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Verisk Analytics, Inc. (VRSK)

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the Verisk Fourth Quarter 2018 Earnings Results Conference Call. This call is being recorded. At this time, for opening remarks and introductions, I would like to turn the call over to Verisk's Head of Investor Relations, Stacey Brodbar. Ms. Brodbar, please go ahead.

Stacey Brodbar

Head of Investor Relations, Verisk Analytics, Inc.

Thank you, Grace, and good morning, everyone. We appreciate you joining us for a discussion of our fourth quarter and full year 2018 financial results. With me on the call this morning are Scott Stephenson, Chairman, President and Chief Executive Officer; Mark Anquillare, Chief Operating Officer; and Lee Shavel, Chief Financial Officer.

Following comments by Scott, Mark, and Lee, highlighting some key points about our financial performance, we will open up the call for your questions. The earnings release referenced on this call as well as the associated 10-K can be found in the Investor section of our website, verisk.com. The earnings release has also been attached to an 8-K that we have furnished to the SEC. A replay of this call will be available for 30 days on our website and by dial-in.

Finally, as set forth in more detail in today's earnings release, I will remind everyone that today's call may include forward-looking statements about Verisk's future performance. Actual performance could differ materially from what is suggested by our comments today. Information about the factors that could affect future performance is contained in our recent SEC filings.

Now, I'll turn the call over to Scott.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Thank you, Stacey, and good morning, everyone. Apologies for my voice today. As we turn the page on 2018, I want to give you my bottom line view of the year just passed. We did well and see opportunity to improve. The single most important reflection of our vitality is our rate of organic revenue growth. And normalizing for the effect of exceptional storm related revenues and a significant contract signing in Financial Services in 2017, our organic constant currency revenue growth was 7.2%, ahead of our long term financial target of 7%.

Moreover, our growth was broadly based across our Insurance vertical, along with Wood Mackenzie and the Energy space and our core consortium data analytics in the Financial Services vertical.

The heart of our position in the three verticals is sound and forms the basis for cross-selling new solutions in the future.

Looking more deeply into the organic revenue outcomes across the company, I see eight contributing factors.

Number one, very high rates of customer retention; two, growth in the number of products consumed by existing customers; three, the introduction and adoption of new innovative solutions; four, positive pricing due to enhanced value in many solutions; five, in those places where we have head-to-head competition, share gains in those

categories, including cat modeling, remote imagery, and underwriting decision support; six, effective progress in non-domestic markets, especially the UK; seven, a high rate of captured business with new entrants in the Insurance vertical, including the InsurTech companies; and eight, our position as a partner to our customers who continue to entrust Verisk with their data, enabling us to build new solutions in new categories.

For example, in Insurance, we are working with our customers to repurpose some contributory policy data already used in our underwriting business to develop innovative claim solutions. One such solution will enable carriers to automate the subrogation process quickly and seamlessly.

In Energy & Specialized Markets, Wood Mackenzie is leveraging the consortium model developed by our insurance colleagues and bringing it to the Energy sector, where we believe it is in a nascent stage. We are currently finalizing an agreement to create an energy data consortium in one of the key U.S. tight oil plays.

And in Financial Services, we are working with our card issuer partners in Mexico to launch a fraud consortium to help combat the transaction-based fraud plaguing their system.

An important underlying foundation to our growth is the agility of our technical infrastructure, which permits us to bring new solutions to market faster and with greater analytic content. On this front, I was pleased with the following in 2018.

Our analytics community has grown substantially through our own program of cultivating data scientists along with industry hiring. And all of this supported by the naming of our new Chief Analytics Officer. We saw a doubling of our consumption of public cloud capacity in 2018. We have made progress in advancing our data methods to support widespread tokenization, which contributes to our internal security and presents opportunities to access new datasets from equally security minded data sources.

On the innovation front, we introduced a wide variety of unique and customer driven solutions across our verticals. In Insurance, we launched programs to address new risk exposure, including cyber and flood. We also successfully introduced a variety of disruptive and award winning innovations to the market, which Mark will talk to you about in more detail.

In the Energy and Specialized Markets segment, we launched Lens, a cloud-based data and analytics platform, which allows customers to access, analyze, and model data in every major commodity in every market. And in our Financial Services sector, we delivered next generation merchant analytics to retailers.

As a complement to our innovation agenda, we are very focused on driving operational efficiency. As we shared with you in detail at our Investor Day in December, we worked diligently to advance our operational excellence initiative through Lean Six Sigma. With 3,100 employees trained and 85 active projects under way and more soon to be launched, Verisk is driving a culture of continuous improvement by measurably improving processes and meeting the critical customer needs of quality and speed.

Another leading indicator for me comes from the many conversations I have with the CEOs of our leading customers. Are they thinking of Verisk as a partner or as a vendor? A consistent message across 2018 is that we are engaging our customers around some of their highest priority initiatives for the future. And they see Verisk as a distinctive and trusted partner in doing so. The result of many of my CEO visits is a request that their teams be placed in closer proximity to our innovation pipeline.

A last comment about the year just passed regards the planning cycle we went through at the end of the year. I have never seen a higher volume of fresh ideas for new solutions and approaches for engaging our customers. We have the wonderful problem of needing to choose among a wide variety of opportunities.

Finally, I'm pleased to announce, as you've seen, that our board of directors has approved the initiation of a cash dividend to shareholders. This represents an important milestone in what is the 10th year of our history as a public company and demonstrates the confidence we have in our ability to drive sustainable profitable growth, generate significant free cash flow, and create long term shareholder value through careful capital management.

