Wide Angle Shot: Austria soon top-notch AAA-rated sovereign again?

After the leading rating agency S&P raised its outlook to 'positive' (Aug 2024), Austria came closer to a top-notch triple AAA rating. Since the downgrading into the AA space in the wake of the euro sovereign debt crisis, S&P and Fitch had previously occasionally flagged positive outlooks. This time, we see the medium to longer-term (S&P) upgrade possibility as more likely than before. However, our assessment of some short-term (economic) risks differs slightly compared to S&P. Hence, the return to the exclusive euro-triple-AAA club could take some time and may require economic policy adjustments. Overall, the example of Austria shows: Returning to AAA status — if at all — is usually a long-term uphill battle. Austria is not (yet) priced as an AAA credit on financial markets.

Sovereign debt crisis cost several euro countries their AAA rating

In the **course** and **aftermath** of the **euro sovereign debt crisis**, **Austria**, like **France** and **Finland**, lost its top AAA rating by the three major rating agencies. In 2012, S&P lowered Austria's rating to AA+, followed by Fitch and Moody's in 2015 and 2016 respectively. Of the aforementioned countries, however, **Austria** was and still is the **closest** to **regain** the **AAA status.** Fitch already had a positive outlook outstanding from July 2018 to May 2020, which was downgraded again to 'neutral' due to the coronavirus pandemic. Between October 2022 and August 2023, the rating outlook was even temporarily set to 'negative' due to uncertainty surrounding Russian gas supplies. S&P already had a positive outlook outstanding between February 2022 and August 2022, which was then downgraded to 'neutral' again due to the same uncertainties. **Beginning** of **August 2024, S&P changed** the rating **outlook** for Austria back to **'positive**' again.

In addition to the three leading agencies mentioned above, Scope and DBRS should also be mentioned, whose ratings are also taken into account by ECB. Austria has an outstanding AAA rating from DBRS. Scope withdrew Austria's top rating in its last review in April 2024 and lowered it one notch to AA+.

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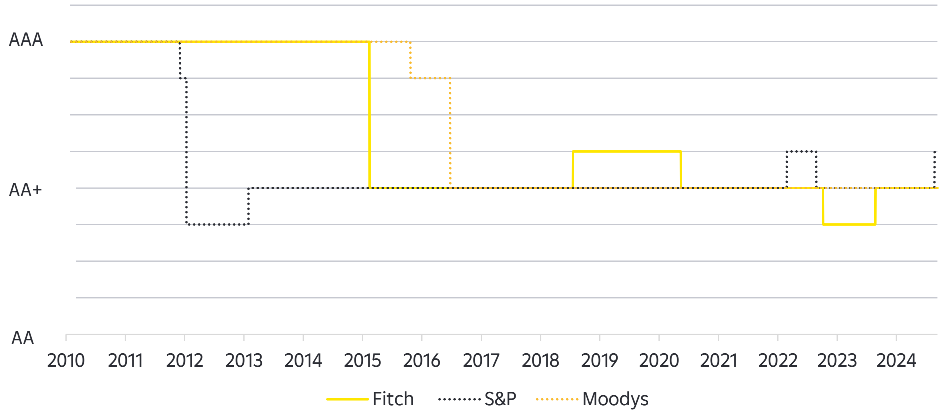
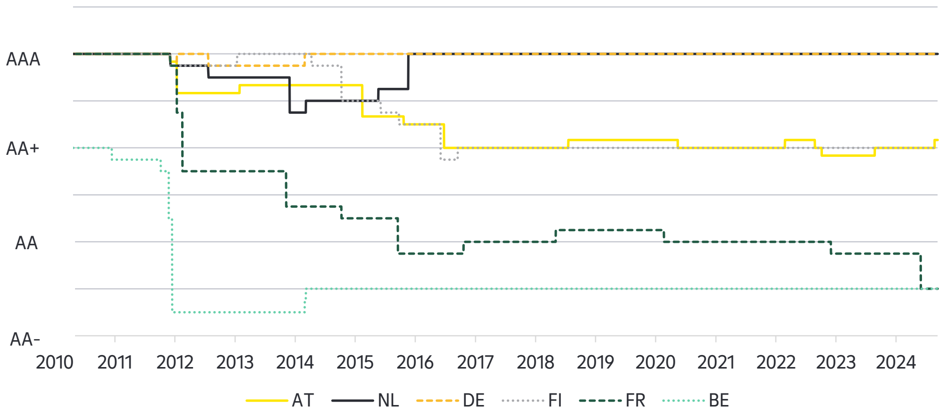
Chart 1 - Republic of Austria sovereign rating leading agencies



Rating incl. outlook
Source: Rating agencies, RBI/Raiffeisen Research

Chart 2 - Republic of Austria sovereign rating vs. peers



Average of S&P and Moody's; incl. outlook
Source: Rating agencies, RBI/Raiffeisen Research

In principle, the **rating agencies' assessments** are **very similar to each other,** especially when it comes to the highest rating bucket(s). All EU countries with a AAA rating by at least one of the three leading rating agencies are also assigned a triple-A rating and stable outlook by all other major rating agencies. These are the euro members **Germany, Netherlands** and **Luxembourg**, as well as **Denmark** and **Sweden** inside EU and **Norway** plus **Switzerland**. Rating agencies also agree on the second-highest credit rating bucket inside the euro bloc. In addition to Austria, Finland can be found here. There is a tendency towards greater fluctuation among sovereign ratings as creditworthiness falls, also inside the euro area (see Chart 3).

