

06-Nov-2020

Kambi Group Plc (KAMBI.SE)

Q3 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Kambi Group Q3 Report 2020 Call. Throughout the call, all participants will be in a listen-only mode. And afterwards, there will be a question-and-answer session. Just to remind you, this conference is being recorded.

Today, I'm pleased to present Kristian Nylén, CEO; and David Kenyon, CFO. Please begin your meeting.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

Good morning, and welcome to Kambi's third quarter result presentation. I am Kristian Nylén, Chief Executive, and joining me is our CFO, David Kenyon.

Please turn to slide 2. I will begin with a brief overview of what was a record Q3, after which David will take you through the financial performance. I will then speak about the quarter in a little bit more depth, and also a few updates from Q4 so far.

But, first, on slide 3, let me give you a brief introduction to Kambi. Kambi is the industry's trusted and independent sports betting supplier. Our multichannel service is managed through an in-house developed platform, which has been continuously developed over the last decade. The platform, together with 860 highly skilled staff, forms the foundation of our service.

The Kambi sportsbook consists of multiple elements, from front-end user interface and open APIs, through to odds compiling, customer intelligence, and risk management, enabling our customers to offer their players a tailored and leading sportsbook experience from day one.

On to slide 4. Kambi's business is built upon revenue share model, with our growth linked to our partners' success. The foundation of our strategy is based on scalability. At no additional cost to our partners, Kambi continuously invests in products, people, and technology to maintain market leadership.

We operate an experienced in-house trading and risk management team to optimize operator trading margin, and our business is underpinned by our corporate probity and integrity. And we have successfully obtained all licenses [indiscernible] (2:34). All of these combined enable us to offer our partners the flexibility and scalability required to succeed in today's highly regulated and global market.

Our technology has been structured in a way that enables Kambi and its partners to quickly and efficiently comply with regulatory requirements, removing a major barrier to market and allowing them to enter new markets as and when they require.

Kambi is a trusted partner to more than 30 operators across six continents, including some of the most recognizable and successful brands in the industry. Together, they create a powerful network of operators which combine to generate powerful data insights that we use to inform and continuously iterate our products and service.

Let's look at the highlights on slide 5. Before looking at the highlights, let me reflect a bit on the pandemic and the impact on our business going forward. I'm proud of how well and prompt our staff have reacted to the changing circumstances, being ready to provide our operators with top quality service regardless of the circumstances.

What we have seen from a heighten restrictions across Europe in the last weeks, top tier sports seem to be shielded. I believe sports federations have shown they can run operations in a relatively safe manner and it has been a very positive impact on people to be able to enjoy sports also in a lockdown. We hope this can continue, of course, as it will significantly limit any impact on our business going forward.

Q3 was a record quarter for Kambi with revenue up 22% and operator turnover up 62% year-on-year. We also demonstrated the scalability within our business model, posting an operating margin of 23%. We signed a new partner in Churchill Downs which operates BetAmerica's sportsbook brand in the US. This is a great partner win for us, and I will speak more about this later.

We also extended our partnership with LeoVegas. Not only does this extend the length of our agreement, but it also expands the partnership to cover additional brands. And as had become the norm, we have supported our partners with many launches, including the Barstool Sportsbook launch with Penn National Gaming.

For now, I will hand over to David who will talk you through the financial highlights, turning to slide 6.

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

Thank you, Kristian. Good morning, everyone. In Q3, we had revenue of €28.1 million, up 22% on last year. For the year, to the end of September, revenue was €70.8 million, up 8% on last year. Operating costs for the quarter were €21.6 million, giving operating profits of €6.5 million at a margin of 23%, whilst for the first nine months, we made an operating profit of €10 million at 14%.

Let's look at the income in more detail, turning to slide 7. This slide sets out the Kambi turnover index, with the graph showing the aggregated results of Kambi's operators. The turnover is the total stakes placed with the operators by their end users. In Q3, operator turnover was up by 62% on Q3 last year, reflecting the opening up

and growth of the market in various US states such as Pennsylvania, Indiana, and Illinois. And the return of the sporting calendar after the heavy impact of the global pandemic in Q2.

