

Investor briefing

23 May 2014



Beautiful accounting software

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(Company number NZ 1830488, AU ARBN 160661183 NZX/ASX:XRO).

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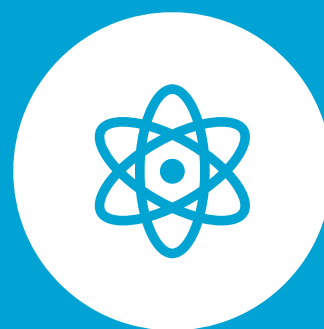
All currency amounts are in NZ dollars unless stated otherwise.



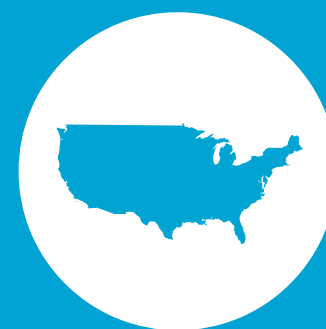
What we're going to cover



**Financial
performance**



**Business
model**



US update



Q&A

FY2014 highlights

Operating revenue

\$70.1m

ACMR at \$93m

Customers

284,000

45% in “Class of 2014”

Staff

758

Staff numbers
doubled in 12 months

Accounting partners

11,573

45% of partners
added in FY2014

Cash to invest

\$210m

Raised \$180m
in Oct 2013

Financial performance

Year ended 31 March

	2014 (\$000s)	2013 (\$000s)	% change
Operating revenue	70,091	38,353	83%
Other income	1,383	936	48%
Total revenue and other income	71,474	39,289	82%
Cost of revenues	24,516	13,916	76%
Gross profit	46,958	25,373	85%
Total operating expenses	85,920	41,657	106%
Operating deficit	(38,962)	(16,284)	139%
Net loss after tax	(35,546)	(14,443)	146%
Cash balance	209,886	78,244	168%

Country growth

	Customers			Operating Revenue (NZ\$000s)			Partners		
	2014	2013	Growth	2014	2013	Growth	2014	2013	Growth
NZ	102,000	73,000	40%	24,104	16,420	47%	2,646	2,150	23%
AU	109,000	51,000	114%	29,297	13,734	113%	5,328	2,694	98%
UK	47,000	22,000	114%	10,429	5,477	90%	1,797	919	96%
Nth America	18,000	6,000	200%	3,589	1,345	167%	1,518	425	257%
Rest of World	8,000	5,000	60%	2,672	1,377	94%	284	120	137%
Total	284,000	157,000	81%	70,091	38,353	83%	11,573	6,308	83%

Market share

	Small business			Partners		
	Current customers	Small businesses*	Current market share	Current partners	Accounting & Bookkeeping firms*	Current market share
NZ	102,000	0.45m	23%	2,646	3.5k	76%
AU	109,000	2.0m	5%	5,328	29k	18%
UK	47,000	4.3m	<1%	1,797	34k	5%
Nth America	18,000	29.0m	<1%	1,408	500k	<1%
Rest of World	8,000	-	<1%	394	-	<1%
Total	284,000	-	<1%	11,573	-	<1%

