KP+GH

KELLY PARTNERS GROUP HOLDINGS LIMITED

# KPG 2023 Shareholders' Letter

The 2023 financial year has been one of great progress for KPG.

## Built to Last

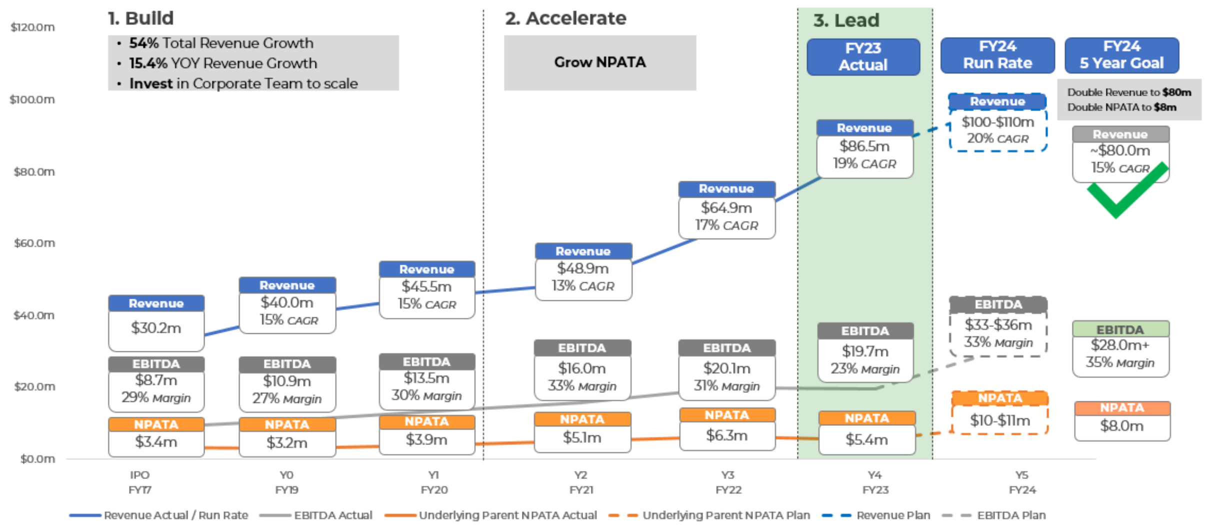
It is important to understand the framework from which we operate the business, that is, not to build a business to flip but rather to build a business to last more than 100 years. We are on a long march to modernize the accounting industry providing the best of opportunity for:

- Owners who care about their people and clients;
- Professionals in our industry;
- Clients that are private business owners;
- Communities that want to see world class services and growing employment in their region.

This is a different market position and one that we communicate regularly to our team members, clients and the communities within which we operate.

## 5 Year Plan Progress

In 2019 we published a 5 year plan as we found that many investors couldn't understand or visualize how KPG could make progress over time. It had always been our plan not to provide guidance - Warren Buffett has often said "I do not like guidance. I think the guidance leads to a lot of bad things, and I've seen it lead to a lot of bad things". That said it has been useful to be transparent in this way to make clear to our Quality Shareholders how we saw the business could and would likely develop.





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Certified B Corporation

**Progress of 5 Year Plan in 2023**

Our efforts against our stated 5 year plan have proceeded more rapidly than expected with growing revenues. However, by doubling our traditional growth rate and increasing the number of transactions we haven't achieved the EBITDA margins to the levels that we expect of ourselves.

This has led us to state clearly here for you as an investor, partner and share owner of KPG that at an operating level we must focus on managing:

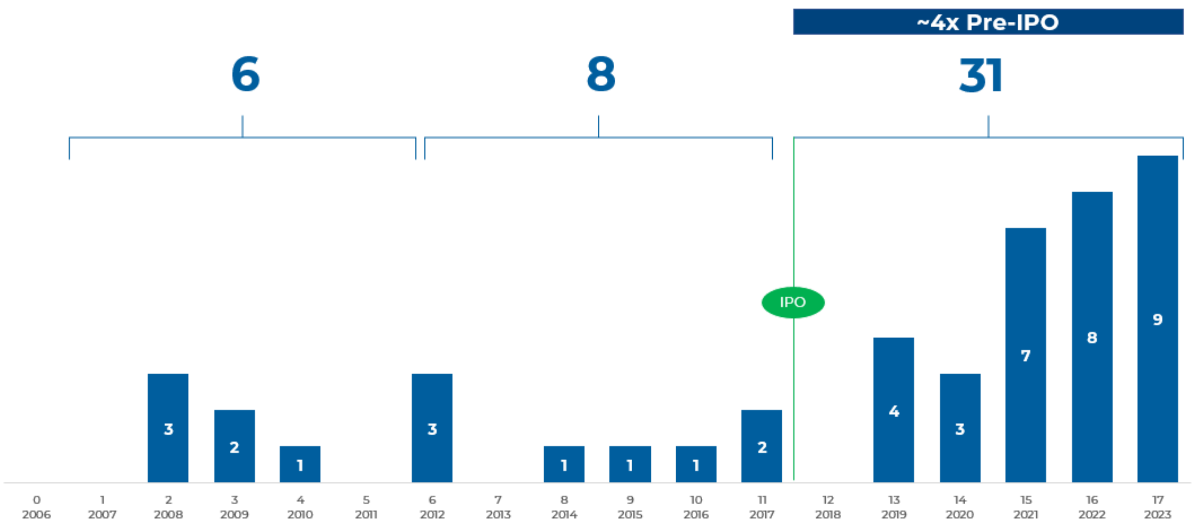
1. Revenue growth;
2. EBITDA margin;
3. Working capital lockup.

