

# China's Surging Defaults Test Courts And Bond Recovery

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**S&P Global**  
Ratings

*This report does not constitute a rating action.*

# Key Takeaways

## Bond Recovery Offshore

- Offshore defaults surge to unprecedented 3.3% rate, may continue amid steep maturities in 2022.
- Most offshore default cases are resolved out-of-court, settled via tenders, exchanges and swaps.
- Offshore resolution time ranges from 5 to 18 months, with out-of-court the fastest while liquidation the longest.
- Recovery rate average 24% for in-court and 45% for out-of-court resolutions.
- Recovery rates for SOEs tend to be materially higher than for POEs, likely due to more assets or access to resources.

## Bond Recovery Onshore

- More failed firms with more contagion risk created a greater need for orderly post-default resolution.
- Most onshore default cases are resolved in-court, settled via a mixed use of cash, shares and bond swaps.
- Onshore resolution takes 4 to 20 months, while unresolved cases can drag on for 2 to 3 years.
- Similar to offshore recovery, cash recovery rate is much higher out-of-court (62%) than in-court (22%).
- Viable defaulters can resolve with tenders, but less viable ones may have little choice but court restructuring.

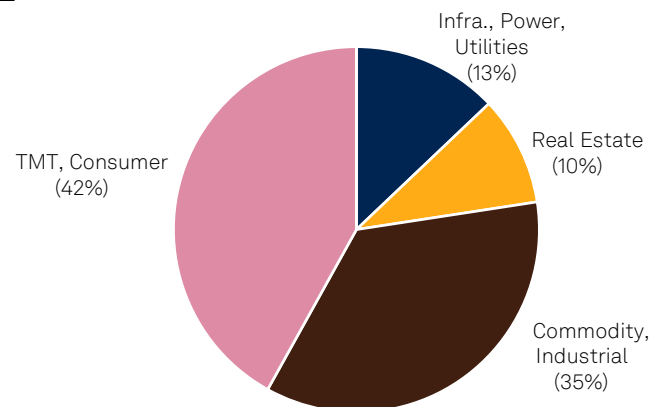
# Sample Overview: Bond Defaults And Resolutions

|                          | Offshore   |             |                |                             |              |                  | Onshore     |             |               |                             |              |                  |
|--------------------------|------------|-------------|----------------|-----------------------------|--------------|------------------|-------------|-------------|---------------|-----------------------------|--------------|------------------|
|                          | Bonds no.* | Issuers no. | Amt. Bil. US\$ | Default year (no. of bonds) |              |                  | Bonds no. § | Issuers no. | Amt. Bil. RMB | Default Year (no. of bonds) |              |                  |
|                          |            |             |                | Pre-2015                    | 2015 to 2019 | 2020 to 2022 YTD |             |             |               | Pre-2015                    | 2015 to 2019 | 2020 to 2022 YTD |
| POE                      | 193        | 72          | 79             | 32                          | 37           | 124              | 419         | 197         | 423           | 1                           | 228          | 190              |
| SOE                      | 31         | 10          | 12             | 2                           | 6            | 23               | 81          | 39          | 98            | 0                           | 34           | 47               |
| Central                  | 17         | 4           | 8              | 2                           | 0            | 15               | 31          | 15          | 47            | 0                           | 17           | 14               |
| Local                    | 14         | 6           | 4              | 0                           | 6            | 8                | 50          | 24          | 51            | 0                           | 17           | 33               |
| <b>Total</b>             | <b>224</b> | <b>82</b>   | <b>91</b>      | <b>34</b>                   | <b>43</b>    | <b>147</b>       | <b>500</b>  | <b>236</b>  | <b>521</b>    | <b>1</b>                    | <b>262</b>   | <b>237</b>       |
| Conglomerate             | 5          | 1           | 1              | 0                           | 1            | 4                | 61          | 23          | 64            | 0                           | 39           | 22               |
| Infra., power, utilities | 30         | 17          | 10             | 8                           | 15           | 7                | 43          | 17          | 51            | 0                           | 12           | 31               |
| Real estate              | 114        | 27          | 56             | 1                           | 7            | 106              | 69          | 29          | 83            | 0                           | 11           | 58               |
| Commodity, industrial    | 42         | 19          | 13             | 18                          | 15           | 9                | 222         | 101         | 224           | 1                           | 151          | 70               |
| TMT, consumer            | 33         | 18          | 11             | 7                           | 5            | 21               | 102         | 63          | 98            | 0                           | 46           | 56               |
| Other                    | 0          | 0           | 0              | 0                           | 0            | 0                | 3           | 3           | 1             | 0                           | 3            | 0                |

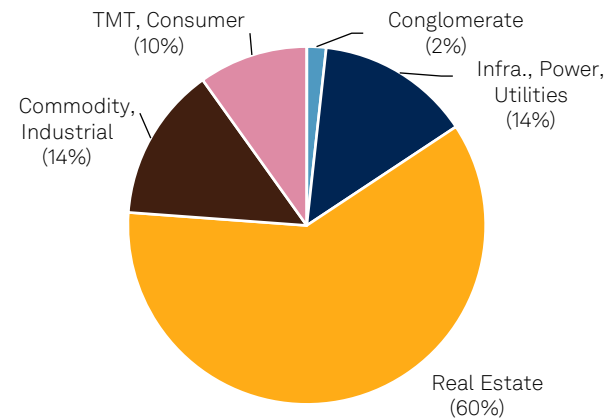
Note: Data as of April 27, 2022. Includes defaults of all nonfinancial Greater China corporates in the offshore U.S. dollar bond market from 1998 and China's domestic bond market from 2014. Amount is the amount at issuance. \*Total number of defaulted bonds in our data base, going back to 1998. §Total number of defaulted bonds in our data base, going back to 2014. Amt.--Amount. Bil.--Billion. YTD--Year to date. SOE--State-owned enterprise. POE--Privately-owned enterprise. Infra--Infrastructure. TMT--Technology, media, and telecom. Source: Wind, Bloomberg, S&P Global Ratings.

# Sample Overview: Bond Defaults And Resolutions By Industry

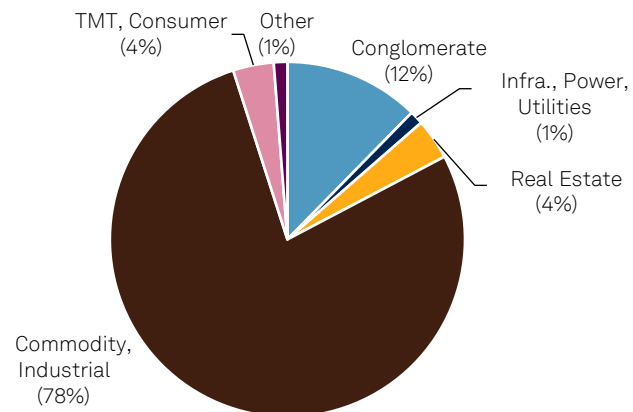
## Offshore SOE



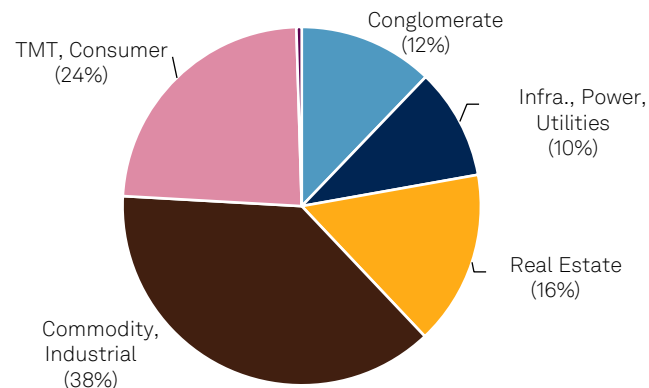
## Offshore POE



## Onshore SOE



## Onshore POE



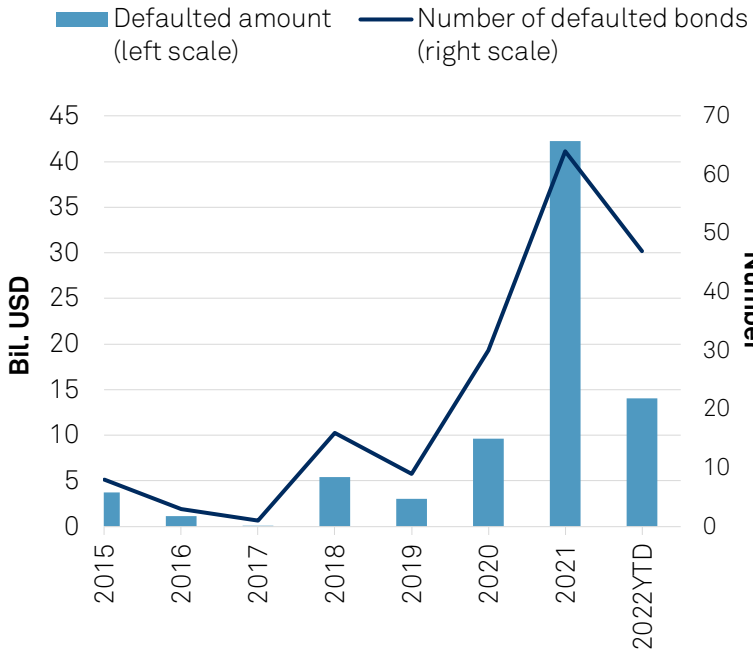
Note: Data as of April 27, 2022. Includes defaults of all nonfinancial Greater China corporates in the offshore U.S. dollar bond market from 1998 and China's domestic bond market from 2014. Percentages are calculated according to the number of bonds. SOE--State-owned enterprise. POE--Privately owned enterprise. Infra.--Infrastructure. TMT--Technology, media, and telecom. Source: Wind, Bloomberg, S&P Global Ratings.

