

Swedbank AB

Key Rating Drivers

AML Controls Drive Ratings: The key rating driver in Swedbank AB's risk appetite is the material shortcomings in anti-money laundering (AML) risk controls identified by Swedish and Estonian regulators. The ratings also reflect Swedbank's low risk retail banking business profile, strong asset quality, profitability and capitalisation. The bank's franchise and the confidence of covered bond investors have been largely unaffected by the negative publicity.

AML Investigations, Manageable Fine: In March 2020, the investigations by the Swedish and the Estonian regulators confirmed deficiencies in the bank's AML controls. The Swedish regulator fined Swedbank SEK4 billion (about a quarter of its 2019 net profit).

Asset Quality to Deteriorate: The economic fallout from the coronavirus outbreak will have a moderate impact on Swedbank's asset quality as the bank has limited direct exposure to industries most vulnerable to the current crisis. However, its loan book is geographically concentrated in Sweden, strongly linked to the performance of the Swedish economy, and sensitive to raising unemployment.

Profitability Headwinds to Intensify: We expect reduced business volumes and rising loan impairment charges. Swedbank's wide net interest rate margin has sufficient space to absorb an upswing in wholesale funding costs and its operating cost efficiency should remain solid, despite costs related to the strengthening of its AML controls.

Capitalisation May Weaken: Solid capitalisation is key in light of the bank's wholesale funding reliance and the need to maintain investor confidence. Following the reduction of the Swedish countercyclical buffer to zero, Swedbank's surplus common equity Tier 1 (CET1) capital above regulatory minimum equalled about 1.3% of gross loans at end-March 2020 (1.9% if the 2019 dividend is cancelled).

Solid Funding Profile: Swedbank relies significantly on covered bonds and this funding source has been reliable due to a strong captive domestic investor base. The bank's ample liquidity (also underpinned by available central bank's funding facilities) sufficiently covers its short-term refinancing needs. It is also sufficient to service even intensified drawdowns of committed credit facilities by corporate customers.

Rating Sensitivities

Stable Outlook: We expect the bank will progressively strengthen its controls to effectively combat and prevent money laundering and that these remedies will become structurally embedded in its corporate governance structure. In addition, Swedbank entered the economic downturn from the coronavirus outbreak from a relative position of strength at its rating level, given its strong financial metrics.

Strengthening of AML Controls: An upgrade would require evidence that the bank has fully addressed its shortcomings in AML controls in the Baltics; durable improvement in its risk-control framework clearly embedded in the bank's risk culture and board oversight; an increased certainty that further potential fines (particularly in the US) would not weaken its capital materially; and a clear resilience to economic fallout from the coronavirus outbreak.

Economic Stress: The most immediate downside rating sensitivity for the bank's ratings relates to the economic and financial market fallout arising from the coronavirus outbreak. This represents a clear risk to our assessment of asset quality, earnings and capitalisation. The ratings could also be downgraded if the bank receives a substantial fine, leading to a material weakening in its capitalisation.

Ratings

Foreign Currency

Long-Term IDR	A+
Short-Term IDR	F1
Derivative Counterparty Rating	AA-(dcr)

Viability Rating	a+
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Support Rating	5
Support Rating Floor	NF

Sovereign Risk

Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

Applicable Criteria

[Bank Rating Criteria \(February 2020\)](#)

Related Research

[Global Economic Outlook: Crisis Update May 2020 - Coronavirus Shock Broadens](#)

[Coronavirus Rating Impact: Western European Banks \(April 2020\)](#)

[Fitch Downgrades Swedbank's Long-Term IDR to 'A+', Outlook Stable \(April 2020\)](#)

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Debt Rating Classes

Rating level	Rating
Long- and short-term deposits and senior preferred debt	AA-/F1+
Senior non-preferred	A+
Tier 2 subordinated debt	A-
Additional Tier 1 notes	BBB

Source: Fitch Ratings

Swedbank's long-term deposit and senior preferred debt is rated one notch above the bank's Long-Term Issuer Default Rating (IDR) of 'A+', to reflect the protection that could accrue to deposits and senior preferred debt from the bank's junior resolution debt and equity buffers. The Swedish resolution authority has already set minimum requirements for own funds and eligible liabilities (MREL) for Swedbank.

Under the current regulations only senior non-preferred or more junior debt will be MREL-eligible in Sweden from 2024. However, the enactment of the finalised second Bank Recovery and Resolution Directive (BRRD 2) into Swedish legislation will introduce a cap on subordination requirement.