At the Head Co Level, we must focus on managing:

1. Additional investment above the service fee & IP license fee we receive from our operating businesses;
2. Net Debt to EBITDA;
3. Cashflow conversion;
4. ROE & ROIC.

As we look to the new financial year we will aim to manage these metrics to provide the best possible returns to our shareholders.

*Number of acquisitions completed since inception*



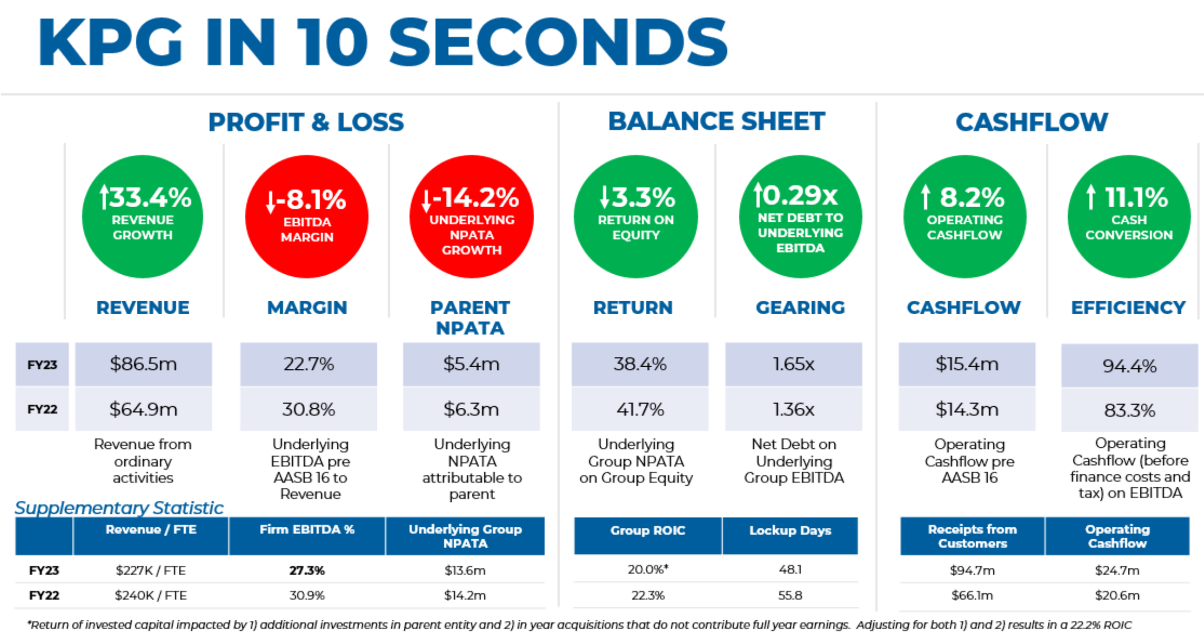

*Note: based on acquisitions that are announced in the stated financial year, e.g. acquisition that was announced in FY22 but completed in FY23 is shown in FY22.*

**Additional Investment above services fee & IP license fee**

The history of our additional investment above the 9% central costs paid to KPG is outlined in the following table:

| | FY18 | FY19 | FY20 | FY21 | FY22 | FY23 |
|---|---|---|---|---|---|---|
| Group revenue | $39,468,666 | $39,975,031 | $45,495,584 | $48,906,446 | $64,862,110 | $86,524,364 |
| Revenue growth | - | +1.3% | +13.8% | +7.5% | +32.6% | +33.4% |
| Additional investment | $371,913 | $742,439 | $1,630,905 | $371,127 | $77,836 | $2,479,110 |
| % of Revenue | 0.9% | 1.9% | 3.6% | 0.8% | 0.1% | 2.9% |

This table makes clear that KPG has a history of investing portions of its earnings while dramatically growing the earning power of the Group. From time to time, it has been said to me that we should increase the 9% or invest less in our businesses (e.g. to generate a profit via under investing in our businesses). It is difficult to argue that shareholders will not now be better off with us having made these additional investments.




