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PRESENTATION

Operator

Good day, and welcome to this Ultralife Corporation First Quarter 2022 Earnings Release Conference Call. At this time, for opening remarks and introductions, I'd like to turn the call over to Ms. Jody Burfening. Please go ahead.

Jody Burfening - *Lippert/Heilshorn & Associates, Inc. - MD and Principal*

Thank you, Ashley, and good morning, everyone, and thank you for joining us this morning for Ultralife Corporation's earnings conference call for the first quarter of fiscal 2022. With us on today's call are Mike Popielec, Ultralife's President and CEO; and Phil Fain, Ultralife's Chief Financial Officer. The earnings press release was issued earlier this morning. If anyone has not yet received a copy, I invite you to visit the Company's website, www.ultralifecorp.com, where you will find the release under Investor News in the Investor Relations section.

Before turning the call over to management, I would like to remind everyone that some statements made during this conference call will contain forward-looking statements based on current expectations. Actual results could differ materially from those projected as a result of various risks and uncertainties. The potential risks and uncertainties that could cause actual results to differ materially include the impact of COVID-19, potential reductions in revenues from key customers, acceptance of new products on a global basis, and uncertain global economic conditions.

The company cautions investors not to place undue reliance on forward-looking statements, which reflect the company's analysis only as of today's date. The company undertakes no obligation to publicly update forward-looking statements to reflect subsequent events or circumstances. Further information on these factors and other factors that could affect Ultralife's financial results included in Ultralife's filings with the Securities and Exchange Commission, including the latest annual report on Form 10-K.

In addition, on today's call management will refer to certain non-GAAP financial measures that management considers to be useful metrics that differ from GAAP. These non-GAAP measures should be considered as supplemental to corresponding GAAP figures.

With that, I would now like to turn the call over to Mike. Good morning, Mike.

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

Good morning, Jody, and thank you, everyone, for joining the call. Today, I'll start by making some brief overall comments about our Q1 2022 operating performance, after which I'll turn the call over to Phil, who will take you through the detailed financial results. After Phil is finished, I'll provide an update on the progress against our 2022 revenue initiatives before opening it up for questions.

For the first quarter of 2022, strong demand drove our Battery & Energy products, medical revenues up 9% and oil and gas revenues up 20% year-over-year, organically growing our Battery & Energy Products business, and when combined with the revenue boost from our Excell Battery Group acquisition, more than offset continued supply chain impacted government/defense revenues in both Battery & Energy products and Communication Systems. This resulted in a 17% total company revenue increase over the prior year. We also exited Q1 2022 with approximately \$92 million in backlog, an increase of 45% from the end of the previous quarter.

Operating earnings in Q1 continued to be pressured by global supply chain challenges with seemingly daily raw material and input component price inflation, not yet fully recovered with our price increases to customers. Other gross margin headwinds included substitute product identification, qualification and procurement costs, long lead time and manufacturing inefficiencies and new product transitions. Nevertheless, through price increases, cost control and the positive earnings contribution of Excell, our team significantly narrowed the operating loss from the fourth quarter.

In a few minutes, I'll give you further updates on our revenue initiatives. But first, I'd like to ask Ultralife's CFO, Phil Fain, to take you through additional details of the first quarter 2022 financial performance. Phil?

Philip A. Fain - *Ultralife Corporation - CFO, Treasurer & Corporate Secretary*

Thank you, Mike, and good morning, everyone. Earlier this morning, we released our first quarter results for the quarter ended March 31, 2022. We also filed our Form 10-Q with the SEC and have updated our investor presentation, which you can find in the Investor Relations section of our website.

Consolidated revenues for the 2022 first quarter totaled \$30.4 million compared to \$26.0 million reported for the first quarter of 2021, an increase of 16.9%. Commercial sales increased 62.1%, reflecting the contribution of Excell and solid growth across virtually all commercial end markets, including medical, oil and gas and industrial. Government Defense sales declined 38.8% due to continued supply chain disruptions, including increased lead times on components from suppliers and other related logistics matters impacting both our internal and customer manufacturing delivery schedules, resulting in delays in our shipments to future periods.

