



ROYAL CARIBBEAN CRUISES LTD.

(Equity Ticker: RCL), (Bond CUSIP:
780153AG7)



Bond Price: \$86.8 (11/04/22)	Yield to Maturity: 11.04%	Debt/EBITDA: NM
Asset Coverage: 1.15	S&P Credit Rating: B	Interest Coverage ratio: NM
Sector: Consumer Discretionary	Industry: Hotels, Restaurants & Leisure	Author: Madhu Chaudhary

RCL is the second largest cruise operator worldwide revenue wise and operates a combined total of 64 ships, covering over 1000 destinations across seven continents.

IN THIS FRESH LOOK WE'LL COVER:

► Summary of the Business

RCL is one of the most prominent and largest cruise companies globally catering to the travel and leisure needs of cruise passengers.

► Recent Developments

RCL is leveraging pent-up demand for cruises created due to the pandemic-led travel restrictions imposed in 2020 and 2021. However, normalization is yet to be achieved as evidenced by lagging occupancy rates and gross yield relative to 2019.

► Competitive Environment

The company competes with Carnival, Norwegian Cruise Line, MSC Cruises, and various other small players. RCL is the second-largest cruise company based on revenue.

► Conclusions/Recommendations

Positive business outlook driven by improving yields and occupancy is leading to considerable improvement in the financial profile of RCL. Besides, improvement in earnings power also leads to better access to credit markets. This makes its highly discounted bonds attractive. We assign a "GREEN LIGHT" rating to RCL.



Grab-and-Go™ THESIS

An investment in RCL is a play on growing demand for cruise travel worldwide. The company has grown globally to become one of the largest and most prominent cruise companies through organic and inorganic investments. Its success will depend on its ability to continue expanding its capacity to cater to more passengers and increase its yield while taking meaningful steps to reduce its costs and leverage.

Data as of 11/04/22 unless specified

Stock Price:	\$54.7	Debt/Equity:	1.67x	Interest Coverage Ratio:	NM
EBITDA (TTM):	-\$431.7	Debt/EBITDA (fwd):	7.3x	Interest Expense:	\$1.2B
EBITDA (fwd):	\$3,184	Market Cap:	\$13.9B	Cash/Cash Eq.:	\$1.6B
Total Debt:	\$23.3B	Enterprise Value:	\$35.7B	Debt/EV Ratio:	0.65x
Revenue (TTM):	\$7.22B	Operating Profit (TTM):	-\$1.81B	Free Cash Flow (TTM):	-\$3.42B
Insider Transactions (2022): Michael Bayley (Pres. & CEO, Royal Caribbean International) sold 27K shares, and Lisa Lutoff-Perlo (Pres. & CEO, Celebrity Cruises) sold 10.5K shares.					
OAS Spread:	727 bps	YTM:	11.22%	Spread/Turn Leverage:	1.53x

(Report based on 7.500% semi-annual fixed-rate bond with \$300M outstanding and maturing on 10/15/2027; CUSIP: 780153AG7)

 **SUMMARY OF BUSINESS**

Royal Caribbean Cruises was founded as Royal Caribbean International (RCI), formerly known as Royal Caribbean Cruise Line (RCCL) in 1968 in Norway. In 1997, RCI acquired Celebrity Cruises, a Miami, FL headquartered cruise company to mark the official beginning of Royal Caribbean Cruises Ltd. (RCL). The company continued its M&A stint in the years following its formation by acquiring several other prominent luxury and ultra-luxury cruise lines including British and Brazilian-based Island Cruises in 2000, Madrid-based Pullmantur Cruises in 2006, Monaco-based Silversea Cruises in 2018, and many others.

Currently, RCL owns and operates three global cruise brands namely, Royal Caribbean International, Celebrity Cruises, and Silversea Cruises. Additionally, it also holds a 50% JV interest in TUI Cruises GmbH which operates TUI Cruises and Hapag-Lloyd Cruises. In 2020, RCL announced the corporate identity rebranding and changed its official name to Royal Caribbean Group to account for the inclusion of global and partner brands. RCL ships are popular

across all age groups with the company providing a slew of fun activities to the travelers such as surfing, rock climbing, aqua theatre, etc. The company also caters to individuals across broad income range as evidenced by consumption of its services by guests with a median household income of over \$100,000. The table below depicts the lines of cruises that the company owns and their relevant capacity and size.

