

**Sunlands Online Education Group [STG]
Q1 2021 Earnings Conference Call
May 25, 2021 8:00 AM**

Executives

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

Analysts

Henry Li, Tree Fund
Phoebe Chen, CDC Capital

Presentation

Operator: Ladies and gentlemen, thank you for standing by, and welcome to Sunlands' First 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' first 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.

On the call, our CEO Tongbo Liu will provide an update on our operational performance, as well as our strategic initiatives. Our CFO Selena Lu Lv will give you an overview of our financial performance, and also provide our guidance for the second quarter of 2021. 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' First Quarter 2021 Conference Call. We are pleased to announce that Sunlands Technology Group had a very strong opening quarter for 2021, starting with net revenues that rose to RMB694.3 million, a 22.9% year-over-year increase. The increase in net revenues was mainly driven by the year-over-year growth in gross billings since the second half of 2020.

Gross billings in the first quarter rose to RMB593.7 million, representing year-over-year growth of 14.9%.

In terms of new enrollments, we achieved a 107.6% increase year-over-year, which surged to over 145,000 students. This solid performance was driven by our continued efforts in diversifying product offerings, raising brand awareness and improving student satisfaction.

Sunlands continues to focus on expanding and refining its master's degree-oriented programs. Because of this strategy, gross billings in master's degree-oriented programs attained a growth rate of 73.6% year-over-year and contributed approximately 34% to total gross billings compared with 22% in the same quarter last year.

New enrollments also grew at a significant rate of 72.8% year-over-year.

Our master's degree programs cater especially to students with full-time jobs, who are more financially stable but have relatively limited time and demand more customized assistance for learning. Students with full-time jobs tend to be more dependable and are more eager to attend online test-prep courses like those offered by Sunlands. We believe this fact, coupled with Sunlands' continued investment in brand awareness and course offerings, will continue to provide thrust for our wider market share.

We also continued to focus on market opportunities for our professional certification and are making significant progress in growing this segment as well. Since the outbreak of Covid-19 last year, people are getting more comfortable attending online classes to improve work-related and hobby-related skills.

Moreover, the employment market is becoming more competitive for employees, and they are feeling the growing sense of urgency to attend professional certification courses with the purpose of maintaining their level of employability.

In addition, the Chinese government also established multiple policies to support the professional certification education such as subsidies, training vouchers and so on. According to the State Council of China, more than 27 million subsidized vocational training opportunities were provided in 2020. We believe these factors will continue to play out in the future and bode well for our professional certification businesses.

While it is encouraging to see such strong growth momentum in both master's degree-oriented and professional certification programs, we remain confident of our STE programs and will continue to fine tune and expand our product offerings.

According to the Seventh National Population Census of China, only 218 million Chinese held an Associate Degree or above, representing a percentage of 15.5% compared to the total population of 1.41 billion in China. We believe STE is still a sizable market that the Company will continue to generate revenue from this industry.

High-level teaching quality is our priority and we are devoted to recruiting first-class teachers with competitive compensation packages. By the end of the first quarter, more than 70% of our teachers held degrees from top tier universities in both China and around the world.

Furthermore, we are committed to building an extensive teacher rating and training system, deploying our database of case studies and templates in teaching, and establishing dimensional teaching channels to ensure top-notch teaching standards. Driven by our efforts in pursuing high-level teaching quality, we are enthused that our students' level of satisfaction has reached a record high according to our internal survey.

Aside from our efforts in upgrading teaching quality, we continue to expand and improve our academic research team, refine our research and development framework for new courses with the assistance of AI technologies, in order to widen our course offerings and accelerate the pace we introduce new courses.

We believe as our academic research team continue to grow, our research personnel will have better opportunities to become more specialized in his or her own academic discipline, which will further enhance the synergies between our existing and new course offerings, and subsequently improve the overall academic research efficiency. We are confident this snowball effect in academic research will pave the way for solidifying our competitive position and strengthening our economic moat in post-secondary education industry.

Looking ahead, we are endeavoring to proliferate our master's degree-oriented and professional skills programs to capture the benefits of economic scale, while solidifying our market-leading position in STE programs. We are devoted to delivering the best learning experience to our students so they can have the best career prospects, while also creating values for all stakeholders.

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. We are pleased to see first quarter net revenues beat guidance once again and hit a record high, as rising brand recognition for our master's degree-oriented and professional skills programs bolstered our top line growth momentum. Our ongoing diversification from STE programs and our commitment to optimizing the student experience affirms our confidence in sustaining this momentum.