Revenues from our Battery & Energy Products segment were \$29.2 million compared to \$22.1 million last year, an increase of 31.8% attributable to EXcell sales of 6.4 and a \$2.5 million or 17.2% increase in commercial sales, partially offset by a \$1.9 million or 24.1% decrease in government defense sales. The increase in commercial sales, excluding Excell, consisted of a \$1.1 million or 30.5% increase in industrial end market sales, a \$0.8 million or 20% increase in SWE's oil and gas market sales, and a \$0.6 million or 8.5% increase in medical battery sales.

The backlog for our Battery & Energy Products business of \$82.9 million, the highest in our history, includes \$66.2 million requested for shipping in 2022, representing an increase of \$14.3 million over the comparable amount at year-end 2021.

The sales split between commercial and government/defense for our battery business was 80-20 compared to 65-35 for the 2021 first quarter, and the domestic to international split was 50-50 compared to 57-43 last year, accentuating both the delays in U.S. government defense sales and the continued success of our global revenue diversification strategy.

Revenues from our Communications Systems segment were \$1.2 million compared to \$3.9 million last year, a decrease of 68.3%, reflecting shipments delayed to future periods due to increased lead times on components from suppliers and the timing of orders placed by our customers. We have identified 8 sales opportunities, which were pushed out to future periods by our customers and 8 opportunities, which we did not have the components on hand to ship in the first quarter.

The backlog for our Communications Systems business of \$9.0 million includes \$7.6 million requested for shipping in 2022, representing an increase of \$1.0 million over the comparable amount at year-end 2021.

On a consolidated basis, the commercial to government defense sales split was 77-23 versus 55-45 for the year earlier quarter.

Our consolidated gross profit was \$7.0 million for both the 2022 and 2021 periods. As a percentage of total revenues, consolidated gross margin was 22.9% versus 26.9% for last year's first quarter.

Gross profit for our Battery & Energy Products business was \$6.7 million compared to \$5.4 million last year. Gross margin was 23.1%, a decrease of 130 basis points from 24.6% reported last year, primarily reflecting raw material and component material cost inflation ahead of customer price realization, material usage variances on new product transitions and the completion of the purchase accounting adjustments for finished goods inventory sell-through related to the acquisition of Excell.

For our Communications Systems segment, gross profit was \$0.2 million compared to \$1.5 million for the year earlier period. Gross margin was 19.4% compared to 39.9% last year, reflecting lower volume resulting in the under absorption of factory costs and unfavorable sales mix.

Operating expenses were \$7.3 million compared to \$6.0 million last year, an increase of \$1.3 million or 20.4%. The increase was primarily attributable to the addition of Excell. Excluding Excell, operating expenses increased \$0.2 million, reflecting our continued investment in engineering resources and test materials dedicated to the conformal wearable battery IDIQ contract. As a percentage of revenues, operating expenses were 23.9% compared to 23.2% for last year's first quarter.

Operating loss, inclusive of \$0.1 million of purchase accounting adjustments and remaining Excell acquisition costs, was \$0.3 million compared to income of \$1.0 million for the 2021 quarter.

Our tax benefit for the first quarter was \$0.3 million compared to a provision of \$0.2 million for the 2021 quarter computed on a GAAP basis.

Including the interest expense to help finance the Excell acquisition, net loss was \$0.2 million or \$0.01 per share. This compares to net income of \$0.7 million or \$0.04 per share on a diluted basis for the 2021 quarter. Excell was accretive by approximately \$0.02 per share.

Adjusted EBITDA, defined as EBITDA, including non-cash stock-based compensation expense, was \$1.1 million or 3.6% of sales compared to \$2.0 million or 7.8% for the first quarter of 2021.

