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Full Year 2020 Sage Group PLC Earnings Call

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PRESENTATION

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Hello, everyone, and welcome to Sage's FY '20 results presentation webcast. I'm Steve Hare. I'm the Chief Executive of Sage. And also presenting to you today is Jonathan Howell, our CFO.

I want to thank you very much for joining us. And in particular, in these continued uncertain times, I sincerely hope that you, your colleagues and your families are safe and well.

Now before we get going, as normal, I just draw your attention to the safe harbor statement on Slide 2.

Now moving now to the agenda for the day. I'm going to share some opening remarks about the year that we've just had. Jonathan is then going to take you through the numbers. And then I'll return to talk about the strategic progress that we've made since I became CEO 2 years ago, and why it is that we're confident about our plans for the future?

Now FY '20 has been a very different year. Life has changed for all of us. So I wanted to start by reminding you of what is the constant for Sage? It's our purpose to transform the way people think and work, so their organizations can thrive. This is our why. It's the reason we do what we do, along with our overarching value to do the right thing. This has guided our response to COVID-19.

From the beginning, we've put colleague safety and welfare as our top priority. We've provided constant support to our customers and our partners. And our decisive approach has brought results. Over 90% of our colleagues say they approve of how we've handled COVID, and they've showed their pride in Sage through Glassdoor, where our rating is now 4.4 out of 5 compared to 2.9 2 years ago.

And customers have stayed with us. With customer churn, which was slightly elevated in some geographies in the third quarter, now back to normal across the group. Now of course, COVID continues to have an impact on people's lives, their communities and their organizations. But we're not waiting for things to get back to normal. We're focusing on what we can control, being there for our customers, helping them to adapt and survive, and making sure that Sage is well placed to seize the opportunities that this period will ultimately present.

So before I hand over to Jonathan, I'm going to cover 3 messages. We delivered a strong business performance in FY '20. We've continued to execute our strategy at pace, and we approach the future with confidence.

So starting with business performance. We started the year with real momentum following a very good year last year. And we've continued to build recurring revenue quarter-on-quarter, despite the impact of COVID in the second half of the year. Now this has meant that we achieved the recurring revenue growth that we guided to at the beginning of the year.

We've also achieved operating profit in line with expectations, and our cash flow generation was strong. But just as important as this, is how we've achieved it? We've achieved it by living our values and by doing the right thing. We've supported our people and our customers. We haven't made any redundancies as a result of COVID. We haven't accessed any government support. And we've continued to pay our dividends. All of these decisions we made at the very start of the pandemic.

We've also continued to execute on our strategy. We've driven further growth on Sage Business Cloud, with revenues up 32%, and over 90% of our revenue is now recurring. We continue to simplify the business. We sold Sage Pay and Sage Brazil in the first half. And this morning, we announced a further 4 businesses held for sale at the year-end.

We also made further progress across the 3 strategic lenses: we've improved customer experience through new ways of working and improved technology; we've supported colleagues through training, development and engagement activities; and we've delivered innovations on schedule, in line with our road map throughout the year.

So looking to the future, despite the near-term uncertainties, we're confident. Our business is based on high-quality recurring revenue, a diverse base of small and medium business customers and is backed by a resilient balance sheet. We have a strong market position and engaged colleagues. And in terms of product, we've developed a compelling portfolio of differentiated solutions, which is driving our performance, attracting new and existing customers to Sage Business Cloud.

So while COVID is slowing our trajectory in the near term, we are well positioned for growth. As small and medium businesses adapt to the ongoing pandemic, they want to embrace and invest in a digital future. They are adopting digital tools at a faster rate as they look to serve their own customers in a different way. Think about how restaurants and pubs are enabling advanced food ordering and takeaways, others adapting to a mixture of remote and office working. This helps them build resilience and productivity for the long term and in many of our markets, creates the conditions for an SME-led recovery.

Our solutions are designed to equip customers to thrive in this era of digital transformation. So I believe it's vital that we continue to invest through this economic cycle, sustain our pace of innovation and use the momentum to accelerate our growth.

Now later in the presentation, I'm going to set out our plans to increase the pace of progress across Sage. But for now, I'm going to hand over to Jonathan to take you through the numbers.

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Thank you, Steve, and welcome to you all. I hope you are all safe and well. Before I go through the financials, I wanted to touch upon the strategic progress Sage has made over the last 2 years. This has translated to significant improvements in our key metrics. Subscription penetration, which has increased from 45% in FY '18 to 65% in FY '20. And Sage Business Cloud penetration, which is 61% is up from 31% in FY '18. These metrics demonstrate the progress we have made in our transition to a SaaS company. And importantly, this has driven strong financial performance, which is in line with expectations.

So turning to our financial highlights for FY '20, which demonstrate its consistency in performance and execution. The key messages are: firstly, high-quality recurring revenue growth. We've delivered recurring revenue growth of 8.5%, which reflects good strategic and operational execution. Secondly, on target margin. The organic operating margin of 22.1% is in line with our targets. This reflects good business performance and ongoing investment to drive future growth. Thirdly, strong cash conversion. Cash conversion has continued to be particularly strong at 123%. This is the second year in excess of 100% and remains a core strength of Sage. And finally, a resilient balance sheet with GBP 1.2 billion of cash and available liquidity. And with this, Sage enters FY '21 in a strong financial position.

Turning now to the P&L. And first, to be clear, the numbers in this presentation are on an organic basis. This strips out the impact of disposals and assets held for sale at the end of the year. Total revenue has increased by 3.7% to GBP 1.8 billion, and recurring revenue is up by 8.5% to GBP 1.6 billion.

Organic operating profit is GBP 391 million and a margin of 22.1%. This reflects continued investment to drive strategic execution. This also includes a GBP 17 million charge to provide for potential bad debts in connection with COVID-19.

