

NetDragon (0777.HK) 2021 Interim Results Conference Call and Webcast

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NetDragon's Management Team

Dr. Simon Leung, Group Vice Chairman and Executive Director

Mr. Ben Yam, Group CFO

Mr. Lin Chen, Group Senior Vice President

Mr. Vin Riera, CEO of Promethean

Moderator:

Dear friends. Good morning. Thank you for joining NetDragon Websoft Holdings Limited today for our 2021 interim results presentation.

Our presentation PPT will be broadcast on the live-streaming platform. The PPT is also available for download on our company website at www.nd.com.cn under the investor relations pack in IR webcast section.

Before the start of our presentation, please allow me to introduce the management who are joining us today.

Dr. Simon Leung, Group Vice Chairman and Executive Director.

Mr. Ben Yam, Group CFO.

Mr. Lin Chen, Group Senior VP.

Mr. Vin Riera, CEO of Promethean.

Now let's pass our time to Dr. Simon Leung to host our presentation today.

Simon Leung:

Well, thank you. Good morning. You can see my background is actually in Hong Kong. I hope you guys get to the office safely. Well thank you for joining our call this morning. I wish we can meet you face to face but with COVID, this is actually where we have to make do. I have not travelled for the last year and a half, which is very unusual. Happy to report. We have a very, very strong finish for our first half. It's all set on our businesses, gaming and education. We look at all the metrics that we track, revenue is up, margin is up, cash is up and profit is up. So, the team will take you through all this. Let's take a look at our performance in the first half. Before

we do that, let me introduce the team very quickly one more time. So I will talk about all the highlights. A lot of people are having conversations and questions about China's new direction in terms of education and how it impacts education business. I'll talk through that very quickly. Vin will talk through the education business. Vin actually in addition to Promethean, has also taken over the Edmodo responsibility. We see the market actually moving towards blended solutions. It is the right time to combine Edmodo and Promethean so he is not only the CEO of Promethean, he is actually the CEO of the combined education business. Lin Chen will talk about the gaming business, and then Ben will talk about the financials. He will talk about the shareholder value enhancement program that we're going to be rolling out in the second half, which is the most exciting part coming on the back of our very strong performance. We call it capital management.

Okay, let's move on to slide number four. We've talked about it in the press release, and I'll just repeat a couple of the numbers. 19% year-over-year combined revenue growth, which is quite impressive. EBITDA is up quite a bit, 42%. Both operating profit and net profit are up. Net profit is up 28%. If you take a look at operating profit, it is actually up 59%. Slide number five, it's really a quick highlight, the team will go through it. In gaming, we are back to double digit growth, which is very good in the current environment. Another highlight is our overseas gaming revenue growth, which is 29%. In terms of education, it continued to be very strong. We've improved our bottom line. And amid the COVID challenges, logistics and freight are actually a very big challenge for us, but I am very happy to report that the team has done a very good job in managing the cost for freight and logistics. Quick word on our country strategy. We continue the rollout. We're picking up steam, continue to work on countries like Egypt. To add to it, we just signed an MOU with Thailand. We're going to pilot English learning smart classroom. Once that's completed, we're going to roll it out to the rest of the country. I just hope COVID is not going to be there to rain on our parade. Last but not least is something that I'm very happy and excited about. We're going to be announcing a bunch of activities that're going to unlock the value of NetDragon. The reason we can do that is on the back of many quarters of strong financial performance.

Ok, turning the focus to China a little bit. The market got very affected because of the change of education regulations. The overall market got impacted. But I want to assure you guys that actually we are quite different from some other companies. So I'm going to spend a couple minutes taking you through it and you can have more questions about it. We can go to slide number seven. The gist of this slide is to tell you the new policy actually doesn't affect our business because we are not in the after-school tutoring business. As a matter of fact, because of the change, a lot more focus is put into the classrooms, putting the right infrastructure in the classrooms, developing the teachers, which in turn will benefit the students. That is our strategy, which is the blended learning solutions. So the future of China education actually works very well with our strategy, which we've been pushing since day 1 and we have never changed. So in a way, the market is coming to us in the rest of the world because of COVID, and in China because of all the new regulation, and also COVID I have to say.

So let's go to page eight, because of that, we are very clear in what we're going to be doing in China. We have experimented quite a number of products and strategy. With the change of the regulations, it is very clear to us our future belongs to the classroom and belongs to well I guess, 2G or 2B business. So what we're going to do is that we're going to be focusing on a couple of strategies. As a result, we're going to be rightsizing our organization in China. With the rightsizing, we're going to save some money, which will go to the bottom line. I think that's very good for the investors. So with that, I am going to turn it over to Vin Riera, and he's going to take you through both of the Promethean business and Edmodo business.