Turning to our solid balance sheet. To proactively manage our supply chain, reduce the impact of potential component price increases and optimize our position to service our rise in backlog, we increased inventory by \$3.2 million or 9.6% compared to year-end 2021. We ended the 2022 first quarter with working capital of \$49.1 million and a current ratio of 3.5 compared to 47.6 and 3.5 for year-end 2021. Debt to capital at quarter end remained low at 0.15.

As a result, we remain well positioned to fund organic growth initiatives, including new product development and strategic capital expenditures, while continuing to expedite our organic growth through accretive M&A.

Going forward, with our growing backlog, ample liquidity, diversified end markets and growth initiatives, we remain steadfastly focused on utilizing the full leverage potential of our business model.

I will now turn it back to Mike.

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

Thank you, Phil. For 2022, we continue to focus on driving revenue growth by market sales reach expansion, primarily through diversification, new product development and strategic CapEx for competitive advantage and a disciplined approach to acquisitions.

For the Battery & Energy Products business, diversification and market and sales reach expansion has meant further penetrating the global commercial markets as well as the international government defense markets, which has helped deleverage our historical concentration in the U.S. government defense market. This was nicely demonstrated in the first quarter as our medical and energy markets revenue increases led to 3%

of net B&E organic revenue growth. In Q1 and including Excell, the total commercial and international government defense revenues represented approximately 82% of our total B&E sales.

We remain very excited about the recent Excell Battery Group acquisition as it is another step in diversifying our end markets while providing further scale of our Battery & Energy Products business. It bolsters our engineering and sales capabilities for participation expansion of existing energy, industrial and medical markets and penetration of new commercial markets, such as automated meter reading, ruggedized computers and mining. The initial 100-day functional tactical integration plans are substantially complete, and we are now transitioning Excell into the regular Ultralife operating cadences. The acquisition was EPS accretive in Q1 and revenues met expectations its first total quarter as part of the Ultralife portfolio.

Overall global B&E Medical revenues represented approximately 26% of total battery energy product sales. Demand from current customers was for applications such as ventilators, respirators, infusion pumps, digital x-ray and surgical robots. We also received over \$4 million in delivery orders from existing medical customer blanket and/or multiyear agreements.

Q1 oil and gas and subsea electrification commercial revenue was approximately 31% of total B&E product sales. Driven by increasing oil prices and rig counts, we continue to see gains in our core oil and gas business. Since the acquisition a few years ago, our SWE operations also continue to diversify their capabilities, solidly supporting our engineering efforts for product development in both medical and government defense end markets.

On the international government defense front, in Q1, we received an order for our Land Warrior battery products, which we'll ship within the next 12 months.

B&E's Q1 U.S. government defense business represented approximately 18% of total B&E product sales, consisting primarily of radio battery and chargers to OEM primes. We also have a separate small delivery order to complete under a prior 5390 IDIQ contract, which is expected to ship later this year.

The wearable conformal battery IDIQ contract, which we announced last May, continues through the product development process and component testing with first article testing expected to begin in the middle part of this year, demonstrating full compliance with the contractual product specifications and program requirements. As an IDIQ contract, actual delivery orders, including quantities and timing are at the discretion of the DoD.

New product development remains a core element of B&E's organic growth strategy, and during the first quarter, we continued to advance several of our multiyear development new products. In March, we showcased our X5 next-generation medical cart battery and power system at the Healthcare Information and Management Systems Society trade show in Orlando and has significant interest from both cart manufacturers and IT professionals. As evidence of this interest, towards the end of the quarter, we received our first \$2 million order for this new medical cart battery and power system as well as additional accessories with shipments starting later this year. We have also conducted demonstrations of the system at several OEMs with positive results, maintaining the momentum from the trade show.

Other new product development projects currently underway include, but not are limited to, a higher capacity smart U1 battery, New 5790 and XR123A CFx-blend primary batteries, OEM public safety radio batteries, and next-generation ruggedized modular large-format energy storage batteries.

New product development and multigenerational product planning continue to keep us current with market needs and give us the opportunity to remain close with and provide value to our key customers.