Underlying operating profit is GBP 411 million. And underlying EPS is 27.43p, which is slightly lower than last year. We've increased the full year dividend by 2% to 17.25p. This reflects the strong performance and cash generation during the year and is in line with our policy to maintain the dividend in real terms.

Finally, ARR has increased by 4.8% to GBP 1.6 billion. This reflects continued recurring revenue growth despite the impact of COVID-19 during the second half.

Looking at the phasing of growth across the year. You can see in this table the impact of COVID-19 in the second half, when year-on-year revenue growth slowed to 7% and ARR growth to 5%. Even with this, we continue to generate good levels of profit, demonstrating the resilience of our business model. This profile is important when considering the phasing of growth next year, with ARR growth the leading indicator. We, therefore, expect growth in FY '21 to be weighted towards the second half.

So now looking at revenue categories. As you can see, performance has been strong, demonstrating the progress in our strategic execution. We delivered recurring revenue growth of 8.5% to GBP 1.6 billion. This is underpinned by strong growth in software subscription of 21% to GBP 1.1 billion, which is an increase of nearly GBP 200 million. North America and Northern Europe continue to be the standout performers with recurring growth of 11% and 9%, respectively. This was driven by good momentum from FY '19 and continued execution in Sage Business Cloud.

Other recurring revenue, which is largely maintenance and support, decreased by 13% to GBP 451 million. This demonstrates the ongoing migration of customers to subscription contracts. And other revenue decreased by 26% to GBP 176 million. This reflects the managed decline in licenses and low-margin professional services. As expected, this decline accelerated in the second half due to the impacts of COVID-19.

It's remarkable to see that 90% of our revenue is now recurring. And as I said earlier, 65% of our revenue is from subscription, up from 56% in FY '19. Renewal by value reduced to 99%, reflecting lower levels of up-sell during the second half. This indicates that ARR growth of some 5% continue to be supported by good levels of new customer acquisition and reactivation.

Now turning to the portfolio view of revenue. The overall future Sage Business Cloud opportunity continues to show strong performance with recurring growth of 10%. And as I mentioned, Sage Business Cloud penetration is now at 61%. This is up from 51% last year. The key points to note are: growth in Sage Business Cloud has been driven by new customer acquisition, reactivation and migration. Importantly, cloud native solutions have delivered recurring revenue growth of some 29% to GBP 222 million. The growth in cloud connected revenue of 33% to GBP 636 million is principally driven by our major territories of North America and Northern Europe. And recurring revenue in the non-Sage Business Cloud portfolio was broadly flat, in line with our expectations.

Looking now at the regions. North America delivered recurring revenue growth of 11% to GBP 634 million. And Sage Business Cloud penetration is now at some 71%. Cloud native growth is driven by Sage Intacct with continued strong renewal by value, resulting in recurring revenue growth of 26% to GBP 144 million. Our growth in cloud connected is driven by existing customer migration and new customer acquisition in small and medium products.

Northern Europe has continued to perform well. It delivered recurring revenue growth of 9% to GBP 377 million. Sage Business Cloud penetration is now at some 82%, up from 67% last year, reflecting successes in cloud connected solutions. This growth reflects strong performance in FY '19 as well as new accounting and payroll contracts added during FY '20. This is supported by growth in cloud native solutions.

Finally, Sage Intacct, which launched in the U.K. last November, continues to build momentum through new contract wins. Central and Southern Europe grew recurring revenue by 4% to GBP 467 million. Sage Business Cloud penetration now stands at 40% compared to 27% last year.

France, which is the largest country in this region, grew recurring revenue by 4% to GBP 246 million. This was driven by cloud connected, together with accelerating growth in cloud native.

And finally, the international region has delivered recurring revenue growth of 11% to GBP 114 million. With most of Asia Pacific held for sale, Africa and Middle East now represents almost 90% of the region's revenue. And here, growth of 12% in recurring revenue was driven by local products and cloud native.

Turning now to the cash flow and balance sheet. As a result of particular focus over the last 2 years, Sage has a resilient balance sheet and strong liquidity. The group has over GBP 800 million of cash and nearly GBP 400 million of undrawn facilities. This means that cash and available liquidity totals over GBP 1.2 billion. In addition, term debt and facilities have a long maturity profile extending to 2025. Cash conversion of 123% continues to be strong, in excess of 100% for the second consecutive year. This reflects sustained improvements in working capital as we transition to subscription, and also particular success in the collection of receivables during the year. This has led to underlying free cash flow of GBP 382 million. Net debt has reduced to GBP 151 million, and net debt-to-EBITDA is now 0.3x.

Now turning to capital allocation. Sage's disciplined and consistent approach remains unchanged. We will continue to focus on organic investments and will consider bolt-on acquisitions to support execution against our strategy. Our policy is to maintain the dividend in real terms. And in line with this, reflecting the strong operational performance, we've increased the full year dividend by 2%. And if there is surplus capital, we may consider making additional returns to shareholders.

Moving on to leverage. It is still our intention to operate in a broad range of 1 to 2x net debt-to-EBITDA over the medium term. However, we will move outside this range as business needs require. Accordingly, given the current environment, we are comfortable with our net debt-to-EBITDA leverage of 0.3x.

And so to summarize. Firstly, Sage has delivered a strong and consistent performance, resulting in recurring revenue growth of 8.5%. Secondly, we've delivered an organic operating margin of 22.1%, in line with our targets. Thirdly, continued strong cash conversion of 123%. This remains a core strength of Sage. And finally, we have a resilient balance sheet to support investment for long-term growth.

Thank you. I now hand back to Steve.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Thanks, Jonathan. So 2 years ago, I set out our purpose, vision and strategic focus, and talked about how we would be different. I also set out our initial priorities to drive our SaaS transition, with a focus on growing Sage Business Cloud, driving innovation and enhancing the customer and colleague experience. So what I'm going to do now is just spend a few moments recapping on this and looking at our progress.

