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

PRESENTATION

Operator

Good day, and welcome to the Sage Q3 Trading Update Conference Call. This conference is being recorded.

At this time, I’d like to turn the conference over to Steve Hare, Chief Financial Officer. Please go ahead, sir.

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Thanks very much, and welcome, everyone, to the Sage Q3 FY ’18 trading update. As always, I’ll start by making some introductory comments, and then we’ll move on to the Q&A session.

So as we’ve disclosed in the trading statement this morning, the Q3 group organic revenue increased by 6.8% in the quarter, which gives us 6.5% for the first 9 months of the year.

We were encouraged to see that the organic revenue growth has been driven by an acceleration in recurring revenue growth, with recurring revenue increasing by 6.8% in the third quarter to give 6.6% for the first 9 months of the year. This acceleration reflects the primary focus on recurring revenue that we’ve had in the business with the country managing directors now laser-focused on driving growth through subscription and the cloud as a strategic priority. Within recurring revenue, software subscription increased by 25% for the first 9 months of the year. Software and software-related services revenue increased by 7.7%.

Now if you look regionally, I’ll largely focus on our largest regions, we remain encouraged by the progress made in North America in the third quarter, reflecting strong performance across-the-board in the U.S., Canada and Sage Intacct, driving growth both through cloud connected solutions, like Sage 50cloud and Sage 200cloud, and also through cloud-native solutions like Sage Intacct and Sage People.

Within Europe, in France, we are seeing early signs of recovery with the strongest quarter since Q4 ’16. In Northern Europe, the U.K. & Ireland, performance in the quarter was broadly flat. However, leadership in the region has made good progress in laying the foundations to rebuild recurring revenue in FY ‘19. We called out in the release that in the U.K. & Ireland, we have added more cloud connected subscriptions in the third
quarter than in the first half as a whole. I also want to add that in both France and the U.K. & Ireland, we delivered an increase in sequential recurring revenue from quarter 2 to quarter 3. Other geographies are broadly where we would expect.

A quick word on group financial position, which remains strong. Net debt at the 30th of June of GBP 766 million reflects FX headwinds from the U.S. dollar, but also the dividend payout during the quarter. Net debt-to-EBITDA leverage stands at 1.5x, and you should expect this lever to trend down further in Q4. Our primary focus is driving recurring revenue, and ensuring that we carry momentum into the financial year ’19. We do remain confident of achieving our full year guidance of around 7% organic revenue growth, and around 27.5% organic operating margins. Further revenue acceleration in the fourth quarter is set to come from continued success, particularly in cloud connected solutions and the conversion of our Enterprise Management pipeline.

So I’ll wrap up there, and hand over to questions. Are we going to do questions?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We’ll go ahead with our first question from the line of Steven Goulden from Deutsche Bank.