In addition to the investment in new product development and multi-generational product planning, we are also continuing to deploy strategic CapEx investment in our facilities to strengthen our competitive differentiation.

Progress continues at our Newark, New York facility on the new lithium manganese dioxide primary 3-volt cell manufacturing line. We continue to see interest from OEMs in the lighting and medical markets for the new 3-volt product. Historically, we have developed technology to meet the stringent demands of some of the most challenging applications in the defense, medical and industrial markets with unique products. In our latest 3-volt product, we have leveraged that technology to improve the power capabilities in more widespread applications. This means lights that shine brighter and last longer in the LED Flashlight segment and longer operating time in medical applications, 2 large markets for this product. We also have a customer evaluation underway for a similar form factor cell, except using a CFX-blended battery chemistry that was initially developed to provide longer-lasting power to our warfighters and is now being tested and validated in commercial medical and industrial markets to provide some of the longer performing benefits needed for the most critical applications.

At our China facility, we are deep into the second phase of a multistage project to upgrade our thionyl chloride primary ER cells. And in Q1, ER cell production and customer testing has continued and with positive results. While testing these products take a long time because of the demands of the applications, we are beginning to see some of the results of our sampling efforts. Several customers are in various stages of commercial activity, driving an increase in our production of our ER product in our China facility. With each stage of product and process improvements and newly identified thionyl chloride ER cell commercial and industrial applications, we are expanding our available revenue opportunity set.

We also continue to grow our China operations value proposition with global medical and industrial customers for the supply of our cells and battery pack solutions. In Q1, our total China operations revenue was up 13% year-over-year.

Our goal is to produce the highest buyer proposition best quality and safest products in close collaboration with our end market and OEM customers, at whichever one or more of our global locations best serve their supply chain.

Looking at Communication Systems, in Q1 new product development revenue from products less than or equal to 3 years old represented approximately 16% of Communication Systems revenues.

For the U.S. Army's Handheld Manpack Small Form Fit and Leader Radio programs, we continue working the supply chain in preparation for manufacturing and delivering later in 2022, the previously announced \$4.2 million vehicle amplifier adapters award.

New product development activities for defense and commercial applications continue in concert with several OEM partners to meet multiple emerging requirements and system integration. One opportunity is a power solution for radio integration into aircraft, where current efforts are focused on prototype refinement testing and field trials throughout 2022 with procurement potential production units in 2023 and 2024. Another project is for an Edge server system integration, which has completed multiple customer tests and evaluations. This configuration is a 2-case system with one housing a server and the other providing uninterruptible power supply backup with ancillary items. Incremental small volume DoD orders continued in Q1 with delivery expected in Q2.

Regarding our Communications Systems team push into commercial markets, the initial low rate production units of a mobile data card delivered in 2021 are undergoing operational testing with the customer, conducting analysis of autonomous vehicle data during testing and manufacturing of the vehicles.

Our second commercial product is a virtualized radio access network enclosure, supporting 5G network deployments worldwide, which was delivered to a customer and now supporting test and evaluation by a cellular network provider for use in expanding 5G market installation.

Communication Systems initial entry into commercial products, leading to larger programs, combined with our strong participation in global ongoing military radio programs, provides a roadmap for long-term sustainable growth.

In closing, for the first quarter of 2022, we were delighted to start the new year with strong commercial revenue generation, boosted by the addition of Excell.

As we progress through 2022, we are well positioned for additional revenue lift from the growing firm order backlog, our increased exposure to the oil and gas recovery, the dry powder of multiple DoD IDIQ awards in various stages of maturity, including the 5368, 5390, 5790 and conforal

wearable batteries, the initial revenue realization from the new medical cart batteries and our new CR and ER cells, shipments against the latest Leader Radio VAA follow-on contract, and several of our new Communication Systems integrated computing, 5G and AI commercial solutions. Our capabilities and the mission-critical end markets we serve -- military defense, energy and medical, align well with current world events and needs.

