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FINAL TRANSCRIPT

Cascades Canada ULC

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CORPORATE PARTICIPANTS

Jennifer Aitken
Cascades Canada ULC — Director, Investor Relations

Mario Plourde
Cascades Canada ULC — President and CEO

Allan Hogg
Cascades Canada ULC — CFO

Charles Malo
Cascades Canada ULC — President and COO, Containerboard Packaging

Jean-David Tardif
Cascades Canada ULC — President and COO, Tissue Group

Jérôme Porlier
Cascades Canada ULC — President and COO, Specialty Products

CONFERENCE CALL PARTICIPANTS

Sean Steuart
TD Securities — Analyst

Hamir Patel
CIBC Capital Markets — Analyst

Matthew McKellar
RBC — Analyst

Zachary Evershed
National Bank — Analyst

Frédéric Tremblay
Desjardins — Analyst

PRESENTATION

Operator

[Operator Remarks in French]

Good morning. My name is Sylvie (phon), and I will be your conference Operator today. At this time, I would like to welcome everyone to the Cascades Third Quarter 2023 Financial Results Conference Call. Note that all lines are currently in a listen-only mode.

After the speakers' remarks, there will be a question-and-answer session.

I will now pass the call over to Jennifer Aitken, Director of Investor Relations for Cascades. Ms. Aitken, you may begin the conference.

Jennifer Aitken — Director, Investor Relations, Cascades Canada ULC

Thank you, Sylvie. Good morning, everyone, and thank you for joining our third quarter 2023 conference call. We will begin with an overview of our operational and financial results, followed by some concluding remarks, after which we will begin the question period.

Today's speakers will be Mario Plourde, President and CEO, and Allan Hogg, CFO. Also joining us for the question period at the end of the call are Charles Malo, President and COO of Containerboard Packaging; Jérôme Porlier, President and COO of Specialty Products; Jean-David Tardif, President and COO of Tissue Papers; and Luc Langevin, Senior VP of Corporate Services.

Before I turn the call over to my colleagues, I would like to highlight that certain statements made during this call will discuss historical and forward-looking matters. The accuracy of these statements is subject to risk factors that can have a material impact on actual results. These risks are listed in our public filings.

These statements, the investor presentation, and the press release also include data that are not measures of performance under IFRS. Please refer to our Q3 2023 investor presentation for details. This presentation, along with our third quarter press release, can be found in the Investors section of our website. If you have any questions, please feel free to contact us after the session.

I will now turn the call over to our CEO. Mario?

Mario Plourde — President and CEO, Cascades Canada ULC

Thank you, Jennifer, and good morning, everyone. Before discussing our results, I would like to announce that we have some sad news this morning. Mr. Bernard Lemaire, founder of our company, died yesterday. Even though Bernard has retired from Cascades several years ago, he remained the heart and the soul of the Company and never ceased to inspire us.

Cascades will be mourning for this great man and will celebrate his memory and exceptional achievements. On behalf of all Cascades employees, I would like to offer our most sincere condolences to the Lemaire family and Bernard's loved ones.

Beginning with the call. We are pleased with our strong Q3 consolidated results and, in particular, the record quarterly performance of our Tissue Papers segment. On a consolidated basis, sales increased 2 percent, year over year, while adjusted EBITDA of $161 million rose 45 percent from the prior year.

In both cases, strong results in the Tissue Papers segment were the main driver as benefits from our strategic action yield results. More broadly, year-over-year top line growth benefitted from strong volume in Containerboard, which includes Bear Island and a favourable foreign exchange for all of our business segments.

While our packaging businesses saw lower average selling prices, following the index decrease, the impact at that consolidated level was partially offset by higher selling price in Tissue. The year-over-year EBITDA improve (sic) was also driven by stronger Tissue results and lower raw material prices for all segments. Freight and energy costs were lower, but benefits were largely offset by higher production costs.

Sequentially, sales increased 2.6 percent. This was driven by higher volume in Containerboard and a more favourable mix in Tissue Papers. Selling prices were lower for both our Containerboard and Tissue Papers segments.

EBITDA increased 14 percent sequentially. This was driven by improved volume in Containerboard and Tissue Papers and lower overall production costs. Raw material prices were headwinds for our packaging businesses but were tailwinds for our Tissue operation.