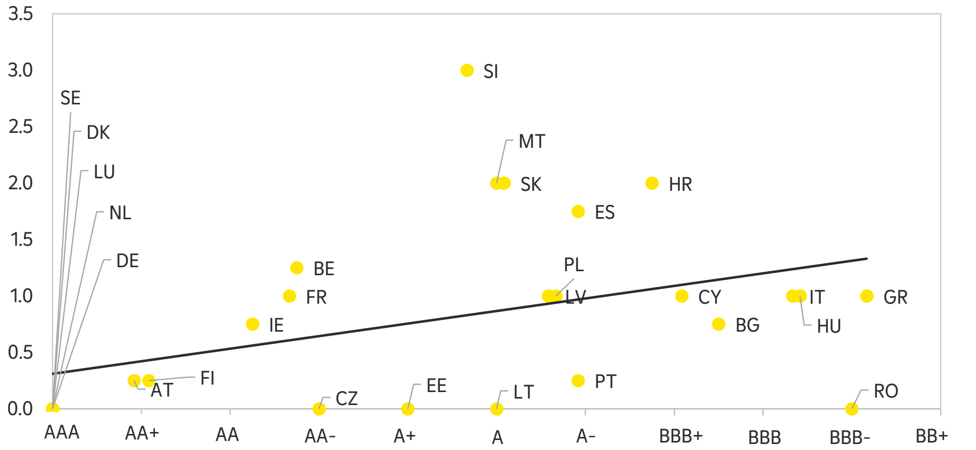
Table 1 - Ratings

Issuer	S&P current	S&P next review	Moody's current	Moody's next review	Fitch current	Fitch next review
Germany	AAA (sta)	22/11/2024	Aaa (sta)	next year	AAA (sta)	next year
Netherlands	AAA (sta)	10/18/2024	Aaa (sta)	next year	AAA (sta)	next year
Luxembourg	AAA (sta)	next year	Aaa (sta)	01/11/2024	AAA (sta)	22/11/2024
Sweden	AAA (sta)	next year	Aaa (sta)	next year	AAA (sta)	next year
Denmark	AAA (sta)	next year	Aaa (sta)	next year	AAA (sta)	next year
Austria	AA+ (pos)	next year	Aa1 (sta)	next year	AA+ (sta)	next year
Finland	AA+ (sta)	25/10/2024	Aa1 (sta)	13/12/2024	AA+ (neg)	next year
Ireland	AA (sta)	15/11/2024	Aa3 (pos)	next year	AA (sta)	15/11/2024
France	AA- (sta)	29/11/2024	Aa2 (sta)	25/10/2024	AA- (sta)	10/11/2024
Belgium	AA (sta)	25/10/2024	Aa3 (sta)	10/4/2024	AA- (neg)	next year
Czech Republic	AA- (sta)	10/11/2024	Aa3 (sta)	next year	AA- (sta)	next year
Estonia	A+ (sta)	29/11/2024	A1 (sta)	next year	A+ (sta)	next year
Slovenia	AA- (sta)	06/12/2024	A3 (sta)	10/11/2024	A (sta)	10/11/2024
Lithuania	A (sta)	29/11/2024	A2 (sta)	10/18/2024	A (sta)	08/11/2024
Malta	A- (sta)	06/12/2024	A2 (sta)	22/11/2024	A+ (sta)	next year
Slovakia	A+ (sta)	25/10/2024	A2 (neg)	13/12/2024	A- (sta)	06/12/2024
Latvia	A (sta)	29/11/2024	A3 (sta)	next year	A- (pos)	15/11/2024
Poland	A- (sta)	08/11/2024	A2 (sta)	next year	A- (sta)	08/11/2024
Portugal	A- (pos)	next year	A3 (sta)	15/11/2024	A- (pos)	next year
Spain	A (sta)	next year	Baa1 (pos)	next year	A- (sta)	08/11/2024
Croatia	A- (pos)	next year	Baa2 (pos)	08/11/2024	A- (sta)	next year
Cyprus	BBB+ (pos)	13/12/2024	Baa2 (pos)	22/11/2024	BBB+ (pos)	06/12/2024
Bulgaria	BBB (pos)	22/11/2024	Baa1 (sta)	next year	BBB (pos)	10/18/2024
Italy	BBB (sta)	10/18/2024	Baa3 (sta)	22/11/2024	BBB (sta)	10/18/2024
Hungary	BBB- (sta)	25/10/2024	Baa2 (sta)	29/11/2024	BBB (neg)	06/12/2024
Romania	BBB- (sta)	10/11/2024	Baa3 (sta)	9/27/2024	BBB- (sta)	next year
Greece	BBB- (pos)	10/18/2024	Ba1 (pos)	next year	BBB- (sta)	22/11/2024

Grey background: Review in upcoming 30 days; Green/Red text: positive/negative outlook; countries sorted by average of outstanding ratings incl. outlook

Source: LSEG, RBI/Raiffeisen Research

Chart 3 - Rating fluctuation between the rating agencies



Ratings from S&P, Fitch and Moody's incl. outlook taken into account, Y-axis corresponds to difference between minimum and maximum rating, where 1=one rating level, or 0 means that all three rating agencies have the same rating (incl. outlook) outstanding

