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PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Second Quarter 2024 Franklin Covey Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to turn the conference over to your speaker for today, Derek Hatch. Please go ahead.

Derek Hatch *Franklin Covey Co. - Corporate Controller of Central Services - Finance*

Thank you. Hello, everyone. On behalf of Franklin Covey, it's my pleasure to welcome you to our conference call to discuss our second quarter fiscal 2024 financial results. We hope that you're enjoying good weather wherever you are in the world this spring or fall if you're in the Southern Hemisphere.

Before we begin this presentation, we'd like to remind everybody that the presentation contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements are based upon management's current expectations and are subject to various risks and uncertainties, including, but not limited to, the ability of the company to grow revenues, the acceptance of and renewal rates of our subscription offerings, including the All Access Pass and Leader In Me memberships, the ability of the company to hire productive sales and other client-facing professionals, general economic conditions, competition in the company's targeted marketplace, market acceptance of new offerings or services and marketing strategies, changes in the company's market share, changes in the size of the overall market for the company's products; changes in the training and spending policies of the company's clients and other factors identified and discussed in the company's most recent annual report on Form 10-K and other periodic reports that are filed with the Securities and Exchange Commission.

Many of these conditions are beyond our control or influence, any one of which may cause future results to differ materially from the company's current expectations. And there can be no assurance the company's actual future performance will meet management's expectations.

These forward-statements are based on management's current expectations, and we undertake no obligation to update or revise these forward-looking statements to reflect events or circumstances after the date of today's presentation, except as required by law.

With that out of the way, we'd like to turn the time over to Mr. Paul Walker, our President and Chief Executive Officer. Paul?

Paul S. Walker *Franklin Covey Co. - President, CEO & Director*

Thank you, Derek. Hello, everyone. Thanks so much for joining us today. We're glad to have the opportunity to talk with you. Joining me today are Steve Young, our CFO, Jennifer Colosimo, the President of our Enterprise division; Sean Covey, the President of our Enterprise division and other members of our executive team.

Our results for the second quarter came in right in line with our expectations, with revenue of \$61.3 million in adjusted EBITDA of \$7.4

million, which was slightly stronger than expected. And our free cash flow was stronger than expected, \$24.7 million in the first 2 quarters of this fiscal year.

In addressing our performance for the quarter and year-to-date, I thought I'd start out by organizing my comments into 3 categories. First, the areas that have been a challenge in which we're not particularly pleased with.

The second, the areas that are going well and that we're encouraged by. And then third, 3 areas of focus that we're really excited about and that we believe are going to accelerate our growth.

First, let's talk about the areas that have been a challenge in which we're not particularly pleased. I'm not pleased that our services sales didn't rebound as rapidly as we thought and that as a consequence, reported revenue for both the third and fourth quarters and for the year are going to come in lighter than we expected when we reported our Q1 results.

As a result, rather than achieving low double-digit revenue growth in the back half of this year, as we had expected, we now expect reported revenue to grow approximately 1% in Q3 and 6% in Q4. I'm also not pleased that since last fall, there's been an environment in which companies decision-making has been extended longer than normal.

During the late summer and early fall, as interest rates spiked, many organizations either eliminated costs or pushed off decision-making. This impacted 2024 budgets and created a more difficult selling environment for us in the first half of fiscal '24.

And finally, I'm not happy that even though, we do expect adjusted EBITDA to increase significantly this year to \$54.5 million in constant currency, that result will be only within the low end of our guidance range of between \$54.5 million and \$58 million.

Second, I would like to share a few things that are going well and which we are excited about and encouraged by. The first of these is, as I said a moment ago, we're now expecting reported revenue to grow approximately 1% in Q3 and 6% in Q4, which is accelerating from the first half of the year.

And I just want to point out, this 1% and 6% reported revenue is largely revenue that's converting from prior period sales activities and is also muted somewhat by lower-than-anticipated services sales, and those services are recognized in the period that they are sold and delivered.

In our subscription model, the majority of what will actually sell between now and the end of the year will not be recognized this year, but it would be deferred and add to our growing deferred build and unbilled subscription balances to come into revenue and be recognized next year.

The volume of subscription sales we're selling today and that we expect to sell in Q3 and Q4 is actually growing at a rate faster than the 1% and 6% reported growth that we're expecting in this year. This will put, as I mentioned, more deferred billed and unbilled revenue on the balance sheet to come into revenue next year, and that's happening at the same time, we're beginning to see our booking pace and our services sales accelerate.

The second thing that I'm pleased about is that, despite the economic environment and revenue being lower than expected, we expect that both the company's overall revenue and the revenue in both the enterprise and education divisions will still reach all-time highs in the third and fourth quarters on top of all-time high comparisons from the previous year.

And I'm pleased that revenue in the overall business has grown significantly over the past 4 years to more than \$280 million.

Third, I'm pleased that in addition to generating record levels of revenue, due to the strength of our business model with its high recurring revenue, strong gross margins, SG&A that declines as a percentage of revenue and low capital intensity, we expect both adjusted EBITDA and cash flow to come in strong for the year.

We expect adjusted EBITDA for the year to increase to approximately \$54.5 million in constant currency, up from \$48.1 million last year. We also expect to generate a very significant amount of free cash flow for the year.

As I mentioned, year-to-date through this year's second quarter, free cash flow has been \$24.7 million compared to \$3.3 million through the second quarter of last year. As you'll recall, free cash flow in the first half of last year was reduced somewhat as a result of changes in working capital.

And what I'm really pleased with is the resilience we've been seeing in the enterprise and education businesses and with the positive direction of some of the recent trends we're seeing across key parts of the business.

I thought I would just share for first a few of the points of resilience we're seeing in enterprise and education and then a comment or two about some of the trends in leading indicators.