I'll now turn the call over to Mark to comment specifically on our Insurance business.

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

Thank you, Scott. I'm pleased to share with you that 2018 was a strong year in our Insurance businesses, one marked by solid growth across most of our lines of business, fueled by leading innovation and enhanced customer engagement.

Excluding the impact of approximately \$16 million of storm related revenue in 2017, Insurance revenue on an organic constant currency basis grew 8.3% in 2018. Our customer retention rates remain very high. And the overall portfolio of new and truly innovative solutions is more robust than ever.

As Scott mentioned earlier, we've received numerous innovation of the year awards for our creative solutions, including, one, LightSpeed Auto, our innovative data forward workflow solution that delivers a faster and more efficient experience for underwriting and buying insurance. A fully bindable online auto quote is delivered after providing only three pieces of key data. We've extended the LightSpeed technology and platform to address the property and small commercial insurance segments. Several customers have signed contracts. And our pipeline of interest for LightSpeed is growing.

Two, Verisk Data Exchange, our IoT data consortium that collects connected car data from our GM, Honda, and Hyundai partnerships on more than 4.7 million vehicles, covering more than 80 billion miles. The insurance applications range from driving behavioral scores for underwriting to instant notice of loss solutions for claims.

And three, EPIX, our Energy & Power Intelligence Xchange or insurance platform that helps energy insurance professionals research, assess, and underwrite complex risks. The solution addresses a critical profitable growth need by combining Verisk risk scoring and benchmarking insurance expertise with WoodMac's unique energy data.

A steady stream of first-to-market innovation is one of the four distinctives at Verisk and is also a key driver of our growth. It is also an important force of change within the insurance industry.

On that front, InsurTech is gathering lots of mind share and meaningful capital investment, which we think creates future growth opportunities for Verisk. In my view, InsurTech has grown in two distinct areas.

One, startup insurers and managing general agents, or MGAs, who are underwriting and distributing insurance. These type of InsurTech startups are likely to need data analytics to effectively price and sell insurance in a competitive market. We believe these startups have the potential to become Verisk customers. And in fact, in 2018, we engaged with 67 of these startups on 182 opportunities and had 79 product wins.

Second, other InsurTech startups include service providers, who are trying to improve the insurance process. These startups may be competitors of ours. But many recognize the value of our services and continue to solicit our data analytics, distribution channel, or even possible investment.

The threat from InsurTech players has ignited investment by more traditional insurers, who are focused on analytics, digital engagement, and automation to compete with InsurTechs and deliver a better customer experience for their policy holders. This momentum and insurer investment have led to increased opportunities for us.

A common description of InsurTech is the use of technology innovations designed to improve the insurance process by squeezing out savings and driving efficiency from the current insurance industry model. With this definition in mind, I view Verisk as the most comprehensive and trusted InsurTech provider.

As we've communicated to you over the years, international expansion is an important part of our long term growth strategy. And in 2018, it was a solid contributor to growth.

The United Kingdom provides a playbook for success in future international expansion. The global insurance market, the specialty – especially specialty lines has hubs [audio gap] (12:25) world, with London as a key gateway to global markets and an accelerating step on our journey to extend beyond the United States.

This vision is becoming reality in the UK. Our strategy is to provide a comprehensive suite of solutions across the entire insurance value chain, driving data and automation from broker to underwriter to reinsurer and from quote to claim settlement.

During the quarter, we acquired Rulebook, an industry leading provider of business intelligence and software solutions for the London insurance market. Rulebook, in combination with Sequel, furthers our goal of providing leading solutions to the global insurance market, including a comprehensive chain of solutions to specialty insurers for mitigating risk and optimizing total cost of operations. Our customers are recognizing the advantages of these integrated solutions, resulting in new contracts and increased sales opportunities.

With a successful 2018 behind us, we are focused on 2019 and are actively meeting with employees and customers. To kick start each year, we hold a series of town hall meetings at our major offices to share Verisk insurance solutions strategic direction.

We also held our annual insurance sales meeting in Nashville earlier this month. The first evening of the sales meeting was an award ceremony and a celebration of a strong 2018. The meeting then serves as a forum for leadership to communicate our goals for 2019 and for the sales teams to learn about our new innovative solutions.

Our 200-person sales team experienced demos from our product experts and were briefed in our innovation lab on Verisk's cutting-edge AI in automation technologies. Several customers joined us and emphasized the importance of our products and thought leadership to their businesses, as well as suggested enhancements to our solutions. The teams left our town hall and sales meetings with a sense of accomplishment, energy, and momentum from 2018 and motivated for 2019.

With that, let me turn the call over to Lee to cover our financial results.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Thanks, Mark. First, I'd like to bring to everyone's attention that we've posted a quarterly earnings presentation that's available on our website. The presentation provides background data trends and analysis to support our conversation today.

Moving to the financial results for the quarter, on a consolidated and GAAP basis, revenue grew 7.7% to \$614 million. As a result of an income tax benefit of \$89 million recorded in the fourth quarter of 2017 related to tax reform, net income decreased 28.5% to \$146 million for the quarter.

Diluted GAAP earnings per share were \$0.87 for the fourth quarter 2018, a decrease of 28.7% compared with the same period in 2017. Equalizing the fourth quarter 2017 effective tax rate to that of the fourth quarter of 2018, adjusted net income and diluted adjusted EPS would have increased 5.6% and 6.1%, respectively.

Let's focus our quarterly discussion on our normalized organic constant currency results for all year-over-year growth rates and to eliminate the impact of currency fluctuations, recent acquisitions for which we don't have full year-over-year comparisons, and nonrecurring items, including the impact of the storm related revenues recorded in the fourth quarter of 2017.