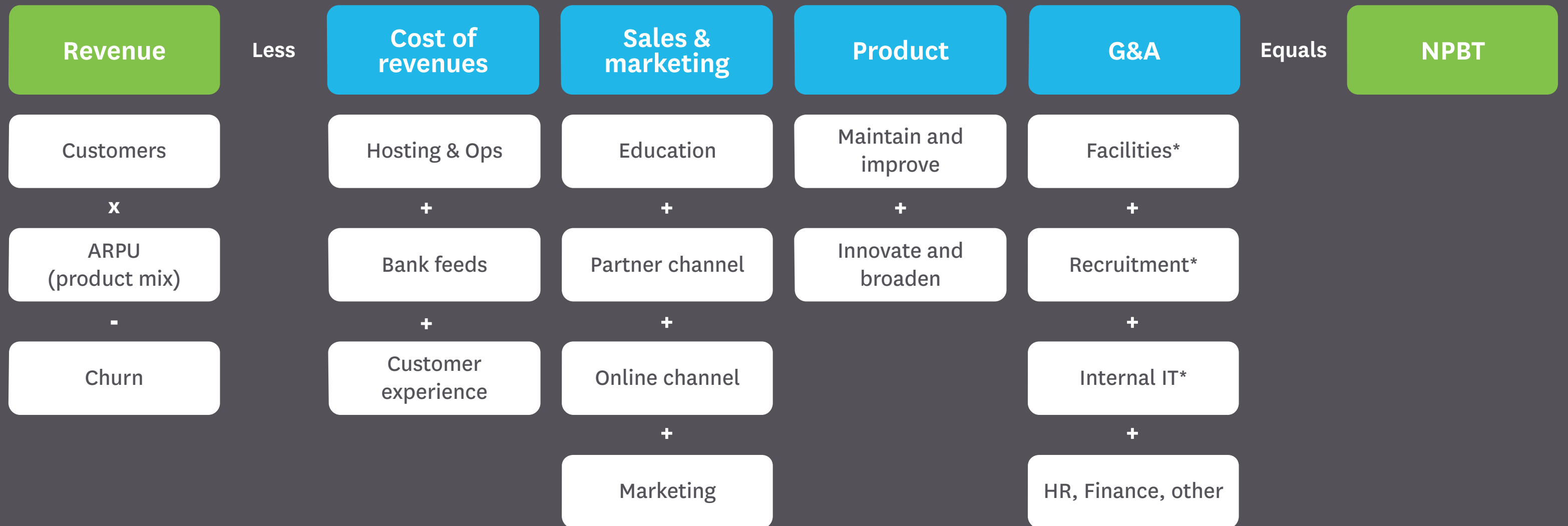
*Estimated from various market sources.

Expenditure

Year ended 31 March

	<u>2014</u>	<u>2013</u>	<u>% Change</u>
Cost of revenues	24,516	13,916	76%
<i>% operating revenue</i>	35%	36%	(1%)
Sales and marketing	55,105	22,043	150%
<i>% operating revenue</i>	79%	57%	22%
Product design & dev	34,089	18,898	80%
<i>% operating revenue</i>	49%	49%	0%
General and admin	12,406	7,996	55%
<i>% operating revenue</i>	18%	21%	(3%)

Our business



*Allocated to cost of revenues, sales and marketing, and product or retained in G&A based on headcount for Facilities and Internal IT, and based on number of new employees hired for Recruitment



Revenue

- Customer acquisition: Build initial relationship with Xero and the partner ecosystem
- Drive ARPU: Grow average revenue per user by product mix
- New ARPU: Add new business services across a large scale customer base.

“Well, if you believe, as we do, that technology markets tend to be winner-take-all, the leaders in any given category will get an unfair share of the overall economic pie.

True, not every SaaS company deserves the benefit of this doubt. But for category-leading companies going after huge markets with business models that demonstrably scale, we shouldn't let the headlines get in the way of a great story.”

