

## Q3 2015 Earnings Call

### Company Participants

- Antonio Sergio Alfano, Chief Financial & Investor Relations Officer
- Fábio Schvartsman, Chief Executive Officer

### Other Participants

- Alan Glezer, Analyst
- Caio Ribeiro, Analyst
- Carlos F. De Alba, Analyst
- Jonathan Brandt, Analyst
- Lucas Ferreira, Analyst
- Thiago Lofiego, Analyst
- Victor Penna, Analyst

## MANAGEMENT DISCUSSION SECTION

### Operator

Good morning and welcome to Klabin's conference call. At this time, all participants are in listen-only mode and later we will have a question-and-answer session when further instructions will be given for you to participate.

I would like to remind you that this conference is being recorded and also being broadcast live via webcast and may be accessed at <http://cast.comunique-se.com.br/klabin/Q315> where the presentation is also available.

Before we proceed, I would like to clarify that forward-looking statements that might be made during this conference call related to the business perspectives of the Company, projections and operating and financial targets related to the growth potential of the Company, are mere forecast based on the Company's management expectation vis-a-vis the future of Klabin.

These forward-looking statements depend on market conditions and the general performance of Brazil, the industry, and international market, and therefore they are subject to change.

Today with us in São Paulo, we have Mr. Fábio Schvartsman, CEO; and Mr. Antonio Sergio Alfano, CFO and IRO. Initially, Mr. Schvartsman and Mr. Alfano will talk about the operating performance of the Company during this quarter, and afterwards they will answer questions that might be asked.

Now, I would like to give the floor over to Mr. Schvartsman. Mr. Schvartsman, you may proceed.

## Fábio Schvartsman

Thank you very much. Good morning, everyone, and thank you once again for your participation in this conference call. Once again we deliver a good operating performance, 15%. It was necessary - the challenged situation, especially in the Brazilian markets, Klabin with a lot of discipline has been focusing more on exports and export, 8% in volume already in the third quarter of the year on a year-on-year basis, showing that we have started to obtain results from this action focusing on the external markets.

In the domestic markets, of course, we know that it is very weak especially the corrugated box, and according to ABPO, in the third quarter of this year, there was a 5% drop in volume on a year-on-year basis, and Klabin had a similar performance. So it becomes evident, based on the figures that I have just mentioned, that Klabin has been using its recognized flexibility, focusing more on the export market and being able to offset the difficulties in the domestic market with the adequate performance and the results are behaving as expected.

I would like to mention especially the good performance of our coated board production that in the third quarter had the highest ever level of production reached by the Company that led to an increase in sales, both in the domestic and external coated board market. Maybe this is the highlight of the current performance of the Company.

I would also like to mention very quickly the Puma Project. The Puma Project, at the end of October, will be attaining over 90% of the work concluded in this mill. And this means that we achieved a lot of progress to such an extent that last week the first smoke was produced, symbolically, in the site by means of the beginning of production of steam so that we can start to blow the lines and we have just started the process. But nevertheless, it's important to say that this is just another evidence that Klabin's project will be ready according to schedule and with enough time to do it - do the commissioning of the equipment in order to allow a smooth start-up of this new mill.

As I always do, I would like to make a brief remark about our expectations for the next quarter. The next quarter should be extremely strong for Klabin. And the reason for that is that exports are accelerating, and we estimate an important growth in our exports in the fourth quarter where we will have growth vis-à-vis the previous quarter of about 10%, and we will achieve growth of about 30% according to the figures that we achieved in the same quarter last year. And, of course, this means a good quarter for the company. Reinforced by the fact that our plant efficiency right now has already reached the peak, we are able to have the maximum production of all our machines and therefore, the Company is taking advantage of this good moment for exports.

Thus, we can say without the possibility of making a mistake, that the fourth quarter will have a robust growth. In terms of results, vis-à-vis the fourth quarter of last year, and by

far, it should be the best quarter in this current year, and of course driven by exports and by the exchange rate that is at very favorable levels.

So, it is with pleasure that we are delivering a good quarter and with the expectation of an even best fourth quarter. Now, I would like to give the floor to Sergio Alfano, and he will go more into details about the Company's performance in the third quarter. Sergio.

