

Transcript of
Calian Group Ltd.
Fourth Quarter 2021 Conference Call
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Participants

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Analysts

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Nick Agostino - Laurentian Bank Securities, Inc.
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Presentation

Operator

Good morning, ladies and gentlemen, and welcome to the Calian Fourth Quarter 2021 Conference Call. At this time, all participants are on a listen-only mode, and the floor will be open for your questions and comments following the presentation.

It is now my pleasure to turn the floor over to your host, Kevin Ford, Chief Executive Officer. Sir, the floor is yours.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thank you, Katherine, and good morning, everyone. With me this morning is Patrick Houston, our CFO. And we'd like to welcome you to Calian's fourth quarter and 2021 full-year results conference call.

Please note, that certain information discussed today is forward-looking and subject to important risks and uncertainties. The results predicted in these statements may be materially different from actual results.

I'm going to start with our fourth quarter results. And the fourth quarter saw revenue of \$128 million, a 4% increase compared to the same period last year. Adjusted EBITDA and adjusted net profit grew year-over-year at 35% and 54%, respectively.

We have continued to see momentum in new contract signings this quarter with \$84 million in new wins, leaving us with a solid backlog of \$1.3 billion. Dividend levels remain unchanged at \$0.28 per share. And as a reminder, this quarter marks our 80th consecutive profitable quarter. That's over 20 years of profitable execution and delivery.

I'm thrilled to share, for the first time in company history, we have passed the \$0.5 billion mark with annual revenues of \$518 million. This is a major milestone for Calian, on our journey to become a \$1 billion innovative global growth company.

COVID-19 has presented many challenges, particularly around maintaining our manufacturing capabilities, traveling to customer sites and supporting customers virtually.

And I'm pleased we were able to achieve this milestone even during a difficult time. Adjusted EBITDA and adjusted net profit increased by 41% and 58% respectively. And at 24%, gross margins are the highest they've ever been. Another point of pride for our team.

Our net cash has grown threefold year-over-year, and EBITDA margins are now above 10%. Our success in fiscal 2021 can't be told through numbers alone. We acquired 3 new companies, bolstering our capabilities in areas such as cybersecurity and high-performance antenna capabilities, allowing us to expand our customer base.

Calian was named to the FP500, a ranking of the top 500 largest Canadian companies by revenue. And we were added to the TSX SmallCap Index. We've continued to add new leaders to help propel the company forward. It's included Michele Bedford, our Chief Commercial Officer; Seann Hamer, our Chief Technology Officer; and Sacha Gera, as President of IT and Cyber Solutions.

We have also made significant contributions to our communities. We are a key partner in Canada's response to COVID-19. We supported indigenous communities with remote healthcare. We continue to deliver our Military Family Doctor Network and assisted over 20 charities. Our efforts to diversify our revenue has shown tremendous progress.

Just a few years ago, almost 70% of our revenue came from government customers at the federal, provincial and municipal levels. While we have continued to grow our government revenue, our efforts to diversify into commercial and international segments have resulted in significant growth. And the revenue split is now 50/50 between traditional government sources and commercial customers.

I'd like to spend a moment sharing an update on each of our segments. If you've been on one of these calls before, you've heard me mention our 4-piston engine, and how growth in one segment balances a potential decline in another.

It is my sincere belief that this 4-segment structure as well as our 4-pillar growth framework of continuous improvement, customer diversification, customer retention and innovation are key ingredients to our success. Three of the 4 segments delivered double-digit revenue growth this quarter.

IT and Cyber's impressive revenue growth of 61% was led by the contribution of the newly acquired Dapasoft and iSecurity companies.

For Advanced technologies, Advanced Technologies is the segment that has been most impacted by COVID-19, with supply-chain challenges and travel restrictions delaying completion of some

projects. And despite this, Advanced Technologies saw increases across the board in revenue, EBITDA and gross margin.

Acquisitive revenue makes up 7% of the total increase, and is attributable to revenue from the acquisitions of InterTronic and Tallysman.