On the raw material side, highlighted on Slide 5 and 6, the Q3 average index price for OCC decreased 46 percent year over year, but increased 26 percent from Q2. The OCC market saw a more active export market in Q3 with increased volume to Asia, leading to some pressure on pricing.

Seasonal fibre generation remained good, albeit at a slower pace than recent years. We have had no problems supplying the needs of our operation, which have increased with the ramp-up of Bear Island.

Average Q3 index prices for white recycled paper grades decreased 22 percent, sequentially, and 42 percent from the prior-year levels. We saw favourable market dynamics over Q3, with the index prices continuing to reduce, but at a slower pace than previous quarters.

Similar trends were seen with the virgin pulp. The hardwood pulp index decreased 20 percent, sequentially and 37 percent year over year, while softwood pulp index prices decreased 14 percent from Q2 and 28 percent year over year.

Market conditions have begun to reverse, following more demand from China and a scheduled downtime and closures announced at multiple mills in North America. Notwithstanding these changes in the market conditions, the material has been readily available for our mills. Near-term market dynamics will be influenced by whether or not Asian markets continue supporting both export activity and pricing.

Moving now to the results of each of our business segments, as highlighted on Page 7 through 12 of the presentation.

Beginning with Containerboard, sequentially, sales increased 6 percent in Q3. This reflects higher volume due to usual seasonality and the addition of the volume from Bear Island. These were partially offset by the impact from lower average selling prices related to the index changes and the less favourable sales mix, given the greater weighting of the parent rolls.

The 8 percent increase in shipments reflects increases of 12 percent in parent rolls and 4 percent in converted product. Sequentially, converting shipments increased 4.3 percent in Canada, outperforming the 0.4 percent increase in the Canadian market. US converting shipments increased 1 percent above the 0.4 percent US market increase.

Q3 adjusted EBITDA of $101 million, or 17 percent on a margin basis, was 5 percent above the Q2 levels, reflected higher volume and lower operating costs. These were partially offset by lower selling prices and higher raw material and transportation costs.

The contribution of Bear Island improved sequentially but is still a negative contributor to our performance, given the mill is ramping up.

Year over year, sales and EBITDA both decreased by $2 million with the impact of lower selling prices, largely offset by higher volumes at the top line, while tailwind at the EBITDA level also included lower raw materials, energy, and transportation costs.

Year over year, shipments increased by 10 percent in Q3, reflecting a 14 percent increase in external parent roll shipments, largely related to the new Bear Island volume, and a 6 percent increase in converting shipments.

Specifically, converting shipments increased by 5.7 percent in Canada year over year, outperforming the 0.8 percent increase in the Canadian market. US converting shipments increased 9.5 percent, once again significantly outperforming the 4 percent of the US market decrease.

Continuing with our packaging business, Q3 sales levels in our Specialty Products segment decreased by 4 percent, sequentially, following lower volume in moulded pulp and cardboard products. Production challenges in our moulded pulp activity during the quarter are now resolved, and volumes are expected to be back to normalized levels in Q4.

EBITDA decreased by $3 million, sequentially, driven by lower realized spread in some subsegments, mainly due to product mix and lower volume.

When compared to the prior year, Q3 sales decreased by $11 million or 7 percent, driven by softer volume, primarily in cardboard, and lower selling prices in almost all subsegments. These were partially mitigated by a more favourable exchange rate.

EBITDA level decreased by $4 million year over year to $21 million in Q3, as benefits from higher realized spreads were more than offset by the impact from lower volume and higher production costs.

Moving now to our Tissue business, we've generated a solid quarterly EBITDA margin of 14.5 percent. This strong performance reflect benefits from favourable raw material pricing and recent wide-ranging commercial, operational, and strategic initiatives that include the repositioning of this segment's operational platform.

This repositioning includes closure of several facilities, all of which have now been completed. The decommissioning process is underway and on schedule with limited impact on our customers, thanks to good planning by our team and production being shifted to other plants.

Moving now to results. Sales were stable, sequentially, increasing 1 percent, which reflects 5 percent growth in converting side. This was partially offset by lower parent roll sales following the closure of our St. Helens-Oregon mill and higher integration within our own network.

The average selling price increased by 1 percent, driven by the lower proportion of parent rolls in the sales mix, the benefit of this partly offset by a lower average selling price in converted products that reflects a less favourable mix and lower prices with some key customers, due to contracted pricing model agreements. Approximately 50 percent of our retail volume are linked to such agreements.

