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Gregg Moskowitz, Cowen & Company
Arjun Bhatia, William Blair & Company, LLC
Ittai Kidron, Oppenheimer & Co., Inc.
Robert Majek, Raymond James
John DiFucci, Jefferies
Sanjit Singh, Morgan Stanley
Jacqueline Cheong, Bank of America Merrill Lynch
Jonathan Kees, Summit Insights Group, LLC
Hannah Rudoff, D.A. Davidson
Heather Bellini, Goldman Sachs

PRESENTATION

Operator:

Good afternoon, ladies and gentlemen. Thank you for joining Atlassian’s earnings conference call for the first quarter of fiscal 2019. As a reminder, this conference call is being recorded and will be available for replay from the Investor Relations section of Atlassian’s website following this call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero.
I will now hand the call over to Ian Lee, Atlassian’s Head of Investor Relations.

Ian Lee:

Good afternoon and welcome to Atlassian’s First Quarter Fiscal 2019 Earnings Conference Call. On the call today we have Atlassian’s Co-Founders and CEOs, Scott Farquhar and Mike Cannon-Brookes; our Chief Financial Officer, James Beer; and our President, Jay Simons.

Earlier today we issued a press release and a shareholder letter with our financial results and commentary for our first quarter of Fiscal 2019. These items were posted on the Investor Relations section of Atlassian’s website at investors.atlassian.com. On our IR website there’s also an accompanying presentation and data sheet available.

We’ll make some brief opening remarks and then spend the rest of the call on Q&A.

Statements made on this call include forward-looking statements. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. You should not rely upon forward-looking statements as predictions of future events. Forward-looking statements represent our Management’s beliefs and assumptions only as of the date such statements are made.

Further information on these and other factors that could affect the Company’s financial results is included in filings we make with the Securities and Exchange Commission from time to time, including the section entitled Risk Factors in our most recent Forms 20-F and 6-K.

In addition, during today’s call we will discuss non-IFRS financial measures. These non-IFRS financial measures are in addition to and not as a substitute for or superior to measures of financial performance prepared in accordance with IFRS. There are a number of limitations related to the use of these non-IFRS financial measures versus their nearest IFRS equivalents, and they may be different from non-IFRS measures used by other companies. A reconciliation between IFRS and non-IFRS financial measures is available in our earnings release, our shareholder letter and in our updated investor data sheet on our IR website.

I will now turn the call over to Scott for his brief opening remarks before we move to Q&A.

Scott Farquhar:

Good afternoon and thanks everyone for joining today. We had a great start to Fiscal 2019. This quarter we grew revenue by 37% year-over-year and generated more than $74.2 million of free cash flow. We also added over 5,800 net new customers during the quarter and now have more than 131,000 customers in total.

At Atlassian’s Summit Europe in Barcelona last month, Mike and I were privileged to meet with many of our European customers, listen to their feedback, and share our latest product and Company updates with them.

In keeping with the theme of doubling down on IT themes that we discussed last quarter, we made two significant announcements at Summit that enabled more than 90 (phon) organizations to better manage one of their biggest challenges: preventing and responding to service disruption.

First we announced the acquisition of OpsGenie, our leader in incident (inaudible). Second, we launched our newest product, Jira Ops, which is the centralized hub for IT teams to coordinate their work during an incident. Together with our other products, OpsGenie and Jira Ops helps IT operations teams resolve...
outages faster and incur fewer incidents over time. We’ve provided more detail on those announcements, along with many other updates, in our shareholder letter that was issued earlier today.

With that I’ll pass the call over to the Operator for Q&A.

Operator:

Okay. We will now begin the question-and-answer session. To ask a question, you may press star, then one on your touchtone phone. If you’re using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. At this time we’ll pause momentarily to assemble our roster.

The first question comes from Gregg Moskowitz with Cowen & Company. Please go ahead.

Gregg Moskowitz:

Okay. Thank you very much and good afternoon, guys. Just to start off, a question either for James or Jay; how would you characterize the amount of pull-forward this quarter as compared with what you saw a year ago?

James Beer:

Gregg, this is James. In terms of the billings number generally, I was pleased with the results that we recorded in Q1. Nice business strengths really right across the board, but particularly around the Cloud side of our business.

