

Transaction Update: Bank of Aland PLC (Category SWE Mortgage Covered Bonds)

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Ratings Detail

Reference Rating Level	a-	+	Jurisdiction-Supported Rating Level	aa-	+	Maximum Achievable Covered Bond Rating	aaa	Covered Bond Rating	
Resolution Regime Uplift	+2		Assigned Jurisdictional Support Uplift	+3		Collateral Support Uplift	+4	AAA/Stable	
Systemic Importance	Very Strong		Jurisdictional Support Assessment	Very Strong		Overcollateralization Adjustment	0	Rating Constraints	aaa
Resolution Counterparty Rating	N/A		Legal Framework	Very Strong		Liquidity Adjustment	0	Counterparty Risk	aaa
Issuer Credit Rating	BBB		Systemic Importance	Strong		Potential Collateral Based Uplift	+4	Country Risk	aaa
			Sovereign Credit Capacity	Very Strong					

Major Rating Factors

Strengths

- The issuer is committed to manage available credit enhancement, so it exceeds the required credit enhancement for the current rating.
- There is a public commitment from the issuer to cover 180 days of liquidity risk.

Weaknesses

- Bank account risk and commingling risk are not legally or structurally addressed.
- The program features a timing mismatch between the weighted-average maturity on the assets and the liabilities that is higher than for other programs that we rate.

Outlook: Stable

Under our covered bonds criteria, Bank of Aland PLC's SWE mortgage covered bond program is eligible for four notches of uplift above the jurisdictional rating level (JRL), but it only requires three to achieve an 'AAA' rating, which results in one unused notch of collateral uplift (see "Covered Bonds Criteria," published on Dec. 9, 2014). The stable outlook reflects the one unused notch of uplift, which means that we would not automatically lower the ratings on the

covered bonds if we were to lower our long-term rating on Bank of Aland by one notch.

Rationale

We are publishing this transaction update as part of our periodic review of Bank of Aland's SWE mortgage covered bond program.

Our rating process follows the methodology and assumptions outlined in our covered bonds criteria.

In our analysis, we assume the issuer's insolvency and look to the resolution regime, the jurisdictional support, and the pool to repay the covered bonds. The ratings reflect the likelihood of the covered bonds being repaid in a timely manner at their legal final maturity.

Bank of Aland is domiciled in Finland, which is subject to the EU's Bank Recovery and Resolution Directive (BRRD). We consider that mortgage covered bonds have a very strong systemic importance to Finland. These factors increase the likelihood that Bank of Aland (BBB/Positive/A-2) would continue servicing its covered bonds without accessing the cover pool or receiving jurisdictional support, even following a bail-in of its senior unsecured obligations. Under our covered bonds criteria, a very strong systemic importance means the reference rating level (RRL) is the maximum between two notches above the long-term issuer credit rating (ICR) and the Resolution Counterparty Rating (RCR). Given that we have not assigned an RCR to Bank of Aland, the RRL is 'a-', which reflects the two-notch uplift from the ICR.

We consider the likelihood for the provision of jurisdictional support, which we assess as very strong for covered bonds in Finland. This could result in a potential uplift from the 'a-' RRL of up to three notches under our covered bonds criteria. As a result, we assess the JRL as 'aa-'.

We have assessed the cover pool's credit risk by reviewing the loan-level data as of Dec. 31, 2020, and we have run cash flows based on aggregated information as of December 2020. The cover pool comprises Swedish residential mortgages. Based on our cash flow analysis, we believe that the available credit enhancement exceeds the required credit enhancement for a 'AAA' rating.

Lastly, the ratings on the program and related issuances are not constrained by legal, operational, country, or counterparty risks.

We have based our analysis on criteria articles referenced in the "Related Criteria" section.

