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Milwaukee Housing Authority; General Obligation

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Milwaukee Housing Authority; General Obligation

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ICR		
Long Term Rating	A+/Stable	New

Rationale

Standard & Poor's Ratings Services assigned its 'A+' issuer credit rating (ICR) on the Housing Authority of the City of Milwaukee (HACM), Wis. The outlook is stable. The rating is based on HACM's stand-alone credit profile (SACP), which we assess at 'a'. The moderate likelihood of extraordinary government support results in a one-notch upgrade of HACM's SACP to 'A+', pursuant to our government-related entity (GRE) criteria.

The rating reflects our view of HACM's strengths, which include:

- A strong enterprise risk profile, supported by very strong industry risk, strategy and management, and asset quality and performance;
- HACM's strong financial profile, bolstered by extremely strong debt and strong liquidity profiles; and
- The strong essentiality of HACM housing, evidenced by a waiting list of more than 10,000 applicants for HACM-operated housing, including public housing and housing choice vouchers (HCVs);

The aforementioned strengths are offset by our view of these weaknesses:

- Vulnerable financial performance based on declining EBITDA;
- Adequate economic fundamentals and market dependency score, based on low population growth and relatively low-cost housing alternatives in Milwaukee, and
- Uncertainty over the effects of impending reforms and public sector funding levels in the medium term.

HACM comprises 3,100 public housing units, 980 nonsubsidized units, and 972 tax credit units that include 477 public housing units and 6,166 housing choice vouchers.

HACM represents that its strategic plan is geared toward establishing a fiscally sustainable and resilient organization. We understand the authority will maintain a modest debt profile. HACM also seeks to increase diversified revenue sources to support other affordable housing activity.

To maintain the 'A+' rating, however, HACM must balance having a certain level of financial stability against its overall public purpose goals. In our opinion, housing authorities with large portions of their income derived from federal subsidies are exposed to weak margins and a negative change in net assets to equity in any given year. In fiscal 2013, about 68% of HACM's revenues came from federal subsidies. Like all housing authorities, HACM's subsidies are subject to changes in congressional appropriations. Total contributions and grants, including HUD subsidies, capital grants, and other sources, declined significantly in 2013 compared with the previous five years. HACM's overall occupancy has remained around 97% over the past four years.

Profitability ratios, as indicated by EBITDA to revenue, have fluctuated, ranging from 31% in 2012 to 3% in 2013. We

believe this is primarily due to changes in grant revenues.

Outlook

The stable outlook reflects our view of HACM's strong management and strategic plan to maximize its affordable housing role in Milwaukee and its vital essentiality to meet the current and future market demand for low-income housing. We believe the authority will continue to seek ways to increase revenues outside of federal subsidies and seek more financial and operational flexibility within the guidelines of the U.S. Department of Housing and Urban Development (HUD). However, declining federal subsidies, particularly as observed in 2013, could pressure the rating. This outlook is based on HACM's ability to maintain or raise additional leveraged resources, its net working capital, liquidity, and profitability position. Failure to do so could impair its financial strength in the long term and lead to a lowering of the rating.

Comparative Analysis

Table 1 details how HACM compares in key measurements with two international entities (Places for People Group of the United Kingdom and Fastighets AB Forvaltaren of Sweden) and four U.S. public housing authority (PHA) peers (Baltimore, Chicago, Cuyahoga County, and Newark). HACM relies on social housing activity (traditional public housing) less than all the compared authorities except Fastighets AB Forvaltaren. This is a positive sign that shows diversification on the part of the PHA. HACM faces challenges in its market, as the social rent as a percentage of market rent is the highest of all of the U.S. PHAs.

