

**[TME] - Tencent Music Entertainment Group
Q1 2021 Earnings Conference Call
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Officers

Millicent T., IR
Cussion Pang, Executive Chairman
Ross Liang, Chief Executive Officer
Tony Yip, Chief Strategy Officer
Shirley Hu, CFO

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Operator: Ladies and gentlemen, good evening and good morning, and thank you for standing by. Welcome to the Tencent Music Entertainment Group 2021 First Quarter Earnings Conference Call. Today, you will hear discussions from the management team of Tencent Music Entertainment Group followed by a question-and-answer session. Please be advised that this conference is being recorded today.

Now I will turn the conference over to your speaker host today, Ms. Millicent T. Please go ahead.

Millicent T.:

Thank you, Amanda. Hello, everyone, and thank you all for joining us on today's call. Tencent Music announced its quarterly financial results today after the market close. An earnings release is now available on our IR website at ir.tencentmusic.com as well as via IR newswire services. Today, you'll hear from Mr. Cussion Pang, our Executive Chairman, who will start the call with an overview of our recent achievements. He will be followed by Mr. Ross Liang, our CEO, and Mr. Tony Yip, our CSO, who will offer more thoughts on our product strategies, operations and business developments. Lastly, Ms. Shirley Hu, our CFO, will address our financial results before we open the call for questions.

Please note that this call may contain forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on management's current expectations and observations that involve known and unknown risks, uncertainties and other factors that not under the management's control, which may cause actual results, performance or achievements of the company to be materially different from the results, performance or expectations implied by these forward-looking statements.

All forward-looking statements are expressly qualified in their entirety by the cautionary statements, risk factors and details of the company's filings with the SEC. The company does not assume any obligation to revise or update any forward-looking statements as a result of new information, future events, changes in market conditions or otherwise, except as required by law.

Please also note that the company will discuss non-IFRS measures today, which are more thoroughly explained and reconciled to the most comparable measures reported under the International Financial Reporting Standards in the company's earnings release and filings with the SEC. You are reminded that such non-IFRS measures should not be viewed in isolation or as an alternative to the equivalent IFRS measures, and other non-IFRS measures are not uniformly defined by all companies, including those in the same industry.

With that, I'm very now pleased to turn over the call to Cussion, Executive Chairman of Tencent Music. Cussion?

Cussion:

Thank you, Millicent. Hello, everyone, and thank you for joining our call today.

Echoing the reorganization of the Tencent digital content ecosystem and expediting TME toward the next phase of development, we recently announced a change of leadership. As Executive Chairman of TME, I will be responsible for setting our long-term strategy, and TME's overall coordination and management of the Board and also the Company. I will also focus more on building the most comprehensive music and audio content ecosystem in China.

Also joining us on today's call is Mr. Ross Liang, TME's new CEO who will oversee QQ Music, Kugou, Kuwo, WeSing and long-form audio business.

Having worked closely with Ross for a number of years in the past, Ross and myself share the same vision in TME's strategic goal. As the GM of QQ Music from 2014 to 2016, and one of the key members of WeSing's founding team, Ross has a deep understanding of the nature of our businesses. A warm welcome of Ross back to the TME family, and I look forward to working with him again as we continue to execute our strategy and grow the business.

Since TME's establishment in 2016, we have stayed true to our original aspiration of creating more value for users, musicians, the industry, and society as a whole.

We pioneered and advanced a model benefiting for the long-term development of China's music and entertainment industry. Our established and comprehensive services now include online music, online audio, and social entertainment, positioning us as an **all-in-one music and audio entertainment destination for hundreds of millions of users**.

We are not only great believers in upholding digital music copyrights, but also strong advocates for effectively raising income levels for China's indie musicians and cultivating China's original music ecosystem.

We have been pushing the boundaries of the music entertainment ecosystem, committing to explore innovative ways to promote upstream content production. This has resulted in numerous chart-topping songs originating from our platform, alongside our growing capabilities in artist incubation and additional channels for distribution and promotion. We also pioneered TME Live, which has earned a solid standing in the industry.

