

Airgain, Inc. NasdaqCM:AIRG

FQ3 2023 Earnings Call Transcripts

Thursday, November 09, 2023 10:00 PM GMT

S&P Global Market Intelligence Estimates

| | -FQ2 2023- | | -FQ3 2023- | -FY 2023- | -FY 2024- |
|-----------------------|------------|----------|------------|-----------|-----------|
| | CONSENSUS | GUIDANCE | CONSENSUS | CONSENSUS | CONSENSUS |
| EPS Normalized | 0.00 | 0.00 | (0.02) | (0.10) | 0.11 |
| Revenue (mm) | 16.54 | - | 14.03 | 62.46 | 69.40 |

Currency: USD

Consensus as of Oct-26-2023 12:24 PM GMT



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Call Participants

EXECUTIVES

Jacob Suen

President, CEO, Chief Revenue Officer & Director

Michael Elbaz

CFO, Secretary and Principal Financial & Accounting Officer

ANALYSTS

Craig Andrew Ellis

B. Riley Securities, Inc., Research Division

Unknown Analyst

Presentation

Operator

Afternoon. Welcome to Airgain's Third Quarter 2023 Earnings Conference Call. My name is Sherry, and I will be coordinating for today's call. Joining us for today's call are Airgain's President and CEO, Jacob Seun; and CFO, Michael Elbaz. As a reminder, this call will be recorded and made available for replay via the link found in the Investor Relations section of Airgain's website at investorrelations.airgain.com. Following management's prepared remarks, the call will be open for questions from Airgain's sell-side analysts. I caution listeners that during this call, Airgain management will be making forward-looking statements about future events and Airgain's business strategy and future financial and operating performances. Actual results could differ materially from those stated or implied by these forward-looking statements due to risks and uncertainties associated with the company's business. These forward-looking statements are qualified by cautionary statements contained in today's earnings release and Airgain's SEC filings. This conference call contains time-sensitive information that is accurate only as of the date of this live broadcast, November 9, 2023. Airgain undertakes no obligation to revise or update any forward-looking statements to reflect events or circumstances after the date of this conference call. In addition, this conference call may include a discussion of non-GAAP financial measures. Please see today's earnings release for further details, including a reconciliation of the GAAP to non-GAAP results. I would now like to turn the call over to our CEO, Jacob Suen.

Jacob Suen

President, CEO, Chief Revenue Officer & Director

Thank you, operator. Welcome, everyone, and thank you for joining us. For today's call, I will first cover our operational highlights and achievements for Q3. Then I will hand over to Michael to walk you through our financial performance for the third quarter and our guidance for the fourth quarter. Afterwards, I will provide an update on our strategic product and marketing initiatives for Q4 and beyond before opening the call up for questions. I would like to start by briefly introducing who we are and what we do for those who may be new to Airgain in our industry. And again, we simplified wireless connectivity for the consumer, enterprise and automotive markets. Our technology spans across the value chain from embedded components to integrated systems. Our products fall under 3 sub brands, including Airgain Embedded, Airgain Antenna Plus and Airgain Integrated. At the beginning of the year, we announced our initiative to improve the 5G customer experience by fixing coverage gaps, boosting performance and simplifying the delivery of 5G connectivity to the home office and vehicle. Earlier this year, we introduced our lantern 5G text wireless access device in lighthouse 5G C-band smart repeater, and we will be announcing a third product initiative in the coming months that fits into our effort to improve the 5G customer experience. Our goal is to begin shipping some of these innovative products to partners and end customers in the first half of 2024. We work with a global network of BOSS system integrators, distributors enlarged customers to help solve critical connectivity issues, improve wireless performance and effectively shorten time to market for their products. With Airgain's growing product portfolio, we offer complete wireless solutions to our channel partners and customers that help them get connected quickly. Now for our performance, third quarter sales came in at \$13.7 million, which was close to the midpoint of our guidance range. Macroeconomic conditions such as demand softness and inventory corrections have continued to create downward pressure in all 3 of our main markets: consumer, enterprise and automotive. While we focus on growing our customer base, we expect the continued inventory overhang in our channel and one of our lead customers to persist in the fourth quarter, coupled with the shift of a large enterprise project from the fourth quarter to the first quarter of 2024. We are projecting a lower guidance range in the fourth quarter. However, we are nearing our cleaning point and are beginning to see signs of a market recovery. We expect growth in our enterprise market in the first half of 2024, with broader growth in the second half of the year from our consumer and automotive markets, especially with the launch of our product initiatives. Moving to a review of each of our markets. Our consumer market is comprised of our custom embedded antenna design for CPE devices sold primarily to major service providers. In addition to demand softness and inventory corrections, there are additional forces within the consumer market, creating downward pressure. First, as we discussed last quarter, service providers are on the cusp of a transition from Wi-

