Sage 2021 Interim Results

Friday, 14th May 2021

Opening Remarks

Steve Hare

CEO, Sage

Good morning and a warm welcome to Sage's 2021 first half results presentation. I'm going to start with a few brief opening remarks, and then Jonathan will take you through the numbers. I'll then come back and update you on Sage's strategic progress and outlook, and give some insight into the momentum that we've created.

Key messages

So, let's start with the highlights. Sage has had a good first half, despite the continued disruption during the period, and I'm pleased with the progress. We've achieved recurring revenue growth of 4.4% and this is in the upper half of our guidance range for the full year. We grew ARR by 4.2% and our growth strengthened during the period. In the second quarter, Sage increased sequential ARR at the fastest rate since the end of FY19. And importantly, this was driven by cloud native ARR growth of 36%. This in turn was underpinned by increasing levels of new customer acquisition and supported by migrations. This is in line with the strategic priorities that we set out at our FY20 results in November.

So, with this performance in mind, I'd like to focus on three key messages, starting with the opportunity.

Our market opportunity is growing. Our customers have been resilient during the pandemic, adapting their business models to the new reality, and now, as we look towards recovery, small and medium sized businesses are accelerating their investment in digital technology as they prioritise flexibility, resilience and productivity. And as the economic environment improves, optimism among our customers is increasing.

Secondly, our capabilities. These position Sage well for this opportunity. Our global scale combined with local expertise gives us a unique understanding of the needs of small and medium sized businesses. Our solutions enable businesses to be more productive by automating processes and providing better business insights, continuously enriched through innovation. Our customers tell us that our people and our dedication to solving their problems differentiates Sage, and I'd like to take this opportunity to thank all of my colleagues for their determination and hard work over this last year.

Our well-established partner network of accountants and re-sellers, together with a growing ecosystem of ISVs, enhances our capabilities and reach.

And thirdly, execution. We are consistently executing in line with our strategy. We continue to rapidly grow Sage Business Cloud revenues, up 18% in the first half. This is at the heart of our strategy. Ultimately, I want all of our customers to be on Sage Business Cloud, where they can benefit from Sage's cloud services as part of a connected digital environment.

Our strategic investment is on track as we increase our spending on sales and marketing, and accelerate innovation through R&D. And we've largely completed our disposals programme, resulting in a leaner Sage that's focused on growth across all of our markets.

So, now I'm going to hand over to Jonathan, who's going to take us through the financial review of the first half.

Financial Performance

Jonathan Howell

CFO, Sage

Thank you, Steve, and good morning. To start with, I'll run through our financial highlights, which demonstrate the strong performance in the first half.

And as you can see, we've continued to make good strategic progress, with consistent execution against our plans.

Financial highlights

With that in mind, the key messages are firstly, high-quality recurring revenue growth of 4.4%. This was driven by good progress in new customer acquisition across Sage Business Cloud, and was against strong comparators. Secondly, on-target margin. The organic operating margin of 20.2% is in line with our targets. This reflects good business performance and planned investment to accelerate growth. And finally, strong cash conversion at 133%. This continues to be over 100% and remains a core strength of Sage.

P&L summary

Turning now to the P&L. And first, to be clear, the numbers in this presentation are on an organic basis. Total revenue has increased by 1.4% to £890 million, and recurring revenue is up by 4.4% to £811 million. Organic operating profit is at £180 million at a margin of 20.2%. This reflects planned investment to accelerate growth across Sage Business Cloud. As a result of this investment, underlying operating profit is £191 million, which is 11% lower than last year. And underlying EPS is 12.14 pence. We've increased the interim dividend by 2% to 6.05 pence. This reflects the strong performance and cash generation in the first half and is in line with our policy to maintain the dividend in real terms.

Moving on to ARR, this has increased by 4.2% to £1.6 billion. Renewal by value reduced slightly, to 97%. This was in line with the second half of FY20, reflecting our focus on customer retention, resulting in lower levels of upsell. And churn has remained stable, in line with pre-Covid levels. Importantly, this means that we've added some £110 million of ARR from new customer acquisition and reactivations in the last 12 months, up from £90 million at FY20. In line with expectations, our cloud native solutions have performed particularly well, with ARR growth of 36%.

Revenue bridge

Turning now to the revenue bridge. Our focus remains on growing Sage Business Cloud in both cloud native and cloud-connected solutions. Growth of some £71 million, or 18%, reflects strong progress in accelerating new customer acquisition, together with continued migrations. Accordingly, revenue to be migrated decreased by £30 million, in line with expectations. Importantly, cloud native solutions now represent 16% of recurring revenue, up from 13% last year. This demonstrates good execution of our strategy, with a shift in revenues towards Sage Business Cloud.

And the impact of all this is Sage Business Cloud penetration, which is now 65%. This is up from 61% at FY20.

Revenue categories

So now looking at revenue categories. As you can see, we've delivered recurring revenue growth of 4.4% against strong comparators. This is underpinned by strong growth in subscription of 11%, to £608 million, which is an increase of nearly £60 million. This was driven by growth from new and existing customers, principally in North America, Northern Europe and France. Other recurring revenue, which is largely maintenance and support, decreased by 10%, due to the ongoing migration of customers to subscription contracts. And as expected, other revenue decreased by 21% to £79 million. It is worth reiterating that over 90% of our revenue is now recurring, and 68% of our revenue is from subscription, up from 65% at FY20.