Steven James Goulden - Deutsche Bank AG, Research Division - Research Analyst

I just wanted to hone (sic) [home] in on the guidance point for Q4. So to hit, and I know you’ve left it at around 7%. If we were to hit 7%, given you did 6.3% in the first half and just done 6.8%, you’d need to be doing about, well, roughly 8.5% in Q4 on what will be a tougher comp. You just had a 6.3% comp and you’re going into a 7% comp. But can you give us a bit more confidence around that? And on a sort of related point, SSRS was good, but a lot of that was driven by training and services. That’s obviously not really the core of what you do. How sustainable is that growth? And as that normalizes, will that have a negative impact on organic? And just the last point, last question for me, you didn’t say anything in the release about margins. Can you give us a bit of an update there? Obviously, to hit 27.5%, you probably need to be doing plus, well, north of 1 percentage point in the second half, whereas you did minus 80 bps in the first half. But can you give us any indication of where that confidence comes from?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Sure, thanks, Steve. So to start with the guidance, absolutely spot on. We need to be over 8% in Q4 to hit the guidance. As I indicated, it will come from 2 sources. We will continue to see an increased momentum on recurring revenue. I said at the first half, whilst we don’t officially guide around recurring revenue, we expected that for the full year, we’d be somewhere around the 7% mark. So with this acceleration in Q3, the recurring’s now cumulatively at 6.6%. So I’m expecting that we’ll see some strength and acceleration there. On the SSRS, to date, the – it has been driven, and this is true in Q3 as well, by services, and there’s 2 principal sources of that now. One is the add-on services with Enterprise Management, and the other is we have had some boost, particularly in Continental Europe, around training to support GDPR. In Q4, the SSRS growth is driven principally by Enterprise Management and add-on services, and actually, in Q4, probably more Enterprise Management license than service, but it is both. And the reason for that is, again, if we go back to the first half, I said that we’d had some slippage in Enterprise Management. We didn’t think we’d lost any market share or lost any opportunities. But we had seen slippage, particularly in Africa, Middle East, and to some degree, in the U.S. I also indicated that we’d bolstered in both cases the Enterprise Management teams. And also, we were increasing the focus to make sure that people were using the CRM system, so that we could get better visibility and better discipline around opportunity conversion. What we’re starting to see is the benefits of that. So we have -- we’re going into Q4 on Enterprise Management with strong pipeline cover. So obviously, those opportunities have to be converted. So you still have to convert them. It’s not a slam dunk, so to speak. But we have much better visibility going into Q4 than we did at Q2, and indeed the beginning of Q3. So I think -- and in terms of the sustainability, the focus, as I’ve said, is absolutely on driving recurring revenue. Now from a strategic perspective, we still sell Enterprise Management on license. In some jurisdictions, we do also sell it on subscription, but it is predominantly license because it’s on-premise. But it is our intention that more of the mix, more of the growth in FY ’19 will come from recurring revenue. And it -- the momentum that we have we’re encouraged by, but obviously the way the maths works is, as we’re signing customers
on a 12-month recurring revenue contract, we're only rev rec-ing on a monthly basis. So the fact that both the U.K. and France have shown sequential recurring revenue growth, which is the first time this year, I think is very encouraging. Margin, we don't disclose in the trading updates. But again, your analysis is obviously correct. We're not in a dissimilar position to where we were last year, and we always front-load the investments. And all I can say is I have good visibility on the path to margin. So I think it follows if we hit the revenue, we'll hit the margin.

Operator
We'll move on to our next question from the line of Charlie Brennan from Crédit Suisse.

Charles Brennan - Crédit Suisse AG, Research Division - Research Analyst
Great. Just a couple, if I can. It's very nice to see the growth in the ARR in the Sage Business Cloud. Can you give us some indication of how much of that growth has come from the existing Sage base and how much of that has come from new customers? And secondly, just a clarification on this fourth quarter guidance point. You were cautioning about the speed at which you can recognize recurring revenues. Is it practically possible to get a percentage point acceleration in Q4 in recurring revenues? Or arithmetically, is that just challenging?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director
Yes, so if we take the business cloud first, so on -- I should just actually say on the Sage Business Cloud numbers that we quote, we're quoting ARR, and we quote absolute amounts, which means that they are subject to exchange rate differences, because obviously, a significant amount of our Sage Business Cloud revenues in the U.S. in the dollar to sterling exchange rate has been volatile. So the first thing to say is that about roughly on a constant exchange rate basis, we've added -- we're adding about 40 million a quarter of ARR on Sage Business Cloud. And of that 40 million, Q2 to Q3, about 30 million of it was cloud connected. So it's Sage 50 and Sage 200 migrations. The remainder, the remaining 10 million is the native cloud increases. And whilst that's not 100% new customer acquisition, because obviously, Sage Intacct and Sage People have some degree of add-ons with their existing customers, and that is -- that's the main adding of new customers because we're obviously leading with cloud native. The other thing I would say is that on Enterprise Management, just to emphasize, we only include Enterprise Management in Sage Business Cloud if it's the cloud version. So the vast majority of the Enterprise Management revenue is not in Sage Business Cloud because it's still on-premise. And likewise, Enterprise Management is obviously a primary new customer acquisition tool. And as I said earlier, we continue to see -- we see continuously good traction on that. Now on your question on recurring revenue, is it possible to increase the growth rate in the quarter, i.e., could we go from 6.8% in Q3 to say, 7.8% in Q4? That is arithmetically possible. It's a bit stretching, but it's arithmetically possible. What is not arithmetically possible is to go from a cumulative 6.6% to a cumulative 7.6%. That would require a level of acceleration which is not possible. And maybe just a quick insight into sort of partly why. What we're doing with particularly Sage 50 customers is we're contacting them in advance of their renewal date. So if your renewal date is, say, the end of July, we would call you in the middle of June, and we would seek to reach agreement with you that we're going to migrate you to subscription in the cloud connected version. So we may well book that opportunity, but from a rev rec point of view, we won't recognize that as a migration until the 1st of August when we migrate that customer. So we are not early migrating. We're letting customers finish their contracts, whatever kind of current contract they're on, and then we are activating them onto their new contract. So I have -- what that does is it means I have pretty good visibility of the momentum in some of the bookings that we already have on cloud connected in both the U.S. and the U.K. But obviously, it means that there is a limit to how much we can get rev rec-ed. But I can tell you that the -- both the ARR and the annualized -- the growth in annualized subscription is both -- both of those measures are running ahead of the actual number that we're quoting. So our ARR growth is higher than 6.8%. In other words, the run rate's higher.