# Bond Recovery Offshore

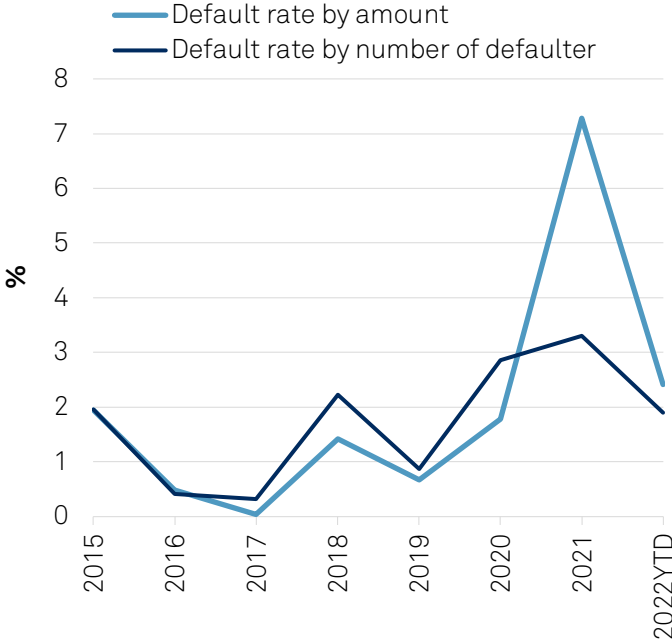
# Unprecedented Offshore Defaults Continue Amid Steep Maturities

- 2020 offshore defaults reached a historic high, driven by large SOEs such as QPIG and PUFG.
- 2021 broke that record by 4.2x in amount, with a 3.3% default rate driven by unprecedented failures of property firms.
- 2022 will see even more bonds due at US\$103 billion, larger than both 2020 (US\$87 billion) and 2021 (US\$96 billion).

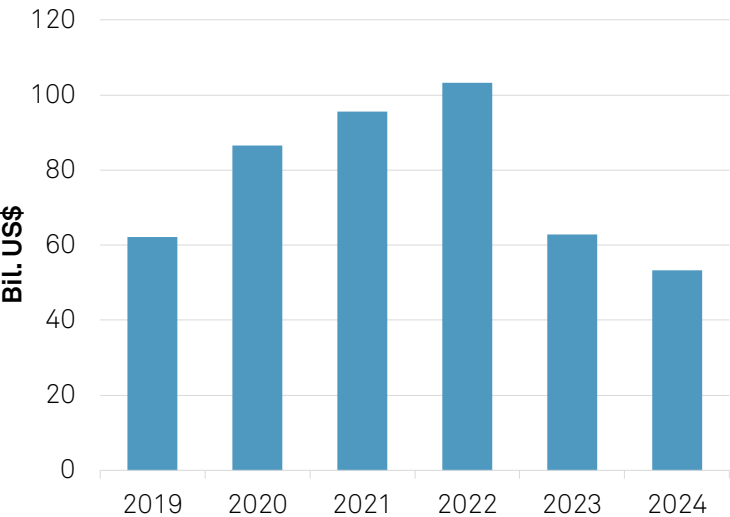
## Offshore Defaults Remain Elevated



## Default Rate Hits Record Levels



## Maturities Will Peak This Year

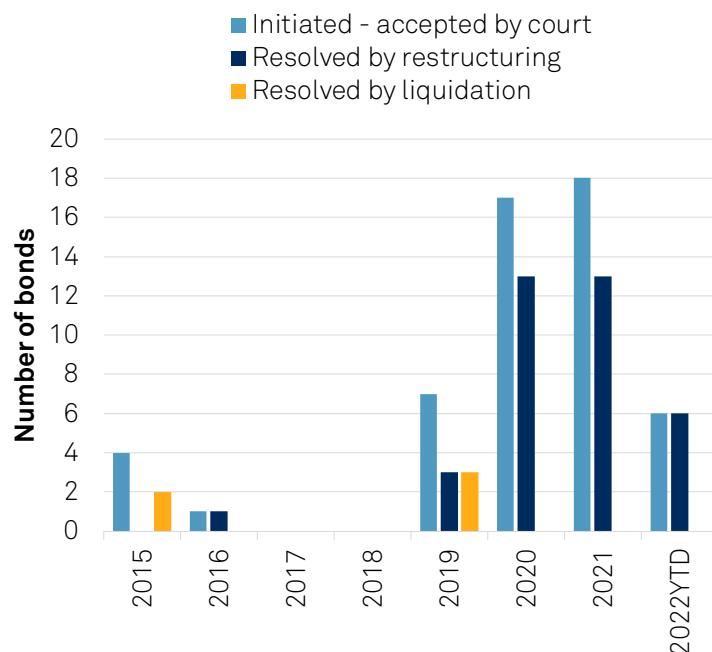


Note: Data as of April 27, 2022, includes all nonfinancial Greater China corporates in the offshore U.S.-dollar bond market. Defaults are failures to pay interest or principal in full and on time, including maturity extension and other distressed restructurings. Defaulted amount includes only the defaulted bond (i.e., not other debt by the same issuer). Number of defaulters is the number of first-time defaulted issuers. Maturing amount includes only bonds that mature or are puttable in the indicated years. Bil.--Billion. QPIG--Qinghai Provincial Investment Group. PUFG--Peking University Founder Group. Source: Bloomberg, S&P Global Ratings.

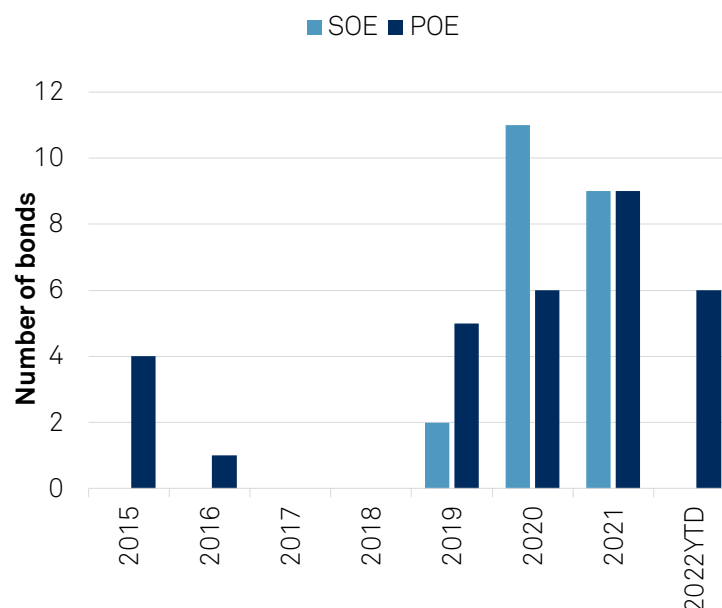
# More Offshore Bondholders Are Going To Court As Defaults Mount

- Cases entering offshore courts more than doubled since COVID began as both SOE and POE cases multiplied.
- Most resolved offshore cases have been resolved through restructurings.
- Liquidations became rare after 2019, with no cases in the past two years.

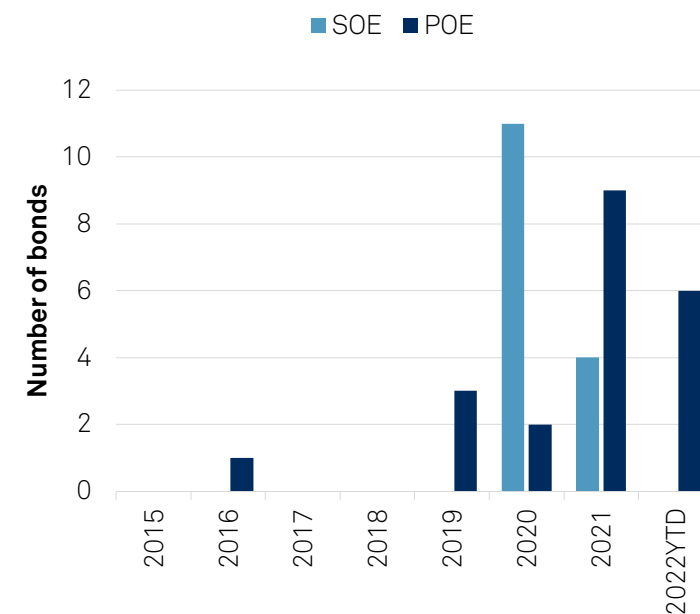
## In-Court Resolution Types



## Initiated--Case Accepted By Courts



## Resolved By In-Court Restructuring

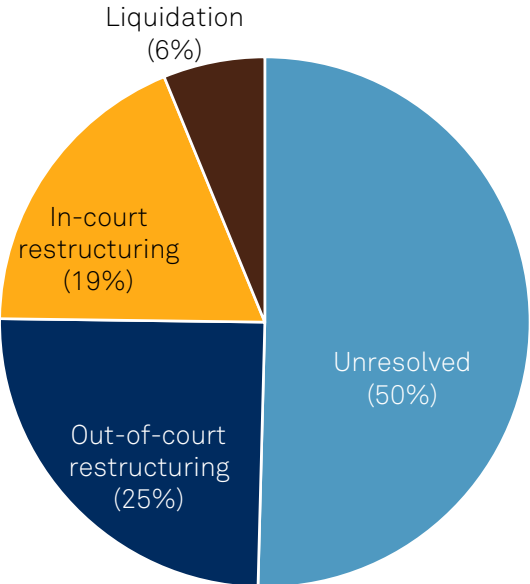


Note: Data as of April 27, 2022. Restructuring refers to in-court restructurings in which the normal operation of an entity is restored. Liquidation refers to a process in which an entity ceases normal operations and distributes or sell assets to repay relevant stakeholders. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: S&P Global Ratings.