Fi 6E to Wi-Fi 7. They are counting on WiFi 7 to improve performance and user experience, and they are looking for ways to accelerate the Wi-Fi 7 adoption and transition. In anticipation of this shift, our key OEM customers are operating cautiously in order to avoid excessive inventory. While the market is hesitant in the short term, this shift presents a compelling long-term opportunity for Airgain to deliver its cutting-edge Wi-Fi 7 technology. We have invested heavily in our Wi-Fi 7 capabilities, and we recently secured a design win from a Tier1 cable operator for its next-generation Wi-Fi 7 CPE. Second, consumer demand continues to shift from wire to wireless providers for Internet service as they cut the cord and make the transition to SWA. We recognized this trend and focus our strategy on penetrating this growing market, which offers significant average selling price or ASP growth. We are pleased to announce we recently secured a large design win with a Tier1 mobile network operator or MNO for the antenna design in their indoor FWA router, for which we expect to begin shipments in Q1. In addition, we are working on several other opportunities with cable operators and MNOs and look to secure these opportunities in early 2024. As we navigate a challenging demand environment, we expect declining consumer sales in the next 2 quarters, followed by gradual growth from our MNO design win and from our cable operator Wi-Fi 7 technology transition. Our enterprise market represents a mix of components in systems that include our embedded modems, asset truckers, enterprise antenna design and custom products. Inventory overhang continues to dampen our embedded modem revenue. And while some of our distributors are back to normal buying patterns, others are still clearing inventory that will last a few more quarters. Despite the inventory overhang, we see end customer demand growth in our models as evidenced by growing point of sales at our distribution partners, and we expect a gradual recovery in the first half of 2024. The EV charging in visas continue to be strong markets for our modems, and we do see industrial agrobusiness, energy and managed IoT applications as growth opportunities. Our custom products, offerings, features joint engineering collaboration with our customers to develop products for specific applications while helping them reduce their time to market. These projects can often help shifting time lines, depending on product requirements, engineering resources, certifications and manufacturing schedules. Shipments can fluctuate from quarter-to-quarter based on the complexity of the product offering which has had a material impact on our expected timing for such revenues. Specifically, one of our lead customers is going to a technically complex platform refresh in the combinations of high inventory in its current platform and the completion delay in this new platform created a material shift of revenue from the second half of this year to the first half of 2024. Our asset structure business continues to show significant growth potential. We continue to see growing applications for pallet, packaging and logistics tracking, which represented a bright spot in our Q3 revenue. In addition, our pipeline includes several opportunities in railways, warehousing, equipment management and rental, lot management and coaching. This is one of our existing product lines that presents a significant growth opportunity in 2024 due to the market size, flexibilities of applications, opportunity for recurring revenue and our strategic product differentiators. Because of the size of the customers, with which we are interacting in the established pilot process, the sales cycle for this product can be from 9 to 18 months. While our potential deal pipeline is strong, we are working to address our resource constraints, streamline our processes and shorten the sales cycle to help create a more consistent revenue stream in 2024. Lastly, our automotive market includes both our aftermarket antennas as well as our vehicle networking devices. Our focus in the automotive market has largely been in the public city, transportation and municipalities. Inventory corrections from the customers have lengthened the growth in this market, and we expect this trend to continue in the first half of 2024. However, we are seeing signs that our combined strategic focus on new and differentiated products, supply chain flexibility and global channel expansion is yielding results in Q4. We expect our previously announced RECON13 and ULTRAMAX-class 5G products will begin to ship this quarter, both of which fit into our new low-profile design focus. This is in addition to our EC Connect platform, which adds supply chain flexibility by separating the antenna from the cable harness minimizing the valuations in SKUs. In addition, we signed a new system integrator in the public safety and municipality market that we believe will contribute significantly to our automotive sales next year. Despite the downward pressure from macroeconomic forces that have persisted throughout 2023, we remain optimistic that our sales expansion strategies pay a path to growth in 2024 and beyond. By the end of 2023, we expect to have added 5 new distribution partners in a major system integration partner, greatly expanding our reach. We have also announced new products that should start to impact revenue in Q4 alongside 2 of our 3 major product initiatives to improve the 5G customer experience, all of which help sulfide an addressable market that should contribute significantly to 2020 revenue and beyond. We have expanded into 2 new key