Charles Brennan - Crédit Suisse AG, Research Division - Research Analyst
Okay, great. And just one last question, actually. The acceleration in training in Q3 or the growth in training, is that a lagged effect from this mechanism to swap out maintenance for training that you stopped in the first half of the year? Or is that genuinely new training during the quarter?
Stephen Hare - The Sage Group plc - Group CFO & Executive Director

So I can say, categorically, there is no service boost revenue that we -- of the start we talked about in the first half. That is being stopped. The sort of spike in training that we've had in Q3 is to do with GDPR, which is obviously not sustainable. This is a boost that we'll also see in Q4, and the rest of the service is straight training is [attached] to largely Enterprise Management. So we're not doing any of the service booster. What the service booster does do though, just as a reminder, is it obviously affects the comparator, which is why I'm also emphasizing the Q2 to Q3 sequential because that's what's important now. What's important is that the monthly recurring revenue sequentially is increasing, and that we're topping up the recurring revenue pool of -- the pool. So we are adding more than we're losing in attrition.

Operator

We'll move on to our next question from the line of Mohammed Moawalla with Goldman Sachs.

Mohammed Essaji Moawalla - Goldman Sachs Group Inc., Research Division - Equity Analyst

I was wondering if you could perhaps put some numbers or quantify the strength in North America. I didn't see any numbers in the release. And then secondly, as we think about some of that you referred to just as slipped business, and I think it was mostly kind of licenses. Would that -- if that sort of closes in the second half, I know you still have to close those deals. Would that be meaningful in terms of sort of a tailwind to the growth rates for Q4 in the second half?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Yes. So on North America, you're right, we didn't split it out. We just talked about it in total. The way to think about it is that the cloud connected migration has continued at the same sort of pace. So when I was quoting the growth in Sage Business Cloud ARR, that's obviously heavily underpinned by the performance in the U.S. Your point on license is absolutely right. We had some -- we did have some catch-up of the slippage in Q3. But if you sort of think about the maths that I was referring to earlier, if we need to hit sort of overall about 8%, so just over 8% in Q4, SSRS is going to have to grow at a similar level to that, which it has in the last couple of quarters, i.e., it's probably going to have to grow at 8 percent-ish. And that is helped by what we expect to see as a bit of a tailwind on the Enterprise Management licenses catching up. Now as I say, going into Q4, we have a stronger pipeline cover than we've had in previous quarters, but obviously, we need to convert. But if we miss the number, it won't be because we didn't have the opportunities. It will be because we didn't convert. But the good news is that, as I said, we have absolute sort of adherence to using the CRM systems. So we know what the opportunities are that we need to convert, and we just need to convert them and make sure that we also execute on any associated services and training.

Operator

Next question comes from the line of James Goodman with Barclays.

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

Steve, you say good visibility on the path to margin. I was wondering if you could give us some more detail, specifically on what OpEx you're going to be taking out in the second half. Because Sage is not a particularly seasonal business. I know we had this seasonality in the business for the last couple of years. But could you remind us, is that primarily digital marketing spend? Or what that OpEx takeout is and is there a tradeoff there in terms of the run rate of growth into FY '19? And then secondly, could you clarify -- you talk about the U.K. success that the management have had in setting up that business. Is the management situation now permanent in the U.K.? Or do we still have some sort of management positions to fill there?
Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Yes, so on margin, a couple of things. We typically front-load marketing. So we tend to -- I mean, in the past, we've had events like Sage Summit, which we've now replaced with what we call Sage Sessions. But we've done a lot more of those in the first half than we do in the second half. So the marketing tends to be very front-loaded. We have, during the course of the first half, been doing some slowing of recruiting. We have natural attrition, so that tends to run typically anywhere between sort of 12%, 15%, so -- which is pretty similar to most software companies. And during the course of the first half, we have been doing some sort of thinning out of -- or flattening of the organizational structure. So we've been hiring less people than we've been losing. So we're carrying a lower run rate into the second half anyway. And I think I've touched on this before, that also, obviously following the reduction in guidance at the half year, we're obviously now at the lower end of the revenue range compared to what we would have expected at the beginning of the year. So by definition, bonus payouts are also lower. So if you take all those things together, we have a very clear visibility of our current run rate. And as I say, if they hit the revenue, we'll hit the margin. In terms of the U.K., we announced recently, I think in the last few weeks that we've now appointed the sort of permanent head of the U.K. business. Sabby Gill, who's come -- who has joined us from Epicor. The person who was doing it on an interim basis, Lee Perkins, was always going to do it on an interim basis, and it is intended. Lee's part of the management team. So he will be doing another role, but the -- yes, the U.K. leadership team is now stable. And we already had changed a number of the sort of next levels down. I think I referred last time to, we've had in place now for some time a head of U.K. sales. So we have much greater stability, and I think that's reflected in the performance.

