

**Sunlands Online Education Group [STG]
Q3 2021 Earnings Conference Call
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Executives

Yuhua Ye, IR Representative

Tongbo Liu, CEO and Director

Selena Lu Lv, CFO and Director

Presentation

Operator: Ladies and gentlemen, thank you for standing by, and welcome to Sunlands' Third Quarter 2021 Earnings Conference Call. (Operator Instructions). 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 your host today, Yuhua Ye, Sunlands' IR representative. Please go ahead.

Yuhua Ye: Hello, everyone, and thank you for joining Sunlands' third quarter 2021 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 CFO Selena Lu Lv. 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 would now like to turn the call over to our CEO Tongbo Liu.

Tongbo Liu: Thank you, Yuhua. Hello, everyone, and thank you for joining Sunlands' third quarter 2021 earnings conference call. We are pleased with our third quarter financial metrics.

Our net revenues grew 9.9% year-over-year to RMB595.1 million despite the evolving industry dynamics. We recorded net profit of RMB92.8 million compared with net loss of RMB165.8 million during the same period last year, and a year-over-year 33.8% and 29.3% decline in new enrollments and gross billings, respectively, which are attributable to our continued efforts to execute our balanced long-term growth and profitability strategy.

As Covid-19 pandemic resurgences in certain regions in China, continue to create challenges for business operation and the broader economic recovery, businesses have taken steps to improve operating efficiency and reduce costs.

With respect to talent acquisition, many companies have become more prudent in selecting talents and have raised their expectations for candidates and new hires. This ultimately led to a more competitive labor market in the third quarter, prompting working professionals to seek enrichment courses like ours to increase their competitiveness through further education and re-skilling and up-skilling.

Meanwhile, industry dynamics are also evolving rapidly, with an increasing number of companies joining the adult education business after the implementation of China's K-12 after-school tutoring regulations.

Within this landscape, we continued to execute our balanced long-term growth and profitability strategy, and sought to enhance our competitiveness by focusing on optimizing our product mix, improving services, reducing costs and enhancing student acquisition efficiency. We are pursuing quality growth rather than user scale only.

Our professional certificate and skills programs maintained their growth momentum during the quarter. Net revenues and gross billings increased 148.2% and 49.3% year-over-year, respectively, driven by our constant efforts to broaden our course catalog as well as strong user demand for career advancement and skills enhancement. This exceptional performance reflected students' growing adoption of our platform as we refine our course offerings with more premium and diverse course content.

The breadth of our course offerings also appeals to more people across a wider range of age groups, which could help further expand our student base. We believe that with our relentless endeavors to provide our students with a better learning experience, we are well-positioned to fulfill the surging demand for role-or-interest-based learning catering to adults of all ages.

We achieved a 20.8% year-over-year increase in net revenues in our master's degree-oriented programs, while new enrollments and gross billings decreased by 22.2% and 10.2% year-over-year, respectively, as we prioritized quality growth. However, we continued to expand our global footprint during the quarter by forming additional partnerships with overseas universities, and made encouraging progress.

At the same time, we continued to diversify our course portfolio for this segment, looking to capture the huge growth opportunities in this market. Demand for exam preparation courses remains strong, and we expect further growth given the competitive employment market.

Notably, a large number of our students are middle-or senior-level managers who are strongly motivated to acquire more knowledge and sharpen their management skills through MBA and EMBA degree education. Helping them to achieve their learning goals will continue to be a priority as we see solid growth momentum and potential in this space.

Turning now to our STE programs, as we strove to optimize our product mix, gross billings and new enrollments for STE moderated, which was also partially due to the tightening regulation on advertisement for continuing education. We believe these regulations will help the industry achieve healthy and sustainable growth and contribute to China's effort to build a lifelong learning society. We have implemented strict compliance standards and will continue to monitor and comply with relevant rules and regulations, while providing quality courses to our students.

In addition, we adopted stringent polices and attractive incentive plans to enhance our operations and services in the third quarter, with the goal of providing students a smoother, more rewarding learning experience. We also implemented effective cost reduction measures with an emphasis on improving student acquisition efficiency, resulting in a 35.2% year-over-year drop in operating expenses. We achieved this remarkable improvement by fully embracing technology and utilizing the natural synergies across our various segments to realize meaningful growth.

