

S&P Global
Market Intelligence

Sleep Number Corporation

NasdaqGS:SNBR

Earnings Call

Thursday, March 12, 2026 12:30 PM GMT

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Call Participants

EXECUTIVES

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Robert Kenneth Griffin
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Presentation

Operator

Welcome to Sleep Number's Fourth Quarter and Full Year 2025 Earnings Conference Call. [Operator Instructions] As a reminder, this call is being recorded today, Thursday, March 12, 2026. This conference call will be available on the company's website, ir.sleepnumber.com. Please refer to today's news release to access the replay.

On today's call, we have Linda Findley, President and CEO; and Amy O'Keefe, Chief Financial Officer of Sleep Number. Before handing the call over to the company, we will review the safe harbor statement. The primary purpose of this call is to discuss the results of the fiscal period ending on January 3, 2026.

Commentary and responses to questions may include certain forward-looking statements. These forward-looking statements are subject to a number of risks and uncertainties outlined in the company's earnings news release and discussed in some detail in the annual report on Form 10-K and other periodic filings with the SEC. The company's actual future results may vary materially.

In addition, any forward-looking statements represent the company's views only as of today and should not be relied upon as representing its views as any subsequent date. The company specifically disclaims any obligation to update these statements.

Please also refer to the company's news release and SEC filings for a reconciliation of certain non-GAAP financial measures and supplemental financial information included in the news release or that may be discussed on this call.

I will now turn the call over to Linda Findley, Sleep Number's CEO.

Linda A. Findley

President, CEO & Director

Thank you, Rob, and good morning, everyone. Before I begin, I want to welcome Amy O'Keefe, our new CFO. After an extensive search, she joined us in December and brings with her decades of experience leading operational and financial transformations across public and private companies. Her focus has been on streamlining our business operations and strengthening our capital structure to support our turnaround strategy. You'll hear more from her shortly.

In today's call, I will cover 3 things: First, how we're executing on our strategy, both for growth and cost cutting; second, why we believe that our new marketing and product strategies are working; and third, what we're doing to manage liquidity and the capital structure.

First, on delivering our strategy. 2025 was a pivotal year for Sleep Number as our reshaped team drove big turnaround changes at every level of the company, from retail and corporate operations to marketing strategy and the rapid development of our new product line. Importantly, we delivered on the guidance we provided in our last call.

Full year net sales were \$1.41 billion, in line with our guidance despite reduced marketing spend and lower traffic throughout the year. Adjusted EBITDA was \$78 million, exceeding our guidance of \$70 million. Our use of cash for 2025 was \$18 million compared to the \$50 million guidance.

For the full year, pro forma adjusted EBITDA margin was approximately 9%, and Amy will discuss how we plan to improve margins further in 2026. The long-term benefit to adjusted EBITDA margin comes from 2 places: First, the renewed growth from our product line redesign; and second, the significant cost savings we have already done and will continue to do this year.

We radically reset the business by lowering our fixed cost structure and built a leaner, more nimble organization. We removed more than \$185 million of annualized costs and have identified another \$50 million of annualized fixed costs that we are executing on now. We are still in full turnaround mode, and our progress in 2025 doesn't change the fact that we still have hurdles to clear in 2026.

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We saw the same pressures as the rest of the industry in January and early February from severe weather and macroeconomic impacts. We had 236 stores that were closed for at least 1 day in the month of January, and therefore, sales at the start of the year were significantly down. We adjusted our marketing spend and strategy to lean in when things improved, and we have seen sequential improvement into February and March, driven mostly by our product launch.

That brings us to our next point about why we believe our product and marketing strategies are working and will carry us through the next phase of the turnaround. We launched our first new bed and a new adjustable base in January and the response from customers has been fantastic. The ComfortMode mattress priced under \$1,600 gives us access to a new group of customers while maintaining personalized comfort as the core of the experience.

As of the end of February, sales are 3.5x what we expected and nearly twice all the sales of all 3 C Series beds that this bed replaces. In addition, we are seeing very strong attach rates for adjustable bases and bedding. The success of the first ComfortMode bed is an important indicator for the rest of the portfolio we announced this morning as it's built off the same principles and the same value proposition.