Table 1

Comparative PHA Enterprise And Financial Profiles									
Entity	Enterprise Profile					Financial Profile			
	Economic fundamentals and market dependencies				Asset quality	Financial performance	Debt profile		Liquidity
	Proportion of revenues from social housing activity (%)	Annual population growth (%)	Average social rent as a percentage of market rent in the main region of operation	Average dwelling price as a percentage of national average	Vacancy rates (three-year average; %)	EBITDA / Revenues (%)	Debt/EBITDA (x)	EBITDA/Interest (X)	Liquidity ratio
Places for People Group Ltd.	74.00	0.54	60.70	61.06	2.00	31.73	16.56	1.21	1.86
Fastighets AB Forvaltaren	0.00	2.40	100.00	185.50	1.62	27.94	12.31	2.26	1.30
Chicago Public Housing Authority	90.81	0.40	16.88	116.14	6.60	33.57	1.11	17.22	8.83

Table 1

Comparative PHA Enterprise And Financial Profiles (cont.)									
Newark Public Housing Authority, NJ	85.24	0.33	18.07	109.12	17.33	21.45	0.54	59.45	2.17
Baltimore Housing Authority	87.21	0.20	18.83	73.46	2.77	14.06	1.44	15.52	7.12
Cuyahoga Metropolitan Housing Authority, OH	92.11	(0.80)	16.43	35.09	1.00	14.41	1.91	8.49	3.47
Housing Authority of the City of Milwaukee	61.20	0.25	46.47	80.35	3.00	21.82	9.76	37.72	1.29

Extraordinary Government Support

We view HACM as a new GRE; therefore, we apply our recently published criteria. Under this criteria, as mentioned above, we view HACM as having a "strong" link with the U.S. government, as per government policy, which is reflected by its track record of providing strong credit support for public housing under certain circumstances. We also view HACM as having "limited importance" to the government, since an HACM credit default would have a limited impact on the government. Based on the combined "strong" link and "limited importance", we view the likelihood of extraordinary support that may be available to this GRE when required as moderate, resulting in a one-notch upgrade of the SACP of 'a' to an ICR of 'A+'.

Enterprise Profile

Industry risk: U.S. PHAs' focus on affordable housing lends further stability, with low competitive risk

The U.S. PHA industry risk scores a '2', representing a combination of individual assessments: sub-scores of '2' for cyclical risk and competitive risk, with no adjustment for the government's support toward the industry. Economic cycles are most likely to affect U.S. PHAs vis-à-vis other types of social services because real estate fluctuations can change asset values. Also, real estate markets tend to be overbuilt, leading to depressed occupancy rates, rentals, and property values. Residential rental markets typically pose less risk relative to other property classes, however, and U.S. PHAs' collective focus on affordable housing typically lends further stability. Competitive risk is fairly low due to effective entry barriers in many jurisdictions, minimal substitution risk, and overall stability in growth and margins. In addition, government subsidies, other support, and oversight limit volatility, with the overall importance of the service delivered therein limiting the potential for negative government intervention, in our opinion.

Economic fundamentals and market dependencies: low demand for housing relative to other U.S. cities

HACM is the local housing authority established under Wisconsin law to provide public housing and related services in Milwaukee. The authority receives federal government subsidies, primarily for operations and modernization activities.

HUD is the designated federal oversight entity and is responsible for allocating subsidies for all PHAs. HACM owns 3,100 public housing units; 972 tax credit units, which include 477 public housing units; and 980 nonsubsidized units and administers 6,188 Section 8 or housing choice vouchers.

We view HACM's essentiality to the market it serves as very strong. Like many other U.S. PHAs, market demand for HACM services far exceeds available supply. In 2012 HACM closed its housing wait list for families, which now numbers 8,158, or about 80% of its current household population. In addition, HACM has approximately 1,000 applicants for elderly and disabled housing and 800 applicants for housing choice vouchers. HACM serves low-income residents who often have few housing alternatives despite a relatively affordable housing market and typical affordable housing rental costs. The average dwelling price in the region compared with the national average price is 71%, indicating a below-average housing cost market. HACM's rents for all units, including those that are nonsubsidized, are less than half of the market rent, indicating that the authority offers a significant discount in an affordable city. The discount is not as large as in other U.S. cities, in part to the large number of unsubsidized units. The low discount, 0.7% population growth, and qualitative factors yield an adequate score for economic fundamentals.