Program Description

Table 1

Program Overview*	
Jurisdiction	Finland
Year of first issuance	2014
Covered bond type	Legislation-enabled
Outstanding covered bonds (bil. SEK)	4.5

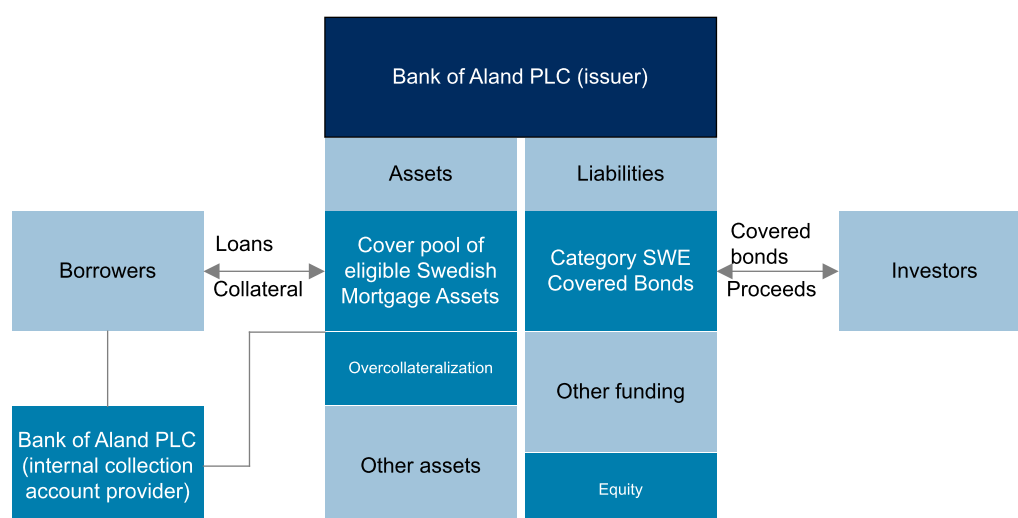
Table 1

Program Overview* (cont.)	
Redemption profile	Soft bullet
Underlying assets	Swedish residential mortgage loans
Jurisdictional support uplift	3
Unused notches for jurisdictional support	0
Target credit enhancement (%)	33.28
Available credit enhancement (%)	51.71
Credit enhancement required for current rating (%)§	25.93
Collateral support uplift	4
Unused notches for collateral support	1
Total unused notches	1

*Based on data as of Dec. 31, 2020. §Given the JRL of 'aa-', overcollateralization that covers 'AAA' credit risk and 75% of refinancing costs or 25.93% of credit enhancement is required to achieve the 'AAA' rating.

Bank of Aland PLC

Transaction structure



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Bank of Aland is a relatively small regional Scandinavian bank with a strong presence in the Finnish region of the Aland Islands. The bank's operations in Finland are concentrated in the Aland Islands and South-West of the country. The bank focuses on offering private banking to high-net-worth clients, complemented by operations in Sweden's largest cities with branches in Stockholm, Gothenburg, and Malmö with focus on the same type of clients. We believe Bank of Aland follows a prudent approach in its loan underwriting, demonstrated in its good asset quality and very low arrears levels.

On Sept. 20, 2019, Bank of Åland announced that it had signed an agreement to establish a new Swedish mortgage company together with four partners: ICA Bank (belonging to retailer ICA Group), IKANO Bank (IKANO Group,

belonging to the Kamprad family), Söderberg & Partners (advisor in wealth management, insurance, and pensions), and Borgo (digital mortgage company). The purpose is to create a platform to allow the distribution of mortgage loans granted to Swedish customers from each of the partners and to refinance them in an efficient way through the issuance of covered bonds. The collaboration with Swedish based ICA Bank already began in the last quarter of 2019, and ICA Bank started to distribute mortgage loans to the Bank of Åland.

We expect the joint venture will further diversify Bank of Åland's revenue base and give growth opportunities in Sweden. Bank of Åland will provide its knowhow in covered bond issuance, and together with its 100% information technology (IT) subsidiary CrossKey will provide IT, treasury, and risk management systems and services to Borgo.

Under its €3 billion covered bond program, Bank of Åland maintains two separate cover pools, each backing a separate set of covered bonds. The "Category FIN" covered bonds have a preferential claim on a pool of Finnish mortgage assets, while the "Category SWE" covered bonds are collateralized by a pool of Swedish mortgages. Both sets of covered bonds are issued under the terms of Finnish Covered Bond Act. This transaction update covers the Category SWE covered bonds only.

