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The Boeing Co. (BA)

BofA Global Industrials Conference

CORPORATE PARTICIPANTS

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

MANAGEMENT DISCUSSION SECTION

Unverified Participant

Thank you for joining us. Brian West, CFO and Executive Vice President, Finance of the Boeing Company. Thanks for taking time out and spending it with us today.

Nice to be here.

QUESTION AND ANSWER SECTION

Q

Yeah. So maybe to just start it off. There's been a lot of headlines about Boeing lately. How do you think about what's confronting Boeing and what is Boeing doing that encourage the changes required for the company to really emphasize a focus on quality, safety and compliance?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Let me first start by saying that we continue to be fully committed to transparency and accountability with our regulators. The FAA is deeply involved and undertaking a tougher audit than anything we've ever been through before. And as they do their important work, we're undertaking comprehensive actions, so that we can move forward to strengthen quality and build confidence.

There's changes that need to happen. There's no doubt about it. But we're going to do so diligently and expeditiously. But we won't rush or go too fast. In fact, we're deliberately going to slow to get this right and we're the ones who made the decision to constrain rates on the 737 program below 38 per month until we feel like we're ready and we'll feel the impact of that over the next several months. The events of January the 5th in Alaska Airlines Flight 1282 and everything we've learned since, we acknowledge that we need to improve upon safety and quality and conformance. And one area that we're focused on in particular is something called traveled work. Traveled work has existed for a very long time and in recent years, we tried to get ahead of it. Turns out it wasn't enough.

So now, our CEO, is calling for a step change improvement in how we think about traveled work. And I've known him a long time and he is determined on this point like I've never seen because it speaks to our culture and it speaks to our people. For years, we prioritized the movement of the airplane through the factory over getting it

done right and that's got to change. The leadership team got it in the immediate aftermath of January the 5th. We control how this happens, and it's about our resolve to get ahead and get after traveled work. And Dave is in the factory, personally making sure that we do get control of it because once you do reduce traveled work, your quality gets better, your stability gets better and probably most importantly, the work of the mechanic gets better. And they know that better than anybody – better than anybody. And we've got to listen and act on their behalf and this goes beyond the 737 program. All BCA programs and factories have to deal with this and it's going to impact them in the near term as well.

Beyond our own factories, traveled work also is something you have to think about with your supply chain. And we've got work happening there too. In fact, starting on March the 1st of this year, we no longer travel work between Wichita at our fuselage supplier, and Renton. It had been going on too long. So now, we will only accept a fully conforming fuselage from Spirit, which means in the near term, there might be variability of supply. But long term, the predictability that we're going to get is dramatically better and the non-conformances dropped significantly in our factory because it takes those non-conformances and it pushes them upstream where they belong to get actioned. That is an example of a step change improvement that Dave is looking for and we're getting after it.

Beyond traveled work, the other things that we're working on to get after safety, quality and regulatory compliance are around things like training, tooling, our quality management system and how that links with our safety management system and picking up the signals on the factory floor, incentive compensation, to name a few. So, rest assured that there's a lot of change happening at Boeing right now and it's a hard moment and we're probably better because of it, but I'm confident that we're going to see our way through it.

Q

So, just kind of following up on one of your comments. Can you speak to the news that Boeing might reacquire Spirit? There's been a lot of incoming questions I get, I'm certain you have. How are you thinking about the longer term strategic synergies and so on and so forth?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

So you all would have seen our response to the discussion in the media. When there's more information to share, we certainly will do that. I would say I'd point back to comments that Dave made in January around how Boeing, more than 20 years ago, probably got a little too far ahead of itself on the topic of outsourcing and this is probably the example. We believe, and Spirit believes, that reintegrating these two companies is what's best for safety and for quality for the aerospace industry. We have conviction on that.

