Good morning, ladies and gentlemen. Thank you for standing by. Welcome and thank you for joining the Q3 2022-2023 Earnings Call of ABOUT YOU. (Operator Instructions)

It's my pleasure and I would now like to turn the conference over to Frank Bohme, Head of IR and Communications. Please go ahead, sir.

Frank Böhme - ABOUT YOU Holding AG - Head of IR & Communications

Thank you. Good morning, everyone, and welcome to our third quarter 2022-2023 results presentation. Today's conference call will be hosted by Hannes Wiese, Co-Founder and Co-CEO of ABOUT YOU. Hannes will walk you through our Q3 results in just a second. The corresponding slides to this presentation have been published on our IR website under the Publications section this morning. After his presentation, Hannes will be happy to answer your questions.

And with this, I hand it over to you, Hannes.

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Thanks, Frank, and good morning to everyone also from my side. Today as usual, we are focusing on the following topics: update on our business, financials, outlook and Q&A. Let's directly jump into the business update starting with the key takeaways of the third quarter '22-'23. Despite a continuously unfavorable macroeconomic environment, we managed to grow our top line by 8.3% year-over-year reaching EUR 555 million in revenue in Q3. The number of active customers of the commerce segments increased by 17.4% in the last 12 months. For Q3, DACH revenue growth came in at 8.2% and Rest of Europe at 11.1%. TME, our B2B segment, increased profitability to a 15.6% adjusted EBITDA margin in Q3. This is as the continued growth of B2B revenues scales against the predominantly fixed cost base. Adjusted EBITDA came in at a negative EUR 43 million.

Profitability was impacted by investment commitments and strategic growth initiatives and the low gross margin resulted from elevated inventory levels leading to high discounts in a heavily promotional environment. Today, we confirm our guidance for the full year '22-'23. However, due to the difficult macroeconomic environment and considering the revenue and profitability development in Q3, we now expect revenue growth and adjusted EBITDA to come in at the lower end of the guided ranges. Let's now take a closer look at our trading against the current market backdrop. The macroeconomic environment remained challenging in the third quarter, the inflation in the Eurozone peaked and remains on elevated levels. Consumer confidence reached a historic low in September and has only slightly improved since then. Withstanding these headwinds, we were able to grow our revenues by 8.3% year-over-year. This corresponds to a 27% CAGR over the last 2 years and a 3-year CAGR of 35%.
This is a clear outperformance of the overall market and underlines the resilience and strength of our business model. To navigate the current market situation and to support our break-even target in FY’23-’24, we are selectively slowing down growth investments as planned. First positive results are already visible in Q3 so let me give you 2 examples here. After years of constant headcount growth for the company, Q3 marks the first quarter with a slight decline in the number of FTE as we are adjusting our headcount particularly in non-tech areas. Also, our inventories remained flat quarter-over-quarter following a strong build-up phase over the last years. In an environment where demand is generally lower than expected, this was achieved through various measures in cooperation with our suppliers as well as dynamic pricing and campaigns to clear inventories.

Some examples of these sales campaigns are shown on the left-hand side of this slide. They include our Appy Birthday campaign celebrating the anniversary of our market entry in respective markets. For the first time, we also started a fear of missing out or so-called FOMO campaign providing discount vouchers to those users who interacted with us on Instagram during the campaign. And we ran our Black Friday campaigns with unusually high discounts in a highly promotional market environment. These sales campaigns had a positive impact on new customer acquisition and revenue generation in a difficult market. They, however, also came at the price of a gross margin impact of around three percentage points in Q3. Last quarter was also characterized by large scale branding campaigns, which were planned and committed back in 2021. On the one hand side, we see these campaigns as large successes against their initial targets.

ABOUT YOU Fashion Week in Milan generated billions of media contacts and strengthened our reputation in the fashion ecosystem on a global scale. Our exclusive collection campaigns with international top tier celebrities like Bella Hadid or Katy Perry generated record new customer numbers and strengthened our image as a unique fashion assortment destination. On the other hand, we have to acknowledge that these long-term brand investments are not suitable for the current market environment. The estimated impact on marketing costs of around EUR 25 million is not in line with our tightened ROI targets and we hence do not plan such large-scale branding campaigns for the next year. This is also a good segue into our next slide showing our bridge to achieve adjusted EBITDA breakeven in ‘23-’24. Reaching this breakeven remains our top priority so let’s go through the key levers to achieve this goal.