geographies and look to take advantage of the market needs in these regions. While 2023 has presented some significant challenges, we believe we have the right product road maps and expansion strategies to recover and grow in 2024. With that, I'll turn the call over to Michael.

Michael Elbaz

CFO, Secretary and Principal Financial & Accounting Officer

Thank you, Jacob. Before diving into the numbers, please note that my review of our financial results and guidance refers to non-GAAP figures. Information about the non-GAAP financial measures, including GAAP to non-GAAP reconciliations are found in our earnings release. Now let's turn to this quarter's results. As Jacob mentioned, Q3 sales were \$13.7 million, below the \$40 million midpoint of our guidance range. The variance was primarily due to lower-than-forecasted consumer sales. Our sales declined 13% sequentially and 29% year-over-year, primarily due to the high inventories across both our channel and direct customers, coupled with demand softness in our consumer market. Consumer sales were \$4.4 million, reflecting a sequential decrease of \$1.8 million as our Q2 quarter had a strong uptick of Wi-Fi 6E embedded antenna shipments. Enterprise sales were \$6.8 million, which decreased sequentially by \$0.5 million. The decline was driven by lower sales of custom products, partially offset by higher sales of embedded modems as some distributors are recovering from inventory overhang. Automotive sales were \$2.5 million, reflecting a sequential increase of \$0.2 million. Q3 gross margin was 39.1% compared to our guidance range midpoint of 40%. The variance was primarily due to the unfavorable consumer sales mix. Q3 gross margin was 130 basis points lower sequentially due to the unfavorable consumer sales mix and a lower enterprise margin driven by an unfavorable product mix change. Q3 operating expenses totaled \$6 Million, slightly higher than our guidance of approximately \$5.8 million. Operating expenses decreased sequentially by \$0.5 million, driven by lower contractor and other variable expenses, resulting from G&A efficiencies. Our Q3 operating expenses at \$6 million represents the lowest spend level since the acquisition of NimbeLink in Q1 of 2021. As we mentioned in prior earnings calls, we are focused on driving operational efficiencies to reduce our expenses and make room for the investment needed for the launch of our 3 initiatives that will help drive revenue in 2024. As a result, our Q3 adjusted EBITDA was negative \$0.5 million, and non-GAAP EPS was negative \$0.06. Our cash balance as of September 30 was \$10 million, \$0.7 million higher sequentially, driven by working capital management. The \$10 million cash balance was \$0.8 million higher than the same quarter in the prior year despite lower year-over-year sales. Our accounts receivable balance was \$6.3 million, \$2.4 million lower sequentially due to strong cash collections and lower sales. Net inventory was \$4 million, \$0.8 million lower sequentially. Given our cash balance and our tight expense management, we believe we have sufficient resources to execute on our growth strategies. Now moving to our outlook for the fourth quarter ending December 31, 2023. We project sales to be in the range of \$9.25 million to \$10.75 million or \$10 million at the midpoint of the range. The lower revenue guidance compared to prior expectation is due to lower-than-anticipated consumer sales and continued inventory corrections coupled with a large enterprise project pushout Jacob mentioned. We expect non-GAAP gross margin for the fourth quarter to be in the range of 38.5% to 41.5% or 40% at the midpoint of the range. Leveraging our CM model is a primary driver of our gross margin improvement initiatives. And we completed the first phase of this leverage with our automotive antennas. Despite the lower projected consumer sales mix, we expect our gross margin to improve sequentially as a result of our automotive product cost reductions. We project our operating expenses to be approximately \$6 million. Non-GAAP EPS is expected to be negative \$0.19 at the midpoint of our guidance. Adjusted EBITDA is expected to be negative \$1.8 million at the midpoint of our guidance. Despite the revenue challenges we faced in the fourth quarter, we remain focused on generating positive cash flows in the first quarter of 2024 while we'll continue to execute on our strategic product initiatives. Now I would like to turn the call back over to Jacob, who will walk us through those strategic initiatives.

