

GSX Techedu Inc.
Third Quarter 2020 Financial Results Conference Call
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Operator

Ladies and gentlemen, thank you for standing by. And welcome to the GSX Techedu Inc. Third Quarter 2020 Earnings Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note this event is being recorded on November 20, 2020.

I would now like to hand the conference over to your first speaker today, Ms. Sandy Qin, IR Senior Manager of GSX. Thank you. Please go ahead.

Sandy Qin

Thank you, operator. Hello, everyone, and thank you for joining us today. GSX's earnings release was distributed earlier today, and is available on the Company's IR website.

On the call with me today are Mr. Larry Chen, GSX's Founder, Chairman and Chief Executive Officer, and Ms. Shannon Shen, Chief Financial Officer. Larry will give a general overview, and then Shannon will discuss the financials. Following the prepared remarks, Larry and Shannon will be available to answer your questions.

Before we begin, I'd like to remind you that this conference call contains forward-looking statements as defined in the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements are based upon management's current expectations and current market and operating conditions, and relate to events that involve known or unknown risks, uncertainties and other factors, all of which are difficult to predict, and many of which are beyond the Company's control, and may cause the Company's actual results, performance or achievements to differ materially.

Further information regarding these and other risks, uncertainties or factors is included in the Company's filings with the SEC. The Company does not undertake any obligation to update any forward-looking statement except as required under applicable law.

As a reminder, this conference is being recorded. In addition, a live and archived webcast of this conference call will be available on GSX Investors Relations website at gsx.investorroom.com. You are also welcomed to subscribe to our quarterly investor newsletters through the same website.

It is now my pleasure to introduce Larry. Larry, please go ahead.

Larry Chen

Thank you, Sandy. Good evening, and good morning to you all. Thank you for joining us today on this earnings call.

We have achieved another robust quarter, with net revenues hitting an all-time-high of RMB 1.97 billion, which is 3.5 times that of the same quarter of last year. We are also pleased to report that our student structure has grown healthier, with net revenues from our primary school became the largest contributor. These outstanding results speak to our continuous focus of providing the highest quality services to students and parents, our consistent training to frontline employees and our unwavering efforts to improve the operational efficiencies and organizational capabilities. In the face of increasingly fierce competition and ever-rising customer acquisition costs, we remain committed to pursuing effective traffic acquisition through high ROI channels, sticking to efficient sales and marketing spending, and to executing an effective growth strategy based on customer lifetime value. This summer we have achieved the highest operating efficiencies in the sector, and we believe we will continue to be so on a full-year basis in 2020. In the meantime, we continued to invest extensively in our teaching staff, product design, content development and technology innovations, raise overall compensation for our tutors and attract more top-tier talents. While it does put pressure on our gross profit and net income over the short term, we view all of this spending as an important investment in our long-term future. Online education is a labor-intensive and talent-intensive industry and leading companies have to manage a huge number of employees. Excellent organizational capabilities will be the key driver for a player to achieve long-term success and be the ultimate winner.

In terms of business model, we chose to focus on the online live large class format in the past and will continue to focus on it in the future. We recently integrated our K-12 business under our Gaotu Ketang brand. Gaotu Ketang fully combines and streamlines our instructors and tutors teams, service standards, products and technologies. Our goal is to deliver the quality of a large class, the learning experience of a small class, and the feeling and educational results of one-on-one tutoring. We believe this integration further demonstrates our dedication to our focused strategy, opens a new chapter of operational efficiency enhancement, and better positions us to capture the enormous opportunities ahead during a coming era of fast consolidation for the online education industry. So far, the integration has exceeded our expectations: the class completion rates and conversion rates are showing significant improvements. Our Genshuixue brand will focus on providing postsecondary education training courses, such as CET, graduate school admission exam and various professional qualification exams.