The covered bonds constitute a senior secured unsubordinated obligation and rank pari passu with other obligations secured by the same cover register. In the event of bankruptcy, the pools would be separate and independent of each other.

Table 2

Program Participants			
Role	Name	Rating	Rating dependency
Issuer	Bank of Åland PLC	BBB/Positive/A-2	Yes
Originator	Bank of Åland PLC	BBB/Positive/A-2	No
Servicer	Bank of Åland PLC	BBB/Positive/A-2	No
Bank account provider	Bank of Åland PLC	BBB/Positive/A-2	No

Rating Analysis

Legal and regulatory risks

In our legal risk analysis, we applied our legal criteria (see "Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017). The Finnish Covered Bond Act of 2010 sets out the legal framework for issuing Finnish covered bonds. In our opinion, the Finnish covered bond legal framework is in line with the relevant legal requirements of our covered bonds criteria. This enables us to rate the covered bonds above the long-term ICR on the issuer.

If the issuer defaults, bondholders can initiate regular insolvency proceedings. In addition, under the Covered Bond Act, they have a preferential claim to a cover pool. The cover pool can comprise residential mortgage loans, commercial mortgage loans, public-sector loans, and substitute assets from European Economic Area countries.

Under the legal framework, the cover pool's assets must be registered in the issuer's cover pool, in order to be isolated from the issuer's other assets if it becomes insolvent. The issuer must report the information in the register to the

Finnish regulator monthly.

If the issuer were to become insolvent, the Finnish regulator would appoint a special cover pool administrator to supervise the covered bondholders' interests. If necessary, the administrator can sell assets or accelerate the payment of the covered bonds if it considers this to be in the bondholders' best interests, subject to Finnish regulatory approval.

To facilitate liquidity management, up to 20% of a mortgage cover pool can include substitute assets, such as state, municipal, or other public-sector/financial entities.

Under the Covered Bond Act, the issuer's bankruptcy would not result in the covered bonds' early redemption, or the suspension of payments to bondholders. Accordingly, we rate the covered bonds on the basis of their legal final maturity.

Operational and administrative risks

In our last meeting with the issuer we reviewed its origination, underwriting, collection, and default management procedures for the cover pool assets. We also reviewed the cover pool management and administration and have not observed any major changes or new risks arising.

In our view, operational risk is mitigated by internal policies and procedures and does not represent a rating constraint; we view the origination and servicing procedures as prudent and in line with market peers. On top of that, in our cash flow analysis, we model a stressed servicing fee that we feel is sufficient to incentivize a replacement servicer in an active market with several players should the need arise.

The criteria apply a pool-level adjustment of 0.7x-1.3x to reflect the observed historical performance of various pools from different originators or lenders within each jurisdiction.

We have reflected the prudent origination standards and pool performance by applying a positive pool-level adjustment factor in our analysis.

Our analysis of operational and administrative risk follows the principles laid out in our covered bond ratings framework.

Resolution regime analysis

As part of our covered bonds criteria, our analysis considers any resolution regime in place in Finland in order to determine the RRL. As Finland is part of the EU and is required to implement the EU's Bank Recovery And Resolution Directive (BRRD), this analysis considers the support provided by its eventual adoption. The RRL is equal to the greater of: (i) the issuing bank's ICR, plus up to two notches for programs in jurisdictions with effective resolution regimes that exempt covered bonds from bail-in, and (ii) the RCR on the issuing bank, where applicable. As for Bank of Aland there is no RCR assigned, the resulting RRL is 'a-', two notches of uplift from the ICR.

Jurisdictional support analysis

Under our analysis of jurisdictional support in our covered bonds criteria, we determine a JRL, which is our assessment of the creditworthiness of a covered bond program once we have considered the level of jurisdictional support, but before giving credit to the amount of collateral.

In our jurisdictional support analysis, we assess the likelihood that a covered bond program facing stress would receive support from a government-sponsored initiative instead of from the liquidation of collateral assets in the open market. Our assessment of the expected jurisdictional support for Finnish mortgage covered bond programs is very strong (see "Assessments For Jurisdictional Support According To Our Covered Bonds Criteria", published on Nov. 27, 2020). Under our covered bonds criteria, this means that the program can receive up to three notches of jurisdictional uplift from the RRL. This results in a JRL for these mortgage covered bonds of 'aa'.

