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## A.P. Moller - Maersk A/S

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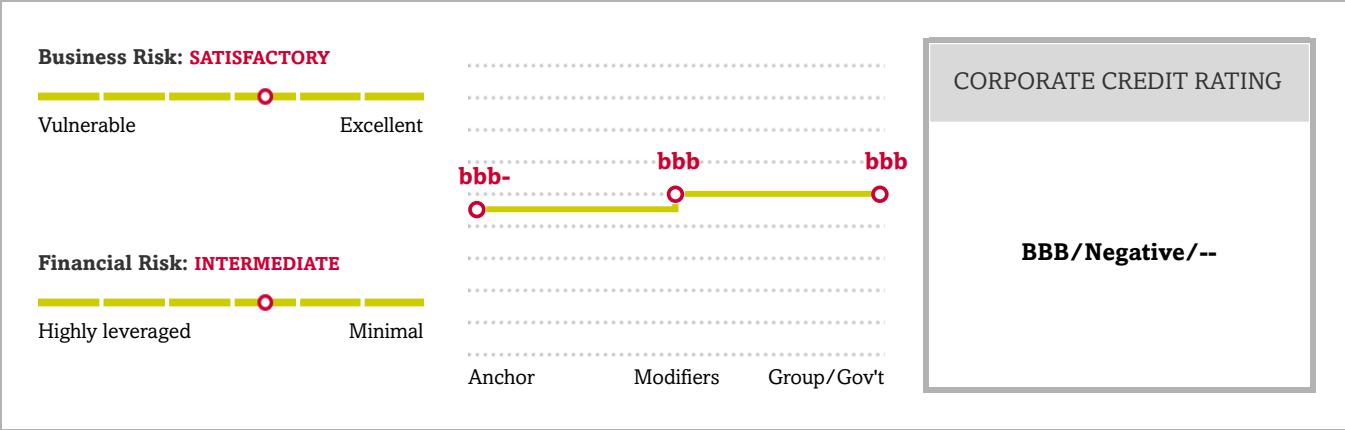
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# A.P. Moller - Maersk A/S



## Rationale

Business Risk: Satisfactory	Financial Risk: Intermediate
<ul style="list-style-type: none"> <li>• Large and diversified scale and scope of operations.</li> <li>• Leading global market positions in container liner operations and terminals, and strong position in energy segments such as drilling and exploration and production (E&amp;P).</li> <li>• Significant geographic and business diversification.</li> <li>• An ongoing strategic review may lead to less diversification benefits for the group in the future.</li> <li>• Our expectation that the cyclical downturn in transportation and energy sectors will lead to continued weak profitability at least over 2018.</li> </ul>	<ul style="list-style-type: none"> <li>• Expectations about continued robust liquidity and financial flexibility.</li> <li>• Over the cycle, the capital-intensive operations will continue to demand high investment from time to time.</li> <li>• Historically volatile free cash flow generation due to material swings in earnings and working capital patterns.</li> </ul>

**Outlook: Negative**

The negative outlook on A.P. Moller - Maersk A/S (Maersk) predominantly reflects the risk of a one-notch downgrade because of the group's ongoing strategic review, which could lead to materially less diversification benefits. The negative outlook also reflects that Maersk's credit metrics could deteriorate beyond our expectations, due to the very weak market conditions the group is currently facing, or if Maersk undertakes a large acquisition without any offsetting credit supportive actions.

**Downside scenario**

A negative rating action could occur if the reorganization leads to a majority of the ownership in either of the main energy business units (E&P or drilling) separating from the group. If so, we would likely remove the one-notch uplift for diversification, which would most likely lead to a one-notch downgrade. But we would also monitor how the proceeds from any potential sale of a division would be used; returning major divestment proceeds to shareholders would likely intensify pressure on the rating.

Furthermore, we could lower the rating if the industry downturn persists and becomes more severe than we currently anticipate, placing considerable strain on Maersk's profitability and cash flows. This pertains to Maersk's container segments, in particular.

Funds from operations (FFO) to debt of about 25% on a prolonged basis, with the limited likelihood of a near-term recovery to about 30%, would likely result in a downgrade.