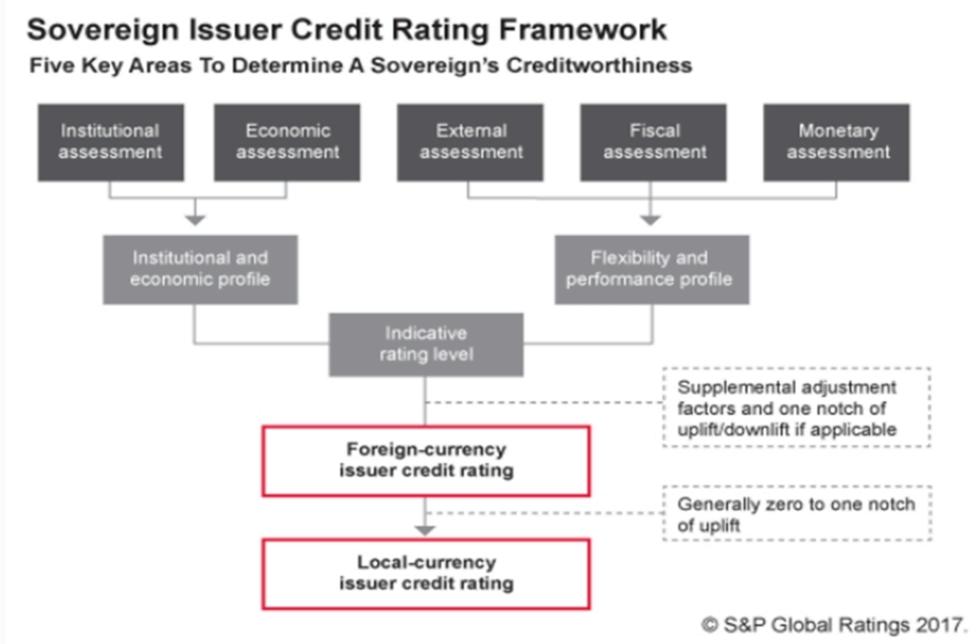
Source: LSEG, RBI/Raiffeisen Research

Methodology of the rating agencies

The **similarity** in **sovereign ratings** is not surprising at all. Rating agencies have **by and large similar approaches** to their assessment and **basically work** with the same **indicators**. In a **first step**, a preliminary **indicative rating** is usually calculated based on **quantitative** and **qualitative factors**. Here, the quantitative indicators and relevant creditworthiness figures have a clear overweight. Above all, realized values over a longer period of time are also included, not just forecasts (i.e. past performance counts). In a **second step**, the **indicative rating** is **adjusted** based on factors that were not, or not sufficiently, taken into account in the first place. Overall, creditworthiness indicators/ factors, which are taken into account by the rating agencies, are highly comparable. However, they **differ** in the **details** of the selected quantitative time series/ratios and in the weights they assign to individual factors. For example, S&P uses the **net government debt ratio**, among other things, to measure the debt burden, whereas Moody's uses the more conventional **(gross) public debt-to-GDP ratio**. There are also differences in the treatment of structural factors, such as membership in a monetary union.

S&P bases its indicative rating on five pillars. This comprises institutional, economic, external, fiscal and monetary factors (see Exhibit 1). A rating is assigned for each of these pillars (1-6). Specific predefined data and qualitative adjustments are included here. In a first step, the five factors are combined with different weightings to form two sub-factors ('Institutional and economic' and 'Flexibility and performance'), which ultimately determine the indicative rating. In a final step, an **additional adjustment** ('supplemental adjustment') can then be made to the indicative rating. This is intended to take into account additional factors that were not adequately reflected in the previous five pillars. The reason cited for the current factual rating of the Republic of **Austria**, which is **ultimately one notch lower than** the **indicative rating**, is the remaining **uncertainty** regarding **future gas supplies.** In regard to the USA, for example, the role of the US dollar as world reserve currency has a positive risk-mitigating effect. In the **case of top-notch sovereign credit ratings**, however, an **adjustment** to the indicative rating like in the case of Austria is the **exception rather than** the **rule** (Table 2).

Exhibit 1 - S&P methodology



Source: S&P

Table 2 - S&P methodology - rating subcomponents

Country	Institutional & economic profile		Flexibility and performance profile				Indicative rating	supplementetal adjustment	Rating
				Fiscal					
	Institutional	Economic	External	Flexibility and performance	Debt burden	Monetary			
Austria	2	1	1	3	3	2	aaa	-1	AA+
Germany	2	1	1	2	2	2	aaa	0	AAA
Netherlands	2	1	2	2	2	2	aaa	0	AAA
Sweden	1	1	2	1	1	1	aaa	0	AAA
Denmark	1	1	3	1	1	3	aaa	0	AAA
Switzerland	1	1	1	1	1	2	aaa	0	AAA
Finland	2	1	4	1	2	2	aa+	0	AA+
USA	2	1	2	5	6	1	aa	1	AA+
New Zealand	1	1	5	3	3	1	aa+	0	AA+

