Sage Group Plc H1 2022 Results

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Overview

Steve Hare

CEO, Sage Group plc

Delivering a faster-growing business

Good morning, and a warm welcome to Sage's 2022 First Half Results Presentation. I'm going to start with an overview of our key messages for today.

Firstly, our performance. Sage delivered strong results in the first half, and our growth is accelerating. Recurring revenue increased by 8% and annualised recurring revenue by 10%. Cloud-native ARR continued to grow strongly at over 40%, and now represents around a quarter of the Group total. And our margin increased in line with expectations, as our growth drives operating efficiencies.

Moving to opportunity. Sage has a strong position in a robust growing market. Our solutions are critical for enabling efficiency and resilience in millions of small and mid-sized businesses around the world. And despite the uncertain geopolitical and economic outlook, SMBs continue to invest more in digital technology as they look to automate processes, gain better business insights and comply with regulation. And Sage's trusted solutions across finance, HR and payroll position us well to support them.

And finally, we continue to execute in line with our strategy. Our investment in sales, marketing and innovation is paying off, as we rapidly grow Sage Business Cloud revenues up more than 20% in the first half. We're delivering against our strategic priorities with good progress in all areas. And having recently completed our disposal programme, we're now focused on growing revenue and earnings in absolute terms.

Now I'll come back to talk about our progress later in the presentation. But for now, I'm going to hand over to Jonathan for the financial review.

Financial Review and Outlook

Jonathan Howell

CFO, Sage Group plc

H1 '22 Financial Highlights

Thanks, Steve, and good morning, everyone. I'm pleased to share with you today our interim results. In summary, we've executed well in the first half and made good strategic progress.

So, starting with the financial highlights. It's been another strong period for Sage with continuing investment driving faster growth and margin expansion in line with our plans.

Firstly, we've delivered recurring revenue growth of just over 8%, which is in line with our guidance for the full year. This was driven by strong levels of new customer acquisition across Sage Business Cloud, with particular strength in cloud native.

Secondly, operating margin was 19.9%, and is trending up from last year-end, following a period of additional investments.

And finally, cash conversion has remained strong at 120%. This reflects continued growth in subscription revenue and good working capital management.

Growth drivers

Adding some colour to our growth drivers gives us a sense of the strategic progress we continue to deliver. We achieved strong ARR growth of 10%, up from 4% last year, reflecting the accelerating momentum from Sage Business Cloud. In addition, as Steve said, we saw particularly strong cloud-native ARR growth of 43%, up from 35% last year. Renewal rate by value was 100%, up from 97% last year, with improved churn rates and targeted price rises.

Cross-sell and upsell also increased, supported by a good performance in customer add-ons. Sage added £150 million of ARR from new customers over the last year. This was up from £110 million in the previous year, and demonstrates that our growth continues to be well balanced between existing and new customers. And this success creates strong momentum as we go into the second half.

P&L summary

Turning now to the P&L. Total revenue growth was just over 5% for the year, driven by recurring revenue growth of 8% to £866 million. Organic operating profit increased by 4% to £184 million at a margin of 19.9%, whilst underlying operating profit reduced by 3% to £183 million, reflecting the impact of disposals in FY21.

Underlying EPS grew by 6% to 12.62p. This reflects a good performance in the business and the impact of the share buyback programme. The interim dividend of 6.3p is up 4%. And with a progressive policy going forward, we intend to grow the dividend over time.

Revenue bridge

Let’s now look at the performance in more detail, starting with the drivers of revenue growth. Our focus remains on growing Sage Business Cloud. And in line with this, we achieved growth of some £101 million or 21%. Both cloud native and cloud connected have delivered a strong performance, growing by £57 million and £44 million, respectively. Importantly, a large proportion of this growth has been driven by significant levels of new customer acquisition.

Migrations also continue to drive growth, mainly in our cloud connected solutions. Accordingly, revenue to be migrated decreased by £24 million. The impact of all this is Sage Business Cloud penetration, which is now 72%. This is up from 65% last year with an increasing number of customers participating in Sage’s digital network.