Now, in terms of the price increase effect, recall that we announced those server price increases a couple of weeks later than we did last year, so that was only two weeks before the end of the quarter. We saw some pull-forward, but, really, it was quite a modest affect. I would expect to see more of that affect in Q2 as we move forward here. Of course, I further expect that that pull-forward would be, in essence, drawn moving billings up from the second half of the fiscal year.

Gregg Moskowitz:

Right. That makes sense. Then a question on Jira Ops. I know it’s in early access for the rest of the calendar year, but I’m curious how significant you think the attach opportunity is, both for current opportunity customers as well as for your install base more broadly going forward.

Scott Farquhar:

Thanks, Gregg. This is Scott. I’ll take that one. I’ll just got back into explain how we think about the whole space in order to answer that question. We said in previous calls that this year IT would be an increased investment for us and you’ve seen that. There’re significant changes happening in IT teams around the world. They’re investing more in software and software is a bigger part of what they do. They’re also increasingly collaborative. Both of those changes make us very well-positioned to attack the IT space. They’re both strengths of Atlassian.

Into the management there’s a convergence of software and IT. It’s actually where they come together. As we said, the acquisition—you’ve got about $700 billion of outages caused every year just in North America, so it’s a very, very big opportunity if you can reduce the cost of outages to businesses.

We’ve got three products in this space now. OpsGenie, which is the sort of call rostering and awarding, so your developers and your IT teams are on call, they manage all that through OpsGenie. We have Statuspage where we communicate out to end-customers and it’s the leading solution for that. So when you have downtime or outages, you wonder if your customers are aware of that so that they know and
build trust with your customers. Third, we’ve got Jira Ops. The reason we built that is that many of our customers already want to manage work in Jira, all the work that they have happens in Jira and Jira Ops is a specialization of Jira specifically for incidents. We have tens of thousands of customers using Jira already and we see that incident management is going to be a fact of life for almost every software developer out there as people move to the cloud and they have to manage things 24/7. That’s sort of a big cultural change for every single developer.

So we see a world where in the coming 5 or 10 years it would be unusual for developers not to be on-call and not be part of an on-call rostering system. So the combination of opportunity in Statuspage and Jira Ops will be sort of something that every developer will need.

Gregg Moskowitz:

All right. Terrific, Scott. That’s very helpful. Thank you.

Operator:

Okay. The next question comes from Bhavan Suri with William Blair. Please go ahead.

Arjun Bhatia:

Hey, guys. It’s actually Arjun in Bhavan. I actually just wanted to follow up on the last question. You have three products addressing the IT market now. What role do you see new product introductions playing in your IT growth strategy into the future? I there anything you’re hearing from customers in terms of product apps that you can share with us?

Scott Farquhar:

This is Scott. I’ll take that again. First of all, we have more than three products we see that target IT. Confluence is used actually overwhelmingly by IT teams. It may be even our most deployed product because IT teams use a lot of Confluence in documentation and run books and procedures. Jira Service Desk is used heavily to answer customers who’ve got queries or internal queries for an IT help desk. In addition to the three products and, of course, many IT teams develop software so they’re using Jira Software for that. They use Jira Core to manage workflow across the business.

So I would view our product portfolio as largely already targeting IT teams. Now, I can’t go into specifics on gaps there. We see ourselves pretty well-placed at the moment to serve a lot of IT team needs. There are some specific things that we’re looking to improve, but I wouldn’t say there’s an overwhelmingly huge gap in our line-up. Of course, as we get into this market and we have a larger customer base, they will be telling us the bits that they want us to deliver for them.

Arjun Bhatia:

Great. Thank you.

Operator:

Okay. The next question comes from Ittai Kidron with Oppenheimer. Please go ahead.

