

EMEA Utilities

Energy transition investments reduce rating headroom

January 14, 2025

This report does not constitute a rating action.



What's changed?

Conditions for U.K. water companies have taken a turn for the worse following Thames Water's demise. We expect the regulator's final determination to enable continued sector investment.

Weaker economics decelerate the deployment of hydrogen and batteries and costlier nuclear and offshore wind make the transition less affordable than expected.

High interest rates and grid capital expenditure (capex) test energy transition economics. For grids, strong and adapting regulations broadly offset risks associated with considerable leverage.

What are the key assumptions for 2025?

High and volatile gas and power prices benefiting power generators, especially those with flexible production assets. Tight gas supply test affordability amid tepid GDP growth.

Caution on generation and power grid investments. Massive capex necessitate cautious financing, to be prioritized over dividend growth.

Reduced ratings headroom for power producers and integrated players. Balance sheets, while typically solid, are eroded by high and growing capex, interest rates, and dividends.

What are the key risks around the baseline?

Supply chain issues, interest rates, inflation, and regulatory and fiscal setbacks. Changes in assumptions or weak contracting could impair a utility's business risk or financial risk profile.

Political and regulatory. Making the energy transition faster and cheaper could weigh on ratings.

Cyber risk, physical sabotage, or weather, particularly for issuers with thin liquidity.

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Ratings Trends: EMEA Utilities

Chart 1
Ratings distribution

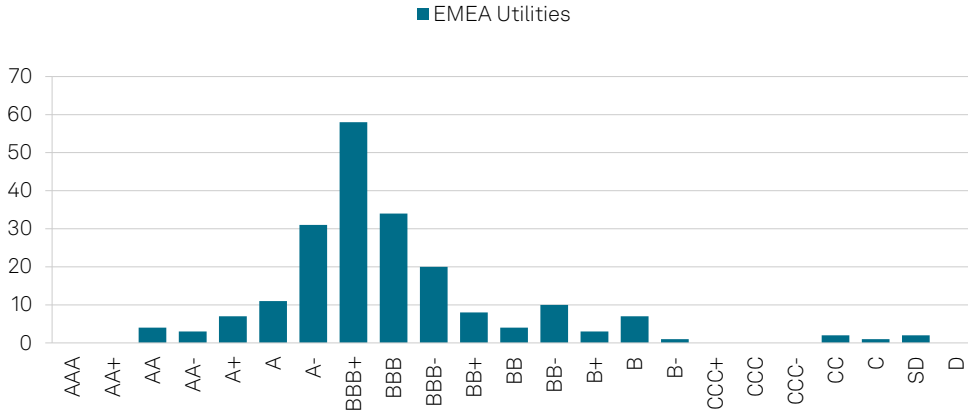


Chart 2
Ratings outlooks

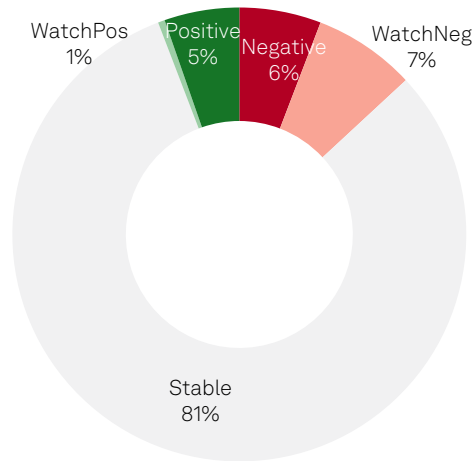
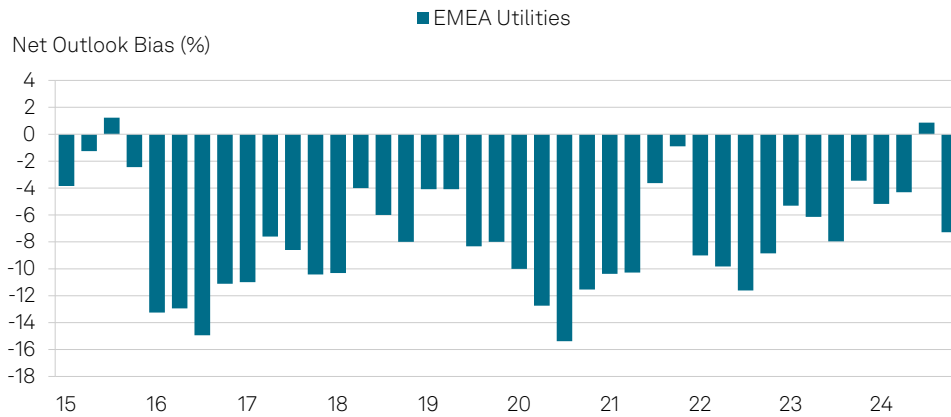


