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Blucora Q4 2016 Management's Prepared Remarks

The following is Blucora management's prepared remarks on a conference call Thursday, February 16, 2017 at 7:30 a.m. CT / 8:30 a.m. ET to discuss Blucora's fourth quarter and full year 2016 financial results. This webcast can be accessed within the Investor Relations section of the Blucora corporate website at www.blucora.com.

FORWARD LOOKING STATEMENT - STACY YBARRA, VICE PRESIDENT INVESTOR RELATIONS

Good morning, and welcome to Blucora's investor conference call to discuss the fourth quarter and full year 2016 earnings.

Before we begin, I'd like to remind you that during the course of this call, Blucora representatives will make forward-looking statements, including but not limited to statements regarding Blucora's expectations about its products and services, outlook for the future of our business and growth initiatives, and anticipated financial performance for the first quarter and tax season.

Other statements that refer to our beliefs, plans, expectations or intentions - which may be made in response to questions - are also forward-looking statements for purposes of the safe harbor provided by the Private Securities Litigation Reform Act. Because these statements pertain to future events, they are subject to various risks and uncertainties, and actual results could differ materially from our current expectations and beliefs. Factors that could cause or contribute to such differences include, but are not limited to, the risks and other factors discussed in Blucora's most recent Quarterly Report on Form 10-Q on file with the Securities and Exchange Commission. Blucora assumes no obligation to update any forward-looking statement, which speak only as of the date the statement is made.

In addition, during our call, our management will discuss GAAP and non-GAAP financial measures. In the press release, which has been posted on our website and filed with the SEC on Form 8-K, we present GAAP and non-GAAP results along with the reconciliation tables, and the reasons for our presentation of non-GAAP information.

We have also provided supplemental financial information to our results in the investor relations section of our corporate website at www.blucora.com and filed with the SEC on Form 8-K. Now, I'll turn the call over to John Clendening. Following his comments, Eric Emans will review fourth quarter and full year results and first quarter outlook. Then we'll open up the call to your questions.

JOHN CLENDENING, PRESIDENT AND CHIEF EXECUTIVE OFFICER

Good morning everyone, and thank you for joining our call today. We are calling you from Irving for the first time, and while the corporate headquarters won't move here until the end of June, I've already moved my office to be closer to the HD Vest team as well as to shorten the flight to Cedar Rapids where most of the TaxAct team works.

2016 was an important year for Blucora as we made significant progress on our transformation into a simplified, streamlined, and synergistic technology-enabled financial solutions company. When I joined the team in April of last year, I spent a lot of time listening and learning. I confirmed that we have two good businesses well-positioned in attractive markets and with the potential to grow. I told you that we were focused on the four D's: Divest, De-lever, Deliver and Drive. I'm pleased to say that we made strong progress on each of these, and exited 2016 even more convinced about the strength of our businesses and the opportunities that are ahead.

As you know, we ***divested*** Infospace in August and Monoprice in November for a total of $85 million. We continued to ***de-lever*** the business by paying down $172 million in debt, ***delivered*** strong cash-flow performance, and began to ***drive*** synergies between HD Vest and TaxAct while acting to improve the growth trajectory of each.

I am particularly encouraged by HD Vest's performance in the fourth quarter, which shows momentum heading into this year. And while the digital DIY tax market is growing increasingly competitive, we have a solid platform and are embarking on a multi-year plan to re-establish TaxAct as the challenger brand in the space. Big picture, we are beginning 2017 well-positioned to complete the final phase of our multi-stage transformation. With HD Vest and TaxAct as our operational foundation, we will focus on completing the organizational elements of the plan and growing our businesses organically.

As we recently announced, we have added incredibly talented leaders to help us take these businesses to the next level. In the beginning of January, we announced the appointment of Sanjay Baskaran as president of TaxAct. Sanjay joins us from Amazon and brings more than 20 years of experience driving growth in technology and financial services businesses. We are confident that he can take that business forward in exciting ways. Working closely with the TaxAct team, Sanjay will leverage his customer-centric focus and digital experience to execute on our growth objectives. While he's only been a part of the team for a couple of weeks, it's clear we have the right leader in Sanjay.

