Investor briefing

Full year results to 31 March 2018

Xero

10 May 2018  Junk & Disorderly, Auckland
Important notice

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• includes forward-looking statements about Xero and the environment in which Xero operates, which are subject to uncertainties and contingencies outside of Xero’s control. Xero’s actual results or performance may differ materially from these statements
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All information in this presentation is current at 31 March 2018, unless otherwise stated

All currency amounts are in NZ dollars, unless otherwise stated

See page 32 for a glossary of the key terms used in this presentation
Agenda

Business overview
Steve Vamos
Chief Executive Officer

Operating performance
Sankar Narayan
Chief Operating and Financial Officer

Financial results
Kirsty Godfrey-Billy
Chief Accounting Officer

Outlook

Q&A
Business overview

Steve Vamos
Chief Executive Officer
Xero platform – scalable growth through partners

**For small business**
Small businesses can manage their day-to-day finance with software that’s smart and easy-to-use, having instant access to their data and files.

**For accounting partners**
Accounting partners can connect their clients’ data and work efficiently, bringing various work streams of their practice on to one platform in the cloud.

Platform
Leveraging machine learning and artificial intelligence

Single ledger, data and documents

**Growth drivers**
- Deeper penetration in existing markets and geographic expansion
- Adjacent products for small businesses and accounting partners
- Transactional activities
- Finweb
- Other data driven solutions

**For small business**
- Online invoicing and quotes
- Reporting
- Information security
- Projects
- Expenses
- Inventory
- Purchase orders
- Dashboards
- Payroll
- Payments
- Multi-currency
- Bank feeds and reconciliation
- Contacts
- Compliance
- HQ apps and explorer
- Practice management
- Workpapers
- Advisor directory
- Tax solutions
- Reporting

**For accounting partners**
- Connected app ecosystem
- Multi-currency
- Payroll
- Online invoicing and quotes
- Reporting
- Information security
- Projects
- Expenses
- Inventory
- Purchase orders
- Dashboards
- Payroll
- Payments
- Multi-currency
- Bank feeds and reconciliation
- Contacts
- Compliance
- HQ apps and explorer
- Practice management
- Workpapers
- Advisor directory
- Tax solutions
- Reporting
Focus going forward

- Continued alignment with strategy
- Global and regional operating model
- Great product management
- Capital investment framework
Xero’s mission is to rewire the global economy, connecting millions of businesses to their banks, advisors and each other

- Great people and teams
- Win with accountants and bookkeepers
- Beautiful products and global platform
- Grow into new spaces and places
- Love and protect our customers
- Build to scale globally
Operating performance

Sankar Narayan
Chief Operating and Financial Officer
Positive EBITDA with continued growth

- **AMRR**
  - $484.4m
  - +33% YOY

- **Subscribers**
  - 1.4m
  - +351,000 YOY

- **Positive EBITDA**
  - $26.0m
  - +$55m YOY

- **Operating Revenue**
  - $406.6m
  - +38% YOY

- **Operating Cash Flow**
  - $41.2m
  - +46m YOY

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1 See page 32 for details on annualised monthly recurring revenue
Consolidated listing on the ASX – inclusion in S&P/ASX 100

- Access to a larger market
- Increased liquidity
- Increased relevance to a more diverse range of larger investors
- Broader analyst and broker coverage
Listed ASX & NZX tech companies by revenue growth and market capitalisation

Source: FactSet
Note: Analysis excludes companies under A$50 million market capitalisation and share registry companies
1,386,000
Subscribers
$484m
Annualised monthly recurring revenue

$121m
added in 12 months
Cash outflow\(^1\) as % of revenue

\((71\%) \text{ to } (9\%)\) in 3 years

\(^1\) Operating and investing cash flows
Increasing lifetime value

<table>
<thead>
<tr>
<th></th>
<th>March 2018</th>
<th>Progress from March 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>ARPU</td>
<td>$29.13</td>
<td>—</td>
</tr>
<tr>
<td>MRR churn %</td>
<td>1.10%</td>
<td>—</td>
</tr>
<tr>
<td>Gross margin</td>
<td>81%</td>
<td>—</td>
</tr>
<tr>
<td>LTV per subscriber¹</td>
<td>$2,310</td>
<td>+9%²</td>
</tr>
</tbody>
</table>

Total group subscriber lifetime value (LTV)

$990m ($1.0b in CC²) added in 12 months

1 Increased 8% YOY in nominal terms
2 Constant currency based on FX rates at 31 March 2017
Contribution margins improving

Australia and New Zealand improvements highlight continuing efficiencies and operating leverage.