Starting with the gross margin, which is significantly under pressure this year due to elevated inventory levels and a highly promotional environment. We expect a cleaner inventory position going into ’23-’24 as we adjusted our Spring-Summer ’23 orders to the current demand levels, which should ease pressure on gross margin next year. Further, we are implementing a new commission scheme for our 3P model as a function of the selling price and return rate per item and this results in a positive effect on the gross margin and an extended assortment for customers. Moving on to fulfillment costs, which are currently impacted by inflationary dynamics, the expansion of our European distribution network and increased inventory levels. To counter some of these effects, we are now introducing shipping costs below minimum gross order value. First markets are already live, and we plan a complete European rollout over the next months.

This will be followed by the planned introduction of further measures to support unit economics over the course of ’23-’24. Another tailwind for the fulfillment cost ratio is expected from reduced ramp-up costs compared to ’22-’23. This is as our new DCs are either already live or in late implementation stage today. Coming to marketing costs, which are expected to significantly decline in ’23-’24 providing the largest efficiency lever compared to this year. As discussed on the previous slide, large scale events and branding campaigns will be reduced. Further, there won’t be any major new market entries, eliminating big bang and market entry investments as our newer markets can now scale from a solid base. On top of that, the full effect of globally tightened ROI targets will become visible on a full year basis next year. Lastly, admin expenses will benefit from operating leverage as we further grow the business and continue to see the positive results from our operating efficiency measures.

Moving on to some organizational changes, which we have initiated around SCAYLE. SCAYLE continues to show a very strong business performance. Encouraged by this, we are now in the process of spinning off the tech part of our SCAYLE business into a separate legal entity within AY Group. With this, we want to create the optionality to better crystalize value for SCAYLE in the future and we want to give more structure and operational separation for the different business lines. Further to this, we have also started the process to spin-off our payments unit into a separate regulated legal entity within AY Group. We are doing this to create monetization opportunities around payments and we want to be able to offer fully integrated marketplace services to our SCAYLE Tech clients. This will be an additional feature on top of the already comprehensive USPs for SCAYLE. The timeline to implement this new setup is around 1 to 2 years.

Related costs for the separation will be treated as an adjustment item. We expect these to be in a single-digit million range for each ‘22-’23 and ‘23-’24. Let’s now move on to the financial update. On top line, all segments were growing with a broadly similar rate despite the difficult market conditions.
environment. But let’s start with the Group trading on the left-hand side of this chart. We grew our revenues by 8.3% in Q3, which corresponds to EUR 555 million in revenues. This growth rate is below our own ambitions. Q3 revenues, however, were negatively impacted by a difficult macroeconomic environment and the consumer sentiment on historic lows. Let’s take a closer look at our segments to analyze this. Starting with DACH where revenues increased by 8.2% in the third quarter. The development of revenues in the DACH region was twofold. In Austria and Switzerland, ABOUT YOU continued to grow strongly and gain considerable market share.

The German market, on the other hand, was more difficult and reported slower growth particularly due to a very negative consumer sentiment and high inflationary dynamics. In the Rest of Europe segment, revenue was up by 11.1% in Q3. The Nordics and Benelux countries developed positively and in line with expectations both in top line and contributions. Southern and CEE markets, however, suffered from low consumer sentiment as well as a highly competitive and promotional environment. Moving on to our TME segment where revenues grew by 9.5% in the third quarter. This increase is largely driven by the successful brand positioning of SCAYLE and the onboarding of new clients. However, our recurring revenues from existing scale customers continue to be muted to declining. This is as many of our B2B customers continue to see their own online revenues affected by the difficult market environment and are confronted with strong comps from last year.

