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# Electrolux Professional AB (EPRO.B.SE)

Q2 2023 Earnings Call

## CORPORATE PARTICIPANTS

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### Gustav Hagéus

*Analyst, Skandinaviska Enskilda Banken AB*

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## MANAGEMENT DISCUSSION SECTION

### Jacob Broberg

*Chief Communication & Investor Relations Officer, Electrolux Professional AB*

Good morning and welcome to Electrolux Professional Group Q2 Result Presentation. My name is Jacob Broberg. I'm heading up Investor Relations and Communications. I'm here in sunny Stockholm today. I have Alberto Zanata, our President and CEO; and Fabio Zarpellon, our CFO with me.

And as always, we kick off with Alberto. Please go ahead, Alberto.

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### Alberto Zanata

*President & Chief Executive Officer, Electrolux Professional AB*

Thank you, Jacob. Good morning to everybody. Q2 was a strong quarter. During the quarter, we delivered organic growth, sales development around 15% and organic above of 8%. But, in particular, we expanded the margin and the earnings by 65%. So, we delivered a profitable growth. It's another step towards our financial target, an important step that is bringing us closer to the target that we have.

Result was achieved, we have to say also despite the performance of an area that we expect to be the most profitable one, the North America Food that reported a decline in sales and a good margin, but a margin below our expectations. We said also that the comparison with 2022 has to consider that last year in Q2 we had the items that have been affecting the comparability, like the divestment of the Russian operation accounting for SEK 35 million. And also during Q2, the Laundry business suffered. Laundry business, in particular, the overall business was suffering because of the supply chain challenges, but in particular, it was Laundry that was affected by missing production. We had to stop production for missing component in May. It went through for some weeks where we were not able to complete the product. So, we produced, if you remember, product with the missing electronic boards and then we started to deliver them in Q3. So, in some way, we have been missing business that we estimate with an impact of roughly SEK 30 million negative in Q2.

So, even if adding these two items to the 2022 numbers, the 2023 performances in Q2 are showing up profitable growth, a profitable development. The third element of the financials is obviously the operating cash flow and we had a strong generation of cash in Q3. That is, by the way, normalizing the performance for what cash generation is concerned. Last year was affected by a relatively weak cash generation during the first three quarter of the year. This year, we started the year already much better. In Q1 and in Q2, we are at a normalized level confirming that this is a company that can generate more than 100% cash conversion.

If we move now to the analysis of the different dynamics in the different geography, in the different regions, we have to say that – you see that we have basically the Americas positive, Europe positive, and flat Asia-Pac. Let me start from Asia-Pac because, again, it seems to be the area where we did not grow. Reality is that in that area last year we delivered very large project in Uzbekistan. You have to consider that the project in Uzbekistan that was that both for Laundry and Food delivered in the second quarter of last year accounted for roughly 15% of the total sales of the region. So, if I'm excluding that one, also that region is growing significantly the business along the year and in particular in Q2. Food was [indiscernible] (00:04:37) in China even if below our expectation and India. Again, food was the one affected by the Uzbekistan as well as Laundry, but mainly Food. More than two-third of the Uzbekistan project was Food. Beverage was good all across the regions and Laundry, again, all across the region, in particular, again, India and China.

Now, Europe, a very strong performance in Europe, in particular, Beverage and Laundry that we have been growing all across the different countries in Europe. Clearly, Beverage is the season high quarter. So, very important to do strong in such a way. Food grew a little bit less than Beverage and Laundry, but still very good performance in the Mediterranean area. Mediterranean area, we call the Hispanic or the [indiscernible] (00:05:36) region, Greece, Turkey. And remarkable performance also in Finland, where we completed pretty large projects.