Ittai Kidron:

Yes. Thanks. James, just want to make sure I got the billings caller correctly. Basically you’re saying that you have less impact from a time standpoint of the increase in the quarter, therefore the pull-forward effect was not as expect as expected and lot of it will be absorbed in Q2 before normalizing in the second half; is that the way we should think about that pattern of billings in the year?
James Beer:

Well, I would say that just a tad differently because in Q1 we got a relatively modest pull-forward, but that is what we expected. Again, the price increases were only announced a couple of weeks before the end of the quarter and that was a couple of weeks later than the price increases that were rolled out a year ago. So it’s not a surprise to us that there would be a relatively modest pull-forward activity in Q1. Therefore, I would expect to see more of a pull-forward in Q2. Again, that would tend to be pulled, in essence, billings moving up originally from the second half, up into Q2 to some degree.

Now, I also think that it’s important because this is, after all, the first quarter that we’ve been reporting under IFRS 15 and so it’s important, as you think about estimating our billings in terms of revenue plus change in deferred, that you do that calculation on a fully IFRS 15 basis. If you do that, you get to a billings growth rate year-over-year for the first quarter of 33%, so you get to a $289 million calculated billings bigger. So, it’s a very different if you ended up using some of the old IAS 18 accounting statistics.

I think it’s important just to make sure that we’re all focused on this new IFRS 15 world.

Ittai Kidron:

Yes. Very good. Thanks for clarifying. It sounds like a lot of fun. Help me think about the Perpetual License revenue. We’re now down into the single digits. Would you expect that to recover or you think at this point this figure needs to continue to kind of fade away as your Subscription revenue grows? Maybe tying into that, you keep surprising us on the gross margin even though you keep trying to guide us to expect lower gross margin given your Cloud ramp. Help me reconcile the two.

James Beer:

Yes. First of all I’ll talk about Perpetual License. We saw growth during the quarter of 12% year-over-year and I think this is a good illustration of how more and more of our customers are choosing either our Cloud Service offerings for our Data Center offerings. Both of those, of course, are accounted for within the Subscription revenue line which grew very nicely at 55% year-over-year. There’s clearly a customer choice here.

In terms of what I’d expect for this line going forward, remember that we’ve just rolled out some price increases for the Service side of our business, so that will, over time, help support both the Perpetual License and Maintenance lines in the revenue part of our equation. In terms of License revenue, when a current customer upgrades their footprint with us, so adds more users, then we’d be adding License revenue, and those upgrades would be subject to the new pricing as time goes by. I think that will, at different points, tend to support the growth rate of that line item.

Moving to your question about gross margins, yes, we do still believe that over time, as we have more and more of our mix of business moved to the Cloud, that we would see a gradual pressure downward on gross margins. In the more short-term, a variety of other factors playing out. In the quarter we just closed, I was pleased with the gross margin performance. One of the things that was going down there is we’ve had a number of initiatives in-house to ensure that we are utilizing our AWS resources. We use AWS to power the delivery of our Cloud services. We’ve had initiatives underway to make sure that we are utilizing those services from AWS as efficiently as we can, so that helps support the Q1 gross margin.

As you think about gross margin for the rest of the year, there’s also an AWS, frankly, to think about because I would foresee that we’ll financially be investing further in that AWS infrastructure in order to support the performance levels of our fast-growing Cloud Services. It’ll be a few feet different factors, but strong gross margin in Q1; I would expect a lower gross margin over the remainder of the year.
Ittai Kidron:
Very good. All right. Helpful. Good luck, guys.

James Beer:
Thanks.

Operator:
Okay. The next question comes from Michael Turits with Raymond James. Please go ahead.

Robert Majek:
Hi. This is actually Robert Majek on for Michael. Just following up on a prior question on OpsGenie, can you just talk about how the customer response has been so far and what the integration opportunity is with Jira Service Desk?

Scott Farquhar:
Yes, Robert. It’s Scott here. The customers have been really happy, extremely happy. OpsGenie is a fantastic product. We’re really excited by the product. It’s also great culture fit which is really important for us as a Company as well to make sure that they fit very well with Atlassian. They have about 3,000 customers at the moment and the biggest thing we can do is introduce our 130,000 Atlassian customer to OpsGenie. The product itself is a fantastic product, fully featured, and we’re really excited to sort of introduce our customer base to that product. It’s definitely a big need in the market. We had a great reception at our Summit when we announced it and we continue to hear a lot of demand from customers.