Vin Riera:

Great. Thank you. Good morning, everybody. I want to start by talking about the strong market demand that has been driven by COVID. COVID pushed the education segment into finding solutions for blended learning, and that really led to an inelastic demand for our education products within our portfolio. We see that the interactive classroom technology is a core part of blended learning. During last 18 months, schools all over the globe bought more one-to-one devices. They bought more software programs and they looked at different ways of educating students in a blended learning environment. And our interactive front-of-class technology is at the absolute core of that. The demand for higher-end technologies to support the blended learning solutions is evident in the results. And I'll share that with you shortly. There's also a huge opportunity because there's a relatively low penetration of interactive devices globally. About one third of the classrooms have interactive displays on a global basis. That still means that we have significant opportunity, not only to continue to replace legacy technologies in more mature markets, but also continue to go after the emerging markets, and win businesses and gain new share. The last point on the overall strong market demand is that this is the new normal of learning. The solutions that we're seeing being put in place around the globe are not short-term fixes for the next year or two. It's considered the new normal and how schools are going to continue to operate not only from a face-to-face classroom setting, but also how they're going to operate in a blended learning environment. So we have a very strong belief that blended learning is driving the demand today, it's also the future of our business. From a market growth outlook, you'll see that the market grew between 2020 to 2021 is estimated to grow 20%. We're obviously participating in that growth and we also see growth continuing on to 2022. Next slide please.

So some of the drivers that are helping in with the growth of Promethean is our brand equity. I talked about this on every earnings call. Promethean has expanded in the education segment for over 20 years, we're well known, we are well-respected with a following of teachers and administrators and IT professionals around the globe and that brand equity really helps open doors for us. The second thing is that we have a premium product, but we price it and configure it specifically for education. There're so many different use cases for interactive devices. We chose to focus our development and R&D efforts on front-of-classroom technologies and use cases and how they're used within schools, or even within ministries of education in some of the emerging markets. We have a unique blended learning focus. We're very conscious of how

our products are used in the classroom and how they are used in traditional ways, where you have students in front of you, but also where you need to connect cameras, where you have to run different types of software in order to engage the students remotely. And then the final point is we're able to cover the territory that we're able to cover because of the great relationship we have with our channel around the globe. We're always building out and looking for white spaces that we could better cover with deeper new channel relationships and make sure that as opportunities present themselves, that we're there and we're competing for those opportunities. We take our relationship with our channel very seriously, and we invest in our channel to ensure that not only that we're successful, but they're also successful as well. And the result of this is we've been able to expand our market share. So globally, excluding China, in the second half of 2020, we are at 21%, first half of 2021, we at 24.5%. And then in our top three markets, which are the biggest markets that we have outside of our emerging markets, we gained share in the US, UK and Germany, respectively. Next slide please.

So we have had both significant revenue and volume growth. Revenue growth on a half-over-half basis was 21%, on a year-over-year basis, 35.6% (in USD). The same thing goes for volume growth. The market grew 6% where Promethean grew 21.5%. So we're seeing growth both in our number of units within the market and also top-line revenue. Next slide please.

And we continue to focus on operational excellence. Simon talked about this a little bit during his first set of comments, but the supply chain and logistics have been extremely challenging for all businesses. We've put a lot of focus on how we can continue to operate efficiently, operate cost effectively, and make sure that we have products in our channel and with our distributors to be installed in schools. The first thing that you'll see here is that from a product mix standpoint, our ASP went up year-over-year. There're a couple of factors for that. The first is with blended learning solutions, schools are really looking to put in our higher end product. It's a faster product. It has more computing capability. It works effortlessly in a blended learning environment. It's not that our lower end product doesn't work, but in a blended learning solution, the higher end product certainly works effortlessly. It's also worth mentioning that there are significant funding streams in place globally that are fueling EdTech spending, and when there's money to spend, schools are looking for solutions that are sustainable solutions, not only for this year, but for the next few years. Gross margin went up, and again, back to our discipline on costs, we're making sure that we're planning appropriately for inventory and managing our supply chain and logistics down to every last penny to make sure that we're extracting the value that we need to out of that and passing that along to our customers as well. And then from an operation efficiency standpoint, OPEX as a percent of revenue, went down from 27.2% to 23.6%. And with that said, I'm going to turn it over to Lin to talk about gaming.

Lin Chen:

Dear investors, nice to meet you. I'm Lin Chen, I'm happy to share with you our gaming performance for the first half of 2021.