Revenue categories

Turning to the revenue categories. As you can see, subscription penetration has continued to trend upwards, reaching 74%. This is up from 68% last year. Growth in recurring revenue of 8% was driven by 14% growth in software subscription to £682 million. And as expected, other recurring revenue and non-recurring revenue continued to decline by 8% and 24%, respectively. This demonstrates the improved quality in our revenue base.

Portfolio view of recurring revenue

Looking at the portfolio view of revenue. The future Sage Business Cloud opportunity continues to show a strong performance, with recurring revenue growth of 11%. And as I mentioned, Sage Business Cloud penetration is now at 72%. As you can see, the pace of growth in both cloud native and cloud connected is significantly ahead of the Group as a whole.

Recurring growth of 44% in cloud native to £187 million is driven by new customers and migrations. Cloud connected revenue has grown by 13% to £385 million, which is underpinned by a good performance in the international region. And recurring revenue in the non-Sage Business Cloud portfolio decreased by 14% to £69 million, in line with our strategy.

North America

We've seen growth accelerate during the year across all our regions. In our largest region, North America, we delivered recurring growth of 12%, again, driven by strong performance in the medium segment. Sage Intacct continues to be the standout performer, growing recurring revenue at 31%. This is driven by record levels of new customer acquisition, demonstrating strong win rates against our competitors in the market.

In addition, the Sage 200 franchise continues to contribute to overall growth. And the impact of all this is Sage Business Cloud penetration of 75%, up from 73% in the prior year.

Northern Europe

Northern Europe had recurring revenue growth of 7%. Growth in cloud native products was driven by new customer wins in Sage Accounting, Sage Intacct and Sage People. This is supported by continued growth in Sage 50. Sage Business Cloud penetration is now at 89%, up from 85% last year, reflecting the high levels of cloud adoption in the region.

International

And finally, the International region, which delivered recurring revenue growth of 5%. This was underpinned by strong growth in Sage Business Cloud penetration, now at 56% compared to 43% last year. Growth in France and Germany was driven by a good performance across the Sage Business Cloud. And Africa and APAC delivered strong recurring revenue growth of 7%, with momentum building through Sage Accounting in particular.

Investment driving growth and margin

In order to accelerate growth, we've continued to invest in the business during the first half. However, we now expect the level of spend to increase at a slower rate than revenue. And as a result, margin is expected to trend upwards in FY22 and beyond. You can see this already in the first half, with margin progressing from 18.4% and ARR growth accelerating. Our investment in sales and marketing, which is now 43% recurring revenue is focused on driving new customer acquisition across our business. And we continue to invest strongly in product and development, which remains at 16% of recurring revenue.

We've maintained a disciplined approach to investment. Accordingly, G&A spend is around 10% of recurring revenue, demonstrating our commitment to efficient growth.

Strong cash generation

Turning now to the cash flow. Cash generation remains a core strength of the business. The Group generated £220 million of cash from underlying operations, resulting in strong cash conversion of 120%. Importantly, cash conversion has now been over 100% for more than three years, and free cash flow is £167 million, which is net of interest and tax.

Robust financial position

This in turn has resulted in a strong balance sheet, underpinned by cash and available liquidity and of £1.2 billion. During the period, we completed the acquisition of Brightpearl for £225 million. And we've disposed of Sage Switzerland and the payroll outsourcing business in South Africa. This now completes the disposal programme.

Since March of last year, we've returned £600 million through share buybacks, which concluded in January. Leverage is 1.5 times net debt to EBITDA, which is in the middle of our mid-term target range of 1 to 2 times. However, we retain the flexibility to move outside this range, as business needs require.

Going forward, Sage will adopt a progressive dividend policy, intending to grow the dividend over time. Importantly, we retained significant capacity to support both organic and inorganic growth.

Full year outlook

Turning now to the outlook for the Group, which remains unchanged. We expect organic recurring revenue growth in the region of 8-9% in FY22, driven by continuing strength in Sage Business Cloud.