Robert Majek:
That’s great. Maybe just one more for me; can you just talk about how you did with (Inaudible) on the quarter and then maybe touch on the curve (phon) business and go-to-market strategy there?

Scott Farquhar:
Sorry, with what on the quarter?

Robert Majek:
(Cross-talking) Federal, right.

Jay Simons:
It performed in line with what we expected. I think no major—it tends to be a larger quarter for Federal and we sort of delivered what we wanted to.

Robert Majek:
Thanks a lot.
John DiFucci:

Thank you. I think the first question is for Scott. Scott, I think in your shareholder letter you said that almost 60% of the attendees at the Barcelona conference identified themselves as part of IT teams. You just mentioned earlier that you’re sort of—I’m not sure exactly how you said it—but investing in the IT world. But I just want to make sure, like, I understand what that 60% means because does that mean the other 40% were mostly non-IT people? I guess, I think that’s a bigger number than—and I know you’re not sure exactly how many people that are non-IT using your stuff, but I’ve always thought of it as about a third in the past. I guess I’m just wondering, are you seeing adoption of Atlassian products—OpsGenie aside because it’s a true IT product—by non-IT people picking up over the last, I don’t know, six months or so and how should we think about that going forward?

Scott Farquhar:

Thanks, John. Roughly 60% attended identifying as IT, that’s people working IT department of businesses. There are other software people also that work in other departments of businesses, and so there’ll be some of that. But your point around increasing beyond sort of our traditional base of software and IT, we’re continually happy with that. We know that Trello is largely used beyond a traditional technical user base and we announced the 35 million accounts or users of Trello today and that’s a huge growth. Even at very large numbers, that continues to be very strong for us.

Confluence, as I mentioned before, is sometimes originally deployed by IT, but our most successful instances is when Confluence becomes wall-to-wall inside an organization and because the hub for how information flows around a business. So we continued to be very happy with how Confluence is performing inside our user base. It’s sort of something that doesn’t get as much focus as it possibly should. It’s a great product that has a huge number of fans and does get deployed wall-to-wall into an organization.

John DiFucci:

Okay. Great. I do have a follow-up on something else. Maybe for James, on the Slack partnership, I know when you announced it last quarter you announced it and you announced earnings, and you couldn’t really say a whole lot on any details on the financial side. I’m just curious if there’s anything more you can share with us at this point now that you’re a quarter into it, perhaps on revenue sharing, anything, like even general information because you couldn’t say a whole lot last time. Then maybe you, James, or Scott or Jay or somebody, anything on the status of the progression of that partnership as far as adoption within both customer bases?

James Beer:

Hi, John. It’s James. In terms of the financials around developing a relationship with Slack, that is proceeding along as I would’ve had expected it to. We see obviously some of our customers have tried and hit chat already, looking to migrate over to Slack, and so we’re helping those customers make that movement and Slack is paying us as we expected for those migration services. That is moving ahead very much according to plan. That had a very modest impact on our bookings during the quarter, but it was a factor within those results.

In terms of go-to-market activity, I think very early days in that regard so nothing material at this stage driving the bookings line in that manner. I think just another illustration of the strength of the partnership and how it’s developing is we’ve very much been at each other’s user conferences very prominently and so forth, and so we’re pleased to the start that we’re off to.
John DiFucci:

Okay. Great. Thank you guys.

Operator:

Okay. The next question comes from Heather Bellini with Goldman Sachs. Please go ahead.

Heather Bellini:

Great. Thank you so much. I just wanted to do another follow-up on OpsGenie and Jira Ops. I was just wondering who are you guys replacing there; is anyone even using a competitive product or is this done still via Excel spreadsheets today and how do you see that helping differentiate the Jira Ops offering? Then the other thing I was wondering is listening to you guys talk about this, how do you think about this Jira Ops pulling Jira Service Desk into conversations and vice versa, do you see these as kind of a flywheel to get both products ultimately deployed at a customer? Thank you.

Scott Farquhar:

Thanks, Heather. It's Scott here. OpsGenie completes with other awarding systems in the market out there. It does well. We estimate a significant part of our new customer adds come from competition, but this is an area that is really changing at the moment. I would say it's still a very small number of developers today that are on-call, but everyone we talk to says that's the way that it's headed. This is very, very early in sort of the market adoption of the space and we expect to be part of helping people in their transition.