Next page. To begin with, our gaming business revenue grew by 12% and overseas gaming revenue by 29%. Our flagship IP *Eudemons* has achieved steady growth for more than 7 years. These numbers are the result of our deep understanding of the gaming market and contents. You can see how we produced high-quality gaming contents and our continued efforts in user community operations. These reflect NetDragon's long-time investment in the gaming industry and understanding about the market. In my opinion, companies must find their niche and core competencies to do well in the current gaming market. Our IPs and core users are our major competencies and economic moat. Leveraging on these strengths, we will continue to enhance our R&D capabilities and will see better opportunities for our gaming business in the future, especially in the area of game content development for MMO, a genre that we are good at. We will also leverage our understanding of the market and users to explore new gaming genres. We firmly believe that NetDragon's gaming business will continue to grow in the foreseeable future.

Next page, a quick review of our gaming business. NetDragon mainly focuses on MMO and MOBA games. We've also been exploring the casual game genre. MMO is actually a major game genre with great long-term potential, and we have accumulated a lot of experience in this genre on how to refine its core gameplay and launch contents over a long period of time. We continue to invest in the *Eudemons* IP, acquiring valuable know-how that can also be deployed into other games, including some new genres we're exploring. All of these ensure that our gaming business will maintain sustainable and healthy development.

Next page, I will introduce our most important IP *Eudemons*. Revenue of the *Eudemons* IP was up 14% year-on-year in the first half of the year. Another positive development is a 6% increase in the MAU of the overall IP. This proves that our growth has been stable and sustainable, as the increase in revenue comes with an increase in long-term players as well. This is especially evident in the mobile titles, where MAU and DAU were up by 68% and 34% year-on-year respectively. It is reasonable to conclude that our enhanced content quality is capable of attracting users to the game and retaining them. Having more user access in both PC and mobile allows us to better keep core users within our IP pool. As we rejuvenate some of our IP series products, we will continue to expand the user base in the whole IP.

Next page, again, this is the result of our profound understanding of the MMO genre and its contents. *Eudemons'* sustained revenue growth demonstrates the excellent quality and our extensive know-how in game contents production, which includes rejuvenating gaming contents, incorporating and integrating cultural elements, IP crossovers, maintaining brand equity and upgrading graphics. We will introduce such contents and keep users engaged with the right timing. These contents not only rejuvenate the IP, but also increase brand value. In terms of monetization, we can have a better rhythm when selling to our core paying users.

Next page, "*Eudemons Youth Tour*" is the key theme for the anniversary celebration event this year. It has been well-received by new and old users, proving that *Eudemons* is an evergreen

IP capable of constantly rejuvenating itself, and the spirits and experiences are also well accepted by our users.

Next page, it's about incorporating Chinese culture elements. In my opinion, this is highly favored by users in the gaming market - especially those from Mainland China. Based on the Chinese culture favored by users, we have also combined fantasy and pop culture elements, which have been well received by our users. Beside *Eudemons*, we're seeing the same trend in *Heroes Evolved* as well. In the current gaming market, there's already a clear trend about users' content preference. As long as we can produce good contents that suit their preference, they are willing to pay for them. This also enables us to continue producing contents.

Next slide. This slide shows how we highlight the nature of our IPs as we continue to do IP crossovers. *Eudemons* is a passionate IP, and when choosing another IP for a crossover, we would carefully consider how the partnership will highlight the nature of our IP and enhance user experience. This particular IP crossover has been very successful, proving that those passionate IPs have great compatibility with *Eudemons* and that we've received high recognition from our IP users. This is a key element to ensure a game's sustained operation in the long run.

Next page, for *Eudemons*, in the past both the PC and mobile games of *Eudemons* were powered by our self-developed 2.5D engine. The Company has strong capabilities in developing game engines. We have now transformed the game engine, allowing it to support both 2.5D and 3D graphics. Our continued graphics upgrades would improve user experience. For older users, there will be a transition period for them. For newer users, 3D is a format that they will be able to easily accept. We'll be able to offer users an improved, updated and more immersive gaming experience with these enhanced 3D graphics.

This is our *Conquer* IP. The MMO elements of the *Conquer* IP are based on our understanding of this gaming genre and also some successful experiences from *Eudemons*. As we continue to launch new contents, we can maintain loyalty and revenue from long-term users. At the same time, the *Conquer* IP has been doing relatively well overseas. Its overseas revenue has exceeded revenue from the domestic market. Based on the successful experiences accumulated in Egypt and other countries, we have had "zero to one" breakthrough in some new countries. I believe that with this breakthrough, we can also see higher overseas revenue growth in the second half of this year and next year.

Next page, the successful experience in Egypt. As part of our group's global strategy, with *Neopets* or some other games, we can reach more users through the *Conquer* IP platform. We can also promote other high-quality games to more players based on the existing channels and user base.

Next page, this is our *Heroes Evolved* IP. Although the overall revenue of the *Heroes Evolved*

IP has dropped, we are happy to see that our *Heroes Evolved* PC version achieved year-over-year and half-over-half revenue growth. In this process, we could also see that the innovative integration of MMO and MOBA, two gaming genres that we are good at, has yielded some very good results. Though the number of users has decreased, the spending power of the users have increased. We have also found a way to convert MOBA users to high-paying MMO users. This has done relatively well in the PC version and driven the rebound in PC revenue. We will also apply these experiences to the pocket version.