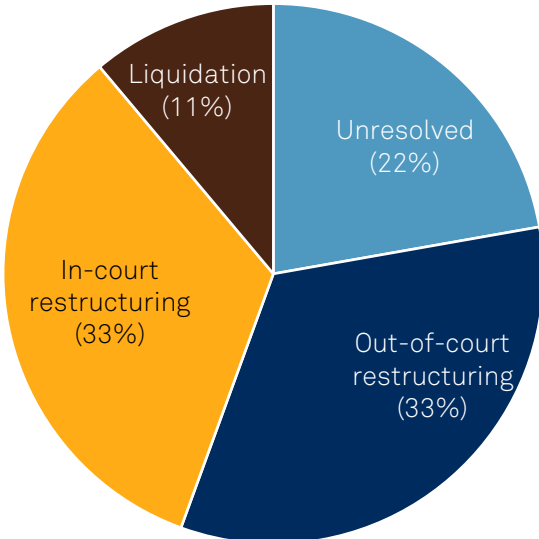
# Most Offshore Cases Are Resolved Out-Of-Court

- A quarter of offshore defaults were resolved by out-of-court restructurings, only 19% by in-court restructurings.
- More SOEs are resolved in court (33%) vs. POEs (15%), likely due to more complexity and stakeholders, may need defined processes.
- Half of the cases remain unresolved, a fifth for SOEs (22%), and over half for POEs (57%).
- Liquidations remain rare at 6% of cases, as they tends to be the last resort that most stakeholders aim to avoid.

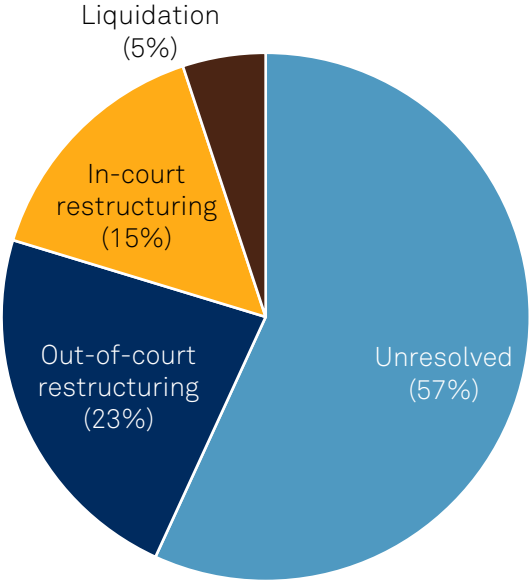
**Overall**



**SOE**



**POE**



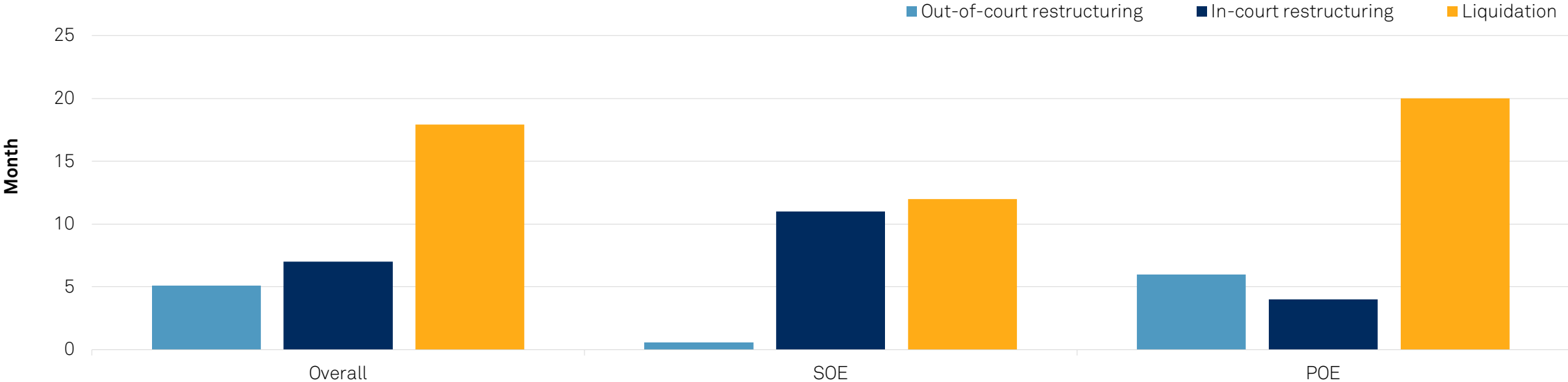
*Note: Data as of April 27, 2022. Percentages are calculated according to the number of bonds, not the value of bonds. Percentages in the charts do not total 100% due to rounding. SOE--State-owned enterprise. POE---Privately-owned enterprise. Source: S&P Global Ratings.*



# Offshore Resolution Time: Five to 18 Months

- Out-of-court resolutions are the fastest on average at five months, followed by in-court at seven months.
- Liquidations take the longest at 18 months, as they are often the last resort after other options fail.

## Average Resolution Time

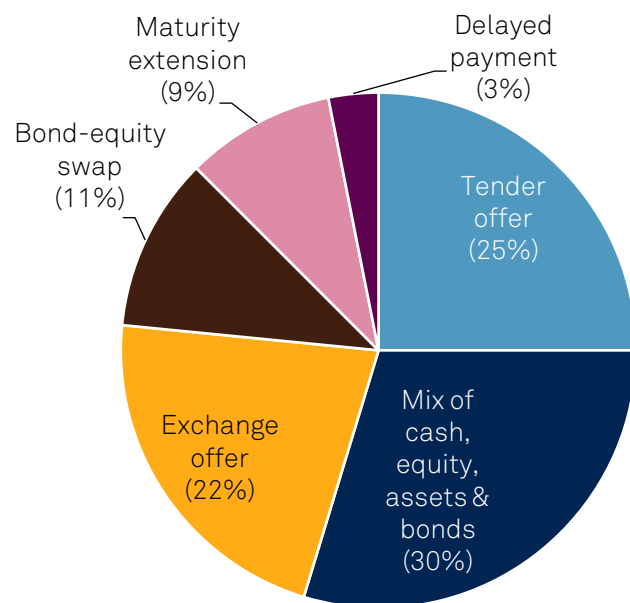


*Note: Data as of April 27, 2022. All the numbers shown above are calculated as an average. Agreement settlement date earmarks the end of an out of court restructuring process. Court acceptance marks a case entering court process and court approval marks an official end of it. GITIC was the only SOE liquidation case offshore and was excluded as it was not representative. GITIC -- Guangdong International Trust and Investment Corp. SOE-- State-owned enterprise. POE--Privately-owned enterprise. Source: S&P Global Ratings.*

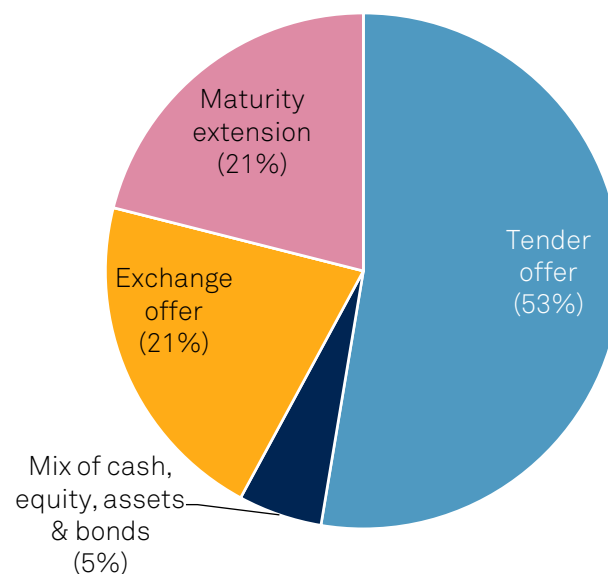
# Offshore Settle Out-Of-Court Via Tenders, Exchanges, Mixed Assets

- For cases resolved out-of-court, about half involve bond tenders or exchange offers, the rest used mixed assets, swaps or extensions.
- For SOEs, 53% paid cash (tender), 42% extended or exchanged, as more SOEs have assets to back these options.
- For POEs, most paid in mixed assets (40%) or exchanged (22%), as fewer may have enough assets to back options above.