We also expect other revenue to continue to decline in line with our strategy. And we expect organic operating margin to trend upwards in FY22 and beyond as we focus on scaling the Group. Thank you. I'll now hand back to Steve.

Strategic Update

Steve Hare

CEO, Sage Group plc

Strategic framework for growth

Thanks, Jonathan. Now, as I said earlier, our strong performance in the first half is a result of consistent strategic execution. And underlying this is our strategic framework for growth. This ensures that everything we do is aligned to drive our growth and future success. And it starts with our purpose to knock down barriers so that everyone can thrive. We do this by creating solutions that make our customers' lives easier, removing friction from their processes and delivering insights.

Our ambition expresses how we serve our purpose, and it's to be the trusted network for small and mid-sized businesses. This digital network connects our customers to the individuals and organisations they need to interact with, providing features and services that facilitate the smooth flow of work and money.

And we drive our ambition through five strategic priorities. These are the areas that have the greatest impact on our growth, and we're making good progress in all of them.

Our stakeholders are instrumental in delivering a sustainable and thriving business. And finally, our strategic framework is underpinned by our values. At Sage, we value being human and bold and creating trust and simplicity for all of our stakeholders. And above all, we value doing the right thing.

Delivering on our stakeholder promises

Now Sage's success depends on our ability to engage effectively and work constructively with all of our stakeholders. And this engagement is underpinned by our stakeholder promises. For our customers, we seek to knock down the barriers to their success, building every experience with human insight and ingenuity.

Now when I speak to customers and partners from sole traders to the CFOs of larger businesses, they all say they're looking to digitise faster. And what they love about Sage is that we combine our solutions with a human touch, championing their interests, providing business advice and always with experts on hand to help them.

For colleagues, knocking down barriers means committing to our people, encouraging a culture of innovation and energising everyone to make a difference. We do this by focusing on development, training, inclusion and wellbeing. I'm really loving seeing colleagues in person again, but also seeing them experiment with their teams about how they can be most productive through our flexible working model.

And we also continue to be recognised as a great place to work, winning awards, including for Best Global Culture and for being one of Glassdoor's Best Places to Work.

On society, we aim to use our time, technology and experience to tackle digital and economic inequality in the climate crisis. We're on track to support more than 5,000 peoples across the Northeast of England this year with STEM skills training. And through our partners, Kiva and the BOSS Network, we've enabled thousands of loans and grants to support small businesses worldwide.

I particularly enjoyed spending some time with Cameka Smith of the BOSS Network on a recent visit to Atlanta. What we are doing together to support black female entrepreneurs is making a real difference to people's lives. And on climate, we've pledged net zero emissions by 2040, halving them by 2030, and we're on track to submit our science-based targets for validation later this year.

And of course, for shareholders, our overriding objective is to create sustainable growth in shareholder value, and we will do this by growing revenue and doing so more efficiently over time.

Focusing on our customers

So, turning to focus on our customers, where the breadth of our business gives us really good visibility into SMB trends. And today, I'm going to highlight three key insights.

Firstly, having proved highly adaptable and resilience over the last couple of years, the majority of SMBs are confident in the future success of their business, but they continue to face barriers. And they tell us that increasing cost pressures and labour shortages are their biggest obstacles.

But against this backdrop, over 90% of SMBs say technology is key to their growth and resilience. And accounting and HR software are among the top areas where they're looking to invest. This investment brings efficiencies and productivity gains that help mitigate inflationary pressures and ensure SMBs are better equipped for the future. All of this means the opportunity for Sage is increasing. Our software saves customers' time and money, making accounting and HR processes more efficient through automation and providing better business insights that support growth.

And as Jonathan said, we've been investing across our business to enhance the opportunity for Sage, expanding sales and marketing to drive and convert more new business leads and accelerating innovation to deliver better customer experiences.

Refreshing our brand

Now part of our investment has been in refreshing our brand. Launched globally over the last couple of weeks, the updated brand focuses on the simplicity and confidence that Sage delivers to customers, highlighting how our solutions help customers make better, faster decisions backed by expert human advice and insights.