So let's start with the strategic framework, which guides everything we do. As I said earlier, our purpose is to transform the way people think and work so that their organizations can thrive. This is our why. Our vision is the way we serve that purpose by becoming a great SaaS company. The strategic lenses are the way we focus and prioritize our actions to achieve this vision. And all of this is underpinned by our values. And I really want to emphasize how these are embedded in our business, guiding our behaviors and our actions. It is through this simple, clear framework that we've achieved tangible progress in the SaaS transition over the last 2 years.

So 2 years ago, I said our primary focus would be to grow Sage Business Cloud by executing our migration strategy, but also attracting new customers. This is really important because it's through Sage Business Cloud, but we developed the deep subscription-based relationships that we need to be a great SaaS business.

Now Sage Business Cloud comprises both cloud connected and cloud native revenues. And you can see on the slide the progress we've made within the revenue mix. Cloud connected revenues have almost traveled, driven by strong progress in migrations. Cloud native has also shown good progress, driven largely by new customer acquisition. We also said we would focus the business by simplifying the portfolio. And since FY '18, we've undertaken 20 divestments or end-of-life projects, reducing noncore revenues and increasing our capacity to invest in the core portfolio. And the result of this is a group with much higher quality of revenue. So I'm going to take a moment just to look at the strategic progress and see how we've delivered against the priorities over the last 2 years, starting with customer success.

We said we would deliver best-in-class customer service and create a personalized customer experience. What we did was to reorganize the business from the bottom-up, focusing our activities around the specific needs of our small and medium businesses. We invested in systems to improve the quality of customer service and support. And in response to COVID, we've launched upgrades to help customers access government schemes. We've provided expert online and phone support. And in challenging times, small and medium businesses have turned to us. But we need to go further by focusing more on the end-to-end customer experience, not just resolving pain points, but building lifetime relationships. That's why we've launched our internal campaign to start with the customer, with initiatives including Customer Days, when all colleagues, regardless of role, will spend a day meeting with customers, engaging each and every Sage colleague in customer success.

Now on colleague success, 2 years ago, our engagement scores were low. We said we'd improve this by investing in training, development and technology, but most crucially by focusing on culture. We've overhauled our performance management system, changed the way we engage with our people, provided more training opportunities and embedded new values and behaviors across the group. The result has really been quite remarkable, with an increase in Net Promoter Score from our people of 60 points over 2 years. And as I said at the start, our Glassdoor score has improved to 4.4, helping us to attract new talent as well as retaining our existing colleagues.

Now whilst I'm pleased with what we've achieved, we certainly will not be standing still. We will continue to focus on culture and on enhancing colleague experience. And whilst we've made progress on diversity and inclusion, there is more to do to create greater equality and diversity of hiring and development opportunities.

On innovation, we said we'd spend more on R&D and expand the availability of Sage Business Cloud. Since 2018, we've increased our annual R&D investment by GBP 60 million a year, taking it to around 15% of recurring revenue.

In May, we launched Sage Accounting Plus, our small business solution for professional users, enhancing our cloud native offering for businesses in the U.K. We've also brought Sage Intacct to 3 new markets: the U.K., Australia and South Africa, already generating annualized recurring revenue of nearly GBP 2 million from over 100 new customers. And we've invested in artificial intelligence through Sage AI Labs, creating innovations, such as Sage Intelligent Time and error detection tools, both live in market now.

Looking ahead, our focus will continue to be on Sage Business Cloud. We will enrich our cloud solutions, increasing their availability and expanding the ecosystem. We will also further develop the digital environment, delivering collaboration and workflow tools, integrating with third-party platforms, such as Teams and Slack, and building secure digital invoicing. The results of our investment in innovation is our model portfolio, which highlights our cloud connected and cloud native products today.

Now over the last 2 years, we focused on building this out, particularly in cloud native, ensuring that we have the right solutions to address the needs of our customers. For smaller businesses, we created a truly differentiated and fully integrated cloud proposition based around Sage Accounting, but also spanning payroll, HR and automation.

For medium-sized businesses, our solutions provide deeper insight and richer functionality around Sage Intacct and Sage People, providing the intelligent office for the CFO. We are constantly enhancing this, for example, developing SEOS, our managed cloud solution for partners, and enriching other features and functionality across our portfolio. And with continued focus and investment, this model portfolio provides a strong platform for growth.

Now as you'll know, if you attended our Investor event at the end of September, we're focused not only on the individual products but also on the digital connections and the broader capabilities that they enable. Our vision for Sage Business Cloud is to create a digital environment where it's easy to connect, collaborate and to do business. And this vision is rapidly becoming a reality. We've already created digital connections between our customers and their employees. So for example, over 2.5 million employees in the U.K. are accessing digital pay slips and other information from their payroll via Sage Business Cloud. But probably the best indicator of progress is the number of log-ins of Sage ID, as this is the key to creating digital relationships. And in September alone, we approached nearly 7 million Sage ID log-ins. This is 50% higher than the same period last year. So that's what we've done.

So let's turn to the future. Our plans are grounded in customer needs. So it's worth reflecting on the current business environment both for our customers and for small and medium businesses more widely. Now as I said at the beginning of the presentation, they are facing unprecedented uncertainty. Many of them have had to rapidly reinvent or change the way they do business.

So for example, DPR, a Sage 50 cloud customer, has turned a physical motor racing business into an online motor sport community. And Roobba, a luxury furniture retailer and Sage accounting customer, has brought forward a significant technology investment in order to keep ahead of booming online demand.

Now the pace of digital change around the world is only accelerating, in the U.K., our research shows that only 17% of small businesses were planning digital investment before the crisis. But now, 3 quarters, say, it's the technology they're turning to, to keep their businesses functioning. And around 2/3 have told us, they want to invest more in technology. We believe the recovery will be led by small businesses. So after the last recession, created over 70% of new jobs, resulting in a more digital, more resilience economy. And the progress you've just heard about means that we are well positioned to support these customers as they transform their businesses and adopt digital business models.