We also managed to lower costs, delivering 52.2% and 16.3% reductions in G&A and R&D expenses, respectively. As a result, first quarter net loss narrowed 18.7% year-over-year to 53.3 million RMB. As we look ahead, our marketing department will continue to explore avenues to promote brand awareness, while our sales team will target a higher referral rate and sales

conversion rate to fuel future growth. And most importantly, our management is keeping an eye on implementing optimal strategies that deliver the best returns for all shareholders.

Now let me walk you through some of the key financial results for the first quarter of 2021. All comparisons are year-over-year and all numbers are in RMB, unless otherwise noted.

In the first quarter, net revenues were 694.3 million, an increase of 22.9% year-over-year. The increase was mainly driven by the year-over-year growth in gross billings since the second half of 2020.

Cost of revenues increased by 9.8% to 106.4 million in the first quarter from 96.9 million in the first quarter of 2020. The increase was primarily due to an increase in compensation expenses.

Gross profit increased by 25.6% to 587.9 million from 468.2 million in the first quarter of 2020.

In the first quarter, operating expenses were 666.6 million, representing a 17.4% increase from 567.8 million in the first quarter of 2020.

Sales and marketing expenses increased by 32.5% to 606.4 million in the first quarter from 457.9 million in the first quarter of 2020. The increase was mainly due to increases in, number one, compensation expenses related to our sales and marketing personnel, and number two, spending on branding and marketing activities, including more marketing promotional activities to diversify student acquisition channels.

General and administrative expenses were 42.3 million in the first quarter of 2021, decreasing 52.2% year-over-year, mainly due to the decline in compensation expenses.

Product development expenses decreased by 16.3% to 17.9 million in the first quarter from 21.4 million in the first quarter of 2020. The decrease was primarily due to a decrease in the compensation expenses incurred related to our product and technology development personnel during the quarter.

Other income decreased to 21.3 million in the first quarter of 2021 from 29 million in the first quarter of 2020. The decrease was primarily due to a decrease in value-added tax exemption offered by the relevant authorities as part of the national COVID-19 relief effort.

Net loss for the first quarter was 53.3 million compared with 65.6 million in the first quarter of 2020. Basic and diluted net loss per share was 7.87 in the first quarter of 2021.

As of March 31, 2021, the company had 826.6 million of cash and cash equivalents and 306.5 million of short-term investments.

As of March 31, 2021, the company had a deferred revenue balance of 2,902.5 million compared with 3,024.4 million as of December 31, 2020.

Capital expenditures were incurred primarily in connection with IT infrastructure equipment and the leasehold improvement necessary to support the company's operations. Capital expenditures were 1.7 million in the first quarter compared with 7 million in the first quarter of 2020.

And now for our outlook. For the second quarter of 2021, Sunlands currently expects net revenues to be between 600 million to 620 million, which would represent an increase of 17.1% and 21% year-over-year. This outlook is based on the current market conditions and reflects the company's 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: Thank you. We will now begin the question-and-answer session. (Operator Instructions). 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.

Our first question is from Henry Li from Tree Fund.

Henry Li: (Speaking foreign language).

Selena Lu Lv: (Speaking foreign language).

Tongbo Liu: (Speaking foreign language).

Henry Li: (Speaking foreign language).

Selena Lu Lv: (Speaking foreign language).

Henry Li: (Speaking foreign language).

Operator: [Phoebe Chen] from CDC Capital.

Phoebe Chen: Thanks for sharing because I really didn't get the question from Mr. Li. So I'm not sure if there's any repeated questions. If there is, I'm sorry, my apologies. But I'd like you to probably answer it again in English.

My first question, could you please kindly provide the breakdown of STE and MBA business and other certificate sectors?

My second question, what is the reason that gross billing was lower than net revenue in 1Q21?

Selena Lu Lv: Okay. Maybe I can answer your second question first. In Sunlands, we pre-collect all the gross billings from the students, and we recognize revenues in the following periods. As a result, revenues were not equal to gross billings all the time.

The speed of recognizing the gross billings depends on the mixture of our products. In comparison to the STE programs, the service periods of non-STE programs were shorter. Subsequently, as the

percentage of revenues and gross billings that were generated from our professional certification and master's degree-oriented programs grew higher and higher in the past several quarters, the overall recognition period became shorter. In conclusion, that's why our net revenues were greater than the gross billings in the first quarter of 2021.

Phoebe Chen: Thank you. That has perfectly answered my second question.

Selena Lu Lv: I will now answer your first question. In terms of gross billings, STE, master's degree oriented and professional certification programs accounted for 24.0%, 33.8% and 42.2% respectively. In terms of net revenues, STE, master's degree oriented and professional certification programs accounted for 40.8%, 22.6% and 34.4% respectively.

Operator: Showing no further questions, 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 the earnings conference call. You may now disconnect your lines.