Jacob Suen

President, CEO, Chief Revenue Officer & Director

Thanks, Michael. During Q3 and Q4, our team has spent a significant amount of time and effort on our strategic planning process. As a result of this analysis of our products and markets, we developed a product road map that stretches into 2025 and captures our strategic product launches that we believe will save our revenue in the future. Of our current product lines, we believe that our asset trackers offer the greatest strategic growth opportunity. When we narrow the market to similar connected asset trackers,

we estimate the 2024 serviceable available market or same to the \$900 million. In addition, we have been in the market for over 3 years and have built a strong pipeline of deals. As mentioned previously, because of the pilot process and size of the end customer, the sales cycles can be longer than some of other products. However, the deals are larger, more sustained and involve a significant component of recurring revenue. We continue to make very good progress and are optimistic that our asset tracking offering will become an even greater revenue contributor to the overall business. In addition, we have previously discussed our initiative to improve the 5G customer experience. While 5G delivers on its promises of lower latency, increased capacity and higher throughput, it comes at the expense of a shorter signal range from the base station. Consequently, this creates coverage gaps for 5G customers. We believe Airgain is well positioned to solve these major coverage deficiencies, and we have identified 3 key areas where we believe we can make an impact. These areas include the network itself, customer premises in the vehicle, improving 5G connectivity and customer experience begins at the edge in the home or office with fixed wireless access. These devices allow wireless operators to compete with cable and wire solutions for the broadband connection. This year, we announced our entry into this market with the introduction of an enterprise-grade CPE called Lantern FWA. Lantern is an outdoor rigidized sub-6 gigahertz 5G device, but which the trade-off between performance and ease of install. It is equipped with directional high gain antenna that is optimized for mid-band and high-band frequency range, offering superior performance for all MNO customers. It also includes a patent-pending EV installation kit comes with a mobile app that significantly reduces installation time and eliminate the need for professional installation. When we narrow our focus to 5G outdoor non-millimeter wave devices in the regions where we plan to compete, we estimate the same is over \$500 million in 2024 alone, offering a lucrative market in which to compete. While most FWA devices are indoor solutions currently being sold to consumers through MNOs and are subsidized as part of a monthly fee, our enterprise-grade device is coming out its own niche in the market. Our global MNO partners see this product as a pathway to help them walk into the B2B market in a meaningful way, even calling it a needle mover for them. In addition, the product is receiving significant interest from our channel partners who have had to piece together enterprise FWA solutions from multiple expensive components. Airgain's Lantern FWA offers a simpler and less expensive option, allowing them to better compete in the market. There is a area of use cases where the device can be used. However, broadband fallover and mobile operations seem to be the tool gaining the most early interest. The product has been in trial with several channel partners and MNOs, and we are targeting a Q1 ship date for the first versions of this product. The feedback from trial customers has been positive, and we are pleased to announce that we have secured early purchase orders for the Lantern FWA products, showing the market potential for the device. With the reduced transmission range of 5G signals, the cost of ownership for network operators increases significantly due to the infrastructure and equipment required to expand high-quality coverage. An active smart repeater can overcome this challenge by facilitating efficient use of existing infrastructure to ensure a stable and high-quality signal. Earlier this year, Airgain introduced the lighthouse smart repeater, which offers a single pole installation, carrier aggregation, active echo-cancellation, support for multi updaters frequency bands, active steering capability and requests nonfiber backhaul. It is a cost-effective way to deliver a targeted 5G signal in areas that lack quality coverage. Based on the global number of base stations to the regions we plan to serve in factoring rollout, we estimate the same for 2025 to be around \$600 million for this product. making this a lucrative market in which we can compete. We have completed multiple field trials on Tier1 upgrader networks in our own track for product launch by the end of 2024. Additionally, another key area where we feel that we can improve the 5G customers experience is in the vehicle. We have been in the fleet and vehicle networking industry for many years. With the deployment of 5G, the use cases for higher data rate applications have multiplied substantially. This is especially important for several segments, including public safety, transportation, agriculture, utility and many more. Based on vehicle routers and focusing on 5G, we estimate a same in 2024 of \$200 million. We will be announcing the next generation of our vehicle networking device in early Q1 to tackle this market and provide opportunities for growth. We have seen early excitement from several major customers on this next-generation product. Our current target ship date will be Q2 of next year. Between these 3 major product initiatives, we estimate over \$700 million in potential additional fund in 2024 and \$1.7 billion in 2025, effectively doubling our foundational same of \$1.8 billion for our existing products. This gives us not only the ability to grow organically from our existing product lines, but also to expand our growth opportunities by adding value to our existing markets and exploring new markets. It is also the combinations of the strategy we announced 2 years