With Jira Ops what we find across our customer base is that people want to manage their work in Jira in one location and whether that is the development work they've got to do to get stuff out or the marketing team who's working around a launch or it's the IT teams who want to manage internal tickets with their internal helpdesk, having that work in one location makes a huge difference for them. So, when we looked at whether to build Jira Ops or not, now thing we found was our customers want to manage their incidents in one spot with all the other work, but they also, more importantly, want to manage all the follow-up items from those incidents in one place.

The great part of Jira Ops is not only is it useful during the incident but it's even more useful after the incident where you want to track all the actions that come out of that to prevent it happening in the first place. The idea is that by using Jira Ops you have fewer incidents in the future and you maintain and track work in one place. So with Jira as the platform for work, we've done Jira Service Desk, we have Jira Core, as the general business work flows to your software, some people writing software in now Jira Ops has some people handling the incidents. You'll see more of that at a time with just us finding ways to help our customers track more work in Jira.

Mike Cannon-Brookes:

Heather, just a small thing. This is Mike. At a philosophical level, it's worth zooming out slightly. Both Jira Ops and Jira Service Desk are extremely customer led. In both cases we've used what customers are already using Jira for and then built a more specific, better version for that particular workflow or use case. Jira has thousands of different workflows and opportunities to track work inside a business. When we saw a 30%, 40% of customers using it for service delivery of some kind, we built a far better service desk to handle that workflow with features that were tailored for that workflow; Jira Ops is very similar. A lot of these customers are already using Jira to manage the work during their incident, we've just built a better way for them to do that. It's more tailored and more specific to that use case which will both get more customers using that but also the existing customers having a better experience.
Heather Bellini:

Thank you very much.

Operator:

Okay. The next question comes from Keith Weiss with Morgan Stanley. Please go ahead.

Sanjit:

Hi. This is Sanjit for Keith Weiss. Thank you for taking the question. There’s been a lot of focus on the IT side of the house, but I guess maybe for Mike or Scott, or even for Jay, as you think about the non-IT work side moving into the user market, I think you probably need a little bit onus on products like Confluence, products like Trello. Could you give us an update on how the monetization has been progressing with Trello now that you’re up to sort of 35 million users, any sort of update there?

Mike Cannon-Brookes:

Yes. Good day, mate. It’s Mike here. I can certainly take that. Look, again, if I start at the philosophy level, both software and IT are incredible landing spots for us within an organization. There are teams that actively go out and seek solutions and seek improvements to their workflows. There are also teams that work with a lot of other companies, so that’s why you see us often landing Jira or Confluence in IT teams in various different flavors for Jira, but then expanding to the rest of the business. When we think about all teams in a business we think about Jira and Confluence as much as we think about something like Trello. It’s worth saying that all of those are—when we consider all teams there’s a huge amount of non-IT, non-software work happening in both of those products.

Trello has some of the same semantics, so it does land in IT teams, it does land in software teams, especially in smaller organizations, but obviously expands much more rapidly than that and does a huge amount of landing outside of that as well. We obviously continue to be hugely excited about the Trello opportunity. I don’t think we could’ve been more excited. What are we, 18 months into the journey with the Trello team? We did say that Trello was past 35 million registered users which is up from about 25 million a year ago, so obviously continues to have great growth.

No change in our workload there in Trello. It continues to be priority number one of continuing to grow the Trello business and the Trello product for the opportunity to have it by itself; and, secondarily, focusing on monetization and integration with the rest of the Atlassian Family. We’ll continue to put things in that order. Trello did, as we said last quarter, meaningfully exceed the $20 million target for FY’18 on the revenue side, which is great, but we continue to put Trello growth and Trello monetization by itself first and cross-selling and cross-flow second.

Sanjit:

That’s very helpful. Thank you for that. Then maybe for James, just so that I’m clear, if we go back to last years’ price increases, for the customers that renewed early and maybe they signed an annual contract, or in some cases multyear contracts, just so that—given the price increases, if they were up for renewal this year or even next year, they would be exposed to the new price increases; do I have this dynamic correct?