In addition to acquisitive growth, Advanced Technologies has demonstrated growth in ag tech product sales, and continued expansion and growth in European ground system products.

For Health, while revenue decreased 22% this quarter as a result of the onetime deployment of mobile respiratory care units in Q4 2020, revenue grew 20% for the year. Demand for high-quality healthcare services has increased during the pandemic. And Calian has been engaged for a variety of services across Canada, including vaccinations, screening, quarantine support and virtual clinic setup.

As an example, Calian nurses support a 1-800 hotline that offers COVID-19 screening, complete contact tracing, and public health education for Nunavut residents. These are critical services for residents who live in remote areas at a far distance from healthcare services.

For Learning, revenue growth in Learning was strong both in the quarter and the year. The team has embraced both in-person and virtual delivery of this learning platform. And growth in the fourth quarter was 23% when compared to the same quarter last year.

Just after the fiscal year end, we announced the acquisition of SimFront, a leader in immersive training solutions incorporating augmented, virtual and mixed reality technologies. Now, we can offer customers an end-to-end military training and simulation solution with opportunities not just in defense, but in health care and oil and gas.

For IT segment, the IT and Cyber Solutions saw the largest increase in revenue growth with 52% related to acquisitive revenue. This demonstrates that the capabilities and assets from our acquisition of Dapasoft and iSecurity, R&D transforming or IT segment.

Another proof point is the 2021 Microsoft Canada Healthcare Impact Award, presented to Dapasoft for the Corolar Virtual Care solution, a solution that helps acute care providers quickly roll out premium virtual clinic services. All-in-all, we see multiple new growth opportunities across all of our segments, and are excited about the momentum we have created this year.

Now, I'd like to pass it to our CFO, Patrick, to discuss results and key performance indicators.

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Thanks, Kevin. We have several important achievements in the fourth quarter, including increases across the board in revenue, adjusted EBITDA, and adjusted net profit. This performance can be largely attributed to investments we have made in each of our segments to bring technology and differentiated services that resonate with our broad customer base.

Acquisitive growth in the quarter was 8% and 12% for the entire year. The acquisitions we have completed during our fiscal year have all been meaningful contributors. Organic growth in the quarter was negative 4% and 8% for the entire year. Passing the half billion-dollar revenue mark is a major milestone for Calian in growing gross margins and EBITDA margins ahead of revenue speaks to our profitable growth agenda.

Gross margin performance in the quarter was strong reaching 26% compared to 19% in the same quarter a year-ago. Improvements in EBITDA of 35% and adjusted net income of 54% significantly outpace our revenue growth in Q4.

Our balance sheet remains a strength. We ended the quarter at \$78 million in cash and credit facility of \$120 million, which is still undrawn. We completed 3 acquisitions, during FY 2021 and have already successfully closed 1 acquisition in FY 2022. We continue to invest in our team to facilitate further investments in M&A and our pipeline of deals is as busy as ever.

I'll turn the call back over to Kevin.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thank you, Patrick. I can't overstate how pleased I am with how far Calian has come. And I hope this demonstrates why? In only 4 years, we have nearly doubled our annual revenue, more than doubled EBITDA and achieved record high margin levels. This has been the result of how we go to market, the assets and technologies we own, and the geographical expansion we have accomplished. And, I believe, this is just the beginning of our journey. These results have reinforced our strategy to invest in our existing assets and technologies to accelerate organic growth in the long-term.

We've talked quite a bit about how our recent acquisitions have contributed to revenue growth. We spent \$70 million on M&A this year, the most in company history to acquire technology assets that strategically bolster our capabilities in different areas like cybersecurity, and immersive training solutions. We've never had more technology assets than we have right now, and will continue to grow this portfolio through M&A and continued organic investments.

On guidance, I must caution the revenues realized or ultimately dependent on the extent and timing of future contract awards, customer realization of existing contract vehicles and any impacts due to COVID-19 and specifically government regulations related to social distancing, stay at home orders, and broader global travel restrictions.