Chart 3
Ratings outlook net bias



Source: S&P Global Ratings. Ratings data measured at quarter-end.

Industry Outlook

Ratings trends and outlook

The sector enters 2025 with a slight negative outlook bias (following a temporary net positive one in 2024), mainly from adverse credit dynamics in the U.K. water utilities sector. On the power side, business fundamentals remain solid as Europe executes its energy transition, with investment prudence needed in nuclear, offshore wind, and new technologies. For gas grids, financial discipline is crucial to preserve ratings as issuers face stranding risk. For power grids, we will look at how much regulations and disciplined financial policies preserve cash-flow-based credit metrics in the face of a capex super-cycle; for some, particularly in the Netherlands, Belgium, and Germany, we continue to expect state support to protect credit quality.

Our remaining negative bias primarily reflects the following:

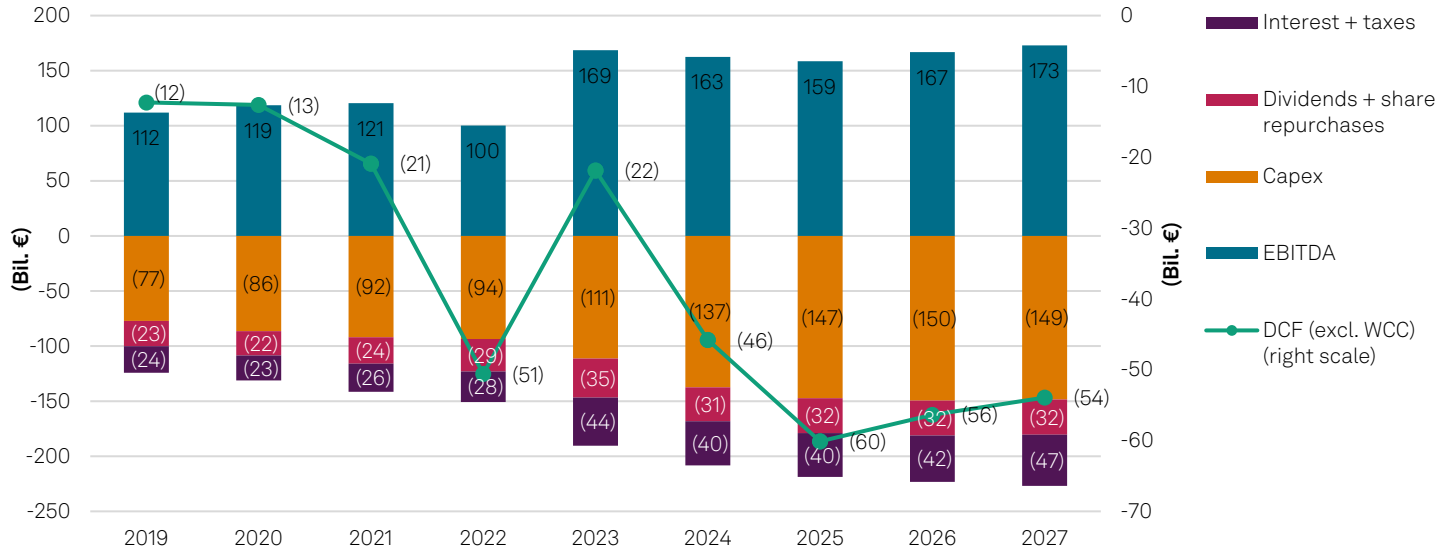
- The regulatory reset risk for U.K. water companies is high, with potentially more challenging operating and financing conditions for almost all rated U.K. water utilities over the April 2025-March 2030 regulatory asset management period 8 (AMP8). The regulator's determination published Dec. 19, 2024, indicates the nature of regulatory allowances and requirements for each company for AMP8, which has significant implications for the sector's ability to invest given the significant increase in required investments over the next five years. We expect to assess the impact on our ratings on U.K. water companies in the coming weeks.
- There are risks and opportunities from gas and power prices, with prices elevated through 2026, even if much less so than in 2022; higher-for-longer refinancing rates; and continuing issues about supply-chain and sector-specific inflation, notably for offshore wind and power networks.
- For networks, in particular power, tensions are emerging on financial risk profiles from heavy capex, regulatory reset risks on the weighted-average cost of capital (WACC), and dependence on new equity.
- We expect the EU to approach, but not reach, its 2030 target of a 42.5% share of renewables in the primary energy mix, as solar capacity additions continue to offset weak wind additions amid tepid demand growth, which we expect at 1-2% from 2025 (see "[Europe's Power Producers Continue Their Balancing Act As Electricity Prices Stay Low](#)," published July 10, 2024). On the grid side, we expect Europe's power transmission and distribution network expansion over 2023-2030 to absorb €800 billion in capex. Including all generation technologies and storage, costs will likely exceed €2 trillion across Europe, about 20x the total annual capex of our top 25 rated European energy utilities by cash flow.

