Avantax®

Q4 2022 Earnings

Dee Littrell, Investor Relations

Thank you and welcome everyone to the Avantax fourth quarter 2022 Earnings Conference Call. On Wednesday afternoon, following market close, we posted our earnings release and supplemental information on the investor relations section of our website at Avantax.com.

I am 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 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 SEC filings, including our most recent Form 10-K and Form 10-Q, 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 the investor relations section of our website at Avantax.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.

CHRIS WALTERS, CHIEF EXECUTIVE OFFICER

Thank you, Dee.

Good morning.

I am pleased to share our fourth quarter 2022 earnings results for the first time under the Avantax name. On January 26, we changed our corporate name from Blucora to Avantax and changed our ticker symbol to AVTA, marking our next step as a pure-play wealth management company.

During our third quarter earnings call, we shared that we had agreed to sell our TaxAct software business to an affiliate of Cinven for $720 million, subject to post-closing adjustments. On December 19, we announced the completion of the sale of TaxAct, which positioned us to shift our organization to reflect our singular focus on continuing to grow our wealth management business and return capital to stockholders. We successfully achieved these milestones while at the same time having a record-breaking year in many of our key wealth management operating metrics. I would like to thank all of our financial professionals, employees and board members for their contributions to realizing these accomplishments.

As noted, we have made significant progress on our more focused operations and capital structure.

- **On Operations:** We have begun streamlining our organization and are positioning our team to execute our wealth-only growth strategy. As part of this work, we have announced the plan to reduce the size of our Board of Directors at our 2023 annual meeting and the departure of multiple executives whose contributions are greatly appreciated. Our team has been aligned to deliver our strategic priorities of:
  1) Growing NNA by supporting existing Financial Professionals growth and recruiting new Financial Professionals and accounting firms.
  2) Retaining existing Financial Professionals by providing exceptional service and tools.
  3) When in the best interest of the client, shifting to a higher value mix by increasing fee-based assets and continuing RIA acquisitions.

  We've also made targeted incremental investments to support our Financial Professionals and affiliated CPA firms.

- **On Capital Structure**: In January, we repurchased 460,160 shares for a total of $12.5 million. On January 24th, we entered into a new term loan facility of up to a maximum principal amount of $270 million that also provides for a $50 million revolving credit facility. This facility has a lower interest rate compared to our previous credit agreement, has a delayed draw feature that further enables us to keep interest costs down and does not have significant upfront costs as compared to other options.

On January 27th, we announced that we commenced a modified Dutch Auction tender offer to purchase up to $250 million of our common stock for between $27 and $31 per share. This is in addition to our approved $200 million share repurchase authorization.

Moving on to our results for the fourth quarter, we continued to excel across the most important indicators that we use to measure the performance of our business.

- **First, our net positive flows**. We have seen net positive asset flows for the 4th consecutive quarter. In Q4, we had $495 million in net new assets – up $115 million over last quarter and setting a new record of $1.3 billion for the business for the trailing 12-month period.

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- **Second, our recruiting**. We also continued to successfully recruit Financial Professionals with over $401 million in newly recruited assets during the fourth quarter, finishing another record year adding approximately 79% more in recruited assets than our next best year. We also recruited 3 new CPA firms to Avantax Planning Partners and have a strong pipeline for 2023 in both our independent broker dealer model as well as our employee-based RIA.

- **Third, our firm acquisitions**. This quarter, we marked a milestone with 20 acquisitions completed in 20 months, increasing total client assets held in our employee-based model to approximately $7 billion, up from $4.4 billion a little over two years ago.

- **Fourth, we continued to retain productive Financial Professionals.** Our consistently high production retention rate came in at 99.3% for the quarter. Of the Financial Professionals who departed during the quarter, 90% were non-producing Financial Professionals with less than $50K in rolling gross production.

- **Lastly**, **our Financial Professional satisfaction**. We regularly conduct Financial Professional satisfaction surveys to assist us in better meeting our Financial Professionals' needs. In the survey, our Net Promoter Scores improved by 14 points from our Spring '22 survey and 21 points from winter survey last year.

In short, we are executing well on our mission to be the leader serving a community of CPAs, tax professionals, and tax-focused Financial Professionals by providing clients tax-advantaged investment solutions, innovative technologies, and tax-inclusive financial planning. We remain focused on extending our lead on the key differentiated aspects of our strategy, which include:

- Nurturing and growing the largest community of tax-focused Financial Professionals in the wealth management industry through training, growth communities, coaching programs and purpose driven events;

- Providing best in class service and support; and

- Delivering capabilities to accelerate our Financial Professionals' growth, including continuing to develop investment solutions, growth consulting, practice management and digital products.

In addition to these efforts, we are providing opportunities for Financial Professionals to work with Avantax in the way that aligns with their priorities, which has led to rapidly growing Avantax Planning Partners, our employee-based RIA, and resulted in a significant pipeline to further grow this portion of our business.

Our pure-play wealth management business is effectively executing on plan, is serving our Financial Professionals and end clients well and is taking actions on our capital structure that, together, we believe will result in an exciting future for our Financial Professionals, employees and shareholders.