The region with the larger gap, let me say or differences in [indiscernible] (00:05:57) is United States, where we had the Laundry performing super well, while Beverage was slightly positive and Food was negative. And, again, I'm repeating here the comments that I made during the Q1. In North America, we experienced a declining demand of our product in relation to the stocking of our distributors. It is in particular related to the distributors that are selling the refrigerators that they've been destocking since the beginning of the year. We see some positive sign with the new orders coming that we saw this happening at the end of June and continuing into July.

So, let's now have a deep dive in the two segments, starting as usual from the Food & Beverage. Overall, Food & Beverage was organically growing 0.5%, so a flattish business. Again, remember the Uzbekistan project that was pretty large and we delivered it in Q2 with a good performance in Europe, while, again, the sales decline in the Americas, comments already made and in Asia with a reference to be considered about the Uzbekistan project. In particular, Beverage within the Food & Beverage was very good. Beverage was the one suffering the most years ago during the pandemic and it is the one recovering more than any other on these years.

China grew, yes, double-digit growth, but is less than what we were expecting because the recovery and the reopening of the Chinese market is slower than expected. Margin improved significantly, so the profitability improved and it was mainly, thanks to the price and the mix up, thanks to customer care where in our operation we grew the participation. Participation means customer care sales versus the total sales of the company and we grew the participation of the customer care business to the total sales.

If we go to Laundry, Laundry performance were really strong. But, again, we have to look at the comparison. There was also the Uzbekistan project inside. Indeed, sales were super strong in Americas, in Europe. In Asia-Pacific, they were single-digit growth compared to the double-digit in the other two region. But, again, in Asia, we had the Uzbekistan project who was the leader in there. In this case, also the margin grew more than 100% that is

good clearly and is driven also for price, but in this case also volumes. So, volumes had a very positive effect on the Laundry business.

Two comments about the Laundry, two additional comments in addition to the fact that, again, the comparison with last year has to consider also the fact that in Q2 we did not sold a lot of product because we produced [ph] incomplete (00:09:53) units that are being recovered in Q3. So, there been a sort of shift of business from Q2 to Q3 last year. We said that that the impact in the earnings is roughly SEK 30 million. In addition to that one, I think it has to be mentioned a comment between the Q1 and Q2 of this year, where in reality we had a super strong March in Q2 and a relatively weak in April that normally they should be normalized. March was an extremely long month and April extremely short month. So, I would look at the two quarters together with a normal progressive development of the business in Laundry.

The other element in Laundry is also that we increased, in particular in Q2 with a catch-up versus Q1 again. So, we should divide between the two quarter the R&D investments because we started a very important project to renew the [ph] architectural or some line (00:10:58) in the Laundry portfolio.

With this said, I would like now Fabio going deep into the analysis of the financial performances.

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## Fabio Zarpellon

*Chief Financial Officer, Electrolux Professional AB*

Thank you, Alberto, and good morning to everybody. As you have seen from the financial data, since quarter two 2021, supported also by the market recovery, we have been consistently increasing both the top line and the EBITA performance compared with the previous year. And this, let me say, pattern of consistency – positive consistency improvement, I believe, it is beside that such an important pattern of our development. In quarter two, we generate close to SEK 400 million in EBITA and a margin over 12%. Also, here, consistent improvement, both in Food & Beverage where we are over 12% and in Laundry where we are over 16%.

The value increase in EBITA was roughly SEK 150 million. Alberto mentioned that in the comparison we need to consider that last year we had SEK 35 million one-time costs related to divestment of the business in Russia and the disruption of the supply chain that we had in Laundry affected the profitability in quarter two of last year for roughly SEK 30 million. But even excluding these couple of items, the improvement as being roughly SEK 90 million, so plus 40% that I consider really a remarkable improvement. Back to the comment of we are growing, but we are also growing profitability.

EBITA was increased, thanks a combination of higher gross margin, but also lower selling, administrative expense on sales. We have expanded the gross margin value by 19%, higher than sales. This increase was driven by price, more than compensated in the quarter and also year-to-date, the inflationary items. The volume growth in Laundry, the mix-up of customer care, these were the main driver of the gross margin increase.