Based on currently available information of contract backlog, sales opportunities and our assessment of the marketplace, we expect to continue our growth posture in the coming year. Our guidance does not incorporate any additional M&A activity. Should we close on any new opportunities, their contributions would be incremental.

With that backdrop, our guidance for the fiscal year ended September 30, 2022, we expect revenues in the range of Canadian \$550 million to \$590 million, adjusted EBITDA in the range of \$57 million to \$61 million, and adjusted net income in the range of \$39.25 million to \$42.75 million. And please see our press release and MD&A for detailed reconciliation of our guidance.

As mentioned, this guidance indicates that FY 2022 will be another record year with potential for double-digit growth in revenue and EBITDA. This guidance includes several millions in new investments in our health, cyber and communication assets to create long-term value.

So, why should investors have confidence in Calian? We've been in business for 39 years, having just celebrated 80 consecutive profitable quarters. Our balance sheet is strong. And our strategy of diversity, profitable growth, and both organic and M&A growth is delivering results.

I don't believe our stock price properly reflects our recent performance and our upward trajectory. As CEO, I'm confident that we have the team, the assets and the strategy to deliver long-term profitable growth.

And finally, I want to thank our staff for once again, achieving not only record results, but for being there for our customers. What has been demonstrated through the COVID is our services and solutions are essential to our customers across all of our segments. And I'm extremely proud of our team for rising to the challenge yet once again.

With that, Katherine, I'd like to now open the call to questions.

Operator

Ladies and gentlemen, the floor is now open for questions. [Operator Instructions] Your first question is coming from Amr Ezzat. Your line is live.

Q: Good morning. It's Michael Vaccarino on behalf of Amr. Congratulations on the strong quarter.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thanks, Michael.

Q: Hi. You are sitting on a record cash position with no debt. I appreciate that these things are hard to time. But going into 2022, can you give us a sense of how much capital you're looking to deploy into M&A? And then, can you speak to which areas you're seeing opportunities in?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Hi, Michael. Thanks for the question. So, yeah, we've been busy on M&A in the last couple of years. We've completed on average here 4 M&A deals per year. We've done 1 so far this year. I'd say our pipeline is quite full in terms of new opportunities coming to us. And right now, we're busy trying to assess which ones that make sense to us and execute those. It's hard to give you an exact number of how much capital we deploy, but we're certainly looking to continue the same momentum we've done here in the last couple of years and complete multiple transactions.

The timing will just depend on as those come into focus and we get them done to our satisfaction.

Q: All right, thank you. And then, on the Health segment, I understand the year-on-year decline with the MRCU last year. But I'm looking to get more color on the quarter-to-quarter movement from Q3. How much of the decline is COVID-related work that isn't there anymore?

And then, when thinking about your reported \$44 million in revenues for the quarter, is that a good plateau to build growth on top of or is there still some COVID-related work that will taper off?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah, the COVID-related work, specific response kind of in our healthcare group this year was about \$30 million for the year. That started to taper off, obviously, in Q4. Our expectation right now and in our guidance, we're expecting that there might be a slight amount, a bit left in Q1, but not beyond that. But, of course, the environment is changing pretty rapidly. So if that came back on, certainly, the team is ready to respond to that. That would be incremental to where we're at. But I think that's our understanding of the environment.

Q: Okay. And on IT services, very impressive gross margin performance again. In your MD&A, you mentioned that this is on the Dapasoft acquisition. Is there anything unusual in the quarter that helped contribute to the margin expansion or is that the new normal?

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Yeah. Great question. It's Kevin. I think from my viewpoint, that's the new normal from our viewpoint. Dapasoft and iSecurity coming out of the block very strong, both in the cloud migration, our healthcare platforms and cyber. And it's exactly the type of assets and companies and staff and talent that we want to acquire for not only the capabilities we can bring to customers, but the impact to our margins, to your point. So we're not expecting that to be a blip. We're expecting that to be more of a longer-term trend and trajectory now for IT business.