Now, I'll turn it over to Marc and we'll be happy to answer questions after the prepared remarks.

Marc Mehlman, CHIEF FINANCIAL OFFICER

Thank you, Chris, and good morning everyone. The work over the last several months, since the announced sale of TaxAct has culminated in this moment where we can share our financial results as a stand-alone wealth business, and as you can tell from our financial performance, our business is strong.

Starting with fourth quarter results, as Chris mentioned, we are thrilled to have executed well this quarter. 2022 was a strong year for the business. Avantax broke records for recruited assets, total net new assets for the year and the percentage of our assets in advisory.

Now, on to fourth quarter financial results:

- Total revenue of $172.4 million was a record for the business, slightly up from the fourth quarter of the prior year, up 4% versus the 3rd quarter of 2022 and above the high-end of our guidance. Achieving this record revenue figure despite the market being down meaningfully is a reflection of the favorable interest rate environment as well as asset mix-shifts we've seen in our portfolio. Return on Assets is up 109 basis points versus Q4 of 2021. Transaction-based commission revenues were $19 million, an increase of 7% sequentially. Year-over-year transaction-based commission revenues decreased 21% for the quarter and 16% for full year 2022.

- As it is difficult to tell from the discontinued operations treatment, for ease of comparison the Adjusted EBITDA for both continuing and discontinued operations came in at $18.6 million for the fourth quarter, which is near the high end of our guidance. As for adjusted EBITDA for continuing operations, the result was $25.9 million with performance driven by favorable revenue performance and lower than expected costs in the quarter. Q4 is a higher expense quarter than Q3 because of the National Conference.

- GAAP net income was $368 million, or $7.66 per diluted share. Included in our GAAP net income is a pre-tax gain on sale of TaxAct of $472.2 million.

A few other details regarding our performance this quarter:

Our pay-out rate in the fourth quarter decreased to 74.2% from 75.1% in the third quarter, the lowest rate we have seen since Q1 2021, when it was 74.4%. We will see fluctuations in payout rate depending upon the concentration of transaction-based revenues, the make-up of net flows and the mix of assets in the quarter.

We ended the year with total client assets of $76.9 billion. Fee-based advisory assets were down 9% year-over-year to $38.3 billion with advisory assets as a percentage of total client assets ending the quarter at a new high of 49.8%. Net flows into Advisory for the year were $2.9 billion with $638 million in the fourth quarter with total client assets having net inflows of $1.3 billion for the year and $495 million for the fourth quarter.

We have driven our newly recruited assets for full-year 2022 to $1.7 billion versus $929 million in 2021, which was a record for the business at that time. As shared previously, our goal is to drive 2.0% to 2.5% organic growth per annum via newly recruited assets.

Liquidity

Turning to the balance sheet, we ended the year with cash and cash equivalents of $264 million and no debt, as we paid off the outstanding term loan with proceeds from the TaxAct sale. We have subsequently entered into a Term Loan A with a newly established banking group where we can borrow up to $270 million over the next twelve months, along with a $50 million revolver. We expect to draw $170 million in late February to help fund the Tender Offer with the remaining capacity of the $270 term loan expected to be borrowed over the course of the year to primarily fund continued share repurchases.

We were pleased with the financing result and the confidence our bank group showed in our business. We believe the interest rate and low cost to fund are attractive relative to other options and provide us the opportunity to create meaningful value.

Our capital allocation priorities continue to be returning capital to shareholders following the tender offer under the remaining $187.5 million in our repurchase authorization, investing in our business to fuel growth and continuing to execute on our acquisition program of individual Financial Professionals into our employee-based model.

For the medium term we expect our net leverage ratio to be between 1.5x and 2.5x.

2023 Full-Year Outlook

With that, let’s turn to our Full-Year 2023 outlook:

We expect full-year revenue between $750 million and $758 million and Adjusted EBITDA of $124.5 million to $135.5 million. These figures assume 4% market growth from the end of 2022, with 1% growth per quarter. As it relates to Fed Funds rates, we continue to leverage the forward curve, and at the time of finalizing our guidance, assumes one more 25 basis point hike in March.

Other factors that can drive revenue outcomes include the performance of transaction sales and the timing of asset flows throughout the year.

Our guidance assumes that we will drive meaningful cost efficiencies in the business, that will be realized throughout the year, with a larger amount following the provision of transition services in connection with the TaxAct sale, which we believe will mostly be completed by the end of the third quarter 2023.

With respect to GAAP Net Income, we expect between $25.5 million and $40.1 million and GAAP earnings per share of $0.63 to $0.96 per share. We are anticipating between $7.8 million and $14.5 million in adjusted expense items relating to the cost of delivering cost savings, potential proxy matters and other one-time items related to the sale of TaxAct.

Lastly, we have assumed between $12.7 million and $13.5 million in interest expense, roughly $14 million in depreciation and $25 million in amortization expenses for the year.

This concludes our prepared remarks; 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 Avantax. Speak with you next quarter.