We also recently announced that Bob Oros was named CEO of HD Vest. Bob brings many years of sales and operational experience and has served in leadership roles at leading brokerage and investment advisory firms, most recently heading up Fidelity's RIA business. He has a strong track record of successfully recruiting and partnering with independent advisors to drive growth. Bob succeeds Roger Ochs, who will be with the company through the end of March to facilitate a seamless transition. I'm looking forward to Bob joining us at the end of the month, and expect he'll hit the ground running.

As I've shared, we intend to build the very best team in the business - Bob and Sanjay are great additions to the team. I'm sure there will be opportunities for our analysts and owners to get to know Sanjay and Bob later this year.

With the go-forward operating companies now in place, new leaders to head them up, and clarity on what it takes to win, our teams are energized to deliver for our shareholders and customers in 2017 and beyond. Now, let's turn to the operational highlights for the quarter.

Starting with Wealth Management.

Fourth quarter revenue performed ahead of expectations at $83.1 million up slightly compared to the prior year. Segment income was strong at $13.8 million up 13 percent over the fourth quarter 2015. We capped the year with positive results in all the primary drivers of value. Highlights include:

- Assets under management (AUM) in fee-based advisory accounts grew to $10.4 billion. The fourth quarter was the strongest in advisory net flows in seven quarters. Much of this growth is a direct result of the efforts of our advisors to anchor their investment strategies in our goals-based planning tool VestVision®. We will continue to drive adoption of this tool, as a goals-based plan puts our advisors in the best possible position to service clients and drive asset accumulation. And, for Blucora, these represent attractive "annuitized" assets.

- Sweep revenue increased in the fourth quarter as we benefited from rising interest rates, which while not at the level we built into our plan, are an important driver of profit growth.

Advisor recruitment remains a top priority as it helps drive long-term value for the firm. We recruited approximately 400 new advisors in 2016. It's important to point out that our model is different from other independent broker dealers in that we recruit tax professionals and enable them to provide wealth management solutions to their clients. With this approach, new advisors typically take a few years to build their business and begin making meaningful contributions to asset accumulation at HD Vest. This model is a source of advantage for us because it drives stronger loyalty among our advisors and better economics than those enjoyed by typical independent broker dealers.

Given that our advisor model is a strong competitive advantage, we continue to explore ways to improve our advisor recruiting and retention program. We are off to a very good start this year, and we are also having strong results with our succession-planning program, which helps retain the client assets of long-tenured advisors and drives value. Among those advisors who retired in 2016, we maintained 47% of their client's assets through this program, allowing us to keep the assets in-house by transitioning the clients to another HD Vest advisor. So, while advisor count is reduced, larger, healthier advisor practices are created.

We continue to invest in technology to drive growth. As mentioned last quarter, we are upgrading our advisory platform trading technology. In November, we announced that we are partnering with FolioDynamix to provide a cloud-based solution for HD Vest Advisors to manage the entire client lifecycle from proposal generation to account opening and management, including trading and rebalancing, to reporting. This is an important investment in our capabilities, and the new platform will provide our advisors with enhanced insight into client portfolios, and will support the strong growth we continue to see in adoption of for-fee advisory solutions. The new platform will be fully operational this summer.

Even though the DOL rule is under review by the new administration, we are continuing to make investments that will enhance our ability to provide our advisors and their clients with best-of-class wealth management services. We will continue to express our support for an investment fiduciary standard of care that is collaboratively developed by industry participants and our regulators. The majority of our advisors are already able to act as a fiduciary under the investment advisors act. They advise on approximately 80 percent of our clients assets under administration, and act as a fiduciary on $10.5 billion of advisory assets. We know that when our advisors are at their best, they can advise clients better than far larger incumbents, because they can provide integrated tax and investment solutions – something these other firms are simply unable to do.

Now turning to our financial and operational results for tax preparation.

As you know, tax season is underway – although at a slower than normal pace – and the market remains increasingly competitive with advertising spend and promotions up significantly thus far. The siren call of "free" tax filing continues to dominate the marketplace, the large storefronts are more aggressive with their online offers and marketing spending, and there is a new entrant in the digital-do-it-yourself space this year. As we look at our position in the market, we see a real opportunity to differentiate TaxAct as the brand that stands for exceptional value and is known as the most trustworthy.