Portfolio view of revenue

Now turning to the usual portfolio view of revenue. The overall future Sage Business Cloud opportunity continues to show strong performance with recurring growth of 6%. And as I mentioned, Sage Business Cloud penetration is now at 65%. The key points to note are cloud native solutions have delivered recurring growth of 30%, to £130 million. This was mainly driven by continued good growth in Sage Intacct, together with accelerating growth in other cloud native solutions. The growth in cloud connected revenue of 14% to £345 million is principally driven by the International region, with continued growth in North America and Northern Europe. And recurring revenue in the Non-Sage Business Cloud portfolio decreased by 8% to £82 million, in line with our expectations.

North America

Looking now at the regions, North America delivered recurring revenue growth of 6% and Sage Business Cloud penetration is now at some 73%. Cloud native growth is driven by Sage Intacct, resulting in recurring growth of 19% to £78 million. And growth in cloud connected is driven by both existing customer migration and new customer acquisition in both the Sage 50 and Sage 200 franchises.

Northern Europe

Northern Europe had recurring revenue growth of 3% and Sage Business Cloud penetration is now at some 85%. This reflects accelerating growth in cloud native solutions and continued success in Sage 50 cloud connected. Cloud native growth is driven by new customer acquisition in accounting and HR solutions, supported by ongoing migrations. And Sage Intacct continues to build good momentum in ARR.

International

And finally, the International region, which now includes Central and Southern Europe. Recurring revenue grew by 4% and Sage Business Cloud penetration now stands at 43%, compared to 32% last year. France, which is the largest country in this region, grew recurring revenue by 5%. This was driven by growth across the Sage Business Cloud. And Africa and APAC delivered strong recurring growth of 8%. This reflects a good performance in local products and cloud native solutions, particularly Sage Accounting in Africa. This was offset by a decline of 4% in Iberia, reflecting a reduction in maintenance and support revenues.

Strategic investment to drive growth

Looking now at the evolution of our cost base, our planned strategic investment remains on track. This is helping drive growth across Sage Business Cloud, including the very good performance in our cloud native solutions. In line with these plans, investment in sales and marketing has increased to £340 million. This represents 42% of recurring revenue, an increase of 100 basis points. And investment in product development grew by 240 basis points to £135 million. This now represents some 17% of recurring revenue. Steve will give more colour on this later.

Strong cash generation

Turning now to the cash flow, this remains a core strength of the business. Cash conversion of 133% continues to be strong. Importantly, this has now been over 100% for more than two years. And as you can see from the bridge, working capital improvements are the key driver of this, due to growth in subscription revenue and continued strength in debtor collections. Net of interest and tax, this has generated free cash flow of £190 million.

Robust financial position

Now turning to the balance sheet and leverage, as a result of particular focus in recent years, Sage has a resilient balance sheet and strong liquidity, which has served us well during this period of economic uncertainty. The group has over £700 million of cash and also undrawn facilities of almost £700 million. This means that cash and available liquidity totals nearly £1.4 billion. The group issued a £350 million bond in March, extending its debt maturity profile and diversifying its sources of funding. Net debt has reduced to £96 million and net debt to EBITDA is now 0.2 times.

Capital allocation

Turning now to capital allocation, our policy remains unchanged. We will continue to focus on organic investment and acquisitions, to accelerate execution against our strategy. We will maintain the dividend in real terms and therefore we've increase the interim dividend by 2%. And lastly, we will consider returning surplus capital to shareholders. In line with this, Sage announced in March the launch of a £300 million share buyback. This reflects both the sale proceeds from recent disposals and strong cash generation. As I mentioned, our leverage ratio is currently 0.2 times. Over time, we expect to move back to our medium-term range of 1 to 2, through organic investment, M&A and capital returns.

Summary

And so to summarise, Sage has delivered a strong and consistent performance, resulting in recurring revenue growth of 4.4%. Secondly, we've delivered an organic operating margin of 20.2%, in line with our targets. And finally, strong cash conversion of 133%. This remains a core strength for Sage.

Thank you and now I'll hand back to Steve.

Strategic Progress and Outlook

Steve Hare

CEO, Sage

Thanks, Jonathan. So as you've heard, the business performed well in the first half. And as I said, this is a result of continued strategic execution.

Purpose-driven performance

And underpinning this is our purpose. We're here to help our customers thrive. This, together with our over-arching value that we do the right thing, shapes the important role that we have to play in supporting businesses and equipping them for the future.

But our purpose extends beyond our customers and also shapes the wider role that we play in helping our communities and the planet. This isn't new to Sage. We set up Sage Foundation five years ago as a way for colleagues to channel their energies into charitable causes, and we're committed to knocking down barriers so that everyone has that opportunity to thrive, both at Sage and in our wider communities.

As we reflect on how the events of the last year have highlighted inequalities in society, we want to do more, for example, by developing digital and business skills in under-represented groups, helping to build and support the next generation of more diverse and sustainable businesses. And as part of our environmental commitment, we've been evaluating emissions across our own operations, but also our full supply chain, and we will shortly commit to science-based targets with a roadmap to net zero, and building on our favourable ESG ratings, from MSCI and Sustainalytics.

All of this is the right thing to do. It's also good business. I believe that strong performance comes from being purpose driven. It means we attract people who care, we can better address key business risks, and it makes us the first choice for customers who are looking to support positive change.

Saas capabilities and culture

Now, our purpose is core to our culture and is key to ensuring we have engaged, motivated colleagues. But alongside this, we're investing in the core areas of digital marketing, artificial intelligence and innovation, to enhance our SaaS capabilities. Providing training and development opportunities are key. So for example, over 1,000 colleagues across the organisation have now undertaken our '10x continuous innovation' training, which is encouraging people to experiment, iterate, learn without the fear of failure.