“Understanding SaaS: Why the Pundits Have It Wrong” May 2014

ANDREESSEN HOROWITZ

Churn trends down

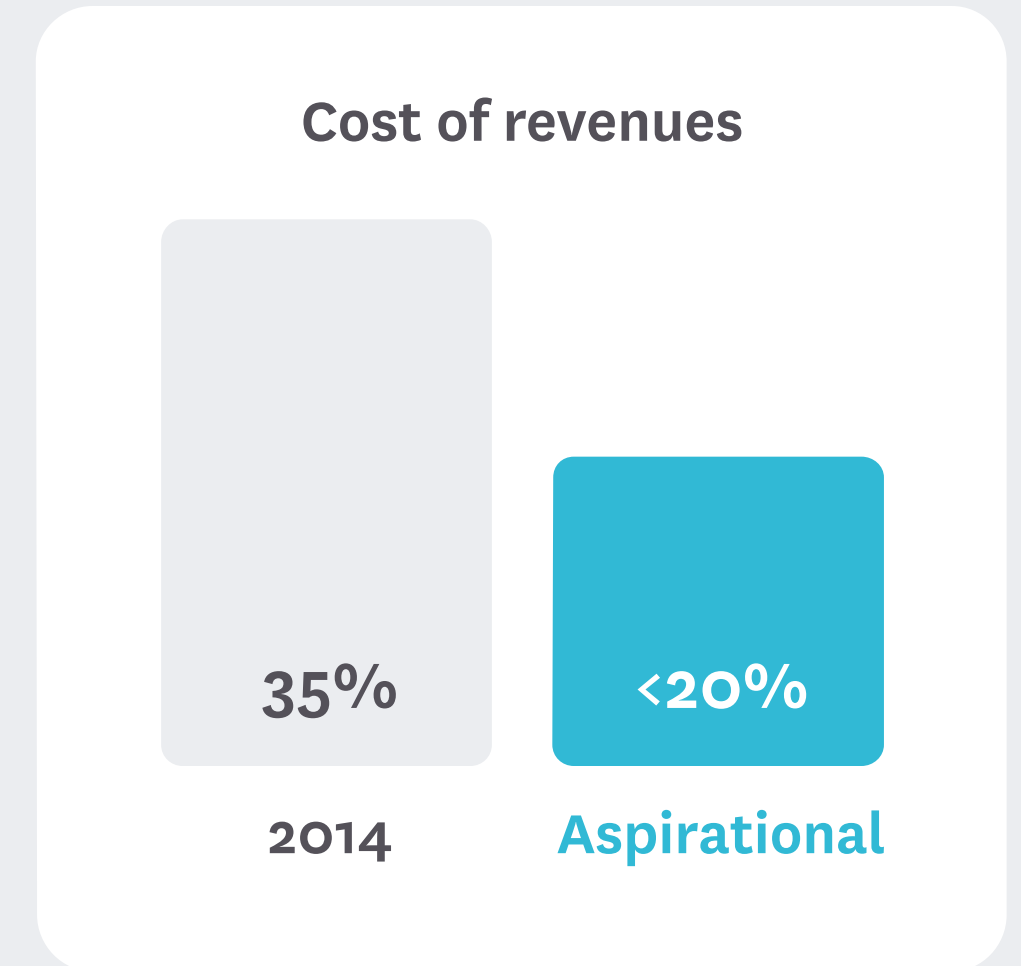


Cost of revenues

(SaaS term: Cost To Serve or CTS)

Drivers based on product volume:

- Hosting – PaaS/IaaS trends provide future opportunities for substantially improved economics
- Bank feeds – range from nil to \$3.00 per customer/month, the view is costs will trend towards nil over time
- Customer experience can be reimaged in SaaS:
 - Targeted education and online content
 - Automated self service driven by real-time insights



Sales and marketing

(SaaS term: Cost to Acquire Customers or CAC)

- High growth in a SaaS business requires substantial upfront CAC investment that delivers revenues in future periods
- Current accounting practices do not allow CAC costs and revenues to be aligned i.e. if average life of a customer is 5 years then 80% of CAC cost relates to generating future revenues
- Two SaaS measures used in assessing sales and marketing model efficiency are “months of ARPU to recover CAC” and “Lifetime value (LTV) to CAC” – see following page
- Along with multiple channels, Xero has the advantage of operating in four major markets all at different phases of growth and CAC investment.

