



## TurboTax LIVE is a game changer

### Q3 2018 was the first data point on TurboTax Live - it said pay attention

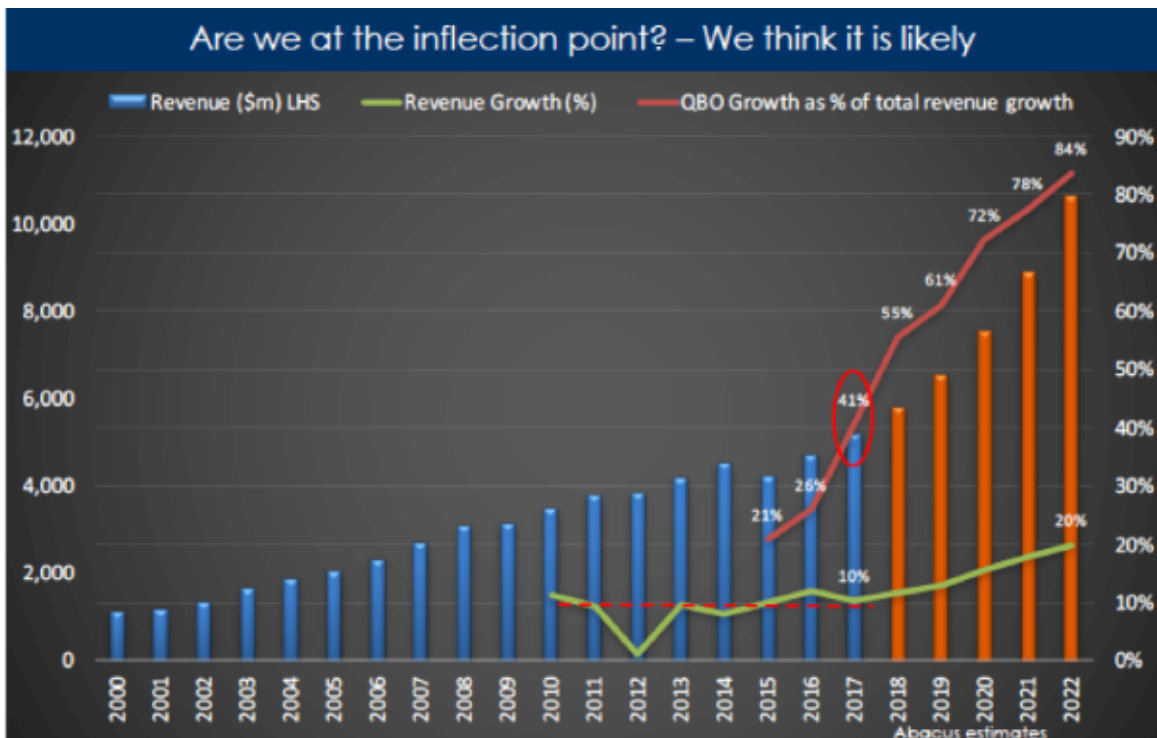
- We think TurboTax Live is a structural change in the tax market.
- Estimate INTU upside to \$263 (+34%)
- Estimate that there is a high chance TurboTax Live revenue contribution in FY18 was ~\$100m and there are potentially 670k Live customers today.
- TAM for Live is at least \$5bn.
- Estimate potential revenue growth acceleration to 16% vs street at ~9%.

### Core thesis remains unchanged

Our [initial report on INTU](#) in Nov 2017 had 50% upside based almost entirely on QuickBooks Online (QBO). Our upside **thesis was that QBO was winning the land grab for a truly huge TAM and we had high confidence in their ability to grow at 40%** for a prolonged period of time.

Since Q1 FY2016 QBO growth has shown a consistent acceleration in revenues to 40% and average subscriber growth of 51%. It has also shown better mix than we were predicting. Fewer self-employed subscribers, more core subs. So, all in all **we continue to have confidence that our upside driven by QBO is in play, and not fully discounted in the stock.**

Ignoring the changes in TurboTax, we had upside to \$227 - this still stands.