Some investors may wonder what we think about AI interactive courses. From what we've witnessed, the adoption of artificial intelligence in online education is still only at the buzzword stage. The application of AI in the pre-school market and the synergies created by AI between

the pre-K and K12 markets are still in need of further observation and discussion. Of course, with the advancement of technology, if we can solve some of the basic needs of students through systems and AI, then the varied requirements and personalized demands will be better matched by technology. Hence, as you may see, we have been constantly making efforts to increase our investments in research and technology, with the third quarter's R&D expenses totaling RMB 200 million. However, no matter how technology and AI develops, frankly speaking, I believe the ultimate key to genuinely earn the trust of clients and truly bring meaningful learning results to students is to always try to win over their hearts, to impress and bring warmth to our students, to ignite their interests in learning, to help them cultivate great learning habits and to shape their personalities through our sincere and distinguished services. Regardless of the intense competition today, we still see vast potential in the online education industry and are fully prepared to explore all possibilities based on the solid foundation that we have built over the past years. We are looking forward to generating more value for shareholders and sharing the future of online education with you.

Now, I will pass the call over to our CFO, Shannon to walk you through our financial and operational details.

Shannon Shen

Thanks Larry, and thank you everyone for joining the call.

Now, I will walk you through our operating and financial results, and provide guidance for the next quarter. Please be reminded that all the financial data that I mention will be in RMB terms, unless otherwise noted.

For the third quarter of 2020, we continued to deliver solid results. Net revenues increased by 253% year-over-year to 1,970 million. For the first time, our revenue reached just shy of 2 billion in one quarter, which nears how much we generated for the entire year last year. This helps us rank as one of the top players in the online live large class industry.

This is our 8th consecutive quarter with year-over-year net revenue growth of more than 250%. Net revenues from our online K-12 business grew by 283% year-over-year, which is the 11th consecutive quarter that we have been above 250%. We recorded 2,100 million in gross billings, up by 137% year-over-year. The growth in gross billings was mainly due to our solid recruitment of new students, despite the tough competition. Because of the pandemic, both college and high school entrance exams were delayed, and the timing of the summer holidays in different provinces and cities varied. As a result, the summer vacation in 2020 was shorter than in prior years, which also affected us by reducing one term of our curriculum. Even though this situation was quite challenging, we were able to attract a satisfactory number of new paid course enrollments.

At present, we have set up regional operation centers in 15 cities outside of Beijing. We increased our recruitment and training of high-quality tutors to meet enrollment demands during the summer vacation. We are committed to constantly providing better and more customized learning experiences for parents and students.

In the third quarter, we recorded paid course enrollments of 1,260 thousand, which was up by 134% year-over-year. The number of student enrollments in both regular priced courses and promotional courses continues to set new records, which has led to a huge increase in our brand awareness. The increase in first time users was primarily driven by our effective investments in sales and marketing efforts.

Now, let's break down our operations and financials by business line.

Net revenues from our K12 courses increased by 283% year-over-year to 1,800 million, and accounted for 89% of net revenues. We expect the proportion of K12 revenue will continue to expand as our main source of revenues. Going forward, all K12 related service will be solely provided by Gaotu Ketang brand.

Within the K-12 business, our primary school segment continues to grow at a very high speed, which made it the largest contributor in terms of net revenues. This achievement validates our strategy of prioritizing the primary school market, and demonstrates the effective and consistent execution of our corporate strategy.

Gross billings contributed by K12 courses rose by 141% year-over-year to 1,800 million.

Paid course enrollments for our K12 courses increased by 141% year-over-year to 1,150 thousand. The average selling price per K12 paid course enrollment was around 1,600, compared with around 1,500 in the last quarter and around 1,600 in the same period last year. The quarter-over-quarter increase in the average selling price per K12 paid course enrollment was mainly due to seasonal factors. The year-over-year ASP remains stable, which is what we promised at the beginning of the year because we wanted to consistently provide fair access to high quality education resources across the country. We have always tried to hire the best instructors and the best tutors in the industry so that our students receive the highest quality instruction. Because of this, we have been able to maintain fairly stable ASPs.

Average enrollments per class rose to 2,800 compared with 2,000 in the second quarter of 2020 and 1,400 in the same period of 2019. The significant year-over-year and quarter-over-quarter improvements demonstrate the rapid increase of our enrollment size during the summer vacation. Throughout this summer, our student structure has grown sustainable, with the students of non-graduate grade significantly increased, which lays solid foundation for our future retentions.