Cruise Lines	Total Ships	Est. Capacity (in berths)	Gross Tonnage (GT)
Royal Caribbean International	26	92,584	3.8M
Celebrity Cruises	13	32,280	1.4M
Silversea Cruises	11	3,742	260K
TUI Cruises	7	17,644	697K
Hapag-Lloyd Cruises	7	1,590	120K
Total	64	~147,840	~6.3M

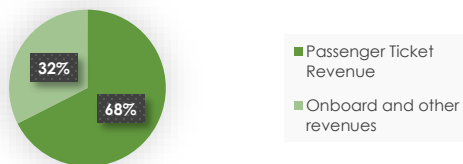
Source: [Company's IR website](#)

The company derives revenue primarily via two sources.

Passenger Ticket Revenues: The company earns revenue through the sale of passenger tickets. Additionally, the revenue is also earned from providing air transportation services to guests allowing them to make to and fro journeys from the ship. Passenger ticket revenue contributed 68% of total revenue in [Q3 2022](#).

Onboard and other revenues: The company also derives revenue from the sale of cruise add-ons not included in the cruise fare such as drink packages, shore excursions, Wi-Fi, etc. The company also generates revenue from third-party independent concessionaires by providing them rights to offer selected goods and services to guests that onboard ship. Onboard and other revenues contributed 32% of the total revenue in [Q3 2022](#).

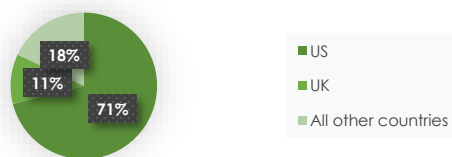
Revenue Mix - Q3 2022



Source: [Press Release – Q3 2022](#)

Based on reservation origination, passengers from the US contributed 71% of total passenger ticket revenue followed by passengers from the UK which accounted for 11% of total passenger ticket revenue in [Q3 2022](#).

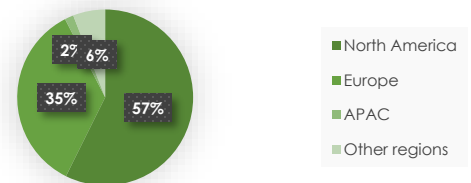
Passenger Ticket Revenue Mix by Geography - Q3 2022



Source: [Company's 10-Q](#)

The company provides a wide catalog of cruising destination choices for passengers. In Q3 2022, 57% of the total revenue (excl. revenue related to cancellation fees, vacation protection insurance, pre-and post-cruise tours, etc.) was derived from North America which includes destinations such as the US, Canada, Mexico, and the Caribbean. Europe contributed 35% to total adjusted revenue whereas the rest was accounted by destinations in APAC and other regions in Q3 2022 as shown below.

Revenues by Itinerary - Q3 2022



Source: [Company's 10-Q](#)



LB•LOGIC

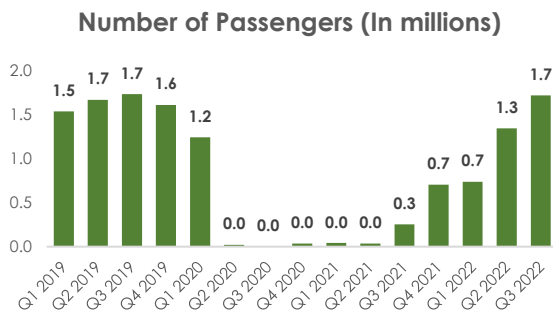
The cruise industry is seasonal in nature meaning that demand generally surges during the Northern Hemisphere's summer months and holidays. The company's broad destination catalog allowing passengers to capitalize on the summer season in Southern Hemisphere during winter in Northern Hemisphere helps it to mitigate the seasonal trends to some extent in the industry.