## **Antonio Sergio Alfano** {BIO 4337533 <GO>}

Thank you. Fábio. Good morning everyone and thank you for participating in our call.

Klabin in the third quarter of 2015 showed 463,000 tonnes, the same level of the first quarter of the previous year. And taking advantage of the cost-competitiveness and the high quality of our products, Klabin increased the number of ports – of products for exports, as Fábio said, decreasing the impact of the slowdown in the domestic market in the third quarter.

The exported volumes grew by 8%, totaling 154,000 tonnes exported, reaching 33% of total sales, vis-à-vis 31% in 3Q 2014. With this increase in export, the sales to the domestic market were 309,000 tonnes, 5% lower year-on-year. Net revenue in 3Q 2015 including wood was R\$1.446 billion, a 13% growth year-on-year as well, impacted by the higher average exchange rate in this period.

And the participation of exports in total revenues went up from 24% in the third quarter of 2014 to 33% in the third quarter of 2015, which was a big leap. Unit cash cost, net of the non-recurring effects of other operating revenues and expenses was R\$2,007 per tonne, a 9.8% nominal growth vis-à-vis the third quarter of 2014. And this cost was impacted mainly by the higher cost inflation in this period, energy acquisition costs and also the input that are paid in dollars, and on the other hand, lower cost with the purchase of third-party papers and the harvest of wood in part mitigated the increase in cost in the third quarter.

EBITDA was R\$520 million, 15% higher than the third quarter of 2014, and the 17th consecutive quarter of evolution in our EBITDA. In the nine months of the year, EBITDA reached R\$1.372 billion, 13% higher than the same period last year. Consolidated net debt at the end of September amounted to R\$11.6 billion, a R\$3.5 million increase compared to the end of June, especially, due to the accounting impact of the exchange rate variation in the dollar-denominated debt and also the disbursements related to the construction of the new plant, the pulp mill in the period.

Indebtedness, we have no financial covenants linked to our debt. And the effect of the exchange rate variation in the period has no significant cash effect in the short run. And the net debt-to-EBITDA ratio closed the third quarter of 2015 at 6.2 times in reals and 4.6 times in dollars. And in terms of investment, Klabin invested in the third quarter R\$1.1 billion, being R\$970 million exclusively invested in the Puma Project.

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The works of the new mill with a capacity of 1.5 million tonnes of pulp continue to progress according to our schedule, and up to this time, the site was already 87% complete. In the physical evolution, the 75% of the total CapEx or the total disbursement already realized.

Very well now, Fábio and I will be available to answer any questions that you might have.

## Q&A

### Operator

Ladies and gentlemen, now we will start the Q&A session. Our first question, Thiago Lofiego, Bank of America Merrill Lynch.

#### Q - Thiago Lofiego {BIO 16359318 <GO>}

Good morning, Fábio. I have two questions. The first has to do with the future growth of Klabin and talking about machines, coated board machines, I would like to know about the capacity increases that we see both in Europe and in China. China, mainly in this market, do you believe that this could play a role in your decision to go ahead with your project for coated board or do you - And the second question, if you could talk about the acceptance of the most recent price increases that you announced in Brazil. When looking at a worsening scenario in 2016 or the macro side, what is the export mix that you consider reasonable for us to project? Is there a cap for that or could we consider that you will continue to export more and more?

#### A - Fábio Schvartsman

We apologize, however, the sound is not reaching the interpreter. The interpreter apologizes because she is not receiving the sound. Once the Puma Project just - operating - we apologize, however, it's the sound is not reaching us. Our competitiveness as a consequence is measured by hundreds of dollars per tonne of cost -- lower cost and what happened is that if a company is legitimate, we imagine making a new machine. Klabin is this company, this is the reason why Klabin will continue as was the case with the Puma Project.

And I believe that you must remember that when we announced the Puma Project, we said that there were questions about the demand and the price, and what about other projects and surplus capacity, excess capacity and we have always answered that we would have a project that would be unbeatable regarding cost.

So, regardless of where supply is and demand is, our project will be the most competitive of all. This is the reason why we went ahead with Puma. And the same rationale is applied to the coated board machines. Regarding the increase impact in prices, it is not our custom to talk about prices. What we say is that the company has been very careful and reasonable in terms of price increases and price increases of Klabin have been much more guided by cost than anything else, any other factor.

