

Tencent Music Entertainment Group Second Quarter 2024 Earnings Conference Call Script

Millicent T.:

Good evening, good morning, and welcome to Tencent Music Entertainment Group's Second Quarter 2024 Earnings Conference Call. I'm Millicent Tu, Head of IR. We announced our quarterly financial results earlier today before the US market opened. The earnings release is now available on our IR website and via PR Newswire services.

During today's call, you'll hear from Mr. Cussion Pang, our Executive Chairman, and Mr. Ross Liang, our CEO, who will share an overview of our company's strategies and business updates. Then Ms. Shirley Hu, our CFO, will discuss our financial results before we open the call for questions.

Before we continue, I refer you to the Safe Harbor statement in our earnings release, which applies to this call as we'll make forward-looking statements. Please note that we will discuss non-IFRS measures today, which are more thoroughly explained and reconciled to the most comparable measures reported under IFRS in our earnings release and filings with the SEC.

All participants are muted at this time. After management's remarks, there will be a Q&A session. And please be advised that today's call is being recorded.

With that, I'm pleased to turn the call over to Cussion, Executive Chairman of TME. Cussion?

Cussion:

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

We are excited to report another solid quarter, underpinned by a 28% year-over-year growth in online music services as well as a 26% year-over-year increase in adjusted net profit. The outstanding net addition of over 10 million music subscribers in the first half of 2024, coupled with a rise in ARPPU, once again demonstrated our strong ability to break new grounds within China's streaming landscape. We remain optimistic about the music industry's long-term potential and are committed to our mid to long-term goals. In the meantime, we are constantly adjusting ourselves to better adapt to changing external environments, evolving user mindsets and our different business development stages to continuously innovate and achieve sustainable growth, at a healthy pace and with the right balance.

Let me now share some recent highlights on our expansive content ecosystem, which is getting increasingly rewarding:

- 1) First of all, we continued to expand and reinforce partnerships with artists and record labels to enrich our music library, and to bring the best content available to our

users. Our long-standing and extensive win-win partnerships with music labels enable us to secure more content-centric privileges for users, including but not limited to early access to the latest hits. This quarter, we extended our collaborative licensing agreements with some well-known Chinese bands such as Sodagreen (苏打绿), and a top Korean label, CJ ENM, which represents the highly popular K-pop boy band ZEROBASEONE. All these contract renewals include a 30-day head-start privilege of their new songs. Overall, we are pleased to see that such privilege has effectively improved membership conversion and engagement.

2) Second, we continued to explore more engaging ways for users to enjoy music. During the quarter, we combined proprietary fan-artist interaction benefits, such as live video calls, with digital album releases, and effectively increased sales. “Shenself (反深代词)”, the new digital album of a popular Chinese singer, Zhou Shen (周深), is a recent success. It features artist-themed in-App decorations and virtual souvenirs, and exceeded 1 million copies in sales within three months of release, ranking as the top-seller year-to-date on our platform. We’ve also seen solid digital album sales results from other artists, such as Chinese singer Lay Zhang (张艺兴) and the popular K-pop girl group, aespa.

3) Third, as the demand for offline live performances continues to surge, we stepped up our efforts to host concerts and music festivals with more value-added services.

In July, we hosted our upgraded flagship annual event, TMEA (Tencent Music Entertainment Awards) 2024, in Macau. We broadened our horizons this time, featuring A-list domestic singers and rising musicians, as well as international idols. Notably, over 60 household names including Zhou Shen (周深), TIA RAY (袁娅维), Jane Zhang (张靓颖), and a K-pop girl group BABYMONSTER performed at this year’s event. TMEA 2024 sparked billions of social media buzz, showcasing our elevated industry influence. We are also bolstering our capabilities to organize large-scale concerts for top-notch singers. For instance, we hosted TIA RAY’s landmark concert tour and helped her achieve a milestone of over 10,000 attending fans. We are happy to see a significant year-over-year growth in our revenues from offline performances in the second quarter.

This quarter, as a new initiative, we customized event-themed artist merchandise for Karen Mok’s (莫文蔚) concert with head-start sales on our platform. We also provided our subscribers with member-only access to the online premiere concert of a popular Chinese band Teens In Times (时代少年团) as a remarkable benefit.

4) Fourth, our self-produced content continued to win popularity and boost user conversion. We strategically leveraged our extensive resource advantage in TV, film IPs, and artists to elevate production, promotion and success of our self-produced content. For example, we invited popular artists Zhou Shen, Kenji Wu (吴克群) and MIKA to perform the original soundtracks (OSTs) for Tencent Video’s blockbuster TV series Joy of Life 2 (庆余年第二季) and The Tale of Rose (玫瑰的故事). These self-produced songs amassed over 200 million streams in total on our platform within 3 months of debuts,

ranking top 3 on OST charts year to date.