Collateral support analysis

We base our analysis on the loan-level data provided by the issuer as of Dec. 31, 2020. The cover pool comprises Swedish residential loans backed by single-family houses and tenant-owner rights.

Since our previous review, we have updated our criteria for the assessment of pools of Swedish residential mortgage loans. We base our credit analysis on the specific adjustments defined for Sweden under our global residential loans criteria (see "Global Methodology And Assumptions: Assessing Pools Of Residential Loans," published on Jan. 25, 2019), effective for Sweden since July 10, 2020.

Compared with our last review, both the weighted-average foreclosure frequency (WAFF) and the weighted-average loss severity (WALS) decreased significantly to 8.86% and 35.64%, respectively, from 18.93% and 59.59%.

The reduction in the WAFF to 8.86% from 18.93% is mainly due to the application of our global residential loans criteria and its new LTV curve, which considers effective loan to value (ELTV) ratios when calculating the WAFF. The ELTV ratio gives the original LTV ratio and current indexed LTV ratio an 80% and 20% weighting, respectively, for the WAFF calculation. In our previous criteria, only the original LTV ratio was considered for the WAFF. In addition, the geographic concentration adjustment is now applied only to the excess over the threshold limit. The pool is highly concentrated in Stockholm at 68.33% currently and 73.90% in our previous review, but the adjustment is now applied only to a 23.33% of the pool compared with 73.90% in our last review.

The WALS decreased to 35.64% from 59.59% driven mainly the application of our global residential loans criteria, under which jumbo valuation thresholds are higher and the fact that the adjustment is applied now only to the excess over the threshold. As well under the new criteria there is no adjustment to the market value decline to properties of tenant-owner-right loans (which represent 48.8% of the cover pool). Finally, the slightly lower CLTV of 51.45% compared to the previous 51.71% is also positive for the WALS.

One of the reasons for the high WALS in this program, compared with the Finnish program, for example, is the effect of overvaluation. Our global residential loans criteria consider the effect of overvaluation when analyzing the loss severity. Swedish property prices have recently stabilized following a considerable increase over the past years when house prices outpaced income levels, leading to a material overvaluation in the housing market. In contrast the Finnish mortgage market is undervalued, in our view(see table 4).

Additionally, the portfolio's historical performance has been good, which we believe reflects the quality of the loan origination and underwriting processes. The positive pool-level adjustment in our analysis reflects this factor.

There are no substitute assets in this cover pool.

The tables below summarize the results of our collateral support analysis.

Table 3

Pool Composition				
Asset type (mortgage loans)	As of December 2020		As of December 2019	
	Value (SEK)	Percentage of cover pool	Value (SEK)	Percentage of cover pool
Residential assets (single family homes and condo apartments)	7,131,225,376	100.00	4,001,890,571	100.00
Commercial assets (multifamily housing and condo associations)	0	0.00	0	0.00
Total	7,131,225,376	100.00	4,001,890,571	100.00

Table 4

Key Credit Metrics		
	As of December 2020	As of December 2019
Weighted-average Effective Loan-to-Value (ELTV)(%)	57.94	N/A
Weighted-average whole loan-to-value ratio (%)	51.45	51.71
Weighted-average loan seasoning (months)*	42.14	47.19
Balance of loans in arrears (%)	0.04	0.40
Jumbo valuations (%)	73.49	78.40
Interest-only loans (%)	51.30	51.30
Loans secured by tenant-owner rights (%)	48.78	50.00
Credit analysis results		
WAFF (%)	8.86	18.93
WALS (%)	35.64	59.59
WAFF x WALS (%)	3.16	11.28
Asset default risk (%)	3.88	15.69

*Seasoning refers to the elapsed loan term. SEK--Swedish krona. WAFF--Weighted-average foreclosure frequency. WALS--Weighted-average loss severity.