The first part of the quarter were the conclusion of the main European soccer leagues and the final stages of the Champions League. In September, we saw the start of the new seasons for the soccer leagues and the NFL. It's extremely positive to note that operator turnover accelerated through the quarter, with 43% of the quarter's total being generated during the month of September. The margin represents the combined trading margin made by the operators. In Q3, this margin was 7.2%.

We can see the split of operator GGR by region on slide 8. With the growth of the total business, the European GGR was up 11% on the same quarter last year. Q3 saw a resumption in the growth trend of the Americas GGR, driven by the return of the main US sports and the entry into new US states, with this being a first full quarter of revenue in Illinois and Colorado, for example.

We can see the conversion from the movement in operator turnover to our revenue on slide 9. Operator turnover post foreign exchange impact was up by 62% compared to Q3 2019. The comparative operator trading margin was very high in Q3 last year, so the increase in operator GGR was 38%.

The effect of the significant increased level of operator NGR was to decrease the effective commission rates charged to our operators due to a tiered structure in some contracts. The net effect is the revenue for Q3 2020 is up by 22% on Q3 last year to €28.1 million.

Let's turn to the full income statement on slide 10. Operating expenses for the third quarter were €21.6 million, up from €18.1 million last quarter, as our operations returned to pre-COVID levels. Looking ahead to Q4, we anticipate costs will increase by 5% to 8% as we press ahead with our US license applications and data supply costs reflect the busy sporting calendar.

The operating profit for Q3 was €6.5 million, up from €3.4 million in Q3 last year and €10 million for the first nine months, up from €8.6 million. The profit after tax for Q3 was €5.1 million and €6.8 million for the first nine months.

Now, let's look at the cash flow on slide 11. Set out on the slide are the major components which impacted our cash position during the quarter. Our opening cash balance was €46.4 million. The cash inflow from the operating profit was temporarily offset by a negative cash movement in our working capital. Trade receivables increased in the quarter, predominantly due to a much higher level of invoiced amount in the months preceding the quarter-end compared to in Q2. A large part of these amounts has been received after the end of the quarter.

Capitalized development costs in the quarter were €3.6 million, while the amortization charge on previously capitalized costs was €3.2 million. The net cash outflow for the quarter was €0.5 million and our closing cash balance €45.9 million.

In summary, our financial performance, which showed a high level of resilience earlier in the year, this quarter reflected the business's ability to respond immediately to the resumption of sports and demonstrated the inherent scalability in the business model.

So now, let me pass you back to Kristian, turning to slide 12.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

Thanks, David. In August, we signed a new partner in Churchill Downs, which is a large multi-state business in the US with a fantastic heritage in sports and, in particular, races, hosting one of our most prestigious events in racing calendar, the Kentucky Derby. Churchill Downs operates the BetAmerica's sports betting brand, which has been active in a few states for a couple years. We have yet to really invest in the marketing of the brand, but plan to do so once they are transitioned to the Kambi sportsbook.

They also operate a racing platform called TwinSpires, which has enjoyed great success in the US. Churchill Downs' plan is to align this closely with BetAmerica and as well seen with the success of ATG where it's a good crossover between both better racing and those bettors of the sports. So, Churchill Downs is an exciting partner for us. We are already live on the property in two states and we'll add more in the near future. The company also has great market access, so BetAmerica has a great opportunity to become one of the leading sportsbook brands in the US for years to come.

Turning to slide 13. As I have said before, extending partnerships is just as important as adding new partners. So, I'm delighted to have signed a new agreement with LeoVegas. Not only is this an extended agreement, but it's also an expanded one, with additional brands added to the contract. And we are already live with two of those brands in the UK market. LeoVegas has been successful in using the Kambi technology to build a unique sportsbook experience. And we look forward to supporting their development through the coming years.

Turning to slide 14. Q3 also saw the much anticipated launch of Penn National's Barstool Sportsbook. The launch in Pennsylvania was a success and Penn themselves set out last week in their report. And we look forward to supporting the launch of [ph] that app (14:00) in multiple states over the next 12 to 18 months. The app itself is a great demonstration of what's possible with Kambi's technology. Kambi acts as a blank canvas for operators that wish to develop something unique on our platform, which Penn have successfully done here, creating their own proprietary app and IP, built in-house with them with no [indiscernible] (14:32).

