

**Sunlands Online Education Group [STG]  
Q3 2020 Earnings Conference Call  
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Executives

Yuhua Ye, IR Representative  
Tongbo Liu, CEO and Director  
Selena Lv, CFO and Director

**Presentation**

Operator: Ladies and gentlemen, thank you for standing by, and welcome to Sunlands' Third Quarter 2020 Earnings Conference Call. At this time, all participants are in listen-only mode. After prepared remarks by the management team, there will be a question-and-answer session. Today's conference call is being recorded. If you have any objections, you may disconnect at this time.

I would now like to turn the call over to our host today, [Yuhua] Ye, Sunlands' IR Representative. Please go ahead.

Yuhua Ye: Hello, everyone, and thank you for joining Sunlands' third quarter 2020 earnings conference call. The Company's financial and operating results were issued in a 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.

On the call, our CEO Tongbo Liu will provide an update on our operational performance, as well as our strategic initiatives. Our CFO Selena Lv will give you an overview of our financial performance, and also provide our guidance for the fourth quarter of 2020. Following their prepared remarks, we will move into the 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 2020 conference call.

Despite the short-term impact on our operations of the COVID-19 pandemic in the first half of 2020, Sunlands delivered steady year-over-year increases in both gross billings and net revenues in the third quarter. Our results were fueled by a combination of the recovering macroeconomic conditions in China, as well as the implementation of optimization initiatives within our business.

In the third quarter, our gross billings reached RMB 654.3 million, increasing by 6.6 % year-over-year and 23.1% quarter-over-quarter. We attribute our strong gross billings results largely to improvements we made in sales efficiency with new approaches to student acquisition, as well as our enhancing brand awareness and continuous upgrades to our product categories.

Additionally, following the solid performance in the second quarter of 2020, net revenues increased 2.7% year-over-year to RMB 541.6 million, exceeding the top end of our guidance by 4.2%. Moreover, our new enrollments reached over 140,000 in the third quarter, growing 47.8% year-over-year and 70.5% quarter-over-quarter.

During the third quarter, we made further progress to balance our top line growth mix, proving the efficacy of our long-term strategy in efforts to continually expand our portfolio of educational products and bring content innovation. While maintaining a leading market share in STE programs, Master's degree-oriented programs and professional certification and skills programs continued to reveal great potential to become the next pillars among the Company's offerings.

Let me start with Master's degree-oriented programs, which contributed a rounded 31% to gross billings in the third quarter, compared with approximately 17% in the same quarter last year. The growth of Master's degree-oriented programs in terms of gross billings was phenomenal, registering 93.3% year-over-year and 48.4% quarter-over-quarter. This growth was primarily driven by increasing needs from working professionals, as uncertain shifts in the labor market remain in the wake of the COVID-19 pandemic, together with the increasing demand for talent with higher educational background.

In light of this, in order to enrich our program portfolio and address the increased demand for diversified and differentiated higher education, in the third quarter, we further expanded our partnerships with overseas universities, such as Belarusian State University, to provide joint offering programs. Taking into account our existing partners in the United States, the United Kingdom, and Australia, we have now established joint offering programs with over 10 foreign universities. In line with our balanced growth strategy, this effort is designed to further enhance our attractiveness and competitiveness and complement our Master's degree-oriented offerings.

Due to the current macro conditions, in particular, international COVID-related travel restrictions, we are seeing an uptick in demand for these international online-focused joint offering programs. And we believe this trend will continue for the foreseeable future.

Based on the current number of admission applications received for 2021, already announced by most universities in China, we expected the number of applicants for Post Graduate Entrance Exams for 2021 admission to surpass the record of 3.41 million set for 2020. Given this trend,

also with feedback reports from our sales and marketing department, we have high confidence in the continuing favorable demand in this area.

With our proven ability to bring compelling offerings to the market that meet students' needs, we see a sustainable growth pathway ahead in developing our portfolio of Master's degree-oriented and joint offering programs. These programs also typically carry higher margins than our standard programs owing to their higher ASPs, especially MBA programs.

To further implement our sustainable overall growth strategy, we continued to promote the rapidly-growing on-demand course offerings targeting professional certification, vocational education and popular hobbies.

I am very pleased that this segment also delivered significant growth in gross billings in the third quarter. It generated gross billings of RMB 139.9 million, up 301.9% year-over-year and 135% quarter-over-quarter. In the third quarter, this segment accounted for 21.4% of our total gross billings, compared to 5.7% for the third quarter of 2019. The increase in this segment primarily stems from rising requirements from the labor market for workers and candidates equipped with occupational skillsets and professional qualifications to meet higher demanding roles and responsibilities.

With our course offerings presenting attractive ASPs and shorter time durations than traditional post-secondary options, we see favorable growing demand in this segment in the long run. Moreover, we believe graduates from these courses are more likely to purchase services from us again when changing employment factors require enhanced competitiveness.

