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PRESENTATION

Operator

Good morning, and welcome to the Olympic Steel 2019 Fourth Quarter Financial Results Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would now like to hand the conference over to Rich Manson, Chief Financial Officer at Olympic Steel. Please go ahead, sir.

Richard A. Manson - *Olympic Steel, Inc. - CFO*

Thank you, operator. Welcome to Olympic Steel's Fourth Quarter and Full Year 2019 Earnings Call. Our call this morning will be hosted by our Chief Executive Officer, Rick Marabito. And we will also be joined by our President and Chief Operating Officer, Andrew Greiff.

Before we begin, I have a few reminders. Some statements made on today's call will be predictive and are intended to be made as forward-looking within the safe harbor provision of the Private Securities Litigation Reform Act of 1995 and may not reflect actual results. The company does not undertake to update such statements, changes in assumptions or changes in other factors affecting such forward-looking statements. Important assumptions, risks, uncertainties and other factors that could cause actual results to differ materially are set forth in the company's reports on Forms 10-K and 10-Q and press releases filed with the Securities and Exchange Commission.

During today's discussion, we may reference adjusted net income per diluted share, which is a non-GAAP financial measure. A reconciliation of this non-GAAP measure to the most direct comparable GAAP financial measure is provided in the press release that was issued this morning, and that can be found on our website.

Today's live broadcast will be archived and available for replay on Olympic Steel's website. At this time, I'll turn the call over to Rick.

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

Thank you, Rich. Good morning, and thank you for joining us to discuss Olympic Steel's results. This morning, we announced the fourth quarter 2019 loss of \$890,000 or \$0.08 per share, and that's compared with the fourth quarter 2018 loss of \$1.3 million or \$0.11 per share. For the full year of 2019, we reported net income of \$3.9 million or \$0.34 per share, and that's compared to net income of \$33.8 million or \$2.95 per share in 2018.

2019 was a year of progress for Olympic Steel in a challenging environment that saw carbon steel prices under extreme pressure after the 2018 run-up in prices. Supporting our large OEMs fueled significant growth in our carbon flat products segment during the trade and tariff-induced market of 2018. Our carbon segment then felt the fourth quarter 2019 impact of those OEMs downsizing their inventories as carbon pricing plummeted and demand waned.



Through the challenges, however, in 2019, we furthered our diversification strategy. We improved our financial position, and we recorded strong performance in our specialty metals and pipe and tube businesses. Together, our specialty metals and pipe and tube segments now comprise 41% of our net sales versus 37% a year ago. Our specialty metals business recorded its second most profitable year ever, with EBITDA levels just shy of last year's record. Our pipe and tube segment also had solid performance, delivering its third most profitable year since joining Olympic Steel in 2011.

We continued our diversification efforts by acquiring 2 downstream metal-intensive branded products companies into our carbon flat segment, which had an immediate positive impact on profitability. We continue to actively seek additional acquisition opportunities to further diversify our portfolio, achieve higher returns and temper the volatility in results.

In 2019, we also focused on working capital by closely managing inventory levels throughout the year. We delivered strong cash flow, which was used to fund our acquisitions, make select CapEx investments and reduce our debt by over \$110 million or 36%. We entered 2020 with a strong balance sheet and the flexibility to quickly execute on additional growth opportunities.

As part of our planned succession, on January 1, Andrew Greiff was named President of Olympic Steel in addition to his existing Chief Operating Officer responsibility. Andrew has more than 30 years of experience in the metals industry and has demonstrated exceptional leadership as our Executive Vice President and Chief Operating Officer since 2016 and previously as President of our Specialty Metals business. We are confident that we'll benefit from Andrew's wisdom, experience and leadership. As part of our planned succession, in early 2020, we announced that Bill Zielinski assumed the role of President of our Chicago Tube and Iron business unit in addition to his existing responsibilities as CTI's Chief Operating Officer.

As I conclude my opening remarks, I'd like to take a moment to thank David Wolfort and Don McNeeley for their exceptional dedication and contribution to Olympic Steel and their continued leadership through our planned succession process. David is a true steel industry professional who has driven our commercial success for over 36 years and helped transform Olympic Steel into a leading U.S. metal service center. Don McNeeley has been an integral part of the continuous success of Chicago Tube and Iron for over 40 years, and he has delivered strong results since joining the Olympic Steel family in 2011. We are fortunate that both David and Don remain actively involved in the commercial activities of our company. David also continues as a valued member of Olympic Steel's Board of Directors, and Don is actively engaged in strategy and leadership development at CTI.

I will now turn the call over to Andrew for his comments.