Now to bring the look and feel of the new brand to life, we're going to play you a short video.

[Video]

Now to bring this to life across our markets, we've kicked off a new advertising campaign to enhance the way we engage with and serve our customers. We're introducing Sage Membership, where every Sage customer has access to exclusive benefits, including talks and articles from the world's leading business experts, and we'll continue to invest in communities.

So, for example, staying true to our roots in the Northeast of England, we'll bring our brand and values to life by supporting the development of a community-focused business and entertainment venue in Newcastle. Called The Sage, this venue is expected to provide a £70 million annual boost to the local economy and create 2,000 jobs.

And through these and other initiatives, we'll drive deeper and broader customer engagement and encourage new audiences to consider Sage solutions.

Scale Sage Intacct

So, let's now turn to our strategic priorities, starting with scaling Sage Intacct. Our focus here is on accelerating Sage Intacct's expansion into both existing and new markets. And we've made strong progress in the first half, launching more features, providing customers with improved AI capabilities and expanding sales and marketing.

Now as a result, momentum continues to grow, with a record number of new customer additions during the first half. ARR in the US is up by a third year-on-year. And outside the US, where Sage Intacct was more recently launched, it's more than tripled to £12 million. We've also taken significant steps to expand Sage Intacct's vertical reach.

The acquisition of Brightpearl provides retail and e-commerce customers with a highly configurable SaaS-based retail operating system, helping them to grow their business. And the launch of Sage Intacct manufacturing in France offers an intelligent production management solution, leveraging our deep domain expertise from Sage X3.

Looking ahead, we're also focused on driving earlier adoption of Sage Intacct, reducing upfront costs for customers and accelerating time to value, streamlining the customer journey.

Expand medium beyond financials

The next priority involves broadening the value proposition for mid-sized businesses. Here, we aim to deliver benefits to customers beyond core accounting by expanding into adjacent areas in line with the enlarged remit of today's CFO, driving increased value for customers and stronger renewal rates.

In February, we launched a new service to automate accounts payable, which in most SMBs today is a manual and often paper-based process. We estimate that customers can save around 80% of their invoice processing costs as well as reducing data entry errors. And through this, we're helping CFOs elevate their focus towards higher value activities. We've also continued to develop Sage Intacct Planning, launching it outside the US for the first time, initially in Canada, but with other markets, including the UK to follow.

Build the small business engine

Our next priority is to develop a scalable digital engine to acquire and serve small business customers. And here too, we've made significant progress. By investing in digital marketing and the customer experience, Sage has grown its UK cloud-native ARR from small business solutions by over 50% in the last year.

And in November, we launched Sage for Accountants, our new cloud-native practice management software, complemented by our recent GoProposal acquisition. And so far, it's beating expectations, having attracted more than 1,000 new practices since launch and serving as a key advocacy tool for Sage.

And we've just further enhanced the proposition by acquiring Futrli, a live forecasting tool for accountants and their clients.

Beyond the UK, we're also rolling out the small business approach in the markets, initially, South Africa and Canada.

Scale the network

Now I mentioned earlier, our ambition is to be the trusted network for SMBs. We'll achieve this by scaling and developing our digital network and continually making the experience richer for our customers. This creates a strategic flywheel effect with more customers leading to more network activity and more data, which, in turn, powers the insights that we need to develop more compelling AI-driven features leading to better customer experiences.

Now scale is key. And by rapidly growing Sage Business Cloud, we're enabling more network participation. We've launched new cloud native solutions in International, including Sage Accounting in Spain, Sage HR in Germany and Sage Intacct Manufacturing in France. And we're investing in our network powered services. For example, connecting customers to more than 11,000 financial institutions worldwide to enable automated bank reconciliations or developing the first real-time AI-driven outlier detection engine for a general ledger, now adding value to customers of Sage Intacct as part of its core functionality.

And we're continuing to expand our ecosystem of software partners and ISVs, extending the reach of our solutions and helping to grow the network.