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And as a consequence, there is a justification and a reasonable rationale for that. Having said that, of course, nobody likes price increases anywhere or anytime. So, it is unfortunate that we have this inflation in the country and because of that, costs are going up because of inflation and they have to be transferred and they are being transferred.

Regarding the percentage of exports that we estimate for the future, theoretically speaking, we can export everything that we produce. This is just in theory because in fact, we want to continue to deliver to our countries and - our clients in the domestic market. How much will be exported will be determined by how much the domestic market is absorbing from our production. If the domestic market weakens further, we will continue to export more and more and I have already talked about the fourth quarter when our exports will be growing.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

I would like to know the export margin. Is it better than your margins in the domestic market? My question was more focused on that. Would you not deliver to the domestic market because you get much better margins in your exports? This is the comparison that I would like you to make. I was talking about splitting your sales, focusing more on export due to the fact that the margin is better even if the domestic market has a good demand.

**A - Fábio Schvartsman**

Okay, Thiago. Now, I understand. We believe that there will be a tomorrow. We are not living the end of an era or something that needs a more drastic or dramatic action. The company is making money and will continue to make more and more money, so this is the first point.

And the second point is the following. We have our commitments with our clients here in the domestic market and we continue to cater to them and this is our intention. We are not going to be opportunistic. We are not going to hinder our domestic clients and we have a long-term relationship with these clients.

Of course, it is very painful to waive a higher margin if we have to sell in the domestic market. Of course, it is painful. However, we are sure that this will bring about recognition on the part of these clients in the domestic market. Some day, things will get better here.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

Thank you very much, Fábio.

**Operator**

Our next question comes from Caio Ribeiro with BTG Pactual.

**Q - Caio Ribeiro** {BIO 18420483 <GO>}

Good morning, everyone, and thank you for the opportunity. Could you talk about the cost side of your operations? With the new inflation level and with a certain pressure on the

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part of your dollar-denominated input, how do you see the evolution of cash cost per tonne for the next few quarters and can you keep the guidance of going below inflation? And talking about consolidation, given this challenging scenario today do you see any opportunities for consolidation in the sector? And would Klabin prefer to grow organically only with a possible new coated board machine or would it be through consolidation?

### A - Fábio Schvartsman

Thank you for your questions. Let's talk about costs first. The first point I would like to mention is that the participation of imported inputs in our cost metrics is very small. It's about 9% of imported inputs in our metrics. So, the effect of the exchange variation is rather diluted if you consider the total cost of the Company. And, of course, we continue to work to keep our cost under control and if possible reducing them. And our view right now is that the cost evolution will be in line with the inflation, and as there is an upward trend in inflation, our expectation is to have a deceleration of the same measure.

Regarding consolidation, vis-à-vis organic growth, Klabin is maybe one of the few companies that can continue to grow organically. This means that organic growth, regardless of anything else, will be pursued because Klabin is very competitive in what it does. And regarding consolidation, I have a motto, we don't talk about consolidation. Consolidation is not talked about. It is done. And this is a non-issue, up to the moment; we can say anything about it. So, for the time being, I have nothing to say about consolidation.

### Q - Caio Ribeiro {BIO 18420483 <GO>}

Okay. Thank you very much.

### Operator

Lucas Ferreira from JPMorgan

### Q - Lucas Ferreira {BIO 16552031 <GO>}

Good morning, Fábio and Sergio. Could you go back to the production that you expect from Puma for next year? As the project is on time, what will be the ramp up and can you increase production at some moment in time next year? And what about the expected product mix for 2016?

### A - Fábio Schvartsman

Very good question. Thank you very much, Lucas. Let me answer them. Regarding the expected production for Puma for next year, it's around 900,000 tonnes, the expectation that we have. And we will always work to extract as much as we can and really go beyond any targets that we had established.

Nevertheless, it wouldn't be reasonable for us to start making projections of output increase in a plant that has not been started up yet. So, I think 900,000 tonnes is a good estimate and the proportion of products is identical to the proportion of products that we will have in capacity. Hardwood and softwood as you know, one-third and two-thirds, and

one-third of softwood will be also for fluff and 2016 will be a year in which fluff will be presented to many consumers and they will run tests and experiment, so that they may start buying from Klabin.