selected countries

Source: S&P, RBI/Raiffeisen Research

S&P's sovereign rating Republic of Austria - A look behind the scenes

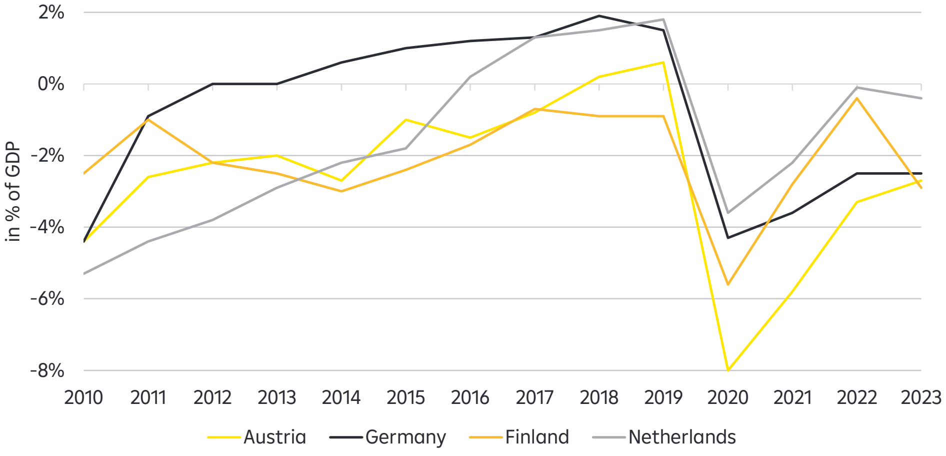
On **25 February 2022**, S&P confirmed Austria's AA+ rating, which was also flagged by the indicative rating back then, and at the same time **raised** the **outlook from** '**neutral**' to '**positive**'. The main reason given for this was the improving fiscal outlook. **One day before** the rating outlook was raised, **Russian** troops **invaded Ukraine**. At the occasion of Austria's next rating review in August 2022, the outlook was **lowered** again to '**neutral**' due to **uncertainties** regarding **gas supplies** from Russia. Two years later in August 2024, as gas shortages have not materialized, S&P **raised** the **outlook** again to '**positive**'. **In contrast** to **August 2022**, however, the rating agency's **indicative rating** now **points to** the top-notch **AAA-rating**. Since 2023, the 'external' factor has been raised by one notch, which has led to the indicative rating being raised to aaa. Among other things, this takes into account the expectations of continued high current account surpluses and the comparatively low **net external debt** (overall economy) in **relation** to **current account inflows.** Compared to the AAA-rated peers, **Austria** stands out **favorably** in regard to this external liquidity measure. Only Germany and Switzerland can also capitalize on a top-notch score (1) here.

Austria receives a **lower scoring** compared to **AAA-rated euro peers** in the **fiscal domain.** Regarding this rating driver, Austria's assessment (3) is one notch lower than that of the Netherlands and Germany (2) and two notches lower than that of Denmark and Sweden (1). In particular, the **high net debt** (including consideration of liquid funds) in relation to GDP of 68% in 2023 has a negative impact. No other AAA-rated country exhibits such a high value. Austria's final AA+ rating is based on an additional adjustment ('supplemental adjustment') of one notch downwards. The rating agency cites the **uncertainty regarding energy supplies**. At the same time, S&P stresses that Austria can cope with possible short-term disruptions and limit the economic damage that could be caused by the end of the gas transit agreement between Ukraine and Russia at the end of this year. S&P cites **two points** for a **possible rating upgrade** in its latest review. Firstly, **continued robust economic performance**, even in the event of energy supply disruptions, and secondly, **fiscal results** that **exceed current expectations**. The **next standard rating reviews** by **S&P** in **2025** are **expected** to take place in **February**/**March** and **August**/**September**.

Austria with higher deficits than Germany and the Netherlands...

The **rather subdued performance** of Austria in **peer comparison** to **other AAA credits** in the **fiscal domain** is also evident when looking at budget balances. **Since 2016**, Austria posted **higher deficits/lower surpluses** than **AAA-rated countries** like Germany and the Netherlands in each and every year (Chart 4). The most "recent" outperformance vis-a-vis Germany when it comes to fiscal accounts dates back almost two decades (2005). On the one hand, this is due to **higher interest expenditure** (Charts 6 & 7), which had been higher in relation to economic strength as well as relative to government revenues since the 2010s. However, the difference has narrowed since the inflation crisis and the rise in interest rates. The longer duration of Austrian government debt and the generally faster rise in government revenue with higher inflation may have evidently had a positive effect. On the other hand, Austria has also generated **relatively low primary surpluses** (Chart 5). From 2016 to 2022, these were consistently lower than in Germany or the Netherlands. Only in the last two years has the primary balance been on a par with Germany, whereas the Netherlands continues to show better results. Although the **longer-term track record** on the **budget** and **primary balance** is **worse in Austria compared** to **Germany** and the **Netherlands**, there has **recently** been a **convergence with Germany**, although this appears to be due more to a deterioration in Germany than a structural improvement in case of Austria.