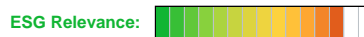
When the Swedish resolution authority sets the revised resolution buffer for Swedbank (in line with BRRD 2 subordination rules) we will review if it is sufficient to recapitalise the bank in a resolution scenario without causing losses to senior preferred creditors. Under our rating criteria Swedbank will need to hold a resolution buffer (comprising junior and senior non-preferred debt) of at least 10% of its risk-weighted assets (RWAs) to maintain the one-notch uplift for deposits and senior preferred debt.

Senior non-preferred debt is rated in line with Swedbank's Long-Term IDR because it is a direct, unsecured and senior obligation of the bank. Fitch views the probability of default on the senior non-preferred debt as the same as the probability of default of the bank.

Subordinated debt and additional Tier 1 securities issued by Swedbank are all notched down from its Viability Rating (VR). We rate subordinated debt two notches below Swedbank's VR to reflect the higher-than-average loss severity of this type of debt. The additional Tier 1 securities are four notches below Swedbank's VR to reflect the higher-than average loss severity risk of these securities (two notches) as well as the high risk of non-performance (two notches).

Ratings Navigator

Swedbank AB



Banks
Ratings Navigator

	Peer Ratings	Operating Environment	Company Profile	Management & Strategy	Risk Appetite	Asset Quality	Earnings & Profitability	Capitalisation & Leverage	Funding & Liquidity	Viability Rating	Support Rating Floor	Issuer Default Rating
aaa										aaa	AAA	AAA
aa+		↓								aa+	AA+	AA+
aa		↓	↓				↓	↓	↓	aa	AA	AA
aa-		↓	↓		↓					aa-	AA-	AA-
a+		↓	↓	↓	↓		↓	↓	↓	a+	A+	A+ Stable
a		↓	↓	↓	↓					a	A	A
a-		↓	↓	↓	↓					a-	A-	A-
bbb+										bbb+	BBB+	BBB+
bbb										bbb	BBB	BBB
bbb-										bbb-	BBB-	BBB-
bb+										bb+	BB+	BB+
bb										bb	BB	BB
bb-										bb-	BB-	BB-
b+										b+	B+	B+
b										b	B	B
b-										b-	B-	B-
ccc+										ccc+	CCC+	CCC+
ccc										ccc	CCC	CCC
ccc-										ccc-	CCC-	CCC-
cc										cc	CC	CC
c										c	C	C
f										f	NF	D or RD

Significant Changes

Finalised AML Investigations

In March 2020, the Swedish and Estonian financial regulators and Clifford Chance US LLP concluded in their separate investigations that Swedbank did not have adequate control over the money laundering and economic sanctions risk in its Baltic subsidiaries. The Swedish regulator fined Swedbank and issued a warning. The Estonian regulator obliged Swedbank to address shortcomings within eight months. Clifford Chance's investigation found about USD5 million of suspicious transactions, which constitute potential sanction violations. Swedbank has informed the US Treasury's Office of Foreign Assets Control about these transactions.

The bank remains subject to several other inquiries, including some by the US authorities, which may result in a material fine. Swedbank has acknowledged deficiencies in AML controls and the new chief executive's strategic priority is to address most of them by end-2020. The bank has been strengthening its AML controls since spring 2019.

Coronavirus Outbreak Drags on Swedish Operating Environment

Business activity in Sweden has been less constrained than in most European economies because the authorities introduced only moderate restrictions instead of a full lockdown. Nevertheless, we expect Sweden's GDP to contract 6.3% in 2020 and then rebound by 3.4% in 2021. The uncertainties surrounding growth forecasts are extremely high, and an even larger decline in output in 2020 and a weaker recovery in 2021 are possible.

Headwinds for the Swedish banks could be mitigated by the government's direct fiscal support (about 4.5% of 2019 GDP). The employment-related measures include subsidies (until end-2020) reducing employers' wage costs by about 50% in the event of reduced working hours. The government proposed to cover the entire cost of sick pay until July for employees and up to 14 days for the self-employed and then the coverage could be extended until September only for coronavirus-related sick pay. There are also payment deferrals of taxes, social contributions and temporary subsidies of up to 50% of rental costs for companies, additional financial aid to municipalities, and state guarantees on 70% of new loans, primarily for SMEs (up to SEK75 million).