Next page, you can see our pocket version. As our IP crossovers and Chinese culture elements have becoming more and more popular among players, revenue of the pocket version has basically been steady since June compared to the same period last year. We have already started transferring some of the good practices to our pocket version. At the same time, there are greater opportunities in the mobile version. We always think that understanding players and producing high-quality contents are at the core of a gaming company's research and development process. We believe if we can bring these know-hows to the mobile version, we will see good performance in the second half of this year.

Next page is about our new games. As mentioned earlier, the market is constantly changing. Players' pursuit of content quality and aesthetics are also constantly changing. Here are "*Eudemons Mobile 2*" and "*Under Oath*", which we have been working with Season and Bilibili respectively to finetune the contents. We believe that the market is changing and we can only gain market recognition by launching high-quality contents. Furthermore, I think an IP like *Neopets* also has good potential. It's the group's first globally developed project. The team in Fuzhou and the team in the US have worked together closely to develop better games that suit the international market. This will bring us a lot of opportunities too.

Next page, we all know that this year there has been a lot of pressure from the regulations. But on our side, we have been proactively responding to these changes. Firstly, we can see that the whole group in the past has been proactive in protecting minor players. We have been proactive in understanding the policies and improving our work in this aspect. Gaming revenue from the minor players actually contributes less than 1% of the entire group's (gaming) revenue. At the same time, we are on the right track in terms of integrating Chinese culture elements into our games and proactive collaboration with the government in launching contents about the cultural and creative industry. After all, gaming is part of the creative and cultural industry. We have some crossovers with the Forbidden City and Intangible Cultural Heritage, so our contents are moving towards the right or appropriate direction.

Also, we can see that there's excellent growth in our overseas gaming business, which makes our overall gaming revenue composition more stable and healthier.

Next page, in the first half of this year, we continued the momentum from the second half of last year and achieved better development. In the second half of this year, we have high

expectations on our existing IPs as they have been stable. We expect that they can continue to develop. At the same time, we have found the direction and know-hows to revive the revenue of *Heroes Evolved*. As we launch our new games, I believe that in the second half of this year, our gaming revenue will see a healthier and more stable growth. That's all from me. Thank you all.

Ben Yam:

Hello everyone, this is Ben and let's get right into our financials for the first half. So first of all, our income statement, our revenue growth was close to 19%, with gaming and education, both performing exceptionally well. Our gaming revenue growth continued from the momentum we saw in the second half of last year, with a 12% growth. Our education business recorded one of our strongest performances in recent years, with 23.7% growth on the back of two main drivers, one is overall market growth and the second one is the fact that we've been increasing our market share, as Vin pointed out earlier. We are also seeing benefits from the operating leverage as we continue to scale our top line while we manage our businesses with cost discipline. So, as you can see here, all of our SG&A expenses as a percentage of revenue have all gone down compared to prior year. And as a result, we're seeing 28% increase in net profits, 42% increase in EBITDA, and 26% increase in non-GAAP profits. And in the meantime, we continue to maintain a very strong financial position as our net cash amounts to over RMB4 billion. Next slide please.

Onto the segmental financials, first on the education business, our overall gross margin increased by 5.5 percentage points. And that's largely driven by Promethean's gross margin enhancement. It's also worth to point that about our core segmental loss for the education business continued to trend down as I guided earlier, as you can see going from RMB377 million last year to RMB266 million and going into the second half, we do expect the education loss to continue to narrow. Onto the gaming business, again, we saw double digit growth in terms of both top line and bottom line on the back of the relatively stable operating expenses. Next slide please.

So the next part of this presentation is shareholder value enhancement, and we're very excited to be announcing these measures, and the goal here is really, we're aiming to initiate these new capital measures to maximize capital return to our shareholders while allowing us to continue to invest in the future. Next slide.

First to tee it up, NetDragon has been consistently growing our profitability and also our cash flow in the past several years, as many investors would know who have followed us for many years. And, in the meantime, we've also been generating a growing free cash flow, as you can see here. So in 2020, our free cash flow was close to RMB1 billion and in the coming years we

are fully confident that our free cash flow will continue to grow. Next slide.

As we increased our earnings and free cash flow, in the past several years, we've also been consistently increasing our cash return to shareholders via dividends, and also share buyback. In 2020, we returned a total of 355 million in terms of Hong Kong dollars to our shareholders, which increased by over 50% compared to 2019, and also represented 37% of our net earnings. Next slide.

To break down cash returns further, first, we can talk about dividends as you can see, we've been declaring increasing dividends in the past several years. We are also pleased to say that we're going to increase our interim dividends by 60% to HKD 40 cents per share. Next slide.