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

Thank you, Rick, and good morning. I'd like to take a few moments to review each of our operating segments. During 2019, we saw the price of carbon hot-rolled steel fall to less than 1/2 of the tariff-induced high pricing seen in 2018. Since hitting bottom of 2019 pricing in October, we have seen 5 mill increases totaling approximately \$190 a ton, but it's come at a time when manufacturing demand has been challenged. As a result of falling carbon steel prices and uncertainty of U.S. trade policy, end user demand in agriculture, automotive and Midwest manufacturing declined in 2019 versus 2018.

During the fourth quarter, we also experienced the General Motors strike and the destocking of inventory in the supply chain, which impacted our sales and earnings, especially in the carbon segment. Specialty metals continues to outperform the market, especially in stainless. According to the MSCI Metals Activity Report, through the fourth quarter of 2019, the overall stainless flat-rolled market was down 4.5%, while Olympic Steel was up 7.2%. Overall, specialty metals had a strong fourth quarter, which enabled the business to complete 2019 as its second most profitable year in our history. Our success in this segment has been bolstered by our 2018 capital expenditures in both Schaumburg and Streetsboro, which expanded our in-house specialty metals processing capabilities as well as the 2018 acquisition of Berlin Metals.

In addition, our Chicago Tube and Iron business had another solid quarter, and CTI has had its third most profitable year since we acquired the business in 2011.



We're also pleased with the contributions from our 2 most recent acquisitions, which we have noted before are countercyclical to overall carbon market dynamics. The performance of our 2 manufacturing acquisitions continues to exceed our expectations and are contributing bottom line benefits to our business. The results have reinforced our belief that our strategy to move further downstream is effective as we can look for more acquisition opportunities.

Overall, we remain optimistic, but cautious in our outlook and mindful of the uncertainty that exists. We do know that new carbon steel producing capacity will be coming online over the next 12 to 24 months, which will likely pressure pricing for our carbon flat products. We continue to address the volatility associated with these uncertainties by reducing risk through lower inventory levels and increasing our transactional or spot business.

For Olympic Steel, we will continue to capitalize on the success of our specialty metals and pipe and tube businesses, and we seek additional acquisitions. We remain vigilant in the containment of our operating expenses and diligent in our working capital management so that we are ready to execute on additional growth opportunities.

Now I will turn the call over to Rich to discuss the financial results for the quarter and full year.

Richard A. Manson - *Olympic Steel, Inc. - CFO*

Thank you, Andrew, and good morning to everyone. Before I review our results, I want to remind everyone about a few things that impact 2019 comparisons with 2018.

2019 results include revenues and expenses from McCullough Industries, which we did not own in 2018. 2019 also includes 12 months of Berlin Metals operating expenses, while 2018 only includes 9 months. And lastly, Section 232 tariffs enacted in late March 2018 had a profound impact on increasing 2018 volumes, sales dollars, gross margin and profitability, which reversed in 2019, making for difficult year-over-year comparisons.

Consolidated net sales for the fourth quarter totaled \$320 million, down from \$430 million in last year's fourth quarter. Softness in end user demand, including the impact of the GM strike and falling carbon steel prices, continue to have a significant impact on our overall results in the quarter.

Net sales for the full year 2019 were \$1.6 billion, down from \$1.7 billion in 2018. Operating expenses for the fourth quarter were \$67.6 million, down \$3.5 million or 4.9% compared with the fourth quarter of last year. For the full year, operating expenses were \$282 million compared with \$285 million in 2018. We were able to reduce our operating expenses in 2019, while absorbing an additional quarter of Berlin Metal operating expenses and the operating expenses associated with our 2 manufacturing acquisitions. We remain diligent to seek additional cost reduction opportunities in 2020.

For the fourth quarter of 2019, we reported a net loss of \$890,000 or \$0.08 per share compared with the loss of \$1.3 million or \$0.11 per share in the same quarter last year. The 2019 fourth quarter results include \$2.4 million of LIFO income compared with \$3.7 million of LIFO expense in 2018.

For the full year, net income totaled \$3.9 million or \$0.34 per share compared to \$33.8 million or \$2.95 per share for 2018. 2019 included \$3.7 million of LIFO income compared with \$8.4 million of LIFO expense in 2018. Our effective tax rate for the year was 27.1%. As we head into 2020, we expect our effective tax rate to be in the range of 27% to 28%.