CAC metrics

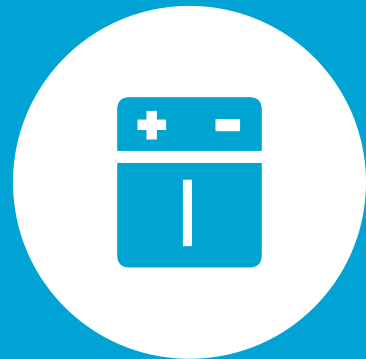
	Market phase Recruit, Educate, Grow	2014 Months of ARPU to recover CAC	2014 LTV	2014 LTV:CAC	2015 Projected trend
NZ	Educate, grow	5.7	\$1300	9.5X	steady
AU	Recruit, educate	9.5	\$1300	4.3X	steady/improvement
UK	Recruit, educate	9.8	\$1100	4.5X	steady/improvement

“Months of ARPU to recover CAC” represents the number of months of revenue required to recover the cost of acquiring each new customer, i.e. sales and marketing costs divided by new customers divided by monthly ARPU

“LTV:CAC” is the ratio of the gross margin derived over the life of a customer to the cost to acquire that customer, e.g. for New Zealand the gross margin derived from a customer is currently on average 9.5x the cost of acquiring that customer. The calculation of the components are: LTV = average customer lifetime multiplied by ARPU multiplied by gross margin; CAC = sales and marketing costs divided by new customers