Now, supporting colleague wellbeing is a key priority. In addition to our thriving colleague support networks, we've been running initiatives focused on mental, physical and financial wellbeing. We've also given colleagues additional wellbeing days, over and above their normal holiday allowance. And we're making sure that we retain these initiatives as our offices start to reopen and as we transition to new ways of working and collaborating under a hybrid model. And I'm pleased and proud that in spite of the pressures of lockdown and remote working, our people continue to show real enthusiasm and commitment, and are willing to share that publicly. So as a result, Sage has been listed among Glassdoor's best places to work in the UK, Canada, France and the US.

Customer insights

Now turning to customer insights, where the breadth of our business gives us really good visibility into small and medium business trends globally. And what we've seen is that customers have been resilient, adapting their businesses to the new environment, and they're accelerating their investment in technology to become more flexible and more productive. Now, that includes not just finance systems, but also people and payroll, as businesses do more to ensure colleague recognition and retention.

Now, as the world starts to look to the future, confidence is definitely increasing. In our recent survey of US businesses, 75% anticipate growth this year, and almost half expect their revenue to return to pre-Covid levels by the end of the year. There's also been a record number of new business formations. And finally, driving an inclusive, sustainable recovery is really important. Over 70% of our customers say that they, like Sage, are committed to improving their environmental and social impact. And they want to work with companies who are doing the same. And all of this means that the opportunity for Sage is increasing.

Addressing our customers' needs

Now, as I said at the start of the presentation, Sage is well positioned to capture this opportunity. With about half our revenue coming from solutions for small businesses, and half from solutions for medium, we are a global business with a well-established brand. Our customers trust us and we champion their interests with governments and at global events like the G7's business conference this week. Our solutions, whether cloud native or cloud connected, enable businesses to be more productive, resilient and flexible. And we are innovating to enrich these solutions, not just adding better features but providing a rich digital environment, a network of applications and services that make it easier for customers to connect, collaborate and do business. Customer engagement with these services is rapidly accelerating, with almost 10 million log-ins to Sage Business Cloud Services in March, and that's up nearly 40% during the first half.

Sage is differentiated in particular by our people and their dedication, not just to serving customers but to solving their problems and helping them thrive. And Sage also has a well-established partner network, including accountants to support small business segment, resellers and distribution partners to support medium-sized businesses, and ISVs to enhance the capabilities and reach of our solutions.

Now, last week we launched Sage Intacct into the AWS marketplace, further enhancing our distribution. And to lead our global partner strategy, I'm delighted that we've hired Aziz Benmalek, who spent many years at Microsoft and brings deep partner and customer knowledge.

Progress in medium

Now, as I said in November, that we would focus initially on accelerating cloud native growth in the medium segment in North America and in the small segment in the UK. And in medium, we've successfully driven growth through Sage Intacct, adding over 700 new customers in North America during the first half. That's an increase of more than 50% compared to the first half of FY20, driven both by increased demand and supported by progress in migrations. And also, outside North America, we've now achieved almost £3.5 million of ARR from Sage Intacct, and that's up from just under £2m at the end of FY20.

Contact Engine, shown here on the slide, is a really good example of a customer migrating to Sage Intacct. They're experts in conversational AI technology, and started in the UK with just six people, but have rapidly grown to more than 85 people on both sides of the Atlantic. And they've grown with Sage, graduating from Sage 50 to Sage Intacct as their processes matured, and they're now benefiting from multi-currency capabilities, bespoke reporting and integration with their other systems.

To drive further growth, we are investing to enable Sage Intacct to address additional industry verticals more effectively. And beyond Sage Intacct, we've also seen cloud native growth through migrations to Sage Partner Cloud, our managed cloud solution, complemented by the launch of a new cloud-hosted data and analytics service.

Progress in small

In the small segment, we've focused on developing and growing our cloud native software suite, initially in the UK. To drive growth, we've invested in sales and marketing, optimising our e-commerce platform and growing the accountants channel. As a result, Sage Accounting is winning more customers at a higher average contract value than ever before. Direct customer wins through the digital channel have doubled in the first half. Customer wins through accountants are up by a third. And we've also increased the rate of cross-sell of Sage Payroll to Sage Accounting customers by 50%. And we've grown Sage HR, both through new customer acquisition but also significantly through migrations. Customer ratings of Sage Accounting is also improving. Its Net Promoter Score is up 24 points year-on-year.

Now, on the slide you can see someone I spoke to recently, Sam Mitchum from SJCM Accountancy in Lancashire. Now, Sam set up her accountancy practice in 2019 and she's needed to be agile, giving advice on government initiatives, loans and furlough schemes, all whilst growing her client base. Now, Sam chose Sage based on the quality of our solutions, but critically, also on our human customer support element, and she's now become a member of our Accountants Advisory Board, providing valuable feedback on our products and services.

Investing to accelerate growth

Now, as Jonathan showed earlier, we've increased our strategic investment in both sales and marketing and R&D during the first half. This is very much in line with our plan and is helping to drive growth.

In sales and marketing, we're investing in the capacity and capabilities of our sales teams, but we're also driving growth through increased digital marketing investment and, most notably, through our Boss It advertising campaign. Now, let's take a quick look at this campaign for those of you that haven't seen it.