Operator

(Operator Instructions) We'll move on to our next question from the line of Stacy Pollard with JPMorgan.

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

Just going to the U.K. again, do you think the cloud subscriptions that you have done in that region are enough to push growth to the 7% range for the region, let's say, as early as Q4 or H1 2019? Or will that take a little bit longer? And then maybe second quick question would be on the mid-term. What growth rate do you need to achieve, do you think, to start getting more leverage in the operating margins, so beyond the current guidance for 2018?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Yes, so I think in the U.K., as I said earlier, we have good momentum. We still have plenty of runway in terms of penetration. I mean, we're not halfway through the conversion of our Sage 50 base. The other -- we're starting to see some early -- and this is early so I don't want to be too optimistic, but we are starting to see some early success in terms of reactivations. As we've always said in the U.K., like the U.S., we have an on-plan maintenance and support base that we're, over time, converting to subscription. But the U.K. also has a very large number of Sage 50 customers who are off-plan, and so we have been trying to reach out to those customers and encourage them to come back on-plan. Now one of the ways that we do that is that to be -- to have features like Making Tax Digital, you need to be on-plan. So if you're off-plan on an old version, you don't have the Making Tax Digital functionality, and that's starting to have some impact. So we've started to see some -- we are seeing some acceleration of those reactivations, but it is early days. And those customers, as I've said before, are a little harder to contact, obviously, than the ones that are on-plan. So I absolutely can see in the U.K. for cloud connected, the appropriate momentum to drive growth in the same way that we have in the U.S. And I think if you sort of ignore the comparator, because as I explained at the first half, the service booster has distorted the comparator, we can see that recurring revenue in the U.K. sequentially will continue to increase quarter-on-quarter. So once we get into -- well into FY ’19 and the sort of distortion of the comparator disappears, there's no reason why the U.K. shouldn't be growing in the same sort of way that the U.S. is. I should also add, I haven't said very much about Continental Europe, but we are starting to see the same strategy working in Continental Europe. The cloud connected strategy is now getting a lot of momentum in France, and we're starting to see some early momentum also in Iberia. So I think, overall, cautious optimism. As far as the gearing is concerned, the operational gearing, look, we've sort of said what we think, where we are now, what we think the mid-term outlook looks like. As I've always said, the big sort of choice here is that, particularly, when it comes to driving new customer acquisition, it's just how much you spend on sales and marketing, particularly as you're driving behind the recurring revenue model. So as I've repeatedly said, if we can deploy money effectively to drive growth, that's what we should do. If we can't, we should increase the margin. But the
thesis at the moment is that the focus is on reaccelerating recurring revenue growth, and that's what we're doing. Okay, thanks, Stacy. Any more questions?

Operator
Yes, we'll move on to our next question from the line of Michael Briest with UBS.

Michael Briest - UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research
A couple for me. Just going back to the original question about the sort of cadence of growth you have to get to hit the 7%. Are you targeting then over 8%, and specifically, a 7.0% growth for the year? Because I guess around 7% could mean anything as little as 6.5%. Are you actually expecting to do over 8% in Q4?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director
So I think, obviously, the guidance is around, and that's what it means. I don't think 6.5% is around. So -- but as I've said before, we're driving a recurring revenue model, and the numbers are tiny. So if we're at 6.8%, 6.9%, and recurring revenue is strong, I'll be perfectly happy with that. This is -- it's not about whether it's exactly 7%. But we are targeting, as I've said, to get over 8% in Q4, so that we're around 7%. And that will require us to show both further acceleration on recurring revenue, and it will require us to convert this Enterprise Management pipeline and deliver SSRS growth in a similar region. So the SSRS growth in Q4 is going to need to be around 8% to deliver on the guidance.