Market Position

Strategy and management

HACM meets HUD's strategic planning guidelines, which mandate annual and five-year plans. Beyond that, HACM has delineated a resiliency plan designed to reposition its housing portfolio, increase non-HUD revenue streams, and evaluate existing and future partnerships.

The portfolio repositioning includes public housing and nonsubsidized housing. The nonsubsidized housing element has been addressed, thus far, through the increase of rents as permitted, which has resulted in more rental revenue and permitting the issuance of additional debt while maintaining affordability. In terms of the nonsubsidized housing portfolio, HACM intends to refinance an existing bond issue to generate additional funds through lower interest rates. The refinancing will also fund renovation and improvements to the authority's Berryland, Northlawn, Southlawn, and Southlawn Park housing developments, and will finance construction of market-rate housing.

Recently, HACM raised its rent cap from 80% of comparable rent to 90% of fair market rent. The higher rents increased rental revenue. The authority has reorganized the operation of its public housing portfolio to increase efficiency. HACM has implemented new procedures to shift rehabilitation to capital fund grants from the HUD operating subsidy and has leveraged federal resources to create new mixed-income, mixed-finance communities.

Another strategy is to increase the nonsubsidized housing portfolio. HACM plans to slowly build up new units to replace the lost units using replacement housing factor grants and capital fund grants in connection with future redevelopment activities.

HACM's management, in our view, is very strong. The secretary-executive director, chief financial officer, and assistant secretary have an average tenure with the authority of 13 years. Prior to working at HACM, senior staff gained related experience in either housing, finance, or human services at other entities.

The authority is governed by a seven-member board of commissioners, who are appointed by the Mayor of Milwaukee and confirmed by the city's Common Council. Two of the commissioners are residents. Terms are five years in length and stagger to foster smooth transitions. The board has a range of experience with HACM. Two members have been on the board for at least 15 years, three have served for more than three years, and two have been on the board for less than one year.

The board approves the agency plan and all policies. The policies cover finance, lines of authority, personnel, performance management, and appraisal. The board meets monthly and reviews financial reports quarterly. It approves all purchases and contract of at least \$100,000.

HACM has a cooperation agreement with the City of Milwaukee. The two entities share administrative services, information technology infrastructure, the employment retirement system, and health insurance. Thirty five of HACM's employees are city employees assigned by the city, and the other 177 are at-will HACM employees. HACM also has an intergovernmental cooperation agreement with the Redevelopment Authority of the City of Milwaukee.

Asset quality and operational performance

HACM manages over 4,000 units of low-income housing and administers more than 5,700 rental assistance vouchers. The authority also owns and manages more than 1,000 units of unsubsidized/affordable and market-rate rental housing. The housing portfolio consists of 29 developments, broken into 17 public housing asset management portfolios, nine tax credit developments, and three unsubsidized housing developments. The average age of the developments is 41 years from original construction, with significant renovations averaging 13 years after construction. The units serve family and elderly populations in a variety of settings, including high rise, single family and multifamily.

Following site visits to a sampling of HACM properties, we rank the overall portfolio at '3' on a 1-to-5 scale, ranging from highest to lowest. Physical curb appeal on newly developed and renovated properties is good, in our view, and in most cases better than surrounding neighborhood properties. HACM has a central maintenance operation that provides major unit rehabilitation, general repair, and maintenance of HVAC and building systems, as well as pest control. Onsite maintenance staff handle routine maintenance repairs and general cleaning and site upkeep. A modernization and development department is accountable for building structure, major building rehabilitation, and new construction.

HACM serves as its own developer for its development projects. Through this activity the authority receives developer fees. This development includes planned market rate housing. The authority has other neighborhood initiatives and tax credit proposals that it is either considering or has applied for.

Occupancy has generally been very high in the authority's public housing and tax credit units, with an average of 98% in both types. Three unsubsidized housing developments have a three-year average occupancy of 91% to 97%, but the 2014 occupancy was at least 96% for all three developments.