VIDEO: Who's the boss? I'm the boss. No, I'm the boss. He thinks he's the boss, but I'm definitely the boss. Yeah, but I'm still the boss. Taking control of business. I was born ready. Invoices, sorted. Expenses, smashed.

Now, it's live in almost all of our geographies. Boss It has had a really positive impact on perceptions of Sage, driving engagement and sales. In the UK alone, it's significantly increased website clicks and online conversion. And we're taking this campaign to new audiences. So for example, reflecting the fact that 60% of business owners who launched their venture during the pandemic are aged between 18 and 34, we ran Boss It as the first ever B2B campaign targeting small businesses on TikTok. This resulted in over a million user-generated video responses, of businesses showing how they've been bossing it through the challenges of last year, and amazingly generated over 7 billion views, a really powerful driver of brand awareness and perception.

Now, going into the second half, we'll invest further in the Sage brand, looking to drive deeper customer engagement and to take Sage to new audiences.

Turning to innovation, in R&D we're investing to accelerate the development of the Sage Business Cloud digital environment, to enrich our cloud solutions and to enhance our AI capabilities. Now, the digital environment is the focus for Sage's technology strategy. By enhancing the services available through Sage Business Cloud, we're making the environment more compelling to customers, increasing the number of users and growing the value of the network. And that's why we've made further investments to create a more scalable and configurable microservices architecture, allowing easier deployment of new cloud services and integrations with third-party software. We've also invested in the services themselves. For example, we've enhanced our service for bank reconciliations, with over 11,000 banks now connected, take-up has grown by more than 50% in the last six months. And we're developing other services too, such as secure digital invoicing, collaboration, workflow tools.

In AI and machine learning, we've substantially expanded our team of data scientists and AI engineers, and the sheer scale of Sage Business Cloud across cloud native and cloud connected means we can develop more accurate AI tools much more quickly. So for example, our general ledger outlier detection tool has identified over 15,000 incorrect journal entries since commercial launch in February, and this is based on a training data set that is growing by 500,000 transactions a day. Our recent acquisition of Task Sheriff, an Israeli-based AI specialist, will further bolster our capabilities in this area.

We're also investing in strategic partnerships that allow us to innovate and broaden our insight into emerging business trends. In December, we completed a minority investment and strategic partnership with Brightpearl to enhance our e-commerce capability, unlocking further opportunities for Sage Intacct. We also made a minority investment in CountingUp, a combined accounting and banking app for sole traders and micro-businesses. And two days ago, we announced our new partnership with Tide, to provide accounting and compliance as a service to small business owners and entrepreneurs.

Outlook

So, let's move on to the outlook. Following the strong performance in the first half, full-year recurring revenue growth is now expected to be towards the top end of the 3% to 5% range. Other revenue will continue to decline, in line with the strategy, and consistent with previous guidance, we expect our margin to be up to 3 percentage points below last year, reflecting the strategic investments that we're making in the business.

Now, as we look beyond FY21, we continue to expect margins to trend upwards over time, driven by top-line growth and operating efficiencies.

Conclusion

So to conclude, Sage performed well in the first half, the market opportunity for Sage is growing, digital transformation among our customers is accelerating, and we have the right solutions to help them transform and thrive. We have a strong platform from which to scale and I'm happy with the levels of investment that we're making and the returns that we're seeing. We also have a team that knows how to execute, delivering high performance with a strong sense of purpose.

I firmly believe that the actions we are taking will drive the success of Sage for all our shareholders and all our stakeholders, supporting colleagues, customers, partners and communities, both now and in the long term.

Thank you very much. That concludes today's presentation, and Jonathan and I would now be happy to take any questions, so I'm going to hand over to the operator.

Q&A

Paul Kratz (Jefferies): Hi. Good morning everyone. Thank you for taking my question. I just had one question really, around the development of your annualised recurring revenue. If I look at your FY20 figures, of £1.61 billion, and I effected[?] for churn, it suggests that actually customer additions in the first half have been maybe a little bit slower. I mean, is there anything else that we should take into account for that? For example, you know, FX, or any other one-off impact that might be within that?

Steve Hare: Thanks very much for your question, Paul. No, I think, you know, if we look at the first half and we compare it to the same half in FY20, we've definitely seen a pick-up in new customer acquisition, I think, and we'd quoted, for example, with Sage Intacct that we've added 700 customers in that first half, which is, you know, a 40% increase over the same period in the previous – in FY20. And also in the small segment in the UK, we've seen – also seen a pick-up in NCA. So, I mean, we've quoted that we've added over £110 million of ARR through new customer acquisition and [inaudible] and migrations. And two-thirds – about two-thirds of that is NCA. So, we're definitely seeing strength there.

Jonathan Howell: And yes, I could also add that if you look – if you compare that with the July year-end figure – sorry, FY20 figure, then you would have – you'd see that we're at[?] 90% in terms of – sorry, £90 million in terms of ARR. And so therefore, there's a good – you know, there's a good increase compared with the last year-end number that we gave. So, there is improvement there.

Paul Kratz: And just maybe a follow-up question. In the second half, it's clear that there is going to be an acceleration I guess in your ARR growth. Could you maybe share with us any kind of figures around exit rates or how renewal rates are looking at this point that gives you the confidence to kind of raise your guidance in the first half?