Table 5

Current Loan-To-Value Ratios		
Residential		
	As of December 2020	As of December 2019
Weighted-average whole-loan LTV ratios (%)	Percentage of the residential mortgage loan cover pool (%)	
0 to 50	42.56	43.60
50 to 60	25.23	23.79
60 to 70	31.57	22.54
70 to 80	0.64	9.06
80 to 90	0.00	1.01
90 to 100	0.00	0.00
More than 100	0.00	0.00

LTV--Loan to value, after S&P adjustments.

Table 6

Loan Seasoning Distribution		
Residential		
	As of December 2020	As of December 2019
Seasoning (years)*	Percentage of the residential mortgage loan cover pool (%)	
Less than 2	30.79	5.70
2 years to 5	43.72	69.90
Above 5	25.49	24.40

*Seasoning refers to the elapsed loan term.

Table 7

Geographic Distribution Of Loan Assets		
Residential		
	As of December 2020	As of December 2019
Region	Percentage of the residential mortgage loan cover pool (%)	
East Middle Sweden	3.46	1.15
North Middle Sweden	0.88	0.06
Smaland and the islands	0.94	0.07
South Sweden	13.28	10.94
Stockholm	68.33	73.87
Upper Norrland	0.20	0.00
West Sweden	12.91	13.91

Table 8

Collateral Uplift Metrics		
	December 2020 Analysis	March 2020 Analysis
Asset WAM (years)	27.54	31.77
Liability WAM (years)	4.11	4
Asset-liability maturity mismatch	23.43	27.77
Available credit enhancement*	51.71	54.41
'AAA' credit risk (%)	3.88	15.69
Required credit enhancement for first notch of collateral uplift (%)	11.23	26.33
Required credit enhancement for second notch of collateral uplift (%)	18.58	36.97
Required credit enhancement for third notch of collateral uplift (%)	25.93	47.61
Target credit enhancement for maximum uplift (%)	33.28	58.25
Potential collateral-based uplift (notches)	4	3
Adjustment for liquidity (Y/N)	N	N
Adjustment for committed overcollateralization (Y/N)	N	N
Collateral support uplift (notches)	4	3

*After our adjustments. WAM--Weighted-average maturity.

According to our covered bonds criteria, the maximum potential collateral-based uplift on a covered bond program above the JRL is four notches. We then look to make adjustments to the maximum collateral-based uplift by reviewing

the coverage of six months of liquidity and the level of commitment for the overcollateralization. The issuer has a liquidity commitment and an overcollateralization commitment published on its website that are both in line with our criteria. Therefore, we do not adjust the collateral support uplift for liquidity or committed overcollateralization.

By applying our credit and cash flow stresses, we calculate a target credit enhancement (TCE) of 33.28%. This is lower than the 58.25% target credit enhancement at our previous review. The decrease is mainly driven by a decreased asset-liability maturity mismatch, resulting from the decrease in the assets' weighted-average maturity and an increase in the weighted average maturity of the liabilities resulting from the issuance of a new covered bond in May 2020. In addition, the application of the new criteria has had a positive effect on the TCE driven by the lower credit risk results, lower servicing fees applied and lower commingling risk.

Given that we do not deduct any notches of collateral uplift for uncommitted overcollateralization or liquidity risk not covered, because both are covered with the issuers' public statement and given that the program's JRL is 'aa-', the overcollateralization required to achieve an 'AAA' rating needs to cover 'AAA' credit risk and 75% of refinancing costs. We calculate the credit enhancement needed to cover 'AAA' credit risk and 75% of refinancing costs at 25.93%. The program's available credit enhancement after adjusting for bank employee loans and set-off risk of 51.71% is above the required credit enhancement for a 'AAA' rating and the TCE. This means that the program could achieve the full four notches of uplift, but because it only needs three to reach a 'AAA' rating, the result is that there is one unused notch of collateral uplift.

Counterparty risk

We have identified account bank and commingling risk as a relevant counterparty risk that is not addressed structurally or by law. We have considered the frequency of our access to information on the program's available credit enhancement to estimate the size of the account bank and commingling risk--currently 1.31% of the additional credit enhancement--and take the view that overcollateralization sufficiently mitigates this risk.