RECENT DEVELOPMENTS

The cruise industry was faced with significant headwinds stemming from the coronavirus pandemic. The imposition of stringent social distancing norms coupled with travel restrictions in order to contain virus left the whole industry

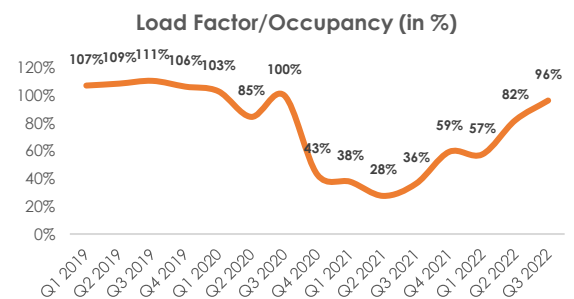
at an almost complete standstill mode in 2020 and in the first half of 2021. As per Cruise Lines International Association (CLIA), the number of cruise passengers plummeted by more than 80% YoY to 5.7M in 2020 causing the overall industry to record a cumulative loss of around \$77B. RCL was not immune to pandemic-led disruptions. The company's number of passengers carried tumbled from 6.5M in FY 2019 to 1.3M in FY 2020 and 1M in FY 2021 causing its top line to decline about 86% from \$11B in FY 2019 to \$1.5B in FY 2021.



Source: Company's Press Releases

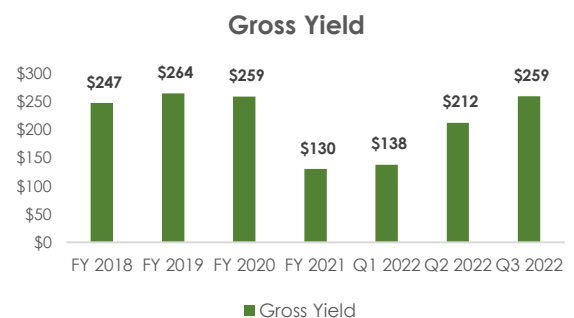
Despite headwinds in the recent past, it is worth noting that business environment in the cruise industry has improved significantly from the peak of the global pandemic. Global rollout of COVID-19 vaccines has helped consumer spending on discretionary services including travel and leisure to recover close to pre-pandemic levels. In fact, a 2022 Member Survey by Cruiseline.com and the booking app Shipmate concluded that 91% of the respondents were affirmative about taking a cruise in 2023. Another report by Arrivia, a travel loyalty provider indicated that 75% of its members mostly comprised of regular leisure travelers plan to opt for a cruise journey in the next two years. Much to the benefit of RCL, after challenging last two years, number of passengers carried and load factors/occupancy is seeming reverting to a more normalized level. In [Q3 2022](#), the company's load

factor increased to 96.3% from 36.4% in Q3 2021. However, on comparing with Q3 2019 occupancy of 111%, the company's Q3 2022 occupancy percentage remains well below signifying that further normalization is yet to be achieved. Investors must note that the occupancy percentage in excess of 100% is quite normal on cruise lines and implies that three or more passengers occupying some cabins.



Source: Company's Press Releases

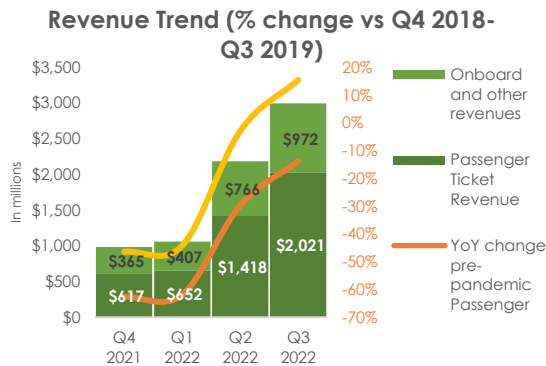
Like occupancy, gross yield, calculated by dividing total revenue by Available Passenger Cruise Days (APCD), increased from \$130.2 in FY 2021 to \$258.8 in Q3 2022. Still, it remained short of FY 2019's gross yield of \$264.3. The management projects yield to continue to increase in the first half of 2023 as further normalization is achieved.