## Turbo Tax just became a second accelerating growth driver

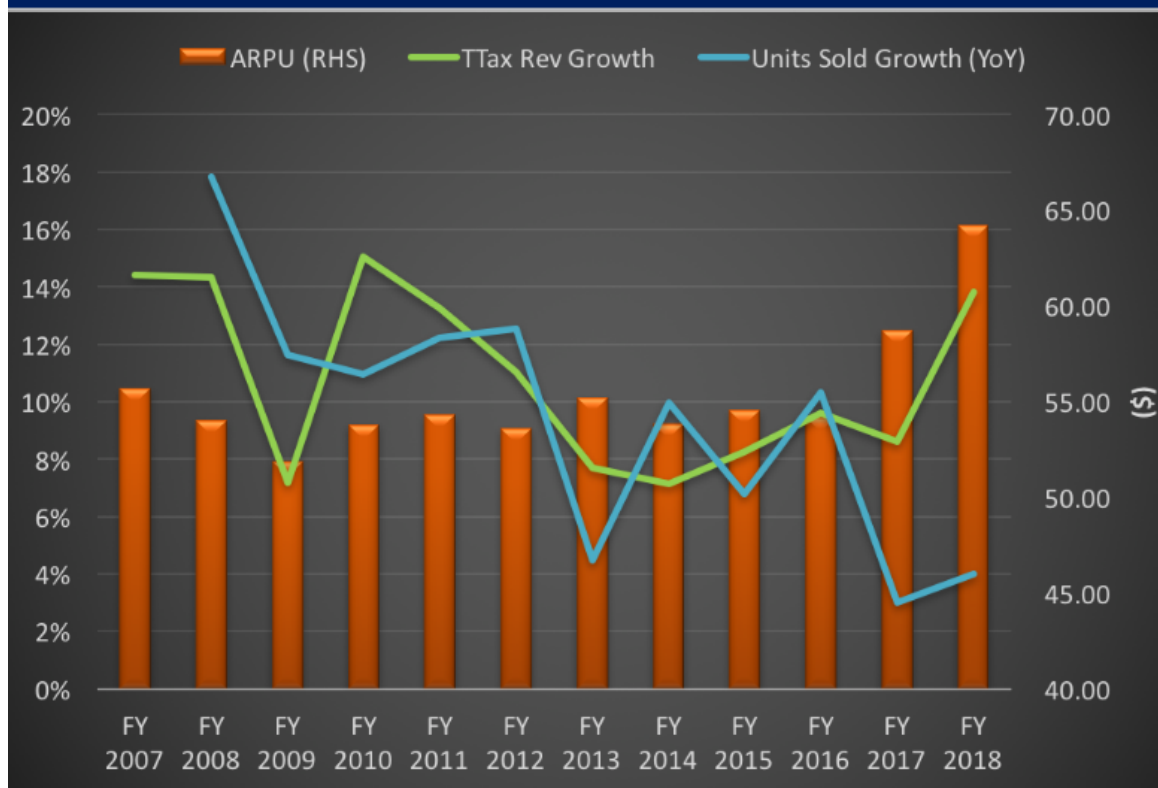
Where Q3 FY18 really changed our opinion was on numbers for TurboTax.

**Turbo Tax is becoming a disruptive platform.**

Total TurboTax growth for FY 2018 will be 14%. Driven by:

- 4% volume growth
- 10% ARPU growth

## ARPU Acceleration after 6 years of calm



### That now makes two years of ARPU growth driven by mix and pricing

FY 2017 ARPU growth:

- Benefitted from a **mix shift to the higher end of their product range.**
- Complicated tax season due to delayed start and new IRS requirements to combat fraud.

FY2018 ARPU growth:

- **Mix shift to higher value product - mostly Live?**
- Attach / Cross sell
- Pricing

### We think this is probably the beginning of a long term trend

**Our prior upside estimates had 8% TTax growth for FY2018, falling to 6% over 3years. 3% volume growth, 3-4% pricing.**

**As TurboTax is 42% of revenues, 14% has a meaningful impact if it is sustainable.** The problem with INTU is that we now have to wait 12 months until we get another meaningful number on TurboTax growth.

## If TurboTax is structural, we estimate Upside to \$263 (+34%)

**Assuming TTax Live change is structural, we estimate the revenue growth of INTU over the next 4 years in Scenario 3 below.**

- Total company revenues would be growing at a sustainable 16%.
- 84% GM's and expanding operating margins as growth slows. **Gives upside to \$263 (34%)**
- Street continues to estimate a fading growth scenario, not that dissimilar to our downside revenue assumptions.
- We have not changed our upside QBO scenario.

Intuit Total Revenue Growth					
	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
1) Abacus Downside Ests	13.2%	8.5%	7.8%	7.5%	7.3%
2) Street Assumptions	14.0%	10.0%	9.0%	8.0%	7.0%
3) Abacus Upside Ests	14.4%	12.5%	16.2%	15.9%	16.2%