On a normalized organic constant currency basis, Verisk delivered revenue growth of 6.9% and adjusted EBITDA growth of 7.3% in the fourth quarter of 2018, reflecting strong organic growth across the Insurance and the Energy and Specialized Markets segments, offset by weakness in Financial Services.

Adjusted EBITDA margin for the quarter of 47.8% was up from 47.6% on a normalized basis in the prior year period. Please bear in mind that our reported fourth quarter 2017 margin, not adjusted for the storms, includes the benefit of 100% margin on the \$8 million in storm-related revenue.

For the full year of 2018, normalized for both the storm related and nonrecurring implementation revenues, we achieved 7.2% organic constant currency revenue growth and 7.7% organic constant currency adjusted EBITDA growth. Adjusted EBITDA margin was 48.5% in 2018, up from 48.3% in 2017. We achieved these results while also maintaining substantial investment in our business and sustaining ongoing recovery in our Energy and Specialized Markets and Financial Service (sic) [Services] (17:25) sectors.

Let's now turn to our segment results on a normalized organic constant currency basis. As you can see in the press release, Insurance segment revenue grew 8.5% and adjusted EBITDA increased 9.9%, reflecting an adjusted EBITDA margin of 53.5%, up from 52.8% in the prior year, and inclusive of substantial investments in remote imagery and telematics.

Within our Underwriting & rating business, we saw solid performance with healthy growth in commercial lines, personal lines, and catastrophe modeling services.

Within Claims, the strong growth was driven by solid performance across most of our Claims businesses, partially offset by continued softness in our workers' compensation claim resolution services.

Energy & Specialized Markets delivered revenue growth of 5.1% for the quarter, as the energy industry continues to recover. We experienced growth in both our core research and consulting solutions, as well as strong

contribution from our breakout areas, including power and renewables, chemicals, and subsurface. We also had positive contributions from environmental health and safety and weather and climate analytics revenues.

Adjusted EBITDA increased 4.6%. Adjusted EBITDA margin of 31.3% was slightly down from the prior year period of 31.4%, as we continue to invest in WoodMac 2.0, or Lens as it is branded in the marketplace, and our chemical, subsurface, and power renewables breakouts. These areas represent opportunities to leverage Wood Mackenzie's data and industry expertise more broadly and to deliver and develop products more swiftly and efficiently.

Financial Services revenue declined 2.2% in the quarter and adjusted EBITDA decreased by 12.8%. Solid growth in portfolio management solutions and spend informed analytics were offset by headwinds from tough comparisons with prior year implementation revenues as well as some timing differences.

As we articulated previously, we continue to make progress on our initiative to reduce the variability of revenues in this segment, particularly around project based items. As we work through this process, we will continue to see quarterly fluctuations on revenue and growth higher than our other businesses. That said, we are encouraged by the long term growth potential in our Financial Services segment, as we set the business on a stronger foundation for future growth.

Reported interest expense was \$33 million in the quarter, up 1.6% from the prior year quarter due to the funding of acquisitions over the last 12 months and our share repurchase program.

Total reported debt was \$2.7 billion at December 31, 2018, down from \$3 billion at December 31, 2017. Our leverage at the end of the quarter was 2.3 times.

We are very pleased to share that on January 30, Standard & Poor's upgraded Verisk's credit rating to triple B flat with a stable outlook from triple B minus with a stable outlook and assigned a short term rating of A2.

Our reported effective tax rate was 18.6% for the quarter. This compares to the negative 14.1% we experienced in the prior year quarter, as we recorded a benefit resulting from the revaluation of our net deferred tax liabilities in connection with tax reform. For the full year, our effective tax rate was 16.8%, which was lower than our targeted range due to significant exercises of soon-to-expire employee stock options related to our 2009 IPO that produced a favorable tax impact.

For 2019, we expect our tax rate to be between 19% and 21%, though there will be likely some quarterly variability related to the impact of employee stock option exercises, which depends in part on the Verisk stock price and employee personal decisions.

Adjusted net income was \$174 million and diluted adjusted EPS was \$1.04 for the fourth quarter, down 21.8% from the prior year. This decrease reflects the impact of a prior year \$89 million tax benefit related to the 2017 tax reform. Equalizing the fourth quarter 2017 effective tax rate to that of the fourth quarter of 2018, adjusted net income and diluted adjusted EPS would have increased 5.6% and 6.1%, respectively.

Further normalizing for the elevated storm revenue in the quarter, adjusted net income and diluted adjusted EPS would have increased to 10% and 10.6%, respectively, consistent with our long term objective for double digit EPS growth.

Net cash provided by operating activities was \$173 million for the quarter, up 14.5% from the prior year period.

Capital expenditures were \$77 million for the quarter, up 9.8% from the prior year period, reflecting continued investments in future growth opportunities, including remote imagery, telematics, and Lens, and software development to support and improve new and existing products across the organization.

Total capital expenditures for 2018 were \$231 million and represented 9.6% of total revenue. As we have said previously, we expect capital expenditures to decline as a percentage of revenues in 2018 – I'm sorry, 2019 and over the long term and to be within a range of \$220 million to \$240 million in 2019.

As that translates to depreciation and amortization, we expect fixed asset depreciation and amortization to be within a range of \$175 million to \$185 million in comparison to the \$165 million for 2018. And we expect intangible amortization to be approximately \$135 million in 2019 in comparison to \$131 million in 2018. Both depreciation and amortization elements are subject to FX variability and future M&A activity.