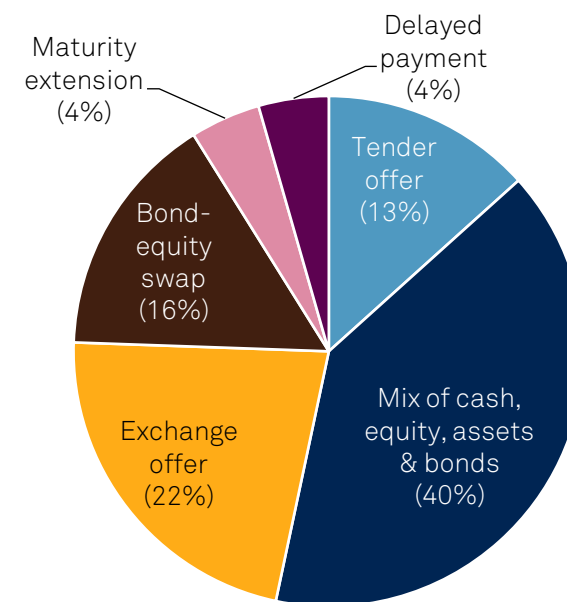
## Overall



## SOE



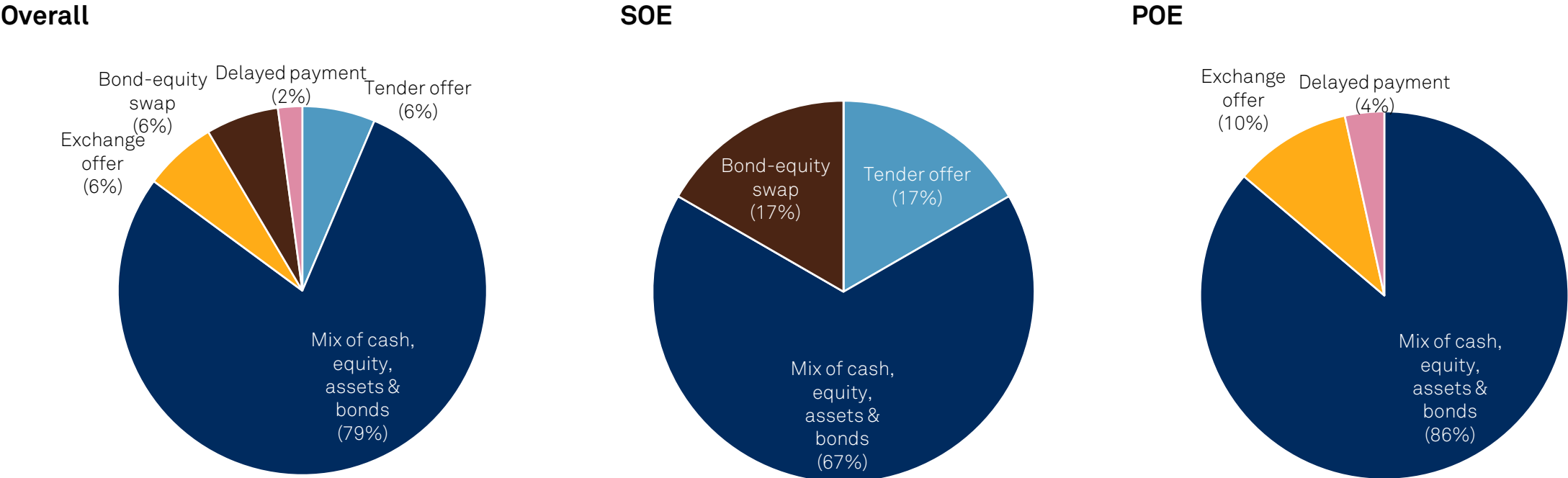
## POE



Note: Data as of April 27, 2022. Percentages are calculated according to the number of bonds. Percentages in the charts do not total 100% due to rounding. Tender offer--issuer buys back the outstanding bonds with cash only, usually at a haircut rate. Bond-equity swap--no cash repayment involved, bonds are exchanged for shares of a company or a trust plan. Exchange offer--no cash repayment involved, bonds are exchanged into a series of newly issued bonds with a different coupon rate and/or maturity date (including maturity extension). Delayed payment--issuer repays in full with cash at a later date with no negotiation process involved. Mix of cash, equity, assets, and bonds--a combination of above-mentioned methods. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: S&P Global Ratings.

# Offshore Compensate In-Court With Mixed Assets

- About 80% of offshore cases resolved in court pay a mix of cash, equity, assets, and bonds.
- This is true for 67% of SOE bonds and 86% of POE bonds.
- Offshore cases that end in court pay a mix as they often don't have enough assets; those that do tend to resolve out-of-court.

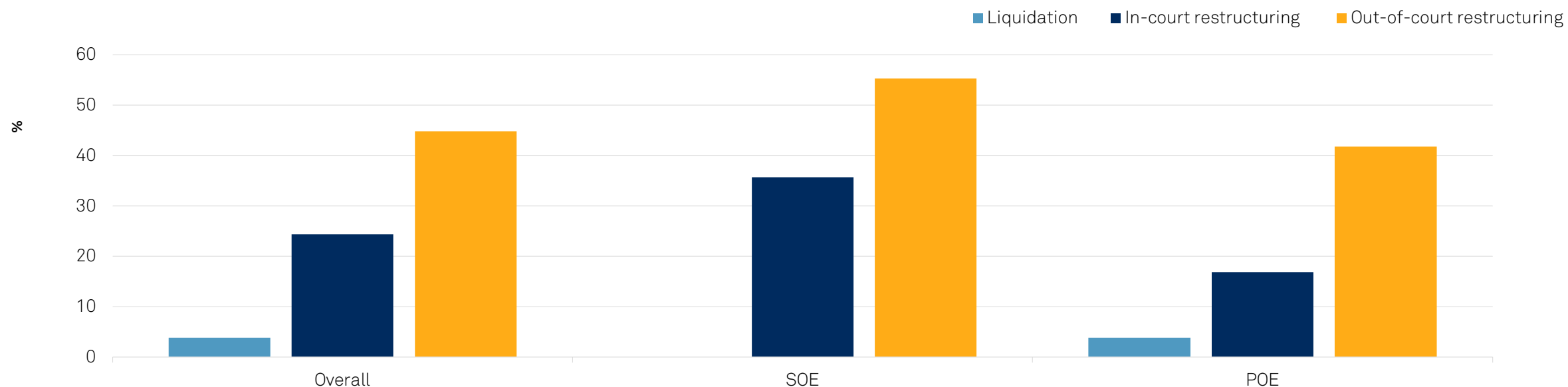


Note: Data as of April 27, 2022. Percentages are calculated according to the number of bonds. Percentages in the charts do not total 100% due to rounding. Tender offer--issuer buys back the outstanding bonds with cash only, usually at a haircut rate. Bond-equity swap--no cash repayment involved, bonds are exchanged for shares of a company or a trust plan. Exchange offer--no cash repayment involved, bonds are exchanged into a series of newly issued bonds with a different coupon rate and/or maturity date (including maturity extension). Delayed payment--issuer honors repayment with cash at a later date with no negotiation process involved. Mix of cash, equity, assets, and bonds--a combination of above-mentioned methods. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: S&P Global Ratings.

# Offshore Cash Recovery: 24% In-Court, 45% Out-Of-Court

- Recovery rates of Chinese global bonds average 24% for in-court and 45% for out-of-court resolutions.
- In-court, the SOE recovery rate (36%) is double that of POEs (17%); out of court, SOEs (55%) are a third higher than POEs (42%)
- In-court or out-of-court, recovery rates for SOEs tend to be higher than for POEs, likely due to more assets or access to resources.

## Average Cash Recovery Rate

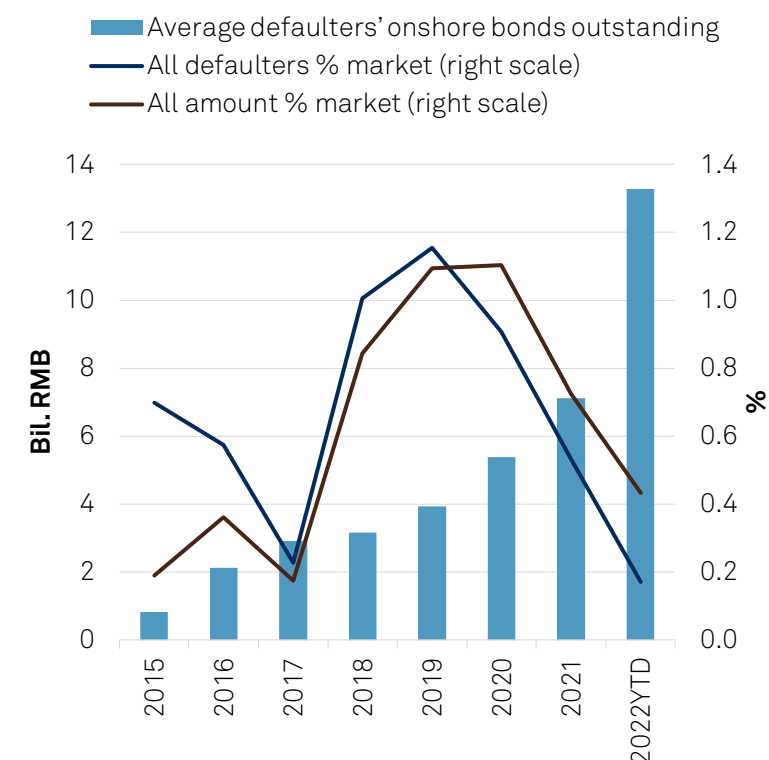
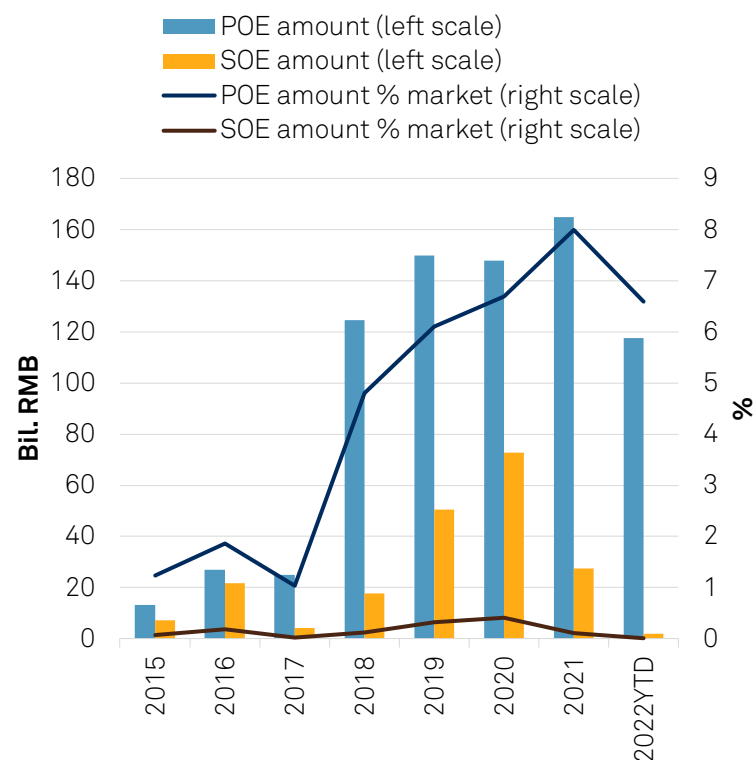
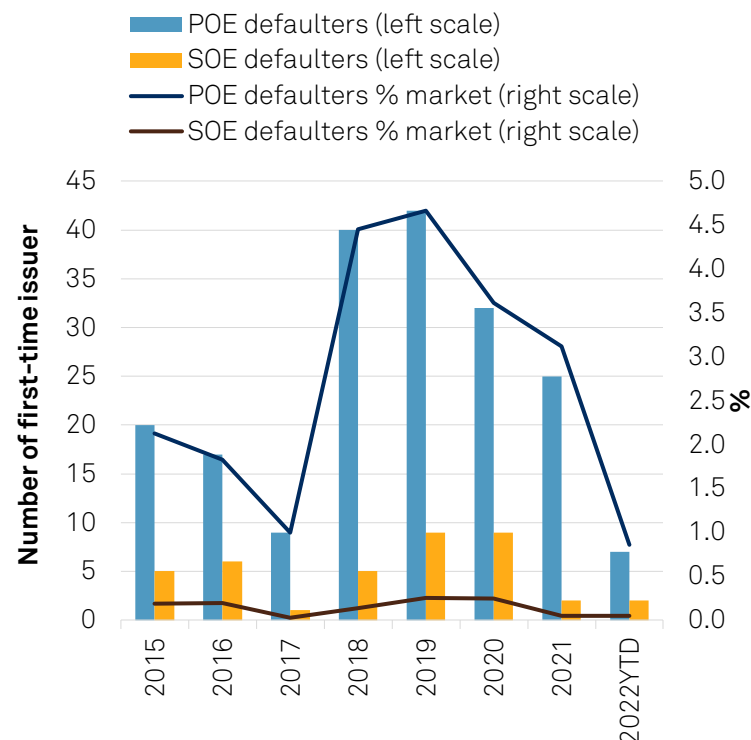