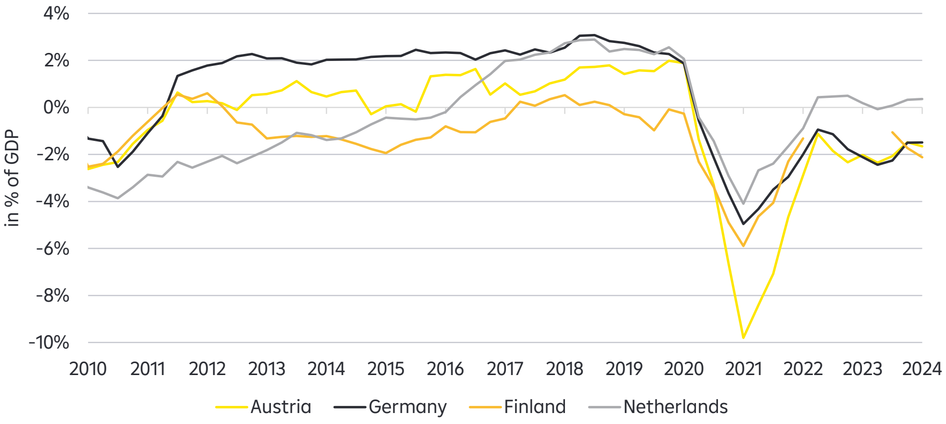
Chart 4 - Budget balance



yearly data

Source: Eurostat, RBI/Raiffeisen Research

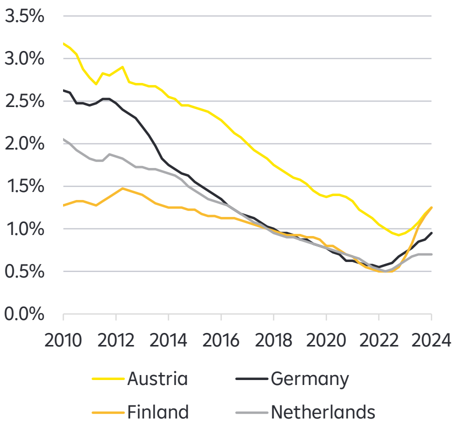
Chart 5 - Primary budget balance



Average of the last 4 quarters; missing data for Finland Q2/Q3 2022

Source: Eurostat, RBI/Raiffeisen Research

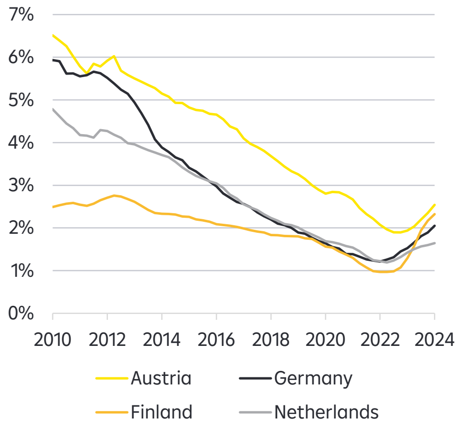
Chart 6 - Interest payments (in % of GDP)



Average of the last 4 quarters

Source: Eurostat, RBI/Raiffeisen Research

Chart 7 - Interest payments (in % of revenue)



Average of the last 4 quarters

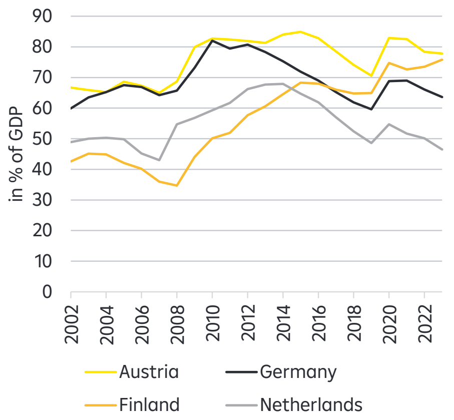
Source: Eurostat, RBI/Raiffeisen Research

... and also with a higher or increased debt ratio

The (relative) **level** of **government indebtedness** in **Austria** is also **higher** than in **Germany**, the **Netherlands** and **Finland**. From the mid-2000s until the euro sovereign debt crisis, Austria posted a public debt-to-GDP ratio in the neighborhood of Germany (Chart 8). With the stronger decline in interest costs and a more bold fiscal consolidation in Germany, the public debt-to-GDP ratio fell more strongly/earlier. In the late 2010s, Austria's debt ratio was around 10 percentage points (pp) higher than in Germany. **Since** the **coronavirus pandemic**, the **difference** has **increased slightly**. In Austria, public debt as a percentage of GDP in 2023 was 7 PP higher than in 2019, in Germany 4 PP higher and in the Netherlands 2 PP lower (Chart 9). In Finland, the debt ratio rose by 11 PP.

