

## Q3 2017 Earnings Call

### Company Participants

- Jose Luis Gutierrez, Chief Operating Officer, Carrefour Retail
- Jose Roberto Meister Mussnich, Chief Executive Officer, Atacadao
- Noel Prioux, Chief Executive Officer
- Paula Cardoso, Chief Executive Officer, Carrefour Solucoes Financeiras
- Sebastien Durchon, Chief Financial Officer

### Other Participants

- Alana Imaizumi, Analyst
- Cedric Lecasble, Analyst
- Fabienne Caron, Analyst
- Joseph Giordano, Analyst
- Marco Calvi, Analyst

### Presentation

#### Operator

Good morning, ladies and gentlemen. Welcome to Grupo Carrefour Brasil's Third Quarter and Nine Months of 2017 Conference call. At this time, all participants are in a listen-only mode. Later on, we will conduct a question-and-answer session and instructions will be given at that time. (Operator Instructions) As a reminder, this conference is being recorded and broadcasted live on the Investor Relations website at [www.grupocarrefourbrasil.com.br](http://www.grupocarrefourbrasil.com.br). A slide presentation is also available on this website. The replay of the -- the presentation will be controlled by you. The replay of this conference call will be available until November 15th via phone on 55 11 3127-4999, access code: 51500973.

Before proceeding, let me mention that forward-looking statements that are being made under the safe harbor Office Securities Litigation Reform Act of 1996. Actual performance could differ materially from that anticipated in any forward-looking comments because of macro conditions, market risks and other factors.

With us today in this conference call, we have Mr. Noel Prioux, Chief Executive Officer, Sebastien Durchon, Chief Financial Officer, Roberto Mussnich, Director, President of Atacadao, Jose Luis Gutierrez, Officer of Carrefour Brazil, Paula Cardoso, Director, President of Carrefour Solucoes Financeiras and Daniela Bretthauer, IRO. First, Mr. Noel Prioux and Sebastien Durchon will comment on 2017 third quarter and nine months results

and provide concluding remarks. Afterwards, management will be available for a question-and-answer session.

It is now my pleasure to turn the call over to Mr. Noel Prioux for his initial comments. You may proceed, sir.

## Noel Prioux

Good morning, everyone and thank you very much for joining us on this call. I am Noel Prioux, and as you know, I became CEO of Grupo Carrefour Brasil last month. I am delighted to be with you today, and I will do my best to make these introductory remarks in Portuguese, or at least in my best Portunhol.

It's a magnificent challenge to take over the helm of Grupo Carrefour Brasil, and I would like to take this opportunity to thank the team for the work they have done and successfully completed the IPO and bring the company to where it is today, the leader in food retail in Brazil.

I have only been in this job for a month. So, I am sure you will understand that I am going to leave the presentation of the results to the oldest in the house, Sebastien, whom I have known for six years, Roberto, for 10 years, Jose Luis, he worked with me in Spain 10 years ago and Paula, that I know from our meetings in France. However, before I leave the call, I would like to make a few observations. First of all, my short time here has reinforced my conviction that Grupo Carrefour Brasil has excellent, dedicated teams on which we can count on keep developing the company further. What I have seen has also strengthened my opinion that we have very solid foundations on which to grow in the future. I will not run you through a catalogue in detail, but I just wanted to give you a flavor of some of the key pillars that the company is working on.

First, we intend to maintain a dynamic pace of well-balanced multi-format expansion with further openings of Atacadao and Express stores. Secondly, we will continue to implement our initiative stores productivity and efficiencies throughout our business. Thirdly, we will derive the full benefits from the roll-out of the Atacadao credit card, whose roll-out is now completed and which has already led to an increase of -- 15% increase in average ticket by cardholders.

Fourthly, we will also continue the roll-out of our digital strategy, growing our non-food marketplace and our recently launched food offer, through the app called Meu Carrefour. And finally, we will benefit from the enhanced financial flexibility that comes from our solid balance sheet and a better gross debt. We will have the opportunity to discuss all of these subjects in the future.

But now, I will leave the call and I will hand it over to Sebastien, who will comment on our third quarter performance and also he will speak about the year to September figures.