*Note: Data as of April 27, 2022. All the numbers shown above are calculated as an average. Cash recovery rate is calculated as upfront cash repayment per 100 of principal amount. Compensation that does not include cash portion of repayment (e.g., pure maturity extension, conversion into equity, or a combination of both) will not be included in the cash recovery calculation. Guangdong International Trust and Investment Corp was the only SOE liquidation case offshore and was excluded as it was deemed not representative. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: S&P Global Ratings.*

# Bond Recovery Onshore

# Surging Domestic Defaults Are Driving Resolution Needs...

- In the onshore market, bonds of defaulted POEs spiked fivefold in 2018, bonds of defaulted SOE quadrupled from 2018 to 2020.
- In 2021, defaulters had RMB7 billion of onshore bonds on average, 2.3 times 2017, seven times 2015. In 2022, this doubled again.
- More failed firms with more contagion risk created a greater need for orderly post-default resolution.

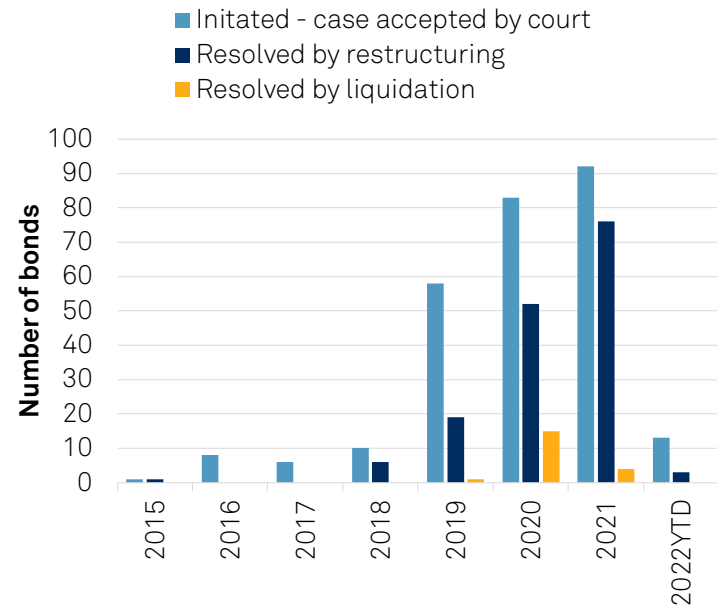


Note: Data as of April 27, 2022, includes all nonfinancial corporates in China's domestic bond market. Defaults are failures to pay interest or principal in full and on time, including maturity extensions and other distressed restructurings. Default amount is defaulters' bonds outstanding on the date of first default, defaulter number is the number of first-time defaulters. Market is total bonds outstanding or number of issuers in the market. Bil.--Billion. RMB--Chinese renminbi. SOE--State-owned enterprise. POE--Privately-owned enterprise. YTD--Year to date. Source: Wind, S&P Global Ratings.

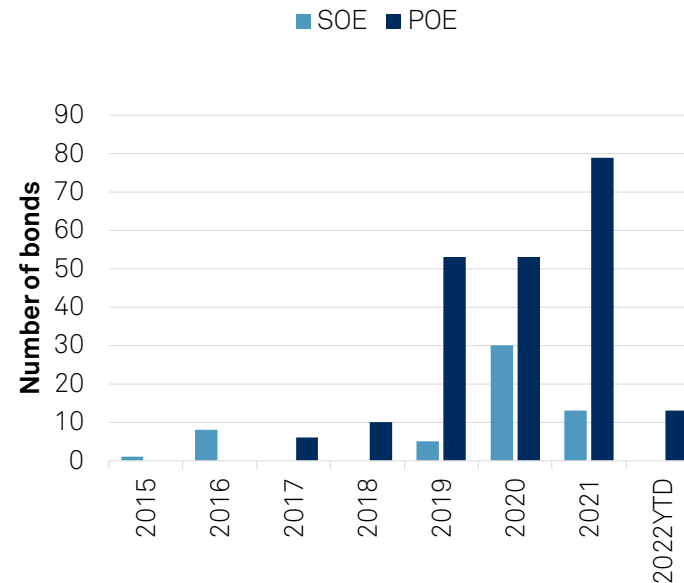
# ... And Pushing More Cases To Onshore Courts

- Cases entering the courts grew ninefold between 2018 and 2021 as both SOE and POE cases multiplied.
- The courts' resolution record improved and kept pace with rising caseloads.
- Contrary to expectations, most court cases did not end in liquidation--only 18% did in 2020, and 4% in 2021.
- As courts continue to function and liquidations remain rare, more cases are likely to go to court.

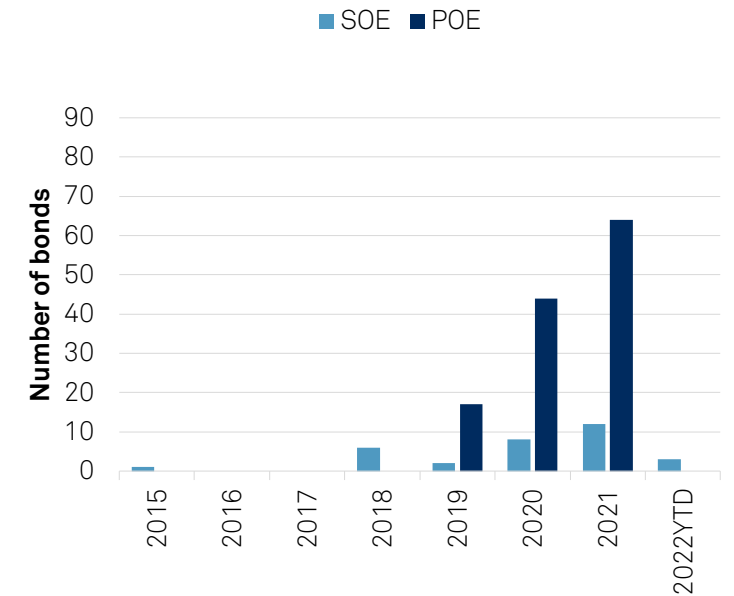
## In-Court Resolution Types



## Initiated – Case Accepted by Courts



## Resolved by Restructuring

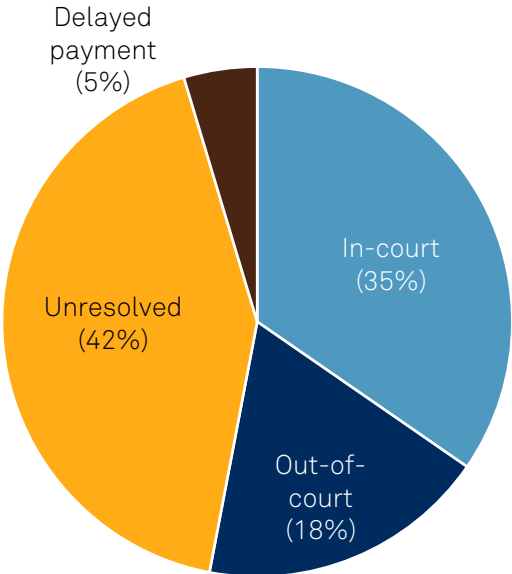


Note: Data as of April 27, 2022. Restructuring refers to in court restructuring in which normal operations of an entity is restored. Liquidation refers to a process in which an entity ceases normal operations and distributes assets to repay relevant stakeholders. SOE--State-owned enterprise. POE--Privately-owned enterprise. YTD--Year to date. Source: Wind, S&P Global Ratings.