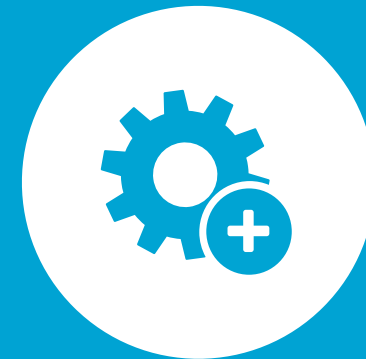
Sales & marketing



Partner channel



Online channel



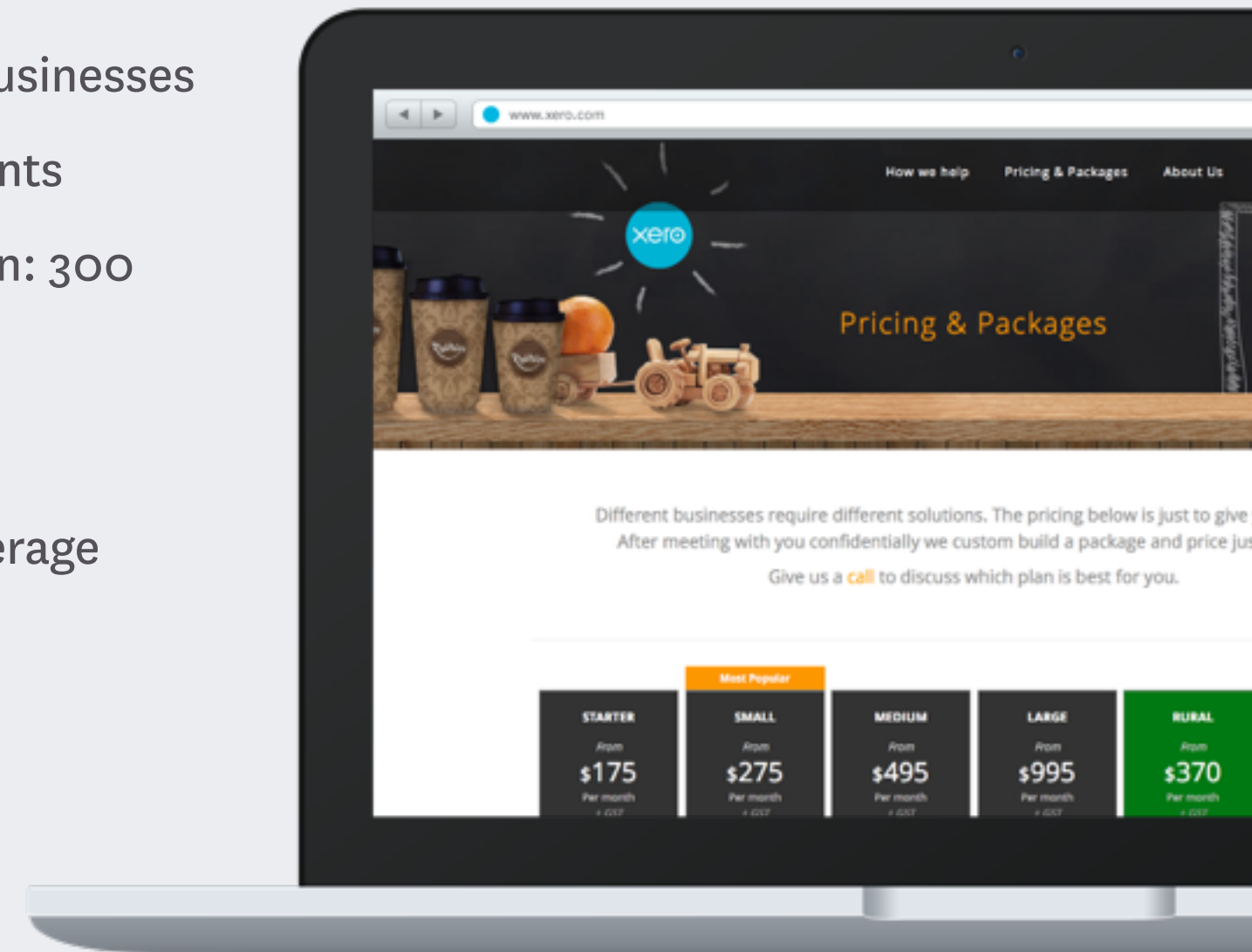
Ecosystem

Partner channel

Unique to accounting software

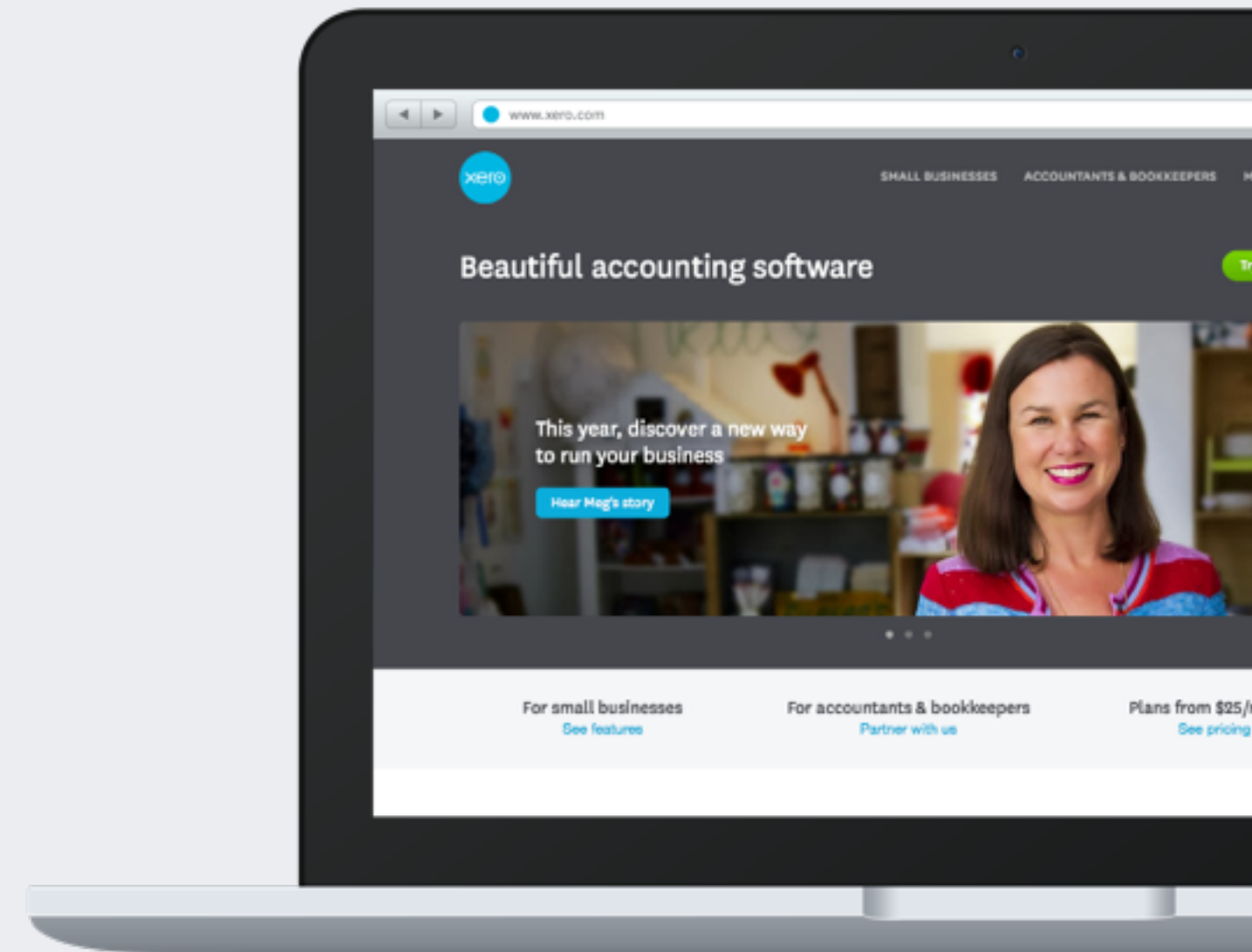
- Accountants and bookkeepers are a proven channel to small businesses
- Education led sales approach via XeroU, XeroTV and online events
- The partner channel is a leveraged model (e.g. one sales person: 300 Partners: 100 customers per partner). High CAC as we recruit and educate the partner and add the first few customers
- Once a partner is on the Xero journey, CAC for new customers trends down substantially. Demonstrated by higher ratio of average customers per partner in maturing markets:

Average customers per partner	NZ	AU	UK	Nth America	ROW
	31	15	18	6	10



Online channel

- Increasing investment in online
- Substantially lower CAC than partner channel
- Improved sign up experience will lift conversion of unique visitors to new customers
- Focus on vertical solutions using add-on partners
- Non-traditional marketing investments:
 - PR
 - Reviews
 - Online SEO/SEM



Ecosystem channel

- Network of companies stronger than a single brand
- We believe an open approach wins
- Seek large partners upstream
- Be the easiest partner for innovators
- Leverage energy and investment of many partners.

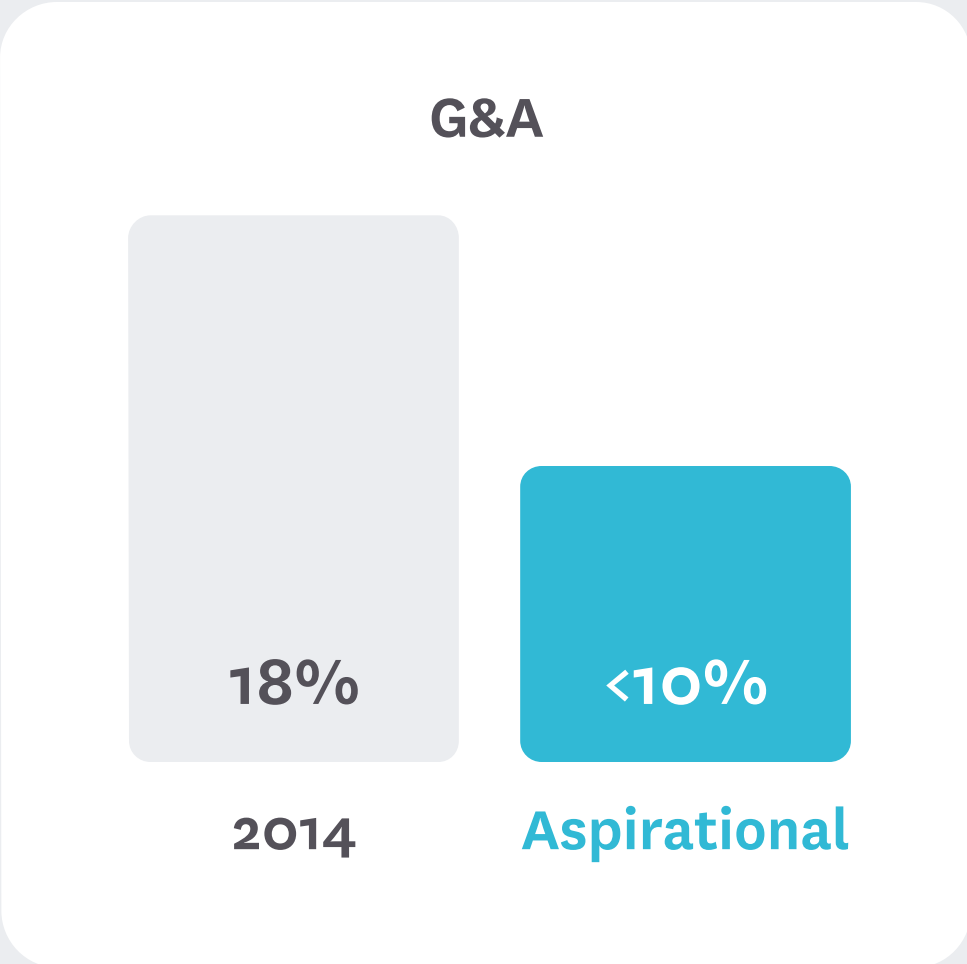


Product design and development

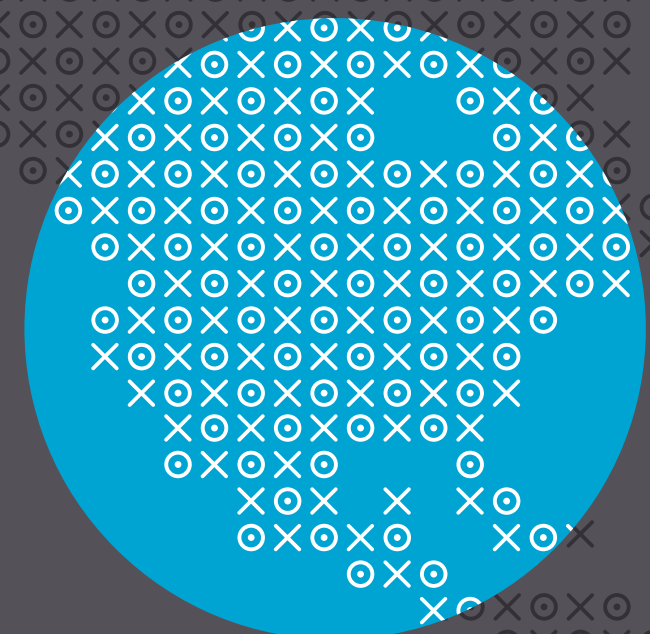
- Leverage clean architecture to deliver on a faster cadence and broader product set than incumbents
- FY14 substantially increased capacity of team to 236 (119 added in FY2014)
- Xero built by Xero's - we believe in the craft of software development
- Moved from centralised development team to decentralised global model
 - Added substantial development management capability
 - Structure is now many small delivery teams, distributed across regions
 - Ability to easily scale teams to focus on new initiatives
 - Approach is open, integrated platform on which to deliver the best end-to-end customer experience