Shipments were stable in Q2, reflecting a 5 percent increase in converted products and a 24 percent decrease in parent rolls, following the closure of the St. Helens mill.

Q3 EBITDA of $61 million, or 14.5 percent on a margin basis, improved $17 million or 39 percent from Q2. This increase was driven by benefit from lower raw material and freight and a decrease in fixed costs' level following the plant closure. These were partially offset by lower selling prices for the converted products and higher energy costs.

Year over year, sales rose 10 percent, with pricing and sales mix initiatives and a more favourable exchange rate contributing to the stronger performance.

EBITDA increased $57 million from the prior-year period. This was driven by higher selling prices, favourable sales mix, and lower raw material and energy costs.

Allan will now discuss the main highlights of our financial performance. Allan?

Allan Hogg — CFO, Cascades Canada ULC

Thank you, Mario, and good morning, everyone.

So on Slide 13 and 14, we illustrate the specific items recorded during the quarter. The items that affected EBITDA were $12 million of impairment charges on US assets, restructuring costs related to closure of plants in the US.

Slide 15 and 16 illustrate the year-over-year and sequential variance of our Q3 adjusted earnings per share and the reconciliation with the specific items that affected our quarterly results.

As reported, Q3 net earnings per share were $0.34. This compared to a net loss per share of $0.02 last year and net earnings per share of $0.22 in Q2 of this year.

On an adjusted basis, net earnings per share were $0.44 in the current quarter. This compared to net earnings per share of $0.20 in last year's results and net earnings per share of $0.27 in Q2. Year over year, this variance mainly reflects improved adjusted EBITDA, partially offset by higher financing expenses, while sequential variance also reflects a positive adjustment of income tax from prior years.

As highlighted on Slide 17, third quarter adjusted cash flow from operations increased by $53 million year over year to $115 million, and adjusted cash flow levels improved by $96 million year over year. This was driven by higher operating results and lower net CapEx paid in the third quarter of 2023.

Slide 18 provides details about our capital investments. New investments this year totalled $229 million, and paid capital expenditures, net of disposal and accounts payable variation, totalled $297 million in the first nine months of 2023, including $56 million in Q3. For 2023, our planned capital investment of $225 million has not changed.

Moving now to our net debt reconciliation as detailed on Slide 19. Our net debt increased by $12 million in the third quarter despite stronger cash flow, lower CapEx paid, and positive working capital variance. Exchange rate increased net debt by $47 million during the quarter.

Our average ratio of 3.8 times is down from 4.1 at the end of Q2 and 4.6 times at the end of Q1. As we have mentioned in the past, it includes the impact of the recent investment and ramp-up of operations of the Bear Island facility.

Financial ratios and information about maturities are detailed on Slide 20, and other information and analysis can be found on Slides 23 through 29 of the deck.

Mario will now conclude the call with some brief comments and our near-term outlook before we begin the question period. Mario?

Mario Plourde

Thank you, Allan. We provide details regarding our near-term outlook on Slide 21 of the presentation. As a reminder, this outlook is based on current forecasts and expectations and may change.

Our near-term outlook for Containerboard is for results to be softer sequentially. This reflects higher raw material costs and lower selling prices, both of which are linked to indexes, as you know.

We also expect volume to decrease in Q4, due to the usual seasonal downswing in the period and a slight softening of demand due to the economic uncertainty. We expect to take approximately 47,000 tons of downtime in the fourth quarter for maintenance and inventory management, which is similar to what we took in Q4 last year.

Year-over-year performance is expected to be lower due to the impact from cost inflation, lower selling prices, following index price decreases, and higher raw material costs.

More broadly, results will benefit from ongoing ramp-up of the Bear Island. We are very pleased with the progress, which is on schedule, and our team is focused on ramping up production of lightweight grades.

Results in the Specialty Products segment are expected to be stable sequentially year over year. This reflects usual seasonal volume, stable selling prices trend and raw material costs, and capacity and efficiency improvements in several subsegments.

Our outlook for Tissue is for fourth quarter results to be stable sequentially, reflecting more favourable raw material and energy costs, benefit from profitability, productivity, and networking optimization initiatives, and stable volume. These will be offset by slightly lower pricing, connected to contracted input cost adjustments with customers. Results are forecast to be significantly above the prior-year levels, driven by the same factors.

