

**Sunlands Online Education Group [STG]
Q4 and FY 2020 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' Fourth Quarter and Full Year 2020 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 conference over to your host today, Yuhua Ye, Sunlands' IR representative. Please go ahead.

Yuhua Ye: Hello, everyone, and thank you for joining Sunlands' fourth quarter and full year 2020 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 first 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' Fourth Quarter and Full Year 2020 Conference Call. While faced with a year of both unusual challenges and changes, we

concluded 2020 with steady and solid growth in the fourth quarter. We continued our strategic focus on developing diverse product offerings, improving student acquisition efficiency and enhancing curriculum effectiveness, and pursued the opportunities in the market, as overall demand grows for higher education and professional skills programs.

In the fourth quarter, our net revenues reached RMB584.6 million, growing 6.3% compared to the same period of 2019, thanks to enhanced operational efficiency and expanded course categories. Our new student enrollment increased remarkably by 51.8% year-over-year to over 140,000 in the fourth quarter.

The driving force behind the sturdy student growth was our further expansion of course portfolios spanning all of our categories based on the solid foundation of our degree-oriented programs. Our exploration of diverse avenues for user acquisition, as well as enhanced operating efficiency and service quality, also contributed to the strong growth.

Our master's degree-oriented programs continued to yield robust results in 2020. With the COVID-19 pandemic impacting many industries and creating heavy uncertainty in the job market, there has been an increasing recognition of the importance of post-graduate education. The national post-graduate entrance exams for 2021 concluded in December, with registered applicants reaching a record high of almost 3.8 million, and we are well-prepared to handle the growing volume and demand.

As the competition intensifies and admission rates continue to decline, we are seeing more applicants willing to pay for preparation courses. In fact, our master's degree-oriented programs showed strong growth momentum in 2020, with RMB632.9 million in gross billings, increasing 49.5% compared with 2019. This solid performance was a result of our high-quality and tailored courses that helped capture the increasing number of applicants for post-graduate studies who are mostly working professionals.

We are also developing more undergraduate-oriented programs to meet the changing demands of adult education. We offer rich opportunities and various options for people wanting to pursue their undergraduate education later in life. For example, we are adding preparation courses targeting entrance exams for adult universities and the Open University of China in addition to our STE programs, which will further diversify our income sources and consolidate our market position.

The online education has become more accessible and widely accepted in China, and the Chinese government has been supportive of vocational and continuing education. We believe the demand for quality online post-secondary courses will continue to grow, and we are well positioned to seize growth opportunities as we roll out diversified curriculum mix meeting various demands.

In the fourth quarter, we witnessed robust growth as we further developed more professional certification and skills courses. New enrollments in the fourth quarter increased more than 6 times year-over-year, primarily due to the increase in professional skills and general interest courses catering to growing demands for diverse personal education, as well as the low base last year. We developed more general courses helping users cultivate soft skills, interests and

hobbies, as we saw a surge in interest for these courses online, especially during the COVID-19 pandemic.

All these efforts and expansion of course portfolio have paved the way for promising further growth, as we continue to release new courses and programs to satisfy the market demands. With our course portfolio's solid foundation, we can effectively scale up our user base for both existing and new programs to similar fields.

In pursuit of boosting operating efficiency and enhancing curriculum effectiveness, our team further improved our user acquisition and service quality. This enables us to take advantage of rising opportunities in professional certification and skills education.

We further improved our sales efficiency to serve our enlarged product portfolios, and we saw notable increases in the efficiency of our workforce. With rising traffic acquisition costs, we also expanded our sales channels through B2B training services working with corporations and institutions, which began to bear fruit. We are confident that the integration of various channels targeting individual users and corporate customers will further increase our market penetration and user base as well as optimize our user acquisition cost.

With our commitment to offering high-quality online education, we have established procedures to both procure and train first-rate teachers. We have also improved their services to encourage active and participatory learning, which is especially valuable for adult students. In 2020, the number of class participants increased 29.3% year-over-year. In the STE exam held in October 2020, we maintained a high-level pass rate of above 60%, which further cemented our market leadership.