The per-unit maintenance cost has remained stable since 2009, with a slight decrease of about \$200 to \$3,640 in 2013.

Financial Profile

HACM's recent financial performance has been volatile, in our opinion, however the fluctuations have been mitigated by strong debt and liquidity profiles. The resulting financial profile designation is strong. Standard & Poor's analyzes PHAs with their component units if any exist. One key metric, EBITDA, declined significantly in 2013 to \$2.7 million from \$34.6 million in 2012. The main contributor was a lower capital grant drawdowns of \$4.5 million in 2013 compared with \$22.1 million in 2012. The high level of capital grants drawdowns in 2010 to 2012 was related to the stimulus grants. The capital grant funding will not return to prior levels as the authority converted many units to nonpublic housing, making them ineligible for capital grants. At the same time, the reduction in units lowers costs associated with housing.

Financial performance: weakened profitability, mainly due to lower HUD contributions

HACM's financial performance had been fairly stable from 2008 to 2012 before trending down in 2013. Net operating income had been positive in every year but one between 2008 and 2012, with the loss being about \$2 million. In 2013, the net operating loss was nearly \$15 million, driven by the lower capital fund receipt.

The loss of grants drove the EBITDA to revenues ratio down to 3%, extremely low among PHAs. However, the three-year average of 20% is high among the group. PHAs typically have low EBITDA-to-revenues ratios, so a strong standing within this category relative to other housing authorities is not an indication of a strong mark.

Strong debt profile among the majority of HACM's global and U.S. peers

HACM achieves an extremely strong debt profile. One reason for HACM's strong ratios, in our view, is its debt management practices. The authority had \$71.6 million in outstanding debt in fiscal 2013, slightly higher than in 2012, but much more debt than the \$17.2 million in 2011. The majority of this increase, however, is due to loans that appear as debt in the audited financials but are actually paid by equity investments in Low Income Housing Tax Credit projects. Its debt-to-EBITDA ratio (average of the past three years actual) is 9.8x, which is high compared with its domestic peers. However, given HACM's lack of an obligation to pay the debt that is ultimately paid by equity investors, the authority's EBITDA-to-interest ratio (average of the past three years actual) is a very high 37.74x, representing an extremely strong debt profile on a global scale, leading to a final score of '1'.

Financial policies: positive credit impact, with focus on operations

HACM's financial policies are well-established, in our view, and provide oversight and prudence that we deem consistent with an investment-grade rating. The authority has detailed policies that related to budgeting, audits, investments, and financial statements. We believe HACM's financial management benefits from current planning and budgeting practices while implementation of its financial plan is enhanced through an extensive financial reporting system and a written financial policy and procedure manual.

The authority uses three software components for financial reporting, budgeting, and public housing and housing choice voucher management. The systems serve different purposes and enable the authority to track expenses and payment delinquency.

HACM prepares monthly financial statements on public housing, nonsubsidized housing and housing choice vouchers

while the component units provide independent financial information to the authority. The authority has the ability to track performance of properties, which provides metrics for employee assessment. The authority anticipates it will integrate the data into employee performance measurement in 2015.

Liquidity: Strong position

We expect HACM to have \$39.6 million in liquidity sources in two years. These sources include cash from operations, cash and equivalents, and current investments. Meanwhile, we expect liquidity uses, including debt service less noncash working capital (if negative), to be around \$30.8 million. Historically, HACM has paid such obligations in a timely manner. Given the current liquidity sources and cash flow operations, we expect the organization might achieve a 1.29x liquidity ratio over the next two years. We base this view on HACM's two-year debt service schedule and projected liquidity sources, which correlates to a strong position even without a strong external liquidity adjustment.

Economy

We consider Milwaukee's economy to be weak with estimated market value per capita at \$44,380 and projected per capita effective buying income for 2017 at 68% of the nation's level. Milwaukee is Wisconsin's largest city and is the center of southeastern Wisconsin's diverse economy. According to the 2010 U.S. Census, the city's population stabilized at 594,833 in 2010, after falling 17% from 1970 to 2000. The city estimates that its current population is 595,425. The economy is based on services and manufacturing, with downtown Milwaukee serving as an employment center for surrounding suburban counties.