In the Enterprise division, each of our 6 key indicators remains strong and resilient in the second quarter and year-to-date. First, we had very strong logo retention. In fact, the second quarter was one of the best quarters we've ever had in terms of logo retention.

Second, our revenue retention for the quarter and year-to-date was also very strong, continuing to be higher than 90% and with the pattern of client renewals being consistent with historical patterns.

Third, as shown on Slide 4, our subscription revenue also grew to an all-time high for the second quarter, year-to-date and latest 12-month periods, reaching \$26.3 million in the quarter, that was up 9%, \$53.1 million year-to-date, up 11% and \$104.5 million for the latest 12-month period, which is up 9%.

The fourth point about enterprise is that the percentage of total All Access Pass contract value for multiyear periods increased to a historic high 62% compared to 57% at the end of Q2 last year. And in addition, the percent of total All Access Pass contracts, which are for multiyear periods increased to a historic high of 56%, up from 50% at the end of Q2 last year.

The fifth point is that our deferred revenue, billed and unbilled, reached an all-time second quarter high balance of \$128.7 million versus \$124.8 million at the end of last year's second quarter.

And finally, the round out Enterprise. Our total subscription and subscription services revenue increased to record levels for the second quarter, year-to-date and latest 12-month periods with \$37.5 million of subscription and subscription services revenue in the second quarter, \$79.1 million year-to-date and \$162.1 million for the latest 12 months.

While this combination of subscription and subscription services sales achieved a historic high watermark, its growth rate was muted somewhat by the fact that while clients have continued to purchase, renew and expand their All Access Pass subscriptions and purchase a substantial number of subscription services.

As noted, they have been purchasing a somewhat smaller amount of those services. This is a pattern we've seen and spoken about over the last couple of quarters.

In the Education Division, as shown on Slide 5, education subscription revenue grew also to an all-time high for the second quarter year-to-date and latest 12-month periods, reaching \$9.5 million in the quarter, that was up 7%, \$19.3 million year-to-date, that's up 7% and \$40.9 million for the latest 12 months, up 10%.

Second, in education, amounts invoiced also grew to an all-time high for the second quarter and for the year-to-date in latest 12-month period, reaching \$9.8 million in the quarter, representing 23% growth, \$18.1 million year-to-date, that's up 14% and \$79.7 million for the latest 12 months or growth of 13%.

Third and finally, for education. While it is still early in our contracting year, the number of new schools we've contracted is significantly

higher than it was at the same point last year, a year in which we added a record number of schools. In addition, the number and percent of schools retained is also up significantly year-over-year.

I'm also particularly encouraged by the progress we're making on many of the important leading indicators that point toward accelerating growth and thought you might find a few of these interesting and helpful. Specifically, I'll talk about the areas of new client acquisition and then, of course, services bookings.

First, related to new client acquisitions. We closely track the leading indicators related to new client revenue growth. Two important metrics in North America are the number of people participating in our marketing events, where thousands of prospective clients join us throughout the year to learn more about Franklin Covey solutions; and second, the volume of new client acquisitions that actually enter into our pipelines.

As it relates to the number of people participating in our marketing events, we're very pleased with the year-over-year growth we're experiencing in that participation rate and particularly over the past 120 days.

We're experiencing a meaningful increase in attendance on a year-over-year basis, and this strengthening is due in part to high interest in our new speed of trust and navigating difficult conversation solutions, as well as general interest in our overall solutions to help organizations improve leadership, culture and execution.

We would expect this increase in participation rates to lead to an increase in new client opportunities entering our pipeline, and it is.

As it relates to increases in the volume of new client opportunities that are entering our pipeline, over the same last 120-day periods, our pipeline of new client acquisition opportunities has also increased steadily on a year-over-year basis.

While we, of course, don't close every opportunity that enters our pipeline, this acceleration in new client pipeline is a positive leading indicator of future new client growth, of course, that we can then add services too and expand and retain.

The second area I would just talk about as it relates to these leading indicators is, we closely, as you would imagine, watch our subscription services booking pace. Booking pace is important because before we can deliver services, we first need to book them and get them scheduled with the client.

Just maybe a note about services. When a person buys a subscription, whether that's All Access Pass or Leader in Me, included in that purchase is access to either an implementation strategist in our enterprise division or a Leader in Me coach in the education division. And they're there to help the client drive maximum impact of their subscription.

In addition to those services, which are included in this subscription, clients can also purchase access to Franklin Covey delivery consultants to train and coach their employees on an as-needed basis to help deepen the impact. When we refer to subscription services, it's those services we're talking about.

Prior to the pandemic, the attachment rate of services to All Access Pass subscriptions had steadily increased, reaching 55%. So, \$0.55 of every dollar in every dollar of subscription was represented by subscription services. We reached that level in 2019.

During and in the post-pandemic work from home environment, clients took advantage of our tremendous live online services delivery capability to engage their remote workers, and this pushed our services sales above their normal attach rates all the way to 60%.

That specific pandemic and post pandemic use case has moderated somewhat, and our return to the pre-pandemic high services attach rate is actually a primary contributor to our reduced services sales this year. We expect the services attach rate to be high. We expect it to end the year at 55%, which is about what it was pre-pandemic.

However, despite the environment and despite this tougher comp, we've been encouraged from a leading indicator standpoint, that in

our US and Canada enterprise business, our services bookings, again, a leading indicator of future services revenue, which has been down to prior year, 60 days ago, and in the last 60 days is now ahead of prior year.

While the purchases of services over the past couple of quarters have been down slightly compared to last year's elevated levels, we expect increases in the purchase of services to be a strong contributor to our revenue growth in the second half of this year and into next year.

First, we expect to achieve strong services revenue growth in the education division, particularly in the fourth quarter, when new schools and districts typically complete a meaningful portion of their onboarding training and coaching prior to the start of the new school year.