Furthermore, we also continue to observe a relatively low spending willingness among B2B customers. This creates a challenging environment especially for our media and marketing services. Moving on to our customer engagement metrics for the Commerce segments. We were able to grow our active customer base to 12.5 million in the last 12 months. This is a healthy increase of 17.4% versus last year. Net adds and active customer numbers for the Q3 were, however, below expectations. This is because customer reactivation and acquisition was challenging for us in a highly promotional and transactional market environment. For instance, we’ve seen more need-based categories like men casual and sportswear perform better in the current environment than more discovery-led categories like women trend and occasion wear. The average order frequency per active customer still increased by 5.5% in the last 12 months.

This increase is the result of the expansion of the product range, the improved customer experience and increase in brand awareness and age structure effects of the customer cohorts. The average order value declined by 6% in the last 12 months. This development is driven by increased discount levels as well as higher return rates compared to the previous year. If we look at the basket dynamics in Q3, we see that AOV is slightly down year-on-year, but the decline is smaller than in the last 12-month perspective. So, the downward trend observed over the last year seems to be slowing down. With that, let’s move on to our bottom line, which continues to be under pressure. This is due to macro factors, elevated inventory levels, and committed growth investments. Let’s start again on the left-hand side of this chart showing our Group adjusted EBITDA margin. We grew our revenues by 8.3% in Q3, which corresponds to an adjusted EBITDA margin at a negative 7.8% in Q3 ’22-’23 versus a negative 6% last year.

Adjusted EBITDA development in Q3 is characterized on the one hand by revenue growth creating continued operating leverage and an improved marketing cost to revenue ratio. On the other hand, this development is contrasted by a low gross margin and elevated fulfillment costs. Our DACH business was also burdened by these factors. The adjusted EBITDA margin in Q3 ’22-’23 declined to a negative 1.6% compared to 5.5% last year. The decrease mainly resulted from a higher level of discounting, which was necessary to clear inventory in a highly promotional environment. Further to this, DACH is also showing a higher fulfillment cost ratio than last year. This is mainly driven by higher returns as well as inflation and network related cost increases. Moving on to our RoE segment where we slightly lowered our investments year-over-year, but adjusted EBITDA margin is still at a negative 17.6%.

The main drivers for these losses were high discount levels to clear inventory, elevated fulfillment costs related to the logistics network expansion, and the discussed commitments in international brand building campaigns. Improved EBITDA compared to the prior year quarter resulted from the lower scale of market entry campaigns in new markets, which negatively impacted our RoE EBITDA especially in Q3 last year. On B2B, our TME business achieved an improved adjusted EBITDA margin of 15.6% in Q3, up from 14.6% last year. Margin increase is the result of the growth in B2B revenues, which scale against the predominantly fixed cost base. Further, our TME margin benefited from revenue mix effects and cost discipline. Let’s now take a closer look at the key cost lines of the group. Starting with the gross margin where we saw a decline of 3.5 percentage points to 35.4% in Q3. This was mainly driven by sales campaigns and high discount levels, which were necessary to clear inventory in a highly promotional market environment.

Our high margin B2B and own label revenues were only partially able to offset these negative effects. Next our fulfillment cost ratio, which is at 23.4% in Q3. Fulfillment costs were lower by 5.1 percentage points quarter-over-quarter, which is due to seasonality and cost measures. But our
fulfillment cost ratio still increased by 4.6 percentage points year-over-year coming from 18.8% in Q3 ’21-’22. The year-on-year increase is attributable to several factors. First, as expected, we are seeing an increase in return rates towards pre-COVID levels. Second, logistic costs face pressure from inflationary dynamics. Third, the expansion of the European distribution network creates nonrecurring costs and operational complexity. Fourth, the lower-than-expected revenue levels continue to cause underutilization in our DCs. And finally, increased inventory levels lead to a temporary increase in processing costs.