James Beer:

Yes. I mean, you do at a high level. It’s a rolling effect, if you will, because in that circumstance, if someone last year, in essence, pulled forward their renewal, say, for a year, and the renewal was coming up right around the time in which we announced those price increases, they could, once again, in essence, pull forward the next renewal. But, of course, that new renewal would be, in essence, at last
year’s price increased rate. So, you’re you just being able to defer, so some portion of our customer base decide to early renew and therefore, in essence, extend their old pricing for another year or so.

**Sanjit:**

That makes perfect sense. Thank you.

**Operator:**

Okay. The next question comes from Nikolay Beliov with Bank of America Merrill Lynch. Please go ahead.

**Jacqueline Cheong:**

Hi. This is actually Jacqueline Cheong on for Nikolay. For this year, did you see any difference in customer behavior around the pricing changes versus last year? Could you comment on both the Cloud and Server ignition (phon)? If we could get an update on the Home product as well.

**Jay Simons:**

Sure. I’m going to pass it to Mike on the Home product, but really quickly on the pricing—this is Jay—no differences. As we said before, we do a ton of analysis to support the changes that we do make around pricing. Do keep in mind that with the changes that we announced in September, the increase for an average customer is pretty nominal, measured in hundreds of dollars, and still our prices remain incredibly affordable relative to what our customers would spend on software that they value less. Then maybe the only other point is that just from a floppy perspective—we’ve stressed this before but it’s worth stressing again—that our pricing philosophy is pretty deeply rooted. We want to provide the best value at the absolute best price in every category in which we compete and that tends to be an Atlassian advantage.

Over to Mike for Home.

**Mike Cannon-Brookes:**

Yes. Hi, there. I can take the Home product down here in Sydney. Again, worth perhaps a reminder, so the Teamwork platform that we have been building now for a couple of years that underpins a lot of our product, not all—obviously not in OpsGenie, not yet in Trello really in a meaningful way—continues to be something that we invest in for a number of different reasons. Firstly, from a cost in R&D perspective, obviously if we can get more products using similar infrastructure. We’ve moved almost all our products now to a common identity call, for example, for login and sign up and user management, things like this. That obviously uses cost advantages in building things. We can invest in building better and more and leveraging that across a number of products. Secondly, it gives the customers a more consistent experience.

We are constantly trying to be pragmatic about the balance between providing a great single product experience and providing a great Atlassian Family experience. It’s not an easy balance to strive and we continue to work to do that. One of the areas that we have been working now for about a year-and-a-half on is what’s normally called Home. One should be careful; it’s a product, yes; it’s not a for-sale product. You can think about it as something you get free when you have a single Atlassian product, two Atlassian products, three Atlassian products, you get Home in the box, and consists of a number of pieces. It continues to be more and more of a default starting location for our customers whether they’re using Jira Confluence, our Jira and Confluence together, and we’ll continue to do that.

There’s an advantage, obviously your chances of choosing a second product if you’re using Home, and it includes the people directory which is now largely common in Cloud, so who is using these product, what
are they doing in the products, etc. It will just be something that we continue to work on across people, cross search, across notifications and various other things. It's not all for-sale product per se, but obviously long-term it'll drive higher customer satisfaction and better crossflow among the product.

**Jacqueline Cheong:**

Thanks. Maybe another follow-up. The Cloud version was a major area of the assessment. Now that the Cloud version is up and running, are we going to see some R&D leverage going forward? Also, what are the R&D priorities looking ahead?

**Mike Cannon-Brookes:**

Look, I can take that. I would say one thing to be cautious on, yes, the Cloud version is quite up and running, but it continues to require major investment. There’s still a lot of work we’re doing on continuing to be more and more world-class cloud provider. You can see that on the enterprise side of things. This quarter we both raised the 2,000 user upper limit to 5,000, so obviously giving our larger customers in Cloud a lot more headroom to continue to expand, and obviously we’d only do that if we thought we could support those customers and give them a great experience. Secondly, we’ve launched products like Atlassian Access, which launched about three months ago for common user provisioning, identity control and security management product for organizations that have a large number of users in our Cloud offerings. So there continues to be a lot of work. (Inaudible) also just in the infrastructure of scaling the Atlassian Cloud, we’ve launched a couple of new regions so now we’re available in Ireland and Sydney in Australia for the Asia-Pacific region and we announced that we’re bringing up two other regions as well in Singapore and in Frankfurt in Germany. So, they all continue to be large areas of investment for the R&D infrastructure side of Cloud beyond the historical movement to AWS which is largely finished now, yes.