Source: Company's Press Releases

In [Q3 2022](#), the company reported \$3B in total revenue as compared to \$457M in weak Q3 2021. When compared with Q3 2019, the revenue was

down 6% from \$3.2B. While the capacity measured as APCD reached 11.6M in Q3 2022 as compared to 10.7M in Q3 2019, the revenue was negatively impacted by lower occupancy and yield as discussed already.



Source: Company's Press Releases

The management is experiencing accelerating demand for sailings in 2023. In fact, the company recorded twice more booking volume in Q3 2022 for 2023 sailings than in Q2 2022. Booking volume in Q3 2022 for 2023 sailings was also significantly higher than the booking volume for 2020 sailings in Q3 2019. As a result of robust demand pipeline, the company expects to generate \$2.6B in total revenue in Q4 2022, translating into a growth rate of 3% relative to Q4 2019. The management also projects to return to overall historical occupancy and yield levels by late spring of 2023.

"While 2022 bookings remain strong and on pace to achieve occupancy targets, the most notable change over the past few months has been a substantial acceleration in demand for 2023 sails. We received twice as many bookings for 2023 sailings in Q3, as we did in Q2, resulting in considerably higher booking volumes than during the same period for 2019 sailings. As a result, all four quarters of 2023 are booked well within historical ranges at record prices, with bookings accelerating every week." - [Jason Liberty, CEO](#)



LB•LOGIC While last two years have remained challenging for the company as well as overall cruise industry, the recent signs including increasing yield and occupancy are indicating reversal to normalization. RCL being the largest cruise company worldwide, based on number of passengers carried is well placed to capitalize on pent-up demand and get back to its historical yield and occupancy levels.

It is also important to note that the company has begun its capacity expansion plans, which were temporarily halted during the pandemic by ordering new ships. It ordered a total of 10 ships which are not only expected to increase the company's overall capacity by 14% as compared to 2019 but are also projected to positively impact its yield. In fact, every 1% change in 2025 yield (post-completion of its currently planned capacity expansion) is forecasted to drive \$130M more in revenue and bring down operating costs by \$60M.

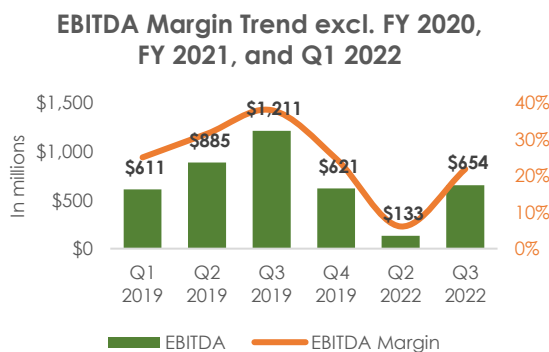
"We expect new ships as well as our relentless focus on the customer to drive additional yield benefits, cost efficiencies, and profitability of at least triple-digit EBITDA per APCD by '25. Every 1% improvement in yield in 2025 will result in \$130 million more in revenue, and every 1% of change in NCC, excluding fuel, will result in \$60 million benefit in operating costs." - [Naftali Holtz, CFO](#)

The table below details company's planned capital expenditure on new ships.

Cruise Lines	Total Ships Ordered	Expected Delivery Dates	Approx. Births
Royal Caribbean International	4	Q2 2024 Q4 2023 Q2 2025 Q2 2026	22,500
Celebrity Cruises	1	Q4 2023	3,250
Silversea Cruises	2	Q2 2023 Q2 2024	1,460
TUI Cruises	3	Q2 2024 Q4 2024 Q2 2026	11,100
Total	10	-	38,310

Source: [Company's 10-Q](#)

The company reported \$654M in EBITDA (operating income adjusted for depreciation & amortization) in [Q3 2022](#) as compared to -\$680M in Q3 2021 and \$1.2B in Q3 2019. On an adjusted basis i.e., after adjusting for non-recurring items, EBITDA increased from -\$704M in Q3 2021 to \$742M in Q3 2022. Operating margin i.e., EBITDA as a percentage of revenue stood at 22% in Q3 2022 as compared to 38% in Q3 2019. Operating margin benefited from increased occupancy and yield relative to the same quarter last year partially offset by transitory cost headwinds pertaining to fleet ramp-up and inflationary pressures relating to fuel and food costs. When compared with Q3 2019, operating margin was significantly down due to a 10% increase in gross cruise costs per APCD from \$184.1 in Q3 2019 to \$203.2 in Q3 2022 as a result of the aforementioned transitory cost headwinds.