Furthermore, Penn has also been leveraging our price differentiators to differentiate themselves forward in the market, while we have also had great success in using the Barstool personalities to create unique betting opportunities for that app, as you can see on this slide. For example, players can bet with or against David Portnoy, the Barstool founder. Overall, I'm confident about the next 12 months will be, as we support Penn in creating a leading omnichannel experience, with retail channels also a major focus for them.

Moving to slide 15. In total, Q3 saw 17 partner launches in the US, with 3 online and 14 on-property. As you can see on the slide, these launches span seven customers in seven states. On the states we have launched sports betting since the repeal of PASPA, the Kambi sportsbook is live in more properties than any other B2B or B2C sportsbook.

Turning to slide 16. In the events after Q3, we recently launched in Tennessee our 12th state, enabling DraftKings to be the first tranche of operators to go live in the state. Tennessee is online-only due to the fact that we have no land-based casinos. It's worth noting that Tennessee shares a border with eight states, none of which currently offer online sports betting. As we have seen elsewhere, bettors are more than willing to cross the state line in order to place bets on mobile. So we may see similar in Tennessee, which will increase their potential marketplace.

In events after Q3, we also signed with Belgian National Lottery, and we'll get into more depth on that exciting partnership in our Q4 report.

Turning to slide 17. On this slide, we can see the scale we have built in the US. We are active in 12 states and operate in sportsbook in 45 properties, which, as I said earlier, is more than any other B2B or B2C sportsbook in the States launched post PASPA. With more states to come, as well as the expansion of our current partners, we can expect the number to grow substantially during coming 12 months.

And finally, onto slide 18. So, to summarize, it has been a return to form for Kambi following a difficult Q3. In Q3, we delivered a record financial performance. As part of that, we have proven our scalable business model, delivering strong operating margin. And what has been pleasing of late is that we have carried this momentum into Q4, with October delivering a strong performance with growth accelerated. And we look forward to pushing on further through the final two months of the year.

Now, I will pass over to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Erik Moberg from ABG. Please go ahead.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Hi. And thanks for taking my questions. So, 43% of Q3 turnover was generated in September, which you then guided has accelerated into Q4. Aside from NBA, is there anything else that has a negative impact sequentially and on a year-over-year basis, if we look at the full Q4?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Hi, Erik, Yes, I would say ice hockey will have a little bit of a similar pattern, since the NHL also had a very prolonged season into Q3. But other than that, nothing that I can see.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Got it. So, all things equal then, given that you will also see the full effect for the Barstool brand and you will also have contribution from Tennessee, you should at minimum be able to have an average monthly turnover in line with September for the full Q4. Is that a fair assumption?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I would say that's a very fair assumption, yes.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Got it. Thanks. And then, in terms of the new contract with the Belgian National Lottery, do you have any view on the type of market share its sports betting brand possessed in the past? And also, do you have any guidance in regards to what market share it targets going forward?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I can't really communicate anything on that at this point, Erik. But I can say that it's coming from quite a low number. So, they are certainly not market-leading in the Belgian market at the moment.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Fair enough. And in regard to your Virginia sports betting, it is expected to launch in Q1 2021. Should we expect DraftKings to launch in Virginia with SBTech or with you guys?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I don't want to comment on that at this point.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Got you. And just in general, obviously, you're experienced in rapid growth, but if you could give some more flavor on the growth in receivables and how you worked to improve working capital into Q4?

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

Hi, Erik. David here. It's...

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

Yeah.

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

Yeah. I mean, the improvement in receivables is entirely linked to the growth in revenue. So, at any period end, we have two months outstanding because it's the month before and then the invoice issued by the end of the month, at the end of the period. So, versus Q2, of course, the revenue is significantly higher. That directly translates into a higher debt impairment at the end of Q3.

Current debt balance, half of it has been recovered since the end of the quarter. So, absolutely no concerns with the increase in debtors at the end of the quarter. And yeah, it's certainly stable and debtors are typically stable. And if they go up, revenues go up, debtors go up. So, it's a very safe pattern and we're very happy with the position.

Erik Moberg

Analyst, ABG Sundal Collier AB

Q

All right. Fair enough. Thank you very much. That's all for me.

Operator: And the next question comes from the line of Marlon Värnik from Pareto Securities. Please go ahead.