Now turning to the balance sheet. We reduced our working capital by over \$115 million during 2019. Our DSOs were 40.1 days in 2019 compared with 41.2 days in 2018. And during 2019, we turned our flat-rolled inventory at 4.6x compared to 4.3x in 2018. And our pipe and tube inventory is turning at the fastest rate we have seen since our acquisition of CTI in 2011.

Capital expenditures totaled \$10.2 million in 2019 compared to \$17.7 million of depreciation expense. We estimate our 2020 depreciation to be approximately \$18 million to \$19 million and our CapEx levels to be less than depreciation.

During 2019, we generated approximately \$130 million from operations, which we used to reduce our debt by over \$110 million. At year-end, our debt was \$193 million, the lowest level we have seen since December 2017. We have plenty of availability under our low-cost, asset-based revolving loan to allow us to execute on additional acquisitions or organic growth opportunities.

Our Board of Directors declared a regular cash dividend of \$0.02 per share, which is payable on March 16 to holders on record as March 2. And this marks our 59th consecutive quarter that we have paid a cash dividend. Later today, we plan to file our Form 10-K, which will provide additional details on our operating results for the fourth quarter and the full year of 2019.

Now operator, let's open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Martin Englert with Jefferies.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Can you touch on quarter-on-quarter volume expectations across the carbon business as well as specialty based on what you're seeing thus far in first quarter '20?

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

Martin, this is Andrew. We expect that our first quarter volume versus fourth quarter of '19 will be better. And we expect our first quarter of '20 to be about the same as what we saw in the first quarter of '19. Our specialty metals continues to grow. So our first quarter, same thing is in carbon, we'll be stronger than our fourth quarter. And on a quarter-over-quarter basis from last year, same thing, we expect to see that volume up.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay. So kind of, if I understand that right, flattish year-on-year within carbon, but some growth in specialty year-on-year?

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

Correct.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay, understood. And similarly, if you could comment based on the pricing trends that you're seeing to date and anticipating throughout the corner, what kind of ranges would you expect for carbon and specialty gross profits per ton in 1Q?

Richard A. Manson - Olympic Steel, Inc. - CFO

Well, we can certainly talk about where the index pricing has been. So you saw a low as we were in October of '19. We saw in that mid-\$400 range we had by mid-January. It got up to just under \$600 a ton. And now we're starting to see a retreat. My expectation is that we'll probably see the numbers here maybe a little bit lower as we trend through the first quarter. On the specialty side, we certainly have seen a hit on the nickel side of



it. We saw it about the same time that the coronavirus was really talked about where commodities took a hit. And so we're seeing nickel lower today, and that certainly has impacted the margins on our specialty metal as surcharges have dropped. And we do expect that they'll come down a little bit heading into next month as well and then probably stabilize from there.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay. So it sounds like carbon may be a little bit of tailwind quarter-on-quarter from a margin perspective or gross profits per ton; and then specialty, a little bit of some headwinds?

Richard T. Marabito - Olympic Steel, Inc. - CEO & Director

I'd tell you, Martin, it's Rick. I'd tell you on carbon, probably a little bit of headwinds based on what Andrew said on basically the market pricing in the first quarter. And as you know, we saw prices on carbon really peak very early in the year, and they've been under a little bit of pressure. So I think first quarter on carbon, probably a little bit of pressure on margins, if you want to say quarter-on-quarter, fourth to first quarter. And then on pipe and tube side, seeing -- continue to see some strong results there. So I'd say favorable on pipe and tube in terms of being pretty flat with very strong fourth quarter results and then some -- a little bit of pricing and margin pressure on the other 2 segments.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay. So kind of rolling that all up together, we'll probably have some volume gains, but lower profitability across the volumes are going across in 1Q, yes?

Richard T. Marabito - Olympic Steel, Inc. - CEO & Director

Yes, I think that's right. And the volume gains will likely be on only in the specialty segment.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay, understood. But sequentially, volume gains more so across the business?

Richard T. Marabito - Olympic Steel, Inc. - CEO & Director

Yes, sequential. Yes.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay, understood. What type of demand are you seeing from yellow and green goods in the first quarter here? And how does that compare to what those customers indicated their demand would be like this year?

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

Yes, that's a good question. So certainly, the announcements from the yellow and green has been the expectation is going to be down. Our expectation is that we'll see some good volume. We've -- there's certainly important customers to us, and our expectation is that we should have a good year with the yellow and green.



Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Do you think it's running ahead of planned, meaning that some of these companies were expecting a down year, but maybe it's pivoting and we're actually seeing growth in 1Q here year-on-year?