So, it's very difficult right now to tell you how much fluff we will be selling next year because it depends on our client's speed in terms of testing, et cetera. And the good news is that our negotiations with our clients are going very well and we are not facing any difficulty whatsoever in the sense of placing our products, be it softwood or hardwood or fluff.

#### **Q - Lucas Ferreira** {BIO 16552031 <GO>}

And regarding coated boards, the volume of sales drew my attention in this year. You have a higher production capacity than you had last year thinking about the average. But it was a very strong volume indeed, even for the domestic market. When we talk about the (0:24:30) figures that are very weak, are you gaining market share, are you selling more LTB? What about this difference between the average of the market and what Klabin was able to place in the second and the third quarters?

#### **A - Fábio Schvartsman**

Well, the volume is strong in coated board. And in the fourth quarter, our production of coated board will be even stronger than in the third quarter. That of course, this facilitates our sales and the explanation of what happens in domestic market has to do with the acceleration of sales by the companies that use liquid packaging boards and that increased their consumption, and maybe offsetting weaker months in the rest of the year.

So, there is nothing very special regarding this. Maybe we are gaining a little bit of market share, but if we are gaining market share, I think it's very little. I think the answer has to do with the consumption of liquid packaging board by our clients.

#### **Operator**

Our next question will be in English. Jon Brandt, HSBC.

#### **Q - Jonathan Brandt** {BIO 17988091 <GO>}

Hi. Good morning, Fábio. Good morning, Sergio. I wanted to come back quickly to the exports and the profitability. My assumption is that the exports that you have been doing historically have been the more profitable exports. So I'm wondering if you could tell us a little bit or try and quantify the profitability of the marginal tonne of exports. Is there a big difference between the profitability that you've done historically versus the profitability of the marginal tonne?

And then secondly, I just wanted to ask you about the debt and the leverage ratios that you have assuming granted a big part of it is due to the CapEx and to the FX rate. I'm wondering if you had any discussions with the credit agencies, how comfortable they are with you at your 6.2 times net debt, or they're looking at your balance sheet more in dollar terms which is just over four times is a more reasonable. Thank you.

## A - Fábio Schvartsman

Jon, thank you very much for your question. And your question about profitability is very interesting regarding our exports. And, of course, when you export, you export first the products at the highest price and only after that you export to markets with a lower price. Nevertheless, the markets where we operate, especially the coated board market, this is a market where demand is very, very strong right now.

So, everything that Klabin has regarding coated board available for export, it is sold very easily at the top price that we practice today. As a consequence we are not reducing our prices in order to carry out any sales and in the products such as kraftliner which is more commoditized so to say, you could expect more of this effect. But here, fortunately, we have been achieving - we have been successful in terms of increasing our exports and practically with no price decrease in dollar terms.

And this means that the whole benefit of the exchange rate variation plays in favor of the company. The company right now is living a situation in which everything that is exported by us brings about a major increase in the Company's profitability. And as I explained to one of your colleagues who asked a question, theoretically, we would love to export even more. However, we have our commitments with our client in domestic market, and we are going to honor our commitments always with our clients in the domestic markets. And the percentage that we export will be sufficient and the figures in the fourth quarter will show this very clearly, and this will continue to drive the growth in our EBITDA.

Now regarding your question about the credit agencies and the leverage of the Company, in fact we talk very regularly with the credit rating agency and we impart all the information about the Company. And the crux of the matter is not the level of leverage of the Company, the current leverage of the Company as you said. It is due to a combination of the fact that we are disbursing a lot to the Puma Project that hasn't been started up yet and the effect of the exchange rate variation, which is only accounting and with no impact on our cash.

So, this is not their concern. Their concern is the behavior of the Company's leverage from now on. And the good news is that any exercise that you carry out in this regard, it shows that the Company will start deleveraging very quickly during next year. And at the end of 2016, it will go back to normal levels. Of course, I don't have the authority to mention any figure regarding our leverage by the end of 2016. What I can guarantee is that we expect to reduce our leverage to regular normal levels for companies of Klabin's kind.

## Q - Jonathan Brandt {BIO 17988091 <GO>}

Thank you very much, Fábio. Thanks.

