S&P Global
Ratings

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Siemens AG

Primary Credit Analyst:
Tuomas E Ekholm, CFA, Frankfurt (49) 69-33-999-123; tuomas.ekholm@spglobal.com

Secondary Contact:
Tobias Buechler, CFA, Frankfurt +49 69-33 999-136; tobias.buechler@spglobal.com

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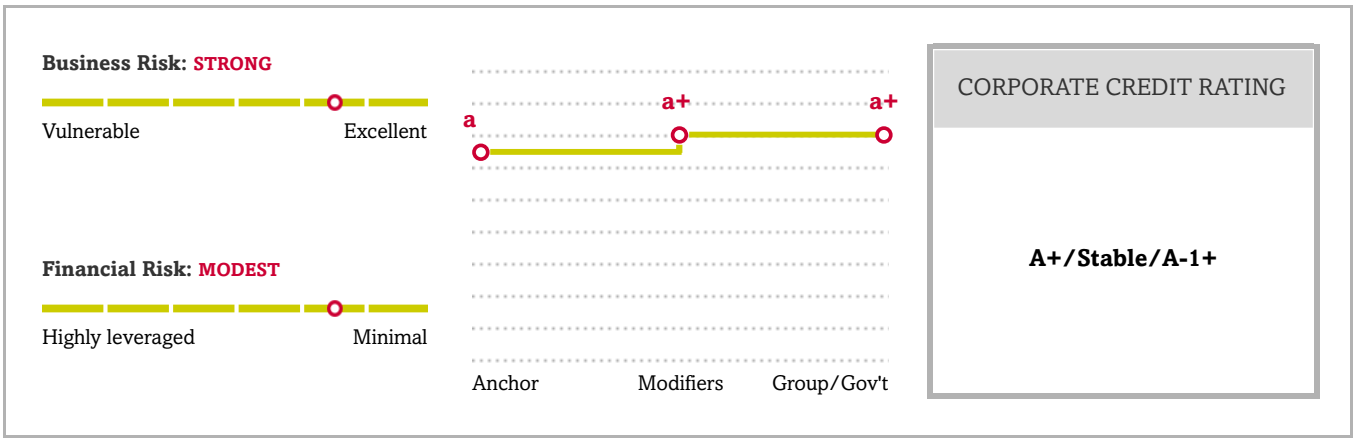

Rationale

Business Risk: Strong	Financial Risk: Modest
• Leading market positions in all business divisions, and a highly diverse global industrial portfolio, including activities unrelated to the industrial investment cycle such as healthcare. • Strong technological capabilities across all covered product segments, high entry barriers, and an ability to reorient portfolio toward areas of growth. • Continuous margin improvement owing to group-wide cost-saving initiatives and strategic focus on expanding advanced technology segments and services, in particular digitalization and industrial software. • Political risk in different regions across the world and overcapacity in energy- and commodities-related end markets, hampering growth and putting pressure on operating margins, making it necessary to rightsize operations in related divisions.	• Strong credit metrics as a result of steadily improving operating and financial performance and strong cash generation, and despite significant acquisition-related cash spending in 2017. • Conservative financial policy, including a cap on industrial net debt to EBITDA of 1x. • Abundant liquidity, with sound discretionary cash flow generation through the cycle providing a high degree of financial flexibility. • Significant steady cash outflow through shareholder distributions via dividends and share buybacks, as well as acquisitions.

Outlook: Stable

S&P Global Ratings' stable outlook on Germany-based manufacturing and technology group Siemens AG, reflects our base-case expectation that the group's operating and financial performance will remain steady, despite the need to reduce overcapacity in operations related to energy and commodity markets. In our view, the group will be able to offset these weaknesses through improved growth and margins in its advanced automation, software, and healthcare activities, and related digital services. This should enable the group to maintain an S&P Global Ratings-adjusted ratio of funds from operations (FFO) to debt at the higher end of the 45%-60% range in the next several years, even in the case of larger acquisitions. We consider this in line with the current ratings.

We expect that Siemens will have adequate financial means to absorb the impact of modest global economic growth and continuously low investment in energy and commodities-driven end markets, while continuing to match shareholder distributions and acquisitions to cash generation. Furthermore, the proceeds from the announced partial listing of its healthcare division should provide Siemens with additional financial flexibility to execute growth and investment.