**Upside scenario**

We currently see limited potential for an upgrade, given Maersk's exposure to volatile industries and uncertainty regarding its new strategy. We might revise the outlook to stable if the group's FFO to debt were to remain steadily above 30%, alongside positive free operating cash flows (FOCF) and continued diversification benefits. This assumes some modest recovery in shipping freight rates as well as of oil prices.

**Our Base-Case Scenario**

Assumptions	Key Metrics			
<ul style="list-style-type: none"> <li>• Ongoing muted global economic expansion as in recent years, with GDP growth of 3.5% in 2016 and 3.7% in 2017, after 3.4% in 2015. This average GDP growth rate hides wide regional variations. China, and many of the emerging market economies are slowing down; Brazil and Russia are in recession; while the economic growth in the U.S. and the eurozone should hold up.</li> <li>• Net oil production of 310,000-320,000 barrels per day in 2016, and oil price of \$42.5/bbl for the remainder of 2016 and \$45/bbl and \$50/bbl in 2017 and 2018, respectively. In the next few years we assume a material decrease in production, especially in 2018, following the cessation of a major contract in Qatar (about a third of production).</li> <li>• Transport volumes of about 10 million-11 million of forty-foot equivalent containers in 2016, with average freight rate of about \$1,800-\$1,850 per container.</li> <li>• About 36 million-38 million containers handled in the terminal business annually.</li> <li>• High operational uptime of 98% in 2016, with a contract coverage rate of 76% and 55% assumed in 2016 and 2017, respectively.</li> <li>• High-single-digit decline in revenues in 2016, mainly due to lower freight rates affecting the Maersk Line and lower oil prices affecting Maersk Oil. There is a low-single-digit increase in revenues in 2017 due to the slight uptick in volumes.</li> <li>• Annual FFO of \$5.5 billion-\$7.0 billion.</li> <li>• Gross capital expenditure (capex) of about \$4 billion-\$5 billion in 2016, a considerable decline from the 2015 levels of \$7.1 billion. In our base case, we anticipate lower investments in E&amp;P.</li> <li>• Dividends of about \$1 billion in 2016 with considerably lower payouts in 2017 and 2018. No share buybacks.</li> </ul>				
		<b>2015a</b>	<b>2016e</b>	<b>2017e</b>
	Unadjusted EBITDA margin (%)	24.3	16.0-18.0	16.0-18.0
	Debt to EBITDA (x)*	1.6	2.0-2.5	2.0-2.5
FFO to debt (%)*	49.7	27.0-32.0	27.0-32.0	
<p>*S&amp;P Global Ratings-adjusted. FFO--Funds from operations. a--Actual. e--Estimate.</p>				

## Company Description

Known primarily for its shipping operations, Maersk is a Denmark-based conglomerate present in 130 countries. Aside

from shipping, the group operates in energy industries, with a focus on the following core sectors:

- **Maersk Line:** It is the world's largest container shipping company with a fleet of over 600 vessels, as of September 2016, out of which 286 are wholly owned and 325 are chartered container vessels. Maersk Line controls about 16% of the market. Of the total \$46.6 billion invested capital, 43% relates to Maersk line. Maersk has also signed an agreement to acquire the German container liner Hamburg Sud. The transaction is expected to close in 2017 and would increase Maersk Line's market share to about 19%.
- **Maersk Oil:** With 312,000 barrels of net entitlement oil equivalents produced in 2015, Maersk Oil is a midsize E&P company. Production is predominantly focused in stable geographic areas, such as Denmark, the U.K., the U.S., the Gulf of Mexico, and Qatar. However, the contract in Qatar has not been extended so we foresee a decrease in production levels in 2017-2018 to the 160,000-180,000 level. Of the total \$46.5 billion invested capital, 9% relates to Maersk Oil.
- **APM Terminals:** It provides global port and cargo inland services. With about 36 million handled twenty-foot containers in 2015, Maersk's subsidiary APM Terminals is among the four largest terminal operators worldwide. Of the total \$46.5 billion invested capital, 17% relates to APM Terminals.
- **Maersk Drilling:** Maersk Drilling owns 23 rigs with the strongest concentration in the North Western Europe area where they maintain a market leadership. Of the total \$46.5 billion invested capital, 17% relates to Maersk Drilling.
- **APM Shipping Service:** The shipping service includes Maersk Supply Service, Maersk Tankers, Svitzer, and Damco. Of the total \$46.5 billion invested capital, 10% relates to shipping service.