So what does all this mean for Sage? Well, first of all, Sage Business Cloud adoption and growth remains our key priority. Just as 90% of Sage's revenue is now recurring, I want to increase Sage Business Cloud penetration to that sort of level, too. But going forward, our focus is on accelerating fully hosted or cloud native solutions. This will allow us to leverage the strong cloud platform that we've built over the last few years and to support our customers as they increasingly adopt digital tools and technology.

Now it's important to note that cloud connected will continue to be an important growth driver. But Sage Business Cloud will increasingly be powered by cloud native. And we expect this to be driven by new customer acquisition, but supported by migration.

Now our ambition is to accelerate cloud native across the group. But initially, our focus will be on our largest markets of Northern Europe and North America, which account for almost 2/3 of Sage's recurring revenue. In Northern Europe, we're going to increase new customer acquisition through our integrated small business proposition based on Sage Accounting, but leveraging our brand and customer success expertise to defend and grow. In North America, our priority is to grow our medium solutions, including Sage Intacct and Sage People. This will include building the solutions and commercial propositions to enable us to compete effectively in all significant industry verticals. But it's not just about Northern Europe and North America, in all of our regions, we intend to serve our customers with Sage Business Cloud and to win against the competition.

And we'll support all of this by continuing to embed SaaS capabilities, further developing a customer obsessed, innovative and fast-paced, inclusive culture to enable colleagues to perform at their best in a sustainable way. And to support these priorities, we will allocate further resource to Sage Business Cloud. We intend to increase R&D investment from its current level of around 15% of recurring revenue to around 17%. Our focus will be on enriching cloud native solutions, developing the digital environment, growing our AI capability and further driving the availability and adoption of Sage Business Cloud. And we intend to increase our investment in sales and marketing. This will drive new customer acquisition directly through digital marketing as well as helping to promote and build the Sage brand.

Now this investment will be part funded by cost savings from amongst other things, professional services restructuring and other efficiencies across the group. Given the uncertain economic environment, we may flex, particularly the level of sales and marketing investment, dynamically during the year in response to market conditions. The return on this investment is sustained, efficient, medium-term growth.

So what does all this mean in terms of our outlook? Well, firstly, it is important to acknowledge that the economic backdrop remains highly uncertain. But against this, our current expectation is that recurring revenue growth in FY '21 will be in the region of 3% to 5%. Given the profile of FY '20, we expect this growth to be weighted towards the second half of the year. Other revenue is expected to continue to decline in line with the strategy. And organic operating margin is expected to be up to 3 percentage points below last year, depending on the level of additional investment that we decided to make. And looking beyond FY '21, we expect margins to trend upwards over time as the investment drives recurring revenue growth and operating efficiencies.

So to conclude, the business performed well in FY '20 with strong profit and cash generation. We've made continued progress on our strategic priorities, building a higher quality and more resilient business. And with Sage well positioned for further growth, we are confident for the future. Now I firmly believe that by investing through this economic cycle, we will drive the long-term success of Sage, creating value for colleagues, customers, partners and shareholders.

So thank you very much. That concludes today's presentation. And Jonathan and I would be delighted to take your questions. So I'm going to hand over to the operator.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We are now taking our first question from the line of Stefan Slowinski from Exane.

Stefan Julien Henri Slowinski ***Exane BNP Paribas, Research Division - Research Analyst***

Just a question around the cloud native business and some of the investments you're making, I guess twofold. If we could just maybe go into a bit more detail on where those investments are going. I think you alluded to maybe Intacct, some earlier success there in the verticalization of Intacct. Do you expect to develop Intacct for more verticals? And then, I guess, secondly, around cloud native as well. These investments that you're accelerating, do you see that driving cloud native growth consistently at 30% over the coming years? Or do you hope to see that growth accelerate once we get through 2021?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Sure. Thanks for the question, Stefan. This is Steve. So in terms of the investments, yes, they will go into Sage Intacct, both in terms of driving additional functionality in the markets that we already operate in, but also as we alluded to, expanding the verticalization. So this means enhancing our functionality in verticals such as wholesale distribution and manufacturing where we need greater capability. But we are also continuing to invest in our small business suite, so based on Sage Accounting, but also continuing to enhance the payroll, HR and automation within that suite.

In terms of the growth, I mean we're not guiding specifically to cloud native growth. Having said that, we are being clear that we are going to push more strongly with our cloud native products, particularly when it comes to new customer acquisition. And therefore, it is our ambition to increase the rate of growth above the 30%. But that's an ambition, and we'll have to see how things go in terms of market conditions. But just to finally emphasize, the primary driver of that cloud native growth is new customer acquisition.

Stefan Julien Henri Slowinski ***Exane BNP Paribas, Research Division - Research Analyst***

Okay. Great. And maybe just a quick follow-up just on the balance sheet and the low level of net debt that you have. You mentioned, I think, the fourth category, potentially of accelerated shareholder returns, presumably large-scale M&A is not on the menu right now. So would you consider accelerated share buybacks?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

So I think on M&A, large-scale M&A, probably not on the radar, as you say. But having said that, some acquisitions absolutely are on the radar. We will continue to monitor the availability of compelling acquisitions, particularly in the technology area. But I'll just let Jonathan talk about capital structure.

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. I think on balance sheet and capital structure, I think the important thing is that the allocation policy that we have has been now completely consistent now for 2 years. And our priority has been to improve our cash conversion. You can see that we have done that now for 2 successive years where we've exceeded 100%, and this year was 123% at the operating level.

We're also in a position where through improved working capital and also some receipts from disposals, we are now down at 0.3x the net debt-to-EBITDA, which is a strong position, and also have the robustness for the medium- to long-term of GBP 1.2 billion of cash and available liquidity.