Whereas supply chain-related issues and inflation have continued to impact profitability, we are encouraged by the directional progress made in Q1 and are expecting continued financial performance improvement throughout the remainder of the year as manufacturing efficiencies return and price increases start to hit the ledger. We will also continue working with our suppliers and customers to strategically manage working capital, including inventory, to best position us for making customer delivery schedules and mitigating to the extent possible, raw material and component shortages and cost inflation.

As a result, we are targeting total year profitability, solid cash flow from operations and maintaining our strong balance sheet while supporting transformational products and investments. Our goal in 2022 remains to return to our next year of profitable growth.

Operator, this concludes my prepared remarks, and we'll be happy to open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will now take our first question from Josh Sullivan of the Benchmark Company.

Joshua Ward Sullivan - *The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Just as far as supply chain dynamics here, last year seemed to be maybe a little more related to transit and other factors now are staring down inflation. Can you just give some color on what supply chain issues are maybe improving versus those that are maybe going to grow throughout 2022?

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

Josh, thanks for the question. I think it would be difficult at this point to really call any victories of supply chain issues improving at this point. I just think that we probably have a better process of understanding what to be looking for, working very closely with our suppliers to try to get a real beat on what deliveries look like, what cost increases potentially look like and then working very, very closely with our customers to pass along that information, evaluate how their supply chain is looking and try to balance out the things that are coming into us and the things that are going out from us with our customers to make prudent decisions. But I think it'd be difficult at this point to really point out anything in the overall supply chain situation that's dramatically improving at this point. It's probably just more -- we're getting more used to it and getting better at handling it and have real broad and open lines of communication with both our suppliers and our customers.

Joshua Ward Sullivan - *The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Got it. Got it. And then with new products moving into revenue generation year in '22, how should we think of margin progression, should we expect an inventory build or marketing effort impacting margin? Just trying to get an idea of sequential the cadence through the year.

Philip A. Fain - *Ultralife Corporation - CFO, Treasurer & Corporate Secretary*

Yes. I think our cadence for the year as you look at all the various new products and where they are in the transition process from the new product group, putting it over the wall into high-volume manufacturing, historically, we can look back and we can see how long it's generally taken. And

it seems that the time frame that is taken now has been extended because of the sheer quantity of the new products. So for us, the challenge is how we deploy best our manufacturing engineers and our operation's leadership and personnel. And I think, Josh, that we're going to see margins build over the year because we analyze everything, just like our cost increases with our suppliers, we analyze everything, we know what to attack and where and how we attack is in full gear. And what we're attacking, I'll quantify it. What we're attacking is \$0.02 to \$0.03, \$0.02 to \$0.03, I look at various buckets. And I think we feel that there is improvement in the \$300,000 to \$500,000 range, and it's getting to that improvement as quickly as we possibly can. And in doing so, we're methodical. We want to make sure that the mission-critical products that we're providing are meeting the specs with absolutely no shortcuts, and that has been our approach.

Joshua Ward Sullivan - *The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Got it. And then just kind of related to that, the \$83 million in backlog, how much of that is related to some of these new products you're launching this year, 3-volt, [medical] (corrected by company after the call) carts (inaudible) et cetera?

Philip A. Fain - *Ultralife Corporation - CFO, Treasurer & Corporate Secretary*

Well, I would say a relatively small part of the 90 -- let me just take you through the backlog. The backlog is \$92 million. And then we break it down as to what is requested for shipping this year, it's \$74 million of what is being requested this year versus \$58 million what was requested for shipping last year. The \$92 million compares to \$63 million as we exited the year. So as Mike said, it's a big 45% increase, but a lot of it is just either new products that are in the process of transitioning or have transitioned to high-volume manufacturing. And I would say that the majority is ongoing products, a handful of products that are in the process of transitioning, which includes some of the military batteries, some of the public safety batteries. And as Mike had mentioned, the \$2 million order that we received for the medical carts. So the large majority are ongoing products that we're, I would say, comfortable with on the operations side, not so comfortable with on the supply and component side.

