clients, and develops cost-sharing structures with other smaller Danish banks to improve its IT efficiency.

We believe Jyske has a strong and stable management team and a prudent corporate strategy that has helped it to weather the Danish banking crisis without needing extraordinary capital or liquidity support from the state. The bank continues to optimize its capital base with share buybacks, dividends, and by issuing hybrid capital instruments. We anticipate a long-term return on equity of 10%, excluding one-off and restructuring costs, although negative interest rates present challenges to revenue levels even as the bank reduces staff and expenses.

Chart 1

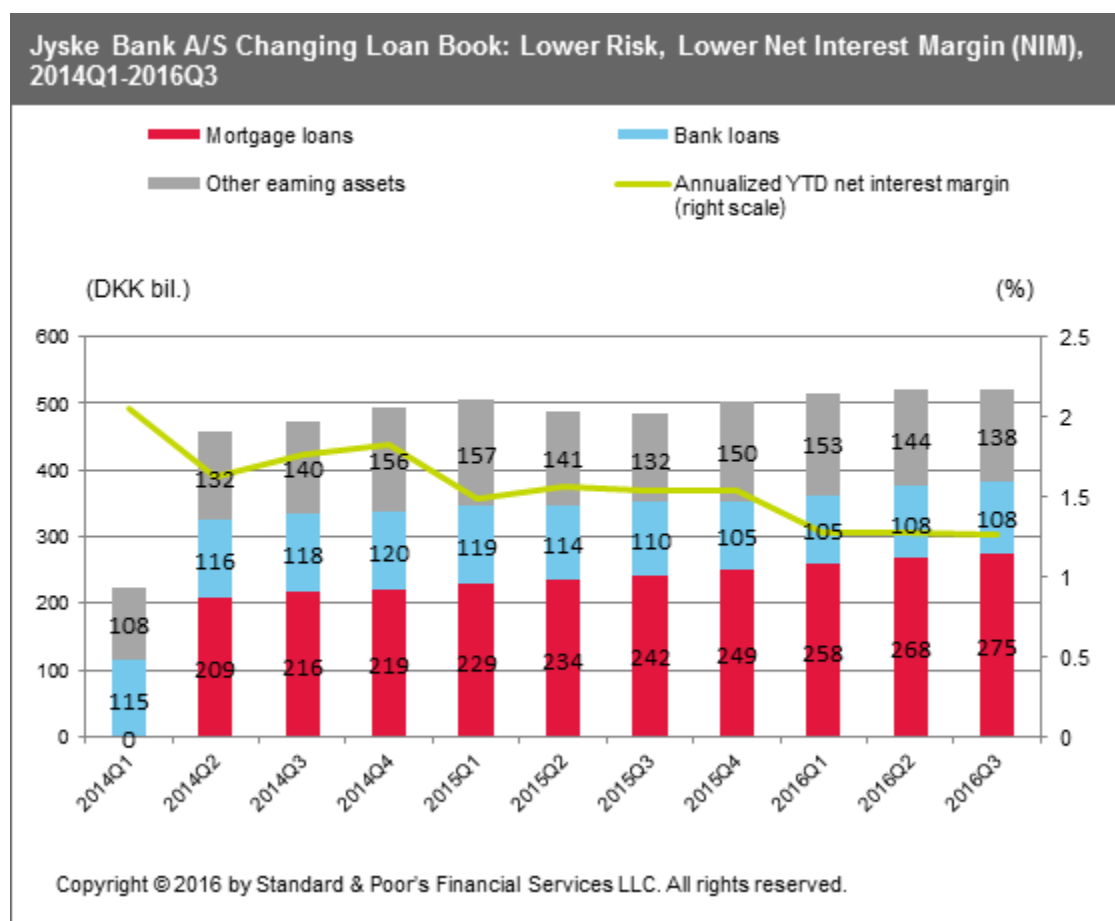


Table 2

Jyske Bank A/S Business Position

	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Loan market share in country of domicile	9.8	9.3	8.9	3.0	2.9
Deposit market share in country of domicile	10.0	9.6	10.1	9.6	8.1
Total revenues from business line (currency in millions)	6,907	10,241	11,174	8,239	7,516
Commercial & retail banking/total revenues from business line	83.0	77.5	63.6	86.6	85.8
Trading and sales income/total revenues from business line	N/A	N/A	N/A	6.0	8.1
Other revenues/total revenues from business line	17.0	22.5	36.4	7.4	6.1
Investment banking/total revenues from business line	N/A	N/A	N/A	6.0	8.1
Return on equity	8.4	8.6	13.7	10.9	4.0

*Data as of Sept. 30.