The A.P Moller foundations, with 70.34% of the votes, controls Maersk. We believe it is very unlikely the ownership situation would change over the long term.

The management recently announced a reorganization of the group into two separate divisions, transportation and logistics, and energy, with a heavier focus on transportation going forward. This shift may lead to reduced ownership in one or several of the energy-related operations (Maersk Oil, Maersk Drilling, Maersk Supply Service, and Maersk Tankers) over the next 24 months. However, for now, we continue to incorporate our view of the group's broad diversification and strong positions in all of its key business lines, as no firm decision has been taken.

## **Business Risk: Satisfactory**

We believe Maersk's business risk profile has weakened over the past quarters, due to weaker industry fundamentals in many of its core areas, which will lead to substantially lower cash flow and profitability in 2016 and 2017 compared with previous years. Nevertheless, Maersk has major competitive advantages, notably in the container liner operations (Maersk Line generated about 36% of the group's EBITDA), resulting from its leading global footprint through a broad and strategically located route network; attractive fleet profile supported by a large, young, and diverse fleet; and strong customer diversification. We believe that the group's established track record of achieving significant cost savings and proactive efforts to continuously improve operating efficiencies will continue to support earnings. Negative factors include the group's participation in high-risk, competitive, and volatile industries, such as container shipping where depressed freight rates, owing to structural overcapacity and fierce competition for the market shares, have affected the margins. However, we still believe that Maersk has a better cost position than industry peers, making the group more resilient than most other operators.

In addition, most of Maersk's sectors are very capital intensive and require high ongoing investments, notably the E&P division. With an increased focus on the transportation sector, investments in the energy segment have been cut to very low level.

### Our Base-Case Operating Scenario

Under our base-case scenario, we expect the competitive position of the E&P division (representing 30% of the group's EBITDA in 2015) to worsen due to lower investments going forward and for production levels to lower when the Qatar contract expires, resulting in lower reserves and declining production. Persistently low oil and gas prices and lower production in 2017 is also likely to hinder results and hamper cash flow generations over the medium term.

We view Maersk's terminal operations as positive for the overall business risk profile, due to stability provided in earnings and margins, typically about 14%-18%. The terminal industry carries high barriers to entry, and we view Maersk's position as strong due to the large number of terminals (72 in operation), global presence, and long average remaining concession time. Going forward, we believe it's likely to play a more important role in the group's overall strategy. We notice that no other container line operator has such strong positions within the terminals.

In the short term, we expect Maersk's drilling division to benefit from decent contract rates (68% for the rest of 2016 at Q3), however, this is already likely to fall in 2017, leading to lower profitability. Performance will also be affected by the cost of keeping rigs idle. With the recent increase in the global fleet and much less demand for rigs, we foresee a sharp reduction in new contracts, compared with two-to-three years ago, which is likely to hamper profitability over the medium term. Maersk's drilling fleet is young, and in the past has repeatedly reported high utilization rates.

### Peer comparison

Maersk is a diversified company with participation in several uncorrelated businesses. Therefore, it is not possible to find perfectly matching peers with the same exposure. We are instead focusing on industry peers. On the transportation side, Maersk has two direct peers, CMA CGM S.A. and Hapag-Lloyd, the third and fifth largest container lines in the world, respectively.

Hess Corp is similar to Maersk Oil to the extent that it is a midsize E&P company. It is well-diversified geographically across key U.S. basins, Europe, West Africa, and Asia. Transocean Inc. is a direct peer of Maersk Drilling, albeit larger. It operates a fleet of offshore drilling units and provides oil and gas drilling project management services.