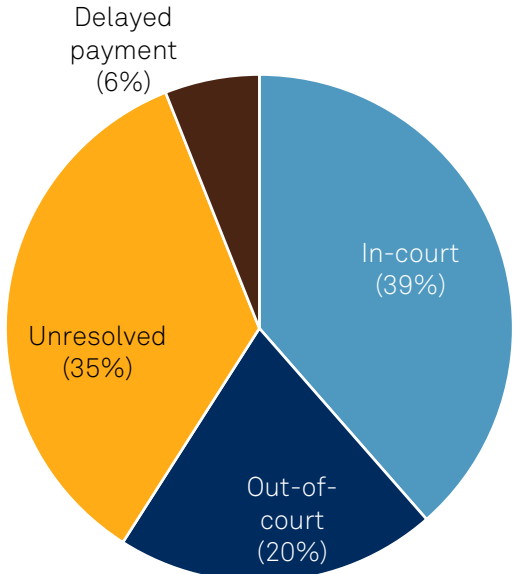
# Most Onshore Cases Are Resolved In-Court

- A third (35%) of all domestic bond defaults to date were resolved in-court, and a fifth (18%), out-of-court.
- Nearly half (42%) of cases remain unresolved.
- More SOE cases are resolved in-court (39%) than POEs (34%), as SOEs tend to be more complex and involve more stakeholders, making unstructured out-of-court resolutions more challenging.

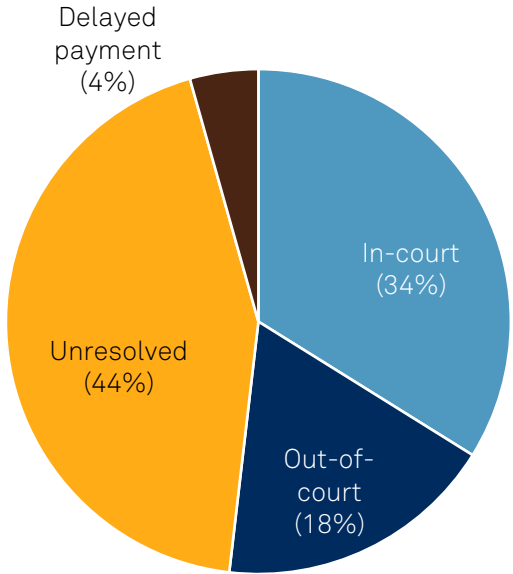
Overall



SOE



POE

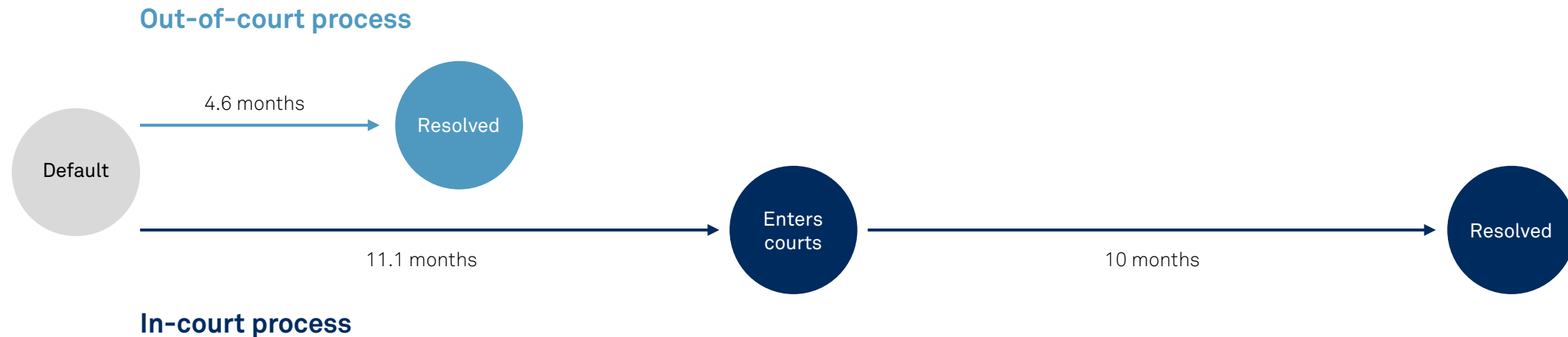


Note: Data as of April 27, 2022. Percentages are calculated according to the number of bonds. Delayed payment refers to an issuer making repayment afterwards without entering any negotiation process on bond terms, which is not treated as a resolution approach in our definition. In-court--In-court restructuring and liquidation. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: Wind, S&P Global Ratings.



# Onshore Resolution Time: Four To 20 Months

- On average, out-of-court resolutions take 4.6 months after default.
- If not resolved, they may take another 6.5 and 10 months after to enter and resolve in-court.
- SOE cases are resolved out-of-court in 1.5 months, if not, another 6.4 and 16 months after to enter and resolve in-court.
- POE cases are resolved out-of-court in 5.2 months, if not, another 6.7 and 8.9 months after to enter and resolve in-court.

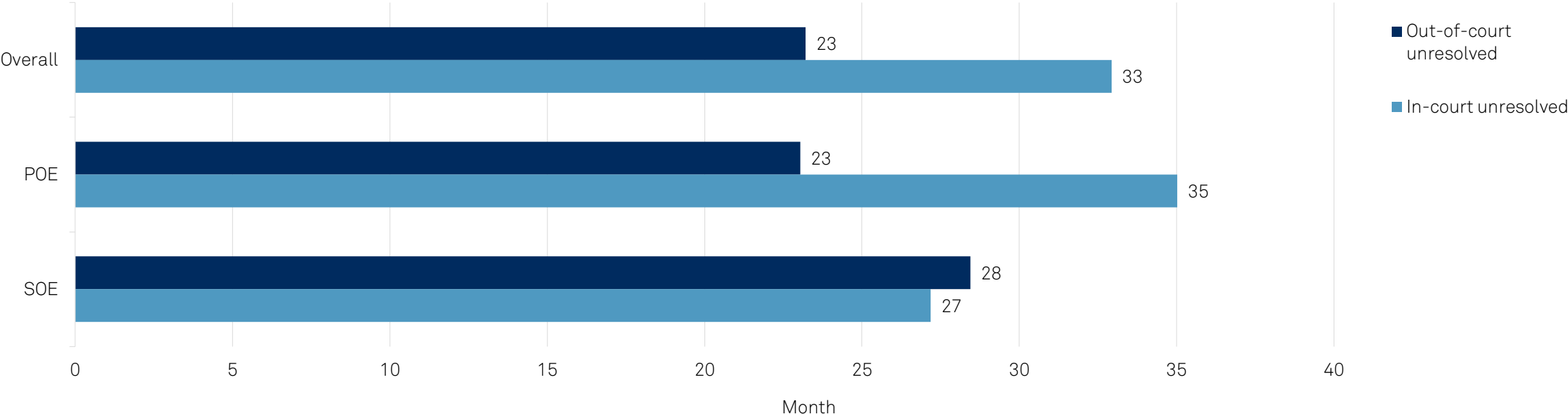


*Note: Data as of April 27, 2022. All the numbers shown above are calculated in average. The out-of-court restructuring in this slide does not include cases resolved via delayed payment. In-court--In-court restructuring and liquidation. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: Wind, S&P Global Ratings.*

# Unresolved Cases Can Drag On For Two To Three Years

- Unresolved cases can be stuck out-of-court for 23 months, and in-court for 33 months.
- SOE cases may drag on out-of-court for 28 months and in-court for 27 months.
- POE cases may remain unresolved out-of-court for 23 months and in-court for 35 months or longer.

## Average Resolution Time

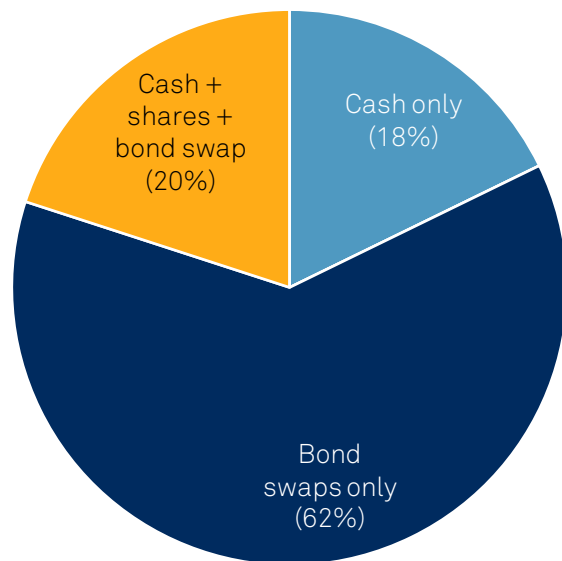


*Note: Data as of April 27, 2022. All the numbers shown above are calculated in average. The out-of-court restructuring in this slide does not include cases resolved via delayed payment. Unresolved time is the time from default date of an individual bond to April 27, 2022. In-court--In-court restructuring and liquidation. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: Wind, S&P Global Ratings.*

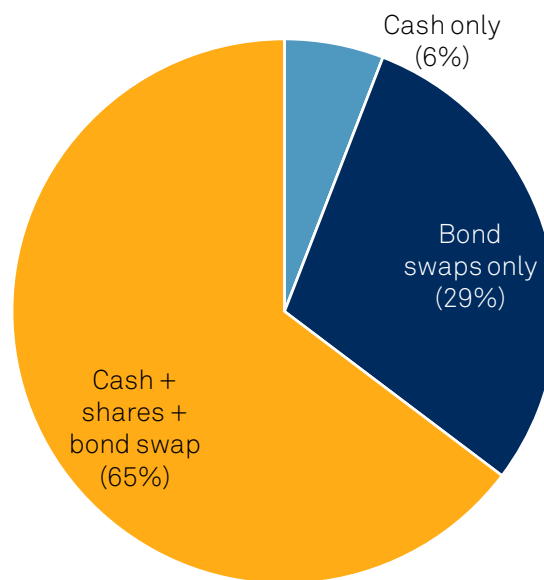
# Onshore Compensation Out-Of-Court: Expect Bond Swaps

- Recovery is highest with "cash only" but they make up less than a quarter of cases resolved out-of-court.
- A mix of cash, shares and bond swaps make up 20% of cases.
- "Bond swaps only" is by far the most common at 62%, may be due to onshore holders often not having to book them as defaults.