In addition, our self-produced pop songs "Heard of You (听说你)" and "Who Am I (何物)" went viral on short video platforms soon after being featured on the national music variety show "The Treasured Voice Season 5 (天赐的声音第五季)", which significantly boosted streams on our platform.

Our high-quality original content, combined with unique fan-artist interactions, fulfils diverse music tastes and entertainment needs, fostering an increasingly dynamic content ecosystem.

We always strive to inspire society and share our love through music. In the second quarter, we jointly launched another "Little Red Flower Concert" with Tencent Charity, partnering with volunteer artists and teachers to support local education for children in rural areas through online and offline performances. We amplified its online reach and social influence this time by deeply collaborating with Weixin Video Accounts to livestream the concert.

In summary, we recorded solid second quarter performance, finishing the first half of the year on a strong note, both operationally and financially. We believe the power of our platform, the value of premium music content and expanding member privileges will have a snowball effect, leading to a healthy and sustainable growth. Guided by a long-term view, our goal is to lay a solid foundation for future progress and to promote the vibrant, win-win development of the industry.

Now I would like to turn the call over to Ross for more details on our overall platform development. Ross, please go ahead. Thank you.

Ross:

Thank you, Cussion. Hello, everyone.

Our focus on user-centric innovation has effectively increased music subscribers and enhanced retention during the quarter. This reflected our ongoing efforts to advance our product and services, especially the focus on the higher-value subscription plan, the Super VIP membership. Our approach to continuously delight users keeps us at the forefront of the streaming industry.

A few quarterly highlights to share:

- 1) First, we further enhanced sound quality and effects as part of our premium offerings. For example, QQ Music upgraded its self-developed AUDIO 3D 2.0 ("臻品全景声 2.0") and Kugou Music launched Viper Ultra Sound ("蝮蛇超清音质"), both featuring ultra-clear sound quality. We also presented users with new ways to enjoy the music, including sound quality for certain high-end headphones and playlists with best-in-class audio quality. These improvements have led to not only higher user adoption but also

increased music consumption.

2) Second, to meet users' personalized needs, we've launched a series of benefits, including customized players and ringtones based on well-known IPs and artists. These features resonate with users' desire for self-expression, and proved effective in user conversion and retention.

3) Third, our premium SVIP membership is gaining more traction. Empowering a holistic and seamless listening experience across various devices and multiple scenarios, SVIP integrates music with long-form audio and online karaoke services, all with superior sound quality. It wins the hearts of our highly active members with comprehensive online and offline privileges, such as priority access to digital albums and ticket booking for live music events including our TMEA. We are pleased with the early progress of SVIP membership adoption and are looking forward to sharing more exciting news down the road.

Next on more personalized music discovery and optimized listening experiences.

A few key projects to spotlight:

1) We upgraded our recommendation middleware across our music apps, enabling users to discover songs better cater to their tastes. During the quarter, nearly 40% of streams were generated from recommendations. With our evolving large audio models, we continue to empower more efficient music distribution and the discovery of new and long-tail content.

2) We also elevated our platform's overall experience with AIGC applications. For example, we introduced data-saving AI-enhanced SQ Lite Mode (无损省流模式) while preserving superior sound quality, and Kugou Music's virtual DJ features and QQ Music's 3D Avatar offer users a sense of companionship.

3) On the visual side, we refined our streaming UI design to offer a more inviting and effortless experience. For example, QQ Music launched an industry-first multi-device matching playback feature and a compact, half-screen music player. Users can now enjoy seamless music streaming when switching across different devices and applications.

4) Last but not least, we further expanded our rewards program to include more benefits, such as artist merchandise. Its growing popularity among users has effectively boosted music content consumption and increased user engagement.

To sum up, all the above efforts contributed to higher stickiness on our platform, as reflected by both year-over-year and quarter-over-quarter increases in time spent per user in the second quarter.

Moving forward, we are committed to offering more compelling services that better align with the needs of diverse music lovers, ultimately expanding our paying user base and

increasing user loyalty.

With that, I would like to turn the call over to Shirley, our CFO, for a deep dive into our financials.

Shirley:

Thank you, Ross, and greetings to everyone.

I will now turn to our financial results. Our effective monetization of online music services and operational efficiency management continued to drive strong financial results in the second quarter of 2024. IFRS net profit increased by 33% year-over-year to RMB 1.8 billion, and non-IFRS net profit rose by 26% to RMB 2 billion.