Marlon Värnik

Analyst, Pareto Securities AB

Q

Good morning, Kristian, David. First, a follow-up question on football here. You mentioned the strong trend from September has continued in Q4. Have you seen this trend also as strong in the US, given that basically it's only NFL ongoing, or have you seen it offset by new launches in the US?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I think the major sports deal by quite some margin is American football. So, I would say that we see a positive trend in the US as well.

Marlon Värnik

Analyst, Pareto Securities AB

Q

All right. Good. And second question then, can you also comment just on the initial free bets and bonuses offered recently? How big of a short-term impact, negative impact you've seen in the US market [ph] particularly here? (22:58)

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

Yeah. I mean I think the important thing from a Kambi perspective is we kept the amount that can be deducted in terms of our – in what impacts our revenues. So, it's a known quantified amount kind of before we get into any contract. So, yeah, that's why you don't see a – you see a fairly stable deduction on the waterfall we show because we know exactly the capped amount that can be deducted before we calculate commission. So, yeah.

Marlon Värnik

Analyst, Pareto Securities AB

Q

All right. And on Churchill Downs, how should we view the long-term potential of Churchill Downs contract in relation to other US partners, [indiscernible] (23:42) and what can you tell about the rollout plans here?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

So, I mean it's always hard to know the potential, but they have great market access. I mean, they are one of the largest when it comes to having already a network in different states. So, from that perspective, it's very high potential.

And as we talked about, I mean, the customer base within the ratings is quite fantastic. So, if they can transform that into sportsbook, as ATG was successful doing it in Sweden for instance, then they have a very, very good chance of being one of the leading brands in the US going forward.

Marlon Värnik

Analyst, Pareto Securities AB

Q

Interesting. And can you say anything about the rollout plans here potentially down for the next couple of quarters?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Not anything in specific. But they have quite a aggressive plan to rollout into more states. So I hope they will be very [ph] attractive (25:12) in the next 12 months, both online and retail in several more states at the moment.

Marlon Värnik

Analyst, Pareto Securities AB

Q

Great. Also, can you also – given the comment of the outcome and your exposure on the US election, and if you can give some color of the turnover in compared to other events?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Yeah. So, first of all, I mean, the US election actually is one of a – it is quite high turnover. But you have to remember that you can't bet on political events in the US [indiscernible] (25:56) the European turnover actually. I don't think – I mean, it will not be significant for us either outcome of the election event. I mean, it's clearly less than a regular Champions League game, I would say. So, yeah, it's a big event for being politics, but compared to a large Champions League match, it's not that big.

Marlon Värnik

Analyst, Pareto Securities AB

Q

All right. That's all for me now. Thanks.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Thank you.

Operator: And the next question comes from the line of Viktor Högberg from Danske Bank. Please go ahead.

Viktor Högberg

Analyst, Danske Bank A/S (Sweden)

Q

Yeah. Good morning. So, I have a couple of questions. The first one is on the waterfall and the FX effects. I think this is the first time you've put forth the number or the figure of a turnover growth in local currencies as well. Is that correct? And is that why the FX effect in the waterfall is so large, the net effect is not as much?

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

No. I mean, we have disclosed it before but it's probably more noticeable this time. I think we've seen movements both on the Colombian peso against the euro and the US dollar against the euro. So it's actually, nominally said, at a very small amount. [ph] Perhaps (27:26) going to get bigger this quarter. Yeah, it's around €1 million, I think, if you translate kind of waterfall into some real money. So, that's versus – yeah, using Q3 2019 FX rates, it would have been €1 million higher, I'd say, yeah, so to an extent it's fairly material.

Viktor Högberg

Analyst, Danske Bank A/S (Sweden)

Q

Okay. And also I just want to double shift gear on Erik's question earlier on the implied turnover comment on the start to the fourth quarter with the average monthly turnover in line with September being a fair assumption. So, [ph] 288 times 3 (28:07), would that be a fair assumption as a baseline for Q3? Is that how we should read that comment?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I would say that's a fair assumption.

Viktor Högborg

Analyst, Danske Bank A/S (Sweden)

Q

Okay. So, seems like a strong start then. So, last question, US out of the Americas, how much is that? Did you quantify it? I didn't find it in report.

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

We didn't quantify it in the report, but it's in the range of 30% to 40% of the total. Of the 43%, 30% to 40% is US and the rest is kind of Central and South America.

Viktor Högborg

Analyst, Danske Bank A/S (Sweden)

Q

Okay. Thank you very much.