Downside scenario

Siemens currently has significant headroom in terms of key credit metrics at the current rating level. Nevertheless, we would consider taking a negative rating action if Siemens pursued a more aggressive financial policy than we anticipate. This could result from sizable cash- and debt-financed acquisitions, with no offsetting asset disposals, leading to credit ratios no longer in line with the current rating, in particular FFO to debt at the lower end of the 45%-60% range.

A negative rating action could also stem from a higher shareholder payout ratio than the 40%-60% of net income we assume in our base case, and the current €3 billion share buyback program we expect Siemens will complete and extend. Moreover, we could also lower the rating if Siemens' operating performance, margins, or portfolio diversification were to worsen significantly. This could occur as a result of, in particular, the group giving up control of its healthcare division, which, with strong margins and steady cash flow, is the most stable of its operating divisions.

Upside scenario

Upside rating potential could develop if we thought that Siemens could consistently achieve debt-protection measures commensurate with a minimal financial risk profile, including FFO to debt well above 60%. This would likely involve a more conservative financial policy than the group's current targets, refraining from cash- or debt-funded acquisitions, and a change in shareholder remuneration, therefore boosting key credit metrics on a permanent basis. However, we do not currently believe this to be the case, and expect the group to follow its leverage guidance of industrial net debt to EBITDA of 1x in the long term.

Our Base-Case Scenario

In 2017, the capital goods sector experienced an increase in broad-based demand for equipment and services across

the most important end markets. Siemens was able to expand its revenues modestly by 4.3% to €83 billion, which was a stronger growth rate than that of its global peers, and its adjusted EBITDA by 11% to €11.9 billion, with EBITDA margins widening from 13.6% to 14.5%. Siemens' recent performance underlines the stability of its business and the group's ability to execute its strategy, aimed at developing a portfolio of operating businesses with improved growth and margins.

The 2017 acquisition of Mentor Graphics for $4.5 billion, as well as the earlier acquisition of industrial software supplier, CD-adapco, demonstrates Siemens' strategic direction. In our view, this has strengthened Siemens' business profile by complementing its digitalized products and solutions portfolio, accelerating growth, and generating synergies. We view Siemens' announcement that its mobility division will merge with its French competitor Alstom S.A. (not rated), as supportive for the rail equipment and automation business. The merger will create a leading global rail equipment and systems manufacturer with annual sales of about €15 billion, and adjusted EBIT of about €1.2 billion on a pro forma basis. The merger will also strengthen the position of Siemens and Alstom in competition against other rail equipment manufacturers in global markets, in particular the larger Chinese state-backed rail equipment group, CRRC Corp. Ltd.

We expect the market environment for Siemens in 2018 to remain mixed, as slower than expected recovery in the commodity markets and continued weakness in the energy markets are likely to continue to offset the strength in the non-commodity end-markets, such as automotive, construction, general industrial, and healthcare. Therefore, in 2018 we expect Siemens will continue to show only modest revenue growth, and face permanently reduced demand in the power generation and commodities markets, with planned related capacity reductions in related divisions likely resulting in stagnating or even moderately decreasing operating margins. This is despite expected strong performance of, in particular, industrial automation and healthcare segments. In November 2017, Siemens announced plans to react to structural changes in the fossil power generation market and the commodity sector, with a restructuring plan for its Power and Gas, and Process Industries and Drives Divisions. The plan aims to increase capacity utilization and efficiency, including a reduction in headcount of 6,900. As a result of Siemens' cost saving initiatives and growth in higher margin segments, we expect the group's operating margins to widen again in 2019.