Although the impact of the COVID-19 pandemic still lingers and some uncertainties remain, China's music industry is thriving and flourishing. With a steadfast focus to create a one-stop shop online music and audio ecosystem, we will unite our efforts to drive the next phase of development for TME.

Moving to the quarterly discussions. In the first quarter of 2021, we achieved robust performance with 24% YoY growth in total revenues, while hitting multiple milestones across the spectrum of our business.

- Net addition of music paying users reached a **record high of 4.9 million** in the first quarter, demonstrating our strong momentum and further inspiring us to unlock the value of music and elevate its role in people's lives.
- For our long-form audio business, we have also made significant breakthroughs, with **MAUs surpassing 100 million** at the end of 2020, and **MAU penetration crossing the 20% milestone** in the first quarter of this year, making us one of the leading players in China's online audio industry.

Our content ecosystem is becoming increasingly robust, dynamic, and powerful. In the past quarter, we were very excited to see increasing user engagement from young users, thanks to a broader offering of genres such as hip-hop, Chinese ancient style and music for a wide range of entertainment including popular television programs, variety shows and online games, through both licensing or self-production.

Also, in the hip-hop category, QQ Music launched the Rappers' Alliance in January, attracting participation from both uprising and top-tier established rappers. By providing a stage to perform and shine, we helped rapper Lambert (凌杰) be enlisted by "The Treasured Voice (天赐的声音)", a well-recognized music variety show in China. These efforts have brought increasing engagement from young users, and on QQ Music, the

penetration of young users among hip-hop listeners is more than 15 percentage points higher than their overall platform presence.

As another example in the first quarter, we worked with Tencent Games to create the highly praised theme song "Battle For Glory" for "PUBG Mobile," one of the most popular mobile games in the world. In 2021, as an essential component of Tencent's platform and content group, we plan to strengthen and develop additional ways through collaboration with the broader Tencent ecosystem.

Cultivating indie musicians is another strategic tenet of ours. In the first quarter, the scale of the Tencent Musician Platform, as indicated by the original songs uploaded, continued with industry leading growth. On a year-over-year basis, the number of artists on our Tencent Musician Platform more than doubled to over 200,000, and the music streaming volume of Tencent musicians witnessed an increasing share in our platforms on a sequential and year-over-year basis. This demonstrates musicians' trust in our promotional capabilities, platform support, incentive plans and other comprehensive services, as well as our ability to drive influence in the industry by successfully incubating and promoting hit original songs.

Tencent Musician Platform also serves public welfare with its social influence. For example, it cooperated with a leading logistics company, using music to promote the revitalization in the Southwest of China, namely, Sichuan, Guizhou and Yunnan provinces.

Also, we further expanded our content ecosystem to live concerts. **TME Live** celebrated its first anniversary in March this year. In just a year's time, it hosted 60 live concerts for over 100 artists, with 18 billion social buzz, building and cementing TME Live's strong industry influence as a brand.

In 2021, we will innovate more interactive features such as ticketing, VIP privileges, reserved camera, and virtual gifting, to create a holistic and more immersive user experience that will get us one step closer to unlocking the massive value and market potential for online live performances.

Apart from music content, **long-form audio** forms a core building block for us as we evolve into a leading all-in-one music and audio entertainment platform in China. We emerged as a key player in China's fast-growing long-form audio market.

Firstly, we provide **a broad spectrum of audio categories**, expanding into diversified audio genres such as drama, comics, Chinese comedy, history, parenting, relationship and education, among others. The consolidation of Lazy Audio in March further allowed us to gain access to an extensive library of high-quality audiobooks. In the first quarter, licensed titles more than quadrupled year-over-year. We are also accelerating the addition of PUGC and UGC long-form audio content, bringing both professional and long-tail podcasting content to users. Our initial efforts have included QQ Music's in-depth collaboration with Xiaoyuzhou, a leading podcasting app in China. In February, QQ

Music initiated the Ground Zero Podcast Program, under which we aim to continue introducing various features and widening support to facilitate podcast creation.

