Intuit Inc.
Third-quarter Fiscal 2017
Conference Call Remarks
May 23, 2017

Introduction

Good afternoon and welcome to Intuit's third-quarter fiscal 2017 conference call. I'm here with Brad Smith, our chairman and CEO, and Neil Williams, our CFO.

Before we start, I'd like to remind everyone that our remarks will include forward-looking statements. There are a number of factors that could cause Intuit's results to differ materially from our expectations. You can learn more about these risks in the press release we issued earlier this afternoon, our Form 10-K for fiscal 2016 and our other SEC filings. All of those documents are available on the Investor Relations page of Intuit's website at intuit.com. We assume no obligation to update any forward-looking statement.

Some of the numbers in these remarks are presented on a non-GAAP basis. We've reconciled the comparable GAAP and non-GAAP numbers in today's press release.

Unless otherwise noted, all growth rates refer to the current period versus the comparable prior-year period, and the business metrics and associated growth rates refer to worldwide business metrics.

A copy of our prepared remarks and supplemental financial information will be available on our website after this call ends.

With that, I'll turn the call over to Brad.

Third-quarter Fiscal 2017 Overview

Thanks Jerry, and thanks to all of you for joining us.

We're pleased with our performance in our third fiscal quarter. As you know, this is our largest quarter of the year, and we successfully delivered strong financial results in a complicated tax season.

Exiting the quarter, our Consumer Tax revenue is up 9 percent year to date and is on track to finish at the high end of our guidance range for the full fiscal year. We're also driving continued momentum in our small business franchise, with QuickBooks Online subscriber growth accelerating to 59 percent and over 2.2 million subscribers, which is above the upper end of the target we established for the full fiscal year.

As a result, we're raising our outlook for QBO subscribers to 2.3 million, we're raising our full-year revenue guidance and we're tightening the earnings per share range to the high end. All in all, we're on track to deliver another good year.

With that overview, let me click down into the drivers of our performance in the third quarter, beginning with our tax results.

This tax season proved to be eventful from beginning to end, with a delayed start to tax filings compared to prior years, a renewed competitive environment in the "free" category and new Internal Revenue Service requirements designed to reduce fraud.

The combination of these factors were reflected in the four key drivers of the tax business that we discuss with you on a regular basis:

- The first driver is overall growth in the number of tax returns filed with the IRS. The latest IRS data indicates that total returns are down slightly, below the 0 to 1 percent growth we had forecasted. If this trend plays out for the remainder of the tax filing year, it will be the slowest growth in total tax returns since 2013.

- The second driver is the percentage of returns filed using do-it-yourself software. To date, DIY category share has grown two-tenths of a point, less than the 1.2 points we had expected. With that said, DIY category growth once again outpaced the year-over-year declines in the assisted tax prep methods.

- The third driver is TurboTax's share within the DIY category. After strong share gains the past several seasons, our share of DIY e-files this season was flat. This performance is below the 1 point of share gain we strive to achieve each year, and we're already designing innovative ways to accelerate customer growth as we look ahead to next season.

- The fourth driver is revenue per return, which finished stronger than our multi-year average of 1 percent. Our pricing was relatively stable this season, so the benefit resulted from a mix-shift to the higher end of our product lineup.

While the drivers of our tax results played out differently than expected, I am proud of the agile execution and innovation the team delivered this season. If you recall the game plan our team shared at our Investor Day last fall, we outlined a plan to extend our leadership in DIY tax, begin transforming the assisted tax category, and run experiments to evolve beyond tax through a trusted, open platform.

This season, we made progress across several fronts:

- We leaned into SmartLook, providing broad access to an expert with the simple touch of a finger at a much lower cost than going to a tax store.

- We also began driving value through the broader Intuit ecosystem, leveraging the credit score functionality in Mint to provide more than 1.3 million free credit scores to TurboTax customers this season.

- And we introduced a self-employed bundle of QuickBooks and TurboTax, targeting the freelancer and gig economy, driving strong results which I'll discuss in greater detail in a minute.