And without going into synergies and efficiencies, it's really about focus and running that business, not as a business, as a factory. Run it as a factory and stay focused on safety and quality and stability and that opportunity sits there. And I will also say that one thing that I've commented previously is how important our investment grade rating is to us. And we work very closely with the rating agencies. And I will say that if a transaction were to occur, we would not use equity. We would fund it with a mix of cash and debt. But in terms of how that all plays out, can't comment, but the discussions are happening.

Q

Got it. Got it. Got it. When investors are thinking about the stated financial targets that were put out before some of the stuff happened, what framework should they be thinking about now from that perspective?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

I'll pick up from my earlier comments. The path to stable financials is a stable factory and that's what we're focused on right now. In regards to the longer term, the vision and the framework that we laid out in November of 2022 is still intact. It's still intact. It's going to take us longer to get there.

Yeah.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

If I think about BCA, for example, commercial demand continues to be robust. We've recently got orders from American on the 737-10. We've got Thai on the 787 order. Ethiopian put in an order for the 777X. So, there is real momentum and we continue to grow.

I'd also point out that on the demand discussion, both the 787 and the 737 are sold firm through 2028. So, we're quoting 2029 and early 2030s. So that's a steady picture that's been there that is underwriting everything. So, the backlog's big and that backlog also represents over seven years of production that we've got to go fulfill.

At the same time, we've got these two big shadow factories we've discussed, one is the 787 – one is the 737. We are intent on shutting them down as we exit this year and liquidating those – that inventory, delivering those airplanes to our customers. And the productivity benefit is enormous because you're going to take some of our most highly skilled labor and point it away from rework and point towards first-run production. That's pretty powerful. And then when the time comes, there is an opportunity to increase our rates in our commercial business. And my guess is that's going to happen. And the commercial business, we think about that, managing it for that longer term 2025-2026, the pieces still hold.

As it pertains to our defense business, equally, there's some very nice, robust demand given the global threat environment that we find ourselves in around the world. And we are competing and our products are showing up nicely and missions are being supported by our customers. We, at the same time, are de-risking these fixed price development contracts. Every day that goes by, there's less risk as we move towards delivering those for our customers.

I'd also say that in BDS, even since November 2022, we've made even more progress on tightening the underwriting standards and the contracting is getting stronger. And then more broadly, we expect the portfolio within our defense business to stabilize so that all the products are collectively going to deliver margins that are in the high single digits as we think about the 2025-2026 timeframe and the business will throw off meaningful cash flows.

So again, the pieces are holding, lot of work to do. On BGS, wonderful services franchise that's set up well for the long term. It's going to grow in the mid-single-digit top line. It'll be capital-efficient. The margins are the mid-teens. The cash flow conversions are high. And I would also say that this is a part of our business. It's the most global – it's got the most global footprint and we've got thousands of colleagues who are out with our commercial and our

defense customers all day every day to understand what their needs are and how the fleets are performing and that's incredibly powerful information that we bring back to the company. So, BGS also, pieces are clicking.

With regards to capital allocation in our framework, no change. We want to generate cash after having invested in our own growth and then de-lever the balance sheet. And as I've said, the investment grade rating is still a priority. And when all is said and done, we believe the \$10 billion of free cash flow that we put out there, it's going to take us longer to get there than we planned. It'll be further out in that 2025-2026 window. But we believe that the actions that we're taking right now better position us for that long term.

Now, let's talk about here and now. So, we did not give annual guidance, but I will say that there are some important changes that you have to consider. So as we have decided to hold airplanes in position longer and get after this traveled work broadly, it is going to impact revenue, earnings and cash flows both in the quarter and in the year. And in the quarter, our free cash flow will be a usage of somewhere between \$4 billion and \$4.5 billion and that's higher than we originally planned back in January and there's two things driving it.