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

No, I think 1Q start a little bit slower. I think that there was some inventory that they needed to work through. And so the expectation that January was going to start off strong probably has not in yellow and green. But as the quarter is progressing, we're seeing an improvement.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay, excellent. And if I could, one other one. The company has made notable progress diversifying its businesses in recent years, which has aided improved results across some of these, I guess, newer businesses. Have you looked into changes in the legacy carbon flat segment, perhaps shifting focus to a different customer base or changes in steel product offerings beyond some of the downstream additions that we've seen to improve the through-cycle profitability, I guess, essentially keep it more EBITDA profitable when we hit some downturns?

Richard A. Manson - Olympic Steel, Inc. - CFO

Sure. So strategically, you're exactly right. We've -- on the carbon side, we've looked at a couple of strategies. One is to continue to figure out ways to add more value to the carbon steel, inclusive of the acquisitions we made, but also internally doing more processing and creating more value to the base metal-based deal. Second, we've done a fairly good job of really focusing on the internal side of the business on the carbon from an expense standpoint and from an inventory turnover standpoint, Martin. And so what you're talking about that volatility, a big piece of that volatility is the obvious swings we see in the market pricing. And I think 2018 and '19 were perfect evidence of that. The swings and the speed of the swings in the market, for us, what we're intensely focused on is making sure that we're turning our inventory faster and we're trying to keep our inventory closer to the market. And we had some good success doing that in 2019, and we're certainly focused on improving that going into '19. So we talked about -- we turned our inventory, I think, 4.6 or 4.7x in carbon in 2019, and we're pushing to the goal of 5x. So I think that certainly helped in combination with pushing more into downstream value added. And acquisitions are certainly continuing to be a piece of that strategy.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

Okay. And maybe if you could just touch on, how much are you working with a hedging strategy to try to mitigate some of the volatility and to lock in your price/margin with some of your customer base, utilizing lagging contracts as well? Is there something you've explored a bit more to try to pull the volatility out of the business in carbon?

Richard T. Marabito - Olympic Steel, Inc. - CEO & Director

So we certainly actively follow and watch the futures in the hedging market. We do some hedging, but most of the hedging is not -- we're not hedging our inventory book per se. We're hedging exact business that we have, and we're marrying the hedge to the business we have with our customer, but that is something that we continue to take a look at. But at this point, Martin, we have not felt comfortable that hedging the actual inventory book would actually take some of that volatility away. But we'll continue to look at that, obviously, as that market continues to evolve and become a little more perfected.

Operator

(Operator Instructions) Our next question comes from the line of Chris Sakai with Singular Research.



Joichi Sakai - *Singular Research, LLC - Equity Research Analyst*

Just was wondering about your integration of EZ-Dumper. I wanted to just ask about how that's going?

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

Sure, Chris. This is Rick. It's going fabulous. We acquired the company in mid-year last year. It's fully integrated into our Pennsylvania operation, doing quite well. Obviously, it's a very small acquisition. The acquisition -- our other acquisition was significantly larger. But it's very small, but we're optimistic about the go-forward benefits of that acquisition.

Joichi Sakai - *Singular Research, LLC - Equity Research Analyst*

Okay, great. And one other question I had is, are you guys seeing any negative effects from the coronavirus on your demand?

Andrew S. Greiff - *Olympic Steel, Inc. - President & COO*

Chris, this is Andrew. We have not at this time, but we're certainly hearing from our larger customers, and automotive certainly being part of that, that potentially that could impact their business. But as of yet, we have not seen that impact.

Operator

Our next question comes from the line of Phil Gibbs with KeyBanc Capital Markets.

Philip Ross Gibbs - *KeyBanc Capital Markets Inc., Research Division - Director & Equity Research Analyst*

Rick, as you look at the M&A strategy, it seems like you're quite comfortable with what you've achieved last year with the EZ acquisition. Is there more to come this year on that front?

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

Yes. So Phil, we are comfortable. We also believe that continuing to grow our business and grow our profitability through acquisition is a good strategy. We're actively looking. I would expect in 2020 for us to make another acquisition. And really the criteria is really looking for businesses that enhance our returns and our profitability. So whether it's a service center or a metal manufacturing company, the key really is, is that it's a fit with the model of our returns and what those businesses bring with the integration of the full Olympic Steel behind those acquisitions. So yes, we're comfortable. We're actively looking to make acquisitions. And as I said, I would hope that we would acquire in 2020.

Philip Ross Gibbs - *KeyBanc Capital Markets Inc., Research Division - Director & Equity Research Analyst*

What's the mindset right now on inventories? Obviously, the market reduced risk last year as prices fell and demand softened up a bit. What's the mindset at the current time?

