

Sunlands Technology Group
Third Quarter 2023 Earnings Conference Call Script
November 22, 2023, 7:30 PM BJT

Operator: *Ladies and gentlemen, thank you for standing by, and welcome to Sunlands' Third Quarter 2023 Earnings Conference Call. At this time, all participants are in listen-only mode. Today's conference call is being recorded. I will now turn the call over to your host today, Yuhua, Sunlands' IR representative. Please go ahead.*

Yuhua Ye

Hello, everyone, and thank you for joining Sunlands' Third Quarter 2023 Earnings Conference Call. The company's financial and operating results were issued in our press release via newswire services earlier today and are posted online. You can download the earnings press release and sign up for our distribution list by visiting our IR website. Participants on today's call will be our CEO, Mr. Tongbo Liu, and our financial representative, Mr. Hangyu Li. Management will begin with prepared remarks and the call will conclude with a Q&A session.

Before I hand it over to the management, I'd like to remind you of Sunlands' safe harbor statement in relation to today's call. Except for the historical information contained herein, certain of the matters discussed in this conference call are forward-looking statements. These statements are based on current trends, estimates and projections, and therefore, you should not place undue reliance on them. Forward-looking statements involve inherent risks and uncertainties. A number of important factors could cause actual results to differ materially from those contained in any forward-looking statement. For more information about the potential risks and uncertainties, please refer to the company's filings with the Securities and Exchange Commission.

With that, I will now turn the call over to our CEO, Tongbo Liu.

Tongbo Liu

Thank you, Yuhua.

Hello, everyone. Welcome to Sunlands' Third Quarter 2023 Conference Call. Prior to commencing, I would like to kindly remind all attendees that the financial information referenced in this release are presented on a continuing operations basis, and all figures are denominated in RMB, unless explicitly specified otherwise.

In Q3, our business has consistently adjusted to the evolving economic landscape and has strategically progressed despite the challenges. Our overarching objective of propelling the Group toward sustained, high-level profitability has yielded positive results, as we maintained sizable net profits for ten consecutive quarters. Net income reached 131.6 million. Net revenues, despite a slight year-over-year decrease, exceeded the high end of our guidance range and reached 524.6 million. We were also pleased to see our ongoing efforts to optimize our product structure and expand our course portfolio rewarded with enhanced operational results, reflected in a 14.3% year-over-year increase in our new student enrollments and a 6.7% year-over-year increase in gross billings.

We are delighted in our capability to remain profitable under challenging environment. This success is attributed to improvements in gross margins, the implementation of cost-cutting measures, and enhanced financial planning and analysis across the entire business. Our cost of revenues has achieved a year-over-year decrease of 24.5% and general and administrative expenses have achieved a year-over-year decrease of 21.0%. We firmly believe that only by adhering to a long-term perspective and ensuring the healthy growth of the enterprise can we create sustainable value for shareholders and users.

Now, let's turn to the performance of each of our major course programs.

Due to uncertainties surrounding the macroeconomic environment, our degree or diploma-oriented consumers have adopted a more conservative approach to the spending. This sector experienced a year-over-year revenue decline of 55.2%, influenced by our strategic

reduction in marketing activities. We will persistently enhance our operational efficiency through continuous market observation and remain dedicated to providing premium courses for our in-progress students.

The segment including professional certifications, professional skills, and interest programs has represented as our new growth driver, accounting for 70.4% of the total revenue, and exhibiting a year-over-year revenue growth of 23.8%. We have strengthened our determination and confidence to increase investment in interest-based education following a thorough process of testing and validation. The number of new student enrollments in professional certifications, professional skills, and interest programs for the first nine months of 2023 increased by 29.1% compared to the same period of 2022, and the total number of paid students has exceeded 1.2 million since 2021.

Today, we would like to delve deeper into our understanding of the sector.

There are several noteworthy shifts in the adult education landscape. Firstly, there's the burgeoning market potential of the silver economy. While the age group of 20-50 remains a steadfast pillar in the industry, it's crucial to highlight that the demographic size of the silver generation continues to grow. According to data disclosed by the National Bureau of Statistics, as of the end of 2022, China's elderly population reached 280 million (aged 60 and above). Among them, 153 million are internet users, indicating that at least one in every two elderly individuals has internet access. A significant portion has already adopted habits of online learning, communication, and socialization. Furthermore, projections indicate that during the "14th Five-Year Plan" period, China's population aged 60 and above will surpass 300 million, accounting for over 20% of the total population. With the aging population, extended life expectancy, and rising per capita income, this represents a significant incremental market.

Based on this observation, we introduced a series of courses tailored to elderly individuals, covering various interest areas such as vocal music, musical instruments, calligraphy and traditional painting. Leveraging our two decades of accumulated content creation, service

capabilities, and technological expertise, we quickly gained recognition from this group. Specifically, according to our survey, the satisfaction rate for calligraphy courses is as high as 94.59%, and for traditional Chinese painting courses, it reaches an impressive 98.25%. We are delighted to see that this group not only learn online but also connect with like-minded friends, establishing new social relationships from our platform. We received numerous feedback from this group, and their vivid narratives resonate deeply with us, affirming the meaningful impact of our work. They illustrate how our learning platform caters to the diverse interests and learning needs of various users, fostering continuous personal development and meaningful connections.