Learn and disrupt

Turning to our final strategic priority, learn and disrupt, which focuses on continuous innovation to underpin the long-term success of Sage. We continue to grow our team of data scientists and engineers within Sage AI Labs, supporting the development of new network powered services.

We've also progressed our external partnerships to accelerate innovation. For example, with Experian for wage verification and with Tide to launch a combined banking and accounting app. And we will continue to invest in our innovation capability so that we can create, learn from, and participate in future disruptive trends.

Key messages

So, in conclusion, Sage has performed strongly in the first half of the year, delivering sustainable growth and increased margins. Our market opportunity is significant and continues to grow, as small mid-sized businesses turn to digital technology to become more resilient, flexible and productive. And we are executing well with consistent delivery against our strategy.

So, we entered the second half of the year with real momentum, which continues to build across all of the right areas, giving us confidence for the future.

So that concludes today's presentation. Thank you very much. And Jonathan and I would be happy to take your questions. So, I'm now going to hand over to the operator.

Q&A

Operator: Ladies and gentlemen, we'll now begin the question-and-answer session. To ask a question, you will need to press star then one on your telephone. The first question is from the line of Adam Wood from Morgan Stanley. Please go ahead.

Adam Wood (Morgan Stanley): Hi. Good morning, and congratulations on a good first half. I've got two, if I could, please. Just first of all on the margins. There's obviously a few moving parts with a provision release in there and sequential changes. I wonder if you could just help us a little bit with how you're thinking about the seasonality of margins as we're looking into the second half and how you expect them to trend.

And maybe secondly, just on the NCA, great to see such strong additions there. Could you maybe just remind us what the mix is in there between actual new customer additions and then reactivations? How that's trended, please? Thank you.

Jonathan Howell: Good morning. Thanks very much, Adam. Yes, on margin, you can see we've reported 19.9%. That's taken the benefit of the COVID-19 bad debt provision release that we've got in the first half. And that compares – it's a nice step-up though from 18.4% in the second half of last year.

Two or three big moving blocks there in the margin. First of all, total revenue. That's up by 5% to £924 million. That's a £45 million or so uplift. Offsetting that going out of the way, sales and marketing, we've invested another £25 million in the first half in sales and marketing. Other cost lines have gone up slightly. And you take all of that together, and that gives us a 19.9% reported margin in the first half.

If you recall at the beginning of the year, we guided to the margin increasing in FY22 and beyond. That's exactly what we are seeing. And as we sit here today, analyst consensus is around 20% for the full year, and we're comfortable with that position. And so, it's going – the trend line is set for a full year exit of around 20%.

The – in terms of NCA, yes, a very good strong performance there, up £150 million in the first half in terms of NCA – in terms of ARR. In broad terms, about three quarters of that is coming from new customers and a quarter is coming from reactivations. And again, that's a step up from where we were, say, 12 months or so ago when I would probably sort of put that split at about two-thirds, one-third.

Adam Wood: That's very helpful. Thank you.

Operator: Thank you for your question. The next question is from Will Wallis from Numis. Please go ahead.

Will Wallis (Numis): Good morning. Thank you. I wanted to ask about the ARR growth. You look to have had a strong quarter, growing close to 3% sequentially. To what extent was pricing affecting that? And could you talk about how you see pricing affecting revenues and ARR going forward over the next two or three quarters? So how does that pricing flow through?

And secondly, in terms of seasonality, do you think there's any reason to expect underlying seasonality in ARR growth? In other words, are there going to be some quarters we should – we expect Q2 to be a strong quarter for ARR, typically? And finally, I suppose, just – is there anything that you see that suggests that market conditions are getting tougher just in the last few weeks or so?

Steve Hare: Thanks very much. I'll make a few comments, and then I'll hand it over to Jonathan. A couple of things. I think in terms of the kind of seasonality and underlying trends, there's really a very strong underlying trend to continue to invest in digital tools among small, mid-sized businesses. And I think there are obviously some unfavourable macroeconomic conditions. But I think despite those, I think small, mid-sized businesses will continue to invest, in many ways, actually acts as a bit of a counterbalance to inflation to invest in your own efficiency and continue to invest in digitisation.