International investment loss reduced even with investments in new geographies such as South East Asia. Strong revenue growth rate for the international segment of 49% YOY.
Australia and New Zealand

Australia

- 31% subscriber growth to 583,000 subscribers (adding 137,000 in the period). Revenue growth of 35% YOY
- Extending partnership with NAB on payments and data
- Xero Small Business Insights highlights real-time trends in the small business economy

New Zealand

- 22% subscriber growth to 301,000 subscribers (adding 55,000 in the period). Revenue growth of 27% YOY
- With good market penetration and moderating subscriber growth, the focus is on deepening customer relationships and leveraging platform strengths

Graph source: Google trends of Xero and competitor products
United Kingdom

47% subscriber growth to 312,000 subscribers (adding 100,000 in the period). Revenue growth of 60% YOY

Leadership position further enhanced with cloud based accounting revenue growth. Overtaken New Zealand to be the second largest region behind Australia

Xerocon London is now UK’s largest accounting industry conference with over 2,000 attendees in October 2017

Open Banking, Payment Services Directive (PSD2) and HMRC Making Tax Digital continue to create favourable market conditions. Added support for HMRC Construction Industry Scheme (CIS)

A number of new Finweb partnerships launched including Worldpay, UK’s largest merchant acquirer

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**Graph source:** Google trends of Xero and competitor products
North America

43% subscriber growth to 132,000 subscribers (adding 40,000 in the period). Revenue growth of 28% YOY

Continued focus on strengthening the accounting partner channel, making inroads into mid and large size accounting firms

Under-penetrated cloud accounting market with slow market adoption in the small business accounting segment

Improvement in Google search trends YOY, and brand position expected to improve with further accounting partner channel buildout

Strengthening banking relationships with new partners including a top five Canadian bank

Accounting partner channel capacity¹

¹ Capacity is the number of small business subscribers connected to Xero’s certified and revenue generating partner base
Rest of World

49% subscriber growth to 58,000 subscribers (adding 19,000 in the period). Revenue growth of 47% YOY

South East Asia

• Enhancing financial partnerships and integrations. Improving brand position in the cloud accounting market
• Focus on developing the accounting partner channel

South Africa

• Continuing to gain traction among accounting partners and small businesses
• Over 1,200 attendees at the 2018 roadshows

Graph source: Google trends of Xero and competitor products
Growing the small business platform

- **Core accounting**: 1%
- **Platform revenues**: 3%
- **WorkflowMax**: 3%
- **Non-recurring**: 1%

**Group operating revenue**

- Total: $406.6m
- Core accounting: $17.3m (37%
- Platform revenues: $375.3m (94%)
- WorkflowMax: $117.7m (29%)
- Non-recurring: $13.7m (50%)

1. Platform revenues include revenue derived from related services, including add-ons with incremental revenue (such as payroll and expenses modules) and revenue share agreements with partners.
2. Revenues relating to Workflowmax, online workflow and job management software.
3. Non-recurring includes revenue from events (such as Xerocons and roadshows), and other non-subscription or platform services.
Financial results

Kirsty Godfrey-Billy
Chief Accounting Officer

Little Veggie Patch, Melbourne
## Financial performance

Operating revenue growth of 38% YOY driven by Australia and New Zealand segment growth of 33% and International segment growth of 49%

ARPU is stable compared to FY17

Earnings improvement driven by operating efficiencies

Continued investment in geographic expansion and new products

EBITDA impacted by $1.5m in costs relating to ASX consolidation and higher share-based payments. Share-based payments increased 45% to $17.0m in FY18