Free cash flow was \$97 million for the quarter, an increase of 18.6% from the prior year period.

This quarter we returned \$156 million in capital to shareholders through the repurchase of approximately 1.3 million shares at a weighted average price of \$119.55. At December 31, 2018, we had \$428 million remaining under our share repurchase authorization. In addition, we initiated a new \$75 million accelerated share repurchase to be executed in the first quarter of 2019.

Of course, the big news on the capital front was the initiation of a cash dividend of \$0.25 per share this quarter. We are very pleased to reach this milestone in our 10th year as a public company and to deliver another source of value to our investors.

This dividend underscores the stability of our business, profitability, and cash flow, as well as a diversification of our capital return discipline, balancing share repurchases and dividends. We further expect that the dividend will open new groups of potential shareholders to Verisk.

It's important to note that the dividend initiation does not reflect any diminution in our growth prospects or the opportunities to invest our capital. We will continue to have sufficient capital to support our long term growth objectives, which remain unchanged.

We remain excited about the opportunities to invest in our business and remain focused on long term profitable growth and solid returns on capital. We remain confident that we have the financial strength and capital structure to support investment for the long term. We continue to appreciate all the support and interest in Verisk.

Given the large number of analysts we have covering us, we ask that you limit your questions to one and one follow-up. With that, I'll ask the operator to open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you, Mr. Shavel. [Operator Instructions] We will proceed in the order that you signal us and will take as many questions as time permits. [Operator Instructions] Our first question comes from the line of Toni Kaplan of Morgan Stanley. Your line is open.

Toni Kaplan

Analyst, Morgan Stanley & Co. LLC

Q

Hi. Good morning. Scott, you mentioned that you've been meeting with the CEOs of your customers. Could you just call out what themes may be on their minds that might be different than last year? Or just give us a sense of the most important priorities that they're focused on?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah, thanks, Toni. Two things immediately come to mind. One is, I would say almost every insurance company CEO believes and expects that they can find ways to make their company grow faster than their competitors, faster than the industry.

And I think that's really significant, because it means that what they are leaning into is improved methodologies. They're not just trying to sort of hunker down and play a cost game. They are looking to grow their businesses. And they realize that the world around them really has changed and continues to change because of technology.

So I would say that that's really the first and the most important thing that's going on.

I would say the second thing that is also pretty obviously true, I would say especially for the mid and larger companies, is they are really persuaded of the importance of accessing partnerships and supply from outside of their own companies. In other words, they realize that there are ways that their businesses can be benefited by tying in with others.

And so I see a lot more partnering. I see a lot more venture investing, as they try to get closer to technology. And I just see a lot more outreach to a company like ourself that is recognized as being sort of distinctively able to help across multiple fronts.

So these are very constructive meetings. They are partnership meetings.

Toni Kaplan

Analyst, Morgan Stanley & Co. LLC

Q

Terrific. And then for my follow-up, I wanted to ask about margins. So in Insurance, I think we've seen investment impacting margins. Same with first quarter in Energy last year.

I guess, should we view 2019 as maybe a little bit – a continuation of investing, but maybe a little bit less so than 2018? Or how should we directionally sort of think about it?

And then outside of scale, are there any margin initiatives across the business, like efficiencies, that you're looking to drive this year? Thanks.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Sure, thanks, Toni. This is Lee. So I think it's – I would start off by saying, certainly all of our businesses we think have superb operational operating leverage. And so as you know, across the organization, our expectation is that each of the businesses will demonstrate improvement in margin.

I think it's a fair observation that in 2018 there was a high level of investment in a variety of initiatives, Geomni, Lens, the IoT and telematics, where we chose to make those investments. And that those obviously had a negative impact on margin.

But notwithstanding that, I want to reiterate, as I mentioned in my comments, that both for the fourth quarter and for the year as a whole, when you normalize for the storm activity, we had margin expansion on the year-over-year periods.

And so from our perspective, recognizing that that storm revenue and the implementation revenue for TSYS was 100% margin. And so that certainly skewed that year-over-year comparison. We believe that we delivered margin expansion as well as substantial investment in the businesses for that period.

In 2019, we won't have that storm comparison. And as Scott indicated, we still see very attractive opportunities to invest. But I think it's fair to say that probably in 2018 from a scale standpoint, particularly around Geomni, it was a higher level, consistent with our CapEx guidance. That was an acceleration.

We expect to see that absolute level of investment decline as a percentage of revenue. So we feel good about the opportunity to strive towards our goal of margin expansion.

Toni Kaplan

Analyst, Morgan Stanley & Co. LLC

Q

Thank you.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Thanks, Toni.

Operator: Our second question comes from the line of Hamzah Mazari from Macquarie Capital. Your line is open.

Hamzah Mazari

Analyst, Macquarie Group

Q

Good morning. Thank you. Just on the Financial Services segment, maybe you could just touch on how you plan to reduce variability of revenues in that vertical? And maybe just timing of that initiative?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Sure, Hamzah. This is Lee. Thanks for that question. So the process is essentially in recognizing in project – on project related revenues. I think the tendency in the past had been to recognize more of that revenue upfront.

I think as we have the flexibility in structuring those relationships as new business comes on, we are – and this is not perspective, this is already occurring. We are structuring the relationships so that that revenue is realized over time, so that we don't have these large chunks of revenue that create that variability.

So that is part of the objective. That's a structural initiative as we work with clients.

But also I think fundamentally as we think about developing the growth of the business, our focus is on building the sustainable growth component off of the four constituent businesses that we've described before. So that it is more incremental growth across that base. I think both of those will contribute to more stable, less variable revenue and profitability over time.