Secondly, our adoption of a **valuable two-pronged product strategy** evolves to unlock significant value from our music and standalone long-form audio applications. This approach allows us to leverage our massive music user base, and nearly quadruple our long-form audio MAU penetration to 20% in the first quarter, compared to 5.5% for the same period last year. Long-form audio content also contributes positively to time spent per user. It inspires incremental listening of audio content in addition to music, and newly converted audio users stream even more music content than before. Our standalone application launched in April, Lanren Changting, pioneers a well-rounded visual and audio experience through comics, surround sound and bullet chats to offer an immersive and interactive user experience, and aim to address the needs of heavy audio users.

Lastly, we commenced **ad-based monetization**, which gives our users easy access to a vast amount of high-quality audio content. Users are able to gain membership privileges or title rights by watching advertisements or completing certain tasks. We believe that such a model will not only be effective in scaling our user base quickly, but also unlocking additional monetization methods. China's long-form audio market remains extremely underserved as compared to the online music and video market, and we are eager to continue cultivating users' listening habits to ultimately accelerate the penetration of online audio in China.

Now, I would like to pass the call to Ross, who will share more about the strategy of our key business lines. Ross, please go ahead.

Ross:

Thank you, Cussion. Hello, everyone.

I want to start off by saying how excited and honored I am to join TME as CEO. I see tremendous strength and future upside potential in TME, particularly with its leadership in driving industry growth, its innovative business models, and last but not least, its remarkable team consisting of a talented group of people in the industry.

I firmly believe the pandemic has changed, and continues to change, the content distribution and user interaction within online music industry in China. And TME, from a position of strength, is at the forefront of this paradigm shift.

Leveraging the growing momentum of the visualization and socialization of music platforms, we plan to launch the **TME Video Account** to further strengthen the interactions between artists and fans. We see significant upside to music-centric social activities through the cultivation of private domains for musicians and a boost of music content promotion on each social platform.

We will pool and streamline resources, enhance **middleware and architecture** sharing among all our online music services, to pursue R&D and technology breakthroughs. As we harness cutting-edge technologies and innovate operation models, we endeavor to provide a more immersive online karaoke and concert experience, making virtual reality as real as the offline experience and potentially better.

Our **multi-product portfolio** puts us in a strong position to offer differentiated services for the diverse and nuanced needs for users nationwide: with QQ Music cementing its position as a young and trendy brand, and Kugou Music serving a diverse user base by offering multiple versions customized for different verticals of target audience such as children, silver and senior citizens. Kuwo Music will focus more on catering to users' intrinsic demand of music streaming and providing a superior experience with easy-to-use music streaming features.

We will also establish a tighter and more seamless **collaboration with Tencent's strong product portfolio** to enhance music content promotion. By working more closely with the broader Tencent ecosystem, we will explore interactions between music and social platforms, innovate content production and artist incubation with digital content platforms, and promote the development of long-form audio leveraging our partnership with online literature platforms. We are dedicated to harnessing the power of music while opening up more monetization opportunities.

We will also be stepping up our efforts on international expansion and have appointed the Group Vice President Dennis Hau to lead this effort. Dennis was previously in charge of the operations and management of QQ Music. Under his leadership, QQ Music successfully launched Putong Community to enhance social interaction between music fans and their idols, developed industry leading music discovery prediction technology and substantially strengthened promotion capabilities for trending hit music. With the support of Dennis and a deep bench of senior managers, and leveraging my prior experience with QQ Music and WeSing, I will personally take on a more active role in driving the growth of QQ Music and WeSing.

I look forward to working in close partnership with Cussion and side by side with other TME management members, staying laser-focused on efforts to enhance product features and services to elevate the user experience.

Now I would like to turn the call over to Tony who will discuss business highlights and important areas of focus. Tony, please go ahead.

Tony:

Thank you, Ross. Hello, everyone.

I will first talk about the key operational and financial performance during the first quarter.

Online music services growth rate continued to accelerate for two consecutive quarters. We delivered another strong quarter for subscription business, with a record-high net adds of 4.9 million online music paying users. The strong subscriber growth was primarily driven by better content offering, effective marketing campaigns and improving retention rate.

We also made notable progress in advertising within online music services. Advertising revenues more than doubled year-over-year in the first quarter, for the third time in a row, as we benefited from an increasing number of advertisers from various industries attracted to our platform, as well as triple-digit YoY growth in ad inventory and double-digit YoY ecpm growth.