Our total revenues were RMB7.2 billion, down by 2% year-over-year. Revenues from online music services had strong growth, largely offsetting the decline in revenues from social entertainment and other services.

In the second quarter of 2024, our online music revenues increased by 28% to RMB 5.4 billion on a year-over-year basis. This increase was driven by the strong expansion of our music subscription revenues, supplemented by growth in advertising revenues, as well as growth in revenues from offline performances.

Music subscription revenues in the second quarter of 2024 reached RMB3.7 billion, marking a 29% increase year-over-year and a 3% rise sequentially. Monthly ARPPU was 10.7, up from 9.7 in the same period last year. The number of online music paying users were 117 million, representing a 18% increase year-over-year with quarterly net adds of 3.5 million paying users. With a large scale of music subscribers, our focus is to manage music subscription revenue growth with the right balance and pace to achieve growth in both subscribers and monthly ARPPU. Our enriched content offerings and enhanced member privileges, such as QQ Music introducing AUDIO 3D 2.0 and Kugou Music rolling out Viper Ultra Sound, have made our products more attractive and improved user stickiness. And our SVIP membership program is our strategic focus operationally and will lead to ARPPU improvement in the long run.

Advertising revenues also had strong year-over-year growth, primarily due to the growth in ad-supported advertising. We provided more attractive interactive features to our users, which helped improving entrance rate for our ad-supported advertising. Promotions for the 618 mid-year shopping festival also contributed to increased advertising revenues. Moreover, our interactive rewards program opened new avenues for commercialization in advertising for our users. Additionally, we continued to innovate and diversify our product offerings and advertising formats, while deepening the integration of brand sponsorships with our offline performances.

Social entertainment services and other revenues were RMB 1.7 billion, down by 43% year-over-year. We will continuously monitor market conditions, the competitive

landscape, regulatory environment, and our product features for social entertainment services.

Our gross margin for Q2 reached 42%, marking an increase of 7.7 percentage points year-over-year, due to the following factors. First, the expansion in paying user base and improved monthly ARPPU for online music as well as increased advertising revenues had favorable impact on our gross margin. Second, we have been focused on ROC as a key metric to manage our costs. Third, the ramping up of our own content continued to help improve our gross margin. Lastly, we have enhanced monetization of WeSing membership and advertising within social entertainment, which positively impacted our gross margin. All above factors have collectively enabled us to move to a healthier margin.

Moving on to operating expenses, in the second quarter of 2024, they amounted to RMB 1.1 billion, representing 16% of our total revenues, compared with 17.2% in the same period of last year.

Selling and marketing expenses were RMB210 million, and remained relatively stable comparing with same period of last year. We continue to maintain ROI focused approach for promotion expenses and will continue to invest in areas such as online music with a long-term growth perspective, as well as in content promotions.

General and administrative expenses were RMB938 million, down by 10% year-over-year, primarily driven by lower employee-related expenses.

Our effective tax rate for Q2 2024 was 19.4%, compared to 12.2% in the same period of 2023. This increase was primarily attributed to the accrual of withholding tax of RMB111 million related to earnings to be remitted by our PRC subsidiaries to offshore entities. Additionally, changes in preferential tax rates for certain entities also impacted our effective tax rate.

For Q2 2024, our net profit and net profit attributable to equity holders of the Company were RMB1.8 billion and RMB1.7 billion, respectively. Non-IFRS net profit and non-IFRS net profit attributable to equity holders of the Company were RMB2 billion and RMB1.9 billion, respectively.

Our diluted earnings per ADS reached a record high this quarter at RMB1.07, up 30% year-over-year. Non-IFRS diluted earnings per ADS increased to RMB1.19, up 23% year-over-year. These results underscored our robust financial performance, enhanced operating efficiency, and the beneficial impact of our share repurchase program.

As discussed during Q1 2024's earnings call, we declared the annual cash dividend for the fiscal year 2023 in May, and have made a payment of US\$212 million in June 2024.

As of June 30, 2024, our combined balances of cash, cash equivalents, term deposits and short-term investment were RMB35 billion, as compared with RMB34.2 billion as of March 31, 2024. This combined balance was also affected by changes in the exchange

rate of the RMB to USD at different balance sheet dates.

Looking forward, we will continue to focus on high quality growth in our music business, such as expanding SVIP memberships, as well as operating efficiency improvement. We will continue to invest in high-quality content, original content production, as well as innovative technologies to further improve user engagement and enhance user experience.

This concludes our prepared remarks. We are now ready to take your questions.

Millicent:

Thanks, Shirley.

Millicent:

Thank you. Thank you everyone for joining us today. If you have any further questions, please feel free to contact our IR team. And this concludes today's call, and thank you so much again and look forward to speaking to you next quarter.