In terms of the seasonality, not really, except that one of the things you do sometimes see when conditions get a bit more uncertain is sometimes with bigger customers, it can take a little longer to make decisions. So, CFOs sometimes take a little bit longer to decide what it is that they actually want to do.

But I think the long-term trend, the underlying trend is very clear. Digitisation is happening, and it will continue to accelerate. Jonathan?

Jonathan Howell: Yes. So, look, on ARR, yes, it's accelerating at the moment. So Q2 sequential ARR growth was 3%, Q1 was 2% and Q4 was 2% last year. That means, by definition, exiting with an ARR growth rate of 10% and recurring revenue growth rate of 8%, we will see acceleration in recurring revenue during the course of the second half.

In terms of the impact of inflation and pricing on margin, we – our pricing policy has not changed, given the context that Steve has just set out. What's it based on? First of all, it's the fair value exchange between ourselves and customers for the products and services that we're providing. Also, that's in the context of the competitive environment that we're in, in particular, products and in particular geographies. And then lastly, the assessment of any inflationary inputs into our business.

That is the mix of things that we take into account. As we sit here today, we are not seeing any acceleration in profit growth or margin expansion as a result of pricing. And that is a very consistent model that we applied, if you recall, throughout the COVID environment and pre-COVID.

And then on seasonality, just reiterate what Steve said. There's no particular trend. If you look back over the last couple of years, you see a little bit more in the autumn in Q4 and towards the end, but I wouldn't read too much into that.

Will Wallis: Sorry, can I just come back on the question on the pricing effect? I'm trying to get to the effect on revenues of the pricing increases that you've put through. So, across the portfolio, what on average is the pricing increase that's put through? And what's the timing of that coming through to revenues?

Jonathan Howell: Yes. So, if you look at the sort of the renewal rate by value, one of those components to drive that to 100% has been pricing. The pricing element that we put through during the course of the first half and intend to put through in the second half will not be matching inflation. I think it will be below inflation and margin is being achieved through efficiency, upsell and cross-sell and NCA.

Steve Hare: I would just add at the moment, just to reiterate what Jonathan said. We have not put any price increases through, which would be above the norm that we've been putting through in the past. So, I think in the first half, the impact has been in the range of what we would normally do of around 2.5% to 3% in terms of the components of revenue growth. And at this point in time, we'll have to see how it goes, but we will only put prices up if there is a fair value exchange with our customers.

Will Wallis: Clear. Thank you.

Operator: Thank you for your question. The next question is from James Goodman from Barclays. Please go ahead.

James Goodman (Barclays): Good morning. Thanks very much. I'll go for two as well, please. Firstly, just on the encouraging development in ARR in the UK native cloud segment. I think over 50% you called out. I don't think we've spoken about competition for a while there, following Xero's results recently. And clearly, they're becoming quite sizable, but at the same time, calling out actually a few challenges in the UK at the moment, I think around the channel and some of the Making Tax Digital phase two expectations not quite coming through. So just thought an opportune time for you to comment on the competitive developments that you're seeing for that product.

And then related to that, the second question just on the cloud native portfolio, and I guess, a little bit more specifically on Intacct. Just stepping back from things, I think that business was breakeven or unprofitable when you bought it. Clearly, native cloud is becoming an ever-bigger part of the portfolio. And as that happens, you're also talking about margin improvement. So, I wondered if you could just help us a little bit with how you're thinking about the profitability of the cloud native portfolio from here? Thank you.

Steve Hare: Sure. So, start with the UK. I think in terms of the competitive environment, it remains very much as it's always been. It is a competitive environment. We're focused on two things. One is – well, three things really. One is product, product enhancement.

And I think you're seeing evidence of us both organically in terms of not just our accounting offerings, but our payroll offering, our HR offering and our automation offerings through the digital network. You have seen significant enhancements to those capabilities and those solutions within the UK market.