We also continued to innovate with advertising products to further tap into the growth potential for advertising. In 2021, we are focusing on developing creative advertising solutions, and enhancing in-house capabilities to further boost our advertising revenues and complement subscription model.

Online music mobile MAUs were 615 million in the first quarter. While there are some churn of casual users resulting in a year-over-year MAUs decline, our total music user time spent was up YoY, demonstrating the increasing engagement of our core users.

In terms of expanding our services beyond the mobile phone, we continue to broaden our services to (Internet of Things) **IoT space** and find more and better ways to interact with our users. Opportunities arising from the IoT market are exciting and we are actively expanding use cases for users to enjoy all our services. We will continue to solidify our leading position through extensive cooperation with mainstream automakers, smart speakers, television and other connected device manufacturers. In the first quarter, our IoT MAUs were 69 million, representing an increase of 50.0% year-over-year. The IoT market will serve as a new distribution and promotional channel, as well as serving as a potential additional driver for future subscription growth.

Moving to visualization and socialization, our concerted efforts to enrich both music and audio content offering as well as enhanced innovative features and services, such as music community and video content, have helped us gain higher mindshare among our users, illustrated by 10% YoY growth in average daily time spent per mobile user in the first quarter.

For Putong Community, we introduced more social scenes such as synchronized music and podcast listening, video and concert watching, as well as improved private messaging, catering to our users' needs for interactive social connections. As a result, DAU penetration and retention rate of Putong Community both increased steadily.

Kugou Fans Club, another community on our platform, has also drawn many leading artists, labels and content IPs. Highly rated and domestically produced animation series, Scissor Seven (伍六七) is a recent example. Fans Club is becoming a well-loved

destination for young generation, evidenced by an increasing proportion of young users, and its time spent per user increased sequentially in the first quarter.

Now let's turn to our **social entertainment services**. In the first quarter, we delivered solid performance.

Both online karaoke and live streaming delivered steady year-over-year growth. Our strategic shift to focus on monetization efficiency gain has continued to lead to strong advertising revenue growth for WeSing. QQ music live streaming gathered further momentum during the quarter and we are on track to scale it up over the course of 2021. Social entertainment MAUs improved quarter-over-quarter to 224 million, as user base of QQ music live streaming ramped up and our efforts to invigorate content ecosystem and enhance social attributes for WeSing took place. Paying users of social entertainment services also sequentially recovered to 11.3 million in the first quarter by 4.6%.

Our **online karaoke services** strengthened its core singing and entertainment functions with material improvement in monetization through advertising. Our concerted efforts to make the experience more immersive and fun through video enrichment, personalization, and community resulted in sequential improvements in users' willingness to sing and record, and further content distribution, driving an increase in average daily time spent within WeSing, and also daily active users bottoming from the last quarter.

With the dual approach in splash screen ads and news feed ads, advertising revenues for WeSing more than doubled year-over-year in the first quarter, making it a more meaningful revenue stream of WeSing. For the remainder of 2021, we expect strong advertising revenue growth to continue and become an important topline driver for social entertainment services.

For **music-centric live streaming services**, through efforts such as full screen live streaming and category expansion for content of ACG, gaming, Chinese ancient style, and dancing, we maintained a healthy interactive ecosystem as evidenced by steady quarter-over-quarter improvement of retention rates for performers and users.

The closed-loop ecosystem between online music and music-centric live streaming have been demonstrated by higher streams of Chinese ancient style during the quarter. Inspired by the increasing trend of this genre on our online music services, Kugou Live hosted the live show "Chinese Ancient Style for Today (现在国风)", for more than 80 groups of Chinese ancient style singers, further integrating Chinese traditions with a modern twist. This show in turn led to 17% higher streams of music by the participated singers during the days of this event.

In conclusion, we kicked off 2021 with a firm step forward in our evolution into an all-in-one online music and audio entertainment destination in China for users and artists.

With that, I would like to turn it over to, our CFO, Shirley Hu, for a closer review of our financials.

Shirley:

Thank you, Tony. Hello everyone.