## Operator

Your next question will be in English as well. Carlos De Alba, Morgan Stanley.



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### **Q - Carlos F. De Alba** {BIO 15072819 <GO>}

Thank you very much. : So my question has to do with the price increases in the domestic market that the Company is trying to implement. If you can comment as to how successful that effort has been. And also what are the strategies when the customers are not accepting the price hikes? Would you stop selling to them or how you want to handle that situation?

And the second question I have is regarding your receivables and any defaults that you have seen from your customers. Have your NPLs or non-performing receivables increased in the recent quarters? If you can comment on that, that would be useful. Thank you.

### **A - Fábio Schvartsman**

Okay. I have just made a remark. In the sense, we are increasing our prices reasonably in line with the increase in cost in Brazil Carlos, and we have not been facing major difficulties to carry out these price increases. Our clients - most of our clients do understand the need for the Company to protect its operations because the cost increases have to be transferred. So, if there is one or other companies that doesn't like this price increase, they are just a minority and we have had no major consequences on the Company coming from the situation regarding NPLs, I would like to ask Sergio to talk about that because I think he has good news to tell you, Carlos.

### **A - Antonio Sergio Alfano** {BIO 4337533 <GO>}

Regarding NPLs, at Klabin, default is very low because of our relationship with our clients, our sales on a monthly basis, and so this means that we have a very good control over our accounts receivables, and we have a very good relationship with our clients. And we have not been having any problems regarding default. Our default levels are extremely low.

### **A - Fábio Schvartsman**

Carlos, I would like to add something to that. In the measurement made on September 30, we were at an all-time low in terms of NPLs or receivables problems in the Company, and of course, this is excellent news if you consider the current macro scenario.

### **Q - Carlos F. De Alba** {BIO 15072819 <GO>}

Great. Thank you very much.

### **Operator**

Victor Penna from Banco de Investimento.

### **Q - Victor Penna** {BIO 16384328 <GO>}

Good morning, everyone. I would like to know about investments made in the past in the Goiana machine, Piracicaba, Angatuba. What about the ramp-up of this investment? Are they operating at full capacity, all these machines? And how many thousand tons were added in 2014, how much could we expect for 2016?

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Are you focusing more on kraftliner or corrugated boxes or what? Could you quantify that? And also I would like to know about the Puma CapEx. How much will it be in 2016 and what will be the maintenance CapEx projected by the Company during the ramp-up period or up to the moment it is finalized? And could you talk about Puma still? What about the new coated board machine? You have already talked about the decision making process and that you would be more focused on market and conditions to make this decision. But do you intend to make any smaller investments that are you analyzing and what would be the capacity increase coming from these smaller investments?

### **A - Fábio Schvartsman**

Thank you very much for your questions. Regarding investments that we made and that increased the Company's capacity from 1.7 million tonnes to 2 million tonnes, talking about each one of them, Goiana paper machine was the first one, 70,000 tonnes capacity. It is operating at full capacity without any problem. The Goiana machine is also reaching currently its nominal capacity. So, we are reaching the end of the ramp-up of Machine 24 with excellent performance and the Piracicaba machine is going very well. Thank you.

So, all these machines have been adding capacity. And as we said before, part of this capacity has already materialized in 2015 and part of that will materialize in 2016. And I believe it will be about 100,000 tonnes additional capacity for 2016, give or take. And you should understand that the people look at the Company's figures and say well, invested in machines but the total volume is not growing.

In fact the total volume is growing and the difference is that as we are focusing more on exports and as the export chain is a longer chain, then the chain of domestic sales, when you choose this path, ultimately, you have to fill the pipeline and part of the production stays in the pipeline. But they mean future sales, and as you fill the pipeline, which is the case of the Company right now, exports give a leap and exports will give a leap in the fourth quarter, which is the factor that I mentioned in my initial remarks. Regarding your questions about CapEx pro forma and maintenance CapEx, I would like to ask Sergio to answer.

### **A - Antonio Sergio Alfano** {BIO 4337533 <GO>}

Puma CapEx or the remaining Puma CapEx, we will be making payments up to June and July 2016. And we estimate the end of our disbursement at R\$1.6 billion for the project, which will be paid out during the next five months - the next seven months. And in terms of maintenance CapEx we spend R\$370 million to R\$400 million on average per year in maintenance CapEx. And next year, in addition to - will be the replanting of the new harvesting areas that we will be carrying out in order to meet the needs of the Puma Project. So, basically, this is it.