Q: Okay, great. That's all from me. Thanks. I'll pass the line.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thank you so much for the questions.

Operator

Your next question is coming from Benoit Poirier. Your line is live.

Q: Yes. Good morning, Kevin. Good morning, Patrick. And congrats again. First question, if we look at Advanced Tech, what was the contribution from the large satellite ground system contract in Q4? And how should we be thinking about Q1, if there is anything to be done?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah, with sub-\$10 million this quarter, Benoit, and we've got probably about \$6 million last year, this year to recognize and finish the project. We're right in the last stages here. So even that project has ramped down as we expected, as we completed it. And the team's won some new ones in Europe and those have been ramping up. So I think from Advanced Tech, strong quarter across those deliveries of the new projects, plus some incremental product sales. So it's good to see a strong performance from AT this quarter.

Q: Okay. And what should we expect once this contract is finished from a working capital standpoint? And maybe should we expect profitability for Advanced Tech to be back and toward more normal range for fiscal year 2022?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah. So, for working capital, we had some good progress this quarter. We brought back in about \$20 million of that. So you saw that appear in the cash and with balance come down. We're expecting kind of similar contribution probably in Q1 and Q2, as that kind of ramps down and gets to completion. And, in profitability, yeah, I think, this is the first step back to kind of more historical levels for AT this quarter, and then, you'll probably see some incremental improvements next year.

Q: Okay. That's great. And, could you talk about the timing to start the other large one worth \$33 million that was awarded in February 2020? I thought it was expected to start early in 2022, and if you could talk about the pipeline to replace those large satellite ground system? I would be curious to get more color on the pipeline, unfortunately, especially for Advanced Tech.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Yeah, thanks very much. This is Kevin. Yeah, the large project which has been ramping up, primarily in Q4, and will definitely continue into our new year. So we'll have a positive impact to our 2022 AT trajectory. I think the exciting part I'm seeing at Advanced Tech right now, if you think about our antenna line and with the acquisition of Tallysman, SatService, InterTronic. If you had a menu in front of you with all the different antennas required for our communications, right now, we have a much deeper solution set than we've ever had.

If you think about that announcement on the electronic vehicle manufacturer that we've sold the Tallysman antennas [which gives] [ph] global navigation support. You think about the full motion antenna capability to InterTronics, you think about our presence in SaaS service in Germany now. The pipeline is actually probably the strongest it's been in our Advanced Tech business for both large aperture tenders and also the GNSS antenna.

So, we're expecting AT to continue on a solid trajectory, and very excited by the opportunity, not just because of the number of them, but the size and scope of some of these are actually quite significant. So we just got to do our thing, keep our head to the ground, and then win our share. But, I think, you'll see some good progress on the NASDAQ this year just by the nature of the investment we've made in our antenna line.

Q: Okay, that's great, Kevin. And, Pat, could you maybe share some thoughts about CapEx, R&D and free cash flow for fiscal year 2022? How should we be thinking?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah, CapEx is up a bit this year, we obviously had the one-time investment in our ERP platform that projects scheduled to be done in February. So, I think, you'll see CapEx come down a bit next year, back to kind of more normalized levels, in that \$3 million, \$4 million normalized level. And then, the dividend we've been holding right now there'll be about for next year at the current shares outstanding about \$12.5 million to \$13 million. So, I think, those are clear, and then it's really how

much we can generate. And, obviously, we're growing again from an EBITDA perspective. Our guidance indicates plus 10% growth again there. So you should see free cash flow increased pretty significantly compared to this year.

Q: Okay. And from a dividend standpoint, how should we be looking at the payout right now, and the timing to consider a potential increase down the road?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah, we communicate to investors that our objective was to get the payout from a free cash flow perspective down into the 30%. So, I think, as of Q4, we've kind of gotten to that level. So our objective in the last couple of years has been to grow that that cash flow and bring the dividend back in line with where it should be. So, I think, as we go into next year, and we see incremental growth, I think we'll start to look at whether we should adjust it. But, I think, certainly the plan over the last few years has worked in terms of bring it in line with where we want it to be.