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

Capital and earnings: Continued strengthening of capital ratios expected, mainly driven by retained earnings

We assess Jyske's capital and earnings as strong. We project the RAC ratio to remain between 10.5%-11.0% over the

next two years, from its June 2016 level of 10.2%. Jyske issued DKK1.5 billion in additional tier 1 capital in the third quarter of 2016 and the proforma RAC ratio was 10.7% as of June 2016, given the intermediate equity content of the instrument (see chart 2).

The bank is undergoing a capital optimization through 2017 with share buy-backs and dividend distributions. The share buy-back program is now DKK1 billion and the bank's guidance is for 2016 dividends to be in line with 2015 (DKK500 million). This transition is included in our capital forecast and we still view the quality of capital as high, with hybrids representing only 5% of the capital included in our RAC ratio and considerable flexibility to reduce dividend and buy back activity during a stress.

Jyske's regulatory CET1 capital ratio and total capital ratio were 15.9% and 17.8%, respectively, at September 2016. The bank aims to maintain a total capital ratio of 17.5% and CET1 ratio of 14% in the long term, which will ensure meeting future regulatory requirements and supporting our expectation of a RAC ratio above 10%. In addition, the bank issued tier 2 capital in May 2016 offsetting the decline in equity in its regulatory capital ratio. We believe the bank would reconsider its buy-back activity if regulatory capital requirements were to increase materially as a result of proposed standardized risk weights and/or floors.

Despite increased diversification, the lower risk profile due to larger mortgage volumes and lower demand for corporate lending are pressuring top line revenues. In addition, margins on bank lending and deposits continue to be pressured by low interest rates. We note that increases in the market level of administration fees on mortgage loans could eventually improve revenues, though the bank continues to focus on growth via lower margins. We expect operating expenses to decline as the bank continues to focus on improving efficiency, and we forecast the long-term cost-to-income ratio to be around 55%-60% until the interest rate environment changes. This results in expected annual net profits exceeding DKK2.5 billion by 2017. Core earnings to adjusted assets have plateaued at 0.46% over the last two years and are expected to remain that way unless the bank materially changes the administration fees for mortgage lending.

As the bank increases its efficiency, our earnings buffer metric is expected to improve to over 100 basis points (bps), indicating that the bank's earnings generation provides a meaningful cushion to absorb normalized losses of DKK1.5 billion--well above our annual loss expectations over the two-year rating horizon.