In terms of the allocation, first of all, the first element of it is to continue to invest through the P&L, and that's exactly what we've done. The second element is to look at M&A opportunities. We haven't seen any so far this year, but clearly, we did 2 good acquisitions last year. And then the third element, which is very important, is the maintenance of the dividend in real terms. And that's exactly what we've done. Today, we know it's an important component of total shareholder return. And then the very last element of our capital allocation policy with regards to returning, if we think it's appropriate or there is surplus, we don't see that being as a sensible use of our funds at this stage.

Operator

We are now taking our next question from the line of James Goodman from Barclays.

James Arthur Goodman ***Barclays Bank PLC, Research Division - Research Analyst***

And firstly, just on Intacct. I wondered if we could dig a bit into the financial performance of that business. I mean is it still a loss-making business, if you were to look at it separately? Just curious how it trended since you acquired it. But more specifically, it looks like it was growing closer to 20% in the second half, then 30% in the first half. Just wondered if you could talk about your expectations there because I would have thought the COVID, order intake effect on that business would be more seen next year than in the second half?

And then just secondly, on the Sage Accounting portfolio, you've made it very clear that this is absolutely how you're targeting the market now in the U.K., But the price points here are much lower than Sage 50. I mean they're very comparable at the 3 different tierings to 0. And I just wondered if you're now thinking that 0 is more of a direct competitor in that small segment, given the performance that they continue to pose?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Thanks, James. Jonathan, why don't you cover the Intacct performance, then I'll make some comments about the price points on accounting.

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. Intacct's important. For the full year, as you see, it grew at 26% and at a reduced level of growth in the second half. But actually, the performance really exceeded our expectations. When we reported to you at the first half stage, we had some expectations. We drew a plan for the second half. And actually, the performance for Intacct and across the whole business exceeded our expectations at this stage. The important thing to understand about Intacct is only part of the cloud native portfolio. The portfolio in its totality grew at 29%, with GBP 222 million of recurring revenue. And across the piece, those are the less profitable parts of the business, but clearly it's the fastest-growing part of the business and is the destination of where many of our customers are going to be transitioned over the forthcoming years.

I think the other thing that's just worth pointing out, just trying to give you a trajectory, is that if you recall at the first half stage, we said that the first month of the second half, which was the first full impact of the new COVID environment for trading conditions, we said that NCA was about 50% of plan in that first month on a pre-COVID basis. That has improved progressively during the second half. And as we exit the second half, we're running at a NCA level of about 70% to 80% of our pre-COVID plan. So that has recovered significantly. And we anticipate that, that should continue as we move into the first half.

I think the other thing that I would just point out, and this applies across the portfolio, is that in the second half, we focus very much on supporting our customers and maintaining our customer base, and less on cross-sell and up-sell, where their attitude to sort of purchase in the first wave of lockdown was more restricted. And therefore, you can see that we exited the year with a full -- with a renewal rate by value of about 99%, and a little bit lower in the second half. So all in all, the performance in the second half for Intacct and the whole portfolio was more resilient than we anticipated and was improving as we move towards the year-end.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

So on the accounting and the price points, first of all, yes, with the small business suite of not just accounting, but HR, payroll and also the automation that we have through AutoEntry, we now have a compelling pure cloud small business suite, which allows us to compete. Whilst we are not focused on micro business, we are able now to address that part of the market in a way that has compelling economics. So the short answer to your question in terms of are we competing against 0 and indeed Intuit? The answer is yes. And we fully intend to defend our home market and ensure that we enhance our market share. But we're not -- our priority is not going after the very, very small businesses. Although as we have enhanced or reinvigorated our relationships with accountants, it does give us the ability to sign up more of those customers. And as I say, we have the product suite to do it.

In terms of the price points versus Sage 50, Sage 50 is a very -- it is a different product. There are some Sage 50 customers who may choose to migrate to accounting. But as other competitors have found often on-premise or desktop customers migrate to cloud products quite slowly, which is why we've adopted the cloud connected strategy, which has been very, very successful to allow those customers to consume cloud services without moving completely across to a purely cloud native solution.

Operator

Our next question comes from the line of Stacy Pollard from JPMorgan.

Stacy Elizabeth Pollard ***JPMorgan Chase & Co, Research Division - Head of Software and IT Equity Research***

Two questions from me, please. First of all, you said that FY '21 revenue growth would be H2 loaded. Do you think that's more macro driven? Or is it because the comps are harder on a year-on-year basis? Or is this driven by your product cycle and releases expected?

And the second question is on margins. You've spoken a little bit about it, the difference and whether you spend more or less, and you'll make that decision during the year. It sounded like it would be -- I guess I was trying to figure out, is it more macro demand or again based on your satisfaction with the product set? And then it sounded like that 2 percentage points in R&D was a sort of definite, and then the 1% on sales and marketing could be flexible. Make sure I interpret that right. And then the extension of that question is, you said 2022 margins would recover. Does that mean back towards the 2020 -- sorry, the 22% level of 2020? Or do you think we should be more gradual in picking up margins beyond?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Sure. Why don't I take that second question first, and then Jonathan can talk about the H2 loading of the revenue. I think that first of all, the important thing to say on the margin is that to some degree, this is a product of the fact that the growth is a bit slower. We have seen an impact of COVID, particularly in the second half. And had it not been for COVID, we would have expected that in this financial year, we would be achieving a recurring revenue growth more like high single digit, maybe even double digits. So to some degree, the investments that we are making, we are basically sticking to our investment programs, but we have lower revenue growth, so we have less revenue to cover it. And having said that, we are moving up R&D a bit more than I had previously decided to do because I think it's important that we invest in these areas that I'm talking about, both in terms of Intacct, in terms of accounting, but also in terms of artificial intelligence, so that we take advantage of the accelerated digital transformation that is taking place.