Bar Chart Legend

Vertical bars – VR range of Rating Factor
 Bar Colors – Influence on final VR
 ■ Higher influence
 ■ Moderate influence
 ■ Lower influence

Bar Arrows – Rating Factor Outlook
 ↑ Positive ↓ Negative
 ⇅ Evolving □ Stable

The key economic stimulus measures include: a lowered counter-cyclical buffer to 0% from 2.5%; a relaxed liquidity coverage ratio (LCR) requirement for individual and total currencies; a suspension of the loan amortisation requirement until end-August 2021; and an extended phase-in period for compliance with the MREL until 2024. The regulator has also advised banks to retain 2019 earnings.

To safeguard credit supply to the economy, the Swedish central bank, the Riksbank, took several actions after the onset of coronavirus crisis: cut the overnight lending rate to 20bp (down 55bp), offered up to SEK500 billion corporate loan programme (channelled through banks); introduced a fresh three-month unlimited collateralised lending facility; increased the purchase of securities up to SEK300 billion in 2020; and provided up to USD60 billion of loans through a swap facility with the US Federal Reserve. The Riksbank also relaxed some collateral rules. We believe that the central bank is ready to take further measures to combat potential credit supply shortage or liquidity stress in the banking sector.

Summary Financials and Key Ratios

	31 Mar 20		31 Dec 19	31 Dec 18	31 Dec 17
	3 months - 1st quarter	3 months - 1st quarter	Year end	Year end	Year end
	(USDm)	(SEKm)	(SEKm)	(SEKm)	(SEKm)
	Unaudited	Unaudited	Audited - unqualified	Audited - unqualified	Audited - unqualified
Summary income statement					
Net interest and dividend income	663	6,695	26,141	25,409	25,533
Net fees and commissions	319	3,223	12,984	12,836	12,030
Other operating income	31	314	6,835	5,300	4,195
Total operating income	1,013	10,232	45,960	43,545	41,758
Operating costs	532	5,370	20,071	17,149	16,611
Pre-impairment operating profit	482	4,862	25,889	26,396	25,147
Loan and other impairment charges	213	2,151	1,469	521	1,285
Operating profit	269	2,711	24,420	25,875	23,862
Other non-operating items (net)	-396	-4,000	0	677	680
Tax	39	398	4,711	5,374	5,178
Net income	-167	-1,687	19,709	21,178	19,364
Other comprehensive income	452	4,565	-2,858	-811	-1,108
Fitch comprehensive income	285	2,878	16,851	20,367	18,256
Summary balance sheet					
Assets					
Gross loans	162,495	1,640,568	1,612,308	1,593,677	1,514,037
- Of which impaired	1,324	13,372	13,593	11,239	8,579
Loan-loss allowances	862	8,706	6,679	6,023	3,886
Net loans	161,633	1,631,862	1,605,629	1,587,654	1,510,151
Interbank	4,846	48,927	45,443	36,176	30,235
Derivatives	8,462	85,429	44,695	40,431	56,469
Other securities and earning assets	54,433	549,558	479,277	381,573	377,119
Total earning assets	229,373	2,315,776	2,175,044	2,045,834	1,973,974
Cash and due from banks	29,263	295,442	195,286	163,161	200,371
Other assets	6,364	64,251	37,898	37,097	38,291
Total assets	265,000	2,675,469	2,408,228	2,246,092	2,212,636
Liabilities					
Customer deposits	103,563	1,045,579	953,994	920,109	846,902
Interbank and other short-term funding	37,641	380,029	198,477	203,513	226,736
Other long-term funding	74,396	751,114	753,239	681,721	708,688
Trading liabilities and derivatives	7,333	74,034	75,322	69,649	60,659
Total funding	222,933	2,250,756	1,981,032	1,874,992	1,842,985
Other liabilities	27,029	272,883	272,081	222,322	225,029
Preference shares and hybrid capital	1,018	10,274	16,482	11,169	11,050
Total equity	14,021	141,556	138,633	137,609	133,572
Total liabilities and equity	265,000	2,675,469	2,408,228	2,246,092	2,212,636
Exchange rate		USD1 = SEK10.0961	USD1 = SEK9.32	USD1 = SEK8.971	USD1 = SEK8.2322