First of all, there's a combination of lower deliveries, lower volume at BCA and negative mix from inventory airplanes. That's a big piece of the delta. And then there are some working capital pressures, both inventory as well as some receipt timing. That is what's going to happen in the quarter, and we also believe that some of that will not be made up for, for the full year. So, the full year free cash flow is expected to be in the low single digit billions of free cash flow generation. We are not at the moment where we can manage the near term for these financial outcomes because of the work at hand around stability. But I will tell you, we're doing everything we can to make sure that we exit the year stronger and we still are intent on delivering and solving for that long-term target that I just went through. And our expectation is that we'll get more predictable and better positioned not only for our customers, but for our investors. It will take time.

Q

So maybe as a follow-on, you addressed a bit, how should investors think about a rate ramp? We always get that question, you always get that question. So, how in that backdrop that you painted, how should we think about that?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

So with rates, I don't know exactly what the rates are going to be for reasons I described. So, I'm not going to guess, it's not the right time. But I will say that our objective is to get quality up, get traveled work down and drive supplier stability and some things that have happened recently that reinforce all three of those. I talked about quality and traveled work. As it pertains to suppliers, we have recently updated our master schedule to reflect this slowdown that I've mentioned in the factory. But I will tell you that our objective is to keep with the practice that we had in the post-pandemic recovery, where we held the supply chain and paced them just ahead of final assembly.

And we're going to keep doing that. What it also means is that some suppliers, we are going to pace differently and it will get tactical. The ones who are behind get caught up, the ones who are ahead get to slow down. And we're managing that supplier by supplier as we speak, in fact. We understand that when we do this, net-net, there will be spots where we are going to build inventory and we're doing that because we believe when the time comes and we want to increase our rates that we want to do it in a way that it's stable. A very stable fashion is our objective.

So, yes, it's an investment, but we view it as an important investment as it's going to be a cash headwind. It's going to be an important investment when you consider the size of that backlog. We're just going to have to do it and face into it. So in terms of the timing, we're going to take advantage of this moment. We are going to get the suppliers back where they need to be if they were behind. And we're also going to incorporate these findings that we have from our own 737 factory team, as well as the FAA because lots of things that are coming in that we want to change the production system and we're going to do that. At the end of the day, I think on the 737, the way I think about it is the first half, the rates will be lower, second half, they're going to be higher. As we get towards that 38 per month and beyond 38 per month, will be up for the FAA.

Q

Got it. Got it. So, how do you manage the customer expectations? Right. I mean, there's been a fair number of headlines from customers that are not happy with not getting airplanes. How do you manage that as a company to keep the customers happy?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Yeah. We put the customers in tight spot, the most important thing we do is communicate with them. And they have been supportive of everything we're trying to do to enhance safety and quality for the industry. We are in regular, very transparent communications and they know precisely where we stand and the progress that we're making and we, at the same time, have to understand what their needs are as they think about their flight schedules and their passengers.

So, in the near term, the slowdown has impacted us and it's impacted them and we're communicating it to them so that we can work our way through it and we will stand behind our customers. In the medium term, we are using the flexibility to help support the customer. And what I mean by that is the production lines in Renton can do any minor mix model. So, we will adjust and we'll be flexible to make sure that the customers get the airplanes they need in the near term. In the longer term, particularly in our 737 family, we believe that the markets can grow. We believe that the product performs very well in the marketplace and we're going to keep proving out its capability. And ultimately, our job is to make sure that we can execute on behalf of our customers in a way that's more predictable, more dependable, with the highest quality in mind and we're going to do that one airplane at a time and our customers are hanging with us and we're appreciative of that.

Q

And from a penalty perspective, is there any compensation that customers are seeking or are we in an environment where there's so much demand for airplanes that that's off the table?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

So, as it pertains to the events of January the 5th, of course, there's customer consideration that is going to manifest itself in the quarter, in the P&L and we've got to take care of that and we're well down the road to do that. And we continue to stand behind our customers with that responsibility.

