

# Global Innovation

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## Atlassian - fostering collaboration and cashflow

**Innovation cash kings of the next decade** - *In this series we look at the standout companies that are 'pivoting to profit' and are at an inflection point of converting customer-driven innovation into shareholder value. In the last of this series, we take a closer look at Atlassian.*

Few have probably heard of Atlassian – this Australian company selling cloud-based collaboration software to developers and IT departments is far from a household name. Yet knowingly or unknowingly, you will have been touched by the company's productivity solutions. If you have been on a Zoom call, you have experienced Atlassian – they are Zoom's go-to-tool for software development and technical project management. If you use Slack to communicate in your workplace, it is Atlassian that helps to power a frictionless experience through its IT service ticketing solutions. The athletes among us using Strava benefit unwittingly from Atlassian's ticketing resolutions, while the non-athletes gain equal pleasure through Atlassian's developer tools that help Domino's deliver pizza and technology faster.

Jira software and Jira service management (the company's flagship developer and IT operations tools respectively) might sound foreign to us, but they form the linguistic bread and butter of software developer communities. Simplistically, these collaboration tools make developers and IT teams more productive: think of them as an ecosystem that displays every task fellow teammates are working on, outstanding problems to be solved, and tracks project progress.

Providing the platform for developers and IT departments to collaborate with each other leads to faster development and deployment of software features, a customer value proposition that has never been more pertinent than in today's world: demand for AI driven software is supply, not demand, constrained and companies' most scarce resource are developers. Indeed, at the top of CEO's priority lists across industries right now is the burning question of: 'how do I make my developer's more productive?' Atlassian is in a prime position to service this cry as the only vendor that brings developers, IT operations and non-technical teams together on the same

platform. This competitive advantage is key to why the company continues to win share from higher priced legacy players.

Yet the past 18 months has been a tough operating environment for software names and Atlassian has not been immune from the pullback in IT budgets and optimisation of cloud spend by its customers. How has the company responded? With speed and agility.

Over the past two quarters, management has taken significant strides to realign its cost structure with revenue growth: expenses have been reassessed to maximise the return on every investment dollar spent; bonuses for executives have been slashed and headcount has been trimmed as part of restructuring efforts to create a leaner organisation. The result? Underlying operating margins have re-inflected, growing 8 percentage points versus the same quarter last year to 22% while free-cash-flow has rebounded at an even faster clip of 42%, climbing to a 29% margin.

Crucially, the Atlassian innovation machine has not been sacrificed at the altar of cost rationalisation. When we talk of companies focusing on the core and pivoting to profitability, we want to see the preservation of innovation that fuels customer growth – companies who can achieve similar growth outcomes with the same customer value proposition, just at lower cost. While senior management's bonuses have been axed, R&D budgets have not. Atlassian is spending over 50% of its revenues on R&D, proportionately almost double its peers who instead spend twice as much on sales and marketing. The idea here is that a more innovative product can sell itself, creating a flywheel of network effects that act as a formidable barrier to competition.

Why do we expect cash generation to materially ramp from here? Three key reasons. Firstly, the company has capitalised on the post-Covid market downturn (as it did after the global financial crisis) by making versions of its products essentially free, appealing to companies who have never considered Atlassian before. 70% of new customers convert from the free edition, so as the macro environment improves, we expect more paying customers to enter the fold – almost 20,000 have been converted in the past year already. Secondly, Atlassian outspends its competitors on R&D by a country mile, ensuring best-in-class products that attract more customers. And lastly, the company is poised to benefit from the surge in interest in AI. Not only is Atlassian's 'AI powered teammate' embedded in each and every one of its cloud-based products, but its addressable market is about to explode: AI will enable more people to create software; more creators mean more collaboration needs.

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We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments

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