The year-on-year increase in the fulfillment cost ratio in Q3 ’22/’23, therefore, continues to be a mix of temporary effects, which are expected to ease in the coming quarters and structural effects, which are expected to persist over a longer time horizon. Let’s move on to our marketing costs. The marketing cost ratio declined to 16.4% in Q3, down 4.9 percentage points compared to last year. This is the result of 3 factors. First, the fade-out of large-scale market entry campaigns, which negatively impacted marketing costs particularly in Q3 ’21-’22. Second, a more conservative steering of online marketing channels with tightened return on investment targets. And third, cost discipline and process improvements across marketing functions. Despite these factors, marketing costs are still elevated in Q3 ’22-’23. This is due to the commitment to international brand building campaigns, which we discussed in the business update section.

Based on the success of these and previous campaigns, the necessity for brand building measures particularly in newer markets will continue to decline in the coming quarters and this should lead to a further improvement in marketing costs. Lastly, our Admin and other cost ratio declined by 1.4 percentage points despite a generally high level of inflation. This is due to continued operating leverage, peak revenues in Q3 as well as positive effects from our overhead efficiency measures. All the sectors combined resulted in a decrease of our Group adjusted EBITDA margin by 1.8 percentage points to a negative 7.8% margin in Q3 ’22-’23. Let’s now take a look at our cash flow drivers. Our net working capital returned to negative territory ended at a negative EUR 7.3 million at the end of Q3. However, we are not yet back at the working capital efficiency levels, which we’ve shown the last year. This is because our stock turnover is still not where it should be as a result of slower-than-expected top line growth.

CapEx amounted to EUR 15 million in Q3. The majority of CapEx went into our growing IT and logistics infrastructure as well as joint ventures with influencers and incubators. Moving on to our cash position. Let us first look at our operating cash flow, which is at a negative EUR 17.8 million in Q3. This is as the positive net working capital dynamics were able to offset some of the EBITDA losses in Q3. CapEx translates into investing cash flow and our financing cash flow is at a negative EUR 9.2 million in Q3. Financing cash flow is driven by payments for leasing agreements largely relating to our DC network rollout. We ended the quarter with cash and equivalents of EUR 306 million. While this is still a comfortable cash position, we are continuously evaluating different measures to optimize liquidity. This is done in order to be able to grow with sufficient liquidity buffer also through a potentially longer period of macroeconomic uncertainty.

We are looking at a broad spectrum of measures here as a matter of prudence in the current market environment and to determine an ideal capital structure for the next years. Let’s now move on to the final section of the presentation, the financial outlook. We confirm our guidance for the financial year ’22-’23. However, due to the difficult macroeconomic environment and considering the revenue and profitability development in Q3, we now expect Group revenue growth and adjusted EBITDA to come in at the lower end of the guided ranges. For group revenue, we hence expect growth at the lower end of the 10% to 20% guided range. For our group profitability, we expect adjusted EBITDA to come in at the lower end of the negative EUR 120 million to a negative EUR 140 million range. CapEx expectations continue to be around EUR 60 million to EUR 80 million and net working capital is expected to be neutral towards the end of the financial year ’22-’23.

I would like to finish this presentation by thanking you all for your time today and for your trust in us to maneuver through these challenging times. I’m now looking forward to answering your questions. So, moderator, let’s start.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is from Nizla Naizer from Deutsche Bank.
Fathima Nizla Naizer - Deutsche Bank AG, Research Division - Research Analyst

I just had a question on sort of how Q3 started and ended. If you can give us some color as to individual months what was the take-up like et cetera, how did you exit November? Maybe some color over how Christmas trading was going. Some color there would be greatly appreciated. And my second question is then linked to the implied Q4 where to reach the low end of the guidance, we're looking at 3% year-over-year growth and maybe minus 6% margins or around EUR 25 million of losses. So that's a clear sort of improvement from Q3 when it comes to profitability. Could you give us some color there as to why maybe growth would be slower than Q3? Is that implying some conservatism? Some color there would be fantastic.

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Thanks for the questions. Starting with the shape of Q3. So we've seen a good start into the quarter so September growth looked quite good. We had a good start into the Autumn-Winter season and then October was more muted, I would largely relate this also to weather patterns. So we had quite warm weather across Europe and this more like muted environment for us stayed until beginning to mid of November. And then with colder weather patterns and Black Friday precampaign starting, trading and growth picked up again and we exited November with a growth rate that was broadly in line with the growth for the full Q3. And since then, trading remains volatile.

