

Q3 2021 Earnings Call

Company Participants

- Guillaume Gras, Chief Financial Officer and Investor Relations Officer
- Jorge Faical, Chief Executive Officer

Other Participants

- Unidentified Participant

Presentation

Operator

Good morning, everyone. Thanks for standing by and welcome to the Earnings Conference Call to discuss the results of the Third Quarter of GPA. For those who need simultaneous translation, we have this tool available on the platform. To do this, just click on the Interpretation button via the Globe icon at the bottom of the screen and choose your preferred language, Portuguese or English. For those listening to the video conference in English, there's an option to mute the original audio in Portuguese, by clicking on Mute Original Audio.

We inform you that this conference call is being recorded and will be made available on the company's website, where the complete material of our earnings release is available. You can also download the presentation using the Chat icon.

During the company's presentation, all participants will have the microphone disabled. Then we'll start the Q&A session. (Operator instructions) We recommend that questions should be asked at all at once.

We point out that the information contained in this presentation and any statements that may be made during the video conference regarding the business prospects, projections and operational and financial goals of the GPA constitute beliefs and assumptions of the company's management, as well as information currently available. Forward looking statements are no guarantee of performance. They involve risks, uncertainties and assumptions, and therefore, depending on circumstances that may or may not occur. Investors should understand that general economic conditions, market conditions, and other operating factors could affect GPA's future results and could lead to results that differ materially from those expressed in such forward-looking statements.

Today with us are the CEO of GPA Jorge Faical; the CFO and Investor Relations Officer, Guillaume Gras; and CEO of Grupo Exito, Carlos Mario Giraldo; and CFO of Grupo Exito, Ruy Souza.

I'll turn the call to Guillaume Gras for him to start the presentation.

Guillaume Gras

Thank you. Good morning, everyone. I would like to thank you for attending the earnings call of the results of GPA Group. I will start the presentation by briefly talking about our financial performance and then I will hand the floor over to Jorge who will comment on the operational highlights for the period, strategy and business perspectives.

On Slide 4, we present the numbers of the consolidated performance. The group's consolidated sales totaled BRL12.1 billion in the third quarter of 2021 in line with the third quarter of 2020, and growing by 11.1% compared to the Q3 '19. In a challenging environment, we maintained or strict control of SG&A, which decreased by 0.6 bps in rate this quarter, and which also presents in the nine first months of the year, a dilution of 10 bps compared to the same period of last year.

Our consolidated EBITDA reached BRL794 million, down 1.2 points versus last year impacted by the Brazilian activities, which will be discussed later. In the period of the first nine months, we had an EBITDA of BRL2.6 billion in line with the same period of 2020, and 13% higher than that in 2019.

Moving to Slide 5 now, we've presented the results of GPA Brazil, which account for 54% of the group's revenues this quarter. From a macroeconomic point of view, we faced a third quarter that was much more difficult than expected, and that put pressure on both our sales and our margin. Strong inflation and still high unemployment rate holding back the recovery of consumption. In this context, some store sales were in line in the Q3 '21 versus Q3 2019 and grew by 3.6% in the first nine months of 2021 versus the same period of 2019.

In the vision excluding hyper and drugstores, which are models that as announced will be discontinued, grew by 8.4% in the quarter when compared to the Q3 '19 and growth of 10.1% versus the first nine months of 2019.

E-commerce is growing in importance in the business strategy. In Brazil, we broke the record reaching a GMV of online operations of BRL475 million in the quarter, even higher than that of GMV in the Q4 '20, which had seen seasonal effect such as Christmas and Black Friday. Proximity formats were also highlights in sales, posting double-digit growth for the 13th consecutive quarter.

Gross margin in the quarter was 23.7%, 2.5 bp below Q3 2020, reflecting the repositioning of regular prices and the resumption of promotions, mainly in the extra paper format in order to mitigate the effect of strong food inflation, the high unemployment rate and increased competition with cash and carry. In the comparison between the nine month period of 2021 and 2020, the gross margin remained stable at 25.1%.

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In order to mitigate the effect of the investment price, we continued our work of strict SG&A control to improve productivity rates and gain efficiency in the operation of stores and distribution centers. This quarter, we had a delusion of 0.1 bp to 19% of net revenue, driven by the initiatives implemented over the last 12 months. In the first nine months of 2021, the level of dilution reached 0.5 bp compared to last year, reaching 18.4% of net revenue.