Chart 2

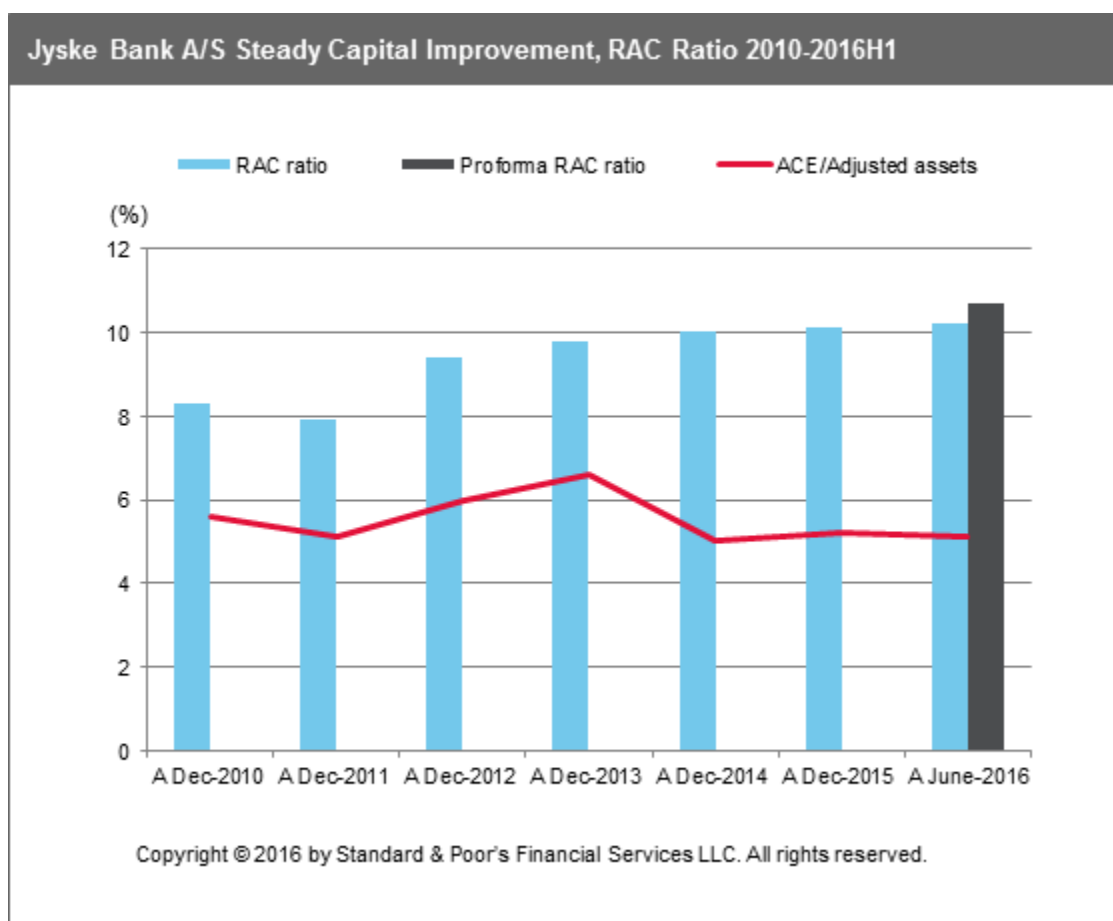


Table 3

Jyske Bank A/S Capital And Earnings					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Tier 1 capital ratio	17.1	16.5	15.8	15.9	15.3
S&P RAC ratio before diversification	N.M.	10.4	10.0	9.8	9.4
S&P RAC ratio after diversification	N.M.	9.8	9.4	9.7	9.0
Adjusted common equity/total adjusted capital	95.2	100.0	100.0	100.0	100.0
Net interest income/operating revenues	70.3	75.2	77.7	60.9	64.9
Fee income/operating revenues	14.9	17.9	20.7	21.0	22.0
Market-sensitive income/operating revenues	7.3	1.0	(6.7)	7.2	4.0
Noninterest expenses/operating revenues	59.5	54.8	65.0	58.2	64.2
Provision operating income/average assets	0.7	0.9	0.7	1.3	1.0
Core earnings/average managed assets	0.5	0.5	0.1	0.7	0.2

*Data as of Sept. 30.

Table 4

Jyske Bank A/S RACF [Risk-Adjusted Capital Framework] Data					
(Mil. DKK)	Exposure*	Basel II RWA	Average Basel II RW (%)	S&P Global Ratings RWA	Average S&P Global Ratings RW (%)
Credit risk					
Government and central banks	16,680	0	0	526	3
Institutions	93,852	5,866	6	5,312	6
Corporate	161,545	76,597	47	107,672	67
Retail	266,977	47,028	18	86,991	33
Of which mortgage	229,057	34,810	15	62,813	27
Securitization§	615	137	22	242	39
Other assets	6,015	6,070	101	6,787	113
Total credit risk	545,685	135,698	25	207,531	38
Market risk					
Equity in the banking book†	2,661	5,791	218	20,706	778
Trading book market risk	--	21,738	--	32,606	--
Total market risk	--	27,529	--	53,312	--
Insurance risk					
Total insurance risk	--	--	--	0	--
Operational risk					
Total operational risk	--	17,032	--	22,439	--
(Mil. DKK)		Basel II RWA		S&P Global Ratings RWA	% of S&P Global Ratings RWA
Diversification adjustments					
RWA before diversification		180,259		283,282	100
Total Diversification/Concentration Adjustments		--		12,565	4
RWA after diversification		180,259		295,848	104
(Mil. DKK)		Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global Ratings RAC ratio (%)
Capital ratio					
Capital ratio before adjustments		29,548	16.4	28,773	10.2
Capital ratio after adjustments‡		29,548	16.4	28,773	9.7

*Exposure at default. §Securitisation Exposure includes the securitisation tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡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. DKK--Danish krone. Sources: Company data as of June. 30, 2016, S&P Global Ratings.

Risk position: Asset quality metrics improving as Denmark's economy strengthens

Jyske's risk position is adequate, in our view. The quality of the bank's domestic loan book is in line with our assessment of industry risk for the Danish banking system based on our BICRA methodology. BRFKredit's collateralized loan book provides regional and product diversification to Jyske's SME-focused loan book, and we expect asset quality metrics to continue to show steady improvement.

Jyske continues to report a considerable reduction in loan impairment charges (DKK381 million through September 2016 compared to DKK1,372 million in 2015 and DKK2,536 million in 2014), reflecting a reduction in general provisions and net reversals for the non-agriculture portfolio in 2016. Given general improvements in the Danish economy coupled with continued pressure on the agriculture sector, for which the bank has already made significant provisions, we expect losses to remain at about 20 bps of loans over the next two years. However, right-sizing of general provisions and reversals could lead to volatility over the next two years.