Given the very strong results generated by our Tissue in Q3, some of you may be questioning whether our '24 EBITDA target for this business of between $120 million and $140 million is too low. It is a fair question, given that annualizing our Q3 results would bring us well above this range.

Let me address the question by saying that we are pleased that the wide-ranging actions put in place have positioned us to be tracking above the high end of this range. Notwithstanding this, and the fact that we are confident about the future performance of this business, we remain prudent, given some pricing pressure in the market, following the recent drop in raw material costs.

With that, we can open the call for questions, Operator.

Q&A

Operator

Thank you. Merci. [Operator Remarks in French]

Thank you. If you would like to ask a question, simply press the *, then number 1 on your telephone keypad. And if you would like to withdraw your question, please press *, followed by 2.

Again, if you have a question, please press *, then 1 on your telephone keypad.

And your first question will be from Sean Steuart at TD Securities. Please go ahead.

Sean Steuart — TD Securities

Thank you. Good morning, everyone. A few questions.

I'd like to start with containerboard markets and getting mixed messaging from a few sources; RISI showing prices flat in October; the Bloomberg survey reference prices declining $20 to $30 a ton across craft and recycle grades. With choppy box data of late, can you comment on what you're seeing in terms of price pressure in the containerboard market right now?

Charles Malo — President and COO, Containerboard Packaging, Cascades Canada ULC

So thank you, Sean, for the question. As you know, I'm not going to comment on the overall market. I can talk about what we're seeing. So we are still progressing on the developing business for our business, and that's really related to the investment that we made in both of our Piscataway facilities—also in Ontario, major investment, so that's sourcing our growth—and also with the addition of our mill in Bear Island.

So as we see right now, the pricing has followed the index of what has followed on the market, but we're still working with our customers to make sure that we provide them with the right service. The fact also that we're providing lightweight solutions is probably a positive for Cascades.

Sean Steuart

Thanks for that detail. And with Bear Island specifically, can you give us an indication of start-up costs that were embedded in overall third quarter EBITDA?

And what's the timing for the transition to positive EBITDA at the asset?

Charles Malo

Okay. So we, like Mario mentioned in the introduction, the Q3 was still not positive overall, but the good news for us is in September, we broke the positive side, if I can say it like that, and we intend to continue that in Q4 and ongoing.

Sean Steuart

Okay. That's encouraging. Last question for me, on Tissue. The gains that Cascades saw in margins this quarter outpaced the industry. More generally speaking, can you give updated comments on where the Company stands regarding attaining all the benefits through the various restructuring efforts you've rolled out in recent quarters? And I presume all the price increases are fully baked into your realizations at this point. But I guess, the potential for further margin expansion, absent fibre costs, volatility, and any further gains to be expected on that front?

Mario Plourde

Yeah. Good morning, Sean. Yeah. We believe there's still potential. We just don't know about the market and what will happen with the virgin pulp and the recycled fibre prices. But internally, I can say that we have a lot of opportunity and, again, network optimization, having the right product being produced at the right mill.

Also, in terms of integration, we're still buying a lot of jumbo roll internally, so optimizing the trims with the converting lines that we have, et cetera. And there's an important initiative for cost reduction at the mill level. So we still foresee good improvement, good potential.

But overall, what will happen with the market, so what will be the end result in terms of margin? It's tough to predict but, internally, I can say there's still a great opportunity to capture.

Sean Steuart

Okay. Thanks very much for that detail. That's all I have.

Operator

Thank you. Next question will be from Hamir Patel at CIBC Capital Markets. Please go ahead.

Hamir Patel — CIBC Capital Markets

Hi. Good morning. Allan, what are you planning for CapEx in 2024?

And maybe, if you could just update us on where you see your leverage ratios going by the end of next year?

Allan Hogg

Well, Hamir, we're keeping the same target as we disclosed in our strategic planning update, so at $175 million for next year, so. And we feel that our leverage should come within the target range we announced.

Hamir Patel

Great. And, Allan, how do you think about, just given Bear Island's ramping up well, the need to add additional converting capacity? And timing of when that capital investment might follow?

Charles Malo

So I'm going to take that one. I mean, so the plan for us since we started the Bear Island was, first, to make sure that we set up the mill to run well and follow the ramping up, which is the case right now. So the product is well received by the market, so that was our first objective. To optimize the mill is also part of our phase one, which is being done right now and following path.