Your assertion is correct, Stacy, that, therefore, that R&D investment is a bit more permanent? It is partly self-funded, though, because we are making efficiencies elsewhere. And the area that we will flex will be the sales and marketing because we're not going to spend lots of digital marketing dollars if the market's not there, if you see what I mean. So we will assess what the propensity is for customers to buy and what the market looks like for new customer acquisition. If it's there, we will invest to capture our share, but there may be months or quarters where we ran back a bit if we think that the recessionary macro environment means that actually efficiently capturing those customers that the timing is not right.

Jonathan, do you want to talk about the phasing?

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. Stacy, it's an important question. If you look at -- as you say, we've guided to 3% to 5% recurring revenue growth in FY '21, and that will be second half weighted. The best way of articulating the drivers behind that is to look at the ARR trends that we've seen during the course of this year. If we go right back to the start of the year, we exited FY '19 with a growth rate in ARR of 12.6%, and that was off the back of an exceptional performance. We expected the growth rate during FY '20 to reduce and normalize back to a more normal growth rate. And therefore, at the beginning of the year, we guided to recurring revenue growth, if you recall, of 8% to 9%. So we were already sort of baking in a normalization of the ARR growth rate. And therefore, the first half, we reported an ARR growth rate of 10%. And by the time, with an additional impact as a result of COVID. But as I say, less pronounced than we'd originally anticipated, we've exited with an ARR growth rate of about 5%. And if you look at that sequentially, H1 sequentially was about 4%, H2 sequentially was about 1%. And therefore, as we move into H1 of FY '21, we're going to be down at those lower levels of sequential growth for the first half. And therefore, that ARR trajectory looking forward informs that very much of the growth that we anticipate is going to come in the second half and not in the first half.

And then to your question, so it's not really product led or macro led, it's just the dynamics of the business that we've seen in the first half and the second half of this last year. I think the only other thing that I would say is that there is uncertainty. There's economic uncertainty. There's market uncertainty. And as Steve alluded to, market opportunity uncertainty for us. And so we will flex the spend to ensure that we're spending appropriately and efficiently. But also importantly, for you and your colleagues, we will continue to update guidance as we move through the year, the Q1 stage and the first half stage as we can get better visibility.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

And then the final thing, Stacy, sorry, I didn't quite answer the final bit of your question, which is, as we look from FY '22 onwards, we will see a gradual improvement in the margins. Whilst we're not giving midterm guidance, I have repeatedly said, that I aspire to see continuing efficiency and therefore, a continuing improvement in those margins. But it will be gradual as we see the stronger growth -- a return to stronger growth in '22 and '23.

Operator

Our next question comes from the line of Michael Briest from UBS.

Michael Briest ***UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research***

One for you, Jonathan, I think. Just looking at the disposals of sort of Central Europe and parts of international, it looks as though these weren't previously considered part of the noncore because the noncore business in 2019 was GBP 251 million when you reported it last year, i.e., before the disposals. And now it's GBP 218 million. So it looks like a lot of what you're selling is previously considered core. Can you address that?

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. And it's a good question. Look, first of all, you can see the impact of those assets being held for sale. It's important to stress that we will be retaining the global cloud native products in those regions, but all other aspects will be assets held for sale. And as you can see, just in very broad terms, we've taken out about GBP 100 million of revenue. As a result, put it on to an organic basis and about GBP 15 million or so of profit.

You -- some of that -- some of the revenue that is held for sale now related to non-Sage Business Cloud and some related to Sage Business Cloud. And that's really, just effectively, an evolution over the last 2 to 2.5 years as we see the structure of the group. And we're moving through rationalization, focusing on the fewer key territories. And therefore, the definition of those parts of the business or those product lines that fall outside of what we want to take forward, may change from our original assessment about 2 to 2.5 years ago. But I wouldn't read too much into that, but you're absolutely right. And I won't sort of break it down now on the call. But some of that revenue is absolutely had always been not seen as the core and some of it by virtue of cleaning up those regions was previously considerably Sage Business Cloud. But I wouldn't read too much into it, and it's not too material in terms of understanding the whole picture of where we are in Sage and that mix between potential Sage Business Cloud and other revenue.

Michael Briest ***UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research***

Okay. And then just to your last comment, I think you said that you would update guidance as the year progresses. I mean should we read that then what you're saying here is quite conservative because of the lack of visibility and you hope to be in a position to raise that? Or just maybe more clarity around seasonality in those investments?

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. No, it's -- look, we want to be helpful. We've set out our best estimates at this stage of the guidance for next year. But as you appreciate, we are going through a second series of lockdowns, the economic uncertainty that affects most of our major territories. Combined with rapid and increased investment in sales and marketing means that there are quite a few variable components that we probably have less visibility on than we would in sort of business as usual with an established sort of product mix. And so therefore, we put something out that to be helpful. And so all I'm flagging up is that we will keep a very close eye on how we're performing, and we'll update you. And to your question, which is a good question, does that mean you're being conservative or over optimistic? I'm saying neither. That's our best estimate at this stage. But I'm sure will be subject to change as we move through the year.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Yes. Maybe just 1 additional comment to try and give a little bit of additional context. Even within the installed base, it's very difficult to predict at the moment because customers are less likely to take additional modules or to upgrade when there is considerable uncertainty. So if you look at the dynamics of what's happening in Intacct, for example, the renewal rate by value has eased back, but it's not because of churn, it's eased back because customers are just not taking on the additional user licenses or they're not taking on the additional modules because they're tightening their belts a bit whilst they see what happens. And the challenge for all of us is it's just impossible to judge how long that uncertainty is likely to last because some of it is also driven by a lot of sentiment, how governments react, how you -- what the general feeling in the market is at any point in time. So look, we're clear. We aspire to stronger growth than we're guiding to. But this is the best estimate that we can see at this point in time.