Secondly, the increasingly competitive job market is still calling for higher overall qualifications from individuals, leading to a varied and personalized demand for adult education. The transformation is evident on the supply side as well, with an increase in the diversity of professional courses offerings. Our strategy is in alignment with the market as well. We have meticulously curated and provided a suite of premium, tailor-made courses with a professional focus. We are pleased to witness our students' unwavering commitment to actively participate in these courses, and we take pride in assisting them in navigating the challenges of the dynamic working environment. Additionally, we have carefully augmented our selection of interest-based courses in response to the burgeoning inclination towards personalized and passion-driven education. We strive to provide a comprehensive range of additional services and products that extend beyond the confines of traditional learning experiences.

Furthermore, we have also been closely monitoring the application of new technologies in our industry, such as the latest AIGC technology, in our educational business context. We are optimistic about the prospects of the development of this technology. It's worth mentioning that our product development expenses have also increased by 5.3% compared to the previous quarter.

In summary, drawing on a decade of valuable experience and industry acclaim, we are poised to rapidly and efficiently expand our market presence. Going forward, our

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dedication remains unwavering as we adjust our educational offerings to align with the changing needs of learners, reinforcing our leading position in the adult education sector.

With that, I will turn the call over to our Financial Controller, Hangyu, to run through our financials.

Hangyu Li

Thank you, Tongbo. Hello everyone.

I am pleased to present our third quarter results, which were in line with our expectations and demonstrated the effectiveness of our pursuit of sustainable growth.

As you can see, last quarter was another excellent quarter in operations. As a result of steady growth in interest programs, new student enrollments went up by 14.3% and gross billings increased by 6.7% year-over-year. Thanks to our strategy of balanced, sustainable growth and profitability, gross profit margin increased by 2.5 percentage points to 87.8%, compared to the same period last year. Operating expenses as a percentage of gross billings decreased 2.1 percentage points, compared to the third quarter of last year. These improvements were reflected in our net income. Last quarter, we achieved net income of 131.6 million, which is the 10th profitable quarter since the second quarter of 2021.

Looking ahead, we are optimistic about long-term growth. We are committed to expanding online course offerings, optimizing cost-effectiveness, and providing exceptional service to our valued students. These strategic initiatives are conducive to capitalizing on new opportunities and consolidating our prominent position in the industry, which in turn will help us maintain our competitive edge in the industry and continue to create value for our stakeholders.

Now let me walk you through some of our key financial results for the third quarter of 2023. All comparisons are year-over-year, and all numbers are in RMB, unless otherwise noted.

In the third quarter of 2023, net revenues were 524.6 million, a decrease of 9.0% year-over-year. Cost of revenue decreased by 24.5% to 64.1 million in the third quarter of 2023 from 84.9 million in the third quarter of 2022. The decrease was primarily due to declined compensation expenses related to our cost of revenues personnel.

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Gross profit decreased by 6.3% to 460.5 million from 491.3 million in the third quarter of 2022.

In the third quarter of 2023, operating expenses were 338.5 million, representing a 4.1% increase from 325.0 million in the third quarter of 2022.

Sales and marketing expenses increased by 9.6% to 295.0 million in the third quarter of 2023 from 269.1 million in the third quarter of 2022. The increase was mainly due to increased spending on branding and marketing activities.

General and administrative expenses decreased by 21.0% to 35.1 million in the third quarter of 2023 from 44.4 million in the third quarter of 2022.

Product development expenses decreased by 27.0% to 8.4 million in the third quarter of 2023 from 11.5 million in the third quarter 2022. Product development expenses were mainly comprised of compensation expenses.

Net income for the third quarter of 2023 was 131.6 million compared with net income of 168.1 million in the third quarter of 2022.

Basic and diluted net income per share was 19.13 in the third quarter of 2023.

As of September 30, 2023, the Company had 751.8 million of cash, cash equivalents and restricted cash and 122.3 million of short-term investments.

As of September 30, 2023, the Company had a deferred revenue balance of 1,277.0 million compared with 1,690.9 million as of December 31, 2022.

Capital expenditures were incurred primarily in connection with IT infrastructure equipment and a leasehold improvement necessary to support the Company's operations.

Capital expenditures were 1.4 million in the third quarter compared with 1.3 million in the third quarter of 2022.

And now for our outlook. For the fourth quarter of 2023, Sunlands currently expects net revenues to be between 490 million to 510 million, which would represent a decrease of 11.9% to 15.3% year-over-year. This outlook is based on the current market conditions and reflects the company's management's current and preliminary estimate of market, operating conditions and customer demand, which are all subject to change.

With that, I'd like to open up the call to the questions. Operator?

[Operator provides instructions and hosts Q&A]

For the benefit of all participants on today's call, if you wish to ask your question to management in Chinese, please immediately repeat your question in English.

[After Q&A...]

Operator: At this time, we are showing no further questions, so this will conclude our question-and-answer session. At this time, I would like to turn the conference back over to Yuhua for any closing remarks.

Yuhua: Once again, thank you, everyone, for joining today's call. We look forward to speaking with you again soon. Good day and good night.

Operator: This concludes this conference call. You may now disconnect your line. Thank you.