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Blucora, Inc. Second Quarter 2021
Earnings Conference Call

<u>Dee Littrell, INVESTOR RELATIONS</u>

Thank you and welcome, everyone, to Blucora's second quarter 2021 Earnings Conference Call. By now, you should have had the opportunity to review a copy of our earnings release and supplemental information. If you have not reviewed these documents, they are available on the investor relations section of our website at Blucora.com. I'm joined today by Chris Walters, Chief Executive Officer, and Marc Mehlman, Chief Financial Officer.

Before we begin, let me remind everyone that today's discussion contains forward-looking statements based on the environment as we currently see it that speak only as of the current date. As such, they include risks and uncertainties, and actual results and events could differ materially from our current expectations. Please refer to our press release and our other SEC filings, including our Forms 10-K and 10-Q and other reports, for more information on some of these specific risks and uncertainties. We assume no obligation to update our forward-looking statements, except as required by law.

We will discuss both GAAP and non-GAAP financial measures today. Our earnings release and supplemental financial information are available on blucora.com and include full reconciliations of each non-GAAP financial measure discussed to the nearest applicable GAAP measure.

With that, let me hand the call over to Chris.

<u>CHRIS WALTERS, PRESIDENT AND CHIEF EXECUTIVE OFFICER</u>
Thank you Dee, and good morning everyone.

Opening

I am pleased to report that Blucora's second quarter financial results have exceeded our expectations across the board and that we continue to execute effectively against our strategic vision. Our market position across our respective businesses sets the Company up for long-term sustainable growth potential, and our team is clear on both our short-term and long-term execution plans for success. In short, the state of the business is strong.

Having just shared our long-term vision for the business and updating our full year guidance for 2021 during Investor Day in June, our remarks today will be relatively brief.

Before I delve into the details of the second quarter, I will reiterate the elements of our sustainable growth strategy:

- TaxAct unit growth driven by providing a fully featured value offering
- AUA and advisory growth through technology, marketing, and service enhancements

- Realizing the value of our differentiated model through a targeted synergy program; and lastly
- Implementing a unified, learning & customer focused, and performance-oriented culture

Our formula is paying off and our excitement is building.

With that, let's turn our attention toward the highlights of the second quarter:

TaxAct

During Investor Day we shared the highlights of tax season, with our discussion that day having taken place on the same day as the extended deadline for the remaining 3 states that had been impacted by severe winter storms. With those three states now complete, and having met our expectations, we are reiterating our full year 2021 financial guidance for TaxAct, which as a reminder, is for 7.1% to 8.5% revenue growth over 2020 and between $80M to $82M in Segment Operating Income, which represents greater than a $30M year over year increase.

As a reminder I will share a few of the key highlights:

- We meaningfully improved our value proposition by lowering federal pricing to offer a great experience at up to a 20%-50% discount relative to the market leader.
- Drove a 10x increase in our number of partnerships versus prior year
- Refreshed the end to end customer experience while also launching a new hybrid offering
- Improved start rate, conversion rate, paid customer retention and NPS scores versus the prior season.
- Continued to gain share in the Tax Professional market

With this strong momentum behind us, we now turn to preparation for the next tax season. For the balance of this year we plan to focus our attention on several key areas:

- Continue to drive improvements in our brand recognition, which has a direct effect on our marketing tactics in season
- As it relates to marketing, prioritize our first party data collection efforts to expand our one to one reach as well as improve our start rate in coming seasons through personalized customer experiences
- Execute on our user experience upgrades, with a special focus on the areas with greatest friction in the workflow; and lastly
- Focus on our Year 2 filers, where we have the opportunity to meaningfully improve retention and with that lifetime value.

I am pleased with the results of TY 20 and the many learnings that our relatively new team has absorbed. I look forward to sharing the progress over the next two quarters as we prepare for next season.