We listened to both current and prospective customers and built a product line that addresses their most critical needs of comfort, durability and value. We also refer to the core of what only Sleep Number can offer, personalized comfort, adjustability, smart technology and temperature benefits, the only bed in the industry that bed owners can fully control whenever they want.

It's comfort that shifts with you night after night. With 4 new beds available in-store and online starting March 23, Sleep Number beds will now reach a broader set of consumers in the premium category. We are leveraging years of innovation and experience servicing luxury materials, features, comfort, temperature management and adjustability at better price points than ever before.

This enabled us to build more value per dollar in each bed, protecting our margins while also achieving a lower price point for today's premium customer. In addition to these innovative new beds, we are also making it easier to find the right bed for you by simplifying the buying experience in-store and online.

With this launch, we are reducing our core lineup from 12 mattresses to 7, organized into 3 clear collections. First, ComfortMode is our new entry point to the brand. It delivers personalized comfort and temperature management controlled without an app, all at an accessible price.

In January, we launched the 10-inch ComfortMode bed, and now we're adding an 11-inch model called ComfortMode Lux with 3-zone comfort layer and advanced temperature materials starting at just \$2,099 for a Queen. Second, the ComfortNext line, starting at \$2,999 for a Queen, is our biggest innovation in the launch with 3 all-new beds, including 2 that feature our new Tri-Brid design.

We are the first company to combine foam, advanced temperature materials and micro coils on top of air adjustability to deliver improved comfort, pressure release and durability with personalized comfort we are known for. These exceptionally luxurious beds will be the start of our smart technology in our portfolio and will track and improve your sleep at incredibly competitive price points.

Third, we have our Climate Collection, starting at \$5,499 for a Queen, and it includes our existing ClimateCool and Climate360 beds that differentiate with true active temperature management. This category represents the ultimate and luxurious comfort. When combined with the base, it remains the only line of mattresses on the market that offers personalized firmness, smart technology, adjustability and active temperature control, all in one bed.

In fact, our temperature programs on Climate360 result in up to 52 more minutes of restful sleep per night. But the new product alone isn't what gives us confidence. The marketing changes we have made are substantial.

As I've said before, we can do more with the dollars we spend, and that is happening. First, we rebuilt our marketing foundation and modernized how we identify and attract customers. As a result, we saw meaningful improvements throughout 2025 in our funnel metrics. Our marketing into Q4 maintained this

improvement, and we're seeing accelerated year-over-year improvement in cost per acquisition so far in 2026.

Second, we also started refreshing our creative and messaging last year in social and digital channels. We also recently launched our first new commercial in more than 2 years with a dedicated ComfortMode spot, where recent performance has now surpassed our prior campaign and current competitive benchmarks. The combination of this work is showing up in our annual brand tracker that we completed in January just before we announced our partnership with Travis Kelce.

Despite overall pressure in the industry, we saw significant increases in every aspect of Sleep Number's brand. Brand consideration among premium shoppers grew 10% and achieved the highest consideration in the premium category. We also saw the highest levels in 6 years of critical consideration drivers, including value, quality, aspirational fit, comfort and individualized comfort.

Now it's up to us to build on that success and turn that brand strength into sales growth. The marketing changes are still underway, and you will continue to see new creative, new strategies and our partnership with Travis Kelce come to life.

Finally, let's talk about liquidity and capital structure. It isn't news to anyone that we need to fix our capital structure. I knew that when I joined the business less than a year ago, and it remains our top priority. Three things hit us particularly hard in the end of 2025 and beginning of 2026. The industry-wide softness we already spoke about, our work to clear out inventory as we roll out the new product line and our continued careful management of marketing spend as we lap a very high inefficient spend of Q1 last year.

This puts pressure on our liquidity, and we are implementing a plan to address this. As part of that plan, we hired Guggenheim Securities to evaluate the inbound interest we have received and advise on other opportunities to refinance our credit facility as we shape Sleep Number back into a profitable growing company. Amy will talk about this in more detail.