Net revenues from our foreign language, professional and interest courses, offered under our Genshuixue brand, were up by 125% year-over-year to 200 million, and accounted for 10% of net revenues.

Gross billings contributed by foreign language, professional and interest courses were up by 135% year-over-year to 300 million.

Paid course enrollments for our foreign language, professional and interest courses increased by 79% year-over-year to 110 thousand.

Gross profit margin increased by around 250 basis points year-over-year to 74%. Non-GAAP gross profit margin, which excludes share-based compensation, increased by around 260 basis points year-over-year to 75%.

Selling expenses increased to 2,100 million in the third quarter of 2020. Within that, expenses for traffic acquisition were approximately 1.5 billion, expenses for branding activities were approximately 58 million, and the remaining expenses cover labor, servers, bandwidth, etc. There was a certain time mismatch between our gross billings and traffic acquisition expenses due to our front-loaded traffic acquisition. In the third quarter, we strategically front-loaded investments of around 200 million in traffic acquisition for the promotional course recruitment for the fourth quarter, which generated no gross billings in the third quarter. This spending, offset by the other around 200 million that we front-loaded in the second quarter, as mentioned in our prior earnings call, resulted in bare changes in the actual traffic acquisition cost for this quarter. Excluding the cost of brand promotion, our Return on Investment (ROI) for pure first-time user acquisition was around 1.3. From various channels feedback, our ROI was still ahead of the industry. We have greatly improved our student structure on several dimensions. Firstly, paid enrollments from lower-tier cities increased to 57% in this quarter, signaling our penetration into lower-tier cities further improved, due to really successful execution of our customer acquisitions strategy in those regions. Lower-tier cities possess large unexploited market, and our higher

growth of paid enrollments in lower-tier cities proves our potential. Secondly, back in the spring semester, a proportion of those enrollments were from short-term or graduate grade courses. Throughout this summer, we significantly increased the size of non-graduate grade students, a.k.a., retainable students. This structure will benefit our future retentions, and greatly help propel our subsequent overall growth. Going forward, we will take an advantage of our strength in operational efficiency and continue to invest in traffic acquisition.

Research and development expenses increased by 286% year-over-year to 200 million. This rise was primarily due to an increase in the number of content professionals and technology development personnel, as well as an increase in compensation for such staff. Our constant investments on research and development is important for our ability to further drive operational efficiency in the future.

General and administrative expenses increased to 200 million from 24 million in the third quarter of 2019. The increase in general and administrative expenses was mainly due to an increase in the number of general and administrative personnel, an increase in compensation paid to general and administrative staff, and an increase in fees for the ongoing investigation.

Interest income and realized gains from investments this quarter from cash, cash equivalents, short-term and long-term investments, 254% to 18 million, from 5 million in the third quarter of 2019. This increase was primarily due to an increase of cash, cash equivalents and short-term wealth management investments, as well as the realization of gains generated from short-term and long-term wealth management investments during the quarter.

As of September 30, 2020, we had cash and cash equivalents, short-term investments and long-term investments of 2,100 million in aggregate, compared with a total of 2,700 million of cash and cash equivalents, short-term investments and long-term investments as of December 31, 2019.

Net operating cash outflow for the third quarter of 2020 was 680 million. The outflow was primarily due to higher marketing expenses paid to improve our market share and brand awareness, an increase in compensation for our fast-growing staff, and increased server and bandwidth expenses to support our rapid growth of students and daily operation activities. Furthermore, an installment of 24 million was paid for our Zhengzhou properties purchases, and we also had 99 million in capital expenditures during the period.

With that, I will now provide our business outlook. Our net revenues for the fourth quarter are projected to be between 2,076 million and 2,116 million, representing an increase by 122% to 126% on a year-over-year basis. These estimates reflect our current expectations, which are subject to change.

Thanks, operator. We are now okay to take questions.

Question and Answers

Operator

(Operator Instructions) The first question today comes from Gregory Zhao of Barclays. Please go ahead.