General and administration

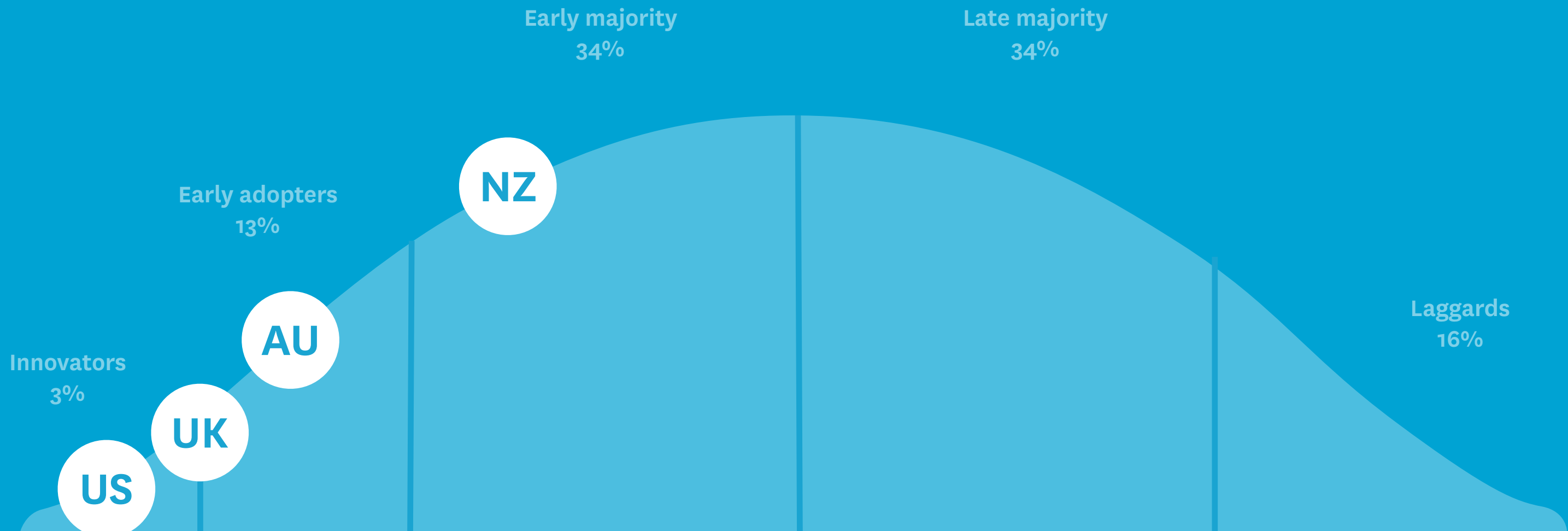
- Investing in scalable cloud based systems
- G&A will reduce as a percentage of operating revenue with scale



Focus on the USA



Adoption curve



Win influencers

Recruitment and go broad

Go deep and win share B2B and B2G initiatives

Drive ARPU and network effects



US market entry phase

Product

Foundations in place
Payroll first-release
Product reviews match QBO
Superior customer service ratings

People

US Directors
Nth American CEO
VP Education
Denver Support team

Partnerships & Integrations

Square
H&R Block
Expensify
SquareSpace
ADP
Clio

GTM

Influencers
PR
Education
Accounting channel



"Xero is superior to QuickBooks Online in some ways. It supports multiple currencies, which QuickBooks Online has not yet made available for the U.S. market. Xero also has a built-in safeguard that QuickBooks Online does not: transaction approvals. Finally Xero offers multiple payment gateways and has exceptional online help and support. "

20 May 2014 – pcmag.com

US plans 2015

Product

**Deliver best in class
US product**

Innovate faster

**Change product
category**

QB Conversions

People

**Complete
US leadership team
for scale**

**Global Management
focussed on US**

New US Directors

Partnerships & Integrations

Best ecosystem

**Execute on existing
relationships**

**Large distribution
partners**

GTM

Online Channel

**Focus on key
segments**

Q&A



Beautiful accounting software