Net nonperforming loans (NPLs) also showed considerable improvement in the first three quarters of 2016, we expect these trends to continue in the broader Danish economy. Gross NPLs were at 5.35% as of September 2016 and net NPLs 3.9%, both relatively high versus larger domestic peers but generally falling for banking and mortgage customers. In addition, we note the reduction in the risk profile due to the relative increase in retail mortgage lending. New residential mortgage loans are expected to keep the total loan growth at about 7% in 2016 and 2017 and will improve overall asset quality as the portfolio balances more toward these lower risk assets.

While the Danish economy continues to improve, high risk segments remain--related to agriculture. Milk producers and pig farming (less than 1% of total lending) are the most affected segments, but are already well provisioned. Improvements in pork prices during 2016 have provided hope for improved asset quality and profitability of the sector, but the recovery remains sensitive. At September 2016, the individual balance of loan impairment charges and provisions for guarantees relating to milk producers amounted to 45% of loans, advances and guarantees, and 27% related to pig farming. At September 2016, the total impairment ratio for milk producers and pig farming, inclusive of collective impairment charges, came to 35% of lending for these segments.

Table 5

Jyske Bank A/S Risk Position					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Growth in customer loans	10.4	4.6	199.1	4.8	(1.7)
Total diversification adjustment / S&P RWA before diversification	N.M.	6.1	5.9	1.5	3.7
Total managed assets/adjusted common equity (x)	19.5	19.2	20.0	15.4	16.9
New loan loss provisions/average customer loans	0.1	0.4	1.1	1.0	1.7
Net charge-offs/average customer loans	0.3	0.3	0.5	1.1	1.0
Gross nonperforming assets/customer loans + other real estate owned	5.4	6.9	7.2	8.9	8.1
Loan loss reserves/gross nonperforming assets	28.6	24.9	23.2	41.2	46.3

*Data as of Sept. 30.

Funding and liquidity: Funding profile now similar to larger Danish peers

We consider Jyske Bank's funding to be average and liquidity to be adequate. Jyske's group funding profile is similar to that of domestic peers Danske Bank and Nordea Bank Danmark, which consolidate bank and mortgage financing in the group's metrics. The group's stable funding ratio was 99.3% at September 2016, compared to 86% at mid-year 2014, following the merger with BRF, which we see as sustainable. We note continued marketwide efforts to reduce one- and two-year interest rate fixings (F1 and F2 loans, respectively) in the Danish mortgage market (see "Credit FAQ: The Danish Covered Bond Market Explained," July 15, 2014). However, the SFR is expected fall somewhat

through mid-2017 due to large maturities in the BRFkredit portfolio.

The bank's efforts to extend funding maturities in the medium to long term are also expected to improve liquidity buffers over time. As BRF reduces its structural mismatch of asset and liability maturities, we expect a direct positive impact on our core measures of funding and liquidity for the group. In our view, the 2018 implementation of the supervisory diamond for mortgage institutions and the future regulatory funding and liquidity requirements will encourage BRF and other mortgage institutions to incentivize longer-term funding structures. We expect an even distribution of funding maturities over time due to the annual and quarterly refinancing limits of 25% and 12.5%, respectively, of outstanding covered bonds in the upcoming "supervisory diamond".

Customer deposits, particularly large term deposits from corporates, have also been declining since 2015. This has been partly because of the negative interest rate environment, which, along with increased repo lending and growth in mortgage lending, is putting pressure on SFR. Despite the substantial contribution of corporate deposits in Jyske's deposit book, we believe the majority to be granular and stable--befitting Jyske's SME lending profile and providing the bank with a steady source of funding for its nonmortgage lending. Core customer deposits formed 29% of the funding base at March 2016.

We view Jyske's liquidity as adequate, and note the structural support of the Danish covered bond market, as well as the soft bullet nature of Danish covered bonds since the passage of the Danish law enacted on all new covered bonds since April 2014 (see "Credit FAQ: Why Denmark's Proposed Covered Bond Law Doesn't Fully Eradicate Refinancing Risks," Feb. 4, 2014). Our one-year liquidity ratio (broad liquid assets to short-term wholesale funding) was 1.1x at September 2016, from the mid-year 2014 level of 0.8x, following the merger.