Q: That's great color. Thank you very much for the time.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thanks, Benoit.

Operator

Your next question is coming from Nick Agostino. Your line is live.

Q: Yes, good morning. If I just go back to the fiscal 2022 guidance. I think, in your MD&A, you highlight a shortage of trained staff has been – I guess, part of the variables that you considered in putting together the guidance. Can you maybe talk a little bit to what areas where you're seeing that that shortage, learning, health or whatever the case is? And maybe what steps you're taking to rectify that? And when you think you can have that that shortage fully rectified?

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Yeah. So from our viewpoint, I think, like all companies right now, not just Calian, you hear with my colleagues at the organizations and CEOs and C levels, the war on talent. And what we've seen in a virtual world, Nick, is that the ability to work virtually, is giving everyone opportunities, frankly, to work from home, for wherever they want to work, whether it's in Canada or around the world.

What we see primarily the demand really for us is in 2 pockets. I think, we're seeing on health care practitioners, and then software and software engineers. We've never been busy in our software engineering group, right now, we continue to grow. And you think about Calian now, we have software capability in all of our segments. We've moved from strictly services in some areas now to have technology asset. So we continue to look at methods and mechanisms to retain and attract talents both in those 2 domains. And so far, actually, we've been able to keep up.

So we just wanted to highlight everyone like all companies right now, talent is going to be a constraint. But we continue to work with our CHRO, Sue Ivay, and our business unit leaders on mechanisms and ways to ensure that we can step up to our customer requirements. So, right now,

it's not impeding our growth, but it's something we've got an eye on, and we're not taking for granted.

Q: That's great color. Can you maybe quantify how much of a wage impact it's having on your overall business? Or how much of an impact it's having on your EBITDA margin assuming that that you've got to pay higher wages possibly for retention purposes?

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Yeah, we try to respond to the market conditions wherever those people are working in the roles they have. And, we certainly – that's an important factor, not the only one in terms of retaining the people, but it's certain one, and then – as we get new customer deals, we try to take all of that information whether our fixed costs and our variable costs, and try to price it appropriately. So far, we haven't seen a massive margin erosion because of it, but that's certainly one we're going to have to be dynamic with us, as we continue to do bid on new deals.

Q: Okay. Well, I just heard clearly, you're pretty much able to pass on in a lot of cases whatever higher wages.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

So far, to some extent, yes. I mean, obviously, you've been seeing in the news pretty significant increases, and it's unclear, when this is going to end. So, I say, so far, but our ability to that depending on the magnitude going forward is going to be something to watch.

Q: Okay. And then just one last question for me, supply chain issues, obviously, it's something that's impacted the entire IT space. I would assume that you guys are going to feel it on your Advanced Tech side and your IT side. Can you maybe talk a little bit about what specifically we're seeing, and just based on the feedback from your suppliers? How long you think that issue is going to persist in first half 2022? Or do you guys think it's going to persist through next year? And has it resulted in you guys maybe carry a little bit higher inventory in some cases? And I'll pass the line. Thanks.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Yeah, thanks, Nick. So in that area, it really depends on our segment. In certain areas, we've been absolutely able to find alternative sources, if we've had issues, whether it's on chips or components. Other areas, it's been maybe lead times or longer. But, so far, we just did an update and did a review yesterday. So far, we continue to be able to make schedules and deadlines from Calian's perspective.

The risk is, as you said, as this continues maybe we will see some delays, but I don't think it's going to be across the whole company, it'll be in pockets of the company. And our procurement teams right now are working day and night to confine alternative sourcing both domestically and globally, ensure that we don't hit that wall.

So far, we've been able to manage through it, much to the thanks of our procurement supply teams that are scanning a little globally. And if we see some issues, it will likely be in certain pockets. But, again, we're not expecting a major delay, maybe minor delays currently. That could change

to your point, because of the current dynamics. As far as how long does this go? It's a bit of a crystal ball exercise, I think for the world right now. We're starting to see some things come back online. But I think to your point, the first half of this year, I think, most companies are going to be dealing with some form of this until we see supply chains get back to 100% capacity.