Jonathan Howell: Yes. So if you look at the progression on ARR, last year at the first-half stage, we had ARR growth of 10%. As we exited last year, FY20, we grew ARR at 4.8% and we just reported 4.2%. And if you recall, at the Q1 stage we expected that the decline in the ARR growth rate would bottom out during the course of the first half. As you can see from the guidance that we've given today for recurring revenue, that's completely compatible with that. And so, we're now guiding that recurring revenue will grow towards the top end of the range of 3% to 5%. And so therefore, if we are exiting at the top end of the range of recurring revenue, then by definition ARR will be higher than that when we exit FY21. And so we are expecting that to accelerate during the course of the year.

Paul Kratz: Thank you. Thank you.

Adam Wood (Morgan Stanley): Hi. Good morning and thanks for taking the question. I've got two please. Just first of all, on the Sage Business Cloud, we've got very strong growth in the first half, of 18%, but obviously you're flagging that some of that is being helped by migrations from some of the products that are outside of that scope. Obviously, very simplistically we get down to what the group's doing if we put everything together, but could you maybe – but not everything that falls out of the other space will be going into Sage Business Cloud. Could you maybe just give us a little bit of a feel for what's going on in the Sage Business Cloud, excluding those kind of internal migrations? You know, what's happening externally and with new customers? That was the first one. And then secondly, you know, you commented a few times around Sage Accounting. It feels as if there's a – or a little bit of a change in the market there and you're having more success. Could you kind of talk about competitive environment and maybe specifically on support, how you're managing to make that cost effective in that space, which I think has been a challenge in the past? Thank you.

Steve Hare: Sure. I'll let – I'll say a few words and then I'll let Jonathan just talk a little bit more about the detail at Sage Business Cloud. But we've definitely in Sage Business Cloud seen a switch to more of the growth coming from new customer acquisition, rather than from migration and reactivation, but Jonathan can give a bit more colour. And I'll – I'll just answer that second question. We're definitely making more progress with Sage Accounting in the UK and with the whole suite, so it's not just accounting, it's also the HR and payroll add-ons. We've seen our win rates[?] improve and we've seen our ACV improve. But I would be the first to admit that, you know, it's a very competitive market. But the good news is the market's getting bigger all the time, so as small businesses invest more and more in their digital tools, the size of that market is increasing, but we're definitely making progress. Jonathan, do you want to talk about Sage Business Cloud?

Jonathan Howell: Yes, and I think that the most important thing that we've seen develop in Sage Business Cloud in the first half is the growth in cloud native. And so you can see on a recurring revenue basis that grew at 30% to £130 million, and on an ARR basis, it grew by 36%. About 60% of that ARR base comes from Intacct and that grew at 19% in North America in the first half. And so therefore, by definition, the other products in that cloud native space were growing significantly faster, and that's really come from Sage Accounting, Sage People and Sage HR, where not only have we seen NCA, we've seen good migrations also with Sage Partner Cloud. So, if you take all of that together, you can see a rapid increase in ARR growth in cloud native, and that is also complemented and supplemented by what we're seeing going on in cloud connected. As you know now, North America and Northern Europe are substantially migrated into cloud connected, and so that's the Sage 50 base, the Sage 200 base in those territories. It's in the region of about 85% to 90% migrated. But we still have further to go in continental Europe, where that migration is about probably 60% of the way through. So all in all, we've got a good mix of growth coming into the Sage Business Cloud. Some of that was the existing trend, which we saw going into cloud connected over the last two years, and some of that is new, through both NCA and also migrations. And I think just on cloud native, one last point to note is that of that total growth in cloud native, about a quarter or so of that came from migrations. So by definition, the rest of that is NCA or up-sell and cross-sell, and the bulk of that is NCA.

Adam Wood: That's very helpful, thank you.

Ben Castillo-Bernaus (Exane BNP Paribas): Good morning. Yes, thanks for taking my question. Two things really on NCA and the marketing spend. On the NCA trend, you mentioned at Q1 that you would sort of return to something like 80% of pre-Covid levels. Can you just talk about where we're at now versus pre-Covid levels? And importantly, how does that compare to your expectations say at the end of the FY20 when you though – you know, what was your time horizon on returning to those levels? And then secondly, can you just touch on this – the Boss It marketing campaign? You know, you're using TikTok now, which is quite a change for Sage. Can you just talk about the traction you're having there versus your initial expectations before you launched it? You know, is this an attempt to take the fight more to the likes of Xero and Intuit, who have historically had success in that low end of the market? And has the success in those campaigns sort of changed your outlook on where you'll allocate incremental spend for the rest of this year? Thanks.

Steve Hare: Sure. Thanks – thanks for the question. So, on NCA, we are really back at – in terms of run rate, I would say we are back at now pre-Covid levels. And actually, I alluded to in terms of pipeline, you know, we're seeing increasing confidence and optimism amongst the small medium business community. And therefore, from an opportunity perspective, you know, there's reasons to be optimistic about how the size of the market opportunity is actually increasing as people look to invest in digital tools. In terms of where we are versus where we thought we were maybe sort of a year or so ago, it was obviously very difficult to predict a year ago. You know, I would say we're probably about where we thought things would be. Maybe a bit more optimism, maybe a bit more confidence than perhaps we would have anticipated, but in terms of results, you know, probably sort of pretty much bang in line. In terms of the Boss It campaign and, in particular, you know, what we did on TikTok, yes, look, you know, we are looking to refresh, you know, how Sage is perceived from a brand perspective, and you know, we are looking to, you know, win our fair share of voice and market across all of the customers and markets that we're seeing to serve. We're doing a lot of experimenting, so you know, doing something like TikTok was a bit of an experiment to see how that would work from an engagement perspective, and I would say that, you know, very much exceeded our expectations in terms of the interaction that we got. The other thing I'd point to, this week we announced the partnership with Tide, and so to provide accounting as a service as part of their banking offering. I think it's fair to say that type of partnership with Tide is not something we would have done two or three years ago, and I'm very excited by, you know, doing that sort of thing, where we can access, you know, new markets in a very effective way by partnering.