**Table 1**

A.P. Moller - Maersk A/S -- Peer Comparison					
Industry Sector: Oil & Gas Exploration & Production					
	A.P. Moller - Maersk A/S	CMA CGM S.A.	Hapag-Lloyd AG	Hess Corp.	Transocean Inc.
Rating as of Nov. 22, 2016	BBB/Negative/--	B/Negative/--	B+/Watch Neg/--	BBB-/Stable/NR	BB-/Negative/NR

Table 1

A.P. Moller - Maersk A/S -- Peer Comparison (cont.)					
Industry Sector: Oil & Gas Exploration & Production					
	A.P. Moller - Maersk A/S	CMA CGM S.A.	Hapag-Lloyd AG	Hess Corp.	Transocean Inc.
--Fiscal year ended Dec. 31, 2015--					
(Mil. \$)					
Revenues	40,308.0	15,674.1	9,603.4	6,636.0	7,386.0
EBITDA	11,600.5	2,340.4	1,475.9	3,586.5	4,319.0
Funds from operations (FFO)	9,202.4	1,666.2	1,112.0	3,562.2	3,465.9
Net income from cont. oper.	791.0	566.7	121.2	-3,008	789.0
Cash flow from operations	9,418.4	1,907.3	935.1	2,721.2	3,313.9
Capital expenditures	6,973.0	507.4	781.4	4,276.0	1,861.0
Free operating cash flow	2,445.4	1,399.9	153.7	(1,554.8)	1,452.9
Discretionary cash flow	(3,792.6)	1,300.8	151.4	(1,841.8)	1,071.9
Cash and short-term investments	3,569.0	1,217.7	602.4	2,716.0	2,339.0
Debt	18,512.9	10,587.9	5,790.0	8,419.4	7,102.4
Equity	35,797.1	5,405.5	5,480.9	20,401.0	14,816.0
<b>Adjusted ratios</b>					
EBITDA margin (%)	28.8	14.9	15.1	54.0	58.5
Return on capital (%)	3.2	7.1	4.1	(4.6)	14.9
EBITDA interest coverage (x)	11.4	3.8	4.2	5.3	7.3
FFO cash int. cov. (X)	23.4	8.8	6.0	11.3	7.0
Debt/EBITDA (x)	1.6	4.5	4.0	2.3	1.6
FFO/debt (%)	49.7	15.7	18.8	42.3	48.8
Cash flow from operations/debt (%)	50.9	18.0	15.7	32.3	46.7
Free operating cash flow/debt (%)	13.2	13.2	2.2	(18.5)	20.5
Discretionary cash flow/debt (%)	(20.5)	12.3	2.2	(21.9)	15.1

## Financial Risk: Intermediate

We forecast that Maersk's core credit ratios—FFO to debt and debt to EBITDA—will be about 27%-32% and 2.0x-2.5x, respectively, over 2016 and 2017. This is despite our forecast of materially lower EBITDA and FFO in the next two years, compared with 2014-2015, due to ongoing depressed industry conditions. The expected ratios are thanks only to significantly lower debt currently, compared with the past two-to-three years. We expect FFO in 2016 and 2017 of about \$5.5 billion-\$7.0 billion, respectively, down from \$9.2 billion in 2015. Furthermore, we believe management is proactive and has prudently pushed out debt maturities, which are fairly spread out.

We acknowledge the sharp reduction in capex and believe it's likely to be below management's public guidance for the full year 2016. We anticipate that the group will keep its investments at a low level in 2017, compared with previous

years, and we forecast capex of approximately \$4.0 billion-\$4.5 billion, which is about one-half of the amount spent in 2014. We believe this will lead to positive FOCF to debt of about 10%-15% in 2016 and 2017. Although this is positive for the credit ratios in the short term, we believe levels will remain high over in the investment cycle.

We perceive Maersk's new strategy as more aggressive than in the past in its container liners operations and believe Maersk will likely be an active consolidator in the container shipping industry, with an aim of expanding its market share, as evidenced by the recent announcement to acquire Hamburg Sud, which we view as a bolt-on acquisition. We factor in that the group will meet these expenses with the proceeds from disposals over time.

We believe that management, due to the group's size, has considerable financial flexibility, which should support management to keep a fairly strong balance sheet. We believe that management is committed to maintaining credit measures commensurate with an investment-grade rating. While we forecast that debt will have reduced to about \$18 billion-\$20 billion at year-end 2016 from \$31 billion in 2011, we also take into account that shareholder distributions are sometimes high. We make sizable adjustments to reported debt, mostly relating to operating leases and asset retirement obligations.

### Our Base-Case Cash Flow And Capital Structure Scenario

Our base-case assumptions for 2016 and 2017 include:

FFO of about \$5.5 billion-\$7.0 billion annually.