Hamzah Mazari

Analyst, Macquarie Group

Q

Great. And just for my follow-up question, on the international business, what sort of next milestones should we be looking at in that business? I know you talked about products essentially needing to be more customized locally. So just any color on long term international insurance strategy? Thank you.

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

Yeah, thank you. This is Mark. Just to kind of follow-up on the question. So I think what we've seen is it's a bit of a build-and-buy scenario.

So what we are now doing, which has become very powerful in front of customers, is we've taken many of our solutions, and we've started to integrate them in a more holistic way. So walking into a customer as opposed to buying all these point solutions, there's an attractiveness of knowing that your data is going to flow from the beginning of a process that starts at maybe a quote or an underwriting decision on through the process, so you can see it from a portfolio perspective in some of our catastrophe modeling solutions. And all of that is information that's embodied in the solution at Sequel.

The concept and the construct here is, I can do it more effectively. I can do it more efficiently. I can do it more accurately. And on top of that backbone, we've added some of, I'll refer to it, the ISO and some of the other analytics that has been so powerful here in the States.

So that continues to evolve. I think we'll be able to do more and more with customers as we gain access to more data.

And maybe just to take your question one step further, to maybe highlight that I think we see London as being kind of a gateway into the international community, especially with the specialty lines. So as we win these contracts, we're doing work not just in the UK but with companies who are located in the UK but are underwriting business throughout the world. So our next step into other geographies is that much easier.

Hamzah Mazari

Analyst, Macquarie Group

Q

Great. Thank you.

Operator: Our next question comes from the line of David Togut from Evercore ISI. Your line is open.

David Mark Togut

Analyst, Evercore Group LLC

Q

Thank you. Good morning. I'd like to ask about the Financial Services business, which was really weak for the second year in a row. I'm wondering if this business has the same distinctives that really characterize both your Insurance and your Energy and Specialized Markets businesses? Especially since competition here seems to be increasing with a number of well-capitalized competitors like Mastercard offering more and more analytics to credit card issuers.

So my question really is, does this business really still fit within Verisk? Especially given the broader capital allocation framework that you've rolled out today, which seems to focus more on capital return?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

[ph] David, Scott here. (35:39) Yes, the business does fit. I think that many of the folks on the call today are familiar with what we call our four distinctives, which we talk about a lot. Which, just to remind everybody, are unique data assets, deep domain expertise, first mover advantage, and deep embedment in customer workflows. And what we do in Financial Services has all four of those qualities.

So as Lee previously talked about some of the things that have sort of moved through the business of late, we talked about the sort of the lumpy quality of the way that some of the revenues have been recognized in the past.

But what I would go back to is that the heart of the business is built on consortium data, which is absolutely unique. And unlike the data which is available to anyone else, including the players you just mentioned, on top of which then we have very deep relationships with our customers. And really a large data platform, which is really remarkable for a company of its size. So all of the conditions are there.

And then I would also say, again, echoing what Lee said, the strength of portfolio analytics plus the spend analytics that we do are the leading parts of the business. And they're actually healthy.

So we expect that as these other effects sort of wash through, you'll get sort of a more clear view of those things built upon the distinctives, which really will power the business going forward.

David Mark Togut

Analyst, Evercore Group LLC

Q

Thanks for that. As a quick follow-up, I'd just like to ask about dividend policy. The math shows that the LTM payout ratio is about 28%. How do you think about the payout ratio that you're using to set the dividend? And do you expect the dividend to grow in line with earnings or faster than earnings going forward?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Right. Thanks, David. It's Lee. Let me take that. So we – in setting that level, we looked at the payout ratio. Really also what proportion of capital are we allocating to the dividend. And an eye on kind of yield and where yields are out there.

We recognize that investors will expect and reward growth in the dividend over time. And we certainly believe that our ongoing earnings growth will provide a very strong consideration for these decisions by our board in the future. We also expect to weigh capital investment and return opportunities in the allocation decisions ahead.

So all of those I think factor into it. But there clearly is a recognition that there will be an expectation given our overall growth that the dividend should grow as well. And that's what we will balance looking ahead in advising the board on those decisions.

David Mark Togut

Analyst, Evercore Group LLC

Thank you very much.

Q

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Thanks, David.

A

Operator: Our next question comes from the line of Manav Patnaik from Barclays. Your line is now open.

Manav Patnaik

Analyst, Barclays Capital, Inc.

Thank you. Good morning. Scott, I think at the beginning of the call, you talked about the repurposing of some of the insurance consortium data. And I was wondering if you could just expand on that? Maybe taking a step back and letting us know how much of the data do you have access now to play around and innovate with? And if this is a new or ongoing opportunity?

Q

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Yeah, so let me start, and, Mark, you may want to amplify some of this. But when we think about data and the Insurance vertical, it's really a combination of looking for opportunities to tease additional meaning out of existing datasets and generating new datasets.

A

So up front, I mentioned, for example, subrogation. Subrogation is essentially bound up in the claims resolution process. And as I think most folks know, we have a lot of claims data. So finding a way to point that at the subrogation case and to think about affiliated things like clearing payment between counterparts is just interesting. And it's really a process that hasn't really been transformed yet in the insurance industry. So that would be an example of repurposing.

But then there are other places where we're trying to generate original datasets. And one thing I would just comment on here is that on the one hand, we're very alert to opportunities to position data to where it can be repurposed. On the other hand, we're very diligent about the reasons why our customers made the data available to us in the first place.

And so we're going to always be striking a balance between what's possible and what our customer contributors would like to see us do. But there's plenty of room in there for innovation.