Adam Wood: Thank you. That's helpful. If I could squeeze one more in, just on the – more on the Intacct side of things, about targeting industry verticals, do you touch on, as where are[?] the near-term industry focused that you can go after?

Steve Hare: Yes. We're really alluding to doing more in the complex distribution, wholesale distribution, and also manufacturing, you know, where historically Intacct's been very strong in non-for-profit service industry, etc, and we're doing work to, as I say, expand, you know, more deeply into those additional verticals.

Adam Wood: Okay, thank you.

Steve Hare: Thank you.

James Goodman (Barclays): Morning. Thank you. Firstly, just to come back on accounting in the UK, in the past you've shared some subscriber numbers for that portfolio, I think in the UK and globally, and given us a couple of data points around ARPU. It seems like it's gaining a lot of traction now and a pretty established market presence. I wondered if you might give us some ball-park figures there for, you know, particularly sort of subscriber numbers and ARPU development in the UK. And then secondly, coming to the investments, a couple of years ago when you announced significant investments, it took quite some time to actually get that investment into the business, I think because of, you know, the time it takes to hire, etc. And presumably there's still some challenges around hiring and the bulk of the 200 basis point investment you put in in the first half was in the marketing initiatives that you spoke to. Is that really where the investment will remain focused for the second half, or are we seeing sort of an increase in R&D and hiring as well, and do you expect sort of a shift of that investment as we go through the rest of the year? Thank you.

Steve Hare: Sure. I'll take the marketing question first and then I'll pass to Jonathan to see whether – see how helpful he's prepared to be over your ARPU and subscriber number question. On the marketing and R&D, yes, we are adding in terms of hiring. Particularly in the R&D we have, as we alluded to, been hiring AI and ML specialists, data scientists. We've also been adding into – both Intacct and the small business suite, including accounting, HR and auto entry. But you know, most of the additional monies that is going into sales and marketing is going into marketing, and it's going into digital marketing to drive demand generation and it's going into, you know, things like the Boss It campaign, as we seek to, you know, enhance our brand, increase our share of voice, and ultimately, you know, convert more of the demand generation into digital, particularly in small. Now, it's also important with – you know, the partner channels are important, so in small the accountants channel remains incredibly important, and in the medium segment, you know, a lot of our growth does come through business partners, through our network of VARs. And I just point to the fact that 39 out of 40 of our top traditional Sage partners who carry Sage 200, 300 in the US have now signed up and are dual-authorised to carry Sage Intacct. So, not only will – are they now looking for new customers using Sage Intacct, but they're also looking at where they can migrate customers from Sage 200, 300 to Intacct. Jonathan, do you want to cover the accounting point?

Jonathan Howell: Yes. You know, thank you James for the question. Look, first of all, what we can say about accounting in UK: we've seen a sharp pick up in NCA – a very marked pick up. And in addition to that, we've seen a good attach rate, with Sage HR, auto entry and also our cloud payroll product. And that is going very well indeed. The other thing that I can reiterate to you is what I said in a previous question, was that with an ARR growth rate of 36% in cloud native, and 60% of that revenue base being cloud – being Intacct, then clearly the other products, which are Sage People, Sage Accounting, and migrations are growing considerably faster. The other thing that I can say is that the LTV to CAC and the unit economics are exactly where we would expect them to be and are – demonstrate to us that we are investing the right way and generating good value. But the specifics of, you know, can we give individual count to[?] ARPU, as you know now, for a good number of years we haven't broken down product by product in our individual territories, individual sort of unit counts. And so we're not going to start doing that. But I hope the information that I've given you though is – gives you a good indication of how positive we feel about these new cloud native products.

James Goodman: Yes, that's very helpful, thank you. Just quickly on sort of price, just as it relates to net renewals into the second half, I think you delayed some price rises through Covid, sort of partly related I guess to ARPU, but in[?] the 97% net renewal that you had, is there a price element that's going to help you to increase the net renewal into the second half?

Steve Hare: No. In the second half, we are likely to continue not to implement across-the-board price increases. There are some discount unwinds, so you know, there's a little bit of help from that, but we're not going to put across-the-board price increases through as a matter of norm.

James Goodman: Okay, much appreciated. Thank you.

Jonathan Howell: James, sorry, just one additional thing on that, because – sorry, a couple of – yourself and previously someone touched on renewal rate by value. As you can see, it's 97%, which is absolutely in line with the second half of last year, and that is underpinned by a churn rate which has been absolutely consistent, the first half this year with the second half last year, and indeed which in turn was in line with the first half of FY20, which is you recall was entirely on a pre-Covid basis. And the reason I just want to call that out is to say that the – you know, across the small and medium segments, across our cloud native and our long-standing Sage 50 and Sage 200 products, we've seen incredible resilience over the last 12 months, and that gives us a really good base for a really good stepping-off point into FY22 with regards to our ability to continue to grow ARR.

James Goodman: Okay, thank you.