As a result of these effects, we presented an adjusted EBITDA of BRL369 million in the third quarter 2021, down 2.3 points against last year, a loss largely concentrated in the hypermarket format, driven by the investment prices, year-to-date at the drop from 30 bps versus last year and remains stable versus 2019, both in value as in rate.

We move onto Slide 6, where the results of Grupo Exito which accounted for 46% of consolidated sales reaching BRL6.4 billion in the quarter, an increase of 7% compared to the third quarter of 2020, which includes negative foreign exchange rate impact. At constant exchange rates, total sales of Grupo Exito sales grew by 14.6% compared to the third quarter 2020 and 16.4% when compared to the third quarter 2019. Growth was driven by the reopening of the Colombian economy and by the commercial events, that accompany is recovery.

The digital strategy continues to show positive results reaching BRL572 million with penetration of 9.3% of sales. In addition to the good performance in digital and in physical stores, the result in Columbia has important contributions from complimentary business, such as Tuya credit card activity and the improvement in real estate businesses.

In Uruguay, the growth was below inflation and the finally in Argentina, we recorded an increase above inflation with a reduction of circulating restrictions in the country and an increase in the traffic of customers and in stores and galleries. In this context of recovery of sales, Grupo Exito managed to improve its gross profit of 70 bps as a result of both better negotiation with suppliers and the greater share of complimentary activities.

With regard to expenses, it's worth mentioning that they grew below inflation in all countries where Exito Grupo operates, driven by the gains in operational efficiency in the stores. Thus in the third quarter 2021, expenses totaled BRL1 billion up 1.6% against last year, with an important delusion of expenses reaching 17.4% of net revenue.

As a result of these effects, we presented an adjusted EBITDA of BRL494 million in the third quarter 2021, a growth of 13.3% compared to the third quarter 2020. The adjusted EBITDA margin grew 0.5 bp versus the third quarter 2020 and reaching 8.7% of the net revenue.

And finally on Slide 7, we kept our leverage level low at 2.1 times our EBITDA. We ended the quarter with a cash position of BRL4.5 billion corresponding to two times our short-term debt, which ensures excellent liquidity. It's important to mention that in this position, we still haven't had an impact from the transactions of hyper stores in the amount of BRL5.2 billion.

I end my presentation here and I would like now to turn the floor over to Jorge. Thank you.

Jorge Faical {BIO 21768322 <GO>}

Thank you, Guillaume. Thank you to everyone for joining us on our earnings results call. Guillaume showed us the results of Q3 of the year up to date and I will highlight strategic operating factors of our business for everybody.

First and foremost, it is important to highlight our strategic decision to exit the hypermarket format. This is the most transforming transformation that GPA has carried out in its recent story in the country. We announced in a call this transaction and now I'm strengthening some points because this is important in order to understand not only the performance of Q3, but also understand our future.

We carried out a transaction of 71 stores in this format to our site and 32 remaining stores. We're going to close four of them and 28 stores will be converted or to Mercado Extra. This is a transaction of BRL5.2 billion, including all stores and all the assets of GPA within these stores. Now it is important to highlight that this transaction has a potential of creating value and compared to anything that we have done in our history. Now, this is a unique business opportunity in order to focus all our strategic rationale on businesses that generate more value and profit.

Here, we have premium Pao de Acucar -- mainly the Pao de Acucar brand, our proximity formats that show a positive trend in the country and obviously E-commerce that is reality into buying -- to do their groceries through e-commerce.

Now with this, we will have a leaner structure with much more focused and -- on the main basis, our foundations of retail. We are going to broaden here or we're going to focus more on our results on the retail operations day and day, providing the best assortment and the best service to our customers, a better quality of product to focus on logistic change in order to avoid out of stocks. These are operational strategies, not only to provide more value to our shareholders, but also to our customers. Here, we are simplifying things in an efficient fashion.

Now this decision enabled us to have a higher EBITDA margin because what remains with XE performance have a greater margin mix and with a bottom line profile that is more favorable. Therefore, this will favor our cash generation, not only the proceed of this transaction generating positive impact on our leverage, but the cash of the future business and after the transition, we will have a brand new company that will be completely transformed. We have to highlight that this transaction was carried out with a high level of governance with the vote of our independent board members.