Assumptions

- Higher capital expenditure (capex), particularly on new equipment over the next two years in the sector. This is as a result of continuous positive trends across several important end markets, such as automotive construction, and despite slower than expected recovery in the commodity markets and continued weakness in related energy markets.
- Broadly improving GDP growth in the eurozone of 2.0% in 2018 and 1.7% in 2019 as recovery continues, and of about 2.5% in 2018 and 1.9% in 2019 in North America. In Siemens' other key operating region, Asia-Pacific, we forecast GDP growth of 5.4% in 2018, and 5.6% in 2019.
- Low-single-digit revenue growth resulting from strong short-cycle business and digitalization, and accretive acquisitions.
- EBITDA margins on an adjusted basis to stagnate at about 14% in 2018, following Siemens' restructuring in power and large drives businesses. Cost-saving initiatives, strong expansion in the digital solutions business, and growth in healthcare, continue to support margins, leading to margin expansion again from 2019.
- Research and development expenses of 6% of revenues and capex of 3% of revenues, as Siemens intends to further develop and expand its digital services and healthcare businesses.
- Initial public offering of a 1%-20% minority stake in Siemens Healthineers during the first half of 2018, with significant cash proceeds going to the group.
- Annual capex of about €2.5 billion.
- A dividend payout ratio of 40%-60% of net income according to Siemens' financial policy.
- Modest mergers and acquisitions-related cash spending not exceeding €2 billion annually over the next two years. We expect the group will adjust future acquisition-related spending to its annual cash generation and its leverage targets.
- Continuation of the share buyback program with a volume of about €1 billion per annum.
- No changes in financial policy.

Key Metrics

	2017a	2018e	2019e
Adjusted EBITDA margin (%)	14.5	14.0	14.0-14.5
FFO/debt (%)	74.4	80.0-85.0	85.0-90.0
Debt/EBITDA (x)	1.0	0.9-1.0	08-0.9

Note: All figures are fully S&P Global Ratings-adjusted. a--Actual. e--Estimate.

Company Description

Headquartered in Munich, Siemens is a leading global technology and engineering group, with a diverse portfolio ranging from power plant construction and wind turbines to rail vehicles and medical technology. The group is a leading global provider of digitalized solutions, including diagnostics, simulation services, and industrial software across all product segments. The group is present in almost all countries worldwide, and had about 372,000 employees on Sept. 30, 2017.

Siemens' businesses are bundled into the following divisions: Power and Gas; Energy Management; Building Technologies; Mobility; Digital Factory; and Process Industries and Drives; as well as the Strategic Units—Healthineers and Siemens Gamesa Renewable Energy, which together form the Industrial Business. Financial services are offered through Siemens Financial Services.

During the fiscal year ended Sept. 30, 2017, Siemens AG generated €83 billion of sales and €8.3 billion of operating income before taxes. Sales were split between segments and geographies (see table 1).

Table 1

Siemens AG--Revenue

(%)	Fiscal year ended Sept. 30, 2017
Division	
Power and Gas	18.10
Energy Management	14.40
Building Technologies	7.70
Mobility	9.50
Digital Factory	13.30
Process Industries and Drives	10.40
Healthineers	16.20
Siemens Gamesa Renewable Energy	9.30
Financial Services (SFS)	1.10
Total	100.00
Region	
Europe, C.I.S., Africa, Middle East (Excluding Germany)	33.10
Americas (Excluding U.S.)	5.60
Asia, Australia	15.80
Germany	23.90
U.S.	21.60
Total	100.00

Business Risk: Strong

Siemens is exposed to a wide variety of industries and their related risks, primarily within the traditional capital goods area. We consider that the group's less cyclical divisions, such as Digital Factory and Building Technologies, have

lower risk, while we view Power and Gas, Process Industries and Drives as more volatile. In our view, the Energy Management, Siemens Gamesa Renewable Energy, and Mobility divisions, have long operating cycles and higher industry risk. The group has decided to operate its lowest risk division, healthcare, as a separate listed entity, but it will hold a majority stake after listing. We expect the listing to take place during the first half of 2018.

Our view of Siemens' business risk profile is supported by the group's strong industry, geographic, and customer diversification, leading market positions as a systems provider rather than as a component supplier, and supportive long-term demand characteristics in most of its business lines. Siemens typically holds a top-three global position and is often the leading player in the markets it competes in. We expect that the group will continue to focus on higher-margin businesses and digitalization, as demonstrated by its latest notable acquisitions, Mentor Graphics for example, and continue to restructure or divest its noncore low-performing businesses, as well as adjust capacity in its core traditional industrial segment to match current market needs.