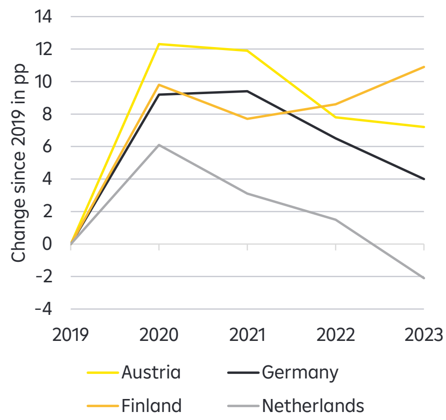
The **long-term subdued fiscal performance** compared to AAA euro credits and the less constant generation of primary surpluses in economically 'good growth times' has meant that **Austria** has only been able to **reduce** its **government debt-to-GDP ratio** by around **10-12** percentage points (from the peak in the 2010s to 2019), **while** the **Netherlands** and **Germany** managed to **lower** their **public debt-to-GDP ratio** by around **20 percentage points** (during the same time horizon). Compared to AAA-rated sovereigns inside the euro area, Austria has **hardly managed** any **structural fiscal consolidation** over the **last decade**. In our opinion, institutional reasons rather than direct economic factors can be held responsible for this. The more recognizable fiscal consolidation in the Netherlands should also be a reason for the significantly faster return to the status of an untarnished AAA debtor (following a loss of the AAA-status in the early 2010s). In principle, Austria is not yet at the same level as the AAA-rated euro peers Germany or the Netherlands in terms of **deep sovereign credit fundamentals** when it comes to structural government debt and refinancing metrics (e.g. interest payments in relation to economic output, government revenues or the government debt ratio).

Chart 8 - Debt level



yearly data
Source: Eurostat, RBI/Raiffeisen Research

Chart 9 - Debt level since 2019

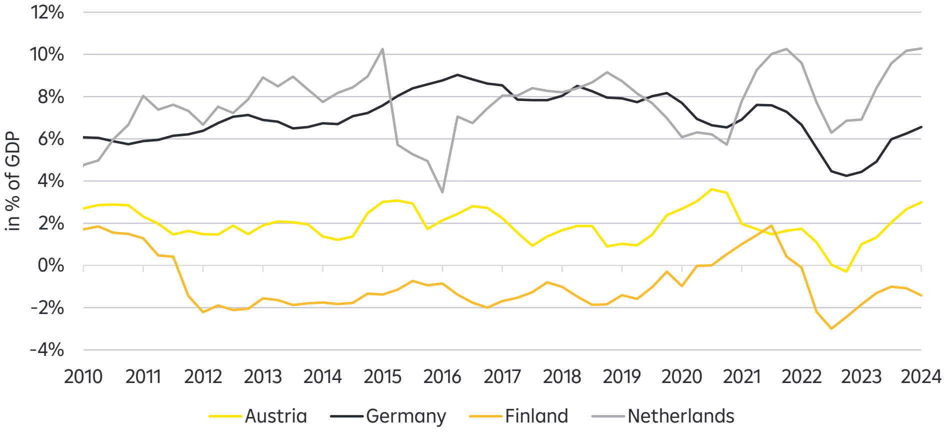


yearly data
Source: Eurostat, RBI/Raiffeisen Research

Lower current account surpluses compared to DE and NL

Austria's **current account balance** has **recovered** from its lows in 2022, similar to Germany and the Netherlands (Chart 10). However, the level of surpluses is still significantly lower in Austria. In Austria, the surplus in 2023 was 2.7% of GDP, in Germany 6.3% and in the Netherlands 10.2%. The **increase** in **Austria's** current account **balance** is due in particular to a **recovery** in **trade** in **goods** (Chart 11). The surplus in the goods sector has even risen above that in the services sector, a situation that was not observed in the past. However, it should be noted that the increase in the current account surplus and the solid export performance up to now were **'subsidized'** via **lower profitability** and **profit margins**. Instead of passing on the substantive (wage) cost increases on the Austrian home market to end customers abroad (the export price trend is in line with the European average), i.e. Austrian (industrial) companies have accepted lower profits. With regard to Austria's external position, S&P positively takes note of the low net external debt (total economy) compared to current account inflows. With regard to the **current account (surplus) position**, we currently **see downside risks** given increasing signs of an erosion of the **international price competitiveness** of the Austrian economy at the macroeconomic level.