Stacy Pollard (JP Morgan Cazenove): Hi. Thanks very much for taking my questions. I have three please. Firstly, can you give us those cloud connected numbers for mainland Europe again? And then how does that compare to cloud native expectations in Europe? And maybe just a quick comment to Iberia, where recurring revenues fell – maybe just a quick explanation for what happened there versus France and Central Europe, which seemed to do better. Sorry, that was all one question. Number two: you mentioned operating margins could improve from 2022 onwards and, you know, really trying to get a sense of how we should think about that evolution over the next few years. Is it kind of a gradual return to the, you know, 21%, 23% level that you were at, or are there step changes along the way, and do you think you could ever get back to that 27% that you ran at for quite a number of years, and perhaps that's longer term? And third question: just basically, even with the £300 million in share buybacks, you're probably running still below your comfort zone of 1 to 2 times net debt to EBITDA. So, sort of what happens from here? Are you considering more M&A? And indeed, could you do more disposals as well or is that pretty much done? Sorry, that was a lot of questions.

Steve Hare: No, thanks Stacy. I'll pass over to Jonathan on the cloud connected and the capital allocation. Just a quick word on margin. The way to think about it is, you know, we want to reassure people that it is an improving trajectory from here, but it will be gradual, and what will come first is an increase in the rate of revenue growth. So, it's important we continue to invest, particularly into sales and marketing, to pull through that new – continue to pull through that new customer acquisition. You'll start to see the recurring revenue growth accelerate, as Jonathan has alluded to, and then as that happens the margin will follow. As you know, we're – you know, we're not giving, you know, specific guidance, so the time scales, you know, will be – it will be a gradual thing. Jonathan, do you want to handle the other two?

Jonathan Howell: Yes. So, in terms of France and Germany and Continental Europe, that product mix is still primarily on premise or cloud connected, and you know, across the Sage 50 and Sage 200 families, we're about 50%, 60% penetrated in terms of migration to cloud connected. Cloud native: that will be a subsequent way in those territories, but it's definitely planned and this is where some of the investment is going. In terms of Iberia, that was the one territory, as you could see, where we saw a decline in revenues compared to last year. And that was really due to customers [inaudible] effectively coming off plan. So these were on-premise customers who were coming off plan during the course of the period. Those customers are not lost. You know, they're still using the software and we hope that, you know, when we all emerge from the lockdowns across Continental Europe, we will see an improvement there. In terms of capital allocation, you're absolutely right. We're running at 0.2 times net debt to EBITDA, at a net debt level of about just under £100 million. We have made a very clear statement in the announcement that we will move back into the range of 1 to 2 times and we will do that through three different ways. We will do that through organic investment, through the P&L, which is what we are doing. We will also do additional M&A as we find appropriate opportunities that we can execute on. And then, you know, if there is surplus, we will also return capital to shareholders. And so that point – and exactly to your question – we're now about £120 million through the £300 million share buyback programme that we started only in March. And that will continue and we anticipate that that will complete towards the end of August or early September. We are therefore really executing completely in line with the capital allocation programme and model that I've actually, you know, probably talked everybody through consistently over the last two years or so. We will just keep under review and we will execute to make sure that we do move back to within the range, as you describe. I hope that answers the question, Stacy.

Stacy Pollard: Disposals – I guess you're saying that's mostly done?

Steve Hare: Sorry, say that again, Stacy.

Stacy Pollard: On the disposal side, that's largely completed?

Steve Hare: Yes. Yes, largely completed. We're very focused now on scaling and growing. Obviously, there may be the odd one, but that's not the focus now. The focus is scaling and growing.

Stacy Pollard: Okay, got it. Thanks very much.

Steve Hare: Thank you.

Gautam Pillai (Goldman Sachs): Good. Thanks for taking my questions. Firstly, can I please check if there's an element of conservatism built in the guidance, given the strong start of the year and the business environment is getting better and comps are considerably easier in the second half? Are you baking in any assumptions of higher churn as the furlough and support schemes roll off? Secondly, Xero commented yesterday on increasing level[?] of investments to capture more of the [inaudible]. Does that have an impact on your investment plan over the mid-term? Thank you.

Steve Hare: Yes, so if we take that second one in terms of the investments in verticals, yes, that's not new. We're just emphasising that that's what we're doing. But it's part of the existing investment plans. I'll let Jonathan just comment a little bit more about guidance, but yes, just to say that, you know, we've seen a lot of resilience in our customer base, and whilst there is always a risk as the furlough and government support schemes are reduced, we do not anticipate that having a material impact. We think that our customer base is showing, as I say, a lot of resilience and there's a lot of optimism amongst our customers for the future. Anything you want to add, Jonathan?

Jonathan Howell: No. So, just on guidance, you know, what you see that we've done today is we've just moved the guidance towards the top end of the range, to 3% to 5%, and that is completely consistent, you know, with our best estimate at this stage. But you know, we will be updating you, you know, at Q3 and obviously at the year-end. But that is very much our best estimate at this stage.

Gautam Pillai: Got it. Thank you.

Michael Briest (UBS Investment Bank): Thank you. Good morning. A couple from me. Just starting with a clarification, Jonathan, on ARR, I wasn't sure whether you were saying it was up £90 million sequentially, comps and currency. Can you just tell us what the sequential growth in ARR is on an underlying basis? And then just looking at the – sort of following up on the last question, I mean, insolvency rates in Europe I think are down about 30% to 40% year-on-year, and in North America or the US, down 15% because of all the government support. So, sort of trying to marry that with your comments just now about business sort of sustainability and your decision to not change the big bad debt provisions you took against Covid last year, so something doesn't quite match up there. You've still got lots of provisions for bad debt, but you're saying you don't expect attrition to increase, but insolvency is very low versus history. And then I've got one on margins, which is, you know, you have 300 basis points down in the first half. Is there any prospect it will be better than that for the full year? Because the guidance is still for up to 300 basis points in[?] effect.