Joshua Ward Sullivan - *The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst*

And then just on the Excell acquisition, how is the integration progressing? Any new opportunities that you've seen, you've had some time to get acquainted.

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

No. I mean, actually, it's been very exciting and very positive. Like as I mentioned in the prepared remarks, the tactical stuff you want to go through immediately to make sure it gets paid, all the collections are being put into the right bank accounts and our customers are receiving the products they deserve. And so now we're moving really in the next phase where we can get more deeply into order some larger level cost synergies, what are some more strategic revenue synergies. We found that the actual -- on the revenue side, there's actually very little overlap. So we're participating in a broader energy market than we were before the acquisition. We're looking at some short-term small cost synergies to take advantage of. But at the end of the day of the thing, and I always say that and it certainly isn't pandering, it's the absolute truth. I just love getting the talented people in our space. We have -- between the acquisition we did in the U.K., the acquisition that we did with SWE a couple of years ago and now with Excell, I think we have some of the smartest and most experienced battery and battery pack engineers and salespeople that there are in the marketplace. And that's the most -- to me, the thing I get most excited about. But so far, so good. I mean, we'll come across issues from time to time, and that's just the way business is. But I'm very confident that with how we're positioned today and with the talent that we have on board both of our teams that the issues that do come up, we'll be able to solve pretty quickly.

Joshua Ward Sullivan - *The Benchmark Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Got it. And then just one last one on the aircraft application, you're testing, I think you mentioned there in the prepared remarks, can you just expand on what markets or airframes you're going after there?

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

I mean it's definitely in the military, and that's really about all I can say about this point, Josh, but it's in the military segment.

Operator

We'll take our next question from [Barry Lewis] of Sandler.

Barry Lewis - *Analyst*

I expect the purpose of the call is to ask you, you mentioned the wearable battery and you mentioned you got the order in May. Where do we stand with that order? I think I heard you talk about the end of the year, but I wanted to clarify that.

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

As we mentioned and what is pretty common for these large IDIQ contracts, there's a pretty substantial development period. And one of the milestone events at the conclusion of that development period is the first article testing. And we expect to be in sort of the formal first article testing really towards the middle part of this year. And depending on the outcome of that, which is an iterative process with the Army upon completion of that first article testing and checking of that box, then we would be in a position to potentially receive delivery orders. So the next major milestone is the initiation and completion of the first article testing, which we expect to start in the middle part of this year.

Operator

We'll take our next question from Stuart Citron, private investor.

Stuart Citron - *Private Investor*

This has been a very professional presentation. I've enjoyed it. Recently, I read where Mr. Fain exercised some stock options. And I'm wondering when were those stock options set to expire?

Philip A. Fain - *Ultralife Corporation - CFO, Treasurer & Corporate Secretary*

The options were set to expire the day -- 2 days of, let's say, past the date that I exercised those options. So I held those options for the life of the option absent 2 days, which was a full 7 years. Now when I exercise those options, I used what's called the net exercise method, so I retained all of the shares. It's synonymous with the way I look at it as a purchase of the shares.

Stuart Citron - *Private Investor*

Yes, that makes sense. I just wondered when they were set to expire. And so are you saying they were set to expire 2 days after you exercised them?

Philip A. Fain - *Ultralife Corporation - CFO, Treasurer & Corporate Secretary*

Yes, absolutely.

Stuart Citron -- *Private Investor*

Okay. Well, thank you very much. Have a nice day. Thanks for taking my call.

Operator

(Operator Instructions) There are no further questions at this time. I'd like to hand the call back to Michael for any additional or closing remarks.

Michael D. Popielec - *Ultralife Corporation - CEO, President & Director*

Well, great. Well, thank you once again, everybody, for joining us for this call in the first quarter of 2022 recap. We look forward to sharing with you our quarterly progress on each quarter's conference call in the future. As Phil mentioned, we updated our investor presentation, that's on the website, so please check it out. And everybody, have a great and safe day. Thank you very much.

Operator

Thank you. That now concludes the call. Thank you for your participation. You may now disconnect.

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