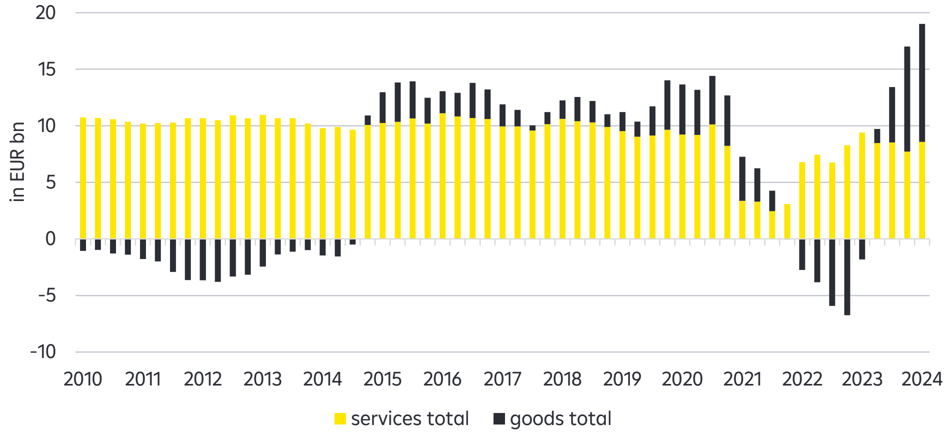
Chart 10 - Current account balance



last 4 quarters

Source: Eurostat, RBI/Raiffeisen Research

Chart 11 - Goods and services component of Austria's current account



sum of last 4 quarters

Source: Eurostat, RBI/Raiffeisen Research

National Council elections without short-term impact on rating

According to the latest polls, the **balance** of **political power** in Austria is likely to **change** after the upcoming **National Council elections** on **29 September**. According to the polls, the current governing parties would no longer have a majority, which means that a new coalition is to be expected. In the short term, we **do not expect** a (potential) **change** of **government** to have any tangible **impact** on the **rating** of the **Republic** of **Austria**, which means that we share the view of the rating agencies. S&P expects the economic policy of the new government to remain largely unchanged, while we certainly see an opportunity for an economic policy that is more strongly orientated towards supporting the competitiveness position and business location via supply-side oriented policies. However, a change towards a **lower degree** of **fiscal responsibility** in the sense of comprehensive spending or economic stimulus programmes **would** clearly have a **negative impact**. In this context, reference should once again be made to the more subdued fiscal performance compared to other AAA sovereigns and the lack of a 'track record' when it comes to structural fiscal consolidation. In this respect, the **new government** should actively take current **fiscal** and **macroeconomic challenges into account**.

Country rating upgrade possible with strategic course setting

We share the view that **Austria should not expect any challenging gas supply shortages.** Despite the currently still high import quota from Russia, Austria is still well "hedged" due to the filled gas storage. The increased diversification from abroad and the expansion of gas pipelines to Germany and Italy are prepared for a possible abrupt end of the gas transit via Ukraine (see scenario analysis by the Austrian Energy Agency, in German language). However, more clarity about the future energy purchasing strategy could reduce market and rating uncertainty. Here, more decisive action or clear communication from the future government might be required.

On a **macroeconomic level** we are currently **observing alarming developments** in the **Austrian economy** that warrant great **caution** when it comes to the **near-** to **medium-term growth outlook** (see Austrian focus: Endless recession instead of the end of the recession?). Shortly after the rating outlook was raised by S&Ps, the Q2 growth rate was substantially revised downwards (from 0.0% to -0.4% QoQ). Hence, **we** have **adjusted** our **GDP call** for the **full year 2024 substantially downwards** (from +0.2% to -0.5%). After a recession in 2023, we now expect another year of negative GDP growth in 2024. On a per capita basis, real economic output in Austria at the end of 2023 is 1.6% lower than at the end of 2019. Inside the euro area, only Estonia (-2.1%) posted a worse result. Furthermore, low investment activity has been observed since 2022. **Gross fixed capital formation** as a percentage of GDP has been **lower** in **Austria** since 2022 **than** inside the **euro area** and **also lower than** in the **"sick man of Europe" Germany**. If the trend of low investment activity continues, this could lead to additional medium-term risks when it comes to the international competitiveness position (lack of productivity gains, production relocations, further decline in international competitiveness), including a potential **eroding of the current account surplus** position. In addition, the significantly worsening economic outlook — also compared to other AAA-rated countries — makes fiscal consolidation an uphill battle. These risks clearly do not appear to be fully shared by S&P (yet). In this respect, the **better-than-expected budgetary results** demanded for a rating upgrade are **possible**, but have become **less likely** in light of the **challenging near- to medium-term macroeconomic outlook**. S&P expects fiscal deficits of 3.0%, 2.8% and 2.8% in 2024, 2025 and 2026. The European Commission (as of May) is forecasting budget deficits of 3.1% and 2.9% in 2024 and 2025. Our expectations (as of July) are slightly worse than those of S&P at 3.1% and 3.0% respectively (2024 and 2025), and currently face upside risks. Any potential **improvement** of the **sovereign rating** should thus also be **backed** up by a **credible fiscal policy perspective —** bearing in mind that there is no history of bold structural consolidation over the last decade.

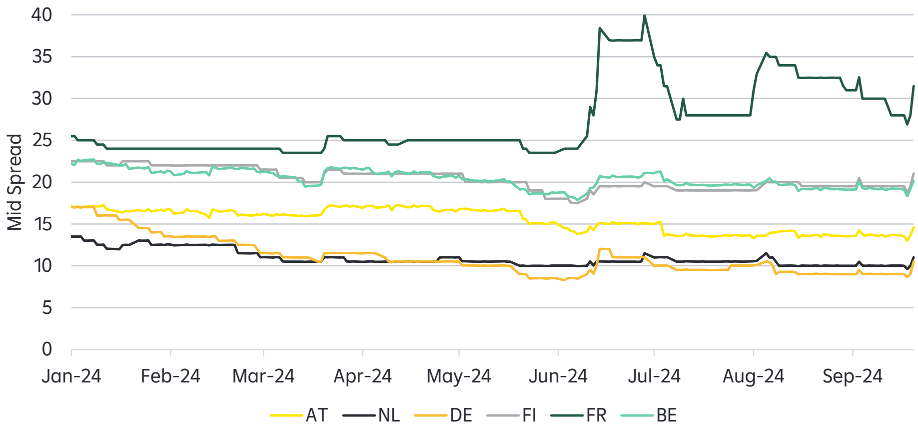
In sum, the **improved indicative rating** of **S&P** in particular speaks for an upgrade to AAA. Like the rating agency, we do not expect to experience any economically damaging shortage in gas supplies. The argument for the additional adjustment ("supplemental adjustment") of the rating could accordingly be dropped in the medium term. However, we see **risks** on the **economic front**. The **budget deficit** could be higher than previously expected this year according to the latest data. If the competitiveness position of the domestic industry continues to deteriorate, the **current account surplus** position could also decline. In the short term, a possible change of government should not affect the sovereign rating and in case substantive economic policy slippages will be avoided. All in all, we think **sovereign rating upgrades (S&P)** for **Austria** to **AAA** in the **coming years**, **possibly later** in **2025, remain feasible**. However, a stability-oriented course setting in the areas of fiscal policy and wage setting plus a greater focus on the international competitiveness position of the Austrian economy (with likely positive effects on the current account position) could be **supportive** for such **a re-rating outlook**.