And second, as I've shared, we also expect to see a rebound in All Access Pass' client's purchase of subscription services in the enterprise division. I'm encouraged by these trends and thought you might find those insights into the business interesting and hopefully helpful.

So, so far, I've shared with you what I'm not pleased with and also areas that we're encouraged by. And I'd now like to transition to my third point, before I turn time to Steve, which is to talk about some areas in which I'm excited in which we believe will accelerate our growth.

I'd like to briefly share 3 big executable opportunities for accelerating our growth that are right in front of us, and we're executing on these key initiatives, which we expect both individually and collectively will make major contributions to not only continuing this growth, but to meaningfully accelerating it.

As shown on Slide 6, the first of these opportunities is what I'm going to refer to as project penetration. Since the launch of All Access Pass, 8 years ago, the company has become quite good at retaining All Access Pass clients, expanding All Access Pass' penetration levels within these clients and providing clients with best-in-class services to help them achieve their most important jobs to be done.

As a result, the average revenue per All Access Pass holder has increased from approximately \$54,000 in fiscal '18 to more than \$83,000 at the end of fiscal '23.

As significant as this growth has been approximately 3 years ago, in an effort to see how high up might be in terms of client impact and therefore, in client expansion and penetration, we organized an increased number of client-facing resources around a subset of our client partners in North America to create client Impact Pods.

These pods included providing client partners involved in this test with access to one or more implementation strategists, the services of client success specialists and the ability to access Franklin Covey's deep bench of delivery consultants to help in the implementation of client solutions.

Under the direction of the client partner, this Impact Pods sole focus has been to help clients achieve such great results that we would earn the right to expand our solutions even further throughout the client organization and create clients for life.

This group of client partners who directed the activities of these Impact Pods were set up to have the same number of potential accounts assigned to them, as did the traditional client partner group of similarly experienced client partners.

They also had essentially the same number of All Access Pass-holding clients as to the traditional group. And so, therefore, what have the results been. While both the Impact Pod Group and the Traditional Client Partner Group achieved very strong results. By comparison, the results of the Impact Pod Group have been truly extraordinary along several key dimensions. I'll outline 4 of them here.

First, as shown on Slide 7, the size of the average All Access Pass subscription contract, where the client partners and the Impact Pods average All Access Pass size grew to \$80,000, whereas the Traditional Client Partner Groups average All Access Pass size grew to \$45,000.

Second is the subscription services attach rate. Both the Impact Pod and the Traditional Client Partner Groups achieved significant growth in their services attach rate. However, the Impact Pods subscription services attach rate, now represents more than 67% of the amount of their All Access Pass subscription itself compared to a services attach rate of 50% for the Traditional Client Partner Group.

Third, the combined subscription and subscription services revenue per All Access Pass holder, so the sum of those first two metrics, where the Impact Pod now achieves an average of \$132,000 per All Access Pass client compared to an average of \$63,000 per All Access Pass client for the traditional group.

And fourth, the logo retention rate. While the All Access Pass logo retention rate is very high overall, the Impact Pods annual logo retention averages are more than 500 basis points higher than the traditional client partner group.

As a result of the combined impacts of this focus, our top-performing client partners who used to average approximately \$1.5 million in annual revenue, now average between \$2.5 million and \$3 million, with several generating more than \$3 million each year. This compares to average revenue for all client parts of approximately \$900,000.

Importantly, as significant as the penetration and increases in revenue have been for the client Impact Pod Group, each still has tremendous opportunities for growth. We're still only penetrated 10% to 15% of the way into these clients' total populations and potential.

Project penetration's potential impact on accelerating revenue growth is quite significant. For example, if its full implementation resulted in the average client partner generating even an extra \$300,000 per client partner or 20% of the increase achieved by the Impact Pod Group, this would ultimately add nearly \$40 million of incremental revenue compared to the normal client partner ramp.

And, in as much as the Impact Pod is simply a resource pool, which can be accessed by a number of client partners. And since we already hired and trained a significant number of client-facing team members to populate additional pods, so we'd be in a position to expand the rollout of project penetration in the coming quarters.

As noted several earnings calls over the past year, the incremental flow-through of this increased revenue to adjusted EBITDA and cash flow is expected to be high. So, we're excited about project penetration.

The second of these targeted growth acceleration opportunities, as shown on Slide 8, is what I'll refer to as project speed-to-ramp. New client partners primarily focus on winning new clients or new logos and then retaining and expanding our business with them.

The focus of project speed-to-ramp is in the name. Its focus is to significantly increase the number of new client logos, which ramping client partners add each year. This will accelerate the ramp trajectory and increase the number of clients with whom we can then continue to penetrate and continue to grow over many years.

For context, in addition to increasing our penetration of existing subscription clients, another of our key strengths over many years has been our ability to hire, train and ramp up new client partners.

We've generally counted on these client partners to prospect and generate their own business from a list of accounts provided to them, and we've established a strong infrastructure to support them in doing this, including things like to recruit new client partners, we've built a strong team that uses all of the latest recruiting tools, has a strong social media presence and a rigorous interviewing process to ensure that new recruits meet our established profile of a successful client partner.

Once recruited, these client partners are assigned a list of named accounts and are responsible for penetrating that list and winning new clients.

Our efforts to support these new client partners as they ramp up include having them go through an extended live and live online sales school, providing sales mentorship with lots of sales presentation aids, holding many hundreds of live and live online thought leadership

events to which they can invite potential and prospective clients and assigning them to a managing director who works with them weekly, going on sales calls with them and who has them go on calls with more experienced client partners and does many other things to support them in their development.

This process, which we continue to regularly refine, has been quite effective.

As a result, our number of client partners has grown significantly and their ramp-up has driven significant sales growth across the world. Over the years, while primarily relying on client partners to generate their own new business from a list of qualified accounts provided to them, we've also tested and work to establish various ways to further accelerate the speed at which they ramp up, while at the same time, continuing to increase the revenue growth rate for already ramped client partners.