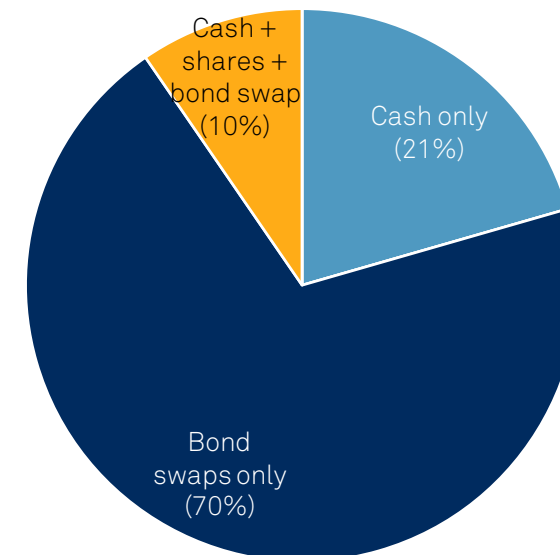
## Overall



## SOE



## POE

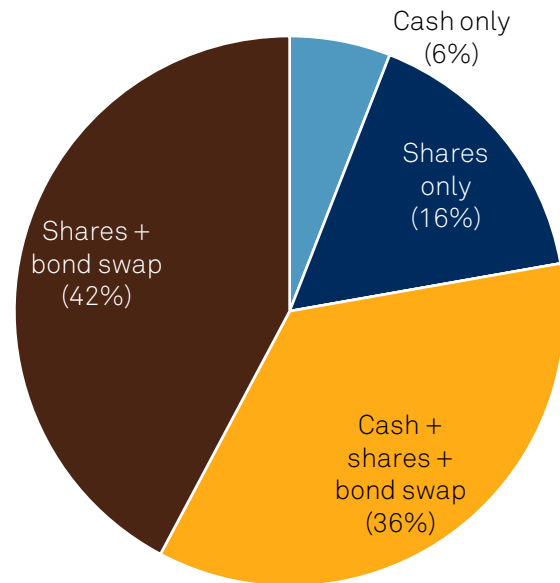


Note: Data as of April 27, 2022. Percentages are calculated according to the number of bonds. Percentages in the chart on the right do not total 100% due to rounding. Shares--No cash repayment involved; bonds are exchanged into shares of an entity. Bond swaps--No cash repayment involved, bonds are exchanged into a series of newly issued bonds with a different coupon rate and/or maturity date. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: Wind, S&P Global Ratings.

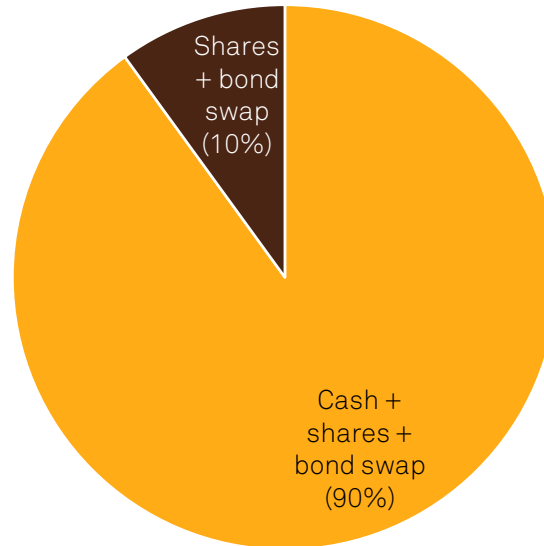
# Onshore Compensation In-Court: Expect Mixed Assets

- For cases resolved in-court, 6% paid cash only, 16% shares only, 42% shares and bond swaps, 36% in all three.
- For SOEs, none paid in cash or shares only, 10% paid in shares and bond swaps, and 90% in all three.
- For POEs, 8% paid cash only, 21% shares only, 51% shares and bond swaps, and 20% in all three.

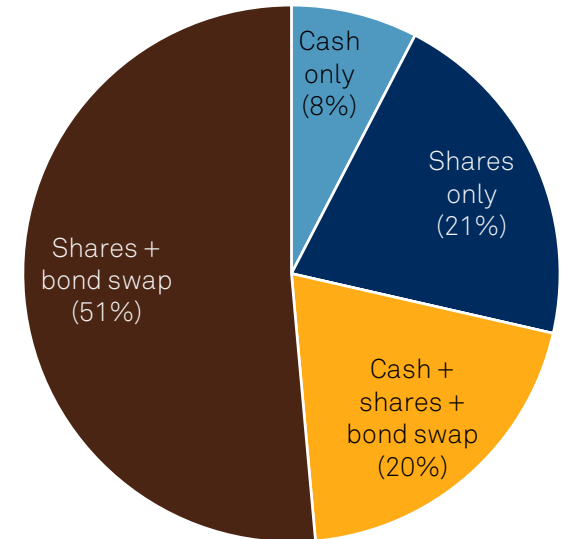
## Overall



## SOE



## POE

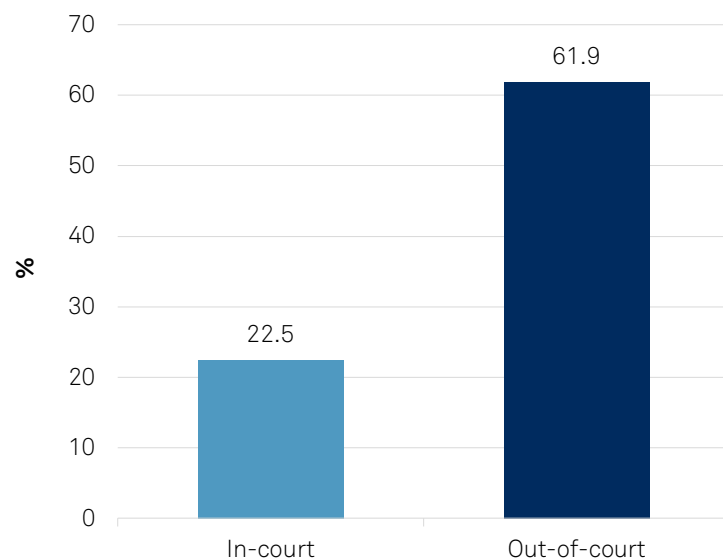


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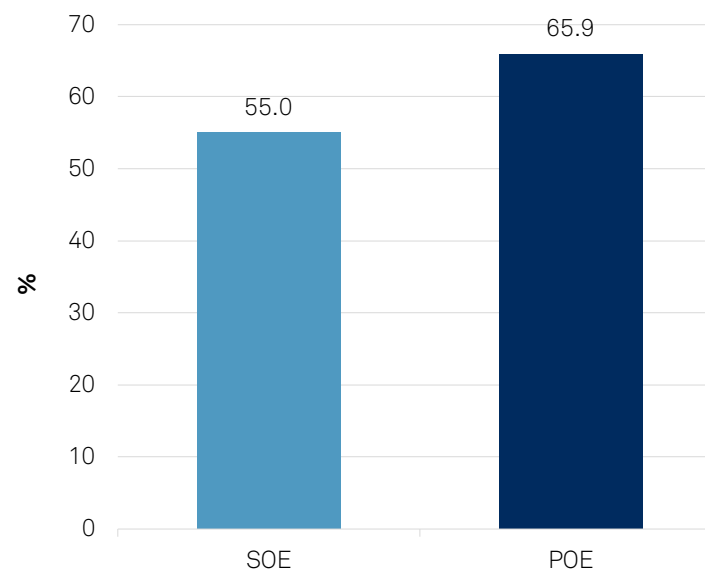
# Onshore Cash Recovery: 22% In-Court, 62% Out-Of-Court

- Cash recovery rate is much higher out-of-court (62%) than in-court (22%), as viable defaulters can resolve with tender offers, but less viable defaulters may have little choice but to accept a court restructuring.
- Out-of-court cash recovery is 55% for SOEs, 66% for POEs, as SOEs are more likely to use non-cash means.
- In-court cash recovery is 29% for SOEs, 14% for POEs, as POEs that end up in court often have less assets.
- So far, all onshore defaults that ended up in liquidation have been POEs.