Product capitalisation rate was lower YOY at 42%

<table>
<thead>
<tr>
<th></th>
<th>FY17 ($000s)</th>
<th>FY18 ($000s)</th>
<th>YOY change ($000s)</th>
<th>YOY change (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total operating revenue</td>
<td>295,389</td>
<td>406,579</td>
<td>111,190</td>
<td>38%</td>
</tr>
<tr>
<td>Gross profit</td>
<td>226,004</td>
<td>330,333</td>
<td>104,329</td>
<td>46%</td>
</tr>
<tr>
<td>Gross margin</td>
<td>77%</td>
<td>81%</td>
<td>+4pp</td>
<td></td>
</tr>
<tr>
<td>EBITDA</td>
<td>(28,614)</td>
<td>26,006</td>
<td>54,620</td>
<td>n/m¹</td>
</tr>
<tr>
<td>EBITDA margin</td>
<td>(10%)</td>
<td>6%</td>
<td>+16pp</td>
<td></td>
</tr>
<tr>
<td>Net loss</td>
<td>(69,057)</td>
<td>(27,843)</td>
<td>41,214</td>
<td>60%</td>
</tr>
<tr>
<td>EBITDA excl. SBP</td>
<td>(16,891)</td>
<td>43,010</td>
<td>59,901</td>
<td>n/m¹</td>
</tr>
<tr>
<td>EBITDA excl. SBP margin</td>
<td>(6%)</td>
<td>11%</td>
<td>+17pp</td>
<td></td>
</tr>
</tbody>
</table>

¹ Not meaningful
Improving gross margin

Gross margin of 81% for FY18, +4pp over prior year

Realised benefits of AWS platform since successful migration in H2 FY17

Opportunities to further increase gross margin with further efficiencies in AWS platform and automation in customer experience

Gross profit as percentage of revenue

81%

FY16 FY17¹ FY18

¹ Duplicated costs due to transition to AWS
Positive EBITDA

First positive EBITDA for the full-year driven by operating efficiencies across the business

EBITDA excl. SBP\(^1\) was $43.0m in FY18, an improvement of $59.9m YOY from $(16.9m) loss in FY17

\(^1\) SBP is a non-cash cost to Xero
Improved product and acquisition efficiencies

Next phase of investment in realising benefits from a single global platform

Investments focused on driving future ARPU and revenue growth:

- Strengthening core product and platform leveraging machine learning and artificial intelligence
- Adjacent products for small businesses and accounting partners
- Transactional activities
- Finweb
- Other data-driven solutions

Product costs including opex and capex as % of revenue

LTV to CAC

1 Net of government grants
Positive operating cash flow

Positive operating cash flow of $41.2m for FY18, an improvement of $45.6m from $(4.4m) in FY17.

Operating and investing cash flows as a % of revenue improved to 9% in FY18. Total operating and investing cash flows was $(36.9m) for FY18, a reduction from $(70.8m) in FY17.

Cash and short-term deposits balance at 31 March 2018 was $80.0m.

No current plans to draw down on two-year stand-by debt facility of $100m.
Outlook
Xero will continue to focus on growing its global small business platform

Cash outflow\(^1\) in FY19 is forecast to reduce from FY18. Xero is managing the business to cash flow break-even within its current cash balance (without drawing on its debt facility) through operational efficiencies

Following cash flow break-even, it is intended that surplus cash flow will be reinvested, subject to investment criteria, to drive long-term shareholder value

\(^1\) Operating and investing cash flows
Appendix
Glossary

Subscribers
Subscriber means each unique subscription to a Xero-offered product that is purchased by an accounting partner or an end user and is, or is available to be, deployed.

AMRR
Annualised monthly recurring revenue (AMRR) represents monthly recurring revenue at 31 March, multiplied by 12. It provides a 12 month forward view of revenue, assuming any promotions have ended and other factors such as subscriber numbers, transaction volumes, pricing and foreign exchange remain unchanged during the year.

ARPU
ARPU is calculated as annualised monthly recurring revenue at 31 March divided by subscribers at that time (and divided by 12 to get a monthly view).

MRR churn
MRR churn is the value of monthly recurring revenue (MRR) from subscribers who leave Xero in a month as a percentage of the total MRR at the start of that month. The percentage provided is the average of the monthly churn for the previous 12 months.

Total lifetime value
LTV is the gross margin expected from a subscriber over the lifetime of that subscriber. This is calculated by taking the average subscriber lifetime (1 divided by MRR churn) multiplied by ARPU multiplied by the gross margin percentage. Group LTV is calculated as the sum of the individual segment LTVs, multiplied by segment subscribers, divided by total Group subscribers.

CAC months
CAC months or months of ARPU to recover CAC represent the number of months of revenue required to recover the cost of acquiring each new subscriber. The calculation is sales and marketing costs for the 12 month period less conference revenue (such as Xerocon) divided by gross new subscribers added during the same period, divided by ARPU.

Opex
Operating expenses

SBP
Share-based payments

Capex
Capital expenditure

Finweb
Financial web

CAC
Customer acquisition costs

GAAP
Generally accepted accounting principles