Against this background, we anticipate sector capex and debt to rise steadily with most rated utilities' cash flow growing in stride. This should protect credit metrics, except for companies, notably power grids, that ramp up capex so aggressively as to weaken metrics, at least for a few years. For our top 25, over 2025-2027, we project capex to represent 1.22x funds from operations (FFO) compared with about 0.9x each year over 2017-2023 (except 2022, the year of the energy crisis, see chart 4). Leverage in particular could increase for some power grids and U.K. water utilities, which face growing pressure to raise service quality. We will monitor the extent to which works in progress get sufficient remuneration and higher interest rates are effectively and timely passed on to WACCs, as some regulations are now doing. For instance, Italy's regulator has lowered its WACC remuneration for 2025-2027 by 30-60 basis points for power and gas networks to reflect lower interest rates. We had already accounted for this in rated utilities' strategic plans (see "[Italian Electricity And Gas Transmission And Distribution Frameworks: Supportive](#),"

published May 14, 2024; and “[WACC Revision For Italian Regulated Utilities Is In Line With Our Base Case And Shows Regulation's Consistency](#),” published Dec. 3, 2024).

Chart 4

Top 25 European utilities: Capex will continue increasing, dragging down DCF



DCF—Discretionary cash flow. WCC—Working capital change. Source: S&P Global Ratings.

For integrated companies, we expect less rating pressure than a year ago from the dilution of regulated activities in the overall business mix as a number are rebalancing capex toward grids, translating in faster EBITDA accretion; many are also moderating renewable investments.

Financial policy and credit rating commitments support many ratings and stable outlooks in the 'BBB' band. We perceive that many managements see a 'BBB' rating category—in particular, ratings of 'BBB' or 'BBB+'—as a floor, including to preserve operating momentum and continued, competitive access to debt markets. We factor in potential new equity to the extent we think key shareholders are publicly committing to it for the near term.

Outside the U.K. water sector, we expect downgrades to be limited to one notch in 2025, similar to 2021-2024, and senior debt to remain clustered in the 'BBB+' and 'BBB' range.

Main assumptions about 2025 and beyond

1. Elevated gas and power prices until 2026 in an evolving market design.

Through next winter, Europe's gas and power markets will remain tight, resulting in still-elevated and volatile power prices. This is a price issue, because we do not foresee volume shortage for winter 2024-2025.

2. Heavier investments in power networks, and moderation in renewable energy.

Depending on the company, we expect capex for power grids to rise 50%-200% over 2023-2028, mostly to accelerate the energy transition. Many rated utilities are moderating capex on renewables.