Value

I am pleased to report that TaxAct recently received PC Magazine's Editor's Choice for affordable tax preparation software, receiving one of two Editor's Choice awards. As the magazine noted, "If you're looking for an inexpensive service for doing your 2016 taxes, TaxAct is tops." We are proud of this accomplishment and the dedicated TaxAct team that is responsible for it. They don't intend to rest on their laurels - we are committed to continuously improving the user experience. We help guide customers through their filing process while also offering a far better value than the industry leaders with whom we are compared. To bring that better value in sharp relief, even with pricing actions we have taken this year, today we offer customers as much as a 50 percent savings versus Turbo Tax and H&R Block. We are working to make this superior value clear to our target customers.

Brand and Consumer Targeting

There are many online tax prep solutions out there, but even those that say they are free too often come at a "price." Simply put, millions of customers enter the filing process thinking they will file for free and instead are charged at checkout. Along the way, they are charged for add-on services or are inundated with offers. For our part, we have heard loud and clear from a segment of valuable customers that they don't want to be lured by promises of free filing, only to be charged for things they didn't expect to have to pay for, or to be bombarded with emails pitching products they don't need or want.

So, at TaxAct, we are focused on acquiring savvy customers who value great products at fair prices and are fed up with the industry's games. We think transparency is the way to go and that is our pledge to our customers.

We just launched a new ad campaign – The System to Beat the System – to highlight these industry practices and put an end to them. This season we have taken steps to be transparent in our messaging and pricing. For example:

- Customers know up front what they will pay to file with TaxAct. Though TaxAct is free for many filers, some pay for specific services. That's why this year in our advertising we don't emphasize "free" offers in our marketing – we are clear and transparent about the pricing so that customers know right from the start what they will pay for our service.
- Our price lock guarantee ensures that customers pay the price listed on the product at the time they start their return, not when they finish their return. TaxAct is the only major online provider that offer a price lock guarantee.
- We do not charge anyone for phone support. Customers can contact TaxAct's team of trained tax professionals via phone for tax and technical help at no additional charge. This is an added value not included in free product from competitors.
- For the first time, all customers can access up to three years of prior TaxAct online returns for no additional charge.

We are committed to being the brand that delivers transparency, with a focus on paid filers. What leads us to be confident that this is the right path, in stark contrast to all the other players?

- First, a pivot toward paid filers creates superior economic returns and, as a result, we're willing to sacrifice total units in the form of fewer "free" filers;
- Second, there is clear consumer demand for a transparent approach; and,
- Third, we believe transparency leads to trust and trust enables us to add more value and help more customers manage their financial well-being, beyond the once-a-year transactional relationship that most tax-prep firms have with their customers.

A manifestation of helping more customers manage their financial well-being is our recent launch of BluVest, an integrated platform that offers TaxAct customers the option to receive affordable and objective investment advice. The service is designed to provide our customers with a current-year tax benefit by investing in retirement accounts during the tax return filing process, and fund their investments directly with their tax refund into a "robo" type offering. While BluVest is not expected to materially impact our financial results this year, offering financial solutions that are relevant to our customers adds value and begins to build a year-round relationship between the customer and the TaxAct brand. And it's a great example of the synergy value between our two units.

As you know, the IRS opened four days later than last year. As a result, the industry overall is off to a slow start this year across all tax preparation methods. Instead of the typical early season peak, we are seeing that peak spread out over a longer period. This change in the timing of consumers filing returns challenges comparisons to prior seasons.

However, we continue to believe the digital-do-it-yourself category will demonstrate healthy growth again this year, and we expect to benefit from that growth over time. Eric will give you some additional color on how we are trending season-to-date compared to the market.

LOOKING AHEAD

One of our shareholders commented that we are undertaking the largest transformation he's seen in any of his portfolio companies. It is a big undertaking, and we have a busy 2017 ahead as we complete the final stages of our transformation. We will finalize our go-forward leadership team, re-build the corporate team in Irving, and execute our plans in each business. We will also develop a clear path to capturing the synergy value we know exists. Some bumps in the road are to be expected, but we are committed to taking the right steps to build shareholder value over time.

With that, I will turn it over to Eric for more details on the financials.

ERIC EMANS, CHIEF FINANCIAL OFFICER

Thanks John.

We have a lot to cover today including fourth quarter and full year 2016 results, an update of our tax season expectations and first quarter 2017 outlook.