Q: Okay, thank you.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thanks for the questions.

Operator

Your next question is coming from Neil Bakshi. Your line is live.

Q: Good morning. Thanks for taking my question. So, I thought it start off just by following up on that last question about supply chain issues. Just wondering if that affects in any way that \$5 million to \$10 million opportunities you last noted regarding that EV manufacturer integration. Just wondering if that affects it at all or we're seeing – and replenished with other opportunities as well?

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

So far it hasn't. I think we've been trying to overcome it with just sheer time and effort. The team is working day and night to make sure that we can keep up with the customer demand. And we have to buy slightly more than we normally would have just to make sure that we can do that. So, so far it hasn't, but it's not because we aren't putting in the effort to try to make sure it doesn't happen and the teams are working very good and very hard.

Q: Right. Okay. And then, just a question regarding the modular reactor, nuclear reactor services. I guess, coming off of COP26, and a lot of kind of alternative energy sources, just wondering what you're seeing in terms of pipeline of other servicing opportunities in that space or the pipeline, you could speak to there.

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah. Thanks, Neil. How exciting is it to be the CEO of a company that's working with organizations on small modular reactors, nuclear reactors, when you think about the climate challenges globally that, obviously, we're highlighting [indiscernible] and COP conference. So I'll just say the team, our nuclear group probably doesn't get enough visibility or highlight in our company because of the diversity and led by Annie and Francois.

We have a very talented group of nuclear engineers that are working with organizations on SMRs with regard to their initial feasibility studies, the whole kit. So, we believe this is not just a domestic opportunity, but a global opportunity, but we're going to walk before we run. So we have quite a few discussions going on. We've won some contracts to start working through that.

In many ways, we're winning our, more than our share I think, which demonstrates the talent of our team. So, nothing I want to look at. Longer term, short term, it's going very, very well. But I think, frankly, that opportunity in its own could be a pretty interesting one for Calian over the next

couple of years, not just from a growth perspective, but to your point, on the potential impact to climate. And, so we're really excited by it. And standby, we'll continue to try and update as we go through our next calls. And thanks for that question, because we probably don't talk about those areas enough in the company.

Q: Excellent. Thank you. And then, just one question, with regards to the telenursing services contract. Just wondering if the margin profile is to be seen as similar to what you've been seeing in the last year or if there is any kind of higher or lower, just any color you can provide there? Thank you.

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Sorry, I just missed the beginning of that. Which contract, sorry?

Q: This is the telenursing services. It's about \$13 million in the backlog for Q4.

Patrick Houston - Chief Financial Officer, Calian Group Ltd.

Yeah. So we continue with that one. It's been going well. I don't see any expectation and change on demand or margins. So I think that one continues here in the short-term as the customers still want the services.

Q: Okay. Thank you. I'll pass the line.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Thank you.

Operator

We have no further questions from the lines at this time. I would now like to turn the floor back to Kevin Ford for closing remarks.

Kevin Ford - Chief Executive Officer, Calian Group Ltd.

Good. Thanks, Katherine. I appreciate you [hosting] [ph] this event today. And I want to thank everyone who attended and participated. I think you all are hearing a pretty excited CEO at the end of the line. The team, I want to thank again.

I have just never seen so many assets in this company on the technology elements, we're looking at healthcare platforms, we're talking about virtual care platforms, we're talking about learning platforms. So I think that journey as an innovative global growth company is well, well entrenched. And the team is committed to making that happen.

I just really want to highlight again my thanks to the Calian staff who have really knocked it out of the park from my viewpoint, and not only created amazing results, but created a foundation for our continued growth to \$1 billion company. So, my thanks. And, with that, Katherine, we can end the call.

Operator

Thank you. Ladies and gentlemen, this concludes today's event. You may disconnect at this time and have a wonderful day. Thank you for your participation.