## Sebastien Durchon {BIO 20242758 <GO>}

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Thank you, Noel. I will start by speaking about consolidated sales performance in Q3 on slide five. Overall, our gross sales in Q3 expect for Petrol grew 5.5%. This is a very strong performance given the environment in which we are operating, marked by very sharp food deflation.

If you look at the chart on the right-hand of the slide, you will see that we faced a particularly challenging comparable base, as the food inflation in Q3 of last year was running at 16%, whereas in the same quarter, it was a negative 5%.

Growth this quarter was driven by expansion, which accounted for 5% of growth in the quarter, which reflects the opening of 72 stores over the past 12 months. Most stores are Atacadao format and also Express convenience store. LFL, like-for-like growth in the quarter was 1.1%, driven mainly by Atacadao.

In addition, we also benefited from the growth of our non-food e-commerce, which is gathering momentum. In the quarter, we saw a single digit growth in food sales and double-digit growth in non-food. The calendar effect was slightly favorable in the quarter at 0.1%.

Also note that this quarter was also impacted by the temporary closure of the Atacadao store in Rondonopolis, which suffered extensive damage from a fire in May. Without that effect, our sales would have been up by 6.3%. The Rondonopolis store was reopened at the end of September, so we should see a positive contribution in Q4.

Let's now turn to slide six that shows a simplified P&L, which shows, as in previous quarters a solid underlying performance despite the short-term impact on our profitability caused by regulatory changes on revolving credit that impacted Carrefour Solucoes Financeiras.

Our results also reflect this quarter, as previously announced, the positive impact of ICMS-ST tax credits. ICMS-ST is a tax that we pay to our suppliers, when we buy from them on a presumed expected margin on those goods when they are sold to the final consumer. This tax is levied at varying rates on a state-by-state basis.

As you know, the Supreme Court of Brazil ruled last year that companies could reclaim in the form of tax credits, any overpayment in taxes if their real margins ended up being lower than the presumed margin. This quarter, we included in our results the tax credits for the first nine months of the year in our gross profit.

This largely explains the 91 basis points improvement in our gross margin, which stood in the quarter at 21.7%. In addition, we also recorded this quarter, tax credits from 2012 to 2016 amounting to 750 million. These credits from the past are in non-current line of our P&L, so that you can easily distinguish between what is recurring and what was a one-off situation. Net sales in the quarter stood at about BRL550 million, up by 4.9% and in the context of sharp food deflation that we already described before.

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Adjusted EBITDA was up by 6.9% to BRL845 million. If we exclude Carrefour Solucoes Financeiras, adjusted EBITDA in our Cash and Carry and retail operations was up 17.8%. Our adjusted EBITDA margin was up by 7.2%, up by 13 basis points and the adjusted EBITDA in our Cash and Carry and retail operations, excluding CSF, was up by 70 basis points.

So, net income, Group share reached BRL562 million, a gain of 125.6%. So, that was due to the recognition of ICMS-ST tax credit. But if we exclude all non-recurring revenues and expenses, our underlying performance remains very sound and net income up by 17.5% in Q3.

Let's now look at the performance of each of our segments and I will give the floor to Roberto, CEO of Atacadao, to comment on our Cash & Carry operations.

Net income Group share reached BRL562 million a gain of 125.6%. So that was due to the recognition of ICMS-ST tax credits, but if we exclude all non-recurring revenues and expenses our underlying performance remains very sound and net income up by 17.5% in Q3. Let's now look at the performance of each of our segments and now give the floor to Roberto, CEO of Atacadao, to comment on our Cash & Carry operations.

### **Jose Roberto Meister Mussnich** {BIO 18298845 <GO>}

Good morning, everyone. Thank you, Sebastien. So, let's look at slide number seven. On this slide, Atacadao posted another very strong quarter with growth sales up by 5.6% in gross sales in this quarter, reaching 8.5 billion. Growth was driven by expansion, as we opened eight stores and one wholesale operation since the start of the year, of which four stores only in Q3.

Like-for-like gross sales at Atacadao were also up by 1.6% in Q3. This growth was achieved despite -- if we look at our challenging comparable base, so it was despite that and despite a particularly sharp drop in food commodities, which account for a significant share of our sales. This was offset by a significant increase in volume and also tickets in the stores.