Before I turn the call over, I want to thank our team members. Delivering a product reset of this scale in just 10 months, work that typically takes more than 2 years, reflects a new level of speed, collaboration and execution across the company. Our work is focused on delivering better value for our customers, shareholders and team members and on bringing Sleep Number back to profitable growth.

With that, I'll turn it over to Amy.

Amy K. O'Keefe
Executive VP & CFO

Thank you, Linda, and good morning. I joined Sleep Number in mid-December because I view it as a company whose intrinsic value far exceeds its market capitalization.

While Sleep Number is in the midst of a turnaround, the value of its underlying assets is undeniable, leading brand recognition, differentiated product and the tens of billions of hours of sleep data that validate the benefit our beds have on the quality of your sleep. We have a lot of work ahead of us, but fortunately for me, Linda and the team have already done a significant amount of the hard work to put the company on a path to profitable growth.

One, rightsizing the cost structure to a lower revenue base by executing on \$185 million of annualized cost reductions with line of sight to an incremental \$50 million to be executed in 2026. Two, executing in record speed for Sleep Number on a completely new line of products that Linda described, which we are launching on March 23. And three, modernizing our marketing engine with new leadership, new creative, new channel-specific media strategies and a new partnership with Travis Kelce to strengthen the brand and drive top line growth.

This is a pivotal time for the company, and I'm excited to partner with Linda and add my deep turnaround experience to unlock value for our shareholders. I want to thank the team for their very warm welcome and efforts to get me up to speed quickly.

Now let's get into Q4 results, which were better than expected. Net sales were \$347 million in Q4 or 8% below the same period in the prior year. As a reminder, fiscal year '25 benefited from a 53rd week, which favorably impacted year-over-year results by approximately 660 basis points.

Notably, the performance trend across the year improved sequentially, while the number of stores decreased by 40, exiting the year with 600 stores. And as Linda noted, the impact of our improved marketing offense continues to drive efficiencies.

Gross profit margin was 55.6% in the quarter, a 430 basis point decline versus the prior year, primarily driven by a \$9.6 million nonrecurring inventory obsolescence charge associated with our new product launch and the impact of unit deleverage and higher tariffs. Excluding the impact of the inventory charge, adjusted gross profit margin was 58.4%.

Operating expenses in the quarter were \$197 million, down 9% year-over-year, excluding restructuring and other nonrecurring costs. The reduction was driven by ongoing cost savings initiatives to rightsize the fixed cost base and lower variable selling expenses.

Media investments were comparable to the fourth quarter of the prior year despite a 53rd fiscal week. Adjusted EBITDA was \$19 million, down \$7 million versus the same period last year.

For the full year, net sales were \$1.41 billion, consistent with our expectations, but down 16% versus the prior year. Full year gross margin was 59%, and down 60 basis points year-over-year, and aligned with the guidance of 60% that we shared last quarter when excluding the impact of the fourth quarter inventory charge.

Operating expenses for the full year were \$824 million, a \$136 million reduction from the prior year, excluding restructuring and other nonrecurring costs. On an annualized basis, we've executed approximately \$185 million of cost savings initiatives, which gives us an estimated \$50 million tailwind as we head into 2026.

As Linda mentioned, 2025 adjusted EBITDA was \$78 million, exceeding our most recent outlook of \$70 million. Importantly, for the full year, pro forma adjusted EBITDA margin was approximately 9%, a 200 basis point improvement versus the prior year.

Turning to the balance sheet and cash flow. We ended the year in full compliance with our credit agreement and debt covenants. Total liquidity, including cash and revolver capacity, was \$58 million at year-end, well above the amended \$30 million covenant floor.

Full year free cash flow was a use of \$18 million, which was just over \$30 million favorable to expectations. However, it was unfavorable by \$21 million compared to the prior year, primarily due to top line pressure and nonrecurring cash restructuring costs.