All of this is built on the investments we've made in innovation over the past several years in areas such as artificial intelligence, where we've applied for more than 100 patents and have more than 30 AI applications in market across the company.

Putting a bow around Consumer Tax, we're exiting this season with strong financial results, although generated in ways that were different than we had expected. We'll learn from our experience this season and continue to invest in our multi-year strategy to deliver against our long-term objectives. We'll share more details on our results and our long-term strategy at our annual Investor Day in the fall.

With that overview on the Consumer Tax side of the business, let's shift to the assisted tax results in ProConnect.

This business delivered results that were better than our expectations, with year-to-date revenue growth of 2 percent. ProConnect plays an important role across our ecosystem, with approximately 60 percent of our TurboTax SmartLook agents being staffed by ProConnect tax experts this season. We've also seen early success in driving QBO subscribers through our tax sales efforts, fostering growth within our QuickBooks Online franchise.

With that overview on tax, let me now shift to small business.

Subscriber growth continues to accelerate, driven by improvements across our platform serving the self-employed, small businesses and accountants. We've also increased our marketing effectiveness and expanded our addressable footprint internationally in the self-employed segment. As I mentioned earlier, total QBO subscribers grew 59 percent in the quarter, up from 49 percent growth in the second quarter. Our TurboTax Self-Employed offering contributed 11 points to this subscriber growth rate.

We continue to drive strong growth in both our core U.S. business and international markets. Outside the U.S., our subscriber base grew 70 percent year over year to 433,000 subs, up from 61 percent growth in Q2.

Within QuickBooks Online, QuickBooks Self-Employed subscribers doubled to 360,000, up from 180,000 last quarter, and 75,000 a year ago. During Q3, we launched QuickBooks Self-Employed in Singapore, adding another geography to our lineup. We expect to launch in Hong Kong and South Africa soon, as well.

Finally, our TurboTax Self-Employed offering has contributed approximately 160,000 subscribers to the QuickBooks Self-Employed total so far this year. Our tax customer base is proving to be a great channel for reaching the self-employed, as we know nearly 4 million TurboTax customers are self-employed tax filers. We're pleased to report that QuickBooks Self-Employed customers who come through TurboTax have higher product recommendation scores as well.

Our momentum in QBO subscriber growth is driving top line revenue, with online ecosystem revenue growing 30 percent again this quarter, at the high end of our 25 to 30 percent target range. We expect online accounting to be the primary driver of online ecosystem revenue for the foreseeable future, as we prioritize seeding the global market with QuickBooks Online.

Add-on services such as payroll and payments – the blades to the QBO razor – certainly remain important, and will play an increasingly larger role in later chapters, but our strategic priority at this time is getting more QBO razors in the market. This playbook should sound familiar, as it served us well for decades in the QuickBooks desktop franchise.

Putting it all together, our strategy of a vibrant One Intuit Ecosystem is gaining real momentum. We're seeing proof points with more ecosystem connections between customers and products creating greater value for our customers, and sources of competitive advantage for Intuit.

Whether it's TurboTax driving QuickBooks Self-Employed subscribers, ProConnect accountants serving TurboTax customers through SmartLook, or Mint credit scores being delivered to TurboTax customers, we're unleashing the power of many for the prosperity of one. You'll hear more from us on this front in the coming months.

With that overview I'll hand it to Neil to walk you through the financial details.

Financial Results and Segment Details

Thanks, Brad and good afternoon everyone.

For the third quarter of fiscal 2017, we delivered:

- Revenue of $2.5 billion, up 10 percent year over year.
- GAAP operating income of $1.4 billion, versus $1.3 billion a year ago.
- Non-GAAP operating income of $1.5 billion, versus $1.4 billion last year.
- GAAP diluted earnings per share of $3.70 versus $3.94 last year.
- And non-GAAP diluted earnings per share of $3.90, up from $3.43 last year.
- As a reminder, our GAAP results last year included $0.68 per share from the sale of discontinued operations.