We have also identified set-off risk to be relevant for this transaction. As we believe that loans to borrowers with deposits with the issuer are exposed to set-off risk and that loan repayment could potentially be unavailable to service the covered bondholders' claims, we have reduced the available credit enhancement by the amount at risk. We have also adjusted the available credit enhancement by removing loans granted to the bank's employees from the cover pool, due to the risk of such loans being set off if the issuer were to become insolvent. As a result, the available collateral has been reduced for our analysis.

There are no derivatives registered in the cover pool.

We believe that counterparty risk is addressed and that therefore does not constrain the maximum achievable ratings on the covered bonds.

Sovereign risk

We assess country risk by applying our structured finance ratings above the sovereign criteria (see "Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions," published on Jan. 30, 2019). Given that assets in this cover pool are domiciled in Sweden and the issuer is domiciled in Finland, and the current unsolicited ratings on Sweden and Finland are AAA/Stable/A-1+ and AA+/Stable/A-1+ respectively, our rating on

the program is not limited by the application of these criteria.

Environmental, social, and governance factors

Environmental and social credit factors influence Bank of Åland's SWE cover pool's credit quality in a broadly similar way to other Swedish issuers. The issuer currently does not offer specific mortgage products focused on environment or social factors, which could affect the credit profile. Swedish cover bond law does not require the coverage of six months liquidity and overcollateralization (OC) is normally not committed by the issuer. However, Bank of Åland is committed to maintain a minimum level of OC commensurate with the rating, and the bonds' soft-bullet repayment structure covers 180 days liquidity. The program's governance initiatives support the current rating and the credit enhancement required for the rating.

Potential effects of COVID-19

S&P Global Ratings believes there remains high, albeit moderating, uncertainty about the evolution of the coronavirus pandemic and its economic effects. Vaccine production is ramping up and rollouts are gathering pace around the world. Widespread immunization, which will help pave the way for a return to more normal levels of social and economic activity, looks to be achievable by most developed economies by the end of the third quarter. However, some emerging markets may only be able to achieve widespread immunization by year-end or later. We use these assumptions about vaccine timing in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Related Criteria

- Criteria | Structured Finance | General: Global Framework For Payment Structure And Cash Flow Analysis Of Structured Finance Securities, Dec. 22, 2020
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Criteria | Structured Finance | General: Incorporating Sovereign Risk In Rating Structured Finance Securities: Methodology And Assumptions, Jan. 30, 2019
- Legal Criteria: Structured Finance: Asset Isolation And Special-Purpose Entity Methodology, March 29, 2017
- Criteria - Structured Finance - Covered Bonds: Covered Bond Ratings Framework: Methodology And Assumptions, June 30, 2015
- Criteria - Structured Finance - Covered Bonds: Covered Bonds Criteria, Dec. 9, 2014
- Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Global Covered Bond Characteristics And Rating Summary Q1 2020, March 31, 2020
- Global Covered Bond insights Q1 2020, March 31, 2020

- Sweden 'AAA/A-1+' Ratings Affirmed; Outlook Stable, Feb 12, 2021
- Outlooks On Seven Finnish Banks Revised Due To Their Resilience In The COVID-19-Induced Downturn, Jan 22, 2021
- Norwegian And Finnish Covered Bond Market Insights 2021, Jan 19, 2021
- Banking Industry Country Risk Assessment: Finland, Feb 09, 2021
- S&P Global Ratings Definitions, Jan. 5, 2021
- Assessments For Jurisdictional Support According To Our Covered Bonds Criteria, Nov. 27, 2020
- Assessments For Target Asset Spreads According To Our Covered Bonds Criteria, Nov. 27, 2020
- ESG Industry Report Card: Covered Bonds, Nov. 9, 2020
- Swedish Covered Bond Market Insights 2020, Sept. 11, 2020
- Finland 'AA+/A-1+' Ratings Affirmed; Outlook Stable, Sept. 4, 2020
- Bank of Aland PLC, Dec. 15, 2020
- Banking Industry Country Risk Assessment: Sweden, Sep 14, 2020
- Glossary Of Covered Bond Terms, April 27, 2018

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