**James Beer:**

Yes. This is James. I’d just add to your question about leverage that we would continue to expect to record modest annual increases in our operating and free cash flow margins over time.

**Jacqueline Cheong:**

Okay. Thank you.

**Operator:**

Okay. The next question comes from Jonathan Kees with Summit Insights Group. Please go ahead.

**Jonathan Kees:**

Hi. Thanks for taking my questions. Just wanted to ask I guess more on the competitive picture. If I can be specific, Microsoft obviously was purchased and invested now in GitHub, and also its new version of Project. Are you rubbing elbows more with that; are you seeing any change in that dynamic? Obviously since you’re doubling down in IT are you also now rubbing elbows more with ServiceNow in IT, as well as with their version of Service Desk in terms of RFPs and in terms of your competitive lens? Thanks.

**Scott Farquhar:**

This is Scott here. I’ll take that. Look, in terms of GitHub and Microsoft we’re not seeing any change there. We’re not seeing any material changes in what’s happening there. As I said before, we believe that Microsoft’s key rationale for acquiring GitHub is to encourage developers to use their Zero (phon)
platform and that’s obviously a very different thing to what we’re trying to do with our customer base and with (inaudible).

In terms of ServiceNow, we’ve mentioned before, while we both play in the IT space, we don’t come across them very often. They are largely a top-down sale to the (inaudible) 2,000; we sell to the (inaudible) 500,000 and so our business models are very different and the way we go to market is very different. So, we don’t come across them very often.

Jonathan Kees:

Okay. Great. The last question is with Trello, it sounds like most of the growth is just, especially if your focus is just growing Trello first and then second would be cross-selling, it sounds like most of the Trello users are just purely Trello users, they’re not using any of the Atlassian products. Just wondering if there’s been any particular strengths in terms of Trello; is it via country wise, is it more domestic? At one point you talked about Trello in Japan was going to be a big opportunity. They were looking forward to the inclusion of Trello in terms of the local apps there and the market there was very keen in terms of the Trello purchase. Just some more color in terms of the Trello traction. Thanks.

Mike Cannon-Brookes:

Sure. This is Mike again. Look, Trello is a global phenomenon and one of the things that Atlassian has been able to do since they came on board is do some country-specific launches, as you mentioned in Japan, for example. We’ve also done Sweden and the Nordics, and I believe France as well, though that may have been just before they came on board. Those country-specific launches tend to have a series of local PR events, often user group events where we’ll get Trello users in the country together, as well as specific power ops for Trello that deal with popular local applications.

That tends to just add topspin to Trello in that particular country. I should mention we do localization, although I believe we already had Japan for Trello before that. That’s just a way of driving some more energy in a particular geography. We have Trello users all over the planet, so it is by far our most widely geographically global product. It has a huge amount of opportunity in lots of different flavors. Again, we have a huge amount of Trello work that happens in Japan, as I mentioned, in the Nordics, a lot of users in South America, as well as the traditional audiences of North America and Western Europe. It’s just a very, very large product that we continue to invest in growing all over the world.

You’ll probably see us do some specific country launches, but I wouldn’t get too distracted by that. That’s just where we try to add a little bit of topspin. Usually we’re already in country when we’re doing that and we continue to invest all over and globe in Trello’s opportunity, as well as—what people use it for, a lot of home teams, a lot of teams outside of organizations, as well as teams inside of organizations. Quite often people start using Trello to manage projects with their partner, with their construction person, whatever it may be doing that they’re trying to manage with their families often. Often people get their kids into Trello are doing some family management. If that’s successful for them, they often bring that into their workplace as much as they do vice versa. It’s what makes Trello such a unique product.

Jonathan Kees:

It sounds it. Thanks. I appreciate that color.