Gregory Zhao

So my question is still about the market as a competitive landscape, right? So we noticed some private companies, they raised a lot of money in the past 6 months and a lot of the investment has been spent in marketing and user acquisition. So just want to understand GSX's plan and strategy in response to the competition? And how long do you think this kind of competition will last? And also, how shall we think about the market competition, the impact to your student enrollments in subsequent quarters, and we saw the sequential trend of the enrollments is a bit different from the past years.

Larry Chen (Speaking Chinese)

(Translated) Thank you, Greg. When people talk about online education, we say they are the top four companies. And we have seen that in the past several months, there is big changes in the market conditions. And there are some private companies raising a lot of funds.

So if we look at market data, in the third quarter, just look at online live large class, in terms of revenue, we actually ranked the top among the top #4 -- top 4 players. And we know that summer is always a critical moment for new enrollment recruitment across the whole year. So we did strategically expand our investments. During this summer, our sales and marketing spending increased much more compared to the same period last year, but we have to pay attention to the market changes. Through some third-party data, we have heard that there are some players, their summer and marketing study exceeded RMB 4.5 billion. And in terms of ROI, it's very probable, we are still the highest.

According to current market conditions and the funding of each player, we believe, in the year of 2021, this competition still gonna be fierce. And we believe that the peer competition might reach a turning point by the year 2022. So our strategy is always focusing on our customers, focusing on the efficiency and focusing on the continuous improvement of intrinsic metrics. We believe that, as far as we become the company with the highest operating efficiency, the capital will always support us, favor us.

Shannon Shen

Thanks, Greg. And adding to Larry's point, in the short term, the fierce competition seems to bring pressure to a company. However, if we look at, in the long term, the industry position will become more clear after the competition and companies with low operational efficiency will accelerate their cash burning speed. And only the companies with higher operating efficiency will become the final winner. So we think the rule has never changed, when we look at each of the sectors in the TMT business. So -- but we've got a lot of questions about like how to evaluate, which company has the highest operating efficiency. So from our perspective, we think there are

a couple aspects we can testify. So first, financial results is always the most straightforward way to look at a company's operating efficiency.

Since 2017, we have spent basically the least of money, but gain a fairly fast growth speed across the sector. And also, although we have a single quarter of net loss, but if we look across the whole year, we still has the confidence -- we still have confidence that we have a very competitive operating margin. And if -- we are not only -- probably will be one of the very few companies that we still have a -- we will still highly probable to have a positive operating cash flow, if you look at it in a whole year's perspective.

And the second way to testify a company's organizational capability is the team and the organizations. So from our organization point of view, we have always been building and solidifying an exceptional and stable senior management team and middle level management team. This team is a diversified, young and change-embracing team and has a very high sense of identity of our corporate culture.

We all know GSX has been through a lot of things this year and the pandemic and also we were attacked by a lot of short sellers and both being in the dark place, but none of our core management team has left the company voluntarily, except for health reason or turn back to families. And not to mention none of them went to other companies in the industry. So when a company grows really fast, a stable, and a group of people really like the company and willing to contribute their energy and their time to the whole -- to contribute the whole career to the company will be the most valuable asset for us.

And so we have emphasized a lot of times that the online education has a really long service chain, and we need to do better. We need to be good on each of the value chain a couple of times. But the more -- the larger our skills are the more significantly we realize the importance of this perception. For instance, some companies may be particularly good at servicing students in a long-term and normal priced courses but a little bit weak at new students' recruitment. Well, other companies may have advantage on traffic acquisition or traffic tools, but face difficulties to serve their students in long-term courses.

So for us, we remain focused on improving our own organizational capabilities. And we strive for 3% to 5% better on each link of the long value chain. So that's our way to face the competition. And we believe when they are doing the rightful things, the results will turn favorable to us. So we don't have to excessively fix on the external competition.