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

So our mindset is, as I spoke a little bit earlier, we're pretty focused on staying close to the market. And what that means for us is being laser-focused on turning our inventory. And so I spoke a little bit about being at 4.6, 4.7 turns on the carbon side last year. And we're pushing hard to get to that

consistent 5 inventory turn. Obviously, with fluctuations in volume versus maybe what market expectations are, sometimes that becomes a little bit more challenging, also with lead times changing. But we're pretty focused on that. I would tell you, probably as we move through 2020, we'll make progress towards that 5 turn. And we'll probably carry a little bit less inventory as we move through the year. And then I'd also add, we've been really successful in our pipe and tube business in terms of improving those turns, and I think we've got more opportunities on that side as well.

Philip Ross Gibbs - KeyBanc Capital Markets Inc., Research Division - Director & Equity Research Analyst

In terms of U.S. [MCA], I mean, I know you guys deal with a lot of U.S. manufacturers that produce here, ship here, ship abroad, but a lot of big time players that can make big time decisions. As you look at the changing policy with the region, is this becoming part of the discussion? Or is it -- or is it just more of a political talking point? I'm just trying to understand how real this could be in terms of content changes and if it's even part of the dialogue with the suppliers?

Andrew S. Greiff - Olympic Steel, Inc. - President & COO

So Phil, this is Andrew. I think your -- the second part is probably more so than the first. It certainly has become more politically charged. I think our customers that are in Mexico are continuing to build their participation down there. We haven't seen them pulling away. And I think the expectation was we were going to get to the point that we're at. I think when it comes to the auto content, I think that there's certainly more to be seen, and we have to understand that a little bit more. But I think our customers are pretty much status quo the way that it is today.

Philip Ross Gibbs - KeyBanc Capital Markets Inc., Research Division - Director & Equity Research Analyst

And my last question is, with a lot of the relationship with China being what it is and the push to bring back some manufacturing or diversify manufacturing bases, are you all seeing that happen? Is there a push to make that happen over the next couple of years, whereby your customers are going to be making more things here because of that policy?

Richard T. Marabito - Olympic Steel, Inc. - CEO & Director

Yes, it's a great question. I would tell you that we have seen that. It probably started 2 or 3 years ago. We have not seen a greater push since that time, but we certainly have been the recipient of manufacturing being shifted back to the U.S. from our large industrial OEMs. And I think at this point, they're just kind of maintaining where they're at. And I think that there's some pockets here and there, but I think we really saw the big push starting a few years ago.

Operator

Our next question is a follow-up question from the line of Martin Englert with Jefferies.

Martin John Englert - Jefferies LLC, Research Division - Equity Analyst

I wanted to ask about some aluminum processing. I know a number of years ago, the company had explored, I think, a tolling agreement for some aluminum-rolled products. And I just wondered, did anything ever come of that? Or is that something that could still happen in the coming year or years here?



Andrew S. Greiff - *Olympic Steel, Inc. - President & COO*

The answer is, it could still happen going forward. It did not happen in the way that we had anticipated, but we have continued ongoing discussions that we're optimistic that we'll see some of that going forward.

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

Yes. And I think, Martin, we've been pretty successful in the last year growing our aluminum business, some of it on non-automotive, actually. Specifically on that automotive business that we had talked about a few years ago, that just never materialized from the customer perspective. So we didn't -- not get that business because it was awarded to somebody else, that was just at the customer level. They decided not to go forward with some of the plans they had on that processing. But as Andrew said, we're optimistic about our aluminum business. And I am very confident that's going to be a business that we continue to grow moving forward.

Martin John Englert - *Jefferies LLC, Research Division - Equity Analyst*

Okay. And one last one, if I could. Do you have an opportunity if you wanted to, to try to increase your tolling volumes? I know it's a portion of the mix and has been for a number of years. But is there an opportunity, I guess, to grow that and better leverage some of your fixed costs?

Andrew S. Greiff - *Olympic Steel, Inc. - President & COO*

Yes, Martin, this is Andrew. The answer is yes. We do. And we are actively looking in that area today.

Operator

There are no further questions in the queue. I'd like to hand the call back to Mr. Marabito for closing remarks.

Richard T. Marabito - *Olympic Steel, Inc. - CEO & Director*

Thank you, operator. Once again, thank you for joining us this morning and for your interest in Olympic Steel. We hope to speak with some of you at the Bank of Montreal Global Metals & Mining Conference next week. In the meantime, have a great day, and we look forward to talking with you again next quarter. Thank you.

Operator

Ladies and gentlemen, this does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time, and have a wonderful day.



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