3. Still-supportive financial policy despite often-slim buffers.

For many companies, high capex and dividends are eliminating credit-metric buffers at current ratings.

Gas prices will remain high and volatile in 2025, then moderate. This is due to Europe's supply-demand tightness following the loss of most Russian volumes (including the full cut since Jan. 1, 2025, of volumes transiting through Ukraine), supporting prices 2.0x-2.5x above pre-pandemic levels. As its energy transition goals make long-term contracting less attractive, Europe needs to continue capturing excess spot liquefied natural gas (LNG) volumes at prevailing prices.

The main European exchange-traded index, the Title Transfer Facility (TTF), remains in backwardation. Specifically, we assume it will moderate to \$10 per million British thermal units (mmBtu) in 2026 from a high \$12/mmBtu in 2025, equivalent to about €40 per megawatt-hour (/MWh; the levels has hovered within €40-€50/MWh since November) (see "[S&P Global Ratings Revises Its Natural Gas Price Assumptions; Oil Price Assumptions Unchanged](#)," published Sept. 10, 2024). This will depend in particular on inventories, which at 71.8% fullness opened 2025 a sixth lower than a year ago.

Power prices will remain high and volatile until 2026. We expect prices of €80-€100 per megawatt-hour outside Scandinavia, Spain and, from 2026, France. Prices for gas—notably landed LNG—will continue to drive (and support) power prices, despite fossil-fuel generation down by about a fifth in 2024. In addition, EU carbon allowance prices, the other key factor behind power prices, could somewhat support power prices if they clearly exceed the €70 per ton mark; our base-case scenario remains that in 2025 they will not, however.

Europe's power demand has weighed on electricity prices by declining in 2022 and 2023, and remaining subdued at under 1% growth in 2024, back to 2004 levels. Demand should offer some price support given data center demand growth and the gradual electrifications of electric vehicles and heat pumps. In our view, each factor is susceptible to add 20-30 basis points to average annual power demand growth and lift it to about 2% each year over 2025-2027—in other terms, while each is positive, unlike in the U.S., none is a game-changer, individually or even combined. Also, from 2028, we expect annual power demand growth to moderate to near 1%.

Looking at the 10 key markets combined, wind and solar should easily meet even 2% (under 50 TWh per year) demand growth, under normal weather conditions. These two should contribute to a record 36% of generation, based on S&P Global Commodity Insights estimates. We assess wind and solar generation to grow about 100 TWh annually. In other words, nuclear and hydro being tendentially flat, each percentage point of demand growth beyond 1% implies some 50 TWh per year less demand on electricity produced from gas and coal. We therefore expect gas- and coal-fired capacities to continue closing, also given negative clean spark spreads expected across markets (except Italy).

Beyond average baseload prices, we expect an increasing bifurcation in prices captured by the various technologies. Increasing risks, particularly on solar and wind, of capturing a low proportion of wholesale prices heighten the importance of contracting to protect generators' cash flow (see "[European Electricity Producers' Credit Quality And Revenue-Support Contracts: It's Complicated](#)," published July 10, 2024). The most flexible ones—in particular, reservoir-based hydro and combined-cycle gas turbines (CCGTs)—should be able to capture peak prices (even as CCGT economics increasingly rely on remuneration via capacity markets for CCGT plants running for ever-fewer hours). By contrast, captured prices for intermittent renewable energy should decrease even more than baseload prices, because storage and interconnections are increasing too slowly to smoothen the absorption of wind and solar generation and lack the flexibility to support renewable revenue (see "[The Energy Transition, Geopolitics, And Cannibalization Are Shaping Europe's Power Prices](#)," published Sept. 12, 2024). As a result, we expect negative prices to remain about as frequent as in the record 2024, when the Netherlands, Germany, and France recorded 350-457 such hours (and Nordic countries even more). We do not see material quantities of hydrogen for electrolysis or seasonal storage as plausible over the next decade.