Operator:

Again, if you have a question, please press star, then one. The next question comes from Rishi Jaluria with D.A. Davidson. Please go ahead.
Hannah Rudoff:

Hi, guys. This is Hannah on for Rishi. Thank you for taking my question. I was just wondering regarding OpsGenie how much customer overlap you guys have.

Scott Farquhar:

It’s Scott. We’ve disclosed that OpsGenie had 3,000 customers, but we haven’t got into the overlap. That’s not something we typically disclose between the different products. But you could imagine that we have 130,000 customers that you’re going to find a reasonable overlap across the customer basis. But we don’t get any more specific than that, I’m afraid.

Hannah Rudoff:

Okay. Sounds good. Then my second question, I was just wondering how we should think about the Subscription growth going forward on a year-over-year basis.

James Beer:

Yes. We don’t break out the specific revenue lines, if you will, in terms of our guide, but I would say that since the Subscription revenue line encapsulates both our Cloud business and our Data Center business that I would expect that to be a very robust number going forward. So we clearly see more and more customers moving in those directions and I think that will be reflected in our results going forward.

Hannah Rudoff:

Okay. Thank you very much.

James Beer:

If we don’t have any further questions—Operator, let me confirm that first.

Operator;

There are no further questions in the queue.

James Beer:

Okay. Let me just make a few remarks about operating margins. I thought I’d group these remarks first of all in terms of the first half of the year, then address the second half of the year and then give some quarter-specific comments as well.

In terms of the first half of Fiscal ‘19, I mentioned at the start of the call that we were pleased with the revenue performance in Q1. That certainly drove a strong margin result as a result of our performance right across the business—Cloud Server and Data Center. It’s fair to say that during Q1 a goodly portion of our recruitment resources were very much focused on a couple of very discrete projects, the first of all which was our decision to withdraw from the Stride and Hipchat markets and enter into the building relationship with Slack. That drove us to very much focus on finding the right next career step for the material number of our team who have been developing Stride and Hipchat over recent years. I was very pleased that we were very successful in that regard in terms of finding the good next step further and a very significant majority for that team.

The second major initiative that the Recruitment Team was focused on, of course, was the acquisition of OpsGenie which brought into the Company around 200 new employees as well. I would expect that in the
second quarter now with much of that work behind us, that the Recruitment Team will be able to focus more of their effort around our organic hiring goals.

That brings me to some thoughts around the second half margin story in Fiscal ‘19. I would expect organic headcount to increase and that therefore the second half operating margins would be lower than those recorded in the first half of the year. Now recall I mentioned earlier in this conversation that we also expected somewhat lower gross margins in the second half of the year as a result of our AWS investment plans. More specifically, I would look in the second half of the fiscal year for opportunities to really invest against the very significant opportunity that we have in the IT teams area. Obviously we’ve talked a lot about that on this call in the last 45 minutes or so, and we are very excited in particular about our OpsGenie opportunity. I would see hiring marketing and product development resources all being a part of that focus in the second half of the year.

Lastly, just turning to some additional quarter-specific commentary on operating margins, first of all, just building on that last thought of us really working hard in support of the OpsGenie opportunity, we plan to initiate some targeted marketing spend in Q2, so I would expect to see a slightly higher ratio of our Q2 marketing spend as a percentage of revenue when we get together in 90 days’ time. Second, I would expect there to be a decline in margin from Q2 to Q3, as is quite typical because since the start of Q3 we that we roll out new salary increases for our team and also reset payroll taxes. I would further expect that that sequential decline from Q2 to Q3 in terms of operating margins would be pretty consistent with what we saw last year between Q2 and Q3 on an IFRS 15 basis. Again, it’s important that we be working in the new IFRS 15 accounting structures.

With all of that said, just, again, to wrap up, as I mentioned earlier, that we would expect ongoing annual modest increases in both operating and free cash flow margins over time.

Mike, you going to wrap up?

**Mike Cannon-Brookes:**

Thanks, James, and thanks, everyone for joining the call today. We really appreciate your time and look forward to keeping you updated on our progress in the future quarters. Have a kick ass weekend.

**Operator:**

The conference has now concluded. Thank you for attending today’s presentation. You may now disconnect.