Due to a still-recovering real estate market, Milwaukee's assessed valuation (AV) decreased 18% from 2008 to 2013. The estimated market value of the property tax base, in terms of equalized valuation as determined by the state, fell 19% from 2008 to 2013, to \$26.09 billion, which we consider adequate at about \$44,380 per capita. We consider the tax base very diverse, with the 10 leading taxpayers accounting for just 4% of AV. We view the city's median household effective buying income as adequate at 75% of the state's and 73% of the nation's levels. Milwaukee's unemployment rate has historically been above average and was 10.1% in 2012, substantially higher than the state's 6.9% and the nation's 8.1%.

Table 2

Housing Authority of the City of Milwaukee Liquidity			
	2013	2014	2015
Sources of liquidity			
Forecasted cash generated from continuing operations if positive (\$)		464,000	1,476,400
Cash and liquid investments (\$)	34,450,867	34,450,867	34,450,867
Undrawn committed facilities that mature after 12 months and can be drawn (\$)		4,800,000	2,800,000
Expected ongoing cash injection from a component unit (\$)	427,634	922,200	922,200
Other receipts if applicable (\$)		11,307,000	
Total sources of liquidity	34,878,501	51,944,067	39,649,467
Uses of liquidity			
Forecasted cash generated from continuing operations, if negative (\$)	10,708,368	10,708,368	10,708,368
Forecasted working capital excluding cash outflows, if negative (\$)		-	9,569,553

Table 2

Housing Authority of the City of Milwaukee Liquidity (cont.)			
Expected capital expenditure over the next 12 months (\$)		5,700,000	5,800,000
Interest and principal payments due on debt over the next 12 months (\$)	1,517,878	1,074,141	1,967,234
Other payments, if applicable (\$)		4,800,000	2,800,000
Total uses of liquidity	12,226,246	22,282,509	30,845,155
Liquidity ratio	2.85	2.33	1.29

Table 3

Housing Authority of the City of Milwaukee Financials			
(In \$ unless otherwise indicated)			
	2011	2012	2013
Balance sheet			
Assets			
Current assets			
Total current assets	36,197,262	45,981,736	37,411,529
Long-term assets			
Total long-term assets	296,799,157	370,968,775	365,887,466
Total Assets	332,996,419	416,950,511	403,298,995
Average total assets	494,654,149	536,631,195	529,805,437
Liabilities			
Current liabilities			
Total current liabilities	49,839,905	78,822,799	87,205,252
Long-term liabilities			
Total Long-term liabilities	48,255,649	83,689,620	78,756,705
Total liabilities	98,095,554	162,512,419	165,961,957
Net assets / Equity			
Unrestricted net assets	83,139,128	93,774,517	91,821,703
Accumulated deficit	(4,410,217)	(23,886,437)	(17,600,173)
Temporarily restricted	-	-	-
Permanently restricted	41,051,099	74,115,364	58,209,343
Other	115,120,855	110,434,648	104,906,165
Total net assets / equity	234,900,865	254,438,092	237,337,038
Average equity	275,966,644	285,735,258	277,184,731
Total liabilities and net assets / Equity	332,996,419	416,950,511	403,298,995
Income statement			
Revenue			
Rental income	19,703,380	20,859,658	23,515,933
Total contributions and grants	79,603,157	78,282,382	54,154,640
HUD operating subsidies	54,600,766	53,235,192	48,651,066
HUD capital grants	22,683,902	22,125,255	4,519,647
Other grants and HAP	2,318,489	2,921,935	983,927