U.K. water companies and power grids will increase capex. U.K. water utilities and power transmission system operators (TSOs) are increasing capex fast, both to strengthen networks and expand them to connect new renewable capacities. Some power grids are tripling their annual investments, with some rating implications. We revised our outlook to stable from positive on SSE PLC to account for the group's significant increase in its capital intensity until at least fiscal 2027 (year ending March 31, 2028), via its now £20 billion five-year Net Zero Acceleration Programme Plus.

While we see the related regulatory frameworks as strong, we monitor how regulators respond to capex stress on these sectors; tensions that might appear as users see the full impact of the increase in their energy bills (including distribution costs, which could be about double the TSO costs); and the degree and duration of credit metrics being potentially below our guidance for ratings. Financial policies then become paramount, and the ability and willingness to effectively raise sufficient new equity might be an important credit support.

In all cases, we expect funding and liquidity management to bridge discretionary cash flow (DCF) gaps. Given likely rigid capex requirements for urgently needed energy-transition projects, we assess the reliance on new equity issuance in the context of the specific ownership structure and shareholder commitment, full ownership by a single highly rated and committed sovereign being particularly credit supportive (as is the case in the Netherlands).

Gas grid prospects remain weaker than for power, given long-term stranded-asset risk. In the Iberian peninsula and Latvia, we differentiate gas networks' long-term prospects from those of power grids and we could extend this to more countries. We expect gas grid operators that do not invest significantly away from fossil fuels to accumulate balance-sheet headroom as free cash flow remains steady. In that light, financial policies and shareholder support are paramount in our prospective credit analysis.

In contrast, the Netherlands and Germany are actively preparing their transition to hydrogen. Across gas grids, we monitor closely how regulators prepare the ground, notably through sufficient remuneration of new assets and accelerated depreciation of legacy fossil-fuel assets, unless new hydrogen assets are directly subsidized by the government, as in the Netherlands.

Large integrated utilities are cutting plans for greenfield renewables. We observe contrasting capex trends among integrated companies. In 2024 Iberdrola, Enel, EDP, and Orsted all reduced their targets of installed capacity, whereas SSE is pressing ahead with renewable capacity deployment. Positively, most appear to cautiously approach further investments into wind and solar, and particularly offshore wind, as they prioritize projects with the strongest economics over volume growth.