Siemens' performance, with the exception of Healthineers, is linked to GDP growth and the investment cycle, but we see a positive long-term demand pattern for Siemens' products and solutions. Generally, Siemens' process know-how and technological capabilities provide the group with a strong competitive advantage, and should underpin performance the longer term. In our view, these strengths are reduced by Siemens' exposure to late- and long-cyclical markets, and average profitability relative to wider capital goods industry. However, we expect the growing share of services, including digital solutions and software, will result in less volatility in earnings and improved margins in the medium term. We also expect Siemens will continue to address its controllable cost base with targeted productivity improvement of 3%-5% of aggregate functional costs annually.

Peer comparison

Table 2

Siemens AG--Peer Comparison

Industry Sector: Capital Goods/Diversified

	Siemens AG	**General Electric Co.**	**ABB Ltd.**	**Schneider Electric S.E.**
Rating as of March 5, 2018	A+/Stable/A-1+	A/Stable/A-1	A/Stable/A-1	A-/Stable/A-2
	--Fiscal year ended Sep. 30, 2017--	**--Fiscal year ended Dec. 31, 2017--**		
(Mil. €)				
Revenues	82,275.0	100,970.2	28,572.6	24,743.0
EBITDA	11,994.5	17,028.1	3,956.9	3,924.5
Funds from operations (FFO)	9,298.6	(1,821.6)	2,908.5	3,174.7
Net income from cont. oper.	5,993.0	(4,555.9)	1,847.8	2,244.0
Cash flow from operations	5,863.6	9,954.0	3,508.9	3,185.7
Capital expenditures	2,003.0	6,560.2	790.3	749.0
Free operating cash flow	3,860.6	3,393.8	2,718.6	2,436.7
Discretionary cash flow	759.6	(3,809.4)	1,251.4	1,303.7
Cash and short-term investments	9,617.0	15,164.8	4,686.6	3,077.0
Debt	12,453.8	99,518.7	5,039.9	4,854.3
Equity	41,919.0	71,102.7	12,781.6	19,942.0

Table 2

Siemens AG--Peer Comparison (cont.)				
Adjusted ratios				
EBITDA margin (%)	14.6	16.8	13.8	15.9
Return on capital (%)	15.3	7.1	15.4	11.3
EBITDA interest coverage (x)	11.2	0.9	13.1	14.5
FFO cash interest coverage (X)	10.4	3.9	18.7	N.M.
Debt/EBITDA (x)	1.0	5.9	1.3	1.2
FFO/debt (%)	74.7	(1.9)	57.4	65.4
Cash flow from operations/debt (%)	47.1	9.9	69.3	65.6
Free operating cash flow/debt (%)	31.0	3.4	53.6	50.2
Discretionary cash flow/debt (%)	6.1	(3.9)	24.5	26.9

N.M. - Not meaningful.

Financial Risk: Modest

We base our assessment of Siemens' financial risk profile as modest due to the group's strong balance sheet, exceptional liquidity, strong discretionary cash flow generation through the cycle, and financial flexibility. At fiscal year ended Sept. 30, 2017, Siemens' adjusted debt was about €12.5 billion, €1 billion less than the previous year. This decrease was largely due to a decreased pension deficit following the high discount rate assumptions as compared to 2016. Additionally, adjusted FFO to debt was about 74.4%, and adjusted debt to EBITDA was 1.0x. In our adjusted debt calculation, we exclude €22.5 billion of debt at the group's captive finance operations, and deduct €7.2 billion of surplus cash. We view the captive finance operations as neutral to Siemens' credit profile.

We anticipate that Siemens will maintain credit ratios that compare favorably with our expectations for the rating, including adjusted FFO to debt at the upper end of the 45%-60% range or higher; debt to EBITDA below 1.5x; and significantly positive free operating cash flow. Siemens currently has significant headroom under its key credit ratios relevant to the rating, and we expect proceeds from the announced listing of a minority share of Siemens Healthineers will add to the financial flexibility of the group.

We continue to view Siemens' financial policy as conservative, reflecting the group's commitment to a strategy focusing on low leverage, including its publicly communicated leverage target of 1x industrial net debt to EBITDA , long-term funding, access to undrawn committed bank facilities, and ample liquid funds. We expect Siemens to continue to follow its leverage guidance in the long term, and to allocate its capital according to group principles of investment and shareholder remuneration.