Also in the quarter, happy to report that with the stabilization of the supply chain, also the logistic cost have been decreasing quarter-on-quarter. Selling, administrative expenses increased in the quarter in value also because of inflationary item. But the weight on sales has been reduced by roughly 1 percentage point, meaning that we are growing profitably getting also productivity improvement of our organization.

And this result has been achieve whilst continuing to invest in innovation and the digitalization of the company. This is, I believe, an important also things to consider because we are growing profitably, but we are also investing to create the condition for a sustainable, profitable growth also going forward.

Coming out from the EBITA, a few words about the financial net. Financial net in the quarter was SEK 24 million, lower than the level of quarter one. It has been help by reduced level of funding, but also, we had a positive contribution from currency transaction in the not SEK denominated deposit.

The tax rate in the quarter was 20%, below the average. At the same time, also to give you a sort of guidance, I expect that for the quarters to come, to go back to the guideline we gave in the past of around 25% of tax rate on the income. The income for the period was closer to SEK 260 million. Earning per share at SEK 0.89 per share. Also, here, a remarkable result, we doubled more or less the net income compared with the last year quarter two.

Then a few words about the cash flow. Alberto already mentioned it earlier. We are back or what we say is normalized cash flow. This group historically has been a strong cash generating group. The level of operating cash flow has always been above the EBIT and EBITA generation. And, also, this quarter, I will say after, let me say, a good quarter one, we further improve the cash flow despite the additional requirement we had on the operating working capital.

Few words on the CapEx in the quarter. The level of CapEx has been relatively low this quarter, but I expect is going to normalize to historical spending in the quarter to come. I mentioned operating working capital development. Year-over-year, operating working capital increased by 20%, 5.56 points are currency translation related and the rest is increase of the operating working capital value, also related to the pricing that is affecting the value of our goods, but also the value of our receivable.

Here to be said that I consider somehow we are reaching the peak of the operating working capital in term of weight on sales. And now, I believe that with the stabilization that we have in the supply chains, we have finally the conditions to work on improving the operating working capital, in particular, around the inventory side. Yes, we have now the condition to review the safety stock, for example, of finished product or the size of purchasing for what concern the component, bringing down the inventory to a normalized level.

When it comes to the receivable, as I reported in the previous quarter, the situation is pretty good. I believe we have the historical low past due on sales than ever. Overall, you see our financial position is pretty solid. We reduced [indiscernible] (00:18:27) net debt on EBITDA at 1.3 times. So, significant down compared to the level we had in December. In the quarter, we have repaid another part our term loan, we repaid €15 million on top of the €35 million we repaid already in quarter one. So, overall, €50 million repayment in funding in two quarters.

We started quarter three with a strong liquidity. We have over SEK 700 million in liquid fund and SEK €200 million revolving crediting facility fully available. I mean, overall, as a conclusion, solid quarter, overall good profitable growth and a pretty stronger balance sheet.

And with that, let me say I'm really – look at the – this group with a solid group with really also from a funding perspective, the condition to support the profitable growth.

And with that, back to you, Alberto.

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## Alberto Zanata

*President & Chief Executive Officer, Electrolux Professional AB*

Thank you, Fabio. And now, I – when I started, I said that we have been making another step towards our financial targets. But I'm also proud to say that we are making other steps towards our overall goals. The overall goals to be the most sustainable company in this industry. And this is also certified by external institutes that are right in this company highly for what concern the sustainability objective.

And in this case, I'd like to report that in the Q2, we did another step towards the reduction of the CO2 emission. We have a target to be carbon neutral, and we are making these steps quarter-by-quarter because these are things that we can achieve also through one-by-one step. And we made another step. And I have also to say that we are ahead of our plan. So, we can do better. Everybody can do better for the environment, for the sustainability of our business.