Source: Company's Press Releases

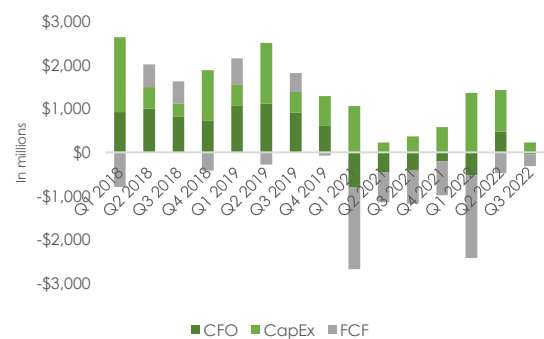


LB•LOGIC Fuel expense is one of the major operating expenses that the company has to bear as evidenced by its 16% contribution to total cruise operating expense. While increasing concerns around inflation exist, the company has partially hedged its fuel costs. In fact, company's fuel consumption is 64% and 50% hedged for 2022 and 2023.

CASH FLOWS GENERATION

RCL used \$45M in operating cash flows in [Q3 2022](#) as compared to \$403M in used operating cash flows in Q3 2021. The company generated \$912M in Cash Flow from Operations (CFO) in Q3 2019 and \$815M in CFO in Q3 2018 signifying that it has historically remained a cash rich company. The company made \$226M in capital expenditures in Q3 2022, significantly down from its historical average to improve its Free Cash Flow (FCF) profile amidst pandemic-led disruptions. While FCF is gradually improving on account of accelerating demand, we expect FCF to turn positive upon complete normalization.

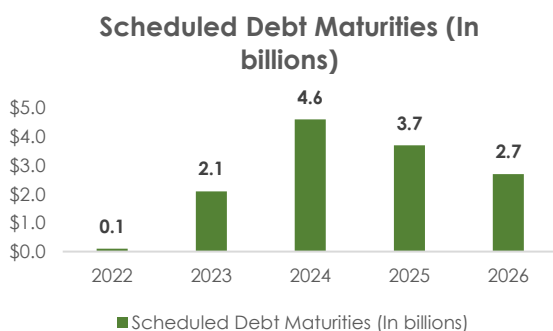
CFO & FCF Trend



Source: Company's Press Releases

 **LEVERAGE & DEBT MATURITIES**

Being a capital-intensive business with high fixed costs, RCL has a history of maintaining a large amount of debt on its balance sheet. The company tapped corporate debt market throughout the pandemic to leverage a low-rate environment and sustain the business continuity. Its total outstanding debt as of the recent quarter ended stood at \$23.3B which leads to a debt-to-equity ratio of 1.7x. While the company's leverage ratio seems elevated, it has been able to shift its near-term maturities further in the future through its recent debt refinancing program. It is visible from the graph below that the company has scheduled debt maturities of \$2.1B in 2023. Given the company's liquidity position of \$3.1B comprising of cash & cash equivalents and undrawn revolving credit capacity, it is well positioned to pay down its near-term debt obligations with cash on hand.



Source: [Company's Press Release – Q3 2022](#)

As indicated in the table on right, we have estimated company's EBITDA generating capacity for FY 2023 under two scenarios - a worst-case scenario as well as an optimistic scenario. In both scenarios, the company can comfortably pay interest on its obligations in terms of EBITDA. However, post interest, it will need to tap credit markets to refinance maturities and fund contractual capex (if it wishes to maintain current liquidity levels). We believe that

given the strong recovery in EBITDA in 2023 projected, the company will not have a difficult time trying to raise funds from the credit market and refinance its debt.