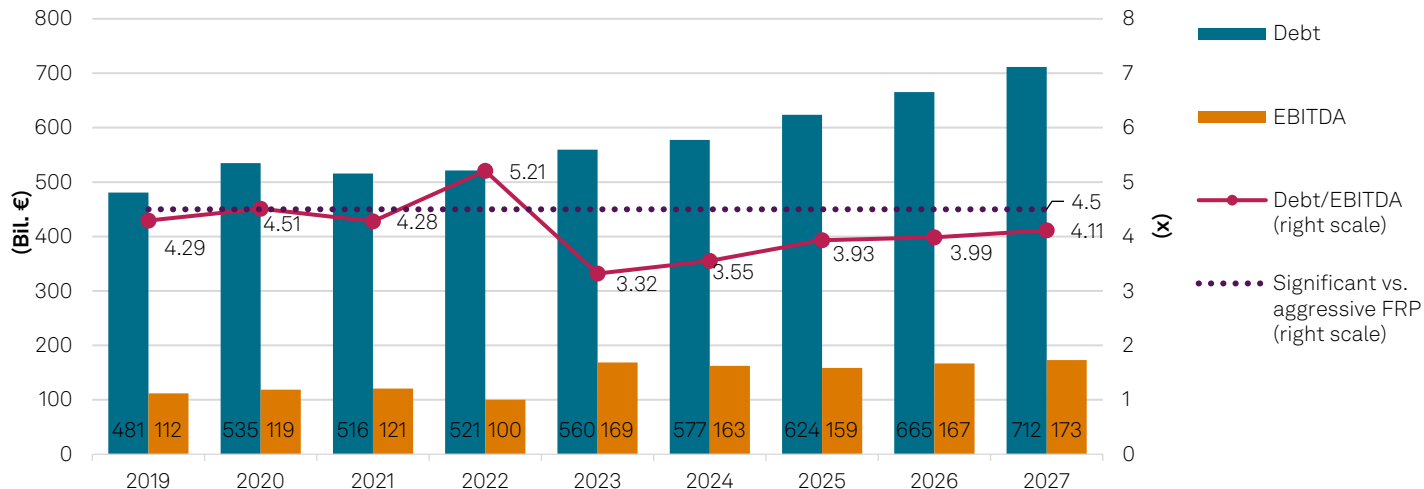
Credit metrics and financial policy

Credit-metric headroom has fallen as capex expands but the sector retains asset sale flexibility and access to capital, especially outside U.K. water. Overall, we expect the sector to keep posting metrics within expectations for the ratings. Over 2025-2027, we anticipate absolute debt to continue rising, including by a hefty €45 billion annually for our top 25 utilities combined (see chart 5); this is based on high and increasing capex and, despite moderate dividend growth expectations, continuingly negative DCF. However, existing buffers and EBITDA growth of about 2% allow adjusted leverage to be contained near 4.0x, in line with 2019-2021 levels, and FFO to erode gradually to just below 18%, from 22% in 2023. We estimate an annual increase in the sector's adjusted debt of about 7%, with a significant dispersion between those increasing debt 10%-200% (notably networks) and those we expect to stabilize metrics. At the same time, a mild economic recovery from 2025, sustained gas and power prices, and new renewables capacity

should support earnings growth. Given reduced rating headroom, we expect dividend moderation and any M&A to be conservatively financed, as with Iberdrola’s acquisitions of Electricity NorthWest in the U.K. and of some minorities in its key U.S. subsidiary Avanguard.

Chart 5

Top 25 European utilities: Mounting debt will likely keep leverage metrics around 4x



FRP—Financial risk profile. Source: S&P Global Ratings.

Key risks or opportunities around the baseline

1. Oversized price volatility or event risks disrupt operations or liquidity.

For companies where increasing capex is depressing DCF (in particular), cyber or physical sabotage could aggravate liquidity tightness. Companies active on energy exchanges could also face liquidity squeezes.

2. Political and regulatory risks and opportunities cloud the overall investment picture.

Measures to accelerate the energy transition run against affordability constraints and limited budgetary firepower in a context of increasing risks concerning security of supply.

3. Deteriorating economics complicate low-carbon power capacity deployment.

Continuing supply-chain constraints, together with persistently high interest rates and slow inflation reduction, complicate the economics of the low-carbon capacity buildup.

Event risks can disrupt operations, liquidity, and credit quality. As for many other corporate sectors, rating risk often relates to liquidity. Some companies’ liquidity buffers are thin relative to our minimal expectation at the adequate assessment, a tightness we reflect both in our liquidity and management and governance analyses. We will continue to monitor liquidity as market behavior is hard to predict, especially as power mixes and market designs evolve.

For 2025, we see event risks affecting liquidity relating to:

- Wholesale price volatility, as happened in 2022;
- Extreme weather;
- Geopolitical events, including wars and sanctions, which could foster volatility and even affect physical supply; and
- Cyberattacks.

Despite Europe's increasing exposure to extreme weather events—most recently, the Valencia floods in October—the impact on utilities' credit quality has been muted. We expect this to continue and governments to typically play a more supportive role than in the U.S., whether for existing government-related entities or companies that could become one. Still, weather conditions are expected to continue deteriorating given continued climate change.

Geopolitical events that might affect EMEA utilities—mostly energy—include wars in the Middle East and Ukraine and sanctions, such as on Russian LNG, to the extent they foster price volatility and affect physical supply.

Generally, the possibility physical sabotage cannot be excluded, particularly for offshore assets like the highly developed gas and power lines in the North Sea and the Baltics, and gas pipelines to Italy, which are difficult to continuously monitor. Of particular relevance are Norway's gas export pipes and Scandinavia's power interconnectors with their continental clients in Germany and the Baltics.

Finally, cyber risk might materialize, particularly for power grids, especially distribution; for these, digitalization is essential in optimizing the use of existing assets in the face of growing and ever-more distributed supply and demand. In turn, it may expose them to even more risk of disruption of operations than for other utilities.