We haven't materially improved growth in December versus what we've seen in Q3. And given the high level of volatility and uncertainty, we also want to preserve a certain level of cautiousness for the full year guidance as you inferred from the Q4. We can confirm that we are relatively cautious given the volatility and uncertain environment that we see for top line. And for bottom line, we definitely don't want to over-invest in these times and hence also expect lower investment especially on the marketing side, which should give or lead to the lower end of the guided range also for the adjusted EBITDA.

Nicolas Katsapas - BNP Paribas Exane, Research Division - Research Analyst

Thanks for a very comprehensive presentation. I have 2 sort of areas for questions, might amount more than 2 questions. But the first one is gross margin. So I understand that your gross margin was weighed on by your own sales campaigns. But could you give us a sense of that in the context of the market, were you more or less promotional than the market? And then maybe if you could expand on how much B2B or mix was in the 3.5% net decline in gross margin? And I'll ask the second set of questions after that.

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

So the gross margin development I think relates to both a promotional environment and consumers seeking for discounts actively especially in the period around Black Friday, which caused also a market-driven need for higher discount on the ABOUT YOU side and then certainly also a higher need to clear inventory driven by our own elevated inventory position. So we also had to be aggressive in the base pricing also aside from the mentioned campaigns. And whether we were more or less aggressive than the market, that's hard to say. Honestly, I would think this plays out different by region.

In some regions, we have perceived competitors or the market more broadly as being more promotional than what we offered and others maybe the other way around. And the mix over the last quarters, we've seen support on the gross margin from increased share of especially B2B revenues and also own labels. That hasn't materialized to such an extent this quarter given that our B2B segment has grown at a broadly similar rate as the commerce segments and same also is true for our own labels. So there weren't substantial mix effects coming into play.
Nicolas Katsapas - BNP Paribas Exane, Research Division - Research Analyst

Great. That's very clear. The last question is just to confirm. You mentioned that the restructuring costs for splitting the business for payment and scale. I heard FY '23 and FY '24 low single-digit million. I presume that means OpEx and can you confirm whether that's in the guidance already for FY '23?

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Yes, it's single-digit million not low single-digit million and we are adjusting OpEx, that's correct and that's factored into the guidance already.

Operator

The next question comes from Anne Critchlow from Societe Generale.

Anne Critchlow - Societe Generale Cross Asset Research - Equity Analyst

I've got 2 questions, please. First of all, you mentioned the new commission scheme for the brands. I just wondered what that entails and how it's different. And then secondly, if you could talk about the liquidity measures that you're currently looking at, what is the list of measures you would consider?

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

So the new commission scheme first is a unification of the different schemes that we have today. So today we have commissions agreed on a per partner basis, these can be flat or as a function of the selling price or the product group or the return rate. And we are now unifying this towards a scheme that applies to all partners where commission is derived as a function of the selling price of the item and of the return rate so to better align interest of the platform and the partners. We want to incentivize partners to also provide low unit economic items so low selling price, high return rate and we want to monetize better high unit economic items so high price, low return rate. That is already being brought out. So many partners are already live on this new commission scheme and we plan a full rollout now towards the start of '23-'24.

And on liquidity — sorry, on liquidity. So if we look at our current cash position, that's comfortable with above EUR 300 million, but we are looking at negative cash flow expectations for the Q4 and also although we are targetting positive EBITDA for the next financial year, still negative cash flow. And we see it as a matter of prudence to now look broadly into different measures to improve our liquidity buffer. This could be net working capital financing, this could be debt or also hybrid and equity financing measures. So I'd say we're looking at the broad spectrum, but more as a matter of prudence rather than that we are currently planning to implement any such measures.

Operator

The next question comes from Emily Johnson from Barclays.