Gross capex of about \$4.0 billion-\$4.5 billion annually, although part of this is not committed.

S&P Global Ratings-adjusted FFO to debt at 27%-32%.

Debt to EBITDA between 2.0x-2.5x

## Financial summary

Table 2

### A.P. Moller - Maersk A/S -- Financial Summary

#### Industry Sector: Oil & Gas Exploration & Production

	--Fiscal year ended Dec. 31--				
	2015	2014	2013	2012	2011
Rating history	BBB+/Stable/--	BBB+/Stable/--	BBB+/Stable/--	-/-/-	-/-/-
<b>(Mil. \$)</b>					
Revenues	40,308.0	47,569.0	47,373.0	49,525.6	56,090.4
EBITDA	11,600.5	15,122.3	15,180.7	15,881.2	17,327.0
Funds from operations (FFO)	9,202.4	10,302.8	9,664.1	10,347.0	9,589.5
Net income from continuing operations	791.0	2,159.0	3,054.4	3,458.4	2,628.0
Cash flow from operations	9,418.4	10,211.8	10,544.2	8,894.3	8,616.2
Capital expenditures	6,973.0	8,404.0	6,083.6	7,476.7	7,274.6
Free operating cash flow	2,445.4	1,807.8	4,460.6	1,417.6	1,341.5

Table 2

A.P. Moller - Maersk A/S -- Financial Summary (cont.)					
Industry Sector: Oil & Gas Exploration & Production					
	--Fiscal year ended Dec. 31--				
	2015	2014	2013	2012	2011
Discretionary cash flow	(3,792.6)	528.8	3,393.7	472.0	481.2
Cash and short-term investments	3,569.0	2,886.0	2,389.5	1,206.7	1,782.1
Debt	18,512.9	19,190.5	23,977.3	29,123.2	31,145.3
Equity	35,797.1	42,225.0	42,597.0	39,347.8	36,226.1
<b>Adjusted ratios</b>					
EBITDA margin (%)	28.8	31.8	32.0	32.1	30.9
Return on capital (%)	3.2	9.1	11.3	11.5	14.7
EBITDA interest coverage (x)	11.4	12.8	10.7	10.1	10.3
FFO cash int. cov. (x)	23.4	14.5	13.2	12.4	10.6
Debt/EBITDA (x)	1.6	1.3	1.6	1.8	1.8
FFO/debt (%)	49.7	53.7	40.3	35.5	30.8
Cash flow from operations/debt (%)	50.9	53.2	44.0	30.5	27.7
Free operating cash flow/debt (%)	13.2	9.4	18.6	4.9	4.3
Discretionary cash flow/debt (%)	(20.5)	2.8	14.2	1.6	1.5

## Liquidity: Exceptional

We assess Maersk's liquidity as exceptional. We estimate that the group's liquidity sources will cover its uses by more than 2.0x over the 12 months started Oct. 1, 2016--even if EBITDA fell by 50%. In our view, management has a proactive approach toward financing planned capex, and debt maturities are fairly spread out. Although part of this cash is restricted, Maersk has large undrawn amounts under committed long-term credit facilities exceeding \$9 billion. The main facility of \$5.1 billion is not due until 2021. We further consider the group to have a high standing in the credit markets--as reflected in its low yields compared with its peers, large asset pool, a sound relationship with its banks, and generally prudent financial risk management.

We understand from management that there are no financial covenants in any corporate loan documentations. Also, we believe Maersk's business diversification will enable it to withstand high-impact, low-probability events without being forced into any major refinancing.

Principal Liquidity Sources	Principal Liquidity Uses
Cash and short-term investments of \$4.15 billion.	Upcoming debt maturities of about \$1.6 billion.
About \$9 billion of undrawn credit facilities.	Capex of about \$4 billion-\$5 billion.
Unadjusted FFO of about \$5.0 billion-\$5.5 billion.	Cash dividends below \$1 billion.

**Debt maturities**

As of Sept. 31, 2016:

:

- Within one year: \$1.6 billion
- Thereafter: \$13.8 billion

**Other Credit Considerations**

Despite the recent announcement about a potential reorganization of the group into two separate divisions, we view Maersk as a diversified company with its five core business units. The shift in strategy may result in reduced ownership in one or several energy-related operations but it would likely only happen over the next 24 months. We understand no firm decision has been taken yet and we therefore continue to view Maersk as moderately diversified in our analysis.