Operator: And we have one more question from the line of Hjalmar Ahlberg from Kepler Cheuvreux. Please go ahead.

Hjalmar Ahlberg

Analyst, Kepler Cheuvreux SA (Sweden)

Q

Thank you. [indiscernible] (28:58) I have a question around the potential for a new contract in Europe. I mean, you saw the Belgian National Lottery win here and we are seeing now Germany regulating and Netherlands regulating. Are these countries – do they have the potential to add new clients on this type?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Well, let's hope to win new clients, of course. And, yeah, of course, regulations has always been a good catalyst for new business. So, obviously, we hope for some new opportunities in both Netherlands and Germany.

Hjalmar Ahlberg

Analyst, Kepler Cheuvreux SA (Sweden)

Q

Thanks. And just a question on the revenue mix. I mean, you added a lot of new clients. [ph] I think you (29:50) commented that in 2020 and 2019, you said the two largest clients were 58% of revenue. Can you say if this has changed anything in terms of dependence on large clients?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Well, we'll kind of give the full year numbers in the annual report, but I don't think when you say that 30% to 40% from the US, you can say that probably that there's probably a shift in the numbers in those and reliance on specific customers. So, yeah, we'll give you the full numbers in the next annual report, probably a little bit different to last year.

Hjalmar Ahlberg

Analyst, Kepler Cheuvreux SA (Sweden)

Q

Okay. Those were the questions. Thank you.

Operator: And we have just one follow-up question from the line of Marlon Värnik from Pareto Securities. Please go ahead.

Marlon Värnik

Analyst, Pareto Securities AB

Q

Yeah. Hi. It's Marlon here. What can you tell us regarding the potential partner expansion plans in Maryland, Louisiana, South Dakota who voted for sports betting during the US election?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I think some of our partners already have market access into both Maryland and Louisiana. South Dakota is a very small state, so not sure if anything – yeah, that will not be very important, but I'm sure we will see some of our customers probably going there as well. But moving Maryland and Louisiana, our existing customer base already has some market access and I would expect more to find ways to get market access.

Marlon Värnik

Analyst, Pareto Securities AB

Q

And given that the US market is legalizing now at a rapid pace, how should we now think about OpEx in the long-term?

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

A

Well, I think [ph] Vik (32:00) internally our plans are to keep growing costs in the control where we've seen before. I mean, the growth of the US, it does bring some additional licensing costs but it's nothing that materially changes the path of our cost growth. So, where we are growing costs, it's because we're doing it to really improve our service, recruitment and product improvement. So, I don't see the US – kind of continued growth of the US market necessarily shifting our cost base to what has been in the past.

Marlon Värnik

Analyst, Pareto Securities AB

Q

All right. Cool. And the final question, a more nitty-gritty question recently do you find more difficult to price markets more obscurely, given some of the professional sportsbook brokers have recently suspended its offering in those kind of markets?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

I'm not sure I understood the question. Can you expand?

Marlon Värmik

Analyst, Pareto Securities AB

Q

So, basically, some professional sportsbook brokers, they have taken away the more obscurely markets, at least lowered the limits on those. Have you found it now recently last month more difficult to price those markets to your customers?

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

No. I guess, the biggest issue here is, of course, having sufficient information to understand. If they [ph] can field a team (33:35) and that becomes an even bigger issue in a market like Sweden where we also have the regulations that's controlling – you're not having under-18 players.

So, I think that is probably a much bigger concern for us to be able to follow regulations when teams are depleting the best sports, rather than the pricing of it. But of course, I mean, if you don't have the information about the proper team being out, it makes your pricing poor for a very short while. But that is not as a big issue, I would say. It's more of integrity concerns and regulatory concerns that we would not price stocking up, rather than we're uncertain about the pricing.

Marlon Värmik

Analyst, Pareto Securities AB

Q

All right. Thank you, Kristian. Thank you, David.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

A

Thank you very much.

Operator: And as there are no further questions, I'll hand it back to the speakers for closing remarks.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

All right. Thank you, all, for your questions and for listening in. We look forward to updating you on the 10th of February, 2021, when we publish the fourth quarter report of 2020. Thank you.

Operator: This now concludes our conference call. Thank you, all, for listening. You may now disconnect your lines.

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