Michael Briest - UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research
And just in terms of SSRS, if I go back last year, it shrank, albeit in Q4, it looks like it was growing in the mid-term. So the guidance would imply, as you shifted the cloud and subscription, that it should decline. But [seeing has obviously] been very strong. And you said in Q3, licenses were down. Can you talk about X3? And Q4 last year, I think, was very strong for X3 -- oh sorry, and Sage Enterprise. What sort of confidence you have in the ability to close those deals and get to the 8% growth?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director
Yes, yes, and you're right. Some of this is captured. It's because, relatively speaking, in Q2, the license growth was a bit weak because we had slippage. Some of that's being recovered into Q3, but we are carrying a decent sized pipeline coverage for license into Q4, which gives us confidence, I wouldn't call it converted, but we have the visibility and we know what we need to do. Now, long-term, as I say, it is on strategy to sell Enterprise Management on perpetual license as long as it's on-premise. Now it is our intention over time to convert Enterprise Management to subscription as well. But -- and we obviously already sell the cloud version. We're introducing hosted versions. But in a number of territories, I mean, take the U.S. as an example, customers are extremely reluctant to pay subscription for an on-premise product. If it was cloud and it was hosted, that's fine, but on-premise, there's a lot of resistance. So we are driving what is a strategic product, selling it in the way that we've agreed, perpetual license. But the important thing is for the rest of the business, where we have decided to switch to subscription and drive subscription, that is what the countries are doing. We are not switch-selling to make the numbers. The recurring revenue focus is absolutely our primary focus. We need to rebuild and accelerate the growth in recurring.

Michael Briest - UBS Investment Bank, Research Division - MD of Global Technology Research Group & Head of the European Technology Research
Okay. And just on Intacct, can you talk about the internationalization there? Is that available now in any other countries besides the U.S?
Stephen Hare - The Sage Group plc - Group CFO & Executive Director

No, it’s not. We’re working on it, and we’ll probably say more at the year-end results. But it’s not available yet, but it is in the pipeline.

Operator

Next question comes from the line of Will Wallis with Numis.

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

Can we dig back into that [cal kinetic] growth that you were sort of characterizing as being around about GBP 30 million per quarter -- on a constant-currency basis? How much of that is revenue growth? And how much is that -- of that is just transferring from other forms of revenue?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Yes, so there is -- you're absolutely right. There's a mixture because this is largely migration. So there is some new customer acquisition on both Sage 50 and the Sage 300 family, but it's relatively small in comparison to the migration. So -- and most of this is the U.S. -- well, it's North America, U.S., Canada and the U.K. And typically, just as an average, we are migrating customers from maintenance and support to subscription. That's about a 20% premium. Now there is, as I said earlier, there is also a slight boost from reactivations because, particularly in the U.K., we have a number of customers who are not on plan. And so if we reactivate them, obviously, we're getting the benefit of the full reactivation in our growth. But the way to think about it is that the sort of true uplift in overall revenue is this 20% on migration. Otherwise, what we're doing is we're substituting M&S for subscription.

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

Okay. Can I ask a couple of clarification questions? Firstly, in the release, you give a SSRS growth number of 7.7%. It's a small effect, but is that for the quarter or is that year-to-date?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Let me just -- no, no, that's year-to-date. That's for the 9 months, yes.

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

Okay. And on the GDPR effects, training effect, are we going to find in a year's time that, that was actually quite significant? Can you give us any idea of the scale of the GDPR training effect in the quarter just gone?

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

Yes. It's not hugely significant for the group. It is significant for the countries, particularly for Iberia. I mean, I think we've called out in the release, but I'm not sure we have called out in the release, actually. But the -- in Europe, Iberia is one of the countries that has grown double-digit, and that has been boosted by GDPR. So we're talking about sort of low millions of impact. So from a group perspective, it's not hugely material, but it's helpful.
Two questions for me, please, if you wouldn’t mind. So first off, any clarity on the weakness in the U.S. on the Enterprise product area, to what extent might that be a competitive issue? And then secondly, in terms of the ARR on the cloud products, the sort of, the balance seems to have changed there in terms of the mix of ARR from the cloud enabled and the native cloud. I’m just wondering, is there an issue on churn rates, not so much on Intacct and People, but on the rest of the cloud native products?