In terms of the stock buyback, our board has authorized a committed stock repurchase program whereby we expect to buy back our stocks worth up to 300 million US dollars over the next three years. And this really follows through on our long-term commitment to maximize value for shareholders. We believe that given the level of our stock price at the moment and the fact that we've been consistently growing our business, net profits and cash flow in the past many years, this is a very optimal timing to initiate a stock buyback program of this scale. On top of that, our decision to commit to this stock buyback program and also increasing our cash dividends, really underscore our confidence in the long-term business outlook and also our future cash generation abilities. So we're going to implement this buyback program, while maintaining a very strong balance sheet and also liquidity profile. And we also expect that we're going to return in the next three years, a substantial portion of our free cash flow through a combination of this stock buyback and also dividends. And again, I would like to emphasize that, while we implement this program, we're going to continue to maintain a very strong net cash position. As at the end of first half, our net cash is over RMB 4 billion, and that will enable us to capitalize on strategic and also acquisition opportunities going forward. And with that, I'm going to pass the stage back to Simon, who's going to take us over the outlook.

Simon Leung:

Thank you. Ben. I can see some of you are still looking at page 37, doing a lot of math between the 300 million and the 600 million. So, have fun on that one. So all kidding aside, I'm going to go on outlook. For the rest of the year, I think Lin Chen has done a really good job in articulating where we're going to grow our gaming business, especially with the new games to be launched in the second half. On the education side, I just have to say we are very confident that we're going to end the year on a very high note. One of the reasons is that, we have a really strong backlog going into the second half of the year on the back of the high growth in first half, very good news.

I talked about it in our last meeting here. We believe our stock is actually quite undervalued. So our focus is to unlock the value of the company. Ben talked about the buyback, talked about increasing the dividend. On the dividend side, we are basically very confident that we'll continue that trend on the back of our good performance and good cash generation. I think the big one is to unlock the value, is to think about the spinning off of our education business. So we've commenced that planning, actually we started the process already. We'll update you in due course. Again, at the end of day, we also execute our stock buyback plan in a very thoughtful way. This is another way to unlock the value and also return the value back to the shareholders in addition to our dividends. With that, thank you for your patience. I hope you are okay with our performance in the first half. Looking forward to talking to you about our second half in about six months' time. With that, I'm going to open up for Q&A. Thank you.

Moderator:

Thank you, Dr. Leung and management. Now it's time for our Q&A session. You're welcome to raise questions in two ways. First, if you would like to raise questions through the teleconferencing system, you may press star one on your phone keypad and our operator will put you through. Star one on your phone keypad. Second, if you would like to raise questions via our webcast platform, please click the question mark on the screen and type your question in the Q&A box.

We would like to welcome questions in both English and Chinese.

Let's welcome our first question.

So we have a question from the webcast platform. Can you please talk about the margin and the cashflow outlook of Promethean next year? Is there any room for further improvement on margin, and do you see inflation pressure on materials? Thank you.

Simon Leung:

Vin, you will take that?

Vin Riera:

We are not going to give any guidance for next year.

Okay. So, we still have issues in the supply chain that we're monitoring very closely. We're continually looking to source components to make sure that we have it ahead when we need it. There's still challenges in logistics. There's still challenges in the supply chain. I'm optimistic that I think it's going to get better, but I don't think it's going to get better in the near term. I think we're going to continue to work through some of the challenges and as we get into next year, I hope to be more forthcoming about some of the improvements that we're seeing when we talk again in six months, but between now and the next six months, I don't see major changes in

the supply chain.

Simon Leung:

Actually, I do like to add a comment on that one. So in terms of margin, the freight cost is only a part of it. The team is actually working very hard on not only on the freight charges, but also on the costs of the product. Also, it is actually on product mix and also on ASP. So again, if I can remind you on one of our charts that Vin showed, our ASP is up. Our gross margin is actually up. So it's a combination of things that increase gross margin. I can assure you, Vin and his team are laser focused on improving it. So is there room to improve? The answer is Yes, but there will be a lot of hard work, but I think the team can do it. What was the cash flow question again?

Moderator:

Yes. The cash flow question is the cash flow outlook and the margin outlook, and do we have further improvement on the margin and also would there be any inflation pressure on the materials?

Simon Leung:

I think we are missing the question big time. So we answered the Promethean question on margin and everything. Ben, you may answer the overall cash flow issue, because that's about both gaming and education. So Ben.

Ben Yam:

In terms of the cash flow, I can talk about cash flow from an overall perspective. So as you can see, cash flow throughout the year is related to kind of revenue growth, right? And as we look into the second half of this year, I think we'll be looking at a sequential revenue growth. We are very confident as Simon mentioned in the outlook, we're going to keep costs under control. So with that, we are very confident that we're going to be able to continue to increase our cash flow, both in terms of operating cash flow and also free cash flow in the second half of the year. So that would be the question of cash flow. Yes.