ago to shift from exclusively components to full systems. In closing, 2023 has been a challenging year for Airgain along with the rest of the industry in which we compete. Market forces have created a downward pressure on our traditional lines of business that will persist to the end of this year. While we anticipate a challenging environment in 2023, we underestimated the severity of its impact on our business. We are disappointed with our revenue and EBITDA guidance for Q4 as we expect stronger headwinds resulting from the combination of lower than previously anticipated consumer sales, continued inventory correction and customer project pushouts. However, despite these significant challenges, we believe we have made the right strategic moves and now have a line of sight to revenue recovery starting in Q1 of 2024. Our Q1 backlog is currently higher than that of our Q4 backlog. We are maintaining our existing customer base and are adding new customers as evidenced by our recent design wins in our consumer, automotive and enterprise markets, and we have a strong pipeline of opportunities that should accelerate our future growth. We are focused on being EBITDA positive in 2024 in generating positive cash flows based on the resolution of inventory issues in the market, expansion of channels and geographies, the demand for Wi-Fi 7 and FWA devices by major upleaders in the launch of our new products. While our strategy is ambitious, we believe we have the right team in place to execute. We are very pleased to have the new additions of Evan Jones as our VP of Engineering. Evan spent over 23 years at Sierra Wireless as their VP of IoT system engineering and customer experience. Evan is an industry veteran who has joined Airgain at this pivotal time because he believes in our vision and product roadmap. He is also very excited to work with the seasoned executive team already in place at Airgain to help grow our existing product lines and ensure the successful launch of our 3 new product initiatives into the marketplace. Evan has undergone a fundamental transformation in our technology, product road maps, operations, sales approach and brand to shift from components to systems. As is often the case, transformations can be difficult and painful for organizations, and we are no exception. I would like to thank our team for continuing to persevere and execute despite the challenges. While we look to recover and generate organic growth from our core products and customers, we believe our strategic focus on growing our asset tracker business and improving the 5G customers experience through these major initiatives, offers a pathway to larger growth in 2024 and beyond. As these initiatives begin to come to market in early 2024, we believe they will begin to help shape our future as a systems-focused company. And with that, we're ready to open the call for your questions. Operator, please provide the appropriate instructions.