The focus of what we're calling project speed to ramp is to further accelerate client partners speed to ramp by focusing on both sides of the math of acquiring new clients.

The first site is to significantly increase the percentage of a client partner's time that is spent making sales presentations versus the time spent prospecting. This will involve implementing a significantly expanded lead generation effort, which we've been testing, including both inside and outside lead generation activities.

And second, at the same time, increasing the percentage of sales presentations that are successful in acquiring a new client. This will involve having a much higher percent of the ramping client partner sales presentations be done in partnership with somebody who's more experience, a sales coach or a partner.

We've tested these 2 efforts in a variety of circumstances and are really excited about the results and the potential project speed to ramp has to both accelerate ramp time for new client partners and increase their total revenue once ramped.

As we add more than 100 net new client partners in the coming years, this powerful combination of faster ramp and higher trajectory could add tens of millions of dollars of incremental profitable growth.

Importantly, because of the investments already being made and relatively modest incremental investments required to implement projects penetration and speed to ramp and the high gross margins generated on incremental sales, we can make the required incremental investments to accelerate revenue growth and still maintain our position as a high EBITDA, high cash flow growth company.

As part of the implementation of project penetration and project speed-to-ramp, we've recently completed an evaluation of the size and deployment configuration of our approximately 290 client partners and our more than 150 additional client-facing field teams of business developers, implementation strategists and leader in the coaches.

Through this evaluation, we determined 2 things. First, that we should place a few additional resources in roles to focus on business development and account penetration. And second, that we had approximately 8% of our client partners or 24 in total, who didn't fit within our planned future field deployment structure.

As a result, we made the difficult decision to separate from these client partners. This is temporarily reducing our number of client partners from approximately 290 to approximately 265. This refinement of our client partner force is similar in nature and scope to the refinement we made in 2016 when we move to a subscription model, and the cost is reflected in the restructuring charge on the income statement.

We expect to begin aggressively hiring new client partners in fiscal '25 and beyond, as well as continue adding to our important client-facing field roles, as we fully implement project penetration and project speed-to-ramp.

The third growth accelerator idea or a project that we're working on that I'd like to talk about here is what we're calling project impact, as you can see on Slide 9. The substance of this third key growth opportunity is our ongoing investment in developing high-impact solutions

to drive collective action at scale.

As you know, we partner with organizations to address their most important people-related challenges, data of developing leaders at all levels, building winning cultures and creating a system of execution to achieve breakthrough results.

We achieved these goals with our clients by flexibly delivering world-class solutions that seamlessly generate behavior change at scale. The solutions we implement do not simply create individual performance improvements or pockets of excellence. We work systematically to transform performance across an organization.

To that end, I'd like to provide a few product updates and the results of those product updates. In order to help our partner organizations achieve breakthrough results, we develop principal centric industry-leading solutions and technologies that allow for seamless, flexible, scalable, impactful deployments. Over the past 2 years, we've significantly expanded the scope of our efforts.

And as shown on Slide 10, in the last 6 months alone, we completed and launched leading and working at the speed of trust. This substantial update and refinement to our industry-leading winning culture solution, both modernize the solution, so it's increasingly relevant and applicable for contemporary work cultures and by launching a scalable working at the Speed of Trust companion solution, extended the impact to individual contributor audiences.

3 months post launch, leading at the Speed of Trust has earned a Net Promoter Score of a remarkable 78, representing a 34% increase compared to our previous world renowned solution, making them among our highest performing solutions to date.

And importantly, through our investments in technology, including the impact platform, working at the Speed of Trust has been assigned on demand to more than 10x as many learners as the previous solution.

The second product-related update is that, we launched an important and hard hitting new communications offering entitled navigating difficult conversations. We launched this in February. It's an extremely engaging solution that helps individuals and teams adopt the paradigms and gain the skills necessary to have the kinds of high-impact conversations that can move relationships and teams forward.

And it does so in an action-pack 2-hour session that meets the time demands of modern workers, while maintaining Franklin Covey's principal centric inside out world-class quality differentiation. This solution has garnered more client interest than any new solution launch in the last three years.

And within 1 month of launch, has already been adopted by clients twice as much as any other skill specific solution we've launched.

Third, we launched a top-level solution selling offering entitled Helping Clients Succeed Strikingly Different Selling. This leverages the intellectual property we've had in our traditional helping clients succeed sales offerings.

We launched this in January. The solution was designed leveraging the latest science of learning research and with the Impact Platform in mind, utilizing unique blend of asynchronous and synchronous experiences that will drive improved measurable selling outcomes for business-to-business sales. Early client reactions are overwhelmingly positive.

Our impact platform has now become an industry-leading technology solution. The impact platform, our proprietary learning platform where clients can easily launch, manage and measure compelling behavior change experiences has evolved into an industry-leading technology solution.

In the past 6 months, we've launched the impact platform in over 20 languages, built a robust diagnostic experience to measure behavior change over time, built one-of-a-kind functionality for clients to launch their own client facilitated courses and integrated with popular LMSs and LXPs.

Over 80% of our clients are now upgraded to the Impact platform and clients who have upgraded assigned 4x as much content to their

employee populations and participants now complete 10x as much content as those on the legacy All Access Pass portal. We expect to upgrade 100% of our clients by January 2025.

Just a couple of notes about upcoming product developments. An updated 7 Habits Solution will be launching in the fall of '24. 7 Habits, our flagship solution for individual effectiveness is undergoing its most substantial revamp in a decade.

The solution is being reimagined to engage modern workers globally. We've completed the most extensive development and beta testing we've done for any solution to date, and we're receiving great reviews in the early pilots and beta testing, and we're eager to unveil the solution this fall.