Our gross profit was up 21% in the quarter to 1.2 billion in the quarter, and gross margin was up 205 basis points to 15.9%. So, that was a result of the recognition of ICMS-ST tax credits as mentioned previously by Sebastien. However, if we exclude this one-off tax gain, our gross margin would be up by 56 basis points to 14.4%, notably due to enhance commercial efficiency in the quarter in addition to a reduced shrinkage.

Adjusted EBITDA of Atacadao rose 34.7% in Q3, whereas our EBITDA margin reached 7.9%. Here too, stripping away the gains from tax credit, which were positive, the underlying performance was very solid with adjusted EBITDA margin rising 21 basis points to 6.4%, reflecting continued efficiency gains in our operations. So, these are the comments we have and we will be available to take your questions later on.

With that, I would like to give the floor to Jose Luis Gutierrez, who will present the quarterly performance of our retail operations.

## **Jose Luis Gutierrez** {BIO 18843096 <GO>}

Good morning, everyone. Thank you, Roberto. Let's move to slide eight, where I will present the results of Carrefour Retail. We continue to post sales growth. Gross sales, excluding petrol rose 5% because of the result of four factors. As announced before the expansion of our stores, we opened 27 new Express stores, the launch in Q3, 2016 of non-food e-commerce, the reopening of Jardim Pamplona Flagship store and good performance of non-food. These four factors compensated for the strong deflation in food prices in the market as Sebastien mentioned.

Express convenience stores and e-commerce continued to grow their contribution to our total sales and now account for 6% of our overall retail sales versus 2% in the same quarter of the year before. Non-food sales continued to show dynamism and grew again in double digits, notably in consumer electronics.

Our gross profit rose 2.2% in our retail operations, reaching BRL1 billion in the quarter. Gross margin dropped 39 basis points to 25.3%. And this is a consequence of change in the mix of format, mainly as a result of greater participation of e-commerce and the sales mix and the strong growth of consumer electronics, which carries lower margins.

Adjusted EBITDA decreased by 20% with margin of 4%. This reflects what we could call a squeeze effect, as we faced deflation in prices, while at the same time, we had an impact in 2016 inflation on our 2017 costs, the strong carryover effect of past wage inflation.

Indeed, we had a 9.6% wage increase in 2016 because of collective bargaining negotiations, reflecting past inflation. Please note that the recently concluded collective bargaining negotiations for the coming 12 months, resulted in a much lower wage increase of 1.7%. So, this scissor effect is easing going forward.

Now, I'll give the floor to Paula Cardoso, who will comment on the performance of our financial operations.

## **Paula Cardoso**

Thank you, Jose Luis. Good morning, everyone. Carrefour Solucoes Financeiras' total billings and our credit portfolio continued to show significant growth rates in the third quarter, while our results continued to show the impact of the change in regulations on revolving credit, an effect that is gradually easing and that we are progressively offsetting.

As you can tell, on the chart on the upper left corner of slide nine, our total billings rose 22.8% in Q3 to nearly BRL5 billion. This reflects the solid growth of 12.6% in billings from Carrefour credit card, but also the encouraging initial results back of the Atacadao credit card, which represented billings of BRL414 million in fourth -- in this quarter.

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The roll-out of Atacadao credit card is now complete and it is now available in all 143 stores. Our total number of cardholders from CSF has reached 6.6 million, up by 11.9% on an annual basis. Our credit portfolio also continued its growth trajectory, growing in double digits by more than 11% over 12 months to BRL5.6 billion. At the same time, you can see on the slide that despite the challenging macroeconomic environment, we improved our risk profile, the percentage of loans overdue for over 30 days fell to 14% against 18.9 a year ago.

Now, loans overdue for more than 90 days over 90 returned to -- had a drop of 360 basis points when compared to the same quarter of the year before. This resulted in a drop of 5.3% in provisions for loan losses. Our coverage ratio is 14 point now, a substantial drop of 260 basis points when you look at the same period of the year before.

Revenues were down 13.2, or 73 million in this quarter to 475 million, reflecting the impact of the new regulation limiting the use of revolving credit since April 2017, as well as lower interest rates. However, the effect of the new regulation is gradually decreasing.