Question and Answer

Operator

Our first question is from Craig Ellis with B. Riley Securities.

Unknown Analyst

I was just wondering if you could provide some color as we move the product mix towards higher volume in clients and services and in a tough macro, what are some products in the consumer and enterprise that can drive meaningful revenue to 4Q or potentially into 2024? And is there any changes in the segment gross margin, like consumer gross margin or enterprise gross margin?

Jacob Suen

President, CEO, Chief Revenue Officer & Director

From a consumer standpoint, as we mentioned, the revenue level is a bit depressed. We started in Q3. We're expecting a further decline in Q4 primarily because of our OEMs trying to manage their inventories or excess inventories with the pending Wi-Fi 7 technology transition, along with some soft demand taking place at the MSO level. And so what we have secured so far is really an MNO Tier1 design win, which we expect to start shipping in Q1. So this will give us a bit of a bump in Q1, but really the overall growth on that market will really come from the Wi-Fi 7 technology transition, which we expect to see at the end of Q2 and certainly in the second half of the year. On the enterprise business, what we are facing right now is more of an inventory overhang with one of our lead customer, and this is also the same lead customer where we have also a custom design of a new platform. This is a complex project, which is now delayed to the early part of next year, Q1 specifically speaking. And so while we see an overall depressor lower revenues in Q4, we expect to see the uptick in Q1. And then some resumption after that of growth in the fiscal year '24, mainly because of the inventory corrections being sorted out through the first half of the year. And then finally, on the automotive, it's more of a mixed story here between some of the inventory correction going on with some of our lead customers, but also that being offset with a growing new products. We have recently announced a number of new products, but also new channels and new geographies as well, too. And those, again, for the second half of the year will start to really pan out for us as what to, along with the new product initiatives. In terms of mix, it's a bit uncertain right now, given the low level of visibility on how everything plays out. All of our OEMs are certainly trying to be very conservative in the inventory level. We could see some surprise in December with some surprise orders, but we're not counting on that. And so in terms of the mix, it could be fluctuating quite a bit. The good news here is that on the margin front, with the automotive product cost reduction that we have initiated about 2, 3 quarters ago, and those are becoming effective in Q4. We do see our overall gross margin starting to improve with the CM leverage that we have been counting on, and this trend will continue on. And so I think we will be somewhat protected with some of the consumer market mix, which has been unfavorable over the past few quarters.

Craig Andrew Ellis

B. Riley Securities, Inc., Research Division

So what are your view about cash or any change in inventory days? How do you feel about your cash level, whether it's sufficient for your working capital?

Jacob Suen

President, CEO, Chief Revenue Officer & Director

So our cash actually increased in Q3 at the end of September, increased compared to quarter-over-quarter, but also year-over-year basis. We are at \$10 million right now. And this has been mostly driven out of working capital management, lower inventories, and as I mentioned, but also lower account receivable, not only because of lower sales, but also primarily because we achieved a record low DSO with some very strong collections. So the team is definitely very focused on whatever we can do from a working capital management standpoint with the EBITDA loss that we are projecting for Q4 of a \$1.8

million at the midpoint of the guidance, we expect our cash balance to be at around \$8 million, which is definitely sufficient for enough of resources to be able to pursue our growth initiatives, and especially in light of a growth resuming in the first half of the year.

Operator

That will conclude our question-and-answer session. If your question was not taken, you may contact Airgain's Investor Relations team at AIRG@gateway-grp.com. I would now like to turn the call back over to Mr. Suen for closing remarks.

Jacob Suen

President, CEO, Chief Revenue Officer & Director

Thank you for joining us on today's call. We look forward to updating you on our next call.

Operator

This concludes today's call. Thank you for joining us for Airgain's Third Quarter 2020 Earnings Call. You may now disconnect.

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