Table 6

Jyske Bank A/S Funding And Liquidity					
	--Year-ended Dec. 31--				
(%)	2016*	2015	2014	2013	2012
Core deposits/funding base	28.8	27.5	29.0	58.0	51.5
Customer loans (net)/customer deposits	274.9	274.9	254.7	91.6	102.8
Long term funding ratio	80.6	78.0	81.9	66.9	64.3
Stable funding ratio	99.3	97.8	107.5	110.5	107.1
Short-term wholesale funding/funding base	20.7	23.4	19.2	35.8	38.5
Broad liquid assets/short-term wholesale funding (x)	1.1	1.0	1.5	1.3	1.3
Net broad liquid assets/short-term customer deposits	6.8	3.3	44.8	24.4	22.1
Short-term wholesale funding/total wholesale funding	28.9	32.3	27.0	85.4	79.4
Narrow liquid assets/3-month wholesale funding (x)	2.2	1.5	1.7	1.7	1.5

*Data as of Sept. 30.

Support: The implementation of bail-in provision of BRRD decreases the likelihood of extraordinary government support; ALAC buffers remain small

We consider that Jyske has moderate systemic importance in Denmark. However, following the implementation of the bail-in provisions in BRRD in June 2015, we view government support as uncertain for senior unsecured creditors. As such, we no longer add any notches to the issuer credit rating for government support.

We view Denmark's resolution regime as effective under our ALAC criteria because, among other factors, we believe it contains a well-defined bail-in process under which authorities would permit non-viable systemically important banks to continue critical functions as going concerns following a bail-in of eligible liabilities. We provide no notches of ALAC uplift to the rating and project that ALAC buffers will remain below 3% of S&P Global Ratings' risk-weighted assets, well below the 5% threshold for notching, through the end of 2017.

Key Subsidiary: BRFkredit

Although the merger was only completed in April 2014, we view BRFkredit as a core subsidiary and align the rating and outlook with those on the Jyske Group. We believe that BRFkredit is highly unlikely to be sold, given its status as a vital part of the combined entity's future funding strategy for Danish residential and commercial mortgages. This is in line with how we see other banking group structures and covered bond-issuing subsidiaries in Denmark and the Nordics.

Related Criteria And Research

Related Criteria

- Methodology For Mapping Short- And Long-Term Issuer Credit Ratings For Banks - May 04, 2010
- Commercial Paper I: Banks - March 23, 2004
- Group Rating Methodology - November 19, 2013
- Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17, 2013
- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity - April 27, 2015
- Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions - January 29, 2015
- Banks: Rating Methodology And Assumptions - November 09, 2011
- Bank Capital Methodology And Assumptions - December 06, 2010
- Banking Industry Country Risk Assessment Methodology And Assumptions - November 09, 2011
- Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework - June 22, 2012
- Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Nordic Banks' Capital Growth Tapers Off, Aug 2, 2016
- The Future Of Banking: Nordic Banks Looking Svelte In The Fintech Race, June 14, 2016
- Nykredit Realkredit's Proposed Senior Subordinated Tier 3 Notes Rated 'BBB+', May 26, 2016
- Banking Industry Country Risk Assessment: Denmark, Jan. 28, 2016
- Various Rating Actions On Four Danish Banks After Review Of Government Support And Additional Loss-Absorbing Capacity, July 13, 2015
- Various Rating Actions On Danish Banks On EU Bank Recovery And Resolution Directive To Be Implemented In Denmark, May 12, 2015
- Credit FAQ: The Danish Covered Bond Market Explained, July 15, 2014
- Credit FAQ: Why Denmark's Proposed Covered Bond Law Doesn't Fully Eradicate Refinancing Risks, Feb. 4, 2014

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 November 15, 2016)

Jyske Bank A/S

Counterparty Credit Rating A-/Stable/A-2

Nordic Regional Scale --/--/K-1

Certificate Of Deposit

Foreign Currency A-2

Junior Subordinated BB+

Senior Unsecured A-

Short-Term Debt A-2

Subordinated BBB

Counterparty Credit Ratings History

01-Dec-2011 A-/Stable/A-2

20-Feb-2009 A/Negative/A-1

30-Sep-2008 A+/Negative/A-1

10-Feb-2012 *Nordic Regional Scale* --/--/K-1**Sovereign Rating**

Denmark (Kingdom of) AAA/Stable/A-1+

Related Entities**BRFkredit A/S**

Issuer Credit Rating A-/Stable/A-2

Senior Secured AAA

Senior Secured AAA/Stable

Short-Term Secured Debt A-1+

*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.

Additional Contact:

Financial Institutions Ratings Europe; FIG_Europe@spglobal.com

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