Now, turning to our results. EBIT in the third quarter of 2017 stood at 138 million, excluding the investments in the roll-out of the Atacadao credit card amounting to 38 million in the quarter. The figure of 146 million in third quarter 2016 doesn't take into account gains of BRL8 million in financial revenue from the bank's capital increase, also related to the launch of Atacadao credit card.

EBIT, excluding these effects was down by a limited BRL8 million, demonstrating that we are succeeding in gradually offsetting the impact of the change in regulation, notably through better management of our credit portfolio and costs.

Now, I will hand the floor back to Sebastien.

### **Sebastien Durchon** {BIO 20242758 <GO>}

Thank you, Paula. Now let's look at slide 10, and see how we strengthened and deleveraged our balance sheet following the successful completion of the IPO of Grupo Carrefour Brasil in July. As mentioned at the time of the IPO, we have largely used its proceeds to pay down our debt and strengthen our balance sheet.

As you see on the slide, we reduced our gross financial debt at the end of Q3 to 3.2 billion when compared to 6.3 billion at the end of Q2 by reimbursing most of our intercompany loans as well as another foreign currency loans. This reduced our leverage ratio of gross debt over EBITDA to 0.9 times from 1.8 times at the end of Q2.

In October of 2017, we issued BRL2 billion in promissory notes at a much lower cost than previously announced, lowering our overall cost of financing. We used good part of these proceeds to pay down the remaining intercompany debt, so our leverage ratio, net debt over EBITDA remains at roughly 1 time. Grupo Carrefour Brasil now holds only local debt and denominated in Reais and has no remaining intercompany loans with Carrefour Group. This strengthened balance sheet enhances our financial flexibility.

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On slide 11, we look at the key financial highlights of our performance over nine months, which showed further sales and profitability growth. Our gross sales reached BRL36 billion, up 8% despite food deflation in the quarter. Adjusted EBITDA was up 5.6% and stood at 2.4 billion, including Carrefour Solucoes Financeiras, and an even stronger increase of 16.2% if we exclude CSF. EBITDA margin stood at 6.9%. Adjusted EBIT at 1.9 billion grew 3.4% in total and 17.0%, excluding CSF. This amounts to an EBIT margin of 5.5%.

Finally, net income stood at around BRL1 billion and year-to-date up -- including CSF, up 56.8% and 82.9% excluding CSF, whereas the net margin rose 92 basis points to 2.9%. Excluding all other non-recurring income and operating expenses, net income was up by 14.6%, reaching 793 million .

I would like to conclude on slide 13 with some key takeaways of our third quarter performance. First of all, we posted robust sales growth despite strong food deflation. Second, our profitability, even though it was boosted by tax credits, it continued to show a solid performance even after the impact on regulation on revolving credit at CSF.

Third, Grupo Carrefour Brasil continued to invest in multi-format and multi-channel expansion in a well-balanced way, including the launch in October of our food e-commerce activity. And finally, we strengthened our balance sheet by paying down debt, thus gaining greater financial flexibility. Grupo Carrefour Brasil is well positioned for further growth.

Thank you very much for your attention. And Roberto, Jose Luis, Paula and I are now available to answer your questions.

## Questions And Answers

### Operator

(Operator Instructions) Our first question comes from Joseph Giordano from J.P. Morgan. You may proceed, sir.

### Q - Joseph Giordano {BIO 17751061 <GO>}

Hello. Good morning, and thank you for taking my question. In fact, I have two questions. My first question is addressed to Jose Luis Gutierrez. I would like to have a better understanding about the impact on the margins for e-commerce and non-food. I would just like you to separate things a little bit, so that I can see -- I can take a better look at the recurring margin. If you could please help us to identify the differences in the margins of both segments. And also, I would like to understand the non-food performance in the fourth quarter. I think that there has been a deceleration in the market.

And my other question is to Noel. I would just like to understand a little bit more because we are questioned by investors about Argentina. I mean, they report to you, but they are

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not part of the Grupo Carrefour Brasil. I would just like to understand what could be expected from that relationship or what can you tell us about that? Thank you.

**A - Sebastien Durchon** {BIO 20242758 <GO>}

I did not really understand your second question. Could you repeat that, please?