## The potential Live market is easily large enough

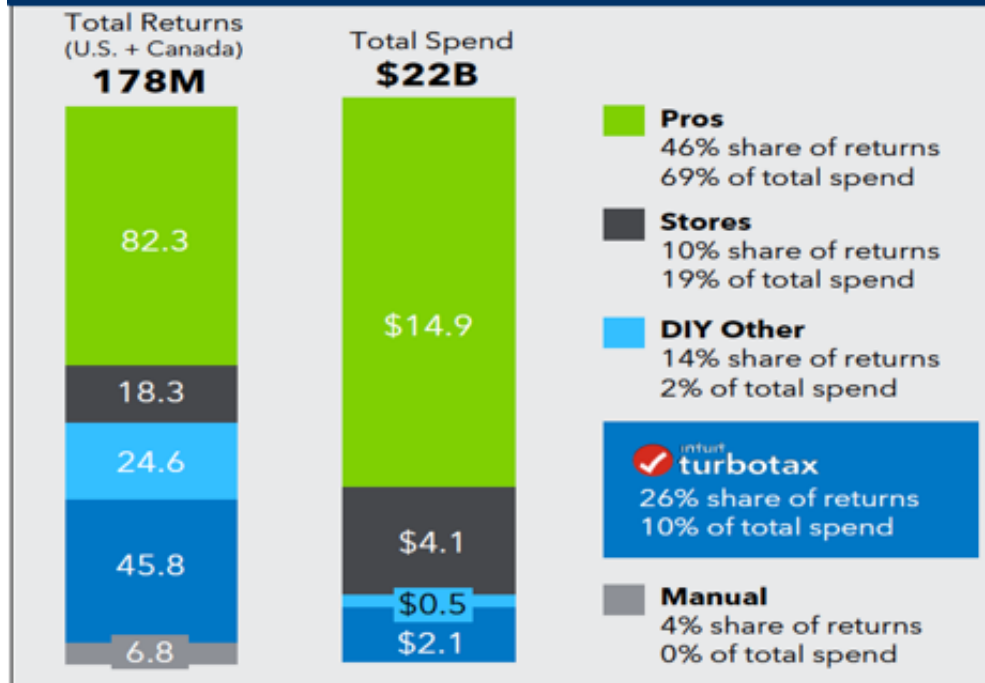
- **Intuit states that there are 30m filers out of 100m Pro&store filers that file simple returns but still go to a tax pro.**
- Intuit also has 3m filers per year that start on TTax, but churn off "because of a nagging question" assumedly to go to a pro for help.
- 3m to 5m people enter the tax category for the first time each year.

**Therefore, we can assume that there are at least 33m customers a year that a price insensitive/ happy to pay at least \$273 to file their taxes.** (According to the NSA survey, it costs an average of \$273 for filing a 1040 + state taxes via an accountant)

TTax is pricing an equivalent service at:  $\$180 + \$40 = \$220$ .

**I.e. it is at least a \$5bn TAM, vs current \$2.5bn in TTax revenues.**

## TurboTax can now go after the green bit



### With at least 33m customers to go after 15% sustained growth doesn't seem so challenging.

2018 Revenues for TTax will be \$2.5bn. with underlying growth of ~7%. (3% volume, 4% pricing)

- **I.e. to grow at 15% TTax needs an incremental \$200m in TTax revenues.**
- **\$200m from Live = 1.1m new customers per year, from a pool of at least 33m.**

### How does TurboTax Live work?

**TurboTax Live is a two sided network**, with a huge amount of automation (TTax software) sandwiched between.

- Live enables customers to ask questions at any point in the process of filling out a tax return and get a video / telephone call answer from a pro.

**In 2018 T.Tax Live had 2,000 pros (mostly accountants) connected to the system.**

- Pros, work from home, are paid per hour, where pay determined by regional location and years of experience. There is a bonus paid out at the end of the season based upon performance. (Performance depends on customer feedback, issue resolution, and completion of the assigned season)

A key feature is a live one-on-one video review of your filing before you submit it.

Live costs \$180, but was discounted to ~\$150 in FY2018.

## TurboTax Live Investment and Risks

FY2018 was an experiment. **2019 is going to see a big sales and marketing focus.**

- conf call: *Marketing: "we are confident enough we're going to put our foot on the gas with TurboTax Live."*
- ***"I don't believe that you see a onetime event here. I think you're starting to see a structural shift in the business economics"***

FY 2018 had dual marketing campaigns, one for free product and another at high end. Given the growth, it is clear that both worked at the same time.

**The biggest risk we see is that Incremental revenue from Live does not equal incremental operating profit**, however we believe that this is unlikely to show up in the near term

- The average accountant takes 1.5 hours to do a tax return. Hence the \$273.
- **Intuit is arbitraging the average time needed per Live customer, who is charged a fixed price, and the cost per hour for their pro network.** (Uber for tax?)
- Given that the first 33m customers they are going after are relatively simple, this should not be a problem.
- Problems arise, like obamacare, if the most difficult customers are too high a proportion. Costs would spiral and margins suffer.

## Mix and Pricing

ARPU is \$64 in FY2018

- **Management mentioned that all 3 levers, mix, pricing, attach rate hit with equal importance in FY 2018.**
- Pricing is always hard to measure as TurboTax and H&R Block will begin ratcheting up their prices as you get closer to the tax deadline.