And finally, our clients are expressing delight at the increasing access, engagement and enjoyment and the impact of the learner experience we've been working on. This spring, summer and fall, we're excited to unveil substantial improvements to our industry-leading impact platform.

We'll launch our first ever native mobile apps, learner and facilitator certificates to incentivize completion and awareness, a powerful AI coach and enhancement to the admin experience will make it even easier to launch, manage and measure behavior change at scale.

Stepping back, I'm very pleased about these 3 key projects, Project Penetrate, Project Speed to Ramp and Project Impact, and we have high expectations that they'll drive increased growth in the coming quarters and years and would now like to turn some time to Steve to talk about some of our results in the quarter more specifically.

Stephen D. Young *Franklin Covey Co. - CFO & Corporate Secretary*

Thank you very much, Paul. Good afternoon, everyone. It's a pleasure to be with you today. I'd like to briefly provide more detail on the factors underlying our performance, focusing on the overall company results for the quarter and then on the results in 3 key areas of our company, specifically, our enterprise business in North America, our enterprise business internationally and our education business.

Since I'm focusing just on these 3 areas, I'd like to point out to everyone as you probably already know, that in our slide deck appendix, we include the current balance sheets, income statements and other financial information will allow you to see our complete results for the quarter and year-to-date.

So, for the company. As shown on Slide 11, second quarter sales were \$61.3 million, which as we expected, was roughly even with the record \$61.8 million we achieved in the second quarter of last year.

Year-to-date sales were \$130 million compared to \$131 million in the prior year. And for the latest 12 months, sales were \$279 million compared to \$276 million in the prior year. These results are essentially even with the record levels achieved last year with year-to-date sales down about 1% and the latest 12-month sales up about 1%.

Second quarter adjusted EBITDA was \$7.4 million this year compared to \$8.2 million last year. Year-to-date adjusted EBITDA was \$18.4 million compared to \$19.7 million in the prior year and the latest 12 months adjusted EBITDA was about \$47 million compared to about \$44 million in the prior year.

Now, as shown on Slide 12, results in our enterprise business in North America continued to be strong in the second quarter in the latest 12 months. Sales in North America, which accounts for about 73% of total Enterprise Division sales was \$34.1 million in the second quarter, \$72.5 million year-to-date and \$150 million in the latest 12 months.

Revenue achieved in this period, as you can see, is essentially even with prior years, which were themselves up 8% in the quarter, 12% year-to-date and 15% for the latest 12 months. So, even compared to last year, but last year was up seemingly compared to the prior year.

Subscription sales in North America were \$22 million, growing 5% in the quarter or \$44.5 million year-to-date, which is up 6% and \$87.8 million latest 12 months, which is also up 6%.

The combination of subscription and subscription services sales in North America was \$31.5 million in the second quarter, representing 4% growth on top of the 7% achieved in last year's second quarter. These sales were \$66.3 million year-to-date, which is up 2%, and they are \$136.4 million in the latest 12 months, which is up 4%.

Our balance of deferred subscription revenue billed and unbilled in North America continued to be strong, growing to \$117 million in the quarter, which is up 3% on top of the 22% growth achieved in last year's second quarter, establishing, as Paul talked about the strong foundation for next year's growth.

The percent of North America's All Access Pass' for multiyear periods increased to 56% from 50% last year, and the percentage of invoice sales represented by multiyear contracts increased to 62% from 57% last year.

Now, as shown on Slide 13, revenue from our international operations, which accounts for approximately 17% of our total Enterprise Division revenue was \$7.2 million in the second quarter, which is even with last year and was \$16 million year-to-date, which is down about 4% and \$34.5 million in the latest 12 months, which is up about 5%.

As also shown on Slide 13, our international licensee partner sales were \$2.7 million in the second quarter, a decrease of 6%. There were \$6.1 million year-to-date, which is even with last year and \$11.6 million in the latest 12 months, which is up 3%.

So, if you kind of cut through all of these numbers, you can see that in the Enterprise division, our subscription business is generally up, while our other revenue is generally down, making the overall result essentially flat. The fact that it's our subscription business that's up, like Paul talked about encourages us as we look forward to future quarters and years.

Finally, as shown on Slide 14, sales in our education business, which generally accounts for about 25% of total company sales, grew to \$14.6 million in the second quarter, up 3% on top of the 28% growth achieved in the second quarter of FY '23.

Year-to-date sales grew to \$29.3 million, up 3%, and sales for the latest 12-month period were \$70.5 million, up 4% on top of the 22% growth in the previous year.

Education subscription and subscription services sales grew to \$12.9 million in the second quarter, up 4% on top of the 30% growth in last year's second quarter. Year-to-date, sales grew to \$26.1 million, up 2% on top of the 27% in year-to-date growth achieved in last year's second quarter.

And the latest 12 months education sales were \$65.2 million, which is up 4% on top of the 23% growth achieved in the same latest 12-month period last year. Education's balance of deferred subscription revenue billed and unbilled, increased by \$10 million to \$30 million versus last year's balance.

As you recall, not many years ago, the education business was small and had a traditional services and materials business model. We are pleased that since the launch of the Leader in Me subscription in the Education Division, revenue has grown substantially from just over \$3 million in the first year to more than \$70 million in the latest 12 months and education's business model has transformed to closely mirror that of enterprise with approximately 90% of Education's revenue, now represented by subscription, subscription services revenue.

We also expect that after years of accelerated investment, the Education Division's adjusted EBITDA margins will also expand this year and beyond.

Now, cash flows and the balance sheet. As shown on Slide 15, our year-to-date cash flows from operating activities was \$30 million this year versus \$11 million last year.

Our free cash flow for the first 2 quarters increased to \$24.7 million compared with \$3.3 million for the prior year, reflecting the changes in the elements of working capital were very favorable in the first and second quarters of this year, compared with last year, particularly

reflecting changes in accounts receivable, accounts payable and accrued liabilities and deferred revenue.