Moderator:

Thank you very much. So, allow me to introduce our way to raise questions again through the teleconferencing system. If you would like to raise your questions through the teleconferencing system, please press star one, star one, on your keypad.

So our next question also comes from our online platform. It's a question about our educational business. Management mentioned that the spinoff of our education business is on the way. So can you please share a little bit more about the detailed plan, timetable or any progress?

Simon Leung:

No, we commenced the planning and I had also said in my presentation, maybe I didn't make

it clear, we will update everybody in due course.

Moderator:

Okay. Thank you very much. Next we have a question from Feng Cuiting, TF Securities. Good morning, management, I would like to ask about the gaming segment. The first question is, what was the mix of revenue and user growth of the mobile and PC games under the company's flagship IP *Eudemons* in different markets for the first half of the year? The second question is what is the growth trend for Chinese and overseas markets? The third question is about *Conquer Online*. The game *Conquer Online* has got many opportunities around the world by adopting the model in Egypt. I would like to ask about the specific model and contents. Will the company replicate this model to other games in the future to extend its products life cycle? Thank you.

Ben Yam:

Let me first talk about the mix of mobile and PC games. Currently, we do not disclose the mix of mobile and PC games as many of our mobile games are compatible with PC and have PC-mobile cross platform version. Players can play our games on both PC and mobile phones. In this regard, we feel that currently the mix of our PC and mobile games may be quite ambiguous. Regarding the domestic and overseas revenue, we can share with you that our overseas revenue increased by 29% year-on-year in the first half of the year. We are also quite optimistic about the outlook.

I will pass over to Lin Chen for the other questions.

Lin Chen:

First, currently we base our development on our IPs. Taking the *Eudemons* IP as an example, we have established a lot of channels to reach users through launching new contents and our overall revenue growth was driven by the IP.

Second, I will talk about the model of *Conquer Online* in Egypt. *Conquer Online* is a first mover in Egypt. We are among the first batch of companies entering the Internet cafe systems in Egypt. *Conquer Online* is mainly operated on PC. With that, we've entered the nascent market in countries along "Belt and Road" like Egypt. After that, we've continued to expand through launching more contents and gameplay, as well as capitalizing on the transition from PC to mobile in Egypt. In fact, we can see that China's gaming industry is at a leading position in the global market. In particular, we see opportunities in the big genre of MMO amid the transition from PC to mobile. This involves early-stage opportunities in the mobile gaming market. *Conquer* is an IP that incorporates plenty of Chinese culture elements including some Chinese professions and contents, which makes it popular among overseas players. We are expanding our business from zero to one in some new countries. As we think that the game contents in each country should be localized, we will spend time on it. For now, we have achieved breakthroughs from zero to one. In the future, we hope to continue to implement these practices.

Moderator:

Thanks for your answers, Lin Chen.

Our next question is about our educational business. Our investor Okada would like to know about Egypt's business. When would the pop-up classroom be launched in big scale?

Simon Leung:

That's the only question?

Moderator:

Yes, that's the question.

Simon Leung:

So actually, we have done some pilot, unfortunately the COVID is not under control. So that is actually being put on hold at the moment, but there're still other activities going on. We're working with the Egyptian government. So the answer to your question is that we do not know at this point, but I can reassure you that as soon as COVID is under control in Egypt, they will come back and look at how to roll out the pop-up classrooms.

Moderator:

Thank you very much Simon. Our next question comes from Yang Linlin of GF Securities. GF Securities has a few questions. The first is that now the loss of the education business has narrowed and the expense ratio is under control, can management share their forecast on future profit and revenue trend? The second question is what will be the revenue size of the upcoming Thailand and Egypt projects? The third question is about the listing plan and progress of the education business, which has been asked just now. The fourth is the plan for launching new games including *Eudemons Mobile 2* and *Under Oath*.

Simon Leung:

Okay. I'm going to take the first two, and Lin Chen can talk about the third one.

Oh, sorry, in Mandarin, right? We will definitely go into the direction of profit making when we do business. So when you look at our overall trend, we are going in that direction from two aspects. In fact, I mentioned in my introduction just now. First, we are very confident in our future growth. Second, I also mentioned that we will make some efforts in reducing costs because we are clear about our direction after different attempts in the past several years. We will take some significant cost cutting measures. We are confident in going in that direction. However, since we are not going to give guidance here, we can't tell the specific timing. Same for Thailand and Egypt projects. We have relatively high expectations for these two markets. We will not indicate how large our projects will be but they will not be too small. In Egypt, we fully collaborate with them (the government). Apart from the pop-up classrooms and interactive panels, our Edmodo platform has also been deployed there. We have many other products

under discussion there so our project in Egypt is well-rounded. We hope we will follow the same direction in Thailand. All our country-level projects will go in that direction too.