Particulars	FY 2023 (worst-case)	FY 2023 (best-case)
Available Passenger Cruise Days (APCD)	46,067,122	47,218,800
Gross Yield (F)	\$229.8	\$264.3
Total Revenue (In M\$)	\$10,587.4	\$12,479.9
EBITDA Margin	27.0%	32.0%
EBITDA (In M\$)	\$ 2,858.61	\$ 3,993.58
Total Debt (ST + LT) (In M\$)	\$ 21,763	\$ 21,763
Leverage Ratio (times)	7.6	5.4
Interest Expense (In M\$): 2023	\$ 1,420.0	\$ 1,420.0
Interest Coverage Ratio (times)	2.01	2.81
Capex	\$ 3,000	\$ 3,000
EBITDA - Capex	\$ (141)	\$ 994
EBITDA - Interest - Capex	\$ (1,561)	\$ (426)

Source: Company filings, LBIR estimates

RCL has several outstanding bonds trading in the market, however, we are interested in the 7.500% coupon rate bond maturing in 2027.

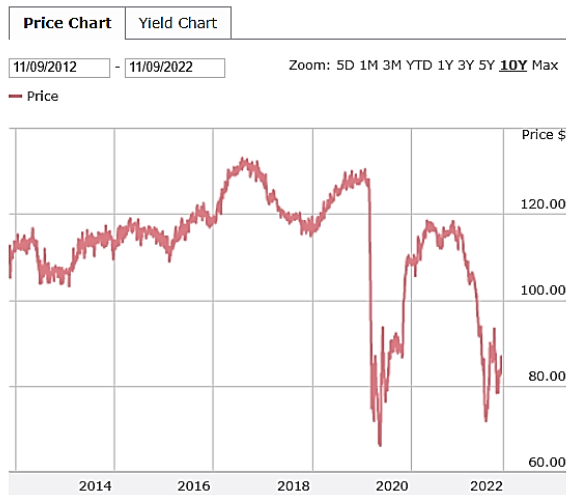
CUSIP	Maturity	Coupon	Current Yield	Pre-Pandemic Yield*	Bond Price
780153AG7	2027	7.500%	11.22%	3.35%	\$86.2

Source: [Finra-Markets](#). *pre-pandemic yield calculated on 02/24/2020

After declining over 30% since the onset of the pandemic in late February 2020, bond yield has shot up to 11.62%. We expect yield to narrow going forward as the business fundamentals improve thus helping fixed-income investors to benefit from capital appreciation. It is also worth noting that the bond has historically traded at a premium since its issuance. We believe that the bond comes with an attractive risk-reward as

investors could potentially benefit from both capital appreciation as well as current income.

Price/Yield Chart



Source: [Finra-Markets](#)



LB•LOGIC We like the fact that the company is guided by seasoned professionals with years of experience in the industry and within the company.



**CONCLUSION /
RECOMMENDATION**

The Covid-induced headwinds, including travel restrictions and strict social distancing norms, caused cruise operators to face significant financial headwinds in the last two years. However, the worst is behind for cruise lines. RCL leveraged a low-rate environment in the last two years to keep its operations afloat by raising debt. However, with business prospects now improving driven by increasing yield and occupancy, we expect company to continue paying its obligations and improve its financial profile in the coming quarters. Besides, RCL has sufficient liquidity cushion to support its near-term commitments and streamline its business operations further. We like the company's bond as it is trading at a significant discount to its past and holds strong-income potential. We assign a **"GREEN LIGHT"** rating to RCL's bond.



COMPANY MANAGEMENT

[Jason T. Liberty](#) is the group's CEO and President. He has been at the helm of RCL since 2005 serving in various senior-level executive roles in the past, including EVP and CFO. Prior to joining RCL, Mr. Liberty was a senior manager at KPMG LLP. He holds an M.B.A. from the UNC Kenan-Flagler Business School, and a degree in accounting and finance from the University of Miami School of Business and Kelley School of Business, respectively.

[Naftali Holtz](#) is currently serving as the group's CFO. He joined RCL in 2019 as the Senior VP of Finance. Prior to working for RCL, Mr. Holtz was the Managing Director and Head of Lodging and Leisure Investment Banking at Goldman Sachs. Before Goldman Sachs, he served as an officer in the Israeli Air Force. Mr. Holtz holds a B.S. degree in computer science and economics from Tel Aviv University and an MBA from the University of Chicago Booth School of Business.