And in terms of a lot of companies, both from public sector and private sector, has -- do some financing activities. So first, let's look at our cash balance from a historical point of view. So here, by cash balance, it represents a combination of cash and cash equivalents, short-term investments and long-term investments in this call. So our cash balance, by the end of 2018, was only around CNY 236 million. And by that time, we do heard the news that other private companies has raised tens of millions of USD dollars or even USD 500 million or USD 800 million. That's basically 15x or 20x higher than us. But when time comes to the end of 2019, we have grown our cash balance to RMB 2.7 billion. With that, full year operating cash flow contributed CNY 1.7 billion. And with 2019 Q4, the single quarter contributed around CNY 700

million operating cash flow. So from this point of view, our cash accumulation has been very abundant.

And second, if we look at operating cash flow for this year, for the first 9 months, we are in a position of cash, operating cash, net outflow for around RMB 33 million, in RMB terms. But that includes our payment to our independent review. If we remove the payment to the lawyers and the accountants from this pool, because this is not a routine expenses, we still have a positive operating cash flow for the first 9 months, despite such intense competition. And with Q4 coming, we are embracing the biggest retention season in the whole year. And we expect to receive a billion level of cash from retention activity. And this enrollment contributed by retention basically has no investment in sales and marketing activities. So still, at this point, we hold a positive view on our operating cash position across the whole year.

And our cash balance still reduce a little bit compared to the beginning of the year. That's mainly because when we grow really fast, we paid installed payments to our Zhengzhou property purchase. And also, we are opening about 15 operating centers in other cities. Then that needs some payment on decorations and rentals at the first place. And also we execute our share repurchase plan in the second quarter.

So in terms of our operating cash flow, we still hold strong confidence that reflects our organizational capability. And as Larry just mentioned, we believe investors or the markets, they always like companies has the highest operating efficiency. So hope that address your questions. Thanks, Greg.

Operator

The next question comes from Mark Li of Citi. Please go ahead.

Mark Li

I want to ask for this quarter's gross margin. I think we have 2- to 4-point decline, which seems to be -- quarter-on-quarter, what I mean, so seems to be a bit softer compared to Q2 and the last year trend. But I think our ASP and scale also are doing well. So may I know what is the reason for the gross margin? And also, what would we think about the trend going forward?

Shannon Shen

Okay. Thanks, Mark. So yes, our gross margin, last quarter, if we look at the gross margin on a year-over-year basis, it's in an increasing trend, but it slightly decreased on quarter-over-quarter trend. So that's -- the reason is basically because of the seasonality. So when we become -- like when our student base become very large, so the seasonality will show its distinction. So in the third quarter, we provided a large number of promotional classes with limited contribution to revenue. However, in the third quarter, it still incurs day-to-day costs such as infrastructures, networks, fixed labor costs and also to provide a better learning experience and service to our students, especially for the promotional class students. We recruit tutors upfront for about a month to provide training to them and help them prep for fully performing all the tutoring to the students. So that all caused our salary paid to tutors increased a little bit.

And also, in this summer, because I just mentioned like -- because of the entrance exams for both college and high school was a little bit late, that caused some concentration on us when we send learning materials to students. And so that you can see the learning materials cost, as a proportion of revenue increased a little bit as well. So that's the reason why we see our gross margin has a quarter-over-quarter decline. But we do foresee the gross margin will get recovered in Q4. Because in Q4, that's a full season that we provide courses to our students and also like the learning materials distribution will be more even. Thanks.

Operator

The next question comes from Maggie Zheng of Haitong International. Please go ahead.

Maggie Zheng

I noticed there is a quarter-on-quarter decline in the K-12 paid enrollments even though that we have increased selling and marketing efforts, can you explain that? Is it because there were conversion rates or is it because the -- some of the student base was shrunk in this quarter?

Shannon Shen

Thanks, Maggie. So this is also due to the seasonality. So paid enrollment and gross billings for K-12 trial business actually shows distinct seasonality. Typically, most retentions happened in the second quarter and the fourth quarter, while most new student recruitments happen in the first and in the third quarter. So during the third quarter, when majority of the paid enrollments are first-time users, we spent selling and marketing expenses to attract them. So This compares to the second quarter when most paid enrollments come from retention and do not cost too many extra dollars. As such, the third quarter typically shows dipped enrollments but rising selling and marketing expenses.