Lin Chen:

Regarding the question of *Eudemons Mobile 2* and *Under Oath*, we are collaborating with Season for *Eudemons Mobile 2*. We have been finetuning and testing the game, and hope to launch it in the first half of 2022. *Under Oath* has gone through several rounds of testing on Bilibili already and we expect it will be officially launched for open-beta in the second half of this year.

Moderator:

Thank you, Simon. Thank you, Lin Chen. Please allow me to introduce how you can raise questions by the teleconferences system. If you would like to raise questions through our teleconferencing system, please press star one, star one.

Our next question comes from Eng Hou. With the fast growth in education business, would there be a chance that the overall gross profit margin may go down? Is the company comfortable with this, or what would the company do to improve the overall margin?

Simon Leung:

Honestly, I don't know how to answer that question. The gross margin in our case is actually a complicated issue because we have different businesses, but our track record shows you, we are doing very, very well in terms of gross margin. So again, I remind you to take a look at our slide, ASP up, cost is under control so our margin is up. The reason I laughed a little bit is because we have so many different businesses, but the overall trend of our business in education is actually moving towards a mix of software and hardware, and services. Because of that, I would expect the margin to improve because of the product mix, because typically in software and services, the margin is higher than the hardware. But that doesn't mean our hardware margin will go down. It is not our goal to drive the margin that way, I have to be very clear. Our goal is to improve our margin by operating in excellence and also, working on businesses that will give us a higher gross margin. Right, Vin?

Vin Riera:

Exactly. Well said.

Moderator:

The next question also comes from online platform. I just saw the Company mentioned that we will have a USD 300 million buyback plan. I guess the Company is very confident about the future. Can you tell us about the growth strategy in the future? And also, how to implement the buyback from the cash flow perspective?

Simon Leung:

Ben has already talked about cash flow. I guess he doesn't mind repeating it once. In terms of strategy, we made it very clear just now. Lin Chen spent a lot of time talking about the development of our games. Vin talked a lot about our development in education. I also mentioned that apart from our current businesses, we will develop more in software and services. So this is our strategy.

Another important thing is our country rollout projects. I also talked about their progress just now. You can go through them again, if not enough, we can talk about it another time. Ben has mentioned the issue of cash flow. Since we will make more money, cash flow will improve for sure. Right, Ben?

Ben Yam:

Right, there are two points here. One is that our current net cash has exceeded RMB 4 billion. This amount is very sufficient for us to capitalize on mergers and acquisitions or strategic opportunities in the future.

Second, we are very confident that we can continue to maintain our growth in profits and free cash flow in the future. In the past few years, all these metrics have been growing. In the past two decades, except for two or three years, these metrics have been growing. So based on this trend and track record in addition to our future outlook, including the decreasing loss in our education business, we have confidence in our future cash flow. As mentioned earlier, we hope that we can pay back a substantial portion of our free cash flow to our shareholders in the next few years through buyback and dividends. At the same time, we also have over RMB 4 billion of net cash.

Moderator:

Thank you. Next, we are taking a question from the conference call system. Operator, please proceed.

Operator:

The question is from Sun Mengqi of BOCOM.

Sun Mengqi, BOCOM:

Thank you, management. I have a question about the education business. Management mentioned before that Promethean has planned to enter the Chinese market this year. We mainly want to know about Promethean's current business development in the Chinese market and what strategies will it adopt to differentiate itself from its competitors? Also, what's your outlook on Promethean's development in the Chinese market this year, such as how many schools will it enter, shipment volume etc.?

Simon Leung:

We didn't mean that we are going to enter the Chinese market this year. We have been doing

business in China so we did not wait till this year to enter the Chinese market. Maybe I was unclear. What I mean is that the current changes in the regulations are very favorable for us to do bigger promotions in the country. I didn't mean we started entering the market this year. What makes us different from other companies is that we adopt blended learning. Our platform can be used not only in the classroom, but also at home and on-the-go. It is very different from other products. That's why I mentioned that Vin is not only the CEO of Promethean. He also integrates our hardware and software platforms. Edmodo is also managed by him. This is how our direction is like, combining hardware and software. As for the forecast, excuse us, we are not disclosing it here.

Moderator:

Thank you. The next question comes from Ken Chui of China Galaxy.

He would like to ask when will the monetization of Edmodo kick off? Is there any target on Edmodo's revenue scale in 2021 and 2022?

Simon Leung:

Do you want to take it, or you want me to take it? Go ahead.