In Q1 and Q2, we invested \$18.4 million to purchase 461,000 shares. And over the past 4 quarters, we've invested more than \$49 million to purchase shares. We ended the quarter with over \$103 million in total liquidity, including \$40.9 million in cash and \$62.5 million available under the revolving credit facility, even after investing the \$18.4 million to repurchase stock.

Compared to Q2 of FY '23, the sum of billed and unbilled deferred subscription revenue increased 9% to \$158.5 million, giving us a substantial and increased visibility into future sales results.

The deferred subscription revenue increased 13% to \$86 million, while the unbilled deferred revenue increased 4% to \$73 million. We continue to report a very strong balance sheet.

Now, guidance. In our first quarter earnings call, we communicated that we expected revenue in the back half of this fiscal year to be higher than in the first half and that we expected to finish the year with adjusted EBITDA at the bottom of our range of between \$54.5 million and \$58 million in constant currency.

While we expect our back half revenue growth to exceed that which we achieved in the first 6 months, we expect the absolute amount of that growth to be lower than the low double-digit growth that we had expected for the back half.

This is in large part due to the fact that though our expected rebound in services is occurring, it began a bit later than we had anticipated. As a result, we now expect total sales for the year to be lower than previously expected, with growth of approximately 1% in the third quarter, increasing to approximately 6% in the fourth quarter.

Despite this lower revenue, we still expect adjusted EBITDA to come in at the bottom end of our previously announced guidance range of \$54.5 million to \$58 million in constant currency. This result reflects, one, expected high flow-through of incremental revenue to adjusted EBITDA, driven primarily by our high gross margin and declining SG&A as a percentage of sales.

Two, the restructuring event that Paul talked about; and three, the fact that a significant portion of our compensation throughout the company is tied to growth in sales and overall financial performance.

For Q3, we expect net sales to grow approximately 1%, as I said to approximately \$72 million and adjusted EBITDA to be between \$12 million and \$13 million, reflecting a midpoint increase of approximately \$600,000 over the prior year.

Our back half projections are consistent with our current expectation that add-on sales will continue to strengthen, as we've talked about, and that our education division will have a very strong Q3 and Q4.

So, I'd now like to turn the time back to Paul.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Steve, thanks so much for that. Thanks for going through the quarter. And why don't we now invite Lisa to open the call up to the questions that she does that. I'll just say, we feel very good about the building momentum we're seeing in the business and are looking forward to a good back half and a good fiscal '25.

So Lisa, let's take some questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will be coming from Dave Storms of Stonegate.

David Joseph Storms Stonegate Capital Markets, Inc., Research Division - Director of Research

Just want to kind of start around the slower-than-expected rebound. It sounds like that's just a timing issue. Can we kind of expect that to hopefully restart back in the early parts of 2025? Or is there anything that you would expect to maybe bring that back into play for the second half of this year?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes. Are you referring specifically to the services rebound?

David Joseph Storms Stonegate Capital Markets, Inc., Research Division - Director of Research

Yes.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes. Okay. Great. Yes, the leading indicators and the services booking pace suggests that the rebound has begun, and it is a quarter or so slower than we thought it was going to be. So, we're beginning to see the rebound.

We expect that rebound will accelerate through the back half of the year, and we'll certainly be as part of what's driving growth in the back half of this year overall versus being flattish in the first half of the year, and then we expect that to continue.

And as I mentioned, what that looks like is having reached a high watermark of 60%, at least a high watermark for now, 60% service attach rate, it's regressing back to what was already a higher rate of about 55%. We expect that it will stay there and we'll try to improve that over time.

David Joseph Storms Stonegate Capital Markets, Inc., Research Division - Director of Research

And then just, it sounds like you had a really strong quarter for logo retention. Any thoughts around that going forward? It sounds like, there might be less belt-tightening going on among clients. Is that expected to kind of be the trend going forward?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes. Great question. So, we were pleased with the logo retention in the quarter. As I mentioned, it was one of our best quarters we've had in logo retention. And I think there's a couple of things driving that.

One is, and as I mentioned a few minutes ago, I don't know that I understood the degree as we were in the fall this year, executing the degree to which clients were pausing, thinking about their budgets, maybe creating new budgets, pulling back a little bit on their budgets at the same time that interest rates were spiking were kind of moving out of the zero interest rate world.

And I think that had created some headwinds for us in the first part of this year. I think now clients have their budgets. They know what those budgets look like. There's still some uncertainty out there, but more certain, I think now in the economy that I think will shift from a headwind to not a tailwind at least less wind.

And then I think the second thing, though, that's driving that logo retention rate is that we've learned a lot over 8 years that we've been a subscription company. We converted the subscription 8 years ago.

We've never been a subscription business before, didn't even have a post-sale motion and so, over time, we've created and we've talked the last year or so about these field-facing teams of implementation strategists that come alongside client partners, and we continue to refine those processes as we mature and understand what does it look like to support our clients post sale.

I think we're also getting better execution. Our processes are getting better, and we're getting better execution on those processes as well. And as I mentioned, this project penetration, the real goal of project penetration is actually to increase the retention of clients, both logo and revenue, and we're starting to see the fruits of that as well, which is why we're excited to begin to extend that more broadly in the company.

Operator

And our next question will be coming from Jeff Martin of ROTH.

Jeffrey Michael Martin ROTH MKM Partners, LLC, Research Division - Co-Director of Research & Senior Research Analyst

So, Paul, could you touch on the client partner changes? I mean you ended Q1 at about 300 client partners. The goal is to add 40 net new this year. It looks like we took a step back down to 265. Maybe touch on what the plan is for this year? And did I hear correctly, you're taking a pause at hiring and open partners until next year?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes, you heard that correctly. So, what's underlying that is, so, as we've been working on, as I mentioned, Project Penetration, Project Speed to Ramp, part of that, as we built this more than 400 person, 430-or-so person field-facing organization.