Capital expenditures of \$14 million were down \$9 million compared to the prior year. Looking ahead to 2026, as Linda mentioned, January demand was soft versus last year and our internal expectations. As we planned, the media investment in January was down significantly year-over-year and reallocated to after the launch of our new products when the return on investment is likely to be much higher.

Moving into February, we saw a sequential improvement in performance during the President's Day event as we launched ComfortMode. Not only were we pleased with ComfortMode's sales performance, but gross margin is well above our legacy opening price point beds. This provides another proof point that we can regain competitive positioning in the premium opening price point as we planned. We're excited to launch the rest of our product line in late March.

Given the magnitude of the change that we are executing in 2026 as part of our turnaround plan, we will not be providing guidance today. However, I will provide some indications of our performance expectations for the balance of the year.

I will also note that we are planning cautiously to ensure that our cost base and our liquidity planning are set appropriately as revenue ramps sequentially over the balance of the year. While we expect Q1 net sales to decline in the high teens because of the softness we saw at the beginning of the year, with the full

impact of the new product launch in the second quarter along with an increase in year-over-year media spend, we expect a significant improvement in year-over-year revenue performance in Q2.

We further expect double-digit sales growth in the second half with the full benefit of; one, new products; two, new creative assets; and three, marketing reach with our new strategic partner, Travis Kelce. As a result of cost savings initiatives and the expected ARU improvement from new products, adjusted EBITDA for the full year is expected to increase in the high teens to mid-20s percent range year-over-year, and we expect free cash flow to be positive.

Lastly, but importantly, and as Linda mentioned, while we are seeing improvement in the business, the softness from the start of the year and the clearance of our existing products have put pressure on our liquidity and covenants. We are actively implementing a plan to address this as further detailed in our Form 10-K, and have engaged an advisory bank, Guggenheim Securities, to help us.

We will continue to monitor our liquidity position and covenant compliance and we'll work with our advisers to address our credit facility and evaluate inbound interest and other opportunities to improve the company's liquidity, balance sheet and financial flexibility.

With that, I will turn it to the operator for Q&A.

Question and Answer

Operator

[Operator Instructions] Your first question today comes from the line of Dan Silverstein from UBS.

Daniel Arnold Silverstein

UBS Investment Bank, Research Division

Congrats on the announcement of the product launch. First question is just on that. So with the new product launches, what were the main pain points you were trying to address?

And then the ComfortMode product replaced its predecessor at a higher margin. How will this new announcement today, how will these new beds reset the impact on ASPs, cost per bed and margins going forward?

Linda A. Findley

President, CEO & Director

Sure. Yes. So I'll start on both of those, and then I'll have Amy jump in as well. So first of all, thanks very much for the congratulations and the questions.

So pain points, first of all, was, going back to exactly what we talked about before, customers right now, when you think about the people who are most interested in the premium category, we really wanted to expand our audience to be able to serve our existing customer base and then broaden into younger demographics and additional demographics that would want access to the benefits of a Sleep Number bed.

So we focused on comfort, value and durability in everything that we built. But one of the advantages that we have is all of the investments that Sleep Number has made in innovation over the years really came to pay off in this particular product line, where we were able to take incredibly luxurious materials, temperature management materials and other new innovations around comfort, including foam and our new micro coils that we're putting into 2 of our new beds, to really say we're going to take luxury materials and bring them to a much more accessible premium price point.

So what this allows us to do is both more directly address comfort and improve sleep from our past innovation history in a better price point for our customers. And there's a much clearer step-up strategy too now. So there's the beds that don't require an app that allow people to experience the brand for the first time. And then you can move into some of our smart technology and our other beds that we're rolling out today or introducing today.

In that concept, we built these beds for manufacturability. And one of the challenges, and you've heard us say in the past is that in order to really maintain our margin, we were kind of selling up the line. We have some incredible beds, and we still have our Climate Series beds that we mentioned today, they are doing extremely well.

But we wanted to make every bed in the line the same margin and a strong margin profile in order to make sure that our sales team could really sell the best bed for whoever the customer is and not have to worry about the impact to the margin profile.