Bond Details for RCL's 7.500% 2027 Senior Unsecured Notes (RCL)

Bond Detail

Lookup Symbol:

ROYAL CARIBBEAN CRUISES LTD

[+ ADD TO WATCHLIST](#)

Coupon Rate	Maturity Date	Symbol	CUSIP	Next Call Date	Callable
7.500%	10/15/2027	RCL.GF	760153AG7	—	—
Last Trade Price	Last Trade Yield	Last Trade Date	US Treasury	Yield	—
\$86.80	11.037%	11/04/2022	—	—	—

[Trade History](#)

Price/Yield Chart



Classification Elements

Bond Type	US Corporate Debentures
Debt Type	Senior Unsecured Debenture
Industry Group	Industrial
Industry Sub Group	Service/Leisure
Sub-Product Asset	CORP
Sub-Product Asset Type	Corporate Bond
State	—
Use of Proceeds	—
Security Code	—

Special Characteristics

Medium Term Note	N
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Issue Elements

Offering Date	10/08/1997
Dated Date	10/14/1997
First Coupon Date	04/15/1998
Original Offering*	\$300,000.00
Amount Outstanding*	\$300,000.00
Series	—
Issue Description	—
Project Name	—
Payment Frequency	Semi-Annual
Day Count	30/360
Form	Book Entry
Depository/Registration	Depository Trust Company
Security Level	Senior
Collateral Pledge	—
Capital Purpose	—

*dollar amount in thousands

Credit and Rating Elements

Moody's® Rating	B3 (08/08/2022)
Standard & Poor's Rating	B (02/25/2021)
TRACE Grade	High Yield
Default	—
Bankruptcy	N
Insurance	—
Mortgage Insurer	—
Pre-Refunded/Esrowed	—
Additional Description	Senior Unsecured Debenture

Put & Redemption Provisions

Call Date	Call Price	Call Frequency
—	—	—

Put Date	Put Price	Put Frequency
—	—	—

Bond Elements

Original Maturity Size*	300,000.00
Amount Outstanding Size*	300,000.00
Yield at Offering	7.62%
Price at Offering	\$98.59
Coupon Type	Fixed
Esrow Type	—

*dollar amount in thousands

Source: Finra-morningstar

Debt Ratios

	2017	2018	2019	2020	2021
DEBT/EQUITY	0.29	0.50	0.34	1.06	1.07
DEBT/ENTERPRISE VALUE	0.23	0.33	0.26	0.57	0.55
TOTAL DEBT (IN MILLIONS USD)	7539.5	10002.2	9600.7	18919.7	21090.3

Credit Data

	2017	2018	2019	2020	2021
REVENUE (MILLIONS USD)	8777.8	9493.8	10950.7	2208.8	1532.1
EBITDA (MILLIONS USD)	2695.3	2928.5	3328.6	-3322.3	-2571.5
DEBT/EBITDA	2.80	3.42	2.88	NM	NM
DEBT/EBIT	4.32	5.28	4.61	NM	NM
INTEREST COVERAGE	8.98	8.78	8.15	NM	NM
ASSET COVERAGE	2.44	2.08	2.31	1.48	1.25
FREE CASH FLOW (MILLIONS USD)	2310.4	-180.9	691.7	-5696.8	-4107.5

Yield Data

	2017	2018	2019	2020	2021
OPTION ADJUSTED SPREAD (BPS)	146	265	156	500	302
YIELD TO MATURITY (BPS)	386	531	342	565	437
SPREAD PER TURN LEVERAGE	1.38	1.55	1.19	NM	NM

Equity Data

	2017	2018	2019	2020	2021
STOCK PRICE (\$/SHARE)	120.2	96.4	134.6	74.8	77.6
MARKET CAP (MILLIONS USD)	25686.2	20165.6	28120.9	17767.6	19780.6
SHARES OUTSTANDING (MILLIONS)	213.7	209.2	209.0	237.5	255.0

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