Regarding the integration, I mentioned earlier that our Piscataway and our investments that we made in Ontario in the last two years, we still have room to integrate more volume, so that's the next step that we're doing. And for the rest of the integration, we are working and looking at projects, but we are going to look at the $175 million that we set for capital investments and follow that path. But the goal is still to work on integration, increase that, once we took the step that I just mentioned.

Hamir Patel

Great. Thanks, Charles. That's all I had. I'll turn it over.

Operator

Thank you. Next question will be from Matthew McKellar at RBC. Please go ahead.

Matthew McKellar — RBC

Hi. Good morning. Thanks for taking my questions.

I'd like to start here, so Tissue's running really well. You spoke to your target for that business as it relates to '24, as well as to your leverage target. Just more broadly, how are you thinking about your level of confidence around some of those other 2024 targets? And anything you'd call out that seem either more or less achievable at this point?

Jean-David Tardif — President and COO, Tissue Group, Cascades Canada ULC

Well, what we can see, Matthew, at this time is that we are still comfortable, even though we're facing some headwinds in our packaging business, but we have, as you saw, strong tailwinds in Tissue. So all in all, I think we're still comfortable, and I think we'll reconfirm everything in the next—after the fourth quarter. But for now, we're still within the targeted objective we set to the market.

Matthew McKellar

Okay. Thanks for that. Just shifting over, I think you mentioned some pricing pressure in Tissue as part of your outlook in the prepared comments. Can you talk about what the latest is that you're seeing in that market?

Allan Hogg

Yeah. Good morning. Right now, we're not seeing—we're seeing pressure in Canada, as you know, from the government against the retailers, so there's a lot of discussion around retail in Canada. We don't see much pressure elsewhere. I think people are waiting to see what will happen with the raw material pricing, pulp price, SOP pricing.

So we're managing. As Mario mentioned, we have a pricing model in place with important customers also, so we believe we're kind of protected for an important part of the business. But we'll continue to work with our customers and follow the market in the coming quarters.

Matthew McKellar

Okay. That's helpful. Thanks. And then last for me, there was a comment on your moulded pulp business that labour challenges limited shipments in a quarter, and I think you previously spoke about some operational issues there. Are you able to provide a bit more colour on what happened? And whether those challenges are persisting into Q4?

Jérôme Porlier — President and COO, Specialty Products, Cascades Canada ULC

Yeah. Good morning, Matthew. Jérôme speaking. So in terms of moulded pulp, yes, we announced for the Q2 that we had some operational issues that continue, part, in Q3. However, as mentioned by Mario at the beginning, those operational issues are behind us, and we're forecasting—we're seeing a good Q4 for the moulded pulp because the demand's still there, so.

Mario Plourde

So investment has been made to stabilize and have a—

Jérôme Porlier

Mm-hmm.

Mario Plourde

—stabilized production and of the desired output.

Jérôme Porlier

Yeah. Exactly.

Matthew McKellar

Okay. Thanks. That's all for me. I'll turn it back.

Operator

Thank you. Next question will be from Zachary Evershed at National Bank. Please go ahead.

Zachary Evershed — National Bank

Thank you. Good morning, everyone, and congrats on the quarter.

Mario Plourde

Thank you.

Jérôme Porlier

Thank you.

Allan Hogg

Thank you.

Zachary Evershed

As we're thinking about the sustainability of Tissue margins, you did indicate that lower raw material cost contributed $15 million to Tissue EBITDA, and lower freight was another $1 million dollars.

Could you maybe comment about how much of that benefit you can backfill with operational improvement, when or if pulp and freight tailwinds begin to fade?

Jean-David Tardif

Well, I don't have the exact number, but what I can tell you, as we explained in our investor day in Virginia, the Tissue business that we have now is much more resilient than it was years ago.

So when you look at the platform that we have, with 10 mills instead of 20, with fewer employees, fewer customers, fewer products, I think now we have a much better business that will go through the cycles in the coming year. So honestly, we won't see, again, issues as we saw in 2018 and 2022.

I'm really confident that the market will be able—the business, sorry, will be able to follow a typical market cycle as our competitors are seeing but, again, we have a much better and stronger business today with the investments also that were done, modernization, closure of older plants, et cetera.

Zachary Evershed

Thank you for that. And then, could I get your view on the supply and demand dynamic in Containerboard going into 2024, given the recent announcement of mill closures versus new capacity ramping up? And what you're seeing on the ground in terms of consumer demand trends?