Let's start with a quick summary of our fourth quarter results which finished ahead of our expectations:

- Consolidated revenue of $86.8 million
- Adjusted EBITDA of $2.8 million
- Non-GAAP net loss of $7.5 million or an $0.18 cent loss per share, and
- GAAP net loss of $19.3 million or a $0.46 cent loss per share, which includes a restructuring charge of $3.9 million or a $0.09 cent loss per share and losses from discontinued operations of $5.1 million or a $0.12 cent loss per share

This translates to the following full year results and pro forma year on year growth:

- Consolidated revenue of $455.9 million, up 4%
- Adjusted EBITDA of $94.2 million, up 15%
- Non-GAAP net income of $45.1 million up 22% or $1.06 per diluted share which is up 20%, and
- GAAP net loss of $65.2 million or $1.57 loss per share, which again includes a restructuring charge of $3.9 million or a $0.09 cent loss per share and losses from discontinued operations of $63.1 million or a $1.48 cent loss per share

Turning to the balance sheet, we have cash, cash equivalents and short-term investments of $58.8 million. During the quarter, we paid down $38 million in debt which brings our total debt pay down for the year to $172 million. We exit the year with net debt of $377.2 million and a net leverage ratio of 4 times – quite a change from the greater than 6 times net leverage we entered the year with and highlights our execution toward our stated goal of 3 times net leverage. To this end we expect to utilize at least $30 million in cash from operations to pay down term loan B debt in the first quarter 2017.

Shifting to segment performance, beginning with Wealth Management.

HD Vest full year revenue was $316.5 million down 1% versus prior year on a pro forma basis, and segment income was $46.3 million and up about 8%. I think the best way to sum up this year is we started out with some challenges given market conditions including a S&P 500 52-week low in February, coupled with typical integration challenges that are to be expected with a significant acquisition. As we entered the second half of the year we began to build momentum boosted by the market. As a reminder, a positive market helps us in a couple ways – first we are about 50 percent correlated to the S&P 500 so upward movement grows our AUA and AUM benefiting fee-based and trailer revenue and second, we typically see increased inflows in times of S&P 500 growth. Additionally, we benefit in an increasing interest rates environment to the tune of approximately $2 million in annualized sweep revenue and segment income for every 25 basis point increase.

For the fourth quarter, HD Vest revenue was $83.0 million up 1 percent versus prior year and above the high-end of our guidance expectations for the quarter driven by other revenue which resulted in a gross margin increase of 6 percent. Fourth quarter segment income was $13.8 million up 13 percent versus prior year pro forma and again ahead of our expectations. The beat to expectations to segment income was driven by lower than expected costs and gross margin driven by revenue out performance.

The highlight in the quarter was net fee-based flows of $152 million. This came on the heels of the third quarter net fee-based flows of $132 million – it certainly feels like we have good momentum entering 2017. Total fee-based AUM as of the year-end is $10.4 billion, up 7 percent year-on-year and 2 percent sequentially and represents 26.9 percent of total AUA which is up 40 basis points versus last year. We are pleased to see a continued mix shift towards fee-based AUM. We exit the year with AUA of $38.7 billion, up 6% year-on-year and flat sequentially.

Turning to first quarter 2017 outlook – we expect revenue between $80.0 and $82.5 million and segment income of $11.0 to $12.0 million or a segment margin range of 13.8 to 14.5 percent.

Transitioning to Tax Preparation

TaxAct full year revenue was $139.4 million up 18% versus prior year and segment income was $66.9 million up 17% year-on-year. Simply stated, last year was a great year financially for TaxAct in the face of a significant pivot of our pricing and packaging model. And as we shared, we leaned toward segment income given our focus on paying down debt.

For the fourth quarter, TaxAct revenue was $3.8 million up 31% versus prior year and segment loss was $6.1 million which is up 35% over prior year as our investment leading into tax season was increased, primarily in marketing, and a bit more back end loaded versus the prior year.
Shifting to first half and first quarter 2017 outlook let me echo John's comments – the season is off to a very slow start. DIY efiles are off 21% thru February 3rd per the IRS weekly filing statistics and while the season was delayed for four days there seems to be other factors at play such as the PATH act which requires refunds involving the Earned Income Tax Credit and Additional Child Tax Credit be held until the latter part of February. It is also worth noting – that we don't believe or see any evidence that the slow start is suggesting a shift toward tax professionals, we expect DIY to continue to grow at a rate that outpaces overall filer growth.

For the same period, our efiles are down approximately 34 percent versus last year which is not too surprising that we are lagging the market due to our focus on paid units that typically file later in the season. We did make up some ground on units in the second week based on the IRS statistics and remain hopeful we can continue to do so as the season progresses.