We're focused right now on understanding exactly how to configure those groups. And we feel like we have a really good configuration map. Historically, we've gone to market without a lot of segmentation. We haven't segmented historically around client size or around verticals, as we look into the future, we see an opportunity to increase the level of segmentation of that field force.

And so, while we want to put the right amount of resources into business development to help gin up more opportunities for our salespeople, also have that sales force configured against the biggest opportunities on the map. And I think there's a natural segmentation that occurs around large enterprise organizations versus mid-market.

And then the team that supports post-sales implementation strategies, we're getting more strategic and more refined in how we want to deploy. And so, in that set of discussions and strategic planning, we recognized there were about 24, well, there were 24 that didn't fit within the structure we're going to build towards.

And so, we're pausing just briefly here to then come out and accelerate with more hiring into an even more strategic segmented approach, both presales, sales and post sales, but also in how we divide up the market.

I'm actually quite encouraged about this. I think this is the next big step for us as a sales organization, and I think it will unlock a tremendous amount of growth, because we see so much potential in the existing accounts we already have. And then, of course, there's a significant amount of white space out in the market that we're not even touching today.

And so, this segmentation of these 2 Project Penetration and Project Speed to Ramp are really about getting at that in a much bigger way than we even have in the past. So, we'll be going back on the hiring in fiscal '25, Jeff. And, I'm sure we'll add a few, I'm sure, in the back half of this year as we move forward, but the bulk of the hiring will be in fiscal '25.

Jeffrey Michael Martin ROTH MKM Partners, LLC, Research Division - Co-Director of Research & Senior Research Analyst

That's a natural segue. And then my other question here is the executable opportunities that you went into quite a bit of detail on where are you in terms of implementation of those? When do you expect to see traction in those efforts? And when should we expect a material reacceleration of revenue growth?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Great question. A couple of thoughts. One, we're in the middle of implementing that wide scale now, and that will be the effort over the back half of this year. So, we'll be fully configured September 1 as we start the new year or at least moving people into that configuration between now and then.

Second, as far as the acceleration of revenue growth, we're already pleased. I mean, the reason we have the confidence to step into those projects is we've been executing against those in kind of a test way over the past couple of quarters, and we're encouraged by the results.

So, we're already seeing the results show up. That gives us the confidence that a step across and really do this at a bigger scale.

As far as its ability to accelerate revenue growth, as I mentioned, there's 2 things that are happening that are accelerating revenue growth. Even if we didn't make the step across and fully execute Project Penetration and Project Speed to Ramp, we're seeing natural acceleration in revenue growth, as I mentioned, because our subscription business is growing faster right now than the overall company is growing, and that's going to pull with it increases in reported growth as we go into next year.

That fact plus what I think is going to be impact as we go into next fiscal year and throughout next fiscal year of these 2 key growth initiatives, I think, will all point towards more accelerated growth in the coming quarters and years.

Operator

Our next question will be coming from Samir Patel of Askeladden Capital.

Samir Patel Askeladden Capital Management LLC - Founder & Portfolio Manager

Congratulations for executing so well in a tough environment. I'd like to start with a comment. So, I followed you guys for almost a decade, and I've been a continuous shareholder for 8 years now.

The biggest pushback I always got from other investors is, FC is cyclical. They'll be killed in a recession. So, when I look at consulting companies, professional services companies today, many of them are actually seeing double-digit organic declines over the past few quarters.

So, the fact that your subscription invoices are growing in this type of environment, you're throwing off prodigious free cash flow, I think that really demonstrates the power of your business model and suggest that your stock should be trading at a much higher multiple. And I think if the market is too shortsighted to see it, you guys should take advantage of it and consider doing a tender.

So, that's my comment. I don't know if you have any observations there before I get to my question.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Thanks for your comment. Of course, I want to grow faster, and we will. But I will say, as we mentioned, we are pleased with the fact that we are growing in a tougher environment. And so, I want to thank all the people on our teams around the world for the great work they're doing and our ambition is to do even more.

Samir Patel Askeladden Capital Management LLC - Founder & Portfolio Manager

So, my question is sort of related. You talked a couple of quarters ago about the potential for M&A. And it seems like in this environment, you might have competitors that are over reliant on a single type of content, single modality that don't have your subscription model that might be facing a tough time, but have great customers or content set that might be additive to yours. Do you think you're any closer to being able to close on 1 or 2 of those types of opportunities?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes, it's a great question, Samir. So, maybe just let me -- we were spending a fair bit of time thinking about how to utilize our excess cash and what role M&A might play in our utilization of that cash.

So, the short answer to your question is I think that it's likely that M&A will play a bigger role in the future than it has in the past. And I think we have some opportunities there. We've been a little bit careful over the past year or 1.5 years or so because many of the companies in our space fared far worse than we did in the pandemic and coming out of the pandemic for a couple of years there, started to put up pretty significant growth numbers on a percentage basis, but that growth was just getting them back to their pre-pandemic highs, not above.

At the same time, we were also hit a little bit in the first couple of quarters, but our business did quite well during the pandemic and then has grown substantially over our pre-pandemic highs.

And recognizing that companies you might want to look at acquiring out there, they'd like to sell based on the growth rate they've

achieved getting back to where they were, we wouldn't want to probably pay based on that.

And so, we've been just kind of watching and waiting and we're starting to see what you alluded to in your opening comment there that those growth rates are kind of coming back down to where we thought they might. And so, I think there are opportunities as we talk as a team here, and we're investigating those and looking at those as you would imagine.

Samir Patel Askeladden Capital Management LLC - Founder & Portfolio Manager

And then on the other uses of cash, I mean any reason it slowed down in the quarter? I mean kind of the outlook for -- sorry, when I say use of cash, I mean, on repurchases and the outlook for that? I mean, your stock is down double digits after hours, you have \$40 million in cash.