And then there are a variety of new datasets, where we're making original calls for data. And actually even that takes a couple of forms. One is we have existing platforms like PCS, where we started the call data related to cyber incidents. And we didn't used to do that. So that's original data but around an existing platform.

We're always trying to enrich the data that comes into a platform like ClaimSearch. And then we're trying to find, yeah, new forms of claims data that we don't receive today. For example, commercial claims histories are not as developed as personal claims histories. Mark, anything you want to add to all that?

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

Yeah. I think that was well said. I think it goes back to the earlier comments you made about partnerships and conversations with CEOs.

In the world of data, obviously our customers and many people feel their data is valuable. So we need to provide them with valuable use cases back to their businesses in order for them to let us use the data. So having the great partnerships and relationships is very important. We continue to be a trusted intermediary for that data. And we feel that it's a privileged position.

Manav Patnaik

Analyst, Barclays Capital, Inc.

Q

Got it. And just for the follow-up, Lee, just on the Energy and Specialized [Markets] side, I think last year, you guys called out I think it was a bank and then a merger-related kind of headwind to the business. Have we lapped those comps? And does that mean next year the numbers should start looking better?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Thank you, Manav. The – we will lap that in the first quarter of 2019. So we were still experiencing that headwind in the fourth quarter. But that will go away in the first quarter of 2019.

Stacey Brodbar

Head of Investor Relations, Verisk Analytics, Inc.

A

Next question?

Operator: Our next question comes from the line of Andrew Steinerman from JPMorgan. Your line is open.

Andrew Charles Steinerman

Analyst, JPMorgan Securities LLC

Q

Hi. It's Andrew. Wanted to ask about WoodMac 2.0 Lens. What are some milestone and rollout that we should be looking for? And will WoodMac 2.0 help margins and revenues? Or just one of them? And particularly make it a comment for 2019.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah, so let me take it at a general level, Andrew. And maybe, Lee, if you want to add anything. It's constructive on both the revenue and the margin side, because part of what Lens is getting after is the very nature of our data aggregation. And it becomes more efficient on this platform that we built. But equally, there's more functionality there for customers. And so we think it'll be constructive in both ways.

I don't – I wouldn't point you so much to milestones or at least not those that will be called out in the overall performance of the business. What I'm trying – and I'm not making a comment about the future profile of the

financial performance of the business. I'm simply saying, the revenue streams are all – sort of think of it as a bowl of spaghetti. And Lens works its way through things that we already do, in addition to representing modules, new modules that we can license to customers.

But as called out specifics, basically it'll be – we do business with so many companies already, this will really enhance cross-selling into existing relationships. But in terms of visibility to the outside, I'm not – I wouldn't call out any particular milestone, just the general progress of the business really. Lee, anything you want to add to that?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

No, I think Scott covered it. I would just make the comment that Lens really represents the platform that enables us to continue the evolution of a very good research and consulting business into, increasingly, a data analytics business that can serve a broader customer base, can develop and integrate data products more effectively, which is beneficial both from a revenue growth standpoint as well as from a margin perspective.

And I would just finally add that the team there continues to work on operational efficiencies to improve the margin as well.

Andrew Charles Steinerman

Analyst, JPMorgan Securities LLC

Q

But, Lee, might there be a time, like maybe this year, where you're running two infrastructures for WoodMac, and it might be a drag to margins?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Well, I mean, yes but no. So you observe something, yes. But the implication I don't think is right.

So yes, we need to be running things in parallel. And we have been investing, as Lee has referenced several times, to build the platform.

But the actual operation of the platform – I mean, one of the things that's so constructive inside of our business is that we enjoy the gift of Moore's Law every day. And so actually the cost of compiling data or even processing data inside of the platform that you have built, the incremental cost is not really all that great. I'm not saying that it's zero.

So you're correct about what we will do operationally. But I think the implication you were trying to reach in terms of operating expense going forward is not so accurate.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Yeah. And I would go more broadly, Andrew. I think that definitely has some relevance with regard to our transition to cloud, where we are making investments and see opportunities to find greater efficiencies where we still have legacy costs. I think that is – would be a valid observation, not so much in this context. So thank you for the question, [ph] Andrew (46:46).

Andrew Charles Steinerman
Analyst, JPMorgan Securities LLC

Q

Okay. Thanks. You bet. Thanks.

Operator: Our next question comes from the line of Tim McHugh from William Blair & Company. Your line is now open.

Timothy J. McHugh
Analyst, William Blair & Co. LLC

Q

Yes. Hello. First, I wanted to ask on the Energy side of the business, in the prepared remarks you talked about being close to signing a consortium deal. Can you talk more about that and the nature of the data I guess and the product I guess that would flow out of it?

Scott G. Stephenson
Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah. So those of you who have followed us know that the majority, in fact, a large majority of the data that we've had up until today has been mostly about the commercial dimensions of the oil and gas business. So observations about productivity and the cost factors associated with the assets that produce either the raw materials or the refined materials. So those are the datasets that have typically traditionally been a part of what we do.

The datasets we're adding are what we call the subsurface datasets. And these are the ones that take into account the actual real-time operations, even in the oilfield, in combination with the nature of the rock and the nature of the fluids and the nature of the fields. So that we can complement everything we've already done, always done, with basically much more real-time optimization of the operations of our customers' assets.

And this is something that we haven't done as much of, in fact, very little of, up until now. So the datasets relate to that, real-time operational optimization.

Timothy J. McHugh
Analyst, William Blair & Co. LLC

Q

And did you say it was for a specific region or sub-sector of companies you would start with?