Moreover, when and if financial markets will fully price the Republic of Austria as **AAA credit** and/or if such a top-notch rating will be is finally attained Austria could save approximately **EUR 1 billion** in debt (re-)financing costs in the coming years. Additionally, some reform measures necessary to achieve an untarnished AAA rating in the market should also **sustainably improve** the **structural fiscal position** of the **Republic** of **Austria**, promising further savings and/or cost reductions in the public sector. **Private issuers** on the capital market might also be able to achieve slightly more favorable refinancing costs, although we would expect the effects here to be rather minor compared to the Republic of Austria.

Market sees Austria between AAA and AA

In the CDS market, Austria's default risk is priced between that of AAA-rated countries like Germany and the Netherlands, and countries with AA+ to AA- ratings like Finland, Belgium, and France (Chart 12). Austrian bonds, on the other hand, price a comparable risk premium to Belgium and Finland (Chart 13). An **AAA rating** for **Austria would** be **consistent** with **pricing** in the **CDS market** but is **not implied by it.** On **bond markets**, Austria is currently **not priced as AAA sovereign credit**. Thus, an upgrade or market speculation in this direction would have a positive impact, including on the actual refinancing costs of the Republic of Austria.

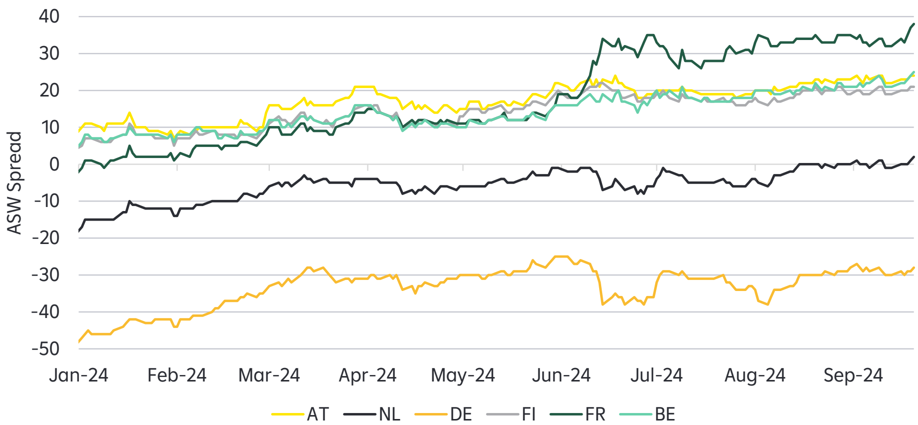
Chart 12 - Risk premia euro area sovereigns - CDS



5y USD CDS, 2014 contract

Source: LSEG, RBI/Raiffeisen Research

Chart 13 - Risk premia euro area sovereigns - Bond market



ICE Indices 7-10y

Source: LSEG, RBI/Raiffeisen Research

Appendix

Table 3 - Fundamental indicators

	economics					debt metrics				refinancing risk			population		governance
	GDP nominal (EUR mn)	GDP per capita (EUR, PPP)	GDP per capita (EUR)	cum. growth since Q4 2019*	Q2 2024: qoq	budget balance/ GDP**	debt/ GDP	interest paid/GDP**	interest paid/revenue**	avg debt life (years)	1y	5y	2019-2023 p.a.	old-age-dependency***	World bank governance indicators****
AT	480,875	46,200	52,370	1.1%	-0.4%	-2.9%	80%	1.3%	2.5%	10.9	17%	50%	0.7%	29.6	87
FI	273,596	40,700	49,000	-0.3%	0.1%	-3.4%	78%	1.3%	2.3%	8.1	15%	45%	0.3%	37.8	95
DE	4,217,990	43,400	49,520	0.2%	-0.1%	-2.5%	63%	1.0%	2.1%	7.8	15%	50%	0.1%	34.7	88
NL	1,083,067	48,900	59,710	7.6%	1.0%	-0.4%	44%	0.7%	1.6%	9.1	10%	42%	0.8%	31.4	92

**until Q2 2024; **average of the last four quarters; ***65+/(15-64); ****average of the six indicators; refinancing risk based on ESDM risk indicators Q2 2024*

Source: Eurostat, ESDM, RBI/Raiffeisen Research

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	Column A	Column B
Investment recommendation	Basis: All recommendations for all financial instruments (last 3 months)	Basis: Recommendations for financial instruments of all issuers, for which special services were rendered in the last 3 months
Buy recommendations	28.2%	32.3%
Hold recommendations	53.8%	48.4%
Sell recommendations	17.9%	19.4%

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Creation time of this publication: 24/09/2024 7:19 A.M. (CEST) ;

First Dissemination of this publication: 24/09/2024 7:19 A.M. (CEST)