On this slide, with the exit -- with the exit of the hypermarket business, here we're creating three platforms that are not different from what we've seen in the past quarters, but here it's clear and here you can see what platforms are we using to expand our business.

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In Brazil, our growth pillars, the first one would be digital. I've been talking about digital during this quarter. We broke the record in our history. We had BRL475 million in sales. This is more than the last quarter of last year when we had Black Friday and Christmas. And during the third quarter, we were able to do this. So BRL475 million is very important. This represents an amount of orders higher than what we had in 2019. So practically in one quarter, we had more orders than in the year 2019.

If you analyze these BRL475 million and you carry out a yearly projection, this is a business of around BRL2 billion. In 2019, we sold between BRL300 and BRL400 million and now we have a business of BRL2 billion in our digital area. We are very proud of this result of these construction. We have a good scenario and this is important for stakeholders and shareholders to know. Now our digital is early stage. So this means we are making our first steps. The market has a potential to grow, and I'm going to talk more about this.

The Pao de Acucar brand is also one of our growth pillars for the future. All our store retrofits with the proceeds of the transaction. We are going to accelerate this. We announced that our G7 model that is the latest model that favors the purchase of perishable goods that can give better -- that provides better services is growing above the average of others stores.

So at the end of next year, we will refurbish all the stores of Pao de Acucar, turning them into a G7 model. Therefore, this is where we are going to invest part of the proceeds that we received.

We are also going to accelerate the expansion of the traditional form at the supermarket format of Pao de Acucar. We had announced 15 new stores up till 2023. Now we commit to open a 100 stores of Pao de Acucar until 2024. This is an accelerated expansion. We are prospecting properties throughout the countries, and we are going to accelerate even more these expansions.

Currently out of the 100 stores, we have 14 new stores that have been approved and around 14 conversions of hypermarkets. So we have around 28 new Pao de Acucar stores, and we are practically in the beginning of the project, or we're under construction. Two construction sites underway, one in [ph]Limede this year and the other one in Sao Paulo in the beginning of next year.

And now we will start with a pipeline. This would be like an industrial expansion, and this is how we see Pao de Acucar. Today within GPA, now the same store sales in Pao de Acucar, they are still below inflation level throughout the two years. We grew 8.4%. vis-a-vis the same quarter of 2019, but there is a reversion in the Pao de Acucar market share trend. Pao de Acucar growing above this Brazilian self-services and above other the premium players. So here, our perspective is very positive for the banner.

Now, the Proximity pillar, we also are accelerating our expansion program. Here we would like to -- we will have a 100 new stores until 2023. These are Proximity stores. We have opened three stores this year. Then we have over 20 stores that are approved, that will

go through retrofit and will be expanded. Now the Proximity format has had 13 consecutive quarters of double digit.

This is very important and with this, you can see that we have a strong format to roll out, and this is a profitable format. And out of the national chains, we are one of the few that have a replicable format and positive model.

We are proud to announce that we have a new member that is called Pao de Acucar Fresh, that is for the vegetable and fruit market and perishable product. This would be butchery, fish mongrel bakery in order to service neighborhood -- an expanded neighborhood. This format is between Minuto Pao de

Acucar and a traditional supermarket format that has between 400 square meters and 700 square meters. It has great potential throughout Brazil to be copied we've already opened the first store in (inaudible) and we have a store in the City of San Paolo.

We are convinced that this format is going to work because number one, there is a strong demand in the country for convenience neighborhood formats to compete with this green grocery stores. And we have a great deal of expertise and this format can result in hundreds of futures stores because of the success of the first units that are being opened. These three pillars, I believe -- that are the three pillars that I would like you to bear in mind, because these are the growth pillars. This would be what we call the new GPA and formally, it is the leaner and more fluid GPA and a faster GPA in order to achieve growth.

Now, let's go to the next slide. Now, when -- still on this matter and about our portfolio with the exit from the hypermarket business on the right hand side, you can see that we are the leader in retail in Brazil, in food. We have to highlight this. We continue with a big size. Although we have exited 71 Hiper marks. We have around 697 stores here amongst the different formats that you can see here.