Michael Briest ***UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research***

Okay. I mean just, Steve, Workday yesterday were talking about sort of weaker demand in core financials and HR. Would you say your product category for back office software is just maybe a little bit of the priority list at the moment? Or you think this is just general macro?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

I think what tends to happen is it depends what's happening at the time. So if you are a business and you're looking forward, and you're confident that you will survive and you're confident that you've kind of got your economic sorted out, then, yes, you look at things like efficiencies. You look at ways you can run your business more effectively. But if you're looking at, am I cutting jobs, am I going to survive, are my people on furlough, et cetera, then sure, thinking about your back office is not the top of your priority list because you're worrying about other things on a day-to-day basis. And this is what makes it difficult to predict. I think if you look at the cycle longer term, investing in digital tools, investing in automating your back office is something that's very compelling. But it isn't necessarily something that you address immediately if you're worried about survival.

Operator

Our next question comes from the line of Steven Robertson from Canaccord.

Steven John Robertson ***Canaccord Genuity Corp., Research Division - Analyst of Technology***

It's a quick question, I think. It's just on the COVID GBP 17 million provision that you've taken. Is that over and above the additional GBP 13 million, I think, that you took in half 1? And also, why did you sort of end up with GBP 17 million? Or is it sort of how long is a piece of string, I guess, but those are my questions.

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. That's a good question. I'm glad you've asked it actually. It's important to clarify. So that -- the GBP 17 million provision is the full year-end provision over and above our normal IFRS 9 provision, and is not over and above the GBP 13 million, if you see what I mean we made at the first half. So what you can see is that the first half additional COVID-related provision was GBP 13 million. By the year-end, that had moved to GBP 17 million. That wasn't as a result of a worsening of our assessment of economic conditions. It was more related to what debtors were present in which territories. It's our best estimate at this stage. It's done of economic modeling, territory by territory, working out what is the potential level of bad debts that we could see. It's our best estimate at this stage. And clearly, as we move to the H1 stage, we will revise those estimates as we can see how we progress on cash collections. I have to say at this stage, we have not seen an uptick yet in bad debt.

Operator

Our next question comes from the line of Will Wallis from Numis.

William Alexander Edward Wallis ***Numis Securities Limited, Research Division - Head of Research***

I want to ask a couple of questions about cloud connected. And firstly, the transition of cloud connected customers to native cloud, as we know, that is slow. Are you seeing any signs of that accelerating? Your customers wanting to move to native cloud products? Or is that something that you're worried about happening over the next year or 2 as digitalization is top of mind?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Yes. So we're not seeing any particular increase at the moment. I think what I would say is probably more in the sort of medium-sized customers, we're seeing a greater interest. So we're seeing people exploring and thinking about how they might migrate in the future. But it is something that, historically, I think everybody would say is pretty slow because if you've been running your business for a long period of time in a particular way, it requires moving to cloud native, requires you to change some of your ways of working. And therefore, there tends to be quite a lot of inertia. It's not something I'm concerned about. This is something where we want to offer the best solutions for our customers. And if they want to migrate, we want to be able to offer them that ability. Our real focus in terms of cloud native is new customer acquisition. It's really using those tools to acquire new customers. And the phrase I would use is supported by some migration, but the lead is new customer acquisition.

William Alexander Edward Wallis ***Numis Securities Limited, Research Division - Head of Research***

On the other side of cloud connected, obviously, what you've benefited from the move to cloud connected, particularly in the U.S. and U.K.? How much do you think that's going to be significant in Southern Europe, et cetera, over the course of the current year? Is there much left to go for now? Is there -- are you in position for that to happen this year?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Yes. I think we'll see now in both Continental Europe and also to some degree in regions like South Africa, we are going to see further movements like we did in Northern Europe and the U.S. It may be a bit slower, and also some of the uplift may vary. I mean I think it's important to say that the migration to cloud connected in both Northern Europe and the U.S. created what we described at the time as a wave of growth because we did that migration at an uplift as we offered more functionality through the cloud connected services. I think the opportunity for that uplift in other regions like Southern Europe, for example, is probably a bit lower because the customers are a bit larger and the uplift in functionality is a bit less.

The other thing I would say is that where we do migrate customers from cloud connected to cloud native, although it's unlikely to be material in the short term, where we do, do it in this -- for smaller customers, that is unlikely to result in an uplift. So a number of you have pointed out the difference between Sage 50 and Sage Accounting pricing. It is highly unlikely that if we move a Sage 50 customer to Sage Accounting, that we would see any uplift in price. With medium customers, however, there is a possibility of creating growth because if we migrate customers from the Sage 200, 300 franchise to Sage Intacct, then we would expect to be able to achieve some uplift.

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

And if I could just add. And I think that the Sage Business Cloud penetration numbers sort of almost give you the numeric answer. If you look at North America, just over 70%; Northern Europe, just over 80%, those migrations are substantially complete. And then if you look at Central and Southern Europe, it's been a very good year. So the Sage Business Cloud penetration has gone from 27% to 40%. And so this is the second wave of migrations that we probably referred to about 2 years ago. And if you look at France and Iberia, we're about 50% to 60% of the way through those migrations. So there's still further to go. It may take a little bit longer, and the revenue impact may not be quite as great because there's still plenty to do.

William Alexander Edward Wallis ***Numis Securities Limited, Research Division - Head of Research***

And just kind of 1 final clarification, just on the tax rate. Are you able to give us some guidance on tax rate going forward?

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes, you can see the effective tax rate for this year is 23%. We had the benefit this year of a French patent box claim, which meant that certain elements of our revenue is at a lower rate than the French statutory tax. We also had a couple of small one-off items, and that meant the effective tax rate came down to 23%. Our anticipation is that, that will normalize back up to 24% to 26%, which is roughly where we've been operating in previous years. So this was very much a sort of a particular year driving that tax rate.

Operator

Our next question comes from the line of Charlie Brennan.