We leveraged targeted, cost-effective new media marketing tools to acquire students, and also continued to capitalize on cross-selling opportunities among different programs to increase repurchase rate and user lifetime value.

We maintained profitability for 2 consecutive quarters as we enriched our course offerings to address varied student needs and optimized cost structure to enhance student acquisition efficiency with more cost-effective, innovative and regulation-compliant marketing tools. We will continue to refine these measures to build on this success and drive quality growth.

That concludes my prepared remarks. Thank you and I will turn the call over to our CFO, Selena, for further review of our financials. Selena, please?

Selena Lu Lv: Thank you, Tongbo. Hello, everyone, and thank you for attending Sunlands' third quarter conference call. We are encouraged by our sustained profitability in the third quarter with registered net profit reaching a new high, driven by continued year-over-year top line growth mainly attributable to professional skills and master's degree-oriented programs.

Profits also benefitted from our efficient cost control measures, which led to a 35.2% year-over-year reduction in operating expenses. Notably, sales and marketing expenses as a percentage of net revenues decreased significantly, by 45.7 percentage points year-over-year.

Going forward, we will continue to focus on operating efficiency enhancement, product mix optimization and service improvement, which will prepare us for the opportunities and challenges ahead while pursuing sustainable growth.

Now, I would like to share our financial results for the third quarter of 2021 in detail. In the third quarter of 2021, net revenues increased by 9.9% to RMB595.1 million from RMB541.6 million in the third quarter of 2020. The increase was mainly driven by year-over-year growth in gross billings since the second half of 2020 through the first quarter of 2021.

Cost of revenues decreased by 10.6% to RMB83.1 million in the third quarter of 2021 from RMB92.9 million in the third quarter of 2020. 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 14.1% to RMB512 million in the third quarter of 2021 from RMB448.7 million in the third quarter of 2020.

In the third quarter of 2021, operating expenses were RMB430.6 million, representing a 35.2% decrease from RMB664.1 million in the third quarter of 2020.

Sales and marketing expenses decreased by 37.9% to RMB353.5 million in the third quarter of 2021 from RMB569.4 million in the third quarter of 2020. The decrease was mainly due to, number one, lower spending on branding and marketing activities; and number two, decreased compensation expenses related to our sales and marketing personnel.

General and administrative expenses decreased by 17% to RMB63.2 million in the third quarter of 2021 from RMB76.1 million in the third quarter of 2020. The decrease was mainly due to a decrease in compensation expenses.

Product development expenses decreased by 24.7% to RMB14 million in the third quarter of 2021 from RMB18.6 million in the third quarter of 2020. The decrease was mainly due to a decrease in compensation expenses.

Other income was RMB12.9 million in the third quarter of 2021, compared with RMB47.3 million in the third quarter of 2020. Other income for the third quarter of 2021 was mainly comprised of rental income of RMB7 million. The decrease was primarily because value-added tax exemption offered by the relevant authorities as part of the national Covid-19 relief effort came to an end in April 2021.

Net income for the third quarter of 2021 was RMB92.8 million, compared with net loss of RMB165.8 million in the third quarter of 2020.

As of September 30, 2021, the Company had RMB661.2 million of cash and cash equivalents and RMB178.8 million of short-term investments.

As of September 30, 2021, the Company had a deferred revenue balance of RMB2,540.9 million.

Capital expenditures were incurred primarily in connection with IT infrastructure equipment and leasehold improvements necessary to support the Company's operations. Capital expenditures were RMB1.8 million in the third quarter of 2021, compared with RMB14.3 million in the third quarter of 2020.

For more of our 2021 first 9 months financial results, please refer to our earnings press release for further details.

And now for our outlook: For the fourth quarter of 2021, Sunlands currently expects net revenues to be between RMB590 million and RMB610 million, which would represent an

increase of 0.9% to 4.3% year-over-year. This outlook is based on current market conditions and reflects the Company's management's current and preliminary estimates of the market, operating conditions and customer demand, all of which are subject to change.

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

Questions and Answers

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

Since there appears to be no questions, this will conclude our question-and-answer session. At this time, I would 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 the earnings conference call. You may now disconnect your line. Thank you for attending.