	FY 2016	FY 2017	FY 2018	FY2019	FY2020
Units Sold - TTax Live (k)	0	0	669	2,168.80	3,668.80
Revenues					
Consumer Tax - Live			100	355	610
Consumer Tax Rev (ex Live)			2,405	2,549	2,702
<b>Total Consumer Tax Rev</b>	<b>1,973</b>	<b>2,201</b>	<b>2,505</b>	<b>2,904</b>	<b>3,312</b>
<b>Growth</b>			<b>13.8%</b>	<b>15.9%</b>	<b>14.0%</b>

Given that we estimate INTU sold 670m units in FY 2018, when they apply more marketing - can they sell an incremental 1.5m units in 2019?

## 670k Live customers already?

**We estimate TurboTax Live revenue contribution in FY18 was \$100m.**

As in the table above, the basis of our calculation is :-

- Total increase in TurboTax revenue \$304m in FY18
- TurboTax Live contribution to the ARPU increase as well as the volume is ~33%.

Assuming 70% of mix shift is Live and \$150/user, additional revenue from Live = \$100m in FY18.

- Sanity check: Assume a normal growth of 8.5% = \$187m.
- We believe there is no new catalyst in FY18 and hence incremental revenue to \$304m is Live, which ties in with our assumption of ~\$100m.

This indicates **TurboTax Live was ~670,000 filings in FY 2018**, which gives us confidence that with a significant Ad campaign and clear market to go for, it could be an additional 1.5m in FY2019 and FY2020.

**Giving us confidence that there is a step change in TurboTax growth from a historical 5-10% to more like 12%-14% for at least the next few years.**

## What Margins for TurboTax Live?

We estimate gross margins on Live of ~50%, however cash contribution per filing is potentially very high.

Lets say 1m new Live customers per year is a sensible number.

- 1m customers at \$170, **spending an average of 30mins with a pro.**
  - **This is a key variable. if it is only 5 mins, then TTax doubles its incremental profit per customer. At 55mins there is zero incremental profit.**

- **Given that there is no scaling effect in the business - This year's experience in time used should be the same as next year. We should have high confidence in Intuit's ARPU growth impact in 2018 being applicable to the future.**
- Pro costs = \$70. (\$140 per hour)
- Will there be incremental marketing costs & discounting to attract this customer vs a traditional customer? **We guess yes in the near term, no in the long term.**
- Thus, incremental revenues of \$170 less \$70 incremental costs, less fixed costs of \$25 per return= **\$75 incremental operating profit per return.**

## Engagement? No, it is all about certainty

Nobody is engaged on filing taxes, however there is a high cost, both emotionally and potentially monetary, of getting it wrong.

What turboTax has effectively been doing is moving from a workflow product that enables **ease of use** (they lead in this metric) to a **guaranteed peace of mind product, with an easy workflow that maximises deductions.**

- **Ease of use is how they have competed in the past.** Pricing set by the market, better product = volume.
- **Guaranteed peace of mind looks to be how they are competing in the future...** priced on value to the customer.
- **Maximising the rebate and confidence in the rebate cannot be understated as a metric.** From our research, it is this metric that determines how a person files.

From a business model perspective, the big change is that TTax is offering increasing guarantees that their "system" will maximise the tax rebate.

**At a minimum this will improve retention.**

**Attach:** has a similar role to play. Again the focus looks to be peace of mind.

- Up-sell Live through the process- when you need help, here it is.
- Audit defense -protection against being audited by the IRS.
- Refund - ability to pay out of the tax rebate. (costs \$40 extra)

## The FY2019 Q3 Problem



- **FY 2019 will be a noisy tax season, vs a very "simple" FY 2018.**

Given the new tax legislation, it is highly probable that there will be a mix shift towards standard deductions away from itemized deductions.

Therefore, there will be pressure on ARPU as customers can move to lower price products in the DIY category.

Historically, Intuit has been excellent at finding the right point to charge, and there has been controversies in the past such as Free.

- It's much simpler to claim the standard deduction than to itemize, but it could cost you money. The IRS recommends that you take the time to run the numbers to see which option gives you a bigger deduction (TurboTax will do this for you).
- Simplification enables INTU to take share of the assisted category.

The variance in 2019 tax season could be big, and visibility is always limited.

## Some perspective on DIY

- **TurboTax has 80% market share of paid DIY returns.** 81% of paying units are online.
- FQ3 is the only quarter that matters. (reported around 23rd May) Getting any insight into the quarter is challenging.
- Each tax season is different. Rule changes mean that the area of competition / how products trying to differentiate changes each year. **Intuit has a long history of consistent execution**, with consistent operating margins in the 62% to 67% range.
- **Price increase has been a 3.4% CAGR over the last decade.** (excluding FY2018)
- Most tax filers receive a refund: the average refund in 2016 was \$3,000. 73% of filers earning less than \$100k get a refund.

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