

**Sunlands Online Education Group [STG]
Q2 2022 Earnings Conference Call
August 18, 2022 7:30 AM**

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' Second Quarter 2022 Earnings Conference Call. (Operator Instructions). 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' second quarter 2022 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 our 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 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' Second Quarter Conference Call. Amid the pandemic's resurgence and macroeconomic weakness in the second quarter, we achieved RMB114.6 million of net income, representing a fourfold increase year-over-year. The increase was primarily driven by our consistent emphasis on operating efficiency

and solid execution of our business strategies, as we remained steadfast while navigating the Company through external uncertainties.

We were also pleased to see our continued efforts to optimize our product mix and expand our course portfolio rewarded with improving operational results, reflected in a 39.4% year-over-year increase in our new student enrollments and a reduced year-over-year decrease in gross billings. We accomplished this by acquiring students from a wider range of age groups with higher sales efficiency, as we cut down our sales and marketing expenses by 34.8% year-over-year. These results highlight our organizational resilience and reinforce our confidence in our strategy to achieve balanced growth and profitability.

During the second quarter, massive pandemic outbreaks in several major cities severely disrupted business operations across an array of industries. The pandemic also resulted in the cancellation of many qualification exams, affecting demand for our professional certificate courses and leading us to seek other pockets of opportunity to increase profitability in this segment.

Furthermore, amid the complex macro environment, businesses took a more conservative approach in their operations and emphasized cost reduction and efficiency improvement more than ever, with the goal of enhancing their risk resistance. Against this backdrop, consumers were more prudent about purchasing discretionary goods. For example, they may temporarily delay their self-improvement plans within this period.

To combat the lingering external uncertainties in the macro environment, we also prioritized cash flow management and focused on profitability-generating business while continuing to improve our cost efficiency.

Despite that, many people remained enthusiastic about honing their skills, hoping to elevate their overall competence within the highly competitive job market. Others also sought ways to shake off pandemic inertia, such as attending online courses, resulting in surging demand for our skill courses. As such, we seized this opportunity to deliver an enhanced learning experience to our students and developed new skill training courses to address a broader range of student needs, helping our students improve their career flexibility and competitiveness in the job market or turn a skill into a side hustle to see them through tough times.

As a result, our gross billings for professional certification and skills programs in the second quarter grew by 82.9% year-over-year, driven by a 94.9% year-over-year increase in new student enrollments. Net revenues generated by these programs also increased by 30.3% year-over-year.

Furthermore, our extensive course resources, high teaching quality and efficient online learning platform have contributed to improved student satisfaction and stickiness, as well as a higher referral rate. As we continue to optimize our product mix, we will keep developing premium courses covering in-demand skills and general interests, as well as industry-recognized credentials.

With our established brand awareness in this field, diverse course choices, and quality course content, we are confident that we can continue to attract new students and capture additional growth opportunities presented by students' rising demand.

For master's degree-oriented programs, new student enrollments and gross billings decreased on the back of our strategic reduction of marketing activities, and growing market competition as new players try to capitalize on this segment's enormous potential.

Highly-rated teaching staff, which is difficult to replicate for late-comers to the segment, is considered to be the main differentiating factor among industry players. Thus, we believe that our 19 years' experience in exam preparation, experienced and well-received teaching staff and extensive learning resources will position us advantageously compared to our competitors in the long run.

Despite the intense competition and the complex macro environment, we are proud of the critical role that we have played in helping our students achieve individual success in the face of huge economic uncertainty. And we remain committed to doing the right thing to maintain our influence in this field. For example, on June 18, we held our fifth MBA Education Promotion Event, with many top universities in China joining us to share their MBA admissions information. The event was a great success and attracted a huge number of students to participate.

In terms of government policies, we are encouraged by the Chinese government's support of the diverse forms of education, as evidenced by the revised vocational education law adopted during the meeting of the Standing Committee of the [13th] National People's Congress on April 20. This was the first major reform in 25 years since the law was enacted in 1996. It upgrades the status of vocational education in China to be equally important as general education, and encourages collaboration between schools and enterprises while also supporting societal participation in vocational education.