More broadly speaking, as we think about delivering the backlog, these changes and how they impact our customer fleets will create conversations. They could be in a position where there are some things we're going to

have to do, but we want to make sure it's contained because our customers really want lift and there's enough flexibility in the skyline to try to get them the right lift. It might be some changes about when and what model. But our objective is to try to satisfy their growth targets and we're hard at work to do that. And if there's an impact, we'll deal with it. But there's nothing that's significant as I stand here today.

Q

Got you. And is there any one particular area that worries you most when you think about what's going on? Is there any one tent pole that's a little longer than the other ones?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

I would say our ability to get – executing on this new step function – step change that Dave has described is really important because it requires a lot of focus and everyone going in the right direction. I would say in the last couple of years, three, four years, 2021 beyond, there's been a lot of work at the company. There's been a lot of progress. We ungrounded the entire MAX fleet. We went from producing zero 737s to getting to a rate of the low to mid-30s. We stopped production for a prolonged effort well over a year on the 787. We stood up two shadow factories to deal with the rework for those airplanes on both the 737 and the 787. We've dealt with China. And it turns out, all of that wasn't enough and we were reminded of that on January the 5th. And now, it's a clear message. There's more work to do and we're not going to be satisfied until we complete this journey and it's going to be all the things that I outlined earlier around making sure that we can do it in a predictable, dependable, high-quality fashion to deliver those airplanes for customers. So, there is a lot of work to do right now and we want to do that constructively with our regulators and that's job one.

Q

Got it. Got it. You mentioned China. But how should investors think about demand for airplanes out of China and when could we potentially see orders? And that's sort of the one thing that is out there.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

China is a very important market. We've been in China for over 50 years supporting our customers and seeing this amazing growth over decades. We like to see the strong traffic recovery that's been happening. As you know that it was about a little over a year ago where we began to return the 737 MAX fleet to service in China and that happened through the course of last year, happened in a very deliberate, conscious way and it got 95-plus airplanes flying and generating revenue for our customers out there. Good sign and we're supporting them as they made that move.

Now, there's 85 airplanes that were in inventory at the end of the year. That's the focus. We want to make sure we get those airplanes delivered to our customers as they go integrate them into their fleet and grow their businesses and we're hard at work at that. And having very close conversations as we understand all those near-term requirements, and of course, we want to understand where they're headed long term. Important market, focus on return and delivery and very exciting times.

Q

Got you. Got you. Another question I think that's on investors' minds is, how should we think about the timeline for the certification of the 737-7 and 737-10?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

So, on the 737-7 and the 737-10, the timelines that we discussed recently are unchanged. Important to know that there are separate teams both at Boeing and in the FAA working on three very important work scopes. There's the anti-icing effort. There's the 737-7 certification and there's the 737-10 certification. On the anti-icing, that is an effort that we have swarmed our very best resources on to determine a design solution and we're making good progress on that front. That's likely going to take us until towards the end of the year. We've got to harden the design. We've got to perform all the testing and the analytics that go associated with that, working closely with our engine partners, working closely with the FAA. So, that's moving forward nicely.

On the 737-7, we're essentially complete with our documentation requirements and now it's with the FAA. And it will be done in conjunction with the anti-icing efforts that I described. On the 737-10, that's an airplane that in December of last year, the FAA began its flight test program and that's also progressing well. Keep in mind, the airplane, the 737-10, has been flying for two and a half years before the FAA even started its flight test program. So we feel confident. And specifically on the 737-10, finish the flight test program. We want to incorporate the anti-icing solution from the 737-7 because it's a common solution for the 737-7 and the 737-10, and in fact, it's the common solution for the 737-8s and 737-9s that are in the field and then on the 737-10, complete the documentation and the analytical requirements. And our expectation as we move through those milestones is that we will take all the lessons that we've learned collectively with the FAA partner to bring that into the process of the 737-10 certification so it can move at pace. Ultimately, we've got work to do, certification decision and the timeline is up to the FAA.