Sustainability is not only obviously reducing the CO2 emission of our operation, but this also means to bring to market product that are sustainable, that are reducing the impact of the utilization of this product, the utilization made by our customer of this product. And during the Q2, we brought a new product to market. We brought the high-speed oven, call it, the GourmeXpress, that is a product targeting the customer care – sorry, the chain customers, because is small, flexible, rapid, so fast cooking and save energy, save energy for the operation of our customers.

So, we continue to bring – we continue [indiscernible] (00:21:57) to invest, to develop innovative solution with a target to bring to market sustainable solution for the operation of our customers. And this is, I believe, we mentioned the other quarter, the other product that we were in testing with other chains, that is the [ph] HeroDry (00:22:14). The HeroDry was under test in Q1. And now, we will be launching in Q2. And it is another product targeting customer needs, solving problems, but also reducing the operations – the running operation.

With this said, I would like to conclude – to conclude or to summarize the quarter saying that we deliver profitable growth. It is another steps towards the financial targets, but as I mention just recently, not only the financial target, but the overall goals of this company.

We improved significantly the margin and the earnings. And the market – this development was supported by a quite positive market demand with the exception of what was mentioned in the United States – in the United States. The order intake was good all along the quarter with the exception of North America, again. And, freshly, also the amount today order intake – because of the order intake in July is positive and, in this case, is positive also in North America.

We continue to invest to bring new product. We will continue to invest in new product. I mentioned earlier the increase of the R&D spending in Laundry. Laundry is the most profitable business, is a high margin business, is a business where we have been leading the market historically also, thanks to the innovative solution, sustainable and innovative solution of our Laundry appliances. We continue to invest and we are planning to bring additional solution to market.

We are currently sitting on a good order stock. We are talking about roughly two months. So, it is lower than the one we had last year. Absolutely, yes. But I said more than once that the last year order stock was unhealthy because it was an order stock that was, let me say, boosted by orders of customer that were placing order even if they didn't need the product just because they were afraid not to have it on time or when was needed. And it was also boosted by delays in production that were leaving product in inventory just because we were not able to deliver the complete package.

So, it is lower than last year, but today is a healthy order stock. There are some projects inside, yes, as usual. This is a company that is very strong in projects. We are, remember again, the only company that under one brand is able to deliver a full project for kitchen, beverage and Laundry solution. The Uzbekistan case that I mentioned earlier is one example.

So, we have some projects that we should deliver by the end of the year. They could go into 2024. But at the same time, we have more than two months of order stock. With an order intake that has been relatively good, recovering little bit also in the United States in July. So, this is the reason why, similarly to what we said in Q1, we are cautiously optimistic, cautiously because we see what is happening around us and we have to consider all the things that are happening in the environment where we operate.

With this said, back to you, Jacob.

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## Jacob Broberg

*Chief Communication & Investor Relations Officer, Electrolux Professional AB*

Thank you, Alberto. And with that, we open up for questions. Please go ahead, operator.

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## QUESTION AND ANSWER SECTION

**Operator:** We will now begin the question-and-answer session. [Operator Instructions] The first question is from Gustav Hagéus from SEB. Please go ahead.

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### Gustav Hagéus

*Analyst, Skandinaviska Enskilda Banken AB*

Q

Thank you, operator. Good morning, guys. Thanks for taking my questions. A few from me. If I may start with that – if I understand correctly that R&D or your development projects that was ongoing and was allocated some costs in the Laundry division in Q2. Could you elaborate a bit? Is that something that is also going to carry into Q3 and affect margins, or was that isolated to Q2?

And when looking at Laundry margins into H2, do you think Q1 or Q2 margins for Laundry are better proxies for what to expect in the second half?

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### Fabio Zarpellon

*Chief Financial Officer, Electrolux Professional AB*

A

I may take the question. First of all, what concern the R&D cost in quarter two for Laundry, we needed to consider that there was a sort of a catchup of spending also compared with the quarter one. Going forward, I expect their R&D cost to – that we continue to invest in term of R&D to keep the premium position that we have in the market, but the increase will not be at the same level we have seen in quarter two this year.