Steve Hare: So, let me – I'll just touch – I'll touch on the insolvency point from a market perspective, and then I'll let Jonathan answer the rest. I think if you take the market as a whole, there is going to be some changes. So, there will be businesses that, you know, go out of business, but at the same time, there's also in our major markets record levels of business formations. What we're also seeing is amongst, you know, bigger businesses, more established businesses that have been around a long time, you know, those sorts of businesses are very resilient, they've seen difficult times previously and, you know, talking to customers and taking our own sort of surveys and customer pulses, you know, our view is that the impact on Sage – it may not be the same for others, but the impact on Sage, you know, we believe will be within the boundaries we've set, i.e., you know, Jonathan can comment more, but we have put bad debt provisions in place. We don't see any reason to take any, you know, more pessimistic view looking forward, based on the information we have. Quite the reverse. If anything, we're more optimistic and we're definitely more optimistic about new customer acquisition. Jonathan?

Jonathan Howell: Yes, so just on the bad debt provision, that's at – this is the additional bad debt provision that we put in place a year ago for the first time, on the onset of Covid – that's being held at about £16 million. We have not seen an uptick in bad debts over the last six months, or indeed over the last 12 months, but nonetheless, for exactly the point that you raised, we are – you know, we are holding that provision in place and we will sort of review that, you know, as we move through the next couple of quarters. The other thing that's[?] just worth talking about in relation to the resilience of the base is that, you know, if you're looking at us compared with peers, don't forget that about half of our revenue and customer base comes from small segment and the other half comes from medium segment. And by definition, those larger, more established businesses are therefore more resilient during – you know, during a downturn. And then in the small segment, Sage 50, you know[?], that is towards the top end of the small segment as opposed down at the micro and start-up, and those are more established businesses, and they've probably been customers of ours for 20 or 30 years, they've been through a couple of recessions. So again, we anticipate against – you know, against peers that there's a degree of resilience there that may not be, you know, first apparent. Having said that though, we are holding that bad debt provision and we will continue to monitor it as we move forward. In terms of sequential growth rates, the – you know, if you look on a sort of an actual currency basis, as you can see it looks pretty flat, but you know, we always report, you know, on a constant currency basis, you know, and as you can see, there is momentum there. If you take Q4 last year to Q1 this year, that was 1% sequential growth. Q1 this year to Q2 this year is 2% sequential growth in ARR. So, this is very much compatible with the momentum that we're talking about and the ARR growth rate bottoming out during the course of the first half. And if you just then look at recurring revenue, sequential growth this first half on the second half last year is 3%, and that compares with sequential growth at the second half last year of 2%. So, all of the measures, on a quarterly basis or on a half-year basis, are indicating, for both ARR and recurring revenue, an improving trend as we go into the second half. And then I think lastly in terms of margin – and I'll be brief on that because we've got very clear guidance – we guided at the beginning of the year for a decrease in margin of up to 3 percentage points. At the Q1 stage, we'd slightly changed that guidance and said it would be more second-half weighted, and that's a – you know, completely consistent with what we're seeing at the first half stage now. So, we anticipate that we will continue to invest and if there's, you know – and if possible, we will accelerate investment, if we think that's appropriate, but we are still sticking to that guidance for the full year of up to 3 percentage points. But don't forget that we are staying that as we move into FY22, we do expect that margin to – you know, to begin to trend upwards over time.

Michael Briest: Thank you.

Ross Jobber (Citi): Good morning. Thank you very much. I wanted to focus, if I may, on the comment you made about rising margins. You identified two principal drivers: top-line growth and operating efficiencies. And it's really the second of those, the operating efficiencies, that I wondered if you could give us more colour. I mean, clearly you are a scaled business in many areas. You've got global scale. Your non-core businesses are now largely disposed of or in the process, and I think you described yourself as having a renewed focus. So, do you think that you could – given that in mind, could you give us a bit more colour on exactly what these operating efficiencies[?] – which areas these operating efficiencies are going to arise that are going to help drive up the margin? Thank you.

Steve Hare: Yes, sure. I mean, the key – at a high level, the key area really is sales and marketing spend. So, you know, Jonathan in his presentation talked about the structure of the P&L and the fact that we currently spend 42% of recurring revenue on sales and marketing costs. That is – that's high, and the reason it's high is because we're investing up front to create the momentum, particularly around new customer acquisition, and also as we shift to a more digital model, you know, we have a number of inefficiencies because we are running, you know, duplicate sales and marketing processes. So, as the growth comes and accelerates, and as we make that go to market, that sales and marketing more efficient, you will naturally see the amount that we're spending as a percentage of recurring revenue come down. It won't come down in absolute terms, but it will not need to grow at the same rate as revenue. Jonathan, anything you want to add?

Jonathan Howell: No, sorry, Steve said it all and nothing really to add. But look, when we get to the year-end, you know, we'll be up – you know, updating on our investment plans and how that can further drive growth and where we're allocating that additional investment as well.

Ross Jobber: That's useful, thank you.

Steve Hare: Right. Well, thanks very much everyone. Really appreciate, as always, everyone taking time to dial in and spend some time with us, and we'll looking forward to updating you at the end of the third quarter. Thanks very much.

[END OF TRANSCRIPT]