Political and regulatory risks and opportunities abound, particularly where governments run budget deficits, where capex need are massive or where affordability is at risk. Measures to protect end-user affordability could erode related utilities' credit quality, notably via price caps, windfall taxes, and slowness to recognize higher interest rates and inflation in regulated revenues. These measures can prompt higher debt or lower earnings.

Still, we see a steady trend for regulators to grant stronger remuneration on new projects, as decided since 2023 for example in Germany, Italy, Belgium, and France (for gas, and possibly in 2025 for electricity (see [“WACC Revision For Italian Regulated Utilities Is In Line With Our Base Case And Shows Regulation's Consistency,”](#) published Dec. 3, 2024).

Besides accelerating the energy transition, affordability is a cornerstone of Europe's REPowerEU strategy and Fair Transition Plan. Protecting citizens' purchasing power will remain high on political agendas, just as grid fees may double.

Low-carbon project economics are thornier. Supply chains, permitting, grid access, and public policies influence project pace, costs, and risks. This is especially the case for offshore wind, nuclear; batteries; carbon capture, use, and storage; and hydrogen. The latter four necessitate public support to become financially viable—for instance, the financing is still not closed for any of Europe's three major nuclear projects in the U.K., France, and the Czech Republic (see [“Is Europe Ready For A Nuclear Renaissance?”](#), published Dec. 9, 2024). New technologies are struggling even more than we expected a year ago. A number of batteries and low-carbon hydrogen products were abandoned in 2024 given weak economics and high investment and demand risks. This has been compounded by significant political uncertainty in key countries like France and Germany, further delaying the adoption of supportive regulations, for example on hydrogen-fired power generation.

Across regions, we will monitor the following:

In the U.K., progress on power generation and grid investments required to meet 2030 net-zero goals. These goals stand high in the agenda of the recently elected U.K. government, which published its clean power action plan in December 2024. The plan includes significant reforms for the country's energy systems, notably on connection queues, to speed up the planning process and changes and consultation to the government flagship Contract for Difference scheme ahead

of the seventh auction, which is due to be held later this year and is critical for 2030's targets. Swift progress is needed given ambitious commitments to increase clean power sources with offshore wind, solar, and onshore wind installed capacity to 43-50, 45-47 and 27-29 gigawatts (GW), respectively, by 2030 from the current 15, 17 and 14 GW. These in turn require rapid and considerable increases in grid investments, to accommodate the new sources of renewables. The regulator, Ofgem, has enacted its accelerated strategic transmission investment framework, a fast track for major transmission projects that accelerates the funding process by up to two years via the regulator's initial list of 26 onshore transmission projects. As a result, we expect a significant uptick in transmission investment among rated utilities such as National Grid, SSE, and Scottish Power for the rest of the decade. We also monitor nuclear reactors' contribution boosts to energy security, as the recent life extensions of four reactors of up to two years mitigate the delays at EDF's new Hinkley Point C plant.

In France, important milestones for the sector. These include the publication of the TURPE 7 regulation for the period starting in January 2025 shaping the remuneration trajectory of RTE's massive investment plan; and the costing and financing arrangements for EDF's ongoing construction of six new nuclear reactors (and for the sector's back-end segment, as per the president's Feb. 26 decision to launch the Aval du Futur program). We see continued subdued demand growth and net exports remaining solid after 2024's 89 TWh record.

In the Benelux region, the execution of massive investment plans for power TSOs TenneT and Elia. We expect progress on structural solutions to TeneT's equity needs to bridge to the state's shareholder loans exceeding €20 billion, which mature by the end of 2026. We'll also monitor the decommissioning of the majority of Belgium's nuclear fleet by the end of 2025, and the initial price of the contract for difference at which Engie's two remaining reactors will operate until 2035.

In Spain, how depressed power prices weigh on generation earnings as hedges elapse. We expect limited demand growth, coupled with increased renewable generation, to affect Spanish prices through 2025. We expect the regulator to publish a draft of the upcoming regulation for power grids in first-half, potentially accelerating the pace of much needed investments on both transmission and distribution infrastructures from 2026 onward.