Financial summary

Table 3

Siemens AG--Financial Summary

Industry Sector: Capital Goods/Diversified

	--Fiscal year ended Sep. 30--				
	2017	**2016**	**2015**	**2014**	**2013**
(Mil. €)					
Revenues	82,275.0	78,820.0	74,781.0	71,174.0	72,484.0
EBITDA	11,964.5	10,746.5	9,100.0	9,628.0	8,777.5
Funds from operations (FFO)	9,259.5	8,136.7	6,494.7	7,908.4	6,983.3
Net income from continuing operations	5,993.0	5,262.0	5,251.0	5,266.0	4,053.0
Cash flow from operations	5,863.6	6,450.6	5,669.4	6,353.9	6,101.0
Capital expenditures	2,003.0	1,793.0	1,543.0	1,488.0	1,474.0
Free operating cash flow	3,860.6	4,657.6	4,126.4	4,865.9	4,627.0
Discretionary cash flow	759.6	1,594.6	1,198.4	2,152.9	1,892.0
Cash and short-term investments	9,617.0	11,897.0	11,132.0	8,938.0	9,791.0
Debt	12,453.8	13,341.8	9,601.0	5,375.7	6,567.1
Equity	41,919.0	32,193.0	33,633.5	29,543.4	27,225.5
Adjusted ratios					
EBITDA margin (%)	14.5	13.6	12.2	13.5	12.1
Return on capital (%)	15.3	16.0	17.3	19.6	16.0
EBITDA interest coverage (x)	10.7	9.4	9.8	108.6	38.6
FFO cash int. cov. (x)	10.4	11.5	13.7	14.2	17.0
Debt/EBITDA (x)	1.0	1.2	1.1	0.6	0.7
FFO/debt (%)	74.4	61.0	67.6	147.1	106.3
Cash flow from operations/debt (%)	47.1	48.3	59.1	118.2	92.9
Free operating cash flow/debt (%)	31.0	34.9	43.0	90.5	70.5
Discretionary cash flow/debt (%)	6.1	12.0	12.5	40.0	28.8

Liquidity: Exceptional

The short-term rating is 'A-1+', derived from our financial risk profile and liquidity assessments. We regard Siemens' liquidity as exceptional, with an expectation that liquidity sources will continuously exceed uses by at 2x over the next 24 months. We further view Siemens' bank relationships as well established, its credit market standing as high, and its financial risk management as very prudent.

Principal Liquidity Sources	Principal Liquidity Uses
• Reported cash and cash equivalents of about €10 billion on Dec. 31, 2017; • A total of €7.0 billion of committed revolving credit facilities (RCFs), including an RCF maturing in 2020, all of which are currently undrawn; and • FFO in the range of €9.0 billion-€9.5 billion per year.	• Long- and short-term debt maturities of about €5.4 billion in 2018, and about €2.1 billion in 2019; • Annual capex in the range of €2.5 billion to €3.0 billion; • Our assumption of discretionary dividend payments within the group's targeted payout range of 40%-60% of net income; and • Discretionary share buybacks of about €1 billion annually.

Debt maturities

Long-term bond maturities:

- 2018: Approximately €5.4 billion
- 2019: Approximately €2.1 billion
- 2020: Approximately €3.4 billion
- 2021 and beyond: Approximately €21.1billion

Other Credit Considerations

Our analysis includes a one-notch uplift from the anchor of 'a', based on Siemens' moderate diversification, reflecting the broad reach of the group's moderately correlated products and end markets. In particular, we view the contribution of the healthcare segment as positive for the group's credit profile. We believe that this segment will continue to benefit the group in terms of diversification, despite the recently announced partial listing of the entity.

Ratings Score Snapshot

Corporate Credit Rating

A+/Stable/A-1+

Business risk: Strong

- **Country risk:** Intermediate
- **Industry risk:** Intermediate
- **Competitive position:** Strong

Financial risk: Modest

Anchor: a

Modifiers

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

Issue Ratings

Capital structure

Siemens' outstanding debt consists largely of senior unsecured obligations issued by a number of the group's financing entities.

Analytical conclusions

We consider that issuers such as Siemens, which have a financial risk profile assessment of modest, have leverage that is low enough to limit the possibility of any lenders being more significantly disadvantaged than others. Therefore, we rate the senior unsecured long-term debt issued by such issuers at the same level as our corporate credit rating on the issuer.