For what concern the margin development going forward, I believe that we needed to look at the current performance of Laundry, putting together quarter one and quarter two. I believe that this is, I will say, a good proxy of the underlying business [ph] development (00:28:31) and profitability of Laundry.

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### Gustav Hagéus

*Analyst, Skandinaviska Enskilda Banken AB*

Q

All right. So, that's helpful. And then, I'm curious on the working cap. Obviously, a very strong organic – or operating cash flow in the quarter. And saying that working capital sales has peaked now, is obviously positive. But given that your history is a bit volatile coming out into COVID – in the midst of the COVID and so forth, it's hard to sort of extrapolate. What would you consider to be an optimal inventory level for you as things stabilize in relation to sales or in absolute terms that would be helpful?

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**Fabio Zarpellon**

*Chief Financial Officer, Electrolux Professional AB*

A

Okay. For what concern the – let me comment the overall working capital and then spend a few words on the inventory. First of all, our financial target in term of operating working capital on sales is to be in the area of 15% or below. I believe, we have the ingredients to achieve this target over time.

When I look into our development and the reason behind the increase of the operating working capital, is not related to receivable. I mentioned earlier that the quality of receivable is, I will say, pretty good, pretty solid, is not related to account payable where we are actively, consistently with history. The deterioration came from inventory.

Now, with the stabilization of the supply chains, I believe we have the condition now to work into this area, reducing the inventory level wise, maintaining or even improving the weight of inventory on sales. It's clear that this will require time, but I've seen already in quarter two this year, even if it is not visible in the trend, but tiny, but we have had a reduction of the inventory value quarter-on-quarter at the same currency rate. So, it will come. It will not come faster. But we will start to see the benefit already in the second part of the year.

**Gustav Hagéus**

*Analyst, Skandinaviska Enskilda Banken AB*

Q

And sort of a number or a range where you would be happy in terms of inventory as of end of the year?

**Fabio Zarpellon**

*Chief Financial Officer, Electrolux Professional AB*

A

Inventory, our expectation according to the plan is that we will bring down the inventory compared to the level we have today. So, the guidance will be towards what, I will say, even lower to the level we had at the end of last year.

**Alberto Zanata**

*President & Chief Executive Officer, Electrolux Professional AB*

A

Also to consider that if [indiscernible] (00:31:36) compare the inventory value, because one thing is the percentage that is fine, but the inventory value and the product today are – they have a value – unitary value much higher than the one that they had in 2019 and because of the increase of the cost of material. So, it is more important that that is what we are looking for. We are looking at the percentage because if we increase pricing, we increase the cost of the material. Because if we just look at the pure cost of the single product, it is much, much higher. The value of the inventory, same number of item. The value of the inventory is higher than the one we had pre-COVID.

**Gustav Hagéus**

*Analyst, Skandinaviska Enskilda Banken AB*

Q

Yes, that's reasonable. And that sort of feeds into my last question on pricing and so forth. Is it fair to assume that you had mid-single digit or high-single digit contribution in the quarter from price increases? And then a follow-up on that. We're starting to hear enough from some companies that perhaps not in your sector, but related sectors that they see prices coming down net year-over-year in H2. Do you see and do you hear any discussions with your partners on the price pressure or that perhaps inflationary environment will translate to more campaigns and so forth from your end?



**Alberto Zanata***President & Chief Executive Officer, Electrolux Professional AB*

A

No. No, we don't. First, yes, prices positively contributing, yes. But we don't see this – we don't see price coming down yet, at least. Even if I have to say that this is an industry where rarely I saw that one. For sure, in particular with large customers, there are discussions about the price. But still the impact or the delta between price and material is not a situation where we are entertaining this kind of discussion.