The government is planning to adopt various measures to organize diverse forms of occupational education such as training prior to employment, on-the-job training, re-employment training for the unemployed and other special groups of people, which significantly enhances our confidence in the industry.

We will closely follow the government's policies and will remain steadfast in our contributions to China's efforts to improve its workforce's skills and employment rate through occupational education.

Finally, I am pleased to state that in June, we declared a special cash dividend to share our success with shareholders following 4 consecutive quarters of profitability.

Going forward, we will strive to create additional shareholder value by continuously improving our profitability and cash flow. At the same time, we remain focused on developing diverse skill and interest courses and enhancing our teaching and service quality to attract new students, with the target of bringing life-changing and fulfilling learning experiences to our students.

With that, I will turn the call over to our CFO, Selena, to run through our financials.

Selena Lu Lv: Thank you, Tongbo. Hello, everyone. Our second quarter results were in line with our expectations, with sustained bottom line strength despite the 11.8% year-over-year decrease in net revenues, as we strove for healthy and sustainable growth.

During the quarter, we continued executing various initiatives to build a highly efficient and lean organization while optimizing our expense management, leading to a 32.4% year-over-year decrease in our operating expenses.

Our cost efficiency improvements resulted in notable net income growth from RMB22.1 million for the second quarter of 2021 to RMB114.6 million for this quarter.

Going forward, we are optimistic that our continued efforts to broaden our online course offerings, streamline our cost structure, and dedicate ourselves to providing enhanced services to our students will ultimately enable us to realize long-term growth.

Now let me walk you through some of our key financial results for the second quarter of 2022. All comparisons are year-over-year, and all numbers are in RMB unless otherwise noted.

In the second quarter of 2022, net revenues were 555 million, a decrease of 11.8% year-over-year.

Cost of revenue decreased by 6.2% to 91.2 million in the second quarter of 2022 from 97.3 million in the second quarter of 2021. The decrease was primarily due to the decline in employee compensation expenses related to the cost of revenues.

Gross profit decreased by 12.9% to 463.8 million from 532.2 million in the second quarter of 2021.

In the second quarter of 2022, operating expenses were 351.2 million, representing a 32.4% decrease from 519.6 million in the second quarter of 2021.

Sales and marketing expenses decreased by 34.8% to 293 million in the second quarter of 2022 from 449.1 million in the second quarter of 2021. The decrease was mainly due to, #1, lower spending on branding and marketing activities; and #2, declined compensation expenses related to our sales and marketing personnel.

General and administrative expenses decreased by 9.7% to 46.6 million in the second quarter of 2022 from 51.6 million in the second quarter of 2021.

Product development expenses decreased by 38.3% to 11.6 million in the second quarter of 2022 from 18.8 million in the second quarter of 2021. Product development expenses were mainly comprised of compensation expenses.

Other income decreased by 41.8% to 4.8 million in the second quarter of 2022 from 8.2 million in the second quarter of 2021.

Net income for the second quarter of 2022 was 114.6 million, compared with 22.1 million in the second quarter of 2021.

Basic and diluted net income per share was 16.89 in the second quarter of 2022.

As of June 30, 2022, the Company had 727.5 million of cash and cash equivalents and 138.7 million of short-term investments.

As of June 30, 2022, the Company had a deferred revenue balance of 1,998.1 million compared with 2,348.2 million as of December 31, 2021.

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 0.3 million in the second quarter compared with 7.8 million in the second quarter of 2021.

And now for our outlook. For the third quarter of 2022, Sunlands currently expects net revenues to be between RMB520 million to RMB540 million, which would represent a decrease of 9.3% to 12.6% year-over-year. This outlook is based on the current market conditions and reflects the Company's management's current and preliminary estimate of the 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). Showing no questions at this time, this will conclude our question-and-answer session.

Now, 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.