Source: Fitch Ratings, Fitch Solutions, Swedbank AB

Summary Financials and Key Ratios

	31 Mar 20	31 Dec 19	31 Dec 18	31 Dec 17
Ratios (annualised as appropriate)				
Profitability				
Operating profit/risk-weighted assets	1.6	3.8	4.1	5.8
Net interest income/average earning assets	1.2	1.2	1.2	1.3
Non-interest expense/gross revenue	53.0	44.5	40.3	40.7
Net income/average equity	-4.8	14.8	16.1	15.2
Asset quality				
Impaired loans ratio	0.8	0.8	0.7	0.6
Growth in gross loans	1.8	1.2	5.3	3.6
Loan loss allowances/impaired loans	65.1	49.1	53.6	45.3
Loan impairment charges/average gross loans	0.5	0.1	0.1	0.1
Capitalisation				
Common equity Tier 1 ratio	16.1	17.0	16.3	24.6
Tangible common equity/tangible assets	4.6	5.1	5.4	5.3
Basel leverage ratio	4.7	5.4	5.1	5.2
Net impaired loans/common equity Tier 1	4.2	6.3	5.0	4.7
Funding and liquidity				
Loans/customer deposits	156.9	169.0	173.2	178.8
Liquidity coverage ratio	162.0	182.0	144.0	173.0
Customer deposits/funding	47.4	48.8	49.6	46.9
Net stable funding ratio	116.0	120.0	111.0	110.0

Source: Fitch Ratings, Fitch Solutions, Swedbank AB

Key Financial Metrics – Latest Developments

Asset Quality Stress

We expect asset quality to deteriorate in 2Q20 as contraction in economic activity and increases in unemployment continue, and as the bank conducts a thorough review of its loan exposure. However, the moderate coronavirus-related restrictions on business activity in Sweden, together with loan amortisation holidays, a more relaxed approach to debt restructuring and government guarantees, should mitigate loan transfers to Stage 2 and Stage 3 and a corresponding increase in credit losses. The resilience of Swedbank's asset quality also reflects its prudent underwriting and the large stock of well-collateralised loans.

At end-March 2020 Swedbank's impaired loans ratio (comprising Stage 3 loans) was modest at 0.8%. The proportion of Stage 2 loans increased modestly to 7.6% (up 1pp qoq). Loan impairment charges amounted to 45bp of average gross loans in 1Q20, the highest level since 2009.

The bank's exposure to "considerably" and "moderately" vulnerable sectors was 8% and 4%, respectively, of its loan portfolio. In 1Q20, 30% of LICs were directly linked to manufacturing, retail, hotels, restaurants, shipping and offshore. Shipping and offshore is the most risky portfolio (54% of Stage 3 loans at end-March 2020), but represents a moderate 17% of Swedbank's CET1 capital. Asset quality in residential mortgage lending (about 55% of loans, mostly originated in Sweden) will hold up, supported by payment holidays and employment protection measures.

Profitability Under Pressure

Swedbank's loss in 1Q20 was driven by the AML fine (a non-operating expense by our definition). We expect the bank's interest income to shrink due to a slump in demand and margin pressure (given high competition) in residential mortgage loans. However, this could be partly offset by a higher demand for liquidity facilities from corporates. Fee and trading income will remain under pressure until card and payment transactions and financial market volatility normalise. We expect that a material part of the AML-related costs (about 12% of Swedbank's 2020 operating expenses guidance), will become permanent and lift Swedbank's structural cost/income ratio above 45%.

Credit losses will continue to absorb a material proportion of the pre-impairment operating profit in 2020 (44% in 1Q20 compared with 5% average between 2019-2016). A materialisation of Swedbank's negative macroeconomic scenario (around an 8% GDP contraction in Sweden with a return to growth only in 2022) would bring about additional SEK 1.2 billion LICs (about a quarter of 1Q20 pre-impairment operating profit).

Strong Capitalisation

Swedbank's CET1 ratio fell by 90bp in 1Q20 to 16.1% due to 6% growth in RWAs mainly driven by loan growth and revised LGD parameters. Swedbank's CET1 ratio surplus of 300bp above the minimum requirement is sufficient to absorb higher RWAs (from asset quality deterioration and loan growth), the potentially higher capital requirement for operational risk (due to the recent AML fine), and the estimated additional 50bp Pillar 2 requirement for commercial real estate from December 2020. Swedbank could increase its CET1 ratio by 1.4pp if it decided to cancel the 2019 dividend.