To whatever degree any shareholder is unhappy with this capital allocation decision making I am personally pleased to take responsibility.

**Capital Allocation and Kelly+Partners**

| | KPG aims to build per-share intrinsic value by: | | FY18 | FY19 | FY20 | FY21 | FY22 | FY23 |
|---|---|---|---|---|---|---|---|---|
| 1 | Improving the earning power of our operating businesses | ✓ | 34.0% | 27.7% | 32.5% | 33.4% | 30.9% | 27.3%* |
| | | | *EBITDA margin of operating businesses* | | | | | |
| 2 | Further increasing their earnings through acquisitions | ✓ | 17.2% | 6.4% | 6.6% | 4.8% | 26.5% | 28.7% |
| | | | *Contribution to revenue growth* | | | | | |
| 3a | Growing our existing accounting subsidiaries | ✓ | 10.3% | (6.4%) | 6.6% | 1.5% | 4.7% | 2.9% |
| | | | *Contribution to revenue growth* | | | | | |
| 3b | Growing our existing complementary businesses | ✓ | 2.7% | 1.8% | 1.4% | 1.2% | 1.5% | 1.8% |
| | | | *Contribution to revenue growth* | | | | | |
| 4a | Making programmatic acquisitions | ✓ | 0 | 4 | 3 | 7 | 8 | 8 |
| | | | *Number of acquisitions* | | | | | |
| 4b | Making an occasional large acquisition (i.e. >$5m in revenue) | ✓ | 0 | 0 | 0 | 0 | 0 | 1** |
| 5 | Repurchasing KPG shares | ✓ | 0 | 2k | 95k | 400k | 0 | 0 |
| | Number of Shares On Issue | ✓ | 45.5m | 45.5m | 45.4m | 45.0m | 45.0m | 45.0m |

It has been made clear repeatedly to me in numerous conversations that it makes no long-term sense to share owners or KPG to continue to pay dividends given the return on invested capital we have been able to achieve. Nonetheless we are proud we have grown dividends at 10% per year for now six years in a row and we've been paying those dividends for much of that time on a monthly basis. I took this approach to demonstrate clearly to share owners the cash generative abilities of KPG that I hope are now clear to all share owners.

**Strategy Update**

Our objective is to be a leading accounting firm in Australia (broadly defined as having a leadership position in that market) while simultaneously pursuing turning Kelly+Partners into Australia's only global accounting firm for private business owners. Specifically, the scope of activity we are seeking to achieve in the global markets is to have a meaningful presence in Los Angeles in the United States and London in the United Kingdom. We believe that we have at least four very differentiated advantages that will lead us to achieving our strategy over time, as follows:

1. Mission, values and vision
2. Partner-owner-driver® model
3. Central services team
4. Intellectual property and know how

Hopefully it is clear that this strategy realizes a blue ocean opportunity and has been tightly defined. We are very aware that many people attempt to globalize their business so we are keen to prove out the strategy via first firing bullets then cannonballs. What this means practically is that we will seek to acquire firms in Los Angeles that are not materially large and that would not and cannot represent any material risk to the Group. We will learn that market and grow in a sensible fashion as we have done in Sydney, and we intend to adopt the same approach to growing our presence in London.

**Ideal Business and Capital Structure**

In order to maximize the opportunity available to KPG on a global basis we must pursue the right business and capital structure that will allow us to achieve our 100-year goal. Hence, we are actively pursue a broader, more comprehensive strategic review of our current ownership and capital structure. To help facilitate this strategic review we have appointed legal, tax and financial advisors to consider options that will maximise value for all shareholders and to close the gap between what we believe is the intrinsic value of the Company and today's market capitalization.

The strategic review is in a preliminary phase and will assist our Board to consider various alternatives to drive shareholder value. The alternatives include options that range from, for example, the optimal listing venue for KPG (e.g. redomiciling to a US listing venue) or a potential privatization of KPG, amongst others.

As we undertake this strategic review, we remain focused on executing our plan, committed to our clients and team, and maximizing the opportunity to ensure the best outcome is delivered for all stakeholders over the long term.

We'll continue to keep our shareholders up to date on this process.