Q

Great. Got it. Got it. With shorter term financial targets off the table, can you speak to all longer term how we could think about BCA margins?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Yes. So BCA margins in the fourth quarter of 2023, they started to give you a little indication of what can happen when things start to go right. Now, I'm not cheering over it was low, but it started to show the trajectory. On BCA, when you can get higher delivery volumes, when you can get better mix, you can have lower abnormal costs and you get the benefit of operating leverage, margins are going to improve.

Now the first quarter and, I guess, long term, but I say first quarter margins at BCA, because of the events of January 5th and everything I described, are going to be more like negative 20%. So, it's going to be impacted for those customer considerations I mentioned and all of the things we're doing around the factory. But we expect BCA margins to get better through the year. They'll still be negative in 2024. But if we run the business for the long term, we believe that those margins are going to get to historical levels in the 2025-2026 timeframe because you're going to have shut down two shadow factories, you're going to have better mix going your way and you're going to have operating leverage from what we expect to be higher production rates.

So, it's a lot that's got to happen between now and then. But the pieces, as I mentioned, still hold together where the BCA margin business gets back to where it was.

Q

Got it. Got it. Maybe changing gears a little bit for the Defense. When you think about the Defense business and you look at the budget request that came out just last week, the Biden administration's budget request, how does that line up for BDS?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Well, let me just say, broadly speaking, overall demand before we get into the budget, overall demand continues to be pretty solid. And what we're seeing is that not only from our US government customer, but also from our foreign allies. Keep in mind, our backlog for international is about 30%, but our revenue today, it's more like 20%. So there's this natural expansion opportunity as we fulfill that backlog. And when that happens, it's going to be better mix and accretive margins. So, we look forward to delivering those important products to our customers, both in the US and especially in international markets and that's pretty good – that's pretty good opportunity for us.

And specifically, very proud of the team that has the P-8 wins in Canada and Germany. It's done a nice job with Australia. Australia government wants to put more money in MQ-28. The Apache is winning. The recent FARA news creates more opportunity for the vertical lift, both Chinook and Apache. And then you round it out with your long-term momentum for the T-7, the MQ-25 and the KC-46. So overall, broadly demand for our Defense products and capabilities, very solid.

As it pertains to the budget, nothing really was surprising there. It landed pretty much a build on what was 2024 Presidential budget which, by the way, hasn't been authorized yet. So, we expect things to move around. But just tactically in the President's budget, we had good inclusion of vertical lift for both Chinook and Apache for the US customer. We had the F-15EX and the F-18 modernization programs, the KC-46 tanker is in there. Missiles and weapons support, the space launch systems in there, continued commitment to development for the T-7 and the MQ-25. So there's a lot of activity and we like where we're positioned.

Q

And then maybe as a follow-on, there's some high-profile competitions going on out there today with NGAD, FA-XX, the multiple unmanned programs that are out there. How should investors think about Boeing and bidding and that whole complex?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Let me just say that we feel very confident in the capabilities that we bring to bear as it pertains to the warfighter, particularly in what we call air dominance fighters. So great franchise. Wonderful innovation happening. And we feel very good about what our long-term prospects are, broadly speaking.

I would say in terms of the contracting question, I said this before, rest assured that we have changed our underwriting standards in our Defense business. We will not take on another fixed price development program and where competitions go, we stand ready, but we'll be very conscious both of the capabilities that we have that completely differentiates the fight with trying to make sure we're prudent and responsible in terms of what the investments and the economics are over the long term.

Q

Got you. And then on Defense, there was a couple of headlines that came out, I think early, late last week – early this week about, if you can speak to it about Boeing maybe selling off some Defense assets.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

We love our strategic position across our Defense portfolio. The ones that I saw got mentioned...

Q

Yeah.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

...and while I won't speculate...

Q

Yeah.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

...pretty small.

Q

Okay.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

...to us both economically and strategically in some of those old, old news. So, we are enthusiastic about our Defense portfolio for sure.