**Ratings Score Snapshot****Corporate Credit Rating**

BBB/Negative/--

**Business risk: Satisfactory**

- **Country risk:** Low
- **Industry risk:** Moderately high
- **Competitive position:** Satisfactory

**Financial risk: Intermediate**

- **Cash flow/Leverage:** Intermediate

Anchor: bbb-

**Modifiers**

- **Diversification/Portfolio effect:** Moderate (+1 notch)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Exceptional (no impact)
- **Management and governance:** Strong (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile : bbb

## Reconciliation

**Table 3**
**Reconciliation Of A.P. Moller - Maersk A/S Reported Amounts With S&P Global Ratings Adjusted Amounts (Mil. \$)**
**--Fiscal year ended Dec. 31, 2015--**
**A.P. Moller - Maersk A/S reported amounts**

	Debt	Shareholders' equity	EBITDA	Operating income	Interest expense	EBITDA	Cash flow from operations	Capital expenditures
Reported	12,743.0	35,087.0	9,814.0	1,870.0	256.0	9,814.0	7,969.0	7,132.0
<b>S&amp;P Global Ratings adjustments</b>								
Interest expense (reported)	--	--	--	--	--	(256.0)	--	--
Interest income (reported)	--	--	--	--	--	71.0	--	--
Current tax expense (reported)	--	--	--	--	--	(1,106.0)	--	--
Operating leases	6,874.8	--	1,941.5	502.9	502.9	1,438.6	1,438.6	--
Postretirement benefit obligations/deferred compensation	42.1	58.1	7.0	7.0	7.0	(20.7)	67.3	--
Surplus cash	(3,569.0)	--	--	--	--	--	--	--
Capitalized interest	--	--	--	--	159.0	(159.0)	(159.0)	(159.0)
Asset retirement obligations	2,422.0	--	--	--	89.0	5.5	102.5	--
Exploration costs	--	--	423.0	--	--	--	--	--
Non-operating income (expense)	--	--	--	71.0	--	--	--	--
Non-controlling Interest/Minority interest	--	652.0	--	--	--	--	--	--
EBITDA - Income (expense) of unconsolidated companies	--	--	(262.0)	(262.0)	--	(262.0)	--	--
EBITDA - Gain/(Loss) on disposals of PP&E	--	--	(478.0)	(478.0)	--	(478.0)	--	--
EBITDA - Other	--	--	155.0	155.0	--	155.0	--	--
Total adjustments	5,769.9	710.1	1,786.5	(4.1)	757.9	(611.6)	1,449.4	(159.0)

**S&P Global Ratings adjusted amounts**

	Debt	Equity	EBITDA	EBIT	Interest expense	Funds from operations	Cash flow from operations	Capital expenditures
Adjusted	18,512.9	35,797.1	11,600.5	1,865.9	1,013.9	9,202.4	9,418.4	6,973.0

## Related Criteria And Research

### Related Criteria

- General Criteria: Methodology For Crude Oil And Natural Gas Price Assumptions For Corporates And Sovereigns - November 19, 2013
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For Contract Drilling - April 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Transportation Cyclical Industry - February 12, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Oil And Gas Exploration And Production Industry - December 12, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology - November 19, 2013
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue - April 15, 2008
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers - May 07, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

### Related Research

- Sovereign Risk Indicators - October 13, 2016
- S&P Global Ratings Raises Its Oil Price Assumptions For The Rest Of 2016, And Assigns Oil And Natural Gas Prices For 2019 – September 20, 2016

### Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
<b>Satisfactory</b>	a/a-	bbb+	<b>bbb/bbb-</b>	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

### Ratings Detail (As Of December 8, 2016)

#### A.P. Moller - Maersk A/S

Corporate Credit Rating  
Senior Unsecured

BBB/Negative/--  
BBB

## Ratings Detail (As Of December 8, 2016) (cont.)

### Corporate Credit Ratings History

14-Nov-2016	BBB/Negative/--
05-Jul-2016	BBB+/Watch Neg/--
19-Feb-2016	BBB+/Negative/--
25-Sep-2013	BBB+/Stable/--

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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