**Earnings Outlook**

| | | W/O Additional Investment | With Additional Investment | | | FY23 |
|---|---|---|---|---|---|---|
| **Additional investment as % of Revenue** | | **0.0%** | **-1.0%** | **-2.0%** | **-3.0%** | **-2.9%** |
| Revenue | | $1.00 | $1.00 | $1.00 | $1.00 | $1.00 |
| EBITDA | 33.0% | $0.33 | $0.33 | $0.33 | $0.33 | $0.27 |
| Depreciation | -2.5% | -$0.03 | -$0.03 | -$0.03 | -$0.03 | -$0.03 |
| Interest | -1.5% | -$0.02 | -$0.02 | -$0.02 | -$0.02 | -$0.02 |
| Group NPBT | 29.0% | $0.29 | $0.29 | $0.29 | $0.29 | $0.23 |
| KPGH Share | 51.0% | $0.15 | $0.15 | $0.15 | $0.15 | $0.12 |
| Additional Investment | | $0.00 | -$0.01 | -$0.02 | -$0.03 | -$0.03 |
| KPGH NPBT | | $0.15 | $0.14 | $0.13 | $0.12 | $0.09 |
| Tax | -30.0% | -$0.04 | -$0.04 | -$0.04 | -$0.04 | -$0.03 |
| **KPGH NPATA** | | **$0.10** | **$0.10** | **$0.09** | **$0.08** | **$0.06** |
| **% of Revenue** | | **10.4%** | **9.7%** | **9.0%** | **8.3%** | **6.2%** |

| 'm | FY18 | FY19 | FY20 | FY21 | FY22 | FY23 |
|---|---|---|---|---|---|---|
| | Actuals | | | | | |
| Revenue | $39.5 | $40.0 | $45.5 | $48.9 | $64.9 | $86.5 |
| NPATA | $4.8 | $2.8 | $4.4 | $5.2 | $5.6 | $15.0 |
| **Underlying NPATA** | **$4.3** | **$3.2** | **$3.9** | **$5.1** | **$6.3** | **$5.4** |
| **% of Revenue** | **11.0%** | **8.0%** | **8.7%** | **10.5%** | **9.7%** | **6.2%** |
| Add back: Additional investments | $0.4 | $0.7 | $1.6 | $0.4 | $0.1 | $2.5 |
| Less: Tax effect | -$0.1 | -$0.2 | -$0.5 | -$0.1 | $0.0 | -$0.7 |
| **Underlying NPATA pre additional investments** | **$4.6** | **$3.7** | **$5.1** | **$5.4** | **$6.4** | **$7.1** |
| **% of Revenue** | **11.6%** | **9.3%** | **11.2%** | **11.0%** | **9.8%** | **8.3%** |

In our quality shareholders note dated 13th June 2023 we outlined clearly that we expect in a five year period our earnings (defined as Underlying Net Profit After Tax before Amortisation i.e. NPATA) to average 10% on revenue as we see that as the earning power for our business on an ordinary basis, that is when we are not striving to achieve enormous growth or pursuing other substantial strategic opportunities. As per our quality shareholders note, our earnings % of group revenue is impacted by 1) the profitability margins of our operating businesses and 2) if we choose to invest in addition to the services and IP license fees that we receive from our operating businesses, both of which we will continue to manage in the future.

**Valuation**

When valuing any business, I have always sought to use the Two Stage Dividend Discount Model outlined in Robert Hagstrom's book "The Warren Buffett Way" published in 1997. Hence the two assumptions that a shareholder needs to consider are 1) can we continue to grow the business over the next 10 years and 2) what is an appropriate discount rate (we have always used average cost of capital or the 30 year U.S. Treasury rate). We operate in our circle of competence in investing in accounting firms so we see minimal risk in KPG and we hope that you do too.

**Shareholders are Global**

We are pleased that we have attracted some of the world's best shareholders in USA, United Kingdom, Finland, Switzerland and Germany etc. Not only have these people become share owners and partners, but they are also contributing to our thinking and adding to the capability of the business to achieve our strategic objectives over time. To the shareholders I want to say thank you for your encouragement and partnership.

**Key person dependency**

Kelly+Partners has been intentionally structured to allow our underlying operating businesses to run independently of me and our partners are incentivized to grow their businesses in their respective regions. My relocation to the US nearly 8 months ago is proof that our businesses are decentralized and can operate effectively with minimal interference from me.

**BK Shareholding**

As outlined in our Owner's Manual on 25 November 2020, I intend to continue to remain the largest shareholder of KPG for the very long term.

**Who you spend your time with matters the most**

Of the last 12 months I have been reminded many times that you become the people you spend the most time with. What I like most about the privilege of leading Kelly+Partners is the quality of our people that include our internal team members, our clients, the communities within which we operate and our shareholders. How these people both challenge us and support us is a reason why we continue to do what we do today.

**Book of the Year**

I am often asked my favorite book for 2023. That book is "***Going Public: How Silicon Valley Rebels Loosened Wall Street's Grip on the IPO and Sparked a Revolution"*** **by Dakin Campbell.** It is a wonderful book and gives you an insight into the work that we have been doing to think about the future of Kelly+Partners.

Yours sincerely,

Brett Kelly