Sure. So Enterprise Management in the U.S., I think I’d probably just repeat the comments that I’ve made more widely, which is that, in the U.S., we have good visibility. We started to convert more of the opportunities, but there’s still plenty to do in Q4. So the level of license revenue is expected to pick up in Q4. So it’s the same comment, good visibility but work to do to ensure it happens. On the ARR, the -- I think what we’re seeing here is there’s no slowing of the native cloud growth. If you take native cloud as a whole, it’s sort of growing in the -- it depends on the quarter, but sort of 30% to 40%. But the cloud connected is growing faster, and it’s quite a big number. So if you go back to what we disclosed at the year-end -- sorry, at the half, where we gave the breakdown, we had about 330, 336 million, I think, of ARR. And over 2/3 of that is cloud connected, and the cloud connected is growing at 70%-plus. So what’s happening at the moment is, yes, cloud connected is showing bigger growth numbers than the native cloud. Now obviously, this is getting boosted because in the short term, we’re driving this migration of our existing customers, whereas, for cloud native, it’s more new customer acquisition. So it’s not surprising that the migration is going faster than the new customer acquisition. But there’s nothing unusual in terms of the churn on the cloud native.

Yes, so I think it -- I’m sort of -- I’m being cautious because I’ve said in the past, with off-plan customers, it’s harder to get in touch with them, and they fall into different categories. We have some customers who are off-plan, but actually, they’re still connected. They -- the product still sort of pings, if you like. So we know that they’re using the product and we’re still -- because those customers have opted in, we can still contact them. But then there are a lot of customers who -- you can’t just cold call people. And so what we’re starting to see some early signs of success with, is going through the accountants channel and working with accountants who have clients who are off-plan and working with the accountants to reactivate them. So look, the -- obviously, the cost of reactivating a customer is higher than the cost of migrating a customer because it takes more effort to find them. But what we’re finding now is where we can engage in a conversation with the customers we’re starting to get some good success of bringing them back on plan. Making Tax Digital is clearly a key driver of that. So people, once they realize that they need to be on the latest version and be on plan to do that, for many, that is a compelling argument. And there’s also, I think, an increasing sentiment that you should
keep yourself up to date, be on the latest version, make sure you're GDPR-compliant, all of these things, right? So I think there's starting to be a greater momentum of people feeling that they should upgrade and they should be on the latest versions, but it's early days. And so I don't want to get carried away, but there are certainly some encouraging signs.

Vijay Anand Chandrasekaran - Jefferies LLC, Research Division - Equity Analyst

Great. And I had a quick follow-up question on the Q4 recurring revenue growth acceleration, or the expectation of an acceleration. And in particular, subscription revenues, because I think the Q3 growth was very similar to what you saw in the first half, and you mentioned that the ASP growth is running ahead of the underlying revenue growth. I think the first half, the ASP growth was 30%, which is, I suppose, a reflection of the new subscription contracts that you signed in March. Can you say the ASP run rate running ahead of the 25% subscription revenue growth, does that just reflect the last month of the quarter? Or did you see the margin performance carry on through all the 3 quarters? Because I suppose if it was all the 3 quarters, that's probably -- that would give us more confidence on the Q4 recurring revenue [could be some] acceleration.

Stephen Hare - The Sage Group plc - Group CFO & Executive Director

No, we've seen it consistently. I think one of the things that distorts the subscription growth a little bit is that what's happening within that category is, in some countries, particularly, actually, in the U.K. and in France, we did historically sell on-premise. Some of our on-premise customers are on subscription. So particularly, in France, Sage 100 customers, we migrated a lot of them to subscription, but it was still an on-premise product, and we put time keys in, so that they required annual renewal. And so what you're seeing now is we are migrating those customers to cloud connected. But obviously, the only thing you see in subscription growth is the premium that we charge them, whereas if we switch an M&S customer to subscription, you obviously get all of that in the subscription growth. So that is to some degree acting as a bit of a dampening effect on the headline subscription growth. But it's obviously a good thing that we are also getting those customers onto the latest cloud versions. So I'm -- to summarize and sort of nail that question, I think -- I mean, we are in a position now, particularly in Q3, where on recurring revenue and run rate of subscription, we're seeing progress on a monthly recurring revenue basis. It's not just that kind of push at the end of the quarter. This is a monthly cadence now.

Okay. Thank you very much, Vijay, and thanks, everyone, for all of your questions, as always, and listening in to the call, and we look forward to seeing you all in person at the full year results. So thank you very much.

Operator

Ladies and gentlemen, this concludes the Sage Q3 Trading Update Conference Call. Thank you for your participation. You may now disconnect.