So our ComfortMode bed is as margin accretive as our Climate360 beds, and that allows us to serve the customer more clearly, more directly and also protect our margins at the same time. So sort of 2 -- double answers there to your questions, but we are really excited about this launch, not only for what it means for customers, but what it does mean for our margin profile.

Anything you want to add, Amy?

Amy K. O'Keefe

Executive VP & CFO

And I'll just jump in on gross margin. We are expecting, as I mentioned, a sequential increase in ARU as these products transition out and the legacy products are discontinued.

The exciting part for a finance person is that gross margin, if I just look at the ComfortMode bed compared -- and this is just the one SKU that we've already launched, which is performing, as Linda mentioned, well above our expectations, 3.5x the plan, the best part of that for me is the gross margin.

If I just look at that compared to the 2 beds in the C Series that it's replacing, it's a 10 percentage point gross margin improvement compared to the prior year. So it's really exciting not only for early indications of the performance, but also the margin profile of the business.

Daniel Arnold Silverstein

UBS Investment Bank, Research Division

Very, very helpful. And just one quick follow-up. Could you just touch on the major sources of the \$50 million of additional savings you think you can drive this year? And will there be any further clearance activity as we nudge up to March 23?

Amy K. O'Keefe

Executive VP & CFO

Sure. And so last year, Linda and the team, as we mentioned, took a significant amount of cost out of the business, annualized basis, it was \$185 million. And I think those were -- forgive the term, but sort of blunt force, right? The team needed to move fast in order to protect our liquidity position.

I think over the last several months, a quarter or more, we have been looking, I think, more surgically at where opportunity remains to take costs out of the business. And at a super high level on the incremental annualized \$50 million, there's a lot of logistics, delivery, last mile, labor model resets, and we're still taking a look at our corporate overhead structure. And so I think those things -- those are the big activities in the \$50 million.

Linda A. Findley

President, CEO & Director

And importantly, just to add to that, all of the \$50 million has already been identified, we're already executing on it, and it is all fixed costs.

Amy K. O'Keefe

Executive VP & CFO

Yes, all fixed costs.

Operator

Your next question comes from the line of Bobby Griffin from Raymond James.

Robert Kenneth Griffin

Raymond James & Associates, Inc., Research Division

Congrats on the first product launch there. I guess, first for me, I think the release or maybe the prepared remarks called out March 23 as the date, but like what's the phasing as we look at getting these -- the 6 new beds now that you talked about on the floors and kind of across the portfolio, how is that phasing work throughout the year? And if you can, just give us a date that you feel the floors will be largely set and the stores will look as you want them to be?

Linda A. Findley

President, CEO & Director

So I'll jump in on that. First of all, the -- all 4 -- so we launched 1 bed earlier this year. That was the ComfortMode bed, the first bed that we launched. There are 4 new beds plus the base -- sorry, we launched the first new bed and base in January.

There are 4 new beds and a new base that are all going to be available for purchase starting on March 23. Those are the ones that we announced today. And that completes the product reset, plus, of course, the existing Climate Series that we have, Climate360, ClimateCool, that are already obviously on floor.

So all the beds will be available for purchase starting on March 23, and we will start setting floors on March 23. So we will start with our first highest volume stores and most of the stores will be set by mid-April. Then we'll have a few more stores that might roll out into May. But for the most part, the key stores will be -- will all be set by mid-April.

Robert Kenneth Griffin

Raymond James & Associates, Inc., Research Division

Okay. So basically, floor will be in good shape for the Memorial Day holiday. That's what I was getting at.

Linda A. Findley

President, CEO & Director

Absolutely. That is exactly what we're planning for. Yes.

Robert Kenneth Griffin

Raymond James & Associates, Inc., Research Division

Okay. That's very encouraging. And I guess, just on -- I understand the dynamics around not wanting to give the guide. But just one clarification, Amy, and then maybe a little help. But the EBITDA number that -- the growth that you're referencing, that's versus the reported number in '25, not the pro forma number?

Amy K. O'Keefe

Executive VP & CFO

That's correct. That's correct. Of the \$78 million adjusted EBITDA base. High teens to mid-20s percent range improvement.