**Q - Joseph Giordano** {BIO 17751061 <GO>}

The question is about Argentina.

**A - Sebastien Durchon** {BIO 20242758 <GO>}

Okay. Yeah, I got it. So, let me start with the retail margin. I think it's important that we understand the current moment. Last year, we launched non-food e-commerce at the end of July, and August and September was just beginning of e-commerce. E-commerce last year didn't have a strong impact in our sales mix. This year, it's totally different landscape. E-commerce is about a year old, so sales increased significantly. And e-commerce share in the sales mix today is totally different when compared to that of last year. Well, it's no secret that e-commerce operates with a lower margin and this is what impacts Carrefour.

Another comment, I mean, as you spoke about non-food. It is true that in the last few months, we have been experiencing a two-digit growth in non-food and particularly in consumer electronics. And one -- and the -- this is a department in retail that has lowest margin. It impacts sales and it also impacts the gross margin mix. So, this is what I can tell you about this question.

Now concerning your second question, I think you understood that the Group announced a few weeks backs, the re-organization of the countries. So, we have a concept of geographic areas. Noel, in this new design of geographic combinations, we have Asia, Southern Europe, Romania, Belgium. There are many different zones. It's a design that does not impact Brazil, the new design of the Group does not impact Brazil. But Noel will take the role of organizing Argentina as well. So, to be more specific about this point, we do not have any plan to do any M&A with Argentina. We do not intend to do that.

**Q - Joseph Giordano** {BIO 17751061 <GO>}

Thank you very much. If you could please elaborate a bit more on the percentage points difference between food and non-food. This will help me out because it will help me look at the margins looking forward.

**A - Sebastien Durchon** {BIO 20242758 <GO>}

Well, you know that we do not give breakdown figures. But if you look at the information on that area, you will find that information very easily.

**Q - Joseph Giordano** {BIO 17751061 <GO>}

Thank you.

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## Operator

Our next question comes from Marco Calvi of Itau BBA. You may proceed, sir.

### Q - Marco Calvi {BIO 19854632 <GO>}

Good morning, everyone. My question is about retail -- wholesale margin. Pardon me. I just want to understand that given this very sound margin that you presented for Cash and Carry, whether you could also invest in pricing in the future? That is my question.

### A - Jose Roberto Meister Mussnich {BIO 18298845 <GO>}

Good morning, Marco. Thank you very much. This is Roberto. In fact, our margin in this third quarter had an increase, even if you exclude the positive effects of ICMS-ST in the margin. So the margin was up by 0.4 percentage points due to internal efficiencies. Well, it is certain that what we saw in the past, both in terms of margin efficiency in the three months in ICMS-ST, these are things that should be adjusted. I mean, if it is not adjusted by the government itself by creating another replacement product, the market has been adjusted itself according to the market average.

Our model, as we've been saying repeatedly, is a top line model with the sales model and we do have tools that can be used to invest in price and competitiveness, always keeping the same performance that we've been demonstrating in the last few years.

### Q - Marco Calvi {BIO 19854632 <GO>}

Perfect. Thank you very much.

## Operator

Our next question comes from Alana from Citi. You may proceed, ma'am.

### Q - Alana Imaizumi {BIO 19982383 <GO>}

Good morning, everyone. I have two questions. My first question is that, I would like to have a better understanding about provisions for operating expenses of 297 million. And the second is about LFL sales for Atacadao. Could you share with us, what part of that refers to Atacadao stores and what part of that is dilutions [ph]? Thank you.

### A - Sebastien Durchon {BIO 20242758 <GO>}

We'll start with provisions and then Roberto will talk about Atacadao. You are right, in the line other expenses in revenues, we, in that line, we recognized 750 million of ICMS-ST tax credit. And as I've said, that refers to previous years from 2012 to 2016 that we posted in that line to highlight that one-off event.

And also in that same line, we did a lot of work to evaluate the effect of this ICMS-ST tax credit and that's why we had that provision of close to 300 million. I mean, tax credits of 750 million, depreciation 300 million and so net is 450 million.

**A - Jose Roberto Meister Mussnich** {BIO 18298845 <GO>}

Now speaking about our stores and wholesale, we do not give you the breakdown figures, but we've been keeping the same balance between these two operations because one complements the other is strategically speaking. So, what we expect [ph] is the maintenance of margins and sales as we've been doing in the past 10 years very consistently.