In Germany, political developments at the federal level possibly at most delaying the implementation of some key initiatives. For instance, we don't expect the Kraftwerkstrategie to be finalized before the election in February 2025, which could push tenders to later that year as several power generators expect a clear regulatory framework to take investment decisions. We see these delays as more detrimental to the country's transition than to utilities' credit quality per se. On the other hand, we expect credit-supportive updates on regulated grids to run independently from changes in government and continue to monitor how the regulatory framework adapts to the tripling capex that power transmission system operators are undergoing. In addition, the impact of the capex super-cycle on credit quality will depend on operators' funding elections, including any shareholder support. We see the ramp-up of a hydrogen supply chain evolving slower than previously expected, which could extend the transition period for gas grid operators, potentially weakening their business profiles as conventional gas grid infrastructure matures. While such a weakening depends on multiple factors, including regulatory protection, overall we view the regulatory framework for hydrogen as slightly weaker than that for gas or power networks because of residual risks operators have to bear if the hydrogen ramp-up fails. For power generators, we expect coal capacity to be retired as planned (for instance, Uniper retired 2.9 GW of coal capacity in 2024), and expect operators owning an efficient combination of dispatchable and renewable generation capacity, and particularly for integrated utilities with trading activities, to fare better than single-technology issuers.

In the Nordics, continued softening of power prices, which could pressure some generators' cash flow. In addition, we expect price volatility to remain very high for most rated entities. This should heighten the competitive advantage of the most flexible and lowest-cost assets, namely reservoir-based hydro-production, which we expect to continue to reap strong cash flow during peak periods. We expect the market in 2025-2026 to be more volatile than before, in part as renewable production in the area has been high in recent years and export capacities increased. Intra-Nordics price differences have increased markedly. Growth of generation capacity remains uncertain; offshore expansion has generally come to a halt (except for a recently announced project in Finland) due to increased costs for interconnections and in Sweden, defense-related considerations. The debate on expansions of nuclear capacity in Sweden is likely to continue over 2025-2026. The government roadmap envisages new nuclear capacity equivalent to at least two large-scale reactors by 2035 and up to 10 by 2045. It remains to be seen, however, if the financial proposal, which includes a state-loan and a two-way contract-for-difference, will be attractive enough for market participants given the massive investment needed. Such a decision would reshape and affect the Nordic power market for decades, however, given its magnitude and very long asset lives.

Related Research

- [Issuer Ranking: EMEA Utilities Issuers Ranked Strongest To Weakest](#), Jan. 9, 2025
- [Is Europe Ready For A Nuclear Renaissance?](#), Dec. 9, 2024
- [WACC Revision For Italian Regulated Utilities Is In Line With Our Base Case And Shows Regulation's Consistency](#), Dec. 3, 2024
- [S&P Global Ratings Revises Its Oil Price Assumptions; North American And Dutch Title Transfer Natural Gas Price Assumptions Unchanged](#), Oct. 1, 2024
- [Utilities Handbook 2024 | Western Europe Regulated Gas](#), Sept. 16, 2024
- [The Energy Transition, Geopolitics, And Cannibalization Are Shaping Europe's Power Prices](#), Sept. 12, 2024
- [Some European Power Markets Will Suffer As Renewables Put Pressure On Prices](#), Sept. 12, 2024
- [Power Sector Update: European Offshore Wind Is Racing Ahead](#), Sept. 10, 2024
- [Utilities Handbook 2024 | Western Europe Regulated Power](#), Sept. 10, 2024
- [Industry Credit Outlook Update Europe: Utilities](#), July 18, 2024
- [European Electricity Producers' Credit Quality And Revenue-Support Contracts: It's Complicated](#), July 10, 2024
- [Europe's Power Producers Continue Their Balancing Act As Electricity Prices Stay Low](#), July 10, 2024
- [Italian Electricity And Gas Transmission And Distribution Frameworks: Supportive](#), May 14, 2024
- [European Utilities: The Rating Relevance Of Net-Zero Commitments](#), May 2, 2024
- [European Utilities' Net-Zero Ambitions Face Myriad Hurdles](#), May 2, 2024
- [Europe's Power Push: Can Project Finance Help Fund Interconnections?](#), Nov. 16, 2023

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