Emily Johnson - Barclays Bank PLC, Research Division - Research Analyst

Two questions from me, please. The first is on scale. Can you go into a bit more detail on how you plan to crystallize value through the legal separation of that business? And then just on the return rates, can you speak a little bit about whether or not you're seeing any difference by region? And are you able to -- I know you referred to them as kind of converging to prepandemic levels, but can you quantify the impact from higher returns rates in Q3 versus the prior quarter and year-on-year?
Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Thanks for the questions. So on scale, what we're currently doing is basically creating the foundations for a potential lever to better crystallize value. So the spin-off basically is taking place within AY Group and this could then lead to more disclosure on the scale business or for the new scale entity. This could also be the basis for an external investment into scale or in the very long time horizon also a carve-out of scale of the group potential separate sale or IPO. So there are many paths that we could potentially take and what we are doing right now is basically to create the foundation and optionality for that, but we do not yet have a clear plan as to how to crystallize value.

And on the returns, the return pattern is different by region of course as it has also been in the past. So for example, we're seeing higher return rates structurally in the DACH markets than what we see for example in the CE markets and the convergence towards pre-COVID levels that has materialized over the last 12 months or so. So it’s not a phenomenon that we're looking at right now in the Q3 so the gap had narrowed already since the end of the COVID measures and restrictions and the impact is actually quite significant. So if we look at the ceteris paribus margin impact, that’s definitely more than 1% EBITDA margin effect that we're looking at from the normalization of the return rates.

Operator

That answers your question, Ms. Johnson?

Emily Johnson - Barclays Bank PLC, Research Division - Research Analyst

Yes.

Operator

(Operator Instructions) We have the next question from Simon Bowler from Numis.

Simon Bowler - Numis Securities Limited, Research Division - Head of Research

I was just wondering could you talk to given the kind of the ongoing kind of challenging conditions that you’re facing into, is there any scenario where you could reverse or kind of change some of your planned logistics expansion?

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Yes. So what we are of course doing is we’re trying to improve or optimize utilization. There are different cost levers that we can pull on the variable costs. We are also improving UPH metrics so the productivity measures in the DCs themselves. But we’re currently happy with the 4 DCs, which are up and running or about to be up and running, and we do neither plan a further extension of the DC network in the mid-run nor a reduction of this.

Simon Bowler - Numis Securities Limited, Research Division - Head of Research

Okay. Great. And then secondly, you kind of mentioned the inventory levels are on where you had hoped them to be with stock turn not where it’d ideally be as a result. What’s to your mind is kind of time scale to get that back to a more acceptable or appropriate level?
Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Yes. We'd expect inventories to remain elevated also now into Q4 and then to improve as we go into the Spring-Summer '23 season. So we have adjusted the order intake for Spring-Summer '23 quite significantly in anticipation of the lower demand levels. So that should improve as we go into Spring-Summer '23, but remain elevated until then.

Simon Bowler - Numis Securities Limited, Research Division - Head of Research

Okay. And then 1 very quick last one, which you're probably not going to answer, but I'll try anyway. But just with regards to kind of thinking about that and also noted within the margin bridge for next year, this reference kind of operational leverage. Is it possible at this time to give any sense of what level of growth might be needed next year in order to be able to realize that kind of margin path that you've spoken to?

Hannes Wiese - ABOUT YOU Holding AG - Co-Founder, Co-CEO of Operations & Finance and Member of Management Board

Yes, indeed. That's too early to say right now. We will give the guidance as usual with our full year results in May. What we can say certainly is that next year will be a very high focus on bottom line. We are also implementing some measures where we expect an adverse effect on the top line. So if we look at this right now, we would definitely be rather cautious on the top line development given the high focus on bottom line.

Operator

There are no further questions at this time and I hand back to Frank Bohme for closing comments.

Frank Böhme - ABOUT YOU Holding AG - Head of IR & Communications

Thank you. Let me close our presentation by saying thank you all for your support and for joining us today on our conference call for the third quarter of 2022-2023. If there are any further questions, please feel free to contact the IR team directly. We are looking forward to seeing some of you during our upcoming virtual roadshow. Have a good day. Bye-bye.

Operator

Ladies and gentlemen, the conference has now concluded and you may disconnect your telephone. Thank you very much for joining and have a pleasant day. Bye.

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