Business Segment Results

Turning to the business segments:

Consumer and Professional Tax

Consumer Tax revenue is up 10 percent in the quarter, 9 percent year to date. Our unit growth was 2 percent and we saw a mix-shift to the higher end of our product lineup, increasing our average revenue per customer. We held share in the category this year, but we did not grow units faster than revenue. This is not consistent with our long-term principle, and we're addressing it in our strategy for next year.

We have had questions on the difference between unit and e-file growth this season, so let me explain. We grew units 2 percent this season, but our e-file growth was flat. New Internal Revenue Service security measures this tax year mandated the only way to e-file is to enter the prior-year adjusted gross income or your existing filing PIN. Many of our new customers had difficulty with this, causing them to print and mail their returns instead of e-filing.

Although these returns were prepared with our software - and customers paid for them - the mailed returns are not included in e-file results reported by the IRS. Nor are they counted in our share calculations, which are based on e-filed returns. We saw at least an incremental 500,000 returns this year that were paid for but not e-filed.

ProConnect revenue was $116 million in Q3, down 8 percent from Q3 last year, reflecting the timing shifts from forms availability we discussed last quarter. Year to date, our ProConnect revenue is $327 million, a little better than our expectations and last year.

Small Business

Moving to Small Business:

Total Small Business revenue grew 16 percent in the quarter.

QuickBooks Online subscriber growth remains strong and we exceeded our guidance for the quarter and the full year, reaching 2,220,000 subscribers, up 59 percent year over year. TurboTax was a significant channel for QuickBooks Self-Employed in Q3, accounting for 11 points of growth.

Small Business online ecosystem revenue grew 30 percent for the second consecutive quarter. This is at the high end of the 25 to 30 percent growth range we’ve talked about and is driven by continued growth of online accounting revenue.

Our online payroll and payments businesses remain healthy, growing 19 percent and 9 percent this quarter, respectively. As we’ve told you before, a portion of each of these businesses are attached to QuickBooks Online and a portion is made up of standalone customers who are not connected to QuickBooks.

Online payroll revenue attached to QuickBooks makes up about 45 percent of our online payroll revenue. That revenue grew 35 percent in the quarter, with subscriber growth of 21 percent. In contrast, online payroll revenue unattached to QuickBooks grew 1 percent.

Online payments revenue attached to QuickBooks makes up about 60 percent of our online payments revenue. That revenue grew 33 percent in the quarter, with active payments customer growth of 47 percent. As we've mentioned in the past, we are not investing in acquiring standalone payments customers and that portion of the portfolio is declining. Revenue for these online payments customers not attached to QuickBooks fell 15 percent.

Our small business desktop ecosystem revenue grew 12 percent. About 6 points of this revenue growth is related to a SKU we introduced at retail last year. This SKU gave desktop customers a QuickBooks license, and the right to access the QuickBooks Online service for one year at no additional charge. This required us to defer a portion of the related revenue. These rights expired in Q3, resulting in recognition of this revenue.

Desktop units declined 15 percent year over year, and units were 3 percent below last year on a year-to-date basis. For fiscal 2017, we expect QuickBooks desktop units to decline mid-single digits and desktop ecosystem revenue to be up mid-single digits. That growth is driven by ratable revenue recognition and continued strength in our QuickBooks Enterprise business.

Financial Principles and Capital Allocation

Turning to our financial principles, we continue to take a disciplined approach to capital management, investing the cash we generate in opportunities that yield a return on investment greater than 15 percent.

With approximately $1.6 billion in cash and investments on our balance sheet, our first priority is investing for customer growth.

Our goal is to drive double-digit revenue growth and to grow operating income in the mid-teens.

We return excess cash to shareholders via both share repurchases and dividends.

- We repurchased approximately $90 million of shares in the third quarter and $1.9 billion remains on our authorization.
- We used some of our operating cash to repay $500 million in senior notes that matured in March and $150 million on our revolver.
- The board approved a dividend of $0.34 per share, payable on July 18, 2017.