## Overall



## Out-of-court



## In-court



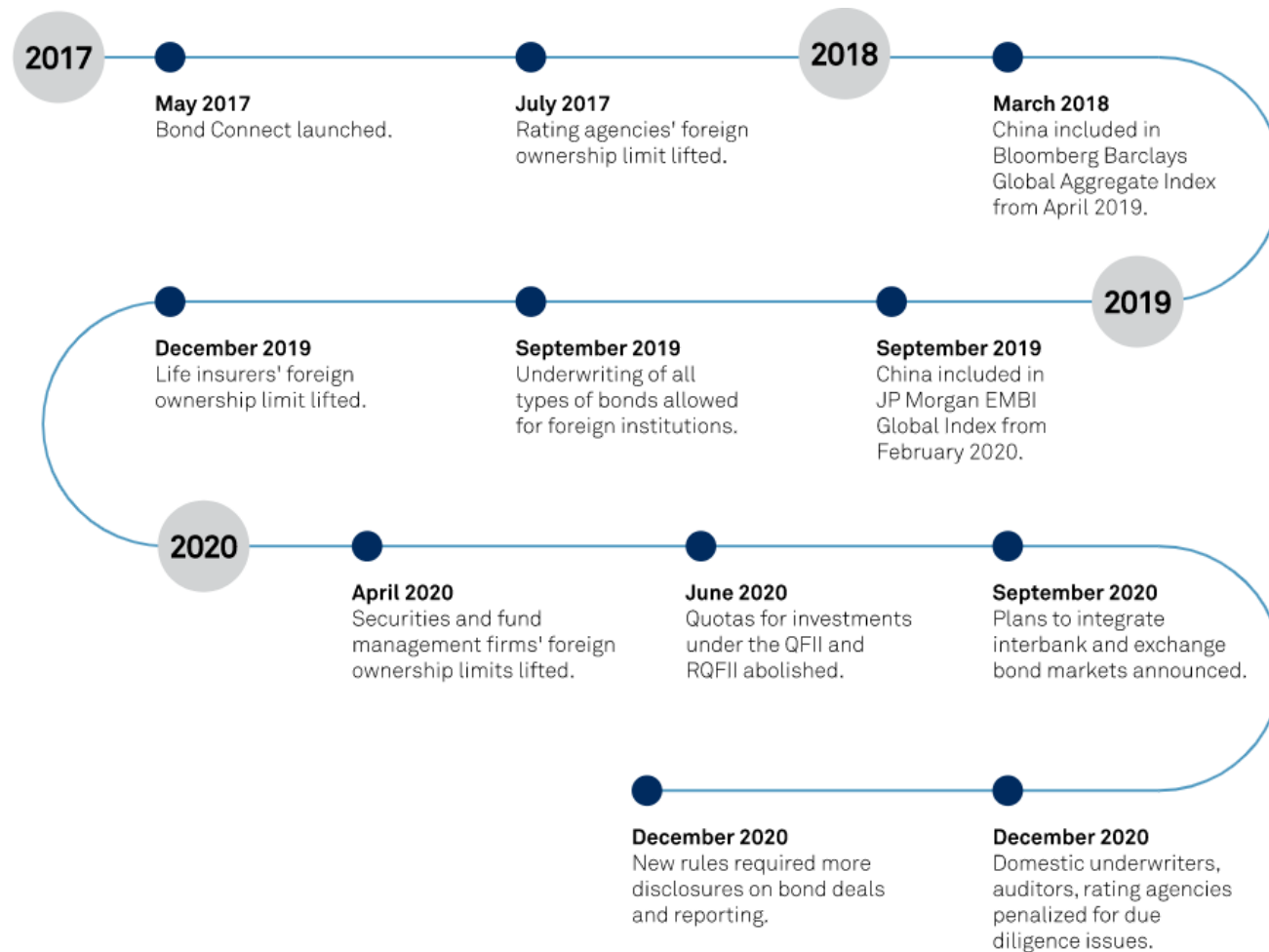
*Note: Data as of April 27, 2022. All the numbers shown above are calculated in average. The cash recovery rate is calculated as upfront cash repayment per 100 of principal amount. Compensation that does not include cash component (e.g., pure maturity extension, conversion into equity or a combination of both) will not be included in cash recovery calculation. The out-of-court restructuring in this slide does not include cases resolved via delayed payment. In-court--In-court restructuring & liquidation. SOE--State-owned enterprise. POE--Privately-owned enterprise. Source: Wind, S&P Global Ratings.*

# Appendix

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**S&P Global**  
Ratings

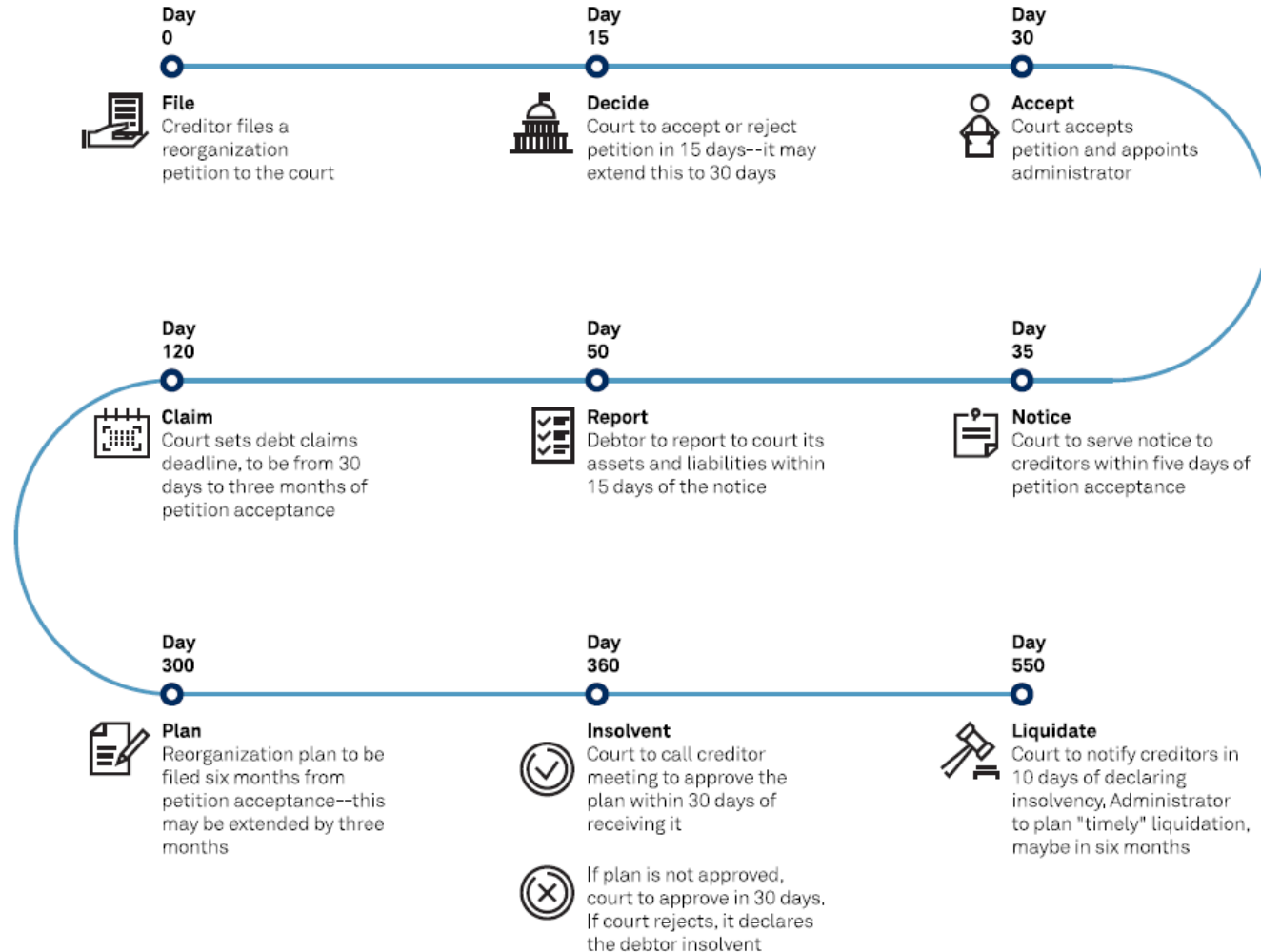
# China Is Pushing Efficiency And Market Discipline



- China is shifting its growth model to focus on efficiency
- This is driving a need to allow markets to allocate capital more efficiently
- Government sees this need and is pushing market opening and discipline
- This means more tolerance for defaults of unfit firms, including SOEs

Note: See "China's Bond Market: As Governance Improves, Foreign Entry Could Grow," published May 24, 2021. RQFII--Renminbi qualified institutional investor. Source: National Association of Financial Market Institutional Investors, State Council of the People's Republic of China, People's Bank of China, Asian Development Bank, Asia Securities Industry & Financial Market Association, International Capital Market Association, National Bureau of Economic Research, S&P Global Ratings.

# China's Legal Bankruptcy Process Is Well-Defined



- Onshore defaults in China historically had widely varying outcomes
- This is not because the legal framework lacks specificity. It is because defaults are new
- Defaults started in 2014; creditors and the courts are not experienced in dealing with them
- Out-of-court processes are undefined and create much uncertainty...
- ...and it takes time for stakeholders to decide to go to court, often due to their fears of low recovery from liquidation

Note: See "China Defaults: What To Expect When," published Dec. 1, 2020. Source: China Enterprise Bankruptcy Law, S&P Global Ratings.



# Related Research

- [China's Property Downcycle Won't End With Policy Easing](#), April 7, 2022
- [China's Soft Landing May Come With Surprises](#), March 11, 2022
- [Asia-Pacific Corporate And Infrastructure Outlook 2022](#), Feb. 14, 2022
- [China's Contagion Risks Rise](#), Nov. 10, 2021
- [China Balances Policy Risk With A Need For Reform](#), Oct. 13, 2021
- [Evergrande Default Contagion Risk--Ripple Or Wave?](#) Sept. 20, 2021
- [China's Zero-COVID Approach To Aggravate Rising Corporate Risks](#). Sept. 6, 2021
- [China Developers Battle Tight Liquidity And Plummeting Profitability](#). Sept. 6, 2021
- [China Bond Defaults 2021: More Tolerance For Bigger Hits](#), June 23, 2021
- [China's Bond Market: As Governance Improves, Foreign Entry Could Grow](#), May 24, 2021
- [China Defaults: What To Expect When](#), Dec. 1, 2020

# Abbreviations Used In This Report

RMB--Chinese renminbi.

1H--First half.

SOE--State-owned enterprise.

POE--Privately-owned enterprise.

Gov.--Government.

YTD--Year to date.

ESG--Environmental, Social, Governance.

LGFV--Local government financing vehicles.

Bil.--Billion.

LRG--Local and regional government.

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