Allan Hogg

Okay. So on the overall market, you all saw the published numbers of the additional capacity and also the closure. As we speak right now—I'm going to use what was published—there's with a 11.4 growth on the market of the demand. The market, in the mid to long term, seems to be better, the way we see it right now. And on our side, you're seeing that we're taking the steps to make sure that we're balancing, also, our inventory level based on the demand.

So the other thing I would add to this is Cascades is a lot better equipped right now with about 1.1 million—1.4 million tons, sorry—of volume on the Containerboard side that is Tier 1, so we're better equipped to compete.

So I would just say that we are going to manage on our side based on the market conditions, but the mid to long term seems to be looking good right now overall in the market.

Zachary Evershed

Good colour. Thanks. And just one last one. You guys are outperforming box shipments in Canada and the US. Now obviously, there's a contribution there from Bear Island. Is anything else lifting that?

Charles Malo

Well, mainly, when we look at the performance that we are doing compared to the market, is really based on the—yes, we have been focusing our sales team on specific markets that are growing a bit faster than the average market right now, so meaning like the e-comm and the distribution, so which is helping us.

One of the markets that is not doing as good for the time being, just because of the economy, is the industrial, so it's about 15 percent of our volumes overall. When we look at the markets, our strategy has been to focus on faster growing markets, and it's paying off.

But in addition to that, as I mentioned earlier, the growth is also coming largely because of the investment that we made in Piscataway, which has been very good for Cascades.

So Tissue is well located and servicing, also, markets that are growing faster than the average, and the same thing also in our region in Ontario. When you look at the overall, the Ontario market is more than 50 percent of the overall market in Canada, and that's where we decided to make a major investment to align our capacity to service the market.

Zachary Evershed

Very helpful. Thanks. I'll turn it over.

Operator

Thank you. As a reminder, ladies and gentlemen, if you would like to ask a question, please press *, followed by 1 on your touch-tone phone.

And your next question will be from Frédéric Tremblay at Desjardins.

Frédéric Tremblay — Desjardins

Thank you. First, my condolences to the Cascades team following the passing of Mr. Lemaire.

Mario Plourde

Thank you.

Charles Malo

Thank you

Frédéric Tremblay

Sorry if I missed it, but maybe as a follow-up to the last question there on Containerboard.

I'm just trying to figure out what would have been the shift from growth from your legacy operations, if we exclude the contribution from new capacity and Bear Island? Can you provide some comments on that?

Charles Malo

No. We're not going to comment on this since we have a—we look at the overall network that we have, and this is what we're doing right now. And when we're making our decision of where the volume is going to be produced, we're making our decision on what brings the most profitability to Cascades. So again, we're seeing this as an overall, so we're not going to disclose any specific—counting the old or new or facility or in the network.

Frédéric Tremblay

Okay. Understood. Switching to Tissue, on the away-from-home, just curious to get your thoughts on what you're seeing in that market right now. And what are your expectations as we sort of progressed in an uncertain economic environment? Is that an area where you're seeing some weakness now? Or has it been fairly resilient so far?

Jean-David Tardif

Good morning, Frédéric. So it's been stable, honestly. I think everybody's waiting to see what will happen. It's a big question mark, for sure.

One thing, also, we've done internally is that business now represents one-third of our business versus almost 50 percent, so we gained some flexibility. So we're less at risk than we were towards away-from-home versus a few years ago, first thing.

The other thing is October was our best month for the year, so in terms of case shift. So I think, overall, it shows that the market is still solid. But as I said earlier, I think we've picked the right customers, also, as Charles mentioned, having the right customers, who are growing in those difficult periods.

And I think the mix of products that we have, which is not in the ultra segment, is also helping us. We're not really strong in the office channel either, so it's also somewhere where we're gaining. So overall, I think we're still optimistic and positive about that business but, for sure, there's a lot of uncertainty, as you all know. But nobody knows exactly what will happen next year, but I think we are, again, much better positioned to go through the coming quarters.

Frédéric Tremblay

Great. That's it for me. Thank you.

Operator

Thank you. There are no further questions at this time. Monsieur Plourde, please continue.

Mario Plourde

Yes. Thank you, everyone, for being on the line this morning and looking forward to talk to you with the fourth quarter. Have a good day. Thank you.

Operator

[Operator Remarks in French]

Thank you, ladies and gentlemen. This does conclude today's conference. You may now disconnect your lines.