Same trend from the second quarter goes with the fourth quarter when we may expect most paid enrollments will come from retention. And if we compare the quarter-over-quarter changes and we only look at the first-time users of paying enrollments growth, if we compare our Q2 to Q3, actually, the quarter-over-quarter growth rate was in the range between 55% to 60%. So that's actually an apple-to-apple comparison. And we do recall that this trend actually happened in our -- Q1 in 2020. If we can all recall that, in the last quarter in 2019, we have around 1.1 million of enrollments. That's a great portion that actually came from retention. But when the time comes to the first quarter in 2020, we see a slight decrease in the paid course enrollments. That's also because of the seasonality I mentioned.

So going forward, we foresee that in the fourth quarter, the paid course enrollment will increase significantly, then probably in the first quarter in 2021, that will show a decrease as well. That's all because if we think about -- if we have a really large student base, I'd say, 1 million or 2 million, then the students, they do retention activities at the same time. In the single quarter, they will contribute over 100 million enrollments. And when we only do new recruitments, that needs a lot of efforts to convince students one by one. So that usually and going forward, we will see a quarter-over-quarter decrease on the paid enrollment and gross billing perspective for the first

quarter and the third quarter. And the paid enrollment number and gross billings will be higher in the second quarter and the fourth quarter, that's all because of seasonality. Thanks.

Operator

The next question comes from Felix Liu of UBS. Please go ahead.

Felix Liu

Good evening, management. Thank you very much for taking my question. I hear -- I very much agree what you mentioned during the earnings release that you will focus on LTV-based approach towards selling and marketing. So could you sort of briefly elaborate on that? And just -- I'm wondering how long does a student typically stay with your platform? And what is the lifetime value of that -- of the average student?

My second question is on ROI. I understand definitely you're outperforming the industry peers. Compared with the previous period, your ROI is declining. So are you working on any strategies to potentially improving the ROI compared with the previous periods? Thank you.

Shannon Shen

Thanks, Felix. Thanks for the question. So the market for primary school is still the largest within K-12 sector. So this is a market, we need to put a lot of energy and the best strategy is always to serve parents and students to their best satisfaction. So -- and that's how we can have them stay on the platform a little bit longer or even a lot longer so we can improve the lifetime value of primary students. And only in this way, we may achieve further strategic advancement over the long term.

Specifically, we have enhanced our primary school segment from a few aspects. First, for the teaching quality. We continued to focus on recruiting and develop our teaching talent. So in the past quarter and recently, we have -- there are quite a few top-tier teachers who are loved by parents and holding strong credibility has joined us as instructors. And with them, we have also comprehensively upgraded our primary school curriculum to provide both learning capability-oriented and result-driven course system to students and parents.

And second, from the service end, we paid greater attention to the tutor we recruited to serve the primary school sector. And we provide trainings to them like education psychology to enable them to better serve our students and to know the young generation of parents very well.

And third, from our internet product, we continuously upgrade our live streaming technology to ensure a smooth learning experience. And also, we hired a top notch visual design team to improve our teaching materials in order to enhance the interaction experience.

So with all that improvements we made, we see significant improvement on our primary school retention rate, even though in the just retention period end in the fall, we do see like the retention rate from our primary school sector increased both on a year-over-year basis and a quarter-over-quarter basis. And it is leading all factors. So like you may all know that in the past, like, the retention rate from our primary school sector was a little bit lower than high school and middle

school. And right now, it's already become the top one in our company. So that all shows our strategy on our primary school sector worked very well.

And also that can partially address your second question about the ROI for the sector. So when we put a lot of energy on the primary school sector -- so actually, primary school sector has a lower level of ROI compared to middle school and high school. So when primary school started to become a major revenue contributor, that we do see ROI was a little bit lower than the past quarter. But as I just mentioned, so the primary school students has potentially the largest LTV. So what we need to do is remain focused on the value on the lifetime, not just on just 1 or 2 single quarter. As long as we can help them stay for a longer time that we can bear a slightly lower ROI in the first place. Thanks.

Felix Liu

Thank you. Thank you very much.

Operator

The next question comes from DS Kim of J.P. Morgan. Please go ahead.