Next, I'll discuss our results from financial perspective. Overall, we achieved outstanding growth in online music services, particularly in music subscriptions and advertising revenues this quarter, and continued healthy growth in social entertainment businesses.

Total revenues for Q1 2021 were RMB7.8 billion, up 24% year-over-year. Our online music revenues reached RMB2.7 billion this quarter, up 35% year-over-year.

Our music subscription business continued to grow rapidly in the first quarter of 2021 with revenues of RMB1.7 billion and year-over-year growth of 40%. We had a record high net adds of 4.9 million in Q1 2021 and paying users grew 43% year-over-year, driven by user retention improvements and higher new adds of paying users, while monthly ARPPU remained relatively stable year-over-year. These were resulted from our continuous improvements in products and contents, expanded sales channels and efficient promotions. And we are very pleased to see that our efforts started bearing fruits and the value of quality music is increasingly recognized by our users.

In addition, on a year-over-year basis, our advertising revenues were more than doubled again for the third consecutive quarter, due to increased ad availability and eCPM improvements. We also enhanced our products to improve ad efficiencies and better serve our customers. Over the past year, we have made various efforts in expanding and educating our customers for their consumption habits and stickiness. As a result, both our customer number and average spending per customer have expanded year-over-year.

Social entertainment services and other revenues were RMB5.1 billion, up 19% year-over-year, driven by growth in revenues from live streaming and advertising services on our social entertainment platform. Social entertainment monthly ARPPU increased 36% while paying users dropped 12.4% on a year-over-year basis. Live streaming revenues had a relatively higher growth year-over-year as we had a lower base in Q1 2020 due to the impact from COVID-19 and adjustments to interactive features. Additionally, our improved ad business model on social entertainment provided more and better ad products on our platforms, resulting in significant growth in ad revenues on our social entertainment platform

Gross margin was 31.5% in Q1 2021, up 0.2% year-over-year and down 0.8% sequentially. Year-over-year increase was due to rapid growth in subscription revenues and advertising revenues. Sequential decrease in gross margin was because social entertainment revenues and advertising revenues were seasonally lower in the first quarter of 2021.

Now moving on to operating expenses. Total operating expenses for Q1 2021 were RMB1.6 billion and was 20% as a percentage of total revenues, as compared to 18% in

the same period last year. Selling and marketing expenses were RMB672 million, up 40% year-over-year. The increase was due to higher user acquisition expenses to enhance our products long-term positioning and spending related to our legacy TMEA event in January. The increase was also because we had a lower base in Q1 2020 as we reduced spending on user acquisitions during pandemic. General and administrative expenses were RMB883 million, up 30% year-over-year, driven by higher number of employees in R&D as we invest in product enhancement and technology innovations such as long-form audio, WeSing International version, content library technology, etc.

Our effective tax rate for Q1 2021 was 11.5%.

Our net profit was RMB 979 million and net profit attributable to equity holders of the Company was RMB926 million. Non-IFRS net profit was RMB 1.24 billion and non-IFRS net profit attributable to equity holders of the Company was RMB1.18 billion. non-IFRS net profit margin was 15.8%.

As of March 31, 2021, our combined balances of cash, cash equivalents, term deposits and short-term investments were RMB27 billion, representing a decrease of RMB2 billion from Q4 2020. The decrease in balances was primarily due to acquisition of Lazy audio, investment in a consortium to purchase additional equity interest in Universal Music Group, as well as repurchase of ordinary shares. Cash generated from operating activities had a positive impact on the combined balances.

Looking forward, we'll continue to invest in core content investments to further increase recognition of the value of quality music by our users and will keep focusing on new products and features such as long form audio. We are optimistic about the future of the broader music and audio industry and are confident in the overall ecosystem and product pipelines that we are building in the long run.

This concludes our prepared remarks. Operator, we are ready to open the call for questions.

Operator:

We are now approaching the end of the conference call. I will now turn the call over to your speaker host today, Ms. Millicent T., for closing remarks.

Millicent:

Thank you, everyone, for joining us today. If you have any further questions, please feel free to contact TME's investor relations team. This concludes today's call, and we look forward to speaking with you again next quarter. Thank you, and goodbye.