In the third quarter, we experienced much greater utilization of our online platform. To help students succeed in national STE exams in August and October, as well as Post Graduate Entrance Exams and MBA programs Candidate Tests in the fourth quarter, our teachers are committed to further improving the quality and efficiency of our live streaming classes, schedules, courses and tutorial materials. With such effort and the increased enthusiasm in exam preparation, the total class time spent, the number of class participants and the number of quizzes completed all increased significantly in this quarter, up 39%, 44%, and 45% respectively year-over-year.

Furthermore, to bring an unparalleled user experience and drive user stickiness, we further integrated our cutting-edge AI technologies into all aspects of our online platform, customizing our curriculum offerings and teaching materials to deliver innovative breakthroughs. Continuing to invest in our platform upgrades and incorporating applications of AI technologies to improve teaching results and efficiency will always be part of the effort to sustain our long-term growth.

With our foresight into the online education industry and sustained multi-pronged growth strategies, we are confident in the continued further enhancement of our brand and diversified products.

Looking forward, we aim to drive top line growth by expanding our program categories, increasing the approaches we use to acquire students, and by improving our lead conversion efficiency. At the same time, we will further optimize bottom line performance, enabled by cross-selling increments and using AI technologies throughout our organization.

With that, I would like to hand over the call to our CFO, Selena, to run through our financials.

Selena Lv: Thank you, Tongbo, and hello, everyone. Our third quarter financial results reflect our balanced expansion strategy. Net revenues increased by 2.7% year-over-year, exceeding our expectations. This result is attributable to broad-based improvements across our organization, in particular, optimizing our revenue contribution structure.

Other highlights in the quarter include a significant increase in gross billings and a higher proportion of revenue coming from non-STE programs. These accomplishments came from improved efficiency in our student acquisition and conversion methods, recognition of our program diversity, and content enrichment.

In terms of cost control management, we pursued a strict spending policy, especially in regard to G&A expenses, which were reduced by 16.7% year-over-year.

Looking ahead, we will continue to focus on product and service upgrades by deploying our AI-enabled platform systems and further refinement of our internal operations. We believe this dual-fold effort will bring long-term value to our users and shareholders through a sustainable and balanced approach to growth.

Now, let me walk you through some of the key financial results for the third quarter 2020. All comparisons are year-over-year and all numbers are in RMB, unless otherwise noted.

In the third quarter, net revenues were RMB 541.6 million, an increase of 2.7% year-over-year.

Cost of revenues decreased by 18.2% to RMB 92.9 million in the third quarter from RMB 113.7 million in the third quarter of 2019. The decrease was primarily due to reduced insurance-related costs incurred for our integrated online education service package purchased by students.

Gross profit increased by 8.5% to RMB 448.7 million from RMB 413.6 million in the third quarter of 2019.

In the third quarter, operating expenses were RMB 664.1 million, representing a 21.4% increase from RMB 546.9 million in the third quarter of 2019.

Sales and marketing expenses increased by 32.7% to RMB 569.4 million in the third quarter from RMB 429.2 million in the third quarter of 2019. The increase was mainly due to increases in, number one, compensation paid to our sales and marketing personnel; and number two, spending on branding and marketing activities, including more marketing promotion activities to diversify student acquisition channels; and number three, share-based compensation expenses recognized in the third quarter of 2020.

General and administrative expenses was RMB 76.1 million in the third quarter of 2020, decreased by 16.7% year-over-year mainly due to the decrease in compensation expenses.

Product development expenses decreased by 29.7% to RMB 18.6 million in the third quarter from RMB 26.4 million in the third quarter of 2019. The decrease was primarily due to a

decrease in the compensation incurred related to our product and technology development personnel during the quarter.

Other income increased to RMB 47.3 million in the third quarter from RMB 5.1 million in the third quarter of 2019. The increase was primarily due to the value-added tax exemption of RMB 44.1 million offered by the relevant authorities as part of the national COVID-19 relief effort.

Net loss for the third quarter was RMB 165.8 million, compared with RMB 129.8 million in the third quarter of 2019.

Basic and diluted net loss per share was RMB 24.62 in the third quarter of 2020.

As of September 30, 2020, the Company had RMB 1.1 billion of cash and cash equivalents and RMB 234.4 million of short-term investments.

As of September 30, 2020, the Company had a deferred revenue balance of RMB 3,090.3 million, compared with RMB 3,228.8 million as of December 31, 2019.

Capital expenditures were incurred primarily in connection with IT infrastructure equipment and leasehold improvement necessary to support Sunlands' operations. Capital expenditures were RMB 14.3 million in the third quarter, compared with RMB 11.8 million in the third quarter of 2019.

And now for our outlook. For the fourth quarter of 2020, Sunlands currently expects net revenues to be between RMB 540 million to RMB 560 million, which would represent a decrease of 1.8% to an increase of 1.9% year-over-year.

This outlook is based on the current market conditions and reflects the Company management's current and preliminary estimates 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?

## **Questions and Answers**

Operator: We will now begin the question-and-answer session. (Operator Instructions).

At this time, we are showing no questions, so this will conclude our question-and-answer session. At this time, I'd like to turn the conference back over to Yuhua Ye, IR representative, for any closing remarks.

Yuhua Ye: 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 our earnings conference call. You may disconnect your line now.  
Thank you.