### **Q - Victor Penna** {BIO 16384328 <GO>}

And what about my final question about other investments? Do you have anything in the pipeline, any smaller projects?

### **A - Fábio Schvartsman**

Well, we have a whole array of projects that are waiting for the right time for us to give the green light. But the right time will be after the Company deleverages. We will not be making additional investments before we are totally comfortable with our leverage level. Certainly, now is not the right time for us to talk about new projects.

The coated board machine is another case. It depends not on the market but on our clients because here, we have specific clients and we are negotiating contracts with them right now. And if we are successful in our negotiations and we believe we will be successful, then we will think more seriously about constructing this new machine.

**Q - Victor Penna** {BIO 16384328 <GO>}

Thank you. Perfect.

## Operator

Alan Glezer from Bradesco BBI.

**Q - Alan Glezer** {BIO 17508681 <GO>}

Good morning, everyone I have two questions. The first one has to do with the Puma Project. Given the evolution of 90% of the physical construction of the project, would it be reasonable to expect some sale of energy that might bring about a decrease in your quarter, in the fourth quarter of 2015?

And my second question has to do with the evolution of sales of coated board in the domestic market. There was an excellent performance of machine with the debottlenecking of the new machine and sales going up by 10%. And I would like to know if this means displacement of some of your competitors? Are you increasing market share or creating market share and how are you placing this volume? Is it to new clients or could you tell us about that please?

**A - Fábio Schvartsman**

Sale of energy, the company could start to sell energy, but the problem is that the price of energy in the spot market dropped quite steeply. And as a consequence, we see no economic reason to start selling energy.

You can imagine that it is different to produce energy with the Company or the plant operating at full steam, and rate of operation of steam and when you're just burning wood in order to take advantage of a good price in the market. And the price is not attractive right now. And this is the reason why we are not in a hurry to sell energy. We could, but we will not start selling energy due to the low prices.

Regarding the domestic board market, our performance has been very good. And another part of the explanation is that fundamentally, it was a good performance for the liquid packaging board and this doesn't mean a big change in the market share. We do

not believe we are gaining share significantly. This is simply due to the fact that the liquid packaging board, as it is very resilient; it is more stable than the other markets.

**Q - Alan Glezer** {BIO 17508681 <GO>}

Thank you very much and I would like some follow up if you allow me. Is there a guidance for a leverage peak and what is it? Thank you.

**A - Fábio Schvartsman**

This is a very good question, but as most of our debt is long-term debt, prepayment of exports, in fact, it varies a lot according to the exchange rate. So, the peak is not a matter of the decision made by the Company. It has to do with the exchange rate. So, according to the exchange rate, we calculate a different peak. What I can tell you is that if the exchange rate remains around R\$4 (0:42:09) as it was at the end of last quarter, the peak is already over.

Now, if we have a further devaluation of the real, of course, the peak is going to change. Unfortunately, this is a mere accounting exercise and the focus should be, and as I believe the rating agencies are doing correctly, what will be the Klabin deleveraging process. And the good news is that deleveraging due to the huge result that will be added by Puma, it would be very quick.

**Q - Alan Glezer** {BIO 17508681 <GO>}

Thank you, Fabio.

**Operator**

And there are no more questions. I would like to give the floor over to Mr. Schvartsman for his closing remarks.

**A - Fábio Schvartsman**

(0:42:59) Once again, thank you very much for having participated in our conference call. We are very pleased with the results delivered by the Company and the Puma Project is going very well. Thank you, according to schedule, ready to start production. According to schedule as well, our operations are all going very well, and we are focusing more and more on exports and business, very good news.

If you consider the prices in the international market and the exchange rate and as a consequence we should have an excellent fourth quarter. And I believe this will be a very good way of finishing this year and really waiting for Puma with a red carpet based on a very good performance of the Company until the moment Puma gets started up.

Thank you very much and have a very good day.

**Operator**

Klabin's conference call is closed. Thank you very much for participating and we wish you all a very good day.

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