Even with the challenges presented by the slow unit start we are confident that we will meet or exceed the high-end of our first half revenue outlook which called for 8 to 10 percent revenue growth versus the first half 2016. Our confidence is bolstered in large part by early season pricing action. This translates to a first half 2017 revenue outlook in the range of $144.0 to $148.0 million. Additionally, we believe on an absolute dollar basis we will likely come in toward the low-end of our first half 2017 segment income outlook of $81.5 to $84.5 million. This is largely driven by decreased marketing efficiency attributable to the season's slow start – in short our early dollars have been less efficient and we expect to need to deploy additional dollars through February.

Further, our first half 2017 outlook reflects investments to re-establish TaxAct as the challenger brand in the space in order to strengthen our competitive position. We are proceeding on these investments and testing a lot this season. Additionally, we may decide to accelerate certain investments as we exit the tax season – more to come on that in future calls as Sanjay and the team assess opportunities, but the message here is we are not going to pull back on investment to offset modest short-term margin compression.

As far as first quarter outlook we expect approximately 67 percent of first half revenue to hit in first quarter which translates to a range of $96.3 to $99.0 million. We expect segment income of $48.0 to $50.0 million or a segment margin range of 49.8 to 50.5 percent.

Let's close out 2016 with unallocated corporate operating expense.
For the full year, unallocated corporate operating expense came in at $19.0 million or up 7 percent versus prior year on a pro forma basis and included approximately $3.5 million in non-recurring costs. Fourth quarter was $4.9 million of which approximately $900 thousand were non-recurring. As a reminder non-recurring costs represent costs associated with our company's strategic transformation, which includes the integration of HD Vest and the divesture of non-core

assets, as well as costs associated with leadership transitions and the cost associated with move of our corporate headquarters that did not qualify for classification within restructuring.

Excluding non-recurring costs and annualizing the fourth quarter we are at a run rate of $16 million. So making good progress against our stated objective to materially reduce our unallocated corporate operating expense. In previous calls we have stated our end goal is to achieve $12 million in expenses annually but as we have gone through the budget process as well as thought through our operating model we expect that we will settle in the $13.0 to $13.5 million range which still represents mid-to-high 20 percent reduction when compared to 2015 pro forma. Obviously, with the headquarters move to Irving, Texas and leadership change at HD Vest we will have some significant non-recurring costs in 2017, that will primarily hit in the first half of the year.

As such, we expect first quarter unallocated corporate operating expense of $8.0 to $7.5 million of which approximately $4.0 million is non-recurring and includes $1.6 million associated with the HD Vest leadership transition.

With that let's turn to the first quarter 2017 consolidated outlook.

For the first quarter we expect revenue between $176.3 and $181.5 million, adjusted EBITDA between $51.0 and $54.5 million, non-GAAP net income of $40.2 to $43.9 million or a $0.90 to $0.98 cents per diluted share and GAAP income from continuing operations of $14.5 to $15.2 million or $0.32 to $0.34 cents per diluted share. As a reminder, GAAP income from continuing operations outlook includes a first quarter restructuring charge estimate of approximately $600 thousand but excludes any impact to tax expense for discrete items.

Before I turn the call back over to John, let me comment on our guidance approach to 2017. At this time, we are not providing full year outlook – this is primarily driven by the uncertainty that still remains around the DOL rule. In addition, with the new leadership at both of our business units, we are going to provide these leaders an opportunity to come in and assess their respective organizations and opportunities to drive long term value. This may involve some added investments in the second half. You can expect us to provide additional clarity over the next couple of earnings calls. However, it's important to note we have provided first half 2017 outlook for TaxAct which represents the lion's share of the segment's full year earnings.

Let me emphasize this does not change our view that these businesses will continue to grow top-line consistently in the mid to upper single digits and may grow faster depending on market conditions and/or the success of our synergy growth initiates. John…..

JOHN CLENDENING, PRESIDENT AND CHIEF EXECUTIVE OFFICER

Before we open for questions, I want to thank our employees for the strong performance this quarter. I am proud of our achievements – we beat fourth quarter expectations, are entering the year with increased momentum at HD Vest, and despite a slow start to the tax season we are reiterating our guidance.

Let me close by expressing my gratitude to our shareholders, clients, customers, advisors and employees. We feel deep accountability to each of you, and the team and I are focused on continuing to position the company for long-term growth, benefiting each one of our constituents.