Table 3

Housing Authority of the City of Milwaukee Financials (cont.)			
State grants	-	-	-
Developer fees	2,219,914	9,510,238	-
Other income	2,594,193	2,428,376	2,478,823
Total revenues	104,120,644	111,080,654	80,149,396
Expenses			
Operations and maintenance	19,016,289	18,427,596	18,317,912
HAP	35,192,849	36,087,098	36,287,376
Real estate taxes	-	-	-
Depreciation/Amortization	10,576,400	12,088,802	13,426,561
General and administrative	21,644,600	22,408,397	23,457,254
Other expenses	3,486,674	2,472,009	3,654,052
Total operating expenses	89,916,812	91,483,902	95,143,155
Total net operating income	14,203,832	19,596,752	(14,993,759)
Adjustments to net operating income			
Gain (loss) on sale of assets	1,875,955	1,005,261	95,629
Tax expense	-	-	-
Interest and investment income	1,646,099	1,923,854	2,275,119
Capital contributed/capital grants	-	-	-
Interest expense	2,344,694	2,962,364	4,246,417
Other expenses	84,452	26,276	231,626
Other income	-	-	-
Change in net assets / Equity (net income)	15,296,740	19,537,227	(17,101,054)
Net assets / Equity at beginning of the year	219,604,125	234,900,865	254,438,092
Prior-period adjustments	-	-	-
Equity transfers of component units	-	-	-
Cumulative effect of change in accounting principle	-	-	-
Net assets / Equity, end of the year	234,900,865	254,438,092	237,337,038
Cash flow statement			
Operating activities			
Change in net assets / equity	15,296,740	19,537,227	(17,101,054)
Depreciation and amortization	10,576,400	12,088,802	13,426,561
Other adjustments from operating activities	63,060,915	(17,479,903)	(7,033,875)
Net cash provided by operating activities	88,934,055	14,146,126	(10,708,368)
Investing activities			
Purchase of depreciable assets	(37,149,323)	(49,020,418)	(5,337,908)
Interest received	781,142	436,601	382,900
Net cash provided by investing activities	(36,368,181)	(48,583,817)	(4,955,008)
Financing activities			
Interest paid	(632,685)	(536,658)	(462,707)
Payments of long-term debt	(630,250)	(659,790)	(702,076)

Table 3

Housing Authority of the City of Milwaukee Financials (cont.)			
Proceeds from sale of bonds/notes	146,318	122,857	95,162
Other adjustments from financing activities	34,828,924	67,147,175	3,539,567
Net cash provided by financing activities	33,712,307	66,073,584	2,469,946
Net increase (decrease) in cash equivalents	86,278,181	31,635,893	(13,193,430)
	Key measurements		
EBITDA	27,124,926	34,647,918	2,679,219
Debt	17,154,468	66,331,246	71,605,258
Debt service	1,262,935	1,196,448	1,164,783
Government support (%)	76.45	70.47	67.57
Voids, vacancy (% of revenues)	3.00	3.00	3.00
Arrears (% of revenues)	1.00	1.00	1.00
Annual market rent in the main region of operation	10,594	10,056	10,056
Average social rent as a percentage of market rent in the main region of operation	36.96	41.22	46.47
Average market dwelling price (\$)	235,448	228,840	228,840
Average national dwelling price	292,200	292,200	292,200
Average dwelling price as % of national average	80.58	78.32	78.32
EBITDA / Revenues (%)	26.05	31.19	3.34
Debt / EBITDA (x)	0.63	1.91	26.73
EBITDA interest coverage (x)	42.87	64.56	5.79
Funds from operations	89,082,512	14,046,069	(10,788,175)
Cash from operation	88,934,055	14,146,126	(10,708,368)
Cash and liquidity	35,214,151	45,017,310	37,134,005
Net working capital	(13,642,643)	(32,841,063)	(49,793,723)
Working capital excluding cash	(38,918,427)	(38,313,335)	(22,785,503)
Population growth (%)	0.70	0.7	0.7

HAP--Housing assistance payments. HUD--U.S. Department of Housing & Urban Development.

Related Criteria And Research

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- USPF Criteria: Investment Guidelines, June 25, 2007
- Criteria: Public And Nonprofit Social Housing Providers, July 11, 2012
- General Criteria: Methodology: Industry Risk, Nov. 20, 2013
- Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

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