Focus Financial Partners
2023 First Quarter Call
May 4, 2023

<u>**Presenters**</u>
Rudy Adolf, Founder, Chief Executive Officer
Jim Shanahan, Chief Financial Officer
Rusty McGranahan , General Counsel
Tina Madon, Head of Investor Relations and Corporate Communications

Operator
Good morning, ladies and gentlemen. I would like to welcome everyone to the Focus Financial Partners 2023 First Quarter Call.

Joining today's call are Rudy Adolf, Founder and CEO, Jim Shanahan, Chief Financial Officer, Rusty McGranahan, General Counsel and Tina Madon, Head of Investor Relations and Corporate Communications.

Mr. McGranahan, please go ahead, sir.

Rusty McGranahan
Good morning, everyone. Before we begin, let me remind you that during the course of this call, we may make a number of forward-looking statements.

We call your attention to the fact that Focus' results may, of course, differ from these statements. These statements are based on assumptions made by and information currently available to Focus Financial Partners and involve risks and uncertainties that could cause the results of Focus to, materially, differ from these statements.

Focus has made filings with the SEC, which lists some of the factors that may cause its results to differ, materially, from these statements. And finally, Focus assumes no duty and does not undertake to update any such forward-looking statements.

In addition, due to our pending merger with Clayton, Dubilier & Rice, we will not be taking questions following Rudy and Jim's prepared remarks and will not be providing earnings guidance for the second quarter of 2023.

With that, I will turn it over to our Founder and CEO, Rudy Adolf. Rudy

Rudy Adolf
Thanks, Rusty, and good morning, everyone. And thank you for joining us today.

This morning, we announced our first quarter results with 557.5 million of revenues, adjusted net income, excluding tax adjustments per share of $.69 and tax adjustments per share of $.20.

Though slightly below our expectations, our financial performance continued to reflect the resiliency of our business, despite the challenging macro backdrop, during the quarter.

Our partners continue to deliver excellent service to their clients and manage their businesses, well, remaining agile during the quarter.

Providing highly personalized, integrated advice is extremely valuable to their clients, especially during periods of volatility.

According to economic partners, industry M&A transaction volumes rebounded in the first quarter from a slower first quarter, last year.

They noted that buyers demand and seller supply is strong and they anticipate activity to increase, as the year progresses.

Year to date, our M&A activity has been strong with 16 closed transactions, including two new partner firms and 14 mergers on behalf of our partners.

Our differentiated ability to source, structure and execute these transactions remains a core element of our value proposition to growth oriented firms. With the largest M&A team in the independent Wealth Management space, we continue to bring industry-leading scale to benefit our partner firms and their clients for acquisitions.

As I have mentioned before, we believe that the flight to comprehensive unconflicted advice will continue to accelerate, due to last year's market correction, leading to substantial growth in client assets managed by the RA industry, as experienced in prior cycles.

Our partners continue to take advantage of our value added programs designed to give them an edge in meeting their clients' growing and highly personalized needs.

By leveraging our scale and dedicated resources, our partners can deliver ever increasing value to their advisors and clients, which are essential catalysts for retention, referrals and organic growth.

But market conditions remain unsettled. Our diverse and growing global partnerships creates a number of scale advantages reinforcing the sustainability of our strong growth, over the long term, and our differentiated value proposition in this industry.

With that, let me turn the call over to Jim. Jim.

Jim Shanahan
Good morning, everyone. Our business remains resilient, supported by a diverse recurring revenue stream, variable management fee structure and the economic alignment we have with our partners.

We are executing well and remain confident that we are well-positioned to capitalize on our industry's substantial forward growth opportunity.

Now, let's turn to our Q1 P&L. Our revenues for the quarter were 557.5 million, up 3.9%, year-over-year but slightly below our guidance of 560 million to 570 million.

This was primarily due to lower than anticipated nonmarket correlated revenues.

Our Q1 results also reflect the 9.1 million in real estate related performance fees, slightly below our 10 million guidance.

Our Q1 adjusted EBITDA was 132.5 million, 1.9% lower, year-over-year, excluding the expenses associated with the merger process.

Our adjusted EBITDA margin was 23.8%, marginally below our estimate of approximately 24%.

The revenue shortfall versus expectations that I just mentioned earlier, contributed to the variance in our margin.

Our Q1 adjusted net income, excluding tax adjustments per share, was $.69, declining 29.6%, year-over-year. This reduction reflects the effect of higher interest expense on our borrowings.

Our Q1 tax adjustments per share was $.20, 11.1% higher, year-over-year, reflecting our tax efficient acquisition activity associated with the high M&A transaction volume for the period.

Our Q1 M&A activity reflected our continued strong momentum. We closed 12 transactions in Q1, including one new partner firm and 11 mergers on behalf of our partner firms.

So far in Q2, we have closed three mergers on behalf of our partner firms and one new partner firm.

The partner firm we closed on January 1 added revenues of approximately 1.2 million and adjusted EBITDA of approximately 400,000 to our quarterly results.

Additionally, Westcourt Capital, the new partner firm that we closed on May 1, is expected to add 11.1 million in annual acquired base earnings.

Now, let's turn to our Q1 expenses and cash flow. Management fees were 124.6 million, or 22.3% of our revenues, lower sequentially by 1.9%, reflecting the contractual economic arrangements we have with our partners.

Our non-cash equity compensation expense was 1.4% of our Q1 revenues, in line with our expectations. As of March 31, our LTM cash available for capital allocation was 303.9 million, reflecting the resiliency of our cash flows during a volatile market year.

We paid cash earnout obligations of 26.1 million in Q1. We also paid 12.5 million in deferred acquisition consideration in Q1.

Now, turning to our balance sheet. We ended Q1 with approximately 2.7 billion of debt outstanding and our net leverage ratio was 4.41 times, marginally above our estimate of approximately 4.3 times, due primarily to the modest shortfall in our adjusted EBITDA versus our expectations.

As of March 31, at our unjoined term loan Addie, together with our unjoined revolver, and cash balance give us over 850 million of available firepower, as we anticipate another strong year of M&A activity.

Additionally, in April, we entered into 500 million in forward started interest rate swaps. These swaps fix our one month term SOFR for 500 million of borrowings at approximately 3.17% plus a spread of 325 basis points for the April 2024 to April 2028 period.

In closing, we continue to navigate the ongoing market challenges well and remain highly disciplined in deploying capital. We remain committed to driving substantial growth, enhancing our value add programs and position ourselves to take advantage of the secular growth opportunity, within the global Wealth Management industry.

I'll now turn the call back to Rudy for closing remarks.

Rudy Adolf
Thank you, Jim. In closing, I would like to reiterate the strengths and resiliency of our business model, our differentiated competitive position and the value of prudent fiduciary advice in volatile market environments.

As I have said before, in this and environments like we experienced last year when our firms industry leadership and the value of what they do really shows, positioning them for solid growth and performance, as financial markets recover.

Rajini, Lenny and I could not be prouder of our incredible partnership and the quality of the business, the focused team, together with our partners has built, over the last 18 years.

We look forward to continuing to grow and evolve the company and to capitalizing on the substantial growth opportunities that lie ahead of us.

Now, as Rusty said, given the pending merger with Clayton, Dubilier & Rice, we won't be opening up the lines for Q&A. However, we want to thank everyone for their time and interest in Focus.

Operator
And with that, ladies and gentlemen, that does conclude the call. you may now disconnect your lines and thank again for joining us today.