Q

Got you. Got you. And then maybe changing gears again to the future. How is Boeing thinking about new airplane development? It seems like on 737 that I'll speculate here, not asking for a response, there probably won't be a MAX II. So, what – how is Boeing thinking about that?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

So let's talk about the future, broadly speaking, versus just next airplane question. There is a lot of investment and innovation that's happening in the company, even as we stand in this moment where we're focused on execution. By the way, our investments on execution have been also pretty dramatic since 2019, mostly in our workforce. Our engineering talent, up 10%, manufacturing team up 11%, our quality team up 25%.

So, we're making investments in the here and now, I don't want that to be lost on anyone and all of those resourcing levels across our workforce are higher now than they were pre-pandemic. So that's important because the most important investment we make is the here and the now. That gives us the ability to think longer term and the longer term things you mentioned, we look forward to delivering an airplane that is fully SAF-compliant by 2030. We look forward to delivering a replacement cycle where we're going to have significant improvements in efficiencies and emissions as airplanes re-fleet.

As it pertains to longer term, there needs to be advanced engine technology and aerodynamic investment in order to get an airplane that's 20% to 30% more efficient than we are today and that will not be rushed. I will say that there is broad investment around capabilities in order to get to another platform in the future. And we're working on those capabilities and investing behind that innovation as we speak and we'll continue to do that and it's not going to be outside the envelope of the financials I described, but it is going to position us for the future. Whatever that future looks like, it's not the right moment, but our people are working on capabilities that we know are going to be part of that eventual solution.

And I'll close with – we spent \$5 billion between R&D and CapEx in 2023. That's 20% plus higher than it was the previous year. So, we are investing and we're ready to do it. What it actually looks like, too soon to say.

Q

I think we have time for maybe one more, two more.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Yeah.

A

Q

You've got some upcoming union negotiations, right, IAM 751, the union that represents the machinists in the Puget Sound. Their contract runs out on September 12th, if I remember right. How are you thinking about that? Having a stable workforce that's energized and retained and the whole thing.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

So, your timing is right. Negotiations began earlier this month. The meetings are productive. We will closely evaluate their initial proposal. I'll always leave specifics to the teams closest to the work, but I believe there's a path to a fair and reasonable agreement. And yes, we completely recognize the importance of our skilled workforce, particularly in the Puget Sound area. They are loyal Boeing employees. And we believe in them because they believe in our products and they believe in the work that they do all day every day to deliver products to our customers. And yes, you want to make sure you keep that enthusiasm moving forward. Like I said, my expectation is we'll get through this and we'll move on.

A

Q

Got it. Got it. And then maybe we'll end on a bright spot. And you brought it up earlier. Services, can you speak more to that and maybe peel back the onion on services, what's going on there?

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

A

Definite bright spot and there's been some nice things happening in that part of our business. Broadly speaking, they are back to pre-pandemic levels, which tells you a little bit about the health and the future of that franchise. There's good momentum.

I would also say that we've done some things differently in the last few years around our business. We've gotten a bit tighter on capital allocation. We are very focused on accretive offerings, particularly ones that are heavy and intellectual property. And we've also decided no longer to chase aspirational targets that might chase market share. We're trying to deliver a very strong business in support of our customers and we're doing that. It's going to have good mid-single digit revenue growth for quite a while. We're confident that it's going to throw off mid-teen margins and the free cash flow conversion is very high. And as I said, our workforce is globally deployed. They're all over the world with our customers, both in the Commercial and the Defense space in order to help support our customers in their missions and then bring all that intelligence back into the company, so we're stronger and we're better for it. So, I've got a lot of enthusiasm and optimism for our services franchise and we got a great team that's executing on that every single day.

Unverified Participant

Okay, Brian, thank you so much for taking the time.

Brian J. West

Chief Financial Officer & Executive Vice President-Finance, The Boeing Co.

Thank you. Good to see you.

Unverified Participant

It's a pleasure.

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