Reconciliation

Table 4

Siemens AG--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Sep. 30, 2017--								
Siemens AG reported amounts									
	Debt	**Shareholders' equity**	**Revenues**	**EBITDA**	**Operating income**	**Interest expense**	**EBITDA**	**Cash flow from operations**	**Capital expenditures**
Reported	32,224.0	43,088.0	83,049.0	10,902.0	7,691.0	1,051.0	10,902.0	7,225.0	2,406.0
S&P Global Ratings' adjustments									
Interest expense (reported)	--	--	--	--	--	--	(1,051.0)	--	--
Interest income (reported)	--	--	--	--	--	--	1,487.0	--	--
Current tax expense (reported)	--	--	--	--	--	--	(2,042.0)	--	--
Operating leases	2,646.5	--	--	853.5	188.0	188.0	665.5	665.5	--
Postretirement benefit obligations/deferred compensation	6,350.1	--	--	(112.0)	(112.0)	193.0	(359.9)	122.1	--

Table 4

Siemens AG--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €) (cont.)									
Surplus cash	(7,212.8)	--	--	--	--	--	--	--	--
Capitalized development costs	--	--	--	(374.0)	(171.0)	--	(374.0)	(374.0)	(374.0)
Share-based compensation expense	--	--	--	512.0	--	--	512.0	--	--
Dividends received from equity investments	--	--	--	381.0	--	--	381.0	--	--
Captive finance operations	(22,531.0)	(2,607.0)	(774.0)	(274.0)	(1,367.0)	(340.7)	(915.1)	(763.0)	(29.0)
Asset retirement obligations	759.0	--	--	--	--	22.0	(22.0)	(12.0)	--
Nonoperating income (expense)	--	--	--	--	1,530.0	--	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	--	--	--	(1,000.0)	--
Non-controlling Interest/minority interest	--	1,438.0	--	--	--	--	--	--	--
Debt - Guarantees	639.0	--	--	--	--	--	--	--	--
Debt - Other	(421.0)	--	--	--	--	--	--	--	--
EBITDA - Gain/(loss) on disposals of PP&E	--	--	--	419.0	419.0	--	419.0	--	--
EBITDA - Business Divestments	--	--	--	(343.0)	(343.0)	--	(343.0)	--	--
Total adjustments	(19,770.2)	(1,169.0)	(774.0)	1,062.5	144.0	62.3	(1,642.5)	(1,361.4)	(403.0)

S&P Global Ratings' adjusted amounts

	Debt	Equity	Revenues	EBITDA	EBIT	Interest expense	Funds from operations	Cash flow from operations	Capital expenditures
Adjusted	12,453.8	41,919.0	82,275.0	11,964.5	7,835.0	1,113.3	9,259.5	5,863.6	2,003.0

Related Criteria

- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, Sept. 21, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria - Corporates - General: Methodology: The Impact Of Captive Finance Operations On Nonfinancial Corporate Issuers, Dec. 14, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013

- Criteria - Corporates - Industrials: Key Credit Factors For The Capital Goods Industry, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- Criteria - Corporates - Industrials: Key Credit Factors For The Health Care Equipment Industry, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

	Financial Risk Profile					
Business 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
Satisfactory	a/a-	bbb+	bbb/bbb-	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 March 6, 2018)

Siemens AG		
Corporate Credit Rating		A+/Stable/A-1+
Corporate Credit Ratings History		
14-Nov-2012	*Foreign Currency*	A+/Stable/A-1+
18-Apr-2011		A+/Positive/A-1+
05-Jun-2009		A+/Stable/A-1
14-Nov-2012	*Local Currency*	A+/Stable/A-1+
18-Apr-2011		A+/Positive/A-1+
05-Jun-2009		A+/Stable/A-1
Related Entities		
RISICOM Rueckversicherung AG		
Financial Strength Rating		
Local Currency		A+/Stable/--
Issuer Credit Rating		
Local Currency		A+/Stable/--
Siemens Financial Services GmbH		
Issuer Credit Rating		A+/Stable/A-1+

*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.

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@spglobal.com