Stable Funding, Low Refinancing Risk

The bank is highly reliant on the wholesale markets, particularly through covered bond issuances. However, this is well mitigated by a deep domestic captive investor base, a high-quality cover pool, robust treasury management and a large buffer of liquid assets comfortably covering short-term refinancing needs. The bank's access to the Swedish covered bond market remained stable despite coronavirus-related disturbance in financial markets, and the negative outcome of AML investigations (although bond interest rates went up).

The bank holds ample liquidity buffer (18% of assets at end-March 2020) which (together with available central bank facilities and unused cover pool overcollateralisation) fully covers its short-term refinancing needs and loan expansion plans. Following the revised deadline for MREL subordination (from 2024) Swedbank will issue less expensive senior preferred debt (than senior non-preferred debt) in 2020 to meet its MREL.

Sovereign Support Assessment

Support Rating Floor		Value		
Typical D-SIB SRF for sovereign's rating level (assuming high propensity)		A+ to A-		
Actual country D-SIB SRF		NF		
Support Rating Floor:		NF		
Support Factors	Positive	Neutral	Negative	
Sovereign ability to support system				
Size of banking system relative to economy			✓	
Size of potential problem	✓			
Structure of banking system			✓	
Liability structure of banking system		✓		
Sovereign financial flexibility (for rating level)			✓	
Sovereign propensity to support system				
Resolution legislation with senior debt bail-in			✓	
Track record of banking sector support		✓		
Government statements of support		✓		
Sovereign propensity to support bank				
Systemic importance		✓		
Liability structure of bank		✓		
Ownership		✓		
Specifics of bank failure		✓		
Policy banks				
Policy role				
Funding guarantees and legal status				
Government ownership				

Swedbank's Support Rating of '5' and Support Rating Floor of 'No Floor' reflect Fitch's view that senior creditors cannot rely on receiving extraordinary support from the Swedish sovereign in the event that the bank becomes non-viable. The EU's Bank Recovery and Resolution Directive provides a framework for resolving banks that is likely to require senior creditors participating in losses, if necessary, instead of, or ahead of, a bank receiving sovereign support.

Environmental, Social and Governance Considerations

FitchRatings Swedbank AB

Banks
Ratings Navigator

Credit-Relevant ESG Derivation

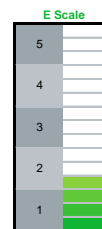
Swedbank AB has 1 ESG key rating driver and 4 ESG potential rating drivers

- Swedbank AB has exposure to board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal/compliance risks; business continuity; key person risk; related party transactions which, on an individual basis, has a significant impact on the rating.
- Swedbank AB has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating.
- Swedbank AB has exposure to operational implementation of strategy but this has very low impact on the rating.
- Swedbank AB has exposure to organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership but this has very low impact on the rating.
- Swedbank AB has exposure to quality and frequency of financial reporting and auditing processes but this has very low impact on the rating.

key driver	1	issues	Overall ESG Scale
			5
driver	0	issues	4
potential driver	4	issues	3
	4	issues	2
not a rating driver	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference
GHG Emissions & Air Quality	1	n.a.	n.a.
Energy Management	1	n.a.	n.a.
Water & Wastewater Management	1	n.a.	n.a.
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Company Profile; Management & Strategy; Risk Appetite; Asset Quality



How to Read This Page

ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

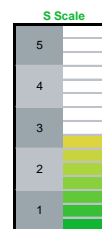
The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board(SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

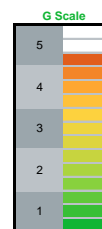
Social (S)

General Issues	S Score	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities; SME and community development programs; financial literacy programs	Company Profile; Management & Strategy; Risk Appetite
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Company Profile; Management & Strategy; Risk Appetite
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Company Profile; Management & Strategy
Employee Wellbeing	1	n.a.	n.a.
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Company Profile; Financial Profile



Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference
Management Strategy	3	Operational implementation of strategy	Management & Strategy
Governance Structure	5	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal/compliance risks; business continuity; key person risk; related party transactions	Management & Strategy; Earnings & Profitability; Capitalisation & Leverage
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Company Profile
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Management & Strategy



CREDIT-RELEVANT ESG SCALE	
How relevant are E, S and G issues to the overall credit rating?	
5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

Swedbank has an ESG Relevance Score of '5' for governance structure due to its shortcomings in money laundering controls, which has a negative impact on our assessment of the bank's risk appetite and is highly relevant to the rating.

Other ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or to the way in which they are being managed by the entity. For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg.

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