Q4 Fiscal 2017 Guidance

We are raising our full-year QBO subscribers and total company revenue guidance, and narrowing operating income and EPS to the high end of the range. We now expect total company revenue growth of 9 to 10 percent for the year.

You can find our fiscal 2017 Q4 guidance details in our press release and on our fact sheet.

With that, I'll turn it back to Brad to close.

Closing Comments

Thanks, Neil.

- Q3 was another strong quarter for Intuit, with a hard-fought tax season that had some bright spots, as well as opportunities to improve, but ultimately delivered at the high end of our revenue guidance for the tax business.
- Small Business continues to gain momentum, with accelerating QBO subscriber growth leading to an increase in our full-year subscriber outlook, and online ecosystem revenue topping the high end of our 25 to 30 percent target range as well.
- Collectively, we're driving strong progress with our One Intuit Ecosystem strategy, creating greater value for our customers and building new sources of competitive advantage.

With that summary, let's open it up to you to hear what's on your mind.

Cautions About Forward-looking Statements

These materials contain forward-looking statements, including forecasts of expected growth and future financial results of Intuit and its reporting segments; Intuit's prospects for the business in fiscal 2017 and beyond; expectations regarding Intuit's growth outside the US; expectations regarding timing and growth of revenue for each of Intuit's reporting segments and from current or future products and services; expectations regarding customer growth; expectations regarding the impact of the One Intuit Ecosystem strategy on Intuit's business; expectations regarding changes to our products and their impact on Intuit's business; expectations regarding the amount and timing of any future dividends or share repurchases; expectations regarding availability of our offerings; expectations regarding the impact of our strategic decisions on Intuit's business; and all of the statements under the heading "Q4 Fiscal 2017 Guidance."

Because these forward-looking statements involve risks and uncertainties, there are important factors that could cause our actual results to differ materially from the expectations expressed in the forward-looking statements. These factors include, without limitation, the following: inherent difficulty in predicting consumer behavior; difficulties in receiving, processing, or filing customer tax submissions; consumers may not respond as we expected to our advertising and promotional activities; the competitive environment; governmental encroachment in our tax businesses or other governmental activities or public policy affecting the preparation and filing of tax returns; our ability to innovate and adapt to technological change; availability of our products and services could be impacted by business interruption or failure of our information technology and communication systems; any problems with implementing upgrades to our customer facing applications and supporting information technology infrastructure; any failure to properly use and protect personal customer information and data; our ability to develop, manage and maintain critical third-party business relationships; increases in or changes to government regulation of our businesses; any failure to process transactions effectively or to adequately protect against potential fraudulent activities; any loss of confidence in using our software as a result of publicity regarding such fraudulent activity; any significant product accuracy or quality problems or delays; any lost revenue opportunities or cannibalization of our traditional paid franchise due to our participation in the Free File Alliance; the global economic environment may impact consumer and small business spending, financial institutions and tax filings; changes in the total number of tax filings that are submitted to government agencies due to economic conditions or otherwise; the seasonal and unpredictable nature of our revenue; our ability to attract, retain and develop highly skilled employees; increased risks associated with international operations; unanticipated changes in our income tax rates; changes in the amounts or frequency of share repurchases or dividends; we may issue additional shares in an acquisition causing our number of outstanding shares to grow; our inability to adequately protect our intellectual property rights may weaken our competitive position; disruptions, expenses and risks associated with our acquisitions and divestitures; amortization of acquired intangible assets and impairment charges; our use of significant amounts of debt to finance acquisitions or other activities; and the cost of, and potential adverse results in, litigation involving intellectual property, antitrust, shareholder and other matters. More details about the risks that may impact our business are included in our Form 10-K for fiscal 2016 and in our other SEC filings. You can locate these reports through our website at http://investors.intuit.com. Forward-looking statements are based on information as of May 23, 2017, and we do not undertake any duty to update any forward-looking statement or other information in these materials.