And then from a go-to-market perspective, two focuses. One is scaling the digital engine. So you're seeing us doing more – acquiring new customers through digital channels. Obviously, the refreshed brand is part of that. So you're seeing us spending more both brand and digital marketing to raise the awareness of Sage.

And then secondly, we have a big refocus in terms of winning the hearts and minds of accountants. And I think if you think about our competitors, in many ways, the biggest competitor in the digital channel is QuickBooks, and in the accountants channel, it's Xero. We are very focused on, as I say, winning hearts and minds in the accountants channel. You've seen us do that both organically through the launch of Sage for Accountants, our Cloud practice management solution.

And you've seen us recently do two acquisitions, GoProposal, which is new business quoting software from GoProposal. And yesterday, we announced the acquisition of Futrli, which is a cash forecasting tool, again, for accountants. So, we're very committed to maintaining and winning market share within UK small. We think we're doing well, and we also think that the underlying trend is very positive. And so, we're very excited by what's going on.

In terms of the cloud native portfolio, including Intacct, again, you're seeing us expand our capabilities all the time, not just in the UK and the US, but now for the first time in Continental Europe through the launch of Sage Intacct manufacturing. We've launched Sage HR in Germany. We've launched Sage Accounting in Spain.

So, we have been investing in product development and sales and marketing over the last two or three years. We were very clear by bringing the margin down that we would invest heavily for the future, and you are now starting to see the benefits of that investment.

As far as whether Sage Intacct is profitable or otherwise, Sage Intacct is no longer a stand-alone business. It's a product. The cloud native portfolio, we don't measure or disclose the profitability of that separately. But as it becomes an increasingly large part of the portfolio, it will obviously contribute to margin. But the cycle we're in at the moment, we continue to invest significantly in our cloud native capability from a product perspective, but also from a go-to-market perspective. And I think you can see the evidence of the return in our results.

James Goodman: Understood. Thank you.

Operator: Thank you for your question. The next question is from Stacy Pollard from JP Morgan. Please go ahead.

Stacy Pollard (JP Morgan): Thank you. One of them I think you answered, but I just want to double check. My question was on, can you comment to recurring revenue growth expectations across the coming quarters? And I think as part of that ARR question. But just to confirm, you said you do expect acceleration in recurring revenues in Q3 and Q4.

And then second question is on capital allocation. The disposals and share buyback returns, I believe that's mostly done. Would you agree there? You've obviously changed your dividend policy to progressive. So that's good. Does this also mean that you're now looking to be a bit more aggressive in M&A? Of course, you did a small deal yesterday. What other areas would you look to expand? Is it sort of more tech-driven? Or would you be looking at new verticals in the US, maybe even new geographies?

Steve Hare: Yes. So, I'll take the acquisitions first, then I'll hand over to Jonathan. The priority is to continue to do the technology acquisitions. So, adding capability to the digital network so that we can offer our customers more and more solutions to help take friction out of their lives, solve their pain points.

You will also see us doing vertical – enhancing our capabilities within a vertical, which we did with Brightpearl, for example. So particularly for Intacct in that medium segment, you may see us doing things to enhance our verticals. But the priority really is to enhance our capability within the digital network. It is highly unlikely you will see us doing anything to expand geographically. Jonathan?

Jonathan Howell: Yes. So, Stacy, thanks for the question. Just by reference to an ARR exit growth rates of around 10% and the recurring revenue growth rates of 8% as we exit the first half, therefore by definition, we will be seeing acceleration in recurring revenue during the course of the second half.

In terms of sort of capital allocation, as you can see, our net debt position has gone up by about £400 million to £650 million net debt at the half year stage. That's led to an increase in leverage from about 0.6 times net debt to EBITDA at the end of last year to 1.5 now. That puts us right in the middle of our mid target range that we have, which is 1 to 2 times, which gives us flexibility, both on an organic and an inorganic basis.