**Q - Alana Imaizumi** {BIO 19982383 <GO>}

Thank you. Perfect.

**Operator**

Our next question comes from Mr. Cedric Lecasble of Raymond. Mr. Cedric, you may proceed.

**Q - Cedric Lecasble** {BIO 3744892 <GO>}

Yes. Good morning. This is Cedric Lecasble from Raymond James. I have three follow-up questions please.

So, first one, could you guide us through the food volume situation in hypermarket? And the second one, regarding Atacadao, what is your best guess or best estimate for the share of Cash and Carry globally in Brazil for this format? What would be the global share of Atacadao in Brazil? How much stores and formats? And what's the potential for store expansion in your view? And would it make sense eventually to remodel hypers into Atacadao?

And the last question is on your productivity measures in the retail area. Do you need a support from the environment to have some improvement in profitability or is it self-helpful? And could you help us maybe understand what were these productivity measures? Thank you very much.

**A - Jose Roberto Meister Mussnich** {BIO 18298845 <GO>}

Okay. Atacadao has continued to maintain its market share and it even grew this past year in a very consistent fashion. And we do have the potential to move forward into some other areas and we've been working on that. Our market share today is according to Nielsen, it's around 39% and 41% of market share.

Now in terms of possible expansion projects and also transformation of Carrefour stores into Atacadao stores, we have done that in the past in 13 stores and we are constantly alert as a Group, and we do not discard to that in the future. But it is still very premature to say anything further. We made 13 transformations in 2010 and 2011 and the result proved to be very successful.

**A - Sebastien Durchon** {BIO 20242758 <GO>}

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And now adding to Roberto's remarks about the hyper model, we went through two years of very strong prices in Brazil and the moment of crisis with a focus of customers was mostly in price. And this is an environment that favors Cash and Carry and therefore, we understood that it would be important to have several formats. At Carrefour, we have different formats catered to different customers and different moments of the economy.

So the hypermarket has this advantage because in a most favorite moment, we can cater to customers differently. I'm not going to talk about -- much about Cash and Carry. We have already many initiatives on demands. And we will have more opportunities down the line to talk more about this initiative. Looking forward, we are working diligently in that regard.

## Operator

Our next question comes from Mrs. Fabienne Caron of Kepler. Mrs., you may proceed.

### Q - Fabienne Caron {BIO 16384276 <GO>}

Yes. Good afternoon. This is Fabienne Caron from Kepler. Two questions from me. The first one, on Carrefour Retail and looking at your margin decline in Q3, excluding the tax credit of 190 basis points, it looks, as you commented on the gross margin and you took about a shift towards consumer electronics and towards e-commerce. So, I'm wondering if you expect a better trend in Q4 for Carrefour Retail given the weight of Q4 in the full year. And the second question is on the tax credits. Can you tell us how much is cash, please? Thank you.

### A - Sebastien Durchon {BIO 20242758 <GO>}

On your first question, the effect on gross margin of Carrefour, once again, it is very important to bear in mind that in the last few months and particularly in Q3, we had a lot of food deflation. This fact alone already changes the mix between food and non-food and when it comes to consumer electronics, our margin is lower. And in addition, as I said before, we also have the impact of the ramp-up, which is stronger this quarter vis-a-vis last year's quarter. And in e-commerce, that has made total margin of Carrefour go down.

Now, speaking about your second question related to the tax credits for ICMS-ST, ICMS-ST tax credit in Brazil is -- it's a subject. I mean, we have to recover all of these credits and that takes some time because what we did in the third quarter was to document all the credits to recognize them in our accounting numbers. We do have the capacity to recover all of these credits within five to six years, and we are also working hard to find solutions available in the Brazilian legislation to expedite the recovery of the credits.

## Operator

(Operator Instructions)

### A - Sebastien Durchon {BIO 20242758 <GO>}

I think we have time for one more question. Okay. If there are no further questions, thank you all very much and I wish you all a very good day.

## Operator

Grupo Carrefour's conference call is now concluded. I would like to thank you very much for participating and have a good day.

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