In the fourth quarter, we held our annual teaching contest to motivate teaching improvement. The focus on teaching quality creates a virtuous cycle of academic success, user referrals, user acquisition and then sustainable growth.

In order to assist our experienced teachers and motivate our students further, we applied cutting-edge AI technology into our teaching processes. Our AI system is able to predict students' exam scores based on their practice performance, with an accuracy rate as high as 80%. It can then offer suggestions to help students adjust their study plans accordingly.

We also employed our AI technology to analyze and predict the most frequently tested questions using our vast historical examination database and big data analysis capability. In the fourth quarter, we further expanded our exercises database and increased the number of exam questions to 825,000, representing year-over-year growth of 18.8%.

Heading further into 2021, we will maintain agility and adaptability as we remain committed to enhancing the development and roll-out of top-notch and diversified products and services for adults' continuing education and skills training. We are also keeping a close eye on improving operating efficiency as well as expanding and boosting sales channels.

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. In the fourth quarter, we deepened our strategy to balance business growth and profitability in a challenging environment. Our net revenues continued to grow at a healthy rate, exceeding the high end of our guidance by 4.4%.

As we further improved operating efficiency and optimized costs, our general and administrative expenses in the fourth quarter declined 44.6% year-over-year, which contributed to the significant narrowing of our net loss to RMB73.5 million from RMB139.5 million in the fourth quarter of 2019. Our net loss margin decreased considerably to 12.6% from 25.4% in the fourth quarter of 2019.

Going forward, we will continue to refine our operation and sales execution, as we strive for robust and sustainable long-term growth, in order to consistently create value for our students and shareholders, as well as the broader society.

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

In the fourth quarter, net revenue was RMB584.6 million, an increase of 6.3% year-over-year. Cost of revenue decreased by 3.6% to RMB97.8 million in the fourth quarter from RMB101.5 million in the fourth 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 8.6% to RMB486.7 million from RMB448.2 million in the fourth quarter of 2019.

In the fourth quarter, operating expenses were RMB673.7 million, representing a 12.5% increase from RMB599 million in the fourth quarter of 2019.

Sales and marketing expenses increased by 27.8% to RMB608.5 million in the fourth quarter from RMB476.1 million in the fourth quarter of 2019. 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 promotion activities to diversify student acquisition channels.

General and administrative expenses was RMB54.7 million in the fourth quarter of 2020, decreased by 44.6% year-over-year, mainly due to the decrease in compensation expenses.

Product development expenses decreased by 56.4% to RMB10.6 million in the fourth quarter from RMB24.3 million in the fourth quarter 2019. 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 increased to RMB109.4 million in the fourth quarter from RMB6.9 million in the fourth quarter of 2019. The increase was primarily due to the value-added tax exemption of RMB77.5 million offered by the relevant authorities as part of the national COVID-19 relief efforts.

Net loss for the fourth quarter was RMB73.5 million compared with RMB139.5 million in the fourth quarter of 2019.

Basic and diluted net loss per share was RMB10.87 in the fourth quarter of 2020.

As of December 31, 2020, the company has RMB760.7 million of cash and cash equivalents and RMB517.8 million of short-term investments.

As of December 31, 2020, the company had a deferred revenue balance of RMB3,024.4 million compared with RMB3,228.8 million as of December 31, 2019.

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 RMB4.7 million in the fourth quarter compared with RMB10.4 million in the fourth quarter of 2019.

For more of our 2020 full-year financial results, please refer to our earnings press release for further details.

And now for our outlook. For the first quarter of 2021, Sunlands currently expects net revenues to be between RMB670 million to RMB690 million, which would represent an increase of 18.6% and 22.1% year-over-year. This outlook is based on the current market conditions and reflects the company's management's current and preliminary estimate 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]. Showing no 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 line. Thank you.