DS Kim

Hi good evening. Thanks a lot for taking my question. I have 2. First of all, just a follow-up on your -- just the older question and your point. May I confirm and check if we can still generate positive unit economics from the newly acquired students only excluding the retained and existing student? And if so, what's the lifetime -- the length of the student that you assume in that assumption? That's my first question. And if possible, to follow-up, how does that unit economics changes the student acquired during summer and those that you acquire now given changes in customer acquisition cost? That's the first question.

My second question, if I may, is regarding high level strategy, perhaps for Mr. Chen. Would you consider developing ways to grow and alter organic traffic in the medium term, say, through homework helping app like some of our peers in the top-tier group or some kind of platforms as we did in the past just to prepare for an unlikely bear case scenario where third-party channel becomes way too expensive to even engage. So to have a backup plan of organic pool, would you consider that over the medium term? And by the way, I also noticed that we have acquired Puxin online business recently? And if possible, could you elaborate a bit as to why and rationale. That's it for me. Thank you, management.

Shannon Shen

Thanks, Mr. Kim. So your first question is about -- I think that's a really good question because that's something that is widely discussed in the sector. So that's whether the new students can generate a positive UE because you may get the news from a lot of companies that, saying, maybe the new students, the retention rate is slightly lower than the existing students. So that's why when we think about how to retain a new student in the platform for a longer time. So that's one thing we did very importantly in the summer. So in the summer, we witnessed quite a few companies, they just gave up the summer semester because, as I just mentioned earlier, this

summer vacation is a lot shorter compared to prior years. And actually, the pace of the summer curriculum is a little bit mess because the different provinces open summer semesters at different times. So then we do see a lot of -- like quite a few other players, they just gave up the summer semester then directly they recruit students for the fall semester. But from our experience and point of view, the longer students stay with us, the higher the retention rate it is.

So when we think about the question, we are taking the client's viewpoint -- the client's view more. So that's why we insist on recruiting students from summer and have them to stay with us to complete both the summer semester and the fall semester. Because if you look at the whole curriculum that's more systematic. Only the students that go through the summer curriculum, they can get better results in the fall examination. And we do see this working out when we do the fall semester retentions that the students, they do have a higher level of loyalty that they stay with us. So that's why we do see like our strategy in the summer actually works.

So then your second question is about the organic traffic like homework app. So I may defer this question to Larry.

Larry Chen (Speaking Chinese)

(Translated) So I want to add about LTV. When we talk about LTV, there are 3 important elements: firstly, customer acquisition cost, which means the cost we spend to bring one traffic to regular priced course enrollment. The second factor is gross profit margin. And this metric relates closely to a company's average selling prices and operating efficiencies. So many companies they care about one factor that if they do not also pay attention to the prices and operating efficiencies, their calculation of LTV will differ. The third factor is retention rates. Retention rate is so important. It decides live or death. And every player will calculate their retention rate. So in short, only if we integrate all the 3 elements that will combine to a leverage effect, we will bring us higher LTV and bring the player long-term competitive advantages.

As for organic traffic, I think many players, they are doing similar explorations as for what this product will look like. It depends on in which stage -- in a specific stage, what method this company use will bring them the best customer traffics. And this methodology has to match the stages of their development, has to match the specific features of the organizations and ultimately has to match their operating efficiency. We are still exploring and observing.

DS Kim

Thank you so much for the insights and opinion.

Shannon Shen

Thanks. So your third question was about the potential acquisition you just mentioned like you saw news that we kind of like takeover two of other online schools. Is that your question?

DS Kim

I read an article. News article said that GSX has acquired online arm of Puxin, another listed company a couple of weeks ago. Maybe that was a misinformation, but just wanted to clarify if that was the case, and if we did any investment with Puxin, the NEW U.S. ticker?

Larry Chen (Speaking Chinese)

(Translated) Puxin has similar business model, operations compared to us and we have communications. The ultimate results still depend on further communications. If we have any -- reach any decisions, we will have public announcements. Not the Puxin Group, just Puxin online school.

DS Kim

Thank you, sir.