Charles Brennan ***Crédit Suisse AG, Research Division - Research Analyst***

Just 2 quick ones from me. Firstly, just on the margin. I'll try another way of asking the question. I think we're all trying to gather arms around the range of outcomes for this year. Is it reasonable to break that up to 3-point margin impact into 2 points coming from your higher R&D and 1 point coming from sales and marketing, so the range of outcomes is minus 2% to minus 3% on the margin front? That's question number one.

And the second question is, you're obviously investing to accelerate growth. And I'm just wondering what success is going to look like for you? If I look at your guidance, it looks like you're going to be exiting this year at a high single-digit recurring revenue growth run rate. Is that what we should expect going forward? Or are you convinced that the holy grail of double-digit growth is now inevitable with this investment?

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Sure. So if we take the margin first, so as I said, there is an element here of self-funding. So the way to think about this is the R&D increase is of a more permanent nature. Now I think, just to give complete transparency, this is the area where there is a bit of change from what I've said previously. Because what I've said previously is that the run rate of R&D expenditure was sufficient. And what I'm now doing is I am accelerating some of that R&D expenditure. But that is actually largely self-funded. The area that has variability is sales and marketing because, obviously, the marketing investment we can turn on or off depending on market conditions.

So when we're saying that the margin could vary by up to 3 percentage points, we are caveating in that way for 2 reasons: one, the level of absolute revenue growth is clearly uncertain and is quite a wide range, 3% to 5%, and so this is a law of percentages, right? Whether the margin is 19%, 20% or 21%, to some degree, it depends on how quickly that growth comes through, which leads me to really your second question, which is the run rate. And we have exited FY '20 with an annualized recurring revenue of around 4.5. So that's our run rate as we exit FY '20. And to some degree, that therefore drives the absolute recurring revenue, which we see in FY '21.

So what does success look like? Well, the first thing success looks like is that you would expect in FY '21 that our exit ARR should be higher than our recurring revenue of 3% to 5% because we should be exiting the year at a higher run rate than we're actually recording in the year. We're not giving midterm guidance. But again, I -- as CEO, I have been very open about my ambitions. I absolutely want Sage to be in a position where it's delivering double-digit growth. But at the moment, it is extremely difficult to see the timescales and indeed the sustainability of that. So we're being cautious, if you like, or we're giving you the best estimate we can see at the moment. But look, our medium-term ambitions remain the same. We want to grow double digit, and we want to do that efficiently. So we want to increase -- we want to deliver increasing margins over time. But we're not going to be -- we're not going to give time scales.

Charles Brennan ***Crédit Suisse AG, Research Division - Research Analyst***

I guess the question that investors are going to have is the fact that you made a permanent change to your R&D intensity of the business. And I guess the question is, is that merely a function of competitors getting more competitive? Or is that really going to drive top line growth? And it doesn't sound like you're going to help us with an answer to that.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

No. I think I did answer that, to be fair. I think I'm saying it's going to drive top line growth. I'm just saying that in the current environment, it's extremely difficult to predict exactly when that comes through. But the fact that I'm making these investments or I've made the decision to make these investments, you should read into that, that I have the confidence that, that's going to drive growth. Because one of the things I've been consistent on since I became CEO was, I said, if we increase investment, it will be because I have the confidence that, that will drive returns, whether that be R&D or whether that be sales and marketing. So you should read into those that I am confident that this will produce increased growth, but it isn't going to do so immediately.

I think we've probably got time for 1 more question, if there's anybody else in the queue.

Operator

We are taking our next question from the line of Toby Ogg from Bank of America.

Toby Ogg

I just wanted to come back on the margin again, actually, and specifically the investments. I know you talked about margins steadily rising from 2021 onwards. I guess what gives you the confidence that, that level of investment is enough to get you into the right position? And then just secondly, on the assets held for sale, could you just give us a sense as to the growth profile of that GBP 100 million? That would be helpful.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Sure. So I'd take the first one and then Jonathan comment on the second one. There's really 2 elements to this. One is obviously the R&D. And therefore, the products and the solutions that we can see on our road maps coming through. And it isn't just the individual products, it's also the capability of Sage Business Cloud in total, backed up by the investments that we're making in artificial intelligence, and that we're also making in the ecosystem more widely. So I think we have good visibility of the road maps for our cloud native solutions, and we have a lot of confidence around that.

The second part is the efficiency of the sales and marketing investment. Now we have, for our major territories now, clear data in terms of the cost of customer acquisition and the lifetime value that we're creating by signing up those customers. So we have the confidence that in our key markets, by spending money on mark -- sales and marketing that we can drive efficiently new customer acquisition. Now I completely understand that we have not delivered that so far at scale, although we have acquired substantial new customers in FY '20, both in the small and medium customer -- in the small and medium-sized segments, but what we now have to prove is that we can accelerate that. And the fact that we are flagging this investment means that we are confident based on the data that we're seeing that we can do that. Jonathan?

Jonathan Anton George Howell ***The Sage Group plc - CFO & Director***

Yes. Look, if you -- as you can see in the announcement today, we've -- the best way to look at your question is through recurring revenue growth, 8.5% is what we reported on an organic basis. And therefore, that is removing those assets held for sale. If you were to include the assets held for sale, that growth rate would be 8.2%. And so by virtue of holding for sale, that's a 30 basis point enhancement in the growth rate that we've seen in the year that we've just reported on. If you look forward to FY '21, in very broad terms, it's a 30 basis point enhancement again, and that's built already into the guidance that you see that we're giving of 3% to 5%.

Stephen Hare ***The Sage Group plc - CEO & Executive Director***

Thanks very much for your Toby. And that's all we've got time for today. So thanks, as always, everyone, for listening to the presentation and for your questions. And obviously, if there's any follow-up, please feel free to contact James. And we look forward to talking to you again at the Q1 results. Thank you.