In the future until 2024, we will total 808 stores. Therefore, you can see Pao de Acucar from 181 to 281. Proximity from 90 to 190 stores and also Mercado Extra from 146 stores to 160 stores, approximately. These are approximate figures but we'll recover the size of our company in three years with these transactions in a more profitable way, and in a self-sustainable way.

In Pao de Acucar, that is our main brand for the future be it supermarket or fresh, or Minuto, we will strengthen the brand as a whole protecting the asset that is one of the most valuable assets of the Brazilian market. We are going to strengthen its concept the purpose of loyalty, the purpose of happiness.

We will continue -- we will rescue our loyalty program, sustainability SG&A, one of the main levers. I talked about recovering the foundations of retail guarantee, differential assortment, new ways of pavement, digital solutions, greater integration between brick and mortar stores and digital self-checkout. So we are confident regarding this future company.

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Now talking about digital on Slide 12. On the right hand side, you can see our [ph]Mandalla that would be the fronts of our ecosystem. It is important to highlight the center of this chart that is our mantra, and this demonstrate our mission since we declared ourselves as a digital company of open collaboration and we are going to be wherever the customer is. It doesn't matter if they're in their own platform, third-party platforms, market platforms. We want to be right beside the customer, wherever they are.

In this chart, you can see that the fixed assets are the beginning of our journey. One of the greatest strengths that we have here are the amount of stores that are 800 stores, in the future 700, right now that are like distribution centers so that we can service fresh and we can provide fresh products and with speed to our customer, wherever they are.

On the bottom part, you can also see something that we call total addressable market. This is the available market in Brazil is around BRL7 billion and this market in five years, we estimate that it will represent BRL45 billion. This is a growth of seven times, and we want to be part of the game and we want to be strong in this game.

So what did we deliver throughout these quarters? I've already talked about results, but some deliverable specially in the 1P platform in our own site. Pao de Acucar and Extra. We've launched social log-in. We launched fresh baskets where the customer can buy a basket with fresh products. We can deliver on Sundays, click and pick up in one hour that now after the restrictions, this as an important tool to deliver products to our customer.

Fixed payment that represents practically 10% of payments in our sites. The beginning of electric -- deliveries through electrical cars in San Paulo and Rio de Janeiro also contributing with the ESG. We're starting to sell through WhatsApp. We are already working strongly during this quarter with a pilot project, but during the next quarter, we will launch WhatsApp via bolt and also personal delivery. This will be hybrid. There are a number of initiatives to deliver to disabled people and elderly. Therefore, we are strengthening the use of our own platforms.

Now our decision here of carrying out business with partners since the beginning of the year, this was more than an assertive decision. We have accelerated our sales to partners that represent more than 40% of our total sales in the digital platform. We would like to thank our partners to all of them that have been supporting us. We have been able to carry out and a number of tools to work with the Pao de Acucar and Extra customers, some initiatives that are interesting. We are launching our retail as a service platform. We started with a partner Omni refill, where we work with sourcing and logistics for home refill,

We've also extended our partnership with Mercado Libre beginning with extra brand and with Mercado Libre, we expand the sales of perishables and we have a list of nearly 3,000 items to be sold.

In the three platform it's also important to mention that this quarter, in addition to our growth of sellers and SKUs, we have also launched our service of fulfillment, which is very important for the marketplace to operate by means of our company GPA lock that is

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going to deliver at a quicker pace to the consumer, freights ever more competitive, and also offering the possibility of -- traceability of our orders with our sellers. This, we do always preserving our service level to the consumer as our first priority.

It's also important to point out that this is the border that Stix our coalition program, completes one year of existence -- one year of existence of six company. It has a right to reach the breakeven point. It starts to be profitable already. And more important than that is that the Stix resumption grows every month based on the improvement of this new program.

I would like to use this opportunity to thank for all the partners of higher (foreign language), where we have been managing to have a very good coalition program for the growth of Stix. So our digital initiative, as I always say, is one of the main platforms for the future growth of the new GPA.

In the next chart, I am going to discuss some highlights of Exito. Exito presented great results for the quarter. This result came by means of different initiatives and particularly the digital segment reaching 9.3% of penetration at the same penetration as a coincidence of GPA, with different initiatives, different levels of maturity, reaching a maturity level of the digital business.