**Gustav Hagéus***Analyst, Skandinaviska Enskilda Banken AB*

Q

And follow-up on that, if I may. On costs from your end, in terms of freight costs, land freight, ocean freight, external factors...

[indiscernible] (00:34:10)

**Gustav Hagéus***Analyst, Skandinaviska Enskilda Banken AB*

Q

Is that going to be a benefit for you in H2 versus H1 or is it going to be a...

[indiscernible] (00:34:17)

**Alberto Zanata***President & Chief Executive Officer, Electrolux Professional AB*

A

Yes. There will be a benefit in transport. We see clearly the cost, container cost, [ph] transportation (00:34:24) cost going down as well. For instance, last year we had a surcharge to cover the transportation cost, the energy cost, and we are not applying that one anymore because I cannot apply to customers something that in reality is going back to normality.

**Gustav Hagéus***Analyst, Skandinaviska Enskilda Banken AB*

Q

Yeah. And just to be totally clear that surcharge that you had, including that, do you still see prices going up net, including campaigns and surcharges and whatnot in H2?

**Alberto Zanata***President & Chief Executive Officer, Electrolux Professional AB*

A

No, the surcharge, they were last year. And we closed the surcharge at the end of 2022, in some cases converting them into pricing in the country or in the situation where there were inflationary item that were clearly too high. But other than that, I repeat, we are not applying the surcharge anymore to any customer anywhere. So, we will benefit from the reduction of the transportation cost during the second part of the year.

**Gustav Hagéus***Analyst, Skandinaviska Enskilda Banken AB*

Q

Yeah, yeah. No, my question was the total price paid by the customer may seem surcharge or list pricing or campaigns that is still higher year-over-year in H2 versus last year, right?

**Alberto Zanata**

*President & Chief Executive Officer, Electrolux Professional AB*

A

Yes.

**Gustav Hagéus**

*Analyst, Skandinaviska Enskilda Banken AB*

Q

Yes. Perfect. Thanks for taking my questions.

**Alberto Zanata**

*President & Chief Executive Officer, Electrolux Professional AB*

A

Welcome.

**Operator:** [Operator Instructions]

**Jacob Broberg**

*Chief Communication & Investor Relations Officer, Electrolux Professional AB*

A

Jacob Broberg here. I have one question from the web. Will you be able to use the somewhat soft US Food & Beverage market to do value-creating M&A? And do you see a strong M&A pipeline?

**Alberto Zanata**

*President & Chief Executive Officer, Electrolux Professional AB*

A

We are looking at M&A as usual. So, we continue to monitor the [audio gap] (00:36:37) priority. But it is not the only area where we are looking at possible acquisition. The balance sheet is stronger. The net debt, the ratio between net debt and EBITA is going down. So, there are all the condition to possibly entertain discussion with companies. Obviously, I cannot comment more than this. I would not relate the softening of the US market with more possibility in term of M&A, at least this is the experience that we had also during the pandemic. It's not that because of the market is weaker that more companies are coming to market. I didn't see this one happening. So, I will not relate the two things, but we continue to look at the possible acquisition.

**Jacob Broberg**

*Chief Communication & Investor Relations Officer, Electrolux Professional AB*

A

Thank you, Alberto. I don't know if we have any more questions, operator?

**Operator:** There are no more questions from the phone.

**Jacob Broberg**

*Chief Communication & Investor Relations Officer, Electrolux Professional AB*

Okay. If we have no more questions, I hope everything was very, very clear. So, with that, I say thank you for today and have a good day and summer. Thank you and goodbye.

**Alberto Zanata**

*President & Chief Executive Officer, Electrolux Professional AB*

Thanks to everybody.

## Fabio Zarpellon

*Chief Financial Officer, Electrolux Professional AB*

Thank you.

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## Alberto Zanata

*President & Chief Executive Officer, Electrolux Professional AB*

Thank you.

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