Robert Kenneth Griffin

Raymond James & Associates, Inc., Research Division

Yes. Okay. Perfect. And then if that comes to fruition and you guys are able to deliver that, would that translate into positive free cash flow for the year? I understand this business typically has really good cash flow metrics, but it would?

Amy K. O'Keefe

Executive VP & CFO

Absolutely.

Operator

Your next question comes from the line of Peter Keith from Piper Sandler.

Unknown Analyst

This is [Sarah] on for Peter. First, just on marketing spend, given the meaningful reductions in 2025, how are you guys thinking about investment in '26? Should we expect those marketing dollars to start trending back up, particularly as the new product lineup rolls out? Or is current spend kind of sufficient to drive demand?

Linda A. Findley

President, CEO & Director

Right. So as we spoke about before, what we're actually doing in 2026 compared to 2025 is you'll see marketing held flat as total spend in 2026 over 2025. But what that means in reality because 2025 had

very high spend in Q1, much lower spend in Q2 and Q3 and then moderated sort of relatively flat spend in Q4, that was the shape of the curve in 2025, someone compared it to a square root at one point.

So when you look at 2026, what we're actually doing is evening that spend out across the entire year. So you don't have any peaks and valleys of spend that can create inefficiencies, and so what that means in reality is Q1 is actually down because, again, Q1 spend last year was extremely high before I joined the business.

So Q1 spend is slightly down. Q2, 3 and 4 will be up year-over-year relative to last year because of the fact that we're evening out the spend. So you are going to see increased spending, as Amy mentioned, in line with our full rollout of the products.

Amy K. O'Keefe

Executive VP & CFO

And the only thing I'd add is that Q2 is up higher, right?

Linda A. Findley

President, CEO & Director

Yes, correct.

Amy K. O'Keefe

Executive VP & CFO

The back half by quarter is roughly flat, but the flip flop is really between Q1 and Q2.

Unknown Analyst

Okay. Very helpful. And then just a quick follow-up on the clearance of existing products. Was that primarily greater markdowns than expected? And then did you say that was expected to be a headwind in 1H with those newer products and on the reduction?

Amy K. O'Keefe

Executive VP & CFO

Sorry, are you finished with your question?

Unknown Analyst

No. Yes, that was...

Amy K. O'Keefe

Executive VP & CFO

Got you. We are going to see unquestionably some margin pressure in Q1. So this new product rollout is monumental compared to other product launches in the company's history. I mean, I think we say we haven't seen such significant change in a decade, and so with a hard stop, and we definitely didn't want to do a rolling change of these products because we wanted to get the revenue ramp and the margin benefits as early as we possibly could.

So we're definitely going to be taking some discounting and hits to margin in Q1 because of the hard stop and the softness that we talked about in January and February. We had a little bit more inventory hangover than we would have liked, and we're working through that in the month of March.

Linda A. Findley

President, CEO & Director

Yes. The only thing I would add to that is it was -- you were asking if it was expected, and we did expect to do some clearance work. So I think that's fairly standard in a launch of this magnitude.

One of the things that we are excited about with what we've seen from the launch of ComfortMode is this -- it outsold 3.5x our plan, but it's also outselling all 3 of the beds it replaces by 2x. So you get leverage with volume as well.

And that's a big part of what we're thinking about long term is, of course, the volume play and how we can increase leverage that way, too. So there's trade-offs in everything that we're looking at, but this one was expected.

Operator

And as we have no further questions, ladies and gentlemen, this will conclude today's question-and-answer session. I'd now like to turn the conference back over to Linda for any closing remarks.

Linda A. Findley

President, CEO & Director

Thank you very much for your time today. We're excited for our customers to experience our new product lineup later this month, and we remain very focused on the key elements of our turnaround strategies as we actively address our capital structure.

I look forward to updating you on our continued progress in the coming months. As always, if you have any questions, please contact us directly.

Operator

This concludes today's conference call. Thank you all for joining. You may now disconnect.

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