Avantax

Moving on to Wealth Management:

I am encouraged by our continued positive trajectory in Wealth Management. We continue to drive growth in AUM, resulting in a greater percentage of overall fee-based assets, which results in a more favorable ROA for the business. At our Investor Day, we highlighted on-platform RIA acquisitions as an opportunity to scale our advisory business by deploying capital at strong returns while delivering compelling solutions to financial professionals and their clients. Our pipeline of independent financial professionals interested in joining our RIA continues to grow, and in case you missed it, we recently announced that Blucora has agreed to acquire Headquarters Advisory Group. The Headquarters team, who have long affiliated with Avantax, was looking for both a succession plan and continued growth opportunities. They concluded that our Avantax Planning Partners RIA was the best solution to achieve both objectives. Once closed, this would bring the acquired assets from our independent channel to APP to $1.3 billion, or approximately 20% of APPs total client assets. The ability to offer our financial professionals choice and a seamless transition to this alternative model is proving to be an attractive option for both our FPs and Avantax.

As we've mentioned on previous calls, we still have much work to do as it relates to the technology experience for FPs and as we discussed in our Investor Day, many of these improvements are in flight and will continue. While we are pleased with the quarter over quarter improvement in our net flows and the feedback we are receiving on our progress on both service support and technical improvements, we are not yet finished. We expect the trend on negative net flows to continue through year-end with a shift toward positive flows beginning next year.

And now a few highlights for the quarter:

- The business set a record through Q2 for the greatest percentage of AUM of total client assets, at 44.9%.
- Our Financial Professional Production retention in Q2 was at 98%
- Of the 145 departing Financial Professionals in Q2, 111 or ~77% were non-producing Financial Professionals (defined as less than $50K in rolling gross production).
- Our RIA roll-up plan, whereby we provide an opportunity for our independent Financial Professionals to be acquired into the RIA continues to accelerate with more than $5B in assets in our pipeline.
- Net new client assets came in at ($250M), our best quarter since Q1 of 2020.

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As I conclude I will reiterate my closing remarks from last quarter: Our business is in a strong position, our cash balance affords us the ability to be opportunistic, our model shift within Wealth Management is well underway and our plans to drive growth and expanding margins in TaxAct are on track.

With that I'll turn it over to Marc to review our Q2 financial performance and our Q3 and Full Year 2021 outlook.

<u>MARC MEHLMAN, CHIEF FINANCIAL OFFICER</u>

Thank you Chris, and good morning everyone.

It's great to be with you all again. I'd like to provide some additional detail on our second quarter results and our outlook for the third quarter 2021 and full year.

Starting with second quarter results:

1. Total revenue of $254.3 million, an increase of 58% versus prior year and, just shy of the high-end of our guidance range
2. GAAP net income of $31.6M or $0.64 per diluted share. Embedded within our GAAP net income figures are:
   - A $11.5M true-up associated with the HKFS earn-out, the full $30.0 million payment for the first earn-out period will be paid out in the 3rd quarter.
   - A ~$2.5M expense associated with the remaining costs relating with the proxy conflict

Adjusted EBITDA, which excludes these and certain other factors, was $78.6 million. 524% growth versus the prior year period and $3 million above the high end of our guidance range.

Non-GAAP net income was $63.1 million, or $1.28 per diluted share. Respective increases of $58.6 million and $1.19 per share versus prior year and both above the high-end of our second quarter guidance range.

Tax Software

Turning now to the tax software segment, which as we discussed during Investor Day came in meaningfully above our expectations entering the season. Tax Software revenue was $91.9 million, and segment operating income was $63.4 million.

Wealth Management

Moving on to wealth management. Second quarter reported wealth management revenue was $162.4 million, slightly higher than the high end of our previously released guidance of $161.5M and up 5% sequentially, which included a 5% increase at Legacy Avantax and 7% increase at APP. Transaction-based commission revenues were down slightly quarter over quarter, but still robust at north of $21M.