Scott G. Stephenson
Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Well, so whenever we talk about the consortium dataset, you're always talking about specific customers and, generally, specific product sets or specific places. So that does apply in what we're doing in building these new datasets, these sub-surface datasets.

And our focus right now predominantly is the lower 48 in the United States, where the need – the situation in the United States is different than the situation in most other parts of the world. Because in the United States what the operators are doing is basically saying, that particular rig, should I move it 2,000 feet? And I can move it. And four days later have 1,000-foot well that's producing. And so that's the speed with which "strategy" is being set and operations are being rebalanced in the United States.

Timothy J. McHugh

Analyst, William Blair & Co. LLC

Q

Okay. Great. Thank you. And then can I just – on the Insurance side, the aerial imagery product set, can you – I think you mentioned is one of the growth drivers I guess. But can you give us more color on adoption, kind of competition for that product at this point? And how it's scaling maybe relative to what the initial plan was 18 months ago or 12 months ago when you kind of made a more aggressive push into this space?

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

Sure. So this is Mark. I think your question is directed at Insurance and at the same time let me maybe even extend a little beyond that. So first of all, we've been very pleased with the takeaway we've had in the market. Our market share is growing. We've won significant customers and many of them. That has clearly contributed to some of the organic growth that we've talked about here.

Beyond what is, I'll refer to it as kind of market share, we've also continued to add products. So remember, in the world of what I view as a complete automated solution, if I was to take and use imagery in combination with some of the scoping and what we refer to as Image-to-Scope, which is the Xactimate tool behind or in front of all of this imagery, we can really automate and become more accurate and more cost effective for those claims adjusters. Literally we think we can double the productivity of the claims adjuster field forces at our customers, saving them hundreds of millions of dollars.

So we're seeing that. What I'd also like to highlight though is that growth is extending beyond what is traditional insurance. As you think about the world of contractors, if you think about the world of, I'll refer to it as mapping and construction, as well as roofing companies, all of those have found use cases in some slimmed down or innovative way we view some of the technology. So that is contributing to the growth across the board even outside of Insurance.

Timothy J. McHugh

Analyst, William Blair & Co. LLC

Q

Great. Thank you.

Operator: Our next question comes from the line of Bill Warmington from Wells Fargo. Your line is now open.

William Warmington

Analyst, Wells Fargo Securities LLC

Q

Good morning, everyone.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Morning, Bill.

William Warmington

Analyst, Wells Fargo Securities LLC

Q

So you mentioned the UK model and a gateway for international expansion. So culturally, there's a lot of similarity between the U.S. and the UK, I guess Winston Churchill would call them, two nations divided by a common

language. But as you go – as you look to prioritize your other geographies for international expansion, what are the ones where you're going to be focusing first?

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

So, Bill, I'm going to assume that that is a continuation of the conversation we had on Insurance. So we think there's a lot more to do in the UK. So we'll continue to push there.

I think what we have identified is looking at like-markets, looking at places that have a more mature insurance marketplace, and a gross premium, and a growing gross premium. We have really identified Europe, but more specifically, Germany and France as kind of the next couple places that are of interest.

Down the road, I think everyone thinks about kind of emerging markets and emerging insurance markets like China, India. We aren't turning a back on that. We're keeping an eye on it. But we kind of think, to your point, trying to stay close to the markets that are a little more mature in Europe is probably the best next step for us.

William Warmington

Analyst, Wells Fargo Securities LLC

Q

Got it. And then for my follow-up, your thoughts on FX impact to revenue in 2019?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Yeah, so, Bill, the reason we try to focus on organic constant currency numbers is that we can't predict what's going to happen from an FX standpoint. So we're focusing on results excluding the FX range.

I do think generally, given the very strong U.S. orientation of our business generally, the fact that WoodMac has a mix of U.S. and international revenues, we think, overall, the exposure is relatively low. So I'd say proportionately, we don't think it'll have a big impact. But our focus is always to try to eliminate that factor, which we can't completely control.

William Warmington

Analyst, Wells Fargo Securities LLC

Q

Got it. Thank you very much.

Operator: Thank you. We have our next question from Jeff Meuler from Baird. Your line is now open.

Jeffrey P. Meuler

Analyst, Robert W. Baird & Co., Inc.

Q

Yeah, thank you. As you productize the subsurface consortium data, as you were just kind of explaining, are you inventing new categories of solutions to sell to customers? And I don't mean new relative to Verisk, I mean new relative to the market. Or said another way, do you have to displace solutions from the leading incumbents that have subsurface data already? Or are these I guess greenfield opportunities?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

It's a combination of the two. And it really hinges upon how much analytic content we get into what we do.

So there are players today that will provide observations about a number of the sort of individual parameters that apply when you're trying to understand the productivity of real-time operations.

So from one place, you can get data that relates to, for example, the completion strategies that have been taken for the individual well. There are other sources where you can make sure that you have completely identified the leasing, the lease holding and ownership structure of whatever patch of land you're talking about. And then other places, you can go for the heavy seismology work and on and on and on like that.

So part of what we will do is to increasingly make those kinds of data available to our customers. But then over and above that, what doesn't exist so much in the marketplace today is the – is really the AI, machine-learned expression of all of that data in quantity across heterogeneous situations, so that in an automated fashion you can really make predictions and drive decisioning. And there we expect, because we're Verisk, we will be distinguished.

How much those kinds of solutions generate completely original revenue streams versus how much they displace, for example, some of these bespoke datasets, I would say that remains to be seen. The primary point here is there is the opportunity for differentiation.