In this quarter, we launched our Turbo-Fresh delivery service with a partnership with Rappi. It's done in Carulla stories. It's a disruptive model that has been very successful in Columbia. And this has been driven by very successful partnership for some years.

Omnichannel reached 12.2% in the first nine months of this year. More than six million orders via less miles have been delivered. And the market place already accounts for a 27% of the digital sales, especially in Columbia. It's always important to mention that one of the highlights of Grupo Exito is always the modernization of the portfolio. The modernization of the portfolio includes modernization in all banners of the group, beginning with Exito, that accounts for nearly 30% of the sales in this format in Columbia, and it has been growing more than the average, and it's a very successful format.

We have been expanding this format ever more in Columbia and Carulla and FreshMarket are related to just seven in the country and 30% of share in the business and growth above average and the low cost model, which also grew accounts for 70% of the sales in Colombia with highlight to Super Inter Vecino, that accounts for 34% of the sales using this banner.

The business improvement in Colombia in Group Exito recorded 17% of growth which was driven by an improvement, not only of the macroeconomic scenario of the three countries. The reopening of the market, which is stronger than what we saw in Brazil, a recovery of the market and the level of confidence of the consumer in those countries, but of course, a result of the attitudes.

So we would like to congratulate our colleagues in Columbia for their extraordinary work they've done, especially in this quarter. I would also like to point out to that the businesses

in Columbia and Argentina accounts for a very important part of which is the real estate segment that have also some exponential growth.

To end this first part, I would like to discuss the ESG agenda, which is our form of total priority for us. It includes different work fronts considering the main pillars, climate -- fighting climate change, promoting diversity and inclusion and social impact.

I'm not going to read the chart, but you can see some of the initiatives. But I would like to point out to the development program for black people, with the partnership with Zumbi dos Palmares University. And I would like to thank them for the support and the partnership. 261 graduate women have participated in a leadership program and we have 264 new places for the new group.

We are more than 52% of our staff declared themselves black and for the case of social investments, this was in a typical year and we are very proud to say that 3,600 metric tons of food have been donated to important institutions and in Columbia, more than 57,000 children have been favored by the program of complimentary nutrition for children.

And with that, I end -- okay, one more slide, please. And these are the main messages for this quarter. So the first one is the priority of ESG and absolute leadership in food e-commerce and the market can be exploited and we are going to strengthen this leadership wherever we are.

The exit of hypermarket format in Brazil accelerates the digital platform. It accelerates the profitable formats as I said, Pao de Acucar and Proximity, especially, and focus on the execution and on operational excellence with the basis in the retail key aspects and the strengthening of our cash, reducing our exposure and leverage considering the increase in interest rates expected for the months to come. So our innovation and omnichannel initiatives continue, and these are the key messages for the quarter.

I would like to thank you for the attention and we are now going to open the Q&A session.

Questions And Answers

Operator

And now we are going to start the Q&A session. (Operator instructions) Our first question comes from [ph]Felipe, sell side analyst at Citibank. Philippe, we're going to open your microphone so that you can ask your question. Please, you may proceed.

Q - Unidentified Participant

Good morning, everyone. Can you hear me?

A - Jorge Faical {BIO 21768322 <GO>}

Yes. Go ahead, please.

Q - Unidentified Participant

Thank you for the opportunity to ask a question. And the idea on our side is to understand what's the promotional dynamics for the year. You had some difficulties in terms of macroeconomics. So what do you have in mind for the fourth quarter 2021?

And looking ahead for 2021, how are the main banners going to be positioned in the group, especially when we refer to Pao de Acucar. Thank you.

A - Jorge Faical {BIO 21768322 <GO>}

Thank you, Felipe, for the question. In the fourth quarter, we understand that that this is going to be a quarter with a transition of the supermarkets. We are going to deliver the empty stores with no goods, no merchandise, the 71 stores to our site in the middle of January. So we are very cautious in terms of purchases with the inventory levels. And we are very cautious in terms of the promotions for the end of the year.

So we are going to -- we're going to adopt a model of destocking creating a sufficient opportunity. So we are going to have Black Friday and Christmas to sell out all inventories or stocks and this is also our project related costs.