You implied you're going to have record free cash flow this year, which suggests another \$20 million free cash flow generation in the back half, plus the revolver, I mean, that's a lot of liquidity. So any thoughts on further share repurchases? And like I said, maybe considering a tender or something more aggressive to retire a much larger percentage of the market cap?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Thanks. Steve, do you want to take that?

Stephen D. Young Franklin Covey Co. - CFO & Corporate Secretary

Yes. Samir, nice to be talking with you. So, yes, we see the situation the same as you do, look at this the same as you do. As you know, we generally don't commit to what we're going to do, but we do see it the same as you do.

Operator

Our next question will be coming from Nehal Chokshi of Northland Capital.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

Steve, what at this point in time where currency rates are? Is your expectation on currency headwind on both top line and EBITDA at this point for the full year?

Stephen D. Young Franklin Covey Co. - CFO & Corporate Secretary

The FX impact. So, we've had an impact of just about \$200,000 on revenue and about \$200,000 on adjusted EBITDA so far this year.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

And what is your expectation as far as how much were currency rates right now? How much would that impact for the next 2 quarters from now?

Stephen D. Young Franklin Covey Co. - CFO & Corporate Secretary

Based upon the current rates, we'd have about \$200,000 adjusted EBITDA in Q3 and \$200,000, again in Q4 at the current rates compared to last year.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

Paul, what's the time to deliver the value on the 3 projects that you have discussed?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

The time to deliver value. I think there's actual, so because we're already -- so take each of the 3, starting with the third one I talked about Project Impact. We've been in the middle and are in the middle of that. We have a multiyear road map.

Our product and technology team has been doing a fantastic job delivering against that. So, we're right in the middle, and that will be something we continue to do, and we're seeing the impact of that every day.

The other 2 projects, Project Penetration and Project speed to Ramp, again, as I mentioned, we've already been testing those were ready

to move to more wide scale. We'll do that over the coming couple of quarters. And I think we will see the impact later this year and into next year on both of those projects.

As far as getting them completed and kind of stood up and the configuration changes and all that will happen in the coming couple of quarters.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

And I think you did give some penetration numbers of both the Impact Pod penetration rate, as well as the penetration of the improved selling structure here.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes. So, the penetration rates for the Impact Pod, first of all, there's services attach rate, you didn't ask about that, but the service attach rate is 67% versus 50% for the others. Their average revenue per client is \$132,000 versus \$63,000 and logo retention is about 500 basis points higher.

And as it relates to penetration, the average subscription side is \$80,000 versus \$45,000 for everybody else. So, they're penetrating their clients further is what we're seeing right now.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

I'm sorry, I meant like what percent of your subscription revenue is being addressed with the Impact Pod versus a standard pod? That's what I meant.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

What percent of the overall revenue, about 20% of the overall subscription, subscription services revenue is represented by the test with the Impact Pods.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

And then, as far as the improved selling structure for ramping client partners, what percent of client partners already have this improved selling structure?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes, that's the other kind of end of the continuum I'd say it's about the same. Different set of client partners, but I'd say it's maybe in that group, it's maybe probably 10% or so today, 10% or 15% are benefiting from that, which will roll out to the rest in the coming quarter or 2.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

And, I'm sorry, functionally, was the difference between an Impact Pod and Traditional Pod? I get that you get all these different results, great results, but functionally, what is the difference between an Impact Pod and a Traditional Pod?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Yes. So, the difference is the amount of support provided to that client partner, the infrastructure around them to help them better engage those clients post sale to uncover and lead to expanded subscription and services sales. So, it's more intensity of implementation strategist support and more intensity of consultant support per client partner.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

And can you share the consumption characteristic to the new and refresh pipeline at this point in time?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Explain that the consumption characteristics of the new and refreshed pipeline.

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

I'm sorry, pipeline. Let me rephrase that. I stated it incorrectly. What are the consumption characters for a new and refreshed content pipeline?

Paul S. Walker Franklin Covey Co. - President, CEO & Director

And by consumption characteristics, do you mean by modality?

Nehal Sushil Chokshi Northland Capital Markets, Research Division - MD & Senior Research Analyst

I mean, like number of hours that are being consumed of the new content relative to the last time when they were refreshed.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Okay. I got you. Yes. Sorry for not understanding the question fully. As I mentioned, so just take a couple of examples. So, we launched our new leading at the Speed of Trust and a brand-new companion module we've never had before, which is working at the Speed of Trust as mentioned to scale to individual contributors.

And that's now on our impact platform as well. And in the first 3 months, we've had 10x more usage of the on-demand modules on our impact platform than we had in total from the previous version.

So, significant increase in consumption around that new solution. And we're just in the early, early days of have any difficult conversations, but the client interest has been very, very high, and so we expect to see significant increased consumption of that solution as well.

And then overall, what we hoped would happen and expected would happen when we acquired Strive, and we eventually got all of our content on to Strive, and we created the ability for Strive to integrate into clients, LXPs and LMSs and their technology infrastructure.

We're seeing significant increases in usage across the board of our content by clients, which we believe that's part of what's driving higher logo retention, although also, by the way, back to Dave's earlier question, our solutions are becoming more sticky, because utilization is becoming much higher by clients across the organization.

Operator

Thank you. And that does conclude the Q&A session for today. I would now like to turn the call back over to Paul for closing remarks. Please go ahead.

Paul S. Walker Franklin Covey Co. - President, CEO & Director

Lisa, thanks so much for turning back over. Thanks, everyone, for joining us today. I really appreciate your questions, and thanks, as always, for your interest and we appreciate you and hope you have a great rest of your day and week.

Operator

Thank you all for joining today's conference call. This does conclude today's meeting. You can have a great evening. Please disconnect.

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