Jeffrey P. Meuler

Analyst, Robert W. Baird & Co., Inc.

Q

That's helpful. And then on the Insurance business, there's been some underlying acceleration. And there was a couple years where maybe it was growing below trend a few years ago. And you called out some various moment in time factors at that point.

But I guess, Scott, as you list out the eight factors that are driving it, they sound largely sustainable. So just how are you thinking about Insurance growth at this point? Like, has bookings growth also accelerated? Is bookings growth outpacing revenue growth? Thanks.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah, so yeah. You definitely understood what I was saying up front. All eight of those trends apply broadly across our company, but specifically in the Insurance vertical.

I mean if you just step back and you say, okay, this environment, this insurance environment, what characterizes it? The customer set is relatively stable. There are occasionally some large merger transactions. And there are some segments like global reinsurance brokers where there's been some of that.

But by and large, the customer demography is steady. Regulation really doesn't change that much. Technology is a constructive factor as it relates to a company like us, because back to the top, virtually every one of our customers believes they can grow faster than their competitors. And so everybody is trying to behave innovatively. And so that's just inherently constructive for folks like us.

And then if you think about all of the many references that we've made this morning, there are just new things that we're doing and bringing to the market that don't exist.

And so it's a constructive environment. I mean the United States property and casualty insurance industry, our home market, is the granddaddy of large-scale contributory data analytics. I mean it was invented that way

practically. And so we really have this wonderful privilege of being who we are inside of that very constructive environment.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Thank you, Jeff. I think we have time for two more questions.

A

Operator: Our next question comes from the line of George Tong of Goldman Sachs. Your line is now open.

George Tong

Analyst, Goldman Sachs & Co. LLC

Hi. Thanks. Good morning.

Q

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Morning.

A

George Tong

Analyst, Goldman Sachs & Co. LLC

I'd like to drill deeper into the Financial Services business. You touched on plans to reduce the variability of revenues through the restructuring of contracts. Can you elaborate on the initiatives you have to improve the overall growth of the segment? Because in the quarter even after normalizing for the year-ago implementation revenues associated with TSYS, organic growth would have been pretty muted. Any color there would be helpful.

Q

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Sure. So, George, this is Lee. And I'm going to refer back to the kind of description and the organization that [ph] Lisa (1:00:01) gave at Investor Day. And so I think it's helpful if you think about it in the four components.

A

The foundation of this business is the benchmarking solutions business. And as we indicated, the growth in that part of the business remains very stable. In addition, the spend informed analytics component remains solid.

The two areas where in the fourth quarter, and I think represent our opportunity to make progress, is in the enterprise data management component, and that really is an emerging space. It is one where we are finding opportunities to develop new data management solutions for our customers, given our scale, given our expertise. And that's something that we certainly think based upon feedback from clients is very positive. But that is something that we'll develop over time. We're encouraged by the initial responses.

And the other element is the fraud component. And that's an area similarly where we feel very good about the contributions from our acquisitions of LCI and G2. We're in the process of developing some of the infrastructure, some of the product sets around that. And we think that over time, that area will also be a stronger contributor to the growth overall.

So that would be the way I would kind of organize thinking around where we see – or where we have immediate focus on improving the growth rate for that business.

George Tong

Analyst, Goldman Sachs & Co. LLC

Q

Very helpful. And as a follow-up, I'd like to switch over to the Energy business. You saw an incremental step-down in organic constant currency growth there. Can you talk about trends in your nonrecurring revenue streams in Energy? And how annualized contract value growth is progressing in light of some of the declines we've seen in oil prices?

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Sure. So I think in that, that's principally the consulting component business that was – it was still growing and growing at a higher rate than our subscription business. But the third quarter was particularly strong.

And so I think that contributed at one level to a slight – and I would just view it as kind of a slight slowdown relative to the third quarter level. But overall, I think we see progress in the – continued progress in the subscription component of the business, particularly as it relates to the new breakout initiatives that are generating strong subscription growth within that segment.

George Tong

Analyst, Goldman Sachs & Co. LLC

Q

Thanks.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

I would just add that the recent movement in the commodity is within a range that we don't consider it material to the performance of our business.

George Tong

Analyst, Goldman Sachs & Co. LLC

Q

Great. Very helpful. Thank you.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Thanks, George.

Operator: Our last question comes from the lines, Jeff Silber from BMO Capital Markets. Your line is now open.

Jeffrey Marc Silber

Analyst, BMO Capital Markets (United States)

Q

Thanks for sneaking me in. I'll be quick. Just a couple of quick numbers questions. Lee, what should we be modeling for interest expense this year? And also the tax rate guidance that you gave us for 2019, is that something we should use longer term? Thanks.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Yeah. So on tax, I think based upon what we see right now, obviously any changes in tax legislation, I think that 19% to 21% range is a good basis.

On interest expense, it's not something that we give formal guidance. We obviously – that's going to flux based upon what happens within the business and our capital allocation decisions. So I think kind of starting with the point of just stability in overall debt levels and looking at the average rates is probably a middle of the way road to go.

But I wouldn't give you any specific guidance beyond that, because that will adjust based upon our capital allocation decisions over time. I would expect that we remain within this leverage range, absent any other material changes.

Jeffrey Marc Silber

Analyst, BMO Capital Markets (United States)



Okay. Thanks so much.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Okay. Well, thank you all very much for your continued interest in Verisk. And we look forward to following up with a number of you, as well as those who are taking a new look at Verisk, based upon our new capital policy, including the dividend. So look forward to our continuing conversations with you. Thanks for this morning and your attention.

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