Part of the proceeds are going to be used -- part of it are going to be used for those -- marking down those stocks and also to the constructions of our site. So the Black Friday is going to be very traditional so as to say in the first -- like the first years of Black Fridays in the United States that was focused on selling the stocks. So we are going to sell out our inventory, the store intention.

As to other formats, there is a growing demand from consumers for more promotions. They're focused on price. So price is key considering the macroeconomic situation. We are probably facing one of the most distinct situations that we have gone through when the income is very low and the inflation is very high. So price is key now. So price is a key factor in promotion is a very important component related to price.

Pao de Acucar and Mercado Extra are going to have very strong promotions, both for Black Friday and for Christmas. We expect some growth for Christmas considering that Christmas 2020 was very weak. So we expect to have an effect of a situation where people will gather together with their families. And we expect that may be a repressed demand for gifts and food.

For 2020, we are in the midst of our strategic planning and we have been very cautious. The scenario is very volatile. So it's very difficult to make any sort of projection, Felipe. So honestly, I would not like to take risks and to provide any future scenarios that could be very precise.

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So the point is that we are very attentive to what's happening to the market. We are looking at everything that can happen. We are also watching whether there's going to be any government support by the government, but somehow it's a scenario that demands us to be very cautious.

Q - Unidentified Participant

Okay. Clear. Okay. Thank you, Faical.

Operator

Our next question from (inaudible). You may proceed and pose your question.

Q - Unidentified Participant

Can you hear me?

A - Jorge Faical {BIO 21768322 <GO>}

Yes perfect.

Q - Unidentified Participant

Now, piggybacking on planning, because I know that you don't have total visibility regarding your planning for 2022, but how can we see the EBITDA margin after hypermarket?

You know, that Pao de Acucar is double digit. Can we expect something close to double-digit when we have hypermarkets with their adjustments?

And another question about Fresh, now is the profit of margin very close to what you have in pound?

A - Jorge Faical {BIO 21768322 <GO>}

Well, I'll start by the second question. Fresh, yes, Fresh, we are pursuing double-digit profit. All the business model is made for this to happen. So as soon as two and three months of operation go by, we will know what a replication appetite will be for this format.

Now regarding the EBITDA margin. Now, mechanically, it will increase with the exit of hypermarkets. We expect an increase of EBITDA margin after the transition stage that will take place until Q1. Something perhaps will remain for Q2 next year. But our target is to end the transition at the end of Q1 of 2022. And here we will observe in growth of bps. I'm not going to give you any guidance right now, but this is organic growth.

Now, please bear in mind that Pao de Acucar that is double digit, it will have between 50% and 60% of sales in the new GPA as of Q2 next year. Therefore, the margin EBITDA growth will be a natural consequence of this entire transactions that we're having with the hypermarkets.

Operator

(Operator instructions) Our Q&A session has come to an end. And now I would like to hand it over to the company for the final remarks.

A - Jorge Faical {BIO 21768322 <GO>}

Well, I would like to thank all of you for joining us. I would like to thank all the participants, all our partners as well, our suppliers, the industries that have constantly supported us in the evolution of this company.

We've had a Q4 in addition of it being a challenge because it's the end of the year. This is a challenging quarter because of the transition that we're undergoing from one company to another. So we are going towards a new GPA with a positive business prospect for our shareholders, stakeholders by and large, and the entire group with the lever -- the growth levers that are opening.

Now, the macroeconomic challenges continue being important. We must challenge them and we must overcome them. And in reality, there is a new opportunity scenario. We have the opportunity to grow in digital, also to change our value proposition, an opportunity to change our business model. And this is something that we're doing, and I've used this word throughout the year after different budgets, after different action plans.

Here we have a power of constant adaptation to the resilient reality, but we are strongly convinced and we are betting on this country. GPA, bets on Brazil, convinced on the pathways that we are taking without losing -- without forgetting about the operational efficiency and the focus on our customer. I would like to thank the team of GPA for all their effort, and there is still a lot to deliver.

So good morning, to everyone, and thank you very much.

Operator

Our video conference call has come to an end. The IR department is at your disposal to answer any further questions. Thank you very much to all the participants and have a good day.

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