Vin Riera:

Happy to take it. So we are in a couple of different areas on the monetization of Edmodo. The first is working on a product specific to ministries of education and countrywide rollouts. We've got a couple underway and a couple of discussions that are underway and we're building pipeline there. The other thing that we're looking to do is to monetize the community that we have and do so in a meaningful way. We have some product releases that are going to come out next year, that are going to help us monetize the business. So we have a couple of different initiatives underway to monetize that business and that community.

Simon Leung:

For the record, actually we are monetizing some of it and we will scale it next year. That's the message from Vin.

Moderator:

Thank you very much. Our next question comes from Panview. On the education business, what is the approximate gross margin headwind today given the US and China trade tariffs? While it's very difficult to forecast policy changes, is it possible that policy environment may improve in the future? So he's just curious what would be the policy in the future and if there is anything that would be beneficial to us.

Simon Leung:

For the question, I would need to look at the crystal ball. I will pass it on to Vin. He is probably better at reading the crystal ball than I am.

Vin Riera:

I don't know if I have a crystal ball but what I will say is that, relative to tariffs here in the US, we have seen our product being exempt from some of the highest tariff levels in the US and I view that as a very positive sign, and I see no signs about that changing, that being said I don't have insight into what future policies can be, but we certainly have not been harmed in any way, incrementally from any tariffs that we've had in the past.

Simon Leung:

But I would like to add, I look at it slightly differently on this one because if you look at our gross margin, it is actually improving. So that means Vin and his team are handling the tariff issue really well. If there are any changes in terms of getting rid of the tariffs, there's only upside for us. And so, and personally, I don't foresee an increase in tariffs. So I think we are in a pretty safe territory in terms of our cost.

Moderator:

Thank you very much. Due to the time limit, we would like to welcome our last two questions.

Our next question comes from Panview as well. How to think about our dividend policy going forward and its growth potential? Should investors expect the dividend to grow at a similar pace as our free cash flow?

Simon Leung:

We don't expect our dividend to go backwards. So let's do it this way. I mean we said it before it is our commitment to return a lot of the value back to shareholders and to do that, dividend is only one of the many ways, share buyback is another one. We can't commit to anything, but we don't foresee that going backwards.

Moderator:

Thank you very much. Our last question is from Kenneth of ICBCI.

We see that the revenue growth rate of the game IPs currently exceeds their MAU. Does this mean that our current strategy is mainly to drive ARPU growth for existing users? Do we have new strategies to achieve growth of new users in the future?

Lin Chen:

At last year's results presentation, we mentioned that during the pandemic last year, there was a relatively big increase in the number of users. But our revenue growth last year was not particularly high. MMO is a long-term game, and we will pursue user acquisition and monetization phase by phase. We generally carry out the two pursuits in turn, to maintain the healthy development of the MMO users' community. Although we don't see high user growth this year but there are several (noteworthy) phenomena. First, the increase in our mobile game

users is quite obvious, which means that the number of user growth in the PC market is shrinking. Our new user growth has definitely come from mobile games. We can also see that there has been a relatively high increase in the number of users of *Eudemons Online Pocket Version*.

As for the future, I think there are two important points. First, in terms of user acquisition, branding, content marketing and high-quality contents are important in attracting users. In terms of user acquisition, we will leverage our brand and content marketing to acquire more new users. In particular, data from *Eudemons Online Pocket Version* has proven this point. In addition, as high-quality contents roll out, ARPU will definitely increase. To a certain extent, this can prove that our content quality has been enhanced. In regard to ARPU, we think it needs to increase in a healthy manner. I think that an increase in ARPU brought about by the improvement of content quality is rather healthy. Thank you.

Moderator:

Now let's have Simon to wrap up the presentation for us.

Simon Leung:

First of all, thank you for your time this morning. I hope you are happy with our report. A couple of key points I like to remind everybody. The first one is when you look at our businesses, both gaming and education, we are a global business, we're not a China-alone business. We are really proud of our market position in China, but at the same time, I think it's good to have diversity. So I think the market is not rewarding us in terms of our global business. So we work very hard to change that perception. The other point I want to make is that if you look at the commitment that we made in unlocking the value and returning the value back to our shareholders between dividends, buyback, and also committing to spin off the education business, that means we are very confident in our business going forward. Our buyback program is not a one-year program. We are very clear that it is a three-year program while maintaining the right cash position to allow us to do something strategic. So that tells you a little bit about the confidence of the team in our businesses, both gaming and education going forward. With that, we'll continue to work very hard to make you guys happy. And then with that, thank you for your time. And, I'm sure you have more questions, feel free to come to us with more questions. Thank you so much.

Moderator:

Thank you very much Dr. Leung. Thank you, Ben, Lin Chen and Vin. And this successfully concludes our presentation today. Once again, I would like to thank you all for joining us. If you would like to communicate with the management further, please contact us for 1-on-1 meeting arrangement. Thank you. And we wish you all have a great day.