The specifics that you mentioned, yes, we have ceased the disposal programme. We have made a significant acquisition of Brightpearl, £225 million, and a £250 million spend on the last element of the £600 million share buyback, which was completed during the course of the first half, and that sort of gives you the building blocks for the change in leverage.

And then lastly, just on dividend. As you can see, we put through a good strong dividend increase of 4%, that's up from 2.5% at the end of FY21 and up from 2% at the end of FY20, so a good step up there. And then in terms of the dividend policy, we have changed the dividend policy from maintenance in real terms to progressive, principally because we have now completed the disposal programme. We are focused on scaling the Group through growing revenue and profit. And therefore, it's not appropriate really to have a dividend policy linked to inflation, particularly in these challenging times for a company that is focused on growth.

So, we are moving to a progressive policy. And in short, that puts us in line with many similar companies. We intend to grow the dividend. We will make the decision at the end of each reporting period, and in the context of the performance and also our capital allocation priorities at the time. But we are very committed to the strong dividend performance for shareholders.

Stacy Pollard: Okay, great. Thank you.

Operator: Thank you for your question. We have the next question from Hannes Leitner from UBS. Please go ahead.

Hannes Leitner (UBS): The new ARR revenues of £150 million compared to £115 million at the same time last year. If we exclude that, then the cohort would have grown 8%. So, can you maybe talk about those moving parts, if pricing wasn't a moving factor? And then the second is on just those new customers. Maybe you can give us a little bit more colour. You pointed out to strong performance in the US. Maybe you can drill down there a little bit into different categories, etc.?

Jonathan Howell: Yes. So, in the ARR growth, as you say, we've reported £150 million has come from NCA, and that's up, as we said earlier, from £110 million. That's almost a 40% increase, driven by cloud native, which grew at 43%. But also we mustn't forget, we have a very strong Sage 50, Sage 200 base with very good retention rates, good renewal rates, good customer add-ons as well, and that all contributes to an overall strong growth rate.

One of the key drivers of overall growth is this step up in the renewal rate by value. We exited the end of the COVID impact on us a year ago, about a 97% renewal rate by value. That's gone up to 100-101%, which we think is the type of target we should be aiming for in order to be able to grow this business across the piece high-single digits, low-double digits.

And so that's come back into line very much more quickly than we probably anticipated, and we're now back at more or less at pre-COVID levels.

Hannes Leitner: Okay, great. And then the second question is maybe you can talk a little bit about the M&A pipeline beyond from here. I mean we know that you have done the last acquisition. So maybe you can talk there. And I saw also in terms of the contribution, it was £4 million and £2 million negative EBITDA. So how do you see that business developing in terms of breakeven and then contributing to margins?

Steve Hare: Yes. So, when we – so the acquisition pipeline, as I said earlier, will be around technology acquisitions that we can integrate into the digital network to enhance our overall offerings to our customers. So, they're likely to be technology first with probably relatively low levels of revenue because we're buying the technology really, not revenue.

And then we will also do acquisitions like Brightpearl, where we're adding to the vertical capability. And it is likely that those types of acquisitions will have more revenue at the point of acquisition.

As far as the margin is concerned, we don't buy – we don't do acquisitions to enhance margin. But what we are committed to doing is maintaining the progress of our underlying margin. So, when we do acquisitions, whether they are breakeven or slightly loss-making, we will absorb that within our underlying margin. And obviously, they will also contribute to revenue.

So, acquisitions are an integral part now of scaling Sage, and we are committed to scaling both revenue and earnings. But what we won't do is give kind of micro commentary on margin contribution of individual line – product lines because, in the end, it's all about it coming together into the digital network to offer integrated offerings to our customers.

Hannes Leitner: Great. Thank you.

Steve Hare: Thank you.

Operator: Thank you for your questions. There are no further questions. So, I hand back over the conference to Mr Hare for closing remarks. Please go ahead, sir.

Steve Hare: That's great. Thank you very much. And thank you to everybody to – in terms of attending the call today. We appreciate it. And we look forward to seeing you next time. Thank you.

[END OF TRANSCRIPT]