On a year-over-year basis, total wealth management revenue was up 40% which included revenue of $9.9 million from Avantax Planning Partners.

Wealth management segment operating income came in at $21.4 million, above the high-end of our guidance of $19.5M, driven by lower than expected operating costs and a strong top-line revenue performance at the end of the quarter.

Total client assets increased 28% year-over-year to $87.8 billion, which included approximately $5.7 billion from the addition of Avantax Planning Partners. Fee-based advisory assets were up 49% year-over-year to $39.4 billion with advisory assets as a percentage of total client assets ending the quarter at 44.9%.

We saw net inflows in advisory assets of $864 million with total client assets having net outflows of $250 million which relates in part to our focus toward higher ROA on platform assets and lower ROA off platform Direct To Fund assets.

At the Corporate level, unallocated corporate expenses came in at $6.3 million, exceeding expectations and below the guidance range as we continue to monitor our corporate costs in support of our businesses. During the quarter, we had about $1.2 million in integration costs related to HKFS and 1G. Based on our ongoing discussions with the SEC we reevaluated our contingent liability reserve for the regulatory matter assumed in the 1G acquisition and increased the liability from $11.3M to $16.8M. The $5.5M increase to the contingent liability reserve has been recognized in acquisition expense.

Liquidity
We ended the quarter with cash and cash equivalents of $232.4 million, and net debt of $329.8 million. Our reported net leverage ratio at the end of the quarter was 1.9x, compared to 3.5x at the end of Q1 2021. I would like to remind you that we will have an outflow of $30M in the 3rd quarter relating to the first HKFS earn-out payment.

As discussed during Investor Day in June, our key priorities for cash include investing in our business to fuel growth. Our capital investments are aimed at:

- Solving critical customer pain points in the workflows of our customers
- Ensuring continued positive momentum in net new assets, rising advisor sentiment, all while delivering on the most critical current needs of our Financial Professionals
- Ensuring we are properly funding the cross-over benefits between our two businesses; and lastly
- Providing capital for RIA acquisition opportunities.

Q3 and Full Year Outlook
With that, let's turn to our third quarter and FY 2021 outlook:

For the third quarter, we expect our tax software segment revenue to be between $5.0 million and $5.5 million and a segment loss of $15.5 million to $15.0 million. For our wealth management segment, including APP, we expect third quarter revenue of between $158.5 million and $162.5 million and segment income of between $16.5 million and $18.0 million. On a consolidated basis for the third quarter, again, including APP, we expect total Blucora revenue of between $163.5 million and $168.0 million, adjusted EBITDA of between negative $6.5 million and negative $4.0 million, GAAP net loss of $34.0 million to $30.5 million or loss of $0.69 to $0.62 per diluted share and non-GAAP net loss attributable to Blucora of $19.0 million to $16.0 million or loss of $0.39 to $0.33 per diluted share. This outlook includes third quarter unallocated corporate expenses of $7.5 million to $7.0 million.

For the full year, we expect our tax software segment revenue of between $223.5 million and $226.5 million and segment income of $80.0 million to $82.0 million. For our wealth management segment, we expect full year revenue, which includes APP, of between $631.5 million and $649.5 million, and segment income of $79.0 million to $83.5 million. This translates to consolidated full year outlook, again including APP, of revenue of between $855.0 million and $876.0 million, adjusted EBITDA of $131.5 million to $139.0 million, GAAP net loss attributable to Blucora of $8.5 million to net income of $1.0 million or a net loss of $0.17 to net income of $0.02 per diluted share and non-GAAP net income of $76.0 million to $84.5 million or $1.52 to $1.70 per diluted share. This outlook includes $27.5 million to $26.5 million in unallocated corporate expenses.

We will now turn the call over to the operator for Q&A. Operator?

CHRIS WALTERS, PRESIDENT AND CHIEF EXECUTIVE OFFICER

Thank you all for joining us today and for your interest in Blucora. Speak with you next quarter.