Shannon Shen

Thanks. Because like for Puxin online like for the whole team that the founder and the management team, they have a very deep experience in the education industry. And they also have some innovative ways to like, acquire new students. That's something we always be humble that we like to learn from, but like -- and also, we are open to all possible cooperation and communications to all kinds of parties. As of now, we don't really have a clear plan about like the potential things that you just mentioned. Then if something substantially happen, we will make an announcement. Thanks.

Operator

The next question comes from Tian Hou of TH Capital. Please go ahead.

Tian Hou

Yeah. Hi, Larry and Shannon and Sandy, I have two questions. it's pretty basic. One is for the -- your elementary, middle school and high school, what is the enrollment composition as well as the revenue composition? That's number one. Number two, what is the average size of the class in Q3? That's the 2 questions.

Shannon Shen

Thanks. So for your first question, because we just mentioned primary school is the biggest revenue contributor this quarter and because the ASP in primary school is a little bit lower than junior high and high school, which basically means the enrollments contributed even more compared to high school and middle high school. And your second question about the average size of class, so in the third quarter, our average size of the instructor's class has reached up to 2,800. Hope that address your questions.

Tian Hou

Yes. Shannon. Thank you.

Operator

The next question comes from Alex Xie of Credit Suisse. Please go ahead.

Alex Xie

Hi, thank you management for taking my question. So I'll ask in Chinese first and then translate myself. (Speaking Chinese)

So my first question is about the organization capabilities. So you always mentioned that this will be your main advantage and main challenges ahead. So would you please elaborate on different aspects of your organization capabilities and what's the change post your organization structure upgrade? And the second question is about your view on the future changes of your product and services. For example, will the services to each of our customers become more intensified, that will become more intense, and will the product portfolio become more diversified?

Larry Chen (Speaking Chinese)

(Translated) Thank you, Alex. So as you know that GSX, we are a pure online player, and we are an independent online education company. Every data metric of our operations, our financials, you can read it into details. And through every data of our company, you can better understand the online education sector. The organizational capabilities is the key competitive strength, a core advantage of our firm.

So GSX, in the first 3 years that we started the company, we have struggled through some darkest moments. And as a result, the people, the staff of GSX, we have like the sense of crisis, we have high standards. We have the self-criticism, and we always review ourselves all these which have all passed down to our bones.

In this -- on the street, people always say the staff of GSX, they look aspirant. And I think it's mainly meaning that our people, we are curious, we are serious. We are all strict, and we always have the aspiration to win the battle. And we actually have embedded all of these values into our daily lives. And those can be figured out in how we recruit talents, how we encourage people and how we kick out people.

Since the September of this year, Genshuixue and Gaotu Ketang, these 2 K12 brands have integrated into new Gaotu Ketang. And through this new Gaotu Ketang brand, we have a larger density of human resources, we have upgraded our talent in technology, in products, in instructors and also in our management team. I believe giving us a little more time, we will see Gaotu Ketang with more competitive and more effective efficient staffs.

In addition, when we mentioned education, the core is not only about teaching, but also about cultivating and training. So we are always looking for the most responsible, the highest quality tutors. As of now, we have recruited near to 15,000 tutors, and this is a guarantee and secure for our future education quality.

And when we mention online education, another key word -- a key word is online. And what the online education wants to solve is, how can we improve the engagements between us and students, improve the interactions frequency and improve the intimacy between students and us. We want to help our students to like us, to believe the education, and they have more motivations. They want to change. They want to improve. This actually closely matches our belief that we want to bring the courses that have the quality of large classes, the learning experiences of small classes and the feelings and education results of one-on-one tutoring services.

Lastly, about the future product mix, the core is always -- we want to meet the demand of customers. And we are currently developing programming courses. Whenever we do some innovative explorations, we try to match it with our current capabilities and our organizational capabilities. Thank you.

Alex Xie

Thank you. Very helpful. Thank you very much.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Sandy Qin for any closing remarks.

Sandy Qin

Okay. Thank you, operator, and thank you, everyone, for joining the call today. If you have any further questions, please don't hesitate to contact us or the company directly. Please feel free to subscribe to our newsletters on the company's IR website at gsx.investorroom.com. Thank you very much.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.
